Morgan Stanley
ASIA INSIGHT

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Australia Media, Internet and Technology

Asia Insight: How Google, Facebook et al. are squeezing the revenue/profit pool of Australian TV, Newspaper and Radio companies

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As demand for advertising moves to be more Internet/digital/data based, we expect the major global players will take a bigger and bigger share of the ad market. This has profound negative implications for the earnings/valuation of the traditional media companies in our coverage universe.

When we talk to our industry contacts one message is clear, the rate of structural change brought about by technology is not abating, if anything it has quickened in the last 12 months and will again in C2016. This is the most significant issue facing every company in our coverage universe. Of course, writing about the structural change occurring in media is not new, everyone following the industry is cognizant of it. What we have attempted to do in this report, is present an alternative, but simple and hopefully effective framework through which to view this change.

Key conclusion: Global tech players are taking all the ad market growth, and then some. In C2016E we estimate global media/ad tech players, including the likes of Google and Facebook, will collectively extract A$4bn-A$5bn worth of ad revenue - representing 35-40% share of the total pool of ad revenues in Australia (A$13.9bn). Its a big number and critically, its growing fast - we estimate the leakage to global players increased 24% or ~A$1bn in C2015. Why is this important for our investment universe? because if the total Australian ad market only grew ~A$300m and global players collected an extra ~A$1bn, that means the revenue pool left for domestic media to compete for actually shrank by ~A$700m. Which hurts, and explains why most domestic media companies reported lower F2015 earnings.

Very negative read-across for Australia traditional media companies. Put simply, the more ad spend shifts from traditional media (e.g. TV/Print) to new media (e.g. Internet/Online), which it will, following the trends of how Australians consumer their media, the more $s will shift offshore to global media/ad tech companies and leave Australia. Therefore, the reality is, the pool of ad dollars left for local traditional media companies is not growing; its shrinking. **Valuation implications are profoundly negative - if the addressable market is shrinking in perpetuity, as we believe it is, these stocks warrant valuations at a substantial discount to historical and market multiples.** We reiterate our Underweight ratings on 4 TV/radio stocks SWM, NEC, SXL, PRT; and Equal-weight NWSA, SKT. We believe the market underestimates the risk to ad revenue, margins, ROE on a five-year view.

Australia Media, Internet and Technology	
Asia Pacific	
IndustryView	**Attractive**

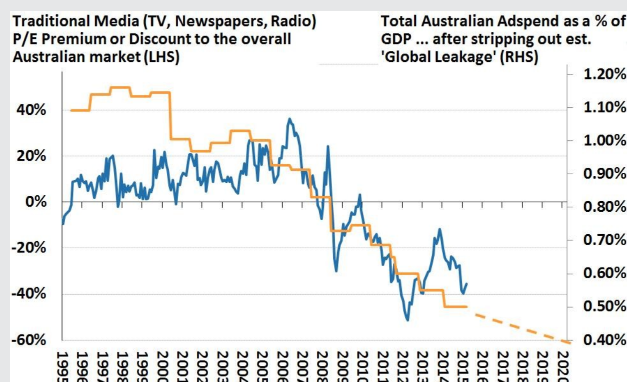

Exhibit 1: Traditional Media: Changes to Price Targets

	Price Target		EBITDA		EPS	
Company	Current	Previous	F2016E ($m)	% change	F2016E	% change
NEC.AX	A$1.50	A$1.50	204	0%	14.5	0%
SWM.AX	A$0.60	A$0.60	368	0%	12.9	0%
TEN.AX	A$0.25	A$0.25	37	0%	0.6	0%
APO.AX	A$6.40	A$6.40	82.9	0%	28.8	0%
FXJ.AX	A$1.20	A$1.20	311	0%	7.1	0%
PRT.AX	A$0.45	A$0.60	56	-3%	7.7	-6%
SXL.AX	A$0.80	A$0.80	173	0%	10.1	0%
APN.AX	A$0.90	A$1.20	164	-5%	7.3	-12%
SKT.NZ	NZ$5.00	NZ$6.10	339.4	-6%	40.1	-3%

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Debate: Is the negative structural change hurting Australian TV, Radio, Newspaper companies now fully factored in? ... is it time to re-visit shares?

Market's view: Unclear ... but after recent significant share price declines we expect some investors will, at the start of a new year, have another look at shares.

Our view: No ... our proprietary 'Global Leakage' of advertising framework suggests there is further downside risk to earnings and valuation over the next 5 years, which we argue, is not yet fully appreciated by the market. TV, Newspaper and Radio companies are mature and in the declining phase of their life-cycle ... on a 3-5 year horizon we forecast declining revenue, declining margins and falling ROEs. Thus, in the construction of portfolios, we would continue to avoid these - **we have Underweight ratings on 4 TV broadcasters SWM, NEC, SXL and PRT** ... and EW on NWSA and SKT. There are only a handful of positive exceptions in our view - FXJ for the rising and still undervalued growth in its Internet asset Domain; TEN as a contrarian view for an as yet unappreciated TV market share turnaround and APO, where we view digital panel billboards as a unique window for revenue growth.

Where we could be wrong?: If the traditional media companies of Australia are able to fight back and reverse the revenue market share gains of international players. Industry consolidation via relaxation of media ownership, could assist, providing greater scale.

Why are we considering this topic?

Traditional media stocks mostly traded significantly lower in C2015 ... PRT -46%, SWM -41%, APN -37%, SKT -24%, TEN -22%, NWSA -15%, NEC -1%, SXL +1% ... with only a few gainers FXJ +6%, APO +140%. At the start of a new year in 2016 it is time to reconsider whether it is appropriate to change our negative thesis on this group of stocks. Have the price declines been sufficient to reflect a poorer structural outlook for earnings? ... or is there still further negative news and downward revisions to earnings and asset values to come?

In this discussion we explore three key areas:

- **Firstly we step-through our "Global Leakage" framework.** Everyone knows traditional media platforms like TV, Newspapers, Radio are losing ad revenue share to the Internet/online, that's not new ... but our framework presents a different perspective on this, which centres on a bottom-up estimate of what global media/tech players like Google, Facebook etc are generating in revenue in the Australian market ... and therefore estimates the residual addressable market for traditional media. Pages 4-9.
- **Secondly, we explore the earnings implications of our Global Leakage conclusions.** In a nutshell, the implications are negative ... we see a 'crowding out' of domestic media companies. As global media/ad tech players continue to grow faster, leveraging their scale advantage with data/analytics etc. Put simply, Global takes a growing share of the market, leaving a shrinking pool for domestic traditional media to compete for. Pages 10-11.
- **Thirdly, we explore Valuation Implications.** Again, we think the implications of Global Leakage are decidedly negative. Admittedly, a meaningful de-rating of these shares has already occurred, historically TV, newspaper and radio stocks commanded a premium PE multiple to the overall market, they are now at a sizeable discount. Key point is that de-rating is warranted ... and permanent, in our view. Pages 12-14.

1. Our proprietary framework for estimating the size of 'Global Leakage' of adspend out of Australia

For a different perspective on structural change and how it is affecting our coverage universe ... we look through the prism of the addressable market ... or the total pool of advertising revenues which is available for all the media companies in our universe to pursue.

There are three steps to our framework:

1. Establish the level of total advertising expenditure (ad spend) in Australia, per annum – as a percentage of GDP.
2. Break down total ad spend into categories to illustrate the changes occurring in the composition of that total ad spend – e.g., Internet/Digital adspend increasing vs. Magazines/Print falling.
3. Make a bottom-up estimate of the total amount of Australian ad spend being collected by global media companies, such as Google, Facebook.

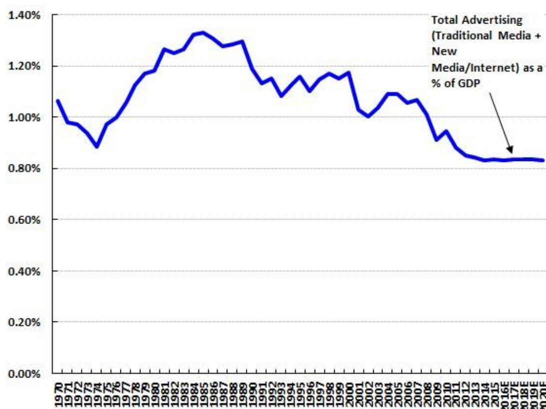
Thereafter, we can quantify the impact on future advertising from stripping out the global leakage ... and consider implications for the domestic media companies in our coverage universe in terms of valuation, outlook for earnings/margins, sustainability of dividends, appropriate debt leverage etc.

Step 1: Total Australian Ad Spend – as a percentage of GDP

In C2015 we estimate the total pool of advertising spend in Australia was ~A$13.6bn – see**Exhibit 25**, page 9. This equates to ~0.8% of total Australian GDP of A$1,637bn – see **Exhibit 2** below. Note this ad spend number is based "main media" only (i.e. TV, radio, newspapers, magazines, internet, outdoor, cinema), we exclude "below the line" ad spend, such as letter-box drops, catalogues, telemarketing, etc from this exercise.

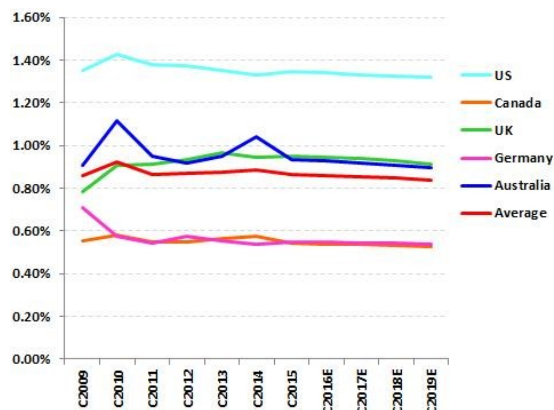
Looking forward, we assume this ratio remains steady for the remainder of this decade ... Australia is a developed, mature economy and we expect ad spend as a percentage of GDP to remain largely unchanged. This implies nominal advertising grows by an average 3% per annum over the next five years ... or a CAGR of +2.5% from A$13.6bn in C2015, up to A$15.4bn in C2020E.

Exhibit 2: Total Adspend as a % of GDP - Australia - a clear declining trend since early 1980s. For simplicity we forecast steady out to C2020E



Source: ABS, Morgan Stanley Research

Exhibit 3: For comparison ... Total Adspend as a % of GDP is forecast to remain steady in other developed markets Canada, Germany, UK and US



Source: IDC estimates, Morgan Stanley Research

Step 2: Changes occurring in the composition of Total Australian Ad Spend – as a percentage of GDP

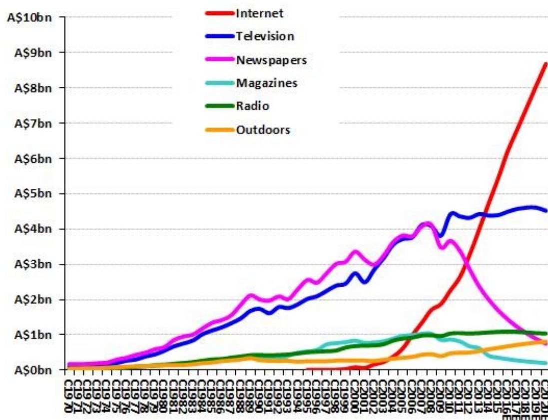
Following on from Step 1, we keep ad spend as a percentage of GDP steady at the ~0.8% level.

But, obviously, there are some substantial changes occurring in the composition of that ad spend over the remainder of the decade. In the main media catagories, these trends are already clearly observable. In our view, the rate of structural change is unlikely to reverse – if anything it may accelerate.

A few key categories:

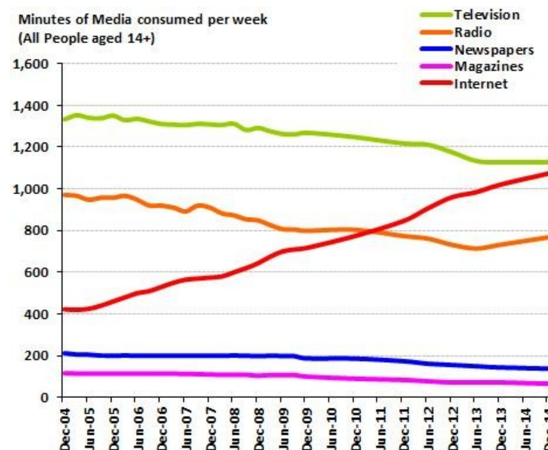
- **TV** ad spend is now forecast to flatline with 1-2% growth for next few years … and experience actual declines in C2020E, based on falling consumption/usage. We forecast FTA TV growth/margins/returns will fall sharply, suffering from streaming/IPTV's growth in viewers/users.
- **Newspaper** ad spend we forecast to decrease sharply by -7% to -8% p.a. out to C2020E, based on continuing declines in readership and circulation and falling consumer usage.
- **Magazines** we forecast to decline -8% to -9% p.a. out to C2020E, based on even sharper observable declines in readership and circulation.
- **Radio** ad spend we forecast modest positive growth of 2-3% p.a. for the next three years, then negative -1% to -2% in later years. We expect Internet streaming players, such as Spotify and Pandora, will ultimately have a negative impact on broadcast radio's growth.
- **Outdoor** ad spend, is the only traditional media category experiencing growth. We forecast 7%-8% pa for next 2-3 years. Unlike TV/newspapers/radio where consumer usage is falling … Outdoor audiences are growing and digital panels are attracting additional dollars.
- **Internet/Digital Media** ad spend we forecast continuing strong growth of 10%-15% p.a. This may appear aggressive but we highlight two points: i) the forecast is really just a continuation of the trend already observable from C2000-C2015; and ii) a sustained period of super-strong growth such as this is not unprecedented. For example, look at the growth achieved by TV and newspapers in 1973-1982, when these media increased between 20%-50% pa for a decade. We expect growth to be fuelled by social network ad spend in Australia – Facebook, Instagram, LinkedIn, et al.

Exhibit 4: Changing Composition of Adspend in Australia Over Time … Internet and Outdoor Rising … All Else Falling



Source: Morgan Stanley Research Estimates

Exhibit 5: Changing Patterns of Time Spend With Media in Australia … Are The Driving Force Behind the Adspend Changes

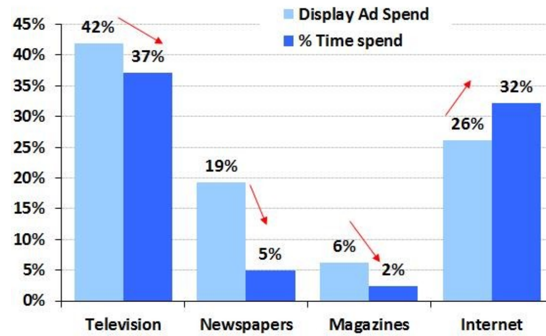


Source: Roy Morgan, Morgan Stanley Research Estimates

Why do we forecast the recent structural changes in adspend patterns to continue? Essentially it is driven by the changing patterns in how Australians consume their media. Looking out to C2020E we expect consumers will continue to spend less time with newspapers/magazines, FTA TV and radio ... and more time Internet/Online media (including streaming TV/radio services). **Where eyeballs go ... we predict adspend will follow -** see Exhibit 6 opposite.

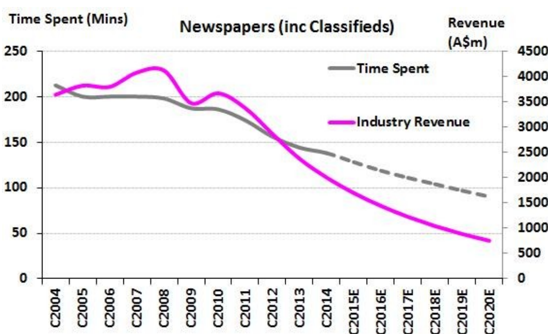
We present our outlook for time spent vs. our forecast for adspend in each of newspapers, magazines, radio, outdoor ... and internet/online in Exhibits 7-12 below.

Exhibit 6: Adspend vs. Time Spent



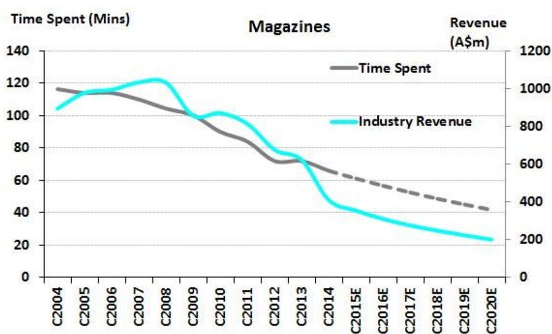
Source: Roy Morgan, Morgan Stanley Research

Exhibit 7: Newspaper Adspend vs. Time Spent



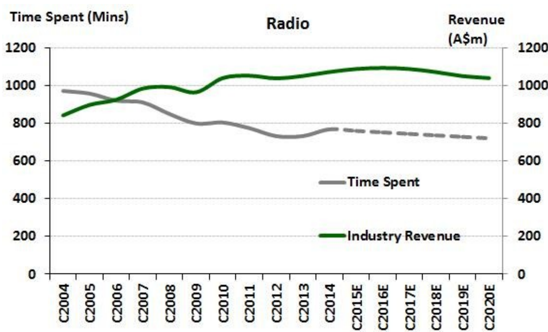
Source: Morgan Stanley Research Forecasts, Roy Morgan

Exhibit 8: Magazine Adspend vs. Time Spent



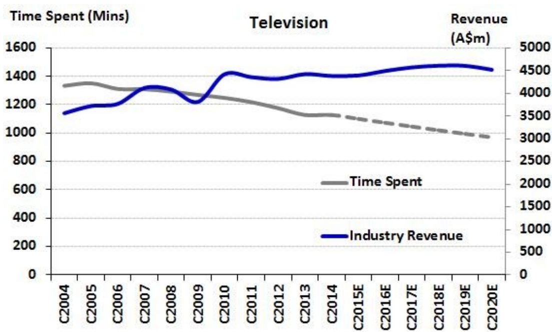
Source: Morgan Stanley Research Forecasts, CEASA, Roy Morgan

Exhibit 9: Radio Adspend vs. Time Spent



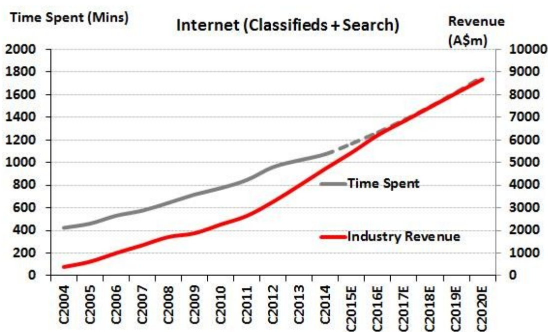
Source: Morgan Stanley Research Forecasts, CRA,Roy Morgan

Exhibit 10: FTA TV Adspend vs. Time Spent



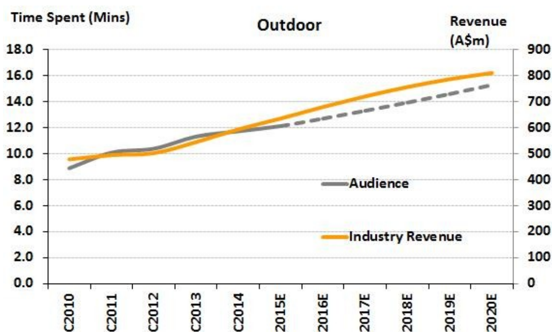
Source: Morgan Stanley Research Forecasts, FreeTV, Roy Morgan

Exhibit 11: Internet Adspend vs. Time Spent



Source: Morgan Stanley Research Forecasts, CEASA, Roy Morgan

Exhibit 12: Outdoor Adspend vs. Time Spent



Source: Morgan Stanley Research Forecasts, OMA, Roy Morgan

As a result of these very different growth rates , large changes in the mix of advertising are forecast to continue - see **Exhibit 13** at the bottom of this page:

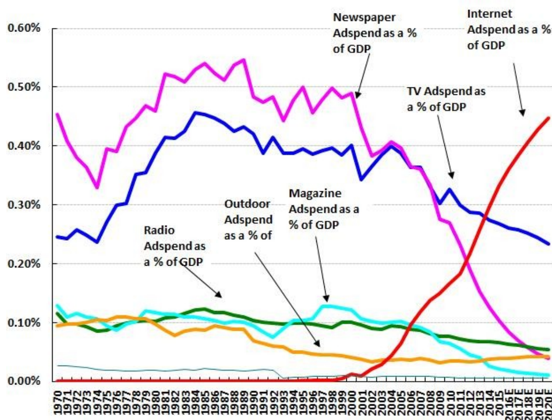
- **TV's share is forecast to decline.** In C2015 it represented for 0.27% of Australian GDP, by C2020E we forecast a lesser 0.23% as consumers have a substitute product in the form of streaming TV. Our industry data dates back to 1970, and interestingly shows TV's share vs. GDP has been in a declining trend since the 1980s, we estimate peak was 0.46% in 1984.
- **Newspaper ad spend set for share declines.** We estimate from 0.10% of GDP in C2015, down to 0.04% in C2020E. Also in long-term structural decline, newspapers' share peaked at 0.55% of GDP in 1989.
- **Magazine ad spend to keep declining.** From 0.02% in C2015, to 0.01% in C2020E. Spiralling lower from a peak share of 0.13% in 1997.
- **Radio ad spend will decline, but not as sharply as print.** From 0.07% of GDP in C2015, down to 0.05% in C2020E.
- **Outdoor is the one bright spot among 'traditional media' ... we forecast rising share.** Outdoor ad spend was 0.032% in C2012, increasing to 0.039% in C2015, we forecast 0.042% in C2020E. Interestingly, outdoor's share of adspend was much higher in 1979 at 0.12% of GDP, before tobacco advertising was prohibited.
- **Internet/Online ad spend is expected to be the main area of growth.** Increasing from 0.33% of GDP in C2015, up to 0.44% in C2020E.

