QUARTERLY NEWSLETTER – January 2018

Major Indices

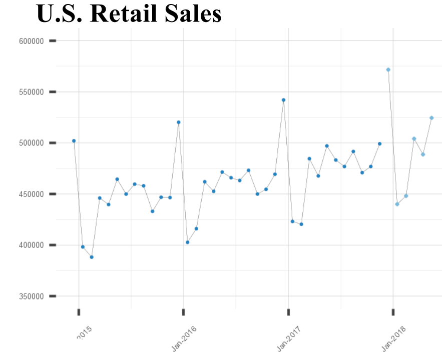
	Currency (AUD)	Interest Rate (%)	Share Index	*PE ratio (historical earnings)	Min daily wage (USD)	GDP Forecast (2018) IMF	Population (million)	Gov. Debt as a % GDP (as of 2016)
Australia	1.00	1.50	All Ords – 6,167	17.5 (All Ords)	136	2.9	24.7	43
USA (Dollar)	0.78	1.50	S&P 500– 2,673	23.8	58	2.3	326	108
Japan (Yen)	88	-0.1	Nikkei 225 – 22,764	17.2	85	0.7	127 (stagnant)	240
China (Yuan)	5.08	4.35	CSI 300 -4,030 Hang Seng 29,919	China-17.6 Hong Kong- 15.7	9.60	6.5	1,388	48
India (Rupee)	50	6.00	BSE 200– 4,686	23.0	3.40	7.4	1,326	69
Europe (Euro)	0.65	0.00	DJ Stoxx 50 3,503	20.4	56	2.0	738 (stagnant)	65 (Germany)
UK (pound)	0.58	0.50	FTSE 100 – 7,687	24.5	80	1.5	66 (stagnant)	88
Global	N/A			21.7		3.7	7,600	

*PE ratios (based on historical earnings),
10 Yr Bond Rate – 2.41% US 30 Yr Bond Rate – 2.73% Source: Bloomberg NB: Fastest growing population is by far Africa.

Commodities

Oil –Nymex (WTI) (USD/barrel)	60	**Iron Ore** ($/tonne) spot price	74
Natural Gas ($per million mbtu)	2.95	**Copper** (USD/pound)	3.26
Lithium(contract) ($/tonne)	12-15,000	**Nickel** (USD/pound)	5.67
Uranium (USD/pound)	24.7	**Zinc** (USD/pound)	1.50
Gold (USD/ounce)	1,303	**Aluminum** (USD/pound)	1.02
Wheat (cents/bushel)	427	**Corn** (cents/bushel)	351
Baltic Dry Index(BDI) +	1,366 (lower)	**Dow Jones Transport Index(DJT)**	10,612 (rising strongly)
US ISM manufacturing index	Oct 58.7	Nov 58.2	Dec
Chinese PMI manufacturing	Oct (Caixin) 51.0	Nov (Caixin) 50.8	Dec (Caixin) 51.5

U.S. Retail Sales



Commentary – Past 3 months

The past 3 months for share markets was another strong quarter of gains. Almost all major global stock markets rose over the quarter, with only Europe falling. Japan was the standout performer rising about 10%. Australian commercial property rose quite well.
Global share market Prices to Earnings (PE) ratios are definitely stretched now with the PE for the Global 100 at 21.7 the same level as the past quarter ended. The US PE is now at 23.8 and looking expensive relative to most other countries (except UK which is on a PE of 24.5), especially as rates are rising. The Buffett Indicator (US market cap/US GDP) is at 143%, suggesting the US stock market is now 43% overvalued. The Trump tax plan may reduce this about 15%.
Asia is on a PE of 16.5 and is about fair value still. China with a PE of 17.6 is becoming overvalued. Hong Kong still looks reasonable with a PE of 15.9. India is looking a bit expensive on a PE of 23, despite their high growth rate.
Global GDP is forecast by the IMF for 2018 at 3.7% in 2018, up from 3.4% in 2017.
USA economy is doing ok, and the IMF forecast is for 2.3% GDP in 2018. President Trump has guided for 3-4% GDP in his term.
Europe is still improving slightly but still with slow growth, with Europe GDP forecast at 2.0% in 2018.
China is doing better than expected thanks to a 2017 pickup in the property sector. The IMF has 2018 China GDP forecast to reach 6.5%. China is also 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 continues to be mediocre. The IMF has forecast 2018 growth to reach 2.9%.
India has slowed slightly but is still doing well, with the IMF forecast 2018 growth at 7.4%.
Emerging Markets are doing better with the IMF projecting 4.9% average growth in 2018.
Interest Rates remained the same in most of the developed world over the past quarter with the exceptions of the USA and UK both raising rates by 0.25%.
US employment fell by 0.3% to 4.1%, and **Australia** fell by 0.2% to 5.4%. 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 mostly unchanged this quarter.
Inflation has still been mild in most countries and currently not a concern.
Currencies over the quarter saw minimal change with the Aussie dollar and US dollar weakening very slightly. The Trade Weighted Index (TWI) fell to 64.9 compared to the AUD at 0.78 indicating the AUD is still around 20% overvalued.
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. The word's total population is now past 7.6 billion.

