# Market Update

## September 2014

Suncorp Financial Planning

## Outlook

Share markets remain at risk of further losses in the near term, particularly as the September/October period tends to be a historically weak time of year for stocks. However, rather than cause for concern, any further weakness in share markets should be viewed as a buying opportunity with the market likely just undergoing a healthy pullback, or 'correction'.

Importantly, global growth looks set to continue this year, led by ongoing recoveries in the US, Japan and Europe; though admittedly growth in the euro-zone is likely to be a little more subdued compared to its US and Japanese counterparts. Further, monetary conditions remain 'easy', i.e. global interest rates are still very low by historical standards, and we continue to see money moving away from low-yielding bonds and cash in favour of equities. Taken together, these factors suggest share markets can indeed continue to move higher, albeit at a more modest pace.

Here in Australia, the mining boom which had kept the economy afloat in recent years appears to have run its course as investment in the resources sector continues to decline. Importantly, we continue to see some positive signs within the non-mining sectors though it'll still be some time yet before these sectors can pick up the slack left by the slowdown in mining activity. As a result, domestic growth this year is expected to once again be below trend.

In terms of interest rates, the RBA is likely to maintain its neutral position on monetary policy for the foreseeable future. Any movement in interest rates will depend on the relative strength or weakness of upcoming key economic data.

## Market update at a glance

Global share markets weakened in September, driven in part by US Federal Reserve tightening expectations, lingering geopolitical uncertainty and Chinese growth concerns. Australian shares were also lower while commodity prices extended their recent decline and the Australian dollar tumbled against its US counterpart.

## Key points

- Australian dollar tumbles against US dollar
- Global share markets lower
- Global bond yields rise
- Australian shares fall
- Commodity prices extend declines

## Interest rates remain on hold

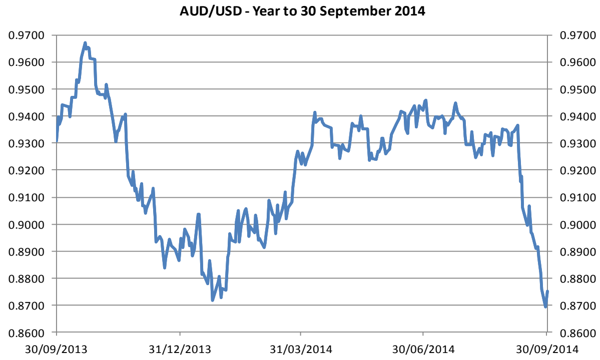
The Reserve Bank of Australia (RBA) left the official cash rate unchanged at a record low 2.50% for a twelfth consecutive month in September; the central bank once again noting that "*on present indications, the most prudent course is likely to be a period of stability in interest rates*." Officials also reiterated their view that domestic growth will likely remain a little below trend over the year ahead.

Elsewhere, the Fed (0-0.25%), the Bank of Japan (0.10%) and the Bank of England (0.50%) all left their respective benchmark interest rates on hold in September. As noted earlier, the ECB lowered its refi rate to just 0.05%.

## Australian dollar tumbles

The Australian dollar (AUD) tumbled against its US counterpart in September; the local currency hurt by commodity price weakness, expectations volatility will increase as the Fed gets nearer to raising interest rates and general USD strength. Concerns that moves by the RBA to slow the housing market will further delay the bank's first rate hike since November 2010 also weighed. The AUD fell as low as USD0.8684 before eventually closing the month down 6.4% at USD0.8752. For the calendar year, the AUD is trading 2.2% lower.

Falling commodity prices and expectations the Fed will raise interest rates before the RBA will likely see the AUD's downward trend continue; possibly to as low as USD0.80 cents by this time next year.



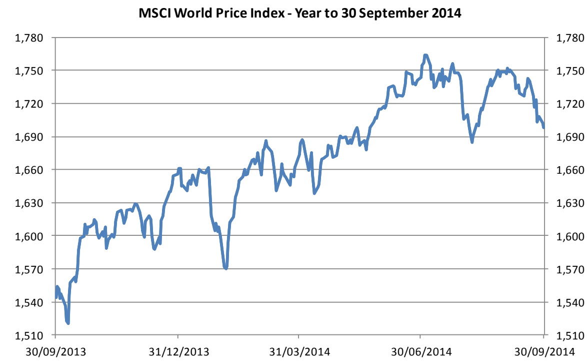

Source: Bloomberg

## Global share markets decline

Global share markets fell in September amid concerns improving US economic data could see the Federal Reserve (Fed) raise interest rates earlier than anticipated, renewed fears of a slowdown in China and ongoing geopolitical risks. Concerns Russia may seize foreign assets in retaliation to Western sanctions and uncertainty surrounding the outcome of Scotland's vote to secede from the UK also weighed on investor sentiment over the period. (Note: Scotland eventually voted in favour of remaining a part of the UK).

Limiting share market losses was the European Central Bank (ECB)'s announcement that it would cut its benchmark refinancing ('refi') rate to just 0.05% and begin purchasing assets in a bid to boost growth in the euro-zone, an upward revision to second-quarter US growth data and hopes of more aggressive central bank stimulus in China.

At the country level, the US S&P 500 Index retreated from its recent record highs to close the month down 1.6%. Shares in the UK (-2.9%[1]) were also weaker while European (1.7%[2]) and Japanese stocks (4.9%[3]) went the other way; the latter in particular benefiting from a weaker yen and growing expectations the Bank of Japan will soon expand its monetary easing program. Collectively, global share markets ended the month down 2.9%[4] (see following chart).




