

Danger analysts get too close

Anthony Klan
Markets

SHARE price targets are of almost no use to investors because the analysts who set them are highly compromised by the companies they cover, according a leading fund manager.

Challenger Financial Services Group equities head Peter Greentree said analysts were reluctant to report sell share recommendations for fear of access to briefings and internal company documents being revoked.

"We don't pay any attention to broker recommendations," Mr Greentree said.

"Analysts want to protect their relationships with companies, and obviously companies react badly if analysts produce sell recommendations. So the recommendations themselves carry very little weight."

The actions of financial analysts came under scrutiny after Citigroup analyst Sanjay Magotra last week downgraded the target share price of rail and port company Asciano from \$6.08 to just 82c.

The report caused Asciano shares to lose \$720 million of their value before the company was suspended from trading. After reassuring statements from management and some other analysts, the company clawed back its losses.

Before Mr Magotra's sell recommendation he had issued 20 reports recommending buying, which proposed numerous target prices for the stock — from \$13.79 in July last year to \$6.08 in September.

Other analyst ratings for Asciano range between \$3.70, set by UBS, and a target of \$5.45, set by Morgan Stanley. Mr Magotra and Citigroup have declined to comment.

BPM Financial Modelling founder Michael Hutchens said a lack of transparency among research houses — and poor reporting by companies — was responsible for huge differences in performance expectations posted by analysts covering the same companies.

"We have the top investment banks in the country coming out with share price recommendations that vary so dramatically you would be better off betting on the Melbourne Cup," Mr Hutchens said.

"Investment banks and researchers aren't required to provide underlying clear justifications of how they come up with their valuations, and all investors see is the tip of the iceberg."

Challenger's Mr Greentree said the overwhelming proportion of buy recommendations to sell recommendations on Australia's largest companies was further proof analysts were compromised by companies they covered.

"If you look at the skew of recommendations I'd say less than 20 per cent of companies would have sell recommendations — probably even less than 10 per cent," Mr Greentree said.

Challenger paid little attention to targets outlined in brokers' reports, he said, but "company insights" and "industry contacts" provided by analysts were of use to the fund manager.

The issue of company insights was highlighted by Corporate Law Minister Nick Sherry who on Wednesday announced he

Danger in analysts getting too close

From Page 31

would investigate the potential disclosure of market-sensitive information at closed analysts' briefings.

The inquiry, to be conducted by the Corporations and Markets Advisory Committee, would also examine margin lending to company directors, trading by directors in blackout periods — before the general release of market sensitive information — and the practice of spreading false rumours to influence share prices.

Australian Shareholders Association chief executive Stuart Wilson said the separation between analysts and other arms in the same institutions was regularly called into question.

A recent case involved BrisConnections, a company established to construct an airport link in Brisbane, which went to the market to raise \$1.23 billion at \$1 a share, he said.

Under the offer, for each share, investors outlaid \$1 initially and contracted to provide an additional \$1 in April 2009 and again in January 2010.

On listing at \$1 on July 30, BrisConnections shares immediately slumped to 41c.

Shares in the company have continued to slide rapidly and have languished for weeks at 0.1c — the lowest value at which a share can trade on the Australian Securities Exchange.

The underwriters for BrisCon-



Surprise call: Sanjay Magotra

nections were Credit Suisse, JPMorgan, Macquarie Capital Advisers and Deutsche.

The three analysts covering the company come from Credit Suisse, JPMorgan and Macquarie.

Between September 5 and 11 — while BrisConnections fell from 13c to 5c — those analysts posted target prices on the stock of \$1.91, \$2.10 and 93c.

“People have bought millions of these things and they can't sell them,” Mr Wilson said. “It's causing a lot of angst and a lot of

people are calling me up very upset, and many of them have been pointing to Macquarie Bank as being the ones who promoted it in the first place.”

Mr Wilson said those target prices reflected future instalments to be invested in BrisConnections, but given there were “no buyers” for the stock currently those target prices were “very, very bullish”.

Macquarie declined to comment specifically on BrisConnections but said the group followed strict procedures to preserve the independence of analysts.

“There are very strict standards, procedures and processes in place and strict Chinese walls in place to ensure that analysts are independent of other business activities,” a spokeswoman said.

A JPMorgan spokesman said its research arm was completely independent of its broking arm.

“The research function is absolutely impartial and independent of the broking function,” he said.

Credit Suisse was unavailable for comment.

BPM Financial Modelling's Mr Hutchens said poor disclosure from companies heavily contributed to the wide range of target prices often seen for shares in the same company: “In cases where analysts are forced to analyse companies with just publicly available information (such as annual reports) they are forced to do the best they can.”

A lack of disclosure from ana-

lysts also caused discrepancies. “Analysts won't provide their models to investors. If you ask an investment bank for a model behind a transaction you will never get it,” Mr Hutchens said.

Analysts typically did not reveal to investors the models used to calculate share price targets for fear of legal action if those models contained incorrect information or assumptions, he said.

BPM Financial Modelling provides internal financial analysis and modelling for listed companies using internal company information.

Corporate watchdog the Australian Securities and Investments Commission said there were no laws specifically on stock recommendations provided by analysts. However, laws concerning “general” financial advice prevented any financial services representative engaging in “misleading or deceptive conduct”.

Those laws were very rarely invoked, with the late entrepreneur Rene Rivkin the last person to be reprimanded under that legislation, in 2000.

Between April 1998 and June 1999 several editions of the *Rivkin Report* published recommendations to buy or hold securities in FAI Insurances, Infratil Australia and three other companies. The report did not tell subscribers that during the same period Mr Rivkin placed orders to sell, or sold, shares in those companies.