

# THOUGHTS ON THE MARKET

25<sup>th</sup> June 2020 - Global markets decline on worsening Cov-19 case numbers and reports of US tariffs on Europe

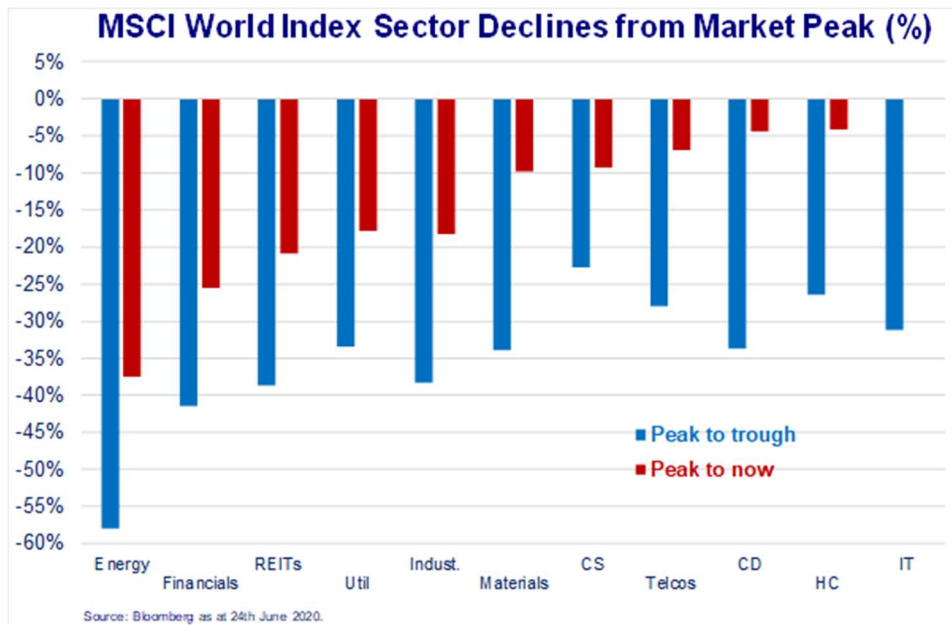
## SUMMARY

- Global risk sentiment is all over the place – yesterday investors were of the view that bad Cov-19 case numbers meant more stimulus, but today another poor set of virus statistics meant that economic re-opening could be slowed or reversed thereby weighing on the strength of the economic and earnings recovery. This change of focus saw global risk markets tumble with losses in all credit and equity markets and sub-sectors, with the negative vibe amplified by reports of the US considering a new wave of tariffs on USD3.1 billion of European goods. Meanwhile, the International Monetary Fund downgraded its outlook for the global economy, projecting a deeper recession in 2020 (-1.9% to -4.9%) and slower recovery in 2021 (-0.4% to 5.4%) than it forecast in April. This completed a trifecta of negative risk factors which saw investor optimism dissipate, but this raises the questions of how long sentiment will remain downbeat and how policy makers will react.
- In other markets, 10-year US Treasuries rallied +4 points with curve flattening, commodity prices were mixed with gold up +0.3% from this time yesterday but oil sank -6% to USD38.07 per barrel and the US dollar found favour against most G10 currencies with depreciations led by the AUD (-0.9% to 68.71), Sterling (-0.3%) and the Euro (-0.3%), but the Yen was unchanged.
- The economic calendar was empty overnight and there were no policy announcements, but Bloomberg caused a storm when it reported that the Trump administration is weighing up new tariffs on USD3.1 billion of exports from France, Germany, Spain and the UK. Meanwhile, an EU spokesman noted that the organisation was set to push forward with a regional digital services tax even if the US sticks with its plans to block a global deal and Fitch downgraded Canada's sovereign rating to AA- as concerns about deteriorating public finances.
- The number of global cases of Cov-19 stands at 9.39 million with another +151k cases so far overnight (before Mexico, Pakistan and some US states report their numbers) which means that Wednesday was the 27th occasion in the past 29 days where daily increases have topped 100k (and the other two were over 99k!). This means 3 countries have more than 600k cases, 10 countries have more than 200k cases and 20 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, a record low 7 days for the ninth million. In the past 36 hours another +391k cases have been confirmed but more importantly, the growth rate of daily confirmed cases (+1.8% since Sunday) is starting to rise. Meanwhile, deaths stand at 481.0k and the global death rate is 5.10%.

