

August 2020

- ▶ The impact of the Covid-19 pandemic on the global economy has been profound, especially in emerging, low-income economies with limited health care capacity.
- ▶ Trade tensions between the US and China added to market volatility, while the outcome of the November US presidential election remains uncertain.
- ▶ A port explosion in Beirut killed at least 135 people and severe flooding in southern China added to the country's woes, displacing millions from their homes.
- ▶ The Reserve Bank of Australia (RBA) kept rates on hold at 0.25% at its August meeting and indicated it will resume purchases of 3-year government bonds.
- ▶ Harsher restrictions in Victoria following a spike in Covid-19 cases could cost the Australian economy \$9 billion, according to the federal government.

July market performance

| Equity Markets – Index Return* | Index | At Close 31/07/2020 | % Return 1 Month | % Return 12 Months |
|--------------------------------|------------------------|------------------------|---------------------|-----------------------|
| Australia | S&P/ASX 200 Index | 5927.78 | 0.50% | -9.87% |
| United States | S&P 500 Index | 3271.12 | 5.64% | 11.96% |
| Japan | Nikkei 225 Index | 21710.00 | -2.60% | 3.03% |
| Hong Kong | Hang Seng Index | 24595.35 | 1.51% | -8.26% |
| China | CSI 300 Index | 4695.05 | 13.56% | 25.06% |
| United Kingdom | FTSE 100 Index | 5897.76 | -4.20% | -19.23% |
| Germany | DAX 30 Index | 12313.36 | 0.02% | 1.02% |
| Europe | FTSE Eurotop 100 Index | 2628.62 | -2.35% | -8.26% |

| Property – Index Returns* | Index | At Close 31/07/2020 | % Return 1 Month | % Return 12 Months |
|---------------------------|--------------------------|------------------------|---------------------|-----------------------|
| Listed Property | S&P/ASX 200 A-REIT Index | 1217.20 | 0.65% | -22.80% |

| Interest Rates | At Close 31/07/2020 | At Close 30/06/2020 | At Close 31/07/2019 |
|------------------------------|------------------------|------------------------|------------------------|
| Australian 90 day Bank Bills | 0.10% | 0.10% | 1.04% |
| Australian 10 year Bonds | 0.82% | 0.87% | 1.19% |
| US 90 day T Bill | 0.08% | 0.13% | 2.06% |
| US 10 year Bonds | 0.53% | 0.66% | 2.02% |

| Currency** | | At Close 31/07/2020 | % Change 1 Month | % Change 12 Months |
|----------------------------------------|---------|------------------------|---------------------|-----------------------|
| US dollar | AUD/USD | 0.72 | 5.10% | 4.63% |
| British pound | AUD/GBP | 0.55 | -1.59% | -3.03% |
| Euro | AUD/EUR | 0.61 | -0.72% | -1.81% |
| Japanese yen | AUD/JPY | 75.27 | 1.80% | 0.57% |
| Australian Dollar Trade-weighted Index | | 61.9 | 3.17% | 4.03% |

* 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

Hopes of a V-shaped recovery faded as Covid-19 cases worldwide ticked over 15 million. Policy settings remain incredibly favourable as central banks and governments support economies via monetary easing and fiscal

measures. Cyclical indicators such as unemployment figures and PMIs remain weak but are showing signs of improvement as the global economy adapts to the pandemic.

US

The impact of the coronavirus caused US GDP to shrink by an annualised 32.9% in the June quarter (-9.5% quarter-on-quarter), slightly better than the expected 34.1% fall. Contractions were seen almost everywhere, particularly in personal consumption and exports, while federal government spending jumped. The recovery in consumer confidence faltered in July, slipping from 98.3 to 92.6 and missing expectations of 94.5. The expectations component was the largest drag, slumping from 106.1 to 91.5. The July ISM Manufacturing PMI increased to 54.2 from 52.6, ahead of the expected 53.6, while construction spending disappointed in June, falling 0.7% (versus +1.0% expected) following a revised 1.7% fall in the prior month. Despite adding 9.3 million jobs over the past three months, total employment remains 12.9 million below its February level and economists fear some job losses may prove permanent. US unemployment stood at 10.8% in July. Congressional Democrats and White House officials remain at odds over further stimulus packages, prompting President Trump to sign a measure to provide an additional \$400 per week to workers displaced due to the virus. At its 31 July meeting, the Federal Reserve left the target rate unchanged at 0.00–0.25%, as expected.

