Markets Summary – September 2020

Taken from the CBA Global Markets Research report, "September Month in Review", first published on 1 October 2020 and "CoreLogic Dwelling Prices – September 2020" first published on 1 October 2020.

Highlights in September

- There was no change to the RBA cash rate but markets began to speculate about further RBA easing actions.
- Credit spreads widened marginally as volatility picked up offshore, impacting local sentiments.
- The Australian dollar (AUD) fell 3% over the month.
- Australian equities gave back the August gains with a 2.4% fall.
- Higher thermal and coking coal prices offset lower iron ore, oil and gold prices.
- Dwelling prices in the eight capital cities fell 0.1% in September.

Summary

A risk-off sentiment for equities invaded markets and for Australia, the prospect of a tweak in monetary policy took short-term government bond yields to new lows. Equity markets gave back gains over the month. The AUD fell 3% against the US dollar (USD) as risk asset wavered and potential RBA monetary policy action came back into focus.

Cash

The Reserve Bank of Australia (RBA) official cash rate and three-year bond yield target remained unchanged at 0.25% in September. A speech by RBA Deputy Governor Guy Debelle prompted a change of view from some in the market to expect a shift lower in rates for the October RBA meeting. As a result very short-term money markets dropped to new lows as the case was built for a lowering the term structure of interest rates further. While Debelle's speech laid out options for the RBA should further easing be required, many commentators came out against these views and yields started to shift higher.

With the imminent budget statement, there was more weight put on a fiscal response than a monetary response.

The Australian Commonwealth Government Bond 3-year rate fell well below the RBA's target rate, while the Bank Bill Swap Rate (BBSW) set lower in all maturities.

Australian and global fixed interest

September was mostly a long slow rally (fall in bond yields) for bonds. The month began with the RBA expanding the Term Funding Facility (TFF), a program to allow banks access to funding at low rates. The RBA explicitly called for monetary policy easing,-and finished with widespread speculation about further RBA easing to come. For much of the month the global backdrop was "risk off", and US equities fell fast for most of September.

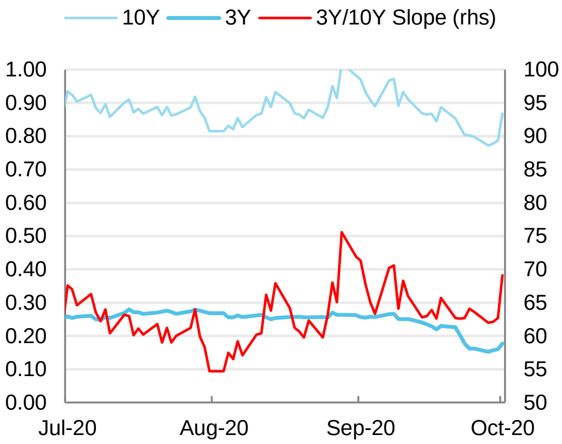
The 10-year Australian bond rallied (fall in yields) by 19 basis points (bp) over September, to close at 0.79%. The 3-year bond rallied too, closing the month 10bp lower in yield at 0.16%.

The global backdrop was similar with US 10-year yields lower by 7bp to 0.65%.

RBA Deputy Governor Guy Debelle's speech on 22 September canvassed possible options for the RBA to undertake further easing "should the Reserve Bank Board" decide that it is warranted. Little in the speech was new, its content having been mostly discussed by the Governor in July. The last week of September was marked by a strong fall in yields in the front-end of the bond curve.

Currently, the RBA's Yield Curve Control measures have a 3-year bond target of 0.25%. After sitting between 0.24% and 0.28% for a long time, the market took 3-year bond yields down into the mid-teens. This suggests that many expect the RBA to lower the target rate at some point. There was a slight retracement into month-end. The RBA continued to buy government bonds in September, with a single large $A2bn transaction on 9 September.

Chart 1 – Australian bond yields



Source: Bloomberg, CBA

Global credit

Australian credit managed to deliver positive total returns in a volatile month. The spread rally that we've seen since late April came to a halt and average spread for A$ credit widened marginally as volatility picked up offshore, impacting local sentiment. Given the strong rally we've seen in the last few months, valuations are starting to look less attractive, especially for financials.

