

NEXT Daily - Thursday 29th April 2010

Overseas

The **Dow Jones** rose 53 pts or 0.48% to 11,045.27 (YTD 5.89%), **S&P 500** rose 7 pts or 0.65% to 1,191.36 (YTD 6.80%) and the **NASDAQ** was flat at 2,471.73 (YTD 8.92%)
The **FTSE** fell 16 pts or 0.30% to 5,586.61 (YTD 3.52%), **Nikkei** fell 287 pts or 2.57% to 10,924.79 (YTD 3.75%) and the **Hang Seng** fell 312 pts or 1.47% to 20,949.40 (YTD - 4.26%)

Oil rose \$1.59 to \$83.30 a barrel.

Gold rose \$0.80 to \$1,171.00 an ounce.

Base metals were mixed with Copper down 1.20% to \$336.00, Nickel fell 1.10% to \$1,164.00, Zinc was down 1.30% to \$106.00 and Aluminium rose 1.90% to \$99.00.

BHP ADR's trading at \$40.90 vs the Aussie close of \$41.07.

SPI 200 Futures closed up 7 pts at 4,833.

Ideas

U.S. stocks clawed back a portion of Tuesday's selloff after the Fed left interest rates unchanged and kept the "extended period" language in its statement. Earlier, stocks had slipped into negative territory after the S&P downgraded its debt rating on Spain. S&P downgraded the sovereign credit ratings of Spain. The agency cut its rating of Spain to AA from AA+, reflecting the country's deteriorating budgetary situation and weaker economic outlook. On the profit front Dow Chemical Co. continued the trend of good results with Q1 profit soaring on strong sales, reflective of higher volumes and prices. European shares extended declines in a tumultuous session, with markets rattled by the third sovereign credit downgrade in two days.

The Henry Tax review is expected to be released on Sunday May 2. This is a broad based review of the Australian tax system and will make recommendations for changes which the Federal Government may elect to implement. Of particular relevance and concern to the Australian minerals industry is the potential for a Minerals Resource Rent Tax (MRRT) to be recommended as a replacement for, or worse case, as an addition to, existing State based royalties. Currently, the States impose royalties anywhere from 2.7%-7.5% on minerals **revenues** generated (mostly, there are some exceptions where the royalties allow operating cost deductions making them a profit based royalty), depending on the type of mineral and the State in which the extraction occurs. The royalties are an allowable deduction for corporate tax which is applied by the Federal Government. JP Morgan (JPM) is discussing the implications of such a tax said:

A MRRT would be applied by the Federal Government and we assume it would be imposed in a similar fashion to the existing Petroleum Resources Rent Tax (PRRT), which is calculated at 40% of operating margin after deducting capital credits. The latter comprise cumulative capital expenditure and exploration expenses. The PRRT is allowed as a corporate tax deduction, and applies only to projects in Federal waters. With detail not yet available, calculations of financial impact rely heavily on assumptions that are made but if we assume the MRRT is quite similar to the PRRT then we estimate **the reduction in NPAT forecasts for BHP and RIO would be 27% (FY12e) and 36% (CY11e),**

respectively. Both companies would receive little capital credit offsets given their mature status and would be badly hit by a 40% MRRT. For companies with all of their assets in Australia, such as FMG, the reduction would be about 25% under a MRRT regime vs the current State based royalty system, with a greater absolute impact when we assume higher LT iron ore prices and hence operating margins. **In summary, the MMRT is severely punitive to high margin (top tier assets), mature companies and rewards developing companies with low quality assets that have high operating costs, low margins, and high initial capital investment.** We understand the minerals industry has not been consulted in the Henry review process. BHP specifically confirmed this in recent analyst forums and indicated they have not seen any specific detail as the MRRT proposal. In a recent analyst forum, CEO Marius Kloppers enunciated four principles which BHP believe should be adhered to in any proposed minerals industry tax reform:

- 1) It should be prospective, not retrospective;
- 2) It should be competitive with minerals tax regimes in other minerals rich countries;
- 3) It should differentiate (ie, different rates) between different commodities – eg, a flat rate tax will penalize lower priced thermal coal vs the higher priced iron ore operations; and
- 4) It should tax the resources, not the associated infrastructure.

