THOUGHTS ON THE MARKET

11th August 2020 - Risk markets begin the new week with marginal advances

SUMMARY

- Global risk markets were marginally higher overnight in a quiet session which didn't add to the recent global narrative. The macro calendar was light, but President Trump's intervention to provide additional unemployment benefits and to defer payroll tax, evictions and student loans repayments dominated the headlines but seemingly face logistical challenges and concerns that they do not remotely address the December quarter fiscal cliff. There also wasn't much in corporate news as the June quarter reporting season winds down which meant markets drifted for most of the session with value and traditional cyclical sectors outperforming for a second consecutive day.

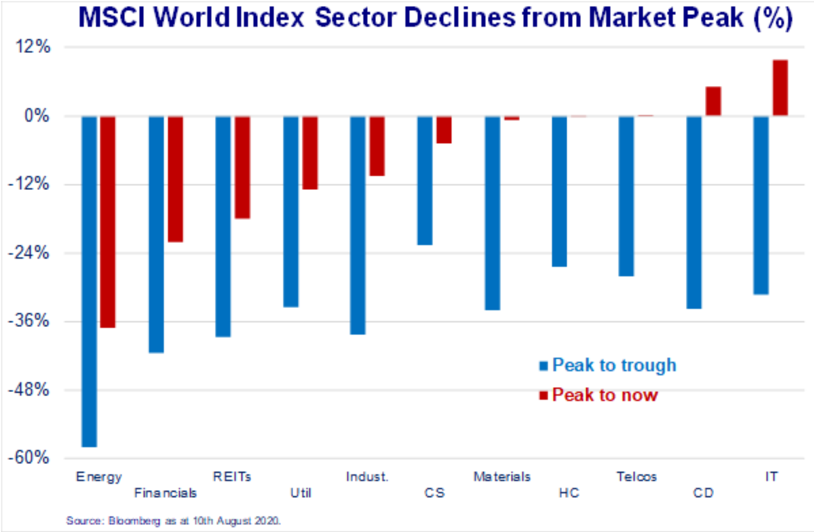
  In other markets, 10-year US Treasuries rose two points to 0.58% (two week high) and the curve slope increased fractionally to 0.48%, commodities were mixed with oil (+1.9% to USD41.99 per barrel) posting its strongest rise in almost three weeks and gold slipped a bit further from its Thursday record high price (-0.6% to USD2,028 per troy ounce), and G10 currencies were mixed against the US Dollar with the Euro (-0.4%) and AUD (-0.1% to USC71.49) both depreciating, the Yen was steady and Sterling (+0.1%) clawed back some of Friday's loss.

- There was nothing of note on the macro or the corporate calendars which were light in volume and even lighter on market changing news. Both calendars will remain quiet until Friday when the US details July retail sales and China provides its slew of its July activity including industrial production and retail sales.

- The number of global cases of COVID-19 is 19.98 million with another +166k cases so far (but Brazil, Mexico, and 7 US states have not reported their numbers) which means that Monday is likely to be the 23rd occasion in the past 23 days where daily increases have topped 200k. This means 4 countries have more than 800k cases, 19 countries have more than 200k cases and 24 countries have more than 100k cases. It took 73 days to record 1 million cases, and after this each subsequent million has taken 13 days, 11 days, 12 days, 10 days, 11 days, 8 days, 8 days, 7 days, 6 days, 5 days, 5 days, 5 days, 4 days, 5 days, 3 days, 4 days, 4 days and 4 days. More importantly, the growth rate of daily confirmed cases (+1.3% since Friday) is once again coming down. Meanwhile, deaths stand at 732.9k and the death rate dropped for the 96th straight day to 3.67% although the number of daily deaths is on the rise.

