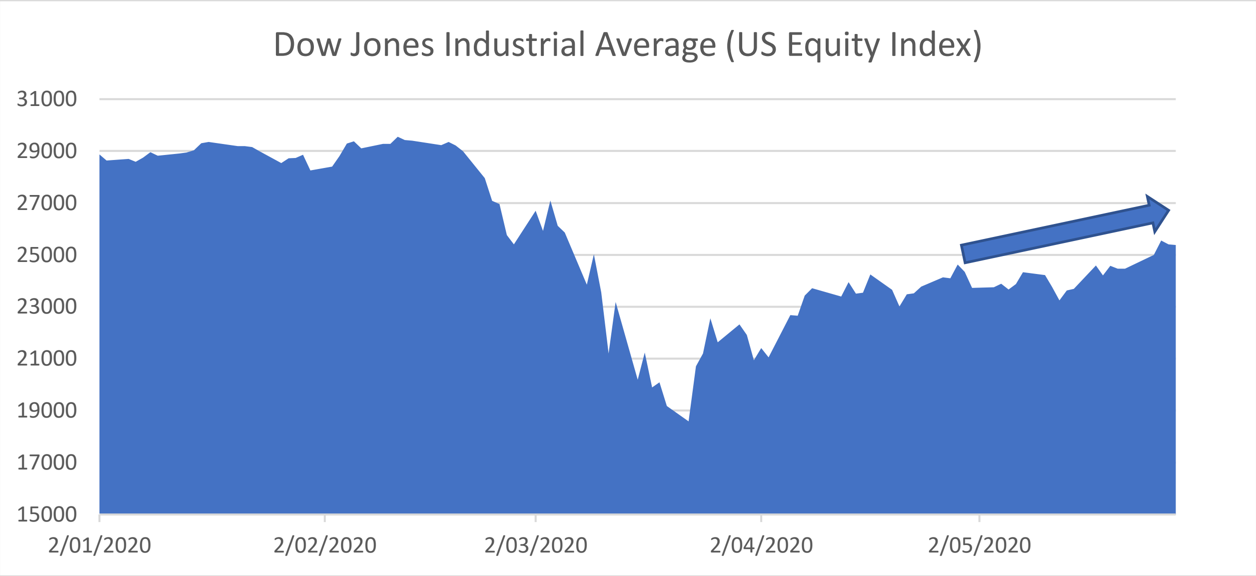
Financial Market Conditions

Global financial markets were volatile over the past month as the world continued to deal with the public health crisis and the economic downturn caused by the COVID-19 pandemic, however, markets began to price in a less severe downturn than initially expected.

The coronavirus (COVID-19) continued to spread around the world over the past month with just over 6.2 million confirmed cases, just under 380,000 confirmed deaths and the virus now active in 216 countries. The United States (US) is now the new epicentre of the virus with just under 1.8 million confirmed cases and over 100,000 confirmed deaths.
The US unemployment rate for April increased from 4.4% to 14.7%, its largest one month rise in history, with many now predicting that the US unemployment rate could exceed 20%. Despite this data and civil unrest in parts of the country, a decline in the number of new cases of COVID-19 buoyed equity markets highlighted by the Dow Jones industrial average rising by around 7% over the course of the month.



The yield on US 10-year bonds did not reflect the same positive sentiment and remained relatively static over the month opening and closing the month at 0.64%.
In April, Eurozone unemployment only rose 0.2% (from 7.1% to 7.3%) and was a much smaller increase than experienced in the US. The lower rate can be attributed to the introduction of short time job schemes (similar to job keeper in Australia) by many countries and lower participation rates due to the shutdown. It is likely that the unemployment rate of the Eurozone will increase dramatically once these government job aid packages end which will force people to start looking for work again.

Australian financial markets also experienced some volatility over the past month, however, markets remained cautiously optimistic about Australia’s economic outlook because of the relatively low number of COVID-19 cases here.
The lifting of many social distancing restrictions by Australian State Governments has created a more optimistic environment for the many Australians that have been affected by the pandemic. While it is still hard to ascertain the true financial impact of the pandemic the Australian unemployment rate for April rose 1% (from 5.2% to 6.2%) which was lower than most forecasts but is likely masked by the Federal Governments job keeper and job seeker programs. It is likely that higher levels of unemployment will become apparent once these programs end. The Australian equity market was also carried along with the positive sentiment seen in other equity markets across the globe rising by almost 10% over the course of the month. In early June Australian GDP printed at -0.3% for the first quarter of 2020 taking the year on year figure down to 1.4%. This result was better than expected, however, most commentators are now declaring that Australia is already in its first recession since 1991. The Australian dollar has benefited from the more positive sentiment and appreciated by over $0.05 USD over the past month and is currently trading at just over $0.69 USD.

Since our last update, the RBA met on 2/6/2020 and left the official cash rate at an all-time low of 0.25% and also committed to keep targeting a 3-year Australian government bond yield of 0.25%. In the accompanying statement Reserve Bank Governor, Phillip Lowe, noted the severe global downturn resulting from the coronavirus pandemic but also noted that it may be possible that the depth of the downturn will be less than earlier expected. The Board once again committed to not raising the official cash rate target until progress is being made towards full employment and until it was confident that inflation will be sustainably within the 2–3 per cent target band. This view is reflected by interest rate futures pricing.

<u>Implied RBA Cash rate as at 31/05/2020:</u>