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Stories To Read From FNArena

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Cash Is Trumps At Evolution Mining

Gold miner Evolution Mining is cashing up and brokers laud the company for its production and debt-free potential.

-FY17 guidance appears relatively easy -Exploration program has potential upside surprise -Decision regarding Cowal stage H cut-back due

By Eva Brocklehurst

Evolution Mining ((EVN)) is cashing up. The gold miner is appealing to many brokers, given perceived upside potential in the near-term gold price. The company sustained record production in the December quarter. Operating cash flow was flat, as reduced cash costs offset a declining realised gold price.

The company has been able to re-pay \$70m in debt and net debt now stands at \$588m. Debt amortisation is ahead of schedule and there are no further repayments until October. The Cowal (NSW) mine had a record quarter under the company's ownership, producing 71,900 ounces at costs (AISC) of \$815/oz. The company has revised the mine plan and is now intent on mining more low-cost tonnage from the open pit.

The offtake from Ernest Henry (Queensland) started to contribute to Evolution Mining from November 1 and the company forecasts FY17 production of 55-60,000 ounces of gold at cost of \$100-150/oz. Deutsche Bank and Credit Suisse rate the stock a Buy and Outperform respectively, noting achieving FY17 guidance appears relatively easy.

Macroeconomic Risks Provide Appeal

While the market has been testing 10-year lows since the election of Donald Trump, Morgans believes this indicates excessive complacency had materialised, given risks that were inherent in the execution of the US President's intended economic reforms.

With this situation, and the abundance of separate macro economic risks in 2017, the broker recognises upside in the short term gold price and therefore the appeal of large, liquid gold producers such as Evolution Mining.

Morgans slightly reduces its valuation but maintains an Add rating, recognising risks to market volatility offer upside. Upside also exists in exploration, the release of positive mining studies at Cowal and Edna May (Western Australia) and commodity price appreciation.

Production beat Macquarie's forecasts, as output from Ernest Henry was over estimated. The broker make some changes to account for the treatment of the Ernest Henry gold revenue. The adjustments result in a -22% decrease to the broker's FY17 estimates but a 4-5% increase in long-term forecasts. There are number of key decisions on the horizon which the broker believes should provide a catalyst or two for the stock. The exploration program also has a potential for an upside surprise. Exploration results were particularly promising at the Cowal stage H cut-back. A board decision regarding the cut-back is expected in the current quarter. The company expects long-term gold recovery can be lifted by 5-88%.

Softer Second Half At Cowal Likely

Despite expectations FY17 guidance will be comfortably achieved, Canaccord Genuity notes a softer second half is expected at Cowal. While continuing to rate the stock amongst the premier gold miners on the ASX, the rally in the last six weeks means it is trading in line with the target. Hence the broker, not one of the eight stockbrokers monitored daily on the FNArena database, downgrades to Hold from Buy.

Canaccord Genuity highlights the company's growing reputation for cost control and also notes accounting treatment has made for a messy reconciliation in the short term for Ernest Henry, although this should normalise by FY18.

Evolution Mining expects to account for production/sales of gold/copper/silver from Ernest Henry thus: under the offtake from Glencore, copper and silver revenue will be recognised in the month of production, while gold revenue will be treated with an effective three-month delay. In contrast, costs will be reported as they are incurred.

Consensus Overweight

Consensus is overweight the stock for a reason, Morgan Stanley asserts. The broker sticks to its Overweight rating. Rapid debt reduction can be accelerated by the company reaching the high end of its FY17 guidance. While several mines contributed to the outcome in the December quarter, the flagship Cowal mine stood out, yet the broker acknowledges it will encounter lower grades in the third and fourth quarters.

Overall, FY17 guidance is for 800-860,000 ounces at cost of \$900-960/oz. Some mines will produce lower grades in the second half such as Cowal and Mungari (Western Australia) but there are others with positive drivers, the broker notes, such as Mt Carlton and Crakow in Queensland.

Morgan Stanley expects the company to be net cash by the middle of 2018. The broker also adjusts for a lower gold price forecast, which brings FY17 estimates for earnings per share down -21% while FY18 and FY19 estimates are adjusted up 3% and down -3% respectively. While the gold price might have been volatile of late, Australian dollar prices and cash flow are considered robust.

The stock remains a top relative exposure in the broker's opinion, given the free cash flow expected over the next three years. While Evolution Mining has significant leverage to ongoing cost reductions and conversion of resources to reserves, the downside risks include a slumping in commodity prices/strengthening of the Australian dollar, as well as mine life reductions and potential problems with the integration of new projects.

Citi continues to rate the stock as a Buy on the basis of valuation, after the value-adding acquisition at Ernest Henry, which provides leverage to copper. The broker divides the company's projects into three high-quality mines - Cowal, Mungari, Mt Carlton - and three of intermediate value - Crakow, Mt Rawdon (Qld), Edna May.

The stock shows seven Buy ratings on the FNArena database including UBS, which is yet to update on the production report. The consensus target is \$2.49, signalling 17.4% upside to the last share price. Targets range from \$2.30 (Credit Suisse) to \$2.70 (Morgan Stanley).

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Aconex Cuts Swathe Through Expectations

Brokers slashed forecasts as software service provider, Aconex ((ACX)) substantially downgraded revenue expectations for FY17, raising questions regarding the reliability of its growth outlook.

-Near-term outlook curbed but brokers retain ratings given the potential -Concerns over management's depth of engagement with clients -Existing business growth seen slowing to around 10%

By Eva Brocklehurst

Construction management software service provider, Aconex ((ACX)), has delivered a blow to investor hopes, substantially downgrading revenue expectations for FY17. The downgrade raises questions regarding the company's growth profile, predictability and momentum in the US and UK markets. Brokers slash price targets.

The company has cut its FY17 revenue forecast to \$160-165m and its operational earnings (EBITDA) forecast to \$15-18m. These estimates are down -8% and -30% respectively at the mid points compared with prior guidance. A slower conversion of new clients in the US and UK, amid the political uncertainty, has been cited as the main cause of the downgrade.

Impact To Linger

Morgan Stanley expects the impact to linger but retains its Overweight rating given the earnings power inherent in the business. Still, the issues are whether this is a one-off, whether the 20% long-term revenue growth rate is achievable and whether the company is still truly a global story.

Morgan Stanley opts for lower growth in FY17, but does not believe the company has downshifted from a 20% growth profile for the longer term. The question for Morgan Stanley is: how can a business with 72% of revenue booked in from July 1 miss expectations twice (first time at AGM)? The broker understands the cumulative nature of any miss in earnings forecasts but suspects volatility in user-based agreements has increased.

The pressure on US and UK growth is not a competitive issue, in the broker's opinion, and the company's service remains a clear product of choice for the world's largest projects. The broker takes heed of two clues to a possible rebound in sales: weighted contract length and bookings growth. The company has indicated a higher proportion of long-term contracts, which should boost contract length and, if new work is longer dated, it should imply the slowdown in bookings would be less pronounced.

Deutsche Bank is concerned by the apparent lack of visibility by management in downgrading guidance that was less than three months old. This adds to existing concerns surrounding poor operating leverage and inconsistent cash flow. Although the reasons given for the weakness are plausible, the sudden nature of the shortfall raises questions for the broker around the depth of engagement the company has with its clients.

While the company's software is world-class, as is evidenced by the strong customer list and consistent channel feedback, Deutsche Bank believes the path to achieving a globally dominant product with strong recurring earnings remains uncertain. Moreover, confidence in management has been severely dented. Deutsche Bank retains a Hold rating, cutting its target to \$4.50 from \$6.80.

Conject Below Expectations

Macquarie also sticks with a Neutral rating. The broker notes the first half includes a full contribution from the Conject acquisition and commentary suggests the performance of this business has been below initial expectations, with revenue affected by changes to recognition policy and integration disruptions. Assuming flat revenues from Conject implies, the broker expects a slowdown in the existing business growth to around 10%.

The stock has fallen a long way but the broker continues to believe in the medium-term growth prospects, although concedes there is little valuation support even at current levels. Delivery of medium-term revenue growth targets and the significant margin expansion that is typical of software-as-a-service will be need to be demonstrated.

Near-term Catalyst Difficult To Find

A near-term re-rating is unlikely and a catalyst difficult to identify, Credit Suisse asserts, given the market is

likely to be sceptical about the value of new enterprise agreements and management credibility has been reduced. The broker retains its Outperform rating despite the decline of 45% in the share price, continuing to envisage potential upside in the long-term at current levels. This is because the company has a first-mover advantage and a large addressable market.

The main change since the AGM in October, UBS observes, is the lower-than-expected performance in the Americas. The broker notes, at the time of the FY16 result, the 72% of FY17 revenue is contracted implied a further \$49.3m of new revenue required to meet the mid point of prior guidance. Hence, the new guidance implies \$35.8m is now required on a full year basis, which equates to a -27% decline in new revenue expectations.

Given the apparent slowdown in revenue expectations, UBS has reduced confidence in the FY18-19 guidance of 20-25% per annum growth and the EBITDA margin of 17-22%. The stock is not expected to outperform with such uncertainty. UBS retains a Hold rating and downgrades its target to \$3.40 from \$8.00.

Citi also downgrades its target sharply, to \$4.95 from \$8.69, but retains its Buy rating. The broker considers the market reaction excessive and there is a low probability of a further material downgrade. First half guidance implies robust second half expectations, which may prove challenging, and medium-term growth could be affected by shifting political landscapes and slower customer uptake.

Citi does point out that the company's visibility on the full year ordinarily increases at the first half result. For example in FY15 the company had 78% of FY16 contracted revenues, which increased to 97% at the first half result. Citi expects a similar outcome for FY17, although acknowledges the company's Connected Cost offer is not contracted, so visibility this year may consequently be slightly lower.

There are three Buy ratings and three Hold on FNArena's database. The consensus target is \$4.05, suggesting 32.4% upside to the last share price. This compares with \$7.72 ahead of the downgrade. Targets range from \$3.40 to \$4.95.

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More Copper, Less Gold For OZ Minerals

More copper and less gold production is expected from OZ Minerals in coming years and Carrapateena's imminent feasibility study could be a catalyst for the stock.

-Main risks in the trajectory of the copper price and AUD -Production outlook materially improved at Prominent Hill -Is the market overlooking the risks with Carrapateena?

By Eva Brocklehurst

Copper-gold miner, OZ Minerals ((OZL)), has revised its medium-term guidance for Prominent Hill, with more copper and less gold expected over the next three years. The Carrapateena feasibility study is expected early in the June quarter, and brokers expect this could be a catalyst for the stock.

