Week

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# Stories To Read From FNArena

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# Domino's Pizza Valuation Puzzles Brokers

While there are few catalysts available for Domino's Pizza at present, Morgans believes the stock warrants a more positive view. Others are more hesitant about the stock.

-AGM likely to reveal softer growth and first half may disappoint -Yet is the stock now undervalued? -Concerns over margins and share of the profit pool

By Eva Brocklehurst

What is the current state of play with Domino's Pizza Enterprises ((DMP))? Is it undervalued? The stock was sold off in the wake of the FY17 as technical problems affected its digital roll-out and earnings forecasts were missed.

Morgans has now decided to upgrade to Add from Hold. The broker accepts that the trading update at the AGM and the first half result could show softer growth in Australasia, given the exceptionally strong base being cycled, but Europe should be accelerating as technology/menu issues have now been resolved.

While not envisaging any upcoming catalysts for the stock, and acknowledging the potential for the AGM to disappoint, Morgans still takes a more positive view based on the fact Domino's Pizza (DMP) is now trading at a discount to its global peer group, despite offering superior growth. Domino's Pizza has guided to 20% growth in net profit for FY18.

The broker envisages the rolling out of stores, mid single-digit same-store-sales growth and margin improvement across all divisions should deliver this level of growth alone and remains comfortable with the company's guidance. Moreover, the buying back of the 25% stake in the Japanese business should be further accretive.

Valuation

Hence, the main question for Morgans centres on the right multiple for the stock going forward. Looking at the global peer group, the average price/earnings (PE) ratio for the next 12 months is 25x and the enterprise value/operating earnings (EBIT) ratio is 18.3x. Growth profiles vary, therefore Morgans believes the most appropriate comparison is the company's US parent, which trades on 30x and 21.7x, respectively.

On the broker's price target of $47.21, Domino's Pizza would trade at 28x and 20.8x, respectively, a discount to the parent, despite a superior growth profile and a less leveraged balance sheet.

Citi believes net profit guidance for FY18 can be met but the extent of upside is modest compared with history. The question of what is the right multiple for the stock also plagues Citi. The broker envisages headwinds to margins on the medium-term horizon, particularly for Australia. The broker's fair value P/E is 23x, given the balance of risks, and a Sell rating is maintained.

After the FY17 results Macquarie downgraded to Neutral from Outperform. Despite the fact much of the de-rating of the stock occurred ahead of the FY17 results, the broker envisages merit pulling back to Neutral because of concerns around the growth drivers and the earnings quality. The broker estimates the company's share of the profit pool outstripped the franchisees in FY17.

Wage inflation and compliance cost increases could exacerbate this trend, and the company's decision to stop disclosing this information reinforces the broker's concerns. Macquarie has also flagged the fact the company may take a number of years before the low value/high-volume model is accepted in Germany, following similar difficulties in France. This suggested the broker that growth may lag expectations should the model not catch on.

Deutsche Bank is also of the view that Domino's Pizza is taking too much from the profit pool. The main disappointment for this broker in the FY17 results was the announcement of a $300m buy-back. The stock delivers an earnings yield of 3-4% and this signals to Deutsche Bank that the buy-back will be barely accretive to earnings, let alone to value, and this will leave the group with too much debt.

Domino's, historically, has taken advantage of its high trading multiple to create value by buying franchises and new territories for lower multiples. The buy-back upturns this strategy and Deutsche Bank cannot comprehend why purchasing a business (DMP) which generates a 3-4% earnings yield can be sound use of shareholder funds.

FNArena's database shows three Buy ratings, two Hold and two Sell. The consensus target is $46.83, suggesting 7.1% upside to the last share price. Targets range from $38 (Deutsche Bank) to $60 (UBS).

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# Risks To The Downside For F&P Healthcare

Fisher & Paykel Healthcare may be capable of producing mid-teens growth for the next few years but the substantial run-up in its shares signals the risks are on the downside.

-Stock now substantially overvalued versus medical device peers -Risks associated with a potential change in NZ government -Growth in OSA market likely to slow

By Eva Brocklehurst

Fisher & Paykel Healthcare ((FPH)) may be a blue-chip NZ company capable of producing mid-teens organic growth for the next 3-5 years but the significant run-up in its share price suggests it is over-bought.

UBS believes so and downgrades the stock to Sell from Neutral. The share price is up 30% since the FY17 result in May and now trading at an all-time high one-year forward price/earnings ratio of 37, and at a 14% premium to the broker's de-risked valuation of NZ$11.35 a share.

Current earnings growth forecasts suggests the stock is now substantially overvalued relative to global medical device peers. UBS believes the three-year EPS growth profile would need to lift to around 25% pa from 16% pa to justify the current share price.

Macquarie has an Outperform rating, acknowledging the stock is trading at demanding multiples but remaining comforted by the company's expansion into adjacent businesses, which should allow mid-teens growth rates for some years to come.

There is also the possibility, UBS concedes, that a large portion of the recent strength in the share price reflects a temporary liquidity squeeze created by index-related buying and loyal Australasian shareholders with limited alternatives.

Nevertheless, scenario analysis suggests the risk is skewed to the downside, especially if the patent disputes with ResMed ((RMD)) in Obstructive Sleep Apnoea (OSA) or North American free trade agreement (NAFTA) negotiations do not go to plan, and growth slows.

Credit Suisse too finds the litigation an unwelcome distraction, although remains impressed by the fact the company achieved an 18% rise in net profit in FY17, despite litigation costs.

NZ Poll

UBS even suggests that the stock may be a good place to park amid risks associated with a potential change in the NZ government. Deutsche Bank agrees the recent polls point to an increased probability of a Labour-led government in New Zealand and suggests this could be a net positive for the stock.

Aside from the potential impact on the NZ dollar (weaker so far and a positive for FPH), the main change would be the way in which the government incentivises R&D. Labour's policy would add around 3.3% to the company's after-tax earnings. Fisher & Paykel Healthcare has received funding under the current government policy, capped at NZ$5m per year. Had Labour's policy applied to FY17, Deutsche Bank calculates the company would have received a NZ$10.5m tax credit.

Slowdown

UBS suggests a slowdown in global revenue growth for the OSA market to around 7% and 6% in 2017 and 2018 respectively, from 8% in 2016, is on the cards. The main question the broker ask is whether the company can maintain its double-digit constant-currency OSA revenue growth as new mask come towards the end of their traditional product life-cycle.

The broker believes structural industry factors will be the major drivers of market growth over the next few years. Incorporating analysis of what is driving the market, UBS suggests a stable market share for F&P Healthcare in FY18 followed by a gain of 0.5% in FY19 and FY20.

At its AGM, the company reiterated FY18 net profit guidance of NZ$180-190m, suggesting a slow start with first half net profit up just 2% on revenue of 8%. Moreover, UBS assesses this reflects lower growth in the traditional invasive ventilation hospital sales and higher legal costs. The broker does not envisage home care revenue growth will rise above 10% in FY18 and FY19.

That said, the broker acknowledges growing penetration of high-flow nasal cannula (HFNC) and long hospital product cycles, as well as reasonable OSA market growth, will underpinned mid-teens growth in earnings per share over the medium term.

The broker's analysis of clinical trials is supportive for HFNC over low-flow oxygen therapy for ICU and post-extubation patients but inconclusive for post cardiac surgery. Channel checks also suggest the company's new mask is driving a higher market share. There are two Buy ratings, two Hold and one Sell (UBS) for the stock on FNArena's database.

# Evolution Mining Parts With Edna May

Confirming speculation, Evolution Mining has sold the Edna May gold mine, divesting its smallest and highest cost asset.

-Viewed positively because of an improvement in margins and reduction in costs -Price realisation below value attributed while part of a larger portfolio -Evolution Mining's next move considered likely to be an acquisition

By Eva Brocklehurst

Evolution Mining ((EVN)) has fulfilled expectations by announcing the sale of Edna May. Ramelius Resources ((RMS)) will purchase the Western Australian gold mine for $40m in cash and up to $50m in extra payments involving royalties and/or scrip.

Edna May was considered an obvious divestment and updated production guidance signals falling costs, providing a positive impetus. The mine is one of the company's smallest and highest cost. The consideration is below the estimates of several brokers but the sale is still viewed positively because of an improvement in margins and reduction in costs.

Canaccord Genuity previously estimated a value of $136m for the mine, modelled on a four-year life and the commencement of underground production in late FY18. Contingent consideration is the largest component of the deal value and, even assuming the full consideration of $90m is ultimately paid, this remains some 34% below the broker's estimated value for the asset.

The broker suspects this soft valuation may centre on doubts around whether underground production will deliver the expected improvement in operating margins or, maybe, Evolution Mining's view of the potential life is below broker model assumptions.

The sale, representing only 4% of Canaccord Genuity's estimated net asset valuation for the stock, has little impact on the investment view. The broker, not one of the eight monitored daily on the FNArena database, retains a Hold rating and reduces its target by 2% to $2.25.

Edna May Valuation

The structure of the transaction is a demonstration of the differential pricing that is applied to mature, challenging assets versus high-quality assets, in Credit Suisse's view. As with the company's divestment of Pajingo the structure is complex and conditional. Price realisation is well below the value that was attributed by the market while the assets were part of a larger portfolio.

Macquarie assumes Edna May has 273,000 ounces of mineable inventory left to produce, leaving 73,000 ounces above the 200,000 ounces royalty trigger point. Using this estimate, the broker believes Edna May can deliver an additional $24.3m to Evolution Mining, if the stage III pit is mined, or $7.3m if Ramelius does not mine stage III.

The broker calculates a discrepancy in perceived value between the discounted cash flow valuation of Edna May and the likely total payments for the mine. This drives a minor reduction to the target. On the upside, the drag from high costs has been removed.

