New York Securities Pty Ltd

Monthly Newsletter - February 2014

GONG XI FA CAI

Happy Chinese New Year to all! A number of Chinese Feng Shui Masters are predicting the year of the Horse will experience volatility in the first two quarters akin to “a galloping horse” (up and down), whilst the second half of the year will be a good time to invest as the markets stabilize leading into 2015. Only time will tell but so far they have been correct in their predictions with the month of January galloping out of the gates at slow pace on a muddy pitch, with a variety of concerns including mixed earnings results from US companies, mixed data from China and a variety of issues in a number of smaller emerging economies dominating the headlines.

The XJO currently sits around 5200, maintaining the long term uptrend which emerged in May 2012. This week is the beginning of the reporting season in the Australian market with the majority of analysts expecting mixed results, with the Health Care sector likely to outperform due to its exposure to the lower Australian dollar. Our main focus will be placed on the ‘Micro’ components related to cost reduction, return on equity, assets and dividend growth against a backdrop of an improving ‘Macro’ picture from US and Europe. If results are anything less than expected, pressure will be placed on the market short term, possibly testing the uptrend. A convincing move below 5200 will result in a pullback to 5050 in the short term as shown by the red line below.

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AFSL: 317392 ABN: 70 111 049 800

Shop 11 “South Shore Piazza” 85 South Perth Esplanade, South Perth, WA 6151 | PO Box 1196, South Perth, WA 6951 | P: (08) 9363 1700 | F: (08) 9367 2450 |

E: info@nysecurities.com.au

W: www.nysecurities.com.au

Manufacturing and Unions

Locally, the high Australian dollar has dealt the Manufacturing sector another blow with SPC Ardmona looking like it will close its doors unless (as we are lead to believe) the Government can inject $25 million into a restructure of the company's operations. The Abbott Government is refusing to bailout any company with tax payer's money and given SPC Ardmona, a subsidiary of Coca Cola Amatil who is forecasted to net a $536 to $558.4 profit for FY13, it's no wonder. A bail-out doesn't guarantee a sustainable future; instead it's likely to give rise to further bailouts and a waste of tax payers' money in the longer term. Perhaps the unions, who never fail to portray themselves as victims when things don't go their way, should take a hard look at themselves and their greedy, unreasonable enterprise bargaining agreements and admit it is their excessive demands that have played a major factor in the demise of the Australian Manufacturing sector. Something needs to change for the better of this country and Abbott is hitting the unions every which way he can, with a Royal Commission on the unions imminent and a clear mandate the Government will not be used to bail-out private enterprise.

US Data and Emerging Economies

The Federal Reserve has pared its bond buying program to $65 billion a month for the second month in a row, on the back of "growing underlying strength in the broader economy". US GDP in the fourth quarter grew at 3.2%, following the strong reading in the previous quarter of 4.1%, bringing with it good momentum leading into 2014, along with the improving unemployment rate which now sits below 6.7%, the first time below 7% since December 2008.

The Federal Fund Rate, the rate at which institutions lend to each other in the overnight market, is set to remain near zero (currently 0.07%) through to 2015, or until data suggests this rate can be lifted. Bernanke or 'Helicopter Ben' is set to leave his post as Chairman to make way for Janet Yellen who is considered 'Dovish' in her approach towards monetary policy. Her mindset gives participants confidence in knowing Fed decisions won't be made with unnecessary risk.

There has been a number of large interest rate rises in some small emerging economies, each for their own specific reasons. The countries that have seen the most drastic moves include:

Brazil - Interest Rates Rise 10% to 10.5%
South Africa - ***Interest Rates Rise*** 5% to 5.5%

The most aggressive interest rate rise to date was conducted by the Turkish Central Bank, who intervened to halt the sharp depreciation of their currency, the Turkish Lira;

Turkey - ***Overnight Lending Rate*** - 7.75% to 12%
- ***Overnight Borrowing rate*** - 3.5% to 8%

Cheap money created years ago by the Federal Reserve set the stage for "The Chase for Yield", and consequently Turkey, amongst other smaller emerging economies benefited from an increase in the flow of capital from those seeking higher yields. Unfortunately many of the smaller emerging economies now find themselves battling persistent high inflation and rapid depreciating currencies, possibly created by the US tapering its bond buying program, forcing them to raise interest rates and creating fear of the potential flow on effects on developed nations.

