

SINKING INTEREST RATES – CONSIDERATIONS FOR INVESTORS RELYING ON INCOME



PERPETUAL PRIVATE INSIGHTS
18/10/2020

The year has been a challenging one in Australia. Having begun 2020 with heartbreaking bushfires tearing across our country, we were allowed no relief as the emergence of coronavirus came to the fore in February.

COVID-19 has presented the world with a health crisis which has, due to the absence of a vaccine, created an economic crisis as a consequence of the lockdown. To put this in perspective, the Deputy Governor of the Reserve Bank of Australia, Guy Debelle, described it as the “largest peacetime economic contraction since the 1930s”.

In response to the economic crisis, monetary authorities (central banks) globally reduced interest rates, in a bid to reduce finance costs for individuals and businesses, as well as to support the prices of financial assets. Through this lens, they have been broadly successful. This is largely the reason that financial markets have regained much of what was lost during February and March this year.

Unfortunately, just as a rising tide lifts all boats, a sinking interest rate drags down all income. So, despite the encouraging progress in softening the impact of the initial shock and now helping facilitate recovery in the economy, it has not been without cost.

Over the past few months, we have seen many companies seek to reduce dividends as a defensive measure to protect themselves through the uncertainty wrought by the pandemic. This has helped drive an acute fall in income distributions across investment markets.

As economies recover, we expect many of the factors that drove income lower, to begin to work in reverse. Inherently, we anticipate income to improve from its current low, into 2021, but not to the levels for 2019. From there, the success of stimulus measures on building a robust recovery, will become the key driver for economic growth, which should further improve income.

In our Quarterly Market Update, we look at the various considerations and challenges that have and will face investment markets through until the end of the year.

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