

MARCH 2020

- ▶ Despite a reasonably robust underlying economy, the impact of the coronavirus is likely to weigh heavily on the US and other China-exposed economies.
- ▶ The Australian government is preparing to release a targeted fiscal stimulus response to support economic growth and avoid a recession.
- ▶ Geopolitical and trade tensions have been forced out of the spotlight, but they remain live issues that could re-emerge as the US presidential race begins.
- ▶ Rate cuts from central banks in response to the coronavirus will be limited in addressing supply-side issues impacting the global economy.
- ▶ As the UK negotiates a trade deal with Europe, Prime Minister Johnson said he will not seek an extension if an agreement is not reached before 31 December.

February market performance

Equity Markets – Index Return*	Index	At Close 29/02/2020	% Return 1 Month	% Return 12 Months
Australia	S&P/ASX 200 Index	6441.20	-7.69%	8.64%
United States	S&P 500 Index	2954.22	-8.23%	8.19%
Japan	Nikkei 225 Index	21142.96	-8.82%	0.98%
Hong Kong	Hang Seng Index	26129.93	-0.38%	-5.37%
China	CSI 300 Index	3940.05	-1.59%	9.81%
United Kingdom	FTSE 100 Index	6580.61	-8.99%	-2.66%
Germany	DAX 30 Index	11890.35	-8.41%	3.25%
Europe	FTSE Eurotop 100 Index	2806.86	-8.96%	2.74%

Property – Index Returns*	Index	At Close 29/02/2020	% Return 1 Month	% Return 12 Months
Listed Property	S&P/ASX 200 A-REITS	1579.40	-4.86%	11.80%

Interest Rates	At Close 29/02/2020	At Close 31/01/2020	At Close 28/02/2019
Australian 90 day Bank Bills	0.80%	0.88%	1.87%
Australian 10 year Bonds	0.82%	0.95%	2.10%
US 90 day T Bill	1.27%	1.54%	2.43%
US 10 year Bonds	1.15%	1.51%	2.72%

Currency**		At Close 29/02/2020	% Change 1 Month	% Change 12 Months
US dollar	AUD/USD	0.65	-2.64%	-8.23%
British pound	AUD/GBP	0.51	0.24%	-5.07%
Euro	AUD/EUR	0.59	-2.07%	-5.32%
Japanese yen	AUD/JPY	70.37	-2.96%	-10.96%
Australian dollar Trade-Weighted Index		57.0	-1.89%	-6.10%

* Closing index values are based on price indices. Index returns are expressed as total returns in local currency.

** All foreign exchange rates rounded to two decimal places.

Past performance is not a reliable indicator of future performance.

Global economies

The focus over the past month has been almost entirely on the coronavirus outbreak, the measures taken to contain it, and the potential economic fallout. At this stage it is difficult to gauge the impact on Chinese and global growth, but so far the disruption caused to supply chains and the effect on confidence has been dramatic.

US

In response to the coronavirus outbreak and anticipated economic fallout, the US Federal Reserve made an emergency cut to the funds rate of 50 basis points – its biggest single cut since 2008 – bringing the rate to 1.25%. Fed Chair Jerome Powell said: “The virus and the measures that are being taken to contain it will surely weigh on economic activity, both here and abroad, for some time.” The virus is likely to have a significant effect on economic growth, coming at a time when the underlying economy is reasonably robust. GDP growth for the December quarter was an annualised 2.1%, which was in line with expectations, while inflation remained well under control. Payrolls growth surprised to the upside while consumer confidence was near record highs, in contrast to more sombre business confidence levels. Although payrolls growth slowed in 2019 with an average 176,000 jobs added each month, down from 223,000 in 2018, 2020 started on a positive note with 225,000 jobs added. After rebounding in January, the ISM manufacturing index moderated from 50.9 to 50.1, just barely in expansion territory. The presidential election race is the other big news story, with the Democrats close to choosing a presidential candidate to take on Trump. Super Tuesday – the biggest voting day of the Democratic nomination process – saw Joe Biden firm as the favourite to win nomination.

