Investment Report – March 2014

In the first two months of 2014, the growth of world sharemarkets stalled with a sense of crisis over events in the Ukraine (particularly for countries like Germany, due to its reliance on Russian gas) and emerging markets, especially those like Turkey, Indonesia, India, Brazil and South Africa that are highly-indebted and sensitive to international money flows. Nevertheless, we remain optimistic. Sharemarkets have historically performed well in periods of low interest rates, low inflation and strong economic recoveries, where we broadly still find ourselves.

USA

The new chair of the US Federal Reserve, Janet Yellen, said the central bank will continue to cut its stimulatory bond buying measures for the economy gradually, as employment and other economic indicators improve. The current unemployment rate is 6.6% versus 7.9% a year ago. She also said that interest rates would remain historically low. Thus, her inaugural testimony signals that she will continue the supportive policies of her predecessor, Ben Bernanke.

The US economy grew at a much slower rate between October and December last year than originally predicted. The annualised GDP growth rate for the final quarter was downgraded from 3.2% to 2.4%. The downgrade was mainly due to slower consumer spending in the period.

China

China's imports of crude oil, iron ore and copper hit record levels in January, though some of the expected strength was likely to be stockpiling ahead of the Lunar New Year holiday rather than underlying strength in consumption. At the same time, data showed that the value of China's overall imports and exports climbed around 10% from a year ago, raising optimism over the health of the economy after recent weak data.

China's inflation rate remained subdued in January, despite rising food prices during the New Year celebrations. Consumer prices held steady at 2.5% from a year earlier.

However, in early March, China's Purchasing Managers' Index numbers for February were released and they were at a level of 50.2, lower than January's 50.5, adding to signs of a factory slowdown. A number above 50 signals expansion. However, the numbers may have been detrimentally affected by the Chinese New Year holidays. The data underscore the challenges facing the government as it tries to sustain growth above 7% while reining in credit, boosting jobs and curbing social unrest

Europe

The euro zone's economy grew by 0.3% in the last three months of 2013, up from 0.1% growth in the previous quarter. It was the third quarter of growth since the end of an 18-month recession, the longest period of contraction to affect the single currency area. The cloud on Europe's horizon is the continuing weakness in inflation, which the central bank is prepared to look through at present.

Japan

Japan's economy grew less than expected at the end of last year. GDP grew by 1% on an annualised basis in the 3-month period to December 2013, compared with market estimates of a 2.8% increase. This was due to weaker private consumption and capital spending as well as lower export figures. However, this was Japan's fourth straight quarterly expansion and the BOJ is still pursuing stimulatory asset purchases and lending policies. Retail sales rose 4.4% in January from a year earlier.

Australia

In early March, the Australian Reserve Bank (RBA) said that earlier interest rate cuts were having the desired impact on the economy and left the official rate unchanged. The RBA acknowledged that the transition away from mining investment was proving difficult and that unemployment could still rise, but it also saw reason for optimism.

"Recent information suggests slightly firmer consumer demand and foreshadows a solid expansion in housing construction," the central bank's governor, Glenn Stevens, said in a brief statement after the bank's March policy meeting.

"Some indicators of business conditions and confidence have shown improvement, and exports are rising." he added. "Over time, growth is expected to strengthen, helped by continued low interest rates and the lower exchange rate."

New Zealand

Recent economic data remains consistent with undeniably strong domestic economic momentum. Business sentiment in particular rose to a 20-year high, labour market data for the 4Q13 further confirmed the economic backdrop is spilling over into better employment outcomes with the unemployment rate falling to a 4.5-year low, and manufacturing activity remains solid.

New Zealand posted its third straight surplus on its terms of trade in January, as sales of dairy products to China cemented its status as our largest market. The terms of trade now stand at a 40-year high. China accounted for 30% of all exports in January, up from 19% a year ago.

While the current strong economic momentum is expected to be a boon for New Zealand company earnings in 2014, interest rate rises pose a risk for some sectors of the equity market.

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