Trump fires new shot

World markets shudder at trade war escalation

HIDEYUKI SANO
WORLD ECONOMY

SHARE markets around the world have come under pressure and the Australian dollar has taken a hit after President Donald Trump ratcheted up the US's trade war with China.

Investors piled into assets regarded as safe havens yesterday after Mr Trump announced the US would slap a 10 per cent import tax on those Chinese imports which were not already subjected to tariffs.

From next month, a new tax will be levied on Chinese imports worth $US300 billion ($441.7 billion) a year.

Mr Trump's move breaks a truce struck in June and analysts said it could further disrupt global supply chains.

"After (the June) US-China summit meeting, people had expected there would be a lull for quite some time," said Masahiro Ichikawa, a senior strategist at asset manager Sumitomo Mitsui DS. "But now investors and companies will have to revise their scenarios."

Eswar Prasad, an economist at New York's Cornell University, said "the stage is now set for a further escalation of trade tensions".

The US had already imposed 25 per cent tariffs on Chinese imports worth $US250 billion a year, and Beijing retaliated by taxing $US110 billion of goods imported from America.

Consumers in the US are likely to feel the pain when the new tariffs take effect.

Mr Trump's earlier tariffs had been designed to minimise the impact on ordinary Americans by focusing on industrial goods. The new tariffs will hit a range of consumer products from mobile phones to silk scarfs. Hong Kong's Hang Seng index fell 2.4 per cent yesterday after Mr Trump's announcement via Twitter, while Japan's Nikkei 225 dropped 2.1 per cent. Britain's FTSE 100 was down almost 2 per cent in early trade last night.

Australia's benchmark ASX 200 index had a more modest fall, down 0.3 per cent.

But the Aussie dollar fell heavily against the greenback, dropping almost US0.7c in the minutes after the tweet.

Last night it was buying US67.89c. Were it not for the "flash crash" that briefly dragged the Aussie to US67.15c in January, that would have been the lowest level since early 2009.

China's state media denounced Mr Trump's announcement, and according to reports last night, China vowed to hit back with "necessary countermeasures".

REUTERS with AP

BEGA CUTS EARNINGS GUIDANCE

DAIRY

BEGA Cheese has cut its full-year earnings guidance as drought and the exit of dairy farmers produces competitive pressure that it says "has never been stronger".

The dairy processor yesterday said it increased its milk intake for the year to June by 41 per cent to a record 1.06 billion litres.

