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Your financial future,
tailored your way

MPW Half Year Market Update - August 2022

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The purpose of this presentation is to provide you general advice and insight into MPW's current market outlook and investment philosophy.

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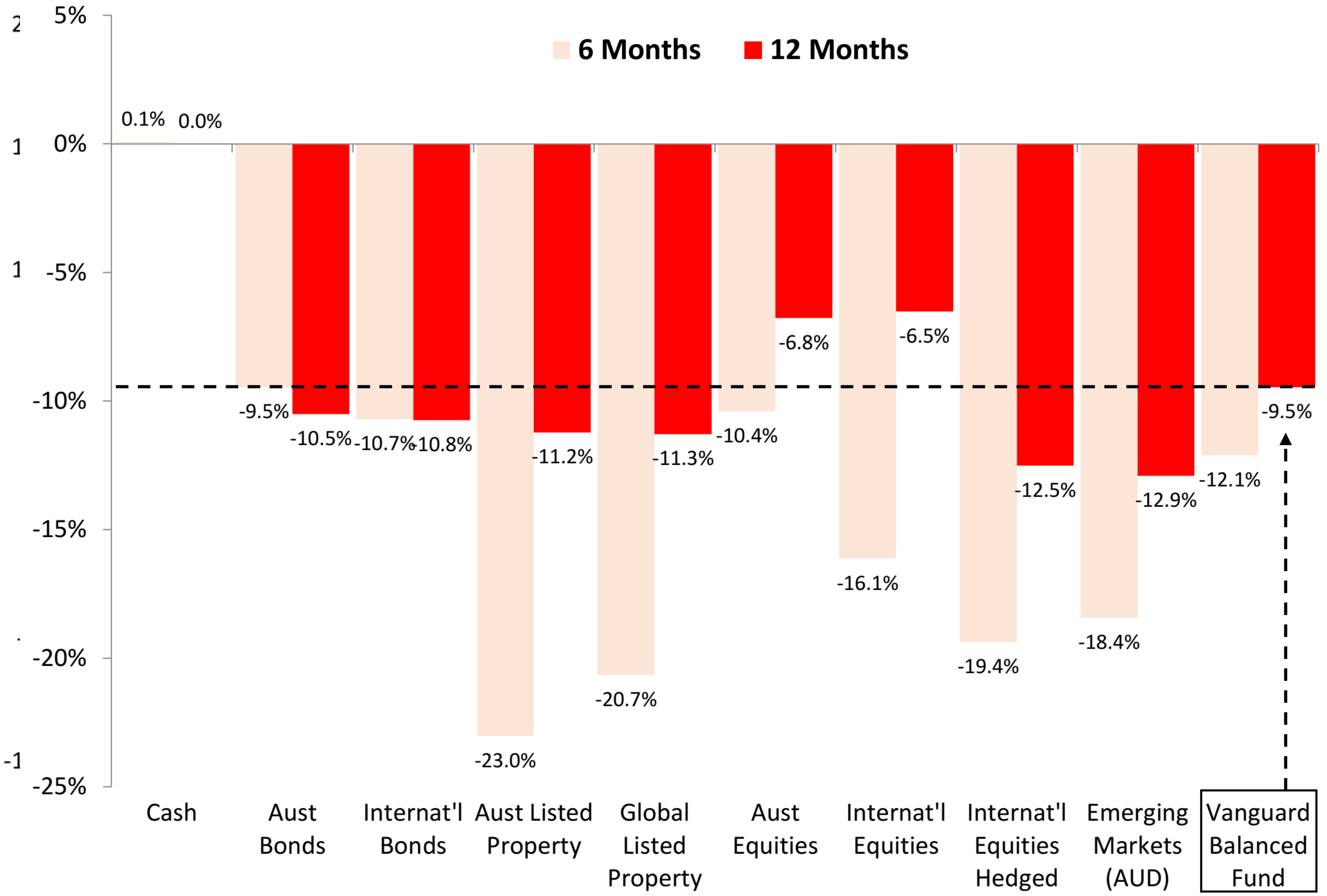
Asset Class Returns To 30th June 2022



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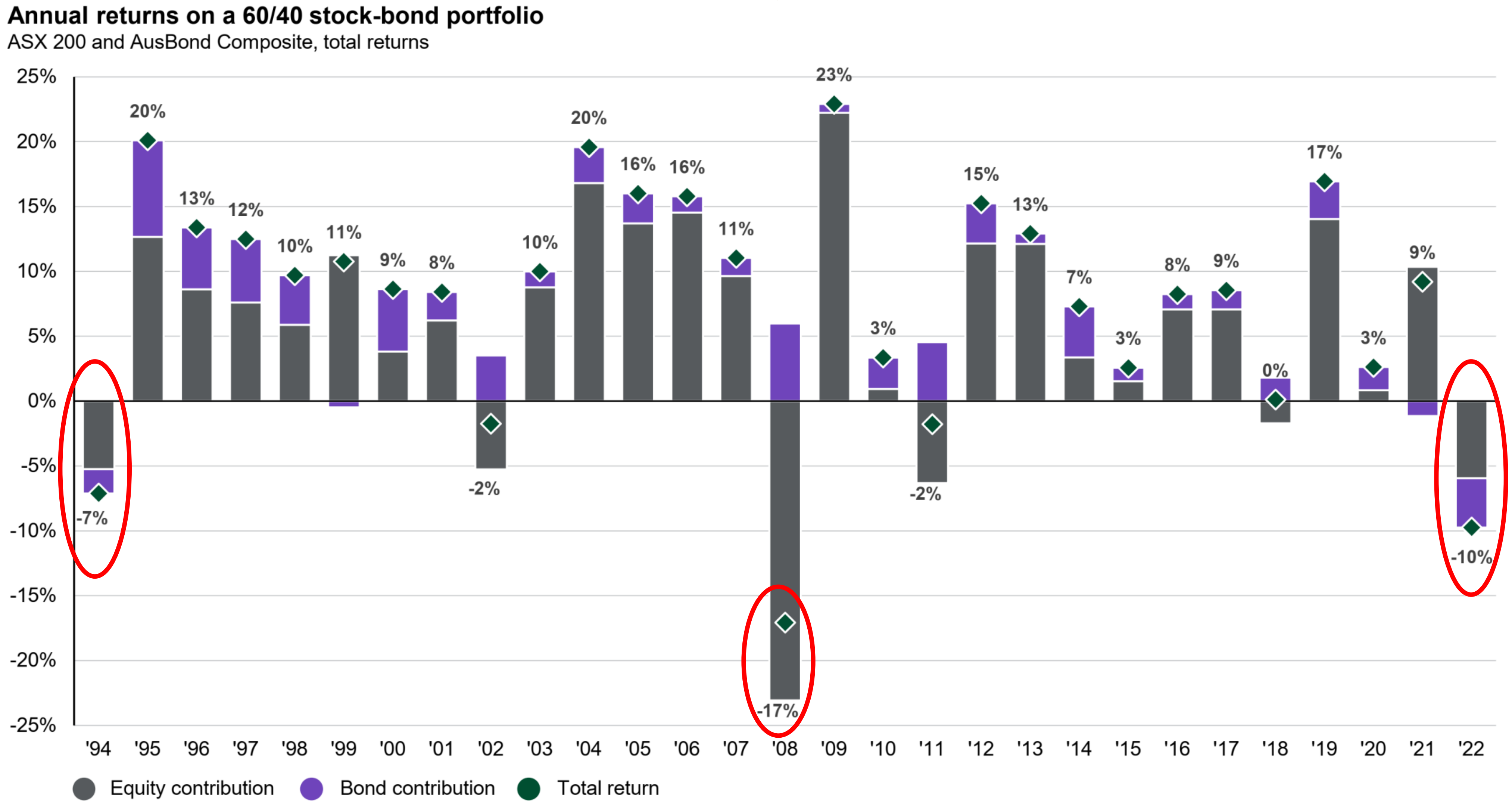
Shares and Bonds: Nowhere to Hide in the 2022 FY!



