


GODFREY PEMBROKE
market
update

JULY 2016

- ▶ After strong rises in equity prices off the lows in February, developed market equities were weaker in June, following the decision by voters in the UK to elect to leave the European Union ("Brexit").
- ▶ Gold prices rose 9% in June and crude oil prices were a little lower during the month.
- ▶ China economic data showed further softness in the manufacturing side of the economy, but other areas such as the housing and services industries were stronger in June.
- ▶ US economic data was fairly good, apart from the non-farm payrolls figures, which were the weakest since 2011.
- ▶ Economic data in Europe was fairly good – particularly in the UK, Germany and France. Eurozone inflation continues to tick up and unemployment is gradually heading lower.
- ▶ Australia's economy is in reasonably good shape with consumers and businesses finding conditions reasonably good. Property prices have been rising strongly, helped by the RBA's rate cut in May.

June market performance

Equity Markets – Price Indices	Index	At Close 30/06/2016	% Change 1 Month	% Change 12 Months
Australia	All Ordinaries	5310.41	-2.5%	-2.6%
Japan	Nikkei	15575.92	-9.6%	-23.0%
Hong Kong	Hang Seng	20794.37	-0.1%	-20.8%
UK	FTSE 100	6504.33	4.4%	-0.3%
Germany	DAX	9680.09	-5.7%	-11.6%
US	Dow Jones	17929.99	0.8%	1.8%
EMU*	Euro 100	973.26	-5.9%	-14.5%
World**	MSCI – Ex Aus (Gross) (Hedged)	1266.00	-1.4%	-4.6%

Property – Price Index	Index	At Close 30/06/2016	% Change 1 Month	% Change 12 Months
Listed Trusts	S&P/ASX 300 A-REITS	1441.25	2.1%	18.7%

Interest Rates	At Close 30/06/2016	At Close 31/05/2016	At Close 30/06/2015
Aust 90 day Bank Bills	1.96%	1.98%	2.14%
Australian 10 year Bonds	1.99%	2.31%	3.01%
US 90 day T Bill	0.26%	0.29%	0.01%
US 10 year Bonds	1.47%	1.85%	2.35%

Currency***		At Close 30/06/2016	% Change 1 Month	% Change 12 Months
US dollar	A\$/US\$	0.74	2.78%	-3.12%
British pound	A\$/STG	0.56	11.91%	13.97%
Euro	A\$/euro	0.67	2.99%	-2.84%
Japanese yen	A\$/yen	76.39	-4.92%	-18.78%
Trade-weighted Index		62.50	1.30%	-2.04%

* 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.

Global economies

It was a difficult month for equities with an initial sell off in June, after the release of weak jobs growth figures in the United States, and another decline later in the month following the UK's surprise decision to vote to leave the European Union.

In most of the major economies, manufacturing activity indicators were in expansion territory and unemployment rates continue to fall. Inflation and wage pressures are rising slowly in the United States. Housing construction and stronger activity in the services sector appears to be supporting growth in China, Australia and the United States.

US

In the United States, the initial reading of the May non-farm payrolls report was very disappointing with just 38,000 jobs created, well down on the 200,000 monthly average over the past few years.

Other activity indicators, such as the ISM surveys of activity in the manufacturing and non-manufacturing sectors, have been reasonably strong suggesting that the weak jobs growth in May could be a one-off.

Given the weak employment figures for May, and the UK Brexit vote, the US Federal Reserve chose to defer any decision to lift interest rates and their 'dot point' forecasts for interest rates show fewer rate hikes over the next couple of years.

Europe

In Europe, the economy continues to perform reasonably well. Core inflation continued to edge up, from 0.8% year-on-year in May, to 0.9% in June, and the unemployment rate fell from 10.2% in May to 10.1% in June.

Eurozone manufacturing activity indicators have improved in Germany and France, however, it remains to be seen what impact the UK's exit from the European Union will have on activity and growth in the Eurozone over the next couple of years.

One area that is cause for concern is the Italian banking sector where bad debts have risen to €360 billion due to weak growth rates and soft retail spending.

China

In China, the economy is performing in line with expectations. Manufacturing surveys showed flat to slightly weaker activity levels in June but the index of activity was stronger at non-manufacturing and services firms in June, when compared with May.

The Chinese housing market continues to perform well and new home prices have risen 6.9% over the past year and strength in the housing sector is helping to support overall construction activity.

Asia region

In Japan, the data has been mixed. Industrial production was weaker in May, by around 2.3%, but housing starts rose 9.8% year-on-year.

After the Brexit vote the Yen – often viewed as a safe haven currency – appreciated significantly and finished the month 9% stronger against the US Dollar. The stronger Yen hurts Japanese exporters and this is the reason that the Japanese stock market was almost 10% lower in June.

Australia

In Australia, employment growth has held up reasonably well and the unemployment rate remained steady at 5.7% in May. Other economic indicators such as the NAB business conditions index have also been reasonably strong compared with long term average levels. And house price growth has accelerated in recent months, particularly in Sydney and Melbourne, helped by the RBA's May interest rate cut.

At the July RBA Board meeting, the Board elected to keep interest rates on hold but the tone of the language suggested that the next move could be a rate cut depending on economic data over the next month, in particular the inflation reading for the June quarter, which will be released at the end of July.

EQUITY MARKETS

- ▶ The China Shanghai Composite Index rose 0.4% in June.
- ▶ Emerging market shares rose 1.7% in local currency terms with Brazil's Bovespa Index up 6.3%.
- ▶ The German DAX Index was 5.7% lower.
- ▶ The broader Euro 100 was 5.9% lower.
- ▶ The Japanese Nikkei Index fell by 9.6%.
- ▶ The US Standard & Poor's 500 Index returned 0.3% in June.
- ▶ Australia's S&P/ASX All Ordinaries Index lost 2.5% for the month.

