

Market Wrap

November 2020

- There was good news on the vaccine front in November, with several drugs claiming 90%+ success rates against Covid-19. It is now up to regulators to approve/reject these treatments, before production can ramp up and for distribution to begin.
- These news releases supported investor sentiment and provided a strong tailwind for share markets. The US S&P 500 Index hit a new all-time record high during the month and share markets in other major regions also made positive progress. Most closed the month between 10% and 15% higher.
- The US election had earlier dominated attention. Donald Trump's reluctance to concede diverted attention from possible policy changes under the new Biden administration, but this will likely become an increasing focus for investors in the months ahead.
- Government bond yields were little changed, resulting in uninspiring returns from fixed income markets.
- Credit spreads narrowed sharply, both in Australia and overseas. This reflected optimism around the vaccines and a potential return to 'normality' in 2020, and supported returns from corporate bonds domestically and internationally.
- **US:** After four tumultuous years the Trump presidency will shortly come to an end, after he lost the election to Democrat rival Joe Biden. This was the first time since the early 1990s that a US president was not re-elected for a second term.
- Attention will now turn towards possible changes to US policy under the new administration. Relations with China will likely be most closely scrutinised, particularly whether Biden will consider removing tariffs imposed on imports from China.
- Separately, lockdowns that were introduced in some areas threatened to derail the rebound in the world's largest economy.
- US unemployment came down by a full percentage point in October, to 6.9%, but consumer sentiment deteriorated quite sharply and was lower than expectations. This likely reflected rising numbers of Covid infections and the likelihood of tougher restrictions being introduced. The spike in virus cases subsequently forced the closure of schools in New York, and saw additional restrictions introduced in California and elsewhere.
- With confidence dwindling, retail sales in the US have deteriorated to their lowest level for six months, suggesting the economic rebound that was underway might be losing steam.
- **Australia:** The Reserve Bank of Australia responded to the ongoing economic malaise by lowering interest rates to 0.1%.
- Policymakers also announced Australia's first ever Quantitative Easing program, which will see the Reserve Bank of Australia buying large quantities of bonds. This should help provide liquidity in the financial system and encourage lending.
- The latest employment data caused some consternation. It emerged that job numbers at the end of October were lower than at the end of September, in all States except Victoria.
- Net migration statistics were also a little surprising. Australia is in the midst of its biggest decline in immigration for more than 100 years. That suggests housing construction activity could slow and that the labour force could shrink in the years ahead.
- **New Zealand:** A policy review from the Reserve Bank of New Zealand indicated economic activity has been "more resilient" than expected. This suggests policymakers might reconsider introducing negative interest rates next year.
- Authorities must be mindful about stoking further house price inflation – prices are already more than 9% above 2019 levels.
- Prospects for a rebound in activity levels in 2021 are promising; consumer confidence jumped 8.7% in October from the previous month, for example.
- **Europe:** Consumer confidence levels dipped in both France and Germany, and were below consensus expectations. Lockdown measures appear to be affecting sentiment.
- Recognising the weakness, European Central Bank officials sounded a more cautionary note in their latest outlook statement. They warned growth in Eurozone economies is now likely to be "bumpier than previously projected" and referenced the risk of a "double-dip recession".
- The UK was in a national lockdown for most of the month, as authorities tried to slow the spread of Covid-19.
- The Bank of England committed a further £150 billion to its quantitative easing program, taking the total to nearly £900 billion; or more than 40% of UK GDP. In the near term, financial conditions and the economic growth outlook are being affected by ongoing Brexit uncertainties and lockdown-related pressures.
- Like elsewhere, there was a strong rebound in UK GDP growth in the September quarter, compared to the virus-related drop in the June quarter. Nonetheless, economic growth was still nearly 10% below 2019 levels, which remains a concern.
- **Asia/EM:** Japan is seeing deflation again; consumer prices were down -0.4% year-on-year in October, amid subdued economic conditions. Department store sales are currently running 1.7% below 2019 levels, underlining the fragility of consumer confidence and the impact of virus-related disruptions.
- Business investment is also subdued. Machine tool orders, normally a reasonable indicator of investment and activity levels, remain around 6% below 2019 levels.
- In China, there was speculation that officials could start to tighten policy settings as the economy continues to recover from Covid-related weakness. Bank funding costs and Chinese bond yields have started to rise as these expectations have increased.

Australian dollar

- The strong 'risk on' sentiment following the vaccine news acted as a tailwind for the Australian dollar; a currency that is typically correlated with global growth.
- The AUD appreciated by 4.9% against the US dollar and by 3.4% against a trade-weighted basket of international currencies.

