Canopus Investments Limited

Investment Advice *Sharebroking* *Managed Funds* *Fixed Interest* *Property* *Company Formations* *Trade Mark Registration*

P O Box 101 662
North Shore Mail Centre
Auckland
New Zealand

Phone: +64 9 444 8055
+64 9 444 8056
Fax: +64 9 444 8059
Websites: www.canopus.co.nz
www.debex.co.nz

Investment Directions **29 April 2016**

"Analysis to action; opportunities to outcomes"

In this Issue

1. **Overview** – Bank of Japan snuffs out global equities recovery with unexpected cap on stimulus. Lower oil and poor US reporting season add to pressure. More moves against property investors and speculators expected in NZ as Reserve Bank keeps OCR on hold. Short term indicators point to lower equity prices in near future.

2. **Equities** – Barramundi warrants worth exercising. Kingfish Limited to issue more warrants. Three of four big Australian banks to report next week. Fast food sector runs into trouble in the US – which could create an opportunity in NZ. Z Energy share price leaps on approval to purchase Caltex.

3. **Interest rates, bonds and debentures** – UDC lowers deposit rates again. Deposit rates for major S&P-rated finance companies.

4. **Strategy** – Caution urged for Australian purchases as AUD falls and election looms. Retirement income isn't all about KiwiSaver and residential property. Things to avoid when building a portfolio. Income and growth portfolios both reach new record high unit values at end of April.

Space Exploration News

Elon Musk's SpaceX, after successfully landing reusable rockets on land and at sea, announces plans to land a craft on Mars as soon as 2018 and hopes to get humans there by 2025. See http://www.thestar.com/business/2016/04/27/spacex-will-land-a-spacecraft-on-mars-as-soon-as-2018-says-elon-musk.html

Physicist Stephen Hawking, science philanthropist Yuri Milner and others announce project to explore concept of light beam powered nanocraft being sent to our nearest neighbouring stellar system, Alpha Centauri. See http://breakthroughinitiatives.org/News/4

1. Overview

The US Fed left its Federal Funds target rate at 0.25% - 0.50% on Wednesday 27 April.

After a strong run-up starting in mid-February, leading US equity markets look to be struggling to move higher as crude oil runs into resistance around US$44 (WTI). Since November 2015 there has been a growing correlation between oil and equity prices. Also, Q1 ’16 US corporate results have failed to impress, including weaker than expected earnings from tech giants Apple, Microsoft and Alphabet although Facebook stood out after Q1 profits trebled to US$1.51B. Overall, 2016 Q1 S&P 500 earnings are expected to be significantly down (-7.3%) on Q1 2015. US economic data is still patchy and the expectation of higher interest rates from the Fed later in the year continues to overhang markets. The old and influential (but rather unreliable) adage of “sell in May and go away” is hard upon us. Present market sentiment foresees a further decline of about 2.2% in earnings during Q2 but then an improvement starting in Q3 based on stronger oil and other commodity prices, a weaker US dollar and a slowly improving US economy.

On Thursday, 28 April, the Bank of Japan confounded market expectations of even deeper negative interest rates by announcing instead a cap on stimulatory measures. The news shocked global equity markets into reverse, the S&P 500 losing 19.26 points (0.92 percent) to close at 2076. Heavy selling of Apple, after a poor result and news that Carl Icahn had quit the stock, added downward pressure.

Even before the event, both oil and equity markets seem to have priced in a failure of major oil producers to agree on production caps at their Doha meeting on 16 and 17 April. Lack of agreement, theoretically at least, should have seen crude oil fall, taking equities with it - but just the opposite occurred - a classic example of “sell rumour, buy fact” (when bad news is expected). That rally looks to have run out of steam for now.

In New Zealand, Finance Minister Bill English released a letter he sent to the Reserve Bank Chairman last November (2015) requesting bi-annual meetings to discuss the board’s monitoring role, including the performance of monetary policy with respect to the Policy Targets Agreement and the governor’s performance “from time to time”. The RBNZ has been viewed by some as providing guidance contrary to subsequent actions and criticised for failing to achieve inflation anywhere near the targeted 1% - 3% band. Measured CPI inflation for the first three months of 2016 was at an annual rate of just 0.4%.

Bill English said his letter setting out his expectations to the board wasn’t linked to concerns about the Reserve Bank’s performance.

