ISSUE DATE: 8-09-2017

Month in Review

Market Moves — as at 31•08•2017

RETURNS (% P.A.)	1 MTH	3 MTH	6 MTH	1 YR	3 YR	5 YR	10 YR
AUSTRALIAN EQUITIES							
S&P/ASX 200 ACCUMULATION INDEX	0.71	0.87	2.40	9.79	5.13	10.56	3.65
S&P/ASX SMALL ORDINARIES ACCUMULATION INDEX	2.71	5.12	5.44	3.20	5.68	5.72	-1.09
GLOBAL EQUITIES							
MSCI WORLD TR INDEX (AUD)	0.85	-3.27	4.85	10.71	12.54	17.80	5.33
S&P 500 TG INDEX (AUD)	0.96	-3.32	2.42	10.14	15.73	20.55	7.89
FTSE 100 TR INDEX (AUD)	-0.01	-6.31	5.09	6.24	3.81	10.66	1.20
MSCI EMERGING MARKETS NET TR INDEX (AUD)	2.90	2.70	14.41	18.00	8.16	11.02	2.69
REAL ESTATE INVESTMENT TRUSTS (REITS)							
S&P/ASX 300 A-REIT (SECTOR) ACCUMULATION INDEX	1.51	-3.21	-1.04	-6.73	10.31	13.35	-0.22
FTSE EPRA/NAREIT DEVELOPED NET TR INDEX (AUD HEDGED)	0.26	1.64	1.69	0.76	7.03	10.88	3.76
FIXED INTEREST							
BLOOMBERG AUSBOND COMPOSITE 0+ YR INDEX	-0.01	-0.66	1.70	-0.66	3.89	4.16	6.09
BLOOMBERG AUSBOND BANK BILL INDEX	0.14	0.43	0.88	1.76	2.16	2.46	3.81
BARCLAYS GLOBAL AGGREGATE TR INDEX (AUD HEDGED)	0.96	1.11	2.54	1.04	4.88	5.34	7.41

Data source: IRESS & Financial Express. Returns greater than one year are annualised.
Commentary regarding equity indices below references performance without including the effects of currency (unless specifically stated).

Australian equities

The Australian market had another flat month in August, with the ASX 200 Accumulation Index posting a meagre 0.71% return and leaning heavily on the commodities price surge. Energy shares (+6.07%) delivered the biggest gains, with Whitehaven Coal up 17.58% in price terms on the back of a rallying coal market and a record NPAT of $405m. Worley Parsons (+13.75% in price terms) also pushed higher, although shareholders will again forgo a final dividend despite a rise in profit. Steel producer Bluescope (-17.53%) had a rough month as earnings dropped and CEO Paul O'Malley announced his departure.

Consumer Staples shares (+5.94) had a bumper month, led by Blackmores (+27.67%), which gained despite a drop in sales and a cut to its final dividend by one third, while A2 Milk (+21.74%) rocketed after nearly tripling profit on the previous year. Market giant Wesfarmers (+8.98%) also had a good month, although results owed more to the group's coal division than its Coles or Bunnings businesses. Webjet delivered a total return of 9.54%, making it one of the best performing shares in August, supported by strong growth in bookings and the integration of its Online Republic acquisition.

Global equities

In the US, the S&P 500 gained 0.96% in AUD terms as global equity markets confronted renewed geopolitical tension emanating from the Korean peninsula. Once again, the market was supported by gains from the Information Technology sector (+4.15%), but this time not from usual suspects Facebook and Alphabet (Google). Apple (+11.44%) gained strongly, but non-GAFA shares such as Micron Technology (+14.44%) and payment solutions provider TSYS (+9.63%) also contributed to the sector's strength.