Australian equities

- Australian equities experienced their best monthly return since the inception of the S&P/ASX 100 Index back in May 1992.
- Impressive vaccine results, bundled with additional monetary stimulus and the outcome of the US election, helped push equities higher across the globe.
- At one point, the S&P/ASX 100 Accumulation Index had risen more than 13%, but weakness in the final stages saw the index finish the month 10.2% higher.
- The reaction to the vaccine news was most noticeable in the previously struggling Energy sector (29.1%).
- Oil prices moved 23% higher (in USD terms) given the prospect of recovering demand, particularly from the transportation industry. As a result, all Energy sector constituents delivered double-digit positive returns in November.
- The Materials sector (7.1%) also moved higher. Rising iron ore prices, up 11% in USD terms, helped offset weakness in the gold price. The 'yellow metal' fell 6% (in USD terms), given rising real yields and vaccine-related optimism.
- Consumer Staples (-1.6%) was the only sector to decline in November. Treasury Wine Estates fell 6.3% following a decision by the Chinese Ministry of Commerce to place tariffs on all Australian wine imports.
- Australia's small companies marginally outperformed their large cap peers, with the S&P/ASX Small Ordinaries Accumulation Index rising +10.3%.

Listed property

- Real estate securities posted strong gains in November, with the FTSE EPRA/NAREIT Developed Index climbing 7.9% in Australian dollar terms.
- The best performing regions included France (35.9%), Spain (33.7%) and Canada (17.8%).
- Property markets were primarily driven by the vaccine-related optimism, which has brought forward expectations for the 'normalisation' of behaviour and economic activity.
- This could provide disproportionate relief to real estate assets tied to non-essential communal interaction and tourism, including hotels/resorts, shopping malls, gaming/leisure assets and hospitality venues, which have been materially affected by Covid-19 restrictions during 2020. Unsurprisingly, these sectors rallied during the month, albeit from heavily sold off levels.
- Locally, the A-REIT market gained 13.2%, largely driven by the shopping mall landlords. Unibail-Rodamco-Westfield (73.1%), Vicinity Centres (36.4%) and Scentre Group (33.3%) all performed extremely well.

Global equities

- It was an exceptional month for major global equity markets, buoyed in particular by the growing vaccine optimism as several companies sought to obtain approval for distribution in both Europe and the US.
- The MSCI World Index rose by almost 12.0%, outperforming the MSCI Emerging Markets Index, which rose by 9.2%, both in local currency terms.
- Gains were led by European markets, notably Spanish equities as the IBEX 35 rose by 25.2%, followed by the Italian FTSE MIB and the French CAC 40, which added 22.9% and 20.1% respectively, all in local currency terms.
- UK equities also rebounded after October's falls, with the FTSE 100 Index rising by 12.4%.
- In Asia, the Japanese Nikkei 225 Index was a standout, adding 15.0%.
- In the US, the beginning of the month was dominated by the presidential election. While the results of the contest boosted sentiment, it was the positive news on a vaccine that drove equities higher over the month. The S&P 500 Index rose by 11.0% in local currency terms.

Global and Australian Fixed Income

- Government bond yields in major regions traded in quite wide ranges during November, but closed the month little changed in most cases.
- In the US, there had been suggestions that Treasury yields might soar in the case of a Biden victory in the presidential election. But in the event, longer-dated yields fell slightly and shorter-dated yields were unchanged.
- The size of the latest US stimulus program seems likely to be smaller than initially expected, suggesting Treasury issuance might not rise as quickly as some had projected. This appeared to prevent yields from rising too significantly.
- Bond yields did rise modestly in the UK and Europe, reflecting comments from central bank officials that suggested support programs could be increased in size.
- Domestic yields rose too, with the 10-year Commonwealth Government Bond yield closing the month 7 bps higher. This resulted in a small negative return from the local bond market.

Global credit

- Encouraging news on the vaccine front and the very strong performance of global equity markets acted as a tailwind for corporate bonds.
- Credit spreads narrowed sharply in both the investment grade and high yield segments of the market, rewarding investments in global credit products.
- There was a fair amount of activity on the merger and acquisition front, with some large deals announced. Collectively, companies appear willing to deploy some of the capital they have raised over the past six months or so, particularly with an end to the pandemic potentially in sight.
- Suggestions that the European Central Bank will persevere with its large asset purchase program were supportive of local issuers. Corporate bonds in Europe outperformed those in the US over the month, though both fared very well.

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