Source: Bloomberg Finance L.P., Standard & Poor's, J.P. Morgan Asset Management.

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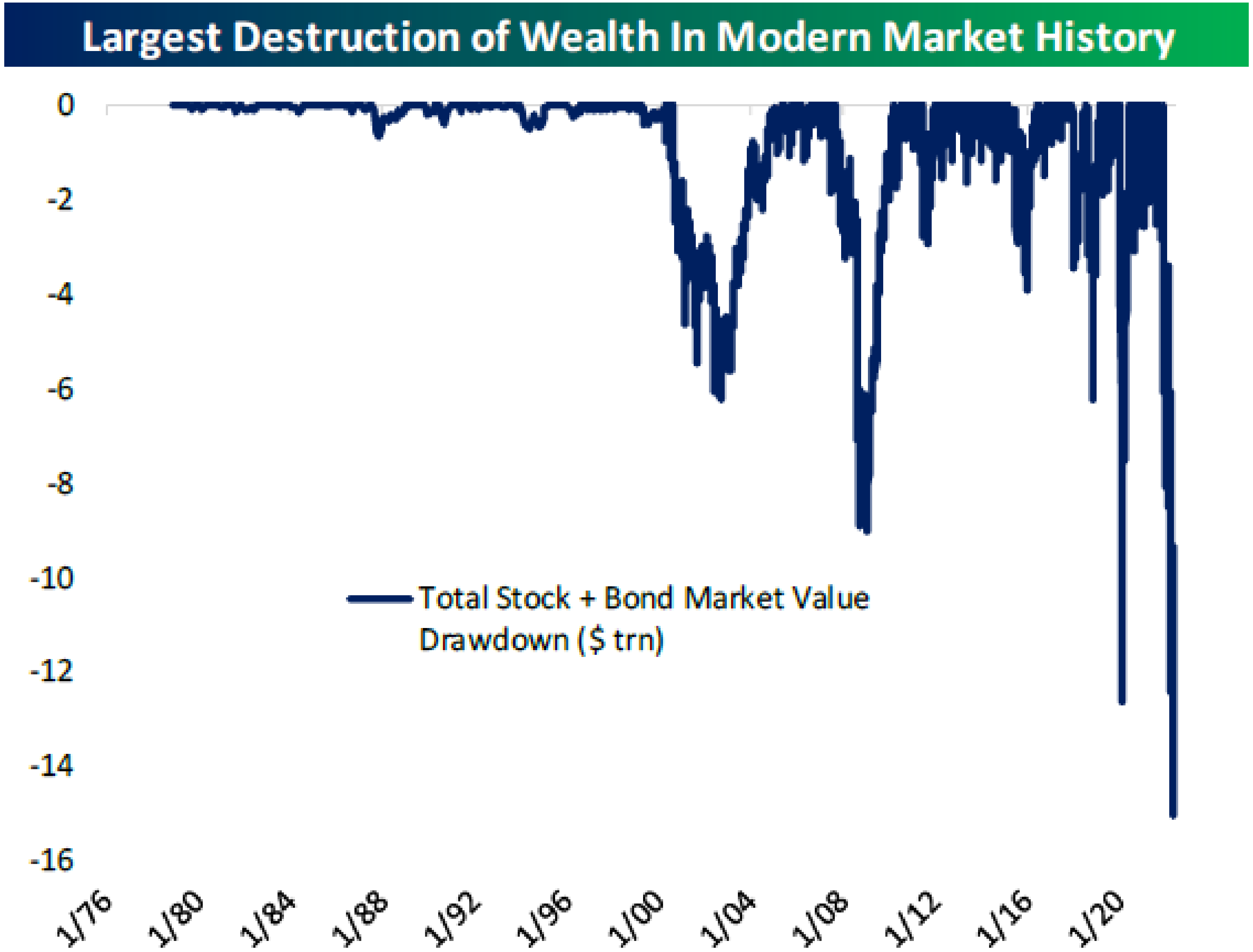
The Largest Wealth Destruction In History



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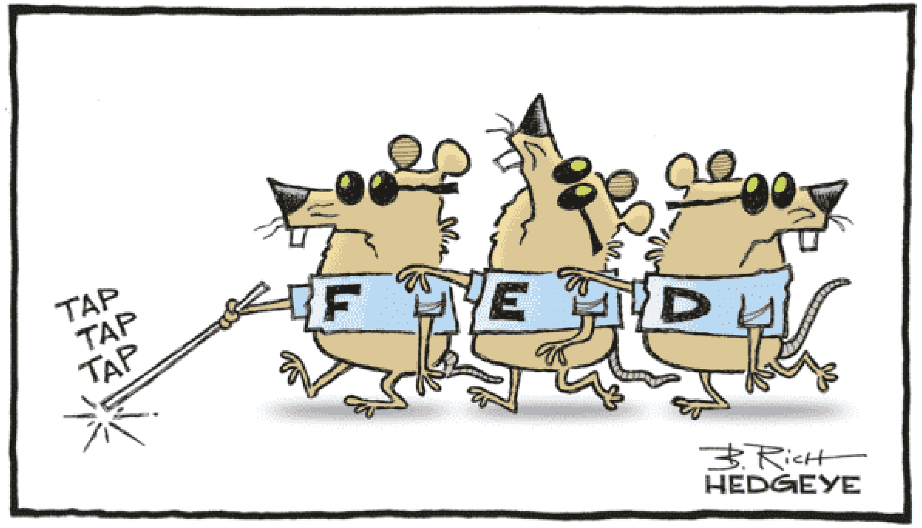
Can Central Banks Engineer A Soft Landing?

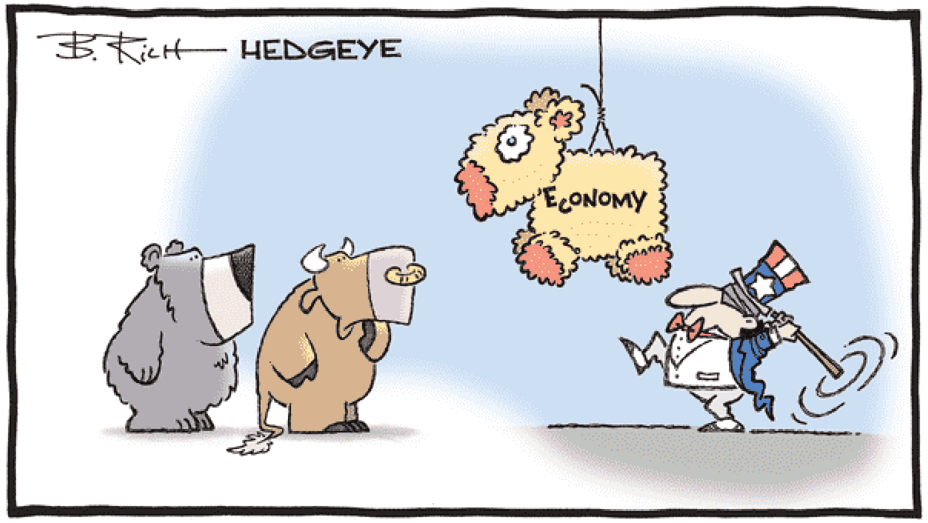
Central bank credibility is being questioned:

- In late 2021 the Fed was wrong on their inflation outlook, calling it transitory.
- In mid 2022 the Fed is saying they can manage a soft landing without a severe recession.
- In early 2022 the RBA said that interest rates in Australia would not rise until <u>2024</u>!
- Is there any credibility left for us to believe central banks can manage a soft landing?