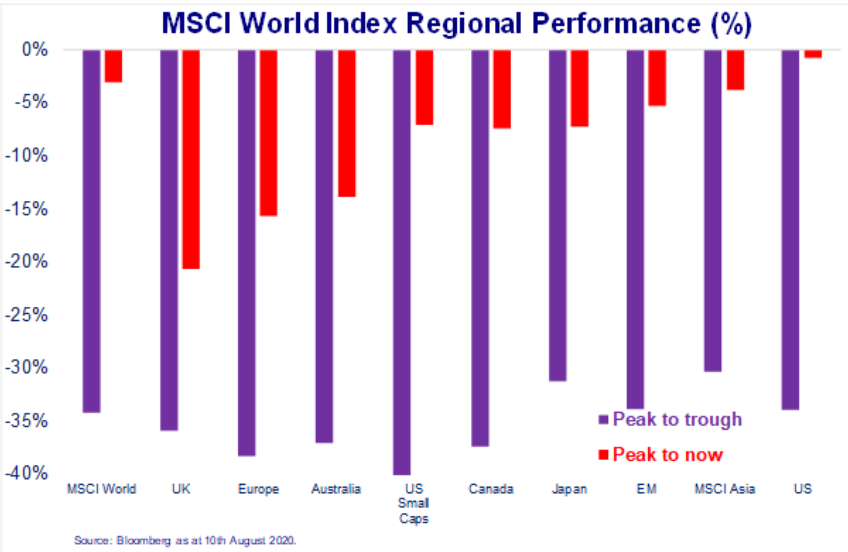
FINANCIAL MARKETS

- **EQUITIES**
  - **The MSCI World Index closed +0.2% higher** with traditional value sectors outperforming. Energy (+2.4%) was the star of the day with investors buoyed by a rising crude price and comments from Saudi Aramco who said that oil demand will continue to build. Similarly, industrials (+1.3%) continued its recent win streak (now at 6 days) with the sector rallying behind cheap valuation and strength in airlines and machinery producers. Meanwhile, financials added to Friday's gains with strength in lift insurers and banks and credit card providers. In contrast, defensive sectors declined including healthcare (-0.4%) and telcos (-0.3%), and growth sectors also fell led by tech (-0.5%) given more FAANG weakness. The overnight moves saw energy (-37.1%) and financials (-22.7%) still in bear market territory, whereas three sectors have recorded complete recoveries (see chart).



- **Among the regions**, performance was subdued across the board, with advances led by US equities (+0.3%) which closed higher in a session where the narrative was unchanged from Friday and this saw value and traditional cyclical sectors outperform again, and tech lag. President Trump's executive actions to provide some additional unemployment benefits, and deferrals for payroll tax payments, evictions and student loans repayments dominated the headlines, but face logistical challenges and don't really do much to address the December quarter fiscal cliff. Interestingly, the market still expects the White House and Congress to reach a deal of around USD1.5 trillion which is a high hurdle. The macro calendar had nothing today and the corporate calendar was also light as earnings season draws to a close which meant most indices drifted with gains in the US market led by the Dow Jones (+358 points, +1.3% to 27791), the Russell 2000 (+1.0%) and the S&P 500 (+0.3%), but the NASDAQ 100 (-0.4%) declined for a second straight session.

  European markets also closed higher (+0.2%) in a quiet session where COVID-19 was the main story with EU health commissioner Stella Kyriakides confident on a vaccine by turn of year. Meanwhile, the Ifo survey suggested that German companies expect public life to be restricted for a further 8.5 months due to the virus, although there is a split between booming and affected industries. There wasn't much else on the macro front and by the closing bell all regional markets closed higher with gains led by Spain (+1.5% which had lagged badly in the past two weeks, Italy (+0.7%), Sweden (+0.5%), France (+0.4%), the UK (+0.3%), Switzerland (+0.2%) and Germany (+0.1%).

