

Navigating 2009/10

The sharp rally in global sharemarkets since the March lows (up 31% at its peak) has come to an end, for now. Earlier this month, our All Ordinaries Index had surpassed the psychologically important 4000 level and consumer sentiment had its strongest gain in 22 years.

However, as expected, profit taking and a degree of nervousness has returned to the markets in recent weeks as doubts over the future strength of the US economic recovery gain momentum.

This is healthy and perfectly justifiable scepticism.

No one said recovery would be plain sailing (it rarely is), but clearly, where we are today is a vast improvement over the situation and psychology earlier this year. No longer are we reading news articles comparing 2008/09 to 'The Great Depression', and the prospect of 'global systemic collapse' isn't taken too seriously. Instead, most debate revolves around the length/depth of recession and the potential for recovery – this line of discussion should be vaguely, almost reassuringly familiar territory to seasoned investors.

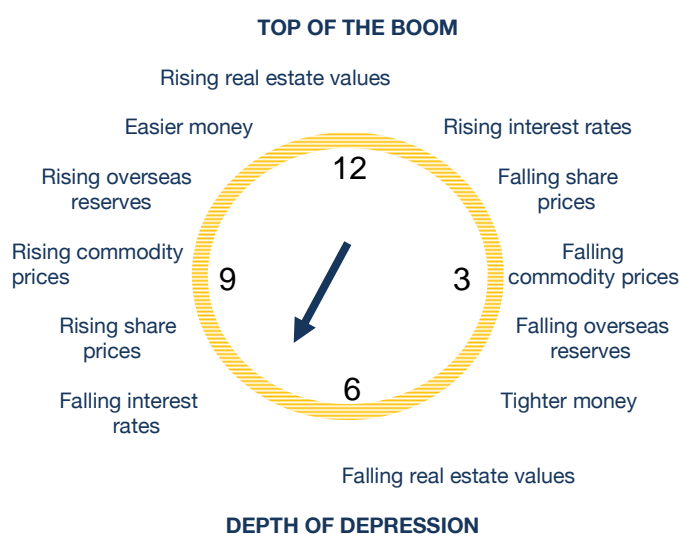
Many are anticipating a shallow economic turnaround taking place in 2010 and it is this optimism that has been fuelling the sharemarket (always forward looking) over recent months, not the current state of the economy.

Unfortunately it is this 'disconnect' (between what is occurring right now vs what may unfold in the future) that can easily throw off investors, leading to poorly timed and emotionally charged investment decisions.

Where are we now in the investment cycle?

Most experts believe the 'investment clock' is between 7 (falling interest rates) and 8 (rising share prices). Where they differ is the amount of time it will take to move between the two.

The investment clock...



Protecting and growing your wealth in 09/10.

Unless you are prepared to use a capital protected product or stay invested for the long-term, we believe clients need to be more proactive than usual during this volatile period, with our help of course.

In practice, this may mean more communication, more frequent reviews, reducing fees (if viable) and not being afraid to make changes to your investments, when necessary. Contrary to popular belief, it is possible, with a little more vigilance, to make profitable shorter-term adjustments to your investment, superannuation or pension portfolio and remain faithful to your long-term strategy. We call it '**short term strategy – long-term vision**', but getting the right advice is even more critical.

Rick Maggi

Axa 'North' - Capital Protection

We've had a huge response from clients and accountants to the article in our April newsletter entitled **'Bullet Proof Your Investments'**. You may recall, this was about the 'capital protected' product – called **'North'**, recently introduced to the Australian market by Axa (ex National Mutual).

Of course, it isn't surprising that this product (and hopefully more like it) is resonating with the Australian public, as the events of 2008 have left many worried about their superannuation or pension balances and sceptical about the benefits of investing.

As the product is unique, it can take some effort to get your head around. So for those interested in knowing more, we have attached a copy of April's newsletter and an Axa Fact Sheet. To view the current Axa North TV commercial go to www.axaguarantee.com.au.

I guess I should warn you, if I turn out to be particularly clear, you've probably misunderstood what I've said.

Alan Greenspan (ex-Chairman of the US Federal Reserve)

China back on track

Several indicators are pointing to a recovery underway in China after its economy slowed sharply late last year – highlighted by a slump in GDP growth from a peak of nearly 13% in 2007 to just 6.1% in the March 2009 quarter.

There has been much talk of 'green shoots' of recovery globally but these signs have been much stronger and more broad-based in China. Talk of a hard landing is now giving way to confidence that GDP growth this year will be around 8% - most developed nations would kill for a GDP figure like this.

But talk of recovery in China has been met with disbelief and suspicion by many – with Chinese growth being so dependent on the US consumer market the assumption is that a weak US consumer must severely limit China's prospects as well. This is not necessarily correct.

During the December quarter last year Chinese policymakers, as here in Australia, introduced a stimulus package designed to boost their economy, focused on infrastructure spending. In addition, monetary conditions were eased, various support plans were released, the gradual appreciation of their currency (the renminbi) came to an end, and policies to promote consumption were stepped up.

Since the stimulus package was released....

- Money supply and loan growth has surged.
- Fixed asset investment has picked-up by 30%.
- Industrial production is growing again.
- Real retail sales growth has remained strong.
- Surveys of business conditions in manufacturing and services sectors have improved for 5 months in a row.
- Property sales are rising.
- The downswing in Chinese exports appears to be diminishing, reflecting the stabilisation in global conditions.

The above suggests that a recovery is in progress and growth is back on track. But is it real?

