Zenith Monthly Market Report (31 January 2009)

MARKET INDICATORS

Market	Indicator	Current	Last Month	1 Month % Change	12 Months Ago	12 Month % Change
Interest Rates	Overnight Cash	4.25	4.25	+0.00%	6.75	-2.50%
	90 Day Bank Bill Swap Rate	3.88	4.80	-0.93%	7.30	-3.43%
	10 Year Bond	4.10	4.02	+0.08%	6.06	-1.96%
Australian Shares	All Ords	3478.10	3591.40	-3.15%	5665.30	-38.61%
	S&P/ASX 200	3540.70	3654.20	-3.11%	5618.70	-36.98%
Regional Shares	Dow Jones Industrials (US)	8000.86	8668.39	-7.70%	12442.83	-35.70%
	S&P 500 (US)	825.88	890.64	-7.27%	1355.81	-39.09%
	FTSE 100 (UK)	4149.64	4392.68	-5.53%	5837.31	-28.91%
	TOPIX (Japan)	794.03	859.24	-7.59%	1320.11	-39.85%
	Hang Seng (Hong Kong)	13278.21	14235.50	-6.72%	23653.69	-43.86%
Property	ASX 300 A-REITS Index	792.09	875.22	-9.50%	1800.97	-56.02%
	US$ Gold Price	898.25	871.45	+3.08%	921.45	-2.52%
	US$ Oil Price – West Texas Crude	43.84	36.24	+20.97%	92.21	-52.46%
	US$ CRB Spot Commodity Index	318.04	312.36	+1.82%	423.42	-24.89%
Exchange Rates	AUD / USD	0.6438	0.6914	-6.88%	0.8881	-27.51%
	AUD / EUR	0.4995	0.4904	+1.86%	0.6015	-16.96%
	AUD / GBP	0.4530	0.4764	-4.91%	0.4463	+1.50%
	AUD / JPY	57.53	62.39	-7.79%	94.81	-39.32%
Volatility	CBOE VIX Index	44.84	40.00	+4.84	26.20	+18.64

Key Points:

- Australian government bonds continued to perform solidly in January but international bonds finally disappointed
- Equity markets fell in January with all regions declining universally. A brief rally prompted by the inauguration of a new president in the US failed to revive the markets as the enormity of the problems facing the US and rest of globe weighed heavily on the markets
- Gold bullion continued to rise as investors sought refuge, climbing 3.08% for the month. Oil rebounded from its lows of late 2008, rising sharply earlier in the month to above $48 due to the conflict in Gaza before settling to above $40 as better than anticipated economic data and supply concerns buoyed prices. Broader commodity prices consolidated in January in $US terms, as measured by the CRB Spot Commodity Index.
- The Australian dollar resumed its slide in January, losing against all the major currencies except the Euro. Increased investor risk aversion, a deteriorating domestic economic outlook with the resulting prospect of more aggressive monetary policy all weighed on the Australian dollar.
- Volatility increased in January as investor risk aversion returned due to worsening economic data and renewed fears about the health of the global financial sector

CASH, FIXED INTEREST & CREDIT

Zenith Benchmarks	Total Return Indices	1 Mth %	1 Yr %	3 Yr % p.a.	5 Yr % p.a.	Fin Yr TD %	Cal Yr TD %
Australian Cash	UBS Bank Bill Index	0.39%	7.38%	6.75%	6.33%	3.90%	0.39%
Australian Bonds	UBS Composite All Maturities	1.39%	15.14%	7.48%	7.12%	13.13%	1.39%
International Bonds	Lehman Global Aggregate $A	-0.62%	6.61%	6.51%	6.81%	6.35%	-0.62%

Summary of Statistics:

- **Australian Cash** returned 0.39% in January and 7.38% for the year as measured by the UBS Bank Bill Index.
- **Australian Bonds** continued to return positively. As measured by the UBS Composite All Maturities Index, domestic bonds rose 1.39% for the month and 15.14% for the year. Government bond yields remained fairly flat in January as the market waited for the deliberations of RBA monetary policy meeting in February. The Australian 10 Year government bond is now yielding 4.06% compared to 3.99% last month and 6.07% a year ago.

