Australia Monthly Wrap I March 2014

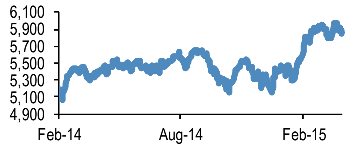
Scratching at the ceiling

- **Key market drivers.** Global markets declined at the start of March as speculation around an imminent rate hike in the US mounted. Subsequent Fed commentary suggesting a slower pace of rate increases saw a relief rally towards mid-March allowing global indices to reclaim some lost ground. Despite this, the MSCI World index ended the month lower (-1.8%) as falling commodities prices led a steep decline in Materials stocks. The ASX200 traced a similar path and, as a result, ended the month largely unchanged (-0.1%, accumulation) despite coming close to breaching the 6,000 point mark several times during the month. At a sector level, Materials (-4.5%, accumulation) was the key laggard whilst Banks (+2.5%, accumulation) and Healthcare (+2.1%, accumulation) outperformed. The S&P500 ended the month down 1.7% whilst the FTSE 100 also declined (-2.5%). Europe, as measured by the Euro Stoxx 50, outperformed (+2.7%) with QE purchasing beginning at the start of the month as did Japan (Nikkei 225 was up 2.2%).

- **Economic news.** The **Fed**'s March statement on monetary policy appeared to delay the much-anticipated rate hikes, leaving the Fed funds target range at 0 to 0.25%. Domestically, the **RBA** also left rates unchanged at 2.25% with the central bank commenting that domestic growth was continuing at a “below-trend” pace. In China, **PBOC** governor Zhou Xiaochuan stated that growth had slowed “a bit” too much and that policy makers had scope to respond both with interest rates and quantitative measures following a below-trend February growth print of 6.3% y/y.

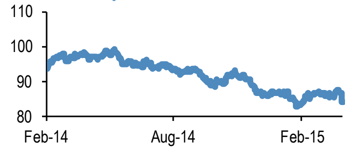
- **Major company news.** Corporate activity picked up during March, with capital management, takeovers and equity raisings all featuring. Orica and Boral announced on-market buybacks; IIN and PanAust received takeover bids from TPG and Guangdong Rising H.K. respectively; and Macquarie Bank raised $500m to partially fund the acquisition of a US$4bn aircraft leasing portfolio. In addition, BHP Billiton introduced details of spinoff, South 32, to the market. Management changes also featured with CEO departures from Orica, Ardent Leisure and Myer.

ASX 200 Price Index



Source: Bloomberg

MSCI Australia relative to MSCI Asia Pacific ex Japan, US$ terms



Source: Bloomberg

Sector and stock returns%

Ranked sector returns				Top and bottom ASX200 universe stocks			
One month		Three months		One month		Three months	
Technology	+3.2%	Consumer Disc.	+14.3%	iiNet	+34.6%	Northern Star	+54.4%
Banks	+2.5%	Banks	+14.3%	Panaust	+31.3%	Toll	+50.4%
Health Care	+2.1%	Utilities	+13.7%	TPG Telecom	+20.3%	Regis Healthcare	+47.8%
Industrials	+1.9%	Health Care	+11.8%	Primary HC	+16.5%	Domino'S Pizza	+47.5%
Telco's	+0.1%	A-REITs	+9.4%	Ainsworth Gaming	+15.6%	Iluka Resources	+42.9%
Consumer Disc.	-0.1%	Telco's	+9.1%				
Consumer Staples	-0.6%	Industrials	+9.1%	Sirtex Medical	-41.5%	Bradken	-61.0%
Utilities	-0.6%	Materials	+7.7%	Regis Resources	-31.0%	Mma Offshore	-46.8%
A-REITs	-2.1%	Technology	+7.1%	Myer	-27.0%	Ugl	-33.6%
Materials	-4.5%	Consumer Staples	+4.0%	Mma Offshore	-25.0%	Kathmandu	-32.2%
Energy	-5.7%	Resources	+3.1%	G8 Education	-22.9%	Regis Resources	-31.9%
Resources	-6.2%	Energy	-3.7%				

Source: Bloomberg, MSCI.

Equity review

Major Market Performance, March 2015

	Level	Change
DJ Industrials	17,776	-2.0%
S&P 500	2,068	-1.7%
NASDAQ	4,901	-1.3%
FTSE 100	6,773	-2.5%
Nikkei225	19,207	+2.2%
Euro Stoxx 50	3,697	+2.7%
ASX 200	**5,892**	**-0.6%**

Source: Bloomberg. Note: Index levels are as at close of business, 31 March 2015.

