Market Highlights – April 2015

China stimulus drives market higher

Central banks continued to dominate headlines in April. It was China's turn to take centre stage, with authorities slashing the amount of money banks need to keep aside for lending (the reserve requirement ratio). The government also undertook several measures to reduce the debt burden of local governments and boost the struggling housing sector. This followed the release of data which showed that, while China's annual growth was in line with the Government's target of 7%, the economy was considerably weaker in the latest quarter.

These measures by Chinese policy makers saw the MSCI China share index leap 18% in local currency terms in April. Improved confidence about prospects for the Chinese economy and a seasonal pickup in activity saw commodity prices lift late in the month, supporting commodity producing emerging markets (EM) such as Brazil. In total, global EM shares returned 4.3% in unhedged Australian dollar (AUD) terms. This was despite a sharp fall of almost 10% in Indian shares; still Indian shares rose 34% over the past year.

Developed markets posted a 1.3% return (hedged AUD terms) in April, underpinned by a 3.2% gain in Japanese (TOPIX) shares in Yen terms. US shares also moved higher as company earnings, which had been revised down owing to a higher US dollar (USD), beat expectations and rising oil prices reduced concerns over the profitability of the US energy sector. By contrast, European shares struggled, with German shares falling more than 4%, as the euro rose in response to better economic activity and concerns continued to rise over the potential that Greece would be forced out of the euro zone.

A rise in the AUD and lower USD weighed on market returns

Currency movements were a significant driver of returns in April. Stronger employment data and comments by the Reserve Bank of Australia (RBA) Governor expressing concern over rapid house price increases prompted markets to reduce expectations for rate cuts in Australia over the remainder of 2015. At the same time, after rising sharply over the past year, the USD showed signs of fatigue, with weaker growth readings and the recent lowering of interest rate projections by the US Federal Reserve (the Fed) seeing the USD decline against most currencies. The combination of these two factors saw the AUD rise 3.9% against the USD to US78.9c, having briefly moved above US80c during the month.

The rise in the AUD saw global shares produce a negative return of 0.8% on an unhedged basis in April. Meanwhile, the combination of higher interest rates and a stronger AUD was a negative for Australian shares. These factors, along with concerns over higher capital requirements for banks, weighed on the local share market which produced a negative return of 1.6%. This followed a rapid gain of 10% in the March quarter (boosted by falling interest rates and a weaker AUD). Financial stocks led the decline in April, falling almost 5%. By contrast, a rebound in commodity prices drove a 4.3% rise in resources shares in the month.

Signs of inflation drive up bond yields

In 2014, lower inflation cemented market expectations for continued low central bank rates, driving bond yields to historically low levels. This was particularly significant in Europe, where headline inflation turned negative at the end of 2014, prompting the European Central Bank (ECB) to announce a program to purchase government bonds. But in April, there were further clear signs of a pickup in euro zone growth combined with a stabilisation in headline inflation reflecting the sharp fall in the euro exchange rate and signs of a pickup in oil prices. Inflation expectations in the US also moved up as wages data showed an acceleration in labour costs. These have seen markets reassess the inflation outlook globally, driving a rise in bond yields. As a result, global fixed income produced a negative return of 0.4%.

Not surprisingly, after falling more sharply over the past year on deflation concerns, the rise in bond yields was largest in Europe. German 10 year bond yields finished the month up 19 basis points (bps), albeit still at an extremely low level of 0.37%, while US yields rose by a less severe 11bps. The larger rise in European yields also reflected a rise in real yields due to stronger growth as well as increased concerns over a potential exit of Greece from the euro zone. The latter saw peripheral European bond yields rise to a greater extent than in Germany, with Italian and Spanish bond yields both rising 26bps in April.

As noted above, stronger employment data and comments by the RBA Governor saw markets reduce expectations for further rate cuts over the rest of 2015. This saw the Australian fixed income market underperform its global counterpart with a negative return of 1.1%.

Finally, the rise in global interest rates weighed heavily on the listed property market after it had benefited significantly from the trend of declining bond yields over the past year or so. In the month of April, listed property posted a negative return of 3.5%.

