

# BRAMWELL BROWN LTD

## INVESTMENT ADVISERS – BROKERS

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### **Bramwell Brown Limited – Newsletter – September 2013**

#### **Meridian Energy**

The Government has confirmed that Meridian Energy will be the next state asset to be sold as part of its mixed ownership model. They will be selling 49 per cent of the company with a listing expected in November. Instalment receipts will be used as an incentive to attract retail investors – allowing payment to be made in two instalments. The first instalment for around 60 per cent of the share price will be paid up front, with the remainder being paid in 18 months. Between the first and second instalments, investors will receive the full portion of any dividends paid out in that period.

In contrast to Mighty River Power there will be no pre-registration, and the minimum initial application will be \$1,000. The shares will be offered in a price-range, with the final price not known until after applications have been submitted. This is the same process used in the Mighty River Power float, and other recent share offers. There will, however, be a price cap for New Zealand retail investors. At the time the offer document is lodged the price range will be announced, with a maximum price retail investors will be expected to pay.

Here is a recap on what we know about Meridian Energy. Like Mighty River and Genesis Energy, Meridian originated from the break-up of the Electricity Corporation during the reforms in 1999.

#### Generation

Meridian owns seven hydro-electric power stations:

- Ohau A, B and C in the MacKenzie Basin, North Otago
- Benmore in the Waitaki Valley, North Otago
- Aviemore in the Waitaki Valley, North Otago
- Waitaki in the Waitaki Valley, North Otago
- Manapouri in the Fiordland National Park (the largest hydro power station in the country)

They have five further hydro projects at various stages of development in North Canterbury, South Canterbury, and the South Island's West Coast.

They own five wind farms:

- Te Uku in Waikato (28 turbines)
- Te Apiti on the northern side of the Manawatu Gorge (55 turbines)
- West Wind on the Makara Coast, Wellington (62 turbines)
- White Hill in Southland (29 turbines)
- Mt Millar in South Australia (35 turbines)

They also own the Brooklyn turbine in Wellington and have a small wind farm on Ross Island, Antarctica. They are developing further wind projects both in New Zealand and Australia. Central Wind is a proposed 52-turbine farm between Waiouru and Taihape, and Mill Creek is a 26-turbine farm currently under construction in the Ohariu Valley. The 64-turbine Mt Mercer wind farm in Victoria is expected to be completed in 2014. Other proposed projects include Mt Munro, south of Eketahuna and the Hurunui project in North Canterbury.

### Retail

Meridian also retails electricity to approximately 270,000 residential and business customers throughout New Zealand through its Meridian and Powershop brands. They have a 10% market share in the North Island and a 25% market share in the South Island.

### Tiwai Point

Tiwai Points remains one of the principle risks for Meridian Energy, as it does for the other electricity generators. The Rio Tinto aluminium smelter at Tiwai Point takes nearly all of the electricity generated by Meridian's Manapouri hydro power station. It accounts for approximately 13% of the electricity generated in New Zealand. The risks around the closure of the smelter were well documented in the Mighty River prospectus and remain particularly relevant to Meridian. The \$30 million subsidy offered by the Government recently to keep the plant running is a short-term measure. The deal struck by the Government ensures the plant will stay open until January 2017 – anything beyond that will be determined by aluminium prices at the time. The closure of Tiwai Point would result in a huge increase in the supply of hydro electricity to the market, and that must lead to lower prices – a great outcome for consumers but not so good for the generators.

Something investors will need to consider when they are weighing up an investment in Meridian is the mix of electricity assets they might like to hold. All the generators have advantages and disadvantages depending on the weather and lake levels throughout the year. The Government website has some very good information on the electricity sector - <https://www.governmentshareoffers.govt.nz/home/>

## Interest Rates

Are we starting to see the bottom of the interest rate cycle? Longer-term mortgage rates have risen recently and we are starting to see higher yields in the longer terms for bonds trading in the secondary market. The sentiment coming out of Europe and the US seems to be more optimistic than it has been for some time, with talk of a reduction in the various quantitative easing programmes around the world. Here is a selection of bonds trading in the secondary market.

