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Month in Review

Market Moves — as at 31•01•2018

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	-0.45	3.02	7.89	12.18	7.31	9.07	5.29
S&P/ASX SMALL ORDINARIES ACCUMULATION INDEX	-0.54	6.65	17.65	22.35	13.82	6.39	1.48
GLOBAL EQUITIES							
MSCI WORLD TR INDEX (AUD)	1.71	3.33	12.37	18.61	11.01	18.13	8.07
S&P 500 TG INDEX (AUD)	2.12	4.33	13.80	18.51	13.18	21.93	10.85
FTSE 100 TR INDEX (AUD)	-0.45	2.54	10.54	16.97	4.50	10.83	3.96
MSCI EMERGING MARKETS NET TR INDEX (AUD)	4.64	6.48	16.85	32.20	10.38	11.24	4.89
REAL ESTATE INVESTMENT TRUSTS (REITS)							
S&P/ASX 300 A-REIT (SECTOR) ACCUMULATION INDEX	-3.25	2.00	6.47	8.08	7.46	11.67	3.01
FTSE EPRA/NAREIT DEVELOPED NET TR INDEX (AUD HEDGED)	-1.31	2.10	2.44	7.32	3.47	8.70	5.32
FIXED INTEREST							
BLOOMBERG AUSBOND COMPOSITE 0+ YR INDEX	-0.27	0.08	0.85	2.75	2.41	4.14	6.03
BLOOMBERG AUSBOND BANK BILL INDEX	0.16	0.43	0.87	1.75	2.02	2.32	3.58
BARCLAYS GLOBAL AGGREGATE TR INDEX (AUD HEDGED)	-0.69	-0.26	0.73	3.24	3.10	4.86	6.85

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 S&P/ASX 200 Accumulation Index fell 0.5% in January, pulled down by yield-sensitive utilities and property. Positive returns were achieved by the healthcare sector (+3.2%), driven by large gains from Sirtex Medical (+66.2%) following a proposed $1.6 billion takeover bid from US cancer care provider Varian, and gains from Resmed (+13.5%), with the sleep disorder device maker announcing a 13% lift in sales revenue for the second quarter. The IT sector (+2.0%) also managed to gain, led by Altium (+14.7%), along with solid returns from Wisetech Global (+9.5%) and Computershare (+2.5%).

Defensive sectors such as utilities (-4.5%) were down, with AGL (-3.8%) and APA Group (-3.2%) lower, along with industrials (-2.1%) and the major financials sector (-0.8%). Banks came under pressure after a flat month in December, offset by gains from asset managers including Perpetual (+8.3%) and IOOF Holdings (+2.8%). The modest fall in Australian shares was of course only a taste of what was to come in early February, with a global sell-off leading to a 4.7% drop in the ASX 200 and hitting defensive shares and small caps the hardest.

Global equities

The US S&P 500 Index rose 5.6% in US dollar terms, pushing to a new record high of 2690.16 points during the month, before dropping early in February as the market underwent a major correction and volatility spiked. January’s gains were driven by the consumer discretionary (+9.3%) and IT (+7.6%) sectors, with strong leads from Netflix (+40.8%) and Amazon (+24.1%), while Apple (-1.1%) was down after a lacklustre quarter.

During the month it was US Nobel laureate Robert Shiller who warned the Davos crowd that markets could “absolutely suddenly turn” and that “it [a market correction] doesn't need a trigger, it's the dynamics of bubbles inherently makes them come to an end eventually.” Somewhat prescient given recent market events, but Shiller was undoubtedly not the only one wondering when the music would eventually stop.

Globally, the MSCI World TR Index rose 1.7% in AUD terms, driven by gains in US, Japanese and European markets. In Europe, the broad STOXX Euro 600 Index rose 1.6%, driven by Financials and Resources, while Utilities and Property took a hit as bond yields moved higher. The German DAX rose 2.1%, with gains from auto giant Volkswagen (+6.4%), insurer Allianz (+6.3%) and major bank Commerzbank (+6.0%). Meanwhile, Deutsche Bank (-6.8%) is contending with a €500 million loss for 2017 (the third annual loss in a row) and has been driven down almost 20% over 12 months. In Asia the Chinese CSI 300 Index rose 6.1% and Hong Kong’s Hang Seng added 9.9%. In Japan, the Tankan survey showed the best business conditions for big manufacturers since 2006, helping boost the Nikkei 225 Index by 1.5% over the month.

