



Breakout session A – Room 2

Thursday, 8 June 2017

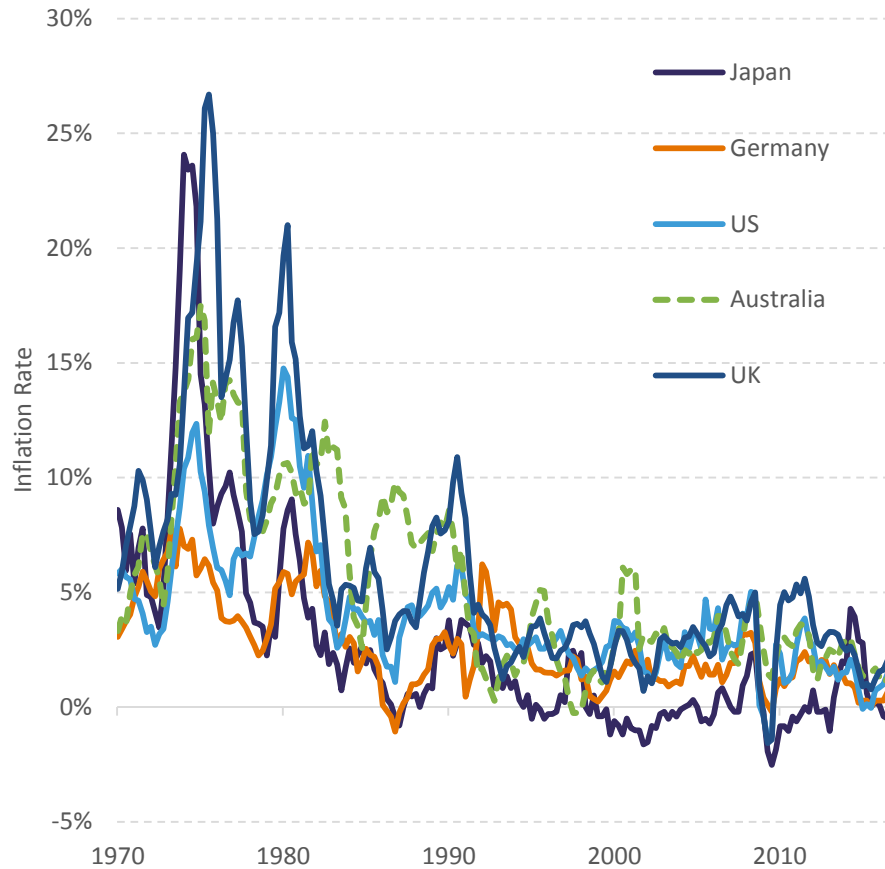


Alternative Debt in a Changing Inflation Environment

Presented on: Thursday, 8 June 2017

History of inflation

Downward shift in global inflation



Source: Datastream, Frontier

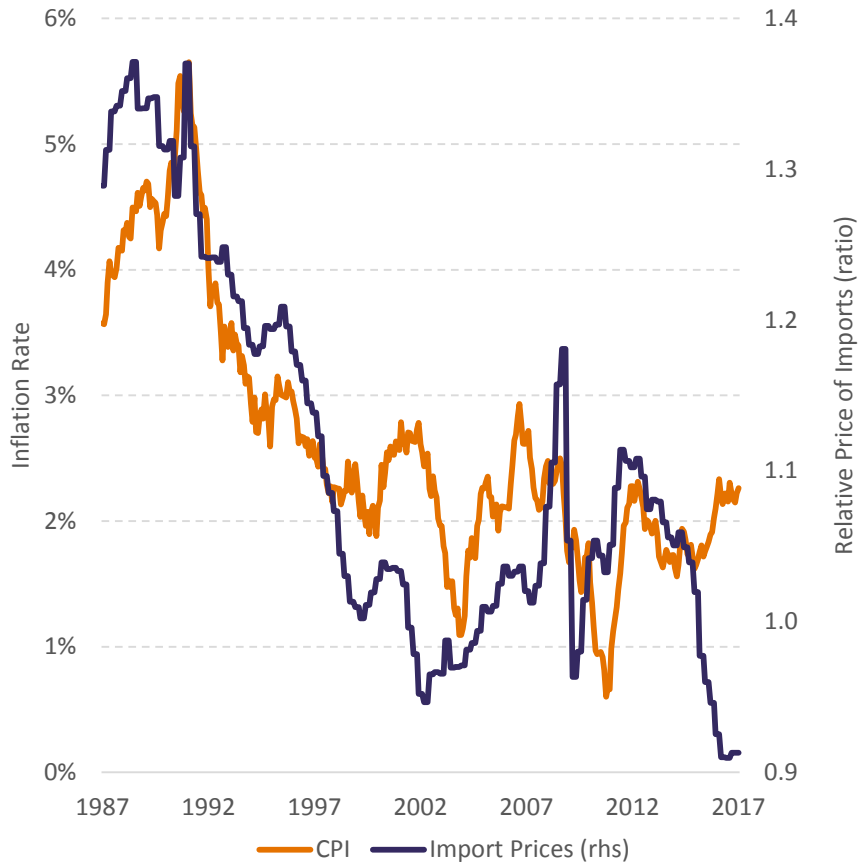
Early adopters of explicit inflation targets

Country	Adoption date	Inflation target (%)
New Zealand	1990	1-3
Canada	1991	2 (+/- 1)
UK	1992	2 (+/- 1)
Sweden	1993	2 (+/- 1)
Australia	1993	2-3
Czech Republic	1997	3 (+/- 1)
Israel	1997	2 (+/- 1)
Europe / ECB	1998	< 2
Brazil	1999	4.5 (+/-2)
Chile	1999	3 (+/- 1)
Colombia	1999	2-4
USA	2012	2 core PCE

Source: S. Roger, Finance and Development March 2010

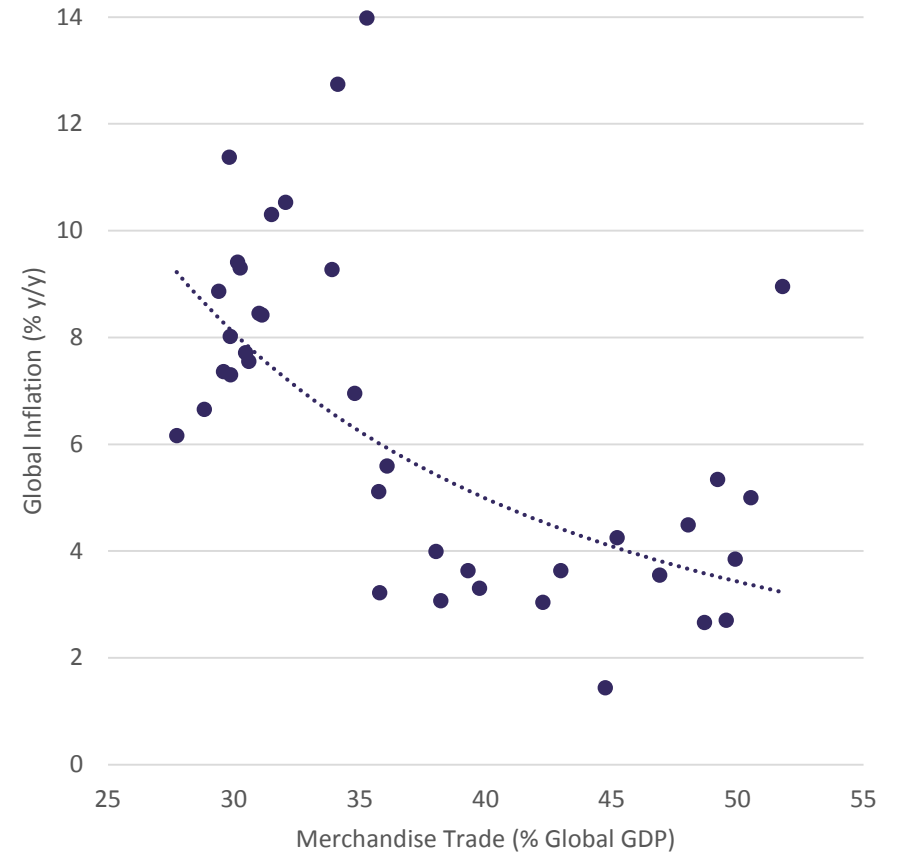
Global trade and inflation (1976-2015)

