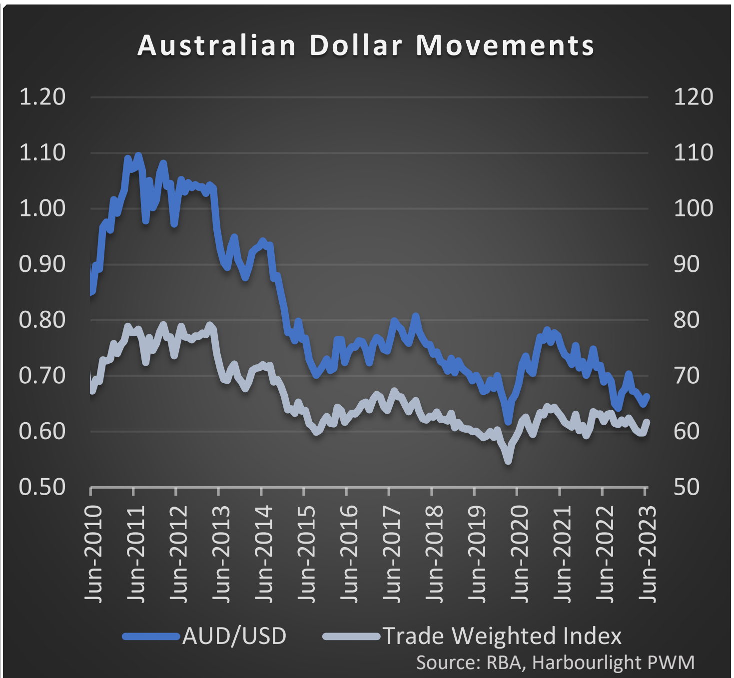
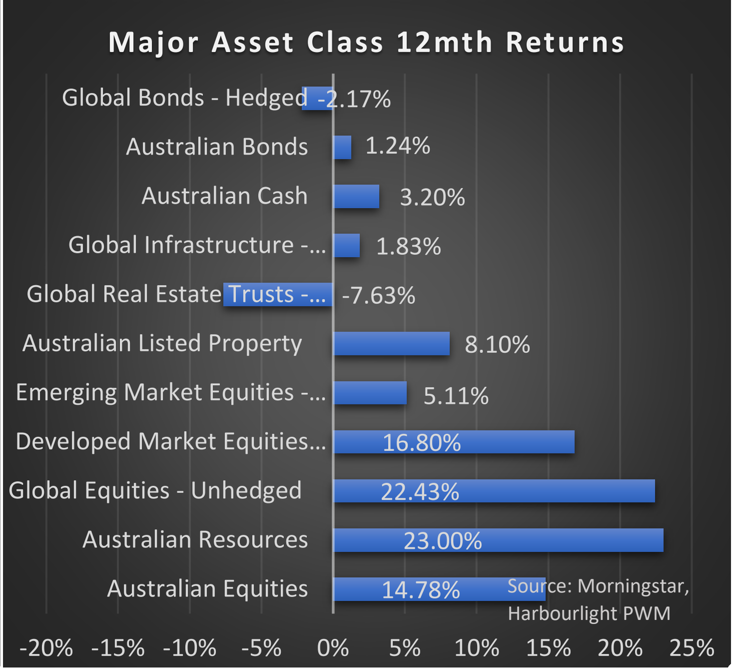
Harbourlight PWM Investment Review and Outlook.

A brief review of investment markets and broader factors affecting clients. **July 2023**

Executive Summary:

