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Welcome to the HouseBulletin.

We would like to take this opportunity to thank you for your past support and look forward to welcoming you to our new offices.

Investment Overview

Is this a Bear Market?

There is much debate on whether the US, in particular, has entered a bear market phase as evidenced by the recent falls in equity prices.

Does it look like a bear market or is this a new paradigm?

Last year's equity slide at least could be attributed to economic weakness, but this year's decline has come through the first phase of an economic recovery, albeit weak, which is usually the best of times for equity investors.

So what is going on?

The extreme share valuations during the 2000 year have already been factored into the slide on Wall Street – a case in point - a company whose stock has fallen 70% need not be cheap as evidenced by some technology stocks on the NASDAQ. Also factored into the turmoil are the recent cases of inadequate corporate governance and questionable accounting practices.

So did you hear the story about the blue chip company that reported a better than expected earnings result and was crucified. It sounds strange that when a company delivers positive news investors sell the stock. But this is the situation at present in the US. In essence, investors have lost confidence in the market – the new paradigm?

Investors are not convinced by the good news coming in this reporting season. They need much more incentive to return to the equity market in the short term. Where that incentive will come is the \$64 question. For those investors who are cashed up, the horizon presents an exciting opportunity. For those that are invested – it is no time to sell especially if they are holding quality investments.

Renowned technical chartist, David Fuller sees that most stock markets have been deeply oversold and that there has been more capitulation selling with the Federal Reserve probably intervening. His view is that there could be a medium term rebound but the final low could be years away. His argument is that the stock markets will remain rangebound for a very long time. That is, a series of medium term recoveries, such as we saw from late September to January, followed by bigger sell offs.

What are the risks?

While most analysts anticipate further advances in share markets, we acknowledge that risks to the outlook remain high. Risks include:

1. Ongoing accounting concerns in the US leading to a major cut in the level of US earnings estimates.
2. The US corporate accounting scandals engulfing major investment banks and triggering a systemic financial crisis.
3. The US economy falling back into recession due to the loss of wealth and blow to confidence from the fall in share prices. For most US households, house prices are more relevant and they are rising. The greater risk relates to the impact on corporate business investment.
4. A US led invasion of Iraq creating increased uncertainty and fear of a major Middle East versus West conflict.

5. Share markets come back and test the low of last week: a classic double bottom. This has been a normal phenomenon at past cyclical lows.

So where to from here?

While it is premature to say that we are out of the woods, investment analyst's assessment is that there is further upside in share markets over the next 6 to 12 months. Firstly, shares remain cheap relative to bonds. A comparison of the forward earnings yield on stocks with bond yields suggests that UK and European share markets are still more than 20% undervalued. The Australian market is about 14% undervalued.

Many now contend that price earnings (PE) multiples for US shares (now around 20 times historic operating earnings) are still too high relative to their own very long-term average (which is around 15 times historic operating earnings) to permit any meaningful rally.

Secondly, the global economic recovery remains on track albeit slow and this should be positive for corporate profits. In fact the current US reporting season for June quarter results has so far proved quite solid with 61% of companies so far reporting better than expected outcomes.

Thirdly, liquidity conditions in the US are starting to improve.

Sector Outlook

Cash

Due to the long-term poor return characteristics of cash, we prefer to value cash as an alternate asset class. Stated differently, we prefer to value cash as a parking spot

Fixed Interest

All government bonds, Australian included, appear significantly overvalued. As investors have been positioning towards defensive asset classes, valuations within government bond portfolios have worsened by moving into what we would consider significant overvalued positions. As such, we recommend investors remain noticeably underweight this asset.

We are recommending investors seek exposure to corporate debt. The massive premiums between corporate and government debt offer good opportunities to investors.

Property

We continue to believe that property trusts offer a good alternative to bonds for those investors seeking a high-income stream. Dividend yields are around 8.0%. Furthermore, unlike bonds, the income stream on listed property grows as profit grows (albeit at the rate of inflation as rents typically grow by the greater of 5% of CPI). Australian listed property trusts are still attractive at current levels.

Australian Equities

Shares continue to appear as the preferred asset class, especially when compared to domestic bonds and international assets. Within the broader market, bank shares are looking increasingly overvalued when compared to the rest of the market. Given the four majors represent over 20% of the index, the large cap stocks are once again skewing valuations.

Australian shares should provide good returns from current levels. Given their greater defensive exposure and outperformance through the downswing, they will probably underperform global share markets during the upswing. However, the local share market comes with lower risk which, as we have seen over the last two years, is not necessarily a disadvantage.

International Equities

International shares continue to appear as significantly overvalued. Much of this overvaluation however continues to be influenced by large cap stocks. As is the case domestically, medium to small cap international stocks are preferred to larger cap issues and securities.

We expect global shares to stage a cyclical recovery over the next 6 to 12 months. It needs to be emphasised that the risks remain significant, particularly for the US share market, and will need to be closely monitored.

Legislative Update

1. What is law

Details of Law	Date of effect	Who is impacted?
<p>Super contributions for people aged 70 or more</p> <ul style="list-style-type: none"> Measures enabling personal contributions to be made by people aged 70 to 74 inclusive (along with related changes to compulsory cashing rules) 	1 July 2002	Certain individuals aged 70 to 74 inclusive
<p>Superannuation divorce measures</p> <ul style="list-style-type: none"> For the first time couples will be able to divide their superannuation interests on marriage breakdown in the same way as their other assets. The legislation will also allow couples to make binding agreements, stating how their interests are to be divided in the event of divorce. 	28 December 2002	Divorcing members of superannuation funds

2. What has been released but is not yet law?

Details of proposed measures	Date of effect	Who will it impact?
<p>Choice of fund</p> <ul style="list-style-type: none"> These measures are for the purpose of introducing changes to the Super Guarantee legislation such that employer will be required to offer employees a relatively unlimited choice of fund to which the employer will make SG contributions. 	1 July 2004	Employers and employees generally

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