Markets Summary – December 2020

Taken from the CBA Global Markets Research report, "December Month in Review", first published on 19 January 2021 and "CoreLogic Dwelling Prices – December 2020" first published on 4 January 2021.

Highlights in December

- Government bond yields rose given the optimistic economic outlook.
- Credit spreads finished the year tighter than where they were before the pandemic.
- The Australian Dollar (AUD) enjoyed a solid rise.
- A positive end of year for equities.
- Dwelling prices rose again in January.

Summary

Government bond yields didn't change too much over the month of December, but the yield curve steepened and touched the highest level in three years. The state governments of NSW and Victoria received a credit rating downgrade by Standard and Poor's post release of the state budgets.

The AUD surged again, adding 3.1% on a trade weighted basis. Equities finished the year on a bullish note, though sectors were mixed. Credit performed well and closed the year tighter.

Cash

The RBA left monetary policy unchanged at its 1 December 2020 meeting. The post meeting statement struck the right tone between recognising that the Australian economic data "*have generally been better than expected*" whilst acknowledging that, "*the recovery is still expected to be uneven and drawn out*". The Reserve Bank of Australia (RBA) also pointed out that it does not expect to increase the cash rate for at least three years and reiterated it is prepared to do more if necessary.

Following the November RBA rate cut, market rates drifted lower into the end of the year in the front end, and Bank Bill Swap Rates (BBSW) touched new lows. BBSW tenors set between 2.5bp and 2bp for the 6 month tenor and between 2bp and 1bp for the 3 month tenor.

Australian and Global Fixed Interest

Bond markets saw yield curves steepen over the latter part of the year, and longer yield rates moved modestly higher.

The month was largely about the Semi government bond market however, as the budget updates came thick and fast and showed what a wrecking ball Covid-19 has been for public finances.

Both NSW and Victoria were downgraded, NSW losing its coveted AAA rating from S&P and going down a notch to AA+. In the case of Victoria, the elongated lock down period and the underlying weakness in budget management caused a double notch downgrade- placing Victoria at the bottom of the ratings pile at AA.

In terms of Commonwealth government bond yields, the three-year yield fell from 0.113% to 0.102%, with a low of 0.098% in December. The 10-year started the month at 0.897%, topping out at 1.036% and finishing the year at 0.97%.

Global Credit

As usual, December was a relatively quiet month for the Australian credit market**.** Average Australian dollar non-financial corporate bonds are now trading 5bps tighter than where they were before the COVID-19 crisis With many sectors now trading tighter than pre-crisis levels, investors have continued to shift into some of the higher beta sectors such as retail REITs and Infrastructure where valuations are still looking attractive. Risk appetite continued to improve in December. Investors moved up the risk curve and into more cyclical names as sentiment improved

Global Equities

Global sharemarkets ended 2020 on a positive note with the US Dow Jones and S&P 500 indexes hitting record highs on the final trading day of the year. Share prices lifted in December as Covid-19 vaccines were approved and began to be rolled out. Risk sentiment was also supported by a new US fiscal stimulus package and Brexit trade deal, despite a resurgence in Covid-19 infections and tightening of government restrictions.

In December, the US Dow Jones index rose by 3.3%, the S&P 500 index gained 3.7% and the Nasdaq index rose by 5.7%. In Europe, the German Dax index rose by 3.2% and the UK FTSE lifted 3.1%. In Asia, Japan's Nikkei index lifted 3.8%, while Australia's ASX 200 index gained 1.1%.

Eight out of Australia's 22 sub-industry sectors posted gains in December. Leading the gains was Software & services (up 9.4%) from Auto & Components (up 9.0%). But Utilities (down 6.8%) led the falls from Household & personal products (down 5.6%). Of the size categories, the ASX MidCap50 index (up 3.2%) rose most from the Small Ordinaries index (up 2.5%), the ASX100 index (up 1.0%) and the ASX 50 index (up 0.6%).

