



The Hudson Report



This weeks Hudson Report is brought to you by **Andrew MacDonald** - Hudson Institute Financial Adviser

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The majority of private wealth created in Australian history has come from two sources, real estate/property investment, and owning stakes in businesses or companies (ie: shares). Australians tend to have a good understanding of property because they often have experience owning their own house or investment properties.

However, many find the sharemarket confusing and intimidating, and in this week's Hudson Report we will explain simply, what shares are, and why over time they have proven to be one of the most rewarding investments.

If you would like more information about any of the subjects in this week's Hudson Report, [make an appointment](#) online or speak with your Hudson Adviser on (free call) 1800 804 296.

Andrew MacDonald



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Share's, also known as equities, are a part ownership in the profits that a company makes. Over the long term, if a company makes higher profits, its share price will go up, if it makes less profit its price will go down. In the short term, there is all sorts of speculation by the market participants as to what will be the earnings of that company in the future, and this is why the price of the shares fluctuate all the time. In reality, this is just noise, the reason why shares in good solid companies increase over the long-term, is that economic productivity increases and company profits increase with it, leading to higher share prices. Why does our economic productivity increase over time and increase the value of company shares with it? The two main reasons are technological improvements and population growth.

In the case of technology improvements, just think back to how business was done 100 years ago. Most people didn't have a car. There were no computers, no other communications technology, and industrial machinery was primitive compared to today. Over a hundred years of technological improvements, we have been able to produce more with less, and in a shorter time. As a result, companies have been able to produce more of their merchandise for consumers. This has increased their earnings and as a result, their share prices. No doubt in another hundred years, they will look back on us and think our methods were primitive too. We look back in disbelief that people used Asbestos in housing, and I have little doubt our great, great grandchildren will look back at us and say, "Why did they burn all that polluting oil and coal



when the sun can give you free, clean and never ending energy?". Technology has allowed business to make more produce for consumers.

Population growth, the second big driver of economic productivity growth is that there are more consumers for businesses to sell their merchandise to. Australia's population in 1909 was around 4.2 million. Today it is over 22 million, and we are relatively more affluent than our forebears. No doubt you've seen the latest Treasury forecasts being reported in every major newspaper, predicting **Australia's population will swell to 35 million by 2049!** This represents a 62% increase in the population. These new 13 million Australians will need to eat, be clothed and housed. They will buy cars, mobile phones, computers, lawn mowers and every other product we buy today. As a result, Australian companies will make higher profits than they do now and their share prices will rise. Furthermore, there will be more Australians in the work force getting their 9% Super guarantee. Currently almost 50% of that 9% finds its way into the Australian sharemarket.

We also have the two largest populations in the world, India and China, going through a multi-decade industrialisation, where by their enormous populations will move from rural areas to major urban areas, and become more affluent in the process. They need enormous amounts of natural resources to build these new cities, and provide these people with jobs, and we just happen to be in their geographic region, and have a lot of the resources they need. So there is very good reasons to believe Australian companies will have higher earnings in 5, 10, 20, 30 years, than they do today, and as mentioned earlier, over the long term, share market prices move with these company earnings.

Q. How do you take advantage of the long term trend in share prices, and which shares should you buy?

The answer to this question comes down to whether you think you can pick the companies whose earnings will outperform the general market, or whether you are happy to accept that the general market will rise over the long term, and you will accept the market return and not risk choosing the wrong companies. This is the difference between an active investor and a passive investor. An active investor thinks they can consistently pick the companies that will outperform the market, whilst a passive investor doesn't think they can consistently pick the outperforming companies, so accepts the market return. As to my own opinion on this topic, I would like to refer you to an answer the world's greatest investor, Warren Buffett, gave in an article entitled, "**What Warren Thinks**" published by Forbes Magazine on April 14, 2008.

