Economic Insights

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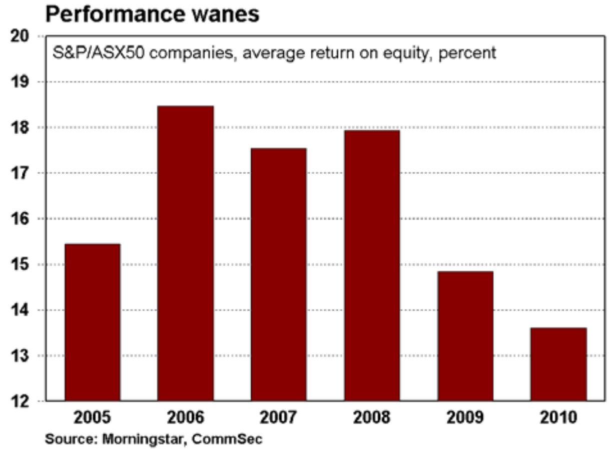
Comparing Aussie companies: facts & fiction

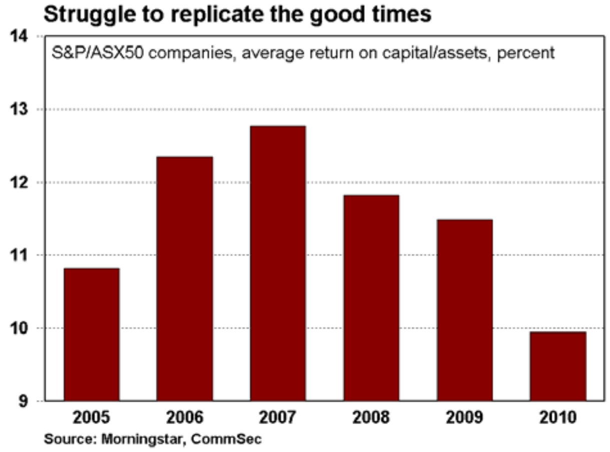
Company financial statistics

- **In recent weeks investors have no doubt found it difficult to sort fact from fiction in the public discussion about company balance sheets. Some commentators have questioned whether banks are generating above-normal profits. Others have questioned whether some companies such as BHP Billiton are making profitable use of capital or whether a portion needs to be returned to shareholders. And still others have focussed on the sustainability of high dividend returns from companies such as Telstra.**
- **To provide a base for the discussion, CommSec has compiled a set of tables on various measures for the S&P/ASX50 – the 50 biggest companies on the sharemarket. The tables are generated from data available from financial research firm, Morningstar.**
- **In 2010 while major banks' posted solid profits, their return on equity ratios were largely in line with the average of S&P/ASX50 companies. And their return on assets ratios were at the bottom of the pack. By contrast Telstra reported market-leading return on equity and return on capital ratios in 2010.**
- **Over the past decade, seven S&P/ASX50 companies had negative shareholder returns including Telstra. Shareholder returns were close to average for CBA, ANZ and Westpac but returns for NAB were below the average of S&P/ASX50 companies.**
- **Resource companies dominate the results of average shareholder returns over the past decade.**

Comparing companies

- The main problem with assessing the performance of Australian companies is that the data isn't generally available in one place. Companies release their financial statistics and these results tend to be analysed on an individual basis or across industry sectors. Unfortunately the data is less commonly analysed across a larger grouping, such as for a top-level ASX index.
- To provide a contribution to the debate on company performance, CommSec has complied data on S&P/ASX50 companies (the 50 largest companies on the sharemarket) from financial information provider, Morningstar.
- While it would be ideal to compare companies across a range of measures, the simple fact is that companies are





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different. For instance measures financial companies don't have sales or revenues in the traditional sense like a mining company or retailer thus precluding assessment on a range of measures. For instance it is not possible to get a directly relatable measure of return on capital for insurance and property companies.

- Another complication is the differing timing of financial years – some companies close off books in June; others December, and many banks have a September year-end. And yet other complications are when there are changes in company structure or ownership or changes in presentation of financial results. These changes can make it difficult to make accurate comparisons across firms.
- Certainly comparisons of companies across a range of metrics can be very useful for an investor. The common problem facing new investors is determining what company to invest in. Still, as is constantly stressed, assessment of past performance may not prove an accurate guide to the future. But it is one step on the road. Assessment of company management, industry structure, industry prospects, the role of government, global trends and merger & acquisition risks are just some of the factors that investors need to undertake before deciding on a share purchase.

