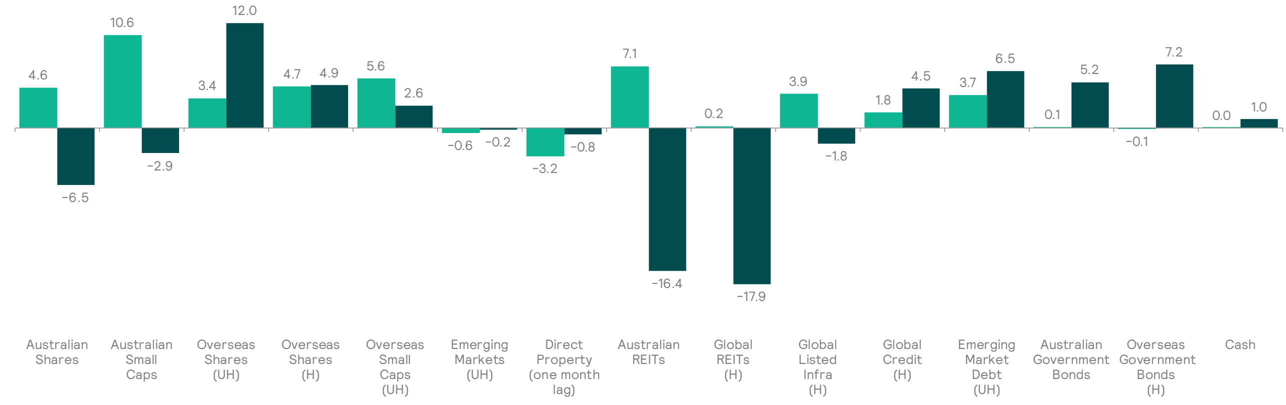
MAY 2020

AUSTRALIAN MONTHLY MARKET REVIEW

SELECTED MARKET INDICATORS
COMMENTARY

ASSET CLASS RETURNS (%) AS AT 31 MAY 2020



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

Following the strong rebound in risk assets over April, the recovery continued into the month of May. Markets were encouraged by the slowdown in new COVID-19 cases and the gradual relaxation of lockdown restrictions across a number of US states, European countries and the United Kingdom. There was also some progress on a number of vaccines that could be deployed as early as this year. Several new fiscal stimulus packages were announced in May, particularly in Europe and Japan, as evidence of the global economic contraction has continued to mount. Political tensions also resurfaced with China imposing a national security law on Hong Kong, reigniting protests and mounting tensions between China and western countries.

Concurrently, questions surrounding the origin of the Coronavirus continued and Brexit negotiations progressed slowly in the background.

Overseas shares and other growth assets performed strongly in May. Small cap and technology stocks led the rally, with the S&P/ASX Small Ordinaries achieving the highest monthly return (+10.6%), whilst, growth continued to outperform value. However, as the slowdown in the spread of the virus in developed markets has been positive the continued spread of COVID-19 in a number of large emerging nations, such as Brazil, Russia and India remained a concern. Consequently, Emerging Market shares suffered over the month, as the MSCI Emerging Markets Index (NR) returned -0.6%.

MERCER

Growth fixed income also did quite well over the month, as credit spreads for investment grade, high yield and emerging markets continuing to tighten. Over the month lower quality credit outperformed higher quality credit. Emerging Market Debt had the strongest growth fixed income performance over the month, returning 3.7% for the month. Within Defensive fixed income, particularly Australian and Overseas Government Bonds, returns were relatively flat with the Bloomberg Ausbond Treasury Index rising 0.1% over the month and the FTSE WGBI ex Australia (Hedged to AUD) declining 0.1% over the month. Bond markets have now priced in the large monetary easing programs initiated by central banks around the world. Major developed market central banks have not increased the pace of easing but have maintained their accommodative monetary stances, while China cut its reserve requirements for the second time in 2020.

Over May, commodity markets also reflected the gradual return to growth and general 'risk on' sentiment displayed by investors. Oil prices rallied during May ending the month at US$35.43 per barrel, and Gold also achieved a strong positive return. The US dollar weakened against the Australian Dollar, as financial conditions have mostly normalised and the safe haven driven demand for the US dollar has reduced.

The Australian share market has continued its positive run, with the S&P/ASX300 returning 4.6% over May. On a global front, Australian shares have performed relatively well compared to other developed nations and has only marginally underperformed its hedged international counterpart. IT (+14.3%) and Communication Services (+8.5%) were the top performing sectors, whilst Healthcare was the bottom performing sector, returning -5.1%.

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) decided to maintain its current policy settings, including maintaining the target cash rate at 0.25% per annum during May, and the targeted 0.25% yield on 3-year Australian Government bonds. Governor Philip Lowe noted that the global economy is experiencing a severe downturn as countries seek to contain the coronavirus. Many people have lost their jobs and there has been a sharp rise in unemployment. Over the past month, infection rates have declined in many countries and there has been some easing of restrictions on activity. If this continues, a recovery in the global economy will get underway, supported by both the large fiscal packages and the significant easing in monetary policies. Globally, conditions in financial markets have continued to improve, although conditions in some markets remain fragile. Volatility has declined and credit markets have progressively opened to more firms. In Australia, the government bond markets are operating effectively. The Bank's market operations are continuing to support a high level of liquidity in the Australian financial system. The Board is committed to do what it can to support jobs, incomes and businesses and to make sure that Australia is well placed for the recovery.
- Australian seasonally adjusted employment decreased by 594,300 in April, above expectations for a 575,000 fall, while March figures were revised to an increase of 700. The unemployment rate increased to 6.2% for April, below expectations for 8.2%. The participation rate decreased to 63.5%, below expectations for 65.3%. Part time jobs decreased by 373,800 and full time jobs decreased by 220,500.
- Australian building approvals decreased 1.8% month-on-month to April, compared to the previous level of -2.6% (revised) for period ending March.
- The Institute for Supply Management (ISM) Manufacturing Index recorded 43.1 in May, below consensus for 43.8, but above the 41.5 recorded in April. Of the 18 manufacturing industries, Non-metallic Mineral Products and Furniture & Related Products were the industries that reported the highest growth. Printing & Related Support Activities and Primary Metals were the largest detractors over the month.