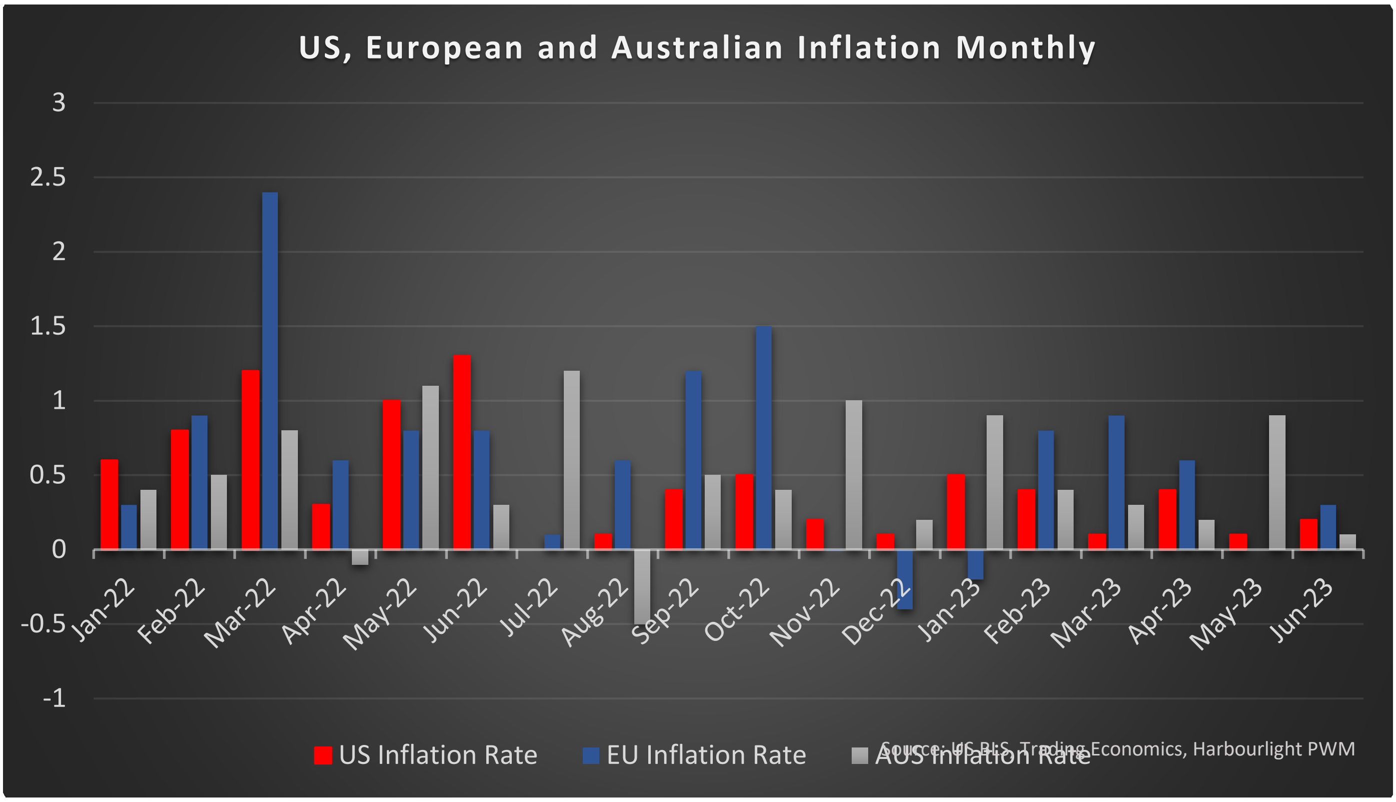
- The economic outlook continues to clear with most economies avoiding recession thus far and political tension seeming to ease. A soft landing and slow but mixed recovery look the most likely outcome.
- Inflation has been falling with shock months rolling off the series. Annualised inflation in the US now sits at 3% and in China near 0%.
- This has resulted in a solid recovery for portfolio performance off last year's lows (see chart below).
- Residential property price falls have eased with median house price growth across Australia showing a 10-year compound rate of return of 1-7% depending on state.
- Investment markets are pointing to a short-term increase in interest rates, followed by subsequent small rate cuts and an expectation of longer-term base rates ranging from 3.75 - 4.25%.
- Commodity prices are falling post the Covid fuelled boom. This will likely impact Australian corporate earnings and government tax takings – Coal has fallen over 60% in the last 12 months, Iron ore less so.
- The recent AUD weakening is the newest theme we are considering in client portfolios.
- This is combined with adding higher yield fixed income. Emerging market government bond and high yield bond portfolios now offer yields of between 7% and 10%.





