Switzer Super Report
Advice you can trust

Thursday 19 May 2016

Radio star

The Internet is obviously playing a major part in the election campaign and media frenzy trying to catch the eyeballs of potential readers and viewers. But what about "old world" media like TV, print and radio? Today, Charlie Aitken says radio and outdoor advertising are going from strength to strength, and analyses Southern Cross Austereo in particular.

Also in today's *Switzer Super Report*, Tony Featherstone has four New Zealand companies that are listed on stock exchanges both sides of the Tasman. Plus, June 30 is just over a month away, so Tony Negline reveals his tax tips for SMSFs.

Sincerely,

Peter Switzer

Inside this Issue

Southern Cross Austereo: tune in to a 6%ff yield
by Charlie Aitken
02

switzersuperreport.com.au

Switzer Super Report is published by Switzer Financial Group Pty Ltd AFSL No. 286 531
36-40 Queen Street, Woollahra, 2025
T: 1300 SWITZER (1300 794 8937) F: (02) 9327 4366

Southern Cross Austereo: tune in to a 6%ff yield

by Charlie Aitken

Today, I thought I'd challenge the conventional belief that all "old world" media is going the way of the dinosaur.

No doubt print media and parts of free-to-air TV are facing substantial structural headwinds from Netflix, Twitter, Facebook etc. That is well-known and most likely discounted into the relevant stocks.

What is less recognised is that radio and outdoor advertising is going from strength to strength. Yes, we do still listen to the radio in the car (or in the tractor) and look at outdoor billboards as we drive along.

Interestingly, despite different growth drivers, all "old world" media has been tarred with the same "structural headwind" brush in terms of P/E. That is why my investment team and I have been scouring through the trading damage, looking for mispriced "old world" media assets that will actually deliver both earnings and dividend GROWTH over the next few years.

The stock we have recent bought after doing our sector research is Southern Cross Austereo (SXL $957 million market cap). This mid-cap industrial is undervalued in our opinion and its sustainable fully-franked dividend alone should support it at current prices.

We see 5 clear catalysts that should lead to SXL being re-rated

1) Net debt is down to $350m, so this stock is no longer highly geared. They also have $100m of franking credits and with the corporate tax rate changes, no point keeping them from shareholders.

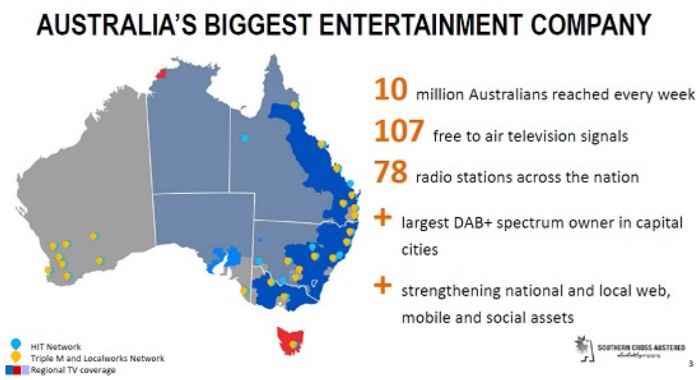
2) They will now be selling Nine product not the third ranked Ten product on their regional TV networks.

3) In my view, much like how the outdoor ad segment has grown share significantly, I feel radio could see a similar uplift from its current share circa 8% of advertising spending.

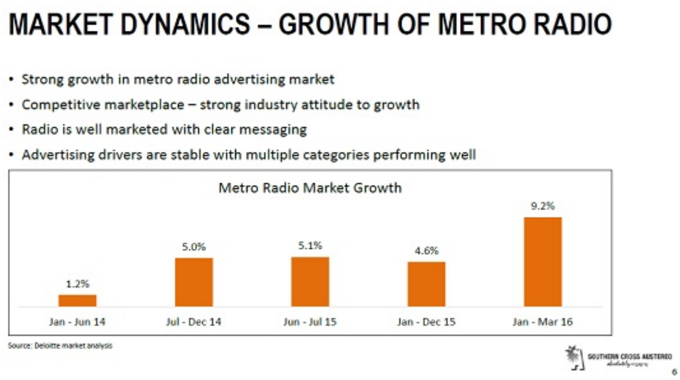
4) I think there is zero chance SXL has interest in buying NEC. Could NEC bid for SXL to diversify away from free-to-air more? Sure, NEC owns 9.9% of SXL already.

5) SXL own around 67 transmission towers. These could prove attractive to infrastructure funds, just like how they value mobile phone towers on big prices.

Let's start by looking at what SXL is.

