Investment Report - December 2013

USA

The improving US growth picture remains a dominant impulse for the world economy.

The economy grew at an annual rate of 3.6% in the third quarter of the year. This was faster than expected and was an improvement on the 2.5% pace seen in the previous quarter. Growth was lifted by rising exports, businesses restocking shelves and a pick-up in home construction. However, the pace of growth in consumer spending, which accounts for about two-thirds of US economic activity, still slowed from the previous quarter.

US jobs growth unexpectedly accelerated in October and November, suggesting that the economy is on a firmer footing and raising the prospect that the Federal Reserve may soon decide to temper its bond-buying stimulus programme. Employers added 204,000 jobs to their payrolls in October and 60,000 more jobs were added to August and September than previously reported. Employers added 203,000 jobs in November and the unemployment rate edged down to 7.0% from 7.3%.

Housing remains a bright spot. In October, housing permits rose to the highest level in more than 5 years, driven by strong demand for multi-family buildings like apartments and condominiums.

China

Recent data showed that industrial output of the world's second largest economy accelerated in October, while retail sales showed solid gains and inflation remained stable. A 10.3% year-on-year gain in production in China's factories, workshops and mines released by the National Bureau of Statistics marked a marginal acceleration from September, when the indicator showed an increase of 10.2%.

China's exports and imports also rose in October. Exports, a key driver of growth, rose 5.6% while imports jumped by 7.6%.

In mid November, the Chinese government unveiled long term economic reform and policy changes. These changes will be felt globally and positively over the next few years e.g. the relaxation of the one-child policy, a reformation of the welfare system, new land ownership rules and new financial market procedures including a freer currency.

Europe

In November, the European Central Bank (ECB) cut its benchmark interest rate to a record low of 0.25%, down from 0.5%. This reflected an outlook of low inflation and general economic weakness in the euro zone. Inflation in the euro zone fell to 0.7% in October, its lowest level since January 2010, stoking concerns of deflation in some countries. The ECB's target is to keep inflation just below 2%, seen as a healthy level for economic growth.

Australia

The Reserve Bank of Australia has forecast below-trend growth and rising unemployment in 2014 as resource investment drops and renewed currency strength drags on the economy, leaving open the possibility of lower interest rates in 2014. Their forecast reflects the substantial fall in mining investment, planned fiscal restraint and the high level of the Australian dollar.

In October, the economy shed the highest number of full-time jobs in 16 months amid the continuing softness of the labour market. The unemployment rate remained steady at 5.7% even as the October figures on the construction industry showed it expended for the first time in three years. Despite this softness, it is likely that the RBA will keep the cash rate on hold at a record level of 2.5% in the short term while housing activity is strong and the cuts already made are still feeding through the economy.

New Zealand

Despite the persistence of an elevated New Zealand dollar and the Reserve Bank's recently introduced high-LVR mortgage restrictions to soften housing market activity, the economy continues to show signs of a recovery building momentum over the second half of the year. Both business and consumer confidence remain robust, household spending is increasing and the housing market activity continues to be supported by a rise in Auckland construction and the on-going Canterbury earthquake rebuild. On the monetary front, it therefore looks likely that interest rate rises will be required in 2014.

Summary

Central banks look likely to continue to support markets with easy monetary policies. Until underlying economic activity improves even more, capital markets will be supported by maximum liquidity.

Reasonable relative valuations, improving GDP growth and growing business and consumer confidence support this constructive view for equities, despite the corrections of recent weeks. Furthermore, there are now clear signs of bond-to-equity switching on a large scale in the US and European mutual fund industries.

We remain relatively positive on equities and target around a 10%+ total return (supported by around a 5% dividend yield and 5%+ earnings growth) over the next twelve months, while we believe that bonds should show better relative value in 2014.

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Peter's disclosure statement is available free of charge upon request.