UNCONVENTIONAL WISDOM | *Unique investor insights from Wattle Partners*

October 2021

The month that was…

- Global markets once again broke with history, not only passing through which is traditionally the most volatile month of the year but delivering the strongest such month in several years. After what seemed like endless queries around the valuation of the US and most global sharemarkets for that matter, the September quarter saw earnings catch up with the increasing price of most companies over the last two years. In fact, according to analysis some 90 per cent of S&P500 companies that have reported, exceeded analysts expectations despite a growing list of concerns. US markets were once again the leaders, the S&P500 gaining close to six per cent after another powerful period for the big tech companies whilst the ASX was hit with a large sell-off on the final day of the month offsetting the entire month of gains.

- October finally saw the reopening of most borders in Australia, with reports that Qantas (ASX: QAN) had seen some four billion frequent flyer points spent since the end of lockdown. The reopening is proceeding at pace with retail, travel, leisure and service trades set to benefit despite several internal borders remaining closed. Whilst the story is generally positive, the forward-looking nature of markets is such that a significant amount of this upside has already been priced into many companies. The reopening trade will not be smooth, as we have seen in the US, with investors needing to be highly selective and focused on identifying those companies who will avoid missteps and supply chain issues.

- 2021 has seen what may best be described as the 'barbell' trade paying off for traders and investors. The concept of Environment, Social and Governance investing is well known and appreciated in investment circles but probably less so by self-directed investors who in many cases simply expect their advisers to 'do no harm' when guiding the investment of their capital. The trade that has paid off in 2021 isn't necessarily 'value vs. growth' as many have suggested, but super clean and super dirty. On the one hand, the energy sector including coal miners and oil producers, have seen incredible returns, up 33 per cent over the last 12 months, and on the other hand, the 'green' power producers, tech businesses offering greater efficiency and high-performance computing companies have dominated.

- The final day of trade in 2021 saw one of the most unique events for fixed income traders in many years with the three-year government bond yield spiking over 800 per cent in just a few hours of trade. The bond had been part of the RBA's Yield Curve Control strategy through which it was seeking to keep the cost of capital low and incentivize the banking and corporate sector to both lend and borrow respectively. Hedge funds and investors had been shorting the three-year bond heavily in recent weeks based on their view that the policy would be abandoned, with the RBA all but giving up on buying the associated bonds on Friday. Then on Tuesday, it was confirmed. Whilst many suggest this points to higher interest rates coming sooner rather than later, the RBA remains steadfast that it is awaiting real wage growth before taking any major action.

- Disappointments continue to be heavily punished in equity markets with any company surprising or failing to live up to expectations being sold off heavily by investors. As October came to a close, Westpac suffered a 10 per cent correction after delivering weaker than expected profit on a blowout in costs and weaker than the expected net interest margin. It was a similar case for A2 Milk which faces a class action and has struggled to offer transparency into the difficult Daigou sales channel to shareholders during the pandemic. Both BHP and Fortescue missed production guidance with analysts growing wary of Twiggy Forrest's ballooning headcount in his green energy focused Fortescue Future Industries group.

- On the somewhat positive side, for Crown shareholders at least, was the fact that despite being found unfit to operate their own casino, the Royal Commission in Victoria did not strip them of said license. Rather they chose to install an independent chair and oversight model as the group sets about cleaning up their act. Macquarie Group reached $200 per share after once again delivering a doubling of profit with the group topping the investment banking table for 2021. Such is the strength of the business and the growing opportunities in renewable energy and other key growth sectors that they are announcing a capital raise at a discount of just 2 per cent to their current share price.

- Fund managers were in focus this month after fast-growing global equity active manager GQG Partners decided to list on the ASX, making it the biggest IPO of the year. Whilst the company didn't deliver a large stag profit as many expected, it reflects Australia's growing stature as a strong equity market and home for global leaders. The IPO comes amid growing pressure on two of Australia's most well-known managers, which we cover later in this report.

- It wouldn't be another month without the mention of Elon Musk, who despite continued concerns about the future growth potential of Tesla, became the latest company to reach a valuation of US$1 trillion dollars. It is an incredible result for a company that was seemingly under real pressure just a few years ago with some professionals suggesting a three trillion-dollar valuation isn't unrealistic given their dominance of both the electric vehicle hardware and software.

