SHOULD WE BE WORRIED ABOUT RISK ASSETS?

QUEENSLAND TREASURY CORPORATION

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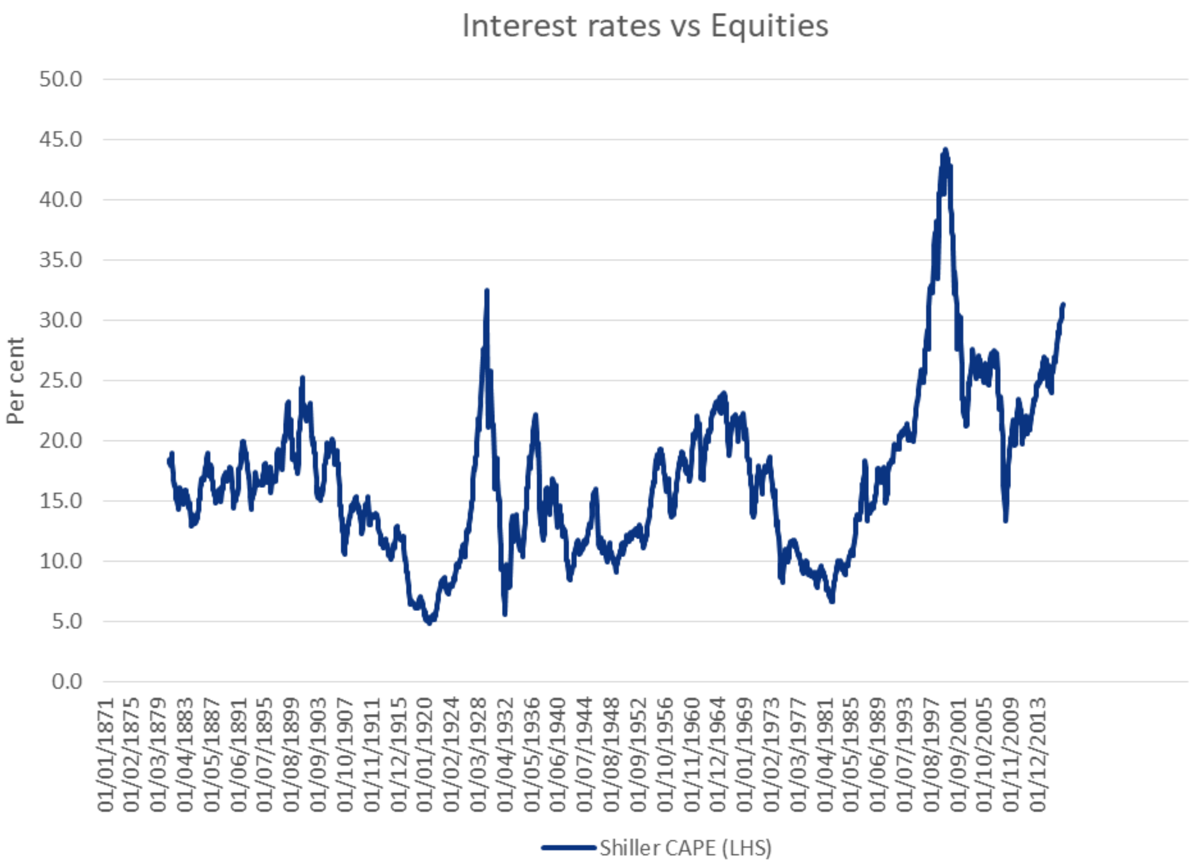
Should we be worried about risk assets?



- If you look at the price-earnings ratio in the US – a measure of how cheap or expensive stocks are to buy – US shares are close to being as expensive now as they were prior to the great depression.
- They do however remain well below the breathtaking peak reached prior to the dot-com bubble bursting.

Source: QTC, Robert Shiller.

