

NEXT Daily – Wednesday 28th April 2010

Overseas

The **Dow Jones** fell 213 pts or 1.90% to 10,991.99 (YTD 5.41%), **S&P 500** fell 28 pts or 2.34% to 1,183.71 (YTD 6.15%) and the **NASDAQ** fell 51 pts or 2.04% to 2,471.47 (YTD 8.92%)

The **FTSE** fell 150 pts or 2.61% to 5,603.52 (YTD 3.52%), **Nikkei** rose 46 pts or 0.42% to 11,212.66 (YTD 6.32%) and the **Hang Seng** fell 325 pts or 1.51% to 21,261.79 (YTD -2.79%)

Oil fell \$1.77 to \$82.43 a barrel.

Gold rose \$16.10 to \$1,169.60 an ounce.

Base metals were weaker with Copper down 4.12% to \$338.03, Nickel fell 4.53% to \$1,173.22, Zinc was down 3.32% to \$105.55 and Aluminium fell 7.27% to \$96.06.

BHP ADR's trading at \$40.92 vs the Aussie close of \$42.00.

SPI 200 Futures closed down 89 pts at 4,795.

Ideas

Concerns over Europe and Financial Reform in the US have overshadowed a better than expected US reporting season and positive economic data. Of the 36% of US companies that have reported to date, 81% have beaten expectations said JP Morgan. Consumer confidence in the US increased from 52.3 in March to 57.9 in April vs mkt expectation of 53.5 and the Richmond Fed regional manufacturing survey surged from 6 to 30. However, this was not enough to offset the concern around Europe. The S&P has downgraded both Greece and Portugal. Greece was cut to junk, which is raising significant worries (especially if Moody's also downgrade) about the ability of Greek banks to use Greek Gvt Bonds at the ECB collateral window. Contagion is becoming a very real concern as the focus spreads from Greece to other countries. Investors are still waiting to hear specifics on the EU/IMF aid package while Germany shows signs of dragging its feet. A Reuters article has revealed that EU/IMF talks w/Greece could wrap up by May 2, with Eurozone leaders talking May 4 and then a vote by Euronations taking place on May 10 (this timetable would accommodate Greece's May 19 debt payment). CDS spreads continue to explode wider across the PIGS – Greece is out 66bp to 800, Portugal is out 34 to 342, Ireland is out 20 to 213, Spain is out 16 to 191, Italy is out 9 to 148.

Australian Consumer Price Index data is due to be released today which will provide a guide as to how the economy is handling the recovery amid renewed activity in the resource and employment markets. The market is expecting the CPI number to show a gain of +0.8% qoq +2.8% yoy. This data will be a major factor for the RBA when they meet in May to discuss their interest rate policy. Royal Bank of Scotland has looked at inflation trends and their impact on firms price setting policies and RBA actions stating, or the market versus the RBA :

Our past work showed that firms are heavily influenced by past inflation trends when setting prices, although they do pay attention to expected inflation. For expected inflation, we find that that the consensus usually beats the RBA in forecasting headline inflation, although there's not much in it given that both have

large forecast misses. For underlying inflation, the RBA has had an average absolute forecast error of about ½pp over recent years. The RBA persistently underestimated inflation during the first stage of the resources boom and it has since factored in a shallower trough in inflation given that the economy has performed much better than had been expected. With a smaller inflation dividend from the global financial crisis than had been expected and the resources boom roaring back to life, we doubt the RBA wants to make the same mistake again and this is why we expect tight policy next year, with the cash rate eventually reaching 6½%.

Continuing our coverage of the major brokers view of the upcoming Bank reporting season, Deutsche Bank (DB) has reviewed their forecasts ahead of the major bank reporting season, which has led to 2-6% upgrades for the majors in FY10. DB said:

We expect banks to deliver strong earnings growth underpinned by continued margin improvements, solid trading income and improving impairment charges. While banks should perform well on the back of these trends, we believe upside risk has largely been captured in what appears fully priced multiples (sector is trading at 12% discount to All Indust. vs 10 year average of 22%). Within the majors our preference is for WBC over ANZ.

We expect the majors to deliver a solid revenue performance underpinned by improving margins (book mix benefits; remaining asset repricing; and benefit of free funds as a result of higher interest rates) and continuing favourable conditions in the markets business. However, in the medium term (FY11 and FY12) we expect margins to come under pressure as highlighted in our recent report *"Not so cosy anymore"*. As such, in our view, the focus in the reporting season will be both on the extent of underlying margin improvements and outlook commentary from the management on the competitive landscape.

While management across the majors were generally cautious on the impairment trends following lower than expected charges in 1Q10, given absence of notable large corporate losses and with improving macro trends we expect the majors to again positively surprise the market with a larger than expected BDD reductions. We estimate if 1Q10 impairment trends persist, this would imply upgrades to 1H10 cash earnings of 5% - 6% for the majors.

While we expect banks to deliver strong EPS growth (14-31%) in 1H10, which would generally suggest a strong performance for the sector, we struggle to see material upside for the banks given relatively full valuations. Based on our forecasts the sector is trading at a FY11 discount of 12% to the All industrials (ex banks) vs. a historical 10 year average discount of 22%. In our view, WBC and CBA are likely to perform well during the reporting season, underpinned by positive earnings surprises. We believe that consensus for WBC is to low and hence positive upside surprise is likely to result in a share price outperformance. As a result our preference is for WBC over ANZ, given ANZ's upside risk has largely been captured by its outperformance over the last quarter (outperformed the market by ~10%) as the market largely captured the upside risk from improving margins and reducing bad debts.

Research

West Australian Newspapers Holdings Limited (\$8.04) – With WAN's 3Q10 NPAT below forecasts, GSJB Were, Macquarie and JP Morgan have retained a BUY, Deutsche, Citigroup and Credit Suisse have maintained a HOLD whilst RBS have **downgraded** to a HOLD and UBS have **downgraded** to a SELL. GSJB Were has a price target of \$9.15.

Oil Search Limited (\$5.79) – Following their 1Q10 production results in line with forecasts, Deutsche, UBS, RBS, Macquarie and JP Morgan have maintained their BUY whilst Credit Suisse and GSJB Were have retained a HOLD. UBS has a price target of \$7.87.

Centennial Coal Company Limited (\$4.52) – With their 3Q production results out, JP Morgan and Deutsche have maintained a BUY whilst Credit Suisse, UBS, GSJB Were, Macquarie have retained a HOLD and RBS have **downgraded** to a HOLD. GSJB Were has a price target of \$5.66.

Infigen Energy (\$1.02) – Following their decision to retain the US business, Citigroup and Deutsche have retained a BUY whilst Credit Suisse, GSJB Were, JP Morgan have maintained a HOLD and RBS have **downgraded** to a HOLD. Citigroup has a price target of \$1.50.

Bank of Queensland Limited (\$12.03) – With the announcement that BOQ will acquire it's A\$500mn CIT leasing portfolio, Macquarie and JP Morgan have retained a BUY whilst Citigroup and GSJB Were has maintained a HOLD. JP Morgan has a price target of \$15.26.

Origin Energy Limited (\$16.11) – With the updated oil prices and currency, Credit Suisse has **upgraded** ORI to a BUY with a price target of \$19.00.

Super Cheap Auto Group Limited (\$5.07) – Following their acquisition of Ray's Outdoors for \$54mn, GSJB Were has **upgraded** to a BUY with a price target of \$6.50.