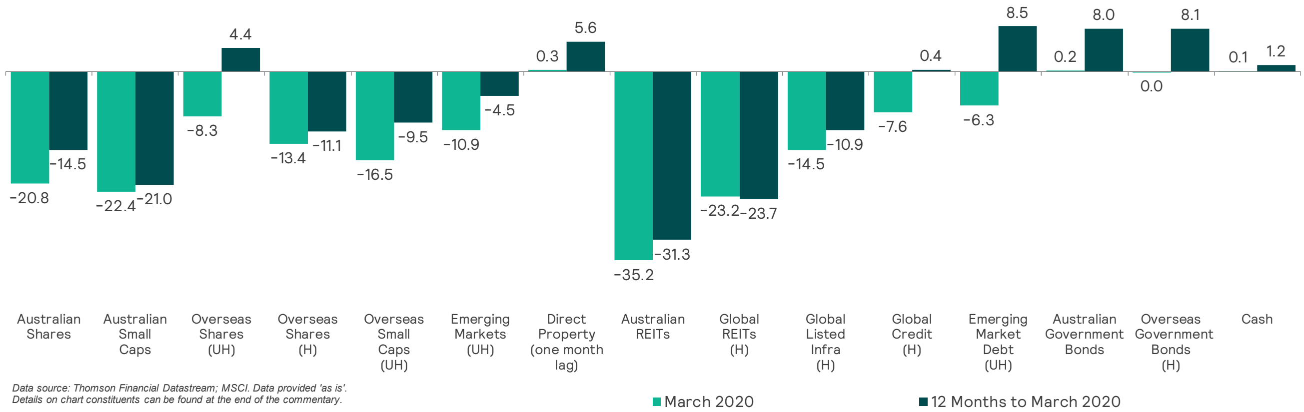
MARCH 2020

# AUSTRALIAN MONTHLY MARKET REVIEW

SELECTED MARKET INDICATORS COMMENTARY

## ASSET CLASS RETURNS (%) AS AT 31 MARCH 2020




*Data source: Thomson Financial Datastream; MSCI. Data provided 'as is'. Details on chart constituents can be found at the end of the commentary.*

COVID-19 has continued to spread rapidly around the world and was declared a global pandemic by the World Health Organisation. This has caused a severe shock to the global economy and financial markets have responded with sharp drops in share prices, a rise in credit spreads and a flight to defensive assets over March. Global shares and other risky assets declined all around the globe with Hedged Overseas Shares returning -13.4% whilst its Unhedged counterpart returned -8.3%, with the depreciation of the Australian dollar benefiting unhedged Australian investors. In anticipation of the economic growth fallout, S&P Global Ratings lowered its forecast for global growth to 0.4% in 2020 with a rebound to 4.9% in 2021. According to Bloomberg, the Q2 GDP average estimate (-11.2% annualised) would be the worst post WWII quarter on record, surpassing Q1 in 1958 with a GDP of -10%.

Unemployment spiked as companies laid off and furloughed workers, as governments forced businesses to close in order to facilitate social distancing. Given the global economic impacts and business disruptions resulting from COVID-19, central banks and governments worldwide announced fiscal and monetary rescue packages. The US fiscal stimulus package approved by the Senate totals US$2.2 trillion, which represents 10% of the US GDP. Whilst the Australian government announced a A$130 billion JobKeeper package to help keep Australians in jobs. Other packages were released in Japan, Singapore and the European Union (EU). For now, geopolitical tensions, including trade issues between the US and China, have faded into the background. Nonetheless, the oil price war that broke out between Russia and Saudi Arabia has put a constraint on oil prices.

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Amid the virus outbreak, the US election season continues with Joe Biden securing the Democratic Party nominee.

Global shares and other risky assets declined over the month. The decline during the month was consistent with the drawdowns seen in past recessionary periods. Share prices in developed markets recovered a portion of their losses in the latter half of March. Factor performance signalled solid risk aversion as investors favoured low volatility and low beta stocks as well as growth stocks. Markets in Japan were resilient whilst return dispersion in Emerging Markets were significant, as Latin America and Russia suffered from falling commodity prices. China outperformed global markets as manufacturing restarted.

The spread of the virus prompted a rally in developed government bonds relative to risky assets, with the Bloomberg Ausbond Treasury Index rising 0.2% and the FTSE WGBI Non Australia Index (Hedged) returning flat over March. However, credit suffered as spreads widened. The Fed cut rates twice in March to a range of 0-0.25% and began quantitative easing, including unlimited buying of Treasury debt, mortgage securities and corporate debt, which has never been done before. Central banks in the UK, Canada and Australia also cut rates and European Central Bank, Bank of Japan, Bank of England and Reserve Bank of Australia initiated QE programs. REITs tumbled on concerns of reduced leases in the commercial real estate sector, with Australian REITs returning -35.2% and Global REITs (Hedged) returning -23.2% over March.

