

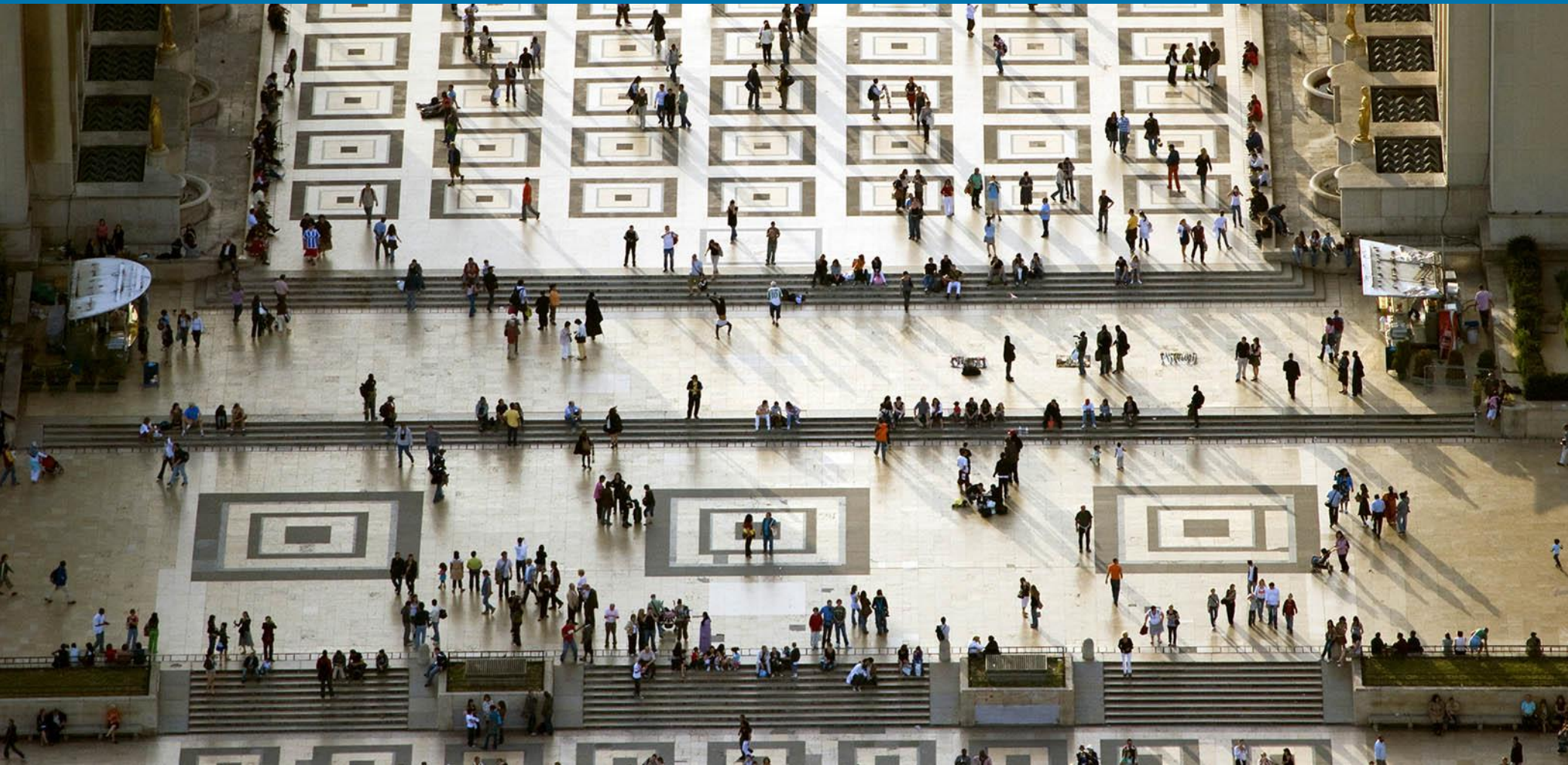
THE MACRO INVESTMENT OUTLOOK



AUGUST 2016

DR SHANE OLIVER

HEAD OF INVESTMENT STRATEGY AND CHIEF ECONOMIST



MEDIUM TERM MACRO SCENARIOS

MUDDLE THROUGH – 70% PROBABILITY

- > Continued recovery, albeit uneven and messy
- > Fed very gradual, global monetary conditions to remain easy
- > Search for yield to continue

GLOBAL BOOM, THEN HIGHER INFLATION – 10% PROBABILITY

- > Growth surprises on the upside (4% plus globally)
- > Inflation picks up quickly, synchronised monetary tightening in 2017
- > Bad for bonds, yield investments under rising pressure, trouble for shares

POOR GROWTH/G3 DEFLATION – 20% PROBABILITY

- > A new downturn – Eurozone risk, China, energy blow up, Fed policy mistake, emerging mkt crisis
- > More easing from Fed
- > Shares fall into significant bear market/growth assets weak, but bonds supported

KEY 2016 RISKS AND MAIN THINGS TO WATCH

Key 2016 risks

- > The Fed and rate hikes
- > Low oil prices could cause more weakness in credit markets
- > Political uncertainty eg. Eurozone, US, Brexit contagion, Australia
- > Chinese growth disappoints
- > Plunging emerging market currencies
- > Weaker Australian economic growth due to lower commodity prices and loss of momentum in housing
- > More geopolitical flare ups
- > Factor X

Main things to watch

- > The Fed – US inflation is key
- > US dollar – particularly against RMB
- > Bond yields in Spain and Italy, Eurozone banks
- > The oil price
- > Global PMIs
- > Chinese manufacturing conditions
- > \$US funding stress in emerging countries
- > Business confidence and non-mining investment in Australia

ECONOMIC AND INVESTMENT OUTLOOK

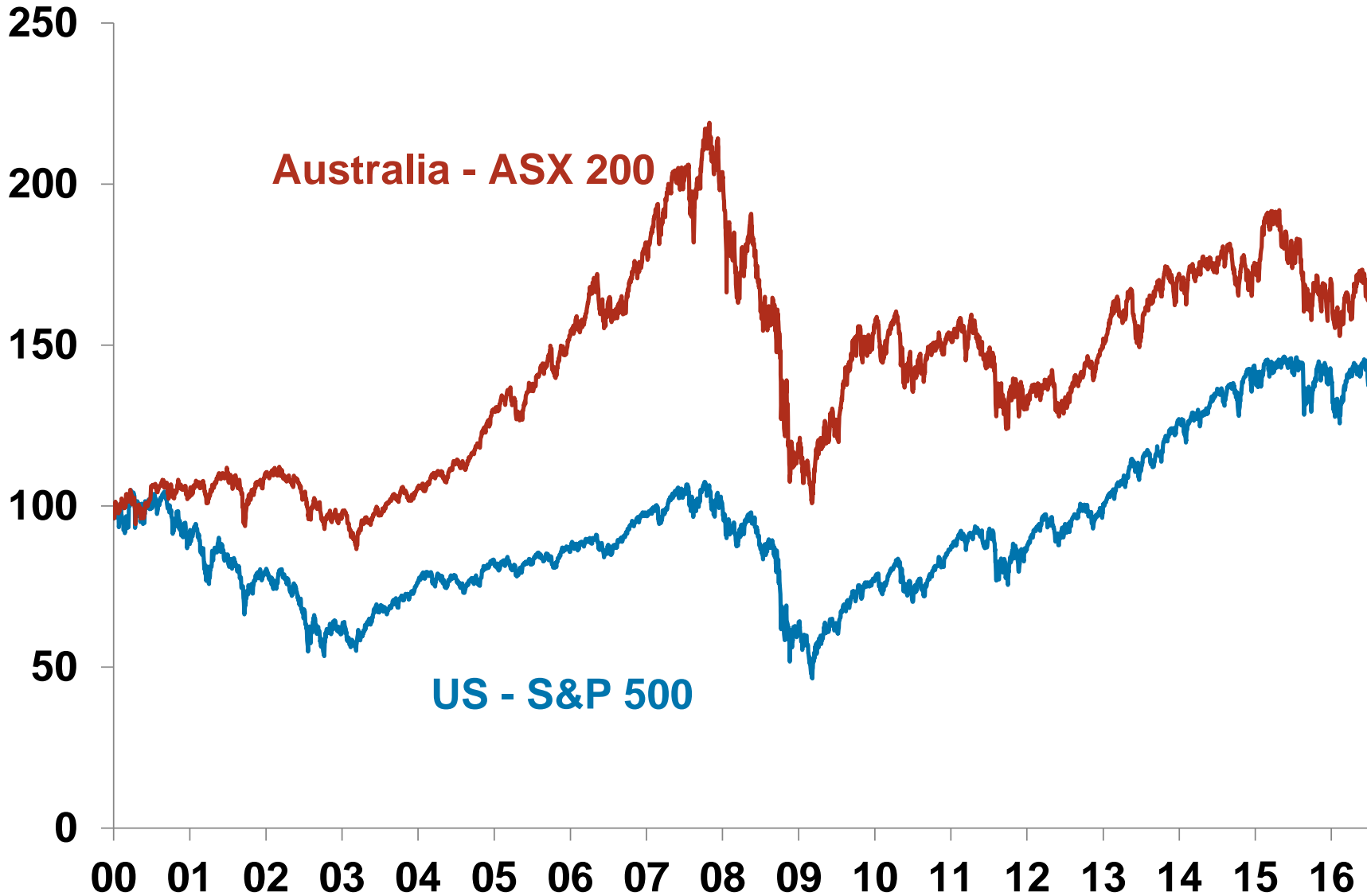
- > Okay but uneven global growth – 2016: 3%, 2017: 3.0%
- > 2016 GDP growth. China 6.5%, US 2%, Eurozone 1.6%, Japan 1%, Australia 2.9%
- > Interest rates to remain low, maybe only one Fed hike this year, further easing likely from ECB, BoJ, PBOC and RBA
- > \$A still headed down - to around \$US0.60 in the years ahead
- > Bonds and term deposits offer low returns
- > Shares up from early 2016 lows but uncertainty still remains in markets. August & September are also often rough for shares. Beyond near-term uncertainties, shares should provide decent returns as global recession is avoided
- > Key risks: the Fed, China, Italian banks/Eurozone, Australia post mining boom/post messy election

LOTS OF NOISE – THE WORRY LIST OF THE LAST 2 YEARS

- > End of US QE
- > Ukraine
- > IS terror threat
- > Ebola
- > Deflation
- > Commodity/oil crash
- > Greece
- > China worries – shares, debt, property, currency
- > Worries about Australian recession, property crash, banks
- > Brazil & Russia in recession
- > Worries about energy producers defaulting
- > Manufacturing slump globally
- > Trump
- > Worries about Fed raising rates/rising \$US
- > Soft starts to the year for US growth
- > Falling profits
- > Brexit
- > Messy Australian election result
- > South China Sea tensions
- > An attempted coup in Turkey