## FINANCIAL MARKETS

### EQUITIES

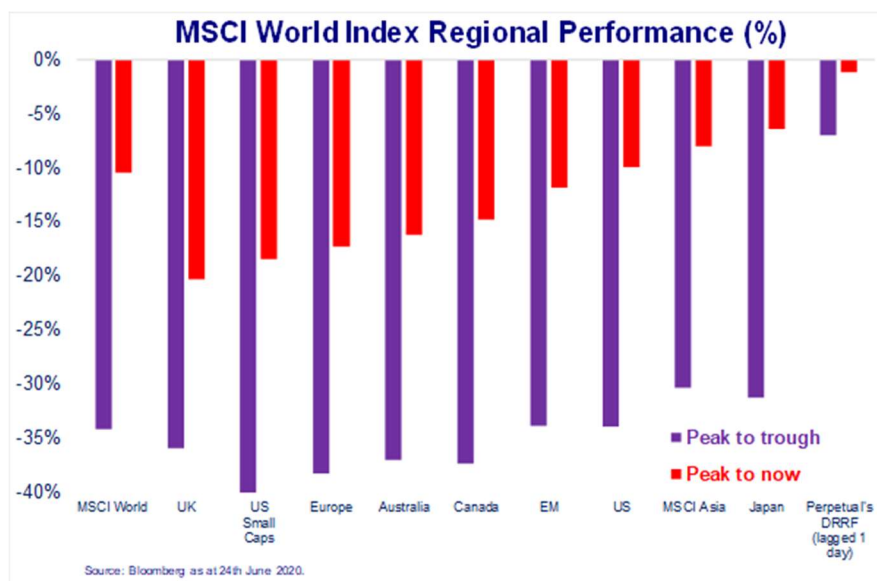
- The MSCI World Index closed -2.5% lower which was its second worst performance in the past 8 weeks. Rising Cov-19 case numbers in the US saw investors finally consider that the second wave of the virus may lead to a delayed recovery which weighed heavily on traditional cyclical sectors such as energy (-4.5%) given the overnight decline in crude prices, financials (-2.8%), industrials (-2.6%), tech (-2.2%) and REITs (-2.1%). These overnight movements saw REITs re-enter bear market territory with industrials (-18.3%) potentially one bad day away from joining the group, whereas IT saw its recovery rate decline back to 100% (see chart).



- Among the regions, losses were led by northern hemisphere markets with Europe squeezed in a classic pincer movement after being hit by the risk of a slower global recovery and potential increases in US tariffs. This combination saw the MSCI Europe Index drop sharply (-3.1%) and record its second largest loss in the past 7 weeks and no regional market was spared from the bloodbath with industrial powerhouses Germany (-3.4%) and Italy (-3.4%) leading the decline, with Spain (-3.3%), the UK (-3.1), France (-2.9%), Sweden (-2.4%) and Switzerland (-2.2%) all recording major declines.

The European price plunge flowed through to the US which recorded its second worst decline in the past 8 weeks as Cov-19 case numbers continued to mount with new daily records for Florida (+5.5k to 109k) and California (+2k to +193k), with the Governor of Texas (+5.2k to 122.9k) declaring there was a “massive outbreak” sweeping his state as intensive care beds rose 97% capacity. This, and the threat of new tariffs on European goods sparked across the board losses led by the Russell 2000 (-3.5%), the Dow Jones (-710 points, -2.7% to -25,446), S&P 500 (-2.6%) and the NASDAQ (-2.2%) which wiped out gains from Monday and Tuesday.

