WEEK 33

FINANCIAL NEWS, ANALYSIS & DATA

STORIES TO READ FROM FNArena

Friday, 12 August 2022

Rudi's View: August Results - First Blood

Megaport: Focus Returns To Global Potential

Negative Industry Trends Impact Australian Clinical Labs

CONTENTS

FNArena
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AUSTRALIA

Trouble On The Aurizon

An in-line result from Aurizon Holdings was somewhat overshadowed by guidance for FY23 that has largely disappointed the brokers.

-Aurizon Holdings delivered an in-line full year result, with a miss from Bulk and a beat from Coal
-Guidance for the coming year implies up to 6% growth on FY22 results
-Growth guidance has largely disappointed as coal decline drags

By Danielle Austin

While rail freight operator Aurizon Holdings ((AZJ)) has delivered a full year result largely in line with consensus expectations, the market is focused on a weaker than expected FY23 guidance.

The company achieved full year earnings of $1,468m, with one-offs contributing $65m, and net profit of $525m. Both realised earnings and net profit were a beat on consensus forecasts of $1,455m and $510m respectively.

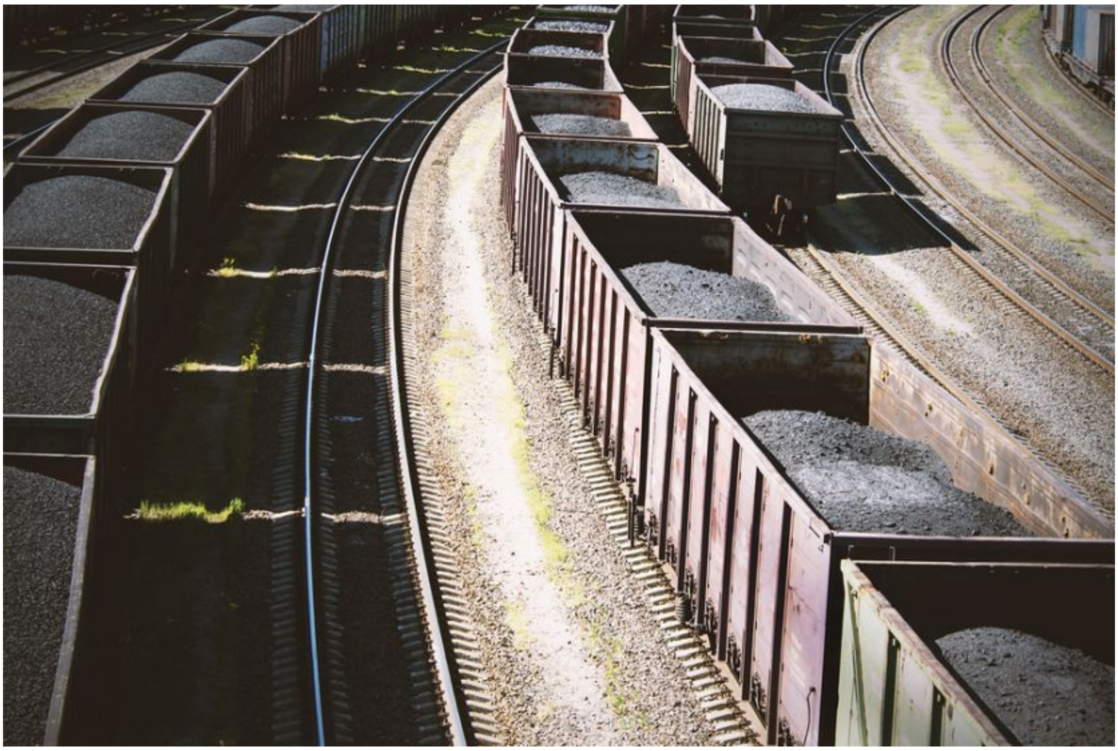
The Bulk segment was highlighted as delivering a disappointing result, reportedly missing its internal earnings target by -21%. Earnings of $130m from the segment were down -7% on the previous comparable period, with iron ore volumes down -20%.

Alongside its results the company has provided initial guidance for FY23, implying 0.0-5.5% growth and largely disappointing against expectations. Guidance for the coming year including a maiden earnings contribution from One Rail Bulk, which is expected to provide an $85-90m earnings benefit over eleven months, or a 6.0% benefit to earnings, as well as a 3.0-6.0% contribution from inflation.

Given this, even the top end of growth guidance of 5.5% implies some earnings benefit will be lost to declines in coal as high margin contracts come to an end.

The company flagged that despite a 5% volume improvement in coal, it expects earnings will decline as contract renewals are made at lower margins.

Upcoming contract opportunities could supplement company earnings, with South32's ((S32)) Dendrobium mine seeking services through to 2035, and Idemitsu's Boggabri seeking services through to 2037, while BHP Group's ((BHP)) Mount Arthur project, for which Aurizon already holds the contract until 2026, is set to close in 2030.



Divestment ahead flagged as a catalyst

With the One Rail acquisition completing in July, the brokers are largely in agreeance that divestment of the East Coast Rail asset will be a next catalyst for Aurizon.

The company has stated it has engaged with around ten potential acquirers for its East Coast Rail asset, and non-binding bids from interested parties are due in September

Following the release of Aurizon Holdings' FY22 results, six FNArena's database brokers updating views have between them issued one equivalent Buy rating, three equivalent Hold ratings, and two equivalent Sell ratings. Between them, these brokers have an average target price of $3.86.

Morgans (Add rated with a target price of $4.20) anticipates downgrades to earnings forecasts from the market given Aurizon 's disappointing initial guidance for FY23. The Morgans analysts also highlighted the entire funding of the One Rail acquisition through a floating rate bank loan will likely drag on earnings moving forward.

Morgans' modelling assumes East Coast Rail is sold at enterprise value of $1.1bn, noting each $100m difference to the sale price represents 5 cents per share to the company's equity valuation. The broker also expects new contract wins in haulage to be a price catalyst.

Despite describing the stock as offering a balanced risk-reward outlook, Citi (Neutral rated with a target price of $4.17) retains its rating given the lower end of growth guidance remains flat year-on-year, but does note the East Coast Rail divestment is attracting positive commentary.

