March 2014

US data continues to show that although growth momentum has moderated, due in part to the severe weather at the start of the year, the level of growth remains robust. The recovery in the labour market continued at a gradual pace with non-farm payrolls coming in at 192,000 in March. Although this was below consensus expectations, the participation rate hit a 6-month high at a seasonally adjusted 63.2%, while net revisions for the previous two months were up 37,000. Manufacturing activity, as measured by the PMI and ISM indexes, also remains at healthy levels, despite both gauges missing expectations.

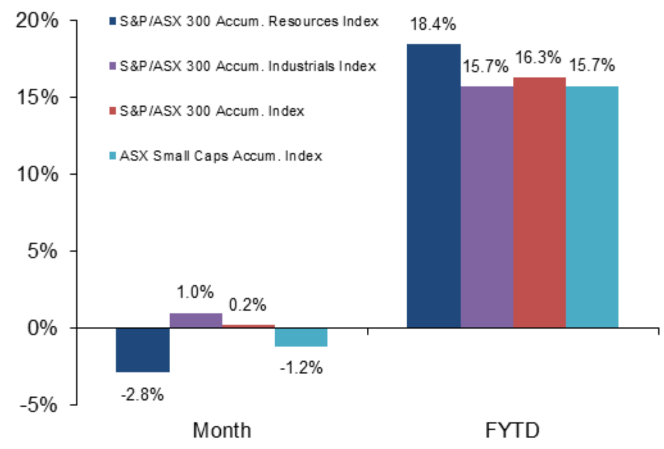
In its March meeting, the Federal Open Market Committee (FOMC) further curtailed its quantitative easing (QE) program by reducing the pace of its purchases of mortgage-backed and Treasury securities by a total of USD10 billion per month. Although the reduction was largely expected, there was a shift in the Fed's guidance. The previously cited 6.5% unemployment rate figure (a trigger for when the first increase in interest rates would likely occur) was replaced with a more qualitative assessment of labour market conditions, inflation and financial developments. The shift represents an evolution in the long road to interest rate normalisation, but also hints at the difficulty in gauging the health of the labour market using the unemployment rate alone.

In China, the official manufacturing PMI edged up to 50.3, reinforcing the view that growth prospects in the country remain relatively weak. Days earlier, authorities announced targeted stimulus measures to provide a degree of support to the economy. Existing tax breaks for small businesses were extended, while social housing and railway construction projects were accelerated. The move is emblematic of the difficulty policymakers face in balancing the need to maintain sufficient economic growth with encouraging the transition to a more consumption driven and less credit intensive model of growth. Earlier in the month, China's credit growth and shadow banking issues gained significant coverage as speculation mounted that its domestic corporate bond market would experience its first default. While it did eventuate, fears this would spark a domino effect seem exaggerated given the company specific issues at play. However, this is unlikely to be an isolated incident given the pace at which the market has grown in recent years. Positively, in the medium-long run at least, there were no signs of an investor bailout although credit growth remains a key risk in China.

Data out of Europe showed economic activity continued to expand in the region. The manufacturing and services PMIs came in at 53.0 and 53.1 in March, just missing expectations, but holding firmly in expansionary territory. More worryingly for policymakers is inflation or lack thereof. The "flash" harmonised measure of consumer prices showed inflation slowed to 0.5% y/y in March, below the expected rate of 0.7%. In response, the European Central Bank left interest rates on hold, but released a statement expressing its "unanimous" commitment to use "unconventional" means to deal with too-prolonged a period of low inflation. Peripheral European government bond yields rallied significantly in response.

In Australia, the Reserve Bank left interest rates on hold as expected, signalling that monetary policy was likely to remain in a holding pattern for the foreseeable future. After the decision, the March labour force survey showed the unemployment rate unexpectedly fell to 5.8% after an additional 18,100 jobs were created.

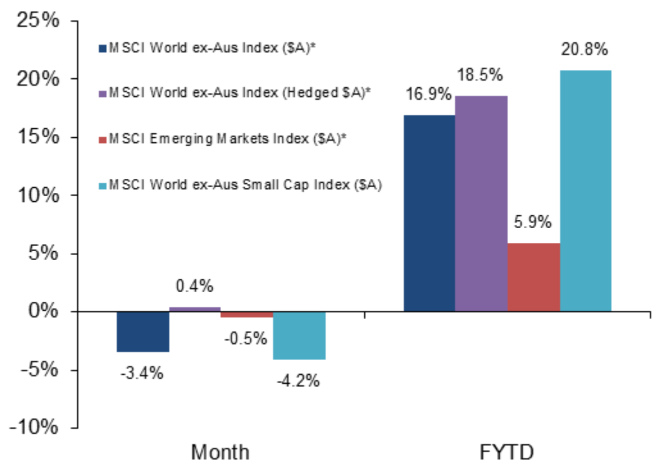
Australian equities



Australian equities, inclusive of dividends, ground out a slight positive return over March. Industrials significantly outperformed Resources as the latter was impacted by a steep fall in bulk commodity prices, particularly iron ore. At the sector level, Utilities was the next biggest loser after Materials, falling by 3.0%, while Financials were the clear winner, gaining 2.3% over the month.