WATTLE PARTNERS

Model Portfolio Update

- Investment Committee –

Index	Index Points - September	Index Points - October	Performance	
			1 Month	1 Year
S&P/ASX 200	7332.2	7323.7	-0.1%	23.6%
All Ordinaries	7629.7	7639.1	0.1%	24.6%
US Dow Jones	33843.9	35819.6	4.4%	35.2%
US S&P 500	4307.5	4605.4	5.7%	40.8%
Hang Seng (HK)	24575.6	25377.2	4.7%	2.8%
FTSE 100 (UK)	7086.4	7272.4	3.7%	28.6%
Nikkei 225	29452.7	29647.1	4.2%	27.3%

Top 5 Performers	1 Month	Bottom 5 Performers	1 Month
Challenger Grop	10.5%	Pinebridge Asia Ex Japa	-3.6%
Macquarie Group	8.7%	Telstra Corporation	-2.8%
Origin Energy	8.5%	BHP Group	-2.8%
Wesfarmers Ltd	5.1%	Cooper Asian Equities F	-2.7%
Boral Ltd	3.9%	Endeavour Group	-2.6%

Sector	October	Year
A-REIT	0.4%	25.8%
Communications	-1.1%	36.8%
Cons. Discretionary	0.2%	33.1%
Cons. Staples	-2.3%	6.7%
Energy	-2.7%	33.1%
Financials	0.8%	43.6%
Healthcare	1.0%	6.6%
Industrials	-3.3%	15.8%
IT	2.1%	21.0%
Materials	-0.5%	10.3%
Utilities	-0.6%	-11.0%
Small Ords	0.9%	28.0%

It was another positive month for the Wattle Balanced Model which continues to eke out strong returns despite an increasingly uncertain outlook. The preference for shorter duration fixed income and defensive alternative allocations to high-quality bonds paid off after the selloff in global and Australian bond markets. The threat of higher interest rates hits traditional bond strategies hardest due to their longer duration and terms to maturity. Whilst we remain confident that the medium-term outlook for rates isn't significantly higher than today, we continue to err on the side of caution and have little willingness for losses in the low-risk component of portfolios.

The domestic equities allocation performed strongly once again, benefitting from very limited exposure to the energy sector which suffered another setback as the threat of supply sent prices lower. The allocation benefit from strong returns in the financial sector, including Challenger and Macquarie Group, both of which will benefit from a return to normal economic activity. Similarly, the allocations to both Wesfarmers and Boral Ltd offered better diversification than the bank dominated index.

The preference for seeking value in Australia and growth overseas has held back the global equities allocation, with growth managers struggling to keep up with lower quality cyclical companies. That said, the Franklin Global Growth and Ausbil Global Small Cap funds continued their stellar run whilst the two Asian equity strategies detracted. In terms of company-specific news, the updates were as follows:

Origin Energy (ASX: ORG) gained another 8 per cent after announcing the sale of a strategic 10 per cent stake in the Australia Pacific LNG project for $2.12 billion. Origin will retain 27 per cent of the business after the deal which allows the group to crystalise an investment they have held since construction and now into operation. The decision de-risks their position, allows for further capital into the business and will support the expansion of their renewable energy program.

Woolworths (ASX: WOW) delivered a difficult third-quarter update, falling 3.2 per cent after management delivered an update following the "most challenging COVID quarter" due to supply chain and staffing disruptions. Total sales were 7.8 per cent higher than the previous year, with Australian food gaining 3.9 and online sales exceeding 12 per cent of total sales after growing by another half. The BIG W division was among the hardest hit, sales falling 17 per cent as the majority of stores were closed and some 22,000 works have been forced to isolate at some point in time.

Boral (ASX: BLD) overcame weakness in the materials sector, which fell 1.2 per cent, gaining 4.6 per cent after management announced that the pandemic hit to asphalt and concrete sales were less than expected. The group took a $33 million hit to earnings, well below the $50 million anticipated with group revenue falling just 1 per cent.

