View from the hill

MARCH 2015

HILLROSS

Market update

The table below provides details of the movement in average investment returns from various asset classes for the period up to 28 **February 2015.**

Asset class (% change)	1 month	3 months	1 year	3 years (%pa)
Australian shares	6.9	12.7	14.5	16.3
Smaller companies	8.4	9.9	3.1	-1.0
International shares (unhedged)	5.3	11.5	23.6	26.4
International shares (hedged)	6.1	5.0	17.3	19.2
Emerging markets (unhedged)	2.6	7.9	20.0	11.0
Property – Australian listed	3.7	16.7	35.4	23.3
Property – global listed	-1.5	7.6	26.9	19.3
Australian fixed interest	0.3	3.6	10.3	7.1
International fixed interest	-0.4	2.5	9.7	7.3
Australian cash	0.2	0.7	2.7	3.1

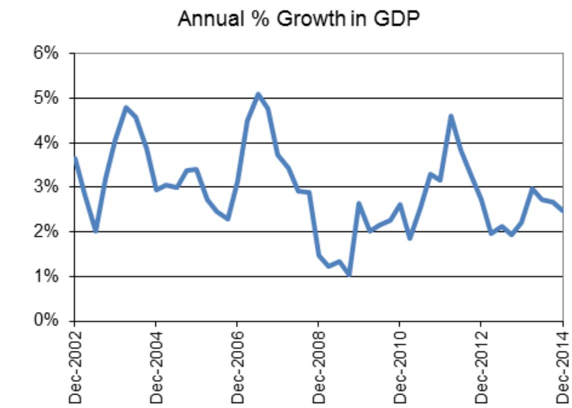
Overview & Outlook

Economic growth in Australia has continued at a subdued rate. National Accounts data for the December quarter showed that Gross Domestic Product expanded by just 0.5% over the 3 month period. In annual terms, the current growth rate of 2.5% remains below the longer term trend rate of over 3%. With annual population growth currently averaging 1.6% per annum, real per capita economic expansion is now less 1%.

In addition to the low headline growth number, the National Accounts data again confirmed that business investment in non-mining sectors has failed to increase as previously hoped. Overall business investment dropped 0.4% during the quarter to be 3.2% below the level recorded one year ago. Measures of business confidence, and surveys of business investment intentions, both suggest that business investment spending may lack any significant growth over 2015.

The household sector did, however, provide some sign of increased activity, with consumption spending rising 0.9% over the quarter. Lower oil prices and low interest rates may be providing some increased capacity for households to lift spending. In addition, there was a 2.5% rise in the value of residential dwelling construction, which is consistent with higher levels of activity in the housing industry in general over recent months.

Opportunities for the Australian economy to benefit from increased trade revenue due to the lower $A are being stymied by ongoing weakness in commodity prices and a subdued global growth environment. Consistent with the moderate growth outlook was the announcement last month that China's official economic growth target was being lowered from 7.5% in 2014 to 7.0% in 2015.

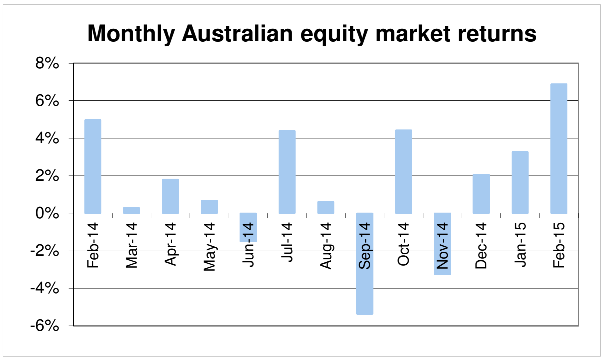


Source: Australian Bureau of Statistics.

Notwithstanding the generally subdued environment for economic growth, share markets have continued rally - both here and abroad. Companies have been able to maintain reasonable earnings growth as cost pressures are benign. This, combined with the ongoing commitment to low interest rates from major central banks, has been highly accommodative for share market growth.

