ECONOMIC AND MARKET COMMENTARY
SEPTEMBER QUARTER 2020

Australia:

Key points:

- **The Australian economy entered its first recession in 30 years after experiencing the largest contraction on record in Q2.**
- **The Reserve Bank of Australia (RBA) left interest rates at 0.25% for another quarter.**
- **JobKeeper payments have been extended until March 2021 at a reduced rate.**

Whilst the outlook for economic rehabilitation was positive at the end of the last quarter, a substantial coronavirus outbreak in Victoria beginning late June saw the State come under another extended lockdown. Economic activity resumed throughout the rest of Australia following successful virus containment, with some states easing their border restrictions. Australian equities were flat over the September quarter (Q3) (-0.1%) following the impressive recovery in Q2. Information Technology and Consumer Discretionary were again the highest performing sectors for the quarter, posting returns of 13.0% and 10.1% respectively, whilst Utilities and Energy were the weakest sectors (-8.2% and -13.5% respectively).

Data released during Q3 revealed the profound impact of COVID-19 on the Australian economy over the June quarter. The economy contracted by a historic 7% in Q2 – the most severe contraction on record following the largest shock to economic growth since the Great Depression – putting Australia into an official recession for the first time in three decades, after the 0.3% contraction in Q1. Annual GDP growth to June 2020 fell to -6.3%. Inflation was -1.9% over the June quarter, driven largely by the declining prices of childcare, fuel and rent despite large increases for some food items and household goods. Overall, year-on-year inflation was negative at -0.3% for the first time since 1997.

The Federal Government announced in July that the JobKeeper scheme would be extended to further support business affected by coronavirus. Originally scheduled to end in September, the scheme will now run until March 2021, however payment rates were reduced at the end of September and are scheduled to reduce further in January 2021. As of 27 September, superannuation funds had made payments of $33.8 billion to members as part of the Superannuation Early Release Scheme, with the second tranche of the scheme beginning in July. The RBA left interest rates unchanged at 0.25% throughout the quarter. The unemployment rate reached a 22-year high of 7.5% in July and the RBA expects it to peak at nearly 10% in the December quarter. Outside of Victoria, the easing of restrictions is expected to aid recovery in the labour market but the improvements may be more than offset by the losses in Victoria as well as the tightening of

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the JobKeeper program where it is expected that some workers will be retrenched once they are no longer eligible for the subsidy.

Other economic conditions were weak over the September quarter. The manufacturing PMI (measured by the Ai Group Australian Performance of Manufacturing Index) fell to 46.7 at the end of the quarter, down from 51.5 at the end of the June quarter, with a reading below 50 representing a contraction in output. The services PMI improved (according to the Ai Group Australian Performance of Services Index), with the index reaching 36.2 by September. While this was an improvement on Q2, a value below 50 indicates that services activity continued to decline, albeit at a slower pace. Business sentiment dropped at the beginning of the quarter but rose slightly to finish at -4 according to the NAB Business Confidence survey. Consumer confidence (measured by the Westpac Bank Consumer Sentiment Index) remains volatile, dropping to 79.5 in August as Victoria went into its second lockdown but recovering to 93.8 by September.

Returns for period ending 30 September 2020	**Quarter**	**1 Year**
Australian Equities[1]	-0.1%	-10.0%
Consumer Discretionary	10.1%	3.3%
Consumer Staples	-3.9%	-3.5%
Energy	-13.5%	-38.9%
Financials, ex Property Trusts	-5.8%	-28.2%
Health Care	0.8%	19.7%
Industrials	0.3%	-13.8%
Information Technology	13.0%	27.7%
Materials	4.1%	7.2%
Telecommunications Services	-2.5%	-8.1%
Utilities	-8.2%	-9.6%

[1] S&P/ASX 300. Below are sub-sectors.

The Aussie dollar appreciated marginally against a basket of major currencies over the quarter with the Trade-Weighted Index measuring 60.7 at the end of September, up from 60.0 at the end of June. In particular, the AUD rose from 68.63 US cents to 71.08 US cents by quarter-end, however it depreciated slightly against the Chinese yuan, euro and British pound.

The Australian Government 10-year bond yield fell by 3 basis points to 0.85% over Q3, down from 0.88% at the end of Q2. Australia's 10-year government bond yield remained above the US 10-year bond yield (0.68%) for another quarter. The Bloomberg AusBond Composite Index was somewhat volatile over the quarter, posting its largest negative return in August (-0.4%) but recovering in September (1.1%) giving an overall return of 1.0% for the quarter.