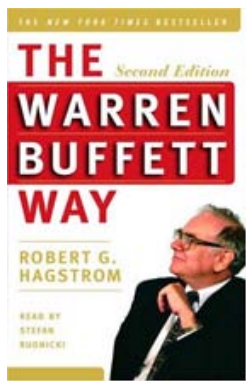
Q. What advice would you give to someone who is not a professional investor, and where should they put their money?

Buffett: Well, if they're not going to be an active investor - and very few should try to do that- then they should just stay with index funds. Any low-cost index fund. And they should buy it over time. They're not going to be able to pick the right price and the right time. What they want to do is avoid the wrong price and wrong stock. You just make sure you own a piece of American business, and you don't buy all at one time. Productivity will increase and stocks will increase with it...

"Be greedy when others are fearful, and fearful when others are greedy, but don't think you can outsmart the market".

If a cross section of American industry is going to do well over time, then why try and pick the little beauties and think you can do better? Very few people should be active investors.

A Compromise - If you are interested in being an active investor or using an active fund manager to try and outperform the general market, then you can use a combination of active and passive investing to achieve this. You can gain the benefits of passive index, investing as described by Warren Buffet above, and also use some of your funds to try and "pick the winners". This investment philosophy, which many Hudson members will be familiar with, is called the Core & Satellite approach. Under this strategy, you invest the majority of your



money in index funds to get a cheap exposure to the general market, and then use the rest of your funds to either invest in direct shares yourself or use an active fund manager.

The Timing Issue - Many of you would have heard the cliché that is often said by fund managers that “it's time in the market, not timing of the market” that counts when investing. Personally I think that's an incomplete definition. Try telling someone who invested \$100,000 in November 2007, and then watched their investment lose 55% of its value, that timing doesn't matter. Of course timing matters, the real issue is that timing the markets correctly and consistently is difficult, if not impossible, over the long term, and being out of the market when the big moves occur can be costly.

A recent study by the index fund manager Vanguard, showed that if you invested \$10,000 in the Australian sharemarket in June 1970, and missed the single best monthly return of 25.5% in October 1974, it would have cost you \$92,109, and reduced your portfolio to \$361,056 at 30 June 2009. If you missed the two best months, you would have cost yourself \$153,215. Furthermore, these best monthly returns occurred in the midst of the 1974-75 recession that was preceded by the OPEC oil crisis. No doubt the headlines at the time were filled with doom and gloom, and many people would have panicked and taken their money out of the market, and missed what would turn out to be the best monthly returns for the next 50 years. History has again repeated, and people who panicked and sold out of their share portfolios around March this year have missed out on a 50% sharemarket rally.

Another famous quote from old Warren Buffet is "I can't predict the short-term movements of the stock market," he writes. "I haven't the faintest idea as to whether stocks will be higher or lower a month -- or a year -- from now." I personally believe very few people can accurately predict on a consistent basis, where stock market prices will be tomorrow, in a months time or a years time. But we do know from over a hundred years of investment history in this country, and overseas, that those who hold shares in companies, are effectively holding a stake in the economic progress of that country, and they will be rewarded over the long term.

You can never guarantee you're going to get the timing of your investment correct all the time. The best way to reduce the risk of investing at a bad time, or increase your chances of investing at a good time, is to invest on a regular basis and be a bit more aggressive in periods after large falls on the sharemarket. Because, as we've seen over the past 100 years, although some times it can take years for it to happen, markets have always exceeded their previous highs.

by Andrew MacDonald | Other Sources | vanguard.com | Forbes Magazine



Hudson focus



When buying a property at auction there are some important finance requirements that you need to have in place before you bid. If you are the successful bidder at an auction you will be required to sign the contract of sale and pay a deposit on the spot, and the contract is unconditional. This means you have to have your finance in place before the auction. It is therefore important that you get your borrowing capacity in place, and should ideally have your finance approved before the auction. You should not allow yourself to exceed your finance approval in the heat of the moment.

