September 2014

Investment Watch

Reporting season FY14: Cash is king

Stocks advanced through the August reporting season despite downgrades to FY15 earnings expectations and a cautious outlook from corporate Australia. This seems counter-intuitive, but the waves of dividends returning to shareholders is an amazing motivator for yield-hungry investors in a low interest rate environment.

The market was cautious heading into reporting season. It was trading about 10% ahead of the long term PE average multiples while expectations for FY14 earnings had been flat over the course of the year. This suggested that expectations were already low and that any misses would be treated harshly.

Large cap stocks avoided any nasty surprises, but delivered lacklustre FY14 earnings below aggregate expectations. EPS growth expectations for FY15 were downgraded to 6.3% (from 7.7%) compared with the 6.5% achieved in FY14. Company outlook statements were cautious and guidance was relatively vague. Analysts are clearly cautious about benign growth in Australia.

Despite this, stocks rose a further 1% through the reporting season and the market is now trading at 50% premium to its long term average PE. The explanation lies in the near record levels of cash dividends being paid to shareholders across the market.

With relatively weak revenue growth, 'cost out' has been the key to companies delivering positive earnings surprises. Reported operating cashflows surprised strongly to the upside, as companies deferred growth in favour of maximising productivity and returns on their existing invesments. Many are subsequently converting these into higher shareholder returns. Notable examples include Telstra, Wesfarmers, Suncorp, and BHP Billiton, Rio Tinto and the large cap oil stocks.

This wave of dividends met our expectations coming into reporting season. They also support our ongoing strategy to align with companies with dominant industry positions offering ongoing cashflow certainty and returns while interest rates remain low. However, we do note that many 'income' stocks are trading above their fundamental valuations and caution investors not to become complacent that yield will forever be the dominant market theme.

The payout ratio for the top 200 stocks is now approaching 75% which exceeds the peak achieved in 2009. Already we are seeing signs that companies need to re-invest into sustaining capex to underpin future earnings (e.g. Aurizon).

In the next few years we expect the market payout ratio to decline back to around 60% as demand for yield eases (global monetary policy normalises) and companies redirect cash into growth again. While we do remain aligned with 'Income investing' as the primary market driver, we do refer readers to the Morgans High Conviction Lists and Growth Model Portfolio which includes companies exhibiting genuine growth, which were also very strongly rewarded through reporting season.

S&P/ASX 200 payout ratio (12m forward)

Source: CIMB

Important disclosures regarding companies that are the subject of this report and an explanation of recommendations can be found at the end of this document.
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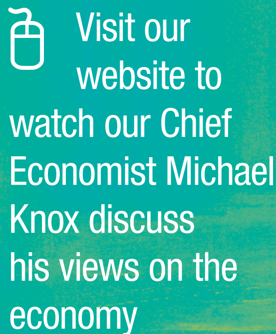

Economic Update

US, Europe, China, Australia

US

The US economy surprised on the upside, producing a 4.2% annualised growth rate for the second quarter of calendar 2014. This was sharply up from the negative growth rate of the first quarter. We think this rebound in growth will be sustained for the rest of 2014. Growth in the third quarter should come in at around 3.6% annualised. This recovery in growth will continue because of a surge in investment in information processing equipment, particularly computers and peripherals. We think that growth in this sector of computer equipment will grow around 17% annualised in the third quarter.

> "We think that the stronger US economy would generate a stronger growth environment for the Australian economy.

This surge in computer investment will happen at the same time as a surge in residential fixed investment. We think this sector will grow at 15% or better on an annualised basis in the third quarter. What we now have is a sustained investment-led recovery in the US. We think these relative high rates of growth will continue through to the end of calendar 2015.

Europe

Events on the Ukraine border with Russia have generated deep concern within European investment markets as indicated by an amazing rally in German 10 year government bonds (bunds) to a yield below 90 basis points. This is the lowest yield on German bunds since Germany was unified in the 1870s. We believe 90 basis points or less are unsustainable, driven by fear of disputes with Russia.

