

Economic update

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Brian reviews events in Australian and overseas markets during November.

How did markets perform in November?

Generally, markets performed quite well. Most of the major world share markets showed decent gains during the month, particularly Japan, which continued to benefit from the big step-up in the Bank of Japan's quantitative easing program.

The emerging markets underperformed the developed world, despite Chinese shares having a very strong month. The People's Bank of China announced a cut in interest rates and that sparked the big gain in Chinese share prices.

Bond investors both in Australia and globally enjoyed solid returns as there were fairly significant falls in government bond yields.

Australia was one of the few markets to lose ground in November: for the month, Australian shares posted a return of -3.2%. In fact, our market has lagged the rest of the world for the year to date.

This month, it was the banks, mining stocks and energy sector that dragged our market down. Lower oil prices and a falling iron ore price did the damage.

What were the key factors driving global markets?

The geopolitical environment remains a source of uncertainty for financial markets. Whether it's Iraq, Ukraine or elsewhere, geopolitical developments still have the potential to unsettle markets. However, events in Iraq haven't prevented further falls in oil prices, and those falls are probably a positive overall for the world economy.

The actions of the major central banks are still a key influence on markets. The end of quantitative easing in the US has passed without major incident, at least so far, and that probably reflects that the US economic data suggest the economy no longer needs the extra help.

And the really aggressive steps taken by the Japanese authorities, together with the hope for some more action from the European Central Bank, have had a big influence on markets. In contrast to the US, the data in those economies suggest that they do need extra steps to boost growth.

What about developments in Australia?

This month, we again tended to see better-than-expected economic news. We're still seeing signs of a recovery in the non-mining economy coming through. We've seen some good numbers on retail trade and there's still a pick-up in demand for credit underway – most importantly, we're seeing some growth in business credit. That's consistent with some other key data released during the month which provided more evidence of a recovery in business investment outside the mining industry.

On the other hand, mining investment continues to taper off and the sharp falls in the iron ore prices are significantly detracting from our national income.

It's still an uncertain environment, and it probably means that the Reserve Bank of Australia will leave interest rates on hold for quite a while. The economy probably isn't weak enough to cut rates further, but it's not strong enough to force them to raise rates either.

How are MLC's portfolios positioned?

We haven't made any major shifts in asset allocation during November:

- we're still defensively positioned in world bond markets
- we still prefer foreign currencies over the Australian dollar, and
- we have reduced our exposure to Australian shares in recent months.

In the MLC Inflation Plus Conservative and Moderate portfolios, we've been holding significant allocations to cash and short-term Australian corporate bonds. That would have held back the performance of those portfolios during the month.

However, we've had very little exposure to Australian shares in any of the MLC Inflation Plus portfolios, so that's certainly helped those portfolios in November.

As a general rule, if we see further falls in share markets, the MLC Inflation Plus portfolios are likely to outperform the MLC Horizon portfolios. And the reverse is still true: the MLC Horizon portfolios are better positioned if markets perform strongly from here.

Our next written update will be in January 2015 and our next video in February.

Important information

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