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INTERNATIONAL

The Case For Emerging Markets Investment Part I

While traditional structural issues may weigh on some investors, many others seek out emerging markets for a core holding, by virtue of sheer size and growth prospects.

-Current investment thesis for emerging markets
-The potential for a global synchronicity tailwind
-Will traditional structural issues impact?

By Mark Woodruff

Emerging markets (EM) are considered a core allocation for many investors seeking long-term growth.

In aggregate, emerging market economies account for around 50% of global economic activity (GDP) and contribute 75% of global economic growth. In looking ahead to 2040, it is estimated that EM economies will have an output that is more than double that of the developed world.

These markets have experienced dramatic growth and transformation over the last three decades. The emerging market investment universe used to represent a mere 1% of the global equity market in the late 1980s, and now accounts for around 11%.

Over time the asset class has evolved and now Asia dominates EM in terms of economic growth, consumption and trade. Within the benchmark MSCI Emerging Market Index, Asia's representation currently comprises more than 75%, with the increasing inclusion of China's domestically listed A-shares driving changes in benchmark weights.

This shows an EM investment is very much a play on Asia, and indeed China, which comprises 43% of the benchmark. The next largest EM countries are Taiwan which accounts for 13% of the index, South Korea 12% and India 8%, while the residual 24% is a long tail of smaller markets led by Brazil at 4%.

Some of above percentages can be misleading as South Korea and Taiwan play an outsized role in the index relative to the size of their economies. Other countries are poised to grow, and the drivers of that growth within EM are changing.

New sources of growth include industry leaders in innovation, which is occurring in areas such as communication services, retail, entertainment and digital platforms. Healthcare is also moving to the fore and becoming a larger part of the opportunity set. From a sector perspective, consumer discretionary at 22% is the largest sector in EM, followed by IT at 18% and financials at 17%.

Asian consumers are driving video streaming, e-commerce and other forms of digital consumption. These are growing rapidly alongside other forms of service-driven consumption.

In Part I of this article, FNArena explores the current investment thesis for emerging markets and what traditionally drives or inhibits their performance.

Part II of this article looks at currency and equity opportunities, within separate emerging market countries. The aim with equities is to identify those industries, sectors and companies that should benefit from tailwinds.

While China is covered in this article, FNArena considered the country warranted separate and more detailed attention, given the country's size relative to the benchmark index.

See *Are Chinese Shaes A Unique Opportunity?*
(https://www.fnarena.com/index.php/2021/01/29/are-chinese-shares-a-unique-opportunity-part-i/)

Before going any further, let's examine what defines an emerging market and who are the EM member countries.

Definitions

EM countries are those that are striving to become advanced countries, and are generally on an economically disciplined track to become more sophisticated. This includes increased fiscal transparency, a focus on production, developing regulatory bodies and exchanges and acceptance of outside investment.

Although some large countries like China and India have high production and industry, other factors like low per capita income or a heavy focus on exports qualify them as being within EM.

According to the Morgan Stanley Capital Emerging Market Index, 24 developing countries qualify as emerging markets. These include China, Taiwan, South Korea, India, Brazil, Russia, Indonesia, Malaysia, Greece, Hungary, Mexico, Pakistan, Chile, Colombia, Czech Republic, Egypt, Peru, Philippines, Poland, Qatar, South Africa, Thailand, Turkey, and United Arab Emirates.

At times this article will refer to Asia Pacific (APAC) which includes East Asia, South Asia, Southeast Asia, and Oceania. Clearly there is a great deal of geographical crossover and some differences between APAC and EM constituent countries. The reader should bear in mind that the likes of Australia, Hong Kong, Singapore and Japan, while included in APAC, are not EMs.

Complicating matters even further, broker research often refers to EEMEA. This stands for Eastern Europe, the Middle East and Africa. This incorporates countries such as Russia, Greece and Hungary for example, which are also captured within the EM definition and includes many countries that are not.

The current investment thesis

Wilsons Advisory sees a **clear inflection point for the global and EM growth cycle** extending at a minimum through 2021 and 2022. The covid-19 situation is now improving in a broad range of emerging markets and their recoveries are gaining momentum.

In 2021 the effect of global vaccine rollouts, ultra-low interest rates and a weaker US dollar should lead to a sharp rebound in EM growth.

Morgan Stanley agrees that EM growth will rebound sharply in 2021 for the reasons cited by Wilsons. They also believe growth will be aided by a widening US current account deficit and the accommodative domestic macro policies of EM (ex China).

The vaccination of the vulnerable population (and not the higher bar for achieving herd immunity) will be the key for reopening the economies, along with the advent of rapid testing. The reopening of economies will even extend to include the covid-19-sensitive sectors.

After a prolonged period in which EM countries have faced a series of cyclical challenges, the Morgan Stanley feels **macro stability is now in check**. With the covid-19 situation improving in a broad range of EMs, their pace of recovery is catching up.

Adding to the impetus, the pace of the China growth recovery has been impressive with China already surpassing pre-covid-19 levels of economic activity. This, in combination with a period of above-trend growth for the global economy, should assist EM growth.

DBS Group also suggests Asia’s success in dealing with the pandemic will pave the way for relative economic and financial outperformance in 2021. Pandemic management is not the only reason behind the optimism. Three additional factors support the Singaporean financial services group’s thesis.

Firstly, regional trade intensity has risen as the world requires substantially more remote work and education, medical supplies and home improvement.

Asia stands ready to meet the global craving for screens, computers, sound equipment, PPEs, computer desks, home gym gear etc. Already the pick-up in export demand is visible in the region’s purchasing managers indices (PMIs). It’s also evident in the order books of electronics and a wide range of consumer goods exporters.

The second reason for likely outperformance is the relatively high levels of foreign exchange reserves, savings and investor participation in the region.

DBS doesn’t see the markets worrying about debt or current account sustainability in the region next year. In fact, there’s expectation for a great deal of interest among external investors to pick up Asia’s **positive yielding bonds and high growth stocks**. They also cite investor interest in gaining **exposure to regional currencies** that are likely to appreciate or remain stable.

The final reason for outperformance is that China will enter 2021 with a tailwind, having made up for the pandemic-induced loss in output. The APAC region presently has deeper trade and investment ties with China than ever before. DBS forecasts that the country is looking at 7% growth in the coming year.

This is further buoyed by sentiment-improving initiatives like asset market liberalisation, the Regional Comprehensive Economic Partnership (RCEP) free trade agreement and the e-RMB (Chinese crypto). The reader may be aware the People’s Bank of China will be the sole issuer of the digital yuan, initially offering the digital money to commercial banks and other operators.

This potential Chinese growth is considered partly due to the country enjoying strong domestic travel and production. In addition, some dissipation of the tension with the US as the Biden administration gets started will assist growth.

<u>Trade war – from headwind to tailwind</u>

The impact of the US-China trade war on the entire Pan-Asian region is perhaps best seen in the relative performance of equity markets over the last couple of years.

With US President Donald Trump increasing tariffs against China from the start of 2018, the MSCI Asia Pacific Index underperformed the S&P500 index over the subsequent two years by approximately -30%. Over this period, global investor appetite for emerging markets and Asian equities dropped materially due to the drag on potential portfolio performance.

The relevance of the win by President Biden and the Democratic Party in the 2020 US election should therefore not be underestimated for Pan-Asian equities. Current Democratic Party policy statements appear to place less emphasis on unilateral actions against China (e.g. tariff escalation), and more on US domestic policy, particularly given the need to support the US economy out of recession.

Longlead Capital Partners see the election of President Biden as leading to a period of greater predictability with respect to US-China geopolitics. Contentious issues such as intellectual property protection for US companies will likely remain sources of tension between the countries, however the impact of such negotiations is likely to be far less material for listed Pan-Asian companies.

Already there are signs that sentiment is improving towards Pan-Asian equities, with tariff risks taking on a lower level of importance for the region, and recent performance suggestive of an ongoing catch up underway.

Longlead awaits the decision of a Biden administration with respect to existing tariffs. It remains a possibility that trade becomes a tailwind for Pan-Asian equities in 2021, and not the headwind of the past few years.

Is there evidence of global synchronicity?

A global synchronous recovery, with both developing markets (DM) and EM growth accelerating in the same year, has taken place about 12 times over the last 40 years, the last one in 2017.

As it is a relatively common occurrence, it's beholden upon us to **examine how DM economies are performing, as a potential indicator of the future for emerging markets**.

Morgan Stanley forecasts global growth of 6.4% for 2021, which is above 5.4% consensus expectation. Despite the sharp gyrations in economic output over six quarters, the global economy is estimated to return to the path it would have followed absent the covid-19 shock.

This projection stands in stark contrast to the consensus, which worries the pandemic will have a bigger impact on private sector risk appetite and hence global growth. However, consumers have driven the recovery so far and investment growth (a reflection of the private corporate sector's risk tolerance) is bouncing back as well.

Morgan Stanley notes the pandemic shock was exogenous, private sector balance sheets and the financial system were in good shape coming into this recession, and we had a policy response that was timely, coordinated and sizeable.

The combination of these three factors meant that **private sector risk appetite, which is crucial in any recovery, has remained relatively healthy**.

Moreover, even as economies are well on their recovery paths, policy-makers are keeping extremely reflationary policies in place as they try to mitigate the impact on unemployment.

Morgan Stanley's US economists highlight that large fiscal transfers and lower spending (constrained by lockdown measures) in the initial months of the pandemic have led households to run up large amounts of excess savings.

Relative to the pre-covid-19 baseline, households had saved an extra US$1.2 trillion as of September 2020, which translates to 8.5% of 2019 personal consumption expenditure (PCE) levels. This **savings buffer should provide an additional cushion for consumer spending** in the coming months.

To an extent a similar dynamic is also under way in Europe, and Morgan Stanley expects consumer activity to surge again once restrictions are lifted.

The investment bank expects a broad-based recovery, both by geography and sector, to take hold from March/April onwards. Driving this synchronous recovery will be a more expansive reopening of economies worldwide and the extraordinary monetary and fiscal support now in place.

Global GDP, already at pre-covid-19 levels (based on seasonally adjusted GDP levels), continues to accelerate and is on track to resume its pre-covid-19 trajectory by the second quarter 2021. The broker expects the US to return to its pre-covid-19 level by the fourth quarter.

Capital expenditure to take over the running from the consumer

A key feature of any self-sustaining recovery is the capex cycle, and Morgan Stanley expects a vibrant capital expenditure (capex) cycle to follow. While consumers have been leading the recovery so far, the damage to the capex cycle has not been as bad as feared.

A continued recovery in consumption and the fact that private sector risk attitudes are healthy mean that the bank expects a vibrant capex cycle to kick off from the second quarter of 2021.

The bank is already seeing some early signs of a pick-up in capex. High-frequency indicators including capital goods production and imports are bouncing back in a similar fashion as aggregate economic activity.

It's instructive to look at US and Asia, where recoveries are arguably more advanced than other economies.

US capex plans have risen to their highest level since August 2019 and core capital goods orders are running ahead of shipments. This suggests a revival in business capex is already under way.

In China and other trade-dependent economies, stronger external demand conditions should also lead to a rise in capex, particularly in the private manufacturing sector.

Indicators show recovery already underway in Emerging Markets

EM (ex China) initially lagged the recovery and is now catching up, according to Morgan Stanley. The covid-19 situation is improving across a large swathe of individual emerging markets, allowing policymakers to reopen their economies further, even before a vaccine was available.

Trade-dependent economies like Korea and Taiwan are already well into their recoveries. A number of indicators for the large, more domestic demand-oriented economies like India and Brazil, have recently exceeded pre-covid-19 levels and are registering positive year-on-year growth.

China's real retail sales are now growing by 2.4% per annum, while Brazil's real retail sales were 7.7% above pre-covid-19 levels in September 2020. Auto sales in India were also growing by 20%.

This strong momentum should continue into 2021, with EM growth rising to 7.4%, higher than the consensus expectation of 6.3%. In particular, Morgan Stanley has a more constructive view on Asia ex Japan and Latin America as compared to the consensus.

EM real exports were already growing on a year-on-year basis in September 2020, helped by a recovery in end demand in key markets and the restocking cycle. These external demand conditions are likely to remain supportive, Morgan Stanley, helped by improving demand in the US and China.

How do domestic policies in both the US and China impact upon emerging markets?

In combination with easy monetary policy, fiscal stimulus will remain an active policy tool in 2021 (and likely beyond) in the US, forecasts Morgan Stanley.

These reflationary policies will also have key implications for global growth, and especially for emerging markets, because of **a shift in the savings-investment balance**.

In contrast to the last cycle, a rise in government deficits will not be offset by increased domestic saving in the private sector, particularly households, for two reasons. Firstly, households do not face the same deleveraging pressures as they did coming out of the GFC. This is evidenced by private debt/GDP ratios having remained stable for some time. Secondly, low interest rates provide little incentive for households to save, explains the investment bank.

The resulting widening of the current account deficit, which occurs when a country spends more on imports than it receives on exports, will be another factor driving the US dollar down.

Continued low real rates and a widening US current account deficit will provide a reflationary impulse for the rest of the world, especially EMs. This is because **EM economies are likely to benefit most from the increase in import demand**, as they account for roughly two-thirds of the US trade deficit.

Chinese infrastructure and manufacturing spend to lift wider EM

Given China's relative size, its economic health has a strong impact on other Asian economies. Strategists at DBS Group highlight how Indonesia, Malaysia, South Korea, and Taiwan benefit considerably from the China growth dynamic.

China will maintain policy support in the near term as policymakers are working on restoring health to the labour market. China's credit impulse has reached its highest level since mid-2016. This will especially impact upon **infrastructure spending,** which will flow through to other EM economies in the coming quarters, notes Morgan Stanley.

Moreover, private consumption is expected to bounce back sharply in 2021 as households gain confidence and will begin to draw down their precautionary savings. The availability of a vaccine will lead to the full resumption of contact-based activities, providing a fillip to consumption growth.

Favourable external demand conditions should also translate to a **rebound in private manufacturing sector capex**, meaning that private sector activity looks set to recover in a fully-fledged manner.

Lower-for-longer EM interest rates

Morgan Stanley presents a compelling rationale as to why **interest rates can stay low for longer than usual in EM**, thereby heightening the impact of monetary policy. Ultimately, this should be reflected in a pick-up in domestic credit demand.

Traditionally, external pressures have cut short EM easing cycles. This time around, with the Federal Reserve on hold for the foreseeable future and the **outlook for a weaker US dollar**, EM central banks will face little pressure to raise rates to protect the exchange rate or prevent foreign capital outflows.

