Eastern promise

BUILDING PRODUCTS

CONSTRUCTION materials supplier Adelaide Brighton expects improved sales in several of its key products, based largely on demand from east coast markets.

Chief executive Martin Brydon told the company's annual meeting that it expects this year's volumes of cement and clinker sales to be similar or slightly less than last year.

Cement sales accounted for 47 per cent of Adelaide Brighton's revenue last year.

But the company expects significant growth in sales of pre-mixed concrete and aggregate in 2016, due to stronger east coast markets.

Sales of concrete products are also expected to rise.

Adelaide Brighton made a profit of $208 million last year.

Its shares closed up 4.2 per cent at $5.65.

RELIEF FOR GREECE

WORLD ECONOMY

GREECE has won an essential batch of bailout funds from international creditors following an exhaustive round of talks and can look forward to debt relief in the future.

After finance ministers from the 19 eurozone members approved Greece's latest reform efforts, they opted yesterday to disburse €10.3 billion ($15.9 billion) to see Athens through the next few months. Greece stands to receive €7.5 billion by the middle of next month, with other disbursements coming after the European summer.

The breakthrough came after 11 hours of tortuous talks. "This opens the way for a return of confidence that is so essential for lasting economic recovery in Greece," EU commissioner Pierre Moscovici said.

People power

Skilled fusion propels labour group

LILLY VITOROVICH
RECRUITMENT

INVESTORS have made a beeline for shares in Programmed Maintenance Services after the labour hire and maintenance group reported solid progress in its integration of Skilled Group on top of a rosy earnings outlook.

Managing director Chris Sutherland said the integration of Skilled, which was acquired for $652 million in October, was proceeding ahead of plan, with annual cost savings of more than $30 million already delivered.

He said the separate management teams had bonded, with rebranding complete and Skilled's core IT systems to be fully integrated within the coming year.

The company says earnings before interest, tax, amortisation and non-trading items should jump sharply to between $100 million and $110 million in the year to March 2017, thanks to the impact of Melbourne-based Skilled.

That compares to EBITA of $65.5 million in fiscal 2016.

The acquisition of Skilled has increased the company's scale and diversification, opening new opportunities across the combined customer base, Mr Sutherland said.

"I often say that our business is very much like the Australian economy, we grow in the parts of the economy that is growing and we shrink a bit in the parts that aren't," he said.

"Customers in markets such as retailing, tourism, transport and manufacturing are hiring people and spending on their assets again, and there are growing opportunities in the education, health and aged care sectors.

"Demand is growing for staff and maintenance services across these sectors, which represent more than two-thirds of group revenue."

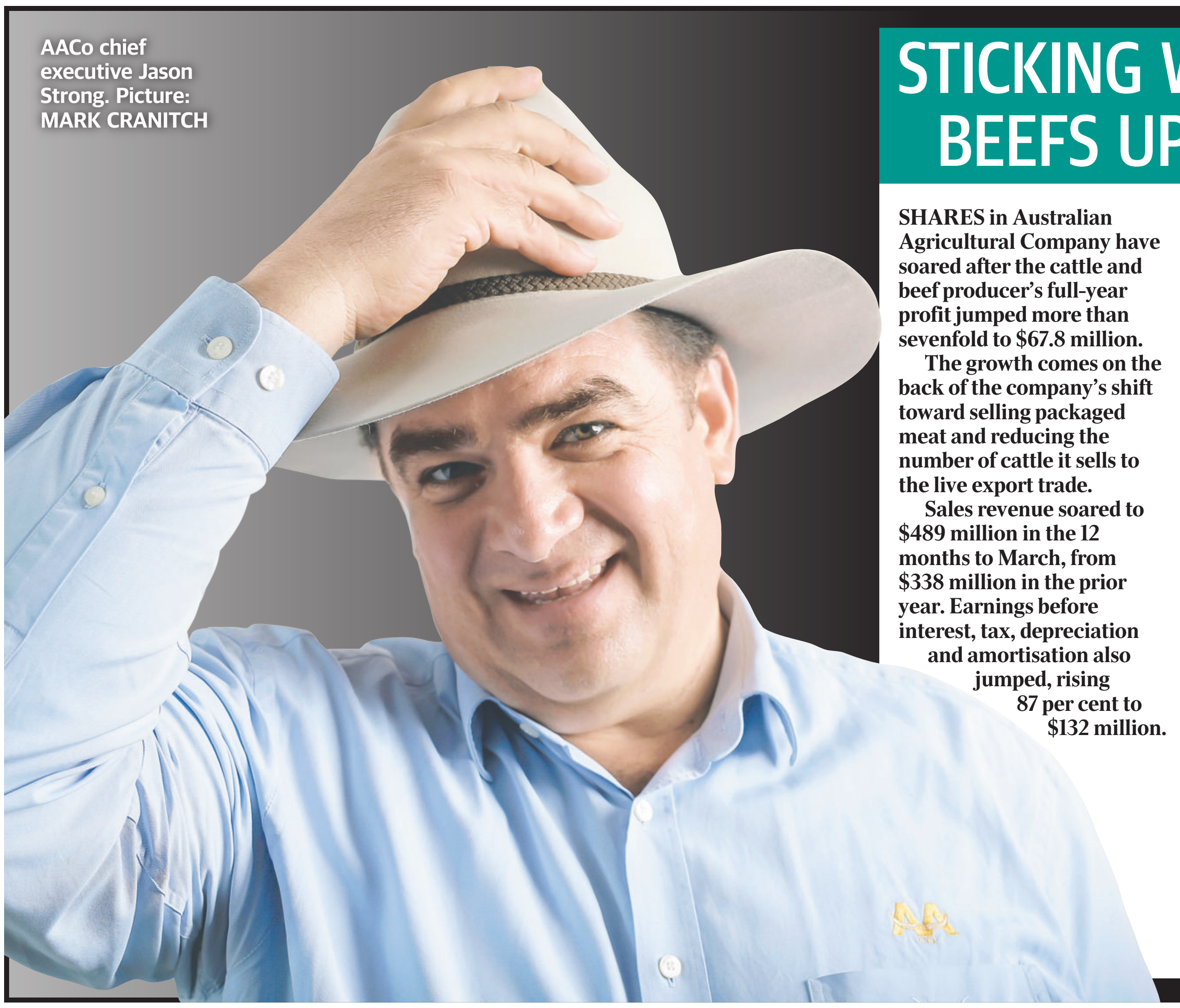
The Skilled purchase had also helped the company deliver a 55 per cent rise in annual revenue to $2.22 billion.

