



# Market Watch

## July 2018

2 July 2018

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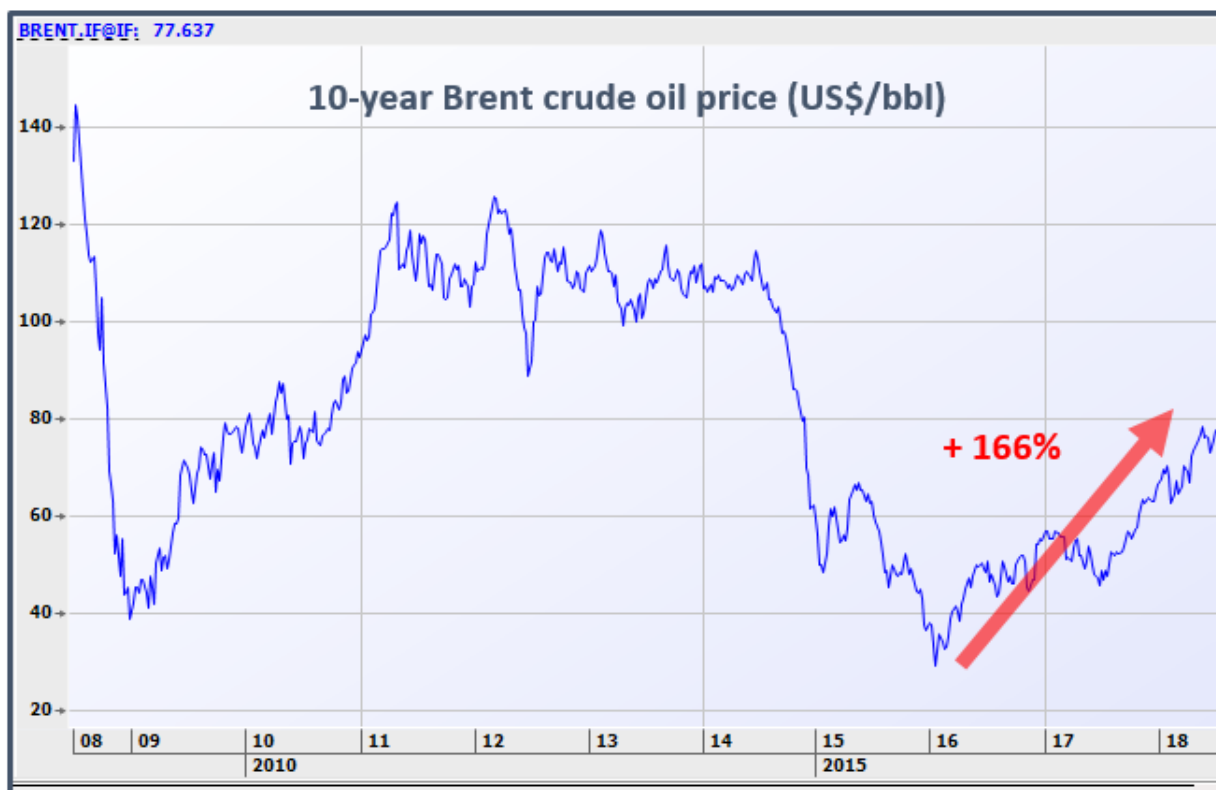
### Editor's Note

