

Equity | Australia | Publishing
26 August 2008

FXJ to reduce workforce by 5%



Merrill Lynch

Maintain Buy with \$3.75/sh PO

Our main thesis on FXJ for some time has been that the company is very well positioned to weather cyclical and structural threats given its attractive business mix and potential to reduce its cost base. The FY08 result confirmed our belief that diversification is finally paying off (metro EBITDA down -9% vs group EBITDA up +7%) and FXJ's subsequent cost reduction announcement highlights the potential buffer the company has to cushion the impact of cyclically slowing revenues into FY09.

Cost base to reduce by over \$60m in FY09

FXJ is on track to reduce its cost base by \$23m in FY09 from synergies (\$19m for Rural Press and \$4m for SBC Radio). On top of this, its Australian newsprint costs are set to decline c.5% in FY09 (NZ flat), equating to a c.\$15m saving. Finally, today's announcement (workforce cut by 5% or 550 people) will see a further \$25m of costs extracted in FY09 (and \$25m in FY10). The combination of these 3 drivers should see group costs cut by around \$63m in FY09.

Focus is on New Zealand and Australian metros

The focus of headcount reduction will be on NZ publishing (160 people), head office/support (90) and Australian publishing and printing (300). Note we understand there will be little impact to the regional or specialist publications, with the bulk of the Australian restructuring focused on the metros and printing divisions. FXJ will take a \$50m charge in FY09 for redundancies and related restructuring costs, with the bulk of this in 1H09. We have taken this below the line.

ML cost forecasts unchanged

Given we had already expected substantial cost savings in FY09, our forecasts are largely unchanged.

Estimates (Jun)

(A\$)	2007A	2008A	2009E	2010E	2011E
Net Profit b/f Abnormals	251.0	378.1	393.3	442.8	499.3
EPS	0.232	0.252	0.258	0.286	0.318
EPS Change (YoY)	-5.4%	8.5%	2.6%	11.0%	11.1%
Dividend / Share	0.210	0.200	0.210	0.230	0.250
Free Cash Flow / Share	0.252	0.202	0.260	0.289	0.319

Valuation (Jun)

	2007A	2008A	2009E	2010E	2011E
P/E	12.8x	11.8x	11.5x	10.4x	9.4x
Dividend Yield	7.0%	6.7%	7.0%	7.7%	8.4%
EV / EBITDA*	9.8x	8.8x	8.4x	7.8x	7.2x
Free Cash Flow Yield*	6.1%	6.7%	8.8%	9.9%	0%

* For full definitions of *iQmethod*SM measures, see page 9.

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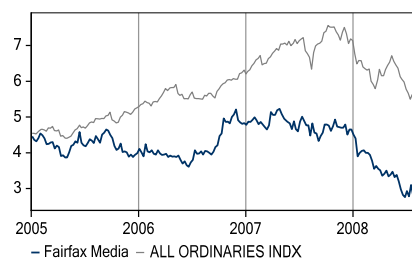
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Stock Data

Price	A\$2.98
Price Objective	A\$3.75
Date Established	21-Aug-2008
Investment Opinion	B-1-8
Volatility Risk	MEDIUM
52-Week Range	A\$2.57-A\$4.99
Mrkt Val / Shares Out (mn)	US\$3,906 / 1,513.5
Average Daily Volume	9,292,593
ML Symbol / Exchange	FFXL / ASX
Bloomberg / Reuters	FXJ AU / FXJ.AX
ROE (2009E)	8.2%
Net Dbt to Eqty (Jun-2008A)	48.7%
Est. 5-Yr EPS / DPS Growth	8.1% / 7.7%
Free Float	100%



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iQprofileSM Fairfax Media Ltd.

