

## September Quarter 2018 Review

# NEWSLETTER

Phone: 1300 763 544 | Email: [info@fmfinancial.com.au](mailto:info@fmfinancial.com.au) | Web: [www.fmfinancial.com.au](http://www.fmfinancial.com.au)



### Equities continue to advance

Despite rising bond yields and worsening trade relations between the United States and China, share markets have continued to move higher. In summary, the September quarter produced the following:

- Strong returns from global equities, with more modest results from the local market.
- Continued nervousness in emerging markets, with a significant sell-off in China.
- U.S. bond yields maintain an upward trajectory.
- Returns for Australian investors with unhedged exposures boosted by a fall in the \$A.

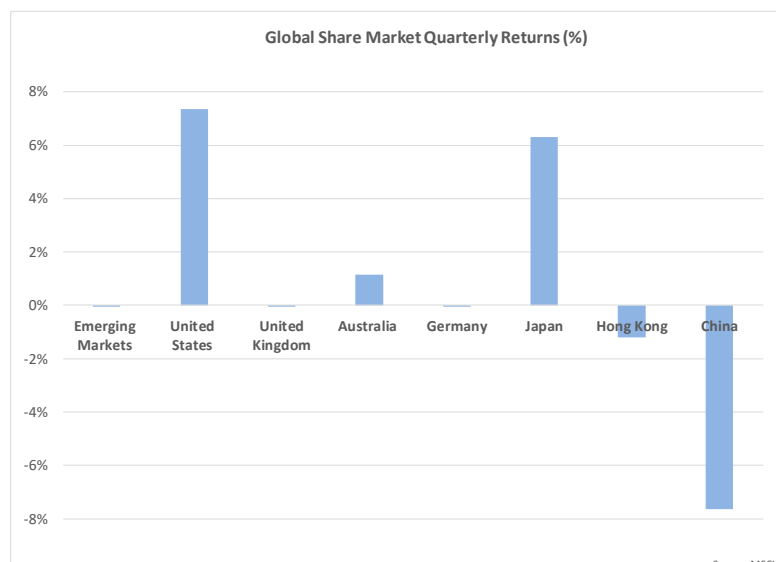
Asset Class Return	Sep Qtr	Annual
Australian Equities	1.5%	14.0%
Global Equities - Unhedged	7.4%	20.8%
Global Equities - Hedged	5.6%	12.9%
Australian Listed Property	2.0%	13.2%
Global Listed Property	0.4%	5.0%
Global Listed Infrastructure	-1.3%	-0.1%
Australian Fixed Interest	0.5%	3.7%
Global Fixed Interest	-0.1%	0.9%
Cash	0.5%	1.9%

Further escalation in the size and breadth of tariffs being implemented on items traded between the U.S. and China once again failed to materially dent equity market sentiment last quarter. Share markets maintained upward momentum, with the United States continuing to attract solid support. Notwithstanding a July sell-off in the Information Technology sector, which saw the price of Facebook fall by 19% in one day, the U.S. equity market hit new record

highs during the quarter with an increase of 7.4%. The successful negotiation of a new trade agreement between the U.S., Canada and Mexico may have helped neutralise the impact on investor confidence from the ongoing deterioration in the U.S. – China trade relationship.

European markets were generally flat over the quarter, with small negative returns recorded in the U.K. and Germany, although France was 3.4% higher. The Japanese market attracted strong support late in the quarter, with a gain of 6.3%. Investor confidence in Japan was boosted by some encouraging economic data, as well as a decline in the value of the Yen, which improves the competitiveness of Japanese exporters. Japan's Nikkei 225 Index reached its highest level since November 1991 during the quarter.

A strong \$US drew money away from some emerging markets, which experienced a marginal decline in share market value. China led the emerging markets lower, with



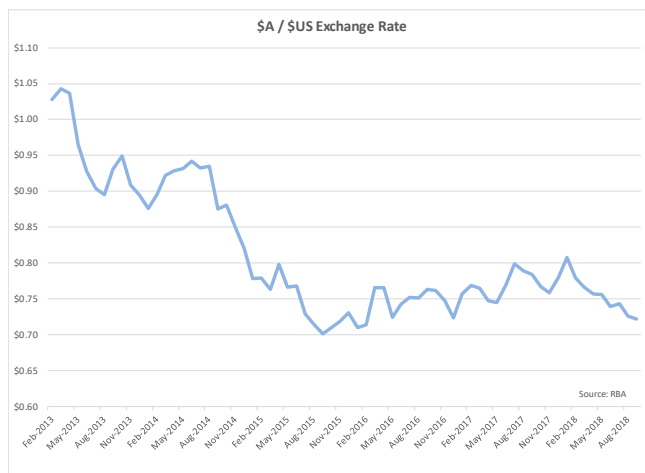
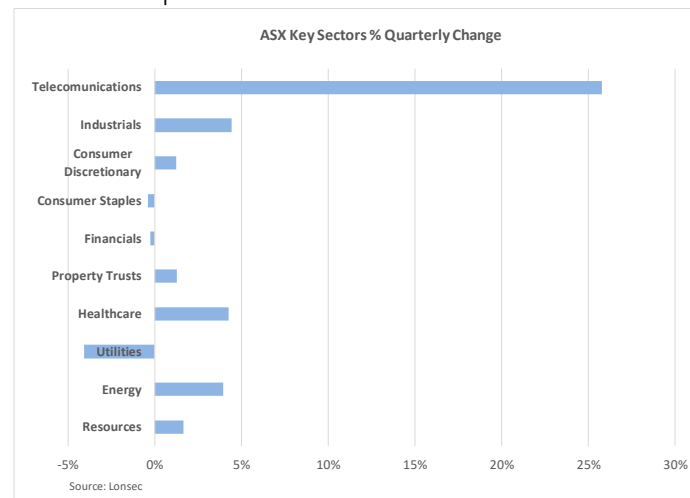
FM Financial is a Hillross financial planning practice. Hillross is one of Australia's most respected networks, a Principal member of the Financial Planning Association of Australia, and ensures FM has the most up to date advice, technical knowledge, and systems and that FM complies with all ASIC regulations.