The company has indicated a $30/oz reduction in all-in sustainable costs (AISC) for the rest of FY18 via this divestment, and an annualised saving of $40-50/oz thereafter. The revised FY18 guidance is 750-805,000 ounces at AISC of $820-$870/oz versus prior guidance of 820-880,000 ounces at AISC of $850-900/oz.

Next Move

Credit Suisse does not expect the company to announce an acquisition in the near-term, as quality assets are not readily available and/or are priced at significant premiums to value. The broker downgrades to Neutral from Outperform and reduces its target to $2.22, reflecting an 8c reduction, on accounting for the sale below prior valuation.

Never say never, is Citi's view of the potential for another acquisition. The broker points to a good track record of value adding via M&A, although acknowledges management has been clear in its view that gold mines are currently too expensive and organic growth is preferred. While the sale reduces FY18 revenue there is less of a fall in terms of earnings per share, because the mine is high cost. It was one of the foundation assets of Evolution Mining.

UBS agrees the transaction price is on the low side, especially in the light of heightened competition for gold assets, Edna May has been an underperformer and lacks the significance of the other mines in the company's portfolio. Around 47% of the reserve is underground and UBS believes only minor capital expenditure would be needed to completely mine the remainder. Beyond this, more investment and exploration success would be required.

Post the divestments, the company sector-leading position within Australian gold miners is reinforced, UBS asserts, underscoring a preference for the stock. The company now holds six assets, at the lower end of its target of 6-8. UBS accepts this is not a hard rule but suggests, therefore, the next move is likely to be an acquisition.

FNArena's database shows four Buy ratings and three Hold. The consensus target is $2.52, signalling 7.9% upside to the last share price. Targets range from $2.22 (Credit Suisse) to $2.80 (Macquarie).

# Revenue Doldrums Beset Myer

Department store Myer is hampered by a weak consumer outlook and having trouble growing revenue. The arrival of Amazon in Australia is only expected to aggravate the situation.

-Increasingly reliant on cost reductions to stem losses -Business appears unable to grow top line without sacrificing margin -Brokers suggest targets need to be re-set

By Eva Brocklehurst

Department store Myer ((MYR)) is beset by a weak consumer outlook and the arrival of Amazon in Australia, with its strong online presence, is expected to aggravate the situation.

Cost reductions may provide some momentum in the near-term, but brokers suggest there is only so much that can be done in this regard. Myer reported a disappointing FY17 result, with sales declining -1.4%, driven in part by the closure of three stores. Another four stores will be closed over FY18-20.

UBS downgrades FY18-20 earnings estimates by -6-7% to reflect the company's statement that FY18 conditions are below expectations. While commentary implies comfort with FY18 consensus net profit estimates of around $66m, the broker envisages downside risk as top-line pressures intensify. UBS factors in three store closures across FY19-20.

Myer is now two years into a five-year turnaround strategy and has missed four out of its five medium-term targets. UBS acknowledges cost reductions should continue to soften the blow but pressures from Amazon and international fashion entrants will inhibit the company's ability to sustain growth in earnings. This is aggravated by the store chain's long and expensive lease tail. UBS retains a Sell rating.

Credit Suisse suggests the ongoing shift in customer shopping preferences is sitting uncomfortably with the company's large store incumbency and talk of resilience appears more hopeful than a reflection of reality. There is scant evidence that core stores are growing sales revenue and, with no compelling reason for revenue to improve, the broker expects earnings will continue to decline.

Sales Vs Margin

Aside from dealing with Amazon, Deutsche Bank explains Myer's conundrum thus: some years ago a formula was employed for growing gross margins by increasing the penetration of exclusive brands, but this came at the expense of sales and likely drove customers away from the format.

The subsequent new strategy was more sensible, with a focus on ranges customers wanted to buy, more discipline on discounting and bringing some theatre back to stores. Top-line sales improved as a result but this came at the expense of margin. The broker fears a renewed emphasis on exclusive brands may raise the old problem and suspects the business cannot grow the top line while maintaining gross margin.

Deutsche Bank suggests potential corporate interest is the main offset to the risks. In FY19 and beyond the broker expects earnings will be flat or slightly lower with continued mix-related gross margin pressure. This could be somewhat offset by reduced costs from space reductions and efficiency measures.

While recognising the productivity benefits that should come with closures, Morgan Stanley is not confident the sales will transfer to other stores and retains little optimism for future sales growth. Gross margins continue to decline, the broker observes, although cost controls and a shift towards concession sales in the mix helped stem the rate of decline.

Morgan Stanley's confidence in the company's sales strategy continues to wane as target metrics appear increasingly hard to achieve. As online and foreign retailers pressure sales, the broker believes the multiple currently factored into the stock adequately reflects a business that is increasingly relying on cost reductions to stem its losses.

Re-setting Targets

Morgan Stanley awaits the November 1 strategy briefing, suggesting the company does need to re-set its targets and retaining an Equal-weight rating based on the corporate appeal in the stock.

Citi agrees it is unrealistic to continue to target a 20% uplift in sales per square metre, 3% sales growth and 15% return on funds employed. It remains possible for operating earnings (EBITDA) growth to exceed sales growth off the low base, but the broker does not expect this to be achieved until FY19. Citi takes heart in the fact the company is actively addressing its cost base and trying to find the balance between gross margin and like-for-like sales growth.

Cost reductions through personnel are largely out of the way and Citi expects benefits from store closures and back-office rationalisation will provide support for earnings. Risk is considered priced in at current levels. Nevertheless, while sales growth is unlikely in the short term the broker agrees this is essential to stabilise the business.

The consensus target on FNArena's database is $0.83, suggesting 18.8% upside to the last share price. Targets range from $0.65 (UBS) to $0.95 (Citi). There are three Sell, three Hold and one Buy (Citi) ratings.

# Outlook Dims For TPG Telecom

The outlook has dimmed for TPG Telecom as it battles to offset margin pressures from the NBN by aggressively rolling out its mobile network.

-Dividend cut in FY17; assumptions for none or little out to FY20 -Subscriber growth continues to slow despite aggressive mobile offering -Capital outlay heading substantially higher

By Eva Brocklehurst

The outlook has dimmed substantially for TPG Telecom ((TPM)) as it battles to offset margin pressures from the NBN by aggressively rolling out its mobile network. Dividend payments were lower than expected in FY17 and the company has flagged a doubling of capital expenditure versus operating cash flow in FY18.

Capex will become substantially higher in the next few years as the mobile business in Australia and Singapore is built. Yet subscriber growth continues to slow, despite an aggressive mobile offering launched in March as a Vodafone re-seller.

Morgan Stanley envisages TPG as a stock presenting investors with higher risk but also higher potential returns, as the company is a disruptor in the consumer and corporate broadband market and soon to be so in mobile. The broker acknowledges the challenges from NBN-related margin pressures and competition but envisages a value opportunity in mobile investment which is under-rated by the market.

Morgan Stanley finds the reaffirmation of mobile capital expenditure and timing constructive, as well as the new bank lines for funding and a cut to the dividends. This all makes strategic and financial sense in the broker's view and an Overweight rating is maintained.

Mobile Transition

Citi agrees a transition to mobile requires a leap of faith and there are likely to be three years of negative cash flow, as the company builds up mobile networks at the same time that the migration to NBN compresses broadband margins. Revenue from these mobile networks is unlikely to flow prior to FY20. This suggests to the broker there is too much uncertainty over the level of future earnings.

Citi estimates the rising cost of NBN access will cut the company's consumer earnings by around -$200m over the next three years, with fixed voice also disappearing completely in that time. The broker expects consumer operating earnings to reach a low point of $306m in FY21.

The relationship between more attractively priced plans and subscriber growth appears to be weakening, Morgans suggests, as the company struggles to convert mobile payments into mobile subscriber growth. In the broker's opinion this illustrates that consumers are not just worried about getting the lowest price.

Credit Suisse also cites the drop-off in subscriber growth as a key concern ahead of the mobile network roll-out. The broker envisages the mobile strategy is high risk and retains an Underperform rating.

Deutsche Bank suggests the stock could offer longer term appeal if management is able to deliver on the Australian and Singapore mobile plans. Nonetheless, the stock faces earnings declines and a low dividend pay-out ratio as capital is conserved and the broker downgrades to Hold from Buy.

FY18 guidance is for underlying operating earnings (EBITDA) to decline -2-4% to $800-815m. Morgans believes this is a solid outcome, considering the substantial pressures on NBN margins. Credit Suisse forecasts net profit to fall -45% in FY19 as full mobile start-up costs and depreciation come through. The broker estimates market share was down to 24.9% of the end of FY17 versus 25.4% at the end of FY16.

FTTB (fibre-to-the-basement) net additions were also disappointing for the broker, at 13,000 in the second half. Macquarie notes the company appears to have slowed its rolling out of FTTB, given concerns about the regulatory environment. The company will apply to the ACCC to improve its functional separation of wholesale activities once legislation is enacted.

Dividends, Capital Outlay

The reduction in the dividend and the increase in the debt ceiling have helped alleviate concerns about another capital raising but Ord Minnett finds no positive catalysts over the next 6-12 months. The broker assumes the dividend will be completely eliminated over FY18-20 and could be reinstated in FY21, as the Australian and Singapore mobile businesses start to generate earnings.

Macquarie believes value will come from executing on mobile strategies and suggests there is some positive progress being made. While no guidance has been provided on forward pay-outs, the broker's FY18 dividend estimates are re-set to 4c per share, held until the end of the Australian roll-out. Any return to a higher dividend would, in the broker's opinion, signal management's increased confidence that the mobiles strategy is delivering.

Accounting Treatment

Management has changed segment disclosures and removes iiNet as a stand-alone segment, consolidating its result into the corporate and consumer segments. The company is also revising guidance for the treatment of spectrum amortisation which will now begin when the mobile network is ready for its intended use rather than from when the spectrum is available.

