An Examination of GNP and GDP relative to Total ASX Market Capitalisation and the significance of CBA, WBC, ANZ, NAB and BHP

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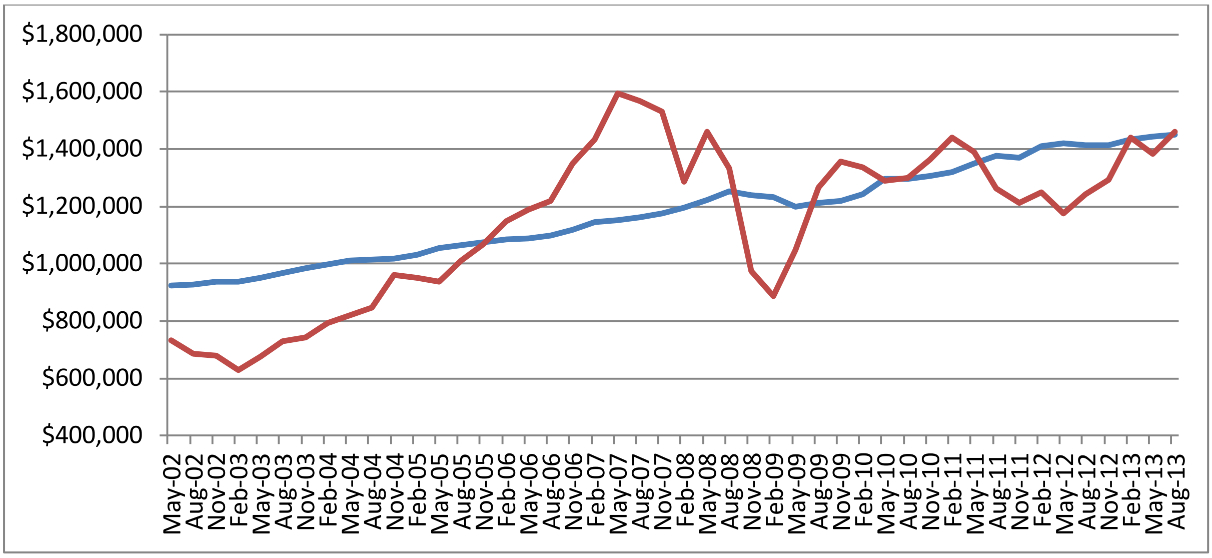
Chart 1: Gross National Product and Total Domestic Market Capitalisation

About this Chart

Data: The Blue line depicts the Quarterly GNP multiplied by 4 to attain an annualized figure. Therefore, the line tracks the growth in Annual GNP more accurately than if yearly data were used. The source of this data is the subscription service *Trading Economics*. Data was provided for the quarters ending in February, May, August and November.

The Red line depicts the total domestic market capitalisation of the ASX in the corresponding months (namely, February, May, August and November.) The data is from the ASX website.

Chart 1 starts from April 2002. GNP Data ends with February 2013, and Market Cap Data ends with May 2013. GNP Data for May and August is an estimate. The vertical axis is in million AUD.



Observations

- Since 2002, the market has traded above GNP for about 4 years (cumulatively). More often, the market has traded below GNP.
- In the last couple of years the market traded below GNP, but has now caught up with GNP.
- The swings in market capitalisation dwarf the growth in GNP.