ANZ Bank (ASX: ANZ) delivered a 65 per cent increase in profit, which hit $6.2 billion. The result benefitted from the reversal of $500 million in debt provisions and sees the group's equity level back to 12.3 per cent. The dividend was more than doubled to 72 cents per share, but it wasn't all good news with management reporting that loan growth was barely positive as the group struggled to deal with and process an influx of loan applications.

It was all about Macquarie (ASX: MQG) though with the company delivering a 107 per cent increase in profit for the half, reaching over $2 billion, and announcing a $1.5 billion capital raising. The company is seeking to cash up amid an abundance of green energy and other opportunities that are becoming available. Macquarie Capital was the key contributor having dominated corporate activity, whilst assets under management in their funds division gained 31 per cent. The company doubled their dividend to $2.72 per share.

Telstra (ASX: TLS) delivered the news of the day, gaining 2.1 per cent after confirming they had teamed up with the Australian Government to purchase Digicel's South Pacific telecommunications business for US$1.6 billion. The deal keeps the company out of Chinese hands, with Telstra contributing just US$270 million in equity, supported by a significant amount of government loans. The business is seen to be 'commercially attractive' with the government essentially underwriting the geopolitical risk. This is a great deal of shareholders but it reflects an unexpected pivot by the Government as they seek to combat the expansion and economic power of China. The days of public-private partnerships of this kind seemed over and when our competitors take similar action tend to be seen in a negative light.

Magellan (ASX: MFG) confirmed that their less than popular equity stake in investment bank Barrenjoey was profitable in the third quarter. They also highlighted strong demand for the FuturePay retirement Income production with Institutional Investments flagging Interest.

Never been a better time to buy big tech

- Drew Meredith -

This may sound repetitive, but the opportunity in Big Tech has never been better. The US quarterly reporting season has all but confirmed that the most important companies in the world remain in robust health.

That is, of course, with one small caveat; your definition of technology. The term Big Tech has come to encompass anything company that has a website or operates online, yet in my personal view, Big Tech really means that group of companies that are making people's lives better and easier.

Having given up on the likes of Instagram, Facebook and Tik Tok in recent months, my definition of tech has narrowed to just two companies: Microsoft and Alphabet, Google's parent company. Both are trillion-dollar companies, recently joined by Tesla in this rarified air, and both are showing few signs of slowing.

Before diving into the detail, it's worth taking stock of the current valuation of these two companies, which many headlines suggest are grossly overvalued.

As it stands today, Microsoft trades on a forward price/earnings (P/E) ratio of 36 times and Alphabet 27 times. As a comparison, two of Australia's better-managed companies, being Woolworths and Wesfarmers, trade on multiples of 28 and 31 times. Sounds expensive, doesn't it?

As is typically the case, the truth and opportunity lie below the surface, and despite the headlines, low bond rates aren't the only contributor to the valuation of these global leaders. In Microsoft's latest quarterly report it delivered a 22 per cent increase in revenue to US$45 billion, which supported a 25 per cent increase in earnings.

This is an important lesson in relying solely on a single measure like the P/E ratio, as 2021 has seen very little expansion in earnings multiples, but rather a 'catch up' from the earnings component as Big Tech flexed its muscles.

CEO Satya Nadella said it best when highlighting that every type of business can improve its productivity and the affordability of its products by "building tech intensity". This is the powerful trend that has supported staggering growth in the last few years, and likely for decades to come, with cloud computing still barely scratching the surface globally. And this comes ahead of what is expected to be Microsoft's biggest increase in the cost of its subscription Office products, which are expected to rise in price by 10 per cent.

The story is similar for Alphabet, which clearly separated itself from the Facebook, Twitter and Snapchats of the world when reporting a 41 per cent increase in revenue and 43 per cent increase in advertising revenue. Management put the outperformance (compared to rivals hit by Apple's new privacy restrictions) to the fact that Google offers an "intent-driven" buying model. This means people are searching for the products to which they receive ads.

Alphabet has continued its growth to become an "artificial intelligence" company, but ultimately is seeing to build more helpful products to people, and this is what truly stands out. Investing in Big Tech companies that are using people's data to target them, versus those that appear to be using people's data to improve the service they deliver and the businesses of those with whom they work.

