Market View

June 2013

Read the latest market update from the Economic and Market Research team at Colonial First State.

Market overview

- Global financial markets were volatile in June, with sharemarkets falling sharply and government bond yields jumping higher.

- These market moves came after the US Federal Reserve (The Fed) provided a more positive assessment of the US economy, signalling that a moderation in its aggressive quantitative easing (QE) program could occur later this year.

- The increase in global bond yields since early May has real term premium, as bond markets have become more responsive to positive US macroeconomic data releases.

- The MSCI World Index (developed markets) fell by 2.6% in US dollar (USD) terms (+2.5% in AUD terms) in June. Following Dr Bernanke's press conference, the Index fell by 3.5% on 20 June 2013 – its largest one day fall since November 2011.

- Australian equities suffered heavy losses in June, reversing all the gains made in the first five months of 2013. Concerns over the domestic growth outlook and poor business sentiment contributed to a growing number of company downgrades. The S&P/ASX 200 Index declined by 2.5% (Accumulation Index, -2.3%) over the month.

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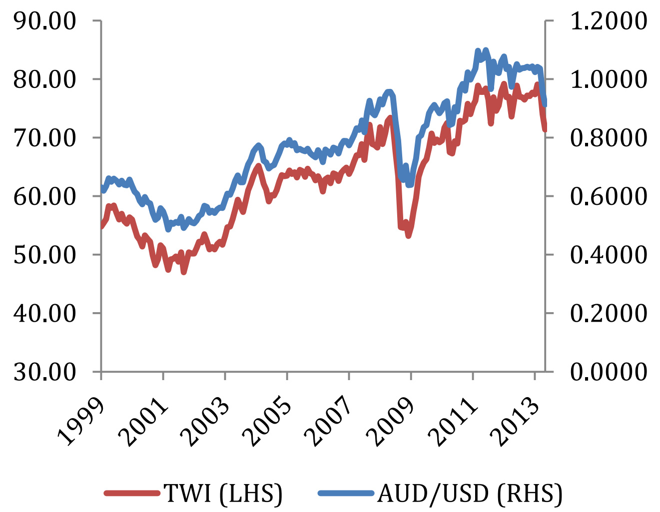
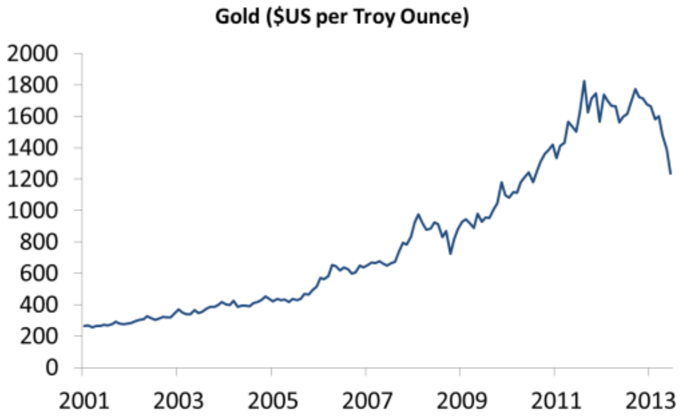
AUSTRALIAN DOLLAR UNDER PRESSURE



Source: Bloomberg as at 28 June 2013

- The Australian dollar (AUD) depreciated by 4.5% against the US dollar (USD) in June – ending the month at $US0.9138, its lowest level since October 2010.

GOLD: THE END OF AN ERA?



Source: Bloomberg as at 28 June 2013

- Commodity prices generally declined, led by gold (-11.0%), as rising short-term interest rates pushed the precious metal to a 3-year low. However, oil (+5.0%) bucked the trend, rising on supply concerns over fears that the Syrian conflict may spread.

- US economic data was mixed. The final estimate of Q1 2013 GDP expanded at 1.8% for the year, down from the previously reported 2.4%, and consumer spending increased.

- The Consumer Price Index (CPI) ticked-up in May, rising by 0.1% to 1.4% for the year. Core prices increased by 0.2% over the month to 1.7% for the year.

- The European Central Bank (ECB) kept its benchmark interest rate at 0.5% at its June meeting, with ECB President Mario Draghi saying the euro-area economy "should stabilise and recover in the course of the year, albeit at a subdued pace."

- He later provided assurances that an exit from its (ECB) exceptional monetary policy measures "remains distant".

- Bank of Japan (BoJ) Governor Haruhiko Kuroda said that the BoJ would consider fresh steps to calm markets if borrowing costs spiked again in the future, but would hold off on new measures for now, arguing that bond markets had stabilised.

- Locally, the Reserve Bank of Australia (RBA) left its cash rate unchanged at 2.75% in June, citing the positive effects from previous easing on non-mining sectors of the economy (ie the housing sector). However, the minutes from the RBA Board described the AUD as "high" despite it depreciating more than 10% against the USD in the past two months.