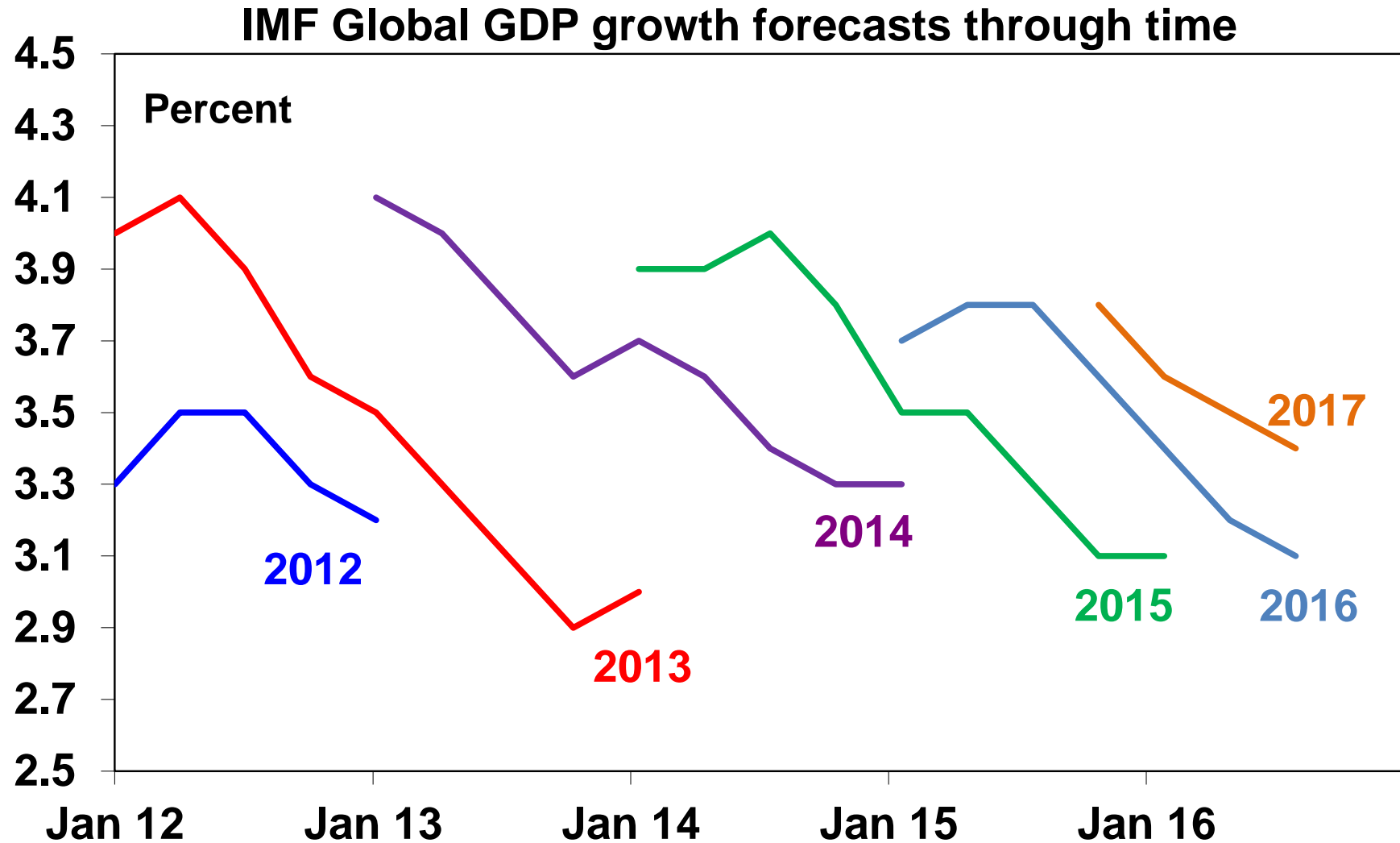
SHARES UP FROM LOWS

VOLATILITY LIKELY TO REMAIN HIGH THOUGH



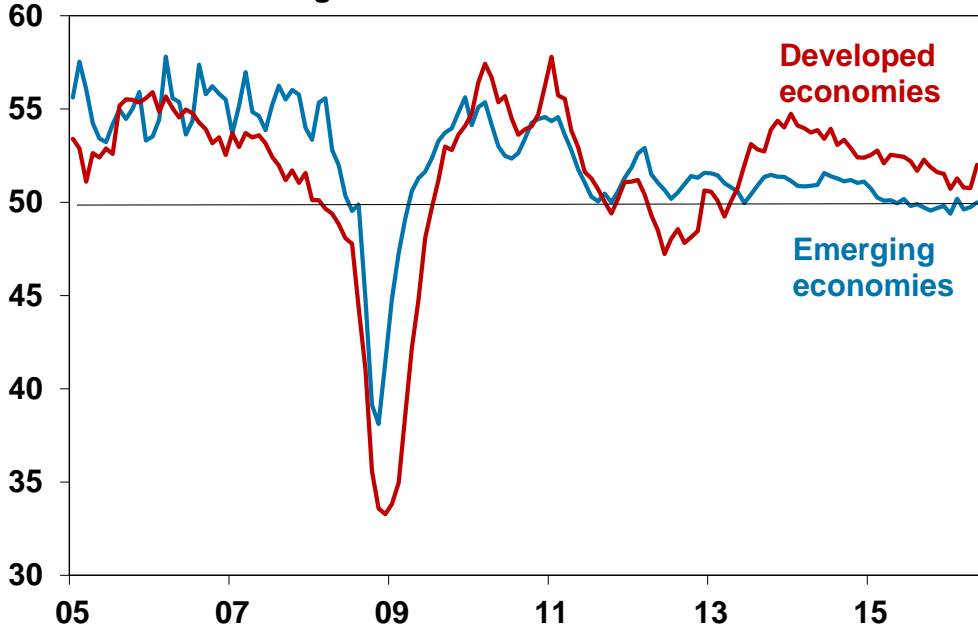
Source: Datastream, AMP Capital

MORE OF THE SAME FOR GLOBAL GROWTH

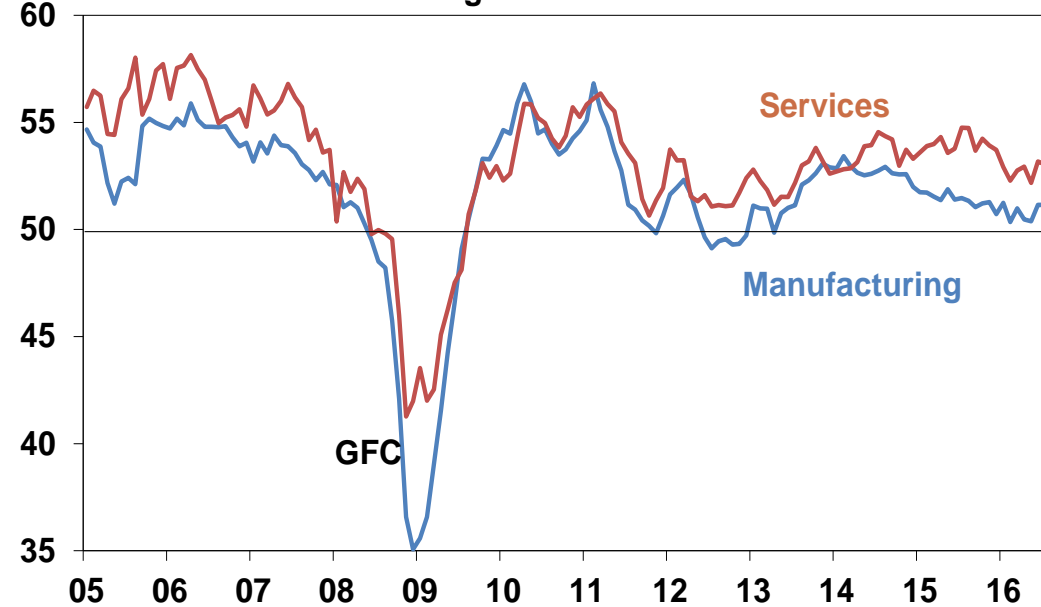


GLOBAL BUSINESS CONDITIONS SOFT, NOT RECESSIONARY

Manufacturing conditions PMIs - DMs better than EMs

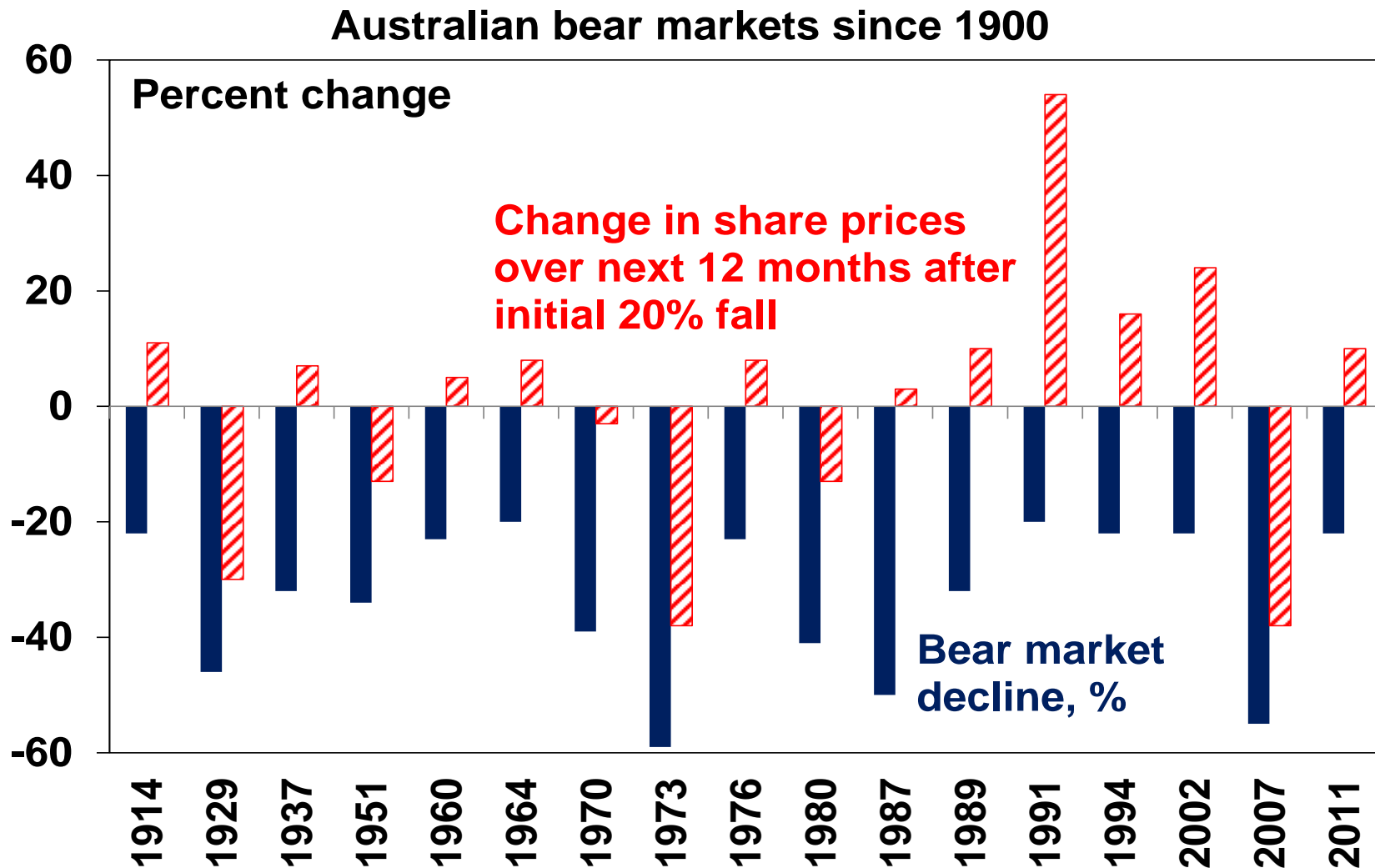


Global manufacturing and services conditions PMIs



BEAR MARKETS IN AUSTRALIAN SHARES SINCE 1900

WILL WE HAVE A RECESSION?



Source: Bloomberg, Global Financial Data, AMP Capital Investors

BEAR MARKETS IN AUSTRALIAN SHARES SINCE 1900

WILL WE HAVE A RECESSION?

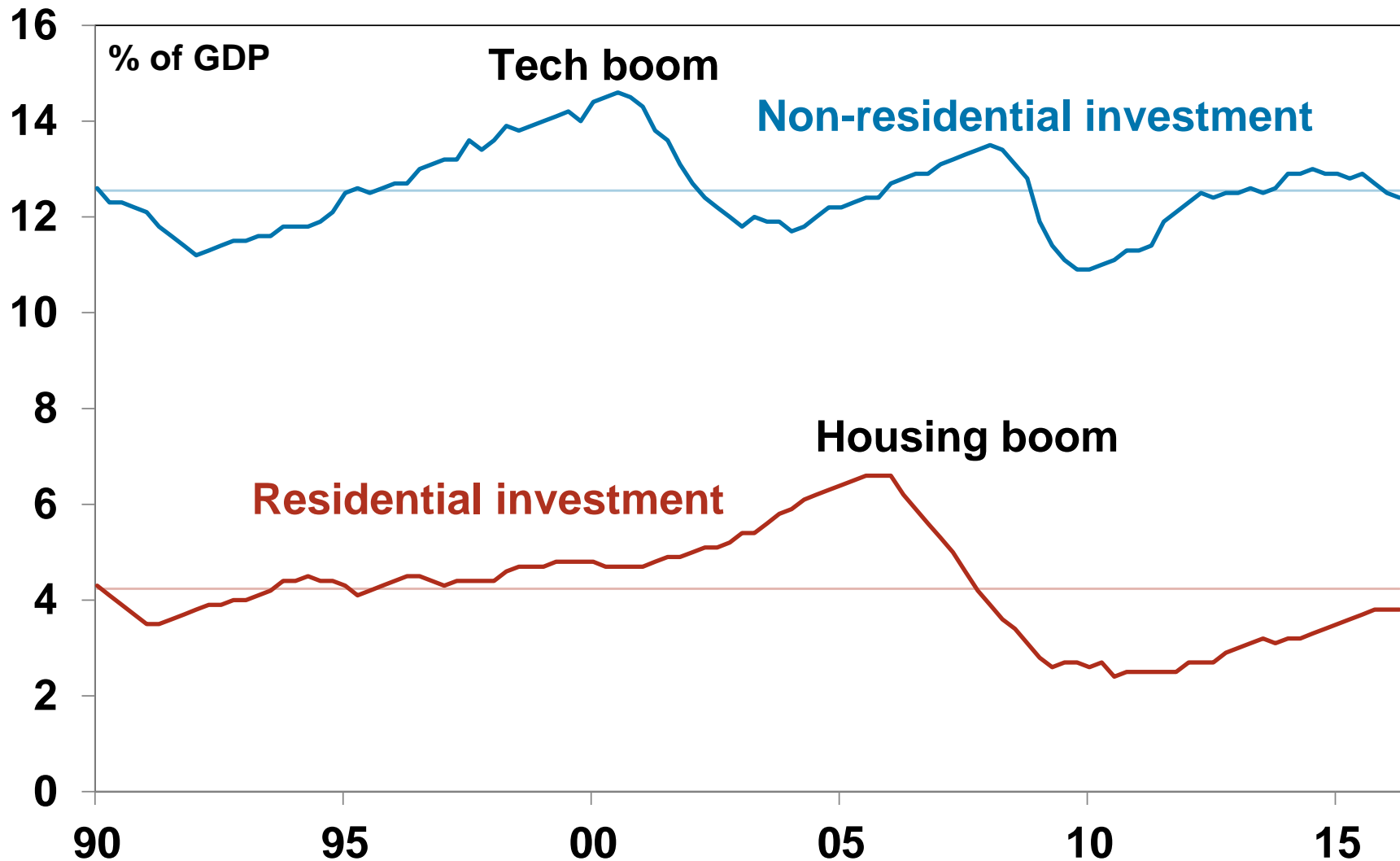
Bear markets in Aust shares	% fall	% chge 12 mths after -20%	Recession Aust, US or both	Fall in profits	Shiller PE plus inf rate
Jun 14-Dec16	-22	11	Yes	NA	NA
Jul 29-Aug 31	-46	-30	Yes	NA	NA
Mar 37-Apr 42	-32	7	Yes	NA	NA
May 51-Dec 52	-34	-13	No	NA	NA
Sep 60-Nov 60	-23	5	Yes	NA	NA
Feb 64-Jun 65	-20	8	No	No fall	NA
Jan 70-Nov 71	-39	-3	Yes	-28%	NA
Jan 73-Sep 74	-59	-38	Yes		23
Aug 76-Nov 76	-23	8	No	No fall	24
Nov 80-Jul 82	-41	-13	Yes	-28%	27
Sep 87-Nov 87	-50	3	No	-13%	43
Aug 89-Jan 91	-32	10	Yes	-51%	29
Aug 91-Nov 92	-20	54	No		21
Feb 94-Feb 95	-22	16	No	No fall	24
Mar 02-Mar 03	-22	24	Yes	-24%	25
Nov 07-Mar 09	-55	-38	Yes	-53%	38
Apr 11-Sep 11	-22	10	No	No fall	23
Avg from 1900	-33	1.2	NA	NA	NA
Avg from 1950	-33	2.4	NA	NA	28
Apr 15- ?	-20 ?	?	?	?	21

