Month in Review

ISSUE DATE: 7-04-2017

Market Moves — as at 31•03•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	3.32	4.82	10.25	20.49	7.53	11.10	4.32
S&P/ASX SMALL ORDINARIES ACCUMULATION INDEX	2.66	1.46	-1.03	13.67	6.44	2.28	-0.83
GLOBAL EQUITIES							
MSCI WORLD TR INDEX (AUD)	1.93	1.12	8.97	16.40	13.23	16.93	5.41
S&P 500 TG INDEX (AUD)	0.90	0.68	10.47	18.16	17.77	20.45	8.13
FTSE 100 TR INDEX (AUD)	2.41	-0.43	4.41	8.20	4.23	10.21	1.30
MSCI EMERGING MARKETS NET TR INDEX (AUD)	3.33	5.78	7.14	18.20	7.96	7.17	3.31
REAL ESTATE INVESTMENT TRUSTS (REITS)							
S&P/ASX 300 A-REIT (SECTOR) ACCUMULATION INDEX	0.71	-0.08	-0.81	6.31	16.76	16.87	0.48
FTSE EPRA/NAREIT DEVELOPED NET TR INDEX (AUD HEDGED)	-1.51	1.22	-1.17	3.85	9.66	11.54	2.56
FIXED INTEREST							
BLOOMBERG AUSBOND COMPOSITE 0+ YR INDEX	0.44	1.23	-1.67	2.09	4.98	5.05	6.15
BLOOMBERG AUSBOND BANK BILL INDEX	0.15	0.44	0.88	1.94	2.30	2.65	4.01
BARCLAYS GLOBAL AGGREGATE TR INDEX (AUD HEDGED)	0.03	0.68	-1.50	2.16	5.59	5.80	7.34

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 powered on through March, returning 3.32% during the month with all sectors gaining. The index delivered 4.82% in Q1 2017, with the 12-month return holding at a non-trivial 20.49%. In March, the Healthcare sector (+5.62%) built on solid gains made through the start of the year, led by Ansell (+13.06%) and Sirtex Medical (+12.23%), which is catching up with the sector after disappointing results in December. Heavyweight CSL (+7.06%) continued to push higher after upgrading its guidance in January.

March was another strong month for Consumer Staples (+5.59%), with a2 Milk (+23.98%) still benefitting from rival Bellamy's fall from grace, and Australian Agricultural Co (+16.90%) was boosted by higher cattle prices and strong demand for beef. Materials (+0.78%) was the worst performing sector in March, posting only marginal gains after falling 3.03% in February. The biggest losses came from Resolute Mining (-19.25%) and Oz Minerals (-13.77%). Small cap equities underperformed the top 200 in March, with Resources a drag (-3.00%) while Industrials (+4.56%) gained.

Global equities

In the US, markets moved slightly higher, with the S&P 500 TG Index gaining 0.90% in AUD terms, while the Dow Jones Industrial Index was down 0.30%. While the reflation narrative has been reflected in higher equity prices, the market pulled back mid-month, with investors returning to duration following the failure of Trump's healthcare bill in the US House of Representatives. The full implementation of tax cuts and the promised infrastructure package have also moved that much further from being a political reality.

Information Technology (+2.98%) continued to rise, with shares like Micron Technology (+23.81%) benefiting from a favourable pricing environment, while Health Care (0.00%) was dead flat following Congress's rejection of the repeal and replace legislation.

Globally, the MSCI World Net TR Index gained 1.93% in AUD terms, boosted by Europe and emerging markets. In Europe, the Euro Stoxx 50 Index rose 6.79%, with major banks, including Banco Bilbao (+19.16%), Société Générale (+14.89%) and BNP Paribas (+14.67%) gaining strongly despite the ECB taking a more stoic approach to monetary policy than the Fed. In the UK, the FTSE 100 TR Index gained 2.41% in AUD terms. In Asian markets, the Nikkei 225 Index lost -0.12% while the Shenzhen CSI 300 Index gained 0.26%. The MSCI Emerging Markets Net TR Index rose 3.33%, with gains in the South Korean and Indian markets.