Our model suggests there is a very high probability of a collapse in German bunds. Our view is that one of the things that could precipitate that collapse is the beginning of the Targeted Long Term Refinancing Operation (TLTRO) about to be begun by the European Central Bank. This program will begin on 18 September. Under this program, the European Central Bank will lend up to a trillion Euros to European banks at the rate of 400 billion Euros per quarter. This money will be provided at a rate of 25 basis points for four years. The objective is to provide additional finance for German businesses so that they can in turn increase investment and lift employment.

China

The Chinese economy seems to have stabilised with a growth rate of 7.5% in 2014. This year retail sales in nominal terms seem to be rising at about 12.5%. Fixed asset investment in nominal terms seems to be rising around 17.7%. The Chinese refer to industrial production as "valued added of industry". This year, this measure of industrial production seems to be rising at a rate of 8.9%.

This continuing healthy growth is happening at a time when inflation is under control. Inflation this year is expected to run at around 2.4%, which generates a healthy profit for business in a situation where producer prices for manufactured goods are expected to fall by around 0.9%.

Australia

Most commentators have been surprised by the growth of the Australian economy this year. When the year started, the consensus for economic growth was only 2.8%. This is now risen to 3.1%. Still, forecasters remain pessimistic about 2015, whereby consensus growth is still only 2.8%.

We think that forecasters are too pessimistic again. We think that the stronger US economy would generate a stronger growth environment for the Australian economy. We continue to believe that economic growth in Australia for 2014 will be 3.0% and will accelerate in 2015 to 3.5%. Our 2015 estimate is 70 basis points higher than the consensus. We think that better growth in the US will generate a higher level of investment by American subsidiaries in Australia next year. This in turn will generate a surprise lift in the Australian economy.

Capital management – Investors demand cash

Prudent cost management and strong cash flow generation were dominant themes throughout reporting season. Those companies which converted these attributes into shareholder returns via surprise dividends or capital management were strongly rewarded. In an environment where interest rates look flat for the foreseeable future, these stocks are likely to continue to command premium ratings from investors.

Below we highlight the major capital management surprises announced through reporting season versus individual stock performance. We also flag several large cap companies which will continue to accumulate cash surpluses (e.g. the LNG developers) which bodes well for higher dividends or potential capital management at future results.

While the market's pre-occupation may currently be with yield, we did notice some subtle changes in language from companies which are clearly still weighing up their options – whether to return cash to shareholders or retain it to pursue growth (either organically or via M&A).

BHP is a good example. While the announced demerger (and lack of a Buyback) dominated the headlines, BHP quietly holds several billion dollars which it has not yet allocated toward either growth or shareholders. We think that companies reserving the right to consider investing in growth again is a good thing for economic growth. Just ask RBA Governor Glenn Stevens who recently said that a return of corporate optimism or 'animal spirits' are required to improve the real economy.

Stocks with current and future capital management potential vs performance

Total Return since Result		Comment
Origin Energy (ORG)	12.0%	To step-up dividend potential post APLNG ramp-up in FY16
Harvey Norman (HVN)	11.9%	To maintain an increased dividend 'as long as capital isn't required elsewhere'
M2 Group (MTU)	10.0%	Payout ratio at the upper end of guidance
Suncorp (SUN)	9.6%	Announced a higher Special Dividend than expected
Telstra (TLS)	6.5%	Announced an off-market Buyback and a higher dividend than expected
Aveo (AOG)	5.1%	Announced on-market Buyback
IAG (IAG)	4.5%	Payout ratio at the upper end of guidance
Downer EDI (DOW)	4.2%	Announced on-market Buyback
Woodside (WPL)	4.0%	Capital management under review – To balance with M&A and growth options
Santos (STO)	3.7%	Capital management under review – Expecting increased divs from FY16
Oil Search (OSH)	2.2%	Capital management under review – Expecting increased divs from the 2H
Wesfarmers (WES)	2.1%	Announced capital return in addition to a Special dividend
Rio Tinto (RIO)	-3.1%	Flagged capital management at the February result
BHP Billiton (BHP)	-7.5%	Deferred capital management until post de-merger
JB Hi-Fi (JBH)	-10.7%	Announced buyback but trading update disappointed

Source: Morgans, Bloomberg, Company reports

It is one thing to be clever and another to be wise

George R.R. Martin

Our Analysts discuss our High Conviction picks

Telstra – better off on market

Telstra's defensive earnings and a healthy dividend yield have turned it from an out of favour stock three years ago into a market darling with shares this month hitting a 13 year high. We have been big fans of Telstra, nominating it as one of our high conviction stocks into its August result which didn't disappoint. In FY14 Telstra reported its highest earnings per share figure it had reported in nine years and for the first time in nine years it raised its ordinary dividend. The 15c fully franked final dividend will be paid on Friday 26 September.

