Australian Monthly Wrap

February Monthly Wrap

Summary

- The COVID-19 (a.k.a. coronavirus) outbreak climbed higher during February with the concern globally about cases outside of China and its potential health and economic impact.
- The trend for risk assets moved from emerging markets to developed markets particularly the US which saw a major sell off in the last week of February. This has continued into March.
- The J.P. Morgan Global Composite PMI slipped into contractionary territory reflecting the shutdown in activity within China to curb the outbreak there as well as weakness in the US.
- The escalation of new cases towards the end of February and into March have cast doubt on how quickly global growth can recover from the shock. This has been exacerbated by a new shock in early March where a collapsed OPEC deal saw oil prices plunge.

Markets – Bid for bonds and bond proxies a standout shift from Dec-19 continuing into this month (see page 11).

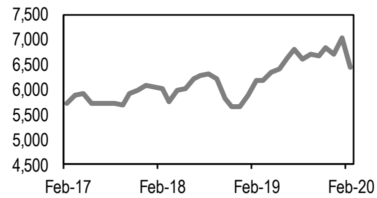
- Australian equities underperformed vs global peers (see chart 2) while growth stocks were flat against value stocks (see chart 3).
- Emerging markets outperformed (see chart 4) led by the Hang Seng Index (down only 0.7%). Coronavirus outbreaks outside of China triggered a selloff in developed markets.

Key economic news –

- The Federal Reserve and Reserve Bank of Australia both cut interest rates subsequent to month-end by 1.5% and 0.25% respectively.
- The coronavirus outbreak has triggered plans for government stimulus across the world following concerns over the impact of limited economic activity from public health responses to counter the outbreak.

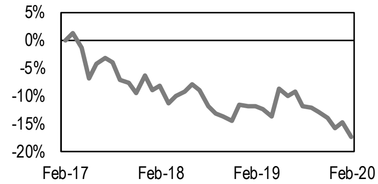
Key company news – Reporting season saw some notable outperformers notwithstanding the virus outbreaks globally. IDP Education (ASX: IEL) and Fisher & Paykel Healthcare (ASX: FPH) were notable standouts. By contrast Wisetech Global (ASX: WTC) and Beach Energy (ASX: BPT) saw earnings misses and commodity price falls respectively that saw their share prices sell off substantially.

1. S&P/ASX 200 Price Index



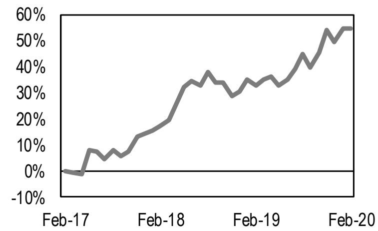
Source: Bloomberg, IOOF

2. ASX200 vs All-World, US$ terms



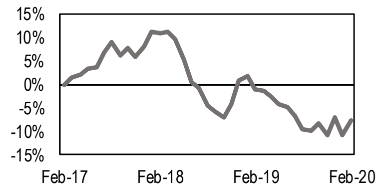
Source: Bloomberg, IOOF

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

ASX/S&P 200 Sectors (GICS)

	Monthly	%Δ	Quarterly	%Δ
▼	Consumer Discretionary	-9.68	Consumer Discretionary	-7.88
▼	Consumer Staples	-7.55	Consumer Staples	-8.07
▼	Energy	-18.16	Energy	-18.83
▼	Financials ex Property	-5.61	Financials ex Property	-2.80
▼	Financials	-5.61	Financials	-2.80
▼	Health Care	-3.76	Health Care	4.94
▼	Industrials	-8.50	Industrials	-10.22
▼	IT	-17.62	IT	-12.66
▼	Materials	-11.89	Materials	-8.96
▼	Property Trusts	-5.29	Property Trusts	-5.28
▼	Telecommunications	-9.97	Telecommunications	-8.32
▼	Utilities	-4.54	Utilities	-4.00

Best and Worst S&P/ASX 200 Performers

Top five stocks		Bottom five stocks	
Monthly			
IDP Education Ltd	+19.6%	Wisetech Global Ltd	-39.7%
Cleanaway Waste Mgmt	+11.3%	Clinuvel Pharma Ltd	-35.8%
Fisher & Paykel Healthcare	+10.1%	Beach Energy Ltd	-34.3%
Pinnacle Invest Mgmt	+9.2%	EML Payments Ltd	-31.2%
Evolution Mining Ltd	+8.9%	Link Admin Holdings	-31.0%
Quarterly			
Silver Lake Resources Ltd	+44.6%	Jumbo Interactive Ltd	-46.2%
Northern Star Res Ltd	+40.4%	Wisetech Global Ltd	-44.6%
Gold Road Resources Ltd	+28.3%	Nearmap Ltd	-41.3%
Polynovo Ltd	+27.9%	Treasury Wine Est Ltd	-41.0%
Saracen Mineral Hldgs Ltd	+22.4%	Clinuvel Pharma Ltd	-36.8%

Source: Bloomberg, IOOF

Equity review

Major Market Performance, February 2020

	Australian Indices	Feb-20 Price	1M return (%)	Nov-19 Price	3M return (%)
▼	S&P/ASX 200	6441	-8.21	6846	-5.91
▼	All Ordinaries	6512	-8.56	6948	-6.28
▼	Small Ordinaries	2728	-8.92	2916	-6.44
	US Indices				
▼	S&P 500	2954	-8.41	3141	-5.95
▼	Dow Jones	25409	-10.07	28051	-9.42
▼	Nasdaq	8567	-6.38	8665	-1.13
	Asia Pacific Indices				
▼	Hang Seng	26130	-0.69	26346	-0.82
▼	Nikkei 225	21143	-8.89	23294	-9.23
	UK & Europe Indices				
▼	FTSE 100	6581	-9.68	7347	-10.43
▼	CAC40	5310	-8.55	5905	-10.08
▼	DAX Index	11890	-8.41	13236	-10.17

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

The S&P 500 index finished the month down -8.4% while the tech-heavy NASDAQ index was down -6.4%. Intra-month markets moved substantially with positive performance during most of February before selling off substantially in the last week of February. International markets also fell during the month (in local currency terms) led by weakness in Europe.

