



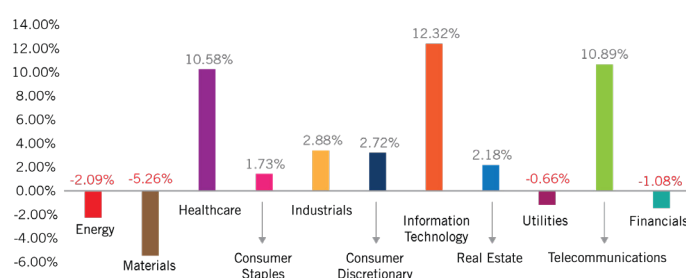
RESEARCH UPDATE

Market Watch - September '18

Global markets were mixed in August with the US stock market outperforming peers. The S&P 500 Index increased 3.03% to close at 2,902 points and the Nasdaq rose 5.71% to close at 5,109 points. Political uncertainty weighed on the S&P/ASX 200 Index (ASX 200) which finished broadly flat, rising 0.63% to close at 6,319 points.

S&P/ASX 200 Sector Performance

Data source: Bell Potter, 3 September 2018.



Sector Performance

Company earnings season resulted in mixed sector performance, with Information Technology the best performing sector rising 12.32% as technology stocks were rerated higher on the back of strong revenue growth.

Healthcare was the next best performing sector rising 10.58% driven by CSL Limited and ResMed Inc which increased 15.61% and 9.87% respectively after both announced positive operating conditions and continued strong earnings growth into the 2019 financial year.

The Telecommunications sector rose 10.89% after the announced merger of discount provider TPG Telecom Limited (+50.00%) and Vodafone Hutchinson Australia raised investor hopes that the return to three main competitors would result in more rational pricing in the industry. Telstra Corporation also rallied 9.15% after it announced strong subscriber growth across its mobile and broadband divisions.

Consumer Staples increased 1.73% driven by Wesfarmers Limited which rallied 4.02% as it announced the sale of the last of their coal mines as well as the Kmart Tyre and Auto business.

Materials was the worst performing sector declining 5.26% as Rio Tinto Limited, and BHP Billiton Limited declined 10.42% and 4.73% respectively. The drop was largely a result of the decline in iron ore price after the strong rally in July as well as management commentary that they were beginning to experience inflationary pressures in their operations.

The Energy index declined 2.09%, driven by Origin Energy which declined 18.36% as earnings did not meet market expectations and management announced cashflow would continue to be diverted to debt reduction. Santos Limited rallied 6.27% on news it would resume dividend distributions.

Economic Highlights

Australia: According to the Australian Bureau of Statistics, (ABS) Australia's population hit 25 million people in August and is expected to increase by 400,000 people per annum over the next three years. This compares to Indonesia which has 264 million people, New Zealand's 4.8 million, UK's 66 million, Canada's 36.7 million and the US's 328 million. The ageing population was also reflected, with the median age of 37 in 2017 compared to 22.5 in 1901. Life expectancy has also increased by approximately 25 years.

Description	1901 (30 June)	2017 (31 Dec)
0-19 (%)	45.1	24.8
85 (%)	0.1	2.0
Life Expectancy at birth (c)	1901-1910	2014-16
Males	55.2	80.4
Females	58.8	84.6

Source: ABS – Australia's population to reach 25 million, released 7 August 2018.

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Economic Highlights cont.

Australia is expected to sign a free trade agreement with Indonesia by the end of the calendar year. The key beneficiaries are expected to be the education services and agricultural sectors in particular grain, live cattle and dairy producers. The mining, architectural, tourism and engineering and construction sectors are also expected to benefit.

Australia's trade surplus hit \$1.87 billion in June, the largest surplus since May 2017. The result surprised the market and was largely driven by lower than expected imports and the higher value of cereal exported despite the ongoing drought that is affecting outback Australia.

UK: The Bank of England (BOE) increased interest rates by 0.25% to 0.75% in response to data showing a tight labour market and CPI inflation of 2.4%, above the 2% target. The BOE forecast average GDP growth of 1.75% over the next three years but remains wary of the impact of the European Union withdrawal will have on the economy. The UK and the European Union separation terms continue to be delayed with an agreement not expected until mid-November 2018 at the earliest.

Greece: The European Commission, the European Central Bank and the International Monetary Fund (IMF) made their last financial bailout payment to Greece on August 20. Greece is the last country to exit financial bailouts following the 2010 European sovereign debt crisis, although concerns still remain around sluggish economic growth and persistently high debt levels.

Argentina: Argentina requested access to a US\$50 billion credit line with the IMF to meet financial commitments. In 2017, Argentina issued US\$2.75 billion in 100-year bonds at 8% which received over US\$10 billion in bids from potential investors despite having defaulted 8 times in the last 200 years.

Turkey: The Lira has come under heavy selling pressure as investor confidence has been shaken. Investors fear that the government is undercutting the independence of the Central Bank, who released data showing inflation was running at 15.75% leading them to increase interest rates to 17.75%. The situation worsened after US president Donald Trump announced he would double tariffs on Turkish aluminium and steel to 20% and 50% respectively. Turkey is the world's 17th largest economy and there are fears this could lead to contagion in global markets considering Turkey's large foreign debt levels.

What to watch out for

The Australian Dollar has been depreciating against the United States Dollar finishing the month just below 72 cents. The major beneficiaries are exporters, companies who generate revenue overseas or compete with imported products in the local market.

The banks are experiencing a reduction in their net interest margins, which is the difference between what is charged to borrowers and what it pays for funding. This is a result of an increase in overseas funding costs. Westpac became the first of the four major banks to respond, raising mortgage interest rates for both investors and owner occupiers by 14 basis points. The other major banks are yet to follow, with some speculating they will absorb the additional cost in order to increase their market share. Increasing mortgage interest rates will impact consumer spending whilst also placing further pressure on property prices.



Conclusion

Investor attention will likely move to government policy as the new Prime Minister is sworn in and we approach the next Federal election. Globally, any signs of contagion from Emerging Markets and the ongoing trade wars will dominate headlines. Inflation is clearly appearing in the US, and signs are beginning to emerge in Australia with many companies reporting cost pressures in their operations in the recent earnings season. The US and UK Central Banks have both begun tightening monetary policy which will begin to impact asset prices.

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