Morgans upgrades FY18 forecasts earnings per share by 10% but this is a function of the new accounting treatment, which capitalises a large portion of the company's mobile expenditure. In the broker's opinion the main upside and downside risk relates to the ability to deliver free cash flow and service increasing debt.

Macquarie observes business-as-usual capital expenditure will remain high in FY18, with guidance of $270-310m, including expenditure on the last part of the Vodafone network roll-out. On the positive side, management has indicated it is progressing discussions for mobile site access in Australia. TPG expects to have clusters of sites ready for service in Sydney, Melbourne and Canberra by mid-2018.

FNArena's database shows one Buy rating (Morgan Stanley), four Hold and three Sell. The consensus target is $5.62, suggesting 7.9% upside to the last share price. This compares with $6.51 ahead of the results. Targets range from $4.30 (Morgans) to $7.00 (Morgan Stanley).

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# Synlait Milk Energised For Growth

Brokers assess the outlook for Synlait Milk, which has had a strong run up in its shares on the strength of its relationship with a2 Milk.

-Looking to establish a Synlait Milk branding strategy -Transition to higher-margin canned infant formula and adult nutrition -Trade off on margin for greater certainty on volume likely

By Eva Brocklehurst

New Zealand's fourth-largest milk processor, Synlait Milk ((SM1)), has had a strong run up in its shares on the strength of its relationship with a2 Milk ((A2M)). The company is the exclusive supplier of infant formula to a2 Milk for that company's product base in China and Australasia.

Synlait Milk, as supplier of dairy ingredients, is a high-growth business with exposure to the agricultural supply chain, and management now considers the business can look to establish a brand, providing it does not conflict with existing relationships, and where it has significant consumer benefits.

This aspect of the company's FY17 results interested Macquarie, as it differs from the previous business-to-business focus.To achieve its strategy, the company will establish further manufacturing sites over time, believing the current balance sheet and projected earnings should provide sufficient funding.

Macquarie suggests this is helped by the abandoning of the building of the additional dryer on the current site at Dunsandel, which frees up $130m. Management has indicated further manufacturing would be established in New Zealand, given the quality of milk and market opportunities.

The new Auckland canning line and investments in flexible packaging capacity for infant formula and adult nutrition products are progressing. Beyond this, the company has highlighted the potential to develop manufacturing capacity in base powders for the infant formula segment.

Any new investment will be conditional on further growth in demand in advance of current projections but for the Bell Potter this highlights the optimism management has in the business. Furthermore, the broker envisages internalisation of the packaging of the a2 Milk adult nutrition product will be a potential profit driver in the second half. The broker estimates a2 Milk accounted for in excess of 80% of the company's consumer-packaged volumes and in excess of 30% of gross profit in FY17.

Outlook

No formal guidance was provided other than for canned infant formula volumes to be 30-35,000t in FY18, amid expectations of a step-up in profit in FY18 because of strong demand for infant formula. Bell Potter believes the transition towards higher margin canned infant formula and adult nutrition, and away from bulk dairy ingredients, remains a key driver of earnings, cash flow and value for the stock.

Following a stronger-than-expected FY17 result the broker upgrades forecasts for net profit by 5.5% in FY18 and FY19. Bell Potter, not one of the eight stockbrokers monitored daily on the FNArena database, lifts its target to NZ$6.07 from NZ$5.20 and maintains a Buy rating.

Deutsche Bank downgrades to Hold from Buy. This is based on a strong re-rating to a level where the stock now reflects the growth potential. Also, the broker points out regulatory processes are still in train for the company's key infant formula customers.

Credit Suisse takes an even more cautious approach and would like to be confident in the transition through regulatory changes in China. While downgrading to Underperform from Neutral, the broker is not suggesting the company cannot meet market expectations but seeks a further de-risking of the company's prospects. If this occurs then valuation should follow the share price.

The broker continues to base long-term forecasts on a reasonable return on investment for a contract manufacturing business. The momentum in the company's key customer, a2 Milk, is such that further growth in volume and profitability can be expected but Credit Suisse, too, observes a number of hurdles to mount.

The China Food and Drug Administration is currently reviewing both applications for registration of imported product, with a new regulatory framework to begin January 1, 2018. Credit Suisse also points out that a2 Milk sales are heavily skewed to product that goes into China through various informal channels.

Moreover, the broker believes margins the company is currently enjoying from a2 Milk will not necessarily endure for the longer term and a trade-off for greater certainty on volume is likely to ensue.

Munchkin

Meanwhile, Bell Potter envisages scope for the Munchkin infant formula grass-fed product to become the growth story in the fourth quarter of FY18 based on the success of the grass-fed beef sector. The last hurdle is to gain US FDA approval.

This is a key prospective customer the company has been working with over the last two years. Munchkin is looking to launch infant formula in the US, providing the company with geographic and customer diversity.

# Nib Grows Corporate Health, Yet Risks Prevail

Brokers are positive about the acquisition of GU Corporate Health as it expands coverage in a growing segment, yet nib Holdings still faces an uncertain outlook in mainstream private health insurance.

-GU has grown premium revenue considerably but net margin has come down significantly -Could grow materially if employer-funded health care increases in Australia -Yet, private health insurance margins are peaking and policy numbers declining

By Eva Brocklehurst

Nib Holdings ((NHF)) will acquire specialist corporate health insurer Grand United Corporate Health for $155.5m. Brokers are positive about the acquisition as it expands coverage in a growing segment, yet nib still faces an uncertain outlook in mainstream private health insurance.

The company will issue up to $75m in equity and the remainder will be funded from a new debt facility. Underlying operating profit has been upgraded for FY18 as a result of the acquisition to "at least $155m".

Morgans upgrades estimates slightly on the back of the acquisition and believes it makes strategic sense to add to core business and accelerate growth in the corporate segment. Moreover, the broker asserts the acquisition diversifies the distribution mix through another channel outside of the direct business, although remains somewhat cautious because of cyclically-high health insurance industry margins.

Credit Suisse supports the strategy of diversifying away from mainstream private health insurance, but cautions that acquisitions are not without risk, as was the case with the company's recent acquisition in travel insurance. While deeming such acquisitions are still worth exploring, the broker does not ascribe significant growth or value in their initial stages.

The transaction is one of the best M&A deals Deutsche Bank has witnessed in recent years. It is in-market and a product the company knows. The transaction size is large enough to be meaningful, without being so large as to overwhelm management's ability to execute, and nib has a strong record of delivering.

The broker also notes corporate health insurance is rapidly growing as, while the number of general policies in Australia is falling, GU Health has grown by 4.4% over the past four years. Deutsche Bank suggests alternative products such as employer-funded health care could become increasingly important in the Australian landscape.

GU Health

GU Health is the only established specialist corporate health insurer in Australia and services over 34,000 policy holders across 260 corporate clients. This is a logical strategic fit, in Morgans' view, and should broadly double nib's corporate member numbers, providing a stronger platform for future growth.

Credit Suisse believes earnings accretion will be dependent on what becomes a sustainable level of earnings. GU Health has grown its premium revenue considerably in recent years, but during this period the net margin has also come down significantly, now sitting below the industry level, at 4.1% versus 5.4%.

Goldman Sachs notes GU has built a strong presence in the fully-funded employee health insurance segment in Australia. These policy holders represent around 35% of the GU space. Such policy holders are attractive for insurers, as the insurer obtains a proportion of policies from people who would not normally be buying health insurance. The remainder are required from voluntary corporate health plans.

Relative to the retail market, this type of insurance is typically characterised by a younger working age demographic and there are lower levels of policy churn. Nevertheless, the bargaining power lies with the corporate client and contracts are generally negotiated on an annual basis. Goldman Sachs, not one of the eight stockbrokers monitored daily on the FNArena database, has a Neutral rating and $5.33 target.

Macquarie believes an Outperform rating is supported by nib's operating performance. The acquisition leverages the combined business to around 20% market share by policy count in the growing corporate channel, where the broker observes customers are "rusted on". The acquisition also provides options for a channel that could grow materially if more corporates start providing health payments to employees as affordability becomes an issue.

Deutsche Bank also lauds nib for its embrace of technology and efficiencies, albeit some headwinds are on the horizon regarding margins from the expected increases in utilisation and the normalisation of reinsurance costs. Hence, the broker retains a Hold rating.

Risks Prevail

The price may be attractive and the portfolio provide a platform to expand in the corporate segment but, given elevated margin and growth risks, Morgan Stanley does not change its view. The broker recently downgraded the stock because of elevated trading multiples, against a backdrop of peaking margins and declining growth.

A structurally challenged market that is shrinking, in which adverse risk selection is rising and competition increasing, is considered a valid reason to stick with an Underweight rating.

Citi approves the expansion into lower-margin but more stable channels and suspects there may be some longer-term capital benefits from merging the health funds that are not yet in view. The company, consistent with Citi's industry feedback, now expects little more in terms of favourable health industry reforms, other than additional prosthesis savings.

The broker suggests even these reforms are probably going to be offset by lower premium rate increases. Citi considers the upgraded guidance still conservative. Nevertheless, the stock appears expensive from a valuation perspective and a Sell call is retained.

FNArena's database shows three Sell ratings, two Hold and two Buy. The consensus target is $5.71, signalling -1.0% downside to the last share price. This compares with $5.58 ahead of the announcement. Targets range from $4.95 (Morgan Stanley) to $6.50 (Macquarie).

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# Solid Short-Term Outlook For Brickworks

Brickworks continues to derive benefit from strong construction activity on Australia's east coast but, beyond the next 6-12 months, the outlook is more uncertain.

-Rising energy costs envisaged eroding margins in FY18 -Property earnings and profits expected to ease from highs -Strong building product order book, not expecting demand to slow for 12 months

By Eva Brocklehurst

Brickworks ((BKW)) is confident in the short-term outlook for building products, particularly on Australia's east coast. Nevertheless, brokers consider the outlook becomes more uncertain as FY18 progresses, because of higher energy costs and slowing building activity.