The company's 2016 copper production of 116,900 tonnes beat guidance of 105-115,000 tonnes and gold production of 118,300 ounces was within the guidance range of 115-125,000 ounces. 2016 C1 cash costs of US 74.1c/lb were in line with expectations, despite the 15 days of power black-outs in South Australia. Management has confirmed the share buy-back will continue.

Citi forecasts higher milling and underground mining rates and raises its expectations for copper and gold grades in FY17-19. Accordingly, earnings per share estimates are increased for those years. Citi expects the news flow will now focus on Carrapateena, one of the world's largest undeveloped copper resources, and possibly include M&A, as the company seeks to acquire base metal and gold assets which can diversify its production footprint.

The main risks for the stock are in the copper price and the Australian dollar. Citi notes copper is highly geared to economic recovery and any change in economic activity has the potential to alter earnings assumptions and valuations for OZ Minerals.

Clearer Path For Prominent Hill

A revision to the mine plan at Prominent Hill has materially improved the production outlook for copper in 2018 and 2019, and Macquarie believes the focus on copper ore in changes to the open pit plan should mean a production rate close to 100,000 tonnes per annum is maintained through to 2019. The broker lifts copper production forecasts at Prominent Hill by 4% for 2017, 13% for 2018 and 53% for 2019 to match guidance.

The drive to produce more copper means the broker's gold production forecasts fall -10-20% over the next three years, while cost assumptions (AISC) rise 32% and 10% for 2017 and 2018 respectively. Factoring in the longer mine life at Prominent Hill means the broker's price target is raised 11% to \$9.30.

Other brokers agree a clearer plan for Prominent Hill has now been established and the market's focus should shift back to Carrapateena, but both Morgans and Credit Suisse highlight the current share price appears to ignore the risks from the undeveloped project.

Morgans upgrades forecasts for earnings per share in line with higher copper price assumptions and the benefits to medium-term operating assumptions at Prominent Hill. The broker notes a significant portion of the upgrade to the Prominent Hill reserve in November was driven by reduction in the mining reserve cut-off grade, which the company believes to be sustainable.

Credit Suisse believes the greatest near-term opportunity is from the re-optimisation of the Prominent Hill underground mine, to progressively include additional resources which, while already defined, have an in-situ value that is too low relative to the cost base. Ultimately, the broker believes exploration success underground will need to be balanced by a cost structure that is more appropriate to the re-configured, lower underground-only milling rate.

The broker believes power availability in South Australia has impacted the company's decision on the configuration of the mill, with a steady power draw possibly more readily accommodated if supply is fragile in coming years.

Carrapateena The Catalyst

Morgans notes Carrapateena remains a technically complex project, where relatively small changes in key inputs

can have large detrimental effects on value. The broker also lauds the company's agility during the October power outage in South Australia, as it mined more underground ore, maintaining its 2016 copper guidance. The company displaced lower-margin gold-only ore with higher-value copper ore.

Morgans suspects the recent rating upgrade of the stock has been driven by general demand for large, liquid and high-margin copper exposures amid rising copper prices. Such stocks are scarce on the ASX and this helps to explain the stock's premium. Still, with prices now well ahead of fundamentals the broker believes the market is overlooking inherent risks and downgrades to Reduce from Hold. Morgans retains a preference for Sandfire Resources ((SFR)) in copper.

Ord Minnett believes the risks to the share price are evenly skewed. The broker remains bearish about the near-term copper outlook, expecting prices will retrace towards US\$2/lb in 2018. Ord Minnett maintains a Hold rating. The stock remains the key pick in the copper space for UBS, supported by its two long-life assets and a positive outlook towards copper. UBS has a Buy rating.

The broker notes investors are somewhat cautious regarding Carrapateena, with a view that the asset is marginal and the risk profile elevated. The broker expects the full feasibility study due by the end of the March quarter to deliver the details necessary to de-risk the asset further.

On FNArena's database there are two Buy ratings, three Hold and three Sell. The consensus target is \$8.01, suggesting -10.4% downside to the last share price. Targets range from \$5.80 (Morgan Stanley) to \$10.50 (Citi).

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Brokers Upgrade As Navitas Finds Clear Air

Education provider Navitas has cleared the headwinds brought about by the loss of its Macquarie University contract and brokers respond with several upgrades.

-Concerns over further contract losses allayed -University more central in the JV structure -Scope for further capital management?

By Eva Brocklehurst

Education provider Navitas ((NVT)) has finally cleared the headwinds created by the closure of its Macquarie University program over a year ago, and brokers have responded with several upgrades to ratings.

The first half result was messy but in line with Credit Suisse expectations at the headline. First half operating earnings of \$76.6m were down 7.5% on the prior corresponding half, primarily from campus closures and currency headwinds. Guidance for FY17 suggests operating earnings (EBITDA) will be flat, ex currency, at the group level.

Credit Suisse expects university partnerships will return to growth in the second half. Further rationalisation of colleges and a possible review of the remaining assets within the professional and English programs could provide scope for further capital management, the broker contends. Credit Suisse upgrades to Neutral from Underperform on valuation grounds because of the recent share price weakness.

The result was in line with Deutsche Bank's expectations at the net profit and EBITDA levels but revenue was well below forecasts. Nevertheless this revenue weakness was offset by significantly better cost performance.

The broker is wary about the step-up in net debt and the low cash conversion during what is still, effectively, a period of transition. The company has confirmed a buy-back will resume, which Deutsche Bank suggests should provide some support for the share price.

Strong International Student Growth

Macquarie upgrades to Outperform from Neutral, believing the company will benefit from strong, long-term international student growth. This should be underpinned by steady fee growth and the additional margin benefits of increased scale and efficiency. The broker forecasts FY18 and FY19 EBITDA growth of 8% and 7% respectively, driven by a respective 10% and 8% growth in the core university partnership division.

Fears of further contract losses have been allayed, following a run of renewals. Macquarie expects all contracts due for expiry in 2017 will be successfully renewed. Regulatory risk is also reduced, with favourable government sentiment in Australia and Canada.

Moreover, international education is economically important in the US and UK, where it contributes US\$34bn and GBP15bn annually, and the broker suggests this provides a safeguard against overly adverse policy shifts.

Macquarie expects the decline in UK enrolments will cease and be followed by a period of low growth. Muted growth is expected in the US.

A positive aspect, in the broker's opinion, is the company's exposure to lower-ranked universities which are suspected to be more reliant on its services. Macquarie also believes the joint-venture structure allays concerns held by higher-ranked universities over outsourcing university programs as, under a JV structure, the university will be more central in the maintenance of standards and ultimately in the protection of its brand.

Is The Share Price Full?

The broker considers Navitas large and competent enough to withstand increased government scrutiny of the various courses on offer and their eligibility for loans. Demand is expected to lift as weaker competitors fall by the wayside. The broker also believes the company has a good chance of lobbying for an amendment to the loan cap on nursing, a key employment growth area.

Morgan Stanley is pleased there is finally clear air ahead for Navitas. The debate for the broker now centres on the level of sustainable growth and the right multiple to pay for this growth. Guidance suggests growth levels are robust but the broker notes this also comes with a wider risk profile than existed in the past.

Morgan Stanley believes the current price/earnings ratio of 20x on FY17 estimates, and 18x on FY18 estimates, is relatively full. Therefore, an Equal-weight recommendation is retained.

UBS upgrades to Buy from Neutral. With the transition from the loss of the Macquarie University contract largely completed, and the recent addition of another US college, the broker believes the market can renew its focus on the potential growth in earnings and the other attractive attributes of the stock. These include a high return on capital, strong cash flow conversion and a low-gearred balance sheet.

FNArena's database contains two Buy and three Hold ratings. The consensus target is \$5.03, suggesting 10.9% upside to the last share price. Targets range from \$4.40 (Credit Suisse) to \$5.30 (Deutsche Bank). The dividend yield on FY17 and FY18 estimates is 4.4% and 4.6% respectively.

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UK OK, But GBST Hits Downgrade Button

Weak conditions in the UK caused financial technology provider GBST to hit the downgrade button. Scrambling to adjust forecasts, brokers still consider the long-term outlook is secure.

-Revenue shortfall expected to be temporary and work pipeline solid -Wealth management in the UK positive in the longer term -Yet, concerns linger about the implied decline in the second half

By Eva Brocklehurst

Another weaker-than-expected outlook for FY17 has been offered, this time by financial technology provider GBST ((GBT)). The downgrade is attributed to four project deferrals in the UK, where weak operating conditions prevail, and a cancellation. The company has indicated it will not adjust its cost base in response, as it expects the revenue shortfall to be temporary, and the pipeline of work remains solid.

Given the company's inherent fixed cost leverage, compounded by its current elevated expenditure on R&D, the lack of services work has had a material impact on second-half profitability. Despite this, Deutsche Bank retains a Buy rating on valuation and expects momentum will improve materially in FY18. The stock is at five-year lows, despite solid revenue and client growth.

The company expects FY17 operating earnings (EBITDA) of \$12m, materially below broker forecasts, with consensus previously around \$19m. A minor positive, Deutsche Bank notes, is that the international capital markets division is expected to report an EBITDA profit in the first half, and this is a division that has been highly challenged over the past seven years.

Deutsche Bank makes material downgrades to FY18 expectations to reflect the trading update but still expects reasonable growth, driven by an improvement in services revenue. The broker remains attracted to the strong cash generating and capital-light business model.

Excessively Weak Guidance In Context of CoFunds Acquisition

RBC Capital Markets is cautious about the outlook given the company suggested the second half looks worse than the first half. The broker believes the guidance is particularly weak in the context of Aegon acquiring CoFunds. This was a significant deal for the company, which closed on January 3 after much delay.

The broker believes this explains a lack of work in the first half but significant work would have been expected some time in the second half. Guidance indicates this is not the case, as the segment will make a loss at the EBITDA level after R&D. RBC Capital Markets, not one of the eight stockbrokers monitored daily on the FNArena database, has downgraded to Underperform with a \$3.00 target.

CLSA, also not one of the eight, downgrades to Outperform from Buy* with a \$3.20 target. The broker notes the week guidance for the second half highlights a lack of leverage with clients and a reliance on lumpy services revenue, amplified by an uncertain macro environment in the UK.

The broker queries whether this is the first of more UK-related Brexit downgrades. Nevertheless, CLSA remains optimistic about GBST's long-term prospects and expects FY18/19 earnings to improve after completion of the Composer upgrade and the start of the CoFunds migration.

Problems Temporary?

Morgans also considers the problems temporary, driven entirely by unforeseen contract deferrals which hit at the same time as the company's peak IT development expenditure occurred, with the upgrading of Composer and the new Catalyst retail advisor product. In the short term, the broker notes there is no solution to the IT development cost issue as backbone system upgrades cannot be deferred.