To help achieve its 1% - 3% inflation target, boost exports and deter a permanent low–inflation mindset the RBNZ needs lower interest rates but a lower OCR will only help push house prices higher. Hence we can expect to see a reluctance for further OCR cuts from the RBNZ but more government moves against property investors and speculators as the chorus for government and RBNZ intervention grows. Such moves could include:

- a land tax on overseas- based house owners, including New Zealanders living abroad (seems to be the preferred option at present)
- limitation of overseas buyers to construction of new houses only
- extra penalties for properties lying idle
- increased deposit requirements for residential investment properties
- more restrictions on depreciation and loss allocation allowances
- mandatory higher interest rates for non-owner-occupied dwelling bank mortgages.

Of two things we can be sure:

1. Any government action will only be poll-driven. John Key has re-learned from his flag debacle a harsh lesson he forgot earlier about offending his own support base.
2. The chorus for action will grow louder as re-ignited Auckland housing prices spread further into adjoining regions and beyond.

The RBNZ kept the New Zealand OCR at 2.25% on Thursday, 28 April.

Australian inflation fell to just 0.2% in Q1 16, the first quarterly fall in seven years, sparking a quick surge in the S&P/ASX 200 on hopes of another OCR cut within the week. The annual rate is down to 1.3%, well outside the RBA target of 2% - 3%. But the news also sparked selling of the Australia dollar which then reflected back into equities, especially banks. Lower iron ore prices added to the pressure, forcing down the big miners. Benchmark 10 year Australian Government bond yields fell to 2.602% with 2 year stock down at 1.932%.

The RBA kept its OCR at 2.00% on 5 April.

In moves that may have a real impact on Australian house prices, CBA and Westpac have announced they will no longer grant housing mortgages to non-residents. ANZ and NAB have also announced reviews and restrictions on foreign borrowers respectively.

Australia looks set to head into a federal election on 2 July after PM Malcolm Turnbull's defeat in the Senate, over a bid to restore the Australian Building and Construction Commission, provided the trigger for a double dissolution of parliament.

Keeping our finger on the pulse of major Leading Economic Indicators (LEI) and other leading data:

	Latest	Mar 16	Feb 16	Jan 16	Dec 15	Nov 15	Oct 15
3 month LIBOR (end of month) %	.63385	.62820	.63310	.61560	.61270	.41620	.33410
TED Spread (points)	.42	.42	.30	0.29	0.45	.20	.25
VIX equity volatility	13.96	13.95	20.55	20.20	18.21	16.13	15.07
US LEI		+0.2%	-0.1%	-0.2%	-0.3%	+0.5%	+0.5%
Japan LEI			-0.6%	-1.2%	-0.5%	+0.1%	+0.0%
Eurozone LEI		+0.3%	-0.2%	+0.1%	+0.2%	+0.6%	+0.4%
Australia LEI			-0.3%	-0.5%	-0.3%	+0.2%	-0.1%
United Kingdom LEI			+0.2%	+0.3%	+0.4%	+0.4%	+0.4%
China LEI				n/a	n/a	+0.6%	+0.3%
US Money Market Funds $T	2.698	2.765	2.807	2.756	2.759	2.741	2.717
US Gov. 10 year T-Bond (%)	1.860	1.786	1.740	1.931	2.269	2.218	2.151
US 5 yr inflation expectations %	1.78	1.75	1.61	1.63	1.77	1.88	1.86
US high yield-treasury spread 3-5yr %	6.26	7.05	7.75	7.77	6.95	6.40	5.90
Foreign holdings of US T-Bonds $B			6236.2	6183.1	6165.8	6125.7	6046.3
Margin debt, NYSE (US$ millions)		445,846	435,814	447,681	461,200	472,772	471,922
US M2 Money Stock (US$B)		12,568.6	12,472.8	12,420.3	12,331	12,288	12,201
Velocity of Money US M2					1.482		
CNN Fear and Greed Index	72	64	51	17	44	53	69
Insider Buy/Sell ratio (US) %	44	58	65	58	53	49	48
Forward P/E S&P 500 (12 month)	17.80	17.55	15.75	15.38	17.19	17.55	18.41
Trailing P/E S&P 500 (12 month)	24.11	23.53	21.82	20.69	22.65	23.18	22.07
Total Put/Call options ratio CBOE	1.15	1.08	1.20	0.91	1.00	1.07	0.95
S&P 500 Share Index	2065.30	2059.74	1932.23	1940.24	2043.94	2080.41	2079.36

NYSE margin debt continued to ease as at the end of February but then move up a little in March – a positive sign for improved market stability rather than growth. A sudden decline in margin debt would be likely to accompany or even precede a sharp retreat in US equity markets. Unfortunately the data is always a month or two old before we get it.