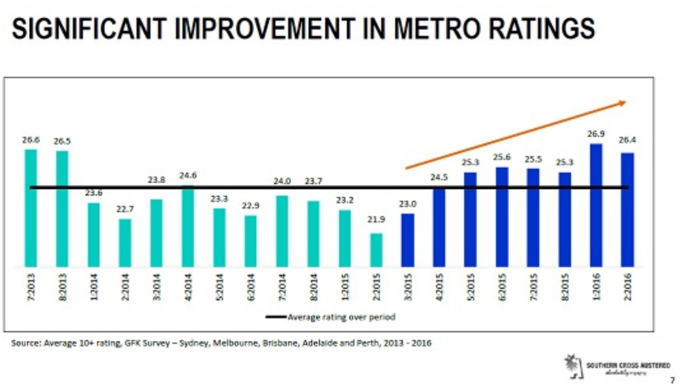


Click here to download a larger image



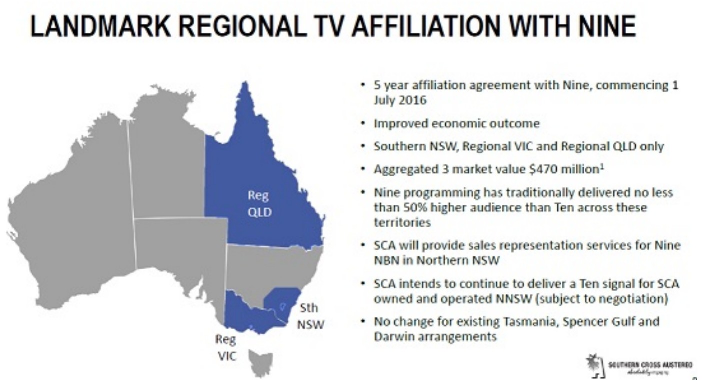
Click here to download a larger image

The clear attraction is SXL are generating strong metro ratings, which leads to a greater revenue share of a growing overall marketplace in radio.



Click here to download a larger image

The most interesting and positive strategic development for SXL was a new broadcast affiliation deal with Nine (NEC).



Click here to download a larger image

Our analysis of this deal is it's a win/win for SXL and NEC, but more so for SXL. In the short-term it leads to us upgrading our FY17 forecasts for SXL by +3%. Sure, not much, but its growth in what is considered and priced as a "growthless" industry.

Click here to download a larger image

NEC & SXL have formed a new affiliation agreement in the regional QLD, Southern NSW and regional Victorian markets. The deal means SXL with broadcast Nine's metropolitan content in these three regional markets for the next five years from July 1st. In return, SXL pays Nine an affiliation fee of 50% of its TV advertising revenue. Also, as part of the agreement SXL will also provide sales services for Nine's NBN channel in Northern NSW and NTD9 in Darwin. Nine and SXL will also pursue other opportunities to mutually grow their businesses (you can see why I think a merger is likely eventually). Before this deal, Nine provided content to WIN Corporation in these regional markets, while SXL broadcast TEN product.

The consensus analyst view of the new agreement is that the switch in affiliation in these three markets will result in a revenue uplift of $55m in FY17 due to high ratings/revenue share from Nine's content. To put this in context, pre the new deal, SXL's revenue share in these three markets was 21% versus WIN's 30%.

Obviously, costs rise too in the first year and analysts estimate the incremental expenses to be up around $50m in FY17 due to the higher affiliation fee (50% versus 30% with TEN), an increase in variable costs due to higher revenue share, and an increase in employment costs due to a larger sales force.

This all translates to EBITDA estimates being increased by +5% to +7% over FY17-FY18, and I would state that we are using conservative revenue and cost estimates. I think these EBITDA upgrades will prove conservative as the deal proves itself through time.

This all translates to a FY17 P/E of 10.4x and dividend yield of 6.3%ff. EV/EBITDA is a cheap 6.9x FY17

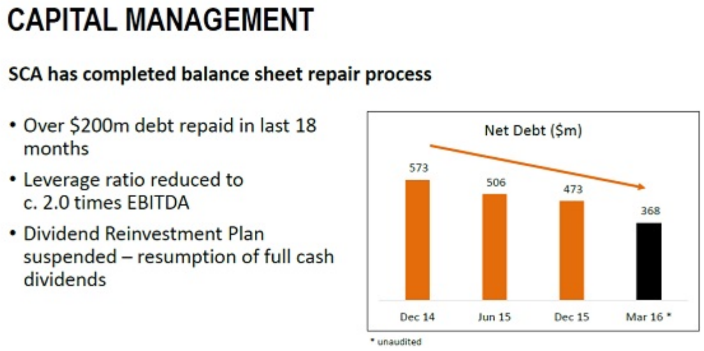
Southern Cross Media Group Limited (Reuters: SXL.AX, Bloomberg: SXL AU)