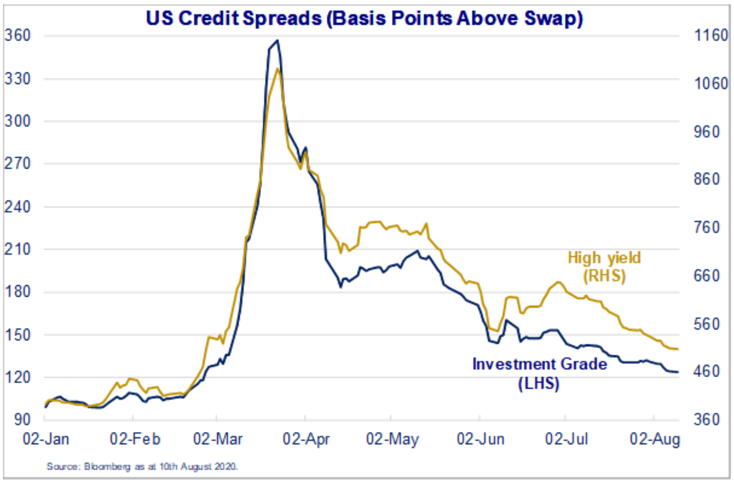


  Asia equities were flat yesterday in a session where there was a lot of headlines, but none of them consolidated into a market changing thematic. The macro calendar was thin in volume with only China inflation of note with the CPI and PPI close to street estimates and therefore had little market impact. Geopolitical tensions between the US and China were noted including the US announcing sanctions on several Hong Kong officials including chief executive Lam for their role in curtailing political freedoms, but this was a non-event from a market perspective. By the close of trading, the MSCI Asia Pacific index was unchanged with large gains in Australia (+1.8%) and South Korea (+1.5%), moderate gains in Taiwan (+0.5%) and mainland China (+0.4%), whereas Hong Kong declined (-0.6%) and Japan was closed for a public holiday.

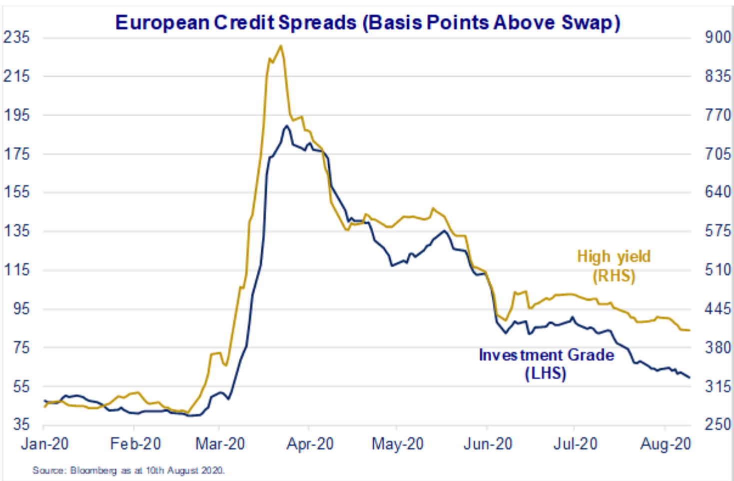
- Futures markets are pointing to a mixed opening in Asia with Australia (-0.1%) slated for opening bell losses, whereas Japan (+0.5%) and Hong Kong (+0.3%) are priced to advance.

CREDIT MARKETS

- Regional credit indices were quiet with spread movements capped by high recovery rates and still high corporate leverage. In the **US investment grade space**, spreads declined -1 point to +124 bpts which kept the recovery rate at 92%. Ten of the 11 sub-sectors recorded lower spreads but only tech (-2 points, +101 bpts, 91%) was more than a basis point. In the high yield universe spreads were unchanged at +509 bpts, which kept the recovery rate at 86%. Seven of the 11 sub-sectors recorded lower risk premiums with the largest moves recorded in cyclical sectors including senior financials (-4 points, +368 bpts, 68%), subordinated financials (-4 points, +533 bpts, 71%) and energy (-3 points, +760 bpts, which has recorded a complete recovery), but these capital gains were partially offset by a decline in industrials (+8 points, +629 bpts, 59%) which defied the trend in its equity peer.



