Market Update

November 2010

- **Local economy's strong performance prompts RBA to lift cash rate to 4.75%**
- **In Europe, the German economy continues to outperform expectations but concerns over smaller European economies persist**
- **AUD hits parity and 28 year high against USD**

What's inside?

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The pulse

↑ **Australian cash rate**
0.25% to 4.75%

↑ **AUD/USD**
1.6 US cents to 98.35 US cents

October market performance

Equity Markets – Price Indices	Index	At Close 31/10/2010	% Change 1 Month	% Change 12 Months
Australia	All Ordinaries	4733.41	2.08%	1.86%
Japan	Nikkei	9202.45	-1.78%	-8.29%
Hong Kong	Hang Seng	23096.32	3.30%	6.18%
UK	FTSE 100	5675.16	2.28%	12.50%
Germany	DAX	6601.37	5.98%	21.91%
US	Dow Jones	11118.49	3.06%	14.47%
EMU [1]	Euro 100	2274.11	2.52%	9.23%
World [2]	MSCI – Ex Aus (Gross)	854.95	2.82%	9.86%
Property – Price Index	**Index**	**At Close 31/10/2010**	**% Change 1 Month**	**% Change 12 Months**
Listed Trusts	S&P/ASX 300 A-REIT	847.56	-0.48%	-1.79%
Interest Rates		**At Close 31/10/2010**	**At Close 30/9/2010**	**At Close 31/10/2009**
Aust 90 day Bank Bills		4.87%	5.01%	3.94%
Australian 10 year Bonds		5.20%	4.96%	5.62%
US 90 day T Bill		0.11%	0.16%	0.05%
US 10 year Bonds		2.60%	2.51%	3.38%
Currency		**At Close 31/10/2010**	**% Change 1 Month**	**% Change 12 Months**
US dollar	A$/US$	0.98	1.69%	9.31%
British pound	A$/STG	0.61	-0.34%	12.08%
Euro	A$/euro	0.71	-0.52%	15.46%
Japanese yen	A$/yen	79.09	-2.09%	-2.44%
Trade–weighted Index		72.70	-0.27%	2.83%

1 Top 100 European stocks trading on the FTSE
2 Price Index – Source: www.msci.com
Source: Iress Market Technology
Past performance is not a reliable indicator of future performance.

Global economies

The Australian economy continues to outperform expectations with key data showing a pattern of strong performance into this financial year.

The latest NAB business surveys for September show the economy has been growing at an average to above-average rate over the past month or two. The NAB Business Conditions Index level in September was up slightly from August's level and is consistent with annual growth in domestic demand of between 3.5% and 4%.

Other key economic indicators were also positive with business confidence slightly above its long-term average and consumer sentiment up 3.3% over the month of September. This puts sentiment at levels consistent with healthy growth in retail and consumer volumes.

The reinvigorated resources sector continues to be a star performer for Australia, boosted by this year's increases in iron ore and coal prices. The Reserve Bank of Australia (RBA) Governor, Glenn Stevens, recently referred to it as the largest resources boom since the 19th century.

With the economy transitioning from fiscal support to private demand, the job market remained strong into September. Forward measures of labour demand point to continued high levels of demand for the next quarter or so. Recent jobless data released on 11 November, however, saw the jobless rate rise due to a stronger participation rate but the outlook for employment remains positive.

In what's seen as one of the strongest indicators of the strengthening economy, the RBA lifted the cash rate in November by 0.25%, taking it to 4.75%.

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In US economic news, the forward estimates of Gross Domestic Product (GDP) for the September quarter rose by 2% following a rise of 1.7% in the June quarter.

While the GDP result was positive, inventory purchases added 1.4% of the 2% GDP rise, sales only added 0.6%. With housing activity turning negative again and consumer spending growth soft, doubts still persist about how soon the US can fully recover.

Also of concern are the high levels of US housing debt, an oversupplied housing market, and vulnerable house prices.

On 3 November the Federal Open Markets Committee (FOMC) announced additional quantitative easing (QE2). This means the Federal Reserve (Fed) will buy substantial amounts of Treasury securities to try and increase their price and thereby lower market interest rates (such as US mortgage rates and business lending and capital market rates). The end result is to put more money in the hands of consumers and boost domestic spending.

In justifying the move, the Fed stressed the importance of inflation as a trigger for the additional stimulus, saying "measures of underlying inflation have trended lower in recent quarters". Although the Fed said inflation expectations "have remained stable", the fear is they will fall, a pre-condition for deflation.

In other economic news China's level of growth over the September quarter fell to 9.6% from 10.3% in the previous quarter. This was still slightly ahead of expectations though, which were for 9.5% growth.

September reports on retail sales, industrial production and fixed assets investment revealed mixed growth momentum for the Chinese economy. There was a pick-up in retail sales but some moderation in growth of industrial production and investment in fixed assets such as infrastructure.

In Europe economic growth remains mixed. While the German economy continues to outperform expectations, continuing concerns about some of the smaller economies, such as Ireland, have adversely impacted market sentiment.

On a positive note, ratings agency Standard and Poors revised the sovereign credit rating outlook for the UK from negative to stable in the wake of the UK Government's latest fiscal consolidation program.

Big movers this month

↑ Materials +5.6%

↓ Property -0.4%

Equity markets

October was another good month for equity markets with global equities, commodities and commodity currencies, such as the Australian dollar, making good gains.

