Our view

Researchupdate

Economic Wrap

August 2020

Summary

- Coronavirus case growth has continued to slow however countries such as India and Indonesia as well as a marked "second wave" of cases in Europe have seen average daily cases continue to climb during August. In some cases, such as Israel, lockdowns have resumed.
- The European second wave has not been met with the same level of fatalities that occurred in early April thankfully. It appears unlikely that severe lockdowns will be repeated.
- Attention is moving away from the pandemic towards geopolitical risks including the US-China relationship, US Presidential and Senate races and, UK-EU negotiations.

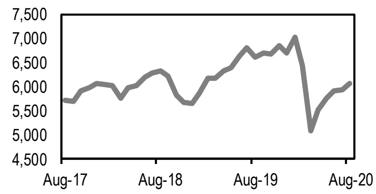
Markets – Strong performance continued for "risk on" assets (see p 11).

- Equities and high-yield bonds continued to perform strongly while safe havens such as government bonds weakened in the face of rising bond yields with investors pricing in improving global growth.
- Australian equities lagged vs global peers (see chart 2) led by a rising Australian dollar and weak banking sector performance while value stocks slightly underperformed growth names (see chart 3), continuing the experience in July. Emerging market relative weakness was a highlight of the month (see chart 4) driven by Chinese share market performance (both A-Share and H-Share Indices were up around 2% in local currency terms only).

Key economic news –

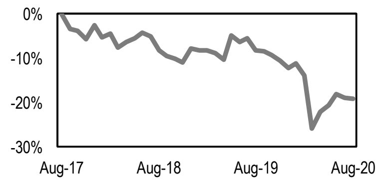
- Australia saw official confirmation of recession for the first time since the early 1990s with -0.3% and -7% quarterly growth recorded for the March and June quarters respectively in 2020.
- Leading indicators improved indicating fundamental economic strength more notable in the US and China. Chinese growth continues to be led by a stronger supply rather than demand response with retail sales continuing to disappoint. This poses additional trade issues with partners other than the US as well
- The Federal Reserve shifted to an average inflation policy target. This suggests more willingness to leave interest rates on hold even if inflation rises above the 2% target in the short run.

1. S&P/ASX 200 Price Index



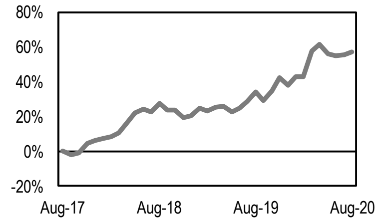
Source: Bloomberg, IOOF

2. ASX200 vs All-World, US$ terms



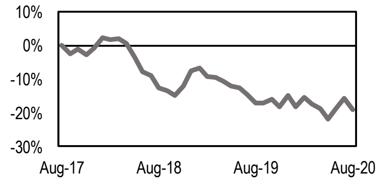
Source: Bloomberg, IOOF

3. MSCI Australia Growth relative to MSCI Australia Value



Source: Bloomberg, IOOF

4. Emerging markets vs Developed Markets, (In USD)



Sources: Bloomberg, MSCI, S&P, IOOF

Sector and stock returns

S&P/ASX 200 Sectors (GICS)

	Monthly	%∆	Quarterly	%∆
▲	Consumer Discretionary	7.78	Consumer Discretionary	16.59
▼	Consumer Staples	-0.77	Consumer Staples	7.71
▲	Energy	2.66	Energy	-5.99
▲	Financials ex Property	0.40	Financials ex Property	3.67
▲	Financials	0.40	Financials	3.67
▲	Health Care	3.93	Health Care	3.40
▲	Industrials	4.34	Industrials	-1.25
▲	IT	15.26	IT	27.80
▲	Materials	0.26	Materials	8.49
▲	Property Trusts	7.69	Property Trusts	5.42
▼	Comm Services	-5.15	Comm Services	-1.81
▼	Utilities	-5.86	Utilities	-7.35

Best and Worst S&P/ASX 200 Performers

Top five stocks		Bottom five stocks	
Monthly			
Corporate Travel Mgmt	+83.2%	Whitehaven Coal Ltd	-32.9%
IDP Education Ltd	+50.9%	Resolute Mining Ltd	-15.0%
Reliance Worldwide Corp	+42.5%	Gold Road Res Ltd	-15.0%
Mesoblast Ltd	+40.5%	Treasury Wine Estates	-14.4%
Ooh!Media Ltd	+37.3%	Resmed Inc - CDI	-13.9%
Quarterly			
Evolution Mining	+51.0%	Flight Centre	-55.5%
Appen Ltd	+48.6%	Unibail-Rodamco Wsfld	-54.7%
Promedicus	+43.0%	Ooh!Media	-52.7%
Afterpay	+42.9%	South. Cross Media	-51.7%
Nearmap	+39.2%	Credit Corp	-48.0%

Source: Bloomberg, IOOF

Equity review

Major Market Performance, August 2020

	Australian Indices	Aug-20 Price	1M return (%)	May-20 Price	3M return (%)
▲	S&P/ASX 200	6060	2.24	5756	5.30
▲	All Ordinaries	6246	3.10	5872	6.36
▲	Small Ordinaries	2820	7.07	2658	6.08
	US Indices				
▲	S&P 500	3500	7.01	3044	14.98
▲	Dow Jones	28430	7.57	25383	12.00
▲	Nasdaq	11775	9.59	9490	24.08
	Asia Pacific Indices				
▲	Hang Seng	25177	2.37	22961	9.65
▲	Nikkei 225	23140	6.59	21878	5.77
	UK & Europe Indices				
▲	FTSE 100	5964	1.12	6077	-1.86
▲	CAC40	4947	3.42	4695	5.36
▲	DAX Index	12945	5.13	11587	11.72

Sources: Bloomberg, MSCI, FTSE, S&P, IOOF

Note: return is reported on a price basis and in local currency terms e.g. S&P500 performance is in US dollars and excluding dividends.

