



Economic & Market Update

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Chief Investment Officer

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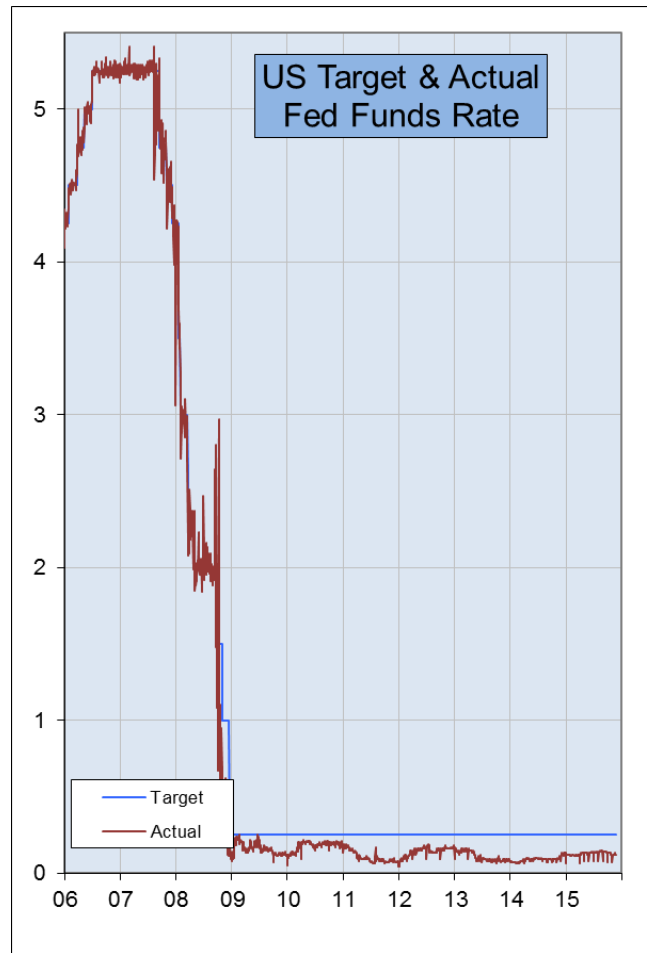
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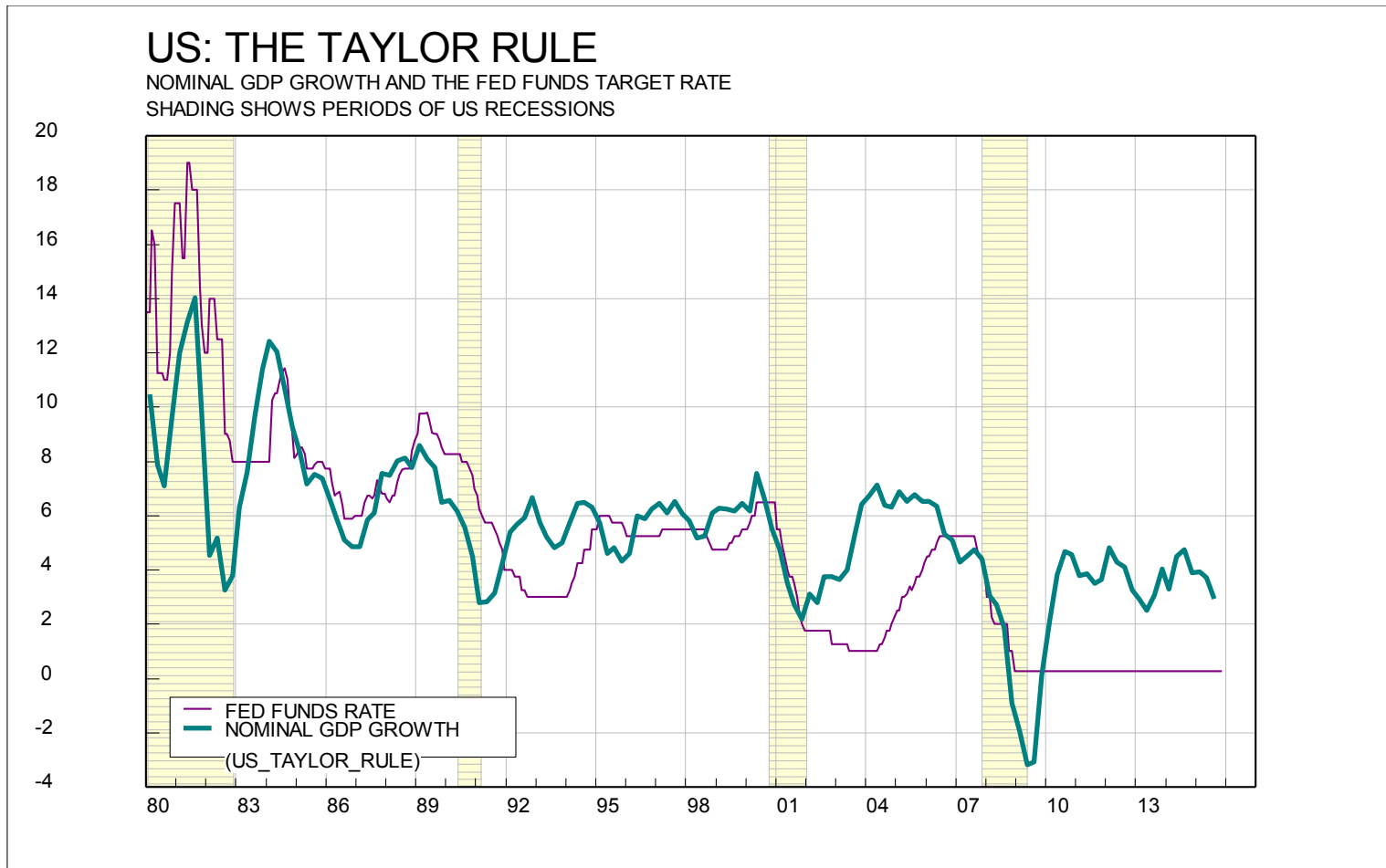
Key Issues

- Will Fed raise?
- Will that affect share markets?
- China still slow
- Paris Climate Conference
- Commods just keep on sliding
- AU economy—turning up?
- AU market

