

Read the latest market update from the Economic and Market Research team at Colonial First State Global Asset Management.

Market and economic overview

Australia

- The Reserve Bank of Australia (RBA) left the official cash rate on hold at 2% in March and again on 5 April 2016 - where it has remained since May 2015. The next RBA Board meeting is 3 May 2016.
- The RBA statement remained relatively upbeat on the domestic economy "the Board judged that there were reasonable prospects for continued growth in the economy", while maintaining a cautious easing bias. The RBA notes that "continued low inflation may provide scope for easier policy, should that be appropriate to lend support to demand."
- The statement did make reference to the recent strength in the AUD noting that it reflected both "some increase in commodity prices" and "monetary development elsewhere in the world". While they stated that the "appreciating exchange rate could complicate the adjustment under way in the economy" they avoided outright calls for a lower dollar.
- House price growth continued to slow in March, rising only 0.2% per month and 6.4% per year down from 11.1% per year in July 2015 according to CoreLogic RP Data. House price gains remained the strongest in Sydney (+7.4% per year) and Melbourne (+9.8% per year).
- The unemployment rate decreased to 5.8% in February from 6.0% in January driven by a 0.3% fall in the participation rate to 64.9%.
- Employment growth was unexpectedly weak during the month with only 300 jobs added compared to the 13,500 expected. This

benign number hid significant discrepancies between the states with Victoria the best performer adding 30,300 jobs while Western Australia was the worst losing 10,100.

- Business conditions and confidence, as measured by NAB remain constructive with Conditions up 3 to +8 while confidence was unchanged from a revised +3 in February.
- Consumer confidence, as measured by Westpac, remains volatile around its long-term average. It decreasing 2.2% in March to 99.1 after increasing 4.2% in February.

US

- The Federal Open Market Committee (FOMC) of the US Federal Reserve Board met on 15 to 16 March 2016 and as widely expected held the Fed Funds target rate unchanged at 0.25% to 0.50%, the rate set in December 2015.
- The Fed remains of the view that the economy will expand at a "moderate pace", but has also highlighted the risks coming from "global economic and financial developments."
- While the Fed continues to expect the process of monetary policy normalisation to proceed in 2016, the Fed's own 'dot' forecasts now imply only two rate hikes this year, well down from the previous expectation of four moves. Further out, the Fed has lowered their long-term Fed Funds target forecast from 3.5% to 3.25%.
- The Fed's economic forecasts have been altered a little. The unemployment rate forecast for 2016 remains at 4.7%, but has been lowered to 4.6% for 2017 and 4.5% for 2018. Economic growth is now forecast at 2.2% in 2016, down from 2.4% previously, then moderating to 2.1% in 2017 and 2.0% for 2018. Underlying inflation is expected to drift higher from 1.6% in 2016, 1.8% (down from 1.9%) in 2017 and 2.0% in 2018.

- The third estimate of Q4 2015 GDP showed growth was 1.4% on a seasonally-adjusted-annualised-rate, compared to the first estimate of 0.7%. The upgrade was due to consumer spending rising more than previously estimated. However there was also some concern caused by the 11.5% fall in corporate profits compared to Q4 2014.
- The US labour market continued to improve. A total of 215,000 jobs were added in March, above the 205,000 the market expected. The unemployment rate increased to 5.0% due to an increase in the participation rate to 63.0%. The participation rate is at the highest level in two years having increased by 0.6% in the last six months leading to a 3.1% annualised increase in the labour force over that period. Average hourly earnings increased by 0.3%, above expectations, to leave annual gains steady at 2.3% per year.
- The manufacturing sector is showing signs of improvement, with the ISM Manufacturing Index increasing 2.3 to 51.8 in March, while the Manufacturing PMI increased to 51.5 from 52.3 in February.
- Energy price weakness during February drove inflation lower, despite the falling USD, with headline CPI down 0.2% and the annual rate falling to 1% per year from 1.4% per year in January. Core inflation (ex food and energy) rose 0.3% per month taking the annual rate to 2.3%.
- The Fed's preferred measure of inflation, Core Personal Consumption Expenditure Price Index, rose 0.1% in February, leaving the annual rate at 1.7%.
- The main refinancing rate and marginal lending facility rate were lowered by 5bps to 0.00% and 0.25% respectively.
- The monthly purchases under the asset purchase programme will be increased from €60bn at present to €80bn.
- The asset purchase programme will now include investment grade bonds issued by non-bank corporations.
- A new series of four targeted longer-term refinancing operations (TLTRO II) will be launched, starting in June 2016.
- The ECB's economic forecasts were lowered slightly. Headline inflation is now expected to be just 0.1% per year at the end of 2016, 1.3% per year at the end of 2017 and 1.8% per year at the end of 2018. Annual real GDP is now forecast to increase by 1.4% in 2016, 1.7% in 2017 and 1.8% in 2018.
- ECB President Mario Draghi offered some forward guidance on rates stating that "the Governing Council expects the key ECB interest rates to remain at present or lower levels for an extended period of time, and well past the horizon of our net asset purchases."
- European manufacturing improved, with industrial production up 2.1% per month for January. Almost all sectors improved but car production was the clear standout up 5.3% per month.
- The labour market continues to expand with unemployment for February down 0.1% to 10.3%, its lowest level since September 2011.

