market watch

July 2015

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2 reasons why dividend yields matter

(Michael Price, Co-head of Fundamental Australian Equities) (Thomas Young, Portfolio Manager/Analyst)

Dividend yield is a way to measure the cash flow received for each dollar invested in an equity position. For a retiree, it can be argued that the best way to increase income from equities is to increase dividend yield, rather than drawing down on capital. There are two key reasons for this:

- Franked dividends are more tax effective for a retiree than capital gains;
- The dividend yield on equities is far more predictable and reliable than capital returns

As such, equity products designed for retirees should be focused on increasing dividend yield. While the prices of equities fluctuate in capital value in the short-term, the success of equity income investing is about focusing on the income stream that a high-quality dividend-paying company can provide.

Short-term market fluctuations are not an issue if retirees receive adequate income for life's everyday expenses.

Final thoughts

- The majority of equity funds are still designed to maximise returns with little or no focus given to income generation. In this way equity product design must move away from the traditional risk/return focus to a more goals-based approach, with the needs of the retiree at the centre.
- For more information on goals-based investing, go to *Ampcapital.com.au/Goals*
- ### Big banks: Fundamentals and valuations
- **(Dermot Ryan, Portfolio Manager - Direct Equities)**
- Australia's four largest banks, namely Commonwealth Bank, Westpac Banking Corporation, Australia and New Zealand Banking Group (ANZ) and the National Australia Bank (NAB have impeccable fundamentals right now. However, with investing, it's not where we are now but where these fundamentals are going that will help determine the price. Earnings growth moderates The banks have increased home loans and improved asset quality since the start of the rate-cut cycle in November 2011. Margin pressure has stabilised as cheaper wholesale funding helps offset declining asset yields along with the benefits of cost and bad and doubtful debts. While the banks' dividend streams may appeal to investors, they may face capital pressure from tier one capital requirements. With the Reserve Bank of Australia's rate cuts continuing to buoy the banking environment, it will be important to keep an eye on where asset quality can move from here.

Valuations are currently high but should revert.

Valuations are now moving to reflect a lower growth profile for earnings and dividends. In saying this, Australia's major banks still sit on high valuations relative to comparable global peers. This has been justified as Australia has been a standout economy post-Global Financial Crisis.

Final thoughts

- The banks will continue to provide strong dividend streams but growth of these dividends will be much harder from here and sustainability of these dividend levels may even prove difficult should earnings dip or capital requirements grow.

- ## Global mobile traffic on the rise: What does this mean for infrastructure investing?

- **(Joseph Titmus, Portfolio Manager/Analyst)**

Communication infrastructure has rapidly advanced over recent decades. While many countries have upgraded their infrastructure to keep up with these changes, the rapid pace in which technology is advancing means countries will continually need to invest to remain globally competitive. Multinational consulting firm McKinsey, forecasts a telecom infrastructure investment of US$9.5 trillion between 2013 and 2030[1].

A large portion of this investment will be used for communication towers, as they facilitate the global transition of mobile communications.

<u>Global mobile data traffic is expected to increase nearly 10-fold between 2014 and 2019.</u>

Emerging trend for private investors

We are beginning to see an increase in interest for infrastructure investing and in the number of investors making discrete allocations to this asset class. As allocations rise, we expect to see a significant amount of new capital enter the space. Investors need to ask themselves whether they want to invest now and benefit from the expected growth in this asset class – or whether they want to wait for the investment trend to become increasingly recognised.

Final thoughts

Through an active approach to portfolio management, investors can seek to take advantage of the emerging communication theme, with fund managers increasing exposure to sectors that are most likely to benefit and reducing exposure to sectors that are expected to underperform.

Global developments and outlook for the remainder of the year

(Dr Shane Oliver, Head of Investment Strategy and Chief Economist)

Greece votes no!

