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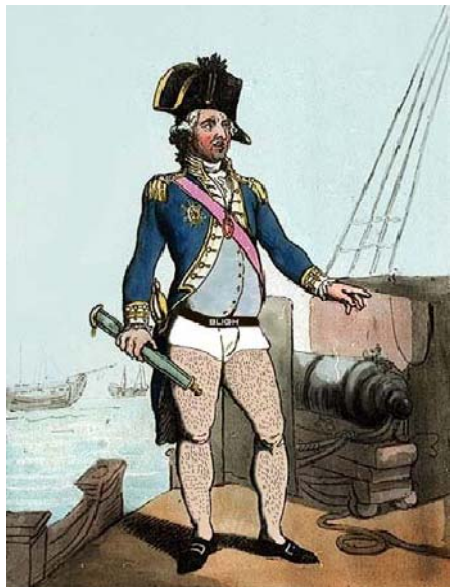
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This week in **BLIGH'S BRIEFS...**



- **Technology One** – the most preferred play in IT space – by quite some margin we argue
- **Programmed Maintenance** – a pedestrian core overlaid by a medium term cyclical upleg
- **Nufarm** – time to recalibrate the thinking
- **ICash** – an interesting microcap with a global edge
- **Emeco** – maybe, just maybe, the new found focus on ROC will inject a bit of life into this play

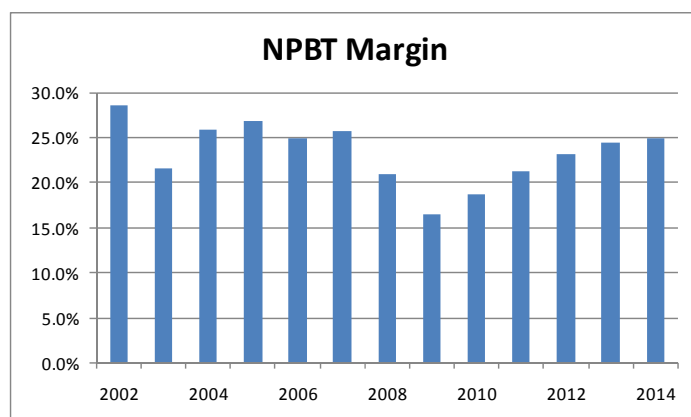
- We waltzed down to Aido's post result-release briefing during the week to buttress our understanding of **TechnologyOne (TNE)**; a story which to us appears better and better at each hearing.

Part of the appeal at this time lies with investors being a little jaundiced when coming to regard the stock; they believing that Aido is betraying the symptoms of Winkler Disease over recent periods¹.

It is worth countering this upfront: with costs up a modest 3% in h1-10 and PD held constant in nominal dollar terms, Aido has been seen to abide by the commitment he made 6mths ago that he would hold both categories of outlay in check (as a percentage of revenue) to allow the re-establishment of (NPBT) margin. He reiterated this position on Wednesday.

Should he retain the discipline, and there is no suggestion in his commentary of diluting the

commitment, then his Winkler moment is well behind².



Top line growth, for its part, should be pretty solid. There was a slowing in the wake of the GFC and customers taking longer to get over the line remains the principal revenue constraint. The pipeline was nonetheless described as 'strong' and likely to remain so into FY11 as previously delayed projects build through aided by the group's broadening of its

¹ An affliction that leads to cornerstone shareholders / management pursuing an agenda of perpetually investing for tomorrow at the expense of today such that returns appear constantly hobbled.

² Rather, Aido suggested he would like to get to his 25% margin target within the next 3 yrs.

product suite as the likes of Works & Assets, Property & Rating, HR & Payroll and Enterprise Content Management (all of which are 'loss making' while under development) make their way forward³.

The group retains a tight focus on its chosen verticals (local govt, federal govt, education, health, utilities and managed services) and it is this, the interoperability of its products on the (internet enabled) Ci platform, the ownership of the products' implementation⁴, and, as a consequence, a well maintained reputation, that shores up its market position. Its share of certain of the verticals (eg 20% in Education; 25% Federal Govt) and the low penetration of certain of the products within same promise ample scope for growth. The toehold the group has in the UK presents as a longer dated field of opportunity (and a modest negative drain in the meantime).