Commodities
Oil rose strongly this past quarter from USD 51to USD 60.
Natural Gas fell slightly this past quarter from USD 3.02 to USD 2.95.
Lithium Carbonate China spot prices steadied last quarter, with China spot prices still around USD 18-20,000 a tonne, or around13-15,000 a tonne for large contract buyers. Lithium prices are up about 10-20% over the past year.
Copper rose again this quarter from USD 2.95 to 3.26 per pound. **Zinc, Aluminum** rose slightly an, while **Nickel** rose very strongly over the quarter.
Iron Ore prices moved sideways from USD 76 a tonne to USD 74 a tonne.
Uranium rose quite strongly from USD 20.5 to USD 24.70 per pound.
Gold moved up from $1,282 to $1,303 per ounce.
Soft commodities (wheat and corn) both fell over the quarter, especially wheat.
Australian Resources price earnings ratio is now back to fair value at 15.5.

Commentary – Forecast next 6 months

Three of the **five** leading indicators are now positive, with one neutral.

Dow Jones Transport Index (DJT) is a US 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 very strongly last quarter from 9,914 to 10,612. A positive sign for the US.

US Retail sales trend higher and are forecasted to continue to trend higher. A positive sign for the US.

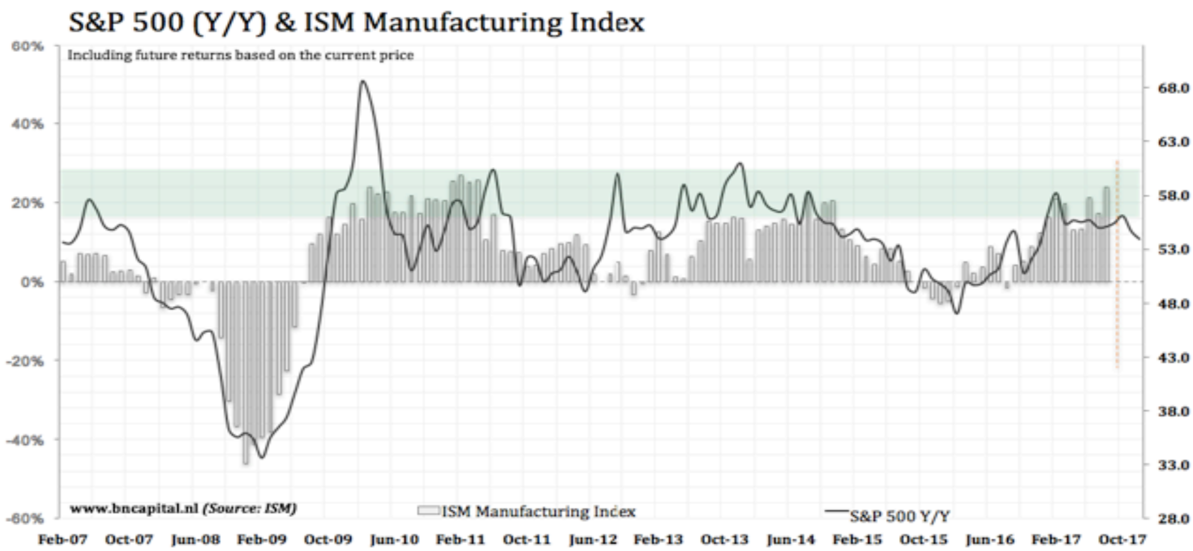
US ISM Manufacturing index - The latest numbers show that the ISM index remains strong at 58.2 points in November. A positive sign for the US.

The HSBC Caixin Chinese Manufacturing PMI index –It been steady over the quarter with the December reading 51.5 showing China's manufacturing sector has picked up slightly. The PMI Services Index has remained strong. Overall, a neutral or slight positive sign for China.

