	Price	5 Day % Change	3 Month % Change	1yr % Change
S&P/ASX300	65,003	1.18%	9.06%	11.82%
MSCI World Ex-Aus. (Unhedged)	9,802	-0.59%	11.05%	14.24%
MSCI World Ex-Aus. (Hedged)	1,747	0.28%	11.06%	7.99%
Bloomberg AusBond 0+ Composite	9,832	0.12%	2.87%	6.91%
BloombergBarclays Global Agg. (Hedged)	1,011	-0.05%	2.23%	4.33%
S&P/ASX300 Property	55,011	2.24%	8.91%	24.56%
FTSE/Epra NAREIT (Hedged)	2,809	-0.20%	9.79%	16.02%
S&P Global Infrastructure (Hedged)	5,222	-0.05%	10.38%	12.72%
BarclayHedge Global Hedge Fund Index (USD)	5,667	N/A	2.09%	-1.03%
AUDUSD	0.7173	0.96%	-0.33%	-7.49%
AUDEUR	0.6349	0.22%	1.17%	0.91%
AUDNZD	1.0606	0.45%	0.54%	0.87%
AUDGBP	0.5487	0.69%	-1.94%	0.67%
AUDJPY	80.3420	1.20%	3.12%	-3.60%

Source: Bloomberg, S&P Dow Jones, MSCI, FTSE/EPRA, Barclays, 14th April 2019

The official sector grabbed most attention last week as the IMF downgraded its economic growth forecasts, the ECB met, the Federal Reserve released the March minutes, and the RBA published the Financial Stability Review.

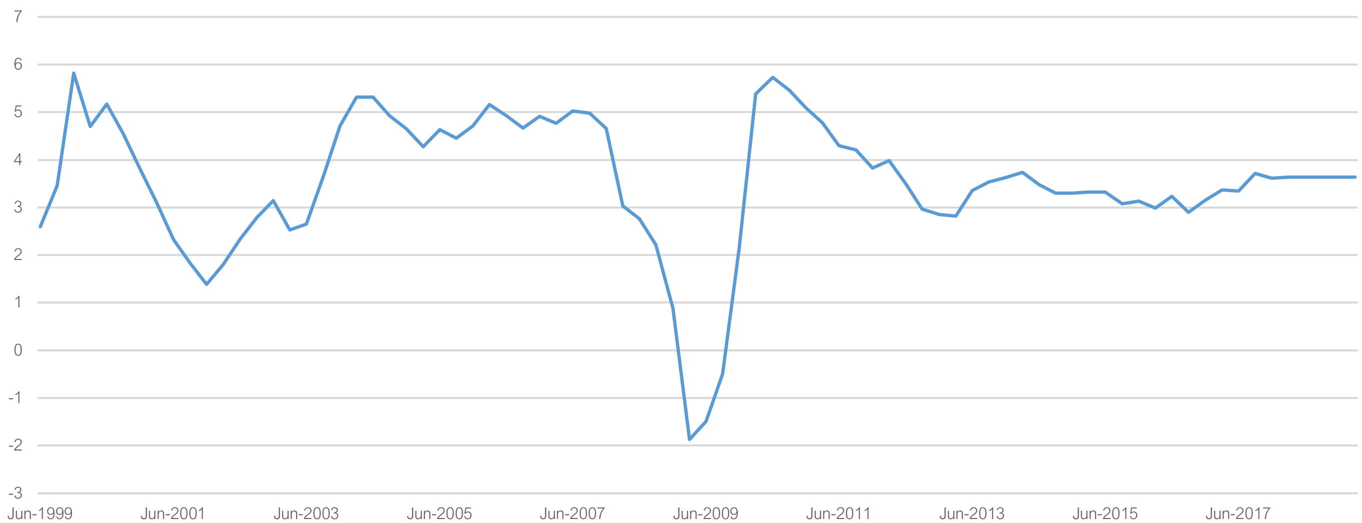
The EU agreed to allow the UK until 31st October to agree on a Brexit solution, greatly reducing the chances of a “no deal” Brexit and an accompanying economic shock. Global data has also improved slightly over the last couple of weeks. As a result, global bond yields have risen, and the chances of US interest rate cuts have receded.

This week we discuss skew in some of the potential downside risks to the Australian economy stemming from household debt and leverage, illustrated in the FSR.

Last week we learned that Australia will head to the polls on Saturday 18th May to decide who gets to be Prime Minister, for a little while at least. The US quarterly earnings season kicked off on Friday, but official institutions mostly held the limelight.