Global equity markets

Global equity markets performed strongly during August with strength in the USA and Japan the most pronounced. Notable drivers include:

- The continued strength of US equities with Tesla climbing into the top 10 companies by market value as investors price in a rosy future for the business and chased the prospect of the stock split as a catalyst for a further rise.
- Notwithstanding weakness in the August PMI data we also saw improvement across most European economic indicators which saw a continuation of the rally in local indices. Germany stood out with its manufacturing and services sectors continuing to recover.

It is worth commenting that we have seen a remarkably long period of larger companies outperforming smaller ones since 2016 in the US as illustrated in Chart 5. In many ways this is driven by the strength of US tech names and their increased dominance and growth. At the same time however those periods of outperformance have tended to be short-lived as competition and the law of large numbers have typically seen larger businesses underperform smaller ones in share price growth eventually (this is the “size” effect in action). The drawdown in relative performance and suggestion of improving growth prospects would be supportive of including some exposure to international small caps over the long term.

5. US share market breadth (Dec-03 to Aug-20)

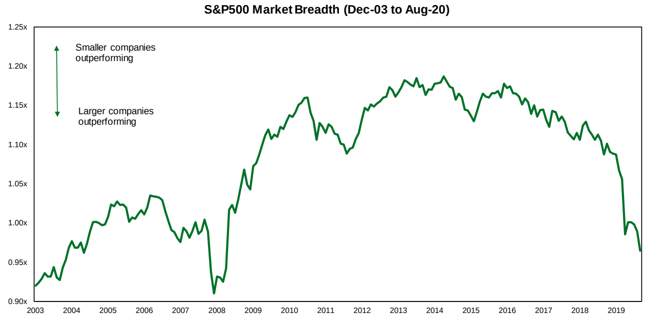


Chart 6 below highlights one driver of the dwindling market breadth in the short-term. There has been substantial large cap buying required to hedge a record uptick in call option purchases (the **blue** line below). This surge in demand has helped drive prices higher with institutional players such as Japanese tech investor, SoftBank also participating.

6. Call option notional volumes for US large caps (Jan-15 to Aug-20)

Source: @sentimentrader and @bennpeifert, 7 September 2020, url: https://twitter.com/bennpeifert/status/1302725085174755329 (accessed 12 September 2020)

Australian equity market

The S&P/ASX 200 index rose 2.2% on a price basis during August with Information Technology the top performer (up 15.3%) and most sectors in the green with the exception of Consumer Staples (down -0.8%), Communications Services (down -5.2%) and Utilities (down -5.9%). Growth stocks such as Seek and Resmed that disappointed expectations were punished substantially as were some defensive names that struggled such as Telstra (down 11%). In addition, the Utilities sector fell on the headwinds of lower electricity prices following the rise of alternative energy sources and lower electricity usage.

Style-wise we saw smaller companies outperform substantially with the Small Ordinaries up 7.2% on a total return basis. The uplift has been even more pronounced in microcaps, up 14.6% in August.

Fixed Income

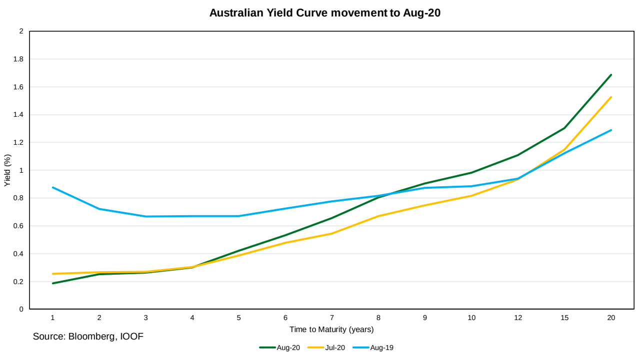
	Fixed Income	Aug-20 yield/ spread	1M mvt (bps)	May-20 yield/ Spread	3M mvt (bps)
	Australian Cash rate	0.25	--	0.25	--
▲	10-year Bond Yield	0.98	0.17	0.89	0.10
▼	3-year Bond Yield	0.26	-0.01	0.26	0.01
▼	90 Day Bank Accepted Bills SFE-Day	0.09	-0.02	0.10	-0.01
▲	US 10-year Bond Yield	0.70	0.18	0.65	0.05
▲	US 3-year Bond Yield	0.15	0.03	0.19	-0.05
	US Investment Grade spread	1.46	--	2.02	-0.56
▼	US High Yield spread	4.63	-0.21	6.37	-1.74

Source: Bloomberg, IOOF

Australian bond market

The Australian yield curve steepened during August with a notable uptick in the 10-year bond yield by 17bps to 0.98% while the 3-year yield remained flat near the RBA's target level of 0.25% (in line with its target cash rate).

7. Australian yield curve movements to August 2020



There is no change to our view that the Bank will keep rates low for a prolonged period and only slowly unwind the impact of these changes given how disruptive a sudden readjustment could be for the economy. FactSet Consensus estimates are unchanged until the end of 2022 at 0.25%.

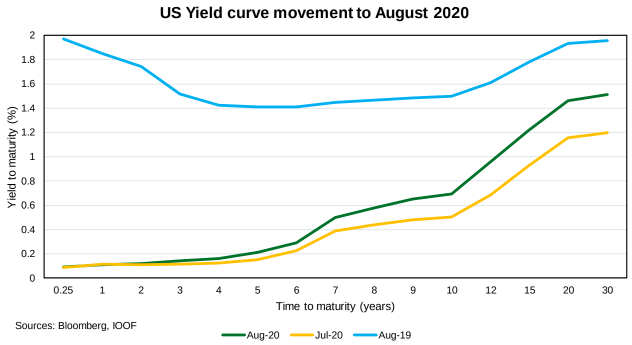
Credit spreads continued to contract during August. This saw corporate bonds outperform by 0.6% domestically favouring managers willing to take on greater exposure to credit risk. The continuation of government support favoured a stronger outlook for this debt and saw investors continue to favour a "risk-on" trade domestically. Floating rate notes also outperformed, benefitting from a similar tailwind.

