



## RESEARCH UPDATE

*Market Watch - September 2019*

**Volatility returned to markets in August, mainly driven by geopolitical events. The S&P/ASX 200 declined 3.06% to close at 6,604 points, slightly underperforming US markets. The S&P 500 Index and Nasdaq Composite Index declined by 1.81% and 2.60%, respectively. Hong Kong's Hang Seng Index was one of the worst performing indices, declining by 7.39% as ongoing protests disrupted financial markets.**

### Sector Performance

Individual sector performance was mixed, with most companies releasing their latest financial results and guidance for the next financial year. Materials was the worst performing sector, declining by 7.9%, driven by packaging company, Orora Limited, which fell 17.46% after its US operations performed worse than anticipated.

Energy declined 6.4%, impacted by Oil Search Limited, which declined by 6.6%, after the new Prime Minister of Papua New Guinea announced he would take a tougher stance around contract negotiations. Woodside Petroleum Limited declined 7.41% after releasing its first half 2019 results, as investors were concerned about declines in future oil production and the lack of progress on replacement projects.

Telstra Corporation fell 6.3%, underperforming the Communications sector which declined 4.5%, after releasing its financial results that reflected the ongoing impact of the National Broadband Network and a decline in average revenue per user in mobile as a result of strong competition, which is unlikely to ease in the short term.

Financials declined by 3.6%, impacted by AMP Limited, which fell 5.31% after announcing a \$650 million capital raising to fund its three-year strategic turnaround plan.

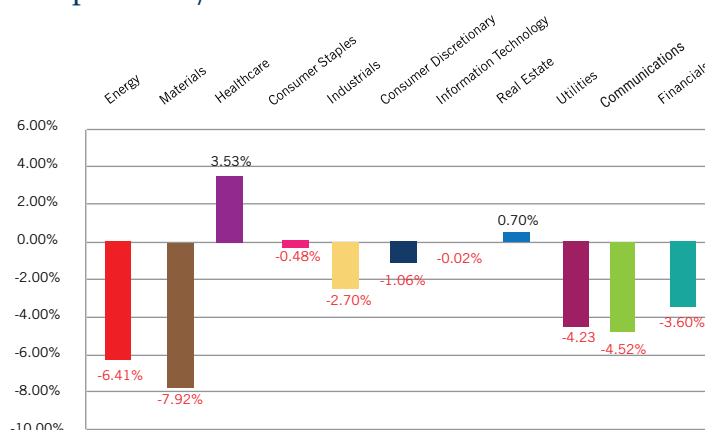
Commonwealth Bank announced it would enter the 'buy now, pay later' sector by investing US\$100 million in European payments company, Klarna, and will also partner with the company to expand its services to Australia and New Zealand in direct competition with Afterpay Limited. Magellan Financial Group fell 18.0%, impacted by a capital raising and the volatility in international equity markets.

The Consumer Discretionary sector declined 1.06%, impacted by Wesfarmers Limited announcing the Australian Competition and Consumer Commission would not oppose the acquisition of online retailer Catch Group. Wesfarmers also released a statement that despite rare earths miner, Lynas, receiving a renewal of its operating licence in Malaysia, a condition to the takeover, they would not be pursuing the acquisition further.

Consumer Staples was flat, despite a 20.90% decline in A2 Milk, which was impacted by concerns that ongoing protests in Hong Kong would depress sales, and management's guidance for lower future margins.

Healthcare was the best performing sector, as CSL Limited (+4.90%), ResMed Inc (+8.37%), Nanosonics Limited (+19.71%) and Pro Medicus (+21.05%) all released financial results that beat market expectations, primarily due to their respective North American operations.

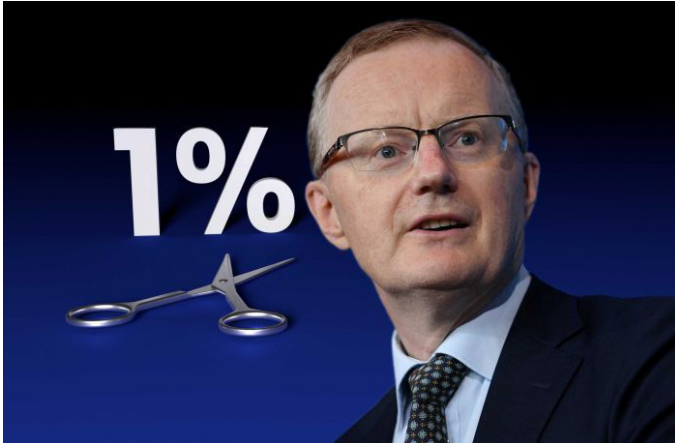
**Graph 1: S&P/ASX 200 Sector Performance**



Data Source: Bell Potter, 2 September 2019.

## Highlights

**Australia:** The Reserve Bank of Australia (RBA) Governor, Phillip Lowe, announced at the House Economics Committee Hearing that 0% interest rates are a possibility as global Central banks cut interest rates. He hopes to avoid negative interest rates and asset purchase programs with recent rate cuts, income tax cuts, a weaker currency and infrastructure spending serving as a turning point and boosting demand.