There is a big dispersion in the degree of spread recovery across different sectors. Sectors that were less impacted by COVID have seen spreads recover to close to pre-COVID levels. This includes Consumer Staples, Utilities and Telco. Industries including REITS, Airlines, Autos, Unis and Industrials are still trading at significantly wider levels compared to where they were before COVID.

Global equities

A raft of factors influenced global sharemarket trade in September. European countries were forced to lock down again to combat second waves of the coronavirus. There was profit-taking across the technology sector. US Congress continued to debate the need for more fiscal stimulus, and economic data encouraged investors, especially US housing activity.

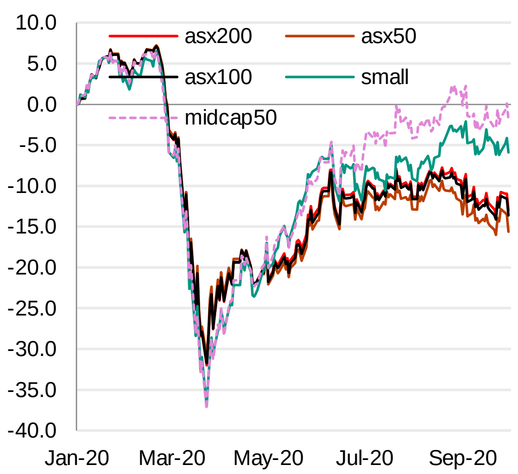
After stellar gains in August, it was a more volatile start for global sharemarkets in September as investors cashed in some of the more recent gains, especially on technology stocks.

Over September, global markets fell after solid gains recorded in August. US sharemarkets posted their first monthly decline since March. The US Dow Jones fell by 2.3%, the S&P 500 fell by 3.9% and the Nasdaq lost 5.2%. In Asia, Japan's Nikkei actually gained 0.2% while Australia's ASX 200 fell by 4.0%. In Europe, the German Dax lost 1.4% and the UK FTSE fell by 1.6%.

Australian equities

Six of Australia's 22 sub-industry sectors posted gains in September with one sector unchanged. Leading the gains was Autos & Components (up 3.0%) followed by Transportation (up 1.7%). Insurance fell the most (down 11.8%). Of the size categories, the Small Ordinaries index and MidCap50 index were down the least (down 3.3%) from the ASX100 index (down 4.1%) and the ASX50 index (down 4.2%).

Chart 2 - Midcaps lead the way



Australian dollar

The AUD fell by 3.0% on a trade-weighted basis in September. It fell against all major currencies except the British pound.

The AUD peaked at 0.7414 on 1 September. A weakening USD and high commodity prices supported the AUD early in the month. The Federal Open Market Committee (FOMC) meeting and Australian labour force report caused some volatility mid-month. August employment data was substantially stronger than expected, with employment rising by 111,000. The unemployment rate fell to 6.2%. We revised our GDP forecasts higher following the release.

However, the AUD largely retreated over the remainder of September as concerns about the global growth outlook emerged. A lack of fresh US fiscal stimulus and the COVID outbreak in Europe clouded the global economic outlook. Growing expectations that the RBA could ease policy settings as soon as 6 October also weighed on the AUD. RBA Deputy Governor Guy Debelle, suggested the RBA could cut interest rates by some 10-15bp amid other policy easing options.

