People's Choice

Banking for life

Market Watch

Monthly Commentary September 2021

Markets this month were hit by a mixed bag full of events, from energy pricing pressures, nuclear diplomacy, name calling in the US senate and the 'wait and see' credit crisis of China's property giant, Evergrande. Europe and China began to roll out policy to cool down a tightening energy market over concerns of expected Winter surges in demand. An AUKUS alliance was formed between Australia, the UK and the US which included the building of nuclear submarines for Australia, while France was left out in the cold.

Developments in the global economy

COVID-19 Update

In Australia, vaccinations continued to dominate COVID conversations. The Federal government continued to seek out countries to expedite vaccine swaps with, successfully securing a shipment of 4 million Pfizer doses from the UK.

However, data released in the beginning of the month began to get states up in arms as evidence came to light of unequitable vaccine distribution across states. Data showed a clear tilt towards vaccine allocation to Sydney, where it's expected Victoria and Queensland were the states to lose out the most as a result.

NSW continued to lead the charge in expediting restriction rollback policy anchored by vaccination rates. The state government released a roadmap at the end of the month that detailed a staggered full re-opening of the economy, segmenting activity freedoms to those fully vaccinated and those not.

In Victoria, protests were seen this month sparked from a 2-week construction halt as it was found three quarters of construction sites were breaking COVID rules. The state saw a surge in cases finishing the month reporting daily case numbers totalling in the thousands.

The ACT extended its lockdown into October, where regional areas of NSW and Victoria went in and out of lockdown as new cases were reported.

In fiscal policy news, the Federal government announced major changes to conditions for COVID support payments.

For states that have reached 70% vaccination rates, receivers of the benefit must re-apply every week for it, as opposed to it automatically rolling over. At 80% vaccination rate, the benefit will be no longer available. This has received mixed feedback as though COVID benefits do require an expiry date, this is expected to hurt industries, such as entertainment, that take longer to ramp up from lockdowns.

International border re-openings framed conversations at the month's close. NSW announced in its roadmap that they will only be requiring international arrivals to quarantine at home for 7 days. The Therapeutic Goods Administration (TGA) has currently been reviewing rapid anti-gen testing kits for COVID to add to governments' toolboxes for re-opening as these tests have already had a high uptake overseas and can be taken at home with a result within minutes.

However, reluctance still pervades on the logistical side for these tests as they have a lower degree of accuracy, and when taken at home, hold no binding obligation to pass results onto state health departments, meaning it could contribute to some dilution in active case reporting.

Overseas, the United States announced that they will now be allowing quarantine free travel for vaccinated international passengers in a bid to increase tourism. Data released at the end of the month by the Centre for Disease Control (CDC) showed that the Delta variant's resurgence in the US might be softening as a 29% decrease in two weeks was reported.

However, on an individual state level a grimmer story is told as Alaska saw a 75% rise in cases over the same period as well as increases in Maine and North Dakota reporting 29% and 25% respectively. The CDC continues to reinforce the significance of the virus, urging citizens not to be complacent but to go and get vaccinated.

In Singapore, despite having been one of the poster children for vaccination rollouts and restriction rollbacks, some restrictions were reintroduced this month. Despite having an 82% vaccination rate, the country has since seen a surge in case numbers. However, this has not been unexpected as the nation aims to be "COVID resilient" rather than COVID free. It's been reported thus far that most new cases of COVID in the country have been either mild or asymptomatic as the death rate for September was steady at 0.1%.

Despite this, the growing case load and burden on the healthcare system has prompted Singapore to reintroduce certain restrictions such as a limit on groups of people who can gather (two now, instead of five). The country is still determined that this is a mere speedbump, and it is still on track to building full resilience to the disease, however it does provide an interesting case study as Australia moves towards opening up based on vaccination rates.

Australia

This month Australia signed a monumental defence deal with the US and the UK, which included Australia now building nuclear-powered submarines for the first time.

This has been an intentional alliance to counter China's growing influence in the area. China has aptly responded negatively and called the agreement 'extremely irresponsible' and calls out the trio for intensifying a regional arms race.

