Goldman Sachs JBWere

Research Bulletin

Australian Equities: Portfolio Strategy Review June 2005

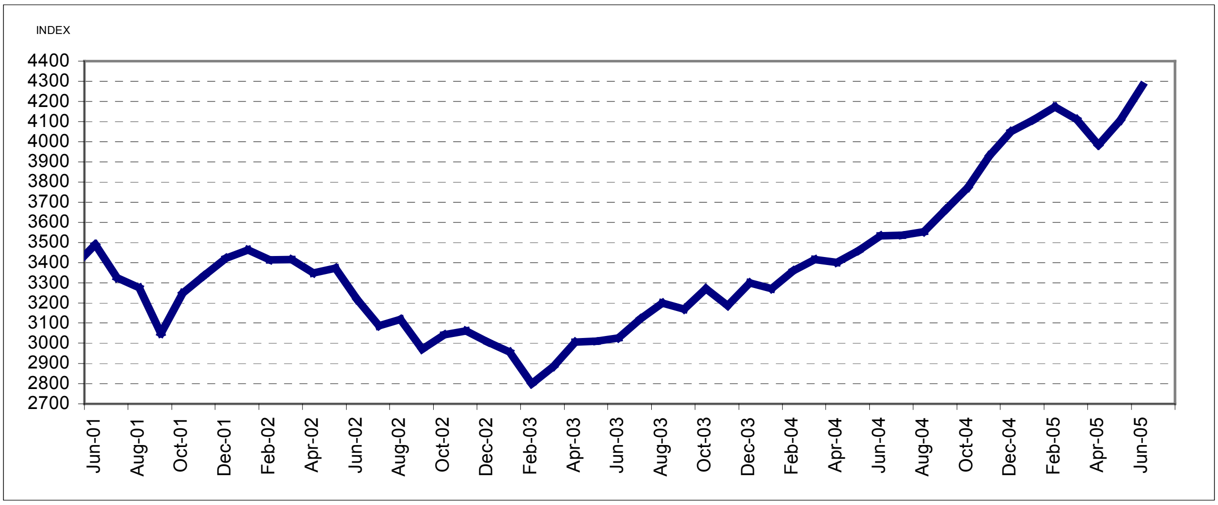
- The S&P/ASX 200 ended the financial year strongly, rising 4.8% during June and establishing new record highs intra-month. Year-to-date the market is up 8% and has returned +26% (including dividends) over the last 12 months. Strong liquidity (completion of large cash takeovers and superannuation inflows) combined with already high cash levels and attractive yields continued to be the main driving force for equities. Australia performed in line with the majority of the region's markets.
- The strength in the market during June was fairly broadly based. Relative to the market, the best performing sectors were Energy, Healthcare and Materials. Telecommunications, Utilities and Consumer Staples lagged the market.
- In light of the increasing margin pressure (higher oil prices, wages) and the frequency of profit warnings, we expect earnings risk will remain high as the market heads into the June 2005 half-reporting period. However, we also believe ongoing buying support will emerge in the event of any further sell-off, reflecting high cash levels of investors (increasing with the completion of various takeovers) and the potential for M&A activity (strong corporate balance sheets).

	Accumulation Index Performance		
	1 Month	**6 Month**	**12 Month**
S&P/ASX 200	4.8%	7.8%	26.4%
S&P/ASX 200 Industrials	3.8%	5.6%	22.6%
S&P/ASX 200 Resources	9.2%	18.7%	45.7%
S&P/ASX Small Ordinaries	5.8%	5.3%	27.4%
	Relative Index Performance to S&P/ASX 200		
Consumer Discretionary	-3.0%	-14.9%	-21.6%
Consumer Staples	-3.1%	-6.5%	2.3%
Energy	8.8%	29.6%	42.5%
Financials	-1.5%	-0.3%	-3.8%
Health Care	5.3%	8.5%	13.1%
Industrials	1.2%	0.9%	12.2%
Information Technology	-3.0%	-6.1%	19.7%
Materials	4.0%	4.0%	10.8%
REITs	0.0%	-6.5%	-8.3%
Telecommunications	-4.3%	-1.6%	-18.6%
Utilities	-3.1%	6.4%	11.0%

Source: GSJBW Research, IRESS

Australian Equity Market Performance: S&P/ASX 200 Index

(June 2001- June 2005)



Source: IRESS

Company Performance: Best and worst performing stocks

In June, the best and worst performing stocks (absolute returns) in the ASX 100 were as follows:

Best	% Change	Worst	% Change
Newcrest Mining	31.3%	Multiplex	-10.7%
Oil Search	23.3%	Challenger	-5.2%
Iluka Resources	23.0%	Ten Network	-5.1%
Cochlear	21.0%	Pacific Brands	-5.0%
PaperlinX	19.9%	Amcor	-3.9%
Woodside Petroleum	17.6%	AXA Asia Pacific	-3.7%
Macquarie Bank	16.6%	National Australia Bank	-3.5%
CSL	15.0%	Henderson Group	-3.4%
Aristocrat Leisure	14.0%	AMP	-3.1%
James Hardie	13.8%	Promina	-2.8%

Source: IRESS

Significant Company News

Energy **Analyst: Anthony Bishop**

- **Woodside Petroleum (WPL): Short Term Marketperform; Long Term Buy; Val'n $21.56**
- **Oil Search (OSH): Short Term Outperform; Long Term Hold; Val'n $2.21**
- **Santos (STO): Short Term Marketperform; Long Term Hold; Val'n $9.30**
- **Tap Oil (TAP): Short Term Outperform; Long Term Buy; Val'n $1.83**

Energy stocks continued to perform strongly during the month (Woodside +18%, Oil Search +23%, Santos +12% and Tap Oil +20%) as positive sentiment towards oil stocks persisted on the back of continuing oil price strength. The price of crude oil reached record highs by breaking the US$60/bbl psychological barrier and is still hovering above US$55/bbl. We review the outlook for the oil price later in this report.

Gold **Analyst: Ian Preston**

- **Oxiana (OXR): Short Term Marketperform; Long Term Hold; Val'n $0.75**
- **Lihir Gold (LHG): Short Term Marketperform; Long Term Buy; Val'n $1.13**
- **Newcrest Mining (NCM): Short Term Marketperform; Long Term Buy; Val'n $9.28**

The gold sector recorded broad-based gains for the month (Newcrest +31%, Lihir +15%). The main driver of this robust performance was continued improvement in the gold price that rallied to a high of US$444/oz during June. In regard to stock specific news, Oxiana (OXR) announced that it was acquiring the Golden Grove base metals operation from Newmont as a going concern for $265m. This transaction fundamentally changes the nature of the OXR asset base by significantly increasing the base metal exposure within the company's asset portfolio. Elsewhere, the board of Lihir Gold (LHG) approved the construction of a flotation plant at the company's gold mine in Papua New Guinea. This extension to the processing facility will materially change the company's production profile, lifting annual production from calendar year 2007 onwards by 140k ounces per annum above the current base of approximately 700k oz pa.