The group has long taken the moral high ground and written off all R&D as incurred. In large part this is dictated by the need to reinvest to remain relevant, but there intuitively is also an element of 'growth capex' to the spend which suggests that the treatment is overly conservative when it comes to using the 'profit' number as a basis of valuation (i.e. we should err on the side of generosity when it comes to the derivation of the appropriate multiple).

Notwithstanding this year's spend on the group's whiz-bang R&D Centre (capex this year should be in the order of \$16m; some 5x deprec), the company's financial structure suggests that it is not capital intensive (Operating Cash Flow before Capex is ~ 80% of EBITDA – the principal deduction being tax paid with working capital a modestly positive contributor thanks to the building through of deferred maintenance fees). Together with the group's \$20 -

\$25m net cash position, this facilitates a sustainably high (75% - 80%) payout ratio.

Not that there are any plans but the group is of a mind to retain the weighty net cash position to take advantage of any acquisition opportunities should they arise (the preference is to do things organically although it would not say no to small pockets of IP).

The group has a guidance out there for the current year to Sept-10 of 10 – 15% growth at the NPAT level but is the first to admit (and the range suggests) that, while the pipeline looks strong, whether it will meet or exceed guidance depends upon whether contracts are signed before or after Sept 30⁵ (visibility is limited on this score). Being a conservative veggie, we suspect that Aido has erred on the light side ('85 – 90% certain that we will meet guidance') but having fallen short last year (when the GFC bit – the delays remember) he is understandably loath to chance his arm. When pushed though, if things fall the way they could, the guidance for the current year could be 'smashed'.

So we have

- A sustainable position in a seemingly resilient market (project delays did not preclude top line growth),
- discernible avenues for revenue growth (deferred projects coming forward; new product releases; payback for investments undertaken over the past couple of years – a period which saw a bolstering of resources and a marked increase in PD),
- scope for margin expansion – particularly if the House of Solutions initiative bears fruit, quite apart from the stated intent to run expenses below revenue growth over the medium term,
- a robust Balance Sheet,
- proprietary ownership of the product (not beholden to the whim of 3rd parties) and
- an equity market that remains to be convinced that things are again going to rock 'n' roll.

³ Some 60% of licence fee income (i.e. new sales) come from two products (Financials i.e. General Ledger, and Business Intelligence i.e. Analytics). There is thought to be considerable scope to grow certain of the others which are still in their infancy when it comes to penetration. Given the existing relationships with clients the path to inveigling the other products is not presumed to be bumpy.

⁴ A key point of differentiation is that the group will not use 'partners' such as Accenture to implement its product (unlike SAP, Oracle et al). While this limits its sales (the House of Solutions initiative is designed to mitigate this) the ownership of both product and implementation leaves any problem, present or subsequent, in the hands of TNE rather than falling through a crack to the frustration of the client. TNE charges a higher upfront (or licence fee) but has a substantially lower implementation charge which leaves it price competitive. The group argues that upfront price is less of an issue in winning business than functionality and price through to installation; and reputation

⁵ As with most software companies, a licence fee is booked as revenue upon the signing of the contract (~30% of the total value depending on the terms); a further 30 – 40% upon completion of the implementation; and the balance is typically a maintenance fee paid annually over the duration of the arrangement

It is a combination that should dictate a chunky premium rating; the prevailing discount sits as an anomaly which should be taken advantage of. BUY.

TechnologyOne							
Shareprice							0.79
Yr to Sept		2009	2010	2011	2012	2013	2014
Profit before SI	\$m	15.7	18.1	22.0	25.8	28.8	31.1
Normalised Profit	\$m	15.7	18.1	22.0	25.8	28.8	31.1
EPS	c	5.1	5.9	7.1	8.3	9.3	10.0
P/E	x	15.3	13.4	11.1	9.4	8.5	7.8
P/E Rel		102	97	85	78		
Dividend	c	3.8	4.6	5.5	6.3	7.0	7.8
Yield	%	4.8	5.9	7.0	8.0	8.9	9.9
Franking	%	100	100	100	100	100	100
EPS Growth	%	-9%	14%	21%	17%	12%	8%

- After some months fluffing around **Programmed Maintenance (PRG)** would appear to have tightened up its act and got comfortable with what it now sees as its role in life.

Not that this week's post results briefing heralded a change to the direction articulated a couple of weeks ago; just a greater sense of confidence exuded that the new way is the right way.

The group presents as a business with a relatively solid core but with a cyclical component which is destined to experience a good kick up into the back half of this year.

