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Companies Featured
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August 17, 2010

Asia/Pacific Morning Meeting Summary

Highlights

The Morning Call

Newcrest Mining (Australia) / Historically NCM Outperforms Gold in 2H of Year	Overweight
ANTA Sports Products (China) / 1H10 Beat on Margin; Maintain OW	Overweight
China Telecommunications / 1H10 Preview: Shifting Focus to Fixed Line	
S. Korea Technology / Recent LED Correction Provides Attractive Entry Point	
China Economics / Renminbi on Summer Break	

Company/Industry Analysis

Austereo Limited (Australia) / No Joking … Hamish & Andy Departure Could Prove Negative For EPS … But No Material Impact On Intrinsic Value	Overweight
iiNet Limited (Australia) / FY10 Result In Line; Near-Term Growth Outlook Dims in Telstra's Shadow	Overweight
Imdex Ltd (Australia) / Fluids Back in Motion	Overweight
Leighton Holdings Ltd. (Australia) / Valuation Attractive for Current Point in the Cycle	Overweight
Anhui Conch Cement Co. Ltd (China) / In-line 2Q10; Maintain EW	Equal-weight
Tingyi (Cayman Islands) (China) / 2Q10: A No Surprise Quarter	Equal-weight
CLP Holdings (Hong Kong) / Turnaround in China and Australia	Equal-weight
China Power / July: Power Demand Slowdown to 13.9% YoY; While 10.7% Growth MoM	
Jinro (S. Korea) / Not Much Upside with Few Catalysts	Equal-weight

Strategy/Economics Analysis

Australia Strategy and Economics / Living in a Bubble

What's Changed

Stock Rating Changes - Downgrades

Ticker	Company	Stock Rating From	Stock Rating To	Price Target From	Price Target To	ModelWare Estimate From	ModelWare Estimate To (FY)	Consensus*
000080.KS	Jinro	O	E	W40,000	W41,000	W2,661 W2,949 W3,383	W2,573(12/'10) W2,940(12/'11) W3,367(12/'12)	-- -- --

Estimates/Price Target Changes - Up

Ticker	Company	Stock Rating From	Stock Rating To	Price Target From	Price Target To	ModelWare Estimate From	ModelWare Estimate To (FY)	Consensus*
2020.HK	ANTA Sports Products	--	O	HK$13.80	HK$17.30	Rmb0.58 Rmb0.67 Rmb0.79	Rmb0.59(12/'10) Rmb0.70(12/'11) Rmb0.82(12/'12)	Rmb0.59 Rmb0.72 Rmb0.86
0941.HK	China Mobile Limited	-- --	E --	HK$88.00 --	HK$90.00 --	Rmb5.94(12/'10) Rmb6.13(12/'11)	Rmb5.75(12/'10) Rmb5.98(12/'11)	-- --
0728.HK	China Telecom	--	E	HK$3.40	HK$3.90	Rmb0.20(12/'11)	Rmb0.17(12/'11)	--
0762.HK	China Unicom	-- --	O --	HK$12.20 --	HK$12.50 --	Rmb0.21(12/'10) Rmb0.23(12/'11)	Rmb0.10(12/'10) Rmb0.11(12/'11)	-- --
0002.HK	CLP Holdings	--	E	HK$55.20	HK$61.34	HK$3.62 HK$3.79 HK$3.95	HK$3.85(12/'10) HK$4.02(12/'11) HK$4.14(12/'12)	HK$3.64 HK$3.78 HK$3.98
LEI.AX	Leighton Holdings Ltd.	--	O	A$39.25	A$40.10	--	--	--
0322.HK	Tingyi (Cayman Islands)	--	E	HK$18.40	HK$18.50	HK$0.71 HK$0.83	HK$0.72(12/'11) HK$0.84(12/'12)	HK$0.74 HK$0.90

