Our view

Researchupdate

Economic Wrap

July 2020

Summary

- Coronavirus case has been slowing with emerging markets such as India remaining hotspots whilst second wave situations are appearing in countries as wide-ranging as Israel to Japan.
- The Australian outbreak continued to worsen during July with Victoria remaining the centre of both rising cases and fatalities. Case growth has also risen in New South Wales but, at the time of writing, does not appear to be on as severe a trajectory as the Victorian experience.
- Pleasingly it appears that some of the worst-affected such as Brazil and the USA are beginning to show a protracted decline in case growth while vaccine trials are showing promising signs of progress.
- Government stimulus spending is a key issue in the near-term with promising progress in some regions such as Europe and worrying signs in the US.

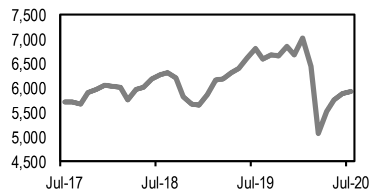
Markets – Strong performance continued riskier asset classes (see p 11).

- Risk assets including equities and high-yield bonds continued to recover from the March quarter with some reaching new highs such as the Nasdaq while safe havens such as the US dollar softened.
- 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). Emerging market strength was a highlight of the month (see chart 4) driven by Chinese share market performance (A-Shares market was up 10.9%).

Key economic news –

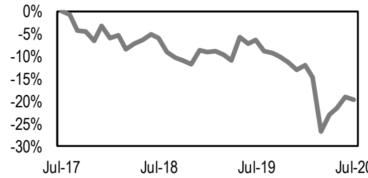
- Australia recorded deflation with the headline CPI falling -0.3% in the year to June 2020 driven by lower oil prices and government subsidies for free childcare. Some of these factors will reverse going forward returning inflation to positive territory.
- US and European economic growth were weak as expected with both results confirming the recession calls by ourselves and others in recent months. Leading indicators continue to point towards recovery albeit at a slower pace

1. S&P/ASX 200 Price Index



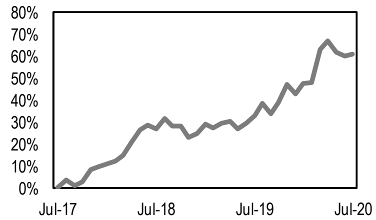
Source: Bloomberg, IOOF

2. ASX200 vs All-World, US$ terms



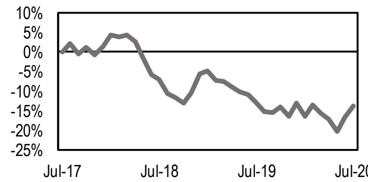
Source: Bloomberg, IOOF

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	2.67	Consumer Discretionary	15.20
▲	Consumer Staples	3.29	Consumer Staples	8.11
▼	Energy	-6.55	Energy	-4.13
▼	Financials ex Property	-1.11	Financials ex Property	8.15
▼	Financials	-1.11	Financials	8.15
▼	Health Care	-3.90	Health Care	-5.82
▼	Industrials	-3.70	Industrials	-1.87
▲	IT	4.64	IT	26.96
▲	Materials	5.82	Materials	16.84
▲	Property Trusts	0.64	Property Trusts	4.71
▲	Telecommunications	3.43	Telecommunications	12.26
▼	Utilities	-0.18	Utilities	1.14

Best and Worst S&P/ASX 200 Performers

Top five stocks		Bottom five stocks	
Monthly			
Netwealth Group Ltd	+33.9%	Avita Therapeutics	-32.6%
ALS Ltd	+29.4%	Adbri Ltd	-30.5%
Orocobre Ltd	+28.6%	AMP Ltd	-21.0%
Fortescue Metals Grp Ltd	+25.7%	Monadelphous Group Ltd	-17.7%
Oz Minerals Ltd	+24.4%	Ooh!Media Ltd	-17.6%
Quarterly			
Afterpay	119.7%	Unibail-Rodamco-Westfd	-25.1%
Perseus Mining	59.1%	Ooh!Media Ltd	-27.5%
Netwealth Group Ltd	58.2%	Orora Ltd	-28.4%
AP Eagers Ltd	57.8%	Corp Travel Mgmt	-31.3%
Mineral Resources Ltd	53.4%	Avita Therapeutics	-34.7%

Source: Bloomberg, IOOF

Equity review

Major Market Performance, July 2020

	Australian Indices	Jul-20 Price	1M return (%)	Apr-20 Price	3M return (%)
▲	S&P/ASX 200	5928	0.51	5522	7.34
▲	All Ordinaries	6058	0.95	5598	8.23
▲	Small Ordinaries	2634	1.33	2405	9.50
	US Indices				
▲	S&P 500	3271	5.51	2912	12.32
▲	Dow Jones	26428	2.38	24346	8.55
▲	Nasdaq	10745	6.82	8890	20.88
	Asia Pacific Indices				
▲	Hang Seng	24595	0.69	24644	-0.20
▼	Nikkei 225	21710	-2.59	20194	7.51
	UK & Europe Indices				
▼	FTSE 100	5898	-4.41	5901	-0.06
▼	CAC40	4784	-3.09	4572	4.63
▲	DAX Index	12313	0.02	10862	13.37

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 were more mixed during the month with strength in the US and China but weakness in Europe. Notable drivers include:

- The continued strength of US tech stocks with majors such as Alphabet (a.k.a. Google) and Amazon beating analyst consensus expectations for the June quarter.
- Promising progress on coronavirus vaccines with several advancing through initial trials.
- For Chinese stocks, strong government support of the stock market via state media promotions has seen a sizeable uptick in retail investor participation with the more domestically focused A-Shares market rallying 10.9% during the month.

