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Commonwealth Financial Services

Quarterly Market Commentary as at 31 March 2010*

Market Indices	Returns as at 31 December 2009						
	1 mth (%)	3 mth (%)	6 mth (%)	1 yr (%)	3 yr (% p.a.)	5 yr (% p.a.)	10 yr (% p.a.)
Australian Shares							
S&P/ASX 200 Accum	5.75	1.36	4.80	41.71	-2.44	8.07	8.90
International Shares							
MSCI World Ex Aust (AUD) Net	3.52	1.12	3.24	14.47	-9.61	-0.83	-4.34
Australian Fixed Interest							
UBSA Composite Bond Index 0+ Yr	-0.58	1.26	2.30	2.73	6.51	5.99	6.28
International Fixed Interest							
Citigroup World Govt Bond 100% Hdg (AUD)	0.31	2.06	2.68	5.69	8.32	7.18	7.82
Property							
S&P/ASX 200 A-REIT	-0.05	-1.51	-6.44	40.55	-22.83	-6.95	3.65
Cash							
UBSA Bank Bill Index	0.33	1.02	1.92	3.54	5.73	5.84	5.59
Currency							
Australian Dollar ($A/$US)	2.50	2.06	4.00	32.10	4.35	3.48	4.22

Australian Shares

The Australian share market was fairly volatile during the March quarter. The year got off to a poor start, with the S&P/ASX 200 Accumulation Index declining 6.2% in January, but the market subsequently rebounded and was able to record a positive return in the period as a whole thanks to a strong rally in March. In the quarter as a whole, the market added 1.4%.

There was a fair degree of variance in the returns from individual sectors. The Health Care (+3.3%) sector was a notable outperformer, while the financials (+1.4%) sector also performed well, buoyed by gains in all four of the major banking stocks. Telecoms (-12.8%) was by far the worst performing area of the market, dragged lower by index heavyweight Telstra, while the energy (-1.3%) sector also underperformed despite the oil price rising 5.5%.

The key focus for investors during the quarter was the steady stream of earnings announcements which were released by listed companies for the December 2009 half year. The reporting season confirmed that the much-anticipated cyclical earnings upgrade cycle is yet to materialise. Indeed, close examination of companies' earnings releases highlighted that sales growth remains modest in most sectors. In many areas of the market, sluggish sales growth is being offset by lower operating and interest expenses, with companies continuing to drive earnings growth through reductions in costs.

International Shares

The MSCI All Countries World Index rose 3.1% in US$ and was up 1.1% when measured in A$ for the March quarter. Over 12 months, the index returned 14.5% in AUD terms and 55.5% in US$ with returns were held back in AUD due to gains in the Australian dollar. Over the quarter, the Australian dollar rose from US 0.8994 cents to US 0.9179 cents.

International sharemarkets added value in the quarter, assisted by a recovering global economy and rising investor confidence. The major economies recorded positive GDP growth rates in the Q4 and some are seeing falls in unemployment rates. Over Q4, GDP rates were recorded at 1.4% in the US, 0.1% in Europe, 0.4% in the UK and 0.9% in Japan.

In the US, company profits have recovered sharply, rising 31% for the 12 months to December 2009. This has largely been driven by aggressive cost cutting and improved productivity. As the economy continues to recovery, operating leverage is expected to provide upside potential for company profits. With profits returning this should encourage further business investment and jobs growth. The US equity market reached a new high since the low 12 months ago in March. Over the quarter, the Dow Jones Industrial Index rose 4.1%, the S&P 500 was up 4.9% and the NASDAQ Index rose 5.7%.

Markets in Europe were predominantly positive, although falls were experienced in markets plagued by sovereign risk concerns. Germany (+3.3%) and France (+1.0%) both rose. The UK FTSE 100 also added value, rising 4.9%. The UK economy is providing some signs of recovery with improving manufacturing output, assisted by recent falls in the sterling. Greece (-5.8%), Spain (-9.0%), Portugal (-4.4%) and Italy (-1.7%) all fell.

Asian markets were also mixed with Japan providing the strongest gains with some signs of a recovery in the economy. The Nikkei rose 5.2% and is now up 36.8% in 12 months. Thailand also recorded strong gains, up 7.3%. Hong Kong (-2.9%) and Singapore (-0.4%) both fell in the quarter despite economic strength in the region.