Estimates/Price Target Changes - Down

Ticker	Company	Stock Rating From	Stock Rating To	Price Target From	Price Target To	ModelWare Estimate From	ModelWare Estimate To (FY)	Consensus*
011070.KS	LG Innotek	--	O	W220,000	W200,000	--	--	--
009150.KS	Samsung Electro-Mechanics	--	O	W192,000	W183,000	--	--	--

Estimates/Price Target Changes - Up/Down

Ticker	Company	Stock Rating From	Stock Rating To	Price Target From	Price Target To	ModelWare Estimate From	ModelWare Estimate To (FY)	Consensus*
IIN.AX	iiNet Limited	--	O	A$3.80	A$3.50	A$0.26 A$0.33	A$0.28(6/'11) A$0.34(6/'12)	A$0.29 A$0.35
NCM.AX	Newcrest Mining	--	O	A$40.63	A$41.09	A$1.45 A$1.63 A$1.52	A$1.59(6/'10) A$1.64(6/'11) A$1.49(6/'12)	A$1.40 A$1.86 A$2.18

* First Call consensus estimate. *For valuation methodology and risks associated with any price targets above, please email morganstanley.research@morganstanley.com with a request for valuation methodology and risks on a particular stock*

The Morning Call

NCM.AX, Newcrest Mining (A$35.20) /Historically NCM Outperforms Gold in 2H of Year

Morgan Stanley Australia Limited
Cameron.Judd@morganstanley.com, Craig.Campbell, Sarah.Lester

Rating: Overweight
Australia Gold: Attractive
Target: A$41.09
52-Week Range: A$39.75-28.47
Mkt. Cap(mn): A$17,071
ModelWare EPS: A$1.59 (FY 6/'10), A$1.64 (FY 6/'11)

Average 4Q return is 18.5% since 2003; Overweight. Although the share price has underperformed the A$ gold price by 12% year to date, several catalysts could reverse this trend. The stock price typically performed most strongly in 3Q and 4Q of each year. Since 2003, it has returned on average 18.5% in 4Q, vs. the average US$ gold price return of 7.3%.

LGL shareholders scheduled to vote on NCM's offer August 23. Should the offer be approved, NCM would assume management control of LGL's assets by August 30. In our view, NCM could re-rate following this event as it brings forward significant growth projects. We would expect buying pressure from domestic institutions who own a relatively small 16% of outstanding shares (international institutions own 69%).

F2010 underlying NPAT A$764mn: The result was9% ahead of our estimate and 16% ahead of consensus, and was driven by increased gold production, lower operating costs and higher commodity prices. EBITDA margin in was 51%, versus 41% in F2009. Operating cash flow was A$1,303mn, 27% higher than F2009.

2020.HK, ANTA Sports Products (HK$14.98) /1H10 Beat on Margin; Maintain OW

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Rating: Overweight
China Branded Sports Apparel and Footwear: Attractive
Target: HK$17.30
52-Week Range: HK$15.48-9.14
Mkt. Cap(mn): Rmb32,603
ModelWare EPS: Rmb0.59 (FY 12/'10), Rmb0.70 (FY 12/'11)

Retain Overweight, raise price target to HK$17.3: Our price target change reflects higher increased earnings estimates for 2010-12. In addition, we have lifted our longer-term earnings forecast given the ongoing enhancement in brand equity and the ensuing more sustainable growth, in our view.

1H net profit of Rmb760 mn, up 25% or 11% above our forecast: The better-than-expected results came from better gross margin and lower operating expenses. More advertising and promotion dollars will be allocated to 2H10 with the recent endorsement of NBA star Kevin Garnett and sponsorship of the Asian Games in Guangzhou. The effective tax rate increased to 20.7% in 1H10 from 14.2% in the same period a year ago, due to the tax holiday expiration at its subsidiaries and the additional dividend withholding tax of 5%.

Raising earnings estimates 2% for 2010 and 4% for 2011-2012: This takes into account better sales and gross margin, partly offset by higher effective tax rates. For the full year 2010, we project net profit growth of 18% to Rmb1,472mn. This implies only modest earnings growth of about 11% in 2H10, reflecting the higher A&P expenses.

