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**From:** Wilson Asset Management [mailto:info@wilsonassetmanagement.com.au]  
**Sent:** Friday, 29 March 2019 5:48 PM  
**To:** Frydenberg, Josh (MP)  
**Subject:** From the Lead Portfolio Managers: Inverted bond yields explained | Spotlight on Think Childcare

Wilson Asset Management



**Dear Big boss,**

The S&P/ASX All Ordinaries Accumulation Index closed down 0.3% for the week with Monday recording the second worst day of trading for 2019 – shedding \$20.5 billion from the local bourse.

The S&P 500 Index (AUD) is currently up 0.6% for the week and the MSCI World Index (AUD) is up 0.3%. In the United States (US) investors were cautious about the inverted US Treasury bond yields and in Europe the release of a range of German economic data showed cause for some concern.

Results from the monthly German purchasing managers' index (PMI) survey showed that manufacturers expectations are at their worst level in six-and-a-half years, following a fall in new export orders due to uncertainty around global growth.

As usual, the Brexit mess continued this week, with eight consecutive indicative votes on the withdrawal agreement all failing to gain a majority – even with Prime Minister May offering to resign if her twice-rejected withdrawal agreement was passed. There will be another vote today in London when Parliament resumes. This will put Prime Minister May's Brexit deal to a vote, but it will hold back the part of the package that focuses on the future trade and security relationship. To quote the words of one of the great novelists in the English language, Joseph Conrad: *"It [Parliament] echoed loudly within him because he was hollow at the core"*. The world is beginning to stop listening as politicians continue to fight amongst themselves.

#### **The week ahead**

There are four key releases we will be watching next week:

1. Australian Housing Industry Association New Home Sales monthly report: Monday, 1 April

This will provide data on the lending environment and construction industry, two major drivers of the Australian economy.

2. Commonwealth Budget for 2019-20: Tuesday, 2 April

The Budget will be released by Treasurer Frydenberg in Canberra. National Australia Bank (ASX: NAB) is expecting the federal budget to show a surplus of \$1.3 billion for the current financial year, a surplus for the first time in over a decade.

3. US monthly retail sales data: Monday, 1 April

Monthly US retail sales data will be released providing insight into consumer sentiment and the state of the world's second largest economy.

4. US monthly PMI manufacturing data: Tuesday, 2 April

Expectations are that the US PMI Index will decrease from February to March due to reduced factory activity amid softer new orders and output.



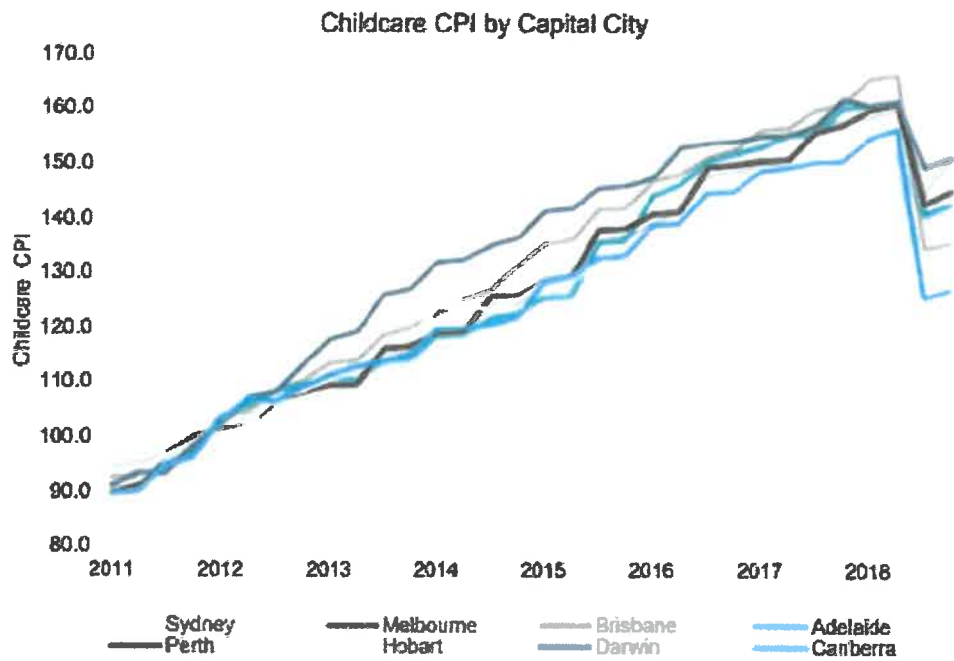
### **Spotlight on Think Childcare**

Think Childcare (ASX: TNK) is a childcare operator with a portfolio of 59 centres operating primarily out of Victoria, with the potential to expand nationally. Our catalyst to invest in TNK was the anticipation that the business would continue to add scale by acquiring new centres and that occupancy was improving, leading to positive changes in consensus earnings estimates.

TNK successfully raised \$18 million in capital this week to immediately fund the acquisition of four newly constructed centres and a capital investment program. These additional funds will enable the company to build greater scale and invest in maintaining centre quality.

We continue to hold TNK as tighter lending conditions have seen a reduction in the supply of new childcare centres, easing local competition. Secondly, since the introduction of the child care subsidy (CCS) reform last year, services have become much more affordable for parents (see chart below). As a quality operator, we believe TNK is well positioned to benefit from this.

We hold TNK as a research-driven investment within WAM Microcap. TNK shares are up 20.9% for the calendar year. We recently participated in a TNK placement at a discounted price of \$1.58 per share reserved for sophisticated investors. TNK is currently trading at \$1.68 per share.



