

# MARCUS TODAY

## MONTHLY REPORT

THE STOCKMARKET NEWSLETTER FOR EVERY INVESTOR

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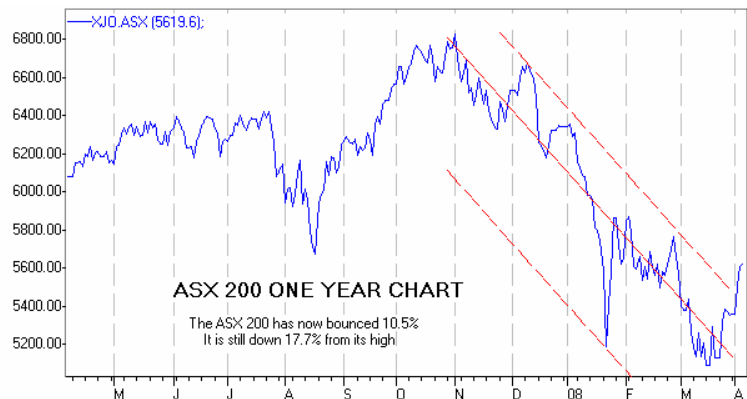
### The Stockmarket in March 2008

March was the fifth month of the bear market and we saw some of the best and worst sentiment so far. We plumbed the depths of Black Tuesday when many market commentators had incorrectly called the bottom (on January 22<sup>nd</sup>) and went lower again. The correction extended from 23.4% on Black Tuesday to 25.5% by March 10th.

#### There were a few themes for the month:

- Sentiment towards financials bottomed and then sharply recovered on the back of co-ordinated international central bank intervention.
- There was a big switch out of resources and into financials.
- A lot of debate about whether the US economy had "decoupled" from the Chinese economy – in other words whether the Chinese economy would be immune from a US recession or not.
- A small margin lender called OPES Prime went into administration after large losses from a small number of clients. In recovering their debts the secured creditors – ANZ, Merrill Lynch and Dresdner Bank – claimed that the assets of OPES's 1200 clients belonged to them and sold them into the market, causing outrage and chaos from the clients and from many of the small companies in which OPES clients held substantial stakes, stakes that were sold into the market causing significant share price damage. See below for more.

PERFORMANCE IN MARCH			Financial	Calendar
INDICES	MAR	NOW	YTD	YTD
ALL ORDS index	-4.67%	5410	-14.3%	-15.7%
ASX 200	-3.88%	5356	-14.8%	-15.5%
ALL ORDS inc Dividends	-4.11%	34555	-11.6%	-14.7%
Dow Jones	-0.03%	12263	-8.5%	-7.6%
S&P 500	-0.60%	1323	-12.0%	-9.9%
NASDAQ	+0.34%	2279	-12.5%	-14.1%
SECTORS				
Industrials	-1.98%	7417	-21.3%	-18.8%
Resources	-8.55%	5645	+5.8%	-7.3%
Property Trusts	-0.27%	1703	-27.9%	-19.3%
Banks index	+2.62%	5950	-21.4%	-21.1%
COMMODITIES				
Aussie Dollar	-1.85%	0.91335	+7.5%	+4.4%
Gold	-6.01%	916.2	+40.8%	+9.3%
Oil	-0.24%	101.54	+44.1%	+5.8%
Copper	-0.0%	8540	+11.6%	+27.9%
Nickel	-1.1%	31150	-13.1%	+20.7%
Zinc	-14.5%	2325.5	-29.6%	+1.6%
Aluminium	-4.7%	2941.5	+9.5%	+25.1%



On March 10<sup>th</sup> the US Fed announced a significant increase in liquidity measures and a collaboration with a number of international banks designed to head off the credit crunch. The market bottomed. The Dow rallied 416 points, the biggest rally in 5 years and things began to tentatively improve.

In the last two weeks the Dow Jones managed another rally of 420 point in a day, a two day rally of 448 points and another day up 391. Volatility of this magnitude is seen as a sign of a change in sentiment (or are we just clutching at straws) and the "technical" picture, and we don't have a better guide at the moment, suggests we have broken the down trend.

## Some of the features of March include:

- **A 3.88% fall in the ASX 200.** A big underperformance of the Dow Jones which fell just 0.03% on the month.
- **A collapse in the resources sector** (down 8.55%) on two factors – concerns that the US economy *would* impact the Chinese economy and a switch out of resources to fund the switch into financials. In a recovery the financials, which have factored in a lot more fear than the resources are expected to snap back a lot more than the resources. Resources have performed relatively well in the downturn.
- **Banks were actually up on the month** (+2.6%) reflecting a bottoming of the “financial fear” factor in the US, the rescue of Bear Stearns by the US Fed (it almost went bust), an oversubscribed \$4bn capital raising by Lehman Bros and a \$15bn placement by UBS.
- **Industrials outperformed** (down 1.98%).
- **Gold peaked** at \$1033 and rapidly fell below \$900. Down 6% on the month taking the gold stocks with it. The sector has been seen as a safe haven in the face of a falling US dollar and uncertain financial markets.
- **Metals mostly flat except for Zinc down 14.5%**, a fall that conspired to drop most of the zinc stocks despite a bid for Zinifex from Oxiana during the month.
- **A\$ down a touch** on the month as the US dollar rallied on hopes the credit crunch might have bottomed.

## Economics – Australia

The RBA has upped interest rates by 25bps to 7.25%. Cash rate at highest point since December 1994. It is the 12<sup>th</sup> time since mid-2002 that the RBA have increased rates by 25bps. They said in their statement that “the overall tightening in financial conditions since the middle of 2007 is substantial” – suggesting to many that after recent policy tightening the RBA was moving to a more NEUTRAL or “wait and see” approach to interest rates. That proved to be true with no interest rate rise at their next April meeting.