REITs

The S&P/ASX 300 A-REIT Accumulation Index added 0.71% in March after an impressive bounce-back in February. The big gainers were Rural Funds Group (+7.01%) and Hotel Property Investments (+5.69%), while the index was dragged down by losses from shopping centre giants Scentre Group (-1.61%) and Vicinity Centres (-2.08%), with slowing wage growth starting to bite (as well as the spectre of online retail).

The A-REIT market has displayed remarkable resilience but has struggled in the uncertain rate environment, with the index ending March where it began at the start of 2017. However, while rising yields will put pressure on A-REIT values, the sector may continue to be a source of stability, especially if equity markets become more volatile through 2017.

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Globally, REITs were under renewed pressure in March, with the S&P Global REIT NTR Index returning -0.18% (in AUD hedged terms), while the FTSE EPRA/NAREIT Developed NR Index was down 1.51% as global yields moved higher. With the Fed signalling two more potential rate rises for 2017, cap rates and leasing spreads may continue to come under pressure, but if the tightening path remains on the dovish side, yield-producing asset classes like REITs may continue to be in demand.

Fixed income

Global yields generally ended flat in March, after some movements higher earlier in the month. While rates have been trending higher since October 2016 and yield curves have steepened, investors appeared to embrace duration again in the latter part of the month, reflected in longer-term fund flow. The US 10-year Treasury yield ended where it started the month at 2.39%, after rising to an intra-month high of 2.63%. While recent CPI releases in both Europe and the US have been promising, the numbers have moderated in recent months, and core inflation remains well below central bank targets. The return on US corporate investment grade bonds was -0.18% in March, while US high-yield debt returned -0.14%. For the first time since October 2016, credit spreads showed a material expansion, with the BofA Merrill Lynch US High Yield OAS rising from 3.74% to 3.92%.

Global bonds, measured by the Barclays Global Aggregate TR Index, returned 0.03% in March (in AUD hedged terms). Returns on Australian corporate bonds were 0.56% while government bonds returned 0.42%, with the yield on Australian 10-year Treasuries falling slightly from 2.72% to 2.70%. The UK 10-year Gilt yield fell from 1.15% to 1.14% in March – softer since its post-Brexit high of 1.51% in January. The German 10-year Bund yield rose from 0.21% to 0.33%, while the 5-year Bund rose from -0.58% to -0.39% and has been persistently negative since October 2015. Since turning positive in November 2016, Japanese 10-year yields rose modestly in March from 0.06% to 0.07%.

ASX 200 Share Movements

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

BEST PERFORMERS		WORST PERFORMERS	
SPOTLESS GROUP HOLDINGS	32.32%	RESOLUTE MINING	-19.25%
A2 MILK CO	23.98%	FLETCHER BUILDING	-16.11%
NINE ENTERTAINMENT CO HOLDINGS	19.52%	OZ MINERALS	-15.81%
BRICKWORKS	18.20%	DOWNER EDI	-12.70%
AUSTRALIAN AGRICULTURAL CO	16.90%	HARVEY NORMAN HOLDINGS	-12.04%

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

BEST PERFORMERS		WORST PERFORMERS	
WHITEHAVEN COAL LTD	356.49%	BELLAMY'S AUSTRALIA LTD	-59.38%
FORTESCUE METALS GROUP LTD	144.31%	ISENTIA GROUP LTD	-56.77%
RESOLUTE MINING LTD	140.74%	VOCUS COMMUNICATIONS LTD	-47.54%
WORLEYPARSONS LTD	104.65%	ESTIA HEALTH LTD	-43.19%
BLUESCOPE STEEL LTD	98.06%	TPG TELECOM LTD	-38.54%

Economic News

Australia

On 4 April, the RBA left the cash rate on hold at 1.50%, where it has been since the August 2016 cut. In his speech delivered that evening, Governor Philip Lowe spoke of the continued improvement in global conditions, noting “the point of maximum global monetary stimulus looks to have passed”, but expressed concern at “a possible retreat from an open rules-based international trading system.” On the domestic side, the housing market continues to be a source of consternation, with continued growth in the Melbourne and Sydney markets. While arrears rates are low, slow wage growth is a drag on the ability of households to pay down debt.

