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Market Watch

Monthly Commentary August 2021

Monthly Commentary - August 202

Countries and markets around the world continued to react to the resurgence of COVID-19's Delta variant. At home, Australia finished the month with 60% of its population under stay-at-home orders reporting record numbers of daily COVID cases. Abroad, COVID management created run on effects in global trade and supply chains that caused manufacturing measures to compress. Inflation continues to be a growing concern in Europe and the US as central banks signal monetary policy updates might be coming soon. China continues its regulatory crackdown aimed at tackling "foreign-related rule of law".

Developments in the global economy

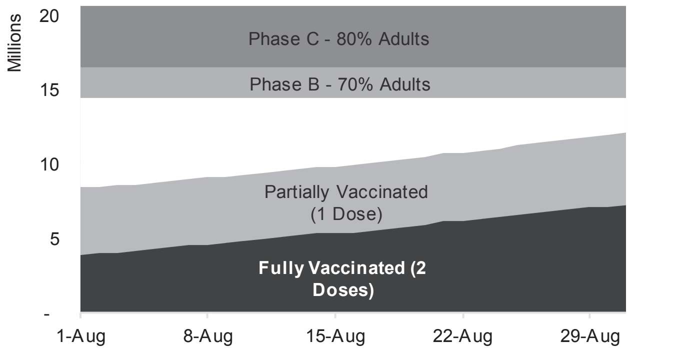
COVID-19 Update

Australia's Extend and Snap – Works every time?

In Australia, August was a month of snaps and extensions as the country continued to respond to the growing threat of the Delta variant.

At the end of July, the Prime Minister's office mapped out a four-phase reopening, contingent on vaccination rates rather than case number milestones. Currently in Phase A, Phase B will mean 70% of the adult population is vaccinated and certain restriction exemptions will be applied to those fully vaccinated. Phase C at 80% will see international borders open. To support this, the Federal government successfully secured an additional million Pfizer doses from Poland that began arriving from 16 August. A deal was signed with Singapore on 31 August that secured an additional half million Pfizer doses. The Moderna vaccine also received approval from Australia's Therapeutic Goods Administration on 9 August with first shipments set to arrive end of September. As at 31 August, 35% of Australia's over-16 population was fully vaccinated. The below chart illustrates Australia's August vaccination rollout, as we begin to make solid headway towards 70% vaccinated.

Chart 1: Australia's August Vaccination Rollout



Source: Australian Department of Health

However, despite increased supply and increasing vaccination rates, the Federal government's re-opening plan was greeted with varying degrees of acceptance across state policies.

In NSW, Premier Gladys Berejiklian was the first to incorporate this into state policy as outbreak management continued. At the end of August, those living in the Greater Sydney area had 66 consecutive days in lockdown, where broader NSW had at least 17 consecutive days in lockdown. NSW case numbers had exponential growth this month, recording 207 on the 1st and 1,164 on the 31st. This increase prompted the roll out of additional restrictions in Sydney, as well as stay-at-home orders imposed on all of NSW. The Premier controversially announced on 26 August (the first day an Australian state recorded more than 1,000 daily cases) that there would be some restriction easing as NSW had reached 6 million vaccinations.

From 13 September, those who are fully vaccinated and living outside local government areas (LGAs) of concern will be able to gather outdoors in public spaces in groups of 5. Those fully vaccinated in LGAs of concern will be able to have 1 hour of outdoor recreation a day on top of their existing 1 hour of exercise. Though signally aligned to the national re-opening strategy by managing COVID based on vaccination numbers rather than cases, other states have not been supportive of this easing.

Victoria also experienced exponential case number growth over the month. They recorded 2 cases on the 1st, day of the month, however finishing the month at 76. As a result, Victorians entered their sixth lockdown of the pandemic on 5 August. Initially scheduled for a seven-day lockdown, they have not re-emerged. Premier Daniel Andrews, despite being a strong critique of NSW's handling of the outbreak and subsequent easing, is expected to announce on 1 September Victoria's own easing plan where vaccination rates are expected to play a role in restriction rollback.