Macquarie assesses the headwinds to growth are very real. Rising energy costs are removing the shine from building product margins while property & development profits are expected to decline. The broker observes the stock has de-rated, down -12% since May, and is trading below historical norms, while there are no clear catalysts to drive a re-rating, given the context of these headwinds and a mature building cycle.

Still, Macquarie likes the fact the company moved pre-emptively to secure price increases to offset a $20m annualised energy cost impost, predominantly involving the brick business. An average price increase of 6.6% has been realised across brick operations as of July 1.

Morgans flags the good exposure to the residential construction market which has served Brickworks well in recent years. While the slowing of activity and higher energy costs should be mitigated by the company's cross holding in WH Soul Pattinson ((SOL)), and land & development activity, the stock appears fully valued at current levels.

Rising energy costs may be offset by strong price increases across the portfolio but Bell Potter suggests this will only be sufficient to cover increasing gas electricity costs, leaving little margin for cost inflation across other inputs, or for declining activity levels.

As such, the broker expects relatively flat earnings for building products in FY18. In contrast, the broker is very positive about the property pipeline, as higher development activity is underway at both Oakdale Central and Rochedale.

The company is also seeking bolt-on acquisitions and Macquarie assumes its intentions are to augment the building products portfolio with niche products.

Building

Underlying operating earnings (EBIT) declined -13.7% for building products in FY17 as the contribution from Western Australia was down by - $12m and only partly offset by higher earnings of $7.3m from the eastern coast.

Deutsche Bank is concerned about this decline, although acknowledges the negative contribution of Western Australia in FY17, where the business is undergoing a restructuring, and a -$5m impact from Cyclone Debbie, both of which are unlikely to be repeated. In response to the difficult conditions in WA the company has undertaken significant restructuring activity and closed six plants, placing the business in a better position to operate capacity in line with demand.

Management expects the east coast to stay strong, given what is in the order book for the next six months, while its builder customers do not expect demand to slow for the next 12 months. As housing demand on the east coast is still robust and the company has managed to deliver 2017 price increases to more than offset cost increases, Deutsche Bank believes 110 basis points of margin expansion is still likely in FY18, to 9.6%.

The broker accepts increasing energy costs are a heightened concern for the second half onwards so does not expect margin expansion beyond FY18. The company increased its dividend, continuing a track record of longer-term increases.

Property & Development

Land & development revenue for FY17 increased significantly, to $78.3m from $2.4m in FY16. The result was primarily driven by higher contributions from land sales. Citi expects lower earnings in property will occur in FY18 because there are no plans for major land sales.

Property trust distributions increased 20%, supported by completed developments. Macquarie observes the sale of Oakdale West has created a high base in FY17 which is not likely to be repeated.

Bell Potter expects a further 120,000 square metres of development to be completed in FY18, leading to a forecast $20.8m in rental income and a forecast net asset valuation for the company share of the trust of around $540m. Acknowledging earnings will be lower in FY18 because of a one-off substantial land sale in FY17, excluding that item, the broker expects comparable earnings should be well ahead.

Bell Potter, not one of the eight stockbrokers monitored daily on the FNArena database, reduces its price target to $13.85 from $14.38. Stripping out the post-tax Washington Soul Pattinson ((SOL)) contribution and property valuations, the implied valuation sits within the broker's blended target range and, hence, a Hold rating is retained.

FNArena's database has one Buy rating (Deutsche Bank) and three Hold. The consensus target is $14.53, suggesting 5.7% upside to the last share price the dividend yield on FY18 and FY19 forecasts is 4.0%.

# Weekly Ratings, Targets, Forecast Changes

By Rudi Filapek-Vandyck, Editor FNArena

Guide:

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

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

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

Summary

Period: Monday September 11 to Friday September 15, 2017 Total Upgrades: 7 Total Downgrades: 8 Net Ratings Breakdown: Buy 41.41%; Hold 42.28%; Sell 16.31%

The Australian share market remains desperately in need of a powerful catalyst, but it isn't coming from the stockbroking community. For the week ending Friday, 15th September 2017, FNArena registered seven upgrades in rating by analysts, and some of these involve companies whose share price was considered to have become too cheap, but the other side of the ledger still showed eight downgrades.

CommBank was among those receiving an upgrade, but it was also the sole upgrade that only went up to Neutral. All others went to Buy, including for Macquarie, Link Administration, Downer EDI and Cleanaway Waste Management.

The flipside saw four downgrades (50%) sink to Sell ratings, including Bank of Queensland, Myer and Newcrest Mining.

Myer and Smartgroup took the honours for target price upgrades for the week, both enjoying a lift above 10%, followed by, at arm's length, Regis Resources, Cleanaway Waste Management and Downer EDI. The negative side only involves two names: Vocus Communications and Commbank, and both only experienced relatively minor cuts to consensus targets; less than -2% in both cases.

Myer also ranks second for positive revisions to earnings estimates, only beaten by Macquarie Atlas Group, followed by Orocobre, Senex Energy and Santos. While those adjustments remain sizeable, the negative side was again rather tepid. Sigma Healthcare was the week's biggest loser with a reduction of no more than -1.26%.

That's the good news story from September: earnings estimates have stopped falling, as have price targets.

Upgrade

COMMONWEALTH BANK OF AUSTRALIA ((CBA)) Upgrade to Neutral from Underperform by Macquarie .B/H/S: 0/6/2

Macquarie observes the bank's historical premium of around 10-15% has been eroded in recent months and CBA is now on a similar multiple to its major bank peers.

While recognising the risk of near-term underperformance, the broker envisages current valuations are more appealing.

While considering it too early to have an Outperform recommendation, the broker believes it justified to upgrade to Neutral from Underperform. Target is reduced to $78.00 from $80.50.

CLEANAWAY WASTE MANAGEMENT LIMITED ((CWY)) Upgrade to Add from Hold by Morgans .B/H/S: 2/4/0

The CEO has highlighted the robust and growing revenue, operating leverage and a strong balance sheet. Morgans revises its forecasts to align with the company's expectations. This results in around 2% upgrades to FY19-20 forecasts.

As well as a change in valuation methodology, this lifts the target to $1.60 from $1.37. The broker upgrades to Add from Hold given the positive momentum being generated.

DOWNER EDI LIMITED ((DOW)) Upgrade to Buy from Hold by Deutsche Bank .B/H/S: 2/2/1

The company's FY17 result demonstrated the core business is performing well with a robust outlook.

While Deutsche Bank believes the company faces integration issues with the Spotless ((SPO)) acquisition and a potential downgrade to Spotless' FY18 guidance, this is considered well-known and reflected in the share price.

The broker upgrades to Buy from Hold and raises the target to $7.45 from $6.62.

HEALTHSCOPE LIMITED ((HSO)) Upgrade to Buy from Hold by Ord Minnett .B/H/S: 3/2/1

Ord Minnett believes Healthscope will face another challenging year as earnings are set to contract, given a number of Victorian hospitals are tracking below plan.

Value has emerged, however, as the stock is trading well below is 2014 IPO price despite adding more than $500m in new capacity.

The broker upgrades to Buy from Hold. Target is $2.

LINK ADMINISTRATION HOLDINGS LIMITED ((LNK)) Upgrade to Buy from Neutral by UBS .B/H/S: 5/0/1

Despite consistently delivering earnings that are ahead of expectations the shares steadily de-rated, UBS observes, amid concerns about stagnant funds administration revenue and the recent acquisition.

Nevertheless, UBS suggests super account consolidation headwinds will ease and the company's low fees versus the industry set it up to be the beneficiary of mergers.

UBS envisages compelling value in what it describes as a defensive and highly cash generating financial infrastructure exposure. Rating is upgraded to Buy from Neutral. Target is raised to $8.85 from $8.55.

MACQUARIE GROUP LIMITED ((MQG)) Upgrade to Buy from Neutral by UBS .B/H/S: 1/5/1

Macquarie Group has signalled that, as a result of stronger performance fees to be recognised in the first half, results are likely to be above the prior corresponding half and broadly aligned with the second half of FY17.

Following the update, UBS upgrades FY18 forecasts by 3% and expects net profit growth of 6.4%. As the shares have pulled back, the broker upgrades to Buy from Neutral.

Although the revenue outlook remains subdued, the broker continues to expect upside as operating leverage is delivered. Target is $91.

SUPERLOOP LIMITED ((SLC)) Upgrade to Add from Hold by Morgans .B/H/S: 1/0/0

In July 2016 Morgans downgraded Superloop to Hold on the belief investors were getting ahead of themselves in valuing the growth of a business that will take some time, leading to the possibility of disappointment. But investors have now weathered that "trough of disillusionment" (sic) and the broker believes operational risk is skewed to the upside.

The last twelve months have seen strong sales in Singapore, completion of the Hong Kong network, expansion of the Australian network, a strengthened sales team and a track record that is starting to deliver solid sales growth. Morgans upgrades to Add. Target rises to $2.81 from $2.15.

Downgrade

BANK OF QUEENSLAND LIMITED ((BOQ)) Downgrade to Underperform from Outperform by Macquarie .B/H/S: 1/5/2

Macquarie continues to expect regional banks to benefit from mortgage re-pricing and an improved funding environment. The broker believes Bank of Queensland's recent re-rating more than captures the upside.

The broker also notes that slowing credit growth and potential longer-term headwinds to mortgage profitability do not bode well for the bank in the medium term.

Macquarie downgrades to Underperform from Outperform. Target unchanged at $12.50.

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

Ord Minnett suggests the improved earnings outlook is increasingly reflected in the share price. On that basis, the broker downgrades to Hold from Accumulate and lowers the target to $11.00 from $11.50.

The broker remains upbeat on the prospects for earnings growth, noting some prospect of a working capital release, although offset by increasing capital expenditure.