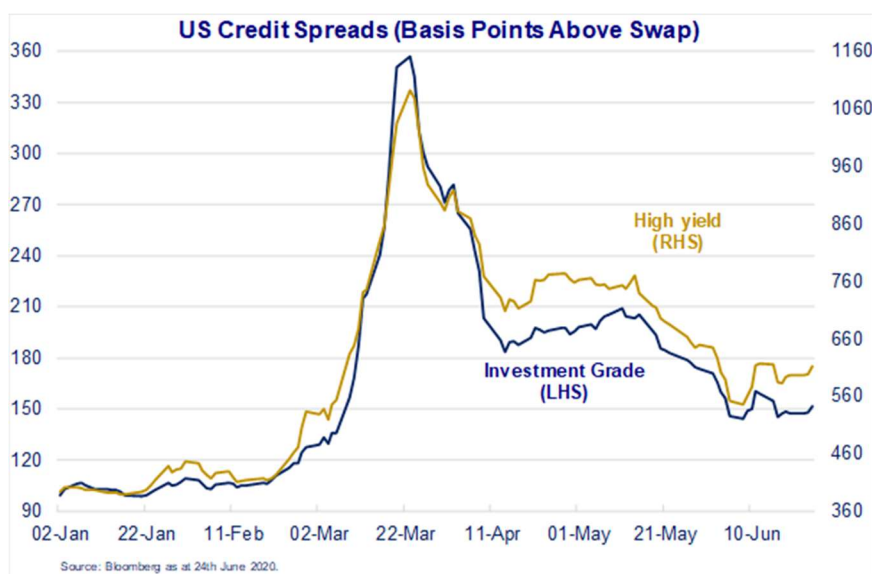
Yesterday, the MSCI Asia Pacific index closed -0.4% lower with gains in Korea (+1.4%), China (+0.4%) and Australia (-0.2%) offset by losses in Japan (-0.1%) and Hong Kong (-0.5%) in a day which was quiet in terms of newsflow. The overnight movements took the UK (with a peak to now decline of -20.3%) back into bear market territory with Europe (-17.3%) potentially one more bad session away from this group, whereas the US (-9.9%) is within inches of entering correction territory (see chart).



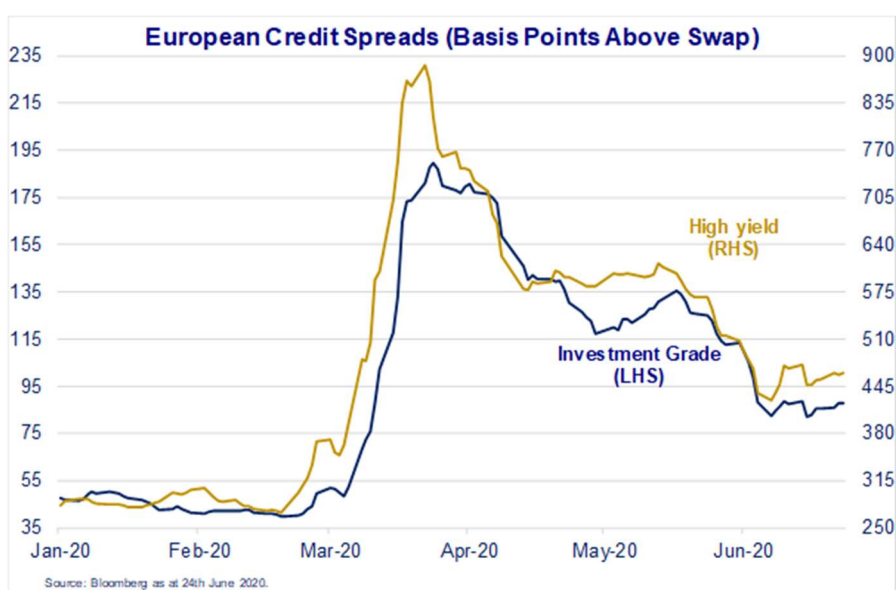
- Futures markets suggest steep losses in Asian market at the bell this morning with declines expected in Hong Kong (-0.9%), Japan (-1.1%) and Australia (-1.5%).

## CREDIT MARKETS

- Regional credit indices declined for a third consecutive day although once again the sell-off was not overly large. Spreads in the US investment grade space increased +4 points to +151 bpts (7-day high), which lowered the recovery rate two notches to 81%. Risk premiums rose in all sub-sectors and were led higher by the traditional cyclical sectors including energy (+6 points, +208 bpts, 87%) given the lower crude price and industrials (+5 points, +167 bpts, 68%). In the high yield space spreads widened by +15 points (2-week high) to +612 bpts (see chart), which lowered the recovery rate to 70%. Across the board spread increases were evident, and 10 of the 11 sub-sectors recorded double-digit rises (again) led by the cyclical sub-sectors including industrials (+26 points, +741 bpts, 42%), subordinated financials (+17 points, +657 bpts, 53%) and energy (+17 points, +938 bpts, 89%).



