MARCH 2019

HOUSE VIEW

EXECUTIVE SUMMARY

While we are late in the investment cycle, relatively subdued inflationary pressures have allowed policy makers to extend the cycle, and possibly support the cycle for a while longer.

OUR VIEW

Modest Chinese stimulus and the US Federal Reserve (Fed) putting the brakes on policy tightening have lifted prospects that the current investment cycle, while already extended, has further to run.

Extended investment cycle peaks are unusual relative to history. The most recent episode stretched from 1995 to 2000, ultimately bursting the tech bubble. Will the current extended cycle continue in the same way?

To date, we saw market jitters in late 2018 as recession concerns rose. But markets were quickly assured by the possibility of a US/China trade war truce, the Fed pausing rate hikes, and the Chinese stepping up stimulus. However, as we're in an already advanced cycle, any whiff of negativity could again bring bouts of volatility.

On an economic front, financial conditions have eased and we consider that both the US and China will stabilise and improve through 2019. We are less confident with respect to outlooks for Europe and Japan as any potential growth in these regions remains low and fragile, and possibly requires further policy support.

Australia is confronted by a combination of softer global growth and mounting domestic headwinds from the slowdown in housing. Support is coming from a mixture of fiscal stimulus, a softer Australian dollar and the Reserve Bank of Australia (RBA) holding rates steady for an extended period of time, with a rate cut on the cards. In our view, the Australian outlook could soften more than the global outlook through 2019.

Overall, we believe the easing in financial conditions has likely lifted prospects that a base in the global growth slide will form around mid-year. This, we think, is already reflected in market pricing and that a true catalyst to carry the market rally forward would require some recovery in corporate earnings into 2020.

Furthermore, the magnitude of any growth bounce that could develop from a base is important as it is another determining factor in whether the market rally can build.

To manage the uncertainty of balancing an advanced cycle that is vulnerable to large and rapid corrections against policy support directed at sustaining the cycle, our preferred strategy is to maintain our current position of benchmark to growth assets, Australian fixed income and the Australian dollar.

ANZ PRIVATE

STRATEGY TILTS

Preference level	LOW	NEUTRAL	HIGH
GROWTH ASSETS	-		+
Australian shares	-		+
International shares	-		+
Emerging markets	-		+
Listed real assets[1]	-		+
Alternatives	-		+
DEFENSIVE ASSETS	-		+
Australian fixed income	-		+
International fixed income	-		+
Cash	-		+
CURRENCY - AUD	-		+

Notes:
Equities, fixed income, cash and currency are relative to benchmark.

1. Comprises of 50/50 split between GREITs and infrastructure securities.

As at March 2019.

STRATEGY POSITIONS

GROWTH ASSETS	
GLOBAL EQUITIES: NEUTRAL	Macro leads have softened further to below-trend growth with US leads now also slowing. Following the recent correction and subsequent rally, valuations across most markets have moved from the cheap side of fair value back to fair value. Earnings momentum is now slowing across all regions and most sectors including the US and now the technology sector. We believe consensus 2019 global earnings per share (eps) has declined from double digits to around 5%. Investment sentiment after plunging in December has now returned to neutral.
AUSTRALIAN EQUITIES: NEUTRAL	Macro leads have eased and have now caught up with the global slowdown. Valuations in December shifted to the cheap side of fair value but have now largely returned to fair value. Consensus 2019 eps growth is moderate at around 3% and we see limited risk of a sharp downgrade cycle that would threaten dividends. We continue to expect Australian equities to perform relatively well given attractive yields and the Reserve Bank of Australia (RBA), and now the US Fed, holding rates steady for an extended period. Financial conditions remain tight due to structural credit tightening and wages growth is weak.
EMERGING MARKET EQUITIES: NEUTRAL	Macro leads are still weak and despite the rally, valuations are still modestly on the cheap side of fair value. A cap and possibly weaker US dollar with the Fed on hold will assist these markets. Outflows out of the region have improved, but the outlook for the USD and China policy easing are key factors in the period ahead.
LISTED REAL ASSETS: Global REITS / Infrastructure NEUTRAL	Valuations in global listed property have recovered from the 2018 correction with valuations now at the expensive end of fair value. With the Fed pausing rate-tightening, this sector will be supported by a cap on yields but this is likely fully reflected in rich valuations. Valuations for listed infrastructure have recovered to the upper band of fair value as the market rotated to defensive sectors. Listed infrastructure valuations are not as stretched as GREITS.
DEFENSIVE ASSETS	
INTERNATIONAL FIXED INCOME: UNDERWEIGHT	The slowdown in global growth and the collapse in the oil price have supported a solid rally in fixed income. After trading around fair value, our valuation for the US 10-year bond yield has fallen with US Fed tightening expectations taken out for 2019 with even a whiff that policy could be eased.
AUSTRALIAN FIXED INCOME: NEUTRAL	Australian fixed income has rallied strongly and signals remain neutral on subdued inflation and the RBA holding rates steady for an extended period. Valuations are moderately expensive possibly reflecting markets shifting to a rate cut. Inflation expectations are subdued compared to the rest of the world and in conjunction with an improved fiscal outlook are key drivers holding yields below US yields.
CURRENCY	
AUD NEUTRAL	Moderately positive signal as valuations are below fair value (US78c) with bulks elevated. Headwind from interest rate differential to the US is partly offset by solid bulk prices. While easing global lead indicators have driven base metals e.g. copper lower (although prices have based over recent weeks), this has been offset by bulks (iron ore, coal), driven by China's supply side reform and now supply disruptions in Brazil favouring higher grade iron ore. Overall, slow global growth and the headwinds from the housing markets are headwinds to our fair value estimate of US78c.