

Australian sharemarket records fifth consecutive monthly gain

Summary

- US housing sector is taking tentative steps towards recovering from its extended period of decline.
- Global sharemarkets rallied with renewed vigour in July.
- The Australian sharemarket rises by more than 30%, from its early March lows.
- Global and Australian property securities perform strongly.

An overview of the US corporate reporting season

US companies on the S&P 500 Index reported results that exceeded expectations in terms of earnings per share. Earnings growth appears to have been reflective of cost-cutting efforts, as opposed to growth in revenues, which limits the prospects for further growth. Also worth noting is that a surplus in productive capacity remains a significant issue for many US companies.

Economic highlights

In the US the housing sector is widely regarded as being pivotal in determining the near-term outlook of the US economy. With this in mind, a stronger than expected pace of new home sales for the month of June was a positive sign. Sales numbers rose by 11%, to reach 384,000 units and this was seen across the country, Midwest (+43.1%), Northeast (+29.2%) and West (+22.6%) all posting significant increases in sales activity. Only the South (-5.6%) recorded a negative return. New homes available for sale continued to fall, down to 281,000 from 293,000 the previous month and the number of months' supply of unsold homes has fallen to 8.8, significantly lower than its recent peak of 11.3 in March. There is also evidence of improving conditions in the areas of existing home sales. All of this data suggest that the overall US housing sector is taking tentative steps towards recovering from its extended period of decline.

Consumer spending has yet to significantly increase. Although US retail sales rose in each of the previous two months, (0.5% in May) and (0.6% in June), a sectoral breakdown of the June result revealed, petrol (+5.0%) and motor vehicle (+2.3%) sales were positive however discretionary areas of spending, restaurants (-0.9%) and general merchandise (-0.4%), resulted in an overall decline of 0.2% for the month. This implies that a broad-based rebound in overall consumer expenditure remains some way off.

The UK housing sector has shown signs of improvement. The Rightmove survey revealed that house prices rose by 0.6% in July, leaving them 3.1% below their level of a year ago. A standout was the annualised measure of prices in the key London market which recorded a rise of 0.6%, its first positive result for 2009.

Retail sales gained ground, the British Retail Consortium (BRC) which measure retail sales recording a year-on-year rise of 1.4% in June. An interesting aspect of the result was that non-food sales over the three-month period to June were the strongest since October last year. Gains were largely seen in the budget end of the market, with sales of more highly priced items continuing to struggle.

Against the backdrop of retail sales result, the annual measure of the UK Consumer Price Index (CPI) eased to a growth rate of 1.8% in June, the first time since September 2007 that inflation has fallen below the Bank of England's target rate of 2.0%.

In Europe, one of the economic highlights for the month was a positive reading on industrial production. The monthly measure of regional industrial production was expected to post a return in the region of 1.5% in May. Although the actual outcome (+0.5%) was lower than expected, it nevertheless represented the first positive result in nine months. Improvements were also evident in both the capital goods (+1.2%) and intermediate goods (+0.3%) sectors.

In China, producer and consumer prices showed evidence of moderation in June. Producer prices recorded a particularly steep fall, the Producer Price Index (PPI) declining by 7.8% on a year-on-year basis. The Consumer Price Index (CPI) posted a year-on-year decline of 1.7%, following a 1.4% fall in May. Businesses and consumers appear to have taken advantage of lower prices, 33.6% increase in the year-on-year measure of fixed asset investment over the year to date, and a 15% year-on-year increase in retail sales. These gains, along with a 10.7% increase in the year-on-year measure of industrial production growth, set the scene for gross domestic product (GDP) in China to record a year-on-year growth rate of 7.9% for the second quarter.

In Japan, the Bank of Japan (BoJ) announced at its Policy Board meeting on 16 July that it would be retaining its key policy interest rate at 0.1%. In its accompanying statement, the BoJ suggested that although "domestic private demand has continued to weaken", there have simultaneously been signs that "exports and production have begun to turn upward". Accordingly, the economy "is likely to show clearer evidence of levelling out over time", while consumer price inflation appears to have "moderated", with a further easing in play.

In Australia the labour market contracted for a second consecutive month in June, with 21,400 jobs lost. Weakness was evident in the full-time sector, where 21,900 positions were lost. The part-time sector recorded a gain of 5,000 positions. At the year-on-year level full-time employment has declined by 1.5%, compared to a 2.9% gain in part-time employment.

An analysis conducted by Deutsche Bank suggested that by switching workers from full-time to part-time arrangements, firms have been able to retain key staff by reducing their working hours, with a view to reversing this arrangement when business conditions improve. At the time of writing, the labour market report for July revealed a further gain in part-time employment.