Chart 2: Gross National Product, Total Domestic Market Capitalisation and Capitalisation of the Big 5

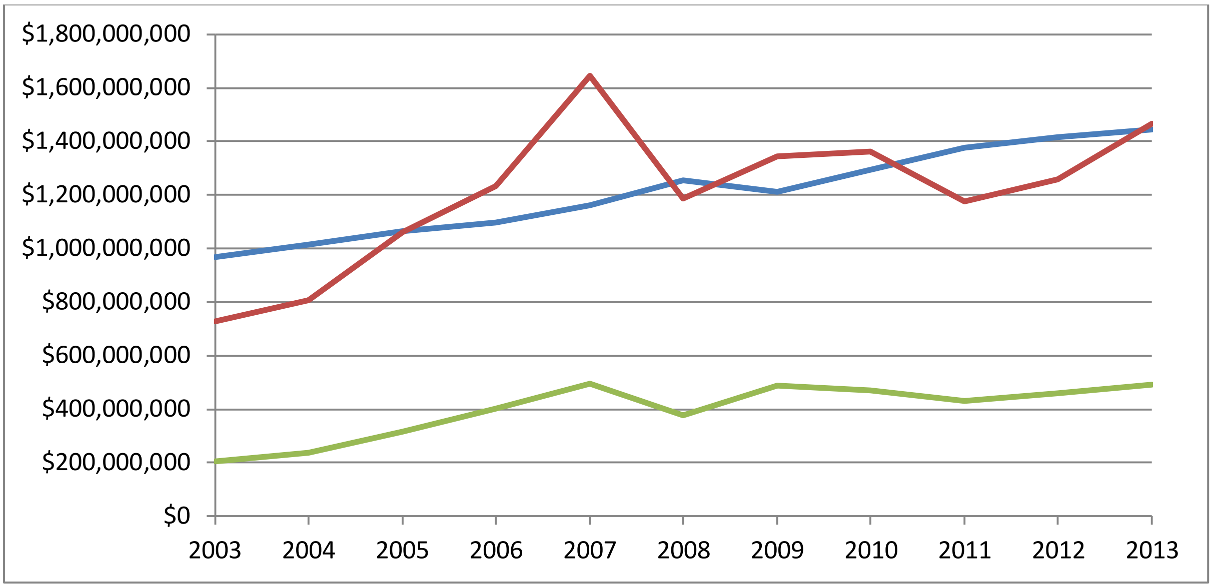
About this Chart

Data: The Blue line depicts the GNP for the quarter ending 15 August multiplied by 4 to obtain an annualized figure. The source of this data is the subscription service *Trading Economics*. The Data spans the years 2003-2013. The final Data Point is an estimate.

The Red line depicts the total domestic market capitalisation of the ASX for September 2003-2013. The data is from the ASX website and the final data point is an estimate.

The Green line depicts the combined total market capitalisation of CBA, WBC, ANZ, NAB and BHP ("the Big 5") on 30 September 2003-2013. The data is from Morningstar and is an approximation only, because the differing reporting dates required adjustments to the market capitalisation of CBA and BHP. These adjustments were only approximate. The last data last data point is an estimate.

The vertical axis is in million AUD.