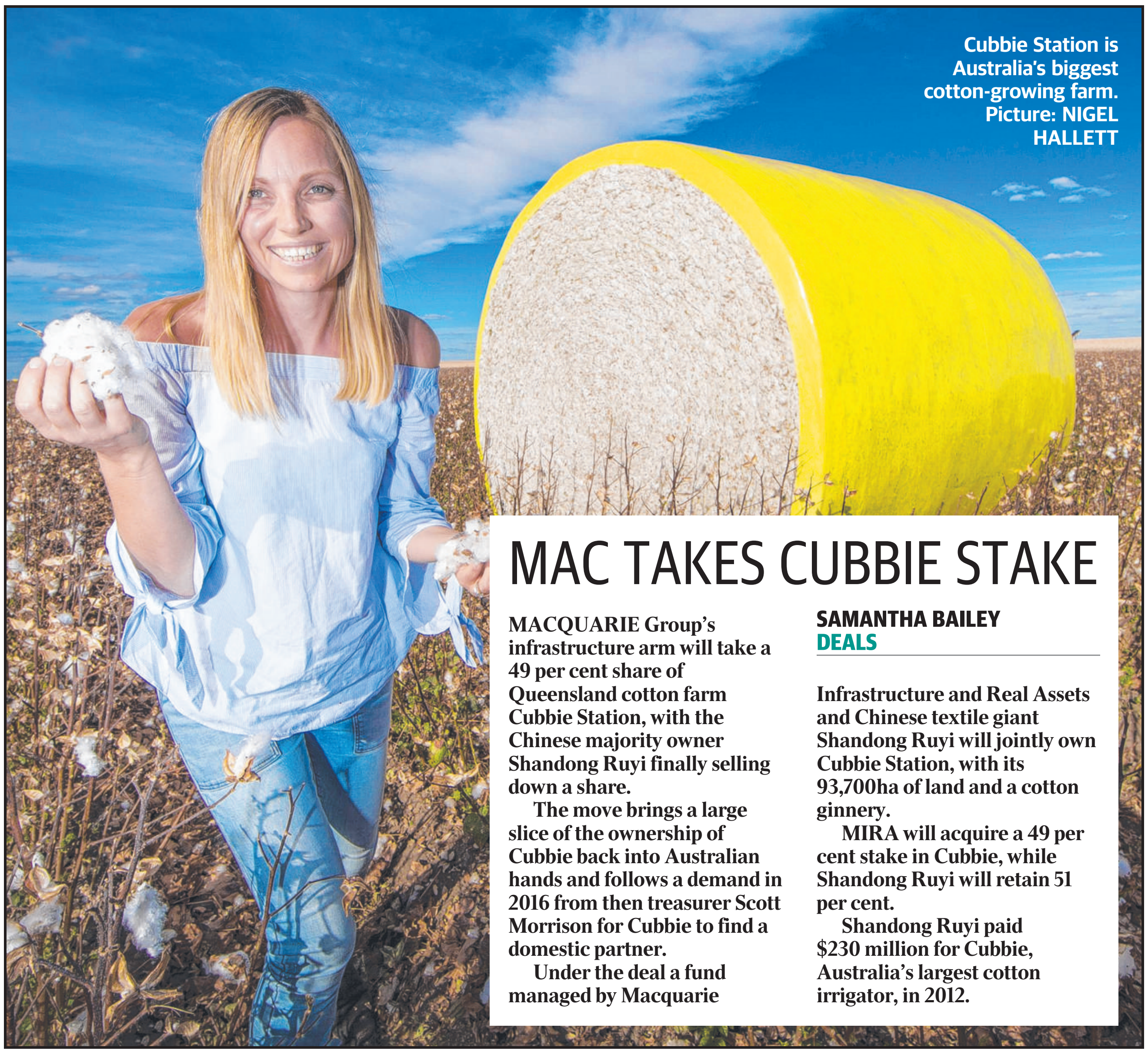
The rise came despite the nation's milk pool shrinking by 733 million litres.

Bega said it had incurred extra costs in the past financial year and more would come in 2019-20.

It now expects normalised earnings before interest, tax, amortisation and depreciation of between $113 million and $117 million, compared with an earlier target of $123 million to $130 million.

Bega has been diversifying beyond dairy, most notably through 2017's purchase of a suite of products that included Vegemite.

Its shares dropped 4.3 per cent yesterday to $4.24.



Cubbie Station is Australia's biggest cotton-growing farm. Picture: NIGEL HALLETT

MAC TAKES CUBBIE STAKE

SAMANTHA BAILEY
DEALS

MACQUARIE Group's infrastructure arm will take a 49 per cent share of Queensland cotton farm Cubbie Station, with the Chinese majority owner Shandong Ruyi finally selling down a share.

The move brings a large slice of the ownership of Cubbie back into Australian hands and follows a demand in 2016 from then treasurer Scott Morrison for Cubbie to find a domestic partner.

Under the deal a fund managed by Macquarie Infrastructure and Real Assets and Chinese textile giant Shandong Ruyi will jointly own Cubbie Station, with its 93,700ha of land and a cotton ginnery.

MIRA will acquire a 49 per cent stake in Cubbie, while Shandong Ruyi will retain 51 per cent.

Shandong Ruyi paid $230 million for Cubbie, Australia's largest cotton irrigator, in 2012.