US inflation versus import prices/GDP deflator



Source: Datastream, Frontier

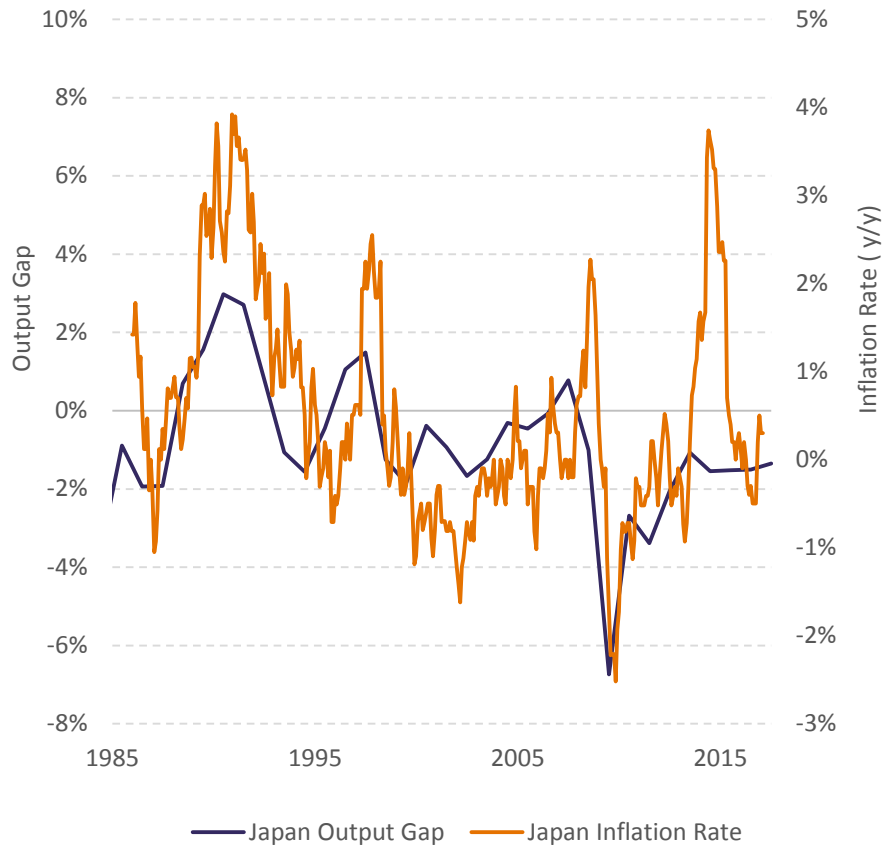
Global trade and inflation (1976-2015)



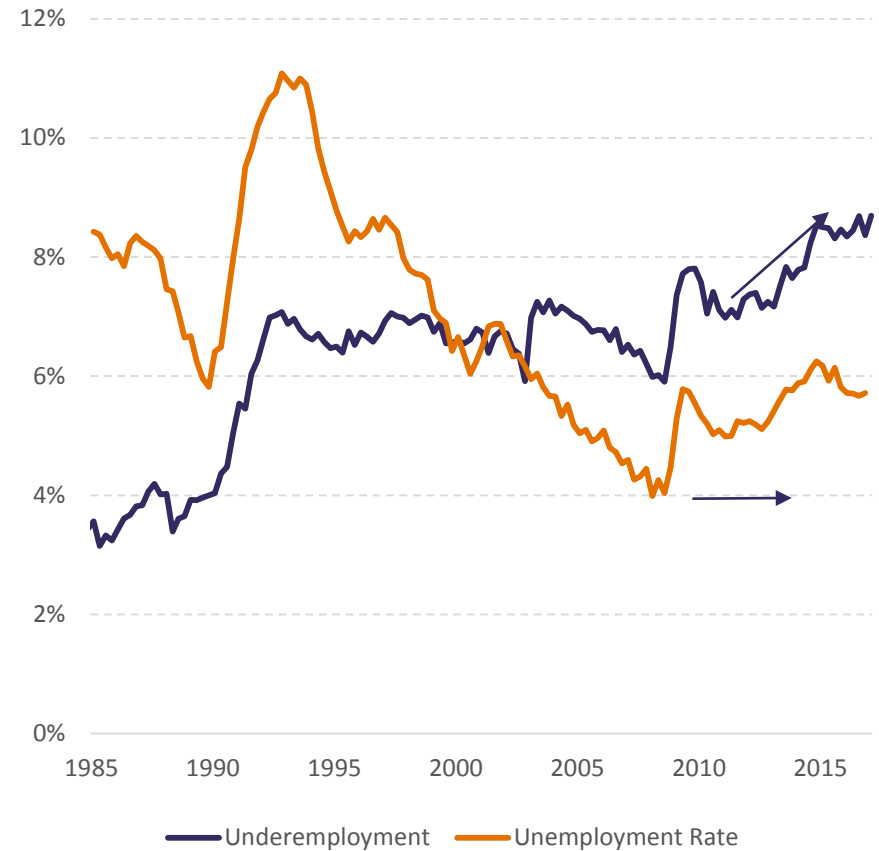
Source: Datastream, Frontier

Global spare capacity

Japan inflation and output gap



Australia unemployment and underemployment rate

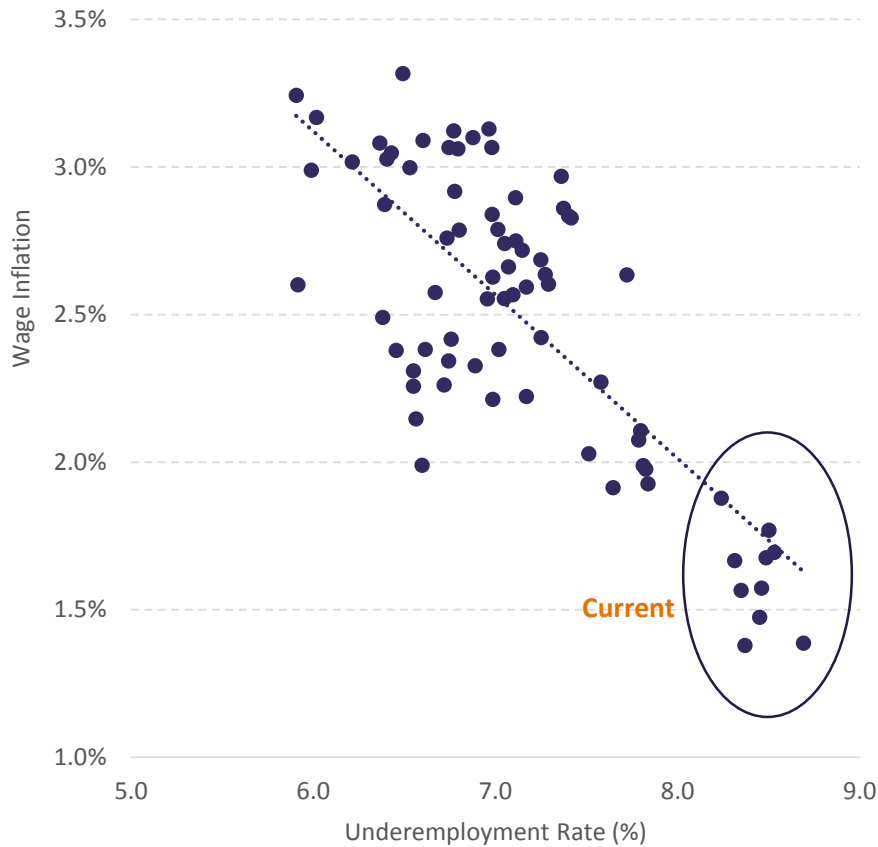


Source: Datastream, Frontier

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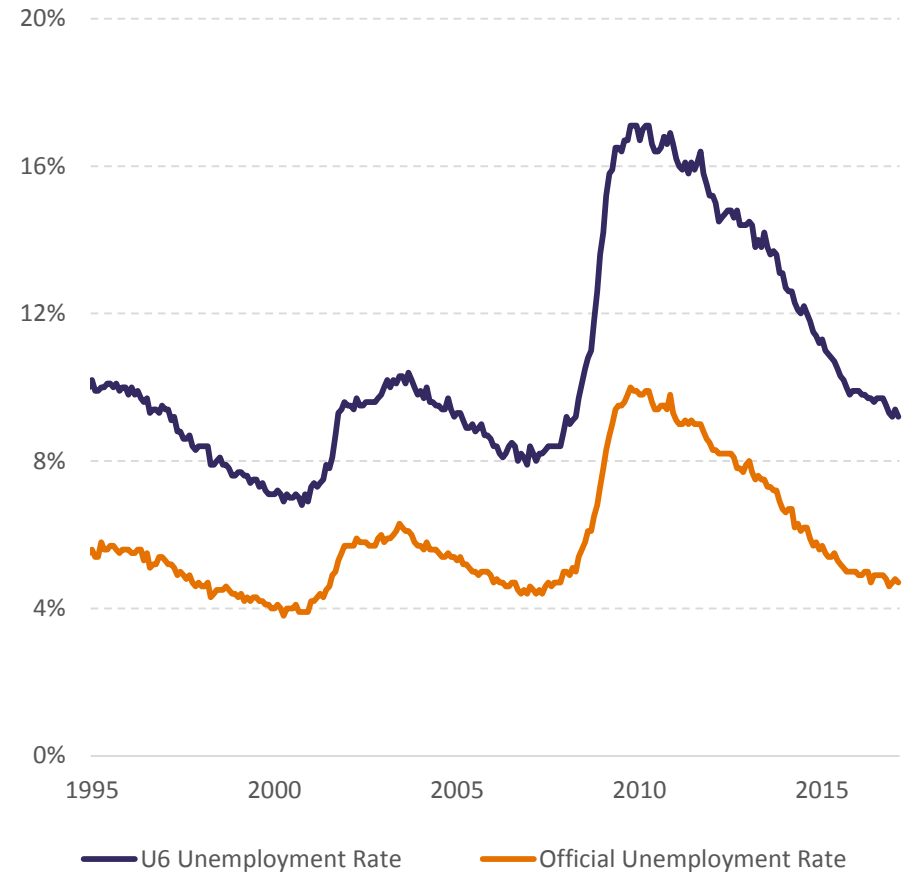
Underemployment

