

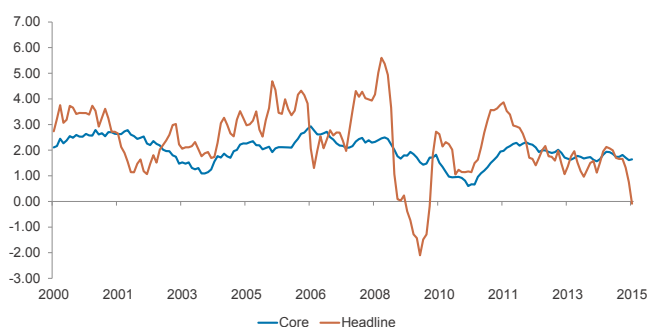
Investment Brief

FEBRUARY 2015

Global shares rallied strongly over February, with share markets in Europe leading the way. The New Zealand share market lagged its global counterparts, but still returned a solid gain over the month. Global bond yields bucked their recent trend and rose on the back of some solid data out of the US and good news on Greece. New Zealand Government bond yields rose over the month as longer term rates took the lead from offshore markets. The New Zealand dollar closed the month higher against all the major currencies.

1. Inflation in the US

US CPI Annual % change



Source: US Bureau of Labor Statistics

2. Japan out of recession but result disappointing

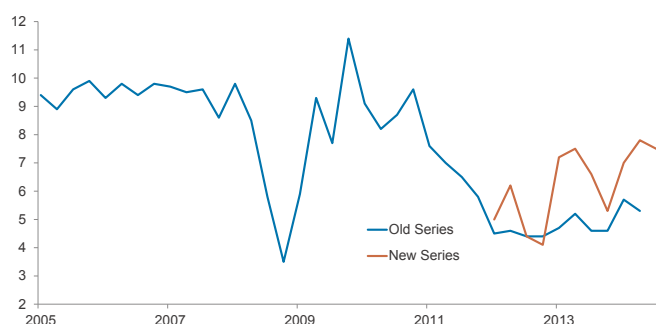
Japan GDP growth Percent change



Source: Bloomberg

3. India GDP revised upwards

India GDP Annual % change



Source: Bloomberg

US

- > US consumer prices fell -0.7% in January, their third consecutive decline. A further decline in energy prices was the key contributor to the weakness. This pushed the annual rate of headline inflation into negative territory with a reading of -0.1%.
- > The more important core inflation measure came in stronger than expected at 0.2% for the month and 1.6% over the year. Core goods prices remain weak thanks to the stronger dollar and a degree of spillover from lower petrol prices into lower goods transport costs.
- > Core services inflation (comprising about 60% of the CPI) was up 0.3% for the month and 2.5% over the year. That's a sign of an economy that is continuing to strengthen and supports our contention that as the output gap closes in the US, inflation will become broader based.

Japan

- > December quarter data saw the Japanese economy grow 2.2% (quarter-on-quarter (qoq) annualised) following two quarters of contraction. The economy is now out of recession although the result came in weaker than expected. Annual average growth for 2014 now stands at 0.0%.
- > There were positive contributions from net exports and consumption while capital expenditure was positive for the first time since the first quarter of 2014. That said, growth in all three components was weaker than expected.
- > We expect continued modest growth in the period ahead. While capital expenditure will remain subdued, consumption will get a boost from lower oil prices, and exports are expected to continue to expand on the back of the weaker yen and stronger growth in the US.

India

- > Historical GDP growth in India is higher than previously estimated. Annual growth that was initially reported at 5.3% for the year to September 2014 has revised up to 7.8% in the new series. Growth came in at 7.5% for the year to December.
- > Looking ahead, growth is likely to benefit from the clearing of roadblocks to major infrastructure investment projects, easing in monetary conditions and continued supply-side reforms.
- > Longer term, it is the labour market that is India's greatest opportunity and the greatest threat to its long-held ambitions of outpacing China growth on a sustained basis.
- > There is reason to remain optimistic about the outlook for India, but that requires the government to deepen reform efforts. If successful, India should enjoy a sustained period of growth in the 7-8% range.