Queensland had multiple snap lockdowns across the state during the month and was able to successfully reach zero cases. The biggest issue of contention has been border controls, as the state continues to lobby to shift the NSW border checkpoint south and struggles with high inflows of hotel quarantine arrivals.

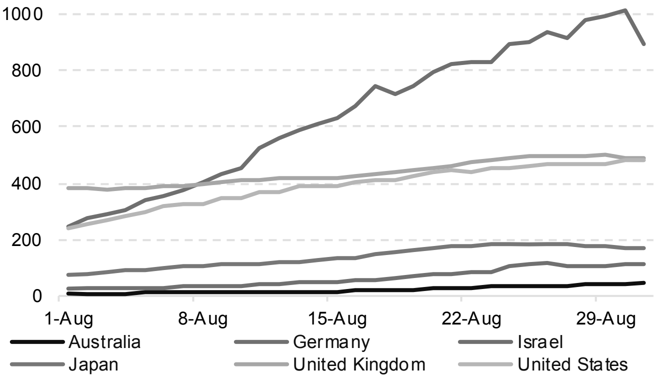
At the beginning of August, multiple joint funding packages between the federal and state governments were announced. For Victorians, a support facility of $400m was jointly raised to help support small and medium sized enterprises. For South Australians, an additional Business Support Grant of $40m was raised to assist businesses impacted from trailing restrictions – South Australia has not been locked down since July.

For Queenslanders, a 50/50 Federal funding agreement was reached to increase Business Support Grants from $260m to $600m, where the Queensland government had fully funded the first $260m. This will complement the state government's existing $48m tourism and hospitality sector COVID-19 support package. For the ACT, multiple state government fully funded support packages were announced to support businesses in lockdown. For NSW, no new funding packages however further announcements were made this month primarily centred around additional comparison periods for some existing measures.

Global COVID – Same, Same but Different

Like in Australia, Delta cases continued to grow. China used snap venue closures as its main mechanism of containment, whereas most other countries (such as UK and US) continued business as usual as they rely upon their high vaccination rates to keep hospitalization levels down. Notably, Israel has posed an interesting case whereby despite being the vaccination poster child is now seeing a huge Delta resurgence. However, comparatively they have been able to keep hospitalisations low therefore still boosting the vaccine narrative. Israel, among other countries, is now considering a third booster shot to be administered to those fully vaccinated.

Chart 2: New COVID Cases per Million People



Source: Our World in Data

Afghanistan

Notably during August, the Taliban took Afghanistan's capital, Kabul, after US and NATO troops fully withdrew from the area in May this year. By 10 August, it was estimated that the Taliban had taken control of 65% of the country, taking the capital city 5 days later declaring the "war is over". Though it appears 2021's Taliban is more progressive (or at least more public relations savvy), there is still large scepticism over how the group will govern the country, especially concerning women's rights. An emergency G7 summit was held, where despite requests from European countries, US President Biden held the original evacuation deadline of 31 August, meaning that the Taliban would be taking control of the airport come September. The evacuation effort was paused on August 26 as an ISIS-K inspired suicide bomber, killed over 189 people at the airport, including 12 US marines. As at 30 August, more than 114,000 people have been evacuated since the Taliban took Kabul in the middle of the month.

Australia – 2020 Déjà Vu

August consensus for the Australian economy was bittersweet. While June quarter reporting season uplifted spirits as positive economic signals were abundant, fear of the current state of the economy soured this. GDP for the June quarter increased by 0.7% quarter-on-quarter. Though the mildest of expansions in the last 12 months, it has been somewhat reassuring that a recession is no longer a guaranteed branding for Australia, ahead of strong expectations for a contraction in the September quarter. Public spending also increased in the June quarter by 2.5% as the government splurged on public infrastructure to boost growth.

Also keeping his head up amidst 60% of Australians being in lockdown, is the Reserve Bank of Australia's (RBA's) Governor Philip Lowe. Surprising economists, Lowe announced in the August policy meeting that the RBA would stay the course in reducing its rate of bond purchases from $5bn to $4bn per week – a move that was determined in more optimistic times (that is, July this year when the Sydney lockdown had a 2-week expiration). Lowe maintained the RBA still held its central case scenario that the Australian economy will rebound strongly from late this year and into next.