Other relations hurt through this deal have been that of Australia and France. Despite former Prime Minister Malcolm Turnbull having signed a major deal with France in 2019 to build 12 submarines, this new 'AUKUS' pact means that existing deal has been torn up. So far this has significantly damaged relations between the two allies, as France has made it clear in the media that they were alerted to this in an offensively flippant manner. The French ambassador to Australia was swiftly flown home in the wake of this deal's announcement.

In monetary policy news, the Reserve Bank of Australia (RBA) showed some softening of its monetary policy in response to Delta's resurgence. Governor Philip Lowe announced that they (RBA) will be delaying the monthly purchase rate reduction to February 2022 instead of September. This has been a welcome surprise to economists though still does not completely quell concerns over the planned reduction in bond buying.

Labour statistics this month continued to reflect lockdowns across the country as Australian jobs disappointingly dropped more than expected in August. Though the unemployment rate shrunk last month, this has been attributed to a reduced participation rate as more people stop looking for work. Hours worked fell this month by a sizeable 3.7%, as employers continued to reduce hours to better help in lockdown resilience.

Consumer sentiment improved this month as the path out of lockdown became more visible. The Melbourne Institute's monthly consumer sentiment index increased by 2.0% to 106.2, to remain above its long-run average.

Consumer confidence has been more resilient through this latest round of lockdowns, compared to the national lockdown in 2020 and the extended Victorian lockdown in late 2020. The improvement in consumer sentiment is supported by the vaccine rollout.

People who have had or are planning to get vaccinated are much more confident than those who are unwilling or undecided. Sentiment lifted strongly in Queensland (up 8.4%) as the state came out of a lockdown in early August. Sentiment also rose by 5.3% in NSW, undoubtedly helped by the state government announcing its roadmap to easing restrictions. Sentiment also rose in Tasmania. Sentiment fell in other states, led by falls in WA and SA down -9.1% and-4.3% respectively. Sentiment in Victoria, which extended its sixth lockdown, was broadly flat at 0.1%.

United States

The US finished the month with high tension in government over the country's tolerance for debt as a possible government shutdown looms. At the Senate Banking Committee hearing, both the US Secretary of the Treasury Janet Yellen and Jerome Powell, the Chair of the Federal Reserve (the Fed), called for an increase of the US debt ceiling as the country will reach this in mid-October. Both public servants have warned on the ramifications of if the US were to face a default, calling out examples of older adults receiving delayed social security payments, uncertainty for when soldiers would receive pay checks and rises in credit, auto and mortgages loan rates.

So far, many Republicans have already come out and said they will not be voting for this increase as they only see it as an enabler for Biden's pro-spend approach to policy. However, given the push for this and ramifications if not completed, it gives the Grand Old Party a powerful bargaining chip to play when needed.

Also coming out from the Senate Banking Committee hearing were comments from Senator Elizabeth Warren calling Jerome Powell a 'dangerous man' who has actively weakened the country's financial system through diluting post GFC bank regulations. Senator Warren called out that the Fed's ability so far to support COVID recovery and navigate May's Archegos collapse should be attributed to luck and has urged Biden not to renominate when Powell's term is up in February 2022.

In monetary policy, the US still has not reached the Fed's required threshold to increase interest rates. August's unemployment rate shrunk by 20 basis points to 5.2%, the lowest level since March 2020. This reduction was in line with market expectations as businesses continue to re-open. The jobless rate remains above pre-COVID levels, however markets are still optimistic that a decline is to come in this metric. Inflation saw a mild reduction in August reporting 5.3%, a 10-bps decline. The used car market showed some signs of cooling down after previously being a dominant driver of high inflation.

Though these current indicators point to the Fed holding interest rates as they are, Powell has conversely clearly signalled upcoming changes in other monetary policy tools. The Fed signalled that within the next two months a plan to reduce government backed security purchases could be announced. This clear movement away from pandemic crisis mode has analysts watching markets closely, as the removal of these purchases have the textbook ability to drive-up long-term government bond yields, while pushing stock prices lower as larger companies will find it more expensive to borrow and operate. The pairing of this uncertainty with a possible impending government shutdown puts a spotlight on the US banking system and possible spill over effects into other markets.