- **An Australian Industry Group study** said the Australian economy will struggle to grow at an average 3% a year for the next 10 years.
- Australian **economic growth came in below expectations** in the 4Q, +0.6% from the previous Q and up 3.9% on the year. Economist’s expected +0.8% for the Q.
- **Australian consumer sentiment fell 9.1%** in March from February – blamed on the impact of higher interest rates, higher fuel prices and the expectations of higher mortgage costs.
- Both the **Reserve Bank of Australia** and **Japans central bank** injected cash into their banking systems to combat the credit crunch.
- **RBA Governor, Glenn Stevens made a few comments** during the month:
  - The Australian economy is weathering the international credit storm well. Profitability remains very strong and capital sound.
  - The cost to banks of raising funds in the market have moved independently of the official rate and said it was an unrealistic presumption to expect lending rates to remain in lock-step with the cash rate- meaning the banks may keep passing on the extra costs of funding.
  - He said the economic environment will remain quite challenging for a while, “but the strength of the Australian financial system is, for Australia, a good basis for meeting the challenge.”

## Economics – US

- **The Dow Jones has its biggest one day rally in 5 years** – up 416 - as the Bank of Canada, the Bank of England, the European Central Bank, the Federal Reserve, and the Swiss National Bank pumped \$200bn into the banking system.
- The Federal Reserve announced an expansion of its securities lending program. In addition they authorized and extended increases in existing temporary reciprocal currency arrangements (swap

lines). They also boosted the size of the Term Auction Facility to \$100 billion and announced a series of term repurchase transactions that inject another \$100 billion.

- A week later the **Federal Reserve cut rates by 75bps** and the Dow responded with another 420 point rise – the biggest one day rally in 5 years again and 3rd biggest rally rise ever. The US now has the lowest rates since 2004 and has had six rates cuts since last September. Interestingly the rate cut was not unanimous amongst Fed members. The 75bp rate cut was only passed by 8-2. 2 Governors thought a less aggressive 50bp was all that was needed.
- The Fed statement included the phrase that **the Fed will “act in a timely manner”**.....taken as meaning that more rate cuts are likely.
- **Retail sales fell an unexpected 0.6%** against forecasts for a 0.2% *gain*. The immediate conclusion was that the **US was already in recession**. The consumer has been the powerhouse of the US economy accounting for 2/3 of GDP.
- **Government plans** were released aimed at slowing the rate of foreclosures which were up 60% in February. Florida foreclosures are up 158% in the last year and house prices in Miami are down 17.5%...the most of any US City **Total foreclosure rates was up 77% in 2007**.
- **US Pending Home Sales** were flat in January, better than expectations for a 1.0% fall.
- **US Mortgage Delinquencies** hit new highs this cycle. The level of delinquencies is now running at a higher level than the 2001 peak. In Q4 just over 20% of sub prime adjustable rate mortgages were past due whilst 2.56% of prime fixed rate mortgages were past due, up from 2.54% in Q3.
- **US Trade deficit** better than expected.
- **Existing Home sales has their first rise in seven months**.
- **Inflation numbers (CPI) were better than expected**.
- **Consumer Sentiment fell** to a 16 year low.
- **The European Central Bank has left rates unchanged** at 4.0% as inflation hits a 15 year high.
- **Feb PPI (Producer Prices)** were in line with expectations.
- **Feb Housing Starts** hit their lowest in 16 years.
- **Consumer confidence fell** to a five year low. 6 month expectations fell to the lowest since 1973.

## OPES PRIME

Although this issue only really broke out on the last day or two of the month the **receivership of margin lender OPES prime** dominated the Australian equity market for a while. OPES Prime is (was) a margin lender with a difference, the contracts between OPES and its clients were not plain vanilla. In a normal margin lending contract beneficial ownership of all assets remains with the client. With OPES, and without anyone really understanding, clients signed over beneficial ownership of all cash, shares and assets lodged as security for loans to OPES Prime itself. When it went bust the clients lost those assets.

OPES was well known for lending against stocks a normal margin lender would not and the impression was that where a normal margin lender would only lend against top 200 stocks OPES would lend against top 300. As it turns out OPES was lending against 700 listed entities. Of those only 16 had a market capitalisation of over \$1bn (approximate cut off for the ASX 200) and about 650 had a market capitalisation below \$200m (approximate cut off for the ASX 300).



Come a market downturn this was a lending book accident waiting to happen. 6 clients in particular got into trouble. One in particular to the tune of \$147m. Rather than close them out and give them a margin call one of the directors set about systematically falsifying cash and stock movements on these accounts to prevent margin calls, presumably to buy some time in the hope some of the positions would improve. The other directors found out, called in the ANZ and ANZ, with \$650m worth of loans outstanding to OPES, called in the administrators. The administrators froze all client accounts at OPES (clients couldn't sell positions).

The market then discovered that under the OPES margin lending agreements (which are called securities lending agreements) clients simply didn't own the stock they thought they did (they never did) - ANZ's administrator owned them. To satisfy their loan ANZ (\$650m) and Merrill Lynch (\$350m) then set about selling over \$1bn of OPES clients assets into the market. Net effect:

- Clients of OPES Prime lost everything they had lodged as security – all shares and cash were claimed by ANZ and Merrill Lynch and sold.
- As the ANZ and Merrill Lynch selling hit the market, most of it in illiquid stocks, share prices tumbled.
- Companies realised that substantial percentages of their companies were in the hands of an administrator and being sold, many stakes over 10%, some close to 50%. A lot of them in the small resources sector. A flurry of trading halts ensued as companies tried to get a handle on how much stock was about to hit the market.
- Clients, some of which had lost enormous wealth (at least one with \$50m) went to Court and unsuccessfully tried to challenge the ANZ claim of beneficial ownership. The Malaysian royal family turned out to have 14.5% of Gindalbie Metals with OPES. They lost that. Some resources company directors lost their own substantial stakes in their own companies. One company lost its shareholding in a company it was bidding for.