Australia's manufacturing Purchasing Manager's Index (PMI) reduced this month to 52, driven by factory activity slowing to its lowest levels since July 2020 because of the COVID lockdowns and supply chain constraints. Manufacturing output and new orders declined for the first time in 14 months as mobility restrictions were extended across the country. Australia's services PMI marginally decreased this month by 1.3 points to 42.9. However, though this is only a marginal month-on-month decrease it still showcases July's deterioration when it fell by 12.6 points compared to June. These consecutive months of contraction represent the toll that lockdown has placed on the services industry in Australia.

While Australia's unemployment rate fell in July, it has been attributed to the decline in the participation rate as people from certain industries give up looking for work during lockdown. The real brunt in July's labour figures was seen at the hours worked level as the number of people working zero hours due to economic reasons increased to 182k, the highest level since September last year.

In property, the Australian Bureau of Statistics (ABS) released home loan data for July that indicated a 0.4% fall in the value of new loans being issued. This is the second straight month of decline amidst the pandemic. Property platform and research house Doman released August auction and vacancy data. In Sydney, 46.5% of residential auctions were sold prior, almost double the decade average, hitting an all-time high since 1995, attributed to stay-at-home orders. Historically, lockdowns have led to higher vacancy rates, however according to Domain current lockdowns are challenging this trend as Sydney rates remain steady as does the national average. Melbourne's on the other hand increased by 0.1% this month, still sitting lower than August 2020 rates.

July's consumer data was also released this month and surprise, surprise lockdown was the headline. Retail sales declined 2.7% in July which is the largest drop in retail trade this year as cafes and restaurants, clothing and department stores saw the biggest declines, partially offset by trade increases in food retailing.

The Westpac-Melbourne Institute Consumer Sentiment Index fell 4.4% in August to its lowest point in the year. However, this metric remains above last year's lowest readings, illustrating that the vaccination rollout has been a key source to support consumer confidence.

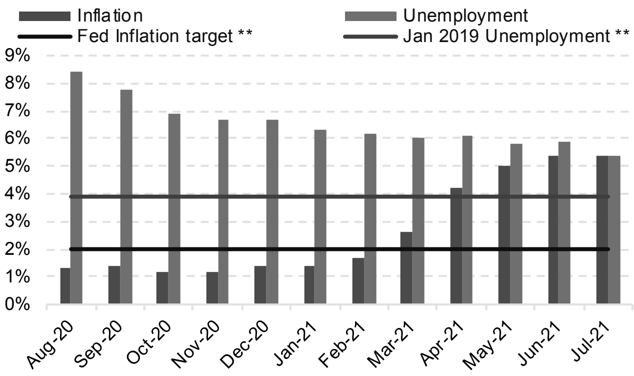
United States – Way Down in Jackson…

In the US, the Jackson Hole Economic Policy Symposium provided the main catalyst for economic commentary this month. United States Federal Reserve (the Fed) Chairman Jerome Powell announced that given positive progress made on some metrics, it is time to stop talking about talking about tapering and start talking about tapering. He expressed his view that if the economy continued to evolve as anticipated, then reducing the pace of federal asset purchases could start soon.

However, it's been warned that investors don't interpret this as a signal that the Fed will be actioning an interest rate uplift anytime soon. Instead, as reiterated over the past 18 months the Fed will be staying the course in federal fund rates until maximum employment is reached, and inflation is steady at 2%, if not exceeding this number.

The US published several July metrics this month. The unemployment rate continues to shrink to now 5.4% in July, however, it still remains above pre-COVID levels. While July's inflation rate remained unchanged, it still tracked at June's 13 year high of 5.4%. Uplifts in food products, new cars and shelter prices offset declines in energy, second-hand cars, apparel, transport, and medical care services prices. The US still has a long way to go to satisfy conditions for the Fed to increase interest rates.