The Citi analysts noted despite meeting expectations in FY22, the company's result was compositionally lower quality. Looking ahead, the broker also continues to see an elevated likelihood of a return of La Nina weather later in 2022, impacting on volumes. Citi revised it net profit forecasts -2%, 4% and 6.5% through to FY24, accounting for the softer near-term coal outlook.

Describing the FY22 result as disappointing, Macquarie (Neutral rated with a target price of $4.05) finds that the result highlights the continuing earnings volatility in the company's Bulk segment. The broker also finds the company's FY23 guidance soft, noting it anticipates a 6.0% earnings benefit from the One Rail acquisition and at least a 3-6% earnings benefit from inflation.

The broker sees coal margins dropping to FY17 levels and dragging on earnings ability but anticipated the company will benefit from gains come FY24. Macquarie has updated its earnings per share outlook by -11.6%, -6.3% and 9.2% through to FY25 to reflect softer coal margins in the next year.

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

AUSTRALIA

Block Still Paying For Afterpay Acquisition

Block's BNPL segment continues to drag on portfolio performance, but brokers largely continue to back the integration opportunity for Afterpay and Cash App.

-Afterpay acquisition fails to deliver for Block in the second quarter
-New products, including the recently launched Borrow loan product, should offer diversification
-Competition looks to intensify, with some brokers anticipating industry consolidation ahead

By Danielle Austin

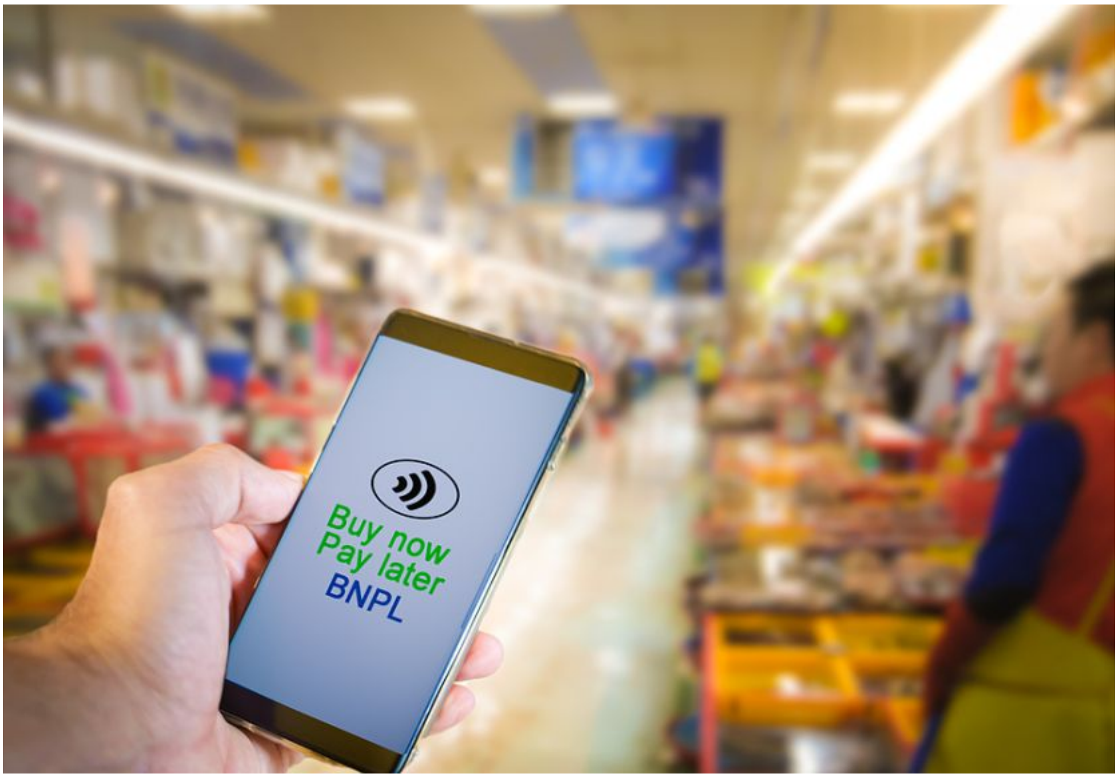
There appears plenty of opportunity in Block's ((SQ2)) recent acquisition of buy now, pay later platform Afterpay, but as integration of the purchase continues to progress the company is yet to deliver on potential.

At the close of the second quarter the company reported total gross profit was up 29% year-on-year, with Afterpay's $150m contribution representing a -2% decline for the business, and the drag from Afterpay is expected to have continued following the second quarter, with the business expected to deliver just 1% growth in July.

Positive commentary around Block's Cash App was a highlight of the result, with the company reporting 47 million monthly users, acceleration in daily and weekly activity growth, and record quarterly inflows. Having achieved 20% gross profit growth in the second quarter, the Cash App is expected to deliver 32% gross profit growth in July.

Integration of the Afterpay and Cash App platforms continues to present a key opportunity for Block, allowing the company to offer consumer platforms with access to a range of lending and banking services products.

Block also released its new short-term lending product during the quarter, offering loans under $200 per month that can be repaid in instalments through the platform.



Shifting trends and intensifying competition

Block management appears to have taken a conservative view on the coming second half, cautiously reducing investments in response to a more volatile macroeconomic environment, and citing increasing competition from pure-play BNPL peers as a concern.

The company highlighted a trend shift in spending mix away from utilising BNPL products for online purchases, and towards using the platforms in-store.

Of FNArena's database brokers, Credit Suisse, Morgan Stanley and Macquarie have reported on Block's second quarter result. Macquarie retains a Neutral rating and has lifted its target to A$130 from A$97. Morgan Stanley also has a Hold-equivalent (Equal-Weight) rating but has cut its target to US$85 from US$110. Credit Suisse has an Outperform rating and has left its target unchanged at US$125.

The target cut from Morgan Stanley represents a desire to see greater investment in, and faster availability of, a wider range of credit products. The broker sees long term potential in a Cash App and Afterpay integration that brings banking and lending services to the underbanked younger generations in the US, but notes an ability to accelerate and launch credit and banking services products on consumer platforms will be key to Block's outlook. The broker highlighted limitations to Cash App's Borrow, and Afterpay's interest-free model, given that both can only finance smaller and shorter-term loans. Morgan Stanley's updated forecasts predict 36% gross profit growth year-on-year, estimating total gross profit of $6,011m.

