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Market Review – April 2020

Impact of COVID-19 in April

- Slowdown of economic activity as entire countries went into “shutdown”, leading to fears of a recession.
- Falling consumption, damaging many businesses, resulting in profit warnings, cancelled dividends and rising unemployment.
- A dramatic fall in oil prices due to continued, steady supply of oil, despite a considerable drop in demand.
- Concerns that key central banks, such as the US Federal Reserve and the Bank of England, are running out of influence, since interest rates are already close to zero for many.
- Scientific data suggesting that the COVID-19 crisis is still far from over, and will continue to affect economies and financial markets for some time.
- In response, key central banks announced emergency stimulus plans, governments pledged fiscal support.
- China markets staged a recovery, as coronavirus related restrictions began to slowly lift.
- Australian shares ruled off their best month since 1988 but a large materials exposure means it’s still one of the worst performing markets year to date.

Australian Economy

The government has done a great job in containing the virus outbreak with Australia being one of the leading examples of how to contain the spread with the $130bn JobKeeper stimulus designed to keep businesses and employment intact through the lockdown.

However, the next phase of the coronavirus crisis has the potential to be far more divisive because of higher unemployment, reduced income, increased debt, closure of businesses, restrictions on movement and social interactions.

The Reserve Bank Governor, Philip Lowe, has released new growth forecasts for Australia as the COVID-19 fight continues. There are several levers, policy makers could pull as we steer towards recovery and a new growth agenda.

The RBA expects a 10% decline in GDP over the March and June quarters. The central bank expects a recovery from the September quarter, meaning the new forecasts show a fall in GDP of around 6% in 2020 before a recovery of 6-7% in 2020.

The RBA also said it expects the unemployment rate to increase to around 10% in the June quarter. The central bank also expects hours worked to decline by 20% over the first half of the year.

Full employment and inflation will guide the RBA’s assessment of the cash rate. The governor said the cash rate will not be increased until Australia makes substantial progress towards those targets.

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To stimulate national growth, the government may very well now turn to implementing some tax reforms e.g. company tax cuts to encourage business growth and investment.

Not surprisingly NAB business conditions fell to -21.1 in March (previous: -0.2), while business confidence fell to -65.6 (previous: -2.4), the worst on record.

Global Economy

Despite the continuing global spread of Covid-19, April saw both equity and credit markets stage a rebound from the severe market shock witnessed in March, which has led to some of the biggest monthly gains certain sectors and regions have seen in years.

Central bank stimulus designed to provide relief from the pandemic has provided some support, while an experimental antiviral drug that appears to be effective in reducing recovery times has provided much-needed hope: the drug could perhaps help countries emerge from the lockdown measures that are severely impacting economic activity worldwide.

All of this has led to a wide disconnect between the unprecedented economic pain felt by many and the seemingly broad optimism of the financial markets. More and more workers are losing their jobs, while many small businesses are asking for loans to keep afloat, and yet, the financial markets are reporting gains.

Central bank stimulus is of course shoring up asset markets, but are the financial markets also pricing in a smooth recovery that is far from guaranteed? Should this be the case, more volatility could well be lying ahead.

US: The economic data may have been grim with millions more American's filing for unemployment benefits but US equity markets recorded their best monthly gain since January 1987.

The US Federal Reserve's (Fed's) announcement of unlimited and open-ended Quantitative Easing (QE) in late March had helped to turn market sentiment. It then looked to push the bar further with an announcement in April that asset purchases would include high yield bonds helping to give further strength to the rally.

With so many workers losing their jobs, consumer spending, the main engine of the US economy, nosedived to record its steepest monthly decline since records began in 1959. By contrast, the US personal savings rate jumped to its highest level since 1981. Households cut back on purchases of big-ticket items, such as cars, as well as on services, for example, restaurant, hotels and sporting events.

UK and Europe: Following a period of extreme weakness, the UK equity market started to recover in recent weeks to end the month in positive territory. Supported by the policy measures implemented by the Government and the Bank of England, UK stocks briefly entered a bull market at the end of April, defined as a rise of more than 20% from recent lows. However, volatility within the UK equity market remains high.

Data published by the European Commission showed that the Economic Sentiment Indicator (ESI) for the Euro Area plummeted to 67.0 (94.2 in March), its lowest level since records began in 1985. The fall resulted from a remarkably strong hit to confidence across all business sectors and amongst consumers. In addition, the Employment Expectations Indicator (EEI) also crashed to a record low – 63.7 in the euro area (93.8 in March).

The European Central Bank announced more support for banks by a reduction in the TLTRO3 (Targeted longer-term refinancing operations) by 25 basis points. TLTRO is an operation that provides long-term financing to banks at attractive conditions with the aim of trying to stimulate bank lending to the real economy.

Meanwhile, after nearly 20 hours of negotiations spread over three days, the eurozone finance ministers agreed to €500bn in additional financing to fight Covid-19. While the agreement is focused on immediate firefighting, the Eurogroup also included a recommendation to create a Recovery Fund to kickstart the economy once things start to normalise.