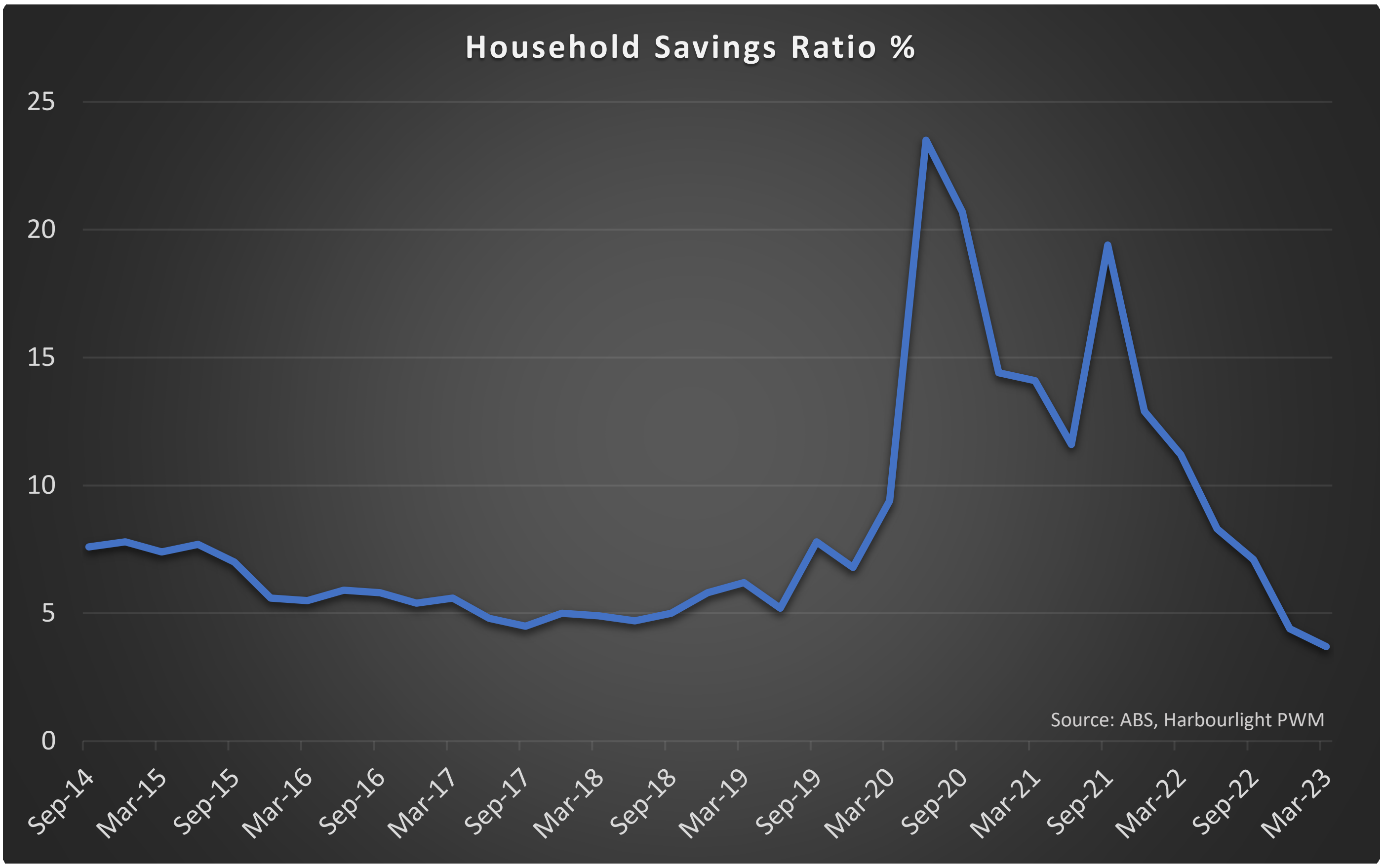
Economy and Financial Markets

Inflation is easing as interest rate rises work, supply chains are remapped and larger prints roll off the data series. In the latest readings, headline US 12-month inflation was 3% and China near 0%. Australia lags at 7% though is likely to follow over the next 12 months.

