IAC update: October 2018

Six Park's Investment Advisory Committee (IAC) believes broad market fundamentals remain positive despite a likely increase in market volatility. There are legitimate areas of concern (see our watch list below) but, collectively, these concerns do not outweigh the tailwinds that support a positive market outlook for the next year.

Our IAC meets regularly to review exchange-traded fund (ETF) product selection, global market conditions, economic and political trends, the performance of our portfolios and asset classes, and how these factors impact our asset allocation and investment strategies that we provide for our customers.

We believe our professional human oversight separates Six Park from other robo-advice services and instils a unique level of trust with our clients while helping drive strong risk-adjusted investment returns (our growth portfolios returned 11.2% to 14.6% after fees for the 12 months ending August 2018).

Our algorithms use historical data to build portfolios with varying risk and return characteristics to suit our clients' risk appetites. However, on the relatively infrequent occasions when we see likely significant, long-term changes to market conditions occurring, the IAC will adjust our portfolios accordingly.

Market outlook

Generally, we view market conditions as fairly benign at the moment, and note an absence of two signs that typically suggest a "top" of an investment market cycle:

No significant asset price bubbles: Asset prices are arguably high in certain pockets, but there is not a broad-based asset valuation bubble along the lines of the internet boom or the sub-prime mortgage bubble that triggered the GFC.

No unjustified, broad-based investor exuberance: People are generally quite nervous about market valuations at the moment. It is typically when the taxi driver is handing out stock tips that one needs to worry about the unforeseen potholes that lie just ahead due to irrational market enthusiasm.

We believe that the global economy is the middle to late stages of a market cycle, and it is not advisable to adopt a more defensive investment position, which some of our competitors did in 2017, thus missing out on the gains of the past year. As such, the IAC advised Six Park against changing its asset allocation parameters at this time.

However, we note that the runway to the time when market conditions will justify a more defensive investment position is probably getting shorter, and there are several risks that could accelerate a portfolio reweighting towards more defensive asset classes.

There is no algorithm or predictive tool to accurately time unexpected geopolitics crises or an erratic Donald Trump, but investors should avoid premature investment tinkering until there are imminent signs of an exceptional market disruption. We do not observe these conditions at the moment.

Regional commentary

UNITED STATES

Strong corporate earnings, healthy employment data, and a lack of upward pressure on inflation numbers provide a positive backdrop for equities for the next year.

Second-quarter GDP 4%+, tax cuts and government spending, and strong consumer/business spending remain tailwinds for economic and corporate earnings growth.

The stimulus provided by tax cuts won't last forever and the pace of growth will eventually slow down but, subject to an unexpected disruption, we believe the most likely recession scenario in the US could play out in 2020 or beyond.

CHINA

Trade tensions represent a risk to Chinese markets, but we currently see an all-out trade war averted. Local authorities remain focused on growth drivers, with spending on infrastructure projects and the central bank's ongoing focus on providing stimulus for a soft economic landing. As such, we see a Chinese economic meltdown as a low risk to Australia's economic conditions.

AUSTRALIA

There will be necessary fixes to problems in the financial services market in the wake of the Banking Royal Commission; however, material legislative or regulatory changes are likely to take 12-18 months to unfold.

We view it as unlikely that such changes will fundamentally alter the way that the financial system functions in Australia.

A key area of focus is the possible contraction of bank lending, particularly if the housing market continues to soften as well. Such a tightening of lending standards could broaden a housing market decline and slow down the local economy.

Economic growth in Australia has been reasonably healthy and is expected to remain so through 2019 (2-3% GDP growth), underpinned by positive employment trends and ongoing modest inflation.

EMERGING MARKETS

Recent underperformance has been driven by currency and geopolitical volatility, as well as the ongoing prospect of rising interest rates.

However, we believe that the outlook for Emerging Markets is relatively benign and the recent pullback in this asset class has been a cyclical correction as opposed to the onset of a regional crisis.

Six Park's watch list

Watch list items are key risks that could foreseeably trigger market disruption.

- Impact of trade tariffs.
- The Federal Reserve: The Fed seems to have a steady hand on the tiller of likely incremental interest rate increases in response to a strengthening US economy. We monitor any signs that there could be an accelerated pace of rising interest rates, which could negatively impact share markets.
- Geopolitical risks in areas such as North Korea, Iran, Russia, Syria and Venezuela should continue to be monitored for any heightened destabilisation that could slow global economic growth.
- In Australia, we are primarily watching for any tightening of credit conditions and the prospect of a related property sector pullback. We also note rising consumer debt and lower consumer spending data in Australia as trends to watch as potential drags on future economic growth.

About Six Park’s team

Our team has more than 100 years' experience in the financial services industry, led by our active Investment Advisory Committee, made up of former JP Morgan Australia chairman Brian Watson AO, former Finance Minister Lindsay Tanner, and founding general manager of the Future Fund Paul Costello.

For more information, visit https://www.sixpark.com.au/about-us/advisors-team