Asia - 'Containing' COVID

The world watched China this month as the country's second largest property developer Evergrande danced around a Lehman sized default. Listed in Hong Kong, Evergrande is part of the global 500 while employing about 200,000 people and estimated to sustain 3.8 million jobs each year. With its investment portfolio ranging from theme parks and artificial islands to soccer teams and training academies, Evergrande's aggressive approach to return caught up with them as their more than US$300billion of liabilities gave them the infamy of China's most indebted developer. Pairing its over diversified business model with a compressing residential property market in China, Evergrande landed in hot water this month with the prospect of default where speculation sent ripples into the global economy.

On 14 September, the company brought on financial advisers to help them navigate through their debt crisis with them then announcing on the 27th that they would sell a US$1.5billion stake in a local bank to raise cash. Year to date, the company's share price has fallen almost 85%. As major rating agencies revised down their credit quality and outlook at the beginning of the month.

Markets reacted as the world watched the Chinese government for any indication that they would intervene. The country's central People's Bank of China started injecting some cash as the month began to close, to keep liquidity in the financial system. In a statement the bank vowed to 'maintain the healthy development of the real estate market and safeguard the legitimate rights and interests of housing consumers'. As uncertainty pervades but at a shallower pace, markets are conscious of the large aftermath that would happen if Evergrande were to default. However, optimism remains that President Xi's risk averse attitude will play a role in prevention of this event.

For the first time since February 2020, China's manufacturing PMI contracted, reporting at 49.6 points – 0.4 points lower than the 50-point threshold for contraction/expansion. Spurred on by continued Delta outbreaks, higher material costs and production bottlenecks, the index faced a further headwind of electricity rationing towards the end of the month. As thermal coal futures in China hit all-time highs on 27 September, the Chinese government imposed rationing across multiple provinces while trying to encourage railway companies and energy administrators to increase coal transportation for winter. Run on effects of these management policies clearly felt within manufacturing measures were also seen anecdotally across the country, as residents fear for economic and political implications if power prices can't be managed in time for Winter.

In India, it was monsoon season this month as rain increased by 30% in September compared to the same time last year. This acts as a healthy signal to the future strength of the country's farming sector where nearly half of which is left fully dependent on annual monsoon rains rather than irrigation.

Japan's Prime Minister Yoshihide Suga stepped down this month after only serving one year in office. Japanese equity markets reacted positively to this news, as Suga's approval ratings hit an all-time low following a huge reoccurrence of COVID, a slow vaccination rollout and the heavily critiqued decision to go ahead with hosting the Olympics this year. Japan's consumer confidence also fully recovered, reaching a 4-month high of 37.8 points, driven through improvement in overall livelihood, income growth and employment perceptions.

Europe

Energy bills have been the headline concern across Europe in September. Driven by low stock levels, competing high Asian demand, high carbon prices in the EU and outages, natural gas prices have felt the pressure, with the fall out expected to heavily impact both households and small businesses. The Dutch gas benchmark rose more than 250% since January, while German and French benchmarks both doubled. In the United Kingdom (UK), two energy suppliers that service ~3% of the domestic market stopped trading on the 20th as they felt the pricing heat. The UK, Spain, France and Greece among others have already started considering policy responses, ranging from household subsidies and vouchers to states loans to energy companies. The EU has yet to release their promised 'toolbox' to manage this, as they aim to balance the pricing pressures and upcoming increased Winter demand, while maintaining the bloc's current approach to the electricity market.

As a result, energy has been a consistent driver of inflation across the region. The German inflation rate reached a 28 year high of 4.1%, Spanish inflation reached a 13 year high of 4% and French inflation climbed to 2.1%. These readings further validate ongoing concerns around the EU's loose monetary policy, and possibly increase the mandate for the EU to aid constituents on navigating electricity woes.

The UK's manufacturing PMI fell this month by 7% to 56.3 from 60.3 in August. This 6-month low was driven by shortages in materials and fading demand, as supply chain issues lead to many manufacturers increasing their output prices. The country's services PMI marginally fell this month by 0.4 points to 54.6 where its relative stability reflected an increase in business activity and improving consumer confidence in the ongoing COVID recovery. The UK reported an August inflation rate of 3.2%, a large jump from July's 2% as well as a 9 year high. However, this statistic becomes more diluted when considering the base effect from August 2020 when the government incentivised discounted restaurant and café prices. The Bank of England left its monetary policy unchanged this month however noted that August's high inflation rate strengthened the Bank's case that some tightening might be necessary to manage inflation back to the target 2%.