Year-end Jun (A$)	FY14A	FY15A	FY16E	FY17E	FY18E
Revenue (A$ mn)	641	611	632	703	719
EBITDA (A$ mn)	188	163	163	166	170
Net Profit (A$ mn)	(296)	(285)	77	78	81
EPS (A$)	(0.42)	(0.40)	0.10	0.10	0.11
P/E (x)	NM	NM	10.5	10.4	10.1
EV/EBITDA (x)	7.3	8.1	7.2	6.9	6.6
DPS (A$)	0.08	0.06	0.06	0.07	0.07
Dividend Yield	6.9%	5.6%	6.0%	6.3%	6.5%
Normalised EPS (A$)	0.11	0.09	0.10	0.10	0.11
Normalised EPS Growth	(5.6%)	(23.9%)	15.5%	4.1%	3.0%
Normalised PE	9.6	12.6	10.9	10.4	10.1

Source: Company data, Bloomberg, J.P. Morgan estimates.

Click here to download a larger image

It's also worth noting that SXL's balance sheet has improved dramatically and will continue too, making the dividend yield more sustainable. The DRP has also been suspended which is a good sign.



Click here to download a larger image

Putting this all together, we see the potential for solid, ground out, total shareholder returns from SXL over the years ahead. Broker valuations are around $1.35 but there's no reason to believe SXL can't head towards $1.50 while paying 6%ff along the way.

The technical picture also looks very encouraging with SXL about to break out of a well-defined trading range. Again, a technical breakout of this trading range would set the next technical target around $1.50.

Click here to download a larger image

We own SXL for a re-rating over the next few years. It's pretty hard to get de-rated from a P/E of 10x and pretty easy to get re-rated to 12x. The sustainable dividend yield alone at 6%ff pays us for the risk of owning the stock and in this new lower cash rate environment should underpin the stock at current prices. I would point out again consensus SXL earnings just got revised UP, which is highly unusual for an "old world" media stock.

In summary, we believe SXL will be re-rated for the following reasons. Momentum in Metro Radio ratings, potential regulatory changes over the next 12-18 months, and the improvement in Regional TV revenue share. "Tune in" for a 6%ff yield with the potential for capital growth.

Important: *This content has been prepared without taking account of the objectives, financial situation or needs of any particular individual. It does not constitute formal advice. Consider the appropriateness of the information in regards to your circumstances.*

Three NZ companies listed on both sides of the Tasman

by Tony Featherstone

New Zealand's economy, described as a "rock star" last year, is now being called a "one-hit wonder", as growth slows and interest rates are cut. But that has not stopped New Zealand companies raising capital in Australia and dual-listing on the ASX.

Forty-three New Zealand-based companies now trade on the ASX and more are on the way. Many have joined the ASX in the last few years through an Initial Public Offering (IPO). Volpara Health Technologies listed on the ASX last month and AFT Pharmaceuticals listed in December 2015 after raising $32 million.

The A2 Milk Company, Adherium, CBL Corporation, and Martin Aircraft Company listed on ASX in 2015 through IPOs. Evolve Education Group, Intueri Education, Orion Health Group and the fast-growing Vista Group International had IPOs in 2014.

The billion-dollar New Zealand energy privatisations, Mighty Power River and Meridian Energy, dual-listed on ASX in 2013 and Z Energy was another large NZ float that year.

More New Zealand companies are choosing to dual-list on the ASX to access capital from Australian fund managers, whose mandate requires them to invest in ASX-listed companies. Higher liquidity on the ASX compared with the NZX and funding diversification are other attractions.

I have followed several New Zealand-based IPOs over the past five years, notably Vista, CBL Corporation and Mighty River Power. The latter has occasionally featured in my reports for the Switzer Super Report on attractive income stocks.

Auckland International Airport looks fully valued after rallying this year and Kathmandu Holdings and Trade Me Group are interesting turnaround stocks. Restaurant Brands is another with good prospects.

Investors might have seen a trend in dual-listed New Zealand stocks when the country's economy was outperforming others in the OECD last year. A better approach is treating each company on its merits rather than basing investment decision on top-down economic trends.

I expect continued growth in NZ companies raising capital in Australia and listing on the ASX. New Zealand has a vibrant start-up culture, probably stronger than Australia's after adjusting for its size. Watch more New Zealand-based tech companies choose this market in coming years.

Here are three dual-listed New Zealand companies to watch on the ASX and one that is not dual-listed on our exchange (Restaurant Brands). I'll cover promising specialist insurance group CBL Corporation in a later column.

