Month in Review

ISSUE DATE: 10-11-2017

Market Moves — as at 31•10•2017

RETURNS (% P.A.)	1 MTH	3 MTH	6 MTH	1 YR	3 YR	5 YR	10 YR
AUSTRALIAN EQUITIES							
S&P/ASX 200 ACCUMULATION INDEX	4.01	4.73	2.01	16.13	6.94	10.30	3.20
S&P/ASX SMALL ORDINARIES ACCUMULATION INDEX	6.02	10.32	10.58	14.58	10.48	6.05	-1.35
GLOBAL EQUITIES							
MSCI WORLD TR INDEX (AUD)	4.29	8.75	7.10	22.53	13.81	19.17	6.70
S&P 500 TG INDEX (AUD)	4.72	9.08	6.41	22.70	15.93	22.35	9.57
FTSE 100 TR INDEX (AUD)	3.13	7.80	6.24	20.97	6.93	11.74	2.30
MSCI EMERGING MARKETS NET TR INDEX (AUD)	5.92	9.74	13.27	25.49	10.62	11.36	2.52
REAL ESTATE INVESTMENT TRUSTS (REITS)							
S&P/ASX 300 A-REIT (SECTOR) ACCUMULATION INDEX	2.25	4.39	-1.47	8.59	10.95	12.54	-0.13
FTSE EPRA/NAREIT DEVELOPED NET TR INDEX (AUD HEDGED)	0.18	0.33	2.25	6.92	6.22	10.30	3.25
FIXED INTEREST							
BLOOMBERG AUSBOND COMPOSITE 0+ YR INDEX	1.09	0.77	1.28	1.64	3.94	4.12	6.18
BLOOMBERG AUSBOND BANK BILL INDEX	0.15	0.43	0.87	1.76	2.11	2.40	3.72
BARCLAYS GLOBAL AGGREGATE TR INDEX (AUD HEDGED)	0.47	0.99	1.79	1.92	4.60	5.08	7.25

Data source: Bloomberg & Financial Express. Returns greater than one year are annualised.
Commentary regarding equity indices below references performance without including the effects of currency (unless specifically stated).

Australian equities

The Australian market followed the world higher in October, after a disappointing run of negative and flat returns. The ASX 200 Accumulation Index returned 4.01%, led by the Information Technology (+8.75%) and Energy (+6.50%) sectors. Construction management software provider Aconex (+27.32%) led the IT gains, but is still struggling to recover from a series of disappointing updates since the start of 2017. Santos boosted Energy sector gains, beating expectations on production, revenue and costs, driven in large part by its Gladstone LNG operations. But it was Blackmores (+35.36%) that topped the leaderboard in October, posting a 28% rise in direct China sales, with the Chinese government having affirmed its commitment to the pilot of cross border e-commerce.

Telecommunications (+2.38%) was the weakest performing sector, with gains from Vocus (+20.50%) and TPG (+11.53%) offset by Telstra’s average performance (+1.43%). Australia’s small cap shares had a good month, with the S&P/ASX Small Ordinaries Accumulation Index posting a 6.02% return, outperforming its larger peers but still underperforming on a 12-month basis.

Global equities

In the US, the S&P 500 gained 4.72% in AUD terms as positive data, including an above-expectations GDP reading, pushed markets higher. On the one year anniversary of President Trump’s election victory, the market is still rallying and volatility is lower than ever. The VIX, or so-called ‘fear gauge’, posted its lowest average monthly level in October (in a dataset stretching back to 1986). Information Technology shares (+10.27%) delivered the greatest gains, with Adobe Systems (+20.16%) beating earnings expectations and making market inroads with cloud-based software. PayPal (+15.97%) also rocketed higher, beating revenue and EPS expectations and raising its full-year outlook. Venmo, one of PayPal's most popular payment methods, processed US $9 billion in payments in Q3 (nearly doubling year-on-year).

Globally, the MSCI World TR Index gained 4.29% in AUD terms, supported by US and Asian shares. Japan’s Nikkei gained 9.63% as the index reached its highest point since 1996, while China’s Shenzhen CSI 300 Index was up 6.98%. The Euro Stoxx 600 Index rose 2.83%, supported by Resources (+6.15%) and IT (+6.07%) sectors. German carrier Lufthansa (+17.32%) was a major gainer, and has already carried more passengers in 10 months than in the whole of 2016 (with some help from Air Berlin’s implosion). In the UK, the FTSE 100 Index rose 3.13%, with market participants following Brexit negotiations closely. The MSCI Emerging Markets Index rose 5.92%, supported by Chinese and Indian markets, as well as a bounce back in South Korea’s KOSPI (+10.37%) as tensions with North Korea reached something of a détente.