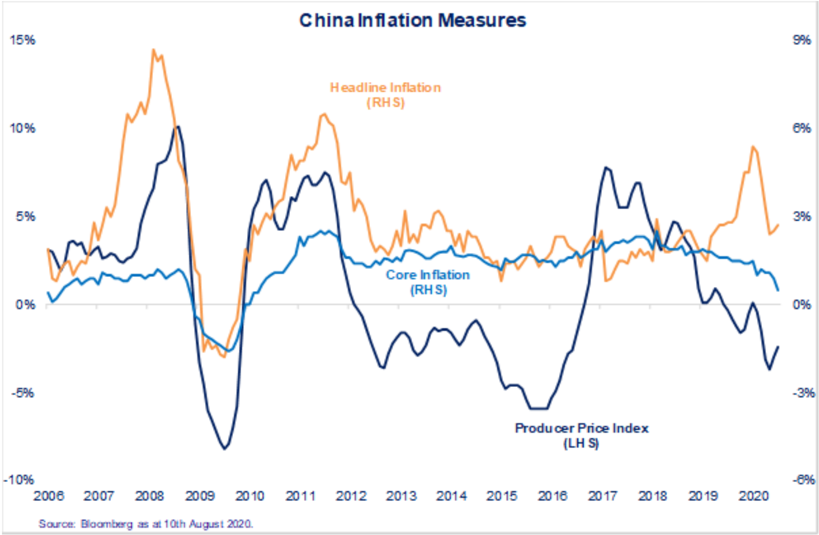
- **European credit markets** were also subdued in terms of price action with spread declines in the investment grade space totalling -3 points to 60 bpts which lifted the recovery rate two notches to 87% (only marginally below its US peer). All 11 sub-sectors recorded lower risk premia, but moves were modest led by healthcare (-3 points, +29 bpts, 93%), materials (-3 points, +49 bpts, 87%) given rising base metals prices, and tech (-3 points, +27 bpts, 83%). In the high yield universe, spreads declined -2 points to +409 bpts, which was enough to lift the recovery rate one notch to 78%. Ten of the 11 sub-sectors recorded lower risk premiums, but movements were minor with consumer discretionary (-3 points, +470 bpts, 82%) the largest.



THE GLOBAL ECONOMY

- **Chinese CPI inflation** rose +0.6% m/m in July which took the annual rate up to +2.7% y/y. Among the components, food inflation increased +2.8% m/m and +13.2% y/y given acceleration in pork prices (+3.6% m/m and +10.3% y/y) and energy prices rose solidly (+2.4% m/m), but when both were excluded the remaining core inflation reading was flat in July with the annual rate declining to +0.5% y/y on base effects, which is a 10-year low (see chart). Meanwhile, PPI inflation increased +0.4% m/m (second consecutive monthly rise) and the annual rate lifted +0.6% to -2.4% y/y given large rises in mining (+3.1% m/m) and raw materials (+0.9% m/m), but the rise in manufacturing was marginal (+0.1% m/m) which suggests that excesses remain within upstream price structures.

  Looking ahead tight food supply will see headline inflation rise in coming months, but this should prove temporary and price inflation is likely to head lower given likely consumption softness. Meanwhile, an expected investment recovery should support the demand for raw materials and industrial products and reduce deflation in the industrial space.



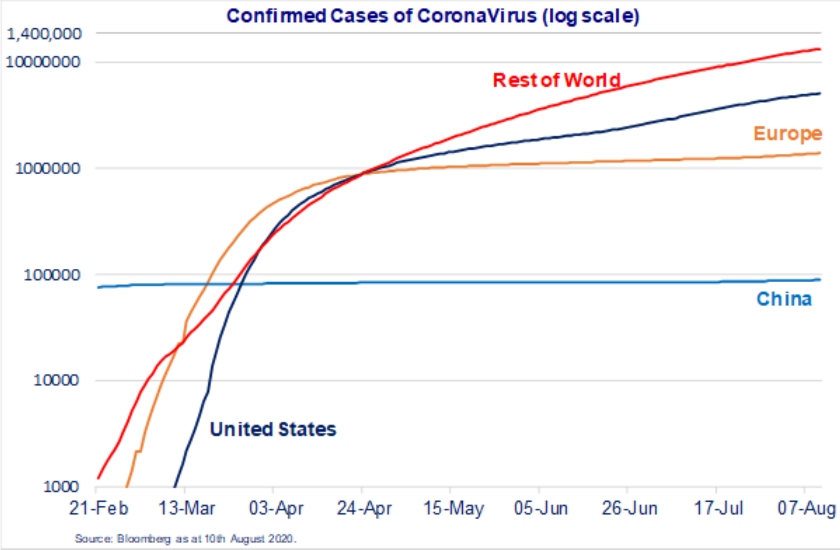
POLICY

- There were no substantive policy announcements overnight. However, data revealed that the Federal Reserve added to USD2.5 billion of assets to its corporate bond portfolio in July which brought the total in its secondary market credit facility to just over USD12 billion. In addition to individual corporate bonds, the bank purchased USD2.5 billion in the iShares iBoxx US Dollar Investment Grade Corporate Bond, USD331 million of iShares iBoxx High Yield Corporate Bond and USD35 million of holdings in the VanEck Vectors Fallen Angel High Yield Bond fund. In addition, Fed loans through the Main Street Lending Facility increased USD92 million across 13 companies, which was in line with what Vice Chair Clarida noted last week about increase usage of the Main Street Lending Facility moving forward.