As at 29 April the Total Put/Call ratio is at 1.15, rising rapidly from a low 0.76 on 25 April with the 10 day moving average reversing to an upward trend – indicating professional traders are concerned about their portfolio values and are taking additional protective measures via purchase of put options – a sign of near term equities weakness. Similarly, the insider Buy/Sell ratio is declining – those in the know are less enthusiastic about buying right now.

Further out, signs are positive. Leading economic indicators have turned positive in the US and Europe with the UK still positive although weaker. LEI data for China is unavailable. US inflation expectations are rising gradually, consistent with expectations of one or two moves to raise the Federal Funds rate later in the year.

2. Equities

Warrants for Carmel Fisher's **Barramundi (NZX:BRM)** come up for exercise on 6 May at 62 cents per new share issued on exercise of each warrant. Barramundi shares are selling today at 63 cents making exercise of the warrants very marginally "in the money" based on market price alone. However, latest published undiluted NAV of Barramundi is 70.95 cents meaning warrant holders have the opportunity to access a diversified portfolio of Australian equities at a discount of nearly 13% based on these latest figures. Along with the other Fisher Funds listed investment companies, **Kingfish (NZX:KFL)** and Marlin **(NZX:MLN),** Barramundi distributes 2% of NAV per quarter (8% per year) as a dividend under a tax-convenient PIE structure. On the latest figures that translates to a high cash dividend income yield of 9.15% p.a. for the new BRM shares.

Barramundi was originally intended as a holding company for a diversified portfolio of small Australian listed shares. Listed on the NZX in October 2006, shortly before the Global Financial Crisis, Barramundi was pummelled by diving share prices and some poor equity selections, reaching a low of 34 cents in March 2009. Improving market conditions saw BRM back up to 90 cents by the start of 2011 but again, poor overall performance of Australian small caps, represented by the XSO S&P/ASX small ordinaries index, and some poor share selections saw the BRM share price drift downwards over the subsequent four years, consolidating eventually around current levels. For anyone astute or lucky enough to invest at 40 cents the outcome has been outstanding. Capital gain over seven years has been reasonable at 58% (6.8% p.a. compounding) but cash income has been spectacular, with dividend yield exceeding 14% p.a. on the original investment.

Over the past three years Barramundi has undergone a major portfolio rearrangement to cull out serious under performers. Mandate has been broadened to include a large number of mid-cap and large-cap ASX-listed companies which should ensure Barramundi at least matches future growth in the broad ASX market. Very small cap shares look to have been eliminated from the portfolio altogether.

On balance the warrants appear to be worth exercising with limited downside risk and considerable upside potential, including the high dividend yield.

Kingfish Limited (NZX:KFL) has announced a fourth issue of warrants, free to existing shareholders on the register at 9 May 2016, in the ratio of one warrant for every four ordinary shares held. Exercise price will be $1.32 less an amount equal to any dividends declared during the period from issue of the warrants up to the exercise date. That should be four dividends, giving an exercise price of about $1.21. The exercise date will be 5 May 2017. The warrants will be listed on the NZX under code KFLWD.

Three of Australia's big four banks report first half profits next week. **Westpac (ASX:WBC)** leads on Monday, 2 May. Investors have marked down banks' share prices after much publicity being given in MSM to reports of sharp or "scandalous" business practice plus predictions of higher impairment charges, higher funding costs, sluggish economic growth, difficulty in maintaining margins and specific corporate defaults in the resources sector. Some reporters predict a small decline in earnings and some slight dividend cuts while others quote analysts who believe earnings can be maintained and dividends even increased – particularly in the case of Westpac. By the end of next week we will know if all the "bank bashing" has been justified. If not, or even if it is to some extent, expect another "sell rumour, buy fact" event (applies when bad news expected). Short selling of Australian banks reached high levels early in the week but had reduced markedly by Thursday.

The US fast food sector is under pressure as little wage growth forces widespread discounting amongst the big names such as McDonalds and Domino's. The fast food sector has been a steady improver over four years in New Zealand where **Restaurant Brands (NZX:RBD)** operates KFC, Pizza Hut and Starbucks Coffee and has recently acquired the rights to Carl's Junior. The RBD share price looks to have got somewhat carried away over recent months with P/E up at 20.7 and dividend yield down to 4% - but still good. Any nervousness reflecting here from the US news may produce a buying opportunity.

The **Z Energy (NZX:ZEL)** share price leapt on news that the Commerce Commission had given clearance for Z Energy to purchase 100% of the NZ assets of Chevron – which operates Caltex in New Zealand. Z expects to deliver $25 – $30m of synergies from improved supply efficiency, reduced offshore back office costs plus IT, systems and process efficiencies. Z will divest 19 retail service stations and one truckstop business as part of the deal. Caltex and Z will remain as separate brands, both with their own special offers and business models. Total purchase price is $785m which will be funded by $115m cash plus new debt of $670m. A $185m pro rata equity issue, which was considered at the time of the intended transaction (June 2015) has been dropped. Abandonment of the possible cash request to shareholders may explain, in part, the big boost in share price.

