MARKET PERFORMANCE AND COMMENTARY – OCTOBER 2020

MARKET PERFORMANCE

Index	Index Level/ Price	1 Month %	3 Month %	1 Year %
Global Equities				
MSCI Emerging Markets	651.21	1.5	2.0	10.8
S&P 500 (US)	3269.96	-2.8	0.0	7.7
Nikkei 225 (Japan)	22977.13	-0.9	5.8	0.2
FTSE 100 (UK)	5577.27	-4.9	-5.4	-23.1
DAX (Germany)	11556.48	-9.4	-6.1	-10.2
CAC 40 (France)	4594.24	-4.4	-4.0	-19.8
Trans-Tasman Equities				
S&P/NZX 50	12084.47	2.9	3.0	12.0
S&P/ASX 300	65275.10	1.9	1.2	-7.9
Bonds				
S&P/NZX NZ Govt Stock	1986.95	-0.2	1.4	6.3
S&P/NZX A Grade Corporate	6042.52	0.1	1.4	5.8
BBgBarc Global Aggregate Hdg NZD	427.64	0.0	-0.3	4.1
FTSE WGBI Hdg NZD	3735.48	-0.1	-0.3	4.7
Oil				
West Texas Intermediate Crude	35.79	-11.0	-11.1	-33.9
Brent Crude	36.90	-9.9	-13.8	-38.0
NZD Foreign Exchange				
AUD	0.9411	2.0	1.3	1.1
EUR	0.5674	0.7	0.7	-1.3
GBP	0.5111	0.0	0.7	3.1
JPY	69.0905	-1.0	-1.9	-0.3
CNY	4.4256	-1.3	-4.8	-2.0
USD	0.6609	0.0	-0.8	3.1

Source: Nikko

Executive summary:

- Another wave of COVID spreads through US and Europe
- Interest rates are trending higher globally
- Biden victory in the US Election has driven investor sentiment upwards
- Encouraging news surrounding a vaccine emerges

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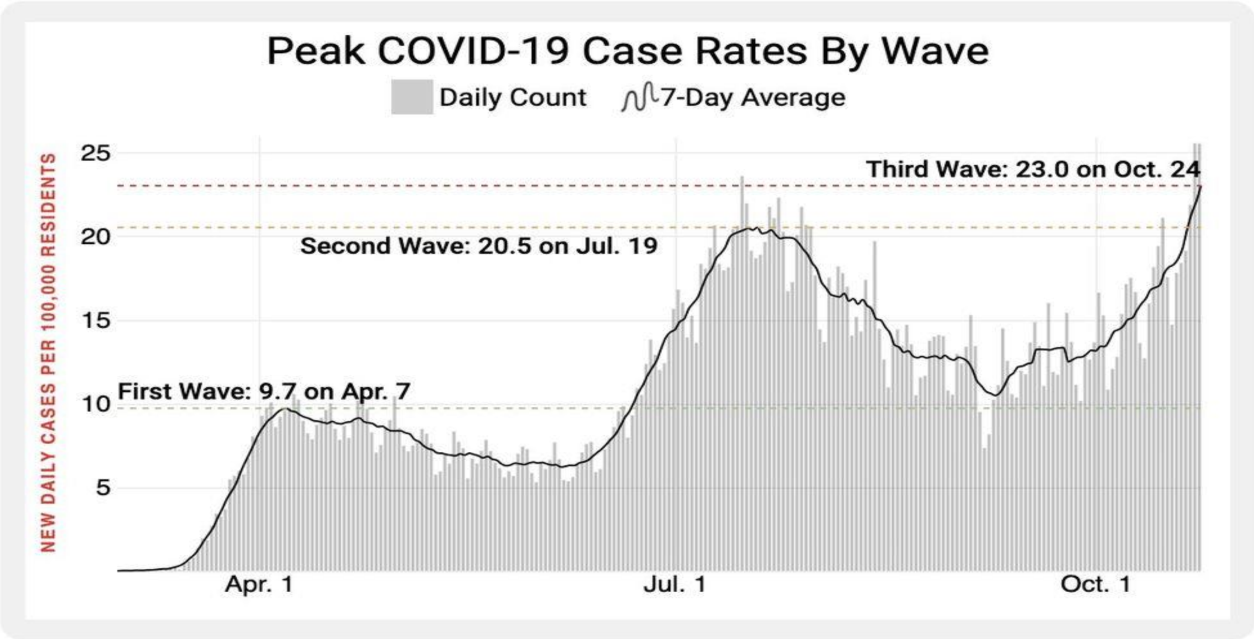
ECONOMIC COMMENTARY

COVID

The second wave hit Europe and third wave covered the US and India. Italy (partially) and Greece are the most recent countries announced to return to lockdown. Lockdowns could provoke protests across Europe.

