GODFREY PEMBROKE

market update

JANUARY 2016

- Global equity markets correct in December – although Australia was a strong performer
- Oil prices continue to weaken
- China stock market volatility, and weaker economic data, creates deflationary fears
- US economic data continues to point to an improved recovery.
- US Federal Reserve commenced the process of normalisation of interest rates in December.
- Eurozone economic activity continues to improve
- Australian non-mining economic sector continues to recover

December market performance

Equity Markets – Price Indices	Index	At Close 31/12/2015	% Change 1 Month	% Change 12 Months
Australia	All Ordinaries	5344.56	2.4%	-0.8%
Japan	Nikkei	19033.71	-3.6%	9.1%
Hong Kong	Hang Seng	21914.40	-0.4%	-7.2%
UK	FTSE 100	6242.32	-1.8%	-4.9%
Germany	DAX	10743.01	-5.6%	9.6%
US	Dow Jones	17425.03	-1.7%	-2.2%
EMU*	Euro 100	1094.37	-6.3%	5.5%
World**	MSCI – Ex Aus (Gross) (Hedged)	1290.80	-2.4%	0.2%

Property – Price Index	Index	At Close 31/12/2015	% Change 1 Month	% Change 12 Months
Listed Trusts	S&P/ASX 300 A-REITS	1269.62	2.4%	8.9%

Interest Rates	At Close 31/12/2015	At Close 30/11/2015	At Close 31/12/2014
Aust 90 day Bank Bills	2.36%	2.26%	2.78%
Australian 10 year Bonds	2.82%	2.86%	2.73%
US 90 day T Bill	0.17%	0.18%	0.05%
US 10 year Bonds	2.27%	2.21%	2.17%

Currency***		At Close 31/12/2015	% Change 1 Month	% Change 12 Months
US dollar	A$/US$	0.73	0.41%	-11.10%
British pound	A$/STG	0.49	2.55%	-5.95%
Euro	A$/euro	0.67	-2.38%	-0.97%
Japanese yen	A$/yen	87.52	-2.02%	-10.80%
Trade-weighted Index		62.70	1.46%	-5.71%

* 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.

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Global economies

Global equity markets corrected in December although Australia was up strongly and outperformed other markets.

Oil price declines have raised concerns of increasing corporate defaults, impacting global credit markets.

The US economy continues to improve although the manufacturing sector was weaker in December.

Business conditions in the Eurozone and Japan improved.

China economic data has been a little weaker in December but appears to be stabilising. However, equity market volatility and weaker commodity prices have raised deflationary fears.

The US Federal Reserve announced the commencement of 'interest rate normalisation' with an initial interest rate increase of 25 basis points (bp) in December.

Australian non–mining economic data continues to recover, positively impacted by the lower Australian dollar, low interest rates and improving business conditions.

US

In the US, although the economic data has been mixed, the overall economy remains in recovery mode. While the manufacturing and services data has been weaker in December, employment growth remains strong.

The final Markit Institute of Supply Management (ISM) Manufacturing Purchasing Manufacturers Index (PMI) at 51.2 was down from 52.8 in November. The stronger US Dollar (USD) is impacting exporters and increasing competition from importers while lower oil prices are reducing demand for goods and machinery from the energy sector.

December data highlighted that the US service sector ended the year on weaker growth with business activity and incoming new work both expanding at slower rates than in November. At 54.3 in December, the final Markit US Services PMI business activity index was down from 56.1 in November.

The December non-farm payrolls data came in at 292,000 while November employment growth was revised up to 252,000 from 211,000 and October revised up 9,000 to 311,000. The unemployment rate remains at 5.0% although it doesn't capture those who've given up looking for work. The U6 underemployment measure was steady at 9.9%.

The Federal Reserve (The Fed) commenced the normalisation of interest rates in December with a 25bp increase in the Federal Funds rate. The Fed comments suggest the pathways to higher interest rates will be gradual.

Consumer prices were up 0.5% year-on-year (yoy) in November, compared to 0.2% rise in October. This was the highest rate in 2015. The annual core inflation excluding food and energy increased to 2%, from 1.9% in the previous two months.

US final consumer sentiment data was higher than the preliminary reading in December, coming in at 92.6. The University of Michigan December data trended higher from the November reading of 91.3.

The December Institute for Supply Management's Manufacturing Purchasing Managers Index (PMI) decreased to 48.2, from 48.6 in November. It is the second consecutive month of contraction in manufacturing activity. New orders, production, employment and raw materials all declined.

The US 2015 corporate earnings growth remains steady at –0.7% (revenues to -3.4%), while the 2016 estimated earnings growth remains steady at 7.4% (revenue growth at 4.2%).

The current 12 month forward Price Earnings (P/E) ratio for the S & P 500 index is 15.0 times.

Europe

Over to the Eurozone, the December Markit Composite PMI index came in at 53.2 compared to 52.8 in November. New orders and new export business all improved.

