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MONTHLY UPDATE ON THE INVESTMENT ENVIRONMENT

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MARKET UPDATE

After starting on a high note, 2020 is now shaping up as a year of considerable headwinds for the global economy, with the rapid spread of the COVID-19 virus taking a heavy toll on markets. The downturn was exacerbated by plummeting oil prices amid an impasse in Saudi-Russian production negotiations.

By mid-March, the COVID-19 virus had exceeded 125,000 confirmed cases and claimed 4,500 lives globally. It has now been designated a pandemic by the WHO. While the rate of new cases in the country of origin, China, has slowed, the virus has now spread across a broad range of countries. COVID-19 now looks set to have a potentially far-reaching economic impact. However, the duration and severity of the epidemic are key uncertainties, and government and central bank responses have, thus far, provided a degree of comfort to investors.

Australia's fourth quarter GDP came in at an improved annual growth rate of 2.2%. Nonetheless, the data was below-trend, with consumer spending, dwelling construction, and new business investment all posting weak data.

Given the Australian economy's reliance on Chinese demand for commodities, tourism and education, the impact of coronavirus on the local economy is expected to be significant. Coupled with the added risk of a local virus outbreak, the RBA made the decision to cut the cash rate by 0.25% at its early March meeting to a new record low of 0.50%. Markets are now pricing in a nearly-certainty of a further cut to 0.25% in early April; the rate at which the RBA had previously signalled it would then turn to quantitative easing.

While the nation's housing prices continued to benefit from record-low interest rates, other data was less sanguine; unemployment increased to 5.3%, underemployment and wage growth remain poor, and sentiment indicators weak.

In the US, fears of a global pandemic led the Federal Reserve to make its first inter-meeting cut since the GFC in 2008, reducing the target range by 50 basis points in early March to 1.00% to 1.25%. Markets are now fully pricing in at least a further 75-basis-point cut at the next meeting on 18 March, in which case the target rate will fall to 0.25% to 0.50%. US jobs data continues to be resilient; the unemployment rate fell to 3.5%, and average hourly earnings grew at a relatively robust 3.0%.

Following 'Super Tuesday' on 3 March, during which 14 US states voted on their preferred Democratic Party candidate for the 2020 Presidential elections, the race has narrowed to two contenders; centrist Joe Biden and leftist Bernie Sanders. The former staged a remarkable comeback after Sanders' early successes in primaries. Biden is more business-friendly than Sanders, however President Donald Trump is considered firm favourite to win a second term against either candidate.

In China, the emergence of COVID-19 led to a dramatic slowdown in manufacturing production. As expected, sentiment gauges fell away, with the Caixin China Services PMI falling from 51.8 to a record low of just 26.5, and its official services equivalent similarly falling from 54.1 to 29.6. Manufacturing PMI also fell, with the official survey falling from 50.0 to 35.7 while the Caixin index fell to 40.3; both record lows, but less pessimistic than the services industry readings. Indeed, there is a glimmer of hope for the Chinese economy, with the rate of new COVID-19 cases within China now slowing. Given the added benefit of central bank stimulus, Chinese equities rallied 14% from their early February low into early March.

While the rate of new COVID-19 cases in China slows, attention is increasingly shifting to the Eurozone economy, particularly Italy, which by mid-March has the highest number of new cases in the world. The Italian government announced fiscal stimulus to help restore confidence in its economy. Elsewhere, Eurozone economic data remains broadly stable, with unemployment low and inflation tepid. However, sentiment data has improved following the easing in Sino-US trade tensions, with the IHS/Markit Manufacturing PMI reading of 49.2 the highest in a year, and the German print hitting a 13-month high of 48.0. These indicators do, however, pre-date the increased spread of COVID-19 in the region.

Risk assets sold down amid fears of a global pandemic. Australian equities fell 7.8% over the month, while hedged developed overseas equities fell 8.5%. Unhedged equities fared better, with the flight to safety triggering a fall in the Australian dollar to an 11 year low against the US dollar. Escalating global concerns saw the VIX Index, a measure of implied US equity market volatility, rise to its highest level since the GFC.

Fixed interest assets, meanwhile, had a strong month as investors flocked to 'safe harbour', driving US and Australian 10-year sovereign yields to record lows.

Table: Index Returns to 29 February 2020

	MONTH (%)	THREE MONTHS (%)	FYTD (%)	ONE YEAR (%)
Australian Equities				
S&P/ASX 300 Accumulation Index	-7.8	-5.2	-0.1	8.7
S&P/ASX Small Ordinaries Accumulation Index	-8.7	-5.9	-1.9	1.6
International Equities				
MSCI World (ex Australia) Index (hedged A$)	-8.5	-6.7	-0.7	4.4
MSCI World (ex Australia) Index (unhedged A$)	-4.9	-1.6	8.3	15.6
MSCI Emerging Markets Index (unhedged A$)	-1.6	1.8	5.3	8.3
Property				
S&P/ASX 200 A-REIT Accumulation Index	-4.9	-3.3	1.1	11.8
Australian Fixed Interest				
Bloomberg AusBond Composite Index	0.9	1.5	3.9	9.0
Global Fixed Interest				
FTSE WGBI ex-Aust (hedged A$)	1.6	3.2	5.1	10.1
Barclay's Global Capital Aggregate Bond Index (hedged A$)	1.2	2.8	4.6	9.3
Cash				
Bloomberg AusBond Bank Bill Index	0.1	0.2	0.7	1.3
Commodities				
Gold (US$ per ounce)	3.2	11.9	15.3	23.1
Copper (US$ per metric tonne)	1.2	-3.9	-6.0	-13.4
WTI Crude Oil (US$ per barrel)	-13.2	-18.9	-23.4	-21.8
RBA Index of Commodity Prices (A$)	1.5	2.4	-6.3	-1.1

Table 1: Australian Dollar versus Foreign Currencies to 29 February 2020

AUSTRALIAN DOLLAR VERSUS	AS AT 29 FEBRUARY 2020	MONTH (%)	THREE MONTHS (%)	FYTD (%)	ONE YEAR (%)
US Dollar	0.65	-2.7	-3.9	-7.0	-8.7
British Pound Sterling	0.51	-1.0	-3.8	-8.5	-5.8
Euro	0.59	-2.7	-4.1	-4.1	-5.7
Japanese Yen	70.75	-3.0	-4.7	-6.2	-10.5