On the back of easing demand for full-time labour, the Producer Price Index (PPI) posted a fall of 0.8%. This resulted in the annual rate of price appreciation falling to 2.1%, from 4.0% the previous quarter. Given the prevailing economic environment, margin compression was a major theme underlying the overall result. Further aspects of note were sharply lower bulk commodity prices and the emergence of deflation in the context of food prices.

In contrast, the Consumer Price Index (CPI) posted a gain of 0.5% for the June quarter. The result, was in line with expectations, and highlighted strong price gains in the health (+2.3%) and household contents and services (+2.2%) sectors, which outweighed relative weakness in the financial and insurance services (-1.7%) and food (-0.9%) sectors.

A particularly noteworthy aspect of the result for fixed interest investors was the fact that the average of the underlying measures of inflation rose by 0.8% over the quarter, lifting the year-on-year rate of increase to 3.9%. The relevance of this lies in the fact that it is widely held that the RBA places a particular emphasis on these measures of inflation for the purposes of determining monetary policy settings. Moreover, this latest result is significantly higher than the RBA's target band of 2%-3% for inflation.

International sharemarkets

Global sharemarkets rallied with renewed vigour in July, with the MSCI World (ex Australia) Index rising by 7.5% in local currency terms. This translated to a gain of 5.5% in Australian dollar terms, reflecting the further appreciation in the value of the Australian dollar. The currency gained ground against all of its major counterparts, notably rising by 2.8% against the US dollar, 2.1% against Sterling, and by 1.7% against the Euro.

At the regional level, all of the major developed markets posted strong gains, with particularly strong performances coming from the leading European markets of Germany (+10.9%) and France (+9.1%). In the US, there were similarly strong gains in the Dow Jones Industrial Average (+8.6%) of leading stocks, the technology-oriented NASDAQ Composite Index (+7.8%), and the broadly-based S&P 500 Index (+7.4%). Further underlining the strength of the markets' performance was the fact that Japan (+2.2%) was the only major developed market that did not achieve a gain of at least 7%.

The emerging markets were notable beneficiaries of the further improvement in economic data. This was reflected in a move by investors to raise the risk profile of their equity exposures, resulting in the MSCI Emerging Markets Index rising by 9.9% in local currency terms over the month.

Australian sharemarket

The S&P/ASX 300 Accumulation Index recorded its fifth consecutive monthly gain in July, rising by 7.3%. The strength of the market's recent performance becomes evident when we consider that, from its lows of early March, the market has risen by more than 30%, and presently stands at a level last seen in November 2008.

Better-than-expected outcomes in relation to economic data and US corporate profit results provided the drive for the market's July rally. Outperformance at the sectoral level tended to be concentrated amongst those sectors that are typically closely correlated with trends in the economic cycle. The Consumer Discretionary, Materials, and Industrials sectors posted particularly strong gains, significantly outpacing the Utilities, Telecommunication Services, Energy and Real Estate Investment Trusts (REITs) sectors. The defensively-oriented Health Care sector was the only area that failed to post a positive return for the month.

At the individual stock level, notable outperformers included West Australian Newspapers Holdings (+38.3%), BlueScope Steel (+33.2%), Leighton Holdings (+28.4%), ConnectEast Group (+27.9%) and Bank of Queensland (+23.9%). Negative returns were posted by Paladin Energy (-7.5%), Lihir Gold (-6.1%), Caltex Australia (-5.9%), Spark Infrastructure Group (-5.3%) and Sonic Healthcare (-5.0%).

Property securities

The global property securities markets performed strongly in July, outperforming the broader global sharemarkets. The UBS Global Investors Index rose by 8.9% in local currency terms, with strength evident in each of the major regions. Singapore (+14.2%), the UK (+11.7%), Continental Europe (+10.9%) and North America (+10.3%) all posted gains in excess of 10%, significantly outpacing the more modest return in Japan (+2.1%).

The Australian property securities sector extended its run of positive monthly returns. The S&P/ASX 300 A-REIT Accumulation Index rose by 2.4% in July, driven primarily by solid gains in the industrial stocks. Leading outperformers included Goodman Group (+37.8%), Valad Property Group (+30.1%), Mirvac Group (+18.1%), Astro Japan Property Trust (+16.2%) and Bunnings Warehouse Property Trust (+14.1%). These contrasted with distinct weakness in Macquarie DDR Trust (-23.1%), Aspen Group (-13.4%), Charter Hall Group (-10.6%), APN European Retail Trust (-6.3%) and Macquarie CountryWide Trust (-3.7%).