6,000 is a long way off

Slides for Ron Bewley interview on Switzer TV 2/10/2013

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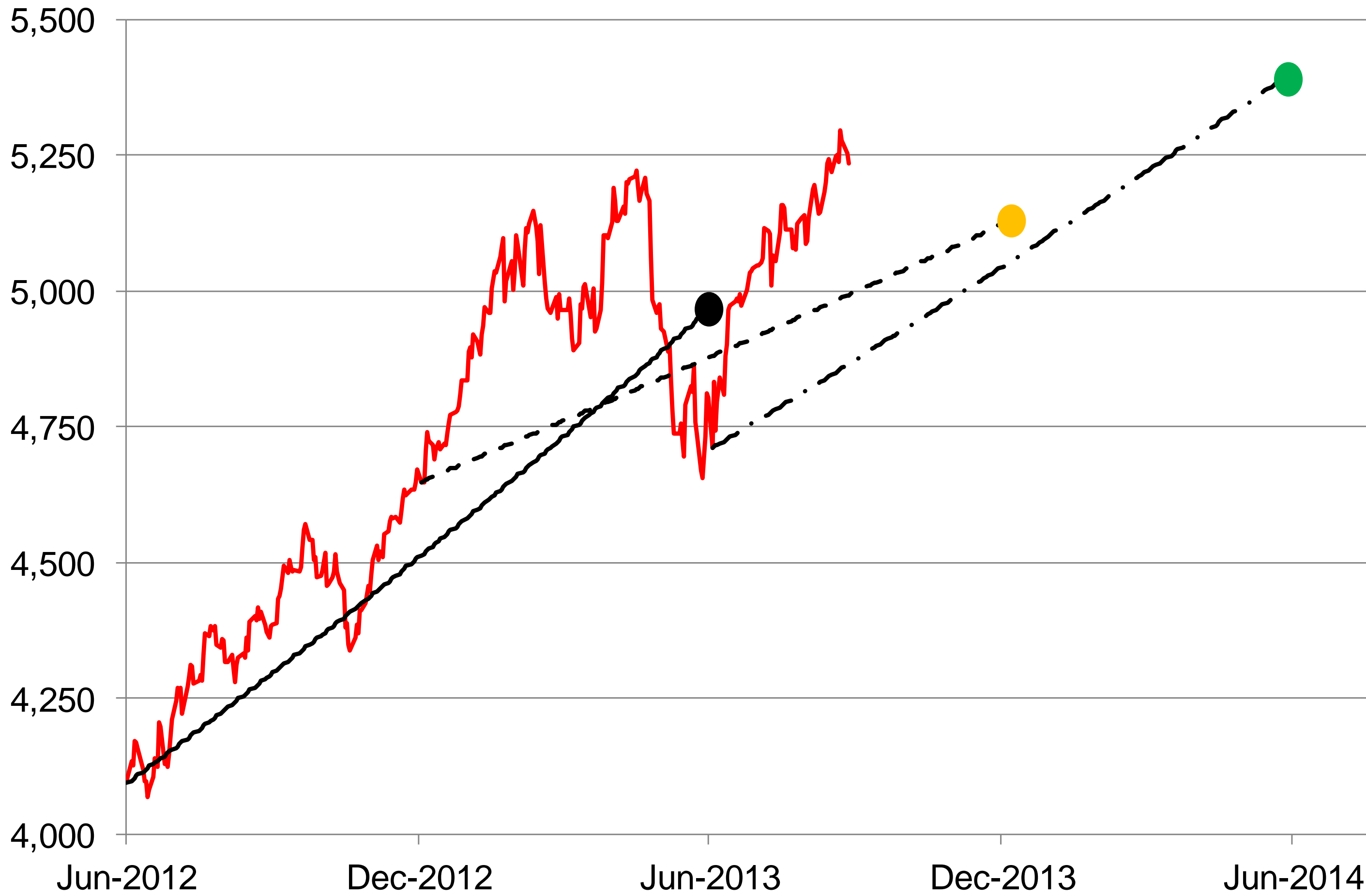
Chart 1: Capital gains forecasts – ASX 200