Europe

Eurozone GDP grew by less than 0.1% in the December quarter according to the flash estimate, marking the slowest rate since the recession in 2012-13. Data showed GDP in Germany was essentially unchanged, while in France it shrank by just under 0.1% amid disruptions over pension reform. Over 2019, eurozone GDP grew by just under 1.0%, which was the slowest year-on-year growth rate since 2013, while industrial production in Germany fell 6.7%, down from the recent peak of growth of 6.5% at the end of 2017. Headline inflation in the zone picked up to 1.4% in January from 1.3%, but core inflation, excluding food and energy, fell to 1.1% from 1.3%. The coronavirus outbreak, along with the combination of flagging growth and sliding inflation, means the ECB is certain to cut rates and may also make changes to bank lending and increase the size of its bond-buying program. After leaving the EU, the UK is now in the process of negotiating a trade deal with Europe. Prime Minister Johnson said he will not seek an extension if an agreement is not reached before the deadline of 31 December. The UK economy failed to grow in the December quarter following a modest 0.5% growth in the September quarter, as political uncertainty restrained business investment, consumer spending and manufacturing production.

China

At this stage it is difficult to gauge the exact impact of the coronavirus on Chinese and indeed global growth. Consensus forecasts for Chinese GDP growth in the current quarter are variable but could be close to zero given the extended closure of industry, restrictions on people movement, and the disruption caused to supply chains. While past epidemics like the SARS virus had a limited effect on global growth, the effect of the coronavirus epidemic is expected to be much greater given China's dominant presence in the global economy. According to a Ministry of Industry and Information Technology spokesperson, only 30 percent of small and medium businesses nationwide have resumed work, while car sales have plunged 80% and passenger traffic is down 85%. China accounts for 18% of global tourism spending (up from 4% in 2008) while overall tourism (domestic and global) spending accounts for more than 10% of Chinese GDP and has been contributing almost 1.5% to annual GDP growth. Many international airlines have either stopped operating in or reduced flights to China, and some countries have closed their borders with China or denied entry to foreign nationals who have recently visited. Major overseas companies have highlighted the impact of supply chain disruptions curtailing production.

Asia region

Japan's GDP contracted at a 6.3% annual rate in the December quarter after the October rise in the consumption tax, posting a result much weaker than the anticipated 3.7% fall. The contraction was similar in size to that seen during previous tax rises, suggesting that stimulus measures were ineffective. Consumption, which fell at an annualised rate of 11%, was the main cause of the fall in output, but business investment also fell at a 14% rate. Department store sales fell 2.0% over the year to December after falling 7.0% previously. Japanese exports fell nearly 8.0% over the year to November and have been falling since December 2018. The weakness, coupled with the virus outbreak and its effect on the Chinese economy and global trade, suggest that Japan could be heading towards a recession. The effects of the coronavirus have been felt throughout Asia, notably in South Korea, the country with the highest number of confirmed cases outside of China. Consumer confidence in Korea fell from 104.2 in January to 96.9 in February—the largest single month decline in five years. In India, the goal of raising economic growth back above 7.0% seems like a dream, although the recent falls in crude oil prices could prove a tailwind by relieving pressure on inflation and reducing foreign currency outflows.

Australia

Unfortunately, the coronavirus and the policy response have come at a time when the Australian economy was showing signs of improvement and the budget was on a firm footing. There is a chance that the domestic economy will contract in the current quarter, prompting calls for fiscal stimulus. In 2018, Australia's exports of travel services to China amounted to \$16.2 billion, of which \$11.7 billion was education-related and \$4.1 billion was classified as 'other personal'. China accounts for 27% of total travel exports and 33% of education-related travel exports. If the 60% of Chinese personal travel exports that typically occur in the March quarter were 'banned' and a third of education-related travel exports waived or delayed, there could be a \$5–6 billion hole in Australia's March quarter GDP (around 1.0% of quarterly GDP). Of course, this doesn't take into account the negative multiplier effects on local employment and investment plans, nor the counterbalancing effects of fiscal measures and a lower Australian dollar. The RBA expects GDP growth of 2.0% for 2019 and 2.7% for 2020, down from the 2.3% and 2.8% projected in the November 2019 Statement on Monetary Policy. These latest forecasts include preliminary assessments of the impact of both bushfires and the coronavirus, although they stressed the high degree of uncertainty around the latter.