REITs

The S&P/ASX 300 A-REIT Accumulation Index returned 2.25% in October, led by residential property manager Charter Hall (+8.01), which hit an all-time high of $5.80. Commercial specialist Propertylink Group (+7.53%) added to September’s gains, helped along by buying from investment bank Citi, which has been buying shares for a mystery international investor. More pain was felt for retail-focused REITs Westfield (-0.89%) and Vicinity Centres (-0.38%), both of which have lost a third of their value since July 2016.

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Global REITs were slightly lower in October, with the S&P Global REIT NTR Index down 0.44% (in AUD hedged terms), while the FTSE EPRA/NAREIT Developed NR Index managed a modest gain of 0.18%. In the US, there were few winning sectors through October, with Data Centres coming under pressure but still maintaining the highest YTD return. Regional Malls and Shopping Centers continued their downward trend in October, and have lost significant value through the year. Overall, low volatility remains an attraction for REITs globally, with only gradual rises in interest rates.

Fixed income

Yield movements were mixed in October, with US sovereign yields slightly higher but most developed markets easing. So far bond markets have been mostly steady as the Fed begins its balance sheet 'normalisation', helped perhaps by the appointment of Jerome Powell to head the Fed. The US 10-year Treasury yield rose from 2.33% to 2.38%, peaking at 2.46% to hit a seven-month high. The return on US corporate investment grade bonds was 0.42% in October with the index closing at another all-time high, while US high-yield debt returned 0.49%, ending the month at near-record levels. The BofA Merrill Lynch US High Yield OAS contracted in September from 3.56% to 3.51% to hit a post-GFC low, with volatility still absent from financial markets.

Global bonds, measured by the Barclays Global Aggregate TR Index, returned 0.47% in October (in AUD hedged terms), with developed market indices still close to their all-time highs. The Ausbond Composite Index returned 1.09%, with government bonds returning 1.17% and corporate debt up 0.98%. The Australian 10-year Treasury yield rose from 2.84% to end the month at a low of 2.67%, further down on its March peak of 3.05%. The UK 10-year Gilt yield was lower in October, moving from 1.36% to 1.33%. In November, the Bank of England raised the Bank Rate for the first time in ten years, from 0.25% to 0.50%. The German 10-year Bund yield fell from 0.46% to 0.36%.

ASX 200 Share Movements

S&P/ASX 200 Share Performance for the Month of October

BEST PERFORMERS		WORST PERFORMERS	
BLACKMORES	35.36%	HT&E	-15.78%
GALAXY RESOURCES	32.69%	FLETCHER BUILDING	-12.06%
A2 MILK CO	30.03%	FORTESCUE METALS GROUP	-9.73%
IPH	28.85%	LENDLEASE GROUP	-9.54%
ACONEX	27.32%	SIGMA HEALTHCARE	-8.49%

S&P/ASX 200 Share Performance for the Year to October

BEST PERFORMERS		WORST PERFORMERS	
A2 MILK CO	335.43%	MAYNE PHARMA GROUP	-58.23%
COSTA GROUP HOLDINGS	122.88%	SIRTEX MEDICAL	-49.96%
QANTAS AIRWAYS	107.32%	VOCUS COMMUNICATIONS	-48.85%
GALAXY RESOURCES	97.14%	SIGMA HEALTHCARE	-40.15%
MONADELPHOUS GROUP	89.33%	HT&E	-33.44%

Economic News

Australia

At its November meeting the RBA left the **cash rate** on hold at 1.50%, noting that monetary policy in other advanced economies is becoming less accommodative. The bank's forecast for growth is largely unchanged, with GDP growth expected to pick up to 3.0% over the next few years. Supporting this view is the continued improvement in business conditions and the employment situation, although low wages growth remains a sticking point and is dampening consumption. Inflation is also low, due to suppressed wages growth and competitive pressure, while headline CPI is being boosted by higher prices for tobacco and electricity.