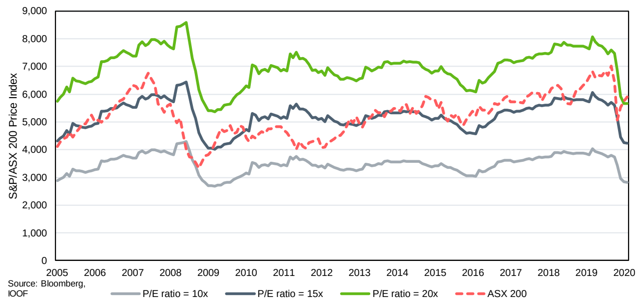
On a style basis, value stocks struggled during July. There was a pronounced move in higher growth and momentum stocks as investors rewarded those names for exceeding expectations with US tech stocks such as Amazon or Apple dominating these styles currently.

Australian equity market

The S&P/ASX 200 index rose 0.5% on a price basis during July with Materials the top performer (up 5.8%) while performance was mixed elsewhere with Energy the worst performer (down -6.6%) followed by Healthcare (down -3.9%) and Industrials (down -3.7%). Style-wise we saw smaller companies outperform with the Small Ordinaries up 1.4% during the month on a total return basis (1.3% on a price basis) while Value stocks (dominated by the banking sector) and Quality names struggled each only up 0.1%

Momentum and growth stocks such as iron ore miners Fortescue and Rio Tinto have been the winners in recent months. Afterpay has been another continuing to be rewarded by increased take up and belief in its investment story. If we turn to Chart 5 we see in red how the market has been driven by an uplift in valuation to slightly above a 20x multiple on forward earnings (the green line). This chart shows the actual forward P/E vs where the index would sit at a 10x, 15x and 20x multiple. Current valuations are driven by a range of factors including the optimism over an earnings recovery and parlous alternatives for investors with bonds trading near record low yields.

5. S&P/ASX 200 at different forward P/E multiples (Jul-05 to Jul-20)



FY20 results season during August will pose an important test to the above expectations with some surprises both good and bad as of early August.

We also suggest some scrutiny of business results is warranted. Companies appear to be adjusting for stimulus support in different ways for their pro-forma results purporting to show their "true" profitability. This may lead to inappropriate extrapolation where stimulus has been crucial to supporting earnings in the near term.

Total returns to July 2020

	1-mth	3-mth	6-mth	1-yr	3-yr	5-yr
MSCI Australia Total Return	0.3%	6.7%	-16.1%	-11.5%	4.7%	4.6%
Value	0.1%	8.8%	-19.4%	-19.1%	-2.6%	-0.1%
Value-Weighted	-0.9%	6.7%	-19.9%	-18.0%	0.7%	2.4%
Momentum	5.3%	12.7%	-5.0%	1.8%	9.5%	9.7%
Growth	3.1%	8.8%	5.4%	20.5%	20.6%	13.3%
Quality	0.1%	2.1%	-1.9%	13.9%	18.9%	13.0%
Low volatility	0.5%	6.7%	-15.3%	-12.1%	4.9%	5.2%
Equal weight	0.3%	8.4%	-14.2%	-10.0%	5.7%	7.4%
Small caps	1.4%	9.9%	-10.9%	-8.5%	6.5%	7.9%

	1-mth	3-mth	6-mth	1-yr	3-yr	5-yr
MSCI World Net Return	0.6%	2.9%	-7.3%	3.1%	11.4%	8.0%
Value	-1.1%	-3.1%	-18.6%	-12.3%	3.0%	3.0%
Value-Weighted	-0.9%	6.7%	-19.9%	-18.0%	0.7%	2.4%
Momentum	2.9%	7.8%	1.6%	13.2%	19.7%	13.4%
Growth	3.0%	8.6%	4.8%	19.6%	20.0%	12.8%
Quality	0.9%	2.8%	-1.2%	13.6%	18.9%	12.7%
Low volatility	-0.1%	-2.0%	-11.8%	-3.3%	10.1%	#N/A
Equal weight	0.3%	8.4%	-14.2%	-10.0%	5.7%	7.4%
Small caps	0.2%	4.2%	-12.7%	-5.7%	6.3%	5.6%

Note: Total returns are in Australian dollars assuming dividend reinvestment.
Source: Bloomberg, IOOF

Fixed Income

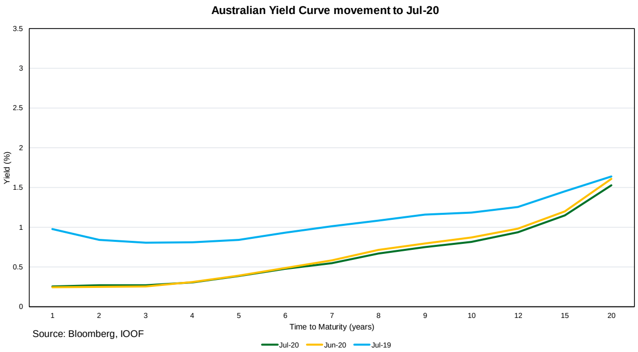
	Fixed Income	Jul-20 yield/ spread	1M mvt (bps)	Apr-20 yield/ Spread	3M mvt (bps)
	Australian Cash rate	0.25	--	0.25	--
▼	10-year Bond Yield	0.82	-0.06	0.89	-0.08
▲	3-year Bond Yield	0.27	0.02	0.25	0.02
	90 Day Bank Accepted Bills SFE-Day	0.11	--	0.10	0.00
▼	US 10-year Bond Yield	0.53	-0.13	0.64	-0.11
▼	US 3-year Bond Yield	0.11	-0.06	0.24	-0.13
▼	US Investment Grade spread	1.46	-0.27	2.18	-0.72
▼	US High Yield spread	4.84	-1.35	7.43	-2.59

Source: Bloomberg, IOOF

Australian bond market

The Australian yield curve flattened during July with the 10-year bond yield declining 6bps to 0.82% and the 3-year yield remaining flat near the RBA's target level of 0.25%.