Chart 3: US Inflation and Employment July Data



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Source: Trading Economics

Despite the slight shrinkage in unemployment, it is clear that the American consumer is sceptical for the future as the notion that COVID is an issue of the past begins to wane. The University of Michigan's consumer sentiment reading captured a harsh, emotional response to high inflation concerns and worry over COVID's resurgence. It reported consumer sentiment at 70.3 for August – a staggering 10.9 point reduction from the previous month and the lowest reading in the last 12 months.

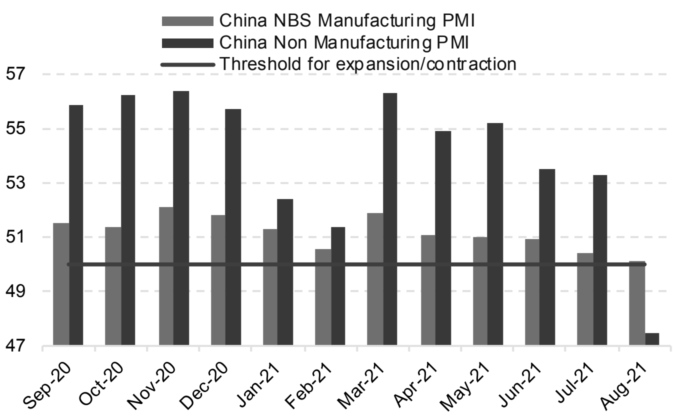
The US Bureau of Economic Analysis released July's income statistics this month. Personal income increased by 1.1% in July, disposable personal income increased by 1.1% and personal consumption expenditures increased by 0.3%. This mismatch between income and spending growth has been attributed to delta variant resurgence as Americans continue to preference saving overspending as the personal savings rate also rose by 0.8% in July to 9.6%.

Asia – "Containing" COVID

Uncertainty pervades global supply chains as China took steps to contain COVID during the month through containership port shutdowns and factory halts.

China's manufacturing PMI and its non-manufacturing PMI both fell more than expected this quarter. Its manufacturing PMI slipped to 50.1, treading finely above the contraction threshold of 50 as factory activity slowed due to Delta outbreak management. This slip was met with a plummet of the non-manufacturing PMI to 47.5 from 53.3 the month before. A strong contraction signal, well below the threshold of 50, this has been attributed also to COVID management as new order rates, new export order rates and employment rates all shrunk more than expected.

Chart 4: China PMI July Data



Source: Trading Economics/National Bureau of Statistics

China's policies have raised fresh concerns about the impact of COVID management on global trade, as supply chains become bottlenecked. Ningbo-Zhoushan, the world's third busiest port, shutdown for two weeks this month in response to the detection of a single COVID case. Immediate follow-on effects of this include further disruption to major trade routes as well as container shortages. However, analysts predict the fall out is not over and believe the shutdown will impact future global supply chains, notably delaying Christmas orders.

The Chinese government maintains its regulatory tightening, unveiling a 5-year plan aimed to tackle monopolies and "foreign-related rule of law". August's flavour of the month has been new data protection laws that give comprehensive rules for data collection and punishments for company non-compliance. Beijing continued to enforce private tutoring changes this month, with the fall out expected to be captured in August's unemployment figures, as it was in July's, where the education sector's unemployment rate was nearly double the national aggregate unemployment number.

Japan kicked off the Paralympics this month, despite the surge in COVID cases causing another extension to their state of emergency into September. August's consumer confidence index fell this month by 0.8 points, driven by deterioration in underlying scorecards for overall livelihood, income growth, employment perceptions and willingness to buy durable goods. Japan has had a difficult month in their vaccination rollout – two men in their 30s died after receiving their second doses, as a batch of 1.63 million Moderna doses were found to be contaminated.

