Stock Market & Economic Update

It has been a turbulent start to 2016 as renewed instability in the Chinese stock market, further deterioration in the oil price, a sharp sell-off in European banking stocks and a lacklustre fourth quarter US corporate reporting season has seen global stock markets post significant negative returns.

In the US, the S&P 500 Index has returned -10.5% (year to date), adversely impacted by concerns of slowing global and domestic growth. US fourth quarter GDP expanded by a disappointing 0.7%, down from 2% in the third quarter. Also weighing on sentiment was a lacklustre reporting season which has led to a flattening out of earnings expectations reflecting lower profits in the energy sector and more challenging global economic conditions overall. Major multinational companies including Apple, Procter & Gamble and Johnson & Johnson expressed concern about the global outlook in their recent earnings briefings.

In the Eurozone, the MSCI Europe Index has returned -12.2% on the back of a 25% decline in the European banking sector (since January 1st). Investors are becoming increasingly nervous about the impact of low interest rates (and their potential to go lower), which put pressure on banks' net interest margins, while there are also concerns about non-performing loans in the Italian banking sector and the global economic slowdown. In Japan, the Nikkei 225 Index has returned -17.4% driven by a sell-off in banking stocks after the Bank of Japan moved to cut the deposit rate into negative territory (ie. charging banks on their excess banking reserves) in an attempt to stimulate more life into their economy. Such a move is likely to lessen banks' profitability and encourages them to misuse capital, potentially creating problems in the future.

In China, the Shanghai Composite Index has returned -21.9% amid a series of headwinds including ongoing weak economic growth, a weaker yuan versus the US dollar and the removal of selling restrictions on stock markets.

In Australia, the S&P/ASX 200 Index has returned -9.0% largely on the back of falls on offshore stock markets and a wider appreciation of the broad range of economic challenges being faced at home. These are no longer confined to commodity exposed resource and energy groups. We are seeing increased headwinds for the banking sector (as growth moderates, funding costs escalate and capital pressures build) and in the retailing, insurance and telecommunications sectors as competitive pressures intensify.

Given offshore developments and risks building in the domestic economy we continue to believe the Reserve Bank of Australia is more likely to cut rather than increase interest rates this year.

SENTINEL STOCKBROKING

PERTH OFFICE
Ground Floor, 45 St Georges Terrace, Perth WA 6000
Tel: +61 8 9225 0000 Fax: +61 8 9225 0001

MANDURAH OFFICE
Suite 1/14 Peelwood Parade, Halls Head WA 6210
Tel: +61 8 9583 5556

www.sentinelgroup.com.au