Australian wage inflation and underemployment rate



Source: Datastream, Frontier

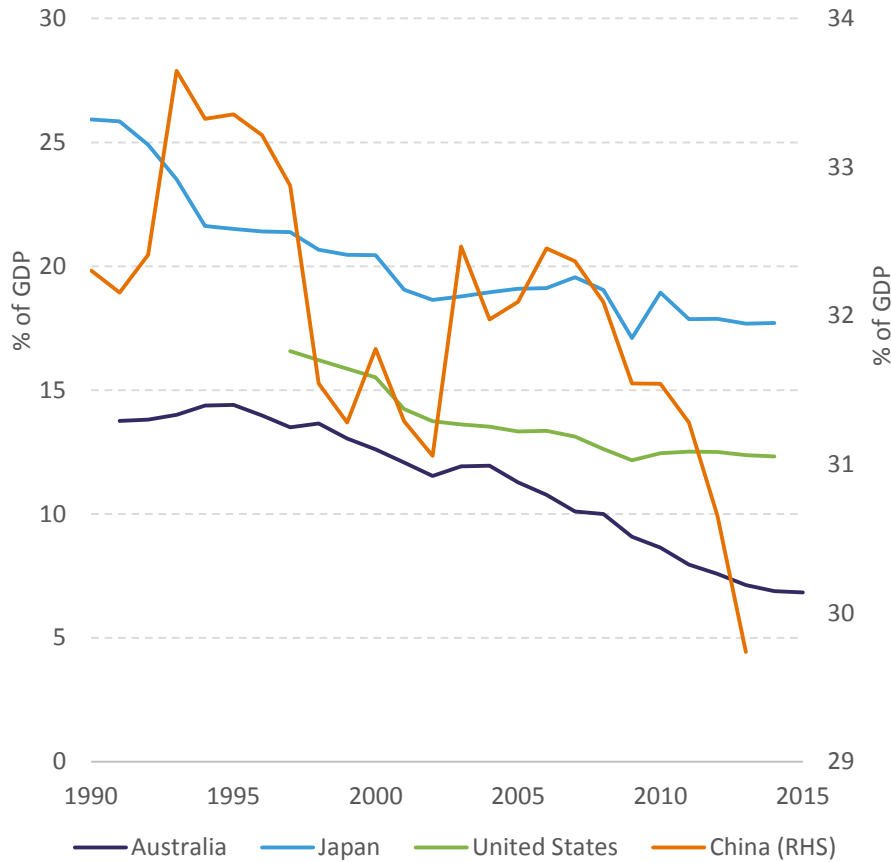
US unemployment rate



Source: FRED, Frontier

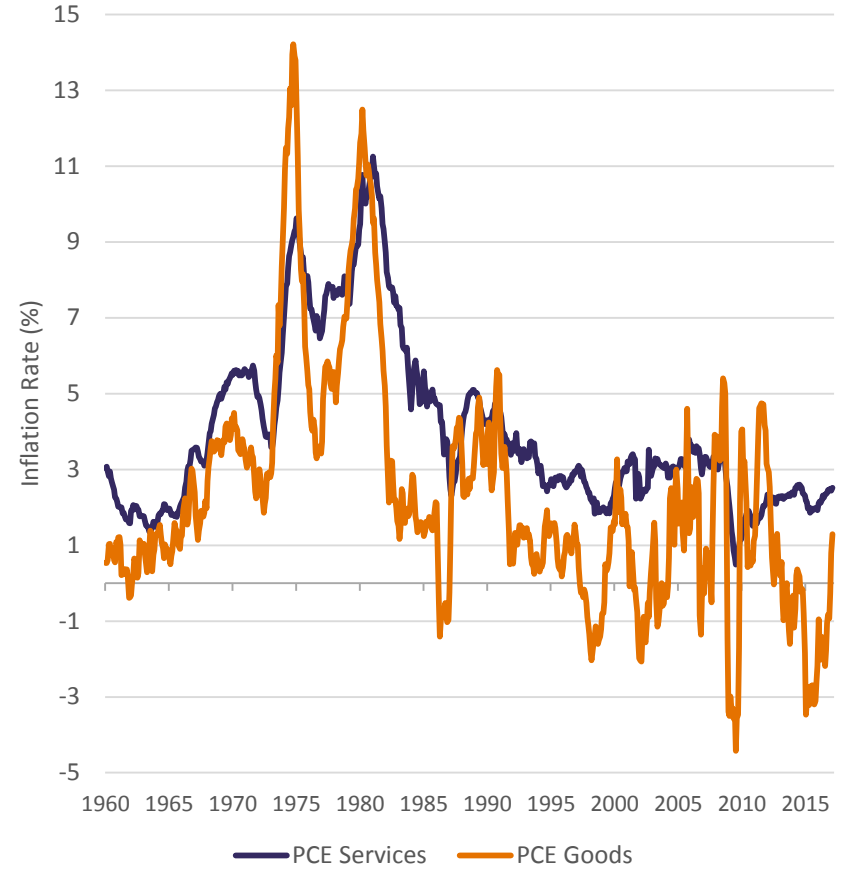
Services inflation

Manufacturing (% of GDP)