4. China trade data

China imports and exports Annual % change



Source: National Bureau of Statistics of the People's Republic of China

5. RBA cuts interest rates

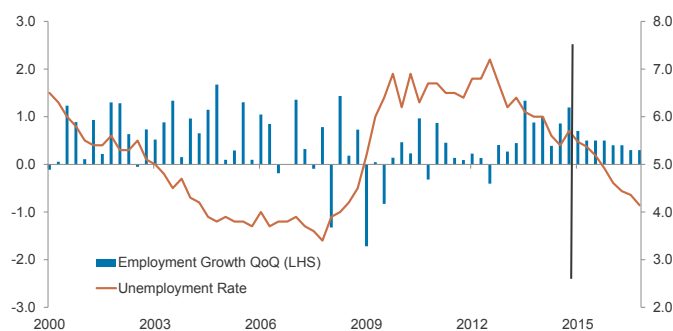
Australia labour market



Source: Australian Bureau of Statistics

6. Strong employment growth in New Zealand

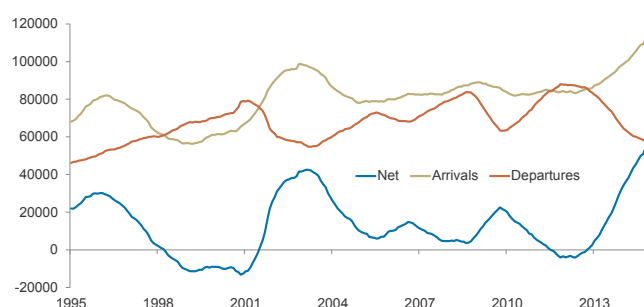
New Zealand labour market



Source: Statistics New Zealand and AMP Capital

7. NZ net migration continues to rise

NZ permanent and long term migration Number, year to date



Source: Statistics New Zealand

China

- > China reported disappointing January exports (down -3.3% year-on-year (yoy)), and imports (down -19.9% yoy). Both numbers were slightly distorted by Chinese New Year timing effects.
- > There was an element of soft demand domestically in terms of imports, with imports significantly reduced in value terms due to the drop in commodity prices, ie oil and iron ore. There was also soft demand more broadly, with global demand still yet to really take off.
- > The soft export and import data will likely underpin the need to maintain the present stimulus programme. A recent cut to the required reserve ratio has been followed by a second interest rate cut. Further interest rate reductions are likely.

Australia

- > The Reserve Bank of Australia (RBA) cut the official cash rate by 0.25% to 2.25% at its February meeting. The RBA justified the cut by stating that Australia's "output growth will probably remain a little below trend for somewhat longer and the rate of unemployment peak a little higher than earlier expected". An interest rate cut "is expected to add some further support to demand".
- > On cue, employment data for January showed some weakness (following three consecutive strong months) and an increase in the unemployment rate to 6.4%. We expect unemployment will move higher in coming months.
- > Australia still has considerable spare capacity in terms of labour supply which is suggestive of only mild wage and inflation pressures in 2015.

New Zealand employment

- > New Zealand's December quarter Household Labour Force Survey recorded strong employment growth of 1.2% over the quarter. Annual employment growth stands at 3.5%.
- > The labour force grew a seasonally adjusted 36,000 over the quarter to a record high thanks to a rise in the working age population and an increase in the participation rate to a record 69.7%. These factors conspired to deliver an increase in the unemployment rate to 5.7%, up from 5.4% in the prior quarter.
- > Wage inflation remained benign with the Labour Cost Index for all salary and wage earners up 1.8% over the year. While this might appear surprising given the strong growth in the economy, it remains a function of strong employment growth currently being met by the rising supply of labour.

New Zealand net migration

- > Net inward migration reached a peak of 53,797 in January 2015, up from 50,922 in the year to December 2014, and is likely to continue heading higher over the next few months.
- > This reflects New Zealand's strong relative economic and labour market performance, especially compared with Australia.
- > Strong population growth will continue to support growth in retail spending and contribute to the current supply/demand imbalance in the housing market. It also supports recent strong growth in the labour force which is helping keep skills shortages and wage pressures in check at a time of strong employment growth.