Next important step ... we recast the numbers in **Exhibit 14**, in two categories:

- Total ad spend in Australia ... and
- Total ad spend ... but **excluding Internet/Digital ad spend**

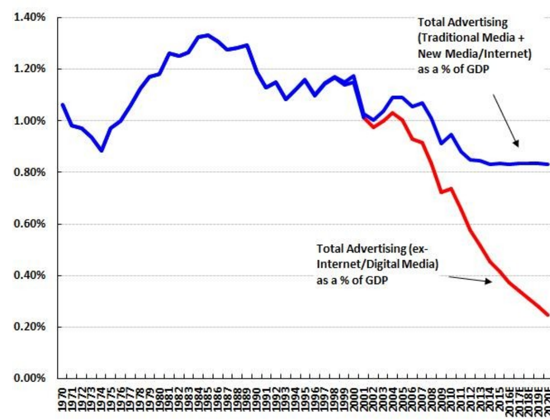
As we stated earlier, we forecast total advertising to remain constant at ~0.8% of GDP over the forecast period to C2020E. Our view is that Australia is a mature, developed industrial country, where advertising expenditure by corporate and governments will continue to register positive growth, but broadly in line with the economy. Australia is not a developing economy like, say, China or India, where advertising as a percentage of GDP is rising. **But, while total Australian adspend as a % of GDP is steady ... look below the surface ... and the key point is total adspend excluding Internet/Online is falling sharply - from 1.0% in C2005 down to 0.4% in C2015** ... and forecast to halve again to 0.25% in C2020E.

Exhibit 13: Changing Composition of Adspend in Australia - as a % of GDP



Source: CEASA, Morgan Stanley Research Estimates

Exhibit 14: Total Australian Adspend as a % of GDP ... Stripping-out Internet/Digital component



Source: CEASA, Morgan Stanley Research Estimates

Step 3: Quantifying the significance of global media/tech players ... within the total Australian advertising revenue pool

The advertising dollars being collected by global media/tech players in Australia are already significant ... and growing fast.

Key points:

- In C2015, we estimate global media/tech players in aggregate collected **A$3.5-A$4.1bn** worth of advertising/marketing revenue out of Australia.
- That A$3.5-4.1bn **accounts for ~30%** of total Australian ad revenues of A$13.7bn in C2015.
- ... and it's growing fast ... we estimate the growth rate was **+25% to 30% on pcp in C2015,** whilst overall adspend in Australia only increased by 2-3% in C2015.

To be clear, the A$3.5-A$4.1bn is our bottom-up estimate, derived from global company financial accounts/presentations, ASIC filings and industry sources. We estimate the largest individual contributors are Google Australia and Facebook Australia ... but it includes many others, all growing fast, off a low base, such as LinkedIn, Microsoft/Bing, Yahoo!7 (we include 50% owner Yahoo! Inc's share as global), Twitter, Daily Mail, Huffington Post and adtech players with Australian operations such as Criteo, Adroll etc.

Some more detail on the two largest global contributors:

- **Alphabet Inc** (covered by Brian Nowak and team; GOOGL.O; rated Overweight; US$820; PT US$820) in its most recent financial results GOOGL reported Q3 C2015 constant currency revenue growth of +21%. For the full year C2015 consensus forecast for total revenues of US$75bn (A$103bn).
- Individual results for Google in Australia are not disclosed. But to put this into context, we estimate Google's revenues in Australia for full year C2015 to be in the range of A$2.5-A$3bn (US$1.8-US$2.2bn), which equates to approximately 2-3% of total Google revenues.
- Australia is part of Alphabet's Rest of World revenue (estimated 47% of total revenue in 2015) which increased by +23% in Q3 C2015.
- Australia has been part of Alphabet's Rest of World revenue **deployment of the Android ecosystem** which has led to a dominant and (through the mobile transition) growing global paid search market share ... and Australia is no different. Our US team expects GOOGL's Rest of World will continue to be an important part of Alphabet's global growth and earnings power ... **as we see that Rest of World will drive over half (52%) of forward revenue growth looking forward to 2018** (See Exhibit 15).

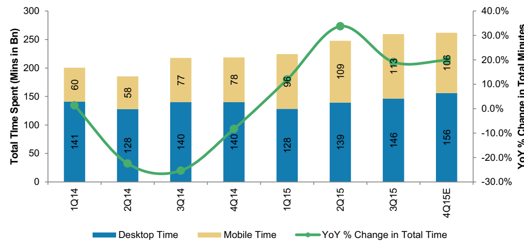
Exhibit 15: We estimate that Rest of World will drive over half (52%) of core GOOGL revenue through 2018

Core GOOGL Revenue (ex-FX, mn USD)	2013	2015E	2018E	2013-2015E CAGR	2015-2015E CAGR	2013-2015E Contrib to Growth	2015E-2018E Contrib to Growth
US	25,587.0	34,441.5	47,722.6	16.0%	11.5%	39.0%	43.1%
UK	5,604.0	7,339.7	8,821.3	14.4%	6.3%	7.6%	4.8%
ROW	24,836.0	36,963.1	53,045.0	22.0%	12.8%	53.4%	52.1%
Total	**56,027.0**	**78,744.2**	**109,588.8**	**18.6%**	**11.6%**	**100.0%**	**100.0%**
ROW as % of Total	**44.3%**	**46.9%**	**48.4%**				

Source: Company data, Morgan Stanley Research estimates

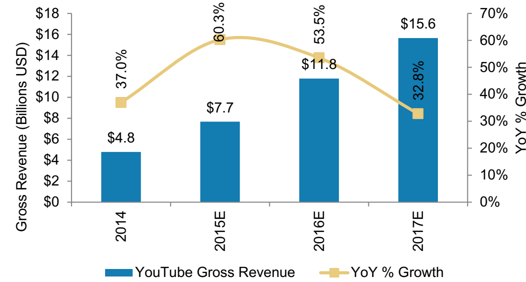
- Brian Nowak and team recently lifted GOOGL C2016 non-GAAP EPS by 6% with drivers including accelerating Mobile Search and growing YouTube user engagement and revenue growth - see Exhibits 16 and 17 below extracted from the team's report - for full detail refer to *Online Advertising: Follow the Revisions (13 Jan 2016)*.

Exhibit 16: Total time spent on YouTube is growing 20% YoY...



Source: comScore, Company Data, Morgan Stanley Research

Exhibit 17: ... while YouTube gross revenue accelerated to ~60% growth in 2015...



Source: comScore, Company Data, Morgan Stanley Research

- And **Facebook Inc** (also covered by Brian Nowak and team; FB.O; rated Overweight; US$130; PT US$130) in its most recent financial results reported Q3 C2015 constant currency ad revenue growth of +57%.
- Individual results for Facebook in Australia are not disclosed. We estimate Facebook's revenues in Australia for C2015 to be in the range A$500m-A$600m (US$365m-$437m) equating to 2-3% of total Facebook revenues of US$18bn in C2015.

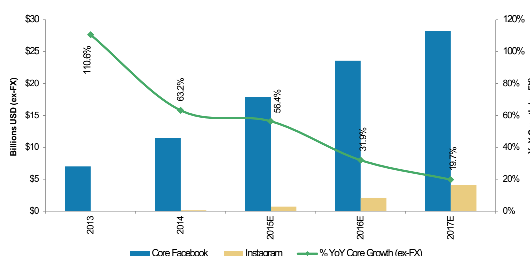
Exhibit 18: FB's increased monetization of Asia users a material earnings driver

Ad ARPU per DAU	2016E
North America	$61.97
Europe	$27.83
Asia	$11.87
ROW	$10.62

Source: Company data, Morgan Stanley Research

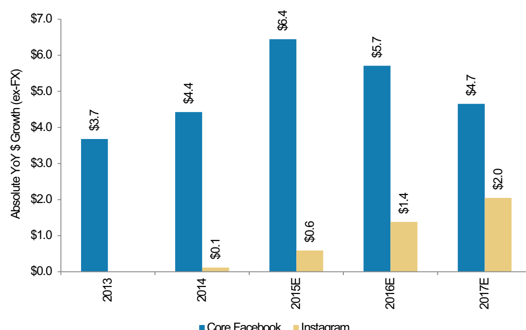
- Our US team's view is that FB's growth story continues to be its global user base and monetization per user continues to rise. But despite its success, we note that Facebook's ability to increase the monetization of its "Asia" region users (where Australian users are included) represents a material tailwind and long-term earnings driver. As down in Exhibit 18, **Facebook's ad revenue per daily active user in Asia is still ~80% less than North America and ~57% less than Europ e**. Looking ahead, our US team sees rising monetization within this 370mn (and growing) DAU user base driving higher earnings growth.
- The team recently lifted FB C2016 non-GAAP EPS by +10% with a number of drivers including Instagram user and ad revenue growth - see Exhibits 19 and 20 from the team's report.

Exhibit 19: We see Instagram revenue ramping to US$2bn in 2016, and model the core business to slow to ~32% growth ex-FX



Source: Company data, Morgan Stanley Research estimates

Exhibit 20: Core FB to add US$5.7bn in C2016



Source: Company data, Morgan Stanley Research estimates

The key point for investors is … we estimate International media/ad tech players currently collect 70-80% of all Internet/online advertising in Australia, or A$3.8bn-A$4.1bn out of total Internet/online revenue pool of A$5.4bn in C2015. Looking forward **as Internet/online becomes a bigger and bigger part of the overall ad pie in Australia - we estimate it is currently 39% - the bigger it becomes, progressively the bigger will be the claim on Australian ad revenues by international players.**

In summary, we estimate in C2015 there was A$5.4bn spent on Internet/digital advertising in Australia, which broadly speaking can be divided into 3 categories:

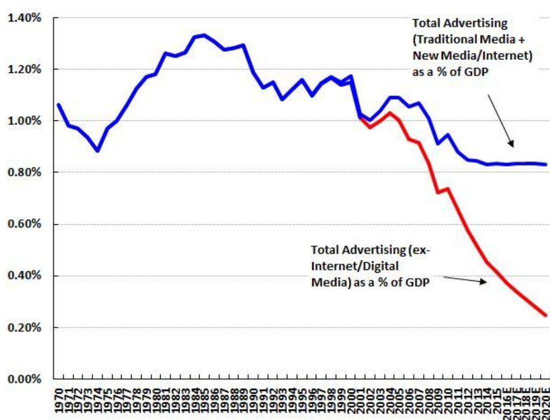
- **Online Search & Directories advertising** - worth A$2.8bn. It is the largest category and is virtually 100% international players, dominated by Google with +90% market share. The majority of the rest split between other internationals, such as Bing.
- **Online Display/brand advertising** - A$1.7bn. Which we estimate international players, such as Google/YouTube and social networks such as Facebook/Instgram/Twitter/Snapchat collectively have a 50-60% market share.
- **Online classified advertising** - worth A$0.9bn. This, in contrast, is dominated by local players, not international players - such as SEK in online jobs; REA and Domain in online real estate and CAR in online car ads. It is though, the smallest online adspend category.

So all-up, international players dominate Search & Directories … and also collectively have the largest share of Display in Australia … these are the two largest revenue pools online. The only area they are absent is in online classifieds. But, in total we estimate International/global players with revenues of A$3.8bn to A$4.1bn account for between 70-80% of the estimated C2015 pool of Internet/online adspend worth A$5.4bn.

Note, we are only capturing advertising/marketing spend in this analysis. Also relevant for our Media coverage universe is the Global Leakage occurring in the area of TV/film content - to global online/streaming players such as Netflix, Amazon/Prime, Hulu, AppleTV, HBO Online, BBC Online. Taking content/subscription dollars away from Australian payTV/FTA TV operators. But that is beyond the scope of this report.

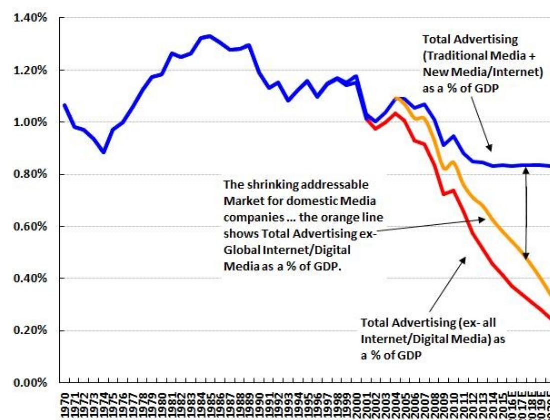
The next important consideration in this debate, is what are the implications for the Australian domestic media companies … as the % of adspend being captured by global players continues to rise … leaving a smaller and smaller residual revenue pool for domestic media companies to compete for. We explore the earnings implications on page 10 … and valuation page 12 of this report.

Exhibit 21: Total Australian Adspend as a % of GDP … ex Internet/Digital Adspend



Source: CEASA, Morgan Stanley Research Estimates

Exhibit 22: Finally … stripping out Global Leakage … Total Australian Adspend for domestic players



Source: CEASA, Morgan Stanley Research Estimates

2. Earnings Implications ... for Australian traditional Media companies, of Global Leakage

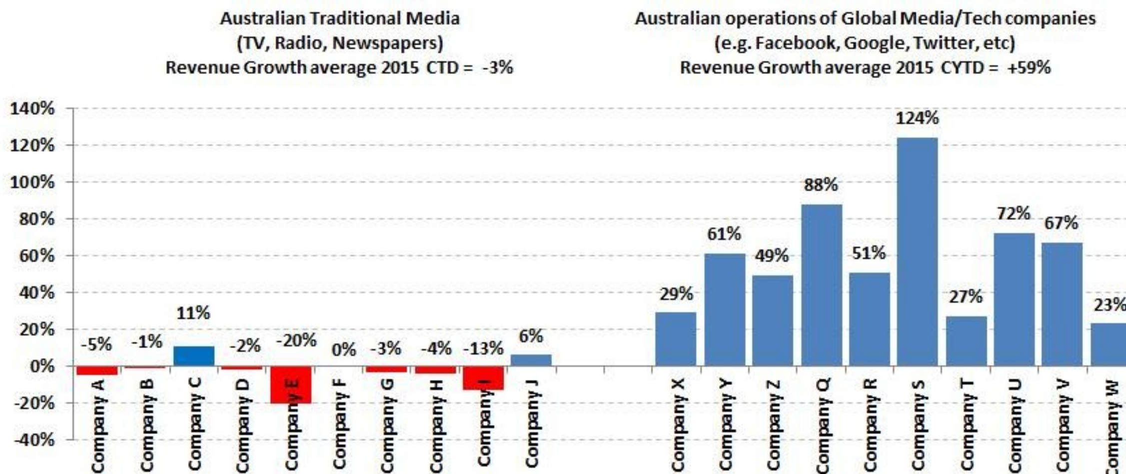
We believe the implications are significantly negative for revenue (and therefore EPS) of the domestic media companies in our universe ... in a nutshell we see a **'crowding out'** of domestic media.

Let's say total ad spend stays approximately the same as a percentage of the total Australian economy (which we believe it will, at say ~0.8% of GDP) ... then the more ad spend moves to the Internet/online ... the more ad dollars will be leaking to global media/ad tech players, such as Google and Facebook, which dominate that space. This is great for them, but not so great for the domestic Australian media companies. Why? Because the pool of ad dollars left over, which becomes the addressable market for which the domestic media companies, has by our estimate stopped growing and started to shrink.

Key points:

- In C2015, we estimate 39% of total adspend in Australia was on Internet/online, i.e. A$5.4bn out of total market A$13.7bn. We expect this to increase steadily over the next few years, reaching 55-60% of total adspend by C2020E.
- Global media/ad tech players currently capture an estimated 70-80% of that Internet/online adspend in Australia (discussed page 6).
- And, importantly, we can't see their grip loosening any time soon. Why? Because the **global players have a huge scale advantage in terms of data/analytics etc, which is increasingly driving the destination for adspend and marketing. That advantage enjoyed by the big global players, if anything, continues to increase.** Thus, it's not surprising that despite their already substantial size in this market, we estimate Google and Facebook still grew revenues between +29% to +61% in Australia in C2015. In addition, there is a growing list of other US/international peers now developing a local presence in this market, with on-the-ground ad sales teams etc , such as YouTube, Twitter, LinkedIn; whilst relatively small in absolute $ terms, from that base they are achieving meaningful growth in display/brand ad revenues, up an estimated average +59% in Australia in C2015 - Exhibit 23.

Exhibit 23: Starkly different revenue growth rates observable ... Top 10 traditional media companies average -3% in C2015 ytd... vs. international media/tech companies in Australia average +59%



Note: We are unable to publish the names of individual company revenue growth rates presented in this Exhibit.
Source: SMI, Morgan Stanley Research

Looking forward … what is worrying for domestic media companies is the severity of *global leakage*, or crowding out, which will likely increase as Australian corporates shift their ad spend online , where global media/ad tech players dominate. Looking out to C2020E we estimate global players could account for A$8bn-A$10bn or 50-60% of total A$16.1bn advertising in Australia. That is a big number, although it represents a 5-year of CAGR of only +18% on the A$4bn-A$5bn global leakage number we estimate for C2015 (**Exhibit 24**). Not unfathomable in light of current +59% revenue growth (**Exhibit 23**).

It is our view that the market has not fully factored in a scenario for domestic media ad revenues, which is consistent with our analysis for an extended period on continual sharp declines in domestic ad revenues. We compare our trajectory of declines for domestic ad revenue, based on top-down analysis of global leakage … with bottom-up estimates for domestic media companies (i.e., APN, APO, FXJ, NEC, NWS, OML (not covered), PRT, SWM, SXL, TEN) – see **Exhibit 25**.

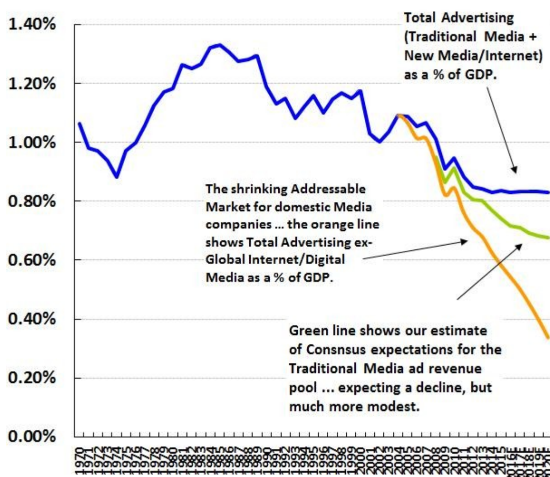
The difference is significant. Consensus (Thomson, Bloomberg) estimates reflect a much softer gradual decline in overall Australian traditional media ad revenues over the next five years (CAGR -1% to C2020E), versus our Global Leakage framework implied sharper fall (CAGR -7%) - see **Exhibit 24**

There are two possible explanations:

- Our top-down estimates of shrinking domestic ad revenues are too harsh. The market does not believe the consequences of the continued growth of Google, Facebook and others are as severe as we suggest in our analysis.
- Or, the market has not fully considered the implications of the concept of "global leakage" of ad revenues yet. This would mean significant downgrades to consensus expectations were likely for the medium- and long-term earnings of APN, FXJ, NEC, SWM, SXL, TEN etc…at some point in the future.

Bottom line, if our thesis on Global Leakage proves accurate, then consensus revenue estimates (and therein consensus EPS estimates) look too high for traditional media companies. **We see a *crowding out* effect if the major global media/tech companies, such as Google/YouTube, Facebook/Instagram … continue their current revenue growth trajectory in Australia.** Next we consider valuation implications.