While conceding structural issues linger in the background, Morgan Stanley believes they are not likely to be constraints on the cyclical recovery. In addition, a cyclical recovery will actually help to alleviate some pressures, such as on public finances, as tax revenues rebound alongside nominal GDP growth.

Caution on EM debt levels

On the severity of structural issues, JPMorgan begs to differ, based on concerns over EM debt levels. The covid-19 shock has led to the largest annual increases in both EM government and private sector debt as a percentage of GDP. They are now at new all-time highs.

JPMorgan concedes governments needed to respond to this health crisis with fiscal support, and future debt levels may have been worse had they not done so. However, it's considered the overall levels of debt across EM will leave a legacy that market participants will be grappling with through the next cycle.

Defaults in 2020 were mostly due to previous debt build-ups, rather than debt caused by the pandemic itself, explains the investment bank. Given EM government debt levels were already elevated in some countries coming into this crisis, the EM sovereign bond default rate reached a 20-year high in 2020.

EM private sector credit to GDP has also increased to an all-time high. At 147% of GDP, emerging markets private sector credit to GDP is now around developing markets averages of 161%. However, China has a large impact on the overall level given its very high levels of debt. EM (ex China) is only 90%, notes JPMorgan.

EM debt increases over the past year have been driven by corporate domestic loans rising, with household debt also increasing, but to a lesser extent. The international EM corporate bond market is small compared to the EM private sector debt stock. That does not mean investors should ignore the risks that this large debt stock may leave for EM countries.

Some of the large EM countries will be left with large debt levels dominated by local debt. Steepening curves in Brazil and South Africa reflect this concern, concludes JPMorgan.

Oxford Economics is similarly concerned, and believes a timid fiscal response to the pandemic threatens to entrench weak demand and low inflation, which should keep bond yields low for most emerging markets. While a large-scale EM funding crisis will likely be averted this year, a large debt burden means vulnerabilities will remain.

On balance, Oxford believes EM governments have probably erred too much on the side of fiscal caution amid fear of market reaction. EM fiscal packages have been less ambitious than those of advanced economies, despite the larger downward revisions to activity of EM countries.

EM funding needs are considered colossal, but there is evidence of easing funding conditions for most. EM countries remain broadly on track to issue enough bonds to meet 2020 needs and Oxford Economics sees limited evidence of funding snowballing into shorter maturities.

Varying debt concerns by country

Despite Asia Pacific (APAC) leading the global recovery from the pandemic, the overall positive trend masks noticeable divergences within the region. Research by Oxford Economics shows APAC's robust growth is built on the strong performance of a handful of economies, whereas others are still struggling with virus-related setbacks.

Northeast Asia continues to lead the recovery within the region, while **India**'s GDP was still expected to be -8% below the pre-pandemic level for the fourth quarter 2020.

In Asia, DBS Group notes that corporate bond defaults were far smaller than in the US. **Hong Kong and Korea** remarkably saw no defaults, while **India and Indonesia** reported a lower quantum of defaults compared to 2019.

Robust loan growth in North Asia and a greater reliance on bank financing in South Asia, supported by loan moratoriums, have helped Asian firms tide through this difficult period better, explains DBS.

China was the outlier in Asia as corporate bond defaults rose by over 50% in 2020. However, this accords with a fast-growing bond market, with the ratio of defaults to maturing bonds having in fact eased from 2019. Nevertheless, a rise in state-owned enterprise (SOE) defaults mean investors should stay cautious on Chinese SOEs that are heavily leveraged and marginally profitable, cautions DBS.

Markets are becoming more judicious in assuming the availability of local government support, with the government having declared that it will foster more market-based credit decisions.

China's real estate sector is a particularly key credit market driver, given a large proportion of Chinese developer credits, and high leverage in some firms.

The pandemic has fallen unevenly across different sectors and different parts of the labor force, and the same is seen in Chinese residential sales. Eastern China is slated to record its fastest annual sales growth since 2016, while Central and Western China will see their worst growth, outlining truly divergent real estate credit risks by geography.

For **India**, the bond market has been through a wrenching journey due to a prolonged credit crunch for non-banking financial companies (NBFC), explains DBS Group. However, credit stress is now considered nearer the end than the beginning.

Incremental new bond defaults in 2020 are close to India's pre-crisis average. While moratoriums have helped to staunch cash flow difficulties, subdued new defaults do give reason to hope that most non-performing assets are already weeded out.

Meanwhile, the largest Indian private sector banks have also raised their capital buffers to ample levels, supported by a stirring equity market. DBS believes Indian credit may finally enter a more confident phase in 2021. This is provided asset quality outcomes meet expectations, covid disruptions subside and India's sovereign rating is held steady at investment grade.

Oxford Economics utilises an in-house funding vulnerability scorecard. This places **South Africa and Brazil** at the most vulnerable end of the spectrum given their large fiscal measures and high financing needs. The scorecard also highlights countries that are behind track in terms of the required bond sales this year (**Philippines, South Africa, Malaysia**) and those with shallow domestic markets (**Indonesia, Mexico**).

Warning of potential contagion

Despite the likelihood of relative outperformance, Asia does not exist in a vacuum. Many developing economies are in precarious positions, weakened by the economic cost and social toll of the pandemic, notes DBS Group.

Several economies in Africa, Latin America, and Middle-East could see deep economic contraction and financial crisis next year, weighed down by debt, funding deficit, and loss of investor confidence.

Low rates and ample liquidity could cause housing prices to soar, as well as push the valuation of a wide array of financial assets. These trends will inevitably accentuate inequality in many parts of the world.

Prosperity is not necessarily progress. A rise in the stock market, an increase in housing wealth and a steady increase in average income can mask several downsides. These include rising inequality, anxiety about future job prospects, burden of debt, health and education outcomes and social cohesion.

Debt will loom large, and financial sector stability may be undermined as frothy valuations have their comeuppance, cautions DBS Group.

Three risks to the positive EM scenario

Firstly, the scenario around the trajectory of the virus may worsen or there are adverse vaccine developments or delays.

There may also be some uncertainty around the fiscal policy path. Political gridlock may prevent fiscal stimulus, leading to downside for Morgan Stanley's growth forecasts.

The final risk is the flip side of the second point mentioned above. There may be a quicker-than-expected inflation overshoot (compared to Morgan Stanley's base case), leading to a disruptive shift in Federal Reserve policy expectations.

The key issue for inflation is the uncertainty around the natural rate of unemployment in this cycle. If the accelerated restructuring of the economy means a higher non-accelerating inflation rate of unemployment (NAIRU), the highly reflationary policies will lead to wage and inflation pressures emerging earlier. The NAIRU is the specific level of unemployment in an economy that doesn't cause inflation to increase.

Policymakers have made clear their intent to enact policies that would help lower-income households, either via direct fiscal action or indirectly by allowing the economy to run 'red-hot'.

By the first quarter 2021, GDP levels in the US would have reached 98.7% of pre-covid-19 levels, yet policy support will likely remain very accommodative.

With policymakers maintaining highly reflationary policies to get back to pre-covid-19 rates of unemployment quickly, wage pressures and inflation will pick up from the second half of FY21. Morgan Stanley expects underlying core personal consumption expenditure (PCE) inflation to rise to 2% in the second half and to overshoot from the first half of 2022. This comes with the risk that it happens ahead of schedule.

Conclusion

Several investment managers can see a rationale for investing in emerging markets at present. In a perfect world, as investors we would all like the optimum time to enter the market.

Based on some strategists' warnings of debt contagion and traditional structural issue in emerging markets, an investor may be tempted to apply some caution. However, for many investors, both private and professional, emerging markets are considered a core allocation when seeking seeking long-term growth.

Part II of this article looks at currency and equity opportunities, within separate emerging market countries. The aim with equities is to identify those industries, sectors and companies that should benefit from tailwinds.

AUSTRALIA

More Babies Brightens Baby Bunting Outlook

Baby Bunting has navigated the issues of 2020 well and several factors are expected to underpin a robust outlook over the next few years

-One of the few retailers likely to grow earnings sustainably in FY22
-Upside could come from increased number of births over FY21-22
-Growth potential extended with store openings planned in NZ

By Eva Brocklehurst

There are several factors that are expected to support Baby Bunting ((BBN)) over the next couple of years, including containment of the pandemic in Australia, more flexible working conditions and a relatively resilient economy.

The company was one of the few Australian retailers not to benefit from JobKeeper or material reductions in rent, which Morgan Stanley points out will mean less onerous numbers are being cycled over FY21.

While the broker upgrades estimates by 7%, if comparable momentum continues, significant upside is envisaged. Revenue rose 16.6% in the first half with operating earnings (EBITDA) up 29% and net profit up 43%.

Online sales grew 100% and private-label/exclusive comprised 39% of the total. Citi envisages like-for-like sales momentum will ease back to 7% over the rest of the second half, relative to the increase of 18.5% experienced in the first six weeks. Ord Minnett agrees the rate of growth will moderate progressively, particularly over May/June.

No guidance was provided but Macquarie considers this understandable in the light of retail uncertainties, and this category is typically more resilient. The supply chain impact was larger than the broker anticipated, given the extended lockdowns in Melbourne but also the tightness of container availability for a lot of importers.

In Macquarie's view, Baby Bunting is one of the few retailers likely to sustainably grow earnings in FY22. The mix of home delivery versus click & collect has changed since the end of the most onerous period of Victorian lockdowns, and data mining signals the importance of the physical store network for the category.

Baby Boom?

Upside could come from the increase in the number of births - as Citi quotes 12-16 week pregnancy-related ultrasounds increased by 16% in 2020. On the other hand, the pandemic is likely to suppress the demand for resale of used products.

Macquarie notes demographers have pointed to a fall in birth rates from the pandemic but considers this information "backward looking". A decline in fertility rates for the six months to December is considered typical of periods of economic downturn and declining job security.

Hence, a rebound in economic activity should mean improvements in official fertility rates will come through over 2021. Morgans suspects, too, that this time the traditional concerns regarding unemployment that prevail during pandemics, which causes birth rates to fall, could be less of an issue in Australia.

While the stock's valuation is at a premium to retail peers, the broker points out the growth profile is far superior and a heightened birth rate could provide a robust backdrop over the next year or so.

Margins

First half gross margin expanded 41 basis points to 37.4% although higher costs and increased online sales caused this to pull back in the second quarter. Gross margin is expected to expand further, nevertheless, as new private-label and exclusive hard goods are launched.

There are also lower-margin nappies and consumables sales to be be cycled from March-April 2020. Higher-margin toys and games are back in stock following supply issues in the second quarter.

Morgan Stanley notes the company has accelerated its share of business and returned the benefits of scale to its value proposition. The broker remains bullish on the outlook for margins although suspects reinvestment may be limiting operating leverage and this can be an issue for investors.

The company is investing ahead of the curve in terms of price, logistics, e-commerce and private label. This delays the potential for margin expansion.

Another concern is the increase in working capital which is ahead of previous years. The broker suspects gross margins were likely understated in the first half, given higher freight costs as well as the high-margin categories being affected by supply disruptions. A new private-label brand in hard goods is planned in the second half, expected to be accretive to margin.

New Zealand

Baby Bunting plans to increase its number of stores in Australia to over 100 and will roll out its first New Zealand store in FY22, targeting a network of more than 10 stores. Macquarie notes Baby Bunting is now just halfway through its planned store roll-out and the growth potential has now been extended with the additional NZ target.

Morgans expects the current NZ plan will be modestly dilutive to profit in FY22 before becoming profitable in FY23. The broker assumes four NZ stores are rolled out per annum and 14 are in place by FY25. Morgans assumes gross margins will be in line with Australia with a slightly lower margin over the ramp-up phase.

Forecasts for FY23 are lifted by 8%, and even more so in future years, to include the roll-out in New Zealand, and the broker upgrades to Add from Hold. FNArena's database has five Buy ratings. The consensus target is $6.25, suggesting 15.8% upside to the last share price. This compares with $5.28 ahead of the results.

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AUSTRALIA

Short-Term Uncertainties Weigh On Mirvac

The timing of residential developments and re-leasing of office space are uncertainties confronting Mirvac Group. Is this why guidance was underwhelming?

-Guidance for FY21 underwhelms
-More investors returning to the residential market
-Office outlook uncertain

By Eva Brocklehurst

Mirvac Group ((MGR)) is being sustained by its large pipeline of potential developments and the diversity and quality of its projects, although timing is of critical concern because of the uncertain demand for office rentals.

UBS concludes the business is a quality domestic urbanisation stock that has sufficiently re-based market earnings and is now positioned for strong growth in the BTR (build-to-rent) sector.

Nevertheless, Mirvac has been cautious in its guidance and this has caused brokers to question why. First half results were down -22% on the prior first half, albeit better than the previous half and ahead of most estimates. FY21 guidance is for earnings of 13.1-13.5c per security with distributions of 9.6-9.8c.

Citi notes guidance implies second half earnings will decline sequentially, in contrast to market expectations. A lower contribution from apartments appears to be the major cause along with more minor factors such as the rolling off of JobKeeper and increased regulatory costs. The broker is inclined to believe guidance is merely conservative rather than "soft".

UBS points out there are risks around the settlement of the locomotive workshops that could slip into FY22. Moreover, **at the Pavilions development the broker estimates around 8-10% of apartments have defaulted and the launch of Green Square was underwhelming with only 24% pre-sold**

The broker reduces earnings estimates by -5-10% for FY22-24 to reflect more conservative retail/office income, higher corporate costs and the sale of the Travelodge hotels. On the other hand, long-term projects such as Waterloo and Harbourside should provide investors with more confidence as the value of these projects emerges over the coming year.

Macquarie also found the outlook for the second half disappointing, given the size of the beat to the first half estimates. There is only one active office development at the moment and that is 80 Ann Street, Brisbane. The asset has been 73% pre-leased, presenting a risk to the remainder.

Nevertheless, the broker notes Brisbane has fared better regarding pandemic restrictions to date. The development pipeline has made limited progress on conversions and Mirvac is yet to finalise the desired capital structure for its industrial developments.

Macquarie is also wary of retail expiries as 15% of leases expire in the second half. Additional re-leasing will continue to be challenging, in the broker's view, prior to the roll-out of a covid-19 vaccine.

Credit Suisse considers Mirvac well-placed to ride out a downturn, with the capacity to fund its diverse developments. Rent collection has improved and the impact of the pandemic on earnings has moderated.

