



- ▶ European and US debt dominates markets
- ▶ Chinese growth remains strong
- ▶ Australia's Carbon Tax unveiled

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The pulse

↑ Gold
8.5% |

↑ Iron Ore,
Chinese Imports
5.2%

July market performance

Equity Markets – Price Indices	Index	At Close 29/07/2011	% Change 1 Month	% Change 12 Months
Australia	All Ordinaries	4500.53	-3.42%	-0.15%
Japan	Nikkei	9833.03	0.17%	3.10%
Hong Kong	Hang Seng	22440.25	0.19%	6.71%
UK	FTSE 100	5815.19	-2.20%	10.60%
Germany	DAX	7158.77	-2.95%	16.44%
US	Dow Jones	12143.24	-2.18%	16.03%
EMU ¹	Euro 100	2247.61	-2.44%	2.75%
World ²	MSCI - Ex Aus (Gross)	890.61	-2.72%	10.33%
Property – Price Index	Index	At Close 29/07/2011	% Change 1 Month	% Change 12 Months
Listed Trusts	S&P/ASX 300 A-REITS	777.46	-6.48%	-7.52%
Interest Rates		At Close 29/07/2011	At Close 30/06/2011	At Close 31/07/2010
Aust 90 day Bank Bills		5.07%	5.03%	4.78%
Australian 10 year Bonds		4.80%	5.21%	5.21%
US 90 day T Bill		0.10%	0.02%	0.14%
US 10 year Bonds		2.80%	3.16%	2.91%
Currency ³		At Close 29/07/2011	% Change 1 Month	% Change 12 Months
US dollar	A\$/US\$	1.10	2.65%	21.54%
British pound	A\$/STG	0.67	0.45%	16.44%
Euro	A\$/euro	0.76	3.46%	10.33%
Japanese yen	A\$/yen	84.49	-2.17%	7.90%
Trade-weighted Index		78.40	0.77%	12.97%

¹ Top 100 European stocks trading on the FTSE

² Price Index – Source: www.msci.com

³ All foreign exchange rates rounded to two decimal places

Source: Iress Market Technology Past performance is not a reliable indicator of future performance.

Global economies

European debt concerns and the US debt standoff dominated global markets in July.

US Debt Situation

Starting with the world's largest economy, US Republicans and Democrats finally agreed on a deal on the last possible day, August 2, to raise the US debt ceiling.

The package included an increase in the \$14.3 trillion debt ceiling through 2012 which was a key component for President Obama who wanted to ensure this was raised until after next year's election.

The agreement also cuts Government spending by around \$US1 trillion over 10 years with a special joint committee to cut a further \$US1.5 trillion from long-term debt by 2021.

Further, if the committee fails to send a report to Congress by Thanksgiving (the fourth Thursday of November) detailing the cuts, there will be cuts across all government areas including Medicare and defence programs.

However, despite the agreement, ratings agency Standard & Poor's have since lowered the US sovereign rating from AAA to AA+ with a negative outlook initially sending global sharemarkets significantly lower.

Since then, sharemarkets and other risk assets have been volatile with some markets moving in excess of six per cent in intra-day trade.

Despite the passing of the debt bill, there is still plenty of concern about the outlook for the US economy. Gross Domestic Product (GDP) figures for the 2011 June quarter showed growth of 0.3% (or 1.3% annualised) which is below market expectations with first quarter GDP being revised to just 0.4%.

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European Debt Crisis

Moving to the other major talking point throughout July, European Union (EU) leaders agreed on a plan to stem Greece's sovereign debt crisis through a new bailout package worth €109 billion.

The bailout package will consist of contributions by the European Financial Stabilisation Fund (EFSF), the IMF and the private sector.

For Greece, Ireland and Portugal the rate of interest on EFSF loans will be cut from 5.5% to 3.5%. In addition, the average maturity of EFSF loans will be extended from 7.5 years to a minimum of 15 years, with some loans extended to 30 years.

The €440 billion EFSF will also be allowed to buy bonds in the secondary market to fight contagion risks.

The 'new' Greek bailout will be formally concluded in September, while the expansion in the EFSF's role will have to be endorsed by national parliaments.

Italy has also come under increased scrutiny in the past month, but the passing of a €48 billion austerity package by the Italian Parliament somewhat eased concerns that it would be the next country to require a bailout.

Early in August as markets grew more concerned of contagion spreading to the larger economies of Italy and Spain, the European Central Bank (ECB) has been involved in buying sovereign bonds in the secondary market to help provide some reassurance to markets.

Furthermore, the European Banking Authority released results of the latest round of bank stress tests in mid-July.

Only 8 of the 91 banks tested had capital ratios below 5%, and will need to raise capital over the next 2 years.

Despite all the sovereign and financial risks in Europe, the ECB President Jean-Claude Trichet did not suggest that interest rates are now 'appropriate' which implies that further rate increases are on the horizon even after the July rate rise.

China

Over in the world's second largest economy, China increased interest rates again in July which is the third 0.25% rate hike this year and the fifth since October 2010.

The move was somewhat expected as there had been speculation within markets that the People's Bank of China (PBoC) would raise rates again in July given the further uptick in inflationary pressures.

Despite the continued monetary tightening, Chinese economic growth remains solid with China's GDP rising 2.2% in the second quarter to be up 9.5% year on year which is above the forecasts of 9.3%.

On the home front

The Reserve Bank of Australia (RBA) recently left the cash rate unchanged at 4.75% at its August meeting as global uncertainty continues to impact the board's decision.

However, June quarter inflation numbers surprised on the high side which means that a rate rise at some point is still on the cards.