6. Australian yield curve movements to July 2020



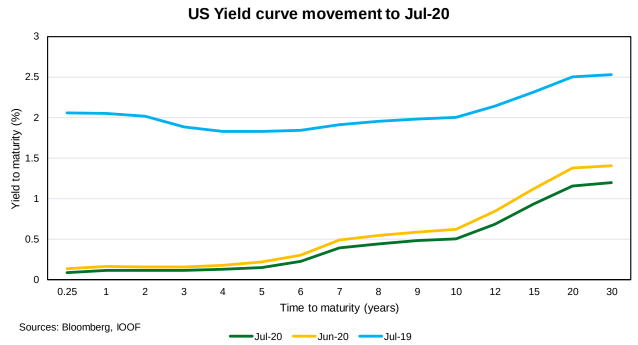
There is no change to our view that the Bank will keep rates low for a prolonged period and only slowly unwind the impact of these changes given how disruptive a sudden readjustment could be for the economy. FactSet Consensus estimates also anticipate no movement on interest rates through to the end of 2022 at the time of writing.

Credit spreads continued to contract during July. This saw corporate bonds outperform by 0.5% 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. The greater yield on offer has been another factor following the March quarter selloff.

US bond markets

US Treasury yields contracted, and the yield curve flattened as investor sentiment towards the US economy softened. The failure to extend certain emergency stimulus payments provisioned under the *CARES Act* was one key driver. Lower stimulus levels remove a material injection from the economy suggesting weaker consumer spending as a result. Negative economic data including preliminary June quarter GDP also point to the depth of the recession still underway with 15.5m American works still receiving ongoing unemployment assistance (as of early August).

7. US yield curve movements to July 2020



Even as investors were "pricing in" a weaker economic environment by bidding government bond prices higher we saw riskier bonds also find investor support.

These two are seemingly at odds, on the one hand lower government bond yields point to tougher economic times ahead but on the other, tighter credit spreads suggest expected credit risk is low in investors eyes. Another complicating and unknown factor is the extent to which central bank purchases have distorted bond price signals, undermining our conclusions.

The tightening of spreads in this context would suggest limited permanent damage is expected. This would be a testament to the scale of government stimulus to date. The Fed is a material contributor providing a floor for riskier bond prices via its willingness to act and intervene if necessary, to support market liquidity.

Outlook

The outlook for fixed income globally sees a lower rate environment persisting for a longer period. Even if we see spikes in inflation the commitment by central banks to support growth would likely delay increasing rates both here and overseas. Higher inflation would make inflation-linked bonds or defensive alternatives more attractive options for clients with defensive risk profiles. Currently weak inflation and deflation is the status quo. In that setting even with low yields bonds have continued to perform well, offering strong after-inflation returns, and diversify equity market risk.

The intervention by global central banks since March appears to be setting a floor in credit spreads even given higher default risk. An improving macro backdrop and abundant suggest there is potential for spreads to tighten further from current levels.

Currencies

	Currencies	Jul-20 Price	1M return (%)	Apr-20 Price	3M return (%)
▲	$A vs $US	71.43	3.48	65.12	9.69
▼	$A vs GBP	54.59	-1.94	51.70	5.58
▲	$A vs YEN	75.59	1.45	69.79	8.31
▼	$A vs EUR	60.65	-1.30	59.44	2.04
▲	$A vs $NZ	107.75	0.75	106.29	1.37
▲	$A TWI	61.90	3.17	57.80	7.09
▼	$US vs EUR	84.90	-4.63	91.31	-7.02
▼	$US vs CNY	6.98	-1.26	7.06	-1.25
▼	$US vs GBP	76.42	-5.23	79.40	-3.75
▼	$US vs JPY	105.83	-1.95	107.18	-1.26
▼	$US vs CHF	91.29	-3.63	96.53	-5.43
▼	US Dollar Index	93.35	-4.15	99.02	-5.72
▲	JPM EM Currency Index	55.60	2.41	52.97	4.96

Source: Bloomberg, IOOF

The Australian dollar (AUD) rose 3.5% against the US Dollar (USD) during the June quarter, from USD 0.6903 to USD 0.7143. Drivers included:

- Improving interest-rate differential: Shorter-dated Australian bonds are offering equal or higher yields to US equivalents, attracting investor demand.
- **Chinese stimulus**: Ongoing investment spending in China has seen a continued bid for Australian iron ore with a limited response for Brazil to date supporting a stronger current account surplus. A current account surplus implies greater demand for your currency from overseas trading partners, boosting the value of the AUD as a result.

We note that the AUD has swung being undervalued (assuming a purchasing power parity (PPP) relationship holds) to being slightly overvalued relative to a PPP value of USD 0.68. At these levels we would suggest being close to neutral in terms of AUD positioning i.e. being ~50% hedged.