Lastly, we note that the RBA has continued to support the banking system through its Term Funding Facility. This provides an alternative to other sources of funds for the Australian banking system, most notably overseas wholesale funding markets. As noted in media reports this may enable banks to shift away from this dependence in the near term and could contribute to lower rates for domestic borrowers (to the extent it is passed on).

US bond market

US Treasury yields rose, and bond prices feel as the US yield curve steepened during August. Declining coronavirus cases and deaths helped spur further relaxation of lockdown measures and we saw headline unemployment rate decline to 8.4% from 10.2%. This triggered a selloff in bonds as investors shifted to anticipating stronger economic growth.

8. US yield curve movements to August 2020



US credit spreads were flat for higher quality investment-grade businesses and contracted further for lower quality high yield issues. In part this reflects an increase in risk appetite and the recovery in oil prices with distressed energy issues a larger part of the high yield universe. It is also an acknowledgement of the tightness in investment grade spreads which are now at levels last seen in June 2019.

Lastly, we note the recent shift in Federal Reserve policy to an average inflation target of 2%. This was well-telegraphed and has implications longer-term for US monetary policy. It suggests that rate hikes will take more time to occur and implicitly acknowledges, we believe, that the Fed made a mistake in hiking too much over the 2017-18 period. We may see further news on policy shifts when the European Central Bank delivers on the policy review currently underway. This follows years of failing to hit its own inflation target and confronting deflation currently (headline flash CPI was negative for the year to August 2020).

In previous updates we had already remarked on the possibility of central banks keeping rates suppressed more than ordinarily would have. We suggested the value of inflation protection potentially and note that inflation break-evens have now recovered to more normal inflation expectations for the next 10 years from a low of 0.5% p.a. in March to 1.7% in early September.

Currencies

	Currencies	Aug-20 Price	1M return (%)	May-20 Price	3M return (%)
▲	$A vs $US	73.76	3.26	66.67	10.63
▲	$A vs GBP	55.17	1.06	53.98	2.21
▲	$A vs YEN	78.12	3.35	71.92	8.62
▲	$A vs EUR	61.79	1.88	60.07	2.86
▲	$A vs $NZ	109.54	1.66	107.48	1.92
▲	$A TWI	62.60	1.13	58.80	6.46
▼	$US vs EUR	83.78	-1.32	90.06	-6.97
▼	$US vs CNY	6.85	-1.82	7.14	-4.05
▼	$US vs GBP	74.80	-2.12	80.95	-7.60
▲	$US vs JPY	105.91	0.08	107.83	-1.78
▼	$US vs CHF	90.37	-1.01	96.16	-6.02
▼	US Dollar Index	92.14	-1.29	98.34	-6.30
▼	JPM EM Currency Index	55.33	-0.49	54.77	1.01

Source: Bloomberg, IOOF

The Australian dollar (AUD) rose 3.3% against the US Dollar (USD) during August, up from USD 0.7143 to USD 0.7376.

Relative economic strength was not as pronounced a factor in August with the Services sector slipping into slight contraction and other economic data disappointing slightly. However, strength in commodity prices, most notably iron ore, supported a strong bid in the **Australian dollar**. Another factor was portfolio flows with investors attracted by the stronger bond yields on offer here relative to other countries. The RBA has come out noting the strength of the AUD and its unhelpfulness for the economic recovery underway (because it makes out export sectors less competitive). However, its current position suggests active intervention is unlikely. We do note the potential for "jawboning" or "talking down" AUD strength in a bid to compel a market reaction. This is a softer policy choice that the RBA could follow if AUD strength continues to persist.

Ongoing weakness in the **US Dollar** was again a feature with the US Dollar Index falling 1.2% in August as it saw a broad-based depreciation against major currencies with the exception of the Japanese Yen, the latter result driven by the resignation of prominent Japanese leader Shinzo Abe. We are continuing to see mean reversion for USD on a purchasing power parity basis against other major countries after a period of overvaluation. At the end of 2019 for instance the Euro was ~26% undervalued vs USD on this measure. Reduced carry with the decline in US interest rates has been another factor as it lowers the relative attractiveness of holding USD. We saw emerging market currencies falter slightly vs the US Dollar, down -0.5% due to weaker performance from Latin American currencies.

Commodities

	Commodities	Aug-20 Price	1M return (%)	May-20 Price	3M return (%)
▲	Aluminium	1772	4.41	1554	14.01
▲	Copper	306	5.92	245	24.78
▲	Nickel	15344	11.48	12339	24.35
▲	Zinc	2498	7.92	1989	25.59
▲	Crude Oil – Brent	45.28	4.57	35.33	28.16
▲	Natural Gas	2.63	46.19	1.85	42.24
	Metallurgical Coal	130	--	143	-9.16
▼	Thermal Coal	48	-4.23	55	-11.03
▲	Iron Ore	122.53	12.52	92.54	32.41
▼	Gold	1979	-0.37	1766	12.06
▲	Silver	29	16.86	19	53.08

Source: Bloomberg, IOOF

Oil prices continued to recover during August. Signs of stronger global growth including slowing coronavirus cases in the US played an important role for energy demand. We also continue to see loss-making production shutdown with major producers cutting back and US shale oil remaining depressed. The Baker Hughes oil rig count remains at low levels with only 176 oil rigs functioning as of early August compared with the 683 operating in early March this year.

Precious metals saw mixed performance by contrast with gold flat whilst silver saw a strong surge. This was arguably a case of mean reversion with silver trading at a substantial discount to gold earlier in the year. In addition, improving global growth benefits silver given its usage in industrial applications. The fall in gold may also be attributable to rising bond yields which increase the relative attractiveness of bonds over precious metals as a safe asset.

Base metals such as Copper and Aluminium saw continued price strength. In the case of copper, we have seen inventories fall substantially with those at the London Metals Exchange at their lowest level in almost 15 years. It also comes against a backdrop of declining copper production longer-term and strong demand out of China for construction and supported by government stimulus. Nickel prices also saw strong performance with a continued ban on Indonesian exports amidst growing battery demand.

