



Market Movements Update

29 October 2018

SUMMARY

- Financial markets have experienced an increase in volatility since late September. This short note provides an update on financial market movements and the potential causes
- Our current analysis suggests the global economic and financial environment remains solid. The US economy and corporate earnings in particular, appears to be strong
- Similar to the February market correction, the recent market movement appears to have been triggered by an increase in the US 10 year bond yield, expectation of accelerating US wage growth/inflation and US monetary policy tightening
 - The September Federal Open Market Committee monetary policy meeting removed “accommodative policy” from its statements although continued to state the positive strength in the US economy
- As we highlighted earlier in the year, a market sell down of the magnitude of -10% is not uncommon, particularly after periods of strong performance, in fact it is the average drawdown in a year
 - The S&P 500 had returned nearly 15% from March to September 2018, so some retracement is not surprising
 - However, developed and Australian equities returns are now negative for the calendar year to date (in local currency terms)
- The recent market movements have not materially impacted our Dynamic Asset Allocation (DAA) views. Clients can find our latest DAA views published in the *Quarterly Market Outlook (QMO)*

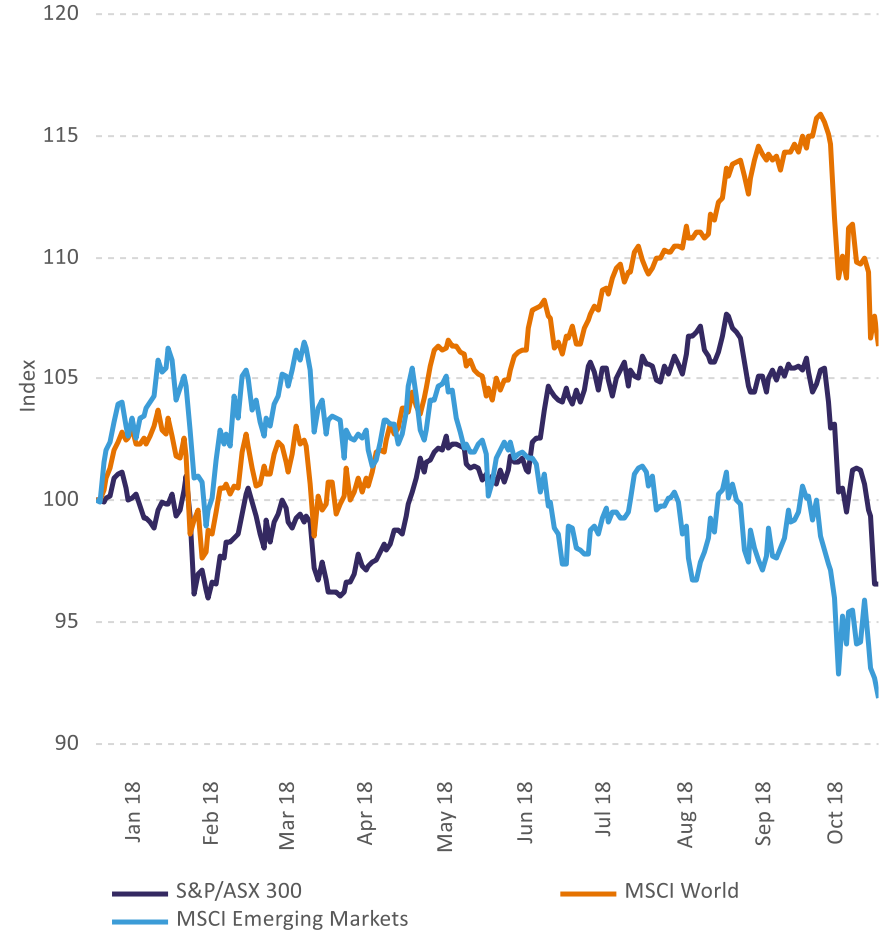
DEVELOPED MARKET AND AUSTRALIA EQUITIES ARE NOW NEGATIVE FOR CALENDAR YEAR TO DATE AFTER MARKET DECLINE

