

Market and Economics Report



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Global economy

Review: Economic data appear consistent with the view that the US recession is over. The manufacturing sector improved again with the Institute for Supply Management composite survey giving the highest reading since August 2008. The US labour market also showed signs of having stabilised and the pace of job losses is steadily falling. Other positive news was that US house prices finally appear to be stabilising after three years of falls. Since their peak, US house prices have fallen 33%. US Federal Reserve Chairman, Ben Bernanke, noted that “economic activity appears to be levelling out... and the prospects for a return to growth in the near term appear to be good”. During August, Japan’s economy also provided encouraging signs that the downturn is ending. The economy expanded by 0.9% quarter on quarter (qoq) in the June quarter, a marked improvement from the -3.1% contraction in the previous quarter. Private consumption, public investment and net exports were all up. Against this, the labour market continued to struggle with unemployment rising further to 5.7%. Chinese economic data signalled that its recovery is continuing. The European economy continued to show some signs of recovery. Europe’s real gross domestic product (GDP) figures showed a small contraction of -0.1% qoq for the June quarter, a significant improvement from the -2.5% contraction in the first quarter. Indeed, Germany and France, Europe’s two largest economies, both recorded a small expansion in the June quarter. Surveys of business and consumer sentiment across the region also suggested a slow recovery. News from the UK suggested that the recession may finally be abating. Revised GDP figures for the June quarter showed that the economy had shrunk less than expected. The Bank of England left interest rates on hold again at 0.5% and the European Central Bank left rates at 1%.

Outlook: The global recession appears to be ending. Monetary and fiscal easing seems to have gained traction, pointing to solid global growth in 2010.

Australian economy

Review: In Australia, the Reserve Bank of Australia (RBA) left the official interest rate on hold at 3.0% for the fifth consecutive month. The RBA signalled increasing optimism about the economic outlook with the implication that interest rates will soon start to rise. Australian economic data releases over August were largely positive, supporting the RBA view that downside risks to the economy have diminished. GDP rose for the second quarter in a row in the June quarter driven by consumer spending and business investment. The labour market remained resilient

with unemployment stable at 5.8% in July. Business and consumer confidence both continued to surge higher. On the negative side, retail sales fell in June and July as did housing finance in July.

Outlook: The Australian economy is likely to remain soft in the short term ahead of a sustainable recovery from later this year and through 2010, driven by global recovery, a housing upturn and stronger investment helped by fiscal stimulus.

International shares

August review: The leading measure of global shares performance, the MSCI World (ex-Australia) Accumulation Index, returned +3.6% in local currencies (or +2.5% in unhedged Australian dollar terms). The US S&P 500 Accumulation Index returned +4.5%. In the European region, the Eurostoxx Accumulation Index returned +5.8%; while the UK FTSE 100 Accumulation Index returned +7.2%. Shares in Asia were mixed as Japan’s Topix Accumulation Index returned +1.7% whereas China’s S&P/CITIC 300 Total Return Index dropped -23.7%.

Short-term outlook [six to 12 months]: After the strong rebound, a short-term correction is likely sooner or later. However, global shares are likely to provide good returns on a 12-month plus view, given the likelihood of better economic conditions in 2010 and still attractive valuations.

Medium-term outlook [five to ten years]: Improved dividend yields following the share slump and profit growth around nominal GDP growth will see medium-term returns from mainstream global shares of around 8% per annum on average.

Australian shares

August review: The Australian share market performed strongly in August, with the S&P/ASX 200 Accumulation Index returning +6.6% for the month. Investor confidence was boosted by a largely positive reporting season with earnings down, but generally ahead of expectations. Economic data also continued to surprise on the upside.

Short-term outlook: The Australian share market is vulnerable to a short-term correction. However, shares are likely to provide solid returns on a 12-month view. Valuations are attractive and interest rates are low, and shares are likely to anticipate better economic conditions and rising profits in 2010.