Telstra (TLS) **Analyst: Christian Guerra**

- **Investment View: Short Term Marketperform; Long Term Hold**
- **Share Price as at 30/06/2005: $5.06 Valuation: $5.50**

Telstra's board appointed Mr Solomon Trujillo as Chief Executive Officer and executive director, effective on 1 July 2005. Mr Trujillo's last executive role was CEO of Orange, a mobile subsidiary of France Telecom. Before joining the Orange board, Mr Trujillo was CEO of technology startup Gravitron. He gained the majority of his telecommunication experience in his 26 years with US West Inc.

Mayne (MAY) **Analyst: Jack Mordes**

- **Investment View: Short Term Marketperform; Long Term Hold**
- **Share Price as at 30/06/2005: $4.74 Valuation: $4.67**

Mayne's board has decided to proceed with a demerger of its generic pharmaceutical division from its domestic healthcare businesses, which it expects to be completed this calendar year. The domestic healthcare business could be marketed as a business with stable cash flows and solid revenue growth, offering some turnaround potential whereas the pharmaceutical business will likely offer global healthcare exposure with growth potential. The market reacted positively to confirmation of the demerger going ahead.

Commonwealth Bank of Australia (CBA) **Analyst: James Freeman**

- **Investment View: Short Term Outperform; Long Term Buy**
- **Share Price as at 30/06/2005: $37.95 Valuation: $37.10**

Ralph Norris will take over as Chief Executive Officer and Managing Director, following David Murray's retirement. Mr Norris is currently the Managing Director and Chief Executive Officer of Air New Zealand and from March 1991 to September 2001, Mr Norris was Chief Executive Officer of ASB Bank (CBA's New Zealand business). Mr Norris will commence with the bank in September, which should help ensure that operational momentum is maintained during this CEO changeover period.

Iluka Resources (ILU) **Analyst: Ian Preston**

- **Investment View: Short Term Marketperform; Long Term Hold**
- **Share Price as at 30/06/2005: $7.53 Valuation: $5.11**

Iluka (ILU) performed very strongly over the month driven by the news that an investment syndicate coordinated by BUKA Minerals had purchased a 7.25% stake in the company. BUKA contributed $5m to the purchase of the stake. BUKA has stated that its strategy is to be an investor in companies, rather than an operator. In response to the activity on its registry, ILU confirmed that it had not been approached by, or had any discussions with either BUKA or any member of the consortium that purchased the stock.

Retail **Analyst: George Batsakis**

- **JB Hi-Fi (JBH): Short Term Outperform; Long Term Buy, Val'n $4.10**
- **Colorado Group (CDO): Short Term Marketperform; Long Term Hold, Val'n $5.90**

The spate of profit warnings across the smaller end of the discretionary retail sector continued during June. Revisions to company guidance for fiscal 2005 from a number of small cap retails outside our coverage universe further depressed sentiment towards the sector. Brazin (BZN) was one such company forced to revise guidance lower due to difficult trading conditions in the last quarter of fiscal 2005. The company identified CD and DVD sales as one of the retail areas suffering particularly weak sales. This is consistent with JB Hi Fi's (JBH) recent trading update that showed a major slowdown in sales growth. The apparel retailers have not been immune from the slowdown in consumer spending. Indicative of the difficult trading conditions for apparel retailers, the Colorado (CDO) apparel franchise introduced 10% to 50% discounts off everything in store during the month of June.

Australian Equities: Key Issues for Portfolio Strategy

- Global markets have spent the past year swinging between periods of optimism and pessimism. A handful of weak economic statistics through March and April, along with the high oil price, sent the marginal global investor scurrying for safety. Come May, the economic statistics brightened, the oil price retreated and the optimism quickly returned. While this optimism spilled over into June, by the end of the month investors were again fretting about the oil price that had breached US$60 per barrel.
- While major structural imbalances persist, the global economy still looks reasonably well placed from a cyclical perspective – particularly if the Chinese economy maintains its current vigor. Relative to 2004, global economic and profit momentum has cooled, but business conditions remain supportive and companies continue to enjoy excellent financial health – particularly in the US. As has generally been the case, the actions of the US Federal Reserve will ultimately determine the duration of the current global business cycle. Goldman Sachs Research believes that the Federal Funds rate will continue to rise through 2005, ending the year around 4.00% (currently 3.25%). To date, the Fed's ability to contain rising inflation risks (and an increasingly speculative US property market) has been curtailed by the resilience of long term bond prices. The Fed will become a far more potent risk for global markets if its "measured" increases in short term rates are ever accompanied by higher long term rates.
- The domestic economy is struggling. Discretionary consumer spending has been soft since late last year, residential construction activity is contracting and the business sector (less-so service industries) is confronting higher cost pressures and sluggish sales. While this slowdown is not a surprise – given the boom conditions of 2002/04 – it remains an open question as to whether it will develop into a genuine cyclical downturn (i.e. rising unemployment) that persists well into 2006 or, with the help of a still supportive policy stance, prove to be short-lived (see below). Over the next six months, the market and ourselves will grapple for an answer to this question. Even if the more positive scenario prevails, it will imply that little has been gained in terms of resolving the structural imbalances/inflationary risks that now overhang the economy. Thus, interest rate pressures would in all likelihood quickly reemerge. GSJBW Research forecasts production (GDP) to expand by 2.0% in FY05, 3.1% in FY06 and 3.2% in FY07.
- The policy stance in Australia remains on the generous side of neutral. Interest rates are relatively low, the terms of trade are at a 50 year high, government policy is expansionary and asset prices are basically healthy – less-so residential property. Soft house prices, and the associated implications for a household's willingness to consume the equity in their home, still stand as the major risks facing the economy as it moves into FY06. While acknowledging these risks, the combination of an accommodative policy stance and a fully employed economy has unsettled the Reserve Bank. Accordingly, we still expect that interest rates will move higher over the next year (5.50% currently), although much will depend on whether household spending rebounds through 2H05.
- The strong May/June performance has pushed the ASX300 back into fully valued territory. On the basis of the prevailing outlook for profits, interest rates and liquidity, we continue to believe that the risk of a prolonged correction at this point is low. Material price weakness requires material profit disappointment and while earnings downgrades are now coming through – particularly at the small-cap level – we still believe that the risks of major market-wide downgrades remains relatively contained – particularly if the RBA adopts a more cautious approach. From a medium term perspective however, it is important to keep in mind just how good the past three years have been. On the basis of GSJBW Research estimates, earnings-per-share growth for the ASX300 has expanded by 58% between FY03 and FY05 – a massive step-up in profitability. While the future is always clouded, we can confidently predict that this sort of profit growth will not be replicated between FY06 and FY08. The phase of unexpectedly strong profit growth is now behind us.
- We continue to recommend an equity portfolio based around a core holding of large-cap defensive stocks. Given full valuations, however, buying opportunities in this area are limited. In our view, **Origin Energy, Macquarie Communications Group** and **Promina** represent the best relative value. Interest in the banking sector has been revitalised as the market seeks out relative earnings certainty. On a three-month view, this support is likely to continue. It will quickly cool, however, if the Australian economy continues to weaken or market sentiment towards the global outlook swings back to favour the optimists. **Commonwealth Bank** and **St. George** are the stocks we prefer in the sector at the moment. For investors who are looking for a global growth/cyclical bias, the stocks we favor at current prices are **News Corporation, AXA Asia Pacific, QBE Insurance** and **Computershare.** We continue to believe the medium term outlook for the resources sector is favourable. Investors with a small exposure to the sector should therefore view any periods of share price weakness as an opportunity to add to positions in **BHP Billiton** and **Rio Tinto.** Recent weakness in global steel prices, along with our expectation of a step-down in the copper price over the next six months, may well prove triggers for such periods of share price weakness.