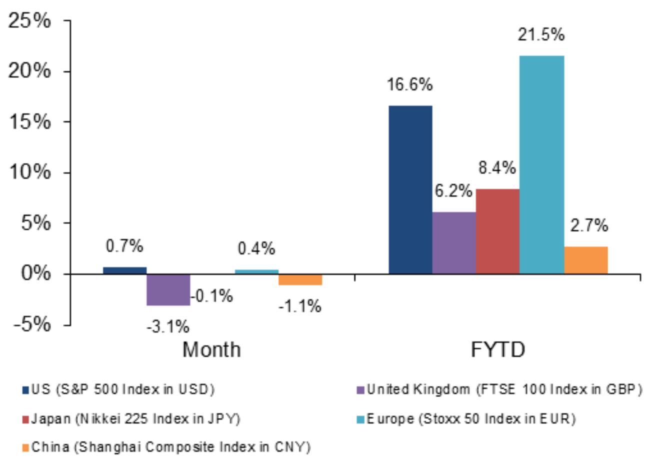
The underperformance of small caps relative to broad caps was driven by the significant (-6.1%) loss in small cap resources.

International equities ($A)



Although underlying equity market performance was broadly positive, unhedged developed market equities gave up significant ground in March due to a strongly rising Australian dollar. It was a similar story in emerging markets as a strong rebound in some of the most heavily sold off markets in recent times such as Turkey and Brazil, was more than offset, for Australian investors, by the impact of the dollar. Unsurprisingly, the benchmark hedged developed market equities index was the only one to record a positive return over the month.

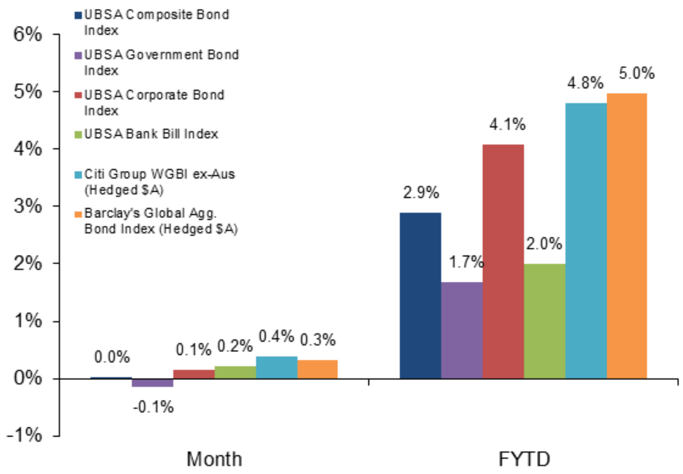
International equities (local currencies)



Peripheral European equity markets continue to lead the way, with local Italian and Spanish equities recording the largest gains over the month amongst the major developed markets. In the US, the S&P 500 closed in on its all-time record high as March came to an end, with the record being broken two days later. Of the major developed markets, the UK was the most significant underperformer, falling by 3.1%.

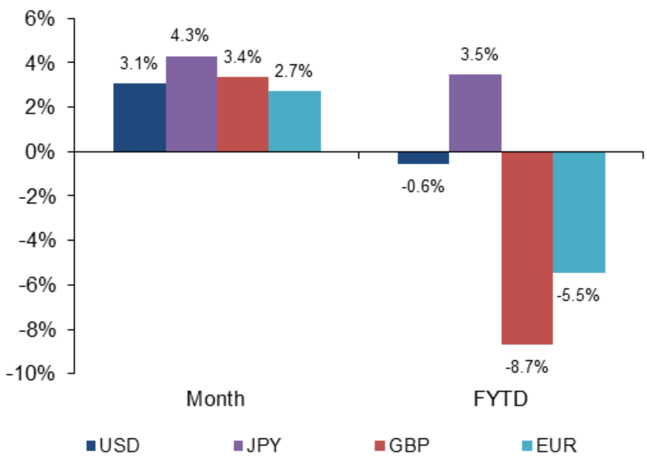
In emerging markets, the local market in China was one of the few to fall in March as concerns over growth and corporate defaults contributed to a mild sell off.

Fixed income



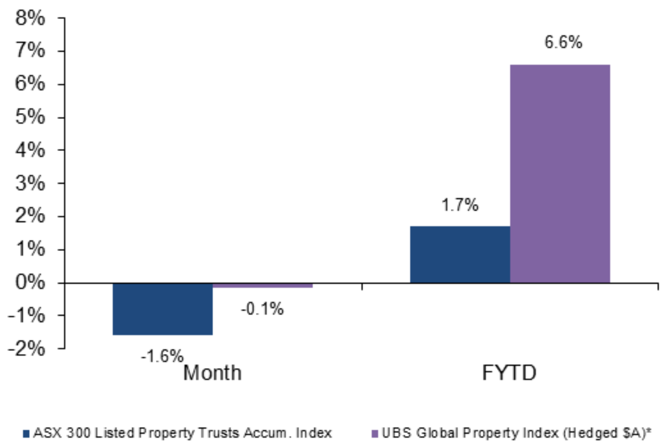
Australian fixed interest, as measured by the UBSA Composite Bond Index, struggled to generate a positive return in March as Australian government bond yields increased over the month. It was a similar story in the US and UK. A combination of higher growth and revised expectations of the first increase in official interest rates saw an increase in yields, particularly in the short and intermediate end of the curve. These moves were offset by the continued decline in peripheral European government bond yields.