Globally, the MSCI World Index gained 0.85% in AUD terms, supported by Asian markets. The Euro Stoxx 600 Index rose 0.19%, with the Resources sector (+5.13%) building on July's gains, led by names such as Anglo American (+13.27%) and Rio Tinto (+7.23%). Energy giants Uniper (+21.78%) and E.ON (+14.96%) rallied in line with commodities. Germany's DAX rose a modest 0.73%, with embattled Daimler (+4.57%) recovering lost ground in the wake of the diesel scandal and Lufthansa (+17.38%) making the most of Air Berlin's insolvency.

In the UK, the FTSE 100 Index was flat, returning -0.01%. In Asian markets, the Nikkei 225 Index fell 0.52% while the Shenzhen CSI 300 Index was up 4.93%. The MSCI Emerging Markets Index rose 2.90%, supported by Chinese and Brazilian shares.

REITs

The S&P/ASX 300 A-REIT Accumulation Index returned 1.51% in August after coming under pressure in July. Gains were widely shared, although retail-focused REITs had another tough month, with Vicinity Centres (-4.73%), Charter Hall Retail REIT (-4.15%), Scentre Group (-4.00%) and Westfield (-1.18%) all down ahead of Australia's retail D-Day. Abacus Property (+14.79%) posted the largest gain in August with a 53% rise in profit, and Arena REIT (+12.14%) was also higher, announcing a 33% rise in profit and an average like-for-like rental increase of 70bps. Overall, it was a solid reporting season for A-REITs, with strong demand for quality real estate boosting asset values and NTAs, and continued strength in the Sydney and Melbourne office markets.

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Global REITs were slightly lower in August, with the S&P Global REIT NTR Index down a modest 0.12% (in AUD hedged terms), while the FTSE EPRA/NAREIT Developed NR Index managed a gain of 0.26%. In the US, yield REIT sectors have generally outperformed through the middle of 2017, including the net lease and manufactured housing sectors. As a whole, REITs have been held back by growth sectors such as offices, malls and hotels. Low volatility remains an attraction, however, and a structural fall in volatility could boost valuations and risk-adjusted returns.

Fixed income

Global yields were compressed in August as investors sought safer ground in bonds, gold, euros and yen. The US 10-year Treasury yield fell from 2.30% to 2.12%. The return on US corporate investment grade bonds was 0.83% in August, with the index reaching a new record high, while US high-yield debt returned 0.18%, with the index similarly near record high levels. The BofA Merrill Lynch US High Yield OAS expanded slightly in August from 3.61% to 3.85%, reaching an intra-month high of 4.00%.

Global bonds, measured by the Barclays Global Aggregate TR Index, returned 0.96% in August (in AUD hedged terms), with developed market indices still close to their all-time highs. Bucking the trend was Australia, with the Ausbond Composite Index returning -0.01%. Returns on corporate bonds were -0.04% while government bonds returned 0.18%. The Australian 10-year Treasury yield rose from 2.68% to 2.71%, but was still down on its March peak of 3.05%. The UK 10-year Gilt yield plunged 23bps to 1.00% in August. The German 10-year Bund yield fell from 0.54% to 0.36% and the 5-year Bund pushed further negative from -0.18% to -0.35%.

The Japanese 10-year bond yield dropped from 0.075% to 0.004% in August and headed for negative territory. The move may be seen as the result of a successful intervention by BoJ Governor Kuroda, who in July offered to buy an unlimited amount of JGBs to support the Bank's policy of holding the 10-year yield at 0%. It is estimated that the BoJ now holds more than 50% of outstanding JGBs in the five- to 10-year range of maturities, leading investors to wonder when the Bank will begin scaling back its stimulus.

