

Market Update

December 2010

- **Global economy grows despite some major economies faltering**
- **All eyes on Ireland as bail out package is announced**
- **AUD declines on the back of European debt fears**

What's inside?

p2 Equity markets

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The pulse

↑ **Australian cash rate**
0.25% in November to 4.75%

↓ **AUD/USD**
2.4 US cents to 95.92 US cents

November market performance

Equity Markets – Price Indices	Index	At Close 30/11/2010	% Change 1 Month	% Change 12 Months
Australia	All Ordinaries	4676.44	-1.20%	-0.83%
Japan	Nikkei	9937.04	7.98%	6.33%
Hong Kong	Hang Seng	23007.99	-0.38%	5.44%
UK	FTSE 100	5528.27	-2.59%	6.50%
Germany	DAX	6688.49	1.32%	18.89%
US	Dow Jones	11006.02	-1.01%	6.39%
EMU ¹	Euro 100	2219.06	-2.42%	5.69%
World ²	MSCI – Ex Aus (Gross)	851.04	-0.46%	6.23%

Property – Price Index	Index	At Close 30/11/2010	% Change 1 Month	% Change 12 Months
Listed Trusts	S&P/ASX 300 A-REIT	830.84	-1.97%	-4.52%

Interest Rates	At Close 30/11/2010	At Close 31/10/2010	At Close 30/11/2009
Aust 90 day Bank Bills	5.04%	4.87%	4.03%
Australian 10 year Bonds	5.41%	5.20%	5.28%
US 90 day T Bill	0.16%	0.11%	0.05%
US 10 year Bonds	2.80%	2.60%	3.20%

Currency	At Close 30/11/2010	% Change 1 Month	% Change 12 Months
US dollar	A\$/US\$ 0.96	-2.48%	4.76%
British pound	A\$/STG 0.62	0.51%	10.65%
Euro	A\$/euro 0.74	4.66%	21.04%
Japanese yen	A\$/yen 80.24	1.45%	1.52%
Trade-weighted Index	73.00	0.41%	4.43%

¹ Top 100 European stocks trading on the FTSE

² Price Index – Source: www.msci.com

Source: Iress Market Technology

Past performance is not a reliable indicator of future performance.

Global economies

On the whole, the global economy looks to be making further economic progress. However, gains are far from being consistent across all economies.

While the Group of Seven (G7) central banks are being very accommodative in their monetary policy, several other central banks, including the Reserve Bank of Australia (RBA), tightened monetary policy to stem re-emerging inflationary pressures.

On the back of strong projected resource investment figures in 2011 and 2012, the RBA tightened monetary policy, raising interest rates 0.25% to 4.75%.

Also fuelling this decision was the RBA's concern about the medium-term outlook for inflation, despite the September quarter Consumer Price Index (CPI) report showing inflation seemingly under control at 2.4%.

With global growth downside risks seemingly receding, and the investment outlook brightening, the RBA's rationale was that "a gradual upward trend in inflation (is) likely over the medium term."

Meanwhile, the Australian economy's official growth rate slowed in the September quarter to a more moderate 0.2% (2.7% annualised) as fiscal stimulus faded and tighter monetary policy slowed demand.

In the US, The Federal Open Markets Committee (FOMC) announced additional quantitative easing at the November 3 meeting.

Plans were announced to further boost the US economy by purchasing an additional \$US600bn of US Treasury bonds by the end of the June quarter of 2011, while continuing to re-invest maturing mortgage-backed and other securities in Treasuries.

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Inflation or lack thereof, was justification for the move, with the Federal Reserve (Fed) saying “measures of underlying inflation have trended lower in recent quarters”.

Unemployment remains elevated and progress toward the Fed’s objective of fostering maximum employment is “disappointingly slow”.

The Fed committed to “adjust the program as needed” to ensure the sustainability of the US recovery. However markets are already speculating the Fed may have to dole out further stimulus.

Over in Europe, the focus in November was on sovereign debt concerns, especially in Ireland.

After initial resistance from the Irish Government to accept aid from the European Union (EU) and the International Monetary Fund (IMF), a deal was struck providing financial assistance from the EU, the IMF and Ireland’s own financial reserves, including its national pension fund.

The Irish Government originally had remained optimistic it could support itself through budget cuts and tax increases. It had intended to present a new fiscal plan on December 7 to demonstrate it was on top of matters. But markets and the European Central Bank (ECB) remained unconvinced.

Despite already deep fiscal cuts, the Irish economy continued to sink. The unemployment rate surged to 13.6% in the September quarter and the Irish Government needed more money to help out a struggling banking sector.

This pushed the fiscal deficit to 32% of Gross Domestic Product (GDP) from an already high level of 14.4% in 2009.

The Irish bail-out package totals €85bn, including €45bn from the EC (including some bilateral loans from the UK, Denmark and Sweden), and €22.5bn from the IMF.

In positive news, comments from Chinese officials that any further tightening would

rely on a series of measures and not just interest rate hikes, helped reduce concerns that China’s economic outlook would pose a serious threat to the global economic outlook.

With CPI increasing 0.7% in October, inflationary pressures still remain a concern in China. Nevertheless, the Chinese authorities appear determined to contain any possibility of higher inflation, causing rumours further tightening of interest rates is likely (although this has not yet materialised).

