Commentary
Model Portfolios

Q3 2024

For Financial Advisers/Wholesale Clients Only. Not for Distribution to Retail

State Street ETF Model Portfolios

- Global equity markets continued to grind higher despite pronounced market volatility.
- A resilient global economy and declining inflation rates encouraged central banks to adopt more relaxed monetary policies.
- Overall, global equities advanced in the third quarter, up 2.6%.[3]

Economic Perspective

- The global economy showed signs of resilience in Q3 2024, with growth in the services sector offsetting weakness in manufacturing. Although global business activity continued to expand in September, the rate of expansion slowed. There was notable divergence among the main economies: the United States (US), Japan, and United Kingdom all experienced growth, while Eurozone, Canada, and China showed signs of stagnation or contraction.

- The US Federal Reserve (Fed) finally pivoted with a larger-than-expected 50 bps cut in September. Market participants are now expecting an additional three 25 bps cuts by December 2024 and at least six cuts by June 2025. The European Central Bank also lowered its policy rates for the second time this year in September, following suit with the Swiss National Bank. Meanwhile, the Bank of England reduced its policy rate in August for the first time since 2020 and the Bank of Canada cut its policy rate for the third time this year. In Asia, while the Bank of Japan (BoJ) surprised markets with an interest rate hike at the end of July, the People's Bank of China announced substantial monetary policy easing measures.

- Domestic economic growth remained weak, with GDP expanding by just 0.2% in Q2, marking the worst performance in over 3 decades (excluding Covid). Business activities stagnated in September as slower services activity growth failed to offset a sharper downturn in manufacturing production. The headline inflation rate fell to 2.7% in August from 3.5% in July, the lowest level in almost three years and now within the Reserve Bank of Australia's (RBA) target range. However, core inflation, the central bank's preferred measure of the trimmed mean, remains above target leading the RBA to keep interest rates unchanged at its September meeting. Labour market conditions remained tight, although there are signs of gradual easing. The unemployment rate remained at 4.2% in August, up from the trough of 3.5% in mid-2023. But the participation rate remains at record highs, vacancies remain elevated and average hours worked have stabilised.

Asset Class Performance (in AUD)[1]

Equity

- **Equity markets** continued their upward momentum in Q3 2024 and have now risen for five months in a row. Equities experienced a volatile July, fluctuating in response to mixed economic data and geopolitical tensions. Early August saw a sharp decline due to escalating growth concerns and the BoJ interest rate hike. However, markets rebounded following positive US economic data that alleviated fears of a downturn. By September, global equities reached new all-time highs as global central banks rate cutting cycle gained traction, while the Chinese government's new stimulus measures to strengthen its economy propelled Chinese stocks higher. From a sector perspective, beneficiaries of rate cuts led — including real estate, utilities, and financials — while the year's first half leaders, communication services and information technology lagged (along with energy). Factor leadership also shifted in the quarter with minimum volatility, high dividends, value, and small cap leading, while momentum, quality, and growth (the year's first half leaders) lagged.

- **International equities** advanced, up 2.4%,[4] with the **multi-factor** (minimum volatility, quality, and value) strategy returning 3.0%.[5] Both **Minimum volatility** and **Value** outperformed, up 6.0%[8] and 3.0%,[6] respectively. While, **Quality** registered small negative return, down 0.2%.[7]

- **Australian equities** surged 7.8%[9] in Q3, posting its best September quarter since 2013, supported by easing inflation, soaring gold prices and optimism about a potential interest rate cut by the RBA. All sectors aside from energy and utilities posted positive returns but top performing sectors included information technology, real estate and materials.

- **Emerging markets** outperformed developed markets, up 6.5%,[10] driven by the announcement of new stimulus measures in China. Chinese policymakers announced significant measures to revive and stimulate its economy, mainly through interest rate cuts and government support for the ailing property market, boosting losing investor confidence.

Fixed Income

- **Bond yields,** which move inversely from bond prices, declined during the third quarter.