- **International bonds** as measured by the Barclays Global Aggregate (Hedged $A) Index actually fell in January declining -0.62%. 10 Year bond yields rose in the US (2.84% from 2.09% last month), the UK (4.07% from 3.47%) and Japan (1.29% from 1.16%).
- Most **credit markets spreads** continued to linger near their "peaks" in January.

Commentary:

One of the more interesting developments over January was the negative return achieved by international bonds. While negative returns are not uncommon in bond markets, in recent months bonds have been a source of positive returns in a market lacking many highlights. However, with interest rates in the US and Japan virtually at zero, the UK and European Union not far behind, there's limited scope for further monetary policy and consequently limited capital appreciation upside for bonds. In fact, US 10 year bond yields bounced significantly off their generational lows in January resulting in the worst month for US government securities since April 2004, dragged down by a dramatic sell-off in long-dated Treasuries. Viewed as a safe-haven throughout the financial crisis investors are becoming increasingly concerned with the rapidly expanding budget deficit of the US government (due to the requirement to fund the bailouts and stimulus packages) and consequent over-supply of government debt.

While deflation has attracted headlines in recent months investors are beginning to focus on the longer-term consequences of the US government pledges, namely inflation. The fear is that with increasing commitments and reduced tax revenue the government will have no option but to print money with resulting inflation. Given that this predicament is common to many countries around the world the concern is valid globally. Another global concern related to the massive government issuance is the "crowding out" effect whereby governments compete for capital with private institutions resulting in rising interest rates as all participants compete for limited capital.

In this context it's important to be aware that bonds perform poorly in inflationary environments as their fixed returns are eroded by inflation. While bonds have been excellent diversifiers in the past year returning positively in an environment where all risk assets have suffered there is limited scope for further capital appreciation given global monetary policy settings. Even in Australia where the Reserve Bank has more scope for interest rate reductions the capital appreciation is limited.

In the credit space spreads remain elevated, implying far above average historical default rates. The markets remain dislocated with government guaranteed Australian bank debt still commanding a significant premium over government debt despite the two securities being fully backed by the government. Fortunately Australian banks continue to be able to source funding overseas, with the Westpac Bank actually being the first foreign bank to issue Samurai bonds into the Japanese market since September, post the Lehman Brothers collapse.

AUSTRALIAN SHARES

Zenith Benchmarks	Total Return Indices	1 Mth %	1 Yr %	3 Yr % p.a.	5 Yr % p.a.	Fin Yr TD %	Cal Yr TD %	% Ch. Fr. High	% Ch. Fr. Low	1 Mth %
Australian Shares	S&P/ASX 300	-4.84	-34.71	-6.71	5.83	-4.84	-27.76	-4.84	-38.94	6.04
Australian Shares - Small Caps	ASX Small Ordinaries	-4.65	-47.86	-12.24	1.20	-4.65	-42.91	-4.65	-51.37	6.79
Australian Shares - Style	SPGI BMI Australia Growth	-2.42	-32.11	-4.07	8.63	-2.42	-27.91	-2.42	-39.62	13.53
	SPGI BMI Australia Value	-7.62	-38.74	-10.13	3.63	-7.62	-28.71	-7.62	-40.79	4.87
Australian Shares - GICS Sectors	S&P/ASX 300 Materials	-0.98	-37.50	-2.75	13.73	-0.98	-38.85	-0.98	-49.91	28.49
	S&P/ASX 300 Industrials	-11.03	-46.38	-14.12	0.19	-11.03	-30.96	-11.03	-48.67	2.60
	S&P/ASX 300 Consumer Discretionary	-8.61	-51.88	-17.35	-7.66	-8.61	-31.27	-8.61	-53.10	2.80
	S&P/ASX 300 Consumer Staples	-0.73	-17.78	4.85	11.59	-0.73	-8.29	-0.73	-23.28	6.55
	S&P/ASX 300 Financials	-8.80	-41.46	-13.01	0.75	-8.80	-27.23	-8.80	-43.41	6.72
	S&P/ASX 300 IT	-4.27	-19.34	-3.76	8.09	-4.27	-22.81	-4.27	-31.97	12.16
	S&P/ASX 300 Telecommunication Svs.	0.06	-9.60	3.98	1.67	0.06	-9.19	0.06	-20.67	7.29
	S&P/ASX 300 Financials ex-Property	-8.63	-38.63	-11.20	2.43	-8.63	-24.24	-8.63	-40.70	7.89
	S&P/ASX 300 Property Trusts	-9.60	-52.84	-20.51	-5.92	-9.60	-39.76	-9.60	-54.92	1.35

