



The Princess and the Pea

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Share markets around the globe seem to be indicating that we are through the worst of the GFC. Financial commentators tell us that the March lows will not be revisited and interest rates in Australia could be up by as much as 1% by the end of this year. This is indeed a fairytale outcome which by all accounts would suggest we are again able to sleep easy...or is there a pea under the mattress that will keep us tossing and turning through the night?

I consider myself to be an optimist. I will search high and low in the face of adversity for a positive outcome or at least an opportunity to create one. Sometimes it is easy, after nothing more than a glance, to follow the crowd in a rally of positive energy to confirm that everything is on track - we are all going to be just fine thank you very much. At the same time, it is important not to get too carried away - to have a quick look in the rear-view, consider just what we have been through, and check for possible risks and opportunities ahead.

In the US

The average work week for June was 33 hours. This is the lowest hours worked since records began in 1964. July added just 6 minutes to the working week. Companies appear to be profiting from the still reduced labour costs, but it is important to remember that for consumers to spend up they need income. Massive government stimulus has been a contributor to the signs of recovery, and there are still large sums to be spent on the back of the highest unemployment rate in the US in 26 years. One would expect that all of this spending, in conjunction with the reported increases in corporate profits should lead to improved employment, although there does not seem to be any support for the unemployment rate doing a u-turn before breaking 10%.



In Australia

The little island continent that escaped relatively unscathed... There are a number of risks that we face here in Australia, some of which are well documented, others less visible. I must admit that as I sat in Tetsuyas on Friday night I reflected that the recession must not have bitten too deeply. As a grateful guest of a VIP I was lucky to even have a seat in a restaurant that charges around \$200 for dinner (they are currently booked out until April 2010). I am pretty sure that the rest of the diners were employees of the big four banks, not because of their table manners, but because they have booked such fat profits in what is supposed to be the worst economic times since the 1930s. Here lies a risk for all Australians. We have entered a new era (or revisited an old one if you like) where the big four banks have almost no competition left. The RBA's ability to control monetary policy is softening as the banks manipulate interest rates to adjust their bottom lines. The inability of smaller banks to compete - thanks to K.Rudd - means that they are being gobbled up by the big four. In July, the big four captured almost 100% of new home loans which were in abundance due to government grants. Over the duration of the GFC we have seen Bankwest, Wizard, Rams and St.George (as well as Challengers' mortgage unit) devoured amongst others. Good luck trying to negotiate a home loan or a term deposit rate in the future....

**The Whiteley family holds a reducing number of big four bank products.*

China

China has had an absolute cracker of a year. Up to July, the Shanghai market was up around 70% for the year. Now, when we talk about bull rallies I would say that this one is up there with the best of them. However, with every boom comes bust and we have seen the market pull back close to 20% in August. I wouldn't call it bust, but it has brought a touch of value back to share prices. That being said, volatility is the core behaviour exhibited by a developing economy so you should expect to see more of it. China's future is brightening. We have seen indicators that China is cleaning up its act, moving from a country that has lost around \$86bn or 0.65% of its GDP per year on bribery and theft by officials and moving to the arrest this year of RIO executives for exhibiting similar behaviour - although I am unsure which Chinese Government Officials were arrested as well... Perhaps they just dislike losing at their own game?

In summary

I'm sure it comes as no surprise that there are still risks that we will face over the coming years - there always will be. There is also a lot of opportunity for the disciplined investor. Playing it safe never got anyone ahead of the pack, while taking calculated risks and playing it smart has often differentiated the winners from the losers. What the short term has to offer us will be forgotten well into the future.

Don't die wondering....