JPM stated the MRRT is a “Nasty beast” and that “it must be defeated”, heavy opposition is expected from the minerals rich States, WA and Qld, as they should be reticent to give up control of their royalties.

Australia and New Zealand Banking Group (ANZ) reported this morning that its first half net profit rose 36% on year, boosted by lower charges for bad loans and higher profit margins amid improving economic conditions in its home market. In a statement, Melbourne-based ANZ said net profit for the six months to March 31 rose to A\$1.93 billion from A\$1.417 billion a year ago and the group declared an interim dividend of 52 cents a share, up from 46 cents last year. The group's net interest income rose 8% to A\$5.19 billion while its net interest margin widened to 2.68% from 2.36% the same time a year ago. ANZ recorded provisions for problem loans of A\$1.08 billion compared with a A\$1.37 billion charge last year. Provision trends look positive, although CEO Mike Smith still somewhat cautious about the outlook. Smith said bad debts were slowly improving, but it was an ongoing issue, particularly among small and medium sized businesses. "I think that we have done what we can for what we now know," he said. There would always be unexpected things which would "crop up", he said. ANZ said collective provisions increased slightly to \$3.037 billion from \$3 billion six months earlier. Collective provisions were 1.38 per cent of credit risk weighted assets. At the same time, gross impaired loans jumped 21 per cent to \$5.33 billion. The group's cash profit was A\$2.38 billion, ahead of expectations. The market had been looking for a cash profit of A\$2.286 billion, according to the average forecast of six analysts polled by Dow Jones Newswires. Expectations ranged from A\$2.14 billion to A\$2.363 billion. Analysts had also been expecting an interim dividend of 55 cents, although there was a broad range of expectations ranging from 48 cents to 62 cents. On the European sovereign debt concerns Smith said European sovereign debt issues could spread. "I think the uncertainty has continued and is possibly going to get worse because I think the contagion issue is now very real," he said. That could have an effect locally, Smith said. "In terms of the funding that the Australian banks have, in terms of their wholesale

funding, obviously credit spreads are going to be more volatile," he said. But Mr Smith said his bank was aiming to move lending rates in line with changes from the Reserve Bank of Australia. "The last thing we want to do is go above official rates," he said. "We feel that we have got to play our part in ensuring the economy is kickstarted. I think it is in everybody's best interest to keep rates as low as we can for the foreseeable future."

Research

Foster's Group Limited (\$5.39) – With FGL seeing softer beer performance in recent months, Credit Suisse and USB have retained a HOLD whilst Citigroup and GSJB Were have maintained their SELL. Credit Suisse has a price target of \$6.00.

ROC Oil Company Limited (\$0.45) – With their Dec 09 quarter sales revenue below forecast and the recent share price strength, Macquarie have maintained a HOLD, UBS have **downgraded** to a HOLD and JP Morgan retains a SELL. Macquarie has a price target of \$0.60.

Whitehaven Coal Limited (\$5.46) – Following WHC's 3Q sales in line with expectations, GSJB Were has maintained a BUY, RBS have **downgraded** to a HOLD whilst Deutsche, Credit Suisse and UBS have retained a HOLD. GSJB Were has a price target of \$6.63.

Asciano Group (\$1.72) – With container volume growth seen in the March 2010 quarter, Deutsche has **upgraded** to a BUY with a price target of \$2.10.

Aristocrat Leisure Limited (\$4.30) – Following commentary on the ALL's 2010 AGM, JP Morgan have retained a BUY, Citigroup and Deutsche have maintained a HOLD whilst Credit Suisse reiterates a SELL. JP Morgan has a price target of \$5.50.

MacArthur Coal Limited (\$15.90) – With MCC recording strong March quarter production and sales, Macquarie and RBS have maintained a HOLD whilst Deutsche and Credit Suisse have retained a SELL. RBS has a price target of \$16.00.

Virgin Blue Holdings Limited (\$0.58) – Following VBA's talks with Air New Zealand regarding a possible trans Tasman alliance, RBS, Deutsche and Credit Suisse have retained a BUY whilst Macquarie maintains a HOLD. Credit Suisse has a price target of \$0.90.

Flight Centre Limited (\$19.59) – With FLT's recent share price underperformance and the reopening of European air space, Credit Suisse have **upgraded** to a BUY with a price target of \$23.00.