

Economic and market update

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Bob reviews events in Australian and overseas markets during August.

How did markets perform in August?

August featured only mild gains for global shares of 0.7% after July's robust performance. Concerns over a possible US interest rate increase before the end of this year constrained share markets.

US shares made marginal gains of around 1% in August. US Federal Reserve (Fed) Chair Janet Yellen signalled in late August that the case for increasing US interest rates had "strengthened" following positive and improved US economic activity.

European shares recorded a modest return of 1.5%. The European Central Bank maintained their assertive stimulus measures at August's meeting with inflation pressures contained.

UK shares were resilient with a 1.3% gain, drawing support from a lower currency and the interest rate cut by the Bank of England in early August.

Australian shares slipped by 1.6% in August. The prospect of higher US interest rates and a lower Australian dollar (AUD) were seen as reducing the chance for another Reserve Bank of Australia (RBA) interest rate cut this year.

The Australian corporate profit season largely met the market's subdued expectations. Yet there were some notably weak profit results and sharp asset write-downs for the mining and retail sectors.

Global bond yields were mixed in August. The Fed's more assertive commentary on interest rates saw US bond yields gradually rise. European and Japanese yields marginally rose but still remain in negative territory. UK bonds made historic lows in yields given the UK interest rate cut.

The AUD fell against the US dollar in August. Lower prices for iron ore and gold, the RBA's cash rate cut in early August, and the prospect of higher US interest rates weighed on the AUD.

What were the key factors driving markets?

The key debate is the timing of higher US interest rates.

Global economic data was generally solid with better US economic activity and stable results from both China and Europe.

In the US, there was strong jobs growth and business surveys were encouraging. Europe's economic activity was generally sound. Business surveys were resilient in August while the unemployment rate held steady. Britain's decision to exit Europe in June has so far had minimal impact.

China's economic activity showed further stabilisation signs in August. China's industrial production maintained a steady 6% annual growth pace while retail sales were robust at 10% annual growth.

Emerging markets provided some positive signals. India's economic growth for the June quarter came in at a robust 7.1% annual rate. Brazil's recession appears to have

moderated in the June quarter (real GDP decreased by 3.8%) ahead of the Olympic Games.

In Australia, the RBA cut the official cash rate from 1.75% to a new historic low of 1.5% in early August. Australia's economic activity was solid. The labour market achieved modest jobs growth with the unemployment rate edging down to 5.7%. The National Australia Bank's business survey showed positive results. Housing construction has also rebounded strongly given lower interest rates in 2016.

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