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AUSTRALIA DELIVERS GOOD COMPANY EARNINGS

The eagerly anticipated Australian corporate earnings season for the first half of the 2014-2015 financial year unfolded during February. Coming into the season, market analysts were expecting earnings results for industrial companies to be realised, with declines in resources sector earnings offset by better growth among industrial companies. Overall, more companies have reported earnings growth in line with estimates and a lower proportion have disappointed the market.

In summary:

> 55% exceeded earnings expectations (versus a norm of 43%);

> 66% have seen their profits rise from a year ago (in line with recent trends); and

> 62% have increased dividends from a year ago (also in line with recent trends)

"A key feature of this results season was significant increases in dividends."

The better performers during the season were beneficiaries of the continuing low interest rate environment such as banks, property and infrastructure companies, along with companies that generate significant revenues from offshore businesses. Efficiency gains from cost reductions also continued to be a common theme.

AMP CAPITAL
Australian Equities Team

A key feature of this results season was significant increases in dividends, with many companies choosing to reward shareholders with additional returns of cash rather than reinvesting in their businesses. While this is good for shareholders, it does raise the question of management confidence in pursuing future growth opportunities.

Looking ahead to the full year results, companies that benefit from a weaker Australian dollar and exposure to strong growth opportunities outside of Australia should continue to do well, as will companies that can continue to deliver sustainable growth in dividends.

INTEREST RATES MOVEMENTS AND GLOBAL INFRASTRUCTURE

As the US Federal Reserve (the Fed) prepares financial markets for incremental interest rate rises, we take a look at what this might mean for global listed infrastructure assets.

"Core and pure infrastructure assets will outperform global equities."

How do interest rate expectations affect infrastructure?

In a steepening interest rate curve environment (where future interest rates are expected to increase more when compared to shorter term rates) long-term assets with fixed income components, such as infrastructure, tend to underperform against both short term fixed income instruments and equities. Higher expected future interest rates can be indicative of an improving economy where equities are expected to outperform bonds and bond proxies. As such, investors are more likely to sell their bond-like assets and invest in equity-like investments in order to benefit from the economic upswing.

In a flattening interest rate curve environment (where future interest rates are expected to be more closely aligned with short-term rates) bond, proxy infrastructure assets tend to outperform equities, in general. This can be for many reasons but includes, at least partly, the reverse of the above scenario.

What does this mean for investors?

We believe that as the Fed starts to steadily increase rates, creating a shift from a rising to a more flattened interest rate curve environment, core and pure infrastructure assets will outperform global equities.

TIM HUMPHREYS
Head of Global Listed Infrastructure

However, the potential of an individual company to outperform will depend on the specific sector that a company operates in, as well as the fundamentals of the company.

Final thoughts

There is the opportunity for an actively managed and well-positioned infrastructure portfolio to take advantage of both current and future interest rate environments and transition to a different mix of optimal assets as the Fed starts to progressively raise interest rates.

BIRD'S-EYE VIEW: AIRPORT INFRASTRUCTURE

The aviation industry can be a tough gig. High cost of capital, high rates of depreciation, fierce competition, thin profit margins and low return on incremental capital are just some of the challenges facing the industry. In this article, we weigh up the advantages and potential risks of investing in the aviation sector.

Aviation is broader than airlines

The aviation sector extends beyond pure airlines, as we traditionally think of them. Frequent-flyer programs, aircraft manufacturing and infrastructure are all examples of related sectors which are often quite profitable and are not so beholden to external factors such as oil prices, which can heavily influence airline profitability.

> "The aviation sector extends beyond pure airlines."

In fact, aviation-related infrastructure – such as airports, runways, terminals, hangars (a closed business structure to hold aircrafts in protective storage), and ground transport systems can present a compelling opportunity for investors. Generally speaking, aviation-related infrastructure has similarities to other forms of civilian infrastructure in that it can provide an ongoing cash stream that gradually rises with inflation. Other advantages of infrastructure as it relates to the aviation industry include monopolistic-like characteristics; high barriers to entry; ancillary income streams and shelter against a nation's economic cycle

MAR BELTRAN
Investment Director - Airports

What are the considerations?

Like all potential infrastructure investments, any prospective investor considering the aviation sector, should carefully assess risks. Competition from other hubs may be an important factor and investors should also consider competition from other travel destinations, which is particularly relevant for airports where traffic is majority inbound tourism.

Positive financial indicators of a 'good' airport investment should include a favourable regulatory framework that doesn't cap returns, high operating margins, strong aeronautical asset base with spare capacity, moderate level of gearing and an ability to expand.

