QUARTERLY NEWSLETTER – July 2017

Major Indices

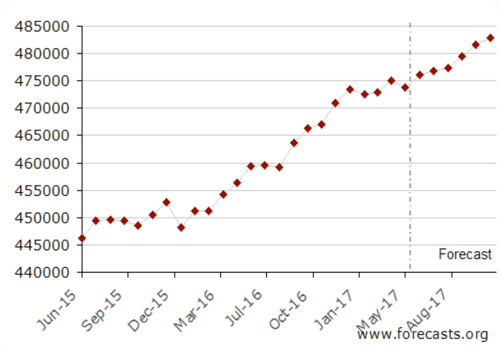
	Currency (AUD)	Interest Rate (%)	Share Index	*PE ratio (historical earnings)	Min daily wage (USD)	GDP Forecast (2018) IMF	Population (million)	Gov. Debt as a % GDP (as of 2016)
Australia	1.00	1.50	All Ords – 5,764	17.8 (All Ords)	136	3.0	24.5	46
USA (Dollar)	0.77	1.25	S&P 500– 2,423	21.6	58	2.5	325	74
Japan (Yen)	86	-0.1	Nikkei 225 – 20,033	15.3	85	0.6	127 (stagnant)	234
China (Yuan)	5.22	4.35	CSI 300 -3,666 Hang Seng 25,764	China-14.6 Hong Kong- 14.7	9.60	6.2	1,384	20
India (Rupee)	50	6.25	BSE 200– 4,149	20.6	3.40	7.7	1,317	52
Europe (Euro)	0.67	0.00	DJ Stoxx 50 3,441	19.8	56	1.5 (Germany)	738 (stagnant)	69 (Germany)
UK (pound)	0.59	0.25	FTSE 100 – 7,312	24.3	80	1.5	65 (stagnant)	92
Global	N/A			20.3		3.6	7,500	

*PE ratios (based on historical earnings),
10 Yr Bond Rate – 2.30% US 30 Yr Bond Rate – 2.83% Source: Bloomberg NB: Fastest growing population is by far Africa.

Commodities

Oil –Nymex (WTI) (USD/barrel)	46	**Iron Ore** ($/tonne) spot price	64
Natural Gas ($per million mbtu)	3.04	**Copper** (USD/pound)	2.70
Lithium(contract) ($/tonne)	12-15,000	**Nickel** (USD/pound)	4.24
Uranium (USD/pound)	20.50	**Zinc** (USD/pound)	1.25
Gold (USD/ounce)	1,241	**Aluminum** (USD/pound)	0.87
Wheat (cents/bushel)	525	**Corn** (cents/bushel)	380
Baltic Dry Index(BDI) +	849 (lower)	**Dow Jones Transport Index(DJT)**	9,563 (rising slightly)
US retail sales forecasts (million USD per month)	July(f) 476	Aug(f) 477	Sept(f) 479
Chinese PMI manufacturing	April (Caixin) 51.2	May (Caixin) 50.3	June (Caixin) 49.6

U.S. Retail Sales



Commentary – Past 3 months

The past 3 months for share markets was marked by a continuation of the Trump rally, albeit at a slower pace. Almost all major global stock markets rose over the quarter, with only Australia falling. Australian commercial property rose slightly.

Global share market Prices to Earnings (PE) ratios are definitely stretched now with the PE for the Global 100 at 20.3. The US PE is now at 21.6 and looking expensive relative to most other countries, especially as rates are rising. The talk of a US corporate tax cut is helping lift valuations. Asia is on a PE of 14.5 and is still reasonable value, and China with a PE of 14.6 is still priced well, but probably only fair value considering China's debt issues. Hong Kong still looks attractive with PEs of 14.7. India is at last looking reasonable on a PE of 20.6, given their 7.2% 2017 forecast growth rate.

Global GDP is forecast by the IMF for 2018 at 3.6% in 2018, up from 3.4% in 2017.