Australian Fixed Interest

In Australia, the focus remains on the pace of tightening of the official cash rate by the RBA, the pace of economic growth and prospects that the Federal Government Budget will return to surplus earlier than current projections, leading the total issuance of Commonwealth Government Securities lower than expected. The Federal Government will release its next Budget on 11th May 2010.

Ten year Australian government bond yields began the quarter at 5.64% and ended it at 5.78%, up from the low of 3.85% reached in January 2009. The return on the UBSA Composite Bond Index in the March quarter was 1.26%, with government bonds returning -0.91%, corporates 8.08% and semi government bonds 2.20%. Returns reflect the rise on Commonwealth Government securities across all maturities, but narrowing spreads on semis and corporates. These trends reflect improving economic conditions and rising demand for riskier assets.

International Fixed Interest

There was a marked difference of performance among the major global bond markets during the March quarter. Different countries' yields were driven variously by sovereign risk concerns, the implications of central banks implementing strategies to exit financial rescue packages and unfolding evidence about the strength of global economic fundamentals.

Several central banks continued to exit from financial rescue strategies, in some cases tightening liquidity conditions. The US exited various extraordinary stimulus programs, while in Australia the RBA continued its monetary policy tightening. China and the UK also undertook policy measures to withdraw stimulus from financial markets.

The most significant decline in bond yields was recorded in Germany, which experienced an intra-European 'flight to quality' as trading flows out of countries experiencing sovereign risk concerns and some risk assets into 'safer' countries helped to see yields fall in major European markets. The UK also participated to some extent in this flight to quality, but faces its own public debt level concerns amid continuing weak economic data.

US ten year bond yields ended the quarter with little change at 3.83%, though as March drew to a close, sentiment was beginning to be dominated by emerging evidence that the economy is recovering more strongly. In Europe, 10-year bond yields rose fell 3.39% to 3.09%. The notably rising spread between Greek and German bonds with continued issues in Greece has flowed into the second-quarter prompting details of a concrete rescue plan should Greece seek assistance. In the UK, 10-year yields rallied in the long end of the yield curve, with yields falling from 4.02% to 3.94%.

Australian Property (including Listed and Direct)

Listed property stocks underperformed the broader Australian share market in the March quarter of 2010, with the S&P/ASX 200 Property Accumulation Index declining 1.5%. Stocks with significant office property exposure performed particularly poorly, while those in the industrial sector fared somewhat better.

Encouragingly, a number of significant transactions of commercial property were agreed during the period. The prices achieved for these sales suggested that the decline in asset values is close to an end, which should help restore investor sentiment towards the sector. Demand is also expected to be supported by improving economic conditions.

The announcement of Australian listed property companies' earnings from the December 2009 half year dominated investor attention during the period. Few companies reported earnings which materially exceeded consensus expectations but, importantly, few companies disappointed investors with unexpectedly bad results.

Cash

The UBS Australia Bank Bill Index returned 1.02% in the quarter and 3.54% over 12 months. The returns from this index reflect interest earnings on short term money market securities and reflect the recent low level of the official cash rate. Ninety day bank bills rose over the quarter, beginning the quarter at 4.28% and ended it at 4.49% with the RBA lifting the official cash rate by 0.25 basis points to 4.0% in the March quarter and again in April to 4.25%. The average ninety day bank bill yield during the quarter was 4.23%, compared with 3.36% a year earlier.

As we look into 2010, yields will be affected by the pace of RBA tightening interest rates, the pace of growth in the Australian economy and the speed at which capacity constraints are faced.

Currency

The AUD rose in the March quarter, with the strongest gains recorded against the pound and the euro given sovereign debt concerns in these regions. The AUD finished the quarter at US0.9179 cents, a gain of 2.1%. The AUD continues to be supported by economic growth, higher official interest rates and commodity price gains.

The AUD rose 8.2% against the euro, 2.6% against the yen and 8.6% against the British pound. The AUD also rose 4.5% against the New Zealand dollar.

At the end of March 2010 the AUD was buying 1.2945 New Zealand dollars, 85.79 yen, 0.6037 UK pence and 0.6782 EUR cents.