Observations

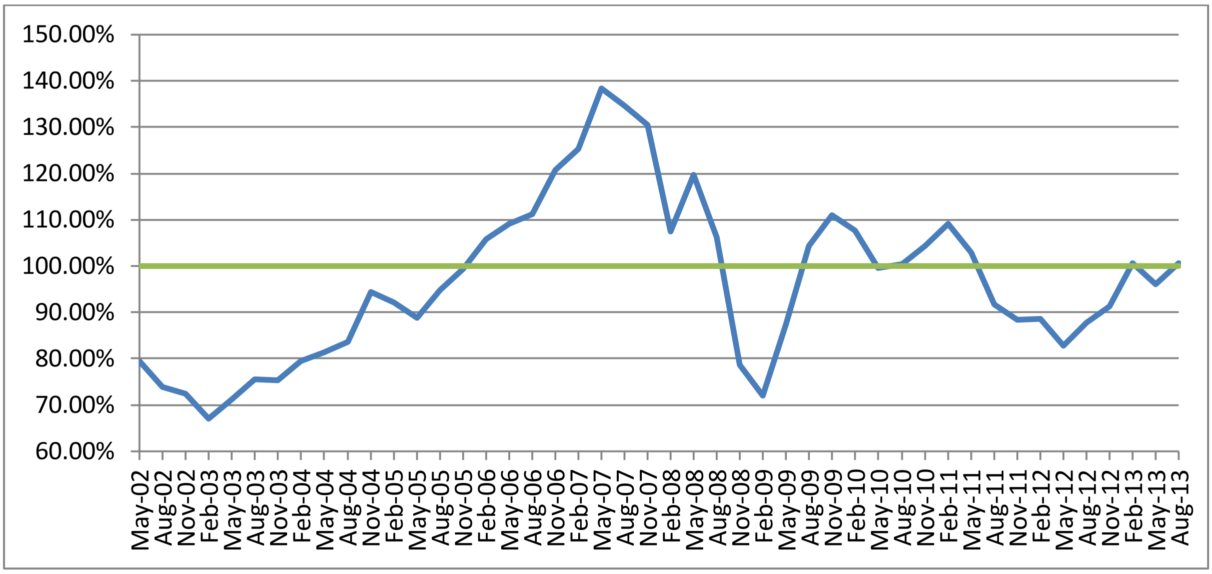
- Total market capitalisation is trending up at a greater rate than the big 5. Even though the Big 5 trend has been affected by the decline of BHP, it appears that the rest of the market apart from the Big 5 is also on a steady trend upwards.

Chart 3: Market Capitalisation as a percentage of GNP

<u>About this Chart</u>

Data: The Blue line depicts the total domestic market capitalisation of the ASX as a percentage of the Annualized GNP for the quarters ending on 15 February, 15 May, 15 August and 15 November. The market capitalisation data is for the end of the corresponding month. The source of this data is the subscription service *Trading Economics* and the ASX website. The GNP Data for May and August 2013 is an estimate; the last two data points on the graph below are approximate only.

The Green line depicts 100%.



<u>Observations</u>

- At the height of the mania in 2007, the value of the total domestic market capitalisation of listed companies (TDMC) was 140% of GNP. In 2009, the market capitalisation reached a low of about 75% of GNP. This suggests the euphoria was a little stronger than the pessimism.
- This small data sample corroborates Buffett's theory arising from his observations of the US market.
- The Average over the period is 96%.
- If we accept the assumption that total market capitalisation will tend to mean revert towards the GNP line over the long term (5 to 10 years), then investors at current prices should expect performance approximating the long term return of GNP.

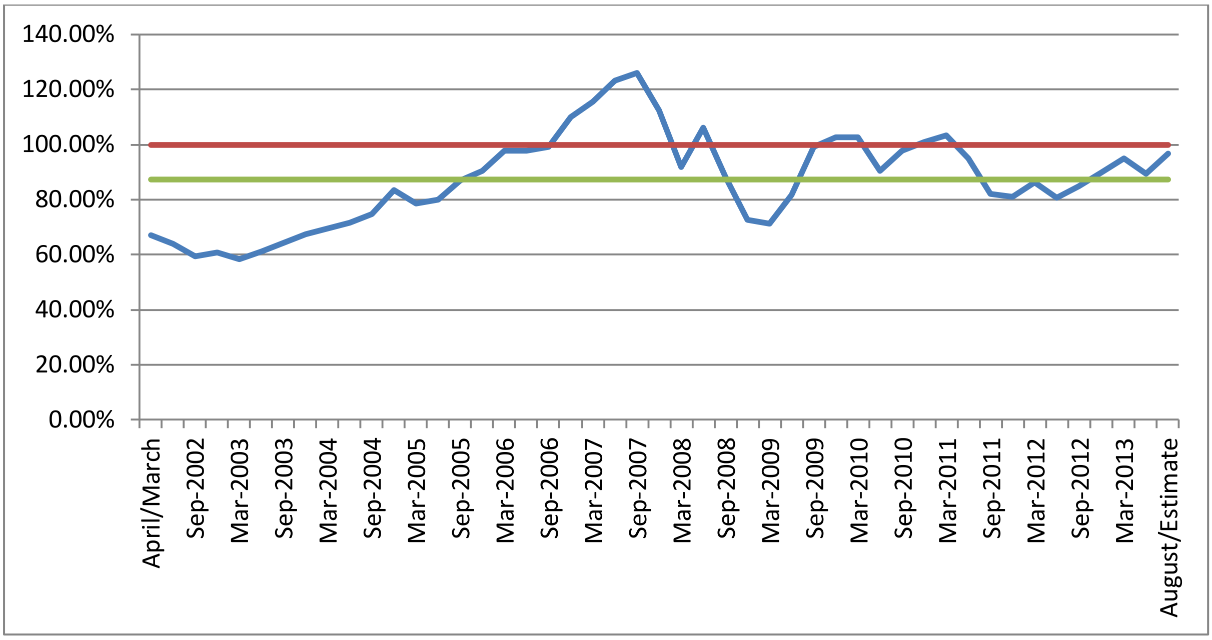
Chart 4: Market Capitalisation as a percentage of GDP