ASX 200 Share Movements

S&P/ASX 200 Share Performance for the Month of August

BEST PERFORMERS		WORST PERFORMERS	
CREDIT CORP GROUP LTD	9.61%	ISENTIA GROUP LTD	-17.34%
WEBJET LTD	9.54%	AUSTRALIAN PHARMACEUTICAL INDUSTRIES LTD	-14.39%
GALAXY RESOURCES LTD	8.42%	SIMS METAL MANAGEMENT LTD	-13.45%
STEADFAST GROUP LTD	8.11%	MAYNE PHARMA GROUP LTD	-11.45%
CYBG PLC	8.05%	MANTRA GROUP LTD	-9.80%

S&P/ASX 200 Share Performance for the Year to August

BEST PERFORMERS		WORST PERFORMERS	
A2 MILK CO LTD	136.59%	MAYNE PHARMA GROUP LTD	-54.05%
MONADELPHOUS GROUP LTD	86.17%	VOCUS COMMUNICATIONS LTD	-54.05%
QANTAS AIRWAYS LTD	83.12%	TPG TELECOM LTD	-53.99%
COSTA GROUP HOLDINGS LTD	77.68%	SIRTEX MEDICAL LTD	-52.58%
NINE ENTERTAINMENT CO HOLDINGS LTD	64.30%	ISENTIA GROUP LTD	-50.36%

Economic News

Australia

With solid GDP growth and continued improvement in the labour market, the Australian economy appears well positioned despite wage weakness. The RBA is possibly even more bullish on employment than in previous months, noting that stronger labour market growth should see a pickup in wages over time. The main challenge is in achieving a balance between stimulatory monetary policy and the medium-term risk of high and rising household debt. Add to the mix an appreciating dollar over recent months, which will likely contribute to subdued price pressure, and it seems rates are destined to stay on hold for some time yet. At its September meeting the RBA left the **cash rate** on hold at 1.50%, where it has remained since the most recent downward move in rates one year ago. Lower petrol prices have contributed to lower inflation, with prices at the pump down 15c/litre nationally since early June.

According to the latest **GDP figures**, Australia's economy grew 0.8% in the June quarter, and 1.8% over the year. Household spending grew 0.7%, picking up on the previous quarter's 0.5%. However, the household saving ratio is only 4.6% in seasonally adjusted terms, down from 5.3% in the March quarter. The ratio has slipped from over 10% in June 2012, while over the past five quarters gross disposable income has grown at an

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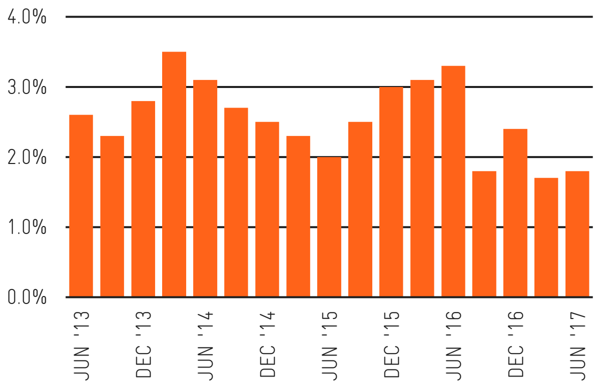
average of only 0.5% (consistently lower than the growth in household spending).

Australia's labour market continues to improve, with 12,201 seasonally adjusted jobs added in July and the **unemployment rate** edging down further from 5.7% to 5.6%. While there was a drop in full-time employment of 20,300, full-time jobs have grown now by around 220,000 persons since September 2016, and makes up the majority of the 250,000 person increase in employment over the period. Monthly hours worked fell 14.4 million hours while the participation rate rose 0.1 points to 65.1%.

Australia GDP y/y growth



Source: ABS

The **AIG Manufacturing Index** jumped 3.8 points to 59.8 in August. Production and new orders were especially strong (61.4 and 64.3 points), but they were coupled with a robust expansion in inventories (58.9 points) rather than in sales (50.9 points). Exports contracted mildly (49.3 points). This suggests current activity is geared towards future orders and stockpiling rather than for immediate delivery. Employment and supplier deliveries expanded at a slower pace in August than in July.

Retail turnover was flat in July, missing the forecast 0.2% growth and following a 0.3% gain in June. Household goods retailing (-1.7%) took a hit and department stores (-2.8%) experienced the sharpest monthly downturn since July 2016, while the major food retailing segment (+0.7%) saw a solid boost.