USA economy is doing ok, and the IMF forecast is for 2.3% GDP in 2017. The IMF forecasts this to improve to 2.5% in 2018. President Trump has guided for 3-4% GDP in his term.

Europe is still struggling along with anemic growth, Germany at just 1.5%, also forecast for 1.5% in 2018.

China is doing better than expected thanks to a pickup in the property sector. The IMF has upgraded 2017 GDP to 6.6%, and also upgraded 2018 GDP forecast to be 6.2%. China is spending big on infrastructure, and building the Silk Road railway and highway from China to Europe under their "One belt One road" master plan.

Australia's economy has been anemic so far in 2017, growing just 0.3 % in the first quarter. The IMF has forecast 2017 growth to reach 3.1%, which is looking rather optimistic.

India is still doing quite well despite a slower than expected first quarter with 6.2% annualized growth. The IMF forecasts 2017 growth at 7.2%, and 2018 growth to increase to 7.7%.

Emerging Market countries growth forecasts have been scaled back recently, with the IMF projecting 4.5% average growth in 2017 and 2018.

Interest Rates remained the same in most of the developed world over the past quarter. The exception was the US raising rates by 0.25% to reach 1.25%.

US employment fell by 0.4% to 4.3%, and **Australia** fell by 0.4% to 5.5% unemployed despite a slow economy, which is a bit contradictory. Both countries have high underemployment rates, suggesting their jobs markets are not as strong as the statistics would suggest.

US long term bonds rates were slightly lower this quarter, as the market is thinking US rates will not rise too fast.

Inflation has still been mild in most countries and currently not a concern.

Currencies over the quarter saw the Euro and UK pound gain. The Aussie dollar strengthened slightly against most currencies (except the Euro and pound).

Population comment – It is interesting to note that India's population is growing quite rapidly and will soon overtake China as the world's most populous country. Asia is home to 60% of the World's population.

Commodities

Oil fell back slightly this past quarter from USD 50 to USD 46. Oversupply concerns persist, and demand is weak, and may weaken further as people adopt electric vehicles.

Natural Gas also fell back slightly this past quarter from USD 3.23 to USD 3.04, following oil's lead.

Lithium Carbonate China spot prices have stabilized between USD 15-20,000 a tonne, or around12-15,000 a tonne for large contract buyers. Lithium prices are up 9% the past 6 months.

Copper rose slightly again this quarter from USD2.65 to 2.70 per pound. **Zinc** and **Aluminium** went sideways, whilst **Nickel** fell and is causing many nickel miners to close.

Iron Ore prices fell from $89 to $64 a tonne.

Uranium fell from USD 23 to USD 20.5 per pound.

Gold moved sideways from $1,250 to $1,241 per ounce.

Soft commodities (wheat and corn) both rose strongly, especially wheat.

Australian Resources price earnings ratio is still cheap at 11.9.

Commentary – Forecast next 6 months

Two of the four leading indicators are now positive, one neutral, and one negative (but maybe turning positive the past week), after 3 being positive last quarter. Of note China has slowed a bit in particular China construction, and the US still looks strong.

Dow Jones Transport Index (DJT) is another leading indicator. This index tells us how the US transport companies such as shipping, rail and air are doing. It is a good early indicator if the USA economy is slowing. In 2007, the DJT peaked in July. This was about 6 months before the GFC began. The DJT increased again last quarter from 9,116 to 9,563. A positive sign for the US.

US Retail sales are forecasted to rise. A positive sign for the US.

The Baltic Shipping Index (BDI) – (the cost to ship raw materials such as coal & iron ore) was dropped from last quarter (from 1,086 to 849), rebounding slightly in the past week. A negative sign for China and the resources sector, however it is possible we have just seen the dip. A negative sign; however perhaps just turning positive now.

The HSBC Caixin Chinese Manufacturing PMI index –It has fallen slightly over the quarter with June reading 49.6 showing China's manufacturing sector is slightly negative to neutral. The PMI Services Index has remained strong. Overall, a neutral sign for China.