Source: Charter Hall Education Trust (ASX: COE), Investor presentation, 26 March 2019



### Inverted yield curve – what is the fuss all about?

If you are unsure of what a “yield curve inversion” is, you are not alone. Google searches for the term have [spiked](#) this month, close to the highest levels in over a decade. This is

important as each of the last nine US recessions were preceded by the yield curve inverting. As a result, some market participants use the comparison between short-term and long-term bond yield curves as a barometer into the overall state of the economy

### What is it and why does it matter?

In normal circumstances, the yield for longer-term bonds is higher than the yield for shorter-term bonds in order to compensate an investor for the additional risk for locking their money away for a longer period of time. If the yield on longer-term debt becomes less than shorter-term debt, the yield curve is inverted. On 22 March, the US 10-year treasury bond yield fell below the US three-month yield for the first time in over a decade. As a further dampener, 18 countries are now sitting on negative yields for treasury bonds – reducing the ability for central banks to stimulate the economy through further interest rate cuts. On average, the US yield curve inverts 14 months prior to the onset of a US recession.

The Negative Bond Yield Matrix													
Country	6-Mo	1-Year	2-Year	3-Year	4-Year	5-Year	6-Year	7-Year	8-Year	9-Year	10-Year	20-Year	30-Year
Switzerland	-0.89	-0.54	-0.77	-0.76	-0.75	-0.69	-0.65	-0.50	-0.55	-0.50	-0.41	0.03	0.15
Germany	-0.51	-0.58	-0.58	-0.56	-0.52	-0.42	-0.38	-0.29	-0.25	-0.17	-0.01	0.33	0.60
Japan	-0.22	-0.18	-0.18	-0.18	-0.18	-0.19	-0.19	-0.19	-0.19	-0.11	-0.09	0.34	0.51
Denmark	-0.60		-0.61	-0.58		-0.44			-0.29		0.07		1.02
Netherlands	-0.52		-0.56	-0.49	-0.38	-0.31	-0.20	-0.12	-0.01	0.08	0.18	0.44	0.64
France	-0.54	-0.54	-0.51	-0.42	-0.32	-0.21	-0.11	-0.07	0.11	0.23	0.36	1.00	1.36
Sweden	-0.40		-0.44			-0.20		-0.04			0.23	0.87	
Finland			-0.49	-0.41	-0.36	-0.25	-0.16		0.10		0.31		0.88
Belgium	-0.53	-0.54	-0.53	-0.45	-0.33	-0.25	-0.12	0.09	0.21	0.28	0.44	1.10	
Austria		-0.52	-0.52	-0.40	-0.31	-0.21	-0.13	0.01	0.07	0.17	0.28	0.72	1.04
Ireland	-0.19	-0.49	-0.45		-0.20	-0.06	0.06	0.21	0.45		0.60	1.17	1.37
Slovakia			-0.26			-0.01	0.06		0.39	0.58	0.64	1.45	
Spain	-0.36	-0.34	-0.27	-0.17	-0.04	0.07	0.40	0.62	0.79	0.91	1.09	1.71	2.25
Portugal	-0.37	-0.36	-0.26	-0.10	0.10	0.22	0.58	0.78	0.95	1.15	1.29	2.01	2.34
Malta	-0.20	-0.20		-0.10		0.15					0.93	1.87	
Bulgaria		-0.10		-0.25		0.20					0.70		
Slovenia		-0.22	-0.18			0.14					0.77		
Italy	-0.16	0.02	0.26	0.75	1.22	1.51	1.79	2.05	2.07	2.31	2.49	3.28	3.49

Source: Pension Partners Director of Research Charlie Bilello as at 25 March 2019

**Inverted Yield Curve (10-Yr minus 1-Yr) and Recessions  
(1956-Present, Monthly Closing Data)**

Recession Start	Recession End	Inverted Curve Before Recession?	First Yield Curve Inversion	Lead (Months)
Aug-57	Apr-58	Yes	Dec-56	8
Apr-60	Feb-61	Yes	Sep-59	7
Dec-69	Nov-70	Yes	Dec-67	24
Nov-73	Mar-75	Yes	Mar-73	8
Jan-80	Jul-80	Yes	Sep-78	16
Jul-81	Nov-82	Yes	Sep-80	10
Jul-90	Mar-91	Yes	Feb-89	17
Mar-01	Nov-01	Yes	Apr-00	11
Dec-07	Jun-09	Yes	Jan-06	23
<b>Average Lead Time</b>				<b>14</b>

Source: Pension Partners Director of Research Charlie Bielek as at 24 March 2019

If you would like to read more on the topic, the Federal Reserve Bank of New York has produced a [frequently asked questions](#) document and the Federal Reserve Bank of Richmond has written an [economic brief](#) on whether yield curves invert for reasons other than a recession.

livewire



Five quality small caps flying high

Lead Portfolio Manager Martin Hickson was featured in the [Australian Financial Review](#) discussing high performing small-cap companies listed on the ASX. You can also watch the full [Livewire](#) video.

### May 2019 Shareholder Presentations

We are looking forward to seeing you all at our semi-annual Shareholder Presentations. Please come along and feel free to bring guests who have an interest in hearing our views on the Australian and global equity markets, how we invest and how we make a difference for shareholders and the community.

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### Franking media

In recent franking news, [The Australian](#) reported that Labor's claim of alleged savings from their retirement tax is potentially modeled from out-of-date data that does not include the effects of the \$1.6 million cap on the tax-free threshold for superannuation. [Robert Gottlieb](#) also wrote that all investors would be worse off and that the flow-on effects have been underestimated. The [Daily Telegraph](#) covered how retirees living in New South Wales would be the most disadvantaged by Labor's proposed changes.

Kind regards,

Lead Portfolio Managers

Martin Hickson



Oscar Oberg



Catriona Burns



Matthew Haupt



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