

# THOUGHTS ON THE MARKET

18<sup>th</sup> June 2020 - Global COVID-19 cases continue to surge

## SUMMARY

- Global risk markets were mostly lower overnight and, in the process, broke a four-day win streak as worrying increases in COVID-19 cases overtook optimism on stimulus measures. On a quiet data night, virus news dominated headlines with large increases in Brazil, Chile, India, the US and Saudi Arabia (among others). Meanwhile, Texas reported a surge in hospitalisations and Iran warned it may need a new lockdown. In the end, the market has run a long way and a lot of good news is in the price and the narrative around policy stimulus, reopenings and better economic data are well known so the market may be needing a new thematic to push materially higher from here. Given we're working with a phenomenon that is not economic or financial in its nature and COVID-19 cases are still growing strongly, there is likely to be sustained higher volatility which means investors may need a comprehensive set of diversifiers to maintain recent gains.

In other markets, 10-year treasuries closed -1 point lower at 0.74% with little curve movement, commodity prices were lower with gold (-0.2% to USD1727 per troy ounce) doing better than oil (-1.8% to USD37.70 per barrel), and G10 currencies mostly weakened against a strong Greenback with losses in the Euro (-0.6%), AUD (-0.7% to AUD68.82) and Sterling (-0.8%), but the Yen (+0.3%) bucked the trend.

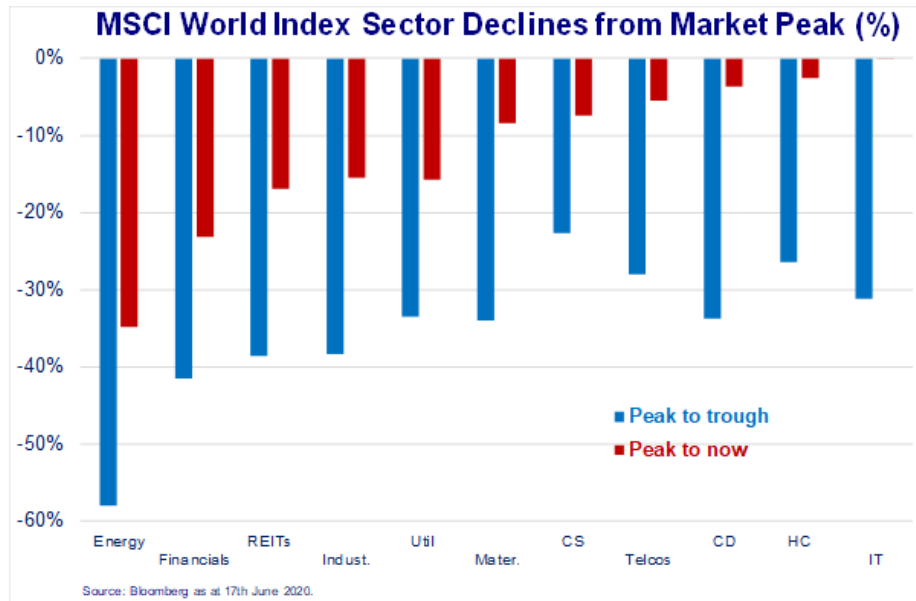
- There was no major economic news overnight and Chair Powell had his second day in front of the US Congress and noted that withdrawing fiscal support too quickly would be a concern. He noted that now is not the time to worry about debt and that individual corporate bond purchases will be reduced as market functioning had improved. Finally he reiterated his recent comments on interest rates (on hold until inflation and unemployment goals are within sight), balance sheet size (not an inflationary concern at present), yield curve control (gathering more information but no decision has been made) and negative rates (highly unlikely).
- Although final numbers are not in for another 5.5 hours, the number of global cases of COVID-19 was 8.3 million overnight with another +154.8k cases so far (second highest and that is before Mexico, Pakistan and some US states report their numbers) which means that Wednesday was the 20th occasion in the past 22 days where daily increases have topped 100k (and the other two were over 99k!). This means 3 countries have more than 500k cases, 9 countries have more than 200k cases and 17 countries have more than 100k cases. It took 73 days to record 1 million cases, 13 days for the next million, 11 days for the third million, 12 days for the fourth million, ten for the fifth million, 11 for the six million and 8 days for the seventh and eighth million. More importantly, the growth rate of daily confirmed cases (+1.7% since Sunday) is starting to rise (albeit modestly). Meanwhile, deaths stand at 447.6k and the death rate dropped for a forty second straight day to 5.38%.

