Lonsec

Portfolio Perspectives

Insights from the CIO Office

August 2024

Key Messages for Investors

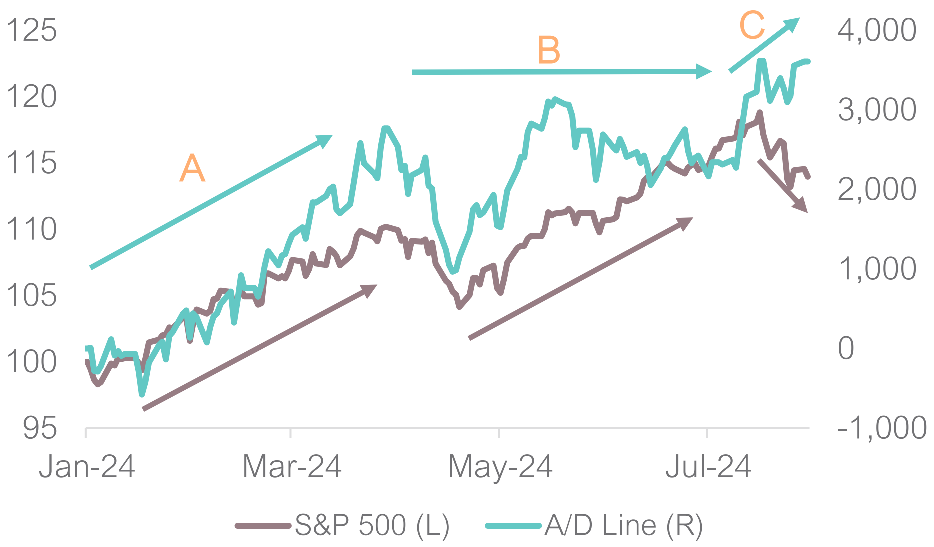
- Corporate profit growth is a strong predictor and driver of higher share prices.
- US reporting season so far is very encouraging for corporate profit growth.
- However, the risk/reward for the Magnificent 7 looks more skewed to the downside the higher they rise.
- There is evidence that the market is looking elsewhere for better value.

Look beneath the surface for better opportunities

Lonsec

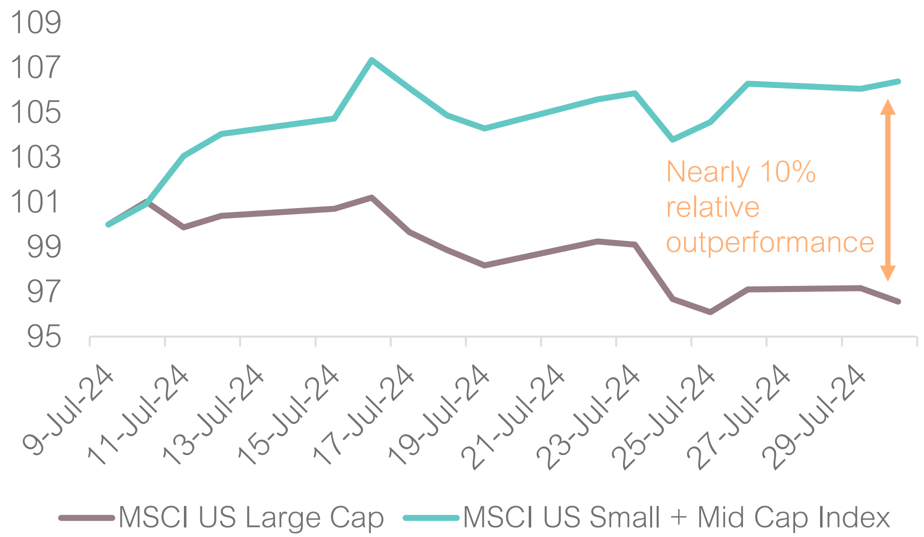
The market is signalling better risk/reward opportunities outside large capitalised stocks

Advance/Decline Line (A/D Line) technical indicator says look beyond the Magnificent 7



- The A/D line is a market breadth technical indicator. Section A shows broader market participation as the S&P500 rose. Section B shows the S&P500 kept rising despite breadth trending sideways reflecting the heavy lifting by the Magnificent 7. Section C shows despite the recent weakness in the Magnificent 7, the broader market continues to rise
- The conclusion is to look beyond the aggregate and dig beneath the surface to find value.
- This is clear from the S&P 500 Equal Weight index, which has risen over 1% since early July, compared to the S&P500 index, which has fallen over 3%.

Similarly there is a growing differential between large and smaller companies



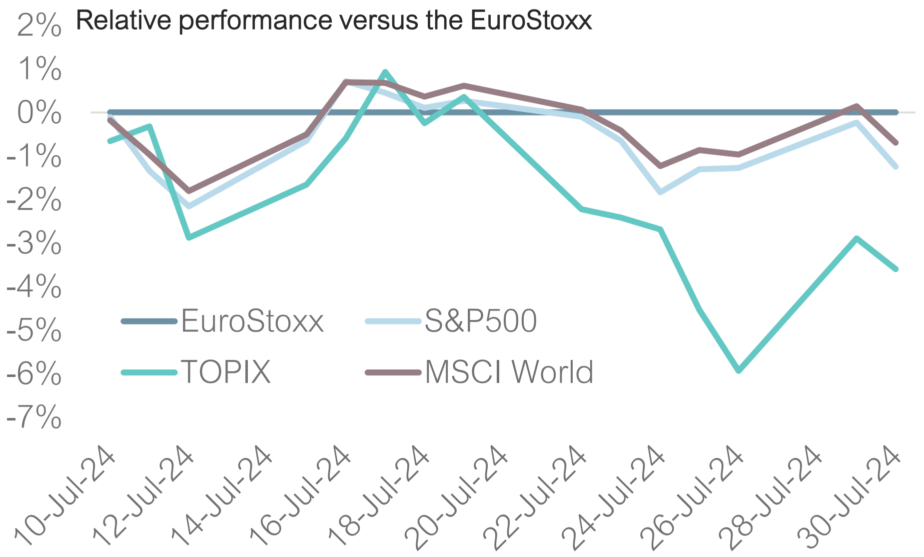
- Since early July, US smaller companies have outperformed US larger companies by nearly 10%. The same dynamic is playing out at a global level, with global smaller companies outperforming global large companies by 6%.

