



GATEWAY INSIGHTS

March 2011

24 Investment Bubbles - Markets Summit 2011 Key Takeouts

Investment bubbles will always be a hotly debated topic amongst the global investment community. There are often discussions that there may be significant bubbles building in the global economy. Do you agree or disagree that this is the case at the moment? Last month Gateway attended the PortfolioConstruction Forum Markets Summit on this issue 'Bubble, Bubble – toil and trouble?'

Notwithstanding the fact that the world has changed considerably with regards to investment markets since then – with the Japanese tragedy and continued conflict in the Middle East - Gateway thought it would be worthwhile recapping on what some influential industry figures had to say about potential current asset bubbles, and what impact they may have to take into consideration when constructing sound investment portfolios for investors.

Background

The question of what is a 'bubble' was used to open the Summit. Professor Niall Ferguson addressed this by saying, via video address, that in his view a bubble is "any asset group that becomes so significantly overpriced compared to fair value that it must certainly eventually fail, and suffer a dramatic reduction in price for a long period of time".

So the big question, put by Graham Rich, CEO of Brilliant and the PortfolioConstruction Forum, to the audience and guest speakers was, as it stands today, "is there any sign of bubbles?"

A macro perspective

Professor Niall Ferguson, Dr Pippa Malmgren and Dr Bob Baur, MD & Chief Economist at Principal Global Investors all were asked to set the scene for the day's debate. Whilst each naturally had their individual perspectives, the one view that they did agree on was the risk of inflation. Dr Malmgren warned of inflation in Emerging Markets and its on flow effect to global markets, and Professor Ferguson echoed

this, but also noted that global Commodities are possibly in the same position. Therefore could both these asset classes be in bubbles right now?

Whilst there was a lot of talk about the significant risk of inflation, Dr Baur shared his opinion that we are now in an 'expansion' phase. His view is that the recovery is over and we have moved into an expansionary phase, because of the strength of the 'fundamentals', and therefore we must adjust portfolios accordingly. Not a view shared by all the audience!

If you'd like to read more about Bob Baur's 'fundamentals' which talk about profit growth, the resilience of Europe, and the Emerging Markets growth story please refer to the reference at the end of the Insight¹. For good measure Dr Baur went through the risks that could unbalance the expansion – not surprisingly they included, Middle East uncertainty! Other risks included:

- Double dip of US housing
- European debt crisis
- Chinese real estate bubble
- Chinese monetary policy
- US debt

Australian story

One of the most intellectually challenging parts of the day was the inclusion of a speaker from academia, Dr Steve Keen an Associate Professor from the University of Western Sydney. Steve was not nearly as bullish as Dr Baur! The key focus of his message was around the effect, in Australia, of the First Home Owner's Grant, both since its inception and its recent doubling as a stimulus boost. Back to bubbles – his point was that this scheme has caused a massive housing bubble in Australia. Also on bubbles, he believes the China story will end and Australia having all our eggs in one basket will be the recipient of a good lesson in diversification. Steve was challenged by Chris Joye, the Managing Director from Rismark International which made for the best debate of the day. Chris' view was that it is ridiculous to suggest that Australia house prices could fall by 40% and that therefore the Australian housing market is not in a bubble. Do you agree or disagree?

¹ Markets Summit 2011 Communique by BlueChip Communication Group

Bringing it all together - portfolio construction implications

With lots to think about - Joe Bracken, Head of Macro Strategies for BT Investment Management, was asked to provide the audience with a base case asset allocation for a medium risk profile and capital accumulation investor. Joe's answer was to implement a 3 step approach to avoid being burnt by potential bubbles. It is summarised below.

- 1. Include bonds, equities and absolute return funds ie. a good mix of betas and absolute returns gives diversification**
- 2. Allocate equally between the asset classes – the rationale here was it protects against inflation as it avoids excessive weighting of any one asset class**
- 3. Add some short term views in if appropriate**

Summary

This Insight does not do justice to the quality and quantity of speakers that went on to present throughout the Market Summit. They were highly knowledgeable, interesting, informative and encouraged lively debate. The key takeouts for Gateway were that:

- global markets are recovering but there are many risks that still cannot be overlooked
- the existence of bubbles and their appearance in various asset classes will continue to be a source of debate and argument
- portfolio construction remains a critical issue for our industry – for advisers and their clients and for fund managers who need to know how and where their offering fits in

References:

Markets Summit 2011 Communique by BlueChip Communication Group

[About Gateway](#)

Gateway Financial Marketing (Gateway) was established in February 2004 by Amanda Rethus and Edwina Best for the purpose of offering fund managers, other product providers and international new entrants, expert advice, services and assistance in negotiating entry into the Australian Retail Financial Services market. Use of Gateway's services provides the opportunity for clients to overcome the hurdles that can often confront fund managers when transitioning from institutional to retail and hence improve participation in retail funds flow. Prior to Gateway, Amanda and Edwina spent over 30 years combined with major institutions in the Retail Financial Services market.

Our qualifications

Amanda has over 20 years' experience in the Financial Services industry and was formerly a Divisional Director in the Financial Services Group of Macquarie. Amanda managed investment portfolios for over 10 years, and has spent in excess of 10 years introducing investment products to the Australian Retail market.

Edwina has a Bachelor of Business from UTS majoring in Marketing and International Business. She has over 12 years' experience in the financial services market, concentrating in relationship management, product management and marketing. They both have extensive contacts in the retail financial services market especially with key decision makers.

If you would like to confidentially discuss your current approach to the retail market or have any questions on the above please do not hesitate to contact us on – Edwina 0404 046 179 or Amanda or 0414 658 323.