## FINANCIAL MARKETS

### • EQUITIES

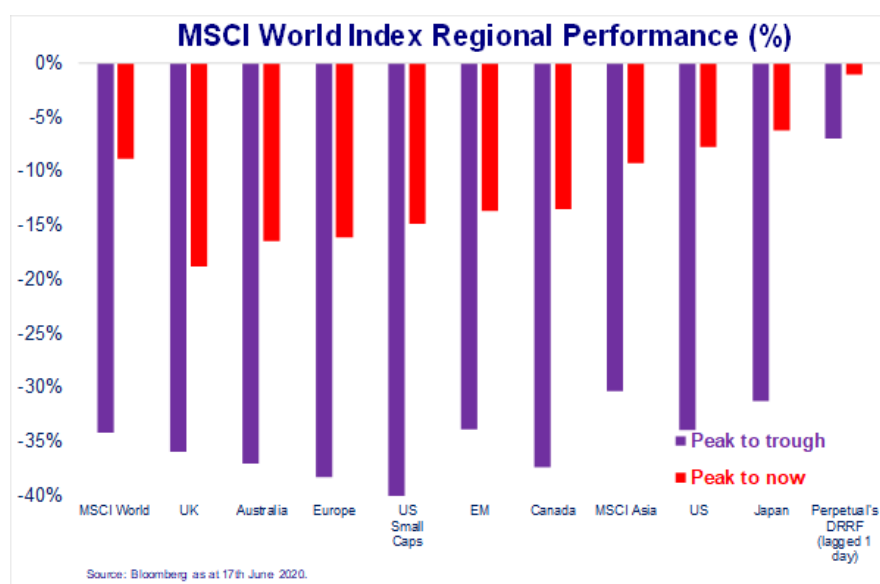
- The MSCI World Index declined -0.1% overnight with mixed performances across regions and sectors as sub-indices swung between gains and losses during the US session, which was characterised with light trading volumes. **Among the global sectors**, performance was the antithesis of recent days in that the traditional value/cyclical sectors underperformed led by energy (-2.3%, and -12.6% in the past 7 sessions) given the lower oil price, financials (-0.9%, -7.5%) which sold off given concerns about the recovery and NPLs, and REITs closed lower (-0.6%, -3.7%) on concerns about higher vacancy rates and the accelerating move to on-line consumer spending around the world.

The overnight moves took energy (with a peak to trough decline of -34.8%) and financials (-23.1%) deeper into bear market territory with REITs (-17.0%), utilities (-15.7%) and industrials (-15.5%) not far away. In contrast, global IT has recovered all its losses since February for the second time (see chart).



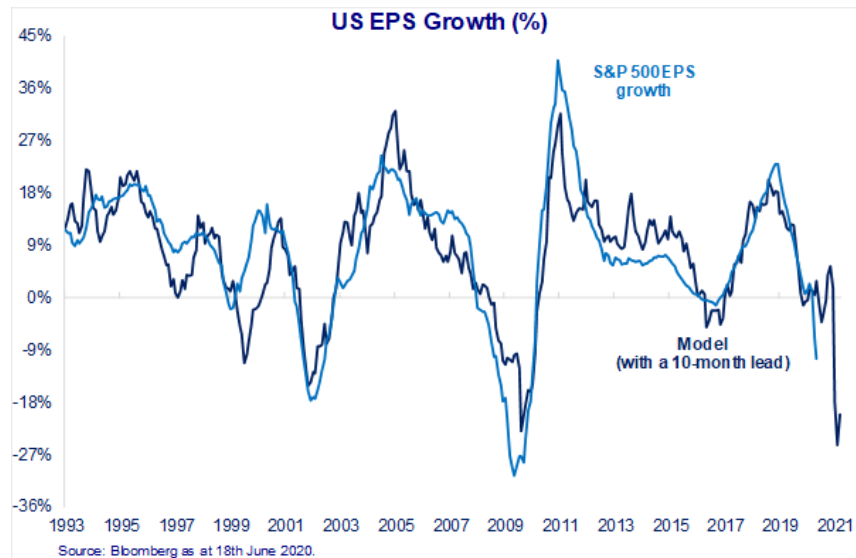
- **Among the major regions**, losses were largest in the US which oscillated between gains and losses for much of the session but eventually closed near its trough in a day which was light on economic news. Given the data absence, Cov-19 news dominated the headlines with record daily case numbers in 9 US states including Texas and Florida which saw investors question the recovery and value/cyclical sectors underperformed and this meant the Russell 2000 Index (-1.8%) was at the wrong end of the performance tables. Meanwhile, strong performance in Amazon (+1.0%) and Microsoft (+0.3%) saw the NASDAQ rise (+0.2%), with the S&P 500 (-0.4%) off less than the Dow Jones Industrial Average (-0.7%, -170 points, 26,120) given the latter's higher value exposure.