Australian equities

	Index/Benchmark (% pa)	1 Year	3 Years	5 Years	7 Years
Australian	S&P/ASX 300 Acc.	0.87%	7.70%	7.20%	8.68%
	S&P/ASX 50 Acc.	-2.64%	6.41%	7.44%	8.81%
	S&P/ASX Small Ordinaries Acc.	14.40%	9.13%	1.00%	4.49%

The S&P/ASX 200 Accumulation Index lost 2.5% in June with IT and financials the biggest losers, whilst the property and utilities sectors were the best performing sectors. Small cap shares slightly outperformed larger companies again with a total return of -1.3%, including dividends.

Sector	1 Month	3 Months	1 Year
Energy	-0.8%	4.9%	-21.8%
Materials	0.6%	11.5%	-2.8%
Industrial	-1.0%	3.1%	18.7%
Consumer Discretionary	-0.2%	3.6%	19.7%
Consumer Staples	-4.0%	-3.9%	1.4%
Health Care	-2.5%	10.2%	21.1%
Financials (ex Property)	-5.9%	0.4%	-8.6%
Info Tech	-7.6%	1.5%	3.8%
Telcos	-1.3%	4.1%	-0.6%
Utilities	5.6%	9.0%	24.4%
Property	3.5%	9.2%	24.6%

BIG MOVERS THIS MONTH

Going up

↑	Utilities	5.6%
↑	Property	3.5%
↑	Materials	0.6%

Going down

↓	IT	-7.6%
↓	Financials (ex Property)	-5.9%
↓	Consumer Staples	-4.0%

Global Equities

	Index/Benchmark (% pa)	1 Year	3 Years	5 Years	7 Years
Global	MSCI World Ex Aus (Gross) in AUD	1.01%	15.46%	15.59%	12.30%
	MSCI World Ex Aus (Gross) in Local	-2.12%	9.37%	9.49%	11.69%
	MSCI World Small Cap (\$A)	-0.19%	15.76%	15.40%	14.66%
Emerging	MSCI Emerging Mkts Free	-7.35%	4.07%	2.38%	6.78%
	MSCI AC Far East Free (ex Japan)	-10.64%	3.35%	1.93%	0.07%

Developed share markets lost 1.3% in June as stocks dropped significantly in Europe following the Brexit decision in the UK. Shares in Japan were the hardest hit with a 9.6% decline over the month on concerns about the strong rise in the Yen which will hurt business competitiveness.

Also impacting share prices was a soft US payrolls figure earlier in the month. Financials were the worst performing sector as concerns about the health of the Italian banking system rose during the month. Utilities were the best performing sector globally as long term bond yields fell in the major economies which boosts the attractiveness of these defensive income-generating stocks.

Emerging markets shares rose 1.7% in June helped by gains in India, China, Mexico and Brazil. Price-to-earnings ratio valuations in developed markets have returned to the 15-17 times range, with European and Japanese shares at lower multiples than the US market.

Property

	Index/Benchmark (% pa)	1 Year	3 Years	5 Years	7 Years
Australian	S&P/ASX 300 A-REIT Acc	24.59%	18.49%	18.01%	16.52
Global	FTSE EPRA/NAREIT Dv ex AUS TR Hdg AUD	12.54%	12.46%	12.54%	17.21

The S&P/ASX 300 A-REIT Accumulation Index (which includes distributions) was up 3.5% in April and 24.6% over the 12 months to 30 June 2016. The S&P/ASX 300 A-REIT Index was up 2.1% in June and up 18.7% over the 2015/16 financial year.

Over one, three and five years, the A-REITs outperformed Global REITs, while Global REITs had marginally higher performance than A-REITs over a seven-year period. Currency-hedged global property, as represented by the FTSE EPRA/NAREIT Index, was up 12.5% over a one-year period.

Fixed Interest

	Index/Benchmark (% pa)	1 Year	3 Years	5 Years	7 Years
Australian	Bloomberg AusBond Composite 0+ Yr	7.02%	6.24%	6.74%	6.73%
	Australian 90 Day Bank Bill	2.20%	2.45%	2.99%	3.41%
Global	BarCap Global Aggregate Index	12.38%	10.12%	9.43%	4.66%
	BarCap Global Agg. Index Hedged	9.34%	7.56%	7.75%	8.16%

Australian bonds returned 1.3% in June as bond yields fell by 10-32 basis points in sympathy with the decline in bond yields in other parts of the world. The 10-year bond yield fell from 2.32% to 2.01% per annum and the two-year bond yield fell from 1.70% to 1.60% per annum.

In the United States, bond yields fell as the market significantly cut the chances of Fed rate rises in coming months. In Europe, government long bond yields moved further into negative territory with the 10-year German government bond closing at a yield of -0.13% per annum following the late June referendum where voters in the United Kingdom decided to leave the European Union. The Barclays Global Aggregate Bond Index (A\$ hedged) returned 1.98% in June boosted by falling government bond yields.

Australian dollar

The US Dollar strengthened marginally in June due to safe-haven buying following the UK referendum result. The British Pound fell to a thirty-year low and the Yen strengthened by almost 9% against the US Dollar. The Australian Dollar rose two US cents to 74.5 US cents.

Against the US Dollar, the Australian Dollar rose 2.8% for the month, and on a Trade-Weighted Index basis, the Australian Dollar was 1.3% stronger.

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