Outlook

Financial Update & Outlook

Autumn 2020

Welcome to the Autumn edition of Outlook, the quarterly newsletter aimed at keeping you up to date with wealth creation and protection strategies.

What an unbelievable month March was. We haven't experienced this level of economic malaise since the 1930's Great Depression nor have we seen lifestyles affected like this since World War II. Fortunately, most of us have not had to experience either of these extreme times.

The question a lot of investors asked was how could our market fall by 7% in a day? Not only Australia but the Dow Jones was down over 2,000 points at one stage. Bear in mind the Dow drop was off a base of 23,856 so bigger percentage daily drops have happened in the past.

The simple answer was the Coronavirus together with squabbling amongst the major oil producers OPEC and Russia produced worldwide uncertainty rarely seen before. This has affected demand for goods and services out of China killing activity worldwide.

But let us keep all of this in perspective. This temporary world-changing virus with short-term but serious economic implications plus this oil spat have created problems that will be overcome. Since then, markets have responded with April producing the highest monthly returns since 1988.

So how worried should we be? It has and remains a very worrying time with many uncertainties yet to evolve. The Australian government has responded by:

- Early access to superannuation
- Default minimum drawdown rates reduced by 50% for account-based pensions
- Reduced deeming rates for calculation of Centrelink pensions
- Up to two separate tax-free lump sum payments of $750
- Tax benefits for small businesses
- Increased payments to the unemployed

Information on all these schemes are readily available on government websites. The worldwide fiscal stimulus packages will provide a good prospect for growth that will power markets up later this year.

Any recession should be short-lived, provided the coronavirus is nailed in an acceptable period. Downturns are sometimes a byproduct of investing in the stock market but over the long term the market makes you richer than term deposits.

So how do investor's weather the storm? Depending on your time frame, stay in a diversified portfolio and look for advice from qualified people not financial journalists who have to produce a sensational story right now and not focus on potential news ahead.

FINPAC portfolios have a selection of investments consisting of shares in modern businesses that are typically better positioned than some others to operate digitally and remotely. Our portfolios benefit from having funds invested across selected fund managers who are specialists in their respective fields.

We endeavour to support our clients in these challenging times by keeping you informed and up to date every quarter on all changes.

Remember if you have any questions please contact the relevant advisor listed below. Alternatively, if you have any feedback on our updates or articles you would like covered please give me a call or send an email to **gricks@finpac.com.au.**

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market overview

The first quarter of 2020 saw global equity indices fall sharply following the outbreak of Corona Virus.

Global financial markets were rocked by the rapid spread of COVID-19, which was declared as a pandemic by the World Health Organisation on 11 March. The MSCI AC World Index fell 21.4% in USD terms during the quarter, the second sharpest fall (behind December 2008) since the creation of the index.

The losses would have been worse (falling 33.7% from quarter peak to trough) had it not been for the prompt and substantial policy response by governments and central banks to mitigate the economic impact from drastic social distancing policies.

Adding to the turmoil, the oil price experienced one of the largest ever falls with the Brent price plummeting 61% over the quarter as disagreements between Saudi Arabia and Russia led to the collapse of the OPEC agreement.

The Australian share market experienced its worst quarter since 1987, with the S&P/ASX 200 Index (Total Returns) falling 23.1%. Large falls were seen across all global equity markets, as the emerging COVID-19 pandemic saw many countries implement travel bans, industry shut-downs and social distancing measures. Australia was one of the worst performing markets in USD terms.

Commodity prices were generally weaker, with oil hit particularly hard by the twin impacts of lower global demand and a breakdown in supply controls from key producers. Iron ore has been the notable exception, holding up well in anticipation of Chinese stimulus. Looking at performance by sector, cyclicals underperformed and there was an overlay around balance sheets, with more leveraged companies being marked down.

Energy (-48%) was weakest, followed by A-REITs (-34%), Consumer Discretionary (-29%) and Financials (-28%). Health Care (+2%) was the only positive performer, with Consumer Staples (-3%) the next best.

Of stocks held by investors, the key negative contributors have been either directly impacted by policy measures to contain COVID-19, had perceived balance sheet weakness, or had oil exposure, or a combination thereof.

The main positive contributors to performance were unsurprisingly defensive holdings. Overweight positions in Coles Group performed very well. Supermarkets have been rare winners in the current environment, receiving a short-term sales boost from panic buying and a lift as people are forced to eat at home due to restaurant closures.

Coles also outperformed its key competitor Woolworths (-2%), with a material improvement in relative sales growth causing the market to reappraise the significant valuation premium it had placed on Woolworths.

“Unprecedented” is a word that most of us have probably heard more in the past few months than we would have ever wanted. Indeed, a search of the Australian Financial Review reveals that the word was used more than 330 times from mid-February to the end of March. And yet which other word would you select to describe the changed circumstances that have confronted investment markets over the past few months?

As investors we are faced with global economies which are suddenly facing one of the biggest quarterly declines in growth on record, an increase in unemployment that barely seems believable, fiscal and monetary stimulus that previously would have been unthinkable and then a bear market that has taken hold in an extraordinarily short time frame.

Overlay this with an attack on personal safety and wellbeing from an invisible foe and we begin to understand why “unprecedented” has been the word of choice.

By way of complete contrast, we only must step back six weeks to when global indices were printing all-time highs. We had been writing for some time that markets were extended and long overdue a pullback. Discussion with investors often turned to the absence of likely catalysts for a pull back, and it was difficult to argue the point.

