# Asia to rally

We never used to use the ANR function on Bloomberg – it always seemed a bit pointless tracking analysts' recommendations and target prices which for the most part followed share prices with a six month lag – but we have now become converts.

The reason? It has become an interesting and occasionally timely source of contrarian ideas, with a significant number of former 'blue chip' companies reaching the pariah status of having NO buy recommendations. In some cases this may be justified as bankruptcy looms, but in others it represents a vitriolic response by previously over-optimistic analysts who vent their spleen on company management for their inability or unwillingness to accurately predict their own earnings, irrespective of the underlying strength of the business. Telecom New Zealand and Brambles are two good examples of these 'fallen angels', and while the problems of both businesses are well known, they do still produce stable cash flows and a decent return on investment – and in both cases are integrated into business processes in a way that keeps a lot of their revenue 'sticky' .Very few management teams are coming through the current environment unscathed, and market participants often attribute too much – good and bad – to the individuals concerned. Perception can change quickly, and we like situations where it can't get a lot worse.

At long last the Chinese 'wall of money' is headed down under. Serious money is being put on the table by both state controlled and private bidders as Chinalco's $20bn for selected minority positions in Rio's operations has been followed by a full bid for Ozminerals (which will presumably require a new name) by Minmet and a stake in Fortescue being acquired by Hunan Valin. It is also interesting to note a consortium of Japanese utilities taking a stake in Uranium One, and a vigorous bidding war breaking out between Arrow and BG over Pure Energy, a Coal Seam Methane company, at prices that are more reflective of $100+ oil than those currently prevailing. Clearly the industry is working off a rather different playbook to the financial participants in the sector. Elsewhere we are also seeing the first sign of opportunistic privatisation, with Crocodile Garments and, possibly, Delta Networks being removed from the scrutiny of the public markets at a healthy premium. Shame the Private equity boys blew their cash in 2007…..

Talking of  Private Equity – the award for worst deal ever done had been a shoo-in for RBS's corporate seppuku with the ABN dagger, but there are a few contenders coming up on the rails. Schaeffler and Continental must be in the running, as would TPG/WAMU, Daiichi/Ranbaxy and Lloyds/HBOS. These sorts of comparators are presumably the reason Ken Lewis of BOFA can declare his purchases of Merrill Lynch and Countrywide as ‘stars’ – presumably supernovae. However, the new favourite in the category of immediate value destruction must be the mooted purchase of 40% of AC Milan for €500M by the UAE. Surely this must ring the bell on the last bubble in the financial world? After all, any higher prices and you would have to think footballers are worth as much as bankers circa 2007.

Despite all the doom and gloom, there has been some positive news on property recently. Sales of apartments in Singapore reached 1000 in February alone, compared to 4,800 for the whole of last year. In Hong Kong, SHK Properties’ upmarket Cullinan development has been selling briskly (kitted out with $15,000 fridges), and we are hearing anecdotal reports of more activity in quite a few Chinese cities as well. While this may be in part a response to aggressive price cutting (in China, anyway), it is evidence that appetite is there at a price, and that funding remains available. This is all in stark contrast to the death-slide being exhibited by property stocks in the UK, Australia, Europe and the US. The crucial difference is gearing – the Asian property stocks are not under pressure to de-gear due to breaches of banking covenants, and there remains a core of buyers with access to finance. The almost total demise of the Australian Property Trust sector and the 20 year lows being seen in the UK property stocks (and those are the blue chips) are a painful reminder of what happens when management can’t remember the last downturn. In Asia the patriarchs of the property companies can vividly recall the near death experience of the Asian crisis and have been in no hurry to repeat it. Times may be tough but most of the property stocks will be around to enjoy the recovery, and aren’t priced for it.

Despite a materially better economic situation than in the US or Europe, and possessing a functional and privately owned banking system, the Australian market has been a disappointing performer, with large swathes of the market that used to enjoy ‘core’ institutional status now reduced to the level of penny stocks, as in vestors exit stage left from anything with debt. In some cases this produces a self-fulfilling downward spiral as enterprise value covenants are breached and management shareholding on margin is called, leading to more selling of the equity and higher interest costs. However, in recent weeks we have seen a subtle change in sentiment as investors become more relaxed about re-capitalisation, paying less attention to dilution and overhang than to the prospect of being a going concern in 2010 and the likelihood of a re-rating from current levels of PERs in the 2-6x range. The furore over Rio ‘selling out at the bottom’ and being actively lobbied by its large shareholders for an issue is a case in point. The market is now littered with value, some of which is a binary trade – bankruptcy or quadruple your money – but is also rich in opportunities with less potentially terminal balance sheet risk, especially after an enormous number of equity issues over the last few months. This is presenting us with some fertile hunting ground across a variety of sectors from media and transport through to real estate and resources. Well worth spending some time screening through the debris of the market for a few golden nuggets.