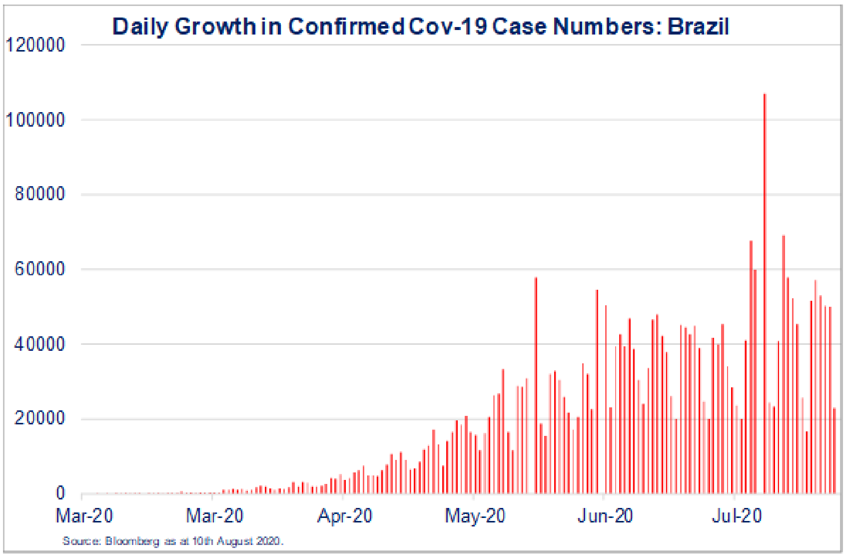
VIRUS UPDATE

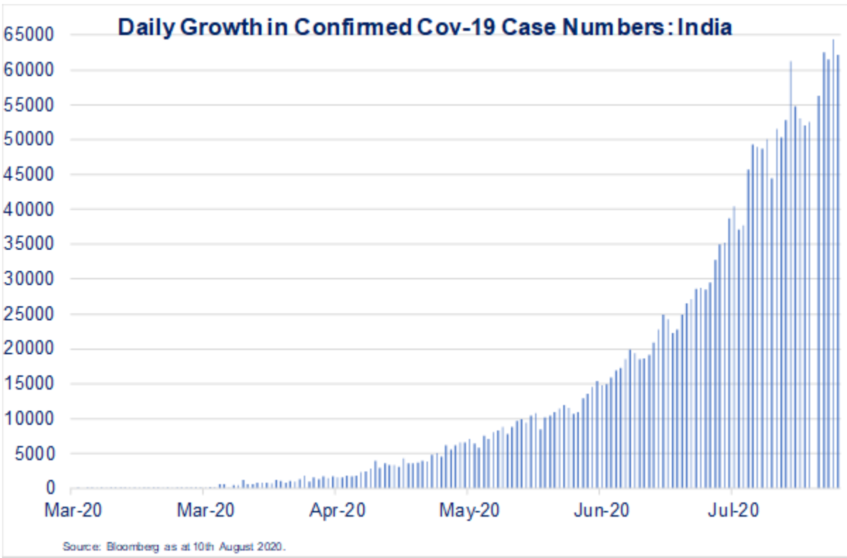
- The number of global cases of COVID-19 is 19.98 million with another +166k cases so far (but Brazil, Mexico, and 7 US states have not reported their numbers) which means that Monday is likely to be the 23rd occasion in the past 23 days where daily increases have topped 200k. This means 4 countries have more than 800k cases, 19 countries have more than 200k cases and 24 countries have more than 100k cases.