Iron ore prices continued to see strong support from Chinese demand which has remained elevated even as Brazilian supply has recovered. **Thermal coal** prices remain a point of weakness as lower energy demand particularly in South-East Asia has seen coal demand continue to decline.

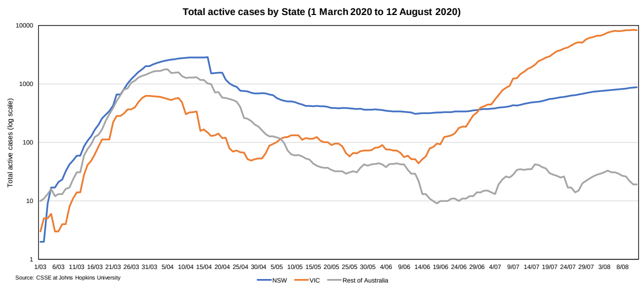
Australia

Victorian lockdown measures will continue persisting in the near term and the recent extension suggests they will drag on the economy into the December quarter. On the positive side we should see further stimulus being implemented via tax cuts while the rebound in consumer confidence is important to support spending across the economy.

Coronavirus pandemic

The Victorian outbreak slowdown we saw in early August continued as we saw case growth slow materially from a peak of 533 cases a day (7-day average) to 42 as of 12 September. NSW cases continued to remain contained during the month with the spike experienced in Victoria not being repeated to date as daily case growth has not risen above 20 cases throughout the Victorian second wave. Sadly, however we continued to see deaths rise in Victoria with those in aged care facilities the worst hit. The death toll there has risen to over 700 since the second spike began. In addition, Premier Andrew has announced an extension of harsher lockdown measures until the end of October. These will be relaxed gradually with some high hurdles required to be met including zero case growth for two weeks to move from Level 3 to Level 2 restrictions.

9. Australian active coronavirus cases by State (Mar-20 to Sep-20)



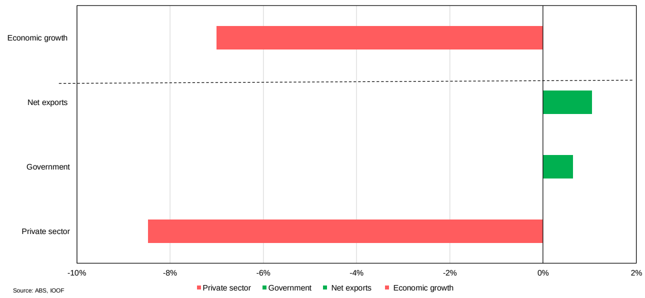
It appears that by the end of 2020 we will have some resumption of inter-state travel across most of the country with Western Australia a laggard. This will foster a further recovery in economic activity during the December quarter and beyond. However, this must be balanced against the damage that extended Victorian restrictions will likely cause. The lockdown will likely delay the economic recovery underway and extend the damage being done in the September quarter into the December quarter as well.

Policy

Speculation on further fiscal support continued into August. It appears likely that the government will bring forward its legislated personal income tax cuts (that were due to occur in FY22) following the October Budget announcement. In addition, we would anticipate more being done on the deregulation front in line with the Government's policy agenda. Business investment allowances and State government infrastructure spending would also be potential areas we are watching. On balance, these are welcome efforts but there will likely be a period of economic weakness as policy supports are removed given the scale of the injection currently underway.

Economic growth

10. Quarterly economic growth to June 2020 split by contribution



Australian economic growth disappointed expectations, falling -7% (consensus: -6.2%) during the June quarter. At a high level, the impact of lockdowns saw private sector consumer and investment spending fall, contributing over 8% to this decline. Net exports and government spending were positive offsets but unable to counter the full decline.

The Westpac-MI Leading Index continues to improve gradually rising to -4.37% in July, up from -4.44% in June. This continues to suggest negative growth over the next 3-9 months, but gradual improvement suggests April was the bottom for our economy.

Consumer and Business Sentiment

The NAB Monthly Business Survey for August was mixed with business confidence improving from depressed levels in July (although still negative) while business conditions deteriorated. The latter result was caused by a sharp decline in the employment index as well as trading and profitability sub-indices. The employment result suggests the potential for further labour market weakness with businesses remaining at below-average levels of capacity utilisation.

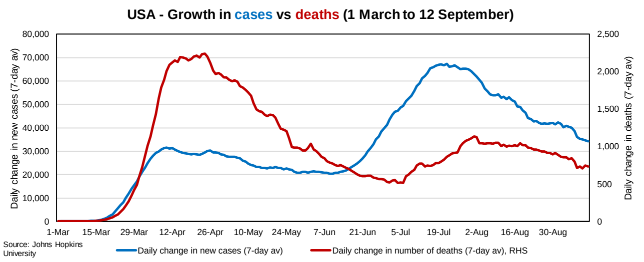
The Westpac-MI Index of Consumer Sentiment saw a pronounced bounce back in September, rising by 14.3 points from 79.5 to 93.8. Improving confidence of household finances tied to sizeable fiscal support was one notable driver. We also saw improving confidence in purchasing major household items as well as property. Interestingly the outlook for property prices remains subdued at some 37% below the 6-month average level prior to the coronavirus outbreak. Overall, the result suggested household spending should provide a positive support for the economy.

United States of America

Policy deadlock in Washington continued into August. Leading indicators suggest the economy is continuing to recover with limited impact from stimulus withdrawal thus far. Attention is focusing on the upcoming Presidential and Senate races with Democrat candidate Joe Biden the favourite against incumbent President Trump.

Coronavirus pandemic update

11. Total US case growth by region, 7-day average (Mar-20 to Sep-20)



Daily new case growth has continued to moderate since peaking in mid-July. After a period of being elevated we saw a similar result for coronavirus deaths as well with a steady decline beginning from mid-August. The unwind of lockdown restrictions in US States is providing a tailwind for growth and allowing for a return to normal business settings within the US with unemployment still at elevated levels but gradually falling.

