Month in Review

Index returns at end November 2018 (%)

Australian Equities	1 mth	3 mth	6 mth	1 yr	3 yr	5 yr	10 yr
S&P/ASX 200 Accumulation Index	-2.21	-9.28	-3.67	-0.96	7.69	5.83	8.98
S&P/ASX Small Ordinaries Accumulation Index	-0.37	-10.25	-7.98	-1.63	10.39	7.07	7.77
Global Equities							
MSCI World TR Index (AUD)	-1.79	-6.57	2.12	4.67	8.83	12.19	10.24
S&P 500 TG Index (AUD)	-0.97	-5.32	6.75	10.48	11.87	16.22	13.01
FTSE 100 TR Index (AUD)	-4.64	-7.90	-7.80	-2.67	1.38	4.41	5.82
MSCI Emerging Markets NR Index (AUD)	1.06	-6.36	-6.63	-5.50	9.13	6.57	7.89
Real Estate Investment Trusts (REITs)							
S&P/ASX 300 A-REIT Accumulation Index	-0.27	-4.87	0.78	1.64	8.36	11.86	9.26
FTSE EPRA/NAREIT Dev. NR Index (AUD Hgd)	3.58	-1.56	2.63	3.26	5.67	8.54	13.14
Fixed Interest							
Bloomberg Ausbond Composite 0+ Yr Index	0.24	0.30	1.76	2.45	3.30	4.47	5.16
Bloomberg Ausbond Bank Bill Index	0.15	0.48	0.99	1.91	1.93	2.17	3.10
Barclays Global Aggregate TR Index (AUD Hgd)	0.45	-0.16	0.32	0.45	2.99	4.44	6.47

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 Index returned -2.2% through November as Australian shares appeared to miss out on the market bounce experienced in the US and Asia. Following October's volatility and market drawdown, losses were stemmed in the Information Technology sector (+1.0%), with Wisetech Global (+16.5%) and Afterpay Touch (+15.5%) partially recovering, while employee share plan provider Computershare (-8.2%) was down following the completion of its acquisition of Swiss-based Equatex Group. In a reversal of recent fortunes, it was the Financials sector (+1.4%) that drove optimism through the latter part of November, with gains from Platinum Asset Management (+10.4%) and Insurance Australia Group (+6.6%) while the major banks saw mixed results.

After spiking in October, the ASX 200 VIX remains elevated, ending November above 17 points as investors prepare for a possible end to low-volatility conditions seen through most of 2017 and 2018. Small cap shares fared relatively well through November, falling only 0.4%, although over the past 12 months they remain the underperformers, returning -1.6% compared to -1.0% from the ASX 200 Index. The Energy sector (-10.4%) was the hardest hit in November, with Santos (-16.9%) and Beach Energy (-13.4%) leading the losses with oil prices declining sharply on rising US output and slowing global economic growth rates.

Global equities

Global shares fell 1.9% in Australian dollar terms but rose 0.8% in local currency terms. Plunging oil prices brought US shares under pressure in November but the S&P 500 Index managed to end the month 2.0% higher after Fed Chair Powell backtracked on hawkish comments, hinting that the Fed may need to slow the pace of tightening. In early December, markets reacted favourably to news of a halt to new trade tariffs during a meeting between US President Trump and Chinese President Xi Jinping at the G20 summit in Argentina.

Emerging markets also rebounded from October's weakness, driven by a recovery in Chinese equities. In the US, the Health Care sector (+6.8%) was November's biggest gainer, benefiting from the mid-term election results, which saw the Democrats reclaim the House of Representatives. Interest rate sensitive sectors including Real Estate (+5.3%) and Utilities (+3.1%) were supported by a fall in long-term Treasury yields, while a stabilisation in commodity prices (outside of energy) resulted in gains for Materials (+3.8%). Japan's Nikkei 225 Index returned 2.0% in November while the STOXX Europe 600 Index lost 1.1%, with falling energy prices and the possibility of a failed Brexit deal weighing on returns.