The IMF downgraded its global growth forecasts this year. After softening to 3.6% in 2018, growth is expected to slow to 3.3% in 2019 as approximately 70% of the countries see slower growth. Growth is expected to pick up the second half of the year and reaccelerate to 3.6% in 2020, due to a high degree of monetary accommodation allowed by generally low inflationary pressures.

This outlook is generally positive for earnings. 3.3% is not materially slower than the average since 2012. But investors should be aware that the full extent of the slowdown in the first half of 2019 is not likely to be reflected in earnings until mid-to-late 2019, and the IMF itself is careful to highlight the fragility of the reacceleration. In other words, downside risks remain elevated.

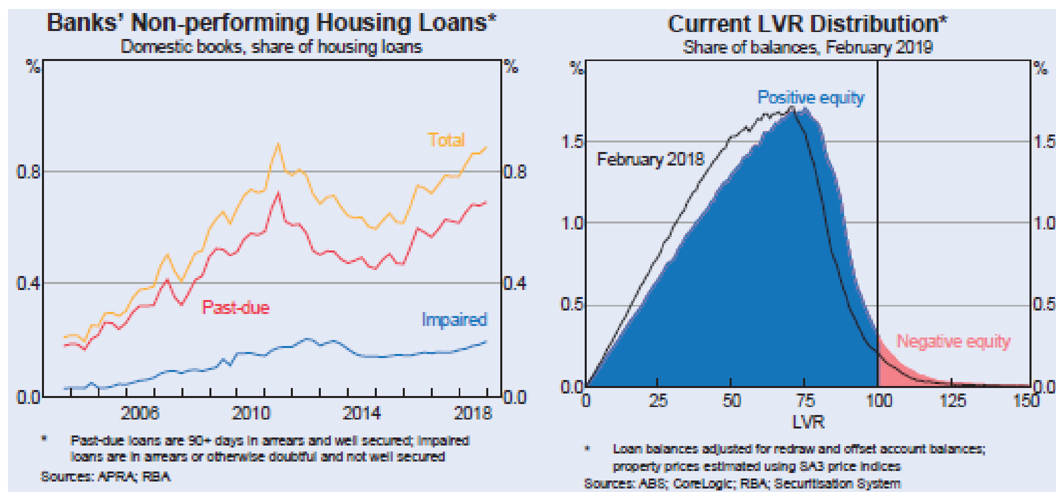


Source: Bloomberg, ABS, 14th April 2019

The wariness of "downside risks" was echoed in the RBA's Financial Stability Review on Friday. The Reserve Bank acknowledged a slowing international and domestic growth impulse, and the high levels of household debt, but was relatively comfortable with the outlook as most households had some buffer to be able to service debt. Even in the case of a deterioration, the financial system is now more resilient than it used to be.

On (Sydney and Melbourne) house prices:

"It is unusual, in Australia and internationally, for property prices to be falling while interest rates and unemployment are low. The prevalence of negative housing equity is low, but substantially larger price falls would see a large share of households' housing equity eroded or even turn negative. This would increase the risk of costly defaults for lenders if unemployment were to rise. Further price falls could also increase lenders' perceptions of the riskiness of housing lending, compounding the somewhat tighter availability of credit seen to date. Greatly reduced credit supply would be detrimental to the economy and so financial stability".

