

Market commentary

Provided by Advance Investment Solutions –
January quarter 2010

Historically low interest rates combined with large central bank liquidity programmes and fiscal stimuli have continued to support improvement in global sentiment. Although the outlook is generally positive, inflation will be a key issue globally in 2010.

Economic overview – January 2010 quarter

The pace of improvement has varied amongst the key economies. China's GDP increased at a rate of 8.9% over the year to September 2009. The US economy grew for the first time since June 2008. Positive growth was also recorded in Europe (0.4%), Australia (0.2%), and Japan (0.3%). The UK has lagged with its economy contracting by 0.2%. Inflation is likely to be an issue particularly in the emerging world and especially in China and India. Inflation is also likely to drift higher in the developed world.

Outlook by asset class

Australian shares

We continue to hold a positive view of Australian equities and anticipate the market to return around 19% over 2010. However, the market is still likely to be volatile, with the current rally expected to falter around April/May once the headwinds to global economic growth are more pronounced. A forward-looking market will, in most cases, react well in advance by discounting the slower global (and in particular, emerging) economic and subdued earnings growth outlook and become more defensive. Once that phase is over, the market is likely to rally into year-end.

International shares

We expect international equity markets to return around 15% to 19% over 2010.

However, we believe the markets will experience pronounced bouts of weakness and strength, which is typical after a strong post-recession rally.

Diversified property

We anticipate returns of around 9% from the domestic listed property market and around 16% returns from the global listed property market in 2010. We suspect the full impact of anticipated price declines that are yet to be priced into the unlisted market will eventually impact the listed property market in Australia, although this is not a major issue in other markets. We believe listed property will be a good investment later this year or early next year.

International bonds

We anticipate global sovereign bond yields moving higher during the early part of 2010 due to significant supply/demand imbalances as global monetary authorities roll back their quantitative easing and investor preference for growth assets increases. We anticipate returns for hedged global bonds for 2010 will be around 8.5%.

Australian bonds

We anticipate Australian bonds returning around 4% over 2010 with an estimated year-end Australian 10-year bond yield at around 5.80%, 5-year at around 5.25% and 3-year at around 5.00%. We expect government bond yields to move higher for the same reasons as international bonds.

Alternative assets

We anticipate returns of around 15% to 20% through nimble tactical and active strategy implementations. Given our anticipated profile of market movements where risky assets do well at the start of the year, retreat around mid-year and then rally into year-end, investors should consider using both directional and relative value strategies throughout the year.

Commodities

We believe that the broad structural/macro positive outlook for commodities is still valid. We anticipate commodities returning around 14% during 2010. Commodity prices are expected to move higher in the first half of 2010, led by a sharp rise in base and precious metal prices. Many 'alpha' generating opportunities are likely during 2010. As for most asset classes, a tactical, active and nimble approach should be considered when investing in commodities during 2010.

Currencies

We expect the Australian dollar to move into the 0.98 to 0.99 ranges during early part of this year and then move lower towards the 0.77 to 0.82 range during US dollar strength, ending the year around the 0.88 level. Significant investor risk-aversion will have a material negative impact on the prospects for the Australian dollar because of the high levels of speculative activity associated with it.