QUARTERLY NEWSLETTER – October 2018

Major Indices

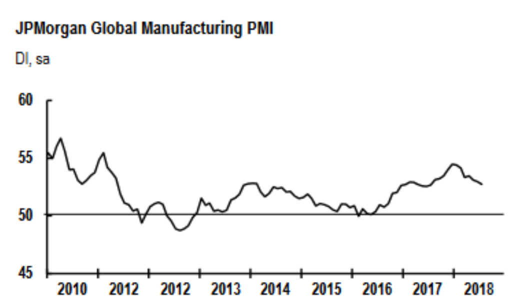
	Currency (AUD)	Interest Rate (%)	Share Index	*PE ratio (historical earnings)	Min daily wage (USD)	GDP Forecast (2019) IMF	Population (million)	Gov. Debt as a % GDP (as of 2016/17)
Australia	1.00	1.50	All Ords – 6,325	16.6 (All Ords)	136	2.8	25.0	42
USA (Dollar)	0.72	2.25	S&P 500– 2,914	25.0	58	2.7	328	105
Japan (Yen)	82	-0.1	Nikkei 225 – 24,120	13.9	85	1.5	126 (stagnant)	253
China (Yuan)	4.96	4.35	CSI 300 -3,438 Hang Seng 27,788	China-12.5 Hong Kong- 10.0	9.60	6.3	1,394	48
India (Rupee)	52	6.50	BSE 200– 4,631	20.9	3.40	7.5	1,337	69
Europe (Euro)	0.62	0.00	DJ Stoxx 50 3,399	15.3	56	1.5	733 (stagnant)	64 (Germany)
UK (pound)	0.55	0.75	FTSE 100 – 7,510	14.3	80	1.5	66 (stagnant)	85
Global	N/A			20.8		3.9	~7,700	

*PE ratios (based on historical earnings),
10 Yr Bond Rate – 3.06% US 30 Yr Bond Rate – 3.21% Source: Bloomberg NB: Fastest growing population is by far Africa.

Commodities

Oil –Nymex (WTI) (USD/barrel)	73.5	**Iron Ore** ($/tonne) spot price	69
Natural Gas ($per million mbtu)	3.01	**Copper** (USD/pound)	2.81
Lithium(contract) ($/tonne)	16,000	**Nickel** (USD/pound)	5.72
Uranium (USD/pound)	27.5	**Zinc** (USD/pound)	1.16
Gold (USD/ounce)	1,191	**Aluminum** (USD/pound)	0.92
Wheat (cents/bushel)	509	**Corn** (cents/bushel)	356
Baltic Dry Index(BDI) +	1,540 (higher)	**Dow Jones Transport Index(DJT)**	11,379 (higher)
US ISM manufacturing index	July 58.1	August 61.3	Sept
Chinese PMI manufacturing	July (Caixin) 50.8	August (Caixin)	Sept (Caixin)

Global manufacturing PMI



Commentary – Past 3 months

The past 3 months for share markets was mostly up
Most major global stock markets moved up over the quarter, with only China and Hong Kong falling on trade war concerns. Australian commercial property rose.
Global share market Prices to Earnings (PE) ratios have not changed much in the past 3 months. The US PE is now at 25.0 and still looking expensive relative to most other countries, especially as rates are rising. The Buffett Indicator (US market cap/US GDP) is at 148%, suggesting the US stock market is 48% overvalued. The Trump tax plan may reduce this overvaluation with a boost in US corporate earnings.
Asia is on a PE of 11.8 and is quite cheap (partly due to fears of a trade war). China with a PE of 12.5 is also well valued. Hong Kong is a standout for value on a PE of 10.0. India is on a high PE of 20.9, but has a high growth rate. The trade war has sent Chinese shares and China's PE lower.
Global GDP is forecast by the IMF at 3.9% in 2019, the same as 3.9% in 2018.
USA economy is doing well, and the IMF forecast is for 2.7% GDP in 2019. President Trump has guided for 3-4% GDP in his term, and the latest US GDP figure was 4.2%.
Europe is forecast to slow with Europe GDP forecast at 1.5% in 2019.
China is now starting to slowdown as confidence falls and the trade war with the US intensifies.
Australia's economy continues to be mediocre. The IMF has forecast 2019 growth to reach 2.8%.
India is still doing well, with the IMF forecast 2019 growth at 7.5%.
Emerging Markets are doing well with the IMF still projecting 5.1% average growth in 2019.
Interest Rates rose by 0.25% in the USA and the UK, while the rest of the developed world was unchanged. India also rose by 0.25%.
US employment rose 0.1% to 3.9%, and **Australia** fell by 0.1% to 5.3%. Both countries have high underemployment rates, suggesting their jobs markets are not as strong as the statistics would suggest.
US long term bonds rates rose slightly over the quarter.
Inflation has still been mild in most countries with some signs of increasing.
Currencies over the quarter saw the US dollar strengthen/Australian dollar and the emerging market currencies weaken. The Trade Weighted Index (TWI) remained at 0.62 compared to the AUD at 0.72 indicating the AUD is still around 14% 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 7.7 billion.

Commodities
Oil fell this past quarter from USD 79 to USD 73.50.
Natural Gas rose this past quarter from USD 2.89 to USD 3.01.
Lithium Carbonate China spot prices have fallen from elevated levels, with China spot prices now around USD 14,000 a tonne. Global contract prices are up about 20% in 2018 to ~16,000 a tonne for large contract buyers.
Cobalt prices have fallen to US$28.12, after peaking above US$40.
Copper fell this quarter from USD 298 to USD 2.81 per pound. Most of the other base metals also fell on trade war concerns; except vanadium that rose again.
Iron Ore prices rose from USD 65/tonne to USD 69/tonne.
Uranium moved up slightly from USD 22.70 per pound to USD 27.50/lb.
Gold moved down from $1,250 to $1,191 per ounce.
Soft commodities – Wheat rose and corn rose very slightly over the quarter.
Australian Resources price earnings ratio is good value at 13.0.

Commentary – Next 6 months

The major concern right now is an escalating global trade war. Chinese shares have now lost 20% as has Hong Kong; indicating China will be worst affected by a US-China trade war.

Ideas

- Growth and Aggressive investors could buy into the disruptive technology areas such as electric vehicles, lithium/cobalt/vanadium 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 about 50-60% in safe areas, as valuations are still stretched in US markets (but ok in other regions), 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 further, and is still overvalued.

Conclusion

Stock market Valuations - Most metrics suggest the US stock market is still significantly overvalued. It appears to me that about a 20-30% market fall is necessary to get the US back closer to fair value. Having said that the US market may continue to trade at a premium valuation. Many other global markets valuations such as Europe, UK, Japan, China, Australia and Canada are at more attractive valuations than the US.

Forward indicators - Forward indicators are mixed. The Global PMI is still quite positive despite slowing slightly. The US continues to look very good with China having weaker forward indicators.

The above data suggests to me the global economy continues to do quite well; however trade war tariffs have caused a sudden worsening of investor sentiment. Slowly rising US interest rates and bond yields also need to be watched, with no panic needed as they are coming of a very low base. High debt related investments should be reduced. Right now a full blown trade war is a growing concern.

Investors should assess their portfolio and be sure they can hold long term in case a trade war breaks out. It would be wise to have at least 40% in cash or safe assets, and more if you are a conservative investor or retiree.

My latest Seeking Alpha articles
http://www.hnwfinancialadvising.com.au/hnw-articles.html

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