The ISM Non-Manufacturing Index recorded 45.4 in May, above consensus for 44.4 and above the 41.8 recorded in April. Of the 18 non-manufacturing industries, the top performers in May were Agriculture, Forestry, Fishing & Hunting and Finance & Insurance. Mining and Arts, Entertainment & Recreation the two industries, which reported the largest decreases over the month.

- US Non-Farm Payrolls increased by 2,509,000 in May, above the 20,687,000 decrease (revised) recorded for April. The unemployment rate decreased to 13.3% over May, below expectations of 19.0%.
- US gross domestic product (GDP) second estimate for Q1 2020 is -5.0% quarter on quarter (QoQ) annualised, above expectations for -4.8%.
- The Caixin Manufacturing PMI in China recorded 50.6 in May, slightly below expectations for 51.1. Manufacturing output has risen solidly as COVID-19 restrictions begin to ease.
- A preliminary estimate of the European Core Consumer Price Index (CPI) recorded 0.9% over the year to May, above expectations for 0.8%.
- The Eurozone composite PMI increased to 31.9 in May, above expectations for 30.5. Eurozone operating conditions has improved compared to April.
- The final value recorded for Q1 2020 Eurozone seasonally adjusted GDP is -3.6% for quarter-on-quarter (QoQ) and -3.1% for year-on-year (YoY).

AUSTRALIAN EQUITIES

The Australian share market marginally underperformed against its hedged overseas counterpart over the month, as the S&P/ASX 300 Index returned 4.6%. The S&P/ASX Small Ordinaries was the strongest relative performer, increasing 10.6%, while the S&P/ASX 50 was the weakest, returning 3.2% over the month.

The best performing sectors were IT (+14.3%) and Communication Services (+8.5%), while the weakest performing sectors were Healthcare (-5.1%) and Consumer Staples (-0.5%). The largest positive stock contributors to the index return were Afterpay, Fortescue Metals Group and Goodman Group with absolute returns of 52.0%, 17.0% and 17.1% respectively. In contrast, the most significant detractors were CSL, CBA and Woolworths Group with absolute returns of -10.7%, 1.7% and -1.2%, respectively.

GLOBAL EQUITIES

The broad MSCI World ex Australia (NR) Index increased 4.7% in hedged terms and increased 3.4% in unhedged terms over the month, as the Australian dollar (AUD) appreciated against most major currencies. In AUD terms, the strongest performing sectors were IT (+6.2%) and Materials (+5.1%), while Real Estate (-0.3%) and Energy (0.0%) were the worst performers. In AUD terms, the Global Small Cap index was up 5.6% and Emerging Markets index was down 0.6% over May.

Over May, the NASDAQ increased 6.8%, the S&P 500 Composite Index increased 4.8% and the Dow Jones Industrial Average increased 4.7%, all in USD terms. In local currency terms, major European share markets experienced positive returns as the CAC 40 (France) increased 3.4%, the DAX 30 (Germany) increased 6.7% and the FTSE 100 (UK) increased 3.3%. Returns were mixed in Asia, as the Japanese TOPIX (+6.8%) increased, whilst the Indian S&P BSE 500 (-2.4%), Hang Seng (-6.3%) and Chinese SSE Composite (-0.3%) decreased over May.

REAL ASSETS

The Real Assets sector generally experienced positive returns again over May. The FTSE Global Core Infrastructure Index returned 3.9% and the Global Real Estate Investment Trusts (REITs) Index increased by 0.2% over the month (both in AUD hedged terms). Domestic REITs increased 7.1% over May, while Australian Direct Property (NAV) returned -3.2% on a one-month lagged basis.

FIXED INTEREST

Global bond markets returned mixed results over May. The Barclays Capital Global Aggregate Bond Index (Hedged) increased 0.3% over the month, whilst the FTSE World Government Bond (ex-Australia) Index (Hedged) returned -0.1%. Ten-year bond yields decreased in the US (-1bp to 0.63%), the UK (-7bps to 0.12%), whilst bond yields increased in Japan (+5bps to 0.01%) and Germany (+14bps to -0.45%). Two-year bond yields also decreased over the month in the US (-4bps to 0.17%), the UK (-6bps to -0.04%), but increased in Japan (+2bps to -0.16%) and Germany (+13bps to -0.63%).

Returns for Australian bondholders were mixed over May, with 10-year yields decreasing (-1bp to 0.89%), five-year yields remaining flat and two-year yields increasing (+5bps to 0.28%). Of the Bloomberg Ausbond indices, the Inflation Index produced the highest return, increasing 2.3% over the month.

CURRENCY MARKETS

The AUD Trade Weighted Index increased to 58.8 over May, up by 1.7% from April. The AUD appreciated against most major currencies, including the US Dollar (+1.4%), Japanese Yen (+2.0%), and Pound Sterling (+2.5%), but depreciated against the Euro by 0.7%.

COMMODITIES

Iron Ore increased 21.6% over May, finishing the month at US$101.5 per metric tonne. The S&P GSCI Commodity Total Return Index increased 14.8% over the month. Gold prices finished the month at US$1,731.55 per ounce, increasing 1.6% over the month, and the oil price increased 38.8% to US$35.43 per barrel over May.

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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IMPORTANT NOTICES

MARSH & McLENNAN COMPANIES