GSJBW Market Forecasts:

As at 30/06/05	**Price Earnings Ratio (PER)**			**Earnings Per share Growth (%)**			**Dividend Yield (%)**		
	FY04	**FY05E**	**FY06E**	**FY04**	**FY05E**	**FY06E**	**FY04**	**FY05E**	**FY06E**
S&P/ASX 300	18.7x	15.2x	13.6x	16.4	23.7	12.0	3.2	3.8	4.2
S&P/ASX 300 Industrials	17.9x	16.2x	14.9x	11.5	10.8	9.2	3.6	4.3	4.6
S&P/ASX 300 Resources	21.4x	12.8x	10.8x	34.6	67.1	18.7	2.2	2.6	3.1

Source: GSJBW Research estimates

Portfolio Management: Switching Ideas

Real Estate Investment Trusts **Analyst: Simon Wheatley**

- **Lend Lease (LLC): Short Term Marketperform; Long Term Hold; Val'n $12.29**
- **General Property Trust (GPT): Short Term Marketperform; Long Term Buy; Val'n $3.55**

Year End December	2005 Estimate		2006 Estimate		2007 Estimate	
	LLC	GPT	LLC	GPT	LLC	GPT
Net Profit ($m)	273.9	493.5	312.8	555.2	344.8	578.0
EPS Growth	16.7%	12.1%	11.5%	12.5%	8.0%	4.1%
PER	16.4x	15.0x	14.7x	13.4x	13.6x	12.7x
Yield	4.2%	6.7%	4.6%	7.5%	5.1%	7.9%

Source: GSJBW Research estimates

- To date, Lend Lease (LLC) has managed to weather the storm of earnings revisions that has battered the property sector over recent months. Nonetheless, we highlight LLC's exposure to both: (1) construction, and (2) residential development as skewing the balance of risks to the downside in the short term.
- For Bovis (LLC's construction business), cost push inflationary pressures relating to building materials are likely to maintain downward pressure on margins over the short to medium term. In addition, the earnings outlook for Delfin (LLC's house and land division) remains a concern. The company recently reconfirmed FY05 earnings guidance for the division, despite having previously made negative comments towards the businesses current state of operations less than two months ago.
- **We retain our neutral hold recommendation for LLC, preferring other opportunities within the listed property sector such as General Property Trust (GPT)**. Following twelve months of uncertainty surrounding management, GPT has now completed a significant restructure involving the internalisation of management, establishment of a joint venture (JV) fund in Europe with Babcock and Brown (BNB) and the sale of interests in three shopping centres.
- Whilst the risk profile of GPT has changed with its foray oversees, we believe this is offset by the increased scope for earnings and distribution growth. We view the Group's high quality, stable domestic portfolio, continued non reliance on construction and development income, and the growth optionality afforded by the BNB JV as supportive of our long-term Buy recommendation.

Steel **Analyst: Andrew Gibson**

- **Bluescope Steel (BSL): Short Term Marketperform; Long Term Hold; Val'n $7.76**
- **Onesteel (OST): Short Term Outperform; Long Term Hold; Val'n $3.10**

Year End December	2005 Estimate		2006 Estimate		2007 Estimate	
	BSL	OST	BSL	OST	BSL	OST
Net Profit ($m)	1022.1	120.5	625.5	131.3	355.3	123.0
EPS Growth	82.1%	11.6%	-35.5%	6.8%	-42.9%	-6.7%
PER	5.9x	10.5x	9.1x	9.8x	16.0x	10.5x
Yield	5.5%	4.9%	5.1%	4.9%	3.5%	4.9%

Source: GSJBW Research estimates

- Hot Rolled Coil (HRC) prices remain the key driver of Bluescope Steel (BSL). In recent months, a substantial rise in inventories in Europe and the US has resulted in HRC price falls across these regions. In our view, there is further downside risk to HRC pricing over the next three months and declining global HRC prices will eventually flow through to BSL's realised HRC price. On our estimates, BSL shows a declining EPS profile from fiscal 2005 onwards, in line with our expectations that HRC prices will peak in the second quarter of 2005 and that input costs increase significantly in fiscal 2006.
- Whilst we believe the buyback may provide some near term share price support, BSL continues to trade at a premium to our valuation. Further, sentiment towards the sector continues to deteriorate. As such, given the above factors and risks, **we are comfortable for investors seeking a more defensive exposure within this volatile sector to switch from BSL into Onesteel (OST)**.
- We retain our positive investment view on OST. We believe that robust levels of non-residential and engineering construction will result in stronger volumes and higher margins in fiscal 2006. On the operational front, issues at Whyalla now appear largely resolved. We believe the near term investment case for OST is further underpinned by solid valuation support, given the stock continues to trade at a significant discount to our valuation and on a relatively attractive fully franked FY06 yield of 4.9%. We also note that falling HRC and scrap prices are positive for OST as the company's margins are under less pressure.
- In the longer term, whilst we believe there is some risk associated with the influence of global pricing and competition, we note that a key positive of Project Magnet (iron ore development) is that it should go some way in offsetting the impact of an eventual downturn in the construction cycle on OST's earnings.

Portfolio Management: Switching Ideas

Healthcare **Analyst: Jack Mordes**

- **Cochlear (COH): Short Term Outperform; Long Term Buy; Val'n $35.85**
- **Healthscope (HSP): Short Term Outperform; Long Term Buy; Val'n $4.76**

Year End December	2005 Estimate		2006 Estimate		2007 Estimate	
	COH	HSP	COH	HSP	COH	HSP
Net Profit ($m)	52.4	16.6	65.1	36.7	81.9	49.9
EPS Growth	23.0%	21.1%	25.8%	59.6%	26.7%	22.1%
PER	37.7x	24.0x	30.0x	15.0x	23.7x	12.3x
Yield	2.0%	2.2%	2.4%	3.5%	2.7%	4.1%

Source: GSJBW Research estimates

- Positive news flow following the release of Cochlear's (COH) new hearing implant, the Nucleus Freedom, has seen the stock appreciate strongly in recent months. We retain our short term Outperform, long term Buy recommendation on COH, confident that fiscal 2006 will likely see a return to solid unit sales growth for the world's largest cochlear implant developer and manufacturer. Offshore feedback indicates that the vast majority of new cochlear implant patients in the US are choosing the Nucleus Freedom because it is the newest device and has more advanced features (e.g. first water-resistant processor). Continuing regulatory issues for its competitors, as well as potential upside from recent acquisitions adds further support to our view.
- The investment case for Healthscope (HSP) also remains compelling. The stock is currently trading on ~15.0x FY06 earnings and in line with our DCF valuation. We highlight that, in the short term, integration risk for HSP remains high as the company digests two major acquisitions, Gribbles and Nova Health. However, feedback to date indicates that the vertical integration of Gribbles Pathology into HSP's hospital business is progressing well and obtaining support from doctors. In addition, HSP has boosted its executive team through the hiring of 6 senior pathology managers which gives us further confidence in the ability of HSP to integrate and manage a business which sits outside the company's core competency of operating hospitals.
- For those investors reviewing their overall exposure to the healthcare sector, we note that COH's solid share price performance may now mean that this stock constitutes a disproportionately large weighting within their portfolios. Should this be the case, **we are comfortable for investors to reallocate some of their healthcare exposure into HSP at current levels**. We reiterate that our long term Buy recommendation on HSP is based on valuation support, the company's strong earnings growth profile and a favourable industry outlook (ageing population base, government support for healthcare services and scope for further consolidation in the sector).