Regional Equities Performance in Local Currency



Source: Thomson Reuters Datastream

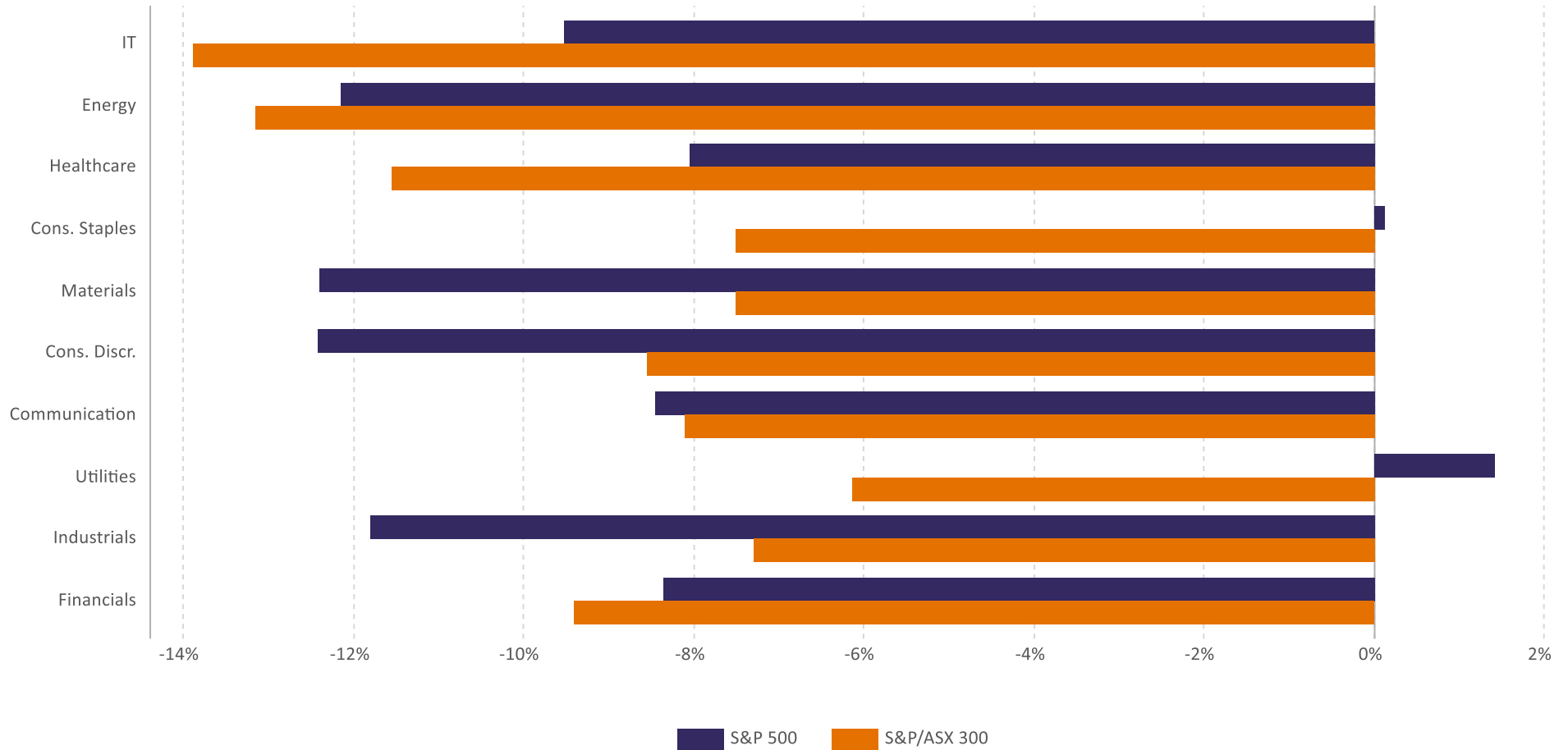
Regional Equities Performance (A\$)



Source: Thomson Reuters Datastream

BROAD-BASED MARKET FALL WITH GROWTH/CYCLICAL SECTORS PERFORMING THE WORST

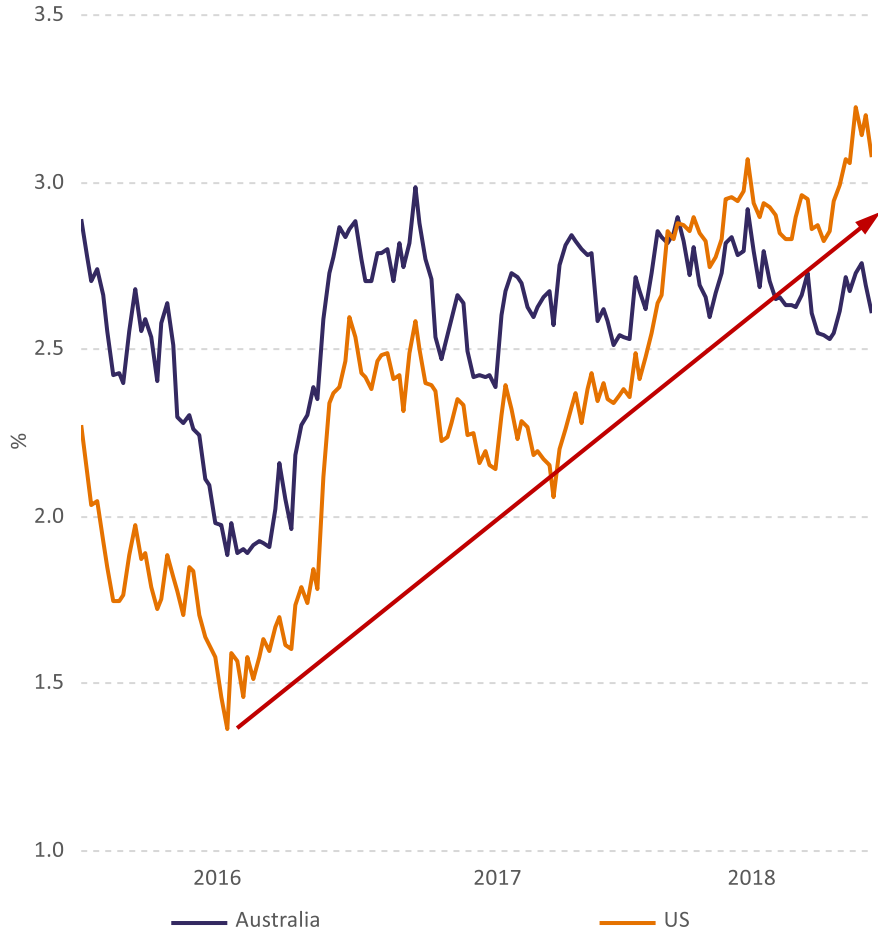
S&P500 and ASX300 Sector Month To Date Performance at 26 Oct 2018



