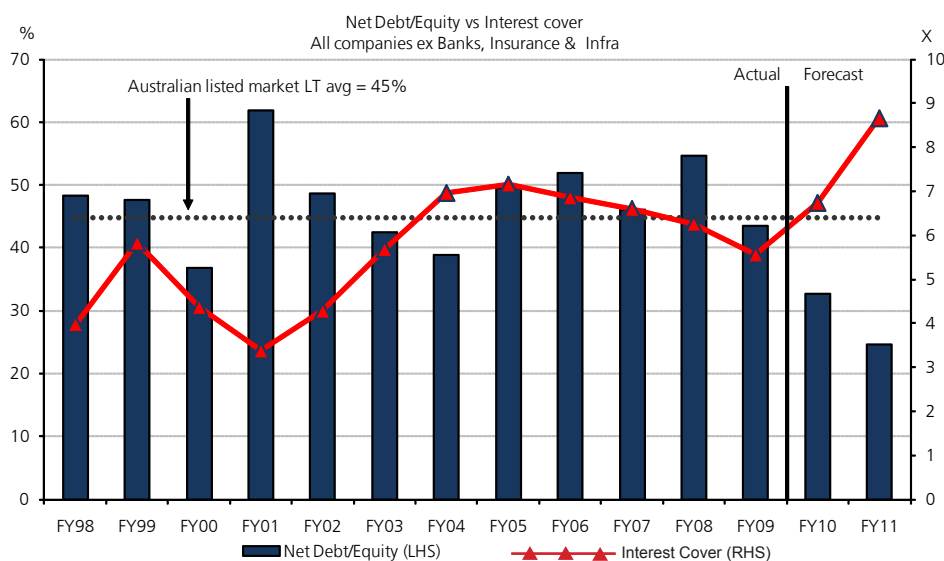


Corporate Australia is in good shape

Global sharemarkets have suffered a crisis of confidence over the past month, with positive sentiment from a nascent global recovery being replaced by fears of the world slipping back into recession. These sentiments have been no different in Australia, with local investors concerned with sovereign debt defaults in Europe and the potential for a wider contagion, any signs of a slowing Chinese economy and the negative impact of the 'Resources Super Profits Tax'. After a period of sustained rate rises, the Official Cash Rate was left unchanged at the June meeting as the RBA reassessed the growth dynamics affecting the Australian economy.

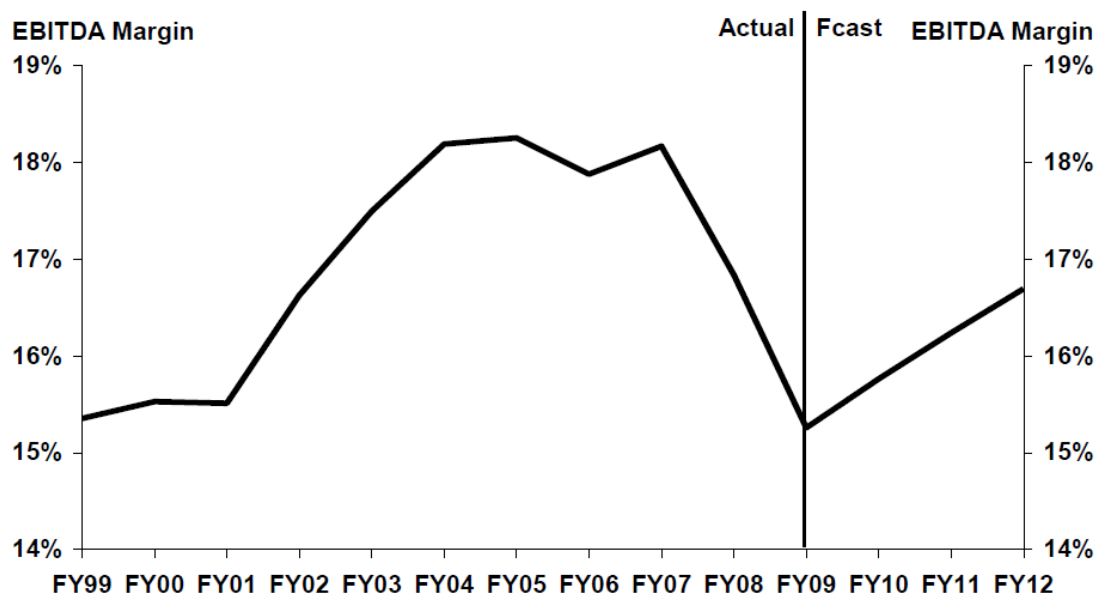
Despite being punished in share price terms over the last two months, Australian companies remain in a very strong financial and operational position. As highlighted below, corporate balance sheets have been fortified since the onset of the Global Financial Crisis - by recapitalisation and cost control – such that gearing levels have fallen from over 50% in 2009 to below 30% by 2011. Consequently, interest cover is also expected to increase significantly as a result of the lower debt levels and improving earnings. As a result, corporate Australia is likely to be less impacted by rising interest rates than in previous cycles.



Source: Macquarie Research

During the slowdown in 2008, many Australian listed corporates reduced their cost of doing business. These cost cutting programs included, but were not limited to, advertising, marketing expenditure, closure or divestment of non-core business units and reductions in labour force. As the rebound in earnings recommenced in late 2009 and early 2010, companies kept their costs relatively stable, resulting in a more than proportional improvement in margins, and earnings uplift, particularly for those cyclical companies geared towards changes in GDP growth.

This margin improvement is highlighted in the chart below. Expectations for corporate earnings remain conservative, and therefore profit margins could also be better than expected.



Source: Macquarie Research, Industrials EBITDA margin forecasts remain well below peak FY04-07 levels.

As stated at the outset, macroeconomic factors are negatively influencing sentiment in the short-term. However, with lower gearing levels, higher interest cover multiples and improving profit margins, fundamentally, corporate Australia remains in a stronger financial position than prior to 2008. We believe this should create a strong platform for future earnings growth.