Exhibit 24: Consensus Expectations … are for a mild decline in Traditional Media adspend in Australia … at a CAGR of -1% from A$9.5bn to A$9bn in C2020E



Source: CEASA, Morgan Stanley Research Estimates

Exhibit 25: Our Global Leakage framework … points to Traditional Media adspend declining much more severely at CAGR of -7% from A$9.5bn to A$6.5bn in C2020E

Source: CEASA, Morgan Stanley Research Estimates

3. Valuation Implications ... for Australian traditional Media companies, of Global Leakage

As well as earnings implications, we believe there are also valuation implications from this global leakage thesis ... as growth rates in revenue slow, so too will future growth rates of earnings and free cash flow generation.

Three key points:

1. **The market will adjust for this either by applying lower earnings capitalisation multiples for media stocks (lower P/Es, or EBITDA multiples), or in a DCF approach, a higher WACC/cost of capita**l i.e., because of lower terminal growth rates, and/or possibly higher betas to reflect greater intensity of competition in a declining industry.
2. **Clearly, the market has made some significant adjustment for this already.** As traditional media stocks are already trading at much lower multiples today than in the past - see Exhibit 26 - with the typical trading range shifting from 15x-20x ... down to current 5x-10x. Our view is that the traditional media sector's de-rating, which has already occurred since C2008, is justified, is permanent, and won't reverse.
3. **Of course, there will likely be some shorter periods of multiple expansion in media stocks, associated with: i) cyclical upswings ... and/or ii) M&A activity as the industry eventually enters a consolidation phase.** For example, in C2016 we could experience a moderate cyclical recovery but longer term and through the economic cycle we believe the de-rating of domestic media relative to the market is permanent – in fact, it could have further to go as the rate of change accelerates; i.e., the faster ad spend moves online, then the faster it moves to global players – and the faster is the shrinkage of the addressable market left over for domestic media players.

Historical perspective

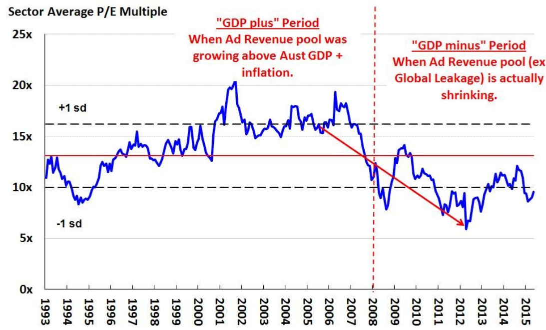
Over the past two decades there have been three main phases for the Australian media industry in terms of growth and valuation:

a) The "Golden Years" ... when media was a "GDP-plus" industry:

In the 1990s-2002 when total advertising revenue in Australia consistently grew between 5%-10% annually, the media industry was broadly considered a "GDP-plus" industry as advertising revenue growth consistently outstripped GDP growth of 3%-4%. Moreover, the total ad revenue pool was healthily positive in real terms. Advertising as a percentage of GDP ranged between 1.0%-1.2%.

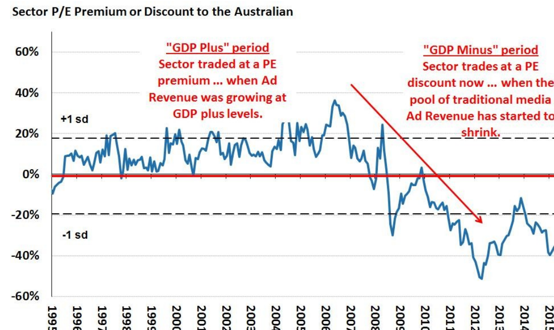
Not surprisingly, this coincided with a period when media equities were broadly considered growth stocks and generally traded at premium P/E multiples compared to the broader Australian market – see **Exhibit 27**. There was no Global Leakage of adspend to speak of during this period. Global/international media/technology players had zero presence in Australia.

Exhibit 26: P/E Multiples … TV/Newspaper/Radio stocks in Australia have seen a de-rating from 15x-20x to 5x-10x … coinciding with Adspend falling as a % of GDP.



Source: Thomson, Morgan Stanley Research

Exhibit 27: P/E Premium … relative to Australian market has shifted from a historical premium to a current discount … coinciding with Adspends falling as a % of GDP.



Source: Thomson, Morgan Stanley Research

b) Recent Past … media considered a "GDP in-line" industry: From 2002-08 when total advertising revenue in Australia grew on average 4%-5%, the media industry was widely recognized as starting to mature.

The total advertising pool was growing broadly in line with GDP growth of 3-4%. The total ad revenue pool was experiencing flat to low single-digit growth in real terms, during a period when inflation averaged 2-3%. Advertising as a percentage of GDP moved into a lower range of 1.0%-1.1%.

During this period traditional media equities were broadly no longer considered growth stocks, but generally still averaged a "market multiple". Global leakage of advertising was in its early stages, growing from 0% of the ad pool in C2004 up to 7% of total advertising by C2008, but remained largely indiscernible.

c) Present and the future … will domestic media be considered "GDP minus"?

From 2009-onwards we estimate total advertising revenue in Australia will record negative revenue growth in real terms. Critically, this is after stripping out the ad revenue captured by global players. On this basis, advertising as a percentage of GDP, has fallen below 1.0% to a range of 0.8%-0.9%. This has coincided with a period of de-rating of the media equities, which now broadly trade at lower multiples to the market. Looking forward, if advertising as a percentage of GDP (ex-global) continues to fall … we believe further de-rating is entirely possible.

Of course there will be periods, where domestic/local media companies will still be able to achieve positive revenue and earnings growth, for example when there is a cyclical upturn in advertising revenue; or when its businesses are winning market share from competitors; or if extra shareholder capital is deployed to make acquisitions (further industry consolidation is another likely implication). There will always be individual winners – but in aggregate, the industry loses, in our view.

Bottom line on valuation implications … whilst a meaningful P/E de-rating has already occurred in these stocks, we believe there is still risk to multiples ahead. If the market is underestimating the potential negative implications of Global Leakage on revenue/earnings over the next five years … we think too there is still meaningful risk to asset values.

Conclusion on this debate - is it time to take a more positive view on Australian traditional Media stocks? ... we say no

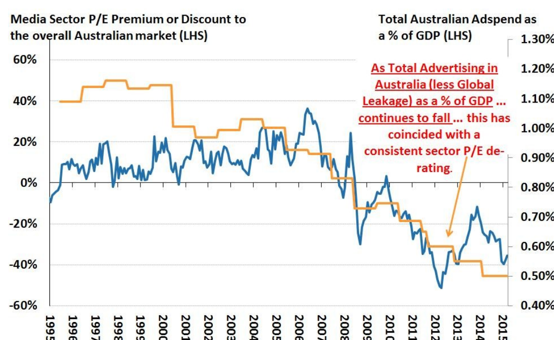
Everyone knows there is structural change occurring in the media industry – it's not a new concept – but what we have outlined in this report is a different perspective on how to think about it.

Our thesis is simple ... if total advertising stays steady as a percentage of the total Australian economy (which we believe it will, Australia being a mature, developed economy) ... then the more ad spend moves to the Internet/online (currently 39%, we forecast increasing to 55% by C2020, which may prove conservative) ... then the more ad dollars will be leaking to offshore global media / ad tech players, such as Google, Facebook etc. This simply means, what is left ... or the addressable market of advertising dollars for which the local/domestic media companies compete ... will be shrinking in real terms (and potentially nominal terms as well). The key numbers: we estimate ad spend as a percentage of GDP for domestic media companies will fall from 1.0% in C2008 ... down to 0.3% in C2020E (**Exhibit 24**). That is significant.

The bottom line on Global Leakage ... we see this analysis as supportive of our view that in the construction of portfolios, investors should be underweight the traditional media stocks - TV broadcasters, radio broadcasters, newspaper/magazine publishers. Whilst we believe there is a prospect of a modest cyclical bounce in advertising in C2016, aided by improving consumer/business confidence, the Rio Olympics and likely Federal election ... we expect any outperformance of traditional media equities will be relatively short-lived ... because over the medium and longer term we believe the global leakage of an increasingly large percentage of the pool of advertising dollars in Australia is a significant issue. It means the profitability and returns of the domestic media industry face continual downward pressure ... and the associated de-rating of those stocks will be permanent.

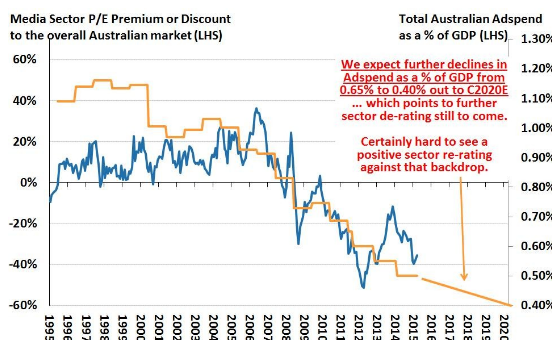
We reiterate our Underweight ratings on 4 TV broadcasters SWM, NEC, SXL and PRT ... and EW on NWSA and SKT. In these cases, we believe the market is underestimating downside to revenue, margins and ROE on a five-year view. We have only a handful of positive exceptions to our generally bearish view of traditional media, which are situation specific - FXJ, not for its newspapers (which are in decline), but for the rising and still undervalued growth in its Internet asset Domain (+70% of EV); TEN as a contrarian view for an as yet unappreciated TV market share turnaround, working in partnership with new strategic partner FOXTEL ... and APO where we view the continued rollout of digital panel billboards as providing a unique window (but not in perpetuity) for revenue growth and margin expansion.

Exhibit 28: Traditional Media Stocks P/E De-Rating ... we argue coincides with a period of significantly declining Adspend as a % of GDP in Australia



Source: Thomson, Morgan Stanley Research

Exhibit 29: Is Further De-Rating Possible? ... Yes, we think so ... based on our Global Leakage framework predicting Adspend as a % of GDP will continue to fall out to C2020E.



Source: Thomson, Morgan Stanley Research estimates

Companies featured in this report

Risk-Reward, Valuation and Earnings Estimates

Following we present the risk-reward framework, valuation summary and earnings estimates for the 10 traditional media companies mentioned in this report.

Key points:

- **No further change after recent cuts - NEC, SWM, TEN**. Late last year we cut our earnings estimates for TV broadcasters NEC (24 November 2015), SWM (24 November 2015) and TEN (24 November 2015).
- **No change after recent increase - APO.** On the flip side, in late C2015, we increased our earnings estimates for Outdoor company APO (4 Dec 2015).
- **In this report we make new estimate cuts - APN, PRT, SKT.** We revise our earnings lower for APN C2015E EPS -12% (see page 38); PRT F2016E EPS -6% (page 32); SKT F2016E EPS -3% (page 41). Our price targets move lower as a result.
- We have made no change to FXJ and SXL.

Exhibit 30 below summarises the major changes.

Note: The 10 traditional media companies featured in this report represent a sub-set of our total coverage universe of 15 companies in Australia Media, Internet & Technology.

Exhibit 30: Summary of Morgan Stanley Price Target and Earnings Estimate Changes

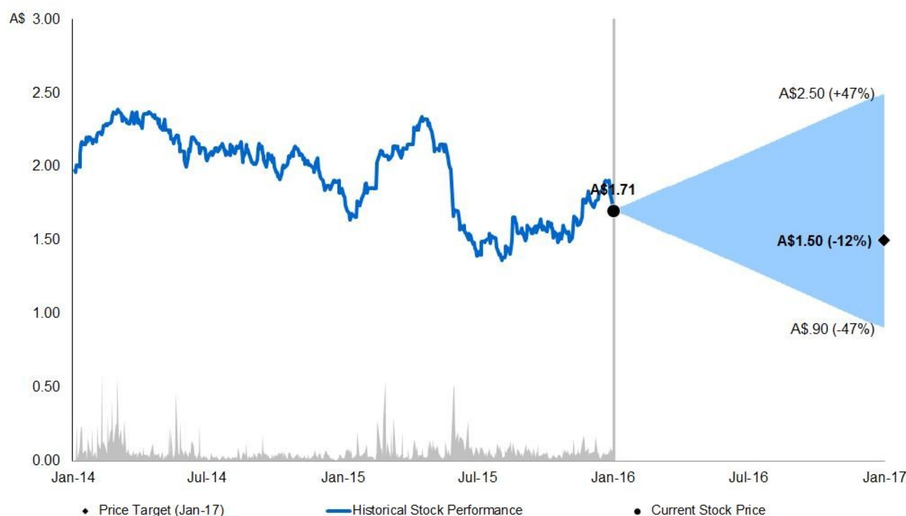
		Price Target		EBITDA				EPS			
Company	Ticker	Current	Previous	F2016E ($m)	% change	Consensus	MS vs. Cons (%)	F2016E	% change	Consensus	MS vs. Cons (%)
Nine Entertainment	NEC.AX	A$1.50	A$1.50	204	0%	220	-7%	14.5c	0%	15.4c	-6%
Seven West Media	SWM.AX	A$0.60	A$0.60	368	0%	364	1%	12.9c	0%	12.8c	1%
Ten Network Holdings	TEN.AX	A$0.25	A$0.25	37	0%	18	106%	0.6c	0%	-0.1c	700%
APN Outdoor	APO.AX	A$6.40	A$6.40	83	0%	80	3%	28.8c	0%	27.5c	5%
Fairfax Media	FXJ.AX	A$1.20	A$1.20	311	0%	307	1%	7.1c	0%	6.5c	9%
Prime Media Group	PRT.AX	A$0.45	A$0.60	56	-3%	58	-3%	7.7c	-6%	7.9c	-3%
Southern Cross Media	SXL.AX	A$0.80	A$0.80	173	0%	169	2%	10.1c	0%	10.0c	1%
APN News & Media	APN.AX	A$0.90	A$1.20	164	-5%	160	2%	7.3c	-12%	7.3c	0%
Sky Network Television	SKT.NZ	NZ$5.00	NZ$6.10	339	-6%	347	-2%	40.1c	-3%	40.7c	-1%

		Price Target		EBITDA				EPS			
Company	Ticker	Current	Previous	F2017E ($m)	% change	Consensus	MS vs. Cons (%)	F2017E	% change	Consensus	MS vs. Cons (%)
Nine Entertainment	NEC.AX	A$1.50	A$1.50	215	0%	235	-9%	15.5c	0%	17.5c	-11%
Seven West Media	SWM.AX	A$0.60	A$0.60	303	0%	324	-6%	10.3c	0%	11.3c	-9%
Ten Network Holdings	TEN.AX	A$0.25	A$0.25	55	0%	35	57%	0.9c	0%	0.2c	350%
APN Outdoor	APO.AX	A$6.40	A$6.40	98	0%	91	8%	34.5c	0%	31.7c	9%
Fairfax Media	FXJ.AX	A$1.20	A$1.20	328	0%	312	5%	7.8c	0%	6.9c	13%
Prime Media Group	PRT.AX	A$0.45	A$0.60	51	-7%	55	-7%	6.8c	-12%	7.9c	-14%
Southern Cross Media	SXL.AX	A$0.80	A$0.80	176	0%	172	2%	9.9c	0%	10.3c	-4%
APN News & Media	APN.AX	A$0.90	A$1.20	160	-6%	162	-1%	7.5c	-12%	8.0c	-6%
Sky Network Television	SKT.NZ	NZ$5.00	NZ$6.10	336	-3%	347	-3%	39.4c	-3%	40.2c	-2%

Source: Morgan Stanley Research, Thomson Reuters

NEC Risk-Reward

P/E Looks Low vs. History – but Can Be Misleading in View of Earnings Risks Ahead



Source: Thomson Reuters (historical share price data). E = Morgan Stanley Research estimates

Price Target A$1.50	Base case, blended methodology
Bull A$2.50 13x bull case F2016E EPS of 20c	Booming Australian economy, rising consumer/business confidence lifts TV ad spending 7-8%; alternatively Nine picks up a better-than-expected 100-200bp of TV market share; and/or positive regulatory change lifts valuation. Operating leverage in the TV business is significant. Bull case EPS of 20c based on either stronger overall TV ad market or higher Nine market share. Alternatively, either a cut in TV licence fees, or the introduction of retransmission fees would boost valuation.
Base A$1.50 10x base case F2016E EPS 14c	Mild recovery in the Australian economy continues in F2016; with overall flat growth in TV ad spending; Nine Network's TV market share falls modestly, to 37%. Base case EPS forecast is 14.5c in F2016. No change in regulatory environment and/or TV licence fees or retransmission fees factored into our estimates or valuation.
Bear A$0.90 9x bear case F2016E EPS 10c	Economic deterioration in Australia causes TV ad market to fall sharply; and/or Nine's TV ad market share drops sharply; and/or a there is a poorly received M&A event. If key drivers of TV ad spending, such as business/consumer confidence, retail sales, fall sharply, TV ad spending could decline 5-10% on pcp. Bear case EPS of 10c in F2016 is 30% lower than in the base case. Alternatively, our bear case could also materialize in the event that Nine's TV ad market share were to collapse to 35% vs. our base case 37%. This could occur if a rival, such as TEN, were to make a recovery in its TV audience share. Thirdly, it is also possible that an M&A event which the market assesses as strategically flawed and/or significantly EPS-dilutive and destroying shareholder value could force the stock lower.

Investment Thesis

- Underweight – we forecast an absolute -10% decline in share price.
- Our PT of A$1.50/share is 13% below the consensus PT of A$1.72/share.
- We expect the shares to underperform our Australian Media/Internet/Technology coverage universe on a 12-month view.
- Our cautious view has three key pillars: 1) risk of NEC losing greater than expected audience/ad market share in the next 2-3 years; 2) risk of NEC's TV costs surprising on the upside in the next 2-3 years, including renewal of cricket rights; 3) downward structural pressure on FTA TV asset values.

Key Value Drivers

- TV advertising market – for every +/- 100bp in the overall TV ad market growth rate, the NEC EPS impact is +/- 5%.
- Nine Network's TV advertising market share – for every +/- 100bp in Nine's own market share, the NEC EPS impact is +/- 10% to 15%.

Potential Catalysts

- Negative cyclical impact on earnings – if the Australian economy goes into recession and thus the TV ad market suffers.
- Negative outcome on Nine's TV market share, prompted by a recovery by rival TEN and/or further gains made by Seven, at Nine's expense.
- Negative structural change accelerates. FTA TV use falls more dramatically than expected, prompting a sharp fall in TV's share of overall ad spending.

Risks to Achieving Price Target

- Positive earnings surprise – from either a stronger Australian economy, prompting a sharper climb in TV ad spending and/or Nine achieving higher-than-anticipated TV market share.
- Positive regulatory change – a cut in TV licence fees; or the introduction of retransmission fees; or removal of the 75% audience reach rule.
- Increase in capital management, with NEC in a net cash position.
- Highly EPS/FCF-share accretive acquisition.

NEC Valuation

Our price target is **A$1.50/share**. This is unchanged from our prior estimates (**Nine Entertainment: Hypothetically ... What if NEC's next deal for Australian cricket TV rights costs rise +77% ... in line with recent NRL and AFL rights deals? (24 Nov 2015)**)

The PT of A$1.50 represents the midpoint of our fundamental value range of A$1.30 to A$1.70/share, derived from three methodologies – P/E, SoTP and DCF. Currently our SoTP reflects the highest valuation (A$1.70/share) and our P/E multiple (A$1.45/share) ... both of these methods are based on one-year forward multiples. Our DCF reflects the lowest value (A$1.30/share) – as it captures the substantial increase in NRL TV rights cost from F2018E onwards, followed by the substantial increase in cricket rights costs from F2019E onwards. Thus the DCF is an important aspect of our thinking, as it captures the declining trajectory for NEC earnings/returns over the next 10 year forecast period.

Key outcomes:

- **P/E valuation is A$1.45/share :** Based on our F2016 EPS estimate of 14.1c and a target P/E multiple of 10x, to the structural change within the FTA TV industry. We believe that NEC warrants a P/E premium to its TV peer SWM, reflecting what we view as NEC's better asset mix (i.e., no newspapers/magazines). However, the multiple should also reflect a premium to peers, but not the overall Australian market in our view, reflecting FTA TV's higher risk profile around medium-term margins/returns and NPAT growth prospects amid ongoing structural change.
- **SOTP value is A$1.70/share:** Based on our F2016 EBITDA estimates. We apply 7.0x to NEC's TV earnings, representing parity with Seven – striking a balance between Seven's TV assets generating higher returns and better EBITDA margins ... but our outlook for Nine's TV assets to generate slightly higher growth. We apply 10x to Nine Digital. In aggregate, we believe NEC warrants a higher EV/EBITDA multiple vs. SWM. Why? i) asset mix, FTA TV and 9Digital, although not premium assets in our view, do have a superior earnings outlook vs. SWM's declining newspapers/magazines businesses; and, ii) NEC's net cash position.
- **DCF value is A$1.30/share.** Based on our forecast FCF estimates to F2025 and a WACC of 10.6%. Our WACC includes a pre-tax cost of debt of 6.5% and a cost of equity of 14.7% to reflect the greater risk we see from operating in the FTA TV industry and streaming/OTT players start to disrupt viewers and eventually revenues/returns. Every 100 basis point shift in WACC results in an 5-6% shift in DCF value. For example, application of a 9.6% WACC (rather than our 10.6%) would produce a higher DCF value of +5c/share higher.