Source: Bloomberg, Global Financial Data, AMP Capital Investors

SEVERE BEAR MKTS UNUSUAL WITHOUT RECESSIONS

RECESSIONS ARE UNUSUAL WITHOUT PRIOR EXCESS

No US investment boom

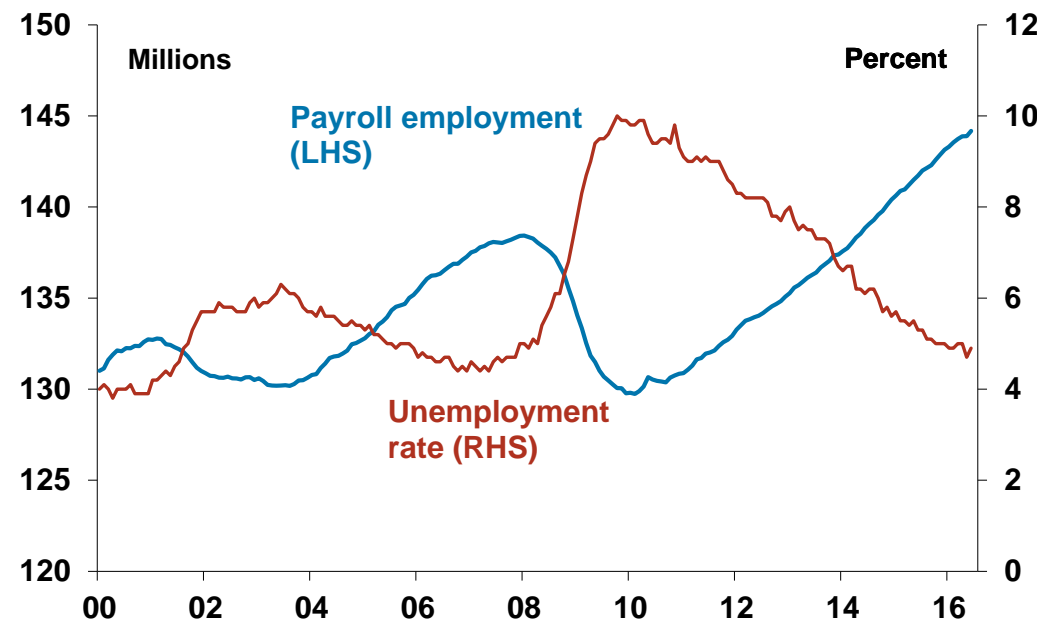


Source: Thomson Reuters, AMP Capital

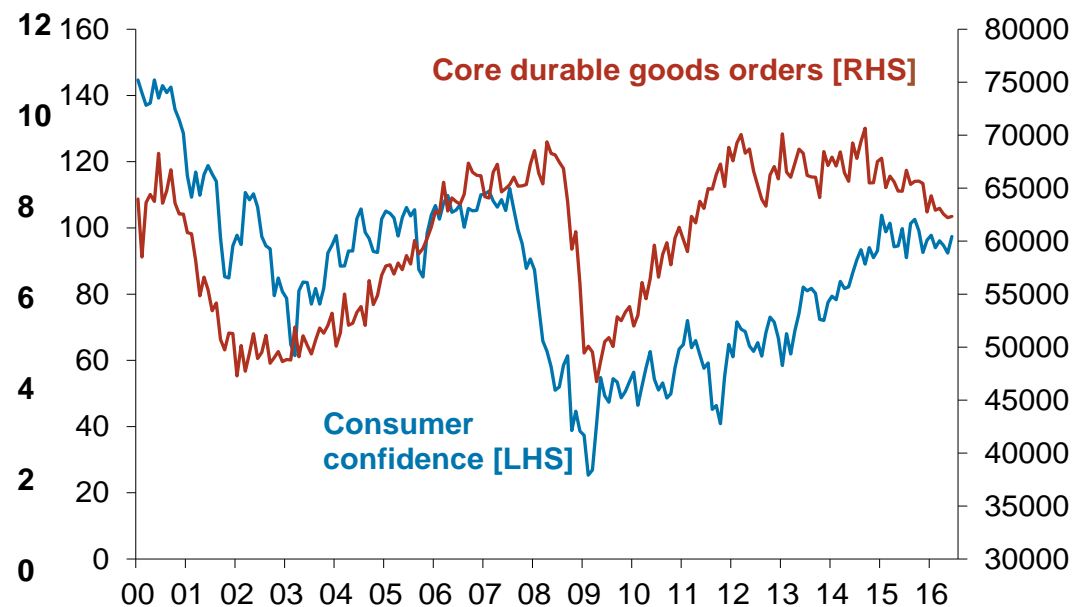
THE US ECONOMY OK, NOT BOOMING

SOLID JOBS MARKET AND CONSUMER BUT WEAK BUSINESS INVESTMENT & STILL LOW INFLATION CONSTRAIN THE FED

US employment above 2008, jobless well down, nearing full employment



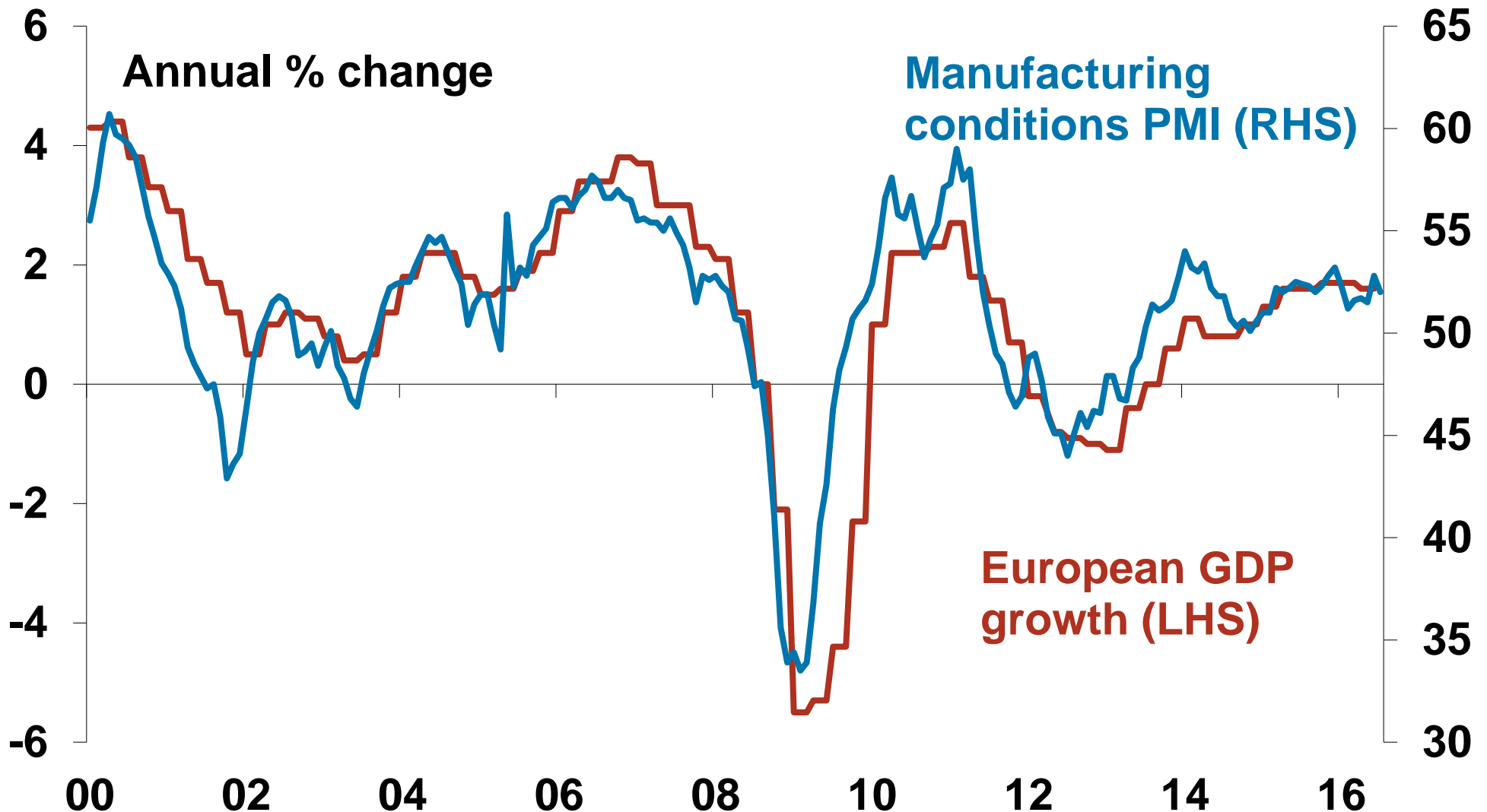
Consumer confidence okay but capex indicators have lost some momentum





THE EUROZONE LOOKING OKAY

WITH ONGOING ECB SUPPORT FOR BANKS

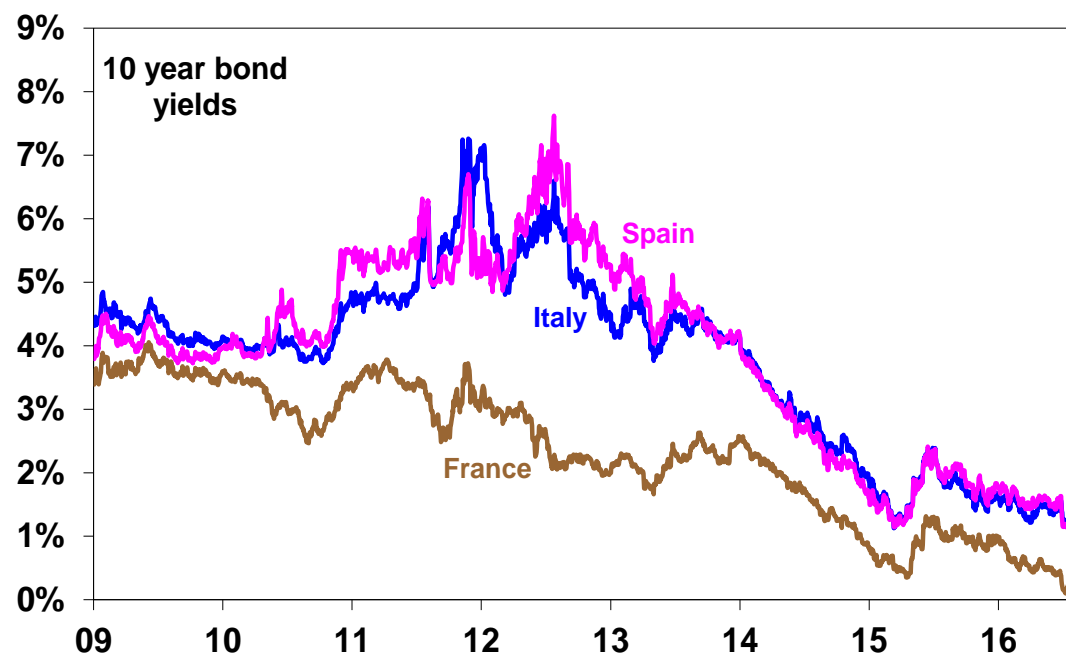


Source: Bloomberg, AMP Capital

Key issues and what to watch

- > Bad for the UK economy but its only 2.5% of global GDP and takes only 2.7% of Australian exports
- > Will the UK actually exit?
- > Key issue is contagion to rest Eurozone but the rest of Europe sees the EU as a source of strength and peace and less a driver of economic prosperity
- > The hurdle for Eurozone countries to leave is also greater than for the UK leaving the EU
- > Watch the Italian banks & Senate referendum, the Austrian presidential election re-run, Spanish and Italian bond yields and the \$US – so far so good

So far Italian and Spanish bond yields remain very low



CHINESE GROWTH APPEARS TO BE STABILISING

STIMULUS MEASURES ARE HELPING

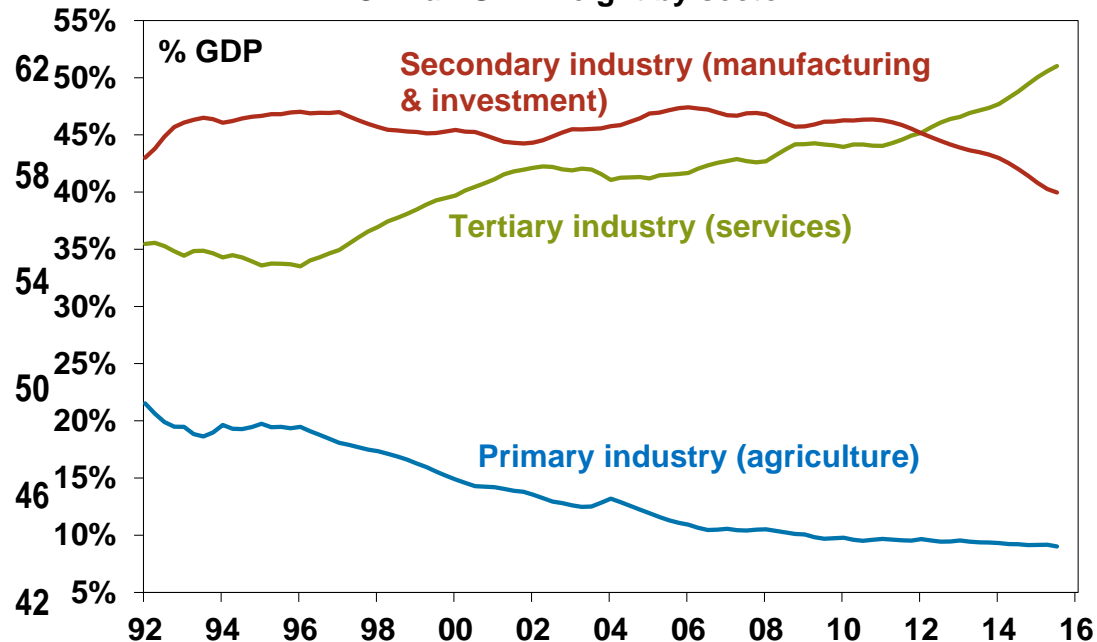
Chinese growth appears to be stabilising