Source: FactSet, Lonsec estimates.

The case for Europe

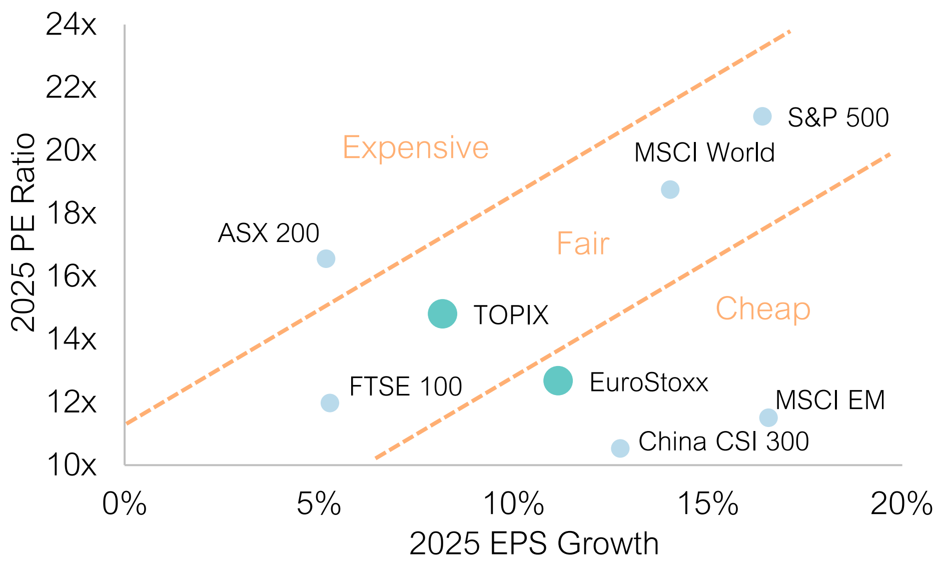
The dramatic shift to the political Right has not hurt European markets

Post the French elections, Europe staying ahead of other Developed Markets



- Concerns over a shift to the political Right have given way to the view that political fragmentation will slow, not accelerate, policy change.
- Japan's recent weakness stems from the Bank of Japan raising interest rates which is driving Yen strength. A stronger yen is a headwind for Japanese exporters (a key segment of the Japanese market).
- We believe the market is missing the point, normalisation of monetary policy was inevitable and reflects economic strength.

PE Ratio vs EPS Growth



- There is a strong linear relationship between prices for stocks and expected profit growth.
- Europe looks cheap given the forecasted profit growth.
- Japan's valuation also looks attractive compared to other developed markets, particularly considering that 2024 and 2025 earnings forecasts are rising. This makes the year-over-year earnings growth optically less appealing, but one must maintain sight of the underlying lift to aggregate profits.

Source: FactSet, Bloomberg, Lonsec estimates.

Outlook and Positioning

Becoming constructive on risk. Overweight DM Equities preferring Europe, Japan and US Small Caps. Reducing Cash. Don't ignore your Fixed Income allocations because risks remain.

Growth Assets	Underweight			Neutral	Overweight		
Australian Equities				●			
Large Caps				●			
Small Caps				●			
Developed Market (DM) Equities					●		
Large Caps				●			
Small Caps					●		
Emerging Market (EM) Equities				●			
Australian Listed Property				●			
Global Listed Property				●			
Global Listed Infrastructure			●				
Growth Alternatives				●			

Defensive Assets	Underweight			Neutral	Overweight		
Australian Bonds					●		
Global Bonds				●			
Diversified Income				●			
Conservative Alternatives				●			
Cash			●				

Growth Assets

- DM Equities. We are taking a constructive approach to risk and bringing the overall Growth/Defensive split back to Neutral by overweighting DM Equities funded by a reduction in Cash.
- DM Equities. The distortion caused by the Magnificent 7 in the US has us preferring Europe and Japan given more attractive valuations.
- DM Equities. DM Small Caps typically move ahead of the turn in the economic cycle, and US Small Caps, in particular, could move with the Fed starting its easing cycle. This leads to a Slight Overweight DM Small Caps with a preference for US over ex-US Small Caps.
- Global Listed Infrastructure. We see better risk/return opportunities in other asset classes for those seeking yield or capital appreciation.

Defensive Assets

- Australian Bond yields are now offering good value and bonds can once again play a defensive role in diversified portfolios. Focus on long-duration assets.
- Global Bonds. Supply/demand imbalances in the US treasury market remain a focus, reducing their relative preference versus Australian government bonds. The end of YCC policy in Japan should lead to an extended period of relative underperformance in Japanese Government Bonds.
- The potential start to an easing cycle reduces the relative attractiveness of floating rate yields.
- We maintain an allocation to gold which acts as a risk-diversifier against a further deterioration in economic conditions or escalation in geopolitical tensions.

Lonsec