Our view

Researchupdate

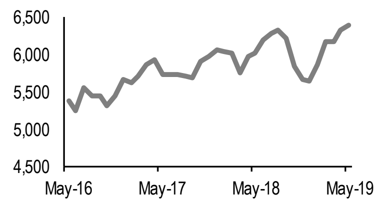
# Economic Wrap

May 2019


**Summary**

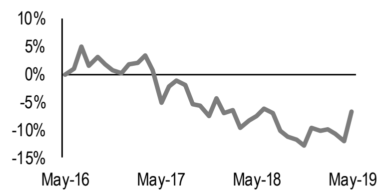
- Signs of emerging weakness in leading indicators and now, official economic data point towards slowing growth for this year in the US.
- Tariff and other forms of trade escalation continued over the month following the breakdown in US-China trade talks during April.
- The Trump Administration has continued to wield tariffs with Mexico the latest major partner to be affected in recent months.
- The Markit Global Manufacturing PMI has slipped into contractionary territory for the first time since 2016 with the slowing growth in the US insufficient to offset weakness in Europe, notably in Germany, and elsewhere.
- In keeping with the slower growth outlook Australian bonds rallied further while US yields also fell notably with trade and growth concerns weighing on economic expectations and seeing possible rate cuts ahead.


**1. S&P/ASX 200 Price Index**



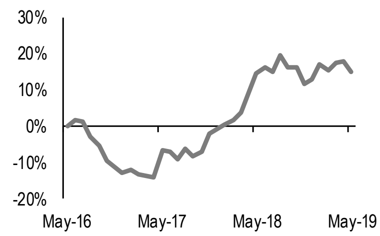

Source: Bloomberg, IOOF

**2. ASX200 vs All-World, US$ terms**



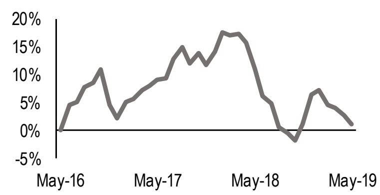

Source: Bloomberg, IOOF

**3. MSCI Australia Growth relative to MSCI Australia Value**




Source: Bloomberg, IOOF

**4. Emerging markets vs Developed Markets, US$ terms**




Sources: Bloomberg, MSCI, S&P, IOOF

**Markets** – May saw a retreat from risky assets with most global equity asset classes falling as did high yield bonds and, Australian mid and small caps (see page 14). Australian listed property was the best performer (up 2.3%) closely followed by Australian government bonds (up 1.9%) with both benefitting from the drop in Australian bond yields ahead of expected interest rate cuts by the Reserve Bank of Australia. In keeping with a "risk off" sentiment, we saw emerging market equities continue to fade relative to developed markets with Chinese equities struggling (see chart 4) and ongoing US Dollar strength a notable driver. The ASX notably outperformed global markets this month following the surprise Coalition victory (see chart 2) while value stocks outperformed on a relative basis (see chart 3) as tech company and other growth stocks trading at loftier valuations were sold off.

**Key economic news** – The Reserve Bank of Australia followed through on its May statement pointing to labour market weakness and the need for rate cuts to meet its economic forecasts with a 0.25% cut to interest rates in early June. March quarter GDP was also released that saw the Australian economy grow by 0.4% in the quarter and 1.8% in the year ended March 2019. Softer contributions by household spending and business investment were key drivers.

**Key company news –** Downgrade season was again a feature with the likes of Costa Group (ASX: CGC) and Link Administration Holdings (ASX: LNK) lowering their guidance ahead of results for FY19. Some notable beneficiaries of the Federal Election and signs of a stabilising property market included Domain Holdings Group (ASX: DHG) and its majority shareholder Nine Entertainment Company (ASX: NEC). Lynas (ASX: LYC) was a standout following signs that its operations in Malaysia would be allowed to continue and a surge in sentiment at the prospect of Chinese production cuts for rare earth metals.

## Sector and stock returns

**ASX/S&P 200 Sectors (GICS)**

| | Monthly | %Δ | Quarterly | %Δ |
|---|---|---|---|---|
| ▲ | Consumer Discretionary | 1.78 | Consumer Discretionary | 7.90 |
| ▼ | Consumer Staples | -4.22 | Consumer Staples | 6.57 |
| ▼ | Energy | -3.80 | Energy | -6.95 |
| ▲ | Financials ex Property | 0.85 | Financials ex Property | 2.30 |
| ▲ | Financials | 0.85 | Financials | 2.30 |
| ▲ | Health Care | 3.27 | Health Care | 6.84 |
| ▲ | Industrials | 0.09 | Industrials | 4.23 |
| ▼ | IT | -4.06 | IT | 5.60 |
| ▲ | Materials | 3.10 | Materials | 2.96 |
| ▲ | Property Trusts | 2.48 | Property Trusts | 5.87 |
| ▲ | Telecommunications | 7.32 | Telecommunications | 13.72 |
| ▼ | Utilities | -1.06 | Utilities | -0.67 |

**Best and Worst S&P/ASX 200 Performers**

| Top five stocks | | Bottom five stocks | |
|---|---|---|---|
| **Monthly** | | | |
| Lynas Corp Ltd | +54.0% | Costa Group Hldgs Ltd | -30.3% |
| Domain Hldgs Aust Ltd | +21.9% | Reliance Worldwide Corp | -24.8% |
| Evolution Mining Ltd | +21.3% | Nufarm Ltd | -22.1% |
| Syrah Resources Ltd | +19.4% | Bluescope Steel Ltd | -21.6% |
| NIB Holdings Ltd | +19.1% | Link Admin Holdings | -21.4% |
| **Quarterly** | | | |
| Lynas Corp Ltd | +73.3% | Eclipx Group Ltd | -43.3% |
| DuluxGroup Ltd | +33.7% | St Barbara Ltd | -40.9% |
| Fortescue Metals Grp Ltd | +32.8% | New Hope Corp Ltd | -37.4% |
| Afterpay Touch Group Ltd | +31.0% | Galaxy Resources Ltd | -28.3% |
| Nearmap Ltd | +30.4% | Costa Group Hldgs Ltd | -26.0% |

Source: Bloomberg, IOOF

## Equity review

### Major Market Performance, May 2019

| | Australian Indices | May-19 Price | 1M return (%) | Feb-19 Price | 3M return (%) |
|---|---|---|---|---|---|
| ▲ | S&P/ASX 200 | 6397 | 1.13 | 6169 | 3.69 |
| ▲ | All Ordinaries | 6492 | 1.14 | 6253 | 3.82 |
| ▼ | Small Ordinaries | 2817 | -1.34 | 2765 | 1.88 |
| | **US Indices** | | | | |
| ▼ | S&P 500 | 2752 | -6.58 | 2784 | -1.16 |
| ▼ | Dow Jones | 24815 | -6.69 | 25916 | -4.25 |
| ▼ | Nasdaq | 7453 | -7.93 | 7533 | -1.05 |
| | **Asia Pacific Indices** | | | | |
| ▼ | Hang Seng | 26901 | -9.42 | 28633 | -6.05 |
| ▼ | Nikkei 225 | 20601 | -7.45 | 21385 | -3.67 |
| | **UK & Europe Indices** | | | | |
| ▼ | FTSE 100 | 7162 | -3.46 | 7075 | 1.23 |
| ▼ | CAC40 | 5208 | -6.78 | 5241 | -0.63 |
| ▼ | DAX Index | 11727 | -5.00 | 11516 | 1.83 |

Sources: Bloomberg, MSCI, FTSE, S&P, IOOF

Note: return is reported on a price basis and in local currency terms e.g. S&P500 performance is in US dollars and excluding dividends.

