


GODFREY PEMBROKE
market
update

JANUARY 2017

- ▶ In December global equity markets continued to make new highs as investors factored in stronger economic growth and higher corporate earnings in the United States following the US election in November.
- ▶ Oil prices rose 8.7% to US\$53.75 per barrel (WTI) following the agreement by OPEC and several non-OPEC oil producing countries to cut production in 2017.
- ▶ The US ISM manufacturing index rose to the highest levels in two years.
- ▶ The US Federal Reserve increased its Federal Funds rate from 0.50% to 0.75% and indicated that it expects to raise interest rates a further three times in 2017.
- ▶ Chinese economic activity indicators were stronger than expected.
- ▶ Australia's economy has been somewhat mixed with the unemployment rate rising from 5.6% to 5.7% and the government revised its economic forecasts to show marginally larger budget deficits over the next few years.

December market performance

Equity Markets – Price Indices	Index	At Close 31/12/2016	% Change 1 Month	% Change 12 Months
Australia	All Ordinaries	5719.14	3.9%	7.0%
Japan	Nikkei	19114.37	4.4%	0.4%
Hong Kong	Hang Seng	22000.56	-3.5%	0.4%
UK	FTSE 100	7142.83	5.3%	14.4%
Germany	DAX	11481.06	7.9%	6.9%
US	Dow Jones	19762.60	3.3%	13.4%
EMU*	Euro 100	1112.05	7.4%	1.6%
World**	MSCI – Ex Aus (Gross) (Hedged)	1377.99	2.6%	6.8%

Property – Price Index	Index	At Close 31/12/2016	% Change 1 Month	% Change 12 Months
Listed Trusts	S&P/ASX 300 A-REITS	1371.45	5.1%	8.0%

Interest Rates	At Close 31/12/2016	At Close 31/11/2016	At Close 31/12/2015
Aust 90 day Bank Bills	1.81%	1.76%	2.38%
Australian 10 year Bonds	2.76%	2.73%	2.82%
US 90 day T Bill	0.50%	0.48%	0.17%
US 10 year Bonds	2.44%	2.39%	2.27%

Currency***		At Close 31/12/2016	% Change 1 Month	% Change 12 Months
US dollar	A\$/US\$	0.72	-2.00%	-0.47%
British pound	A\$/STG	0.59	-0.91%	18.72%
Euro	A\$/euro	0.69	-1.43%	2.50%
Japanese yen	A\$/yen	84.46	0.32%	-3.50%
Trade-weighted Index		63.90	-2.14%	1.91%

* Top 100 European stocks trading on the FTSE

** Price Index (Source: msci.com)

*** All foreign exchange rates rounded to two decimal places (Source: FactSet)

Past performance is not a reliable indicator of future performance.

Please Note: To get mthly data for Australia bonds (UBS Composite 0+ Years) and global bonds (Hedged and Unhedged), please refer to FactSet. Under FactSet, under "Benchmarks", go to "Global Fixed Income" category; "UBS Bond Indices (Australia)" and then choose "UBS Bank Bill Index 0 + YR" under 'description'. Under FactSet, under "Benchmarks", go to "Global Fixed Income" category; "Barclays Indices" and then choose "Hedged (AUD) or Unhedged (AUD)" under 'Category' and then scroll down 'Description' until you find "Barclays Global Aggregate (AUD Hedged or Unhedged)".

Global economies

Equity and commodity markets continued their post-US election rally in December with the US Dollar continuing to strengthen to new 14-year highs helped by the US Federal Reserve's decision to lift interest rates.

Most of the economic data released during December confirmed that the major economies are travelling reasonably well.

US

In a relatively quiet month for economic releases, the limited data that was released showed that the US economy continues to perform in line with recent trends. Consumer confidence moved back up to post-financial crisis highs, unemployment fell to the lowest levels since 2007 and the ISM manufacturing index rose to two-year highs.

As expected, at its December committee meeting, the US Federal Reserve lifted interest rates from 0.50% per annum to 0.75% per annum and its new set of “dot point” forecasts show that the median expectation is for a further three interest rate rises in 2017.

Europe

In early December investor attention remained focussed on political events, namely the Italian referendum and Austrian Presidential election. However, neither of these events had much impact on markets and attention shifted to the European Central Bank’s decision to extend its asset purchase program for nine months but at a lower rate of monthly purchases – a sign that it wants to end its aggressive monetary stimulus program later this year.

China

Chinese activity indicators released in December were better than expected and show that fears of a sharp deceleration in growth have been unfounded and this has helped support commodity prices such as iron ore and coal. More recently, new house price data has pointed to slower price growth in the major cities, which will help ease Government concerns of a housing bubble.

Asia region

In Japan, the sharp depreciation of the Yen against the US Dollar in the past two months has meant that policymakers at the Bank of Japan have become more optimistic on the economy. Despite their more upbeat assessment, economic data has continued to show that the economic growth has remained low and that its consumers are reluctant to spend or invest, despite the very low interest rate environment.

Australia

In Australia, recent economic data has been soft with the unemployment rate ticking up from 5.6% to 5.7% and some other labour market measures, such as hours worked and wages growth, also painting a picture of some overcapacity in the labour market. Building approvals, which had been running at close to record levels in 2016, have also contracted sharply, which could point to an earlier-than-expected slowdown in housing construction activity.

EQUITY MARKETS

- ▶ China's Shanghai Composite Index fell by 4.5% in December.
- ▶ Emerging market shares rose 0.2% in local currency terms.
- ▶ The German DAX Index gained 7.9%.
- ▶ The broader Euro 100 rose 7.4%.
- ▶ The Japanese Nikkei Index rose 4.4%.
- ▶ The US Standard & Poor's 500 Index gained 1.8% over the month and 9.5% in 2016.
- ▶ Australia's S&P/ASX All Ordinaries Index rose 3.9% in December and 7.0% over the year.