The business is experiencing strong sales of developments in Victoria while Queensland and Western Australia have moderated and more investors are returning to the market, which has helped sales volumes.

UBS anticipates a strong residential market will broaden and push up pre-sales. In contrast to several years ago when pre-sales surged and regulators attempted to put a lid on the home investor market, no macro prudential policy tightening is anticipated in the next 6-9 months.

Build-To-Rent

Mirvac has identified around $8.8bn in office/mixed-use potential. Focusing on the industrial side, Credit Suisse notes the BTR strategy is somewhat unclear, as to whether Mirvac can develop and hold 100% on the balance sheet or need to find capital partners.

Regardless the broker considers any meaningful earnings contribution is a longer-term proposition. UBS considers Mirvac well-placed, given the 2200 units across five projects that will settle in the current year.

Yet Morgan Stanley notes these will predominantly be land lots, rather than apartments, and this means the dollar value and earnings will decline in the second half and stay low in FY22.

In order to achieve its 5000 units target by FY22, Mirvac now needs to lease up existing secured projects while introducing external capital, and the broker suggests partners should come on board as operational success becomes evident.

UBS also calculates two projects per year will be needed in order to reach 5000 BTR units over four years and Mirvac can earn upside of 5% in FY23 if capital partners worth 50% can be introduced on two projects at a 4% yield.

Office

Mirvac has noted a number of large office tenants with mandates for new space in 2026-27. Macquarie is also interested in the comment that **floor space requirements have not shrunk as a result of working from home - at this stage**.

The broker suspects there is downside risk in that area, which may be partially offset by the growth in employment in white-collar personnel. Office leasing spreads were 15% with incentives at 21%. Across the portfolio, Mirvac believes that it is around 1% over-rented at current market rents. On the positive side, Macquarie notes only 10% of leases will expire over the next 18 months.

Morgan Stanley does not find the office outlook that convincing, without the clarity on future active profits. The average duration of new leases of 3.5 years and the supposedly strong tenant enquiries for 2026-27 does not excite at this stage.

The broker finds the stock relatively inexpensive and it could offer investors with a longer-term horizon the opportunity to benefit from a late-cycle re-opening trade.

FNArena's database has three Buy ratings and three Hold. The consensus target is $2.62, suggesting 11.6% upside to the last share price. The dividend yield on FY21 and FY22 forecasts is 4.1% and 4.5%, respectively.

FNArena is proud about its track record and past achievements: Ten Years On

AUSTRALIA

Aurizon Expands Horizons

Coal volumes and the stoush with China hold few concerns for Aurizon Holdings, which is expanding its presence in bulk ports

-Bulk earnings continue to surprise to the upside
-Coal volumes being managed with diversion to India
-Record interim dividend, robust dividend yield

By Eva Brocklehurst

Aurizon Holdings ((AZJ)) is moving up the supply chain via port services as coal contracted volumes continue to decline. While coal exports are expected to be well-managed over the short term, heightened environmental concerns are likely to have a longer impact.

Coal volumes were -4% lower in the first half, which exposes the fixed cost leverage in this division where earnings (EBIT) were down -17%. UBS points out that FY21 forecasts have declined by less than -10% over the past 12 months and a significant amount of the decline will be recovered in a couple of years under the revenue cap provisions.

Hence, the broker considers the share price underperformance is overdone, although potentially quantifies the ESG (environment, social and governance) de-rating of the stock. The company has lifted FY21 earnings guidance by 4% at the mid-point, on the back of a non-recurring $40m catch-up in Wiggins Island revenue as well as gains from short-term grain volumes.

Citi upgrades estimates to reflect the recognition of the Wiggins Island fees and forecasts are revised to the mid point of the new $870-910m guidance. Nevertheless, the broker decreases FY22 numbers because of expected declines in coal contract volumes.

Jarden envisages further upside to earnings and cash if the schedule of fees for Wiggins Island is approved by the Queensland Supreme Court during 2021. The broker assesses bulk earnings are continuing to surprise to the upside and the division can increase its earnings over the forecast period, anticipating a 3-year earnings growth rate of 3.4% out to FY24.

Macquarie points out bulks offset the drag on earnings from coal, noting additional iron ore contracts, yet remains concerned that **contracts for bulks are competitive and often involve smaller volumes** that could easily be moved by truck.

Contract length is also a lot shorter, creating renewal risk. The company is managing the risk, with the cascading of older coal equipment that still has useful life and this development will lower the risk of stranded assets.

TrainGuard

TrainGuard, which has been developed to improve safety, has experienced some delays. Deployment on the Blackwater line is scheduled for the second half of FY22. Macquarie suggests benefits will not occur before 2023 but should be material.

Coal Re-allocation

Beyond FY21, Credit Suisse suspects conditions will normalise and coal volumes will be redirected to destinations other than China, filling a global supply gap, should geopolitical tensions persist.

Aurizon calculates around 10mt of the 18mt being exported to China has already been re-allocated. Forecasting volumes to China is difficult but a cut of -5% appears reasonable to UBS. Management remains confident of volume growth in FY22 as a result of better contracted utilisation.

Citi has a relatively optimistic view on the short-term outlook for coal but still expects contracted volumes will decline. In FY22 NSW and south-east Queensland contracted volumes are expected to decline to 63mt from 71mt.

To date, it appears the coal originally bound for China has been diverted to India, with that country importing a record high 6.75mt from Australia in January. There has also been an uptick in coal imports to Japan, the largest importer of Australian coal.

Moreover, Citi notes Aurizon's major coal customers have relatively unchanged production plans. Macquarie still expects miners will reduce their contracted capacity to meet the independent review of track capacity on the network rather than spend money to increase capacity.

The broker anticipates coal volumes will return and in tandem improved productivity will emerge. System volatility on a weekly basis means it's impossible for Aurizon to downsize. Hence, **volumes must recover for productivity to also resume an upward trend** and this is likely to be driven by a resumption of trade with China.

Macquarie assesses medium-term demand for coal is secure, underpinned by steel manufacturing growth in India as well as thermal demand for power generation in Asia.

Acquisitions

Morgan Stanley notes the company is building on the momentum in bulk with its acquisition of Conport, a copper and zinc bulk export terminal at Newcastle. This is the second acquisition in this segment following the Townsville Bulk Storage and Handling acquisition in March 2020.

Citi considers the acquisition a signal that the company intends to move up the supply chain into port services, although Aurizon already has a major share of the bulks market and further acquisitions are expected to be small. Management has indicated customers are receptive to integrated port/rail solutions and this underpins its decision.

There was no expansion of the buyback and, while disappointed, Macquarie was not surprised, given the potential to bid for OneRail. OneRail remains an opportunity for a step-change, particularly in bulk ports where it would add scale to the South Australian network.

No formal sale process has commenced but the broker notes Aurizon is interested, although points out there may be some competition concerns. The Acacia Ridge sale proceeds will not contribute to additional buybacks as this was already included in surplus capital flagged some years ago.

Credit Suisse suspects **further acquisitions may be behind the decision not to extend the buyback program** at this stage and expects bulks will constitute a higher proportion of the business in future. Aurizon has indicated there is $900m in excess capital that can be deployed.

Citi considers the relative resilience of the business and capital management are appealing although a sustained recovery in coal market conditions is required for a re-rating back towards historical multiples.

As an increasing number of funds are inhibited by carbon concerns, Citi is taking a more pragmatic view of its valuation and incorporating an ESG discount into multiples. As a result the broker downgrades to Neutral from Buy on valuation and reduces the target by -16.8%.

A new record interim dividend was announced and the company continues to pay out 100% of earnings. A$1.2bn distribution to shareholders is on track as a result of the legal separation of the network. UBS considers the dividend yield sustainable which should appeal to yield-interested investors.

Jarden believes the recent decline in the share price presents a good risk/reward for investors over the next 12 months and the longer-term risks for coal demand are reflected in estimates.

The broker, not one of the seven stockbrokers monitored daily on the FNArena database, raises the rating to Overweight from Neutral and lifts the target to $4.30. The database has four Buy ratings and two Hold. The consensus target is $4.75, suggesting 17.2% upside to the last share price. The dividend yield on FY21 and FY22 forecasts is 7.0% and 7.3%, respectively.

AUSTRALIA

Improved Confidence Yet To Play For Altium

Risks implied in second half forecasts suggest Altium is not completely out of the woods, although longer-term growth appears solid

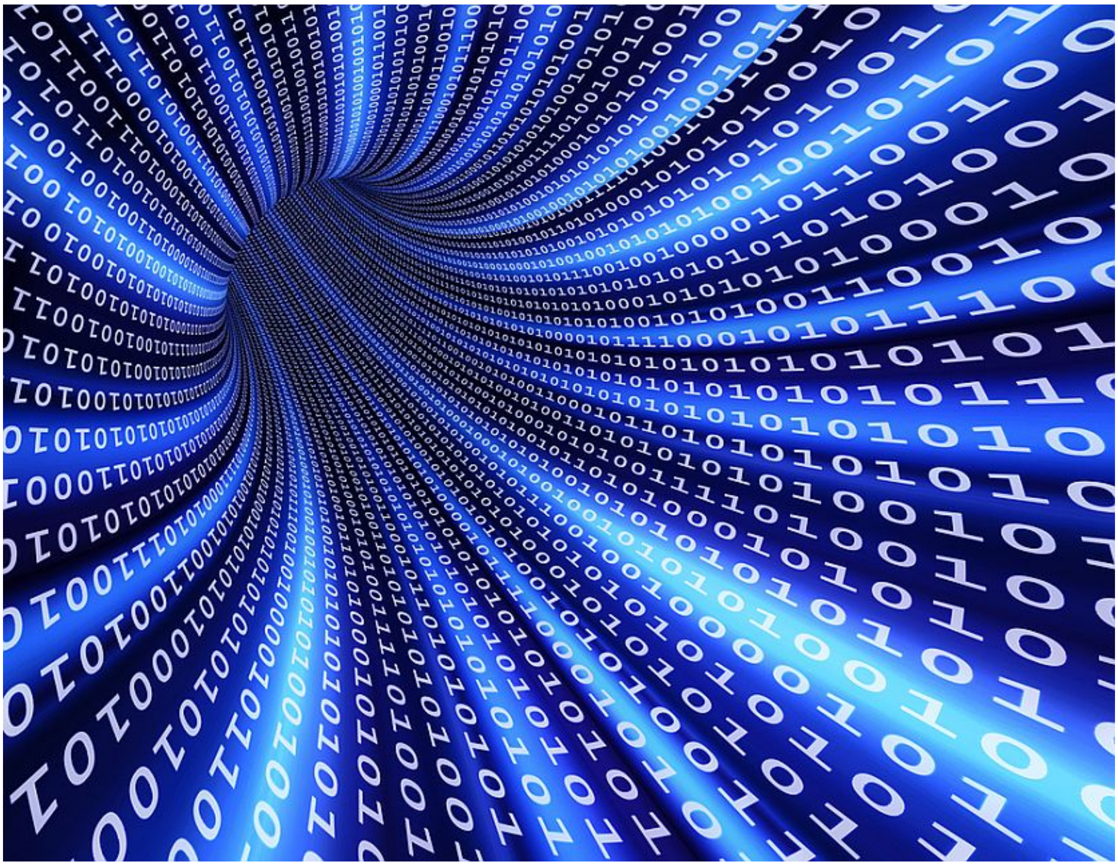
-Set to take advantage of renewed confidence as vaccines roll out
-Margins likely to remain under pressure until FY23
-Flight Path outlook assumes 10-20% from future acquisitions

By Eva Brocklehurst

Software designer Altium ((ALU)) is experiencing an improvement in customer confidence, although with the pandemic yet to come under control across the globe brokers are wary that accelerating momentum in earnings and better margins could be some time away.

While FY21 guidance has been retained at the lower end of the former range, with revenue of US$190-195m and operating earnings of US$70-76m, a large acceleration is required in the second half, Credit Suisse points out.

There are improving signs from customers and company specific drivers, such as reduced discounting and a reorganisation of sales, but the broker did not find enough incrementally positive news to be completely comfortable and suspects risks may well weigh on investor sentiment. Over the longer term, nevertheless, the growth outlook appears solid and M&A is also likely to feature.



The business is exposed to high levels of non-recurring sales that underscores the cyclical nature of the stock, and therefore headwinds such as the pandemic are meaningful.

Credit Suisse attributes a weak first half to the pandemic and believes the business is well set to take advantage of the roll-out of vaccines over 2021. Citi agrees **new business will improve over 2021 as the vaccine rolls out and demand becomes more settled**, particularly among small-medium enterprises. The broker awaits further details on the FY25 targets post the sale of Tasking.

UBS places forecasts at the lower end of both revenue and operating earnings guidance, noting the skew for earnings implied for the second half is 56-57%.

Still, the broker also observes some tailwinds, such as pent-up demand that is likely to return as business confidence improves. Significant discounting occurred in the second half of FY20 and first half of FY21 and a return to more normal pricing levels should also occur.

UBS remains confident in the company's product leadership as well as the upside from long-term aspirations, upgrading to Buy from Neutral.

Moreover, the balance sheet should allow Altium to take advantage of M&A opportunities in the medium term. The adoption of Altium 365 has accelerated, with 4500 companies and 9400 active users on the platform, up 83% on the prior corresponding half.

As a result, UBS expects there will be a modest impact on revenue in the short term but a reduction subscription lapse rates. The company remains confident in the aspirational target of US$500m in revenue and 100,000 subscribers. A recurring revenue outlook of 80% is maintained for FY25.

Furthermore, there is upside to this target, in the broker's view, via the **accelerating momentum in China along with a more automated sales and a subscription platform** that should drive lower churn. Catalysts also exist in the commercialisation of the relationship with Dassault.

Margins

Macquarie assesses future margins will remain under pressure before turning around in FY23. The company expects FY21 margins of 37-39%, which implies a material pick-up in the second half.

A combination of both operating improvements as well as an acceleration in earnings as the pandemic eases is likely. Yet Macquarie has limited confidence that margins will rebound materially over that time frame.

The 2025 Flight Path strategy is guiding to a declining earnings margin trend until FY23 and, while this may well be the path to longer-term profitability, Macquarie believes investors will require further data regarding Altium's ability to transition to a cloud-based platform.

Hence, there are limited catalysts to justify investment on the basis of a margin turnaround that may be two years away. The revised Flight Path outlook, significantly, now assumes 10-20% from future acquisitions, which Morgan Stanley considers a negative as it entails a step up in risk.