1. Trade Me Group (TME)

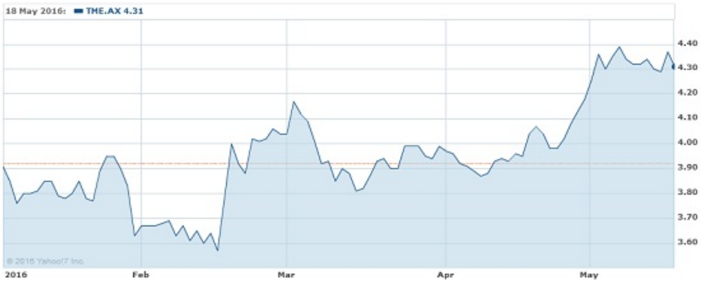
I nominated the online auction and marketplace services company in a column in early April on technology stocks for this report. To recap, Trade Me Group was spun out of Fairfax Media over 2011 and 2012.

It tumbled from $4.70 in April 2013 to $2.70 in August 2015 amid losses in market share and market concerns that more investment was needed to lift its performance. Trade Me has since rallied to $4.37 – it jumped about 10% in April alone – and has hit a five-year high.

I like Trade Me's prospects. It is through most of its capital-expenditure program, the core online auction business is going okay, and the online classified-advertising business has plenty of potential. The business is well run and trades on a forward Price Earnings (PE) of 19 times. That's a lot less than many of the larger internet advertising stocks.

Trade Me is due for a pause after strong recent share-price gains, but looks in good shape and is strongly leveraged to any improvement in the New Zealand economy.

Chart 1: Trade Me Group



Source: Yahoo!7 Finance

2. Kathmandu Holdings (KMD)

The former retailing star had a horrid 2014, plunging from $3.10 in August that year to $1.10. A savage drop in earnings, management changes, and concerns about Kathmandu's direction crunched its share price. Some of its store formats were too big, it relied too much on a handful of sales, and its product range had become tired and copied elsewhere.

Kathmandu has recovered to $1.39 after a better-than-expected half-year result for FY16 – still a long way from its previous high, but enough to restore some market sentiment. Sales rose 9.3% to NZ$196 million and underlying earnings (EBITDA) more than doubled to $21.9 million.

Kathmandu is considering selling its product in other channels, in addition to its stores. Several US leisurewear brands successfully sell their clothes in company-owned and franchised stores, department stores and other specialist retailers. Kathmandu is doing a good job of optimising its stores format, improving its pricing and promotions and relying less on big sales.

It's early days in the recovery strategy and Kathmandu has plenty of hard work ahead to regain market confidence. But its new management is off to a good start and the company still has a great brand and product and a valuable membership base through its Summit Club. The long-term theme of more people travelling and buying leisurewear is a positive.

Chart 2: Kathmandu Holdings

Source: Yahoo!7 Finance

3. Vista Group International (VGL)

Asian demand for Western cinema and entertainment is one of the more interesting trends. Chinese consumers could not get enough of the latest James Bond movie Spectre and superhero movies are super business in Asia. As tens of millions of Asians join the global middle class this decade, demand for cinema in the region will boom.

That's a strong trend for Vista, the New Zealand-based cinema software company that listed on the ASX through an $83 million IPO in August 2014. Vista has soared from a $2.15 issue price to $5.65, after comfortably beating prospectus forecasts.

Vista has a rapidly growing international footprint. Its software is installed in more than 4,500 cinema sites worldwide and it announced in March the sale of its Chinese subsidiary into a new venture owned by Vista and Weying Technology. Weying's online ticketing App is integrated into WeChat, the giant Chinese App that more than 600 million people use.

About three quarters of movie tickets in China are sold online through Apps, and Weying is thought to have a 15% share of this market. That relationship should give Vista a much stronger position in the

Chinese cinema market, which is on track to become the world's biggest box office before long.

Vista looks fully valued on most broker forecasts and is due for a share-price pause after strong gains this year. Any price weakness could be an opportunity to buy one of the more promising New Zealand companies and capitalise on the sweet spot of technology, entertainment and Asia over the next five years.

Chart 3: Vista Group International

Source: ASX

4. Restaurant Brands New Zealand (NZ: RBD)

The lack of fast-food stocks on the ASX is frustrating. Domino's Pizza Enterprises is priced for perfection, Collin's Food has rallied and Retail Food Group has disappointed. The New Zealand-listed Restaurant Brands is an option for those prepared to invest directly through the NZX. Restaurant Brands operates the New Zealand franchises for KFC, Pizza Hut, Starbucks Coffee and burger chain Carl's Jr. It serves about 60,000 customers each day in New Zealand.