"It will take a number of years for the benefits of our increased size, scale and efficiency to be fully realised as we integrate business systems and seek growth across our expanded network," Mr Sutherland said.

Programmed shares gained 15c, or 10 per cent, to $1.615.

However the company made an annual net loss of $98 million due a massive write-down on its marine division, related to the impact of a steep drop in oil and gas prices on demand.

AAP



AACo chief executive Jason Strong. Picture: MARK CRANITCH

STICKING WITH HERD BEEFS UP PROFITS

AGRIBUSINESS

SHARES in Australian Agricultural Company have soared after the cattle and beef producer's full-year profit jumped more than sevenfold to $67.8 million.

The growth comes on the back of the company's shift toward selling packaged meat and reducing the number of cattle it sells to the live export trade.

Sales revenue soared to $489 million in the 12 months to March, from $338 million in the prior year. Earnings before interest, tax, depreciation and amortisation also jumped, rising 87 per cent to $132 million.

"Our strategic decision to own cattle right through our supply chain has increased revenue and margin," chief executive Jason Strong said.

"We are not done. This result just provides a solid platform for us to grow."

During the past three years, AACo has transformed from a cattle producer into an integrated beef producer and exporter, after opening a large abattoir in Darwin and focusing on extracting the maximum value out of its own herd.

Beef sales accounted for 88 per cent of revenue in 2015-16, up from 61 per cent two years ago. The company said it received higher live cattle prices, but this was offset by lower volumes sold on the market.

The strong result was welcomed, AACo shares lifting 12.4 per cent, to $1.68.

Cautionary tale of a Chinese bank and the use of WMPs

THE SHORT CUT
with ANDREW MACKEN

THERE is a bank called China Minsheng.

Minsheng used to be an investor's dream: growing earnings consistently above 30 per cent a year, benefiting from the boom that was the Chinese economy.

But times have become tougher for Minsheng of late: the bank recently printed its first year-on-year decline in pre-tax profit since the global financial crisis.

You see, Minsheng is still growing its loan book at a steady rate of 13 per cent a year. But lending in China is not what it used to be.

Net interest margins are being squeezed from both directions: interest rates on new loans are not what they were now that too much credit chases too few economic opportunities; and deposit rates have been deregulated meaning Chinese banks now need to compete with each other for deposits.

Furthermore, Minsheng is being forced to rapidly book impairment allowances (which reduce profit) for existing loans that are deteriorating in credit quality.

The proportion of the total loan book that is now classified as poor quality (impaired and "special mention") has accelerated sharply to over 5 per cent, from around 3 per cent last year.

And Minsheng is not booking enough allowances in its income statement to meet these poor loans — suggesting the bank's earnings and book value are potentially overstated.

So, as the profitability of lending deteriorated, Minsheng needed a new game. Enter fees and commissions from "asset management".

Not a new trick at all — indeed many banks in the world are favouring these sorts of earnings streams as they are less capital intensive and, therefore, carry higher returns on equity.

This strategy has plugged the gap created by the falling profitability of lending. But only just.

And on the recent trajectory, growth in fee and commission income will unlikely be sufficient to offset the declines from lending.

You might ask: from where did these fee and commission earnings fortuitously appear?

Well, Minsheng, along with many peers, have got into the wealth management product origination business. WMPs are short-term (one to three months), high-yielding pieces of paper that have become popular with Chinese investors in place of deposits.

The WMPs are typically backed by very long-term assets, including property and infrastructure projects. While WMPs might sound risky, investors have historically been less concerned if they have been sponsored by a "reputable" bank.

The reason is that investors believe they are granted an implicit guarantee by the bank on the return of their capital. This idea remains untested, though we can get an insight into the credibility of any potential guarantee by looking at the size of the outstanding issues relative to Minsheng's book value of equity.

Based on the company's most recent filings, the combination of WMP trust products sponsored by Minsheng and others (where Minsheng retains an interest), combined with other off-balance-sheet guarantees, equates to nearly eight times book value.

Said another way, it would take only a 12.5 per cent loss on the underlying assets to completely wipe out Minsheng's equity, rendering it insolvent.

This is a large exposure which may limit the future growth of this business.

Minsheng may be looking at some tough times ahead.

As China slows, demand for loans will slow; net interest margins are already narrowing; credit quality of existing loans are deteriorating at an accelerated rate; and the sharp growth in fee and commission income that was being used to plug the gap may well be coming to an end. Earnings appear set to decline.

ANDREW MACKEN IS A PORTFOLIO MANAGER AT MONTGOMERY GLOBAL INVESTMENT MANAGEMENT