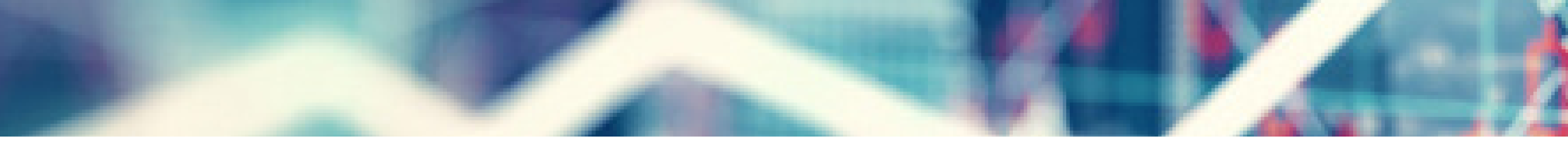
22 January 2019

Investment Market Conditions UPDATE

Summary of key points

- Since New Year, equity markets have recovered some of the steep decline that occurred in the December quarter of 2018. Both the decline and the partial recovery have been driven by shifts in sentiment rather than much in the way of major change in economic conditions, although significant economic change may be on the way in the next two years. The shifts in sentiment have been driven by reactions to statements by political leaders such as Trump and Xi, and policy makers such as central bank chiefs Powell and Draghi.
- Trump escalated the rhetoric on the trade dispute with China before reaching a truce on new tariffs until 1 March, to allow for a negotiation of some sort of settlement. Markets remained concerned about the fragile nature of the truce and the potential for a resumption of trade hostilities which could cause a major slowdown in economic growth worldwide.
- Chairman Powell of the Federal Reserve merely repeated the long-standing position that the Fed would increase short interest rates further in 2019 and continue to not replace the $US 50 billion of bonds that are maturing each month, thereby continuing the process of quantitative tightening. This prospect of an ongoing reduction in liquidity heightened concerns for many investors that it may become too difficult to adjust their allocation to equities as we progress into 2019 and 2020 and approach the next recession. Many promptly shifted funds from equities to bonds with the effect that the US ten-year bond yield declined even though an increasing supply from the US Treasury (to fund the fiscal deficit) is being met with reducing demand from central banks.
- With the exception of the self-inflicted wound that is Brexit, Trump is a common factor in most of the dramas that are concerning investors: US-China trade negotiations, US Federal finances and the government shut down, the independence of the Federal Reserve and its interest rate policy, the increasing scale of US bond sales. We do not expect the disruptor-in-chief to depart the scene nor change his modus operandi any time soon. Short run equity market volatility will remain the norm for some time to come. This will include some useful bear market rallies in 2019, which will allow investors to reduce the allocation to equities if they wish to, at better than expected prices.



Summary of key points cont...

- While the shape of the yield curve, a good forward indicator of recessions and downturns in equity markets, has flattened, it has not yet inverted or turned negative and so it is not yet signaling recession or a more severe equity market downturn.
- While the equity markets are better than fairly priced from a longer-term point of view and, both monetary and fiscal policy are still supportive of economic growth as well as financial asset prices, equity market momentum has definitively turned negative. More significant falls are quite possible over a shorter-term horizon out to three years.
- While the very short-term outlook for equities may be better in recent weeks, the medium-term case is being weakened by three sets of factors:
    - Firstly, growth in GDP and in earnings per share are likely to slow as the effect of the trade dispute impacts volumes of trade and global supply chains. The recent downgrades in revenue outlook for both Apple and Samsung are a foretaste of a wider slowdown over the next year or so.
    - Secondly, notwithstanding recent falls in bond yields, the sheer volume of borrowing needed by the US government combined with the retreat of major central banks from holding bonds, will eventually push up the long-term bond yields, reducing the value of future cash flows from investments and with it the prices of financial assets.
    - Thirdly and most importantly, central banks have shifted from quantitative easing to quantitative tightening (QT). The tide of monetary support for asset prices is turning, albeit gradually over the next few years. By itself QT may not produce a recession, but it will impact financial asset prices, just as the effects of QE went mostly into asset prices rather than economic growth between 2009 and 2018.
    - In such conditions, investors with a shorter horizon of one to three years will feel more comfortable reducing their equity exposure. This may best be done during the periodic rallies in prices which will occur during a period of increased market volatility which we are likely to see in 2019.
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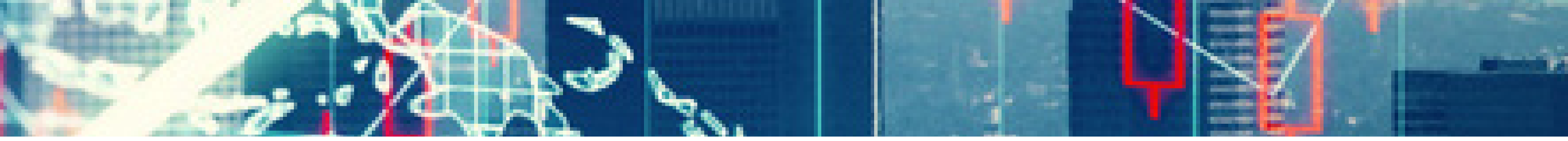
- Investors with longer term horizons and an ability to tolerate equity market downturns and await the recoveries that follow, should remain invested at benchmark or neutral weight in equities, but be aware that there may be further falls of up to 20% in the next two years. Some longer-term investors may want to consider the opportunity of using short term rallies to move some of their portfolios into cash pending reinvestment at lower prices after subsequent market declines. It is important to remember that it is very difficult to get both legs of such market timing moves right.