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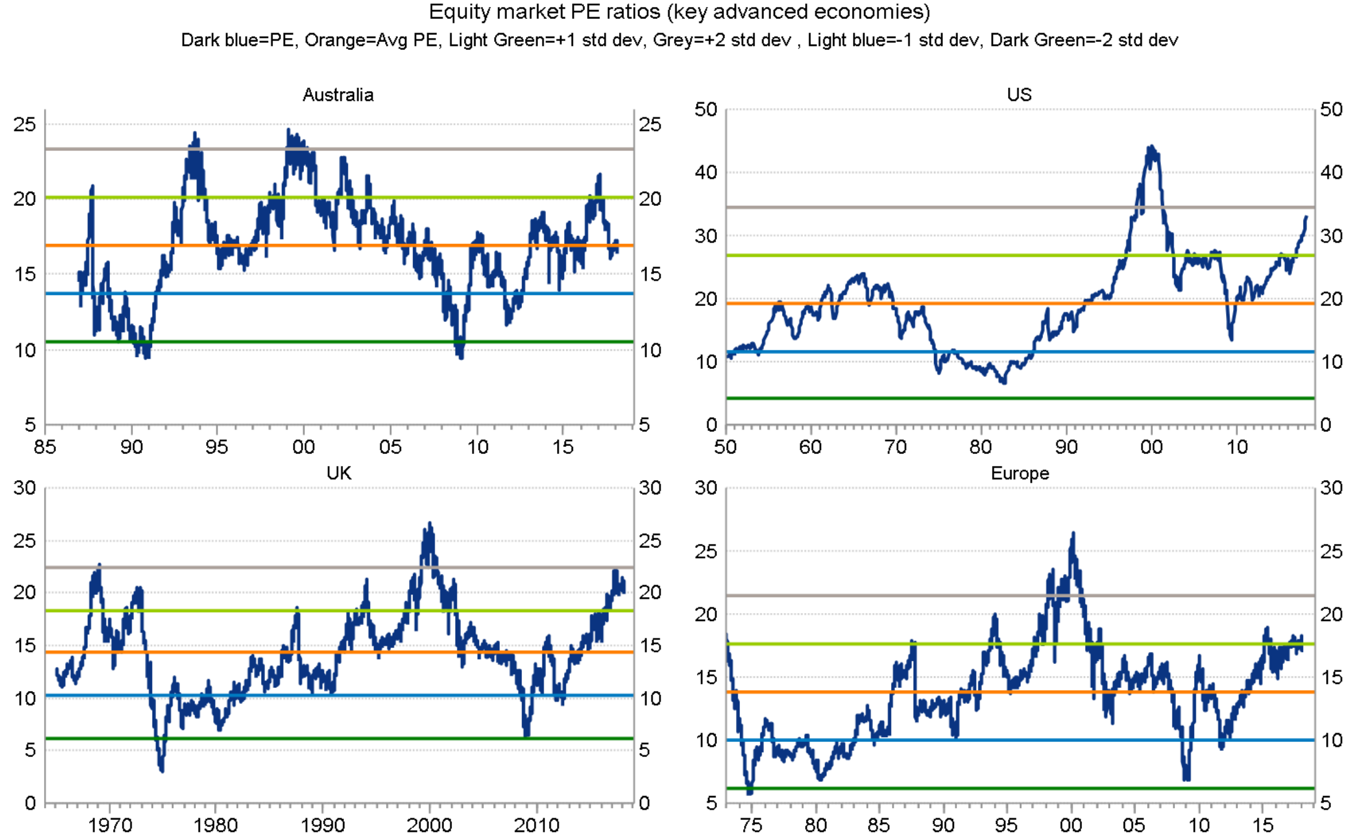

- The ratio of stock prices to earnings is between one and two standard deviations above long-run averages in key advanced economy markets.
- The one exception is Australia where prices are around average.

Source: QTC. This chart has been created in Thomson Reuters Datastream.

