

NEXT Daily – 21 June 2010

Overseas

The **Dow Jones** rose 16 pts or 0.16% to 10,450.64 (YTD 0.22%), **S&P 500** rose 1 pt or 0.13% to 1,117.51 (YTD 0.22%) and the **NASDAQ** rose 2 pts or 0.11% to 2,309.80 (YTD 1.79%).

The **FTSE** fell 3 pts or 0.06% to 5,250.84 (YTD -2.99%), **Nikkei** fell 4 pts or 0.04% to 9,995.02 (YTD -5.23%) and the **Hang Seng** rose 148 pts or 0.74% to 20,286.71 (YTD -7.25%)

Oil rose \$0.39 to \$77.18 a barrel.

Gold rose \$11.65 to \$1,256.80 an ounce.

Base metals were weaker with Copper down 0.18% to \$290.66, Zinc fell 2.01% to \$76.97 whilst Aluminium was down 1.11% to \$86.82 and Nickel fell 1.07% to \$885.41.

BHP ADR's trading at \$38.89 vs the Aussie close of \$39.13.

SPI 200 Futures closed up 6 pts at 4,566.

Ideas

The Dow finished the week ahead 2.3% - the first time in seven months that the index posted back-to-back weekly gains of 2% or more. The S&P 500 Assisting with the gain was Caterpillar Inc.'s (+1.4%) retail sales rising in the three-month period ended in May, as demand for construction equipment in North America improved for the first time in nearly four years, according to sales figures released by the company. Citigroup advanced 1.3% as the bank is mulling a plan to raise \$3bln in private equity and hedge funds this year. Also positive signs in the US jobless rate showed that in 37 states and Washington, D.C. the rate fell MoM in May as the nation's unemployment rate dipped to 9.7%. European shares eked out yet another small gain as wins for banks offset losses for major pharmaceuticals. It was the eighth consecutive day of positive outcomes for the UK, its longest winning streak in 11 months.

JP Morgan (JPM) reported that the Bank of China (BoC) released a statement on Saturday that pledged to increase the flexibility of China's exchange rate regime and further improve the exchange rate mechanism. Overall this is in line with JPM's long-standing view that China would begin to allow more RMB flexibility by mid-year. This is because the window was closing for China to act before China-US relations get even more politically charged heading into the US midterm election. JPM Believes that since the US Treasury immediately responded positively to the PBoC statement the weekend's events look like a coordinated move by both Chinese and US governments, and potentially provides the US Treasury the leeway to release its delayed FX report without naming China as a currency manipulator. They also note that the PBoC statement falls short even of their modest expectation of a widening of the RMB trading band. Instead, the statement basically reiterated the official goal to "improve the exchange rate mechanism and increase the regime's flexibility" without specifying any concrete action. JPM have continually emphasized that RMB/USD management has been a bilateral political issue, so as long as US government finds this weekend's statement acceptable, then it seems unlikely that China will do anything more than this at this juncture. As such, to the degree that anyone in the market still expects a one-off, significant appreciation, such expectations will continue to be disappointed. The pace of RMB/USD appreciation will likely be accelerated as the Chinese government gains more confidence in the resilience of the global economic recovery and a soft-landing of the domestic economy. JPM continue to expect RMB/USD to reach 6.6 by end of this year.

UBS has looked at how Australia's debt metrics compare with the rest of the world stating:

This week - for the record - we canvas debt metrics for Australia often raised by investors. Drawing on UBS global research & RBA Deputy Governor Battellino's speech, we look at Australia's country 'risk'; comparing debt across government, households and corporates; net foreign liabilities; and current account deficit. UBS' macro risk index for Australia is one of the lowest for developed economies, as is the gross debt-to-GDP ratio at 199%, with our gap above Asia partly reflecting our later stage of financial deregulation. We have minimal Government debt of 23% (net debt is lower), quite low corporate debt of 66% (net of cash is 42%), but high household debt of 110% (albeit similar to major economies). While rising net foreign liabilities (55% of GDP) indicate increased vulnerability to currency & liquidity risk, Battellino notes that Australia is a developed economy with a floating exchange that can borrow in its own currency. Further, NFLs to total financing – indicating the proportion of offshore funding – drifted down to 20% over the last 15 years, while NFLs to the capital stock is steady at 10%. Capital inflows have largely been used to fund investment (not over-consumption), and we use foreign capital not because saving is low, but rather investment is high. Overall, we argue that Australia's external position leaves it more vulnerable to a higher cost of capital and slower growth, rather than some 'risk event'. And for the consumer, high debt explains why our above trend GDP growth in FY11 is based on above trend investment and housing - but only a return to trend consumption.

Telstra has announced that they have signed a non-binding Financial HoA with NBN Co to participate in the rollout of the NBN. In total, TLS estimates the total NPV of the deal to be worth \$11bn composed of \$9bn compensation for TLS infrastructure, the value of decommissioning its Copper and HFC network and migrating its Fixed traffic onto the NBN and \$2bn for Telstra's Universal Service Obligations and to assist in retraining and redeployment of Telstra staff. JPM stated that if this HoA progresses to a definitive agreement, the relevant legislation is passed, ACCC approval is given, then Telstra will take the deal to shareholders in 1HCY11. Based on the deal in this non-binding HoA, JPM values Telstra at \$3.49. They have increased the probability of this scenario to 90% with the other possibilities a better deal for TLS (valuation \$4.12) or a worst case scenario which leads to functional separation (valuation \$2.58).

Research

David Jones Limited (\$4.49) – Following the resignation of CEO Mark McInnes and the appointment of Paul Zahra as CEO effectively immediately, GSJB Were has retained a BUY, UBS has maintained a HOLD whilst Credit Suisse has **downgraded** to a SELL. GSJB Were has a price target of \$6.23.

Alesco Corporation Limited (\$2.77) – With ALS updating their full year guidance, UBS has retained a BUY whilst GSJB Were, Macquarie and JP Morgan have maintained a HOLD. UBS has a price target of \$3.80.

MApp Group (\$2.96) – Following the release of MAP's May traffic figures displaying a solid recovery from the volcanic ash related weakness in April, GSJB Were, Macquarie, JP Morgan and RBS have all retained a BUY. RBS has a price target of \$3.50.