Australia's consumers are still struggling to stay positive. The Westpac Melbourne Institute **Index of Consumer Sentiment** fell 1.2% in August from 96.6 in July to 95.5. While the jobs environment is improving, survey details indicate households are feeling the pinch, with concerns around interest rates and housing affordability. Some of the softening in sentiment in August may be a delayed reaction to recent mortgage rate increases, with the major banks raising rates on interest only mortgages in late June.

Global

The second estimate for **US Q2 GDP** showed real growth of 3.0% p.a., up from the first estimate reading of 2.6% and well ahead of the surveyed 2.7%. Personal consumption expenditure (PCE) grew at a healthy 3.3%. The impact of Hurricane Harvey, which ravaged parts of Texas, is expected to have an impact on output, although estimates for Q3 growth remain relatively positive, with the Atlanta Fed's GDPNow model tracking at 3.2% following the release of employment figures.

In a shock for Fed watchers, Vice-chair Stanley Fischer submitted his resignation in early September, citing personal reasons. His departure leaves the Fed with only three out of its seven board seats – the smallest number in the Fed's history – and giving President Trump the opportunity to appoint a majority of the Fed's board. Minutes from the Fed's July meeting revealed some concern with recent inflation results. In June, the staff forecast for the core PCE index was revised down for 2017 from 2.0% to 1.7% in response to weaker-than-expected data, and the board expects inflation to remain below 2% in the near term.

The **ISM manufacturing PMI** moved higher in August from 56.3 in July to 58.8 in August, beating expectations and notching up the 99th consecutive month of expansion. Most sub-indices were higher on the previous month, including Production (+0.4 to 61.0), Employment (+4.7 to 59.9), and Inventories (+5.5 to 55.5). New Orders were down slightly (-0.1 to 60.3) but still firmly in expansion, New Export Orders softened (-2.0 to 55.5), and Prices were steady at 62.0.

Non-farm payrolls delivered on the downside in August, with 156,000 jobs added versus the expected 180,000. The unemployment rate was slightly higher from 4.3% to 4.4%. With data predominately collected before Hurricane Harvey hit, there was very little impact on the figures. The number of long-term unemployed (those jobless for 27 weeks or more) was essentially unchanged in August at 1.7m and accounted for 24.7% of the unemployed. The broader U-6 measure of unemployment, which includes discouraged workers and those marginally attached to the labour force, was steady at 8.6%.

US CPI figures rose 0.1% in July on a seasonally adjusted basis and 1.7% on an unadjusted y/y basis. The energy index showed signs of stabilising, with gasoline prices flat after a period of volatility since the start of 2017. The core PCE index – the Fed's preferred measure – fell to an annual 1.4% in July, down from the more promising level of 1.9% reached at the start of 2017 and lower than the 1.7% forecast for 2017.

For those in need of their political hit following major elections in the US and Europe, the **German federal election** to be held on 24 September is now the main event. Polls point to the return of Angela Merkel as

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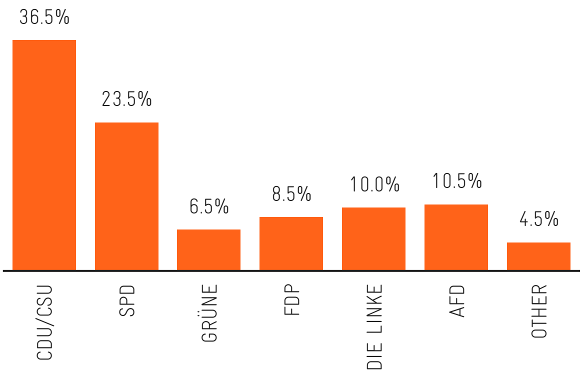
Chancellor, with the return of the 'grand coalition' between Merkel's CDU and the centre-left SPD likely, although there is a chance the CDU could form a government with the free-market FDP and Greens. The right-wing AfD has seen its poll numbers reduced due to infighting. Of course, while the result may seem like a foregone conclusion, recent history would warn against such presumptions.