We note that continued claims rose slightly in early September one of the first signs of potential weakness that we will monitor closely. The jobs recovery challenge for the US far exceeds what we saw following the global financial crisis (continued claims peaked at 6.6m then vs 13.4m currently) and remains a point of concern particularly if fiscal support is withdrawn too early.

Policy update

Additional fiscal stimulus remains in a deadlock between the Democrat and Republic parties. It now appears unlikely for this to happen prior to the November Elections. That will leave a challenge for the victor in the Presidential race to address with much hinging on how the Senate race transpires as well, specifically whether the President's party will control both Houses of government and be able to pass legislation without lengthy negotiation efforts.

A looming 1 October deadline will also require bipartisanship to prevent a US government shutdown. We expect this to occur but note that this self-imposed risk has become reality in the past. If that were to occur, we and other market participants would revise our expectations for US growth lower particularly given the weak economic environment.

Geopolitics

Tensions with China continued into August. Amidst further rhetoric from President Trump we saw the US Treasury release a report calling for the delisting of businesses that refused to subject their auditing records to US scrutiny. China is a clear target of these efforts given their long-standing refusal to cooperate with US authorities. The move comes at a time where one such Chinese company Luckin Coffee was delisted from the Nasdaq for accounting fraud after soaring to an all-time high in early 2020.

Separately US and Chinese representatives still appear in favour of keeping the Phase 1 trade agreement alive and operational with no substantive efforts to unwind it following talks in August. Trade at present appears be segregated from other foreign policy concerns such as national security.

Economic growth

Leading indicators continue to improve for the US with the ECRI Weekly Leading Economic Index and the Conference Board's Leading Economic both recovering further during August. This suggests a low risk of a second trough in economic activity in the short run.

Despite the ending of generous unemployment insurance supplements there has not yet been a material decline in consumer spending. This may partly be due to a seasonal "back to school" uptick in consumer spending but even weekly data series such as the Redbook Index are not yet ticking materially lower and as of late August have shifted to be positive year-on-year. Continued strength in housing starts and new business formation are other near-term indicators strengthening our convictions at present.

Sentiment

The IHS Markit Composite PMI improved to 54.6 in August, up from 50.3 in July and its strongest reading since March 2019. A key driver was the first uptick in new business orders since February this year with the strength broad-based as new export orders also resumed growing. Employment picked up as well (the unemployment rate fell to 8.4% in August, down from 10.2%). The strength in services businesses was led by financial and business services as well as the tech sector whilst those reliant on free movement such as tourism and recreation continue to struggle from social distancing rules. Uncertainty over the upcoming Presidential election and future policy changes poses a challenge for business confidence.

US manufacturers also saw a pleasing bounce in export growth with new export orders rising at their fastest rate in four years with a return to expansion. Dollar weakness is likely to have played a part here.

China

The Chinese economy continues to recover from its February lows largely as a supply-led response to government stimulus encouraging infrastructure and construction spending. While domestic activity is getting back to normality, the weaker global economy continues posing challenges for China's exporting industries.

Business activity and sentiment

The Caixin China Services PMI fell slightly to 54 in August, down from 54.1 in July, a sign of continued recovery albeit at a slower pace. New orders increased further but at a slower pace, below the long-run series average, driven by a fall in new export orders for a second month. The recovery in services sector demand remains domestic-led and pleasingly saw the first increase in hiring since January to meet the new order requirements. Services firms continue to remain confident on the economic outlook, but the degree of confidence slipped to a three-month low with concerns on the pandemic impact for sales in the months ahead.

The Caixin China Manufacturing PMI picked up further, rising from 52.8 in July to 53.1 in August. The notable driver was again stronger output and new business growth. Total new order growth expanded at the fastest rate since the beginning of 2011 with manufacturers seeing their first uptick in new export sales since December 2019. This uptick helped drive an expansion in output with the shedding of jobs stabilising at its slowest contraction in 2020.

The combination of results saw the Chinese Composite PMI rise to 55.1, up from 54.5 in July. The weakness in services sector sales saw overall new order growth hit a three-month low. The improvement in new hires for services was a welcome development but more progress on the recovery, particularly overseas as well as government support are likely to be required before the jobs market improves further.

Economic growth

Chinese retail sales fell -1.1% for the year to July versus a 4.8% rise in industrial output highlighting the supply-led nature of the economic recovery. For momentum to be sustained we would prefer to see stronger recovery in consumer demand as a sign of stronger consumer confidence. However as highlighted above this is difficult to anticipate in the near term given weakness still present within the jobs market with Chinese firms reluctant to expand new hiring until they see stronger demand.

Inflation

The Producer Price Index (PPI) fell -2% for the year to January, in line with expectations, while the Consumer Price Index (CPI) rose 2.4% over the same period, also in line with consensus. The weakness in producer prices suggests limited inflationary pressures within the Chinese economy and marks a seventh consecutive month of annual declines. In this case the fall was at its slowest rate since March this year (the bottom of the trough in economic activity) suggesting we are nearing more normal economic conditions. At present however inflation is well-contained, a far cry from the price shock induced by food prices early this year.

Trade

Chinese exports rose for a third-consecutive month and 9.5% for the year to August, the strongest increase since March 2019 (consensus: 7.1%). Disappointingly imports fell -2.1% over the same period (consensus: +0.1%) reflecting a weaker demand dynamic domestically. The overall result saw the trade balance at $58.9bn (consensus: $9.2bn). This may reappear as an issue in the future with China arguably benefitting from the fiscal support of other countries that drove demand for its exports. A lack of similar measures (at scale) within China has seen the country's trade surplus expand sizeably not only against the US but also against Europe. We already saw what these imbalances can lead to with the trade conflict instigated by President Trump and arguably, the ground is being laid for more of the same.