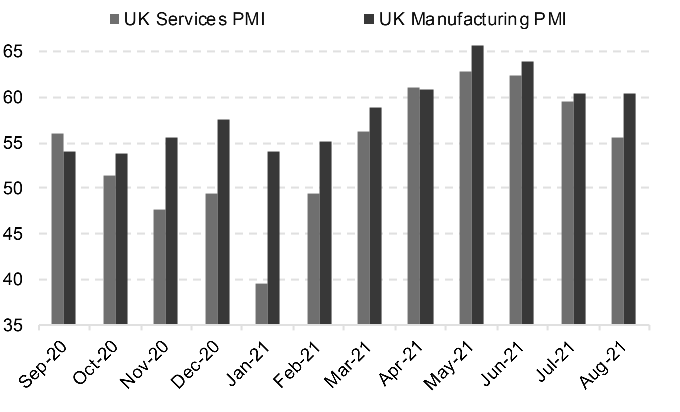
The strength of India's economy becomes a question of reporting interpretation. Though reporting a record GDP growth rate of 20.1% year-on-year for the June quarter, this is propped up by the same quarter last year suffering a 24.4% GDP contraction. The Indian government has attributed this V-shaped recovery to manufacturing and construction growth. In comparison to other developed countries, India is yet to return to pre-COVID levels.

Europe – Inflation having a European Staycation?

For the first time since COVID, European growth in the services sector exceeded that of the manufacturing. This was driven by service tailwind of further re-opening across Europe as well as manufacturing headwind of global supply chain delays. The growing concern of the Delta variant was reflected in this month's business confidence as the index contracted slightly compared to July's 12 month high.

The United Kingdom's recovery momentum dried up this month, with preliminary reports showing a decrease in both services PMI and manufacturing PMI to 55.5 and 60.3, respectively. Reflecting on this data, there's a clear trend of retraction in services as this measurement underperformed the market expectation of 59 points. Driven by COVID re-entering public concern as well as less favourable demand conditions, this number should be taken with a grain of salt as historically UK's PMI has been revised up from preliminary estimates. In manufacturing, the UK was not immune to run on effects from global supply chain issues as shortages of raw/input materials and delivery delays saw a slight shrink in this metric this month.

Chart 5: UK PMI Preliminary August Data



Source: Markit Economics

During August, the UK released inflation figures for July. Inflation fell below market expectations to 2% from June's 2.5% - hitting the Bank of England's target rate. Drags in the cost of consumer discretionary goods were offset by boosts in prices in the second-hand car market. This boost has remained a key driver of inflation in the last 12 months with increased demand from consumers opting to stay away from public transport, as well as global shipping delays and shortages of goods tightening car supply.

However, economists are not convinced that this reduction in inflation is here to stay, citing that this slowdown reflects the jump in prices seen last year in July when Britain was first re-emerging from lockdown, and does not properly capture the full inflationary pressures in the British economy. The Bank of England's August meeting re-affirmed its expectation that they would tighten monetary policy moderately over the next three years.

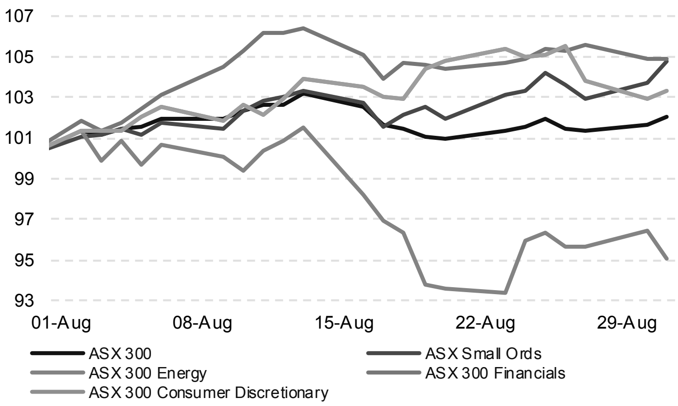
Germany reported their June quarter GDP movements in August, recording a quarter-on-quarter increase of 1.6%. This is an apt recovery from the 2% shrinkage in the March quarter. Driven by economic rebound, high energy prices and global supply chain disruption, German inflation rose to 3.4% this month. These rises were mimicked across Europe, as France's inflation not only exceeded market expectations but reached a three-year high reporting 1.9% in August. This is expected to intensify market concerns over the European Central Bank's (ECB) ultra-loose monetary policy as it stays the course of its "transitory" branding of current inflation rises.

