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Commonwealth Financial Services

Quarterly Market Commentary as at 31 March 2009*

Market Indices	Returns as at 31 March 2009						
	I 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	7.98	-1.98	-19.87	-29.52	-7.25	5.50	6.12
International Shares							
MSCI World Ex Aust (AUD) Net	-1.40	-11.92	-21.90	-24.48	-13.17	-1.84	-3.33
Australian Fixed Interest							
UBSA Composite Bond Index 0+ Yr	0.12	0.28	6.63	12.77	6.84	6.41	6.19
International Fixed Interest							
Citigroup World Govt Bond 100% Hdg (AUD)	1.23	0.31	7.04	10.02	8.44	7.55	7.50
Property							
S&P/ASX 200 A-REIT	-0.04	-24.37	-49.23	-57.64	-25.12	-9.88	0.28
Cash							
UBSA Bank Bill Index	0.26	0.96	2.67	6.69	6.63	6.25	5.76
Currency							
Australian Dollar ($A/$US)	8.76	-0.34	-11.92	-23.89	-0.86	-1.87	0.96

Australian Shares

The Australian sharemarket fell over the quarter, with the S&P ASX 200 Accumulation Index down 2.0%. Over 12 months the sharemarket was down 29.5%. The global recession, a slowing Australian economy, reduced company profitability and continued issues in the global financial system saw sharemarkets retreat.

Australia's economic growth figures (as measured by gross domestic product, GDP) was weaker than expected at -0.5% for the December quarter 2008 (versus +0.1% for the September quarter). This took the annual pace of growth to just 0.3%, the lowest rate since the end of 1991 (the last recession).

On the policy side, the Federal Government announced a new $A 42 billion spending package over four years. Around $A 12 billion will be spent on cash handouts to provide an immediate boost to economic growth and around $A 28 billion will be spent on infrastructure projects over the coming years. The Reserve Bank of Australia (RBA) also cut official interest rates from 4.25% to 3.25% as economic conditions worsened globally, impacting on Australia.

The resource sector was the best performer over the quarter, rising 7.7% with commodity price gains. Signs of stabilisation in the Chinese economy with some positive economic indicators released led to the rebound in the market and as coking coal contract prices were settled at better than expected levels. The large miners, Rio Tinto (+51.5%) and BHP Billiton (+7.0%) led the sector.

Leading the market lower was the industrials sector, which fell 19.2% over the quarter. The sector has been weighed down by the slowing Australian economy, weaker outlook for company profits and concerns over debt levels. The February profit reporting season indicated that the sector had suffered from the downturn with the share prices of Transpacific Industries (-44.8%), Asciano Group (-39.7%) and Brambles (-33.0%) falling.

Among the top 20 companies, top performers included Commonwealth Bank of Australia (+24.1%), Wesfarmers (+13.2%) and Westpac Banking Corporation (+12.5%). The announcement of the Public Private Investment Program (PPIP) and the Financial Stability Plan out of the US and suggestions some US banks returned to profitability to date in 2009 buoyed share prices in the major banks.

As debt financing remains challenging and expensive, companies turned to the equity market over the quarter. Those companies that undertook equity raisings generally faired less well with heavy discounts offered to entice investors. AXA Asia Pacific (-29.3%), Suncorp-Metway (-21.8%) and Bank of Queensland (-15.1%) all fell with equity raisings over the quarter.

Late in the quarter some hints of optimism returned to sharemarkets and while this has provided the market with hope, caution is needed. Economic data in Australia is likely to get worse over coming months, reflecting the force of the global recession. While the sharemarket appears to have factored in much of the expected bad news, low confidence and risk aversion may take over and the sharemarket could retreat again. Nevertheless, recent aggressive policy actions in the US and UK are positive and should make a difference over time and help the global economy recover in 2010 and beyond.

International Shares

International sharemarkets were weaker in the March quarter. Despite the falling Australian dollar Australian investors still received negative returns.

The MSCI All Countries World index fell 11.9% in $US and was down 11.6% when measured in Australian dollars. Over 12 months, the index was down 24.6% in $A terms. During the quarter, the Australian dollar was only marginally lower from US 70.46 cents to US 69.27 cents.

International sharemarkets had to deal with a global recession and continued upheaval in credit markets. Markets were volatile with growing concerns over government takeover of some large US banks with further capital needed to ensure survival. Uncertainty over the future of policy action also led to falls and it wasn't until several major policy announcements, the Financial Stability Plan, Public Private Investment Program (PPIP) and quantitative easing that sharemarkets responded.

Over the quarter, the Dow Jones Industrial index fell 13.3%, the S&P 500 was down 11.7% and the NASDAQ index fell 3.1%. Over 12 months the Dow Jones Industrial index is down 38.0%.

Markets in Europe were all down with the economy in recession and concerns over Eastern European debt levels. The policy response to date out of Europe has been muted compared to counterparts prolonging the potential for quick economic recovery. The DAX Index fell 15.1%, while France was down 12.8%.

In the UK, the FTSE 100 index fell 11.5%. The Bank of England cut interest rates from 2.00% to 0.50% over the quarter, as well as introduced quantitative easing. The UK sharemarket is dealing with tight financing conditions and a recession.

Asian markets fared slightly better over the quarter. Japan's Nikkei index fell 8.5% and reached its lowest level since 1983. The Japanese economy is in recession, weighed down by sharp fall in trade and manufacturing. The Nikkei is down 35.3% over 12 months. Hong Kong (-5.6%) and Singapore (-3.5%) both fell while China rose 45.2%. Chinese stimulus policies have started to work with the economy showing signs of improvement. Emerging Markets outperformed, rising 2.2% in $A on some risk taking.

