OUTSIDE THE FLAGS

The Pizza Pandemic

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The global pandemic wrought by COVID-19 has created great uncertainty among policymakers, investors, workers and consumers, but it's worth noting that its repercussions on the economy and the share market have not been all in one direction.

Yes, the Australian share market is still down year-to-date (about 9% at time of writing), but it's more than 30% above the lows of mid-March. Most other markets have staged similar recoveries, with the US being the standout—recently hitting its highest levels on record.

A common question from investors is how can the market be moving up when the economy is going in the other direction? The Australian statistician, for instance, recently reported a record quarterly slump in GDP, confirming the nation's first recession in three decades.[1]

The answer to that question is twofold. Firstly, share markets are a forward-looking mechanism. That means they're not so much taking the temperature of the economy and earnings as of now, but where they *think* things will be next year and the years after that. These estimates represent the collective estimate of all participants, whether optimistic or pessimistic.

While governments have forced parts of the country into lockdown, closed borders and directed folk to stay home, the Reserve Bank of Australia recently said the downturn has not been as severe as expected earlier and a recovery is underway. Even so, the central bank and other institutions have warned that the future path of the recovery is highly dependent on containment of the virus and the rolling out of an effective vaccine.[2]

Of course, that view may change if the news gets worse from here. But we can't predict that. Conversely, the situation may start to look better than what is priced into date, in which case the market may adjust higher in response. Who knows?

The second point to remember is that the pandemic hasn't crunched the economy entirely and that stocks don't move in lockstep. In other words, while many firms have been hit hard by the lockdowns, others have prospered. Let's look at a few examples:

Unsurprisingly, Australia's list of worst performing stocks in 2020 so far is dominated by firms exposed to the slump in air travel (booking agents, airlines, holiday parks), the plunge in advertising (media companies) and the disruption to rents (real estate investment trusts).

Oil and gas explorers like Woodside Petroleum have also been hit as crude prices have fallen amid a slump in demand for their products, while traditional brick-and-mortar retailers like Myer have suffered from the change to a stay-at-home economy.

But while consumer spending has slowed overall, it has not stopped altogether. Instead, the *way* we are spending has changed in the face of the pandemic. And the impact of that transformation is evident among the best performing stocks of the year.

Pure online retailers like Kogan, which recently reported a near 70% increase in pretax earnings, have benefited from consumers shopping from their lounge rooms for computers, phones and home sports equipment, as has the hybrid retailer JB Hi-Fi.

People may not be going out to dine, but that's offset by a significant increase in home-delivered food. One of the top performing stocks on the Australian market this year has been Domino's Pizza, whose share price recently hit record highs after a bumper earnings result.

But it's not just online retailers and takeaway food companies that have been doing well this year in the face of COVID-19. Some materials stocks such as iron ore producer Fortescue Metals Group and gold miners have also outperformed.

This being a health crisis, it's also not surprising that healthcare stocks have done well. The healthcare sector is up about 5% year to date, with leading gainers including cellular therapy company Mesoblast and protective equipment maker Ansell.

Exhibit 1
ASX Stock Winners and Losers 2020
Total Return YTD, 15 Sep 2020

ASX Stock Winners and Losers 2020	Total Return YTD, 15 Sep 2020
Afterpay (transaction and payment services)	158.95%
Kogan (internet and mail order)	156.18%
Mesoblast (biotech & medical research)	130.77%
NEXTDC (IT and cloud computing)	89.59%
Fortescue Metals Group (iron ore)	73.10%
Saracen Minerals (gold)	64.65%
Domino's Pizza Enterprises (takeaway food)	58.10%
Ansell Ltd (medical equipment)	30.37%
JB Hi-Fi (computer and electronics retailer)	29.44%
Sonic Healthcare (medical laboratories)	15.93%
S&P/ASX 300 (total return)	–9.46%
Stockland Corp (residential REITs)	–16.48%
Tabcorp Holdings (casinos)	–21.93%
Sydney Airport Holdings	–34.64%
Mirvac Group (diversified REITS)	–35.45%
Qantas Airways	–44.59%
Woodside Petroleum	–44.75%
Webjet (travel agents)	–55.21%
Myer Holdings	–57.95%
Flight Centre (travel agents)	–67.07%
Southern Cross Media	–75.42%

Past performance is not necessarily indicative of future performance.

Total Return includes the reinvestment of dividends. (Source: Bloomberg).

What are the lessons from all of this for everyday investors? Firstly, unless you can predict news (ask yourself who predicted a global pandemic at the start of this year?), it's impossible to predict which parts of the market will do well and which will do poorly.

That means your best strategy is to diversify—hold stocks across different sectors and countries, across large stocks, small stocks, low relative price stocks and profitable stocks to ensure that you'll always be invested in the winners somewhere.

The second lesson is to work *with* the market rather than against it. Today's news—GDP, inflation, earnings, geopolitical developments—is already reflected in prices. It's too late to do anything about it. The market looks forward, not backward.

The final lesson is to exercise discipline. Things can change quickly, as we saw from late March when one of the fastest and most dramatic downturns in stocks was followed by one of the fastest and most dramatic recoveries. No-one can pick it, so stay invested in the plan your advisor has designed for you. It's less stressful and easier to stick with if you stop speculating.

Keeping up with the news is important as a citizen. Using news to navigate your way around financial markets is not such a good idea. Markets will do what they do, which means your best bet is to focus on all the things you can control—like pizza for dinner for instance.

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1. Australian National Accounts, June Quarter, 2020, Australian Bureau of Statistics.
2. Statement by Philip Lowe: Monetary Policy Decision, *Reserve Bank of Australia*, 1 September 2020.