Key Income Statement Data (Jun)	2007A	2008A	2009E	2010E	2011E
(A\$ Millions)					
Sales	2,121	2,918	2,996	3,102	3,215
Operating Expenses	(1,549)	(2,087)	(2,128)	(2,180)	(2,221)
EBITDA	571	831	868	922	994
Depreciation & Amortization	(94)	(109)	(113)	(114)	(116)
EBIT	477	722	755	808	878
Net Interest & Other income	(111)	(187)	(195)	(177)	(165)
Associates	3	0	0	0	0
Pretax Income	366	535	559	631	713
Tax (expense) / Benefit	(97)	(139)	(148)	(170)	(196)
Net Profit b/f Abnormals	251	378	393	443	499
Non-Recurring Items	(6)	(8)	(35)	0	0
Net Income (Reported)	262	387	375	460	516
Avg F Diluted Shares Outstanding	1,082	1,503	1,524	1,546	1,569

Key Cash Flow Statement Data

EBITDA	571	831	868	922	994
Change in Working Capital	(6)	(46)	(18)	(19)	(20)
Deferred Taxation Charge	8	3	15	0	0
Other Adjustments, Net	0	(42)	0	0	0
Cash Flow from Operations	362	420	521	555	613
Capital Expenditure	(89)	(115)	(125)	(109)	(113)
(Acquisition) / Disposal of Investments	(558)	(588)	48	0	0
Other Cash Inflow / (Outflow)	(1)	0	0	0	0
Cash Flow from Investing	(584)	(699)	(77)	(109)	(113)
Shares Issue / (Repurchase)	0	92	0	0	0
Cost of Dividends Paid	(176)	(269)	(273)	(308)	(338)
Cash Flow from Financing	533	11	(308)	(308)	(338)
Free Cash Flow	273	304	396	447	NA
Net Debt	1,981	2,418	2,282	2,143	NA
Change in Net Debt	526	437	(136)	(139)	0

Key Balance Sheet Data

Property, Plant & Equipment	860	875	946	963	982
Other Non-Current Assets	149	206	158	158	158
Trade Receivables	409	499	524	551	579
Cash & Equivalents	366	94	94	94	94
Other Current Assets	1	17	17	17	17
Total Assets	8,001	8,293	8,322	8,345	8,373
Long-Term Debt	2,335	2,496	2,360	2,221	2,058
Other Non-Current Liabilities	93	125	125	125	125
Short-Term Debt	12	16	16	16	16
Other Current Liabilities	179	166	183	183	183
Total Liabilities	3,040	3,328	3,218	3,089	2,937
Total Equity	4,961	4,965	5,103	5,256	5,436
Total Equity & Liabilities	8,001	8,293	8,322	8,345	8,373

iQmethodSM - Bus Performance*

Return on Capital Employed	6.3%	7.2%	7.2%	7.6%	NA
Return on Equity	7.6%	8.0%	8.2%	9.0%	9.8%
Operating Margin	22.5%	24.7%	25.2%	26.1%	NA
EBITDA Margin	26.9%	28.5%	29.0%	29.7%	30.9%

iQmethodSM - Quality of Earnings*

Cash Realization Ratio	1.4x	1.1x	1.3x	1.3x	NA
Asset Replacement Ratio	0.9x	1.1x	1.1x	1.0x	NA
Tax Rate (Reported)	26.6%	26.0%	26.5%	27.0%	27.5%
Net Debt-to-Equity Ratio	39.9%	48.7%	44.7%	40.8%	36.4%
Interest Cover	4.1x	3.4x	3.8x	4.4x	5.2x

Key Metrics

Franking	100%	100%	100%	100%	100%
EBIT Growth %	12%	51%	5%	7%	9%
EBITDA GROWTH %	13%	46%	4%	6%	8%

* For full definitions of iQmethodSM measures, see page 9.

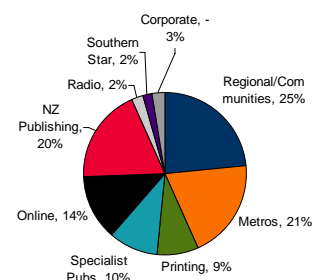
Company Description

Fairfax operates Australia's two largest broadsheet dailies in Sydney and Melbourne (The SMH and The Age), the only national financial daily (The AFR) and Sunday newspapers in Sydney and Melbourne. It also has significant NZ assets (7 dailies, 2 Sundays, 61 communities), generating 30% of group EBIT. Fairfax now also has the greatest online exposure of any traditional media company in Australia, following the NZ\$700mn Trade Me acquisition.

Investment Thesis

FXJ should continue to trade at a premium relative to its US/UK peers given its (1) attractive portfolio of assets, with close to 20pct of earnings derived from online in FY10 and 35pct from high-margin rural/regional and specialist publications, and less reliance on metros, (2) impressive circulation record, with circulation flat to up in the past two years, and (3) much less competitive markets, with most regional/rural markets having only one newspaper delivered to them daily.

