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September 2017 Quarter In Review

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Legislative changes

On line source Shed Connect revealed an unintended consequence of the reduction in the company tax rates for smaller companies. Franking credits earned at the former 30% rate can only be distributed at the new 27.5% rate. This means the excess credits can never be distributed. [Read the article.](#)

Markets and trend lines

The following charts show, respectively, the best fit of constant compound growth in the Australian and United States of America broad market indices together with some statistically derived probability percentiles. On this statistical basis, both markets provide reasonable value, but, on other measures, the US market, in particular, remains high.

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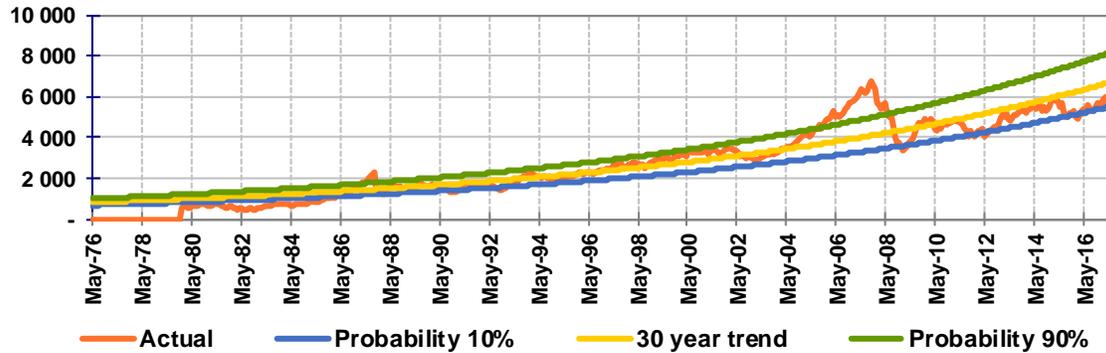
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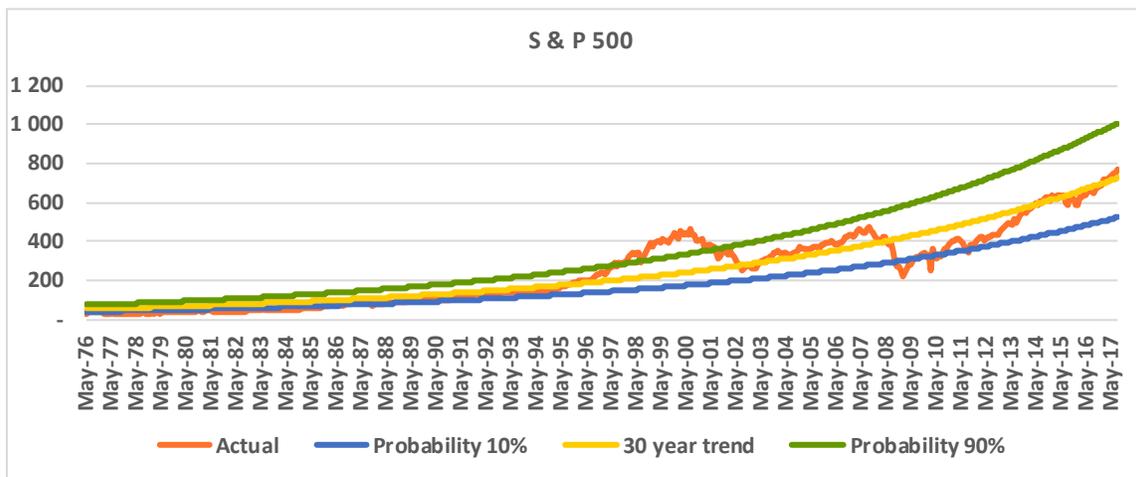


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Economic milestones

October will see the US Federal Reserve Board cautiously start to unwind the almost decade old money printing response to the Global Financial Crisis known as “Quantitative Easing”. QE involved buying private sector bonds from banks. The Fed will be allowing some of these bonds to mature, instead of “rolling them over”, thus reducing the amount of money in circulation.

On 1 September, the AFR reported two bits of good news – the growth of 18% in the expected capital expenditure by business referred to as a “welcome change from two years of stagnation” by an ANZ economist and the 3% annual GDP growth in the USA.

Good news continued on 5 September when the AFR reported the strongest wage growth for 3½ years. This is good news for the Federal budget which was predicated on what many saw as optimistic assumptions about wage growth.

As indicated in the table below, the unemployment rate continues to drift downwards, but underemployment is persistent.

Industrial relations confusion continued with the AFR reporting, on 30 August, the termination of the Murdoch University Enterprise Bargaining Agreement (EBA) on the University's application while other employers ditch their EBAs because of a new interpretation of the "better off overall" rule to mean that no individual can be worse off.

