Economic update

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Brian reviews events in Australian and overseas markets during June.

How did markets perform in June?

Of the major asset classes, Australian shares lost ground in June, but all the other asset classes produced a positive return over the month. The decline in local share prices was quite broadly-based, with most sectors weaker in June.

Australian real estate trusts posted a particularly good return of 3.3% for the month. This is quite a turnaround as listed real estate in Australia has lagged both the broader share market and global real estate securities over the past year.

Global share markets performed reasonably well in June, even though a stronger Australian dollar took some shine off unhedged global share returns.

What were the key factors driving global markets?

We're still in an environment where the actions of the central banks are critical for financial markets. As I've said before, even though the US Federal Reserve is gradually unwinding its quantitative easing program, the reality is that monetary policy is still extremely accommodative. Official interest rates are still very low across the world – or virtually zero in some cases – and that's still a very positive environment for share markets.

And this month, the European Central Bank took steps to inject more liquidity into the banking system and encourage banks to expand their lending. But they still fell short of introducing a quantitative easing program such as we've seen in the US, Japan and elsewhere.

Perhaps the most surprising aspect of the way markets are performing is that events in the Ukraine and (even more worryingly) in Iraq haven't unsettled markets as much as we might have thought. Whether markets are right to be so relaxed remains to be seen.

What about developments in Australia?

The overall economy started 2014 on a fairly strong note. If you look at Australia's headline economic growth rate, the economy has accelerated over the past year or so, but the more recent data have been a bit mixed. The key issue for the Australian economy is the one I've mentioned often. On the one hand, mining investment is declining, and is going to be an ongoing drag on growth. But on the other, can the combination of exports and the non-mining economy pick up soon enough and fast enough to offset that? The jury is still out on that.

How are MLC's portfolios positioned?

Share markets look – at the very least – fully priced to us, but if monetary conditions remain supportive, share markets could continue to rise for some time.

Our broad positioning in portfolios hasn't changed significantly in recent months, either in MLC Horizon or in Inflation Plus. Across all our multi-asset portfolios we remain defensively positioned in world bond markets, since we still expect poor future returns from government bonds. And we still favour a range of foreign currencies over the Australian dollar, which continues to look very vulnerable in a number of adverse potential scenarios.

In the MLC Inflation Plus Conservative and Moderate portfolios, we're still holding significant allocations to cash and short-term Australian corporate bonds.

What this positioning means is that if share prices continue to rise, the MLC Inflation Plus portfolios will still deliver solid absolute returns, but they'll underperform the MLC Horizon portfolios. However, if we see a significant fall in share markets, the MLC Inflation Plus portfolios are likely to perform significantly better than the MLC Horizon portfolios.