Earlier in Europe stocks rallied (+0.8%) and outperformed their global peers for a second consecutive session, but it was not across-the-board advances with northern markets such as Switzerland (+1.7%), France (+0.9%), Germany (+0.5%) and the UK (+0.2%), outperforming weaker periphery markets such as Italy (-0.2%), Spain (-0.2%) and Greece (-0.7%). Before that, the MSCI Asia Pacific index closed +0.3% higher as advances in Australia (+0.8%), Hong Kong (+0.6%), Korea (+0.1%) and China (+0.1%) were partially offset by a decline in Japan (-0.6%) given the weaker Yen. Overnight movements had little impact on market peak-to-now losses and recovery rates (see chart) with the UK (-18.8%), Australia (-16.5%) and Europe (-16.1%) all close to bear market territory.



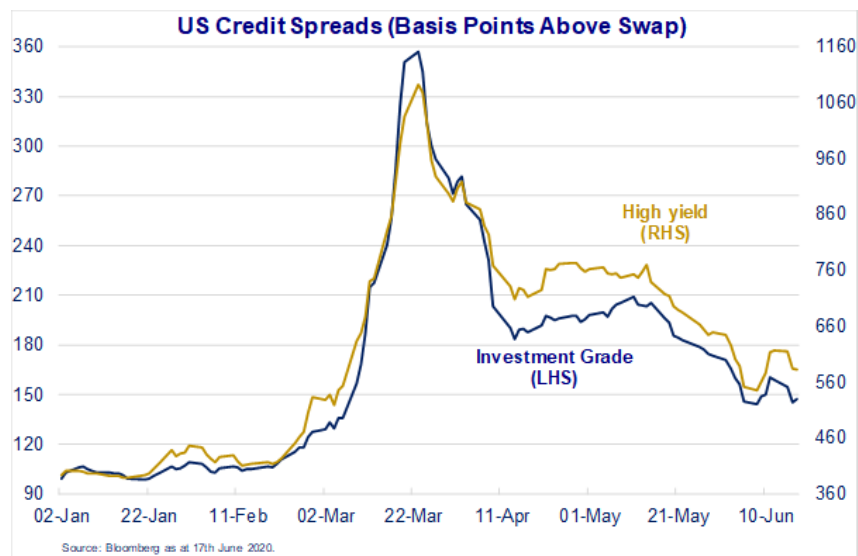
Futures markets suggest a negative opening in Asia with at-the-bell losses expected in Australia (-0.6%), Japan (-0.4%) and Hong Kong (-0.2%) with China flat.

Meanwhile, the second last variable in our US earnings model was released overnight and the model has risen for the first time in four months and suggests that US EPS growth should trough at around -25% -30% in 2020 (see chart), and then potentially recover. Interestingly, the model's 2020 estimate is lower than that of early 2009 but the key here is the potential for a turn, although one has to be careful about not over-emphasising a single month of improvement even though it's hard to imagine re-openings being bad for corporate bottom lines. We are all allocating capital and undertaking EPS estimates in a world of elevated uncertainty which means things may not go up or down in a straight line, but the May improvement is a better sign than a further deterioration.

