2021 calendar year in review

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The global economy continued to recover in 2021 but is still being challenged by rising virus cases as well as high inflation and persistent supply disruptions.

The pandemic's path evolves from Alpha to Delta to Omicron

For the second year running, the pandemic was the key health and economic concern. The opening months of 2021 brought both pain and promise. A rapid acceleration in virus cases across the globe saw constrained economic activity. However, there were rays of sunshine with the rollouts of the AstraZeneca, Moderna and Pfizer vaccines. Rising vaccination rates during 2021 allowed global economic activity to recover. Employees have been able to return to workplaces and even bars and restaurants started to re-open.

Yet all nations are not equal in vaccine access. Australia's fully vaccinated rate at 77% of the total population compares to Indonesia's 41% and only 9% for Africa at the end of 2021. The virus has also evolved with a more contagious variant in Omicron in late 2021. This adds to the list of Alpha, Beta, Gamma and Delta that have proven so dangerous over the past two years. The virus remains a threat as we enter the third year of this pandemic.

The 2021 report card for the global economy was mixed. The US economy saw a solid recovery in 2021 with improving jobs growth and the unemployment rate falling from 6.7% to 3.9%. Europe's recovery has been a 'stop-start' sequence with lockdowns in early 2021, then a brief rebound until Omicron ended the year on a troubling note. China's sharp economic slowdown and the financial woes of their property developers also filled the headlines in 2021.

Low interest rate settings by central banks and government budget measures provided tremendous support for global economic activity in 2021. However, there is concern that with rising inflation and high budget deficits, this policy support is not sustainable.

Commodity prices had some tumultuous twists and turns during 2021. Iron ore started the year in 'boom' conditions. The spot iron ore price surged from US$156 to US$230 per tonne in May given high levels of global steel production. However, China's sharp economic slowdown and property development woes then saw demand slump. Iron ore prices ended the year around US$112 per tonne which is a 28% annual decline.

Consumers experienced the commodity gyrations in their weekly visits to supermarkets and service stations. In Australian dollar (AUD) terms, global coffee prices surged 82%, sugar by 28%, bacon by 22% and wheat prices for your daily bread rose by 26%. Oil prices skyrocketed by more than 56%.

Given this commodity price spiral as well as congested supply chains with the shortage of computer chips and container ships, rising inflation has also become a key economic and social concern this year. Global annual inflation measures surged to multi-year highs in 2021. US consumer inflation ended 2021 at 7% which is the highest since 1982. European inflation was 5% while Brazil's inflation surged to nearly 11%.

Australia's consumer inflation was running at 3% in the year to September 2021. This 3% inflation rate still represents a loss of purchasing power. For Australian savers, the current 0.1% nominal cash rate by the Reserve Bank of Australia provides minimal compensation for inflation. Australian workers are also feeling the squeeze with wages growth barely above 2% in 2021. While share investors have had a 'very good year', spare a penny for employees and savers reliant on income yields.

Australia's economy had a rollercoaster year in 2021. There were encouraging gains in economic activity up until mid-2021. However, the virus outbreaks in NSW and Victoria in June then saw the Australian economy hit reverse gear. Since October, there have been more promising signs. Employment and retail spending have recorded sharp gains after NSW and Victoria emerged from lockdowns. Yet the surge in virus infection cases in the closing weeks of December are a troubling reminder of the continuing virus threat entering the new year.

A remarkable year for investment returns

Asset class returns in Australian dollars – periods to 31 December 2021

Asset class	Returns			
	1 yr	3 yrs (pa)	5 yrs (pa)	10 yrs (pa)
Cash	0.0%	0.6%	1.1%	1.9%
Australian bonds	-2.9%	2.9%	3.4%	4.2%
Global bonds (hedged)	-1.5%	3.5%	3.2%	4.6%
Australian property securities	26.1%	12.8%	9.3%	13.8%
Global property securities (hedged)	28.6%	10.4%	6.9%	10.5%
Australian shares	17.5%	14.0%	9.9%	10.8%
Global shares (unhedged)	25.8%	19.1%	14.3%	15.8%
Global shares (hedged)	20.9%	20.3%	14.0%	13.0%
Emerging markets (unhedged)	3.4%	9.8%	9.8%	9.2%

Past performance is not a reliable indicator of future performance.

Sources: FactSet, MLC Asset Management Services Limited. Benchmark data: Bloomberg AusBond Bank Bill Index (cash), Bloomberg AusBond Composite 0+ Yr Index (Aust bonds), Bloomberg Barclays Global Aggregate Index Hedged to $A (global bonds), S&P/ASX200 A-REIT Total Return Index (Australian property securities), FTSE EPRA/NAREIT Developed Index (net) hedged to $A (global property securities), S&P/ASX300 Total Return Index (Aust shares), MSCI All Country World Indices hedged to $A and unhedged (net) (global shares), and MSCI Emerging Markets Index (net) unhedged to $A (emerging markets).

Global share investors had a rewarding year with a market return of 26% for unhedged and 21% for AUD hedged portfolios. The primary drivers of this very strong global share performance were surging corporate profits and supportive low interest rates.

Extraordinary US share gains were the key contributor with the benchmark S&P 500 delivering a 28% return. Wall Street made new record highs given robust corporate profit results. Corporate profits are expected to rise by 45% in 2021. Strong business surveys and job gains also provide encouragement that the US economic recovery is progressing.

Yet there have been some dark clouds amidst the blue skies for share investors. Brazilian share prices declined by nearly 22% given rising inflation and interest rates. Chinese share prices fell by 22% through a combination of increasing government regulation of education and technology companies as well as the debt woes of property developers such as Evergrande.

Australian shares as represented by the ASX 300 delivered a strong 18% return for 2021. The Communication Services (33%) and Financials (ex A-REIT) (25%) sectors led the charge. There were some exceptional share gains from mining companies in Lynas (156%) and South32 (66%) as well as Sonic Healthcare (48%) and Telstra (46%). However, there were some notable disappointments with sharp falls recorded for Magellan (-57%) and AMP (-35%).

Bond investors had a tough year with negative returns given rising inflation and concerns that central banks are set to raise interest rates in 2022. The Australia fixed interest market return came in at -3% for 2021 while the benchmark global bonds (hedged) return was -2%.

Prospects for 2022

The global economy continued to recover in 2021 but is still being challenged by rising virus cases as well as high inflation and persistent supply disruptions. So central banks, governments, as well as investors face considerable challenges in balancing the potential rewards versus the risks.

The promising prospect of vaccinations ending this pandemic in 2022 needs to be weighed against a wide array of potential risks. These risks could involve further dangerous virus variants emerging, global political risks escalating (eg Russia/Ukraine as well as China/Taiwan tensions) and persistent inflation pressures requiring sharply higher interest rates. There can also be major events that shock and surprise investors which are not currently on our radar screen.

MLC believes that maximising returns over time is about getting the balance right between understanding opportunities and managing risks. MLC's 'participate and protect' investment philosophy aims to gather returns from a diverse range of assets while also keeping a watchful eye out for any potential setbacks.

As 2021 has shown with the destructive path of COVID-19, gradual vaccine rollouts and rising inflation – keeping your balance is a continual challenge.