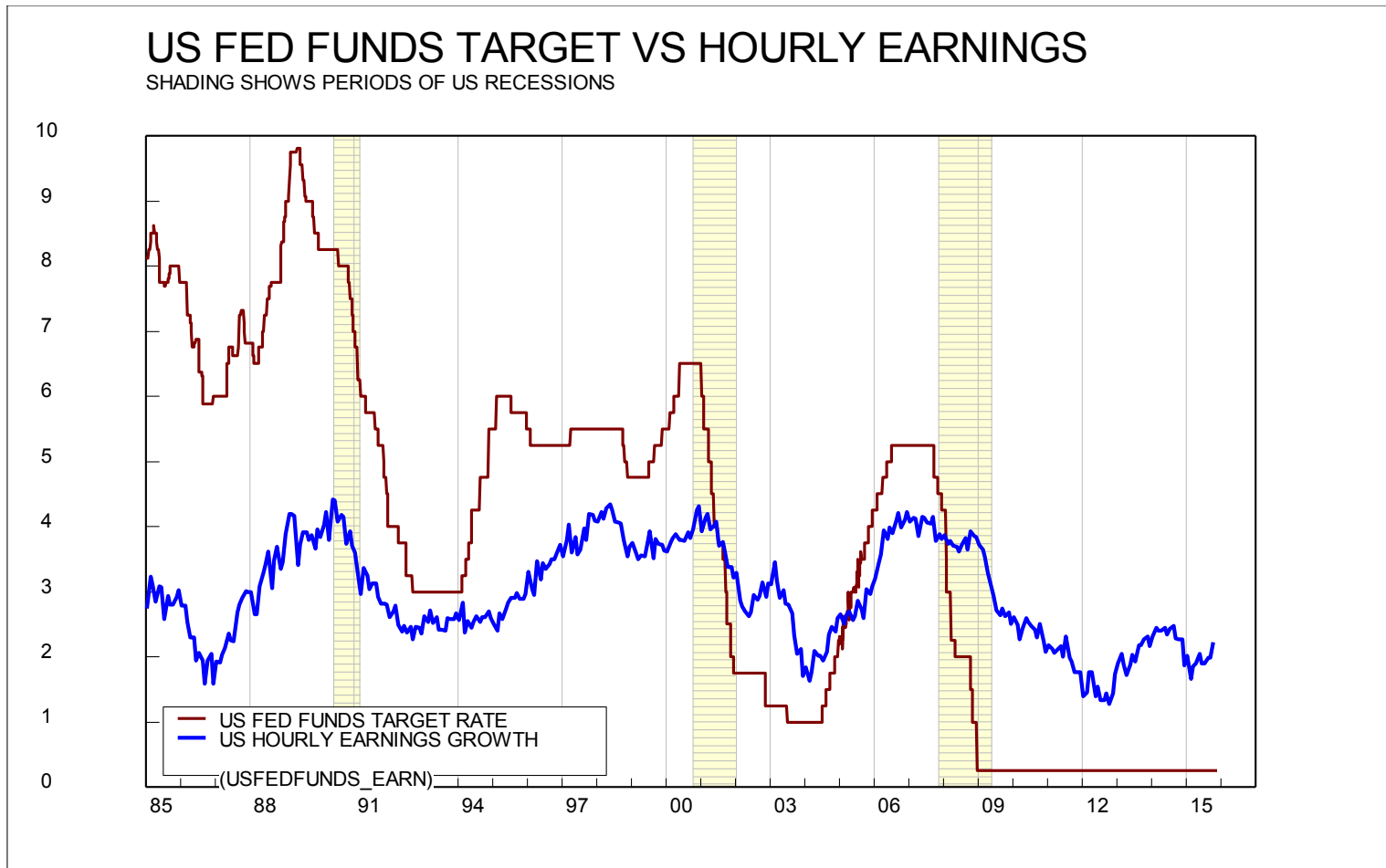
Fed Funds at emergency level



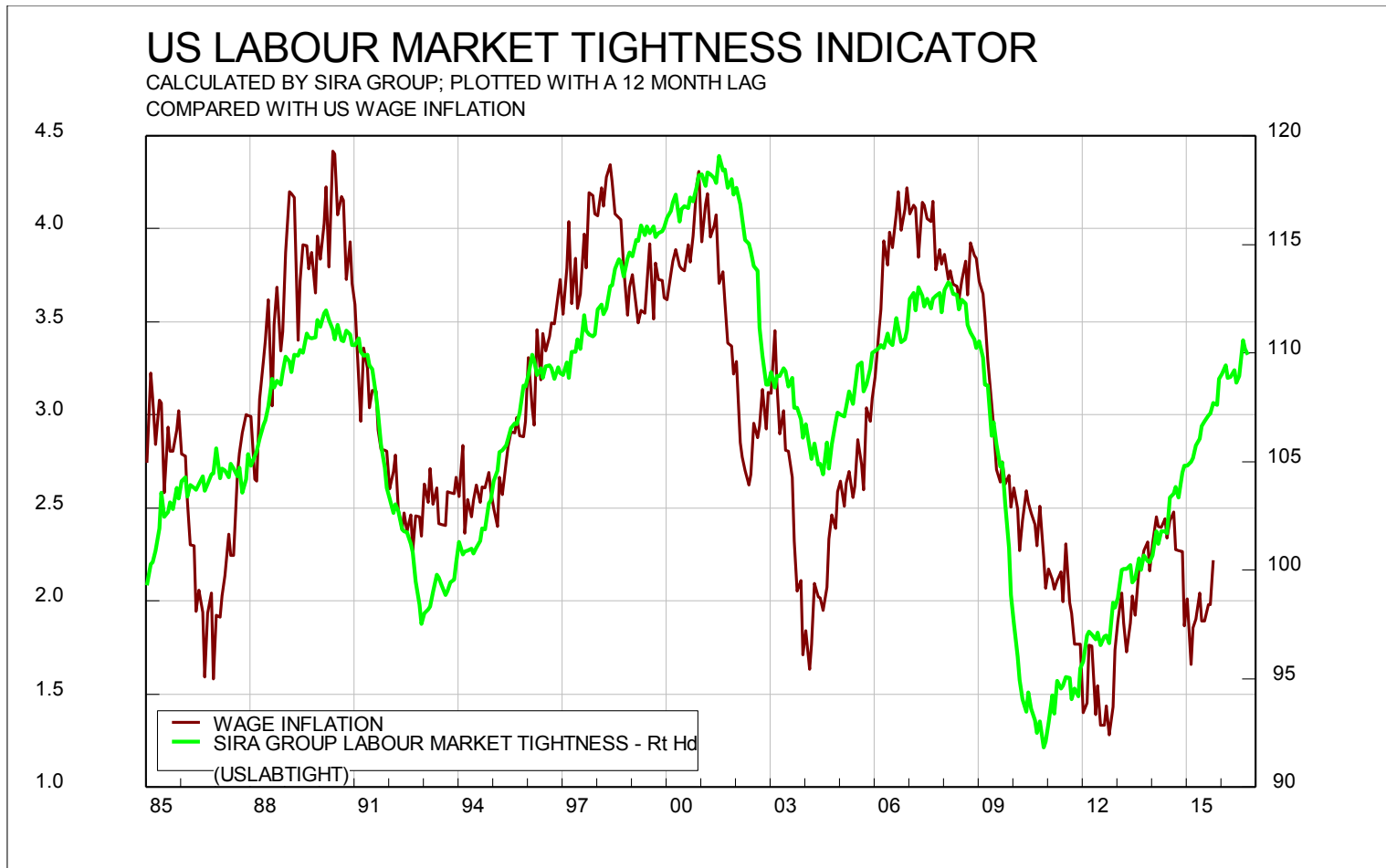
The Taylor Rule



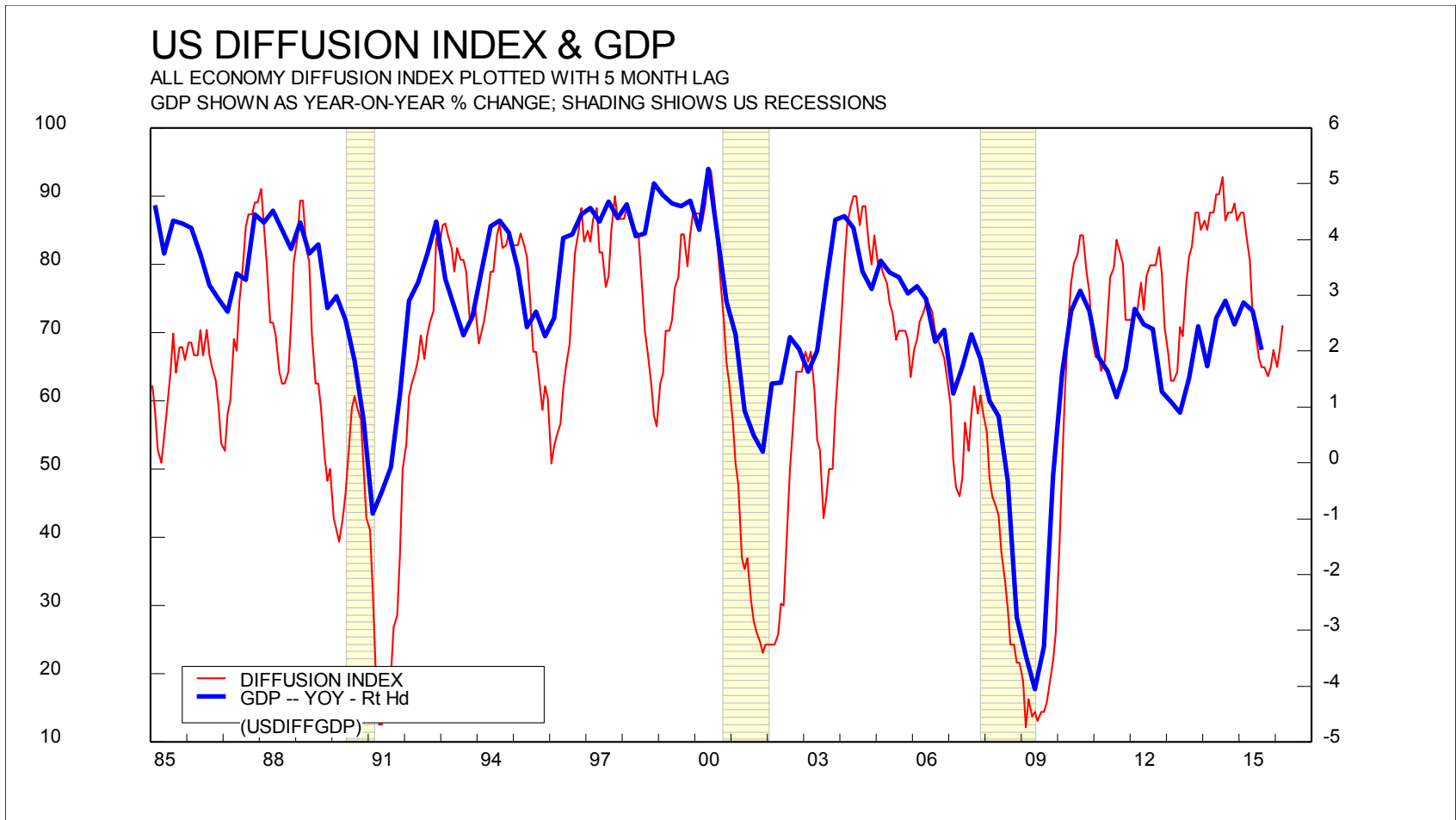
But Fed follows earnings



Labour market tightening



Recent weakness to reverse



Will rate rise affect market?

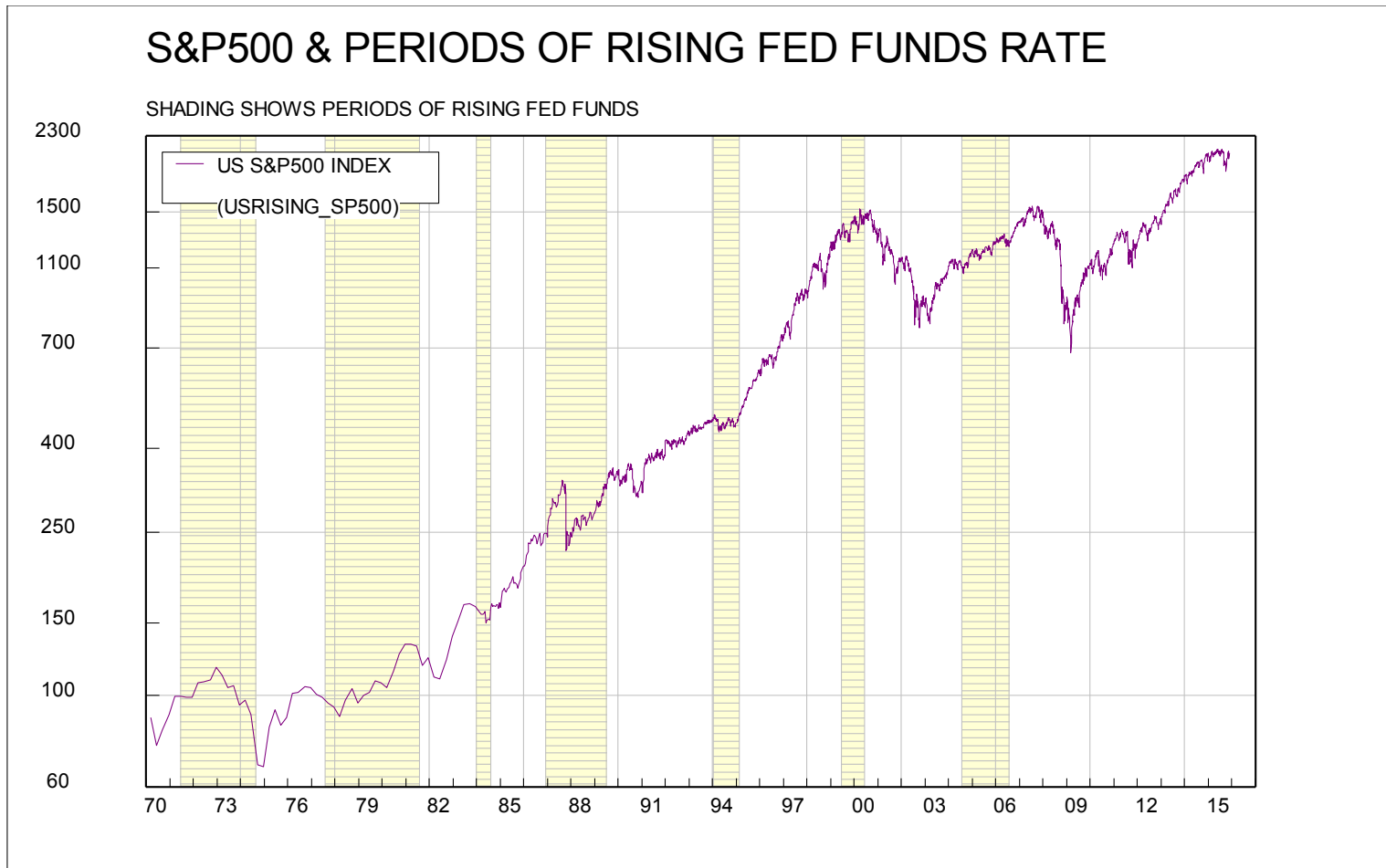
Price=EPS/discount rate

i.e.:

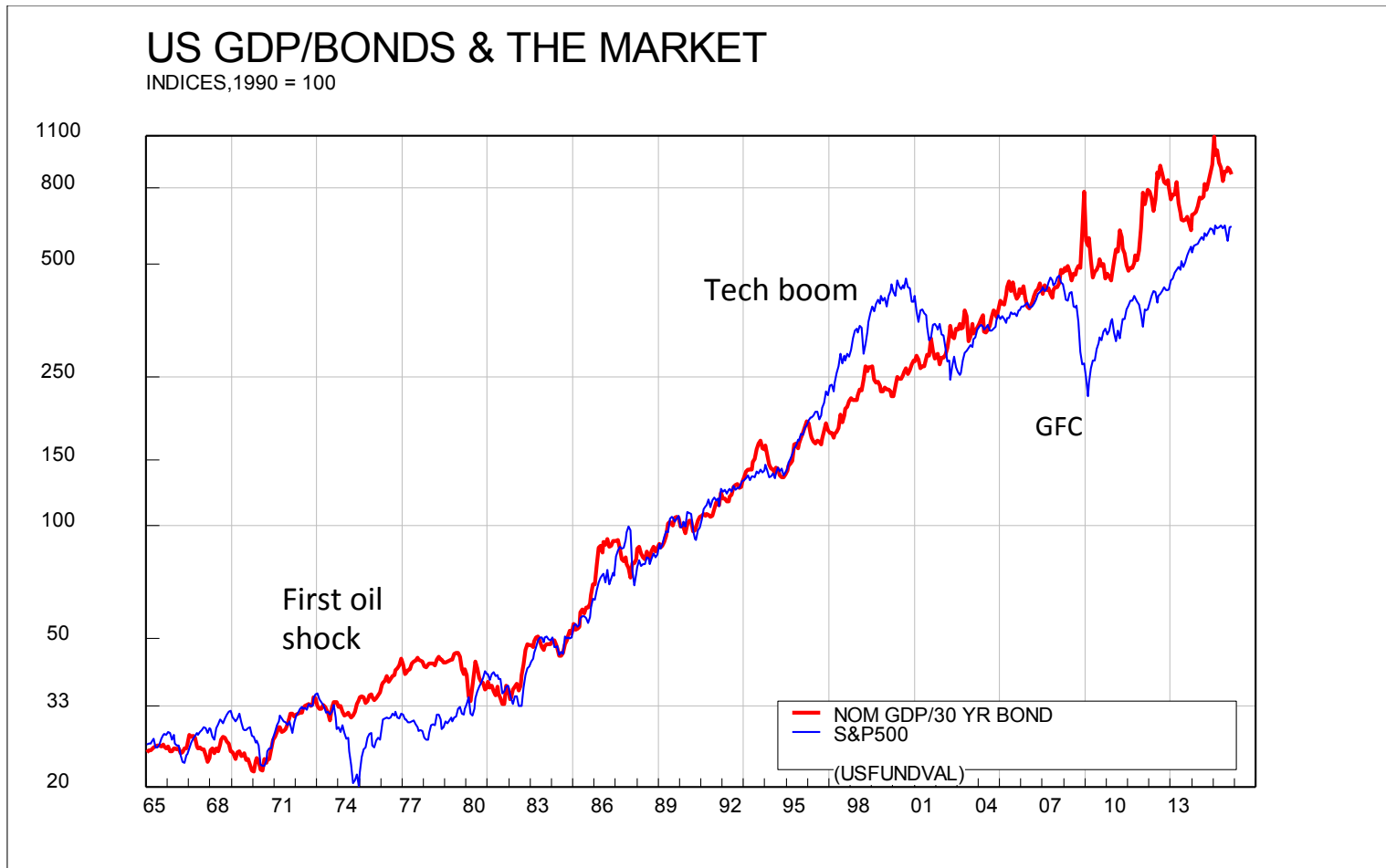
Price = EPS/EY or Price =EPS/Bond Yield
or EPS/cash rate

(Confidence reflected in EY/PER, mostly)