By comparison to these outstanding numbers, Wesfarmers, a company I consider among the best managed in Australia, delivered revenue growth of 10 per cent for the full-year and profit growth of 16 per cent, yet it trades just 10 per cent cheaper than two of the largest and fastest-growing companies in the world.

Investing globally has always been a step too far for many investors, yet it has become easier than ever to achieve via ETFs, managed funds, platforms and other trading accounts. When we look back 10, 20 or 30 years from now, I know which companies I want to be holding.

Green October and the power of buybacks

- Investment Committee -

Despite a growing chorus of calls for a significant market correction, as is usually the case in October, nothing has been forthcoming during the most dreaded of months. In fact, it has been a story of the opposite, with US markets near all-time highs and massive flow of dividends and buybacks combined with zero term deposit rates forcing money back into the market.

After hoarding capital in 2020 as uncertainty placed significant pressure on boards all around the world, October has seen somewhat of a bonanza in capital returns and dividend boosts. Most importantly for retiree and superannuation investors, the franking credit-focused off-market buyback is back in vogue.

Plato
INVESTMENT MANAGEMENT

Dr Peter Gardner, senior portfolio manager at the specialist dividend-seeking Plato Investment Management group, this week highlighted the shareholder value delivered by the boards of both the Commonwealth Bank of Australia (ASX: CBA) and Woolworths (ASX: WOW).

According to Plato's analysis, CBA's $6 billion buyback and Woolies' $2 billion buybacks resulted in 67.7 million and 58 million shares being cancelled respectively. They were both significant windfalls for those who chose to tender, but particularly retirees in the pension phase; with Plato noting that "for pension phase and tax-exempt investors, one dollar of pre-tax income from fully franked dividends is actually worth $1.43."

In the case of the CBA buyback, Plato estimates an approximate after-tax profit of $14.27, or 14 per cent for those in the pension phase, compared to the market price of CBA. Woolies was even better, with $7.31 or 18 per cent in additional value. In total, $1.94 billion in franking credits were distributed by CBA and $750 million by Woolies.

"During the August reporting season, our analysis shows approximately $15 billion in franking credits were distributed, in addition to over $38 billion in cash dividends," said Plato.

Looking ahead, Plato expects there will be many more tax-effective buyback opportunities moving into 2022.

Don't get seduced by yesterday's returns

- Jamie Nemtsas -

"Money makes money. And the money that money makes, makes money" – Benjamin Franklin

To many, this quote likely stands out as being among the most capitalist comments that would appeal to a billionaire professional investor, managing over $100 billion for investors all around the world. Yet at the core of this quote is the almost singular focus that has been key to the success of Magellan Financial Group (ASX: MFG) since its founding in 2007.

The quote refers not to greed, but rather to the benefits of compounding returns. After a difficult period, which has seen Magellan's core global fund give up long-held outperformance against the MSCI benchmark, Magellan co-founder Hamish Douglass was quick to stress this point during his latest presentation.

His briefing was likely quite timely given the exuberance spreading into many parts of the market and ultimately greater volatility that lies ahead. Douglass offered insights into the impact of compounding on varying levels of return over a period of 20 years. Should Magellan continue to deliver the 12 per cent a year return that it has since 2007 for another five years, initial investors will have seen their investment increase tenfold over the period; a slow-burning ten-bagger.

As I wrote in a previous article recently, many have thrown the baby out with the bathwater in the case of Magellan, despite an exceptional long-term track record. Douglass confronted this head-on, highlighting the defensiveness of his approach, which targets a return of 9 per cent a year (rather than to beat the MSCI index), and comparing it to the ride of today's top performers.

The presentation explored the journey of one of many of 2020/2021's top performers, which tend to experience significantly higher volatility on a year-to-year basis, to show the benefit of patience and downside protection. In the case of the global fund, this downside protection is sought by investing in 'defensive' assets, being consumer staples names and truly high-quality companies like Microsoft, Alphabet and Visa.