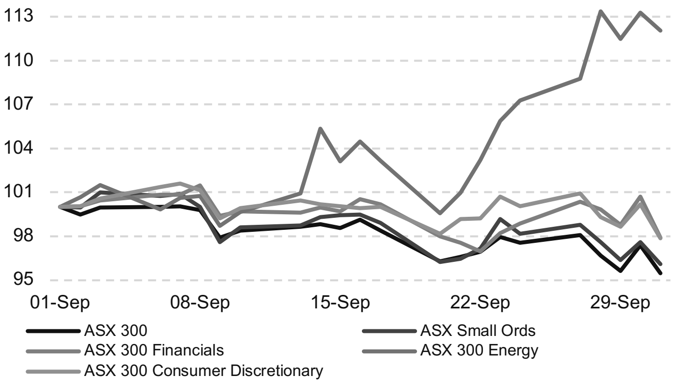
In Germany, political change was the finishing flavour for the month as voters took to the polls to elect a successor to Angela Merkel's 16-year Chancellor reign. The Social Democrats closely pulled ahead of the conservatives (CDU/CSU) however the narrow margin there's opportunity for a coalition to be formed and claim the government mandate. A clear outcome from the election is the shift of the German political compass as Merkel's conservative party received 8.9% of the vote compared to 2017. Markets had a relatively soft response to the election results; however, analysts are watching this space as the Social Democrats campaigned on promises of higher minimum wage, stable pensions, more affordable housing and a carbon-neutral economy.

Developments in financial markets

Australian Equity

Australian markets were mixed this month as the ASX300 Accumulation returned -1.89%. Energy boomed this month, returning +14.02%, as Aussie energy providers were thrust into the spotlight amongst the global electricity shortage. Materials struggled this month as markets finished down -6.70% as compressing iron ore prices continued to spill over. As COVID restriction rollback begins to put pressure on hotspot hospitals, Healthcare markets reacted by returning -4.03%.

Chart 6: Australian Equity September Performance, rebased to 100
Source: BTIS / Bloomberg



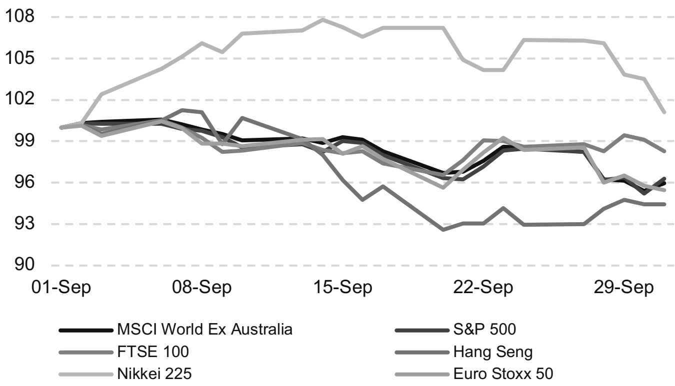
International Equity

Overall, global markets finished in negative territory this month, pulled down by concerns over Evergrande. The Hang Seng, where the company is listed, returned -5.04% over the month, spill over effects into Korea saw a -4.08% monthly return for the KOSPI. The Shanghai Composite defied this trend by reporting a muted positive return of +0.68%.

The Japanese Nikkei 225 had a booming month, reporting a +5.50% return, reaching valuation highs for the year. Analysts have attributed this growth to the market response to Prime Minster Suga's resignation, however performance began to peter off towards the end of the month as the market began to correct itself and properly respond to China's September slowdown.

In Europe, similar negative returns were seen as the Europe 600 STOXX reported -3.41%, the French CAC 40 -2.40%, and the German DAX -3.63%. the FTSE100 Reported more muted negativity of -0.47%. US markets, especially the NASDAQ, performed inline with September's "spooky" season market expectations, making this the year's worst month for returns. The NASDAQ saw -5.27% returns, Dow Jones reported -4.20% and the S&P500 reported -4.65%.