About this Chart

Data: The Blue line depicts the total domestic market capitalisation of the ASX as a percentage of the Annualized GDP for the quarters ending in March, June, September and December. The source of this data is the Reserve Bank website and the ASX website. The first data point is slightly inaccurate (as there was no data for Market Cap prior to April 2002) and the last data point is an estimate.

The Red line is 100%.

The Green line depicts the average ratio over the period, namely 87.4%.



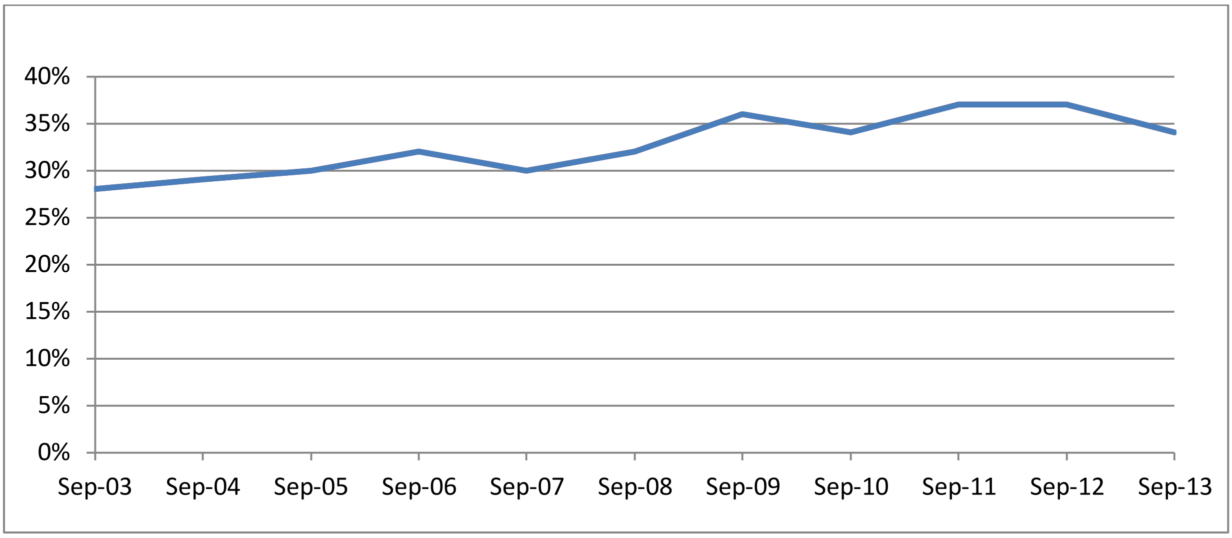
Observations

- Despite encompassing the entire bull market of 2003-2007, the average since early 2002 is well below 100%, at 87.4%
- Whereas the GNP adjusts for money earned by foreign corporations, the GDP does not.
- One would expect GNP be lower than GDP as GNP takes into account the income earned (and taken out of Australia) by direct foreign investment. It is reasonable to assume that GNP is a more realistic measure of the economy and the likely profits of the domestically listed companies.
- It is safe to conclude that when total market capitalisation matches GDP, there is significant optimism. Total market capitalisation already exceeds GDP at the time of writing.

