Month in Review

ISSUE DATE: 7-09-2016

Market Moves — as at 31•08•2016

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	-1.55	2.07	13.91	9.30	6.59	9.68	5.17
S&P/ASX SMALL ORDINARIES ACCUMULATION INDEX	-1.56	5.47	19.30	26.55	7.13	2.62	1.45
GLOBAL EQUITIES							
MSCI WORLD TR INDEX (AUD)	1.27	-0.45	7.30	1.24	14.28	18.22	5.30
S&P 500 TG INDEX (AUD)	1.27	0.35	7.96	6.17	18.84	23.10	7.68
FTSE 100 TR INDEX (AUD)	1.43	-4.47	1.86	-8.30	5.84	11.68	1.53
MSCI EMERGING MARKETS NET TR INDEX (AUD)	3.64	7.91	16.60	5.49	7.00	6.89	4.07
REAL ESTATE INVESTMENT TRUSTS (REITS)							
S&P/ASX 300 A-REIT (SECTOR) ACCUMULATION INDEX	-2.68	6.16	14.80	25.97	19.79	19.51	2.48
FTSE EPRA/NAREIT DEVELOPED NET TR INDEX (AUD HEDGED)	-2.18	5.67	14.50	17.10	14.03	13.94	4.99
FIXED INTEREST							
BLOOMBERG AUSBOND COMPOSITE 0+ YR INDEX	0.42	2.50	3.84	6.19	6.46	6.21	6.62
BLOOMBERG AUSBOND BANK BILL INDEX	0.17	0.51	1.10	2.22	2.46	2.99	4.28
BARCLAYS GLOBAL AGGREGATE TR INDEX (AUD HEDGED)	0.05	2.75	4.61	8.95	7.66	7.23	7.85

Data source: IRESS & 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 took an early stumble in August following the RBA's rate cut, with investors concerned about the signal low rates are sending about the health of the economy. The S&P/ASX 200 Index was down -2.18% following the announcement, before sliding further late in the month to finish at 5415.6 points. Returns on Australian shares, measured by the S&P/ASX 200 Accumulation Index, were -1.55% in August, taking the 12-month return to 9.30%.

The largest gains came from the Information Technology sector (5.16%), with the index supported by a rebounding Energy sector (3.14%) as well as Consumer Staples (2.41%), while Materials managed a modest 0.7% gain following a 7.0% surge in July. Altium led the tech gains, returning 26.06% following the release of strong full-year results at the end of the month, while Whitehaven Coal added to its July performance, returning 15.73% after announcing strong revenue growth and a return to profit. Small cap returns, measured by the S&P/ASX Small Ordinaries Accumulation Index, were -1.56% in August, in line with large cap results, with returns over 12 months reaching 26.55%.

Global equities

Calm fell over markets in August, bringing with it both a sense of relief and disquiet. Equity indices were mostly flat as investors took time to assess the economic situation and to await guidance from central banks. Global shares, measured by the MSCI World NR Index (AUD), returned 1.27%, which was matched by the US market. US shares were little changed on earnings, and a key speech from Janet Yellen at the annual Jackson Hole symposium provided no clues as to the timing of any interest rate hike. Despite promising economic developments, earnings remain the missing piece of the recovery puzzle. Earnings per share have moved slightly higher, although this is largely the result of share buybacks. Consumers continue to drive the economy forward, reflected in strong results from department stores Nordstrom and Macy's.

In the UK, the FTSE 100 TR Index returned 1.43%, still below its pre-Brexit level in AUD terms, but fully recovered in local currency terms. UK GDP grew by 0.6% in Q2, comforting investors worried about the impact of the referendum on consumer spending, however much uncertainty remains regarding the medium-term impact on the UK and European economies. Europe's top 50 shares performed solidly in August, with the Euro Stoxx 50 Net Return Index returning 2.04%. The MSCI Emerging Markets Net TR Index returned 3.64%, while in Asian markets the Nikkei 225 Net TR Index gained 1.94% and the Shenzhen CSI 300 Net TR Index rose 4.28%.