Source: Bloomberg

[1] UK shares measured by the FTSE 100 Index
[2] European shares measured by the EuroStoxx 50 Price Index
[3] Japanese shares measured by the Nikkei 225 Index
[4] Global shares measured by the MSCI World (Price) Index

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## Global bond yields rise

Major government bond yields rose in September after a series of stronger US economic data – including the upward revision to second-quarter growth figures – led to speculation the Fed will raise interest rates sooner than expected. The yield on 10-year US Treasuries rose 15 basis points (bps) to 2.49% while yields on 10-year UK gilts (+6 bps, 2.43%), German bunds (+6 bps, 0.95%), French bonds (+4 bps, 1.29%) and Japanese bonds (+3 bps, 0.52%) were also higher. By contrast, the yields on 10-year Spanish (-9 bps, 2.14%), Italian (-11 bps, 2.33%) and Portuguese (-6 bps, 3.16%) bonds were all lower for the month.

Here in Australia, the yield on 10-year government bonds tracked their global counterparts higher, rising 19 bps to 3.48%. Importantly, Australian bonds – widely considered a safe haven investment on account of their AAA credit rating – still represent better value than many of their global counterparts, including US Treasuries. In fact, the yield differential between Australian 10-year bonds and their US equivalent is currently 99 bps (or 0.99%). However, this yield advantage is unlikely to last if the US economy continues to improve as expected.

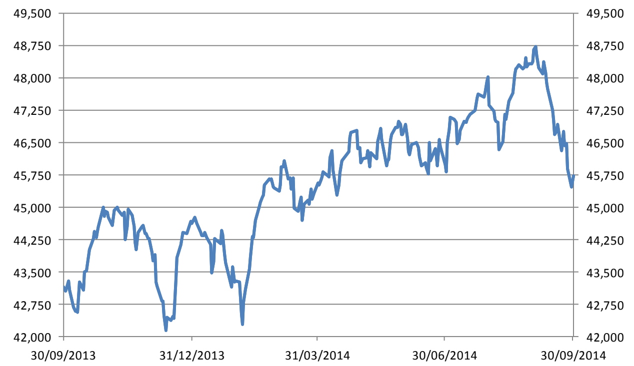
## Australian shares fall

The Australian share market fell significantly in September with the S&P/ASX 200 Accumulation Index closing the period down 5.4%. Contributing to the market's loss was news the local economy slowed to its weakest pace in more than a year in the June quarter, fears of an earlier-than-expected rate rise in the US and sharp declines across the major banks and miners; the latter hurt by the almost 10% drop in the price of iron ore. Some disappointing Chinese economic data and a sharp dip in consumer confidence also weighed on investor sentiment.

Limiting the market's decline were expectations domestic interest rates will remain lower for longer, a sizable drop in the local unemployment rate – it fell from 6.4% in July to 6.1% in August – and the promise of increased monetary policy support in Europe.

So far this year, the Australian share market has returned 2.4%. This compares with 6.7% in the US, 3.8% in Europe, -0.7% in Japan and -1.9% in the UK.

S&P/ASX 200 Accumulation Index - Year to 30 September 2014




Source: Bloomberg

## Commodities extend losses

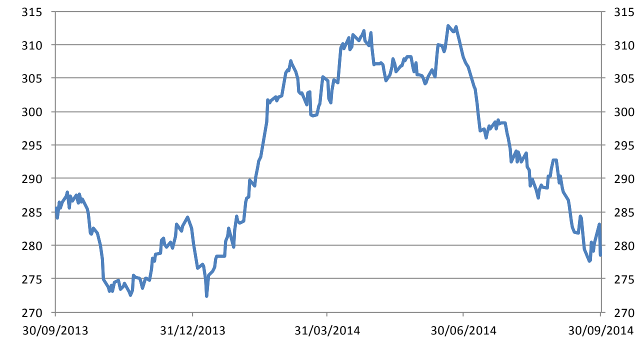
Commodity prices continued to fall in September with the Thomson Reuters/Jefferies CRB Commodity Index closing the month down 4.9%.

Oil prices fell for a third consecutive month in September amid Fed tightening expectations and softer Chinese and euro-zone economic data. News that the Organisation of the Petroleum Exporting Countries – or OPEC as it's more commonly known – had lowered its demand forecasts also weighed on prices. Oil fell 5.0% over the month, closing at USD91.16 a barrel. For the calendar year, oil is down 7.4%.

Gold was also lower in September amid further US dollar (USD) gains and fears that stronger US economic data will prompt the Fed to raise interest rates sooner than expected. Helping to limit the precious metal's decline were lingering tensions between Russia and Ukraine and news that President Obama had authorised US airstrikes on Islamic State in Syria. Gold closed the month down 6.2% at USD1,207.26 an ounce. For the calendar year, gold is 0.4% higher.

Base metals were lower for the month. Nickel (-13.2%) posted the biggest declines on the back of USD strength, weaker Chinese demand and news that a Philippine ban on nickel exports would likely be deferred for several years. Iron ore (-9.6%), aluminium (-7.6%), lead (-6.6%), copper (-4.1%) and zinc (-3.3%) also fell over the period.

Thomson Reuters/Jefferies CRB Commodities Index - Year to 30 September 2014




Source: Bloomberg

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