All in all it was a shambles, a very poor reflection on the Australian equity market, a serious hit for private investor confidence in the market, and a very poor reflection of the big financial institutions ANZ and Merrill Lynch who understandably but savagely protected themselves at the expense of 1200 innocent individuals. And it is not over yet. It has been an episode of random injustice and devastating bad luck for OPES clients.

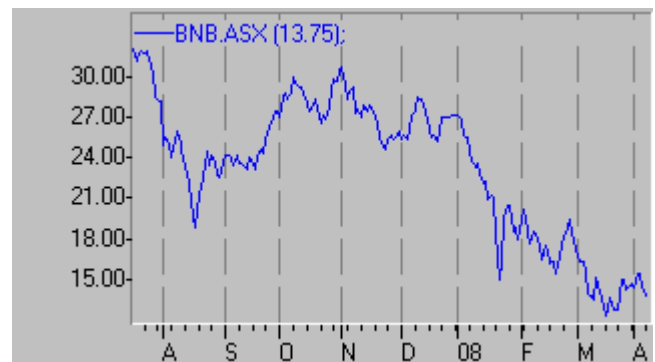
There has been the obvious call for tighter regulation of the margin and securities lending business and doubtless the legal issues will continue to be fought and in particular the issue of "small print".

#### The lessons to be learnt so far include:

- Read the small print.
- Issues that affect financial institutions, no matter how remote (sub-prime), can affect us all.
- To assess you own risk you need to imagine the unimaginable. Ask yourself. Whose insolvency are you exposed to. Nothing is impossible – Bear Stearns – the third largest broker in the US went bust this month and had to be rescued by the Federal Reserve. For a while there the market thought that Lehman Bros and even UBS itself was going out of business. No one is 100% safe. Spread your exposures. Don't put all your financial eggs in one basket.

## Company news: Industrials

- In a sign that conditions in the credit market might be improving and that institutions and banks are beginning to see through to the other side of the credit crunch **Babcock & Brown announced a range of new funding initiatives.** This followed a 65% fall in the share price as the market struggled with and feared the complexity of their exposures to the credit markets. 25 banks (up from 20) formally committed to participate in the expansion of BNB's corporate debt facility which was expanded to \$2.8bn (from \$2.35bn) and extended until 2011. They also "materially lowered the market capitalization review threshold", arranged \$400m in new infrastructure asset specific debt facilities and completed an institutional equity placement raising \$220m. In addition they announced \$4.7bn in committed un-invested



equity in their unlisted managed infrastructure vehicles, vehicles that continue to attract institutional cash flows. BNB down 21% for the month.

- **James Packer's Crown Macau** casino has been recovering market share in Hong Kong thanks to a strategic deal late last year with a HK listed operator, A-Max and the decision to focus on the VIP gambling market. Melco PBL's market share is up from 5.7% in November to 18.1% in February. NASDAQ listed Melco PBL is still 57% below its listing price of \$21 back in January 2007. CWN fell 12% in March.
- **Leighton Holdings** (LEI) announced the purchase of \$260m of ConnectEast stapled shares at 115c. A sign of confidence in the Eastlink project – CEU announced last December that a \$260m bridging facility would be replaced on completion of the Eastlink project by \$260m of equity investment from LEI. **ConnectEast** (CEU) published an institutional investor presentation. They talk about a strong financial position, an early completion bonus, on budget. All good for a company in a sector struggling with the fear of financing issues. CEU down 7.6% for March. **LEI** was also awarded a US\$720m contract to construct offshore pipelines in India for Oil and Natural Gas Corporation. Work will begin in November this year and will take place during November and May each for the next 3 years. LEI down 16% in March.
- **Qantas** (QAN) said it has kept, and will continue to keep, the market informed about fuel costs and that it doesn't need to alter its profit forecasts. *The Age* ran a story saying a private email to senior management from CEO Geoff Dixon warned the airline's fuel bill could increase to over \$1bn. QAN down 10.5% last month.
- **WA News** (WAN) Chairman Peter Mansell has labelled Kerry Stoke's attempt to take control of the board as "opportunistic". He will release the company's March-Q results on April 10, two weeks earlier than initially planned, to prove that the disappointing half year result was affected by one-offs. He believes this whole process could cost WAN \$500m. WAN lost 3.57% in March.
- **Wesfarmers** (WES) announced it will not be selling Kmart after conducting a strategic review. MD Richard Goyder said the board was encouraged by the division's performance and its ability to grow earnings. Kmart's MD Larry Davis has decided to retire, Mark Goddard, currently Kmart's general manager, merchandise will become acting managing director while a replacement is found. WES up 1.19% on the month.
- **Myer Group** announced a 37% increase in 1H net profit of \$78m despite revenue falling 1.9% to \$1.63bn from \$1.66bn.
- **ABN AMRO** is cautious on the banking sector saying significantly higher funding costs could lead to constrained lending and believe each bank may have a funding requirement of \$40bn in FY09 just to refinance the current balance sheet. It has cut its FY09-FY10 earnings forecasts for the big four by around 4%. They say, "Australian banks have underperformed the broader market as investors are now in the 'race to become the most bearish". But they do say that history will show the current correction as a great buying opportunity if prices continue to fall.
- **Goldman Sachs JB Were upped their Bank sector recommendation** from UNDERWEIGHT to OVERWEIGHT saying current prices imply earnings growth of 1.1% to 3.8% for the next 10 years compared to the long term average of 5-6%. "The bad news appears to be priced in, suggesting banks are undervalued". They upgraded the NAB to a BUY with a 3585c target price. They have also **added Macquarie Bank** to their CONVICTION LIST.
- **St George Bank put out a market update.** Reaffirming 10% EPS Growth Forecast For FY08. Remains Appropriately Provisioned – "All exposures are within prudential and internal policy



guidelines". Funding Requirements On Track. FY08 Underlying Margin Contraction Around 10 Pts. Overall Credit Quality Strong. Wealth Funds Under Management Affected By Markets. Strong volume growth In Mortgage and Business Lending.

