RHODES DOCHERTY & CO
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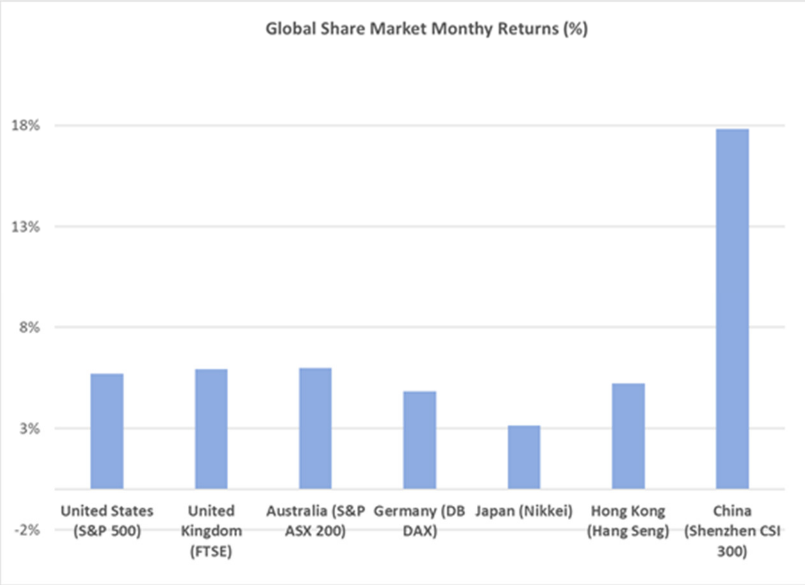
February 2019 Review – Markets continue strong recovery

The share market recovery experienced in January picked up further pace in February with leading indices across the globe recording solid gains. Some of the notable developments for the month included:

- Positive sentiment stemming from the hope of a trade agreement between the US and China
- Global bond yields remained steady, while Australian yields fell
- The benign outlook for interest rates supported listed infrastructure and property
- Australia's financial sector experienced a recovery on the less significant than feared Royal Commission recommendations

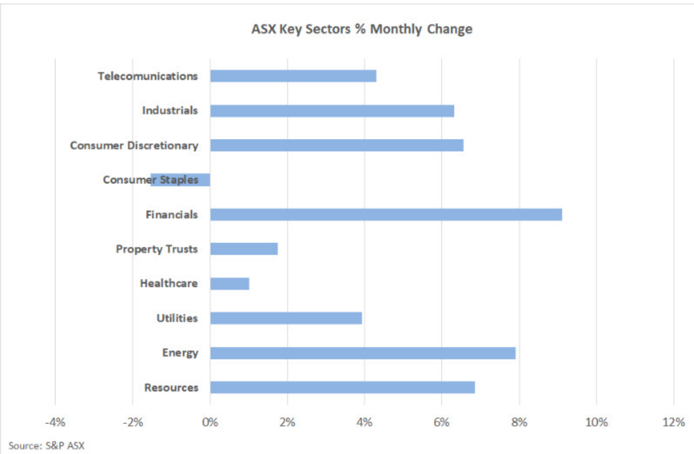
Over February, global equity markets continued the rally that commenced at the start of 2019, finishing 3.4% higher in in hedged currency terms. The rally came in response to further indications that the U.S central bank was more willing to avoid further interest rate increases than previously thought. In addition, news that negotiations between the US and China were progressing towards some form of agreement was also a major impetus to confidence. President Trump had been threatening to increase tariffs on over U$ 200 billion of Chinese imports from the current 10% to 25% level from the 1st of March. The Chinese Shenzhen CSI 300 Index rallied nearly 18% on the expectation this would be avoided. Chinese market sentiment was also supported by ongoing domestic economic stimulus, with President Xi Jinping looking to quicken the pace of development of the domestic financial services industry in particular. Chinese economic growth for the fourth quarter was 1.5%, creating an annual growth rate of 6.4% for 2018.

Asset Class Return	Feb-19	3 Months	Annual
Australian Equities	6.0%	9.9%	7.1%
Global Equities - Unhedged	5.6%	5.2%	10.1%
Global Equities - Hedged	3.4%	1.5%	2.4%
Australian Listed Property	1.8%	9.9%	19.1%
Global Listed Property	0.3%	3.7%	16.8%
Global Listed Infrastructure	2.9%	4.9%	7.9%
Australian Fixed Interest	0.9%	3.1%	6.2%
Global Fixed Interest	0.1%	2.5%	3.7%
Cash	0.2%	0.5%	2.0%