This stock is not covered in-house by Ord Minnett. Instead, the broker whitelabels research by JP Morgan.

EVOLUTION MINING LIMITED ((EVN)) Downgrade to Hold from Buy by Deutsche Bank .B/H/S: 5/2/0

Deutsche Bank considers the gold sector now fully valued. The ASX gold index is up 15% since the start of the reporting season and the Australian dollar gold price is up 4%.

The broker incorporates a proposed 3.75% WA state royalty and believes this is a marginal drag on sector valuations. Evolution Mining is downgraded to Hold from Buy on valuation. Target is $2.50.

ILUKA RESOURCES LIMITED ((ILU)) Downgrade to Neutral from Outperform by Credit Suisse .B/H/S: 2/3/2

The company has announced a US$130/t increase to its zircon reference price, to US$1230/t, effective October 1. Credit Suisse's view on a continued recovery in mineral sands markets is unchanged and zircon supply is notably tight.

Yet, the broker believes the stock is fairly priced at current levels. Moreover, a stubbornly high Australian dollar could continue to be an impediment in 2018. Hence, a downgrade to Neutral from Outperform. Target is reduced to $9.85 from $9.90.

MYER HOLDINGS LIMITED ((MYR)) Downgrade to Underperform from Neutral by Credit Suisse .B/H/S: 1/3/2

Credit Suisse observes the results displayed declining sales and non-repeatable benefits from cost reductions at head office. FY18 forecasts are boosted by lower depreciation as a result of advancing store closure assumptions.

As there is a lack of evidence showing there is a core of stores for which sales revenue is growing, the outlook hinges mainly on accelerating cost reductions, in the broker's view.

Rating is downgraded to Underperform from Neutral. Target is reduced to $0.67 from $0.72.

NEWCREST MINING LIMITED ((NCM)) Downgrade to Sell from Hold by Deutsche Bank .B/H/S: 0/4/4

Deutsche Bank considers the gold sector now fully valued. The ASX gold index is up 15% since the start of the reporting season and the Australian dollar gold price is up 4%.

The broker incorporates a proposed 3.75% WA state royalty and believes this is a marginal drag on sector valuations. Newcrest is downgraded on valuation.

Rating is downgraded to Sell from Hold. Target is $19.

NORTHERN STAR RESOURCES LTD ((NST)) Downgrade to Sell from Hold by Deutsche Bank .B/H/S: 0/4/2

Deutsche Bank considers the gold sector now fully valued. The ASX gold index is up 15% since the start of the reporting season and the Australian dollar gold price is up 4%.

The broker incorporates a proposed 3.75% WA state royalty and believes this is a marginal drag on sector valuations. Northern Star is downgraded to Sell from Hold on valuation. Target is reduced to $4.40 from $4.50.

SIRTEX MEDICAL LIMITED ((SRX)) Downgrade to Hold from Add by Morgans .B/H/S: 2/1/0

Morgans believes intense competition, ongoing legal battles and no specifics around a viable forward strategy limits the upside for the stock.

The broker downgrades to Hold from Add. Target is steady at $16.53.

Total Recommendations Recommendation Changes

Broker Recommendation Breakup

Broker Rating Order Company New Rating Old Rating Broker Upgrade 1 CLEANAWAY WASTE MANAGEMENT LIMITED Buy Neutral Morgans 2 COMMONWEALTH BANK OF AUSTRALIA Neutral Sell Macquarie 3 DOWNER EDI LIMITED Buy Neutral Deutsche Bank 4 HEALTHSCOPE LIMITED Buy Neutral Ord Minnett 5 LINK ADMINISTRATION HOLDINGS LIMITED Buy Neutral UBS 6 MACQUARIE GROUP LIMITED Buy Neutral UBS 7 SUPERLOOP LIMITED Buy Neutral Morgans Downgrade 8 BANK OF QUEENSLAND LIMITED Sell Buy Macquarie 9 BREVILLE GROUP LIMITED Neutral Buy Ord Minnett 10 EVOLUTION MINING LIMITED Neutral Buy Deutsche Bank 11 ILUKA RESOURCES LIMITED Neutral Buy Credit Suisse 12 MYER HOLDINGS LIMITED Sell Neutral Credit Suisse 13 NEWCREST MINING LIMITED Sell Neutral Deutsche Bank 14

NORTHERN STAR RESOURCES LTD Sell Neutral Deutsche Bank 15 SIRTEX MEDICAL LIMITED Neutral Buy Morgans Recommendation Positive Change Covered by > 2 Brokers Order Symbol Company New Rating Previous Rating Change Recs 1 LNK LINK ADMINISTRATION HOLDINGS LIMITED 67.0% 50.0% 17.0% 6 2 HSO HEALTHSCOPE LIMITED 33.0% 17.0% 16.0% 6 3 CWY CLEANAWAY WASTE MANAGEMENT LIMITED 33.0% 17.0% 16.0% 6 4 DOW DOWNER EDI LIMITED 8.0% -8.0% 16.0% 6 5 CBA COMMONWEALTH BANK OF AUSTRALIA -25.0% -38.0% 13.0% 8 6 VOC VOCUS COMMUNICATIONS LIMITED -6.0% -13.0% 7.0% 8 7 SXY SENEX ENERGY LIMITED 71.0% 67.0% 4.0% 7 Negative Change Covered by > 2 Brokers Order Symbol Company New Rating Previous Rating Change Recs 1 SRX SIRTEX MEDICAL LIMITED 67.0% 100.0% -33.0% 3 2 BOQ BANK OF QUEENSLAND LIMITED -13.0% 13.0% -26.0% 8 3 EVN EVOLUTION MINING LIMITED 71.0% 86.0% -15.0% 7 4 MYR MYER HOLDINGS LIMITED -21.0% -7.0% -14.0% 7 5 RRL REGIS RESOURCES LIMITED -63.0% -50.0% -13.0% 8 6 NCM NEWCREST MINING LIMITED -50.0% -38.0% -12.0% 8 7 SIQ SMARTGROUP CORPORATION LTD 75.0% 80.0% -5.0% 6 Target Price Positive Change Covered by > 2 Brokers Order Symbol Company New Target Previous Target Change Recs 1 MYR MYER HOLDINGS LIMITED 0.826 0.747 10.58% 7 2 SIQ SMARTGROUP CORPORATION LTD 9.275 8.412 10.26% 6 3 RRL REGIS RESOURCES LIMITED 3.616 3.480 3.91% 8 4 CWY CLEANAWAY WASTE MANAGEMENT LIMITED 1.433 1.395 2.72% 6 5 DOW DOWNER EDI LIMITED 6.713 6.575 2.10% 6 6 LNK LINK ADMINISTRATION HOLDINGS LIMITED 8.640 8.590 0.58% 6 Negative Change Covered by > 2 Brokers Order Symbol Company New Target Previous Target Change Recs 1 VOC VOCUS COMMUNICATIONS LIMITED 2.679 2.716 -1.36% 8 2 CBA COMMONWEALTH BANK OF AUSTRALIA 78.538 79.475 -1.18% 8 Earning Forecast Positive Change Covered by > 2 Brokers Order Symbol Company New EF Previous EF Change Recs 1 MQA MACQUARIE ATLAS ROADS GROUP 54.634 44.094 23.90% 6 2 MYR MYER HOLDINGS LIMITED 7.664 6.429 19.21% 7 3 ORE OROCOBRE LIMITED 15.020 13.020 15.36% 6 4 SXY SENEX ENERGY LIMITED -0.189 -0.221 14.48% 7 5 STO SANTOS LIMITED 13.703 12.725 7.69% 8 6 BLD BORAL LIMITED 35.720 35.149 1.62% 7 7 HSO HEALTHSCOPE LIMITED 10.581 10.439 1.36% 6 8 OGC OCEANAGOLD CORPORATION 37.158 36.773 1.05% 6 9 LNK LINK ADMINISTRATION HOLDINGS LIMITED 35.213 34.880 0.95% 6 10 PTM PLATINUM ASSET MANAGEMENT LIMITED 28.125 27.875 0.90% 4 Negative Change Covered by > 2 Brokers Order Symbol Company New EF Previous EF Change Recs 1 SIG SIGMA HEALTHCARE LIMITED 5.628 5.700 -1.26% 4 2 GNC GRAINCORP LIMITED 67.907 68.740 -1.21% 5 3 TPM TPG TELECOM LIMITED 46.416 46.916 -1.07% 8 4 EVN EVOLUTION MINING LIMITED 17.857 18.014 -0.87% 7 5 ORI ORICA LIMITED 106.038 106.788 -0.70% 8 6 TAH TABCORP HOLDINGS LIMITED 22.233 22.370 -0.61% 4 7 SBM ST BARBARA LIMITED 29.995 30.170 -0.58% 4 8 SYR SYRAH RESOURCES LIMITED -9.019 -8.979 -0.45% 5 9 CTD CORPORATE TRAVEL MANAGEMENT LIMITED 75.980 76.180 -0.26% 5 10 AMC AMCOR LIMITED 88.452 88.642 -0.21% 8 Technical limitations

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

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# Uranium Week: All Talk But Little Action

Nuclear will be the second fastest growing source of global energy out to 2040, the EIA forecast last week, but minimal impact was felt in uranium markets.

By Greg Peel

Over the period 2015-40, world energy consumption is forecast by the US Energy Information Agency to grow by 28%. To provide for that growth in demand, renewable energy sources are forecast to see the fastest growth, of 2.3% per annum, followed by nuclear power at 1.5%.

The demand for coal is expected to remain flat as coal-fired generation is increasingly replaced by gas-fired, renewable and nuclear sources and the demand for coal in industrial processes weakens.

Some 60% of growth in global energy demand is expected from China and other non-OECD Asian countries.

The Pakistani prime minister last week inaugurated the country's fifth nuclear power plant, built by the Chinese.