**Global equity markets**

The S&P 500 index finished May down 6.6% while the tech-heavy NASDAQ fared worse, down 7.9%. The market performance was negative across all sectors except Real Estate (up 0.9%) with Energy (down 11.7%), Technology (down 8.9%) and Materials (down 8.5%) the worst performers. Real estate benefited from the fall in US bond yields while other Defensive sectors such as Utilities also benefitted with drawdowns notably below that of the broader market.

Globally most markets fell during the month led by concerns on a mix of trade and in the case of Europe, Brexit fears. On the trade front, the escalation following the targeting of Huawei by US authorities and planned Chinese responses to restrict rare earth exports in addition to other relation has seen investor sentiment sour considerably. The prospects for China have been notably poor with the Hang Seng Index down 9.4% during the month. In Europe the resignation of Theresa May has seen the prospect of delayed Brexit negotiations and the likely election of a firmer "Brexit" candidate emerge making a "no deal" deal Brexit a more realistic prospect again.

**Australian equity market**

The S&P/ASX 200 index finished the month up 1.1%. Most sectors were in positive territory with consumer staples (down 4.2%), energy (down 3.8%), technology (down 4.1%) and utilities (down 1.1%) the notable exceptions.

The poor performance of consumer staples in the context of a strong overall market was due predominantly to the poor performance of milk producers A2 Milk (ASX: A2M) and Bellamy's (ASX: BAL) as well as a decline in Treasury Wine Estates (ASX: TWE). The milk producer performed was potentially due to fears of trade war impacts which were arguably realised in early June with a report from the Chinese National Development and Reform Commission that called out domestic milk production to be above 60% share (potentially negative for foreign producers such as A2 Milk). Treasury Wine Estates struggled following an attack by a US-based short seller as well as news from Wine Australia that export volumes to China had fallen (prompting fears over its Chinese growth prospects).

The Communication sector rallied thanks to the prospective takeover bid for Vocus (ASX: VOC) by Swedish firm EQT Infrastructure at a considerable premium to the prevailing share price prior to the bid. Subsequently in June after conducting due diligence EQT has walked away from any prospective deal with the Vocus share price declining accordingly. Optimism on the property market was also a driver of the sector performance with REA Group (ASX: REA) and Domain (ASX: DHG) rallying following the re-election of the Federal Coalition government and end to fears over Labor's perceived anti-property policies including negative gearing reform.

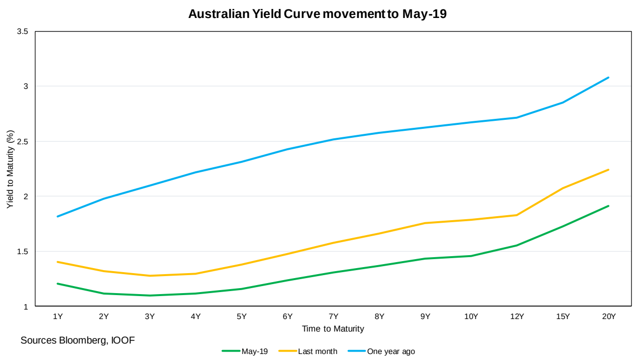
## Fixed Income

| | Fixed Income | May-19 yield | 1M mvt (bps) | Feb-19 yield | 3M mvt (bps) |
|---|---|---|---|---|---|
| | Aussie Cash rate | 1.50 | -- | 1.50 | -- |
| ▼ | 10-year Bond Rate | 1.46 | -0.33 | 2.10 | -0.65 |
| ▼ | 3-year Bond Rate | 1.10 | -0.18 | 1.63 | -0.53 |
| ▼ | 90 Day Bank Accepted Bills SFE-Day | 1.42 | -0.14 | 1.87 | -0.45 |
| ▼ | US 10-year Bond Rate | 2.12 | -0.38 | 2.72 | -0.59 |
| ▼ | US 3-year Bond Rate | 1.87 | -0.37 | 2.49 | -0.62 |

Source: Bloomberg, IOOF

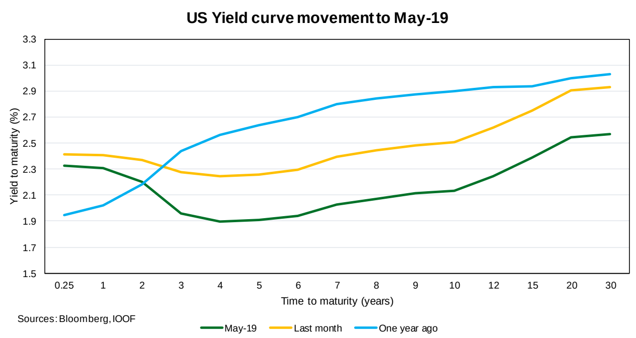
The Australian yield curve fell further in May as markets increasingly priced in the prospect of RBA rate cuts with the movement sharpest at longer durations. The 10-year bond yield fell 33bps and the 3-year yield was down by 18bps. A collection of disappointing economic data including the headline miss on the unemployment rate which rose to 5.2% and weaker NAB business survey results featured prominently. This was especially so after the release of the RBA May meeting minutes that highlighted readiness to cut rates to meet its May *Statement on Monetary Policy* economic forecasts. That disclosure coupled with the weaker economic data saw the market continue to price in this possibility aggressively which was confirmed in early June by a 25bps cut to move the cash rate to 1.25%. This was a sharper shift in sentiment even relative to our last publication in April which is a reflection not just of our domestic economy but also prospects globally.

### 5. Australian yield curve movements to May 2019



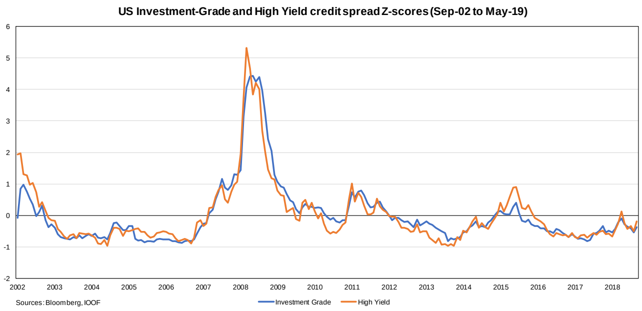

The U.S. yield curve continued to fall in May following concerns over global growth and softening leading indicators in the US with the May manufacturing PMI continuing to slow. US economic growth for the March quarter was revised downwards slightly to 3.1%. This weighed on sentiment because while net exports and an inventory build were supportive during the quarter, growth excluding these factors was relatively weak with this update serving to confirm this. An alternative, leading measure for GDP, Gross National Income only grew 2.2% for the quarter (annualised), below the post-GFC average of 2.4% and suggesting slower growth going forward. Other factors included the prospect of weaker trade as a result of tensions with China and also Mexico. The focus on weak inflation as temporary in the May Fed Minutes was poorly received as an indicator of an unwillingness to cut rates. Yields fell as a result with pronounced moves at both short and long durations.

### 6. US yield curve movements to May 2019




Lastly, we illustrate the fading of risk appetite globally as seen by an uptick in credit spreads for US investment grade and high yield debt. These are still relatively contained even in comparison to the 2018 December quarter sell off and may expand further should trade war concerns and disappointing economic data eventuate. Notably investment grade spreads (the **blue line**) have not expanded much during the month (reflecting their better credit quality) helping explain the performance gap on page 14 with investment grade returning 1% versus a high yield (the **orange line**) return of -0.9% during May.