There are three Buy ratings and three Hold on FNArena's database. The consensus target is $33.33, suggesting 13.8% upside to the last share price. Targets range from $30 (Macquarie) to $37 (Morgan Stanley).

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AUSTRALIA

BHP Group Hits The Dividend Nerve

BHP Group is bullish about the outlook for key commodities, confirming its view with a surprise increase in its interim dividend

-Growth in underlying earnings largely driven by rising prices
-Climate change policy in US could mean restricted oil & gas
-Market likely to focus on cash returns

By Eva Brocklehurst

BHP Group ((BHP)) has delivered what everyone likes, a surprise increase to its interim dividend. Nevertheless, underlying net profit missed consensus expectations because of write-downs at Turrum and higher depreciation at Yandi.

Morgans highlights the company was more bullish regarding the outlook for commodities compared to its view at the August results, assessing durable growth was stemming from growing population and improved living standards in key consuming economies.

Growth in underlying earnings was largely driven by rising prices, as copper equivalent production was broadly flat. Iron ore and copper accounted for 70% and 25% of group operating earnings, respectively.

Macquarie lowers earnings estimates after incorporating the results because of increased depreciation expenses in petroleum, iron ore and Queensland coal, while noting these changes are essentially non-cash.

The broker flags US president Joe Biden's signing of orders to tackle climate change which could mean restrictions are placed on oil & gas developments in the US, although this should impact future developments rather than the status quo.

The company has retained a commitment to metallurgical (coking) coal and petroleum, noting the complimentary nature of metallurgical coal with China's steel industry. Morgan Stanley points out, unlike iron ore, the business is diversified across several markets and demand should remain resilient for a high-quality coking coal product.

Credit Suisse compares the latest commentary with August, noting currency is providing a headwind on the cost side while commodity and economic commentary is far more assertive.

The broker remains positive about the iron ore business but prefers Rio Tinto ((RIO)) at current prices as BHP's oil interests remain one of the risks to a relative call. The company has taken note of environmental (ESG) concerns regarding oil & gas but envisages solid fundamentals in the industry. That said, only high-returning investments will be made and mature assets are likely to be divested.

Meanwhile, a process to exit assets at the BMC joint venture in NSW thermal coal as well as the Cerrejon assets will commence, although no timeframe was provided. A final decision will be made based on circumstances at the end of a two-year period.

In copper, BHP is looking at medium-term debottlenecking options at Olympic Dam. Morgan Stanley notes the capital costs of the expansion will be significant and this implies low returns. Consequently, there needs to be a shift in productivity assumptions to improve the economics.

At Escondida, a high prevalence of coronavirus in Chile has hampered the business although the roll-out of vaccines is accelerating. Citi believes with deployment of the vaccine underway a major downside risk has been substantially mitigated. Moreover, the scale of stimulus being applied in several economic zones should mean solid support for a recovery.

Cost guidance is unchanged, although higher unit costs at Queensland coal are anticipated because of low volumes and maintenance. Capital expenditure guidance was lifted to US$7.3bn, given the higher Australian dollar.

Distribution

BHP paid out 85% of net profit, equal to 100% of free cash flow in the first half. This translated to an interim dividend of US$1.01. Management stated its minimum 50% net profit pay-out policy remains in place but flexibility is retained for higher distributions based on market conditions.

Morgans was certainly surprised by the strength of the pay-out and is not concerned if the dividend exceeds free cash flow as BHP Group has signalled the decision was also based on net debt being at the lower end of its preferred range.

Credit Suisse asserts the capacity for even further strong capital returns exists in August and this should keep investors on the front foot. The company will continue to assess its cash returns on an interim basis.

Ord Minnett believes **BHP has set the dividend scene for other large miners to follow.** The broker retains a positive investment view, based on an attractive valuation, high forecast returns and the global growth backdrop.

Jansen

UBS suspects the company's desire to diversify and grow into future-facing commodities, including potash, could mean Jansen is readily approved. Potash has become one of BHP Group's preferred future-facing commodities along with copper and nickel.

The project has ticked the requirements for scalability and low costs but the final test will be whether Jansen can compete with internal growth options, in Morgan Stanley's view, as well as the desire to return cash to shareholders.

BHP is also assessing market dynamics in lithium, although its view has not changed given the product's flat cost curve and inability to generate significant economic rent. All up, short-term growth is likely to be limited and UBS asserts the market will focus on cash returns.

FNArena's database has four Buy ratings and three Hold for BHP Group. The consensus target is $47.18, signalling -4.1% downside to the last share price. Targets range from $42 (Credit Suisse) to $52 (Ord Minnett). The dividend yield, at present FX values, on FY21 and FY22 forecasts is 5.9% and 5.7%, respectively.

AUSTRALIA

Heightened Demand Plays into Ansell's Hands

Demand for protective gloves is unprecedented and Ansell is at the forefront of global supply. When will the market return to balance?

-Heightened demand for surgical gloves to remain
-Supply disruptions could still occur
-Yet may take time for PPE to return to balance

By Eva Brocklehurst

One of the few companies to benefit from the pandemic, Ansell ((ANN)) has delivered record organic sales and underlying earnings growth in the first half as demand for personal protective equipment (PPE) has been unprecedented.

Even with a strong earnings base in FY21, management is targeting growth of 6-12% and remains confident about demand for the medium term. This is supported by assumptions that, as the pandemic ebbs, global economic growth will accelerate.

Depressed industrial sectors should then recover and safety practices at both industrial sites and hospitals are now heightened, which is likely to play into the company's hands. Morgans believes pandemic has strengthened Ansell's earnings trajectory along with customers looking for long-term supply agreements and amid likely sector consolidation.

The company has upgraded FY21 guidance to US160-170c per share, which represents 51% skew to the second half. Ansell has switched to a pay-out ratio from a progressive dividend, leading to an unfranked US33.2c per share, ahead of forecasts.

In the second half volumes will be cycling a tough comparable yet UBS is confident guidance can be achieved, as normal seasonality favours the second half.

Surgical Gloves

Demand for surgical gloves should continue as the large elective surgery waiting lists are managed over

2021/22. Macquarie notes Ansell has secured new business in categories outside of traditional examination/single-use gloves via the bundling of products.

Examination/single-use glove revenue stood out in the half, up 47.5% amid pricing initiatives and a favourable mix. Pricing is expected to normalise in FY22 but remain above pre-pandemic levels. Growth was largely driven by volume increases and use outside the surgical setting, and demand expected to remain strong for several years as hospitals work through their backlog.

<u>Supply/Demand</u>

The main risk in Ord Minnett's view is the re-balancing of global examination glove supply that could mean **a sharp downward adjustment in price if the market moves into oversupply**. Ansell has taken advantage of some missteps by competitors, the broker notes, and lifted market share so this does place the business in a strong position as the world economy starts to recover.

Management has indicated supply disruptions could occur amid worsening shipping conditions and container availability. Ocean freight capacity is constrained and second half costs are potentially rising by around 100-300%. Increased raw material expenses are expected to be passed on.

The rolling out of a vaccine may signal the start of the decline in coronavirus but Credit Suisse suspects it will take years for PPE supply/demand to return to balance, given the behavioural changes required over the past 12 months.

Additionally, a recovery in mechanical use gloves and market share gains in surgical and chemical as well as more in-house manufacturing of single-use gloves should support earnings growth.

Morgan Stanley assumes leverage to increased demand for PPE over the short term although, while additional internal capacity may alleviate cost pressures, **competitor expansion plans underscore a degree of uncertainty**.

Ansell's additional capacity in Thailand is expected to double internal production volumes by FY22-23 compared with pre-pandemic levels. Ansell has also signed multiple long-term supply agreements with several global organisations, partners and hospital groups across countries such as the US, Canada, Brazil and Germany.

The company continues to invest in production of single-use gloves in-house, intent on reducing its reliance on third parties to around 50% from 80%. While the move is sound, Ord Minnett is cautious as it leaves the company more exposed if the market becomes oversupplied.

Still, management argues that demand and prices will remain above pre-pandemic levels and its focus on differentiation will protect from oversupply. Nevertheless UBS ascertains the longer term implications of demand on PPE are difficult to quantify.

Morgan Stanley finds several reasons to remain Overweight on the stock, including expectations for organic growth in FY21 to remain substantially above the 3-5% long-term target. There is also flexibility on the balance sheet, with US$381-564m in headroom for capital deployment.

Rising nitrile prices could pressure small manufacturers, the broker suggests, and this may lead to a more favourable industry structure post the pandemic. Moreover, given the company's view of the severe capacity constraints in PPE it is possible the tailwinds will extend into FY22.

FNArena's database has five Buy ratings and two Hold. The consensus target is $44.18, suggesting 13.4% upside to the last share price. Targets range from $38.30 (Macquarie) to $48.10 (Morgan Stanley).

AUSTRALIA

EML Payments Lights Up Reloadable Cards

EML Payments is showing promise, with the benefits of diversification becoming obvious in the first half

-PFS already proving its worth as an acquisition
-Substantial opportunities for reloadable cards in new verticals
-Upgrade potential as growth outlook becomes more assured

By Eva Brocklehurst

Payment solution provider EML Payments ((EML)) has delivered a much brighter outlook for gift and reloadable cards, given the past year has been dogged by uncertainties.

In the first half, general purpose reloadable (GPR) card revenue increased 313%, and remains core to the strong trajectory. Gift & Incentive (G&I) revenue of $35m was down -13%, affected by social distancing and weaker spending patterns.

Currency headwinds are significant, as around 90% of revenue is sourced outside of Australia, yet guidance for FY21 revenue of $180-190m and operating earnings of $50-54m is considered likely to be on the conservative side.

Canaccord Genuity points out EML has a history of tightening guidance to the top end throughout the second half. **The company has probably passed the worst and there should be a strong uplift in earnings performance throughout FY22-23,** with little in the way off incremental costs.

PFS (Prepaid Financial Services) is proving to be a great acquisition in Macquarie's view, having made a solid contribution in the nine months of ownership with a revenue of $38m. Synergies are not expected until FY23.

The G&I segment was materially affected by the pandemic and the temporary shutdown of shopping centres. Investors had been concerned that revenue would be severely weaker but in the end the company has proved resilient, particularly in light of the harsher lockdowns in Europe and the UK.

Assuming lockdowns are not extended, Macquarie suspects the top end of the guidance range for operating earnings is just a starting point, although tough conditions are likely to continue through to at least the third quarter.

The company has commenced the rolling out of new retail platforms for shopping centres in Europe, integrating both in-store and online selling of gift cards in anticipation of a recovery.

UBS believes the gift card environment can recover to around -20% below pre-pandemic levels by FY24, although there is plenty of upside risk to forecasts. The company can leverage the structural shift to digital payments and has a strong track record of growth.

The gift card business in shopping centres may retain some lingering uncertainty but it can also be a large driver of the upside post the pandemic. The half year featured the launch of Project Accelerator with the intention of integrating a number of the company's technologies along with its partners into one solution.

Canaccord Genuity notes the company is in a reinvestment phase with a $10-15m investment plan in technology over FY21-22. Organic growth has been complemented by accretive M&A and management will secure a debt facility in the second half to enhance liquidity.

Reasons To Be Bullish

EML is likely to be a beneficiary of the re-opening of shopping centre trade along with general consumer activity. The main risk Macquarie envisages is prolonged lockdowns and a failure to convert the sales pipeline. The broker maintains an Outperform rating with a $5.70 target.

UBS, which also has a $5.70 target and a Buy rating, considers the re-rating of the stock on the back of the first half results is likely to be the start of a growth story and there is further upgrade potential as the market becomes more comfortable with the multi-year growth story.

There were 79 new contracts gained in the first half and 64 new programs launched. UBS estimates the global prepaid card market was around $1.1tn in 2020 and growing at double digits.

Moreover, there is substantial opportunities for penetration in the GPR segment with application to new vertical markets. Wilsons remains constructive on the stock and considers FY21 will be a year in which the PFS acquisition will prove its value proposition.

Wilsons calculates GPR to be 53% of FY21 gross profit, with the shift to this segment resulting in a more resilient and less "lumpy" business. Meanwhile, the outlook for G&I is improving as vaccines become more readily available.

Earnings margin expansion remains plausible, in the broker's view, with more than $6m in synergies available and a strong balance sheet. Incremental traction at Project Accelerator is also a highlight and Wilsons retains an Overweight rating with a $5.41 target.

Estimates for operating earnings are ratcheted down in FY21 to allow for operating expenditure and increased investment and the broker assesses FY22 is likely to be the more "normal" year.

Canaccord oints out payments companies typically trade on large valuation multiples because of the recurring and higher margin revenue streams. A highly regulated industry also provides barriers to entry. Amid increasing medium-long-term earnings growth forecasts the broker raises its target to $5.50, maintaining a Buy rating.

ESG FOCUS

ESG Focus: The Virus And Shrinking Democracies

FNArena's dedicated ESG Focus news section zooms in on matters Environmental, Social & Governance (ESG) that are increasingly guiding investors preferences and decisions globally. For more news updates, past and future:
https://www.fnarena.com/index.php/financial-news/daily-financial-news/category/esg-focus/

2020 has seen the biggest global shrinkage of personal liberties during peacetime, but it's all about the global pandemic and last year's trend is not necessarily spelling doom and gloom for the world's democracies

ESG Focus: The Virus & Shrinking Democracies

-The global pandemic's seen the biggest global rollback of personal liberties during peacetime
-Autocratic leaders are using the pandemic as justification for further suppression of citizens
-Today just 23 nations - most in Western Europe - are deemed full democracies

by Ed Kennedy

The democratic model of government suffered a major setback in 2020 around the world.

That's according to the findings of The Economist's Democracy Index 2020. 70% of the countries included in the index saw a decline in the overall score, according to Agathe Demarais, Global Forecast Director, and Ana Nichols, Industry Operations Director, of The Economist's Intelligence Unit, the hosts of a recent webinar on the Index's findings.

The Good and Bad News in the Data

The Democracy Index measures each nation via the health of its electoral process, its civil liberties, the functioning of government, and related metrics.

2020's global average score on the Index hit an all-time low of 5.37 (out of 10). It's a regression upon the previous year's score of 5.44.

The vast majority of countries covered by the Index recorded a decline in their total score. When measured by their total average score, every region of the world also recorded a regression.

