

## Companies say next year to be tough

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Sunday, August 15, 2010

Investors have reassessed their rosy earnings expectations as the companies that have reported so far warn that the next year is likely to be tough. Companies including Commonwealth Bank, Telstra, Rio Tinto and Coca-Cola Amatil have already reported earnings, saying the near term will be difficult as consumers remain exceptionally cautious and the global economy remains volatile. That outlook, together with reports from the US, Europe and China that the global economic recovery is stuttering, prompted a sell-off in Australian shares this week, with the All Ordinaries Index losing 2.3 per cent. With two weeks of earnings reports to go, investors may need to be prepared for a volatile time. Australian Foundational Investment Company (AFIC) managing director Ross Barker said the outlook statements so far had been a “bit of a shock” for many investors. “The market had priced in a continuing recovery, and the outlook comments don’t look to be that optimistic,” said Mr Barker, who helps manage about \$5 billion in equities. “This has happened at a time when the US recovery is looking more in doubt.” Mr Barker said many analysts had been pricing in between 12 and 15 per cent earnings growth for financial 2011. “We’ve always felt earnings optimism for 2011 was a bit too high,” Mr Barker said. The All Ords rose 1.3 per cent on Friday to close at 4,480.9. That was down from last Friday’s close of 4,586.7 and after reaching a one-month low 4,422.4 on Thursday. Telstra was the biggest drag on the index this week. The telecommunications provider dropped 9.5 per cent on Thursday when it reported that earnings were likely to fall this financial year. Telstra shares slumped 11.8 per cent over the week. “Telstra was a shock,” Tyndall Investment Management head of equities Robert Van Munster said. Mr Van Munster, who helps manage about \$4.3 billion, said Telstra wasn’t the only one to disappoint some investors, with Commonwealth Bank also showing contracting margins and a cautious outlook. “It’s not the time for companies to put out hairy-chested forecasts,” he said. Commonwealth Bank, Australia’s largest lender, said lower corporate and consumer confidence had hurt the underlying momentum of its business. “It is appropriate to maintain a degree of caution,” Commonwealth Bank chief executive Ralph Norris said. Other companies that were dropped by investors include the world’s biggest share registry Computershare, which tumbled 10.6 per cent to a 13-month low on Wednesday after saying that earnings per share would probably fall this financial year. James Hardie fell 7.5 per cent to a 12-month low on Thursday after the building materials maker said the recovery in the US market, where it makes most of its sales, remained disappointing and fragile. US housing starts for the June quarter were 142,000, up from last year’s figure of 124,000, but still 74 per cent down from their 2005 peak. Combined with that, the number of Americans filing new claims for jobless benefits jumped unexpectedly last week to the highest level in six months. China’s rapid rebound from the global recession also looks to be cooling, with factory production, retail sales and new investment all slowing. “We are potentially heading into a lower growth world,” Fidelity International head of Australian equities Paul Taylor said. But, it’s “a time companies can really stand up and be counted.”

Mr Taylor, who manages \$5 billion in Australian equities, said those companies that could demonstrate good revenue, or “top line” growth, would be looked on favourably by investors. Rio Tinto and Coca-Cola Amatil (CCA) both fell into that category, Mr Taylor said. Rio Tinto reported last week that first half underlying profit more than doubled to \$US5.78 billion (\$A6.45 billion) and net debt was reduced by more than two-thirds to \$US12 billion. Coca-Cola Amatil (CCA) increased first half profit by 12 per cent to a record \$213 million and revenue by 4 per cent to \$2.13 billion. Still, both Rio’s CEO Tom Albanese and CCA boss Terry Davis expressed caution about the period ahead. “It would be a pretty brave company not to take a cautious view of the world,” Fidelity’s Mr Taylor said. Cautious outlooks are likely to be the norm over the next two weeks of the profit season. Leighton Holdings, the country’s biggest construction company, starts the reporting week on Monday, followed by OneSteel, Westfield, Woodside and Wesfarmers as the week wears on. Rubber products maker Ansell kicks off the week after next, followed by Origin Energy, Foster’s Group, BHP Billiton, AGL Energy and Woolworths. While caution is likely to reign, fund managers point out that now is a good buying opportunity, because even good companies are looking cheap. “You can pick up high-quality companies at good prices,” Mr Taylor said.

“We look at it as a great opportunity.”