Monthly

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Economic & Market Commentary

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Conrad Burge
Investment Manager

For more information contact:
Your Financial Planner

The global economy remains sluggish, weighed down by particularly slow growth across the developed world.

The International Monetary Fund (IMF) in its latest report (October) once again downgraded its forecast for growth for the advanced economies to a meagre 1.6% for this year, while growth for 2017 is expected to be only a slightly better 1.8%.

As Christine Lagarde, Managing Director of the IMF, said on 1 September, the world appeared to be close to 'what I fear could become a low-growth trap'.

A feature of such a 'low-growth trap' is low productivity growth and this is occurring now across the developed world, with annual productivity growth below 1% in the US (the lowest it has been in the post-war period) and even lower in the European Union and Japan.

As Lagarde also noted, 'stubbornly weak demand … threatens to harm long-term growth as firms reduce production capacity and unemployed workers are leaving the labour force and critical skills are eroding'.

Furthermore, 'weak demand also depresses trade, which adds to disappointing productivity growth'.

Alan Greenspan, former Chairman of the US central bank, has also weighed in on this issue, stating on 27 May that 'until we can rein-in entitlement (welfare) spending, which has been rising at 9% per annum in the US and at comparable rates throughout the world, we are going to find that productivity is going to maintain a very low rate of increase'.

Furthermore, 'entitlements are crowding out savings and hence, capital investment. Capital investment is the critical issue in productivity growth and productivity growth in turn is the crucial issue in economic growth'.

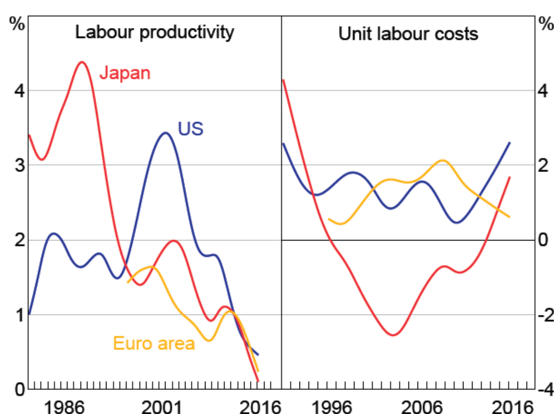
Also of concern, he added that 'if we stay down at the 2% or less economic growth rate in the US (currently around 1%) and elsewhere, we're not going to be able to fund what we are already legally obligated to spend'.

Indeed, Lagarde's 'low growth trap' could already be here and, as Lagarde points out, 'without forceful policy actions, the world could suffer from disappointing growth for a long time'.

Given this, we expect expansionary monetary policy to continue across the developed world and we expect more expansionary fiscal policy as well (through infrastructure spending) to be implemented over coming months.

The Australian economy is currently delicately balanced, with growth for the June quarter coming in at 0.5% but with 'longer-term risks becoming increasingly apparent as resource exports start to level off and dwelling construction turns negative' (NAB July business survey).

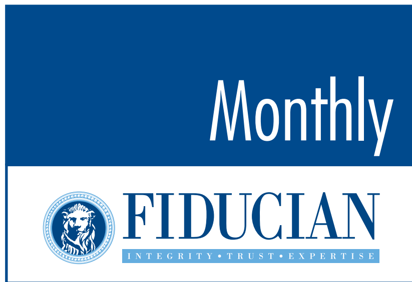
Figure 1 - Major Advanced Economies – Productivity and Unit Labour Costs (Year-ended growth)



Source: Eurostat, RBA, Thomson Reuters

Major share markets have been trending up since soon after the UK voted in a referendum on 23 June to leave the European Union.

From 1 January to 10 October, market movements included rises of 6% for the US (S&P500), 14% for the UK and 3% for Australia and declines of 1% for Germany, 14% for China and 11% for Japan.



Valuations mostly remain fair and most share markets still appear to be fairly priced, especially compared with other sectors such as bonds and cash.

Major global government bond markets experienced a downwards trend in yields (interest rates) from late last year (soon after the US central bank began to raise interest rates) until late July, taking yields close to historic lows, since when there has been a slight lift in yields. Overall, most bond markets continue to look expensive.

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

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