For those of us who live in free societies and would like to keep doing so, such statistics are very confronting. Yet a contextualisation of the data in combination with a recognition of 2020's unusual dynamics show that democracy's current condition is serious, but by no means terminal.

Nonetheless, the pandemic's emergence confirms there are a number of fractures in the current democratic model governments across the world use, just as autocrats are using the pandemic to their advantage in further restricting individual freedoms within their regimes.

The Campaign Pitch for Democracy

Advocates of the democratic model argue it's the greatest vehicle for empowering economic growth, especially in combination with a free market economic model.

With the right to protest shall come the right to bargain for higher wages and better working conditions, with the right to free speech corruption can be called out, and the ability for citizens to pursue private enterprise in lieu of operating in a planned economy encourages commercial innovation and upward mobility.

At no other time in history did the belief in the superiority of the democratic model have greater credence than in the 1990s. With the fall of the USSR in 1991, the decade saw democratic nations dominate the rankings of the world's biggest economies by GDP, with the USA accompanied by Japan, Germany, France, and the UK at the top of the table.

But the blistering economic growth of China in the years to follow -alongside a decline in trust in the democratic model - over a long period of time, but particularly since the post-9/11 era that saw the calamitous wars in Afghanistan and Iraq begin - affirms the 1990's was not the beginning of a long victory lap for the nations who advocate for a democratic model, but simply a brief intermission before resuming serious competition with the autocratic form.

The China Challenge

The prevailing wisdom for years among many academics, diplomats, and those of similar ilk was that the rising economic wealth of China would eventually pressage a period of democratic reforms.

Many in the Chinese government would argue their system is already a socialist democracy -one in which there is only one party but the capacity for diverse dialogue and lobbying within its inner sanctum- but the era President Xi Jinping has presided over since coming to power in 2013 certainly makes this claim ever more dubious.

Xi's fervour for further restricting civil liberties, quashing dissent and jailing opponents -under the auspices of a 'corruption crackdown'- means the Chinese government is missing many key freedoms and protections in its apparent performance of the democratic process.

But ultimately, the greatest challenge for democrats globally is not what the Chinese government is doing within its borders, but within its foreign policy alongside fellow advocates for the authoritarian model such as the Russian government.

Making an Effective Case

As Demarais and Nichols identified, a key challenge for the democratic model is the perception among everyday citizens their government is out of touch with their concerns.

In turn, even if they're attuned to the issues, they're unable to provide an adequate response.

Part of this necessarily owes to the complexity of a modern economy that is increasingly digitising and globalising. The old favourite adage of politicos that 'all politics is local' really isn't applicable after decades of free-flowing trade across all four corners of the earth.

Yet, unquestionably, any self-indulgent antics by elected officials will deal a savage blow to the democratic brand.

The revolving door of leaders -including multiple changes of prime minister -both the Australian Labor Party and the Coalition- contributed to over the past decade occurred during the same timeline that saw democratic satisfaction in Australian government essentially halve.

In 2010 under the Rudd government the satisfaction rate was 72%, in 2018 under the Turnbull government it was just 41%. Autocrats won't offer elections, but they'll bring stability with an iron-fisted rule.

<u>The People Get Their Voice Back</u>

The findings of The Economist's Democracy Index 2020 are startling, but must also be considered in context.

Although contemplating counterfactuals is by its nature an imprecise endeavour, if not for a pandemic it's fundamentally unimaginable any fully-functioning democracy would flip the switch overnight and opt for mass restrictions on liberty via lockdowns.

Once the pandemic ends, so too can the current restrictions on civil liberties be expected to, and scores to rise once more on the Index.

Furthermore, while this certainly wasn't a good year for democracy on the Index overall, the improved results on last year in nations like South Korea and Taiwan evidence much promise for these nations, and the Asian region as a whole.

Over the lifetime of the Index since it began in 2006 Asia is the only region where its score is higher in 2020 than it was in 2006. Such results in South Korea and Taiwan offset the rapid decline of democratic norms seen in Hong Kong and its impact on the score.

It's also necessary to note signs of trouble in the system can rally a response for its cure. For anyone who would opine Donald Trump's election to the presidency in 2016 can largely be attributed to apathy among the electorate, the record turnout of more than 156 million Americans in the 2020 election suggests an electorate newly engaged with their civic duty.

What's more, regardless of the fates and fortunes of democratic nations, evidence suggests the leaders of the autocratic form are now in for a rough ride of their own.

Although an abundance of evidence suggests the Russian government had a hand in attempting to destablise the US political system in recent years, in anti-corruption activist Alexei Navalny and his supporters Vladmir Putin's decades-long rule on Russia is facing it's strongest test to date.

In turn, for all its bravado the Chinese government knows any progress it seeks to make in its strategic aims during the decade ahead will be far harder than gains made in the decade prior.

Recent years have seen Washington DC decisively shift away from the prior aspiration to see China one day become a 'strategic partner', to now deeming it a major rival and challenger to American interests.

Furthermore, while China is seeking to cement its rising power with 'Wolf Warrior' diplomacy that's seen Beijing escalate old quarrels -such as with India and the UK- and commence new ones altogether (such as its trade war with Australia), these actions are ultimately amplifying the voices of those who advocate for nations to undergo a 'conscious uncoupling' with China.

Such an uncoupling is simply impossible in the short term. But Beijing's current grip on the global supply chain which it wields in its strategic aims isn't absolute, nor invulnerable.

For governments with ample time on their hands to draw up a national strategy for the post-pandemic era, and other Asian economies rapidly growing, there's a new appetite for a strategic rethink, and many countries are ready to build new trade ties with a long-term view.

FNArena's dedicated ESG Focus news section zooms in on matters Environmental, Social & Governance (ESG) that are increasingly guiding investors preferences and decisions globally. For more news updates, past and future:
https://www.fnarena.com/index.php/financial-news/daily-financial-news/category/esg-focus/

WEEKLY REPORTS

Weekly Ratings, Targets, Forecast Changes - 12-02-21

Weekly update on stockbroker recommendation, target price, and earnings forecast changes

Guide:

The FNArena database tabulates the views of seven major Australian and international stock brokers: Citi, Credit Suisse, 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 February 8 to Friday February 12, 2021
Total Upgrades: 15
Total Downgrades: 10
Net Ratings Breakdown: Buy 50.98%; Hold 40.62%; Sell 8.40%

By Mark Woodruff

For the week ending Friday 12 February, there were fifteen upgrades and ten downgrades to ASX-listed companies by brokers in the FNArena database.

ASX received three upgrades to Neutral from Sell by separate brokers and Transurban Group received two upgrades to Neutral from Sell.

There was some consensus amongst brokers regarding a turnaround for ASX. Ord Minnett considers the company has reached the bottom of its earnings cycle and is expected to see some rebound in FY22, while Citi believes all of the main negatives are now known.

Citi upgraded Transurban Group after a -20% share price underperformance over the past three months. Meanwhile, Credit Suisse raised FY21 distribution estimates with higher numbers expected in FY22 and FY23, due to lower financing costs after Chesapeake proceeds are received.

Pilbara Minerals had the largest percentage rise in target price for the week, despite Credit Suisse lowering its rating to Neutral from Outperform after a recent share price rally. Ord Minnett also rewarded Harvey Norman with the second largest percentage target price rise and simultaneously lowered its rating to Hold from Accumulate on valuation grounds.

For Pilbara Minerals, Credit Suisse doubts we are going back to a period of extreme oversupply and price depression and the stock continues to be the broker's preferred pick. Meanwhile, Ord Minnett anticipates Harvey Norman's underlying pre-tax profit for the first half will be up 91% at $545.7m. The company's earning result is due on March 1.

In terms of percentage downgrades to target prices for the week, all four of the brokers that cover Cimic Group in the FNArena database were disappointed by the FY20 results.

The 'miss' seemed to largely stem from pandemic effects on the awarding of new projects and on construction activity. Operating cash flow conversion was also weak, impacted by the unwinding of Leighton Asia projects and a reduction in debtor factoring.

Next in terms of negative revision to broker target prices was Origin Energy. As mentioned last week, the company lowered guidance for FY21 and headwinds facing the electricity sector do not appear to be weakening anytime soon.

An adjustment in data due to no recent updates by broker Ord Minnett had Pushpay Holding atop the table for downgrades to price targets.

The largest percentage fall in earnings forecasts by brokers in the FNArena database went to Transurban Group.

Cimic Group, Origin Energy and Pilbara Minerals have already received dishonourable mentions above in regard to falling target prices. They were also placed in the top three for percentage declines in forecast earnings by brokers.

Next was Crown Resorts which has been deemed unsuitable for the Crown Sydney licence and Macquarie assesses the pathway to obtaining approval is onerous and may take two years.

In the case of positive revisions to earnings forecasts for the week, Insurance Australia Group was the standout. Six of a possible seven brokers updated estimates and Citi upgraded the rating to Buy from Neutral.

It seemed to be a case of relief after first half results were impacted by a -$1.2bn provision loss, booked due to Business Interruption claims. Macquarie feels the result was strong under the circumstances and Citi can see momentum starting to build in the business.

There were surprises all around for the four brokers that updated earnings forecasts for News Corp after second half results. They were by driven by cost-out and operating leverage and the trends from both the Move and Dow Jones businesses were seen as indicative of structural growth.

GrainCorp appeared high on the table for largest percentage earnings upgrades after higher-than-expected grain receivals and grain exports. This comes after the largest east coast winter grain crops on record.

Nickel Mines was next after Macquarie noted a remarkable surge in electric vehicles in the fourth quarter, which has has propelled nickel sulphate prices higher. The company is the broker's preferred nickel exposure, featuring strong forecast free cash flow yields, which increase further in a spot price scenario.

Finally, Oil Search and fellow Papua LNG partners (Total and ExxonMobil) have finally signed an agreement with the PNG government. This is considered an important milestone for the project.

Total Buy recommendations take up 50.98% of the total, versus 40.62% on Neutral/Hold, while Sell ratings account for the remaining 8.4%.

Upgrade

AMP LIMITED ((AMP)) Upgrade to Neutral from Underperform by Macquarie .B/H/S: 1/6/0

Having initially retained an Underperform rating after a first glance at AMP's result yesterday, Macquaire has now decided to upgrade to Neutral.

The result was overshadowed by the back-down of Ares Management from any takeover intentions, which led to the big share price fall.

Macquarie sees it differently, suggesting the focus can now return to that within mangement's control. That includes an unchanged cost-out target. AMP managed to get close to its FY20 cost-out target even with additional unforeseen covid costs.

No dividend was declared but the board is committed to reinstating capital management, and a breakdown of divisional earnings has provided more clarity, and led the broker to upgrade forecasts. Target rises to $1.45 from $1.30.

ASX LIMITED ((ASX)) Upgrade to Neutral from Sell by Citi and Upgrade to Neutral from Underperform by Credit Suisse and Upgrade to Hold from Lighten by Ord Minnett.B/H/S: 0/6/1

Citi upgrades its rating to Neutral from Sell.

ASX has increased guidance for both capex and costs, a development that had already been anticipated by Citi. Costs grew 8% in the first half but Citi still expects cost growth to moderate from here while expecting higher revenue.

Issuer services revenue grew strongly by 44% in the first half, notes the broker, mainly reflecting the strong growth in retail broking accounts and activity. Citi expects momentum to soften from here.

With all the main negatives now known, the broker upgrades its earnings forecasts for FY21-23.

Target price rises to $70 from $68.

Credit Suisse upgrades its rating to Neutral from Underperform with a target price of $71.

ASX's first-half net profit was 3% above Credit Suisse's forecast. ASX's latest result demonstrates the resilience of its business, suggests the broker, with earnings down only -3% versus last year.

Going ahead, the broker believes ASX's earnings will contract by -5-10% in FY21 and a further -0-5% in FY22 led by softening of certain revenue lines like capital raisings supporting issuer services and elevated cash equities activity.

Ord Minnett looks at some key issues investors should look for in the interim result. In the broker's view, ASX has reached the bottom of its earnings and the broker expects to see some rebound in FY22.

Rating is upgraded to Hold from Lighten with the target price reducing to $73.78 from $77.28.

CHALLENGER LIMITED ((CGF)) Upgrade to Add from Hold by Morgans .B/H/S: 3/4/0

The normalised profit (NPAT) for Challenger was -2-3% below Morgans expectations, due to a -50 basis point decline in the life cash operating earnings (COE) margin.

The broker notes this margin is expected to be assisted in the second half when excess liquids are further invested. Morgans sees FY21 as the bottoming out of earnings and moves to an Add rating from Hold. The target is decreased to $6.72 from $6.80.

The analyst lowers FY21 and FY22 EPS forecasts by -4% and -7%, respectively, mainly reflecting higher net book growth assumptions, offset by reduced COE margin forecasts.

See also CGF downgrade.

CHAMPION IRON LIMITED ((CIA)) Upgrade to Neutral from Sell by Citi .B/H/S: 1/1/0

Citi raises benchmark iron ore forecasts to US$140 and US$110 per tonne for 2020 and 2021, respectively. The broker believes the higher-for-longer iron ore prices will benefit Champion Iron and upgrades to Neutral from Sell.

On Citi's modelling the share price is implying a long-term benchmark iron ore price of US$65/t versus its forecast of US$60/t.

COCHLEAR LIMITED ((COH)) Upgrade to Hold from Lighten by Ord Minnett .B/H/S: 2/3/2

After an encouraging first-half update and positive feedback from the US, Ord Minnett is confident Cochlear will a report a strong earnings recovery led by market share gains and flat operating costs. No guidance is expected.

Earnings estimates have been increased by 8% in FY21 and 7% in FY22.

Cochlear will report its first-half FY21 result on February 19.

Rating is upgraded to Hold from Lighten with the target rising to $200 from $175.

DETERRA ROYALTIES LIMITED ((DRR)) Upgrade to Neutral from Sell by Citi .B/H/S: 3/1/0

Citi upgrades its rating to Neutral from Sell with a target of $4.50.

Citi highlights Iron ore prices rose 80% in 2020 to nine-year high levels of US$177/t before moving back to US$150/t. The broker expects prices to rise to US$165/t over the next 3 months before falling to US$140 in 2021.

Deterra Royalties will report on a fiscal year basis and report first half results on 24 Feb. Citi expects earnings of $26m but notes this will be a tricky result since the first half will have a different incorporation date (15 June 2020) and implementation date (2 Nov 2020).

Citi forecasts a first half interim dividend of $0.02 with full-year dividend expected to peak at $0.22 in FY23.

