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Woodhall's Weekly

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Key points

Volatility: The market fell by 1.4% over the week as Greece finally finished a debt restructure and triggered a credit event. Even so, there was barely a ripple in volatility - a 'baby' cluster around the pre-GFC mean rather than a jump back up for an extended period.

Fear: Not did our measure of fear - or irrational volatility - not jump up on the Greek showdown, it even fell below the lower bound. The market was ready and waiting!

Disorder: Disorder - a measure of the lack of similarity in returns across sectors of the market - hovered around the lower tramline. Controlled fear and disorder is, in our opinion, a necessary condition for the market to sustain a rally. Providing there is no 'new' bad news about the credit event over the weekend, there is little reason to expect anything other than an orderly ASX 200 on Monday - and beyond.

Capital gains forecasts: Our forecast for the next 12 months climbed a little higher to just under 15%. The future continues to look brighter.

Market exuberance: Exuberance fell to -2%. Some of this fall could well be due to the US's hot market coming off the boil last Tuesday. There are no danger signs now in either market.

Sectoral exuberance: Materials took a hit on the China story and is now 6.3% underpriced. We contend that there was no news in the 7.5% GDP China target as it had been flagged some time ago as part of the next 5-year plan. Since China rode well above its 8% target for the last 5-year plan, and inflation just came in at 3.2%, China looks in great shape! Staples continue to be cheap but nearly all of the heat has been taken out of Industrials and Discretionary.

Summary: After months of waiting for a solution to the second Greek bailout, all was revealed overnight. President Sarkozy called it done and dusted. The US kept up its improving labour market with the best six months data since 2006. Our GDP figure was a bit shoddy and so was unemployment but a cut in rates would not redress the imbalance in our economy - it is a crisis in confidence and savings ratios that are the roots of our problems.

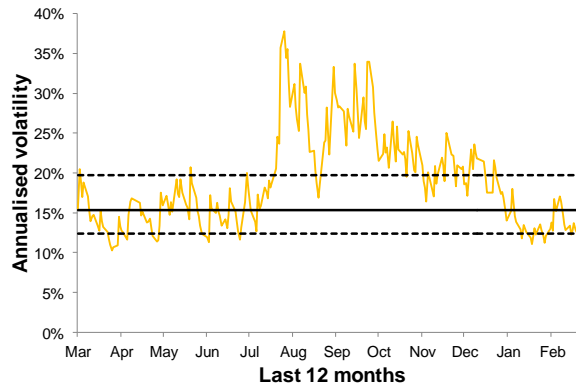
All data are sourced from Thomson Reuters Datastream.

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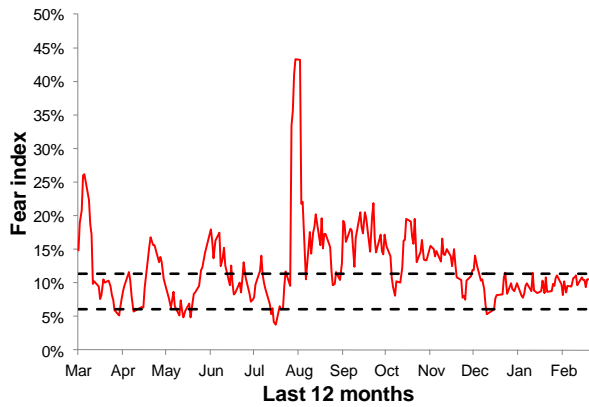
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Chart 1: Daily volatility



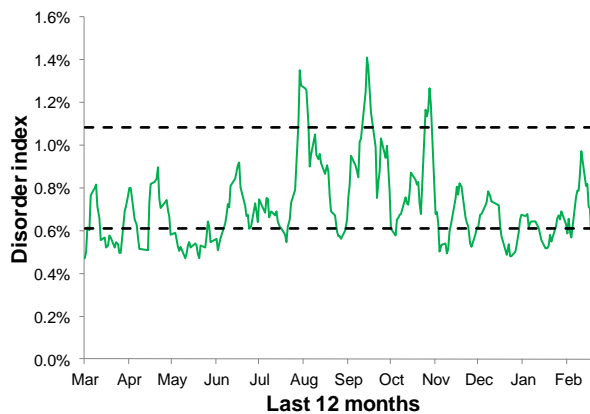
Notes: The solid black line denotes the current average volatility since January 2010; the lower dotted line denotes the average volatility pre GFC; the upper dotted line denotes average volatility during the GFC.

Chart 2: The fear index



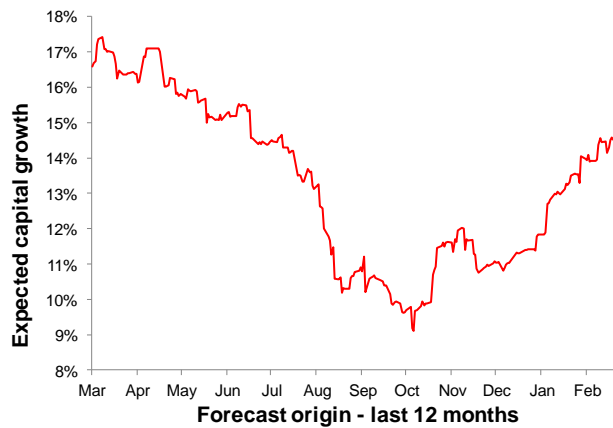
Notes: The two dotted lines denote the range where fear resided pre-GFC for two thirds of the time

Chart 3: The disorder index



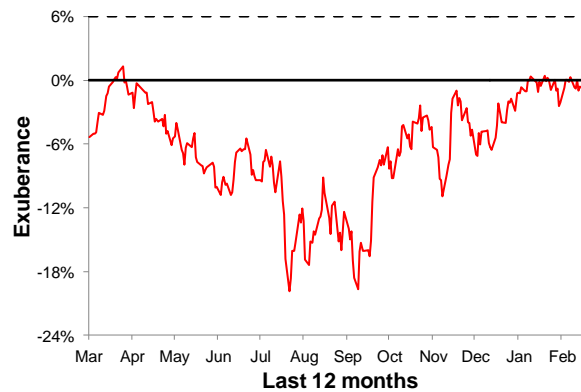
Notes: The two dotted lines denote the range where disorder resided pre-GFC for two thirds of the time.

Chart 4: Forecasts of capital growth



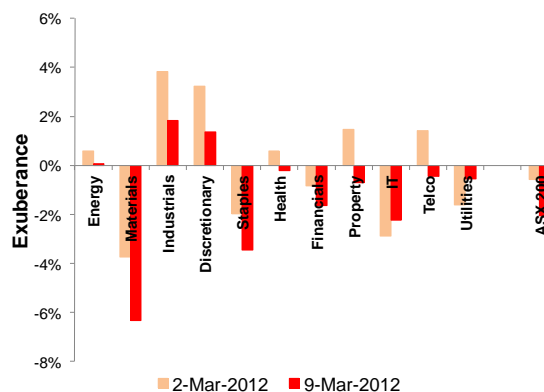
Note: These forecasts are updated daily for the following 12 months. Dividends should also be taken into account when assessing possible performance.

Chart 5: Exuberance over time



Notes: 0% represents 'fair pricing' and the dotted line at 6% represents possible overheating preceding a correction. Cheap markets (below the 0% line) can get a lot cheaper before they recover!

Chart 6: Sectoral exuberance



Notes: Our *Guide to Woodhall's Publications* should be consulted for a better understanding of how all six charts are constructed.