The former has had its issues: the paint contracting business has experienced some leakage as contracts roll off – some customers opting for an as-you-go approach rather than rolling the arrangement for another 6yrs⁶. Those that are prepared to enter a contract are now entertained by two competitors (one of which is SPT) who are prepared to be increasingly competitive when it comes to price. The consequent margin pressure layers that in the spot painting market (of equal size to the contracting business within the group's makeup) and a tendency of people to defer maintenance where they can to make this area tough going (albeit that it does appear to be basing). With maintenance only able to be deferred for so long, there is anticipated to be modest growth hereforward.

The group is looking to broaden its offering and further develop its grounds and corporate imaging

arms to complement its painting offering but save for an acquisition (which the group is of a mind and has the capacity to undertake) this is likely to prove incremental.

The Workforce business (10-15% of group EBIT before Unallocateds) is too making slow progress – SMEs et al being slow to add contract labour in what remains an uncertain environment.

For what we know at the moment it is inappropriate to expect a substantial step up in performance out of the Property Maintenance, Facilities Management or the Workforce Divisions in the current year (to Mar-11) over and above that afforded by the acquisition of KLM. While it harbours ambitions of undertaking more Facilities Management and participating in more PPP tenders, the space is well occupied by established and larger players (although it did win some nice contracts late last year which should make their presence felt in FY 11).

Which leaves us with the Resources & Industrial play (presently ~35% of group EBIT before Unallocateds) where again the group's status as a mid tier player has forced it to tighten its focus and pare its offering by disposing of its offshore contracting business. It has entered into an understanding with the acquirer of this undertaking which may see more opportunity come its way in the provision of manning and maintenance services to the new projects coming forward.

As things stand, the group is not expecting a step up in activity levels until the back end of this year; but this should be the beginnings of an extended period of heightened activity as the scheduled fields on the NW Shelf are brought through to production.

Dimensioning this dynamic with any degree of accuracy is difficult; particularly given that there is also a need to discern how much of the work will be of an ongoing nature as distinct from that which is drawn to a close upon the completion of the construction phase (although there sounds as though there will be a number of construction phases).

Be that as it may, the strong tailwind afforded over the next 3 – 5yrs from the NW Shelf constitutes the most appealing feature of the stock in the absence of a broader economic pick-up that could be expected to benefit the core.

So apart from a bit of P/E arbitrage that might be forthcoming as the group utilises what Balance Sheet capacity it has (interest cover this year

⁶ With 70% of revenue booked in Yr 1 of the contract period, this hurts.

should be ~5x), it is this kicker which makes the story worth evaluating.

We have been as generous as we dare in crafting the numbers below but there is a need to capture the acquisition of KLM and the aforementioned tickle to the Resource arm later in the year. At the \$2.72 price point this will throw a 30% discount rating, a level that we are inclined to think errs on the cheap side. It might be a discount stock by virtue of the pedestrian nature of the rump but it does look to be 10 – 15% undercooked. ACC. SB.

Programmed Maintenance						
Shareprice				2.72		
Yr to Mar		2009	2010	2011	2012	2013
Profit bef S Items	\$m	31.7	26.2	36.3	44.2	49.8
Normalised Profit	\$m	35.4	27.8	37.6	44.2	49.8
EPS	c	36.2	26.0	31.6	36.6	40.5
P/E	x	7.5	10.5	8.6	7.4	6.7
Relative P/E		50	76	67		
Dividend per Share	c	14.2	9.0	16.0	18.0	20.0
Yield	%	5.2	3.3	5.9	6.6	7.4
Franking	%	100	100	100	100	100
Norm eps growth	%	23%	-28%	22%	16%	11%

- It was a little coincidental that **Nufarm (NUF)** held a conference call this morning covering off on the glyphosate market a day after we had a long chinwag with Rob Reis.

What encouraged us to touch base with the company was the chart below



Rightly or wrongly the market has clearly walked away from the story following the bursting of the glyphosate bubble; and some disaffection with management following the periodic selldown of personal holdings – sometimes ahead of the release of bad news⁷.

⁷ We may be being kind, but we do not think that there was anything untoward in this

Glyphosate represents a third of the business (the balance runs across other herbicides eg phenoxy, fungicides and insecticides, with a small but growing modified seed business) and has succumbed to the breaking down of the pricing structure of the market that came with the introduction of new capacity in China and more recently, in North America. The company was not alone in not reading the looming collapse: Monsanto's experience was no better.

