Investment Report – February 2015

The World Bank has cut its forecast for global growth in 2015 due to a faltering recovery in the euro zone, tighter monetary policy in developed countries and the prospect of a slowdown in emerging markets. The World Bank is forecasting global growth of 3% this year, down from a 3.2% prediction in October, which was also revised down from 3.4% in June last year. The downward revisions come despite an expected boost to global growth from the lower oil prices.

USA

We still expect solid economic growth in 2015 in the US, even with the likelihood of a Federal Reserve tightening during the year, as well as very low inflation.

US retail sales slumped in December, falling 0.9 per cent, despite cheaper petrol prices and falling unemployment.

US producer prices in December recorded their biggest fall in more than three years on tumbling energy costs. The producer price index for final demand declined 0.3%, the biggest drop since October 2011, while consumer prices fell in December by the largest amount in six years, reflecting another big monthly decline in gas prices and providing further evidence of falling inflation pressures. The consumer price index dropped 0.4%, the biggest one-month drop since December 2008.

A gauge of US business investment plans fell for a fourth straight month in December, a potential sign that slowing global growth and falling oil prices were weighing on the economy. Other data released, however, suggested any damage would be limited. Consumer confidence vaulted to a near 7-1/2 year high in January and new home sales in December hit their highest level since June 2008.

China

China is midway through its major structural reforms. Its economy grew at its slowest pace in almost a quarter of a century in 2014, as the country's leaders warned further downward pressure remained on the economy.

China's gross domestic product (GDP) expanded by 7.4% in 2014, down from 7.7% growth in 2013. It beat consensus analyst estimates of 7.3% but fell short of the Communist Party's official target for the year of "around" 7.5%. GDP also expanded 7.3% year-on-year in the fourth quarter of last year, holding steady from the previous quarter.

The country's overheated real estate market is also expected to slow further this year, putting further pressure on global iron ore prices already reeling from the effects of over-supply.

Europe

In January, as expected, the European Central Bank (ECB) announced a massive quantitative easing programme to counter deflationary conditions there. It said that it would now purchase 60 billion euros a month of assets until September 2016 and reduce the cost of its long-term loans to member banks. In addition, the central bank will kept its interest rates at record lows.

Japan

Japan struggled in 2014 with its economy never recovering from a large sales tax increase in April. While 2015 growth will be better, the recovery will still struggle to generate anything near self-sustaining growth.

Australia

The Australian economy looks set to continue recording below trend growth well into 2015. Its share market has been a poor relative performer in recent months, with falling commodity prices due to slowing Chinese demand and increased regulatory requirements for banks behind its lack of support.

The Reserve Bank of Australia unexpectedly lowered the official cash rate from 2.5% to 2.25% in early February. This may well be the recipe which may reignite a cautious consumer and provide a lever for economic growth in the absence of any near term improvement to iron ore and other commodity prices.

New Zealand

Economic data released over the past month suggest that growth momentum, while slowing continues to remain above trend.

Supportive factors have included a robust increase in building consents, an upturn in the rate of growth in house prices and sales, historically high levels of net migration, together with an upturn in consumer sentiment. Offsetting these positive factors, the negative effect of the sharp decline in dairy auction prices has increasingly been in evidence through a fall in broader commodity price indices and a worsening NZ terms of trade.

Despite the pace of economic activity remaining above trend, domestic inflationary pressures remain subdued. The December quarter consumer price index fell by -0.2% to give an annual result of only +0.8% and, in late January, the Reserve Bank left interest rates unchanged.

Summary

Central banks look likely to continue to support markets with easy monetary policies through most of 2015. Inflation is virtually non-existent, so interest rates need not rise in the short term.

This scenario still supports a constructive case for buying selected shares, at least until interest rates begin to rise to make bonds more attractive. However, many asset classes are nearing full value and it is now becoming harder to find good investment opportunities.

A diversified approach to investment, as always, remains appropriate. Moreover, as all sharemarkets have risen strongly over the last few years, we continue to encourage investors to reflect upon their portfolios which may have drifted away from their benchmark ratios due to the strong share returns of recent years.