G8 EDUCATION LIMITED ((GEM)) Upgrade to Neutral from Underperform by Macquarie .B/H/S: 1/4/0

Macquarie reviews sector conditions and upgrades to Neutral from Underperform. Feedback from the industry signals improving occupancy with some potential for limited price increases.

This is offsetting rent and sector funding, where there is limited appetite from financiers that may affect divestment plans.

The broker upgrades 2020 earnings (EBIT) by 5%, adjusting its model such that earnings per share are reduced by -11%. EPS estimates for 2021 and 2022 are raised by 161% and 21%, respectively.

Rating is upgraded to Neutral from Underperform and the target is raised to $1.20 from 85c.

INSURANCE AUSTRALIA GROUP LIMITED ((IAG)) Upgrade to Buy from Neutral by Citi .B/H/S: 3/4/0

Citi assesses momentum is building in the business and underlying margins although on current estimates there is only modest value appeal. Still, enough to upgrade to Buy from Neutral.

The broker anticipates the margin target of 15-17% will be achieved by FY23. Target is raised to $5.90 from $5.00.

Citi expects a significant increase in hazards allowance in FY22 while in the short term there is likely to be a modest adverse impact from lower investment returns and higher costs.

MOUNT GIBSON IRON LIMITED ((MGX)) Upgrade to Buy from Neutral by Citi .B/H/S: 2/0/0

Citi raises 2020 and 2021 benchmark iron ore price forecasts to US$140 and US$110 per tonne. Since the beginning of the year the Mount Gibson share price has fallen -15%.

Along with large earnings revisions this causes the broker to upgrade the rating to Buy/High Risk from Neutral/High Risk. Target is raised to $1.20 from $1.10.

NEWCREST MINING LIMITED ((NCM)) Upgrade to Add from Hold by Morgans .B/H/S: 6/1/0

Morgans regards strong cash flow and progress towards operational growth at Lihir and Cadia as positives for Newcrest Mining after first half results were released.

The company is on track for mid-point FY21 guidance for gold and copper production, predicts the broker.

The analyst highlights guidance for costs was revised to the top of the range for FY21, on the back of a higher Australian dollar and additional covid-19 costs.

Underlying profit (NPAT) was up 98% from the first half FY20 and broadly in-line with consensus, driven by an increase in the gold and copper price, assesses Morgans.

The broker lifts the target price to $29.98 from $27.87, driven by the longer-term growth and strategy spelt out by management for both Lihir and Cadia. The rating is lifted to Add from Hold.

NORTHERN STAR RESOURCES LTD ((NST)) Upgrade to Buy from Hold by Ord Minnett .B/H/S: 3/1/1

Northern Star’s result was in line with Ord Minnet's forecast and the broker can see over 10% free cash flow (FCF) yields from FY23.

With $123m net debt and no material capex on the horizon, cash flow and returns will remain an important part of the analyst's investment case.

The company has reconfirmed the 6% revenue-based dividend policy.

Ord Minnett highlights significant leverage to the gold price with only 13% of the three year forward production hedged in the broker's model.

Upgrade to Buy from a Hold rating with the price target rising to $14.40 from $14.3.

TRANSURBAN GROUP ((TCL)) Upgrade to Neutral from Underperform by Credit Suisse and Upgrade to Neutral from Sell by Citi.B/H/S: 3/4/0

Credit Suisse upgrades its rating to Neutral from Underperform with the target price increasing to $13 from $12.6.

Transurban Group's first-half result showed toll revenue at $1,165m, -3% below Credit Suisse's forecast of $1,204m. Proportional operating income for the half came in at $840m, -11% below the broker's forecast. Credit Suisse notes the miss was driven by weak traffic performance in Melbourne, and lower average dynamic toll pricing in the US Express Lanes.

FY21 distribution estimates have been raised by the broker in FY21 to 33.8c with higher numbers expected in FY22 and FY23 due to lower financing costs after the Chesapeake proceeds are received.

Citi has upgraded Transurban Group to Neutral from Sell following the release of an interim report that proved slightly above expectations, even though the analysts also suggest it missed market consensus by some -5% at the operational (EBITDA) level.

The upgrade was more so inspired by the -20% share price underperformance over the past three months, explain the analysts.

Three key factors are preventing Citi from lifting the rating to a Buy: the valuation remains above long term average, with leverage high and potential downside risks medium term from increased work-from-home (which impacts on the traffic on toll roads).

Citi's target price has lifted to $13.35 from $12.83.

Downgrade

CHALLENGER LIMITED ((CGF)) Downgrade to Neutral from Outperform by Macquarie .B/H/S: 3/4/0

FY21 guidance for normalised net profit remains in a range of $390-440m, despite lower rental abatements. First half results slightly missed expectations.

Macquarie notes the life division missed consensus forecasts by -6%, although this was broadly offset by strength in funds management. Given the slower rebound of life margins, the broker downgrades to Neutral from Outperform.

Target is raised to $6.30 from $4.60 to reflect the stronger life balance growth from institutional sales over the longer term.

See also CGF upgrade.

CIMIC GROUP LIMITED ((CIM)) Downgrade to Neutral from Outperform by Credit Suisse .B/H/S: 1/3/0

Rating is downgraded to Neutral from Outperform. Target is reduced to $21.90 from $34.

Credit Suisse is disappointed by CIMIC Group's weak full-year result noting the subdued result was further compounded by various one-offs and suboptimal cash flows that will likely dampen sentiment in the near term.

While the company's investment thesis includes a capital-light structure and an improving balance sheet, Credit Suisse believes this will take time to reflect in the stock's multiples.

Post a lukewarm 2021 guidance, the broker cuts its 2021-22 earnings forecasts by -36-42%.

CROWN RESORTS LIMITED ((CWN)) Downgrade to Neutral from Outperform by Macquarie .B/H/S: 2/4/0

Crown Resorts has been deemed unsuitable for the Crown Sydney licence and Macquarie assesses the pathway to obtaining approval is onerous and may take two years.

The broker believes the NSW casino inquiry report brings into question the company's suitability to operate both the Melbourne and Perth casinos. Nevertheless, Macquarie expects Melbourne and Perth gambling will continue without hindrance.

As there is a high level of risk and uncertainty as to how the company will manage the pathway to approval going forward, the broker downgrades to Neutral from Outperform. Target is reduced to $8.30 from $11.00.

ECOFIBRE LIMITED ((EOF)) Downgrade to Hold from Buy by Ord Minnett .B/H/S: 0/1/0

Ecofibre's first-half revenue at $14.7m was in line with Ord Minnett's estimate, although the operating loss was more than expected.

The company has revised its guidance from “break-even” to expecting a loss of circa -$7m in FY21 due to the lack a meaningful near-term recovery in revenue.

Ord Minnett remains convinced on the long-term potential of CBD and Hemp and views Ecofibre as a key player in the development of the industry.

Even then, with trading severely curtailed in the US and uncertainty on the timing of the recovery, Ord Minnett downgrades its recommendation to a Hold from Buy with the target price reducing to $1.65 from $2.26.

GRAINCORP LIMITED ((GNC)) Downgrade to Neutral from Outperform by Credit Suisse .B/H/S: 3/1/0

Credit Suisse believes GrainCorp's FY21 guidance puts to rest some arguments with respect to crop leverage under the new crop production contract. Carry out for FY21 is guided to 2.5-3.5mt, implying a circa 0.5-1mt boost to FY22 export volume due to carry-out.

Net profit is guided to be $60-85m versus the broker's $80m forecast. Credit Suisse thinks normalisation of inventory will likely lead to the core net debt rising to $130m in the first half.

Credit Suisse downgrades its rating to Neutral from Outperform with the target price rising to $5.06 from $5.03.

GALAXY RESOURCES LIMITED ((GXY)) Downgrade to Underperform from Neutral by Credit Suisse .B/H/S: 1/2/3

December quarter production met full year guidance. Record sales were a positive, Credit Suisse notes, but a further improvement in recoveries is required to reduce costs. No sales price was disclosed.

2021 production is guided at 162-175,000t, 55% above the prior year. This assumes full plant throughput at Mount Cattlin from the second quarter.

Credit Suisse downgrades to Underperform from Neutral on valuation grounds. Target is raised to $2.10 from $1.30. The broker notes the updated feasibility study on Sal de Vida is due for release in the June quarter.

HARVEY NORMAN HOLDINGS LIMITED ((HVN)) Downgrade to Hold from Accumulate by Ord Minnett .B/H/S: 5/1/0

Ord Minnett downgrades its recommendation on Harvey Norman to Hold from Accumulate due to the lack of valuation support. Target rises to $5.50 from $5.25.

The broker expects Harvey Norman's underlying pre-tax profit for the first half to be up 91% at $545.7m.

The broker awaits more comments on the tailwinds from rising home investment and the extent to which this can moderate sales and margin declines.

PILBARA MINERALS LIMITED ((PLS)) Downgrade to Neutral from Outperform by Credit Suisse .B/H/S: 0/1/3

Credit Suisse downgrades its rating to Neutral from Outperform with the target rising to $0.95 from $0.40.

The broker expects lessons learned over the past 24 months including a period of significant lithium oversupply leading to low utilisation rates and prices to translate into more controlled future expansion.

Even so, the likelihood of going back to a period of extreme oversupply and price depression is considered low by Credit Suisse. Pilbara continues to be the broker's preferred pick.

REA GROUP LIMITED ((REA)) Downgrade to Underperform from Neutral by Credit Suisse .B/H/S: 1/4/1

Despite Rea Group reporting first half results broadly in-line with Credit Suisse's estimates, the broker lowers the rating to Underperform from Neutral following the recent strong share price performance.

A key takeaway for the analyst includes a flattening out of depth listings, with a slight sequential decline, despite the 4% year-on-year growth in National listings in the first half.

The target price is lowered to $136.70 from $137.7

SUNCORP GROUP LIMITED ((SUN)) Downgrade to Hold from Accumulate by Ord Minnett .B/H/S: 3/4/0

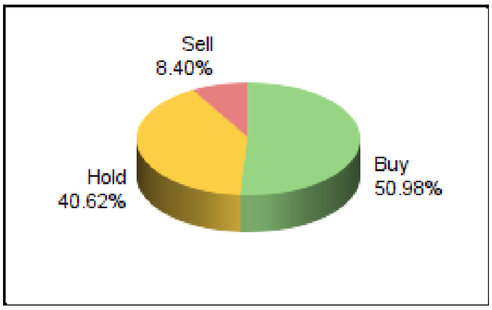
Suncorp Group reported a first half FY21 net profit of $490m, below Ord Minnett’s $518m forecast, while the headline result was
boosted by the bank achieving a high net interest margin (NIM) and low bad debt charges.

A fully franked interim dividend of 26 cents was declared, versus the broker's 22 cent forecast.

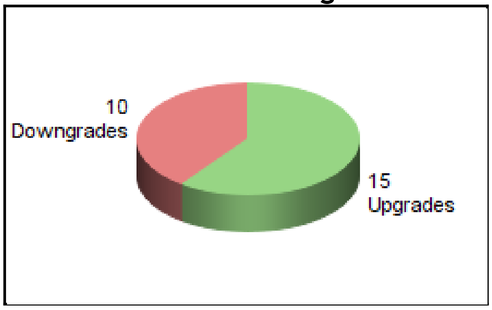
The analyst makes a significant reduction to forecasts due to weak underlying trends, a period of reinvestment in the business and a strong share price performance relative to other general insurance stocks.

The rating is downgraded to Hold from Accumulate and the target price falls to $12 from $12.83.

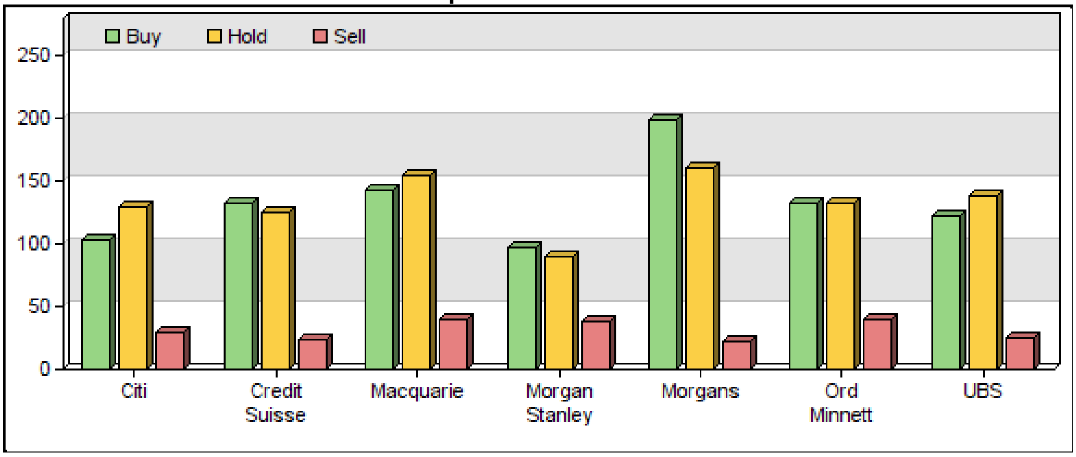
Total Recommendations



Recommendation Changes



Broker Recommendation Breakup



Broker Rating

Order	Company	New Rating	Old Rating	Broker
Upgrade				
1	AMP LIMITED	Neutral	Sell	Macquarie
2	ASX LIMITED	Neutral	Sell	Citi
3	ASX LIMITED	Neutral	Sell	Credit Suisse
4	ASX LIMITED	Neutral	Sell	Ord Minnett
5	CHALLENGER LIMITED	Buy	Neutral	Morgans
6	CHAMPION IRON LIMITED	Neutral	Sell	Citi
7	COCHLEAR LIMITED	Neutral	Sell	Ord Minnett
8	DETERRA ROYALTIES LIMITED	Neutral	Sell	Citi
9	G8 EDUCATION LIMITED	Neutral	Sell	Macquarie
10	INSURANCE AUSTRALIA GROUP LIMITED	Buy	Neutral	Citi
11	MOUNT GIBSON IRON LIMITED	Buy	Neutral	Citi
12	NEWCREST MINING LIMITED	Buy	Neutral	Morgans
13	NORTHERN STAR RESOURCES LTD	Buy	Neutral	Ord Minnett
14	TRANSURBAN GROUP	Neutral	Sell	Citi
15	TRANSURBAN GROUP	Neutral	Sell	Credit Suisse
Downgrade				
16	CHALLENGER LIMITED	Neutral	Buy	Macquarie
17	CIMIC GROUP LIMITED	Neutral	Buy	Credit Suisse
18	CROWN RESORTS LIMITED	Neutral	Buy	Macquarie
19	ECOFIBRE LIMITED	Neutral	Buy	Ord Minnett
20	GALAXY RESOURCES LIMITED	Sell	Neutral	Credit Suisse
21	GRAINCORP LIMITED	Neutral	Buy	Credit Suisse
22	HARVEY NORMAN HOLDINGS LIMITED	Neutral	Buy	Ord Minnett
23	PILBARA MINERALS LIMITED	Neutral	Buy	Credit Suisse
24	REA GROUP LIMITED	Sell	Neutral	Credit Suisse
25	SUNCORP GROUP LIMITED	Neutral	Buy	Ord Minnett

