Switzer Super Report

Monday 21 September 2015

The waiting game

So now we play a waiting game when it comes to US Fed interest rates, but what does that mean to us in Australia and for your portfolio? I reveal all today – and it's not all bad news, although we have had a rough ride of it on the market today.

Also in the *Switzer Super Report*, Paul Rickard has some great health stocks to consider. They might be trading on high PEs but at today's prices, they are certainly worth considering.

James Dunn has five stocks under $5 and in *Buy, Sell, Hold – what the brokers say*, Oroton Group and TPG Telecom get upgrades. And finally, our *Super Stock Selectors* like Telstra but don't have time for Myer or Blackmores.

Sincerely,

Peter

Peter Switzer

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3 hot healthcare stocks to buy in weakness

by Paul Rickard

Key points

- *Ramsay might be fully priced but it is a company that has consistently met or exceeded its forecasts.*
- *CSL recently completed the acquisition of Novartis' influenza vaccine business, making CSL the second largest influenza vaccine manufacturer in the world.*
- *Resmed's FY15 revenue was US$1.7 billion, up 13% on a constant currency basis. It's a little more speculative, but worth the risk.*

The healthcare sector has been the best performing sector on the ASX over the last decade. To the end of August, it's up 15.1% pa compared to an average of 6.2% pa for the S&P/ASX 200 – or a massive outperformance of almost 9% per annum. The same is true over 5 years, 3 years, 1 year – and even this calendar year, where the S&P/ASX 200 (as measured by the accumulation index) is down 0.85% to last Friday, while healthcare is up by 4.96%.

Total Returns

	YTD to 18 Sept	1 yr to 31/8/15	3 yrs to 31/8/15	5 yrs to 31/8/15	10 yrs to 31/8/15
S&P/ASX 200	-0.85%	-3.20%	11.3% pa	8.2% pa	6.2% pa
Healthcare	4.96%	21.8%	24.5% pa	20.6% pa	15.1% pa

An ageing population, government expenditure on healthcare growing at 2% to 3% above GDP growth, new technology, Australia having access to a world class health system and medical research infrastructure, a global market place for products, ideas and innovation – are some of the factors that have led to the performance of Australian healthcare stocks. Australia has global leaders in their fields – companies such as CSL, Cochlear and Resmed – and there aren't too many other industry sectors where we can make this claim.

Like the rest of the market, healthcare stocks have pulled back in price over the last couple of months. They are not cheap, however, they are certainly more attractively priced – and the long-term factors are still in place. Here are three of my favourite stocks to put on your shopping list for the next pullback.

1. Ramsay Health Care (RHC)

Australia's largest private hospital operator, Ramsay has been a superb performer on the ASX over the last several years (see chart below). More recently, it has diversified into the UK and France, completing the acquisition of Ramsay Générale de Santé on 1 July. Ramsay Générale de Santé is the largest private hospital group in France – Ramsay holds 50.9%.

Ramsay Health Care – September 2010 to September 2015

In the year to 30 June 15, Ramsay grew NPAT (net profit after tax) by 19% to $412.1 million, or its preferred measure, core earnings per share, by 20% to 196.6c. For the FY16 year, Ramsay is forecasting core NPAT and EPS growth of 12% to 14%.

On Friday's close of $60.98, Ramsay is trading at a 10% discount to the broker consensus target price of $67.05. Sentiment is marginally positive (four buys/two holds/two sells). The multiple (27 times FY16 earnings) is high – with some brokers feeling that Ramsay is fully priced – however this is a company that has consistently met or exceeded its forecasts. On track record, a "must have" in growth portfolios.

	FY 16 Forecast	FY 17 Forecast
EPS Growth	21.9%	14.3%
PE Ratio	27.0	23.7
Dividend Yield	2.0% (F)	2.2% (F)

2. CSL Limited (CSL)

CSL is a global specialty biotherapeutics company. With major facilities in Australia, Germany, Switzerland, the UK and US, CSL employs 14,000 staff working in 30 countries. CSL has two main operating divisions – blood plasma products through CSL Behring – and vaccines and pharmaceuticals through bioCSL. CSL recently completed the acquisition of Novartis' influenza vaccine business, making CSL the second largest influenza vaccine manufacturer in the world.