The answer to this question will determine the market's direction heading into 2023.

<u>In our view – It is not a high probability outcome</u>.





MPW Outlook & Scenario Analysis For 2023 FY

1. Hard Landing: Global Recession MPW Probability = 70%	2. Soft Landing: Mid-Cycle Slowdown MPW Probability = 25%	3. Strong Growth: New Bull Market MPW Probability = 5%
• Inflation remains stubbornly high	• Inflation moderates towards targets	• Inflation moderates quickly
• Central banks tighten too much	• Central banks pause rate hikes	• Central banks consider rate cuts
• Unemployment rises 1-2%	• Unemployment rises marginally	• Employment growth remains strong
• Savings rates evaporate	• Savings rates are preserved	• Savings rates remain elevated
• Economic data deteriorates	• Economic data stabilises	• Economic data pivots to growth
• Corporate earnings fall	• Higher revenues offset higher costs	• Companies pass on higher costs
• Geopolitical risks intensify (wars)	• No further sanctions are imposed	• Russia and China pivot their stance
• Covid-19 resurgence hits mobility	• The “endemic” runs its course	• Supply chain & labour issues abate
Markets are not priced for this, expect another decline from here (~10-30%)	**Markets are priced for this, value can be selectively found at current levels**	**Markets are not priced for this, risky assets will perform very strongly**

US & Global Inflation At 40-Year Highs

There is some optimism around inflation peaking as commodity and food prices have softened recently, but surging wages and labour shortages will keep upward pressure on inflation

The Fed suggests inflation can be back at 2% by the end of 2023

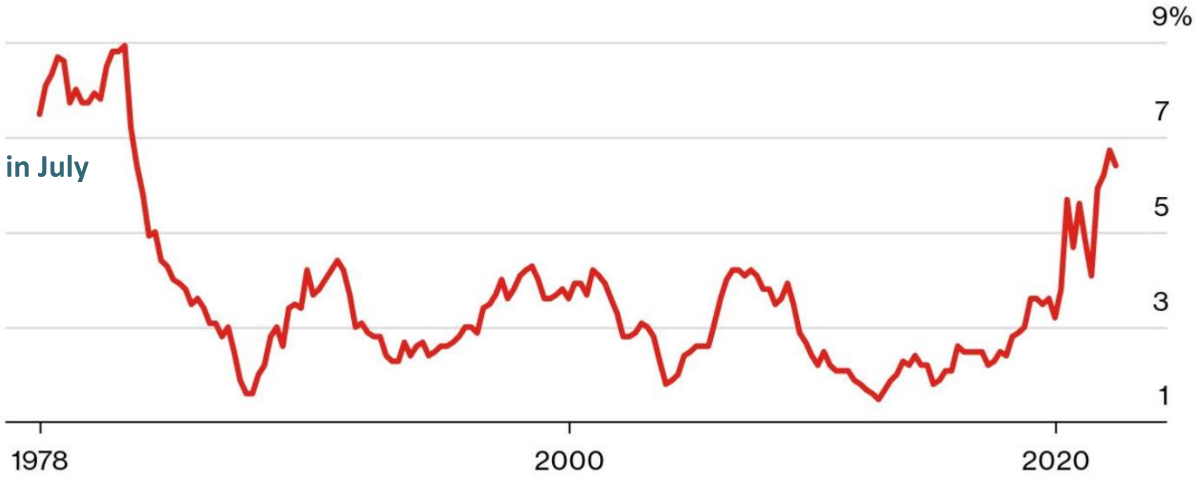
Year-over-year percentage change in the Consumer Price Index

Source: Bureau of Labor Statistics

But 'sticky' inflation such as wages and rents take time to fall

Wages Are Surging

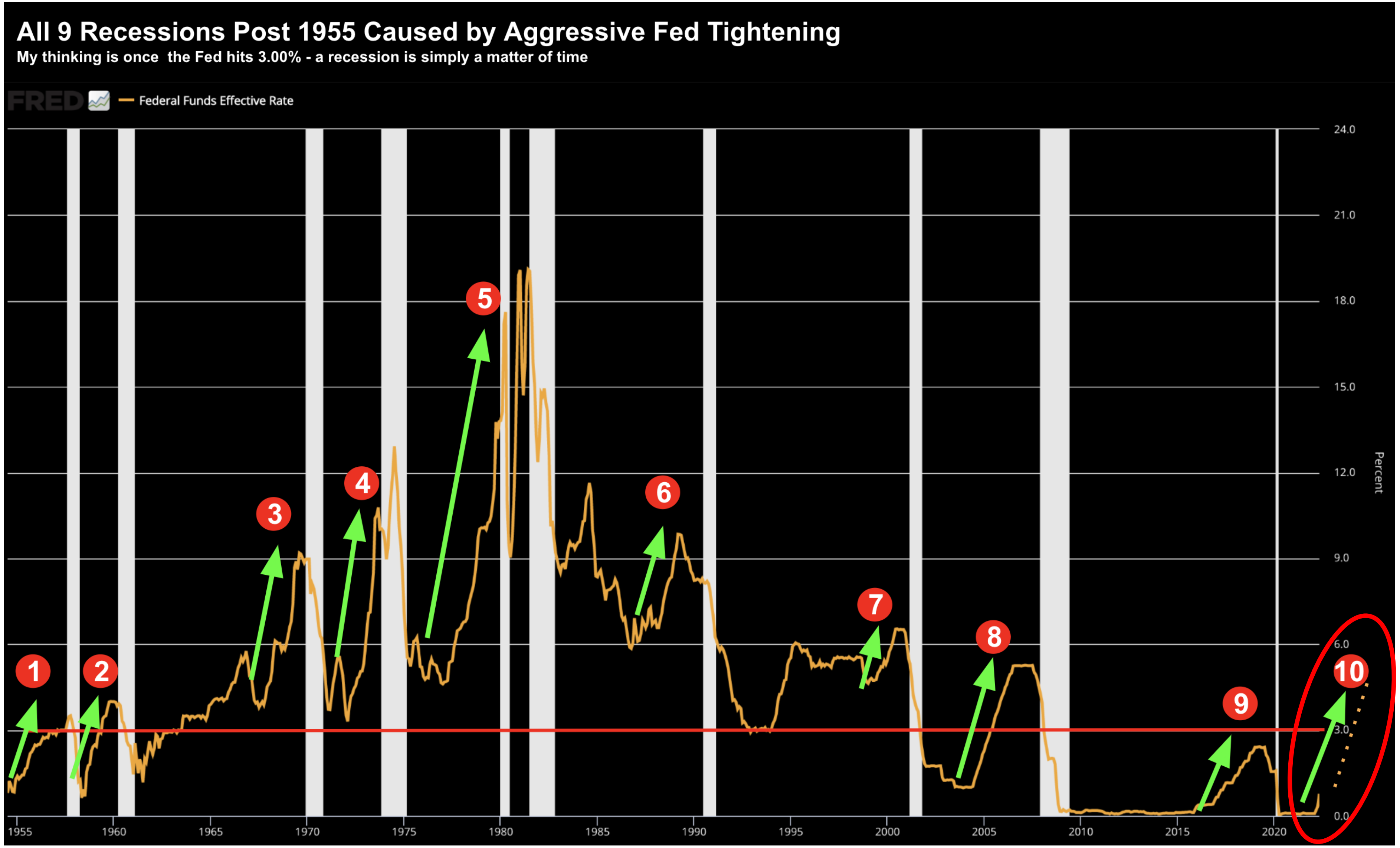
Annual average hourly earnings climb in tight US job market



Source: Bureau of Labor Statistics
Year-on-year change in private production and non-supervisory roles, charted by quarter

Bloomberg

Will Central Banks Cause A Global Recession?