Over the December quarter, the Dow Jones index jumped 10.2%; the S&P 500 index soared 11.7% and the Nasdaq index gained 15.4%. The Japanese Nikkei index (+18.4%) performed strongly with the S&P/ASX 200 index (+13.3%) capping its strongest December quarter in history. In Europe, UK FTSE index rose 10.1% and Germany's Dax index lifted 7.5%.

In 2020, the S&P/ASX 200 index fell by 1.5%, dragged down by energy (-29.9%) and Utilities (-21.5%) shares. The broader All Ordinaries rose 0.7%. And the MSCI Australia index in US dollar terms rose 6.9% and ended 2020 just off record highs set on December 18. The MidCap50 index (+14.5%) outperformed, but the S&P/ASX50 fell most (-4.9%). Movements of other key indexes over 2020: US Dow Jones (+7.2%); US S&P500 (+16.3%); US Nasdaq (+43.6% – best annual performance since 2009); Japan Nikkei (+16.0%); UK FTSE (-14.3%); and German Dax (+3.5%).

Australian Dollar

The AUD rose on a trade-weighted basis by 3.1% in December 2020. AUD outperformed against all the currencies under our coverage. AUD/USD rallied to its highest level since April 2018 supported in part by surging iron ore prices and encouraging Australian economic activity.

Australia real GDP lifted more than expected by 3.3% over Q3 2020 (consensus: 2.5%) and leading indicators point to further improvement ahead. In December 2020, the consumer confidence index rose to a ten-year high and the composite PMI increased to a five-month high of 57.0.

Table 1 – Australian dollar December performance

	AUSTRALIAN DOLLAR		
	End Nov	End Dec	M/M %
	30-Nov-20	31-Dec-20	Change
AUD-USD	0.7344	0.7694	4.8
AUD-JPY	76.61	79.47	3.7
AUD-EUR	0.6158	0.6298	2.3
AUD-GBP	0.5512	0.5629	2.1
AUD-CHF	0.6675	0.6809	2.0
AUD-CAD	0.9548	0.9796	2.6
AUD-NZD	1.0469	1.0709	2.3
TWI	61.5	63.4	3.1
Month High		0.7686	30-Dec-20
Month Low		0.7342	1-Dec-20

Source: Bloomberg, CBA

Australian Property Prices

December's Corelogic data showed that dwelling prices were up by 0.9% across the eight capital cities combined in the month. Dwelling prices finished the year 3.0% higher. There were solid gains in each of the capital cities in the month ranging from 2.3% in Darwin to 0.7% in Sydney. Regional dwelling prices also rose solidly.

Over the year dwelling prices rose in all capital cities with the exception of Melbourne (-1.3%). The COVID-19 pandemic has had the largest negative impact on the Melbourne property market, with this jurisdiction facing the highest number of cases and the tightest and longest restrictions so far. Dwelling prices in Melbourne are now recovering, but are still 4.1% below their peak in March 2020. Sydney dwelling prices are also still a touch below pre-pandemic levels.

Sales volumes have staged a recovery and were around 30% higher in H2 2020 compared to the first half of the year. Once again the exception is Melbourne, where sales volumes didn't start to recover until October when the winding back of restrictions was well underway.

Chart 1 – Dwelling Price moves – monthly change and annual change

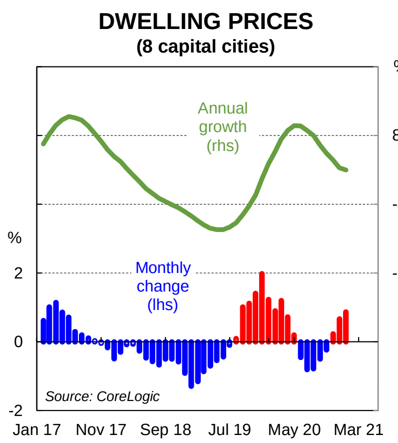

Chart 2 – Dwelling Price Index