China Telecommunications: 1H10 Preview: Shifting Focus to Fixed Line

Navin.Killa@morganstanley.com, Gary.H.Yu, Yvonne.Chow

China Telecommunications: In-Line

Retain In-Line industry view; China Unicom still our preferred name. We expect interim results overall to come in strong, as mobile competition has not worsened much, and mobile revenue will continue to benefit from an improved macro environment.

Results will likely turn the market's focus back to fixed line segment. The proposed "three network convergence" (TNC) initiatives from the government create medium-term risks. We see risks of pre-emptive capex increases, broadband tariff cuts and higher marketing spend from the fixed line operators in anticipation of competition from cable companies in 2-3 years.

Stock thesis: China Unicom (0762.HK, HK$.50, O) is our preferred pick, as we remain believers in its 3G technology advantage. CU's 3G business has continued to show steady momentum with monthly net adds reaching 1mn for the past two months. We also expect the fixed line business to show steady performance in 1H10. We stay Equal-weight on China Mobile (0941.HK, HK$83.70) and China Telecom (0728.HK, HK$3.79) with a relative preference for the former. (See our published report for details, including changes to our EPS forecasts and price targets.).

S. Korea Technology: Recent LED Correction Provides Attractive Entry Point

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S. Korea Technology: In-Line

Remain positive on global LED market outlook. Despite a recent slowdown in LED order momentum on global LCD TV inventory adjustments, our channel checks indicate that industry dynamics remain skewed to the suppliers' side. We continue to view the recent slowdown as a temporary hiccup of a newly growing industry. Barring any significant macro slowdown impacting LED TV demand outlook, we think oversupply concerns are premature and expect healthy earnings growth to continue

Accumulate LED names. We believe the recent share price correction is overdone and recommend that investors accumulate LED names. We maintain our Overweight rating on SEMCO (009150.KS, W129,500) and view the recent share 19% correction as excessive. Our new price target implies 41% upside. We also stay Overweight LG Innotek's (011070.KS, W146,000) and view its 24% correction as excessive. Our revised target price of W200,000 implies 37% upside.

Overall LED momentum should resume by September. We think LED TV makers, particularly in Korea, will aggressively promote LED TVs in 2H10 as the window of opportunity to charge a premium on LED TVs will narrow in the next one year or so. We expect strong demand and limited ASP erosion to prevent any sharp margin erosion for the Korean LED makers.

China Economics/Renminbi on Summer Break

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Currency update: Since it exited from its peg against the US$ on June 20, the Renminbi has appreciated vs the US$ rather fast (~0.8% in the first 10 trading days through July 2). However, the US$/CNY rate has since been broadly stable at around 6.77, while most other EM currencies have registered meaningful appreciation against the US$.

Chinese authorities have recently launched an educational campaign articulating the virtues of and their strong commitment to a flexible FX arrangement in the form of five consecutive articles published under the name of PBoC Deputy Governor Hu Xiaolian. This is the first time that Chinese authorities systematically address several important issues pertinent to China's exchange rate policy.

What's next: Authorities will likely more proactively put their strategy of pursuing a flexible FX rate arrangement into action by: a) allowing faster appreciation of Renminbi vs the US$ in part to ease political tensions (especially vis-à-vis the US); b) such that Renminbi would appreciate on a trade-weighted basis meaningfully as long as large trade surpluses (i.e., over 2.0% of GDP) persist; and c) imparting more transparency to the operation of currency basket by officially publishing the nominal effective exchange rate index for Renminbi. We maintain our forecast that the US$/CNY rate will reach 6.60 by end-2010 and 6.20 by end-2011.