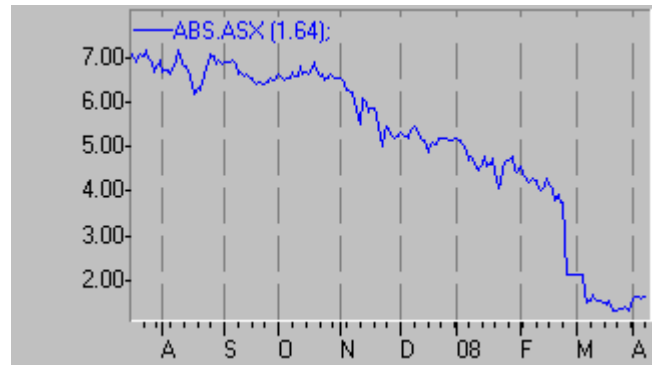
- **Macquarie Group (MQG)** has acquired a majority stake in Allegiance Investment Management whose headquarters are in Orange County, California and manages around \$US4.5bn in fixed-income products. No price was mentioned. Citigroup upped their recommendation to BUY from SELL. MQG down 7.7% last month.



- **Westpac (WBC)** announced a pretax gain of around \$270m after Visa Inc listed on the NYSE. The ANZ will also book a \$350m pre tax profit as a significant item in its interim result on April 28, so will the CBA (\$355m), the National Australia Bank (\$221m) and St. George Bank (\$75m). WBC up 0.17% last month, ANZ up 1.92%, CBA down 3.5%, NAB down just, 0.5%, and SGB up 1.21%.
- **David Jones had interim results** - Profit up 25% at the top end of expectations. The stock is down 38.4% from its recent highs and struggled last month like the rest of the retailers, down 14%.

- **The Goodman Family sold down shares in the Goodman Group (GMG)** in order to avoid the need for margin calls. GMG has been down 52% at its worst. They have sold 78m shares at 370c and against the price at the time of 409c. "The majority of securities have been acquired by GMG global equity partners in the Middle East and Europe". GMG lost 6.6% last month.

- **ABC Learning (ABS)** was smashed after results and following the MD Eddy Groves losing almost his whole stake in the company to a margin call. There was a rumour (denied by the company) they were in breach of their banking covenants. Despite that the company maintained their earnings guidance for the full year and announced they are selling a 60% stake in their US business for \$750m to Morgan Stanley Private Equity. They will use the \$750m to pay down debt. They say that at no point has the company been in breach of its banking covenants and that following these transactions they will be in a strong financial position. They also expect to conclude the sale of their UK vouchers business in H1 2008 by tender (the papers say it will fetch £100m).



- **SP Ausnet (SPN) upgraded earnings forecasts** for 2008/9. They expect earnings up 15% to \$147.5m and distributions up 2.5%. SPN flat on the month.
- **Nufarm** interims results were in line with the company forecasts. Revenue up 71%. They reiterated guidance for a FY operating profit of \$150m. "The outlook for the remainder of Nufarm's 2008 financial year is positive". NUF was up 2.2% in March.
- **Ten Network (TEN)** released its 1H result which Missed analysts' expectations. EBITDA up 11%. TEN lost 14.8% last month.
- **Brickworks (BKW)** announced its 1H profit result. Up 9.7% to \$40.3m. Fall in construction affordability and access to affordable land to continue to affect profits. Predicts building industry will continue to face tough times. BKW up 0.7%.
- **Incitec Pivot (IPL) - profit upgrade** – earnings expected to rise 135% this year on doubled fertilizer prices. Forecasting EBIT of \$700-730m against consensus forecasts of \$625m (10-15% ahead of expectations).
- **Allco Finance Group (AFG)** announced David Coe, Gordon Fell and David Turnbull have stepped down as executive directors. The board is now searching for an independent chairman. AFG down another 68% last month.
- **City Pacific (CIY)** got smacked after one of its funds - City Pacific First Mortgage Fund - breached a condition on a loan from the Commonwealth Bank of Australia (CBA). CBA has demanded the

fund pay back a \$240m facility by May 31, with a first instalment of \$90m due by March 31. CIY fell 49% on the day of the announcement or 94.5c to 97.5c before going into a trading. Not great news for the banks and not great news for other financial engineers. **City Pacific (CIY)** also announced it will sell its interest in the Townsville Ocean Terminal to CEC Group for \$30m. It expects to receive \$12.5m of the sale price in the financial year ending June 30, \$12.5m in the 2009 financial year and \$5m in the 2010 year. CIY down 61% in March.

- **Gerry Harvey bought 2m HVN shares** at 389c after a near halving of the share price in 5 months. He joins one of the many directors putting on a display of faith in their own company during the correction. Othe notable companies in which directors have been actively buying their own shares include the ANZ and the NAB. The Commonwealth Bank just became a substantial shareholder in HVN. HVN down 26% last month...shocker.