International:

Key points:

- **Reported global COVID-19 cases surpassed 30 million and the death toll reached one million.**
- **Governments and central banks continued to implement expansive economic policy; the Federal Reserve shifted its inflation targeting approach to be more accommodative.**
- **Economic data for Q2 indicates severe global contraction in Q2, putting many countries into a recession.**

COVID-19 cases showed no signs of slowing down over the quarter, with over 34 million recorded infections and one million deaths by the end of September. Many countries experienced secondary outbreaks after easing their restrictions earlier in the year, and a severe outbreak in India saw the country become one of the global leaders in infections. US-China relations deteriorated further, with the US rejecting China's claim in the South China Sea and President Trump terminating Hong Kong's special trade status. Tensions between Australia and China have also risen markedly, following the arrest of Australian television anchor Cheng Lei, who was working for Chinese state media, and the announcement that China would be investigating alleged subsidies to Australian winemakers on top of an anti-dumping investigation. Global equity markets were positive, with the MSCI World Index ex Australia (hedged to AUD) posting a 6.4% return over the quarter. Following the significant recovery in the June quarter, and positive performance over the September quarter, Chinese and US equity markets recovered to pre-COVID levels.

The US economy shrank by a record-breaking 31.4% in the second quarter of the year (as revealed in Q3), pushing the economy into a recession. In August, the US Federal Reserve announced it would be modifying its inflation targeting approach to be more accommodative. The central bank is now targeting an average of 2% inflation instead of a fixed 2% and is now willing to tolerate a period of "moderate" inflation overshooting after a period of undershooting to achieve the target. The change was implemented in September, with the Federal Reserve indicating that rates are expected to remain unchanged at 0.00%-0.25% until at least 2023. The second round of financial stimulus was a point of significant debate over September, with negotiators unable to broker a deal. House Democrats passed an updated version of the HEROES Act, originally passed in May but immediately dismissed by the Republican Senate, which featured a reduced price tag ($2.2 trillion, compared to the original $3.4 trillion), but the revised bill is still unlikely to be passed by the Senate. Unemployment in the US continued to fall, reaching 7.9% by quarter-end (down from 11.1% last quarter), although the jobs recovery has begun to show signs of slowing down following reduced government stimulus and a sustained rise in coronavirus case numbers.

US equities rose 8.9% over the quarter, as measured by the S&P 500 Composite in local currency terms, with the index recovering to pre-pandemic levels in August – although a monthly dip in September marked the first month of losses since the index began its rallying recovery in March. The National Association of Home Builders/Wells Fargo Housing Market Index (HMI) rose to a record 83 in September, with the reading indicating a positive overall outlook for sales conditions as record-low mortgage rates continue to boost demand for new homes. Activity in the manufacturing sector also recovered as measured by the US Markit Manufacturing PMI, with the index reaching 53.2 in September (a reading above 50 indicates expansionary activity) after recording three months of contractionary activity throughout Q2. Consumer sentiment remains low, as measured by the University of Michigan Consumer Sentiment Index which currently reads at 74.1 for August (down from 78.1 at the end of last quarter). US annual core inflation was reported at 1.7% in August 2020 (the latest figure available), up from 1.2% in June.

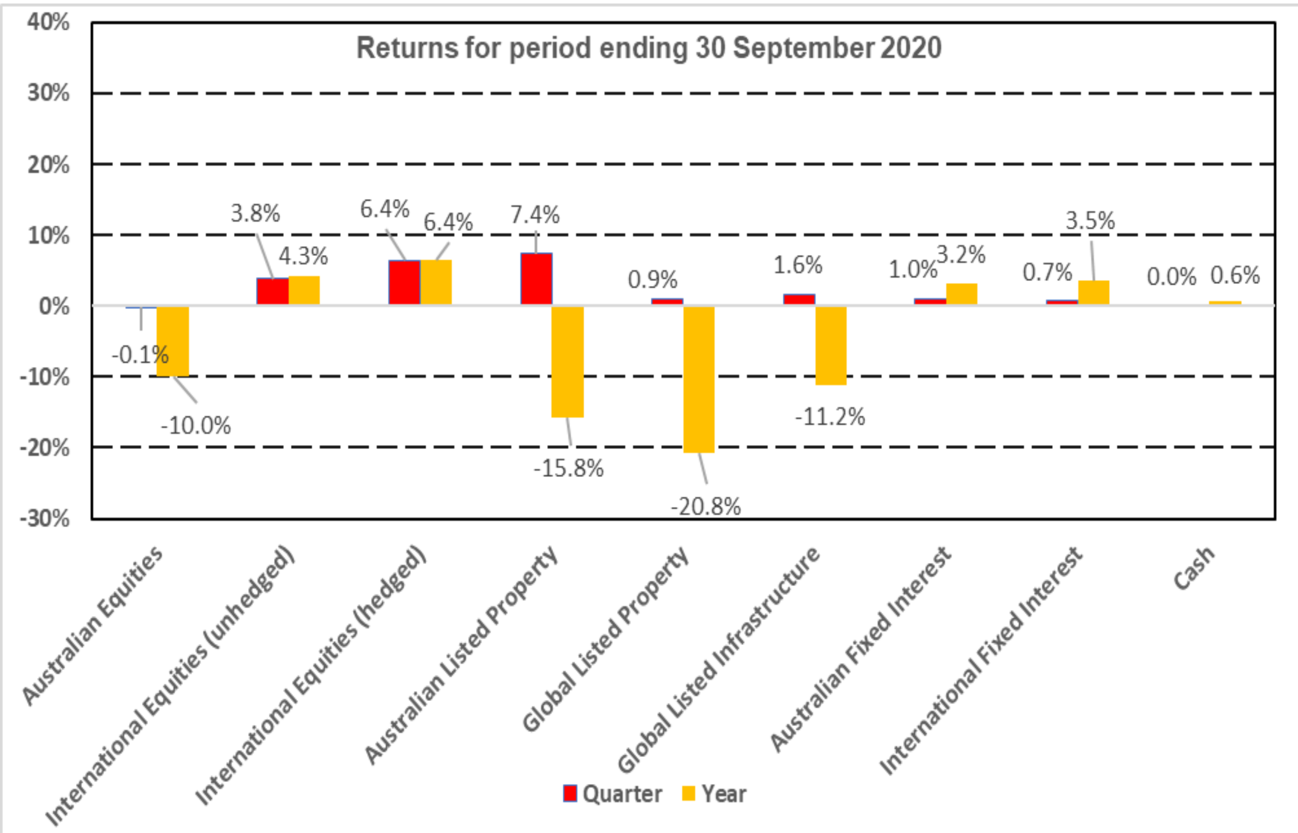
European equities fell by 0.8%, as measured by the Euro Stoxx 50 Index in local currency terms. In July, the European Union reached a deal on an economic recovery plan worth €750b. The European Central Bank left rates unchanged at -0.5%. Manufacturing activity recovered over the quarter, with the Markit Eurozone Manufacturing PMI reaching 53.7 in September, up from 47.4 in June. Eurozone headline inflation is expected to fall to -0.3% year-on-year in September, the steepest fall in prices since April 2016. Annual Eurozone core inflation (which excludes prices of volatile items such as food and energy) is likely to decrease further to a record low of 0.2% in September 2020, down from 0.8% in June over the same month in the previous year.