Source: Thomson Reuters Datastream

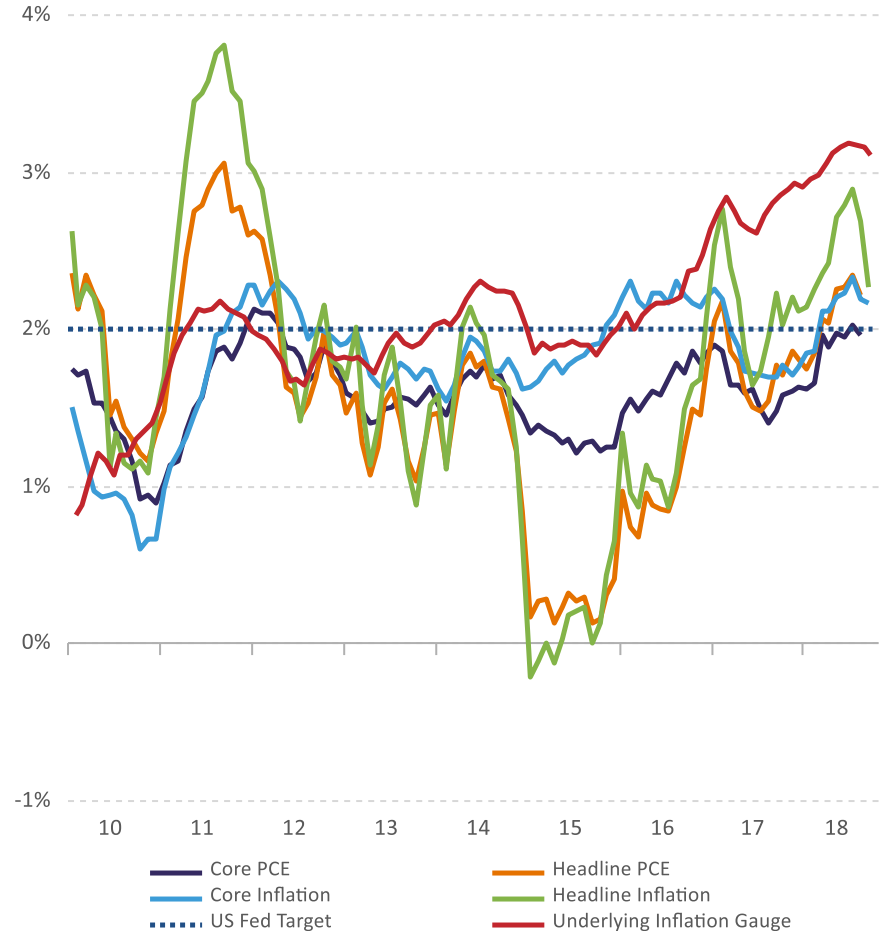
RECENT SPIKE IN US BOND YIELDS PART OF UPWARD TREND SINCE MID 2016 DRIVEN BY INCREASING US INFLATION AND GROWTH