Australia's labour market continues to improve, with 19,800 seasonally adjusted jobs added in September, which included 6,100 full-time and 13,700 part-time positions. The **unemployment rate** fell 0.1 points to 5.5%. The participation rate remains more or less steady at 65.2%, and has been rising consistently in trend terms throughout 2017. The number of unemployed persons looking for full-time work fell by 1,200 to 224,400, and monthly hours worked rose 11.2 million to 1,718.2 million hours.

The **AIG Manufacturing Index** fell 3.1 points in October to 51.1. The index shows a significant deceleration in growth since August, when the index hit 59.8 (its highest value since May 2010). Major sub-indices contracted, including production, which plunged 8.4 points to 48.4 (indicating contraction for the first time

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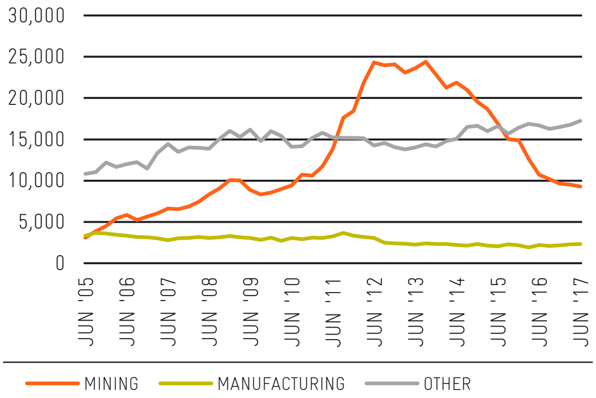
since August 2016). New orders fell 0.8 points to 55.1, sales inched 0.4 points lower to 51.0, exports moved into contraction, falling 2.5 points to 48.7, and inventories fell sharply by 9.1 points to 42.6.

Business investment ($ million)



Source: ABS

Retail turnover rose a very modest 0.1% in September, with department stores continuing their comeback, growing 2.1%. The major food retailing sector rose 0.6%, while cafes and restaurants were also higher by 0.3%. Detracting from an already disappointing month was a fall of 0.4% in household goods retailing, which is in danger of missing the pre-Christmas bump. It was the third consecutive month of disappointing retail figures, following falls of 0.5% in August and 0.2% in July.

Contrasting with September's woeful retail numbers, consumer sentiment appeared to turn a corner in October. The Westpac Melbourne Institute **Index of Consumer Sentiment** rose 3.6% to 101.4 from 97.9 in September. This is the first time that optimists have outnumbered pessimists since November 2016. While confidence is still not especially strong, with family finances a clear weak spot, respondents were buoyed by reports of further economic improvement and job gains.

Australia's **balance on goods and services** rose a seasonally adjusted $872 million to post a surplus of $1,745 million in September. Exports of general merchandise rose $604 million, non-rural good rose $599 million, and metal ores and minerals added $584 million. On the debits side, imports of consumer merchandise grew $214 million and consumption goods rose $191 million. Net exports of non-monetary gold rose by $217 million.

Global

The advance estimate of **US Q3 GDP** indicated real growth of 3.0%, similar to Q2's growth of 3.1% and well ahead of the expected 2.5%. While subject to further revision, the result was seen as positive by the market, speeding up the rally through the rest of the month. Consumer spending grew by 2.4%, which, although below recent trends, has held up well against the natural disasters that hit the US during the quarter.

The **ISM manufacturing PMI** moved lower in October from 60.8 in September to 58.7, but remains firmly in expansion. Some manufacturers reported shortages in the wake of hurricanes Harvey and Irma, which may explain the drawdown in inventories, but overall the impact appears minimal. Others reported strong incoming orders, mainly due to recovery efforts. Most sub-indices were down on the previous month, including new orders (-2.1 to 58.7), production (-1.2 to 61.0), employment -0.5 to 59.8), inventories (-4.5 to 48) and prices (-3.0 to 55.0).

Non-farm payrolls rose 261,000 in October, bouncing back after drop of 33,000 in September as the US was hit by major storms and hurricanes. The unemployment rate edged down by 0.1 points to 4.1%, and the number of persons employed part time for economic reasons declined by 369,000 to 4.8 million. The largest employment gains came from food services and drinking places (+89,000), which was hardest hit during the hurricanes, losing 98,000 in September. The broader U-6 measure of unemployment, which includes discouraged workers and those marginally attached to the labour force, fell further in October from 8.3% to 7.9%.