Portfolio investment strategy for investors with a longer-term horizon of five years or more

- For longer term investors with horizons of five years or more, which would take them beyond a major downturn and recovery episode, keep a neutral or benchmark weight to Australian equities and International equities. Stay invested for the recovery.
- Stay short in interest rate duration in fixed interest to avoid capital losses as bond yields increase.
- Avoid traded securities with credit risk, as credit spreads are too tight to offer adequate return for risk.
- Hold a major underweight to AREITs (Listed Property Trusts) and be selective about unlisted property assets – minimum yield of 6% p.a., weighted average lease expiry (WALE) longer than the life of the fund or trust, maximum debt of 45% of gross assets, good tenants, and great managers with a proven track record.
- In the longer run beyond the next year or so, the prospects are for greater increases in short term interest rates in the USA relative to interest rates in Australia. This means that eventually the AUD is more likely to fall than rise against the USD, so international investment on a three to five-year horizon should be unhedged.
- Overweight cash and well managed alternative equities which have a proven capacity to make asset allocation shifts in response to evolving market conditions

Table 1: Recommended asset allocation positioning for portfolios for investors with a longer-term horizon of five years or more:

RECOMMENDED ASSET ALLOCATION RELATIVE TO BENCHMARK OR NEUTRAL:	ZERO	MAJOR UNDER WEIGHT	MINOR UNDER WEIGHT	NEUTRAL OR BENCHMARK WEIGHT	MINOR OVER WEIGHT	MAJOR OVER WEIGHT
Asset Class						
Cash					X	
Fixed interest			X			
Property		X				
Australian equities				X		
International equities				X		
Alternative equities					X	

For investors with a shorter-term horizon of one to five years:

- Reduce the allocation to Australian and International equities to between 60% and 80% of benchmark or long-term strategic asset allocation in Australian and/or International equities. This could be implemented by selling into rallies in the next six to twelve months, which can be expected in volatile market conditions;
- In fixed interest, stay short in credit duration and in interest rate duration
- Stay well underweight in listed property securities (AREITS and GREITS)
- Overweight cash and well managed alternative equities which have a proven capacity to make asset allocation shifts in response to evolving market conditions.

Where are we now?