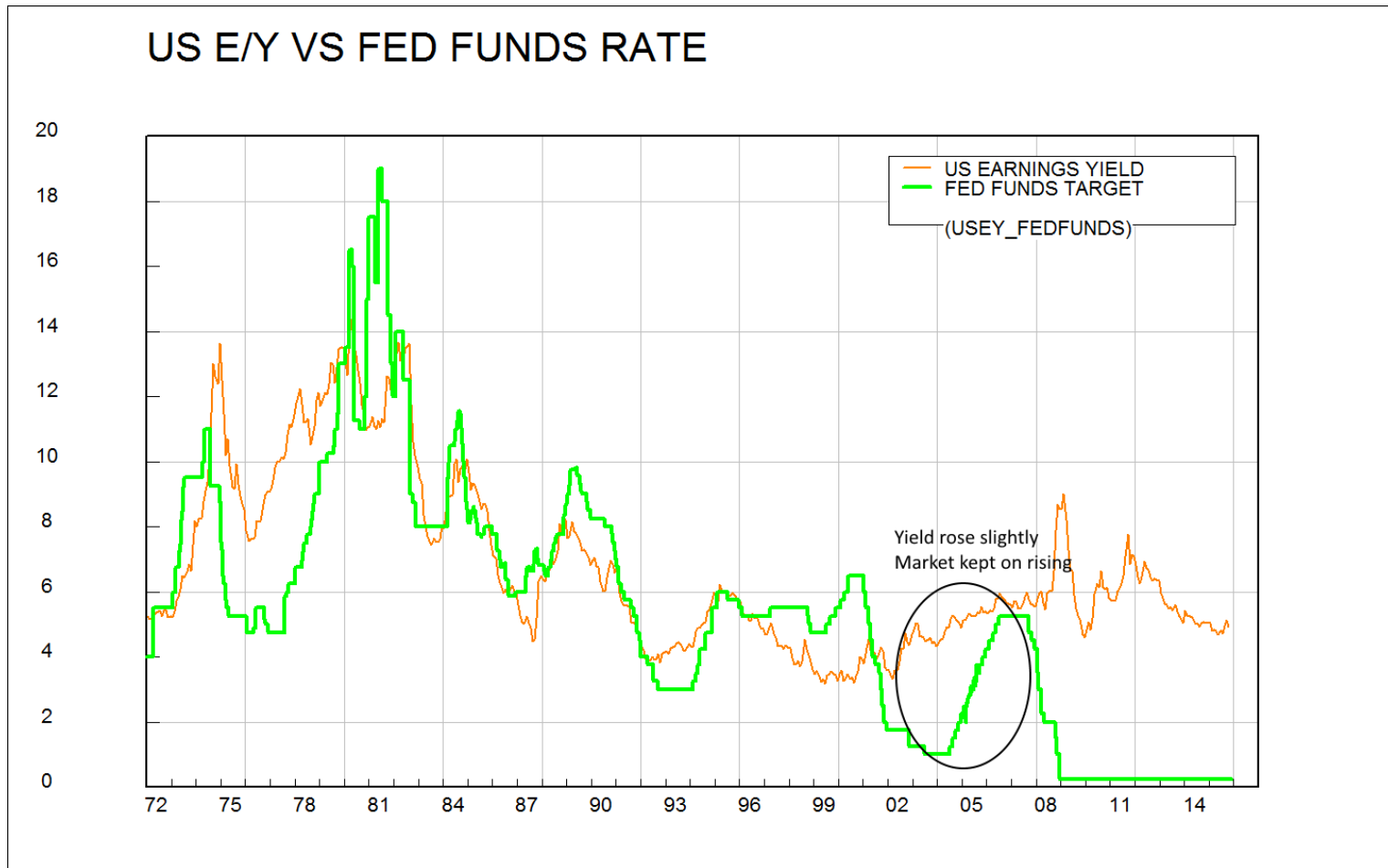
Relationship not obvious



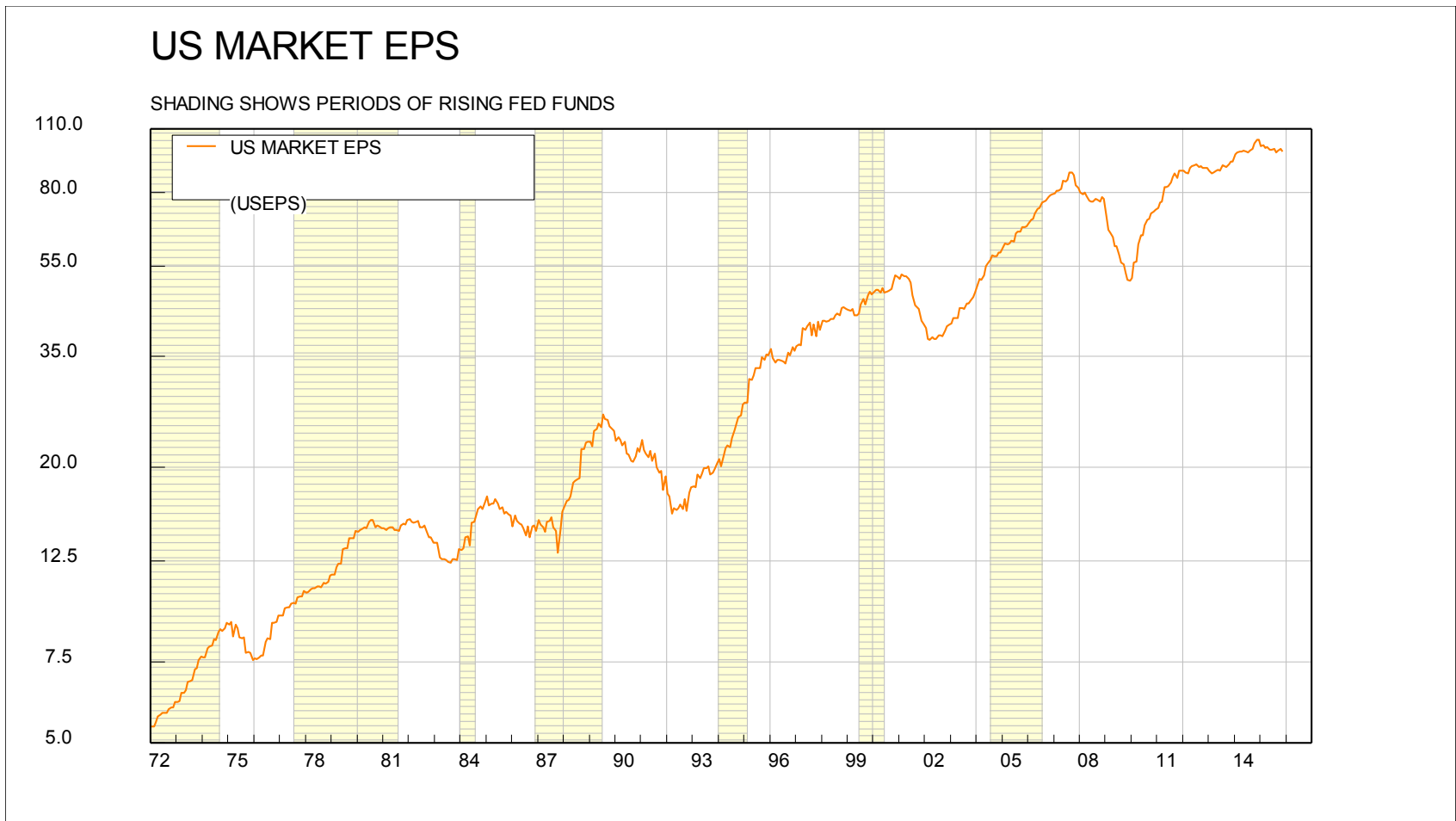
Market cheap rel to bonds



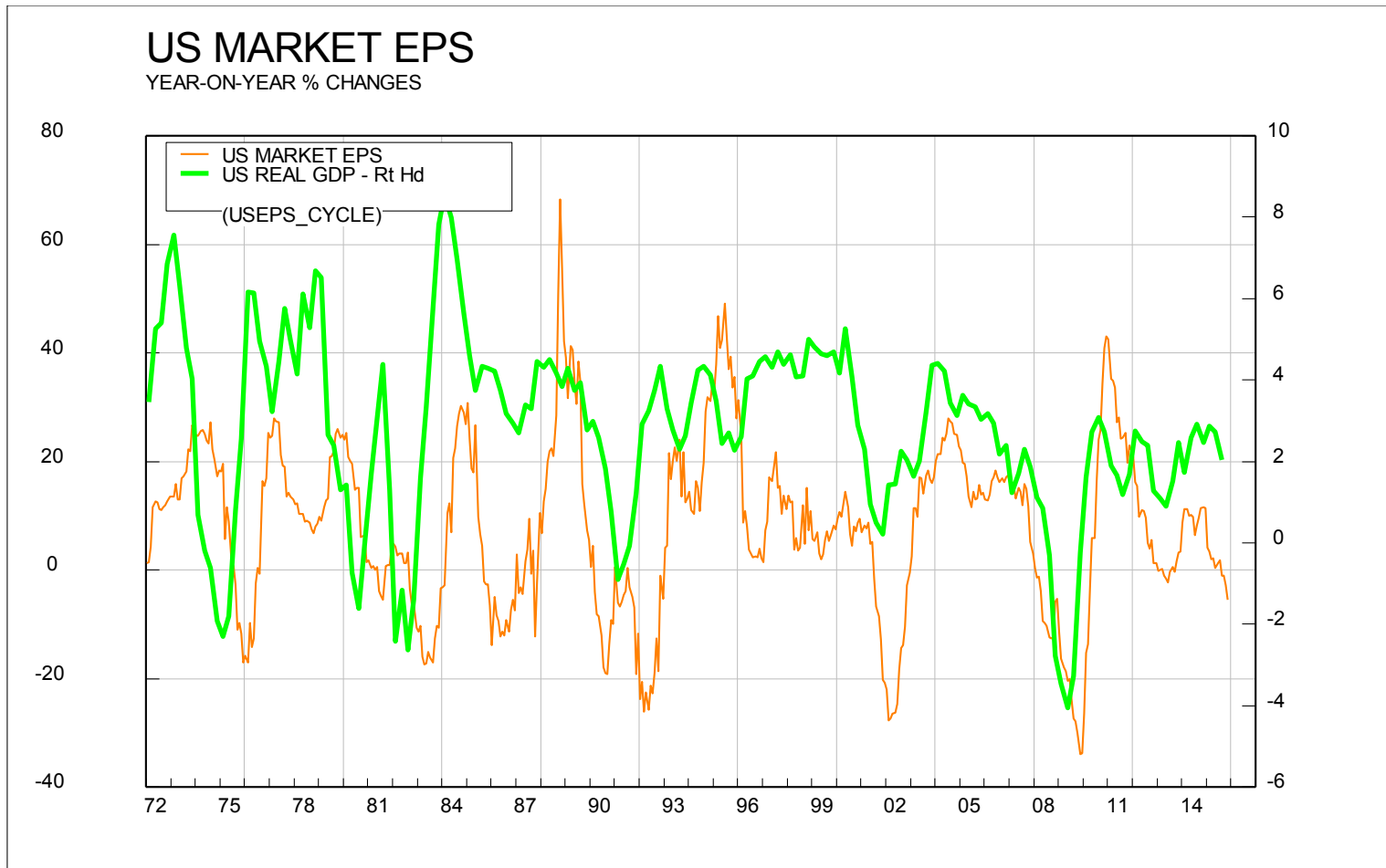
E/Y way above Fed Funds



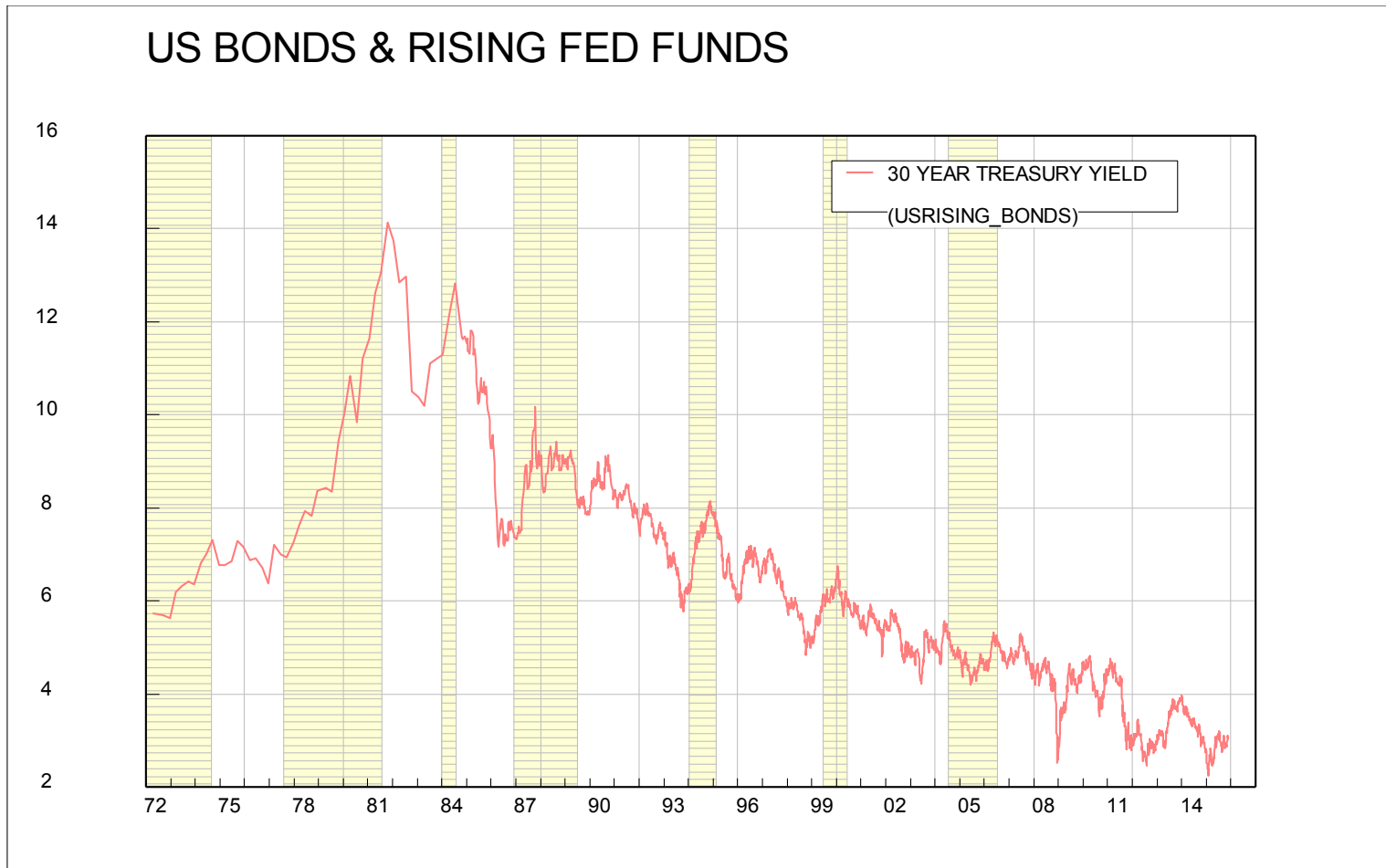
EPS uncorrelated with int rates



EPS mostly cyclical



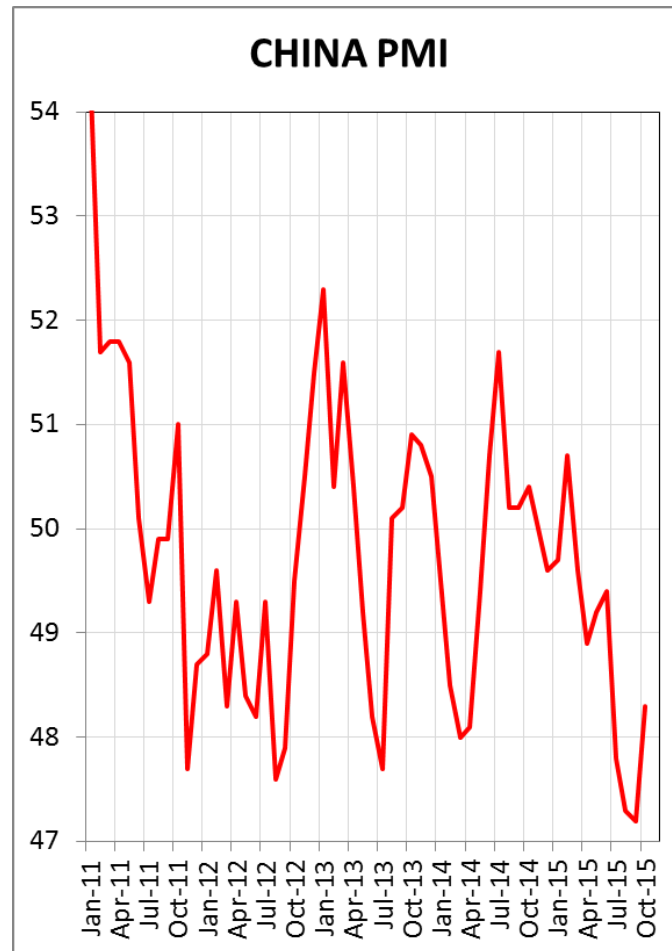
Bonds do respond to rate rises



US Share Mkt Conclusion

- Fed will start raising Fed Funds rate this December
- Rise will be slow and cautious
- This will have little impact on overall share market
- But will drive up bond yields
- Low likelihood of US recession
- Bull Market will continue, with blips