Our view has always been that catalysts are near-impossible to pick. In these two respects our views have sadly proven correct. However, there is clearly no “back-slapping” on our part because in two other key respects our expectations to date have proven to be very much wide of the mark.

and preservation

Firstly, we were of the view that whilst a correction was likely, it should be reasonably shallow as we did not expect earnings to collapse like what happened in the Global Financial Crisis (GFC); global economies looked to be entering a firmer period following trade wars and the cessation of some monetary tightening. Under normal circumstances this would support corporate earnings.

Secondly, given the extreme valuations accorded to leading industrial stocks we were strongly of the view that the correction would be driven by the underperformance of this group of stocks, which have played such a big role in buoying markets to ever higher levels over many years.

Whether what we are living through is "unprecedented" can be debated but there is little doubt that we are faced with a set of circumstances that few if any of us have encountered. When markets were reaching new highs there were signs of "greed" everywhere and some caution was warranted.

The question a contrarian should now be asking is whether this "greed" has been replaced with an unnecessary degree of "fear" - have investors become overly cautious as we generally do when faced with great uncertainty?

In our view this is very much the case in respect of the exceptional valuations being placed on stocks that are perceived to offer "certainty"; particularly but not limited to the healthcare names.

As to the market itself there is a need for balance – a 30% decline is substantial, and this is probably not the time to be ultra-bearish. However, we are of the view that this is not your typical downturn and with capital raising pressures becoming evident a degree of caution is warranted.

COVID-19 and insurance policies

The novel coronavirus (COVID-19) has had a profound impact on our daily lives and it's become more important than ever that we take care of one another and support those that need us most.

For many Australians, the pandemic has placed a sudden and severe strain on your finances, so as the situation with COVID-19 continues to develop insurers have recognised the importance of supporting Australians through this unprecedented time and have introduced a range of options.

We want to support our clients who are facing hardship, so please contact us to discuss your individual situations. We recognise that this is not a one size fits all situation, and will approach insurers to get a solution that suits you.

Small and Medium (SME) business customers

For Business Packages, Commercial Motor and Individual Personal Accident renewals, insurers are maintaining renewal premiums at the same rate where the sum insured hasn't changed.

Deferral of premium payments for up to six months for small businesses experiencing financial hardships. Most insurers are offering small business customers the option to defer payment of their annual or monthly premium for up to six months.

This means you will continue to be covered by your existing insurance policy without needing to pay your annual or monthly premiums now.

Small businesses which need to close premises due to the impact of COVID-19 can maintain full insurance cover on the premises with no changes to premium.

'Laid up' cover is available for Commercial Motor policies where vehicles are no longer on the road.

For small business customers to take up this offer it will require you to contact us to make these arrangements for you with the insurers.

Life and Income Insurance customers

Firstly and most importantly all Australian life insurers that Finpac uses fully cover the Covid-19 virus, and will pay claims associated with the contraction of the disease.

There were media reports that some companies do not cover the virus for existing policy holders which was incorrect. Some insurers are adding some medical questions about the Covid-19 virus on new applications.

Most insurers have the option to pause your cover and premiums. This option allows for the suspension of cover for a period of up to three months at a time, for a maximum of 12 months. The insurer will automatically reinstate to the original level of cover without any additional underwriting assessment at the end of the agreed period.

Although premiums will not be payable, no claim will be paid for any event that occurs, or for which signs or symptoms became apparent or were diagnosed, while the cover is suspended,

Some insurers will allow a full premium holiday for periods of one or two months. This means that the full cover continues whilst premiums are suspended.

Landlords Insurance customers

We are finding that each insurer is taking a somewhat different approach to Rent Default claims. It seems the critical issue is abiding by the current Act and Tribunal instructions.

Some insurers are not varying the current way that rent default is treated. So the tenant would have to leave the property prior the end of the lease agreement with rent outstanding, or been legally evicted with rent outstanding for a claim to be paid.

Under of the hardship section, the lease would need to be terminated by a tribunal due to hardship, then the insurers may pay up to 6 weeks rent.

If your tenant makes an agreement with you this would be seen as a variation to the lease agreement so you would not be able to claim for the difference.

The current moratorium on evictions is simply a hold on eviction proceedings, so you would need to wait until the moratorium has been lifted to proceed with the eviction before a claim could be submitted.

Other insurers are showing some flexibility with the Rent Default claims. These insurers have temporarily removed the requirement for landlords to provide an eviction notice when making a claim for loss of rent.

Landlords are only required to provide proof of financial loss rather than a tenant eviction notice or intent to re-let when lodging a claim.

The insurer will generally provide cover in line with the terms and conditions of the policy, for a shortfall arising from a temporary rent reduction negotiated between a landlord and tenant during state and territory governments' moratoriums on residential tenancy evictions.

As the attitudes and processes of each insurer differ, it is critical that you contact us to discuss your individual circumstances before agreeing to rent reductions or rent holiday.

what's happening at finpac?

To protect the health and safety of our staff and their families we now have some staff working remotely.

You can still contact us on our regular numbers and emails are operating normally, so we'll still be able to assist.

The office is closed for all visitors. We will endeavour to keep our response times to our usual service standards.

FINPAC Financial clients please call 4772 5655

FINPAC Insurance clients please call 4771 5600

We thank you for your understanding during these difficult times and we trust that you stay safe and healthy.