IT costs are expected to remain high until the second half of FY18. The broker expects wealth management customer services revenue will build slowly, as customers can only defer system maintenance for so long before they hurt their own performance. The company is building a powerful global franchise as a supplier of core wealth management platforms and Morgans expects substantial long-term earnings growth. The broker retains an Add rating.

Earnings growth in Australian capital markets over the next five years looks challenging to UBS and structural headwinds remain a feature of the broker's base case for the segment. While conditions are subdued and additional investment and currency volatility will weigh on divisional earnings, the broker believes the longer term picture for UK wealth management is positive. The division continues to benefit from regulatory reforms which are driving a lift in advisor/D2C platforms.

Still, UBS is concerned about the extent of the implied second-half earnings decline in the UK. Continued weakness in the British pound is likely to have an impact on the company via offshore earnings translated back into Australian dollars and the potential for further project deferrals. UBS downgrades to Neutral from Buy, given the headwinds and uncertainty.

FNArena's database shows two Buy ratings and one Hold (UBS). The consensus target is \$3.85, suggesting 23.9% upside to the last share price. This compares with \$4.69 ahead of the update. Targets range from \$3.40 (UBS) to \$4.40 (Deutsche Bank).

* CLSA has a five level ratings system in which Buy is the top rating and Outperform a step below.

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Upper For Downer

Diversified engineering & construction conglomerate, Downer EDI, is expertly managing the move to infrastructure from resources but brokers believe this is largely reflected in the share price.

-Large potential in balance sheet for acquisitions and/or buy-backs -Large amount of upside now factored into share price -Citi: one of the best-placed options in the infrastructure sector

By Eva Brocklehurst

Engineering & construction conglomerate, Downer EDI ((DOW)), is moving with the times, countering the mining investment downturn with new business in infrastructure and ongoing work on the National Broadband Network. Net profit in the first half of \$78m beat many broker forecasts, while FY17 net profit guidance has been raised by 7% to \$175m.

The results beat Macquarie's estimates in four out of the six divisions, with the main surprise in technology & communications services, driven by a ramp-up in the NBN and Telstra ((TLS)) work. The broker expects these two should remain healthy contributors to Downer's income for the next 2-3 years, which highlights the benefits of the company's diversified nature.

The company has over \$400m in potential capacity on the balance sheet for acquisitions and/or buy-backs, in Macquarie's calculations, and the earnings recovery for Downer has started earlier than expected, with 8.6% growth in prospect for FY18.

Soft Result In Utilities & Mining

The broker notes the completion of a major gas project and lower-than-expected profit from the Ararat wind farm muted the results in utility services in the half year. Moreover, the completion of the Christmas Creek contract contributed to a soft result in mining earnings, where EBIT declined 34%.

A \$25m reduction in depreciation flattened the first half result, but as this relates to mining and the sale of some equipment, Macquarie does not believe it detracts from the services result, which was better-than-expected.

The company remains reasonably confident that the Adani Queensland coal project will proceed, having a letter of intent for both contract mining and the coal handling plant. However, Macquarie does not factor this into its forecast, nor has the company factored it into guidance.

While there is potential to exceed provides guidance and a high level of recurring revenues with low debt, Deutsche Bank is of the view that this is largely reflected in the share price, maintaining a Hold rating. Credit Suisse is even less enthusiastic, although concedes there was no hiding the strength of the result.

While it was hard to find an area that was disappointing the broker believes the outcome is reflected in the share price response. Credit Suisse upgrades its earnings base for FY17, assuming a similar, but now higher, earnings trajectory.

Record Work In Hand

Work in hand was a record \$21.1m, reflective of recent wins in rail and around 58% of revenue being generated from public infrastructure clients. The growth outlook for transport, utilities and rail is strong while there are some headwinds across mining and engineering, construction & maintenance. Credit Suisse believes the business is exiting the high capex mining cycle in good shape, but this is reflected in the multiple.

The broker struggles to get its valuation close to the share price. Hence, an Underperform rating is retained. Nevertheless, Credit Suisse suspects this will be unlikely to compel holders of the shares to sell, particularly if they feel further earnings surprises can be delivered.

Morgan Stanley also suspects, despite the upgraded guidance, that downgrades to consensus EBITDA forecasts for FY17 are likely. The broker estimates that whilst FY17 net profit guidance implies around a 9% uplift to consensus, it is in fact a -7% downgrade to consensus EBITDA. The broker acknowledges the flexibility on the balance sheet and that a possible lifting of the final dividend has been flagged, but suspects the company's ability to fully frank this would be somewhat limited.

Citi notes management has taken definitive steps to restructure and appears to be managing the downturn in resources, shifting the portfolio towards the growing infrastructure and utility sectors. The broker is of the view that the exposure to public infrastructure investment puts it in a robust position for the medium term. While the 50% jump in the share price since the FY16 result has anticipated this to some extent, the broker still believes the stock is one of the best placed options in the sector.

FNArena's database shows one Buy (Macquarie) rating, three Hold and one Sell (Credit Suisse). The consensus target is \$6.25, signalling -9.9% downside to the last share price. This compares with a target of \$5.54 ahead of the results targets range from \$4.01 (Morgan Stanley) to \$7.45 (Macquarie).

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Material Matters: Silver, Zinc And Coal

A glance through the latest expert views and predictions about commodities. Silver use in PV cells; zinc markets; China's coal policies; dividend outlook for miners.

-Silver demand in solar cells likely to decline in the medium term -High price of zinc relative to other metals will begin to destroy demand -Coal output restrictions likely to return in China -Morgan Stanley suspects relative underperformance in mining sector

By Eva Brocklehurst

Silver

Citi suspects demand for silver in the photovoltaic (PV) cells market may improve in 2018, based on optimistic estimates of global cell capacity. Demand for silver in solar cells is in a state of flux and likely to decline over the medium term, as 2017 becomes a year of de-stocking of capacity and global demand catches up with supply.

Demand for silver emanating from solar cells comprised 7% of total silver demand in 2016, according to industry estimates. It is believed, based on these estimates, that the volume of silver used within PV cells is declining around -5% every year, because of continued efforts to reduce costs.

In the event that silver prices rise rapidly, the broker believes companies may adopt more stringent cost-cutting programs, or invest in non-precious metal components altogether. Alternative technologies are still too expensive to displace existing solar cells but the risks of copper substitution within IBC solar cells could decrease the silver paste market share over the medium term.

Meanwhile, PV rooftop tiles may eventually improve end use in residential markets and grow the distributed energy network. The amount of silver used in roof tiles is not yet clearly evident. Much depends on whether the tile is a thin-film solar cell or a monocrystalline silicon. Hence, based on current arrangements, Citi approximates 100-120 mg of silver per tile could be in use. The broker expects both the efficiency and rising adoption rates will increase the penetration of PV cells among US households.

In the current market, where the Chinese government has clamped down on feed-in tariffs for solar PV systems, Citi believes only the lowest-cost manufacturers are likely to survive and possibly increase market share. Policy and subsidy changes may begin to slow down production and, while solar growth in China exceeded expectations in 2016, the broker question is whether the rate of growth is sustainable.

Zinc

Chinese trade and smelter production data have confirmed that market tightness is yet to emerge. Nevertheless, zinc prices look robust in the high US\$2000/t range, Macquarie asserts. Chinese smelters are now making minor reductions in output and the ex-China market is preparing for a marathon negotiating period for 2017 concentrates. Macquarie believes the wind is favouring sellers at this juncture.

The broker agrees continued price strength suggests prices will be above US\$3000/t by the end of the year. After that, the trajectory is less certain. Glencore's shuttered mines are likely to return to production at some point while new projects are being accelerated.

The price of zinc relative to other materials such as aluminium will begin to destroy demand the longer the price remains high. In 2018 the broker expects continued shortages of metal but also a subsiding of demand growth. Macquarie's current base case rests on a re-start of the Glencore mines in mid 2017. A combination of these changes is likely to dampen prices before more concrete physical market re-balancing arrives in 2019/20 to bring zinc prices back down to earth.

Coal

China is expected to underpin the global coal market in the near term. If prices continue to slide, Macquarie expect some form of output restrictions will come back, such as the 276 days policy, which was suspended in November until the end of the first quarter. The government recently outlined a thermal coal price target around the annual contract price of RMB535/t.

Supply intervention now appears only likely if prices are above RMB600/t or below RMB470/t. The Chinese government's pronouncements may be enough to prevent prices trading outside this range and the broker's confidence in this scenario is one of the main factors underpinning its recent upgrades to coal price forecasts.

The broker also contemplates a scenario where China will pull back from its readiness to accept coal imports, as an alternative measure to support domestic coal prices, particularly as the policy goal is to support domestic mining.

Macquarie notes Beijing's ability to strongly intervene in domestic supply renders traditional supply and demand analysis for coal largely obsolete. It is possible the government could make further adjustments to import taxes and/or coal quality cut-off levels, in an effort to dissuade imports and provide more assistance to domestic coal mines.

This is not Macquarie's base case. Nonetheless, the broker believes it is a risk worth highlighting, as if this was to happen it would clearly provide downside risks to seaborne coal price forecast.

Dividends

The potential for the mining sector to re-rate on structural changes in dividend policies is a key debate, Morgan Stanley observes. Yet, analysis indicates the mining sector is unlikely to re-rate on a shift to dividends, based on pay-out ratios.

Analysis of long-term dividend trends suggest there is a modest historical correlation between dividend yield and relative performance, except at extreme levels. The broker warns the market is currently close to such an outlier and, historically, this has driven 2% relative underperformance in the following 12 months.

The broker believes dividend signals are not as strong as the debate suggests and the market is currently close to such a level which is not helpful for sector performance. The broker notes a switch from progressive dividends to pay-out ratios reduces the risk of over-investment during periods of high cash flows. On average, Morgan Stanley calculates companies are targeting 50% pay-out ratios.

This compares to 42% and 44% for Rio Tinto ((RIO)) and BHP Billiton ((BHP)) respectively. The pay-out ratio dropped to 26% and 32% respectively during the super cycle, as progressive dividend policies encouraged more re-investment in growth relative to dividends. In the pre-super cycle period pay-out ratios reconcile neatly with the new dividend policies, the broker asserts.

Considering the outlook for volume growth across commodities Morgan Stanley believes it will be hard to replicate double-digit rates of growth. On a base case estimate the broker's forecasts imply 3% and 2% growth in dividends per share for Rio Tinto and BHP Billiton, respectively, for the 10 year period 2017-27.

Find out why FNArena subscribers like the service so much: "Your Feedback (Thank You)" - Warning this story contains unashamedly positive feedback on the service provided.

