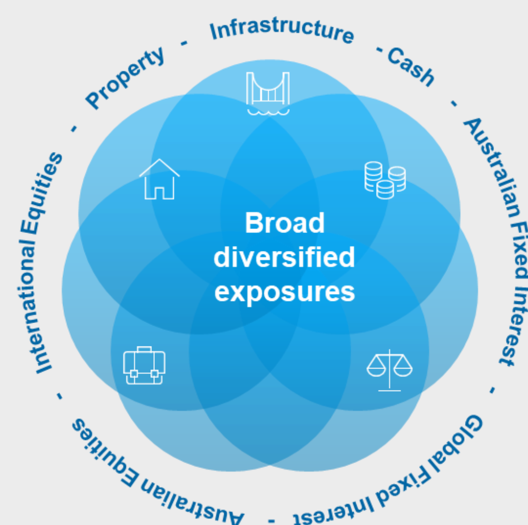
Investment Management

Macquarie Access Growth Multi Asset Portfolio

Quarterly Report – September 2020

The performance information and commentary below is based on a Model Portfolio. The information does not take into account differences between the Model Portfolio and the actual portfolio implemented by the operator of your managed account or any fees, expenses or other costs. The performance of your managed account will differ to that of the Model Portfolio (and may differ significantly) due to factors including an incomplete implementation of all trades, the timing of trades, the individual circumstances of an investor as well as the fees, expenses and other costs charged by the operator of your managed account. All references to selling, investing, participating, positioning or similar are references to the Model Portfolio only and may not reflect the holdings in your actual portfolio. Please contact the operator of your managed account for further information.



Model portfolio performance to 30 September 2020

	Gross returns*1	Net returns2	Investment return objective3	Net excess returns
3 months (%)	0.74	0.70	1.03	-0.33
6 months (%)	8.02	7.94	2.65	5.29
Since inception (% nom)**	-3.81	-3.93	4.62	-8.55

* Performance information is based on the performance of a model portfolio. See above for further information that will result in differences between the performance of the model portfolio and your managed account. Performance information excludes fees and other costs that may be charged by the operator of your managed account.

Past performance is not a reliable indicator of future performance.

** Inception date is 25/11/2019

[1] Gross returns are quoted prior to the deduction of all fees and expenses. Total returns are calculated based on changes in net asset values and assumes the reinvestment of distributions. Due to individual investor circumstances, the gross returns for an investor may differ from the gross returns quoted above.

[2] Net returns are quoted after the deduction of a management fee of 0.154% (inclusive of GST) which is the highest management fee applicable for an SMA managed in accordance with the Macquarie Access Growth Multi Asset Portfolio. Total returns are calculated based on changes in net asset values and assumes the reinvestment of distributions. Due to individual investor circumstances (including different management fees), the net returns may differ from the net returns quoted above.

[3] The investment return objective is 4.5% pa above Australian inflation over the medium term (before fees). Inflation is defined as the Consumer Price Index (CPI) as measured by the Reserve Bank of Australia Trimmed Mean, as published by the Australian Bureau of Statistics.

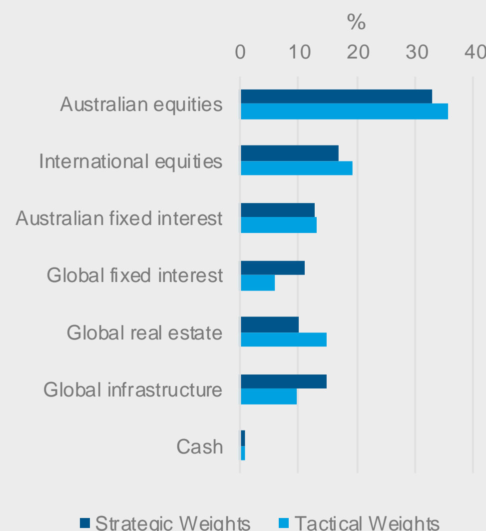
Model portfolio performance

The Model Portfolio delivered a positive return in the third quarter of 2020, with the exposure to growth assets contributing to performance. From an asset allocation standpoint, the Model Portfolio has been positioned with a modestly defensive bias in light of the declining fundamentals. However, we took the recent correction in equity markets as an opportunity to move the Model Portfolio to a more neutral positioning.