That said, it would appear that the year to Jul -10 should represent that cycle's nadir: pricing had stabilised in the problematic North American market and was firming in this country on the back of strong demand⁸.

So let's recalibrate the thinking.

The group, simply put, is a blender and packager of other people's stuff, and has developed a portfolio of brands and distribution arrangements in the key food growing jurisdictions around the world.

The thematic backdrop that complements this reason for being is based on the fact that the world needs to be more productive when it comes to food; whether by extracting more off the present farmed acreage or by opening up more land to agriculture⁹. What dictates this is the emergence of a middle class in the burgeoning economies of Asia, and the advent of bio-fuels.

GFC notwithstanding, this backdrop remains intact.

For its part the group has pursued a strategy of establishing beachheads in each of the jurisdictions. From these footholds it sets out to progressively introduce its brands, and thereby increase its relevance to distributors in those regions. The need to go through a prolonged and costly process of getting product registered in each of the jurisdictions is presumed to constitute a barrier to entry.

As a strategy, this too holds water even if it has been called to question recently by the breaking down of the glyphosate market's pricing structure brought on by 'traders' who sourced cheap product

⁸ The group is holding to its guidance of \$80 - \$100m NPAT after Significant Items (principally a writedown of glyphosate inventory)

⁹ There remain vast tracts in Russia, Eastern Europe and South America which have either been left fallow by virtue of poor economics (incl the lack of availability of appropriate infrastructure) or are virgin territory

in say, China, and provide it direct to the end market at well under the prevailing price¹⁰ and yet still bank a healthy profit (suggesting that NUF, Monsanto et al were creaming it ahead of the introduction of this new capacity).

This is text book boom-bust. What is now relevant is that as things sit the gap between the landed cost and the end sale price has closed enough to all but preclude traders from the market. NUF has stated that under the new pricing structure, it can source the input, do its thing, and derive a price for the end product that still delivers a profitable outcome (even if the gross margin in the US is well under half what it was).

It is also pertinent to note that the group pursued a strategy during the rout of pricing so as to retain its market position. By its account it has been successful in this endeavour thereby leaving open the channels as the market recovers.

The group is understandably loath to suggest a rate at which pricing will move through to something that approximates to a 'new normal' (although it did suggest that the mega-margins of FY 08 are unlikely to be repeated anytime soon).

Quite apart from the dynamic around glyphosate the group's business is affected by weather but given the geographic and product footprint¹¹ and the attendant portfolio effects, this is not a key variable if a holistic stance is adopted.

South America has proved a wildcard in years past with the outcome driven by the credit worthiness or otherwise of the farming community (it swung from a \$59m EBIT in FY 08 to a \$49m loss the following year). FY 10 should see a break-even result on revenues of ~\$350m: it should provide something of a contribution on a go-forward basis aided by the improving economic backdrop in Brazil (the principal market).

It is South America and the basing of the glyphosate business, which constitute the key nearterm positive inputs to the NUF story; with the aforementioned thematic and scope to broaden both product and geographic reach the medium term also looks highly prospective.

With the group's winding back of its working capital position (there is a positive aspect to the glyphosate price collapse) the company is holding to its forecast of debt ending the period below \$400m (vs mkt cap \$1.6bn): the Balance Sheet accordingly does not constitute an issue (although the position is highly seasonal – July being the low point).

Sumitomo has built through to its 20% cornerstone position on the register via its \$14 a share tender offer. The two companies will get closer over time; both in terms of sharing product and access to each others' distribution platforms, and given Sumitomo's stated intent to add to its position over time (although it is limited to one 3% creep only after which it must put a proposal to the Board).

Given the vagaries at play the earnings trajectory sketched below has a 'feels like' flavour but does encompass the bits of the puzzle touched in this piece. It does not suggest that the stock is unambiguously cheap though, despite the collapse of the shareprice over the past 12mths.

