akambo FINANCIAL GROUP

THE MONTHLY VIEW

A look back at last month and an outlook on the months ahead

WHAT WE LIKED

- The Australian Industry Group Australian Performance of Manufacturing Index (Australian PMI®) increased by 3.5 points to 58.8 in February 2021, with the stronger pace of recovery delivering the index's highest monthly result since March 2018 (readings above 50 points indicate expansion in activity, with higher results indicating a faster rate of expansion).
- Australia's economy expanded at a much faster-than-expected pace in the final quarter of last year. The economy accelerated 3.1% in the three months to December, data from the Australian Bureau of Statistics (ABS) showed. Economists in a Reuters poll forecast a 2.5% rise following an upwardly revised 3.4% gain in the third quarter.
- A measure of Australian business confidence rose to decade highs in February as sales, profits and employment all picked up sharply in a positive sign for a continued economic recovery from last year's COVID-induced recession. National Australia Bank's index of business confidence climbed four points to +16 points in February, levels last seen in 2010. Its measure of conditions rebounded 6 points to +15, almost entirely recouping a pullback in January.
- Nonfarm Payrolls in the US rose by 379,000 in February, the data published by the US Bureau of Labor Statistics showed. This reading followed January's increase of 166,000 (revised up from 49,000) and beat the market expectation of 182,000 by a wide margin.
- The business activity in the US manufacturing sector grew at its strongest pace in three years with the ISM Manufacturing PMI rising to 60.8 from 58.7 in January. This reading came in higher than the market expectation of 58.8.
- Japan's job availability increased, and the unemployment rate fell in January, indicating the immediate impact of the country's second pandemic-related state of emergency was limited.

WHAT WE DIDN'T

- Australian and Chinese trade tensions continue to simmer away, leaving potential for further trade restrictions during 2021.
- U.S. homebuilding dropped to a six-month low in February as severe cold gripped many parts of the country, in a temporary setback for the important housing market.
- Americans shopped less in February, leading retail sales to fall 3% on a seasonally adjusted basis, the Census Bureau reported. Economists polled by Reuters had forecast retail dropping 0.5% in February. On a more positive note, January sales were revised up to show sales rebounding 7.6% instead of 5.3% as previously reported.
- The Caixin/Markit services Purchasing Managers' Index (PMI) in China fell to 51.5, the lowest since April, from 52.0 in January but remained above the 50-mark that separates growth from

contraction on a monthly basis. The loss of momentum came as China faced coronavirus flare-ups at the start of the year, while overseas demand continued to be hit by the COVID-19 pandemic.

- The euro zone economy contracted more than previously estimated in the last three months of 2020 against the previous quarter, revised data showed on Tuesday, as household consumption plunged because of COVID-19 lockdowns. The European Union's statistics office said gross domestic product in the 19 countries sharing the euro fell by 0.7% quarter-on-quarter, more than the initial 0.6% estimate, for a 4.9% year-on-year drop, less the previous estimate of 5.0%.
- The Japanese GDP increased by 2.8% in the fourth quarter of the last year, which is less than has been expected by analysts. Consensus expectations were to see 3% growth during that period.

BASE CASE

Our view of the most likely scenario for markets over the coming months, for which our portfolios are currently positioned.

73% Probability

Uneven speed of vaccination rollouts in different regions are expected to weigh on market sentiment. Despite this economic activity is expected to remain robust, as social normalisation and stimulus provides support. While the economic improvement is not expected to be linear, markets will continue to focus on expected economic improvement over the rest of the year. Companies and sectors leveraged to economic activity and fiscal stimulus are expected to continue their recent outperformance in this environment.

Global central bankers have reiterated their accommodative stance recently, with the expectation being they will continue with unprecedented amounts of stimulus to support global economies and financial markets alike. On the fiscal front governments have indicated they are willing and able to step up with spending to support their economies. The U.S government USD$1.9 Trillion stimulus package is being implemented, and we now expect markets to focus on the details of the planned U.S infrastructure package. Current estimates are for somewhere around USD$3 Trillion in spending to be articulated.

Despite the expectation for significant central bank and government support we remain alert to economic risks in global economies and within the financial system. Those we view as most prescient include China and Australia trade tensions, faster than expected increases in government bond yields, the increase of COVID-cases in the northern hemisphere, slow vaccine production and stimulus packages that underwhelm expectations.
This scenario is likely to see us maintain a constructive view on growth assets, despite the expectation for short-term volatility, with capital preservation targeted through appropriate company and sector allocations. Overall asset allocation will retain a bias to growth assets.

BEAR CASE

Our worst-case scenario for the coming months, which we are prepared to position for should conditions deteriorate.