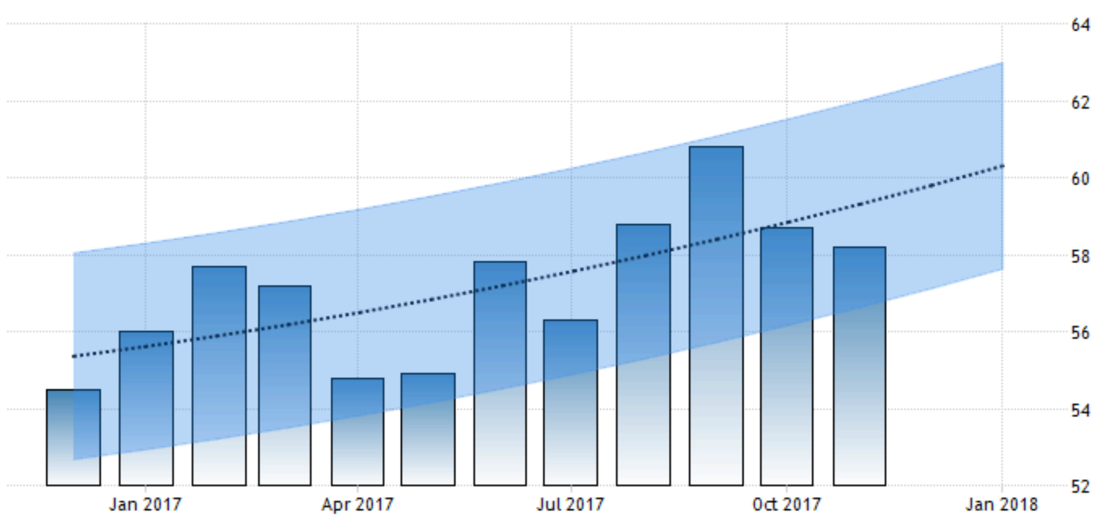
The Baltic Shipping Index (BDI) – (the cost to ship raw materials such as coal & iron ore) dropped recently after a previous surge to end the quarter at 1,366. It should be noted the BDI has been in a steady uptrend until last month. A negative recent sign for China and the resources sector.

A summary of the above leading indicators right now is to expect a positive quarter ahead, but we could expect some slowdown in resources and China. Risks do remain – especially geo-political with North Korea, high current stock market valuations, and slightly rising US interest rates.

US stock market correlation to the US ISM index – Highly correlated



United States ISM Purchasing Managers Index (PMI) and forecast



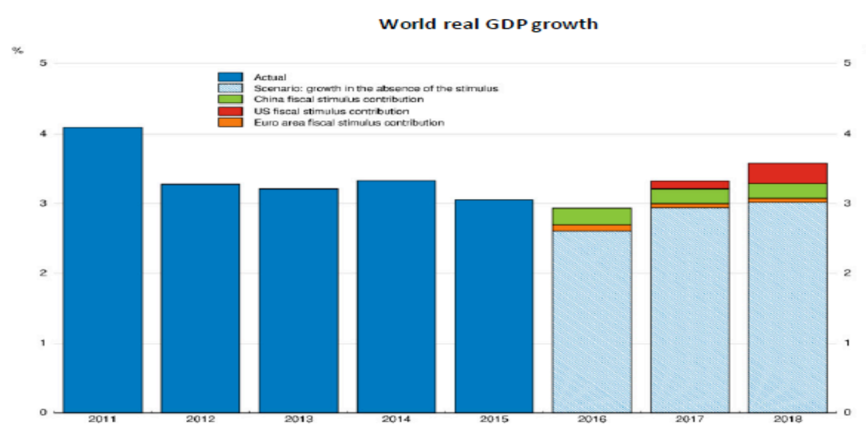
Ideas

- 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 50-60% in safe areas, as valuations are now significantly 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.
- AUD still likely to fall long term, and is still overvalued.

Global share markets discussion on valuation

Put very simply, the past decade since the GFC has had extremely low interest rates which have resulted in a significant property and stockmarket boom, and clearly overvalued markets.
2017 had many parallels to 2007 such as a booming market, and elements of euphoria – think Bitcoin for example. I will not be surprised to see 2018 be a mini version of 2008 when markets fell. By that I mean we could expect a 10-20% market fall in 2018 to bring valuations back to fair levels, especially in the USA and UK. The only strong positive is global growth appears to be picking up.
Investors should remain cautiously invested, with moderate risk clients remaining about 50% in safe areas for now.

World GDP forecast to continue improving in 2018



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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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