The Chinese equity market returned 7.8% as measured by the Shanghai Composite Index (in local currency terms), despite a 5.2% fall in the month of September. China's GDP recovered in the June quarter, growing by 11.5% after its 10% contraction in the previous quarter. The manufacturing industry continued its steady recovery, with the China Caixin Manufacturing PMI increasing to 53.0 in September, up from 51.2 in June.

Japanese equities returned 4.7%, as measured by the MSCI Japan Index (in local currency terms). The Markit/Nikkei Final Japan Manufacturing PMI rose consistently over the quarter, ending at 47.7, although the sub-50 reading still indicates a small contraction in manufacturing activity. In September, Shinzo Abe resigned as Prime Minister of Japan due to health reasons, with his successor Yoshihide Suga pledging to continue to implement Abe's expansive economic policy dubbed "Abenomics". The Bank of Japan left interest rates unchanged at -0.1%. Year-on-year inflation remained below pre-pandemic levels at 0.2% in August, compared to 0.1% at the end of Q2.

Globally, most bond yields fell over the quarter, except in the US and UK where 10-year government bond yields rose to 0.68% (up 3bps) and 0.23% respectively (up 6bps). Italian government bond yields fell by 46 bps to 0.87%. German government bond yields fell by 6bps to -0.52%, whilst Japanese government bond yields were flat at 0.02%.

Global listed infrastructure and global listed property posted modest returns of 1.6% and 0.9% over the September quarter, as measured by the FTSE Developed Core Infrastructure 50/50 Index (AUD hedged) and the FTSE EPRA/NAREIT Developed Rental Net TRI Index (AUD hedged) respectively. Despite their recovery in Q2, one-year returns remain negative at -11.2% and -20.8% respectively.



Returns for period ending 30 September 2020	Quarter	1 Year
International Equities (unhedged) [1]	**3.8%**	**4.3%**
North America	5.0%	8.6%
UK	-3.8%	-20.7%
Europe (ex UK)	2.1%	-1.6%
Japan	2.7%	0.6%
Asia Pacific (ex-Japan)	6.7%	11.1%
Emerging Markets	5.2%	4.0%
China A Shares	9.7%	23.9%
International Equities (hedged) [3]	**6.4%**	**6.4%**
Australian Listed Property [4]	**7.4%**	**-15.8%**
Global Listed Property [5]	**0.9%**	**-20.8%**
Global Listed Infrastructure[6]	**1.6%**	**-11.2%**
Australian Fixed Interest[7]	**1.0%**	**3.2%**
International Fixed Interest[8]	**0.7%**	**3.5%**
Cash[9]	**0.0%**	**0.6%**

1. S&P/ASX 300 Accumulation Index
2. MSCI World ex-Australia Index (with net dividends reinvested in A$)
3. MSCI World ex-Australia Index (with net dividends reinvested hedged in A$)
4. S&P/ASX 300 A REIT Accumulation Index
5. FTSE EPRA/NAREIT Developed Net TRI Index (Net Total Return hedged in A$)
6. FTSE Developed Core Infrastructure 50/50 Index (Net Total Return hedged in A$)
7. Bloomberg AusBond Composite Index
8. Barclays Global Aggregate Hedged in AUD Index
9. Bloomberg AusBond Bank Bill Index

All returns are based on accumulation indices. Data sourced from eVestment Alliance, Datastream and Thomson Reuters.

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