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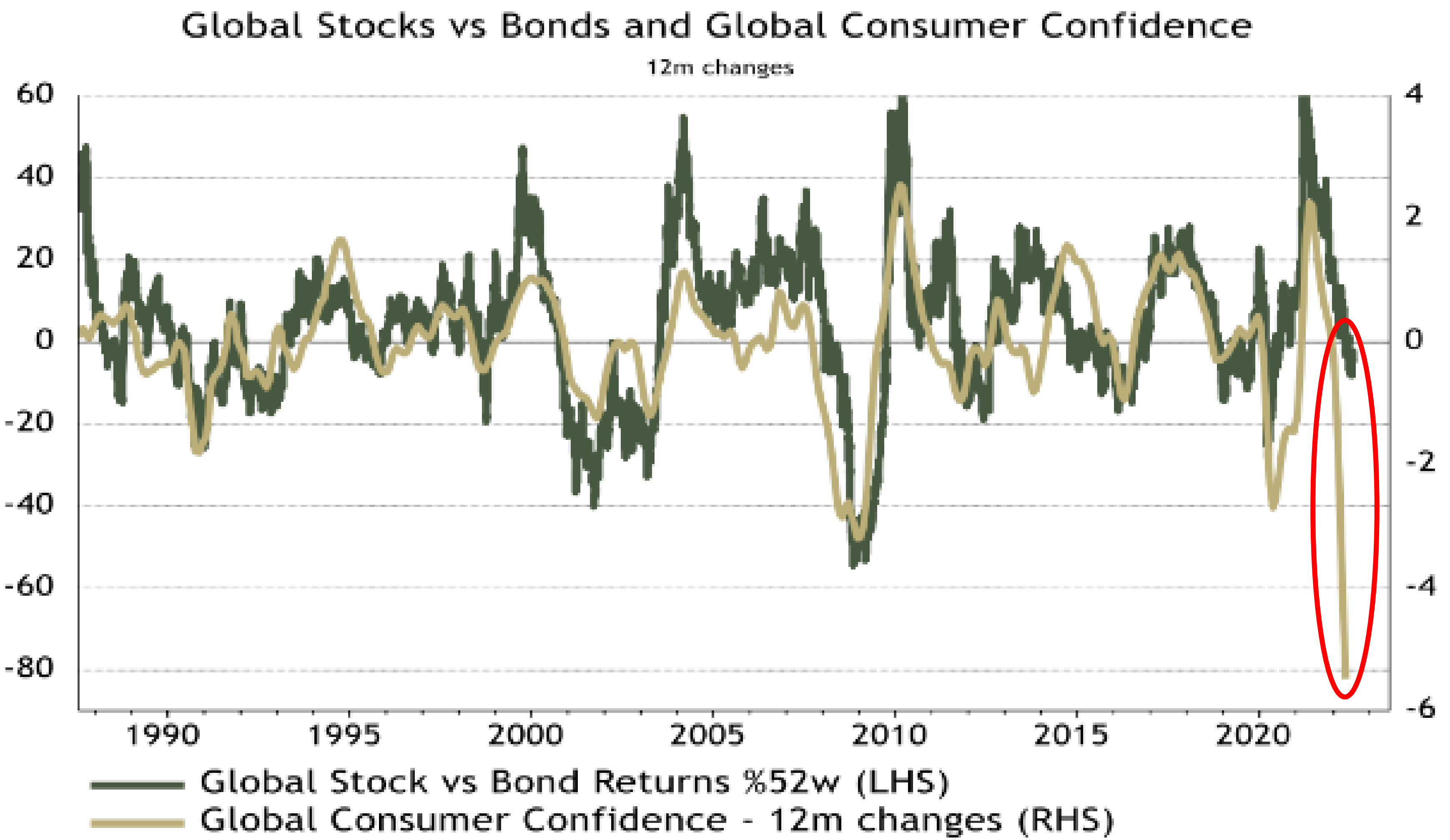
Consumer Confidence Has Collapsed, What's Next?



Source: ASR Ltd. / OECD / Refinitiv Datastream

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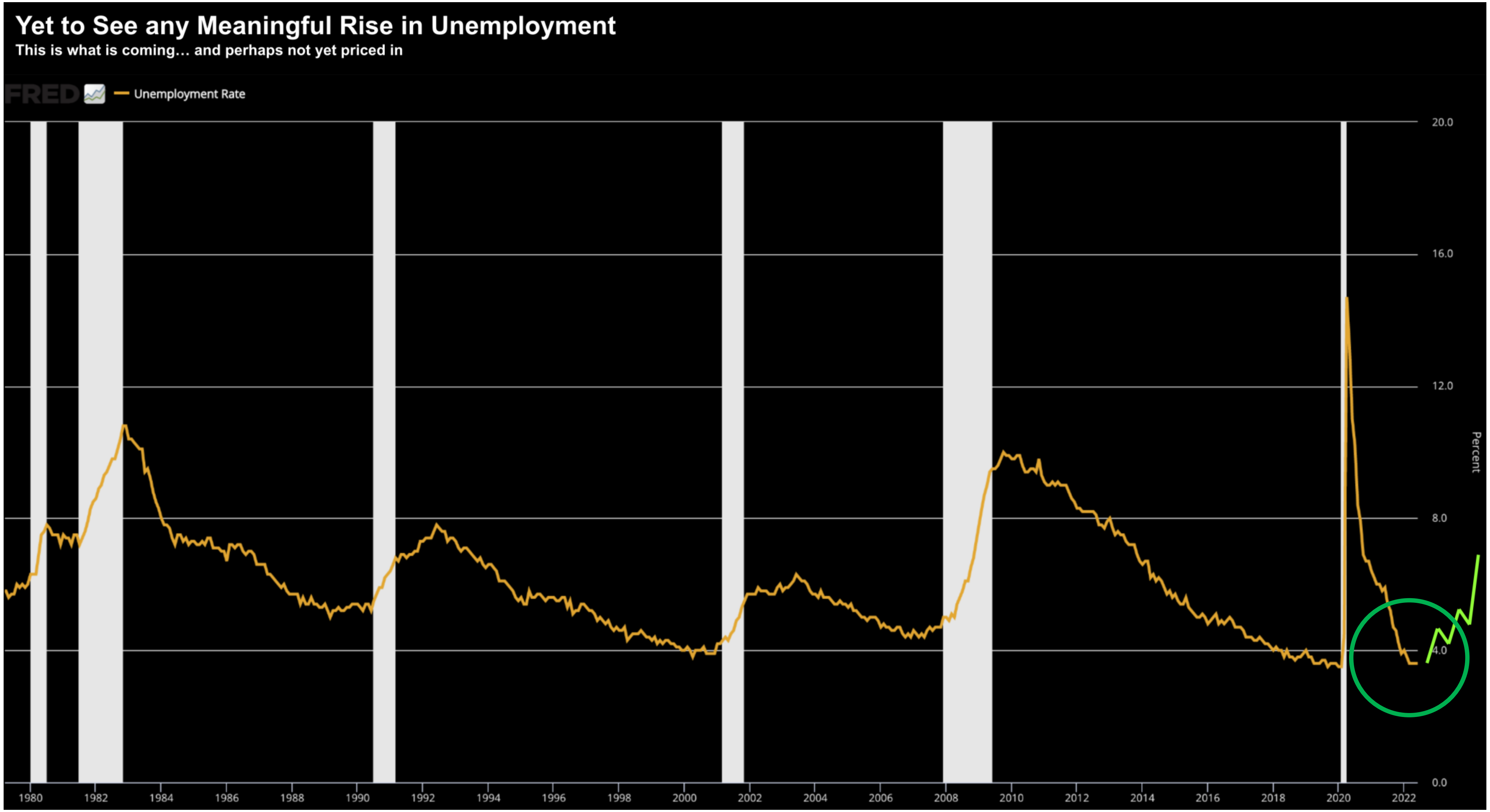
US Employment Growth Is Very Strong… For Now?