The Australian Bureau of Statistics (ABS) reported a month-on-month 0.4% increase in seasonally adjusted retail turnover in June. The strongest results were in Tasmania (+1.5%) and Western Australia (+0.3%) which offset South Australia (-0.3%) and Northern Territory (-0.2%). Online retail turnover contributed 6.1% to total retail turnover, an increase from 5.7% in June 2018. The June Quarter retail turnover increased 0.2% in seasonally-adjusted terms driven by Department stores (+1.4%) and clothing and footwear (+0.7%) which offset food retailing (-0.4%).

The ABS reported a seasonally-adjusted 1.3% increase in new lending commitments to households following a decline of 1.6% in May. The increase was driven by both owner occupier and investor dwellings; however, investor lending continues to remain below previous highs. The increase was driven by New South Wales (+2.4%), which offset declines in both the Northern Territory and Australian Capital Territory. If the increase persists it will likely lead to an increase in property prices.

A \$20 billion Northern Territory solar power project is currently being discussed with investors and other potential financiers, with a targeted completion date of 2027. The project would include a 15,000-hectare ground array of solar panels supported by a 20 to 30-gigawatt storage plant. The electricity generated would supply Darwin, with surplus electricity exported to Singapore through undersea cables. The project is the second mega renewable energy export plant proposed in Australia, after a \$22 billion project in Western Australia which has been financed by Macquarie Group and a number of other Asian based infrastructure investors.



The Federal Government is investigating nuclear power to replace the ageing coal power plants and support the transition to renewable energy sources, which can at times lead to intermittent supply. Nuclear power is currently banned in Australia and faces community opposition. British engineering company, Rolls-Royce, has said it could build a compact nuclear power plant in Australia for \$2.7 billion, and several other companies are also working on new lower-cost compact designs.

**US:** The Federal Reserve announced it intends to build and operate a real-time payment service called 'FedNow' by 2024, as the large banks have been too slow to adopt real-time payments and now lag much of the rest of the world. The service will be available to all depository institutions, such as banks and credit unions, but would exclude technology companies, such as Amazon and Alphabet.

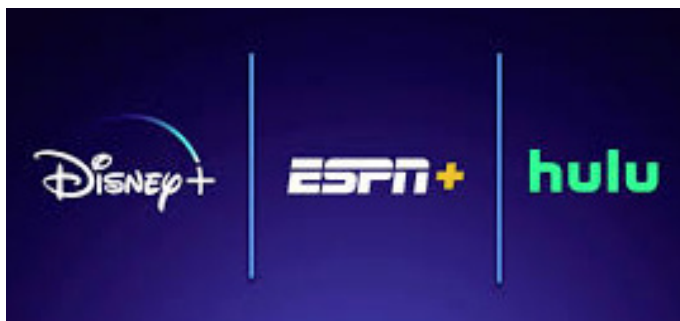
The news comes as a number of alternative systems, such as Facebook's cryptocurrency 'Libra', would enable a complete bypass of the traditional banking system. The RBA is already developing a similar network in Australia.

US President, Donald Trump, has continued to call on the Federal Reserve to cut interest rates and consider further quantitative easing to assist the economy, despite announcing a contradictory message that the American economy is at little risk of recession. The US Federal Reserve is independent from the US Government but may face ongoing pressure from the current Administration, as any weakness in the economy may impact President Trump's re-election prospects in 2020.



Esports continues to increase in popularity, with new competitions beginning to attract sponsor interest. A competition in New York for the popular game 'Fortnite' offered US\$30 million in prize money, with a top prize of US\$3 million for singles and doubles winners. The audience for game streaming is becoming one of the most popular forms of entertainment led by South Korea, with Amazon-owned 'Twitch' the most popular streaming service.

The Walt Disney Company has announced the US launch of a bundled package of Disney+, Hulu, and ESPN+ for US\$12.99 a month, with a launch also planned for Australia. The subscription video on demand (SVOD) segment continues to grow with separate studios announcing direct-to-consumer offerings to bypass traditional aggregators such as Netflix and Amazon Prime, as these services invest in developing their own original content. There is a possibility that the previous aggregators will convert to studios with Foxtel signing an agreement with Netflix to distribute its original content.



**Denmark:** Nordea Bank has announced it will begin offering 0% interest 20-year fixed-rate loans and 0.5% 30-year fixed-rate loans as the Denmark 10-Year Government bond rate slides below -0.5%.

The China-US trade war continues to escalate with the announcement of new tariffs and further declines in China's currency, the Renimibi. A decline in the Renimibi makes Chinese goods and services more attractive to foreign buyers and offsets some of the impact of the American tariffs.

## What to watch out for

An escalation of the protests in Hong Kong has the potential to impact financial markets, with Hong Kong serving as the financial capital of Asia due to its independent judiciary and historically stable political leadership. Chinese multinational conglomerate, Alibaba Group Holdings, has already announced it would postpone a second listing on the exchange.

Recent volatility has seen a rally in the price of gold and sovereign treasury bonds, with a large portion of the world's sovereign treasury bonds now trading on negative yields.



UK Prime Minister, Boris Johnson, has suspended Parliament in an effort to force the UK into a no-deal Brexit strategy, which market commentators speculate would severely impact supply chains, leading to shortages in essentials such as food and medicine.

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## Conclusion

Markets are experiencing the first bout of volatility for 2019, as concerns are raised that the ongoing geopolitical tensions and indicators pointing to a slowing global economy could lead to the next global recession. Central Banks have begun easing monetary policy, however, with global interest rates already below historical norms the impact of these cuts may be limited. The local market has seen a wide divergence in sector performance following company reporting season, with investor attention now likely again focusing on developments offshore.

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