Geopolitics

President Trump has outlined an unwillingness to extend the deadline for Chinese firm ByteDance to divest itself of the US operations for its leading social media app TikTok. Unless the app is sold to a buyer without national security concerns it will be shut down on 15 September. As commented previously this move should not be seen in a vacuum given China's long-standing protectionist stance to online rivals within its own country. Apple is one of the few large companies to operate substantially within China and has had to oblige with substantial efforts to comply with Chinese censorship and controls.

It appears that China and India have come to an initial compromise on recent border clashes. Diplomatic officials from both have reached a five-point consensus on easing tensions in the near term. This is a positive development as it reduces the risk of a more severe conflict between the two nuclear powers.

Europe

A second wave of coronavirus cases continued across Europe with Spain and France the epicentres. This wave has not been as deadly as the early April experience on a positive note. Negotiations for implementing the European Recovery Fund continue to move forward. Brexit concerns emerged as the UK nears a deadline for finalising a formal trade agreement with the EU.

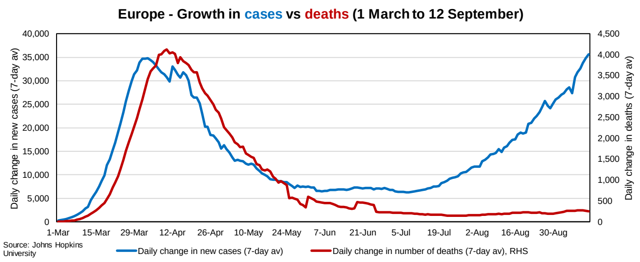
United Kingdom

Brexit concerns are beginning to reappear as we approach the deadline for a finalised transition from the EU. The latest development includes a bill by the UK government to rewrite sections of the withdrawal agreement it signed back in January. These changes pertain to the border between Northern Ireland (part of the UK) and the Republic of Ireland (part of the EU) whereas the Withdrawal Agreement is meant to be followed by both the UK and EU. The EU has given an ultimatum until the end of September to withdraw the bill and it remains to be seen if it is a negotiating ploy. It remains to be seen how negotiations will move forward given both the UK and EU appear to be at an impasse. While we believe there is scope for compromise (and indeed this would be our base) we do note the adverse scenario of reverting to WTO trade rules and tariff barriers. This would exacerbate the economic weakness of both the UK and EU but in our view would be a localised downside risk.

Pleasingly we saw the UK Composite PMI rise to its highest level since August 2014 reaching 59.1, up from 57 in July. While a welcome result it largely reflects pent-up domestic demand with job losses continuing, this time at their fastest rate since May. The ending of government wage subsidies (arguably at too early a juncture) raises the risk of weaker economic momentum in the near term.

Coronavirus pandemic

12. Daily case vs fatality growth in Europe (Mar-20 to Sep-20)



Source: Johns Hopkins University

Over the course of August and continuing into September we saw daily case growth escalate across Europe. The daily case growth 7-day average rose from 11.6k as at 31 July to 35.6k as at 12 September. This was driven by several countries including Spain and France. However, even with a more pronounced surge than last month, the level of deaths (the **red** line in Chart 12) has thankfully remained low. Other observers note hospitalisations in France for instance have remained subdued while ticking up in Spain slightly. Possible explanations include virus mutation into less severe strains, greater population immunity than previously anticipated or a shift in the age distribution where vulnerable, older citizens have not been infected in the same rate as seen in early April.

Policy

Efforts to gain the necessary approvals for the European Recovery Fund remain underway. There are concerns at opposition from some EU member states such as Hungary over the conditions attached which may delay the raising and subsequent release of funds. Harder-hit countries such as Spain and Italy are pushing for a faster resolution given their greater need.

The ECB reiterated its plans to keep interest rates low until inflation neared its 2% target. It also continued its emergency bond purchasing programme until June 2021 at a minimum or beyond this point until it feels the crisis phase caused by the coronavirus has ended. Somewhat surprisingly given the scale of the rally, ECB Governor Lagarde would not comment on the strength of the Euro and its complications for the economic recovery. As the EU is reliant on its export sector a strong currency poses a substantial challenge to exporters by reducing their competitiveness with the rest of the world.

Business Activity and Economic growth

European PMI surveys softened in August. The IHS Markit Eurozone Composite fell to 51.9 in August, down from 54.9 in July, while the Manufacturing PMI softened fractionally to 51.7, down from 51.8 over the same period. While these readings were above 50 and indicating expansion, the pace of the recovery moderated. This was largely due to weakness in the services sector where concerns over the rise in coronavirus infections saw business confidence falter. Social distancing restrictions in countries such as Spain and Italy remain a challenge according to IHS Markit. In addition, foreign trade for services firms remains a challenge with new export business continuing to decline for two years. Manufacturing performance was stronger by contrast but even here concerns persist. Businesses are rallying on a release of pent-up demand but worries over how sustained this will be has prevented further investment and workforce hiring. On the latter, European manufacturers continued to reduce staff albeit at the slowest rate since March. Overall, this result suggests the recovery remains underway but fragile with policy support still required.

Company news (Notable strong and weak performers during the month of August 2020)

Corporate Travel Management (+83.2%)

Corporate Travel Management (CTD) delivered a better than expected FY20 result after an aggressive cost cutting program and provision of essential travel services (government and mining clients) saw its cash burn contained to $3m/month. CTD reported a better than expected net loss of -$8.2m (vs. a profit of $86.2m pcp) and EBIT of $74.4m (vs. consensus $65m). Although global travel restrictions have severely impacted on CTD's earnings, the outlook was encouraging, with management highlighting a high level of pent-up demand and the ability to run a profitable business solely servicing domestic travel needs in key North American, European, and Australian markets while border restrictions remain. No final dividend was declared.