Chart 1: FY08 EBITDA contribution



Source: Fairfax Media

Stock Data

Price to Book Value 0.9x

FXJ announces 5% cut to workforce

As we have been anticipating for some time, FXJ has announced a wide-ranging restructuring, with a reduction of 550 people, or 5% of its workforce.

The total program is expected to achieve annualised cost savings of \$50m, with \$25m realised in FY09 and \$25m in FY10. The focus will be on corporate/support (90 people), Australian publishing and printing (300) and NZ publishing (160).

FXJ will take a \$50m charge in FY09 for redundancies and related restructuring costs, most of which will fall in 1H09.

Table 1: Estimated FY09 cost growth (in A\$)

Division	YoY growth
Australian Regional/Communities	2%
Australian Metros	-2%
Australian Printing	-12%
Specialist Publications	3%
Total Aust. Publishing & Printing	0%
NZ Publishing ¹	-5%
Online	9%
Radio	-1%
Southern Star	-10%
Total	2%

1. NZ costs are expected to decline by -1% in FY09 in local currency.
Source: Merrill Lynch estimates

FY09 cost base to reduce by more than \$60m

Looking into FY09, FXJ's cost base will benefit from:

- **Headcount reduction** – \$25m of costs extracted over FY09 (most in 2H, with a further \$25m in FY10), driven by a 5% (550) reduction in the company's workforce,
- **Synergies** – We estimate a total of \$23m synergies will fall in FY09 (\$19m for Rural Press and \$4m for radio), and
- **Newsprint** – Australian newsprint costs are set to decline c.5% in FY09 (New Zealand flat in NZ\$), which should save FXJ c.\$15m.

This, combined with FXJ's diverse business mix (the benefits of which were evident in its FY08 result), means FXJ is very well placed to weather the impending cyclical downturn.

We forecast FXJ group costs to lift by 2% in FY09, with the Australian metros (-2%) and New Zealand (-1% in NZ\$ and -5% in A\$) the key beneficiaries of the company's headcount, newsprint and synergies cost reduction.

New Zealand

The NZ workforce will be reduced by 160 from roughly 2,500 today (6.4%). Whilst this represents close to 30% of the headcount reductions, we understand NZ will represent around 20% of the actual dollar savings (ie \$5m in FY09 and \$5m in FY10). This, combined with newsprint savings, should see the NZ cost base down slightly in FY09.

Our FY09 forecasts assume flat personnel and newsprint costs, with other costs declining by -2%. This results in a -0.8% reduction for total NZ operating costs in NZ\$ (+0.4% in 1H and -2.1% in 2H09).

A tale of two halves

We expect FY09 to be a tale of two halves for FXJ, and for NZ in particular.

For the top line, we expect 1H09 to be very soft (revenue down -4%), however we expect a modest recovery in 2H FY09 as FXJ cycles easier comps and the economy and ad market benefit from the stimulation of several interest rate cuts.

With the benefits of the cost reduction program also more heavily weighted to 2H FY09, this should result in a steep EBITDA decline of -14% in 1H09 before improving to a +11% gain in 2H09.

Note however that if the currency stays where it is (A\$/NZ\$ at 1.22), then the impact to A\$ will be more severe, with 1H09 EBITDA down -18% in A\$, 2H09 up +7% and FY09 down -6%.