The unemployment figures for February showed an increase in employed persons of 5,200 in trend terms, although in seasonally adjusted terms employment fell by 6,400. The good news was the resumption of growth in full-time employment, which rose 27,100 in seasonally adjusted terms, following January’s fall of 44,800. The unemployment rate remained steady at 5.8% and the participation rate held firm at 64.6%. Labour market underutilisation remains a concern for the RBA, as well as the slower than expected pace of wage growth.

The AIG Manufacturing Index expanded for a sixth consecutive month in March, posting 57.5 but down 1.8 points on February. All seven activity sub-indices were in expansion, with gains from New Orders (62.6) and Sales (57.7), while Production (54.1) and Employment

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(54.1) slowed. Higher prices for coal and other commodities, along with large infrastructure projects, have been supportive of manufacturing activity.

The Westpac Melbourne Institute Index of Consumer Sentiment rose by a modest 0.1% in March, from 99.6 to 99.7, with optimists and pessimists in more or less equal numbers. The most-recalled news categories remain 'economic conditions' and 'budget and taxation'. While the Index of Unemployment Expectations showed that most respondents expected unemployment to fall, the 'Family finances compared to a year ago' component fell by 5.3% to the lowest point since June 2014, indicating that respondents are particularly concerned about their personal finances.

Retail turnover fell a seasonally adjusted 0.1% in February, following a rise of 0.4% in January. Increases in turnover came from department stores (0.8%) and the major food retailing group (0.3%), while decreases came from clothing, footwear and personal accessory retailing (-2.5%) and household goods retailing (-0.4%).

Australia's balance on goods and services recorded a surplus of $3.574b in February, building on January's surplus of $1.503b. The largest increases in Australia's goods exports came from non-monetary gold ($352m) and coal ($238m), while rural goods exports fell (-$195m). Imports of general merchandise (-$1.574b) and consumption goods (-$859m) also fell.

Global

Following its 25bp hike in December, the FOMC voted to increase the funds rate by a further 25bps at its March meeting. The current range of 0.75–1.00% is still accommodative, helping to provide some further strength in the labour market and return to the 2% inflation target. While the Fed has clearly signalled a resumption of the tightening cycle, the return to normalised rates will likely be a slow process. According to the much-analysed 'dot plot' for the March quarter, the median view of committee members is for two more hikes in 2017, with the target range moving to 2.00–2.25% in 2018 (with three participants suggesting a rate of 3.00% or higher).

The 'third estimate' of US Q4 GDP showed a revised annual growth rate of 2.1%, up from the second estimate reading of 1.9% and beating the market's expected 2.0%. Profits from non-financial corporations fell by US $60.4b, in contrast to the $66.4b increase in Q3, with the settlement between Volkswagen's US subsidiary and federal and state governments weighing heavily. The Atlanta Federal Reserve is forecasting GDP to rise at an annual rate of 1.2% in Q1 2017.

The ISM manufacturing PMI fell to 57.2 in March, down from 57.7 in February, representing seven straight months of expansion. New Orders (64.5) slowed slightly, but remain strongly in expansion after surging 7.2 pts in December. Employment was the big mover, rising 4.7 pts to 58.9, while Production fell -5.3 pts to 57.6 but remaining firmly in expansion. Inflation appears to be taking hold, with the Prices component increasing a further 2.5 pts to 70.5.

January's non-farm payrolls delivered 235,000 new jobs in February versus an expected 190,000, pushing the USD higher and firming expectations for the Federal Reserve's rate hike. Annual hourly earnings rose by a healthy 2.8% on an annual basis. Construction employment increased the most (58,000), with significant gains in manufacturing (28,000) and health care employment (27,000), while retail trade employment fell (-26,000). A broader view of unemployment that includes discouraged workers and those holding part-time jobs for economic reasons dropped to 9.2%, its lowest level since April 2008.

US prices rose by an unadjusted rate of 2.7% over the 12 months to February. The index for all items less food and energy rose 2.2%. US consumers saw a fall in energy prices in February, matching retreating crude oil prices, while tighter labour market conditions are also adding to price and wage growth. The core PCE index – the Fed's preferred measure – rose 1.8% annually, up from 1.7% in January and edging towards the Fed's 2% target.