REITs

After four consecutive months of solid gains, the S&P/ASX 300 A-REIT Accumulation Index returned -2.68% in August, as the prospect of rate rises weighed on prices. Stockland and Dexus reported growth in funds from operations of 12.5% and 12.0% respectively, following healthy results earlier in the month from Mirvac Group and GPT Group. Leveraging remains around the historical average, with Dexus reporting 'look through' gearing of 30.7%, although the cost of debt has been low and falling thanks to current monetary policy settings.

Month in Review

Global REITs also pulled back in August, returning -2.85% (in AUD hedged terms), while the FTSE EPRA/NAREIT Developed NR Index lost -2.18%. The S&P United States REITs NR Index returned -3.01%, as the market considered incoming economic data to be supportive of a rate hike in 2016. As of the close of trading on 31 August, a new sector was born, with the S&P Dow Jones Indices and MSCI reclassifying real-estate equities as a standalone sector within the S&P 500. This is expected to increase demand for REIT shares and ETFs as passive funds linked to the S&P 500 incorporate the new sector.

Fixed interest

Global bonds, measured by the Barclays Global Aggregate TR Index, returned a very meagre 0.05% in August (in AUD hedged terms) as yields remain at depressed levels throughout the world. While yields experienced a modest pickup in some markets, the impact on returns is being keenly felt. Added to this is the concern that a tightening in rates, if not done gradually, could cause a disorderly readjustment in fixed income values. In the US, the return on corporate investment grade bonds was 0.21% in August, while US high yield debt returned 2.14% as yields moderated. Credit spreads continued to narrow following a brief Brexit spike, with the Bank of America Merrill Lynch US High Yield Option-Adjusted Spread narrowing from 5.69% to 5.10%, down from its February high of 8.87%.

Australian bonds returned 0.42% in August, with returns on Australian corporate bonds a modest 0.73%. Australian government bonds returned 0.35% as the 10-year yield pushed down from 1.87% to 1.82%.

Brexit has had a sustained impact on British yields, with the UK 10-year Gilt yield moving lower in August, from 0.68% to 0.64%, with a mid-month low of 0.52%. This is compared to the pre-Brexit high of 1.37%. Outside of the UK, sovereign markets are beginning to see a gradual lift in yields, with markets again countenancing the possibility of an early rate hike from the Fed. The US 10-year Treasury yield rose from 1.45% to 1.58%, and the German 10-year Bund rose from -0.12% to -0.07%, making its way slowly back towards positive territory. Japanese 10-year yields lifted slightly from -0.195 to -0.071, heading into its sixth month of negative yields, following an unprecedented low of -0.295% in July.

ASX 200 Share Movements

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

BEST PERFORMERS		WORST PERFORMERS	
GWA GROUP	40.28%	APN OUTDOOR GROUP	-34.86%
CLEANAWAY WASTE MANAGEMENT	32.16%	ESTIA HEALTH	-32.94%
AUSTAL	27.16%	SEVEN WEST MEDIA	-24.64%
ALTIUM	26.06%	NORTHERN STAR RESOURCES	-23.15%
CREDIT CORP GROUP	24.72%	SARACEN MINERAL HOLDINGS	-23.03%

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

BEST PERFORMERS		WORST PERFORMERS	
ST BARBARA	424.07%	LIQUEFIED NATURAL GAS	-100.00%
SARACEN MINERAL HOLDINGS	200.00%	MESOBLAST	-59.64%
A2 MILK	190.55%	ESTIA HEALTH	-49.11%
MINERAL RESOURCES	159.50%	SPOTLESS GROUP HOLDINGS	-46.98%
FORTESCUE METALS GROUP	156.54%	SELECT HARVESTS	-44.49%

Economic News

Australia

The Australian economy may yet remain the envy of the world, with Q2 GDP growth showing an expansion of 0.5%, versus an expected 0.4%, and annual growth at 3.3%. This represents 21 straight quarters of growth, and the economy has not seen a recession since 1991, if only due to some statistical luck along the way. Growth appears indicative of a relatively smooth transition from mining-led growth, and it appears the worst of the commodity price slump is behind us, with metals and energy stabilising in recent months.