Summary of Statistics:

- **Australian shares** as measured by the S&P/ASX 300 index experienced a poor month returning -4.84%.
- The less liquid, higher risk **small cap sector** once again outperformed large caps but is still down 47.86% for the past year. There was a large discrepancy between **value** (-7.62%) and **growth** stocks (-2.42%) for the month, with growth stocks now outperforming over the year.

- On a **sector** basis, Consumer Staples (-0.73%) and Telecommunications (0.06%) were the best performers during the month. Financials (-8.80%), Property Trusts (-9.60%) and Industrials (-11.03%) were the worst performing GICS sectors.
- The Australian share market continued its decline in January as global and domestic economic/corporate news weighed heavily on investors.

Commentary:

January marked the fifth consecutive negative month for the Australian share market. Similar to the US market the ASX initially tracked higher as optimism about the start of a new year and the inauguration of a new US president flowed into the market. However, as the month progressed a raft of poor economic news globally and domestically weighed heavily on the market. The news included negative private sector credit growth for the first time since 1992 and Chinese growth slowing considerably over the four quarters to December to 6.8%. Despite the fact that the January effect (historical precedent where shares rally in January) failed to materialise Australian shares managed to outperform most other markets, including the US, by a considerable margin.

Irrespective of commentary about the saying that "as January goes so goes the rest of the year" Australian shares remain attractively priced from a longer term perspective. While predicting the short term direction of the market is virtually impossible, with even the most talented and seasoned investors unable to consistently time markets, the foundations for a recovery are currently being established with governments around the globe initiating massive co-ordinated action in the form of stimuli and slashing interest rates. In addition the amount of cash currently parked in the cash accounts that will need to be deployed in coming months given the poor returns on offer in these accounts should result in a sizeable bounce when investor risk appetite returns.

INTERNATIONAL SHARES

Zenith Benchmarks	Total Return Indices	1 Mth %	1 Yr %	3 Yr % p.a.	5 Yr % p.a.	Fin Yr TD %	Cal Yr TD %	% Ch. Fr. High	% Ch. Fr. Low
International Shares	MSCI World Ex-Au A$	0.21	-16.77	-6.42	1.34	-5.83	0.21	-17.79	5.81
	MSCI World A$	0.07	-17.27	-6.42	1.46	-6.47	0.07	-18.41	5.83
International Shares - Small Caps	MSCI World Small Companies Ex-Au A$	1.49	-16.68	-10.93	1.05	-5.79	1.49	-19.14	10.71
International Shares - Regional	MSCI US A$	0.71	-13.73	-6.49	-0.58	0.00	0.71	-16.58	7.73
	MSCI Europe A$	-2.46	-24.85	-6.28	3.08	-16.02	-2.46	-27.50	7.53
	MSCI AC Asia Ex-Jap $A	3.72	-26.41	-1.99	6.80	-11.82	3.72	-29.60	7.53
	MSCI Japan A$	2.19	-2.84	-8.64	2.89	6.87	2.19	-4.33	13.93
	MSCI China A$	0.54	-19.33	12.65	15.04	-7.19	0.54	-27.06	31.69
	MSCI India A$	7.43	-43.22	0.06	12.73	-10.65	7.43	-45.64	14.17
	MSCI Emerging Markets A$	2.60	-29.77	-4.59	9.72	-22.13	2.60	-35.16	11.91
International Shares - Hedged	MSCI World ex-Au $A (Hedged)	-7.13	-37.58	-12.31	-2.40	-33.25	-7.13	-41.27	7.84

Summary of Statistics:

- **International Shares (ex-Australia)** returned 0.21% in December on an unhedged basis and -7.13% on a fully hedged basis.
- Consistent with domestic shares, **Small Caps** (1.49) outperformed the broader market (0.21%).
- On a regional basis, India was the best performing country in $A followed by Emerging Markets. Emerging markets outperformed developed markets as risk appetite returned.