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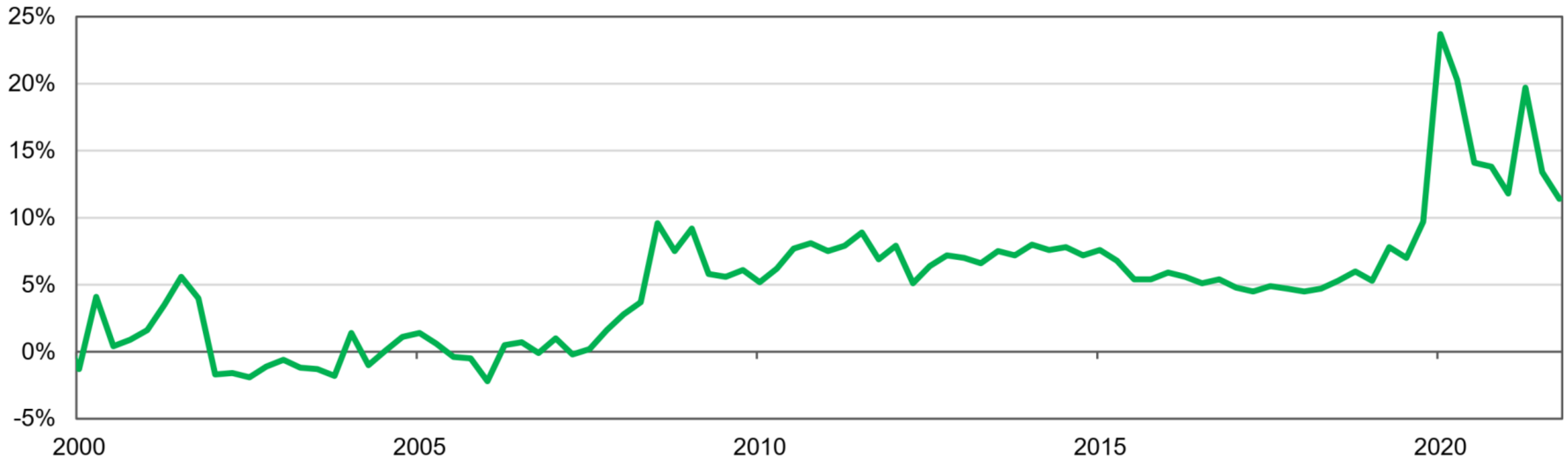
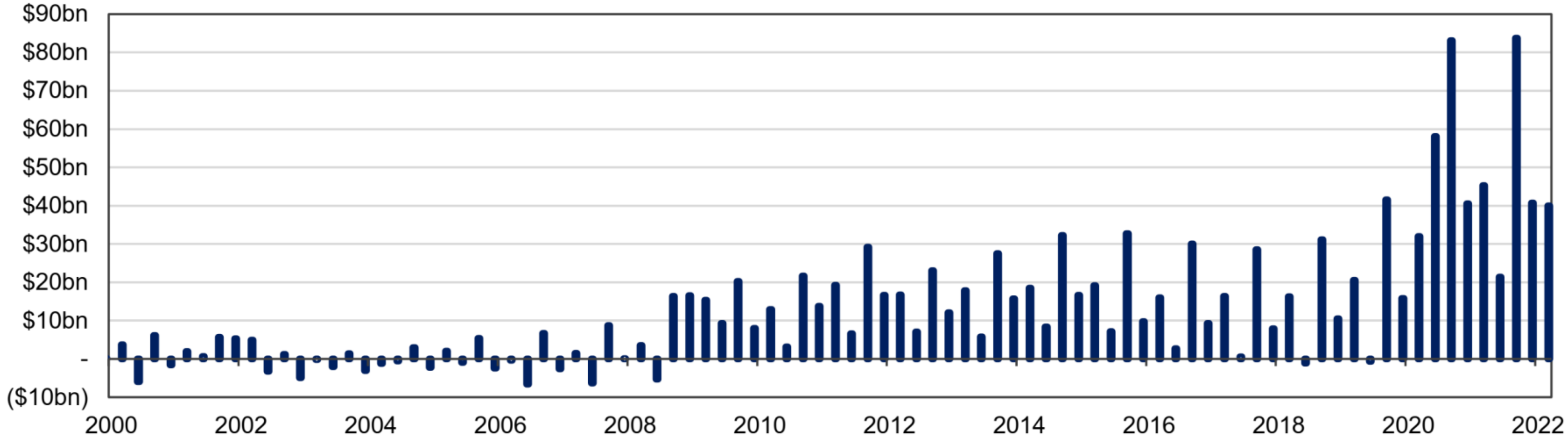
Household Savings Are High… But Falling

Household saving ratio (%)



Source: ABS, Auscap

Quarterly Net Household Saving ($bn)



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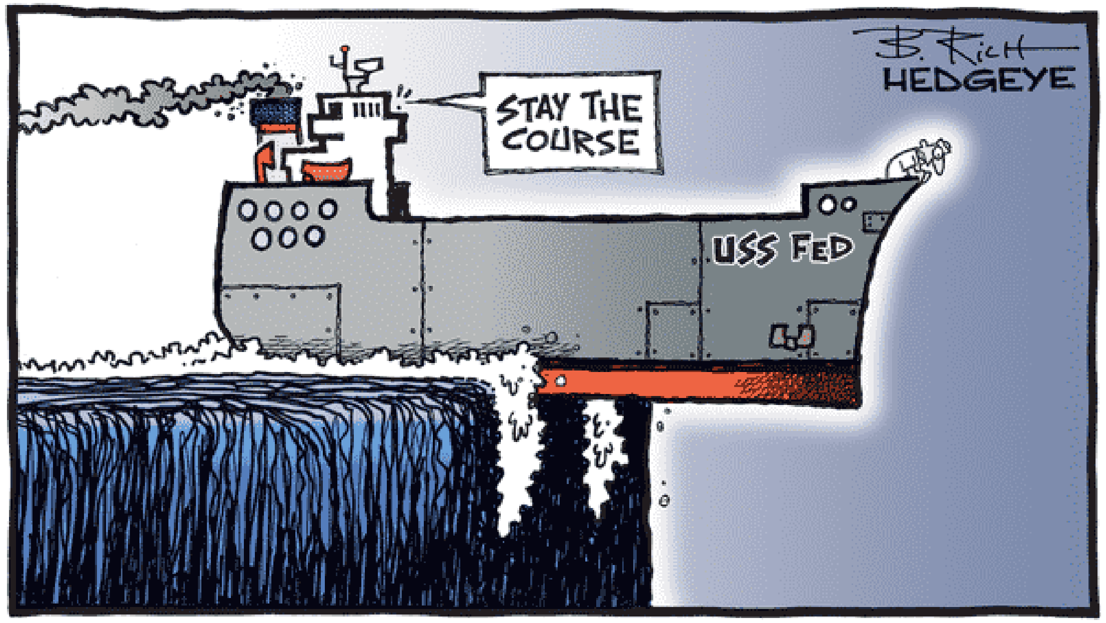
So What Does This Mean For Markets?