10 Year Government Bond Yields



Source: Thomson Reuters Datastream

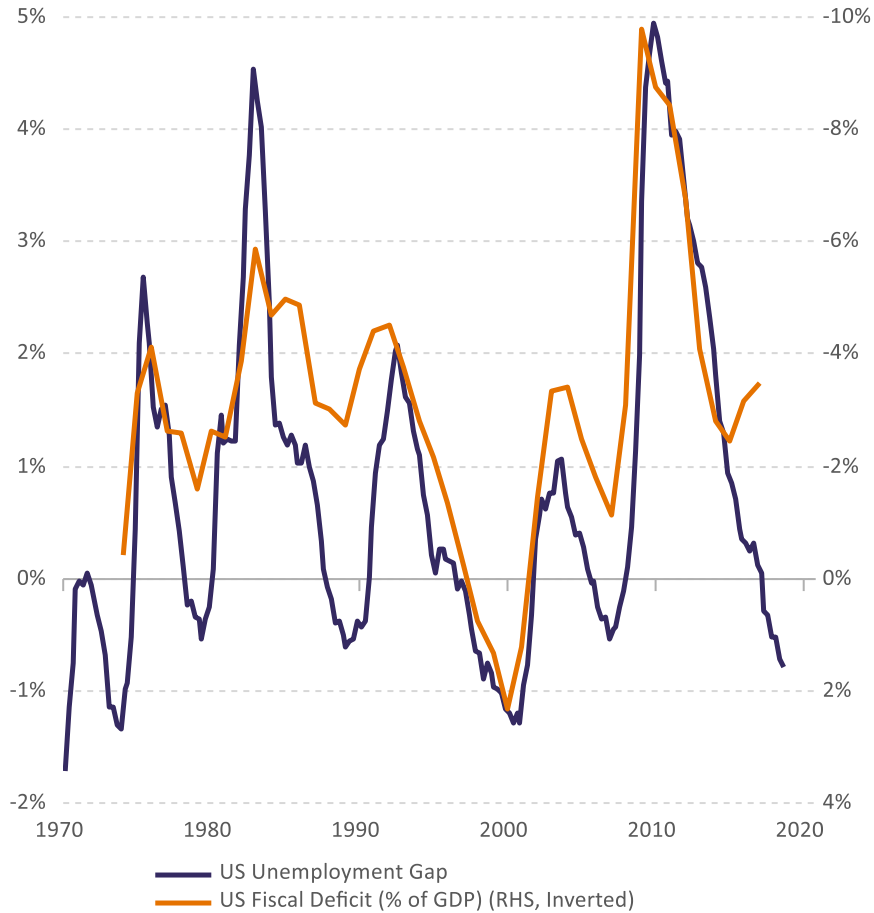
US Inflation Measures 12 Mth Growth



Source: Thomson Reuters Datastream, BEA, FRBoNY

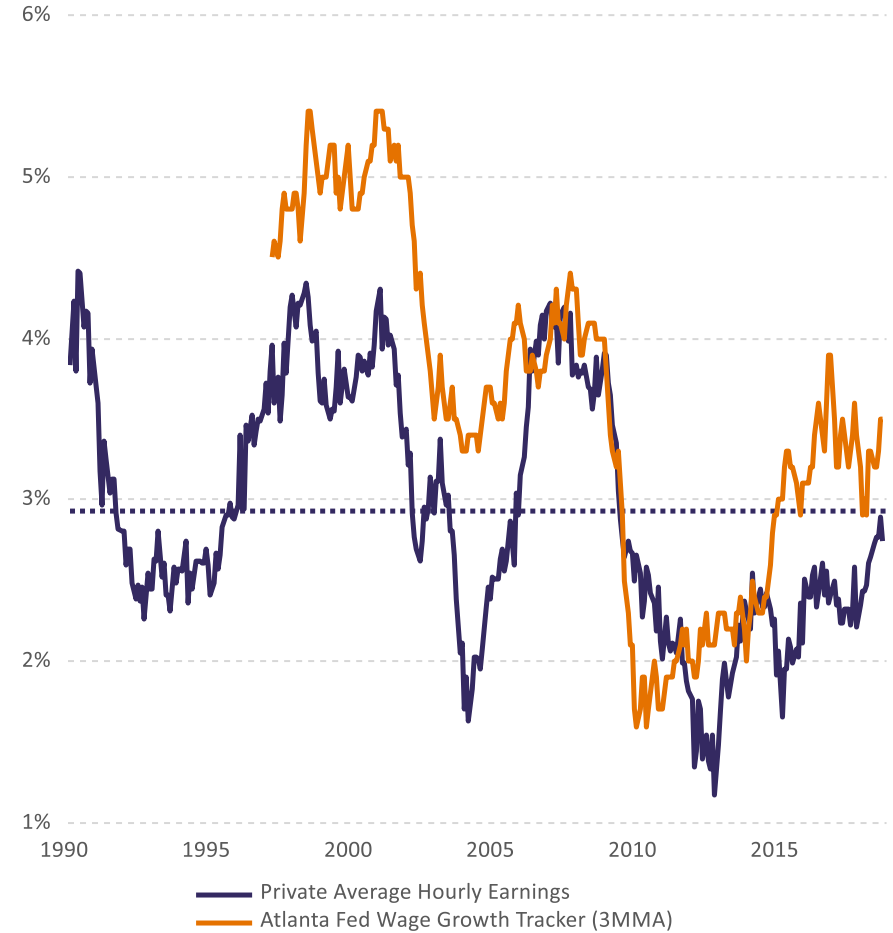
US ECONOMY REMAINS STRONG WITH BOOST FROM FISCAL STIMULUS