Return on equity

- This measure attempts to show whether investors are getting a decent return on their investment. In other words it is important not to look just at the size of the profit being achieved, but to compare it with equity being provided by investors. The ratio is "calculated by dividing net profit before abnormals by shareholders equity."
- On average the S&P/ASX50 companies had an average return on equity of 13.61 per cent in 2010, down from 14.84 per cent in 2009 and 17.93 per cent in 2008. Mining companies tended to out-perform in 2010 while property companies tended to under-perform. Fortescue led the rankings by a considerable margin (51.6 per cent) from Telstra (30.6 per cent) and Computershare (30.3 per cent).
- Banks were generally close to the S&P/ASX50 average with CBA, Westpac and ANZ slightly above the norm and NAB, Macquarie and Suncorp-Metway below average.

RETURN ON EQUITY, 2010

Fortescue	51.6	ASX	11.5
Telstra	30.6	News Corp	11.1
Computershare	30.3	Toll Holdings	10.3
AMP	29.5	Incitec Pivot	10.3
Coca Cola Amail	28.1	Lend Lease	9.7
Brambles	27.6	Macquarie Bank	9.4
Woolworths	26.7	Crown	8.6
Foster's	26.5	Westfield	7.6
BHP Billiton	25.7	Wesfarmers	6.3
Leightons	24.5	Origin Energy	6.0
CSL	22.1	Suncorp Metway	5.8
Orica	21.8	Stockland	5.5
QBE Insurance	19.3	GPT Group	5.4
CBA	16.8	One Steel	5.4
Worley Parsons	15.9	AGL Energy	5.3
Newcrest	15.4	CFS Retail	5.2
Westpac	15.4	Mirvac	5.1
ANZ	15.1	Asciano	4.6
Rio Tinto	14.5	Oil Search	3.8
AXA Asia Pacific	13.9	Santos	3.6
Woodside Petroleum	13.9	IAG	3.1
Tabcorp	13.6	Qantas	2.9
NAB	11.9	Bluescope	2.6
Sonic Healthcare	11.5	Transurban	1.5
Amcor	11.5	Macquarie Airports	(4.0)

Source: Morningstar, CommSec

Return on capital/assets

- This measure shows the return on equity and debt capital. "It is measured by dividing operating profit after income tax before interest by shareholders equity and long-term debt."
- On average the S&P/ASX50 companies had an average return on capital or assets of 9.95 per cent in 2010, down from 11.49 per cent in 2009 and 11.82 per cent in 2008. Leighton Holdings led the rankings (27 per cent) from Fortescue (26 per cent) and Woolworths and BHP Billiton (both 21 per cent).
- Banks had the lowest return on assets – around 1 per cent – and well below the average return for major companies.

RETURN ON CAPITAL / ASSETS, 2010

Leightons	27.0	News Corp	9.0
Fortescue	26.0	Crown	8.0
Woolworths	21.0	Toll Holdings	8.0
BHP Billiton	21.0	Wesfarmers	7.0
CSL	20.0	Origin Energy	6.0
Orica	19.0	One Steel	6.0
Telstra	18.0	Asciano	6.0
Computershare	17.0	AGL Energy	5.0
Brambles	16.0	Transurban	5.0
Coca Cola Amail	16.0	Oil Search	4.0
Foster's	16.0	Santos	4.0
Newcrest	15.0	Qantas	3.0
ASX	13.0	Bluescope	3.0
Worley Parsons	12.0	Macquarie Airports	2.0
Tabcorp	11.0	ANZ	1.0
Rio Tinto	11.0	Westpac	1.0
Incitec Pivot	10.0	CBA	0.9
Amcor	10.0	Suncorp Metway	0.9
Woodside Petroleum	9.0	Macquarie Bank	0.7
Sonic Healthcare	9.0	NAB	0.6