Ongoing weakness in the US Dollar was again a feature with stronger Chinese data and Eurozone news key drivers. Historically there has been a discount baked into the Euro recognising the risk of a Eurozone breakup. The successful agreement to a Recovery Fund is an important step towards regional integration and supported the Euro vs USD.

We saw emerging market currencies recover during the month as investor risk appetite continued to return to risk assets. It also reflects the extent some of these were substantially undervalued on a PPP basis with many having violently sold off during the March quarter when the JP Emerging Markets Currency Index fell 13%.

Commodities

	Commodities	Jul-20 Price	1M return (%)	Apr-20 Price	3M return (%)
▲	Aluminium	1684	4.68	1500	12.23
▲	Copper	287	5.11	235	21.91
▲	Nickel	13748	7.56	12208	12.61
▲	Zinc	2312	13.20	1941	19.10
▲	Crude Oil – Brent	43.30	5.22	25.27	71.35
▲	Natural Gas	1.80	2.74	1.95	-7.70
▼	Metallurgical Coal	130	-9.16	143	-9.16
▲	Thermal Coal	51	0.76	49	2.53
▲	Iron Ore	108.90	5.78	83.84	29.89
▲	Gold	1986	9.09	1705	16.48
▲	Silver	24	29.94	15	60.59

Source: Bloomberg, IOOF

Oil prices continued to recover during July. Product cuts by OPEC+ members were strong supports of the market while improving global growth prospects (as seen in rising PMI prints) also supported prices. We note however that plans to increase production in the near term by several producers may halt the recovery from progressing further. Global demand, whilst improving is still challenged by recessionary conditions that can act as a ceiling preventing further price growth. In addition, unlike past recessions we arguably have a larger swing producer in US oil production that could become increasingly viable were prices to increase further and begin to add new supply to the market.

Precious metals continued to benefit from a weaker real yield (bond yield after inflation) environment as the US yield curve continued to flatten. In addition, strong ETF inflows have supported further purchasing creating a momentum flywheel effect at present. Silver outperformed substantially as it closed the relative valuation gap with gold (its value vs gold had dislocated sizeably in recent years) and also saw more demand for its industrial applications as global manufacturing PMIs returned to expansion.

Base metals such as Copper and Aluminium saw continued price strength following supply disruptions from coronavirus lockdowns as well as tighter scrap metal controls by Chinese authorities (which boosts pricing for higher quality ore). **Iron ore** prices continued to see strong support from Chinese demand.

Coking or metallurgical coal prices fell on weaker steel production from countries outside of China such as Japan and India (a major driver given existing Chinese supply is adequate according to market observers).

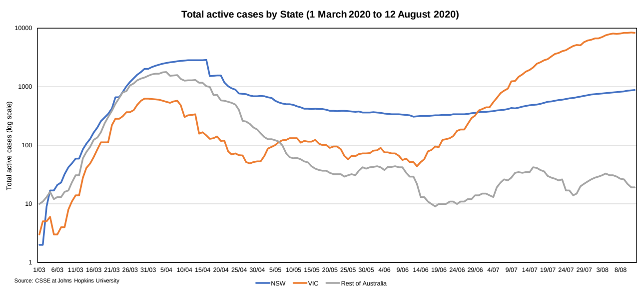
Australia

We saw the JobSeeker and JobKeeper programs and, early release of superannuation all extended to add support to the economy. This was in part a response to further lockdown severity with Melbourne entering level 4 restrictions. On the positive side we saw increasing hours worked and jobs growth in July that should help support the economy in the near term. The base case still suggests weak growth in the near term.

Coronavirus pandemic

The Victorian outbreak continued to see rising daily case growth over July. However, growth has begun slowing into August suggesting the harsh lockdown measures were showing signs of success. NSW cases continued to rise during the month, but the State has not seen the same pace of growth experienced in Victoria to date.

8. Australian active coronavirus cases by State (Mar-20 to Aug-20)



We have seen hospitalisations rise over the month to a peak of 685 (as of 12 August) with total coronavirus deaths rising from 104 as of 30 June to 331 (as at 12 August). Elderly people have been the most affected In Victoria several aged care facilities amongst the worst-hit. Sadly, it may take some weeks before deaths peak going by overseas experience.

Policy

The government has announced new policy extensions with JobKeeper and the JobSeeker supplement the most anticipated. The former extends to March 2021 and the latter until December 2020. While welcome news given the economic drag introduced by the Victorian pandemic more may be required. An open question remains as to just how much repair has been achieved in terms of jobs growth and business solvency. Widespread mortgage deferrals by major banks as well as JobKeeper support prevent us fully understanding the economic damage already done. There is a real possibility that the extended programs may need to be bolstered further given the still rapid pace at which these are being scaled down over the next half-year. More will likely be forthcoming in the October Budget results.

Economic growth

The Westpac-MI Leading Index rose to -4.44% in June, up from -5.29% in May. This continues to suggest negative growth over the next 3-9 months. The Victorian lockdowns impacted sentiment negatively and are expected to weigh on growth in the near term. Pleasingly as noted elsewhere the recovery in hours worked nationally is welcome as is the continued recovery of industrial production overseas such as in the US and stronger iron ore prices continuing to rise over the month, an important driver of national income.

Consumer sector

The Westpac-Melbourne Institute Index of Consumer Sentiment fell substantially to 79.5 in August, down from 87.9 in July and near the extreme low of 75.6 in April (last seen previously during the global financial crisis). The escalation of lockdown restrictions in Melbourne to Level 4 was a key driver with confidence in Victoria falling 8.3%. It has spill over effects in other states as well with NSW and Queensland readings falling 15.5% and 8.1% respectively. The effects in the latter two are perhaps reflective of the shock of interstate border closures and the reliance on Victorian demand for Queensland for instance.