### 7. US investment grade and high yield debt credit spread (Z-scores)




## Currencies

| | Currencies | May-19 Price | 1M return (%) | Feb-19 Price | 3M return (%) |
|---|---|---|---|---|---|
| ▼ | $A vs $US | 69.38 | -1.56 | 70.94 | -2.20 |
| ▲ | $A vs GBP | 54.93 | 1.55 | 53.49 | 2.70 |
| ▼ | $A vs YEN | 75.12 | -4.36 | 79.02 | -4.93 |
| ▼ | $A vs EUR | 62.11 | -1.19 | 62.39 | -0.45 |
| ▲ | $A vs $NZ | 106.25 | 0.62 | 104.22 | 1.95 |
| ▲ | $US vs EUR | 89.54 | 0.41 | 87.94 | 1.82 |
| ▲ | $US vs GBP | 79.16 | 3.17 | 75.40 | 4.99 |
| ▼ | $US vs CHF | 100.06 | -1.83 | 99.82 | 0.24 |

Source: Bloomberg, IOOF

The Australian dollar (AUD) fell by 1.56% to USD 0.6938. The calls for interest rate cuts on domestic weakness were key to offsetting stronger iron ore prices which would ordinarily support the dollar. Markets have continued to focus on the increasing interest-rate differential between the US and Australia in recent years. Key to that dynamic is the pressure on global trade from escalation between the US and China (and now Mexico) with the US Dollar enjoying safe haven demand. By contrast economies with greater leverage to global trade such as the EU or China have seen their currencies struggle in this environment. This foreshadowing came to pass in early June with the RBA cutting rates to 1.25% citing general economic weakness and the need to meet their inflation and other forecasts to abide by their policy mandate.

The US Dollar rose against the Euro and the pound during the month even as the divergence of PMI data has begun to close with slowing US manufacturing production. A key geopolitical event on this front has been the re-emergence of an unruly Brexit as a scenario for global markets to digest. This follows the resignation of PM Theresa May and the expectations of a harder "pro-Brexit" candidate leading government such as Boris Johnson. Such a trend supported the Australian and US Dollar against the pound.

## Commodities

| | Commodities | May-19 Price | 1M return (%) | Feb-19 Price | 3M return (%) |
|---|---|---|---|---|---|
| ▼ | Aluminium | 1778 | -0.48 | 1917 | -7.29 |
| ▼ | Copper | 264 | -9.09 | 295 | -10.63 |
| ▼ | Nickel | 11980 | -1.67 | 13073 | -8.36 |
| ▲ | Gold | 1311 | 1.50 | 1329 | -1.34 |
| ▼ | Silver | 15 | -2.78 | 16 | -7.39 |
| ▼ | Crude Oil - Brent | 64 | -11.41 | 66 | -2.33 |
| ▼ | Lead | 1802 | -6.20 | 2154 | -16.35 |
| ▼ | Zinc | 2630 | -8.39 | 2774 | -5.17 |
| ▲ | Iron Ore | 98.76 | 5.92 | 87.33 | 13.09 |

Source: Bloomberg, IOOF

Commodity prices fell over the month except for gold and iron ore. Iron ore prices continued to be supported by the continued suspension of production by major Brazilian miner Vale following the collapse of a tailing dam with loss of life and environmental damage as a result. This came at a time where Chinese stimulus has been supportive of stronger steel production. Expectations of stronger Chinese stimulus on the back of disappointing April economic numbers and to offset trade war-induced weakness have also been supportive of prices. A similar supply shock dynamic has not played out to the same extent in other base metals which, along with oil, fell on the back of global growth concerns triggered by the breakdown of the US-China trade negotiations and the implications this has for weaker global trade.

Gold prices rose on the back of market volatility as a "safe haven" asset as well as increased speculation of cuts to US interest rates to combat an economic slowdown. Gold as an asset offers no yield so can struggle in rising interest rate environments. The prospect of a rate cut makes it more competitive with fixed income as a "safe haven" alternative, helping support prices.

## Australia

**Additional negative economic data along with a weaker global backdrop saw the RBA cut rates in early June. The latest GDP growth figures confirmed weaker economic momentum with annual growth slowing to 1.8% in the year to March. The surprise election win by the Coalition sparked an uptick in property markets with the correction slowing further.**

The RBA cut interest rates in early June by 0.25% to 1.25%. A cut had been flagged in recent policy statements as necessary to maintain the growth trajectory the RBA had forecast. This was confirmed in the Statement immediately after the meeting noting the need to support employment growth and the Bank's conviction that lower unemployment could be sustained without an excessive increase in inflation. It was also a reflection on concerns for the global economy with weaker growth in global trade highlighted as a factor detracting from global growth and supportive of a more accommodative stance on interest rates. Finally, a speech by the Governor Lowe following the meeting left open the real possibility of another rate cut by the end of this year in line with current market pricing. He also highlighted the need for other policy support such as fiscal and structural reforms to reduce unemployment and improve growth outcomes.

Market expectations and the Reserve Bank moved faster than we noted in the last monthly report. This reflects the additional negative economic updates we flagged then and general global concerns after trade disputes between the US and China escalated once again. Current market expectations suggest another rate cut by October if not in September which would take the cash rate to 1% in line with Governor Lowe's remarks. Much will depend on the global backdrop and the state of the domestic economy with the Coalition victory removing the possible threat of substantial tax and policy reform.

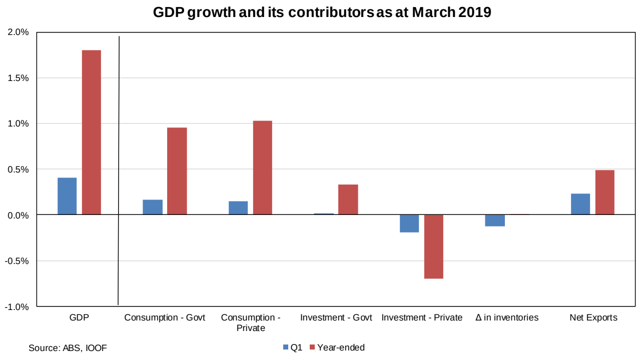
In May we saw the ruling Coalition government returned with a slightly larger majority contrary to both the predictions of polls leading into the election as well betting markets. This victory ends the possibility of the substantial Labor reform agenda coming to fruition. This saw a mix of companies rally after the election particularly those with property exposure that investors expected to suffer most from the predicted Labor victory. We expect the Coalition to follow through on its electoral promise of smaller scale tax cuts this year with the larger scale tax reform not due for several years. Both sets of measures require legislation to become effective which we believe should be forthcoming. Beyond these and announced support for new infrastructure the policy agenda of the Coalition should develop in time.

The March quarter GDP figures were slightly below weaker growth expectations heading into the result with 0.4% growth during the quarter (consensus: +0.5%). Private sector investment continuing to drag influenced by weaker residential construction (as we raised in earlier weekly commentary on the decline in building approvals). In addition, household and government consumption spending were weaker contributors adding only 0.15% and 0.16%

each to quarterly growth versus 0.24% and 0.39% contributions in the December quarter respectively. While Net exports swung from a detractor to contributor this was insufficient to see headline growth meet estimates.

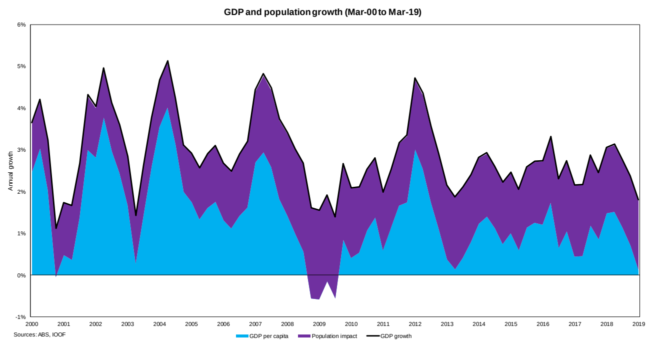
We can see this dynamic illustrated below in chart 7 where the factors of interest include the weaker state of household consumption during the quarter. This was accompanied by a slight uptick in the household savings rate potentially suggesting that consumers were responding to the declining value of property wealth by cutting back on consumption, the negative “wealth effect” we had discussed in the March quarterly report.