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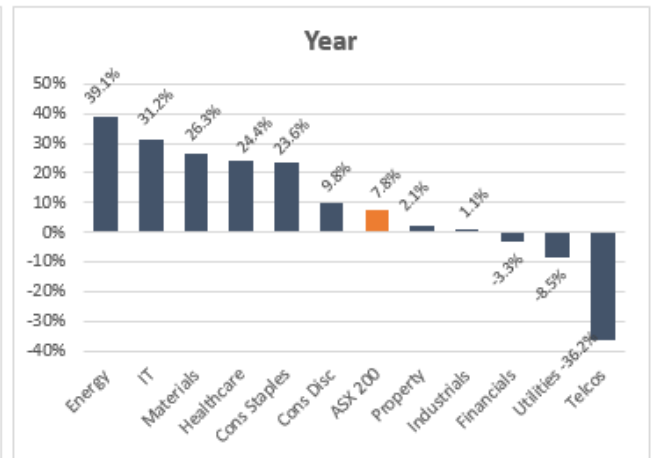
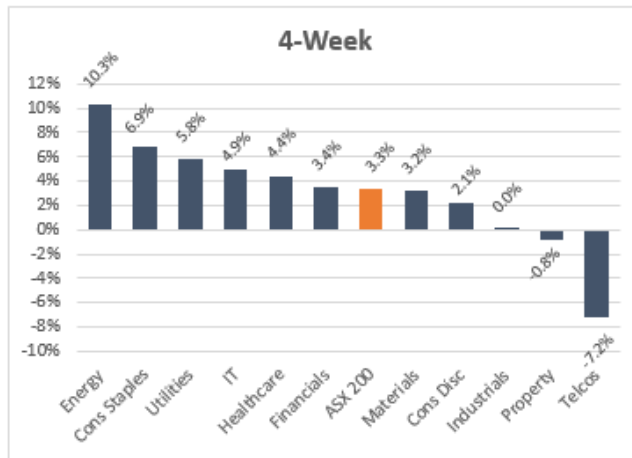
Brent crude oil prices have recovered strongly (+166%) from a low of ~US\$30/bbl in January 2016 to current price levels of US\$77/bbl. Goldman Sachs is bullish on the commodity, and in a recent research note, forecasts that higher oil prices are here to stay. Against this encouraging backdrop of stable, higher oil prices, Goldman Sachs advised investors to pour into US and Canadian oil plays. We agree the outlook for oil prices is looking attractive – particularly from a supply perspective. While OPEC recently agreed at its latest meeting in Vienna to increase world oil production by 1% (the equivalent of 1 million barrels per day) from July 2018, the increase is smaller than some market commentators expected. In addition, the threat of sanctions against Iran could curb global supplies by up to 1.3Mbpd from this key oil producer. The socioeconomic problems at Venezuela, another important global oil producer, are ongoing and unlikely to be resolved in the short-term. On the other hand, the US shale oil industry - which accounted for ~80% of total global output growth in 2017/2018 – falls outside OPEC's sphere of influence and diminishes OPEC's ability to "bully" the market to its will. The biggest near-term demand negative, we believe, is the potential for an escalation in the US-China trade war.

The varied supply/demand factors make up a conducive environment for speculation in the world's largest screen-traded commodity; speculation by itself could lead to sharp fluctuations in the oil price.

Looking at ASX-listed energy plays, the most upside is in the smaller developers/explorers. FAR Ltd's (ASX:FAR) IRESS consensus target price of 17cps offers some 55% upside potential; Karoon Gas's (ASX:KAR) IRESS consensus target price of A\$1.61 offers some 49% upside potential. The larger established plays Woodside Petroleum, Origin Energy, Santos and Oil Search appear fully valued relative to their IRESS consensus target prices. The big question is if the market has still to factor in a higher long-term oil price?

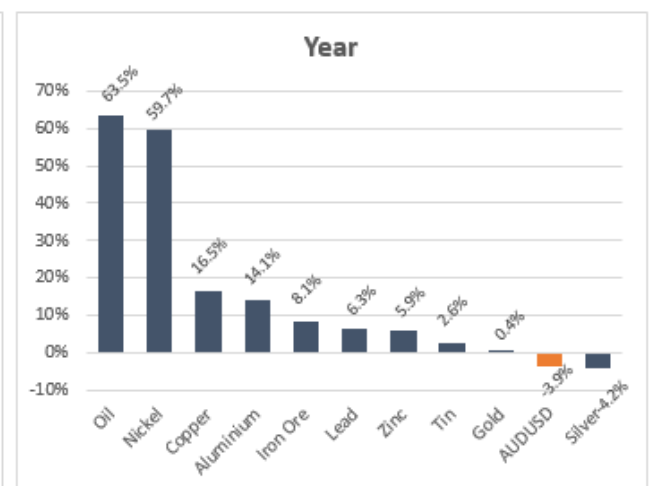
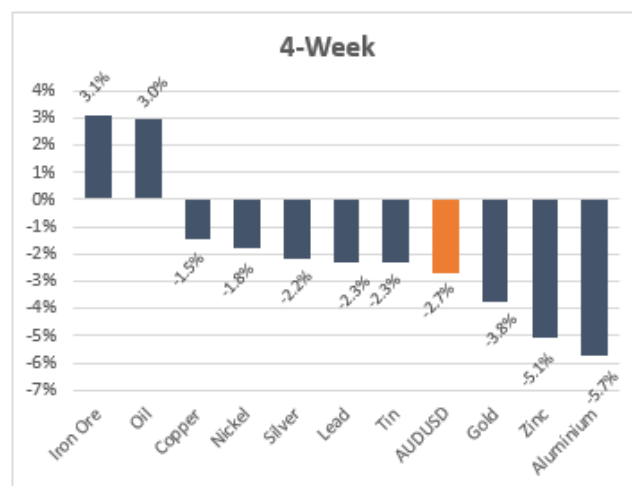