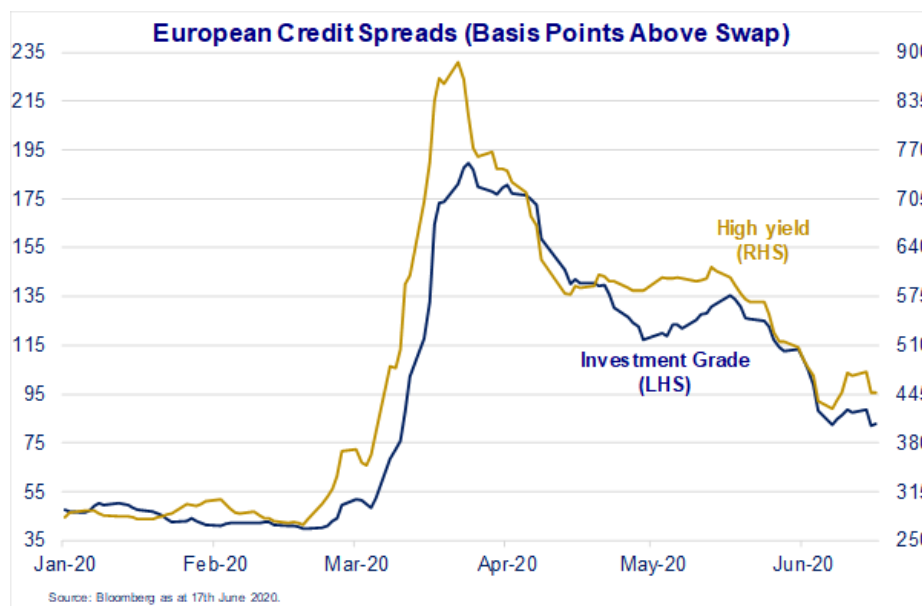


## • CREDIT MARKETS

- Regional credit indices were moderately lower overnight with spreads widening by small amounts. In the US investment grade space, risk premiums rose +3 points to +147 bpts, which lowered the recovery rate one notch to 83%. There was spread expansions in every sector but no underlying trend in that the increases were led by healthcare (+3.5 points, +129 bpts, 85%), consumer staples (+3 points, +136 bpts, 86%) and industrials (+2 points, +163 bpts, 69%). Conversely, spreads in the high yield space contracted by -1 point to +583 bpts (see chart), which left the recovery rate at 75%. There were risk premium contractions in 7 of the 11 GICS sectors led by energy (-6 points +911 bpts, 91%) which defied lower oil prices, industrials (-6 points, +689 bpts, 50%) and senior financials (-2 points, +402 bpts, 62%), but the widenings were modest and not noteworthy.



- European credit markets were also fairly quiet with spreads in the investment grade universe contracting -1 point to +83 bpts, with increases in 10 of the 11 sub-sectors lead by consumer discretionary (+2 points, +111 bpts, 73%) and consumer staples (+1 point, +68 bpts, 69%). In contrast, spreads in the high yield space contracted -1 point to +467 bpts (see chart), which kept the recovery rate at 72%. Spreads contracted in 7 of the 11 sub-sectors but movements were subdued with the largest being in energy (-4 points, +552 bpts, 72%) and consumer staples (-2 points, +468 bps, 99%).



## THE GLOBAL ECONOMY

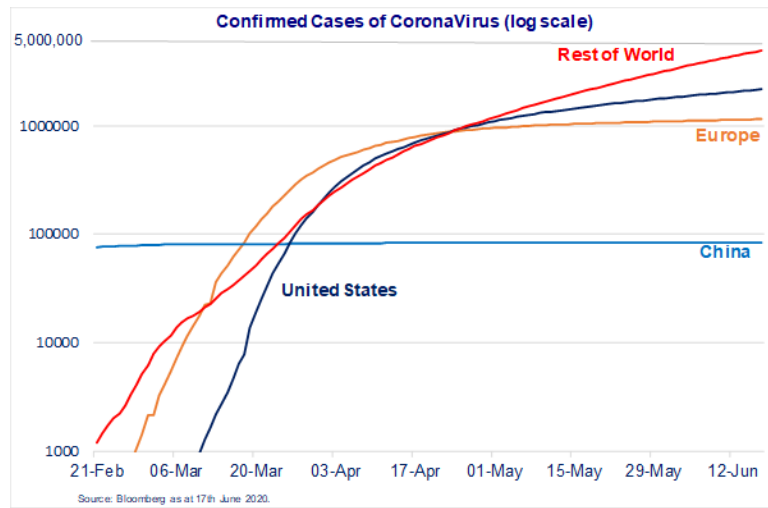
- No major economic data.