Table 2: New Zealand earnings

June Year NZ\$	2007A	1H08A	2H08A	2008A	1H09E	2H09E	2009E	2010E
Revenue								
Total Revenue	578.4	301.8	291.1	592.8	289.7	297.2	586.9	604.5
Growth	-0.8%	3.8%	1.1%	2.5%	-4.0%	2.1%	-1.0%	3.0%
Total Expenses								
Total Expenses	392.5	206.9	194.4	401.2	207.7	190.3	398.0	400.4
Growth	1.5%	3.3%	1.1%	2.2%	0.4%	-2.1%	-0.8%	0.6%
EBITDA								
EBITDA	185.9	94.9	96.7	191.6	82.0	106.9	188.9	204.1
Growth	-5.2%	5.0%	1.2%	3.1%	-13.6%	10.6%	-1.4%	8.0%
EBITDA Margin								
EBITDA Margin	32.1%	31.4%	33.2%	32.3%	28.3%	36.0%	32.2%	33.8%
D&A								
D&A	12.5	7.0	7.0	14.0	7.1	8.0	15.1	15.2
EBIT								
EBIT	173.4	87.9	89.7	177.6	74.9	98.9	173.8	188.9
Growth	-6.5%	3.8%	1.2%	2.4%	-14.8%	10.2%	-2.2%	8.7%
A\$1 Buys NZ\$								
A\$1 Buys NZ\$	1.15	1.16	1.18	1.17	1.22	1.22	1.22	1.22
June Year A\$								
Revenue	504.7	261.3	247.4	508.7	237.4	243.6	481.0	495.5
Growth	-3.0%	5.1%	-3.4%	0.8%	-9.1%	-1.6%	-5.4%	3.0%
Expenses								
Expenses	342.5	179.1	165.5	344.6	170.3	156.0	326.2	328.2
Growth	-0.8%	4.4%	-3.2%	0.6%	-4.9%	-5.8%	-5.3%	0.6%
EBITDA								
EBITDA	162.2	82.2	81.9	164.1	67.2	87.6	154.8	167.3
Growth	-7.4%	6.3%	-3.5%	1.2%	-18.2%	7.0%	-5.7%	8.0%
D&A								
D&A	10.9	6.0	5.9	12.0	5.8	6.6	12.4	12.5
EBIT								
EBIT	151.3	76.1	76.3	152.4	61.4	81.0	142.4	154.8
Growth	-8.6%	5.0%	-3.2%	0.7%	-19.4%	6.2%	-6.6%	8.7%

Source: Fairfax Media, Merrill Lynch estimates

Australian publishing and printing

Whilst reported costs for the Australian publishing and printing (AP&P) division lifted by 30% in FY08, we understand underlying cost growth (ex acquisitions) was c.1%.

Looking into FY09 we forecast flat costs for the division.

Table 3: Australian Publishing & Printing

Year end June	2007A	2008A	2009E	2010E
Revenue				
Revenue	1425.5	1972.2	1974.1	2010.0
Change		38.4%	0.1%	1.8%
Operating costs				
Operating costs	1100.5	1433.5	1433.7	1461.2
Change		30.3%	0.0%	1.9%
EBITDA				
EBITDA	325.0	538.7	540.3	548.7
Change		65.8%	0.3%	1.6%
EBITDA Margin				
EBITDA Margin	22.8%	27.3%	27.4%	27.3%

Source: Fairfax Media, Merrill Lynch estimates

Cost assumptions for each sub-division are as follows:

Metros (estimate 44% of total FY09 AP&P costs) declining by -2%

With the bulk of the estimated 300 people taken out of Australian publishing coming from Melbourne and Sydney, we believe this division will see the greatest benefit. Note metro costs reduced by -0.9% in FY08, therefore we think -2% should be achievable given the magnitude of the current restructuring program.

Regional & Communities (37% of total) lifting by 2%

Underlying costs rose by 2.3% in FY08 and we forecast a further 2% increase in FY09. We do not expect any significant cuts to be made to the regionals, given these have already been run very efficiently by Rural Press.

Australian Printing (3% of total)

We forecast a further -12% decline in operating costs in FY09 after a -10% decline in FY08. FXJ indicated that there are no printing presses expected to be closed as part of this current restructure, however we see the potential for this to happen further down the track.

Specialist Publications (17% of total)

We forecast a further 3% lift in operating costs in FY09 after 3% underlying growth in FY08. We would not expect any significant cuts to be made at the agricultural publications, and any reductions at the *AFR* to be minimal.

Valuation

FY09 SOTP Valuation

Our \$3.66/sh SOTP valuation assumes a blended FY09 EBITDA multiple of 9x. Within this we assume 8x for Australian publishing (6.5x for the metros), 9.0x for NZ publishing and 13.0x for the combined online assets.