NEC Financial Summary

Exhibit 31: Nine Entertainment – Financial Summary

Key Assumptions

Year End June	F2015	F2016E	F2017E	F2018E
Overall Metro TV Adspend (to 30 June)	-1.5%	1.0%	2.0%	1.0%
Nine's Metro TV Adspend market share	38.9%	37.0%	36.5%	35.5%
Nine's TV Cost Inflation	1.6%	-1.1%	1.9%	2.7%
Nine TV Programming Cost Inflation	6.0%	-1.7%	2.8%	8.7%
Nine Events Revenue Growth	4.7%	6.7%	5.6%	4.9%
Nine Events Costs Growth	24.5%	-3.5%	4.4%	4.3%
Nine Digital/Mi9 Revenue growth	33%	4%	4%	4%
Effective Tax rate	30%	30%	30%	30%
Capital Expenditure (A$m)	27.0	25.0	23.8	22.6
Events "Key money" (A$m)	26.2	0.0	0.0	0.0
Total Capex as % of Sales	3.3%	1.8%	1.7%	1.6%

Ratio Analysis

Year End June	F2015	F2016E	F2017E	F2018E
EV/EBITDA	5.3x	7.1x	6.2x	7.7x
EV/EBIT	6.7x	8.1x	7.1x	9.1x
P/E multiple	11.1x	11.4x	10.7x	13.2x
EBITDA margin	18%	15%	15%	13%
EBIT margin	14%	13%	13%	11%
Dividend yield	5.5%	7.9%	8.4%	6.8%
Dividend payout ratio	62%	90%	90%	90%

Income Statement

Year End June (A$ mn)	F2015	F2016E	F2017E	F2018E
Op revenue	1,610	1,357	1,393	1,387
Op expenses	-1,340	-1,167	-1,193	-1,228
EBITDA	**284**	**204**	**215**	**174**
Depreciation & Amortisation	-58	-27	-27	-27
EBIT	**226**	**178**	**188**	**148**
Net Interest	-31	5	7	9
Profit Before Tax	195	183	195	157
Tax	-59	-55	-58	-47
Net Profit After Tax - pre Minorities, DI	**137**	**128**	**136**	**110**
Associates NPAT	3	4	4	4
Net Profit (pre-NRI, DI)	**140**	**131**	**140**	**113**
Non-recurring Items - net				
Reported Net Profit	**140**	**131**	**140**	**113**
EPS - Reported	15c	15c	15c	13c
EPS - Normalised	**14.9c**	**14.5c**	**15.5c**	**12.5c**
EPS growth	-9%	-3%	7%	-19%
DPS (¢ per share)	9.2	13.1	13.9	11.3

Half yearly analysis	1H14	2H14	1H15	1H16
Television	650	578	646	562
% growth	*5%*	*4%*	*-1%*	*-3%*
Nine Events/Ticketek	135	93	103	136
% growth	*81%*	*1%*	*-24%*	*46%*
Nine Digital/Mi9	61	61	81	82
% growth	*-22%*	*-12%*	*32%*	*34%*
Total Revenue	**846**	**733**	**829**	**781**
% growth	*9%*	*2%*	*-2%*	*7%*
Total EBITDA	187	120	169	115
% growth	*16%*	*-10%*	*-9%*	*-4%*
NPAT	**95**	**49**	**89**	**51**
% growth	*24%*	*-18%*	*-7%*	*5%*

Balance Sheet

Year End June (A$ mn)	F2015	F2016E	F2017E	F2018E
Current Assets	987	1,575	1,663	1,612
Non Current Assets	1,434	941	989	1,045
Total assets	**2,420**	**2,516**	**2,652**	**2,657**
Current Liabilities	676	670	679	691
Non Current Liabilities	662	662	762	762
Total Liabilities	**1,338**	**1,332**	**1,441**	**1,452**
Net Assets	1,083	1,185	1,211	1,205
Share Capital	793	793	793	793
Reserves	19	19	19	19
Retained Profits	271	370	392	379
Minorities	0	0	0	0
Total Shareholders Equity	**1,083**	**1,182**	**1,203**	**1,191**
Property, Plant & Equipment	119	115	117	119
Intangibles	1,044	530	530	530
Borrowings	576	576	576	576
Net Debt (A$m)	63	-119	-195	-146
EBIT/net interest cover	7.4x	-35.5x	-26.8x	-16.4x
EBITDA/net interest cover	9.3x	-40.9x	-30.7x	-19.4x
Net Debt/EBITDA ratio	0.2x	-0.6x	-0.9x	-0.8x

Cash Flow Statement

Year End June (A$ mn)	F2015	F2016E	F2017E	F2018E
EBITDA - operational	284	204	215	174
Operating cashflow	**246**	**206**	**264**	**153**
Payments for Property, Plant & Equi	-59	-49	-48	-47
Net Payments for investments	-5	576	-24	-24
Investment Activities	**-80**	**520**	**-69**	**-76**
Proceeds from Borrowing	150	0	0	0
Repayment of Borrowing	-179	0	0	0
Dividends paid	-79	-83	-118	-126
Financing Activities	**-206**	**-83**	**-118**	**-126**
Net change in cash	-40	643	76	-49

Segment Information

Year End June (A$ mn)	F2015	F2016E	F2017E	F2018E
Revenue				
Television	1,208	1,187	1,216	1,202
Nine Events/Ticketek	239	0	0	0
Nine Digital/Mi9	163	170	178	185
Total Revenue	**1,610**	**1,357**	**1,393**	**1,387**
EBITDA				
Television	206	196	206	165
Nine Events/Ticketek	70	0	0	0
Nine Digital/Mi9	22	23	24	25
Unallocated	-14	-14	-15	-15
TOTAL EBITDA	**284**	**204**	**215**	**174**

Source: Company data, Morgan Stanley Research Estimates

SWM Risk-Reward

Vulnerable: High Operating Leverage and Still High Financial Leverage

Source: Thomson Reuters (historical share price data). E = Morgan Stanley Research estimates

Price Target A$0.60	Our PT equals our base case (A$0.60) and is based on a combination of P/E Multiple, SOTP and DCF valuation.
Bull A$1.50 10x bull case F17E EPS of 15c	**More bullish ad conditions + Seven's TV market share increases to 41%-42%.** TV EBITDA margin steady. Bull-case EPS is 15c in F2017E. Higher P/E in recognition of higher EPS growth outlook and faster debt paydown and/or higher dividend possibilities. Bull case value of A$1.50/share – with higher earnings and higher multiples - equates to 10x-12x EV/EBITDA in line with where international TV comps such as ITV plc and CBS Corp are trading.
Base A$0.60 8x base case F17E EPS 10.3c	**Low-single-digit TV advertising growth in C2016 and C2017 between +1% to +2%.** Seven's TV ad revenue market share falls slightly from 40% to 38-39%: Base-case EPS of 10.3c.
Bear A$0.20 5x bear case F17E EPS 4.0c	**Australian economy softens, TV ad spending falls -3% to -5% in C2016 and C2017,** and Seven TV market share falls to 36% to 37%: Bear-case EPS of 4c .The lower 5x P/E multiple we apply was the level observable during the GFC. An equity recapitalisation is possible.

Investment Thesis – Why Underweight?

- We remain Underweight. Our PT of A$0.60/share implies downside over the next 12 months ... and sits -40% below the average sell-side PT of A$1.00/share.
- SWM is a well-run and profitable TV/newspaper/magazine company, but in our view, the current returns/margins will likely prove unsustainable over the medium and long term.
- Compared to other TV peers, we note: i) SWM is the only TV broadcaster in Australia also burdened by owning structurally declining print assets; ii) has higher financial leverage; and iii) we believe SWM's TV business has peaked at 41% ad market share, and faces downside risk to that share number.

Key Value Drivers

- Ad revenue: Accounts for ~95% of revenue for SWM's FTA TV assets, ~80% of revenue for SWM's Newspaper assets (i.e., the old WAN).
- Cost control and delivery of cost savings as recently outlined.
- EBITDA margin of ~40% for WAN and ~30% for FTA TV assets are amongst the highest of Australian peers.

Risks to Achieving Price Target

- A stronger-than-expected recovery in the advertising market and/or market share gains by any of SWM businesses (TV, newspapers, magazines) ... but TV market upside would be the key upside risk.
- SWM has stated it may look at M&A opportunities in the media industry. The market may greet such news positively, if the terms are accretive.
- Potential cut of TV licence fees (currently 4.5% of revenue) would be positive for SWM earnings/valuation.
- A potential demerger or spin-off of SWM's print assets could result in a re-rating
- The possibility of Seven Group lifting its stake

SWM Valuation

Our price target is A$0.60/share. This is unchanged from our prior estimates (**Seven West Media Ltd: Hypothetically ... What if Seven Group increases its shareholding in SWM? ... we explore a range of scenarios (24 Nov 2015)**

In summary, our fundamental value range spans from A$0.48/share to A$0.87/share, derived across a range of methodologies – P/E, EV/EBITDA and DCF. We have selected A$0.60/share as our price target, which represents the approximate midpoint of this range.

In summary:

1. **P/E based value – A$0.82/share.** Based on F2017E EPS of 10.3c and applying a 8.0x multiple. We believe a discount to TV peers, such as NEC on 10x, is appropriate in view of SWM's print/newspaper earnings and higher debt levels.
2. **Sum-of-parts value – A$0.87/share.** Key variable is applying 7.0x to F2017E EBITDA estimate to derive EV of A$1.7bn (A$1.14/share) for SWM's TV assets.
3. **DCF value – A$0.48/share.** This methodology produces the lowest value estimate, mainly because it captures our forecast continuing fall in SWM's TV earnings over the next 10 years and into perpetuity. We apply a WACC of 12.3%.

SWM Financial Summary

Exhibit 32: SWM Financial Summary

Key Assumptions

Year End June	F2015	F2016E	F2017E	F2018E
5 Capital City TV Ad Market	1.6%	1.0%	2.0%	1.0%
Seven Network's 5 Cap City Share	40.0%	39.0%	38.5%	38.5%
Seven Network TV Revenue growth	-2.0%	0.4%	1.3%	1.3%
Seven Network TV Cost growth	-1.2%	2.6%	6.9%	2.7%
WAN Advertising Revenue growth	-9.8%	-10.8%	-11.8%	-12.8%
WAN Circulation Revenue growth	-5.4%	-5.4%	-5.4%	-5.4%
WAN Operating cost growth	-1.8%	-7.7%	-7.1%	-7.2%
Magazine Circulation Revenue	-8.0%	-8.9%	-9.0%	-9.0%
Magazine Advertising Revenue	-4.9%	-14.0%	-15.0%	-15.0%
Magazine Cost Growth	-7.8%	-5.9%	-9.1%	-9.9%
Interest cost	7.3%	7.3%	7.3%	7.3%
Effective Tax rate	29%	30%	30%	30%
Capital Expenditure (A$m)	-33	-34	-35	-35
Capex as % of Sales	1%	1%	1%	1%

Income Statement

Year End June (A$ mn)	F2015	F2016E	F2017E	F2018E
Op revenue	1,775	1,735	1,710	1,689
Op expenses	-1,372	-1,371	-1,411	-1,411
EBITDA	403	364	300	277
Associates	4	8	9	13
EBITDA & Associates	**407**	**368**	**303**	**290**
Depreciation	-51	-48	-46	-45
EBIT	**356**	**320**	**257**	**246**
Net Interest	-61	-45	-40	-34
Profit Before Tax	296	274	217	212
Tax	-87	-79	-61	-60
NPAT (pre-NRI, pre-Goodwill Amort)	**209**	**196**	**156**	**152**
Non-recurring items - net	-2,097	0	0	0
NPAT (reported)	**-1,887**	**196**	**156**	**152**
ModelWare EPS (A$)	**20.1**	**12.9**	**10.3**	**10.0**
ModelWare EPS growth	0%	-36%	-20%	-2%
Average diluted shares outstanding (	1,042	1,513	1,513	1,513
EBITDA margin	23%	21%	18%	17%
EBIT margin	20%	18%	15%	15%

Half-yearly analysis	**2H13**	**1H14**	**2H14**	**2H15**
Television	602	684	622	1,306
% growth	*-1%*	*3%*	*3%*	*91%*
Newspapers	171	139	146	286
% growth	*6%*	*-12%*	*-14%*	*105%*
Magazines	123	124	114	238
% growth	*-11%*	*-7%*	*-7%*	*92%*
Other	12	29	-13	16
Total op revenue	**906**	**976**	**870**	**1845**
% growth	*-2%*	*-1%*	*-4%*	*89%*
EBITDA & Associates	**190**	**275**	**183**	**458**
% growth	*16%*	*-5%*	*-4%*	*66%*
EBIT	**163**	**250**	**158**	**408**
% growth	*-1%*	*-3%*	*-3%*	*63%*
NPAT (pre-NRI, pre-Goodwill Amort)	**83**	**150**	**86**	**236**
% growth	*30%*	*6%*	*4%*	*57%*

Half yearly forecasts	**2H15E**	**1H16E**	**2H16E**	**2H16E**
EPS	8.0	7.8	5.2	12.9
- change	16%	-36%	-36%	-36%

Balance Sheet

Year End June (A$ mn)	F2015	F2016E	F2017E	F2018E
Cash	142	260	338	402
Receivables	272	266	262	259
Inventories	152	149	147	145
Other	8	8	8	8
Current Assets	574	683	755	814
Receivables	4	4	4	4
Investments	39	39	39	39
Property, Plant & Equipment	219	189	178	168
Mastheads & Radio Licences	1,555	1,555	1,555	1,555
Future Tax Benefit / (Liability)	0	0	0	0
Non Current Assets	2,032	2,002	1,990	1,980
Total assets	**2,606**	**2,684**	**2,746**	**2,794**
Creditors	298	291	287	283
Tax liabilities	49	49	49	49
Borrowings	875	875	875	875
Provisions	133	133	133	133
Other	0	0	0	0
Total Liabilities	**1,411**	**1,404**	**1,400**	**1,397**
Net Assets	1,195	1,280	1,346	1,397
Share Capital	3,397	3,397	3,397	3,397
Reserves	-3	-3	-3	-3
Retained Profits	-2,199	-2,101	-2,039	-1,985
Minorities	0	0	0	0
Shareholders equity	**1,195**	**1,293**	**1,355**	**1,409**

Cash Flow Statement

Year End June (A$ mn)	F2015	F2016E	F2017E	F2018E
EBITDA - operational	330	359	295	277
Interest Expense	-59	-45	-40	-34
Cash taxes paid	-7	-79	-61	-60
Working capital	0	3	2	2
Other cash items (eg. dividends	19	12	12	12
Operating cashflow	**283**	**250**	**207**	**197**
Payments for Propery, Plant & Ec	-41	-34	-35	-35
Proceeds from sale of PPE, inve	1	0	0	0
Loans (to)/repaid by other entitie	-4	0	0	0
Investment Activities	**-43**	**-34**	**-35**	**-35**
Proceeds from Borrowing	45	0	0	0
Repayment of Borrowing	-400	0	0	0
Dividends paid	-120	-98	-93	-99
Financing Activities	**-167**	**-98**	**-93**	**-99**
Net change in cash	73	118	79	63

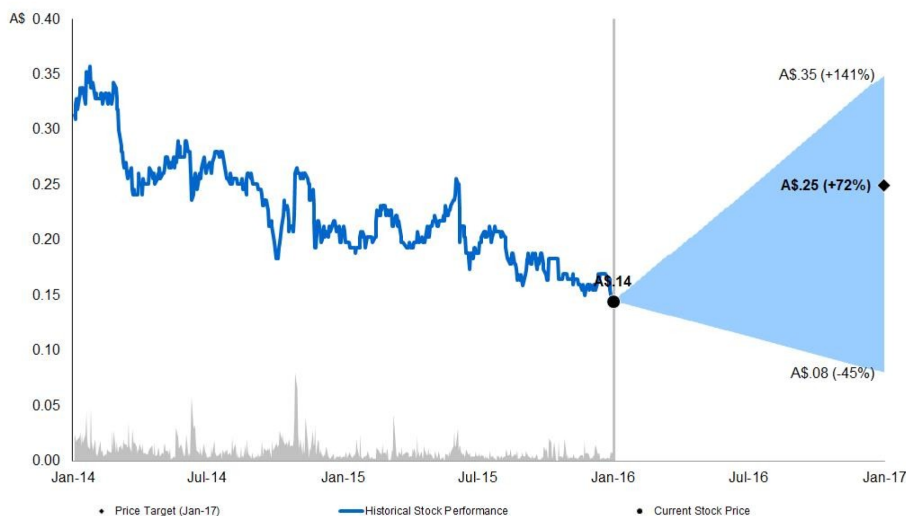
Ratio Analysis

Year End June	F2015	F2016E	F2017E	F2018E
P/E, Modelware (diluted, pre NRI	3.6x	5.6x	7.0x	7.2x
EV/EBITDA	3.5x	4.4x	5.0x	5.1x
Price to free cash flow multiple	3.3x	5.1x	6.5x	6.7x
FCF yield ratio	30%	19%	15%	15%
Net Debt (A$m)	733	615	536	473
Net Debt/EBIT	2.1x	1.9x	2.1x	1.9x
Net Debt/EBITDA ratio	1.8x	1.7x	1.8x	1.7x
EBIT / net interest cover	5.9x	7.1x	6.4x	7.3x
EBITDA / net interest cover	6.7x	8.1x	7.6x	8.6x
Dividend yield	13.9%	13.6%	13.0%	13.7%
Dividend payout ratio	50%	50%	60%	65%

Source: Company data, Morgan Stanley Research Estimates

TEN Risk Reward

Extra Wide Risk/Return Profile is Due to Restructuring/Turnaround Story



Source: Thomson Reuters (historical share price data). E = Morgan Stanley Research estimates

Price Target A$0.25 — Equates to our Base Case.

Bull A$0.35
14x Bull Case F2017E EPS

Stronger TV ad market in combination with TEN's significantly higher revenue market share. Overall 5 capital city TV advertising market growth of +5% to +7% in C2016-17 and furthermore, TEN's own revenue market share is +200 basis points higher than our base case, returning to 26%-27% share. Operating leverage is extremely high. Bull case EPS of 2.5c is approximately 250% higher than our base case EPS of 1c only.

Base A$0.25
25x Base Case F2017E EPS

Flattish overall TV ad market, with TEN growth coming largely from revenue market share gains. Overall 5 capital city TV advertising market achieves 0-2% growth in C2016-17e. TEN's TV revenue market share improves from 22% in F2015 ... up to 24% in F2016 and 25% in F2017E. Base Case EPS of 1c in F2017E. We factor in no potential upside to earnings/valuation from regulatory change and TV Licence Fee cuts etc.

Bear A$0.08
0.80x Price/Book Value

Wind-up scenario. TEN reported a net loss and cash flow deficit in F2015, whilst we forecast a return to profitability and cash flow positive outcome in F2016E, a sharp deterioration in the overall TV ad market and/or unexpected fall in TEN's market share could result in another loss. In our bear case scenario, we value TEN's 5 capital city TV Licences at their last stated (2015 Annual Report) book value of A$482m, plus Net Cash of A$14m post capital raising, plus receivables (A$111m) ... but deduct payables (A$204m), provisions (A$53m) and tax liabilities (A$1m) ... equating to a net total of A$349m or 10c/TEN share ... to which we apply a 20% discount for assessed value of 8c/TEN share.

Investment Thesis

- We are Overweight, TEN remains a turnaround story, with a lot of work to do.
- We view shares as inexpensive (based on implied TV licence value) and very significant operating leverage, and as such, higher than average risk.
- On a 12-18 month view, we see valuation upside versus peers, and also expect the stock to outperform the broader market.
- Driving a turnaround in TEN's F2016-17E earnings will be: i) flattish overall TV advertising market of 0%-2% growth; ii) a significant forecast lift in TEN's audience and advertising market share to 24-25%; and iii) assumed achievement of TV cost guidance of +6.5% in F2016E.

Key Value Drivers

- TV advertising revenue is a key driver for earnings.
- We estimate any +/- 1% change in industry-wide TV ad revenue growth would cause a +/- 10% change in EPS.
- Our positive thesis depends on TEN increasing its TV revenue market share. Every +/- 100 basis point in market share causes +/- 30% change in EPS.