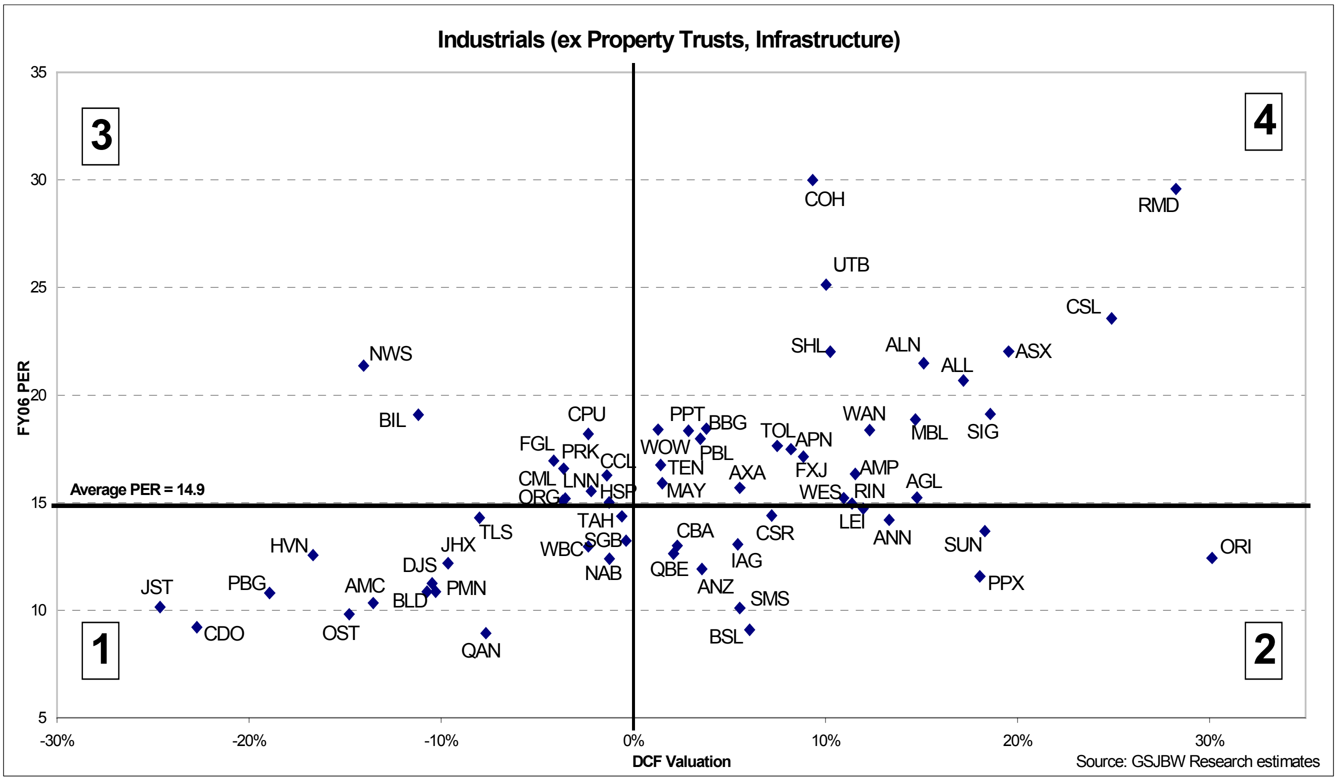
Portfolio Management: Relative Valuation Analysis

In an equity market at all-time highs and awash with liquidity, it may be quite challenging to identify value opportunities in which to invest. Furthermore, many stocks that have performed well may now constitute an excessive proportion of many investors' portfolios. Hence, in times like these where 'value' appears hard to find, it is a useful exercise to return to key indicators of 'value' as a guide for prudent portfolio construction:

- **Price/Earnings Ratio (PER)** – The prospective price/earnings ratio (i.e. the current share price's capitalisation of next year's earnings) is a short-term valuation tool which provides an indication of how reasonable the market's current pricing of the stock is – in other words, how much is the market paying for near term earnings? *We prefer to invest in stocks that have a relatively low PER ratio (based on our forecasts)*.

- **DCF valuation** – The Discounted Cash Flow valuation is focused on a longer time horizon. It attempts to capture the fundamental long term potential of a company (as reflected in its free cash flow generation)*. We prefer to invest in stocks that are trading at or below their DCF valuation (based on our forecasts)*.

To this end, the chart below maps the large-cap industrials universe (excluding Property Trusts and Infrastructure) in terms of fiscal 2006 PER ratio versus DCF valuation. **The objective of this exercise is to identify stocks that are expensive and comfortably valued on both measures**. On the following page, we discuss the implications of this analysis and highlight some of our preferred switching ideas in the current environment.



Source: GSJBW Research Estimates

Chart Notes:
Quadrant (1) – stocks trading at a discount to their DCF valuation and the market PER ratio[1]
Quadrant (2) – stocks trading at premium to their DCF valuation and discount to the market PER ratio
Quadrant (3) – stocks trading at discount to their DCF valuation and premium to the market PER ratio

[1] The market PER is based on our FY06 estimates and calculated on ASX 300 Industrials excluding Property Trusts.

Quadrant (4) – stocks trading at premium to their DCF valuation and the market PER ratio

Based on the analysis as presented in the chart, we can make the following broad conclusions:

- The health stocks are relatively expensive – Cochlear (COH), Resmed (RMD), CSL Limited (CSL). While this is not new, we suspect the gap has widened over recent months.

- The media stocks are relatively expensive, mostly the newspaper publishers – Fairfax (FXJ), APN News & Media (APN), West Australian News (WAN) – particularly compared with other domestic cyclicals. Clearly, a corporate activity premium is priced in. As the risk of an advertising slowdown has increased, we recently downgraded our EPS assumptions for the TV stocks. Furthermore, given the slowing economy in both Australia and New Zealand, coupled with the fact that very strong share price moves have largely removed previous valuation support, we have revised our positive recommendations for FXJ and APN to Underperform/Hold.