Notes

- The previous slide shows our 12-month-ahead forecasts of the ASX 200 made at the end of June 2012, December 2012, and June 2013.
- Arguably the first forecast (black circle) was ‘wrong’ at just under 4,950 when the e-o-y 2012 was about 4,700 – but a few days later it was spot on! Such is the volatility of the market. As a decision to invest or not, the forecast had some quality.
- The orange dot looks low given where we are today. We think broker forecasts - on which we base our estimates – may soon be revised (as we argue later in this interview) Our current e-o-y forecast is 5,300.
- The green for June next year certainly looks low. Why, when at least one broker is calling for 6,000 by then, is our forecast so low?
- To put these forecasts into context, the AFR reported on 13 March 2013 that of 6 major international houses, the range of forecasts based at the start of 2013 was 4,250 (JP Morgan) to 5,000 (Goldman Sachs) and, even after the first three months, three of the houses were still forecasting under 5,000 for e-o-y 2013! I argue that their forecasts implied it would have been better not to have invested in equities in 2013.
- Our long-run model since the beginning of the year has been for 5,550 to be ‘fair value’ for e-o-y 2013 so we have continually argued for ‘upside risk’.
- On the next slide, we give our current forecast for the next 12 months (ending October 2014). We argue that High Yield sectors are constrained by dividend yields and so will not contribute much to capital gains in the ASX 200 so the other two sectors have to do all of the heavy lifting – and they are only half of the market. Please read our weeklies and monthlies for added colour. To add to the problem exuberance (mispricing) is currently moderately high. The following slide (not used in the interview) contains more detailed information from which Chart 2 is constructed.

Chart 2: Sector forecasts for ASX 200

Sector	Exub- erance	12 month forecasts			Index weight
		Yield	Cap. gain	Fwd P/E	
Resource-related	-1.1%	3.5%	17.4%	13.6	29%
High yield	2.0%	5.5%	3.6%	13.5	52%
Other	1.1%	3.3%	10.2%	18.0	20%
ASX 200	0.5%	4.5%	9.4%	14.1	100%

Source: Thomson Reuters and Woodhall Investment Research

Resource-related: Energy, Materials, Industrials

High yield: Financials, Property, Telcos, Utilities

Other: Discretionary, Staples, Health, IT

Chart 2a: Sector forecasts for ASX 200

	Sector	P/E ratio		Cons.	Market	Exub-	12 month forecasts		
		historical	forward	rec.	cap.	erance	yield	cap. gain	adj. gain
Resource-related	Energy	18.5	15.2	2.6	5.7%	-0.1%	3.6%	21.7%	21.8%
	Materials	13.8	11.9	2.3	16.8%	-2.8%	3.3%	16.0%	18.7%
	Industrials	18.7	16.6	2.5	6.0%	2.6%	4.0%	12.1%	9.6%
High yield	Financials	14.0	13.2	2.7	38.7%	2.7%	5.5%	5.9%	3.2%
	Property	14.9	14.3	2.6	6.1%	-0.9%	5.7%	4.2%	5.2%
	Telco	15.3	14.6	2.9	5.2%	1.4%	5.8%	4.4%	3.0%
	Utilities	16.5	15.1	2.6	1.6%	-0.7%	5.7%	8.4%	9.1%
Other	Discretionary	20.7	18.0	2.4	6.7%	3.4%	2.3%	14.2%	10.8%
	Staples	18.3	16.9	3.1	8.0%	-0.3%	4.6%	8.2%	8.5%
	Health	22.5	19.9	2.5	4.5%	0.3%	2.4%	12.3%	12.0%
	IT	19.8	17.6	2.8	0.7%	-0.3%	3.2%	12.1%	12.4%
	ASX 200	15.5	14.1	2.6	100.0%	0.5%	4.5%	9.9%	9.4%

Source: Thomson Reuters and Woodhall Investment Research; adj. gain is the expected capital gain after taking into account mispricing or exuberance.