### ASX 200: sector performance over past four weeks and year



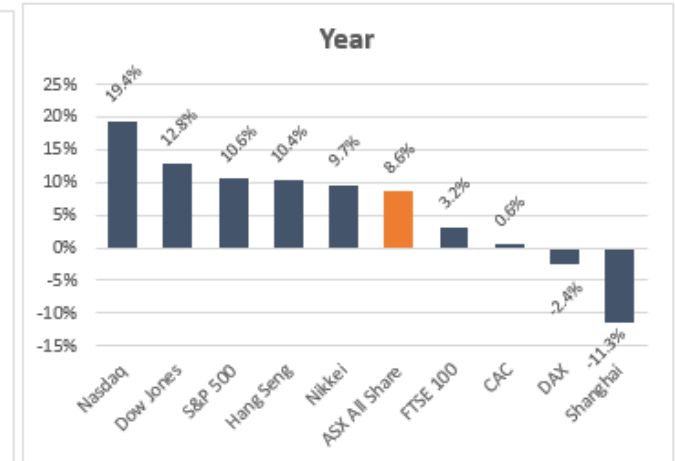
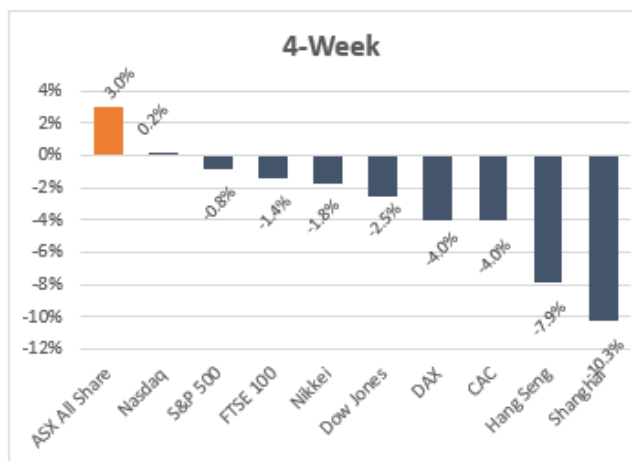
Source: IRESS, compiled by State One Stockbroking