Painfully Incremental Progress

This all should have been good news for uranium markets last week but the spot market managed only three transactions, and while industry consultant TradeTech's spot price indicator rose for a fourth consecutive week, at US10c to US$20.75/lb any gains remain painfully incremental.

Several utilities are currently considering offers for term delivery contracts but no transactions were reported last week. TradeTech's term price indicators remain at US$24.30/lb (mid) and US$31.00/lb (long).

To be fair, the industry did gather in London last week for the annual World Nuclear Association Symposium. Typically, activity drops off each year with many participants away from their desks. But there's no denying any positive reports, albeit long term in perspective, are currently failing to convert to increased activity in uranium markets.

Rather, the same record keeps playing. Japan's regulator last week delayed approval of Tokyo Power Co's request to restart Kashiwazaki-Kariwa units 6 and 7 pending the company's lodging of safety codes and procedures.

[U3O8]

# The Short Report

Guide:

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

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

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

Summary:

Week ending September 14, 2017

Last week saw the ASX200 once again rally from the bottom of the range towards the top.

We were watching to see if there were any short-covering evident in lithium miner Galaxy Resources ((GXY)) last week given its sudden share price spike but since that spike the share price has come off again. Galaxy may well be the most volatile stock on the market at present.

Galaxy shorts are down only to 10.7% from 11.3%.

This week's ASIC table shows Japara Healthcare ((JHC)) shorts falling to 5.8% from 8.0% despite no new news since the company's result in August. I'm going to straight away call that an ASIC data blip.

Hospital owner Healthscope ((HSO)) is not quite a Mover & Shaker this week despite an increase to 10.4% shorted from 9.4% shorted because the stock has been rising steadily up the table for weeks, particularly since a poor earnings result, given a very challenging environment.

Another similarly quiet mover is Rio Tinto ((RIO)), which has now snuck into the 8% bracket from the 7%. It's not the first time Rio has risen up the table before falling back again and I suspect shorts likely reflect a pairs trade against rival BHP ((BHP)).

In terms of actual Movers & Shakers, this week we examine moves in Mayne Pharma ((MYX)), Retail Food Group ((RFG)) and Ardent Leisure ((AAD)).

Weekly short positions as a percentage of market cap:

10%+

SYR 20.2 ORE 16.4 MYR 15.3 IGO 15.1 WSA 14.4 RFG 14.2 SHV 13.3 JBH 13.2 DMP 13.0 ACX 11.7 GXY 10.7 HVN 10.6 AAD 10.4 HSO 10.4 MTS 10.0

In: HSO Out: MYX

9.0-9.9%

ISD, APO Out: HSO, GTY

8.0-8.9%

GTY, MYX, NXT, QIN, RIO

In: MYX, GTY, RIO Out: JHC

7.0-7.9%

AHG, BKL, VOC, FLT, TPM, VRT

In: VOC, VRT Out: RIO, GXL

6.0-6.9%

GXL, NEC, NSR, NWS, MND, SEK, SAR, TAH, IPD, BEN, AAC, HT1

In: GXL, HT1 Out: VOC, VRT, NVT

5.0-5.9%

BWX, JHC, SDA, PRU, BAP, OFX, IPH, MSB, KAR, GMA, CCP, CSV, ING, QUB, A2M, RCG, CSR, OSH, MQA, AWE CTD, WOW

In: JHC, CSR. MQA, AWE Out: HT1, CTD, WOW

Movers and Shakers

Mayne Pharma has been on a downward trajectory, consistent with its US peers, ever since both presidential candidates campaigned on looking into drug prices. The company did enjoy some reprieve last week nevertheless when the Therapeutic Goods Administration approved two new products for the Australian market.

Mayne has long been in the 10% plus shorted club despite the aforementioned downward trajectory, suggesting shorters were happy to hang on, but this news sparked a scramble and Mayne shorts fell to 8.8% from 10.5%.

Retail Food Group owns franchises in various food outlets covering coffee and cafes, such as Gloria Jean's, pizza, such as Crust, and bakeries, such as Donut King and Michel's Patisserie. The company's FY17 result, released at the end of August, showed all brands posted weaker sales other than Donut King.

RFG had issued a profit warning beforehand and the result held no further surprises but the share price had fallen -14% up to last week before stabilising this week. UBS, the only FNArena database broker covering the stock, questioned FY18 profit growth guidance of 6% and has forecast 1.5% instead.

Last week RFG shorts rose to 14.2% from 12.6%.

Just when you thought things couldn't get any worse for Ardent Leisure, they did. The Dreamworld tragedy continues to keep the punters away and the company's flagship Main Event centres had been struggling before analysts warmed to a bit of rationalisation of the business. But the bulk of those centres are in Texas.

And along came Harvey. Last week shorters took the opportunity of further share price falls to reduce positions to 10.4% from 11.8%.

ASX20 Short Positions (%)

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

IMPORTANT INFORMATION ABOUT THIS REPORT

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

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

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

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

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

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

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

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

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# The Wrap: Insurance, Media, Office And NZ

Weekly Broker Wrap: Insurance; media; office; and the NZ election.

-Competition still eroding market share of IAG and SUN -Consolidation to be the main game across media sector -Stronger Sydney office environment emerging -Change in NZ government has implications for ASX200 stocks

By Eva Brocklehurst

Insurance

UBS suggests FY17 was a pivotal turning point for the profit momentum in general insurance. The broker argues, based on a deep dive into APRA statistics, that industry fundamentals are now more supportive of a recovery in margins, admittedly off a lower base.

While retaining key concerns about such specifics as management instability at QBE Insurance ((QBE)) and a questionable execution on strategy at Suncorp ((SUN)), the broker believes these are outweighed by valuation support and the improving profit cycle.

FY17 results from Youi signal the slowdown evident in the first half has continued, with gross written premium shrinking 1.7% in the second half. UBS observes, for the first time since Youi commenced operations in 2009, the major domestic insurers delivered better premium growth.

Moreover, in an environment where most insurers are pushing through rate increases, management's comments that the Australian market continues to experience soft pricing appear at odds. On balance, UBS expects the company will adopt a rational approach to lifting prices across personal lines.

While the threat from challenger brands appears to be slowing, competition across the broader market is still eroding share for Insurance Australia Group ((IAG)) and Suncorp, in Macquarie's view. Youi has also confirmed it will enter the NSW CTP market in FY18 and Macquarie understands that at least 20% of customers bundle CTP with home and motor insurance, making a highly profitable portion of the market inaccessible for insurers without a CTP offering.

Thus, entering the NSW CTP market, worth $2.4bn, should unlock customers for Youi. Macquarie suggests competition by many insurers on state and product specific grounds will continue to erode market share for the majors.

Bell Potter expects, based on international climate models, that a La Nina event may be reached by January 2018. This would imply wetter conditions in Australia. The next El Niño southern oscillation index report from the Bureau of Meteorology on September 26 should provide more guidance. A neutral summer should be good for insurers and a weak-to-moderate La Nina should be manageable, in the broker's opinion.

Bell Potter observes QBE would outperform IAG and Suncorp in any domestic catastrophe event, given its smaller Australian footprint. Based on the broker's analysis, cyclones & storms are more benign than hail and/or flood events on the east coast for the insurers. The former are easier to pre-empt whereas the latter are more inclined to affect densely populated areas.

Media

Morgan Stanley expects consolidation will be the main game across Australia's media industry in the wake of the government achieving Senate approval to relax ownership rules. Approval to remove the two-from-three and audience reach rules presents an opportunity to re-configure the media landscape.

The broker considers the key debate is whether, after any higher growth/better quality media companies emerge, the downside trajectory in earnings and shareholder value resumes. The broker envisages some opportunity to re-invent businesses but still remains a structural bear on traditional media stocks.

The changes are considered to be overdue and arguably too little too late. Still, consolidation would be better than the status quo, in the broker's opinion. Morgan Stanley also expects cost savings to be the primary driver of growth in earnings per share and free cash flow in most M&A deals.

The majority are expected to be share-based offers, commonly with little or no premium. This is because the rate of change in technology and consumer behaviour is accelerating and this makes it difficult to assess relative value. Some of the best opportunities to create value may come from selling assets rather than buying such as the case with the ex-Domain assets of Fairfax Media ((FXJ)).

Office

Citi believes the near-term outlook for the Sydney office market is strong, given accelerating rents, falling incentives and the potential for growth in re-leasing spreads. The broker believes rental growth is more influenced by demand than supply and according to channel checks this is being supported by expansion of co-working tenants, pharmaceutical tenants centralising in the CBD and second-tier legal firms.

A stronger office environment has started to be reflected in operating metrics, with improving comparable net operating income growth and portfolio occupancy. Citi expects this to continue to improve as expiring leases are marked to market. The broker believes Investa Office ((IOF)) guidance for FY18 may prove to be conservative, given the stronger Sydney office conditions.

Office stocks have been sold off recently and Citi notes Investa Office was the worst performer. The broker prefers this stock over Dexus Property ((DXS)), given its cheaper valuation and potential upside to guidance, as well as a high corporate appeal.

NZ Election

A change in the New Zealand government could trigger a substantial change in policies. The election on September 23 remains a close call. A change in policies has implications for ASX200 stocks, in Morgan Stanley's opinion. NZ Labour, if it wins government, is proposing material changes to migration, taxation and housing.

The proposals on the cards include quarantining negative gearing deductions, extending capital gains tax on investor housing out to assets held for less than five years, banning foreign investment in established property and slowing migration.

Morgan Stanley estimates 43 ASX200 stocks carry meaningful exposure to NZ operations including the four major banks. Of the banks ANZ Bank ((ANZ)) and National Australia Bank ((NAB)) carry the largest exposure. For Australian industrials it is Harvey Norman ((HVN)), Corporate Travel ((CTD)), Downer EDI ((DOW)), Woolworths ((WOW)), Kathmandu ((KMD)), Insurance Australia Group, Fletcher Building ((FBU)) and Fairfax which stand out with meaningful NZ revenues.