Australian equities

	Index/Benchmark	1 Yr	3 Yrs	5 Yrs	7 Yrs
Australian	S&P/ASX 300 Acc.	4.67%	-7.64%	5.36%	9.77%
	S&P/ASX 50 Acc.	4.04%	-6.69%	5.82%	9.91%
	S&P/ASX Small Ordinaries Acc.	11.47%	-10.06%	4.91%	9.25%

The Australian market, as measured by the S&P/ASX 300 Accumulation Index, finished the month up 1.84%. Although positive, the Australian market's gains lagged the US market's gains.

Reflecting the increase in investor risk appetite, the S&P/ASX Small Ordinaries Accumulation Index gained 3.31% over the month.

Sector trends in the Australian market over 2010 have been varied. For example, returns for materials to the year ending October have been strong, returning 20%, while Financials have fallen 3.3%.

The banks did well until May, when the Greek sovereign debt crisis struck. Then funding costs, especially for offshore issues, took a big hit and the banks haven't really recovered since.

Mining companies have done well since the election in August and the resolution of the mining tax issue. By the end of October, the resources sector was up by 20% for the year and looking as though it could exceed the previous 2010 high reached in April.

Sector	1 Mth	3 Mths	1 Yr
Energy	1.6%	5.8%	-0.8%
Materials	5.6%	11.4%	20.0%
Industrials	1.3%	11.4%	2.1%
Consumer Discretionary	1.3%	4.8%	1.2%
Consumer Staples	-0.1%	9.8%	11.3%
Health Care	-0.2%	2.4%	0.5%
Financials	0.1%	1.5%	-3.3%
Info Tech	3.3%	2.4%	-4.4%
Telcos	1.9%	-11.5%	-11.5%
Utilities	1.0%	9.6%	13.0%
Property	-0.4%	2.3%	4.5%

Global equities

	Index/Benchmark	1 Yr	3 Yrs	5 Yrs	7 Yrs
Global	MSCI World Ex Aus Acc. ($A)	3.94%	-9.90%	-3.12%	0.50%
	MSCI World Index Hedged ($A)	12.00%	-9.85%	-0.13%	3.84%
	MSCI World Small Cap ($A)	13.21%	-6.23%	-1.29%	3.28%
Emerging	MSCI Emerging Mkts Free	13.90%	-5.76%	8.86%	12.72%
	MSCI AC Far East Free (ex Japan)	12.37%	-6.89%	8.23%	9.04%

One of the key drivers of the US and global markets over the past month was increased conviction among traders that the Federal Reserve was laying groundwork for a second round of quantitative easing (QE2). This saw bond yields fall and equity markets rally. For example, the Dow Jones Industrials Index rose 3.06% over October.

The ensuing announcement of QE2 on 3 November was, however, only greeted with a mildly positive reaction by equity markets in the end. Nevertheless, the Fed hasn't ruled out further quantitative easing to further reinforce the recovery and this has gone some way to supporting the outlook for the US equity market.

Elsewhere, most major global markets gained in October on the back of the anticipated US QE2. Japan, however, was the exception, finishing the month down 1.78% as their strong currency (Yen) continues to hamper their large export dominated markets.

Overall, the MSCI World (ex-Australia) Index in $A terms and MSCI World Small Cap Index in $A terms gained 2.5% and 2.69% respectively over October. Reflecting the strength of the Australian dollar, the MSCI World Index Hedged outperformed the unhedged equivalent, gaining 3.11%.

Emerging Markets also finished the month strongly with the MSCI Emerging Markets Index and MSCI Far East Free (ex-Japan) Index gaining 1.65% and 1.51% respectively during October.

Property

	Index/Benchmark	1Yr	3 Yrs	5 Yrs	7 Yrs
Australian	S&P/ASX 300 A-REIT Acc	4.51%	-24.63%	-8.11%	-0.75%
Global	UBS Global Investors ($A)	18.37%	-11.14%	-3.52%	N/A

Australian property continues to underperform the equity markets and their global property counterparts. The S&P/ASX 300 A-REIT Accumulation Index fell 0.48% in October compared to a gain of 3.22% for global property as measured by the UBS Global Investors Index.

Fixed interest

	Index/Benchmark	1 Yr	3 Yrs	5 Yrs	7 Yrs
Australian	UBS Composite 0 + Years	7.42%	7.61%	6.16%	6.16%
	Australian 90 Day Bank Bill	4.51%	5.14%	5.56%	5.56%
Global	BarCap Global Aggregate Index	-1.47%	5.25%	0.75%	2.43%
	BarCap Global Ag. Index Hedged	10.84%	9.73%	8.20%	7.69%

Australian and global fixed interest was relatively flat over October with all major fixed interest indices, hedged and unhedged, making small gains.

The Barclays Capital (BarCap) Global Aggregate Index was up 0.02% with the hedged equivalent up 0.29%. Australian Bonds as measured by the UBS Composite Bond Index was unchanged.

Australian dollar (AUD)

After much speculation over the past year, the AUD/USD traded up to parity on October 15. This was a post-float high and the strongest level in 28 years at the time. It was propelled higher by a number of factors including:

- an anticipation of further quantitative easing by the US Federal Reserve at the November 2–3 FOMC meeting, which did eventuate.
- heightened speculation of RBA interest rate increases over the coming year; and
- upbeat Asian economic reports which helped fuel gains in stocks and commodities.