Inflation

The ABS Consumer Price Inflation Index fell -1.9% during the June quarter (consensus: -2.1%), slightly beating expectations. This was driven (as noted in our June update) by a mix of weaker energy prices on average, free childcare policies and the general weakness in demand across the economy with the brunt of lockdown measures felt during this period. We expect inflation to recover during the September quarter notwithstanding the weakness triggered by the Victorian lockdowns given the improvement in the economy since the June quarter. At current levels there is no pressure on the RBA to move on interest rates nor do we see this as likely over the next few years barring some severe exogenous shock.

Labour market

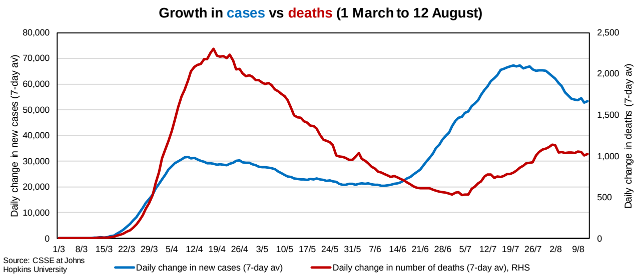
July saw 114,700 new jobs created. At the same time, we saw total hours worked rise 21.7% on the month of June suggesting business activity is normalising. It came as the unemployment rate also rose to 7.5%, up from 7.4% in June. This was driven by a sharp 0.6% rise in the participation rate as more workers re-joined the workforce. The recovery in hours worked was also confirmed by stronger demand in PMI survey. On balance this was a positive report showing signs of progress although we caution the full impact of the Victorian lockdowns may take time to feed into official data.

United States of America

Policy deadlock in Washington has stymied additional fiscal stimulus and seen President Trump intervene to support the economy in the interim. Leading indicators suggest growth is improving although the pace of improvement has moderated. Geopolitical tensions rose but have not yet exerted a material market or economic impact.

Coronavirus pandemic update

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



Daily new case growth has continued to moderate since peaking in mid-July. If the experience in the initial wave of cases affecting the North-East were to repeat it would suggest growth in coronavirus-related deaths will continue to moderate further in line with falling case growth. The measures necessary to achieve this included new lockdown restrictions in some of the worst-affected States such as Texas as well halting the scheduled relief of existing lockdown measures. These will continue detracting from growth while in place.

Policy update

Additional fiscal stimulus remains in a deadlock between the Democrat and Republic parties. It remains unclear whether this will occur. In the interim we saw President Trump take unilateral action. This included a majority-Federal funded solution to partially replace the expired *CARES Act* unemployment benefits of $US600/week. There are plans to suspend payment of payroll taxes to make hiring new workers more attractive to businesses in the US.

Geopolitics

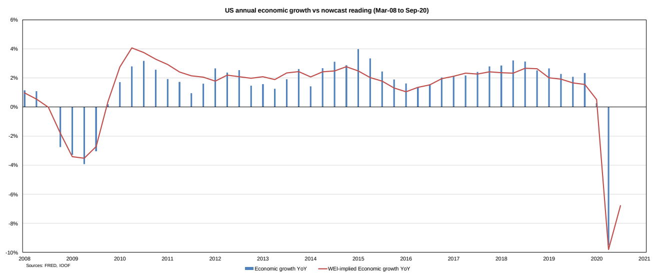
We saw further action on the policy front with President Trump announcing the banning of popular Chinese-owned apps TikTok and WeChat effective from 15 September. This move was ostensibly for national security reasons with US authorities concerned over the reach of the Chinese government into these platforms being used for espionage or blackmailing purposes against US citizens. A second additional benefit was imposing reciprocity given many US technology firm offerings such as Instagram or WhatsApp are effectively barred from China. This move may be costly for certain US firms such as Apple with China a major export market for their flagship iPhone product.

Separately US and Chinese representatives are meeting to discuss the implementation of the Phase 1 trade deal. It comes as China has fallen short of its pledge to increase US export purchases. At this juncture both appear committed to maintaining the agreement despite tensions elsewhere.

Economic growth

US GDP fell -9.5% in the year to June 2020 with substantial declines in consumer and investment spending the main drivers. As Chart 10 highlights we are expecting economic recovery to begin in the current quarter as most lockdown measures have been lifted and coronavirus case growth continues to moderate. The speed of the recovery will be challenged following the expiry of supplementary *CARES Act* unemployment benefits (which were injecting substantial stimulus into the economy). We will be better able to understand this impact over the coming weeks.

10. US GDP growth vs WEI forecast (Mar-09 to Sep-20)



Sentiment

The Markit Composite PMI improved further in July, rising to 50.3, up from 47.9 in June. This suggests activity across the manufacturing and services sectors had returned to expansion overall. The key driver was continued recovery in both output and new orders for US manufacturers with the Manufacturing PMI rising to 50.9, up from 49.8 in June. New orders increased for the first time since February overall, but foreign demand remained weak with a marginal decline in new export orders. While this was a positive result more confirmation will be needed with stronger demand and rising backlogs to cut into excess capacity.

The Services sector PMI rose to 50, up from 47.9 in June. This suggests activity was unchanged to the prior month. Key drivers of improved included stronger confidence and employment growth for the first time since February. However new orders continued to fall tied in part to pandemic restrictions for social distancing. The tightening of restrictions across several major States will also impact the necessary return to growth in the near term.