The $556 million company has been a good performer: the one-year total shareholder return (including dividends) is 31%. The five-year average annual return is 22%. Restaurant Brands recently acquired 42 KFC stores in New South Wales. Macquarie Equities Research believes the company could own as many as 360 stores in Australia and likes its strategy to keep adding stores and create economies of scale. Restaurant Brands has plenty of balance-sheet firepower to fund acquisitions internally and has reasonably defensive qualities. At NZ$5.40, it should yield around 5%.

Macquarie values Restaurant Brands at NZ$6 a share and has an outperform recommendation. The median share-price target, based on a small consensus of broking firms, is NZ$5.53. Restaurant Brands trades on a forward PE multiple of about 18 times, consensus analyst estimates show.

I like the outlook for big fast-food brands as consumers eat out more, and Restaurant Brands can quicken its growth through continued acquisitions. It's a simple, lower-risk model: add one store after another, build a larger network, and create valuable synergies.

Chart 4: Restaurant Brands

Source: Yahoo!7 Finance

Tony Featherstone is a former managing editor of BRW and Shares magazines. This column does not make stock recommendations or offer financial advice. It does not take into account individual investor needs. Readers should do further research of their own or talk to their adviser before acting on themes in this article. All prices and analysis at May 18, 2016.

***Important**: This content has been prepared without taking account of the objectives, financial situation or needs of any particular individual. It does not constitute formal advice. Consider the appropriateness of the information in regards to your circumstances.*

Professional's Pick – Macquarie Atlas Group

by Hugh Cameron

How long have you held the stock?

We have held Macquarie Atlas Roads (MQA) in an overweight portfolio position for nearly two years, and have mentioned it before in this column (in February 2015) but thought it was worth revisiting, as a few things have changed.

What do you like about it?

We like it because it owns strategic stakes in a couple of "the world's best" infrastructure assets. Both are toll roads: one is in France and the other is in the USA. Both have long term toll concessions, with great growth potential in the traffic they carry, and the ability to increase tolls they charge, above the rate of inflation.

Where do you see the value?

We see value in its:

- relatively attractive investment multiples
- defensive style assets
- strategic positioning of its assets
- attractive distribution yield
- near term growth of over 10% pa over the next few years.

How is it better than its competitors?

We also like it because they don't really have any competition. They are essentially monopoly assets, which are great for investors to own. They only compete with older more congested, slower, less direct roads.

What do you like about its management?

Management is very focused on what they do, and they do it well. Currently the management teams are external to MQA, and there's a chance the company will restructure and internalise the management team, which we would see as a further positive for the stock.

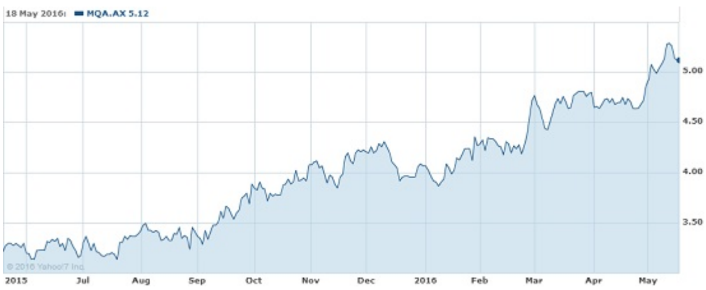
What is your target price? At what point would you sell it?

Our target price has lifted significantly, due to the traffic travelling on these roads being substantially higher in the last 12 months. Currently we value MQA at A$5.50.

How much has it added (subtracted) to your overall portfolio over the last 12 months?

MQA has significantly contributed to our portfolio over the last 12 months adding 51 basis points.

Macquarie Atlas Roads (MQA)



***Source**: Yahoo!7 Finance, 19 May 2016*
Hugh Cameron is a portfolio manager for Equity Trustees.
***Important**: This content has been prepared without taking account of the objectives, financial situation or needs of any particular individual. It does not constitute formal advice. Consider the appropriateness of the information in regards to your circumstances.*

End of financial year tax tips for SMSFs

by Tony Negline

Now is a good time to be considering what to before 30 June. What follows are some ideas:

1. Maximise Your Concessional Contributions

From 1 July 2017, the concessional contribution caps will fall to $25,000 for everyone. These are significant drops on the current amounts ($35,000 for those aged over 49 each 30 June and $30,000 for everyone else).

Remember that this applies to personal contributions that you can claim as a tax deduction and to all employer contributions, including salary sacrifice.

There are couple of points to note here – firstly, employers which borrow money to make super contributions can claim a tax deduction for their borrowing costs; secondly, you might be able to make concessional contributions in advance and claim a tax deduction for those contributions this year. This second point can be complex to implement and I would encourage you to read this article that describes how this works as well as receive some good advice from someone experienced in this area.