Chart 3: Real, per capita other personal debt

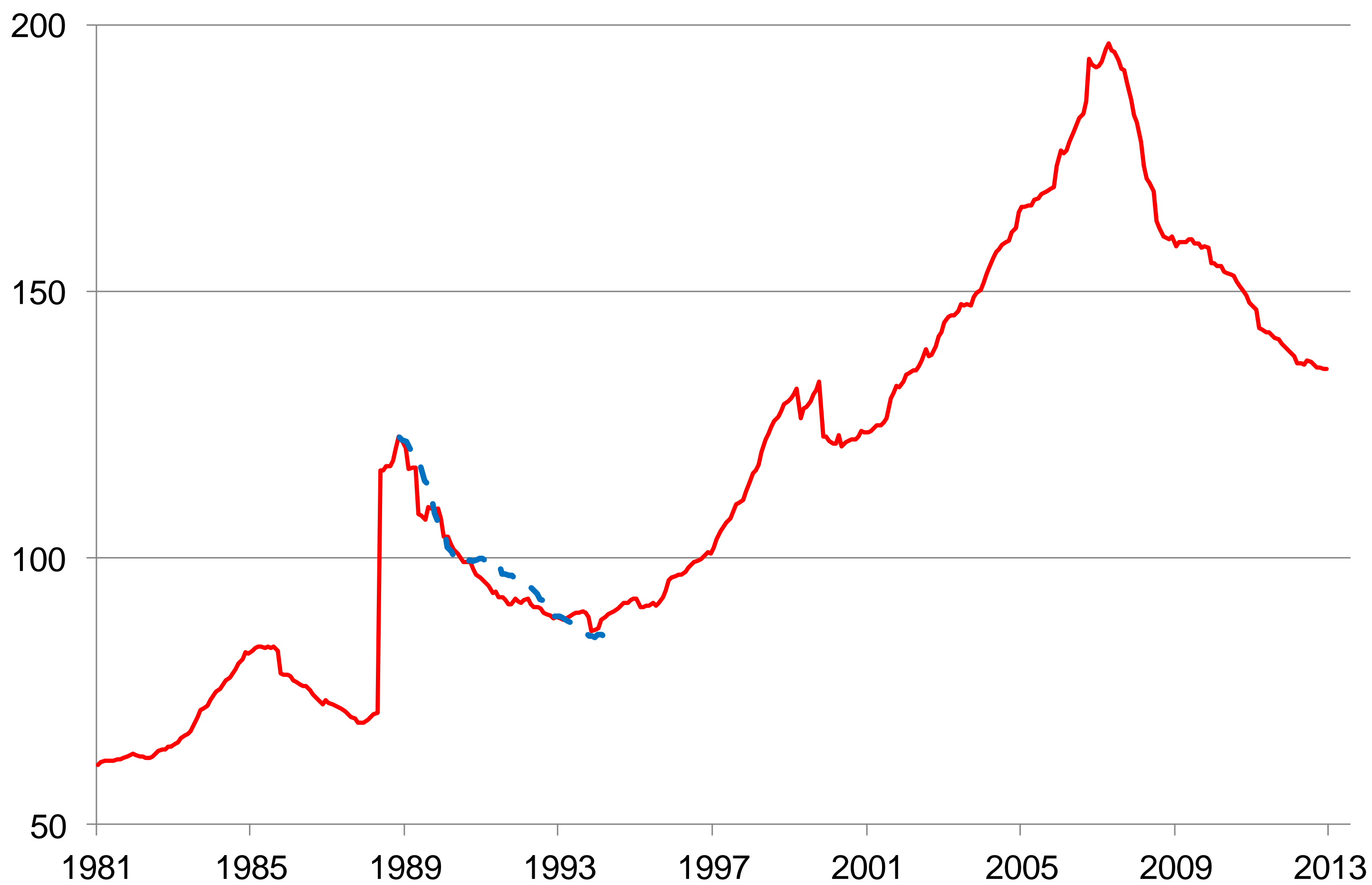
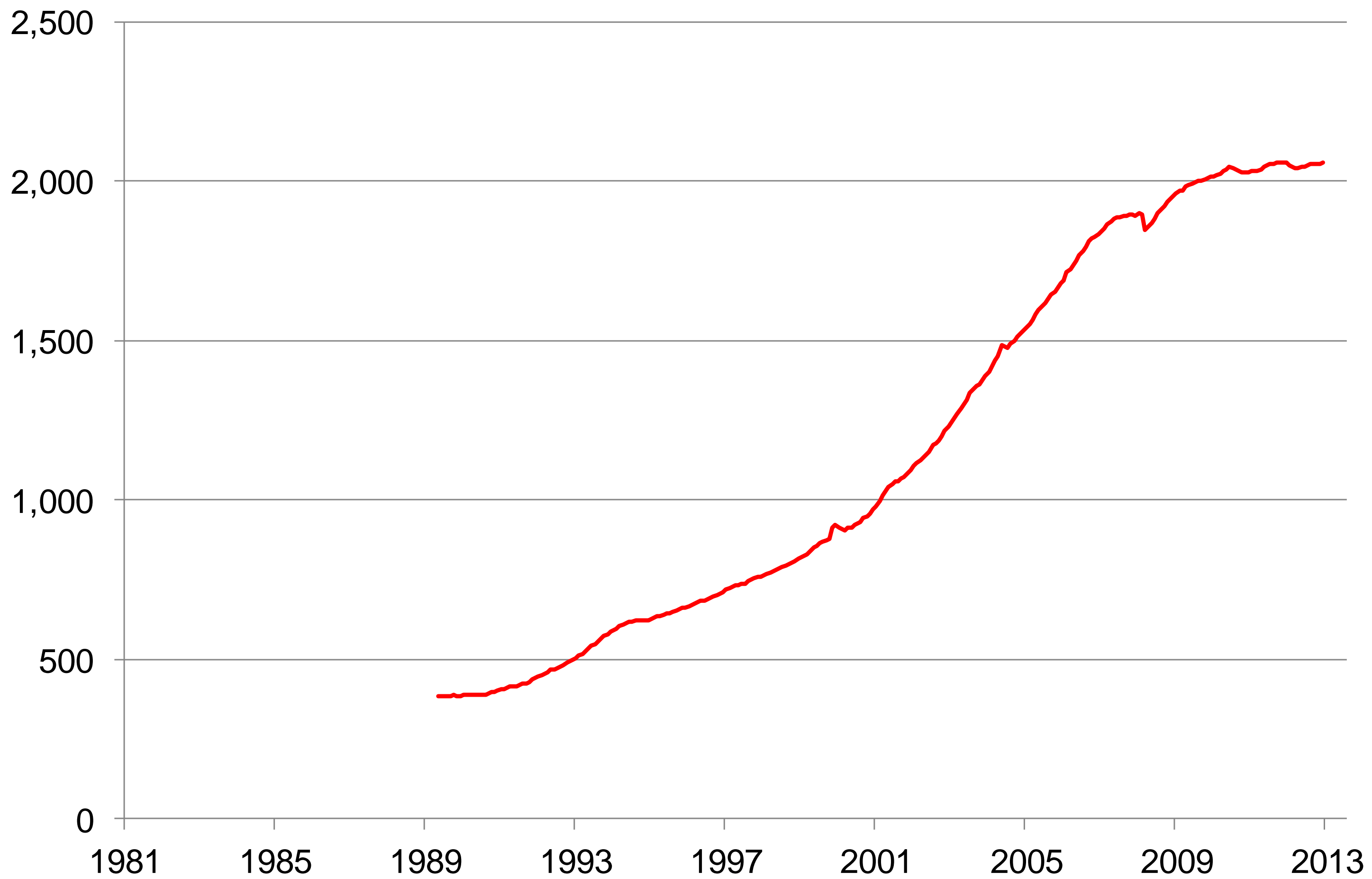


Chart 4: Real, per capita owner- occupied home loans



Notes

- Other personal debt is from all financial institutions and excludes home loans, investment home loans and business loans.
- I have deflated the data to allow for population and CPI increases. I have rescaled the data to be equal to the published data at the latest month.
- People have been paying off credit card debt, personal loans and related debt to a massive extent – but almost at the same rate as in our last recession!
- The blue dotted line is a copy of the fall from the recent 2007 peak rescaled and shifted back to the pre-1990 recession peak. They are almost identical and we now look at the bottom of the deleveraging. So human behaviour has not changed in 20 odd years!
- The owner-occupied home loans data show a plateau over the last few years. People have not been paying down debt but they stopped increasing it.
- Renewed confidence from the deleveraging could start a fall in the savings ratio and a boost to growth.
- We believe our current forecasts, therefore, are more of a floor than a best estimate as brokers seem to be conservative at this stage – and I didn't mention that most people got the China story so wrong.