Fiducian Monthly Economic Commentary Report

30 November 2021

Conrad Burge, Investment Manager, Fiducian Investment Management Services Limited

ECONOMIC OUTLOOK

GLOBAL ECONOMY

The global economy is continuing a slow recovery from last year's recession, which saw the biggest downturn since the Second World War. The global economy is forecast to grow by around 6% this year and 5% next year (IMF estimates), with the US forecast to expand more rapidly than most other advanced economies. China and India, the world's two largest developing economies, are forecast to expand at an even faster rate. However, much depends on the continuing effectiveness of vaccination programs aimed at countering the COVID-19 coronavirus pandemic.

The global economy is continuing its slow recovery from last year's recession, which was the most severe since the Second World War. According to the International Monetary Fund (IMF) in its latest report (October), the world economy is forecast to expand by slightly under 6% this year (rebounding from last year's low base) and by slightly under 5% in 2022. The advanced economies as a whole are forecast to grow by 5.2% this year and 4.5% next year, with US growth expected to be 6% this year and 5% in 2022. However, growth in the Euro zone (5.0% and 4.3%) and in Japan (2.4% and 3.2%) is expected to be less robust. Much of the developing world is also recovering, with China forecast to grow by 8% this year and 5.6% in 2022 and India forecast to do even better, with growth rates of 9.5% and 8.5% over this period. This general forecast of a strong global recovery though is predicated on the effectiveness of vaccination programs to counter the COVID-19 coronavirus that originated in China and spread around the world from early last year. While rising vaccination rates have led to a significant drop in hospitalisation and death rates in most countries, some regions, notably in Europe, have seen the virus begin to spread again after the lifting of 'lockdowns' in recent months.

While expansionary monetary and fiscal policies remain in place around the world, some of the major central banks, notably the US 'Fed', have begun to slowly reduce the size of 'QE'. However, interest rate rises are still some way off, especially as inflation is forecast to subside in 2022.

As Jerome Powell, Chairman of the US central bank (the 'Fed') noted on 3 November in relation to the outlook for the US, 'the path of the economy continues to depend on the course of the virus'. Nevertheless, the 'Fed' has decided that recovery is progressing enough to warrant some slow tapering of its expansionary monetary policy, so that from November it will 'begin reducing the monthly pace of its net asset purchases ('quantitative easing' or 'QE') by a total of $15 billion per month (from its current level of $120 billion per month). It is likely to be some considerable time though before the 'Fed' and other central banks begin to raise interest rates, as while 'inflation is elevated, this largely reflects factors that are expected to be transitory'.

AUSTRALIAN ECONOMY

The Australian economy has also been heavily affected by the coronavirus pandemic but a successful nation-wide vaccination program appears set to lead to a re-opening.

The Australian economy was recovering strongly until the recent spread of the 'delta' variant of the virus, which led to further lockdowns and likely economic contraction in the September quarter and into the December quarter. While high vaccination rates have been allowing the domestic economy to now re-open, continuing stimulus is likely to be needed through 2022.

MARKETS

Major share markets have been rallying since March last year and could potentially rise further over coming months assuming that highly expansionary monetary and fiscal measures remain in place.

Most share markets reacted to the initial spread of the pandemic last year with a short-lived heavy setback but then began to rebound, with most major markets rising in 2020. This year, up to 23 November, market movements have included rises of 25% for the broad US market (S&P500), 22% for the technology-focused Nasdaq, 13% for the UK, France 27%, Germany 16%, Japan 9%, China 3%, India 23% and Australia 13%. Markets could have further upside, assuming expansionary monetary and fiscal policies remain in place.

While major sovereign bond markets have seen yields rise somewhat in recent months, they mostly remain historically low as a result of central bank bond purchases.

Major sovereign bond markets saw yields reach record lows in March 2020. Central banks have since tried to keep rates low to lift economic activity, although longer-term bond yields in some cases have risen this year. The US 10-year Treasury bond yield fell to an historic low of 0.54% on 9 March 2020 but was 1.68% on 23 November 2021. Similarly, the Australian 10-year bond yield was 0.57% on 8 March 2020 but was 1.87% on 23 November. Some sovereign rates though remained either close to 0% (France and Japan) or even negative (Germany). As such, most bond markets continue to look expensive.

FIDUCIAN FUNDS

The Fiducian Funds are currently overweight equities, underweight bonds and overweight cash.

Fiducian's diversified funds are currently above benchmark for international and domestic shares, around benchmark for listed property and well underweight fixed interest sectors, while cash weightings remain well above benchmark.