You should also have thoroughly researched the property you are bidding on. You should check what similar properties in the same or similar suburbs have sold for in the recent past to get a value guide. Alternatively, you can pay and get an independent valuation before the auction, to assist you in finding a price ceiling that you are willing to pay. Its important to have in place a solid price ceiling you are not prepared to breach, to avoid getting emotionally caught up in a bidding war on the day of the auction, and overpaying or breaching your finance limits.

You should also be aware that legislation came into effect on 21 August 2006, that requires that all people bidding at an auction provide their names, addresses and proof of identity to the Auctioneer prior to the auction in order for their bids to be registered.

In summary, if you are buying property at auction you should:

- Have completed a borrowing capacity test
- Have your deposit and finance in place
- If required, have completed a building and pest inspection before the auction day as the sale will be unconditional should your bid be successful
- Research the market you are buying into to get a price guide
- Set a price ceiling you are not willing to breach and not get caught up in an emotional bidding war on the auction day



The Hudson Institute Finance team can assist you in running a test or your borrowing capacity given your income and asset position. They can also establish the finance by helping you chose the best lender, best rate and product from a menu of options. Contact the Hudson Institute on 1800 804 296 for details or [make an online enquiry](#).

Source| www.reiq.com.au

behind the investment news...



It has become well documented that Australia is suffering from an acute shortage of housing at the same time as the federal government has employed a long term strategy of high levels of immigration to create, as PM Rudd called it a "big Australia". This scenario is putting upward pressure on house prices as evidenced by the recent house price growth data released by the Australian Bureau of Statistics (ABS). In the year from September 2008 to September 2009, the ABS Detached House Price Index rose by 6.2%. This is an extraordinary result given the turmoil international property markets have experienced.

This has led to the affordability for first homebuyers issue raising its head again and Federal Housing Minister Tanya Plibersek, is trying to pass the blame onto state and local governments. **Plibersek has warned that state governments and local councils risk pricing first-home buyers out of the market by milking the property industry for too much tax.**

"We are not building enough houses every single year, and part of the problem is the very high cost of a serviced block," Ms Plibersek said, noting that states and councils were placing heavy levies on developers in an effort to meet the cost of providing community infrastructure.

"It might be that the blocks are available, but builders aren't building on them because they don't think they'll make enough of a return on the money they are spending."

Rising interest rates and more cautious bank lending is also making it harder for developers to bring housing supply onto the market in a way that is profitable for them. Harry Triguboff, Chairman and Managing Director of *Meriton Apartments* is the largest owner and builder of apartments in Sydney, and a major force in Queensland claims that if, "the Reserve Bank insists on raising interest rates in the hope of suppressing prices, they must understand that they will in turn, suppress construction... all the evidence on rents and prices points to undersupply for the foreseeable

future”.

Australia is simultaneously increasing its population at near record levels, greatly increasing the demand for housing, and at the same time, high government taxes, rising interest rates and the cautious attitudes of banks to financing property developers is choking supply. **It looks like the housing shortage issue will be with us for the foreseeable future.**

Source| www.news.com.au | www.theaustralian.com.au



from the floor...



Berkshire Hathaway, the company controlled by American super investor and **the world's second richest man**, Warren Buffett, has initiated a huge takeover bid of Burlington Northern Santa Fe (BNSF) railway company. Buffett said the acquisition of 77.4 per cent of BNSF shares it does not already own, would be Berkshire's biggest acquisition and represents "an all-in wager on the economic future of the United States".

In total, Berkshire Hathaway will invest US\$26Billion in its takeover of the BNSF. Buffett believes the doom and gloom surrounding the US economy is overstated, and that the US economy will recover, and that the railway company will benefit from this recovery. He had previously written in the New York Times amidst the panic selling that followed the collapse of investment bank Lehman Brothers, that, "Fears regarding the long-term prosperity of the nation's many sound companies makes no sense".

BNSF is the No.1 U.S. railroad by revenue, operates in the U.S. West and Midwest. It said in September that freight volumes were recovering and it was encouraged by an improvement in consumer-related markets.