In FY15, CSL grew sales by 7%, EBIT by 12% and NPAT by 10% (at constant currency and adjusting for acquisition costs). Reported NPAT of US$1.379 billion was up 6% on the previous period. For FY16, CSL is forecasting revenue growth of 7% (at constant currency), and due to an increase in investment and fixed asset depreciation, NPAT growth of just 5% (excluding the Novartis acquisition). With a further buyback foreshadowed, EPS growth is however expected to exceed NPAT growth.

CSL reports in US dollars. Almost 70% of its sales revenue is earned in the US and Europe. Like Ramsay, CSL has been a terrific share market performer.

CSL – September 2010 to September 2015

On Friday's close of $90.57, CSL is trading at an 11.7% discount to the broker consensus target price of $101.14. Sentiment is positive (six buys/one hold/one sell), and the multiple (20.8 for FY16, based on an A$/US$ of 0.7200 cents) is more respectable. Noting the lower growth forecast for 2016 and investment in the business, brokers see a return to the previous growth trajectory in 2017. A core healthcare stock.

	FY 16 Forecast	FY 17 Forecast
EPS Growth	n/a	12.6%
PE Ratio	20.8	18.5
Dividend Yield	2.0% (Unfranked)	2.2% (Unfranked)

3. Resmed (RMD)

Resmed develops, manufactures and markets products for the treatment and management of respiratory disorders, most particularly sleep apnea. With more than 4,000 employees, Resmed sells its products to approximately 100 countries through direct offices and a network of distributors. For FY15, revenue was US$1.7 billion, up 13% on a constant currency basis, with NPAT up 2% to US$352 million. Resmed does not forecast earnings and reports in US dollars.

While Resmed has been a strong performer on the ASX, it has also had its ups and downs and is a more volatile stock. For example, issues with the SERVE-HF clinical trial saw its share price tumble from over $9.00 to around $7.00 in April.

Resmed – September 2010 to September 2015

On Friday's close of $7.05, Resmed is trading at a 21.0% discount to the broker consensus target price of $8.53. Sentiment is marginally positive (four buys/two holds/two sells), and the PE for FY16 is down to 18.6.

Notwithstanding the significant discount to valuation, the brokers remain wary of competitor activity and the impact of this on sales and margin. A little more speculative, but worth the risk.

	FY 16 Forecast	FY 17 Forecast
EPS Growth	n/a	12.6%
PE Ratio	18.6	16.7
Dividend Yield	2.4% (Unfranked)	2.7% (Unfranked)

All charts sourced at*: Yahoo!7 Finance, 21 September 2015*

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Can 2015 end as a positive year for stocks?

by Peter Switzer

It's around 14 weeks until the end of this year and history said 2015 was supposed to be a good year for stocks, however, we started at 5411 on the S&P/ASX 200 index and we're now at 5140, so we're down 5%! But it wasn't always bad news, as on March 3, we were up 10.8%! So what happened and is there likely to be a turnaround before we start popping champagne on New Year's Eve?

And given the Fed's decision not to raise interest rates in September, does this help or harm the chances of stocks going up over the next two and a half months?

From my point of view, I was hoping the US central bank would raise its official interest rate, stocks would sell off for a short time, then value chasers would return to the market and long-term investors would focus on a US economy heading up. Wall Street would head up, we would follow suit and the usual December stock market rebound — the so-called Santa Claus rally — for us would kick in, and that often rolls into January and February.

What does the Fed interest rate delay mean?

There are those who say stocks should have gone up but US stock market indexes fell the day after the Fed's decision with the Dow Jones index down 290 points (or 1.74%) to 16,384.58. Given 18,351.36 was the all-time high, then the world's most watched market is in correction territory again, off 10.7%.

I remain in dip-buying mode and hope to get my pay-off before Christmas, but if this Fed delay means it happens early in 2016, then so be it. I believe in the post-rate rise process but its start date relies on Janet Yellen and her central bank buddies.

The delay also puts focus on how worried the Fed is about China and its impact on the global economy. I have to confess I am sweating on one or two things happening to help stocks. First, Beijing comes up with a stimulus package that really wows stock market players. Second, the previous stimuli kicks in and we start seeing some better Chinese economic data as we head towards year-end. Of course, if this doesn't show until 2016, then it could mean stocks will be volatile in a zone around 5000-5200 for the S&P/ASX 200 index, but so be it.