China: China and some other Asian countries appear to be gradually getting back to work and have put in place measures to mitigate the risk of a second wave. In particular, China has been ahead of the curve in terms of epidemic control.

The supply side in China is mostly back to capacity, while consumer demand is lagging. As consumption remains a key concern, policy support continued in April, which included further interest rate cuts.

Emerging Markets: Economic news was generally downbeat with factory output slumping across several countries including Asia, although encouragingly, China has started reopening factories and is ramping up infrastructure spending to support the domestic economy.

How the management of the Covid-19 crisis is perceived by investors arguably contributed towards the divergence of performance across emerging markets.

In conclusion: The economic impact of closing the world economy became increasingly apparent in April. Some of the data released covering the previous month was the worst ever recorded. In the UK, the services Purchasing Managers Index (PMI), (a respected indicator of the economic health of a country) declined to 12.3. This is its lowest ever level and, with a figure below 50 indicating contraction. And yet, against this backdrop, financial markets bounced back from their March lows with many parts of the market delivering their best return in decades.

Helping to drive these returns were signs of the virus easing and central bank policy. Having written the playbook after the global financial crisis in 2008, central banks have been able to implement what were once thought extraordinary policies much more rapidly than a decade ago.

Currencies

The USD remained flat in April. The defensive Danish Krone (-0.6%), Swiss Franc (-0.4%) and Japanese Yen (+0.3%) were the worst performing currencies, while the commodity driven Australian Dollar (+6.2%), Norwegian Krone (+1.6%) and Canadian Dollar (+0.8%) were the best performers.

Commodities

Bulk commodity prices were strong in April, Brent crude rose $2.53/bbl to $25.27/bbl. Among the bulks, iron ore continued to remain resilient, falling just $0.50/t to $83.50/t, while thermal and hard coking coal prices rose substantially. Gold prices rose by a significant $93.8/oz to $1,702.75/oz.

Please stay safe and focussed on the long term.

Table 1: Market Performance – Periods to 30 April 2020

Sector	1 Month %	3 Months %	1 Year %	3 Years % pa	5 Years % pa
Australian Shares	8.8	-20.3	-9.1	1.9	3.5
Australian Shares Small Cap	14.3	-19.0	-13.3	3.2	5.0
International Shares Ex-Aus (Unhedged)	3.7	-9.3	3.9	10.1	9.1
International Shares Ex-Aus (Hedged)	10.0	-10.9	-3.3	5.2	5.5
Emerging Markets (Hedged)	8.2	-9.4	-8.2	3.3	2.5
Emerging Markets (Unhedged)	2.1	-10.5	-5.4	5.1	3.7
Australian Listed Property	13.7	-29.8	-20.3	-1.8	3.0
International Listed Property ($A)	-1.2	-16.1	-3.3	4.8	5.0
Australian Direct Property	0.1	-2.6	-1.3	7.5	10.0
Australian Fixed Interest	-0.1	0.6	6.4	5.5	4.5
International Fixed Interest (Hedged)	1.5	1.2	7.3	4.7	4.3
Cash (BAUBIL)	0.0	0.2	1.1	1.6	1.8
		Change over the month			
Australian Govt. 10 yr Bond Yield	0.86%	-3 bps			
AUD/USD	$0.65	$0.04			

Australian Shares (S&P/ASX 200 Accumulation Index)

The S&P/ASX 200 Accumulation Index rose +8.8% in April but down -9.1% for the 12 months.

In Australia, the cyclical Energy (+24.9%), Information Technology (+22.5%) and Consumer Discretionary (+15.9%) outperformed the most, while Consumer Staples (+2.4%), Utilities (+2.7%) and Financials (+2.8%) underperformed the most.

Best performing shares in April were: AP Eagers Ltd (+69.6%), Afterpay Ltd (+66%), oOhMedia Ltd (+66% and Scentre Group (+49%).

The index finished trading at a P/BV of 1.7x and a P/E Ratio of 16.0x and equity yield (dividend) of 4.9%.

The VIX was at 26.0 (the average since 01.10.2010 is 16.4) indicating an extreme level of market volatility.

Australian Shares Small Cap (S&P/ASX Small Ordinaries Index)

The Small Ords Accumulation index rose +14.3% in April reversing one of the shortest bear markets on record.

Key contributors to the index return for April were consumer fintech Wisr (+56.6%), Silver Lake Resources (+41.3%), Appen (+31.0%) and Saracen Mineral Holdings (+30.0%). Key detractor over the month was service office provider Victory Offices (-48.0%).

Trailing P/E Ratio was at 16.1x at the end of the month, P/BV is at 1.7x and equity yield (dividend) of 3.6%.

International Shares (MSCI World ex Australia Index, Net AUD and the MSCI World ex Australia Index, Net LCL)

The MSCI World ex Australia Index (Unhedged) +3.7%% for April whilst the MSCI World ex Australia Index (Hedged) returned +10.0%.