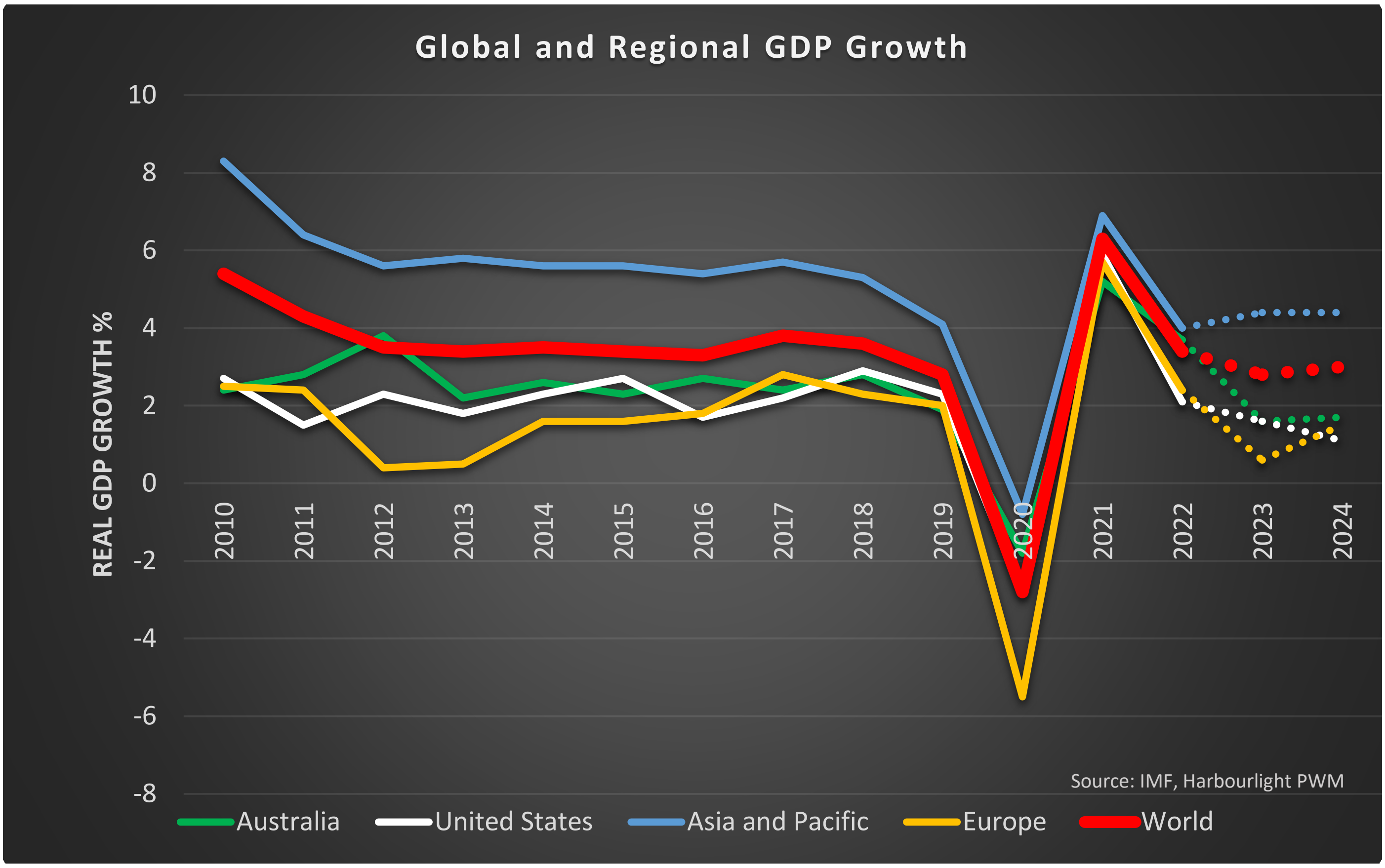


Wage growth is at its highest level in 10 years and combined with government tax takings, fiscal spending and corporate earnings could be a factor which causes higher levels of inflation to linger.

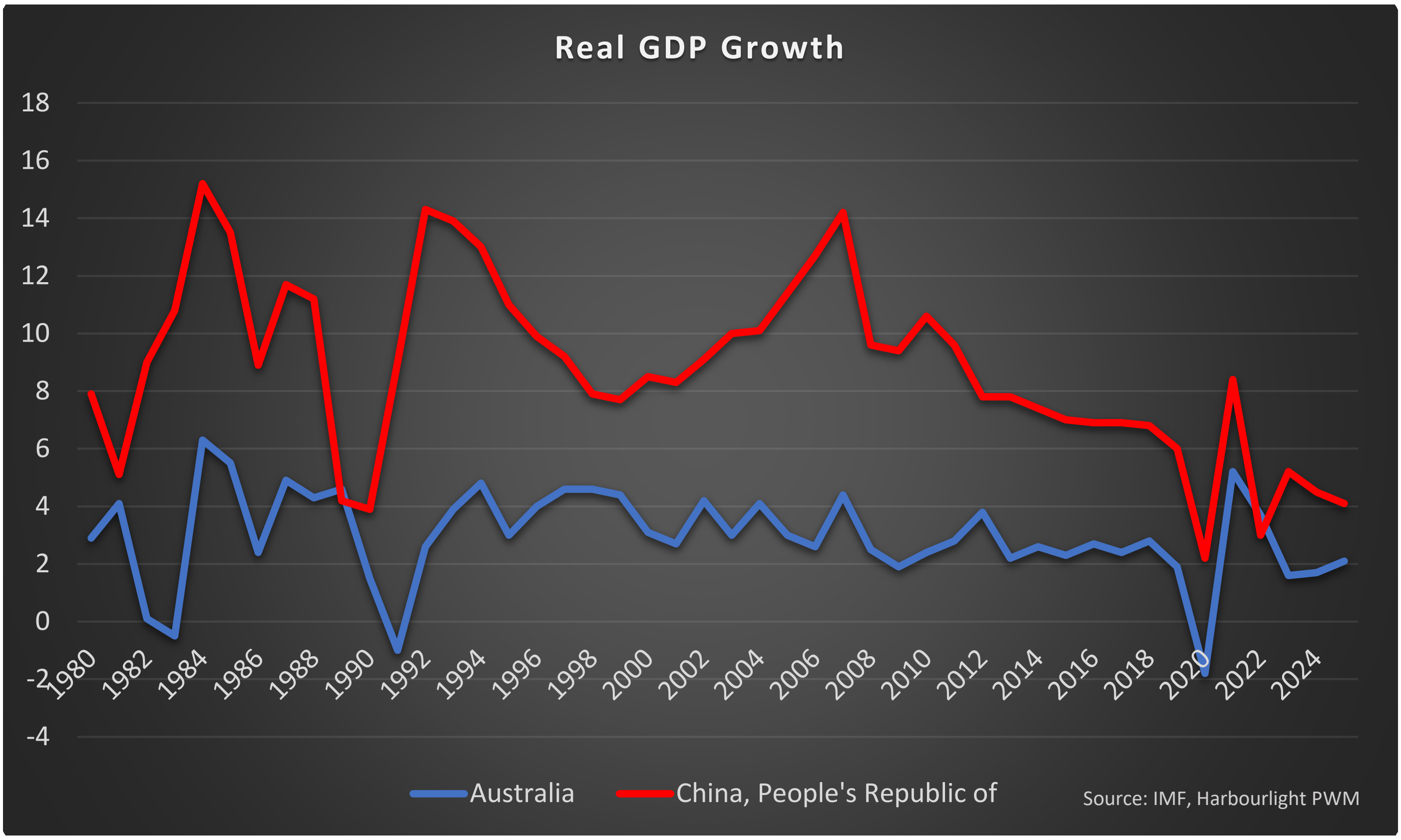
Household savings are at 10 year lows.