REITs

The S&P/ASX 200 A-REIT Index returned -0.4% in November, with positive gains from Charter Hall Retail REIT (+6.4%) and Shopping Centres Australasia (+2.7%) as non-discretionary retail continues to find favour in the market. A-REITs have outperformed the ASX 200 Index over the past year, driven in part by growth in e-commerce and the demand for warehouse space, which has resulted in strong rental growth for industrial property. Oxford Property Group's takeover of Investa Office Fund became effective the start of December and

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Month in Review

is scheduled to be implemented mid-month. Cromwell Property Group (-3.3%) believes commercial property in Australia is at or close to cyclical highs, and recently announced plans to acquire 23 assets throughout Europe for A$605 million. Recent market volatility saw healthcare property specialist Heathley defer plans to list a $528 million REIT despite interest from medical and property funds. Service station owner Viva Energy REIT (-5.1%) was the biggest loser through November. A recovery in US REITs saw the Bloomberg US REIT Index rise 4.4% in local terms, with the biggest gains from Health Care (+7.4%), Apartments (+7.4%) and Single Tenant property (+5.0%).

Fixed income

Global bonds, measured by the Barclays Global Aggregate Index, returned -2.6% in November in AUD terms and 0.5% in AUD hedged terms. The US 10-year Treasury yield finished November at just under 3.0%, following a high of 3.26% earlier in the month. Early December saw a significant flattening of the yield curve as global growth concerns and dovish Fed comments led to a rally in government debt, with the 10-year yield falling to 2.92% while treasury bill rates rose. Long-term inflation expectations priced between Treasury Inflation Protected Securities (TIPS) and nominal Treasuries have held above 2.0% although the spread appears to be narrowing. Towards the end of November Fed Chair Powell stated that the funds rate was "close to neutral", which the market interpreted to mean a potentially less restrictive monetary policy going forward.

In Australia, the AusBond Composite Index returned 0.24%, with Treasuries returning 0.32% and corporate debt 0.08%. The Australian 10-year Treasury yield fell from a high of 2.76% in November to end the month at 2.59%, falling further through December to 2.44%. Emerging market yields were mixed, with Turkey's 10-year yield stabilising at around 7.5% while Argentina's 10-year yield rose back above 10.0%.

ASX 200 share movements

S&P/ASX 200 share performance for the month to November

Best performers		Worst performers	
G8 Education	36.59%	LendLease Group	-28.07%
Appen	30.64%	CYBG	-25.82%
Orocobre	29.73%	BlueScope Steel	-21.85%
Trade Me Group	27.35%	Fletcher Building	-19.75%
Costa Group Holdings	24.75%	Santos	-16.87%

S&P/ASX 200 share performance for the year to November

Best performers		Worst performers	
Afterpay Touch Group	188.40%	Syrah Resources	-60.44%
Bravura Solutions	136.08%	Automotive Holdings Group	-53.42%
Appen	95.72%	AMP	-49.69%
Altium	74.36%	Estia Health	-40.60%
Saracen Mineral Holdings	65.22%	Bellamy's Australia	-36.62%

Economic News

Australia

The housing market continues to dominate the headlines in Australia. House prices are down 7.8% in Sydney and 5.2% in Melbourne over the past year, and lending to investors and 'upgraders' has slumped as banks tighten lending criteria. The RBA sees the correction in house prices and the tightening of lending conditions as a healthy development, reducing financial stability risks and potentially prolonging the cycle. **GDP growth** slowed significantly in the September quarter, falling to 0.3% (2.8% year-on-year) from a rate of 0.9% (3.4% year-on-year) in the June quarter. Net exports and government spending were solid contributors to growth, while household spending was soft, growing 2.5% year-on-year. The results bring into question the RBA's base case assumptions for growth. The economy would need to grow 1.3% in the December quarter to match the RBA's growth forecast of 3.5% for the 2018 calendar year—a highly unlikely outcome.