At its meeting on 6 September, the RBA left the cash rate unchanged at 1.50%, following July's 25bp cut. While growth is strong, the CPI figure for the June quarter recorded an annual 1.0% increase across all groups, reinforcing the RBA's concerns about weak price growth following the March quarter figure of 1.3%. September's rate decision was the last to be made with Glenn Stevens at the helm, with incoming Governor Philip Lowe to take over as of 18 September.

The unemployment rate fell slightly in July from 5.8% to 5.7%, with the number of unemployed persons falling by 5,500 in seasonally adjusted terms.

Month in Review

The participation rate remained steady at 64.9%, while monthly hours worked increased by 3.7 million. While trend employment growth continues, the ABS notes that the rate of growth over the past six months has been slightly below the 20-year average.

There was some worrying news from Australia's manufacturers, with the AIG Manufacturing Index falling sharply from 56.4 in July to 46.9 in August, after 13 straight months of above-50 readings. Retail turnover was unchanged in July 2016, missing the consensus figure of 0.3% growth. The result follows a modest rise of 0.1% in June. There was a pickup in the major food retailing group (0.7%) as well as gains in cafes, restaurants and takeaway food services (0.3%), however these were offset by falls in department stores (-6.2%) and household goods retailing (-0.7%).

The retail figures matched July's fall in consumer sentiment, although the indicator picked up in August, with the Westpac Melbourne Institute Index of Consumer Sentiment showing a 2.0% rise from 99.1 to 101.0, indicating a majority of respondents were positive about the economy. The survey period covered the RBA's rate cut in early August, although the response from consumers was more muted compared to the previous rate cut back in May. While those with a mortgage tended to respond favourably to the latest cut, those who own their home outright were less confident, worried that a rate cut signifies a weaker economy.

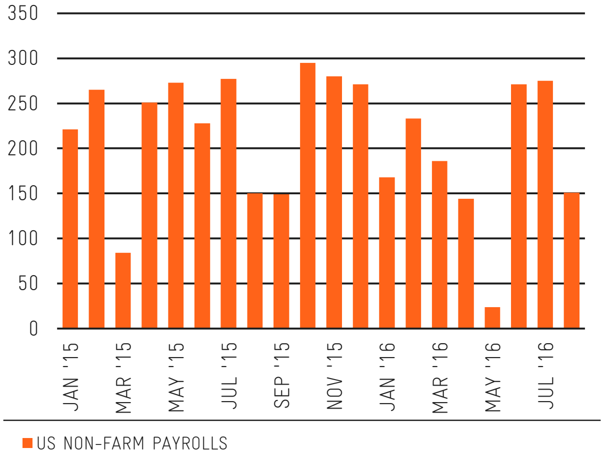
Global

The market's attention in late August was focused on the annual Jackson Hole conference, and any hints from Janet Yellen on the timing of future rate hikes. Once again, investors were told to look to the data, which suggest a reasonably wide range of outcomes for the funds rate. Based on solid labour market performance, the case for a rate increase has strengthened.

Non-farm payrolls recorded an additional 151,000 jobs in August, below the expected 180,000, leaving the unemployment rate steady at 4.9%. The broader measure, encompassing discouraged workers and those working part-time for economic reasons, was steady at 9.7%. August is traditionally a challenging month for the US labour market, and this year was no exception.

US Q2 GDP increased by 1.1% according to the BEA's 'second' estimate released in August, slightly down on the 1.2% advance estimate delivered in July. The Q2 figure reflected strong growth in personal consumption expenditure as well as a boost in exports, offset by negative contributions from private inventory and residential fixed investment, and state and local government spending. While the US consumer appears in rude health, weakness from other components is making for a cloudy outlook.

US Non-Farm Payrolls



Source: US Bureau of Labor Statistics

The ISM Manufacturing PMI fell to 49.4 in August, down from July's reading of 52.6 and falling short of the market's expectation of 52.0. The New Orders Index fell sharply from 56.8 to 49.1, while the Production Index also moved to contraction, falling from 55.4 to 49.6.