- Most financial services stocks are relatively expensive, suggesting an outlook for the economy and financial markets that is inconsistent with the extent of the valuation discount currently being applied to the domestic cyclicals. If this derating of domestic cyclicals is correct, the economy and financial markets will be in for a tough fiscal 2006.

- Valuations within the banking sector are broadly neutral relative to the market. Recently, the banks have been positively re-rated versus the market and are arguably fairly valued at current levels. On a three-month view, we believe this support for the sector will likely continue, particularly versus the non-bank industrial part of the market where earnings risk is increasing.

- Possible **switch ideas** flowing from this relative valuation analysis are:

  1. **CSL, COH and RMD into Healthscope (HSP)**;
  2. **Insurance Australia (IAG) into Promina (PMN)**;
  3. **Australian Gas Light (AGL) into Origin Energy (ORG)**;
  4. **Toll Holdings (TOL) into Brambles (BIL)** – a switch that looks more attractive if the PER is substituted for a cash flow multiple;
  5. **Bluescope Steel (BSL) into Onesteel (OST)**.

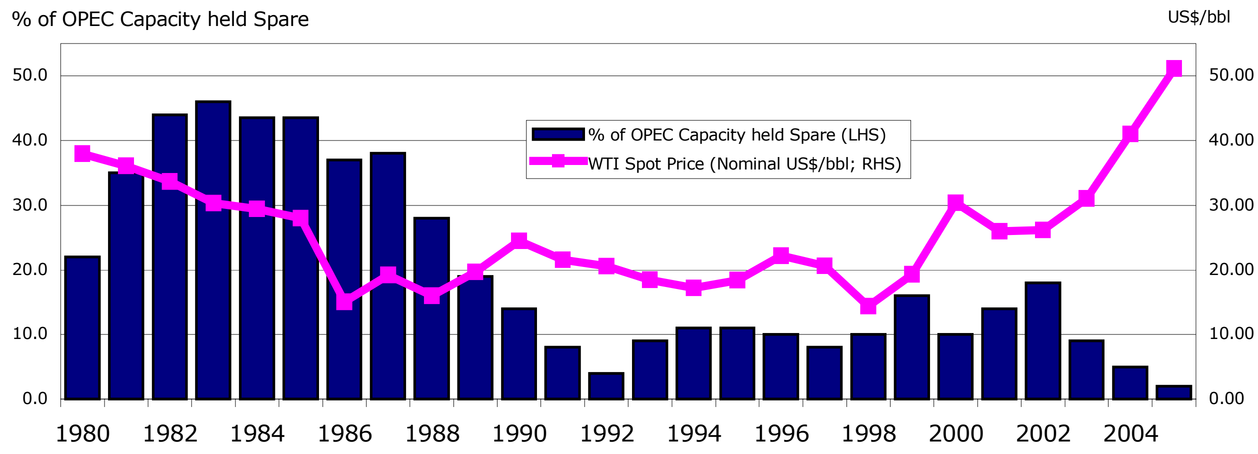
Energy Sector: How High Could the Oil Price Go?

The Energy sector has recorded another very strong month of performance, driven by further appreciation in the spot price of oil, which hit record highs of US$60/bl late in June. With the momentum behind the oil price showing little signs of abating, we believe it is an appropriate time to detail the super spike scenario proposed by our Goldman Sachs colleagues.

The rise in oil prices over the past three years has been accompanied by very strong global demand growth. Historically, an oil price at similar nominal levels to those of today would have been sufficient to suppress demand growth. Goldman Sachs believes that the psychology of a gradual price rise led by strong demand growth (as has been experienced over the past 3 years) is very different from that under which a sudden withdrawal of supply causes a 'spike' in the oil price. It appears that the world has come to terms with rising oil prices much more readily than would have been predicted three years ago.

On the supply side, we believe that oil industry capacity utilisation is running at exceptionally high levels, right from the oil well, through to infrastructure and refining. The amount of spare capacity held back by OPEC is now at an all time low. We believe that the erosion of the spare capacity "cushion" over the past three years (as indicated in the chart below) has been instrumental in driving prices higher.

OPEC Spare Capacity and Oil Price



Source: OPEC Monthly Report, May 2005; BP Statistical Review; GSJBW Research estimates
Note: 2005 data based on year-to-date (June 23)

For oil prices to moderate, either demand growth has to slow materially or supply growth rapidly expand. Goldman Sachs believes that for demand growth to pull back significantly there would have to be one of the following: a rapid and marked change in the behaviour of the US motorist whereby vehicles that operate on high levels of fuel consumption (SUV's for example) were replaced by more efficient means of transport and/or; a postponement of the improving lifestyle aspirations of citizens in countries such as India and China. Goldman Sachs ascribes a very low probability to either of these developments playing out in the near term.

Finally, on the supply side, Goldman Sachs believes that the lead-time for developing sufficient new capacity is substantial. They point out that the most prospective countries for new investment are effectively off limits to Western companies. These areas include Iran, Iraq, Saudi Arabia and even Russia.

With demand proving resilient to rising prices and with supply growth constrained by geo-political issues Goldman Sachs believes that the oil price could trade as high as US$105/bbl before demand is moderated sufficiently to bring prices lower. We find the reasoning behind the super-spike scenario compelling although we question whether an annual average price as high as US$105/bbl would be required to destroy demand.

We believe that an upside scenario with the average price peaking at above US$70/bbl in either 2006 or 2007 is very plausible, and our quantitative judgement is that such a scenario might have a 35% to 40% probability. The following table compares the super-spike scenario price forecasts with the current GSJBW base cash forecasts.

Comparison of Oil Price Forecast Scenarios				
Estimate	**CY05 US$/bbl**	**CY06 US$/bbl**	**CY07 US$/bbl**	**CY08 US$/bbl**
GSJBW Base Case	49.85	47.50	35.00	30.00
Goldman Sachs Base Case	50.64	55.00	30.00	30.00
Goldman Sachs Super-Spike	**50.64**	**75.00**	**105.00**	**75.00**

Source: Goldman Sachs Research estimates; GSJBW Research estimates

The energy sector is an obvious beneficiary of higher oil prices. Stocks with the greatest leverage to the oil price (in order of sensitivity) are Oil Search, ROC Oil, Australian Worldwide Exploration and Santos.

	2006 NPAT			Valuation			Recommendations	
Company	**GSJBW A$m**	**+US$1/bbl A$m**	**Diff %**	**GSJBW A$m**	**+US$1/bbl A$m**	**Diff %**	**S/Term**	**L/Term**
Woodside	1086	1111	2.40%	$21.64	$21.96	1.50%	Marketperform	Buy
Santos	661	680	2.80%	$9.51	$9.69	1.90%	Marketperform	Hold
Origin Energy	347	3.5	0.70%	$7.90	$7.99	1.10%	Marketperform	Buy
Oil Search	322	331	2.90%	$2.21	$2.28	3.20%	Outperform	Buy
Aust Worldwide Exp	34	34	1.70%	$1.72	$1.75	2.00%	Outperform	Buy
Roc Oil	36	37	1.90%	$1.71	$1.75	2.10%	Marketperform	Buy
Tap Oil	37	38	2.80%	$1.86	$1.88	0.90%	Outperform	Buy

Source: GSJBW Research estimates

In the context of the energy sector, we highlight that BHP Billiton also offers significant exposure to the oil price through the operations of its petroleum division. The oil producing assets within BHP are material in scale. We forecast the petroleum business to contribute 18% to group EBIT in fiscal 2006. The core petroleum assets of Bass Strait and the North West Shelf continue to provide outstanding returns on invested capital. Further, we see significant appeal in the company's assets within the Gulf of Mexico, which we forecast will drive strong growth in the company's oil production profile over the medium to long term. We believe that, from a fundamental perspective, BHP's petroleum assets are not being valued with the petroleum premium applied to Woodside (WPL). This is illustrated by the fact that applying the PER rating on which Woodside trades to the BHP Petroleum division would leave the remainder of BHP's assets trading on a prospective FY05 PER of only 8.6x compared to Rio Tinto (RIO) at 10.7x.