But a breakout to the high side will come. The numbers experts think fair value is at least 5400 or higher and both of my TV charts guys — Lance Lai and Gary Stone — say their technical analysis is positive for stocks down the track.

More Fed points

What else can I say following the Fed decision? Try these observations:

- CNBC's Jim Cramer expected a 500-point fall if rates had gone up but I don't agree with the magnitude of the drop, though it would create a great buying opportunity for sure. That said, no rate rise, provided it's not seen as a reason to doubt the US recovery, should help stock prices in coming months.
- If the Fed raises in December and when, say China data improves and/or a new stimulus package comes, then we could see a triple bunger reason for stocks to spike in December! This is my big hope for a Christmas present for all of us in the wealth-building game via stocks.
- The avoidance of a rate rise could make people believe that a recession could be in store. There are those who think China could cause it and while I think the next global recession is a way off, the reluctance shown by the Fed could fuel the fire of those

doomsday merchants who have been wrong since 2009. For history buffs, in the US, a recession has come as early as 11 months after the first rate rise and as long as 86 months later.

- Against this negativity, you can't be serious in thinking the first interest rate rise from virtually zero will end the bull market, so it is only logical that stocks still have a way to go upwards, unless a huge curve ball event completely turns around confidence.
- Anyone trying to justify Janet Yellen's decision could point to low inflation, low wages growth and a much stronger greenback over the past year, which is really like an interest rate rise. So as long as the US economy keeps showing good growth, the whole waiting for an interest rate rise anxiety might be unnecessary.
- In case you missed it, 13 out of the 17 Fed members have been surveyed and they expect a rate rise before 2016.

Conclusion?

We're in the hands of China and the global economy. I expect the up and down volatility we have been seeing recently to continue until some big news — hopefully positive — comes along to get the Fed to move. This will open up the probability that stocks will have a nice run up but until then, we're like Janet Yellen and we'll just have to play the waiting game.

For me, I am going to buy stocks that pay nice dividends every time the market wants to go excessively negative because I am still a strong believer in the long game. If you want some ideas, Simon Conn of Investors Mutual likes three smaller cap companies that pay good dividends — Steadfast, Shopping Centres Australia and Pact Group Holdings. These are the sorts of companies I am looking for — smaller cap companies, with good outlooks and a solid history of paying nice dividends.

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5 great stocks under $5

by James Dunn

Key points

- *Tatts is a strong source of earnings to have in your investment portfolio, and that is reflected in the healthy dividend yield.*
- *GBST Holdings is a little-known financial software business that is following in the footsteps of Computershare in becoming a global leader.*
- *While CSR did not offer earnings guidance for FY16, brokers expect another strong year, with further improvement in housing starts.*

With the August stock market slump still fresh in the memory, and the stock market down again today, there remain plenty of stocks still significantly cheaper – and yielding more – than they were at the end of July.

It's even better when these are good businesses with healthy prospects. Here are five such stocks, priced under $5.

Primary Health Care (PRY)

Consensus estimated FY16 yield 4.8% fully franked

The pathology, medical centres and imaging group has gone through what brokers considered a transitional financial year, which incorporated the departure, through ill health, of founder and managing director Edmund Bateman (who sadly passed away earlier this month), and a shock earnings downgrade in July that triggered a share price fall of 11%. That, and the August correction, have taken Primary back to levels the shares last touched in late 2012, but from here, the analysts that follow Primary see large scope for a recovery, with the consensus target price of $4.91 implying 22% upside.

The FY15 result – revenue up 6% to $1.6 billion, net profit up 3.9% to $119.1 million, dividend maintained at 20 cents – had been expected since the July downgrade. Management gave no guidance, with analysts expecting the company to clarify its FY16 expectations at the annual general meeting in November. But after a stoush with the Australian Taxation Office (ATO), Primary is expected to change its doctor remuneration model, which has traditionally been the upfront payment plus a 50:50 share of billings, and establish a new real estate investment trust (REIT) to provide a more efficient structure for the company to fund and operate its pipeline of new medical centres.

Earnings are predicted to be under pressure in FY16 but grow in FY17. Primary is trading on a consensus forecast fully franked yield of 4.8%, rising to 5.1% in FY17.