The Eurozone manufacturing index continued to make solid progress at the end of 2015 as rates of growth in production, new orders and new export business all improved.

Eurozone economic growth in Q3 was 1.6% yoy and represents around double the average annual growth rate between 2005 and 2014.

Unemployment has been falling and was 10.5% in November, the lowest in more than four years.

Consumer confidence is increasing and is also at a four year high, supported by monetary and fiscal policies, a banking system that is continuing to strengthen, lower energy costs and improved wage growth.

Concerns remain over a China hard landing. China represents the Eurozone's second largest trading partner, behind the US. However, the ECBs €60 billion per month stimulus package is continuing and is expected to offset any China slowdown.

China

In China, the significant news has been centred on the sliding share market, the Government interventions to control the falls in the market and the declining value of the Chinese currency.

The China Caixin Manufacturing PMI dropped to 48.2 in December from 48.6 in November. This data was relatively weak. Factory activity has been contracting since March 2015. Client demand was weak both at home and abroad, with new export business falling for the first time in three months.

China's foreign exchange regulator has stated that the financial system is 'largely stable and healthy'.

The December inflation rate was 1.6% yoy compared to1.5% in November.

China trade data in December was considerably stronger than expected. In USD terms, exports fell by 1.4% yoy and represented a sharp improvement on the 6.8% decline seen in November. Imports fell by 7.6% yoy in USD terms compared

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to a decline of 8.7% in November. In yuan denominated terms, exports rose by 2.3% while imports were down 4.0%.The trade surplus of $60.09 billion was ahead of expectations.

Asia region

Over to Japan, manufacturing activity in December continued the positive trend. New orders increased at a rate that matched October's one year high. This supported further expansions in output, employment and buying activity. The PMI was unchanged from November at 52.6, indicating a sustained marked improvement in operating conditions at Japanese manufacturers. The latest quarter was the strongest quarterly average since Q1 2014.

The seasonally adjusted services PMI index at 51.5, was down slightly from 51.6 in November, but signalled an expansion in business activity at Japanese service providers. Although modest, the rate of increase was solid and broadly in line with the average over the current nine month sequence of growth.

In India, the Manufacturing PMI came in at 50.2, down from the 52.6 in October. Growth in manufacturing production softened to the slowest in the current 25 month sequence of expansion, while service activity stagnated.

The Nikkei India Composite PMI Output Index rose to 51.6 in December, up from 50.2, and indicated a rebound in growth of private sector activity. Whereas manufacturing PMI decreased for the first time since October 2013, services activity increased at an accelerated pace.

The Nikkei Services Business Activity Index rose to 53.6 in December, up from 50.1 in November.

Australia

Back home, the Reserve Bank of Australia (RBA) will not meet until February and expectations remain that they will retain the current cash rate at 2%. The Australian economy continues to improve across the non-mining sector

Rates are expected to remain on hold for an extended period with no increase until mid-2017.

Business credit growth was flat in November against a 1.1% month-on-month (mom) gain in October. This pushed the annual business growth to 6.6% yoy. Housing credit growth was up 0.6% mom while the annual rate was 7.6% yoy.

November non-food sales growth of 5.2% was higher than the food sales growth of 2.5%. Department store sales expanded at 2.5% during November which is in-line with the long term trend rate for this category.

The job advertisements were flat in December. The ANZ Job Advertisements Series shows job listings slipped by just 0.1% in December seasonally adjusted leaving the yearly rate of growth at 10%. In December, online job ads eased by 0.1% while those in newspapers fell by 1.2%.

There is a steady improvement in hiring intentions. The RBA has recognised this steady improvement.

The December unemployment rate remained unchanged at 5.8% in seasonally adjusted terms.

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EQUITY MARKETS

- The China Shanghai Composite Index was up 2.7% in December
- The German DAX Index was down 5.6%
- The broader Euro 100 was down 6.3%
- The Japanese Nikkei Index was down 3.6%
- The US Dow Jones Equity Index was down 1.7% in December
- Australian S&P/ASX All Ordinaries Index ended the month up 2.4%

Australian equities

	Index/Benchmark (% pa)	1 Year	3 Years	5 Years	7 Years
Australian	S&P/ASX 300 Acc.	2.80%	9.01%	6.67%	9.90%
	S&P/ASX 50 Acc.	0.99%	9.10%	7.60%	10.20%
	S&P/ASX Small Ordinaries Acc.	10.16%	1.69%	-2.51%	6.63%

The rally in global markets through October and November came to an abrupt end in December. However, the Australian All Ordinaries reversed its November 1.3% decline and outperformed global markets in December, finishing up 2.4%.

The S&P/ASX All Ordinaries Index on a 12 month basis was down 0.8%.

The 12 month return on the S&P/ASX 300 Accumulation Index was 2.73%.

The ASX/S&P300 Industrials Index was up 3.17% in December and for the 12 months was up 3.42%.