Market commentary

Global shares

The small decline experienced by global equities over January was quickly forgotten as markets rallied strongly over February, gaining 5.9%. Share markets in Europe led the way forward as investors reacted positively to the progress made in Greece and more monetary easing, this time in Sweden. European equities gained 7.4% over the month. US shares were also strong, with the S&P 500 gaining 5.7% helped by more benign comments from US Federal Reserve Chair Janet Yellen. Emerging markets lagged their developed market counterparts, gaining 3.3% over the month. At the end of the month China's central bank cut rates by 25 basis points, bringing the benchmark interest rate to 5.35%. This was their second cut in just over three months.

New Zealand shares

The New Zealand share market lagged its global counterparts, but still returned a solid 2.3% gain over February. The reporting season was the main focus over the month. Air New Zealand delivered a strong result in what have been highly favourable operating conditions. The backdrop for the company remains strong with growing demand and lower fuel prices. Air New Zealand shares rose 9.2% over the month. However, it was Xero which experienced the greatest share price increase over the month, gaining 57.9%. The company announced they had raised funding at a significant premium to the trading price, with the additional funding going towards its expansion into both the US and UK markets.

New Zealand listed property

After several months of strong performances, the New Zealand Property Index stumbled somewhat during February, experiencing a return of 0.0%. Augusta Capital, Property for Industry and NPT were the three strongest performing stocks, while CDL Investments and Precinct Properties were the laggards. Precinct Properties reported a gain of 10% on their distributable profit. However, this was largely overlooked by the market which focused on their 1 for 7 entitlement offer at a 6% discount to the share price.

Global bonds

Global bond yields bucked their recent trend and rose over February. Bond yields rose on the back of some solid data out of the US and good news on Greece as it received approval for a four month extension of its current loan programme. One exception were short term rates in Sweden, as their central bank cut its key interest rate from 0% to a record low of -0.1%. It also launched a programme of quantitative easing, buying government bonds worth 10 billion kronor. The US 10 Year Treasury closed the month at 1.99%, up 35 basis points over the month.

New Zealand bonds and cash

New Zealand Government bond yields rose over the month. The Reserve Bank of New Zealand (RBNZ) reinforced their "on hold for

some time" message delivering a more balanced tone. This saw shorter term rates little changed while longer term rates took its lead from offshore markets and rose over the month. The 90 Day Bank Bill yield fell 3 basis points to 3.63% while the New Zealand 10 year Government bond yield rose 11 basis points to 3.29%.

Commodities

The broad commodity index rose 2.8% over the month led by the energy sector. Oil prices received a boost after Saudi Arabia's Oil Minister, Ali Al-Naimi, stated that oil demand had picked up and that the world's largest oil exporter wanted to see "calm markets". On the flip side, coffee futures experienced the biggest decline as coffee exports from El Salvador rose 56% and Arabica coffee output in Rwanda is expected to jump sharply in 2015 due to the production of additional new plants.

Global listed property and infrastructure

Global listed property and global listed infrastructure declined over the month, falling 0.5% and 0.8% respectively. Relative to the broader equity market, listed property and infrastructure are generally lower risk stocks which provide a higher dividend. This means when bond yields rise the yield spread becomes less attractive to investors.

New Zealand dollar

The New Zealand dollar (NZD) closed the month higher against all the major currencies. The NZD moved closer to parity with the Australia dollar (AUD), finishing the month at \$0.9684, up 3.7%. The rise of the NZD against the AUD came after the RBA cut interest rates to a historic low of 2.25%. Against the US dollar the NZD finished up 4.2% for the month.

	As at 28 February 2015	Change over the month (%)	Change over the year (%)
MSCI - US	8072.21	+5.9	+15.3
MSCI - UK	12795.73	+3.3	+5.4
MSCI - Germany	3548.53	+6.7	+18.3
MSCI - Japan	1902.36	+8.0	+28.0
NZX50	5878.47	+2.3	+17.8
MSCI - World (local curr.)	5019.74	+5.9	+15.3
MSCI - World (NZD)	8774.75	+1.7	+20.3
NZ Official Cash Rate	3.50	0 bps	100 bps
NZ 90-day bank bill yield	3.63	-4 bps	66 bps
NZ 10-year bond yield	3.30	10 bps	-125 bps
US 10-year bond yield	1.99	35 bps	-65 bps
NZD-USD	0.7564	+4.2	-9.8
NZD (TWI)	78.2	+3.6	-0.7
NZD (MSCI weighted)	82.9	+4.2	-4.1

Contact us

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