Research Insight

CommSec

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.

Issue 179 30 September 2010 (4.30pm)

Feature Article

Our feature articles this week are:

- **Austin Engineering Limited**
- **BHP Billiton Limited**

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

Austin Engineering Limited

Last traded: $4.32	Sector: Industrials	Market cap: $312m
Buy		Price target: $4.61

Summary of previous report dated 28/09/10

Austin powers ahead

ANG is one of the largest manufacturers of dump truck bodies in the world. The outlook for this market is strong over the next 2-3 years as global mine production increases in response to the surge in commodity demand and prices. ANG has entered a number of lucrative markets via acquisitions and JVs. The acquisition of Conymet in 2009 has provided ANG with a beachhead into the South American market, a leading mining region globally, and we view the Brazilian JV with Delp Engineering to be a low risk option in a large potential market. Over the last two years Bradken (BKN) has accumulated a 19.9% stake in ANG without making its intentions clear. We believe that BKN will make a bid for ANG to mitigate the impact of losing the Australian distribution license for Esco mining equipment in 2011. Esco's direct entry into the market poses a threat to BKN and ANG, and may be the catalyst for a takeover.

Optimally positioned in growth markets

The recent acquisition of Pilbara Hire as well as several other initiatives are increasing ANG's capability in maintenance and repair. We see a number of potential upside catalysts including a takeover by BKN, further near term acquisitions and an accompanying equity raising.
In light of these catalysts, ANG's conservative gearing and strong FCF generation we initiate coverage with a Buy recommendation and a $4.61 per share target price.

Market Wrap

As investors, you no doubt spend plenty of time reading research reports and doing your own analysis. But no matter how much reading you do, you just can't beat getting information from the 'coal face'. Certainly our CBA Equities Research analysts are not stuck behind the desk with the Head of Resources, Andrew Hines, currently in South America on a BHP analyst tour.

Part of the tour involved a visit to Escondida – the world's largest copper mine. In Hines' words: "Escondida is a truly spectacular asset – you don't need to be a mining engineer to appreciate the stunning scope of world's largest copper mine." Now Escondida has suffered from declining production in recent years but management are committed to boosting production capacity and exploration in the area. In short Hines believes that "Escondida has decades of life left and many expansion options."

Certainly world copper demand continues to rise, led by China. Supply is not keeping pace with demand. Stockpiles are falling and BHP sees a demand/supply shortfall out to at least 2020. There is no alternative to keep exploring and examining ways to boost production

Stephen Karpin
Managing Director

BHP Billiton Limited

Last traded: $38.91 Sector: Materials Market cap: $204,905m

Buy Price target:$49.00

Summary of previous report dated 28/09/10

Escondida proves tier one resilience

BHP is conducting an investor tour of its South American copper operations. The opening visit to Escondida has reinforced ongoing upside in this tier one resource against a forecast for continued strength in the copper market. BHP is very bullish on the outlook for the copper price driven mainly by continued growth of Chinese demand, which is expected to double by 2025. BHP sees demand outstripping supply to at least 2020 with supply also being impacted by falling grades at existing mines. As well, treatment and refining costs remain low for miners as the copper smelting industry remains in over-capacity. Escondida is currently considering a series of project and organic growth options that will not only offset declining grades, but may lift production to levels above previous peaks. In the past two years production at Escondida has been adversely impacted by declining grades and problems with the SAG mill. FY11 production is expected to decline by a further 5-10%, due to lower grades, before a strong recovery in 2012 surpassing historical peak production. Escondida has decades of life left with many expansion options and this visit is likely to result in consensus upgrades to medium and long-term forecasts.

The post-GFC recovery is moving to a new phase

We currently view the stock as outstandingly cheap at around 9xFY11 earnings. Furthermore BHP earnings will continue to lift, rising on robust commodity prices and volumes in the post-GFC environment. The deployment of BHP's enormous cash flow towards a strong pipeline of organic growth projects further leverages this upside. We retain our Buy recommendation and AUD49 price target.