Australian equities

	Index/Benchmark (% pa)	1 Year	3 Years	5 Years	7 Years
Australian	S&P/ASX 300 Acc.	11.79%	6.57%	11.64%	6.69%
	S&P/ASX 50 Acc.	10.86%	5.65%	11.93%	7.00%
	S&P/ASX Small Ordinaries Acc.	13.18%	6.24%	4.87%	1.72%

The S&P/ASX 200 Accumulation Index returned 4.4% in December with all sectors finishing the month in positive territory. The best performing sector was utilities, which returned 8.7% for the month, as bond yields stabilised after the sharp rise over the past few months. Energy shares also enjoyed a strong month with a rise of 6.1% on the back of the higher crude oil prices. Healthcare stocks continued to underperform with a gain of just 0.9% in December as investors priced in softer industry conditions. Small cap shares underperformed larger companies again with a return of 3.6%, including dividends.

Sector	1 Month	3 Months	1 Year
Energy	6.1%	7.4%	15.2%
Materials	3.8%	7.4%	43.5%
Industrial	2.4%	-0.5%	10.6%
Consumer Discretionary	4.2%	-2.5%	10.7%
Consumer Staples	1.7%	-1.6%	4.0%
Health Care	0.9%	-8.8%	2.2%
Financials (ex-Property)	5.5%	12.7%	7.4%
Info Tech	4.0%	-2.7%	3.3%
Telcos	0.5%	-4.2%	-7.0%
Utilities	8.7%	9.2%	20.2%
Property	6.8%	-0.7%	13.2%

BIG MOVERS THIS MONTH

Going up

↑	Utilities	8.7%
↑	Property	6.8%
↑	Energy	6.1%

Going down

↓	None	
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Global Equities

	Index/Benchmark (% pa)	1 Year	3 Years	5 Years	7 Years
Global	MSCI World Ex Aus (Gross) in AUD	8.57%	12.18%	19.27%	12.37%
	MSCI World Ex Aus (Gross) in Local Currency	9.57%	7.55%	13.43%	10.30%
	MSCI World Small Cap (\$A)	13.79%	12.75%	20.87%	14.72%
Emerging	MSCI Emerging Mkts Free	10.11%	3.21%	6.02%	4.29%
	MSCI AC Far East Free (ex Japan)	7.04%	2.30%	6.17%	0.04%

Developed share markets gained 2.8% in December in local currency terms. Shares in the United States made fresh record highs in the middle of the month. The US S&P 500 index gained 1.8% while Japanese shares benefited from the weaker Yen to rise 4.4%. Globally, the yield-sensitive telecommunications and utilities sector stocks were the best performers rising 6.6% and 4.9% respectively in December as value emerged in these sectors, which had previously been out of favour when bond yields rose.

In an absolute sense, price-earnings ratios are full, but compared with returns from bonds or cash, valuations do not seem excessive. Moderate economic growth should be sufficient to support mid-to-high single digit earnings growth for the key US and European indices in 2017.

Property

	Index/Benchmark (% pa)	1 Year	3 Years	5 Years	7 Years
Australian	S&P/ASX 300 A-REIT Acc	13.18%	17.96%	18.51%	12.54%
Global	FTSE EPRA/NAREIT Dv ex AUS TR Hdg AUD	6.49%	11.10%	14.78%	12.85%

The S&P/ASX 300 A-REIT Accumulation Index (which includes distributions) rebounded in December, returning 6.8% for the month. Over the past year, property securities have returned 13.2%.

Over one, three and five years, A-REITs have outperformed Global REITs. Currency-hedged global property securities, as represented by the FTSE EPRA/NAREIT Index, were up 6.5% over a one-year period.

Fixed Interest

	Index/Benchmark (% pa)	1 Year	3 Years	5 Years	7 Years
Australian	Bloomberg AusBond Composite 0+ Yr	2.92%	5.05%	4.95%	6.00%
	Australian 90 Day Bank Bill	1.99%	2.31%	2.69%	3.28%
Global	BarCap Global Aggregate Index	2.57%	7.11%	7.42%	4.92%
	BarCap Global Agg. Index Hedged	5.24%	6.28%	6.13%	7.19%

Australian bonds lost 0.2% in December after government bond yields rose marginally. Over the month the two-year Australian Commonwealth Government bond yield rose from 1.84% to 1.91% per annum and the ten-year bond yield rose from 2.74% to 2.77% per annum.

Internationally, the Barclays Global Aggregate Bond Index (A\$ hedged) gained 0.36% as bond yields rose marginally in the United States and Japan but fell in the United Kingdom and Germany. In the US, 10-year Treasury bond yields rose from 2.37% per annum to 2.43% as investors priced in higher interest rates after the US Federal Reserve lifted interest rates in December and investors priced in higher interest rates in 2017. During December, the credit spread on high-yield corporate bonds fell from 467 to 421 basis points above US treasury bonds.

Australian dollar

The Australian Dollar fell 1.4 US cents to US\$0.7241 as the US Dollar continued to make new highs on a trade-weighted basis.

Against the US Dollar, the Australian Dollar fell 2.0% for the month, and on a Trade-Weighted Index basis, the Australian Dollar fell 2.1%.

The information contained in this Market Update is current as at 6/01/2017 and is prepared by GWM Adviser Services Limited ABN 96 002 071749 trading as ThreeSixty Research, registered office 105-153 Miller Street North Sydney NSW 2060. This company is part of the National Australia Bank Group of Companies.

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