Developments in financial markets

Australian Equity

Australian markets were mixed this month as the ASX300 Accumulation returned +2.61%. Information Technology boomed this month recording +16.19%, spurred on by M&A activity such as Square's $39bn acquisition of homegrown fin-tech Afterpay. COVID and lockdowns seemed to create a catalyst for strong performance in sectors such as consumer staples (+6.79%), healthcare (+6.62%) and telecommunications (5.5%). The Energy and Materials sectors struggled, down (-4.91%) and (-6.92%) respectively, as they reacted to pricing deterioration in commodity markets.

Chart 6: Australian Equity August Performance, rebased to 100



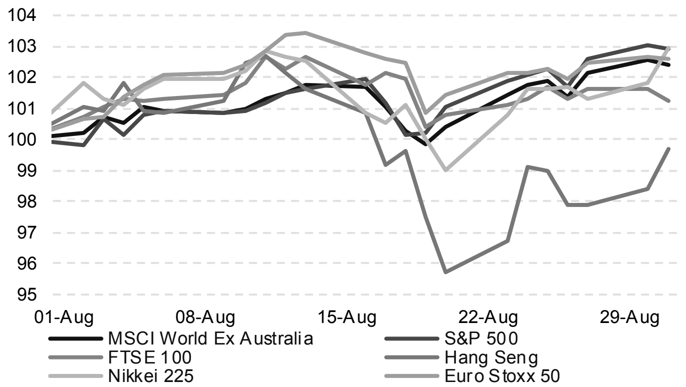
Source: BTIS / Bloomberg

International Equity

Global markets finished showcasing relatively positive investor sentiment. The Shanghai Composite was the frontrunner this month returning +4.3% indicating strength in Mainland China stocks. Conversely, Hong Kong's Hang Seng was one of the few negative performers this month with especially volatile returns of -0.3%, driven by regulatory uncertainty in the technology sector. Japan's Nikkei was mildly volatile throughout the month however still finished positive at a strong +3%.

Indices in the US showed a similar trend to Australia's technology rally as the NASDAQ returned +4.1%, outperforming returns in the Dow Jones +1.5% and the FTSE100 +1.2%. European markets also had positive returns over the month were Euro STOXX was up +2.0% and the German DAX outperformed the French CAC 40 returning +1.9% to France's +1.0% over the month.

Chart 7: International Equity August Performance, rebased to 100



Source: BTIS / Bloomberg

Fixed Interest

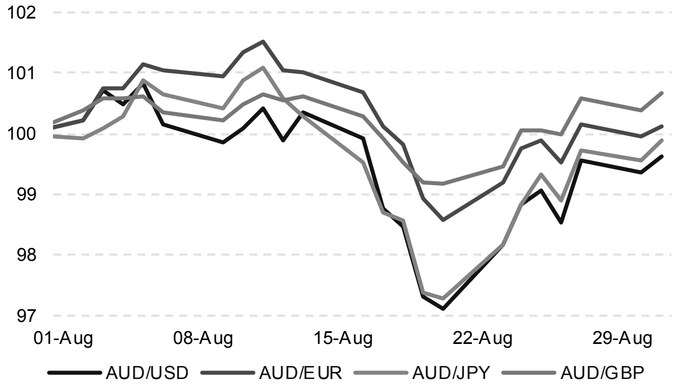
Australia's 10-year bond yield was volatile this month, dipping inline with the timing of NSW's September lockdown extension announcement, however, it was able to make a recovery and finished the month at 1.21%. The US 10-year treasury note was volatile in the opposite direction as it boomed at the start of the month and began to taper off towards the end. Germany's 10-year Bund yield started to recover towards the end of the month, finishing on a high of -0.38% yield. Finishing the highest since July, this is a signal that the ECB may be starting to limit emergency bond-buying in response to surging inflation.

The Bloomberg AusBond Composite (0+Y) index appreciated slightly during the month to return 0.09%. In international fixed income markets, the Barclays Global Aggregate TR Hedged index's returned -0.22% over the month.

