Investment Market Update No. 9

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Editorial

We are a quarter of the way through the year and once again time seems to have flown. Investment markets have moved forward from being overly pessimistic to begin a sound growth course, even shrugging off terrorist activity in the Middle East and Europe. Fickle things markets.

In this issue we cover:

1. Interest rates and inflation;
2. Problems at the Bundesbank; and
3. Investment briefs.

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Interest Rates

Financial markets are a crazy place sometimes and this is evidenced by the reaction in the US to every word uttered by Dr Alan Greenspan, Chairman of the US Federal Reserve. Market analysts from around the world are waiting to hear what Dr Greenspan thinks about the US economy and what this means for interest rates.

Given US interest rates are at something like 40 year lows, a first year economics student could say with some conviction that rates will increase before to long. It should not be a shock to anyone when rates rise and any panic selling in the bond and share markets will be an over-reaction to a fairly predictable event.

If there is another rate rise in Australia before rates rise in the US the Australian dollar will appreciate further and continue to harm exporters by making our goods more expensive overseas. As shown in the latest CPI figures importers (clothes and fuel etc) will benefit.

Following the release of the latest inflation data, as measured by the CPI, the largely uninformed media will be pointing out there is not reason for the RBA to raise interest rates again for a while. The justification will be that inflation is at a four year low and at the bottom end of the RBA's inflation target of 2 – 3 per cent.

The problem in focussing on the CPI is that it is only one measure of inflation and some items that have large effects on the economy are not included in this calculation *(source: Dr Ron Woods, Challenger Financial Services, Challengernomics, 28 April, 2004).* The TBA uses more than just the CPI figures to determine how the economy is going and whether rates should rise, fall or stay the same.

A lower than expected rate of price inflation does not necessarily mean the RBA won't increase interest rates next month. It is difficult to tell when the next move will be. It is less difficult to predict it will be up.

The Bundesbank

Commission based financial planners in Australia often receive soft-dollar commissions offered by fund managers. These include such things as free trips to overseas conferences, hotel stays, and tickets to major sporting events. They claim they are not influenced by these in making product recommendations. (Note: The Rock Investment Planning neither seeks nor accepts these forms of commissions.)

The (recently resigned) President of German's Central Bank (the Bundesbank), Ernst Welteke has made a similar statement after it was revealed Dresdner Bank paid for him to stay in a hotel in 2001. The $12,500 it cost Dresdner has since been paid back, but the damage to Mr Welteke's credibility, and that of the Bundesbank, has been done.

Germany's finance minister, Hans Eichel, put it best "I consider it is not acceptable that the chief representative of the Bank, which also has supervisory functions, should accept a holiday for himself and his family paid for by a bank which is under [his] supervision"*(Source:http://www.economist.com/agenda/displayStory.cfm?story_id=2608090).*

Although there is not proof that Mr Welteke or the Bundesbank afforded Dresdner any special treatment as a result of the freebie, the mere perception that they might was a concern.

It is the perception that was Mr Welteke's undoing and it is the same type of feeling that exists when financial planners accept commissions. In his resignation letter Mr Welteke wrote "…the Bundesbank needs a president…free of outside influence and…[to operate]

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without constraints"*(source:http://www.bundesbank.de/press/download/pn/2004/04/20040416bbk5_en.pdf).*

Financial planners should also operate free of outside influence when recommending products and structures for their clients. Receiving commissions has the potential to cloud judgement. Unfortunately for some investors, the new rules put in place under the Financial Services Reform Act do not go far enough as soft-dollar commissions are still able to be accepted by advisers.

Investment briefs

National Australia Bank (**NAB**): NAB have recently announced forecast earnings to be 8-12 per cent lower than last year. Any reduction in the dividend is expected to result in short term price pressure. The boardroom saga is finally coming to a head with the EGM scheduled for May 21 to decide on the fate of the board.

Telstra (**TLS**): For the quarter ending Mar 31 total revenue was up 2.1 per cent. A boom in mobile sales, stemming from improved technology like camera phones, was responsible for slightly under half the revenue growth.

Amcor (**AMC**): AMC announced net profit after tax up 6 per cent on the previous period, but this was below forecast. However, AMC have advised the market that earnings are likely to be flat for the full year. Adverse currency movements (that is the appreciation of the Australian dollar) was negative factor. Also dragging the company down is the performance of its European division. We do not expect AMC's Europe operations to be as large a financial drain as Chep Europe was on Brambles. AMC have spent in excess of $4 billion on acquisitions since February 2000, and now intends to spend $150 million to restructure their poor performing businesses.

Woolworths (**WOW**): Coles Myer (CML) has begun to make in-roads into WOW's petrol business, and WOW is indication this was the main reason for its disappointing sales data for the quarter. Launching a deal with Caltex, in addition to the WOW petrol stations, is one attempt to reduce CML's impact. WOW remain an extremely well run company.

Westfield (**WSF**, **WFT**, **WFA**): Westfield has announced their intention to merge its three entities into one, the Westfield Group. This will, in effect, create a $22 billion listed property trust and will be the 8th largest company in Australia by market capitalisation. Court approval needs to be sought prior to the merger occurring, which, if successful, is likely to occur in June 2004.

Pacific Brands Group (**PBG**): Listed at $2.50. Has traded between $2.47 and $2.62. Currently trading at $2.49.

New Corporation (**NCP**): In an attempt to access the more liquid and larger US capital markets (amongst other reasons), NCP have announced their intention to list on the NYSE. The impact on their share price is expected to be positive in the short term, but o real long term price appreciation from this move is expected.

ANZ Bank (**ANZ**): ANZ have announced profit after tax is up by 22 per cent compared to the same period last year. The dividend of 47 cents per share is up by 11 per cent when compared to the same period last year. Overall a good result.

Cochlear (**COH**): For the second time in six months COH have cut their profit forecast. COH now expects profit to be in the range of $35 - $39 million for the financial year, which is down from the $58 million forecast in December. Shares in COH fell by 97 cents, or approximately 5 per cent, following the announcement.

The three TAB's (**UTB**, **TAH**, **TAB**): It looks like offer, counter-offer, and counter-counter-offer have finally come to an end with the decision by UTB to withdraw from the race to purchase TAB. Providing TAH acquires 50 per cent of TAB, UTB will buy the TAB Gaming Business and its QLD assets. This is a good result of UTB.

The views expressed herein may not reflect the views of The Rock. You are advised to seek advice regarding your particular situation before acting on anything contained herein.

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