We also wish to highlight that we have recently moved our Oil Search (OSH) recommendation to a long term BUY. This upgrade was driven by the announcement in late June that the PNG gas project had signed a conditional agreement with Alcan for the sale of sizeable quantities of gas to the Gove aluminium smelter. The signing of Alcan as a customer has strengthened our confidence that the pipeline will proceed, a key positive for the stock as the PNG project is a critical element in securing long term growth in the company's production profile.

Our positive view on OSH is further underpinned by the company's strong leverage to the spot price of oil. OSH is completely unhedged to the oil price, a scenario that allows for significant upside risk to our earnings forecasts should the oil price continue to appreciate.

From a near term production perspective, whilst the existing assets in PNG are in decline we believe that the company is successfully managing this issue by optimising production across the company's asset base. OSH is also pursuing step out opportunities in PNG that could extend the life of the production assets currently in place within the region.

Finally, the encouraging outlook for OSH is further enhanced by the company's ongoing exploration program. The company is drilling a number of exploration wells towards the end of calendar 2005 in both PNG and Yemen, most of which have targets in excess of 100mmbbl. We believe favourable drilling reports could provide a further share price catalyst for the stock. We reiterate our long term Buy recommendation for OSH.

Stock Selection Using Quantitative Techniques

The main GSJBW multi-factor Quant stock selection model aims to provide diversification across market themes and thus to deliver stable 'through-the-cycle' returns. This is achieved by combining several individual quant screens which each attempt to capture returns, momentum and value factors. The current top rankings in GSJBW's large industrial stock screening model are shown on the table below, as well as changes in rankings over the last month.

Some of these factors are easy to understand – for example, with many investors (whether rightly or wrongly) pricing Australian equities on the basis of price/earnings ratios, changes in consensus earnings per share expectations for future years can be a good signal for future share price performance. We capture this information in our Quant model through use of a screen measuring actual (consensus) earnings revisions over the last 3 months.

However, one factor which may cause some confusion among investors is the 'Positive RSI' factor which also turns out to be one of the most topical factors in the current market environment given recent strong positive equity market performance.

A **Relative Strength Index** is a measure of price momentum that was developed by J. Welles Wilder Jr. in 1978. It is effectively based on a ratio of the average absolute price change (over a particular period – GSJBW Research uses 14 weeks) on days when a share price closes 'up' from its previous day's close to the average absolute price change (over the same period) on days when a share price closes 'down' from its previous day's close:

$$\text{Relative Strength (RS)} \approx \frac{\text{Average price change on 'up' days}}{\text{Average price change on 'down' days}}$$

For example, if a share price is generally trending higher, then it could be expected that the average price change on 'up' days would be larger than the average price change on 'down' days and, thus, such a stock would have higher Relative Strength than another stock which was either not rising as fast, or trending lower. The Relative Strength Index (RSI) itself is calculated as:

$$\text{Relative Strength Index (RSI)} = 100 - \frac{100}{1 + \text{Relative Strength}}$$

This index ranges between 0 (low average momentum) and 100 (high average momentum) for each stock over the 14-week period of analysis. We then rank the stocks in our coverage universe from highest to lowest on this factor, which provides the 'Positive RSI' screen used in our broader Quant model. A long term investment strategy of investing only in the top quartile of stocks from this screen alone (i.e. those with the strongest average positive momentum, using a portfolio that is re-balanced on a monthly basis) would have returned 19.6% per annum over the last 8 years (before transaction costs).

The current top rankings in GSJBW's large industrial stock screening model are shown on the table below, as well as changes in rankings over the last month.

Rank	Company	EVA Spread: Level	EVA Spread: Trend	Earnings Revision: Actual 3 Month	Earnings Revision: Predicted	Positive RSI	ROFE/ PEG	TOTAL	Previous Rank (31-May-05	Move in Rank
		(out of 15)	(out of 15)	(out of 15)	(out of 15)	(out of 10)	(out of 30)	(out of 100)		
1	JHX	13	15	14	15	9	28	**94**	2	1
2	ALL	15	14	12	15	9	28	**94**	3	1
3	RIN	11	14	15	15	9	25	**89**	1	-2
4	RIO	12	14	13	15	5	27	**86**	4	0
5	LEI	13	15	8	0	9	27	**73**	7	2
6	WES	8	14	2	15	10	23	**72**	5	-1
7	BBG	11	13	10	7.5	6	24	**72**	9	2
8	WOW	14	1	8	15	6	26	**70**	10	2
9	BHP	14	1	2	15	5	30	**66**	6	-3
10	SGB	9	7	12	7.5	8	21	**64**	13	3
11	ANN	9	13	6	7.5	8	19	**63**	24	13
12	CBA	7	11	7	7.5	10	20	**62**	15	3

Source: GSJBW Quantitative Research

GSJBW Model Portfolios

Income Portfolio

Commonwealth Bank of Australia	Rural Press
Telstra Corporation	Macquarie Communications Group
Westpac	Rio Tinto
Australian Gas Light Company	CFS Gandel Retail Trust
St George Bank	Alesco
Tabcorp	Foster's
Promina	Commonwealth Property Office Fund
Wesfarmers	Ten Network
Coca-Cola Amatil	Macquarie DDR Trust
Woolworths	Alinta
West Australian Newspapers	

Source: GSJBW Research

Our changes to the Income Portfolio during June 2005:
Reduced: CFS Gandel Retail Trust
Increased: Macquarie DDR Trust, Promina
Removed: National Foods
Added: Alesco

Income Portfolio Summary: Fiscal 2006 (*Please note, MCG & ALN excluded from the calculation of the EPS Growth rate and PER)

Earnings per Share Growth	7.1%
Price to Earnings Ratio	13.8x
Average Yield	5.6%
Franking	81%

Source: GSJBW Research estimates

Defensive Portfolio

Commonwealth Bank of Australia	Rinker
BHP Billiton	Australian Gas Light Company
St George Bank	Tabcorp
Westpac	Foodland Associated
Woolworths	Macquarie Airports
Promina	Macquarie DDR Trust
Origin Energy	Mirrabooka
Coca-Cola Amatil	CFS Gandel Retail Trust
Rio Tinto	Sonic Healthcare
Macquarie Communications Group	Foster's Group
Telstra	Wesfarmers
Transurban Group	Australian Foundation Company