Table 4: Fairfax FY09 SOTP valuation

Year end 30th June	EBITDA		FY09E Multiple	Valuation (A\$m)	Valuation (A\$/share)
	FY08A	FY09E			
Australian Publishing					
Metro Newspapers (AGE, SMH)	206	213	6.5x	1,386	0.92
Regional/Community Newspapers	174	166	10.0x	1,661	1.10
Printing	73	76	8.0x	606	0.40
Total Australian Publishing EBITDA	453	455	8.0x	3,653	2.41
Specialist Publications	86	85	10.0x	853	0.56
New Zealand Publishing (A\$m)	164	155	9.0x	1,393	0.92
Online (Fairfax Digital and Trade Me)	114	146	13.0x	1,894	1.25
Radio (metro & regional)	20	33	9.5x	313	0.21
Southern Star	17	15	7.0x	105	0.07
Endemol (50% stake)	3	7	7.0x	47	0.03
Corporate costs	-22	-21	8.0x	-169	-0.11
Total Enterprise Value	857	896	9.2x	8,258	5.46
Less Net Debt (incl \$300m SPSs)				2,718	1.80
Derived Equity Value				5,540	3.66

Shares on issue (millions)

1514

Source: Merrill Lynch estimates

DCF valuation

The main drivers of our \$3.87/sh DCF valuation include:

- 10-year revenue CAGR from FY08-FY17 of 2.1%, with the Australian metro revenue CAGR of -1.3%.
- 10-year EBITDA CAGR of 1.8%,
- EBITDA margin declines from 29% in FY08 to 27% in FY18, with the Australian publishing margin declining from 27% to 20%.

Our DCF also assumes a WACC of 9.6% and terminal nominal cash flow growth of 3.0%.

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Table 5: Fairfax summary financials