On 4 July 2017, the AFR noted that household debt to income ratio was at an all time high around 190%.

The attempts to deflate the property bubble gently continued in the quarter. Following its lead last quarter in effectively ceasing investor housing loans, AMP Bank has ceased allowing customers to increase their housing loans to provide cash for other purposes. This reflects concerns about high household debt to income ratios. Other banks are also tightening lending criteria.

On 9 August, the AFR reported that Citibank had released a list of 90 postcodes for which it will require deposits of up to 35% of purchase price for apartment loans.

On 28 August, the AFR reported that a number of investors who bought strata units off the plan against or without legal advice may suffer from the collapse of the developer.

Economic and market statistics

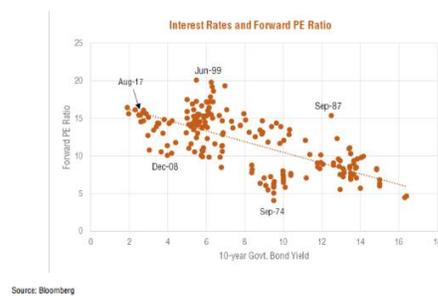
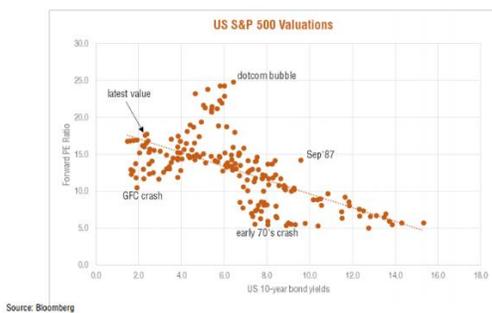
The following table shows key economic and market statistics.

		Now	1 year ago	3 years ago	7 years ago
S&P /ASX 200- Australia	Sep 17	5,682	5,436	5,293	4,583
Annual change to latest date			4.5%	2.4%	3.1%
S&P /ASX 200 dividend yield	Sep 17	4.37%	4.27%	4.65%	4.08%
S&P /ASX 200 P/E ratio	Sep 17	15.6	16.00	15.20	18.30
Topix- Japan	Sep 17	96.6	76.30	76.50	47.80
Annual change to latest date			26.6%	8.1%	10.6%
S&P 500- US	Sep 17	762.9	656.6	597.3	345.6

Annual change to latest date			16.2%	8.5%	12.0%
GDAXI- Germany	Sep 17	12866	10493	9454	6601
Annual change to latest date			22.6%	10.8%	10.0%
Average weekly earnings \$	Jun 17	1,543	1,516	1,454	1,250
Annual change to latest date			1.8%	2.0%	3.1%
Consumer price index	Jun 17	110.70	108.60	105.90	95.40
Annual change to latest date			1.9%	1.5%	2.1%
Unemployment	Aug 17	5.6%	5.70%	6.10%	5.00%
Gross domestic product \$ m per quarter	Jun 17	427,948	420,254	398,998	356,437
Annual change to latest date			1.8%	2.4%	2.6%
RBA cash rate 3 year	Sep 17	1.5%	1.50%	2.50%	4.50%
Commonwealth bond 10 year	Sep 17	2.1%	1.56%	2.80%	4.70%
Commonwealth bond	Sep 17	2.7%	1.99%	3.55%	5.00%
USD/AUD	Sep 17	0.8	0.76	0.88	0.97
Annual change to latest date	Sep 17		2.7%	-3.6%	-2.9%