Table 1 – Australian dollar September performance

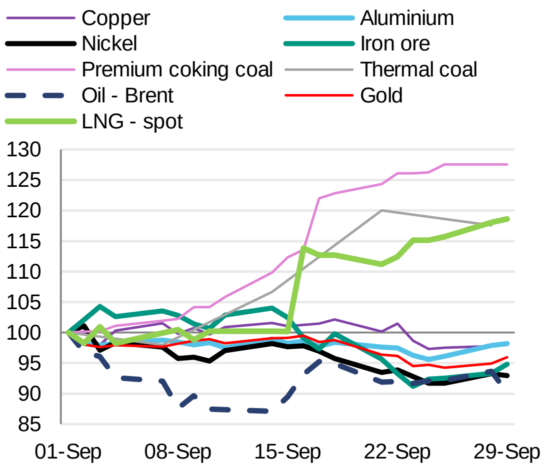
AUSTRALIAN DOLLAR			
	End Aug 31-Aug-20	**End Sep 30-Sep-20**	**M/M % Change**
AUD-USD	0.7376	0.7162	-2.9
AUD-JPY	78.12	75.54	-3.3
AUD-EUR	0.6179	0.6111	-1.1
AUD-GBP	0.5517	0.5544	0.5
AUD-CHF	0.6666	0.6596	-1.1
AUD-CAD	0.9623	0.9539	-0.9
AUD-NZD	1.0954	1.0826	-1.2
TWI	62.6	60.7	-3.0
Month High		0.7414	1-Sep-20
Month Low		0.7006	25-Sep-20

Source: Bloomberg, CBA

Commodities

Commodity prices finished mostly lower in September as the US dollar strengthened. Demand concerns also weighed on prices last month as global COVID-19 cases continued to rise. The increase in case numbers in parts of the US and Europe also boosted the likelihood of a re-tightening of restrictions. Oil fell more than other major commodities, consistent with the amplified threat of lockdown measures on oil consumption (transportation accounts for around two-thirds of oil demand). There were a number of notable exceptions to the fall in commodity prices last month. Coking coal, thermal coal and spot LNG prices saw strong gains.

Chart 3 - Commodity price performance in September



Australian Property

According to CoreLogic data national property prices continued to move lower in September. But the pace of monthly declines has slowed and outcomes were very disparate across the country. Price outcomes by capital city are to a large extent mirroring the different economic fortunes of each state in Australia.

The lockdown in Victoria has continued to have a negative impact on property prices in Melbourne. The 0.9% decline in dwelling prices in Melbourne was the largest across the capital cities. Over the COVID period so far, price falls have been by far the greatest in Melbourne (down 5.5% since March 2020).

Dwelling prices continued to move lower in Sydney over September although the pace of monthly falls has eased. Auction clearance rates, which are a high frequency momentum indicator, have been hovering at around 65% in Sydney over the past two months. Historically that level of clearance rates has been consistent with modest price rises rather than falls.

Dwelling prices rose in all other capital cities. In fact, prices have risen over the COVID period in Adelaide, Hobart, Darwin and ACT while they are little changed in Brisbane. There have been labour market shocks in each of these capital cities and unemployment has risen. But it looks to be the case that the reduction in mortgage rates has offset the negative force of rising unemployment in these markets. Regional markets have also held up well. The combined regional index was up by 0.4% in September.

At the national level housing supply remains tight. And according to Corelogic there are no signs of a rise in distressed listings or stock starting to pile up the market.

Chart 4 – Dwelling Price moves – monthly change and annual change

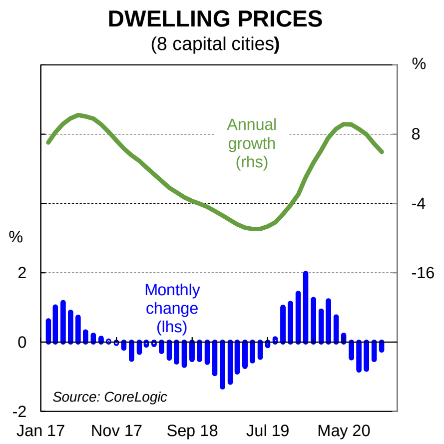
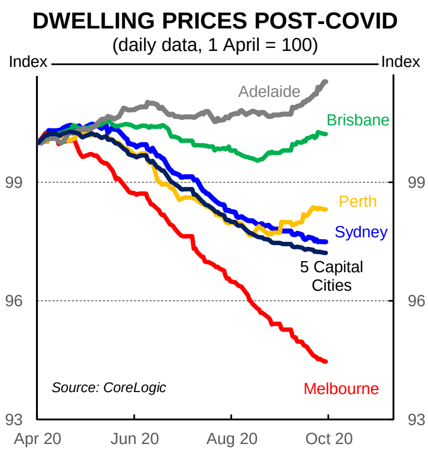


Chart 5 – Dwelling Price Index



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