Amicus

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LBA Payout Likely to be on High Side

Amicus has a detailed knowledge of many of these claims having submitted most of them on behalf of small claimants who missed the CRP Scheme

If any investor has bought CDO's from Grange or Lehman and not as yet made a claim, we encourage them to contact us to discuss potential recoveries

Amicus believes the final dividend payments are likely to be on the high rather than the low side of estimates given

In early September, PPB, the liquidator for Lehman Brothers Australia (LBA), sent out their long-awaited circular updating creditors on progress made towards the next dividend payment.

The circular outlined current balance sheet outcomes for the estate in different scenarios. Overall this showed that for every $4 million recovered by PPB for the LBA estate this equates to approximately 1c/$ of additional dividend payments for all creditors on their accepted claim amounts.

The largest variable in the balance sheet is described as "Related Party Debtors" where recoveries between $17.5 million and $31 million is expected. A further explanation of this category shows that LBA is owed a minimum $17.5 million from the agreed intercompany claim with Lehman Brothers International Europe (LBIE) but this could rise to $22 million, and LBA hopes to recover $6.6 million and $2.4 million from Lehman Brothers Australia Holdings (LBAH) and Lehman Brothers Australia Finance (LBAF), two subsidiary companies within the group.

These matters are currently before the courts and our understanding is that a judgement on both issues in favour of LBA is likely. Other differences in between the high and low scenarios outlined are due to outcomes from catch up distributions and new claims provisions. These categories are for claims recently made against the estate or ones that are currently being assessed.

Amicus has a detailed knowledge of many of these claims having submitted most of them on behalf of small claimants who missed the CRP scheme. We believe it is highly likely these claims will be successful and also that there may be more claims submitted in the future as we are currently working with a number of additional claimants; however, the amounts are relatively minor and not significant to the overall outcome for creditors. If any investor has bought CDO's from Grange or Lehman and not as yet made a claim we encourage them to contact us to discuss potentially recoveries.

Amicus believes the final dividend payments are likely to be on the high rather than the low side of the estimates given. If any investor wishes to further discuss any of the issues above or has not received a copy of the LBA official circular, please feel free to contact us so we can assist.

China Sovereign Debt Rating Cut

The ratings agency anticipates economic growth in China "to remain strong at 5.8 per cent or more annually through to at least 2020"

S&P recently lowered China's sovereign debt rating by one notch to A+ from AA- (the rating agency's first downgrade since 1999). The downgrade is based on S&P's view that economic and financial risks have increased after China's prolonged period of strong credit growth. The ratings outlook is stable reflective of S&P's view that "China will maintain robust economic performance and improved fiscal performance in the next 3 to 4 years."

The ratings agency anticipates economic growth in China "to remain strong at 5.8 per cent or more annually through to at least 2020," while forecasting credit growth will outpace that of nominal GDP growth for much of this time. S&P believes that although credit growth "contributed to strong real GDP growth and higher asset prices, we believe it has also diminished financial stability to some extent."

It is an indication of increased risks to the health of the Chinese economy, which if it were to slow significantly would adversely affect the Australian economy

S&P's downgrade follows a similar move by Moody's earlier this year. Moody's downgraded China's rating in May citing "the increase in size, complexity and interconnectedness of (debt) exposures have resulted in sharply rising risks." The three rating agencies' sovereign debt rating for China are now all in line.

There is no direct impact of this downgrade on Australian investors (unless they hold debt issued by Chinese state owned or heavily state supported banks). However, it is an indication of increased risks to the health of the Chinese economy which if it were to slow significantly would adversely affect the Australian economy and therefore most companies and banks in Australia.

Consensus for Interest Rate Rises

The economists' forecasts are also consistent with the yield curve which is predicting [two cash rate increases in 2018] and now three more 0.25% increases in 2019

As of mid-September, the four major banks were predicting the following for the future level of the cash rate in Australia. NAB is forecasting two 25bps interest rate rises in late 2018, followed by a further two in 2019. This is a change from August when they were predicting no rate increases in 2018 at all. CBA is similarly predicting interest rate rises in late 2018. ANZ is now predicting two interest rate rises in 2018 and none in 2019. While Westpac is the most dovish predicting no interest rate change in 2018 at all. The economists' forecasts (excluding Westpac) are also consistent with the yield curve, which is predicting an increase in the cash rate to 1.75% by August 2018 and a potential increase to 2.00% by November 2018, and now three more 0.25% increases in 2019.

Amicus agrees with the expressed reasoning behind the ANZ forecast which is that economic and employment growth is positive, but the RBA is uncomfortable with negative real interest rates (i.e. the cash rate below the rate of inflation) and that this will cause the RBA to move interest rates upwards as soon as they can reasonably do so without fear of adversely affecting GDP growth or dampening inflation.

This scenario is likely to prove problematic for investors heavily exposed to fixed rate term deposits

This scenario is likely to prove problematic for investors heavily exposed to fixed rate term deposits and we encourage any investors with concerns to contact us regarding advice re-balancing their portfolio with floating rate notes.

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Who is Amicus?

Amicus is an investment advisory firm, licensed by ASIC to provided financial services to wholesale investors only (Australian Financial Services License No. 384126). We deliver impartial research, advice, valuations, reporting and other services to wholesale clients. We also provide assistance with the formulation of individual client investment policies and strategies, funding requirements, debt advisory assistance with transactions and help with mixed financial and legal issues.

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