Drought hammers GrainCorp

LOGISTICS

GRAINCORP shares have wilted after the company flagged an underlying full-year loss of up to $90 million thanks to continued drought and "significant" global grain market disruptions.

The bulk grains handler yesterday said its 2019 financial year results would be worse than previously announced, with the $40 million earnings hit predicted in April now blowing out to between $60 million and $70 million.

GrainCorp said new crop trading opportunities in the fourth quarter were no longer expected to materialise due to a reluctance by international market participants to consider new-season contracts.

"This is an extremely difficult year for GrainCorp due to the significant disruptions we've seen in global grain markets, compounded by the drought in eastern Australia," chairman Mark Palmquist said.

GrainCorp shares dropped 5.4 per cent yesterday to close at $8.13.

Super Retail a broad brand sporting plenty of resilience

THE SHORT CUT

ROGER MONTGOMERY

SUPER Retail Group is Australia's number one player in retailing aftermarket auto parts through its Supercheap Auto brand.

The company's auto division generates 38 per cent of sales and 48 per cent of group earnings before interest and tax.

Through its BCF brand, the company is also the number one retailer in leisure outdoor, and having acquired MacPac a year ago it has converted its Rays Outdoor stores to MacPac.

The outdoor division generates another 24 per cent of sales and 13 per cent of group EBIT.

Finally, Super Retail is the number one sporting goods retailer through its Rebel Sports brand, which generates 38 per cent of sales and 40 per cent of group EBIT.

Of course, when you are already number one, there is the ever-present threat of being toppled.

To counter the online threat Super Retail is investing heavily in its online offering.

Consequently, online sale growth has been double digits for all brands and Rebel Sport has had the highest at 40 per cent growth.

Most interesting is the fact that the company's EBIT margins are unchanged since 2008 for BCF, higher than in 2008 for Supercheap Auto and only slightly lower than 2010 for Rebel.

Invariably, the best defence of margins and against the ubiquitous online threat is to provide excellent service as well as exclusive or "owned" brands.

In Auto, 45 per cent of sales come from owned/exclusive brands, 35 per cent at BCF and 11 per cent in sporting goods.

With the exception of sporting goods, the proportion of owned/exclusive goods sales has increased over the past year.

And the market does not appear to be overly ambitious in its expectations for sales, EBIT and net profit.

All are expected to grow in the 2 per cent to 4 per cent range for the next three years.

What the market has rerated is the share price.

Super Retail group shares are up over 30 per cent since the start of the year.

From a relative perspective the shares have moved from being on a PE ratio that was well below its historical average at the start of the year to be a full standard deviation above the average today.

I should point out that on three occasions since 2015, the shares have been two standard deviations about their PE average.

Another way of thinking about valuation is to ask what the market price might be implying.

It appears there will not be any future changes to market share.

It's important to consider this implication, because if it is reasonable to expect Amazon to grow share, the assumption is they will take it from smaller players.

So far Amazon has been less of a concern than many analysts predicted but it is often the case that markets over-estimate the impact of a new entrant in the short term and underestimate it in the long term.

The current price also assumes Super Retail will not be able to improve its margins even by migrating more sales online.

On the face of it, this seems pessimistic.

However, the company will face a cost headwind in 2020 as a result of a new enterprise bargaining agreement that restores weekend and evening penalty rates, and casual loadings which were previously traded away for a higher base rates.

According to Citi Research, a 1 per cent increase in wage costs corresponds with a 2.3 per cent decline in EBIT.

Some retailers — those whose employees are covered by the general retail industry award — face higher labour costs because the award is expected to rise more than 3 per cent in 2019, Citi points out.

A combination of higher employee costs and a slowing economy would, however, be negative for margins as sales recede.

Super Retail is certainly a higher-quality retailer with prospects that do not seem as dire as previously contemplated.

But the share price does suggest the risks could be to the downside.

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