On 30 March, Britain formally invoked Article 50, following convincing support from both houses of parliament for the European Union (Notification of Withdrawal) Bill. The letter to European Union President Donald Tusk expressed the UK's desire to leave the single market, but also included new intricacies, such as an explicit desire to include financial services in any future trade deal.

While the Dutch election passed the markets by without much commotion, the main event will be France's national election on 23 April. A major Ifop-Fiducial poll held in early April showed support for Le Pen still sitting at 25%, equal with En Marche! candidate Emmanuel Macron, who has moved up from 21% since the start of February. Meanwhile, Republican Francois Fillon has seen his support fall from 21% to 17.5%, while Socialist Party candidate Benoît Hamon has fallen from 18% to 10%. The most recent Harris Interactive poll, which followed the television debate between the candidates, has Macron leading Le Pen 25% to 24%.

Euro area inflation fell to an estimated 1.5% for March, down from 2.0% in February. The energy component was again a major contributor to inflation, rising 7.3%, while non-energy industrial goods rose only 0.2%. Core inflation (excluding energy, food, alcohol and tobacco) moved from 0.7% to 0.9%, and has remained stubbornly low since the GFC. The euro area unemployment rate fell from 9.6% to 9.5% in February, remaining the lowest rate since May 2009. Youth unemployment is still very high (19.4%), while significant dispersion still exists between member states.

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China's official PMI survey showed Chinese manufacturing entered its eighth month of expansion, with the March figure coming in at 51.8, slightly above the expected 51.6. The Caixin PMI, based on a survey of smaller manufacturers, fell from 51.7 in February to 51.2, slightly lower than the expected 51.6. Inflation for February was 0.8% y/y, well below the expected 1.7% and down from 2.5% in January.

Brazil's economy remains in contraction, with GDP falling 0.9% in Q4 and 2.5% y/y. Unemployment remained steady at 13.2%, but has been rising steadily from 6.9% in January 2016. Russia's inflation continues to fall, reaching 4.3% y/y in March – the lowest rate since July 2012 – while unemployment is steady at 5.6%. India's inflation rate was 3.7% in March, up from 3.2% in February. Following the shock decision to demonetise Rs 500 and 1,000 notes, the pace of cash withdrawals in India has slowed, and the economy has begun to adjust to the new currency system, although not without significant dislocations.

Commodities

Metals were mixed in March, with Nickel falling heavily in the start of the month to end 8.7% lower. Copper was down 2.3% after being largely flat through January and February, and Zinc was down -1.9%. Tin (+4.9%) and Lead (+3.7%) moved higher, as did Aluminium (+2.0%), which reached its highest level since May 2015. The price of iron ore delivered to Qingdao in China tumbled 11.9%, from US $91.27 to $80.39/t, falling steeply in the second half of the month.

After building through January and February, Gold had a rocky month in March, losing nearly US $50/oz early on before recovering to end the month at $1249.20/oz (0.1% higher on the start). Gold appeared to take on new life following the Fed's rate hike, indicating the future path of tightening is perhaps not as aggressive as investors were expecting. The Brent crude oil spot price moved lower from US $53.36 to $52.20/b, while the WTI crude price rose slightly from US $54.00 to $50.54/b (-1.9%).

Currencies

The AUD fell 0.4% against the USD in March, from 0.7657 to 0.7629, after hitting a mid-month high of 0.7731 (the highest rate since November 2016). The AUD fell 0.8% in trade-weighted terms, losing against most major currencies, including EUR (-1.1%), JPY (-1.6%), GBP (-1.7%), but gaining against the NZD (+2.3%).

The US Dollar Index closed the month 0.8% lower, falling against major currencies including EUR (-0.7%), JPY (-1.2%), GBP (-1.4%), and CHF (-0.3%). After gaining in the wake of the US election, the USD has taken a breather through Q1 2017, but generally remains strong, with future Fed hikes ensuring continued strength in the near term, along with a potentially more recalcitrant ECB.

The Mexican Peso (MXN) recovered big in March, gaining 7.4% against the USD, and has now moved back to its pre-US election level.

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