US Fiscal Deficit and Unemployment



Source: Thomson Reuters Datastream, BLS, CBO US

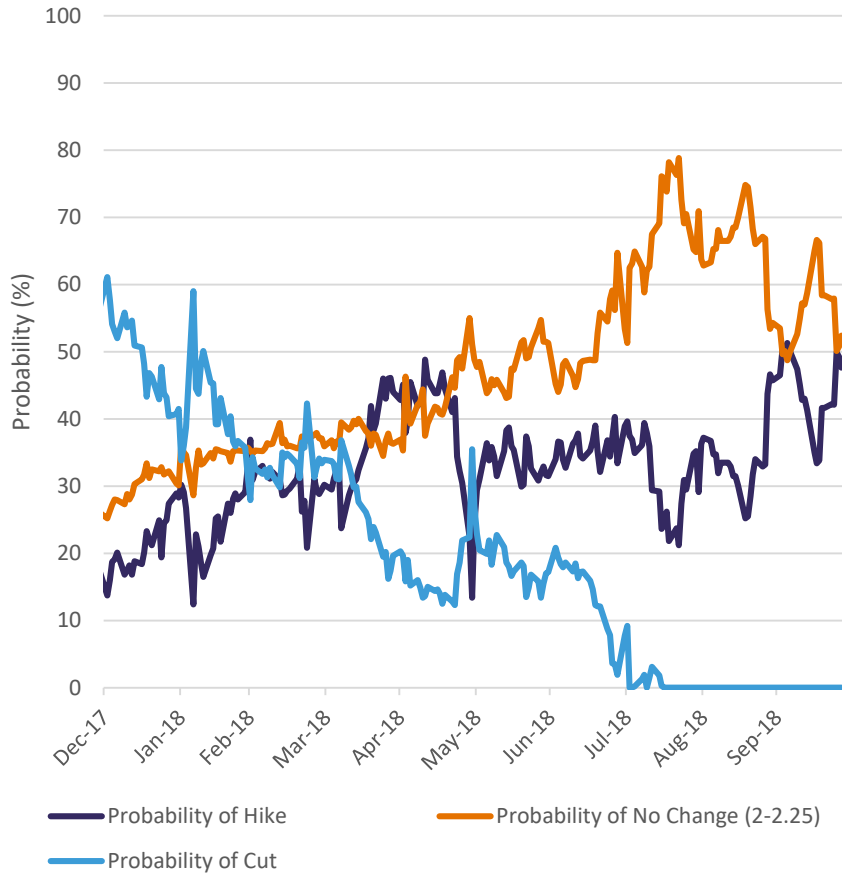
US Wage Growth



Source: Thomson Reuters Datastream

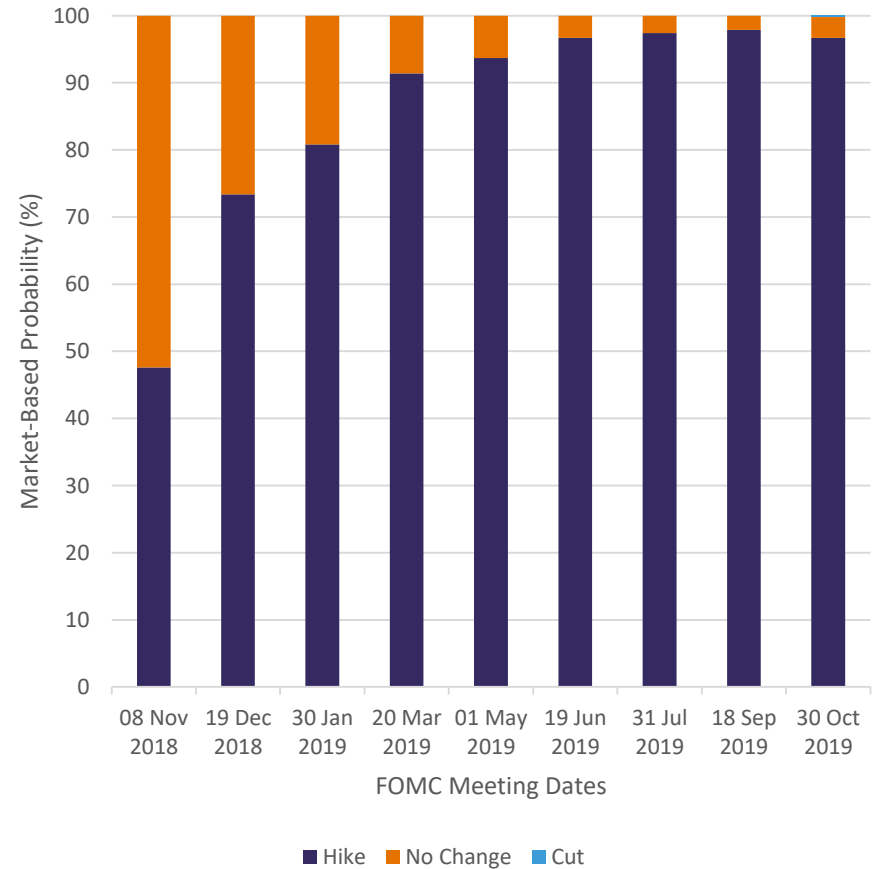
MARKET CONTINUES TO EXPECT FURTHER HIKES

