No recovery until there is 'blood on the street'

Equities

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The sharemarket's comeback will be tested again this week as investors are forced to reconcile the optimism that has driven stocks off their COVID-19 lows with the reality of terrible economic data that saw Wall Street follow the local market sharply lower on Friday.

Just a day after Australian stocks sealed their best month since 1988, driven by accommodative monetary policy and governments easing containment measures to stem the economic bleeding, hopes of further gains were dashed in Friday's 5 per cent slide by the S&P/ASX 200, matched by a more than 600-point drop in the Dow Jones Industrial Average.

Fresh data revealing the economic toll inflicted by the pandemic is clashing with expectations of a quick or V-shaped economic recovery.

"You've had this view that once things open up, it'll be back to something like normal and I think the reality is probably starting to set in," said Schroders' head of multi-asset and fixed income, Simon Doyle.

"The data that we're starting to see flow through is now actually the data that's starting to pick out the shutdown of the economy. And you are starting to see it flow through in the US in terms of the production data, the labour market data and I think, even some of the earnings numbers are starting to pick it up."

> **More than ever this is a stockpicker's market – index funds in this period are not your best option.**
> Lachlan Hughes, Swell Asset Management

The week ahead will see US labour market data released, trade figures for the Australian economy and Chinese business activity, which all stand to test the resolve of investor confidence.

The US economy shrank at an annualised rate of 4.8 per cent in the March quarter, the worst result for the world's largest economy in more than a decade, and 80 basis points below the average expected by the market, it was revealed last week.

That was followed by figures released on Thursday that laid bare the blow to European economic activity, with measures of consumption and production for individual economies and the broader eurozone revealing a significant hole.

Domestically, Treasury warned of an economic shock worse than the Great Depression and the Australian Bureau of Statistics reported that a third of all households were financially worse off due to COVID-19.

While shares in the US fell over the final two days of trade last week, the sharp rebound in equities over the preceding weeks has pushed prices to levels considered historically expensive.

The companies that make up the S&P 500 trade at an average price-to-earnings (PE) multiple of 19.3 times on current earnings and 22 times forward earnings. That is significantly above the 10-year average for the US benchmark of 15.2 times, and more unusual because it's happening in the middle of a pandemic.

The ASX 200 by comparison, ended the week on a multiple of 16.8 times, which is still above its 10-year average of 14.5 times, but far more moderate than the US.

The Australian market greets the week close to 27 per cent below its February peak, whereas the S&P 500 is close to 16 per cent off its last high after rallying a massive 31 per cent from its March low.

"Even though we're managing the situation better, there's probably a bit more of a realistic pricing in the market here, whereas the US has probably got the biggest risk of a setback but the least risk premium for that occurring in pricing," Mr Doyle explained.

The investment manager expected sharemarkets to record further falls in future, with forthcoming economic data as well as corporate failures seen as the potential catalysts. "As some of these businesses actually really do start to get into trouble – we've seen it in airlines for example but there'll be other parts of the market that actually get into trouble – we think until you get a bit of blood on the street, that'll be when the low in markets will be.

"And at the moment, you're not really seeing that, it's all about central banks coming to the rescue yet again and 'it'll be right', the economy will restart and everything will be back to normal quickly."

While the outlook for many businesses and the economy remains highly uncertain, Swell Asset Management's chief investment officer Lachlan Hughes said the current environment represented an opportunity. "I think there's going to be a huge disparity between companies that will benefit from this and companies that will not benefit from it," he said.

"More than ever this is a stockpicker's market – index funds in this period are not your best option."

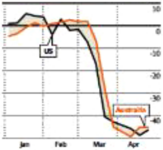
Mr Hughes cited the acceleration of a shift toward digitisation as an example of a theme that will drive share price performance for businesses that are positioned to capture the shift.

Microsoft and Amazon are standouts to him, as well as locally listed companies with effective online retail offerings. Amazon sank 7.6 per cent on Friday after reporting its earnings on Thursday and guiding to a quarterly loss.

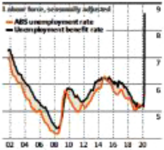
Friday's 5 per cent slide by the S&P/ASX 200 was matched by a more than 600-point drop in the Dow Jones Industrial Average. PHOTO: AP

The week ahead

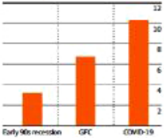
Economic activity tracker (% change)



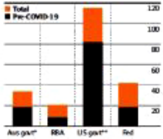
JobSeeker v unemployment (%)



Cumulative discretionary fiscal measures (% GDP)



Govt debt and RBA assets to 2021 (% GDP)



*Net govt debt. **Debt held by public, inc $1.5b additional stimulus. SOURCES: WESTPAC, AMP CAPITAL, ANZ

MONDAY	TUESDAY	WEDNESDAY	THURSDAY	FRIDAY
AU ANZ job ads Apr, Building approvals Mar	**AU** Payroll jobs and wages (weekly), RBA meeting	**AU** Retail sales Mar/1Q	**AU** Trade balance Mar	**AU** National cabinet meeting on restrictions rollback plan, RBA statement on monetary policy
EU Eurozone manufacturing PMI Apr	**US** ISM non-manufacturing index Apr	**NZ** unemployment rate 1Q	**China** Trade balance Apr, Caixin services PMI Apr	**US** non-farm payrolls and unemployment rate