Meanwhile, solid employment growth and evidence of a moderate lift in wage growth are supporting economic conditions. Employment growth defied expectations of a slowing in momentum, with October recording an additional 42,300 full-time jobs, offset by a fall in part-time jobs of 9,500. The **unemployment rate** remained steady at 5.0% in seasonally adjusted terms and fell 0.1 points to 5.1% in trend terms—it's lowest rate since

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Month in Review

early 2012. Unemployment rates remain the lowest in Victoria and New South Wales, which have seen the largest increase in employment over 2018, while higher rates persist in Queensland and Western Australia, which have experienced more moderate growth. Monthly hours worked in October rose by 6.1 million to 1,764.4 million while the participation rate rose 0.1 points to 65.6%.

The **AIG Manufacturing Index** dropped 7.0 points in November to 51.3, indicating a substantial slowing in growth for the sector. New orders (-10.1 points to 48.7) fell into contraction and, while the series is volatile month-to-month, the sub-index has been trending down since the start of 2018 and has been particularly weak in the metals sector. Production (-9.8 points to 51.8) also slowed significantly in November, while input prices (+2.2 points to 75.0) continued to rise, reflecting ongoing issues with high energy input costs, while the effects of falling oil prices have yet to flow through the supply chain.

The Westpac Melbourne Institute **Index of Consumer Sentiment** rose from 101.5 to 104.3 in November, recovering from a mild setback in the September quarter. This might bode well for the Christmas retail season, although the response to Christmas spending plans shows a third of Australians expect to spend less on gifts then they did last year. The 'finances, next 12 months' sub-index rose a solid 3.2 points over the month, while the 'time to buy a dwelling' index is up 17% on last year, suggesting falling prices are starting to attract buyers.

But whether this improved confidence is translating into more money in retail tills is less certain. **Retail turnover** rose a modest 0.3% in October on the back of a weak September quarter, with a downturn in restaurants and a disappointing month for the major food retailing group, while department stores have struggled to bounce back from negative turnover growth in the first half of 2018. Given a combination of falling home prices, the return of financial market volatility, and weak wage growth, behaviour may speak louder than sentiment in the consumer sector.

Australia's current account deficit narrowed slightly in the September quarter from $12.056 billion to $10.688 billion. While trade contributed 0.4% to Australia's September GDP growth, performance was driven less by export growth (+0.1%) and more by a reduction in imports (-1.5%). Non-rural goods contracted by 1.8%, including a $1.375 billion drop in exports of metal ores and minerals. Services exports rose 4.5% over the quarter, helped by the ongoing demand for education exports and a lower Australian dollar.

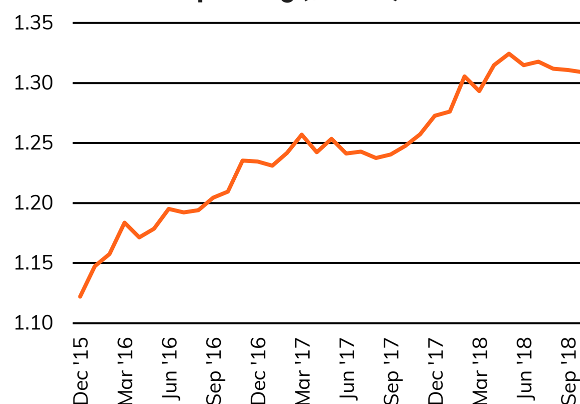
Global

At least for the near-term, the US growth story appears positive, with broad-based momentum supported by fiscal policy measures and robust consumer spending. Wage growth broke above 3% year-on-year in November and may squeeze higher as labour market conditions continue to tighten. However, the US economy is likely to face headwinds from the lagged effects of interest rate tightening and fading fiscal stimulus, as well as a stronger US dollar which threatens to put a brake on activity.

US **September quarter GDP** grew by an annualised 3.5% according to November's second estimate, in line with October's advance estimate and economists' expectations. After-tax corporate profits grew 3.3% after rising at a 2.1% pace in the June quarter, while consumer spending was weaker than expected in the September quarter, revised down from 4.0% to 3.6%, but still the main driver of growth. Non-farm payrolls increased by 155,000 in November, lower than the expected 200,000 but still enough to sustain momentum.