You should carefully consider your salary sacrifice arrangements and, if possible, look to rejig your circumstances to take into account the lower limit before it commences.

2. Split Contributions With Your Spouse

Effectively, this means taking your taxable contributions and moving them to your spouse's super account. Obviously it means your spouse's account increases whilst yours doesn't increase as quickly. There is a simple ATO form to complete to action this item, which your SMSF administrator can help you complete, if you have any questions.

I have been a proponent of this strategy for many years – I have personally done this for at least the last five years – primarily because I have seen little risk in using it and it potentially protects you against adverse government super and tax changes. It gives me no joy that I was right.

This strategy is particularly important for those likely to be impacted by the new $1.6 million pension limit (see below).

3. Transition to Retirement Pensions

As you would be aware from 1 July 2017, the government intends to remove the tax exemption for the earnings on assets supporting these pensions. This will mean that the earnings will be taxed at 15%.

If you're younger than 60, then your TtR income will be taxed at your marginal rate, less a 15% tax offset.

If you're over 60, then your TtR income is paid to you tax free.

When you include the 15% tax within the super fund, some people will find TtR pensions are no longer tax effective.

As a result, some will want to permanently retire.

Others will want to cease the pension and continue to work. If you're in this category then one option, for the 2016 and 2017 financial years, is to consider taking more income from these pensions than you might require so that it can be available, as income, for the 2018 financial year and potentially beyond. The idea is that you might be able to continue with your current strategy for some future years by taking more income now. Obviously you will need to do some careful analysis to work out what is best for you.

4. Non-Concessional (after-tax) Contributions – NCCs

This is a very tricky area. At present, the government wants to limit new non-concessional contributions to $500,000 and have all contributions made after June 2007 counted under this rule. If you were lucky enough to make NCCs of more than $500,000 before 3 May 2016, then you won't have to remove these contributions.

One option is to follow the Governments requirements because you would prefer to limit the potential for any hassle because contributions that breach these new rules will have to be taken out of the system.

Another option is to make contributions based on the current rules because you believe the government will have to water down its new policy. If we weren't caught in an election campaign, I suspect this might be a reasonably safe bet. In any event this is only a good idea if you accept that if the government does formalise this new rule as announced, then you might have to take the excess contribution out of the system or pay a penalty tax.

5. $1.6 million Pension Limit

This is a per-person limit and means that a couple can have a combined $3.2 million in pensions. From my discussions with many financial planners and accountants, this will probably generate adequate income for most people.

If you currently have pension account balances of more than $1.6 million, then you need to be planning to implement a strategy to reduce your pension balance by July 2017.

Where possible, you should consider rejigging the cost base of your investments. For example, suppose your pension has XYZ company shares in it and they were originally bought for $1 per share. They're currently trading at $10 per share. You have no desire to sell out of this company for the foreseeable future. At present, your pension fund can sell these shares and buy them back for $10 per share.

In this way, if those assets are then transferred back to the 15% tax phase, you will pay less CGT in the future because your cost base is lower, which means less tax to pay if they have to be sold in a taxed environment.

One option is to take money out of your pension and then contribute that money to your spouse's name – this might be a good idea if your spouse can make super contributions and it won't cause excess contribution cap problems for your spouse.

6. If you or your spouse has income under $37,000

There are two potential changes:

a. Right now, you might be eligible to have the super contributions tax – paid on employer contributions and personal contributions claimed as a tax deduction – refunded to your super scheme. This is currently called a Low Income Super Contribution and is due to cease before July 2019.

As part of the Budget, the Government has said this refund idea will continue but from 1 July 2017 will be called a Low Income Super Tax Offset.

This tax refund is sent automatically to your fund so there is nothing for you to do. One option, if you have the cashflow, is to try and maximise your concessional contributions this year and ensure your income is below the $37,000 threshold. The definition on income here including a number of items, such as your taxable income, reportable fringe benefits, some foreign income, tax free government pensions or other benefits and net investment losses.

The maximum tax refund paid here is $500.

b. Spouse super contribution tax offset – this is only available if your spouse earns less than $13,800 but from 1 July 2017, the income threshold will be increased to $37,000. It will pay a refund of 18% of contributions. The maximum refund is $540, meaning that it is payable on the first $3,000 of contributions if income is less than $10,800. A reduced maximum rebate is paid when income is between $10,800 and $13,800. It is only paid when a contribution is made for a spouse.

This is one concession you might want to remember if you're wanting to split benefits with your spouse. This is paid based on assessable income for income tax purposes – yes, this is a different definition of income to that mentioned just above.