Chart 5: Big 5 as a Percentage of Total Domestic Market Capitalisation.

About this Chart

Data: The Blue line depicts the combined total market capitalisation of CBA, WBC, ANZ, NAB and BHP on 30 September 2003-2013 as a percentage of the total domestic market capitalisation of the ASX. The source of this data is the ASX website and Morningstar. Data is approximate and the final data point is an estimate.



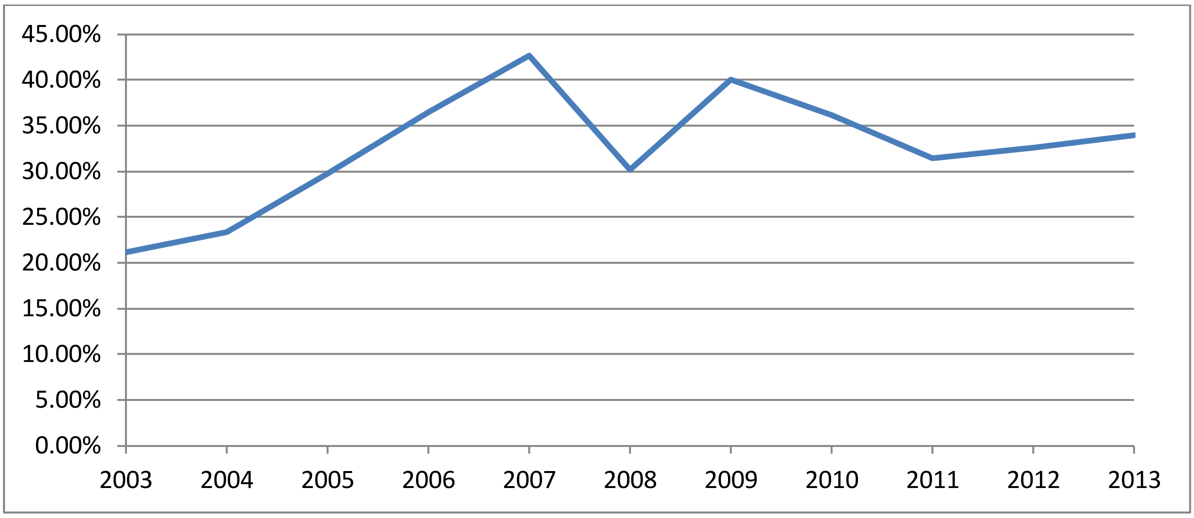
Observations

- The 10 year average is 33%, approximately in line with the current level.
- Given that the combined impact of the Big 5 is not anomalous, this suggests that they are not having much of a distorting impact on Chart 3.

Chart 6: Big 5 as a Percentage of GNP

About this Chart

Data: The Blue line depicts the combined total market capitalisation of CBA, WBC, ANZ, NAB and BHP on 30 September 2003-2013 as a percentage of the GNP of Australia (as of 15 August each year). The source of this data is the subscription service *Trading Economics* and Morningstar. Data is approximate and the final data point is an estimate.