<b>Bond</b>	<b>Coupon Rate</b>	<b>Maturity</b>	<b>Current Yield</b>	<b>April 2013 Yield</b>	<b>Current Price/\$100</b>
Wellington Airport	7.50%	November 2013	4.00%	5.00%	100.71
Tauranga City Council	7.05%	December 2013	2.85%	3.49%	101.06
Contact Energy	8.00%	May 2014	4.00%	4.20%	102.78
Fletcher Building	9.00%	May 2014	5.30%	5.40%	102.53
Vector	7.80%	October 2014	4.10%	4.10%	104.02
Auckland Airport	7.00%	November 2014	3.61%	3.70%	104.07
Kiwi Income Property Trust	8.95%	December 2014	5.55%	4.85%	106.03
Trustpower	7.60%	December 2014	4.84%	5.00%	103.44
Auckland City Council	6.28%	March 2015	3.67%	3.71%	103.94
Fonterra	7.75%	March 2015	3.67%	3.74%	106.04
Meridian Energy	7.15%	March 2015	3.96%	3.88%	104.74
Goodman Property Trust	7.75%	June 2015	4.44%	4.60%	105.67
Warehouse	7.37%	June 2015	4.50%	5.10%	104.88
Telecom	8.35%	June 2015	4.44%	4.25%	106.65
Trustpower	8.40%	December 2015	5.55%	5.30%	106.21
Fletcher Building	9.00%	May 2016	5.40%	5.30%	108.95
Goodman Fielder	7.54%	May 2016	5.30%	5.90%	105.62
Infratil	8.50%	June 2016	5.90%	6.10%	106.65
Z Energy	7.35%	October 2016	5.25%	5.30%	105.97
Air New Zealand	6.90%	November 2016	5.40%	5.60%	104.35
Auckland Airport	8.00%	November 2016	4.70%	4.25%	109.71
Trustpower	8.00%	December 2016	5.15%	5.40%	108.58
Meridian Energy	7.55%	March 2017	4.90%	4.43%	108.53
Infratil	8.50%	June 2017	6.20%	6.50%	107.72
Trustpower	7.10%	December 2017	5.60%	5.40%	105.69
Z Energy Limited	7.25%	August 2018	5.90%	5.60%	105.77
Infratil	6.85%	June 2022	7.00%		99.02

You can see that short-term rates are lower than they were in April; however some of the long-term yields are starting to rise. The recent Infratil bond is a good example. Issued with an interest rate of 6.85%, you can now buy it in the secondary market with a yield to maturity of 7.00%. There is clearly a market expectation that rates are going to go up in the longer-term. Those who have invested in fixed interest over the last couple of years are likely to be disappointed as they see rates rising and the value of their bonds falling. Of course we can't have it both ways. Those who invested before the global financial crisis have been enjoying returns of 8% and over for the last five years. My advice has always been to spread your fixed interest maturities so that you always have money maturing regularly over a five year period. This will help take the volatility out of your fixed interest returns.

### **Ross Asset Management**

David Ross has pleaded guilty to the biggest fraud in New Zealand history. Ross was operating a Ponzi scheme after promising returns of up to 30% per annum. I have written previously about how best to prevent falling victim to a fraud such as this, and I believe the key point is to ensure your investments are registered in your own name. By all means seek advice from an Authorised Financial Adviser, but when you purchase securities make sure they are in your name. You should then be in a position to trade those securities through any broker in the country. Also, think very carefully before giving an adviser discretion over your investments. Ross ran a discretionary investment management (DIMs) service which allowed him complete discretion over where and how he invested client money.

### **Rabobank**

In the July newsletter I talked about the relationship we have developed with Rabobank. We now have the ability to take out term deposits with Rabobank on behalf of clients. Rabobank also offer a Premium Saver account which is an on-call account offering interest of 4.20%. The balance of your account must increase by \$50 per month to qualify for that rate.

Other rates available (annual interest):

<b>Term</b>	<b>Rate</b>
1 year	4.10%
2 years	4.40%
3 years	4.60%
4 years	5.00%
5 years	5.50%