China is in transition from manufacturing & investment to services & consumption

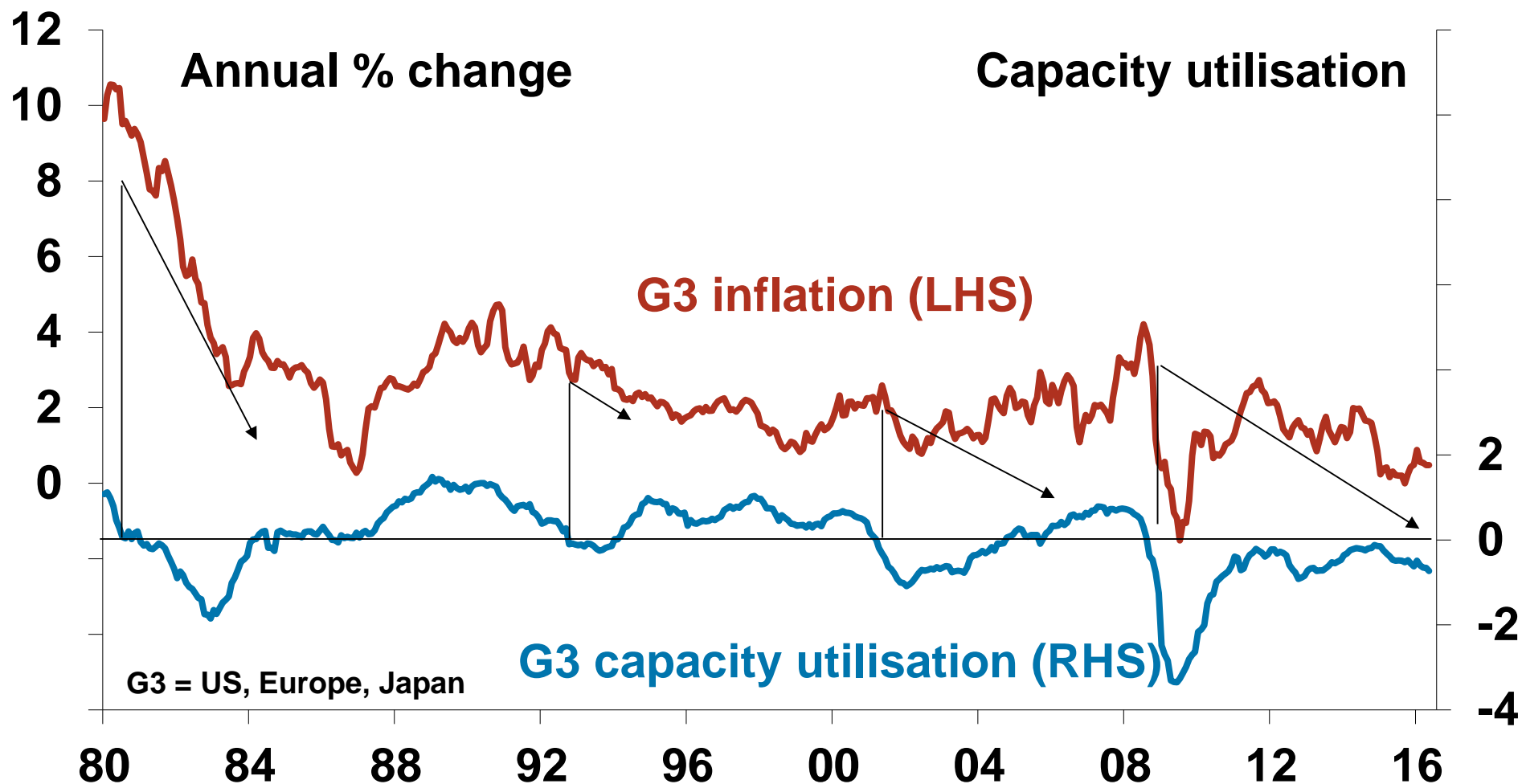
Chinese growth down from last decade



China - GDP weight by sector



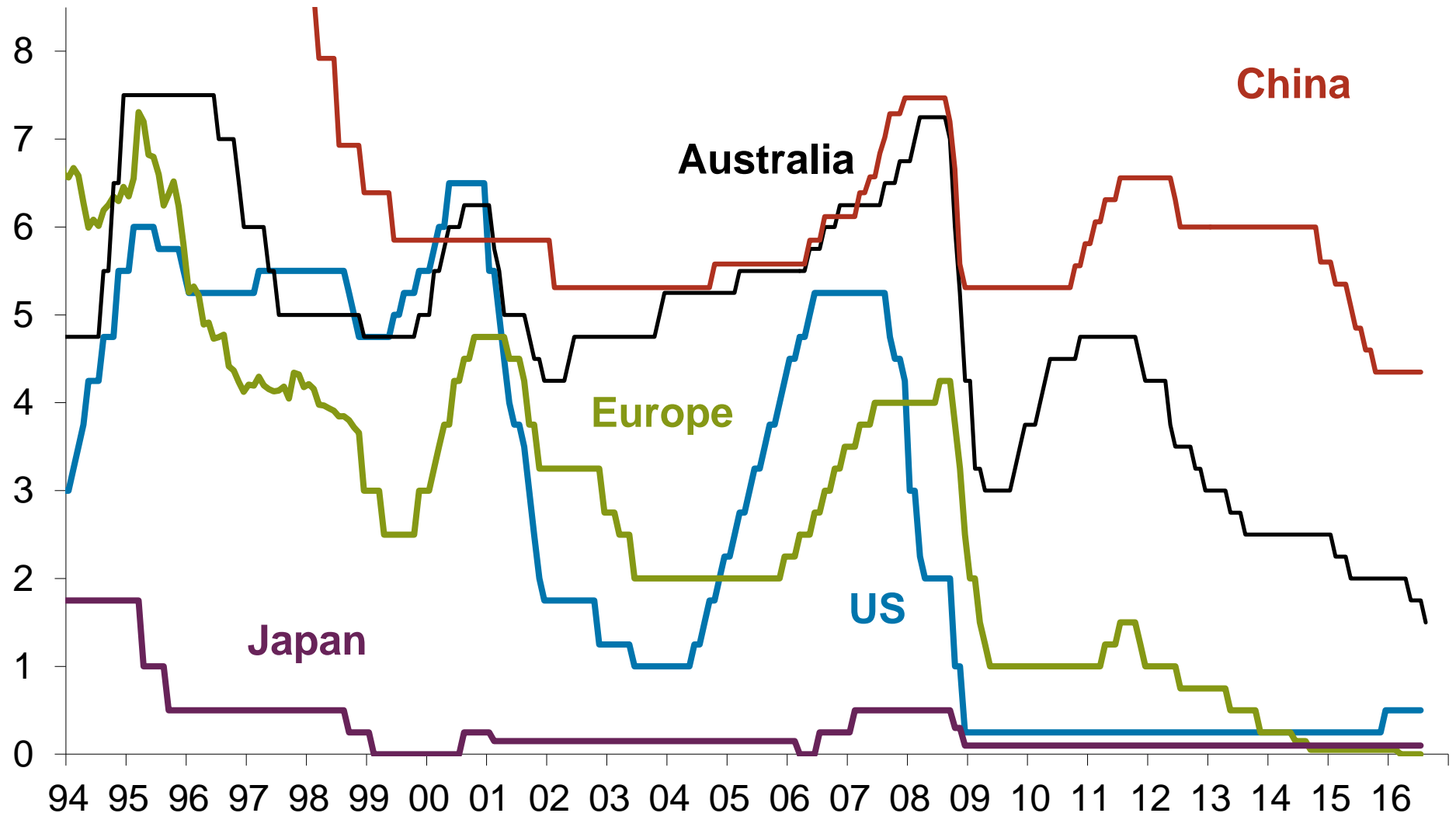
CONTINUED SLOW GROWTH MEANS INFLATION WILL REMAIN LOW, CENTRAL BANKS DOVISH



Source: Bloomberg, AMP Capital Investors

INTEREST RATES TO REMAIN LOW AS THE GLOBAL ECONOMY REMAINS FRAGILE

Interest Rates %

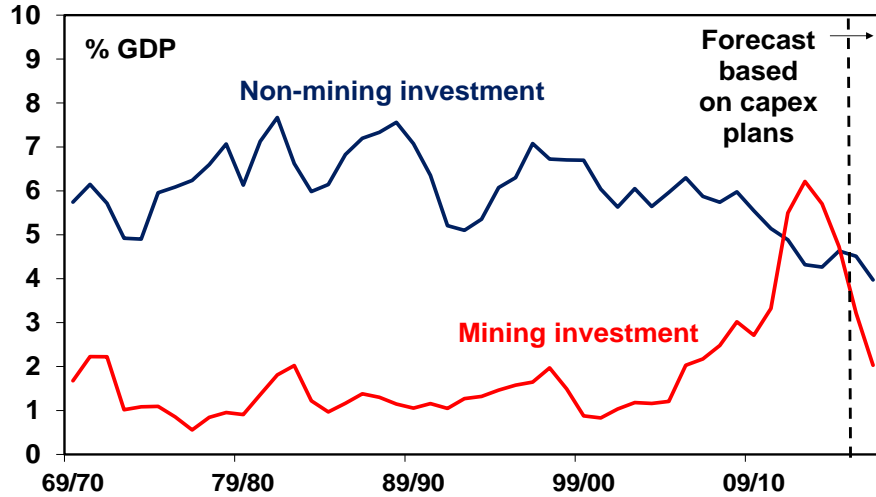


Source: Thomson Reuters, AMP Capital

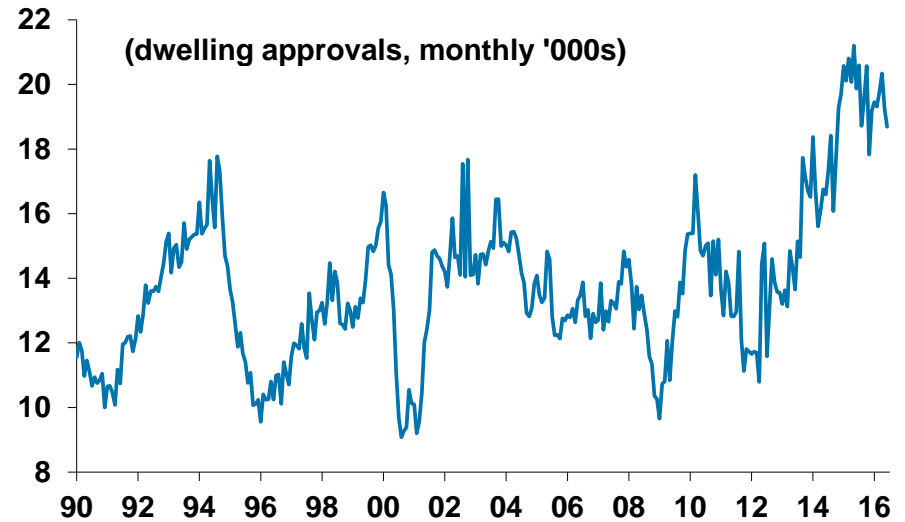
THE AUSTRALIAN ECONOMY

STRONGER THAN FEARED

Mining investment slowing, non-mining still weak



Strong dwelling construction...

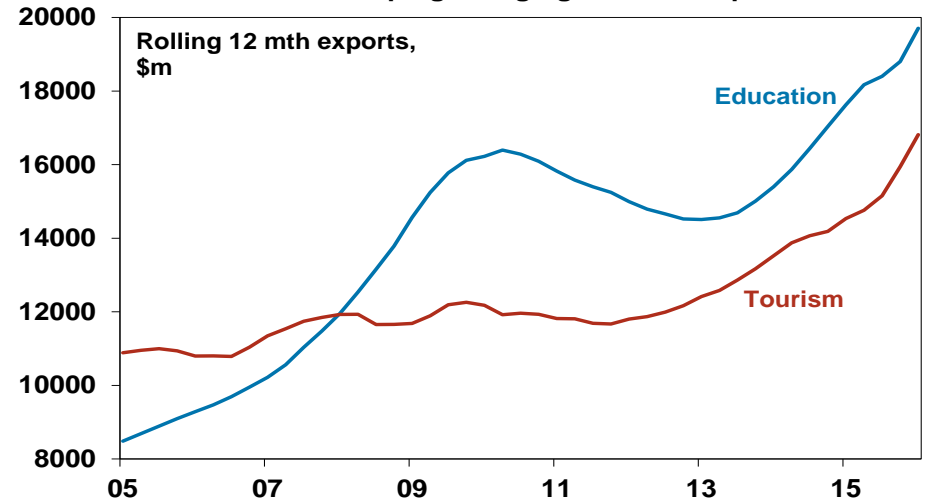


...has helped retail sales...