Potential Catalysts

- Any government decision to: i) cut TV licence fees, ii) introduce retransmission fees, and/or iii) improve TV production incentives should be positive for TEN earnings/valuation.
- Any government decision to relax Australian media ownership rules (e.g. the 75% audience reach rule, and/or two-from-three rule) should be positive for TEN's asset values.

Risks to Achieving Price Target

- Weaker-than-expected TV advertising market.
- Lower TEN TV ad market share, dependent on ratings/viewership.
- TV programming cost overruns.
- Another capital raising is possible, which will likely dilute existing TEN shareholders at current levels.
- Loss of support of any of the major shareholders, including FOXTEL 15% stake, WIN/Birketu 14%, Hancock Prospecting 10%. CPH 9% and Illyria 9%.

TEN Valuation

Our price target is A$0.25/share. This is unchanged from our prior estimates (**Ten Network Holdings: Hypothetically ... What if TEN's TV revenue share returns to 27%? ... and what are the implications for competitors SWM and NEC? (24 Nov 2015)**

Our A$0.25/share PT, is the mid-point of our fundamental valuation range of A$0.18-A$0.29/share. This is determined via P/E, EV/EBITDA and DCF methodologies - a summary of outcomes below. In our assessment A$0.25/share which equates to F2017E P/E of 28x and F2017 EBITDA of 15x reflects a justified premium to TEN's historically observable 1-year forward multiples of 18x P/E and 10.4x EBITDA, in view of where the company sits in its earnings cycle and the recovery in earnings we forecast. A WACC of 10.2% is appropriate for the high risk surrounding that forecast recovery in TEN's revenue share and earnings.

- **P/E value is A$0.18/share**. It is based upon F2017E EPS of 0.9c and a target P/E multiple applied of 20x. This is a higher multiple than we would apply to 'steady state' TEN earnings, but reflects our expected recovery trajectory in earnings as TEN's revenue share is forecast to return to long-term average of 27%.
- **SoTP value is A$0.25/share**. We apply 15x target EBITDA multiple to F2017E EBITDA forecast of A$55m. Again, the multiple is higher near term, reflecting growth on recovery path.
- **DCF value is A$0.29/share**. The increase reflects our higher long-term revenue share, increasing gradually to 27% over the next five years vs. previous assumption of TEN returning to a maximum 24% revenue share only. Thus, notwithstanding the application of a higher WACC of 10.2% to reflect higher structural change impacting the overall TV industry, the DCF value has increased.

TEN Financial Summary

Exhibit 33: TEN: Financial Summary

Key Assumptions

Year End August	F2015	F2016E	F2017E	F2018E
TV Adex - 5 capita cities (to year end Au	0.2%	1.0%	2.0%	2.0%
TV Adex market share (5 cap cities)	21.6%	24.0%	25.0%	26.0%
TV Affiliate Revenue growth	0.2%	1.0%	20.0%	2.0%
TV Cost Inflation	-3.8%	5.4%	4.9%	4.2%
Programming Cost inflation	-4.5%	6.3%	5.8%	4.9%
Labour Cost inflation	2.0%	2.0%	2.0%	2.0%
TV Headcount	1002	992	982	972
Effective Tax rate	30%	30%	30%	30%
Interest cost	7.0%	7.0%	7.0%	7.0%
Capital Expenditure (A$m)	-9	-8	-8	-7
Capex as % of Sales	1.5%	1.1%	1.0%	0.9%

Ratio Analysis

Year End August	F2015	F2016E	F2017E	F2018E
ModelWare EPS (¢ per share)	-1.3	0.6	0.9	1.2
ModelWare EPS growth	-71%	-143%	63%	33%
Average diluted shares outstanding (m	2,537	3,307	3,564	3,564
EV/EBITDA	-45.2x	14.9x	9.3x	6.8x
Price to free cash flow multiple	-11.9x	25.8x	18.8x	13.9x
FCF yield ratio	-8.4%	3.9%	5.3%	7.2%
P/E, reported	-1.3x	30.0x	18.5x	13.9x
P/E, Modelware	-1.3x	30.0x	18.5x	13.9x
EBITDA margin	-2%	5%	7%	9%
EBIT margin	-4%	3%	6%	7%
DPS (¢ per share)	0.0	0.0	0.0	0.0
Dividend yield	0.0%	0.0%	0.0%	0.0%
Dividend payout ratio	0%	0%	0%	0%
ROIC	17%	17%	17%	17%

Income Statement

Year End August (A$ mn)	F2015	F2016E	F2017E	F2018E
Op revenue	629	713	764	808
Op expenses	-641	-676	-709	-739
EBITDA	-12	37	55	69
Depreciation & Amortisation	-14	-14	-13	-12
EBIT	**-26**	**23**	**42**	**57**
Net Interest	-16	5	5	5
Profit Before Tax	-42	27	47	63
Tax	13	-8	-14	-19
Net Profit After Tax - pre Minorities, DI	**-30**	**19**	**33**	**44**
Minority Interests	-4	-1	0	0
Net Profit (pre-NRIs)	**-30**	**19**	**33**	**44**
Non-recurring Items - net	-286	0	0	0
CanWest Debenture Interest (DI)	0	0	0	0
Minority Interest Adjustment for DI	0	0	0	0
Reported Net Profit	**-320**	**19**	**33**	**44**

Balance Sheet

Year End August (A$ mn)	F2015	F2016E	F2017E	F2018E
Current Assets	308	470	522	582
Non Current Assets	551	541	535	530
Total assets	**859**	**1,010**	**1,057**	**1,112**
Current Liabilities	239	223	236	248
Non Current Liabilities	208	208	208	208
Total Liabilities	**447**	**431**	**445**	**456**
Net Assets	411	579	612	656
Share Capital	2,782	2,936	2,936	2,936
Reserves	-1,189	-1,189	-1,189	-1,189
Retained Profits	-1,182	-1,163	-1,131	-1,087
Minorities	1	1	2	2
Total Shareholders Equity	**411**	**585**	**618**	**662**
Property, Plant & Equipment	45	35	29	24
Intangibles	482	482	482	482
Borrowings	155	155	155	155
Net Debt (A$m)	141	-34	-66	-109
EBIT/net interest	-1.7x	-5.1x	-8.5x	-10.5x
EBITDA/net interest	-0.8x	-8.1x	-11.2x	-12.7x
Net Debt/EBITDA	-11.7x	-0.9x	-1.2x	-1.6x

Cash Flow Statement

Year End August (A$ mn)	F2015	F2016E	F2017E	F2018E
EBITDA - operational	-12	37	55	69
Operating cashflow	**-55**	**29**	**40**	**51**
Payments for Property, Plant & Equi	-8	-8	-8	-7
Net Payments for investments	1	0	0	0
Other operating cashflow	22	0	0	0
Investment Activities	**15**	**-8**	**-8**	**-7**
Proceeds from Borrowing	325	0	0	0
Repayment of Borrowing	-280	0	0	0
Dividends paid	-5	0	0	0
Debenture interest	0	0	0	0
Financing Activities	**40**	**154**	**0**	**0**
Net change in cash	0	175	32	44

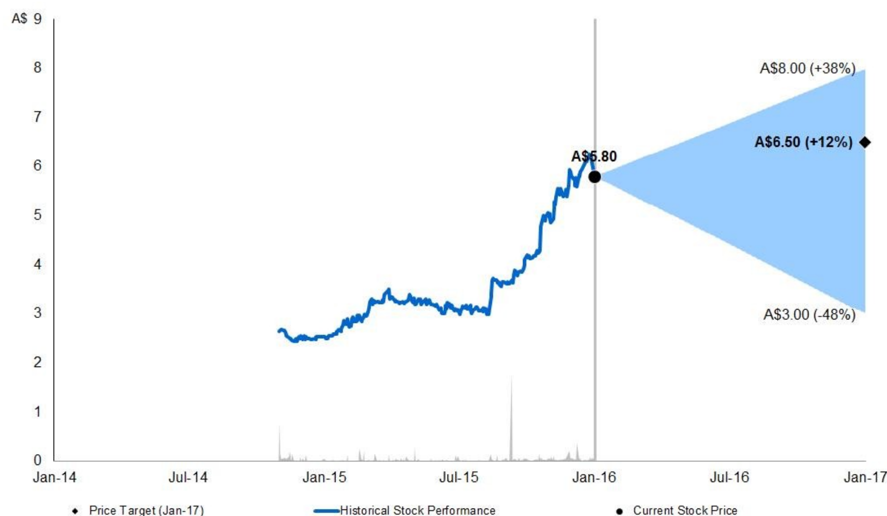
Segment Information

Year End August (A$ mn)	F2015	F2016E	F2017E	F2018E
Revenue				
Television	629	713	764	808
Outdoor	0	0	0	0
Other	0	0	0	0
Total Revenue	**629**	**713**	**764**	**808**
EBITDA				
Television	-12	37	55	69
Outdoor	0	0	0	0
Other	0	0	0	0
TOTAL EBITDA	**-12**	**37**	**55**	**69**
TV EBITDA margin	**-1.9%**	**5.1%**	**7.2%**	**8.6%**

Source: Company Data, Morgan Stanley Research. E = Morgan Stanley Research estimates

APO Risk Reward

Digital Panel Rollout Is Primary Earnings/Valuation Driver



Source: Thomson Reuters (historical share price data), E = Morgan Stanley Research estimates

Price Target A$6.50	Base case scenario, approximate average of three methodologies: P/E, EV/EBITDA-based sum of parts, and DCF.
Bull A$8.00 20x Bull Case C2017E EPS 40c	**Stronger economic recovery + Outdoor market share wins occur at a faster rate:** Strong real GDP growth in C2015 and C2016 supports consumer confidence, allowing for a stronger-than-expected Outdoor advertising market. APO grows its outdoor market share by 2.5ppts, and Outdoor advertising as a % of the total ad pie grows to 7% by C2018, driven by a faster-than-expected digital rollout. Modest higher P/E multiple than base case, earnings ~20% higher than base case.
Base A$6.50 19x Base Case C2017E EPS 35c	**Modest, gradual economic recovery - Outdoor industry continues to gradually increase its share of revenues:** Moderate real GDP growth in C2015 and C2016 supports consumer confidence, yet not enough to produce greater-than-expected Outdoor ad growth of 8-10% in C2016. APO grows its outdoor market share by 1.5ppts, and Outdoor advertising as a % of the total ad revenue pie grows to 5.2% by C2018.
Bear A$3.00 12x Bear Case F2017E EPS 25c	**Economic slowdown, advertising contracts - Outdoor industry share slips backwards:** Real GDP declines in C2016-17, resulting in poor consumer confidence and negative Outdoor advertising growth in C2016-17. APO's outdoor market share is flat, and Outdoor advertising as a % of the total ad pie remains flat, at 5% , digital rollout slower-than-expected. EPS is 25-30% lower than our base case.

Investment Thesis

- Overweight – we expect shares will rise +20% in an absolute sense ... and also outperform Australian media peers on a 12-month view.
- Our positive thesis has 3 key pillars ... i) Outdoor advertising industry gaining share of the total ad revenue pool of dollars; ii) APO winning Outdoor market share, supported by its continued planned roll-out of large format digital panel billboards, driving faster revenue growth vs. peers; and, iii) high fixed costs mean high operating leverage, this revenue growth drives higher EPSg and we think warrants a premium multiple.

Key Value Drivers

- Outdoor ad market – for every +/- 100bps in the market growth rate, the APO EPS impact is +/- 3% to 4%.
- APO ad market share – for every +/- 100bps in APO's market share, EPS impact is +/- 4% to 5%.

Potential Catalysts

- Positive earnings surprise – from a stronger Australian economy &/or APO achieving higher-than-anticipated Outdoor market share.
- If APO is able to expand its digital rollout faster than expected. Looking forward, we assume addition of a further 15-20 large format digital boards annually.
- APO undertakes a highly accretive and strategically astute acquisition.

Risks to Achieving Price Target

- Negative cyclical impact on earnings – if the Australian economy goes into recession, and demand for ads falls.
- Negative if APO's market share &/or profit margins are hit by competitive action of rivals... and/or loss of contracts if these are taken in-house.
- Negative structural change. Outdoor Advertising use falls dramatically, prompting a fall in Outdoor's share of the overall pool of Australian ad revenue.

APO Valuation

Our price target is **A$6.50/shar e.** This is unchanged from our prior estimates (**APN Outdoor Group Limited: Asia Insight: We explore the structural forces driving Outdoor's growth vs. FTA TV's decline ... Keep Overweight. (04 Dec 2015)**

We use three main valuation methodologies – target P/E multiple, Sum-of-Parts and Discounted Cash Flow – to derive a fundamental valuation range of A$6.22 – A$6.78/share. From this range, we select an approximate midpoint of A$6.50/share to be our price target.

In summary:

- **P/E valuation is A$6.22/share** . Based on our C2017E EPS estimate of A$0.35c and target P/E multiple of 18x. We believe 18x is justified....as compared to traditional Media peers, which currently average only a 6-11x P/E one-year forward... given the stronger-than-forecast EPSg trajectory driven by the digital panel rollout. We forecast APO to achieve a three-year EPS CAGR of +16% vs. media peers average flat to +2-3% growth at best. Every +/- 1 P/E multiple point... has approximately +/- 35c/share impact to our P/E valuation.
- **Sum-of-the-Parts (SOTP) value is A$6.55/share**. Similarly, we believe APO warrants a higher EBITDA multiple than the traditional Australia media peers... we believe the blended 11.5x is reasonable...we split the business into digital and traditional static ... we put traditional outdoor media panels on 8x, at a small premium to traditional Media peers' average 7x.... and the digital outdoor media panels on 15x, below the Internet media average of 16-18x.
- **Discounted Cash Flow (DCF) value is A$6.78/share**. We have selected a WACC of 9.4%, which includes an additional 0.5% loading on our cost of equity estimate due to the risk of heightened Outdoor industry competition, in the form of price wars for new inventory/sites/contracts, as well as advertising discounting. To date we have not seen any evidence of this, hence the temper in the rate, however, it remains a risk in our view. Every +/- 100 basis points on WACC (i.e., if you think 10.4% is more appropriate than our 9.4%) has approximately +/-98c/share impact on our DCF valuation.

APO Financial Summary

Exhibit 34: APO Financial Summary

Income Statement

(A$m) Year End December 31st		C2014	C2015E	C2016E	C2017E
Total Sales Revenue	**A$m**	**250.6**	**295.6**	**325.4**	**360.2**
- change	%	11%	18%	10%	11%
Site Costs	A$m	-108.2	-118.0	-125.6	-133.8
Staff Costs	A$m	-30.9	-32.0	-33.7	-36.0
Marketing Costs	A$m	-24.3	-27.1	-29.8	-33.0
Other Costs	A$m	-42.0	-48.5	-53.4	-59.1
Operating Expenses	**A$m**	**-205.3**	**-225.6**	**-242.6**	**-261.9**
- change	%	7%	10%	8%	8%
Total EBITDA	**A$m**	**45.3**	**70.0**	**82.9**	**98.3**
- change	%	34%	55%	18%	19%
Depreciation & Amortisation					
Depreciation	A$m	-7.2	-9.1	-10.0	-11.1
- change	%	5%	26%	10%	11%
Amortisation	A$m	-2.8	-2.8	-4.3	-4.8
- change	%	-3%	0%	53%	11%
Total D&A	**A$m**	**-10.0**	**-11.9**	**-14.3**	**-15.9**
- change	%	3%	19%	20%	11%
Total EBIT	**A$m**	**35.3**	**58.1**	**68.5**	**82.4**
- change	%	46%	65%	18%	20%
Net interest	A$m	-4.1	-4.0	-3.8	-4.2
Profit Before Tax	**A$m**	**31.2**	**54.1**	**64.7**	**78.3**
Income Tax	A$m	-9.6	-16.2	-18.8	-22.7
Profit After Tax	**A$m**	**21.6**	**37.9**	**46.0**	**55.6**
Minorities	A$m	0.0	0.0	1.0	2.0
Non-Recurring Items (post-tax)	A$m	0	0	0	0
Reported NPAT	**A$m**	**21.6**	**37.9**	**46.0**	**55.6**
- change	%	52%	76%	21%	21%
Modelware NPAT (pre-NRI)	**A$m**	**23.7**	**39.9**	**48.0**	**57.6**
- change	%	45%	68%	20%	20%
EPS	**cps**	**14.2**	**23.9**	**28.8**	**34.5**
- change	%		68%	20%	20%
DPS	**cps**	**1.0**	**13.6**	**16.6**	**20.0**
Dividend Payout Ratio	%		57%	57%	58%
EBITDA Margin - Group	%	18%	24%	25%	27%
EBIT Margin - Group	%	14%	20%	21%	23%
NPAT Margin	%	9%	13%	14%	15%
P/E Ratio	**(x)**	**38.6x**	**22.9x**	**19.1x**	**15.9x**
EV/EBITDA	(x)	21.6x	13.9x	11.7x	9.7x
EV/EBIT	(x)	27.7x	16.8x	14.1x	11.6x

Other Value Drivers

(A$m) Year End December 31st		C2014	C2015E	C2016E	C2017E
Net Debt/(Cash)	A$m	64.6	62.4	51.8	38.4
Net Debt/S'holders Equity	%	31%	28%	21%	14%
Net Tangible Assets	A$m	140.0	157.4	181.7	210.6
NTA/Share	$ actual	0.34	0.54	0.16	0.24
ROA	%	4%	6%	11%	13%
ROE	%	10.3%	12.8%	18.4%	20.6%

Balance Sheet

(A$m) Year End December 31st		C2014	C2015E	C2016E	C2017E
Current Assets					
Cash & cash equivalents	A$m	14.7	16.9	27.5	40.9
Receivables	A$m	37.6	44.4	48.9	54.1
Inventory	A$m	0.7	0.9	0.9	1.0
Other	A$m	7.8	7.8	7.8	7.8
Total Current Assets	**A$m**	**60.9**	**70.0**	**85.2**	**103.9**
Non-Current Assets					
Deferred tax assets	A$m	10.6	10.6	10.6	10.6
Property, plant & equipment	A$m	67.9	76.2	85.4	95.6
Intangibles	A$m	212.1	209.3	205.1	200.3
Investments	A$m	0.0	0.0	0.0	0.0
Other non-current assets	A$m	0.6	0.6	0.6	0.6
Total Non-Current Assets	**A$m**	**291.2**	**296.8**	**301.6**	**307.0**
Total Assets	**A$m**	**352.1**	**366.7**	**386.8**	**410.9**
Current Liabilities					
Accounts Payable	A$m	22.5	22.1	23.7	25.6
Borrowings	A$m	0.0	0.0	0.0	0.0
Current tax liabilities	A$m	0.0	0.0	0.0	0.0
Provisions	A$m	0.0	0.0	0.0	0.0
Other current liabilities	A$m	-0.6	-0.6	-0.6	-0.6
Total Current Liabilities	**A$m**	**21.9**	**21.5**	**23.1**	**25.0**
Non-Current Liabilities					
Borrowings	A$m	79.3	79.3	79.3	79.3
Provisions	A$m	0.0	0.0	0.0	0.0
Deferred tax liabiliites	A$m	34.3	34.3	34.3	34.3
Other	A$m	6.1	6.1	6.1	6.1
Total Non-Current Liabilities	**A$m**	**119.7**	**119.7**	**119.7**	**119.7**
Total Liabilities	**A$m**	**141.6**	**141.2**	**142.9**	**144.7**
Net Assets	**A$m**	**210.5**	**225.5**	**243.9**	**266.2**
Total Shareholders Equity	**A$m**	**209.2**	**224.2**	**242.6**	**264.8**

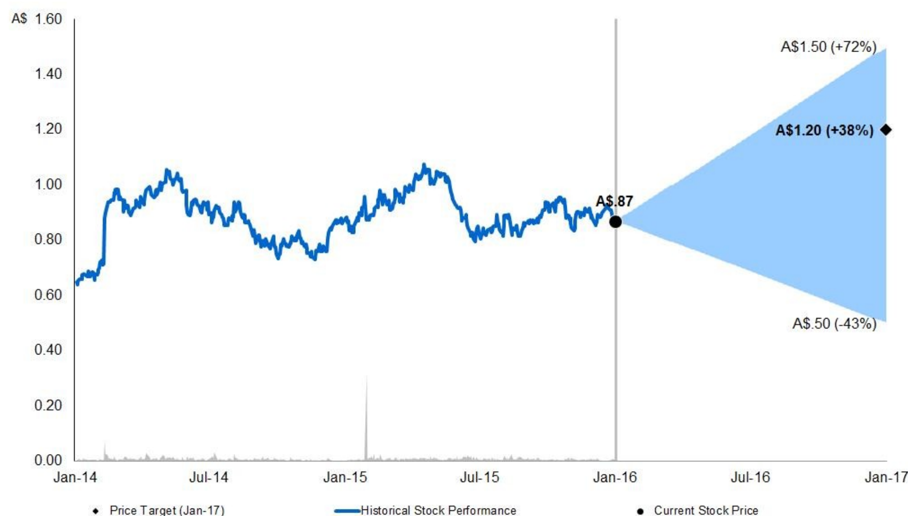
Cash Flow Statement

(A$m) Year End December 31st		C2014	C2015E	C2016E	C2017E
Operating Cash Flows					
EBITDA	A$m	45.3	70.0	82.9	98.3
Working capital (incr.)/decr.	A$m	-1.0	-7.3	-2.9	-3.4
Net interest	A$m	-3.8	-4.0	-3.8	-4.2
Income taxes paid	A$m	-9.6	-16.2	-18.8	-22.7
Other	A$m	-0.1	-0.1	0.0	0.0
Total Operating Cash Flows	**A$m**	**30.7**	**42.4**	**57.4**	**68.0**
- change	%	59%	38%	35%	18%
Investing Cash Flows					
Purchase of PPE	A$m	-22.3	-17.4	-19.2	-21.3
Payments for Intanglibles	A$m	0.0	0.0	0.0	0.0
Other investing	A$m	0.0	0.0	0.0	0.0
Total Investing Cash Flows	**A$m**	**-22.3**	**-17.4**	**-19.2**	**-21.3**
Financing Cash Flows					
Dividends paid	A$m	0.0	-22.7	-27.6	-33.3
Proceeds from borrowings	A$m	-44.5	0.0	0.0	0.0
Other financing	A$m	41.7	0.0	0.0	0.0
Total Financing Cash Flows	**A$m**	**-2.9**	**-22.7**	**-27.6**	**-33.3**
Net change in cash	**A$m**	**5.5**	**2.2**	**10.6**	**13.4**

Source: Company data, Morgan Stanley Research. E = Morgan Stanley Research estimates

FXJ Risk Reward

Shape of the Ad Cycle + Rising value in Domain + Potential M&A



Source: Thomson Reuters (historical share price data), E = Morgan Stanley Research estimates

Price Target A$1.20

Base case scenario, approximate average of three methodologies: P/E, EV/EBITDA-based sum of parts, and DCF.