Macquarie reiterated a favourable view of Block's legacy business (Square payment system), which it described as pulling the weight of the company's recent result. Looking ahead, the broker cautions cost controls will come into play to support management focus on profitability. The broker previously warned of Afterpay continuing to drag on the remainder of the portfolio and continues to see risk here, noting more stabilisation of Block's BNPL segment would be needed to support a more positive outlook. On the back of Block's second half result, Macquarie lifted earnings per share forecasts 37-66% through to FY24, and 25-37% in outer years. By product, the broker is anticipating Cash App to deliver 21% gross profit growth in July, Square 14% and Afterpay 1%.

Credit Suisse has lifted its earnings estimates to account for Block reducing its operating expense growth, removing longer-term and experimental sales and marketing and slowing hiring. The broker is anticipating Cash App and Square to achieve full year gross profit growth of 40% and 24% respectively. Credit Suisse anticipates industry consolidation will occur over the next decade, but finds Square well positioned to remain a leading digital financial services platform in the US.

RUDI'S VIEWS

Rudi Interviewed: August Focus On Quality

As has become an unofficial tradition, FNArena Editor Rudi Filapek-Vandyck was interviewed by Livewire Markets co-founder James Marlay ahead of the August results season in Australia.

A link to the video which can also be viewed via YouTube is included at the end of the edited transcript below.

James Marlay, co-founder Livewire Markets:

Last time we had a chat, a little bit of a debate erupted in the comments section [on the Livewire website] and the general context was about you holding extra cash in your portfolio, given the uncertainties you had identified in the market.

So, before we get into the reporting season, I want to hear your views on the idea of timing the market, because it always draws debate. I'd really love to hear what your views are on that particular topic.

Rudi Filapek-Vandyck, Editor FNArena:

This might actually surprise you. I've seen many statements like: it's a bit foolish to try to time the market. And I agree with that.

I also think there's a misunderstanding amongst investors about when someone like myself increases the cash level in the [All-Weather] portfolio.

That's not because I try to time the market, it's done because I make a risk assessment.

I think investors put too much emphasis on trying to sell at the ultimate peak in the share price and to buy back in at the ultimate bottom of the share price.

There is way too much emphasis and too much effort for something that is very difficult to achieve.

But what we all can do, if we take good care of the money we have in the market, we can all assess the risks; whether they increase or decrease.

And when risks become very, very high; whereby I suspect there is an above-normal drawdown waiting to happen in the market, then I wouldn't be a cautious investor if I would not increase my level in cash.

That's basically the long and the short of it. I'm not timing the market. I'm simply adjusting the [All-Weather] portfolio in line with my assessment of the risks that lay ahead.

To put this in very simple terms: when you leave the house and you look out the window and it's raining, you take an umbrella with you. That's just the normal thing to do.

The same thing applies to the share market. When the only thing that's going to work is keeping your money in cash, why wouldn’t you do it? It is but the logical thing to do.

James:

That conversation happened back in February. More recently, you talked about phase one being the quality recovery.

So, my question to you is: are you carrying more or less cash than when we spoke in February and can you articulate some of the thinking behind your position right now?

Rudi:

I think this might surprise you and some of the viewers, but I have done very little since [All-Weather Model Portfolio] raised the cash level earlier in the year.

I've basically been sitting on the stocks I've felt comfortable with and that cash was just sitting on the sidelines.

In recent times the [All-Weather] portfolio re-allocated some of that cash back in the market, but still holding more than 22% in cash at the moment.

As I always like to point out, [a bear market] is a process and effectively what has now happened is the risk is now shifting towards corporate results. There's more than likely a recession on the horizon, so the risk is not necessarily diminishing.

Risk is descending from the macro level, which previously consisted of high valuations with very low bond yields. As those bond yields had to reset, the share market had to come down in terms of valuation, and that has now happened.

But now we're going to find out how sturdy and resilient companies are in the face of all the challenges that already have exerted themselves this year and, equally important, in the face of the challenges yet to come.

This is where the true challenge for investors lays in the upcoming reporting season.

James:

Interesting, even in some of the early reports that are coming out, you're seeing some big moves based on the fundamentals that companies have reported.

We've seen some big surprises and we've seen a couple of big disappointments. Most recently we're talking about Appen ((APX)) with its share price down -30% last time I checked.

Rudi:

And we have also the likes of United Malt Group ((UMG)), which yet again issued a profit warning. Needless to say, shareholders cannot be happy with what's happening with that share price.

We also have some smaller companies [disappointing], the likes of Nitro Software ((NTO)), for example: big reset in expectations, thus big impacts on share prices.

Then you have the likes of Bega Cheese ((BGA)); again, big drawdowns.

This is one of the reasons why I believe holding a big chunk of cash is still valuable.

Because you can't predict all these drawdowns before the season. There are many challenges out there and we can only adjust our views once we see the details that are coming out of those companies.

Not in advance, as we don't yet have all the details available.

James:

I was reading through one of your most recent notes and against that uncertain backdrop that we've had *there's been a gravitation towards resources companies, but you're not convinced?*

Can you talk me through your circumspect position on resources companies?

Rudi:

I'm trying not to laugh too hard.

There's a fundamental misunderstanding amongst investors about how price earnings (PE) ratios work. And I've seen this throughout the whole year.

If you look at the likes of BHP Group ((BHP)), Rio Tinto ((RIO), Fortescue Metals ((FMG)), BlueScope Steel ((BSL)), Woodside Energy ((WDS)) and Santos ((STO)); they are all trading on a mid-single-digit price earnings ratio, based on the forecast 12 months out.

This is not because those companies offer great value. This is because the market is preparing for a recession.

The fear is those companies are enjoying peak-of-the-cycle product prices for crude oil, iron ore, copper, nickel, you name it.

So, you are not by definition buying a bargain because it's only trading on a PE of seven. You have to take the view that the price of iron ore or crude oil is not going to fall.

If we have an economic recession coming up, that is a big call to make [that those prices won't fall].

My favourite response when I am confronted with such views is I try to turn it into a little bit of a joke.

