

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

Market and economic overview

Summary

In Australia, the RBA left the official cash rate on hold at 2% in October and again in November. The US Federal Open Market Committee met on 27 to 28 October 2015 and decided to leave the official Fed Funds target rate at 0% to 0.25%. The European Central Bank met on 22 October 2015 and made no changes to policy. The Bank of England left policy unchanged when it announced its decision in October. The Bank of Japan's (BoJ) policy board convened on 30 October 2015 and left its qualitative and quantitative easing (QQE) program at an annual increase of ¥80trillion to its monetary base in an 8 to 1 vote.

Australia

The Reserve Bank of Australia (RBA) left the official cash rate on hold at 2% at its meeting on 6 October 2015 and again on 3 November 2015 - where it has remained since May this year.

In announcing the November policy decision the RBA delivered a balanced assessment of the influences on monetary policy - with economic growth prospects having improved, but inflation now expected to be lower than previously forecast.

This balanced outlook is captured in the RBA's final paragraph, stating that "at today's meeting the Board judged that the prospects for an improvement in economic conditions had firmed a little over recent months and that leaving the cash rate unchanged was appropriate at this meeting."

"Members also observed that the outlook for inflation may afford scope for further easing of policy, should that be appropriate to lend support to demand. The Board will continue to assess the outlook, and hence whether the current stance of

policy will most effectively foster sustainable growth and inflation consistent with the target."

The outlook for monetary policy seems, therefore, to be linked to the demand side of the economy and upcoming data releases that focus on the outlook. With underlying inflation at the bottom end of the RBA's 2% to 3% target band the low pace of inflation affords the RBA to ease monetary policy further if they think that is necessary.

The Australian Consumer Price Index (CPI) was released for the September quarter, rising a lower than expected 0.5% per quarter. This left the annual rate of inflation at 1.5% per year, below expectations and still well below the RBA's 2% to 3% target range.

The two measures of underlying inflation (the trimmed mean and weighted median) both rose by just 0.3% per quarter, taking the annual rate down to just 2.15% per year, the lowest since Q2 2012.

The unemployment rate held steady at 6.2% in September, with 5,100 jobs lost in the month. Over the past 12 months 230,000 jobs have been added and the unemployment rate peaked at 6.4% in July 2015.

Both business and consumer confidence rose in the month, post the change in Prime Minister. The NAB Business Confidence Index rose to 5, from 1, while Business Conditions was flat at 9 over the month. The Westpac Consumer Confidence Index rose 4.2% in the month but still remains below its 10-year average.

CoreLogic RP Data for October showed house prices gained 0.2% per month nationally, compared to 0.9% per month in September. This took annual gains to 10.1% per year, down from 11% per year in the prior month. Adelaide (+1.5% per month), Melbourne (+0.6% per

month), Sydney (+0.3% per month) and Brisbane (+0.2% per month) all rose. Perth fell a sharp 2.8% per month and is down 3.6% per year.

US

The US Federal Open Market Committee (FOMC) met on 27 to 28 October 2015 and decided to leave the official Fed Funds target rate at 0% to 0.25% as was widely expected.

More importantly, the Fed has signalled that a rate hike at the 15 to 16 December meeting remains a live option, stating that "in determining whether it will be appropriate to raise the target range at its next meeting, the Committee will assess progress – both realised and expected – toward its objectives of maximum employment and 2% inflation".

News in October was also dominated by negotiations over a new funding deal for the government and the debt ceiling. The final deal included the suspension of the \$US18.1 trillion debt ceiling until 15 March 2017 and government funding for two years.

The first estimate of Q3 2015 GDP was 1.5% on a seasonally-adjusted-annualised-rate, down from the 3.9% rate recorded in Q2 2015. Much of the lower rate was driven by reduced inventory levels, with companies taking advantage of business and consumer spending to unwind high inventory levels.

On the inflation side there remains limited signs of a trend up. The Fed's preferred measure, the Core Personal Consumption Expenditure Index rose 0.1% per month and 1.3% per year in September. Headline inflation fell -0.2% per month to be flat for the year and ex food and energy and rose to 1.9% per year from 1.8% per year where it has been for the last six months.

Wages growth also remains anaemic, with the quarterly Employment Cost Index rising 0.6% per quarter and 2% per year despite the unemployment rate at 5.1%, close to most measures of full employment.

Europe

The European Central Bank (ECB) met on 22 October 2015 and made no changes to policy. The main refinancing rate remained at 0.05% and a target of €60bn of securities are to be purchased each month.

The ECB noted that "while euro area domestic demand remains resilient, concerns over growth

prospects in emerging markets and possible repercussions for the economy from developments in financial and commodity markets continue to signal downside risks to the outlook for growth and inflation."

The ECB are particularly concerned about factors that could delay the return of inflation to 2%.

As a result of this, the ECB President Mario Draghi noted "the degree of monetary policy accommodation will need to be re-examined at our December monetary policy meeting".

Inflation remains low, with the CPI estimate for October at 0.0% per year, with core inflation at 1.0% per year. The Eurozone unemployment rate fell to 10.8% for September, down from 10.9% and the lowest since January 2012.

