



Investment market update December 2009 *(Prepared by FSS Trustee Corporation)*

The signs of recovery are there

After a deep global recession that began in 2007, economic growth has turned positive, at least partly in response to government intervention and spending that has supported demand and lowered uncertainty and risk in markets. But the recovery is expected to be slow as financial systems remain weak and emergency levels of government spending are withdrawn.

The global economy appears to be expanding again, propped up by the strong performance of the Asian economies and more stable conditions and even modest recovery elsewhere. Looking ahead, the policy forces that are driving the current rebound are expected to gradually lose strength as governments around the world tighten the purse strings. Also, consumption and investment are only slowly improving as financial conditions remain tight in many economies.

So after a contraction of around 1% in 2009, global activity is forecast to expand to about 3% in 2010, which is a big improvement on the previous year but well below the growth rates achieved before the crisis.

Despite the positive economic news, global markets are still nervous. The recent debt deferral in Dubai and similar signals in Greece suggest that the huge levels of government debt will be an issue for some time to come.

And in Australia... better news for super funds but caution prevails

Super funds on the whole have posted excellent returns since their March 2009 lows as share markets around the world have continued to strengthen. Most "balanced" investment options hold around a third or more of their money in shares so the better performance of share markets since March has helped this performance.

But the recovery is fragmented. Many overseas economies are recovering more slowly than Australia and this, together with the implications of the rising Australian dollar, is an important consideration, particularly for any fund investing offshore.

While we support the outlook for a mild recovery during 2010, we are maintaining a cautious investment approach. We are keeping our investment portfolios very liquid, which means holding reasonably high levels of cash. This gives our investments some degree of protection from adverse market movements and avoids the possibility of having to make forced asset sales at less than satisfactory prices. It also allows us to respond to investment opportunities that might arise as part of any recovery.

Local cash rates are still at relatively low levels but they are rising. Fixed income assets such as government bonds have helped us through the crisis, but in an environment of rising rates, the risk of holding fixed income assets rises accordingly. There will be opportunities in share markets as part of any recovery, but there are concerns around companies with big debt levels and their ability to arrange re-financing if this becomes necessary, which could contribute to short term market volatility.

The conclusion

Investment returns in 2009-10 should be substantially better than the previous two financial years, but we will continue to proceed with caution as investment markets digest the strength and durability of the recovery.

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