- European credit markets were more subdued with spreads in the investment grade universe up +0.1 of a point to +82 bps, which kept the recovery rate at 68%. In fact spreads declined in 8 of the 11 sub-sectors led by healthcare (-1 point, +47 bpts, 77%), consumer staples (-1 point, +71 bpts, 67%) and tech (-1 point, +47 bpts, 63%) but this was offset by a notable increase in risk premiums for subordinated financials (+7 points +183 bpts, 66%). In the high yield space, spreads increased +2 points, to +463 bpts (see chart) which lowered the recovery rate to 69%. Eight of the 11 sub-sectors recorded higher risk premiums led by healthcare (+7 points, +318 bpts, 70%), subordinated financials (+4 points, +494 bpts, 66%) and materials (+4 points, +399 bpts, 72%).



## THE GLOBAL ECONOMY

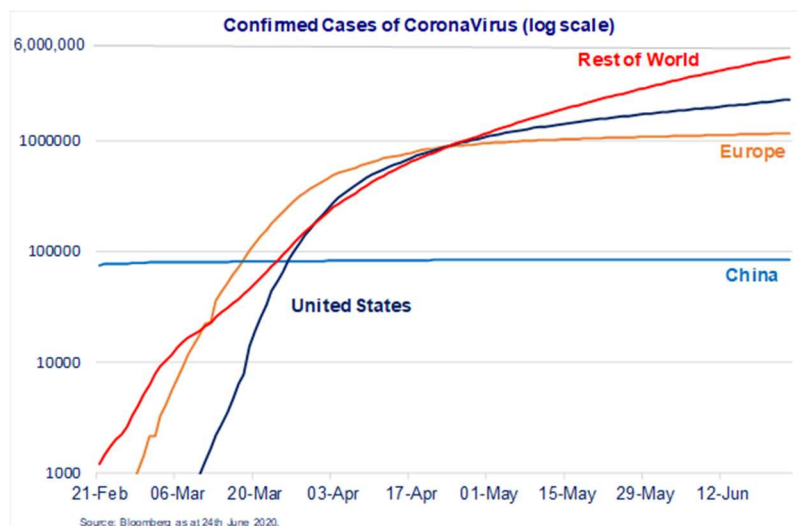
- There were no major economic data releases overnight.

## POLICY

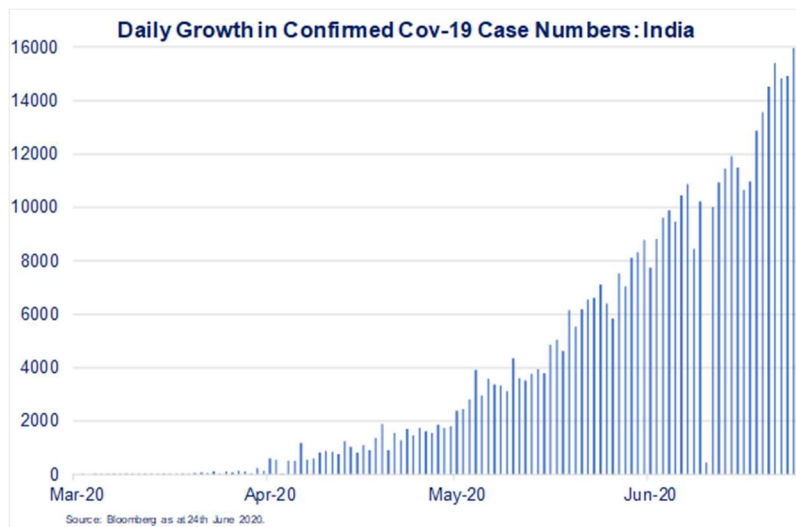
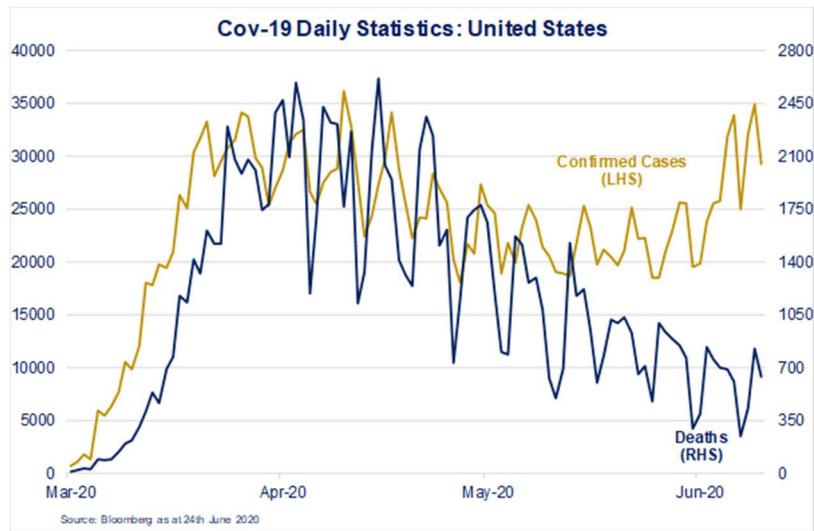
- There were no major policy announcements overnight. However, Bloomberg reported that the Trump administration is weighing up new tariffs on USD3.1 billion of exports from France, Germany, Spain and the UK. Affected products include olives, beer, gin and trucks, while existing levies on products including aircrafts, cheese and yogurt could be increased. These tariffs are part of a long-running dispute between the US and EU over aircraft subsidies. Meanwhile, Politico cited comments from European Commission Executive Vice President Vestager that the European Union will push forward with a regional digital services tax even if the US sticks with its plans to block a global deal.
- Ratings agency Fitch downgraded Canada to AA+ from AAA citing the continued deterioration of public finances from the pandemic which is expected to see the country's government debt increase to 115.1% of GDP in 2020, up from 88.3% last year.