## POLICY

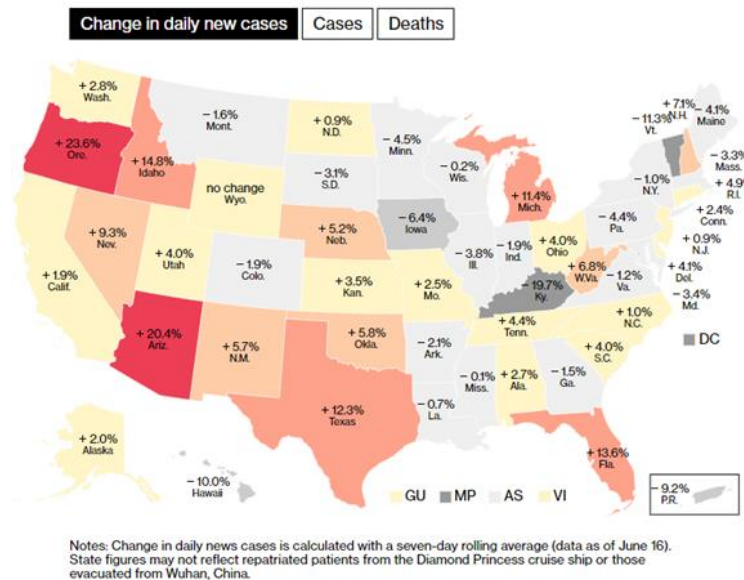
- Nothing on the policy front in terms of new stimulus measures. However, Fed Chair Powell told the House Financial Services Committee that withdrawing fiscal support to businesses and households too quickly would be a concern and that losing unemployment benefits would curb consumer spending. He noted that by doing more now, the economy would be stronger later and that now is not the time to worry about debt. He added that individual corporate bond purchases are the main way the Fed will support that market's functioning over time with ETF purchases taking a back seat, and that the Fed would likely buy fewer bonds as market functioning had improved. Finally he reiterated his recent comments on interest rates (on hold until inflation and unemployment goals are within sight), balance sheet (not an inflationary concern at present), yield curve control (gathering more information but no decision has been made) and negative rates (highly unlikely).

## VIRUS UPDATE

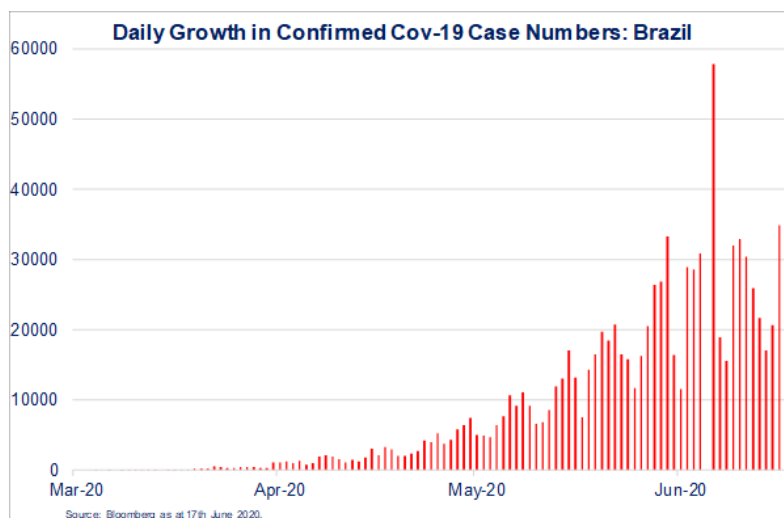
- Although final numbers are not in for another 5.5 hours, the number of global cases of COVID-19 was 8.3 million with another +154.8k cases so far overnight (before Mexico, Pakistan and some US states report their numbers) which means that Sunday was the 20th occasion in the past 22 days where daily increases have topped 100k (and the other two were over 99k!). This means 3 countries have more than 500k cases, 9 countries have more than 200k cases and 17 countries have more than 100k cases. It took 73 days to record 1 million cases, 13 days for the next million, 11 days for the third million, 12 days for the fourth million, ten for the fifth million, 11 for the sixth million and 8 days for the seventh and eighth million and in the past two days a further +318k cases have been recorded. More importantly, the growth rate of daily confirmed cases (+1.7% since Friday) is starting to rise (albeit modestly). Meanwhile, deaths stand at 447.6k, with the US now over 115k (26.2% of global deaths even though they have only 4% of the global population), the UK, Italy and Brazil over 30k, with Spain and France over 25k, and the death rate dropped for a forty second straight day to 5.38%.