Stocks at a glance

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

Stocks by sector

Consumer discretionary

TGA
30/09/10

Summary of report dated 28/09/10

Thorn Group

Last Traded: $1.50	Market Cap: $194m	Sector: Cons. discretionary
Buy		Price target:$1.80

Playing the leasing game

TGA is a specialist finance provider dominating a niche in the small ticket leasing market. In the post-GFC environment, TGA see opportunities in the broader financing sector, ranging from cash loans to mid-ticket SME asset and vendor financing. Like its competitor FlexiGroup (FXL) the expansion of product offerings partly reflects the market opportunity, as established funders have exited and/or reduced exposure to SME and vendor finance. It also reflects the limited long-term growth within their existing markets. Both companies have the capability to compete effectively in new markets. We view TGA as a low-risk investment due to high forecast growth within its core business, and minimal long-term funding risk given its growth to date has been self-funded, and it has the capacity to continue doing so, while achieving our forecast earnings growth. Although we believe FXL has better longer-term growth options following its move into mid-ticket leasing.

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Initiating coverage with a Buy recommendation

TGA like FXL is dominant in its own niche financing markets with considerable capabilities in leasing, sales, credit controls and product development. Our PE-based valuation applies a market discount to TGA based on its long-term funding risk and growth options. We initiate coverage on TGA with a Buy recommendation and $1.80 price target.

Healthcare

BKL
30/09/10

Summary of report dated 27/09/10

Blackmores Limited

Last Traded: $28.26	Market Cap: $460m	Sector: Healthcare
Buy		Price target: $28.00

Sowing the seeds of growth

We met with the BKL Asia management team recently. Asia is a key growth priority for BKL over the next 3-5 years and successful execution is critical to unlocking the value potential in the stock. BKL is actively pursuing a number of low-risk initiatives to drive growth, including new and existing channel expansion, retail supply agreements, new market entry and new product development. The strategy will give BKL considerable growth options in coming years which is currently not reflected in the share price. We continue to see upside on a constant currency basis over the next 12-24 months from positive margin leverage and as volumes in Asia continue to grow. BKL is also looking to directly source raw material inputs which will boost gross margins.

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Buy recommendation retained

The stock is now up 20% since July and we increase our price target to $28.00 from $25.90. Margin leverage out of Warriewood and growth in Asia are now both delivering ahead of expectations. We continue to see upside for FY11 and FY12 on the back of the volume leverage story and as the momentum in Asia starts to build, albeit off a low base.

CSL
30/09/10

Summary of report dated 27/09/10

CSL Limited

Last Traded: $33.05	Market Cap: $18,303m	Sector: Healthcare
Hold		Price target: $32.42

Octapharma announces a total recall

On 24 September, Octapharma announced a voluntary withdrawal of all lots of Octagam 5% (its lower concentrate IVIG brand) in the US. While product recalls do happen in the plasma derived product market, this recall is large and has involved a high number of thromboembolic events. Moving forward, Octapharma's handling of the recall could determine its longer term viability and opportunities for its major competitors. Octapharma appears to have identified the "root cause" of the manufacturing problem and it expects to have fixed the problem by the end of CY10. If the recall is managed well, Octapharma is likely to minimise its reputational damage and market share leakage. This means it will have a limited impact on CSL. Conversely if it is not well managed, its major competitors, including CSL, will effectively split its market share. Given Octapharma's progress with the recall to date and FDA's generous stance, we are factoring in only a small gain in market share to CSL in FY11.

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Maintain Hold recommendation

We have made minor positive changes to our CSL forecasts and price target. While the product recall is a short-term (possibly longer) positive for CSL, it will continue to face short-term headwinds with reimbursement scrutiny and a stronger AUD. In turn, we maintain our Hold recommendation on the stock with the buyback program limiting any downside risk.

Happy investing!

Recommendation definitions
CBA Institutional Equities Investment recommendations are determined by the covering analyst and reflect the analyst's assessment of a stock's expected total shareholder return (TSR). TSR is calculated as the difference between the analyst's 12-month price target and the current share price plus the forecast dividend yield.

Buy: Stocks with a Buy recommendation represent the most attractive stocks under the analyst's coverage. They are forecast to generate significantly positive expected total shareholder returns.

Hold: Stocks with a Hold recommendation are less attractive than Buy rated stocks. They are forecast to generate flat to slightly positive expected total shareholder returns.

Sell: Stocks with a Sell recommendation are the least attractive stocks. They are forecast to generate flat or negative expected total shareholder returns.

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

Disclosure and Disclaimer

End of Report