- Former Prime Minister Kevin Rudd displaced incumbent Australian Labor Party leader Julia Gillard, attracting 57 caucus votes to 45.

- March quarter 2013 GDP growth slowed to 0.6% and 2.5% for the year. Growth was led by a strong contribution from net exports and a gain in consumer spending. This was partially offset by detractions from capital spending and inventories.

- Employment rose by 1.1k in May. The unemployment rate fell slightly to 5.5%.

- The Westpac consumer confidence index for June rebounded by 4.7%, after plunging by 7.0% in May.

Australian shares

- Sentiment towards the Australian sharemarket continued to be affected by offshore events in June, such as expectations that the Fed would taper its QE program later in the year.

- A spike in Chinese interbank interest rates did little to support investor sentiment towards equity markets in the Asia Pacific region, in particular.

- There have been increasing concerns about a moderation in Australian economic activity. The big question remains whether the non-mining sector can offset the clear slowdown that is occurring in the mining sector.

- Several miners and companies that provide services to the sector continued to downgrade their earnings expectations in June. Various companies in this area of the market are restructuring, cutting costs and deferring capital expenditure plans.

- A number of companies in other areas of the market also issued disappointing earnings outlooks during the month, suggesting that business conditions are subdued across the broader domestic economy.

- The market weakness in May and June was disappointing, but it was insufficient to prevent Australian shares from recording their strongest gains in six years in the 2012/13 financial year. In the 12 months ending 30 June 2013, the S&P/ASX 200 Accumulation Index added nearly 23%.

Property

- Australian listed property securities dipped by 0.8% in June.

- Diversified property securities generated the strongest returns, while the commercial segment, consisting of office and industrial assets, underperformed over the 12-month period.

- At a stock-specific level, Commonwealth Property Office Fund (+3.3%) and CFS Retail Property Trust Group (+3.0%) performed strongly in June.

Global shares

- In the US, the S&P500 Index decreased by 1.5% in June, also weighed down by market anxiety over the Fed's likely plans to gradually reduce its asset purchasing program later this year.

- S&P500 Index defensive sectors outperformed in June, led by Telecommunications, Consumer Staples, Health Care and Utilities.

- Cyclical sectors such as Materials and Energy were among the poorest performers, led lower as selling pressures associated with the Fed's comments were intensified by concerns over China's slowing economy and banking system.

GLOBAL EQUITY MARKETS DRIVEN HIGHER UNTIL RECENTLY

Source: Bloomberg as at 28 June

- Equity markets also tumbled across the Atlantic, however, ECB President Draghi calmed the market somewhat by assuring that aggressive loose monetary policy would remain in place for a long time to come, potentially de-coupling from US policy.

- The Euro Stoxx 50 Index was down by 6.0% in June, despite diminishing tail risks and modestly better growth prospects.

- Core European equity markets such as Germany (-4.7%), Holland (-5.2%) and France (-5.3%) performed better than the peripheral markets of Italy (-11.5%) and Spain (-6.7%).

- In Japan, the Nikkei 225 and Topix Indices fell by 0.7% and 0.2%, respectively. June was marked by continued high volatility and a sharp intra-month reversal. In the first week, the Topix dropped more than 10% to a level almost 20% below its 23 May 2013 peak. The subsequent reversal was trigged by better economic data and the BoJ forcing stability onto JGB yields. Sectors such as Telecommunications, Financials and Utilities led the recovery.

- The MSCI Asia ex-Japan Index fell by 6.3% in USD terms (-1.4% in AUD terms), led lower by a decline in Chinese equities. The Shanghai Composite Index fell by 14.0%, dragged down by a combination of economic growth concerns, policy risks and a slowdown in credit growth.

Global emerging markets

- Emerging market equities fell over concerns the Fed will scale-back its asset purchases.
- The MSCI Emerging Markets EMEA Index declined by 5.1% in USD terms (-0.1% in AUD terms) over the month.
- The rise in US Treasury yields and falling commodity prices also drove down the emerging market currencies, causing several countries to intervene in currency markets.
- Financials, Materials and Energy were the bottom three sectors in across emerging markets in June. Telecommunications, Health Care and Consumer Discretionary stocks were the best performers.
- Emerging markets ex-Asia equity markets were led lower by Turkey (-10.9%) during the month, on increasing political risks associated with continued protests at Istanbul's Gezi Park.
- Latin American equity markets were sharply lower in June with the MSCI Emerging Markets LatAm Index declining by 9.1% in USD terms (-4.3% in AUD terms), led by Brazil (-11.3%).
- Rising inflation (+6.5% for the year in May), policy rates and anger over endemic political corruption has caused widespread unrest and activism.
- S&P revised Brazil's sovereign BBB credit rating outlook to 'negative' citing weak economic growth and an eroding fiscal stance.

Need more information?
Please speak with your financial adviser or visit our website at colonialfirststate.com.au. Alternatively, you can call us on 13 13 36.