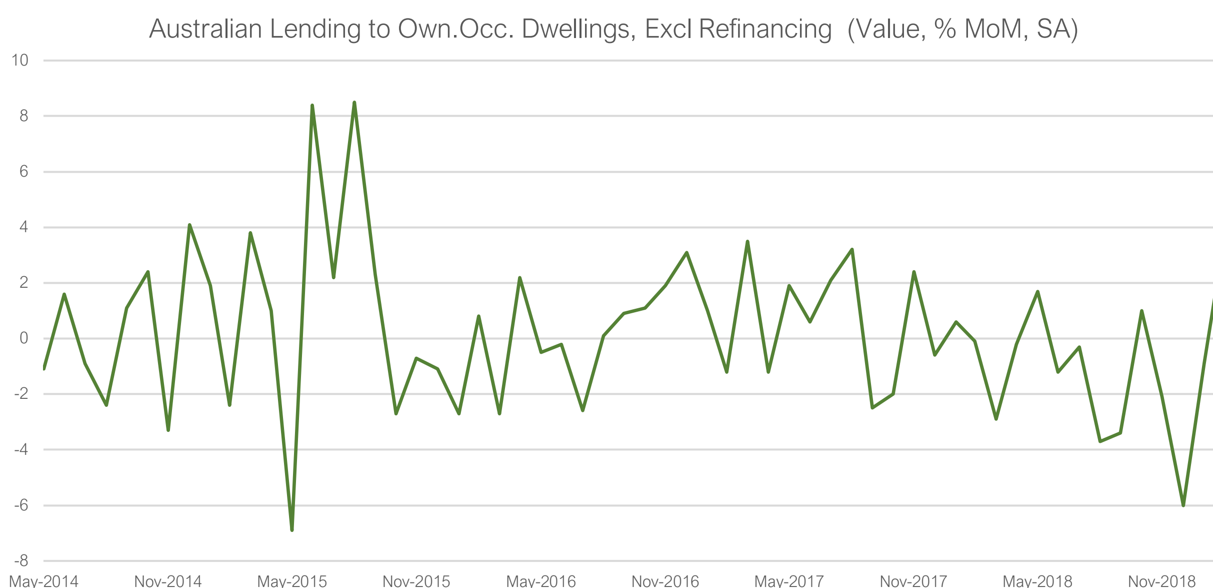


Source: RBA, Financial Stability Review, April 2019

That really is the issue – the nature of the housing market and high leverage means that the situation does not gradually deteriorate forever. Things are ok, until they are not, very suddenly. For example, the “sharkfin” profile above shows the high volume of mortgages around the 75% LVR point. As house prices decline, the sharkfin moves to the right and the number of homeowners in negative equity increases not gradually, but dramatically.

Providing that households can continue to grow incomes through employment and wages, the problem can be avoided. House prices generally will rise. But if household incomes deteriorate, and arrears mount up, credit gets turned off, and the problem can escalate quickly into a severe recession.

The unemployment rate is holding firm at around 5% (where it is expected to be for March when released on Thursday), with some recent improvement in the underemployment rate. But ANZ job advertisements continued to decline last week, suggesting a weaker outlook. Wage growth is low and sticky. Nevertheless, there are signs that there may be some support for the housing market. Last week saw the value of new owner-occupier loans increase 3.4% in February (see chart below). And given that the change in house prices is the driving variable when it comes to negative equity, the situation appears to be ok for the time being but should be closely monitored.



Source: Bloomberg, ABS, 14th April 2019

The ECB last week also discussed the fragile growth outlook, maintain a very stimulatory stance and guidance.

The EU granted the UK an extension up until October 31st to achieve a domestic agreement on Brexit, as cross-party talks continue. There is no guarantee that a deal will be reached and very little clarity on what the deal might look like. But the chances of a negative shock from a “no deal” Brexit have dropped to near zero from being, officially at least, the default option.

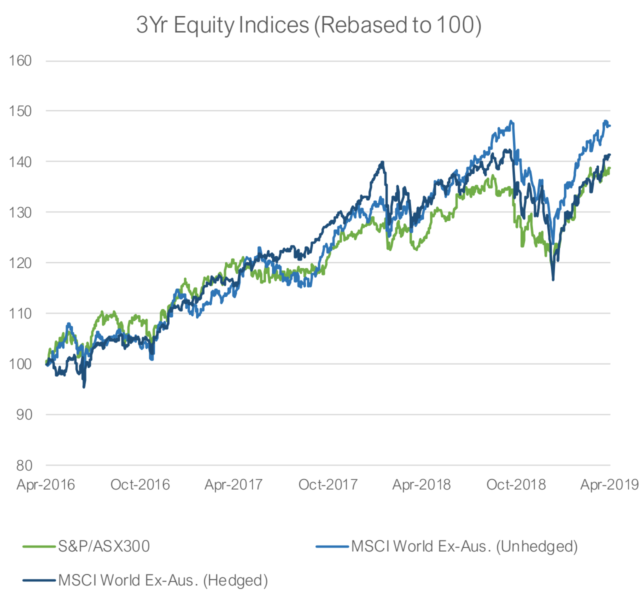
In the US, market pricing of the Federal Funds interest rates has seen the chances of a cut decrease dramatically in the last two weeks, from roughly 80% to 50% by the end of January.