Manganese Is Energy Critical

By Richard (Rick) Mills aheadoftheherd.com

As a general rule, the most successful man in life is the man who has the best information

In 1917 the War Industries Board (WIB) noted that the United States was deficient in certain minerals of great importance to war making and self defense. A pre-World War II list of materials contained a total of 29 materials: 14 were strategic materials that 'must be based entirely or in substantial part on sources outside the United States.' There were 15 critical materials that would be easier to source, perhaps even domestically, than the strategic materials.

The 1939 Strategic Materials Act authorized US\$100 million to purchase strategic raw materials for a stockpile of 42 strategic and critical materials needed for wartime production.

By May 1940, small quantities of certain materials - ie. chromite, manganese (Mn), rubber and tin (Sn) - had been procured under the Strategic Materials Act. The purchases certainly weren't enough and all throughout the war effort these and other numerous materials had to be imported in large quantities.

By 1948 the WIB's Munitions Board had developed a list of 51 required strategic and critical material groups. By 1950 the number of required strategic and critical materials had expanded to 54 groups, representing 75 specific commodities.

Let's fast forward a few decades...

The Metallurgical Achilles' Heel of the United States

A concise summary of U.S. mineral vulnerabilities was presented to the Industrial Readiness Panel of the House Armed Services Committee as early as 1980 by General Alton D. Slay, Commander Air Force Systems Command. General Slay pointed out that technological advances have increased the demand for exotic minerals at the same time that legislative and regulatory restrictions have been imposed on the U.S. mining industry.

"The U.S. depends on southern Africa's minerals for about the fifty percent of the "big four". Thus, a long-term cutoff of any or all of these materials has the potential for an economic and strategic crisis of greater proportions than the oil crisis of the 1970s. An embargo of South African minerals to the U.S. would affect millions of American jobs in the steel, aerospace, and petroleum industries, and could in effect shut down those industry groups." U.S. Strategic and Critical Materials Imports: Dependency and Vulnerability

The 1981 report "A Congressional Handbook on U.S. Minerals Dependency/Vulnerability" singled out eight materials "for which the industrial health and defense of the United States is most vulnerable to potential supply disruptions" - chromium, cobalt, manganese, the platinum group of metals, titanium, bauxite/aluminum, columbium, and tantalum - the first five have been called "the metallurgical Achilles' heel of our civilization."

In 1981, President Reagan announced a "major purchase program for the National Defense Stockpile, saying that it was widely recognized that our nation is vulnerable to sudden shortages in basic raw materials that are necessary to our defense production base.

In 1984 U.S. Marine Corps Major R.A. Hagerman wrote: "Since World War II, the United States has become increasingly dependent on foreign sources for almost all non-fuel minerals. The availability of these minerals have an extremely important impact on American industry and, in turn, on U.S. defense capabilities. Without just a few critical minerals, such as cobalt, manganese, chromium and platinum, it would be virtually impossible to produce many defense products such as jet engine, missile components, electronic components, iron, steel, etc. This places the U.S. in a vulnerable position with a direct threat to our defense production capability if the supply of strategic minerals is disrupted by foreign powers."

In 1985, the secretary of the United States Army testified before Congress that America was more than 50 percent dependent on foreign sources for 23 of 40 critical materials essential to U.S. national security.

The 1988 article "United States Dependence On Imports Of Four Strategic And Critical Minerals: Implications And Policy Alternatives" by G. Kevin Jones was written in regards to what he thought are the most critical minerals upon which the United States is dependent for foreign sources of supply - chromium, cobalt, manganese and the

platinum group metals (PGE). These metals represent the "metallurgical Achilles' heel" of United States strategic mineral supply because their role in the economy is pervasive and they are vulnerable to supply interruption.

The May 1989 report "U.S. Strategic and Critical Materials Imports: Dependency and Vulnerability. The Latin American Alternative," deals with over 90 materials identified in the Defense Material inventories as of September 1987. At least 15 of these minerals are considered "key minerals" because the US is over 50% import reliant. All these minerals are essential to domestic security and the national economy but four are referred to as the "first tier" or "big four" strategic materials because of their widespread role and vulnerability to supply disruptions - chromium, cobalt, manganese and platinum group metals.

In 1992 Congress directed that the bulk of the strategic and critical materials the U.S. had been able to accumulate in the National Defense Stockpile be sold.

According to the United States Geological Survey (USGS), in 1999 the United States was at least 50 percent dependent on a foreign source for 27 out of the 100 materials covered in its publication Mineral Commodity Summaries. By 2013, this number had grown to 41 materials out of 100.

The primary purpose of the National Defense Stockpile (NDS Program) is to decrease the risk of dependence on foreign suppliers or single suppliers on supply chains of strategic and critical materials used in defense, essential civilian, and essential industry applications. The NDS Program allows for decreasing risk by maintaining a domestically held inventory of necessary materials.

Section 12 (1) of the Stock Piling Act defines strategic and critical materials as materials that (A) would be needed to supply the military, industrial, and essential civilian needs of the United States during a national emergency and (B) are not found or produced in the United States in sufficient quantities to meet such need. Based on the results of the 2015 Requirements Report research, the NDS Program recommended new authorities for twelve of the 21 materials exhibiting a net shortfall:

aluminum oxide, fused crude antimony beryllium metal carbon fiber (two types) chlorosulfonated polyethylene europium germanium lanthanum magnesium manganese metal, electrolytic silicon carbide fiber, multifilament Manganese

Aside from iron manganese is the most essential mineral in the production of steel. You can't produce steel without adding 10 to 20 lbs. of manganese per ton of iron. Which makes manganese the fourth largest traded metal commodity.

Both Canada and the United States have numerous and vast iron ore deposits, yet neither country produces manganese.

Fact - Manganese is a strategic mineral essential for the economy and defense of the United States.

Fact - Manganese cannot be sourced in adequate quantities from reliable and secure domestic suppliers.

Fact - There is no substitute for manganese, as a matter of fact manganese has itself become a substitute in certain alloy applications.

Security of supply

Many minerals were recognized as critical and strategic almost a hundred years ago (manganese was identified among them). Some - referred to as the big four, the top tier or the metallurgical achilles heel of the U.S. - are more critical than others.

Chromium, cobalt, manganese and the platinum group metals (PGE) - are the basic building blocks any nation needs for its economic foundation.

The U.S. is dependent on South Africa, the politically unstable Democratic Republic of Congo (DRC) and an increasingly unreliable and aggressive China for over half of its supply of what it considers strategic or critical minerals.

"As resource constraints tighten globally, countries that depend heavily on ecological services from other nations may find that their resource supply becomes insecure and unreliable. This has economic implications - in particular for countries that depend upon large amounts of ecological assets to power their key industries or to support their consumption patterns and lifestyles." Dr. Mathis Wackernagel, President of the Global Footprint Network

Critical materials, especially the 'big four' - chromium, cobalt, manganese and the platinum group - are the metallurgical Achilles' heel of our civilization. Accessing a sustainable, and secure, supply of these raw materials

is going to become the number one priority for all countries.

So why have I singled out manganese? Out of all the strategic or critical minerals I could have talked about I choose manganese. Yes, it's been considered strategic for a century because of its use in steel making and alloys but something else is up with manganese that you, an intelligent well informed ahead of the herd investor should know about.

"the country (U.S. - editor) is devoid of any electrolytic manganese production, importing it all from — you guessed it — China, with lesser amounts from South Africa...

It is important to be clear we are talking about electrolytic manganese, not ferro-manganese or silico-manganese, which are produced in the US from manganese ores imported from Gabon, but mostly supplied as ferro-alloys imported from South Africa, China and elsewhere. Electrolytic manganese is used as an alloying element in aluminum and copper alloys, as a colorant in bricks, and combined with lithium or nickel in batteries. Indeed, its use in lithium-ion manganese batteries is its fastest and potentially most challenging application — if the US cannot access competitively priced and reliable supplies of manganese, a host of high-tech new applications will be lost to foreign competitors.

Although manganese has been used for years in conventional batteries, its use in the newest generation of batteries for electric vehicles is likely to grab the most attention." Stuart Burns, U.S. Facing Supply Risk for Electrolytic Manganese Metal

Current tensions between the United States and China highlight the need for security of supply regarding the materials and minerals the U.S. considers strategic and critical.

Critical Materials

A strategic or critical material is a commodity whose lack of availability during a national emergency would seriously affect the economic, industrial, and defensive capability of a country. Manganese has met this criteria for over 100 years.

In its 2011, Critical Materials Strategy Report, the U.S. Department of Energy (DOE) focused on materials used in four clean energy technologies:

wind turbines - permanent magnets electric vehicles - permanent magnets & advanced batteries solar cells - thin film semi conductors energy efficient lighting - phosphors The DOE says they selected these particular components for two reasons:

Deployment of the clean energy technologies that use them is projected to increase, perhaps significantly, in the short, medium and long term Each uses significant quantities of key materials The DOE defines "criticality" as a measure that combines importance to the clean energy economy and risk of supply disruption.

A Report by the APS Panel on Public Affairs and the Materials Research Society coined the term "energy-critical element" (ECE) to describe a class of elements that currently appear critical to one or more new, energy related technologies - batteries certainly fit in here.

Conclusion

For the last couple of decades energy researchers have focused on capturing power from renewable sources and making our existing electric infrastructure as efficient as possible. Energy storage is the last vital piece, the still missing third link needed to wean the global economy off fossil fuels and enable widespread adoption of renewable clean energy and electric cars.

We know the United States has long considered manganese a strategic material. We know the U.S. has no production of its own - instead relying on others to supply Mn ore and value added manganese products.

We also know energy storage is critical for renewable integration and electrification of the energy infrastructure. So, shouldn't manganese suddenly becoming an "energy-critical element" be on all our radar screens?

Is manganese on your screen?

If not, it should be.

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Richard is the owner of Aheadoftheherd.com and invests in the junior resource/bio-tech sectors. His articles have been published on over 400 websites, including:

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If you're interested in learning more about the junior resource and bio-med sectors, and quality individual company's within these sectors, please come and visit us at www.aheadoftheherd.com

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Weekly Ratings, Targets, Forecast Changes

By Rudi Filapek-Vandyck, Editor FNArena

Guide:

The FNArena database tabulates the views of eight major Australian and international stock brokers: Citi, Credit Suisse, Deutsche Bank, Macquarie, Morgan Stanley, Morgans, Ord Minnett and UBS.

For the purpose of broker rating correlation, Outperform and Overweight ratings are grouped as Buy, Neutral is grouped with Hold and Underperform and Underweight are grouped as Sell to provide a Buy/Hold/Sell (B/H/S) ratio.

Ratings, consensus target price and forecast earnings tables are published at the bottom of this report.