Europe

- The European Central Bank (ECB) met on 10 March 2016 and announced further monetary policy easing across multiple fronts in response to downward revisions in inflation and inflation expectations. The easing, which exceeded the market's expectations, once again put into practice ECB President Mario Draghi's promise to "do whatever it takes".
- The ECB's monetary policy easing has taken multiple forms:
 - The rate on the deposit facility was lowered by 10bps to -0.40%.

UK

- The Bank of England (BoE) left policy unchanged when it announced its decision on 17 March 2016, as expected. The Bank Rate was unchanged at 0.5% and the stock of asset purchases remained at £375bn.
- Despite recent weakness in some data the committee concluded that there had been little change to the near term growth outlook since the last meeting. The BoE does, however, continue to view near term growth risks to the downside – owing to the weak

global backdrop, the coming EU referendum in June, and the impact that may have already had through a rise in uncertainty.

- GDP growth forecast for Q4 2015 was revised up to 0.6% per quarter (was 0.5% per quarter) and to 2.1% per year (was 1.9%). The upward revision to growth was driven by construction output and services growth, which were both stronger than initially estimated.
- CPI data showed inflation increased by 0.2% in February, with strength in recreational services and packaged holidays enough to offset continued weakness in food and energy. The annual rate of inflation remained at 0.3% per year while core inflation was stable at 1.2% per year.

NZ

- The Reserve Bank of New Zealand (RBNZ) surprised the market and cut interest rates by 25bps to 2.25% at its meeting on 10 March 2016.
- In the accompany statement the RBNZ noted the weaker global outlook and domestic inflation expectations, "Given the weaker world conditions and lower inflation expectations, the Bank judges it appropriate for monetary policy to be more stimulatory than projected in December".
- The policy outlook remains biased towards further easing with the bank noting that "Further policy easing may be required".

Canada

- The Bank of Canada (BoC) left the overnight lending rate on hold at 0.50% at its meeting on 10 March 2016. The next BoC meeting is 14 April 2016.
- The unemployment rate increased to 7.3% for February with 2,300 jobs lost over the month. Inflation rose, up 0.2% per month, however the annual rate fell to 1.4% from 2.0% in January.

Japan

- The Bank of Japan's (BoJ) policy board convened on 15 March 2016 and left interest rates and its qualitative and quantitative easing (QQE) program at an annual increase of ¥80trillion to its monetary base.

- Headline CPI increased from 0.0% per year to 0.3% per year over February while the core measure excluding food and energy increased 0.1% to 0.8% per year, both well below the BoJ's 2% target.