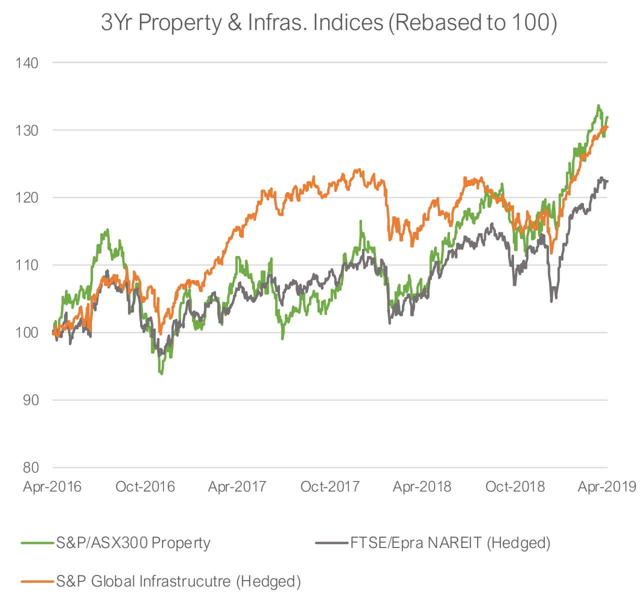
The minutes of the Federal Reserve March meeting that were published last week offered little new information. The change is more likely to due to a combination of factors that include generally better employment data, a slightly firmer CPI reading of 1.9% YoY, the rebound in Chinese manufacturing and a reduced threat from trade disputes and Brexit.

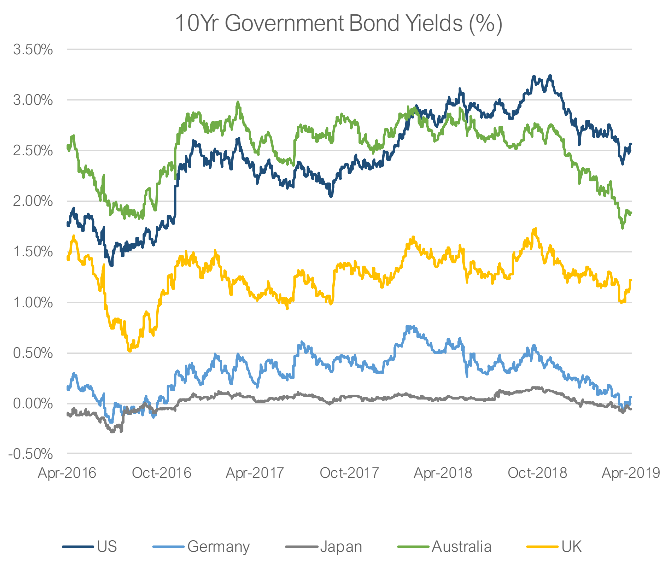
Bond yields also rose, but only back the levels consistent with the more gradual declining trend of January and February. There is no apparent reacceleration in growth or inflation yet.

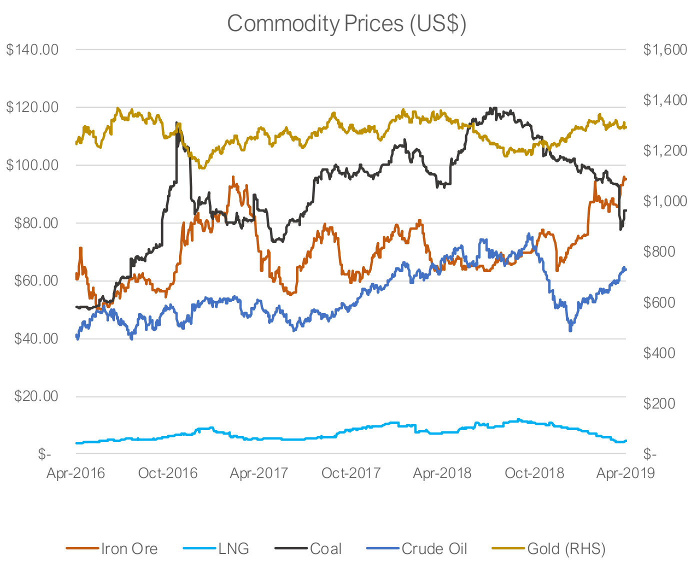
Significant Upcoming Data:

	Monday	Tuesday	Wednesday	Thursday	Friday
Australia		RBA Minutes		Unemployment	
US	Empire Manufacturing	Industrial Production	Mortgage Applications; Trade Balance; Wholesale Inventories	Markit PMIs; Retail Sales; Philly Fed; Leading Index; Business Inventories	Housing Starts; Building Permits
Europe	Finnish CPI	ZEW Surveys; UK Unemployment	Eurozone, Italian & UK CPI	Eurozone, French & German PMIs; UK Retail Sales; Swiss Unemployment	Italian Manufacturing & Consumer Conf.
Japan		Tertiary Ind. Index	Industrial Production; Trade Balance		National CPI
China			GDP; Ind.Prod.; Fixed Asset Inv; Retail Sales		









Source: Bloomberg, S&P Dow Jones, MSCI, FTSE/EPRA, 14th April 2019

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