"Don't get seduced by yesterday's returns," said Douglass, highlighting that his firm's core strategy has outperformed in every crisis, capturing just 45 per cent of the downside. And downside still matters, given the many risks to the near-perfect conditions that exist today. These include the threat of further vaccine mutations, speculative bubbles bursting, unexpected inflation or another hiccup in emerging markets.

So where do you turn in this environment? At the core of Magellan's approach is finding those companies and sectors that are growing faster than "world economic returns" which it calculates as the level of global GDP growth plus dividends. This becomes increasingly important as we stare at a period in which there is no doubt that interest rates will be higher in five, 10 or 15 years' time.

The focus must be on investing in defensive companies, or "structural growth assets" that are able to compound revenues at multiples of world GDP and most importantly, to do so consistently. There are several sectors that offer this type of opportunity, ranging from the shift to cloud, digital advertising, enterprise software, streaming and of course, Chinese consumption.

On the latter, Douglass didn't add to the hyperbole around China, stating that the region is not "uninvestable" as many high-profile commentators suggest, but rather the consumption story remains as strong as ever. Investors simply need to be patient and "wear the short-term volatility" with the potential for great opportunities.

Microsoft (NYSE: MSFT) remains the largest position in the fund, with the company described as "simply the best on offer." It's the third largest hyper-scale cloud provider in the world, has a 90 per cent market share in productivity products, 80 per cent in PC operating systems, and Magellan expects revenue to more than double to more than US$400 billion by 2030.

Netflix (NYSE: NFLX) is a more recent addition, with management willing to take the hits on short-term subscriber numbers for what they see as a long-term price. Their growing subscriber base, which now exceeds 200 million, opens both the streaming and advertising markets, but ultimately creates a "virtuous cycle" whereby cash flow breeds more content, and the content quality improves. This is highlighted by NFLX's 44 Emmy wins and the massive success of the local Korean series Squid Game.

There was no apology for the defensive positioning of the fund, given his mandate to protect capital. There was some contrition, however, on the decision not to put more into cyclicals after the vaccine announcements in November.

Infrastructure's disappearing act and the risk of home bias

While every self-directed investor knows that Australia's sharemarket represents just 2 per cent of the world's listed companies, investing in overseas markets remains a bridge too far for most. ASX-listed exchange-traded funds remain the most popular, however, the likes of iShares S&P500 (ASX: IVV) is gaining in popularity.

The most common concerns cited by prospective investors are that global equities are higher risk, introducing currency risk for example, or that they are 'over-valued' based on anecdotal evidence or recent headlines. Add to this the fact that most online trading platforms have very poor-quality international trading options, and it likely is easier to do nothing.

However, recent events in the domestic infrastructure sector are offering evidence into what the future, and perhaps the recent past, looks like for growth-starved investors. In a recent white paper, Ausbil's Global Essential Infrastructure team covered the seeming desertion of global quality infrastructure companies from the ASX.

In just the last few months, Sydney Airport (ASX: SYD), Spark Infrastructure (ASX: SKI) and AusNet Services (ASX: AST) have received takeover offers, each of which will either take them private or reduce the options available to investors. From a peak of 15 infrastructure companies in 2005, there are now less than ten and the trend is clearly moving towards zero.

The solution, Ausbil suggests, is to look global. And the same case can be made for the DIY investors who have limited their universe to the old-fashioned ASX blue chips. A cursory scan of the S&P/ASX50 and to be honest, there isn't much to write home about. On the one hand, we have four great banks, better known for their dividends than their ability to fight off the wave of fintech disrupters eating into their profit margins. We then have three iron ore miners, a global leader in the healthcare space and one technology company that has benefited from the boom in residential property.

Thinking about investing and diversification in its most simple form, and most would suggest holding an investment in each of the 11 major sectors of the economy. Yet building this sort of portfolio solely from the largest companies listed on the ASX is exceedingly difficult. Not so if you look overseas.

While Australia bats above the average in terms of global leaders, with CSL (ASX: CSL) and BHP (ASX: BHP) the standouts, years of investors focusing on income has seen our best and brightest head to global markets. The US market is flush with global leaders in everything from technology to computing, healthcare and financial services. Europe, despite the slow recovery from the GFC, is also home to some of the world's leading global brands, manufacturers and machinery companies. And that's without mentioning China.