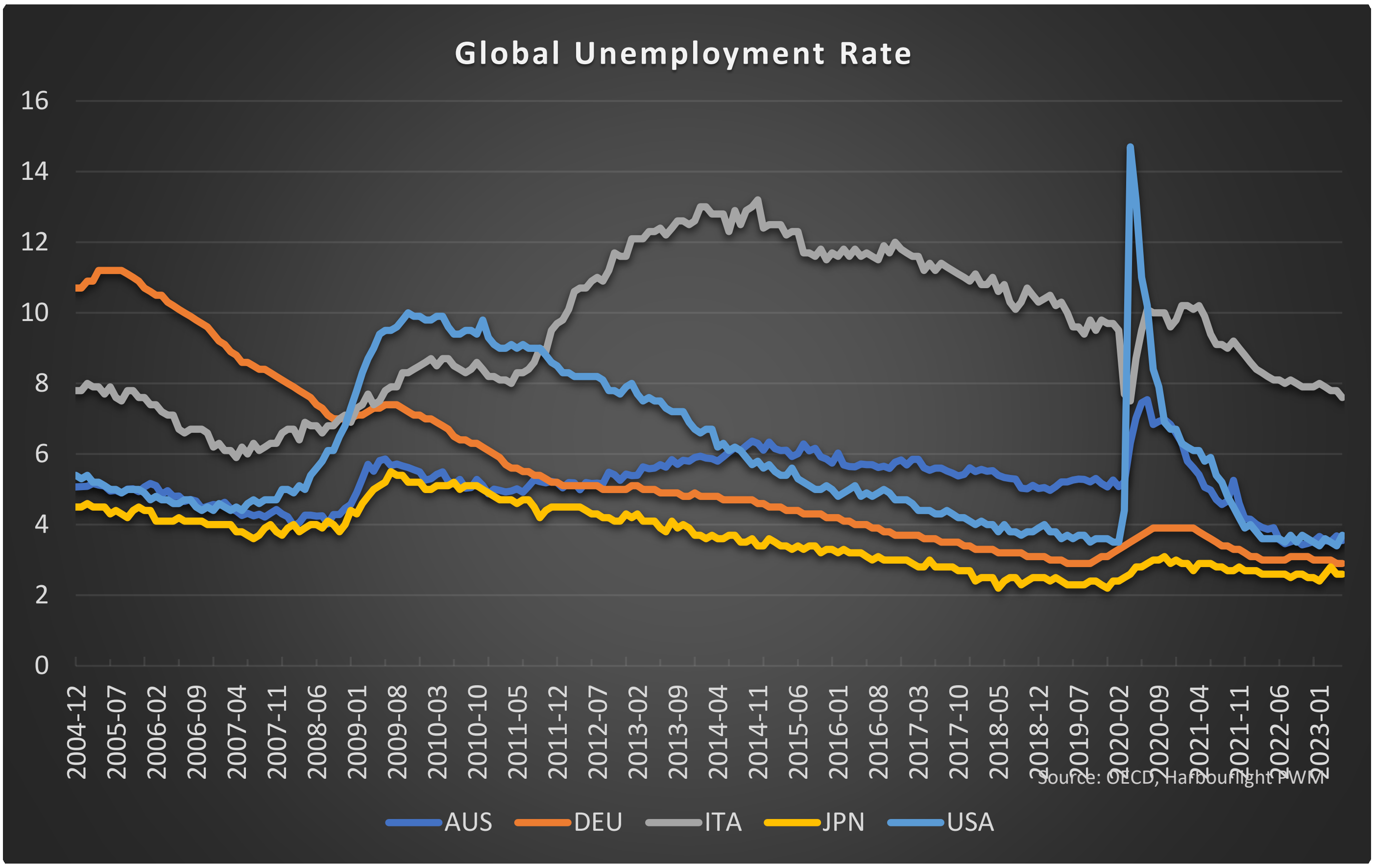
Global Growth is avoiding recession, whilst slowing is likely, so is a soft landing.



