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Chris Burrell's
Market View Blog

Market Outlook November 2024

The S&P/ASX 200 Index was up 2.1% for the four months to 31st October 2024. Most Burrell portfolios have started the year well and better than the index. The banks reported in line with expectations, with bad debts still at extremely low levels. Healthcare also reported well, while consumer staples underperformed, with poor updates during the quarter. Consumer spending is spluttering globally, primarily due to a reluctant consumer constrained by high interest rates, inflation particularly food and rent/housing costs together with a reluctance to spend in the current economic and geopolitical climate. Companies that reported below analysts' expectations were severely dealt with. These large market price falls on negative earnings surprises are a US phenomenon, we presume imported to Australia by the US merchants e.g Target US down 21% in a day after the retailer cut the profit outlook on weaker consumer spending. Higher end Target shoppers are apparently moving to Walmart!

Macro

The probability of interest cuts in Australia was reduced so that no interest rate cuts are expected in 2024 and several economists have moved their first cut from February 2025 to May 2025. An issue of increasing concern is future energy costs. Robert Gottliebsen commented that Australia is in an extended period of stagflation. "The stagflation of the 2020s will last a long time underwritten by high energy prices".

The outlook in the US is more positive than Australia with a soft landing still the central case i.e. that GDP will continue to increase, that interest rates will eventually fall albeit slowly and unemployment will not escalate too high.

Trump

The market has responded positively to the Republican win, with the stock market up and the bond market down. Key policy areas from a market perspective include:

- Trade policy shifts, with high tariffs
- Immigration reductions, resulting in lower population growth
- Government spending to be reduced
- Taxes lowered
- Less regulation

Historically one should be hesitant to be too definitive based on election promises. Lower US government spending could provide space for the private sector to grow, particularly given lower taxes and less regulation. What this means for the deficit depends on whether the ability to reduce government spending offsets government taxes. The impact on inflation from higher tariffs and less immigration is likely an increase. This will make the Fed more reluctant to reduce interest rates and more likely to hold. High tariffs are a lose/lose with China being punished for what the US sees as aggressive economic and military policies. In the first Trump administration, the tariffs led to bilateral deals between the various parties. For example, the USA is concerned that China is stealing its intellectual property. China could agree to strengthen its IP laws – it does have extensive IP laws, in return for lower tariffs. A likely loser in all scenarios is Australia, unless the Australian government can negotiate an exemption based on our free trade agreement and allied status. Trump's tariffs will fail dismally, as they did in his first term, but not before causing Australia collateral damage.

The extreme levels of government debt are so far troubling neither party in the US. With increased interest rates, the interest on the US government debt now exceeds the total US defence spending.

Valuations

Valuations in the US on average are above mean levels with the average PE 25x. These valuations are not uniform however and there are large parts of the market that show reasonable valuations.

The situation is similar in Australia although the banks look expensive and the resources sector less reliable going forward. We have already seen nickel collapse in Australian, due to Chinese sponsored Indonesian investment. There is concern that the Chinese sponsored Iron Ore development in Guinea, Africa will reduce Iron Ore prices over time. The mining sector in the US is not viewed with the same premium as in Australia, largely because many of the US mines are old and the ore grades are lower. Australia may be heading down this path, as mine lives are finite. In the US 'mining' is lumped in with 'materials' in the industry codes.

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Opportunities

Looking forward the likelihood of a stronger US dollar with higher inflation but stronger economic growth is the central outlook. While those companies earning US dollars are likely favored, technology valuations in particular look stretched due to the AI (Artificial Intelligence) momentum.

Burrell have recently adopted the Refinitiv data system from the London Stock Exchange Group (LSEG). This global information system provides not only pricing, but analysts' consensus both in Australia and internationally. We have upgraded our internal programs to provide in real time a cascading Burrell galaxy comparing market price to consensus expectations and this is a useful tool for both domestic and international portfolio stock selections.

US banks have reacted positively to the reduction in regulation, which will likely provide some wind back of the restrictions placed on the major banks after the global financial crisis. However Australian banks won't receive the benefits of the lower regulation and look unattractive relative to the US banking sector. In Australia, we are cautious on stocks dependent on the consumer. Banks look expensive. There remain a number of value and growth at reasonable price stocks across the broader industry categories. The banks are unlikely to assist with returns in the 2024/25 financial year and so it important for investors to have an open mind in terms of industries and stocks in broader industry categories.

With respect to international, it is recommended over time that portfolios increase their weightings by 5%. This can be done via LICs, exchange traded funds, managed funds and the BWET28 portfolio, a portfolio of 28 international stocks selected across various industry categories and with longer term returns.

Happy Investing!

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