Europe

The flash estimate for eurozone June quarter GDP came in as expected, falling 12.1%, making it the largest contraction on record as lockdowns continued to impact global demand. Inflation remained subdued in July, with the yearly rate at 0.4%, slightly above the 0.2% expected. In positive news, the July Markit composite PMI printed at 54.8 in July, ahead of expectations of 51.1, with both manufacturing and services returning to growth as more businesses began reopening. In Germany, GDP for the June quarter fell 10.1%, worse than the expected 9.0% fall, taking the year-on-year rate to -11.7%. Incredibly, Germany's unemployment rate held steady at 6.4%, with a surprise jump in employment of 18,000. France, Italy and Spain also reported double-digit falls in Q2 GDP. Europe is under threat from a second wave of Covid-19 infections, with the French government describing the situation as "under control but fragile", while Britain's health secretary said, "I think you can see a second wave starting to roll across Europe, and we've got to do everything we can to prevent it from reaching these shores." In signs of lockdown fatigue, around 17,000 people marched through the streets of Berlin to protest restrictions and mask-wearing, while easyJet announced it would schedule additional flights to meet better than expected demand during the European summer.

China

China's June quarter GDP came in above expectations, with the yearly rate increasing to 3.2% (2.5% expected), following a -6.8% reading in the previous quarter and becoming the first country to report growth since the beginning of the pandemic. Industrial production recovered in June, with the year-on-year rate increasing from 4.4% to 4.8% (4.6% expected), while retail sales disappointed, rising from a -2.8% year-on-year rate to -1.8% in June, well below the expected +0.4% yearly rate. The Caixin Manufacturing PMI for July came in above expectations of holding flat at 51.3, rising to 52.8 and posting the third consecutive rise in factory activity as consumer demand continues to pick up following the impacts of the coronavirus. Flooding in southern China has destroyed roads, property and farmland, and displaced millions of people from their homes. China's Ministry of Emergency Management estimated the direct economic cost of the disaster is around \$21 billion. Preliminary research indicates that the floods could shave 0.17% from China's 2020 GDP. A World Health Organization team arrived in Wuhan where the outbreak was first detected to begin laying the groundwork for an international investigation into the cause of the Covid-19 virus, including how it was transmitted from animals to humans.

Asia region

Japan was initially successful in preventing the spread of Covid-19. Cases have been rising recently, with over 40,000 confirmed at the start of August, but to date the economic effects have been less dramatic compared to other regions. The Japanese government released different forecasts for GDP growth over the current fiscal year based on how prolonged the pandemic proves to be, but under each scenario GDP is expected to contract by less than 5%. Japan's composite PMI came in at 43.9 in July, improving from the upwardly revised level of 40.8 in June, while the services PMI improved 0.2 points to 45.2 from the revised June level of 45.0. CPI rose 0.1% in June, leaving the yearly rate unchanged at 0.1%. Vietnam, which was officially virus-free for some months, began reporting new cases in Hanoi, Ho Chi Minh City and the Central Highlands, while the third-largest city of Da Nang was locked down to contain a new outbreak. By the end of July, India was accounting for around 17% of new infections reported globally each day. The response from the Indian government has helped to mitigate the economic fallout, with a fiscal stimulus of 20 trillion rupees (around 10% of GDP). The manufacturing PMI has recovered 50% since May but at 46.0 points it remains in contraction.

Australia

The Australian government warned that the economy likely shrunk at its fastest pace in recorded history in the June quarter, while the budget deficit will be the biggest since World War II as payments were extended to businesses and job seekers. The prime minister said the harsher lockdowns in Victoria would reduce GDP by between \$7 billion and \$9 billion in the September quarter, while the total hit to GDP is forecast to be around \$12 billion. At its August meeting the RBA left interest rates on hold and maintained its target for the 3-year yield curve at 0.25%. In his statement Governor Lowe said the worst of the contraction has passed, but the outlook remains highly uncertain, especially given Victoria's move to stage four lockdowns. The recovery is expected to be gradual and highly contingent on how the pandemic evolves. The June quarter CPI release reported a 1.9% fall in consumer prices (versus -2.0% expected), the largest recorded fall in the index's 72-year history. The quarterly fall was largely driven by plunging childcare (-95.0%), slumping automotive fuel prices (-19.3%), and a fall in pre-school and primary education (-16.2%). The federal government announced a \$15.6 billion expansion of the JobKeeper program, of which \$13 billion is estimated to flow to Victoria.

