Economic and market update

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Bob reviews events in Australian and overseas markets during June.

How did markets perform in June?

Global shares drifted lower in early June with concerns over Britain's pending referendum on whether to remain part of the European Union (EU). The surprisingly decisive vote for Britain to exit the EU, known as 'Brexit', caused initial alarm in markets by raising the possibility of Scotland's independence as well as concerns over European political stability.

However some share markets recovered their balance in the final week of June with soothing comments from Britain's central bank and the recognition that UK's exit may take some time. Surprisingly UK's FTSE 100 Index recorded a strong 4.4% gain for June given the benefit of a sharply weaker currency and expectations for an imminent interest rate cut. US shares ended flat for the month while the Euro Stoxx 50 Price Index fell by 6.5% with concerns that European economic integration has been set back. Japan's Nikkei 225 Index was particularly weak (a 9.6% fall) given the sharp surge in the Japanese yen which penalises their exporters. Australian shares fell with the S&P/ASX200 Accumulation Index down 2.5% for the month.

Global government bond yields edged lower in the opening weeks of June with the soft US employment report. The US Federal Reserve's (Fed) decision to keep interest rates steady at June's policy meeting was expected. However the Fed's lowering of interest rate forecasts over coming years added some momentum to the fall in bond yields. Britain's surprise decision to exit the EU only accelerated this fall further. Despite losing their AAA credit rating, British government bonds saw a remarkable decline in yields after the Brexit vote. Australian government bonds rallied strongly given concerns over European political risk.

The Australian dollar (AUD) managed mild gains against the US dollar given the more cautious interest rate forecasts of the Fed as well as gains in commodity prices. Both gold (+8.8%) and iron ore (+11%) recorded strong price gains in June. However the AUD was weaker against the Japanese yen given the sudden flight to safety following the Brexit outcome.

What were the key factors driving markets?

Britain's decision to leave the EU generated considerable turbulence in markets as well as European politics. European economic integration could come under severe pressure if countries decide to have a vote on EU membership.

US economic data was mixed in June. A disappointing May payroll report with subdued jobs growth caused some anxiety over economic growth prospects. However there were more encouraging gains in consumer confidence, retail spending, house prices and sales activity.

China's economic activity data stabilised in June. China's industrial production was steady at 6% annual growth while retail sales were robust at 10% growth. China's residential property markets remain exuberant with strong 6% annual price gains for new house prices.

Australia recorded solid economic activity. Australia's March quarter GDP data shows the nation's economy expanded by 3.1% over the past year. Strong growth in consumer spending, housing construction and exports have managed to offset the downturn in mining investment. Australia's labour market achieved solid growth in new jobs for May with the unemployment rate remaining steady at 5.7%. The National Australia Bank's business survey shows positive business conditions, suggesting that the Reserve Bank of Australia's decision to cut interest rates in May has been supportive ahead of July's Federal election.

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