Tatts Group (TTS)

Consensus estimated FY16 yield 5.6% fully franked

The gaming and wagering giant fell more than 14% in the August correction, from $4.06 to $3.47, but managed to creep back to $3.61. At that price, Tatts' dividend expectations put it on a 5.6% fully franked yield for FY16. Tatts brought out a solid result for FY15, with earnings up 25% and the dividend up 22%: however, these results fell short of expectations because of a weak result in the wagering businesses. But the lotteries business did very well, and continues to vindicate the company's decision in 2005 to move into this area – the lotteries business now generates 60% of Tatts' earnings. The lotteries licences are long-life assets and give Tatts a highly dependable core earnings base. And analysts expect the rebranding of the wagering business as UBET – which was launched in April – to rejuvenate it.

There are digital threats to Tatts, but it is a strong source of earnings to have in your investment portfolio, and that is reflected in the healthy dividend yield. Analysts are looking for a consensus target price of $3.97.

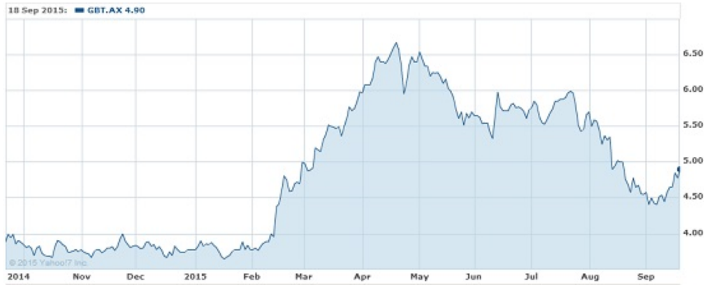
GBST Holdings (GBT)

Consensus estimated FY16 yield 2.4% fully franked

This little-known financial software business is following in the footsteps of Computershare in becoming a global leader. GBST's main products are the Composer funds administration and registry platform software, which it sells to the pension and wealth management industry in Australia and the United Kingdom, and its GBST Syn~ capital markets platform, provides new-generation technology to process transactions in shares, derivatives, fixed income products and managed funds. In Australia, GBST also offers the GBST Shares platform, which is the country's most widely used middle- and back-office system.

GBST was hammered in August, losing 22% to $4.41. The shares have recovered somewhat, but still give investors an opportunity to buy into an emerging global leader at a good discount. In FY15 the company lifted revenue by 16%, net profit by 52% and its fully franked dividend by 24%. This year will see heavy investment and mounting costs as GBST looks to lock-in potential new business in Asia, Japan and the US – the latter of which is going to be both (a) tough to crack, and (b) potentially transformative.

This investment load means that GBST is a relatively miserly dividend payer, with 2.4% fully franked expected this year and 2.7% in FY17. But broker Morgans sees the stock reaching $6.10, which is about 25% higher than the current price.



CSR (CSR)

Consensus estimated FY16 yield 6.8% unfranked

Building materials company CSR lifted its FY15 result ahead of market expectations, buoyed by strong Australian residential construction activity, particularly on the east coast. CSR's range of building products includes Monier roof tiles, Hebel high-performance masonry, Gyprock plasterboard, Bradford insulation systems, Edmonds ventilation products, PGH bricks and pavers and Viridian glass (the only Australian manufacturer of architectural glass). CSR also owns 36% of the Tomago aluminium smelter, near Newcastle in New South Wales.

While CSR did not offer earnings guidance for FY16, brokers expect another strong year, with further improvement in housing starts. The company believes the housing market should remain strong until FY17, given that the lag between approvals and completions is now nine months. The future of aluminium – which was a strong performer in FY15 – may weigh on some investors, but as broker Macquarie points out, Tomago represents less than one-fifth of CSR's market valuation.

CSR lost almost 20% in the August rout, but is up from its low point, and is now priced on an (unfranked) expected yield of 6.8% in FY16, rising to

7.7% in FY17. The analysts' consensus target price of $4.17 would represent a very nice 28.6% gain from here, if achieved.

Mortgage Choice (MOC)

Consensus estimated FY16 yield 8.4% fully franked

Mortgage and loan broker Mortgage Choice entered August at $2.28 but then fell as low as $1.89. The housing recovery is clearly a plus for Mortgage Choice. Home loan approvals in April hit their highest level since October 2009, when the boosted first-home-owner grants were coming to an end, but new lending restrictions from the regulator APRA – aimed at dampening investment levels – have had an impact more recently.