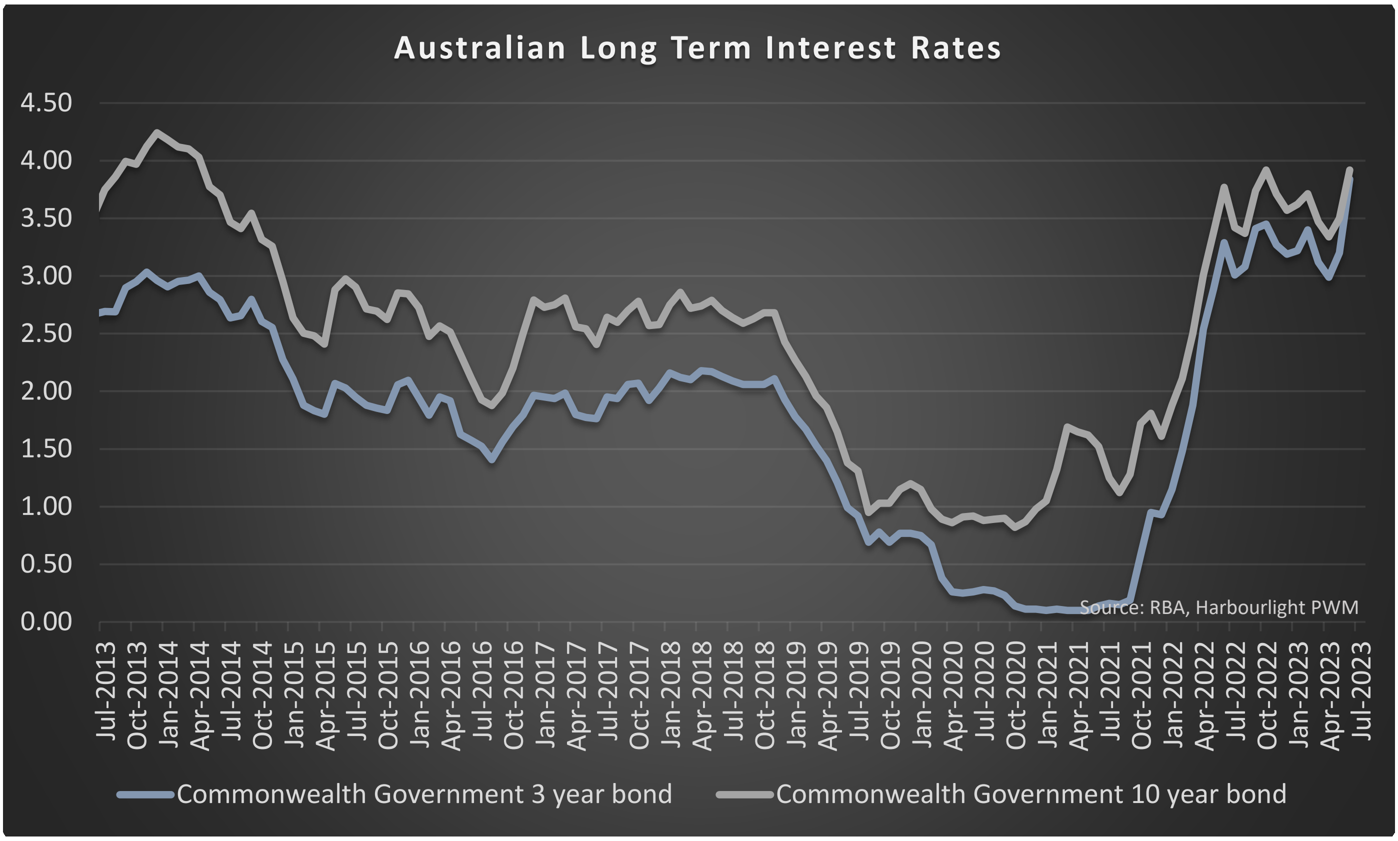
China (20% of global GDP) is showing higher but still relatively low growth post lockdown whilst experiencing low levels of inflation.



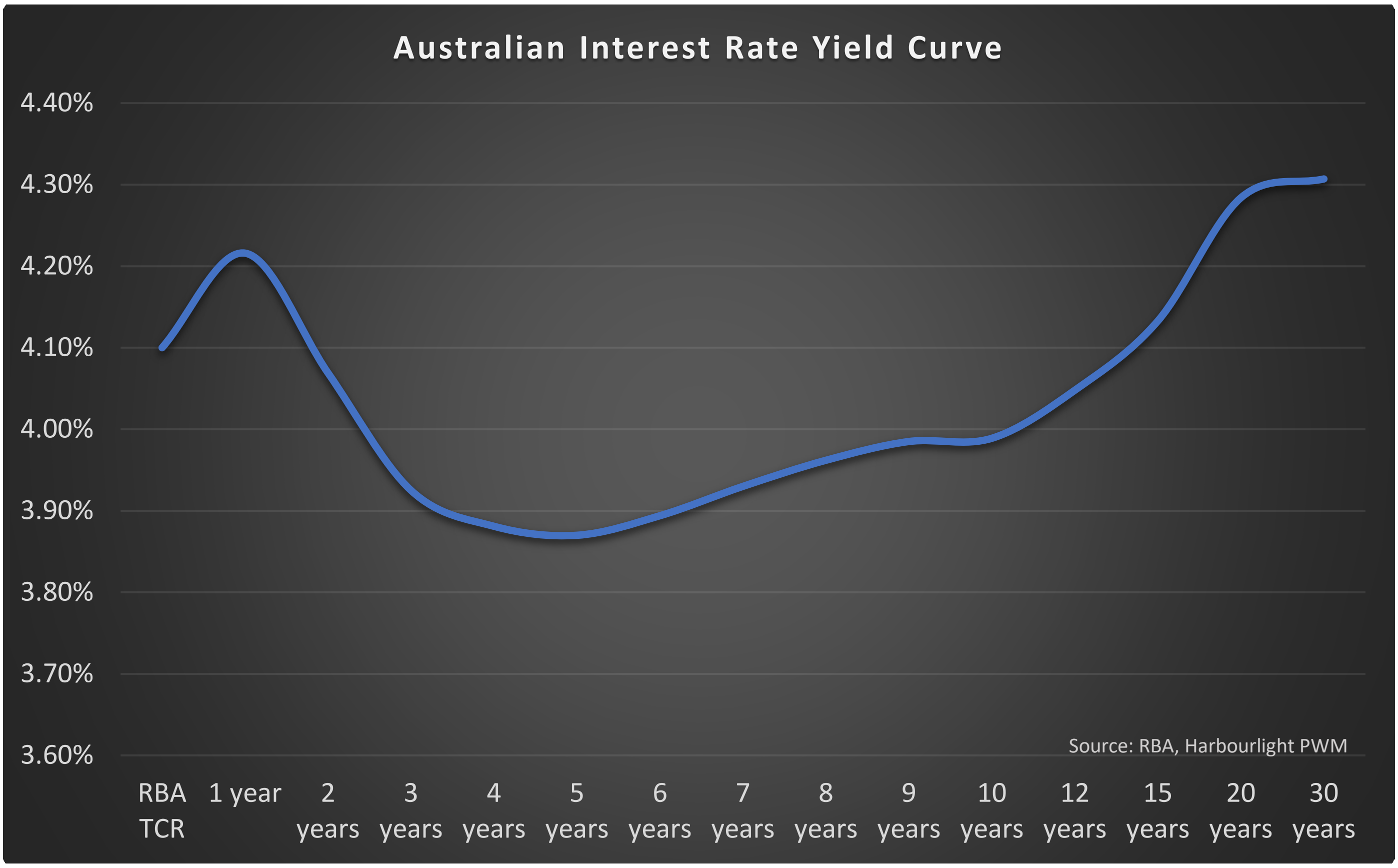
Employment remains strong globally.