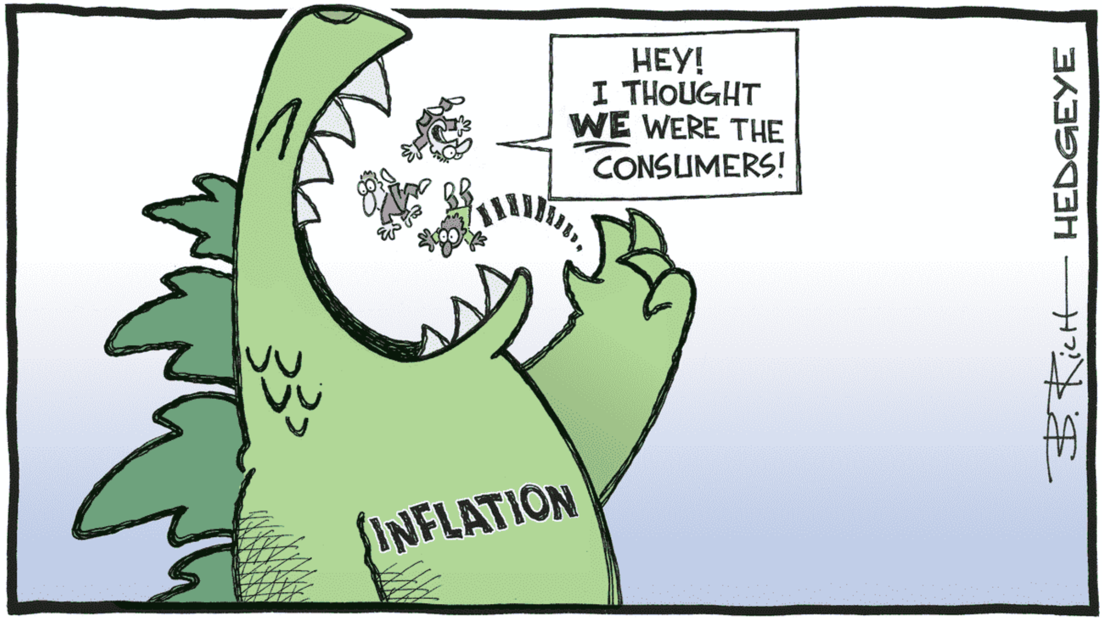
If central banks stay the course and fight inflation at all costs by aggressively raising interest rates, then it is hard to see the US economy avoid a deeper recession.

… BUT

If inflation declines on a sustainable basis, then the Fed will be able to 'pivot' and keep rates steady or even flag rate cuts. It is then a 'risk-on' environment.



VS



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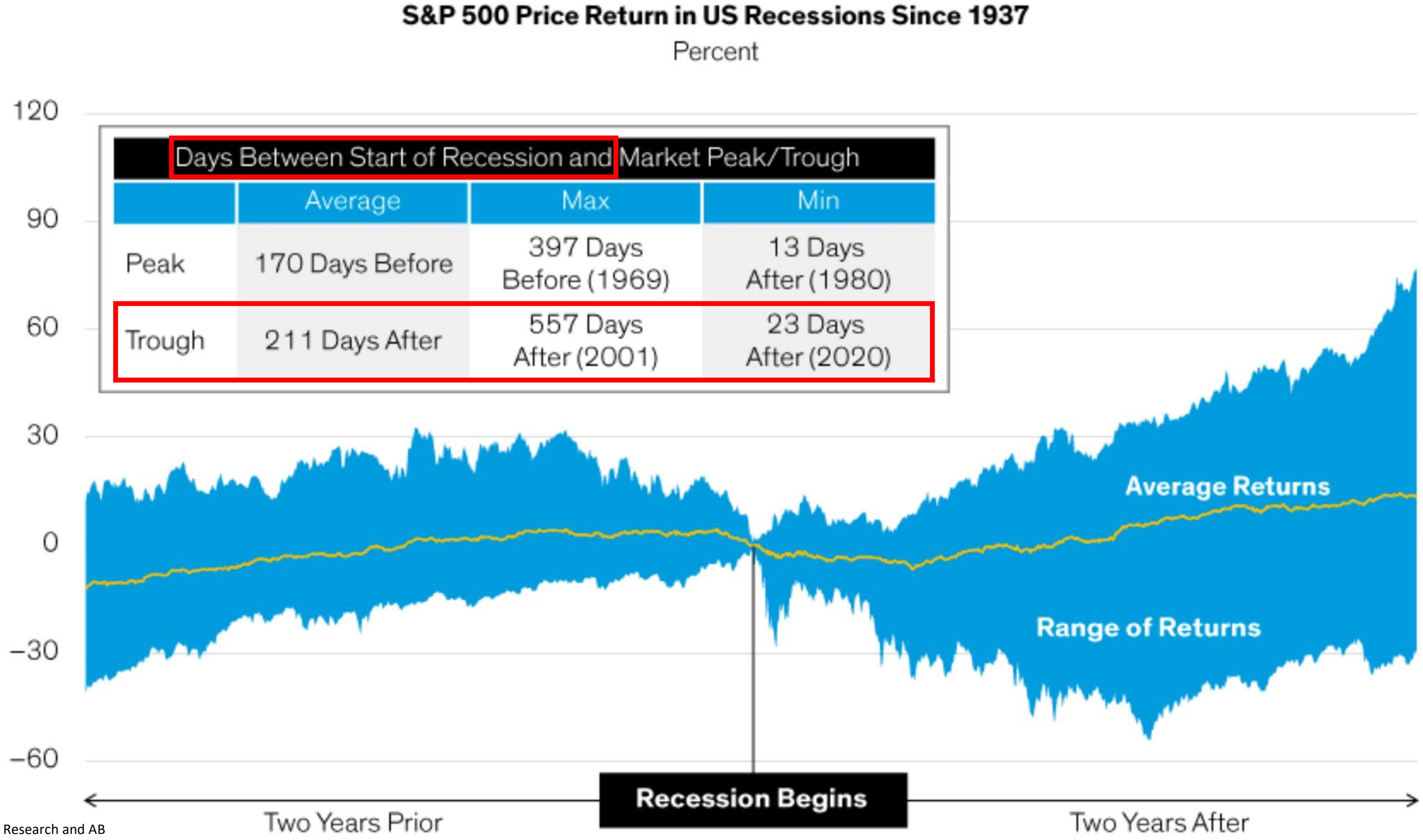
Timing Market Inflection Points Is Impossible

How Does the Market Respond to Recession?



