

NEXT DAILY – 11th May 2010

Overseas

The **Dow Jones** rose 404 pts or 3.90% to 10,785.14 (YTD 3.42%), **S&P 500** rose 48 pts or 4.40% to 1,159.73 (YTD 4.00%) and the **NASDAQ** rose 109 pts or 4.81% to 2,374.67 (YTD 4.65%)

The **FTSE** rose 264 pts or 5.16% to 5,387.42 (YTD -0.47%), **Nikkei** rose 166 pts or 1.60% to 10,530.70 (YTD -0.15%) and the **Hang Seng** rose 506 pts or 2.54% to 20,426.64 (YTD -6.61%)

Oil rose \$1.76 to \$76.87 a barrel.

Gold fell \$7.13 to \$1,201.28 an ounce.

Base metals were stronger with Copper up 2.50% to \$321.34, Zinc rose 2.18% to \$95.57 whilst Aluminium was up 3.59% to \$95.90 and Nickel rose 2.01% to \$1,040.36.

BHP ADR's trading at \$38.90 vs the Aussie close of \$39.00.

SPI 200 Futures closed up 50 pts at 4,660.

Ideas

World markets staged an explosive rally overnight after European policy makers unveiled an unprecedented loan package worth almost \$US1 trillion and a program of bond purchases to stop a sovereign-debt crisis that threatened to shatter confidence in the euro. Goldman Sachs JBWere reported:

Jolted by last week's slide in the currency and soaring bond yields in Portugal and Spain, European Union finance chiefs met in a 14-hour session in Brussels overnight. The 16 euro nations agreed in a statement to offer as much as 750 billion euros (US\$962 billion), including International Monetary Fund backing, to countries facing instability and the European Central Bank said it will buy government and private debt. The rescue package for Europe's sovereign debtors comes little more than a year after the waning of the last crisis, caused by the U.S. mortgage-market collapse, which wreaked \$1.8 trillion of global credit losses and writedowns. Under U.S. and Asian pressure to stabilize markets, Europe's governments bet their show of force would prevent a sovereign-debt collapse and muffle speculation the 11-year-old euro might break apart.

"It might temporarily calm nerves but questions will come back later on how they will pay for this package when all of them need fiscal consolidation. The message has gotten through: the euro zone will defend its money," French Finance Minister Christine Lagarde told reporters in Brussels early today after markets punished inaction last week. ECB policy makers said they will counter "severe tensions" in "certain" markets by purchasing government and private debt, and the bank restarted a dollar-swap line with the Federal Reserve. Under the loan package, euro-area governments pledged 440 billion euros in loans or guarantees, with 60 billion euros more in loans from the EU's budget and as much as 250 billion euros from the International Monetary Fund. In a step that skirts EU rules barring direct central bank lending to governments, the ECB said it will conduct "interventions" to ensure "depth and liquidity" in markets. The purchases will be sterilized, meaning they won't increase the overall money supply in the financial system. Central banks in Germany, France and Italy all said they began buying government bonds today. None provided further detail. The ECB also reactivated unlimited fixed-rate offerings of three-month loans, a key tool in the ECB's efforts to fight the credit crisis. In Brussels, finance ministers from the 16-nation euro region -- joined by ministers from the 11 EU

countries outside the euro -- raced against time to weld the contingency lending arrangements before markets opened in Asia. Inability to craft a convincing package in time would have left deficit-plagued countries at the mercy of the "wolfpack behavior" of speculators, Finance Minister Anders Borg of Sweden, a non-euro member, said as the meeting began.

The new war chest would be used for countries like Portugal or Spain in case their finances buckle. Deficits are set to reach 8.5 percent of gross domestic product in Portugal and 9.8 percent in Spain this year, above the euro region's 3 percent limit. Both countries pledged "significant" additional budget cuts in 2010 and 2011, which will be outlined in May, an EU statement said. European Central Bank President Jean- Claude Trichet indicated the bank's decision to buy government and private bonds wasn't supported by all 22 Governing Council members. "On some of the decisions there was unanimity, I won't give details, and on some there was an overwhelming majority," Trichet said in an interview with Bloomberg Television today in Basel, Switzerland. "On bond purchases we had an overwhelming majority." The ECB announced overnight it will buy government and private bonds as part of an historic bid to rescue the euro after Greece's fiscal crisis spread to other indebted nations in the currency bloc. The move came in tandem with the unveiling by European finance ministers of a loan package worth almost \$1 trillion. ECB council member Axel Weber said today that purchases of sovereign debt pose "significant risks" and he's "critical" of that aspect of the central bank's contribution. "This decision is a decision of the Governing Council and not a result of any kind of pressure of any sort," Trichet said at a press conference in Basel after a regular meeting of central bankers from around the world. "We are fiercely and totally independent."

