

# Economic and Strategy Review

Monthly Report as at 31 March 2014

The Fed remained upbeat on the underlying growth path for the US.

**Economic and Policy Trends:** In the US, output appears to be recovering from a cold snap that resulted in disruptions to global supply chains earlier in the year. At its latest FOMC meeting, the Fed remained upbeat on the underlying growth path for the US economy and labour market. The Fed announced a further \$10 billion of tapering beginning in April and Yellen also noted that once tapering had finished, a period of around six months was likely before conventional tightening would begin. This suggests that should inflation remain stable in the US and the labour market continue to recover as anticipated, that we could see the first tightening in the federal funds rate in Q2 2015.

Other G-3 central banks remain well behind the Fed given less developed recoveries in Europe and Japan. There, the focus remains on providing highly accommodative levels of policy support. In China, the NPC concluded in early March with authorities declaring a “war on pollution”, rolling out further structural reform and indicating a growth target of 7.5% for 2014.

In Australia, the underlying tone of economic data improved over the month. According to the Q4 national accounts, real GDP rose by 0.8% over the quarter and by 2.8% over the same quarter a year earlier. Net exports were the major driver of growth, contributing 0.6 percentage points to the quarterly outcome. The domestic economy expanded by a more modest 0.3% with growth in private consumption, dwelling and the public sector helping offset a sharp fall in business investment.

The most recent monthly trade and building approval data suggest that these sectors will continue to add to growth in the Q1 national accounts. Labour force data for February surprised on the upside with total employment jumping by 47,300, though the unemployment rate remained unchanged at 6%. Consumer and business confidence edged lower over the month. The Reserve Bank of Australia (RBA) left the cash rate unchanged at 2.5% at its last meeting and continues to hold onto its neutral bias. We continue to look for the RBA to begin tightening monetary conditions in H1 2015.

**Equity Market Trends:** Offshore equity markets were buffeted by a range of offsetting forces that included rising geo-political tension over Crimea, further Fed tapering and mixed global economic data. In the US, the S&P500 ended the month 0.7% higher. In Europe, the Euro STOXX 50 edged ahead by 0.4% while in Japan, the

Nikkei was unchanged over the month. The MSCI World ex-Australia Accumulation Index in Australian dollars fell 3.4% over the month, with a strengthening Australian currency a drag on sector returns. In Australia, the S&P/ASX 300 Accumulation Index limped ahead by 0.2% over the month.

**Bond Market Trends:** Yields rose over the earlier part of the month on stronger economic data, rallied mid-month on heightened geo-political and Chinese growth concerns and then drifted higher again as these concerns unwound. After falling to as low as 2.79% and 3.98%, three and ten year government bond yields ended the month at 2.99% and 4.08%, respectively. These moves resulted in a modest flattening in the yield curve, with the spread between the three and ten year government bond yield coming in from 119 to 109 basis points. For the month, the UBS Composite Bond Index crept ahead by 0.02%, while the cash sector, as measured by the UBS Bank Bill Index, rose by 0.22%.

**Investment Strategy:** Under our investment metrics, the Australian equity market is showing up as fairly valued. Accordingly, multi sector funds are maintaining benchmark exposures to the sector. We maintain our bias to add exposure to the sector given where we are in the cycle.

Multi sector funds continue to hold a benchmark weighting to Australian fixed interest. The slight rise in yields over March helped take the sector from the expensive end of our fair value band back towards the middle of that band.

Frank Uhlenbruch, Investment Strategist

## Tactical Asset Allocation Summary (as at 31 March 2014)

Asset Class	Multi Sector Trusts*
Australian Shares	Benchmark
Australian Fixed Interest	Benchmark
Cash	Benchmark
International Shares	Benchmark fixed
Australian Listed Property	Benchmark fixed
Global Listed Property	Benchmark fixed

\* Multi-sector Trusts may have differing asset class weights, including no exposure to a particular asset class

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