Medium-term outlook: Reflecting much higher dividend yields and reasonable growth prospects, medium-term returns of around 11% per annum are likely.

Real Estate Investment Trusts

August review: The S&P/ASX Property 200 Accumulation Index returned +16.0%, considerably outperforming the broader equity market. The month of August was the fifth consecutive month of positive returns for the listed property securities sector, although there continued to be a wide dispersion of returns.

Short-term outlook: Most property stocks have recapitalised, most are good value from a long-term perspective, and the credit crunch is fading. As such they should provide solid returns over the next 12 months.

Medium-term outlook: Solid yields and moderate growth prospects mean medium-term returns of around 12% per annum are likely.

International bonds

August review: International bond yields fell across the board in August as inflation fears faded, although the global economy continued to demonstrate signs of improvement. The US ten-year bond yield fell 8 basis points (bps) to 3.40% and Japan's ten-year bond yield fell 12 bps to close July at 1.31%. In the European region, Germany's ten-year bond yield fell 4 bps to 3.26%; while the UK ten-year bond yield fell 24 bps to close the month at 3.56%.

Short-term outlook: Sovereign bond yields are likely to remain low in the short term on the back of the uncertainty about the strength of an economic recovery and falling inflation.

Medium-term outlook: AMP Capital expects low returns from global sovereign bonds, reflecting low bond yields.

Australian bonds and cash

August review: The Australian long-term bond market strengthened over August, in line with global trends. The yield on the Australian ten-year bond fell 16 bps to 5.42%, but the three-year bond yield rose 15 bps to 4.95%, which saw the domestic yield curve flatten. Bank bill yields rose in August on increasing expectations for interest rate hikes. The three-month bank bill rate opened at 3.20% and closed 29 bps higher at 3.49%. Six-month bank bill yields traded similarly, opening at 3.35 and closing 48 bps higher at 3.83%. Credit markets continued to perform well over the month.

Short-term outlook: Bond yields are likely to remain low in the short term on uncertainty regarding the growth outlook and as inflation falls.

Medium-term outlook: Returns from local sovereign bonds over the medium term are likely to be poor, reflecting low yields.

Australian dollar

August review: The Australian dollar (A\$) pushed slightly higher again in August, rising against the US dollar (US\$) and the currencies of Australia's major trading partners (as per the Trade Weighted Index [TWI]), but falling against the Japanese yen (JPY). The A\$ closed the month at 84.38US cents (up 0.8% from 83.75US cents) and JPY78.44 (down 1.2% from JPY79.36). The TWI closed the month at 66.3 (up 0.6% from 65.7).

Short-term outlook: Further gains in the A\$ are likely on the back of the improving global growth and commodity outlook and the prospect for rising local interest rates.

Medium-term outlook: AMP Capital expects the A\$ to be strong over the medium term, helped by strong commodity prices.

Key financial markets

	31 August 2009	Change in one month	Change in 12 months
S&P/ASX 200 Accumulation Index	30,939	+6.6%	-8.1%
MSCI World (ex-Aust Accumulation/unhedged in A\$)	3,423	+2.5%	-15.7%
US S&P 500 Accumulation Index	1,684	+4.5%	-17.6%
Dow Jones Eurostoxx Accumulation	398	+5.8%	-16.4%
UK FTSE 100 Accumulation Index	3,078	+7.2%	-8.9%
Japan Topix Accumulation Index	1,180	+1.7%	-21.4%
S&P/CITIC 300 Total Return Index	2,603	-23.7%	+18.9%
S&P/ASX 200 Property Accum. Index	18,638	+16.0%	-34.5%
UBS Global Real Estate Investors Index	875	+13.4%	-32.7%
Aust 90-day bank bill yield	3.49%	+29 bps	-378 bps
Aust 10-year bond yield	5.42%	-16 bps	-34 bps
US 10-year bond yield	3.40%	-8 bps	-41 bps
A\$ in US cents	84.38	+0.8%	-1.5%
Trade-weighted index	66.3	+0.9%	-1.3%

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