German federal election polling



Source: Insa, Handelsblatt, 4 September 2017

Euro area GDP grew by 0.6% in Q2 2017 according to August's flash estimate, representing annual growth of 2.2%. Over recent quarters, the economic recovery has also become more broad-based across euro area countries and the different sectors of the economy. The IMF predicts the Eurozone will grow 1.9% in 2017. The ECB left its key rates on hold once again in early September, confirming that its net asset purchases of €60 billion per month will run until the end of 2017, or beyond if necessary. The ECB is forecasting economic growth of 2.2% in 2017 and 1.8% in 2018.

Of concern to the Governing Council is the surprise comeback of the euro, which broke the USD 1.20 mark in August and reached its highest value since January 2015. Recent euro strength has been driven by political uncertainty, including a US showdown with North Korea, prompting investors to swap their dollars for euros. However, the main driver behind the rise of the euro since the start of 2017 has undoubtedly been the divergence between Fed and ECB monetary policy.

Euro area inflation is expected to be 1.5% p.a. in August, up on 1.3% in July. Core inflation (excluding energy, food, alcohol and tobacco) was steady at 1.2%. **Euro area unemployment** was steady at 9.2% in July and remains the lowest rate recorded since February 2009. Dispersion in unemployment rates is still present among members, but the gab has been narrowing steadily as the unemployment rate falls across the board.

China's GDP recorded growth of 6.9% in Q2 2017, which proved enough to ward off fears of a slowdown, as well as satisfying officials that efforts to tighten lending have not been detrimental to the economy. **China's official PMI** survey was boosted in August, reaching 51.7, up from July's 51.4 and beating the expected 51.3. The Caixin PMI, which surveys smaller, private manufacturers, defied expectations of a fall, moving up from 51.1 in July to 51.6 in August.

In other **emerging markets**, Brazil's GDP grew by 0.2% on through Q2 2017, marking the second consecutive quarter of positive growth and an end to the worst recession in the country's history. Unemployment continued to fall, reaching 12.8% from 13.0% in July. Russia's CPI fell to a new low of 3.3% – the lowest rate since the collapse of the Soviet Union – putting pressure on the CBR to cut its policy rate from the current 9.0%. India's GDP for Q1 2017 slowed to 5.7% y/y, down on Q4 2016 growth of 6.1%. With the impact of demonetisation and the GST now in the rear-view mirror, growth is anticipated to move higher for the remainder of 2017.

Commodities

Commodities had a bumper month in August, driven higher in the wake of North Korea's missile tests. Nickel rallied the hardest, gaining 15.5% and reaching its highest price level since July 2015, while Zinc rose 12.6% to hit its highest point since 2007. Aluminium jumped 10.38% after a period of flatness since March, copper gained 6.6% after a sharp move higher in July, lead rose 2.6% and tin 0.10%.

The price of iron ore delivered to Qingdao in China rose 7.1% to US $78.91/t after rising 13.5% the previous month. Gold finished 4.1% higher at US $1,321.43/oz after posting solid gains in July. In oil markets the Brent spot price fell 0.5% from USD $52.65/b to $52.38, and WTI fell 5.9% from $50.17 to $47.23.

Currencies

The AUD fell 0.65% against the USD in August, but remained at an elevated level after rising sharply in July, finishing the month at USD 0.7928. In trade-weighted terms, the AUD depreciated 1.5%, dampened by a fall in export prices and volumes. The AUD ended the month down against major currencies, including the EUR (-1.3%) and JPY (-0.9%) but was higher against the GBP (+1.6%) and NZD (+3.9%).

The US Dollar Index closed the month 0.6% lower, and has been falling steadily since the start of 2017. The USD was down against the EUR (-0.6%), JPY (-0.2%) and CHF (-0.5%) and higher against the GBP (+2.3%). The EUR has had an impressive winning streak through the year to date, boosted by the continued economic recovery, which appears broad-based, but benefiting from a weaker USD.

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