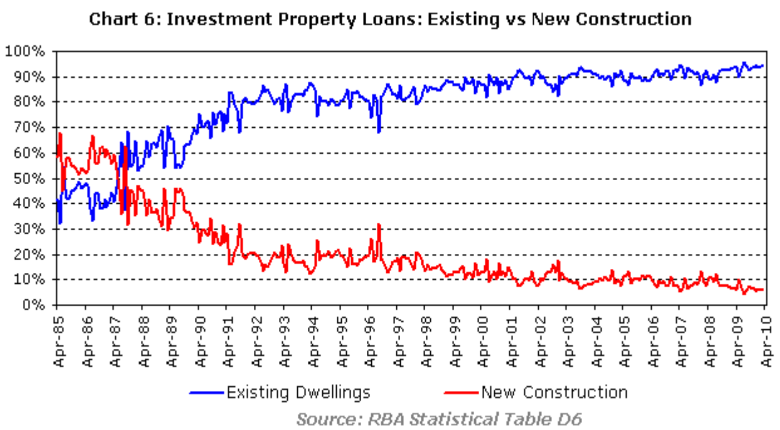
Monthly Newsletter – April 2015

THE RBA CALLS FOR BACKUP

The RBA's minutes during the month painted a rather unflattering picture of the current economic environment. There's only one conclusion that could be drawn from it all and that is a rate cut near term is inevitable. What we found interesting was the RBA comments seemed more transparent than usual and after reading the Financial Stability Review (FSR) which emphasized its concerns over the housing market, a hidden message was revealed, **HELP**. It's been four years to the month since Glenn Stevens made his first television appearance as RBA chief on the morning show "Sunrise". His message back then was clear, **no good could come of a prolonged period of very low interest rates, nor should households consider property to be an easy path to prosperity**. Now, whether he's just a very good economist or he stole a time machine is debatable, but these comments are an eerie reflection of where we stand today. In essence, his call for help contains a little more detail… Considering rates are at record lows, further action by the RBA (rate cuts) needs to be as burden free as possible to have any meaningful influence. In other words, the Government and the regulator APRA need to step up, be proactive and reduce the risks associated with an overheated housing market.

JOE HOCKEY ANSWERS THE CALL

A few days after the release of the RBA's FSR, Joe Hockey released the Governments discussion paper on tax reform. One hot topic discussed was Negative Gearing. This measure was first introduced to encourage the supply of **new housing** and to propel the economy forward in the 1930's right after the Great Depression. The Hawke Government had it quarantined in 1985 but due to persistent arguments made by the Housing Industry Association, which were that the Governments decision was driving up rental costs, it was reinstated in 1987. Since then it has been a driving force behind the surge in property prices and the very thing the HIA argued against: rental costs. In our opinion, **for the greater benefit of the economy** there should to be a "cap" placed on the tax benefits derived from investment on existing dwellings. This should dampen excessive speculation and assist in achieving a balanced and gradual restoration toward its initial purpose, which has clearly not been the case since 1987;



XJO INDEX TO BREAK 6000 – HERE'S WHY

In the chart below we can see a distinct upward sloping channel defined by the parallel red line and black trend lines. This channel A.K.A "bullish continuation move" has now met the significant long term resistance line of 6000 index points. The strong advance from 5400 index points (January) to 6000 index points (March) continues to be tested by the sellers who have so far failed to overwhelm buyers. The long term trend is still very well in play and although there has been two failed attempts to exceed 6000 index points we believe it will be a case of "third time lucky" for the index by the end of May, the month we believe the next rate cut will occur. In our opinion, despite some analysts commenting that valuations are stretched, the current downward trend in interest rates and the risks associated with rising asset prices will force investors to seek a more liquid and high yielding investment environment- the stock market.

FOOD FOR THOUGHT

It is estimated a total of $89.8 billion is set to pour back into the hands of investors during 2015. This amount consists of $80.5 billion in dividends and $9.3 billion in share buybacks. To put into perspective the total $89.9 billion represents about a month's worth of buying on the XJO S&P/ASX200. It is not unreasonable to conclude that this money will be looking for a respectable return, far beyond what the local bank is willing to offer. Our opinion is the stock market will be a large beneficiary of these funds. The property market will benefit to a degree but the risks to bricks and mortar are far too high compared to a market which offers far more liquidity. When the risks are rising you want to have the ability to exit as quickly as possible and where else can you do this but the stock market?

TWIGGY SNAPS

As the saying goes "When it rains it pours" and unfortunately for Andrew "Twiggy" Forrest he was caught up in a big storm during the month. After their $2.5 billion bond sale was terminated and the Iron ore price continued to tank the frustration finally hit Fortescue Metals Group Ltd (FMG)'s largest shareholder and he "snapped" calling upon the largest iron ore producers to create a cartel and cap production to push up the iron ore price. His request is reflective of a desperate person, highly concerned about the current situation and its outlook. It's a terrible look for the FMG board and shows he has no confidence in them to tackle the current and future challenges. Our view remains unchanged, be sure to stay out of the high cost producers, FMG, Atlas Iron, Gindalbie, BC Iron and Mount Gibson. We don't see any light at the end of the tunnel for the price of iron ore at this stage.