FINANCIAL PERFORMANCE					FINANCIAL POSITION				
	FY07A	FY08A	FY09E	FY10E		FY07A	FY08A	FY09E	FY10E
Sales revenue	2,117.6	2,917.7	2,995.8	3,101.9	Cash	366.3	93.9	93.9	93.9
<i>growth</i>	11.3%	37.8%	2.7%	3.5%	Receivables	408.9	499.1	524.4	550.9
Associates contribution	3.0	0.0	0.0	0.0	Inventories	48.5	44.8	47.1	49.4
EBITDA	571.3	831.2	867.7	922.0	Other	0.5	17.4	17.4	17.4
<i>growth</i>	13.1%	45.5%	4.4%	6.3%	Current Assets	824.3	655.1	682.7	711.6
EBITDA Margin	27.0%	28.5%	29.0%	29.7%	Receivables	1.3	3.7	3.7	3.7
Depreciation & Amortisation	94.0	109.1	113.0	113.7	Fixed assets	860.0	875.2	946.2	963.1
EBIT	477.2	722.1	754.7	808.3	Investments	36.0	63.9	63.9	63.9
<i>growth</i>	12.2%	51.3%	4.5%	7.1%	Intangibles	6,131.0	6,492.6	6,470.6	6,448.6
Net interest	-111.2	-186.9	-195.4	-177.4	Other	147.9	202.5	154.5	154.5
Pre-tax profit	366.0	535.2	559.3	630.9	Non-Current Assets	7,176.3	7,638.0	7,639.0	7,633.9
Tax expense	-97.3	-139.3	-148.2	-170.3	Total Assets	8,000.5	8,293.1	8,321.7	8,345.5
Net profit	268.7	395.9	411.1	460.6	Debt due within one year	12.2	15.8	15.8	15.8
Minority interests	1.1	0.6	0.6	0.6	Payables	289.5	330.0	339.8	349.8
Underlying NPAT	267.6	395.3	410.5	460.0	Provisions/Other	177.4	165.3	182.3	182.3
SPS dividends	16.6	17.2	17.2	17.2	Current Liabilities	479.2	511.2	537.9	548.0
Underlying NPAT post SPS	251.0	378.1	393.3	442.8	Long-term debt	2,335.5	2,496.1	2,359.8	2,220.7
<i>growth</i>	9.9%	50.6%	4.0%	12.6%	Provisions/Other	223.5	319.5	319.5	319.5
EPS pre abnormals	23.2	25.2	25.8	28.6	Non-Current Liabilities	2,559.0	2,815.6	2,679.3	2,540.1
<i>growth</i>	-5.4%	8.5%	2.6%	11.0%	Total Liabilities	3,038.2	3,326.8	3,217.2	3,088.1
Net abnormal items	-5.6	-8.4	-35.0	0.0	Net Assets	4,962.3	4,966.3	5,104.5	5,257.4
Reported NPAT	245.5	369.7	358.3	442.8	Share Capital	4,184.3	4,318.4	4,383.7	4,450.0
					Reserves	15.6	-186.1	-186.1	-186.1
					Retained Profits	748.2	822.0	894.2	980.3
					Shareholders' Equity	4,948.1	4,954.3	5,091.9	5,244.2
					Outside Equity Interests	12.9	11.0	11.6	12.2
					Total Shareholders' Equity	4,961.0	4,965.3	5,103.5	5,256.4
DIVISIONAL BREAKDOWN					BALANCE SHEET CAPACITY				
	FY07A	FY08A	FY09E	FY10E		FY07A	FY08A	FY09E	FY10E
Revenue					Net debt	1,981.4	2,418.1	2,281.8	2,142.6
Australian Regional/Communities	402.5	728.5	746.7	776.6	Net debt + SPS	2,281.4	2,718.1	2,581.8	2,442.6
Australian Metros	825.0	802.0	781.4	775.1	Net debt/Equity	39.9%	48.7%	44.7%	40.8%
Australian Printing	18.0	114.0	111.7	110.6	Net debt/Net debt+Equity	28.5%	32.8%	30.9%	29.0%
Specialist Publications	180.0	327.7	334.3	347.6	Interest cover	4.3x	3.9x	3.9x	4.6x
Online	187.4	246.9	290.7	338.4	Net debt/EBITDA	3.5x	2.9x	2.6x	2.3x
NZ Publishing	504.7	508.7	481.0	495.5					
Radio	0.0	81.4	119.0	123.1					
Southern Star	0.0	108.5	131.0	134.9					
EBITDA (pre associates)									
Australian Regional/Communities	84.0	205.5	213.3	227.1					
Australian Metros	191.0	174.1	166.1	153.7					
Australian Printing	11.5	73.1	75.7	74.3					
Specialist Publications	38.5	86.0	85.3	93.7					
Online	81.1	114.4	145.7	177.7					
NZ Publishing	162.2	164.1	154.8	167.3					
Radio	0.0	19.7	33.0	33.8					
Southern Star	0.0	16.6	15.1	16.1					
EBITDA Margin									
Australian Regional/Communities	20.9%	28.2%	28.6%	29.2%					
Australian Metros	23.2%	21.7%	21.3%	19.8%					
Australian Printing	63.9%	64.1%	67.8%	67.1%					
Specialist Publications	21.4%	26.2%	25.5%	27.0%					
Online	43.3%	46.3%	50.1%	52.5%					
NZ Publishing	32.1%	32.3%	32.2%	33.8%					
Radio	na	24.2%	27.7%	27.5%					
Southern Star	na	15.3%	11.5%	11.9%					
DIVIDENDS					CASHFLOWS				
	FY07A	FY08A	FY09E	FY10E		FY07A	FY08A	FY09E	FY10E
Dividends per share	21.0	20.0	21.0	23.0	EBITDA	571.3	831.2	867.7	922.0
Payout ratio	90.5%	79.5%	81.4%	80.3%	Change in working capital	-6.5	-46.0	-17.8	-18.9
Dividend Cover	1.1x	1.3x	1.2x	1.2x	Interest income and divs from associates	7.1	34.0	4.7	4.7
Yield	7.0%	6.7%	7.0%	7.7%	Interest paid on debt	-96.1	-209.5	-200.1	-182.1
					Income tax paid	-89.1	-136.2	-133.2	-170.3
					Other	-21.7	-53.9	0.0	0.0
					Operating cashflow	364.9	419.7	521.3	555.4
					Sale of fixed assets	64.6	5.2	0.0	0.0
					Net (purchase)/sale of investments	-558.3	-588.4	48.0	0.0
					Purchase of fixed assets	-88.7	-115.4	-125.0	-108.6
					Other	-1.1	0.0	0.0	0.0
					Investing cashflow	-583.6	-698.7	-77.0	-108.6
					Free cashflow (post prefs)	259.5	287.1	379.1	429.6
					Dividends paid - ords	-159.7	-251.6	-255.8	-290.5
					Dividends paid - prefs	-16.6	-17.2	-17.2	-17.2
					Shares issued	0.0	91.8	0.0	0.0
					Other/equity raised	709.1	188.0	-35.0	0.0
					Financing cashflow	532.7	11.0	-308.0	-307.7
					Net change in cash	314.0	-268.0	136.3	139.1
					<i>Free cashflow yield</i>	<i>8.0%</i>	<i>6.4%</i>	<i>8.3%</i>	<i>9.3%</i>
VALUATION					RETURN ANALYSIS				
	FY07A	FY08A	FY09E	FY10E		FY07A	FY08A	FY09E	FY10E
Price (\$/sh)	2.98				ROE	7.5%	8.0%	8.2%	8.9%
Shares (m)	1479.6				ROA	7.9%	8.9%	9.1%	9.7%
Market Capitalisation (\$m)	4,409.3				ROIC (after tax)	4.8%	6.9%	7.2%	7.6%
Net Debt + SPS (\$m)	2,718.1				ROIC - WACC	-4.8%	-2.7%	-2.4%	-2.0%
EV (\$m)	7,127.4								
EV/EBITDA (inc share of associate)		8.6x	8.2x	7.7x					
P/E Ratio		11.8x	11.5x	10.4x					

