AMP CAPITAL


# INITIAL MARKET FALLS PRECEDE STRONGER RETURNS

In 2016 we're looking for global sharemarkets to provide stronger returns than what we saw last year. Despite the sharp falls we've already experienced – caused by increased China fears and ongoing US Federal Reserve rate hike concerns – we see shares trending higher due to this asset class being relatively inexpensive compared to bonds and bank deposits, and easy global monetary conditions.

**Market outlook**

Although we do expect continued volatility throughout the course of 2016, we also anticipate global growth to continue and monetary conditions internationally to remain easy. Both of these factors are going to keep shares relatively cheap compared to the alternative of bank deposits. We're expecting returns of around 7-9%.

**Interest rates**

Interest rates are expected to remain low in 2016. Global growth is still constrained due to low inflation in the US, monetary and quantitative easing in Japan and Europe and further rate cuts in China. Australia's economic growth will remain below potential, with the Reserve Bank cutting interest rates again as a consequence.

**DR SHANE OLIVER**
Chief Economist and Head of Investment Strategy, AMP Capital

**Australian property market**

The Australian property market solicits a different outlook across the various capital cities. Current price declines have been ensuing for some time in Perth and Darwin, while Hobart, Adelaide, Canberra and Brisbane have experienced modest growth. We've seen a lot of strength over the past few years in Sydney and Melbourne however, Australia's two most populated cities are now also experiencing a slowdown. We estimate gains of property prices nationwide over the next 12 months to average around 3-4%.

> "We're expecting returns of around 7-9%."

# STRENGTH IN REAL ASSETS TO CONTINUE – 2016 OUTLOOK

Global investor demand for real assets is expected to strengthen this year, with a number of themes set to influence this sector. We discuss these themes below in relation to each of the assets.

**BOE PAHARI**
Global Head of Infrastructure Equity

**Direct Infrastructure – Equity**

There is more money than ever before to invest in infrastructure. We believe deal flow will remain highest in the largest and deepest infrastructure markets of Western Europe and North America, although we are seeing more investors looking to Eastern Europe for value due to the competitiveness of deal flow in other regions and subsequent pricing pressure.

> "Demand for high-quality Australian real estate is insatiable."

**ANDREW JONES**
Global Head of Infrastructure Debt

**Direct Infrastructure – Debt**

Sectors where we anticipate strong activity and investment opportunity include the energy sector in the US, where continued market volatility is creating deal flow, and a strong pipeline of regulated opportunities across Europe. Our sweet spot will continue to be assets in utilities, energy and transport in OECD countries.

**TIM HUMPHREYS**
Global Head of Global Listed Infrastructure

**Listed Infrastructure**

Much focus has been on the changes in the global oil market and the 'lower for longer' crude oil environment, but our view is that we are in a 'lower for longer' yield environment globally. We expect the strong demand that we've experienced over the past decade for real assets that offer high and sustainable yields to continue in 2016.

**CARMEL HOURIGAN**
Global Head of Property

**Direct Real Estate**

Capital markets will continue to be the most significant driver of investment performance during the next 12 months. Demand (particularly from offshore investors) for high-quality Australian real estate is insatiable. With major institutional investors from Japan, China and Norway yet to put a toe in the water in Australia, we expect capital markets to remain deep for some time yet.

**JAMES MAYDEW**
Deputy Head of Global Listed Real Estate

**Listed Real Estate**

Europe is extremely attractive; it's in the early phases of significant monetary stimulus. Hard assets with contractual income are well positioned to benefit from this. We see great opportunity in certain core German cities – due to strong urbanisation, immigration and net household formation – and Spanish office. We expect certain Spanish markets to have some of the fastest growing rents in the world over the next three years.

# THE CHINESE CONSUMER SHIFT TO EXPERIENCES OVER 'THINGS'

A shift is taking place within the Chinese consumer market – and developed markets more broadly – to spend money on experiences rather than on traditional material products. For the Australian market, this means a boost to tourism from Chinese nationals and to the education and housing sectors from Chinese immigrants.

**Why the shift in consumer behaviour?**
This shift in behaviour most likely reflects the transition to millennials (15-35 year-olds) as they become the dominant source of incremental consumer spending; and as baby boomers retire and are therefore more likely to travel and dine out.

Social media has also facilitated the rise of 'conspicuous leisure', with platforms such as Facebook, Instagram and Snapchat inspiring the observation and creation of lifestyle image posts that highlight an active and adventurous lifestyle as a global citizen.

**Flow-on effect**
China is currently Australia's most important nationality by spend, and Tourism Australia forecasts the potential for this segment to be worth up to $13 billion by the year 2020.

According to independent brokerage and investment group CLSA, approximately 15% of China's 350 million-strong middle class population wish to emigrate, with Australia being the second most preferred destination. Australia may see a spike in Chinese immigration during the next five to ten years, which demonstrates the likely increasing demand for education and housing in the country.

> **"China is Australia's most important nationality by spend – Tourism Australia forecasts the potential for this segment to be worth up to $13 billion by 2020."**


ANDY GARDNER
Australian Resources Analyst
Fundamental Equities


**The future of Chinese consumption**
Australia's tourism, education and property sectors will continue to benefit from Chinese expenditure, a trend that we expect will last for decades to come.

The continual shift in spending from baby boomers to millennials will only progress with time, as will the relentless rise of social media, thus cultivating the trend for consumer spending on non-material expenses and changing the landscape for investors globally.

