Economic and Strategy Review

Monthly Report as at 30 April 2014

Global recovery remains intact despite a rise in geo-political tensions.

Economic and Policy Trends: The latest run of offshore data shows that the global recovery remains intact despite a rise in geo-political tensions. Poor weather conditions in North America earlier in the year slowed the pace of growth, but the latest US data shows that activity levels and labour market conditions have recovered. Output also appears to be recovering elsewhere, though the pace remains varied.

The latest set of comprehensive forecasts in the IMF's April World Economic Outlook have world output lifting by 3.6% in 2014 after gaining 3% in 2013. The recovery is forecast to strengthen in 2015 with world output expected to lift by 3.9%. Tailwinds come from accommodative financial conditions and a lessening in fiscal drag as budget positions improve. Advanced economy growth is forecast to lift from 1.3% in 2013, to 2.2% in 2014 and 2.3% in 2015. Within that grouping, solid recoveries are forecast for the US, Germany, France and the UK. Growth in Japan is expected to slow following recent fiscal tightening. For the emerging and developing economy grouping, growth is expected to lift modestly from 4.7% in 2013, to 4.9% in 2014 and 5.3% in 2015. These more moderate outcomes partly reflect the tightening in financial conditions experienced by many following the shift in the US Fed's policy stance. Within that grouping, growth in China remains solid, forecast to slip from 7.7% in 2013, to 7.5% in 2014 and 7.3% in 2015.

In Australia, data releases were a little more mixed. Building approval and retail sales data for February were both a little weaker than expectations but this follows very strong readings for the previous month. Trade data surprised on the upside again and points to another strong positive contribution to GDP growth from the external sector. Business conditions crept up slightly in March according to the Nab survey though confidence slipped. The recent fall in consumer sentiment halted in April with sentiment up slightly. Labour market conditions continued to improve with total employment lifting 18,100 and the unemployment rate falling from 6.1% to 5.8%. Price pressures moderated with the March quarter CPI rising by a less than expected 0.6% over the quarter. The average of underlying statistical measures rose by 0.5%. These inflation data, along with a likely moderate fiscal tightening in the May Budget, should see the Reserve Bank of Australia (RBA) sidelined until H1 2015.

Equity Market Trends: Offshore equity markets had a volatile month; boosted by periodic good news on the economic outlook, falling on weaker data and were hit hard mid-month by a bout of profit taking in the US on technology, biotechnology and pharmaceutical stocks. Through all this volatility, the S&P500 ended the month 0.6% higher while in Europe, the Euro STOXX 50 rose 1.2%. In Japan, the Nikkei fell 3.5% against the back drop of a lift in VAT rate at the start of the month. The MSCI World ex-Australia Accumulation Index in Australian dollars gained 1% over the month, with a relatively steady Australian currency having little impact on sector returns. In Australia, the S&P/ASX 300 Accumulation Index rose by 1.7% over April.

Bond Market Trends: Yields rallied over the month resulting in capital gains that helped lift the UBS Composite Bond Index by 0.91% over the month. The shorter end benefitted from some softening in economic readings and a better than expected CPI which led the market to push back its expectations for monetary tightening. Longer dated securities benefitted from these factors along with expectations for a modest fiscal tightening in the upcoming May Budget. Three and ten year government bond yields ended the month 9 and 13 basis points lower at 2.90% and 3.95%, respectively. 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 continues to show up as fairly valued. Accordingly, multi sector funds are maintaining benchmark exposures to the sector.

Multi sector funds continue to hold a benchmark weighting to Australian fixed interest. The fall in yields over April has pushed the sector towards expensive levels. Multi sector funds remain at benchmark weighting but we have a bias to move underweight if rates rally significantly from here.

Frank Uhlenbruch, Investment Strategist

Tactical Asset Allocation Summary (as at 30 April 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

Signatory of: PRI Principles for Responsible Investment