ECONOMIC UPDATE: WHAT DOES IT MEAN FOR MARKETS?

Below we provide an an update on key economic development in Australia and globally. We also assess what this means for markets.

Australian developments

The non-mining economy is yet to completely fill the growth gap left by the passing of the mining investment boom. While housing construction is buoyant and retail sales growth has improved, the economy faces headwinds in the form of lower commodity prices, tight fiscal policy, and a still relatively high Australian dollar. As such growth may remain just below potential in the year ahead. Inflation is likely to remain subdued; therefore the Reserve Bank of Australia (RBA) will likely cut interest rates further.

Global developments

Global growth is likely to be okay in 2015, but it is likely to remain uneven. The US economy should continue to see relatively robust growth, Europe will likely record mild but positive growth, while China will likely see growth around 6.5 to 7%. Inflation is likely to remain low. Global monetary policy remains stimulatory, but 2015 will likely see increasing divergence in monetary policy settings. That is, the US will start to gradually raise rates from around mid-2015, as Europe, China, and Japan continuing to ease monetary policy.

What does this mean for investment markets?

Notwithstanding the risk of a correction after recent strong gains, the broad trend in shares is likely to remain up as: valuations, particularly against bonds, are good; economic growth is continuing; and monetary policy is set to remain easy with further easing in Europe, Japan, China and Australia and only a gradual tightening in the US. As such, share markets are likely to see another year of reasonable returns.

DR SHANE OLIVER
Head of Strategy and Economics and Chief Economist

> "Growth may remain just below potential in the year ahead."

Low bond yields point to soft medium term returns from sovereign bonds, but it's hard to get too bearish on bonds in a world of too much saving, spare capacity and deflation risk.

Economic indicators

Gross domestic product (annual rate %)*	Latest	Current	Previous	1 year ago
World (IMF/OECD)	31/12/2013	2.90	3.10	3.10
Australia	31/12/2014	2.50	2.70	2.20
China	31/12/2014	7.30	7.30	7.60
European Union	31/12/2014	0.90	0.80	0.40
United States	31/12/2014	2.40	2.70	3.10
Inflation (annual rate %)*	**Latest**	**Current**	**Previous**	**1 year ago**
Australia	31/12/2014	1.70	2.30	2.70
China	31/01/2015	0.80	1.60	2.50
European Union	28/02/2015	-0.30	0.40	0.70
United States	31/01/2015	-0.10	1.70	1.60
Official cash rates (%)*	**Latest**	**Current**	**Previous**	**1 year ago**
Australia	28/02/2015	2.25	2.50	2.50
China	28/02/2015	3.32	2.61	1.85
European Union	28/02/2015	0.05	0.05	0.25
United States	28/02/2015	0.25	0.25	0.25
Bond yields (%)	**Latest**	**Current**	**Previous**	**1 year ago**
Australia 3Y	28/02/2015	1.79	2.39	2.83
Australia 10Y	28/02/2015	2.46	3.03	4.02
United States 2Y	28/02/2015	0.62	0.47	0.32
United States 10Y	28/02/2015	1.99	2.16	2.65

Exchange rates

Official exchange rate (%)**	Latest	Current	Previous	1 year ago
Australian Dollar / Chinese Renmimbi	28/02/2015	4.9075	5.2448	5.4992
Australian Dollar / Euro	28/02/2015	0.6979	0.6846	0.6479
Australian Dollar / Great Brish Pound	28/02/2015	0.5065	0.5450	0.5340
Australian Dollar / Japanese Yen	28/02/2015	93.5738	101.2976	91.3424
Australian Dollar / United States Dollar	28/02/2015	0.7828	0.8535	0.8949

Share market analysis

Sharemarkets (in local currency)	5yrs (%pa)	3yrs (%pa)	1yr (%)	3 months (%)	1 month (%)
Australia: S&P/ASX300 Accumulation	9.5%	15.8%	14.2%	12.6%	6.9%
Germany: DAX Accumulation	15.3%	18.5%	17.6%	14.2%	6.6%
Global emerging markets: MSCI Accumulation (AUD)	6.5%	11.0%	20.1%	7.9%	2.6%
United Kingdom: FTSE 100 Accumulation	9.1%	9.6%	5.6%	3.9%	3.3%
United States: S&P 500 Accumulation	16.2%	18.0%	15.5%	2.3%	5.7%

* Data is most current available

** Rates are expressed as 1 Australian Dollar (IMF/OECD) purchasing power-parady