Equity Markets

- ▶ Australia's S&P/ASX 200 Index rose 0.5% in July with solid gains from the materials and information technology sectors.
- ▶ The US S&P 500 Index rose 5.6% in July in US dollar terms, supported by large-cap technology shares.
- ▶ In Europe, the UK FTSE 100 Index fell 4.2%, France's CAC 40 Index fell 2.6%, and Germany's DAX 30 Index was flat over the month.
- ▶ In Asia, Japan's Nikkei 225 Index fell 2.6%, while Hong Kong's Hang Seng Index rose 1.5% and China's CSI 300 Index jumped 13.6%.
- ▶ Global developed market shares rose 0.6% in Australian dollar terms and emerging market shares rose 4.6%.

Australian equities

| | Index/Benchmark (% pa) | 1 Month | 1 Year | 3 Years | 5 Years | 7 Years |
|------------|-------------------------------------|---------|---------|---------|---------|---------|
| Australian | S&P/ASX 200 Acc. Index | 0.50% | -9.87% | 5.37% | 5.15% | 6.78% |
| | S&P/ASX 50 Acc. Index | 0.22% | -11.20% | 4.99% | 4.30% | 6.12% |
| | S&P/ASX Small Ordinaries Acc. Index | 1.39% | -8.49% | 6.47% | 7.86% | 6.30% |

The recovery in Australian shares was cut short in July amid reports of growing Covid-19 cases and anticipation of harsher restrictions in Victoria. Early in August, the Victorian government announced a state of disaster and moved to stage four lockdown, which will see an estimated 1 million people restricted from going to and from their workplace for at least six weeks, while only essential businesses including supermarkets and pharmacies may remain open. The S&P/ASX 200 Index gained 0.5% over the month, dragged down by the energy and health care sectors. Materials performed well over the month, with strong returns from Fortescue Metals Group (+25.7%) and Oz Minerals (+24.4%). In early earnings reporting, Rio Tinto (+4.2%) announced that 1H 2020 EBIDTA fell 6% on the prior corresponding period due to lower commodity prices during the half but reconfirmed its 2020 production guidance across all commodities. Wesfarmers (+3.8%) gave a Covid-19 update following Victoria's lockdown announcement: all of the group's retail businesses will continue online operations through home delivery and contactless click and collect, while Bunnings will remain open for trade customers only and Officeworks will be open to service business customers. In FY20, Wesfarmers derived approximately 17% of retail sales from stores within metropolitan Melbourne.

Investment Index/Benchmark returns*

S&P/ ASX 200 Index

| Sector | 1 Month | 3 Months | 1 Year |
|------------------------|---------|----------|---------|
| Materials | 5.82% | 16.94% | 3.78% |
| Information Technology | 4.64% | 26.99% | 19.07% |
| Communications | 3.44% | 12.26% | -7.11% |
| Consumer Staples | 3.35% | 8.19% | 6.14% |
| Consumer Discretionary | 2.71% | 15.25% | 0.75% |
| Property | 0.65% | 6.13% | -22.80% |
| Utilities | -0.18% | 2.50% | -3.96% |
| Financials ex-Property | -1.11% | 8.58% | -23.59% |
| Industrials | -3.85% | -1.64% | -18.77% |
| Health Care | -3.89% | -5.80% | 15.58% |
| Energy | -6.55% | -4.13% | -34.46% |

*Total returns based on GICS sector classification

Big Movers This Month

Going up

| | | |
|---|---------------------------|-------|
| ↑ | Materials | +5.8% |
| ↑ | Information Technology | +4.6% |
| ↑ | Communications | +3.4% |

Going down

| | | |
|---|-------------|-------|
| ↓ | Energy | -6.6% |
| ↓ | Health Care | -3.9% |
| ↓ | Industrials | -3.9% |

Global Equities

| | Index/Benchmark (% pa) | 1 Month | 1 Year | 3 Years | 5 Years | 7 Years |
|----------|-----------------------------------------------|---------|--------|---------|---------|---------|
| Global | MSCI World Ex Australia Index (AUD) | 0.60% | 3.42% | 11.61% | 8.11% | 11.99% |
| | MSCI World Ex Australia Index (LCL) | 3.46% | 5.93% | 7.64% | 7.41% | 9.18% |
| | MSCI World Ex Australia Small Cap Index (AUD) | -0.30% | -5.90% | 6.14% | 5.58% | 10.05% |
| Emerging | MSCI Emerging Markets Index (AUD) | 4.58% | 2.40% | 6.59% | 6.65% | 7.74% |
| | MSCI AC Far East Index (AUD) | 0.05% | 4.66% | 7.67% | 6.35% | 9.53% |