If your spouse has low income then this can provide a small added incentive which you might like to access.

Important*: This content has been prepared without taking account of the objectives, financial situation or needs of any particular individual. It does not constitute formal advice. Consider the appropriateness of the information in regards to your circumstances.*

Buy, Sell, Hold – what the brokers say

by Staff Reporter

In the good books

Ainsworth Game Technology (AGI) Upgraded to Neutral from Underperform by Macquarie B/H/S: 1/1/0

Subject to approval, Novomatic will acquire Len Ainsworth's 53% stake in Ainsworth Gaming, helping to boost the company's market share and making new pokie titles available, as well as enhancing R&D, Macquarie notes. The broker sees the benefits of the sale as outweighing the negatives. Having also adjusted for A$ moves, Macquarie has lifted its Ainsworth target to $2.63 from $2.10 and as a result, upgraded to Neutral.

AWE (AWE) Upgraded to Accumulate from Hold by Ord Minnett B/H/S: 4/2/1

AWE has rejected the bid from Lone Star Japan at 80c a share. This is the right decision in Ord Minnett's view. As share prices of oil and gas companies are depressed, to offer anything other than a substantial premium is not expected to excite shareholders and boards.

Ord Minnett notes the balance sheet is in good shape and, short of an improved offer, believes the company should maintain its current strategy.

Beacon Lighting (BLX) Upgraded to Add from Hold by Morgans B/H/S: 1/0/0

Beacon Lighting has signalled softer trading over the past 10 weeks. Morgans suspects irrational competitor pricing contributed as well as consumers trading down in price points within the lighting category, which is related to sentiment.

FY16 earnings guidance is $28.2-29.2m, 11% below the broker's forecasts, which are downgraded accordingly. Still, Morgans believes most of the drivers of weakness will be short lived and the current share price presents an attractive accumulation point for a quality retailer.

Cochlear (COH) Upgraded to Equal-weight from Underweight by Morgan Stanley B/H/S: 1/5/2

The company's strategies to clear bottlenecks now gives Morgan Stanley more conviction that unit growth of 6.0% can be sustained.

The broker suspects it has been too cautious on the stock and an analysis of the installed bases and upgrade cycles has contributed to a valuation increase.

Integral Diagnostics (IDX) Upgraded to Outperform from Neutral by Credit Suisse B/H/S: 3/0/0

The company will purchase Western District Radiology and the 50% of South West MRI it does not own. Credit Suisse considers it a sensible deal, 2.5% accretive to FY17-18 forecasts.

Credit Suisse believes a short-term valuation gap emerged and upgrades to Outperform from Neutral.

Mirvac Group (MGR) Upgraded to Outperform from Neutral by Macquarie B/H/S: 3/2/1

On the back of the broker's economics team's reduced interest rates forecasts, Macquarie notes lower rates are a positive for the REIT sector and traditionally lead to sector outperformance against the market.

Sonic Healthcare (SHL) Upgraded to Neutral from

Underperform by Credit Suisse B/H/S: 4/3/1

The Australian government has announced an agreement with Pathology Australia. Legislation will be enacted to improve collection centre rents to counter the removal of the bulk billing incentive.

Credit Suisse previously incorporated the cuts to the bulk billing from the MYEFO and now reduces the rental expense, reversing out the benefits from the patient co-payments. This results in FY18 earnings upgrades.

In the not-so-good books

Alacer Gold (AQG) Downgraded to Hold from Buy by Deutsche Bank, and to Equal-weight from Overweight by Morgan Stanley B/H/S: 2/2/1

The company has approved Copler sulphide project and the larger plant, while a simpler design, will take longer to ramp up. Better grade and recovery, however, lift Deutsche Bank's output estimates over the life of the project.

Whilst Deutsche Bank likes the Copler mine it is wary of the company's investment appeal, as near-term production is declining, and there is an intensive capital build approaching.

For Morgan Stanley, the lower 2017 output from the oxide development creates a larger earnings dip, in the broker's view, but near-term exploration success may fill this. Attributable gold production was down 30% quarter on quarter in the March quarter, as expected.

Insurance Australia Group (IAG) Downgraded to Neutral from Outperform by Credit Suisse B/H/S: 1/7/0

The stock has been the best performer in the large cap insurers, Credit Suisse observes. Challenges remain but the broker considers the FY16 earnings margin remains attractive and IAG should meet, or exceed, its guidance.

While the positive theme continues and the broker does not consider the stock expensive this is now factored into the share price.

G.U.D. Holdings (GUD) Downgraded to Neutral from Buy by UBS B/H/S: 1/4/0

The stock has appreciated sharply since February as the company moves its focus to the automotive aftermarket. UBS is positive about the higher proportion of earnings coming from this division post the BWI acquisition and encouraged by the recent sale of Sunbeam. Margins may drift lower but positive industry dynamics should support volumes and prices, the broker maintains.