EQUITY MARKETS

- ▶ The S&P/ASX 200 Index fell 7.7% in February as the world was engulfed by coronavirus fears and markets fled to safety.
- ▶ Market concerns were further compounded by a plunge in crude oil prices that intensified in March as Saudi Arabia and Russia entered a bitter price war.
- ▶ The S&P 500 Index fell 8.2% as the VIX (or 'fear gauge') spiked to its highest level since 2009, with the energy and financial sectors the hardest hit.
- ▶ The UK FTSE 100 Index fell 9.0% and the German DAX 30 Index fell 8.4%, while in Asia the Nikkei 225 Index fell 8.8% and the Chinese CSI 300 Index fell 1.6%.
- ▶ Global developed market shares fell 5.5% in February in Australian dollar terms while emerging markets fell 2.3%.

Australian equities

	Index/Benchmark (% pa)	1 Month	1 Year	3 Years	5 Years	7 Years
Australian	S&P/ASX 200 Acc. Index	-7.69%	8.64%	8.59%	6.17%	7.96%
	S&P/ASX 50 Acc. Index	-7.30%	10.44%	8.74%	5.77%	7.82%
	S&P/ASX Small Ordinaries Acc. Index	-8.68%	1.64%	8.31%	7.42%	5.16%

February saw heavy selling in local and global shares as markets priced in the risk of the coronavirus outbreak, which includes significant disruption to supply-chains due to lockdowns, travel restrictions and other efforts to contain the virus. Reporting season revealed a number of ASX companies have already been forced to make downward adjustments to guidance. Webjet (-18.6%) announced a cut to its FY20 EBITDA guidance in response to noticeable reductions in bookings and total transaction value (TTV) across its WebBeds and Webjet OTA divisions. Qantas (-13.7%) was unsurprisingly also affected, announcing temporary reductions to flights across Asia due to falling demand. Software company WiseTech Global (-39.4%) said the virus is likely to have a significant effect on the global logistics supply chain, which their software caters to. Second-order effects were also evident in companies like Cochlear (-13.9%), which saw a decline in greater-China sales due to deferral of surgeries involving implants. That's not to say there were no winners from earnings season. Domino's (+1.3%) reported strong expansion in European markets, while Appen (-18.3%) reported strong underlying EBITDA growth, although it too was caught up in the risk-off selling.

Investment Index/Benchmark returns*

S&P/ ASX 200 Index

Sector	1 Month	3 Months	1 Year
Utilities	-3.62%	-2.29%	2.27%
Health Care	-3.72%	4.99%	47.57%
Property	-4.86%	-3.27%	11.80%
Financials ex-Property	-4.89%	-2.05%	3.84%
Consumer Staples	-7.13%	-7.61%	20.11%
Industrials	-8.24%	-9.24%	8.43%
Communications	-8.59%	-6.91%	11.82%
Consumer Discretionary	-8.62%	-6.80%	13.97%
Materials	-11.74%	-8.81%	0.39%
Energy	-17.20%	-17.88%	-14.84%
Information Technology	-17.28%	-12.31%	4.36%

*Total returns based on GICS sector classification

BIG MOVERS THIS MONTH

Going up

None

Going down

↓ Information Technology	-17.3%
↓ Energy	-17.2%
↓ Materials	-11.7%

Global Equities

	Index/Benchmark (% pa)	1 Month	1 Year	3 Years	5 Years	7 Years
Global	MSCI World Ex Australia Index (AUD)	-5.47%	14.60%	13.55%	9.98%	15.83%
	MSCI World Ex Australia Index (LCL)	-8.11%	5.24%	7.02%	6.25%	9.56%
	MSCI World Ex Australia Small Cap Index (AUD)	-6.19%	6.65%	10.12%	8.88%	15.13%
Emerging	MSCI Emerging Markets Index (AUD)	-2.25%	7.32%	10.93%	6.60%	8.60%
	MSCI AC Far East Index (AUD)	-2.34%	10.06%	11.31%	8.04%	12.23%