China still struggling



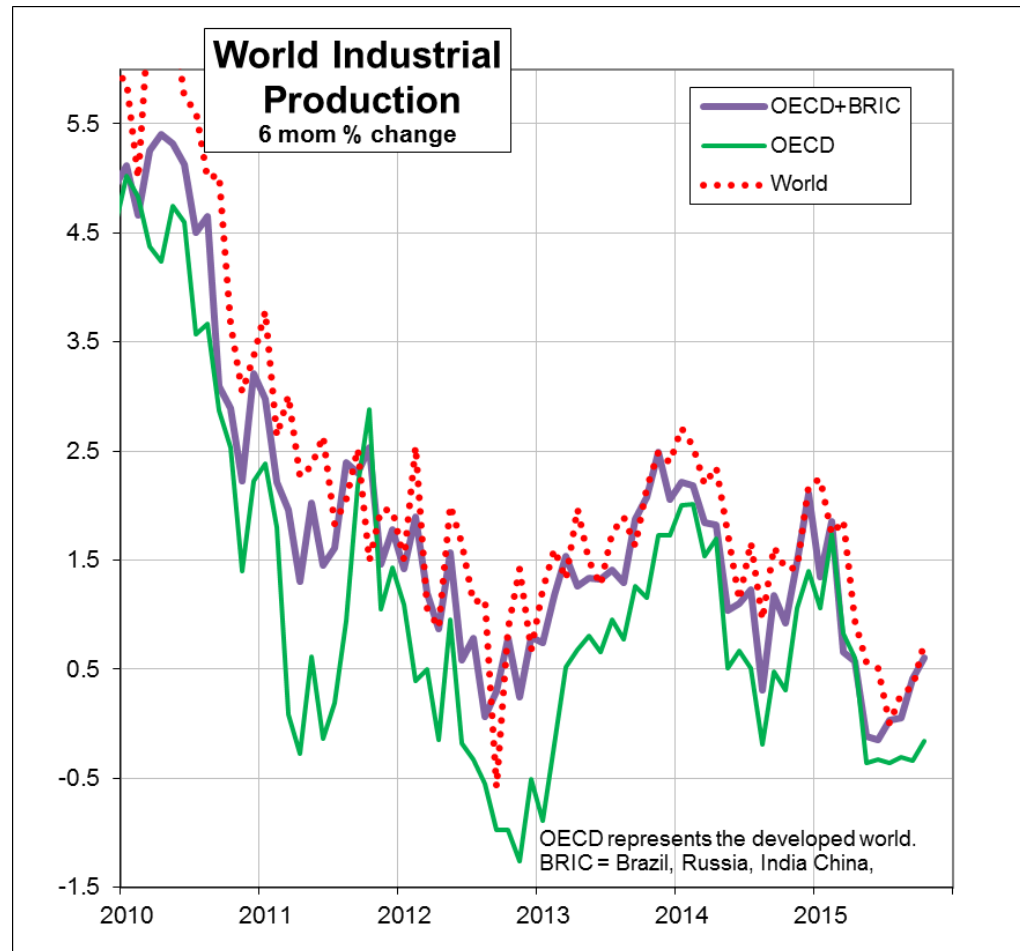
Shift to services

China's Industrial Recession

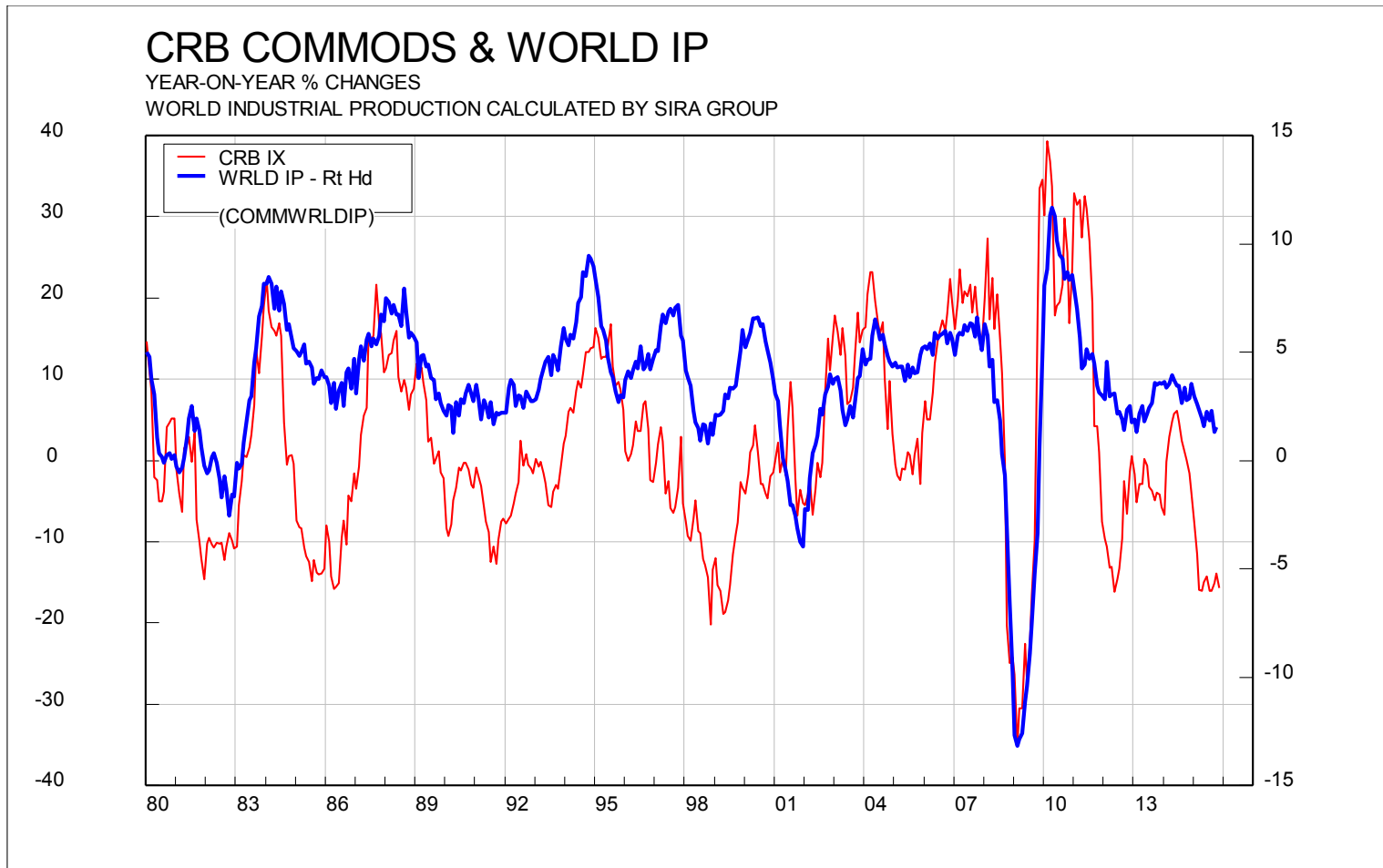


Source: OECD, NBER; Minack Advisors

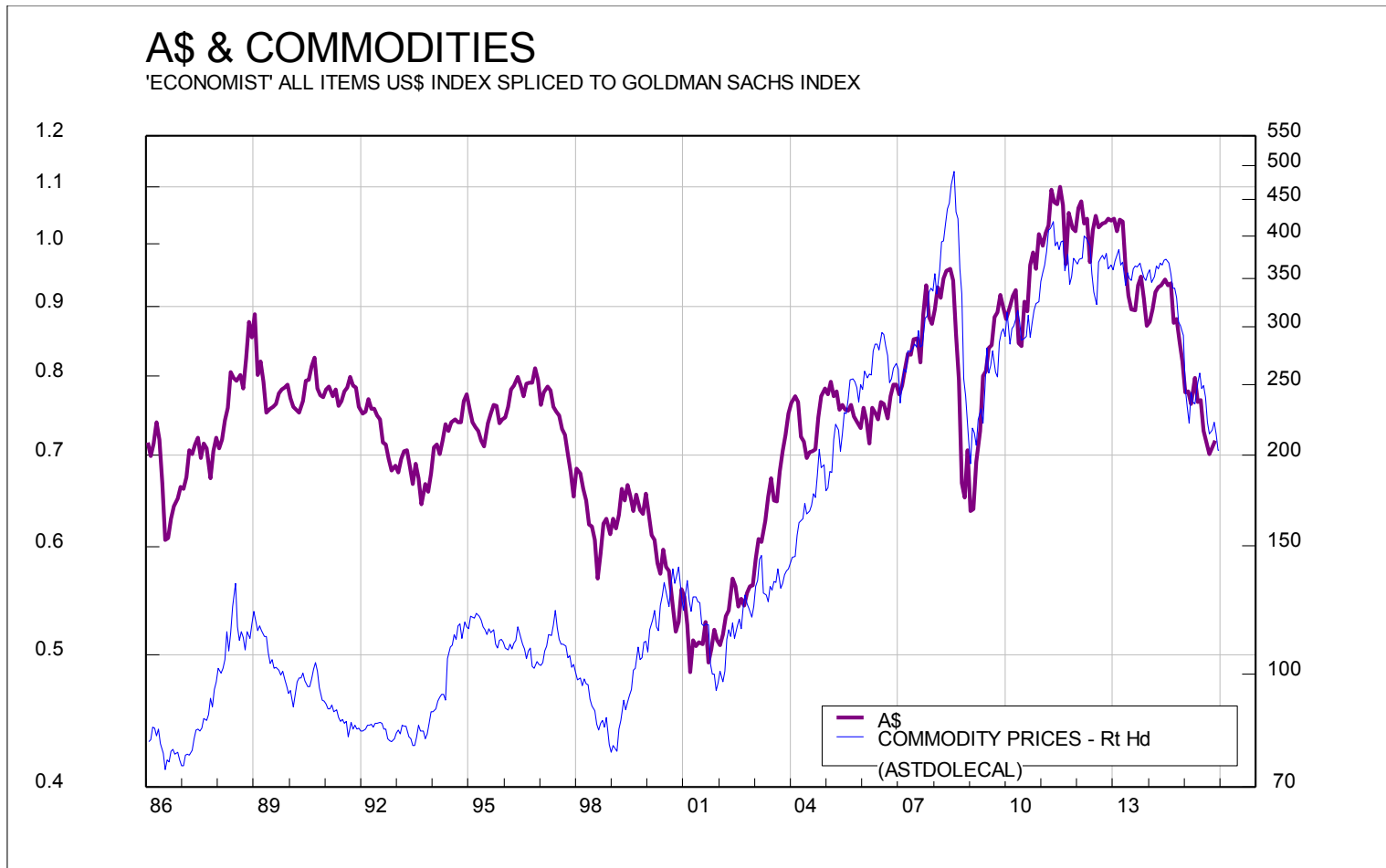
World growth picking up. A little.