Mortgage Choice's share price slipped on the back of this, despite the company's low exposure to investment loans. Broker Macquarie believes market concerns over tighter APRA mortgage controls have been overblown. With that out of the way, continuing strength in Australian housing, and cost controls, should be able to drive further earnings growth – which is expected to be double-digit percentages both in FY16 and FY17.

At present, on current dividend expectations, the share price fall has pushed MOC to a fully franked prospective dividend yield of 8.4% in FY16 and 8.5% in FY17. The analysts' consensus target price of $2.91 implies significant upside potential.

Adding further interest to MOC is the fact that Commonwealth Bank owns just over 20% of the stock, and could move to take control as it did with Aussie Home Loans in 2012.

***All charts sourced at**: Yahoo!7 Finance, 21 September 2015*

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Buy, Sell, Hold – what the brokers say

by Rudi Filapek-Vandyck

Overall activity from stockbroking analysts has quietened down a lot in September as the seasonal lull in between a busy reporting season and the upcoming AGM season is often taken as an opportunity to chill out and maybe even enjoy a short holiday.

We find positive movements for TPG Telecom in anticipation of yet another solid financial result, and as analysts start incorporating contribution and synergies from the acquired iiNet operations. Upmarket retailer, OrotonGroup, attracted one upgrade post its results.

Upgrades

Order	Company	New Rating	Old Rating	Broker
1	Beach Energy	Buy	Neutral	Macquarie
2	Drillsearch Energy	Buy	Neutral	Macquarie
3	OrotonGroup	Neutral	Sell	Citi
4	Rio Tinto	Buy	Neutral	UBS
5	TPG Telecom	Buy	Sell	Citi
6	Transurban Group	Buy	Neutral	Citi
7	Woodside Petroleum	Neutral	Sell	Macquarie

In the good books

BEACH ENERGY LIMITED (BPT) was upgraded to Outperform from Neutral by Macquarie Buy/Hold/Sell: 3/3/1 Macquarie has cut its Aussie forecasts by 8-9% to US63c in 2016, US67c in 2017 and US75c long term. Domestic oil and gas producers reporting in Aussie see a net 37% earnings forecast upgrade as a result, albeit for some this is offset by US dollars costs. The broker's sector multiple has risen as a result, as has the broker's rating for Beach.

OROTONGROUP LIMITED (ORL) was upgraded to Neutral from Sell by Citi Buy/Hold/Sell: 1/2/0 FY15 was a very painful exercise for Oroton, but FY16 should be a significantly better with earnings before interest and taxes expected to nearly treble (from arguably a low base). Citi has set a new target price of $2.55 (was $2.10). The company has its currency exposures hedged and Citi believes the pressure on margin experienced in the year past should not repeat itself this year.

TPG TELECOM LIMITED (TPM) was upgraded to Buy from Sell by Citi Buy/Hold/Sell: 3/1/2 The sector is readying for the grand broadband battle in coming years and Citi analysts have come to the conclusion that TPG Telecom is ready for it. Helped by the acquisition of iiNet the broker is anticipating EPS compound annual growth rate of 30% to FY18. At face value, migrating to NBN Co, away from Telstra copper, means higher access costs and lower gross margins, but Citi believes TPG management can offset this.

In the not-so-good books

BILLABONG INTERNATIONAL LIMITED (BBG) was downgraded to Neutral from Overweight by JP Morgan Buy/Hold/Sell: 0/3/0 JP Morgan suspects the trading environment in the company's biggest market, the US, has worsened, based on the results from rivals. Despite the ongoing turnaround story, the risk/reward proposition is not deemed compelling enough to become more constructive on the stock at this time.

Downgrades				
Order	Company	New Rating	Old Rating	Broker
1	Billabong International	Neutral	Buy	JP Morgan
2	Origin Energy	Neutral	Buy	Citi
3	Regis Resources	Neutral	Buy	Credit Suisse