There will no doubt be setbacks along the way, but there are good reasons to believe the rebound now being seen in China is sustainable. First of all, consumer spending in China has a huge potential for strong growth. Unlike in countries such as the US and Australia, where consumption accounts for around 60-70% of GDP, in China it has fallen to less than 50%. So there is significant potential to push it back up. Also...

- Despite common perceptions, Chinese consumption has actually been growing very strongly.

- The Chinese Government has shifted to promoting more balanced growth with much greater emphasis on consumer spending.
- Chinese per capita consumption of consumer items is a fraction of that in advanced economies, suggesting there is significant pent-up demand.
- Household saving is very high and household debt is miniscule.

Chinese consumers will probably not save the world. However, it does indicate there is significant scope for strong growth in consumer spending. So while most developed countries are constrained by high debt levels, China's downturn has been mainly cyclical and structural forces remain tailwinds for growth.

A rebound in Chinese economic growth is good for Australian shares. China is now Australia's second-largest export market so **any recovery in Chinese economic growth is also good news for us.**

Premium China Fund (Review)

While there is plenty of interest in China, there are very few fund managers focusing exclusively on China (most are typically 'Asian' funds). Even fewer fund managers work locally (in China) doing face-to-face meetings, performing on-site checking of factories, products, people and production lines, as well as analysing cash flows and talking with customers, competitors and suppliers.

The Premium China Fund or more accurately, Value Partners, is a Hong Kong based fund manager employed by the Premium China Fund. They offer Australian investors a direct link to the region and are one of a rare breed of proactive managers willing to go the extra mile.

Value Partner's objective is straight forward and easy to understand – to find companies on a case-by-case basis that are selling below their underlying values, don't overpay (to protect the downside risk) and take a 3-5 year view. If necessary, Value will also work alongside

management to enhance corporate governance and shareholder value.

Their investment team structure is massively experienced, with a long track record and has won numerous funds management awards. From a performance perspective, Value Partners has achieved high long-term returns (15.9% compounded over 16 years versus the Hang Seng Index at 6.2%) with less volatility, thanks to their disciplined and patient 'buy and hold' investment approach.

Even Sir John Templeton, founder of Franklin Templeton Investments, personally invested US\$100 million of his own money with Value Partners several years ago (instead of using a Templeton China fund).

There is a growing consensus that, going forward, most Australians should be looking to have at least some exposure to China (perhaps 5%). Obviously you should seek expert advice on this before leaping-in - however the Premium China Fund would seem like a good start.

DETROITOSAURUS WRECK!

On June 1 General Motors filed for bankruptcy protection, the fourth largest bankruptcy in American history. Like Chrysler, GM is rapidly restructuring itself unloading Saab, Hummer, Opel and others, but early signs are encouraging. So who owns GM right now?

60.8% of common equity will be owned by the US Treasury.

17.5% by the Voluntary Employee Benefit Association (VEBA), the UAW health-care trust.

11.7% by the Canadian Government.

10% reserved for GM for unsecured bondholders and other unsecured creditors.

Number of years GM was the world's largest automaker – **77**

Debts listed by GM in its bankruptcy filing - **\$172.8 billion** (the second highest amount ever, eclipsed only by Lehman Brothers)

Minimum pension payment relief

In the 2009 Federal Budget, the Government extended its 50 percent reduction to minimum pension payment requirements for the 2009/10 financial year. This means the minimum pension payment amount pension clients are required to receive in the 2009/10 financial year has been halved.

We suggest pension clients contact us to determine if they should adjust their payments. The 50 percent reduction will not automatically apply to the calculation of the minimum pension payment requirements for the 2009/10 financial year. Therefore, to reduce pension payments, pension clients will need to submit pension payment alteration instructions, even if they've done so in the past.

In the news today...

States borrow \$230bn for major projects.

The states are set to borrow more than \$230 billion to fund massive infrastructure programs designed to stimulate their faltering economies and to offset a large decline in their revenues.

Colliers buys up Werrett, tops WA shopping league.

Colliers International is buying the WA-founded Werrett Property Group in a move that will see it vault Westfield, Centro Properties and Hawaiian to become WA's biggest shopping centre manager.

Fortescue studies second port.

Fortescue Metals and Aquila Resources will study development of a second iron ore port in Western Australia's Pilbara region as Fortescue continues its quest to gain access to the private railways of Rio Tinto and BHP Billiton.

Timbercorp.

Thousands of investors in almond projects run by the collapsed managed investment scheme operator Timbercorp will be offered a deal to trade their assets for units in a listed trust, in a move the deal's proponents say will give creditors certainty.

US Federal Reserve/Interest rates.

The US Federal Reserve is expected to emphasise its commitment to near zero interest rates later tonight after the World Bank's forecast of a deeper global recession triggered a sell-off across world sharemarkets.

Woodside Petroleum.

Woodside Petroleum and its joint venture partners in the \$30 billion Browse natural gas development are under strong pressure from the West Australian government to set aside their differences and choose an earmarked site for the massive project in the Kimberley in the state's far north.

New Perth waterfront plans released.

The WA state government has today released concept plans for the development of Perth's waterfront as Premier Colin Barnett reiterates work on the scaled back plans is expected to start in 18 months.

Perth office rents predicted to fall 50% by 2013.

Office prices and rental rates in Perth's business district will fall as much as 50 percent by 2013 from last year's highs as mining projects stall and new blocks are completed, real-estate forecasters and agents said. Vacancies in the city centre have risen from a record low of 0.3 percent last June, among the tightest in the world, to about 6 percent and will jump to 16 percent by mid-2010, said Lee Walker, at Sydney-based forecaster BIS Shrapnel. The rate will peak in 2013, with average prime rents dropping to A\$360 (\$286) per square metre from A\$720 now, he said.

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