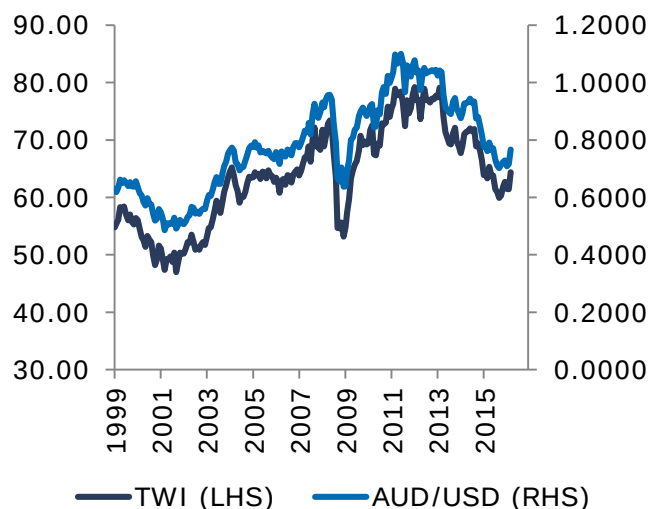
China

- The People's Bank of China (PBoC) left monetary policy unchanged during the month with no rate cuts or reserve requirement ratio easing.
- Following the National People's Congress in March, the Chinese authorities set a growth target for 2016 of 6.5% to 7.0%, down marginally from the "approximately 7%" target for 2015. The Chinese authorities stressed the focus on ensuring economic growth remained within the target in 2016 and indicated that further policy easing –both monetary and fiscal – could be implemented in the months ahead to ensure this outcome.
- USD weakness and a more gradual-fed outlook prompted the PBoC to allow the Yuan to appreciate 1.5% against the USD over March, in-line with their new currency basket approach to managing the Yuan.
- Higher frequency economic data releases point towards some improvement in manufacturing and services sectors. In early April the Manufacturing PMI rose to 50.2 from 49.0 while the Services PMI rose to 53.8 from 52.7.
- Inflation increased, rising to 2.3% per year for February, up from 1.8% per year in January. The increase was led by food costs during the week-long Lunar New Year Holiday.

Australian dollar

- The Australian dollar appreciated against the major currencies in March. The AUD finished up 7.3% against the USD to \$US0.7671. These gains occurred due to reduced expectations of the US Federal Reserve continuing to raise interest rates in 2016 as well as a recovery in commodity prices and the terms of trade.
- The Australian dollar rose against the euro (+2.5%), the sterling (+3.7%), the yen (+6.8%) and NZ dollar (+2.3%) over the month of February.

AUSTRALIAN DOLLAR STRENGTHENED IN MARCH

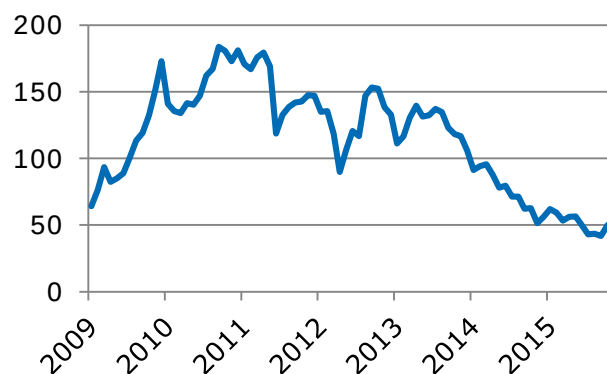


Source: Bloomberg as at 31 March 2016

Commodities

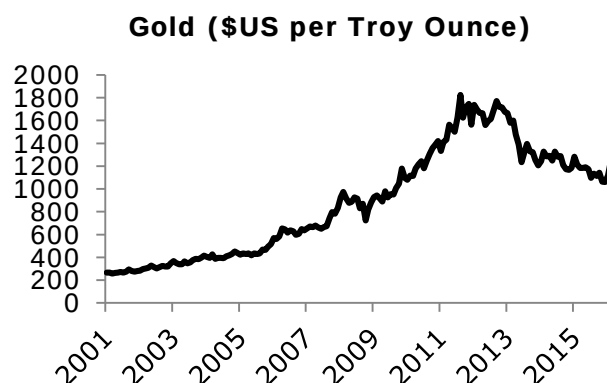
- Commodity prices were mostly stronger in February, driven by the continued fall in the USD and improving fundamentals.
- The price of West Texas Intermediate Crude finished the month at \$US38.3/bbl, up 13.6%, while the price of Brent was up 8.3% to \$US40.3/bbl. Strong demand for gasoline in the US, along with falling non-OPEC supply, supported oil over the month. While discussions around a potential production freeze agreement between OPEC and non-OPEC producers continued to feed positive market sentiment.
- Gas prices remained volatile with the US Henry Hub spot price up 20.0% to \$US1.94/MMBtu while the UK natural gas price was down 4.3% over March.
- Iron ore prices were stronger in February, up 8.3% to \$53.8/metric tonne, as measured by the benchmark price of iron ore delivered to Qingdao China – 62% Ferrous Content.
- Nickel (-0.4%), Aluminium (-3.4%) and Lead (-2.7%) fell in March, while Gold (+0.03%), Zinc (+3.0%) and Copper (+3.2%) made gains.

IRON ORE CONTINUES RECOVERY



Source: Bloomberg as at 31 March 2016

GOLD REMAINS SUPPORTED



Source: Bloomberg as at 31 March 2016

Australian equities

- Australian shares clawed back some of their lost ground from January and February, with the S&P/ASX 200 Accumulation Index adding 4.7%.
- The Index was led higher by stocks in the financials sector. Banking stocks performed well, for example, although gave back some of their earlier gains towards the end of the month. This was in response to ANZ Banking Group (+4.7%) and Westpac Banking Corporation (+5.6%) suggesting that their provisions for bad and doubtful debts would need to increase. The level of bad and doubtful debts for Australian lenders has been extremely low for years; it seems reasonable to assume that it will revert back towards historical norms at some point.