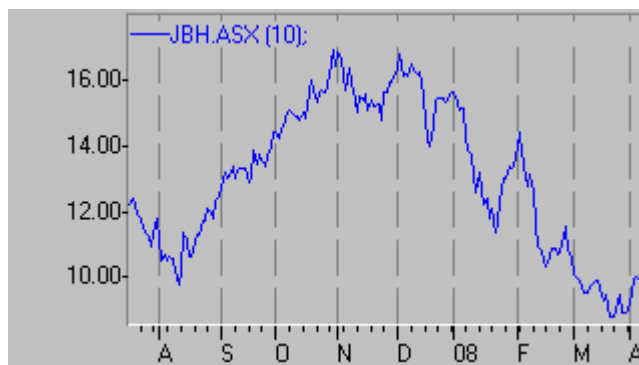


- **Foster's (FGL)** - UBS Warburg wrote a bit of research on Fosters nothing the UK government's 2008 budget included a 14 pence per bottle or 10% increase in wine duty compared to a 4% rise last year. "While largely anticipated, this increase is effective immediately and creates another headwind for Foster's (FGL) to manage". Despite that they upped their recommendation on Fosters to BUY earlier in the month with a 653c target price. FGL did OK – down 2.5%.

- **Gaming sector** - The Victorian government announced ATM's will be removed from gaming venues by the end of 2012. Crown Casino will be exempt. Were's said the impact will be negative for the gaming sector, but is difficult to quantify. Tabcorp (TAH) down 8% in March and Tattersalls (TTS) lost 11.2%.

- **Billabong (BBG)** outperformed after a Citigroup recommendation to BUY after an analyst briefing. They say "long-term investors should be rewarded by a company we expect to sustain 15%-plus EPS growth for the next five years." BBG down 1.1% on the month.

- **JB Hi-Fi (JBH)** upped their store rollout program and now expects to add another 30 stores in Australia and New Zealand. Now targeting 150 stores instead of 120. JBH struggled with the rest of the retail sector. down 20% on the month.



- Talk is that **Toll Holdings (TOL)** is having difficulties selling its 62.7% stake in Virgin Blue. Toll said on February 21 that it expected a resolution in "several weeks" and that is much prefers a stake of 20 to 25%. TOL down 4.7% in March.

- **Asciano Group (AIO)** has announced an interim profit results including a loss. The stock has halved in value since listing at 1076c, last traded at 497c. Concerns grow over its huge debt levels. Revenue was up 3.9%. They see organic growth in EBITDA of 10-15% a year over the long term.

- There was a bit of a rebalancing of the ASX S&P indexes. **Ausenco (AAX)** and **Equinox Minerals (EQN)** joined the S&P/ASX 200 index along with **Felix Resources (FLX)** and fund manager **Platinum Asset Management (PTM)**. **Boom Logistics (BOL)**, **City Pacific (CIY)**, **Compass Resources (CMR)** and **STW Communications (SGN)** were given the boot.

- **Domino's Pizza** acquired Pinky's Pizza. Were's say it's a good bolt-on acquisition and will provide DMP with economies of scale. DMP is on Were's Conviction BUY list. DMP down 2% in March.



- **Macquarie Media Group (MMG)** will sell its 60% stake in Taiwan Broadband Communications to Macquarie Korea Opportunities Fund for around \$400m. If regulators give it the OK, the deal is expected to be completed in the 2Q of the 2008 calendar year. MMG down 5.7%.

- **AGL Energy (AGK)** announced it will sell its GasValpo Chilean gas distribution business and associated assets for US\$90m. The buyers are a consortium of Australian pension funds. Under the sales agreement, the consortium will refinance GasValpo's debt of US\$26m and the remaining

\$US64m will be used to pay down AGK's debt. The sale will result in a small profit but won't alter the company's \$330m-\$360m earnings guidance. AGK managed to lose 4.5% last month.

- **Credit Corp Group** (CCP) updated the market with its strategic review – it is seeking expressions of interest for the sale of two of its businesses. CCP up 37% for the month.
- **MFS** (MFS) shareholders approved a change in the company's name to **Octaviar Ltd.** One way to try and sweep a multitude of sins under the carpet. Re-brand. But we we'll remember they are really MFS, a stock that has lost shareholders 90% of their investment this year. MFS (now OCV) still in a trading halt as it tries to work out its finances and operating structure.

## Company news: Resources

- RIO making headlines with comments from Sam Walsh the head of the iron ore division saying a US recession would knock 1% at most off Chinese GDP growth which is running at 11% and that a **US recession will not therefore affect the resources sector**. 90% of the growth in iron ore has come from China. He also commented that India is "approaching the same take off point China reached in 2002-03". All good news for the whole iron ore sector to hear one its most important managers so upbeat. RIO down 10% last month.
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- **Iluka completed an institutional share placement** – it was 3.5x oversubscribed suggesting strong support (but it was a very deep discount). ILU had a great month, up 31%.
  - **Oil Search** (OSH) published their Strategic Review. Main points:
    - Poised to enter FEED stage on PNG project.
    - In a strong financial position.
    - Looking to sell some international assets.
    - Financing for PNG project is available despite credit crunch.
  - Macquarie Equities had a bit of research out recently saying they could jump 20% on the decision to move to the FEED stage on the PNG project. Nearly there, up 10% in March. Macquarie have a BUY recommendation and a 620c target price. They recently bottomed at 396c.
  - **Santos** (STO) announced its Managing Director John Ellice-Flint will step down after 8 years. He has been in charge since 2000. Executive vice president David Knox will be the acting chief executive while the company looks for a replacement. STO up a big 13% in March.
  - **Fortescue Metals** (FMG) say the final cost of its Pilbara mine and infrastructure project in WA were up \$31m to \$2.8bn but that the company remains on track to ship its first iron ore in mid-May 2008. FMG had a bad month, down 22%.
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- **Admiralty Resources** (ADY) shipped the largest single load of premium quality iron ore ever. The company said the MV Bright Bulker was loaded the "brim" with 49,560 tonnes of premium quality iron ore. ADY struggled, down 34% - it was caught up in the OPES administration with a large lump of ADY stock ending up in the hands of administrators.
  - **Pan Australia** (PNA) - which has hardly moved despite the gold price hitting the \$1,000-an-ounce level – says it has received a few takeover approaches, but nothing concrete. Its MD Gary Stafford told Bloomberg "Yes, there are always people making proposals to us but nothing ever forms". The company is due to start output this month at its \$241m copper and gold mine in Laos. Were's has a BUY recommendation and 130c target price, 40% above current share price. PNA down 7.8% in March.

