

EQUITY RESEARCH

BLT; CHOO; FCSS : BUY



COLLINS SARRI STATHAM
INVESTMENTS

Research Report

ADVISORY SERVICES

Report Date

1st DECEMBER 2014

Analyst

Ravi Lockyer MSc Llb

Collins Sarri Statham
Investments Ltd

People's Bank of China (PBOC) begins its rate-cut cycle

The surprise 0.4% cut by the PBOC on 23rd November 2014 could be the start of a series of downward interest rate adjustments aimed at providing monetary stimulus for the world's second largest economy.

For the last six years, the world's central banks have responded to the 2008 crisis by moving benchmark interest rates to levels that are near zero in many cases. Various measures have been employed, quantitative easing and forward guidance to hold them there. China's People's Bank of China has left interest rates high at levels commensurate with annual GDP growth of between 7%-8%.

The PBOC cut the one year benchmark lending rate by 0.4% to 5.6% and cut its one year deposit rate by 0.25% to 2.75%. The move included a 0.25% cut to personal mortgages but allowed banks to price deposits at up to 20% above their benchmarks (up from 10% previously).

It is odd that a country whose National Bureau of Statistics says grew at 7.4% for the first nine months of 2014 should *require* monetary stimulus. Central banks have more data on the economy than external commentators so this move suggests a wide information gap. Perhaps the PBOC is concerned about a broader slowdown and the deflationary impact of lower oil prices. The real rate of China's GDP growth is quite possibly lower than the 7% target.

The 0.4% interest rate cut is the start of an easing cycle designed to mitigate a sharp GDP slowdown (that is possibly being disguised) and an attempt to signal the PBOC is sensitive and alert to downside risks and expects inflationary pressures to ease.

A timely rotation into China sensitive equities

Since 2009 investors have been cautious on China, this partly reflects a slowdown in its GDP growth rate. The Communist Party plans to shift the economy away from export/ infrastructure focus and onto consumers. The correlation between the Shanghai Composite Index and the MSCI All Country World Index is 0.1 – the lowest amongst major equity markets. This means that Shanghai stocks offer good diversification benefits.

China is opening its capital markets, the Shanghai-Hong Kong exchange link opened on 17th November 2014 allows a net Y23.5bn of daily cross border purchases. This is a significant step to allow HK based investors easier access to Shanghai stocks. The Connect programme also allows international investors access to the domestic Chinese market without the need to obtain a Qualified Foreign Institutional Investment (QFII) quota from the Chinese government.

Currency controls, weak corporate governance, and under reported problems in government sectors mean investing directly is a bit problematic. **Hence we are opting for UK companies exposed to the Chinese stimulus package.**

Collins Sarri Statham Investments Ltd. 6th Floor 5 Lloyds Avenue London EC3N 3AE

Telephone: +44 (0)20 7264 2360 Facsimile: +44 (0)20 7264 2361 www.css-investments.com Email: info@css-investments.com

Collins Sarri Statham Investments Ltd. is authorised and regulated by the Financial Conduct Authority (Registration No 483868).
Registered in England and Wales (Company No 6539190).

BHP Billiton (BLT) BUY

BHP Billiton is the world's largest listed diversified miner with significant interests in copper, coal, iron ore, oil & gas, alumina, manganese, nickel and potash.

During 2015 BHP Billiton plans to demerge its non-core operations into a new London listed entity which will encompass its manganese, silver, alumina, aluminium nickel and Illawara coal. BHP will distribute shares in the new company (expected to be worth c £8.4bn) to existing holders and retain its five pillars of iron ore, coal, petroleum, copper and potash. The demerger should make achieving productivity and efficiency gains easier.

At its Interim Management Statement (IMS) on 24th November, the board revised upwards its targeted annual productivity gains by \$500m to US\$4bn by end 2017. Alongside these savings, BHP is cutting capital spending by \$600m in 2015 and \$1.2bn in 2016. We view this move positively as it demonstrates BHP increased optimisation of development related activity which should free up increased cash for holders. The IMS also repeated that core BHP will not rebase its dividend post the non-core demerger, effectively producing a dividend gain for holders.

The recent decision by OPEC to leave oil production unchanged has led to broader commodity weakness, directly related to the slump in global crude oil prices. Lower crude oil will impact BHP petroleum operations which had \$14.8bn revenues (22% of total BHP revenues), Earnings Before Interest & Tax (EBIT) \$5.28bn (23% Financial Year (FY)14 BHP earnings) in the year to end June 2014.

We assume a worst case scenario is a 40% drop in FY2015 petroleum revenues or around \$2.1bn in terms of EBIT. Assuming the relationship between EBIT \$22.9bn to net earnings \$13.45bn holds in FY15 that would suggest an earnings hit of c.\$1.23bn or 23.2 cents per share. BHP earned \$2.52 per share in FY14 up from \$2.35 in FY13.