I say to people: let me check the last time that commodity prices held up in an economic recession.

I then run through my papers, do an extra check of history and then go:… the last time this happened… oh, that's right, it has never happened before!

So basically, if you put all your money in commodities, you are hoping that this time is different, and that this time, prices will hold up in the face of a recession, which has never happened before.

Let's go back to your first question: I said successful investing is all about managing risk. It doesn't seem to me that betting hard on commodities equals managing your risk very well.

When I manage risks, I'm definitely not going to be taking a large leverage to a forecast that if it proves wrong, I might lose my shirt and my trousers.

I think it is most important as an investor to realise investing is not about making forecasts. It's about making sure that if the forecasts you're making are wrong, that you don't end up going down by -30%, by -40%, or by -50%.

James:

Alrighty, the flip side is that you are interested in looking at some of the technology companies and some of the smaller cap stocks; companies that have really borne the brunt of the selling.

Is that because you like that area, or because you think a lot of the bad news is already in the price?

Rudi:

There are two sides to that. One: I have been waiting until I could feel comfortable with where bond yields are, because bond yields ultimately are the master of everything.

I think bond yields have peaked, for now, which probably is a fair assumption to make. Unless we are all reading inflation in the wrong way.

That means the higher multiple growth companies no longer have to fall on the basis of bond yields rising. So now it becomes an individual story.

Now it's about picking the quality in the sectors you like. And quality, in this case, means you should have an eye on how resilient are businesses going to be in a recession?

As I explained earlier, that is the main question investors should now be asking.

Even if we somehow, by miracle, escape an economic recession next year, the question will still be asked by markets.

That's how I look at the share market right now.

In summary, I think an era of quality is opening up and it's no coincidence that, for example, CSL ((CSL)) is back at almost $300, TechnologyOne ((TNE)) is at $12 and Goodman Group ((GMG)) is back above $20.

You're seeing the quality companies in each sector taking the lead in the recovery. And that is basically happening on that same philosophy I just explained. Other people are thinking the same way.

James:

You named three companies. They're not exactly what I call small caps.

Are there similar areas, outside of the well-established names, that you think have the potential to be quality leaders across a few sectors?

Rudi:

One of the small cap stocks that I've held on to throughout this year's turbulence is IDP education ((IEL)).

[The All-Weather Portfolio] halved its position in that company and recently it was topped up again.

I believe this company is excellently positioned for the post-covid era; it should do well, including in case of a recession.

Obviously, we're gonna find out the answers in August.

The mega trends that existed before we saw a resurgence in inflation and higher bond yields, those mega trends will still continue.

But not every company that can claim to be supported by long term mega trends is necessarily well-run in the short term, is not necessarily profitable, and not necessarily well-managed enough to weather an economic recession.

Hence, it's still a field full of landmines [out there]. I believe that putting an emphasis on quality in each sector that you're looking at will pay dividends.

James:

Let's get on to reporting season because that is the catalyst for us to have a chat.

Before we get into it, is there a chart or a statistic that you can draw on that you think is really important for investors as we head into reporting season?

Rudi:

I am assuming most people know what we're doing at FNArena. For those who don't: we also collect data on stockbrokers.

This might surprise a few people, but the total percentage of Buy ratings in Australia is still 59% - near a decade high.

On that basis, you have to conclude two things: this is still a bear market, plus a lot of corrections still need to happen in terms of forecasts and in valuation modelling for companies.

August is not going to give us all the answers. It'll probably happen in August and February next year. But forecasts are probably too high.

Another statistic I find very interesting is that the average savings rate in the United States is declining, and quite rapidly so.

I can pick up on that because my impression from surveys done in Australia is that the Australian consumer and Australian house owner has been quite resilient but also quite ignorant about what is basically laying ahead.

I think the consumer in general wants to keep doing what he/she's been doing in past years but, ultimately, he or she will have to be forced into changing habits.

That's one of the reasons why I think the changes that will come through on the back of higher interest rates are very slow-paced; we all have to wait until the true effects show up.

I do think investors are realising this and they will be very hesitant to pile in into housing-related companies in Australia and in retailers etc.

It is also becoming clear in the United States that the divergence between new orders and inventories is widening almost every month now and that is not good news either.

This in itself will prove deflationary. It also increases the chances significantly that companies will be left with too [large] inventories.

You can see the bad news building if you have an eye for it.

James:

I noted in your most recent article to FNArena subscribers, you said on face value the Australian market "looks" like a bargain hunters paradise, with the key word there being "on face value".

Rudi:

There are two elements to that statement. First of all, if you take the average price earnings ratio for the ASX200, it's now 13x-something and it was as low as 12x-something a little while ago.

Historically, that looks like very, very cheap. The problem with that is, of course, the numbers behind the average tell a different story.

We have, for example, BHP making up 11% of the index. We have to go back two decades before we had another example of one company [News Corp] representing such a big chunk of the index.

Long story short: after the banks and the financials in general, the energy sector and the mining sector in Australia are the second largest contingent in the index.

Combine the banks and financials with the miners and energy companies; they're all trading on below market average PE ratios.

That's more than half of the index trading below the average which shows you the other half is trading well above 20x.

I just mentioned CSL. That stock is trading on 36x.

But as I explained earlier, the fact the banks are trading on PEs of 11-12x, with exception of Commonwealth Bank ((CBA)), plus the fact that BHP, Rio, Woodside, etc are trading on a PE of six or seven, that's not a cheap market.

That shows you the fear for a big recession coming. Those low PEs give investors the wrong impression.

The other big question mark is: are we in a down-cycle for profit forecasts? If forecasts have to be cut, this means PE ratios automatically rise, assuming the share price stays the same.

You could call this a head fake because the 13x-something might in reality be more like 14x-something and if you accept that the long-term average in Australia is about 14.5x -14.7x then the share market is actually bang on valued in line with the long-term average, not cheap thus.

James:

In context of those comments, to what extent do you think the market has priced in potential earnings downgrades, which, as I keep reading, are going to continue to flow through?

Rudi:

This is one of the answers we are going to find out in August.

The market previously sold down the retailers and anything related to the housing market, but both have bounced hard recently.