Market probability for November FOMC meeting



Source: Bloomberg, Frontier

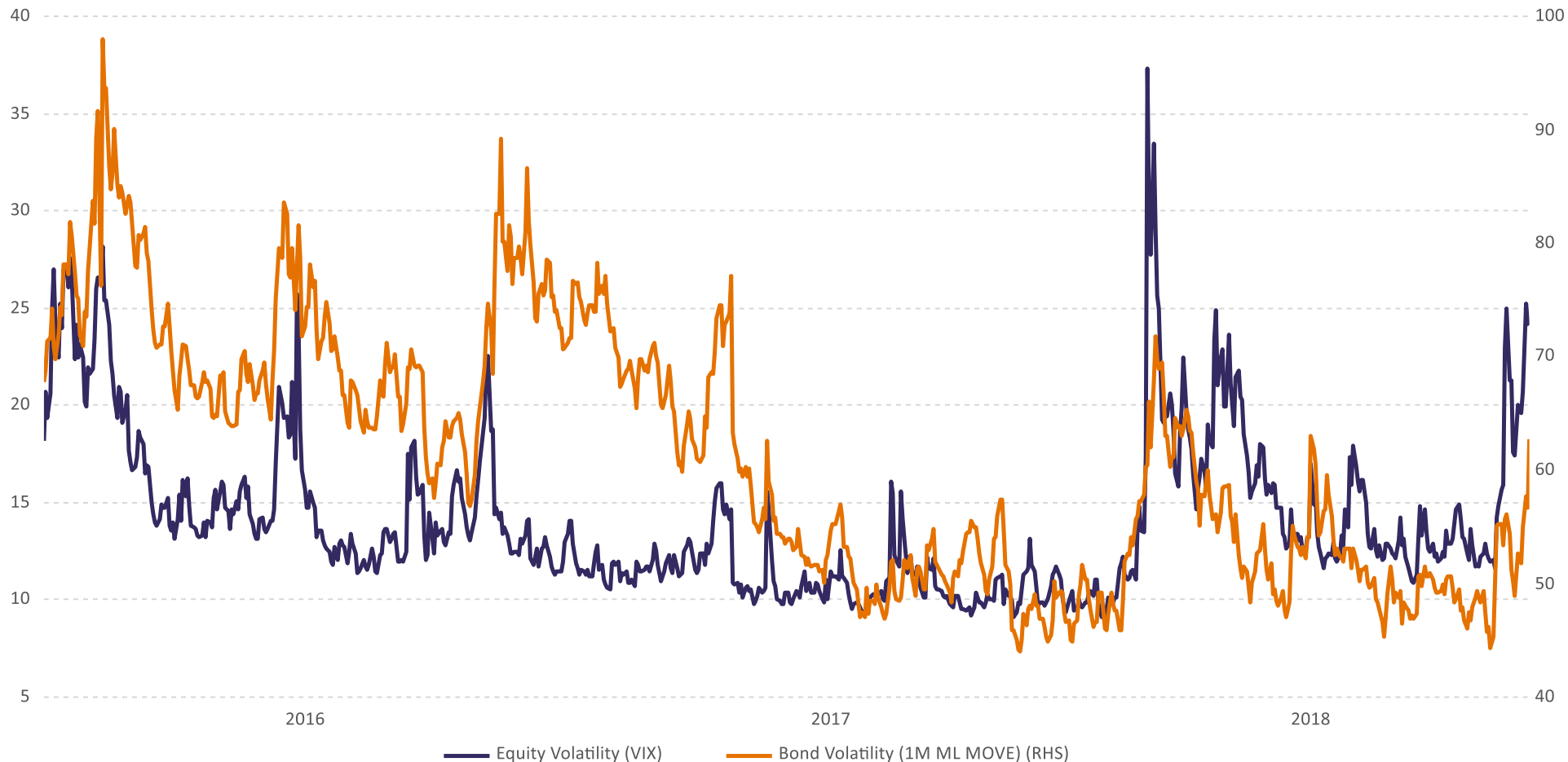
Market probability for FOMC meetings



Source: Bloomberg, Frontier

INCREASE IN MARKET VOLATILITY NOT TO THE SAME LEVEL AS JANUARY/FEBRUARY AND NOT UNCOMMON RELATIVE TO HISTORY

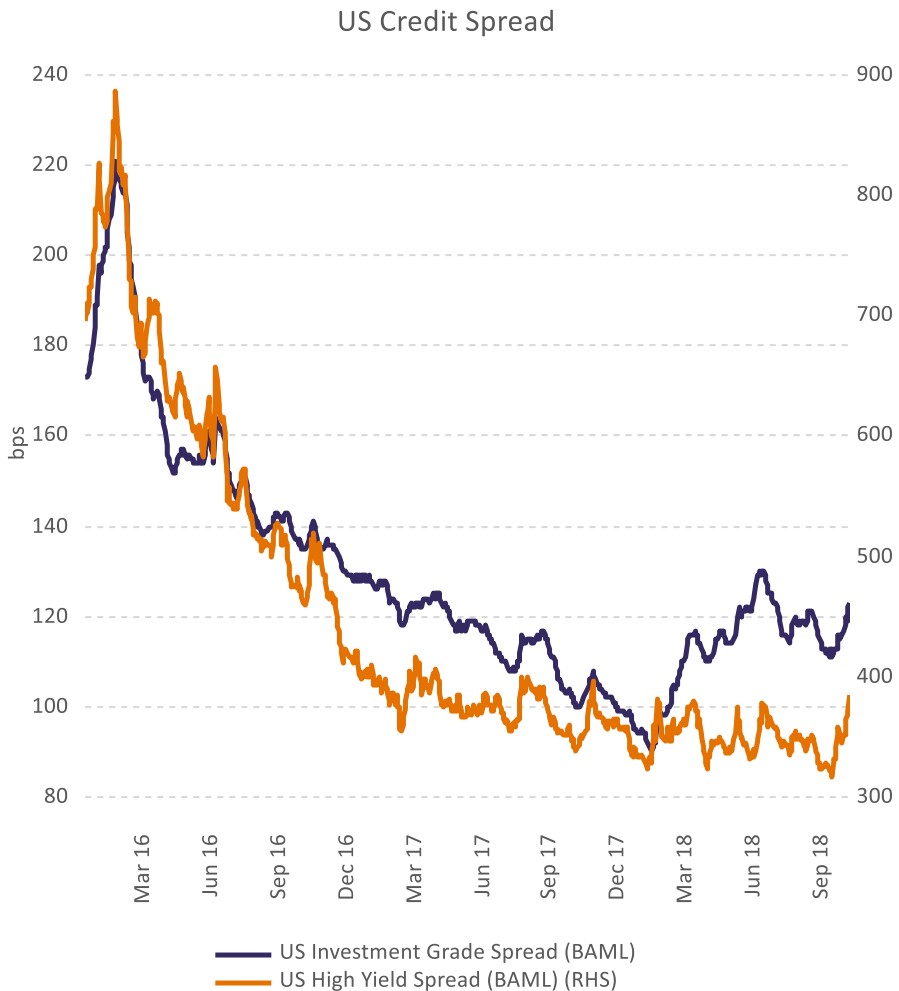
Equity and Bond Volatility