Source: Merrill Lynch estimates, FXJ

Price objective basis & risk

Fairfax Media (FFXLF)

Our \$3.75/share PO is derived from our fundamental valuation of \$3.76/share, which uses a blend of sum-of-the-parts (\$3.66/share) and DCF (\$3.87/share) methodologies.

Our SOTP valuation is based on a blended FY09 EV/EBITDA multiple of 9.2x. This assumes 8.0x for Australian publishing (6.5x for the metros, 10x for the regionals and communities, 8.0x for printing) and 9.0x for NZ publishing. For the online properties (Fairfax Digital and Trade Me), we assume 13.0x FY09E EBITDA.

Our one-year-out Fairfax DCF valuation assumes a WACC of 9.6pct and terminal nominal cash flow growth of 3pct.

Risks: A reversal of Fairfax's impressive circulation gains to declines, a greater-than-expected structural shift in Fairfax's classified print revenues to online, a deterioration of the Australian economy and ad market looking into 2H08 and 2009, and the NZ economy deteriorating sharper than expected.

Analyst Certification

I, Alice Bennett, hereby certify that the views expressed in this research report accurately reflect my personal views about the subject securities and issuers. I also certify that no part of my compensation was, is, or will be, directly or indirectly, related to the specific recommendations or view expressed in this research report.

Australia-Media Coverage Cluster

Investment rating	Company	ML ticker	Bloomberg symbol	Analyst
BUY				
	Austereo	AOGPF	AEO AU	Alice Bennett
	Fairfax Media	FFXLF	FXJ AU	Alice Bennett
	WAN	WANHF	WAN AU	Alice Bennett
NEUTRAL				
	Austar United	AUJCF	AUN AU	Dominique d'Avrincourt
	Seven Network	SVNWF	SEV AU	Alice Bennett
UNDERPERFORM				
	APN News & Media	AUPPF	APN AU	Alice Bennett
	CMH	CMJFF	CMJ AU	Alice Bennett
	Prime Media	YPRTF	PRT AU	Dominique d'Avrincourt
	Seek Ltd	SKLTF	SEK AU	Alice Bennett
	Ten Network	TNWHF	TEN AU	Alice Bennett

26 August 2008

iQmethodSM Measures Definitions

Business Performance	Numerator	Denominator
Return On Capital Employed	$\text{NOPAT} = (\text{EBIT} + \text{Interest Income}) * (1 - \text{Tax Rate}) + \text{Goodwill Amortization}$	Total Assets – Current Liabilities + ST Debt + Accumulated Goodwill
Return On Equity	Net Income	Shareholders' Equity
Operating Margin	Operating Profit	Sales
Earnings Growth	Expected 5-Year CAGR From Latest Actual	N/A
Free Cash Flow	Cash Flow From Operations – Total Capex	N/A
Quality of Earnings		
Cash Realization Ratio	Cash Flow From Operations	Net Income
Asset Replacement Ratio	Capex	Depreciation
Tax Rate	Tax Charge	Pre-Tax Income
Net Debt-To-Equity Ratio	Net Debt = Total Debt, Less Cash & Equivalents	Total Equity
Interest Cover	EBIT	Interest Expense
Valuation Toolkit		
Price / Earnings Ratio	Current Share Price	Diluted Earnings Per Share (Basis As Specified)
Price / Book Value	Current Share Price	Shareholders' Equity / Current Basic Shares
Dividend Yield	Annualised Declared Cash Dividend	Current Share Price
Free Cash Flow Yield	Cash Flow From Operations – Total Capex	Market Cap. = Current Share Price * Current Basic Shares
Enterprise Value / Sales	$\text{EV} = \text{Current Share Price} * \text{Current Shares} + \text{Minority Equity} + \text{Net Debt} + \text{Sales} + \text{Other LT Liabilities}$	
EV / EBITDA	Enterprise Value	Basic EBIT + Depreciation + Amortization