Australian dollar against major currencies



The Australian dollar finished March at its highest level in 2014 against the major currencies. While the RBA's decision to leave official interest rates unchanged was largely expected, the accompanying monetary policy statement failed to mention an "uncomfortably high" Australian dollar. The Dollar was also spurred on by revised expectations for the path of monetary policy following the positive economic releases in recent months. Later in the month, expectations of targeted stimulus measures in China drove the dollar higher.

Property



Australian listed property declined over March, underperforming their hedged international listed property counterparts. However, much of this can be explained by the increase in the Australian dollar over the month.

Over the financial year to date, Australian listed property continues to significantly underperform international listed property.

31 March 2014	Index value	Month	3 months	FYTD	1 year
Australian equities					
S&P/ASX 300 Accum. Index	44,965	0.2%	2.0%	16.3%	13.0%
S&P/ASX 300 Accum. Industrials Index	87,227	1.0%	2.7%	15.7%	15.3%
S&P/ASX 300 Accum. Resources Index	21,594	-2.8%	-0.8%	18.4%	4.6%
ASX Small Caps Accum. Index	5,451	-1.2%	0.9%	15.7%	-1.5%
International equities					
MSCI World ex-Aus Index ($A)*	5,294	-3.4%	-2.4%	16.9%	34.7%
MSCI World ex-Aus Index (Hedged $A)*	1,074	0.4%	1.5%	18.5%	21.5%
MSCI Emerging Markets Index ($A)*	441	-0.5%	-3.9%	5.9%	10.9%
MSCI World ex-Aus Small Cap Index ($A)	353	-4.2%	-1.1%	20.8%	38.0%
US (S&P 500 Index in USD)	1,872	0.7%	1.3%	16.6%	19.3%
United Kingdom (FTSE 100 Index in GBP)	6,598	-3.1%	-2.2%	6.2%	2.9%
Japan (Nikkei 225 Index in JPY)	14,828	-0.1%	-9.0%	8.4%	19.6%
Europe (Stoxx 50 Index in EUR)	3,162	0.4%	1.7%	21.5%	20.5%
China (Shanghai Composite Index in CNY)	2,033	-1.1%	-3.9%	2.7%	-9.1%
AUD versus …					
USD	0.92	3.1%	3.1%	-0.6%	-11.6%
JPY	94.83	4.3%	0.9%	3.5%	-3.3%
GBP	0.55	3.4%	2.1%	-8.7%	-19.5%
EUR	0.67	2.7%	3.4%	-5.5%	-17.8%
Property					
ASX 300 Listed Property Trusts Accum. Index	27,705	-1.6%	3.0%	1.7%	5.0%
UBS Global Property Index (Hedged $A)*	1,733	-0.1%	6.9%	6.6%	4.2%
Australian Fixed Interest					
UBSA Composite Bond Index	7,710	0.0%	1.5%	2.9%	3.3%
UBSA Government Bond Index	7,998	-0.1%	1.2%	1.7%	1.5%
UBSA Corporate Bond Index	7,925	0.1%	1.5%	4.1%	5.1%
UBSA Bank Bill Index	8,011	0.2%	0.6%	2.0%	2.8%
Global Fixed Interest					
Citi Group WGBI ex-Aus (Hedged $A)	-	0.4%	2.7%	4.8%	3.8%
Barclay's Global Agg. Bond Index (Hedged $A)	-	0.3%	2.7%	5.0%	3.7%
Oil and commodities					
Crude Oil ($/bbl)	102	-1.0%	3.2%	5.2%	4.5%
Copper Spot ($/tonne)	6,650	-6.1%	-9.8%	-1.2%	-11.4%
Gold Spot ($/ounce)	1,284	-2.9%	6.7%	4.4%	-20.0%

Fixed income (yields) as at …	**31-Mar-14**	**28-Feb-14**	**31-Dec-13**	**30-Jun-13**	**31-Mar-13**
Australia Bank Bill	2.65	2.62	2.60	2.79	3.04
Australia 10 Year Government Bond	4.09	4.02	4.24	3.76	3.41
US 10 Year Government Bond	2.72	2.65	3.03	2.49	1.85
UK 10 Year Government Bond	2.74	2.72	3.02	2.44	1.77
Germany 10 Year Government Bond	1.57	1.62	1.93	1.73	1.29
Japan 10 Year Government Bond	0.64	0.59	0.74	0.85	0.55

* Net dividends reinvested