It may well be that we're finding out in August that it's still early in this cycle. Don't underestimate we just had a fantastic July. It means a lot of share prices have rallied quite hard already.

I also believe because we are looking towards a recession that hasn't arrived yet, that in particular the institutional investors will be very reluctant to join a rising share price if they don't believe that that share price will prove resilient in light of the recession that is yet to come.

History shows that if a company surprises on the upside in reporting season, that share price usually outperforms by up to four months, in a relative sense.

This time might be different, I suspect, and I think there will be disappointment in that regard.

To put it very simple: people always say the share market is all about company profits and dividends. That is factually incorrect. The share market is about forecasts of profits and dividends.

Those forecasts are going through a down-cycle and the downgrades might well last into next year.

This by definition will act as a headwind so we are looking at a share market that, as I call it, is a bit of Dr. Jekyll and of Mr. Hyde; not everything will be functioning in the same way as it has done in the past.

There will be lots of curve balls and surprises, both to the upside and to the downside.

James:

I'd like to finish our chat on a positive note because I was telling our team today there's been too much bearishness. July was a good month. The sun's shining.

So, to finish off on a positive note, could you share a couple of companies that you think have the potential to provide an upside surprise or, if that's too much to ask, perhaps you can point to the ones that are just unlikely to be disappointing?

Rudi:

I actually don't think my story is that negative. Sometimes, as an investor, we have to accept that risks are elevated during certain times. This is one of those periods.

It doesn't mean that the share market can only go down by definition.

I have for years been poking fun at people who held shares in Telstra ((TLS)), for the dividend and then held on and held on while their capital eroded and eroded away, over two long decades.

Today, I believe Telstra is making a recovery and shareholders might well be positively surprised over the next three, four years.

They should see share buybacks, bonus dividends and higher dividends. The latter hasn't happened for a very long time.

Irrespective of what happens in August, whether Telstra surprises or not, I think a new trend has been set in motion.

I've been very fortunate that in early 2021, when I was looking for a replacement in dividend allocations [for the All-Weather Model Portfolio], that I chose Telstra at that point in time.

It has been a very beneficial ride since. You could say I'm talking my own book, but I truly believe what I just said.

Otherwise, I'm predominantly focused on market leaders and on quality companies. So, what I just said about Telstra also applies to CSL.

I think CSL is making a come-back. You can already see this in the share price response prior to August.

It is not about what CSL might release in August, as that might still be slightly negative. We know the pandemic has had an impact.

I think the future looks increasingly better for CSL which, again, all else being equal, should prove very, very resilient in a recessionary environment.

[The All-Weather Portfolio] also held on to Goodman Group. Obviously, if you look down from the peak, the share price has fallen a lot.

But, again, I do believe that investors who simply treat Goodman Group as a bond proxy and little else will be proven wrong.

The share price is now back above $20. This company should, above everything else, continue to be carried by a mega trend, and that mega trend is not going to disappear anytime soon.

One of the stocks [the All-Weather Model Portfolio] said goodbye to earlier in the year, because I was afraid of how far it might fall, is NextDC ((NXT)).

While reducing [the All-Weather Portfolio's] level of cash, we bought back in recently. Again, those who are worried about data becoming a commodity are way too early in their predictions.

NextDC is, all else equal, another quality operator in yet another sector that is carried by mega trends.

Also, don't forget that if one's worried about energy costs and the like, this company has contracts to pass on those increases to customers.

There will be no shortage in demand for data.

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The video of the interview (28 minutes): https://www.youtube.com/watch?v=bmFqS6iS_pc&feature=emb_imp_woyt

The most recent update on the All-Weather Model Portfolio: https://www.fnarena.com/downloadfile.php?p=w&n=6AC09DA0-E36C-E748-D84CB5BEAF3EB89F

Also: www.livewiremarkets.com

(Do note that, in line with all my analyses, appearances and presentations, all of the above names and calculations are provided for educational purposes only. Investors should always consult with their licensed investment advisor first, before making any decisions.)

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RUDI'S VIEWS

Rudi's View: August Results - First Blood

In this week's Weekly Insights:

-August Results: First Blood
-September Index Rebalancing (Updated)
-Conviction Calls
-FNArena Talks
-Australian Banks Worried (Behind The Curtains)

By Rudi Filapek-Vandyck, Editor FNArena

August Results: First Blood

The August corporate results season is officially more than one week old, but the FNArena Monitor still only contains 11 updates. A lack of sufficient qualified accountants, apparently, pushes the bulk of corporate releases in Australia into the final two weeks of the month.

But the opening salvo this year, including the preceding fourth quarter updates by miners and energy producers, has already provided some valuable insights which might prove prescient of what is yet to be unveiled over the coming three weeks.

So let's start with some of the insights that should come in handy as Australian investors prepare for the seasonal tsunami in corporate updates.

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Members of the Australian Shareholders Association (ASA) in Busselton, WA (*) looked a bit puzzled when I told them in May this year: you do realise that producers of copper, gold, oil & gas, and other commodities are themselves heavy consumers of diesel, steel, water, power, and other commodities?

That reality soon started to show up in quarterly production updates from miners and energy producers. And one sector on the ASX that has been heavily hit are the **local gold producers**, if only because gold has largely traded sideways this year, apart from a temporary spike as Putin's army crossed the border with the Ukraine.

Rising costs when the price of your main output refuses to spike higher can only mean one thing: margin pressure, and lower profits.

Post-April, the sector has had a rough time. While the return of market optimism in July has seen many share prices rallying off their lows, most prices are still nowhere near the levels witnessed earlier this year. Shares in Newcrest Mining ((NCM)), by far the largest producer in this country, are still trading some -35% below their $29-peak in April.

And so it was, when sector **analysts at Canaccord Genuity** updated their modeling and forecasts at the end of July, a lot needed to be accounted for as higher costs translate into higher investments for those companies looking to expand and into higher operational expenses when running daily operations.

Consider the following incomplete list of price increases the industry is dealing with:

-Diesel costs up 60% on average in WA
-Steel prices are up 60% from one year ago
-Freight costs can be up to 400% higher

-Costs for drilling have increased by 15-20% in recent months

No surprise thus, running higher operational costs and capex estimates through its modeling, Canaccord Genuity's valuations reduced by -24% on average for explorers and developers and by -26% for producers.