Source: OECD, World Bank

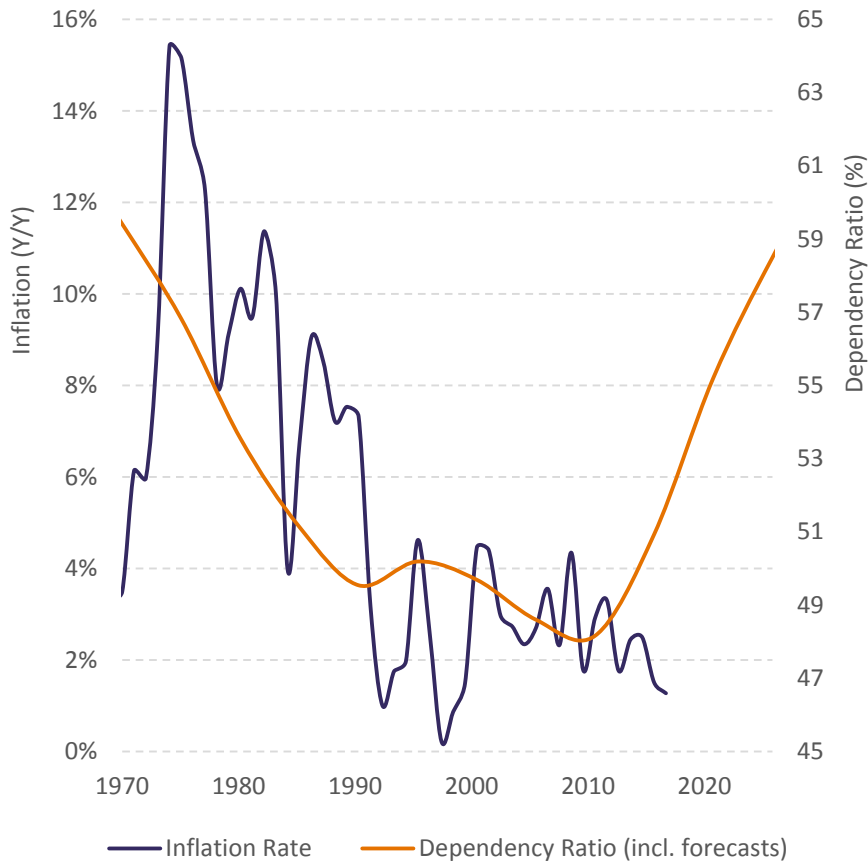
Services versus goods inflation



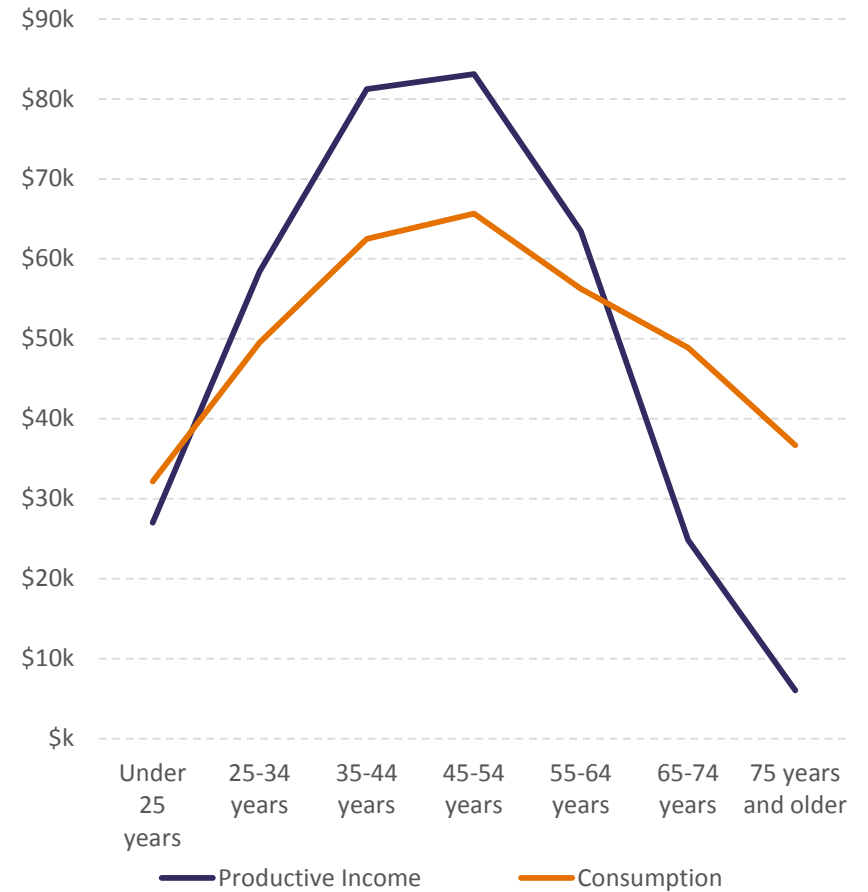
Source: Datastream, Frontier

Demographics

Australia's dependency ratio and inflation



Production/consumption by age US (2014)



Source: UN, Penn, Datastream, Frontier

Source: Frontier, US Bureau of Labor Statistics

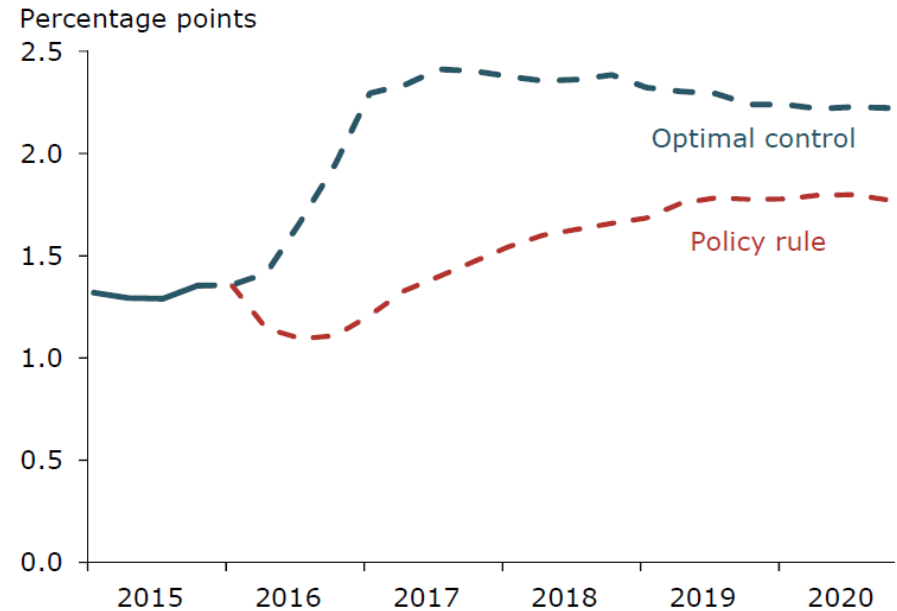
Peak globalisation and evolving central bank policies

Merchandise trade (% GDP)



Source: Datastream, Frontier

Median projections for core PCE price inflation

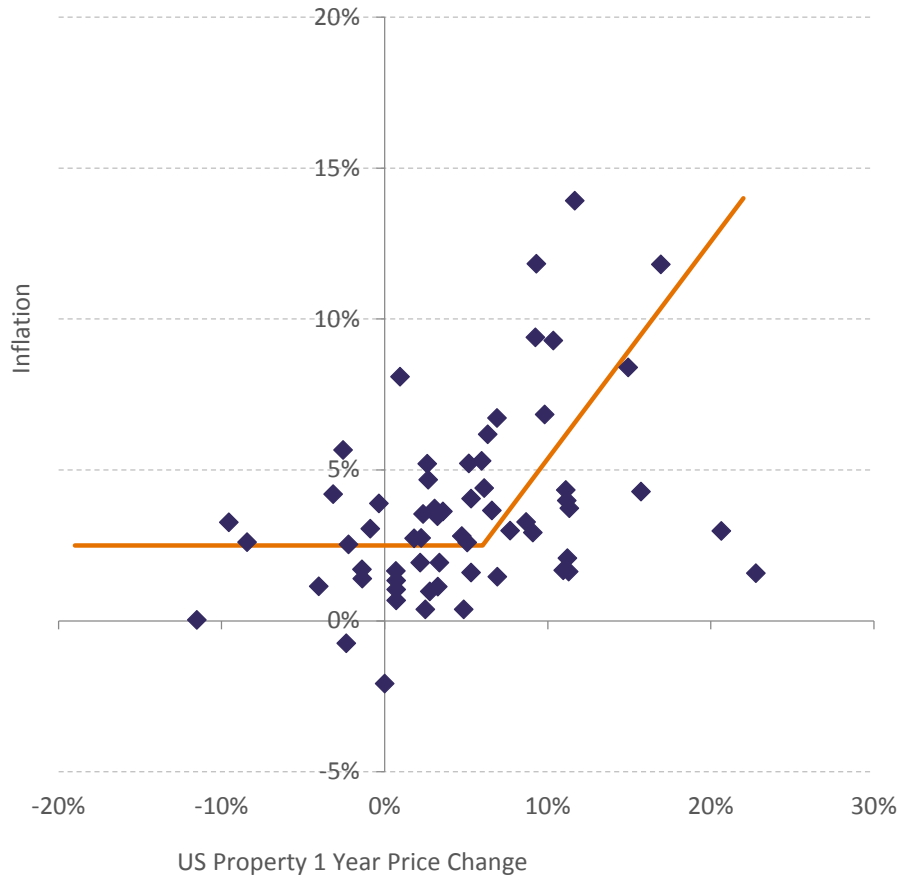


Note: Model-based median projections of four-quarter change in core personal consumption expenditures (PCE) price inflation.

