Economic update

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Brian reviews events in Australian and overseas markets during March.

How did markets perform in March?

World share prices fell back a little in March, after some sound gains in February. But there was a good deal of divergence between the performances of the major markets. Japanese and European markets again performed well, while share prices in the US and UK lost ground.

The Australian dollar fell again, and that gave another boost to unhedged global share returns.

The Australian share market posted a slight negative return in March but that followed a very strong February, when our market posted a return of nearly 7%. If we look at the major industry sectors, energy stocks and the miners were down pretty sharply, as oil and iron ore stocks fell again. Iron ore was particularly hard hit, falling by another 20% during the month. But we saw some reasonable gains in other sectors, particularly the banks.

Bond markets recovered in March, with yields falling in most major markets, and that produced some good gains from both Australian and global fixed income.

What were the key factors driving global markets?

The actions of the world's major central banks remain crucial. US markets are grappling with the likelihood of higher US official interest rates over the coming months. The European Central Bank kicked off its quantitative easing (QE) program and the Bank of Japan's QE program is ongoing. The good performance of share markets in Europe and Japan comes at a time when the financial woes in Greece haven't been resolved, and the Japanese economy isn't faring terribly well.

The bottom line is that the stance of monetary policy globally, the extraordinarily low level of interest rates, and QE programs outside of the US, are continuing to provide support for share prices.

What about developments in Australia?

On balance, the recovery in the non-mining economy is still underway, but it remains unclear whether the recovery in the non-mining economy will be strong enough to offset the drag from mining investment activity. Certainly if the Reserve Bank of Australia (RBA) decides to do more to boost growth, there's nothing in the economic data or in the inflation outlook to stop them from cutting rates further. But given that the cash rate is the lowest in living memory, it's not clear that the level of interest rates is really holding many people back at this point.

How are MLC's portfolios positioned?

We're still defensively positioned in world bond markets.

We continue to prefer foreign currencies over the Australian dollar, which still looks overvalued and vulnerable to further falls.

In the MLC Inflation Plus Conservative and Moderate portfolios, we continue to hold significant allocations to cash and short-term Australian corporate bonds.

The MLC Inflation Plus portfolios are likely to have outperformed the MLC Horizon portfolios during March. This was partly due to some of our non-traditional strategies performing particularly well, and MLC Inflation Plus has a greater exposure to those strategies.

As a general rule, strong share markets lead to the MLC Horizon portfolios outperforming MLC Inflation Plus. However, the reverse is also true: the MLC Inflation Plus portfolios are better positioned if share markets go through another difficult period.