With more uncertainty ahead regarding Greece and the threat of a flow on to other Eurozone countries is likely to keep markets on edge in the short term, it's important for investors to not become too emotional. Contagion is likely to be limited as the rest of Europe is now in far stronger shape than was the case in the 2010-12 Eurozone crisis and defence mechanisms against contagion are now stronger.

As a result we don't see the Greek debacle derailing the European or global economic recoveries. So while the correction in shares looks like it might go further in the short term, the broad rising trend in markets is likely to continue.

<u>"There will be an occasional bounce of volatility."</u>

China stocks in trading halt

China's sharemarket over the past month has suffered sharp price falls approaching -30% for the Shanghai Composite Index. This comes after robust gains over the previous year. All short-selling — the practice of betting that stocks will fall — has been banned, and Chinese media has rushed to reassure citizens. The short-term and structural headwinds facing China's economy mean that more policy action may be needed to stabilise the economy and guard against downside risks.

Outlook for the remainder of the year

The continuation of reserved but steady global growth looks set to continue into next financial year, with growth to remain uneven between different regions around the world. While the economic environment will remain relatively constrained in terms of potential growth, there will be an occasional bounce of volatility. In this environment, it's important to turn down the noise, diversify widely and adopt an active approach to asset allocation.

Economic indicators

Gross domestic product (annual rate %)*	Latest	Current	Previous	1 year ago
World (IMF/OECD)	31/12/2014	3.30	2.90	2.90
Australia	31/03/2015	2.30	2.40	2.90
China	31/03/2015	7.00	7.30	7.40
European Union	31/03/2015	1.00	0.90	1.10
United States	31/03/2015	2.90	2.40	1.90
Inflation (annual rate %)*	**Latest**	**Current**	**3 months ago**	**1 year ago**
Australia	31/03/2015	1.30	1.70	2.90
China	31/05/2015	1.20	0.80	1.80
European Union	30/06/2015	0.20	-0.10	0.50
United States	31/05/2015	0.00	-0.10	2.00
Official interest rates (%)*	**Latest**	**Current**	**3 months ago**	**1 year ago**
Australia	8/07/2015	2.00	2.25	2.50
China	30/06/2015	1.26	3.18	2.91
European Union	30/06/2015	0.05	0.05	0.15
United States	30/06/2015	0.25	0.25	0.25
Bond yields (%)	**Latest**	**Current**	**3 months ago**	**1 year ago**
Australia 3Y	30/06/2015	2.02	1.70	2.61
Australia 10Y	30/06/2015	3.01	2.32	3.54
United States 2Y	30/06/2015	0.64	0.56	0.46
United States 10Y	30/06/2015	2.35	1.92	2.53

Exchange rates

Official interest rate (%)**	Latest	Current	3 months ago	1 year ago
Australian Dollar / Chinese Renmimbi	30/06/2015	4.7661	4.7362	5.8566
Australian Dollar / Euro	30/06/2015	0.6898	0.7113	0.6894
Australian Dollar / Great Brish Pound	30/06/2015	0.4887	0.5146	0.5520
Australian Dollar / Japanese Yen	30/06/2015	94.0497	91.6167	95.6167
Australian Dollar / United States Dollar	30/06/2015	0.7686	0.7640	0.9439

Share market analysis

Sharemarkets (in local currency)	5yrs (%pa)	3yrs (%pa)	1yr (%)	3 months (%)	1 month (%)
Australia: S&P/ASX300 Accumulation	9.5%	14.7%	5.6%	-6.5%	-5.3%
Germany: DAX Accumulation	12.9%	19.5%	11.3%	-8.5%	-4.1%
Global emerging markets: MSCI Accumulation (AUD)	5.7%	14.2%	16.5%	0.1%	-3.0%
United Kingdom: FTSE 100 Accumulation	9.7%	9.2%	0.2%	-2.8%	-6.4%
United States: S&P 500 Accumulation	17.3%	17.3%	7.4%	0.3%	-1.9%

*Data is most current data available
+Rates are expressed as 1 Australian Dollar (IMF/OECD) purchasing power-parady

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