Market review and

The first quarter of 2009 was mixed for share market investors, with pessimism being the dominant influence. By March, however, a sense of optimism began to return to equity markets in particular, as investors started to feel the worst of the global financial market crisis had passed.

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Market commentary and outlook

The outlook for the remainder of 2009 is positive, as we expect optimism to continue and for the economic recovery to gather momentum. This will be a result of extraordinary policy measures, such as the historic lowering of official interest rates, and government stimulus packages continuing to flow through the global economy.

The key factor driving the recovery will be the next leg of the inventory cycle. Evidence suggests that manufacturers and businesses have excessively run down stock levels amid weak global demand and uncertainty.

We also anticipate a moderate recovery in global growth, led firstly by China and then the US and Asian emerging markets. The UK and European economies won't enjoy the same recovery until 2010, while Japan, Latin America and Eastern Europe will lag even further behind.

Australian shares

The Australian share market produced solid gains over the June quarter, after reaching a low in early March 2009. A return of investor confidence was evident as investors bought financial and cyclical stocks like BHP and CBA, and sold out of more defensive sectors, such as healthcare. The S&P/ASX 200 Accumulation Index was up 11.3% over the June quarter, led higher by

outlook

BHP, Rio Tinto, and key consumer discretionary and financial stocks.

We're positive about the Australian share market and expect average returns of around 20% for the next year. We like growth assets such as shares and commodities as Australia's close ties to robust Asian economies will place our economy in a relatively good position. However, over the next few months we expect volatility to continue and the share market to drift lower.

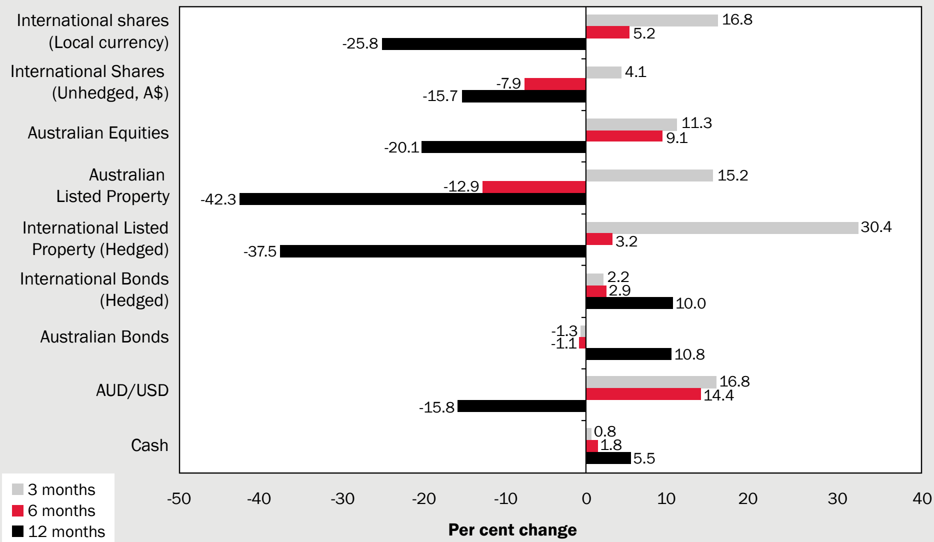
International shares

International share markets fell 25.8% in local currency terms and 15.7% in Australian dollar terms in the year to 30 June 2009. The difference in performance between local currency and Australian dollar returns was due to a weak Australian dollar that depreciated by 15.8% against the US dollar.

We continue to hold a positive outlook for international shares with a positive view towards Asian equity markets

Asset class performance to 30 June 2009

This chart shows asset class performance over the past three, six and 12 months to 30 June 2009.



SOURCE: DataStream, 30 June 2009

over one year. We expect international share markets to return around 20% over the next 12 months with Asian emerging markets delivering over 30%.

Australian and International listed property trusts

The property sectors rallied in mid-March on the back of growing investor confidence. The Australian property market (as defined by the S&P/ASX 200 LPT Accumulation Index) surged 4.6% and was one of the top performing asset classes during June. Meanwhile, global listed property (measured by the FTSE EPRA/NAREIT Global Index hedged in $A) edged 0.4% higher, lagging its Australian peers.

Performance for the 12 month period has been poor for both the Australian and International listed property sectors, recording falls of 42.3% and 37.5% respectively. However, we anticipate the domestic listed property market will deliver modest returns over the year. Due to the diversity and lack of concentration in International listed property trusts markets, we expect them to be in a good position to deliver relatively better returns.

International and Australian bonds

The International Bond Index (hedged) returned 10.0% over the 12 month period to 30 June 2009, whilst the UBS Warburg Composite Bond Index returned 10.8%. Australian and International bond yields fell as investors sought the relative safety of defensive assets during the ongoing market turmoil as many monetary authorities implemented aggressive official interest rates cuts to support economic growth and establish market stability.

The recent sharp rise in international bond yields and the narrowing of credit spreads to government bonds is a good indicator that risk aversion is declining. This prompted us to increase our allocation to global fixed income.

The sharp rise in Australian Government bond yields however, prompted us to reduce our allocation to Australian fixed income. Unlike global fixed income, we're not confident that the Australian fixed income market has the capacity to offer relatively better returns because the Australian credit market is not functioning efficiently enough.

Commodities

We expect crude oil and natural gas prices to remain high over a one-to-three year time frame, while copper, iron ore, coal, soy beans, sugar and corn prices should also fare well.

We expect commodity markets to decline over the next couple of months and market volatility to increase during the northern hemisphere summer break (June to August). But overall, we have a positive outlook for commodities over the short, medium and long term.

Investors should always bear in mind that commodities on their own are an extremely volatile asset class, but when included in a balanced or diversified portfolio there are strong diversification benefits for achieving superior risk and return.

Currencies

In the next month or two, we expect strength in the US dollar and weakness in other major currencies – particularly emerging market currencies. We expect the Australian dollar to drift lower towards US$0.75-0.73 against the US dollar during this period and then move higher into the US$0.83-0.90 range sometime next year. The Australian dollar is likely to be strong against the US dollar, the Euro, the Japanese Yen and the British Pound. ■