Major asset class performance as at 30 April 2015 (%)

Sector	Index	1 month	3 months	12 months
Australian Shares	S&P / ASX300 Accumulation	-1.6	5.1	10.2
Global Shares (hedged)	MSCI World ex Australia (hedged)	1.3	7.1	17.2
Global Shares (unhedged)	MSCI World ex Australia (unhedged)	-0.8	5.3	26.7
Global Emerging Markets (unhedged)	MSCI Emerging Free Net in AUD (unhedged)	4.3	8.1	26.6
Global Small Companies (unhedged)	MSCI World Small Cap ex Australia	-2.3	6.0	25.3
Global Low Volatility Shares (unhedged)	MSCI World Minimum Volatility Index ex Australia (unhedged)	-1.2	1.7	25.0
Global Listed Property	FTSE EPRA/NAREIT Developed Rental Index ex Australia (hedged)*	-3.5	-2.8	16.0
Cash	Bloomberg Bank Bill	0.2	0.6	2.7
Australian Fixed Income	Bloomberg Composite Bond All Maturities	-1.1	-0.1	8.9
Australian Inflation Linked Bonds	Bloomberg Government Inflation Index: All Maturities	-2.0	0.7	13.7
International Fixed Income	Barclays Global Aggregate Bond Index (hedged)	-0.4	0.0	8.9

Source: JP Morgan & ANZ Global Wealth *FTSE EPRA/NAREIT Developed Index ex Australia (hedged) before April 2015

Economic highlights by region

US

The US economy slowed to a standstill in the March quarter, with final sales of goods and services declining in the quarter. As we have noted recently, the weak result was in part due to poor winter weather. That said, the slowing also appears to reflect the impact of the higher USD on manufacturing activity. Though recent indicators have pointed to a relatively slow start to the June quarter, survey measures of services activity remain consistent with robust growth, while lower claims for jobless benefits indicates further falls in the unemployment rate. At the latest meeting, the Fed remained relatively confident in the economy's prospects, leaving the door open for rates to rise later this year should growth strengthen as it expects.

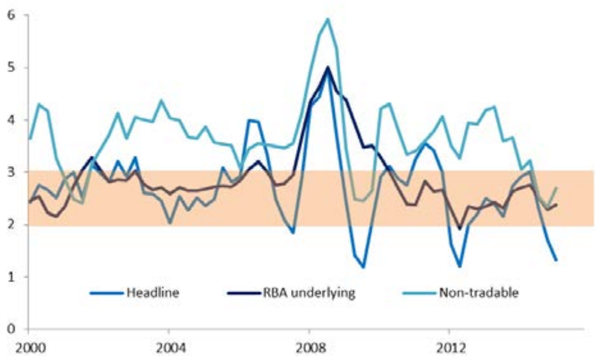
US GDP Growth (%)

Source: Thomson Reuters Datastream

Australia

Inflation remained relatively subdued in Australia during the March quarter. Headline consumer prices rose by 1.3% over the year to March, clearly below the RBA's 2-3% target range. The underlying measures that the RBA focuses on when making its policy decisions remained in the lower half of the target range with average annual growth of 2.4%, in line with the average recorded for these series in the past three years. Domestically generated inflation (non-tradable) remained at a historically low level. On the activity front, the big news was a sharp rise in employment in March, which saw the unemployment rate decline to 6.1%. Retail spending also rose strongly, though weaker consumer confidence casts doubt over the sustainability of this recent strength. The RBA decided at its meeting in May to reduce the cash rate by a further 0.25% to 2.00%.

Australian Inflation (%)*



Source: Source: ABS, ANZ Global Wealth

*excludes impact from GST introduction in 2000

Europe

Euro zone growth remained strong in the early part of the June quarter despite some softening in business surveys in April. Meanwhile there were clearer signs of a pickup in inflation; after falling to -0.6% in January, headline inflation in April was flat. Elsewhere, concern continued to escalate over the possibility that Greece will be forced out of the euro zone single-currency region. With the Greek economy again losing momentum, the Greek government is reluctant to undertake further painful restructuring measures that its creditors (the so called 'Troika' consisting of the ECB, European Government and the International Monetary Fund) are demanding as part of the re-negotiation of its debt bailout. Time is running out with reports that Greece will run out of funds over the next couple of weeks.

Asia

Chinese GDP grew 7.0% in the first quarter, the lowest level since the GFC. This was broadly reflective of the slowdown across a number of activity indicators in the early part of the year. The slowdown prompted policy makers to announce further easing measures, including a cut to the reserve requirement ratio of 100bps for major banks. By lowering the amount of reserves banks are required to hold for lending, market liquidity is expected to rise and bring down the cost of borrowing. These measures, combined with cuts in the official interest rate, should provide enough of a boost to allow the government to defend its target of around 7.0% growth in the economy this year.

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