REITs

The S&P/ASX 300 A-REIT Accumulation Index (which includes distributions) fell 3.25% in January, with higher yields bringing the sector under pressure. Arena REIT (+1.3%) was able to defy the trend with a positive return in January after falling through December, but diversified managers including Abacus Property (-9.9%) and Mirvac Group (-6.4%) felt the heat from their commercial property portfolios.

We strongly recommend that potential investors read the product disclosure statement or investment statement.
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Globally, the EPRA/NAREIT Developed Market Index (AUD hedged) fell 1.3%, outperforming domestic REITs but still underperforming over longer periods. US REITs, measured by the MSCI US REIT Index, had a rough start to the year, falling 4.3%, but with the first earnings reports of the season showing positive signs on the back of strong retail sales.

Fixed income

Fixed income markets saw some serious action through January, with yields expanding significantly in response to the market's reassessment of risk factors and interest rate movements. Australian bonds returned -0.27% over January, with Australian government bonds returning -0.35%, and longer-term government bonds (ten years plus) returning -1.02%. The Australian 2-year government bond yield fell slightly from 2.04% to 2.03%, while the 10-year yield underwent significant expansion, moving from 2.67% to 2.81% and reaching a high of 2.87% mid-month. Globally, the Bloomberg Barclays Global Aggregate Bond Index (AUD hedged) returned -0.69%, with yields in major developed markets rising. In the US, investment grade bonds returned -0.96% while high yield debt returned 0.60%. The US 10-year treasury yields rocketed higher, moving from 2.40% to 2.72%.

Japanese 10-year bond yields rose from 0.04% to 0.08%, moving further from the Bank of Japan's zero yield target. The German 10-year yield rose from 0.42% to 0.70%, while 5-year yields moved into positive territory for the first time since September 2015, rising from -0.21% to 0.10%. The BofA Merrill Lynch US High Yield OAS narrowed in January from 3.63% to 3.29% and again pushed to historic lows during the month, with no sign of moving higher, even as volatility returned with a vengeance in early February.

ASX 200 Share Movements

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

BEST PERFORMERS		WORST PERFORMERS	
ACONEX	66.16%	RETAIL FOOD GROUP	-20.85%
SIGMA HEALTHCARE	17.20%	G8 EDUCATION	-15.25%
ST BARBARA	15.35%	MYER HOLDINGS	-14.13%
BEACH ENERGY	14.68%	QANTAS AIRWAYS	-13.32%
ARDENT LEISURE GROUP	13.47%	APA GROUP	-12.60%

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

BEST PERFORMERS		WORST PERFORMERS	
A2 MILK CO LTD	291.04%	RETAIL FOOD GROUP LTD	-67.77%
SEVEN GROUP HOLDINGS LTD	223.78%	MYER HOLDINGS LTD	-47.22%
COSTA GROUP HOLDINGS LTD	154.64%	MAYNE PHARMA GROUP LTD	-42.91%
ST BARBARA LTD	154.12%	HT&E LTD	-35.69%
MINERAL RESOURCES LTD	132.39%	FLETCHER BUILDING LTD	-31.39%

Economic News

Australia

The RBA's February monetary policy statement was undeniably more bullish compared to its December release, but nevertheless the board opted to keep the **cash rate** on hold at 1.50%, with inflation still low but expected to move higher. The Bank's central forecast for GDP growth is just above 3% over the next two years, supported by monetary policy conditions that remain expansionary, while the benefits of broad-based global growth and increased international trade are flowing through to the local economy.