- **Global bonds** delivered strong returns during the third quarter, up 4.0%[11] driven by higher central bank interest rate cut expectations. Economic data releases continued to surprise to the downside on aggregate by the most since Q3 2021, leading to an increase in risk aversion and a supportive environment for bonds, especially as consumer inflation readings remained muted. **Global High Yield bonds** also rallied, up 5.2%.[13]

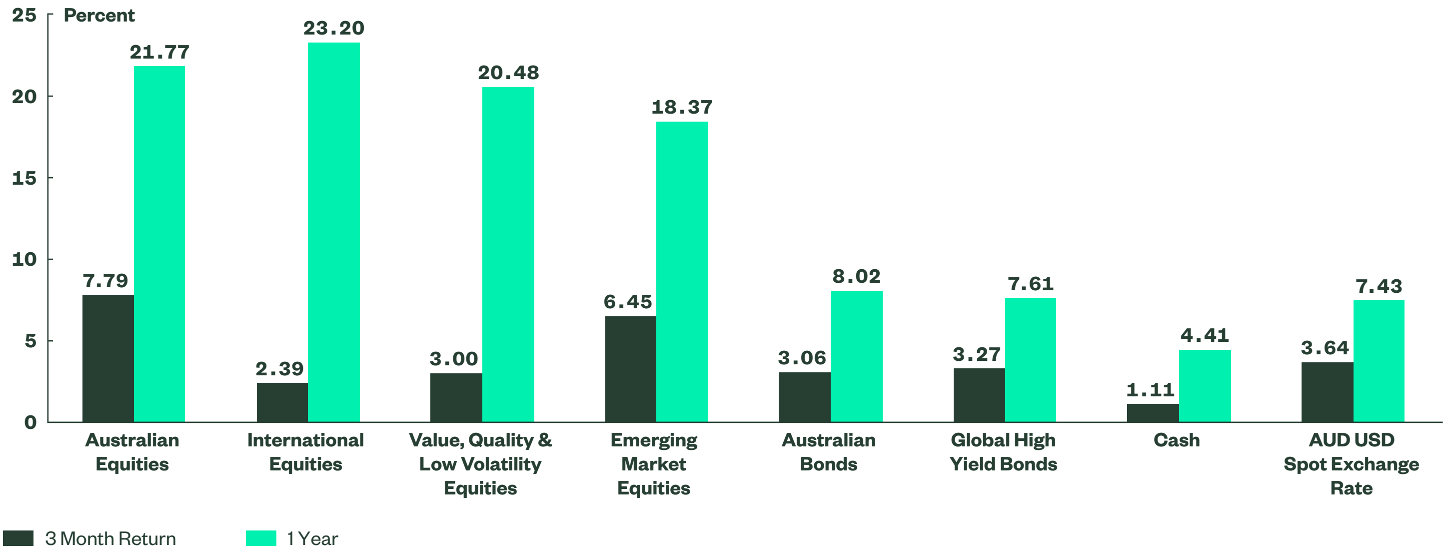
- **Australian credit bonds** returned positive, up 3.1%.[12] The Australian 10-year government bond yield fell from 4.31% at the end of Q2 to 3.97% at the end of Q3 2024,[15] amid growing speculation that the RBA is inching closer to the start of interest-rate cuts.

- **Cash** returns in the Australian money market were up 1.1%.[14]

Currency

- The **Australian dollar** appreciated against the US dollar, up 3.6%.[2]

Figure 1
Major Asset Class Performance (%)



Source: As of 30 September 2024, Bloomberg Finance L.P, MSCI. Index returns are unmanaged and do not reflect the deduction of any fees or expenses. The index returns reflect all items of income, gain and loss and the reinvestment of dividends and other income. Past performance is not a reliable indicator of future performance. Australian Equities = S&P/ASX 200 Total Return Index; International Equities = MSCI World Index (AUD) Net Total Return; Value, Quality & Low Volatility Equities = MSCI World Factor Mix A-Series (AUD) Net Return Index; Emerging Market Equities = FTSE Emerging Markets All Cap China A Inclusion Net Tax Index (AUD); Australian Bonds = Bloomberg AusBond Credit 0+ Yr Index; Global High Yield Bonds = S&P/ASX Australian Fixed Interest Total Return Index; Cash = S&P/ASX Bank Bill Total Return Index.

Strategy Performance

State Street Risk-Based ETF Model Portfolios

For the third quarter of 2024, all equity components contributed positively to the risk-based portfolios' total return.

The portfolio's allocation to domestic equities was the primary driver of total performance, as stocks climbed higher on the back of easing inflation and optimism surrounding potential rate cuts. The materials sector benefitted from rising bullion prices and new stimulus measures in China, while interest-rate sensitive real estate shares surged amid declining yields. Conversely, the energy sector detracted from performance as crude prices fell due to concerns about global economic health. The portfolios' multi-factor international exposure, SPDR MSCI World Quality Mix Fund (QMIX) also recorded positive returns for the quarter, with both minimum volatility (+6.0%)[8] and value (+3.0%)[6] factors rising. Additionally, the emerging market equity exposure contributed positively to the total returns, bolstered by strong performance in these markets following the announcement of new stimulus measures in China.