The key driver was growth in coronavirus cases outside of China. Investors grew concerned about the economic impact of spikes in new cases from South Korea, Italy and Iran. The chief issue for investors is the economic shock that will result from shutting down trade and travel between and within countries.

Australian equity market

The S&P/ASX 200 index fell 8.2% in February. All sectors fell with Energy and Technology the worst performers, down 18.2% and 17.6% respectively. There were exceptions amongst individual stocks such as IDP Education (ASX: IEL) and Cleanaway Waste Management (ASX: CWY) up 19.6% and 11.3% respectively. Defensive sectors led the market such as Utilities (down 4.5%), Healthcare (down (3.8%) and Telecommunications (down 1%).

Highlights from earnings season included fund manager Pinnacle Investment Management Group (ASX: PNI) which continued to track well in growing affiliate funds under management while containing costs at an overall group level to see earnings grow 37% to $13.8m.

Fixed Income

	Fixed Income	Feb-20 yield	1M mvt (bps)	Nov-19 yield	3M mvt (bps)
	Australian Cash rate	0.75	--	0.75	--
▼	10-year Bond Yield	0.82	-0.13	1.03	-0.22
▼	3-year Bond Yield	0.50	-0.12	0.65	-0.15
▼	90 Day Bank Accepted Bills SFE-Day	0.80	-0.08	0.89	-0.09
▼	US 10-year Bond Yield	1.15	-0.36	1.78	-0.63
▼	US 3-year Bond Yield	0.90	-0.40	1.61	-0.71
▲	US Investment Grade spread	1.45	0.13	1.38	0.07
▲	US High Yield spread	5.08	1.07	3.81	1.27

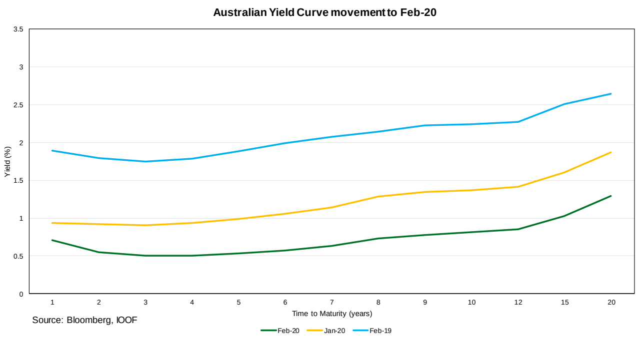
Source: Bloomberg, IOOF

Australian bond market

The Australian yield curve continued falling in February with greater anticipation of rate cuts with the 3-year bond reflecting an assumption of one rate cut in the near term. This occurred following month-end when the RBA cut rates on March 3rd.

In addition, we have seen data highlighted a poor start to the March quarter. Retail sales in January disappointed expectations while the trade balance held up, largely thanks to weakness in imports, a sign of poor domestic demand. Consumer confidence also continued to track at below-average levels according to the Westpac-Melbourne Institute Consumer Sentiment Index. These factors have helped drive Treasury's expectation of a -0.5% hit to March quarter economic growth from the coronavirus outbreak with the bushfires also expected to detract a further -0.2%. This suggests further weakness in the economy with investors bidding up bond prices on expectations of RBA rate cuts.

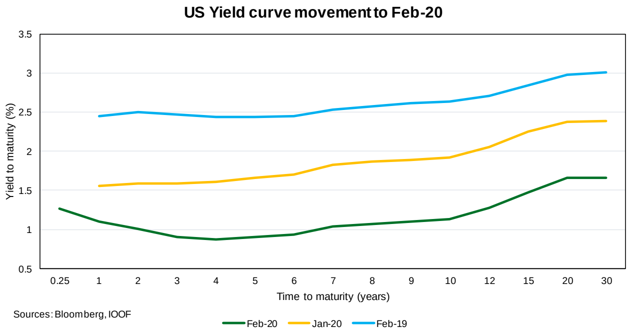
5. Australian yield curve movements to February 2020



US bond market

The U.S. yield curve continued falling into February. Expectations of monetary policy stimulus in response to coronavirus case growth outside of China as well as a flight to safety among investors saw the decline depicted in Chart 6 below.

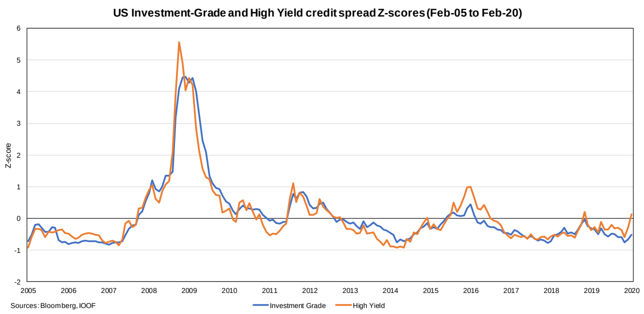
6. US yield curve movement to February 2020



Credit spreads widened during February, especially for high yield bonds. This continued the move we noted in January as well although we note the movement has been less severe for investment grade credit so global corporate bonds still had positive performance during the month (see page 12). The start of this year has seen the trend of contracting spreads reverse signalling tighter financial conditions (and higher perceived risk by investors). As we have noted before high yield debt tends to be concentrated in poorer quality businesses with less diversified business models and often greater leverage. In addition, the high yield universe has a higher exposure to energy companies exposing it to further weakness when oil prices decline as happened in February.