...and the lower \$A is helping Aust services exports

The lower \$A is helping - surging services exports

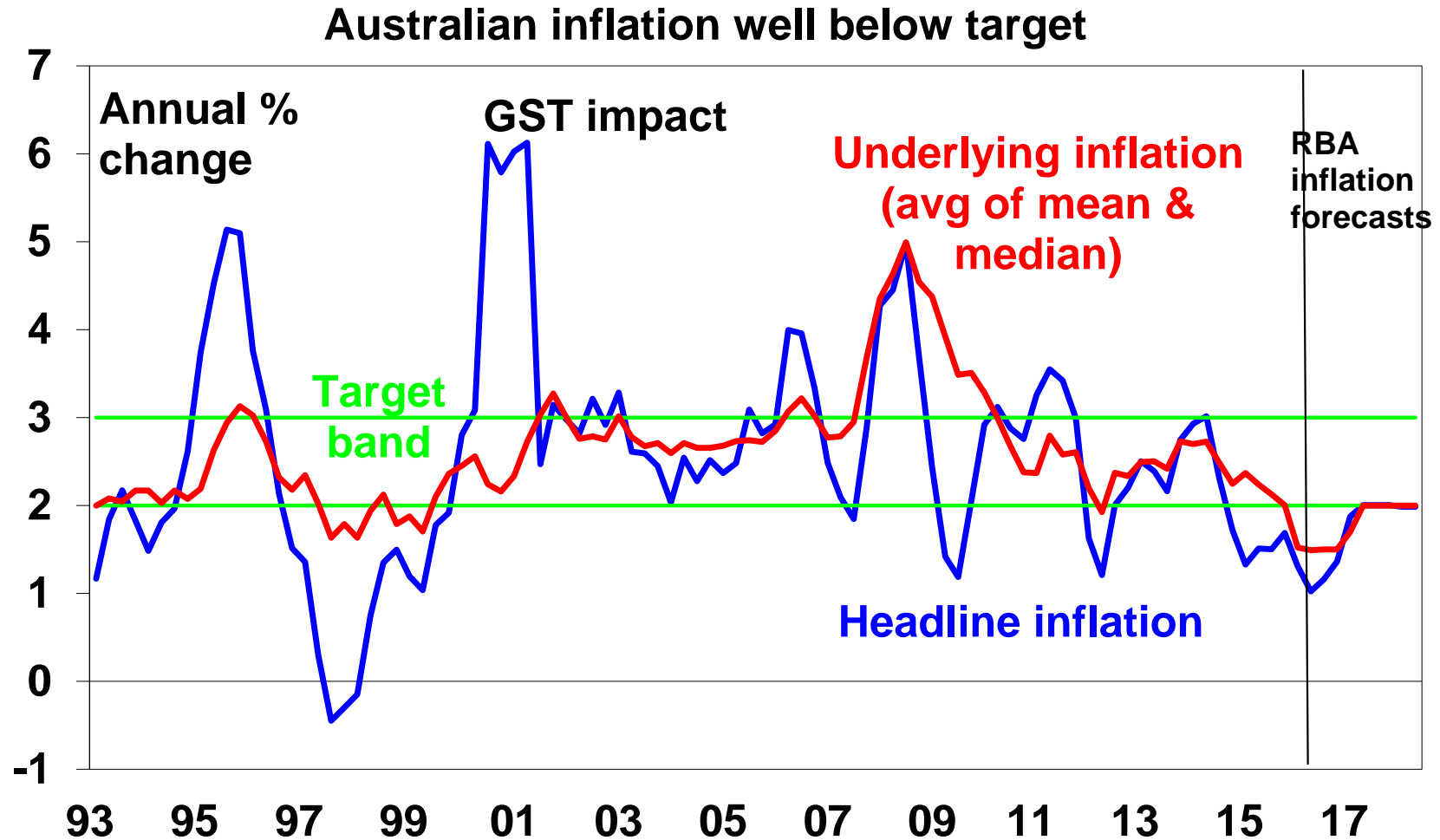


REVERSAL OF THE TWO SPEED ECONOMY = REBALANCING

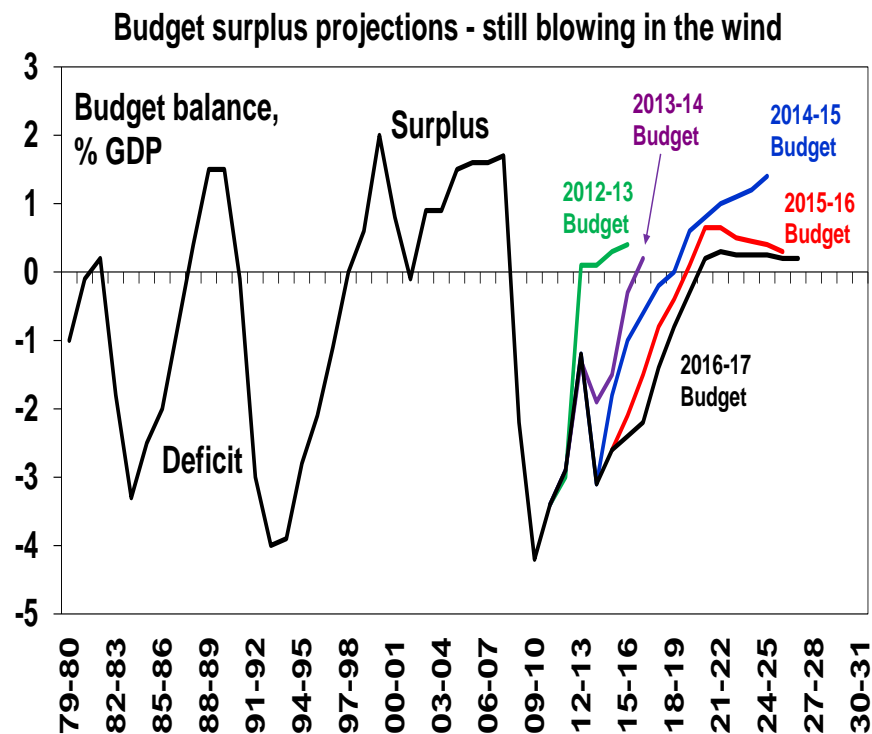
State of the states, annual % change to latest

	Retail Sales	Building Approvals, trend	Real State Final Demand	Home prices	Employment	Unemployment %	Rank
NSW	+3.3	-3.1	+3.9	+9.1	+3.2	5.2	2
Victoria	+4.0	+4.2	+3.2	+7.5	+3.4	5.7	1
Queensland	+1.5	-2.4	-1.8	+3.9	+0.3	6.5	6
WA	+0.5	-34.4	-4.2	-5.6	-0.6	5.6	8
SA	+3.1	+26.5	+0.5	+4.8	+1.1	6.9	4
Tasmania	+4.7	-28	+2.1	+6.2	-1.7	6.5	5
NT	-1.3	+0.7	-16.8	-7.6	-0.2	3.7	7
ACT	+3.8	-2.3	+2.9	+2.9	+1.5	3.6	3

WHILE GROWTH IS FINE, INFLATION IS TOO LOW DRIVING THE RBA TO MORE RATE CUTS



MESSY ELECTION RESULT RISKS FURTHER BUDGET BLOWOUT, LOSS OF AAA RATING, LACK OF REFORM

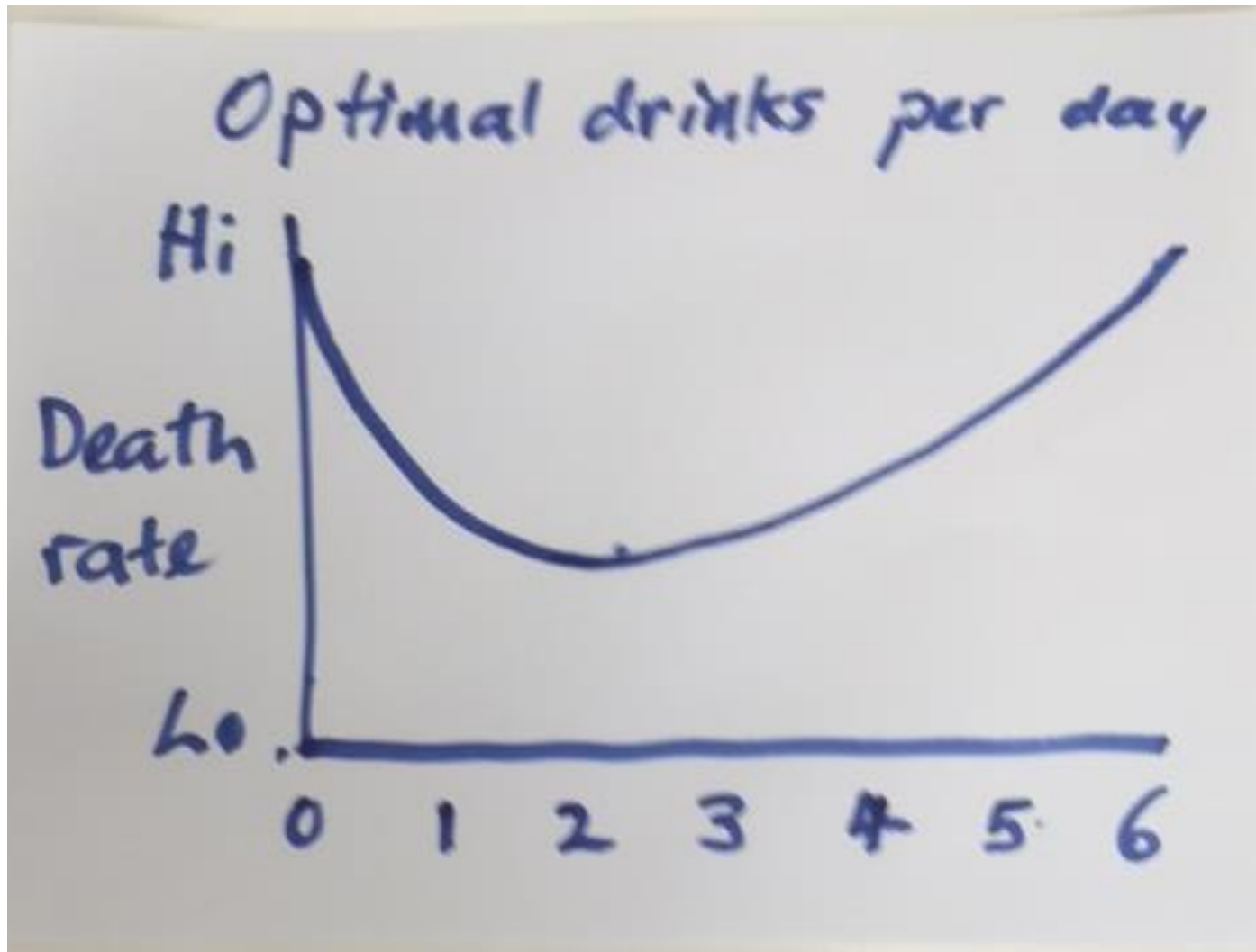


Australia's sovereign rating history

Date of report	Moody's	S&Ps	Fitch
Nov 2011	AAA	AAA	AAA
Feb 2003	AAA	AAA	AA+
Oct 2002	AAA	AA+	AA
May 1999	AA2	AA+	AA
Jan 1996	AA2	AA	AA
Oct 1989	AA2	AA	-
Aug 1989	AA2	AA+	-
Dec 1986	AA1	AA+	-
Sept 1986	AA1	AA1	-
June 1975	AAA	AAA	-
Oct 1974	AAA	-	-
Jan 1962	A	-	-

Source: Australian Treasury, AMP Capital

OPTIMAL DRINKS PER DAY – DR JOHN



OPTIMAL DRINKS PER DAY – BETTER MOVE TO CHILE !

Drinking responsibly?

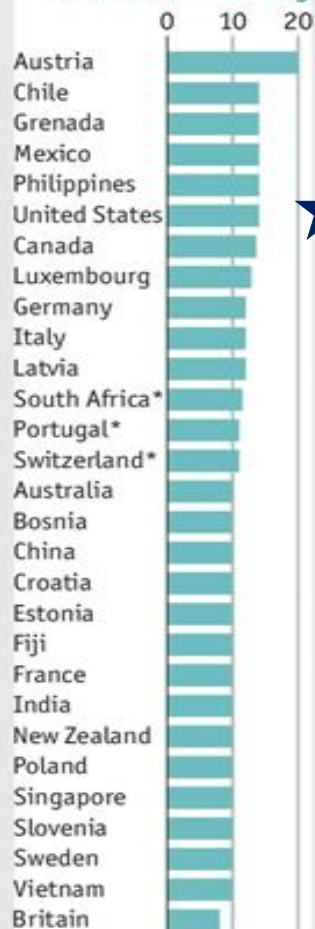
Governmental standard drink definitions and daily guidelines

2016, grams of pure ethanol

National definition
of standard drink

Pure ethanol, grams

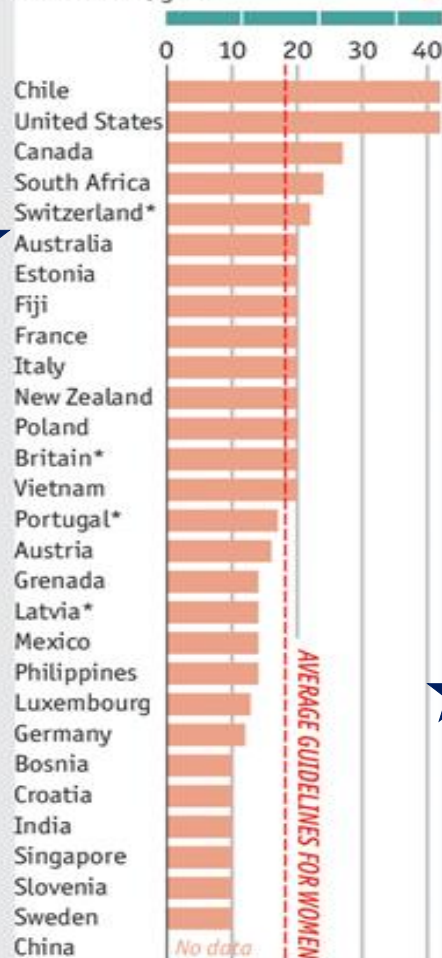
AVERAGE 11.3g



Daily guidelines for women

Low-risk

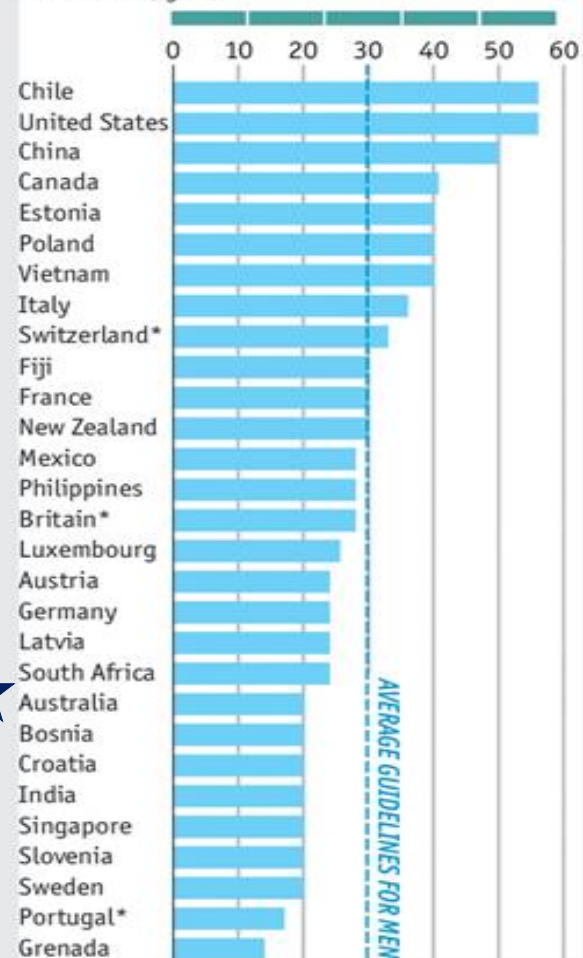
Pure ethanol, grams



Daily guidelines for men

Low-risk

Pure ethanol, grams



Source: Society for the Study of Addiction

* Average within a range

GLOBAL SHARE MARKETS



WHY HAVE SHARE MARKETS BEEN SO ROUGH & REASONS NOT TO BE TOO CONCERNED

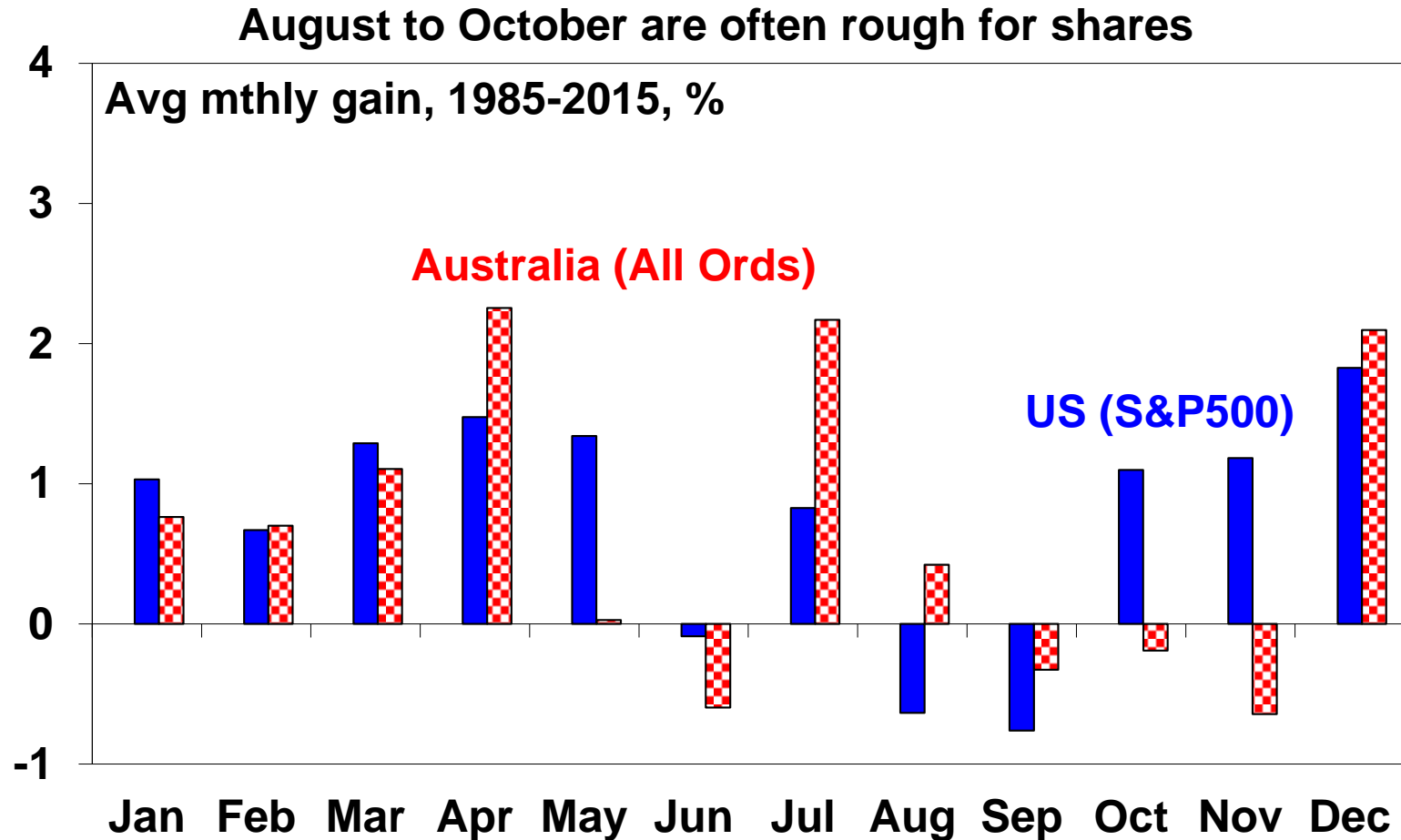
Why have shares had a rough ride?