China

A continuation of the recovery from February lows into June was confirmed in official June quarter GDP result which beat expectations. 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 to 54.1 in July, down from a 10-year high of 58.4 in June, a sign of continued recovery albeit at a slower pace than observed in June. Both supply and demand for services offerings improved during July. However external demand remains a point of weakness with new export orders falling after recording expansion in the previous month with the pandemic seen as a major driver. Services firms continue to remain confidence about the economic outlook with the gauge for business expectations at its highest level since March 2015.

The Caixin China Manufacturing PMI picked up further, rising from 51.2 to 52.8 during July. The notable driver was stronger output and new business growth. Total new orders rose to their highest level since March 2011, driven mainly by domestic demand as new export orders remained in contractionary territory for a seventh-consecutive month.

11. Caixin China Manufacturing PMI (Jul-04 to Jul-20)

The combination of results saw the Chinese Composite PMI fall to 4.5, down from 55.7 in June. While new order growth was a positive, current readings still suggest overseas demand remains a point of concern. In addition, employment remains a recurring issue with the Chinese economy facing a mix of growing production with shrinking employment over recent months. Arguably more time is needed for business confidence to recover sufficiently to see new hiring begin in earnest.

Economic growth

The bounce back seen in Chinese PMI surveys saw confirmed in the June quarter GDP results. The Chinese economy grew 3.2% for the year to June beating consensus expectation of 2.4%. Key to this has been recovering industrial output growing 4.8% over the same period. However, the Chinese consumer recovery has been slower with a fall of -1.8% in the year to June (consensus: +0.5%).

Global tensions

Tensions over Hong Kong continue to persist but have translated into diplomatic retaliation and sanctions without further escalation. For instance, the US sanctioned 11 Chinese officials and allies in Hong Kong including the Territory's Chief Executive Carrie Lam. In response China announced it would sanction 11 US citizens including Republican senators Ted Cruz and Marco Rubio as well as Kenneth Roth, the executive director of not-for-profit Human Rights Watch.

Elsewhere we saw India ban social media app TikTok (owned by Chinese firm ByteDance) along with 58 other Chinese apps over security and privacy concerns. This followed border clashes between the two countries. In early August it appears that ByteDance is attempting to arrange investment by Indian conglomerate Reliance in order to preserve TikTok within India.

Inflation

Inflationary pressures in China have abated from their highs earlier in the year which had been driven by high pork prices. Chinese CPI grew 2.5% for the year to June while producer inflation fell for a fifth consecutive month by -3% over the same period (consensus: -3.2%).

Trade

Chinese imports grew for the first time since the coronavirus pandemic began, rising 2.7% vs consensus expectations of a -10% fall for the year to June. This was driven by increased demand for commodities including iron ore going towards increased investment spending in real estate and infrastructure. Pleasingly after months of struggling demand, they also saw exports rise 0.5% year-on-year a sign that global demand is perhaps beginning to recover after several months of weakness. Given the subdued signs in PMI surveys we note that these results may be a case of gradually rolling off trade war-related disruptions which caused large swings in demand for Chinese goods and abnormally inflated what the trade figures should have been.

Europe

A second wave of coronavirus cases has emerged in Europe centred on countries such as Spain and the Netherlands. These have not been as severe as countries' first wave on a positive note. We saw a landmark event with the European Recovery Fund finally reaching successful consensus. This is a major step not only as eventual economic stimulus but also towards European integration as a functioning union.

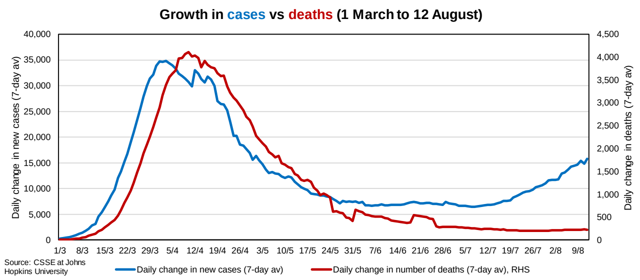
United Kingdom

On the monetary policy front the Bank of England repeated rhetoric that negative rates remain in its toolbox to stimulate the economy. The trade-off there would be in inducing currency weakness (to boost exports) albeit at the cost of effectively "taxing" the banking system.

The UK economy returned to growth during May rising 1.8% month-on-month after a record -20.3% fall in April when lockdown restrictions were at their zenith. A slower recovery in the services sector was a notable driver of the result which disappointed consensus expectations. In addition, the country is facing its own "fiscal cliff" moment in October when the government's wage subsidy program which supported some 9.6m jobs is set to conclude. The government has pushed back against calls for a wholesale extension of the program preferring instead to offer £1,000 payments to businesses for each worker they retain after October. According to the Bank of England some 3.5m workers are still furloughed (i.e. not working but being paid via the government scheme).

Coronavirus

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



Over the course of July and continuing into August we saw daily case growth escalate across Europe. The daily case growth 7-day average rose from ~7,000 as at 30 June to 15,800 as at 12 August. This was driven by a number of countries including Spain and the Netherlands and has prompted some localised lockdown measures as a result. However, this new wave appears to share some resemblance to the experience in the US South-East with average fatalities remaining substantially lower than the peak in early April.

Policy

Talks for an EU Recovery Fund reached a successful conclusion in July after months of negotiations. It amounts to some €750bn in grants and loans to counteract the impact of the coronavirus pandemic on the 27 member States. It will be the largest joint-borrowing effort agreed by the EU and signals an important step towards a functioning fiscal union across the disparate Member States. This was something unable to be reached in the wake of the global financial crisis and contributed to the EU experiencing a second recession during 2011 as a result of too many Members engaging in fiscal austerity at the same time and stifling economic growth.