To give recent moves in the credit space context. We were seeing levels consistent with past episodes of market disruption such as when China devalued the yuan in late 2015 and the Dec-18 sell off. Subsequent to month-end this situation has worsened with US high yields at levels last seen in the 2015-16 collapse in oil prices. If your clients have exposure to higher yielding fixed income this will help explain the weaker performance to them.

7. US credit spreads (Feb-05 to Feb-20)



Currencies

	Currencies	Feb-20 Price	1M return (%)	Nov-19 Price	3M return (%)
▼	$A vs $US	65.15	-2.64	67.63	-3.67
▲	$A vs GBP	50.80	0.24	52.31	-2.89
▼	$A vs YEN	70.37	-2.96	74.04	-4.97
▼	$A vs EUR	59.05	-2.07	61.38	-3.80
▲	$A vs $NZ	104.16	0.66	105.29	-1.07
▼	$A TWI	57.00	-1.89	59.00	-3.39
▲	$US vs EUR	90.69	0.60	90.76	-0.08
▲	$US vs CNY	6.99	0.71	7.03	-0.57
▲	$US vs GBP	78.01	3.02	77.33	0.88
▼	$US vs JPY	107.89	-0.42	109.49	-1.46
▲	$US vs CHF	96.49	0.16	100.02	-3.53
▲	US Dollar Index	98.13	0.76	98.27	-0.14
▼	JPM EM Currency Index	58.25	-2.59	59.82	-2.61

Source: Bloomberg, IOOF

The Australian dollar (AUD) fell 2.6% against the USD ending the month at USD 0.6515. Drivers included:

- **Commodity prices**: The RBA Commodity price index fell 0.7% (in SDR terms) over the month driven by weaker metals and energy prices while agricultural goods were flat.
- **Interest rates**: rate cut expectations increased due to concerns over the coronavirus outbreak with bonds yields also falling.
- **Investment sentiment**: Concerns over economic growth outside of China saw movement to a "risk off" stance retreating to safe havens such as the Yen and USD with the AUD experiencing price weakness consequently.

Commodities

	Commodities	Feb-20 Price	1M return (%)	Nov-19 Price	3M return (%)
▼	Aluminium	1686	-1.49	1775	-5.02
▲	Copper	254	0.67	267	-4.90
▼	Nickel	12201	-4.77	13682	-10.82
▼	Zinc	2013	-8.71	2268	-11.22
▼	Crude Oil - Brent	50.52	-13.14	62.43	-19.08
▼	Natural Gas	1.68	-8.53	2.28	-26.17
	Metallurgical Coal	149	--	149	0.11
▼	Thermal Coal	67	-0.48	68	-1.43
▼	Iron Ore	86.46	-6.47	84.68	2.10
▼	Gold	1567	-1.34	1478	5.99
▼	Silver	16	-9.03	17	-4.28

Source: Bloomberg, IOOF

Commodity prices broadly fell during the month including precious metals.

Oil and **Natural gas** prices continued to struggle in February. The spike in coronavirus cases outside of China weighed on energy prices particularly towards month-end.

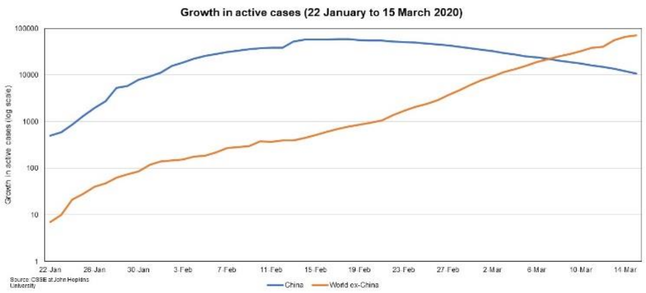
Base metal prices experienced broad weakness with iron ore also retreating on the back of higher inventory builds globally. Business shutdowns lower the need for steel production causing inventories to build higher and suppress prices in the near term. Expectations of China stimulus may see support for some base metals depending on their extent with some such as **copper** potential beneficiaries.

Precious metals showcased the relative lack of correlation, falling in USD terms during the month as investors sought other safe havens in the Yen and US Dollar. In AUD terms gold had positive performance thanks to the decline of the Australian dollar relative to the US dollar.

Coronavirus impact

Since early February we have seen reported cases stabilise in China. This includes cases that are still-infected where growth has been declining as people recover. There are also signs of factory restarts within China albeit from a very subdued start (much of the country was effectively shut down to halt the spread of the virus). By contrast cases outside of China have continued to climb as has the death rate.

7. Growth in infected victim cases (Jan-20 to Mar-20)

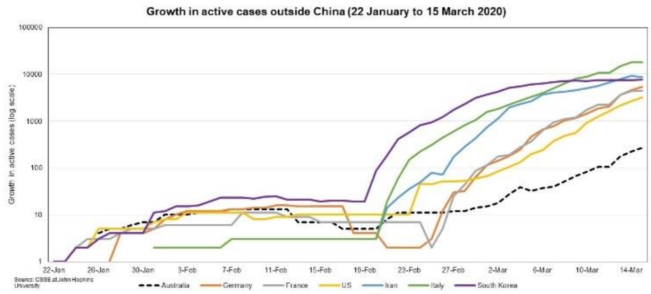


This trend has been led by outbreaks in South Korea, Iran and Italy most notably. Elsewhere in the developed world we have also seen reported cases although it is difficult to have a firm grasp on the figures given the long duration between being infected and showing symptoms as well as a shortage of adequate testing kits.