Summary

Period: Monday January 23 to Friday January 27, 2017 Total Upgrades: 10 Total Downgrades: 17 Net Ratings Breakdown: Buy 43.87%; Hold 41.88%; Sell 14.25%

Stockbroking analysts continue to issue more downgrades for individual stock ratings than upgrades. For the week ending Friday, 27th January 2017, FNArena registered ten upgrades versus 17 downgrades.

Stocks receiving upgrades during the week include BlueScope Steel, ResMed, Vicinity Centres and Western Areas (twice). Stocks receiving downgrades include Bendigo and Adelaide Bank (twice), ERM Power (three times), Village Roadshow, Westfield and, yes, BlueScope Steel too.

BlueScope Steel also tops the week's table for positive gains to price targets (+19%), beating Sims Metal, CSL, ResMed and others. On top of the list for negative revisions to price targets sits Village Roadshow (-10.9%), followed by APN News & Media (-9.3%) and Santos (-3%).

Investors might draw confidence from the fact that one week out from the start of the local reporting season, positive revisions are considerably larger than negative adjustments. This is not necessarily the case for profit estimates.

Western Areas was primus inter pares for positive adjustment to forecasts. The gain of 1589% merely proves how fickle the commodities space still is with leverage high in both directions. Sandfire Resources, Santos, South32 and Sims Metal all enjoyed noticeable gains too.

Negative adjustments were large too with ERM Power grabbing the wooden spoon for the week, suffering a blow of -134% to broker estimates. Other noticeable victims of negative revisions include AMP, Village Roadshow, Senex Energy and Oil Search.

Upgrade

ALS LIMITED ((ALQ)) Upgrade to Buy from Hold by Deutsche Bank .B/H/S: 3/2/2

Share prices for engineers and contractors in Australia have recovered from last year's lows on the basis that outlooks and market dynamics have improved. Deutsche Bank analysts acknowledge this much, but they still maintain it's better to remain cautious.

The analysts continue to see earnings risks across the sector, highlighting there are significant differences between markets and sub-markets when it comes to assessing this part of the share market.

ALS Ltd receives an upgrade to Buy from Hold. Price target jumps to \$6.74 from \$5.50.

BLUESCOPE STEEL LIMITED ((BSL)) Upgrade to Accumulate from Hold by Ord Minnett .B/H/S: 5/2/0

BlueScope has raised its first half earnings guidance by 18% to \$600m driven by improved pricing, spreads and a solid performance from the building products division.

Following the upgrade to guidance, Ord Minnett raises its rating to Accumulate from Hold and the target to

\$12.50 from \$10.20.

Underpinning the broker's view is the fact that the company's low earnings multiples, which more than compensate for earnings volatility, and a rapidly de-gearing balance sheet provide potential for near-term capital management.

See also BSL downgrade.

BRAMBLES LIMITED ((BXX)) Upgrade to Buy from Neutral by UBS .B/H/S: 4/2/1

A lack of disclosure and a poor explanation from management for the surprise downgrade to guidance has driven a sharp correction in the share price, UBS observes.

The impact of US retailer de-stocking experienced in December is without anecdotal support and how long the impact continues is uncertain. The broker notes the company is waiting to see January numbers before assessing the likely full year impact.

UBS takes the view that the de-stocking represents a one-off step change in earnings. Despite the uncertainty, UBS believes the business model is intact and upgrades to Buy from Neutral. Target is reduced to \$11.60 from \$12.60.

See also BXB downgrade.

CHARTER HALL RETAIL REIT ((CQR)) Upgrade to Neutral from Underperform by Macquarie .B/H/S: 0/3/3

Macquarie reviews the outlook ahead of the first half results. The stock remains a relatively defensive proposition although the broker is of the view that near-term income growth will be hindered by fewer anchor tenants in turnover rent, low initial yields on development and further dilutive asset sales.

Nevertheless, with the stock trading near estimates of net tangible assets and the potential corporate risk from Shopping Centres of Australasia ((SCP)) the rating is upgraded to Neutral from Underperform. Target is raised to \$4.24 from \$4.18.

OROTONGROUP LIMITED ((ORL)) Upgrade to Neutral from Sell by Citi .B/H/S: 0/1/0

OrotonGroup's market update yet again did not meet market expectations. Citi analysts have reduced their price target to \$1.90 from \$2.05 but post share price shellacking they've also upgraded to Neutral from Sell.

The decision to upgrade is motivated by the fact the analysts anticipate a turnaround in fortune in FY18, when a new range in designer handbags, jewelry and perfume should help sales, along with less discounting.

RESMED INC ((RMD)) Upgrade to Accumulate from Hold by Ord Minnett .B/H/S: 6/1/0

Ord Minnett considers the company on the cusp of a return to double-digit growth, following the successful launch of its new masks. A refresh of the product should deliver a solid benefit to product mix, supporting a rise in gross margins.

The broker's confidence in the outlook is supported by US political changes, which signal a more benign funding environment and this limits the pressure on prices. The broker raises its recommendation to Accumulate from Hold and the target to \$9.50 from \$8.25.

TOX FREE SOLUTIONS LIMITED ((TOX)) Upgrade to Overweight from Equal-weight by Morgan Stanley .B/H/S: 2/2/1

Morgan Stanley forecasts Tox's earnings from resource sector construction will fall to less than 1% in FY18, from 43% in FY13. Higher margin production earnings will grow in FY18 driven by contract wins.

Tox is trading at a 35% discount to peers and has a history of rapid re-rates, Morgan Stanley points out. With earnings troughing, and the Daniels acquisition offering long term synergies, valuation and risk/reward are now attractive to the broker.

Upgrade to Overweight. Target rises to \$3.00 from \$2.65. Industry view: In-line.

VICINITY CENTRES ((VCX)) Upgrade to Accumulate from Hold by Ord Minnett .B/H/S: 1/2/2

Ord Minnett suggests the A-REIT sector retains all the necessary ingredients for attractive risk-adjusted returns. The main risk is an inflection point in the property cycle. Underperformance has potential to continue if long bond yields continue to rise.

Ord Minnett upgrades to Accumulate from Hold, mainly on valuation grounds. Target is \$3.25.

WESTERN AREAS NL ((WSA)) Upgrade to Hold from Sell by Deutsche Bank and Upgrade to Neutral from Sell by Citi .B/H/S: 1/4/1

December quarter production was ahead of Deutsche Bank's estimates because of strong mined grades. Operating costs were below forecasts.

The broker suspects the company could exceed guidance for the seventh year in a row. The stock trades as a proxy for nickel price sentiment and, given the imminent re-start of Indonesian ore exports, sentiment remains weak.

Whilst uncertainty continues, the broker considers the valuation is less stretched and, while remaining cautious, upgrades to Hold from Sell. Target is \$2.40.

As the company released a stronger-than-expected December quarter performance, Citi analysts have decided to upgrade to Neutral from Sell. They expect the company to either meet or beat FY17 production guidance and have lifted forecasts.

Estimates have received a boost and this pushes up the price target by 46c to \$2.38. On current projections, shareholders should expect resumption of dividend payouts from FY18 onwards.

Downgrade

AIR NEW ZEALAND LIMITED ((AIZ)) Downgrade to Neutral from Outperform by Macquarie .B/H/S: 0/4/0

After a share price rally for Air NZ, Macquarie is downgrading to Neutral, suggesting the stock is now fair value. Dec Q stats showed yields continued to fall due to competition, but that the rate of those falls is now slowing.

Air NZ's numbers should start to improve ahead as a year passes since competition entry, Macquarie suggests. Yield momentum will need to improve but the broker finds competition rationalisation encouraging. Target falls to NZ\$2.18 from NZ\$2.25.

BENDIGO AND ADELAIDE BANK LIMITED ((BEN)) Downgrade to Sell from Neutral by UBS and Downgrade to Sell from Buy by Citi .B/H/S: 0/1/5

Headwinds facing Australian banks are well known and UBS believes in recent times many of these factors have eased.

Investment property lending has picked up again, mortgage re-pricing suggests banks are more comfortable with meeting targets, while higher bond yields should reduce pressure on net interest margins.

To reflect the improvements the broker upgrades FY17 forecasts by around 2%. That said, a subdued medium-term growth outlook continues.

Despite the recent pull back the broker believes most of the positive news is factored in and downgrades to Sell from Neutral. Target is raised to \$10.00 from \$9.50.

Citi analysts have been reviewing the regional lenders in Australia. While Bank of Queensland is seen as offering one of most attractive yields in the market, the opinion about Bendigo and Adelaide Bank at present share price level is quite the opposite.

Citi analysts are of the view "Bendalaide's" strong performance over H2 2016 has run ahead of expectations, and risk is now that disappointment is about to announce itself. Downgrade to Sell from Buy. Target falls to \$11.75 from \$12.25.

BLUESCOPE STEEL LIMITED ((BSL)) Downgrade to Neutral from Outperform by Credit Suisse .B/H/S: 5/2/0

The company has confirmed first half expectations for \$600m in EBIT, materially higher than the guidance "of at least \$510m" delivered at the AGM in November.

The greatest surprise to Credit Suisse was the uplift in building products, dominated by a stronger performance in US operations from higher steel prices and margins.

The broker downgrades to Neutral from Outperform on valuation grounds and increases the target to \$10.70 from \$10.30.

See also BSL upgrade.

BRAMBLES LIMITED ((BXB)) Downgrade to Underperform from Neutral by Credit Suisse .B/H/S: 4/2/1

US retailer de-stocking and weak pricing in recycled pallets, along with delayed purchase decisions, have caused the company to issue a warning that it will not achieve forecast profit estimates in FY17. Credit Suisse lowers its FY17 US pallets EBIT estimates by around 15%.

The broker notes it is not clear how severe or how long the de-stocking will be and there is a risk with the new CEO that earnings will get re-based. Rating is lowered to Underperform from Neutral. Target is reduced to \$9.80 from \$11.30.

See also BXB upgrade.

CIMIC GROUP LIMITED ((CIM)) Downgrade to Sell from Hold by Deutsche Bank .B/H/S: 0/0/3

Share prices for engineers and contractors in Australia have recovered from last year's lows on the basis that outlooks and market dynamics have improved. Deutsche Bank analysts acknowledge this much, but they still maintain it's better to remain cautious.

The analysts continue to see earnings risks across the sector, highlighting there are significant differences between markets and sub-markets when it comes to assessing this part of the share market.

The rating for Cimic has been downgraded to Sell from Hold. Target lifts to \$27.12 from \$25.76.