Bull A$1.50
17x Bull Case F2016E EPS

Stronger advertising recovery in C2016-17E: Bull case EPS of 9c (~30% above base case). Alternatively, bull case could be achieve is M&A interest emerges, in which case A$1.50/share equates to 12x F2016E EBITDA. And/or bull case valuation could also be achieved if the market were to value Domain on same multiples as REA, implying +A$2bn for that asset.

Base A$1.20
16x Base Case F2016E EPS

Modest advertising recovery in C2015-16E, structural challenges persist: Base-case F2016E EPS is 7.1c , combined with target P/E multiple of 16x, a small premium to the market, for a stock with net cash position and increasing digital earnings.

Bear A$0.50
10x Bear Case F2016E EPS

Return to a sharp advertising recession ... structural change accelerates + failure to achieve a meaningful reduction in costs: Bear-case EPS is 5c in F2016E (~30% below base case). Also equate to a lower P/E of 10x.

Why Overweight?

- We see upside in FXJ shares over the next 12-18 months with a forecast +30% capital return.
- In a relative sense, we also expect FXJ to outperform its Australian Media peer group.
- We see upside for shareholders in the areas of:
- Upside from digital/online assets, in particular the online real estate business Domain.com.au.
- A strong balance sheet, with net cash position, FXJ has the flexibility to consider bolt-on acquisitions and/or capital management.
- Further asset sales.
- More aggressive cost savings.

Key Catalysts

- Improvements in advertising conditions.
- Potential further assets sales.
- Variance in operating cost outlook.
- If Domain revenue/earnings growth outstrips expectations and/or if investors are prepared to re-rate this asset and apply higher valuation.
- Return of M&A interest could be positive for FXJ and bolster industry multiples.

Risks to Achieving Price Target

- Deterioration in the ad cycle.
- A sharper fall in newspaper readership and/or circulation.
- Loss of digital/online audiences.
- A cover price war; loss of ad market share (online/print); variance in the operating cost outlook.
- Strategically flawed acquisition.

FXJ Valuation

Our PT is A$1.20/share. This is unchanged from our prior estimates (**Fairfax Media: Lifting 'Domain' valuation to A$1.5bn ... Why the MMP deal is strategically significant (24 Feb 2015).**

We derive a fundamental valuation range between A$1.03/share to A$1.27/share by applying a range of methodologies, including target P/E multiple, sum-of-parts and DCF. From within this range, we select A$1.20/share as the approximate midpoint.

In summary:

- **P/E valuation is A$1.03/share** . We focus on F2016E of A$0.07 EPS and apply a 14x P/E multiple, which represents parity to the Australian market F2016E P/E multiple. We take into account: 1) FXJ now has a net cash position. In recent years there have been concerns about the company's level of debt leverage, but that no longer is valid; and ii) whilst print/newspapers structural challenges certainly remain, Digital/Internet earnings are progressively becoming a larger part of the story.
- **Sum-of-the-Parts (SOTP) value is A$1.27/share**. We use a 15x EBITDA multiple for FXJ's core Australian metro titles (*SMH, The Age*) and also the Internet rights division, which includes Domain, MyCareer.com.au, Drive.com.au and the newspaper websites, etc. We use a 5x EBITDA for FXJ's NZ-based papers and for the Australian regional newspapers given the negative structural challenges. We use 12x EBITDA for Metro Radio stations and 15x for the Australian Digital investments.
- **Discounted Cash Flow (DCF) value is A$1.04/share**. We use a WACC of 10% and a terminal growth rate of 3%. We apply a higher-than-average WACC, reflecting what we consider a higher-than-average risk - due to structural change, inherent high cyclical revenue base, and high operational leverage. For every +/- 1ppt to the WACC, the DCF value declines by ~10% or 10c/share. For example, if we apply a WACC of 11% rather than 10%, the DCF today would be A$0.94/share vs. base case $1.04/share.

FXJ Financial Summary

Exhibit 35: FXJ Financial Summary

Income Statement

(A$m) Year End June 30		F2015	F2016E	F2017E	F2018E
Sales Revenue					
Australian Publishing	A$m	697	640	589	541
Rural Press	A$m	399	365	335	308
New Zealand Publishing	A$m	359	321	303	287
SBC Radio	A$m	109	127	135	140
Australian Digital	A$m	273	369	436	488
TOTAL OPERATING REVENUE	**A$m**	**1,853**	**1,822**	**1,797**	**1,764**
Change on pcp	%	-1%	-2%	-1%	-2%
Total Operating Expenses	**A$m**	**-1564**	**-1511**	**-1470**	**-1444**
Change on pcp	%	0%	-3%	-3%	-2%
EBITDA					
EBITDA - Australian Publishing	A$m	62	31	34	31
EBITDA - Rural Press	A$m	109	92	95	73
EBITDA - New Zealand Publishing	A$m	65	53	46	41
EBITDA - SBC Radio	A$m	14	20	23	23
EBITDA - Australian Digital	A$m	86	115	130	152
EBITDA - total	**A$m**	**289**	**311**	**328**	**320**
Change on pcp	%	-3%	7%	5%	-2%
Depreciation & Amortisation	A$m	-65	-58	-53	-49
EBIT	**A$m**	**224**	**253**	**275**	**271**
Total Net Interest	A$m	-16	-12	-10	21
Net Profit Before Tax	**A$m**	**208**	**241**	**265**	**292**
Tax	A$m	-60	-66	-73	-80
Net Profit After Tax	**A$m**	**148**	**175**	**192**	**212**
Minority Interests	A$m	-5	-8	-8	-9
NPAT (pre-NRI)		**144**	**167**	**184**	**203**
Change on pcp		-1%	16%	10%	11%
NRI - net	A$m	0	0	0	0
Reported net profit	**A$m**	**144**	**167**	**184**	**203**
Weighted average shares	millions	2,352	2,352	2,352	2,352
EPS - Reported (¢)		6.1	7.1	7.8	8.6
Modelware EPS (pre NRI) (¢)		**6.1**	**7.1**	**7.8**	**8.6**
Change on pcp		-1%	16%	10%	11%
DPS	cents	3.1	3.5	3.9	4.3
EBITDA Margin	%	16%	17%	18%	18%
NPAT (Pre-NRIs) Margin	%	8%	9%	10%	12%
P/E Ratio	(x)	15.2x	13.0x	11.8x	10.7x
EV/EBITDA	(x)	8.6x	7.7x	7.7x	7.7x
EV/EBIT	(x)	11.1x	9.4x	9.4x	9.4x

(A$m) Half Yearly Analysis		1H F14	2H F14	1H F15	2H F115
Revenue	A$m	977	889	964	859
Change on pcp	%	-9%	-3%	-1%	-3%
EBITDA	A$m	**181.7**	**117.8**	**171.6**	**139.4**
Change on pcp	%	-1%	-11%	-6%	18%
NPAT (pre-NRI)	A$m	94.0	50.6	93.0	73.9
Change on pcp	%	72%	-4%	-1%	46%
EPS (pre-NRI)	cents	**4.0**	**2.2**	**4.0**	**3.1**
Change on pcp	%	74%	-5%	-1%	46%

Balance Sheet

(A$m) Year End June 30		F2015	F2016E	F2017E	F2018E
Current Assets					
Cash & cash equivalents	A$m	343	450	551	662
Receivables	A$m	315	286	283	277
Inventories	A$m	26	31	30	30
Other	A$m	76	76	76	76
Total Current Assets	**A$m**	**760**	**844**	**939**	**1,045**
Non-Current Assets					
Property, plant & equipment	A$m	330	347	353	345
Investments	A$m	98	98	98	98
Intangibles	A$m	1,523	1,523	1,523	1,523
Other	A$m	112	112	112	112
Total Non-Current Assets	**A$m**	**2,064**	**2,080**	**2,086**	**2,079**
Total Assets	**A$m**	**2,823**	**2,924**	**3,026**	**3,123**
Current Liabilities					
Payables	A$m	242	227	220	217
Borrowings	A$m	31	31	31	31
Provisions	A$m	137	137	137	137
Other	A$m	22	22	22	22
Total Current Liabilities	**A$m**	**432**	**417**	**410**	**407**
Non-Current Liabilities					
Interest bearing loans and borrowings	A$m	263	263	263	263
Provisions	A$m	62	62	62	62
Total Non-Current Liabilities	**A$m**	**325**	**325**	**325**	**325**
Total Liabilities	**A$m**	**757**	**742**	**735**	**732**
Net Assets	**A$m**	**2,066**	**2,183**	**2,290**	**2,392**
Total Shareholders Equity	**A$m**	**2,066**	**2,182**	**2,282**	**2,392**
Net Debt (note: negative = net cash)	A$m	-49	-156	-257	-368
Net Debt / EBITDA	(x)	1.1	0.7	0.7	0.7
EBITDA / Net Interest	(x)	17.8	25.9	32.8	-15.3
EBIT / Net Interest	(x)	13.8	21.1	27.5	-13.0

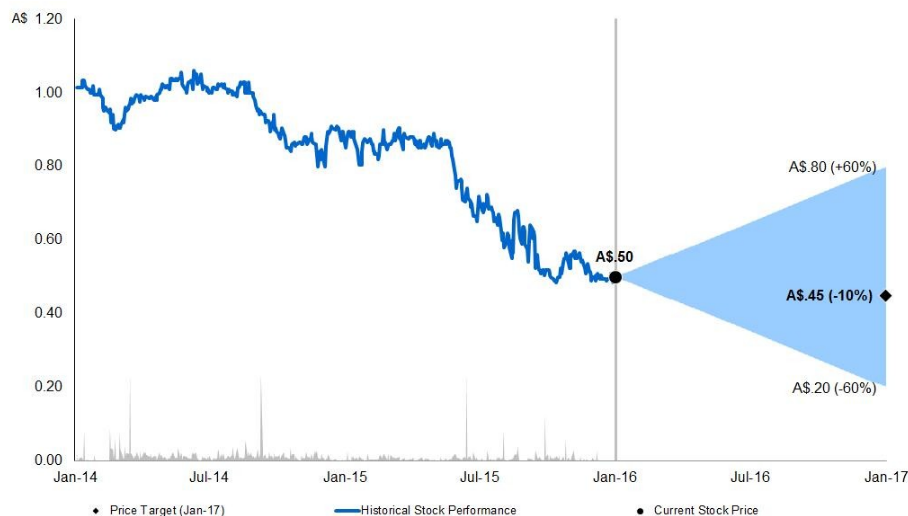
Cash Flow Statement

(A$m) Year End June 30		F2015	F2016E	F2017E	F2018E
Operating Cash Flows					
EBITDA	A$m	0	311	328	320
Working capital (incr.)/decr.	A$m	0	8	-1	2
Net interest	A$m	-13	-12	-10	21
Income taxes paid	A$m	-19	-66	-73	-80
Dividends received	A$m	8	8	8	8
Total Operating Cash Flows	**A$m**	**206**	**249**	**251**	**270**
Change on pcp	%	20%	21%	1%	7%
Investing Cash Flows					
Purchase of PPE	A$m	-62	-61	-59	-58
Other investing	A$m	30	0	0	0
Total Investing Cash Flows	**A$m**	**-32**	**-61**	**-59**	**-58**
Financing Cash Flows					
Dividends paid	A$m	-95	-83	-92	-101
Proceeds from issue of shares	A$m	-38	0	0	0
Proceeds from borrowings	A$m	5	0	0	0
Other cash restructuring costs	A$m	-155	0	0	0
Total Financing Cash Flows	**A$m**	**-283**	**-83**	**-92**	**-101**
Net change in cash	**A$m**	**-109**	**104**	**100**	**111**

Source: Company data, Morgan Stanley Research. E = Morgan Stanley Research estimates

PRT Risk-Reward

Audience share loses are expected to translate into weaker EPS



Source: Thomson Reuters (historical share price data). E = Morgan Stanley Research estimates

Price Target A$0.45	Based on the average of our DCF, P/E and EV/EBITDA valuations.
Bull A$0.80 10x bull case F2017E EPS of 8c	Strong economic recovery: Strong real GDP growth in C2016 and C2017 supports Television advertising growth of 3-4% in FY16-17E. PRT increases its Television advertising market share by 1%, per year until FY17.
Base A$0.45 7x base case F2017E EPS 6.8c	Gradual economic recovery: Moderate real GDP growth in C2016 and C2017 supports 1-2% Television advertising growth in FY16/17E. PRT's Television advertising market share falls ~50bps to 45.5% in F2016E and another 50bps in F2017E.
Bear A$0.20 4x bear case F2017E EPS 5c	Double dip: Real GDP declines in C2016 and is flat in C2017, resulting in Television advertising growth of -5% in FY16E and -8% in FY17E. PRT's Television advertising market share decreases by -2-3% per year until FY18.

Investment Thesis - Why Overweight?

- We expect the stock to underperform the ASX200 and its media peers on a 12-month view. We forecast a capital return of -10%.
- We believe PRT's market share gains have peaked and top-line growth is now dependent on an overall weak ad market.
- Continuing affiliate fee increases shall result in flat EPS growth for the next 3 years.
- Long-term structural risks are emerging with the entrance of OTT video players into the Australian market

Key Value Drivers

- Television advertising growth: All else equal, +/-1% in TV advertising growth means +/-3% EPS.
- Television advertising market share: All else equal, +/-1% in TV advertising share means +/-6% EPS.

Potential Catalysts

- The television advertising market improving dramatically, accelerating top-line revenue growth.
- PRT wins television adex market share from its competitors.
- The Australian Government changes the Media Reach Rules resulting in industry consolidation.

Risks to Achieving Price Target

- The television advertising market slows dramatically, making top-line growth difficult.
- PRT loses television adex market share to its competitors.
- PRT embarks on a period of acquisitions increasing its debt and reducing its operational leverage.
- The Australian Government does not change the Media Reach Rules and consequently PRT is no longer seen by the market as a potential acquisition target.
- TV license fee reduction is not passed into legislation.

PRT Updated Valuation

Our PT is A$0.45/share (was A$0.60/share), lowered due to our view of our lower EPS of -6% to -14% for F2016-18E, as a result of a weaker regional TV ad market.

We derive our price target from three methodologies: P/E, EV/EBITDA-based sum-of-the-parts and discounted cash flow (DCF). We take an average of all three valuation methods. We use a DCF methodology because we think the DCF captures the long-term cyclicality of TV broadcasters, whereas the P/E and EV/EBITDA methods focus on short-term earnings.

In summary:

- **P/E valuation is A$0.41/share**. We base our fundamental P/E valuation of **A$0.41/share** (previously A$0.63) on FY17E EPS of 6.8c (was FY16E EPS 8.2c) and a target P/E multiple of 6x (was ~7x), lowered to reflect the growing threat of OTT players. This represents a ~45% (unchanged) discount to the market. This is larger than PRT's long-term average discount to the market of 16%. We think this is an appropriate multiple because the advertising outlook for PRT is not positive, as PRT is faced with the risk of lower revenue share and PRT, like all FTA TV firms, is facing structural threats from OTT players.
- **Sum-of-the-Parts (SOTP) value is A$0.46/share** (was A$0.62/share). We apply a target EBITDA multiple of 4.5x (was 5.0x) for the television division, broadly in-line with other regional FTA TV peers in Australia, and EBITDA is lower due to the forecast lower earnings. We lower the multiple to reflect a weakening ad market and longer-term structural threats from OTT players.
- **Discounted Cash Flow (DCF) value is A$0.44/share** (was A$0.53)**.** The decline reflects our lowered forecast earnings due to the weaker regional TV ad market. We use a WACC of 11.9% and a terminal growth rate of 2% (both unchanged). For every +/- 1ppt to the WACC, the DCF value declines by ~13-14% or 5-6c/share. For example, if we apply a WACC of 10.9% rather than 11.9%, the DCF today would be A$0.50/share vs. base case $0.50/share.