Fortunately, the excuse of it being too difficult or too risky to invest overseas is gone, with a plethora of options available to investors. The first choice is generally the direct purchase of global stocks, which requires a more advanced trading platform but extends into a growing range of active and passively managed exchange-traded funds. Old-fashioned managed funds remain the most popular option, with the mFunds platform offered by the ASX gaining traction.

The timing couldn't be better for investors given that most SMSF portfolios remain overweight to domestic over global shares, but particularly in comparison to the 'smart money'. Institutional investors like AustralianSuper and the Future Fund have had equal if not larger global weightings than domestic for many years.

How to get your kids involved with investing

- Drew Meredith -

One of the most powerful trends of 2020 was no doubt the huge surge in retail investors joining the stock market frenzy. With fresh stimulus cheques and stay-at-home orders in place, many turned to shares to pass their time.

In a world where financial literacy remains incredibly low, any engagement with investing should be seen as a positive, even if it may be uninformed and quite risky. The trend didn't take off as strongly in Australia, perhaps due to our relative success during the pandemic, so engagement remains as important as ever.

As a financial adviser, I'm regularly meeting with retired clients, or those transitioning into retirement and one of the most common requests centres around how to get their children involved with investing. It seems that for every retiree couple searching for the next dividend-payer, there are 2.4 children ignoring the markets altogether.

With this in mind, I've put together what, in my experience, are the five steps you should take to get your children engaged with investing.

Give them money. I'm sure that got your attention, as it will garner theirs. The best way to encourage young people to be engaged with money is to give them some. But you need to give it some thought; is it best gifted in the form of shares, units in a trust, or an ETF? It depends on your preference and theirs.

Invest in something they know. This leads me to the second tip, which is to find something relatable to your children. Do they enjoy gaming? Do they travel regularly? Are they worried about cyber security? Or climate change? In 2021 the investment options are endless with just about anyone able to access any investment they like. For instance, you can buy shares in Airbnb, an ETF investing in e-sports like Nintendo, or a renewable energy company.

Look outside Australia. No offence, but your children don't want to invest in the same investments as you. They do not want to buy high-dividend-paying stocks, or the old-fashioned, reliable listed investment companies. The world is more global than ever, so don't pass your home bias onto your children.

Find a user-friendly app. UX refers to 'user experience,' or how a customer interacts with your product. It is central to the way we all use our phones and other platforms on a daily basis. Unfortunately, despite significant investment, many of the traditional broking platforms offer little in the way of innovation; this was a major reason for the success of Robinhood. To engage your children, you need to find an app or platform that is both user-friendly and engaging for them.

Throw away the ratios. Your children don't care about dividend yields, franking credits or price-earnings ratios, they are all about growth. This is evident in the way that markets are operating in 2020 and 2021; those who invest with optimism have been rewarded, while those who are concerned about losses have missed out.

Inflation misdirection

- Drew Meredith -

'Inflation risk is real'. 'Federal Reserve turns hawkish'. 'Tapering to begin in November'.

These were the headlines that followed Federal Open Market Committee (FOMC) member Randal Quarles' speech at a conference last week. Yet the headlines once again highlight the risk of confirmation bias that afflicts even the most objective, professional investors.

While the headlines were true, in that Quarles did support a decision to start reducing the Fed's massive bond purchasing program in November, the coverage missed a significant amount of discussion and commentary about what has actually been occurring in the economy.

In a wide-ranging speech, Quarles offered insights into the FOMC's decades of experience and both the issues and opportunities that are arising as a result. At present, he suggested, "supply bottlenecks and labour shortages.....are camouflaging continued strong underlying demand," but this does not of itself lead to the inflation outbreak that we all fear.

There is a growing list of expert hedge fund investors, billionaires and economists suggesting the Federal Reserve is "behind the curve" and not doing enough to avoid a disastrous economic outcome. The speech directly targeted this cohort, with Quarles stating he doesn't believe the Fed is behind the curve for three key reasons: "most of the biggest drivers of the very high current inflation rates will ease in coming quarters; some measures of underlying inflation pressures are less worrisome, and longer-term inflation expectations are anchored, at least for now."