ERM POWER LIMITED ((EPW)) Downgrade to Underperform from Neutral by Macquarie and Downgrade to Reduce from Hold by Morgans and Downgrade to Neutral from Buy by Citi .B/H/S: 0/1/2

ERM Power has made an unusual move in using penalty credits over its inventory to settle 2016 large-scale generation certificate (LGC) obligations. The move should increase earnings and tax, Macquarie notes, yet ERM has not changed earnings guidance.

The broker sees the move as logical, but the absence of an upgrade to Australian gross margins is concerning. Current margins appear thus to be well down on FY16. On that basis, and with no earnings upgrade, Macquarie downgrades to Underperform. Target falls to \$1.15 from \$1.24.

The company has changed strategy regarding Large-scale Generation Certificates (LGC) and this means, bottom line, it'll become a tax payer, accumulating franking credits that can later on be attached to dividends paid.

Morgans analysts point out this will also reduced cash flows in the medium term. This implies there is downside risk to the cash dividend, and that means downside risk for the share price, Morgans finds. Downgrade to Reduce from Hold. Target price remains 99c.

Note: Morgans has cut DPS forecasts to 8c from 12c previously (unchanged on gross basis given the addition of franking credits).

Citi analysts have pulled back the rating to Neutral from Buy. On their observation, the share price has rallied by 50% since July last year. There are issues with management's credibility, given omissions in prior guidance provided, suggest the analysts.

While Citi continues to see value on a longer term horizon, there's now an expectation the twelve months ahead won't be that flash. The new deal (complex and not for everyone to understand, explain the analysts) gets the thumbs up. Target loses 1c to \$1.31.

GPT ((GPT)) Downgrade to Neutral from Outperform by Macquarie .B/H/S: 1/3/2

Macquarie expects 2016 operating earnings per share of 29.9c, in line with the growth guidance provided at the September quarter update. The growth rate into 2017 is expected to slow.

The broker considers the stock a solid, defensive proposition with a diversified exposure but with a single digit return and lower trajectory for earnings expected it is downgraded to Neutral from Outperform. Target slips to \$4.98 from \$5.16.

NATIONAL STORAGE REIT ((NSR)) Downgrade to Hold from Accumulate by Ord Minnett .B/H/S: 1/2/1

Ord Minnett suggests the A-REIT sector retains all the necessary ingredients for attractive risk-adjusted returns. The main risk is an inflection point in the property cycle. Underperformance has potential to continue if long bond yields continue to rise.

Ord Minnett downgrades to Hold from Accumulate, mainly on valuation grounds. Target is \$1.52.

NORTHERN STAR RESOURCES LTD ((NST)) Downgrade to Neutral from Outperform by Macquarie .B/H/S: 2/3/0

Northern Star's net production and costs were largely in line with Macquarie's forecasts for the Dec Q. Increased production at Jundee foreshadows expectation of a similar increase at the Kalgoorlie operation as new mines begin to contribute.

But the share price has gained 30% since December against a 5% rise for the ASX100, reaching the broker's target price of \$3.70. Hence Macquarie downgrades to Neutral.

SCENTRE GROUP ((SCG)) Downgrade to Accumulate from Buy by Ord Minnett .B/H/S: 3/1/2

Ord Minnett suggests the A-REIT sector retains all the necessary ingredients for attractive risk-adjusted returns. The main risk is an inflection point in the property cycle. Underperformance has potential to continue if long bond yields continue to rise.

The broker downgrades to Accumulate from Buy, mainly on valuation grounds. Ord Minnett retains a \$4.70 target.

SANDFIRE RESOURCES NL ((SFR)) Downgrade to Neutral from Buy by Citi .B/H/S: 4/3/1

Citi downgrades to Neutral from Buy following a rally in the share price. The analysts have also pushed out some of their production forecasts.

The analysts point out, with mine life at DeGrussa constrained by exploration, developing a new project medium term is necessary.

SPOTLESS GROUP HOLDINGS LIMITED ((SPO)) Downgrade to Neutral from Buy by Citi .B/H/S: 0/3/0

Citi analysts have updated their analysis and there's now an expectation the company's interim report is poised for disappointment. Estimates have been reduced by no less than -30% for this year and next.

Dividend payout ratio has fallen too. Price target dives to \$1.07 from \$1.80. Downgrade to Neutral from Buy.

VILLAGE ROADSHOW LIMITED ((VRL)) Downgrade to Neutral from Buy by Citi .B/H/S: 2/2/0

As Village Roadshow has reported attendance at its Theme Parks has been adversely impacted by Dreamworld's incident over at competitor Ardent Leisure ((AAD)), Citi analysts have downgraded to Neutral from Buy. Citi analysts estimate Village's total theme park attendance is down -6% since the incident.

The stockbroker finds the short term outlook clouded, with the impact on the international and interstate customers yet to reveal itself. Estimates have been cut. Price target falls to \$3.85 (was \$5.40) also taking into account lower valuation multiples.

WESTFIELD CORPORATION ((WFD)) Downgrade to Underperform from Outperform by Macquarie .B/H/S: 4/1/1

Macquarie reviews the outlook ahead of the 2016 results. The broker expects operational earnings of US\$33.1c, below recently downgraded guidance of US\$33.7-34.0c.

Positive aspects to the investment thesis include the potential for a value-affirming restructure and material apartment earnings potential not yet factored into consensus.

The broker downgrades to Underperform from Outperform as the recent re-rating of the share price has compressed total returns and there is downside risk to the 2017 outlook. Target falls to \$9.30 from \$9.58.

Total Recommendations Recommendation Changes

Broker Recommendation Breakup

Broker Rating Order Company New Rating Old Rating Broker Upgrade 1 ALS LIMITED Buy Neutral Deutsche Bank 2 BLUESCOPE STEEL LIMITED Buy Neutral Ord Minnett 3 BRAMBLES LIMITED Buy Neutral UBS 4 CHARTER HALL RETAIL REIT Neutral Sell Macquarie 5 OROTONGROUP LIMITED Neutral Sell Citi 6 RESMED INC Buy Neutral Ord Minnett 7 TOX FREE SOLUTIONS LIMITED Buy Neutral Morgan Stanley 8 VICINITY CENTRES Buy Neutral Ord Minnett 9 WESTERN AREAS NL Neutral Sell Citi 10 WESTERN AREAS NL Neutral Sell Deutsche Bank Downgrade 11 AIR NEW ZEALAND LIMITED Neutral Buy Macquarie 12 BENDIGO AND ADELAIDE BANK LIMITED Sell Buy Citi 13 BENDIGO AND ADELAIDE BANK LIMITED Sell Neutral UBS 14 BLUESCOPE STEEL LIMITED Neutral Buy Credit Suisse 15 BRAMBLES LIMITED Sell Neutral Credit Suisse 16 CIMIC GROUP LIMITED Sell Neutral Deutsche Bank 17 ERM POWER LIMITED Sell Neutral Morgans 18 ERM POWER LIMITED Sell Neutral Macquarie 19 ERM POWER LIMITED Neutral Buy Citi 20

GPT Neutral Buy Macquarie 21 NATIONAL STORAGE REIT Neutral Buy Ord Minnett 22 NORTHERN STAR RESOURCES LTD Neutral Buy Macquarie 23 SANDFIRE RESOURCES NL Neutral Buy Citi 24 SCENTRE GROUP Buy Buy Ord Minnett 25 SPOTLESS GROUP HOLDINGS LIMITED Neutral Buy Citi 26 VILLAGE ROADSHOW LIMITED Neutral Buy Citi 27 WESTFIELD CORPORATION Sell Buy Macquarie Recommendation Positive Change Covered by > 2 Brokers Order Symbol Company New Rating Previous Rating Change Recs 1 CSL CSL LIMITED 64.0% 29.0% 35.0% 7 2 WSA WESTERN AREAS NL -7.0% -36.0% 29.0% 7 3 SDA SPEEDCAST INTERNATIONAL LIMITED 100.0% 75.0% 25.0% 4 4 BLD BORAL LIMITED 50.0% 33.0% 17.0% 4 5 CQR CHARTER HALL RETAIL REIT -50.0% -67.0% 17.0% 6 6 SYD SYDNEY AIRPORT HOLDINGS LIMITED 29.0% 14.0% 15.0% 7 7 APN APN NEWS & MEDIA LIMITED 80.0% 67.0% 13.0% 5 8 VCX VICINITY CENTRES -30.0% -40.0% 10.0% 5 9 RMD RESMED INC 79.0% 71.0% 8.0% 7 10 PGH PACT GROUP HOLDINGS LTD 42.0% 40.0% 2.0% 6 Negative Change Covered by > 2 Brokers Order Symbol Company New Rating Previous Rating Change Recs 1 EPW ERM POWER LIMITED -67.0% 33.0% -100.0% 3 2 BEN BENDIGO AND ADELAIDE BANK LIMITED -79.0% -36.0% -43.0% 7 3 AHY ASALEO CARE LIMITED 33.0% 67.0% -34.0% 3 4 CIM CIMIC GROUP LIMITED -100.0% -67.0% -33.0% 3 5 WFD WESTFIELD CORPORATION 42.0% 75.0% -33.0% 6 6 SGM SIMS METAL MANAGEMENT LIMITED -7.0% 21.0% -28.0% 7 7 VRL VILLAGE ROADSHOW LIMITED 50.0% 75.0% -25.0% 4 8 AQG ALACER GOLD CORP 60.0% 80.0% -20.0% 5 9 NST NORTHERN STAR RESOURCES LTD 40.0% 60.0% -20.0% 5 10 RRL REGIS RESOURCES LIMITED 31.0% 44.0% -13.0% 8 Target Price Positive Change Covered by > 2 Brokers Order Symbol Company New Target Previous Target Change Recs 1 BSL BLUESCOPE STEEL LIMITED 11.966 9.986 19.83% 7 2 SGM SIMS METAL MANAGEMENT LIMITED 12.387 11.017 12.44% 7 3 CSL CSL LIMITED 116.479 108.990 6.87% 7 4 RMD RESMED INC 9.556 9.078 5.27% 7 5 BLD BORAL LIMITED 6.333 6.143 3.09% 4 6 CIM CIMIC GROUP LIMITED 19.867 19.293 2.98% 3 7 SDA SPEEDCAST INTERNATIONAL LIMITED 4.445 4.333 2.58% 4 8 SFR SANDFIRE RESOURCES NL 6.320 6.164 2.53% 8 9 WSA WESTERN AREAS NL 2.573 2.514 2.35% 7 10 BEN BENDIGO AND ADELAIDE BANK LIMITED 10.821 10.750 0.66% 7 Negative Change Covered by > 2 Brokers Order Symbol Company New Target Previous Target Change Recs 1 VRL VILLAGE ROADSHOW LIMITED 4.500 5.055 -10.98% 4 2 APN APN NEWS & MEDIA LIMITED 3.290 3.628 -9.32% 5 3 STO SANTOS LIMITED 4.613 4.763 -3.15% 8 4 EPW ERM POWER LIMITED 1.150 1.183 -2.79% 3 5 AHY ASALEO CARE LIMITED 1.533 1.567 -2.17% 3 6 NST NORTHERN STAR RESOURCES LTD 4.260 4.280 -0.47% 5 7 ANZ AUSTRALIA & NEW ZEALAND BANKING GROUP 29.175 29.306 -0.45% 8 Earning Forecast Positive Change Covered by > 2 Brokers Order Symbol Company New EF Previous EF Change Recs 1 WSA WESTERN AREAS NL 3.149 0.187 1583.96% 7 2 SFR SANDFIRE RESOURCES NL 53.220 39.438 34.95% 8 3 STO SANTOS LIMITED -4.395 -6.593 33.34% 8 4 S32 SOUTH32 LIMITED 30.248 25.559 18.35% 7 5 SGM SIMS METAL MANAGEMENT LIMITED 59.727 52.111 14.61% 7 6 BSL BLUESCOPE STEEL LIMITED 104.100 96.357 8.04% 7 7 BHP BHP BILLITON LIMITED 176.389 164.585 7.17% 8 8 CSL CSL LIMITED 402.231 377.709 6.49% 7 9 GNC GRAINCORP LIMITED 60.677 57.910 4.78% 6 10 SDA SPEEDCAST INTERNATIONAL LIMITED 17.308 16.597 4.28% 4 Negative Change Covered by > 2 Brokers Order Symbol Company New EF Previous EF Change Recs 1 EPW ERM POWER LIMITED -2.550 7.450 -134.23% 3 2 AMP AMP LIMITED 13.643 19.513 -30.08% 8 3 VRL VILLAGE ROADSHOW LIMITED 23.625 28.975 -18.46% 4 4 SXY SENEX ENERGY LIMITED -12.817 -11.000 -16.52% 6 5 OSH OIL SEARCH LIMITED 10.102 11.819 -14.53% 8 6 EVN EVOLUTION MINING LIMITED 16.780 19.474 -13.83% 7 7 WFD WESTFIELD CORPORATION 34.785 38.773 -10.29% 6 8 NST NORTHERN STAR RESOURCES LTD 35.578 38.504 -7.60% 5 9 BXB BRAMBLES LIMITED 57.511 60.300 -4.63% 7 10 BLD BORAL LIMITED 35.080 36.166 -3.00% 4 Technical limitations