Australia's **CPI** reading for the December quarter was 0.6%, unchanged on the September quarter, with growth of 1.9% over 12 months. While slightly below expectations, and all but scuppering any possibility of a rate hike, inflationary pressures appear to be gradually taking hold nationally, although mostly evident in the eastern states. Growth through the quarter was predominately driven by food and non-alcoholic beverages (+1.0%) and alcohol and tobacco (+3.2%).

Australia's labour market continues to improve, with 34,700 seasonally adjusted jobs added in December, which included 15,100 full-time jobs and 19,500 part-time jobs. The **unemployment rate** rose 0.1 points to 5.5%, due to a rise in the participation rate. The number of unemployed persons looking for full-time work rose 9,900 to 501,800, while monthly hours worked fell 4.2 million to 1,736.4 million hours. Total employment growth through 2017 was 3.4%, while growth in full-time employment was solid at 3.7%, with the employment to population ratio improving from 61.0% at the end of 2016 to 62.0% at the end of 2017.

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The **AIG Manufacturing Index** rose 2.5 points to 58.7 in January, indicating continued robust growth in the manufacturing economy. January marked the third consecutive month that all seven sub-indices were in expansion, with strong growth in Production (+5.0 points to 62.7), Deliveries (+4.6 points to 62.0), and Sales (+3.4 points to 56.0), along with more modest increases in New Orders (+1.9 points to 58.8), Exports (+0.4 points to 51.8) and Stocks (+1.0 points to 56.5). Employment (-0.8 points to 52.1) was the only sub-index to fall.

In more positive news from consumers, the **Westpac Melbourne Institute Index of Consumer Sentiment** rose a further 1.8% in January from to 105.1. This comes on the back of a surprise 3.6% turnaround in December, as households took a more positive view of interest rates and the labour market. However, the degree to which spending improves still looks likely to be constrained with the survey detail suggesting family finances are still under pressure. The 'finances vs a year ago' sub-index remained weak, declining 1.1% to 88.6, retracing some of last month's solid gain and remaining well below 100.

Australia's **balance on goods and services** fell to a deficit of $1.358 billion in seasonally adjusted terms, falling $1.394 billion on November's narrow $36 million surplus. Exports of non-rural goods rose $719 million, general merchandise rose $575 million, and metal ores and minerals added $336 million. While exports were higher, on the debits side imports of general merchandise grew $1.665 billion, consumption goods rose $422 million, and capital goods rose $341 million.

Global

The first estimate of **US Q4 GDP** indicated real growth of 2.6%, slowing from Q3's growth of 3.2% and lower than the market's anticipated 3.0%. Imports, which subtract from GDP growth, increased at their fastest rate in more than seven years, highlighting the challenge facing the Trump administration in achieving its 3.0% growth target. While recent tax cuts will provide some fiscal stimulus, the short-term impact is likely to be relatively modest.

At its January meeting, the Fed voted to maintain the **funds rate** at its target range of 1.25–1.50%, following its 25 bp hike in December. Members voted unanimously to maintain the current range, which remains accommodative and supportive of strong labour labour market conditions and gradual return to the 2% inflation target. The Atlanta Fed's GDPNow indicator, which provides a 'nowcast' of economic activity, is currently tracking Q1 growth at 4.0%, although this is based on only a handful of major economic releases since the start of 2018.

The manufacturing economy expanded in January although at a slightly slower pace on December, with the **ISM manufacturing PMI** falling from 59.3 to 59.1. Major indices fell modestly, including New Orders (-2.0 to 65.4), Production (-0.7 to 64.5), and Employment (-3.9 to 54.2), while other indices pushed further into expansion, including Deliveries (+1.9 to 59.1), Inventories (+3.8 to 52.3), and Prices (+4.4 to 72.7). Customers' Inventories (+2.7 to 45.6) was the only index in contraction.

Non-farm payrolls rose 200,00 in January, beating the market's expected 184,000 and providing further evidence of an improving jobs picture. The unemployment rate was unchanged at 4.1%, and the number of persons employed part-time for economic reasons was essentially unchanged at 5.0 million. The largest employment gains came from construction (+36,000), food services and drinking places (+31,000) and healthcare (+21,000). The broader U-6 measure of unemployment, which includes discouraged workers and those marginally attached to the labour force, rose slightly in January from 8.1% to 8.2%.

