WEEKLY UPDATE

31st August 2020

	Price	5 Day % Change	3 Month % Change	1yr % Change
S&P/ASX300	66,498	-0.23%	6.26%	-4.76%
MSCI World Ex-Aus. (Unhedged)	11,203	0.03%	3.66%	7.49%
MSCI World Ex-Aus. (Hedged)	1,961	2.26%	12.33%	12.29%
Bloomberg AusBond 0+ Composite	10,578	-0.56%	0.10%	1.46%
BloombergBarclays Global Agg. (Hedged)	1,098	-0.48%	0.68%	2.41%
S&P/ASX300 Property	49,041	1.31%	5.75%	-18.35%
FTSE/Epra NAREIT (Hedged)	2,390	1.36%	6.17%	-16.90%
S&P Global Infrastructure (Hedged)	4,644	-0.03%	0.06%	-14.39%
BarclayHedge Global Hedge Fund Index (USD)	5,817	N/A	10.55%	0.55%
Gold in AUD	2,668	-1.55%	3.04%	16.73%
AUDUSD	0.7365	2.85%	10.97%	9.37%
AUDEUR	0.6188	1.89%	3.18%	1.78%
AUDNZD	1.0924	-0.23%	2.17%	2.70%
AUDGBP	0.5517	0.84%	2.36%	0.05%
AUDJPY	77.6070	2.36%	7.95%	7.92%

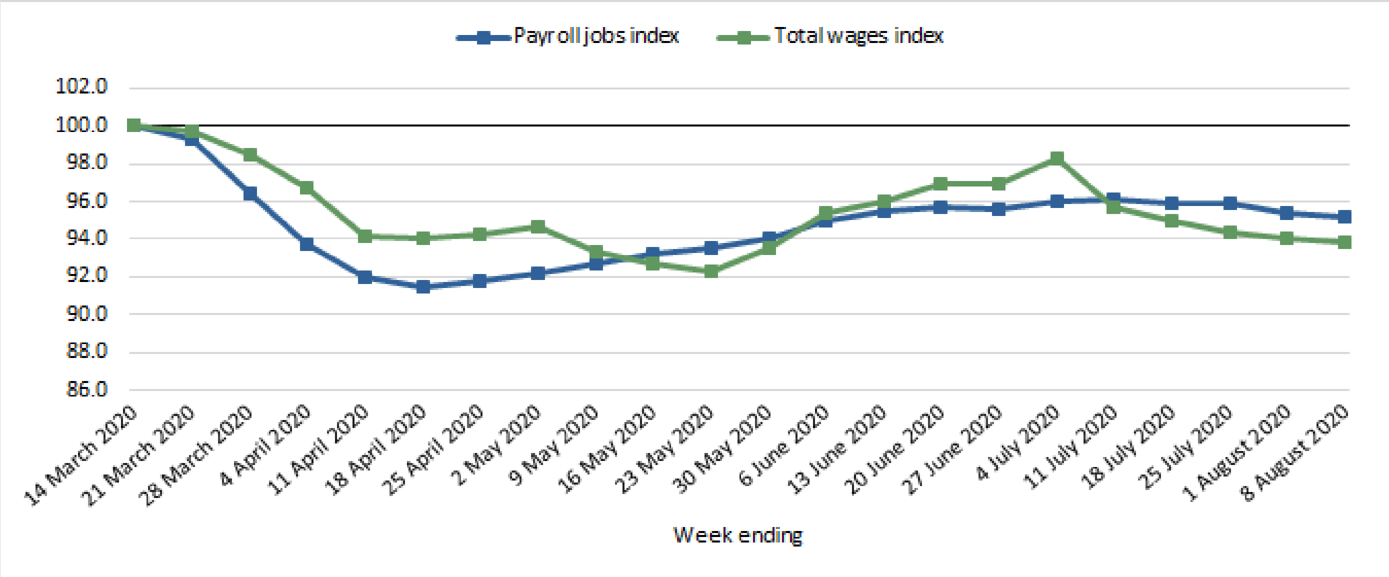
Source: Bloomberg, S&P Dow Jones, MSCI, FTSE/EPRA, Barclays, 30th August 2020

The Federal Reserve's updated monetary policy framework now allows the FOMC to overshoot the 2% target to deliver an average inflation level of 2%, favouring lower unemployment. The muted reaction from markets so far underlines the difficulty in achieving the inflation target, considering that August unemployment is expected to be reported at 9.8% on Friday. But, due to the divergence in monetary policy and the Fed's boost to commodity prices, the Australian dollar was still able to appreciate by nearly 3% last week.

This week, as well as the US labor report and ISM surveys, Australia is expected to report a quarterly decline of 6.0% in Q2 GDP on Wednesday, and a record current account surplus as the RBA meets on Tuesday.