If you are reading this story through a third party distribution channel and you cannot see charts included, we apologise, but technical limitations are to blame.

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Uranium Week: Momentum Builds

The spot uranium price last week booked its eighth consecutive week of positive or neutral price changes.

By Greg Peel

Last week market participants gathered in Washington for the annual Nuclear Supply Forum, a week which typically ensures light trade on uranium markets.

But not this time. Industry consultant TradeTech reports seven transactions conducted in the spot market totalling 900,000lbs U3O8 equivalent. Prices rose steadily over the week, taking TradeTech's weekly spot price indicator up US75c to US\$24.50/lb - its highest price since last September.

Last week marked the eighth consecutive week of positive or neutral price changes. The spot uranium price is now 38% above its December low of US\$17.75/lb. It sounds impressive, but we really are coming off a very low base. A twelve-year low to be precise.

Positive momentum is being carried, TradeTech suggests, since Kazakhstan announced a 10% reduction in state production in 2017 earlier in the month, due to low prices. On the other side of the coin, the Husab Uranium Mine in Namibia - ten years in development - last week produced its first concentrate.

Husab production will not hit the spot market, given an agreement to exclusively supply majority shareholder China General Nuclear Power Co in 2017. While that's good news, it also takes CGNC demand out of the equation.

BHP Billiton's ((BHP)) December quarter production report, released last week, noted a 30% drop in uranium production at the company's Olympic Dam mine in South Australia in the first half FY17. This was not a case of another major producer deciding to curtail production, but rather a result of maintenance work and South Australia's infamous state-wide electricity blackout, that cut off supply to the mine for two weeks.

There were no transactions concluded in uranium term markets last week. TradeTech's term price indicators remain unchanged at US\$22.00/lb (mid) and US\$30.00/lb (long).

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The Short Report

Guide:

The Short Report draws upon data provided by the Australian Securities & Investment Commission (ASIC) to highlight significant weekly moves in short positions registered on stocks listed on the Australian Securities Exchange (ASX). Short positions in exchange-traded funds (ETF) and non-ordinary shares are not included. Short positions below 5% are not included in the table below but may be noted in the accompanying text if deemed significant.

Please take note of the Important Information provided at the end of this report. Percentage amounts in this report refer to percentage of ordinary shares on issue.

Stock codes highlighted in green have seen their short positions reduce in the week by an amount sufficient to move them into a lower percentage bracket. Stocks highlighted in red have seen their short positions increase in the week by an amount sufficient to move them into a higher percentage bracket. Moves in excess of one percentage point or more are discussed in the Movers & Shakers report below.

Summary:

Week ending January 26, 2017

Last week saw the ASX200 regain the 5700 mark before dropping back once more, in a week punctuated by the Australia Day holiday.

In last week's Report I voiced my suspicions that a jump to 13.8% shorted for Super Retail Group ((SUL)) from under 5% prior could well be a blip in the ASIC data and not accurate, as often occurs, given no new news had emanated from the company.

Last week Super shorts were recorded as 4.8%.

Stop Press: After a seeming eternity, Metcash ((MTS)) has dropped out of the elite 10% plus shorted club. Only just, to 9.7%, but the supermarket retailer/wholesaler had been an incumbent at the top of the table for years, and often number one most shorted, so it's worth noting. The company had been seen as loser in the Woolies/Coles price war and from the incursion of Aldi, but since the acquisition of Home Hardware the market has taken a brighter view of the stock.

As of last week, Aconex ((ACX)) was second most shorted stock to Myer by a mere 0.1ppt at 16.0%. After issuing a profit warning, this week saw Aconex shares plunge -45% in one day.

Sirtex Medical was another stock to suffer a share price drop last week, after receiving a thumbs up for its SIR-spheres product from the US. But immediately the share price recovered. Last week Sirtex shorts rose to 6.2%

REA Group ((REA)) had jumped into the table at 6.1% shorted from under 5% the week prior, but last week jumped back out again. REA has a track record of beating earnings forecasts, and will report later this month.

Nickel miner Western Areas has been jettisoned by investors since the lifting of the Indonesian nickel ban. Now quite a familiar member of the 10% plus shorted club, Western Areas has seen at least some profits taken with a fall to 11.1% from 12.1%.

Weekly short positions as a percentage of market cap:

10%+

MYR 16.1 ACX 16.0 TFC 11.6 VOC 11.1 WSA 11.1 VOC 11.8 NEC 10.5

Out: MTS

9.0-9.9%

MTS, WOR, SYR In: MTS

8.0-8.9%

NWS, MYX, HSO, BAL, FLT, NXT

In: BAL, NXT

7.0-7.9%

MND, DOW, ISD, ORE, RWC, MYO, EHE, AWC, BEN, MTR

In: RWC, BEN, MTR Out: BAL, NXT

6.0-6.9%

IVC, SGH, BGA, GTY, JHC, PRU, SRX, SEK, CSV

In: BGA, SRX Out: BEN, RWC, MTR, PDN, REA, CTD, BKL

5.0-5.9%

AAD, OFX, RIO, MSB, IFL, GXL, BKL, OSH, CTD, WOW, A2M, CSR, GEM, TGR, PDN, AWE, KAR, ILU, IGO, AAC, IPH, CAB

In: BKL, CTD, PDN, GXL, TGR, IPH Out: BGA, SRX

Movers and Shakers

Sirtex Medical ((SRX)) last week received a recommendation from the US National Comprehensive Cancer Network for its SIR-spheres product in treating colorectal cancer. Sirtex' shares promptly opened -7% lower.

Did someone read the press release incorrectly? By day's end the share price was almost back where it began. Or maybe it was a so-called "fat finger", where a trader accidentally enters the wrong price into the online system. What we do know is that last week, shorts in Sirtex rose to 6.2% from 5.1% the week before.

The share price of nickel miner Western Areas ((WSA)) is one of the most volatile on the market, reflecting the nickel price status of the most volatile of the base metals. But the trend for the miner had been up in 2016 thanks to the Indonesian ban on nickel ore exports, which led analysts to believe the global nickel surplus would be cleared.

The nickel price was further aided by increased Chinese stainless steel demand, and by another export ban - this time from the Philippines in an environmental crackdown.

The Philippines' environmental audit of nickel mines has been a slow one, but the government is soon to release its list of perpetrators. But Indonesia has since announced a qualified lifting of its own ban, leading mining analysts to slash the earnings forecasts of nickel miners, despite being as yet unsure as to the extent of the impact.

Having long sat at more than 10% shorted, Western Areas has seen at least some profit-taking. Last week shorts fell to 11.1% from 12.1%.

ASX20 Short Positions (%)

To see the full Short Report, please go to [this link](#)

IMPORTANT INFORMATION ABOUT THIS REPORT

The above information is sourced from daily reports published by the Australian Investment & Securities Commission (ASIC) and is provided by FNArena unqualified as a service to subscribers. FNArena would like to make it very clear that immediate assumptions cannot be drawn from the numbers alone.

It is wrong to assume that short percentages published by ASIC simply imply negative market positions held by fund managers or others looking to profit from a fall in respective share prices. While all or part of certain short percentages may indeed imply such, there are also a myriad of other reasons why a short position might be held which does not render that position "naked" given offsetting positions held elsewhere. Whatever balance of percentages truly is a "short" position would suggest there are negative views on a stock held by some in the market and also would suggest that were the news flow on that stock to turn suddenly positive, "short covering" may spark a short, sharp rally in that share price. However short positions held as an offset against another position may prove merely benign.

Often large short positions can be attributable to a listed hybrid security on the same stock where traders look to "strip out" the option value of the hybrid with offsetting listed option and stock positions. Short positions may form part of a short stock portfolio offsetting a long share price index (SPI) futures portfolio - a popular trade which seeks to exploit windows of opportunity when the SPI price trades at an overextended discount to fair value. Short positions may be held as a hedge by a broking house providing dividend reinvestment plan (DRP) underwriting services or other similar services. Short positions will occasionally need to be adopted by market makers in listed equity exchange traded fund products (EFT). All of the above are just some of the reasons why a short position may be held in a stock but can be considered benign in share price direction terms due to offsets.

