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 188 **02 December 2010 (4.30pm)**

Feature Article

Our feature articles this week are:

- **Ridley Corporation Limited**
- **Ramsay Healthcare 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

Ridley Corporation Limited[1]

Last traded: $1.25	Sector: Food & Beverage	Market cap: $400m
Buy		Price target: $1.40

Summary of previous report dated 01/12/10

Principal activity: RIC manufactures and markets animal nutritition solutions and solar salt. Its two businesses are Ridley AgriProducts and Cheetham Salt.

All trends point to Buy

We initiate cover of RIC with a Buy recommendation. RIC's AgriProducts will benefit from widespread crop quality downgrades on the east coast over the coming weeks, lifting feed grain supply for the next two years. We expect herd rebuilding to support stockfeed demand beyond this point. The long-term grain consumption and production trends are also moving in RIC's favour as more grain is likely to be consumed domestically, which underpins the demand outlook for RIC's products and we believe it is an attractive takeover target. On our forecasts, Graincorp (GNC) could pay up to $1.60 per share in cash for RIC and the transaction would still be EPS accretive. RIC has significantly reduced its operating risk by increasing the level of contracted volumes in both its AgriProducts and Cheetham salt and divesting the underperforming North American division. It is now a clean investment.

Investment view

RIC is the only company in the food and agribusiness sector that we forecast will consistently deliver an ROIC above WACC from FY12. Our valuation is $1.31 per share and price target is $1.40 per share.

Market Wrap

If I was to sum up the economy in one word, it would be 'patchy'. The economy is growing, but certainly not uniformly. For instance 11 of the 19 industry sectors actually went backwards in the September quarter. And if you strip out the rural sector, the rest of our economy also went slightly backwards.

Still, we shouldn't panic. The economy is still growing and given the firm result in the June quarter we should have expected some softening in the September quarter. However the soft result is clearly a wake-up call.

All we have been hearing about over the past year is our booming terms of trade (rising export prices and falling import prices). The concern has been that this income boost would filter across the economy boosting wages and prices.

Certainly that is a risk, but it is not the full story. As the Reserve Bank has previously suggested, if the income boost is saved, not spent, it is less of a concern. And that is happening. Businesses are cautious about spending and borrowing and cautious Aussie consumers have been saving more.

But while all this is good news for borrowers – no rate hikes for now – the conservatism will continue to make life tough for retailers.

Stephen Karpin
Managing Director

Feature Article

Ramsay Healthcare Limited

Last traded: $15.58 Sector: Healthcare Market cap: $3,114m

Buy Price target: $17.51

Summary of previous report dated 29/1110

Principal activity: Ramsay Health Care is the largest private hospital operator in Australia and has operations across the United Kingdom, France and Indonesia. The company owns a portfolio of hospitals located in NSW, Victoria, Qld, SA and WA.

Get out of the bed – initiate with a Buy

We initiate coverage of Ramsay Health Care with a $17.51 price target and Buy recommendation. Given this implies a 16.3% total return, we initiate with a BUY recommendation. In line with historical trends, RHC will continue to benefit from a robust private hospital market underpinned by attractive demographics, a supportive regulatory environment and weak competition from the public hospital sector. That said, RHC is currently trading close to its all time share price high ($16.07/sh intraday 11 Nov-10). In turn, we look at three key issues we believe will help RHC outperform the market over the next 12-24 months. 1) The continued trend towards increased day surgery episodes will support margin growth in the near to medium term; 2) With RHC's brownfield program reasonably well understood, we focus on recent initiatives with the public sector such as Surgery Connect and Public Private Partnerships (PPPs). The success of these arrangements combined with sluggish reform in the public hospital sector could lead to further partnerships with cost effective/efficient private operators like RHC; 3) Historically, RHC has paid reasonable prices for assets and integrated them successfully. While there are limited opportunities for RHC in the UK, the combination of a fragmented market and challenging operating conditions should present opportunities in France

Investment view

Despite its recent share price rally, we believe RHC remains an attractive buying opportunity with exposure to the defensive domestic private hospital market, momentum in NHS outsourcing in the UK, a healthy growth profile and upside from contract wins and/or acquisitions. The downside risk to our view is unfavourable regulatory change.

Stocks at a glance

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

Stocks by sector

Consumer staples

GNC
02/12/10

Summary of report dated 01/12/10

GrainCorp Limited

Last Traded: $6.48	Market Cap: $1,279m	Sector: Food & Agribusiness
Buy		Price target: $8.50

A bumpy ride to a bumper crop

GNC is set to receive the largest inflow of grain in many years. However, excess rainfall is leading to crop quality downgrades and harvest delays which limits the upside potential to GNC's earnings. A crop of FY11's size is too large to be exported in one year, and FY12 earnings are likely to be underpinned by strong exports. GNC has a dominant position in the east coast grain supply chain, which is attractive to international grain traders and GNC's network provides it with asymmetrical informational advantages for grain trading. We expect GNC to continue to increase its share of the export wheat market until it eventually controls ~30% of the east coast crop each year. Grain consumption growth on the east coast is outstripping grain production growth, which will eventually lead to less grain exports through GNC's terminals unless there is a supply side breakthrough (e.g. GM crops). However, we believe GNC will respond by lifting grain export pricing at the port by significantly more than CPI over the next decade, and looking for further downstream processing assets, potentially including RIC.

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Investment view

Although recent and forecast rainfall reduces the chance of material upgrades to our forecasts, we still forecast GNC to deliver 68% profit growth in FY11 and the shipping stem for FY12 is likely to become as full as the current stem for FY11 (>7MT booked), which increases medium-term earnings certainty. We maintain our Buy recommendation on GNC.

Industrials

CPB
30/11/10

Summary of report dated 30/11/10

Campbell Brothers Limited

Last Traded: $37.63	Market Cap: $2,475m	Sector: Comm.& prof. services
Hold (from Buy)		Price target: $36.94

Minerals delivers super profits

CPB reported its 1H11 result with adjusted NPAT of $67.8m, up 77% on pcp, and near the top of the guidance range. This was a very strong result, driven by the booming minerals division, which is at the forefront of the global surge in exploration activity. Minerals earnings increased 116% over pcp, driven by a 950bp recovery in the margin. The Environmental division posted a 35.7% increase in profits, aided by a full half contribution from Ecowise as well as an 80bp improvement in margin. A weaker-than-expected performance from the coal business combined with currency headwinds tempered the result.

CPB's share price has increased 17.6% since we initiated coverage in September

Investment view

CPB is a high-quality business with strong growth prospects over the next three years. We have upgraded our EPS forecasts to reflect earnings momentum within the business as well as the contribution from the recently acquired Ammtex business. CPB's share price has increased 17.6% since we initiated coverage in September and therefore we downgrade our recommendation to a Hold. Our price target increases from $34.98 to $36.94.

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.

[1] Members of the Commonwealth Group hold between 5 and 10% of IPL

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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End of Report