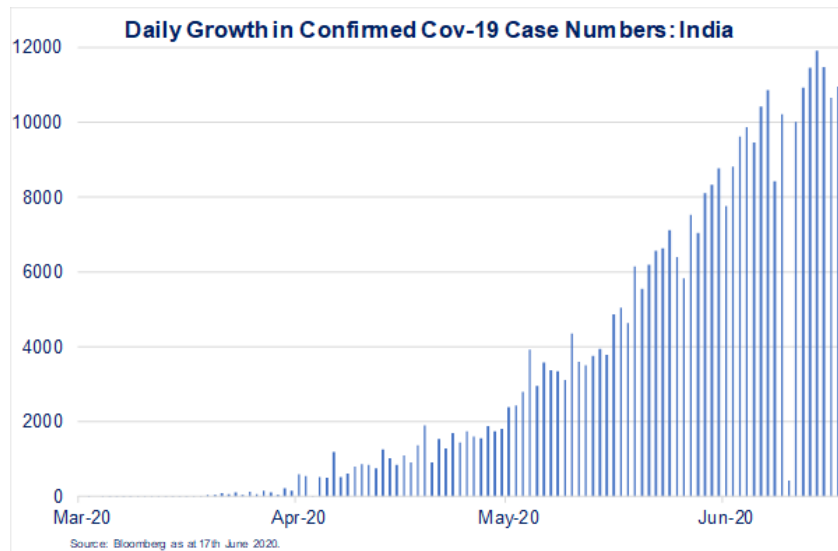


- We break the infections into four groups – the US, Europe, China and ‘others’ and the rest of the world outside the G3 economies now has the most total cases (+116.1k to 4.9 million) and highest daily new cases (and by a considerable margin) followed by the US (+21.7k to 2.16 million) and Europe (+3.4k to 1.15 million). In the US nine states reporting record daily cases overnight including Texas, Florida and Arizona, but states in the North-East are doing better (see chart).



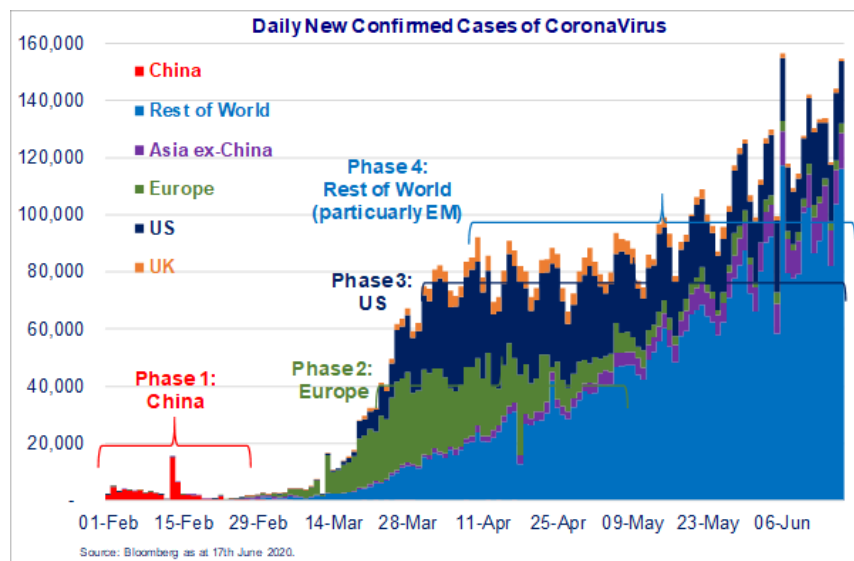
Within the rest of the world, the three concerns here are Brazil (+32.2k, +955.3k, which is the second highest in the world), Russia (+7.8k to 536.5k, third highest) and India (+11.0k to 354.1k, fourth highest – see charts below).