US CPI figures rose 0.5% in September on a seasonally adjusted basis and 2.2% on an unadjusted y/y basis. Gasoline prices jumped 13.1% after rising 6.1% in the previous month. All items less food and energy rose 1.7% y/y, driven predominately by a 3.2% rise in shelter. The core PCE index – the Fed's preferred measure – was steady at an annual 1.3%, down from the more promising level of 1.9% reached at the start of the year and now well below the 1.7% forecast for 2017.

Turning to Europe, **euro area GDP** grew by 0.6% in Q3 according to October's preliminary flash estimate, bringing growth over the past 12 months to 2.5%. Growth across the 19 eurozone countries has improved steadily over the past year, and the recovery has also become more broad-based, both across different countries and sectors. **Euro area inflation** is expected to be 1.4% p.a. in October, down on September's reading of 1.5%. Core inflation (excluding energy, food, alcohol and tobacco) also declined, falling from 1.1% to 0.9%.

Euro area unemployment was down in September from 9.0% in August to 8.9%. The lowest rates were recorded in the Czech Republic (2.7%), Germany (3.6%) and Malta (4.1%). The highest rates are still evident in Greece (21.0%), which has fallen gradually from over 23% since the start of 2017, and Spain (16.7%), which has experienced a similar gradual decline. Greece's primary surplus is likely to rise to 3.9% of GDP next year as the country exits the latest eurozone bailout program and returns to market financing.

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In the wake of September's **German federal election**, talks continue between Merkel's CDU and other minor parties for the formation of a so-called Jamaican collation with with the conservative CSU, liberal FDP and Greens. Discussions have covered everything from security, immigration, refugees, the digital economy, climate change, and social policy. Three weeks into negotiations, and it appears Merkel is close to piecing together a workable majority. But it won't be easy. In one corner, the Bavarian-based CSU is calling for caps on immigration. In the other, the Greens are calling for an end to petrol-powered cars by 2030.

China's GDP recorded growth of 6.8% in Q3 2017, down from 6.9% in Q2 but more or less in line with the market's expectations. The state-owned China Daily was quick to place its customary positive spin on the situation, but noted the necessity of structural, supply-side measures – including market-based reform – to place growth on a sustainable footing. **China's official PMI** survey was lower in October, down from 52.4 to 51.6 and slightly lower than the expected 52.0. The Caixin PMI, which surveys smaller, private manufacturers, was steady at 51.0 and in line with expectations.

In other **emerging markets**, Brazil's unemployment rate fell from 12.6% to 12.4% in October, steadily falling from a peak of 13.7% in April. India's inflation rate was steady in October at 3.3%, with the Reserve Bank of India holding rates steady at 6.00%. The RBI has recently taken a sledge-hammer approach to the corporate debt problem, releasing a list of 40 companies to the country's state-owned banks, ordering them to resolve bad debts. In Russia, inflation moderated from 3.0% to 2.7%, while Q3 GDP was 2.4%.

Commodities

Commodities were able to find new legs in October, but with mixed results. After taking a big hit in September, Nickel rocketed 17.1% in October, with higher exchange prices pushing up physical premiums. Copper was also higher, gaining 5.5%, as was Zinc (+3.3%) and Aluminium (+2.8%), while Tin (-6.3%) and Lead (-2.9%) were lower. Gold was down by 0.65% through October, pushing to a high of US $1,303.82/oz before closing the month at $1,271.45.

The price of iron ore delivered to Qingdao in China fell 5.7% in October from US $62.05/t to $58.52, down from its recent August high of $78.91. In oil markets, the Brent spot price gained 7.8% from US $57.02/b to $61.35, and WTI rose 5.2% from $51.67/b to $54.36.

Currencies

The AUD was lower over the three months to October, falling 3.57% in trade-weighted terms and down against major currencies. The AUD has fallen 4.0% against the USD over three months, building to a high of 0.8077 in September to end October at 0.7662. The AUD has fallen against the EUR (-2.6%), JPY (-1.2%) and GBP (-4.6%), but has appreciated against the NZD (+5.2%).

The US Dollar Index has gained 1.8% over the three months to October, with the currency bottoming out in September and showing signs of moving higher as investors watched the US Senate's tax cut proposal closely. The USD has gained against the EUR (+1.4%), JPY (+1.0%), GBP (+0.9%) and CHF (+2.9%).

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