Chart 7: International Equity September Performance, rebased to 100
Source: BTIS / Bloomberg



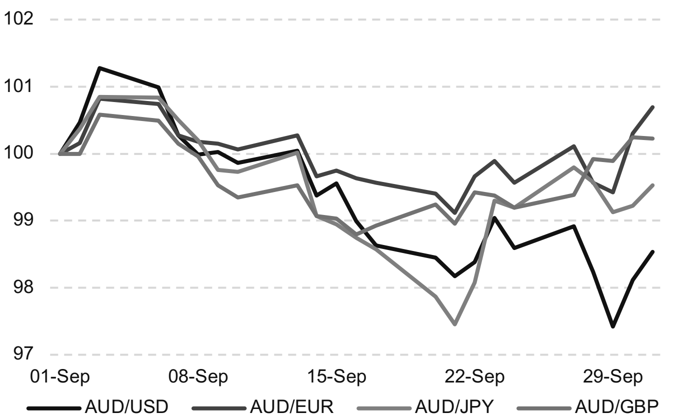
Fixed interest

With growing concerns in the global economy over energy prices pushing up inflation, markets are paying close attention central banks' sentiments and policies. The Bloomberg AusBond Composite (0+Y) index declined during the month to return -1.51%. In international fixed income markets, the Barclays Global Aggregate TR Hedged index's returned -0.97% over the month.

Foreign Exchange

The Australian dollar showed some depreciation over the month however seemed to be able to recover sufficiently. Ongoing concerns on the RBA's approach to monetary policy leave worth of the Aussie dollar uncertain as dovish forward guidance could create a headwind. Against the US dollar, Aussie returned -1.22% over the month. More success was found alongside the Euro as AUD/EUR returned +0.74%. AUD/JPY reached some of the lowest lows this month, however finished on a mild negative return of -0.06%.

Chart 8: Foreign Exchange September Performance, rebased to 100
Source: BTIS / Bloomberg

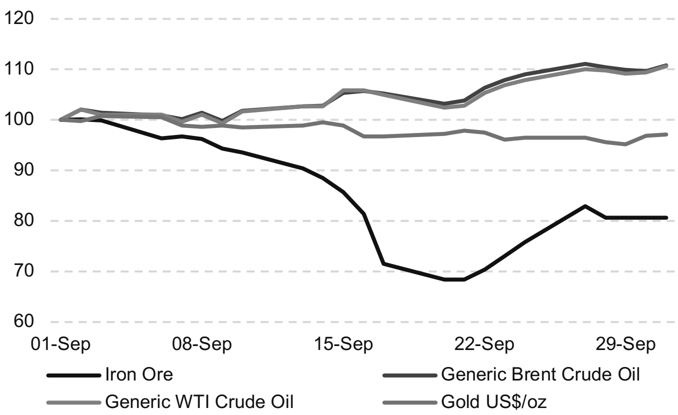


Commodities

Oil remained relatively stable this month, with brent crude returning +7.58% and WTI +9.53%. In the beginning of the month, port closures as a result of bad weather on the Gulf of Mexico saw mild price surges for the commodity. China also began releasing government reserves of crude as a measure to lower prices amid surging domestic energy costs. The government has also indicated that they may continue to release barries if necessary.

The price of gold drifted down this month as it recorded a return of -3.12%. Iron Ore was a big loser, returning -23.72% over the month as global demand continued to soften, unable to meet increasing supply.

Chart 9: Commodity Markets September Performance, rebased to 100
Source: BTIS / Bloomberg



Cryptocurrency

Cryptocurrency had a tumultuous run this month, spurred on by changing government regulation. At the beginning of the month, El Salvador announced that it was be adopting Bitcoin as legal tender and the government had purchased 200 coins before making this announcement. In tandem with this, their announced they would be temporality disconnecting its Bitcoin wallet. This caused a 17% plunge where the government was able to take advantage of the dip and purchase 150 more coins. El Salvador will be giving each citizen $30 worth of coins in order to stimulate this policy.

In the latter half of the month, China's central bank declared that all transactions involving cryptocurrency is illegal, including trading and coin mining. This follows initial regulation put in place in May that prohibited financial institutions and payment companies from providing crypto related services. Markets negatively reacted to this news, as crypto enthusiasts shift their focus back to the US as a hub for growth.

Chart 10: Cryptocurrency September Performance, rebased to 100
Source: Binance