

Research Insight

News from CommSec research

Welcome to this week's edition of the CommSec Research Insight. Each week we share the unique insights of the CommSec Equities Research team based on the research we prepare for institutional clients (ie fund managers). We provide you with a quick wrap on the state of our share market, a few feature articles on the most interesting recent research reports we've issued and snippets on stocks and sectors that have been making the news.

Feature Article

Our feature articles this week are:

- AMP Limited: Room to move but still something to lose
- PrimeAg Australia Limited: No buyback or apparent short-term catalysts
- ResMed Inc: Don't let volatile FX overshadow fundamentals

The comments in the article below are an abbreviated restatement of our analysts' reports.

A glossary of frequently used investment terms can be found at the end of this report

Feature Article

AMP Limited¹: Room to move but still something to lose

Last traded: \$6.35

Sector: Financials

Market cap: \$12,888M

ACCUMULATE / OUT PERFORM

Valuation: \$6.44

Summary of previous report dated 09/11/09

AMP bid for AXA

The proposal to merge with AXA Asia Pacific (AXA AP) ticks a number of boxes for AMP – scale and diversification, along with much needed access to independent financial advisers (where AMP is underweight).

The deal is not so straightforward for AXA shareholders. Given that AMP needs the AXA business to give it the above benefits, AXA AP shareholders want to be rewarded with the appropriate premium for their assets. In this light, AMP's proposal on Monday was deemed inadequate by independent directors of AXA AP.

Just the beginning

The proposal announced by AMP simply starts the process of a potential merger, but an increased bid is required and likely from the perspective of both parties (AXA AP and AMP).

Our current valuation on AMP is \$6.44 (pre any AXA deal) and based on the \$6.12 closing share price of AMP on Monday, we estimate that AMP can pay up to \$4.7b for the AXA A&NZ business without impacting our valuation of AMP.



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Market Wrap

It doesn't matter what you read or watch in the financial media at present, there is probably some reference to China. And that's an amazing transformation in a short period of time. It used to be that the US was the centre of the financial universe, but clearly the centre of gravity has dramatically shifted.

Certainly when we wake up every morning we still want to know how the Dow Jones has performed. The US sharemarket still has a major role in influencing our sharemarket as it does for the majority of major developed markets. But when it comes to assessing economic influence and power, for Australia it is China that dominates.

China is Australia's major trading partner accounting for over 15% of two-way trade. And not only is China the biggest market, trade has lifted by 30% over the past year.

The good news for Australia is that the Chinese economy is growing strongly, boosting prospects for mining, mining services and construction companies.

Matt Comyn
General Manager

Feature Article

PrimeAg Australia Limited: No buyback or apparent short-term catalysts

Last traded: \$1.045

Sector: Financials

Market cap: \$156M

ACCUMULATE / MARKET PERFORM

Valuation \$1.86

Summary of previous report dated 05/11/09

Downgrades to FY10-11 forecasts

Following recent downgrades to our medium term wheat and sorghum price forecasts, we have subsequently downgraded PAG's FY10-11 forecasts.

We believe in the strong long-term fundamental drivers of soft commodities demand, that PAG's water entitlements should appreciate over the next decade and that the current share price implies unrealistically low rural values (just ~25% of what PAG paid). However, with a weaker short-term outlook for soft commodity prices and no share buyback being announced by PAG, we do not see any apparent catalysts to drive the share price towards our valuation. We therefore downgrade our recommendation on PAG to ACCUMULATE / MARKET PERFORM.

Our NAV-based valuation is unchanged (\$1.86 per share) but we have moved our price target from an adjusted NAV-based price target to an FY11 EV/EBITDA-based price target of \$1.19 per share (down 33.9%, using agribusiness FY11 EV / EBITDA multiple of 7.6x).

Feature Article

ResMed Inc: Don't let volatile FX overshadow fundamentals

Last traded: \$5.26

Sector: Healthcare

Market cap: \$776M

BUY / OUT PERFORM

Valuation: \$5.20

Summary of previous report dated 6/11/09

Positive 1Q10 result

RMD's recent 1Q10 result was broadly in line with our expectations, with RMD delivering 13% sales growth to \$247m, 'on target' gross margin at 60.8% and 50% NPAT growth to \$42.1m. The key drivers were a positive product mix, new product launches, supply chain efficiencies and currency movements.

With 'double leverage' to the AUD, RMD faces FX headwinds in the short term. Despite this, we retain our BUY / OUT PERFORM recommendation with the strong fundamentals of the stock offsetting the impact of FX movements (as evidenced recently).

Positive catalysts include additional product launches, ongoing market shares gains and progress on home sleep therapy. Risks include the Medicare competitive bidding program and US healthcare reform.

Stocks at a glance

Following is a summary of a selection of recent reports distributed by CommSec research.

