

# Investment Report – February 2016

The start of the 2016 year has seen sharemarkets fall around the world, mainly due to:

Oil Prices continuing to be weak

Concerns over lower growth in China and potential for the Yuan to fall further

## Oil

Falling oil prices have been increasingly viewed in a negative light by investors. In particular there is a concern that the US economy will slow due to a downturn in oil exploration and production activity.

While the price fell below US\$30, it seemed to find a floor (for now) and bounce back slightly on the hopes of a deal between OPEC countries and Russia to reduce output. There are no immediate signs of this occurring and there is no certainty that oil price lows have been seen.

## Global

A challenging start to 2016 for equities, with US equity markets posting their worst first week of a year on record. The MSCI All Countries World Index (in local currency terms) finished January down 5.4%. Amongst the turmoil, central banks showed the world that they still have firepower—the People's Bank of China provided more than 1.5 million yuan worth of liquidity to local banks, the ECB hinted at more stimulus to come in March, and the Bank of Japan surprised markets with a move to negative interest rates.

## China

Concerns around the prospects for the Chinese economy have grown over the past year. The sharemarket crash in China that began in June is the highest profile example that not everything was going to plan for the Chinese authorities. It is now also widely acknowledged that economic growth has been slowing for some time.

The main event in China now is management of the currency. The Yuan (or Renminbi) was allowed more flexibility in August, which has been a catalyst for weakness since. We understand the Chinese authorities have used substantial foreign exchange reserves to try to ensure that the pace of decline is reasonably gradual.

## USA

US jobs growth remains robust, as the economy added 292,000 jobs in December and 151,000 jobs in January, while the jobless rate fell to a new low of 4.9%. Further interest rate hikes by the US Federal Reserve should now be gradual or they risk hurting already fragile emerging economies, where many companies borrow in dollars.

The head of the International Monetary Fund, Christine Lagarde, said a tightening in US monetary policy, which started in December with the first rate hike in a decade, should be supported by "clear evidence" of inflation in the United States. She also highlighted the negative implications for emerging economies.

## Europe

The European Commission has cut its forecast for economic growth in the Eurozone this year. It has cut its prediction for the 19-country bloc in 2016 to 1.7% from the 1.8% it had forecast in November. That figure would still mark a moderate increase from the figure of 1.6% in 2015.

## Australia

Growing concerns around China, lower commodity prices and mixed domestic data saw investors enter a “risk off phase” during the month. As a commodity dependent country, Australia is closely linked to the fortunes of China, and further uncertainty here placed additional pressure on an already fragile market. Combine this with a negative undertone for equity risk meant the Australian sharemarket experienced one of its worst starts since the turn of the century.

Unlike other markets, Australia is not trading on materially high earnings multiples relative to history. However it is prudent to remain defensive in light of the increased uncertainty.

## New Zealand

The RBNZ left the Official Cash Rate (OCR) unchanged at 2.50%, as expected by almost all economists. The views of market participants are somewhat divided, with some expecting no further rate cuts, and some expecting the OCR to fall as low as 2.00%. In its announcement, the RBNZ noted that, while some further easing may be required, any further moves would be data dependant.

The NZ sharemarket was not immune to the January world market correction. Although the local market has limited exposure to global issues, the negative sentiment surrounding them meant we were caught up in its downward movement. In saying that New Zealand’s defensive characteristic yet again proved beneficial, helping limit its fall; as a result it ended the period as one of the better performers in a global context.

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