MACQUARIE FUNDS GROUP
Economic Commentary
November 2008

MACQUARIE

Market highlights for the month were:

> Financial market instability continued through November given concerns regarding the effects of deleveraging on markets and the broader economy.

> Global government authorities demonstrated their willingness to address financial market dislocations. Significant measures were undertaken which appear to have alleviated market concerns to some degree. The market eagerly awaits further fiscal packages from various governments, especially from the US and any further policies from China.

> While financial markets have been weak, the real economy has also weakened significantly and many industrialised countries are now in technical recessions.

> In response to the deteriorating global and domestic economic outlook, the RBA reduced interest rates by a further 0.75% during the month.

Financial market instability continued through November as concerns remained regarding deleveraging and its effects on the broader economy. This saw the MSCI World Index fall a further 6.0% in November, and the USD appreciation continue, albeit at a slower pace than in previous months. However, encouragingly, government authorities demonstrated their willingness address financial market dislocations. Significant measures were undertaken, particularly in the US, which appear to have alleviated market concerns to some degree, with bond yields actually falling over the month.

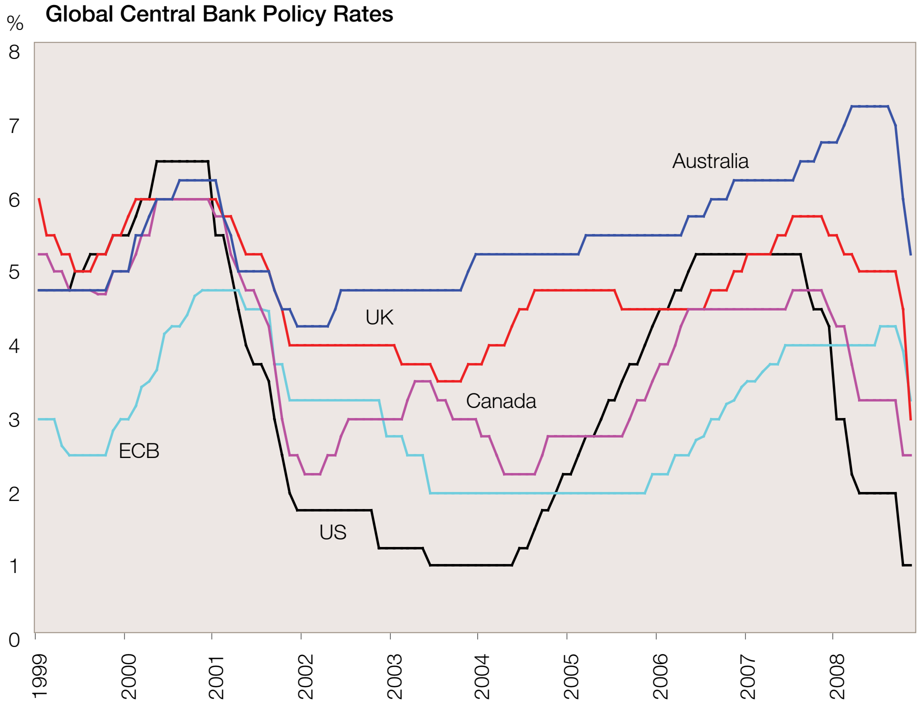
The most prominent market intervention in November was the US Government's bailout of Citigroup, the largest financial sector bailout to date. The US Treasury announced it would use approximately $30bn of TARP funds to ring fence more than $300 billion worth of troubled mortgage assets. The Fed announced another program under the acronym TALF aimed at improving market liquidity, which will see them use their balance sheet to purchase up to US$600 billion worth of GSE debt and mortgage-backed securities. Finally, the Federal Deposit Insurance Corporation announced they would guarantee term funding for US financial institutions. Together these measures helped to thaw credit market to some degree, such that US mortgage rates finally fell. To date, mortgage rates had remained elevated since the onset of the crisis despite the 4.25% point reduction in the fed funds rate.

On the fiscal policy front, the UK Government announced a sizeable package primarily aimed at helping businesses, but also included a reduction in the VAT. Many countries yet to announce fiscal packages, and in particular, markets eagerly anticipate the announcement of fiscal policies of the new Obama Administration, likely to be seen in mid-January, as well as further policies that are likely to be announced in China.

While financial markets have been weak, the real economy has also weakened significantly and many industrialised countries are in technical recessions (the respected National Bureau of Economic Research has dated the US recession as having started in December 2007). The high frequency data continued to print poorly in November across most economies and suggests recessions continued into the fourth quarter. In the US, consumers are especially reticent to spend, with retail and motor vehicle sales continue to fall at rapid clip, and sentiment weaker in line with softer employment data. Businesses also face increasingly challenging conditions, as access to finance remains limited, and foreign demand, which previously offset domestic weakness, continues to soften. The auto sector in particular faces challenging conditions and is the midst of appealing to US congress for assistance. Against this backdrop, inflation has become yesterday's story to be replaced with deflation fears as the monthly CPI and PPI data posted declines, and the Prices Paid component of the ISM survey fell to its lowest reading since 1949. In response, the Fed cut the fed funds rate by another 50bp to 1.00% and indicated that Japanese-style quantitative easing is likely to be undertaken once the zero-lower bound on interest rates is reached.

In other major industrialised economies, the economic landscape is equally as bleak. European measures of business confidence all continued to decline in November, and industrial production plunged further. Consumers retreated further in the month, and declines in confidence measures suggest further falls in consumption are to come in the months ahead. Falls in inflation were also recorded across the euro area in November no doubt comforting the prudent ECB, which cut its official policy rate by 50bp early to month to 3.25%. The Bank of England also eased monetary policy, cutting the repo rate by 150bp early in November in response to its ever-deteriorating economy. The magnitude of this cut shocked financial market participants, as did the dovish nature of the quarterly inflation report, which suggest the further sizeable cuts are to come.

Global Central Bank Policy Rates



Source: Thomson Reuters

In Australia, economic activity continued to slow over the month. Households have continued to pare back spending, and housing activity data remains weak despite lower interest rates and the increased First-home Owner Grant. November also saw a sharp deterioration in business sentiment as the weak outlook for the global economy became increasingly apparent. There were however a few bright spots: employment recorded strong gains (though this may reflect statistical noise) and consumer confidence improved, most likely in reaction to October's generous fiscal stimulus measures and the rapid rate cutting campaign by the RBA. The RBA cut the cash rate by a further -75bps in November and signalled that more cuts were on the way.

Contact details

Macquarie Funds Group Client Service on 1800 814 523
8.30 am to 6.00 pm, Monday to Friday (Sydney time)

www.macquarie.com.au/mfg
email: mfg.clientservice@macquarie.com

Macquarie Funds Group
PO Box R1723, Royal Exchange NSW 1225