PRT Financial Summary

Exhibit 36: PRT Financial Summary

Key Assumptions

Year End June	F2015	F2016E	F2017E	F2018E
TV Adex - (to year end June)	-1%	1%	1%	2%
TV Adex Regional - (to year end June)	-4%	-7%	-5%	-3%
TV Adex market share (Regional)	42.2%	41.5%	41.0%	41.0%
TV Cost Inflation	-1.4%	-5.8%	-5.1%	-2.4%
Broadcasting + Transmisson Inflation	-9.8%	-5.0%	-5.0%	-2.0%
Sales + Marketing Cost Inflation	-1.4%	5.7%	-5.2%	-5.5%
Effective Tax rate	30%	30%	30%	30%
Capital Expenditure (A$m)	6	5	5	5
Capex as % of Sales	-2%	-2%	-2%	-2%

Ratio Analysis

Year End June	F2015	F2016E	F2017E	F2018E
EV/EBITDA	4.0x	0.0x	0.0x	0.0x
Price to free cash flow multiple	5.8x	5.1x	6.2x	6.4x
FCF yield ratio	17%	20%	16%	16%
P/E, Modelware	5.2x	6.6x	7.5x	8.0x
EBITDA margin	26%	24%	23%	23%
EBIT margin	22%	19%	18%	17%
DPS (¢ per share)	6.8	5.7	5.1	4.7
Dividend yield	13%	11%	10%	9%
Dividend payout ratio	70%	74%	74%	74%

Income Statement

Year End June (A$ mn)	F2015	F2016E	F2017E	F2018E
Op revenue	253	232	218	211
Op expenses	192	181	171	167
EBITDA	**67**	**56**	**51**	**48**
Depreciation & Amortisation	11	12	12	12
EBIT	**56**	**44**	**39**	**37**
Net Interest	-5	-4	-3	-3
Profit Before Tax	51	40	36	33
Tax	-15	-12	-11	-10
Net Profit After Tax - pre Minorities, DI	**36**	**28**	**25**	**23**
Minority Interests	0	0	0	0
Net Profit (pre-NRI, DI)	**36**	**28**	**25**	**23**
Non-recurring Items - net	-2	0	0	0
Reported Net Profit	**36**	**28**	**25**	**23**
ModelWare EPS (¢ per share)	**9.1**	**7.7**	**6.8**	**6.4**
ModelWare EPS growth	8%	-16%	-11%	-7%

Half yearly analysis	2H13	1H14	2H14	2H15
Television	118	134	119	253
% growth	*-2%*	*1%*	*1%*	*88%*
Radio	-10	0	0	0
% growth	*-204%*			
Other	3	0	3	3
% growth	*171%*	*-100%*	*17%*	
Total Revenue	**111**	**134**	**122**	**256**
% growth	*-15%*	*-6%*	*10%*	*91%*
EBITDA	**27**	**35**	**29**	**65**
% growth	*-19%*	*0%*	*7%*	*83%*
NPAT	**14**	**21**	**10**	**31**
% growth	*20%*	*7%*	*-27%*	*49%*

Balance Sheet

Year End June (A$ mn)	F2015	F2016E	F2017E	F2018E
Current Assets	63	63	60	59
Non Current Assets	241	240	234	227
Total assets	**304**	**304**	**294**	**286**
Current Liabilities	42	40	38	37
Non Current Liabilities	89	87	73	70
Total Liabilities	**131**	**127**	**111**	**107**
Net Assets	174	177	183	179
Share Capital	310	310	310	310
Reserves	4	4	4	4
Retained Profits	-141	-138	-131	-135
Minorities	0	0	0	0
Total Shareholders Equity	**174**	**177**	**183**	**179**
Property, Plant & Equipment	35	31	24	18
Intangibles	200	200	200	200
Borrowings	89	87	73	70
Net Debt (A$m)	79	77	63	60
EBIT/net interest	11.7x	10.7x	11.4x	11.2x
EBITDA/net interest	14.1x	13.5x	14.9x	14.9x

Cash Flow Statement

Year End June (A$ mn)	F2015	F2016E	F2017E	F2018E
EBITDA - operational	67	56	51	48
Operating cashflow	**58**	**38**	**38**	**36**
Payments for Property, Plant & Equi	-6	-5	-5	-5
Net Payments for investments	0	-10	0	-10
Other operating cashflow	1	0	0	0
Investment Activities	**-5**	**-15**	**-5**	**-15**
Proceeds from Borrowing	118	0	0	0
Repayment of Borrowing	-149	-1	-14	-3
Dividends paid	-24	-21	-19	-17
Financing Activities	**-56**	**-22**	**-33**	**-21**
Net change in cash	-3	0	0	0

Segment Information

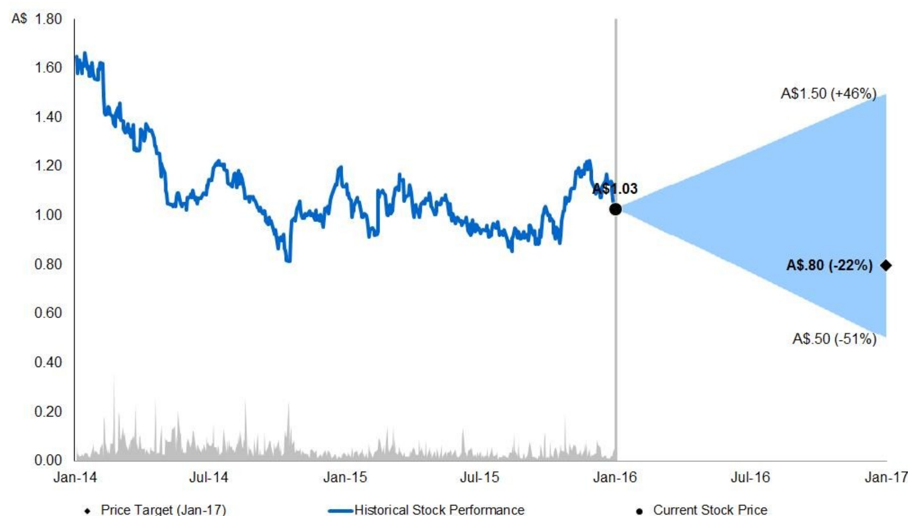
Year End June (A$ mn)	F2015	F2016E	F2017E	F2018E
Revenue				
Television	253	232	218	211
Radio	0	0	0	0
Digital Media	0	0	0	0
Total Revenue	**253**	**232**	**218**	**211**
EBITDA				
Television	67	56	51	48
Radio	0	0	0	0
Unallocated	0	0	0	0
TOTAL EBITDA	**67**	**56**	**51**	**48**

Half yearly forecasts	2H15E	1H16E	1H16E	2H16E
EPS	4.1	4.2	3.5	4.2
- change	36%	-21%	-15%	99%

Source: PRT, Morgan Stanley Research

SXL Risk-Reward

Risk to SXL's revenue, costs and EPS remain wider than Media peers



Source: Thomson Reuters (historical share price data). E = Morgan Stanley Research estimates

Price Target A$0.80	Based on the average of our DCF, P/E and EV/EBITDA valuations.
Bull A$1.50 12x bull case F2017E EPS 12c	**Stronger advertising markets + SXL market share gains.** TV/Radio ad market returns to 5-6% growth in F2016-17E. In addition, SXL increases market share in both TV/radio and, importantly, is able to use cash generated to de-lever and pay down debt faster. Bull case EPS of 12c is ~20% above base case.
Base A$0.80 8x base case F2017E EPS 9.9c	**Modest positive growth in TV & Radio ad market;** SXL's ad market share stabilizes. We forecast 2-3% ad growth in F2016-17. SXL market share in Metro Radio gains 50bps to hold steady at 28%. Base case F2017E EPS of 9.9c.
Bear A$0.50 6x bear case F2017E 8c	**Recession hits Australia, advertising deteriorates further in F2016-17E;** equity raising more likely. Captures: i) higher loss of ad market share in TV and radio; ii) accelerated negative structural change – in Regional TV and from Internet Radio players: Bear case F2017E EPS of 8c is ~20% below base case.

We Remain Underweight

- We see absolute downside in SXL shares of -22% over the next 12-18 months and also expect underperformance versus the rest of our Australian Media coverage universe.

Key Value Drivers

- Overall TV and radio advertising market growth: All else equal, +/-1ppt in TV and/or radio system advertising growth results in +/-2% EPS.
- SXL's TV and radio audience and advertising market share: All else equal, +/-1ppt in market share results in +/-2% EPS.
- Television advertising market share: All else equal, +/-1% in TV advertising share means +/-6% EPS.

Key Upside Risks to our price target

- Overall TV and radio advertising markets could be dramatically stronger in C2016 and C2017. If this occurred, it would result in upside to consensus earnings expectations, even if the company were to lose market share.
- SXL is able to successfully reverse recent Metro radio &/or Regional TV audience and advertising market shares losses.
- Positive regulatory change. For example, this could come in the form of either further TV Licence fee cuts and/or removal of the TV Audience Reach rules (75% audience cap) and/or removal of Cross Media Ownership rules (2-from-3). All of these would be positive for either SXL's earnings or asset valuations.

SXL Updated Valuation

Our PT is A$0.80/share (unchanged) as we roll forward our estimates to F2017E.

We derive our price target from three methodologies: P/E, EV/EBITDA-based sum-of-the-parts and discounted cash flow (DCF). We take an average of all three valuation methods. We use a DCF methodology because we think the DCF captures the long-term cyclicality of TV broadcasters, whereas the P/E and EV/EBITDA methods focus on short-term earnings.

In summary:

- **P/E valuation is A$0.79/share** (was A$0.77/share). Our valuation rises as we roll forward EPS estimates of 9.9c for F2017E (was 9.7c EPS F2016E). We apply a 8x multiple (unchanged), reflecting a ~50-60% discount to the Australian market multiple. We still believe a discount to the broader market is appropriate to reflect the uncertainty surrounding future earnings due to: i) negative structural change facing SXL's media businesses; ii) volatility in SXL's market shares, particularly Metro Radio and Regional TV assets; and iii) considerably higher debt levels than media peers.
- **Sum-of-the-Parts (SOTP) value is A$1.02/share** (was A$0.88/share), also lifted as we roll forward our estimates to F2017E. We apply a 7x (unchanged) EV/EBITDA target multiple to Metro FM Radio (discount to multiple paid for asset due to market share losses), 5x (unchanged) for Regional TV (discount to peers given it's both regional and performing below that of PRT), 7.5x (unchanged) for Regional radio (reflecting SXL's strong competitive position in the regional radio market).
- **Discounted Cash Flow (DCF) value is A$0.66/share** (was A$0.75)**.** The lowered DCF reflect a softer TV ad market and higher corporate costs. We use a WACC of 11% and terminal growth rate of 3% (both unchanged).

SXL Financial Summary

Exhibit 37: SXL Financial Summary

Income Statement

(A$m) Year End June 30		F2015	F2016E	F2017E	F2018E
Metro Radio Revenue	A$m	224	236	241	243
Regional TV Revenue	A$m	201	207	212	214
Regional Radio Revenue	A$m	160	166	172	178
Total Revenue	**A$m**	**585**	**609**	**624**	**634**
- change	%	-4%	4%	2%	2%
Total Operating Expenses	**A$m**	**-422**	**-436**	**-448**	**-458**
- change	%	0%	3%	3%	2%
Metro Radio EBITDA	A$m	58	63	63	62
Regional TV EBITDA	A$m	29	30	29	26
Regional Radio EBITDA	A$m	86	90	94	98
Corporate Overhead	A$m	-9	-10	-10	-10
EBITDA	**A$m**	**163**	**173**	**176**	**176**
- change	%	-13%	6%	2%	0%
Depreciation & Amortisation	A$m	-29	-29	-29	-31
- change	%	1%	2%	6%	2%
EBIT	**A$m**	**135**	**144**	**147**	**145**
- change	%	-16%	7%	2%	-1%
Net interest	A$m	-39	-32	-28	-26
Profit Before Tax	A$m	96	113	118	119
Income Tax	A$m	-31	-34	-35	-36
Profit After Tax	A$m	65	79	83	83
Associates / JVs equity accounted	A$m	0	0	0	0
Minorities	A$m	0	0	0	0
NPAT (pre-NRI)	**A$m**	**64.8**	**78.8**	**82.8**	**83.2**
- change	%	-19%	22%	5%	0%
Non-Recurring Items	A$m	-349.7	0.0	0.0	0.0
Reported NPAT	**A$m**	**-284.9**	**78.8**	**82.8**	**83.2**
- change	%	-4%	-128%	5%	0%
EPS - Basic Reported	cents	-37.8	10.1	9.9	9.8
- change	%	-10%	-127%	-2%	-1%
EPS - Basic (Pre-NRI)	**cents**	**8.6**	**10.1**	**9.9**	**9.8**
- change	%	-24%	18%	-2%	-1%
DPS	cents	6.4	7.5	7.3	7.3
EBITDA Margin	%	28%	28%	28%	28%
NPAT (Pre-NRI) Margin	%	11%	13%	13%	13%
P / E Ratio	(x)	12.4x	10.5x	10.7x	10.8x
EV / EBITDA	(x)	8.0x	7.5x	7.2x	7.1x
EV / EBIT	(x)	9.5x	8.8x	8.5x	8.5x
EV / Sales	(x)	2.2x	2.1x	2.0x	1.9x

Other Value Drivers & Key Ratios

(A$m) Year End June 30		F2015	F2016E	F2017E	F2018E
Net Debt	A$m	526	449	368	346
Net Debt / Equity	%	56%	44%	33%	31%
Net Debt / EBITDA ratio	(x)	3.2x	2.6x	2.1x	2.0x
Net Debt / EBITDA - for covenants	(x)	3.0x	2.4x	1.9x	1.8x
EBIT/Net Interest Expense cover	(x)	3.5x	4.6x	5.2x	5.6x
Net Tangible Assets	A$m	449	531	616	640
NTA/Share	$ actual	0.60	0.68	0.74	0.76
ROE	%	7%	8%	8%	7%
Operating Capex/Sales	%	4.8%	4.8%	4.8%	4.9%

Half yearly forecasts		2H15E	1H16E	2H16E	2H16E
EPS	**cents**	**4.2**	**5.2**	**5.0**	**5.2**
- change	%	-12%	18%	18%	18%

Balance Sheet

(A$m) Year End June 30		F2015	F2016E	F2017E	F2018E
Current Assets					
Cash (Negative = Overdraft)	A$m	143	220	302	323
Receivables	A$m	122	127	130	132
Other	A$m	0	0	0	0
Total Current Assets	**A$m**	**265**	**347**	**432**	**455**
Non-Current Assets					
Property, plant & equipment	A$m	164	164	165	164
Radio licences	A$m	1,289	1,289	1,289	1,289
Investments	A$m	3	3	3	3
Other	A$m	17	17	17	17
Total Non-Current Assets	**A$m**	**1,473**	**1,474**	**1,474**	**1,474**
Total Assets	**A$m**	**1,738**	**1,821**	**1,906**	**1,929**
Current Liabilities					
Accounts payable	A$m	89	92	95	96
Borrowings	A$m	21	21	21	21
Current tax liabilities	A$m	7	7	7	7
Provisions	A$m	21	21	21	21
Other	A$m	0	0	0	0
Total Current Liabilities	**A$m**	**138**	**142**	**144**	**146**
Non-Current Liabilities					
Interest bearing liabilities	A$m	648	648	648	648
Deferred tax liabilities	A$m	0	0	0	0
Provisions		14	14	14	14
Other	A$m	2	2	2	2
Total Non-Current Liabilities	**A$m**	**663**	**663**	**663**	**663**
Total Liabilities	**A$m**	**802**	**805**	**807**	**809**
Net Assets	**A$m**	**937**	**1,016**	**1,098**	**1,120**
Total Shareholders Equity	**A$m**	**937**	**1,016**	**1,098**	**1,120**

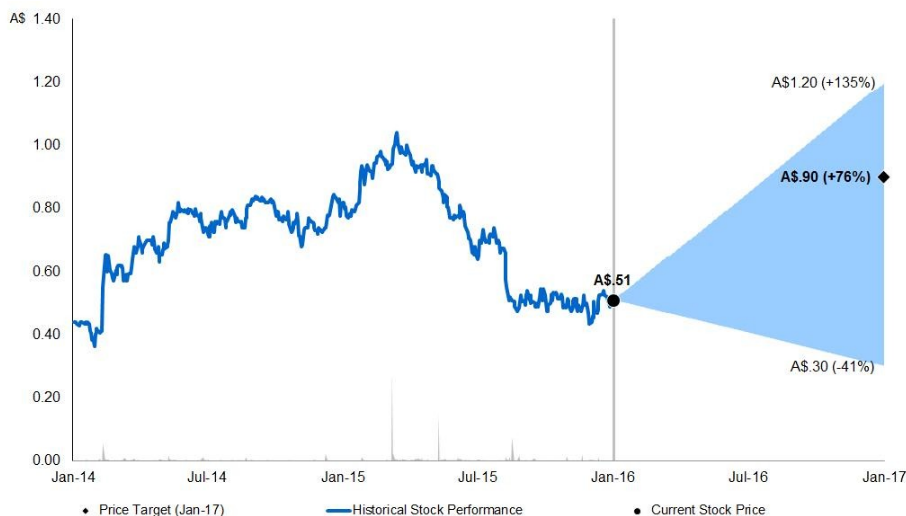
Cash Flow Statement

(A$m) Year End June 30		F2015	F2016E	F2017E	F2018E
Operating Cash Flows					
EBITDA	A$m	163	173	176	176
Working capital (incr.)/decr.	A$m	0	-1	-1	-1
Net interest	A$m	-39	-32	-28	-26
Income taxes paid	A$m	-44	-34	-35	-36
Other	A$m	0	0	0	0
Total Operating Cash Flows	**A$m**	**78**	**106**	**111**	**114**
- change	%				
Investing Cash Flows					
Purchase of PPE	A$m	-28	-29	-30	-31
Proceeds from sale of investments	A$m	0	0	0	0
Other investing	A$m	9	0	0	0
Total Investing Cash Flows	**A$m**	**-19**	**-29**	**-30**	**-31**
Financing Cash Flows					
Dividends paid	A$m	-16	-58	-61	-62
Proceeds from borrowings	A$m	22	0	0	0
Other financing	A$m	16	58	61	0
Total Financing Cash Flows	**A$m**	**22**	**0**	**0**	**-62**
Net change in cash	**A$m**	**81**	**77**	**81**	**21**

Source: Morgan Stanley Research

APN Risk-Reward

Risk-Reward View: Shape of Ad Market Recovery Is Important



Source: Thomson Reuters (historical share price data). E = Morgan Stanley Research estimates

Price Target A$0.90 — Based on the average of our DCF, P/E and EV/EBITDA valuations

Bull A$1.20
13x bull case F2017E EPS 9c

Stronger growth in advertising in C2016-C2017: NZ and Australian economies rebound, giving APN top line growth of +2%. Bull Case EPS of 9.0c in C2017E, ~20% above base case. In addition, higher EPS growth spurs P/E re-rating**.**

Base A$0.90
10x base case F2017E EPS 7.5c

Modest advertising recovery in C2016-C2017: Total revenue still negative because of newspapers, but radio achieves revenue growth. Forecast C2017E EPS 7.5c.

Bear A$0.30
5x bear case F2017E 6c

Australia + NZ; advertising deteriorates in C2016-17 + Radio loses market share + more severe impact of online migration hurts NZ Herald. EPS is a 6c in C2017E, ~20% below the base case, and P/E de-rates to 5x (it hit a low of 4x-5x during C2012-C2013, when solvency was in question)**.**

Why We Are Overweight?

- After an extended period of share price underperformance, over the last 12 months APN has taken action to improve its asset mix, simplify its corporate structure and strengthen its balance sheet.
- We see upside potential to medium-term earnings and potential for faster debt paydown.
- We see absolute upside in APN shares: our PT implies >50% capital appreciation (zero dividend) over the next 12 months.

Key Value Drivers

- APN is a cyclical business and dependent on the advertising cycle – operating in Radio broadcasting (60% of EBITDA), Outdoor (10% of EBITDA) and Newspaper publishing (30% of EBITDA).
- Geographically, the company is heavily exposed to NZ, with approx. 30% of group EBITDA.

Key Risks to our price target

- Weaker ad market than our base case would result in downgrades to APN earnings and valuation and vise versa in a stronger ad market.
- Recent gains in audience and ad market share made by APN radio businesses could reverse.
- The expected reduction in APN's net debt levels over the next 1-2 years could fail to materialize, in the event of a cyclical slowdown in earnings and/or if our expectations for further assets sales fail to materialize.
- Newspapers earnings outlook continues to deteriorate more than expected.

APN Updated Valuation

Our price target falls to A$0.90/share (was A$1.20), as a result of EPS downgrades of -12% to -13% over C2015-C2017E due to weaker newspaper earnings and a higher effective tax rate.

This represents the approximate midpoint of our assessed value range of A$0.70-A$1.01/share, which is derived by using three methodologies – target P/E multiples, sum-of-parts and DCF valuation.

In summary:

- **P/E valuation is A$0.75/share** (was A$1.23/share), lowered due to the -12% to -13% downgrades to EPS and a lower P/E multiple of 10x (was 14x), reflecting the weaker-than-expected newspaper earnings and higher effective tax rate. We also roll forward our EPS estimate to 7.5c C2017E (was 8.3c C2016E).
- **Sum-of-the-Parts (SOTP) value is A$1.01/share** (was A$1.15/share), also lowered due to the EBITDA downgrades of -4% to -6% in C2015-C2017 and a lower target multiple for the Radio business of 8x (was 10x) as initial revenue and EBITDA growth from the acquisition start to moderate. We roll forward our valuation to C2017.
- **Discounted Cash Flow (DCF) value is A$0.70/share** (was A$1.06), similarly lowered due to lower earnings and a higher WACC of 11% (was 9.6%) to reflect the higher risk to earnings from newspapers and the weaker NZ economy. We retain our 3% terminal growth rate.