Stocks by sector

Financials

<p>ASX 12/11/09</p> <p>Summary of report dated 05/11/09</p>	<p>ASX Limited: The October lull</p>
<p>Last Traded: \$33.60 Market Cap: \$5,798M Sector: Financials</p> <p>ACCUMULATE / MARKET PERFORM Valuation: \$38.74</p> <p>Sticking to the trend</p> <p>Following ASX Limited's (ASX) release of its monthly trading report, it was evident that this year's October figures reflect the typical start of the quarter decline.</p> <p>For example, the volume and value figures by majority experienced a breather in October, and while these numbers were up on pcp, they were down on September. This is consistent with the current trend of the first month of the quarter being weak and the last month of the quarter being typically higher.</p> <p>We see the current share price as close to fair value for the stock. We retain our \$38.74 valuation, \$35.44 price target and ACCUMULATE / MARKET PERFORM recommendation.</p>	

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Industrials

<p>TCL 12/11/09</p> <p>Summary of report dated /09</p>	<p>Transurban Group: A second bite likely</p>
<p>Last Traded: \$5.55 Market Cap: \$6,992M Sector: Industrials</p> <p>BUY / MARKET PERFORM Valuation: \$5.60</p> <p>Offer is considered low so a higher bid likely</p> <p>TCL rejected a takeover offer from Canadian Pension Plan (CPP) and Ontario Teachers' Pension Plan (OTPP) at \$5.25 per security.</p> <p>CPP/OTTP are expected to come back with a higher bid with a price up to \$6.00 achievable and consequently we have increased our price target to \$6.00 per security (\$1.25) to reflect the likelihood of a higher bid.</p> <p>In this light there remains significant upside from current prices warranting a short-term BUY recommendation. CBA has upgraded its recommendation to BUY / MARKET PERFORM</p>	

Given our view that CPP/OTTP are likely to come back with a higher bid there remains significant short term upside

Utilities

<p>HDF 12/11/09</p> <p>Summary of report dated 06/11/09</p>	<p>Hastings Diversified Utilities Fund: Progress on funding a major positive</p>
<p>Last Traded: \$1.045 Market Cap: \$507M Sector: Utilities</p> <p>BUY / MARKET PERFORM Valuation: \$1.60</p> <p>Important milestone achieved</p> <p>Epic Energy, 100% owned by HDF, announced that it had secured credit approval for funding the stage 3 expansion of the South West Queensland Pipeline (SWQP).</p> <p>The stage 3 expansion of SWQP will be transforming for Epic Energy and HDF. Epic's EBITDA is expected to double by FY12 whereas FCF per security is forecast to grow by ~26%. This announcement represented an important milestone in terms of securing the funds for the project.</p> <p>Given HDF is trading on an FY10 FCF yield of 13%, little of this upside is currently factored into the current security price. We therefore remain comfortable with our BUY / MARKET PERFORM recommendation.</p>	

The stage 3 expansion of SWQP will be transforming for Epic Energy and HDF

Happy investing!

Recommendation Definitions**SHORT TERM (over the next 6 months we expect the share price to):**

BUY	Appreciate by >10%
ACCUMULATE	Increase between 2% and 10%
REDUCE	Increase by less than 2% or fall by up to 5%
SELL	Fall by >5%
REV	Company is under review - no recommendation available

LONG TERM (over the next 24 months we expect the total return to):

Outperform (O / P)	Exceed market return by >5%
Market Perform (M / P)	Be in line with market return, +/-5%
Under Perform (U / P)	Be less than market return by >5%
REV	Company is under review - no recommendation available

² Members of the Commonwealth Group have received fees within the previous 2 years from AMP Limited

Glossary of frequently used investment terms

2P	proved plus probable	FUM	funds under management
3P	proved, probable and possible	GEP	gross earned premiums
ABARE	Australian Bureau of Agricultural and Resource Economics	GJ	gigajoule
ACCC	Australian Competition and Consumer Commission	GWP	gross written premiums
AGM	annual general meeting	JV	joint venture
APRA	Australian Prudential Regulation Authority	LNG	liquefied natural gas
ARTC	Australian Rail Track Corporation Ltd	L-R	long run
ATO	Australian Taxation Office	MAT	moving annual total
bbl	billions of barrels	Mboe	thousands of barrels of oil equivalent
bbls	barrels	mom	month on month
bp	basis points	MOU	Memorandum of understanding
CAGR	compounded annual growth rate	MRET	mandatory renewable energy target
CCGT	combined-cycle gas turbine	NAV	net asset value
CEO	chief executive officer	NPAT	net profit after tax
COGS	cost of goods sold	NPV	net present value
cps	cents per share	NTA	net asset backing per share
cpu	cost per unit	OCGT	open-cycle gas turbine
CSG	coal seam gas	OIP	oil in place
CSM	coal seam methane	OTC	over the counter
DCF	discounted cash flow	P/E	price-earnings ratio
D&A	depreciation and amortisation	pcp	prior comparable period
DRP	dividend reinvestment plan	ppt	percentage point
EBIT	earnings before interest and tax	PSI	offering into pipelines
EBITDA	earnings before interest, tax, depreciations, amortisation	SOTP	sum of the parts
EPCM	Engineer Procure Construct Manage	TEUs	twenty equivalent units
EPS	earnings per share	VWAP	volume-weighted average price
ETS	emissions trading scheme	WACC	weighted average cost of capital
EV	enterprise value	WIH	work in hand
FTA	free to air	y-o-y	year on year

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More information on our research methodology, organisation structure, summary documenting frequency and recommendations can be obtained at research.commsec.com.au

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End of Report