

MARKET REVIEW

30-April-2009

International Economic Review

United States

The early estimate of growth for the March quarter showed the US economy contracted a quarterly annualised rate of 6.1%, marking the first three consecutive quarters of falls in 34 years. Growth was dragged down by a record drawdown in business inventory and a collapse in exports.

Employment fell for the fifteenth straight month in March, shedding 663,000 jobs. Disappointingly, January's figures were also revised to show a steeper loss of 741,000 jobs, the third largest decline on record. Unemployment rose 0.4% to 8.5%, the highest rate since November 1983.

Retail sales slumped 1.1% in March, reversing the rises seen in January and February. Pleasingly, the University of Michigan Consumer Sentiment Survey strengthened to 61.9 in March from 57.3 in February.

Housing data remained weak with starts and permits falling 10.8% and 9.0% respectively. New homes sales remained unchanged while existing sales fell 3.0% for the month.

Headline CPI edged up 0.1% in March while core CPI rose 0.2%. The annual growth in headline CPI now stands at -0.4%, the lowest number since August 1955, while core CPI rose 1.8% for the year.

While current data remains weak, the closely-watched ISM Manufacturing Index continued its recovery; up 0.5 points to 36.5 in March. Other regional surveys also showed a slower pace of contractions. The Non-manufacturing Index fell a modest 0.8 points to 40.8 in March.

Europe

The closely watched indicator of growth outlook for Europe, the IFO Survey unexpectedly rose 1.6 points to 83.7 in April. Similarly, the ZEW Index rose 16.5 points to 13 in April. Similar to the US, while the deterioration in the outlook data has eased somewhat, the current economic conditions continue to worsen. Europe's unemployment rate rose to 8.9% in March. The European Central Bank (ECB) eased another 25 basis points (bps) to 1.25%, less than the 50 bps expected by the market.

Asia

In Japan, the latest Tankan Survey showed a sharp fall in business sentiment for the March quarter. The Large Manufacturing component fell to -56 compared to -24 previously, while Large Non-manufacturing posted -31, a sharp fall from -9 in the previous quarter. Elsewhere there were some upside surprises with Machinery Orders posting a 1.4% rise in February, and a 1.6% rise in industrial production for March.

In China, the NTC Chinese PMI eased 0.3 points to 44.8 following three consecutive months of rises. The PMI remained below the expansionary level of 50 for the eighth consecutive month.

Australia

The Reserve Bank of Australia (RBA) lowered interest rates by 25 bps to 3.0% in early April, splitting the difference between market expectations of 'no change' and a 50 bps reduction. Following the move, in a key speech later in the month, RBA Governor Glenn Stevens admitted for the first time that Australia was in recession. Evidently, the closely watched Westpac/MI Leading Index fell 0.3% in February and brought the annual rate to -5.1%, the fastest pace of contraction since 1982. As widely expected, the RBA kept official rates on hold following their May board meeting.

Other economic data releases were mixed during the month. Employment fell 34,700 in March following a revised increase of 1,100 in February. Part-time employment rose 4,200, while full time employment fell an alarming 38,900. The unemployment rate rose 0.5% to a 5-year high of 5.7%, already the highest level since early 2004.

Retail sales fell 2.0% in February, and January's increase of 1.0% was revised down to 0.5%. In the corporate world, the NAB Business Confidence Survey rose 9 points to -13, and the Business Conditions Survey rose 3 points to -17 in March.

Private sector credit growth edged 0.1% higher in March to be only 4.9% higher in annual terms. The credit crunch and tightening lending standards have led to the slowest annual rate of credit growth since 1993. Housing finance approvals edged 0.4% in February after rising a healthy 4.9% in January with the First Home Owners' Grant again accounting for much of the demand.

The Westpac/MI Index of Consumer Confidence rose 8.3% in April to 92.7, sharply reversing the fall in March. The second round of fiscal stimulus and rebound in the sharemarket helped to improve sentiment to a fourteen-month high.

On inflation, headline CPI edged 0.1% higher after a decline of 0.3% in the previous quarter. This brought the annual headline CPI down to 2.5%, marking the first time since the third quarter in 2007 that the annual rate fell within the RBA's 2-3% target. Interestingly, however, the RBA's underlying measures were again printed well above the headline figure. The closely watched weighted median and trimmed mean measures stand at 4.4% and 3.9% respectively.

International Sharemarket Review

The global sharemarket continued to experience the rebound that began in March, with broad base gains across most regions. Optimism around the G20 summit in London and some stabilisation in the economic data releases helped to edge the market higher. Importantly, the market also managed to weather news of a possible swine flu pandemic.

Major bourses performed for the month as follows:

Japan Nikkei 225	8.9%
UK FTSE 100	8.1%
US Dow Jones	7.3%
US S&P 500	9.4%
German DAX	16.8%

Australian Dollar Outlook

Major bourses performed for the month as follows:

Japan Nikkei 225	7.1%
UK FTSE 100	2.5%
US Dow Jones	7.7%
US S&P 500	8.5%
German DAX	3.8%

Australian Sharemarket Review

The local equities market built upon the strong gains recorded in March, albeit at a slower pace, gaining 5.6% (S&P/ASX 200 Accumulation Index) for the month. These gains were despite some material earnings downgrades from some big names including Qantas, OneSteel, Aristocrat Leisure and Boart Longyear.

On a sector basis, Resources (up 4.3%) and Healthcare (up 3.9%) underperformed, while the standouts for the month were Consumer Staples (up 11.9%) and Consumer Discretionary (up 11.7%), a benefactor of the latest round of stimulus spending.