Asset Allocation

Asset prices, particularly those of growth assets, have deviated significantly from the real economy since March. In the real economy, businesses are grappling with the 'second wave' or 'second lock-down' with no end in sight, and the labour market recovery has stalled, particularly in areas with worsening COVID-19 spread. Asset markets, on the other hand, are dominated by the theme of 'chase for yield'. Indeed, ultra-loose monetary policy has resulted, and will continue to result, in increasing difficulties for investors to seek higher yielding assets to match their growing liabilities. Consequently, investors can feel forced to increase their investments to the higher end of the risk spectrum. The logical outcomes can be threefold. Firstly, asset prices across the risk spectrum have increased and will continue to increase should monetary policy remain extremely accommodative. Secondly, asset price behaviour will continue to deviate from the real economic activity. Finally, asset price volatility behaviour will change as the market continues to anticipate a prolonged period of ultra-loose monetary easing. Indeed, in the period between 2009 and 2019, where the US Federal Reserve kept ultra-loose monetary policies, equity markets experienced a long period of low volatility and moderate returns. With the current economic outlook of slow economic recovery and astonishing levels of public and private debt at a global scale, monetary easing policies will likely continue for years to come. As a result, we believe markets are entering into a prolonged period of low volatility and moderate positive returns. However, tail risks in asset prices have also increased due to their dislocation from the real economy, where increasing geopolitical tension, social unrest due to inequalities, political uncertainty and sovereign default risks persist. In the real economy, we also witnessed uneven economic recovery at a global level since March. China recovered robustly at all levels, whereas Europe and the US are experiencing an considerably uneven economic 'stop-start' recovery as some areas experience a second wave. Looking

Portfolio allocations



forward, we expect China to remain a relatively dominant force in global growth, even in the slow growth world we envision. In Australia, we also expect a robust economic recovery as the country's COVID-19 situation continues to improve. In theory, this can lead to a similar rebound to that witnessed in China. Putting these altogether, we took the recent weakness in equities as an opportunity to increase our allocation to Australian and international equities. Furthermore, we continue to look to increase our growth assets allocation should valuations improve further, while utilising tactical asset allocation to mitigate against the risk of sudden market shifts.

Market overview

Australian and international equities market

The retracement in risk assets continued in the September quarter as technology valuations drove stock indices to all-time highs. However, heading into September, equities showed signs of faltering and increased volatility, with the markets continuing to rise and fall with the political narrative from the US presidential election, where there has been increased speculation on a contested election. The negotiations on a further fiscal package also added to the uncertainty. International equities rose by over 7.0% in Q3, while Australian equities underperformed, declining by 1.4% over the quarter.

Australian and global credit market

Credit markets performed at a slower pace compared to equities over the quarter. In the US investment grade (IG) market, spreads closed 14bps tighter at 136bps, while high yield tightened 109bps to finish the quarter at 517bps. The rally in credit spreads was very much broad based to begin with, then particularly extended to non-core assets such as BB-rated credit and emerging markets debt as the search for yield intensified into the quarter. European IG credit outperformed the US in Q3, compressing 30bps to 119bps, while Australian credit spreads also tightened 24bps over the quarter.

Australian and global bond market

Bond markets were characterised by lower volatility for the first part of Q3, before yield curves began to steepen into August as risk sentiment re-strengthened. This move was predominantly driven by upside surprises in global data and media focus on potential vaccine candidates. However, this move was partially offset in September by lower yields and flatter curves as risk markets faltered. Overall, the US 10 year Treasury yield ended the quarter 3bps higher at 0.69%. Australian bond yields outperformed global markets, driven by expectations for further central bank easing which emerged later in the quarter, with the 10 year Australian Commonwealth Government Bond yield falling by 8bps to 0.79%.

Outlook

During September, the Macquarie Fixed Income team gathered for our third Strategic Forum for 2020, where the global team stepped back from the daily noise to reassess the market dynamics and drivers. Over the course of the Forum, we discussed the economic outlook and each asset market in-depth to identify a base case outlook and risk assessment.

Summarising our economic outlook, we observed that there has been a noticeable bounce in economic activities. However, it has been uneven across countries and sectors. The depth of decline in growth was severe and it will take multiple quarters (if not more) to get back to where we were in January before the virus impacted the economy, and we recognise that this starting point was one where the pace of economic growth was already lacklustre.

On policy, there is no doubt that the contraction would have been far worse without the incredible support from both central banks and governments, yet we felt it is important to reference these interventions as support and not stimulus. Looking forward, there are now some genuine question marks around whether these programmes can be extended at current levels, in particular on the fiscal side with this avenue more aligned toward 'politics', and as with anything in politics, 'progress' generally takes a lot longer. This is particularly the case in the US, with the upcoming elections creating uncertainty with some scenario outcomes likely to result in significant policy change.

We also considered the outlook for inflation given the incredible policy action delivered. We noted that the structural factors that have worked to depress inflation for the past decade(s) are still present and if anything worse, and are now coupled with a significant output gap. Also, simply doing more monetary easing is unlikely to improve its lack of effectiveness. Thus, low inflation is likely to persist, but we recognise that if fiscal support turns into sustained and substantive stimulus this could change the current environment.

With the 'lower for longer' environment likely to continue, the 'absence of yield' theme is expected to characterise multi-asset investment for a considerable period. This is expected to strongly influence growth assets in particular, though we believe that the uncertainty surrounding the US election is likely to encourage caution in the short term.

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