The highlight of last week was the Federal Reserve's eagerly anticipated update to its long-term monetary policy framework. Chair Jerome Powell introduced the new 2% average inflation target during an online, public, version of the annual Kansas City Fed.'s symposium that usually takes place each year behind closed doors in Jackson Hole, Wyoming. The market had previously understood from earlier communications that the FOMC would tolerate inflation drifting above the 2% target after prolonged periods of less than 2% inflation. However, this was the first time that the Fed has adopted the explicit target of an *average* of 2% over the cycle.

The slight modification allows the Fed to err on the side of higher inflation when the economy is expanding. The main reason for the change is that the Fed would have less scope to ease policy when required if low inflation expectations became entrenched. Moreover, in conducting a series of "the Fed Listens" public events as part of its review, officials have often remarked how persistently high unemployment disproportionately hurts the poorest in American society, and that the social effects can be transmitted across generations. Consequently, the objective to foster maximum employment appears now to be slightly more important than the Fed's second objective; to achieve price stability. Any concerns that loose monetary policy will lead to rising inequality through asset price inflation were referred to Congress and the President to address through fiscal policy.



Source: ABS, 30th August 2020

There is, however, no guarantee that inflation will reach 2% during the cycle. The Fed's preferred PCE measure tends to be persistently lower than CPI, and demographic and productivity challenges to raising inflation are significant. Nevertheless, the risk of higher inflation caused the US Treasury yield curve to steepen as investors began to demand a higher inflation risk premium for longer-dated issues. Bond indices moved slightly lower over the week.

The new Fed policy framework is also likely to weaken the US dollar, especially against the Australian dollar, where monetary policy is significantly tighter in comparison. The change is also positive for gold, commodity prices in general, and other real assets. The Australian dollar strengthened by nearly 3% last week. Property indices also advanced, while infrastructure trailed despite having a stronger link to inflation through concessionary contracts.

Stocks traded higher, with US indices on track for the best August since 1986. August to October tend to be seasonally weaker months. However, the promise of further liquidity is pushing the stock market to new highs even in the absence of a fiscal stimulus extension, very optimistic earnings forecasts, and as credit conditions are obviously tightening. To add to the pain, Capital One cut credit limits across its cards last week.

As the Australian reporting season draws to a close, 267 / 295 S&P/ASX300 companies have delivered an aggregate decrease in semi-annual profits of -24%, according to Bloomberg. Estimates for the next fiscal year are for a wildly optimistic +67% rebound. The very high estimates imply that the actual 1yr forward PE ratio may be much higher than the reported 22.4x. If earnings growth turns out to grow by only +25%, for example, the implied forward PE rises to 30x.

Last week's data revealed little new information. US durable goods and the German IFO survey were a little ahead of estimates, but still significantly below 2019 levels. Australian weekly payrolls continued to decline and would have declined even if Victoria were excluded from the data. On the other hand, Chinese industrial profits were reported to be up 19.6% compared to a year ago.

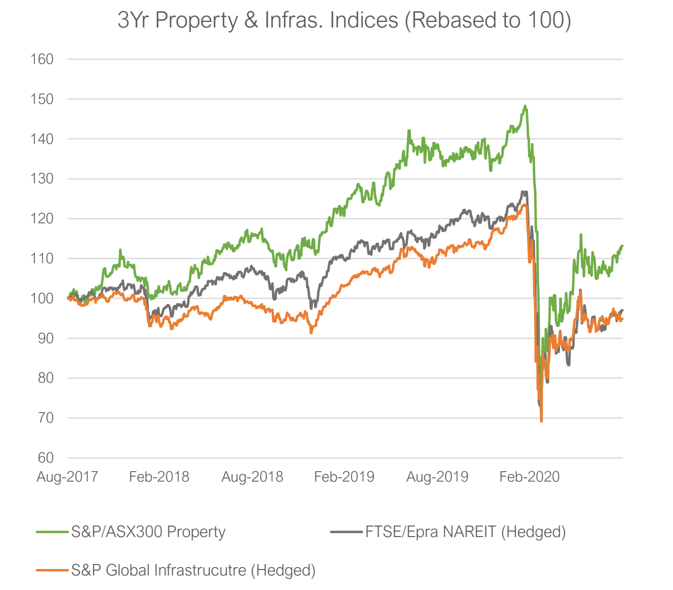
In other notable news, the Republican Party controversially held its National Convention on the lawns of the White House last week and returned the equally controversial Presidential candidate, Donald Trump. Japan's longest-serving Prime Minister and father of Abenomics, Shinzo Abe, will step down due to ill health. And shortly after concluding a small trade deal between the EU and US, EU trade Commissioner Phil Hogan resigned after it was reported that he breached coronavirus travel restrictions. The Irishman will no longer take part in Brexit negotiations. Meanwhile, former Australian PM and Brexit sympathiser, Tony Abbott, has been appointed to a new role as a trade adviser to the British government.