Foreign Exchange

The Australian dollar nosedived this month to a 9-month low, as more Delta concern set in. However, despite mid-month deterioration (timed in line with NSW's announcement of lockdown September extension), the Aussie dollar was able to recover and instead report relatively mild / flat losses. European currencies finished positive against the Aussie this month, with AUD/EUR returning +0.1% and AUD/GBP returning +0.7%. AUD/USD was weaker returning -0.38% and AUD/JPY also had a negative monthly return of -0.1%. Overall, a strong recovery for the Aussie dollar against USD and JPY given the lows reached this month.

Chart 8: Foreign Exchange August Performance, rebased to 100



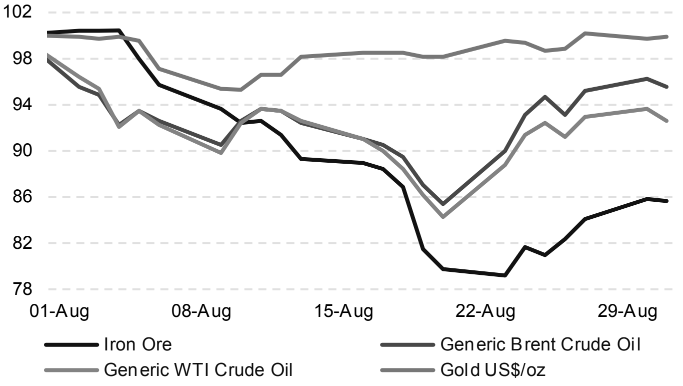
Source: BTIS / Bloomberg

Commodities

Overall, commodity markets shrunk this month. Gold remained the flattest returning -0.03% over the month. Iron Ore diverged from the group as it struggled the most this month. Iron's sudden fall after 12 months of boom is a story of supply and demand. As COVID eases, Brazil has been making a strong return to the market, with analysts estimating that their supply of iron ore has increased by 12% this year. More competition in supply has not been met with more demand as the Chinese economy slows and demand for raw materials softens.

The oils followed relatively similar cadences this month however diverged in the last week, with West Texas Intermediate (WTI) finishing nearly 3% lower than Brent Crude. Russian negotiator to the Organization of the Petroleum Exporting Countries (OPEC), Alexander Novak assured markets on 1 September that OPEC had fulfilled its goal of removing excess oil supply from global markets, indicating that the market should be fully restored by next year.

Chart 9: Commodity Markets August Performance, rebased to 100

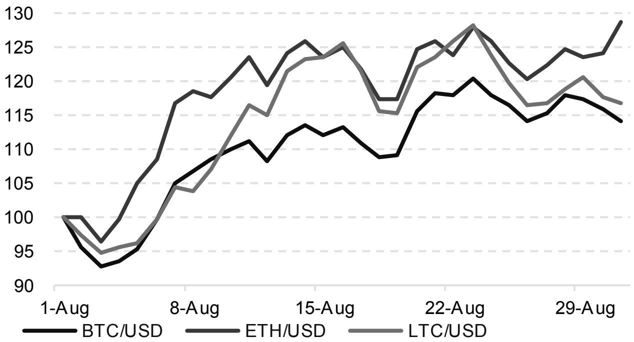


Source: BTIS / Bloomberg

Cryptocurrency

This month saw a large rally in the cryptocurrency market as it began to recover from May's fall. On 22 August, PayPal launched its first cryptocurrency service in the UK to complement its existing US launch last year. This will enable customers to buy, hold and sell Bitcoin (BTC), Bitcoin Cash (BCH), Ethereum (ETH) and Litecoin (LTC). Though this is a step towards global cryptocurrency legitimisation, the markets still remain heavily unregulated. This month, BTC managed to break through its $50,000 valuation for the first time since May, after it plummeted in response to Elon Musk's tweets about its environmental costs. CoinGecko estimates that the crypto universe has reached $2.2trillion capitalization, versus $1.2trill a month ago.

Chart 10: Cryptocurrency August Performance, rebased to 100



Source: Binance