# PART 4 OF THE ESG SERIES: FOOD TRENDS AND INVESTOR IMPACTS

Opportunities to capitalise on a rising demand for food – driven by population and economic growth in Asia – coincides with opportunities and risks related to changing consumer trends. However, there is also currently an increasing obesity issue and the food and beverages sector is exposed to a number of other sustainability issues.

**The food and beverage sector is subject to sustainability drivers, some of which include:**

- **Demographic change** – population growth and rising income levels in Asia.
- **Changing consumer trends** – increased focus on 'healthy living', demand for convenience and affordability.
- **Regulatory change** – increased attention to obesity issues as well as social and environmental effects and costs.
- **Increased competition for constrained natural resources** – lack of arable land and need for yield improvement, competition for water and other scarce resources and impacts on soft commodity prices.

> **"By screening out companies with relatively poor ESG profiles, investors can generate a better pool of stocks to choose from."**


IAN WOODS
Head of Environmental, Social and Governance Investment Research


**So, where does this leave investors?**
Investors can reduce their exposure to companies and sub-segments at risk, although doing this reduces the breadth of their investments. Instead, by screening out companies with relatively poor ESG profiles, investors can generate a better pool of stocks to choose from.

Our review of the food and beverage sector shows that on average, companies with relatively better overall ESG profiles outperform those with relatively poor ESG profiles, in both the short and the long term.

**Looking forward**
The increased regulatory focus on the obesity issue combined with increased consumer awareness about personal health means two things; there are structural challenges for companies that cannot adapt and investment opportunities within companies who make product part of the solution.

1 S&P/ASX 200 Financials Index contains companies involved in activities such as banking, mortgage finance, consumer finance, specialised finance, investment banking and brokerage, asset management and custody, corporate lending, insurance, and financial investment, and real estate, including REITs. Measured 1/7/2015 compared to 1/7/2010

# ECONOMIC INDICATORS

| GROSS DOMESTIC PRODUCT (ANNUAL RATE%)* | LATEST | CURRENT | PREVIOUS | 1 YEAR AGO |
|---|---|---|---|---|
| World (IMF/OECD) | 31/12/2014 | 3.50 | 2.80 | 2.80 |
| Australia | 30/09/2015 | 2.50 | 1.90 | 2.50 |
| China | 31/12/2015 | 6.80 | 6.90 | 7.20 |
| European Union | 30/09/2015 | 1.60 | 1.60 | 0.80 |
| United States | 30/09/2015 | 2.10 | 2.70 | 2.90 |
| **INFLATION (ANNUAL RATE%)*** | **LATEST** | **CURRENT** | **PREVIOUS** | **1 YEAR AGO** |
| Australia | 30/09/2015 | 1.50 | 1.50 | 2.30 |
| China | 31/12/2015 | 1.60 | 1.60 | 1.50 |
| European Union | 31/12/2015 | 0.20 | -0.10 | -0.20 |
| United States | 30/11/2015 | 0.50 | 0.20 | 1.70 |
| **OFFICIAL INTEREST RATES%)*** | **LATEST** | **CURRENT** | **PREVIOUS** | **1 YEAR AGO** |
| Australia | 20/01/2016 | 2.00 | 2.00 | 2.50 |
| China | 31/12/15 | 1.99 | 1.99 | 3.53 |
| European Union | 31/12/15 | 0.05 | 0.05 | 0.05 |
| United States | 31/12/15 | 0.50 | 0.25 | 0.25 |
| **BOND YIELDS (%)** | **LATEST** | **CURRENT** | **PREVIOUS** | **1 YEAR AGO** |
| Australia 3Y | 31/12/15 | 2.02 | 1.83 | 2.13 |
| Australia 10Y | 31/12/15 | 2.88 | 2.61 | 2.74 |
| United States 2Y | 31/12/15 | 1.05 | 0.63 | 0.66 |
| United States 10Y | 31/12/15 | 2.27 | 2.04 | 2.17 |

# EXCHANGE RATES

| OFFICIAL INTEREST RATE (%)** | LATEST | CURRENT | PREVIOUS | 1 YEAR AGO |
|---|---|---|---|---|
| Australian Dollar / Chinese Renmimbi | 31/12/15 | 4.7493 | 4.4583 | 5.0693 |
| Australian Dollar / Euro | 31/12/15 | 0.6711 | 0.6278 | 0.6753 |
| Australian Dollar / Great Brish Pound | 31/12/15 | 0.4945 | 0.4639 | 0.5244 |
| Australian Dollar / Japanese Yen | 31/12/15 | 87.5960 | 84.1220 | 97.8140 |
| Australian Dollar / United States Dollar | 31/12/15 | 0.7286 | 0.7018 | 0.8175 |

# SHARE MARKET ANALYSIS

| SHAREMARKETS (IN LOCAL CURRENCY) | 5YRS(%PA) | 3YRS (%PA) | 1YR (%) | 3 MNTHS(%) | 1 MNTH(%) |
|---|---|---|---|---|---|
| Australia: S&P/ASX300 Accumulation | 6.67% | 9.01% | 2.80% | 6.54% | 2.73% |
| Germany: DAX Accumulation | 9.21% | 12.17% | 9.56% | 11.21% | -5.62% |
| Emerging markets: MSCI Accum (AUD) | 1.95% | 4.97% | -4.30% | -2.84% | -2.63% |
| United Kingdom: FTSE100 Accumulation | 4.88% | 5.66% | -1.32% | 3.71% | -1.71% |
| United States: S&P500 Accumulation | 12.57% | 15.13% | 1.38% | 7.04% | -1.58% |

* Data is most current available

** Rates are expressed as 1 Australian Dollar (IMF/OECD) purchasing power-parady