The Canadian firm specialises in small and micro-cap companies in Australia. When peers at **UBS** reviewed the sector last week, the average damage was a lot smaller as UBS restricts its research and coverage to larger-cap producers. But with no sustainable uptrend predicted for the price of bullion (not anytime soon), the underlying conclusion is pretty much the same:

"*...tempered growth ambitions, continued operating and inflation headwinds combined with our reduced price deck means stocks are not as cheap as they look.*"

Make no mistake, amidst universal, broad-based sector weakness, there are always opportunities for investors, and both teams of sector analysts have their favourites, but the real message seems to be: rigid selection is key.

Not every share price that has fallen represents a great opportunity for mid- to longer-term investing. The challenge for investors is to identify the real gems and the real quality in a basket that is full of pretenders.

For what it's worth, UBS's favourites are Northern Star Resources ((NST)) among the large caps, because of the company's strong organic growth pipeline, and Gold Road Resources ((GOR)) among small caps. UBS analysts advise investors should focus on strong balance sheets, low risk growth and newer mines with a good runway and optionality still ahead.

Canaccord Genuity's sector favourites are Bellevue Gold ((BGL)), De Grey Mining ((DEG)) and Predictive Discovery ((PDI)). All three have rallied off their June-July low.

Macquarie's favourites are Northern Star, Silverlake Resources ((SLR)) and Gold Road Resources among producers, as well as Bellevue Gold and De Grey Mining among juniors in the sector.

Says Macquarie:

"*Though sequentially softer gasoline prices should take some sting out of headline inflation, underlying inflationary pressures continue to broaden and momentum in core services prices does not yet show any sign of letting up.*"

As well as:

"*We think it premature for the market to be anticipating a Fed pivot.*"

The latter suggests those 20%-plus share price moves for the likes of St Barbara ((SBM)), Bellevue Gold, Resolute Mining ((RSG)) and Regis Resources ((RRL)) might look premature once the market's focus changes back to on-the-ground dynamics and a likely persistence by the Fed to tame inflation with aggressive rate hikes.

It goes without saying, the cost-inflationary pressures that have dogged the gold sector this year equally apply for commodity producers elsewhere, as also shown by June-quarter trading updates released by sector heavyweights BHP Group ((BHP)) and Rio Tinto ((RIO)), as well as by the half-year report already released by the latter.

The one commodity producer that also released financial results, other than Rio Tinto, Canadian iron ore producer Champion Iron ((CIA)) equally disappointed last week, and higher-than-anticipated costs proved one important contributor. Its share price weakened some -45% since the beginning of April, and has staged a mini-rally in August after initially selling off on the quarterly financials.

OZ Minerals ((OZL)) -more copper than gold- equally disappointed with its quarterly update in July, but the share price recovered ahead of BHP Group launching an unsollicited, "opportunistic" take-over bid for the company on Monday. Completely predictable, the news has reinvigorated momentum in share prices for other copper/gold producers such as Sandfire Resources ((SFR)) and 29Metals ((29M)).

Combine all of the above and the take-away message for investors might be that sharply weaker share prices may have already discounted a lot of the bad news, at least in the short term, but cost inflation remains a problem and is creating wide divergences inside sectors. As far as OZ Minerals goes: this company is widely seen as a quality operator. Probably no coincidence then it has been on BHP's radar, instead of other, more cheaply priced, lesser quality alternatives?

BHP's take-over attempt also shows August this year won't just be about bottom line-financials and forward looking guidance. Analysts are expecting at least some commentary about a bonus dividend from Woodside Energy ((WDS)), while Origin Energy ((ORG)) should continue its share buyback.

Woodside is also still looking to sell down its Scarborough project, while Santos ((STO)) might soon announce new ownership for its non-core asset in Alaska, and potentially for its equity in PNG LNG too.

Note to us all: **the threat of economic recession has not dissipated**. The odds are actually shortening that Europe and the USA will join the UK in the months ahead.

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Another sector that has equally landed under close scrutiny are **local real estate investment trusts, A-REITs**.

The early part of the earnings season saw both Centuria Industrial REIT ((CIP)) and Centuria Offce REIT ((COF)) releasing FY22 financials and while the former met forecasts and offers optimism now the share price has weakened significantly year-to-date, the latter disappointed and sees investors and sector analysts continuing to adopt a more cautious approach.

What both REITs have in common is management at each trust has adopted a cautious approach regarding the rising cost of debt, which could become somewhat of a sword of Damocles hanging over this sector for the year(s) ahead.

In simple terms, the market has taken what seems a rather dire view as to how high the **weighted average cost of debt (WACD)** can rise up to over the coming three years. While more optimistic sector analysts can thus see "value" in the sector, others think the market's pricing seems but a realistic scenario.

The underlying sentiment seems similar as with gold miners and commodity producers in general: not every weakened share price is offering a great opportunity; it remains necessary to distinguish the wheat from the chaff.

The real estate analyst at **Barrenjoey**, Ben Brayshaw, is among the least enthusiastic. He thinks REITs will meet FY22 forecasts in August, but the outlook is for reduced growth, reduced profits, and reduced payouts for the sector on average. Issues range from rising costs, to deflating property markets, to the threat of less consumer spending, to still struggling office assets, to less opportunities for acquisitions, to higher headwinds from servicing debt.

Regarding the latter, Barrenjoey points out those REITs carrying the highest debt costs in Australia include GPT ((GPT)), Centuria Industrial REIT, Charter Hall Long WALE REIT ((CLW)), Dexus ((DXS)), Shopping Centres Australasia ((SCP)), Charter Hall Social Infrastructure REIT ((CQE)), and HomeCo Daily Needs REIT ((HDN)).

In addition, Barrenjoey is cautious on the FY23 outlook for Mirvac Group ((MGR)) and Stockland ((SGP)).

REITs were firmly in focus throughout week one, with Bunnings landlord BWP Trust ((BWP)) mid-week reporting "strong fundamental performance" and "prudent positioning", but given BWP just about always trades at a sizeable premium versus the rest of the sector, analysts simply cannot get excited, and this includes the perceived risk-profile for the trust.