### 7. Mar-19 quarterly and annual GDP growth by component



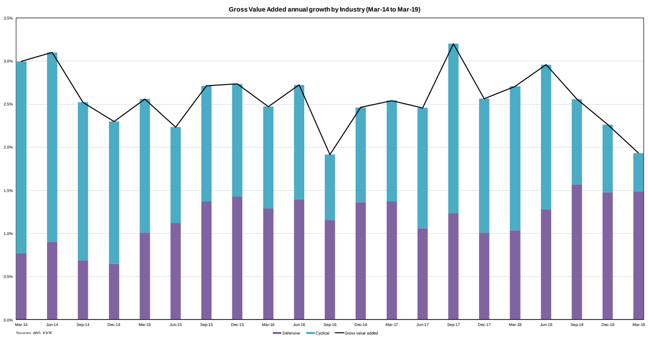

The trend of weak per capita growth noted in previous quarters and webinars has continued. Chart 8 is a decomposition of GDP growth into **GDP per capita** and, **population growth**. As we can see annual growth in per capita GDP is essentially flat with overall growth attributable to a larger population (more people → more demand for goods and services → more economic activity). This is a concern as it suggests weaker productivity growth has continued to run its course i.e. technological and other advancements are not being sufficiently leveraged to expand living standards on an individual basis. This adds to the case for additional government reforms to encourage research and investment to spur average living standards higher.

### 8. Annual GDP growth and its underlying components as at Mar-19




Finally, we turn to an alternative split of the economic growth numbers, the gross value added measure. This is a reflection broadly speaking of the individual industry contributions to economic growth. The sum of gross value-added, government taxes and subsidies and a balancing item add to total GDP. Chart 9 looks at the contributions to growth of cyclical versus defensive sectors. Here Defensive sectors include those such as education, utilities and healthcare. Similar to the split noted in the employment data last month, here the growth that we are seeing has been from those defensive sectors with cyclical ones weakening over the past three quarters. While we expect to see continued demand supported by government spending on the NDIS and infrastructure this serves as another sign of underlying fragility of growth at present. It supports the remarks by Governor Lowe for more work on other policy angles, not only monetary policy to support growth. The tax cuts, once legislated, should assist on this front but more may be required.

### 9. Gross Value Added annual growth by industry (Mar-14 to Mar-19)




Delving into an earlier mixed report we look next at the latest capital expenditure data. It showed new capital spending for the March quarter fell -1.7% (consensus: +0.4%) with the declines led by building and structures (down 2.8%) while machinery and equipment spending was also lower, down 0.5%. December quarter growth was also revised downwards from 2% to 1.3%. On the positive side however, the outlook for FY20 has strengthened slightly with Estimate 2 for FY20 capital spending growth increasing by 12.8% versus last year’s estimate. A key driver has been the increase in estimated mining investment spending (up 21% year on year) thanks to a mix of strong iron ore prices and the need for major producers to invest for maintaining production volumes. This should be a support for growth over the next financial year provided the forward estimates hold up.

Moving then to credit, the ABS reported lending data for households and business to March 2019. The decline is housing credit growth continued with total lending for dwellings (excluding refinancing) falling 18.4% from March 2018. Chart 10 captures the significance of this for house prices using a combination of the ABS and CoreLogic data series (CoreLogic for the March quarter only). Credit growth (in **blue**) has been a good forward indicator for the future direction of house prices (in **red**) on the basis that more money chasing a limited supply of houses leads to price inflation. The current trend points towards further correction in prices over the next half-year. This supports the negative growth expectations of ourselves and other research houses.

**10. Annual housing price growth versus advanced housing finance growth (Dec-05 to Sep-19)**


We note however that the pace of the decline appeared to be slowing ahead of the Federal election. This arguably saw confirmation in the latest CoreLogic data with the pace of the national correction slowing to be only down -0.4%.

Building approvals fell in April by 4.7% (consensus: 0%), an improvement on the 15.5% decline experienced in March. The surprise decline was led by apartments, down 6.5%, as well as weakness in house approvals, down 2.6%. This result points to a continued headwind for residential construction to start the June quarter. We also saw private sector credit growth disappoint with 0.2% growth in April (consensus: 0.3%). It remains to be seen in subsequent data releases how the Coalition election win might have changed this dynamic. The change in APRA regulations for lending as well as the Coalition first-home buyer support may be supportive of a restart in credit growth. This must be balanced against tighter underwriting by major lenders moving away from the looser HEM standard in assessing borrower expenses. We continue to watch the situation and maintain that a sustained uptick in credit growth will be necessary for housing prices to end their current correction.

Moving now to the labour market, wage growth for the March quarter showed a quarterly rise of 0.5% (consensus: 0.6%) and annual growth of 2.3% (consensus: 2.3%) in line with the previous result. The miss on the quarterly numbers was broad-based with state-level numbers pointing towards a weaker quarterly result for NSW of 0.4% for the private sector while Victorian wage growth was slightly better at 0.5% driven by strong public sector wage growth of 0.7%. The result is slightly disappointing as it points to persisting slack within the labour market where even those states with low unemployment (Victoria and NSW at 4.6% and 4.3%) have struggled to generate wage inflation.

The unemployment rate rose to 5.2% in April (consensus: 5%), up from 5% in March. Employment growth also surprised with total employed persons rising by 28.4k (consensus: +15k) continuing its positive trend in recent months. The bulk of this increase came in part-time jobs with 34.7k growth offset by weakness in full-time job creation with the loss of 6.3k part-time roles. The annualised 3-month change highlights jobs growth (+2.13%) slightly above population growth (+2.05%) driven by full-time job creation (part-time jobs growth is slightly negative for the year to date). In addition, if we had seen the participation rate hold steady (it increased by 0.1% to 65.8%) the unemployment rate would have held at 5%. This is a mixed picture on the labour market front than we saw at the beginning of 2018 with the March unemployment rate also revised upwards thanks to a reduction in full-time job losses recorded in the initial release.

As we noted in earlier weekly commentary:

*Given the emphasis placed on the labour market in the RBA April minutes and their May statement we expect that this latest report may add to the case for a rate cut. The RBA case for a cut would need to see an improving labour market and falling unemployment rate i.e. the uptick in participation needs to translate into more jobs and lower overall unemployment. While employment growth improved, the drop in full-time employment, headline rise in the unemployment rate and uptick in underemployment will add to calls for a rate cut particularly if they mark the start of a trend with the latest NAB business survey suggestive of weaker employment growth in the months ahead*.

This came to pass faster than expected. We will continue to watch leading indicators such as the NAB surveys for signs on the future direction of growth. On this note we close with a positive in the latest datapoint, the IHS Markit Composite PMI. There we saw an uptick from 50 in April to 51.5 in May. A post-Election bounce was cited for stronger new business demand and business confidence also improved. Both however are still at levels below historic average but may make a trough in growth for future quarters.

On balance the risks to the Australian economy remain tilted to the downside with the economy growing at its weakest in several years. This is reflective of the slowing economic momentum elsewhere in the world as well as the high indebtedness of Australian households. While weaker growth remains the more likely outcome, we acknowledge the possible deployment of further interest rate cuts and government spending to support the economy.

## United States

**The strong growth to March was confirmed in revised figures. However, expectations of slower growth going forward have increased as underlying consumer and business demand has softened and residential investment drags on growth. The prospects of cuts to interest rates has continued to rise driven in part by fears over the impact of escalating trade tensions between the US and China and, the US and Mexico with the potential to draw in other countries as well.**

One major focus this month was the escalation in trade rhetoric and policy measures between the US and China. As we noted in the last update the US increased tariffs on US$200bn of Chinese goods from 10% to 25% following the breakdown of trade negotiations. Following this China announced its own tariff increases on $US60bn of US goods from June 1 targeting a range of agricultural and industrial goods. This was implemented in a tiered fashion ranging from 5% on some goods to an upper limit of 25% (up from 10% in this case). In addition, the US Trade Representative announced plans to hold public hearings on June 17. These would cover the potential application of 25% tariffs on a further US$300bn of Chinese imports including cell phones and laptops.