# National Bank: Beware The Downside

By Michael Gable

In the last week, we have seen the Australian miners take a breather and banks find a bit of support. This has caused the market to continue its sideways motion with neither sector managing to head in the same direction at the same time. We continue to see movement beneath the blue chips with breakouts in stocks like Eclipx Group (ECX). Gold stocks have also taken a breather in the last week but the gold chart still looks good in the longer term. It is therefore a good time for investors to keep some sort of gold exposure while looking for a chance to add to those positions in the next few weeks.

Today we look at National Bank ((NAB)).

The banks have had a good few days but it is worth coming back and looking at the broader picture on weekly chart. As we have warned before, looking at NAB here, price action resembles that of a flag. Volume has also been decreasing over the last 4 months, as the price has been edging higher (indicated with the diagonal line on the volume chart). All of this graphically shows the weakness that is still inherent in NAB and the banks and we are still wary that at some point they will break down from this flag and drop to a new low for the year. For NAB we are still aiming for $28 as the next possible chance to buy the shares.

Content included in this article is not by association the view of FNArena (see our disclaimer). Michael Gable is managing Director of Fairmont Equities (www.fairmontequities.com)

Fairmont Equities is a share advisory firm assisting Private Clients with the professional management of their share portfolio. We are based in the Sydney CBD but provide services to private clients across Australia. We believe that the concepts of fundamental analysis and technical analysis of stocks are not mutually exclusive. Regardless of whether you are a trader or long term investor, combining both methods is crucial to success. As a result, the unique analysis of Fairmont Equities is featured regularly in the media such as Sky News Business, CNBC, The Australian Financial Review, and the ASX newsletter. Contact us for a free trial of our research and information on our portfolio management services.

Michael is RG146 Accredited and holds the following formal qualifications:

• Bachelor of Engineering, Hons. (University of Sydney) • Bachelor of Commerce (University of Sydney) • Diploma of Mortgage Lending (Finsia) • Diploma of Financial Services [Financial Planning] (Finsia) • Completion of ASX Accredited Derivatives Adviser Levels 1 & 2

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# Oz Construction Cycle: The Impact Is Now

In this week's Weekly Insights (published in two separate parts):

-Oz Construction Cycle: The Impact Is Now -On Bear Market Alert -Conviction Calls: CS, Shaw, Morgans, UBS, Bell Potter, Deutsche Bank -CBA And The Premium Gone (Vol 4) -New Website: Set Dedicated Email Alerts -Rudi On BoardRoomRadio -2016 - L'Année Extraordinaire -All-Weather Model Portfolio -Rudi On TV -Rudi On Tour

[Note the non-highlighted items appear in part two on the website on Thursday]

Oz Construction Cycle: The Impact Is Now

By Rudi Filapek-Vandyck, Editor FNArena

Not a day goes by without at least one economist, or journalist, pointing towards the housing cycle in Australia with the message: the cycle has peaked.

Certainly, recent data support the thesis, at least for high density dwellings, but not so for other segments of the domestic housing market. With high density dwellings, industry commentators are referring to apartment complexes of four storeys, and higher. Recent years have seen a true explosion in the construction of such buildings and most cities outside Melbourne and Sydney are now staring at, or already experiencing, over-supply.

Think Perth and Brisbane, and falling prices.

Here's one ominous sentence from a recent market assessment from the economics team at Westpac: "Our own research highlights large slippages in vendor settlements and valuations."

An Uneven Correction

Overbuilding with Australian households taking on ever more debt, at a time when financing costs are rising, macroprudential pressure is causing credit tightening, and with foreign investors increasingly battling headwinds, this seems like an ominous cocktail for a guaranteed negative spiral down the road. Indeed, there have been times over the past 2.5 years or so that investors in the share market decided to shoot first and wait for more clarity later.

This time around, however, the Australian housing construction market has mimicked the share market in that different dynamics for different segments make this downturn a rather uneven one. So tiny details matter.

There is now broad agreement among experts that the downturn in construction is firmly concentrated in the aforementioned high density dwellings, and more so in Brisbane, Perth and Canberra than it will affect Melbourne or Sydney. There is still growth in medium density and detached houses, but above all, government spending in infrastructure projects is ramping up significantly, in particular in the eastern states.

The bottom line is that growth in roads, rail, hotels, office buildings and hospitals will underpin overall building activity in 2018 and 2019, virtually securing a soft landing for a cycle that had become too dependent on foreign and local investors' appetite for small units, cobbled together inside high rise towers.

This, of course, doesn't mean there won't be any consequences. High density construction is more labour intensive, so there should be, all else being equal, a net negative impact on jobs and on jobs creation. Equally important: how will Australian consumers respond to the absence of wealth creation from rising house prices when electricity prices remain high and real wage increases absent?

The graph above, from a recent ANZ Bank report, shows building approvals for three key segments of the market in Australia. The big blue mountain that is now turning into a serious downturn; that is the new trend in high density construction.

Is RBA Really Ready To Hike?

For good measure: not everybody is on the same song sheet when it comes to assessing the impact from oversupply in small units on the rest of the housing market, apart from the fact that regional differences are real and pronounced. Speakers at the BIS Oxford Economics conference in Sydney last week predict small price decreases for dwellings in Sydney, in general terms, but small decreases are a major change from the steady rises experienced in years prior.

Apart from any potential impact on national jobs and underemployment trends, I am worried about the psychological impact and the consequences for discretionary spending next year. Hence my ongoing aversion to jumping on board bricks and mortar retailers in the Australian share market.

To me, this is not just about Amazon and the potential impact on local profit margins, this is equally so about the devil within Australian households; too much debt, no wealth creation and plenty of threats and annoyances to worry about.

For more than a year now, economists and commentators of all sorts are engaged in a public debate about what it will take for the RBA to start hiking the cash rate again. Those who had set their mind on a Melbourne Cup Day rate hike have now shifted their timing towards the second quarter of next year. A view supported by bond market movements in recent weeks.

I remain firmly in the camp with BIS Oxford Economics, ANZ Bank, Westpac and others, standing stoically behind the response "tell them they're dreaming!"

Further supporting that view is the fact that a re-weighting of the CPI basket will weigh on reported inflation and no, we do not believe there's a significant catch-up, or otherwise sustainable recovery, about to announce itself in wages.

Here's how Westpac Chief Economist Bill Evans put it: "It is fortuitous that the non-residential cycle will ease the impact from a growth perspective although, as discussed, the impact on employment will be significant.

"Under these circumstances we do not support current market pricing which points to the beginning of the rate hike cycle in mid-2018 with a full rate hike priced in by end 2018. We continue to expect rates to remain on hold in 2018."

While it may as yet remain too early to determine who's going to be correct and wrong in the current debate about interest rates in Australia, the next twelve months will bring data and further developments to a head - this debate will be concluded either way.

Morgan Stanley: A New Level Of Concern

Last week, sector analysts at Morgan Stanley reported their proprietary housing model, MSHAUS, has now declined to a record low in the 28 year history of this indicator. According to the analysts, more macroprudential measures, strong supply growth and higher debt servicing on mortgage repricing all conspired to push the indicator to -0.9 in the second quarter.

They in particular singled out a sharp fall in the share of interest only mortgages, a result of APRA placing further restrictions on Australian banks.

Morgan Stanley is looking for ongoing softening in approvals and price growth over the next three quarters. The analysts report apartments already have fallen in relative pricing "and in Brisbane, Melbourne and Perth are increasingly being valued below contract price". Ongoing audits and media revelations around the widespread use of combustible cladding in Australian buildings can potentially impact on demand, valuations and settlements, note the analysts.

Their conclusion: "Housing construction now looks to have peaked, with activity falling over 1H17, but we expect both the 'front book' of approvals and work done to continue declining through 2018. Alongside risks to house prices after an extraordinary ~80% rise in Sydney and ~60% rise in Melbourne since 2013, this makes it even more imperative for both public and private sector investment to create jobs and generate the wage growth that may help rebuild household buffers".

Economists at National Australia Bank have now joined the Yes camp (nothing to do with Same Sex Marriage). On the assumption household budgets will be in a better shape by mid next year, and on expectation of further global economic growth, NAB is now calling for the RBA to hike by 25bp in August 2018 with the cash rate to increase by a further 75bp over the next 16 months (cash rate at 2.50% by end 2019).

See also "The Bubble Is (Finally) Ready To Burst, 15 March 2017.

CBA And The Premium Gone (Vol 4)

This is how successful sequels are born...

I have been arguing in the prior three editions in this series, the share market is displaying a shift in sector leadership for the major banks in Australia. No longer does the sector come with the caveat CommBank ((CBA)) first, and then the rest follows.

This reversal in relative valuations is easily recognised when looking at the gap in share prices for the Big Four and their respective consensus price targets on the FNArena website. National Australia Bank ((NAB)) shares are now at touching distance of their target, whereas for ANZ Bank ((ANZ)), CommBank and Westpac ((WBC)) there is still a gap of 2.0%, 2.3% and 6.3% respectively waiting to be closed.

If my assumption is correct, and NAB is now the new leader, then NAB shares should rise beyond target while the others continue their attempt to close the gap ahead of the banking reporting season in November (ex-CBA). A second observation is, of course, this week's rally is rapidly closing whatever is left in gaps.

The local investment community has thrust itself upon the CBA versus the sector dilemma in recent weeks, including Clime Asset Management which joined in favour of CBA shares, calculating on FY18 forecasts the shares already were valued cheaper than ANZ and Westpac.

The most interesting aspect of Clime's analysis is the chart below, showing how CBA's sector premium has moved since the mid-1990s. The recent de-rating, argued Clime, had transported CBA shares back into the framework of 2001-2003.

