

## **MARKET REVIEW**

31-March-2009

### **International Economic Review**

#### **United States**

While some weakness still appears in the US economy, there were some bright spots in the data releases for March. The ISM Manufacturing Survey improved slightly, though remaining at recessionary levels at 35.8. The Non-manufacturing Index fell another 1.3 points to 41.6. Industrial Production continued to trend down, falling 1.4% in February to be 11.2% lower over the year. Durable goods orders for February rose 3.5% and the closely watched Core Capital Goods Orders rose 6.6%.

Employment fell for the fourteenth straight month in February, shedding 651,000 jobs. Disappointingly, the previous two months' declines were also revised higher. The unemployment rate jumped 0.5% to 8.1%, with this latest rise bringing the number of unemployed to 12.5 million, the highest level since December 1983.

Pleasingly, there was some good news in the housing sector. Housing starts bounced 22.2% to 583,000 in February, primarily due to better weather, while building permits rose 3% for the month. Importantly, the new and existing home sales rose 4.7% and 5.1% respectively in February. On retail sales, the headline number eased 0.1% in February, however, retail sales excluding Auto rose 0.7%. Headline retail sales excluding Auto were also revised higher for the previous month.

In terms of pricing, headline CPI rose 0.4% in February, the largest monthly rise since July last year, while core CPI was also up by 0.2% for the month. The annual growth in headline and core CPI stands at 0.2% and 1.8% respectively. Elsewhere consumer confidence rose slightly from its all time low to 26 from 25.3 previously.

On the policy front, the US Federal Reserve has committed to purchasing an additional \$750bn of agency mortgage-backed securities, a further \$100bn of agency debt and up to \$300bn of longer term treasuries. US Treasury Secretary Timothy Geithner also unveiled the Public-Private Investment Program (PPIP), under which \$75-\$100bn in TARP funding, coupled with private funds, would be used to purchase up to \$1 trillion in "toxic" securities and "troubled" loans to help banks free up their balance sheets.

#### **Europe**

On the back of further evidence of economic slowdown, the Bank of England (BoE) eased interest rates by a further 50 bps to a new low of 0.5%. Importantly, it also indicated that the central bank would inject \$75bn into the economy over the next three months via bond purchases.

The closely watched proxy for European growth outlook, the IFO Business Climate Survey, fell 0.5 points to 82.1 in March. Meanwhile, the ZEW Survey rose better than expected by 2.3 points to -3.5 in March. The European Central Bank (ECB) also cut the key rate by 50bps to

1.5% as expected, but unlike other central banks it gave no clear guide as to its thinking on stimulus through quantitative easing.

### Asia

In China, the NTC Chinese Purchasing Managers Index (PMI) rose in February to 45.1 from 42.2, but remained below the expansionary level of 50 for the seventh consecutive month. The latest reading on inflation showed CPI declined 1.6% in annual terms due to lower food prices and the collapse of commodity prices.

The data released in March continued to portray grim economic conditions in Japan. Industrial Production fell 9.4% in February to be 38.4% lower over the year. Retail sales fell 0.3% in February, while the January number was also revised lower. Concern over the country falling into deflation intensified with latest national CPI showing a fall of 0.1% for the year. On a positive note, the Shoko Chukin Small Business Confidence Index rose 5.4 points to 30.4 in March.

### Australia

The national account report for the December quarter showed the economy contracted for the first time in eight years, raising the prospect of Australia entering its first recession since 1991. GDP fell 0.5% following an expansion of only 0.1% in the September quarter last year. The annual rate of growth slowed from 1.8% to 0.3%.

On more recent data flows, employment rose 1,800 in February following a revised increase in January of only 300. The more closely watched unemployment rate rose 0.4% to a 4-year high of 5.2%.

Consumer confidence eased back 0.2 points in March to 85.6 after slumping 4.6 points in February. Retail sales slumped in February after the government's \$8bn cash payments to households lifted sales in the previous two months. Sales fell 2.0% in March and are now 4.1% higher over the year.

Private sector credit was unchanged in February following a 0.6% rise in January. The annual rate slowed to 5.4, the lowest rate since 1994.

The NAB Business Conditions Survey plunged 9 points to -20 in February, the lowest reading in the survey's history. Meanwhile there was some improvement in the Business Confidence Survey from -32 to -22, but that remains par to the level seen in the 1990s recession.

### International Sharemarket Review

Global equity markets began the month poorly after AIG (American International Group) reported the largest corporate loss in US history, requiring another government bailout. Beyond this event, equities staged a solid rally based on some favourable major US bank profit announcements, some better than expected economic data out of the US, and a positive reaction to the US Treasury's PPIP aimed at ridding banks of toxic assets.

Markets remain in negative territory this year. Regarding global indices, the US S&P 500 gained 8.5% for the month, its best month since October 2002. Despite the rally from 10 March, the S&P 500 still declined for the sixth successive quarter. Japan's Nikkei 225 gained 7.1%, and the FTSE 100 in the UK increased 2.5% for the month.

Many market observers remain sceptical on this latest rally. Late last month, Treasury Secretary Timothy Geithner warned that some banks would need more government assistance. Significantly, President Obama's auto industry taskforce rejected restructure plans submitted by ailing US automakers, suggesting many corporates outside the financial sector remain vulnerable.

