

Act like McDuck, miss opportunities

PUBLISHED: 23 Feb 2011 12:03:05 PRINT EDITION: 23 Feb 2011

Philip Baker

When the global financial crisis hit it did more than just ruin retirement plans and portfolio values. It made investors wary about who to trust and ask why they had paid for expert opinions when so few of them saw the whole catastrophe coming.

As everyone now knows, most experts missed it completely. What other industry can pay themselves so well but throw their hands up in the air and say "don't blame us" when it all goes pear-shaped?

As a result, in the aftermath of the crisis, many managed fund investors were left, at best, flat-footed.

As part of the ensuing fallout, there's been a surge in the use of retail online brokers, while many investors are also taking matters into their own hands by managing their own superannuation.

The arrival of exchange-traded funds (ETFs) is another more cost-efficient way of playing the sharemarket.

The number of Australians trading online rose by 50,000 in the past year to a new high of 650,000 in 2010, according to the Investment Trends *Online Broking Report*.

But already that trend is showing signs of reversing. Commonwealth Bank of Australia announced a better-than-expected \$3.3 billion half-year profit, but also revealed a \$45 million decline in commissions at CommSec, its online broker.

Another trend that has hit the managed funds sector, and also had a considerable impact on other industries, is the flow of funds being poured into term deposits.

According to Deutsche Bank, households now have more cash and hold fewer shares than at any time in the past 15 years. It's clear that, after years of spending, Australians are now starting to save more.

In fact, according to Westpac Banking Corporation's chief economist Bill Evans, over the past two years the household sector has significantly increased its savings rate.

From negative savings rates in the first half of the past decade, the savings rate has now reached about 10 per cent – levels not seen since the 1980s, Evans says.

So, despite the boost from the resources sector that has helped Australia weather the crisis better than most, the upward spike in the savings rate means that consumer spending is now running well below trend.

"Explanations of the rise in the savings rate centre around the shock to households' sense of security during the global financial crisis, obvious concerns with extremely high debt to income ratios at a time when the mortgage rate has increased by more than 200 basis points and a sudden loss of momentum in housing markets," Evans says.

The burning question for investors is: what will happen to this savings rate over the next few years? Westpac reckons it's unlikely there will be any sudden drop in the rate.

"Uncertainty about interest rates, house prices and discomfort with debt levels will see households remain cautious. The recent natural disasters have unnerved households and our consumer sentiment survey shows they are particularly worried about their own finances," Evans says. "Reports that house prices are falling in some areas are likely to further raise households' concerns.

Within our economy, there's little doubt that one of the biggest questions relates to consumer behaviour.

Australian consumers report being more optimistic about the future but they are now so cautious they have increased their savings rate even more than the Americans.

The Reserve Bank of Australia welcomes the cautious behaviour of households and officials say the economy does not have sufficient capacity for both investment in the resources sector and consumption to grow strongly at the same time.

That might mean the official cash rate stays at 4.75 per cent for quite some time.

KEY POINTS

- Australian consumers are optimistic, but they are cautious as well, and saving more than their US peers.
- If households keep showing the same spending restraint, they will be doing the RBA's work for it.
- Once bitten, twice shy investors may miss out on what looks like a record year for the S&P 500.
- Share valuations are reasonable, the price-earnings ratio is below long-term averages, and the US recovery is looking stronger.

If households keep exercising restraint, they will be doing the RBA's work for it.

But if everyone gets too conservative there could be investment opportunities that are being missed.

People have been so burnt they could risk missing the cyclical recovery and an epic earnings recovery. For some experts it looks like 2011 could be an earnings record for the S&P 500.

Over the past few months global sharemarkets have made decent gains and measures of investor sentiment are running at high levels.

February is seasonally not such a good month for shares as investors normally get a little gun-shy after being positive at the start of the year.

As a result, there is a risk of a short-term correction or consolidation in the sharemarket, but any pull-back might best be viewed as a buying opportunity because the fundamental backdrop for shares is positive.

Valuations are reasonable, the price-earnings ratio is still below long term averages, while there has been some better-than-expected data released in the world's largest economy, implying the United States economic recovery is looking stronger.

The global liquidity backdrop is very favourable and the low interest rates in most major countries are expected to stay that way. The corporate sector is cashed up and investors are only just starting to switch from bond funds into share funds.

One issue for many investors is that they also tipped money into bonds while the crisis was in full swing. Now that the recovery is under way, bond yields have soared in recent months but are still below longer-term sustainable levels and bond funds are now starting to see some outflows as investors gain more confidence.

The Australian Financial Review

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