Source: GSJBW Research

Our changes to the Defensive Portfolio during June 2005:
Reduced: Rinker, Transurban Group, CFS Gandel Retail Trust, Mirrabooka, Rinker, Rio Tinto
Increased: Wesfarmers, Macquarie DDR Trust
Added: Australian Foundation Company

Defensive Portfolio Summary: Fiscal 2006 (*Please note, MCG & TCL excluded from the calculation of the EPS Growth rate and PER)

Earnings per Share Growth	9.5%
Price to Earnings Ratio	13.6x
Average Yield	4.8%
Franking	76%

Source: GSJBW Research estimates

All figures or amounts stated in the table above are an estimate only and provided by way of illustration. Actual figures or amounts may vary from those figures or amounts

Balanced Portfolio

BHP Billiton	Billabong International
Commonwealth Bank	News Corporation
Woolworths	Sonic Healthcare
St George Bank	Macquarie DDR Trust
Westpac	Computershare
Origin Energy	Macquarie Infrastructure Group
Promina	Australian Gas Light Company
Coca-Cola Amatil	Foodland Associated
Rio Tinto	Wesfarmers
Telstra	Healthscope
Australian Foundation Company	Brambles
Rinker	Just Group

Source: GSJBW Research

Our changes to the Balanced Portfolio during June 2005:
Reduced: Macquarie Infrastructure Group, Rinker, Billabong, Just Group, Rio Tinto, Computershare
Increased: Wesfarmers
Removed: Cochlear
Added: Australian Foundation Company, Healthscope

Balanced Portfolio Summary: Fiscal 2006 (Please note, MIG excluded from the calculation of the EPS Growth rate and PER)

Earnings per Share Growth	11.4%
Price to Earnings Ratio	13.9x
Average Yield	4.2%
Franking	88%

Source: GSJBW Research estimates

Growth Portfolio

BHP Billiton	Rinker
Commonwealth Bank	Computershare
Woolworths	Sonic Healthcare
St George Bank	Macquarie DDR Trust
Origin Energy	Alinta
Promina	Macquarie Infrastructure Group
Rio Tinto	Foodland Associated
Australian Foundation Company	Toll Holdings
Transurban Group	Brambles
Billabong International	Salmat
News Corporation	Cochlear
Healthscope	Just Group

Source: GSJBW Research

Our changes to the Growth Portfolio during June 2005:
Reduced: Macquarie Infrastructure, Rinker, Billabong, Just Group, Rio Tinto, Cochlear, Transurban, Computershare
Increased: Promina
Removed: WMC Resources
Added: Salmat, Australian Foundation Company

Growth Portfolio Summary: Fiscal 2006 (*Please note, MIG, ALN & TCL excluded from the calculation of the EPS Growth rate and PER)

Earnings per Share Growth	13.1%
Price to Earnings Ratio	14.0x
Average Yield	3.9%
Franking	80%

Source: GSJBW Research estimates

All figures or amounts stated in the table above are an estimate only and provided by way of illustration. Actual figures or amounts may vary from those figures or amounts

GSJBW Recommendation Changes During June

STOCK	ASX CODE	SHORT-TERM Recommendation		LONG-TERM Recommendation	
		NEW	OLD	NEW	OLD
Adelaide Bank	ADB	Marketperform	Not Rated	Hold	Not Rated
APN News & Media	APN	Underperform	Marketperform	Hold	Buy
Foster's Group	FGL	Outperform	Not Rated	Hold	Not Rated
Fairfax	FXJ	Underperform	Outperform	Hold	Hold
General Property Trust	GPT	Marketperform	Marketperform	Buy	Hold
Jubilee Mines	JBM	Marketperform	Outperform	Hold	Hold
Multiplex	MXG	Underperform	Underperform	Sell	Hold
News Corporation (Preferred)	NWSLV	Outperform	Marketperform	Buy	Hold
Telecom New Zealand	TEL	Marketperform	Marketperform	Sell	Hold
WMC Resources*	WMR	Marketperform	Outperform	Sell	Buy
Zinifex	ZFX	Marketperform	Outperform	Buy	Buy

WMC Resources: Research coverage was ceased later in the month.
Source: GSJBW Research

GSJBW Initiation of Research Coverage During June

STOCK	ASX CODE	SHORT-TERM Recommendation	LONG-TERM Recommendation
Babcock & Brown Japan Property	BJT	Marketperform	Sell
Domino's Pizza Australia	DMP	Outperform	Buy

Source: GSJBW Research

GSJBW Cessation of Research Coverage During June

STOCK	ASX CODE
WMC Resources	WMC

Source: GSJBW Research

Referred to in Document:

Stock	ASX code	SHORT-TERM Recommendation	LONG-TERM Recommendation	Share Price (30/06/05)
Adelaide Bank	ADB	Marketperform	Hold	$11.47
Australian Foundation Company	AFI	N/a	Buy	$3.75
Australian Gas Light	AGL	Marketperform	Hold	$14.23
Alinta	ALN	Outperform	Buy	$9.75
Alesco	ALS	Marketperform	Hold	$7.36
APN News & Media	APN	Underperform	Hold	$5.14
Australian Worldwide	AWE	Outperform	Buy	$2.02
AXA Asia Pacific	AXA	Marketperform	Buy	$4.38
Billabong International	BBG	Outperform	Buy	$13.63
BHP Billiton	BHP	Outperform	Buy	$18.15
Brambles	BIL	Outperform	Buy	$8.17
Babcock & Brown Japan Property	BJT	Underperform	Sell	$1.21
Bluescope Steel	BSL	Marketperform	Hold	$8.23
Commonwealth Bank	CBA	Outperform	Buy	$37.95
Coca-Cola Amatil	CCL	Outperform	Buy	$7.89
Colorado	CDO	Marketperform	Hold	$4.56
Cochlear	COH	Outperform	Buy	$39.20
Commonwealth Property	CPA	Marketperform	Buy	$1.27
Computershare	CPU	Outperform	Buy	$5.86
CSL	CSL	Underperform	Hold	$33.72
Domino's Pizza	DMP	Outperform	Buy	$2.37
Foster's Group	FGL	Outperform	Hold	$5.32
Foodland Associated	FOA	Marketperform	Hold	$27.15
Fairfax	FXJ	Underperform	Hold	$4.30
CFS Gandel Retail Trust	GAN	Marketperform	Buy	$1.68
General Property Trust	GPT	Marketperform	Buy	$3.65
Healthscope	HSP	Outperform	Buy	$4.70
Insurance Australia Group	IAG	Marketperform	Hold	$6.01
Iluka Resources	ILU	Marketperform	Hold	$7.53
JB Hi-Fi	JBH	Outperform	Buy	$3.56
Jubilee Mines	JBM	Marketperform	Hold	$7.13
Just Group	JST	Underperform	Hold	$2.11
Lihir Gold	LHG	Marketperform	Buy	$1.22
Lend Lease	LLC	Marketperform	Hold	$12.96
Macquarie Airports	MAP	Outperform	Buy	$3.58
Mayne	MAY	Marketperform	Hold	$4.74
Macquarie Communications	MCG	Outperform	Buy	$6.30
Macquarie DDR Trust	MDT	Marketperform	Buy	$1.19
Macquarie Infrastructure	MIG	Marketperform	Hold	$4.16
Mirrabooka	MIR	N/a	Buy	$1.57
Multiplex	MXG	Underperform	Sell	$2.91
Newcrest Mining	NCM	Marketperform	Buy	$17.38
News Corporation	NWS	Outperform	Buy	$22.35
Origin	ORG	Marketperform	Buy	$7.61
Oil Search	OSH	Outperform	Hold	$3.07
Onesteel	OST	Outperform	Hold	$2.65
Oxiana	OXR	Marketperform	Hold	$0.89
Promina	PMN	Outperform	Buy	$4.71
QBE Insurance	QBE	Outperform	Buy	$16.03
Rinker	RIN	Outperform	Buy	$14.00
Rio Tinto	RIO	Outperform	Buy	$44.82
Resmed	RMD	Underperform	Hold	$8.58
Roc Oil	ROC	Marketperform	Buy	$1.93
Rural Press	RUP	Marketperform	Hold	$10.47
St George Bank	SGB	Outperform	Hold	$26.20
Sonic Healthcare	SHL	Marketperform	Buy	$12.57
Salmat	SLM	Outperform	Buy	$4.72
Santos	STO	Marketperform	Hold	$11.32
Tabcorp	TAH	Underperform	Hold	$16.40
Tap Oil	TAP	Outperform	Buy	$2.40
Transurban	TCL	Marketperform	Sell	$7.45
Telecom New Zealand	TEL	Marketperform	Sell	$5.53
Ten Network	TEN	Marketperform	Hold	$3.55
Telstra	TLS	Marketperform	Hold	$5.06
Toll Holdings	TOL	Marketperform	Buy	$13.06
West Australian News	WAN	Marketperform	Hold	$8.03
Westpac	WBC	Marketperform	Hold	$19.95