Here one of the most interesting pieces of analysis has been released by **Citi** which has attempted to rank the local sector in accordance with a lower-than-average or above-average risk profile. Turns out, BWP Trust is one of the least risky options among local REITs, at least on Citi's assessment.

Scentre Group ((SCG)), Charter Hall Social Infrastructure REIT, Shopping Centres Australasia, and Charter Hall Long WALE REIT have been ranked near the upper side of the risk ladder, echoing similar comments published by peers elsewhere.

There's one thing all sector analysts seem to agree upon, and that is that sector leader Goodman Group ((GMG)) is in great condition, is most likely to continue reporting admirable financials and growth, and, on Citi's ranking, represents the lowest risk profile among peers in Australia. Even Barrenjoey's Brayshaw agrees on this.

The offsetts include a premium valuation (which is easily explainable through Citi's assessment), constant calls the stock looks overvalued by your typical value-investor, and a non-attractive dividend yield of circa 1.6% - a direct consequence of having been accepted as a premium, quality operator in recent years.

The sector as a whole is often described as a beneficiary of higher inflation, but the first three financial results this season have already proved this narrative is too simplistic for general purpose.

Already, though, there is an **underlying sentiment that genuine quality will reveal itself this month**, and I like to think this won't be limited to REITs.

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The first week also saw two **asset managers** releasing FY22 results and the outcome could hardly have been more different.

In one corner we find Janus Henderson ((JHG)), struggling, and struggling heavily to keep investor funds from departing while share markets in general are likely to face ongoing subdued momentum as the threat of economic recession continues to loom large.

In the other corner sits Pinnacle Investment Management ((PNI)), the umbrella group that includes affiliates such as Firetrail Investments, Hyperion Asset Management, Metrics, Plato Investment Management and Solaris. Readers might recognise a few of the very active advertisers and sponsors behind industry events.

Clearly, Pinnacle is enjoying much more popularity than its peers this year, making the impact from sector-wide selling on its share price pre-FY22 release looking extremely silly. But as everyone can see from the price chart, the market has not hesitated to correct that situation in a heartbeat.

Maybe the take-away message here is that **individual strength can overcome general sector malaise**.

The stand-out observation is that just about every analyst thinks local asset managers remain poised for continuing rough times, with the possible exception of a few, including Perpetual ((PPT)), Pinnacle and Navigator Global Investments ((NGI)). The latter, however, has never been fully embraced by local investors since its listing on the ASX pre-GFC.

Just about everyone is looking for more bad news from fallen angel Magellan Financial ((MFG)).

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FNArena will start daily updating its **Corporate Results Monitor**:
https://www.fnarena.com/index.php/reporting_season/

The Monitor also includes a four weeks forward-looking calendar (scroll down).

(*) Zoom presentation for Busselton, WA:

The video can be viewed through FNArena Talks on the website:
https://www.fnarena.com/index.php/fnarena-talks/2022/05/30/2022-outlook-when-cash-is-king/

The presentation slides can be dowloaded via the Special Reports section on the website (scroll down):

https://www.fnarena.com/index.php/analysis-data/special-reports/

September Index Rebalancing

Three weeks ago, Weekly Insights reported on Wilsons' predictions for the September index rebalancing that Standard & Poor's will announce on Friday, 2nd of September.

Those initial forecasts have now been updated with the likely addition of Vulcan Steel ((VSL)) and Neuren Pharmaceuticals ((NEU)) to the ASX300, on top of the 13 candidates identified in July. Having by now also been identified as possible removals: Fineos Corp ((FCL)), Resolute Mining, and Starpharma Holdings ((SPL)).

For the ASX200, Wilsons now believes both Pointsbet Holdings ((PBH)) and Clinuvel Pharmaceuticals ((CUV)) are shaping up for removal in September while Spark New Zealand ((SPK)) is a low-probability inclusion, assuming Life360 ((360)) will be removed.

For the ASX100, Tabcorp ((TAH)) is now ready to be replaced with Shopping Centres Australasia ((SCP)), predict the analysts, while Virgin UK ((VUK)) -previously nominated for removal- is now seen as likely to stay included.

No changes are expected for the ASX50 or the ASX20.

The initial report from three weeks ago, is below.

ASX/S&P Index Rebalance Predictions

The next rebalancing of local share market indices is not due until September but this doesn't stop analysts at Wilsons already reflecting on and publishing predictions of which stocks might get booted out or included.

With some indices, like the ASX300. currently running below capacity there's anticipation September will see a noticeable catch-up with more inclusions than exclusions.

Wilsons is expecting 13 new members for the ASX300 in September, and given six vacancies this forecast only requires seven removals.

Most likely fresh inclusions, on Wilsons' assessment, are Boss Energy ((BOE)), Mincor Resources ((MCR)), Ebos Group ((EBO)), Neometals ((NMT)), Ventia Services Group ((VNT)), Grange Resources ((GRR)), Australian Clinical Labs ((ACL)), OFX Group ((OFX)), Maas Group ((MGH)), Macquarie Telecom ((MAQ)), Seven West Media ((SWM)), Arafura Resources ((ARU)), and Argosy Minerals ((AGY)).

Those believed will be booted out in September are: AVZ Minerals ((AVZ)), PPK Group ((PPK)), Nuix, AMA Group ((AMA)), BWX ((BWX)), Redbubble, and Dubber Corp ((DUB)).

The ASX200 will already see one change on Thursday this week when soon-to-be-acquired Uniti Group ((UWL)) is to be replaced with West African Resources ((WAF)).

Wilsons sees five more probable changes in September with all of Charter Hall Social Infrastructure REIT ((CQE)), Johns Lyng Group ((JLG)), Capricorn Metals ((CMM)), Genworth Mortgage Insurance Australia ((GMA)) and Sayona Mining ((SYA)) poised to replace AVZ Minerals, Zip Co, City Chic Collective ((CCX)), EML Payments and Life360 ((360)).

As far as the ASX100 goes, Wilsons is predicting one probable change with nib Holdings ((NHF)) as a replacement for Virgin Money UK ((VUK)).

It is also possible that Shopping Centres Australasia ((SCP)) replaces Tabcorp ((TAH)), while still an option, but at this stage labeled as "unlikely" are the inclusions of TechnologyOne and Charter Hall Long WALE REIT for which Star Group Entertainment ((SGR)) and ARB Corp ((ARB)) would have to lose their spot.