Earnings Forecast

Positive Change Covered by > 2 Brokers						
Order	Symbol	Company	New EF	Previous EF	Change	Recs
1	KAR	Karoon Gas Australia	-12.02	-6.96	72.70%	6
2	GRR	Grange Resources	2.00	1.67	19.98%	3
3	AWE	AWE	-3.54	-3.15	12.49%	7
4	RRL	Regis Resources	16.78	15.07	11.33%	8
5	MQG	Macquarie Group	568.00	555.29	2.29%	6
6	TPM	TPG Telecom	30.37	29.78	1.96%	6
7	TGR	Tassal Group	30.00	29.67	1.12%	3
8	BHP	BHP Billiton	90.50	89.63	0.97%	8
9	JHX	James Hardie Industries	74.57	73.97	0.80%	7
10	MYO	MYOB	14.77	14.65	0.80%	3
Negative Change Covered by > 2 Brokers						
Order	Symbol	Company	New EF	Previous EF	Change	Recs
1	SXY	Senex Energy	0.99	1.25	-20.69%	7
2	NWS	News Corp	61.56	68.20	-9.73%	6
3	IGO	Independence Group NL	36.05	39.63	-9.01%	7
4	BPT	Beach Energy	6.75	7.33	-7.89%	7
5	A2M	The a2 Milk Company	0.59	0.63	-7.44%	3
6	DLS	Drillsearch Energy	8.62	9.25	-6.78%	6
7	AWC	Alumina	10.11	10.53	-3.99%	8
8	OSH	Oil Search	30.95	32.05	-3.44%	8
9	IRE	Iress Market Technology	38.64	39.77	-2.83%	4
10	STO	Santos	19.33	19.81	-2.42%	8

FNArena tabulates the views of eight major Australian and international stock brokers: BA-Merrill Lynch, CIMB, Citi, Credit Suisse, Deutsche Bank, JP Morgan, Macquarie and UBS.

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Super Stock Selectors – Telstra, TEN and energy

by Penny Pryor

Given our rough day on the market, let's start off with our dislikes. Morgans managing partner, Raymond Chan doesn't like Myer. He's got something in common with Roger Montgomery there, who last week posed the question of whether the company's equity raising was just throwing good money after bad .

"The market position of Myer, the inflexibility of the department store format, and the increasing competition for the high-end consumer suggests that the end result is more likely to be weaker than management's target," Montgomery said.

Also on the dislikes, Michael McCarthy doesn't like Blackmores. He says it's not about the company, but about the share price and the "eye-watering highs" it's been hitting lately.

At around $137 a share, Blackmores's market capitalisation is $2.4 billion dollars, compared to a record full year profit of $46.6 million.

"Good growth story, but the share price has lost touch with reality (in my opinion, largely due to a lack of tradeable shares – a few large shareholders dominate). Sell now to buy back cheaper, later," McCarthy says.

When it comes to likes this week, we don't have much. Raymond Chan likes Telstra and Evan Lucas likes Woodside and Oil Search in the energy sector.

Evan says we should see an increase in the oil price over the coming month. "This is a seasonality event as the northern hemisphere drifts into winter and the consumption of heating oil and gas ramps up. Considering the high level of shorting and the mass selloff in this space over the last year, it's likely to see some buying in the short term."

Michael McCarthy says he likes TEN but he only means as a very short-term trade as traditional media remains under severe pressure.

"However, a surprising acknowledgement by the ACCC of potential damage to TEN if the Foxtel purchase is disallowed, and the potential for changes to media ownership laws, mean there may be a "pop" in TEN's share price. Not a core holding, but a short-term opportunity to possibly juice up portfolio returns."

Expert	**What stock I like**	**What stock I don't like**
George Boubouras, chief investment officer at Contango Asset Management	Sydney Airport Holdings (SYD)	
Raymond Chan, managing partner, Morgans	Telstra (TLS)	Myer (MYR)
Elio D'Amato, CEO Lincoln Indicators	Spark Infrastructure Group (SKI)	Beach Energy Limited (BPT)
Tony Featherstone, financial journalist	Qube (QUB) and Aurizon (AZJ)	
Evan Lucas, IG Markets analyst	Energy sector - prefer Woodside Petroleum (WPL) and Oil Search (OSH)	Concerned for emerging market indices and the ASX
Michael McCarthy, Chief Market Strategist, CMC Markets	Ten Network Holdings (TEN)	Blackmores (BKL)
Roger Montgomery, chief investment officer, Montgomery Investment Management		Myer (MYR)

Our Super Stock Selectors is a survey of prominent analysts, brokers and fund managers. Each week we ask them to name a stock they like, and one they don't like. We purposely ask for 'likes' and 'dislikes' instead of recommendations, so it provides an idea of what the market is looking at, rather than firm buys or sells.

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