Commentary:

On an unhedged basis January wasn't a bad month for world equity markets with the weakness in Australian dollar offsetting the poor performance by most regional markets, once again highlighting the diversification benefits of investing in international shares on an unhedged basis. However, the hedged return presented a far more accurate picture of overseas markets with initial optimism about the inauguration of a new US president quickly dissipating in global markets due to the continual barrage of poor corporate and economic data that acted to quickly remind investors of the harsh economic reality now facing the world (in what the IMF predicts will be the toughest year in the post World War II era).

Financials were once again in the headlines as Citigroup, Merrill Lynch (recently acquired by Bank of America) and Royal Bank of Scotland (RBS) shocked the markets with larger than expected losses. Considered too large to fail with roughly $2 trillion of assets Citigroup announced its fifth straight quarterly loss of $8.3 billion, almost twice the expected average forecast. As a consequence the bank announced plans to split the company into two divisions, sell assets (during the month it sold a 49% stake of its treasured Smith Barney brokerage division to Morgan Stanley) and seek more government assistance. Merrill Lynch announced a fourth quarter loss of $15.3 billion, almost three times larger than the average analyst estimate forcing the recent acquirer, Bank of America, to

request $20 billion in additional government assistance and a guarantee of $118 billion on potential losses on toxic assets. Across the Atlantic the RBS announced the largest corporate loss in UK history, reporting a full year loss of £28 billion. During the month the share price plummeted 70% in a single day as investors fled, fearing full nationalisation of the bank. This pre-empted the government move of converting its preference shares to increase its shareholding to 70%.

While the path to recovery may be a little longer than anticipated, with the IMF recently downgrading world economic growth to 0.5% in 2009, international shares will lead world economies up just as they led on the way down. Given that many international value managers are now seeing exceptional value it's likely that the recovery, when it arrives, will be substantial.

PROPERTY & INFRASTRUCTURE

Zenith Benchmarks	Total Return Indices	1 Mth %	1 Yr %	3 Yr % p.a.	5 Yr % p.a.	Fin Yr TD %	Cal Yr TD %	% Ch. Fr. High	% Ch. Fr. Low
Australian Listed Property	S&P/ASX 300 Property Trusts	-9.60	-52.84	-20.51	-5.92	-39.76	-9.60	-54.92	1.35
Global Listed Property	FTSE EPRA/NAREIT GLOBAL REITS (Hedged $A)	-6.79	-43.33	-36.52		-34.09	-6.79	-45.55	13.54
Global Listed Infrastructure	S&P Global Infrastructure Hedged $A	-5.47	-33.05	-2.70	8.77	-29.81	-5.47	-36.62	7.66

Summary of Statistics:

- Australian Property was once again the worst performing sector domestically returning -9.60%, significantly underperforming Global Property, which returned -6.79%.
- Global Listed Infrastructure as represented by the S&P Global Infrastructure Hedged $A, performed poorly as well in January returning -5.47% for the month.

Commentary:

Domestic LPTs and Global LPTs were once again pummelled in January. The highlight in the Australian market was the announcement by Westfield (representing 46% of the Australian Property Index as at 31 Dec 2008) that it was writing down its assets by $3 billion, reducing its earnings guidance and advised its dividend would be in line with its reduced earnings. The stock promptly declined 7.5% on the day of the announcement but recovered most of the losses during the day.

Domestic and Global property continues to suffer the double misfortune of rising "cap" rates, which are used to value property assets, reflecting a harsher operating environment (i.e. lower operating earnings), as well as restrictive and prohibitively priced capital access. While it's impossible to know where the bottom is for the sector current valuations are highly attractive with many stocks trading below their Net Tangible Assets (NTA).

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Data Source: Thomson Reuters