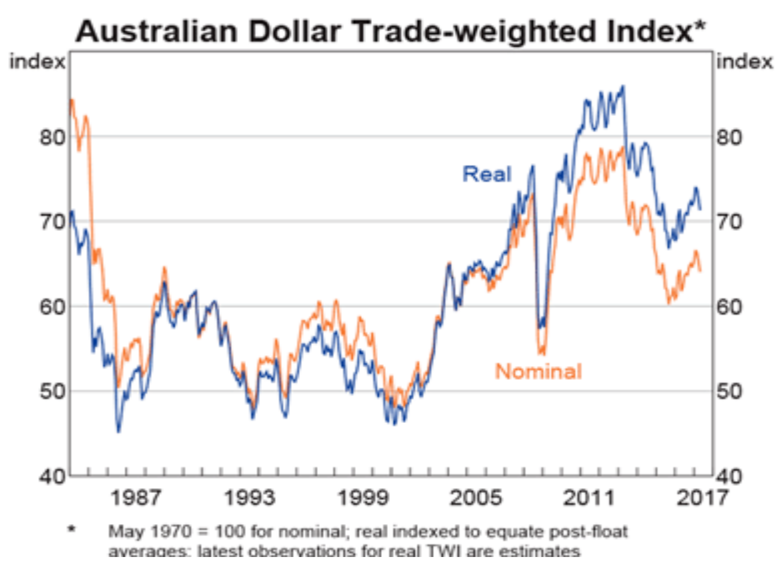
A summary of the above leading indicators right now is to expect "China to do ok, and the US to do well". The recent commodities fall may soon pass, but it is a bit too early to say.

Ideas

- Growth and Aggressive investors could buy into the disruptive technology areas such as electric vehicles, lithium/cobalt miners, solar/wind energy, energy storage and IT areas such as artificial Intelligence (AI), 3D printing, cloud, big data, and robotics.
- Moderate risk (and retiree) investors should be sure to have at least 60% in safe areas, as valuations are now stretched, global debt elevated, and global interest rates starting to rise.
- All investors should still keep at least some money in cash or safe fixed interest
- Sell Australian residential property unless it's your home.
- Invest in countries with good demographics, jobs growth, low debt and positive GDP.
- Buy direct property in countries that are benefitting from globalization and where property is still cheap. Eg: Philippines (household debt/GDP is a very low around 10%), Thailand, Indonesia, Malaysia, Vietnam, Mexico, Myanmar, Cambodia, and Laos.
- AUD still likely to fall long term, and is still overvalued.

AUD v Trade Weighted Index (TWI) – Aussie dollar still overvalued

The AUD is currently 0.77, compared to the TWI of 64.5, or about 19% overvalued.



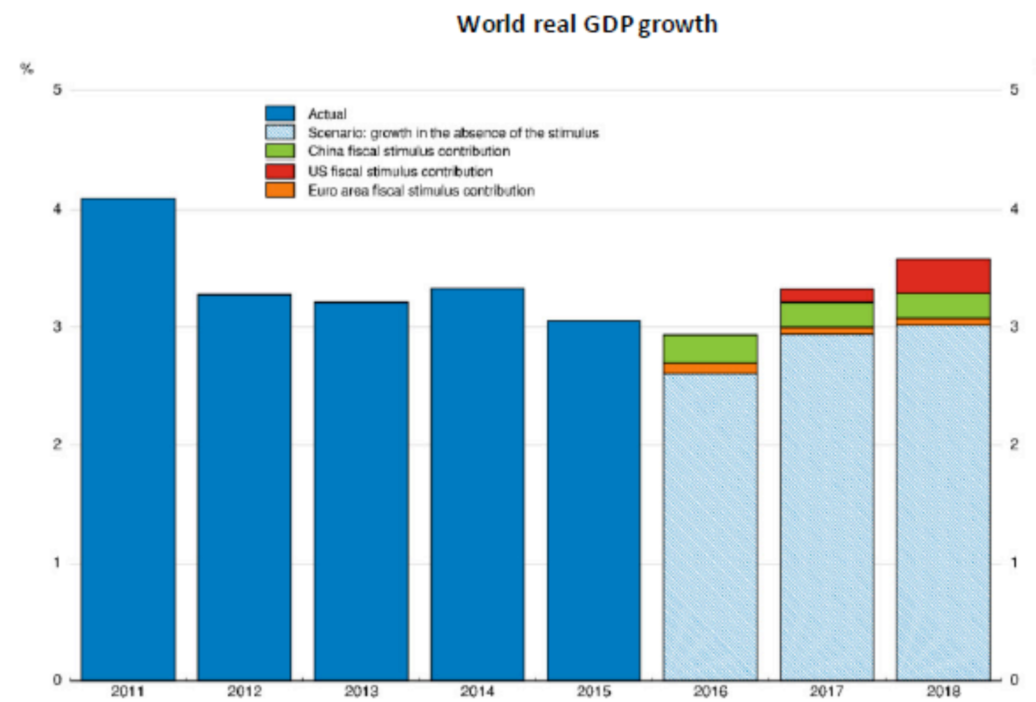
Global share markets discussion on valuation