Source: Federal Reserve Bank of San Francisco

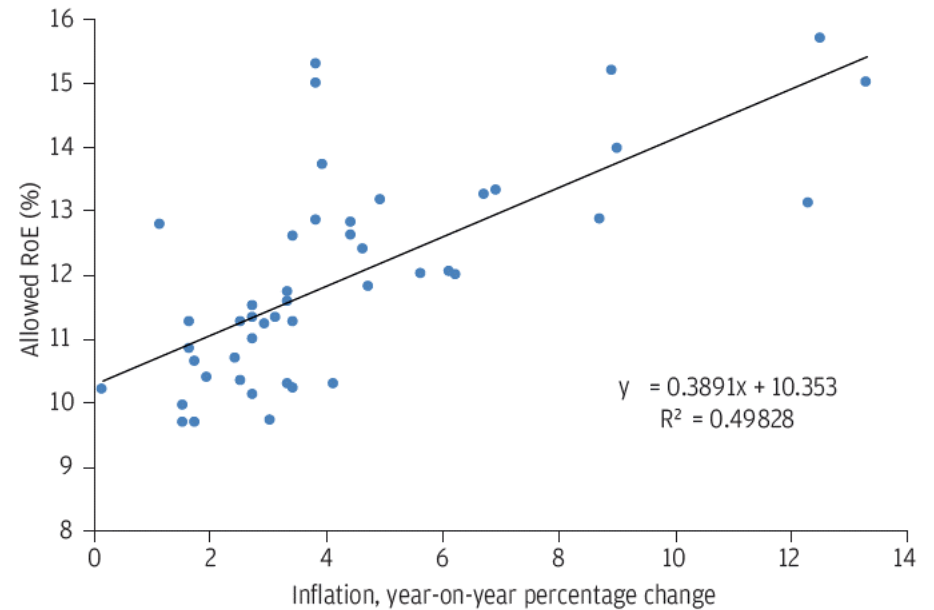
Asset class implications – mid risk real assets

US property price vs inflation (1950-2015)



Source: Frontier, BIS, FRED

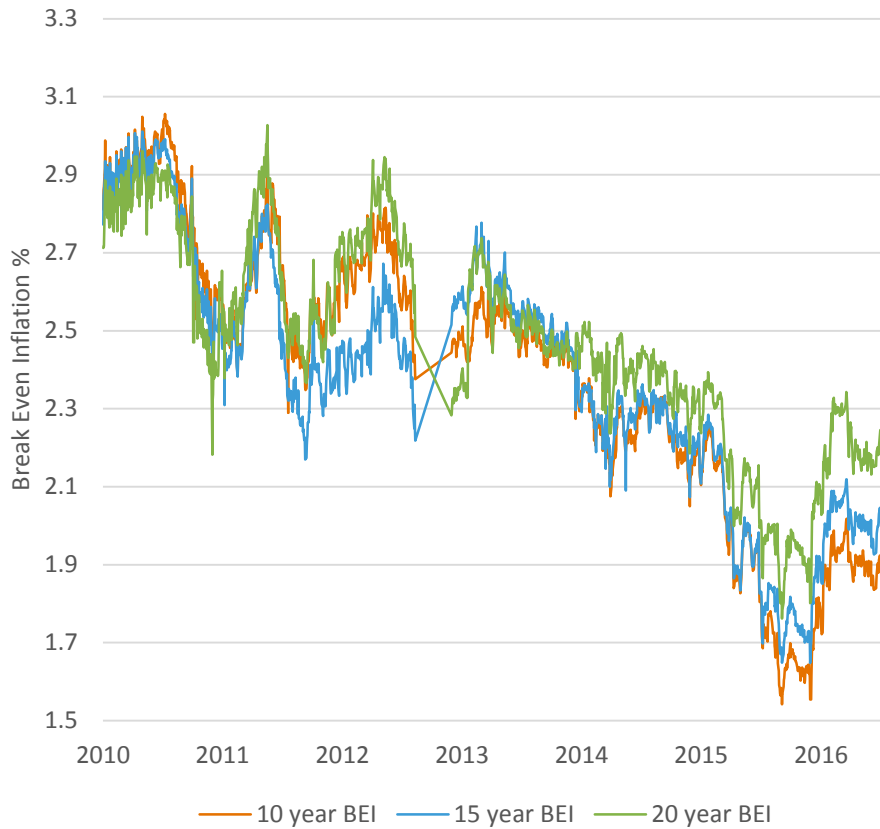
Inflation vs allowed ROE for US utilities



Source: JP Morgan

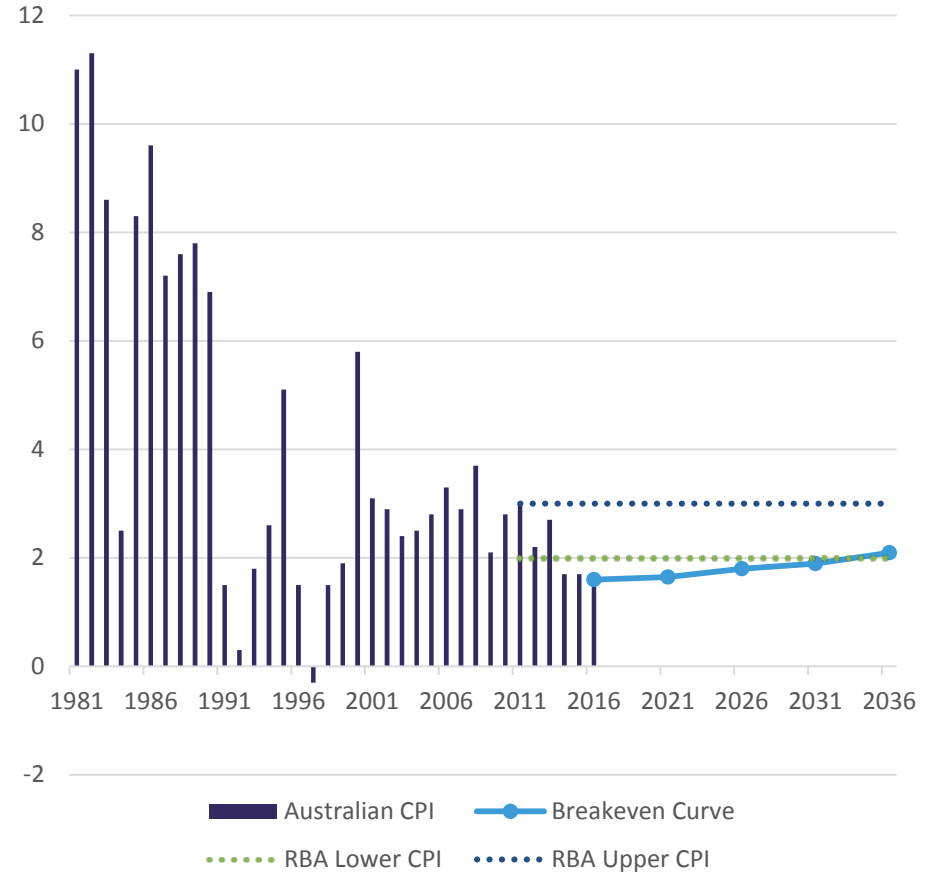
Inflation expectations are low....