Days Between Start of Recession and Market Peak/Trough			
	Average	Max	Min
Peak	170 Days Before	397 Days Before (1969)	13 Days After (1980)
Trough	211 Days After	557 Days After (2001)	23 Days After (2020)

As of June 30, 2022
Source: Bloomberg, National Bureau of Economic Research and AB

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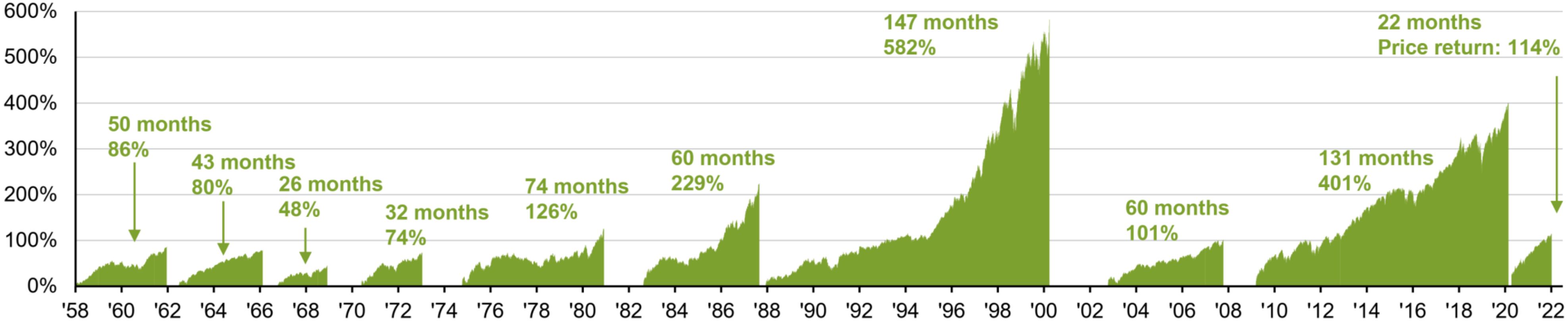
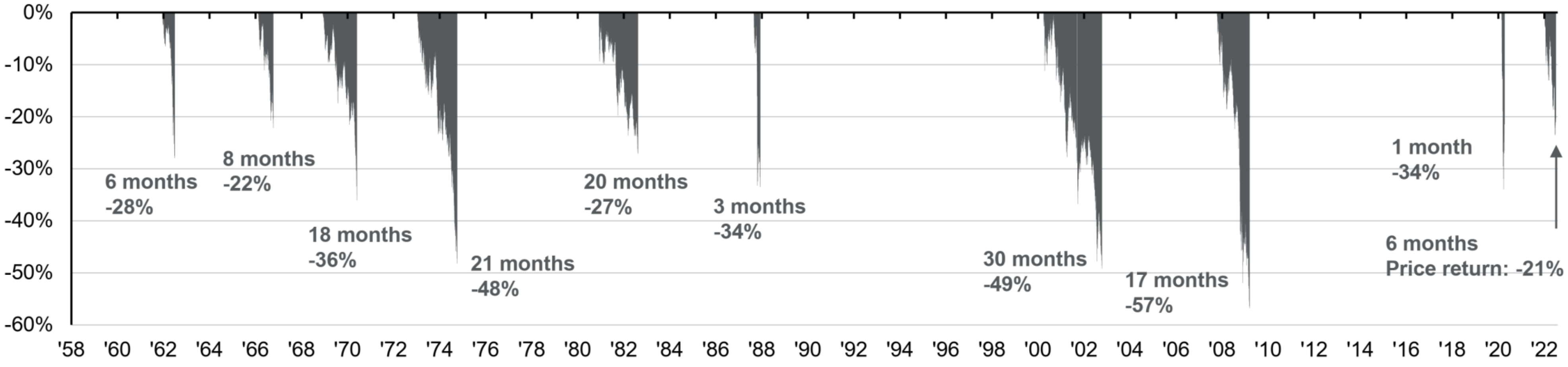
Bull and Bear Markets: Nobody Rings A Bell

S&P 500 bull markets



S&P 500 bear markets



Source: FactSet, Standard & Poor's, J.P. Morgan Asset Management.

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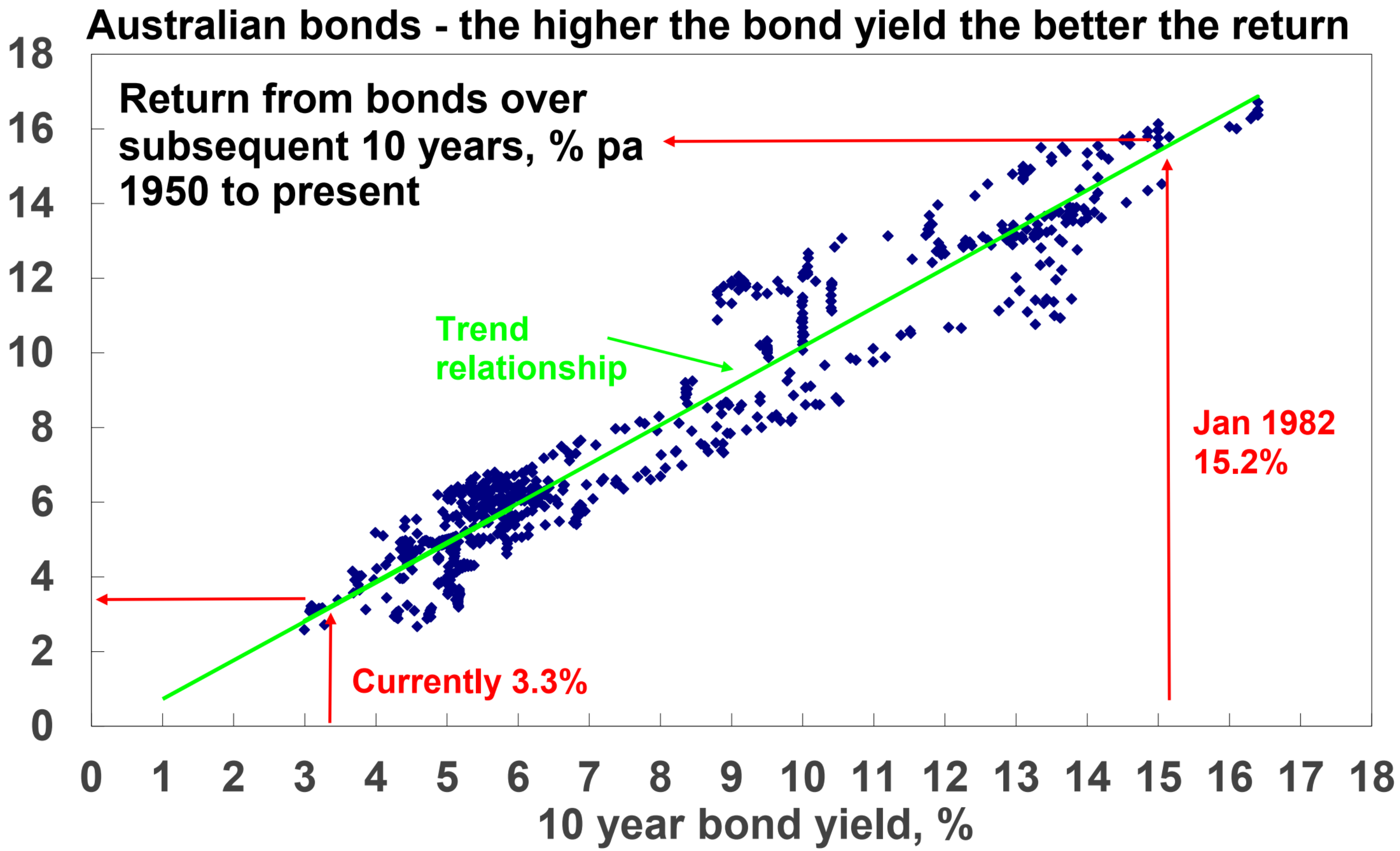
MPW Recommended Portfolio Strategy