SOURCE | www.theaustralian.com.au | www.reuters.com



Share market update for the week ending Wednesday 04/11/2009

It was a mixed week on the major world share markets. The US and UK markets were up slightly, but the major Asian markets, including Australia's All Ordinaries index, were down between 2.5% - 3.0%. During the week, both the Reserve Bank of Australia and the US Federal Reserve met to discuss the interest rate levels for their respective economies. The RBA decided to again raise rates by 0.25% to take the cash rate to 3.5%. The reason given by RBA governor Glenn Stevens for the rate rise was that, "the risk of serious economic contraction in Australia now having passed, the Board's view is that it is prudent to lessen gradually the degree of monetary stimulus that was put in place when the outlook appeared to be much weaker." This had little impact on the Australian stock market as the market participants were expecting the 0.25% rate rise.

In contrast, the US Federal Reserve left US rates at near 0%. The U.S. Federal Reserve on Wednesday expressed growing confidence that an economic recovery was building, even as it stuck to its commitment to keep borrowing costs near zero for "an extended period." The difference in the rate decisions of the Australian and US reserve banks reflects the relative strength that the Australian economy has shown.

On Wednesday in Australia, the sharemarket had its first positive day of the week, with the All Ordinaries index rising 7.6 points to 4,547.60. This was mainly on the back of price rises for the big 4 banks. This was mainly due to comments by both ANZ and NAB suggesting the bad debt cycle may have peaked for Australian lenders. The big diversified miners of BHP & Rio Tinto were also up 20c & 62c respectively. Gold stocks Newscrest Mining, Lihir Gold and Sino Gold were also all up as gold hit a record high near US\$1090.

Source| The Australian Financial Review | www.reuters.com

Index	Close at 04/11/09
All Ordinaries (Aus)	Closed at 4,547.60 down 2.97% for week
Dow Jones (US):	Closed at 9,802 up 0.39% for the week
Nikkei 225 (Japan):	Closed at 9,844 down 2.77% for the week
Hang Seng (Hong Kong):	Closed at 21,615 down 2.56% for week
S&P 500 (US):	Closed at 1,047 up 0.38% for the week
FTSE 100 (UK):	Closed at 5,108 up 0.55% for the week
Australian Dollar	Trading at .907c US

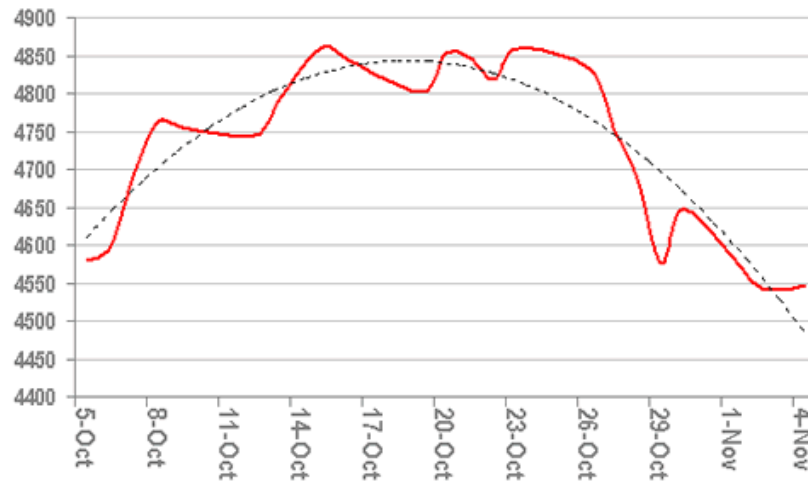
All Ords Price History Nov 84 - Nov 09 (monthly)