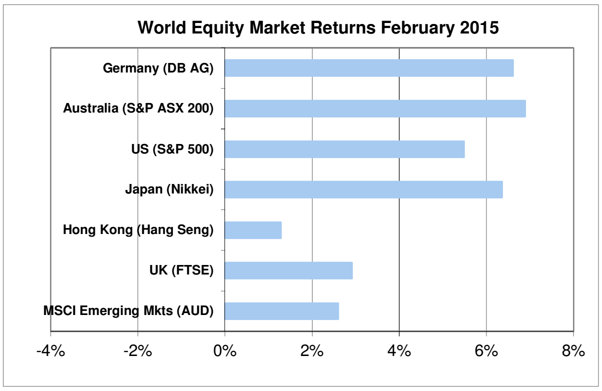
Share markets

Share markets posted very strong gains over February, with the previous month's confirmation of a European Quantitative Easing program continuing to boost confidence. Locally, the Reserve Bank's announcement of an easing in monetary policy also provided a source of support.



Source: S&P ASX 200 Index

The Australian S&P ASX 200 Index surged 6.9% over the month. This was the largest single monthly gain since October 2011. Although there was no recovery in commodity prices, mining stocks rallied strongly with the resource sector gaining 11.3%. Financial stocks also continued rise (up 7.0%), although other more defensive sectors such as consumer staples (up 1.1%) and telecommunications (up 0.6%) lagged the general market. Indicative of an increased risk appetite was the fact that smaller companies out performed, with the Small Ordinaries Index rising 8.4% over the month.



Source: Index as shown.

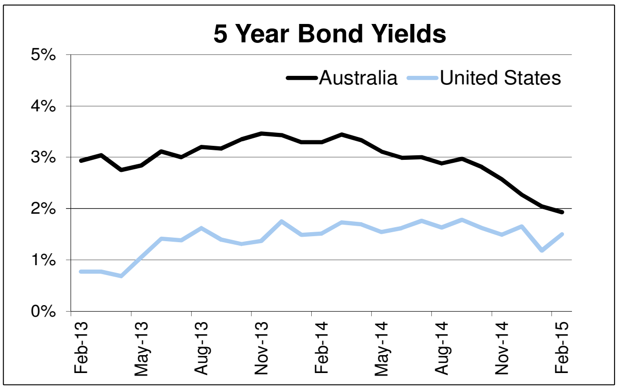
Overseas share markets posted an average gain of 6.1% during February. Investors with unhedged currency positions received a slightly lower average return of 5.3% as a result of the $A appreciating slightly against most major currencies. At the end of February, the $A was valued at U.S. 77.9 cents, up just U.S 0.1 cents for the month.

Gains were consistent across most major markets during February with the U.S., Japan and Germany all experiencing increases of more than 5%. China and other emerging markets did not perform as well, although returns were still positive in these markets.

Interest rates

Following the meeting of the Reserve Bank Board in the first week of February, the Australian overnight cash interest rate was decreased from 2.5% to 2.25%. This was the first change in the overnight cash rate since August 2013. The reduction in the cash rate was accompanied by a slight decline in longer term yields, with the Australian 5-year Government bond yield falling from 2.0% to 1.9%.

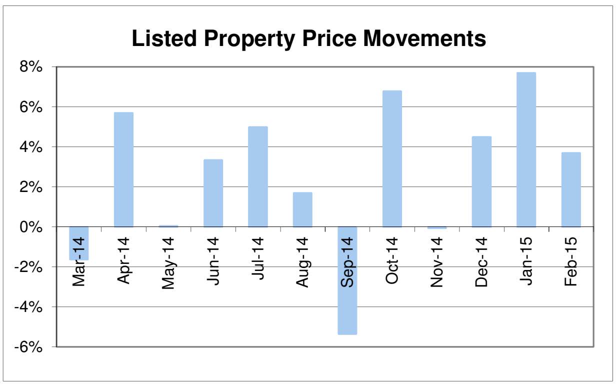
The decline in Australian bond yields was in contrast to the increase that was recorded in the U.S. last month. Over February, U.S. 5-year Government bond yields rose from 1.2% to 1.5%. This increased yield resulted in falling bond prices, thereby creating negative returns for international fixed interest investors. As the chart below shows, the margin between Australian and U.S. yields has narrowed considerably over recent months.



Source: Reserve Bank of Australia. US Federal Reserve.

Property

Once again the Australian listed property market rallied strongly with A-REITs posting a 3.7% increase during February. Over the past 3 months the sector has jumped 16.7%.There was, however, a divergence in trends between the local and overseas listed property markets last month. Possibly due to the increase in overseas bond yields, global listed property was weaker. The UBS Global Investors Listed Property Index fell by 1.5% in hedged currency terms over February; but remains 26.9% ahead on an annual basis.



Source: S&P ASX 200 A-REIT Acc Index.