The escalation was also evident in non-tariff measures with the US following on from national security concerns to ban US companies from selling to Chinese firm Huawei without government approval. China announced its own list of “unreliable entities” in retaliation. In early June China also announced an official investigation into US firm FedEx for diverting outbound packages from Japan that were bound for China to the US. We also saw possible curbs in rare earth exports by China openly raised as another non-tariff tool.

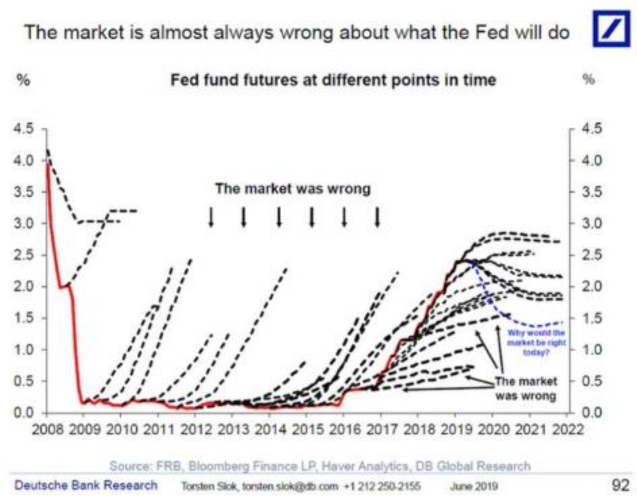
Observers are looking forward to the upcoming G20 Summit in June and an expected meeting between Presidents Trump and President Jinping to see if any thawing in relations occurs. Given the specifics of how the negotiations broke down with China walking back on enforcement commitments, it appears that a final resolution might be delayed for longer than previously expected. The meshing of trade and other strategic imperatives may constrain negotiators on both sides from coming to the table and see continued market volatility as a result. As it stands the tariffs that have been implemented will act as a drag on Chinese growth (discussed below) and broader global growth, especially if they escalate further. The impact on the US is expected to be more muted but still contribute to weaker growth particularly if escalation elsewhere emerges.

On this subject we note the likelihood of rising tariffs levied against Mexico. This emerged late in May as the Trump Administration issued the threat in response to its views on a lack of control over illegal immigration into the US. Talks are underway between the US and Mexico, but the deadline is still for the implementation of 5% tariffs on June 10. The cost of these tariffs for the US economy is expected to be higher given the more direct relationship after years of integration under NAFTA between the two countries. Under the specifics announced the US tariffs would escalate from the 5% level each month to a peak of 25% in October if Mexico could not adequately address the illegal immigrant issue. Bloomberg Economics currently estimates a 0.8% drop in 2021 GDP if it were to implement 25% tariffs on trade with China and Mexico compared with a scenario that has no trade war. We note that these are considering a “worst case” scenario that may not eventuate. The negotiating position of Mexico is weaker than that of China and given past trade concessions to the Trump Administration there remains a real possibility of heading off this escalation by meeting US demands. We continue to watch this space and expect further announcements to contribute to broader market volatility as noted earlier in this report.

The May FOMC Minutes of the US Federal Reserve advocated a patient approach to interest rate adjustments anticipating being on hold in the short term given moderate economic growth and muted inflation expectations. Members also highlighted the transient factors they saw keeping inflation lower at present. One concern was the possibility of inflation expectations across the economy being anchored at lower levels and whether monetary policy would need to be more flexible as a result. The implication being to perhaps allow inflation to run above the 2% target in a more persistent fashion or to change the target. The mechanics of running down the balance sheet and longer term the nature of its investment portfolio were also raised. It looks more likely that quantitative easing is being regarded as a permanent policy lever going forward. Remarks in early

June have added a more dovish tone to the Federal Reserve outlook giving some confidence to market expectations of lower interest rates this year (currently suggesting at three rate cuts). While we do not discount this belief, we will say that activity needs to soften materially more for this course to eventuate. The latest PMIs appear to be pointing to slower economic growth (discussed below) and we will look ahead to the next set of Board projections in late June to see the extent they reduce their interest rate outlook. We close by noting the difficulty in anticipating the Fed's course of action as Chart 10 from Deutsche Bank research highlights tracking the actual interest rate in **red** versus the different expectations of monetary policy implied by market pricing. Additional shocks appear necessary to dictate the current three-cut path being implied and we will continue to observe developments in the US economy and how these affect our outlook.

**11. Fed Fund Futures vs actual US interest rates (2008 – 2022)**




Manufacturing conditions weakened in May. The Markit Manufacturing PMI fell from its May reading of 52.6 to 50.5, its lowest level since late 2009. Slower client demand softened further in the month with the first client in new orders in almost 10 years. This was matched by a weaker expansion in output as well as subdued business confidence. Uncertainty for the forward outlook driven in part by trade tensions weighed on sentiment for the coming year. The close ties between US manufacturers and the Mexican economy suggest this situation could worsen further if the tariff threats of the Trump administration are enacted. In addition, with survey numbers at these low levels relative to earlier results it is likelier that business production will drag on economic growth or make a weaker contribution.

The Markit Services PMI for May also fell from its April reading of 53.0 to 50.9. Weaker demand conditions both domestically and overseas were behind the more marginal increase in business activity. In addition, business confidence was subdued at its lowest level since mid-2016 with global trade tensions being cited as an ongoing cause for the poorer sentiment. On a positive note services firms continued their hiring and the current outlook is still positive for the labour market but the drop off for the manufacturing sector remains a cause for concern. The Composite Index (services and manufacturing combined) fell to 50.9 in May, down from 53 in April with the weakness in both manufacturing and services sectors driving the result. Overall these surveys point towards weaker economic growth. The April run-rate was consistent with annualised growth of 1.9%. This latest result however is consistent with a reading of 1.2% suggesting a notable slide in momentum from the March quarter according to Markit economists. The Atlanta Fed's GDP model almost reflects these readings with annualised growth for the June quarter of 1.3% based on data releases to date. These factors remain in line with our outlook in the December quarterly of slowing US growth.

On balance US risks have shifted to the downside with tariff tensions on top of a weaker economic drop. Fed policy looks to be gradually moving to a more accommodative posture particularly if retaliation to US tariffs requires looser monetary conditions to spur growth.

## China

**Economic momentum held up in manufacturing for May but weakened overall. Trade war escalation with the US looms as a source of uncertainty for future growth. The case for additional stimulus appears to have strengthened given ongoing weakness in export growth and no clear end to the tensions with the US after the Chinese delegation walked back on prior commitments.**

The IMF has lowered its growth forecasts for China to 6.2% and 6% for 2019 and 2020 respectively, a cut of 0.1% from its prior forecasts. While it noted the economy continues to enjoy support from stimulus by the government, the renewal of trade tensions with the US have increased uncertainty and weighed on business sentiment. It does not anticipate the need for further policy easing on the assumption that there is no further tariff escalation. These remarks echo the confidence issues plaguing Chinese firms that have been highlighted in previous monthly reports commenting on the Markit PMI surveys. The lack of progress with the US over the past month continues to weigh on the China outlook with both sides digging in their heels. We note that underlying measures of economic activity such as rail freight and bank loan growth (as opposed to headline GDP) have, while softening, still maintained levels above previous lows such as the 2015-2016 period (a tumultuous time for commodity markets). On the positive side for Australia, any additional stimulus by China would be expected to support export growth and government revenues domestically.