The Federal Government surprised many when it revealed there would be no contract for the National Broadband Network but instead proposed their own high speed broadband network. This caused apprehension regarding the upcoming budget and its implications for other sectors. An outbreak of swine flu created uncertainty late in the month, however, it remains to be seen whether this will affect Australia.

Large Caps

The best performing Australian large-cap stocks during the month were Asciano Group (47.3%), ABB Grain (45.8%) and Lion Nathan (45.2%).

- Asciano Group continues its asset sales process, with a transaction likely before 30 June 2009. The company is considering several offers for assets as well as bids for the entire company.
- ABB Grain received a non-binding takeover proposal from Canadian agribusiness firm, Viterra, to acquire all of its shares. The proposal comprises a mix of cash, Viterra shares and franked dividends.
- Lion Nathan's board have recommended to shareholders a share takeover offer from Japanese brewer Kirin Holdings, to acquire all outstanding shares held in the company (Kirin Holdings currently own 46.13%).

The worst performing large-cap stocks were Iluka Resources (-18.1%), Bendigo and Adelaide Bank (-16.2%) and Commonwealth Property Office Fund (-9.9%).

- Sales volumes for Iluka Resources in the March quarter were well below expectations, and the company plans to adjust its production base in response to weak demand for its major products.
- Bendigo and Adelaide Bank released its trading update and revised earnings guidance with a revised forecast for cash earnings. This was caused by the continued constraint of funding and deterioration in margins in the March quarter in particular.

Small Caps

The best performing Australian small-cap stocks during the month were Pacific Brands (185.7%), Aditya Birla (157.1%) and Biota Holdings (145.0%).

- The market reacted positively to the debt extension negotiated by Pacific Brands, with concerns easing of a breach of debt covenants.
- The outbreak of swine flu throughout the world has benefited Biota Holdings, a leading anti-infective drug development company which specialises in respiratory diseases, particularly influenza.

The worst performing stocks were St Barbara (-34.1%), Flinders Mines (-28.3%) and Macmahon Holdings (-22.7%).

- Cost blowouts and production costs affected St Barbara's share price during the month, with new Managing Director, Tim Lehany, conceding that its Leonora mine in Western Australia is close to being unprofitable.
- Macmahon Holdings announced a profit warning, revising down its expected FY09 profit after tax from \$40m to \$15-20m, citing deteriorating market conditions and several one-off impacts.

Major Indices

The major indices performed as follows during April:

S&P/ASX 200 Accumulation Index	5.6%
S&P/ASX 200 Industrials Accumulation Index	6.1%
S&P/ASX 200 Resources Accumulation Index	4.3%
S&P/ASX Small Ordinaries Accumulation Index	13.5%

Listed Property

The Australian property sector gained 6.1% in April as measured by the S&P/ASX 200 A REIT Accumulation Index. While this represents a slight outperformance of the broader market (up 5.6%), the sector has a lot of ground to cover to pull back the extensive losses of the past 12-18 months. If it were not for a mid-month pull-back following a capital raising announcement by Dexus Property Group, the gains would have been greater, with the sector generally continuing its positive trend from March.

There was again support for previous poor performers as investors' risk appetite increased, with defensive stalwarts like Commonwealth Property Office Fund and CFS Retail Property Trust suffering at the hands of sector rotation.

Australian Fixed Income Review

At its regular monthly board meeting, the RBA chose to further trim official interest rates by 0.25% to 3.0% in April, and left rates on hold following their May meeting. Market expectations continue to favour further rate cuts in coming months.

The global economy remains in recession. Unemployment rates, a lagging economic indicator, continue to rise around the globe. In Australia, the unemployment rate rose sharply by 0.5% to 5.7% last month and has now risen a sizeable 1.8% from its cycle low, back in February 2008. Leading indicators signal worse is to come.

The Federal Government continued to issue Commonwealth Government Bonds (with more coming in the next couple of years), and the major banks continued to issue under the Commonwealth Government guarantee as well as, pleasingly, sizeable issuance without the guarantee.

In terms of market moves, the benchmark 90-day bank bill rate closed lower by 0.06% at 3.08%, the Australian 3-year benchmark Commonwealth Government Bond closed higher by 0.05% at a yield of 3.42% whilst in the longer end the 10-year benchmark Commonwealth Government Bond also closed higher in yield by 0.17% at 4.57%. The UBS Composite Bond Index returned essentially zero.

International Fixed Income Review

The economic backdrop remains poor and the global economy remains in recession, however, so called "green shoots" off better economic numbers have appeared. At this stage though, this represents a moderation in the pace of collapse more than genuine recovery, but is nonetheless worth monitoring. Unemployment rates continue to rise everywhere.

Various central banks cut official rates further in April. The European Central Bank (ECB) cut 0.25% to 1.25%, the Bank of Canada 0.25% to just 0.25% and the Reserve Bank of New Zealand by 0.50% to 2.50%. The Canadian and New Zealand central banks flagged little prospect of reversing course before mid next year. Apart from official rate cuts, policy makers continue to evolve new initiatives especially with regard to fiscal policy measures.

In terms of price action, in the US the 2-year note closed modestly higher by 0.10% at 0.90%, but the 10-year note, the global benchmark, closed at calendar year highs of 3.12%, up some 0.45% as "green shoots" news weighed on fixed income sentiment. In other key global bond markets, the UK 10-year Gilt closed higher by 0.33% at 3.50%, the German 10-year Bund higher by 0.19% at 3.18%, whilst the Japanese 10-year maturity closed at 1.43% up by 0.08%. The global fixed income market return, as measured by the Barclays Capital Global Aggregate Index (hedged into A\$), delivered a positive return of 0.64%.

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