In addition to its good result, Telstra announced on off-market share buyback of up to $1bn. Telstra will give priority to shareholders with 925 or less shares. Generally speaking we don't believe TLS's buyback terms are attractive enough for most of our clients but we think it could work out well for smaller shareholders who are in retirement mode. For remaining shareholders, we estimate it should increase earnings per share by around 2% (due to the same profit being divided by a lower number of shares). Shareholders have been invited to tender into the buyback which opens on 9th September 2014. If you think the buy-back might be appropriate for you we recommend contacting your Morgans Advisor for further details.

Visit our website for the latest on **Telstra – There's more where that came from!** published 14 August 2014.

Proposed BHP demerger

With their full-year result, BHP announced its intention to de-merge its non-core assets into an as yet un-named new entity. The assets to be de-merged comprise of non-core assets in aluminium, coal, manganese, nickel and precious metals consisting predominantly of Australian and South African based operations.

After having assessed individual asset sales for the last 18 months, BHP now sees a de-merger as the best strategy to maximise shareholder value. BHP's rationale is twofold:

- to extract for shareholders the full value for these assets which it doesn't believe the market fully values within the larger BHP; and
- to allow BHP to focus on its existing 'pillars' in iron ore, petroleum, copper, coal and potentially potash which currently generate about 97% of the company's underlying EBITDA. BHP aims to further improve on productivity, costs and profitability from these assets and is targeting further cost savings of at least US$3.5bn by the end of FY17.

Following the anticipated completion of the demerger in mid-CY15, BHP will then reassess its capital management options under the simpler structure. It will maintain its current dividend at a minimum of current levels, and will well and truly be in a position to enact a share buyback by that date, if not sooner, in the absence of alternative growth options.

BHP frustrated yield seeking shareholders at its result by deferring its capital management into next year. However, we argue that leverage to global growth and commodities should be the primary reason for investing in BHP.

Nonetheless, existing holders will be entitled to 100% of the shares in the new entity through a pro-rata in-specie distribution by mid-2015, which in itself is a capital return. The entity itself will be interesting in its own right. "New-co" will be structured conservatively and will comprise of assets at the low end of their respective cost curves, offering upside through further optimisation and/or a recovery in commodity prices off their cyclical lows. BHP shareholders are set to receive both yield and leverage in the coming 12 months.

Visit our website for the latest on **BHP – Leaner or skinnier?** published 20 August 2014.

Retail – post reporting season review

Post a raft of downgrades across the retail sector in June, there were few major shocks from the retailers throughout reporting season (excluding Breville Group). Most companies believe that general trading conditions have improved following the initial budget sticker shock. However, few were confident enough to provide definitive FY15 guidance at this early stage. While FY14 results were broadly in line with expectations given the raft of downgrades across the sector in June, FY15 trading updates brought no major negative surprises.

As we expected, those retailers who are predominantly exposed to the housing sector provided the most resilient FY14 results and trading updates: Beacon Lighting, Dick Smith, Harvey Norman, Wesfarmers (Bunnings) and Nick Scali. The notable exceptions were: Breville Group (largely North American weakness) and JB-Hi-Fi (result in line, but July trading update very weak due to soft tablet sales).

The most impressive combination of result/trading update/guidance came from: Domino's Pizza, Ardent Leisure, Beacon Lighting and Burson Group. No surprises that these are also our preferred 'structural growth' stocks – all taking share in their respective growing markets. It also comes as no surprise that all of these stocks trade at a healthy multiple premiums.