US CPI rose 0.1% in December on a seasonally adjusted basis and 2.1% on an unadjusted year-on-year basis. Core inflation (which excludes food and energy) rose 0.3% during the month and 1.8% year-on-year, driven predominately by shelter (3.2% year-on-year) and transportation services (3.7% year-on-year). Gasoline prices fell 2.5% during the month, following significant rises in the latter months of 2017. The core PCE index – the Fed's preferred measure – was steady at 1.5% year-on-year, still below the headline rate of inflation and stubbornly at odds with overall growth and employment conditions.

Turning to Europe, **euro area GDP** grew by 0.6% in Q4, compared to 0.7% in Q3. This represents year-on-year growth of 2.7% versus 2.8% in the previous quarter. Growth across the 19 eurozone countries remains promising, and the recovery has also become more broad-based, both across different countries and sectors. The ECB's January policy vote revealed a continued shift in rhetoric, pointing to strong cyclical momentum and rises in private consumption and business investment. In early February the EU upped its growth forecast for 2018 from 2.1% to 2.3%, which is broadly in line with ECB and IMF projections.

Euro area inflation is estimated to be 1.3% in January, down from 1.4% in December. Core inflation (excluding energy, food, alcohol and tobacco) is estimated to be 1.0%, higher on the previous month's 0.9% but still very low. **Unemployment** in the eurozone was 8.7% in December, stable on November and still at the lowest rate recorded since January 2009. Among the Member States, the lowest unemployment rates in December 2017 were recorded in the Czech Republic (2.3%), Malta and Germany (both 3.6%). The highest unemployment rates were observed in Greece (20.7% in October 2017) and Spain (16.4%).

The **Chinese economy** slowed marginally in the December quarter, with GDP growth falling to 6.8% after averaging 6.9% in the first three quarters of 2017. A clampdown on factory pollution, a further lift in

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borrowing rates, and tighter financial conditions in the shadow banking sector are likely to have dampened growth. China has already experienced a decline in fixed investment spending, with growth of just 7.2% year-on-year in December, while many housing and property activity indicators are pointing to a slowdown after a recovery in 2016. Industrial production recovered slightly from 6.1% year-on-year to 6.2% in December, while January's official PMI was 51.3, down from 51.6 in December and below expectations.

Commodities

Commodities continued their rally in January, with the pick-up in the global economy contributing to a rise in oil and other commodity prices over recent months. Base metals climbed aggressively through the month, with Tin (+6.7%), Zinc (+6.7%), Nickel (+6.6%) and Lead (+5.0%) all gained strongly, while Copper (-1.8%) and Aluminium (-2.2%) were down. Gold rose 3.3% to reach a high of US $1358.46/oz – the highest since April 2016.

The spot price of iron ore delivered to China (62% Fe) rose 1.2% from US $70.78/t to $71.61, pushing higher but still down on its recent August 2017 high of $78.91. In oil markets, the Brent spot price gained 1.6% from US $66.73/b to $67.78, while WTI rose 7.2% from $60.46 to $64.82.

Currencies

The AUD rose 1.1% in trade-weighted terms over the three months to the end of January, with higher commodity prices boosting export values. The AUD rose 5.1% against the USD, hitting a low of 0.7509 in December and a high of 0.8110 in late January to end the month at 0.8053. The AUD was up against the JPY (+1.1%) and down against other major currencies including the EUR (-1.4%), GBP (-1.7%), and NZD (-2.4%).

The US Dollar Index fell 5.7% over the three months to January, and has fallen 10.4% over 12 months. The USD hit a high of 0.8634 against the EUR in November and a low of 0.8006 in January to end the month at 0.8055, down 6.2% over three months. The USD was down against the GBP (-6.4%), CHF (-6.4%), and JPY (-3.8%).

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