Several public health initiatives have been exercised to halt the outbreak. Following from the Chinese example Italy has announced a halt on free movement until early April. South Korea has showcased a concerted effort to increase testing and be proactive in quarantine efforts that has seen still-infected case growth slow substantially. More recently the USA has announced a travel ban for flights from Europe in a bid to contain any further outbreaks.

Taking a closer look at the cases outside of China we can see how other developed countries such as Germany or the USA are catching up unfortunately to the outbreaks elsewhere in South Korea or Italy. Australia by contrast has a comparably lower number reported although the trajectory remains a concern and could see us follow the example of other countries in restricting travel in the weeks ahead.

8. Growth in infected victim cases outside China (Jan-20 to Mar-20)



In our previous update we discussed potential scenarios for how the global outbreak might develop. The World Health Organisation has now declared it a pandemic. This move is intended to highlight the severity of the outbreak and the need for government authorities to act and curtail it.

In terms of the economic impact we have seen initial estimates highlighting risks to economic growth. To put these into context there is a risk of contraction in Australia with Treasury flagging an expected hit of 0.5% to economic growth. China is likely to have weak to negative growth in the March quarter as well with Europe likewise facing a challenged setting given the slowdown already underway there.

The risks of a global recession have, on balance, increased. A lot will depend on the degree authorities successfully contain the outbreak.

Proactive government action will likely have a negative economic impact in the short-term but benefit over the longer-term if able to slow the pace of the outbreak. In addition, plans for fiscal stimulus as well as interest rate cuts in place should dull the economic blow we expect to occur in the near-term.

Australia

Consistent with our view over recent years the Australian outlook continues to look challenged. Recent moves by the RBA and government to engage in monetary and fiscal stimulus should help to offset

the economic slowdown induced by weaker exports and travel restrictions.

Policy

The Reserve Bank of Australia cut interest rates by 0.25% to leave its cash rate at 0.5% in early March. It cited this as a precautionary move intended to offset the economic slowdown. Markets are currently pricing in a second and final cut by May this year in anticipation of a weaker economic environment. Given moves elsewhere there is a chance it moves forward sooner than this with speculation that its Thursday 19 March announcement might be such a move.

Late last year we noted discussion of quantitative easing (purchase of Australian government bonds by the RBA) and negative interest rates. The former remains the more likely outcome in addition to one more interest rate cut. This would support the economy by keeping longer-term interest rates lower for longer. However, its overall impact is, in our view, unlikely to be very stimulative given the problems for the economy at present are not the price of credit but rather the actual and looming demand shock businesses are facing.

In Australia the Commonwealth has announced its own stimulus package of approximately $17.6bn (0.9% of annual GDP) which includes:

- Increased tax incentives to support business investment.
- Cash flow assistance to businesses to support retaining staff including remittance by the ATO of tax payments between $2,000 and $25,000 and wage subsidies for apprentice workers.

This initiative was designed to have the bulk of spending implemented by June 2020. There is also additional funding being allocated to the healthcare sector and provisions for targeted stimulus to support the industries worst-affected such as the tourism sector.

Going by recent reports there may be more stimulus being deployed in the weeks and months ahead. Initial reports suggest targeted stimulus will be the priority for those sectors that have been worst hit. We would flag that more is likely to be necessary to fill the gap of weaker spending brought about by the virus. A demand shock of this nature is arguably amongst the worst Australia has seen in recent decades coming at a time when the private sector (including households) was already weakened.

Business sector

The NAB Monthly Business survey for February highlighted a weaker economic environment with business confidence and conditions declining to -4 and 0 index points respectively (the long-term average of business conditions in 6). In addition, leading indicators have softened with forward orders (a sign of future demand) and capacity utilisation (how much businesses are using their existing resources) tracking at below average and average levels respectively.

These results pointing to underlying weakness were confirmed by the CBA Composite PMI slipping into contractionary territory in February, well below the highs seen in 2017 and early 2018.

Consumer sector

The Westpac-Melbourne Institute Index of Consumer Sentiment fell in March to 91.9 from 95.5 in February and marks a five-year low in the Index. This maintains the downward trend we have seen recently and remains below the long-run average of 101.4 (readings below 100 point to pessimists outweighing optimists). The largest driver was a drop in economic expectations for the next year while expectations for the longer-term (5 years) only slipped slightly suggesting people are only assuming pain in the short-term. Overall, this points to a challenging retail environment and corroborates the weakness seen in the business surveys discussed earlier.

Labour market

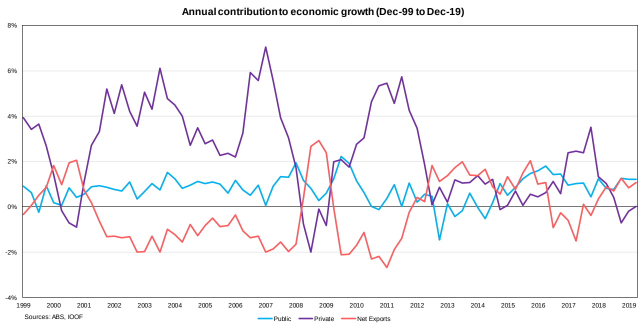
The January Australian labour report was weaker, with the unemployment rate lifting from 5.1% to 5.3% (the largest month on month rise since Jan. 2016). The increase was primarily caused by the participation rate rising by 0.1% to 66.1%, however other labour market statistics were also disappointing including a fall in hours worked and an increase in the underutilisation rate. This move has been consistent with other indicators pointing to economic weakness. These in addition to the expected coronavirus shock are expected to see unemployment rise in the near term, notwithstanding the Federal Government stimulus.