In mid-September both Kathmandu and OrotonGroup are due to report. In our view, both these stocks look interesting from a valuation versus growth perspective. Kathmandu continues to stand out due to its strong growth prospects but undemanding valuation. The retirement of CEO, Peter Halkett, does cause us some concern particularly with the store rollout nearing maturity. Articulating a definitive offshore strategy is increasingly important for the group's longer term earnings growth. CFO and COO, Mark Todd, has been with the business for 16 years and will fill the position seamlessly in our view while a wider search is conducted. OrotonGroup is also looking interesting with strong earnings growth in coming years with the Gap rollout against the backdrop of a reasonable EV/EBITDA valuation.

We believe investors looking for retail exposure should consider **Ardent Leisure** and **Domino's Pizza** which have the most compelling long term growth options (5 year plus). While, the September results of **Kathmandu** and **OrotonGroup** could provide a catalysts to narrow the growth versus valuation gap.

Visit our website for the latest on **Retail – Post reporting season review** published 2 September 2014.

Raising for different reasons – QBE Insurance and Challenger Group

Whilst Suncorp Group (SUN) paid a healthy 30cps special dividend at its result, others in the Diversified Financial and Insurance sectors called on investors for further capital. These were **QBE Insurance** (raising to strengthen its balance sheet) and **Challenger Group** (raising to support the strong growth the company is experiencing).

QBE announced an equity raising of around $750m, which in combination with other capital initiatives such as divestments and a partial listing of QBE LMI will take QBE's gearing down to c30%. We think this has addressed market concerns around QBE's balance sheet, however investors should still be mindful that QBE has been in 'turnaround' mode for a number of years. A range of other strategic changes were announced including further re-insurance over 'long-tail' portfolios and a change to its investment strategy. Ultimately, given the complexity of QBE's business, it is impossible to know whether the Group has now solved all of its reserving issues, and whether it should be considered a higher risk/reward proposition relative to other Financials stocks.

Challenger Group (CGF) announced a $280m raising, adding further capital to support growth. Challenger reported 28% growth in retail annuities sales, the largest division for the group and 27% earnings growth in its up and coming Funds Management division. CGF is benefitting from a strong demographic tailwind (the aging population, looking for secure retirement income products). We believe this sets up a strong medium-term outlook for the company and hence we have added the stock to our High Conviction list this month.

Both QBE and CGF have Share Purchase Plans currently open.

Medibank Private

Proposed Initial Public Offer

Goverment announces intention to complete IPO by end of 2014

Morgans appointed a Co-Lead Manager to the IPO

Not for distribution in the US or to US persons

On 29 August 2014, Senator the Hon Mathias Cormann, Minister for Finance announced that subject to market conditions the Government has decided to proceed with the sale of Medibank Private through an Initial Public Offer in 2014.

The only details that have been released in respect of the proposed timing of the IPO are:

- **All Australians will be given the opportunity to pre-register for a Medibank Private Share Offer prospectus towards the end of September 2014; and**
- **The Government expects to lodge the Medibank Private Share Offer prospectus with the Australian Securities and Investments Commission in late October.**

Morgans is delighted to announce that we have been appointed a Co-Lead Manager to the proposed Initial Public Offering of Medibank Private.

Copies of the Minister's full announcements dated 5 August 2014 and 29 August 2014 can be viewed at www.financeminister.gov.au/media/2014.

There is no further detail at this stage, please feel free to contact your adviser if you would like more information in relation to the offer when it becomes available.

Nothing in this information should be construed as financial product advice or a recommendation to buy shares in Medibank Private Limited

Fixed Interest – the new issuance arrives

The anticipated new issuance finally arrived with the launch of the CommBank PERLS VII Capital Notes and the Challenger Capital Notes at the end of the month. Even prior to these announcements, a number of the securities highlighted in last month's Investment Watch saw price corrections as investors trimmed positions at what we viewed as expensive levels. We expect to see other issuers look to take advantage of this investor demand and continue to believe there is downside risk to a number of securities in the sector given elevated security pricing.

CBA issued $2.6b of CommBank PERLS VII Capital Notes under the bookbuild which was more than the $2.0b initially targeted. Due to this strong demand, the margin was set at 2.80% which was the bottom end of the 2.80% to 3.00% bookbuild range. The security will have an initial annual gross distribution rate of approximately 5.45% and is callable by the issuer in December 2022.