BHP lost 128p per share in November 2014 (£6.7bn in terms of valuation) taking the stock back to under 5 year lows. The downswing in our view goes a significant way to pricing in lower petroleum related profit issues and the soft commodity environment which is likely to prevail in the second half of BHP current financial year.

Company	BHP Billiton
Share Price (p)	1470
Target Price (p)	2000
52 Wk Hi/Low (p)	2096/1582
Shares O/S	5.3bn
Market Capitalisation	£78.2bn
Avg Daily Volume	8.84m
Dividend Yield	4.81%

Source; Fidessa plc

Key Catalysts

BHP has set demanding output targets for 2015, petroleum & copper 5% growth, iron ore 11% growth and met coal 4%. However soft commodity prices oil (-27%) iron ore (16.5%) if they persist are headwinds suggesting revenue drops in the 10%-15% range in some areas.

We are positive on the merits of the demerger. The interims, due 18th February should provide improved clarity on the demerger timetable and the financials / dividend payout of the demerged entity.

Key Risks to Price Target

- i) BHP Billiton profitability is sensitive to base metal prices, oil prices and other commodity related risks such as global metal and oil inventories.
- ii) BHP Billiton is in the midst of demerging its non-core businesses, this involves execution related risks.
- iii) Future profitability will be impacted by Chinese demand for base metals and BHP realising its targeted US\$4bn of annualised productivity gains.

Collins Sarri Statham Investments Ltd. 6th Floor 5 Lloyds Avenue London EC3N 3AE

Telephone: +44 (0)20 7264 2360 Facsimile: +44 (0)20 7264 2361 www.css-investments.com Email: info@css-investments.com

Collins Sarri Statham Investments Ltd. is authorised and regulated by the Financial Conduct Authority (Registration No 483868).
Registered in England and Wales (Company No 6539190).

JIMMY CHOO (CHOO) BUY

Jimmy Choo is a modern high end fashion brand focusing on glamorous shoes and a range of accessory items including sunglasses, eyewear, fragrance and leather accessories. The brand has a wide global recognition and is sold via a growing global distribution network (120 directly operated stores - DOS) alongside a high quality network of wholesale distributors. Jimmy Choo is in the midst of a China/ SE Asia expansion, following an IPO offer of 100.9m shares at 140p on 17th October 2014.

Company	J Choo
Share Price(p)	171
Target Price(p)	225
52 Wk Hi/Low (p)	173/140
Shares O/S	389.74m
Market	
Capitalisation	£666.45m
Avg Daily Volume	229k
Dividend Yield	0%

Source; Fidessa plc

Key Catalysts

We are awaiting updates on the expansion of DOS in greater China, and Russia and potential franchise buybacks in the Middle East, South Korea, Singapore and Malaysia.

Post IPO (140p at the lowest point of the range) we are expecting an update shortly after Christmas. The company has advised it is now organising its corporate calendar.

Key Risks to Price Target

- i) Jimmy Choo success depends on its ability to anticipate and respond promptly to consumer demands, there are significant inventory related risks.
- ii) Jimmy Choo faces competitive pressures in the luxury shoe market. Its main competition comprises very large luxury brand companies.
- iii) Jimmy Choo is exposed to changes in foreign exchange rates, its reporting currency is sterling but it has a high proportion of sales in overseas territories.

FIDELITY CHINA SPECIAL SITUATIONS PLC (FCSS) BUY

Fidelity China Special Situations (a UK listed investment trust) invests in a manager selected portfolio of Chinese equities. Its recent outperformance (total return 14.3% to end September) against an index return of 10.1% was attributed to large gains in Alibaba and BitAuto. Fidelity China does use modest gearing of 20.6% to augment exposure to mainly e-commerce and securities companies. The manager has increased exposure to insurance companies due to low insurance penetration in China and selective property companies which he thinks are undervalued.

Company	Fidelity China Special Sit
Share Price(p)	129
Target Price(p)	160
52 Wk Hi/Low (p)	129/ 97
Shares O/S	571.2m
Market	
Capitalisation	£736m
Avg Daily Volume	1.52m
Dividend Yield	0.89%

Source; Fidessa plc

Key Catalysts

The IPO of Alibaba at over \$220bn was more than 4x the FCSS pre-IPO investment at \$48bn 24 months ago. We await developments on further reductions in the FCSS Alibaba stake.

The board remain confident that property risks have been exaggerated and that current valuations for property companies are too low. The expectation is for an earnings increase of 20% in the coming year which should drive portfolio gains over FY15.