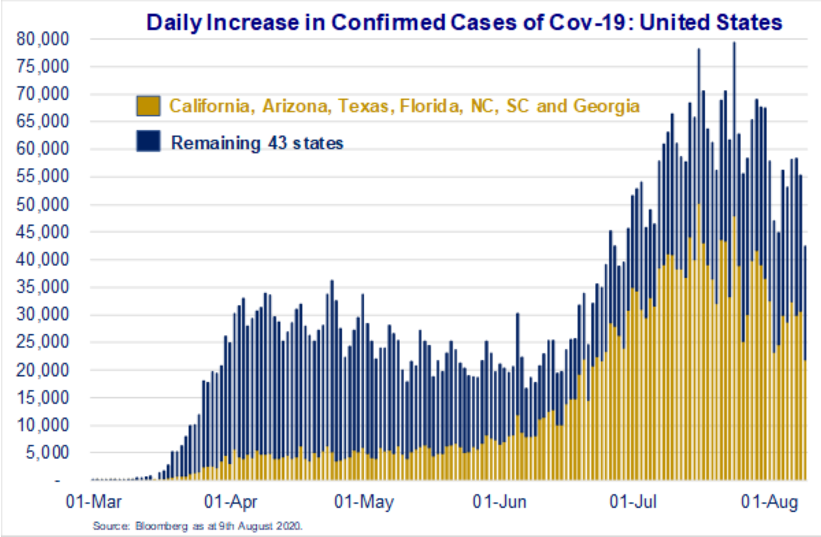
  It took 73 days to record 1 million cases, and after this each subsequent million has taken 13 days, 11 days, 12 days, 10 days, 11 days, 8 days, 8 days, 7 days, 6 days, 5 days, 5 days, 5 days, 4 days, 5 days, 3 days, 4 days, 4 days and 4 days. More importantly, the growth rate of daily confirmed cases (+1.3% since Friday) is once again coming down. Meanwhile, deaths stand at 732.9k and the death rate dropped for the 96th straight day to 3.67% although the number of daily deaths is on the rise.



- We break the infections into four groups – the US, Europe, China and 'others' and the rest of the world outside the G3 economies now has the most total cases (+118k to 16.3 million) and highest daily new cases (and by a considerable margin) followed by the US (+30.8k (50-day low) to 5.08 million, although 7 states are yet to report). The issue for the US is that they never flattened their curve which means economic opening has not been associated with lower case numbers, and rising case numbers are also evident in Europe (+16.3k (16-week high) to 1.4 million - see chart).