There continues to be significant demand from investors for new issuance and this saw the Challenger offer increased to $340m (from $250m) and pricing coming in at the bottom of the 340bp to 360bp bookbuild range. The initial gross distribution rate on the security will be approximately 6.05% and the security is callable by CGF on 20 May 2020. If not called by the Issuer, the security will mandatorily convert on 25 May 2022.

Visit our website for the latest on **CommBank PERLS VII Capital Notes – The Next PERL in the Chain** published 26 August 2014.

High Conviction Stocks

In the digitial edition, you may click on the stock tables for links to the latest company research reports from our website.

Top 100

This month's changes

This month have made several changes to our top 100 High Conviction list, removing Crown Resorts (CWN) and Transpacific Industries Group (TPI) and adding Challenger Group (CGF) and Origin Energy (ORG).

While the CWN share price has performed well since the company reported its FY14 result, the company's recent acquisition of a Las Vegas casino site; a Melco share price at 12 month lows; and the bidding for the Brisbane Casino development, has us question our position on CWN. We like the thematic, but given these issues facing the company, we remove the stock from our High Conviction list. We have also removed TPI after the company disappointed with a substantial increase in expected landfill remediation costs, disclosure on timing of landfill closures, and weaker-than-expected earnings in 2H14.

Brambles BXB			
Price	$9.43	PE (x)	21.0
Price Target	$10.02	Yield	3.4%
Upside	6.2%	Gross Yield	3.8%

Brambles (BXB) is a supply-chain logistics company operating in more than 50 countries, primarily through the CHEP and IFCO brands.

Key reasons to buy

- Long-term international growth opportunities from new products and emerging markets.
- It is leveraged to an economic recovery in the US and Europe (~80% of earnings). With organic growth forecast in those key markets we expect earnings growth to accelerate from mid-single digit to low double-digit.
- Its PE multiple (~21x FY15 at present) is marginally above the historical average of 18x, but well below previous peaks of 25x plus and we think BXB is entering a PE re-rating cycle.

Challenger Limited CGF			
Price	$8.08	PE (x)	12.9
Price Target	$7.76	Yield	3.6%
Upside	-3.9%	Gross Yield	3.6%

Challenger Limited (CGF) is an investment management firm focusing on retirement income products, in particular annuities. Challenger holds the dominant market share of annuities sales in Australia as well as operating a growing Funds Management division.

Key reasons to buy

- Annuities have strong tailwinds: CGF recorded 28% sales growth last financial year. The outlook for annuities sales remains strong over the medium-term, with a structural demographic shift (aging population); and the potential for positive regulatory reform and policy settings to to encourage the take up of retirement products.
- Funds management +27% growth in FY14: CGF's funds management division is one of the fastest growing managers with significant existing capacity.

CGF successfully raised $250m recently to fund growth. The stock trades on a relatively undemanding valuation at just under 13x FY15 PE.

CSL			
Price	$67.80	PE (x)	22.2
Price Target	$70.01	Yield	1.8%
Upside	3.3%	Gross Yield	1.8%

CSL is a leading global human blood plasma company which generates approximately US$5.0bn in sales (40% in US, 30% in Europe and 40% in the Rest of World).

Key reasons to buy

- CSL has delivered average EPS growth of 21% for the last six years and our forecasts suggest mid teen growth for the next three years.
- To fund its continued growth CSL spends over 5% (or A$0.5bn) of revenue on R&D, with most promising targets in the Haemophilia space.
- Although the current share price is higher than our fundamental price target, CSL offers investors with a medium term view attractive capital growth prospects.

Origin Energy ORG			
Price	$14.33	PE (x)	21.8
Price Target	$14.52	Yield	3.2%
Upside	1.3%	Gross Yield	3.2%

Origin Energy (ORG) is the leading Australian integrated energy company, which has diverse operations across the energy supply chain; from gas exploration and production to power generation and energy retailing.