Australian break even inflation



Source: Frontier, Bloomberg

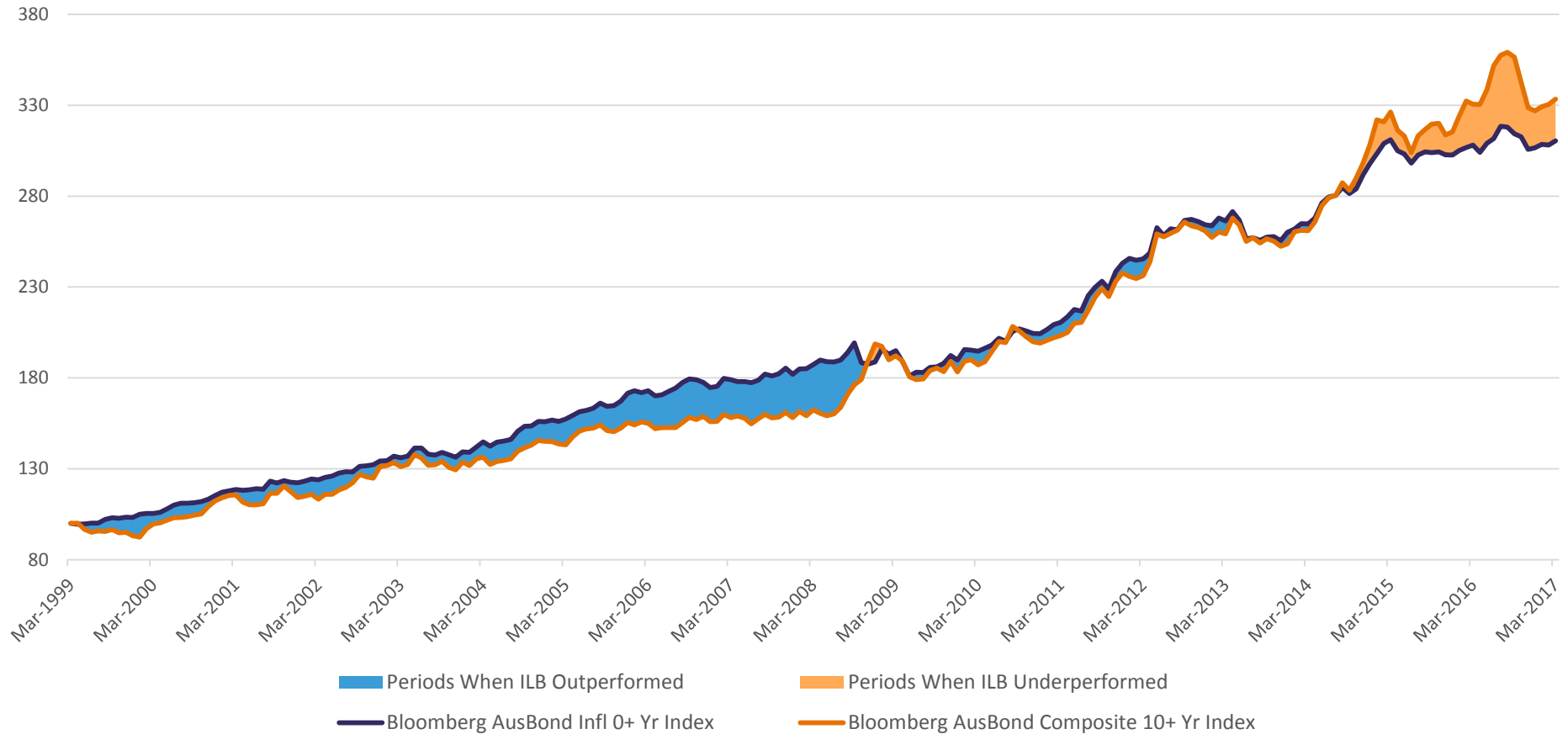
Forward looking break even curve



Source: Frontier, Bloomberg

Matching the duration.....ILB's versus nominals

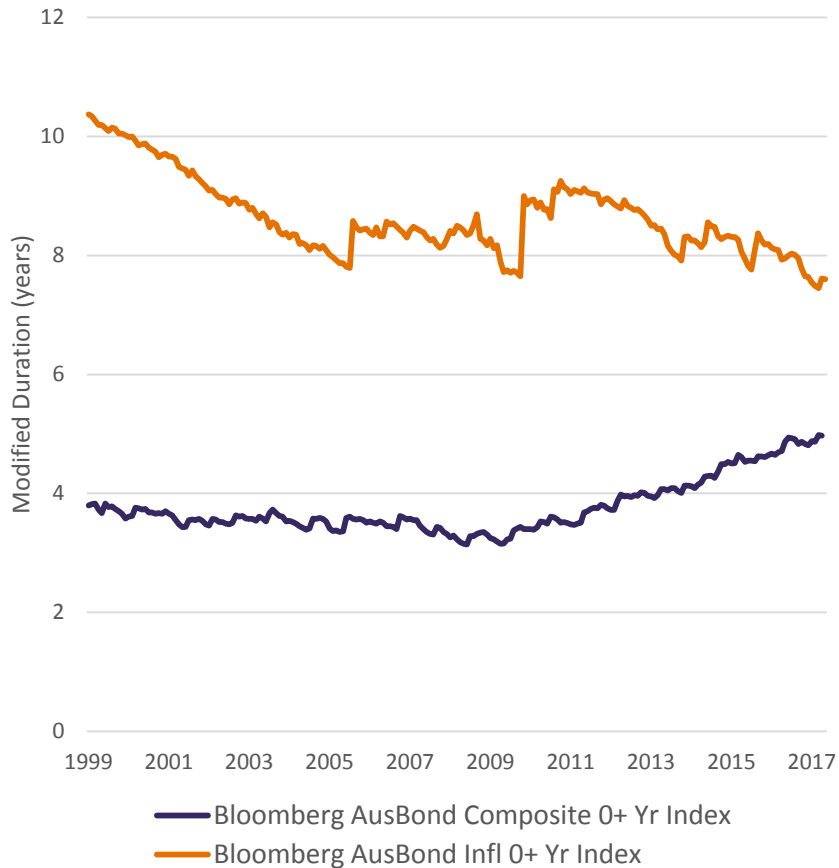
Performance of nominal bonds versus inflation linked bonds (duration matched)



Source: Frontier, Bloomberg

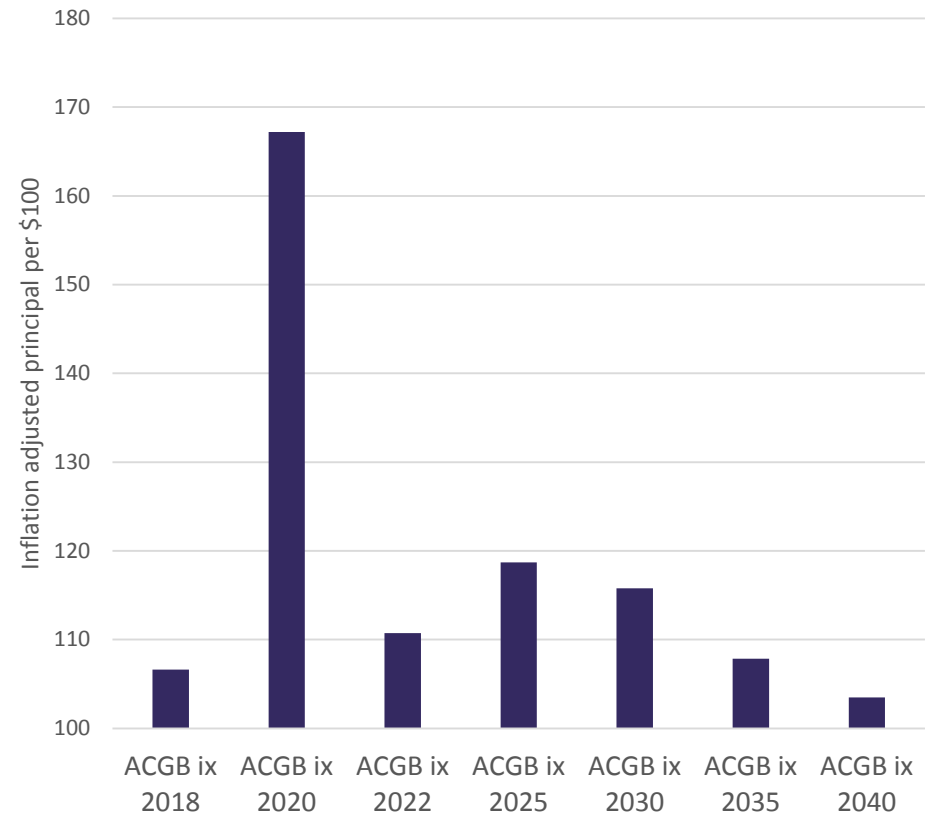
Active management is important in ILB's

Inflation Linked Bonds have significant duration



Source: Frontier, Bloomberg

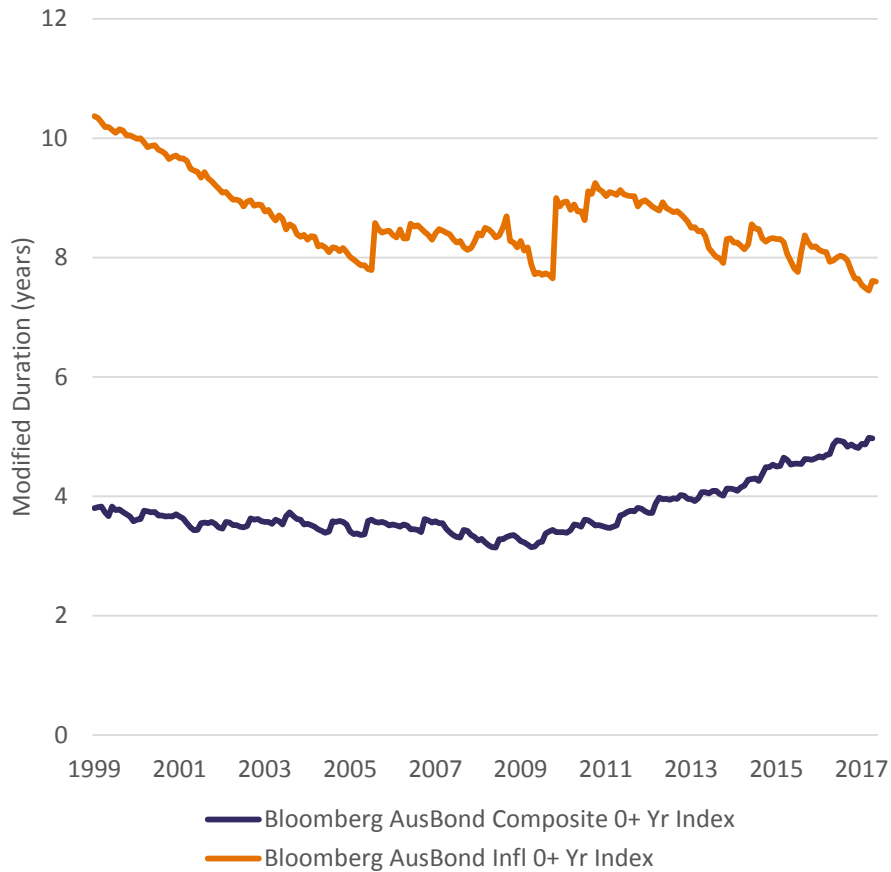
Seasoning in ILBs changes the Inflation profile



