

# MONITOR



## Uncertainty Prevails

Many media reports refer to the current unprecedented level of uncertainty in global financial and debt markets. But is it really unprecedented?

Not really. Of course, each new “crisis” or risk is perceived as being unique. And often they are, at least if you are only using the last couple of decades as a guide. Since the equity market bottom in March 2009 (GFC part 1) our market has had to deal with several unprecedented global risk events. It was less than six months ago that it was feared the uprisings in the middle east could lead to a major global equity market sell off. Temporarily it did. But this highlights how quickly market sentiment and focus can change. When you are in the eye of the storm it seems like things will never calm down. But they always do.

At present, there are numerous uncertainties leading to global risk aversion. This in turn leads to falling equity prices and falling global bond yields (rallying). The slowing US economy and the risk of a double dip recession have some market watchers concerned about the outlook for company earnings over the next year. This uncertainty leads people to question the relative value of shares if the “E” in P/E is sustainable or vulnerable to falling (P/E—Price to Earnings Ratio—the relationship of a share price to its forecast earnings).

The cause of greater uncertainty at pre-

sent is Euro zone sovereign debt issues and the flow on effect this could have on European (and global) banks that own much of the debt issued by these countries. Specifically Greece is of most recent concern. The chart overleaf shows what likelihood the (debt) market is placing on each of the PIIGS (Portugal, Ireland, Italy, Greece and Spain) defaulting on their debt.

As you can see, it is all but a fait-acompli that Greece will default according to current market pricing of their bond yields.

The European Central banks, and now global central banks, have attempted to pump liquidity into the Euro zone system in a move to try and buy time for the PIIGS to get their balance sheets in order. However, it seems the market is viewing these attempts as merely band aid solutions, as evidenced by the market expectations on the overleaf chart.

So if the markets expect Greece to default and Portugal a better than average chance to default one might ask why is this causing so much risk aversion if it is in effect already “known” by markets. The answer is, no one is prepared to take too big a risk until the outcome of a default is known. Everyone fears the “C” word - Contagion. If Greece defaults and the value of its bonds (debt) has to be written off by other Euro zone countries or written down by banks that hold Greek debt,

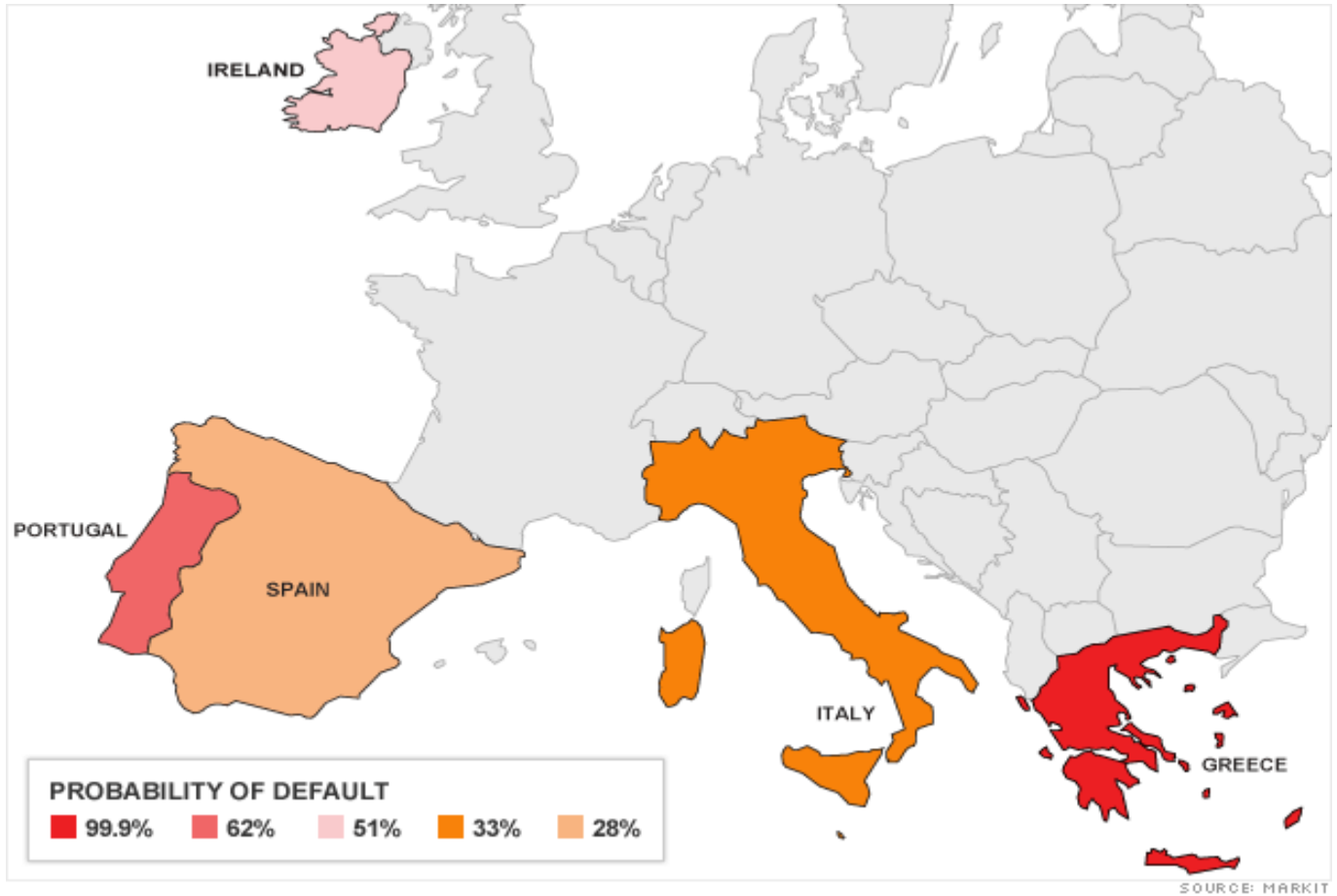
everyone fears a contagion will take over like we saw during the GFC when everyone was too scared to lend to one another (as banks rely heavily on inter bank lending).

Markets hate uncertainty and that is why they have been drifting lower. With US and German 10 year bond yields at near all time lows, debt markets are telling us to be cautious. Hence a higher level of cash holding is currently warranted.

However, we feel the time is shortly coming when at least some of this cash must be re-deployed into companies with sound balance sheets, dependable earnings, growing dividend streams and structurally sound industry macro dynamics.

Remember, no one rings a bell at the bottom of market sell offs. New bull markets are born out of pessimism, not euphoria. If buying makes you feel a little sick in the stomach then it's most likely you are doing the right thing. If not with a one month view, its highly likely with a twelve month view you're right.

Human nature is to be optimistic. This is one reason we came through the GFC (part 1) strongly. FOMO 'Fear of Missing Out' will again takeover shortly and appetite for risk will return with a flourish, leading to higher share prices at some stage over the period ahead.



## CHECK OUT OUR NEW VIDEO!

We have put together a bit of a fun, animated, short video to introduce who we are and what it is we do. It can be found on the home page of our website.

If you can spare 3 minutes to watch this please do so. And of course, please feel free to forward the link onto any family, friends or colleagues that you think may be interested in hearing a short story on what we do.

[www.martinbros.com.au](http://www.martinbros.com.au)

## DAYLIGHT SAVINGS

Remember daylight savings starts on Sunday 2nd October at 2am.

Don't forget to move your clocks forward one hour.



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