Table 2: Financial market movements - financial year to date

Market indicator	Level at 31/12/2017	Level at 18/12/2018	Level at 9/01/2019	Change since 18/12/18	
				In local currency	In AUD
Equity Markets					
S&P ASX 200	6065	5582	5774	3.4%	3.4%
USA: S&P 500	2673	2545	2547	0.1%	0.5%
UK: FTSE 100	7687	6773	6861	1.3%	2.8%
Germany: DAX	12917	10772	10803	0.3%	1.7%
France: CAC	5312	4799	4773	-0.5%	0.9%
Japan: Nikkei 225	22764	21214	20457	-3.6%	0.4%
China: Hang Seng	29919	26087	26352	1.0%	1.5%
Currencies					
USD/AUD	0.7805	0.7186	0.7154		0.4%
GBP/AUD	0.5731	0.5697	0.5616		1.4%
YEN/AUD	87.92	81.01	77.84		4.1%
EUR/AUD	0.6501	0.6334	0.6244		1.4%
Interest rates % p.a.					
Aus: 90 day bank bill	1.78	1.98	2.05	7.0%	
Aus: 10 year govt bond	2.67	2.42	2.35	-7.0%	
US: Fed funds rate	1.42	2.19	2.40	21.0%	
US: 10 year govt bond	2.41	2.85	2.73	-12.0%	
Commodities					
Copper US $ per tonne	7247	6123	5906	-3.5%	-3.1%
Gold USD/ounce	1302	1246	1287	3.3%	3.8%
Oil USD/barrel (WTI)	60	49	51	2.3%	2.7%

- Equity markets have bounced back partially since the severe sell off in the December quarter. The falls in equity markets had taken place against a back drop of firm economic and earnings growth, low unemployment in the USA and interest rates that were still low by historical standards. The downwards shift was driven almost entirely by a shift in investor sentiment which was disrupted and disturbed by statements of key decision makers, including primarily President Trump and Fed Chairman Jerome Powell.
- Equity markets weakened a lot in the week before Christmas due to investors reacting to concerns about the US-China trade dispute and the apparent lack of concern by the Federal Reserve about the monetary tightening effect of its policy of not replacing $US50 billion per month of bonds that are maturing (QT).
- Since New Year equity markets, except for Japan have since recovered as both areas of concern appeared to take a turn for the better. Firstly, the US and China reconvened talks on settling the trade dispute. Secondly, the Chairman and Deputy Chairman of the Fed both indicated that the Fed "would not hesitate to suspend QT if the circumstances deteriorate." This appears to have started a rally which may run for some weeks, at least until there is another policy maker induced short term panic.
- Since mid-December, interest rates at the short end of the yield curve rose in the USA following the decision of the Federal Reserve at its December meeting to increase the Federal Funds Rate by 0.25% p.a. The Fed

Where are we now? cont...

also indicated that it may increase this rate once or twice in 2019 although the US Fixed Interest Futures market is priced as if there will be no further increase. We suspect the market may be right as there have been some indications from Fed board members since New Year, in response to equity market turmoil, that they may pause the process of increases in 2019.

- Australian short-term rates rose slightly in response to the US move even though the RBA once again kept its official rate at the long-running low level of 1.5% p.a.
- Even with these increases the price of short-term money is still at historically low levels in most places, even in the USA, where the rate of increase has been very gradual and well flagged in advance by the Federal Reserve. There is some growing concern that the short rates are rising relative to long rates, causing the yield curve to flatten in the US. This has mainly been due to the fall in the long-term bond yield as some investors bid up bond prices as they shifted from equities to bonds. This has continued to reverse the earlier tendency for bond yields to rise in the face of increased US government borrowing. There is still a significant risk of ten-year bond yields rising in the next year or two, especially as the need for massive borrowings by the US government persists.
- Oil recovered some of the 18% fall experienced in the preceding month but remains difficult to forecast due to political factors involving Saudi Arabia, Russia and Iran as well as the US, where production has continued to surge.
- The Australian dollar was weaker against all major currencies, since mid-December, providing some assistance to returns on International equities.
- The prospect of a US federal government shut down before the end of December has become a reality, with the President and the Congress at a stalemate on spending priorities. If this continues it may increase the risk of an earlier recession in the USA.
- China is taking seriously the prospect of a major slowdown in its GDP growth, due in part to the trade dispute with the USA. Chinese authorities have reacted to a reported slowdown in the fourth quarter of 2018 by ordering provincial governments to bring forward borrowing programs to finance more spending on infrastructure. This is directly counter to earlier moves to constrain credit growth. Estimates of GDP growth in the first part of 2019 are as low as 3% p.a. and are generally below the 6% p.a. rate that investors have become accustomed to in recent years. It may be that the reversal of policy on credit may be too late to prevent a major slowdown in growth.
- The major political problems in Britain and France are not yet resolved and are still likely to disrupt the broader European economy. The ECB has said it has finished buying bonds under its long running quantitative easing program, but it has felt the need to say that it will not start selling any of its accumulated Euro 2.6 trillion of bonds until “an extended period after it starts increasing its policy interest rate”. This is not expected until late 2019. Meanwhile the ECB is keeping its deposit rate at -0.4% p.a., hardly a sign of robust economic prospects.