Economic Growth

The Australian economy grew at a stronger-than-expected 0.5% for the December quarter (consensus: 0.4%). While a welcome headline result, the concerns persist on **private sector demand** with investment spending remaining subdued and housing investment detracting -0.6% from annual growth of 2.2%. Consumer spending has also tracked at weak levels of 1.2% annual growth (versus a 15-

year average of 2.8% p.a.). **Government spending** has remained key to supporting growth and a falling Australian dollar supported export growth and undermined import growth seeing **net exports** remain a growth contributor.

9. Australian economic growth by key drivers (Dec-99 to Dec-19)



We also had some further official estimates on growth for the March quarter. Treasury signalled an expected -0.5% growth hit as a result of industries affected by the outbreak such as tourism and the education businesses. The bushfire impact within January is also expected to drag on growth by -0.2%. This raises the prospect of a negative quarter of growth in March for the first time since March 2011. Policy efforts to support businesses will help mitigate the overall impact but it is important to be aware of these danger signs. The longer the outbreak persists both domestically and internationally the more likely we are to see another rate cut (markets expect one by June this year) as well as a more economic disruption that raises potential recession risk.

Summary

On balance the risks to the Australian economy have shifted more to the downside including a higher risk of recession in the near term. Government stimulus and a lower Australian dollar will act as offsets to this risk. In addition, Chinese stimulus may see a smaller scale repeat of the experience during 2015-16 and the global financial crisis, supporting export earnings.

Overall, however the risks are heightened and may see at least one negative quarter of economic growth depending on how long this situation persists and the extent of any permanent shifts in consumer and business behaviour.

United States

US growth has made a strong start to the year. However, the coronavirus outbreak has taken hold there during March and perhaps earlier judging by cases in Washington State. This raises the possibility of weaker to negative growth during the June quarter and weakness in the economy during March. Fiscal and monetary stimulus should offer some ballast as in the Australian case but note that delays in implementation may exacerbate economic weakness.

Policy

The Federal Reserve used its "ammunition" in the form of a higher cash rate in recent weeks by cutting rates to a range of 0-0.25% down from 1.5-1.75% at the end of February via two emergency sessions. These moves were pre-emptive and intended to counter the risks of coronavirus to economic activity.

In addition, they have announced plans to increase holdings in both government bonds and mortgage-backed securities to support credit markets continuing to flow. It also announced an increase in its repo market activities. This is an important market through which policy can be transmitted and supporting system liquidity in periods like recent weeks is important. Falling asset prices whether stocks or bonds represent "tighter" financial conditions as businesses who rely on rolling over the debt for example will struggle to do so at normal rates and may have to increase the yield on offer to keep their businesses going.

The US government is debating a series of fiscal stimulus moves at the present. These include increased free coronavirus testing, stronger unemployment insurance and increased funding for food programs to support affected citizens. We expect some version of this package to be forthcoming in the next week given the need to act. Lastly President Trump has announced a state of emergency to give access to $50bn in funds to help with a coronavirus pandemic response with initiatives including waiving interest on federal student loans and strategic petroleum reserve purchases (to help the energy sector). He has also indicated a willingness to give Federal support to businesses temporarily affected by this shock e.g. airlines, tourism.

Politics update

The Democrat Party Presidential Primaries have continued throughout the month. The two front-runners are Joe Biden and Bernie Sanders with Biden in the lead after a successful campaign in the Southern States and Texas. Biden has 887 delegates to Sanders' 731 (at the time of writing) with 1,991 required to win the Democrat Presidential nomination to challenge President Trump in November.

Biden appears to be seen as a "safer" candidate by markets given his moderate political stance as opposed to the Sanders' promises of higher spending and taxes and more radical policy initiatives such as student debt forgiveness. We continue to monitor this space as it may contribute to market volatility later this year depending on how the situation evolves.

Business activity and sentiment

The PMI surveys this month have been clouded by the hit to business confidence. This saw the Services sector surveys print a contractionary result of 49.4, down from 53.4, in February while Manufacturing also fell to 50.7, down from 51.9. New business from abroad continued to soften notably results of with weak near-term confidence and subdued new business both domestically and internationally.

Subsequent to month-end, the scale of Federal Reserve stimulus and plans for fiscal policy are testament to the concerns for US growth and the need to counter the expected weakness in aggregate demand.

Consumer confidence

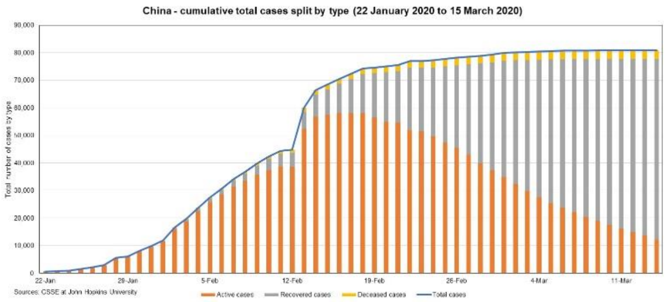
Consumer confidence held up better than expected with a reading of 95.9 (consensus: 95). Consumer expectations was the biggest driver falling to 85.1 from 92.1 in February although consumer expectations for the next 5 years improved suggesting that, like the Australian survey, consumers are looking through this as a temporary shock. This being said weaker confidence levels point to the economic risk associated with the public health measures needed to curb the spread of the virus.

