Month in Review

ISSUE DATE: 8-03-2016

Market Moves — as at 29•02•2016

RETURNS (%) P.A.	1 MTH	3 MTH	6 MTH	1 YR	3 YR	5 YR	10 YR
AUSTRALIAN EQUITIES							
S&P/ASX 300 ACCUMULATION INDEX	-1.72	-4.55	-3.83	-13.45	2.88	4.61	4.32
S&P/ASX SMALL ORDINARIES ACCUMULATION INDEX	0.95	-0.46	6.07	-3.56	-1.41	-3.17	0.41
GLOBAL EQUITIES							
MSCI WORLD ACC INDEX WITH GROSS DIV (A$)	-1.66	-7.14	-5.35	-2.26	19.36	13.23	4.80
S&P 500 COMPOSITE ACCUMULATION INDEX (A$)	-1.10	-5.23	-1.66	2.81	24.87	18.23	6.86
FTSE100 ACCUMULATION INDEX (A$)	-1.91	-9.24	-9.98	-9.81	12.07	8.35	2.34
MSCI EMERGING MARKETS FREE W/GROSS DIV (A$)	-1.13	-7.59	-9.13	-16.05	3.05	1.86	2.55
REAL ESTATE INVESTMENT TRUSTS (REITS)							
S&P/ASX 300 A-REIT ACCUMULATION INDEX	2.81	7.98	9.73	6.56	14.31	14.81	2.11
FTSE EPRA/NAREIT DEVELOPED NR INDEX HEDGED A$	-0.38	-3.35	2.28	-5.65	8.14	9.96	4.65
FIXED INTEREST							
BLOOMBERG AUSBOND COMPOSITE 0+ YR INDEX	1.03	2.61	2.27	2.96	5.39	6.82	6.35
BLOOMBERG AUSBOND BANK BILL INDEX	0.18	0.57	1.11	2.25	2.59	3.28	4.47
BARCLAYS GLOBAL AGGREGATE INDEX HEDGED $A	1.09	2.66	4.16	4.36	6.05	7.62	7.58

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

Australian equities

Australian equities were officially in bear market territory in February, with the S&P/ASX 200 Index down more than 20% since its April 2015 highs. Australian shares, as measured by the S&P/ASX 300 Accumulation Index, were down -1.72% in February, posting a month-end annual return of -13.5%. The main drags on the Index came from Telecommunications (-5.47), Information Technology (-5.46) and Financials (-5.32). Resources and Materials recovered ground in February, adding 7.52% and 9.12% respectively, following large declines in January. The Industrial sector continued its high performance run, adding 5.84% in February.

Growth fears continued to be reflected in Australia's 10-year Treasury yield, which fell from 2.64% to 2.40% during the month. The Australian dollar strengthened only slightly to AUDUSD 0.714 after dropping below the 0.70 threshold earlier in the month.

Global equities

Continued financial market volatility reflected a high degree of uncertainty in commodity markets, despite an apparent stabilisation in oil prices. Slowing growth in China and emerging market economies was again the main source of this uncertainty, with the focus on structural weaknesses and divergent economic cycles intensifying. China's February manufacturing PMI figures were below expectations, with the official indicator dropping to 49.0 – below the median survey figure of 49.4. The People's Bank of China (PBOC) resumed its easing cycle at the end of February, cutting the reserve requirement ratio for banks by 50bps to 17%, injecting an estimated US $100b in long-term cash into the economy.

Saudi Arabia, Russia, Venezuela and Qatar reached an historic agreement to cap oil production at mid-January levels, which helped to rally oil prices in mid-February. However, doubts remain about whether this will have a tangible or lasting impact on global oil production. Financial markets responded positively to the deal, with the S&P 500 Index gaining 5.34% during the week, although this was short-lived, with major indices remaining mostly flat to the end of the month.

The MSCI World ex Australia NR Index lost -1.70% in February, with European and Japanese shares the largest contributors to global equity falls. The S&P 500 Index finished down -0.41% as positive retail and manufacturing data helped to stem losses. In the UK, the FTSE 100 Index fell -2.41%, and in Europe the DAX tumbled -3.09% despite positive manufacturing and employment data at the start of the month.

In Asia, the Nikkei 225 Index fell -8.51% as Japan's Q4 GDP returned to negative territory, shrinking -0.4% over the quarter and missing expectations. The Shanghai Shenzhen CSI 300 Index fell -2.33%, and the Hong Kong Hang Seng Index fell -2.90%.