US equity market

The S&P500 declined at the start of March as fears of a Fed rate hike mounted. Fed comments that rate rises would be slower than the market anticipated sparked a relief rally towards mid-month but declining commodity prices wiped away most of these gains to see the index finish the month down 1.7% on February's close. Materials (-5.0%) weighed most heavily on the bourse with metals & mining the key underperformer within that sector. Sector winners included Health Care (+0.8%), Banks and Financials (-1.0% and -0.8% respectively) as well as Consumer Discretionary (-0.6%).

Staples rallied towards the end of the month at the announcement of a potential tie-up between Kraft Foods Group and 3G- and Berkshire Hathaway-owned Heinz. The combined businesses will have sales of more than US$28bn.

Australian equity market

The ASX200 finished March down 0.1% on an accumulation basis (-0.6% price) despite recording an intraday high just shy of the 6,000 point threshold. Sector performance mirrored that of the US with Materials coming in as the key laggard, down 4.5% (acc) for the month. Banks were a standout (+2.5%), as were the Industrials (+1.9%) and Health Care (2.1%) sectors.

M&A activity picked up in March: a bid by TPG Telecom for its smaller competitor, iiNet for $1.4bn to tap into the latter’s 975k broadband subscribers was unanimously recommended by the Board whilst a second attempt at PanAust by Guandong Rising Asset Management at a downwardly revised offer price (-26%) is still under consideration.

Other Financial Data, March 2015

	Level	Change
AU RBA Cash rate	**2.25%**	**+0bp**
US 10 yr bond yield	1.92%	-7bp
AU 10 yr bond yield	2.32%	-14bp
Australian dollar/US$	0.7607	-2.6%
LME Metals Index	2,751	-0.1%

Source: Bloomberg. Note: Index levels are as at close of business, 31 March 2015.

Bonds

Domestically, the ten-year benchmark yield fell 14 bps whilst, in the US, the ten-year benchmark yield shed -7bps following last months' increase. In Europe, yields fell across the board with Gemany's 10-year shedding 15 bps and yields in the UK (-22 bps), France (-13 bps) and Italy (-9 bps) following suit. The rally in Eurozone debt comes following the start of the ECB’s government bond-buying program which began early in the month and will cover maturities between two and 30 years. The sharpest declines in yields have been observed in longer-dated bonds with the 30-yr German yield plummeting 40 bps during the month.

Currencies

The Aussie dollar fell against the USD at the start of the month only to rally towards the end as the Fed's statement on Monetary Policy alluded to “moderated” economic growth and left interest rates unchanged. Continued USD appreciation (ICE index, +3.3%) saw the Aussie end the month down 2.5% vs the greenback. More broadly, the AUD trade weighted index fell against its largest trading partners (1.2%). The Euro followed a similar pattern, losing as much as 6% against the USD during the month but regained some of this weakness to end the month down 4.1%.

Commodities

Spot **Brent crude** continued its downward trajectory at the start of March as oil production continued to reach record levels in the US. Whilst it reclaimed some ground after Saudi Arabia conducted air strikes on Yemen’s capital, raising concerns around possible supply disruptions in the surrounding oil-producing region, spot Brent nevertheless ended the month down 13.7%.

The benchmark spot **iron ore** price continued its decline for five consecutive weeks of losses and reached its low for the month of US$51.40/t on the final trading day. Declines total 28% YTD as Chinese demand continues to weaken whilst BHP Billiton, Rio Tinto and Vale push ahead with plans to increase production.

Base metals as measured by the LME index were largely unchanged (-0.1%). Of the six primary index metals, Lead, Copper and Zinc all posted gains (+6.9%, +2.4% and +1.2% respectively) whilst Aluminium, Nickel and Tin (-1.1%, -12.1% and -7.7% respectively) lost ground.

Spot gold fell 5.2% to a mid-month low before posting a one-day gain of nearly 2% following the FOMC's March 18 meeting where Janet Yellen made it clear that interest rates would not be raised until inflation lifted. The precious metal ended the month up 2.4%.

US Economy

The Fed's March 2015 FOMC statement replaced the word 'patient' in relation to approaching interest rate hikes with language stating that the current 0 to 0.25pc target range for the federal funds rate "remains appropriate". Fed Chair, Janet Yellen, warned against reading this as a sign that rate rises were imminent and stated that an April increase remained "unlikely".