Commodity prices still falling

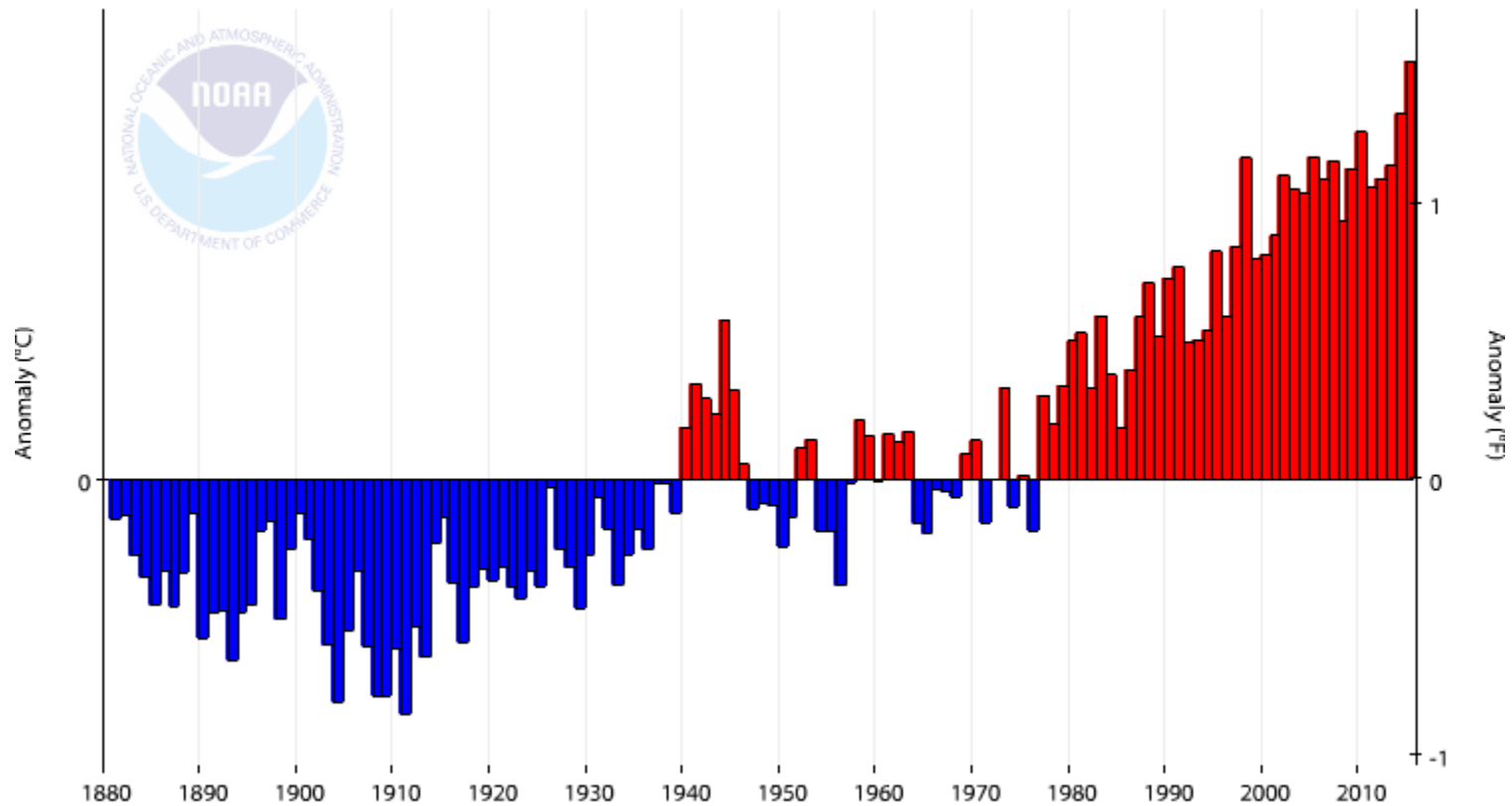


... which means A\$ will be weak too

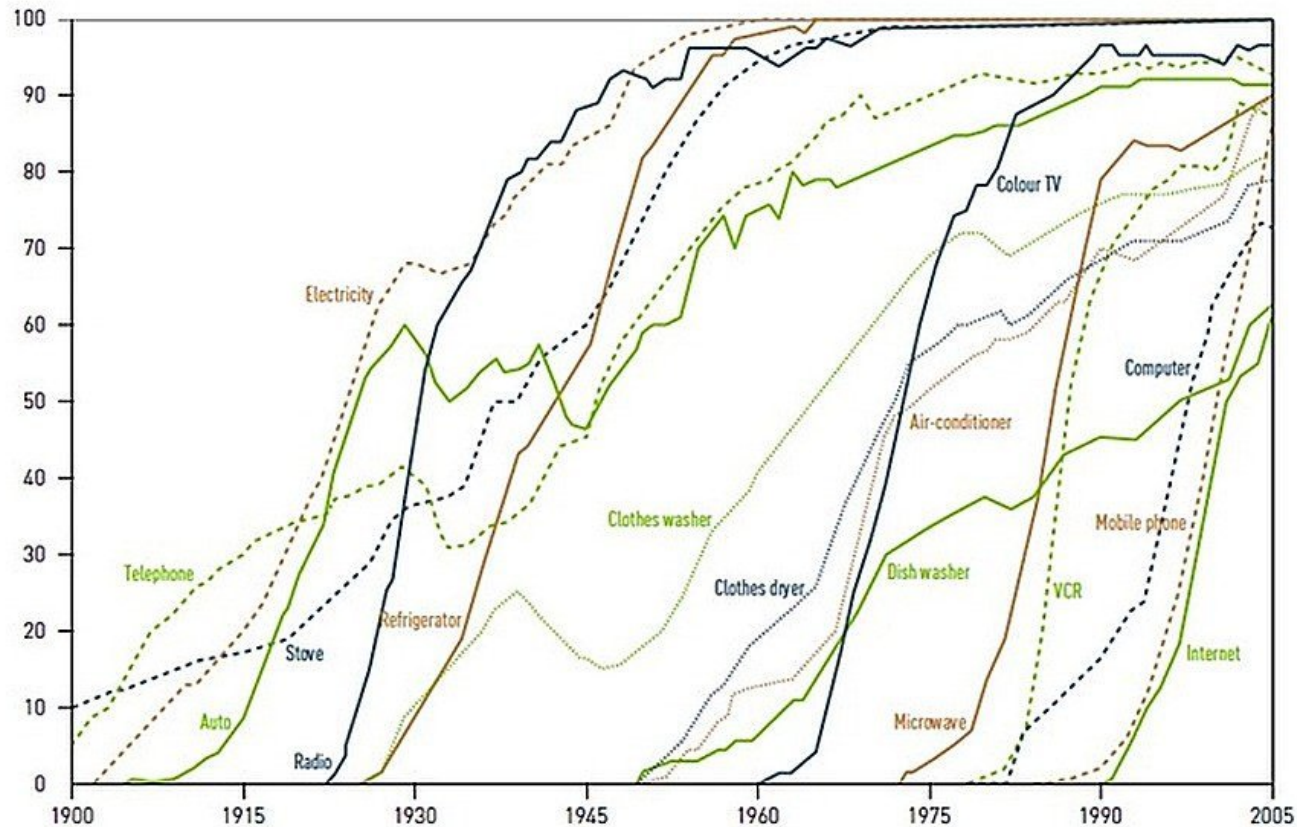


Paris Climate Conference

Global Land and Ocean Temperature Anomalies, November-October



Technology adoption curves



Technology adoption curves for a range of modern innovations. Victorian Government

The Learning curve

Exhibit I
Price of Model T, 1909-1923 (Average list price in 1958 dollars)

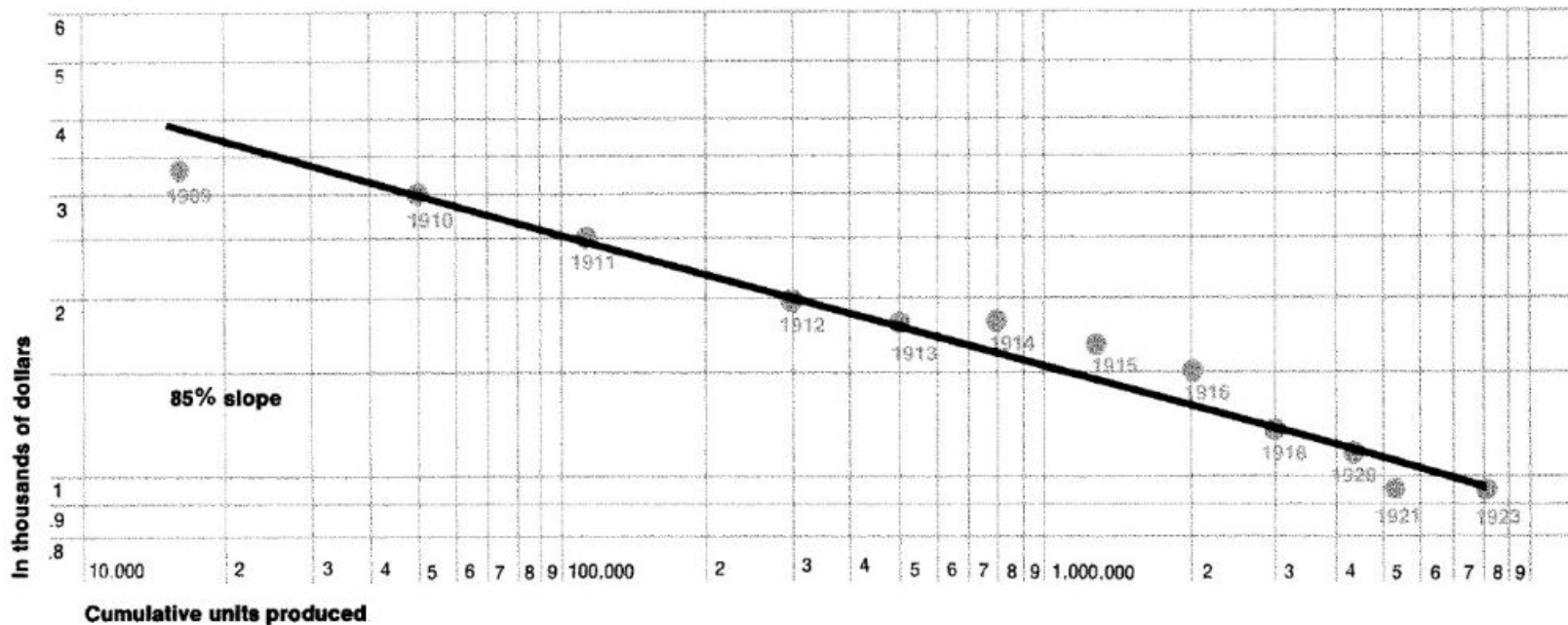
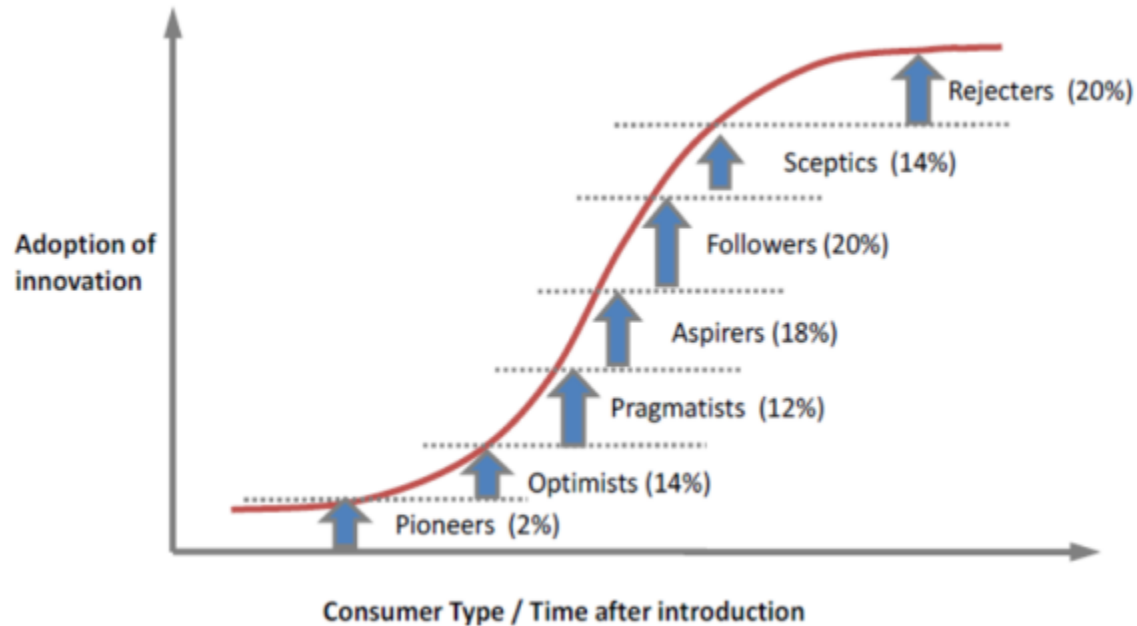
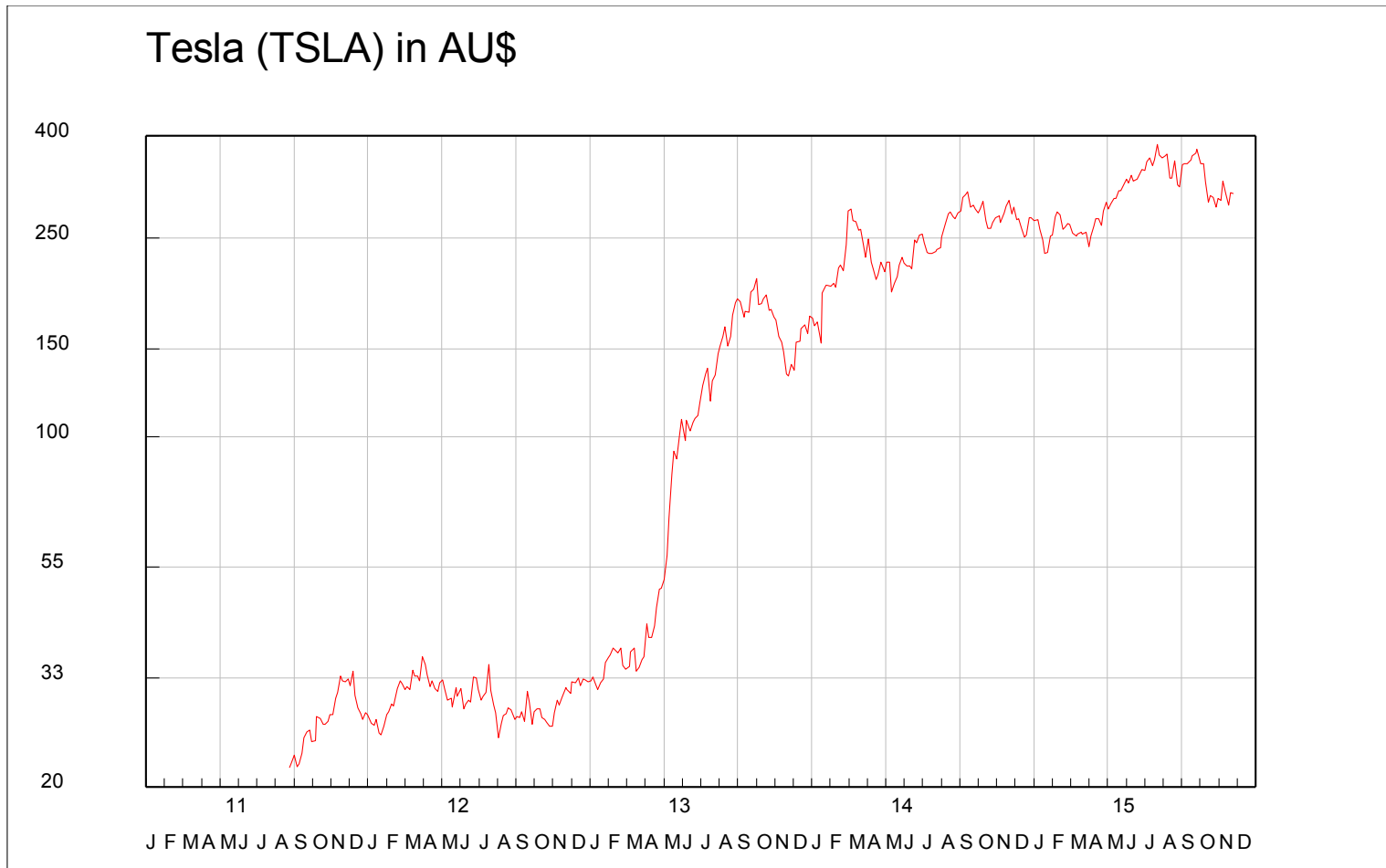


Figure 1. The price of the Ford Model T from 1909-1923[2].