### Commodities and AUDUSD: performance over past four weeks and year



Source: IRESS, compiled by State One Stockbroking

### World Indices: performance over past four weeks and year (local currency)

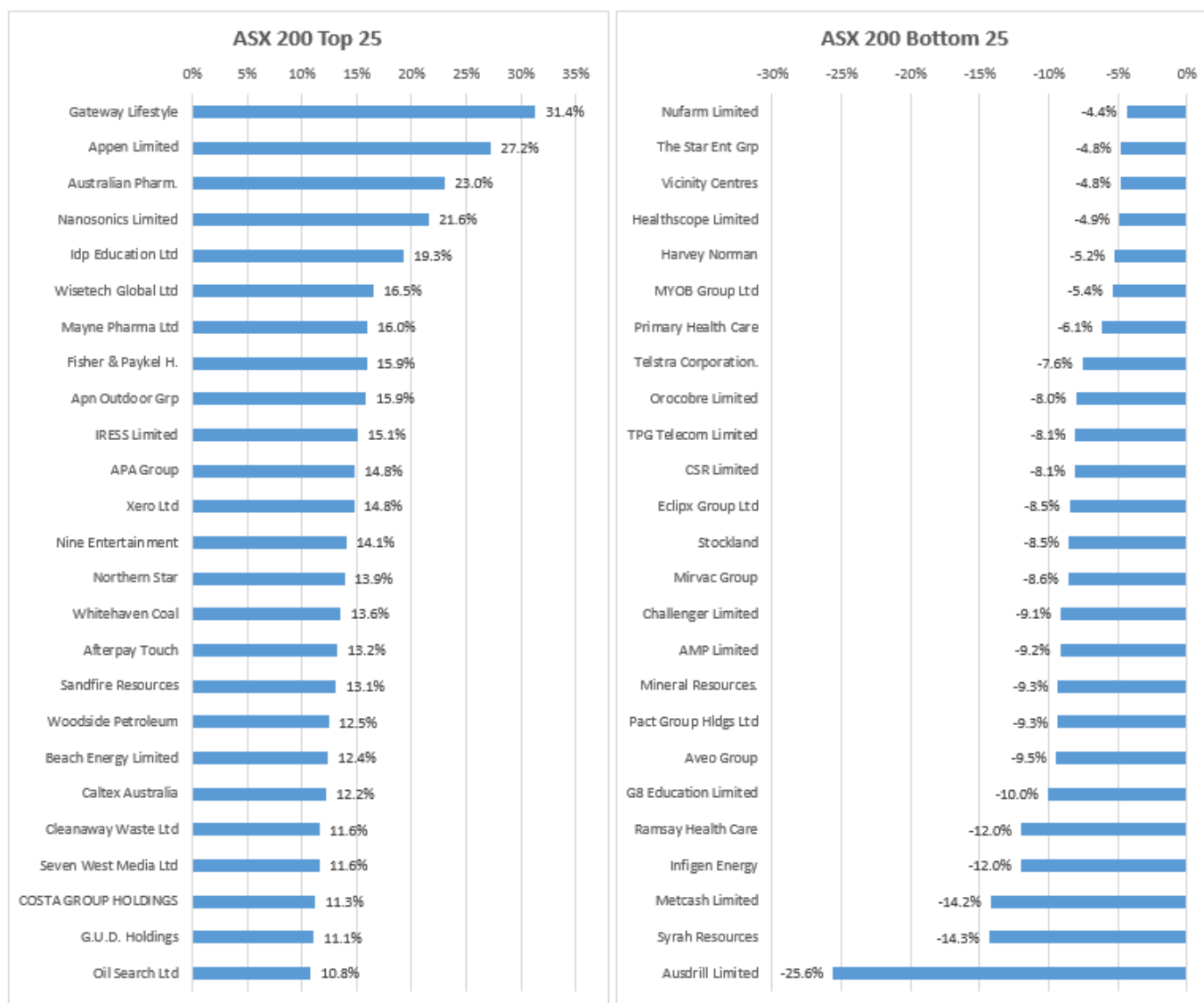


Source: IRESS, compiled by State One Stockbroking

## Commentary

- The FTSE/ASX 200 Index gained 3.3% in June, with the Telco sector posting negative (again); the Energy sector was the standout performer on renewed oil price gains.
- Commodities were mostly negative in June, although the two heavyweights – oil and iron ore – posted 3% gains. Precious metals fell as interest rate hikes in the US, and a strong US dollar weakened demand for safe-haven assets.
- ASX equities outperformed global indices in June. YTD, Australian equities have gained 8.6%, above average, but still a long way short of the buoyant US Nasdaq and Dow Jones.

### ASX 200: top 25 and bottom 25 performing stocks over the past four weeks (% gain/loss)



Source: IRESS, compiled by State One Stockbroking

- **Top performer:** Gateway Lifestyle (ASX: GTY) appreciated by 31.4% on the back of corporate activity with US bidder Hometown upping its offer to \$2.35 per share.
- **Worst performer:** Ausdrill Limited (ASX: ASL) down 25.6% on negative project updates at Hummingbird Resources, PMI, and KCGM (Super Pit).

## Month in review - events that caught our eye in June



Commonwealth Bank pays the biggest fine in Australian corporate history - A\$700m plus legal costs - after federal financial intelligence agency AUSTRAC accuses the bank of breaches in money laundering regulations.



Donald Trump and Kim Jong Un reach out to shake hands at the start of the first meeting between a sitting US President and his North Korean counterpart, at the Capella Hotel in Singapore.



Hong Kong-based CK Group makes a takeover bid for Australia's biggest gas pipeline operator APA Group (ASX:APA). The bid is likely to come under intense scrutiny from the ACCC and FIRB.