The Thomson Reuters/University of Michigan **consumer confidence index** was revised up from 91.2 to 93.0 (exp. 92.0) between the preliminary and final March reports. This compared to February's reading of 95.4. The **ISM manufacturing** PMI registered 52.9, a decrease of 0.6pts vs January's reading of 53.5 (exp. 53.0). The **non-manufacturing** survey rose again to 56.9 (exp. 56.5) from 56.7 in Jan-15.

Nonfarm payrolls rose 295k in Feb-15, well above expectations of +240k. The **participation rate** fell 0.1%-pts to 62.8% (exp. 62.9%) whilst the unemployment rate fell 0.2%-pts to 5.5% (exp. 5.6%) from Jan-15's level of 5.7%.

Housing starts plunged in February, coming in at a seasonally adjusted annual rate of 897k (ecp. 1,049m), down 17% from January's rate of 1,081k. **Building permits**, on the other hand, rose 3.0% m/m (exp. +0.0%) to a rate of 1,092m vs Jan-15's 1,060m.

The headline **CPI** figure for February was flat y/y (exp. -0.1%) which compared with January's decline of -0.1%. The core measure rose 1.7% y/y (exp. +1.7% y/y) vs January's increase of 1.6% were in line with expectations.

4Q14 GDP growth came in at +2.2% (annual rate), unrevised from the forecast the government published last month.

China

Chinese Premier Li delivered the government's work report at the National People's Congress at the start of March, lowering expectations of 2015 GDP growth to "around 7.0%" from previous guidance of "around 7.5%". The government work report also canvassed a number of other major economic targets including CPI inflation of 3.0% (3.5% in 2014), M2 growth target of 12% (13% in 2014) and an FAI growth target of 15% (17.5% in 2014).

The **HSBC flash manufacturing PMI** declined 1.5pts in March to 49.2, compared to the final reading of 50.7 in February, representing an 11-month low.

93.0% of Chinese cities registered m/m **house price** declines in February, and on average, national prices declined 0.2% m/m, narrowing slightly from the 0.5% m/m decline in Jan-15.

M2 money supply growth picked up to 12.5% y/y in February (exp. +11.0% y/y) vs January's figure of 10.8% y/y. **New loan creation** came in at 1,020bn yuan, well ahead of expectations of 750bn yuan. **Total social financing** rose 1,350bn yuan compared to January's increase of 2,050bn yuan.

Australian Economy and the RBA

The **RBA** left the cash rate unchanged at 2.25% during its March monetary policy meeting. Governor Glenn Stevens commented on domestic growth continuing at a "below-trend pace, with domestic demand growth overall quite weak" and that "further easing of policy may be appropriate over the period ahead". The RBA did, however, show some concern for risks that could arise from the strong housing market in Sydney.

The NAB **business confidence** index declined to 0 (exp. +5) from +3 in January, despite the RBA trimming interest rates by 25 bps in February. The **Westpac-MI consumer confidence index** also disappointed with sentiment falling 1.2% m/m (exp. +2.0% m/m) despite an increase of 8% in the month prior.

The economy added 15.6k **jobs** in February on a seasonally adjusted basis (exp. +15k) for an **unemployment rate** of 6.3%, which printed in line with expectations and compared to last January's rate of 6.4%. The **participation** ratio fell a touch to

64.6% (exp. 64.8%), a touch lower than January's 64.7%.

Retail sales rose 0.4% m/m (exp. +0.4%) in January. Food was a significant drag, falling 0.7% m/m with retail ex-food up 1.1% m/m. Among the categories, household goods and department store sales were up 0.7% m/m and +2.2% m/m respectively.

Building approvals increased 7.9% m/m in Jan-15 (exp. -2.0%), driven by NSW and QLD where approvals trended towards apartments rather than larger dwellings.

The volume of new **housing finance commitments** to owner occupiers fell 3.5% m/m on a seasonally adjusted basis in and the value of such loans fell 1.0% m/m for the same month. Separately, the value of housing loans to investors fell by less at -0.1% m/m.

Europe

The ECB's **quantitative** easing programme kicked off on March 9 with the bank buying German and Italian bonds as a part of its €1.1trn agenda. At the same time, fears of a **Greek exit** from the eurozone mounted as the nation's creditors demanded tighter reform policies before bailout funds of €7.2bn would be unlocked.