Global markets were rocked by the spread of the coronavirus as investors struggled to keep up with the flow of information and price in the potential economic damage. In the United States, the CBOE Volatility Index (VIX), known as the 'fear gauge', spiked to 49.5 points, its highest level since 2009. In an extraordinary move, the Federal Reserve cut the funds rate by 50 basis points – its largest single move since 2008 – sparking a short-lived rally in equities, although selling quickly resumed as investors questioned the efficacy of monetary policy. With all sectors deep in the red, the Communications Services sector (-6.3%) was the best performing, thanks to a bump from T-Mobile (+13.9%) following the approval of its merger with rival Sprint, as well as momentum from Netflix (+7.0%) and a small gain from Twitter (+2.2%) as the stock rebuilds after revenue and earnings misses in October. The situation in Europe was much the same, with the biggest falls hitting Lufthansa (-15.5%) and Siemens (-16.5%) in Germany and low-cost carrier easyJet (-21.0%) in the UK. In Asia, Japan's Nikkei 225 Index fell 8.8%, while China's CSI 300 Index fell a more modest 1.6% over February on the hopes that authorities will continue to lower financing costs and possibly provide additional support.

Property

	Index/Benchmark (% pa)	1 Month	1 Year	3 Years	5 Years	7 Years
Australian	S&P/ASX 300 A-REIT Acc.	-4.86%	11.80%	9.86%	8.76%	11.48%
Global	FTSE EPRA/NAREIT Developed Ex Australia Index (AUD Hedged)	-8.09%	2.98%	5.27%	4.82%	8.04%

Listed property was unable to avoid the pain as fears of the coronavirus hit markets in February, sending the S&P/ASX 200 A-REIT Index down 4.9%. The hardest hit was retail shopping centre group Vicinity Centres (-15.0%), which cut its guidance in February noting a material decline in foot traffic, most notably at its Chadstone centre. Fellow retail property manager Scentre Group (-10.4%) and integrated manager Mirvac (-10.6%) were also among the worst performers. The real estate sector is where the green shoots of Australia's recovery were most noticeable, as expected following a period of easing monetary policy. House prices in Melbourne are now just 1.2% off the 2017 peak, while Sydney house prices have surged 5.6% in the past three months. Housing finance for owner-occupiers increased by 17.9% over the year, pointing to further improvement in dwelling approvals. In the US, REITs were down 7.1% in February, with Hotels (arguably the most exposed sector) down 13.8% and Office Property down 10.9%. The start of March saw a bounce-back in domestic-focused and yield-sensitive sectors, although this appears

short-lived. Meanwhile, US mortgage rates dipped to historic lows, representing a potentially large natural stimulus to help boost the resurgent housing market.

Fixed Interest

	Index/Benchmark (% pa)	1 Month	1 Year	3 Years	5 Years	7 Years
Australian	Bloomberg AusBond Composite 0+ Yr Index	0.86%	8.98%	5.98%	4.45%	5.06%
	Bloomberg AusBond Bank Bill Index	0.08%	1.30%	1.68%	1.85%	2.11%
Global	Bloomberg Barclays Global Aggregate Index	4.53%	19.08%	10.70%	6.97%	8.85%
	Bloomberg Barclays Global Aggregate Index (AUD Hedged)	1.21%	9.33%	4.97%	4.46%	5.15%

Fears of significant disruption to global economic growth in the short-term led investors to move into safe-haven assets including bonds, while policy responses from central banks pushed yields to record lows. The yield on Australian 10-year Treasury bonds fell 13 basis points to 0.82% in February, and in the first week of March fell a further 8 points to 0.72%. Its US counterpart fell 36 basis points to 1.15% in February and since the start of 2020 has fallen from 1.92% to 0.91% (as at 5 March), a dramatic drop of 101 basis points. At an unscheduled meeting, the US Fed made an emergency cut to the funds rate of half a percentage point in anticipation of the economic fallout. Markets recognise that monetary policy alone is limited in what it can achieve in terms of preventing supply-side damage to the economy, but lower rates may help to support sentiment or buy time for governments to determine an appropriate fiscal response. Weak growth and slowing core inflation have seen the yields on 10-year German government bonds fall from -0.19% to -0.86% since the start of 2020. Most strikingly, Greek 10-year bonds were yielding less than 1.0% in mid-February, down from over 27% in mid-2012 and below that of Italian bonds.

Australian dollar

The Australian dollar fell from US \$0.6692 to \$0.6515 in February, hitting an 11-year low. The dollar is down from \$0.7024 at the start of 2020 and has endured bushfires, droughts, floods and now the coronavirus. This, along with a plunge in oil prices, saw flows move from riskier currencies like the Australian dollar to safer currencies like the Japanese yen.

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