11% Probability

The effects of the global health pandemic last longer than expected, with countries across the globe struggling to control further outbreaks. In addition, the manufacturing and distribution of a vaccine proves to be more difficult than anticipated, delaying the expected economic recovery further. Despite global economies currently showing resilience the increased cases blunt economic growth. This situation may place the nascent global economic recovery at risk. In such an instance the economic impact becomes more severe resulting in company earnings not improving as quickly as currently expected.

This scenario may see central bank stimulus and fiscal support from governments as lacking the required potency to provide economic stabilisation and provide further improvement in consumer confidence. Any failure of governments across the globe to extend or further stimulate their economies through fiscal spending would further erode confidence in economic improvement. This is likely to see further dislocation in financial markets across the spectrum.

A more elongated downturn may also see social unrest across affected economies, further exacerbating the negative impacts. In such an environment, we may experience volatility at similar levels to early last year, with certain pockets of the financial system coming under heavy pressure in relation to earnings and solvency.
An emerging risk is rising government bond yields. While considered unlikely, an acceleration of bond yields from current levels could see valuation compression in financial markets. This would be more pronounced in high valuation stocks and sectors in markets.

Above scenarios will see us take an even more defensive position and potentially add downside protection measures. The accelerating bond yield scenario would require a more nuanced shift toward companies and sectors that would be greatest beneficiaries of such a move. The overall focus will remain on capital preservation.

BULL CASE

Our most optimistic view for markets over the coming months.

16% Probability

Countries across the developed world continue to control the spread of COVID-19, accelerating the nascent economic recovery. This will allow markets to look through any softness in global economies and begin pricing in rapid economic improvement for the remainder 2021.

Strong fiscal support from governments around the world continue to fill the demand hole left by measures being used to suppress the spread of the virus, while debt burdens are delayed and kept manageable due to historically low interest rates. In the event central banks maintain measures aimed at supressing interest rates we would expect this to further fuel growth asset appreciation, while any acceleration of these policies would have the potential to accelerate the expected upward re-rating of growth asset pricing.

Such an environment would see substantial improvement in economic activity globally. This would occur as pent-up demand from business and consumers combined with massive government and central bank stimulus measures create a potent environment for risk assets as demand returns with a vengeance. High levels of excess saving built up over the past 12 months amongst consumers and corporates will further fuel the expected demand. Sectors expected to benefit most in this environment are those leveraged most to economic activity, in many cases these are the same companies that were most adversely affected by the COVID-19 induced lock downs.

This scenario would be cheered by financial markets as a combination of monetary and fiscal stimulus act to fuel demand for growth assets in a low to negative real interest rate environment. We would act by reducing our cash levels further and adding to the growth asset allocation.

STOCK IN FOCUS

The Chicago Mercantile Exchange (CME) is a global derivatives marketplace based in Chicago. Through its exchanges, provides products across all asset classes, including futures and options based on interest rates, equity indexes, foreign exchange, energy, agricultural products and metals. The Company's segment primarily consists of the Chicago Mercantile Exchange Inc. (CME), Board of Trade of the City of Chicago, Inc. (CBOT), New York Mercantile Exchange, Inc. (NYMEX) and Commodity Exchange, Inc. (COMEX) exchanges. The Company provides electronic trading around the globe on its CME Globex platform. The Company also offers clearing and settlement services across asset classes for exchange-traded and over-the-counter derivatives through its clearinghouses CME Clearing and CME Clearing Europe. It also provides hosting, connectivity and customer support for electronic trading through its co-location services. The Company's CME Direct platform offers side-by-side trading of exchange-listed and privately negotiated markets.

The CME was founded in 1898 as the Chicago Butter and Egg Board, an agricultural commodities exchange. Originally, the exchange was a non-profit organization. CME demutualized in November 2000, went public in December 2002, and merged with the Chicago Board of Trade in July 2007 to become a designated contract market of the CME Group Inc., which operates both markets. On August 18, 2008, shareholders approved a merger with the New York Mercantile Exchange (NYMEX) and COMEX. CME, CBOT, NYMEX, and COMEX are now markets owned by CME Group. After the merger, the value of the CME quadrupled in a two-year span, with a market cap of over $25 billion.

Today, CME is the largest options and futures contracts open interest (number of contracts outstanding) exchange of any futures exchange in the world. CME Group trades several types of financial instruments: interest rates, equities, currencies, and commodities.

CME also pioneered the CME Span software that is used around the world as the official performance bond (margin) mechanism of 50 registered exchanges, clearing organizations, service bureaus, and regulatory agencies throughout the world.