*Helping you make the right financial decisions for both now & the future*



a 7.6% decline. With the Chinese market now down 9.0% since the start of January, the share market appears to be of the view that China will be more disaffected by rising tariffs than the U.S. Outside of China, there were some positive results from emerging markets with the South American region bouncing back strongly from weakness earlier in the year. Rising energy prices, and a 4-year high for the global oil price, buoyed the Russian market over the quarter, which finished 10.2% higher. The Australian share market also continued to rally over the September quarter, with the S&P ASX 200 Index posting a 1.5% gain to be 14.0% ahead for the past year. The political turmoil, which resulted in Scott Morrison becoming Prime Minister, appeared to have no material impact on the market. The telecommunications sector found some support following a prolonged period of weakness, with the sector gaining 26%. The catalyst for the rise in the telecommunications sector was the announcement of a planned merger between Vodafone and TPG. A combining of two competitors in the mobile phone industry was viewed as being positive for the sector overall, as it may lessen the severity of price competition. Telstra (up 23%) was a beneficiary of this announcement, and its own earnings results, which contained no surprises for the market.

Outside of telecommunications, the performance on the local market was far more subdued. Utilities declined in value, which was consistent with the global decline in infrastructure stocks last quarter as higher bond yields made infrastructure yields less attractive on a relative basis. The banking sector also continued to underperform the broader market. Ongoing concerns over weak credit growth and increased funding costs weighed on the sector; with the higher funding costs ultimately triggering a round of small mortgage rate increases. Offsetting the weakness in banking stocks was a rise in resource and energy stocks, with higher energy prices and a fall in the \$A supporting these sectors. The lower \$A also added support for Healthcare, which finished in positive territory despite the strong gains in CSL Limited being largely reversed in the final month of the quarter.



The Australian dollar finished September at its lowest month end level since February 2016. Against the \$US, the \$A declined U.S. 1.7 cents to U.S. 72.2 cents. The Australian dollar was also materially lower against the Euro and British Pound over the quarter; but was slightly stronger against the Japanese Yen and Chinese Yuan. Continued softness in local wages growth and inflation data may have contributed to the weakness in the \$A, with the lack of inflationary pressure pushing out expectations of any change in monetary policy. With little prospect of a change in the cash interest

rate in the near term, there is less incentive for overseas investors to hold \$As – particularly when



U.S. cash interest rates are on the rise. As widely expected, the U.S. Federal Reserve (the U.S. central bank) lifted the Federal Funds interest rate by 0.25% to now be between 2.0% and 2.25%. U.S. longer term yields also moved higher over the quarter, with the 10-year Government bond yield rising 0.20% to 3.05%. The equivalent Australian yield was far steadier, rising just 0.04% to 2.67%.

#### Outlook and Portfolio Positioning

As share markets have continued to rally, increased caution is warranted around equity positions, with valuations approaching the upper range of fair value. Political risks may become an increasing focus of markets in the coming months, with the U.S. mid-terms and potential change of government in Australia. Uncertainty over how the local economy will cope with the housing downturn, and how key Northern Hemisphere economies will cope with the withdrawal of monetary stimulus in the year ahead, may also weigh on market sentiment.

Notwithstanding the above reasons to be cautious with equity allocations, the absolute low level of interest rates, and the fact that company profitability remains strong, suggests that the most likely source of wealth accumulation over the medium terms remains equities. As such, reasonable allocations to the asset class are being maintained in our portfolios.

The predominantly unhedged currency exposure within our portfolios has added value over recent months. Although the \$A has fallen, our portfolios maintain a bias to unhedged exposures as the lack of any prospect of local interest rate rises, and a softer local economy more generally, may be a source of ongoing weakness for the \$A.

#### Important Information

*The following indexes are used to report asset class performance and calculate the benchmark returns for this model portfolio: ASX S&P 200 Index, MSCI World Index ex Australia net AUD TR (composite of 50% hedged and 50% unhedged), FTSE EPRA/NAREIT Developed REITs Index Net TRI AUD Hedged, Bloomberg AusBond Composite 0 Yr Index, Barclays Global Aggregate (\$A Hedged), Bloomberg AusBond Bank Bill Index, S&P ASX 300 A-REIT (Sector) TR Index AUD, S&P Global Infrastructure NR Index (AUD Hedged).*

*FM Financial ABN 80 074 824 749 is an Authorised Representative of Hillross Financial Services Limited, ABN 77 003 323 055, AFSL 232705. The information in this article is not advice and is for general use only as it has not taken into account your objectives, financial situation or needs. If you have any questions on the article please contact your financial planner before taking any action.*