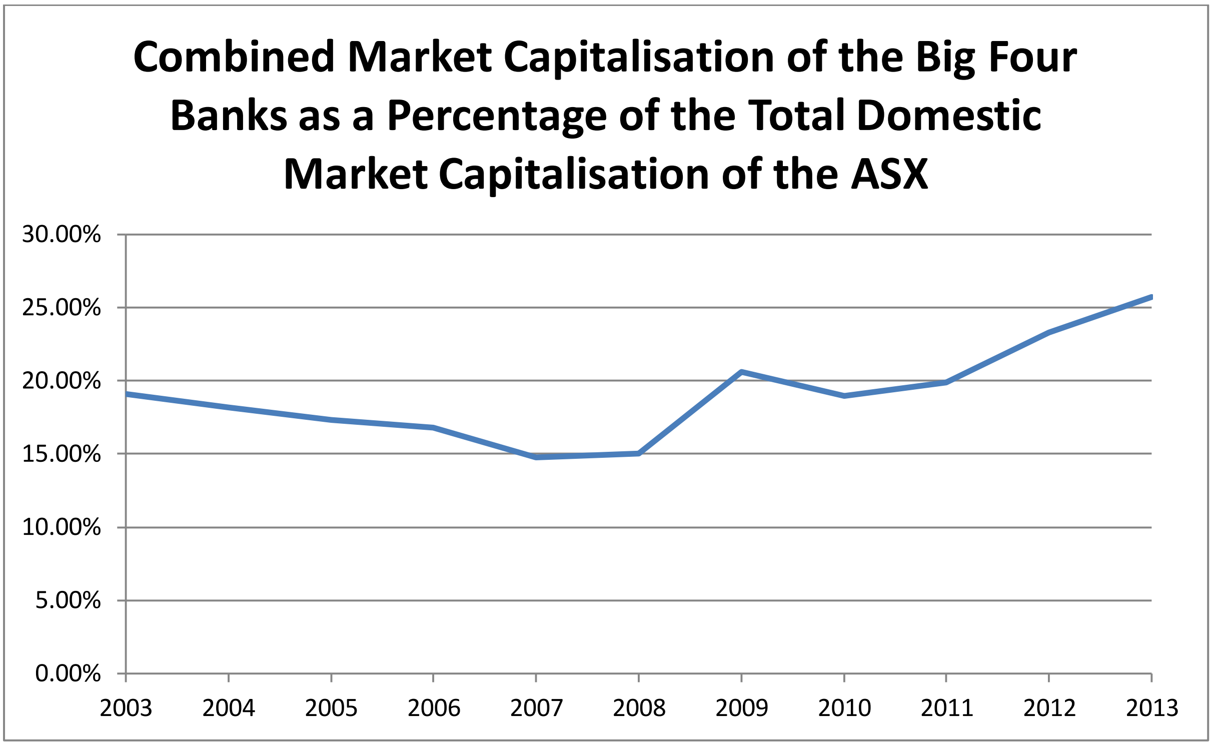
Observations

- The 10 year average is 32.55%, approximately in line with the current level.
- Given that the combined impact of the Big 5 is not anomalous, this suggests that they are not having much of a distorting impact on Chart 3.
- Chart 6 looks similar to Chart 3, as would be expected.

Chart 7: Big 4 Banks as a Percentage of Total Market Capitalisation

About this Chart

Data: The Blue line depicts the combined total market capitalisation of CBA, WBC, ANZ, and NAB on 30 September 2003-2013 as a percentage of the total domestic market capitalisation of the ASX for the corresponding month. The source of this data is the ASX website and Morningstar. Data is approximate and the final data point is an estimate.



Observations

- The 10 year average is 19%, significantly below current levels.
- In the bull market of 2003-2007, the four banks reduced their share of total market capitalisation.
- Since the GFC, the four banks have steadily grown in comparison to the total market. This, in part, reflects the fact that the banks had the opportunity to take over competitors immediately subsequent to the GFC.
- One hypothesis that deserves further research is whether the valuation placed on the banks is an early indicator of general optimism. Given their extremely broad shareholder base, outperforming bank shares mean that a large proportion of unsophisticated investors are feeling like winners.
- If this hypothesis is true, then bank capitalisation may remain steady but reduce as a proportion of total market capitalisation. This would signal that the broader market was ‘catching up’ with bank shares.

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