Other people's views

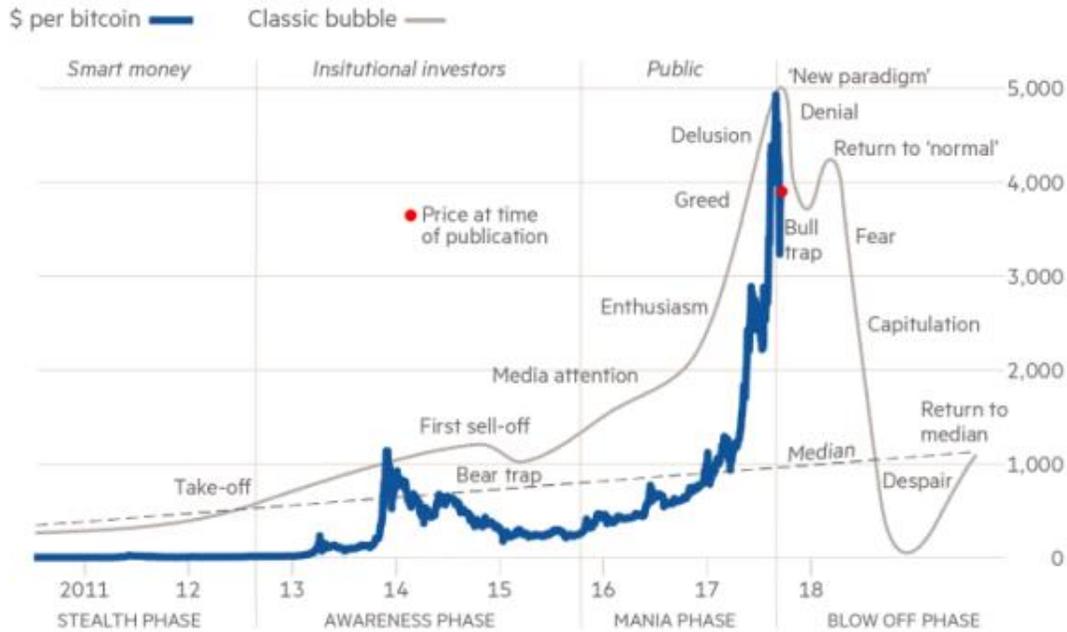
David Bassanese Chief Economist of [BetaShares](#) showed the following charts at a webinar on 24 August to support his view that USA and Australian shares are reasonably priced when one considers the historical relationship between forward price earnings ratios (the ratio of analysts' consensus next year earnings per share and the price) and the return on ten year Government bonds.



Lauren Broomham and Chris Baynes, writing in the retirement village industry e-magazine “the Weekly Source” take Fairfax papers and the ABC to task for their “[confused attack on retirement villages](#)” pointing out that the village that is the subject of the most recent attack is not subject to the relevant State Retirement Villages Act. The retirement village industry is not without its faults, but the irony that the problems highlighted have occurred because documents required by the regulator are too long for some people to read should not be lost. Andep’s view is that people contemplating entering a retirement village contract should seek legal and actuarial advice.

The exact source of this chart is unknown, Andep got it from Justin Byrne of Instreet.com.au. It is interesting in that it shows the build and break of bubbles, not just Bitcoin.

Is bitcoin heading into classic bubble territory?



Source: Thomson Reuters Datastream © FT

Products

The digitisation of financial services continues with insurer AAI Ltd (formerly Vero) offering on demand theft loss and damage cover for specific items under the name Trov Insurance. Users select items (for example Microsoft Surface Pro 4 I7/16gb/256gb), nominate their age and gender and get a quote giving a number of sums insured and excesses, as shown to the right. [More information](#)

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On the same theme of insurance innovation and in a meeting of the old and the new, the AFR of 31 August reported the “gearing up” of Friendsurance. This product, underwritten by the old (a Lloyds of London syndicate), protects the new (friends akin to Facebook). Insurance is limited to bicycles, but a rebate is paid if none of the insured’s “friends” makes a claim. This means the consumers effectively become the marketers and the risk evaluators.

An interesting reversal of digitisation was reported in the AFR of 5 September. ISelect is “mortarising” opening pop up kiosks to market its digital services in bricks and mortar stores.

Are index funds too much of a good thing? Hedge Fund manager Paul Singer was reported in the AFR of 7 August 2017 to have written “Passive investment is in danger of devouring capitalism. What might have been a clever idea in its infancy has grown into a blob which is destructive to the growth creating and consensus building prospects of free market capitalism”

The AFR reported on 7 August 2017 that UniSuper now has 60% of its investments internally managed. While this may contain costs, superannuation funds need to be careful not to risk poor performance by concentrating decision making too much.

The influence of index funds continues to be felt with the magazine [InFinance](#) revealing on 4 July 2017 its effect on producers of investment research (Equities research is on the precipice of immense change.). There is a smaller market for stockbroker research. It is also the case that manager are increasingly reliant on “big data” which they analyse internally. For example one can count cars in shopping centre car parks to gauge trade.

[Beta Shares](#) has released an Exchange Traded Fund linked to floating rate notes issued by Australian banks with 80% of the index comprising “Big 4” bank’s debt. The interest rate on these notes is set as a margin above the Bank Bill Swap Rate and resets quarterly – meaning the capital value of the notes is stable. The yield compares favourably with small term deposit rates.

Bitcoin and other crypto currencies continue to attract interest and attention, (AFR 1 September) being a legal method of payment in Japan (AFR 1 September). Later in the month the Chinese authorities prohibited so called “Initial Coin Offerings”.

[AustralianSuper](#) has announced it will commence “to age 65” income protection insurance from 28 October 2017.

It had to happen. Robots will now invest in robots. [ETF Securities](#) launched “ROBO”, claimed on 14 September to be Australia’s first “global robotics, automation and artificial intelligence exchange traded fund”.

The superannuation march of mergers rolls on with the merger of Concept One (a half billion dollar fund with strong links with private school teachers) merging with [WA Super](#).