The lynchpin of the deal is a 390bn grant program for the worst-affected countries namely Italy and Spain while a further 360bn will be made available as low-interest loans. The goal is to allow governments to maintain spending in the wake of lockdowns that have stretched public finances. It will be funded via issuance on international markets with the UK not involved in the deal. Lastly there are notable financial implications for environmental funding with 25% of all funding set aside for climate change initiatives, news that will further support investment in the region as it looks to meet its obligations under the Paris Agreement.

Business Activity and Economic growth

European PMI surveys continued to recover. The IHS Markit Eurozone Composite rose to 54.9 in July, up from 48.5 in June, while the Manufacturing PMI improved to 51.8 in July from 47.4. This result is consistent with broad-based expansion across both the manufacturing and services sectors. While overall new business grew for the region this was led by domestic demand as international trade continues to remain weak reflecting results seen elsewhere such as China. This is a welcome result but as Markit notes there remain existing challenges with social distancing that will limit the extent certain industries can recover to pre-pandemic levels.

Sentiment

According to Eurostat we saw gauges for both economic sentiment and employment expectations continue to rise from April lows. Sentiment has regained approximately half of the losses seen over the March-April period. Key drivers include recovery in services in retail trade while at a country level it was led by major countries such as Germany, France and Spain all seeing sustained increases.

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

Netwealth Group Ltd (+33.9%)

Netwealth Group (NWL) surprised the market after it released a business update showing that Funds Under Administration (FUA) had grown +35.0% yoy to $31.5bn with a record net inflow of $9.1bn for the financial year end June 2020. Funds Under Management (FUM) also performed strongly, increasing +84.4% yoy to $7.3bn. The growth comes at the expense of incumbent platform operators and despite an overall contraction in the size of the financial adviser market, with 21,687 financial advisers as of 30 June 2020, compared to 26,100 the same time the year prior. Although acknowledging the uncertainties of COVID-19, NWL expects FY20 results to slightly exceed previous guidance of $120m in revenue and underlying EBITA of $62m.

ALS Ltd (+29.4%)

ALS (ALQ) provided a business update at its AGM which showed positive developments in its commodities and life sciences businesses. ALQ's commodities division benefited from an increase in volumes and a strong gold price, while life sciences benefited from new opportunities to conduct COVID-19 laboratory testing (with minimum capital investment) and COVID-19 surface testing for high-touch surfaces. The resilience over COVID-19 combined with a positive outlook supported a strong rally over July.

Orocobre Ltd (+28.6%)

Orocobre (ORE) released its quarterly activities report for June 2020. Lithium carbonate production dropped -27% pcp to 2,511 tonnes and sales dropped -53% pcp to 1,601 tonnes. An average sale price of US$3,913/tonne (-53% pcp) was achieved which resulted in US$6.3m in revenue (-52% pcp). Although COVID-19 had severely impacted operations for the quarter, investors were encouraged by OREs Stage 2 expansion of its Olaroz mine and the increase in Electric Vehicle (EV) demand over the quarter. German and French EV sales grew 100% and 50% yoy respectively in the month of May as a result of increased government subsidies for EVs.

Avita Therapeutics Inc (-32.6%)

Avita Therapeutics (AVH) announced a partnership with the Biomedical Advanced Research and Development Authority (BARDA) in the U.S. to produce its flagship regenerative skin medicine RECELL. BARDA have agreed to a vendor-managed inventory plan valued at US$7.6m while also providing a supplemental funding arrangement of US$1.6m in the event of emergencies. Despite the positive news AVH shares continued to slide on fears that COVID-19 has restricted patients from accessing facilities and a reduction in new burns cases.

Adbri Ltd (-30.5%)

Adbri (ABC) shares declined after it lost a lime supply contract to US aluminium giant, Alcoa, which is estimated to be worth about $70m per year in revenue and ending a five-decade relationship with the producer. It is understood that the decision to withdraw the contract is understood to have come after a 2-year strategic review by Alcoa.

AMP Ltd (-21.0%)

AMP (AMP) shares tumbled after announcing an unexpected -50% decline in (unaudited) underlying profit for the half year in a trading update. AMP has been hit by the coronavirus pandemic, which has led to a decline in investment management and performance fees, while simultaneously facing public backlash for the appointment of Boe Pahari as chief executive of internal subsidiary AMP Capital for his role in a settled sexual harassment claim in 2017.

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

Movers and Shakers for the month of July 2020

ASX Code	Company Name	Closing price ($)	Month ago, close ($)	Month ∆ (%)	Quarter ago close ($)	Quarter ∆ (%)	Year ago, close ($)	Year ∆ (%)
NWL	Netwealth Group Ltd	12.01	8.97	33.9	7.59	58.2	8.33	44.2
ALQ	ALS Ltd	8.49	6.56	29.4	6.81	24.7	7.22	17.6
ORE	Orocobre Ltd	2.97	2.31	28.6	2.28	30.3	2.85	4.2
FMG	Fortescue Metals Group Ltd	17.41	13.85	25.7	11.96	45.6	8.33	109.0
OZL	Oz Minerals Ltd	13.63	10.96	24.4	8.97	52.0	10.29	32.5
CCP	Credit Corp Group Ltd	18.98	15.58	21.8	16.55	14.7	25.15	-24.5
MIN	Mineral Resources Ltd	25.74	21.17	21.6	16.78	53.4	16.07	60.2
APE	Ap Eagers Ltd	8.11	6.75	20.1	5.14	57.8	11.20	-27.6
PRU	Perseus Mining Ltd	1.54	1.31	17.2	0.97	59.1	0.69	122.5
MSB	Mesoblast Ltd	3.78	3.25	16.3	3.36	12.5	1.48	156.3