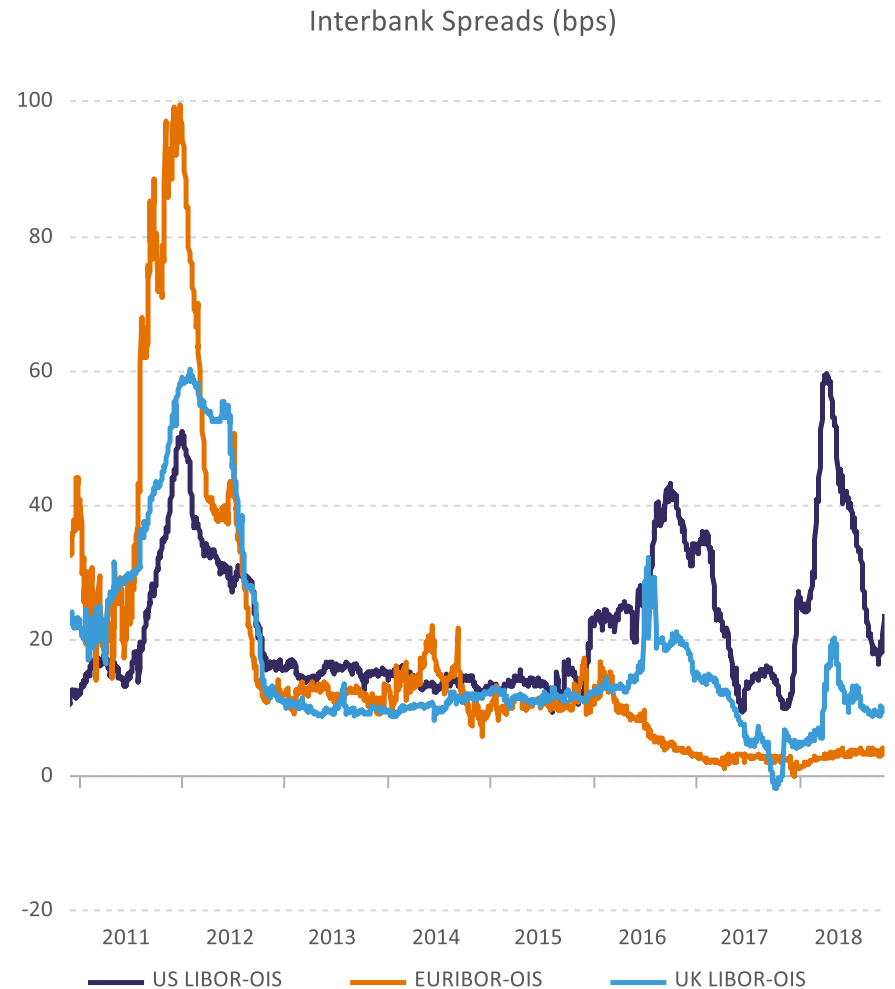
Source: Thomson Reuters Datastream



SOME WIDENING IN CREDIT SPREADS BUT STILL NEAR HISTORICAL LOWS, INTERBANK SPREADS WIDENED SLIGHTLY



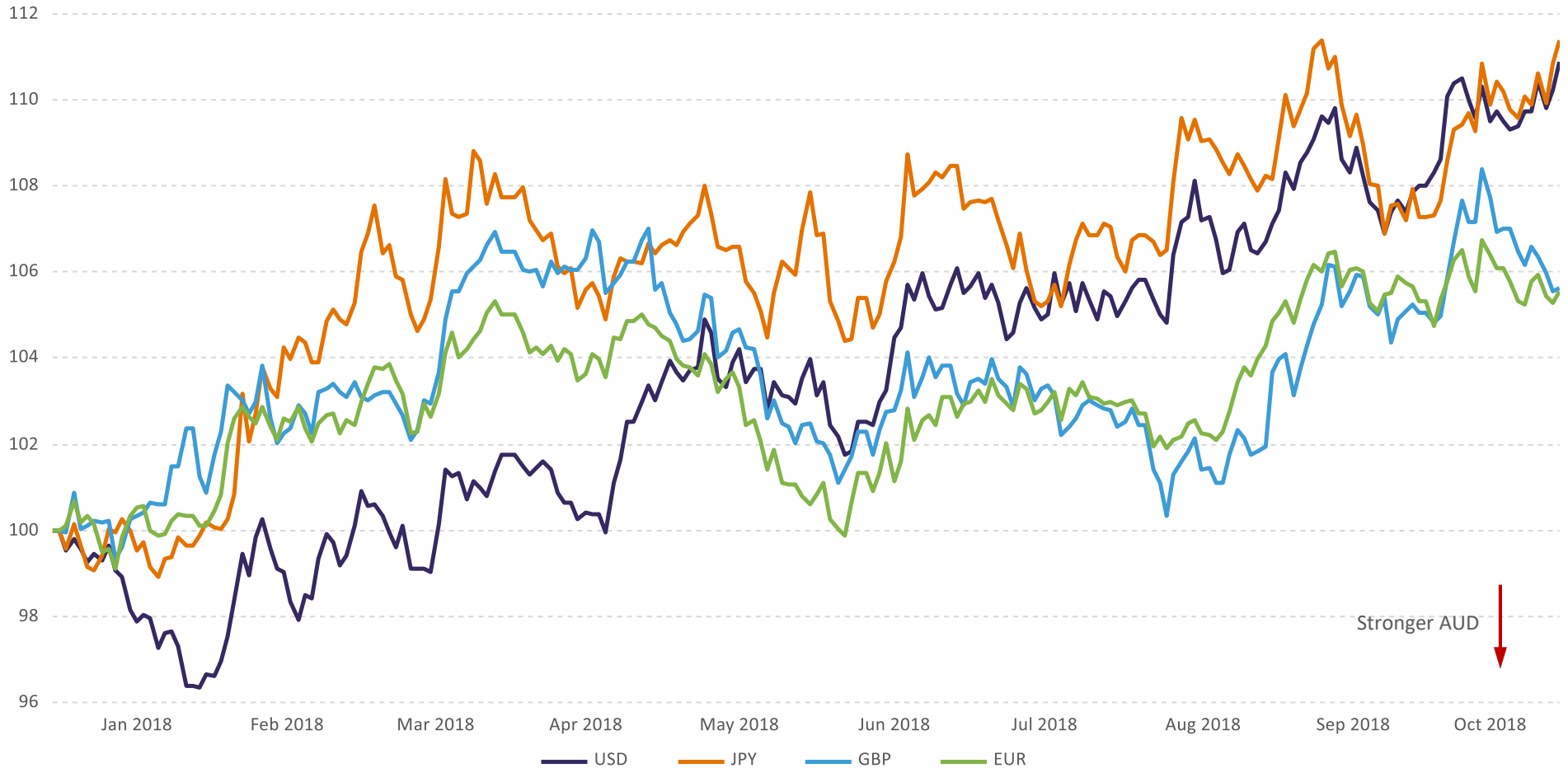
Source: Thomson Reuters Datastream



Source: Thomson Reuters Datastream

AUSTRALIAN DOLLAR APPRECIATED DURING PART OF THE MARKET VOLATILITY, BUT HAS STILL PROVIDED DOWNSIDE PROTECTION