## VIRUS UPDATE

- Although final numbers are not in for another 5.5 hours, the number of global cases of Cov-19 was 9.39 million with another +151k cases so far overnight (before Mexico, Pakistan and some US states report their numbers) which means that Wednesday was the 27th occasion in the past 29 days where daily increases have topped 100k (and the other two were over 99k!). This means 3 countries have more than 600k cases, 10 countries have more than 200k cases and 20 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, a record low 7 days for the ninth million. In the past 36 hours another +391k cases have been confirmed but more importantly, the growth rate of daily confirmed cases (+1.8% since Sunday) is starting to rise. Meanwhile, deaths stand at 481.0k, with the US now over 120k (25.4% of global deaths even though they have only 4% of the global population), Brazil (53.8k), the UK (43.7k) and Italy (34.6k) and over 30k, with France (29.7k) and Spain (28.3k) over 25k, and the death rate dropped for a forty ninth straight day to 5.10%.

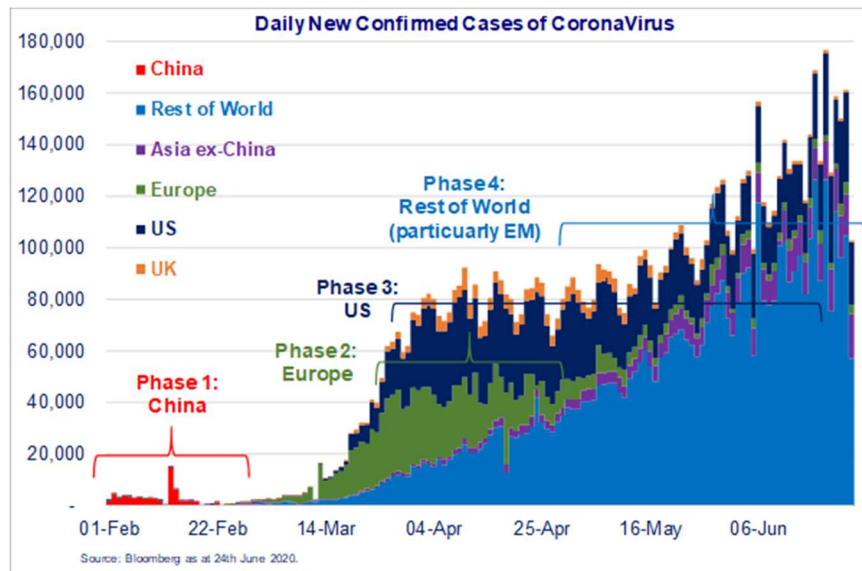


- We break the infections into four groups – the US, Europe, China and ‘others’ and the rest of the world outside the G3 economies now has the most total cases (+100.1k to 5.76 million) and highest daily new cases (and by a considerable margin) followed by the US (+29.3k to 2.38 million) and Europe (+3.6k to 1.17 million - see chart). The issue for the US is that they never flattened their curve which means economic opening has not been associated with lower case numbers (see chart). Within the rest of the world, the three concerns here are Brazil (+42.7k to 1.19 million, which is the second highest in the world), Russia (+7.2k to 606.4k, third highest) and India (+16.0k (record high) to 456.2k, fourth highest – see charts below).