Looking beyond the headline figures, he reiterates that "the inflation we have experienced so far has been very unusual and largely related to supply constraints associated both with production and distribution problems related to COVID and with a demand shock arising from the unprecedented and rapid reopening of the economy."

This is not an unexpected result following a global pandemic not seen for several decades and not once in the careers of those managing money or pontificating about economies today. Referring to the "trimmed mean" measure of inflation, which systematically removes prices that are increasing or decreasing at 'abnormally large rates', the true inflation rate may well be as low as 2 per cent. This once again highlights the importance of policymakers seeking to 'look through' the short-term data towards the longer-term trend, something very difficult for market participants to do.

The concept of 'transitory' inflation remains misinterpreted, with many believing transitory must be short-lived, when it refers to the source of said inflation. That said, if inflation remains high for too long, it may impact inflation expectations, which then impacts wage growth. But ultimately the dilemma faced by the Federal Reserve is likely clear to everyone:

"Demand, augmented by unprecedented fiscal stimulus, has been outstripping a temporarily disrupted supply, leading to high inflation. But the fundamental productive capacity of our economy as it existed just before COVID—and, thus, the ability to satisfy that demand without inflation—remains largely as it was". That likely suggests a return to below trend-growth after this is all over.

Quarles reiterated that regardless of the ultimate inflation result, the Federal Reserve is as confident as ever that it 'has the framework and tools to address' inflation.

Investing in a world where money is free

- Jamie Nemtsas -

Both Magellan (ASX: MFG) and Platinum Asset Management (ASX: PTM) have been gaining plenty of unwanted attention lately. Both their hallmark strategies are suffering from periods of underperformance, the former due to a lack of cyclical exposure and the latter an ingrained value focus.

It is somewhat interesting therefore that both are banking on China as being central to their recovery. One thing they have in common is the e-commerce giant and current Chinese government target, Alibaba. The company was recently reintroduced to the Platinum Asia Fund and remains the only Chinese holding in the Magellan Global strategy.

In a similar vein to Hamish Douglass' recent comments, Platinum highlighted the many misperceptions towards the Chinese market, driven primarily by media headlines. "The danger for Western investors is to not be willing to look at China through a different lens" said the portfolio manager of the flagship fund.

According to Platinum's analysis, China's equity market peaked way back in 2007, along with most developed nations. At this point, it was the most expensive market in the world trading on a forward price to earnings ratio of 27 times. The market then tanked as much as 68 per cent in just a few months and today, 14 years on, it remains 38 per cent below this high.

This, they suggest, is evidence that China does not look like a country that is about to experience a financial crisis, but one that has clearly already seen it. Platinum is somewhat surprised that the selloff hasn't been more significant, noting that markets are well off their highs for the year, but only flat for the year to date.

Not unexpectedly, some two-thirds of the International Fund is held in what can broadly be described as cyclical sectors, being energy and materials, financials and real estate, industrials, and discretionary stocks, with a touch of semiconductors, sprinkled in for growth. Management used the recent volatility to bump up their short positions but ultimately remain confident of the long-term outlook, albeit not for high growth tech stocks.

"In a world where money is free, the disrupters are seen to have fewer barriers to their ultimate success than they would do if money was less readily available". The statement clearly articles the views of traditional value-seeking investors, with the thesis of growth set to be tested as bond yields continue to drift higher.

Returning to the hyperbole surrounding Evergrande and China's property sector, they are quit to highlight how "unremarkable" this looks in comparison to say Sydney, Auckland, or Toronto. Chinese property prices have barely kept up with their developed market peers, with domestic buyers facing the highest loan rates in the world and the need for 30 rather than 20 per cent deposits seen in Australia. It is this confidence that has meant holdings in China Vanke and China Resources have been retained.

Market Thinkers

- Jamie Nemtsas -

We have had an exciting beginning to our latest webinar and podcast series, Market Thinkers, in which we focus on all thing's retirement. These are accessible here:

- Apple Podcasts
- Whooshka