The **ISM manufacturing PMI** rose 1.6 points in November to 59.3, with momentum building in New Orders (+4.7 points to 62.1), reflecting strong demand, and Employment (+1.6 points to 58.4), which is supporting production, but respondents noted that labour market constraints remain a drag on capacity. The Prices sub-index (-10.9 points to 60.7) came in well below estimates, but still points to rising cost pressures. Data from the Commerce Department show total construction spending fell 0.1% to $1.31 trillion in October, below the expected 0.4% rise and the third straight month of contraction.

US construction spending ($trillion)



Source: Commerce Department

Eurozone GDP growth is disappointing, rising 0.2% in the September quarter according to November's estimate and well down on the expected 0.4% growth. In Germany, GDP actually contracted by 0.2% after growing 0.5% in the previous quarter, representing the first fall in three years as new emissions tests resulted in a cut in car production. Carmakers have slowed production until they clear a backlog of new vehicles due to the need to prove the new emissions standards are being met. The IHS Markit Eurozone Composite PMI suggests the slowdown in growth is continuing

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Month in Review

through the start of the December quarter, with an export slowdown linked to rising trade tensions, growing political risks and tightening financial conditions.

Political risk is rising in Italy as the European Commission rejected the government's draft budget, with the Commission affirming there was "no alternative" but to demand changes as the planned increased deficit broke EU fiscal rules and previous commitments. In the UK, the Bank of England warned that a disorderly exit from the EU could result in a decline in economic output of up to 8.0% in the first year and a rise in the unemployment rate to 7.5% under a worst-case scenario.

The **Chinese economy** continues to show signs of slower growth, although the authorities have recently begun stepping up stimulus measures. The **September quarter GDP growth** result of 6.5%, down from 6.7%, was the slowest since the Global Financial Crisis, while PMI readings for the manufacturing sector are at levels last seen in mid-2016 when China was emerging from a period of strong capital outflows, weak property markets, and financial market instability. Restricting local governments' access to credit has led to a major slump in infrastructure investment.

State-owned enterprise investment growth has slowed to 1.8%, while investment in electricity and power production has contracted by 9.6% over the year. **Retail sales** have slowed through 2018, reaching 8.6% in October, or around 6.0% in real terms. The phasing out of preferential taxes on automobiles has seen a sharp drop in auto sales. In response, the authorities have approved tax cuts to take effect in January. For now, the stimulus put in place is relatively modest, but more could be forthcoming if the trade war continues to escalate.

Commodities

Oil prices saw significant falls through November, with the Brent crude price falling from US$74.84 per barrel to $57.71 while WTI fell from $65.31 to $50.78 as a surprise inventory build caught markets unawares. Metals were mixed through November, with Copper (+3.2%), Lead (+2.6%), Zinc (+2.0%) and Aluminium (+0.2%) higher, while Nickel (-2.6%) and Tin (-3.7%) were lower. Gold rose 0.6% to end the month at US$1,220.52/oz, down from its April high of $1358.31.

Currencies

The Australian dollar rose 3.3% against the US dollar in November and appears to have found support in the low US 70 cents region, ending the month at around 73 cents. While purchasing power parity suggests the high 60s is 'fair value', relatively strong prices for some of Australia's key commodities such as iron ore suggest the dollar may be slightly oversold based on a fundamental terms of trade valuation model. The focus of markets has been on relative interest rates, which is why the US dollar has risen through 2018.

The Australian dollar rose 2.3% in trade-weighted terms through November, gaining against the USD (+3.3% to 0.73), EUR (+3.2% to 0.65), JPY (+3.8% to 82.98) and GBP (+ 3.3% to 0.55). Over the three months to the end of November, the Australian dollar has risen 1.6% against the USD, rising from a low of 0.7053 in August to finish November at a high of 0.7322. On a trade-weighted basis the Australian dollar has appreciated 1.8% over the past three months, gaining against the USD (+1.6%), GBP (+3.3%), EUR (+4.2%) and JPY (+4.0%).

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