The US market rose a healthy 5.7%, despite reporting a slower than expected 2.6% annualised economic growth rate in the fourth quarter. In comparison, European growth remained in the doldrums, being reported at just 1.2% for 2018. Germany, Europe's largest economy, had a flat December quarter, after a negative 0.2% the previous quarter, and hence averted a recession. Not so Italy, where a negative 0.2% growth in the final quarter confirmed the economy was in recession. The U.S. – China trade restrictions appear to be having a second round negative effect on European exports to China. Nonetheless, the German market was pushed higher (up 4.8%) off the back of the global rally. In the UK, the Brexit date looms with no clear path to future trade integration with the EU and the impasse is now beginning to fracture both major political parties. But here too the market enjoyed a solid performance, rising 5.9%. Emerging markets were flatter than developed markets, despite China's strength over the month. Weakness on the Brazilian market contributed to the overall emerging market average being higher by just 1.1%.

On commodity markets, oil prices continued their recovery during the Northern Hemisphere winter, with West Texas Intermediate increasing to U$ 57 per barrel - a rise of 6.3%. Gold closed at U$1,313 (down 0.5%), whereas base metals all gained. Zinc (up 2.7%), Copper (up 6.3%), Aluminium (up 0.7%), Tin (up 4.1%) and Nickel (up 5.3%) all showed evidence of positive market sentiment. Iron ore, though, eased 1.2% over the month, following the 21% spike in prices in the aftermath of the tragic Brazilian Vale dam collapse in the previous month. China's apparent decision to limit the flow of Australian coal through one port is not proving to be a material concern to markets at this point. Chinese imports of coal had been running ahead of their usual pace and a slow-down may be part of an attempt to normalise flows.



Generally strong commodity prices helped support the Australian share market, which enjoyed a solid month in February, advancing 6.0%. After a period of some underperformance, smaller companies outperformed their larger counterparts with a 6.8% gain. Financials were the big winner off the back of the release of the Hayne Royal Commission report. Though the Commission's report called for some change in the wealth industry, it stopped short of advocating an end to vertical integration (the practice of advice businesses and fund managers being ultimately owned by the same institution). The big four banks were the major beneficiaries. Information

Technology was the next best sector, following the global trend to be 7.6% higher. Resources continued to advance, rising 6.3%. Similarly, firmer oil prices contributed to a 7.9% jump in the energy sector. Resources have been the strongest sector over the past three months, rising by an impressive 22.6%. Conversely, Consumer Staples fell 1.5% in February and was the weakest sector for the month as well as the past quarter (rising only 2.7%).

Australian longer term interest rates again moved lower as further softness in the local economy increased the probability of a future cash interest rate reduction. The Australian 10-year Government bond yield declined 0.14% to 2.10%. Conversely, US 10-year Treasuries rose 0.10% to 2.73%, thereby reversing some of the previous month's decline. This has seen the spread between US and Australian interest rates widen further to 0.63%. This growing spread in longer term rates, along with the strengthening expectation for lower Australian short-term interest rates, saw the $A fall U.S. 1.2 cents to U.S. 71.5 cents last month.

Outlook and Portfolio Positioning

The ongoing rally across global equity markets has once again pushed valuations to the upper ranges of fair value. These higher valuations increase the vulnerability of share markets to a correction in the months ahead. Potentially, financial markets have become too optimistic that the period of rising U.S. interest rates is behind us. Should further inflationary pressure emerge in the U.S., then the central bank may have little option other than to raise interest rates. Such a course of action would be negatively received by both equity markets and bond markets.

Domestically, there are fewer concerns around rising interest rates, given the subdued outlook for economic growth and ongoing lack of any inflationary pressure. The weak growth cycle does contain risks for parts of the local equity market, with the housing down turn also justifying ongoing low valuations for the banks. With the growth in resource sector values over recent months, the opportunity presented by strong demand and prices appears fully reflected in valuations.

Given the global and domestic concerns outlined above, our portfolio positioning remains relatively cautious with overweight equity and bond positions being avoided. Holdings of cash and Alternative assets are being maintained, providing a potential source of funding should opportunities emerge to purchase equities and bonds at cheaper prices over the course of 2019.

Important Information

The following indexes are used to report asset class performance: ASX S&P 200 Index, MSCI World Index ex Australia net AUD TR (composite of 50% hedged and 50% unhedged), FTSE EPRA/NAREIT Developed REITs Index Net TRI AUD Hedged, Bloomberg AusBond Composite 0 Yr Index, Barclays Global Aggregate ($A Hedged), Bloomberg AusBond Bank Bill Index, S&P ASX 300 A-REIT (Sector) TR Index AUD, S&P Global Infrastructure NR Index (AUD Hedged).