The outlook for the global economy in the remainder of 2009 is weak and this will impact on profit outlook for companies. The good news is that the policy response has been aggressive and quick and this has started to lift optimism. While this is positive, there is the possibility that the global recession may be more prolonged than expected and this could lead to further volatility on sharemarkets.

Australian Fixed Interest

Policy makers continue to work overtime to support their financial system and encourage economic growth. Credit markets remained unsettled over the quarter as issues within the US banking system were worked through. In Australia, the Commonwealth Government guaranteeing State government debts, both new and existing, for a fee and on a voluntary time limited basis. This followed several months of dysfunction within the semi-government bond sector.

The RBA reduced its official cash rate from 4.25% to 3.25% over the quarter with a 1.00% cut in February. Rates were on hold in March. In cutting interest rates the RBA noted the weakening outlook for Australian growth given the severe global downturn and substantial falls in commodity prices. When leaving interest rates on hold in March the RBA noted the significant stimulus from lower interest rates and government spending packages.

In Australia, the return on the UBSA Composite Bond index 0+Yr in the March quarter was 0.28%. Over the 12 months to 31 March 2009 the return on the index was 12.77%.

Ten year Australian government bond yields began the quarter at 3.99% and ended it at 4.42%. Corporate bond yields rated BBB- to BBB+ saw yields rise from 8.40% at the end of December 2008 to 10.72% by the end of March 2009.

International Fixed Interest

Lower yields on foreign government bonds (higher bond prices) added to ongoing interest income and resulted in a strong positive return from international bonds during the December quarter. The Citigroup World Government Bond index (ex Australia) Hedged rose 0.31% for the quarter and returned 10.02% over 12 months.

The demand for government bonds increased dramatically over the quarter, pushing yields to levels not seen since the 1950s in the US. Investors became extremely risk averse in October and November and sold lower rated corporate bonds, causing their yields to rise.

Over the quarter, ten-year US government bond yields fell from 3.82% to 2.21% and in the Euro zone similar bond yields fell from 4.02% to 2.95%. In the UK, yields fell from 4.45% to 3.02% while in Japan they declined from 1.47% to 1.17%.

Official interest rates were cut sharply around the world in the December quarter as the outlook for economic growth diminished sharply. In the US, official interest rates were cut from 2.00% to a target of 0.0% to 0.25%. In the UK, the Bank of England cut rates from 5.00% to 2.00%. The European Central Bank and the Bank of Japan also reduced interest rates. Cash rates stand at 2.50% in the Euro zone and 0.10% in Japan.

Looking ahead into 2009, the key issue will be the global economic slowdown and the switch from focussing on inflation to growth.

Australian Property (including Listed and Direct)

The Mercer Direct Property index fell 2.7% in the quarter to be down 5.2% over 12 months while the S&P/ASX 200 A-REIT Accumulation index fell 24.4% in the quarter to be down 57.6% over 12 months.

The industrial sector was the worst performing sub-sector over the quarter, down 53.0%. The sector was weighed down by weakening demand for industrial properties and issues within specific industrial REITs. The office (-31.7%), diversified (-29.3%) and retail (-18.4%) sub sectors all fell.

The better performers over the quarter were Abacus Property Group (+46.9%), Macquarie CountryWide Trust (+14.3%) and Bunnings Warehouse Property Trust (-4.9%). The bottom performers were Goodman Group (-56.1%), GPT Group (-50.4%) and ING Office Fund (-44.9%) with concerns over debt issues, falling prices and distribution cuts.

Concerns are held over the ongoing viability of several REITs given falling property prices, weak economic conditions and capital requirements. Balance sheet risk is the main concern with property income holding up relatively well. The Australian direct property trust sector has started to fall as property prices are re-valued downwards with the slowing Australian economy.

Cash

The UBS Australia Bank Bill index returned 0.96% in the quarter and 6.69% over the past 12 months. The returns from this index reflect interest earnings on short term money market securities.

Ninety day bank bills fell sharply over the quarter. They began the quarter at 4.15% and ended it at 3.14% as the RBA cut official interest rates aggressively and inflation concerns receded. The average yield during the quarter was 3.36% compared with 7.57% a year earlier.

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After being much of the focus for 2008, new inflation figures released in Australia over January indicated the risk of inflation was diminishing. The Consumer Price Index rose 3.7% for the 12 months to December, down from its high of 5.0% for the 12 months to September 2008. Lower inflationary pressures have assisted the substantial interest rate cuts by the RBA.

Currency

The Australian dollar ($A) fell 1.7% against the US dollar ($US) during the quarter. It began the period at US 70.46 cents and ended it at US 69.27 cents. Over the quarter the $A traded with volatility, reaching as high as US 71.18 cents and as low as US 63.09 cents. The $A rallied late in the quarter as the US introduced quantitative easing and as some risk appetite slowly returned to markets.

In the March quarter the $A rose 7.8% against the UK pound as the Bank of England cut interest rates aggressively and introduced quantitative easing. The $A fell 4.7% against the New Zealand dollar; but was up 9.0% against the Japanese yen and 3.3% against the euro.

At the end of March 2009 the $A was buying 1.2189 New Zealand dollars, 68.82 yen, 0.4844 UK pence and 52.36 euro cents.ghgh