Company/Industry Analysis

AUSTRALIA

AEO.AX, Austereo Limited (A$1.77) /No Joking … Hamish & Andy Departure Could Prove Negative For EPS … But No Material Impact On Intrinsic Value

Morgan Stanley Australia Limited
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Rating: Overweight
Australia Media: In-Line
Target: A$2.00
52-Week Range: A$1.93-1.27
Mkt. Cap(mn): A$610
ModelWare EPS: A$0.16 (FY 6/'11), A$0.17 (FY 6/'12)

Conclusion: We see a larger than typical earnings risk on the horizon with national drive-time *The Hamish & Andy Show* yet to decide whether they will extend their run beyond this year. In radio, typically the 'drive' time period doesn't garner the same audiences or advertising dollars as "Breakfast" ... because the comedy duo Hamish & Andy are: 1) uniquely dominant in their timeslot; and, 2) networked nationally across five capital cities ... it is financially significant.

We estimate this time slot may generate A$30-40m revenue and A$10-15m EBITDA annually. Hypothetically, if the show were to end, whilst the downside could be ameliorated with a lower cost replacement, we still estimate the potential EPS risk to be in the range -5% to -10% for the first 12 months. More important, the DCF impact would be a lesser negative 3c-5c/AEO share (i.e. 2-3%) assuming it takes 2 years to develop a replacement show, with audience ratings at 75% of current levels.

F2010 results in-line. A strong start to 1H provides increased confidence for F2011E EPS/DPS growth. Reported EPS of 13.7c vs. 13.1c in pcp, our est.14.0c. The radio ad market recovered strongly in 2H, up 7% and AEO delivered a 2H EPS lift of 12%. We view AEO stock as attractive, at F2011e P/E of 11x (vs. the long-term average of 15x) with a 6.5% dividend yield (70% payout).

IIN.AX, iiNet Limited (A$2.68) /FY10 Result In Line; Near-Term Growth Outlook Dims in Telstra's Shadow

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Rating: Overweight
Australia/NZ Telecommunications: In-Line
Target: A$3.50
52-Week Range: A$3.13-1.67
Mkt. Cap(mn): A$406
ModelWare EPS: A$0.28 (FY 6/'11), A$0.34 (FY 6/'12)

Still value in iiNet's tangible longer-term growth path, but may be harder to find near term. We see at least four key reasons why Telstra is unlikely to win back significant share in broadband, however: 1) The mobile market opportunity is more attractive; 2) Telstra's broadband prices remain more expensive, with less satisfactory customer service; 3) Telstra will likely fare worse in a flat broadband market, with relatively more churning customers, and 4) Telstra may be obliged to match retail price reductions for wholesale customers, diminishing the competitive value of price cuts. Market share gains by iiNet and others may be harder to find, though, and we have lowered our customer and earnings growth forecasts accordingly.

What's new: The F2011 EBITDA outlook statement was muted at A$106mn. After the impact of Netspace and AAPT acquisitions, guidance implies no organic growth vs F2010. iiNet's F2010 result headlines were pre-announced to the market at the time of the AAPT acquisition announcement: F2010 EBITDA and NPAT were A$80.7mn and A$34.8mn, respectively (after one-off adjustments). We had forecast NPAT of A$28.5mn, and consensus was $30.1mn.

What's next: Telstra plans to outline its growth strategy at a Strategy Day in October. Telstra may choose to provide more detail about the markets it expects to fuel its longer-term growth ambitions, and investors will have an opportunity to stress-test Telstra's growth ambitions.

IMD.AX, Imdex Ltd (A$0.84) /Fluids Back in Motion

Morgan Stanley Australia Limited
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Rating: Overweight
Australia Emerging Companies: In-Line
Target: A$1.20
52-Week Range: A$0.96-0.53
Mkt. Cap(mn): A$164
ModelWare EPS: A$0.09 (FY 6/'11), A$0.12 (FY 6/'12)

Reiterate Overweight. F2010 results demonstrated not only that the company had negotiated the global downturn but also that the rate of recovery has Imdex positioned for an expansive future, with 4Q10 revenue close to a record and June a record month.

F2010 results overview: Imdex reported F2010 revenue of A$134.3mn and EBITA of A$20.7mn. More significant, 4Q revenue was A$42.9mn and EBITA A$8.0mn, representing 32% and 39% respectively of full year, at a margin of 18.6%.