DIVIDEND REINVESTMENT PLANS

Albert Einstein once famously quoted:

"Compound interest is the eighth wonder of the world. He (or She), who understands it, earns it ... he who doesn't ... pays it".

In simple terms it's based on the idea that you reinvest your earnings on an investment to earn more money than before. In general it accelerates the rate of growth in your investment and applying this concept to the share market can assist you in accelerating the growth of your portfolio over time.

How does it all work?

There are a number of companies on the ASX that offer an alternative to receiving a dividend payment each year. They include many of the household names like CBA and if you're not reliant on the income you need to seriously consider the option to participate. Dividend reinvestment plans simply mean rather than receiving a dividend in the form of cash the company will issue you shares equal to the dividend amount you would have received. The advantage of doing so is you are constantly building the base of which your next dividend return is derived. To show you the effects of dividend reinvestment plans here is an example:

Initial Investment: *$10,000* ***Stock:*** *XYZ* ***Number of Shares:*** *1000*
Purchase Price: *$10.00* ***Dividend Yield:*** *6%*

Assumptions:

- ***Expected growth in dividend 5% p.a.***
- ***Expected growth in share price 5% p.a.***
- ***Zero Franking***
- ***Dividend paid annually***
- ***Pre Tax Calculation***

No Reinvestment over the 10 year period		**Dividend Reinvestment over the 10 year period**	
Valuation (includes dividend payments)	$16,288.95	Valuation	$28,394.21
Shares now owned	1000	Shares now owned	1743
Dividend Paid over 10 years	$7,546.74	Dividend Paid over 10 years	$10,033.21 (reinvested in stock)
New Annual Dividend	$977.34	New Annual Dividend	$1,703.65
Total Return	***138.3%***	***Total Return***	***183.94%***
Annualized Return	***9% p.a.***	***Annualized Return***	***11.% p.a.***

The total return generated from DRP participation in the above example was 187.1% or 20.7% greater than the return generated by not participating in the company's DRP. In addition if you were to cancel the DRP today your dividend payments would be $1,726.25 per year compared to $977.34 per year by not participating (assuming future payments consistent with year 10). The advantages are obvious. Participating in the DRP can potentially **accelerate the growth** of your portfolio and **boost your future earnings**. In addition overtime the dividend amounts are reinvested into new stock at levels reflective of inevitable market fluctuations meaning you're not always purchasing stock at the same price, rather you are effectively **dollar cost averaging** the holding in the company. If you have children, nieces or nephews a DRP is a great way to kick start their financial future. So be sure to have a think about it for your current and/or future holding.

Please Note - Dividend Reinvestment Plans do not prejudice attached franking credits (if any) and so despite reinvesting in new shares you will still receive the benefit of the franking credit after you submit the relevant information with your tax return (*Please discuss this with your accountant*).

Performance of Key Indices

Equities	*Close*	*Change (M)*	*Change % (M)*
All Ordinaries	**5861.90**	**-36.6**	**-0.6%**
S&P/ASX200	**5891.5**	**-37.3**	**-0.6%**
Dow Jones (US)	**17776.12**	**-356.58**	**-1.97%**
NASDAQ	**4900.89**	**-62.64**	**-1.3%**
S&P500	**2067.89**	**-36.61**	**-1.7%**
FTSE 100 Index	**6773.04**	**-173.62**	**-2.5%**
Nikkei 225 (Japan)	**19206.99**	**+409.05**	**+2.2%**
10-year bond rate (US)	**1.92%**	**-0.00068**	**-3.4%**

Upcoming RBA Events

Reserve Bank Board Meeting – 7th April
Minutes of the RBA meeting – 21st April
Speech by Glenn Stevens, Banking and Wealth Summit – 28th April

ABS releases March

Building Approvals (February) – 1st April
International Trade in Goods and Services (February) – 2nd April
Retail Trade (February) – 7th April
Housing Finance (February) – 10th April
Lending Finance (February) – 14th April
Labour Force (March) – 23rd April
Consumer Price Index (March) – 22nd April

Upcoming US Economic Releases

ISM Manufacturing Index – 1st April
International Trade (March) – 2nd April
US Employment Situation (March) – 3rd April
FOMC Meeting and Minutes – 8th April
Retail Sales (March) – 14th April
Producer Price Index (March) – 14th April

Housing Starts – 16th April
Consumer Price Index – 17th April
Existing Home Sales (March)–22nd April
New Home Sales (March) – 23rd April
Durable Goods Orders (March) – 24th April
GDP – 29th April
Jobless Claims – Weekly Basis