UK

The Bank of England (BoE) left policy unchanged when it announced its decision on 8 October 2015, as expected. The Bank Rate was unchanged at 0.5% and the stock of asset purchases remained at £375bn. There was one dissent on the nine member board, the third meeting in a row. Ian McCafferty preferred to increase the Bank Rate by 25 basis points based on a view that building domestic cost pressures were likely to outweigh the dampening influence of the appreciation of sterling, causing inflation to overshoot the 2% target in the medium term.

The advance estimate of Q3 2015 GDP data was released with growth of 0.5% per quarter and 2.3% per year, down from 2.4% per year in Q2 2015. This was slightly below expectations and was driven by a 2.2% fall in construction spending and a 0.3% contraction in manufacturing production. Overall the UK economy has expanded 6.4% above its pre-recession peak.

Japan

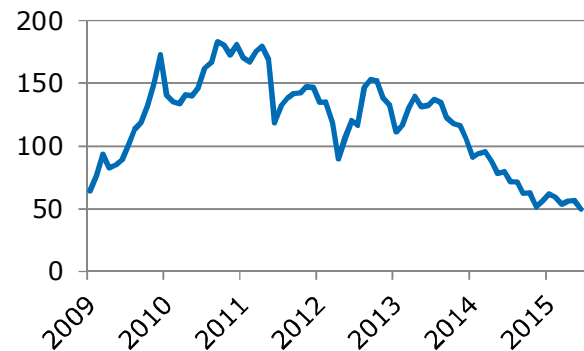
The Bank of Japan's (BoJ) policy board convened on 30 October 2015 and left its qualitative and quantitative easing (QQE) program at an annual increase of ¥80trillion to its monetary base in an 8 to 1 vote, contrary to some expectations.

The BoJ revised down its current inflation forecasts and real growth rate into FY2016 in the semi-annual outlook report released after the meeting. The BoJ now expects inflation to be 1.4% for FY2016 (down 0.5 %pts) with inflation not hitting the target of 2% to around Q4 2016 or Q1 2017.

Australian dollar

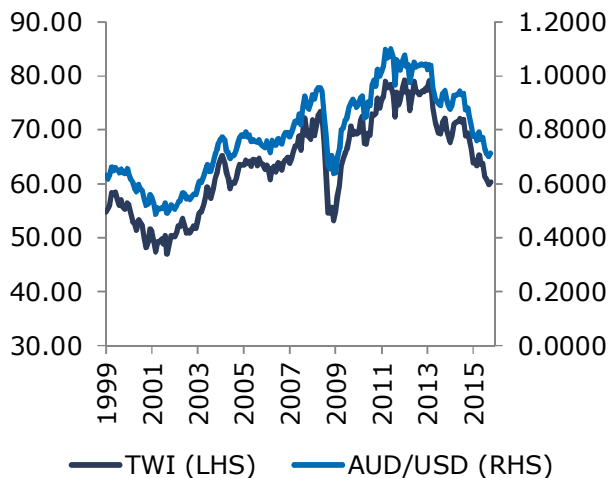
The Australian dollar was mixed against the major cross currencies over the month. The AUD finished up 1.7% against the USD in October to \$US0.7139. The Australian dollar traded as low as \$US0.6979 and as high as \$US0.7382 during the month, largely reflective of changes in views of the first rate hike for the US Federal Reserve and potential for RBA easing in Australia.

The Australian dollar also moved higher against the euro, up 3.3% as prospects for further ECB easing appeared more certain, and against the Japanese yen (+2.4%). The Australian dollar fell 0.3% against the sterling and 3.7% against the NZ dollar.



Source: Bloomberg as at 31 October 2015

AUSTRALIAN DOLLAR HIGH IN OCTOBER



Source: Bloomberg as at 31 October 2015

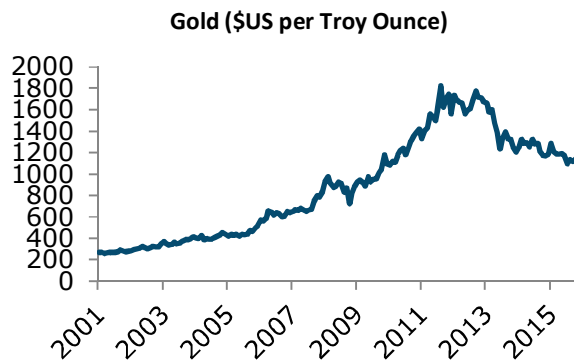
Commodities

There was less focus on commodity prices during the month of October, albeit price moves remained divergent between commodities and sectors. Further easing measures in China and prospects of easing in Europe did help support the sector and the global growth outlook.

The oil price traded in a wide range, with the price of West Texas Intermediate Crude finishing the month up 3.3% to \$US46.59. The iron ore price, as measured by the benchmark price of iron ore delivered to Qingdao China – 62% Ferrous Content drifted lower over the course of the month, finishing down 11.5% to \$US49.83 a metric tonne on supply concerns.