What wins it for us though is that

- the thematic is real;
- it is likely that we have seen the nadir of the (glyphosate) cycle in which case the prognosis for earnings is skewed to the upside (there are large tracts of the market about which this could not be said) ,
- the outcome is not beholden to the economic outcome (again, not something that can be said for the market at large)
- the market is not presently favourably disposed, and
- there is scope for corporate activity

Well worth an ACC. **SB.**

¹⁰ Notable that the remaining two thirds of the group's revenue was relatively unaffected

¹¹ A third of sales take place in Australasia, another quarter in North America, a similar proportion in South America and the balance, Europe. And then we have the spread of product across herbicide, fungicide and insecticide

Nufarm							
Shareprice							6.00
Yr end July		2008	2009	2010	2011	2012	2013
Profit excl SI	\$m	163.9	159.7	111.8	140.5	161.0	179.7
Normalised Profit	\$m	152.3	145.6	97.9	126.7	147.2	165.9
EPS	c	82.7	72.3	41.5	48.5	56.4	63.5
P/E	x	7.3	8.3	14.4	12.4	10.6	9.4
P/E Rel (to XSI)		52	55	105	105		
Dividend	c	33.5	25.8	20.0	23.0	27.0	32.0
Yield	%	5.6	4.3	3.3	3.8	4.5	5.3
Franking	%	100	0	70	60	66	67
EPS Growth	%	44%	-13%	-43%	17%	16%	13%

- We have been keeping a close eye on **iCash (ICP)** for a while; most recently TP updated on the half-time result which yielded the group's first net profit of \$1.86m for h1-10, including a positive return out of the Korean business, NEO ICP (without the need for transfer pricing). While still a young company, this was a significant breakthrough.

A quick refresher: iCash is one of, if not the only, vertically integrated ATM players in the market, it having:

- ATM design and sales capabilities in Australia and Korea;
- ATM assembly plants in Korea (Seoul) via NEO ICP (in which it purchased a 52% stake in Jan-07);
- Recurring revenue sales in Australia via the direct charge model;
- Outright machine sales in Korea via large retail conglomerates; and
- Emerging market opportunities in NZ, China and further out, Taiwan.

AUSTRALIA

The Australian business model {not unlike that of competitor Customers (CUS)} produces a stable, recurring revenue stream by placing machines in retail outlets and splitting transaction revenues with the merchant post costs. Additionally, some machines are sold to third party resellers (see myATM as an example¹²).

While still a small player in the Aus market¹³, what distinguishes ICP from the likes of CUS is the ability (through control of the manufacturing process) to tailor its

highly functional and compliant machines¹⁴ to client needs. This point of difference leaves it less reliant on price in pitching for business; the recently signed Metcash agreement illustrating the argument (the company signed a preferred supplier agreement in October despite ICP being the fourth cheapest on price – suggests the other package elements are important).

Following a boost to FY10 from the annualising of ATM direct charge legislation (introduced March 09), this competitive advantage bodes well for the company expanding its niche position, with the steady earnings stream to grow at a decent rate over the medium term.

	2008	2009	2010	2011	2012	2013
Australia						
Sales Revenue	5.3	7.4	14.0	15.4	16.8	18.1
EBIT	(2.4)	0.9	3.4	3.8	4.1	4.4
Margin	(46.1)%	12.7%	24.5%	24.5%	24.5%	24.5%

KOREA

The Korean business manufactures and sells ATMs and other cash handling machines, thus presenting a potentially lumpier income stream. Recurring revenues consist of maintenance fees (which are covering ~75% of operating expenses this half).

The company aims to replicate the Australian model in Asia, seeking inspiration from the model of 7-Bank in Japan, whose network of 12,000 independent ATMs generates ~\$500m in fee revenue.

While seemingly a long way off, the desired outcome seems achievable, particularly as relationships with the likes of Lotte Group (a Korean retail conglomerate which recently contracted to purchase 1,500 machines with an option for a further 1,500), and other bigger groups are underpinning the network rollout.

In total, the company sees sufficient commitments (in addition to the Lotte contract) to have the plant cranking at full capacity, or 600 machines per month, for the next 2-3 years (roughly 4x the ~150 per month run rate of h1-10).

At first this pipeline will be met through the outright sale of machines, though ultimately the company wishes to maintain ownership; instead leasing its product to clients in exchange for a clip of the transaction fees (as stated above, the primary ambition).

¹² www.myatm.com.au

¹³ ICP has a 4% share of network vs. CUS' 23%

¹⁴ Until recently its machines were the only fully-APCA (regulatory body) compliant ATMs in Australia, with the main competitors yet to meet the standards

In the meantime, there is significant leverage to a potential 4-fold increase in sales revenues. The earnings thus generated will go a way to bolstering the company's capital position, further supporting the pursuit of its objectives.