The Australian share market lost ground over the economic fallout related to COVID-19, with the S&P/ASX300 returning -20.8% over March, underperforming its hedged international counterpart. Domestic small caps also displayed negative performance and underperformed domestic large caps, returning -22.4%. Consumer Staples (-3.6%) and Healthcare (-5.6%) were the top performing sectors, whilst Energy was once again the bottom performing sector, returning -37.6%.

Mercer's most recent views and commentary regarding the Coronavirus can be found through the following link: Coronavirus Outbreak Investment Implications Update.

## SIGNIFICANT DEVELOPMENTS

- The Reserve Bank of Australia (RBA) lowered the cash rate by an additional 25 basis points to 0.25% per annum (pa) during March. This decision was made against the backdrop of the global coronavirus outbreak. Governor, Philip Lowe, noted that the spread of the virus is having a major impact on the economy and financial system, and it is the RBA's priority to support jobs, incomes and businesses. As such, the Reserve Bank Board agreed to the following package to support the Australian economy through this challenging period:
    - Reduction in the cash rate target to 0.25%;
    - Target for the yield on 3-year Australian Government bonds of around 0.25%;
    - Term funding facility for the banking system, with particular support for credit to small and medium-sized businesses;
    - Exchange settlement balances at the Reserve Bank will be remunerated at 10bps, rather than zero as would have been the case previously.
- There is considerable uncertainty regarding the near-term outlook for the Australian economy. The RBA's policy package complements the fiscal response from governments in Australia and acts to support jobs, incomes and businesses through this difficult period, as well as assist the Australian economy in the recovery. The Board has noted that it will not increase the cash rate target until progress is made towards full employment and it is confident that inflation will remain sustainably within the 2-3% target range.
- Australian seasonally adjusted employment increased by 26,700 in February, above expectations for a 6,300 rise, while January figures were revised to an increase of 12,900. The unemployment rate decreased to 5.1% for February, below expectations for 5.3%. The participation rate decreased to 66.0%, below expectations for 66.1%. Part time jobs increased by 20,000 and full time jobs increased by 6,700.
- Australian building approvals increased 19.9% month-on-month to February, compared to the previous level of -15.1% (revised) for period ending January.
- The Institute for Supply Management (ISM) Manufacturing Index recorded 49.1 in March, above consensus for 44.5, and below the 50.1 recorded in February. Of the 18 manufacturing industries, Printing & Related Support Activities and Food, Beverage & Tobacco Products were the top contributors, whilst Petroleum & Coal Products and Textile Mills were the largest detractors over the month.

The ISM Non-Manufacturing Index recorded 52.5 in March, above consensus for 43.0 and below the 57.3 recorded in February. Of the 18 non-manufacturing industries, the top performers in March were Health Care & Social Assistance and Real Estate, Rental & Leasing, while Arts, Entertainment & Recreation and Transportation & Warehousing were the two industries, which reported the largest decreases over the month.

- US Non-Farm Payrolls decreased by 701,000 in March, below the 275,000 increase (revised) recorded for February. The unemployment rate increased to 4.4% over March.
- US gross domestic product (GDP) third estimate for Q4 2019 is 2.1% quarter on quarter (QoQ) annualised, in line with expectations.
- The Caixin Manufacturing PMI in China recorded 52.0 in March, above expectations for 44.8. After deteriorating at the quickest pace on record in February, business conditions faced by Chinese manufacturers were broadly stable over March.
- A preliminary estimate of the European Core Consumer Price Index (CPI) recorded 1.0% over the year to March, below expectations for 1.1%.
- The Eurozone composite PMI decreased to 29.7 in March, below expectations for 31.4.
- The final estimate recorded for Q4 2019 Eurozone seasonally adjusted GDP is 1.0% for year-on-year (YoY) and 0.1% QoQ.

## AUSTRALIAN EQUITIES

The Australian share market underperformed its hedged overseas counterpart index over the month, as the S&P/ASX 300 Index returned -20.8%. The S&P/ASX 50 was the strongest relative performer, decreasing 20.3%, while the S&P/ASX Mid 50 was the weakest, returning -22.7% over the month.

The best performing sectors were Consumer Staples (-3.6%) and Healthcare (-5.6%), while the weakest performing sectors were Energy (-37.6%) and Real Estate (-35.6%). The largest positive stock contributors to the index return were CSL, BHP and Rio Tinto with absolute returns of -4.0%, -13.5% and -2.5% respectively. In contrast, the most significant detractors were NAB, ANZ and Westpac with absolute returns of -33.0%, -31.2% and -29.6%, respectively.

