

How the different asset classes have fared:(As at 31st December 2017)

Asset Class	10 Yr % p.a.	5 Yr % p.a.	3 Yr % p.a.	1 Yr %	YTD %	6 Mo %	3 Mo %	1 Mo %
Cash ¹	3.6	2.3	2.1	1.7	1.7	0.9	0.4	0.1
Australian Bonds ²	6.2	4.2	3.1	3.7	3.7	1.4	1.4	-0.5
International Bonds ³	7.1	4.9	4.1	3.7	3.7	1.8	0.9	0.2
Australian Shares ⁴	4.0	10.4	9.2	12.5	12.5	9.3	8.2	2.0
Int. Shares Unhedged ⁵	6.3	18.4	11.0	13.4	13.4	8.5	5.8	-1.7
Int. Shares Hedged ⁶	7.8	15.7	11.5	20.3	20.3	10.2	5.6	1.1
Emerging Markets Unhedged ⁷	2.9	10.4	10.8	27.1	27.1	13.7	7.8	0.5
Listed Infrastructure Unhedged ⁸	N/A	16.5	8.1	9.4	9.4	2.4	2.3	-4.6
Australian Listed Property ⁹	1.8	13.4	11.3	6.4	6.4	9.9	7.8	0.1
Int. Listed Pty Unhedged ¹⁰	N/A	13.0	5.5	-1.1	-1.1	2.1	3.4	-1.8

¹Bloomberg AusBond Bank 0+Y TR AUD, ²Bloomberg AusBond Composite 0+Y TR AUD, ³Bloomberg Barclays Global Aggregate TR Hdg AUD, ⁴S&P/ASX All Ordinaries TR, ⁵MSCI World Ex Australia NR AUD, ⁶Vanguard Intl Shares Index Hdg AUD TR, ⁷MSCI EM NR AUD, ⁸FTSE Developed Core Infrastructure 50/50 NR AUD, ⁹S&P/ASX 300 AREIT TR, ¹⁰FTSE EPRA/NAREIT Global REITs NR AUD

Cash

The RBA maintained cash rates at a record low of 1.5% for the whole of 2017. It is still unlikely that the Reserve Bank will raise rates in the foreseeable future with Australian household budgets under pressure. Workers are seeing little or no wage increases in real terms (i.e. after taking into account inflation). Meanwhile, regulatory efforts to clamp down on excessive borrowing (a.k.a. 'macroprudential controls') have driven up the ongoing cost of many mortgages while increases in the cost of major spending items, like energy, eat into disposable income.

We do not forecast interest rate increases in 2018 because we do not see an end to these pressures on the Australian consumer. Wage growth is likely to stay meagre as it has in other developed markets where unemployment has either fallen further or faster than in Australia while real wage growth has barely moved. Credit growth still exceeds GDP growth in Australia even though the regulator's efforts to stamp out risky borrowing has seen residential property price inflation dissipate in recent months. Further controls on lending and a flattening out (and even falls) in property prices may also reduce consumers' appetite to spend in 2018.

Bonds

Australian and international bonds finished the quarter largely flat. Concern about the sustainability of exceptionally low yields will likely dominate the news cycle in 2018 as central banks gradually reduce their holdings of fixed-income assets, reversing the 'quantitative easing' measures designed to stoke a post-crisis recovery. At the end of 2017, fixed-income traded sideways as the European Central Bank and Bank of Japan's substantial purchases and the puzzling lack of inflation in the U.S. continued to place downward pressure on yields. Investors remain alert to the prospect that a sudden increase in inflation or unexpectedly restrictive money-market conditions created by central-bank 'quantitative tightening' could lead to a sudden bond-market sell-off (i.e. a spike in yields) in 2018/19.

International Shares

International shares finished the year on a high note, buoyed by unemployment, manufacturing and consumer surveys in the US, Europe and Asia that signalled a healthy global economic expansion. Hedged returns conspicuously outperformed unhedged equities after the Australian dollar rallied from a low of \$0.75 in the final month of 2017.

Emerging Markets

Emerging markets finished the year on a high note with strengthening EM currencies, accelerating manufacturing output and a positive global outlook generating stellar returns for EM investors. Markets shrugged off concerns about the potential, adverse effects of U.S. interest-rate hikes on EM stocks and markets rallied into the new year.

Australian Shares

The final quarter of 2017 was a strong one for Australian shares. The All Ordinaries rallied 8% in the last quarter supported largely by a rally in resource stocks and outperformed all other asset classes in the final month of 2017.

Australian Listed Property

The rally in Australian listed property petered out at the end of 2017. Frank Lowy's headline-grabbing sale of Westfield to Unibail-Rodamco underscored a transition underway in AREITs, which are likely to face headwinds as growing competition from online retailers places downward pressure on commercial rents and highly indebted Australian households make for a circumspect consumer.

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