REITs

The S&P/ASX 300 Property Accumulation Index retuned 2.81% in February, outperforming the S&P/ASX 300 Index, which returned -1.72%. Melbourne and Sydney have continued to drive earnings growth from offices, while residential real estate is slowing from record volumes, with prices flat in the two largest cities. Concerns remain among investors about the perceived risk associated with high A-REIT valuation multiples compared to the broader share market, which may be the result of yield chasing or rising valuations of underlying assets.

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Globally, REITs returned 0.66% over the month of February in USD terms. Similarly, the FTSE EPRA/NAREIT Developed NR Index (AUD Hedged) lost -0.38%. In the US, REITs were down -0.29%, with positive performance in mortgage REITs largely offsetting decline in the equity REIT sector. US REIT performance is reflective of broader market behaviour, but could also signal a plateauing real estate investment market.

Fixed interest

The sharp decline in risk appetite at the start of 2016 has continued, with volatility in financial markets reflecting uncertainty in global growth and commodity prices. Softer economic growth forecasts have pushed out expectations for a Federal Reserve rate increase. Weakness in Europe has placed renewed pressure on the ECB to expand its asset purchase program and cut its deposit rate further into negative territory.

Volatility has benefited government bond investors, with the Barclays Capital Global Treasury TR Index up 1.40% in February in AUD terms. Monthly returns on global corporate and high yield debt were 0.70% and 0.78% respectively. The current attractiveness of government bonds must be weighed against the possibility of further monetary easing from central banks, including experimentation with negative rates. As pressure intensifies on monetary authorities, government bond yields may slide further. Around 27% of global government bonds are yielding below 0%, while 65% are yielding less than 1%.

Government bond yields experienced further compression in February, with the US 10-year Treasury yield falling from 1.92% to 1.74%, the Australian 10-year Treasury yield falling from 2.64% to 2.40%, and the German 10-year Bund yield falling from 0.32% to 0.11%. Japan's 10-year bond yield went negative in February following the adoption of negative interest rates at the end of January, with the Japanese 10-year Treasury yield falling from 0.10% to -0.06%.

ASX 200 Stock Movements

S&P/ASX 200 Stock Performance for the Month of February

BEST PERFORMERS		WORST PERFORMERS	
MINERAL RESOURCES	55.26%	OXFOREX GROUP	-38.94%
BEACH ENERGY	41.33%	PROGRAMMED MAINTENANCE SERVICES	-34.83%
NEWCREST MINING	35.87%	ISENTIA GROUP	-23.86%
WHITEHAVEN COAL	34.15%	VILLAGE ROADSHOW	-23.38%
OZ MINERALS	33.69%	COVER-MORE GROUP	-23.04%

S&P/ASX 200 Stock Performance for the Year to February

BEST PERFORMERS		WORST PERFORMERS	
BLACKMORES	252.84%	SLATER & GORDON	-91.74%
EVOLUTION MINING	121.49%	LIQUEFIED NATURAL GAS	-82.96%
APN OUTDOOR GROUP	105.33%	WHITEHAVEN COAL	-65.84%
PACIFIC BRANDS	91.58%	AWE	-60.89%
BURSON GROUP	85.58%	ORIGIN ENERGY	-58.53%

Economic News

Australia

Unemployment rose unexpectedly to 6.0% in January, up from 5.8% in December 2015, with the loss of 32,200 seasonally adjusted jobs. The participation rate remained steady at 65.2% and monthly hours worked increased 10.9 million hours. The largest increases in the unemployment rate were in Queensland, New South Wales and Victoria, and unemployment remains highest in South Australia (6.8%) and Tasmania (6.5%) despite modest falls in January. The rise in unemployment came as a surprise to the market, casting doubt on the state of economic recovery and placing pressure on the Reserve Bank. Consumer sentiment bounced back in February following a fall of 3.5% in January.

The Westpac Melbourne Institute Index of Consumer Sentiment rose 4.2% in February, moving up to 101.3 points. Job market confidence remains a key determinant of consumer spending, however the broader economic environment remains relatively benign. While in January consumers were responding to sharp falls in shares and commodities, lower oil prices have translated into lower prices at the pump, providing a boost to disposable income. Although volatility remains an issue and lower equity values have had a negative wealth impact on households, consumer sentiment remains in good shape.

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January retail sales rose by 0.3% m/m, below the consensus expectation of 0.4%. Although only modestly higher than the December outcome, which was relatively unchanged, there were positive signs in household goods (1.0%), cafes (1.0%) and the 'other retail' segment (1.4%). Contractions in food retailing (-0.2%) and department stores (-1.3%) dragged down the sector.

The Reserve Bank of Australia kept rates on hold in the start of February, with the cash rate unchanged at 2.00% since cutting by 25bps in May 2015. The Bank drew attention to slower than expected global growth, including moderating growth in China, as well as heightened volatility and substantial declines in commodity prices. Inflation remains low, giving the Reserve Bank some room to move if required. Headline inflation for December 2015 was 1.7% y/y, slightly higher than previous months, but still below the Reserve Bank's target range. Even core inflation, which excludes volatile items, remains relatively low at 2.1%.