On the fixed income side of the ledger, both Australian government and credit bond exposure positively impacted the risk-based portfolios' total return. Domestic bonds delivered gains as treasury yields rose and spreads tightened.

State Street Moderate ETF Model Portfolio overall performance of the hypothetical model portfolio for the quarter was up 3.93%.

State Street Balanced ETF Model Portfolio overall performance of the hypothetical model portfolio for the quarter was up 4.17%.

State Street Growth ETF Model Portfolio overall performance of the hypothetical model portfolio for the quarter was up 4.44%.

State Street High Growth ETF Model Portfolio overall performance of the hypothetical model portfolio for the quarter was up 4.69%.

State Street Target Income ETF Model Portfolio

The State Street Target Income ETF Model Portfolio is designed with an income objective that is determined on an annual basis. For the 2023/2024 financial year the portfolio aims to target, before expenses, an income objective of 4.5% per annum.

The portfolio's allocation to both Australian and International high dividend stocks had a positive impact to the portfolio's total return. Within international exposure, financials, utilities and rate-sensitive real estate stocks drove the performance. In domestic equities, cyclical stocks advanced, with consumer discretionary stocks leading the gains as retail sales grew. Materials, particularly metal and mining shares rallied due to China's stimulus and rising bullion prices, while financials stocks also made a significant contribution.

On the fixed income side of the ledger, all three exposures — government, investment grade and high yield bonds — delivered positive returns. Bond prices rose during the quarter as yields declined and credit markets spreads narrowed.

The income portion of the portfolio's total return for the quarter was positive 0.78%, supporting the portfolio's primary objective to generate income.

Overall performance of the hypothetical model portfolio for the quarter was up 5.19%.

Past performance is not an indicator of future performance.

Model Portfolio Performance presented above is hypothetical and has been provided for illustrative purposes only. State Street's model portfolios are accessed through a Platform or Managed Accounts provider ("Provider"). The actual results of accounts managed by the Provider that receives access to the models may differ substantially from the hypothetical results of a model for a variety of reasons including, but not limited to, the Provider's decision to exercise its discretion to implement a model in a way that differs from the information provided by State Street.

The hypothetical State Street ETF Model Portfolio Total Returns reflect the investment strategy decisions made by State Street's investment professionals for each performance period presented. Returns greater than one year are annualized. The performance was achieved by mathematically combining the actual performance data of the underlying ETFs multiplied by the model portfolio weights allocated to each ETF on a monthly basis. The performance assumes that all distributions paid by the underlying ETFs were reinvested but does not reflect trading fees, spreads or broker commissions for the hypothetical sale and purchase of the underlying ETFs or any other fees which would be charged by the product provider.

State Street has chosen to use the actual historic performance of the underlying ETFs rather than the underlying ETFs index performance to ensure that the model portfolios reflect, as closely as possible, any actual investments that follow the model portfolio strategy, by reflecting differences such as tracking error of the underlying ETFs relative to the underlying ETFs indices.

Endnotes

1 All returns as at 30 September 2024. Index returns reflect capital gains and losses, income, and the reinvestment of dividends. Index returns are unmanaged and do not reflect the deduction of any fees or expenses. The index returns reflect all items of income, gain and loss and the reinvestment of dividends and other income. Past performance is not a reliable indicator of future performance.

2 Source: Bloomberg, AUD USD FX rate.

3 Source: MSCI All Country World Net Total Return AUD Index.

4 Source: MSCI World Net Total Return AUD Index.

5 Source: MSCI World Factor Mix A-Series (AUD) Pacific Net Total Return Index in AUD.

6 According to MSCI World Value Weighted Net Total Return Index in AUD.

7 Source: MSCI World Quality Net Total Return Index in AUD.

8 Source: MSCI World Minimum Volatility (AUD) Net Total Return Index.

9 Source: S&P/ASX 200 Total Return Index.

10 Source: FTSE Emerging Markets All Cap China A Inclusion Net Tax Index (AUD).

11 Source: Bloomberg Global Aggregate Total Return Hedged AUD Index.

12 Source: S&P/ASX Australian Fixed Interest — Total Return Index.

13 Source: Bloomberg Global High Yield Total Return Index Hedged AUD.

14 Source: Bloomberg AusBond Bank Bill Index.

15 Source: Bloomberg, Australia Govt Bond 10 Year Yield.

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