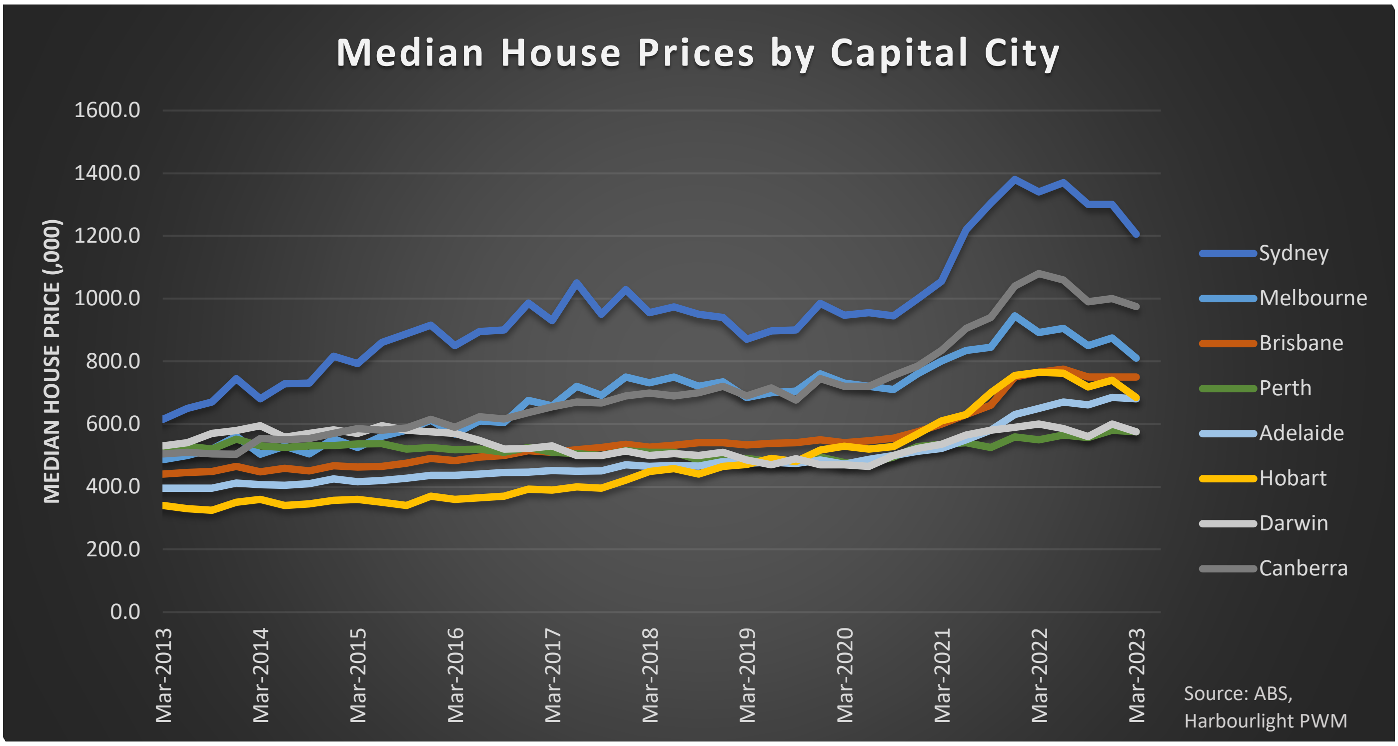
Interest rates have re-elevated to recent highs on wage growth & policy inflation fears.