- **Albidon (ALB)** announced assay results from Zambia showing “significant uranium mineralization”. This is the company that placed stock to the Jinchuan Group in December above the market price. They have been rumoured as a possible takeover target for the combined Oxiana Zinifex company. Keith Goode from Eagle Research Advisory published a BUY recommendation saying BUY with a target of >A\$5.00/share”. Share price now 345c.
- Our resources analyst highlighted **a few resources stocks he would buy on weakness** in the sector (no advice on timing):
  - **Western Areas (WSA)** – They will have more drill results on Spotted Quoll in April/May. Likely to be good. They are cum good news, cashed up and don’t need money for development. WSA up 0.17% in March.
  - **Mincor (MCR)** – Very good value. 8 operating mines and one more likely to be added this year...can therefore absorb individual operational hiccups if they occur. Lower risk. It trades at 285c...a 29% discount to the NPV of 400c. That compares to its peers trading on a 10-15% discount. MCR down 6.4% last month.
  - **Sally Malay (SMY)** – Exploration news likely to continue to drive the price for now. They are drilling two new areas and have already had encouraging intersections. Expect more and the likelihood that they will be able to increase mine life estimates on both their projects. SMY up 4.16% in the past 30 days.

## Takeover Action

### Industrials

- **Challenger Infrastructure Fund (CIF)** which is managed and around 33% owned by **Challenger Financial Services (CGF)**, received a \$2.1bn takeover proposal from a unit of the UK firm Consensus Business Group. The offer is non-binding with an indicative price of 350c a share. The CGF share price took off after one journalist stuffed up and wrote on the wires it was CGF that was getting taken over and not CIF. CIF up 13.5% and CGF down 21% in March - horrid month for CGF which **fell over 20% in a week** on the news that a major shareholder had been pushed into selling on margin (a company called Cardiac Jolt sold 15m shares). The price fell from 316c to 151c. James Packer has 19.2% in CGF and was rumoured to be a buyer of the stock.
- **Bendigo Bank** had a good month – up 10% - According to the *Herald Sun*, France’s BRED Banque Populaire is building a stake in the company. Banque Populaire also built a 6.3% stake in Queensland Bank before disclosing it to the market. BEN also reaffirmed its EPS growth forecasts of 12% for the FY. JP Morgan believes the chances of French company, BRED Banque Populaire, bidding for **Bank of Queensland (BOQ)** is minimal despite an announcement that it has also lifted its stake to 7.44% from 6.44% in BOQ.
- **Incitec Pivot (IPL)** has acquired **Dyno Nobel (DXL)** – the deal values DXL at \$3.3bn or 280c a share and will involve its shareholders receiving 0.01406 IPL shares and 70c cash for each DXL share. Speculation about the deal has been going on for a while. DXL board unanimously recommends its shareholders vote in favour of the deal. IPL lost 8.4% and DXL put on 9.3% in March.
- **QBE Insurance (QBE)** down 7% in march despite having to tell the ASX it didn’t know why the share price went on a huge rally mid

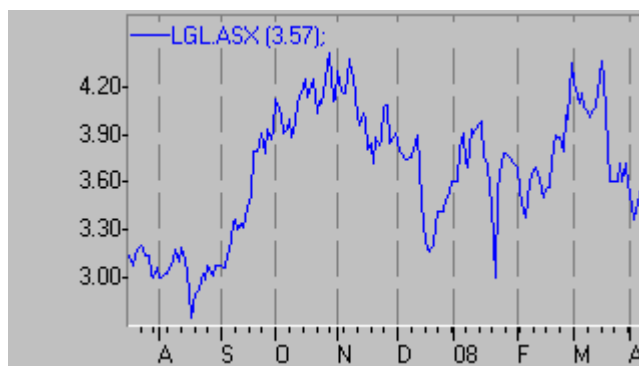
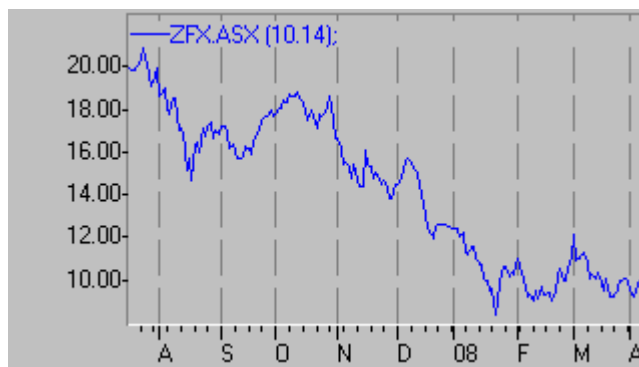


month and that it isn't aware of any takeover approach. There is rumour that Warren Buffett's Berkshire Hathaway might even launch a takeover offer. QBE down 7% in March.

- **Spotless bid for Programmed Maintenance Group (PRG).** The SPT bids for PRG offering \$6.11/share (PRG last traded at 454c). Implied EV/EBIT of ~13X and P/E of ~18X. Three different cash and scrip alternatives for PRG to consider. They have secured relevant interests from three of PRG's largest institutional holders, representing over 10%. Clear synergies exist between two businesses, across facilities management arena. View from our analyst - Makes sense from an operating perspective, with both companies strong in the facilities management arena. PRG's CEO Chris Sutherland (formerly MD of IWF) appears to have the golden touch (PRG acquired IWF not long after Sutherland became IWF MD). Multiples appear satisfactory, especially given current equity market conditions. PRG up 18% on the back of the approach. SPT down 20%.