- > Worries about the emerging world
- > Worries about China
- > Worries about the impact of low oil prices on producers
- > Worries about Fed tightening and the strong \$US
- > Worries about Brexit
- > Worries about worries

Why a severe global bear market is unlikely?

- > Share valuations are okay
- > A recession is unlikely
- > Normal lags suggest the boost to energy consumers from lower oil prices will provide a growth boost this year
- > Monetary conditions are set to remain very easy
- > There is a lot of pessimism around

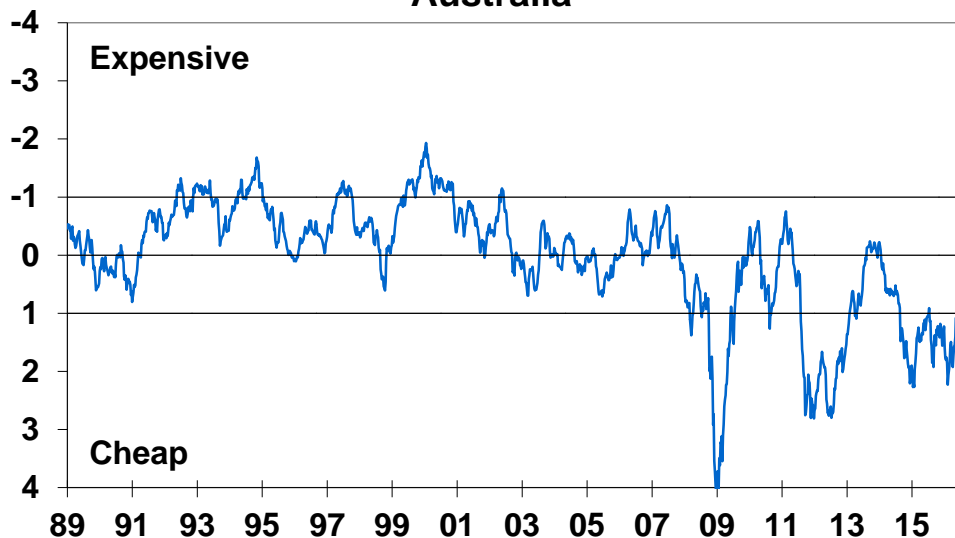
SHARES VULNERABLE TO SHORT TERM SEASONAL WEAKNESS