Retail sales rose 7.2% year-on-year in April (consensus: 8.6%), faltering after a strong March result where stimulus had a more pronounced effect. In addition, industrial output slowed to 5.4% annual growth (consensus: 6.5%) while fixed-asset investment growth was 6.1% (consensus: 6.4%). Digging into the detail paints a picture of underlying weakness with private sector fixed-asset investment spending growing 5.5% in contrast to 6.4% growth in earlier reports suggesting weakness in the private sector which accounts for the majority of both jobs and investment in China. It also suggests that the government stimulus has had a pronounced effect on the more inefficient state-owned enterprises, a path that is regarded as less sustainable in the long run. At the time of the release the results were relatively well-received by markets echoing a “bad is good” dynamic where weaker economic performance is seen as sparking more government stimulus. This is so after remarks by the Chinese central bank raised fears of a more measured approach to further stimulus. We anticipate further stimulus may be deployed given the additional shock of higher US tariffs and possibility of further escalation.

The Markit manufacturing PMI for May remained in positive territory for a third month but was unchanged at 50.2 in May. On the positive side both new work and export sales rose slightly with new export orders returned to expansionary territory (the first time since January). Employment conditions appear to have stabilised while manufacturers showed greater signs of a willingness to replenish diminished inventories. However, the trade war impact took its toll on sentiment towards future output which fell to its lowest level since the inception of the survey in April 2012. We may see manufacturing slip back into contractionary territory depending on the full impact of tariffs and other barriers implemented to date.

Services activity fell from 54.5 in April to 52.7 in May driven by a weaker rise in sector activity. New export orders rose for the services sector as well with overall new business rising slightly (indicating ongoing domestic demand as well). Job creation continued in the services sector while overall competition limited the ability of firms to pass on increases to end consumers. This decline in the headline index saw the overall Composite PMI fall to a three-month low of 51.5 in May, down from 52.7 in April. Overall new business remained in expansionary territory while new export orders returned to this state after contracting in prior months. The negative impact of rising trade tensions could continue to play out in the data and economic performance. Of some concern and suggestive of the need for further stimulus to support growth is the decline of the employment gauge in aggregate which has seen the State Council of China establish a new leading group to promote jobs creation. This would also assist in combatting the decline in business confidence.

## Europe

**Trade concerns and a weak consumption outlook weigh on the European economy. Brexit has been delayed until later in the year following flexible deadlines from EU leaders. A surprise GDP result has sparked calls for a trough in European growth, but still weak survey data suggests caution is warranted.**

Looking to the UK first we note the upcoming resignation of PM Theresa May. Over the past year her leadership has faced several challenges. The inability to deliver a Brexit outcome marked the end of her tenure. At the time of righting several possible candidates are vying for favour among Conservative Party MPs. Among the favourites are more ardent Brexit supporters such as Boris Johnson. These candidates have become further emboldened by the strong showing of the Brexit party in the latest European elections for UK representatives. This has seen political observers ascribe a greater possibility of a disruptive “no deal” Brexit with negative consequences for the UK and the EU. Purely from a practical standpoint the lack of clear leadership makes it less likely that a deal can be reached by October (the end of the latest EU extension). This is because the leadership contest could drag on until late July if a clear winner does not emerge early in the process. On balance this looks to be a net negative from an economic standpoint, especially if the “no deal” scenario comes to pass without a clear plan of action.

The UK economy looks to have slowed materially after a robust 0.5% growth during the March quarter. Much of that growth was driven by business stockpiling ahead of possible disruption from the then Brexit deadline for March 29. The Bank of England has forecast quarterly growth as slowing to 0.2% for the June quarter. Overall this sets the seen for UK rates remaining on hold until after a deal can be done and even then, only if the economic situation strengthens enough to warrant a hike. However, rate cuts remain a real possibility if a Brexit arrangement cannot be reached given the negative impact it is anticipated to have on the UK economy if a “no deal” scenario were to play out. The weak economic situation suggests that the hawkish rhetoric in previous Bank of England statements will no translate into concrete action (in the form of rate hikes).

On the ECB, the April minutes highlighted concerns that economic growth was even weaker than expected and seen market observers advocate further policy support via the upcoming targeted longer-term refinancing operations (TLTROs). The expectation that this programme—a way to offer banks cheaper access to funding provided it is lent to businesses and consumers (and not used for speculation)—will be offered on more generous terms to encourage usage. Negative rates did not feature as a major consideration despite protests by banks during the month over the negative impact this had for profitability. We see the ECB as ready to deploy further easing to support the economy however the lack of further guidance makes the possible use of other unconventional policies such as quantitative easing unlikely in the short-term.

Considering Europe more generally inflation continues to be weak at both a household and business level with Euro area annual inflation sitting at 1.2% in May (consensus: 1.3%) and producer price inflation falling 0.3% in March to be up 2.6% for the year. Producer price inflation is seen as a forward indicator for future consumer inflation and the lack of impetus there is supportive of the business surveys discussed below that point to a weak inflation environment persisting. Notably core inflation also dropped off to be 1% over the year to May, down from 1.4% in April.

Retail trade disappointed in the latest monthly data with a -0.4% drop in April (consensus: -0.2%) and growth in the year to April of 1.5% (consensus: 1.8%). However, on the positive side unemployment reached its lowest level in 10 years during April at 7.6% (down from 7.7% in March).

Geopolitically, the deficit concerns between Italy and the European Commission (EC) also appear to be coming to a head. The EC has announced it will begin its infringement process against Italy calling for up to €4bn in savings to breaching the EU deficit limit of 3%. This has seen Italian bond yields maintain premiums over other Eurozone debt as investors price in the risk of Italy defaulting or leaving the Eurozone. The case for the Italian government appears to have been strengthened with a solid showing in the latest European elections and it remains to be seen whether Italy or the EC will blink should the situation escalate further.

The Markit Eurozone Composite PMI improved slightly in May with a reading of 51.8, up from 51.5 in April. The region’s key manufacturing industry weakened with a reading of 47.7 in May, down from 47.9 suggesting a deeper slump in manufacturing activity. German industry remains a point of weakness with a reading of 44.3 dragging the overall sector down. By sector the weakness is centred in intermediate and investment goods with the consumer space continuing to enjoy growth. Key drivers continued to be weakness in new orders which saw production lower for a fourth consecutive month and backlogs also reduce. Following almost 5 years of expansion, there was a net decline in manufacturing jobs. The weakness was driven by Germany although a decline was also marked for Spain. In addition, there were other signs of weaker utilisation of existing productive capacity with lead times for the delivery of inputs continuing to shorten for three consecutive months together with the weaker output growth of firms in the survey. The divergence between PMI data and the hard-economic data in the March quarter GDP result remains an area we continue to observe for the future direction of European growth.

In May the Markit Services Sector PMI rose slightly to 52.9 from 52.8 in April. While new business growth remained week (at a three-month low) other aspects improved such as increased jobs creation with Germany a standout. This also saw an uptick in wage growth pressuring overall sector costs but due to substantial competition only some of these were passed on to end clients with output charges, a measure of pricing to customers, rising at their slowest pace since August 2017. Overall business confidence remains challenged however. The low growth in new business orders paints a picture of weaker underlying demand. According to IHS Markit economists the surveys at this stage are suggestive of 0.2% quarterly GDP growth, a slower pace than the March quarter 0.4% result.

## Company news (best and worst performers over the month of May)

### Lynas Corp Ltd (LYC)

Lynas shares benefitted this month by the mooted threat of China restricting the exports of rare earth metals to the US. As the producer of approximately 70% of global supply this had notable implications for Lynas as one of the few notable sources outside of China with investors anticipating the benefit of higher prices due to lower global supply. In addition, the company has been troubled by concerns over the possible shutdown of its Malaysian processing operations on environmental grounds. Over the course of the month and following a press conference by the Malaysian Prime Minister it appears these fears have largely been addressed and the company will be able to continue operating. Finally, the announcement of a joint venture in the US to conduct processing operations there should help diversify its geographic footprint and reduce the geopolitical risk of a possible shutdown of its Malaysian business going forward.