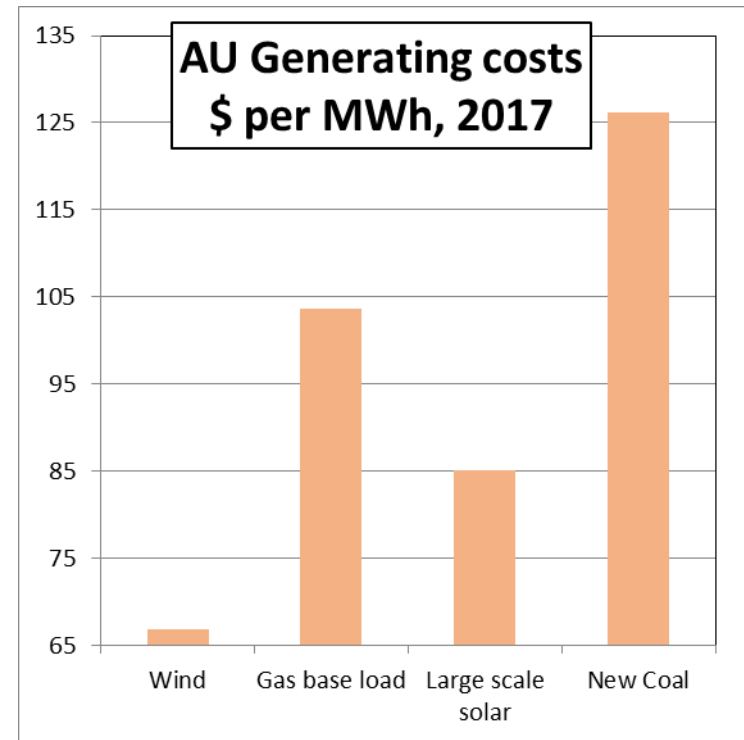
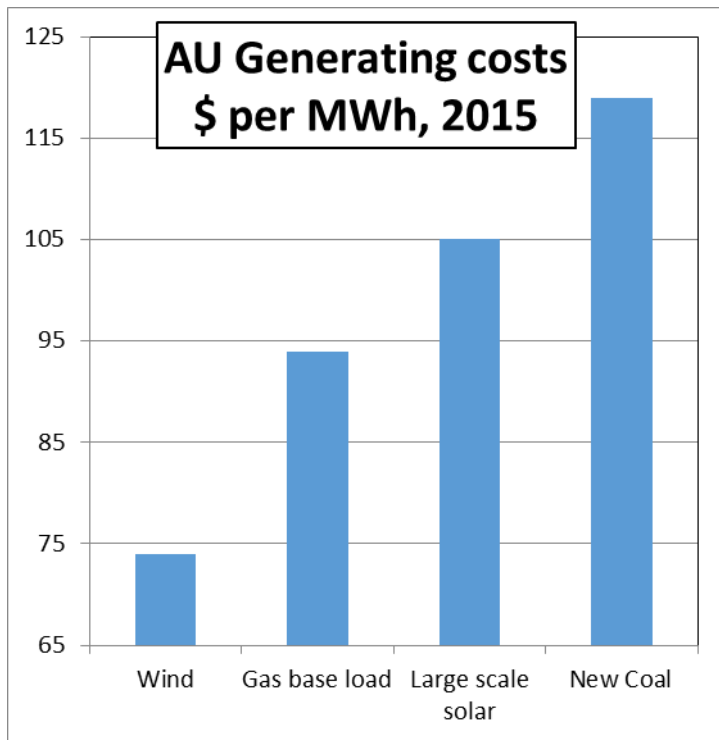
Innovation adoption



Tesla

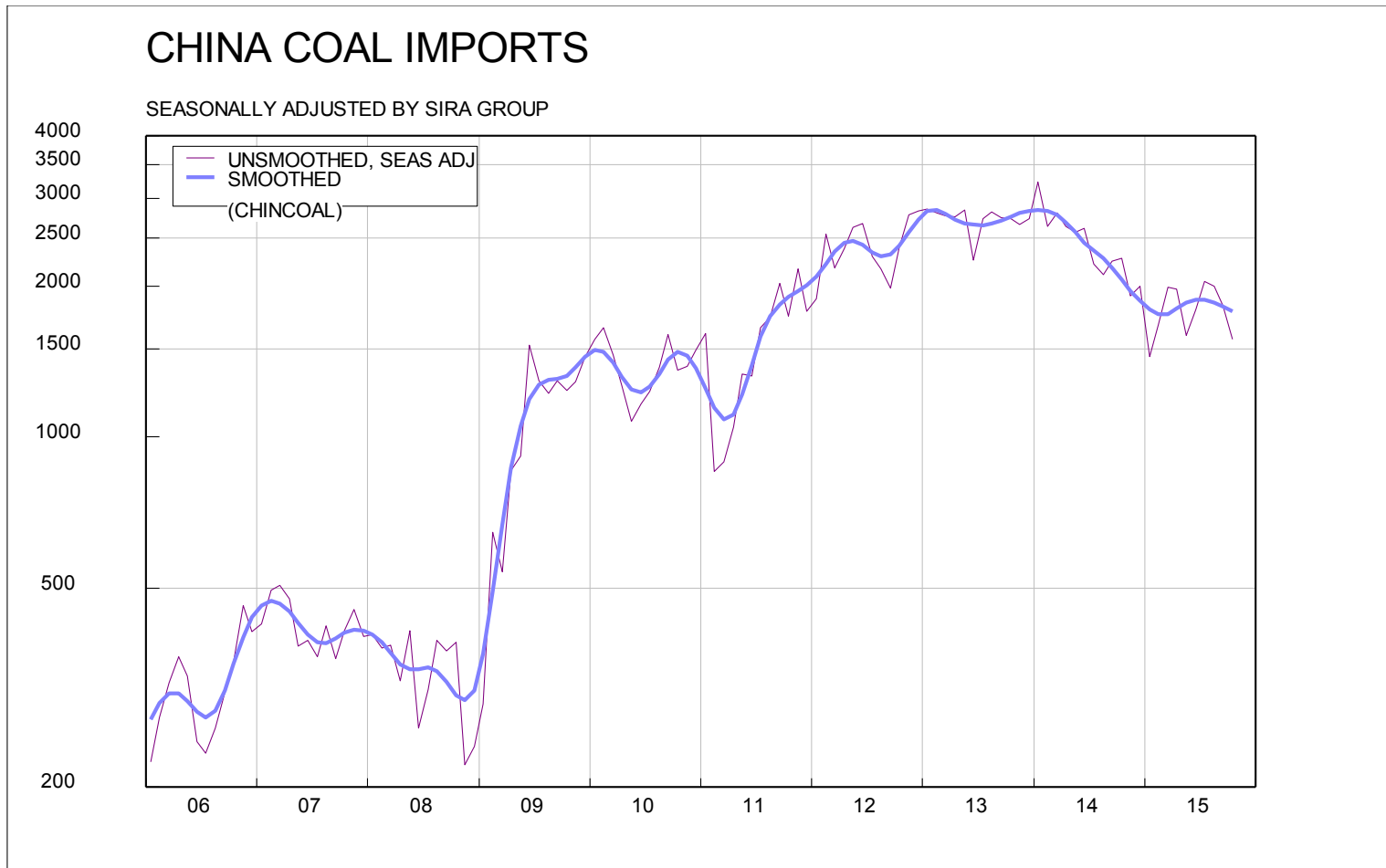


Coal just too expensive

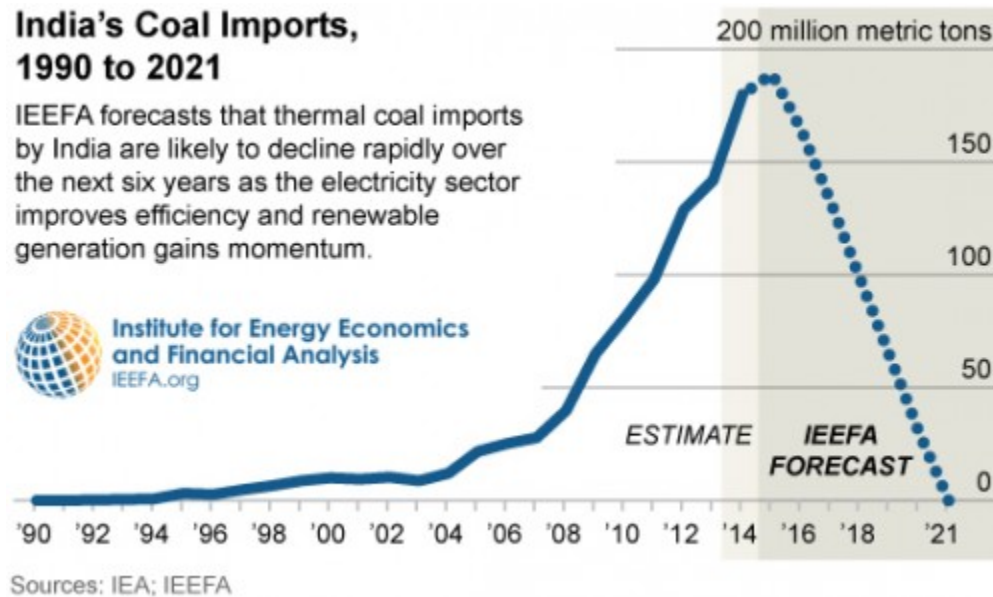


Since Copenhagen (2009) , wind down 60%, solar 80%

China coal imports down



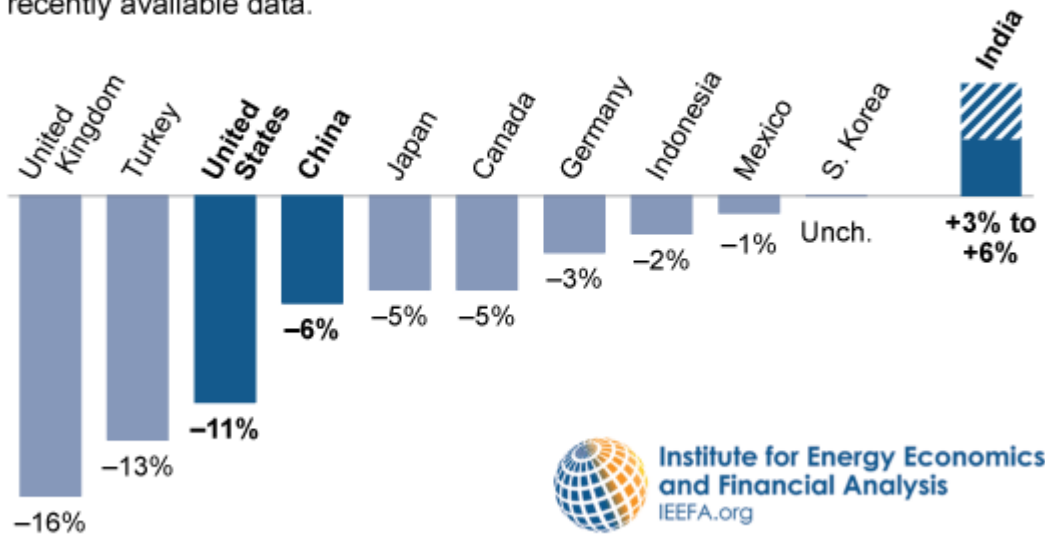
India won't save us



Peak coal

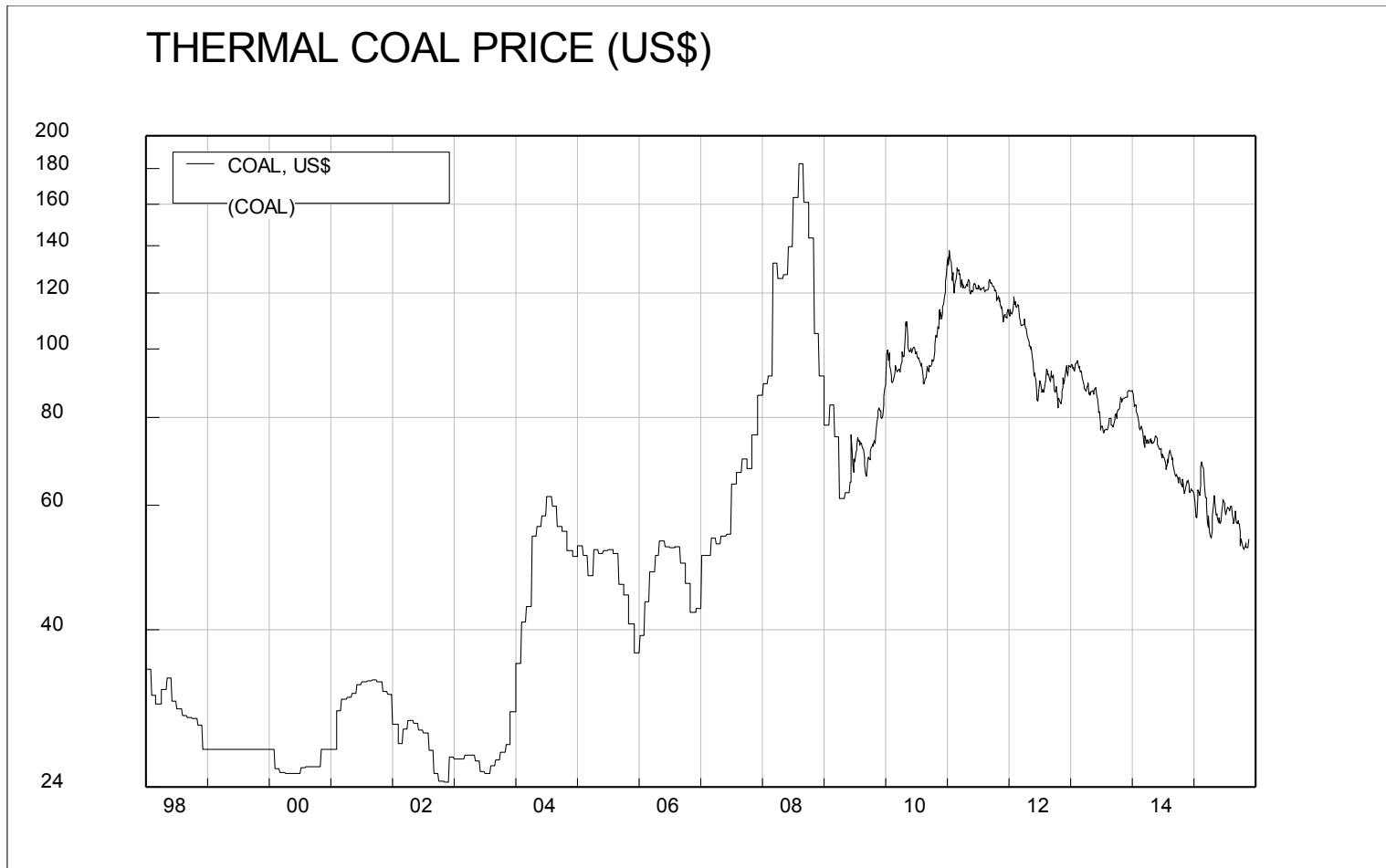
Change in Coal Consumption So Far This Year

IEEFA forecasts an overall 2% to 4% decline in global consumption in 2015. Here are the changes in key countries, based on the most recently available data.