## GLOBAL EQUITIES

The broad MSCI World ex Australia (NR) Index decreased 13.4% in hedged terms and decreased 8.3% in unhedged terms over the month, as the Australian dollar (AUD) depreciated against most major currencies. The strongest performing sectors were Healthcare (+1.5%) and Consumer Staples (+0.1%), while Energy (-25.6%) and Financials (-18.2%) were the worst performers. In AUD terms, the Global Small Cap index was down 16.5% and Emerging Market index was down 10.9% over March.

Over March, the NASDAQ decreased 10.1%, the S&P 500 Composite Index decreased 12.4% and the Dow Jones Industrial Average decreased 13.6%, all in USD terms. In local currency terms, major European share markets experienced negative returns as the CAC 40 (France) decreased 17.0%, the DAX 30 (Germany) decreased 16.4% and the FTSE 100 (UK) decreased 13.4%. Returns were also negative in Asia, as the Japanese TOPIX (-6.0%), the Indian S&P BSE 500 (-24.1%), Hang Seng (-9.5%) and the Chinese SSE Composite (-4.5%) all decreased over March.

## REAL ASSETS

The Real Assets sector experienced negative returns over March. The FTSE Global Core Infrastructure Index returned -14.5% and the Global Real Estate Investment Trusts (REITs) Index decreased by 23.2% over the month (both in AUD hedged terms). Domestic REITs decreased 35.2% over March, while Australian Direct Property (NAV) returned 0.3% on a one-month lagged basis.

## FIXED INTEREST

Global bond markets produced mixed returns over March for hedged Australian investors. The Barclays Capital Global Aggregate Bond Index (Hedged) decreased 1.7% over the month and the FTSE World Government Bond (ex-Australia) Index (Hedged) returned flat. Ten-year bond yields decreased in the US (-48bps to 0.67%) and the UK (-12bps to 0.31%), whilst ten-year bond yields increased in Japan (+17bps to 0.02%) and Germany (+18bps to -0.46%). Two-year bond yields also decreased over the month in the US (-65bps to 0.25%) and the UK (-18bps to 0.13%), whilst two-year bond yields increased in Japan (+11bps to -0.14%) and Germany (+7bps to -0.71%).

Returns for Australian bondholders were positive over March, with 10-year yields (-4bps to 0.77%), five-year yields (-16bps to 0.42%) and two-year yields (-32bps to 0.25%) all decreasing. Of the Bloomberg Ausbond indices, the Treasury index produced the highest return, increasing 0.2% over the month.

## CURRENCY MARKETS

The AUD Trade Weighted Index decreased to 54.7 over March, down by 4.0% from the previous month. The AUD depreciated against most major currencies, including the Euro (-5.5%), Japanese Yen (-6.0%), US dollar (-5.1%) and Pound Sterling (-1.1%).

## COMMODITIES

Iron Ore decreased 0.6% over March, finishing the month at US$84.0 per metric tonne. The S&P GSCI Commodity Total Return Index decreased 25.7% over the month. Gold prices finished the month at US$1,612.10 per ounce, increasing 1.6% over the month, and the oil price decreased 55.3% to US$22.60 per barrel over March.

## CHART CONSTITUENTS

***Notes***

- *Currency: AUD.*
- *UH: Unhedged.*
- *H: Hedged.*
- *Net Index: Total Return (Net Dividends Reinvested).*
- *Total Return: Total Return Index with Gross Dividends.*
- *Where a lag exists, the performance period start and end dates are shifted accordingly.*

| ASSET CLASS | BENCHMARK | DATA TYPE |
|---|---|---|
| Australian Shares | S&P/ASX 300 | Total Return |
| Australian Small Caps | S&P/ASX Small Ordinaries | Total Return |
| Overseas Shares (UH) | MSCI World ex Australia | Net Index |
| Overseas Shares (H) | MSCI World ex Australia 100% Hedged | Net Index |
| Overseas Small Caps (UH) | MSCI World Small Cap | Total Return |
| Emerging Markets (UH) | MSCI Emerging Markets | Net Index |
| Direct Property (one month lag) | MSCI/Mercer Australia Core Wholesale Monthly PFI | NAV Post Fee |
| Australian REITs | S&P/ASX 300: Industry Group: A-REIT | Total Return |
| Global REITs (H) | FTSE EPRA/NAREIT Developed Hedged | Total Return |
| Global Listed Infrastructure (H) | FTSE Global Core Infrastructure 50/50 Hedged | Total Return |
| Global Credit (H) | Bloomberg Barclays Global Credit | Hedged Return |
| Emerging Market Debt (UH) | JP Morgan GBI EM Global Diversified Composite | Total Return |
| Australian Government Bonds | Bloomberg AusBond Treasury 0+ year | Total Return |
| Overseas Government Bonds (H) | FTSE WGBI Non Australia | Hedged Return |
| Cash | Bloomberg AusBond Bank Bill | Total Return |

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