IDP Education Ltd (+50.9%)

IDP Education (IEL) reported a strong FY20 result which was supported by digital initiatives that allowed IEL to navigate through the pandemic better than expected. Revenue decreased -1.8% to $587m, however, EBIT increased +11.0% to $107.8m as a result of margin expansion from cost saving initiatives and the lower cost of customer acquisition from digital initiatives. The rollout of an online "at-home" IELTS test, virtual events, and virtual counselling, allowed IEL to maintain a level of earnings despite physical locations being closed. No final dividend was declared for FY20.

Reliance Worldwide Corp Ltd (+42.5%)

Reliance Worldwide (RWC) announced FY20 results with sales up +5% pcp to $1.16bn, however underlying EBIT fell -9% to $251.3m as a result of weaker APAC sales. Americas delivered +6% constant currency (CC) revenue growth to $495.8m, which benefitted from positive COVID-19 impacts (home renovations), however APAC sales fell -2% and APAC EBIT fell -18% reflecting higher non-recurring ERP and supply chain costs. EMEA was also negatively impacted by COVID-19 with 2H20 sales falling -24% CC as UK lockdown restrictions limited distribution and plumber activity. A final dividend of 2.5cps was declared.

Whitehaven Coal Ltd (-32.9%)

Whitehaven Coal (WHC) reported disappointing FY20 results with revenue declining -30.8% pcp to $1.7bn and NPAT -94.7% to $30.0m as a result of operational issues and a continued slide in the coking coal price. After reaching a high of $120/tonne in June 2018, coking coal has experienced a continued slide downward, fetching only $45 on the spot market in Aug 2020. WHC also experienced disruptions after bushfires impacted operations in its Maules Creek mine, which forced it to cut production forecast by 2m tonnes to 10-11m tonnes. No final dividend was declared for FY20.

Resolute Mining Ltd (-15%)

Resolute Mining (RSG) released 1H20 results with revenue with Gold production up +24%, revenue up +33% and underlying EBITDA up +96%. The positive results were overshadowed by investor concerns on political risk after the resignation of President Ibrahim Boubacar Keita in Mali, the subsequent dissolution of government, and actions by the country's military to resolve the political crisis.

Treasury Wine Estates Ltd (-14.4%)

Treasury Wine Estates (TWE) reported FY20 results with revenue down -7.1% to $2.7bn and EBITS down -21.7% to $533.5m as expansion activity and a supply chain restructure produced elevated costs. Although the result was not unexpected, investor concern revolved around an announcement by China's Ministry of Commerce which said it would begin investigation allegations the Australian wine industry was receiving subsidies and selling into the mainland market below cost.

Sources: ASX company announcements, Bloomberg, *Australian Financial Review*, *Sydney Morning Herald*

Movers and Shakers for the month of August 2020

ASX Code	Company Name	Closing price ($)	Month ago, close ($)	Month Δ (%)	Quarter ago close ($)	Quarter Δ (%)	Year ago, close ($)	Year Δ (%)
CTD	Corporate Travel Management	15.99	8.73	83.2	11.99	33.4	17.37	-7.9
IEL	IDP Education Ltd	20.07	13.30	50.9	17.03	17.9	16.62	20.8
RWC	Reliance Worldwide Corp Ltd	3.82	2.68	42.5	3.06	24.8	3.83	-0.3
MSB	Mesoblast Ltd	5.31	3.78	40.5	4.00	32.8	1.44	270.0
OML	Ooh!Media Ltd	1.03	0.75	37.3	1.08	-4.6	2.50	-58.9
ARB	Arb Corp Ltd	26.32	19.20	37.1	17.04	54.5	18.82	39.9
WTC	Wisetech Global Ltd	28.18	20.65	36.5	20.39	38.2	36.93	-23.7
NEA	Nearmap Ltd	3.08	2.28	35.1	2.29	34.5	2.73	12.8
APT	Afterpay Ltd	91.44	68.54	33.4	47.41	92.9	30.98	195.2
WEB	Webjet Ltd	3.72	2.83	31.4	4.14	-10.1	8.98	-58.6

Source: Bloomberg, IOOF

ASX Code	Company Name	Closing price ($)	Month ago, close ($)	Month Δ (%)	Quarter ago close ($)	Quarter Δ (%)	Year ago close ($)	Year Δ (%)
WHC	Whitehaven Coal Ltd	0.93	1.39	-32.9	1.81	-48.6	3.43	-72.9
RSG	Resolute Mining Ltd	1.11	1.30	-15.0	1.14	-3.1	1.67	-33.8
GOR	Gold Road Resources Ltd	1.56	1.84	-15.0	1.81	-13.8	1.31	19.1
TWE	Treasury Wine Estates Ltd	9.25	10.80	-14.4	9.66	-4.2	18.74	-50.6
RMD	Resmed Inc - CDI	24.36	28.28	-13.9	23.72	2.7	20.59	18.3
TLS	Telstra Corp Ltd	2.89	3.35	-13.7	3.24	-10.8	3.72	-22.3
SAR	Saracen Mineral Holdings Ltd	5.22	6.00	-13.0	5.11	2.2	3.57	46.2
ORE	Orocobre Ltd	2.60	2.97	-12.5	2.35	10.6	2.45	6.1
BVS	Bravura Solutions Ltd	3.67	4.18	-12.2	4.85	-24.3	4.89	-24.9
COE	Cooper Energy Ltd	0.33	0.38	-12.0	0.42	-20.5	0.58	-42.6

Source: Bloomberg, IOOF

Long-term asset class performance to August 2020 (Total returns in AUD)