IRON ORE GONE DOWN SHARPLY

GOLD UP SLIGHTLY



Source: Bloomberg as at 31 October 2015

Australian equities

Australian equities rose alongside their global peers in October, with the S&P/ASX 200 Accumulation Index adding 4.4%.

Concerns surrounding the pace of economic growth in China receded, which appeared to support investor sentiment. A generally favourable corporate reporting season in the US was also supportive.

With the exception of the Telecoms sector – which declined due to negative share price performance from sector heavyweight Telstra Corporation (-3.7%) – all areas of the market registered gains.

Energy stocks performed particularly well, following the announcement of a takeover approach for Santos (+46.7%). This approach was rejected and follows September's bid for Oil Search (+9.5%). More attractive valuations in the sector following months of weakness appear to have increased the appeal of companies in the sector.

In other news, Westpac Banking Corporation (+6.2%) followed the other three 'big four' banks by raising additional equity. Westpac raised \$A3.5 billion, helping to improve its capital position. Elsewhere in the financials sector, both ANZ Banking Group (+0.5%) and National Australia Bank (+0.6%) released their earnings for the 2015 financial year. Neither release held any major surprises for investors.

Listed property

ASX-listed property stocks performed well in October, with the S&P/ASX 200 Property Accumulation Index rising 5.0%.

The Office sub-sector performed particularly well, driven by Dexus Property Group (+8.3%).

Despite this recent outperformance, office stocks have lagged the broader sector over the past year.

The Retail sector also remained buoyant, adding a further 4.8%. In company news, it was announced that Scentre Group (+6.2%) Chairman Frank Lowy will retire in 2016.

Residential stocks regained losses during the month, with notable positive performance from Stockland Group (+5.2%) and Mirvac Group (+4.9%).

Global property securities also enjoyed strong performance in October, generating their largest monthly gain in more than a year. The FTSE EPRA/NAREIT Global Developed Index added 5.7% in USD terms. The uncertain global economic backdrop prompted hopes that the US Federal Reserve will delay increasing interest rates, which supported 'yield investments' such as property securities. Sentiment towards global property securities was also assisted by generally favourable quarterly earnings releases from companies in Europe and the US.

Singapore, with a gain of more than 10%, was the best performing region, followed by Continental Europe (+7.0%).

Global developed market equities

After two months of heavy losses and volatile moves, global developed equity markets recorded strong gains in October.

Expectations of a delay in US Federal Reserve rate hikes and a more gradual rate hike cycle when they do commence assisted the gains, as further stimulus in China and prospects of further monetary easing in Europe also helped improve investor sentiment and the global growth outlook.

The International Monetary Fund (IMF) downgraded its forecasts for global growth in October. Growth of 3.1% is expected in 2015, down from 3.3%. In 2016 growth of 3.6% is forecast, down from 3.8%. Weakness in emerging economies was the main cause of the downgrades.

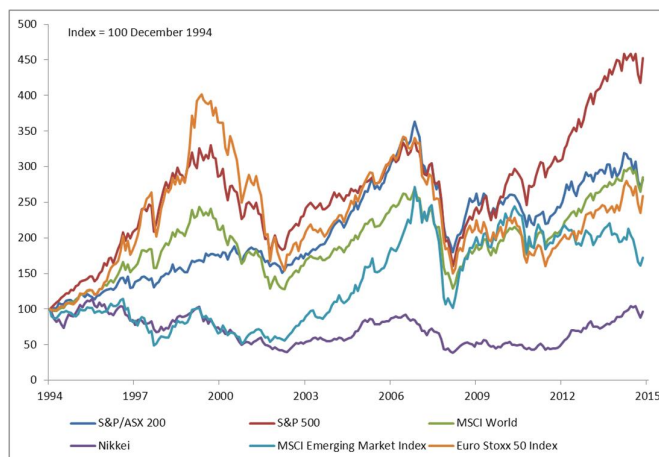
All major global equity markets rose in October. Overall the MSCI World Index rose 7.8% in USD terms and 5.9% in AUD terms.

In the US, the S&P500 (+8.3%) recorded five weekly gains in a row, and recorded its best

monthly gain since October 2011. The Dow Jones (+8.5%) and the NASDAQ (+9.4%) also rose.

Equity markets in Europe were also stronger. The German DAX (+12.3%), France (+9.9%), Spain (+8.4%) and Italy (+5.4%) all rose. The UK FTSE 100 was up 4.9%. In Asia, the Japanese Nikkei 225 rose 9.7%, the best monthly gain since April 2013, while Hong Kong rose 8.6% its first positive gain in six months.

EQUITY MARKETS MIXED



Source: Bloomberg as at 31 October 2015. Past performance is not an indication of future performance.

Global emerging markets

Emerging market equities also rose in October on improved global sentiment and some expectations of a delay in US interest rate hikes. The MSCI Emerging Market Index rose 7.0% in US dollars and 5.2% in AUD terms. All regions recorded positive gains over the month and the index recorded its first positive gain since April 2015.

Further easing in monetary policy in China helped, with the Shanghai Composite Index rising 10.8% in the month. Elsewhere the Argentina Burcap rose a sharp 30.6% following recent sharp falls.

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Want more information?

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