Asset Class	Tactical Position	Comment
Currency (AUD vs USD)	Neutral	Neutral hedge at current levels, noting potential for full AUD hedge into 2023
Cash & Liquidity	Neutral to Over	Returns are ~1%, but increase cash tactically for buying opportunities/bond exposure
Government Bond Duration	Neutral to Over	Long-duration yields are above 3% pa and may provide a recession hedge/capital gains
Corporate Credit & Debt	Underweight	Listed credit spreads can widen further, but own selective private credit strategies
Listed Property & Infrastructure	Underweight	Listed markets are high risk, but own selective unlisted property/infrastructure assets
Australian Shares	Underweight	Long short exposure with a value bias, focus on quality and underweight small caps
International Shares	Underweight	US still expensive, developed and Emerging Markets cheap but represent high risk
Liquid Alternative Assets	Overweight	Equity market neutral, private debt and equity, commodities, and niche opportunities
Illiquid Alternative Assets	Overweight	Private debt and equity, niche illiquid strategies can provide a long-term return premium

Gov't Bonds Are Now A Hedge Against Recession



Source: RBA, Bloomberg, AMP Capital

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The Role of Alternative Assets In Portfolios

Framework-driven portfolio construction: What role do different categories play in the portfolio?

	Fixed income-like	Hybrids	Equity-like	
RETURN ENHANCERS Global diversification and tactical/ opportunistic returns	Distressed credit	Special situations	Private Equity, Venture Capital	LOWER Income/ HIGHER Volatility
CORE COMPLEMENTS Added diversification and/or enhanced returns	Corporate mezzanine loans	Hedge funds	Noncore real assets	
CORE FOUNDATION Stable Income with lower volatility, diversification ad inflation sensitivity	Core Private credit	Core real estate, infrastructure and transport	Low volatility core equity	HIGHER Income/ LOWER Volatility

= Overweight for the next 12 to 18 months

Source: JP Morgan Asset Management Alternative Solutions Group & MPW

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Vanguard & AMP Long-Term Return Expectations

The table below shows the **Vanguard Capital Markets Model return and volatility forecasts over the next 10 years** across four Global Diversified Portfolios.

Conclusion: Generating returns using just listed stocks and bonds will be much more challenging in the future and investors will need to take more risk for less return.

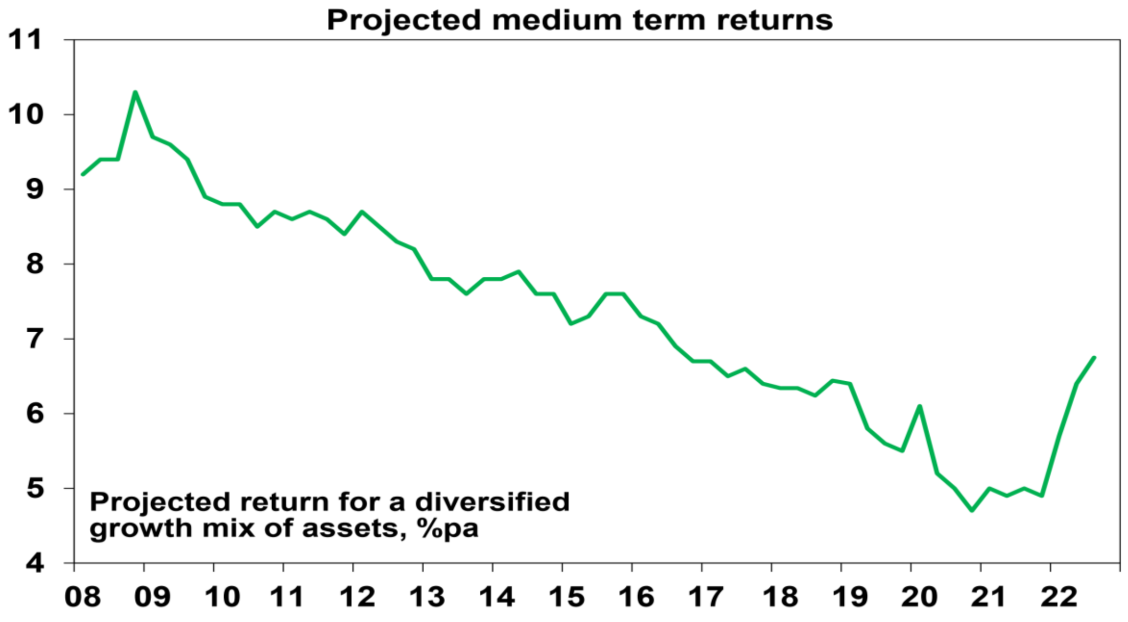
Note: The recent market sell-off has improved these numbers by more than 1% pa which is material over 10 years.

	Return Percentile					Volatility
	5th	25th	Median	75th	95th	Median
Conservative	2.5%	3.8%	4.7%	5.6%	7.1%	5.6%
Balanced	2.0%	3.9%	5.2%	6.6%	8.8%	8.9%
Growth	1.1%	3.7%	5.6%	7.5%	10.4%	12.4%
High Growth	0.0%	3.4%	5.8%	8.3%	12.0%	16.2%

Source: Vanguard, June 2022 using 30 May 2022 VCMM simulation.

The chart below shows **AMP Capital's return forecasts over the next 5-10 years** for their Diversified Growth Portfolio (~30% defensive and ~70% growth assets).

Conclusion: The recent fall in all asset prices means that future return expectations have increased to 6-7% pa.



Source: AMP

MPW Concluding Summary

Uncertainty remains: Can central banks manage a 'soft landing' or do they cause a deeper recession?

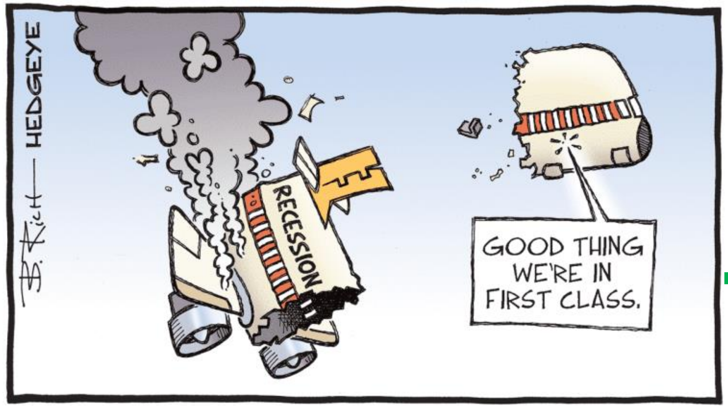
<u>Soft Landing Scenario</u>: *Markets have largely priced-in this outcome and have faith in the central banks.*

- We are at a critical market juncture that requires a cautious approach.
- **This outcome is <u>not our base-case</u>.**

Opportunities will exist if this scenario plays out… but (see below)

<u>Recession Scenario</u>: *Fighting inflation is the Fed's priority and markets have not priced-in the consequences of this.*

- A deep recessionary environment means risk assets fall much further.
- **This outcome is <u>our base-case</u>.**



Even better long-term opportunities will exist if this scenario plays out.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