Overall the global markets are definitely a bit overvalued right now based on PE ratios, long term charts, and the Buffet indicator (market cap / GDP). Note the later is specific to US shares.
Off course with global interest rates very low, the rule of 20 allows PEs to be a bit higher. It says a fair PE ratio is the current market PE less the reserve bank interest rate.
So in the US a fair PE would be 20 – 1.25 = 18.75. The US PE is currently 21.6, which is 15% above 18.75 (fair value).
The Buffett indicator chart below also suggest US markets are about 33% overvalued (market cap is above GDP, or 133% of GDP).
The flip side is that interest rates are not really rising much, and global GDP is improving. The IMF quote from April 2017

"Global economic activity is picking up with a long-awaited cyclical recovery in investment, manufacturing, and trade, according to Chapter 1 of this World Economic Outlook. *World growth is expected to rise from 3.1 percent in 2016 to 3.5 percent in 2017 and 3.6 percent in 2018."*
So overall, best to be just a bit more cautious at this time, but not super cautious as global growth is improving after a few slow years (2015, 2016)."

My current recommendations are for moderate risk clients to be around 60% in safe assets (cash, term deposits). I expect in the next year we will likely see a market pull back of around 10-20%, and then markets will be back to normal. No signs of a second GFC coming, apart from elevated global debt. If interest rates were to rise rapidly, share and property markets will fall heavily.