Key Risks to Price Target

- i) Current 12.3% discount to net assets can vary significantly.
- ii) Sensitive to key staff and confidence in the manager's strategy for the investment fund.
- iii) Movements in foreign exchange rates specifically between sterling and the Yuan will impact the net assets and performance of the fund.

Collins Sarri Statham Investments Ltd. 6th Floor 5 Lloyds Avenue London EC3N 3AE

Telephone: +44 (0)20 7264 2360 Facsimile: +44 (0)20 7264 2361 www.css-investments.com Email: info@css-investments.com

Collins Sarri Statham Investments Ltd. is authorised and regulated by the Financial Conduct Authority (Registration No 483868).
Registered in England and Wales (Company No 6539190).

Collins Sarri Statham Investments Ltd - Analyst Rating Definitions:

BUY: A “buy” rating is applied to companies with established businesses that are profitable and where there is further profit growth expected. A “buy” recommendation means the analyst expects the share to reach the share price target on the note.

HOLD: The company’s valuation appears to reflect investor expectations in the short-term. Alternatively the company is awaiting key developments that will impact on the share price. Investors are advised to await the resolution of these key developments.

SELL: The company’s valuation appears too high having regard to material uncertainties, declining profit prospects or has sizeable funding requirements. A sell recommendation may also be applied where the board have failed in key objectives or appear to be frequently changing strategy. A sell recommendation means the analyst expects the share to fall to the price target on the note.

NEUTRAL (Not Rated): The analyst does not maintain a view in either direction.

Key to Material Interests:

Please be aware that the following disclosures of Material Interests are relevant to this research note:

BHP Billiton Relevant disclosures: < 2>

- 1.** The analyst has a personal holding in the securities issued by the company or of derivatives linked to the price of the company’s securities.
- 2.** Collins Sarri Statham Investments Ltd has clients who hold either shares or CFD positions in this security.

ANALYST CERTIFICATION:

The report’s author certifies that this research report accurately states his personal views about the subject securities, which is reflected in the ratings as well as the substance of the reports.

RECOMMENDATIONS:

Collins Sarri Statham Investments Ltd (CSS) does not in any of its publications take into account any particular recipient's investment objectives, financial situation, and specific needs and demands. Therefore, all CSS publications are, unless otherwise specifically stated, intended for informational and/or marketing purposes only. **CSS shall not be responsible for any loss arising from any investment based on a perceived recommendation.**

No publication (including recommendations) shall be construed as a representation or warranty that the recipient will profit, nor avoid sustaining losses, from trading in accordance with a trading strategy set forth in a publication.

This research is non-independent and is classified as a Marketing Communication under FCA rules detailed in their Conduct of Business Rulebook (COBS). As such it has not been prepared in accordance with legal requirements designed to promote independence of investment research and it is not subject to the prohibition of dealing ahead of the dissemination of investment research outlined in COBS 12.2.5.

RISK WARNING:

Trading in the products and services offered by Collins Sarri Statham Investments Ltd (CSS) may, result in losses as well as profits as the value of investments may go down as well as up. You may not get back the full amount you have invested. Any reference to past performance should not be viewed as an indication of any future performance. Investments held in overseas markets are subject to the effects of changes in exchange rates which will impact on the value of the underlying investment. Leveraged products such as Contracts for Difference (CFDs), derivatives, commodities & Foreign Exchange (FX), carry a higher risk to your capital. They can lose their value rapidly and you may lose substantially more than your initial investment.

Investment trusts are specialised investments and may not be appropriate for all investors. Investment Companies including investment trusts use or may have the ability to use gearing as an investment strategy or may invest in companies that use gearing. Movements in the price of these securities may be more volatile than the movement in the price of the underlying investment.

SPECULATIVE TRADING IS NOT SUITABLE FOR ALL INVESTORS.

The information contained herein is based on materials and sources that we believe to be reliable however we make no representation or warranty, either express or implied, in relation to the accuracy, completeness or reliability of the information contained herein. Please note that the figures shown may, in some instances, be rounded to the nearest penny. Prices can move sharply from those quoted in this document. Current prices can be verified by calling one of our brokers. CSS is under no obligation to update the information contained herein. Neither CSS, nor its affiliates, nor its employees shall have any liability whatsoever for any indirect or consequential loss or damage arising from the use of this document.

Collins Sarri Statham Investments Ltd. 6th Floor 5 Lloyds Avenue London EC3N 3AE

Telephone: +44 (0)20 7264 2360 Facsimile: +44 (0)20 7264 2361 www.css-investments.com Email: info@css-investments.com

Collins Sarri Statham Investments Ltd. is authorised and regulated by the Financial Conduct Authority (Registration No 483868).
Registered in England and Wales (Company No 6539190).