Big movers this month

- ↑ Health Care +5.6%
- ↓ Consumer Staples -5.3%

Equity markets

It’s been a choppy ride for markets over the past month. There was initial enthusiasm for risk assets at the start of the month with assurances of quantitative easing (QE II) by the Fed.

However, since then equity markets have tended to trend lower, remaining volatile through ongoing concerns over European sovereign debt.

A similar pattern played out for exchange-traded industrial commodity prices such as base metals and commodity currencies such as the Australian dollar.

Over the festive season, owing to thin economic data, movements in global risk appetite, rather than relative economic fundamentals, are likely to dictate the direction of the major equity indices.

Australian equities

	Index/Benchmark	1 Yr	3 Yrs	5 Yrs	7 Yrs
Australian	S&P/ASX 300 Acc.	1.82%	-7.04%	4.25%	9.94%
	S&P/ASX 50 Acc.	0.69%	-6.19%	4.64%	10.03%
	S&P/ASX Small Ordinaries Acc.	10.12%	-8.75%	4.40%	9.72%

On the domestic front, the ASX 300 Index started strong in November, despite the RBA rate rise, after the US Federal Reserve’s (Fed’s) quantitative easing announcement initially strengthened markets.

But it was all downhill from there, as global concerns weighed on the local market.

The Australian market, as measured by the S&P/ASX 300 Accumulation Index, finished down 0.97% for the month, again underperforming the broader global equities market.

Despite the reduced risk appetite, small cap stocks outperformed their large cap counterparts finishing up 0.53%. In contrast, the S&P/ASX 50 Accumulation Index was down 1.3%.

Sector	1 Mth	3 Mths	1 Yr
Energy	1.6%	6.2%	0.8%
Materials	1.0%	14.8%	11.1%
Industrials	-1.4%	7.5%	2.1%
Consumer Discretionary	-3.8%	2.1%	-3.3%
Consumer Staples	-5.3%	-2.1%	4.2%
Health Care	5.6%	7.7%	6.0%
Financials	-2.5%	2.5%	-4.4%
Info Tech	-2.2%	4.2%	-5.5%
Telcos	5.1%	2.2%	-9.0%
Utilities	-3.0%	4.9%	9.3%
Property	-2.0%	-3.2%	1.5%

Global equities

	Index/Benchmark	1 Yr	3 Yrs	5 Yrs	7 Yrs
Global	MSCI World Ex Aus Acc. (\$A)	1.18%	-10.07%	-3.92%	0.56%
	MSCI World Index Hedged (\$A)	8.45%	-8.51%	-0.98%	3.70%
	MSCI World Small Cap (\$A)	15.09%	-4.37%	-1.73%	3.70%
Emerging	MSCI Emerging Mkts Free	10.08%	-5.07%	6.84%	12.76%
	MSCI AC Far East Free (ex Japan)	13.12%	-4.86%	6.83%	9.79%

Markets were spooked in mid-November with Ireland's initial resistance of aid from the EU and IMF. This led to a more widespread fear about the economies in Portugal, Spain and Italy.

In Asia, China raised the reserve requirement ratio for its banks by a further 0.5% after the October inflation data showed a jump from 3.6% to 4.4% year on year.

The geopolitical tensions between North and South Korea added to market concerns and ensured markets ended the month in negative territory.

The MSCI World Index Hedged \$A fell 0.15% in November while the MSCI World (ex-Australia) \$A Index finished relatively flat, up 0.05%.

Elsewhere, most major global markets were down with the exception of emerging Asia which rose 1.38% in November.

Similar to Australia, global small caps outperformed their large cap counterparts despite the increase in risk aversion. The MSCI World Small Index gained 2.72%.

Property

	Index/Benchmark	1Yr	3 Yrs	5 Yrs	7 Yrs
Australian	S&P/ASX 300 A-REIT Acc	1.48%	-23.45%	-9.08%	-1.37%
Global	UBS Global Investors (\$A)	13.47%	-10.44%	-4.85%	N/A

Listed property was the worst performing sector in November. Global property, as represented by the UBS Global Investors Trust was down 2.6% with the Australian property sector only slightly better, down 1.97%.

Fixed interest

	Index/Benchmark	1 Yr	3 Yrs	5 Yrs	7 Yrs
Australian	UBS Composite 0 + Years	5.60%	7.37%	5.95%	6.20%
	Australian 90 Day Bank Bill	4.60%	5.08%	5.55%	5.55%
Global	BarCap Global Aggregate Index	-4.30%	2.39%	0.36%	2.28%
	BarCap Global Ag. Index Hedged	8.62%	8.97%	7.91%	7.51%

The typical fixed interest safe havens weren't spared the November sell-off with all major benchmarks down over November, and most underperforming equity markets.

The Barclays Capital (BarCap) Global Aggregate Trust fell 1.69%, while Australian Bonds, as represented by the UBS Composite Bond Index, fell 0.22%.

Australian dollar (AUD)

AUD/USD traded up to a 28 year high of 1.0182 US cents on November 5 in the wake of a surprise RBA interest rate hike and announcement that the US Fed was restarting quantitative easing.

Following this high, the AUD/USD then spent the rest of November declining. This was a result of the re-emergence of fears that Europe's debt problems would spread and have negative consequences for global economic growth.

In addition, some weaker Australian economic reports prompted traders to push out expected RBA tightening toward the end of 2011. At the same time, better than expected US economic reports raised hopes for much better US labour market news.

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