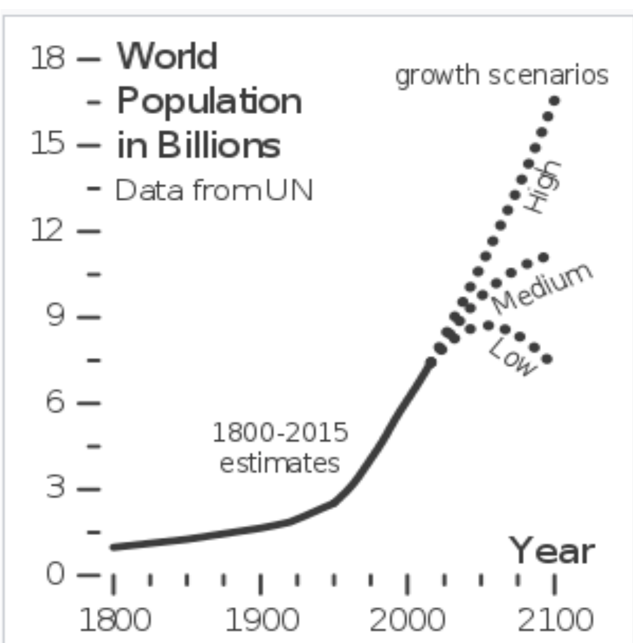
World GDP improving in 2017

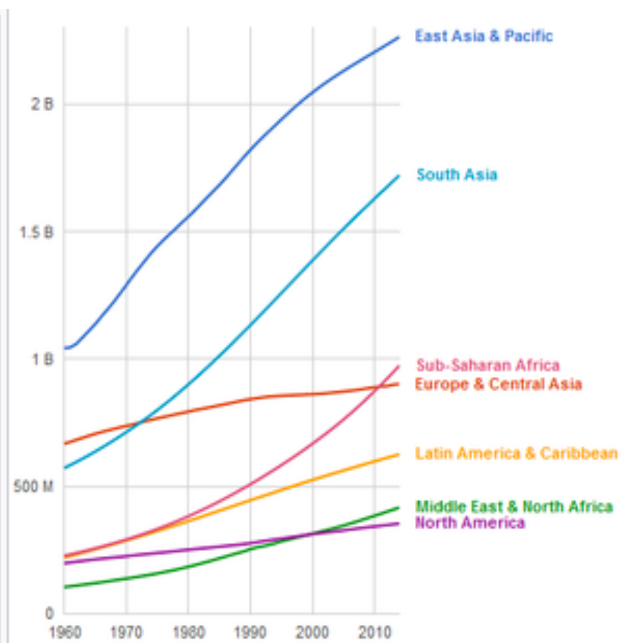


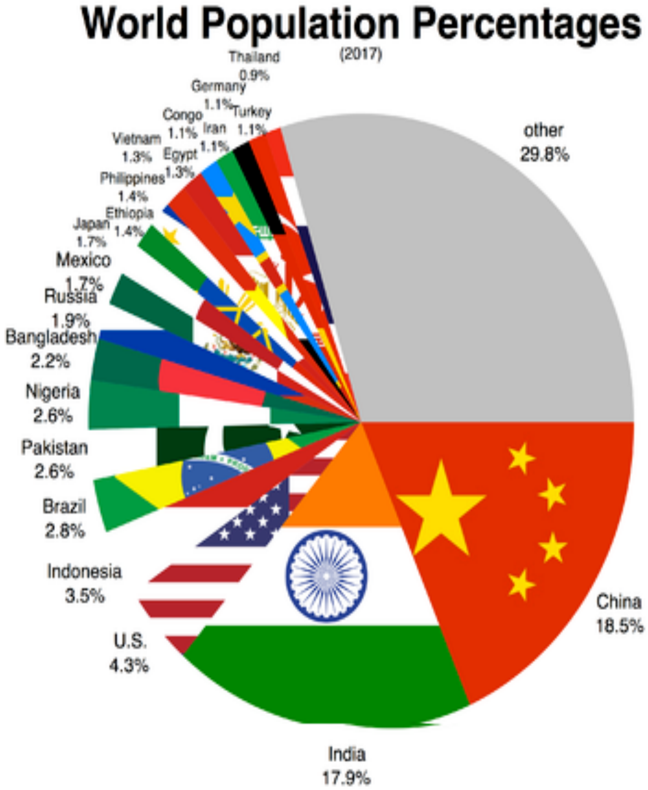
Population study

One of my favourite past times is looking at the big picture of the world – in particular demographics and population growth. Below are some interesting charts. If the global population is increasing that is generally positive for stock markets and property markets.

World population by 2050 is forecast to be between 8.3 and 10.9 billion – Most in Asia







World population (millions, UN estimates)[24]

#	Top ten most populous countries	2000	2015	2030*
1	China*	1,270	1,376	1,416
2	India	1,053	1,311	1,528
3	United States	283	322	356
4	Indonesia	212	258	295
5	Brazil	176	208	229
6	Pakistan	138	189	245
7	Nigeria	123	182	263
8	Bangladesh	131	161	186
9	Russia	146	143	139
10	Mexico	103	127	148
	World total	6,127	7,349	8,501

Notes:

- China = Mainland China only
- 2030 = Medium variant

My latest Seeking Alpha articles
Rather than list them, you can follow the link below.
You can view my articles here- http://www.hnwfinancialadvising.com.au/hnw-articles.html
To find out more please contact an adviser at contactus@hnwfinancialadvising.com.au.

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