European markets rebounded in April; German DAX +9.3%, French CAC 40 +4.0% and FTSE 100 +8.0%.

The index finished trading at a P/BV of 2.1x and a P/E Ratio of 18.3x and equity yield (dividend) of 2.5%.

US market: Biggest monthly gain for US equity markets since January 1987 this advance achieved despite grim economic data as job loses mount. The rally was supported once more by technology stocks, with Apple and Amazon reporting higher sales as consumers increasingly turned to home delivery and streaming entertainment.

The Dow Jones Industrial Average rose +11.1% in April. The S&P 500 Index rose +12.7% and the NASDAQ Composite surged +15.5%.

All sectors rose sharply in April, Communication Services (+18.1%), Consumer Discretionary (+19.7%), Consumer Staples (+10.2%), Energy (+37.2%), Financials (+11.3%), Health Care (+17.9%), Industrials (+11.2%), Materials (+20.8%), Real Estate (+9.5%), Technology (+16.3%) and Utilities (+5.3%).

UK market: Following a period of extreme weakness, the UK equity market started to recover in recent weeks to end the month in positive territory. Supported by the policy measures implemented by the Government and the Bank of England, UK stocks briefly entered a bull market at the end of April, defined as a rise of more than 20% from recent lows.

For the month of April, the UK equity market rebounded strongly, with the UK FTSE Index returning +8.0%.

European markets: European equity markets witnessed one of their strongest rallies ever over the month. The market appeared to look through the short-term data and was boosted by the prospect of a gradual easing in lockdown measures. Eurozone equities as represented by the MSCI EMU Index returned +6.5% in April.

Chinese market: China's equity market rose with a renewal of economic activity. The supply side in China is mostly back at capacity, while consumer demand is lagging. As consumption remains a key concern, policy support continued in April, which included further interest rate cuts.

Emerging markets: Emerging markets rebounded, as governments and central banks continued to provide fiscal and monetary support to economies. The best performing region were Europe, Pakistan and India were the best performing index markets both cutting interest rates in April. By contrast, Mexico and Turkey registered more modest gains and were the weakest index markets.

Emerging Markets Shares (MSCI Emerging Markets Index, Net AUD)

Emerging market (EM) equities, in local currency terms, rose in April +8.2%, and +2.1% in AUD.

The index ended trading at a forward P/E Ratio of 11.4x and P/BV of 1.6x and equity yield (dividend) 3.4%.

Australian Listed Property (S&P/ASX 200 A-REIT Accumulation Index)

The S&P/ASX 200 Property Accumulation index bounced back in April returning +13.7% in outperforming the S&P/ASX 200 by a staggering +4.9%.

S&P/ASX Retail AREITs returned +29.6% in April, S&P/ASX Diversified AREITs returned -11.4%, S&P/ASX Industrial AREITs returned +8.4% and S&P/ASX Office AREITs returned +1.7%.

The best AREIT performers over the month were Scentre Group (SCG) (+49%), Vicinity Centres (VCX) (+44.0%) and Growthpoint Properties (GOZ) (+22.6%). Key underperformers were Cromwell Property Group (CMW) (-1.9%), Shopping Centres Australia (SCP) (-1.8%) and Dexus Property (DXS) (+0.8%).

At the end of April, the index was trading on a dividend yield of 6.1% with a P/BV 0.9x and a P/E Ratio 10.2x.

International Listed Property (FTSE EPRA/NAREIT Developed ex-Australia Index, AUD)

Globally, REITs returned +1.5% over the month of April in local currency terms. Australia was the top-performing region +24.0% in USD, the worst-performing region over the month was Japan +2.9%

At the end of April, the index was trading on a dividend yield of 4.9% with a P/B 1.3x and a P/E Ratio 16.8x.

Australian Direct Property (Atchison Consultants Unlisted Property Funds Index)

Australian direct property posted +0.9% return over 3-month period to February 2020. Investors should see a downward revaluation of the direct property sector in the coming months Capitalisation rates across property sectors continued to trend downwards. Cap rates across office, industrial and retail properties range are 5.0%, 5.3% and 5.0% respectively.

Australian Fixed Interest (Bloomberg AusBond Composite Bond Index)

Australian fixed interest returned -0.07% over the month. Australian government 10-year bond yields increased by 15bps to 0.89% (June futures contract). At this point, the 10-year Australian bond yield was 25bps above the US 10-year Treasury yield. 3-year "single A" corporate credit spreads tightened from 1.73% to 1.48%.

International Fixed Interest (Barclays Global Aggregate TR Bond Index, Hedged to AUD)

Global bond yields moved a little lower in April, with US 10-year bond yields down 2 basis points to 0.64%. Central bank purchases more than offset increased supply. The Aussie dollar moved from 61.40 to 65.11

International fixed interest returned 1.60% over the month (in AUD, as per Bloomberg Barclays' benchmark). The US corporate investment-grade (BBB) credit spread widened from 1.64% to 2.82%.

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