Where to next?

- Equity markets are likely to recover in the short run, but the outlook over the next year or two includes more significant downturns. Day to day and week to week volatility will continue with equity market prices reflecting a balance of positive influences and negative influences which are continually shifting in importance. Mistakes by policymakers and politicians appear to be more likely and of greater consequence than in the last ten years.
- While the short-term outlook for equities may be better, the longer-term case is being weakened by three sets of factors:
  - Firstly, growth in GDP and in earnings per share are likely to slow as the effect of the trade dispute impacts volumes of trade and global supply chains. The recent downgrades in revenue outlook for both Apple and Samsung are a foretaste of a wider slowdown emanating from China over the next year or so.
  - Secondly, notwithstanding recent falls in bond yields, the sheer volume of borrowing needed by the US government combined with the retreat of major central banks from holding bonds, will eventually push up the long-term bond yields, reducing the value of future cash flows from investments and with it the prices of financial assets.
  - Thirdly and most importantly, central banks have shifted from quantitative easing to quantitative tightening (QT). The tide of monetary support for asset prices is turning, albeit gradually over the next few years. The real global monetary base may well shrink, depriving asset markets of liquidity. Only China, among all of the major countries, is currently relaxing monetary policy, in response to a sharp slowdown in output in 2018. By itself QT may not produce a recession, but it will impact financial asset prices, just as the effects of QE went mostly into asset prices rather than economic growth between 2009 and 2018
- Two long term trends which have supported equity prices have now come to an end: the fall in bond yields from 1980 through to 2018 and the strong growth in world trade following China joining the WTO.
- The shift in monetary policy that is now under way will be the main driver of equity markets, overshadowing issues such as the US government shutdown, Brexit or oil price volatility, however there are additional negative influences coming mainly from these and other geopolitical factors which are hard to predict. They currently include:
  - US China trade relations which are far from settled despite the declared 90-day truce although at the time of writing (early January) the prospects for a settlement looked better than before New Year;
  - US policy in the Middle East and Iran and its disruptive effect on oil prices;
  - Political pressure on the Italian and French governments which threatens to disrupt economic growth in these two important economies and more importantly throughout the European Union, the third biggest economy in the world;
  - The search for balance in China between sustaining growth through building infrastructure and restraining credit growth in the interests of longer-term stability, although the authorities seem to now be opting for growth over stability. The Chinese leadership appears to have at least temporarily abandoned efforts to purge financial excess and control credit growth in favour of resuming stimulus that keeps growth above 6% p.a. This has included a fifth cut in the reserve requirements for banks making it easier for them to expand lending. In addition, provincial governments have been ordered to increase and bring forward borrowing to increase investment in infrastructure. This may yet be too late to prevent economic growth from slowing sharply in early 2019 with some estimates of the GDP growth rate coming in as low as 3%p.a.;
- The Federal Reserve has also backed away from its former statements before New Year about continuing quantitative tightening at the rate of $US 50 billion per month. Since New Year, Chairman Powell has said that the Fed "would not hesitate to suspend QT if the circumstances deteriorate". The equity markets reacted to this with relief. Powell's predecessor, Janet Yellen, opined that the Fed could well pause its interest rate increases in 2019, but eventually it may need to have one or two more increases of +0.25% p.a. in due course, to "prevent the economy form overheat-

ing". The financial markets are currently pricing in no increases in the Fed Funds rate in 2019.