President Trump criticises Canadian Prime Minister Justin Trudeau on Twitter as being "weak and dishonest" in the wake of the two-day Group of Seven (G7) summit held in Quebec, Canada.



Telstra (ASX:TLS) announces 9,500 job cuts over the past three years - a quarter of the workforce - as part of a cost cutting exercise and to reposition into the 5G business.



US cable giant Comcast makes an all-cash US\$65bn offer to acquire 21<sup>st</sup> Century Fox, potentially scuppering Disney's US\$52bn all-stock offer.



The 2018 soccer World Cup kicked off with a 5-0 win for the host nation Russia against Saudi Arabia. Australia failed to make the qualifying rounds after losing 2-0 to Peru.



Bitcoin trading at US\$6,000 - a long-way south of its December 2017 high of US\$19,000. RBA verdict on bitcoin - "fascinating, admirable, but dead risky". Recent falls due to more hacking attacks on South Korean exchanges Bithumb and CoinRail.



While the Brexit referendum happened two years ago, it remains a confusing mess, sharply dividing the British public, with 100,000 people demonstrating against it in London.



# Technical Analysis vs Fundamental Analysis



## What is Technical Analysis?

It is the practice of valuing stocks on past volume and pricing information.

Technical analysis assumes the following:

Market value of the asset reflects supply and demand of the asset.

Supply and demand are driven by rational factors, such as data and economic analysis, as well as irrational factors, such as guesses.

Markets and individual stocks move together given trends.

Shifts in supply and demand will shift the trends in the market and can be detected in the market.

## What is Fundamental Analysis?

Fundamental analysis takes a more formal approach. Fundamental analysts review the financial statements of a company and generate metrics, such as price-to-book value and enterprise value-to-EBITDA to value a security.

## Technical vs. Fundamental Analysis

The main difference between technical analysis and fundamental analysis is the use of financial statements to value equities. Technical analysis is the practice of valuing stocks on past volume and pricing information. Technical analysis combines both the use of past information (how stocks have reacted previously) and "feeling" (how the market is moving) to value the security.

### Advantages of Technical Analysis:

- Easy to understand and can be performed relatively quickly, especially with the aid of one of the many types of charting software.
- Does not rely on the use of financial statements for valuation purposes.
- Rather than strict fundamental valuation, technical analysis considers the "feeling" of the market, which is subjective.

### Challenges to Technical Analysis:

- The past is not always an indication of future results, calling into question the validity of technical analysis.
- Technical analysis violates the premise of EMH (Efficient Market Hypothesis) because EMH believers assume that price adjustments happen too quickly to be profitable.

Technical indicators are used widely by traders to help them formulate their view on the market:

### 1. Contrary Opinion

Traders that follow this type of analysis view the majority as being incorrect and choose the opposite direction. One example is Mutual fund cash positions. Given a mutual funds holds a part of its assets as cash, traders monitor cash positions of mutual funds (reported monthly) and trade against them accordingly. To a trader, a large cash position in a mutual fund would be an indication to buy (mutual funds are bearish, hence trader would be bullish). Also, a large number of bearish investment advisory opinions would indicate it was time to buy, again taking the contrary view.

### 2. Smart Money

- Some investors are deemed smarter than others and, therefore, their money is considered "smart money". Traders typically follow the smart money. The following are viewed as smart-money indicators.
- An increase in margin debt would indicate that investors are becoming more bullish.

### 3. General Market

- Breadth of market is the measure of stock declines versus stock increases for the day, indicating direction (a technical indication for the market).
- Short interest is the measure of stocks sold short. If short interest increases, that is a bullish signal as investors will have to buy the stock to cover the shorts.



### 4. Stock Price and Volume Techniques

- **Dow Theory** - A theory which says the market is in an upward trend if one of its averages (industrial or transportation) advances above a previous important high, it is accompanied or followed by a similar advance in the other. The theory also says that when both averages dip below previous important lows, it's regarded as an indicator of a downward trend.
- **Support and Resistance** – This is a psychological view that a stock does not often trade above its support and resistance level. Traders monitor the levels for strategy. If a stock breaks out of its resistance level, it moves to the next resistance level.
- **Moving-average** measures the average moves of a stock over a specified time period. This measure removes daily fluctuations in a price change and the trend can be more readily discerned.

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