

Market commentary

Provided by Advance Investment Solutions

— March quarter 2010

The global economic recovery continued in the last quarter led largely by strong growth in the Asian emerging economies. However, sovereign debt concerns and policy adjustments sparked an increase in asset market volatility. The short-term economic outlook is positive, but investment market returns will reflect heightened uncertainty.

Economic overview — March 2010 quarter

Global growth continues to be driven by a pick-up in world trade and industrial production, reflecting the positive effect of global stimulus measures.

The Asian emerging world continued to power along, led by a 10.7% year-on-year expansion in China. Growth expanded in most of the major advanced economies, but continues to lag in the emerging world.

Strong growth in the emerging Asian economies has reduced the level of unused capital, pushing some asset prices up sharply and raising inflation concerns (China's inflation is running at its fastest pace in almost 15 months). In contrast, underlying inflationary pressures are still largely absent in most major advanced economies due to very high levels of economic resources and high unemployment. In Australia, underlying inflation has continued to trend down.

In response to inflation concerns, China has increased its banks' reserve requirement ratio and tightened rules on personal and business loans. India raised official interest rates by 0.25% in March and Australia's official interest rates rose by a further 0.25% in the quarter up to 4.0%. Whilst there were no changes to official interest rates in other advanced economies, the level of extraordinary policy measures have been reduced.

Outlook by asset class

Australian shares

We expect Australian equities to deliver a total return of around 18% (including grossed up dividend) over the next 12

months. Equity portfolios should be biased towards cyclical and growth stocks during this stage of the market cycle, as a better equity earnings outlook will be the primary driver of the market.

International shares

Our analysis of the broad economic backdrop (including capital flows, market sentiment, equity earnings yield relative to bonds and markets' risk appetite) point to further global equity market gains in the short term. We expect around 12% gains for unhedged global equities with country, sector and stock rotation important at this stage of the economic cycle.

Diversified property

We expect this sector will generate around 12% returns over the next 12 months. The risk of anaemic growth in the Real Estate Investment Trust (REIT) sector could continue, but we expect better returns in the global listed property market due to the diversification across regional, country, sector and stock-specific opportunities.

International bonds

The estimated total return on fully hedged currency international bonds is around 8% over the next 12 months. This is relatively better than domestic bond and cash returns. However, we expect short-term under-performance due to bond yields rising.

Australian bonds

Our outlook for domestic bonds is negative in the short term. We expect bond yields to rise, taking the 10-year bond yield towards 6.5%, and then

declining towards 6.0% during anticipated equity market weakness. The Australian credit market, although attractive, lacks sufficient liquidity to offer efficient diversification. The value-add through active portfolio management is limited when compared with international fixed income markets. We expect the Australian sovereign yield curve to flatten over time as official interest rates continue to rise. We expect Australian bonds to return around 4.0% over the next 12 months.

Alternative assets

We anticipate returns of around 17% from this sector through nimble and active strategy implementations. A good blend of both directional and relative value strategies need to be used throughout the year. Long/short equities, long/short credit, convertible arbitrage and other relative-value strategies should all fare well during periods of moderate financial market volatility.

Commodities

We anticipate returns for this asset class of around 16% with supply/demand imbalances and geopolitical uncertainty combining to keep key commodity prices elevated for some time.

Currencies

We expect the Australian dollar to trade higher in the short term, perhaps towards the 0.97 to 0.98 range and then decline against a strong US dollar that takes the currency towards the 0.88 level. We also expect the Australian dollar will be stronger against the Japanese Yen, British Pound and the Euro.



Disclaimer

This publication has been compiled by Securitor Financial Group Ltd ABN 48 009 189 495 Australian Financial Services Licence Number 240687 (Securitor) and is current as at time of preparation (April 2010).

Past performance is not a reliable indicator of future performance.

Whilst every effort has been taken to ensure that the assumptions on which the outlooks given in this publication are based are reasonable, the outlooks may be based on incorrect assumptions or may not take into account known or unknown risks and uncertainties.

Material contained in this publication is an overview or summary only and it should not be considered a comprehensive statement on any matter nor relied upon as such.

The information and any advice in this publication do not take into account your personal objectives, financial situation or needs and so you should consider its appropriateness having regard to these factors before acting on it. While the information contained in this publication is based on information obtained from sources believed to be reliable, it has not been independently verified. To the maximum extent permitted by law: (a) no guarantee, representation or warranty is given that any information or advice in this publication is complete, accurate, up-to-date or fit for any purpose; and (b) neither Securitor, nor any member of the Westpac group of companies, is in any way liable to you (including for negligence) in respect of any reliance upon such information or advice. It is important that your personal circumstances are taken into account before making any financial decision and we recommend you seek detailed and specific advice from a suitably qualified adviser before acting on any information or advice in this publication. As the rules associated with the super and pension regimes are complex and subject to change and as the opportunities and effects differ based on your personal circumstances, you should seek personalised advice from a financial adviser before making any financial decision in relation to super, pensions or other matters discussed in this publication. Any taxation position described in this publication is general and should only be used as a guide. You should consult a registered tax agent for specific tax advice on your circumstances.

Disclosure

Securitor is a wholly owned subsidiary of Asgard Wealth Solutions Ltd ABN 28 009 143 597 (Asgard). Asgard and Advance Asset Management Limited ABN 98 002 538 329 are wholly owned subsidiaries of Westpac Banking Corporation ABN 33 007 457 141. BT Financial Group is the wealth management arm of the Westpac group of companies.

More information?

For further information on any issue here, or any financial matter, please contact your financial adviser.