New Website: Set Dedicated Email Alerts

As most paid subscribers are probably aware, it is possible to add email alerts to stocks included in Portfolios or Watchlists on the FNArena website. The process centres around individual stocks, but broader sectors are an option in extension of each chosen stock.

But some of our most popular publications -the Australian Broker Call Report, the Overnight Report and Rudi's Views- are not stock specific or even sector-based. Subscribers can set specific email alerts for these stories via the My Alerts section on the top horizontal black bar, squeezed in between "Write a Message" and "Portfolio & Watchlists".

Here one discovers there are currently six such specialised options, including Broker Call Highlight and All-Weather Stocks. The idea is that every time FNArena publishes a story related to such a specific theme, an email shall be sent to your inbox.

There is even the option to click on "Please send me news alerts for every article you publish".

Don't forget to press the Save Alerts button.

Rudi On BoardRoomRadio

Last week's audio interview:

https://boardroom.media/broadcast/?eid=59b75a3d0f7013455d23aa33

2016 - L'Année Extraordinaire

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# Rudi's View: On Bear Market Alert

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[Note the non-highlighted items appeared in part one on the website on Wednesday]

On Bear Market Alert

By Rudi Filapek-Vandyck, Editor FNArena

"Bear markets are inevitable: the question is not if, but rather when, the next one will occur. The problem is that, while bear markets are very obvious with the benefit of hindsight, they are very difficult to identify in real time."

Thus spoke Goldman Sachs strategists in their recent Global Strategy Paper, "Bear Necessities. Identifying signals for the next bear market". The 41-page report lines up the prime reasons as to why investors might be feeling antsy and uncomfortable in the present context:

1) The current bull market is already relatively long-lived and strong by the standards of history. Depending on one's definition, this bull market in US equities can be categorised as the second longest on record, as well as the second strongest on record.

2) On many measures equity markets (and other financial assets) are expensive versus history.

3) Margins (at least in the US) are at record highs, raising the prospect that they might have peaked.

4) After years of extraordinarily low interest rates and QE, which have driven and supported financial returns, we may be close to a turn in the central bank policy cycle.

Offsetting these major concerns are two major sources of support:

1) The free cash flow yield is high (this is true in most equity markets). This, explains Goldman Sachs, is a direct result of companies having held back on capex.

2) Equities are cheap versus bonds. This, of course, remains the case today, and probably for a while to come.

Historical research has taught Goldman Sachs to distinguish three types of bear markets:

1. Cyclical bear markets - typically a function of rising interest rates, impending recessions and falls in profits. They are a function of the economic cycle.

2. Event-driven bear markets - triggered by a one-off ‘shock’ that does not lead to a domestic recession (such as a war, oil price shock, EM crisis or technical market dislocation).

3. Structural bear market - triggered by structural imbalances and financial bubbles. Very often there is a 'price' shock such as deflation that follows.

By splitting bear markets into these groups the strategists find that:

- Cyclical and 'event-driven' bear markets generally see price falls of around -30%, while structural ones see much large falls, of around -50%.

- Event-driven bear markets tend to be the shortest, lasting an average of 7 months, cyclical bear markets last an average of 26 months and structural bear markets last an average of three and a half years.

- Event-driven and cyclical bear markets tend to revert to their previous market highs after around 1 year, while structural bear markets take an average of 10 years to return to previous highs.

So how do we recognise a bear market? Answer: we don't. Given every bear market is different, and caused by different triggers in different contexts, it is plainly impossible to recognise one in advance. Investors who often sell too early are most times not better off than those who wait until the early phase of the ugly bear market announces itself.

As long as one manages to avoid the bulk of the downturn, being early or not matters little, suggests Goldman Sachs. A lot of the research depends on timelines and on definitions used, something the strategists readily admit. For example, they'd be inclined to include April 2011 as the starting point of a brief bear market that lasted five months and ultimately pulled back US indices by -19%.

Including that particular bear market means today's bull market is merely of average length, instead of the second longest in history. The first part of that sentence would make investors a lot less worried than the second part currently does.

The end conclusion from the report won't encourage many investors who'd like to be prepared for when the next bear market arrives: the reliability of indicators tends to be low. "Sometimes it is not a single factor or event but a combination that can contribute to a bear market. On occasion it is not even possible to identify the key trigger even after it is over."

Undeterred, the strategists have selected five indicators that have worked best together, historically, in identifying the next bear market. These five are:

1. Rising unemployment as a precursor to the next economic recession with low unemployment identified as a consistent feature prior to most bear markets

2. Rising inflation has been an important contributor to past recessions and it tends to trigger monetary tightening

3. Flat yield curve; Goldman Sachs argues a flat or inverted yield curve in combination with high asset valuations can be a useful bear market indicator

4. Momentum indicators such as ISM and PMI surveys; typically, when momentum is elevated there's but a reasonable chance the pace will deteriorate and eventually move below recession levels

5. High valuations; they never trigger a bear market in isolation, but in combination with other fundamental factors, high valuations can imply the risk for another bear market is elevated.

Combining all of the above, Goldman Sachs strategist are of the view that while the risk for the next bear market is relatively high right now, suggesting the next market correction has the potential to morph into a bear market, they remain of the view the odds favour low return over the next twelve months rather than a true blue bear market.

The key to their non-bear market outlook is the shift in inflation risk, as "without rising inflation expectations, monetary policy can stay looser with interest rates much lower and more stable than in the past".

Here's the final conclusion from the report: "The combination of higher valuations but lower prospects for interest rates and inflation volatility leads us to expect lower future returns as a central case rather than an imminent bear market. Nonetheless, should inflation expectations rise, necessitating higher interest rates, then the probability would rise that the next bear market would be sharp and, with fewer options to ease monetary policy, it would likely be long".

Conviction Calls: CS, Shaw, Morgans, UBS, Bell Potter, Deutsche Bank

Market strategists at Credit Suisse are concerned the upcoming 19th Communist Party Congress in China might well become a turning point when Chinese policy makers change the direction or magnitude of the current expansionary policy measures. They have reduced their overweight position in Australian resources as a direct result.

This has resulted in the selling of Fortescue Metals ((FMG)) and of South32 ((S32)). The Credit Suisse Long Portfolio still includes BHP ((BHP)), Rio Tinto ((RIO)) and BlueScope Steel ((BSL)). The strategists have added Computershare ((CPU)).

Other stocks included in the Long Portfolio are ANZ Bank ((ANZ)), AMP ((AMP)), Caltex Australia ((CTX)), Star Entertainment ((SGR)), Adelaide Brighton ((ABC)), Premier Investments ((PMV)), Nine Entertainment ((NEC)) and EclipX Group ((ECX)).

Stocks on the Strategy Short Ideas List include Sydney Airport ((SYD)), ASX ((ASX)), APA Group ((APA)), Cochlear ((COH)), Healthscope ((HSO)) and Charter Hall Group ((CHC)).

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Shaw and Partners' Australian Large Cap Model Portfolio has used recent price appreciation in Lend Lease ((LLC)) shares to offload some stock and redirect it to Stockland ((SGP)) in order to keep the portfolio's overall exposure to real estate at 11.3%.

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They certainly like IPH Ltd ((IPH)) over at stockbroker Morgans. The stock is on the radar of portfolio managers for the Income Model Portfolio, as well as the Balanced Model Portfolio with the intention of adding extra exposure in case of further share price weakness. We can only assume Morgans has been buying more shares recently.

The latter has also been topping up BT Investment Management ((BTT)), while the former included Suncorp ((SUN)) in August with the intention of buying more of it, during times of weakness.

Morgans Growth Model Portfolio also bought a new position in BT Investment Management, while buying more of Commbank ((CBA)) and getting rid of South32 ((S32)).

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Small Cap specialists at UBS have used the August reporting season to select their Buy rated preferences: AMA Group ((AMA)), Autosports Group ((ASG)), Bapcor ((BAP)), Infomedia ((IFM)), G8 Education ((GEM)), NextDC ((NXT)), Premier Investment ((PMV)), Tassal Group ((TGR)) and TOX Free Solutions ((TOX)).

UBS's sole conviction Sell call is Ardent Leisure ((AAD)).

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Bell Potter's update on the local Tech Sector contained not one single Sell rating, but that changed a few days later as the share price for WiseTech Global ((WTC)) continued rising. I suspect the broker's downgrade to Sell has since been responsible to keep the bulls, and the share price, in check.

Bell Potter's Top Picks for the sector are Integrated Research ((IRI)) in top spot, followed by (in order of ranking) Adacel Technologies ((ADA)), Empired ((EPD)) and Senetas ((SEN)). The latter replaces Appen ((APX)) which is no longer included as a Top Pick.

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Deutsche Bank's Model Portfolio has added Medibank Private ((MPL)), WorleyParsons ((WOR)) and Santos ((STO)) while removing QBE Insurance ((QBE)), ALS Ltd ((ALQ)) and Woodside Petroleum ((WPL)).

Deutsche Bank strategists have also lowered their ASX200 index projection to 5900 by year-end (down from 6000 prior), to 6000 by mid next year, to 6050 by year-end 2018. The strategists are of the view the global economic backdrop remains supportive, but also this already is reflected in share prices, while earnings growth in Australia is likely to weaken again to mid-single digit percentage.

Note to paying subscribers: updates on Conviction Calls have been a regular feature in my Weekly Insights stories since early February this year, with only a rare exception. For past updates: see Rudi's Views on the FNArena website.

Rudi On BoardRoomRadio (Updated)

Audio interview from earlier this week (not to be confused with last week's):

https://boardroom.media/broadcast/?eid=59c0972724704206917147eb

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P.S. I - All paying members at FNArena are being reminded they can set an email alert for my Rudi's View stories. Go to My Alerts (top bar of the website) and tick the box in front of 'Rudi's View'. You will receive an email alert every time a new Rudi's View story has been published on the website.

P.S. II - 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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