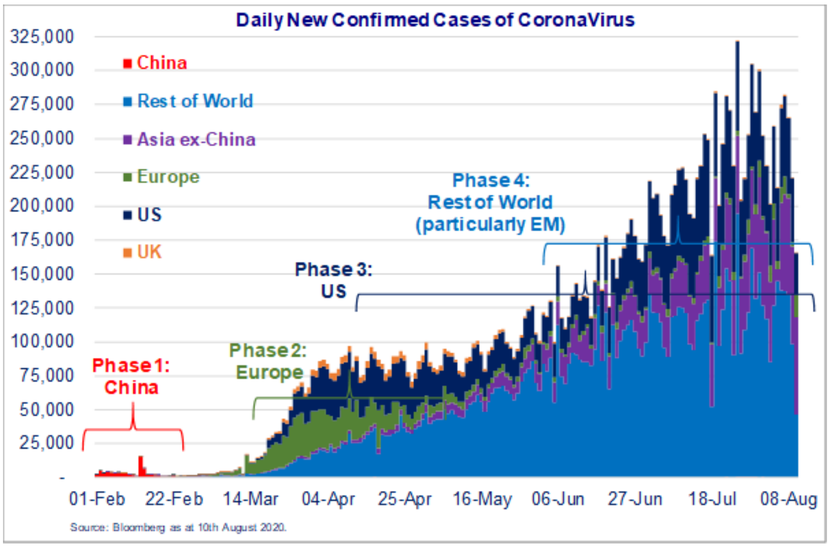






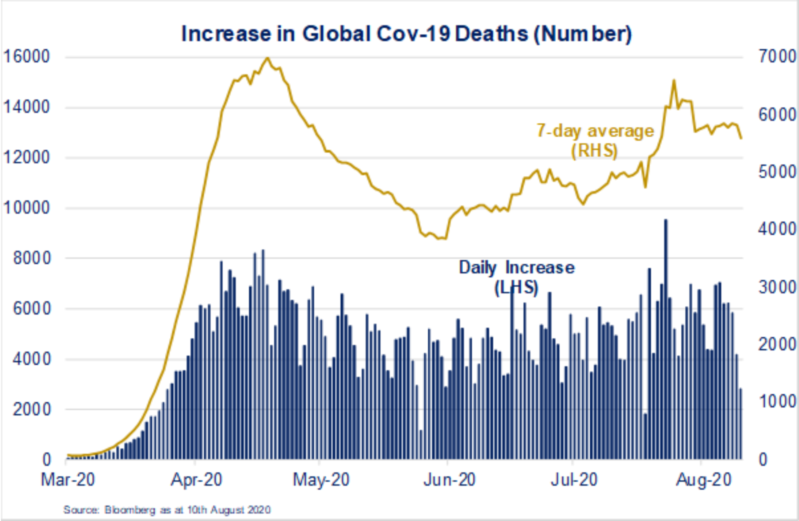
- Among countries, the most cases are in the US (+30.9k (so far) to 5.08 million, with 7 states yet to report), Brazil (not reported to 3.04 million), India (+62.0k to 2.22k), Russia (+5.1k to 890.8k), South Africa (+3.7k to 563.6k), Mexico (not reported, +480.3k), Peru (+7.0k to 478.0k), Chile (+2.0k, 375.0k), Iran (+2.1k to 328.8k), Spain (+8.6k to 323.0k), United Kingdom (+0.8k to 313.4k), Saudi Arabia (+1.3k to 290.0k), Pakistan (+0.5k to +284.7k), Bangladesh (+2.9k to 260.5k), Italy (+0.3k to 250.8k), Turkey (+1.2k to 242.0k), France (+4.0k (14-week high) to 239.3k), and Germany (+1.2k to 218.5k). Australia confirmed cases rose +313 to 21.4k yesterday which placed us 65th in terms of total infections.

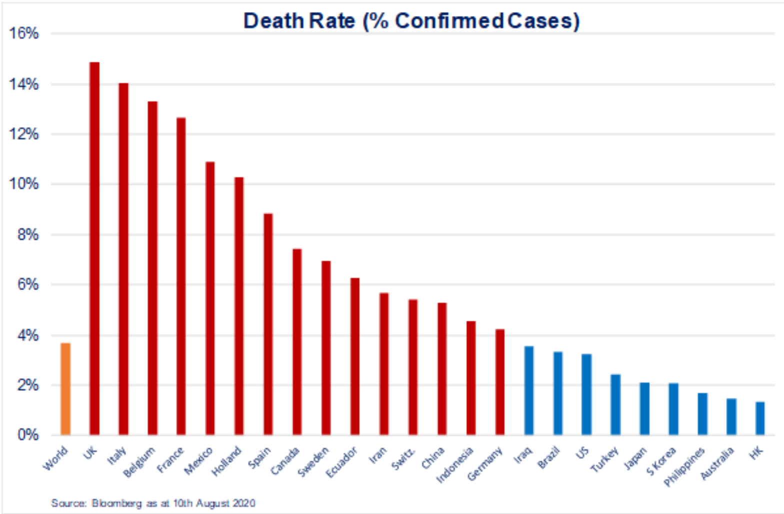
  Elsewhere, Singapore recorded +0.2k new cases to 55.3k most of which are linked to foreign workers who are forced to live in crowded dormitories, but Indonesia (+1.7k to 127.1k) is now on the rise and has the second most cases in the region behind only the Philippines (+6.7k to 136.6k).



- Although final numbers are not in until 1pm AEST, the global death rate declined for a 96th straight day to 3.67% with the global total to 732.9k after another 2.8k deaths overnight, so far, which indicates the daily average deaths is increasing again (see chart). The US (+0.3k so far) has the most deaths at +163.3k, with Brazil (not reported, 101.0k), Mexico (not reported, +52.3k), the UK (+8 to 46.7k), India (+1.0k to 44.4k) ,Italy (+4 to 35.2k) and France (+8 to 30.3k) all over +30k. The death rate is highest in European countries where the health systems had collapsed led by the UK (-0.21% to 14.9%), Italy (steady at 14.0%), Belgium (-0.1% to 13.3%), France (-0.1% 12.7%), the Netherlands (-0.1% to 10.3%), Spain (-0.1% to 8.9%) and Sweden (-0.2% to 6.9%). However, several emerging markets are now on the leader board including Mexico (-0.1% to 10.9%), Ecuador (-0.1% to 6.3%), Indonesia (-0.1% to 4.5%) and Brazil (-0.1% to 3.3%).

Perpetual





Yours sincerely,

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MORE INFORMATION

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