### Domain Holdings Australia (DHG)

The Federal Election win by the Coalition government was a catalyst for Domain in May. The defeat of the Labor Opposition (which had been favoured by both polls and betting agencies) ended concerns that their policy mix would be implemented. Examples include the removal of negative gearing on existing property. This policy mix in addition to poorer credit growth had weighed on the property market in recent times, reducing the volume of property transactions and consequently weighed on Domain's prospects. A brief resurgence has been seen in borrower activity for recent weeks which has been supportive of the Domain share price.

### Evolution Mining (EVN)

Evolution Mining was supported by a rising gold price amid expectations of an interest rate cut by the US Federal Reserve. In addition, the share price recovered further on a mid-month announcement confirming production guidance for FY19 and offering additional detail on its mining asset base.

### Nine Entertainment Company Holdings (NEC)

Nine benefitted from the uplift in the Domain share price as following its takeover of Fairfax Media it has a 59.2% ownership of the real estate business. It also benefitted following its presentation at the Macquarie Conference highlighting continued growth in more profitable lines of business including 9NOW as well as greater integration to leverage both Domain and other distribution platforms and calling out expectations for its streaming platform Stan to hit breakeven profitability by the end of FY19 (on a quarterly basis).

### Costa Group Holdings (CGC)

Costa Group shares fell following a downgrade to its February guidance where it had called out growth in underlying profit by 30%. Instead it guided towards a range of 0.7% to 16.6% due to a mix of factors such as weaker mushroom costs and the late delivery of fruit and vegetable crops.

### Reliance Worldwide Corporation (RWC)

Reliance Worldwide Corporation also struggled following a downgrade to its FY2019 EBITDA guidance from $280m to $290m to $260m to $270m. The key reason was the lack of a "modest freeze" event in the US this financial year as typically colder weather leads to more

### Nufarm Ltd (NUF)

Nufarm shares struggled in the wake of recent US court verdicts that linked glyphosate to cancer. As a supplier of glysophosate-based herbicides it was seen as a risk by investors. This was confirmed in early June with the company warning that it is at risk of litigation as a result while noting that the considerable global scrutiny could affect future sales.

### Link Administration Holdings (LNK)

Link shares suffered after a results downgrade for the 2019 Financial Year as well as concerns raised for future results as Brexit uncertainty contributed to lower activity in European financial markets. The impact of regulatory change domestically with *The Treasury Laws Amendment (Protecting Your Super Package) Act 2019* has seen some early consolidation affecting FY19, by capping fees on smaller super accounts.

Source: ASX company announcements, Bloomberg, *Australian Financial Review*, *Sydney Morning Herald*

## Movers and Shakers for month of May 2019

| ASX Code | Company Name | Closing price ($) | Month ago, close ($) | Month Δ (%) | Quarter ago close ($) | Quarter Δ ( %) | Year ago, close ($) | Year Δ (%) |
|---|---|---|---|---|---|---|---|---|
| LYC | Lynas Corp Ltd | 3.05 | 1.98 | 54.0 | 1.76 | 73.3 | 2.42 | 26.0 |
| DHG | Domain Holdings Australia Ltd | 3.29 | 2.70 | 21.9 | 2.70 | 21.9 | 3.25 | 1.2 |
| EVN | Evolution Mining Ltd | 3.87 | 3.19 | 21.3 | 3.61 | 7.2 | 3.26 | 18.7 |
| SYR | Syrah Resources Ltd | 1.33 | 1.11 | 19.4 | 1.37 | -3.3 | 3.15 | -57.9 |
| NHF | NIB Holdings Ltd | 6.85 | 5.75 | 19.1 | 5.77 | 18.7 | 5.47 | 25.2 |
| NEC | Nine Entertainment Co Hldgs | 2.08 | 1.75 | 18.9 | 1.71 | 22.0 | 2.41 | -13.7 |
| NST | Northern Star Resources Ltd | 9.71 | 8.19 | 18.6 | 9.25 | 5.0 | 6.27 | 54.9 |
| PLS | Pilbara Minerals Ltd | 0.72 | 0.61 | 18.0 | 0.75 | -3.4 | 0.92 | -21.7 |
| SGP | Stockland | 4.43 | 3.77 | 17.5 | 3.50 | 26.6 | 4.15 | 6.7 |
| VOC | Vocus Group Ltd | 4.59 | 3.91 | 17.4 | 3.70 | 24.1 | 2.41 | 90.5 |

Source: Bloomberg, IOOF

| ASX Code | Company Name | Closing price ($) | Month ago, close ($) | Month Δ (%) | Quarter ago close ($) | Quarter Δ ( %) | Year ago close ($) | Year Δ (%) |
|---|---|---|---|---|---|---|---|---|
| CGC | Costa Group Holdings Ltd | 3.95 | 5.67 | -30.3 | 5.34 | -26.0 | 7.69 | -48.6 |
| RWC | Reliance Worldwide Corp Ltd | 3.67 | 4.88 | -24.8 | 4.51 | -18.6 | 5.75 | -36.2 |
| NUF | Nufarm Ltd | 3.94 | 5.06 | -22.1 | 5.24 | -24.8 | 9.34 | -57.8 |
| BSL | Bluescope Steel Ltd | 10.54 | 13.45 | -21.6 | 13.46 | -21.7 | 17.38 | -39.4 |
| LNK | Link Administration Holdings | 5.97 | 7.60 | -21.4 | 7.60 | -21.4 | 6.86 | -13.0 |
| MYX | Mayne Pharma Group Ltd | 0.56 | 0.70 | -20.7 | 0.70 | -20.7 | 0.78 | -28.4 |
| BAL | Bellamy's Australia Ltd | 8.56 | 10.78 | -20.6 | 8.15 | 5.0 | 17.70 | -51.6 |
| PDL | Pendal Group Ltd | 7.26 | 9.13 | -20.5 | 8.58 | -15.4 | 9.75 | -25.5 |
| TNE | Technology One Ltd | 7.15 | 8.79 | -18.7 | 7.38 | -3.1 | 4.30 | 66.3 |
| IFL | IOOF Holdings Ltd | 5.30 | 6.49 | -18.3 | 6.58 | -19.5 | 8.75 | -39.4 |