With a market capitalisation of NZ$3,160m, Z Energy is one of New Zealand's largest listed companies.

3. Interest rates, bonds and debentures

UDC has again lowered deposit rates, up to a maximum of 20 basis points for the 3 month term and by 15 basis points for the 9 and 12 month terms.

Current major S&P rated finance company deposit rates, % p.a., quarterly interest payments:

Issuer	S&P rating	$ min	Call	3m	6m	9m	12m	18m	24m	36m	48m	60m
F&P Finance	BB	1000	2.85	3.15	3.65	3.75	3.85	3.95	4.10	4.25	4.35	4.45
F&P Finance	BB	25,000	2.85	3.30	3.80	3.90	4.00	4.10	4.25	4.40	4.50	4.60
Liberty Fin	BBB-	5,000		3.45	4.05	4.15	4.70	5.05	5.25	5.85	5.75	5.65
Liberty Fin	BBB-	20,000		3.60	4.20	4.30	4.85	5.20	5.40	6.00	5.90	5.80
Liberty Fin	BBB-	100,000		3.65	4.25	4.35	4.90	5.25	5.45	6.05	5.95	5.85
UDC Finance	AA-	5,000	2.45	2.70	3.20	3.15	3.45	3.25	3.30	3.30	3.30	3.40
UDC Finance	AA-	100,000	2.95	2.75	3.25	3.20	3.45	3.30	3.35	3.35	3.35	3.45

Canopus advisory clients receive a full rebate of any brokerage paid on term deposits.

Contact me for copies of investment statements and application forms alan@canopus.co.nz
or telephone 09 444 8055. No brokerage is payable by investors on applications made through Canopus.

4. Strategy

For New Zealand investors it may be wise to hold off ASX purchases until the AUD settles down after unexpectedly weak inflation led to increased expectations of more OCR cuts by the RBA and a down-trending, volatile AUD. After relative stability since mid-March the NZD/AUD cross rate got a quick boost on 27 April to a close of 0.9105 and has moved higher since. A federal election on 2 July won't help stability. In the US, the Fear and Greed index at a high 72 signifies a poor time to be buying equities. The month of May has strong connotations of weakness in the US, further casting a warning for the near future.

Investing for retirement isn't all about KiwiSaver and residential property. Reading the daily papers you would think so. Financial reporters appear incapable of venturing beyond endless articles on how to select the best Kiwisaver fund for you, Kiwisaver fund fee comparisons and references to historic KiwiSaver fund returns. Residential property investment is analysed to death.

At Canopus we seek to build individual investment portfolios which may be a prime investment scheme in their own right or augment direct property investments and KiwiSaver. Canopus portfolios can provide a long term growth strategy for younger savers or act as a main income earner to supplement national superannuation for those in retirement. Portfolios comprise mainly listed shares, bonds, floating rate notes, listed property, fixed interest securities and cash.

In building a personal portfolio it's just as important to know what to avoid as well as what to include. A few examples in particular:

Allocation of 5% or so of one’s portfolio to “alternative assets”, unpredictable commodities or risky derivative strategies – supposedly to improve diversification, provide “insurance” or tap into possible “outstanding returns”. We want every portfolio selection to make a real and expected contribution to portfolio performance. Even with the best of intentions and analysis we won’t get everything right and culling will be necessary. We don’t need to add unknown risk and uncertainty deliberately. In my long experience, alternative assets and the like are highly risky and seldom provide the hoped for “outstanding returns” or “insurance”. It has happened on a few occasions – but very few. More often, gains are modest at best, losses can be substantial and sometimes complete. Such an outcome can seriously impact portfolio performance. Over time, keeping it simple has proven to be the best strategy.

Peddlers of newly-discovered “market cycles” - as well as old such as Elliot waves, Kondratieff cycles and Fibonacci numbers. Perma-bear – tipsters forecasting financial doom and gloom – year after year – dressing themselves up as gurus and preying on inbuilt human fear of the unknown to sell huge volumes of overpriced newsletters and publications of highly dubious value offering “advice” on how to avoid “the coming financial collapse”.

