Monthly

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Economic & Market Commentary

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Conrad Burge
Investment Manager

For more information contact:
Your Fiducian Financial Planner

The global economy slowed last year, with the International Monetary Fund (IMF) reducing its estimate of global growth for 2015 to 3.1%, while noting that 'global economic activity remained subdued' (World Economic Outlook update, 19 January).

The IMF has also reduced its growth forecasts for this year (to 3.4%) and for 2016 (to 3.6%), with recovery expected to be a little less robust than previously forecast.

The IMF has also added the caveat to its forecasts that 'risks to the global outlook remain tilted to the downside'.

In particular, the IMF has identified three key 'transitions' that must be dealt with, noting that 'if these key challenges are not successfully managed, global growth could be derailed'.

These challenges include

1. a continuing rebalancing of the Chinese economy (although so far this transition is being relatively well managed, with growth coming in at a higher than anticipated 6.9% for 2015),
2. lower commodity prices, especially for oil (which, in itself, is related to the shift in emphasis away from manufacturing towards services in China); and
3. 'the exit from accommodative monetary conditions' in the US.

In the latter case, this exit began in December when the Fed raised official interest rates from around 0% to around 0.25% and also foreshadowed further likely interest rate increases this year.

In its 27 January statement though the Fed indicated that 'the actual path of the federal funds rate will depend on the economic outlook as informed by incoming data' and some of this data already looks weak.

The ISM manufacturing index fell to 48.2 in December, indicating that the sector is contracting, while (partly due to a high $US) aggregate corporate profits have been declining and net exports have been soft, while stock markets have fallen recently in response to weaker economic data.

On the other hand, expansionary monetary policy appears to be contributing to an improved economic outlook for much of Europe and for Japan.

The Australian economy picked up some speed in the September quarter, with GDP growth up by 0.9% (and 2.5% for the year).

However, what the Australian Bureau of Statistics calls 'a broader measure of change in national economic well-being', known as real net national disposable income, actually contracted by 0.1% for the quarter (and by 1.0% for the year and by 2.4% on a per capita basis), indicating that the economy remains quite weak, reflecting lower commodity prices and falling mining investment.

Major share markets were mixed in 2015, with the broad US market (S&P500 index) slightly down for the year, while the Japanese, German and Chinese markets were each up by 9%. However, 2016 began with investors in a negative mood, with most markets down heavily, including declines by end-January of 5% for the US (S&P500) and 3%, 9%, 8% and 5% respectively for the UK, Germany, Japan and Australia and a hefty 23% decline for China. Valuations though have now improved and most share markets currently appear to be fairly priced, especially compared with sectors such as bonds.

Major global government bond markets have seen yields (interest rates) drop sharply so far this year, reflecting growing investor doubts about the strength of economic recovery. However, with central banks likely to keep monetary policy accommodative, this may have been an over-reaction, especially as most bond markets appear expensive.

Fiducian's diversified funds are currently around benchmark for domestic shares and listed property but remain slightly overweight for international shares. Exposure to fixed interest sectors is underweight, while cash weightings remain above benchmark.