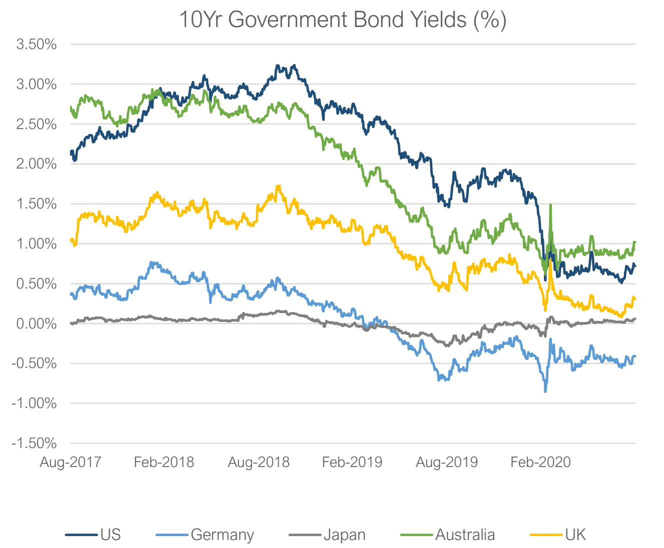
In this week's labor report, the US unemployment rate is expected to have fallen to the still very high level of 9.8% in August. Australia is expected to report a record current account surplus of A$13.0bn on Tuesday, the same day that the RBA meets. On Wednesday, Australia will report GDP figures, expected to show a decline of 6.0% in Q2

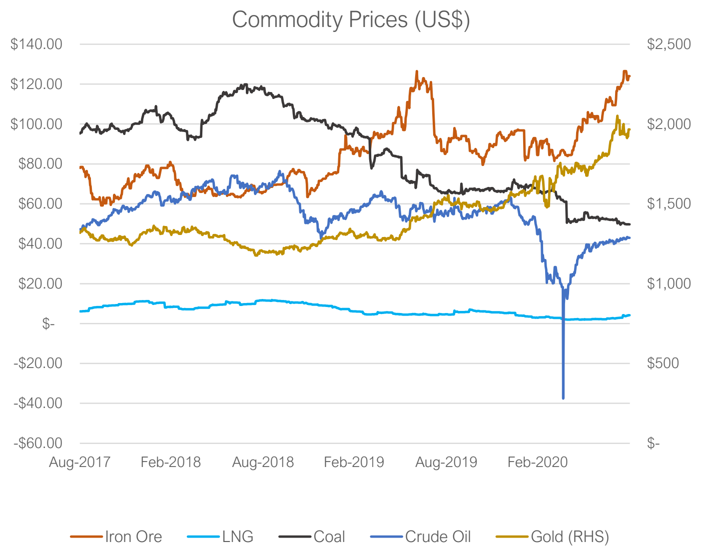
Correction: last week we wrote that Japanese Q2 GDP was an estimated 7.8%. It should, of course, have been -7.8%, as shown on the graphic.

Significant Upcoming Data:

	Monday	Tuesday	Wednesday	Thursday	Friday
Australia	Private Sector Credit; Melbourne Institute Inflation; Company Operating Profit; Inventories	RBA Meeting; BoP / Current Acc; Building Approvals; CoreLogic House Prices; Private Sector Houses; RBA Commodity Index; AiG Perf. of Manuf. Index; ANZ Roy Morgan Weekly Cons.Conf;	Q2 GDP	Trade Balance; AiG Perf. of Const. Index;	Retail Sales
US	Dallas Fed.Manuf. Activity;	ISM Manuf. Index; Construction Spending Wards Total Vehicle Sales	Fed. Beige Book; ADP Employment; Factory Orders; Durable Goods (Final); MBA Weekly Mortgage Apps.;	ISM Services; Trade Balance; Challenger Job Cuts; Unit Labour Costs; Non-Farm Productivity; Weekly Jobless Claims	Labor Report
Europe	German, Italian & Spanish CPI; Italian & Belgian Q2 Final GDP; Finnish Trade; Swiss & Dutch Retail Sales	Tier 2 Manuf. PMIs; Eurozone CPI; Eurozone, German, Belgian, Italian & Irish Unemployment; UK M4 Money Supply & Mortgage Apps.	Eurozone PPI; Spanish Unemp.; German Ret.Sales; UK Nationwide House Prices; UK BRC Shop Price Index; Norwegian Curr.Acc;	Tier 2 Services & Comp. PMIs; Eurozone Ret.Sales; Swiss CPI	German Factory Orders; French & Irish Curr.Acc.; Irish & Greek Q2 GDP; UK & German Construction PMIs
Japan	Consumer Conf.; Construction Orders;	Unemployment; Capital Spending; Company Sales/Profits; Vehicle Sales;	Monetary Base;		
China	Official PMI	Caixin Manuf.PMI		Caixin Services & Comp. PMIs	







Source: Bloomberg, S&P Dow Jones, MSCI, FTSE/EPRA, 30th August 2020

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