Recommendation

Positive Change Covered by > 2 Brokers

Order	Symbol	Company	New Rating	Previous Rating	Change	Recs
1	ASX	ASX LIMITED	-14.0%	-50.0%	36.0%	7
2	DRR	DETERRA ROYALTIES LIMITED	75.0%	50.0%	25.0%	4
3	PPH	PUSHPAY HOLDINGS LIMITED	33.0%	13.0%	20.0%	3
4	NST	NORTHERN STAR RESOURCES LTD	40.0%	20.0%	20.0%	5
5	TCL	TRANSURBAN GROUP	29.0%	14.0%	15.0%	7
6	NCM	NEWCREST MINING LIMITED	79.0%	64.0%	15.0%	7
7	IAG	INSURANCE AUSTRALIA GROUP LIMITED	43.0%	29.0%	14.0%	7
8	CSL	CSL LIMITED	43.0%	29.0%	14.0%	7
9	WES	WESFARMERS LIMITED	7.0%	-7.0%	14.0%	7

Negative Change Covered by > 2 Brokers

Order	Symbol	Company	New Rating	Previous Rating	Change	Recs
1	GNC	GRAINCORP LIMITED	75.0%	100.0%	-25.0%	4
2	PLS	PILBARA MINERALS LIMITED	-75.0%	-50.0%	-25.0%	4
3	CIM	CIMIC GROUP LIMITED	25.0%	50.0%	-25.0%	4
4	CWN	CROWN RESORTS LIMITED	33.0%	50.0%	-17.0%	6
5	MQG	MACQUARIE GROUP LIMITED	25.0%	42.0%	-17.0%	6
6	GXY	GALAXY RESOURCES LIMITED	-33.0%	-17.0%	-16.0%	6
7	ORG	ORIGIN ENERGY LIMITED	43.0%	57.0%	-14.0%	7
8	TLS	TELSTRA CORPORATION LIMITED	30.0%	42.0%	-12.0%	5
9	HVN	HARVEY NORMAN HOLDINGS LIMITED	83.0%	92.0%	-9.0%	6
10	SUN	SUNCORP GROUP LIMITED	43.0%	50.0%	-7.0%	7

Target Price

Positive Change Covered by > 2 Brokers

Order	Symbol	Company	New Target	Previous Target	Change	Recs
1	PLS	PILBARA MINERALS LIMITED	0.833	0.650	28.15%	4
2	HVN	HARVEY NORMAN HOLDINGS LIMITED	5.692	5.292	7.56%	6
3	GXY	GALAXY RESOURCES LIMITED	2.342	2.208	6.07%	6
4	SUN	SUNCORP GROUP LIMITED	11.619	11.031	5.33%	7
5	MQG	MACQUARIE GROUP LIMITED	145.500	139.000	4.68%	6
6	GNC	GRAINCORP LIMITED	5.308	5.080	4.49%	4
7	IAG	INSURANCE AUSTRALIA GROUP LIMITED	5.657	5.463	3.55%	7
8	WES	WESFARMERS LIMITED	50.504	49.033	3.00%	7
9	NCM	NEWCREST MINING LIMITED	32.283	31.639	2.04%	7

Negative Change Covered by > 2 Brokers

Order	Symbol	Company	New Target	Previous Target	Change	Recs
1	PPH	PUSHPAY HOLDINGS LIMITED	0.000	1.110	-100.00%	3
2	CIM	CIMIC GROUP LIMITED	23.913	29.750	-19.62%	4
3	ORG	ORIGIN ENERGY LIMITED	5.407	6.017	-10.14%	7
4	CWN	CROWN RESORTS LIMITED	9.642	10.092	-4.46%	6
5	ASX	ASX LIMITED	69.396	70.436	-1.48%	7
6	TLS	TELSTRA CORPORATION LIMITED	3.526	3.568	-1.18%	5
7	TCL	TRANSURBAN GROUP	14.314	14.470	-1.08%	7
8	CSL	CSL LIMITED	306.814	307.629	-0.26%	7
9	NST	NORTHERN STAR RESOURCES LTD	13.770	13.790	-0.15%	5

Earning Forecast

Positive Change Covered by > 2 Brokers

Order	Symbol	Company	New EF	Previous EF	Change	Recs
1	IAG	INSURANCE AUSTRALIA GROUP LIMITED	20.867	7.883	164.71%	7
2	NWS	NEWS CORPORATION	70.969	51.639	37.43%	4
3	GNC	GRAINCORP LIMITED	34.273	26.203	30.80%	4
4	NIC	NICKEL MINES LIMITED	7.482	6.457	15.87%	3
5	OSH	OIL SEARCH LIMITED	2.545	2.224	14.43%	7
6	MQG	MACQUARIE GROUP LIMITED	691.167	616.167	12.17%	6

7	KAR	KAROON ENERGY LTD	-2.867	-3.200	10.41%	3
8	SUN	SUNCORP GROUP LIMITED	70.886	65.014	9.03%	7
9	TLS	TELSTRA CORPORATION LIMITED	14.508	13.497	7.49%	5
10	COF	CENTURIA OFFICE REIT	19.050	17.850	6.72%	4

Negative Change Covered by > 2 Brokers

Order	Symbol	Company	New EF	Previous EF	Change	Recs
1	TCL	TRANSURBAN GROUP	-2.057	6.972	-129.50%	7
2	CIM	CIMIC GROUP LIMITED	135.750	207.900	-34.70%	4
3	ORG	ORIGIN ENERGY LIMITED	17.896	21.914	-18.34%	7
4	CWN	CROWN RESORTS LIMITED	0.993	1.202	-17.39%	6
5	PLS	PILBARA MINERALS LIMITED	-0.755	-0.655	-15.27%	4
6	GXY	GALAXY RESOURCES LIMITED	-3.651	-3.350	-8.99%	6
7	MP1	MEGAPORT LIMITED	-25.400	-23.667	-7.32%	3
8	DRR	DETERRA ROYALTIES LIMITED	14.428	15.453	-6.63%	4
9	DOW	DOWNER EDI LIMITED	31.617	33.835	-6.56%	6
10	OGC	OCEANAGOLD CORPORATION	-18.594	-17.649	-5.35%	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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WEEKLY REPORTS

Uranium Week: Multiple Tailwinds For Uranium

While the uranium spot price continues to move in a tight range, Cameco remains positive about long-term fundamentals for the uranium market.

-Demand for uranium is rising just as supply becomes uncertain
-The US returns to uranium conversion industry after five-year hiatus
-Uranium spot price falls marginally

By Mark Woodruff

Speaking at the company's year-end results presentation, President and CEO of Cameco, Tim Gitzel, remained positive about the long-term fundamentals in the uranium market.

He noted momentum is building towards **non-traditional nuclear**, such as small modular reactors and advanced reactors as well as recognition of nuclear energy's role in the **production of low-carbon energy for the production of hydrogen and desalination.**

This is occurring as countries and companies around the world are making **net-zero commitments**. This includes the US, where the new administration has expressed support for **maintaining the existing domestic nuclear power fleet and the construction of advanced reactors, as well as recommitting to the Paris Agreement.**

Also, "demand for uranium is rising at precisely the same time that supply is becoming less certain. We know that utilities have not been replacing what they consume annually under long-term contracts," Gitzel said. "This has led to a growing wedge of uncovered uranium requirements."

Citing data from market research company UXC, he said "the base case projects an annual shortfall of almost 100m lbs by 2035. That means the world needs to discover, develop and commission about six McArthur Rivers or Cigar Lakes in the next 15 years. Given the timelines it takes, we should be investing now."

Regarding Cameco's operational performance, Gitzel explained production at Cigar Lake mine remains suspended with "lots of question marks" regarding the timeframe for recommencement. The suspension is due to uncertainties about access to qualified operational personnel caused by the pandemic and a commitment to protecting the health and safety of workers, their families and the broader community.

Gitzel insisted that they don't want to "yoyo" production at Cigar Lake by risking a premature recommencement of operations. He noted they were waiting for the vaccine rollout whilst maintaining close contact with the public health authorities and indigenous community leaders.

Due to precautionary production suspensions at its operations, Cameco produced only a 5mlbs in 2020. Gitzel noted that it was too early to say if there would be an impact on 2022 production guidance at Cigar Lake. Should the Canadian vaccine be a pre-requisite for restarting Cigar Lake, recommencement may be delayed well into 2021.

Company News

Honeywell said this week it would begin preparing to reopen its uranium hexafluoride (UF6) conversion plant, the Metropolis Works Facility (MTW), in Metropolis, Illinois.

Restart work will begin this year and production will restart in early 2023, which will mark the US's return to the uranium conversion industry after a five-year hiatus. In January 2017, the company laid off some of its employees in Metropolis due to significant challenges of the nuclear industry globally and the oversupply of UF6, explains industry consultant TradeTech.

This decision is expected to be positive for the uranium sector, as utilities can now clarify their forward conversion contracts before procuring the uranium to be delivered to the converters.

Australian-listed **Bannerman Resources** ((BMN)) last week announced the raising of $12m via a placement of shares at 10.5 cents. The funds are to be used to complete a pre-feasibilty study at the th company's Etango-8 uranium project in Namibia, with sufficient funding to then undertake and complete a definitive feasibility study. Additionally, funds will be deployed for general working capital and corporate purposes, including financing and off-take initiatives.

Among the investors taking part in the placement was a specialist uranium investor in Tribecca Investment Partners, which provided cornerstone support. FNArena understands the raising was very heavily oversubscribed by both institutional investors and private clients.

As the raising was the first to be undertaken by an Australian uranium company in 2021, it provides a useful insight into uranium investor sentiment.

Uranium Pricing

TradeTech's **Weekly Spot Price Indicator** is US$29.35/lb, down -US$0.20 from last week's Indicator.

The weekly spot uranium price has declined nearly -4% in 2021 while spot price volatility continues to decline on limited market activity. The average weekly uranium spot price in 2021 is US$29.92/lb, US$0.21/lb above the 2020 average.

The spot uranium market remains slow with a total of 500,000lbs U3O8 recorded in transactions for the week.

Market participants continue to wait for spot demand to increase, especially from the utility sector. There has been some limited increase in buying interest from the utility sector since the beginning of the year, explains TradeTech.

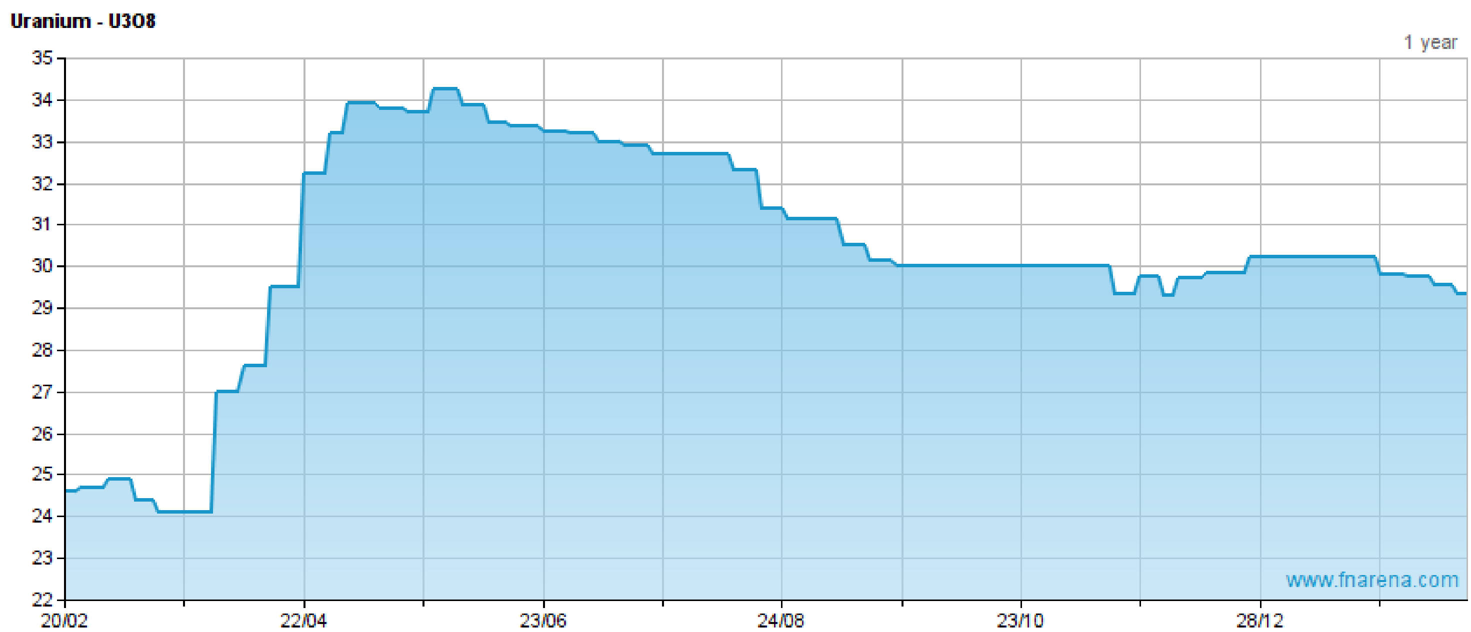
However, non-utility buying continues to outstrip end-users in the spot market with demand overall below sellers' hopes for mid-February. As a result, offer prices fell across all delivery locations as sellers attempt to motivate buying interest with lower prices.

TradeTech's **term price** indicators are US$33.75/lb (mid) and US$36.00/lb (long).

As noted by Cameco in its February 11 quarterly earnings call, the company is seeing off-market interest growing, which has long been an indicator of future long-term buying interest from utilities.