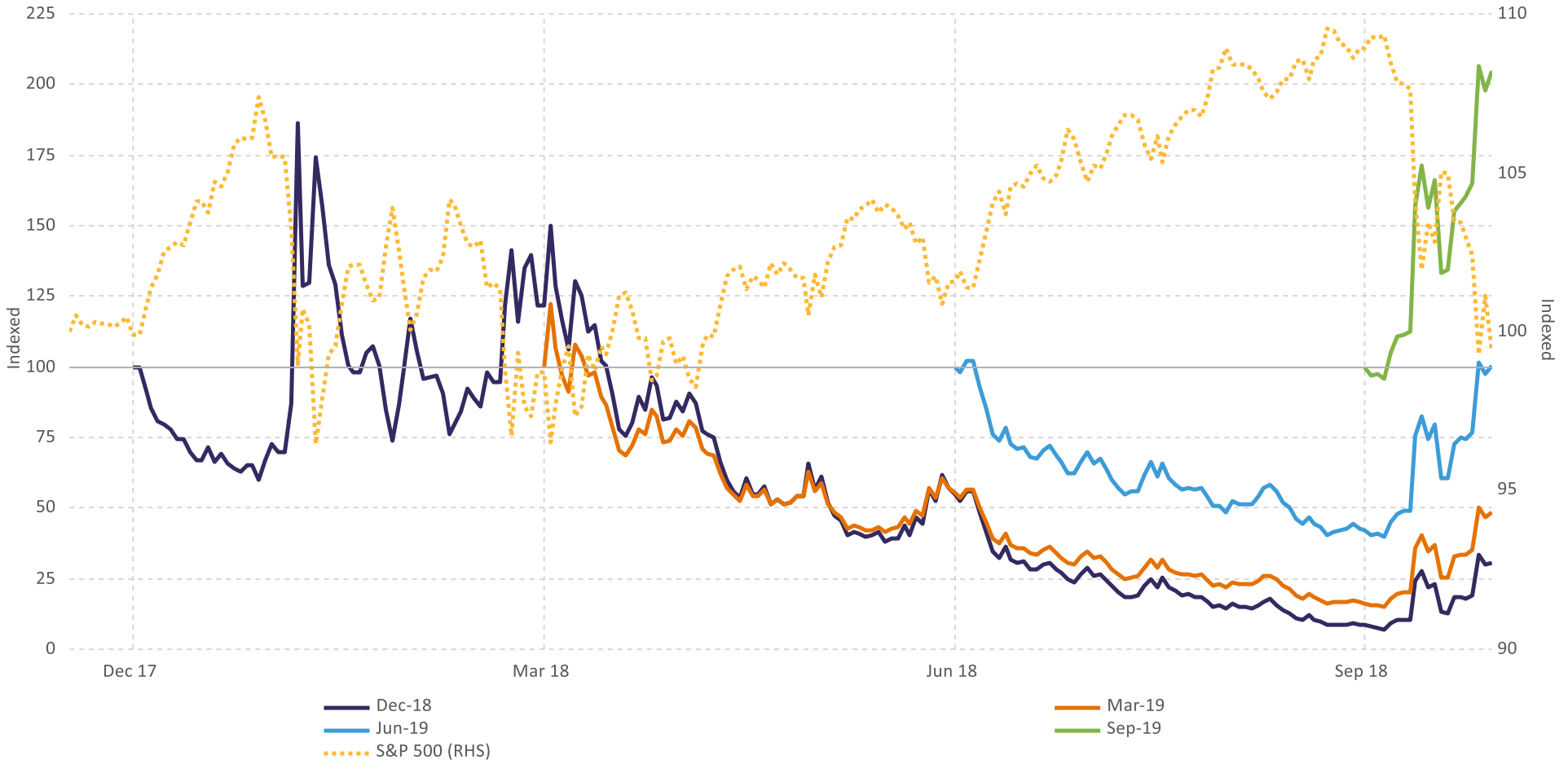
Major Currencies v AUD (Indexed)



Source: Thomson Reuters Datastream

OPTION PROTECTION REDUCED DUE TO "STRIKE DRIFT" FROM PREVIOUS STRONG MARKET PERFORMANCE

S&P 500 90% Put Option Price (index to 26/10/2018)



Source: Thomson Reuters Datastream

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