Even without this uplift in earnings the Balance Sheet looks strong, with a healthy Interest Cover of ~22x (FY10). What little debt there is sits in the Korean business, encompassing 'soft loans' provided by the Korean Government with no recourse to ICP in Australia¹⁵.

While the company did raise capital in Nov-09, it is not particularly capital intensive. The motive was to provide funds to the expansion of the plant facility (allowing it to meet the aforementioned increase in demand) and acquisition of IP, most recently the switching technology obtained from Pulse which allows the company's network to communicate with that of any bank.

It is this and other IP which underpins the company's value proposition, and will ensure that ICP maintains a relationship with the Korean company (with whom ownership of the supply contracts rest) should it divest its stake while moving towards the target model (not that we're suggesting it will). In any case, it seems unlikely the company would execute any such strategy without contracts being in place to secure supply.

With the Korean arm being the key element to success, the company not attaining its recurring revenue objective is a possibility, albeit earnings from the alternative outcome should still prove a good step-up on those of recent past.

In short, the risk that earnings track lower from here appears low, with a significant improvement the more likely outcome.

	2008	2009	2010	2011	2012	2013
Korea						
Sales Revenue	15.2	11.7	28.0	70.0	75.3	80.7
EBIT	0.1	0.2	3.3	14.7	15.8	16.9
Margin	0.8%	1.5%	11.9%	21.0%	21.0%	21.0%

(NB: numbers in above table represent 100% of the Korean subsidiary – ICP holds a 52% stake)

OUR VIEW

The company is still young, and credibility needs to be built before investors can start to feel confident the group will deliver what we have described.

Long term aspirations aside, if the group can demonstrate the earnings we expect them to deliver for h2-10 and into FY11 with the associated improvements in cash flow, the market will be forced to sit up and take notice. Indeed, if the company produces such a creditable result, what may seem like blue sky now could suddenly become relevant.

For those that wish to catch the worm, this warrants a harder look. **ACC. JM**

Shareprice		0.048					
Yr end 30 June		2008 A	2009 A	2010 F	2011 F	2012 F	2013 F
Reported profit bef SI	\$m	-2.5	2.5	4.6	7.8	8.5	9.3
Normalised Profit	\$m	-2.1	2.5	3.5	7.8	8.5	9.3
EPS	c	-0.3	0.3	0.5	1.0	1.0	1.1
P/E	x	-14.1	13.8	10.6	5.0	4.6	4.2
P/E Rel			89	81	44		
Dividend	c	0.0	0.0	0.0	0.0	0.0	0.0
Yield	%	0.0	0.0	0.0	0.0	0.0	0.0
Franking	%						
Normalised EPS Growth	%			30%	111%	9%	9%

Profit & Loss

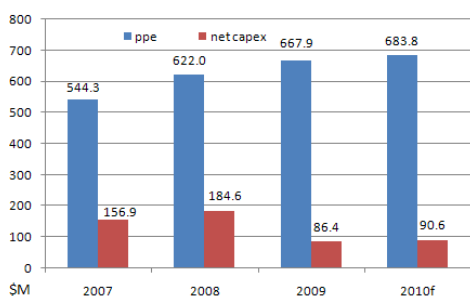
iCash	2009	2010	2011
Australia			
Sales Revenue	7.4	14.0	15.4
EBIT	0.9	3.4	3.8
Margin	12.7%	24.5%	24.5%
Korea			
Sales Revenue	11.7	28.0	70.0
EBIT	0.2	3.3	14.7
Margin	1.5%	11.9%	21.0%
Other	0.0	0.0	0.0
EBIT	1.1	6.8	18.5
Margin	5.8%	16.1%	21.6%
Interest Earned	0.1	0.1	0.1
Interest Capitalised	0.0	0.0	0.0
Interest Paid	(0.3)	(0.4)	(0.5)
Net Interest Expense	(0.2)	(0.3)	(0.4)
Pre tax Profit	0.9	6.5	18.1
Tax Expense	1.7	(0.4)	(5.4)
	2.6	6.0	12.6
Equity in Associates	0.0	0.0	0.0
NPAT before significant items	2.6	6.0	12.6
Minorities	(0.1)	(1.5)	(4.8)
	2.5	4.6	7.8
Extraordinary Items		(1.0)	
Reported NPAT	2.5	3.5	7.8
Depreciation	1.5	1.7	1.8

¹⁵ An accounting anomaly sees these classified as short-term despite the reality being to the contrary