Source: Morningstar, CommSec

Payout ratio

- The payout ratio is "The percentage of net profit paid out as dividends. It is calculated by dividing the total dividend payout during the year by net profit before abnormals. "
- There can be outliers such as in 2010 with Toll Holdings (525 per cent) and Macquarie Airports (-164 per cent). But excluding these companies, on average companies in the S&P/ASX50 paid out 66 per cent of profits to investors as dividends.
- Some companies elect to hold back dividends so they can reinvest earnings back into the companies or pursue mergers and acquisitions. For instance Fortescue had a payout ratio of zero in 2010 with Rio Tinto at 13 per cent, Newcrest at 16 per cent and BHP Billiton at 39 per cent. Clearly mining companies are seeking to expand operations and investigate any profitable M&A opportunities in the current environment. But if the M&A opportunities fail to pan out, there is the option of returning cash to investors.
- Property companies had high payout ratios in 2010 while Telstra was in the top grouping at 89 per cent. Most banks had above-average payout ratios with CBA leading with 81 per cent according to Morningstar calculations.

Total shareholder return

- Total shareholder return is "the annualised return to shareholders, including all price changes and reinvestment of dividends. It includes the effect of bonus issues and splits. This figure is calculated pre-tax. "
- Shareholder return has fluctuated markedly in recent years. On average the return for the S&P/ASX50 companies was 45.4 per cent in 2005, 31.6 per cent in 2006, 38.6 per cent in 2007, 5.4 per cent in 2008, -16.4 per cent in 2009 and 15.3 per cent in 2010.
- Rio Tinto led the returns in 2010 with 155.2 per cent and produced average returns of 44.5 per cent over the past six years, ahead of the average returns of 20 per cent.
- Compared with the 20 per cent average return over the past six years, NAB had

10-YEAR SHAREHOLDER RETURN

Fortescue	91.0	ANZ	10.2
Newcrest	28.2	Westpac	9.9
Origin Energy	25.2	Amcor	8.6
Leightons	22.1	IAG	7.9
Orica	21.9	Macquarie Bank	7.4
BHP Billiton	20.3	Foster's	7.1
Rio Tinto	18.0	Transurban	6.9
Toll Holdings	17.9	Stockland	6.3
Oil Search	17.3	Sonic Healthcare	5.8
Woolworths	17.2	Suncorp Metway	4.9
One Steel	16.8	Tabcorp	3.5
ASX	15.6	NAB	3.2
Wesfarmers	15.6	Qantas	2.9
Woodside Petroleum	15.3	Computershare	2.7
Coca Cola Amail	15.0	Brambles	-1.5
Santos	13.3	Mirvac	-1.8
CSL	13.0	Telstra	-1.9
AXA Asia Pacific	12.3	GPT Group	-3.8
QBE Insurance	11.1	AMP	-4.3
CFS Retail	10.8	Lend Lease	-6.1
CBA	10.2	News Corp	-6.6

Source: Morningstar, CommSec

PAYOUT RATIO

Transurban	525	QBE Insurance	66
IAG	192	ANZ	65
Santos	139	Worley Parsons	64
CFS Retail	120	Toll Holdings	63
Westfield	116	Bluescope	62
Stockland	110	OneSteel	61
Crown	96	Macquarie Bank	59
Wesfarmers	92	AXA Asia Pacific	58
GPT Group	92	Woodside Petroleum	56
Telstra	89	Suncorp Metway	54
ASX	88	Orica	51
AGL Energy	87	CSL	49
Mirvac	86	Lend Lease	47
CBA	81	Oil Search	47
Sonic Healthcare	79	Computershare	42
AMP	79	BHP Billiton	39
Amcor	74	Foster's	32
NAB	73	Incitec Pivot	20
Leightons	72	Newcrest	16
Coca Cola Amail	72	News Corp	14
Origin Energy	72	Rio Tinto	13
Westpac	72	Asciano	0
Tabcorp	71	Fortescue	0
Woolworths	70	Qantas	0
Brambles	67	Macquarie Airports	(164)