- As far as equity earnings in the US are concerned, the consensus of forecasts for earnings per share growth for the S&P 500 for 2019 is at +8.3% (versus actual EPS growth of +20.5% in 2018). This level of EPS growth in 2019 would imply stock price gains of 15% by the S&P 500, according to JP Morgan Chase, a major US bank.
- Taking all of this into account, the outcomes expected under our mainstream scenario over next three to five years are as follows:
    - Short term interest rates rise in the US, rising to 3.0% p.a. over the next two years and above 4.0% p.a. within five years;
    - Short-term interest rates in Australia stay at 1.5% p.a. for the next year or so before rising towards 3.5% p.a. (the RBA neutral rate) by 2022;
    - Long-term bond yields in the US rising above 3.5% p.a. within the next two years;
    - The AUD weakens towards USD 0.65 or lower, adding to International equity returns for Australian investors as well as assisting the earnings of internationally focused Australian companies;
    - Equity prices in most developed markets will rise modestly in early 2019, driven by EPS growth, which continues for the next year or two but is likely to falter after that, especially if either the ten-year bond yield is significantly above 3.5% p.a. or if it is lower than the two-year bond yield (due to the latter rising more). If there is any inability to tolerate a downturn in asset values with a recovery delayed out to three years, it would be prudent to use any equity market rallies of the next year or so, to reduce portfolio allocations to equities. Investors with a longer-term perspective of five years or more should be able to hold equity assets which on longer term valuation assessments are now in the cheaper end of the fairly priced range;
    - Equity markets need to be continually re-assessed as outlined in section 3 below, considering the effects of shifts in the long-term bond yield, changes in earnings per share growth as well as momentum effects and other more difficult to assess qualitative factors.
- The main risks to this mainstream scenario include:
    - The US ten-year Treasury bond yield could well rise more quickly to a level closer to 4% p.a., leading to a major shift from equities to bonds. If this occurs, then a fall of 20% or more in equity markets could easily occur within the next two years;
    - The US China trade war is not settled and becomes more severe or more protracted and a recession is triggered sooner rather than later;
    - A financial crisis arising in Italy or via defaults in emerging market entities such as major corporates or governments transmit stress to the entire global economy via the banking system, causing a crisis and a major world recession.
    - Political instability in Britain (following a hard Brexit) or in France, severely disrupts their economies and financial markets, spreading to the whole of Europe or beyond.

Assessment of equity asset markets

The assessment of equity markets is central to deciding how much of the portfolio to allocate to growth assets over time. Our current assessment of equity markets, which is summarised in Table 3, considers:

- The Valuation of equities comparing current prices to long term Fair Prices;
- The Momentum of equity market price movements; and
- Qualitative indicators that consider the impact of fiscal and monetary policy as well as economic and political factors.

Table 3: Summary of equity markets assessments

Equity Markets Assessment - 9 January 2019

Asset class	Australian equities	International equities
Valuation indicator (scenario weighted,lower is better)	87%	84%
Momentum indicator based on last 12 months price	NEGATIVE	NEGATIVE
Qualititative indicator	POSITIVE BUT WEAKENING	POSITIVE BUT WEAKENING

The market falls in December followed by the partial recovery in early January have left the valuation indicators in the cheaper end of the Fair Price range.

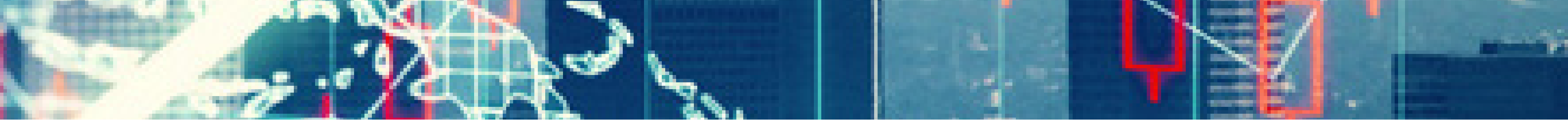
The market movements of the last three months have also shifted momentum based on trailing twelve-month indicators so that it is now decisively negative. This may not turn around in the next six to twelve months.

There is therefore a divergence between the outlook for longer-term valuation focussed investors with horizons of five years or more (i.e. beyond the period during which a major equity market downturn would occur and be followed by a recovery) and those with shorter range horizons of one to three years (i.e. before a recovery from a major fall would be likely to occur).

