



# Martin Bros Monitor

www.martinbros.com.au

September Quarter 2008 Edition

Paul & Jarrod Martin are Authorised Representatives (259367 & 259249) of ABN AMRO Morgans Ltd.



## Look Who's Back!

As most of you will know, Rochelle went on maternity leave last July and gave birth to Joshua in October 2007.

It is with great pleasure we can announce that Rochelle has returned to work, initially for two days per week.

Rochelle can be contacted on her new direct line 9947 4139. Rochelle's email remains the same; rgordon@abnamromorgans.com.au

## Stock Review - (WH) Soul Pattinson

Soul Pattinson (SOL) is the oldest listed stock on the Australian sharemarket. SOL is an equity investor with interests in a diverse range of businesses, all separately managed and many listed on the stockmarket themselves.

SOL's biggest equity investment is a 49.47% interest in Brickworks (BKW). BKW also has a large cross ownership in SOL. The reason for this cross ownership is predominantly as a protection against a hostile takeover.

SOL also has a 61.07% interest in New Hope Coal (NHC). NHC was originally wholly owned by SOL but was demerged and separately listed from the group in 2003, primarily to unlock value.

SOL also has (smaller) interests in Australian Pharmaceutical Industries, SP Telemedia, Clover Corporation, Brickworks Investment Company, Souls Private Equity, Huntley Investments and KH Foods.

NHC has recently sold one of its prospective coal mine sites in Queensland for \$2.45 billion in cash to a BHP Billiton / Mitsubishi Alliance. NHC currently has a market capitalisation of approx. \$3.7 billion. NHC will be left with its current operating coal mines and other exploration rights.

Some of the sale proceeds are expected to be retained for future growth options, but a large portion is likely to be returned to shareholders via a special dividend over time. NHC has a history of returning capital with its surplus cash, usually via a special dividend. As SOL owns 61.07% of NHC, any special dividend would flow through to SOL and most likely be passed on to SOL shareholders.

SOL is currently trading at \$10.60 and has traded as low as \$6.70 in the past six months. It has an all time high of \$11.50. ABN AMRO Morgans values SOL's at \$15.11 with a \$13.60 price target.

## Normal Markets - Part 3



Since the last Martin Bros Monitor was published in June, the economy has shown dramatic signs of slowing, albeit from a very high level of activity over the past few years.

The Reserve Bank of Australia (RBA) has now begun a monetary easing cycle. This demonstrates that the RBA believes their seven year tightening (increasing interest rates) cycle has now sufficiently subdued consumer spending and personal debt demand to the point that downside risks (chance of going into a recession) outweigh the risk of inflation remaining above their target range of 2-3%.

Falling interest rates usually translate into a positive for equity markets as the cost of capital reduces, therefore reducing corporate interest costs and increasing company profits. Falling interest rates also make equities become more attractive from a yield perspective. If an investor holds money in cash and the income (interest) on this cash is falling, dividend income that is being maintained and even growing, will become a more attractive option. This will lead to more cash flowing into the equity markets, subsequently driving up share prices.

***“downside risks outweigh the risk of inflation remaining above their target range”***

This may be a simplistic overview as many different factors come into force in shaping investors' views as to whether the present represents an attractive time to buy equities. Falling interest rates typically mean the economy is slowing, which, on face value would be a negative for equities as falling growth translates into slower profit growth for companies. However, equity markets tend to lead the actual economy by about nine months. Therefore, the equity markets normally rebound well before there is proof the economy has ceased contracting.

The below table shows the Australian sharemarket performance post the first interest rate cut of an easing cycle since 1982.

First Rate Cut	+ 3 months	+ 6 months	+ 12 months
May 1982	-7.6	1.0	19.8
Jan 1986	12.7	17.6	45.7
Jan 1990	-10.9	-3.8	-23.9
July 1996	6.5	11.1	23.4
Feb 2001	0.5	2.6	3.8
<b>Average</b>	<b>0.2</b>	<b>5.7</b>	<b>13.8</b>

Apart from 1990, the last five times an interest rate easing cycle began, the Australian sharemarket had positive performance over the next twelve months. Although 1990 resulted in negative 23.9% performance post the first rate cut, the twelve months before the January rate cut saw the All Ordinaries increase by 12.5%. Quite a different twelve months preceding the January 1990 rate cut to the twelve months we have just experienced.

One headwind that will potentially hold the Australian sharemarket back is the unwinding of the commodities boom. The weak \$US and collapse in world financial markets saw every fund manager in town jump on the long resources / short \$US play since January. Now, as the \$US has strengthened and the world wakes up to what slowing global growth will do to resources demand, commodity prices (and the oil price) have begun to readjust. Refer previous MBM's. Not even China will save the commodities boom now. We are just starting to see proof of China's economy slowing. Why? Because global demand is slowing and this naturally flows through to China as they are a huge exporter to the Western world.



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## S&P ASX 200 Forecasts by Market Participants



### Equity Market Forecasts

Whilst Australian sharemarket forecasts will constantly change as new economic data comes to light, we felt you may be interested in a collective view of forecasts for the S&P ASX 200 over the next six months (as at start of August). See below:

Institution	S&P/ASX 200 (pts) 6 months
ABN AMRO Morgans	5500
AMP Capital *	6000
Ausbil Dexia *	5500
BT Financial Group *	5300
Commonwealth Bank *	5800
Goldman Sachs JBWere *	5600
JP Morgan *	5432
Lehman Brothers Australia *	5500
Macquarie Bank *	5387
Merrill Lynch	6300
National Australia Bank *	4825
UBS	5550
Westpac *	5100
<b>Median</b>	<b>5523</b>

\* Reproduced from the Australian Financial Review, 5/8/08

All except NAB are reasonably confident on the near term prospects for a gradual recovery in our sharemarket. As mentioned on the preceding page, if the resource bubble does burst, this will have a negative effect on the ASX 200. Therefore, the performance of financial and industrial stocks would have to be significant if the ASX 200 is to move higher in the face of falling resource stocks. There are two other possible scenario's that could see the market move higher. One, all sectors gradually move up, and two, resources move higher and financials and industrial stocks do not. We would expect the latter scenario to be very unlikely given the relative performance of financial and industrial stocks over the past six to nine months, many of which now represent very good long term value. In addition, there is no doubt the global economy is slowing and this has to affect the demand for resources.

## Some George Soros Quotes (American Philanthropist and Stock Investor)

“Stock market bubbles don’t grow out of thin air. They have a solid basis in reality, but that reality is distorted.”

“The worse a situation becomes the less it takes to turn it around, the bigger the upside.”

“The markets are always on the side of exuberance or fear. It’s fear and greed. Right now fear has the better of it.”

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