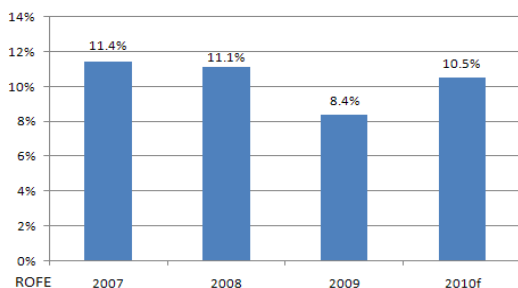
- We caught up with **Emeco (EHL)** CFO Stephen Gobby during the week. The discussion was timely, with the mining services sector under pressure amid proposed RSPT fears and global growth jitters.

The key takeaway was management's newfound focus on return on capital (ROC), which the group is now publicly preaching and privately enacting by rationalising its asset base. (We expect the group will release a strategy overview within the next five weeks, detailing its ROC aspirations and a roadmap by which it seeks to get there).

The importance of ROC targets can best be illustrated by the graph below, which illustrates the high capital intensity of the business.



With an average return on funds employed of 10.3% since IPO, the company has deployed vast sums of capital at inferior returns.



We believe that companies can streamline and “shrink themselves to greatness”. For Emeco, disastrous returns have been generated from the group's offshore foray in Europe and the US. (As at 31 Dec 2009, \$53M and \$116M of assets were tied up in the US and Canada, with these regions generating pre-tax losses of -\$1.1M in 1H10). Steps taken to boost returns include:

- In h2-10, management selling \$20M of equipment in US (40% of US value) and shifting equipment into Canada (most asset sales to be concluded by June 30. Equipment has been sold around book value).

- Europe has been exited (and now serves as a minor procurement hub). Between 2008 and 2009, Europe sustained cumulative EBIT losses of \$29M on assets of \$60M. (Offshore rationalisation has had the effect of eliminating US\$ and Euro exposure and establishing more natural hedges).
- A shift to bigger equipment (100t trucks + diggers) is underway, designed to sustain higher revenues and to avoid oversupply at the smaller end. (Lead times have pushed out to one year on new equipment vs 20wks in February). EHL is targeting \$160M capex in FY11 (similar to FY10).
- Enforcement of take-or-pay minimum hours on rental gear (equivalent to 400hrs/month on a 24/7 basis).
- Targeting double-digit returns vs low-teens WACC.

Against a backdrop of asset rationalisation, market conditions are improving: Qld coal (improving); NSW thermal (strong); WA iron ore (robust); Indonesian coal (quite strong); Canada (slowly improving but winter thaw has impacted). Group-wide utilisation is running around 80% (measured by number and by asset value); asset intensity is ramping up. (We would like EHL to report “true” utilisation, reflecting asset intensity on client sites and detailing hrs operations/mth).

FY10 guidance of \$40M-\$44M NPAT remains intact (EHL may resume DPS in FY10), although management believe that earnings will come in at the lower end. Moving into FY11, it is reasonable to annualise h2-10 NPAT of \$27M to estimate \$54M NPAT.

While the multiples appear undemanding (3x FY11f EV/EBITDA; 5.5x FY11f PE), the balance sheet remains a constraining factor for some investors (3.1x FY10 interest cover). This is a direct result of the pinch on operating cashflow from significant capex and the failed offshore strategies. Notwithstanding, asset backing is strong (71cps) and debt/EBITDA is less than 2x.

The relationship between ROE and book value holds (ie a company returning its cost of capital = 1x book) and we would expect EHL to re-rate towards book value (NTA is 71c cps) as returns improve. Watch out for the upcoming strategy update! ACC. TM.

Shareprice				0.48			
Yr end July		2008A	2009A	2010F	2011F	2012F	2013F
Reported profit bef SI & prefs	\$m	67.5	57.8	40.5	54.7	62.6	73.0
Normalised Profit	\$m	67.5	57.8	40.5	54.7	62.6	73.0
Normalised EPS	c	10.7	9.2	6.4	8.7	9.9	11.6
P/E	x	4.5	5.2	7.5	5.5	4.8	4.1
P/E Rel		30	33	56	47	44	40
Dividend	c	4.5	4.0	2.0	3.0	3.5	4.0
Yield	%	9.4	8.3	4.2	6.3	7.3	8.3
Franking	%	100%	100%	100%	100%	100%	100%
EPS Growth	%		-14%	-30%	35%	14%	17%

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