China

Judging by official estimates the coronavirus outbreak has been brought under increasing control within China with the number of active cases declining daily in recent weeks as more citizens recover. Factory restarts have begun in earnest with Chinese capacity being brought back online. There are challenges in terms of end-export demand, but stimulus is expected to help mitigate this near-term impact and, depending on its extent, help support countries such as Australia with higher resource demand.

Coronavirus outbreak and policy response

10. Cumulative China cases split by type (Jan-20 to Mar-20)



Reported cases in China have plateaued with the total number still active declining substantially (orange bars) with most recovering (grey bars) and some, sadly, passing away from the virus (yellow bars).

China continues to provide monetary stimulus to counter the economic impact of the coronavirus. For instance, the Loan Prime Rate (LPR), which is considered China's *de facto* benchmark funding rate, was lowered from 4.15% to 4.05% for a one-year term. This follows the central bank cutting the rate on its one-year loan to commercial lenders earlier in February. We have also seen some fiscal policy at a smaller scale in regions such as Hong Kong with measures such as payroll and income tax cuts and a $1,200 cash subsidy. More is expected in the form of infrastructure spending although new announcements have not yet been forthcoming.

Economic growth

Partial data such as retail sales and industrial output highlight the weakness caused by efforts to contain the coronavirus and the virus itself. This saw industrial output decline 13.5% in January and February from last year and retail sales down 20.5% over the same period. In addition, the unemployment rate rose to a record 6.2% in February due to weaker demand for factory workers. This serves as an example on the impact to both supply and demand the virus has caused which we may see play out elsewhere.

Business activity and sentiment

The Caixin China PMI surveys highlighted the economic damage caused by the effective shutdown of much of China during February. The Services PMI fell to 26.5, down from 51.8 in January indicating a sharp contraction, the first recorded for services activity since the survey began 14 years ago. The coronavirus outbreak was the key driver via its contribution to company closures and strict travel restrictions with Chinese firms also confronting weaker demand both domestically and overseas.

The Manufacturing PMI likewise fell to 40.3, down from 51.1 in January driven by extended company shutdowns and weaker business confidence. Notably however firm expectations for increased production over the next year improved to its strongest level in five years suggesting businesses are looking through this shock as transitory.

The negative result for the services sector should not be overlooked however. This has been a source of strength for the Chinese economy throughout the trade war saga and did not contract even during the global financial crisis. If this weakness foreshadows the pain elsewhere, we may continue to see further economic damage in the months ahead particularly in the form of higher unemployment.

Europe

Concerns over Brexit have been replaced by a widescale outbreak of coronavirus cases within Italy that has also affected other major European countries (see chart 8 above). This has prompted a policy response with monetary stimulus and, surprisingly, some government spending. Growth conditions were weak heading into this period and despite positive PMIs for February we are facing a greater risk of at least technical recession in the near term (two consecutive negative quarters of economic growth).

United Kingdom

Talks with the EU have been supplanted by a focus on the policy response needed to counteract weak economic growth in the UK. This has two aspects.

First the Bank of England announced a 0.5% cut to interest rates from 0.75% to 0.25%. As part of this move it also announced a new £100bn scheme to ensure banks pass on the rate reduction to UK businesses and households.

Second the government announced a £30bn stimulus package geared towards both healthcare and financial support for businesses and workers during this period. In addition, the government has announced further infrastructure & research and development investment funding as part of its longer-term work to boost growth.

Policy

The European Central Bank (ECB) left its interest rate settings unchanged as expected. It also announced lending programmes to add liquidity to the euro area financial system particularly supporting bank lending to small and medium-sized enterprises. Finally, it flagged an increase in its quantitative easing efforts of €120bn to keep long-term interest rates low and add to favourable financing conditions.

Elsewhere in Europe we have seen increased signs of tighter border controls even between European countries. Italy has been an epicentre of the outbreak with authorities there eventually shutting down non-essential travel within the country until early April in a bid to minimise the further spread of the virus. This has also seen major public events such as football tournaments be suspended indefinitely as authorities look to contain opportunities for already-sick persons to infect larger groups.

Finally, we note that fiscal stimulus appears to be nearing reality with several countries making substantive promises to support their respective economies. Germany has flagged lending as much as €550bn via its state bank to support embattled companies and prevent worker layoffs in the process. Switzerland announced its own program of 10bn Swiss Francs of aid for its companies as well. The European Commission has also signalled its readiness to allow members to act counter-cyclically and use fiscal stimulus despite ostensibly violating its fiscal constraints. Italy is one such example with a €25bn package that will push its deficit beyond the Commission's 3% limit this year. The Commission itself has announced a €37bn investment fund using spare money from the EU budget to support businesses, health care and specific sectors in need with the EU's investment fund looking to guarantee small business loans of up to €8bn in total to enable firms to delay payment as well.

Business Activity and Sentiment

European PMI surveys improved during February before the full extent of the Italian outbreak and spread elsewhere in the continent was fully appreciated. It does add support to the idea of improving global growth that has been derailed in the near term by the coronavirus outbreak.