Source: Bloomberg, IOOF

ASX Code	Company Name	Closing price ($)	Month ago, close ($)	Month ∆ (%)	Quarter ago close ($)	Quarter ∆ (%)	Year ago close ($)	Year ∆ (%)
AVH	Avita Therapeutics Inc-CDI	6.07	9.00	-32.6	9.30	-34.7	8.70	-30.2
ABC	Adbri Ltd	2.21	3.18	-30.5	2.73	-19.0	3.54	-37.6
AMP	Amp Ltd	1.47	1.86	-21.0	1.43	2.4	1.79	-18.2
MND	Monadelphous Group Ltd	8.91	10.82	-17.7	11.30	-21.2	18.93	-52.9
OML	Ooh!Media Ltd	0.75	0.91	-17.6	1.04	-27.5	3.65	-79.4
WEB	Webjet Ltd	2.83	3.32	-14.8	3.06	-7.5	9.85	-71.3
QAN	Qantas Airways Ltd	3.23	3.78	-14.6	3.86	-16.3	5.71	-43.4
IEL	IDP Education Ltd	13.30	15.49	-14.1	14.86	-10.5	19.22	-30.8
CUV	Clinuvel Pharmaceuticals Ltd	22.04	25.65	-14.1	22.03	0.0	32.51	-32.2
PNV	Polynovo Ltd	2.19	2.54	-13.8	2.17	0.9	1.60	36.9

Source: Bloomberg, IOOF

Long-term asset class performance to July 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)	0.5%	7.6%	-14.2%	-9.9%	5.4%	5.1%	6.8%	7.4%	6.6%	7.5%
Australian equities - Mid caps	2.0%	14.5%	-7.2%	-2.2%	7.4%	9.9%	11.9%	9.5%	7.2%	9.9%
Australian equities - Small caps	1.4%	9.9%	-10.9%	-8.5%	6.5%	7.9%	6.3%	4.2%	3.8%	5.3%
Australian equities - Micro caps	6.9%	23.1%	-7.9%	-3.1%	6.8%	9.3%	6.0%	2.2%	4.1%	#N/A
International equities	0.6%	2.9%	-7.1%	3.4%	11.6%	8.1%	12.0%	12.3%	7.1%	3.5%
International equities (Hedged)	3.3%	10.6%	-3.6%	3.5%	6.9%	7.5%	9.9%	11.8%	8.0%	#N/A
International equities - Small caps	0.2%	4.2%	-12.7%	-5.7%	6.3%	5.6%	10.0%	11.6%	7.1%	6.8%
Emerging Markets equities	4.6%	7.6%	-3.8%	2.4%	6.6%	6.7%	7.7%	5.8%	6.9%	#N/A
Australian REITs	0.6%	6.1%	-25.5%	-22.8%	2.2%	3.4%	7.7%	9.2%	3.0%	5.9%
Global REITs	-1.3%	-3.5%	-25.2%	-17.6%	2.3%	1.6%	6.3%	8.1%	4.3%	#N/A
Global REITs (Hedged)	1.2%	3.6%	-22.6%	-17.4%	-1.8%	1.0%	4.4%	7.5%	4.7%	#N/A
Global Infrastructure	-1.2%	-4.1%	-18.5%	-8.7%	6.7%	6.1%	9.9%	10.9%	#N/A	#N/A
Global Infrastructure (Hedged)	1.4%	2.6%	-14.3%	-6.6%	3.3%	5.8%	8.3%	10.8%	#N/A	#N/A
Trend following	-1.2%	-9.7%	-2.6%	-0.8%	4.8%	-1.6%	6.1%	3.8%	4.1%	4.8%
Australian bonds	0.4%	1.0%	1.5%	3.6%	5.6%	4.6%	5.0%	5.6%	5.8%	6.0%
Australian bonds - government	0.3%	0.7%	1.5%	3.6%	5.8%	4.6%	5.1%	5.6%	5.8%	6.0%
Australian bonds – corporate	0.9%	2.4%	1.6%	3.6%	5.3%	4.8%	5.1%	5.9%	6.0%	6.2%
Australian bonds - floating rate	0.4%	1.0%	0.9%	1.7%	2.5%	2.8%	3.0%	3.8%	4.4%	4.8%
Global bonds (Hedged)	1.0%	1.8%	2.8%	5.5%	5.0%	4.7%	5.4%	6.0%	6.5%	7.1%
Global bonds - government (Hedged)	0.8%	0.8%	2.9%	5.3%	5.1%	4.7%	5.4%	5.9%	6.4%	#N/A
Global bonds - corporate (Hedged)	2.5%	5.5%	3.0%	7.4%	5.7%	5.8%	6.2%	7.0%	7.0%	#N/A
Global bonds - High Yield (Hedged)	3.5%	10.7%	-2.9%	-1.0%	2.6%	5.5%	6.0%	8.3%	8.6%	#N/A
Emerging Market bonds (Hedged)	3.8%	14.2%	-1.9%	1.5%	3.7%	5.8%	6.3%	7.3%	8.3%	10.1%
Cash (AUD)	0.0%	0.0%	0.2%	0.7%	1.5%	1.7%	2.0%	2.6%	3.7%	4.1%

Sources: Bloomberg, IOOF calculations

* AUD total returns as at Jul-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

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