## 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

Early March saw the local equity market fall to new lows, before making a recovery later in the month, as confidence renewed following further global stimulus measures and the PPIP announcement in the US. The S&P/ASX 200 Accumulation Index ended the month up 8.0%, assisted by Resources (+9.2%), following better than expected economic data from the US and China, and Banks (+15.0%). In a trend reversal, the more defensive sectors were hit, with Healthcare affected by the rising Australian dollar and Telecommunications weighed down by Telstra's exclusion from the National Broadband Network (NBN) process.

### Large Caps

The best performing Australian large-cap stocks during the month were Macquarie Communications Infrastructure Group (175.9%), Asciano Group (104.5%) and Macquarie Countrywide Trust (100.0%).

- The Macquarie Communications Infrastructure Group Board recommended a \$1.37bn (\$2.50 per share) takeover bid by Canada Pension Plan Investment Board (CPPIB).
- Asciano Group is looking to announce the sale of assets in the near future, as it is currently fielding proposals, possibly leading to a buyout of the group.

The worst performing large-cap stocks were PaperlinX (-19.6%), Austar United Communications (-16.0%) and Oz Minerals (-11.9%).

- The Foreign Investment Review Board approved Paperlinx's \$700m sale of its Australian manufacturing arm to Japan's Nippon Paper, the proceeds of which will be applied to reducing debt.
- Austar United Communications, a subscription television services provider, concluded its 21.8 million share buy-back program worth \$17 million (commenced in December 2008) on March 24, 2009. The company has bought back and cancelled 68 million shares at a cost of \$72 million since May 2008.

### Small Caps

The best performing Australian small-cap stocks during the month were FKP Property Group (174.0%), APN European Retail (136.8%) and Alesco (105.1%).

- Speculation surrounding a possible acquisition of some of FKP Property Group's assets by its largest two shareholders, Mulpha and Stockland, drove the share price up during March. The Group also mentioned that the recent announcement of the conditional pre-sale of the Energex building may have also contributed to the significant price rise.
- At the end of the month Alesco shares soared on news that it may sell its Biolab subsidiary, with several companies having already expressed an interest.

The worst performing stocks were Hastings Diversified (-50.4%), Albidon (-45.8%) and Centro Retail Group (-28.2%).

- Speculation surrounded Hastings Diversified as to whether it may have to sell assets such as the Epic Energy pipeline and its stake in UK-based South East Water. There was also a dividend cut during the month.
- Albidon went into a trading halt in March following its subsidiary, Albidon Zambia, receiving notice of default from lenders to the Munali nickel project.

### **Major Indices**

The major indices performed as follows during March:

S&P/ASX 200 Accumulation Index	8.0%
S&P/ASX 200 Industrials Accumulation Index	7.4%
S&P/ASX 200 Resources Accumulation Index	9.4%
S&P/ASX Small Ordinaries Accumulation Index	10.2%

### **Listed Property**

The Australian property sector fell only slightly in March, recording a 0.04% drop according to the S&P/ASX 200 A-REIT Accumulation Index. This was a sizeable underperformance compared to the broader market which gained 7.98%. The sector followed other sectors of the market in reaching new lows early in the month, before rallying hard to close the month about even. The start of the month continued on from February. Weakness in the sector saw the first week fall 17.75%. This brought the sector to an oversold point, and the rally occurred as risk sentiment changed and higher-beta stocks were preferred to the recent well-performing defensive stocks.

### **Australian Fixed Income Review**

At the regular monthly board meeting, the Reserve Bank of Australia (RBA) left rates on hold at 3.25%. Market expectations continue to favour further rate cuts in the coming months.

On the economic front, the recent poor trends continue. The global economy is in recession and unemployment rates, whilst a lagging economic indicator, are rising around the globe. In Australia, the unemployment rate rose to 5.2% from 4.8% last month and has now risen 1.3% from its low in February 2008.

From an issuance perspective, the Federal Government continued to issue Commonwealth Government bonds. The major banks also continued to issue under the Commonwealth Government guarantee whilst the Government also extended this guarantee to semi-government authorities should they choose to use it.

In terms of market moves, the benchmark 90-day bank bill rate closed lower by 0.02% at 3.14%, the Australian 3-year benchmark Commonwealth Government bond closed higher by 0.13% at a yield of 3.37%, while in the longer end the 10-year benchmark Commonwealth Government bond also closed higher in yield by a modest 0.02% at 4.40%. The UBS Composite Bond Index delivered a return of 0.12%.

## International Fixed Income Review

There has been no change to the global economic backdrop which remains poor and the global economy remains in recession. Various central banks cut rates further in March with the BoE, the ECB, the Bank of Canada and the Bank of New Zealand all lowering their respective official cash rates.

Apart from official rate cuts, policy makers continue to announce new initiatives with both the BoE and US Federal Reserve announcing they will be operating in the market to buy longer dated government bonds in the coming months.

Prices were broadly higher during the month, where the US Treasury market's 2-year note closed lower in yield by 0.17% at 0.80% and the US 10-year note, the global benchmark, closed at 2.67% lower in yield by 0.35%. In other key global bond markets, the UK 10-year gilt closed lower in yield by 0.45% at 3.17%, the German 10-year bund closed lower in yield by 0.12% at 3.11% while the Japanese 10-year maturity closed slightly up in yield at 1.35%. The global fixed income market return, as measured by the Barclays Capital Global Aggregate Index (hedged into A\$) delivered a strong positive return of 1.05%.

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