Source: Morningstar, CommSec

TAX-ADJUSTED DIVIDEND YIELD

Telstra	8.4	OneSteel	2.8
Tabcorp	5.4	Macquarie Bank	2.8
NAB	5.2	Transurban	2.7
Westpac	5.2	Origin Energy	2.6
CBA	4.9	Santos	2.6
QBE Insurance	4.6	Amcor	2.6
ANZ	4.6	Woodside Petroleum	2.2
AMP	4.0	Brambles	2.2
CFS Retail	3.9	AGL Energy	2.1
Macquarie Airports	3.8	GPT Group	2.0
ASX	3.8	Computershare	2.0
Westfield	3.7	Worley Parsons	1.9
Mirvac	3.5	Foster's	1.9
Stockland	3.4	BHP Billiton	1.8
Leightons	3.4	AXA Asia Pacific	1.8
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IAG	3.1	Newcrest	0.3
Coca Cola Amail	3.0	Fortescue	0.0
Crown	3.0	Asciano	0.0
Orica	2.9	Qantas	0.0

Source: Morningstar, CommSec

returns of 8 per cent, Westpac 12.2 per cent, CBA 14.8 per cent, ANZ 12.4 per cent, Suncorp Metway 2.7 per cent and Macquarie 19 per cent. Telstra also under-performed with average returns of 1.8 per cent over the past six years.

- Over the past 10 years shareholder returns for S&P/ASX50 companies has averaged 11.7 per cent per annum. Fortescue has led the way by a large margin with average returns of 91 per cent, followed by Newcrest (28.2 per cent) and Origin Energy (25.2 per cent). At the other end of the scale, News Corp, Lend Lease and AMP were calculated to have produced negative returns over the period.
- If Fortescue is excluded, average returns for S&P/ASX50 companies were 9.7 per cent. CBA, ANZ and Westpac produced close to average returns while other banks under-performed.

Tax-adjusted dividend yield

- The tax-adjusted dividend yield is "calculated by including the effect of imputation credits from franked dividends or, in the case of property trust dividends, by including the effect of tax-free and tax-deferred dividends. For the purposes of the calculation, it is assumed the shareholder is on the top marginal tax rate of 45 percent."
- The average yield across the S&P/ASX50 companies is 2.9 per cent. Telstra leads the way with a yield of 8.4 per cent followed by Tabcorp with 5.4 per cent with the four major banks and insurance companies AMP and QBE taking the next six top positions.
- At the other end of the scale resource and industrial companies offer low dividends together with growth-focussed companies, News Corp and CSL.
- Traditionally telcos, utilities, financial and real estate companies have offered higher yields to reflect their relative lack of growth opportunities compared with media, healthcare and resource companies.

What does it mean for investors?

- Clearly there can be a lot of rhetoric about the relative performances of listed companies. But, as always, it pays to do your homework.
- Certainly the analysis has focussed on just a few measures of corporate performance and has been limited to the top 50 companies on the sharemarket. Other measures such as price to earnings, price to book, extent of leverage (debt reliance), operating margin and profit margin (for non-financial firms), current ratio, quick ratio and earnings stability.
- Comparing company ratios is only part of the journey, and clearly the exercise is backward looking. Investors have to assess other measures like the strength of management and then make an assessment on the outlook.
- Our analysts at Commonwealth Bank are constantly assessing developments affecting individual companies and giving recommendations about which stocks represent the best value. The coverage of stocks extends to 98 companies including smaller stocks across the ASX200. They are particularly positive about prospects for resource companies with Buy recommendations on a raft of stocks such as BHP Billiton, Rio Tinto, Newcrest, Origin Energy and Woodside Petroleum. Amongst the banks the analysts have a Buy recommendation on ANZ (CBA is not covered). The analysts have a Sell recommendation on Telstra highlighting "risks to earnings, cash flows and dividends going forward as the company adopts a much more aggressive share winback strategy, and fixed line competition increases as the NBN is rolled out and Telstra is ultimately structurally separated."
- Certainly Australian companies are very well cashed up and therefore positioned for shocks, increased investment/capital spending and merger & acquisition opportunities. If the opportunities don't arise, companies are positioned to return excess funds to shareholders. Across the S&P/ASX50 stocks cash assets stood at $64.3 billion in 2010, up 5.6 per cent on a year ago. CommSec estimates that ASX200 companies are sitting on cash assets of over $100 billion, up 6 per cent on a year ago.
- Companies will no doubt assess opportunities very carefully as well as the need to return capital to investors. The aim is both to maximise profitability and return on equity/capital as well as to maintain an efficient balance sheet.

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