While sellers are encouraged by the uptick in off-market interest, these informal discussions must translate into firm buying commitments to provide real support to the uranium production sector.

On the supply side, sellers continue to caution that uranium production is in a tenuous position. Along with recent production shutdowns and curtailments, producers warn that the market must monitor the capability of producers to respond as needed on a timely basis and at a reasonable cost should there be any additional disruptions or curtailments to existing production.



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FNArena is proud about its track record and past achievements: Ten Years On

WEEKLY REPORTS

The Short Report - 18 Feb 2021

See **Guide** further below (for readers with full access).

Summary:

Week ending February 11, 2021.

Wow. Never in the history of this Report has one week seen so little change in short positions on the ASX, by a considerable margin.

The ASX200 posted a net rally over the week, once the whole GameStop debacle ended. We might put such a lack of shorting activity down to it being the first week of the local results season, but so few are the reports in the first week this seems unrealistic.

I might be forced to suspect a possible problem with ASIC data, but there *was* some shuffling around of stocks in each percentage bracket, a couple of moves of more than one percentage point in the 10%-plus bracket, and EML Payments ((EML)) did slip a bracket, to 5.8% from 6.5%.

Just as well for someone. The company reported yesterday and shot the lights out, rallying 16%.

Otherwise, we note Webjet ((WEB)) shorts fell to 12.3% from 13.3% as vaccination rollouts offer some hope for a reopening of the border one day, while Northern Star Resources' ((NST)) shorts fell to 10.3% from 11.6%.

I have been suggesting all along, in defiance of other theories, that the large short position in Northern Star represented a play on the merger with Saracen Minerals, implying Northern Star was the overvalued partner. Since the merger was completed this week, Northern Star shares have fallen over -7%.

Stand by for a short position reduction in next week's Report.

No Movers & Shakers this week.
Weekly short positions as a percentage of market cap:

10%+
WEB 12.3
TGR 12.1
NST 10.3

No changes

9.0-9.9

No stocks, no changes

8.0-8.9%

MSB, ING, WSA

No changes

7.0-7.9%

AVH, SSM, MYR, MTS

No changes

6.0-6.9%

FNP, RSG, A2M, IVC, FLT

Out: EML

5.0-5.9%

EML, ALK, EOS, TYR, CUV, BVS, NEA, BOQ

In: EML

Movers & Shakers

See above.

ASX20 Short Positions (%)

Code	Last Week	Week Before	Code	Last Week	Week Before
ALL	0.2	0.3	MQG	0.5	0.4
ANZ	1.1	1.1	NAB	1.3	1.2
APT	1.2	1.2	NCM	0.1	0.1
BHP	3.5	3.6	RIO	0.2	0.3
BXB	0.3	0.3	TCL	0.7	0.7
CBA	0.7	0.6	TLS	0.3	0.3
COL	0.5	0.5	WBC	1.0	0.9
CSL	0.1	0.1	WES	0.5	0.5
FMG	0.3	0.3	WOW	0.2	0.2
GMG	0.2	0.2	WPL	1.0	1.0

To see the full Short Report, please go to this link

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.

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.

RUDI'S VIEWS

Rudi's View: Yet Another Short Selling Failure

In this week's Weekly Insights:

-Yet Another Short Selling Failure
-February: Early Days, Full Of Promise
-A Different Environment For Dividends
-FNArena Webinar

By Rudi Filapek-Vandyck, Editor FNArena

Yet Another Short Selling Failure

Short sellers. They present themselves as the shining white knights if not the morally-driven, diligent sleuths who dig into the finer details of how companies operate and communicate with their investors, with the sole aim of uncovering fraud and management misdemeanors, because investors are best served by honesty and transparency, and somebody needs to do the dirty work when others are simply looking to promote the next pump & dump opportunity.

Great theory. And there have been a few excellent examples, both domestic and overseas, of short sellers uncovering the fraud when nobody else did. Blue Sky Alternative Investments springs to mind, as does failed sandalwood grower and marketer Quintis.

But a much larger number of companies have been targeted mostly via overseas domiciled researchers keen to inform their hedge fund clientele first and then releasing their accusatory research upon the masses. Helped by the fact this is usually a well-prepared, organised gang-attack, the initial result tends to be a sharp fall in the target's share price.

From Macquarie Group and Fortescue Metals a little further down memory lane, to Amcor, Credit Corp, Corporate Travel, Rural Funds Group, Seek, TechnologyOne, Tyro Payments, and WiseTech Global in more recent times; all have been subjected to such an attack from foreign short sellers research, but with quite the mixed outcomes.

Among the recent attacks, shares in Tyro Payments have yet to recover, while TechnologyOne is well off its low but also still at a distance from the top, and Seek shares are setting new all-time highs, having dipped only briefly back in late October-early November.

First observation: while in some cases legitimate questions have been raised, most share prices recover over time and shake off the bad smell that automatically comes with the short sellers accusations, amid broad media coverage and a falling share price. There are always multiple factors in play, in particular over a longer time-frame, but one is hard pressed to find any lingering impact in today's share price of, say, Rural Funds Group, or Credit Corp, or Amcor.

Equally important: while not every accusation and attack is swiftly dealt with or decisively debunked, through the courts or otherwise, none of these targeted companies have since been uncovered as being fraudulent in their operations, accountancy, or otherwise.

I also note that, with the exception of Tyro Payments for which the market is undoubtedly awaiting the next update on technology failure and remediation put in place, the negative impact on share prices is becoming shallower and shorter. At the same time, those familiar with the companies involved are increasingly labeling the research released to inspire such attacks as "low quality", "nothing new" and "factually incorrect".

Last year, those were the key words used in response to GMT research, not necessarily by the company under attack (TechnologyOne), but by domestic analysts familiar with the company and the sector. Same words re-appeared when local media were seeking qualified responses to Blue Orca's attack on Seek.

Last week, J Capital launched an attack on small cap local technology company, Nearmap ((NEA)), and despite JCap's marketing efforts beforehand to gather as much anticipation and impact as possible, it has proved quite the disappointing exercise, mostly for the short sellers who jumped on the bandwagon while -no doubt- expecting another easy clobber-them-handsomely knee-jerk group exercise before anyone starts asking questions.

Nearmap is a not well known, former high flyer, that is not profitable, had a few operational hiccups in years past, and with lots of question marks surrounding its expansion into the US market. At first glance, that seems like a rather easy bounty to target, similar as with Credit Corp, Rural Funds Group and TechnologyOne in the past.

Only this time, things have gone pear shaped quite quickly. Also because of how the company under attack has responded to the many short sellers allegations. Once the share price started weakening, and the company became aware of JCap's report, it simply asked the ASX to halt trading in its shares, which was granted.

Then it pulled forward (by two days) the release of its interim financials, together with presentation slides, an analyst pack, detailed commentary on the financials, plus a dedicated rebuttal of the accusations made in the short sellers report.

We can all argue about this and that until the cows come home, and without finding any concrete answers, but I think Monday's share price response tells the tale: JCap's attack has been found wanting, and short sellers have, at least in part, abandoned their strategy and covered in order to minimise potential losses. In case you are not aware, Nearmap shares surged just under 19% on the day to $2.57, their highest level since November last year.

And as I have been fortunate to read through some of the early responses from some analysts whose daily job it is to monitor and research this little company, the released performance numbers did not reveal a "blow-me-out-of-the-park" performance from the company. They were simply good enough to show investors that JCap's case was built on quicksand. Faulty research. Misguided accusations. Call it what you want.

So here's the irony. In a share market that is deemed extremely well-priced, if not grossly overvalued, by many a market observer, the industry whose *raison d'etre* consists of uncovering fraud and investor deception is increasingly being unmasked as publishers of low-quality, faulty research aimed at uninformed, flighty investors who'd be willing to sell first and ask questions later.

Nearmap was once upon a time part of my selection of local technology companies that deserved investor attention. For a short time it even featured in the All-Weather Model Portfolio. In the current context, I believe the company, given it is unprofitable, with many question marks and execution uncertainties, remains too risky for my appetite.

But on the swift and decisive response to the JCap organised attack, I'd say well done Nearmap. Truly impressive. Let's hope a few nasties got burned really heavily, and they direct their disappointment back at the source of the report.

Serves them well.

February: Early Days, Full Of promise

By Rudi Filapek-Vandyck, Editor FNArena

Only in Australia, I think, can one be in the middle of reporting season, calendar-wise, but with only one-sixth of all companies having reported.

Or to put this in more concrete terms: by early March, when the current February corporate reporting will be done and dusted, FNArena expects to have updated on circa 318 ASX-listed companies.

Today, as I write this week's Weekly Insights, February 15th, the total number of companies included in our daily Corporate Results Monitor still only tallies 52 companies.

I think everybody can do the math. There are more than 260 corporate results still waiting to be released, ex quarterly trading updates such as from the banks outside of CommBank ((CBA)) and Bendigo and Adelaide Bank ((BEN)), and ex the handful of companies that reported on Monday, today, and whose general assessment will be included in tomorrow's Monitor update.

No, I have no clue either, other than that the skew towards the second half of each reporting season in Australia has noticeably worsened in recent years. This skew seemed logical when businesses were under the pump, forced to cut dividends and issue profit warnings, as they found it increasingly more difficult to live up to market expectations.

We should be edging closer to 100 by now, on pre-2019 schedules, but maybe Australian companies are simply finding it difficult to change the new habit?

Whatever the reason, investors will find out what is going on inside corporate Australia over the next two weeks. So far, the early numbers look very promising with the percentage of market beating financial results at roughly 55% and the percentage of clear disappointments at around 15.5%.

To put these numbers in context: total "misses" since August 2013 have never been below 19% and usually are in the low to middle 20s range while the best reporting seasons, September-December last year and March prior, generated exceptional numbers of 49% and 43% respectively.

It's still looking very promising, but we have to take into account that on 52 companies thus far only, and with more than 260 yet to follow, today's statistics can change quite dramatically. One observation to make is that some of yesteryear's favourites are genuinely facing a much tougher environment in 2021 (see: Altium ((ALU)) on Monday) while negative secular trends remain the bugbear for owners of shopping malls and office properties, see Mirvac Group ((MGR)) and Unibail-Rodamco-Westfield ((URW)).

In between, a large number of companies are performing better-than-expected, forcing analysts' forecasts higher. At least, this is the picture for the first two weeks of this February, on a thinner than usual sample.

A Different Environment For Dividends

The addition of Telstra ((TLS)) shares to the **FNArena-Vested Equities All-Weather Model Portfolio** has led to a number of questions from readers and subscribers.

It is true, I am usually not a big fan of investing in low quality propositions, much preferring to avoid getting caught in something like Unibail-Rodamco-Westfield ((URW)) and then hearing management declare there will be no dividend for years to follow. Telstra shares have caused many a loyal shareholder continuous headaches for extended periods since its listing in the late 1990s.

As I have tried to explain since returning from the end-of-year break in January, this year's prospect of rising global bond yields will have a direct impact on bond proxies and share prices of many an income providing stock in the share market. As such, it is my forecast that financials and industrials that are in a position to grow their earnings and dividends will prove a much better investment than most property owners or your typical REIT.

Following on from this forecast, the All-Weather Portfolio has reshuffled its exposure to dividend paying stocks, adding Telstra and Super Retail ((SUL)) while sticking with Aventus Group ((AVN)) and Waypoint REIT ((WPR)). Aventus Group has continued to perform strongly, while Waypoint REIT has clearly been impacted by the rise in global yields.

Investors should also note many of the stocks held in the portfolio are regular and solid providers of growing dividends, including Amcor ((AMC)), Iress ((IRE)) and Coles ((COL)) while, of course, the likes of CSL ((CSL)), ResMed ((RMD)), TechnologyOne ((TNE)) and REA Group ((REA)) equally pay out growing dividends, though their yields are too low to feature in any specific dividend-oriented investment strategy.

Telstra's inclusion might well prove but a temporary decision, in that I believe the prospect of selling off equity in its towers and other infrastructure assets is minimising risk and most likely to unleash value for shareholders. It is on this specific consideration that Telstra is temporarily back in the portfolio, offering circa 4.7% yield after the recent share price appreciation. Lucky me, also, Telstra's financial interim performance did not disappoint this time around.

The inclusion of Super Retail adds a high yielding stock that should be supported by the prospect of a prolonged period of buoyant consumer-related spending while, admittedly, also creating some overlap with one of my long-standing favourites, Bapcor ((BAP)).

As far as the All-Weather Model Portfolio itself is concerned, this is something we set up with a financial partner on an external platform (now: Wealth O2), so no specific details are available on the FNArena website. The Portfolio chooses from the same lists that are available through the dedicated All-Weather Stocks section on the website. It owns most, though not all of the stocks mentioned.

Sometimes an exception is made, as with Telstra and Super Retail, stocks that wouldn't feature on my lists. I haven't as yet figured out how best to communicate this switch in focus when it comes to dividend stocks, other than mentioning it here in Weekly Insights.

Suffice to say, while the five names mentioned under Dividend Champions on the website will continue to pay out dividends, and grow those dividends over the years ahead, with low risk of having to reduce or scrap payouts, they are unlikely to perform well if bond yields keep tilting higher.

This is the one perspective investors should simply be aware of.

For more details about the All-Weather Portfolio, send an email to info@fnarena.com

FNArena Webinar

FNArena organised an online webinar on Monday last week with myself providing an introduction to the website and service provided, followed by a general update on financial markets in early 2021.

Two recordings from the event have been added to the FNArena Talks section on the website:

-First part (30 minutes) consists of a general overview to the FNArena website and the service provided, helping subscribers to maximise their usage and benefits;

-Second part (30 minutes) provides an assessment of what is happening in financial markets, why, and a deeper look into the February reporting season.

To visit FNArena Talks: https://www.fnarena.com/index.php/analysis-data/fnarena-talks/

For Part I: https://www.fnarena.com/index.php/2021/02/11/rudis-view-february-feeding-market-optimism/

(This story was written on Monday 15th February, 2021. It was published on the day in the form of an email to paying subscribers, and again on Thursday as a story on the website).

(Do note that, in line with all my analyses, appearances and presentations, all of the above names and calculations are provided for educational purposes only. Investors should always consult with their licensed investment advisor first, before making any decisions. All views are mine and not by association FNArena's - see disclaimer on the website.

In addition, since FNArena runs a Model Portfolio based upon my research on All-Weather Performers it is more than likely that stocks mentioned are included in this Model Portfolio. For all questions about this: info@fnarena.com or via the direct messaging system on the website).

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