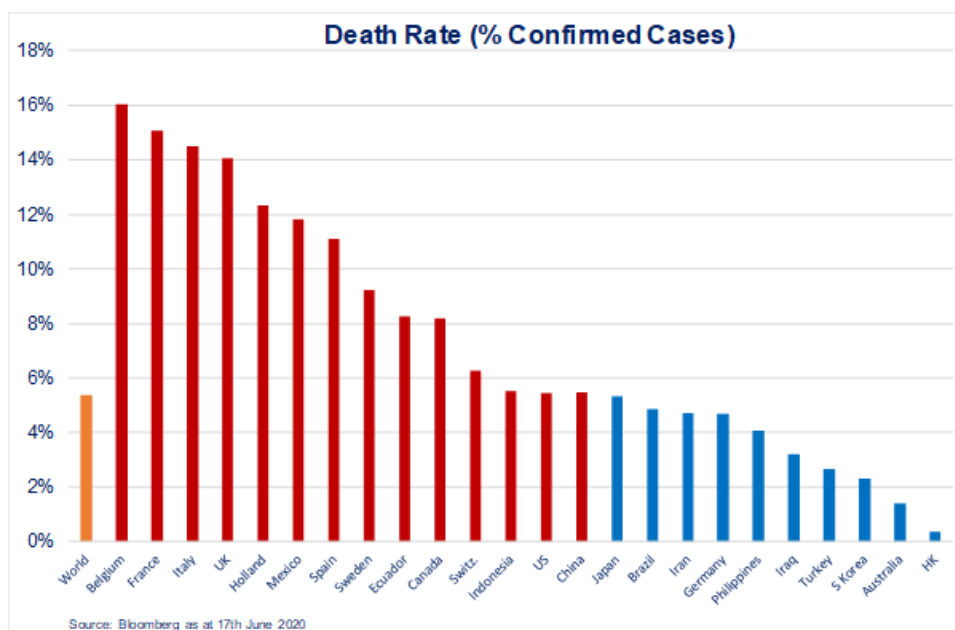
- Among countries, the most cases are in the US (+21.7k (so far) to 2.16 million), Brazil (+32.2k to 955.4k), Russia (+7.8k to 552.5k), India (+11.0k to 354.1k), the United Kingdom (+1.1k to 300.7k), Spain (+0.4k to 244.7k), Peru (+3.7k to +240.9k), Italy (+0.3k to 237.8k), Chile (+36.2k to 220.6k), Iran (+2.6k to 195.1k), France (+0.5k to 194.8k), Germany (+0.4k to 188.6k) and Turkey (+1.4k to 182.7k). Australia confirmed cases rose +23 to 7,370 yesterday which placed us 69th in terms of total infections.

Elsewhere, Singapore recorded +0.2k new cases to 41.2k most of which are linked to foreign workers who are forced to live in crowded dormitories, with the countries having the largest case numbers in South East Asia after overtaking Indonesia (+1.0k to 41.4k) and the Philippines (+0.5k to 27.2k). However, the apparent increase in China case numbers in Beijing has not appeared in China's national tally. Note final numbers for yesterday at not in yet so these numbers can rise.



- Although final numbers are not in until 11am AEST, the global death rate declined for a forty second straight day to 5.38% with the global total to 447.6k. The US (+0.7k so far) has the most deaths at +117.7k, with Brazil (+1.2k to 46.5k), the UK (+0.2k to 42.2k), Italy (+0.04k to 34.4k), France (+0.03k to 29.6k) and Spain (steady at 27.1k) all over +25k. The death rate is highest in European countries where the health systems have collapsed led by Belgium (steady at 16.1%), France (steady at 15.1%), Italy (steady at 14.5%), the UK (+0.1% to 14.1%), the Netherlands (steady at 12.3%), Spain (steady at 11.1%) and Sweden (-0.1% to 9.2%). However, several emerging markets are now on the leader board including Mexico (+0.1% to 11.8%), Ecuador (steady at 8.3%), Indonesia (steady at 5.5%) and Brazil (-0.1% to 4.9%).





Yours sincerely,



**MATT SHERWOOD**  
Head of Investment  
Strategy, Multi Asset



**MICHAEL O'DEA**  
Head of Multi Asset

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**Perpetual Investments** 1800 062 725

**Email** [investments@perpetual.com.au](mailto:investments@perpetual.com.au)

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