The Qualitative factors remain positive but less so than they were a year ago. The major shift has been in the reduction in the stimulus from monetary policy. These qualitative factors are summarised in Table 6. In particular, monetary and fiscal policy in most major countries, are still both supportive of earnings growth for equities and of equity prices in general, but their effect is lessening. In addition, political and economic risks are growing and have shifted to become significantly worse in recent months.

Valuation is the most important part of our assessment for longer-term investment strategy because the momentum and qualitative effects tend to be shorter term in their effects. We continually assess the ratio of Current Market Price to the assessed Long-Term Fair Price of the same market. The lower this ratio, the more attractive investment in a particular share market appears. The Fair Price of an equity market is the price at which the market should trade in order to achieve the long-term Fair Value Return. In turn, the Fair Value Return is the return required to fairly compensates for risk. It equates to the current long-term government bond yield in the investor's home country plus a margin or Equity Risk Premium. We have continued to assume a required equity risk premium of 5% p.a. for developed equity markets and 8% p.a. for emerging markets. This means for instance that an Australian investor investing in the US equity market should expect to earn a total return over ten years of 7.4% p.a. if they are being fairly compensated for equity risk.

A key assumption in the assessment of the long-term Fair Price is the long-term rate of growth in earnings per share. In turn, this depends on assumptions about the long-term rates of inflation and real economic growth as well as the rate of issuance of new equity or buy backs of equity.
We monitor and adjust where necessary our long-term



Assessment of equity asset markets cont...

assumptions about inflation and real economic growth in the major developed countries as well as in the major developing economies. Table 4 below sets out our current assessment of this critical factor for the Australian equity market as well as the major international equity markets. We have revised the GDP growth assumptions downwards over the course of the last month. This partly reflects similar revisions by the IMF but also the increase in political risks to GDP growth, including the risk of slower world trade.

Table 4: Earnings per share growth rates for equity markets

Scenario 1 base EPS growth assumptions: average over ten years

as at 9 January 2019		Real GDP growth % p.a.	Inflation % p.a.	EPS growth % p.a.
USA	S&P 500	2.25%	2.00%	3.25%
China	Hang Seng	4.00%	2.50%	2.50%
Japan	Nikkei 225	1.75%	1.50%	2.25%
Britain	FTSE ALL SHARE	1.75%	2.50%	2.25%
Germany	DAX	1.75%	2.00%	1.75%
France	CAC	1.75%	2.00%	1.75%
Australia	ASX S&P 200	2.50%	2.00%	2.50%

Unchanged since last month

Together with the bond yield, these estimates of EPS growth are the key assumptions used to derive the long run Fair Price estimates in the analysis set out below in Table 5.

These assessments are made for a number of scenarios which may occur over the next ten years. Each scenario implies a different financial market regime and with its different relative returns for the various asset classes. We have reviewed the three long-term scenarios and have kept the assessments unchanged since our last update as well as the assessed likelihood of each of them:

- **Scenario 1:** Modest earnings growth where inflation and interest rates do not rise by much. This is good for valuation of equities. There is a recession within the next three to five years, but it is milder than that of 2008-2009. We rate this as the scenario for the next 3 to 5 years with a likelihood of 50% of occuring. In this scenario we are assuming that the ten-year Australian bond yield will rise from the current 2.35% p.a. to around 3.06% p.a. This extra yield margin of +0.71% p.a. provides a buffer of safety in our valuation analysis.
- **Scenario 2:** Faster earnings growth where inflation and interest rates rise to around 3.5% p.a. This higher rate of inflation is bad for fixed interest and also impacts equity valuation, offsetting some of the effects of faster earnings growth. We continue to rate this scenario with a 20% likelihood of occuring i.e. not very likely, as it depends on fiscal and monetary stimulus in China working and there being no significant policy maker mistakes in any major country.
- **Scenario 3:** A more significant recession where inflation and real interest rates fall significantly and may even turn negative and there is a risk of the economy being trapped in a zero or negative growth pattern. We continue to rate this scenario with a 30% likelihood of occuring, although a recession of this nature is more likely to occur after 2020 than before, unless there is a major deterioration in the US-China trade dispute.

Assessment of equity asset markets cont...