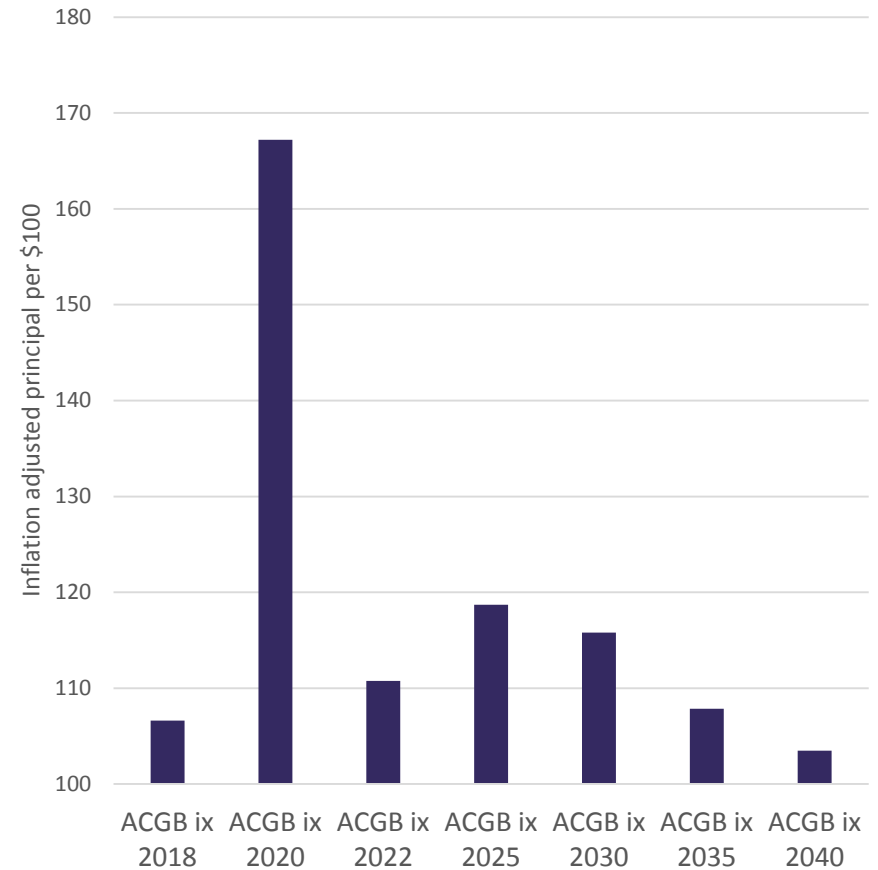
Source: Frontier, Bloomberg

Active management is important in ILB's

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Seasoning in ILBs changes the Inflation profile

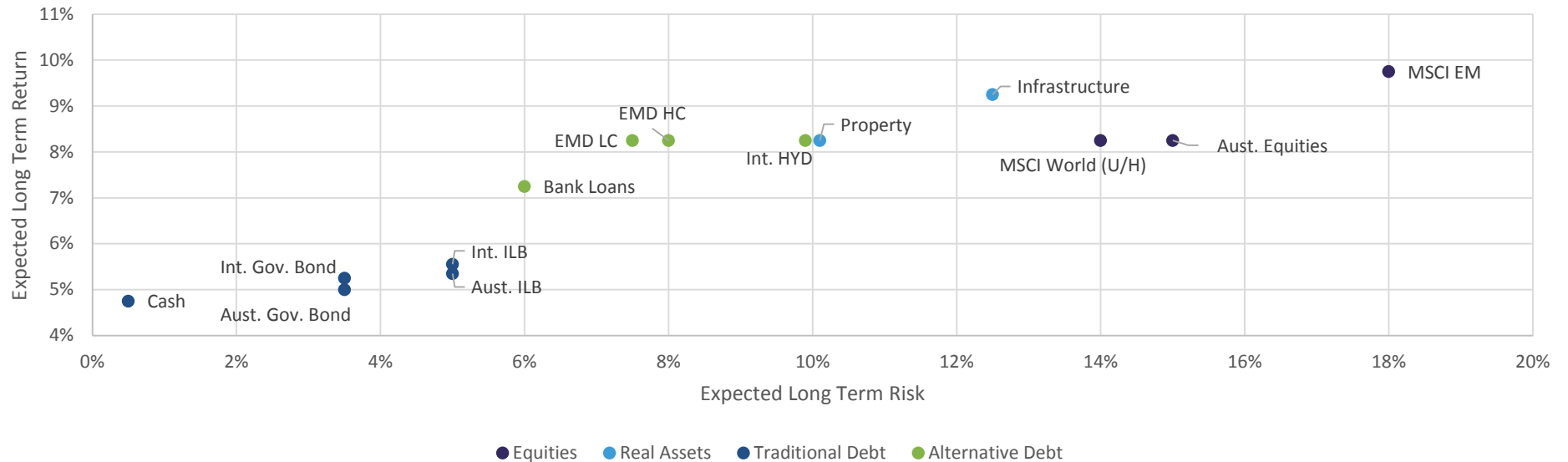


Source: Frontier, Bloomberg

Source: Frontier, Bloomberg

Long term capital market assumptions

Asset classes' long term expected risk and return

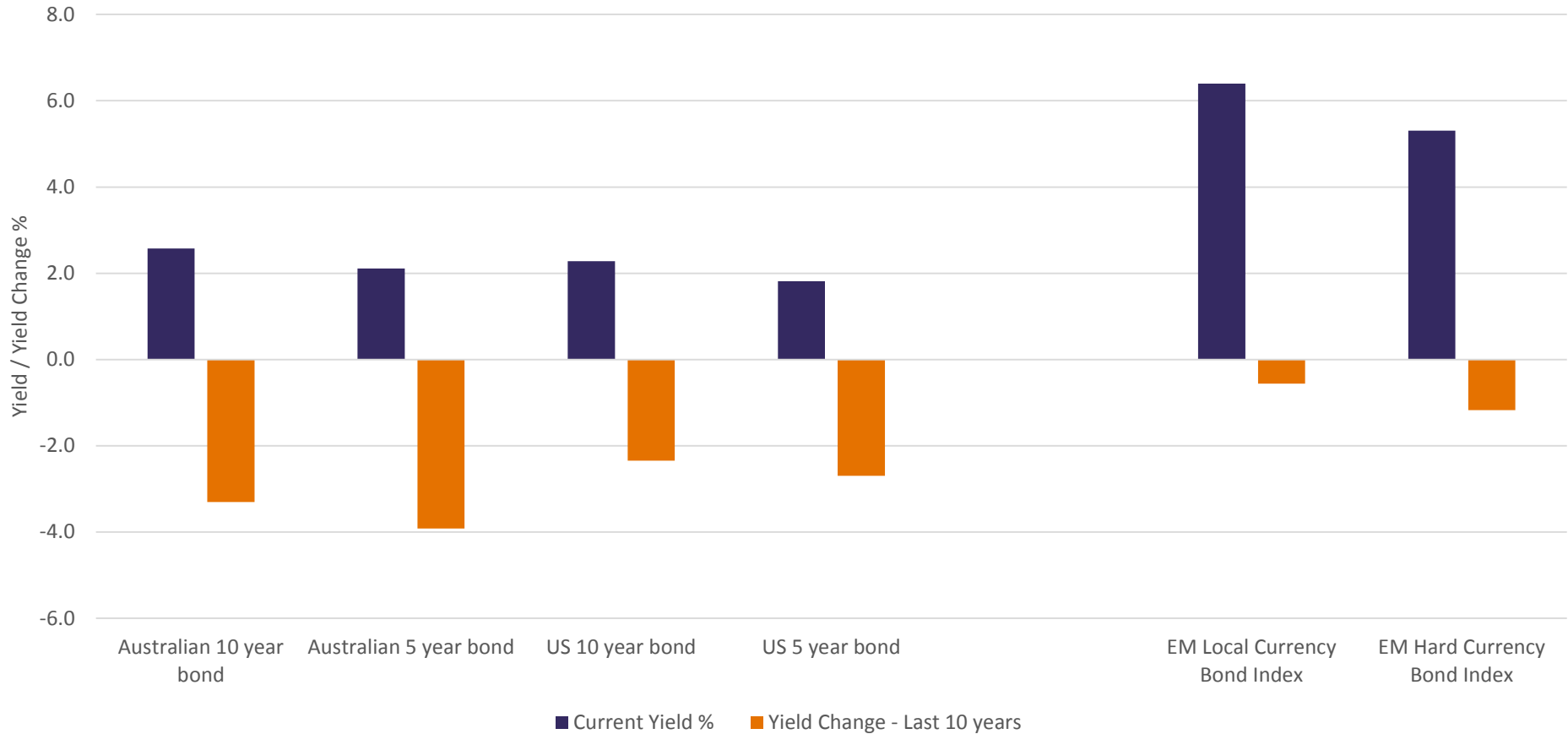


Annualised period returns	CMA (% p.a.)	3 years (% p.a.)	10 years (% p.a.)
Bank loans	7.25	5.7	6.8
International high yield debt (H)	7.75	7.1	9.8
Emerging market debt (sovereign hard currency) (H)	8.25	7.9	8.9
Emerging market debt (Sovereign local currency) (U/H)	8.25	2.9	4.7

Source: Frontier, Datastream, Bloomberg

Developed market government bonds have seen all the flows.....