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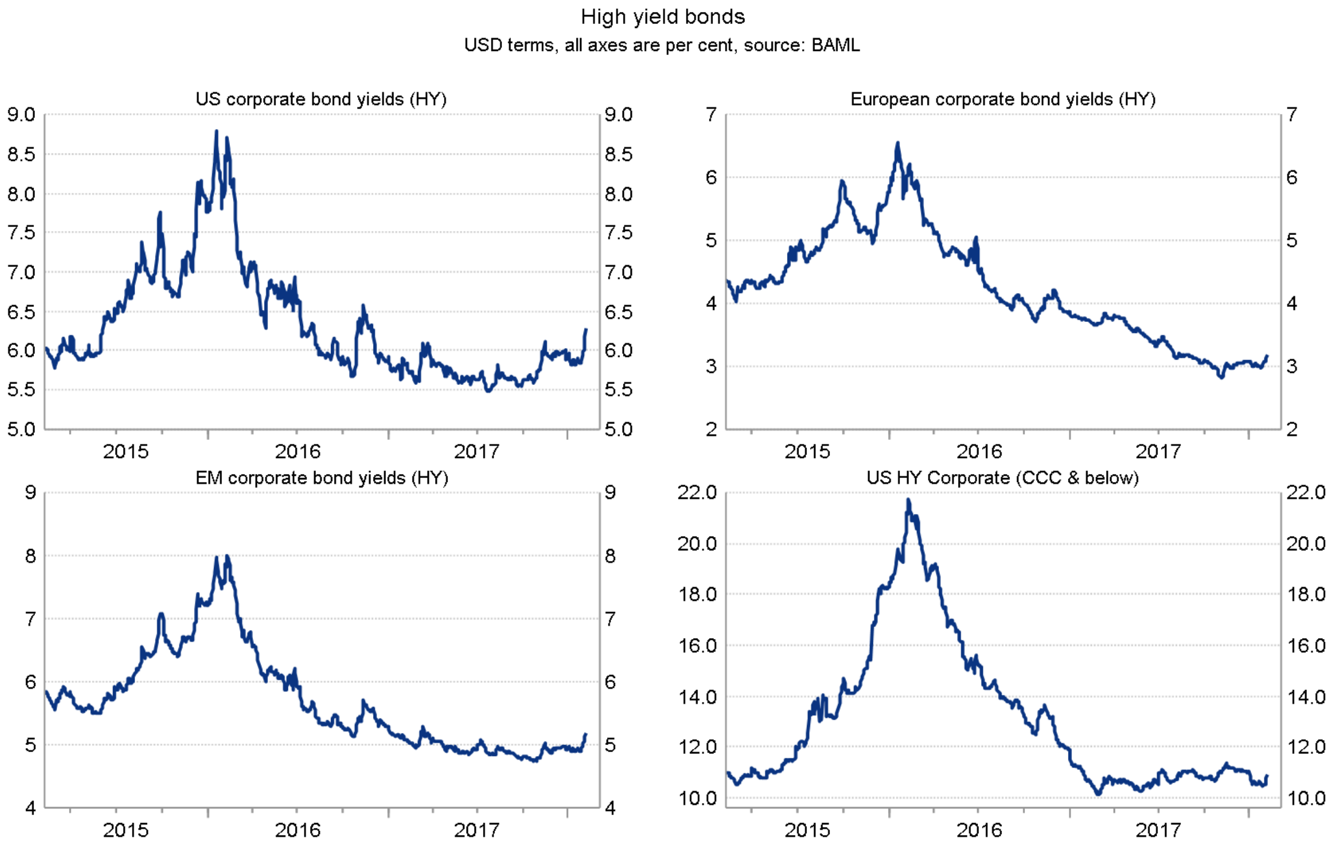

- Beyond equities the valuation of risky assets – such as the bonds of companies with lower credit ratings – are also high.
- This is evident in this chart which shows the yields on these bonds close to record lows, although they have increased a little of late.

Source: QTC. This chart has been created in Thomson Reuters Datastream.

Should we be worried about risk assets?

- The worst combination for risky assets such as stocks would be:
- Slowdown in growth (affects revenue)
- Productivity not picking up (affects profit margins)
- Inflation lifts & policy tightened…higher rates would:
    - Slow the economy and therefore revenue growth
    - Raise debt servicing costs
    - Boost the discount rate used in valuation models and therefore lower valuations
- Wages > inflation (affects profit margins)

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