Wesfarmers	WES	Marketperform	Buy	$40.01
Woolworths	WOW	Outperform	Buy	$16.51
Woodside Petroleum	WPL	Marketperform	Buy	$29.25
Zinifex	ZFX	Marketperform	Buy	$3.04

Source: IRESS, GSJBW Research

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I, Michael Hawkins, hereby certify that all of the views expressed in this report accurately reflect my personal views about the Subject Company or companies and its or their securities. I also certify that no part of my compensation was, is, or will be, directly or indirectly, related to the specific recommendations or views expressed in this report.

Recommendation Definitions

Short Term

Underperform (UP)	Stock is expected to underperform the S&P/ASX 200 on a 0-6 month timeframe
Marketperform (MP)	Stock is expected to perform in line with the S&P/ASX 200 on a 0-6 month timeframe
Outperform (OP)	Stock is expected to outperform the S&P/ASX 200 on a 0-6 month timeframe

Long Term

Sell (S)	Stock is expected to underperform the S&P/ASX 200 for beyond 6 months
Hold (H)	Stock is expected to perform in line with the S&P/ASX 200 for beyond 6 months
Buy (B)	Stock is expected to outperform the S&P/ASX 200 for beyond 6 months

Other Definitions

NR — Not rated. The investment rating has been suspended temporarily. Such suspension is in compliance with applicable regulations and/or Goldman Sachs JBWere policies in circumstances when Goldman Sachs JBWere is acting in an advisory capacity in a merger or strategic transaction involving the company and in certain other situations

Research Criteria Definitions

The above recommendations are primarily determined with reference to the recommendation criteria outlined below. Analysts can introduce other factors when determining their recommendation, with any material factors stated in the written research where appropriate. Each criterion is clearly defined for the research team to ensure consistent consideration of the relevant criteria in an appropriate manner.

SHORT TERM (0-6 MONTHS)

Relative Earnings Outlook: Forward looking assessment of risk to consensus EPS estimates relative to estimated EPS risk across the market.

Earnings Revision: The percentage change in the current consensus EPS estimate for the stock (year 1) over the consensus EPS estimate for the stock 3 months ago. Stocks are rated according to their relative rank, effectively making it a market relative measure.

News Flow: The consideration of stock specific news flow, market and/or cyclical thematics and other issues such as index changes. Addresses two issues: (1) What is the potential news flow; and (2) What is the share price reflecting?

Relative Performance: Historic rolling 3 month performance versus the broader market. Stocks are rated according to their relative ranking.

Valuation Support: Considers a range of valuation methodologies, including discounted cash flow (DCF) valuation, PER, dividend yield and any other relevant measure.

LONG TERM (> 6 MONTHS)

Industry Structure: Based on Goldman Sachs JBWere industry structure ranking. All industries relevant to the Australian equity market are ranked, based on a combination of Porter's Five Forces of industry structure as well as an industry's growth potential, relevant regulatory risk and probable technological risk. A company's specific ranking is based on the proportion of funds employed in particular industry segments, aggregated to determine an overall company rating, adjusted to reflect a view of the quality of a company's management team.

EVA™ Trend: [1] EVA™ trend forecast for coming two years. Designed to reflect "turnaround stories" or to highlight companies Goldman Sachs JBWere analysts believe will allocate capital poorly in the estimated timeframe. (An ROE measure is used for insurance stocks in conjunction with an assessment of the strength of an insurer's balance sheet).

Growth Option: A qualitative and quantitative assessment of a company's long term growth options that the analyst believes should be considered and possibly recognised by the market.

Price:Base Case DCF: The premium or discount to base case DCF valuation at which the stock is trading relative to the average premium or discount across the market.

[1] *EVA™ is a registered trademark of the U.S. consultancy firm Stern Stewart*

For Insurers

Return On Equity: Rating taking into account the expected level and trend of ROE over the next two to three years.

Balance Sheet: Analyst's assessment of the quality and strength of the insurer's balance sheet, including conservatism of provisioning, sufficiency of capital, and quality of capital.

For REITs

EPU Growth: Ranking of Earnings Per Unit growth relative to other listed Real Estate Investment Trusts. Used instead of EVA™ Trend.

Strategy: Used instead of industry structure as many REIT investors are intra rather than inter sector focussed.

Yield: Yield relative to the REIT sector average. Used instead of Valuation Support.

For NZ Companies

Relevant Index: If a research report is published by the New Zealand affiliate of Goldman Sachs JBWere, the recommendation of a company or trust is based on their performance relative to the NZSX 40 Index (Gross) and not the S&P/ASX 200 index.

Distribution of Recommendations - As at 31st March 2005

Short Term	Overall	Corporate relationship* in last 12 months	Long Term	Overall	Corporate relationship* in last 12 months
Underperform	15%	12%	Sell	6%	4%
Marketperform	60%	60%	Hold	60%	55%
Outperform	25%	27%	Buy	33%	42%

* No direct linkage with overall distribution as the latter relates to the full GSJBW stock coverage (>200 companies). The above table combines the corporate relationships and recommendations of both Goldman Sachs JBWere Pty Ltd and its affiliate in New Zealand, Goldman Sachs JBWere (NZ) Limited.

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