APN Financial Summary

Exhibit 38: APN Financial Summary

Key Assumptions

Year End December	C2014	C2015E	C2016E	C2017E
Aust Publishing - Circulation Rev gr	-4.0%	-4.0%	-4.0%	-4.0%
Aust Publishing - Ad Rev growth	-8.0%	-10.3%	-8.6%	-8.0%
Aust Newsprint cost increase / tonne	-8.0%	-5.0%	-5.0%	-5.0%
Aust Labour Cost inflation	-5.0%	-3.0%	-3.0%	-3.0%
NZ Publishing - Circ Revenue growth	-6.0%	-6.0%	-6.0%	-6.0%
NZ Publishing - Ad Revenue growth	11.3%	-3.7%	-2.5%	-2.2%
NZ Newsprint cost increase / tonne	-4.0%	-5.0%	-5.0%	-5.0%
NZ Labour Cost inflation	-4.0%	-4.0%	0.0%	0.0%
Aust Radio Advertising growth	3.0%	3.0%	3.0%	3.0%
Aust Radio Ad Market Share 5 Cap Cities	23.3%	25.7%	26.3%	26.3%
NZ Radio Advertising growth	5.0%	3.0%	3.0%	3.0%
NZ Radio Ad Market Share	45.7%	45.7%	45.7%	45.7%
Effective Tax rate	13%	24%	25%	26%
Interest Cost	9.0%	7.0%	7.0%	7.0%
Capital Expenditure (A$m)	15	32	13	14
Capex as % of Sales	2%	4%	2%	2%

Ratio Analysis

Year End December	C2014	C2015E	C2016E	C2017E
ModelWare EPS (¢ per share)	7.3c	7.0c	7.3c	7.5c
ModelWare EPS growth	-17%	-4%	4%	3%
Estimated Fully Taxed EPS (¢ per share)		6.5	6.8	7.1
Average diluted shares outstanding (m)	1,029	1,029	1,029	1,029
P/E, Modelware	9.2x	9.5x	9.2x	8.9x
DPS (¢ per share)	0.0	0.0	0.0	0.0
Dividend yield	0.0%	0.0%	0.0%	0.0%
Dividend payout ratio	0%	0%	0%	0%

Income Statement

Year End December (A$ mn)	C2014	C2015E	C2016E	C2017E
Op revenue	843	844	839	834
Op expenses	-690	-688	-688	-687
EBITDA (incl. Associate share of Adshel)	**164**	**168**	**164**	**160**
EBITDA (ex. Associate share of Adshel)	**153**	**155**	**151**	**147**
Depreciation & Amortisation	-33	-33	-33	-32
EBIT	**131**	**134**	**131**	**128**
Net Interest	-36	-38	-30	-22
Profit Before Tax	95	96	101	106
Tax	-12	-23	-25	-28
Net Profit After Tax - pre Minorities, NRI	**83**	**73**	**76**	**78**
Minority Interests	-8	-1	-1	-1
Net Profit (pre-NRI)	**75**	**72**	**75**	**77**
Associates		0	0	0
Net Profit after Associates (pre-NRI)	**75**	**72**	**75**	**77**
Non-recurring Items - net	0	0	0	0
Reported Net Profit	**75**	**72**	**75**	**77**

Half Yearly Analysis	1H C2014E	2H C2014E	1H C2015E	2H C2015E
Revenue	438	405	438	403
EBITDA	**71**	**93**	**72**	**91**
NPAT (pre-NRI)	21	54	20	56
EPS (pre-NRI)	**2.0**	**5.3**	**2.0**	**5.5**

Half Yearly Analysis	1H C2015E	2H C2015E	1H C2016E	2H C2016E
EPS	2.0	5.1	2.0	5.2

Balance Sheet

Year End December (A$ mn)	C2014	C2015E	C2016E	C2017E
Current Assets	185	154	235	358
Non Current Assets	944	1,021	1,001	983
Total assets	1,129	1,175	1,236	1,341
Current Liabilities	132	118	118	117
Non Current Liabilities	525	525	525	525
Total Liabilities	657	643	642	642
Net Assets	472	532	594	699
Share Capital	1,223	1,223	1,223	1,223
Reserves	-139	-151	-164	-136
Retained Profits	-647	-574	-499	-422
Minorities	35	35	35	35
Total Shareholders Equity	**472**	**532**	**594**	**700**
Property, Plant & Equipment	134	211	191	173
Intangibles	691	691	691	691
Borrowings	495	495	495	495
Net Debt (A$m)	456	496	415	291
Reported EBIT/net interest	2.5x	2.3x	2.7x	3.4x
Reported EBITDA/net interest	3.3x	3.0x	3.6x	4.6x
Net Debt / EBITDA ratio	2.8x	3.0x	2.5x	1.8x

Cash Flow Statement

Year End December (A$ mn)	C2014	C2015E	C2016E	C2017E
EBITDA - operational	164	168	164	160
Operating cashflow	**72**	**70**	**95**	**138**
Payments for Propery, Plant & Equipm	-15	-32	-13	-14
Net Payments for investments	71	-78	0	0
Other operating cashflow	10	0	0	0
Investment Activities	**65**	**-110**	**-13**	**-14**
Proceeds from Share issue	128	0	0	0
Proceeds from Borrowing	865	0	0	0
Repayment of Borrowing	-842	0	0	0
Dividends paid	0	0	0	0
Debenture interest	0	0	0	0
Financing Activities	**-120**	**0**	**0**	**0**
Net change in cash	18	-40	82	124

Segment Information

Year End December (A$ mn)	C2014	C2015E	C2016E	C2017E
Revenue				
Newspapers	476	446	423	404
Radio	298	325	340	351
Outdoor	50	52	55	58
Corporate	0	0	0	0
Total Revenue	843	844	839	834
EBITDA				
Newspapers	73	59	48	40
Radio	90	104	111	115
Outdoor (incl. Adshel associate)	14	16	17	17
Corporate	-17	-16	-16	-16
TOTAL EBITDA	164	168	164	160
Newspapers as % of EBITDA	44%	35%	29%	25%
Radio as % of EBITDA	55%	62%	68%	71%

Source: Thomson Reuters (historical share price data). E = Morgan Stanley Research estimates

SKT Risk-Reward

Risk-Reward View: Mature Business With Structural Risk Suggest Further De-rating

Source: Thomson Reuters (historical share price data). E = Morgan Stanley Research estimates

Price Target	**NZ$5.00**	Base case scenario, average of three methodologies: P/E, EV/EBITDA-based sum of parts, and DCF.
Bull 15x bull case F2017E EPS 46c	**NZ$7.00**	**Strong economic recovery:** Strong real GDP growth in FY2016 and FY2017 supports ARPU CAGR of 5-6% combined with positive subscriber CAGR growth over the same period. We also forecast EBITDA margin expansion of 1% in FY16 and FY17.
Base 13x base case F2017E EPS 39.4c	**NZ$5.00**	**Gradual economic recovery:** Moderate real GDP growth in FY2016 and FY2017 supports ARPU CAGR of 2-3% combined with negative subscriber CAGR of -2% over the same period. We forecast flat EBITDA margins in FY15 and FY16**.**
Bear 10x bear case F2017E 33c	**NZ$3.50**	**Double dip and SKT loses exclusivity of the Rugby Union TV sports rights:** Real GDP declines in FY2016 and is flat in FY2017, resulting in ARPU CAGR of -5% combined with subscriber CAGR of -1% over the same period. We forecast EBITDA margin contraction of 1% in FY14 and FY15.

Why Equal-weight?

- We expect the stock to perform in-line with the market and peer group on a 12-month view.
- Low pay penetration (~50%) by global standards suggests SKT has the ability to grow its subs base through increasing penetration, which can be achieved by lower priced products.
- As the Ultra-fast broadband network is completed, SKT will increasingly gain the ability to start to offer consumers a triple-play product which has been a significant growth driver for US payTV firms.
- We believe SKT faces competition from OTT players entering the market, however US experience suggest flat to small negative subs growth with increased churn and we believe this is priced in.
- SKT's financial flexibility suggests it could increase capital returns, e.g. special dividends. SKT has publicly stated that investors should not expect capital management in the near term.

Key Value Drivers

- Subscriber growth: All else equal, +/-1% change in subscriber growth means +/-2% change in EPS.
- ARPU growth: All else equal, +/-1% change in ARPU growth means +/-2% change in EPS.

Key Risks to our price target

- An announcement of capital management would be a positive catalyst.
- SKT loses the sports rights for the Rugby, a negative catalyst.
- A global IPTV firms starts in NZ, increasing competition, a negative catalyst.

SKT Updated Valuation

Our price target falls to NZ$5.00/share (was NZ$6.10), as a result of EPS downgrades of -3% to -3% over C2016-C2017E due to lower subscriber growth and higher programming costs.

This represents the approximate midpoint of our assessed value range of NZ$4.54-NZ$5.26/share, which is derived by using three methodologies – target P/E multiples, sum-of-parts and DCF valuation.

In summary:

- **P/E valuation is NZ$4.73/share** (was NZ$6.26/share), lowered due to earnings downgrades mentioned and a lowered PE target of 12x (was 14.4x) due to lower subscriber growth and higher programming costs. We roll forward to F2017E EPS of 40.1c (was F2016E 47c).
- **Sum-of-the-Parts (SOTP) value is NZ$5.26/share** (was NZ$5.92/share), also lower due to earnings downgrades, and we roll forward our focus to F2017E. Target multiple is unchanged at 7x EV/EBITDA, which is below the long-term historical 12-month EV/EBITDA multiple of 8x, due to the rising structural risk of OTT services in NZ.
- **Discounted Cash Flow (DCF) value is NZ$4.54/share** (was NZ$6.08), lower due to the earnings downgrades, which are more substantial in later years. The WACC is 10.5% (unchanged) and terminal growth rate remains 2%.

SKT Financial Summary

Exhibit 39: SKT Financial Summary

Income Statement

(NZ$m) Year End June 30		F2015	F2016E	F2017E	F2018E
Operating Revenue					
Subscription Revenue	NZ$m	831.2	831.7	837.1	836.9
- change	%	3%	0%	1%	0%
Advertising	NZ$m	69.5	70.1	68.2	65.7
- change	%	-2%	1%	-3%	-4%
Installation	NZ$m	4.5	5.6	4.1	3.7
- change	%	-44%	23%	-27%	-10%
Total Operating Revenue	**NZ$m**	**927.5**	**930.8**	**934.0**	**932.2**
- change	%	2%	0%	0%	0%
Operating Expenses					
Programming Costs	NZ$m	296.6	337.5	348.6	356.1
- change	%	6%	14%	3%	2%
Subscriber Management	NZ$m	107.1	108.0	103.3	101.5
- change	%	61%	1%	-4%	-2%
Broadcasting and infrastructure	NZ$m	91.2	92.4	92.5	87.0
- change	%	3%	1%	0%	-6%
Sales and Marketing	NZ$m	32.0	31.7	31.4	31.0
- change	%	0%	-1%	-1%	-1%
Advertising	NZ$m	21.5	21.9	21.7	21.4
- change	%	3%	2%	-1%	-1%
Other Admin	NZ$m	0.0	0.0	0.0	0.0
- change	%	-100%			
Total Operating Expenses	**NZ$m**	**548.4**	**591.5**	**597.4**	**597.0**
- change	%	5%	8%	1%	0%
Reported EBITDA	**NZ$m**	**379.7**	**339.4**	**336.1**	**334.5**
- change	%	0%	-11%	-1%	0%
Depreciation & Amortisation					
Depreciation	NZ$m	-99.0	-94.2	-92.5	-91.3
Amortisation	NZ$m	-9.1	-9.5	-11.2	-5.6
Total Depreciation & Amortisation	**NZ$m**	**-108.1**	**-103.7**	**-103.7**	**-96.9**
EBIT	**NZ$m**	**271.6**	**235.7**	**232.4**	**237.6**
Interest Income	NZ$m	0.8	0.1	0.3	0.8
Interest Expense	NZ$m	-22.5	-19.0	-19.0	-19.0
Net interest	NZ$m	-21.7	-18.9	-18.8	-18.3
Minorities	NZ$m	0.2	0.3	0.3	0.4
Profit Before Tax	NZ$m	249.9	216.8	213.6	219.3
Income Tax (expense)/benefit	NZ$m	-67.1	-60.7	-59.8	-61.4
NPAT (pre-NRIs)	**NZ$m**	**182.8**	**156.1**	**153.8**	**157.9**
- change	%	10%	-15%	-1%	3%
Non-Recurring Items (NRIs)	NZ$m	10.8	0.0	0.0	0.0
Reported NPAT	NZ$m	171.8	155.9	153.5	157.5
- change	%	4%	-9%	-2%	3%
EPS - Basic Reported	cents	44.1	40.1	39.4	40.5
- change	%	4%	-9%	-2%	3%
EPS - Diluted (Pre-NRIs)	**cents**	**46.9**	**40.1**	**39.4**	**40.5**
- change	%	7%	-15%	-2%	3%
DPS	cents	30	28	28	28
Basic Weighted Avg No. of Shares	millions	389.1	389.1	389.1	389.1
Basic No. of Shares on issue	millions	389.1	389.1	389.1	389.1
Diluted Weighted Avg No. of Shares	millions	389.1	389.1	389.1	389.1
Residential TV Subscribers	actual	798,289	792,520	775,412	755,152
Commercial TV Subscribers	actual	9,300	9,472	8,777	8,535
Other Subs	actual	32,000	32,960	33,949	34,967
Total Subcribers	**actual**	**851,561**	**834,952**	**818,137**	**798,655**
- change	%	-1.6%	-2.0%	-2.0%	-2.4%
MySky subscribers	actual	549,906	581,329	592,402	592,402
MySky subscribers as % of residential TV subs	%	69%	73%	76%	78%
Total ARPU - Per Month	NZ$m	79.54	81.88	84.35	86.30
- change	%	3%	3%	3%	2%
Churn - Annualised	%	14.5%	16.0%	18.0%	18.0%
P/E Ratio	(x)	15.3x	16.8x	17.1x	16.7x
EV/EBITDA	(x)	7.8x	8.7x	7.3x	8.3x
EV/EBIT	(x)	10.9x	12.5x	11.0x	12.0x

Half yearly forecasts		2H15	1H16E	2H16E	1H17E
EPS	**cents**	**23.1**	**20.8**	**19.2**	**19.7**
- change	%	3%	-12%	-17%	-15%

Balance Sheet

(NZ$m) Year End June 30		F2015	F2016E	F2017E	F2018E
Current Assets					
Cash & cash equivalents	NZ$m	17.9	24.1	35.2	94.7
Trade & other receivables	NZ$m	69.5	70.5	70.7	70.6
Program Inventory	NZ$m	72.8	58.2	58.3	58.2
Other financial assets	NZ$m	28.4	28.4	28.4	28.4
Total Current Assets	**NZ$m**	**188.6**	**181.2**	**192.7**	**251.9**
Non-Current Assets					
Property, plant & equipment	NZ$m	282.2	319.5	353.1	343.3
Intangible assets	NZ$m	21.0	17.0	11.4	11.4
Goodwill	NZ$m	1421.4	1421.4	1421.4	1421.4
Fair value derivatives	NZ$m	28.8	28.8	28.8	28.8
Deferred Tax	NZ$m	0.0	0.0	0.0	0.0
Total Non-Current Assets	**NZ$m**	**1753.4**	**1787.7**	**1816.4**	**1807.3**
Total Assets	**NZ$m**	**1942.0**	**1968.8**	**2009.1**	**2059.3**
Current Liabilities					
Trade & other payables	NZ$m	184.2	173.5	174.1	173.8
Interest bearing loans and borrowings	NZ$m	3.3	3.3	3.3	3.3
Income tax payable	NZ$m	12.3	12.3	12.3	12.3
Fair value derivatives	NZ$m	1.3	1.3	1.3	1.3
Total Current Liabilities	**NZ$m**	**201.1**	**190.4**	**191.0**	**190.7**
Non-Current Liabilities					
Interest bearing loans and borrowings	NZ$m	347.5	347.5	347.5	347.5
Deferred Tax	NZ$m	48.4	48.4	48.4	48.4
Provisions	NZ$m	0.0	0.0	0.0	0.0
Fair value derivatives	NZ$m	7.8	7.8	7.8	7.8
Total Non-Current Liabilities	**NZ$m**	**403.7**	**403.7**	**403.7**	**403.7**
Total Liabilities	**NZ$m**	**604.8**	**594.1**	**594.7**	**594.4**
Net Assets	**NZ$m**	**1337.2**	**1374.7**	**1414.4**	**1464.9**
Total Shareholders Equity	**NZ$m**	**1337.2**	**1376.6**	**1421.3**	**1471.8**

Cash Flow Statement

(NZ$m) Year End June 30		F2015	F2016E	F2017E	F2018E
Operating Cash Flows					
EBITDA	NZ$m	379.7	339.4	336.1	334.5
Working capital (incr.)/decr.	NZ$m	-5.6	3.0	0.2	-0.1
Net interest	NZ$m	-18.9	-18.8	-18.3	-16.1
Income taxes paid	NZ$m	-60.7	-59.8	-61.4	-61.0
Total Operating Cash Flows	**NZ$m**	**282.9**	**262.8**	**257.6**	**254.7**
- change	%	-7%	-7%	-2%	-1%
Investing Cash Flows					
Purchase of PPE	NZ$m	-114.5	-93.9	-96.7	-87.2
Other investing	NZ$m	0.9	46.0	40.7	0.7
Total Investing Cash Flows	**NZ$m**	**-115.4**	**-139.8**	**-137.4**	**-87.8**
Financing Cash Flows					
Ordinary share buyback	NZ$m	0.0	0.0	0.0	0.0
Proceeds from borrowings	NZ$m	0.0	0.0	0.0	0.0
Repayment of borrowings	NZ$m	0.0	0.0	0.0	0.0
Other financing	NZ$m	0.0	0.0	0.0	0.0
Dividend paid	NZ$m	-131.1	-116.7	-109.1	-107.4
Total Financing Cash Flows	**NZ$m**	**-169.5**	**-116.7**	**-109.1**	**-107.4**
Net change in cash	**NZ$m**	**-2.0**	**6.2**	**11.1**	**59.4**

Other Value Drivers

(NZ$m) Year End June 30		F2015	F2016E	F2017E	F2018E
Net Debt	NZ$m	342.0	335.8	324.6	265.2
Net Debt / Shareholders Equity (Book Va	%	26%	24%	23%	18%
Net Tangible Assets	NZ$m	-105.2	-63.7	-18.4	32.1
NTA/Share	NZ$	-0.27	-0.16	-0.05	0.08
ROA	%	10%	8%	8%	8%
Reported EBITDA Margin	%	41%	36%	36%	36%
NPAT (Pre-NRIs) Margin	%	20%	17%	16%	17%
Effective Tax Rate	%	27%	28%	28%	28%
Net debt/EBITDA	(x)	0.9x	1.0x	1.0x	0.8x
EBIT/net interest expense	(x)	12.5x	12.5x	12.4x	13.0x

Source: Thomson Reuters (historical share price data). E = Morgan Stanley Research estimates

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Analyst Stock Ratings

Overweight (O). The stock's total return is expected to exceed the average total return of the analyst's industry (or industry team's) coverage universe, on a risk-adjusted basis, over the next 12-18 months.
Equal-weight (E). The stock's total return is expected to be in line with the average total return of the analyst's industry (or industry team's) coverage universe, on a risk-adjusted basis, over the next 12-18 months.
Not-Rated (NR). Currently the analyst does not have adequate conviction about the stock's total return relative to the average total return of the analyst's industry (or industry team's) coverage universe, on a risk-adjusted basis, over the next 12-18 months.
Underweight (U). The stock's total return is expected to be below the average total return of the analyst's industry (or industry team's) coverage universe, on a risk-adjusted basis, over the next 12-18 months.
Unless otherwise specified, the time frame for price targets included in Morgan Stanley Research is 12 to 18 months.

Analyst Industry Views

Attractive (A): The analyst expects the performance of his or her industry coverage universe over the next 12-18 months to be attractive vs. the relevant broad market benchmark, as indicated below.
In-Line (I): The analyst expects the performance of his or her industry coverage universe over the next 12-18 months to be in line with the relevant broad market benchmark, as indicated below.
Cautious (C): The analyst views the performance of his or her industry coverage universe over the next 12-18 months with caution vs. the relevant broad market benchmark, as indicated below.
Benchmarks for each region are as follows: North America - S&P 500; Latin America - relevant MSCI country index or MSCI Latin America Index; Europe - MSCI Europe; Japan - TOPIX; Asia - relevant MSCI country index or MSCI sub-regional index or MSCI AC Asia Pacific ex Japan Index.

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INDUSTRY COVERAGE: Australia Media, Internet and Technology

COMPANY (TICKER)	RATING (AS OF)	PRICE* (01/26/2016)
Andrew McLeod		
APN News & Media Ltd. (APN.AX)	O (03/12/2014)	A$0.52
APN Outdoor Group Limited (APO.AX)	O (12/28/2014)	A$5.99
Fairfax Media (FXJ.AX)	O (08/23/2012)	A$0.88
Navitas Limited (NVT.AX)	E (07/10/2014)	A$4.58
News Corporation (NWSA.O)	E (02/09/2015)	US$12.80
Nine Entertainment (NEC.AX)	U (06/09/2015)	A$1.71
Prime Media Group Ltd (PRT.AX)	U (03/01/2015)	A$0.49
REA Group Limited (REA.AX)	O (06/19/2009)	A$53.09
SEEK Limited (SEK.AX)	O (02/21/2013)	A$14.49
Seven West Media Ltd (SWM.AX)	U (10/07/2005)	A$0.83
Southern Cross Media Group Limited (SXL.AX)	U (07/15/2011)	A$1.08
Ten Network Holdings (TEN.AX)	O (08/05/2009)	A$1.50
Trade Me Group Ltd. (TME.NZ)	O (01/23/2012)	NZ$4.19
Mark Goodridge, CFA		
carsales.com Limited (CAR.AX)	O (02/13/2013)	A$11.32
Sky Network Television Limited (SKT.NZ)	E (08/26/2013)	NZ$4.57

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* Historical prices are not split adjusted.

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