## Resources

- **Rio Tinto's** CEO Tom Albanese labelled BHP's \$150bn takeover offer as not good enough. He said the 3.4 a share bid "fails to recognize Rio Tinto's outstanding assets and prospects" and gave insufficient incentive to deviate from a "proven path to value creation." He talked up RIO's aluminium assets and that strong demand from China is expected to continue in 2008 and 2009.
- **Oxiana bid for Zinifex.** Amazing that Oxiana would have flagged the possibility to the press so openly ahead of the approach. It is an agreed merger. Terms 3.1931 OXR for one ZFX. At the current price of OXR at the announcement (397c) it values ZFX at 1267c. It is effectively a 50/50 merger. It makes them the third biggest diversified miner in Australia. Attractive prospect for institutions looking for a better growth profile than BHP or RIO. It gives both companies a more attractive critical mass for investors and the tag line is that they have created/replaced WMC with a solid growth profile and significant cash. The cash will allow them to develop projects and acquire new ones. It propels them to number 4 in the resources sector behind BHP, RIO and FMG. Oxiana has good long term assets with development potential. Zinifex has a lot of cash (\$2bn less \$800m cost of AGM bid) to develop those projects (Prominent Hill and Golden Grove) and buy new ones. It will be a significant copper Zinc play with some Nickel. There are synergies with head office costs amongst others.
- There was **speculation about who Oxiana and Zinifex (or should that be Ziniana or Oxifex) will bid for next.** Names mentioned so far include Equinox (EQN), Kagara (KZL), Albidon (ALB), Independence Group (IGO), Pan Australian (PNA) and First Quantum (Canadian listed).
- **Lihir Gold (LGL) and Equigold (EQI)** announced a merger which is effectively an LGL \$1.1bn takeover offer for Equigold. EQI shareholders will receive 33 LGL shares for every 25 Equigold shares they own. Offer values the company at 533c a share or **\$1.1bn**. 24% premium to EQI's 430c closing price the day before the announcement. EQI and LGL directors have unanimously approved the merger. Combined market cap of the two companies will be \$9bn. Combines group will have 25m ounces of gold



reserves and operations in Papua New Guinea, Ivory Coast, Victoria and QLD. Merger to add significant growth potential and exploration upside. Each company has agreed to pay a break fee of \$11.3m to the other if the deal goes pear shaped. LGL down 7% in March and EQI up 8%.

- The CEO of **Midwest Corp** (MIS), Bryan Oliver, said the company is worth at least 700c a share compared to the 560c a share cash offer put forward by China's Sinosteel. MIS advise shareholders to take no action on Sinosteel's bid. MIS up 22% last month.
- Staples Inc of the US confirmed its bid for **Corporate Express'** (CXP) parent company, Corporate Express NV of the Netherlands (CXPNV) during the month. The board rejected the takeover bid. CXPNV owns 59% of CXP. Were's expects the takeover to support CXP's share price in the short term. They maintain their HOLD recommendation and 690c target price. CXP up 6.2%.
- **Indophil Resources** (IRN) made a 100% off-market all scrip 165c a share bid for **Lion Selection** (LST). IRN say if the offer goes unconditional, they will up their offer to 178c a share. IRN up 4.4%.

## Chosen Article

By Marcus Padley from MARCUS TODAY

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### THE AVERAGE MAN

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The average home loan commitment for owner occupied dwellings in Australia is \$240,300. That doesn't sound too scary but consider the possibility that you actually had to pay that off. That's a lot of cold hard cash to find that after tax. It would mean saving money. Considering most of us already spend 110% plus of everything we earn every year and save nothing it's a big ask.

As a Poor Dad (earning a salary without equity in your business) the prospect of paying the mortgage is bleak. Do some quick numbers and it becomes clear that you would in fact need to save \$1000 (post tax) every month for twenty years to retire mortgageless. That's about \$24,000 of pretax salary you just lost. And if you have less than 20 years to retirement you need to scale up the numbers accordingly.

But there's more. Then there's the \$20,000 of interest every year (soon be \$24,000). Pretax, that's another say \$40,000 off your salary.

Now your average mortgage repayment plan has cost and lost you \$65,000 of salary.

Manageable you might think, but when you consider the average wage in Australia is \$60,434 it becomes clear that the average mortgage is crippling the average man. Someone out there is underwater and if they are to retire debt free (how dull) they will either have to earn a lot more than the average man or at some point downsize their property or risk a drop in their standard of living.

If the definition of happiness is the expectation of an improvement in our standard of living then the expectation of a drop in our standard of living is the definition of unhappy. The average man is unhappy and if he isn't, he's in denial. Hmm.

I have a theory that the more liability you load on yourself (mortgage, kids, responsibilities) the more you get out of life. Debt and responsibility drives us to better ourselves, to improve, innovate, learn and assert. When faced with debt myself I have always lived by the creed "earn more" rather than live like a miser and pay it off. That attitude comes with the luxury of youth, I'm only 46 (cripes – that old). But the time is coming when my earning capacity will likely plateau, not because I can't earn it but because for once in my life I might want to sit down with the wife and read the newspapers without having to rush. Just once would be nice. And it's that desire that will set my financial time frame. It's a while away but it will one day come into focus.



The route to my own happiness has been to set expectations (you'll need to do that with the other half), work out how to deliver them and then hopefully (usually) beat them. As one of my brother-in-laws once said, most dreams are fulfilled by those who set out to fulfill them, the problem with most dreams is that people don't dream hard enough. To achieve your dreams you need unrealistic expectations and to set those you need to take a moment and set expectations. To do that you need a plan.

I went to a financial planner once. We did some very basic planning. In fact it is almost an embarrassment to the industry that financial planning is so simple to do (yet so few of us bother). Get a pen. Get an envelope. Turn to the back (its better on an excel spreadsheet).