Estimate changes: We raise our F2011 forecasts by 3% at the revenue line. EBITA forecasts are 6.1% higher to A$32.8mn, a slightly higher margin of 21.2%, while NPAT forecasts move up slightly after allowing for a higher tax rate. Our F2012 forecasts are broadly unchanged. With continued strength in minerals activity apparent in the mid-term and potential for an expansion into oil & gas longer-term, we reiterate our Overweight rating.

LEI.AX, Leighton Holdings Ltd. (A$30.60) /Valuation Attractive for Current Point in the Cycle

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Rating: Overweight
Australia Capital Goods: Attractive
Target: A$40.10
52-Week Range: A$41.70-27.61
Mkt. Cap(mn): A$9,275
ModelWare EPS: A$2.25 (FY 6/'11), A$2.48 (FY 6/'12)

Solid F2010 results; Price target up, remain Overweight. Leighton reported F2010 earnings that were largely in line with expectations, while strong work in hand and favorable outlook statements were a clear positive.

Key highlights: F2010 earnings of A$612mn were largely in line with consensus/our estimates. WIH rose to a record A$41.5bn, the top end of prior guidance and ahead of expectations. Contract wins post June-30 are likely to mean the order book is currently above A$42bn. Fully franked final dividend of 85c was declared (73% payout ratio), ahead of our 65c expectation. Operating cash flow rose to A$1.7bn from A$875.9mn and gearing fell to 38% (including off balance sheet leases) from 48% removing the risk of a near term equity raising, in our view.

Attractive valuation: Our A$40.10 DCF suggests ~30% upside, with Leighton trading at 13.4x P/E (one year forward consensus), a 12% discount its historical long term average of 15.2x, despite forecast EPS growth of 10.7% and 10.5%, for F2011 and F2012, respectively. Long term growth drivers include: (1) Resource demand from China and recovery of traditional export markets; (2) Infrastructure investment driven by aggressive state and federal government plans; and (3) Offshore expansion in emerging markets poised to grow during recovery.

CHINA

0914.HK, Anhui Conch Cement Co. Ltd (HK$26.20) /In-line 2Q10; Maintain EW

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Rating: Equal-weight
China Building Materials: Attractive
Target: HK$28.00
52-Week Range: HK$29.60-21.45
Mkt. Cap(mn): US$11,910
ModelWare EPS: Rmb1.35 (FY 12/'10), Rmb1.69 (FY 12/'11)

2Q10 results in-line; EPS, price target unchanged; Remain Equal-weight. 2Q EPS of Rmb0.28 was 4% below our forecast of Rmb0.30 but 20% below consensus of Rmb0.35. While GP/ton of Rmb57 was exactly in line, sales volume of 35mn tons was 5% below our estimate, resulting in total gross profit 5% below. Although lower SG&A has resulted in 4% higher EBIT, higher finance cost and income tax brought it back to an in-line bottom line at Rmb1bn.

Capacity expansion on track. In 1H, the company completed construction for 7 clinker lines and 12 cement grinding stations in Sichuan, Gansu and Jiangxi, increasing clinker and cement capacity by 12.6mn tons and 13.2mn tons, respectively, on track with guidance of a 29mnt increase in clinker capacity this year. Looking into 2H, the company will continue to develop new projects and proceed with acquisitions to sustain market share growth.

Positive industry outlook: The company maintains its positive 2H view, on strong demand from infrastructure, social housing, and development in Western China, as well as accelerated closure of outdated capacity. On 8 August, MIIT announced a detailed closure list, which contains 762 producers with 107mnt capacity (~5% of 2010e capacity) to be closed by 3Q10, suggesting an improving demand-supply dynamics.

