kina funds management

investment committee report

29 January 2016

KFM Investment Committee Report

The KFM Investment Committee met this week, and the following summarises our view of the markets over the next six months.

MARKET OUTLOOK (6 MONTHS)

	Current Measure	Previous View	Current View
PNG Macro Environment			
Real GDP Growth (2014) *Source: PNG Budget*	13.3%	→	→
Inflation (trailing 12m) As at September 2015 (NSO)	5.7%	→	↗
PGK/USD	0.3315	↘	↘
PGK/AUD	0.4767	→	→
PNG Cash & Fixed Income			
28 days CBills	1.23%	→	→
182 days TBills	4.67%	→	→
5 year GIS	11.33%	↗	↗
10 year GIS	11.16%	↗	↗
PNG Equities			
KSI	3,380.7	→	→
KSI Home	9,346.3	→	→
Global Macro Environment			
Implied World Growth 2016 *Source: World Bank*	2.9%	→	→
International Cash & Fixed Income			
US 10Y Bond	2.0%	↗	→
International Equities			
MSCI ACWI	US$169.7	→	→
Commodities			
Oil (WTI) (barrel)	US$29.8	→	↘
Gold (troy ounce)	US$1,108.5	→	→
LNG (mmBtu)	US$7.4	→	↘

KFM INVESTMENT COMMITTEE MEMBERS

Victor Shubin General Manager, KFM	**Syd Yates** Chief Executive Officer	**Adam Fenech** General Manager, KWM, KNL, KISS	**Ivan Gutai** Credit Admin Manager
Raicie Guillermo Team Leader, Investment Analysis & Research	**Sermomo Tungapik** Team Leader, Portfolio Administration & Compliance	**Noelyne Togs** Senior Projects Analyst	

PNG Macro Environment
KFM holds the view that GDP growth will be restrained to below c.4.0% in 2016 as commodities continue to follow a downward taper, with the exception of gold. KFM believe the effects of the global commodity glut on the extractive industries to provide impetus for another revised budget as prices fall below budget forecasts. The agriculture, mining and utilities sectors will remain adversely affected by the El Nino. The third quarter CPI update for rolling 12 month inflation was 5.8% while BPNG announced to maintain the Kina Facility Rate at 6.25%. KFM maintains its view that inflation will be around 6.0% mainly driven by the downward momentum of the Kina against the USD

PNG Kina
The PNG Kina has now reverted to pre-trading-band levels and KFM notes that the official FX reserves have now dropped well below US$1.9bn compared to US$2.6bn twelve months ago, we maintain the view that the PGK will continue its downward momentum in relation to the US$ and will fluctuate in relation to other foreign currencies over the next six months. The impact of BPNG's FX trading band continues to affect PNG financial institutions and exporters as the build-up in FX orders persists

PNG Cash & Fixed Income
KFM maintains that short term rates will remain flat at current levels. Subscription activity for government securities has indicated continued weak appetite in the market. On the other hand, the anticipated sovereign bond issuance still remains uncertain, as such long term rates are expected to see an increase over the next six months

PNG Equities & Property
KFM expects equities to remain largely flat with downward pressure on earnings driven by slowdown in the economy, low commodity prices, FX control by BPNG and the likely impact on business. KFM maintains its property market outlook for commercial and residential sectors supported by data analysis on rental rates in POM. Residential properties to remain under increasing pressure amidst increasing stock and competition while commercial sector rates remain stable given the implied positive demand

Global Macro Environment
Sluggish global economic growth persists amidst slowdown in China, collapse in commodity prices, geopolitical tensions in Europe and Middle East. However, on the same note, growth in economies that are net importers of oil could get a boost whilst those that are commodity export-dependent will face economic down turn. The gradual increase in rates by the Fed will affect international borrowing costs for developing nations. KFM maintains the view that global growth will remain subdued in light of continued diverging economic growth trends around the world. **Australian Q4 CPI number has come in above consensus expectations [headline: 0.4% QoQ/1.7% YoY vs expected 0.3/1.5%]. KFM believes that the RBA will stay on hold at 2.0% and have a neutral view of the AUD vs USD [c.0.7]**

International Cash & Fixed Income
KFM maintains its view that most bond yields will remain at current low levels supported by low inflation, weak economic fundamentals, expansionary monetary policies and strong US dollar. Meanwhile US Bond prices are expected to decline off the back of the increase in rates following indications of a strengthening labour market

International Equities
Chinese markets have opened the year on a strong negative note (down c.15% MSCI YTD) with most of international equities following suit; regulations and interventions are likely to follow and it remains to be see to what effect. EMs face 'new reality' of lower growth. Thus far and with the notable exception of the December jobs report, US economic data have been disappointing since policymakers raised the Fed's short-term interest rate in the middle of December. Whilst we expect volatility in the interim, fuelled by investors' risk-averseness amidst geo-political tensions, and an anticipated tightening of the Fed's Monetary Policy, KFM remain cautiously optimistic on equities over the longer term as an asset class supported by expansionary policies in regions of subdued growth, and increasing confidence in the US

Commodities
In light of slowing global growth and continued mismatch between oil supply and demand, KFM expects oil (as well as gold) prices to remain volatile. The number of rigs drilling oil and gas wells worldwide, which has fallen 46 per cent since the fourth quarter of 2014. Also affected by slowing global growth is the price of copper, a key commodity with its wide range of industrial uses. LNG prices will continue to remain under pressure in light of uncertainty around demand levels noting recent decline in energy import levels in Japan and South Korea

Sources: BPNG, 2016 PNG Budget, IMF, World Bank, NSO, FT

together it's possible

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