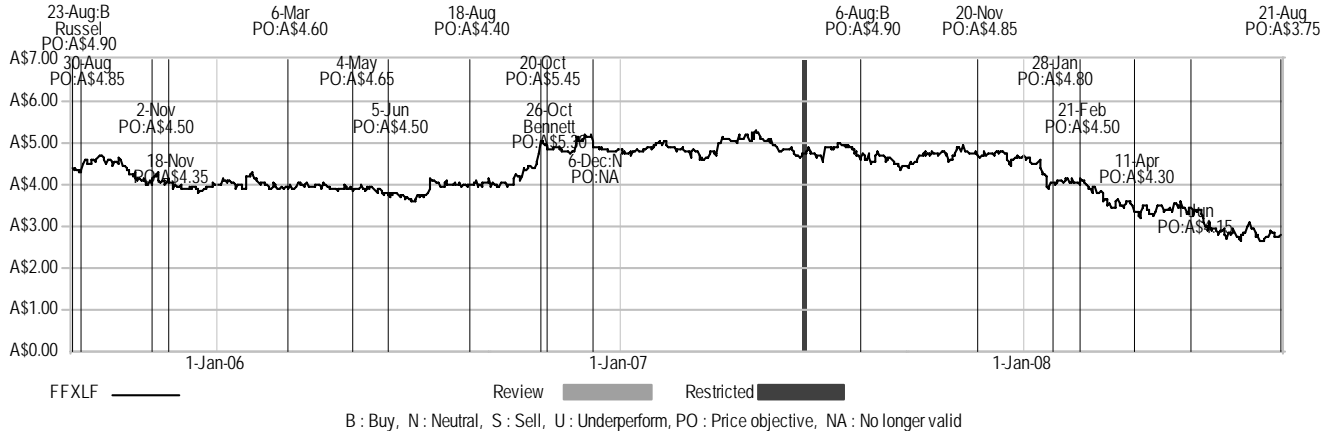
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Important Disclosures

FFXLF Price Chart



B : Buy, N : Neutral, S : Sell, U : Underperform, PO : Price objective, NA : No longer valid

Prior to May 31, 2008, the investment opinion system included Buy, Neutral and Sell. As of May 31, 2008, the investment opinion system includes Buy, Neutral and Underperform. Dark Grey shading indicates that a security is restricted with the opinion suspended. Light grey shading indicates that a security is under review with the opinion withdrawn. The current investment opinion key is contained at the end of the report. Chart is current as of July 31, 2008 or such later date as indicated.

Investment Rating Distribution: Media & Entertainment Group (as of 01 Jul 2008)

Coverage Universe	Count	Percent	Inv. Banking Relationships*	Count	Percent
Buy	53	45.30%	Buy	16	34.78%
Neutral	23	19.66%	Neutral	6	30.00%
Sell	41	35.04%	Sell	9	22.50%

Investment Rating Distribution: Global Group (as of 01 Jul 2008)

Coverage Universe	Count	Percent	Inv. Banking Relationships*	Count	Percent
Buy	1664	47.42%	Buy	441	29.46%
Neutral	803	22.88%	Neutral	224	31.46%
Sell	1042	29.70%	Sell	217	22.84%

* Companies in respect of which MLPF&S or an affiliate has received compensation for investment banking services within the past 12 months. For purposes of this distribution, a stock rated Underperform is included as a Sell.

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Investment rating	Total return expectation (within 12-month period of date of initial rating)	Ratings dispersion guidelines for coverage cluster*
Buy	≥ 10%	≤ 70%
Neutral	≥ 0%	≤ 30%
Underperform	N/A	≥ 20%

* Ratings dispersions may vary from time to time where Merrill Lynch Research believes it better reflects the investment prospects of stocks in a Coverage Cluster.

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