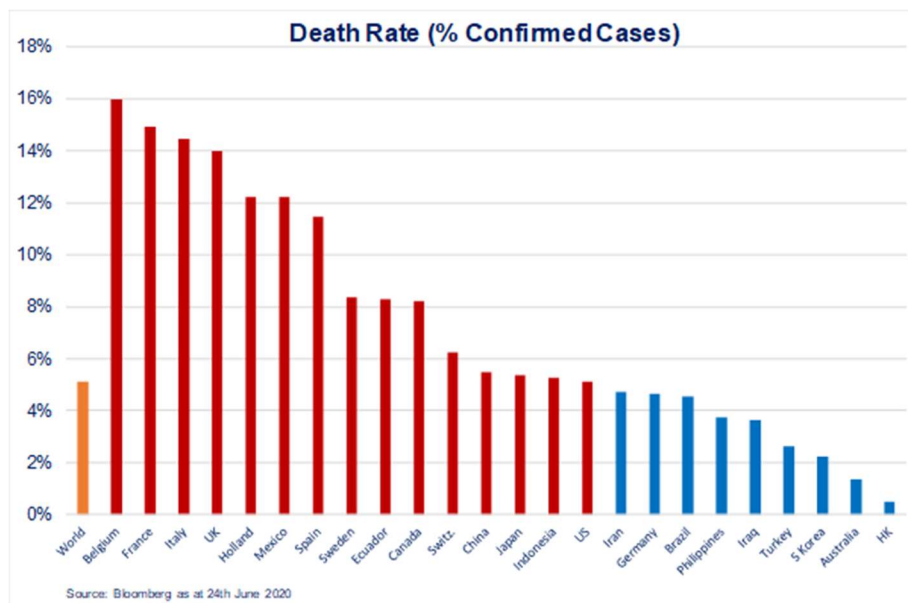


- Among countries, the most cases are in the US (+29.3k (so far) to 2.38 million), Brazil (+42.7k to 1.19 million), Russia (+7.2k to 606.0k), India (+16.0k (record high) to 456.2k), the United Kingdom (+0.7k to 308.3k), Peru (+3.9k to +264.7k), Chile (+3.6k to 254.4k), Spain (+0.3k to 247.1k), Italy (+0.6k (4-week high) to 239.4k), Iran (+2.5k to 212.5k), France (+0.1k to 197.9k), Germany (+0.4k to 192.9k) and Turkey (+1.5k to 191.7k). Australia confirmed cases rose +29 to 7,521 yesterday which placed us 74th in terms of total infections.
- Elsewhere, Singapore recorded +0.2k new cases to 42.6k 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, but Indonesia (+1.1k to 49.0k) is now on the rise and has the most cases in the region, and the Philippines (+0.5k to 32.3k) is also on an upward trend.





- Although final numbers are not in until 1pm AEST, the global death rate declined for a forty eighth straight day to 5.12% with the global total to 481.0k after another 4.1k deaths overnight. The US (+0.7k so far) has the most deaths at +121.9k, with Brazil (-1.2k to 53.8k), the UK (+0.2k to 43.2k), Italy (+0k to 34.6k), France (+0.01k to 29.7k) and Spain (+2 to 28.3k) all over +25k. The death rate is highest in European countries where the health systems have collapsed led by Belgium (steady at 16.0%), France (steady at 14.9%), Italy (steady at 14.5%), the UK (steady at 14.0%), the Netherlands (-0.1% to 12.2%), Spain (steady at 11.5%) and Sweden (-0.1% to 8.4%). However, several emerging markets are now on the leader board including Mexico (steady at 12.2%), Ecuador (steady at 8.3%), Indonesia (steady at 5.3%) and Brazil (-0.1% to 4.5%).



Yours sincerely,



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