- Materials stocks also maintained their positive momentum from late February, benefiting from a further increase in the iron ore price.
- Within the sector, BHP Billiton (+8.3%) and its joint venture partner Vale reached an agreement with Brazilian authorities over compensation for the November 2015 mine disaster at Samarco.

Listed property

- ASX-listed property securities lagged the broader Australian share market in March, but the S&P/ASX 200 Property Accumulation Index nevertheless registered another month of positive returns, adding 2.4%.
- Stocks in the Office sub-sector tended to perform relatively well. Investa Office Fund (+5.5%) and Dexus Property Group (+5.4%) fared well, for example. Dexus' proposed acquisition of Investa in a cash and scrip deal attracted a significant amount of news flow in the sector.
- Retail REITs tended to perform less well. Westfield Corporation (-0.1%) and Scentre Group (1.6%) both underperformed the wider property sector.
- Returns from offshore property markets were very strong in March, with the FTSE EPRA/NAREIT Global Developed Index rising 9.6% in US dollar terms. Europe was the top-performing region. At the other end of the scale, Japan was the worst performer among the major global regions, albeit still registered gains of more than 3%.

Global emerging markets

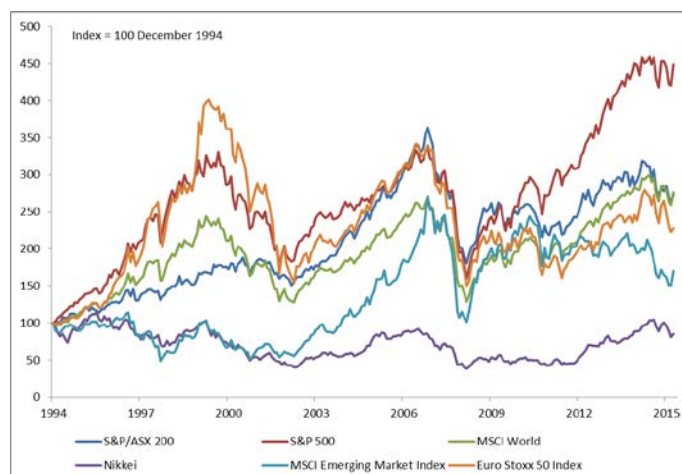
- Emerging market equities were stronger in March, with the MSCI Emerging Market Index up 13.0% in US dollars and 5.4% in AUD terms. The more gradual outlook for US rate tightening and weaker USD along with rebounding commodity prices drove markets with the Latin American region recording the largest gains. MSCI Asia Ex Japan was up 11.1%, with strength in the Shanghai Composite Index (+11.8%) and MSCI India (+9.1%) over March. MSCI EM Latin America rose 20.2% and MSCI EM Europe, Middle East and Africa was up 15.0% in US dollar terms.
- Despite the deteriorating political crisis, Brazil's Bovespa index was the best

performing of the major emerging market indices. The expanding corruption investigation has been taken as a sign of Brazil strengthening institutions while the departure of President Rousseff would be seen as a positive for the private sector.

Global developed market equities

- Global financial markets shook off the negative sentiment that had characterised the start of 2016, with all major equity markets recording gains in March.
- Rebounds in key commodity prices led resource related equities higher over the month, with Materials and Energy outperforming most sectors.
- The MSCI World Index rose by 6.5% in US dollar terms in the month of March but was 0.7% lower in Australian dollar terms.
- In the US, the S&P500 (+6.6%), the NASDAQ (+6.8%) and the Dow Jones (+7.1%) all rose in March. MSCI Healthcare (+2.2%) was the worst performer, while MSCI Materials (+9.0%) was the best performer.
- Equity markets in Europe were also stronger. The German DAX (+5.0%), Italy (+2.8%), Spain (+3.1%) and France (+0.7%) all rose. The UK FTSE 100 was up 1.3%.
- In Asia, the Japanese Nikkei 225 (+4.6%), Hong Kong Hang Seng (+8.7%), Singapore (+6.5%) and Taiwan (+4.0%) all rose.

