The Rock
INVESTMENT PLANNING LIMITED

# Investment Market Update No. 18

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## Editorial

What a few weeks this has been for the stock market. We remain in the midst of the company reporting season and there have been both good and not so good results announced.

In this issue we cover:

1. The state of the market;
2. Value of TRIP;
3. Interest rates; and
4. Investment briefs.

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## The market

With expectations of a bumper reporting season those companies that missed either their own or analysts forecasts had their share prices ravaged. On the other hand those that delivered on forecasts were rewarded with strong gains.

The two main share indices, the All Ordinaries and the S&P/ASX 200 have both retreated from recent highs. Part of the reason for this is the payment of dividends. A company going ex-dividend means that current holders of a stock are entitled to receive that dividend.

When a company 'goes ex' the share price will generally fall by the amount of the dividend paid. This is because the company's value has fallen by the amount of the dividend. Paying dividends to shareholders is really only distributing profits to the owners of the company. These profits, once paid, are no longer available to be used by the company.

## Value of our services

In these times of booming share markets it's easy to think, 'why do I need The Rock Investment Planning (TRIP)?'. In addition to preparing the initial financial plan and subsequent alterations, other things we do include: dealing with Centrelink; advancing money to fund pension payments and floats when there are insufficient funds in accounts; reviewing existing portfolios and making recommendations about existing investments (for example to sell Multiplex prior to the announcement of its result); and prepare minutes for self managed superannuation funds. We also undertake constant reviews of client portfolios with a view to adding value. There would be few clients who have not enjoyed the benefits of new floats like ConnectEact or DUET's.

## Interest rates

The Reserve Bank of Australia (RBA) is due to meet on Tuesday 1 March to decide whether to increase interest rates. The announcement will be made public on Wednesday morning. There is intense media speculation that rates will rise by between 0.25 per cent and 0.50 per cent. Recent speeches by the Governor of the RBA seem to support this view.

One of the most effective tools available to the RBA in managing inflation is public perception. By stating rates are likely to rise the RBA is attempting to use psychology to get consumers to decrease their spending and reduce inflation without actually having to increase interest rates.

Economic researchers believe that current inflation is determined by the current level of inflation and future beliefs. That is, if we believe inflation will be higher in the future consumers will adjust their saving and consumption habits to reflect this belief (rational expectations theory).

In the current environment, if there's an expectation that interest rates will rise, the logic follows that consumers will adjust their behaviour now to take account of this. Essentially this means reducing consumption and spending more discretionary income on debt repayment.

Regardless of what happens this week, we recommend preparing for an interest rate rise of between 25 and 50 basis points. Repaying non-tax deductible debt becomes more important as rates rise.

## Investment briefs

Pacific Brands (**PBG**): PBGs half year profit was around $1.5m less than forecast. The company has, however, re-affirmed its full year earnings guidance. On current prices the yield is expected to be around 6.5 per cent fully franked. Part of the result was mis-interpreted by the market which contributed to the large fall in the share price.

Multiplex (**MXG**): MXG announced they do not expect to make a profit from the re-development of Wembley Stadium in England. Higher steel prices was one of the reasons given. Following the announcement MXG shares fell by $1.08 or 19.35 per cent.

Commonwealth Bank (**CBA**): First half net profit after tax up 8.3 per cent to $1.71 billion. CBA increased its interim dividend from 75 cents to 84 cents per share. The Which New Bank program appears to be delivering early, and better than expected, results for the company.

Telstra (**TLS**): Net profit after tax up by around 4 per cent on the back of higher revenues, particularly in broadband and mobile divisions. The result was better than many expected.

BHP-Billiton (**BHP**): Announced a record interim profit of US$2.8 billion. BHP continues to benefit from high commodity prices largely driven by demand in China.

Transurban (**TCL**): Traffic numbers up 4.5 per cent, revenue up 8.7 per cent. The result was affected by the $9m TCL spent (unsuccessfully) bidding for the Mitcham-Frankston freeway (won by ConnectEast). This remains a well run company.

Seven Network (**SEV**): Poor result with net profit after tax down 35 per cent to $43 million. SEV has made a good start to the 2005 ratings period by knocking Channel 9 from the number 1 position on the back of its two most successful new programs, Desperate Housewives and Lost. It will be tough to maintain this momentum until the end of the year, but the signs are encouraging.

Suncorp-Metway (**SUN**): Net profit after tax up 47 per cent on the previous corresponding period to $413 million. Profits from wealth management were up 35 per cent with funds under management growing by 18 per cent. Management have indicated the full year result should deliver a "substantial increase in underlying profits".

Babcock and Brown (**BNB**): Reported net profit after tax of $111.7 million. Deal pipeline remains strong. BNB have recently announced a deal to take over management rights of GPT (from Lend Lease) which looks to be very positive for BNB. The result was pleasing.

Woolworths (**WOW**): Announced net profit after tax for the half increased by 13.7 per cent to $440.9 million. WOW will pay a 24 cent per share fully franked dividend, up 3 cents or 14.2 per cent on last year.

Sydney Futures Exchange (**SFE**): Result was slightly below expectations with net profit after tax of $53.2 million. SFE announced a fully franked dividend of 16.7 cents per share versus 11.6 cents per share for the same period last year, this is an increase of 43.96 per cent.

Australian Stock Exchange (**ASX**): Announced record net profit after tax of $50.5 million up 18.8 per cent. Contributing to this result was an increase in trading volumes of 15.8 per cent and revenues from new listings rising 19.1 per cent. The ASX increased its interim dividend from 29.2 cents per share fully franked to 44.2 cents per share.

| Stock | Share Price Before Report date | Share Price After Report date |
|---|---|---|
| Foster's | 5.42 | 5.32 |
| Australian Infrastructure fund | 2.75 | 2.64 |
| Commonwealth Bank | 34.43 | 37.09 |
| Telstra | 5.24 | 5.27 |
| Australian Stock Exchange | 21.84 | 22.22 |
| Cochlear | 27.70 | 28.53 |
| Amcor | 7.12 | 7.08 |
| Qantas | 3.64 | 3.50 |
| Repco | 3.26 | 3.25 |
| AMP | 7.48 | 7.51 |
| Toll Holdings | 13.19 | 13.12 |
| Woolworths | 15.07 | 15.47 |
| Brambles | 7.65 | 7.56 |
| Transurban | 7.29 | 7.25 |
| Australian Gas Light | 14.14 | 13.94 |
| Paperlinx | 4.57 | 4.45 |
| Alinta | 8.65 | 8.34 |
| Suncorp-Metway | 18.41 | 19.11 |