The IHS Markit Eurozone Composite rose slightly to 51.6, up from 51.3 in January. The pace of contraction in manufacturing continued to slow to 49.2 in February (above 50 is expansionary), up from a 47.9 print in January. The Services PMI improved fractionally to 52.6 in February, up from 52.5 in January. The uptick was supported by stronger domestic demand with new business orders domestically continuing to climb while export sales fell at the fastest rate in 5 months. This was a result consistent with a slight improvement in quarterly growth to 0.1-0.2% according to IHS Markit economist. However, the demand shock from coronavirus and public health responses means it is likely that, notwithstanding stimulus initiatives, we see a materially weaker result in the March figures.

Economic growth

The European economy grew at 1% for the year to December 2019 (consensus: 1.1%). We note that this quarter was also subject to the tax-related distortions we've mentioned in previous reports. Ireland for example had a 35% increase in domestic final demand for 2019. However, this was highly influenced by tax-related investment in intellectual property offset by imports of R&D services (essentially tax shelter games by large multinationals). Stripping these effects out suggests weak underlying growth (not dissimilar to Australia) that leaves Europe more vulnerable to recession risk.

Company news (best and worst performers during the month of February 2020)

IDP Education (+ 19.6%)

IDP Education (IEL) released a positive 1H20 result showing revenue increasing +25% on the prior comparison period (pcp) to $379m and EBIT increasing +49% to $86.9m. All divisions performed well with an additional +30% increase in student placements, an +11% increase on IELTS English exams taken, and the delivery of +15% more English teaching courses. IEL is benefiting from strong long-term structural headwinds of a growing Asian middle class that is finding international education increasingly affordable and important for their children to succeed. The company has not provided guidance for the impact coronavirus may have. We note that it may suffer a meaningful drawdown in enrolments in the short run due to restrictions on travel for public health reasons, but the long-term drivers remain intact.

Cleanaway Waste Management (+11.3%)

Cleanaway Waste Management (CWY) released solid 1H20 results with a revenue increase +4.1% to $1.2bn and underlying NPAT increase of +13.7% to $76.2m. Statutory results were impacted by a fire in their Perth plant with reported NPAT lower at $45.3m. The positive result proved that the company's $60m purchase of SKM, a collapsed Victorian recycling business that was under administration, proved to be a bargain, with CWY managing to turn a slight profit in the 2 months since the acquisition. The result also showed the resilience of the company's earnings despite headwinds from lower commodity prices, QLD volume declines, and lower economic activity.

Fisher & Paykel Healthcare (+10.1%)

Fisher & Paykel Healthcare (FPH) rose over February after guidance was upgraded from NZ$255-$265m to NZ$260-$270m. FPH also provided guidance on the coronavirus outbreak, citing that its hospital products have been a beneficiary of COVID-19 and that its supply chain remains largely uninterrupted as FPH has no manufacturing facilities in China. It did note however that some suppliers of raw materials are based in China but this was not a material issue at this time.

Wisetech Global Ltd (-39.7%)

Wisetech Global (WTC) suffered a significant drawdown after downgrading its guidance as a result of the coronavirus outbreak. Although 1H20 results contained a number of positives, it was not enough to save the share price from a combination of (1) disruption of Chinese/global freight volumes from the coronavirus, (2) an already stretched valuation multiple and (3) an accusation from a short-seller accusing WTC of hiding poor organic performance from a series of acquisitions. We note that their 1H20 results showed good customer retention (1% churn), a 31% increase in revenue, and 29% in EBITDA, generally in line with consensus expectations.

Clinuvel Pharmaceuticals (-35.8%)

Clinuvel Pharmaceuticals (CUV) released disappointing first-half results after a large increase in expenses caused profits to drop substantially. NPAT decreased -73% as expenses increased +54% as a result of a significant increase in R&D costs for core product, SCENESSE, post receiving FDA approval, and other investments in preparation for global expansion.

Beach Energy Ltd (-34.3%)

Beach Energy (BPT) was sold off after 1H20 revealed disappointing production and sales volumes, with production volumes dropping -15% to 13.0MMboe and sales volumes dropping -19% to 13.4MMboe, resulting in a -27% drop in operating cash flow. Energy was generally sold off during February and further so in March after Russia and OPEC failed to reach an agreement to limit supply in support of the oil price.

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

Movers and Shakers for the month of February 2020

ASX Code	Company Name	Closing price ($)	Month ago, close ($)	Month ∆ (%)	Quarter ago close ($)	Quarter ∆ (%)	Year ago, close ($)	Year ∆ (%)
IEL	IDP Education Ltd	21.25	17.77	19.6	18.14	17.1	14.82	43.4
CWY	Cleanaway Waste Management Ltd	2.27	2.04	11.3	2.12	7.1	2.20	3.2
FPH	Fisher & Paykel Healthcare	24.59	22.33	10.1	20.93	17.5	14.36	71.2
PNI	Pinnacle Investment Mgmt Group	5.23	4.79	9.2	4.96	5.4	5.13	1.9
EVN	Evolution Mining Ltd	4.04	3.71	8.9	3.91	3.3	3.60	12.2
IVC	Invocare Ltd	14.50	13.41	8.1	13.17	10.1	14.77	-1.8
CGC	Costa Group Holdings Ltd	2.96	2.76	7.2	2.60	13.8	4.82	-38.6
NST	Northern Star Resources Ltd	13.46	12.60	6.8	9.59	40.4	9.26	45.4
A2M	A2 Milk Co Ltd	15.42	14.51	6.3	14.77	4.4	13.85	11.3
INA	Ingenia Communities Group	4.99	4.78	4.4	4.70	6.2	3.07	62.5