Table 5: Fair Price assessments for the Australian and International equity markets - 9 January 2019

Economic Scenario:	One: Continued moderate growth	Two: Faster growth	Three: Relapse into recession	SCENARIO WEIGHTED PRICE TO FAIR VALUE
Probability of scenario	50%	20%	30%	
Country	Ratio of current market value to long term fair value	Ratio of current market value to long term fair value	Ratio of current market value to long term fair value	Ratio of current market value to long term fair value
USA	84%	80%	83%	83%
China	84%	80%	90%	85%
Japan	81%	77%	82%	81%
Britain	96%	91%	98%	96%
Germany	75%	71%	77%	75%
France	93%	88%	96%	93%
Australia	88%	83%	88%	87%
Global	85%	81%	85%	84%

Red is expensive (above 120%) Purple is more or less fair value (80% to 120%) Green is cheap (below 80%)

All major equity markets are in the cheaper end of the Fair Price range except for Germany which is definitively cheap. Overall, the valuation factors are supportive of investment in equities and are compelling for longer-term investors.

Qualitative factors used in the overall assessment

Overall our current assessment is that the positive qualitative factors (supportive monetary and fiscal policy) outweigh the negative factors (the risk of mistakes by policy makers). Our summary of the qualitative factors and their effects on equity market returns for each major region is set out in Table 6.

Qualitative factors used in the overall assessment
cont...

Table 6: Qualitative factors affecting equity markets over the next 3 years

Region	Monetary Policy	Fiscal Policy	Economy	Politics and Public Policy	Overall
USA	Fed policy is still supportive of asset prices but is reducing gradually as the Fed continues to reduce its holdings of bonds while raising short-term rates. An interest rate overshoot would add to negative pressures on the equity markets and the mere prospect of this has caused major selling.	Positive but the effect of the tax cuts will run out by 2020. Meanwhile the rise in Federal borrowing needed may eventually push the US ten-year Treasury bond yields up above 3.5% and towards 4.0% p.a., a critical level affecting equity market pricing adversely.	Has been positive and increasing and has been reflected in earnings per share growth of companies but has recently reached an inflexion point and is expected to slow down especially if trade tensions with China are not resolved.	Has been positive but volatile but following the US mid-term elections will be much less positive for the economy and corporate earnings, as shown by the partial closure of the Federal Government which may go on for some months.	Positive but becoming much less so throughout 2019.
China	Positive. The PBOC, the central bank, has been injecting liquidity into the banking system to ward off risks from its policy of deleveraging as well as from the trade dispute with the USA.	Positive as there is a need for continued spending on infrastructure, health care and education. Fiscal deficit is 3.6% of GDP.	Positive but with a strong prospect of a decline in the rate of growth towards 5% p.a. or below over the next three years. This degree of decline could be very adverse for commodity prices.	Positive, but the main risk is if the policy makers make a mistake. Reaching an agreement with the US on trade policy by March 2019 will be critical.	Positive but now more fragile than at any time since the GFC.
Japan	Positive with the BOJ continuing to keep short rates negative and bond yields near zero.	Positive with fiscal deficit of 3.8% of GDP adding to overall demand.	Positive but stalling slightly with real GDP growth easing back to 1.3% p.a.	Positive.	Positive.
Europe	Positive but weakening slightly in 2019 as the ECB reduces its rate of stimulus by not adding to its portfolio of bonds, but replacing those that mature, while keeping its key interest rate at minus 0.4% p.a.	Slightly positive with Euro area fiscal deficit at just 0.7% of GDP although there are wide variations from country to country.	Positive with modest growth but a hard Brexit is now a major threat to EU growth.	Has now come back to neutral and the prospect of turning negative if there is a hard Brexit or a fiscal crisis in Italy or continued problems in France.	Positive but weakening or becoming negative in 2019.
Great Britain	Positive.	Positive due to fiscal deficit running at 1.7% of GDP.	A hard Brexit is now a major threat to the economy and looks to be unavoidable.	Negative and divided. There is much uncertainty about Brexit and hence about the government.	Positive but weakening or turning negative as Brexit approaches.
Australia	Positive with the RBA rate likely to be unchanged till late 2019.	Slightly positive with Federal deficit at a low level of 0.9% of GDP.	Positive due to infrastructure spending by the states.	Negative due to lack of policy focus by Federal government.	Positive but weakening.