JB Hi-Fi (JBH) Downgraded to Hold from Accumulate by Ord Minnett, and to Neutral from Buy by UBS B/H/S: 2/6/0

Following the recent strong share price performance, Ord Minnett downgrades to Hold from Accumulate. The broker believes the upside from Dick Smith's demise has been well incorporated and the medium-term growth drivers are riskier.

Ord Minnett does not believe the stock offers compelling valuation support at current levels but forecasts strong growth in the near term.

UBS observes the share price has risen 36% from its November lows when the market became concerned about risks associated with discounting at Dick Smith. Despite the pressure, UBS observes trading has been strong and JB Hi-Fi should benefit from industry consolidation and the continued roll out of Home.

National Australia Bank (NAB) Downgraded to Neutral from Outperform by Macquarie B/H/S: 2/5/1

Macquarie observes the historical valuation discount to peers has largely unwound in recent months and considers it justified based on the underlying earnings performance.

Earnings growth is expected to be affected by a reduction in insurance earnings and convergence in impairment charges. With limited upside envisaged from current levels the broker downgrades to Neutral from Outperform.

Pact Group (PGH) Downgraded to Hold from Buy by Deutsche Bank B/H/S: 1/3/1

Deutsche Bank considers the company's crate washing and pooling services agreement a positive, as it extends the existing materials handling business and is underpinned by a long-term contract.

The broker estimates it should be 6.0% accretive in FY18. Deutsche Bank downgrades to Hold from Buy as the stock is trading at a 1.0% premium to its revised valuation.

Seven West Media (SWM) Downgraded to Sell from Hold by Ord Minnett B/H/S: 3/1/2

As a result of reducing metropolitan free-to-air TV advertising market forecasts Ord Minnett lowers FY16 and FY17 earnings estimates by 4.1% and 5.8% respectively.

While operationally Seven is considered the best in the business, with highest revenue share and earnings margin, the broker believes it is not immune to the industry and structural trends.

TEN (TEN) Downgraded to Sell from Lighten by Ord Minnett B/H/S: 1/3/1

Ord Minnett updates forecasts to reflect a reduction in metro free-to-air TV advertising forecasts. Ten Network's revenue share estimates are increased to 24.5% from 24.0%.

FY16 earnings forecasts are unchanged but the broker increases the forecast FY17 loss to $33m from $24m.

Tox Free Solutions (TOX) Downgraded to Neutral from Outperform by Macquarie B/H/S: 2/3/0

Chevron has started a process for expressions of interest for provision of waste management services at its WA assets. Tox Free has an existing contract until 2020.

Macquarie expects the most likely outcome of the re-tendering is that Tox Free will eventually retain the business, but at lower margins. The broker adjusts FY17 estimates to account for this scenario.

Given the overhang of the contract on the stock Macquarie downgrades to Neutral from Outperform.

***Important:** This content has been prepared without taking account of the objectives, financial situation or needs of any particular individual. It does not constitute formal advice. Consider the appropriateness of the information in regards to your circumstances.*

Questions of the week – Service Stream and Isentia

by Questions of the Week

Question: What do you think of service stream and what would be a good valuation to sell?

Answer (by Paul Rickard): Service Stream (ASX:SSM) has certainly gone through a purple patch over the last 12 months or so, in part due to its contracts with the NBN.

If you were thinking about getting on board now, I would be a little concerned as the train may already have left the station.

Valuation to sell at? The only broker I can find that covers the stock is Ord Minnett, who has a target price of $0.95.

There is an old saying in markets that you never go wrong taking a profit – my sense is that you may do some now and then sit back and stay along for the ride.

Question: How do you rate Isentia? I'm looking for a growth prospect for long term Self Managed Super Fund investment.

Answer (by Paul Rickard): I like Isentia (ASX Code ISD) as a business. The stock has done pretty well since the IPO. It probably got a little overbought late last year, but since pulling back, it seems to be finding a base again. They recently reconfirmed guidance for revenue to be up 22% to 24% on FY15 and EBITDA to be up 18% to 25%.

The brokers also like it. According to FN Arena, the consensus rating is +0.7 (scale is -1.0 is most negative to +1.0 most positive), with a consensus target price of $4.42.

It's trading on reasonably heady multiples of 22.7 x FY16 earnings and 20.1 x FY17 earnings.

Important: *This content has been prepared without taking account of the objectives, financial situation or needs of any particular individual. It does not constitute formal advice. Consider the appropriateness of the information in regards to your circumstances.*