Key reasons to buy

- Recent outlook statements for FY15 and beyond are for stabilisation and growth in the Energy Markets, a recent area of concern for the market.
- Expectations of a more clear dividend policy of at least 60% payout post APLNG startup, and a decision to issue a European hybrid rather than raise equity this year to fund its acquisition of the Poseidon offshore WA gas discovery.
- A diverse gas portfolio secured ahead of the startup of the LNG projects on the East Coast, which may benefit margins post- the LNG startups in 2015/2016.

Seek SEK			
Price	$16.59	PE (x)	26.0
Price Target	$19.76	Yield	1.7%
Upside	19.1%	Gross Yield	2.4%

Seek (SEK) is the leading provider of online employment services in Australia, China, Southeast Asia and Latin America. The company also owns a rapidly expanding online education business

Key reasons to buy

- The Australian recruitment cycle is at or near to all-time lows in churn rates and recently volumes have begun to rebound.
- We expect SEEK to report double digits earnings growth in FY15.
- Seek's offshore operations will deliver high double-digit growth in FY15 as the benefits of the Jobstreet acquisition become available. The company is achieving strong growth while simultaneously de-leveraging its balance sheet.

Stockland Group SGP			
Price	$4.06	PE (x)	15.9
Price Target	$4.11	Yield	5.9%
Upside	1.2%	Gross Yield	5.9%

Stockland Group (SGP) is Australia's largest developer given its significant landbanks.

Key reasons to buy

- Around a third of earnings are derived from residential development. Given the improving macro environment, we believe SGP is well placed to benefit in the medium term.
- The balance of the investment portfolio is good quality (office, retail, logistics, retirement), and although medium term retail and office conditions are challenging, the earnings visibility is good given contracted rents. SGP's strategy is to reduce its office exposure over time.
- SGP offers investors an attractive FY15 distribution yield of 5.9%

Telstra TLS			
Price	$5.49	PE (x)	16.8
Price Target	$6.00	Yield	5.6%
Upside	9.3%	Gross Yield	8.0%

Telstra (TLS) Australia's largest telecommunications company.

Key reasons to buy

- This is a shorter term tactical call (sector allocation). As we head into seasonally weak period for equity markets (defensive stocks should outperform).
- We think Telstra is the best positioned telco for the upcoming NBN review and the collaborative approach favours Telstra .
- The Government may have seen Telstra exit the negotiations (in mid 2014) in a better position than they entered. As recent example was the A$150 FTTN trial site agreement that Telstra and the Government signed in June.
- We think the company will look to undertake smaller Asian centric acquisitions which will help growth.

High Conviction Stocks

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Transurban Group TCL			
Price	$7.78	PE (x)	na
Price Target	$8.06	Yield	4.8%
Upside	3.6%	Gross Yield	5.4%

Transurban Group (TCL) develops, operates, and maintains toll roads in Australia and the US.

Key reasons to buy

- We expect TCL to generate double-digit EBITDA growth over the next three years driven by traffic growth, CPI/CPI+ toll increases, ongoing cost control, and contribution from growth projects.
- We expect this traffic and earnings growth to translate into double-digit growth in distribution per share.
- Confidence in this growth outlook can be gained from the management incentive plan, which rewards management for growing free cashflow per share at 10-13% per annum CAGR across FY14-17.

Ex 100

This month's changes

This month we have made several changes to our ex 100 High Conviction list, removing Domino's Pizza (DMP) following significant share price appreciation and Industria REIT (IDR) and 360 Capital Office Fund (TOF) to make way for new property names. We have added the following names: GBST Holdings (GBT), Mantra Group (MTR), National Storage REIT (NSR), Shine Corporate (SHJ) and 360 Capital Industrial Fund (TIX).

Admedus AHZ			
Price	$0.15	PE (x)	208.3
Price Target	$0.23	Yield	0.0%
Upside	54.3%	Gross Yield	0.0%

Admedus (AHZ) has a diversified life science portfolio across, medical products, regenerative medicine and DNA vaccines.