So, is the market overreacting? Well we believe the answer is yes. We believe it's been just another excuse to sell into markets and gives the media some content to publish. The smaller emerging economies including Brazil, Turkey and South Africa who are all facing specific issues aren't very high on the list of Australia's trading partners, in fact, all three make up less than 1.1% of Australia's total trade (exports and imports) (source: DFAT). Furthermore, Australia has already been recording a decline in trade from these economies since 2011, so a further decline in total trade won't be an unexpected shock to our economy. On the contrary it's more likely to assist in lowering the Australian dollar to the RBA's target of 85c against the US dollar. Speaking of which, the RBA meets tomorrow and we expect interest rates to remain on hold.

The importance still lies with the underlying performance of Australia's major trading partners, China, Japan and the US. We consider the improvement from a 'Macro' perspective in these economies positive however the 'Micro' situation remains mixed. Our view is yield remains king, so use any pullback as an opportunity to pick up some high yielding stocks for a longer term hold. The R

<u>Debt Ceiling</u>

This week we will progressively hear more and more about the US debt ceiling deadline, due on the 7th February. If the debate goes beyond this point there are additional measures that can be used to extend the full faith and credit of the United States Government. The effects of the discussions over the debt ceiling on market participants is diminishing over time, instead its really now being used as a political tool, so we believe it will once again be resolved and little pressure will be placed on the markets.

<u>Spot The Difference</u>

The note on the left was legal tender issued by the United States Government, known as a "United States Note" or 'Red Seal Note'. It was issued by the United States Treasury on an interest/debt-free basis and backed by Gold until Nixon removed the Gold backing in 1971, much like a 'bill of credit'. It was gradually replaced from the 1940's by the "Federal Reserve Note" (on the right) which is backed by debt purchased by the Federal Reserve (a non-government entity) serving as a conduit to generate interest (Statutory 6% dividend paid on member bank stock) for the benefit of its owners, the private member banks (stock holders)! On another note (excuse the pun), James Garfield, JFK and Abraham Lincoln, were all American Presidents who opposed the control of the Federal Reserve over the financial system and all were assassinated in similar circumstances, by a speeding bullet, the same speed to which the Fed has been printing its Notes.

Performance of Key Indices

Equities	Close	Change (M)	Change % (M)
All Ordinaries	5205.10	-109.2	-2.05%
S&P/ASX200	5190	-130.0	-2.44%
Dow Jones (US)	15698.85	-387.56	-2.41%
NASDAQ	4103.88	+43.99	1.08%
S&P500	1782.59	-23.22	-1.29%
FTSE 100 Index	6510.44	-140.13	-2.11%
Nikkei 225 (Japan)	14914.53	-747.34	-4.77%
10-year bond rate (US)	2.65%	-0.05	-3.58%

Upcoming RBA Events

Reserve Bank Board Meeting – 4th February
Statement on Monetary Policy – 7th February
Minutes of the RBA meeting – 18th February

ABS releases February

Building Approvals – 3rd February
Retail Trade (December) – 6th February
International Trade in Goods and Services (December) – 6th February
Housing Finance (December) – 11th February
Labour Force (January) – 13th February
Lending Finance (December) – 14th February

Upcoming US Economic Releases

ISM Manufacturing Index – 3rd February
International Trade – 6th February
US Employment Situation (January) – 7th February
Retail Sales – 13th February
FOMC Meeting Announcement – 19th February
Producer Price Index – 19th February
Consumer Price Index – 20th February
Durable Goods Orders– 27th February
GDP – 28th February
Jobless Claims – Weekly Basis