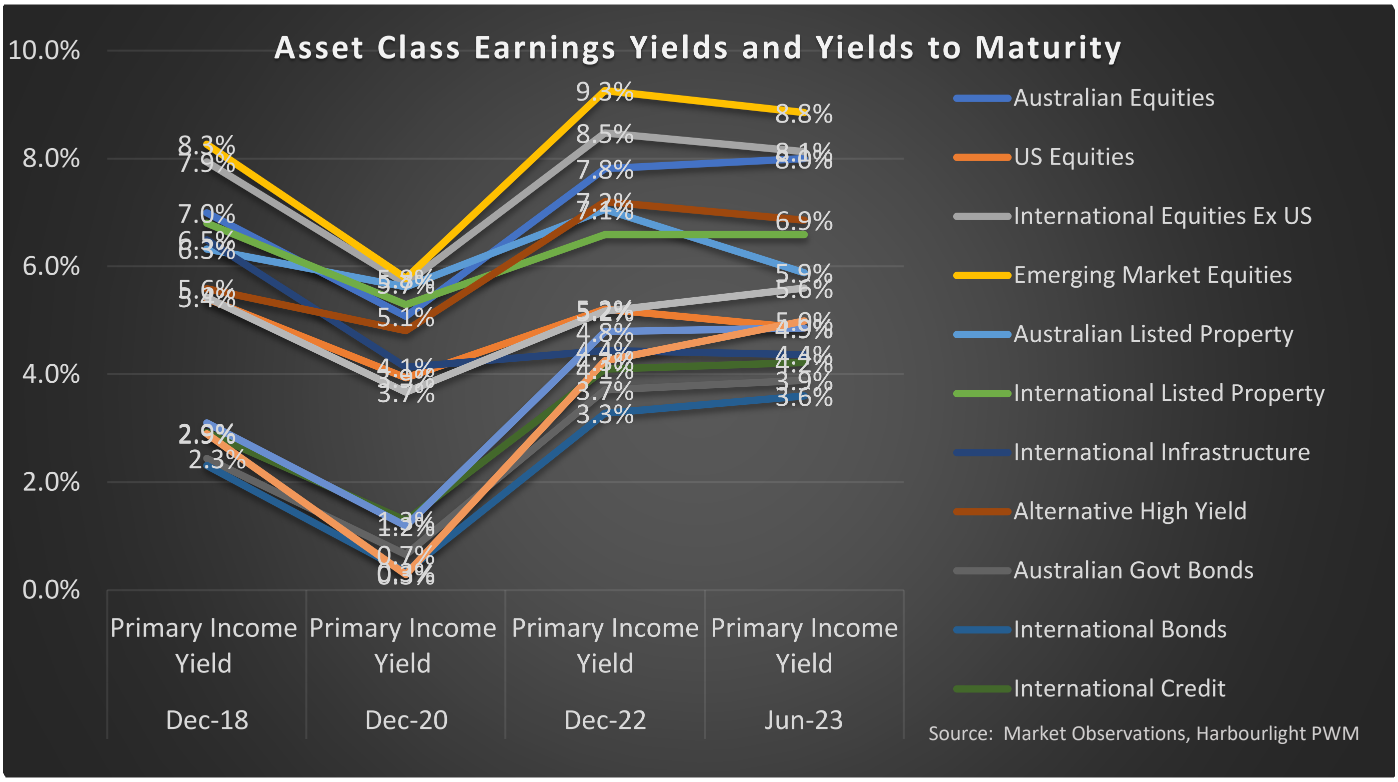
Bond markets imply that based on current information this is the longer term normal.



Median House Prices have fallen and seem to be stabilising, showing compounded annual returns (excluding rent and costs) of between 1 and 8% at state level with Perth & Darwin being the slowest and Sydney, Hobart and Canberra the fastest.



With higher interest rates & inflation, there is a natural push for investors to expect higher **growth asset class returns**, meaning either incomes from assets need to increase or prices fall to match. We expect both these factors will continue to play out in varying asset classes. Unlisted assets like direct property, infrastructure and private equity have generally not seen valuations fall to match higher return expectations. Unlisted property funds for example are broadly showing positive returns over the last 24 months vs listed assets which are some 20% lower.



Company earnings have held up well and some large cap **growth stocks** have bounced back well, but this hasn't been a market wide phenomenon.

Our views for the next 12 months.

With exception of the falling AUD and an increase in currency hedging on international assets, our view remains reasonably constant over the last six months.

We believe the inflation debate will continue, whilst the impact of wage increases and government spending are balanced to interest rate rises. Whilst we are never immune to sudden shocks, a soft landing and slow recovery seem to be the 70% probability outcome.

Asset prices excluding unlisted assets are generally fair. We anticipate seeing support for property and equity prices through inflation linked earnings and rental growth whilst return expectations find balance and fixed income portfolios offer far more attractive returns than 12 months ago.

We continue to prefer a neutral to more aggressive asset allocation for investment portfolios, with gradual implementation.

Some growth stocks still look to have potential to strengthen nicely as more uncertainty passes.

Other Regulative Matters

- Superannuation contribution caps are to remain at $27,500 for concessional contributions and $110,000 for non-concessional contributions for the 23-24 financial year.

- Temporary Covid-19 legislation relating to the halving of minimum pension payments ceased from the 1st July 2023.

- The transfer balance cap applying to commencing retirement income streams has increased to $1.9m from 1st July 2023.

- The age restriction for downsizer contributions has been reduced to 55+ from the 1st January 2023.

- Compulsory super contributions have increased to 11.00% from the 1st July 2023.

Please feel free to contact us if you wish to discuss any of these matters.

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