Funds managed by Morgan Stanley, beneficially own, in aggregate, approximately 9% or more of a class of securities and have appointed a director to hold a board seat in China Shanshui Cement

0322.HK, Tingyi (Cayman Islands) (HK$18.64) /2Q10: A No Surprise Quarter

Rating: Equal-weight

Angela.Moh@morganstanley.com, Penny.Tu

China Food, Bev. & Tobacco: Attractive
Target: HK$18.50
52-Week Range: HK$20.60-13.52
Mkt. Cap(mn): HK$104,328
ModelWare EPS: HK$0.59 (FY 12/'10), HK$0.72 (FY 12/'11)

Maintain Equal-weight, price target of HK$18.5: Our thesis is unchanged after 2Q results; sales should remain robust in the rest of 2010 and long-term growth prospects are still solid, while some margin pressure could come from both higher input cost and intense competition. At 31.6x 2010E P/E or 25.9x 2011E P/E, we feel risk-reward is not attractive and would wait for better entry point.

2Q: Strong beverage sales but opex also higher. 2Q net profit came in at US$95 mn (up 10%), in line with our estimate of US$98 mn. While sales growth of 35% was 9% higher than our expectation due to strong beverage sales, operating profit growth of 15% was in-line on higher selling expense from promotions.

Earnings revisions. We leave our 2010-11 estimates largely unchanged after the following adjustments: 1) bumping up noodle and beverage sales to factor in better sales momentum thus far; 2) trimming gross margin assumptions to leave more buffer for high input cost; 3) slightly higher operating expense from promotions..

HONG KONG

0002.HK, CLP Holdings (HK$58.05) /Turnaround in China and Australia

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Rating: Equal-weight
Hong Kong Utilities: In-Line
Target: HK$61.34
52-Week Range: HK$58.05-51.60
Mkt. Cap(mn): HK$139,677
ModelWare EPS: HK$3.85 (FY 12/'10), HK$4.02 (FY 12/'11)

1H10 results update; Remain Equal-weight. 1H net profit of HK$5.921bn was up 83% YoY. Excluding one-off gains, recurring net earnings rose 26.6% due to a turnaround from the loss of Chinese IPPs and >100% earnings growth in Australia on operational improvement. We believe CLP is now on track to deliver consistent earnings growth from 2010. With an increase in capex in Hong Kong (up 16% YoY) and a stable dividend payout but reduced SOC return, there could be less cash flow available to fund overseas, and we believe CLP's medium-term earnings growth will depend largely on execution of the more visible investment opportunities in HK, China, and India, with a focus on renewable projects.

CLP is negotiating terms on its 17% stake in CGNPC's 6GW Yangjiang Nuclear Project. We believe the consideration CLP will pay to CGNPC will be very close to CGNPC's original cost. Earnings quality for Yangjiang is high as the on-grid power tariff under the feasibility study is very competitive at Rmb363/MWh, compared to the average coal-fired on-grid tariff at Guangdong at Rmb504.2/MWh.

Investment thesis: CLP trades at 14.4x our 2011E P/E and 8.8x EV/EBITDA and offers a 4.5% dividend yield. We have revised our estimates on our latest currency and economic forecasts, as well as improved operation in China and Australia. Among HK utilities CKI (1038.HK, HK$30, O) is our top pick given its highest dividend yield, discount to NAV, and acquisition growth potential.

China Power: July: Power Demand Slowdown to 13.9% YoY; While 10.7% Growth MoM

Simon.Lee@morganstanley.com, Eva.Hou

China Power: In-Line

Julypower demand down slightly to 13.9% YoY, from 14.1% in June. While the YoY growth rate declined 0.2bbp, monthly power demand edged up by 10.7% MoM in July, compared to a modest 1.1% increase last month. We note that the secondary demand growth of 15.4% MoM drives the total demand growth, followed by demand from residential of 20.1% and from tertiary industry of 15.7% due to the seasonally effect. From January-July, total power demand amounted to 2,399bn kWh, up 20.3% YoY but continued to slow from 21.6% in the 1H10.