Very simple. Set up a chart with two columns for every year starting with the current year. Column A and column B.

In column A put expected post tax income. Sounds simple. But the process teaches you a lot about yourself. When you actually look at "expected" income you realise that you simply cannot count the "unexpected income" we all expect. Like stock market gains, bonuses, inheritance, house price appreciation, lotto. They are "risk" items and in a financial planning sense are not guaranteed and cannot be relied on. When you can only put down "expected" income your future prospects suddenly depart from your subconscious expectations. The future starts to look sparse. And that's before you factor in "unexpected losses".

In column B put expected expenses. Household expenses and any predictable annual costs, car loans, utility bills, usual stuff (make a guess).

Food is a big item and you have to inflate by the estimated combined expected annual body mass increase of your many children and their expected length of stay in your abode (Make note to tell kids its your house and that they are simply passing through on your good nature). Multiply costs by 1.5 for boys. You will quickly realise your budget becomes unworkable unless you chuck most of them out at the age of 10.

But the mortgage and mortgage interest and school fees are the major spending items. Inflate school fees at 6% per annum (optimistic) and leave a function to vary that. Then add an unexpected spending column to account for your dreams (annual holiday to Club Med in Bali and the renovation).

You are now looking at reality and if you're anything like column B vastly outweighs column A for about the next years.

After that little game a few things will have hit you.

- You need to earn more.
- Spend less.
- You are in denial.
- You'll be working until you're 75.
- You need a major score or you'll never retire.
- 

Either way it will become clear the "Never Never" is really "Today". Planning isn't hard its simple. Happiness knowing where you are (both) going and going there. if you want to be really happy, set your sights as low as possible. Do that and all your dreams will come true.

The Mother of all stuff ups



"I'VE TAKEN ANOTHER CLOSE LOOK AT THE BUDGET, AND I'M SORRY I'M GOING TO HAVE TO LET TWO OF YOU GO."

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## ON THE HEDGE

# HEDGE FUNDS

The traditional hedge funds work like this. You put up \$20. Your hedge fund manager uses it to borrow \$100 worth of stock (by putting up 20% of collateral). He then sells the stock. Now he uses the \$100 he just raised to buy another stock. Net effect, for a \$20 stake he has created \$200 worth of exposure.

And that's the definition. A lot of firepower for a small capital outlay. No wonder the expression "hedge fund manager" has (used to have) cachet. It stands for having balls, a noble quality in this industry, as long as its backed by brains. And there's the rub.

The average hedge fund in Australia apparently gears up around 8x. That means if you put a \$10 investment into an Australian hedge fund they create \$80 of exposure for you. Its just gearing, not rocket science.

# LEVERAGE

But if you work the numbers you will soon realise that a 5% fall in the value of the investments then causes a 40% fall in the value of the equity holder's stake. Cripes. In fact a 12.5% fall in the value of the investments delivers the equity holder a 100% loss. Double cripes.

One hedge fund in Sydney this year froze redemptions after the value of the fund fell 3% in a month. That 3% fall caused a 25% fall in value for its equity holders. Faced with that the investors hit the doors. Redemptions poured in and redemptions is where the trouble really starts.

With hedge fund redemptions the gearing works the other way around. To repay a dollar to an equity holder the fund has to sell \$8 worth of exposure. Suddenly small requests for a refund translate to big market selling. As the selling starts the securities the fund is holding and selling fall in value causing further falls in the value of their funds, further requests for redemptions and further selling. Snowball. The Sydney fund eventually went to the wall despite its "High Yield Fund" tag. Their investors included the most conservative of charities, super funds and some of the countries most sophisticated (ahem) investors.

# ASSUMPTION

Assumptions are the root of all major losses and all our current travails stem from one "Core Assumption Failure". For the last 18 years we have assumed that people will suffer any deprivation rather than miss a payment on their mortgage. It is an Australian tradition and our mistake is that we have judged others by our own standards. We have been surprised because it turns out that there are billions of dollars of mortgages in the US sold *by* people who didn't care *to* people who didn't care. To people who didn't repay their mortgages. They didn't have our standards. Core assumption failure, the root of all major catastrophes. Add gearing to the failure of "load bearing" assumptions and you have collapse.

Next time you are surprised by anything, including a share price fall, ask yourself, what assumptions have I made. They are the bedfellow of error and surprise.

Back to those nasty nasty hedge funds.

Hedge funds are blamed for almost everything these days and people are getting very upset at the recent Smack Downs, when stock prices get belted, become "inefficient" and cease to reflect their fundamental value. But rather than fight "The Man" I suggest we encourage him. The reality is that an inefficient price is an

# SMACK DOWNS

opportunity. Too high or too low we should shut up, act on it, and take a moment to admire the guts and folly of those who managed to push it there, because they surely cannot hold it there.

Short term pricing does not have to be correct. The stockmarket cannot reflect true value at all times and what a yawn it would be if it did. Let's not dumb it all down so everyone can sleep at night. Do that and I for one may not bother getting up the next morning. Bring on the next smack down I say.

Hedge funds provide a service, putting weak companies under pressure and it is only when systems come under pressure that the weaknesses appear. It is all part of the Circle of Life (cue Elton John), every piece essential to the efficient function of the whole system.



Some people want to be on the edge. They are allowed to be. Hedge funds and their leverage just one investment option available. You wouldn't want it any other way. Hedge funds not a scourge, they are a

choice and they provide a very necessary service offering investment sophistication, risk and leverage to those of us who are not smart enough to create it ourselves. You don't have to invest in them.

Of course it's not much fun if you are the long term shareholder getting beaten up in a besieged share price. But rest assured, the only thing that matters is value and you have to assume that one day, in another timeframe it will re-assert itself.

And there we go. Making assumptions again.



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