The day following the US election was the first day the US recorded over 100,000 new COVID-19 cases in a single day, and that has been the case each day since. With mass protests and celebrations as a consequence of the election, cases are expected to skyrocket even further as there were little to no measures to prevent the spread of the virus at these gatherings.



Source: Time.com

Extreme measures were conditioned by skyrocketing hospitalisation numbers in Europe. Intensive care capacity would be at risk in 15 of Italy's 20 regions within a few weeks unless implementation of new lockdown measures were put in place immediately. In France, 63% of intensive care beds are taken up by COVID patients. On a positive note, death rates have dropped by 18% as treatments improved.

Eleven vaccines have reached Phase III of trials out of 150-plus in development across the world. However, most experts think that the first vaccine won't be available until the middle of 2021 at the earliest. It is thought that 60-70% of the global population need to be immune to the virus in order to gain herd immunity. Will this be when we see a full recovery of economies and the return of free flowing international travel?

Pfizer's first trial showed a 90% success rate for a vaccine, beating market expectations and driving up equity markets. This is an encouraging first step for our vaccinated future, but there still remains the challenge of distribution to all corners of the globe.

A "double-dip", or perhaps just sustained recession is looking likely across many EU countries as lockdowns are put in place as a more deadly second wave of the virus accelerates. The US now has a death rate matching Bolivia, Mexico and the UK. It is still grim in France, Russia, the UK, Spain and central and southern Italy with very serious stress on their hospital systems with death rates starting to rise again.

NZ Election

As many predicted, Labour won the 2020 election with overwhelming number of seats that allowed to govern alone. However, Labour and Greens made a "cooperation agreement" giving two ministerial portfolios to Greens outside the Cabinet. It seems to be a strategic movement to neutralize the Greens from joining a possible National-ACT opposition block.

Geopolitical Tension

The US election has been a roller coaster and is a lesson in not claiming victory too early. Biden is President-elect and it remains to be seen how Trump will concede, if at all. Inauguration day is the 20th January which is a long time for Trump to have an almost consequence-free period. The markets priced in a Biden victory, but it is uncertain how a delay in the confirmation of his presidency could impact volatility.

A Biden presidency is expected to have a stabilising impact on America's foreign relations. By reinstating previously held commitments to institutions, such as the UN Human Rights Council, WHO and the Paris Accord, Biden will bring about a return to Obama principles of international cooperation. An institutionalist by nature, Biden will support small and progressive steps, which will be a welcome change of cadence from the volatile norm we have become accustomed to over the last 4 years.

Other than reinstating important multi-lateral agreements, Biden's immediate focus will be on the current health and economic crises within the US. Broader foreign policy will be a slow burning and incremental exercise amid his domestic focus. All this points to more stable global financial markets than if Trump was in office.

With bipartisan support across the aisle, we do not believe Biden will appease China, but he will take a more structured approach to dealing with their growing influence.

Iran will be on the US agenda to shore up the relationship and look at reinstating previously imposed nuclear restrictions. Turkey will be a challenge for Biden due to their close relationship with Russia. More broadly, we expect to see more tension between the US and countries with more authoritarian regimes, including Iran, Turkey, Jordan and Saudi Arabia, with a likely end to US support for the Yemen War. The current anti-nuclear arms pact with Russia expires in February 2021; re-signing this will be a top priority.

Brexit negotiations continue as pressure mounts on PM Johnson. A hard Brexit seems likely as many large differences remain to overcome. It remains to be seen whether the nationwide lockdown will work in Johnson's favour, but it could be make or break for his tenure in Downing Street.

Markets

QE easing measures are increasing but the foundation of QE is beginning to crack, and the effects of monetary policy are becoming less and less. The RBA recently announced the cutting of the cash rate to 0.1% and a bond buying program of $100bn AUD to flatten the yield curve over the 5-10 year term. Designed to put downward pressure on the AUD and make exports more competitive, the opposite has happened as the fiscal stimulus promises in the US have weakened the US dollar. The Biden victory and news about the Pfizer and Moderna vaccines has driven investor sentiment and equities through previous highs. On the back of this however is the fact that interest rates are trending higher, meaning valuations will be lower and we could see a correction in equity markets at some stage next year.

Markets have improved post-election with investor sentiment increasing with a Biden win and the likelihood of the Republicans regaining the Senate with run-off wins in Georgia. Demand has flowed form tech stocks into the broader market creating fresh opportunities for managers. The market has moved from a risk off environment to risk on, resulting in the NZD appreciating across most major currencies in the week following the election. However, the Central Banks should continue to restrain any ongoing rise in interest rates to a modest level.

In New Zealand, the market is delicately poised. Potential COVID lockdowns could still cause the Reserve Bank to introduce negative interest rates though the likelihood of that being needed has reduced. Hopefully a Trans-Tasman travel bubble will open up to support our economy even more.