Market makers in stock and stock index options will also hedge their portfolios using short positions where necessary. These delta hedges often form the other side of a client's long stock-long put option protection trade, or perhaps long stock-short call option ("buy-write") position. In a clear example of how published short percentages can be misleading, an options market maker may hold a short position below the implied delta hedge level and that actually implies a "long" position in that stock.

Another popular trading strategy is that of "pairs trading" in which one stock is held short against a long position in another stock. Such positions look to exploit perceived imbalances in the valuations of two stocks and imply a "net neutral" market position.

Aside from all the above reasons as to why it would be a potential misconception to draw simply conclusions on short percentages, there are even wider issues to consider. ASIC itself will admit that short position data is not an exact science given the onus on market participants to declare to their broker when positions truly are "short". Without any suggestion of deceit, there are always participants who are ignorant of the regulations. Discrepancies can also arise when short positions are held by a large investment banking operation offering multiple stock market services as well as proprietary trading activities. Such activity can introduce the possibility of either non-counting or double-counting when custodians are involved and beneficial ownership issues become unclear.

Finally, a simple fact is that the Australian Securities Exchange also keeps its own register of short positions. The figures provided by ASIC and by the ASX at any point do not necessarily correlate.

FNArena has offered this qualified explanation of the vagaries of short stock positions as a warning to subscribers not to jump to any conclusions or to make investment decisions based solely on these unqualified numbers. FNArena strongly suggests investors seek advice from their stock broker or financial adviser before acting upon any of the information provided herein.

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The Wrap: Asset Managers And The Consumer

Weekly Broker Wrap: market outlook; Allianz & QBE; asset managers; Australian consumer; Vocus Communications.

-UBS: Global reflation seen favouring cyclical stocks, expressly resources -Sale of QBE to Allianz would be an obvious positive for IAG, SUN -MS: Stock picking rather than the cycle to drive Oz consumer stocks

By Eva Brocklehurst

Market Outlook

A backdrop of global reflation should favour cyclical stocks, UBS believes. The broker considers this best expressed through an overweight holding in resources and a selection of cyclical/reflation stocks within the market ex resources. While holding both domestic and globally exposed industrial stocks, the broker envisages better earnings growth trends in global/US exposed stocks and, domestically, consumer discretionary names are highlighted.

The broker is neutral on banks, while non-bank financials are considered reasonably attractive. The reflationary backdrop, the broker believes, is supportive of equities, although these do not look particularly cheap in an absolute sense. Risks over coming months would appear to be either policy risks or the growth pulse fading.

Allianz & QBE

Ord Minnett has analysed speculation regarding a potential bid for QBE Insurance ((QBE)) by Allianz. Speculation has been forthcoming from media both domestic and offshore. The broker notes QBE has emphatically denied it is in discussions with any party regarding a takeover, although Ord Minnett believes this statement does not preclude there being interest on the part of Allianz.

There are synergy considerations, the broker acknowledges, but, that said, QBE already has a very efficient capital-two-premium ratio which is an offset from its increased use of reinsurance. The broker suggests it may be hard for Allianz is to prioritise an acquisition of QBE ahead of possible acquisitions of companies like Generali. The broker believes any sale of QBE to Allianz, was an obvious positive for shareholders, would be also positive for Insurance Australia Group ((IAG)) and Suncorp ((SUN)).

Asset Managers

Credit Suisse observes, in the December quarter, funds under management amongst the listed managers increased on average 3.7%. Growth was primarily driven by positive market movements and complemented by net inflows. Most managers delivered growth of 2-4%, with the exception of very strong growth from Magellan Financial ((MFG)), up 10%, and a contraction in funds under management for Platinum Asset Management ((PTM)), down -1%.

Credit Suisse downgrades Henderson Group ((HGG)) earnings estimates on the back of weaker retail fund flows but retains an Outperform rating. BT Investment Management ((BTT)) is upgraded to Neutral, following a significant fall in its share price since mid December. The broker believes the stock justifies its price/earnings premium - now trading at a 27% premium to its UK peers - because it has consistently delivered inflows above its peer group and successfully executed on its global expansion plans.

Australian Consumer

Domino's Pizza Enterprises ((DMP)), Metcash ((MTS)) and Treasury Wine Estates ((TWE)) are Morgan Stanley's highest conviction, overweight stocks in the Australian consumer sector, with Woolworths ((WOW)) and Flight Centre ((FLT)) the highest conviction underweights. The broker believes stock picking rather than the cycle will drive Australian consumer stock performances.

Feedback on retail trading over Christmas suggests it was better than feared but the broker notes the cycle is cooling. While downgrades are more likely than upgrades, the broad-based weakness the broker had previously predicted is now considered unlikely.

Housing-linked categories are envisaged faring better than apparel, while supermarkets continue to be affected

by discounting and deflation. The broker expects 2017 to be a more difficult year than 2016, as leading housing indicators soften while the savings rate is lower and income growth is weak.

Morgan Stanley identifies five potential surprises for the current year, where the outcome has a higher probability than the market is currently pricing in. The surprises include Amazon not entering the Australian marketplace in 2017 and suppliers outperforming the supermarkets. The broker also lists discretionary retail enduring lower earnings and a de-rating, driving under-performance in the segment. The other two surprises involve Domino's Pizza shares going above \$100 and Flight Centre shares going below \$20.

Vocus Communications

Macquarie has initiated coverage on Vocus Communications ((VOC)) with an Outperform rating and \$5.30 target. The broker notes the company has assembled a collection of core fixed line assets, with its fibre network now extending beyond metro to include extensive inter-capital city backhaul in Australasia, and soon-to-be international transit assets between Perth and Singapore.

The broker believes there is scope for ongoing profitable on-net growth in the corporate and government segments with opportunities for market share gains in the consumer segment as the NBN rolls out. Capital expenditure demands are likely to remain high because of the nature of the business but the broker expects them to taper from peak levels in FY17 and FY18.

While the issues regarding the number of acquisitions made recently were largely cleansed at the AGM update in November, the broker acknowledges potential risk to corporate sales momentum and also the risk of medium-term earnings deterioration at Commander. The next catalyst will be the first half result and Macquarie is looking for confirmation that the operating outlook has not deteriorated since the AGM and the company is on track to achieve its synergy targets.

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Solid Outlook Prevails For Credit Corp

Brokers flag a solid outlook for debt purchaser and consumer lending business, Credit Corp.

-Record level of debt purchasing in the first half -Loss of market share considered only minor -Double-digit earnings growth expected over FY18-19

By Eva Brocklehurst

Debt ledger purchaser and consumer lending business Credit Corp ((CCP)) has proved its consistency in the first half. Growth divisions are on track, consumer lending should hit pro-forma returns and the US division is expected to become profitable in the second half.

The company has confirmed FY17 earnings guidance for profit of \$53-55m, which would represent 15-20% growth on FY16. Forward flow tenders awarded late in FY16 and the secondary market purchase of NCML's ledger book underpinned a record level of debt purchasing (PDL) in the first half.

Canaccord Genuity suggests investors may have been confused by commentary that signalled market share losses occurred, relating to the unsuccessful renewal of some forward flows. While pricing has improved on some of the larger forward flows, where capital requirements limit competition, some of the smaller business has been aggressively bid away by peers, the broker suspects.

This raises one of the questions frequently put to the broker, as to whether the company is close to reaching a ceiling in terms of market share. The loss of some market share in the half year is suspected to be unfairly interpreted as proof that this is the case. The broker asserts that losing out on a handful of small tenders, as others have opted to bid more than the most efficient operator in the market is prepared to pay, should be a comfort to investors.

Earnings guidance has been maintained, while the company's purchasing for the year is locked in, and there should be limited downside to the full-year result. The broker suggests, if competitors over-reach on price, there will be a benefit from reduced purchasing competition and returns should improve going forward.

Pricing Discipline Maintained

Hence, the company's willingness to maintain pricing discipline in recent weeks should mean free cash flow is generated over the next six months, leaving it well placed to capitalise on pricing improvements and any fall-out in the industry. The broker, not one of the eight monitored daily on the FNArena database, has a Buy rating and \$19.23 target.

Adjusted operating earnings growth of 15.2% was in line with Morgans' forecast, driven by 13.5% growth in cash collections, lending interest revenue, and a slight improvement in the operating margin, to 58.5%.

A second half earnings uplift is expected to be driven by the lending division, which will benefit from seasonally lower volumes and lower planned marketing expenditure. Morgans also expects a meaningful uplift in cash collections, which provides confidence the company is tracking towards the top end of guidance.

Morgans expects solid double-digit organic earnings growth over FY18-19. While stock is trading at the top end of its longer term price/earnings ratio, at around 14.8, the broker believes the premium can be sustained, because of the growth profile and track record. Morgans retains an Add rating and \$19.90 target.

Profit Guidance Easily Attainable

Ord Minnett retains an Accumulate rating on the stock, with an \$18 target. The broker expects profit guidance to be relatively easily attained, given the committed pipeline of PDL acquisitions, the increased head count and a seasonal pause in consumer lending growth. While gearing is elevated, at its highest level since FY09, management has highlighted a significant increase in operating cash flow is expected in the second half.

To fund the medium-term growth aspirations, management has signalled it is actively exploring extending existing finance arrangements as well as asset-backed financing options. Ord Minnett remains cautious on the outlook for the US business, but expects further regulatory clarity over the next six months. Moreover, the upside remains a relatively cheap option for shareholders, in the broker's opinion.

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ASX200: 6000 In Sights

By Craig Parker, asset manager, Moat Capital

You don't always get exactly what you want. I mentioned I would've like to have seen our market down between the 5500 - 5600 level before taking off again. It seems the breakout on the S&P500 I mentioned to look out for was mid-week and off we go again from around the 5600 level. We are now looking to the 6000 level in the coming weeks barring any adverse event. On the positive side, Iron ore has consolidated above the \$80 mark and Oil is also providing some further consolidation above the \$50-barrel mark.

From a technical point of view Iron Ore does have some bearish divergence on the RSI weekly chart. This could be something to keep an eye on in the next week or two as this could affect the S&P/ASX 200 slightly. Another indicator to look out for is our volatility index which has broken down forming a clear peak on the daily chart lower than the previous which, confirms possible further movement down in the current downtrend. This can be good news for our market in the short term as the VIX reaches lower and subsequently equities reach higher.

At the moment, it is still all about Trump and it will be interesting to see how much geopolitical tension the markets can bear in the coming weeks and months when Trump's protectionist policies and attitudes are fully on display. This excludes the home-grown issues he is going to face, further dividing the nation on his anti-science, immigration and feminist issues. Interesting times. The world is apparently flat again.

ASX200 daily

Iron ore weekly

S&P500 daily

ASX200 VIX

Authorised Representative Sentinel Private Wealth AFSL 344762

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