Source: Bloomberg, IOOF

## Long-term asset class performance to May 2019 (in AUD)

| | Asset | 1-mth | 3-mth | 6-mth | 1-yr | 3-yr | 5-yr | 7-yr | 10-yr | 15-yr | 20-yr |
|---|---|---|---|---|---|---|---|---|---|---|---|
| | | | | | Annualised | | | | | | |
| Shares | Australia | 1.7% | 4.9% | 15.3% | 11.1% | 10.6% | 7.7% | 11.5% | 10.1% | 8.9% | 8.7% |
| | Australia - mid cap | -0.6% | 2.5% | 10.6% | 3.3% | 10.3% | 12.0% | 13.3% | 11.1% | 9.5% | 9.8% |
| | Australia - small cap | -1.3% | 2.7% | 10.9% | 2.1% | 9.8% | 8.8% | 6.7% | 6.5% | 6.1% | 5.7% |
| | World ex Australia | -4.4% | 1.4% | 6.7% | 8.8% | 10.6% | 12.2% | 16.0% | 11.6% | 6.9% | 4.3% |
| | World ex Australia (Hedged) | -6.0% | -0.7% | 0.8% | 0.6% | 10.0% | 8.4% | 13.3% | 12.8% | 8.6% | N/A |
| | World - small cap | -4.9% | -1.9% | 4.7% | 0.0% | 9.3% | 11.7% | 16.0% | 13.2% | 8.3% | 8.3% |
| | Emerging Markets | -5.8% | -1.9% | 6.8% | -0.3% | 11.5% | 8.0% | 8.9% | 6.6% | 8.5% | N/A |
| | Global Infrastructure | 1.0% | 5.4% | 15.0% | 23.0% | 11.0% | 13.0% | 15.1% | 10.7% | N/A | N/A |
| | Global Infrastructure (Hedged) | -0.4% | 3.5% | 9.3% | 14.3% | 10.1% | 9.5% | 12.6% | 13.9% | N/A | N/A |
| Property | Australian Property | 2.5% | 6.1% | 16.5% | 17.0% | 7.9% | 13.4% | 14.7% | 14.0% | 5.8% | N/A |
| | Global Property | 1.3% | 4.6% | 12.2% | 17.4% | 6.7% | 11.2% | 13.3% | 12.0% | N/A | N/A |
| | Global Property (Hedged) | 1.1% | 4.5% | 2.9% | 15.5% | 8.5% | 8.6% | 10.6% | 16.2% | N/A | N/A |
| Fixed income | Australia Total Market | 1.7% | 3.8% | 7.1% | 9.0% | 4.3% | 5.0% | 4.7% | 5.8% | 6.0% | 6.0% |
| | Australia government bonds | 1.9% | 4.1% | 7.7% | 9.6% | 4.3% | 5.1% | 4.6% | 5.7% | 6.0% | 6.0% |
| | Australia corporate bonds | 1.2% | 3.2% | 5.6% | 7.5% | 4.8% | 5.0% | 5.3% | 6.3% | 6.2% | 6.3% |
| | Australia floating rate bonds | 0.2% | 0.9% | 1.8% | 3.1% | 3.0% | 3.1% | 3.6% | 4.5% | 4.7% | 5.0% |
| | Global Total Market (Hedged) | 1.4% | 3.1% | 5.7% | 6.0% | 3.4% | 4.7% | 5.1% | 6.6% | 6.8% | 6.9% |
| | Global government bonds (Hedged) | 1.6% | 3.1% | 5.4% | 6.0% | 3.2% | 4.9% | 5.1% | 6.3% | 6.7% | N/A |
| | Global corporate bonds (Hedged) | 1.0% | 3.7% | 7.3% | 6.5% | 4.4% | 4.9% | 5.9% | 8.2% | 7.1% | N/A |
| | Global high yield bonds (Hedged) | -0.9% | 0.6% | 5.3% | 4.6% | 6.7% | 5.6% | 8.3% | 11.8% | 9.8% | N/A |
| | Emerging Market bonds (Hedged) | 0.3% | 1.8% | 9.1% | 6.7% | 5.3% | 5.2% | 6.6% | 9.4% | 9.5% | 11.0% |
| Cash | Bloomberg AusBond Bank Bill Index | 0.2% | 0.5% | 1.0% | 2.0% | 1.9% | 2.1% | 2.4% | 3.0% | 4.0% | 4.4% |

**Source:** Bloomberg, IOOF

* AUD total returns as at May-19 assuming reinvestment of dividends

** Returns reflect index performance excluding any fees; Actual ETF/managed fund performance will vary due to both fees and tracking error.

## Appendix – Index sources

| Asset class | Index |
|---|---|
| Australia | S&P/ASX 200 Accumulation Index |
| Australia - mid cap | ASX Accumulation Midcap 50 Index |
| Australia - small cap | ASX Accumulation Small Cap Ordinaries Index |
| World ex Australia | MSCI World ex Australia Net Total Return (in AUD) |
| World ex Australia (Hedged) | MSCI World ex Australia Hedged AUD Net Total Return Index |
| World - small cap | MSCI World Small Cap Net Total Return USD Index (in AUD) |
| Emerging Markets | MSCI Emerging Markets EM Net Total Return AUD Index |
| Global infrastructure | FTSE Global Core Infrastructure 50/50 Net Total Return in AUD |
| Global infrastructure (Hedged) | FTSE Global Core Infrastructure 50/50 100% Hedged to AUD Net Tax Index |
| Australian Property | S&P/ASX 200 A-REIT Accumulation Index |
| Global Property | FTSE EPRA/NAREIT Developed Index Unhedged in AUD Net Total Return |
| Global Property (Hedged) | FTSE EPRA/NAREIT Developed Index Hedged in AUD Net Total Return |
| Australia Total Market | Bloomberg AusBond Composite 0+ Yr Index |
| Australia government bonds | Bloomberg AusBond Govt 0+ Yr Index |
| Australia corporate bonds | Bloomberg AusBond Credit 0+ Yr Index |
| Australia floating rate bonds | Bloomberg AusBond Credit FRN 0+ Yr Index |
| Global Total Market (Hedged) | Bloomberg Barclays Global Aggregate Total Return Index Value Hedged AUD |
| Global government bonds (Hedged) | Bloomberg Barclays Global Aggregate Treasuries Total Return Index Hedged AUD |
| Global corporate bonds (Hedged) | Bloomberg Barclays Global Aggregate Corporate Total Return Index Hedged AUD |
| Global high yield bonds (Hedged) | Bloomberg Barclays Global High Yield Total Return Index Hedged AUD |
| Emerging Market bonds (Hedged) | J.P. Morgan EMBI Global Core Hedged Index Level AUD |
| Cash | Bloomberg AusBond Bank Bill Index |

Research Analyst – Cameron Curko

Approved By – Matt Olsen

**Research Analyst Disclosures:**

I, Cameron Curko, hereby certify that all the views expressed in this report accurately reflect my personal views about the subject investment theme and/or company securities. I also certify that no part of my compensation was, is, or will be, directly or indirectly, related to the specific recommendations or views expressed in this report.

I, Cameron Curko, and/or entities in which I have a pecuniary interest, have an exposure to the following securities and/or managed products mentioned in this report: Nil

**Important Information**

This report is prepared by Bridges Financial Services Pty Limited ABN 60 003 474 977 AFSL 240837 (Bridges). Bridges is an ASX Market Participant and part of the IOOF group of companies.

Bridges and/or its associated entities, directors and/or its employees may have a material interest in, and may earn brokerage from, any securities or other financial products referred to in this document, or may provide services to the company referred to in this report. The document is not available for distribution outside Australia and may not be passed on to any third person without the prior written consent of Bridges. Bridges and associated persons (including persons from whom information in this report is sourced) may do business or seek to do business with companies covered in its research reports. As a result, investors should be aware that the firms or other such persons may have a conflict of interest that could affect the objectivity of this report. Investors should consider this report as a single factor in making an investment decision.

The document is current as at the date of issue but may be superseded by future publications. You can confirm the currency of this document by checking the intranet site (links below).

The information contained in this report is for the sole use of advisers and clients of AFSL entities authorised by Bridges in writing. This report may be used on the express condition that you have obtained a copy of the Bridges Financial Services Guide (FSG) from the website www.bridges.com.au/fsg

**Disclaimer:** The information in this report is general advice only and does not take into account the financial circumstances, needs and objectives of any particular investor. Before acting on the advice contained in this document, you should assess your own circumstances or seek advice from a financial adviser. Where applicable, you should obtain and consider a copy of the Product Disclosure Statement, prospectus or other disclosure material relevant to the financial product before making a decision to acquire a financial product. It is important to note that investments may go up and down and past performance is not an indicator of future performance.

The contents of this report should not be disclosed, in whole or in part, to any other party without the prior consent of Bridges. To the extent permitted by the law, Bridges and its associated entities are not liable for any loss or damage arising from, or in relation to, the contents of this report.

For information regarding any potential conflicts of interest and analyst holdings; IOOF Research Team's coverage criteria, methodology and spread of ratings; and summary information about the qualifications and experience of the IOOF Research Team please visit https://www.ioof.com.au/adviser/investment_funds/ioof_advice_research_process