Domestically, the Rudd Government will hand down its latest budget tonight, at a time when the Rudd government is experiencing an unprecedented slump in popularity, therefore the government has the challenge of delivering a budget tonight which portrays "fiscal responsibility" (i.e. show us when & how we will return to surplus) but also gives enough to the average Aussie to win a few votes. Therefore JP Morgan (JPM) believes that, with the election still up for grabs, and the latest published opinion polls showing the opposition leading the government for the first time since 2006, the Budget almost certainly will include a few sweeteners for voters. JPM believes we should look out for the following:

- Confirmation of the **personal tax breaks** announced in last year's Budget. The 38% tax rate for those earning above A\$80,000 is being trimmed to 37%, and the A\$35,000 threshold raised to A\$37,000. The tax cuts are worth around A\$3.8 billion, but only around A\$6 per week to an average income earner;
- Confirmation of the planned cut to the **corporate tax rate** from the current 30% to 28% by 2014-15, which was announced last week;
- The provision of **tax breaks for interest** earned on saving deposits, as recommended by the review panel. These could take the form of separate tax-effective accounts, or a sliding scale of lower tax rates applied to existing accounts based on taxable income. The measure could boost deposits with banks, lowering the banks' reliance on offshore wholesale funding;
- Addressing the **punitive tax rates** applying to some low income earners when they move from welfare to work;
- Relief for **unincorporated small businesses**, which will not benefit from the planned cut to the corporate tax rate. There will be more detail on the tax write-off for capital spending announced last week;
- Possible changes to the **tax treatment of superannuation**, including a rise in the 15% concessional tax rate for high income earners, and the contribution limits;

- Easing the **taxation compliance burden** on lower income earners by, for example, making personal income tax returns optional (currently, filing a return is compulsory for all taxpayers earning more than the tax-free threshold);
- More funding for public **child care places**. The government recently controversially shelved promised plans to build new child care facilities;
- A rise in funding for **health and hospitals**, in line with the recent agreement with seven of the eight state and territory governments. There may be changes to private health rebates for higher income earners. New funding probably will be worth A\$7.4 billion;
- Changes to the public funding of **pharmaceuticals**. The package could save as much as A\$2 billion;
- An extra A\$500 million over four years will be spent on **border security and counter-terrorism**;
- Increased spending on **skills training**;
- Savings on **government air travel**, worth A\$160 million per year;
- A\$1 billion in savings from the recent cancellation of the **home energy program**;
- A possible boost to the **old-age pension** and possibly changes to eligibility criteria for other benefits; and
- Steps to improve **housing affordability** for first home buyers (FHBs). Possible measures include a boost to publicly funded construction to help alleviate shortages. The FHBs' grant and the existing tax break on investment in housing (negative gearing) probably will not be touched.

Further to this JPM said with many fiscal measures already in the public domain, the fluffiest "rabbit" the Treasurer will pull out of his hat will be the earlier return to surplus. The transition "back to black" will be helped by the first year of revenue from the new mining tax and the recent rise in the tobacco tax (worth A\$5 billion per year). The government announced the regressive rise in the tobacco tax two weeks ago, just days before releasing the tax review. Cynical commentators suggested this was to divert attention from the government's backflip on its commitment to address global warming; it shelved plans for an emissions trading scheme (ETS) until at least 2013 said JPM. Postponing the ETS will save the government A\$2.7 billion. Given a lot of the significant changes have already been announced as part of the Henry Tax Review (i.e. RSPT), JPM are not expecting anything too dramatic but with this government, never say never they said!

Interestingly, although not surprisingly regulatory risk has become a key concern especially from Global Fund managers. JPM said their London sales desk had feedback yesterday from a Global fund that Australia has now "fallen into the worst 3 markets in Asia for Political risk no sector is safe and they cannot put money into Australia until there is clarification not just on the Resources tax but any other industry tax this government might focus on next."

Research

Incitec Pivot Limited (\$3.18) – Following their 1H10 results, Macquarie, Credit Suisse, UBS and RBS have retained a BUY whilst GSJB Were and JP Morgan maintained a HOLD and Deutsche has reiterated their SELL. Macquarie has a price target of \$4.08.

Crown Limited (\$8.06) – With MPEL's 1st quarter results ahead of expectations, JP Morgan has retained a HOLD whilst Credit Suisse has **upgraded** to a HOLD with a price target of \$8.70.

UGL Limited (\$13.95) – Following their recent share price performance, Credit Suisse has **upgraded** to a BUY with a price target of \$16.30.

Ardent Leisure Group (\$1.19) – With AAD's 3Q10 results released, JP Morgan and RBS have maintained a BUY whilst GSJB Were and Macquarie have retained a HOLD. JP Morgan has a price target of \$1.68.

Avexa Limited (\$0.03) – Following the announcement that AVX has stopped development of its lead HIV program, RBS has **downgraded** to a SELL with a price target of \$0.02.