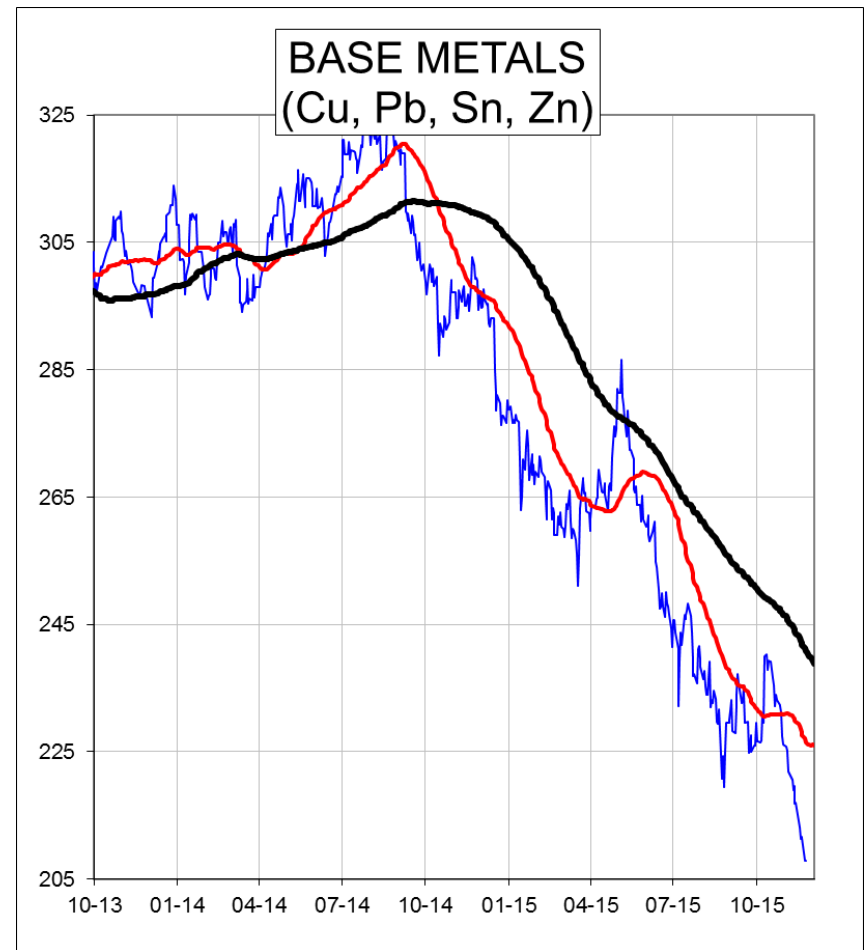
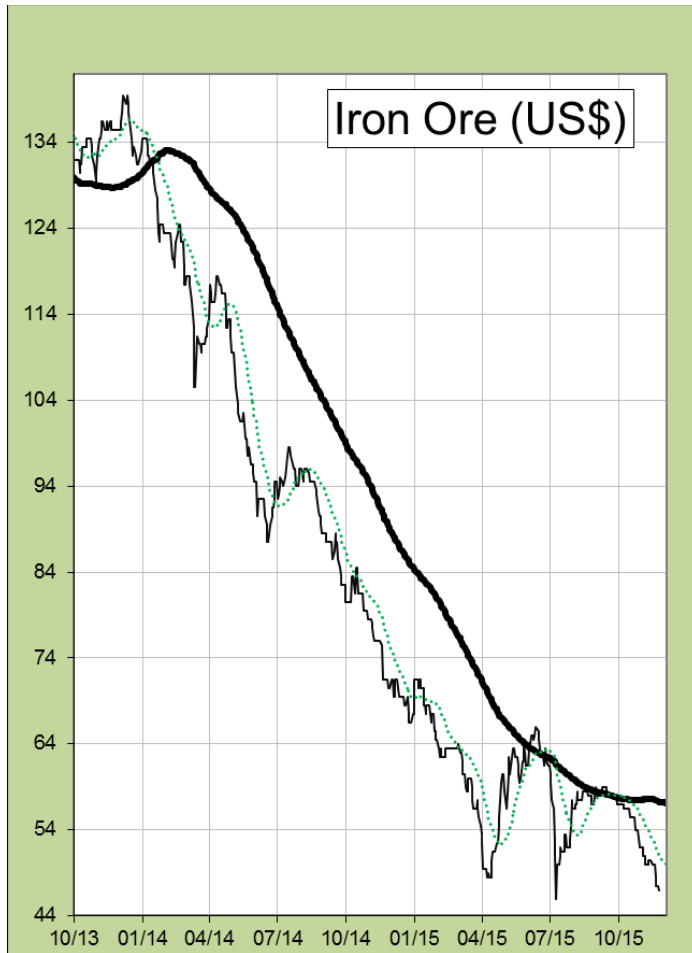


Sources: Government figures from individual countries; International Energy Agency

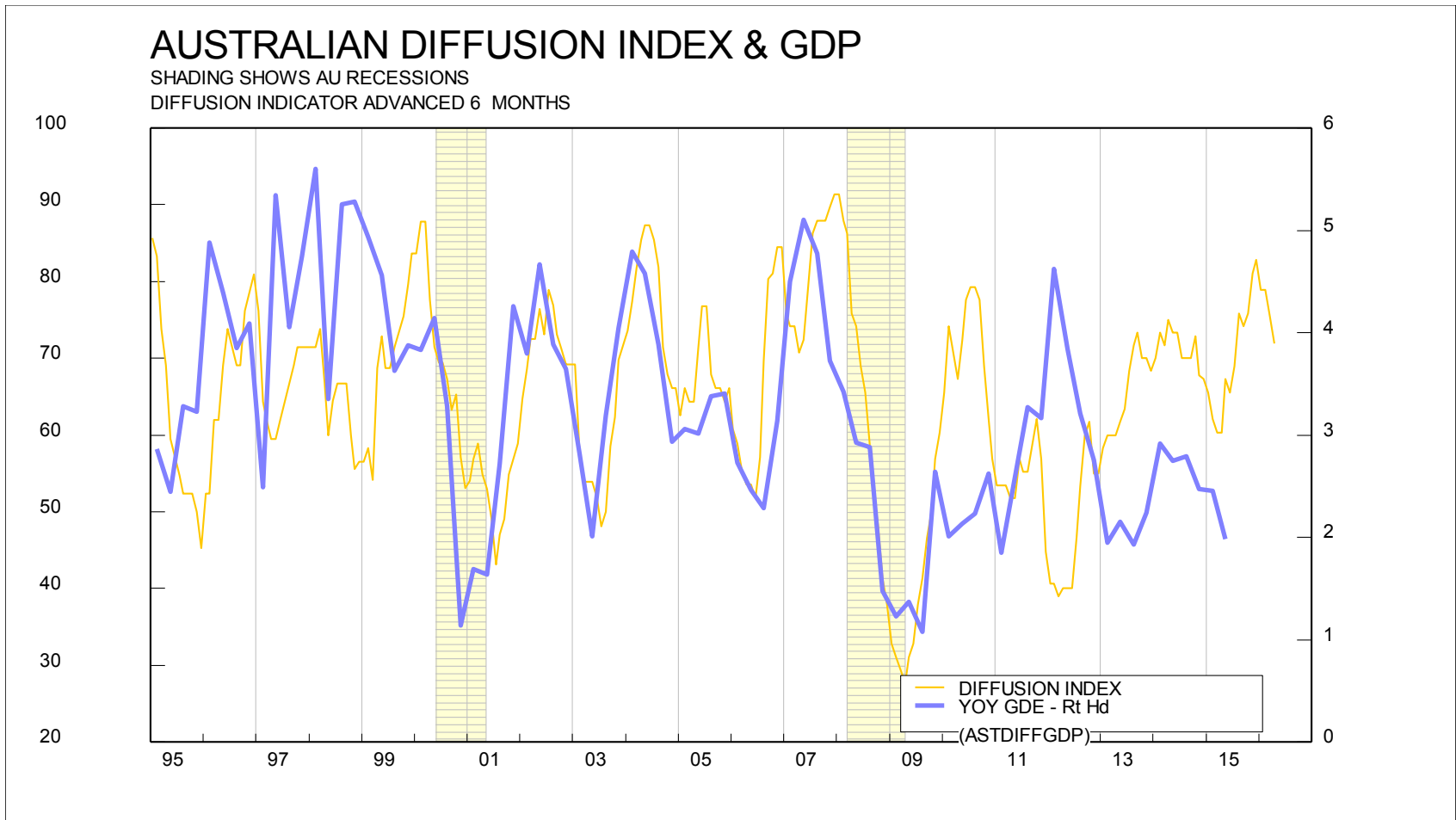
Thermal coal price plunge



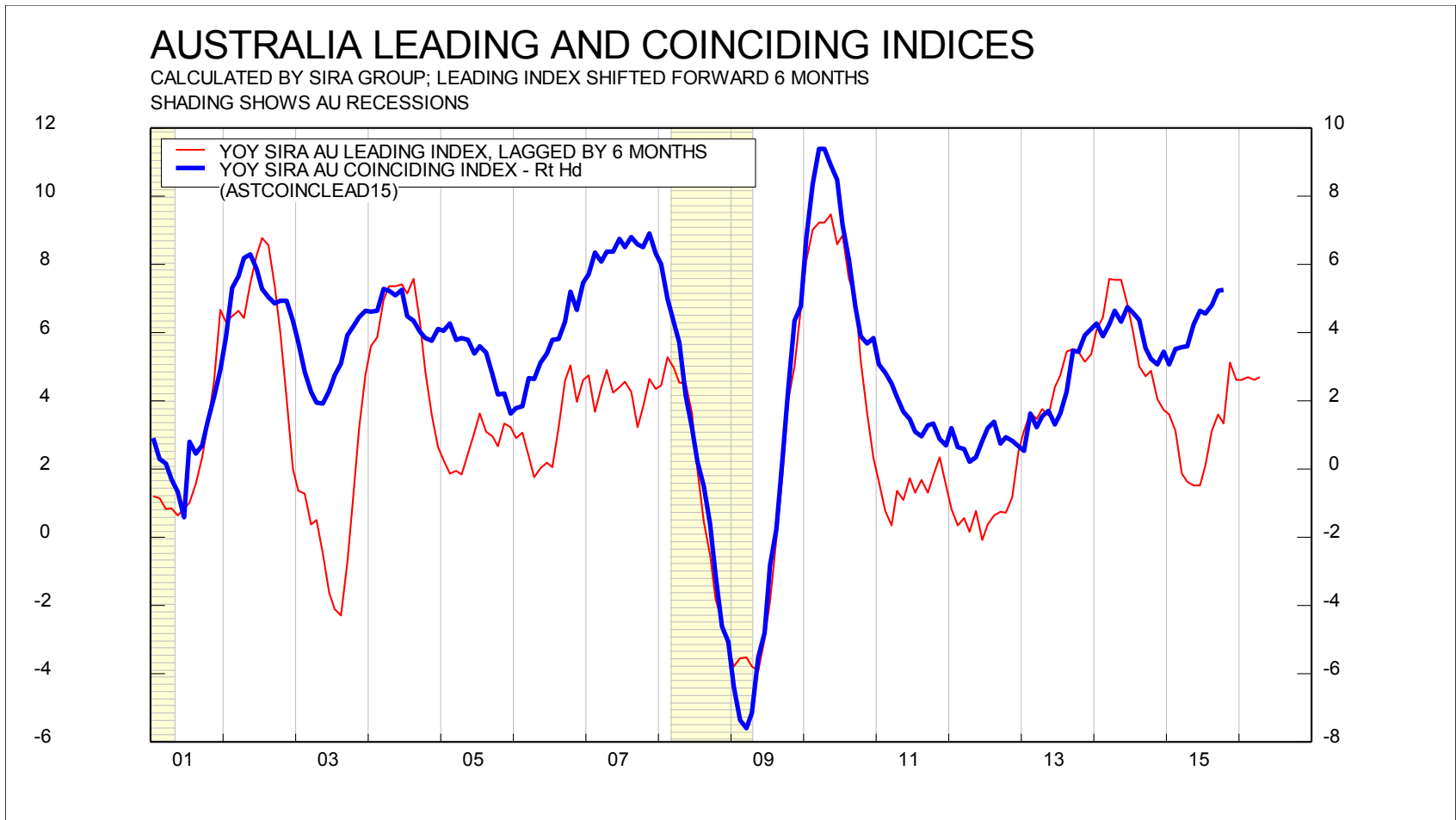
Other commods falling too



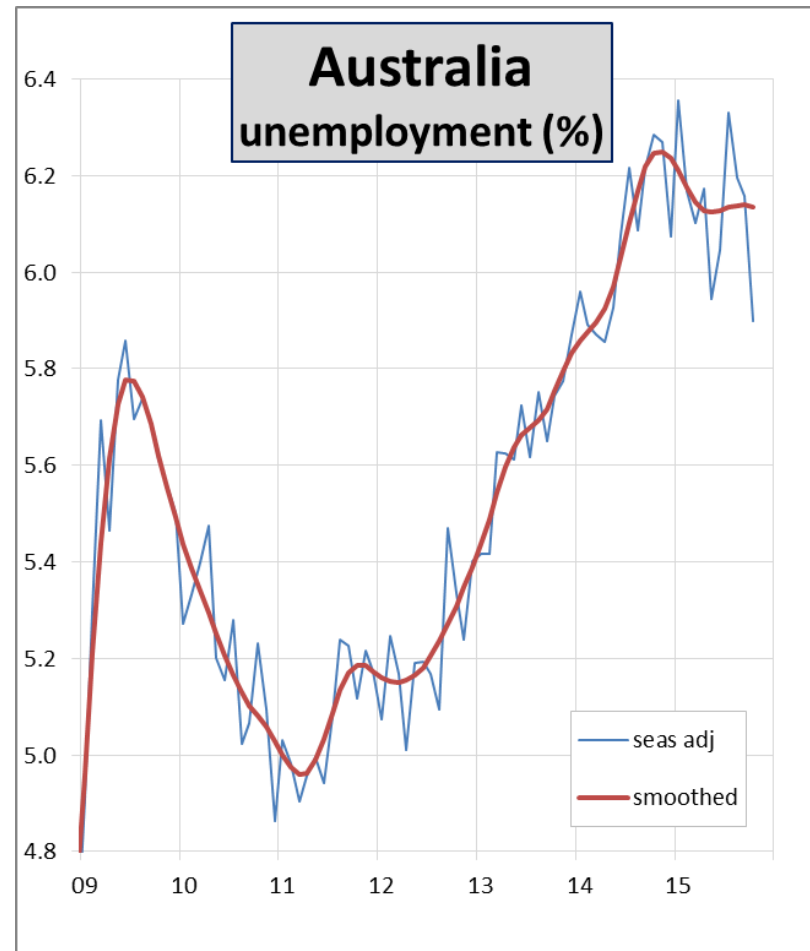
Australian econ should be weak ..



