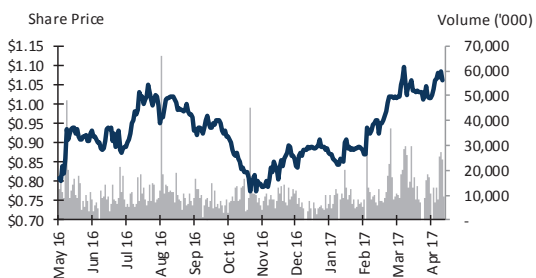




Fairfax Limited (FXJ) - Buy

Likely Restructuring, Divestments Can Extract Significant Value, Growth Potential in New Verticals

Recommendation	BUY
Previous	BUY
Risk	High
Price Target	\$1.25
Previous	\$1.40
Share Price (A\$)	1.06
ASX Code	FXJ
52 week low - high (A\$)	\$0.72-\$1.14
Capital structure	
Shares on Issue (M)	2,309.4
Market Cap (A\$M)	2,448
Net Debt/(Cash) (A\$M)	125
EV (A\$M)	2,573
Fully diluted mkt cap (A\$M)	2,448
12mth Av Daily Volume ('000)	10,516
Board	
Nick Falloon	Chairman
Patrick Allaway	Non-Executive Director
Jack Cowin	Non-Executive Director
Greg Hywood	CEO
Sandra McPhee	Non-Executive Director
James Millar	Non-Executive Director
Linda Nicholls	Non-Executive Director
Mickie Rosen	Non-Executive Director
Todd Sampson	Non-Executive Director
Major Shareholders	
Ausbil	7.7%
Legg Mason	6.1%
Perennial Value	5.1%
Henderson	5.1%
Blackrock	5.0%
Share Price Graph	



Analyst: Darren Odell, CFA +61 2 9993 8121
 darren.odell@fostock.com.au
 The analyst owns no shares in FXJ.

Talking Point mostly discusses stocks for which Foster Stockbroking does not provide formal research coverage. It combines both the dealing desk's market view and basic research analysis. The aim is to offer clients additional investment ideas that lie outside the firm's universe of formally covered stocks. Occasionally, some stocks under formal research coverage will also be discussed in Talking Point.

Event:

- We reiterate our positive view, following company updates.

Analysis:

- We value total Domain operations at \$2.3 billion, including premium plus listings (\$800m), property market leads opportunity (\$360m) & legacy operations (\$1.1bn). Recently, we understand there has been an improvement in listing volumes following a sustained period of weakness. With price increases (+20%, 1st Jan), increasing premium listings penetration and possibly improving national footprint, all bodes well for upgrades to Domain's earnings down-the-track. FXJ are working through the separate listing of Domain, which is on-track for end of CY17E. FXJ commented that they expect debt of \$150m in the entity (FXJ is likely to be net cash). Issues to be worked through include: ATO and commercial agreements between related parties.
- Digital ventures and untapped verticals. Likely hidden gems include: motoring, SVOD, travel, food, health, baby, jobs, et al. An immediate focus is new cars (Drive/112 JV), Stan, Events/conferences & travel (not to mention monetizing Street Talk appropriately).
- One day print advertising will stabilize: We await the day there is a moderation in the decline of print advertising (to c.1-2%), but it is not likely in the next 6 (or 12 mths). Today the decline is -11%. FXJ again reiterated that they will look to cut costs in Metro Media (c.\$30m) enabling earnings stability over the next 2-years. Interestingly, FXJ's print and digital operations have been separated for internal reporting purposes. FXJ is open to the sale of its regional media operations (\$113m: our valuation). We understand there are industry discussions involving digital advertising exchanges and back-end consolidation to reduce costs.
- We would expect further cost outs in FXJ's NZ operations and an increased focus on monetizing stuff.co.nz's audience through transactional business models, in select vertical markets. With investment likely required, it would not be a surprise to see a JV occur in some form down the track, along with agreements from industry participants to reduce costs. We would not necessarily expect the Commerce Commission decision to be appealed.

Earnings, Valuation & Recommendation:

- On a sum-of-the-parts basis, we value FXJ at \$1.25 per share (prior \$1.40). Our valuation of the assets TPG are interested in are \$1.07 (vs TPG's \$0.95 offer), with the remainder \$0.18 (includes corporate costs split 50% and \$150m net debt in remainder). We would expect the FXJ Board to reject the proposal. The current share price appears well under-pinned & fails to reflect any additional wins, as FXJ transitions to a new world organization.
- We maintain our recommendation on FXJ as BUY and have lowered our earnings estimates, largely reflecting lower listing volumes for Domain and continued revenue declines in ACM. The option value of one, two or three successes in certain verticals/investments is likely to provide material upside to the current share price, in time. Property vertical is the 'jewel in the Crown' today.