				Annualised						
Asset class	**1-mth**	**3-mth**	**6-mth**	**1-yr**	**3-yr**	**5-yr**	**7-yr**	**10-yr**	**15-yr**	**20-yr**
Australian equities (S&P/ASX 200)	2.8%	6.0%	-4.5%	-5.1%	6.1%	7.5%	6.8%	7.8%	6.6%	7.6%
Australian equities - Mid caps	6.3%	13.0%	9.2%	6.5%	9.3%	12.3%	12.4%	10.2%	7.3%	10.3%
Australian equities - Small caps	7.2%	6.6%	4.6%	2.1%	8.0%	10.5%	6.9%	4.7%	4.0%	5.5%
Australian equities - Micro caps	14.6%	24.2%	22.9%	11.8%	10.9%	13.1%	7.4%	3.2%	4.6%	#N/A
International equities	3.5%	2.9%	1.1%	6.7%	12.6%	9.6%	12.8%	13.0%	7.2%	3.5%
International equities (Hedged)	6.2%	12.2%	11.8%	12.1%	8.9%	10.3%	11.2%	12.8%	8.4%	#N/A
International equities - Small caps	2.2%	1.2%	-4.8%	-2.4%	6.9%	6.7%	10.6%	12.2%	7.2%	6.5%
Emerging Markets equities	-0.9%	7.3%	-3.0%	4.3%	5.3%	7.7%	7.7%	5.7%	6.7%	#N/A
Australian REITs	7.9%	7.0%	-15.5%	-17.7%	4.4%	5.8%	8.9%	9.6%	3.4%	6.4%
Global REITs	-0.6%	-3.0%	-21.9%	-21.4%	1.8%	2.0%	6.8%	7.9%	4.3%	#N/A
Global REITs (Hedged)	2.0%	5.5%	-14.1%	-17.4%	-1.2%	2.6%	5.4%	7.7%	5.0%	#N/A
Global Infrastructure	-2.7%	-9.3%	-16.2%	-13.9%	4.8%	5.9%	9.9%	10.4%	#N/A	#N/A
Global Infrastructure (Hedged)	-0.3%	-1.4%	-6.6%	-8.2%	2.5%	6.8%	8.7%	10.6%	#N/A	#N/A
Trend following	-3.0%	-9.1%	-9.8%	-13.5%	3.8%	-2.0%	5.7%	3.1%	3.7%	4.4%
Australian bonds	-0.4%	0.3%	0.3%	1.6%	5.5%	4.4%	5.0%	5.4%	5.7%	6.0%
Australian bonds - government	-0.5%	0.0%	0.0%	1.3%	5.7%	4.4%	5.1%	5.3%	5.7%	6.0%
Australian bonds – corporate	0.1%	1.8%	1.1%	2.9%	5.3%	4.7%	5.1%	5.8%	6.0%	6.2%
Australian bonds - floating rate	0.1%	0.8%	1.0%	1.8%	2.4%	2.7%	3.0%	3.8%	4.4%	4.7%
Global bonds (Hedged)	-0.8%	0.7%	0.7%	2.4%	4.3%	4.6%	5.3%	5.7%	6.4%	7.1%
Global bonds - government (Hedged)	-1.0%	-0.2%	0.4%	1.6%	4.4%	4.5%	5.3%	5.6%	6.3%	#N/A
Global bonds - corporate (Hedged)	-1.0%	3.3%	1.2%	4.0%	5.0%	5.7%	6.1%	6.7%	6.8%	#N/A
Global bonds - High Yield (Hedged)	1.3%	7.0%	0.1%	1.9%	2.8%	6.0%	6.2%	8.3%	8.6%	#N/A
Emerging Market bonds (Hedged)	0.4%	7.7%	-0.3%	1.1%	3.1%	6.1%	6.8%	7.1%	8.2%	9.9%
Cash (AUD)	0.0%	0.0%	0.2%	0.7%	1.4%	1.7%	1.9%	2.6%	3.6%	4.1%

Sources: Bloomberg, IOOF calculations

* AUD total returns as at Aug-20 assuming reinvestment of dividends
** Returns reflect index performance excluding any fees; Actual ETF/managed fund performance will vary due to both fees and tracking error.

Appendix – Index sources

Asset class	Index
Australian equities (S&P/ASX 200)	S&P/ASX 200 Accumulation Index
Australian equities - Mid caps	S&P/ASX Accumulation Midcap 50 Index
Australian equities - Small caps	S&P/ASX Accumulation Small Cap Ordinaries Index
Australian equities - Micro caps	S&P/ASX Emerging Companies Total Return Index
International equities	MSCI World ex Australia Net Total Return (in AUD)
International equities (Hedged)	MSCI World ex Australia Hedged AUD Net Total Return Index
International equities - Small caps	MSCI World Small Cap Net Total Return USD Index (in AUD)
Emerging Markets equities	MSCI Emerging Markets EM Net Total Return AUD Index
Australian REITs	S&P/ASX 200 A-REIT Accumulation Index
Global REITs	FTSE EPRA/NAREIT Developed Index Net Total Return (in AUD)
Global REITs (Hedged)	FTSE EPRA/NAREIT Developed Index Net Total Return (Hedged to AUD)
Global Infrastructure	FTSE Global Core Infrastructure 50/50 Net Total Return in AUD
Global Infrastructure (Hedged)	FTSE Global Core Infrastructure 50/50 100% Hedged to AUD Net Tax Index
Trend following	SGI Cross Asset Trend Following Index (AUD)
Australian bonds	Bloomberg AusBond Composite 0+ Yr Index
Australian bonds - government	Bloomberg AusBond Govt 0+ Yr Index
Australian bonds – corporate	Bloomberg AusBond Credit 0+ Yr Index
Australian bonds - floating rate	Bloomberg AusBond Credit FRN 0+ Yr Index
Global bonds (Hedged)	Bloomberg Barclays Global Aggregate Total Return Index Value Hedged AUD
Global bonds - government (Hedged)	Bloomberg Barclays Global Aggregate Treasuries Total Return Index Hedged AUD
Global bonds - corporate (Hedged)	Bloomberg Barclays Global Aggregate Corporate Total Return Index Hedged AUD
Global bonds - High Yield (Hedged)	Bloomberg Barclays Global High Yield Total Return Index Hedged AUD
Emerging Market bonds (Hedged)	J.P. Morgan EMBI Global Core Hedged Index Level AUD
Cash (AUD)	Bloomberg AusBond Bank Bill Index

Research Analyst – Cameron Curko

Approved By – Matt Olsen

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