Global shares continued their march higher in July, rising 0.6% in Australian dollar terms and 3.5% in local currency terms. With around half of S&P 500 companies having reported at the time of writing, it is clear earnings have been severely affected by the pandemic, although not as badly as anticipated. The US share market has been supported by the 'big four' tech giants (Amazon, Apple, Facebook, and Google), all of which beat estimates. Amazon (+14.7%) was arguably the biggest winner, reporting the largest quarterly net profit in its history, nearly double that of the corresponding quarter in 2019. Apple (+16.5%) reported revenue of US\$59.7 billion, above estimates of US\$52.2 billion, while every major product line saw year-on-year growth and beat analyst expectations. Microsoft shares (+0.7%) posted modest gains as the company tried to salvage a deal to buy TikTok's US operations. Across the Atlantic, EU leaders have been relatively successful in containing the Covid-19 virus and providing much-needed fiscal support. In July the European Council approved a €750 billion package to fund fiscal transfers between member states. Since March, the euro has been on the rise against the US dollar as investors see European assets as increasingly attractive.

Property

| | Index/Benchmark (% pa) | 1 Month | 1 Year | 3 Years | 5 Years | 7 Years |
|------------|------------------------------------------------------------|---------|---------|---------|---------|---------|
| Australian | S&P/ASX 300 A-REIT Acc | 0.65% | -22.80% | 2.24% | 3.36% | 7.68% |
| Global | FTSE EPRA/NAREIT Developed Ex Australia Index (AUD Hedged) | 1.44% | -16.66% | -1.81% | 0.97% | 4.35% |

Australian REITs were mixed over July as the economic pain from the pandemic rolled on. Shopping centres, which play a prominent role in the A-REIT index, remain affected by reduced foot traffic and struggling tenants. Scentre Group (-6.0%) gave an update on its half year results, noting that the carrying value of its property portfolio as at 30 June 2020 will be down approximately 10% from the end of 2019, with Covid-19 impacts the overriding reason. Meanwhile, some diversified and industrial funds have held up reasonably well during the crisis. Charter Hall's Long WALE REIT (+8.2%) has been spared the worst despite one of its tenants, Virgin Australia, vacating its Brisbane headquarters. Centuria Industrial REIT (+3.8%) has similarly weathered the storm, reporting funds from operations per unit

of 18.9 cents in FY20, in line with its revised guidance. Centuria will launch a \$341 million rights issue to fund the purchase of the Telstra Data centre in Clayton, Melbourne. In the US, REITs returned 3.6% in US dollar terms, boosted by warehouse and industrial REITs (+12.5%) and dragged down by shopping centres (-10.2%) and hotels (-7.8%). Globally, developed market REITs returned 1.4% in Australian dollar hedged terms.

Fixed Interest

| | Index/Benchmark (% pa) | 1 Month | 1 Year | 3 Years | 5 Years | 7 Years |
|------------|--------------------------------------------------------|---------|--------|---------|---------|---------|
| Australian | Bloomberg AusBond Composite 0+ Yr Index | 0.37% | 3.58% | 5.62% | 4.58% | 5.01% |
| | Bloomberg AusBond Bank Bill Index | 0.01% | 0.73% | 1.49% | 1.70% | 1.96% |
| Global | Bloomberg Barclays Global Aggregate Index | -0.93% | 3.65% | 8.10% | 4.66% | 6.12% |
| | Bloomberg Barclays Global Aggregate Index (AUD Hedged) | 1.03% | 5.54% | 4.96% | 4.72% | 5.37% |

July saw further compression in yields and a tightening in spreads as central bank liquidity continued to flood the market. In the US, the Fed intends to hold the funds rate near zero until the economy has weathered the pandemic. Broad support from the Fed and its presence in the ETF market have helped to tighten spreads across both investment grade and high yield segments. The Fed also includes 'fallen angels' in its corporate bond purchases, while the European Central Bank has been more targeted in its approach, resulting in euro high yield being more exposed to volatility. A hunt for yield in the US market has also seen investors shift up the credit curve. The return on US high yield corporate bonds was 4.7% in July in US dollar terms, the highest monthly return since October 2011. According to the RBA, Australian government bond markets are functioning normally and have seen a solid increase in issuance. The yield on 3-year government bonds has been mostly in line with the RBA's 0.25% target, although it has been slightly higher in recent weeks, prompting the Bank to resume purchases in the secondary market. The yield target will remain in place until the RBA is satisfied it has brought the inflation and unemployment rates in line with its objectives.

Australian dollar

The Australian dollar continued its upward trend in July, appreciating 3.2% in trade-weighted terms and rising from US\$0.69 to \$0.72. While Australians are not travelling much presently, holidays could prove more expensive when the pandemic is over. A ballooning US budget deficit is contributing to a weaker US currency, while Australia's relative success in containing the pandemic has supported the dollar.

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