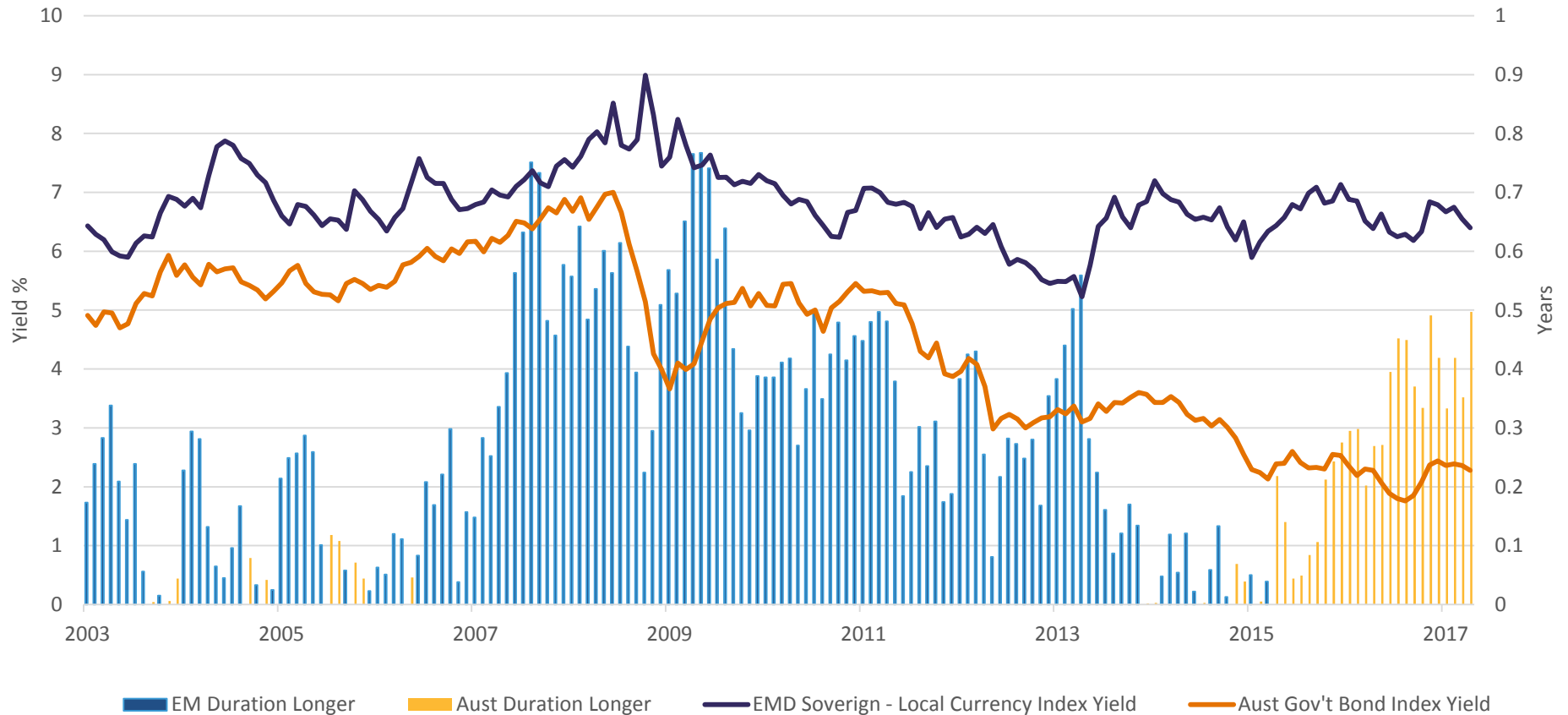
EM yields versus Australian and US bond yields



Source: Frontier, Bloomberg

EMD Local – Now more compelling for Australian investors

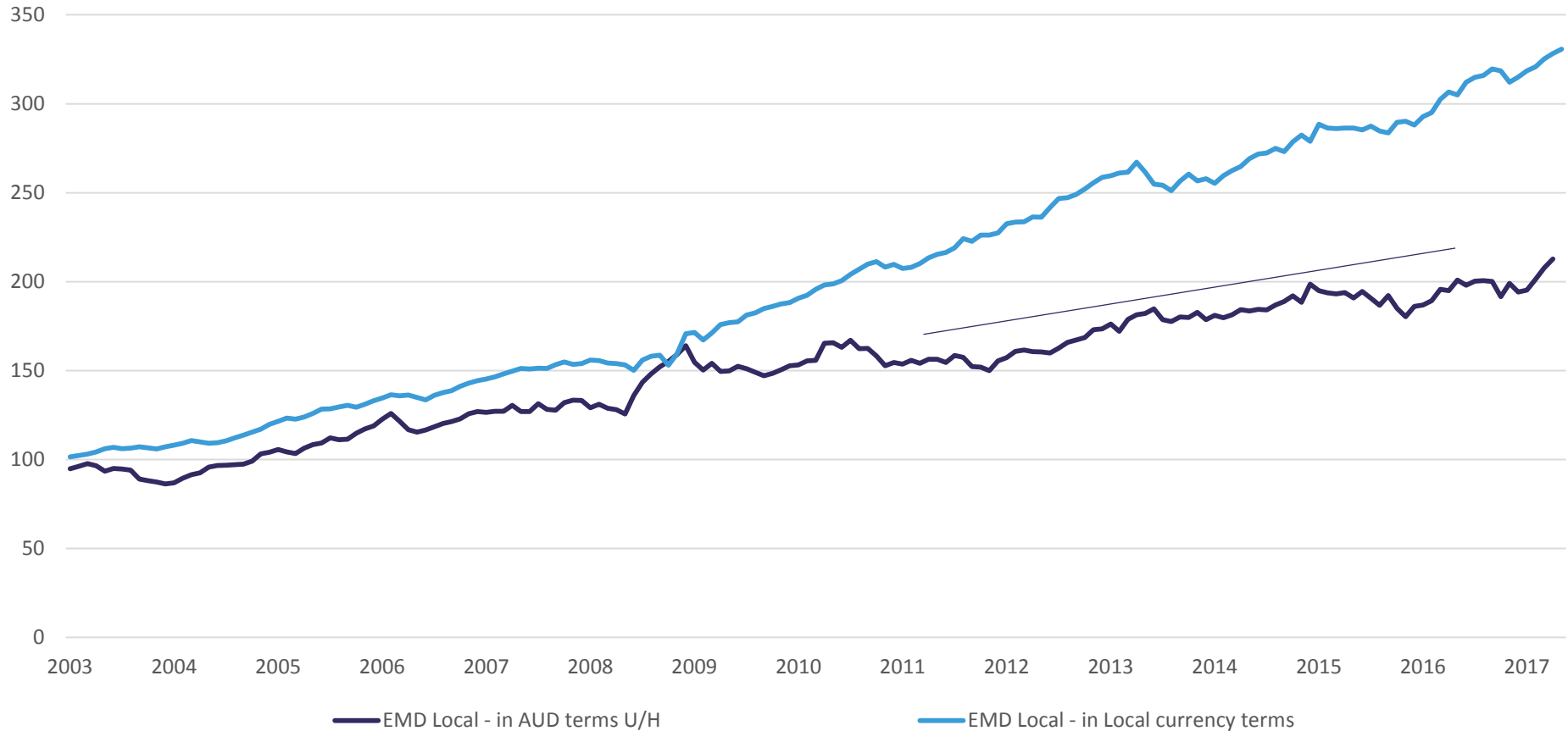
Historical EM yield (local) versus Australian bonds and duration differential



Source: Frontier, Bloomberg

Does the EM currency exposure matter for AUD based investors.....?

Accumulation returns: EM local in own currency versus EM local in AUD terms U/H



Source: Frontier, Bloomberg, JP Morgan

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