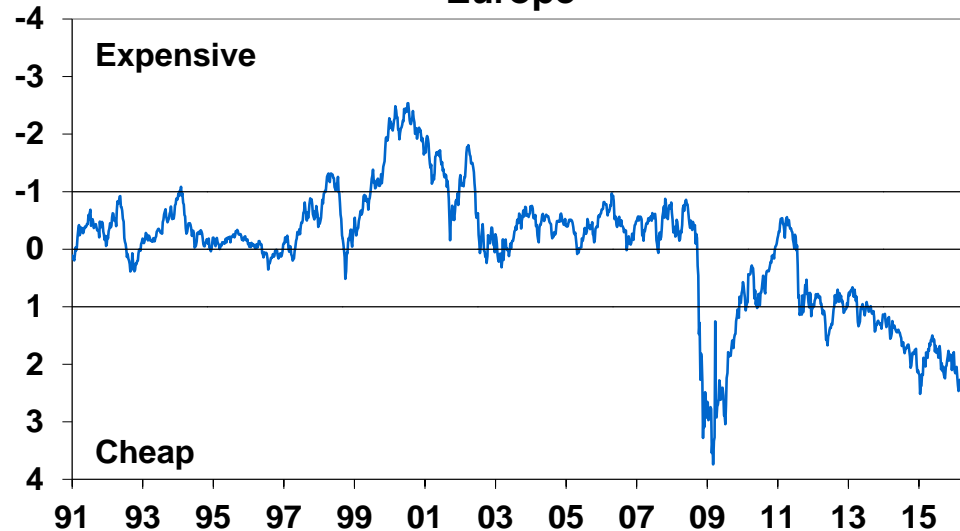
BUT SHOULD BE FINE ON A 6-12 MONTH VIEW

SHARE MARKET VALUATION INDICATORS

Australia



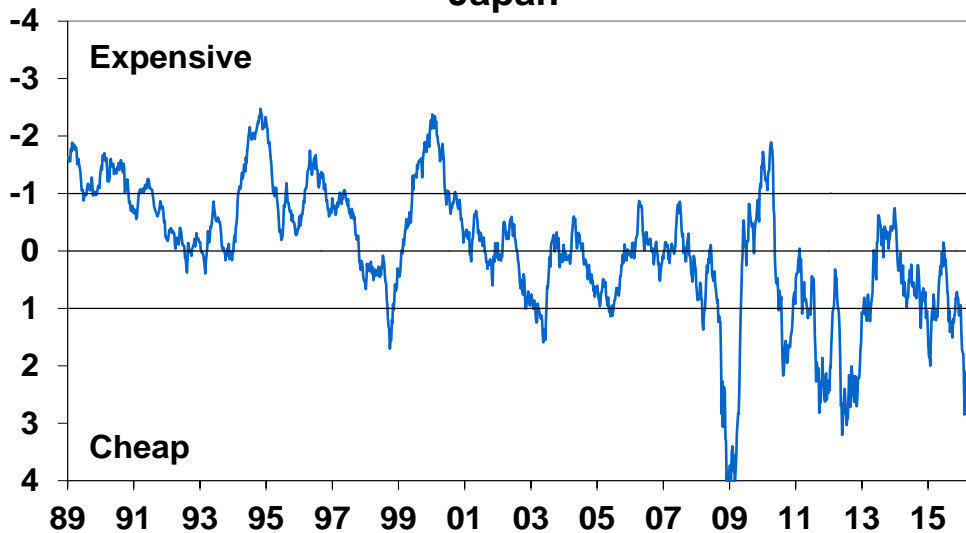
Europe



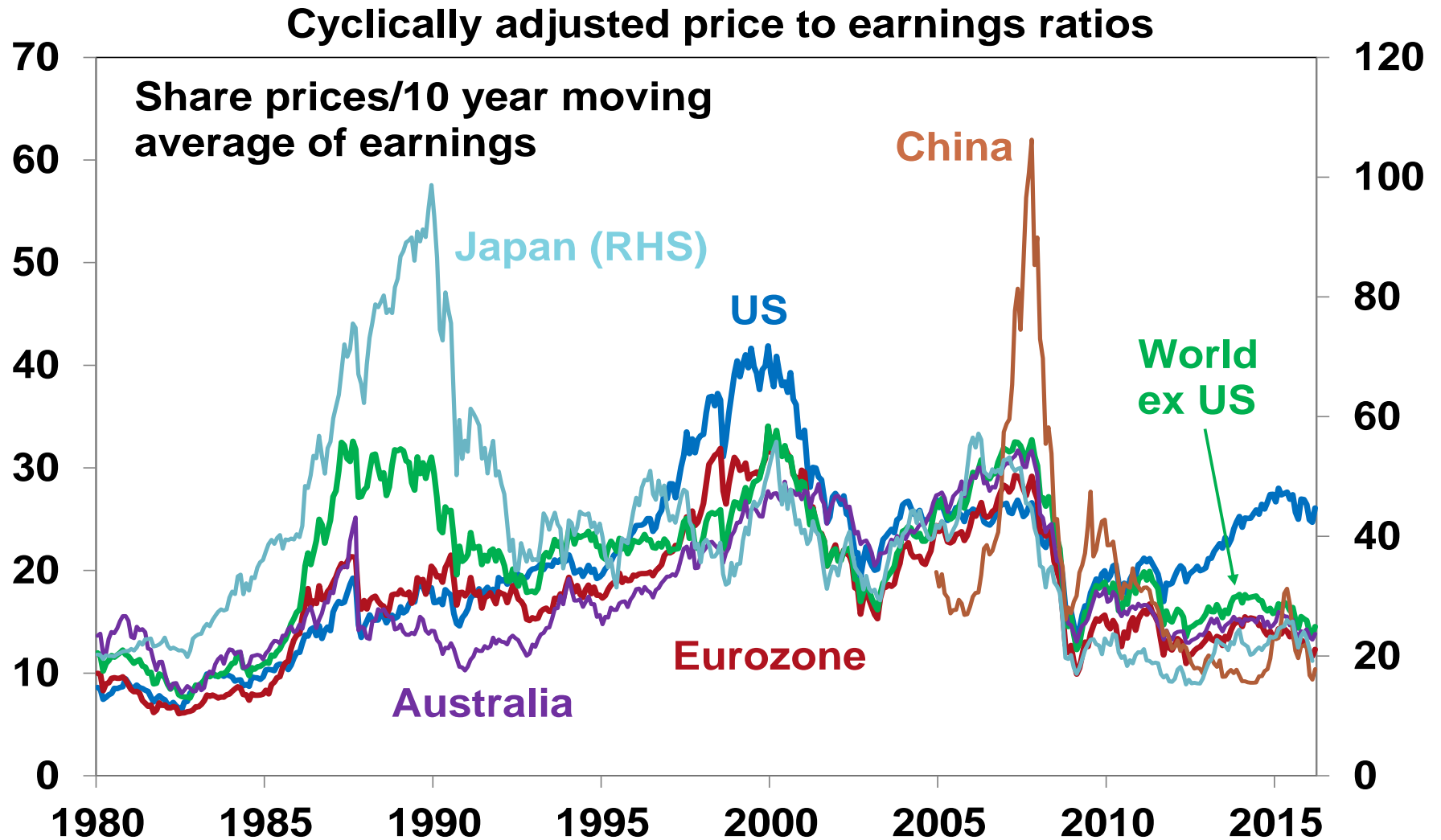
USA



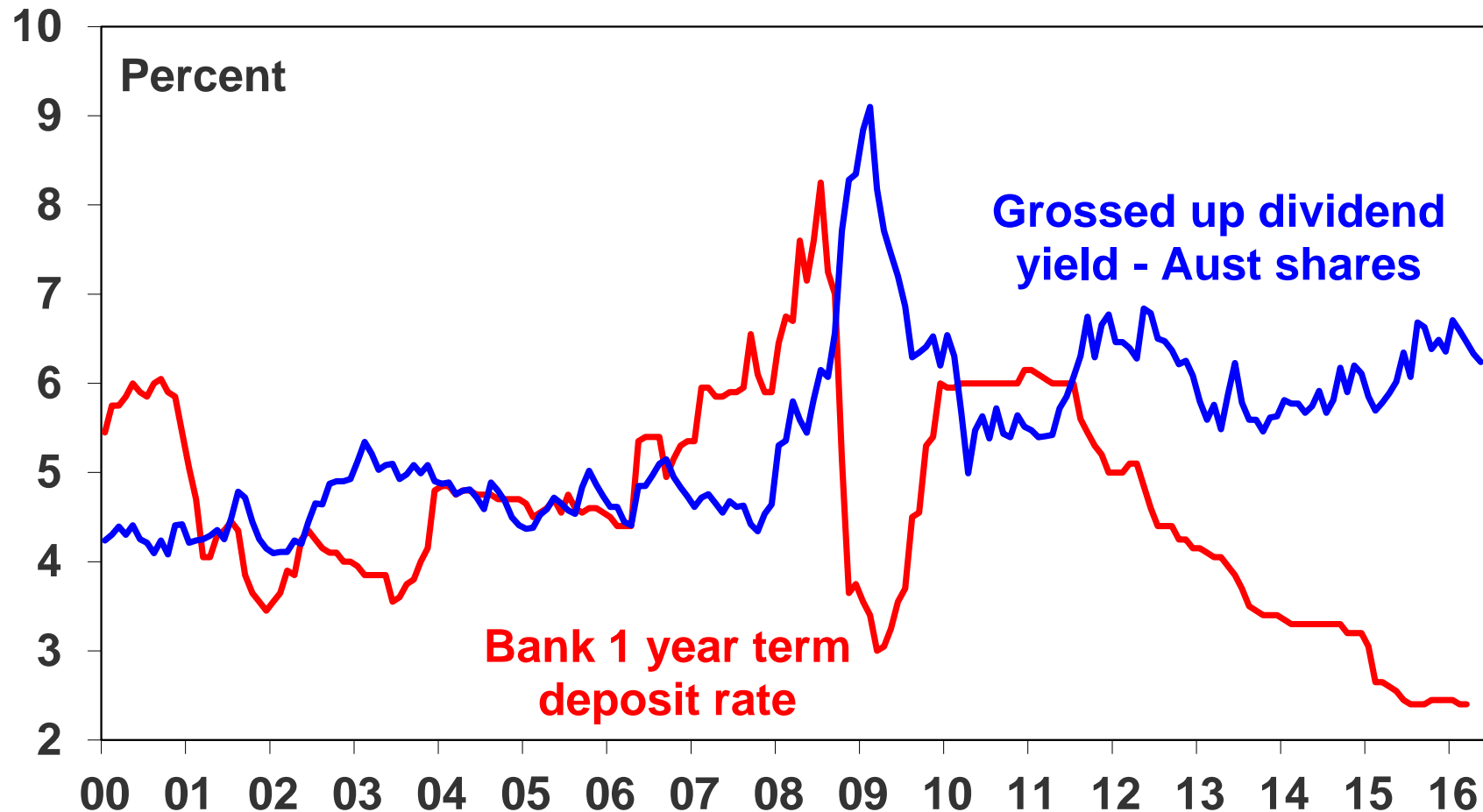
Japan



LOTS OF VALUE OUTSIDE THE US



AUSTRALIAN SHARES ARE OFFERING A HIGH CASH FLOW VERSUS BANK DEPOSITS

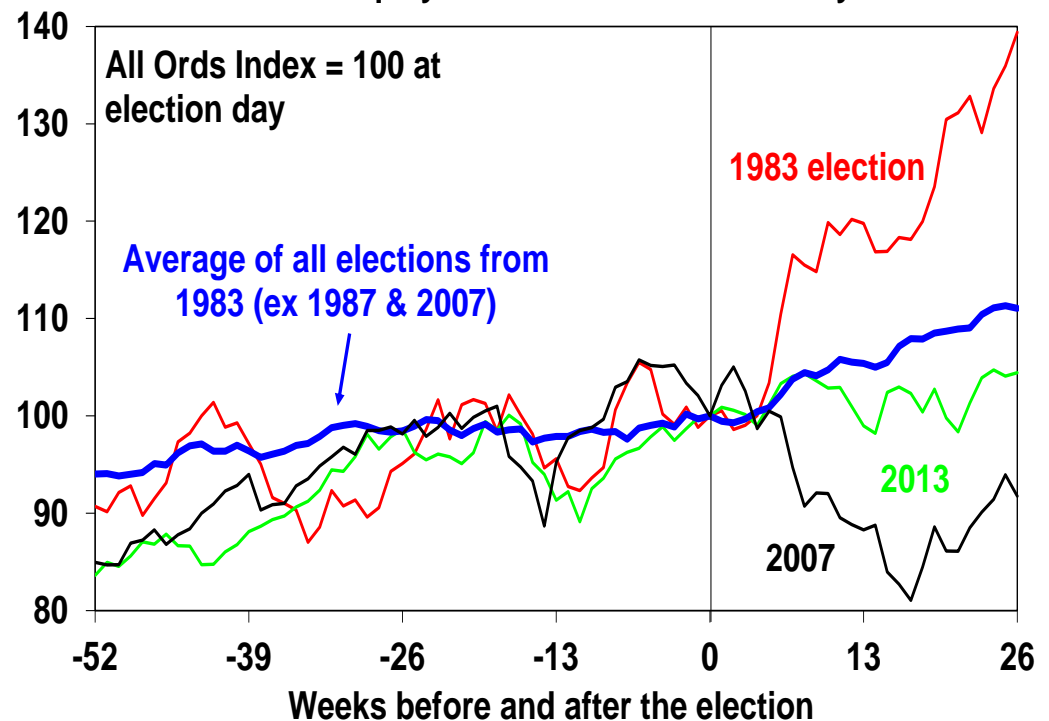


THE AUSTRALIAN ECONOMY, SHARE MARKET AND ELECTIONS

The economy and elections

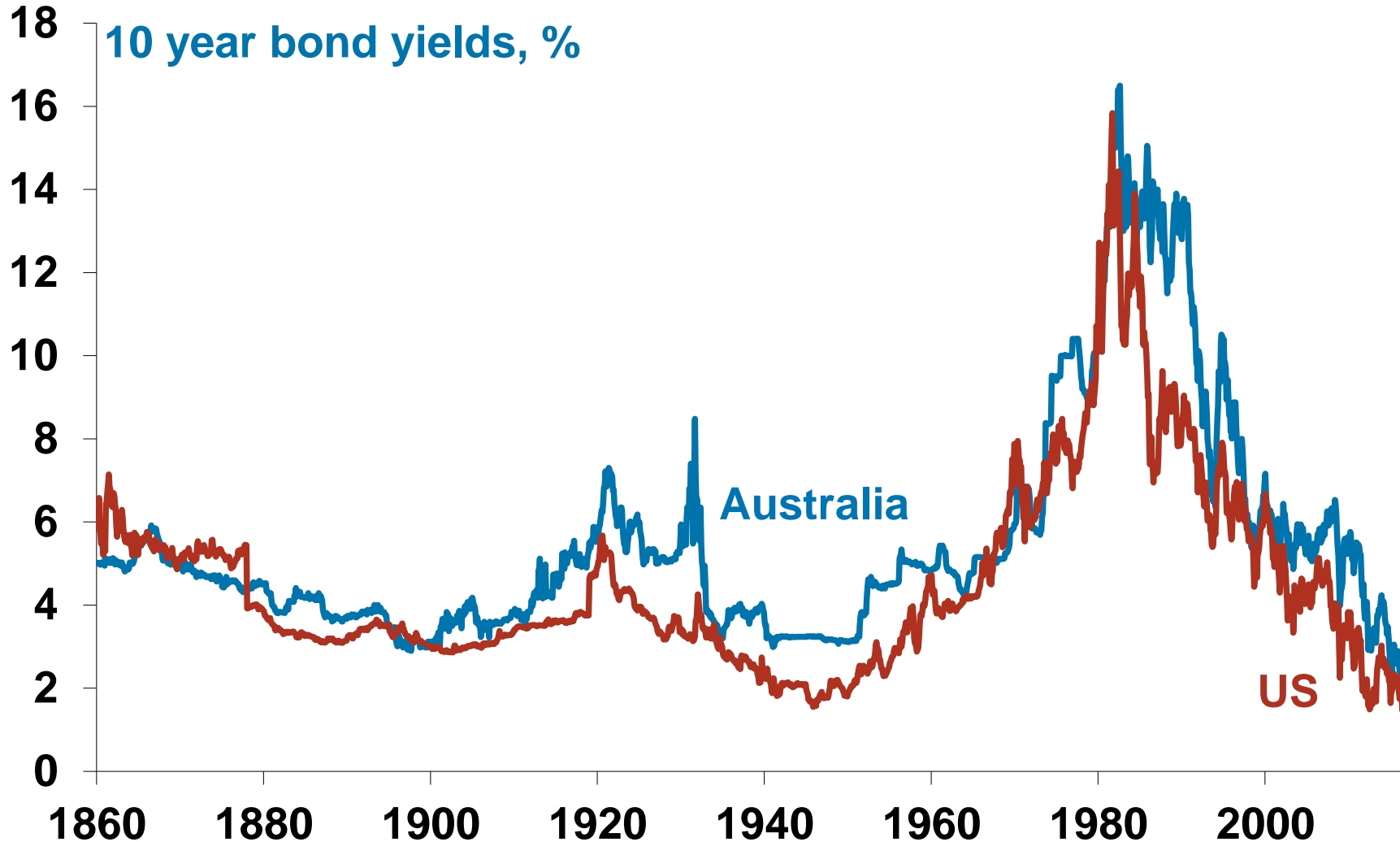
Avg GDP growth, %pa	All years	Election years
Since 1960	3.5	3.2
Since 1980	3.2	3.7

Australian equity market around election days



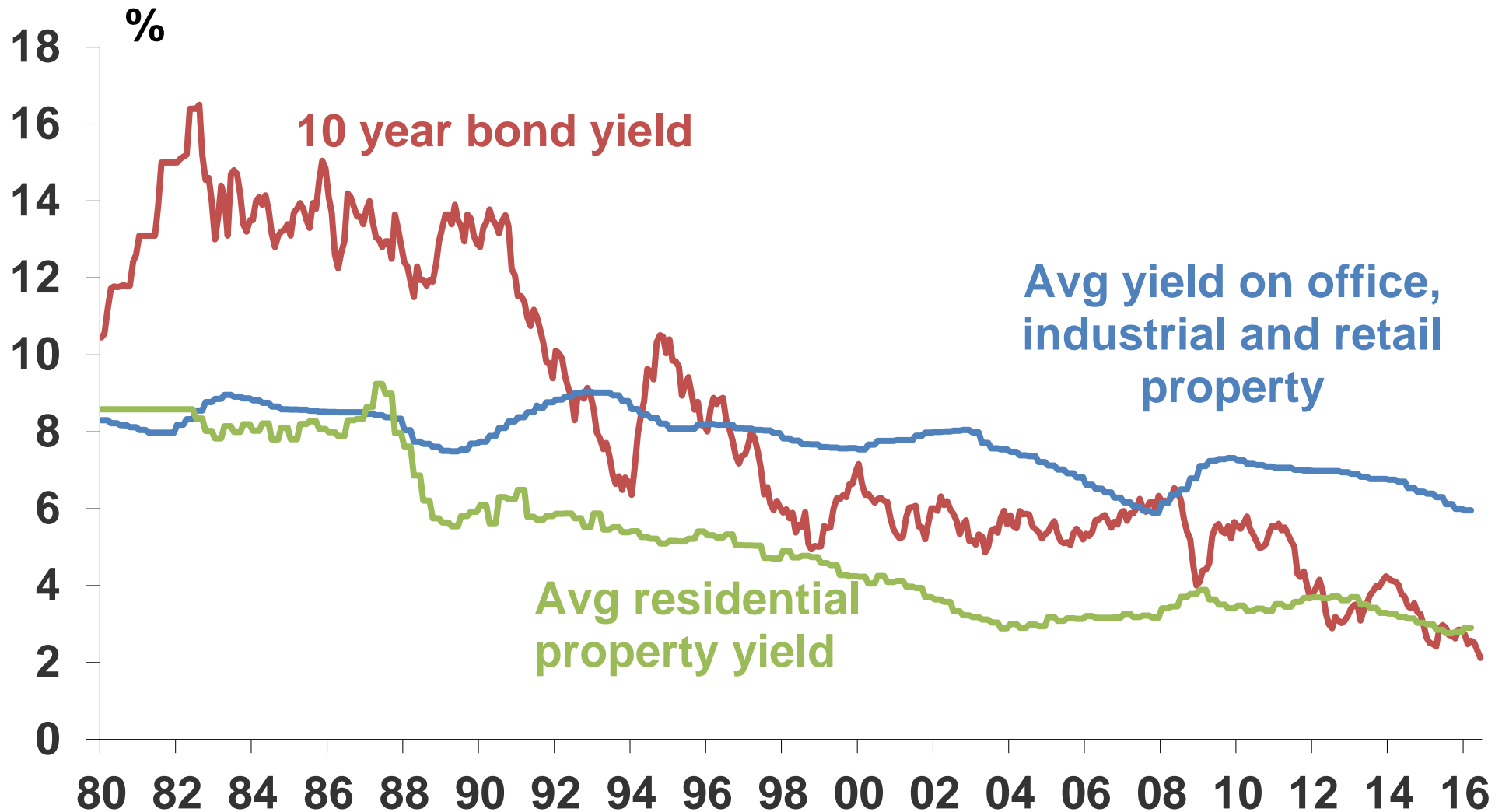
LOW YIELDS POINT TO LOW MEDIUM TERM RETURNS FROM BONDS

BUT THEY ARE STILL A GREAT DIVERSIFIER



WITH INTEREST RATES & BOND YIELDS REMAINING VERY LOW THE “SEARCH FOR YIELD” IS LIKELY TO GO FURTHER

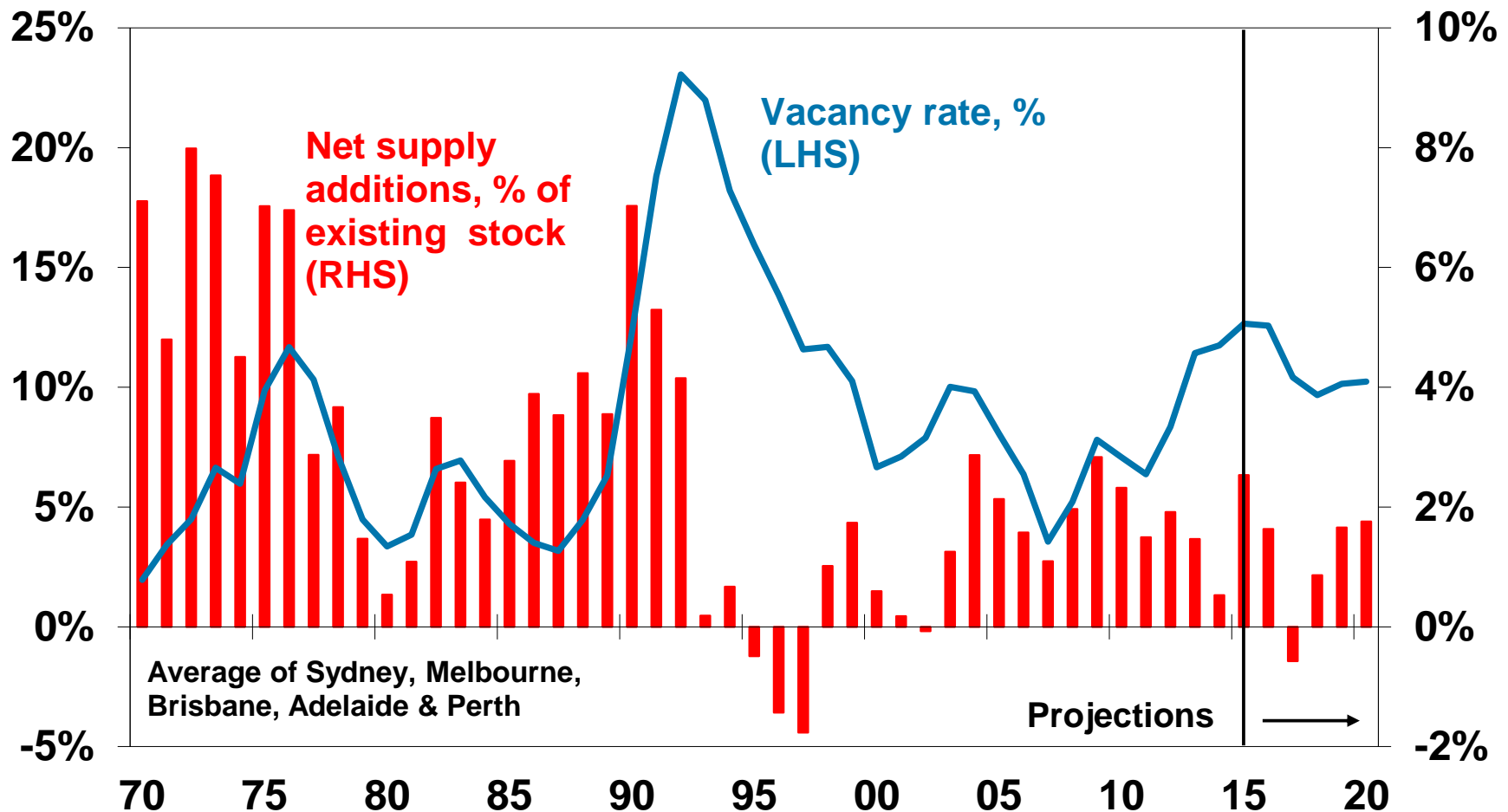
Australian property yields versus the bond yield



