Investment Market Update No. 13

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Editorial

The start of this reporting season has been very positive. Many companies have reported profits ahead of expectation and this has underpinned a buoyant share market.

In this issue we cover:

1. Oil – black gold;
2. 2004 Federal election; and
3. Investment briefs

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Oil – where will the mayhem end?

As this is written the price of oil has fallen from its recent highs of around US$48/barrel to around US$43/barrel. High oil prices are good for no-one. Increased transportation costs push up the prices of most goods and services which the majority of companies will pass on to consumers (for example the Qantas and Virgin Blue fuel surcharges).

Increased prices leads to a reduction in purchasing power as your wage now buys less goods than it could last week or last year. A potential effect of this, if the RBA isn't watching closely enough, is an economic slowdown as consumers curb their spending, leading to a recession and job losses. Luckily oil does not have the same economic impact on the economy as it did in the 1970's. We have read some reports that suggest oil prices would need to reach $US100/barrel to have the same effect as the oil price shock in the 1970's. This is because industry has become much more efficient and so less oil is used per unit of output.

Continued supply interruptions in Iraq are likely to place further short-term pressure on oil prices. The price of oil is set by the Organisation of Petroleum Exporting Countries, although recently Russia and Venezuela have increased production beyond the targets set by OPEC. This sort of competitive behaviour is good while it lasts, but at this stage has had no lasting impact on oil prices. The ACCC would have a field day with OPEC if it were an Australian organisation given the market manipulation and price setting activities it partakes in.

It's on – election 2004

John Howard has just announced we will be going to the polls on October 9. Between now and then we can expect to be bamboozled with shots of politicians kissing babies, hearing grandiose promises about economic management credentials, interest groups threatening to divert preferences to other parties, and a whole lot of media coverage.

The media often fails to separate fact from fiction when it comes to elections. For instance, when the greens invariably direct preferences to the ALP, the media make it sound like the actual distribution is an automatic process. For the House of Representatives it isn't. What the interest groups are saying is that on their How to Vote Cards they will place one party ahead of the other. It remains up to the individual voter to determine how in fact the distribution of preferences is made.

In the Senate it's both similar and dissimilar. If you are like the majority of Australian voters and tick one box above the line then it is true that the party you assign your vote to determines the distribution of your vote. However, if you like to make up your own mind you can number all of the boxes below the line and determine the allocation of your vote.

This is a fascinating time for students of politics and can be made fun for those with a moderate interest by trying to determine the political preferences of various media commentators (some are much easier to pick than others). Reading analysis of policies at election time needs to be taken with a grain of salt. Invariably what passes as fact is often nothing more than the reporters understanding of what is said (be it right or wrong), laced with a degree of bias.

If you are genuinely interested in understanding the policies in order to make an informed decision, doing some internet research and finding the relevant source documents is the way to go. Press releases will gloss over the detail in order to make glamorous statements that will feature on the news. The website addresses for the three major parties are:

http://www.liberal.org.au; http://www.alp.org.au; http://www.nationalparty.org.au

While a long election is likely to cause market uncertainty, our view is that it doesn't matter much who gets in, the market will respond to broader economic issues.

Investment briefs

Sons of Gwalia (**SGW**): In the age of the resource sector boom SGW has been placed into voluntary administration. Trading in the company has been suspended pending the outcome of a creditors meeting.

Pacific Brands Group (**PBG**): Net profit after tax has exceeded prospectus forecasts by $7.1 million. PBG got a free kick from a high Australian dollar as the majority of the group's goods are imported.

ABC Learning Centres (**ABC**): Reported full-year profit of $21.4 million which is up 77 per cent on the previous period. The company continues to expand and while the generous government subsidies continue ABC will benefit. Will a change of government review the existing arrangements?

Suncorp Metway (**SUN**): Net profit after tax for the year of $618 million (this compares favourably to last years $384 million profit) with a final fully franked dividend of 40 cents per share. This is a pleasing result as SUN continues to expand outside its traditionally strong QLD base.

Diversified Utility and Energy Trusts (**DUETS**): Listed at $2.29 and is now trading at $2.39. The trust, along with Alinta, successfully tendered for the operations of the Dampier to Bunbury Natural Gas Pipeline - Australia's biggest gas transmission system - in a deal that pays out the $1.85 billion bank debt owed by Epic Energy.

Australian Infrastructure Fund (**AIX**): The share price has rallied recently to $1.99 on the back of better than expected annual profit (up $7 million to $37.3 million). AIX's assets are first class and future prospects for the company are promising.

Caltex (**CTX**): CTX has had a horrid time over the past couple of years which has been caused by large debt levels. CTX has reported that net debt is down from $854 million from this time last year to $535 million this year. CTX also reported first half net profit after tax of $180 million. A pleasing result for shareholders.

Wide Bay Australia (**WBB**): WBB reported a 7.6 per cent increase in net profit after tax of $9.89 million. Total dividend for the year is 34 cents.

National Australia Bank (**NAB**): Following recent boardroom departures and a review of the company's operations by CEO John Stewart, NAB has made some changes to the ranks of its Senior Executives (the most noteworthy being the recruitment of Ahmed Fahmour (ex-Citigroup) and Michael Ulmer (ex-CBA)). Interestingly both were appointed to the board. Although there has been some negative media attention of the appointments (focusing on the remuneration packages offered, especially to Fahmour), the old adage of paying for quality seems accurate in this case. Time will tell whether the investment has paid off.

Aristocrat Leisure (**ALL**): After reporting a loss of $33.7 million for the first half of 2003, ALL has reported a net profit after tax of $63.3 million for the first half 2004. This is another company that has had its fair share of boardroom battles (being fought in the open).

Fosters Group (**FGL**): The wine business (which is currently being reviewed) continues to detract from FGL's performance. FGL reported net profit after tax decreased by 17.4 per cent to $469.4 million (excluding abnormals and the sale of ALH).

Mulitplex Group (**MXGCA**): MXGCA reported a maiden net profit after tax of $87.2 million. A good result for the recently listed group (December 2003).

Woolworths (**WOW**): Net profit after tax of $687.8 million and a final dividend of 24 cents per share. While recent market focus has been on the turnaround of Coles Myer, WOW continued to do what it does best. The lesson here is to never write-off a quality company with a quality management team.

UniTab (**UTB**): Another good result for the QLD based TAB. Net profit after tax of $53.8 million, with wagering growth up 7.1 per cent due to good weather in QLD and the further rollout of Pub TAB's in QLD (*source: UBS).*

Big Kev (**BKV**):After listing at 54 cents in 2001 the QLD based cleaning products retailer has failed to deliver. Revenue is down 74.9 per cent and the company reported a loss of $1.24 million (up from the $957,049 loss reported the previous year). Without a major restructuring the prospects for this company do not look good.

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