HOW TO TRADE RIGHTS ISSUES

By John Atkinson and Steve Baker

Following the Noble rights trade article many readers asked for a more detailed explanation of the strategy. These notes are historical, but the same principles continue to apply.

Rights Issues shareholders have the opportunity to buy in direction proportion to the size of their current holding. This means that shareholders can often buy more than $5,000 worth, as the amount purchased depends on the number of existing shares (or rights) that they are holding as at the record date announced by the Company.

For instance, if you were holding 60,000 shares at the record date of 15 April 2004 for HDR's recent Rights Issue of 1 for 6 at $1.10, you would have been able to buy 10,000 additional HDR shares at $1.10 i.e. at a 15% discount.

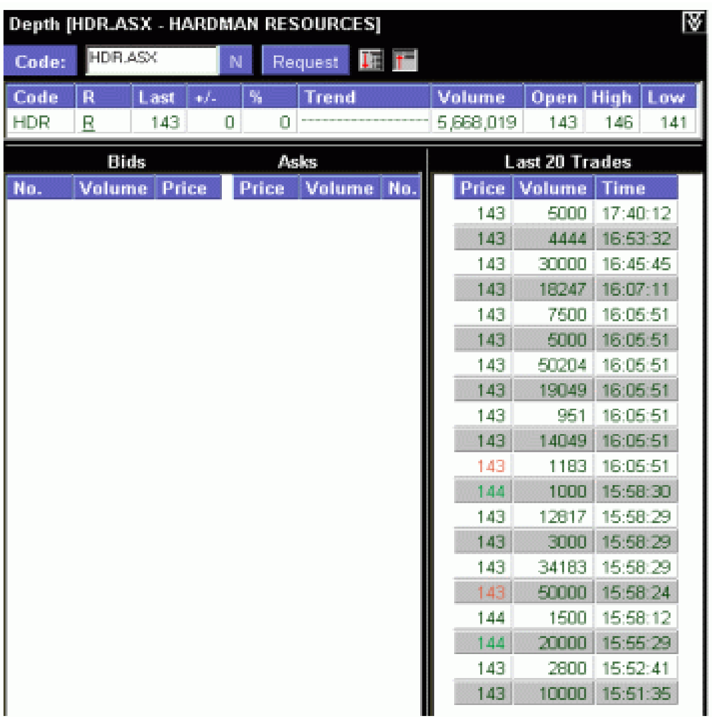
Rights Issues are also the domain of institutional traders who take advantage of these discounts on a much larger scale.

Rights Issues can be Renounceable or Non-Renounceable.

With Non-Renounceable Issues, the right to take up additional shares is non-transferable i.e. the common way of profiting from these Issues is to simply buy up to your entitlement amount at the nominated discount price, with the intention of selling at a later profit.

However, with *Renounceable Issues* the right to take up additional shares is a tradeable instrument and can be sold on market for a defined period, with traded prices fluctuating in relation to the price of the parent share (similar to derivatives) and supply/demand factors. So if traders elect to do so, once they have received their entitlement, they can sell their Rights on market without having to come up with the extra funds to purchase additional shares.

Once a Rights Issue is announced the shares trade "**cum** entitlement" up until the "ex" date when they trade "**ex** entitlement"


Depth [HDR.ASX - HARDMAN RESOURCES]

Code: HDR.ASX N Request

Code	R	Last	+/-	%	Trend	Volume	Open	High	Low
HDR	R	143	0	0	----------------	5,668,019	143	146	141

Bids / Asks

No.	Volume	Price	Price	Volume	No.

Last 20 Trades

Price	Volume	Time
143	5000	17:40:12
143	4444	16:53:32
143	30000	16:45:45
143	18247	16:07:11
143	7500	16:05:51
143	5000	16:05:51
143	50204	16:05:51
143	19049	16:05:51
143	951	16:05:51
143	14049	16:05:51
143	1183	16:05:51
144	1000	15:58:30
143	12817	15:58:29
143	3000	15:58:29
143	34183	15:58:29
143	50000	15:58:24
144	1500	15:58:12
144	20000	15:55:29
143	2800	15:52:41
143	10000	15:51:35

Shareholders who open or increase their position in the days before the share goes 'ex' have built–in additional share value from their potential to buy their entitlement. Correspondingly, those investors buying after it goes 'ex' cannot take advantage of the Rights Issue and so the share is worth less. This decline in value of the "ex entitlement" share price and the value of the Rights can be calculated prior to the shares going "ex entitlement" (see below).

Before we discuss these calculations and some short term trading strategies with Rights Issues, we need to look at some key dates.

As an example, we turn to HDR's recent non-renounceable announcement which was originally advised as:

Ex-Entitlement Date: 6 April 2004 (subsequently revised to 7 April 2004).
Record Date: 14 April 2004 (subsequently revised to 15 April 2004).
Prospectus with Entitlement and Acceptance Form dispatch date: 20 April 2004 (subsequently revised to 21 April 2004).

It is important that readers understand that buying shares just before the Record Date does <u>not</u> entitle them to the Rights Issue. They must buy 'cum entitlement', that is, before the 'ex' date which is usually set by the company as a week before the record date to allow settlement and processing.

The converse of this is also true in that shareholders who sell their shares after the 'ex' date but before the record date are still deemed to be holding as the 'ownership' has not been settled, so they actually still get the Rights Issue entitlement <u>even though they have sold their shares in the meantime</u>.

After a share goes 'ex entitlement', the ASX clears the boards of all buyers and sellers for that share. This is to avoid any unaware investors leaving their shares on screen prior to the subsequent readjustment down in value.

The screen shot shows the last 20 trades and the blank market depth after the close of business for HDR on 6 April 2004, the revised day before it went 'ex'.(note also the four trades that were done after market between brokers).

The next day, traders had to place their orders on screen afresh. One short term strategy on trading a Rights Issue is to buy as soon as possible after the initial announcement of the Issue, provided that the 'ex date' has not already passed <u>and the price is rising</u>.

On the expectation that the share will increase in price as buyers move in to 'get set' and seek their entitlements, the aim is then to hold until the day before it goes 'ex', unless a short term signal e.g. reversal bar/candle is given prior.

In the next article we discuss how these short term trading strategies are implemented.

John may be contacted at john_at_poolside@optusnet.com.au.