Key reasons to buy

- Recently completed a A$18m capital raising, which will accelerate sales in Europe and the US for its key regenerative medicine product called CardioCel.
- AHZ is developing DNA vaccines, using Prof Ian Fraser's technology and an efficacy trial is expected to start later this year following a successful safety trial in HSV-2 (genital herpes).
- Plenty of newsflow in next six month – additional CardioCel approval in the Asian region, increasing sales for CardioCel, further updates on the vaccine trial and a growing revenue stream as confirmed by their FY result.

GBST Holdings GBT			
Price	$4.00	PE (x)	21.2
Price Target	$4.86	Yield	2.4%
Upside	21.5%	Gross Yield	2.4%

GBST provides software and systems to banks and fund managers to enable them to manage order and settlement work flow in a highly automated and efficient fashion.

Key reasons to buy

- The five-year drought in spending on new systems by financial institutions has come to an end, offering GBST a chance to pick up significant new contract wins over the next few years.
- The company implemented 16 new customer projects in FY14, some of whom were implemented at the end if the financial year. The full-year impact of these new installations will deliver double-digit growth in FY15.
- GBST will be debt free in FY15 and will be poised for acquisitions or capital management by FY16.

Mantra Group MTR			
Price	$2.18	PE (x)	16.3
Price Target	$2.45	Yield	4.6%
Upside	12.4%	Gross Yield	6.6%

Mantra Group (MTR) is a leading accommodation operator in Australia and New Zealand and is also expanding in Indonesia.

Key reasons to buy

- The company is leveraged to improving domestic leisure and business travel demand through its Resorts and CBD businesses. It is also benefiting from strong international inbound travel to Australia, lead by Asia.
- MTR offers investors a solid earnings growth profile, strong FCF and an attractive fully franked dividend yield.
- We expect that MTR will rerate towards our A$2.45 valuation as it delivers on its FY15 forecast and makes further accretive acquisitions.

National Storage REIT NSR			
Price	$1.36	PE (x)	14.5
Price Target	$1.45	Yield	6.2%
Upside	7.4%	Gross Yield	6.2%

National Storage REIT (NSR) is the first ASX-listed, internally managed and fully integrated owner and operator of self-storage centres.

Key reasons to buy

- First mover advantage in the self-storage asset space.
- Future growth potential via acquisitions given the fragmented storage market; and
- An attractive FY15 distribution yield of approx. 6%.

Pact Group PGH			
Price	$3.83	PE (x)	12.4
Price Target	$4.31	Yield	5.6%
Upside	12.5%	Gross Yield	7.2%

Pact Group (PGH) is the leading supplier of rigid plastics packaging in Australia and New Zealand. It also has an emerging presence in Asia.

Key reasons to buy

- We view this defensive, strong cashflow packaging business as a core portfolio holding.
- PGH is trading at an unwarranted discount to its global peers given it has industry leading margins and cashflow conversion. We expect that this discount will narrow as the company delivers on its prospectus forecasts.
- PGH also offers a more attractive dividend yield.

Shine Corporate SHJ			
Price	$2.31	PE (x)	14.1
Price Target	$2.70	Yield	1.7%
Upside	17.0%	Gross Yield	2.5%

Shine Corporate (SHJ) is a market leader in the area of damages based plaintiff litigation.

Key reasons to buy

- SHJ is trading at on a FY15 PE of 14.1x versus its Slater & Gordon trading on 17.3x. In our view, the extent of the discount is unwarranted.
- We believe SHJ will continue to benefit from a fragmented market and its ability to acquire value enhancing acquisitions.
- SHJ's organic growth profile (high single digits), internal optimisation initiatives; improvement in operating cashflow and WIP recoverability should be sufficient to hold investors' intentions in the near term as we wait for the next acquisition.

360 Capital Industrial Fund TIX			
Price	$2.40	PE (x)	10.3
Price Target	$2.48	Yield	8.0%
Upside	3.3%	Gross Yield	8.0%

360 Capital Industrial Fund (TIX) owns a portfolio of 21 industrial assets across Australia valued at around $470m.

Key reasons to buy

- Attractive FY15 yield of 8%.
- Cashflows supported by stable rents which average 3.5% rental growth pa.
- Strong portfolio metrics (Woolworths largest tenant) including a WALE of 6 years.

Source: IRESS, Morgans, Company Data
Forecast based on FY15

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