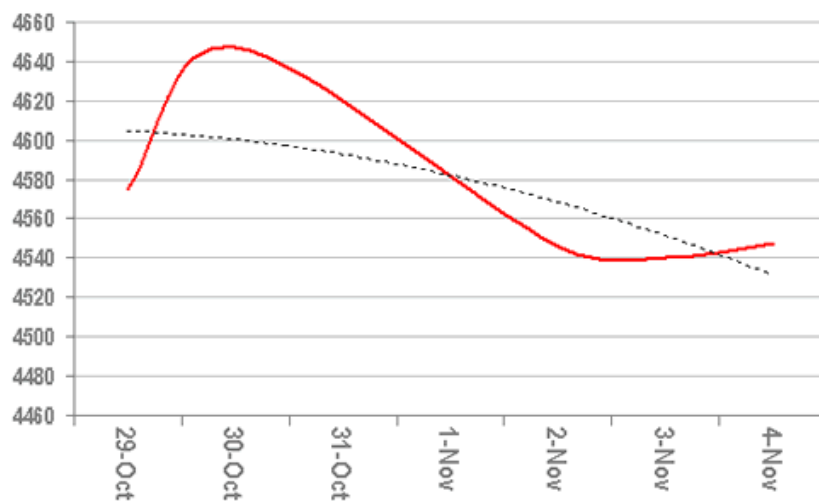
All Ords Price History Nov 08 - Nov 09 (weekly)



All Ords Price History Oct - Nov 09 (daily)



All Ords Price History Oct 29 - Nov 04 (daily)



SOURCE | The Australian Financial Review | www.reuters.com | Graph data: Finance.yahoo.com.au

Whisper of the Week...

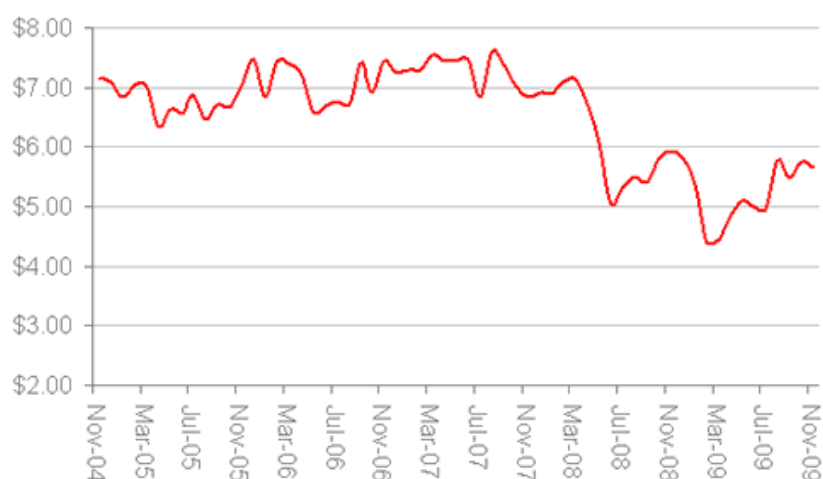
AMCOR (AMC)

Amcor is one of the world's top 3 global packaging companies, based on market capitalisation, sales and profits. Amcor is a leading global packaging manufacturer offering a broad range of plastic, fibre, metal and glass packaging products, along with packaging-related services. It operates in 34 countries, employees 21,000 people worldwide and last year had A\$9.5 Billion in sales. Amcor's key revenue driver is still consumer spending in food, beverages and healthcare. Amcor offers good upside on solid cash flows with a major restructure underway.

Amcor declared a final year dividend of 17c/share for the year ending 30 June 2009, representing a dividend yield of 6%, although this was only partly franked. Amcor's share price had a turbulent 2008 as amidst the panic of late 2008 investors fled its heavily cyclical stock. However cyclical stocks tend to outperform the general market during economic recoveries and Amcor has good prospects of benefiting from this.

Current P/E Ratio	14.30	Long-term buy under \$5.55
Dividend cents/share	17c	
Dividend Yield	6%	
52 week high	\$6.08	
52 week low	\$3.50	

AMCOR 5yr Price History Nov 04 - Nov 09 (monthly)



Source | www.amcor.com | www.etrade.com.au | Graph Stats: finance.yahoo.com.au

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