Source: RBA, AMP Capital

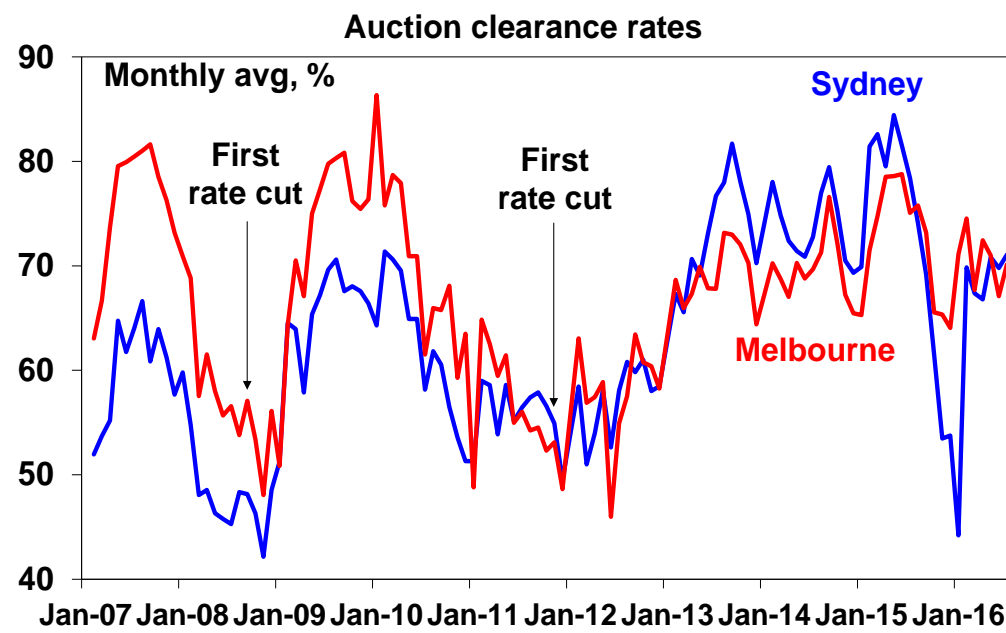
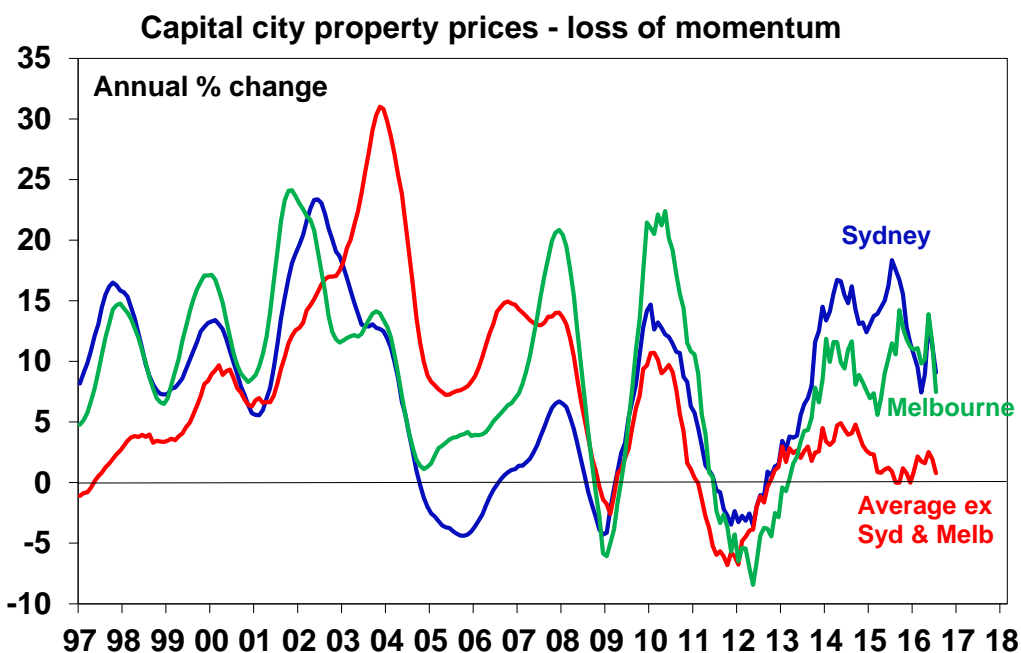
OFFICE VACANCY RATES PEAKING

Average Australian CBD office vacancy rates



THE DIVERGENT AUSTRALIAN HOUSING MARKET

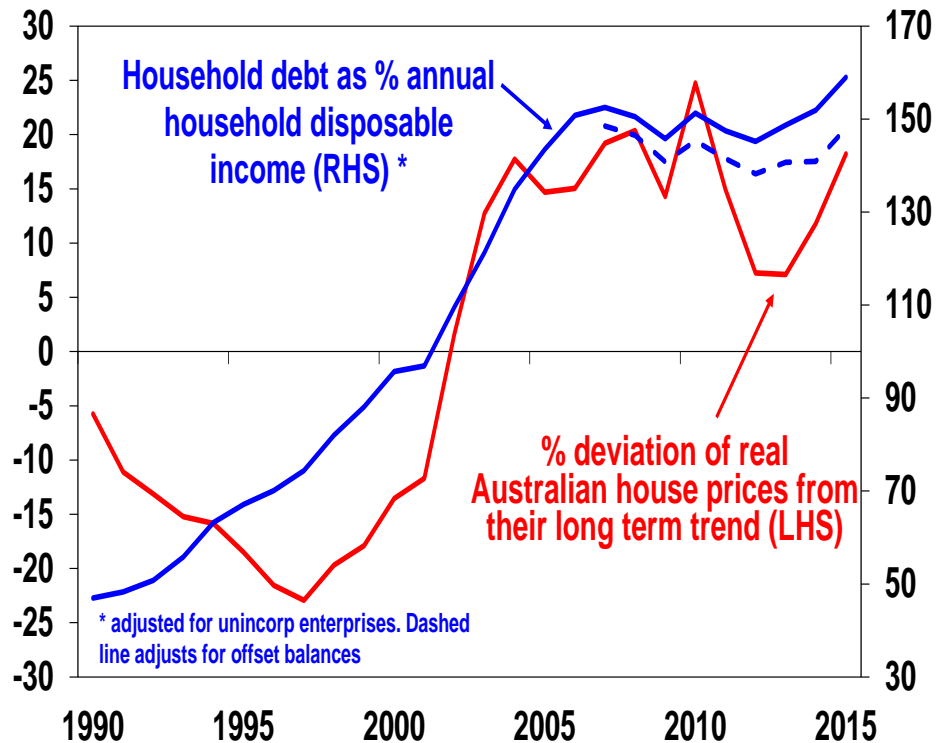
SYDNEY AND MELBOURNE SLOWING (A BIT)



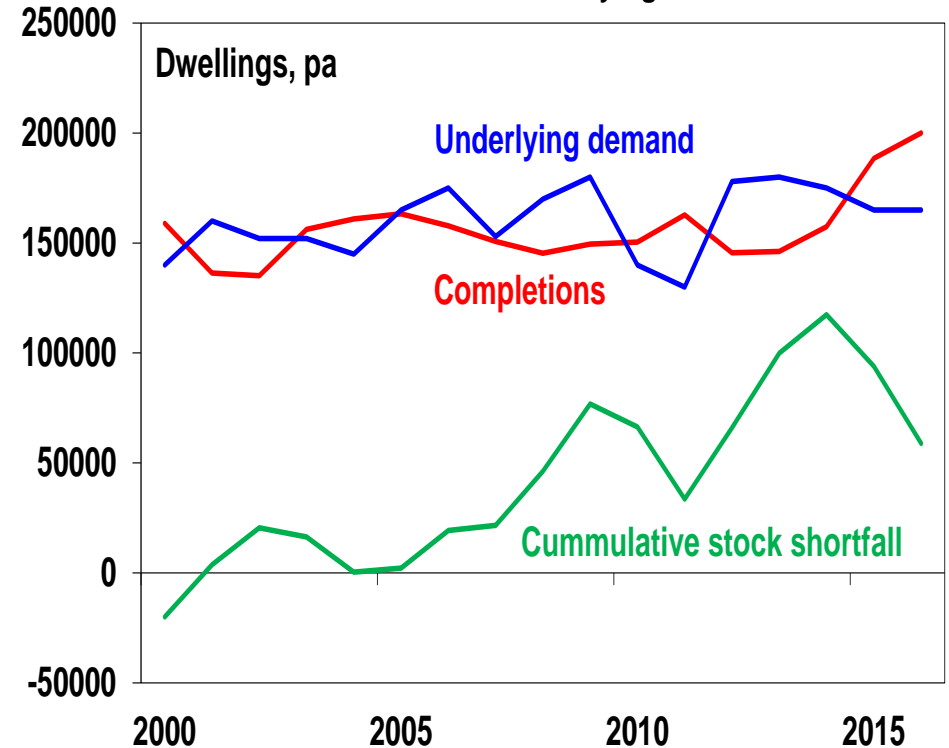
Source: Core Logic-RP Data, Domain APM, AMP Capital

CRASH CALLS FOR AUSTRALIAN PROPERTY? EXPENSIVE HOUSING AND HIGH DEBT BUT YEARS OF UNDERSUPPLY

Australian home prices & debt have been high for a while



Home construction and underlying demand

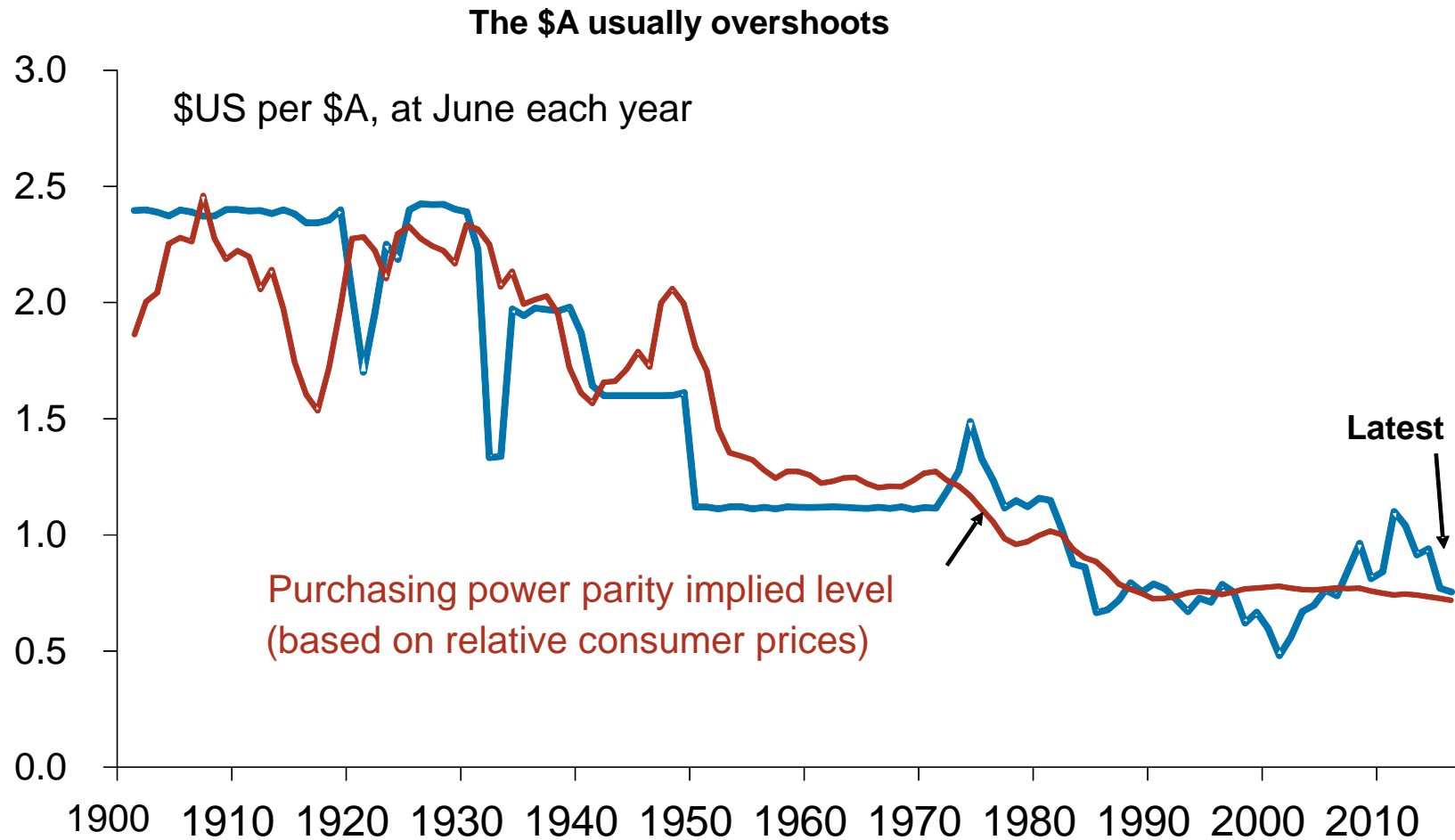


PROJECTED MEDIUM TERM RETURNS, %PA, PRE FEES AND TAXES

	Current Yield #	+ Hedge Points	+Growth	=Return
US Equities	2.1	1.7	4.3	8.1
Asia ex Japan Equities	2.7	0.1	6.8	9.6
Emerging Equities	2.7	-1.9	6.3	7.1
World Equities, local currencies	2.6	1.8	3.9	8.4
Australian Equities	4.9/6.4	0.0	3.3	8.2/9.7
Unlisted Commercial Property	6.0	0.0	2.0	8.0
Australian REITS	4.3	0.0	2.3	6.5
Global REITS	3.8	1.4	1.8	7.1
Unlisted Infrastructure	5.0	0.8	3.1	8.9
Global Listed Infrastructure	3.6	1.7	2.8	8.1
Australian Gov't Bonds	1.8	0.0	0.0	1.8
Australian Corporate Debt	3.2	0.0	0.0	3.2
Australian Cash	2.7	0.0	0.0	2.7
Diversified Growth Mix				7.0

Current dividend yield for shares, distribution/net rental yields for property and 5 year bond yield for bonds. * With franking credits added in
Source: AMP Capital

THE \$A IS LIKELY TO FALL TO AROUND \$US0.60



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