The View From The Outer

David Jarman – Chief Investment Officer

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EVANS & PARTNERS

Economic and Sharemarket Snapshot

Global growth: US Q1 GDP growth of only 0.2% annualised was weaker than expected. Despite a number of "one-offs" including (yet another) unseasonably harsh winter, it does appear the stronger US dollar is impacting while the consumers' initial response to weaker oil prices has been a tad underwhelming. That said, we still expect US growth of at least 2.5% driven by the household sector. As noted last month, the growth outlook in Europe is improving. In China, the property overhang remains and we are still somewhat cautious. Growth in partial indicators including industrial production, fixed asset investment, retail sales and M2 money supply is deteriorating. The areas of the Chinese economy that matter most for Australia look tough.

Global monetary policy: Expectations of Fed Funds Rate lift-off have been pushed back in line with moderating growth expectations. We now expect a rate increase in the US in December (previously September). Policy settings elsewhere remain very accommodative. The "lower for longer" interest rate thematic remains in place.

Global equity markets: Remains our preferred asset class, although return expectations should be moderated. The US Q1 reporting season is exceeding downbeat expectations at the earnings line (but not at the revenue line). The energy sector and strong US dollar have been the major sources of weakness. Globally, 12 month forward EPS expectations are improving again. Among major developed markets Japan has a favourable earnings revisions trend and reasonable valuations.

Domestic growth: April saw a pick-up in employment growth and solid retail trade data. Iron ore prices bounced sharply from below $50/mt at the start of month, but we remain unconvinced the worst is behind us. A soft nominal economy continues to bear down on growth with the terms of trade outlook still poor; coking coal prices recently taking a hit. The outlook for non-mining investment remains poor. On the positive side, this year's Budget has been better received, building approvals are at all-time highs; housing related expenditure remains very buoyant.

Domestic monetary policy: The RBA eased the Official Cash Rate to 2.0% in April but appear to retain an unstated bias to ease. Weak non-mining investment expectations appear to concern the RBA as it is delaying a rebalancing of the economy. So to is the limited weakness in the TWI in calendar 2015.

Domestic equity markets: At around16 times twelve month forward earnings, valuations of the ASX200 look historically expensive in absolute terms; the longevity of the global yield play still a key factor. We remain cautious on the outlook for Chinese demand for our bulk commodities. The Industrials ex Banks, REITS and Utilities, at over 18 times forward earnings, looks expensive. Finding value within the market remains challenging.

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