Outside inflation data, July saw deterioration in most key economic indicators including:

Big movers this month

Going up

↑ Telcos 3.5%

Going down

↓ Consumer Discretionary -7.2%

- house prices continuing to fall
- building approvals declined for the fifth time in six months
- retail trade declined
- credit growth was negative, and
- business and consumer confidence fell significantly.

However, it is the medium-term wage and inflation risk that has the RBA concerned as above trend growth and tight capacity remains.

July also saw the Australian Government announce a carbon tax of \$23 per tonne which will be introduced in July 2012.

The tax will be paid by the 500 largest polluters in Australia and the carbon price will rise by 2.5% per annum in real terms until July 2015 when a 'cap and trade' emission trading scheme will begin.

The Government has provided no estimates on the GDP impact except that GDP in 2020 is expected to be 0.3% lower with a carbon scheme.

Over the next four years, the Federal Budget cost of the carbon package will be around \$4.3 billion but the Government still expects to return the Budget to surplus in 2012-13.

Equity markets

With Italy sharing more of the spotlight in Europe and the US debt ceiling standoff playing out to the very end, July was generally a negative month for equity markets as the rise in global risk aversion led to significant falls.

Australian equities

	Index/Benchmark	1 Yr	3 Yrs	5 Yrs	7 Yrs
Australian	S&P/ASX 300 Acc.	3.00%	0.56%	1.92%	7.74%
	S&P/ASX 50 Acc.	1.45%	1.10%	2.28%	7.86%
	S&P/ASX Small Ordinaries Acc.	12.19%	0.28%	1.58%	7.31%

The ASX 200 was one of the worst performers in comparison to major indices with the market closing out the month of July over 3.0% lower.

Sector	1 Mth	3 Mths	1 Yr
Energy	-3.8%	-12.9%	1.1%
Materials	-1.5%	-5.4%	13.1%
Industrial	-0.7%	-2.5%	7.6%
Consumer Discretionary	-7.2%	-12.8%	-11.0%
Consumer Staples	-4.6%	-3.6%	4.5%
Health Care	-4.8%	-8.1%	1.9%
Financials	-6.2%	-11.1%	-2.6%
Info Tech	-5.0%	-13.6%	-15.8%
Telcos	3.5%	3.3%	3.3%
Utilities	-1.7%	0.7%	9.3%
Property	-6.4%	-7.2%	-2.0%

Global equities

	Index/Benchmark	1 Yr	3 Yrs	5 Yrs	7 Yrs
Global	MSCI World Ex Aus Acc. (\$A)	-2.45%	-4.59%	-5.51%	-1.23%
	MSCI World Index Hedged (\$A)	13.88%	-1.42%	-0.73%	3.64%
	MSCI World Small Cap (\$A)	3.37%	1.45%	-2.79%	1.85%
Emerging	MSCI Emerging Mkts Free	-3.21%	0.10%	3.30%	10.58%
	MSCI AC Far East Free (ex Japan)	0.64%	3.39%	3.90%	8.41%

In the US, equities fell over 2% in July, with the entire decline coming in the final week of the month as the debt ceiling deadline loomed. By early August, the S&P 500 had lost all its gains in 2011 amid the volatility.

Asian and European markets also suffered with the UK FTSE down 2.0% in July, the German DAX down 2.9% and the Chinese market was down 2.4%. Bucking the trend was the Nikkei which was one of the few markets to record a rise in the month gaining 0.2%.

Property

	Index/Benchmark	1 Yr	3 Yrs	5 Yrs	7 Yrs
Australian	S&P/ASX 300 A-REIT Acc	-2.04%	-10.13%	-11.96%	-4.24%
Global	UBS Global Investors Index	3.00%	-3.00%	-7.26%	N/A

The S&P/ASX 300 A-REIT Accumulation Index fell 6.4% over the month of July with the retail sector providing the biggest headwinds. Its global counterpart performed relatively better returning -2.5% over the same period. Geographically, North America provided some positive gains, however this was outweighed by continental Europe, the UK and Japan which were all over 2% lower.

Fixed interest

	Index/Benchmark	1 Yr	3 Yrs	5 Yrs	7 Yrs
Australian	UBS Composite 0 + Years	7.02%	8.01%	6.83%	6.42%
	Australian 90 Day Bank Bill	4.92%	4.49%	5.44%	5.50%
Global	BarCap Global Agregate Index	-10.10%	1.34%	-0.13%	0.62%
	BarCap Global Ag,. Index Hedged	7.30%	9.56%	8.45%	7.58%

The flight to safety saw both domestic and international bonds have a relatively good month. Australian bonds gained 1.67% over July and have returned 7.02% over the last year.

With the Australian Dollar pushing higher against the US Dollar in July, hedged global bonds, as measured by the Barclays Capital (BarCap) Global Aggregate Index (Hedged), outperformed unhedged global bonds by around two per cent to return 1.5% for the month. Over the year, hedged global bonds outperformed by in excess of 17%.

Australian dollar (AUD)

The Australian Dollar (AUD) soared to a new post-float high in late July.

While the AUD spent the first half of the month of July in the 1.06 to 1.08 USD range, it rose after the EU package for Greece was finalised and received a further boost when the US Dollar came under pressure on fears in late July that the debt ceiling would not be raised before the deadline.

The AUD then hit a new 29-year high of 1.1081 after second quarter inflation figures triggered an unwinding of RBA rate cut expectations.

In the early part of August, the AUD had moved closer to parity after investors sold out of risk assets and currencies opting for the more traditional safe havens but was recently trading closer to 1.05 USD.