EQUITY MARKETS RECOVER IN MARCH AFTER VOLATILE START TO THE YEAR

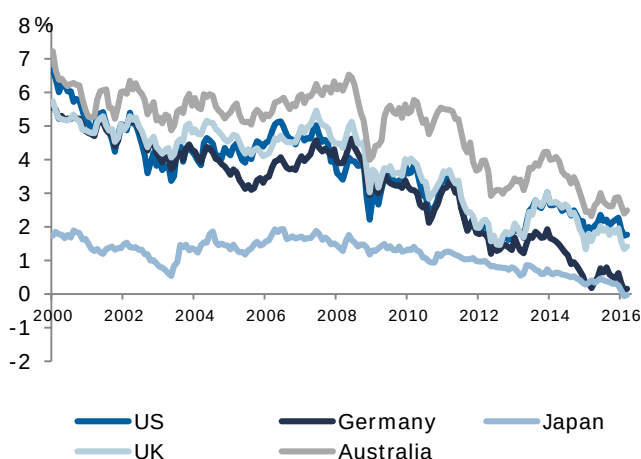


Source: Bloomberg as at 31 March 2016. Past performance is not an indication of future performance.

Global and Australian developed market fixed interest

- Fixed interest markets in March continued to be dominated by action and inaction from the major central banks. In the US, inaction and inference from the Fed had an impact on market sentiment. Action from the ECB was much more concrete as further stimulus was added and commentary consistent with the bank's commitment to its monetary policy stance. In March, 10-year government bond yields in the major markets rose between 3 and 9 basis points (bps).
- US bond yields rose after the strong payroll numbers and in the lead up to the March FOMC meeting. However, they fell again following the meeting decision and after Yellen's dovish speech. The result was only a marginal rise in 10-year Treasury bond yields of 3 bps to 1.77%.
- In line with global bond yields, the yield on the 10-year UK gilt rose marginally by 8 bps to 1.42%.
- In Japan, the 10-year Japanese government bond yield rose 3 bps in the month, but remains in negative territory at -0.04%.
- In Australia, the 10-year government bond yield followed global yields and rose 9 bps to 2.49%.

BOND YIELDS MARGINALLY HIGHER IN MARCH DESPITE CENTRAL BANK EASING



Source: Bloomberg as at 31 March 2016

Global credit

- Credit markets were most notably impacted by the ECB's decision to include corporate bonds in its Quantitative Easing program and the FOMC's dovish stance. As a result global credit spreads narrowed as the downward trend from mid last month continued.
- Overall, the Barclays Global Aggregate Corporate Index average spread was 30 bps narrower in the month, closing at 1.58%. The Barclays US Aggregate Corporate Index average spread finished the month at 1.54%, also narrowing by 30 bps and the Barclays European Aggregate Corporate Index narrowed by 25 bps to 1.31%.
- In line with investment grade markets, the US high yield credit market also saw a narrowing in spreads. The Bank of America Merrill Lynch Global High Yield index (BB-B) spread moved 65 bps tighter to 5.38%. In Asia, credit markets followed the global narrowing trend with the JPMorgan Asia Credit Index (JACI Composite) average spread in by 33 bps to 2.87%.
- Australian credit spreads narrowed marginally in the month. Australian corporate bond issuance in March was notably up from February levels with major bank issuance dominating. Most notable were the deals from ANZ and Westpac which were each over \$2bn. Investor appetite remains impacted by continued concerns over China's growth outlook, ongoing market volatility and falling commodity prices. The average spread of the Bloomberg AusBond Credit Index relative to swap fell from 124bps to 123 bps.

Index return

	Index Level in Base Currency	1 month	12 month
S&P/ ASX200 Index	5,083	4.1%	-13.7%
S&P / ASX 200 Accumulation Index	47,019	4.7%	-9.6%
MSCI World Net Index (AUD)	-	-0.8%	-4.1%
MSCI World Net Index AUD Hedged	-	5.2%	-3.3%
Dow Jones Index	17,685	7.1%	-0.5%
UK FTSE 100	6,175	1.3%	-8.8%
German DAX Index	9,966	5.0%	-16.7%
France CAC Index	4,385	0.7%	-12.9%
Japan - Nikkei	16,759	4.6%	-12.7%
Hong Kong – Hang Seng	20,777	8.7%	-16.6%
MSCI Emerging Markets Net Index (AUD)	-	5.1%	-12.6%
US 10 year bond yield	1.77%	3bps	-15bps
Australia 10 year bond yield	2.49%	9bps	17bps
UBS All Maturities Composite Bond Index	8,736	-0.2%	2.0%
90 Day Bank Bill Index	2.29%	0bps	6bps
Bloomberg AusBond Bank Bill Index	8,413	0.2%	2.2%
S&P / ASX 200 - A-REIT Accumulation Index	41,986	2.4%	11.3%
AUD/USD (end of month)	0.7657	7.2%	0.7%
Oil price	\$US38.34/barrel	13.6%	-19.5%
Gold price	\$US1232.71/ounce	-0.5%	4.1%

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Want more information?

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