Emerging markets - oft touted as the place to go for low P/Es and extra high return opportunities. Maybe so, but years ago an investigative trip through various third world states convinced me that emerging market investment is definitely not for the inexperienced private investor or even for a lot of the so-called specialist fund managers. If anything, the situation seems to be worse now than then. Emerging market P/Es are low for good reason. Corruption is reportedly rife in the BRICS, TIMPs and muchos otros paises – tending to produce highly volatile equity markets and plunging currencies from time to time. We have enough work avoiding the scoundrels and dubious business practices in places where we understand the culture - let alone those where we don’t. Any investment in emerging markets should be done only through the fund of a proven and trusted expert.

As one astute Kiwi investor observed after a guided investment tour of China some time ago – “there’s a lot of money to be made in China – by the Chinese!”

Our published portfolio unit values have continued to rebound strongly during April, setting new records by the end of the trading month. Published returns are after fees and tax at the investor’s prescribed rate on portfolio investments.

Click this link to see charts http://www.canopus.co.nz/investment_advice.html#returns

Please note that I cannot make application for new issues of bonds or shares, trade securities on your behalf or provide personal investment advice unless you have an ASB Securities sharebroking account opened through Canopus.

Contact me if you would like to open an account alan@canopus.co.nz or telephone 09 444 8055.

To discuss building a diversified, low volatility personal investment portfolio designed to produce income, growth or a combination of both, contact me by email at alan@canopus.co.nz or telephone 09 444 8055.

Canopus does not cancel portfolio units to meet fees. In Canopus portfolios, fees are taken on the nose as a portfolio expense. Hence, if you start with 100,000 units of $1.00 and make no further contributions or withdrawals, you will still have 100,000 units years later. The number won’t be whittled away and the current unit value times the original number of units will represent your true portfolio value.

Please note – Canopus does not pool investor funds. Each Canopus investor is treated as an individual with a personal customised investment portfolio being built to suit the investor’s requirements. Investments are registered in your own name greatly enhancing returns, security and transparency while providing access to valuable special issues and minimising management fees. Individual voting rights attached to securities are retained by the investor. Uncommitted portfolio cash is held in the investor’s own personal bank account with full online banking facilities. High liquidity of investments means the investor has ready access to funds if needed. Ultimately, the portfolio owner remains in control of the portfolio.

Regards,

Alan King
Authorised Financial Adviser
Canopus Investments Limited
Email: alan@canopus.co.nz
Mob: 0274 718 253
Tel: +649 444 8055

Postal address:
PO Box 101662
North Shore Mail Centre
Auckland 0745
New Zealand

Financial Adviser Disclosure Statement available on request, free of charge.

Disclosure

Canopus Investments Limited, its directors, officers and associates, may hold or apply for investments referred to in this newsletter for their own investment purposes.

Canopus Investments Limited does not bank or hold investment monies received on behalf of clients unless by special request or arrangement. When held on behalf of clients through special request, client funds will be held on trust in a separate special purpose account. In the normal course of business, investment monies will be passed directly to the securities issuer. All Canopus sharetrading account holders are issued with an individual true bank account from which share purchases are funded and to which share sale proceeds are deposited. Canopus does not pool sharetrading account funds.

Disclaimer

This newsletter does not constitute personal investment advice. Information in this newsletter does not constitute a recommendation or advice to purchase any product or service referred to in this newsletter. Investment products or services referred to in this newsletter may not be suitable for individual investment objectives or individual financial circumstances. Information contained in this newsletter should not be relied on for making investment decisions. In compiling this newsletter, individual personal financial circumstances have not been taken into account. For personal investment advice contact Canopus Investments Limited to arrange an initial advisory interview.

To the maximum extent permitted by law, neither the owners, managers, employees nor associates of Canopus Investments Limited accept any liability whatsoever for any loss or damage resulting from reliance on, or consequent to, the use of information obtained from this communication or any other publication produced by the owners, managers, employees or associates of Canopus Investments Limited. Neither Canopus Investments Limited, nor its directors, officers and associates, guarantee the expected investment return, return of capital, or any other return from investments referred to in this newsletter. Neither Canopus Investments Limited, its directors, officers nor associates accept any liability whatsoever for financial losses that may be incurred as a result of reliance on, or consequent to, any information contained in this communication.

Information provided in this communication does not constitute an offer of securities as such offer is only made on receipt of a completed application form. Application for securities will only be accepted when made on the application form accompanying the formal offer document.

This newsletter is compiled from information believed to be accurate at the time of writing. However, no guarantee as to the accuracy of information contained in this newsletter is given, intended or implied.

Information contained in this newsletter is provided on a non-prejudicial basis only. Information contained in this newsletter is not intended to create, nor does it create, any legal obligation, responsibility or contract between Canopus Investments Limited, its officers and associates and any other party.