A strong recovery in the Consumer Staples, Consumer Discretionary and Telecommunications sectors was a feature of the December sector performance, up 7.1%, 6.3% and 4.3% respectively.

The continued weakness in oil prices impacted the Energy sector, down 7.5%, while the Industrials and Healthcare Sectors had flat performances during the month, down 0.5% and up 0.6% respectively.

Sector	1 Month	3 Months	1 Year
Energy	-7.5%	-1.3%	-27.7%
Materials	1.3%	-6.9%	-15.2%
Industrial	-0.5%	5.6%	16.7%
Consumer Discretionary	6.3%	13.4%	18.7%
Consumer Staples	7.1%	6.2%	1.0%
Health Care	0.6%	12.4%	16.2%
Financials (ex Property)	3.6%	11.5%	4.7%
Info Tech	3.8%	9.2%	11.9%
Telcos	4.3%	0.9%	1.8%
Utilities	3.0%	8.6%	22.8%
Property	4.0%	6.0%	14.4%

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BIG MOVERS THIS MONTH

Going up

- ↑ Consumer Staples +7.1%
- ↑ Consumer Discretionary +6.3%
- ↑ Telecommunications +4.3%

Going down

- ↓ Energy -7.5%
- ↓ Industrial -0.5%

Global Equities

	Index/Benchmark (% pa)	1 Year	3 Years	5 Years	7 Years
Global	MSCI World Ex Aus (Gross) in AUD	12.43%	24.62%	16.18%	11.11%
	MSCI World Ex Aus (Gross) in Local Currency	2.68%	13.82%	10.30%	12.54%
	MSCI World Small Cap ($A)	12.61%	24.79%	15.66%	14.49%
Emerging	MSCI Emerging Mkts Free	-5.40%	1.20%	1.27%	10.28%
	MSCI AC Far East Free (ex Japan)	-5.72%	1.99%	1.78%	0.11%

The sharp recovery in the global equity markets through October and November came to a halt in December. Global markets suffered a sharp correction in December.

The US Federal Reserve commenced the normalisation of interest rates in December with a 25bp rise in the Fed Funds rate

The Shanghai Composite Index was up 2.7% in December and for the 12 months, was up 9.4%.

The Euro 100 was down 6.3% in December, while the German DAX Index was down 5.6%.

The Japanese Nikkei was down 3.6% in December.

Over the 12 months ended 31 December 2015, the German DAX Index and the Nikkei Index were the best performers in the Market Update universe, up 9.6% and 9.1% respectively.

On the other hand, the underperformers over the 12 month period ended 31 December 2015, were the Hong Kong Hang Seng Index and the FTSE Index, down 7.2% and 4.9% respectively.

Property

	Index/Benchmark (% pa)	1 Year	3 Years	5 Years	7 Years
Australian	S&P/ASX 300 A-REIT Acc	14.38%	15.87%	15.25%	12.01%
Global	FTSE EPRA/NAREIT Dv ex AUS TR Hdg AUD	4.63%	12.33%	12.48%	16.88%

The S&P/ASX 300 A-REIT Accumulation Index was up 14.32% over the 12 months to 31 December 2015. The S&P/ASX 300 A-REIT Index was up 2.4% in December and up 8.9% over the 1 year period ended 31 December 2015.

Over 1, 3 and 5 years, the A-REITs outperformed global REITs, while Global REITs outperformed A-REITs over the 7 year period. Global property, as represented by the FTSE EPRA/NAREIT Index, was up 4.63% over a 1 year period.

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Fixed Interest

	Index/Benchmark (% pa)	1 Year	3 Years	5 Years	7 Years
Australian	Bloomberg AusBond Composite 0+ Yr	2.59%	4.73%	6.62%	5.83%
	Australian 90 Day Bank Bill	2.26%	2.57%	3.26%	3.48%
Global	BarCap Global Aggregate Index	8.93%	10.63%	8.06%	1.77%
	BarCap Global Agg. Index Hedged	3.35%	5.27%	7.17%	7.59%

In December, the US 10 year bond yields were up 2.83%, and closed the month at 2.27%.

Australian 10 year bond yields were down 1.57%, and closed the month at 2.82%.

Over a 12 month period, the unhedged global bonds index returned 8.93%, outperforming Australian bonds which returned 2.59%. The hedged global bonds index posted a strong 1 year gain of 3.35%.

Australian dollar

In December, the Trade-weighted Index was up 1.46%, but also down 5.71% during the 12 month period ending 31 December 2015.

The AUD was up 0.41% against the USD in December, to finish the month at 73 US cents. On a 12 month basis, the AUD declined 11.1% against the USD.

The AUD was down 2.38% against the Euro in December. On a 12 month basis, the AUD was down 0.97% against the Euro.

Against the Japanese Yen, the AUD was down 2.02% in December. On a 12 month basis, the AUD was down 10.8% against the Yen.

Against the British Pound, the AUD was up 2.55% in December. On a 12 month basis, the AUD was down 5.95% relative to the British Pound.