Market Highlights – May 2016

- Share markets bounced strongly on central bank stimulus and softer US dollar
- Recovery in China's construction industry supported higher commodity prices
- The AUD rose strongly on declining investor risk aversion but fell on RBA rate cut

Central banks support markets

Improved industrial data in the US and China, and the softening of the US dollar (USD), saw further strength in share and commodity markets in April. This further bolstered markets after three major announcements by central banks over the past few months:

- The European Central Bank (ECB) – in March the ECB increased the monthly size of asset purchases to €20 billion. The ECB also provided cheap funding to the banks, reducing the risk that tighter lending conditions would stifle euro zone growth.
- The US Federal Reserve (Fed) – at its April meeting the Fed retained a level of caution, continuing to signal a reluctance to raise interest rates for the near future on still low inflation and wages growth. The USD softened as a result.
- China stimulus – Government measures to boost credit growth continued to provide genuine support to the industrial sector through a lift in residential construction and infrastructure investment. Steel and commodity markets have surged on the stimulus measures due to relatively low steel inventory.

In contrast, even as risk assets recovered, indicators point to a continued sharp softening in US GDP growth while the US share market's (S&P 500) earnings per share track at a negative pace. Improved investor sentiment and a re-rating across most markets, even as earnings growth remained weak, drove the share market rally.

In Australia, the surprise dip in inflation (-0.2% in the first quarter of 2016) drew a rapid response from the Reserve Bank of Australia (RBA) with rates cut by 0.25% on 3 May, and prospects for further rate cuts factored in. This rapidly transmitted into a sharp downward correction in the AUD, which had been surging upwards on higher commodity prices.

Overall, solid jobs growth has seen the Australian unemployment rate fall back to 5.7%, modestly below recent highs and around the levels of late 2013. However, consumer confidence and retail sales have softened, possibly reflecting a more subdued outlook for housing and soft wages. In contrast, most measures of business confidence have maintained support.

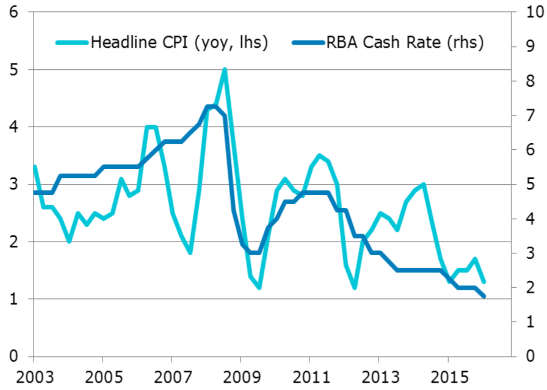
Shares

Global developed share markets rose by 0.6% in USD terms in April, on the back of central bank stimulus. The US market continued to recover with returns up 0.3% as Fed comments saw markets further reduce expectations for rate rises over the next three years. European equities were up 0.7% while Japan was down 0.5%. Japan continues to be buffeted by a strong currency and sharply weaker business surveys.

The Australian share market surged by 3.3%, led by the resources sector, which performed well on higher commodity prices. Returns in the industrial sector of the market were constrained due to the impact of the higher AUD while the banking sector continues to be impacted by rising non-performing loans and the need to build capital buffers.

Emerging market shares slightly underperformed developed markets, up 0.4% in USD terms. Chinese stimulus supported returns, although over 12 months emerging market share returns remain deeply negative. This likely reflects concerns that levels of debt in USD remain high and the Fed is still set to tighten interest rates, albeit gradually.

Inflation and Interest Rates



Bloomberg, ANZ Wealth

Bonds

Despite the rally in riskier assets, bond returns continued to lift, possibly due to soft growth and inflation, further central bank support and the RBA cutting rates. US 10 year yields rose to 1.85%, while core European longer term bond yields edged up.

Conditions across credit markets generally continued to improve as the bounce in commodity and energy prices helped reduce the magnitude of corporate defaults in the high yield market and the energy sector. Across investment grade corporate bonds, central bank stimulus measures, particularly by the ECB, continued to support returns. This underpinned a strong return from corporate bonds which drove a 0.3% return from global fixed interest in April. Australian fixed interest performed in line with global counterparts this month.

Currencies

The risk on environment has seen a broad based weakness of the USD and other safe haven currencies as investor risk aversion declined. The USD fell against most major currencies following the more cautious stance of the Fed with regard to future rate rises. The AUD fell 0.7% against the USD, while the New Zealand dollar rose 1.0% given higher commodity prices and the Reserve Bank of New Zealand not cutting rates as expected. The slightly lower AUD helped unhedged returns.

Major asset class performance as at 30 April 2016 (%)

Sector	1 month	3 months	12 months	5 Years
Australian Shares	3.3	6.4	-4.7	6.2
Global Shares (hedged)	0.9	4.7	-3.5	10.6
Global Shares (unhedged)	2.4	-0.4	-0.8	14.2
Global Emerging Markets (unhedged)	1.4	5.4	-15.1	2.5
Global Small Companies (unhedged)	3.2	3.4	0.7	14.4
Global Listed Property	-1.4	6.3	5.8	11.3
Cash	0.2	0.6	2.3	3.2
Australian Fixed Income	0.3	1.1	3.4	6.6
International Fixed Income	0.3	2.3	5.2	7.6

Source: JP Morgan & ANZ Wealth

Indexes: Australian Shares - S&P / ASX300 Accumulation, Global Shares (hedged/unhedged) - MSCI World ex Australia, Global Emerging Markets - MSCI Emerging Free Net in AUD (unhedged), Global Small Companies (unhedged) - MSCI World Small Cap exAustralia, Global Listed Property - FTSE EPRA/NAREIT Developed Rental Index exAustralia (hedged), Cash - Bloomberg Bank Bill, Australian Fixed Income - Bloomberg Composite Bond All Maturities, International Fixed Income - Barclays Global Aggregate Bond Index (hedged).

Please note: Past performance is not indicative of future performance