WA Super, with roots in local government, is now the sole public offer fund domiciled in WA.

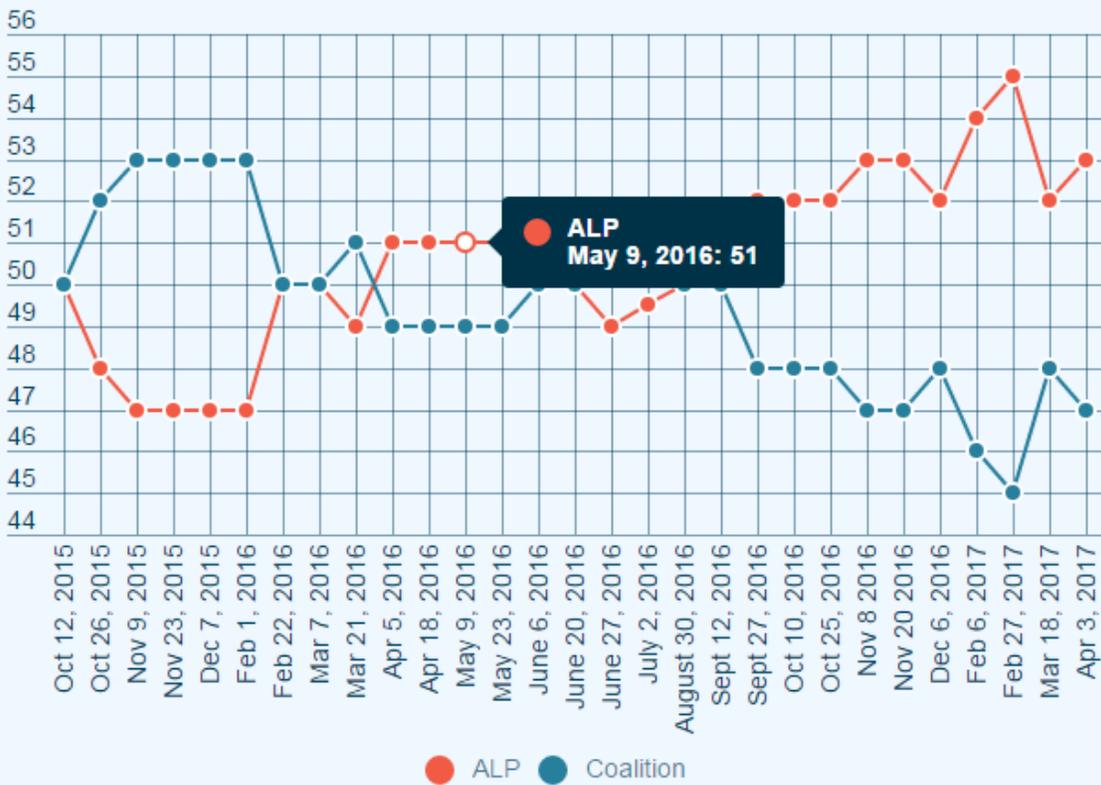
A new online financier of student loans primarily for vocational courses has emerged. [Study Loans](#) offers loans to full-time and part-time students to help meet the course fees. This can be as a complete alternative to the government system or as a supplement where government caps apply. Study Loans is partnering with selected education providers who have a strong track record of delivery courses with high completion rates and high job outcome rates to deliver finance to their students. To-date the company has received over 250 applications from education providers to join the platform. The company is seeking further debt investment to help generate further funds to provide to eligible students.

Politics

The following chart from theaustralian.com.au/national-affairs/newspoll tracks two party preferences.

TWO-PARTY PREFERRED

Based on the preference flow at the July 2016 federal election.



The AFR of 28 August reported the rise in the polls of the New Zealand Labour Party under a new leader Jacinda Ardern as new PM Bill English seeks to win his first election since taking over the prime ministership. The AFR saw parallels with the Australian situation of 2007 when voters tired of a competent but stale government. Voters turned out to be not sufficiently tired of the government to emphatically change it. This made the parallels with Australia even closer as negotiations proceed to determine which major party will govern.

The second last weekend in September saw centre right governments in both Germany and New Zealand retain power with reduced majorities. In New Zealand, all significant parties except Labour lost voter share. In Germany, the centrist parties both lost ground to the advantage of both the left and right. In both countries, the third highest voter getters were the populist right.

The next major elections to look forward to now are in Austria and Japan.

Andep news

On 1 July, Andep moved from the 8th to the 13th floor of 251 Adelaide Terrace.

Courts

This may have been shown in “Other People’s views”, but an [article by Morgan Solomon](#) of solicitors Solomon Hollett and discussions with other lawyers indicate the Courts are tightening up on challenges to wills with need prevailing over greed.

DRAFT