US inflation continues to run below target, with consumer prices rising at an annual unadjusted rate of 0.8% in July, down from 1.0% in June. Energy prices fell 1.6%, following increases over four consecutive months, with the decrease mostly due to falling gasoline prices. All items less food and energy increased by an annual 2.2%, with rises in shelter (3.3%), medical care (4.0%) and motor vehicle insurance (6.3%). The Fed expects that consumer prices will move back in line with the 2% target over the medium term.

US retail sales in July were virtually unchanged from the previous month, representing a 12-month increase of 2.3%. Gains came from auto dealers (1.3%) and non-store retailers (1.3%), while gasoline stations (-2.7%), department stores (-0.5%) and grocery stores (-0.9%) were down.

Turning to Europe, GDP in the euro area grew at an annual rate of 1.6% in Q2, according to the preliminary estimate, with growth failing to take hold following the end of the European recession in 2013. The UK economy grew by an annual rate of 2.2% in Q2 ahead of the Brexit vote, helped by the biggest pickup in industrial production since 1999. However, the construction industry saw a significant loss of momentum in July following the referendum, with the Markit/CIPS PMI Index falling to 45.9.

Euro area inflation was estimated to reach an annual rate of 0.2% in August, remaining unchanged from July. Food, alcohol and tobacco was estimated to rise 1.3%, while the energy component fell -5.7%, following large falls in previous months.

Month in Review

Euro area unemployment was 10.1% in July, steady on June and down from 10.8% in July 2015. The slow pace of employment growth, as well as the very low rates of inflation recorded across the continent, have been a source of much consternation for policy makers. The dispersion in unemployment rates across Euro area members remains high, ranging from 4.2% in Germany and Croatia, to 23.5% and 19.6% in Greece and Spain respectively.

China's August PMI surveys again saw mixed results, this time with the official gauge moving higher, from 49.9 to 50.4 and beating expectations, while the Caixin figure, which tracks smaller-scale private firms, fell from 50.6 to 50.0. China's CPI rose 0.2% in August, with annual inflation falling slightly from 1.9% to 1.8%. Chinese Q2 GDP, released in July, remains steady at an annual rate of 6.7%.

In other emerging markets, Brazilian Q2 GDP showed further contraction in growth, shrinking by -0.6% and -3.8% over the year, while July inflation fell slightly from an annual 8.8% to 8.7%. Russian Q2 GDP recorded a contraction of -0.6% and appears to be heading back towards expansion after large falls in recent quarters. Russian inflation grew at an annual 6.9% in August, down from 7.2% in July. Indian Q1 GDP grew at an annual rate of 7.1%, down on the Q4 2015 figure of 7.9%, according to official data.

Commodities

August saw a rebound in oil, with the Brent crude oil spot price rising from US $41.01/b to US $46.18/b (12.6%), after hitting a high of US $50.03 mid-month. WTI crude rose from US $41.60/b to US $44.70/b, hitting a high of US $48.52/b.

Metals were mixed in August, with Lead (4.5%), Tin (5.7%) and Zinc (3.0%) gaining, while Copper (-6.3%), Nickel (-8.1%) and Aluminium (-1.8%) lost. Gold eased following its post-Brexit rally, falling from US $1351.28/oz to US $1308.97/oz. In August the World Gold Council revealed record investment demand in H1 2016 of some 1,064 tons, which has led to a 25% rise in the price of the precious metal since the start of the year.

The price of iron ore delivered to Qingdao in China fell slightly from US $59.37 to US $58.87 (-0.7%), mostly flat through the month and still much reduced from its April high of US $70.46.

Currencies

The AUD fell -0.2% in August in trade weighted terms, falling -1.0% against USD to end the month at 0.7517, after hitting an early high of 0.7703. The AUD has largely tracked commodity price moves, and has remained under significant buying pressure despite two interest rate cuts in the past four months. The AUD fell against most major currencies, including EUR (-1.0%), GBP (-0.3%) and NZD (-1.8%), but gained against JPY (0.3%).

The US Dollar Index closed August slightly higher (0.5%), gaining against major currencies, including EUR (0.2%), JPY (1.3%), GBP (0.7%) and CHF (0.5%).

Month in Review