Australia's trade deficit closed to $2.9bn in January 2016, a $0.6bn improvement on December's deficit of $3.5bn. A weaker Australian dollar continued to constrain imports, with significant falls across intermediate, capital and consumption goods. Exports rose overall by $260m, despite a significant fall in rural goods.

Global

Data released for the US in February were mostly positive. The ISM Manufacturing Index beat expectations in February, rising from 48.2 to 49.5. Non-manufacturing PMI missed, printing at 53.4, down slightly from 53.5 in January. Non-farm payrolls were strong in February, rising 242,000 – exceeding the 172,000 jobs added in January and beating the market's expectations by more than 50,000. US unemployment remained steady at 4.9%, in line with the Federal Reserve's estimate of the long-run rate. Retail sales in the US were another source of positive data, growing 0.2% in February (versus a forecast value of 0.1%). Consumer confidence was down, however, falling from 98.1 in January to 92.2 in February.

The return to full employment has been accompanied by continued economic expansion, with US GDP recording growth of 1.0% in Q4 2015. US price growth also pointed to expansion, with core inflation rising to 0.3% in January. While inflation remains below the Federal Reserve's objective of 2%, the low pace of inflation reflects the earlier steep declines in oil and other imported goods, as well as US dollar declines. Once energy prices stop falling and the labour market strengthens, the Federal Reserve expects US core inflation to rise.

Negative interest rates were the distinctive theme in February. In her testimony to Congress, Federal Reserve Chair Janet Yellen said the bank is considering negative rates as a potential response to deteriorating economic conditions, sparking renewed debate about the effectiveness of negative interest rate strategies. In January, the Bank of Japan followed the ECB's lead in implementing a negative bank deposit rate.

Chinese economic data continued to weaken, raising investor concern. China's February manufacturing PMI figures were below expectations, with the official indicator dropping from 49.4 in January to 49.0 in February – the seventh straight month of sub-50 readings (with figures below 50 indicating contraction). Similarly, the Caixin China Manufacturing PMI was down from 48.4 in January to 48.0 in February. China's CPI was lower than expected in January, recording 1.8% (versus a forecast value of 1.9%), although slightly higher on previous months.

In the Eurozone, low inflation continued to pose a challenge to monetary policy. Year-on-year CPI throughout the Eurozone hit negative territory in February for the first time since October 2015, recording -0.2% and fuelling scepticism about the efficacy of current monetary policy settings. The President of the German Bundesbank, Jens Weidmann, expressed concern that doubts about monetary policy have spilled into financial markets, causing investors to shift to safer assets.

Growth in Germany, Europe's largest economy, remained subdued in Q4 2015 at 0.3% – in line with the Eurozone economy. While Greece largely reverted to a background issue following the IMF's granting of debt relief last year, the Republic fell back into recession in February, with Eurostat reporting that Greek GDP fell -0.6% in Q4.

For emerging markets, data was mixed. Brazilian inflation reached 10.7% y/y in January, while unemployment rose from 8.0% to 7.6% in January. Russian inflation was down to 8.1% y/y in February, falling from 9.8% in January, reflecting large declines in oil prices. Indian Q3 growth remained more or less steady at 7.3%, down from 7.4% in Q2 and mostly in line with expectations.

Commodities

Energy prices stabilised in February, with WTI crude oil rising to US $32.74/b, from a spot price of US $31.62 at the start of February. Brent crude oil also gained, rising from US $31.09 to US $35.92. The US Energy Information Administration forecasts US crude oil production to average 8.7 million b/d in 2016, with crude oil prices to average US $38/b, rising to US $50/b in 2017. However, growth in global oil inventories continue to put downward pressure on prices.

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Base metals were mostly positive in February, with gold (10.77%), aluminium (5.10%), copper (2.96%), lead (2.02%), tin (7.18%) and zinc (8.03%) all gaining, while nickel (-1.07%) was down.

Currency

Foreign exchange markets restored stability towards the month's end, supported by a bounce in the price of oil. The US Dollar Index closed February -1.4% lower, gaining on major currencies, including JPY (7.3%) and EUR (0.4%), and down against GBP (-1.8%).

The AUD strengthened against most major currencies, including USD (1.0%), EUR (0.4%), GBP (3.2%), however weakened against NZD (-0.8%) and JPY (-6.2). China's central bank fixed the yuan at a softer midpoint in February, resulting in a mild decline, although the Chinese currency was up against USD (0.4%) over the month.

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