Source: Bloomberg, IOOF

ASX Code	Company Name	Closing price ($)	Month ago, close ($)	Month ∆ (%)	Quarter ago close ($)	Quarter ∆ (%)	Year ago close ($)	Year ∆ (%)
WTC	Wisetech Global Ltd	15.10	25.03	-39.7	27.28	-44.6	19.44	-22.3
CUV	Clinuvel Pharmaceuticals Ltd	17.77	27.70	-35.8	28.10	-36.8	25.64	-30.7
BPT	Beach Energy Ltd	1.76	2.67	-34.3	2.40	-26.9	2.06	-14.8
EML	EML Payments Ltd	3.62	5.26	-31.2	4.73	-23.5	1.69	114.3
LNK	Link Administration Holdings	4.70	6.81	-31.0	5.80	-19.0	7.66	-38.6
MYX	Mayne Pharma Group Ltd	0.33	0.46	-28.6	0.47	-30.1	0.69	-52.9
IFL	IOOF Holdings Ltd	5.67	7.91	-28.3	7.83	-27.6	6.66	-14.9
BKL	Blackmores Ltd	64.33	89.32	-28.0	82.51	-22.0	93.51	-31.2
RWC	Reliance Worldwide Corp Ltd	3.38	4.50	-24.9	4.09	-17.4	4.55	-25.7
OSH	Oil Search Ltd	5.49	7.24	-24.2	7.44	-26.2	8.21	-33.1

Source: Bloomberg, IOOF

Long-term asset class performance to February 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)	-7.7%	-5.2%	-0.6%	8.6%	8.6%	6.2%	8.0%	8.0%	7.5%	8.2%
Australian equities - Mid caps	-9.7%	-6.9%	-2.5%	4.8%	8.6%	9.2%	10.8%	9.1%	7.6%	9.7%
Australian equities - Small caps	-8.7%	-5.9%	-2.4%	1.6%	8.3%	7.4%	5.2%	4.4%	4.3%	5.1%
Australian equities - Micro caps	-14.1%	-12.9%	-9.1%	6.6%	2.9%	7.9%	2.0%	1.5%	3.3%	#N/A
International equities	-4.9%	-1.6%	5.6%	15.6%	13.9%	10.2%	15.9%	12.5%	7.7%	4.0%
International equities (Hedged to AUD)	-8.5%	-6.7%	0.3%	4.4%	7.0%	6.9%	10.7%	11.3%	8.1%	#N/A
International equities - Small caps	-6.3%	-4.8%	2.5%	6.5%	10.1%	8.8%	14.9%	12.7%	8.3%	6.9%
Emerging Markets equities	-1.6%	1.8%	7.6%	8.3%	11.2%	6.8%	8.7%	6.6%	7.6%	#N/A
Australian REITs	-4.9%	-3.3%	-2.5%	11.8%	9.9%	8.8%	11.5%	11.8%	5.1%	#N/A
Global REITs	-4.7%	-2.4%	0.7%	12.4%	10.6%	7.1%	12.0%	11.5%	7.1%	#N/A
Global REITs (Hedged to AUD)	-8.1%	-7.1%	-3.9%	2.2%	4.5%	4.1%	7.3%	10.2%	7.0%	#N/A
Global Infrastructure	-5.4%	1.8%	2.7%	16.5%	14.3%	10.3%	14.9%	12.9%	#N/A	#N/A
Global Infrastructure (Hedged)	-8.4%	-2.7%	-1.7%	6.6%	8.1%	7.3%	10.2%	12.0%	#N/A	#N/A
Trend following	4.7%	5.1%	-4.2%	19.3%	4.1%	0.4%	8.8%	4.4%	5.0%	5.3%
Australian bonds	0.9%	1.5%	1.3%	9.0%	6.0%	4.4%	5.1%	5.9%	6.0%	6.2%
Australian bonds - government	1.0%	1.6%	1.3%	9.5%	6.2%	4.5%	5.1%	5.9%	6.0%	6.2%
Australian bonds - corporate	0.6%	1.4%	1.7%	8.0%	5.7%	4.7%	5.2%	6.2%	6.2%	6.4%
Australian bonds - floating rate	0.1%	0.4%	0.9%	2.4%	2.7%	2.8%	3.1%	4.0%	4.5%	4.9%
Global bonds (Hedged)	1.2%	2.8%	1.7%	9.3%	5.0%	4.5%	5.2%	6.4%	6.7%	7.2%
Global bonds - government (Hedged)	1.5%	2.9%	1.3%	9.2%	5.0%	4.5%	5.3%	6.3%	6.6%	#N/A
Global bonds - corporate (Hedged)	0.8%	3.1%	2.8%	12.1%	5.9%	5.2%	5.8%	7.4%	7.0%	#N/A
Global bonds - High Yield (Hedged)	-1.7%	0.7%	1.7%	4.4%	4.2%	5.9%	6.4%	9.3%	8.9%	#N/A
Emerging Market bonds (Hedged)	-1.2%	2.4%	1.5%	9.1%	5.2%	6.1%	5.6%	8.4%	8.6%	10.4%
Cash (AUD)	0.1%	0.2%	0.5%	1.3%	1.7%	1.9%	2.1%	2.8%	3.8%	4.2%

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 to AUD)	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 to AUD)	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

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Research Analyst Disclosures:

I, Cameron Curko, hereby certify that all the views expressed in this report accurately reflect my personal views about the subject investment theme and/or company securities. I also certify that no part of my compensation was, is, or will be, directly or indirectly, related to the specific recommendations or views expressed in this report.

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