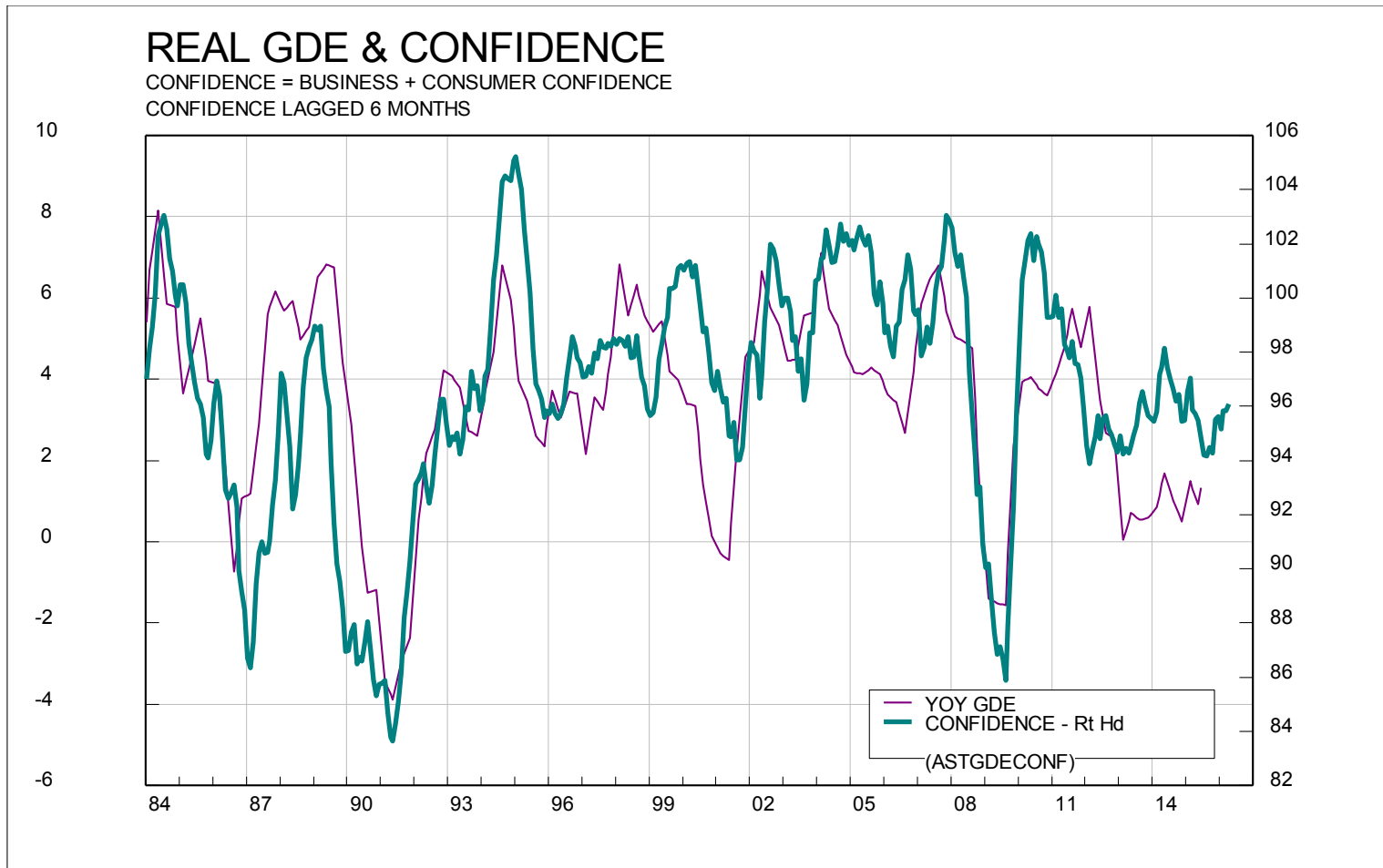
Econ strengthening



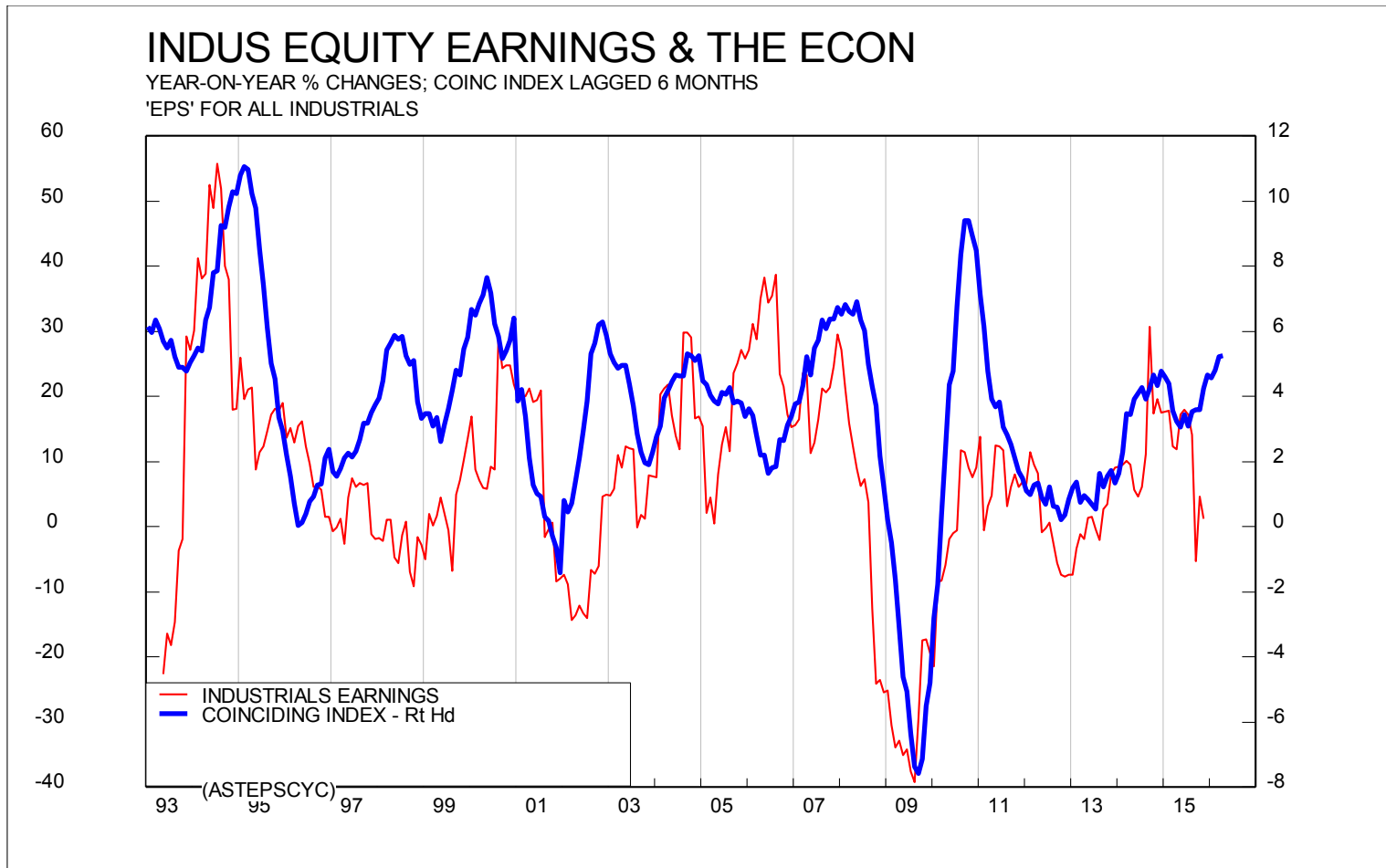
Unemployment rate falling?



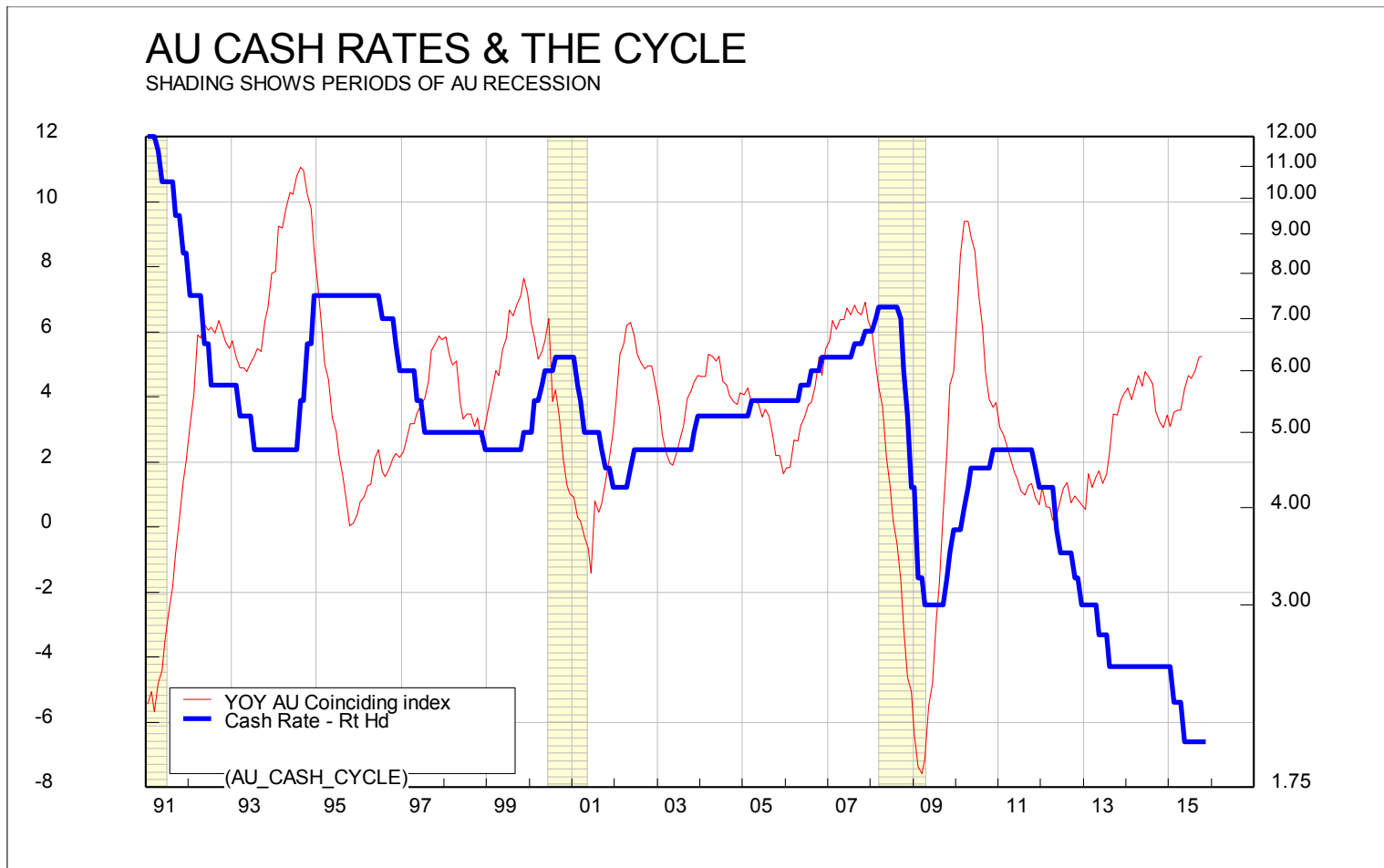
Business & Cons Confidence rising



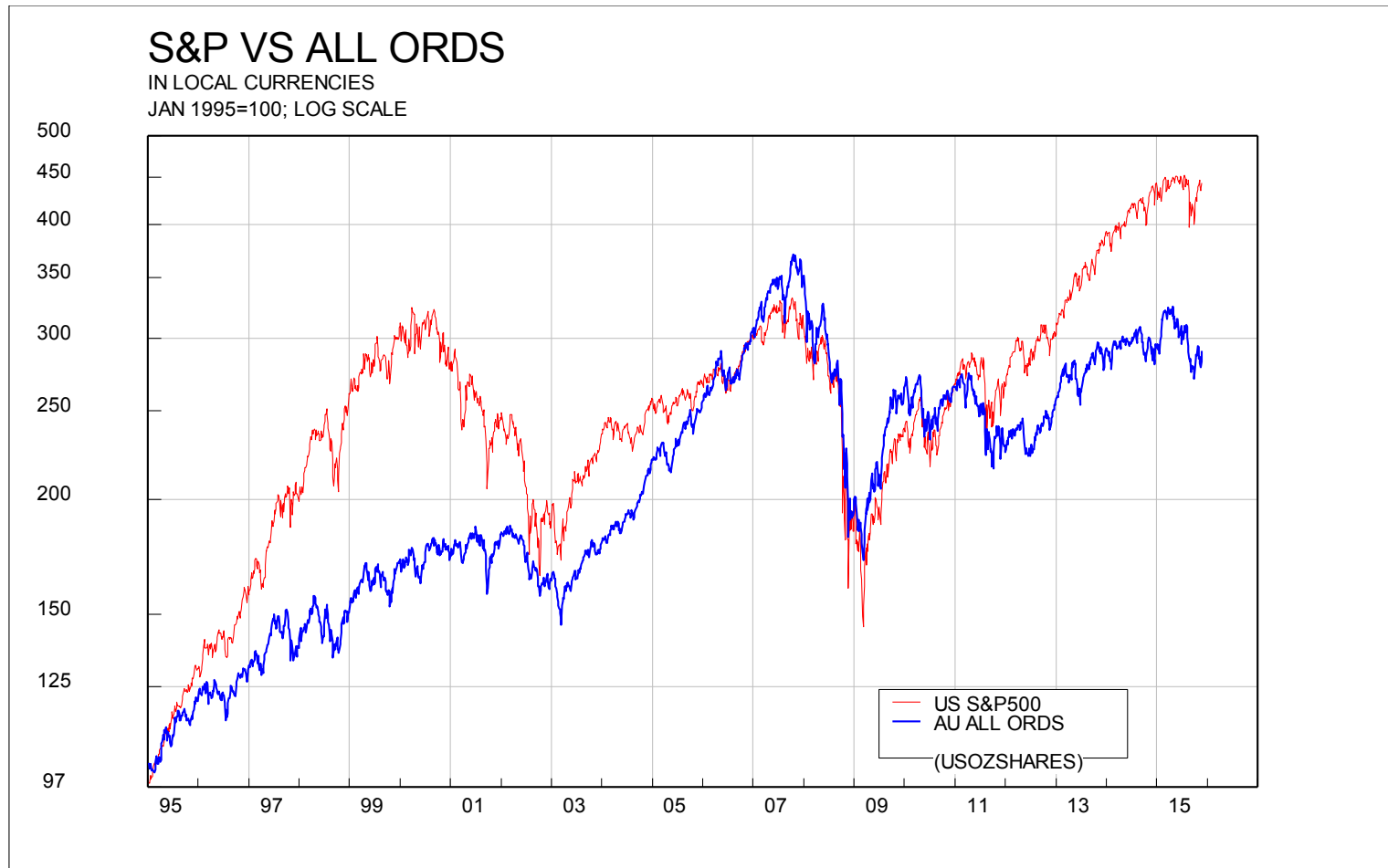
Earnings to recover



Cash rate on hold?



Australia usually follows US



Summary

- AU economy stronger than expected
- Cash rate on hold, for now
- Bond yields rising (yield play?)
- Industrial EPS should recover somewhat
- US Market likely to hold up