What's new: Huaneng (0902.HK, HK$4.71, E) reported 1H10 results last week. Despite a slightly better-than-expected result and earnings growth in 2Q QoQ, we note that both the gross margin and EBIT margin further deteriorated in the second quarter due to the coal price increase. Datang (0991.HK, HK$3.18, E) will release 1H10 results this week. We expect a positive surprise from its hydro power plants but overall earnings should be under pressure.

Investment thesis: In 2010, we believe coastal IPPs such as Huaneng and CRP (0836.HK, HK$17.50, O) will be better than inland IPPs such as Huadian and Datang. We reiterate CRP as our only Overweight in China IPPs, given its power plant enjoys the highest exposure to the coastal area.

S. KOREA

000080.KS, Jinro (W37,750) /Not Much Upside with Few Catalysts

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Morgan Stanley Asia Limited
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Rating: Equal-weight
S. Korea Consumer: In-Line
Target: W41,000
52-Week Range: W44,650-30,150
Mkt. Cap(bn): W1,604
ModelWare EPS: W2,573 (FY 12/'10), W2,940 (FY 12/'11)

Downgrade to Equal-weight. Although a base-year shift lifts our price target slightly to W41,000, strong recent stock performance does not allow much upside from current levels. Due to the high base effect from 2009, we expect earnings momentum could remain weak in 3Q10. We believe 4Q10 could be a better time to revisit the name, ahead of dividend announcement, outlook for a strong earnings pickup, and a visible plan for co-marketing efforts with Hite Brewery.

2Q weaker than expected.N et income was roughly in line with our estimates, but operating income was much lower than expected. We believe weak volume in the soju market (we estimate down around 5-6% YoY) and a high base in Jinro's market share (around 49% in 2Q10 vs. 51.3% in 2Q09) led overall sales to decline -8.6% YoY. A high proportion of fixed costs and rising A&P costs dampened OPM by 5.9ppt compared to last year.

Still challenging base in 3Q10: Last year, Jinro had an aggressive inventory push at the wholesale level, driving overall market growth of +3.7% YoY. We expect this challenging base effect could lead to a volume decline with operating margin contraction again in 3Q10.

Strategy/Economics Analysis

Australia Strategy and Economics/Living in a Bubble

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Australia's debt-fuelled housing market remains a major macro risk. Dodging the worst of the global financial crisis didn't demonstrate that there's no bubble; in my view it just showed we dodged the prick. I'm not persuaded by arguments that houses are sustainably priced; I'm not persuaded by the view that debt is not a problem; and I'm not persuaded that policy-makers could prevent collateral damage to banks. However, the risk of big price declines in the near term seems low.

In my view, Australian house prices are expensive on every value metric. They are expensive relative to history, and expensive relative to houses in comparable countries. Most measures suggest house prices are around 40% above fair value. There's a word for a financial asset that's over-valued by 40%, so let's use it: housing is a bubble. Buying an asset that's over-priced never ends well. The real return on residential property over the next decade is likely to be negative, in my view.

Valuation measures are broadly consistent about the degree of over-valuation. They're also consistent about when the bubble started to inflate: from around 2000. What caused the bubble? The key is the growing ability and willingness of Australians to increase leverage, compounded by what I would view as ill-advised policy (such as grants to first home-buyers). Owner-occupiers have played a game of financial chicken, competing for property by taking on increasingly imprudent amounts of debt. Investors have become Ponzi borrowers – Hyman Minsky's term for borrowers who rely on capital gains to repay debt and interest – in the belief that housing is a sure-fire long-term investment. History shows that it isn't.

What will prick the bubble? The most plausible trigger is broad-based jobs losses. That doesn't appear likely in the near-term (although global risks are rising). Other, more imminent, risks include banks tightening credit and/or Australia's army of loss-making middle-class landlords starting to sell.

Disclosure Section

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Analyst Certification

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Stock Rating Category	Count	% of Total	Count	% of Total IBC	% of Rating Category
Overweight/Buy	1095	42%	380	44%	35%
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Not-Rated/Hold	14	1%	4	0%	29%
Underweight/Sell	362	14%	93	11%	26%
Total	2,594		865		

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