As per usual, there are likely no changes to be announced for the ASX50 or ASX20 with Wilsons ascribing an unlikely chance for replacement of respectively Lendlease ((LLC)) with Lynas Rare Earths ((LYC)) and of James Hardie ((JHX)) with South32 ((S32)).

Historically, any changes to the ASX200 have the largest impact as institutions often cannot own stocks that are outside of that index. Also, when a stock moves inside the top100 it officially becomes a large cap, meaning institutional small cap investors are forced to sell it in-line with their mandate.

Standard & Poor's is scheduled to announce the September changes on Friday the 2nd, to be implemented two weeks later, on Friday the 16th, after the close of the market.

Conviction Calls

Stockbroker Morgans' Best Ideas currently comprise 33 individual ASX-listed companies. In alphabetical order:

-Acrow Formwork and Construction Services ((ACF))
-AGL Energy ((AGL))
-Aristocrat Leisure ((ALL))
-BHP Group
-Challenger ((CGF))
-Corporate Travel Management ((CTD))
-Dalrymple Bay Infrastructure ((DBI))
-Dexus Industria REIT ((DXI))
-Eagers Automotive ((APE))
-GQG Partners ((GQG))
-Healius ((HLS))
-HomeCo Daily Needs REIT
-IDP Education ((IEL))
-Incitec Pivot ((IPL))
-Jumbo Interactive ((JIN))
-Karoon Energy ((KAR))
-Lovisa Holdings ((LOV))
-Mach7 Technologies ((M7T))
-Macquarie Group ((MQG))
-NextDC ((NXT))
-Nufarm ((NUF))
-Pro Medicus ((PME))
-QBE Insurance Group ((QBE))
-Reliance Worldwide ((RWC))
-ResMed ((RMD))
-Santos
-Seek ((SEK))
-South32 ((S32))
-TechnologyOne ((TNE))
-Transurban Group ((TCL))
-Treasury Wine Estates ((TWE))
-Webjet ((WEB))
-Wesfarmers ((WES))

FNArena Talks

As has become a pleasant and enjoyable tradition, your editor was interviewed by Livewire Markets co-founder James Marlay last week ahead of the August reporting season.

The video (28 minutes) can be freely viewed through YouTube:

https://www.youtube.com/watch?v=bmFqS6iS_pc

Australian Banks Worried (Behind The Curtains)

The managing director of specialised daily news medium **Banking Day**, Ian Rogers, posted the following notification on LinkedIn on Monday:

"*Banking Day is hearing that the most candid versions of the outlooks prepared by the economics impresarios at the biggest banks are way more dour and pessimistic than those presented for public consumption so far.*

"Bank boards will be listening, and provisioning levels this profit season are going to be hiked, big time, for the hard landing ahead."

As one would expect, the post has quickly initiated a debate about what is likely, and less likely, to happen in Australia in the year ahead.

(This story was written on Monday 8th August, 2022. It was published on the day in the form of an email to paying subscribers, and again on Thursday as a story on the website).

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

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

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SMALL CAPS

Dr Boreham's Crucible: 4D Medical

Dedicated lung imaging pioneer 4D medical sees itself as a software company, with lots of future potential, including from the US military.

ASX code: ((4DX))

Market cap: $201.7m

Shares on issue: 294,491,837

Chief executive officer: Prof Andreas Fouras

Board: Bruce Rathie (chair), Prof Fouras, Lilian Bianchi, Dr Robert Figlin, John Livingston, Julian Sutton, Evonne Collier

Financials (June quarter 2022): customer receipts of $207,000, cash burn -$8.25m, cash balance $51.1m, quarters of available funding six.

Identifiable major shareholders: Velocimetry Consulting (Prof Fouras) 29.5%, Perennial Value Management 6.7%.

By Tim Boreham

The Melbourne-based lung imaging innovator soon might be able to boast of ‘by appointment to the US military’ among its early achievements.

As 4D noted in a recent media release, the US House of Representatives has called on the powerful US Department of Veterans Affairs to evaluate “emerging tech using existing x-ray imaging to derive four-dimensional models of lung function”.

That may sound vague, but not so much considering 4D Medical is the only current provider of dedicated 4-D lung imaging in the world.

The problem for Vet Affairs is that 3.5m military personnel have served in the Middle East since the 2001 al Qaida terrorist attacks and up to 10% have returned with serious, but hard-to-diagnose, lung conditions, such as constrictive bronchiolitis (more on this below).

A particular culprit is burn pits: the eco-unfriendly military practice of putting unsorted toxic waste into a hole, adding an accelerant and setting it alight - thus creating plumes of acrid, black smoke.

“We are starting to grasp the true health for many of the (veterans) who now suffer from incurable respiratory diseases which existing technologies failed to detect,” says 4D Medical founder and chief Prof Andreas Fouras.

“*We owe it to all veterans and their families to get them the help they need and deserve.*”

Meanwhile - and closer to home - 4D’s imaging has been adopted by I-Med, Australia’s biggest medical imaging chain.

Happy birthday

The 4D tech was the brainchild of Prof Fouras, a mechanical engineer who hung around Monash University's wind tunnel labs. From this experience he realised that there was a better way to measure air movement through the lungs and the product evolved from that.

Funded with a few coins from the back of the couch, Prof Fouras founded 4DX - as the company was then known - in 2012.

4D listed on August 7, 2020 at 73 cents a share after an oversubscribed initial public offer.

August 7? Many happy returns and let's hope we all have enough breath to blow out the candles.

Pre-float, 4D had raised $19m in equity and $17m in convertible notes.

4D contends that existing methods do not assess 'regional' performance in various parts of the lung, so are a substandard assessment.

In essence, 4D's tools supplements - but does not replace - the images produced by conventional x-rays, computed tomography (CT), magnetic resonance imaging (MRI) and the relatively crude spirometry.

X-ray and spirometry have been around since the late 1800s and are tried and trusted - but also have their limitations. For instance, CT scans work better with bones and dense structures rather than our air-filled bellows.

Here's to 'boring' lungs

4D's imaging can detect conditions including emphysema, chronic obstructive pulmonary disease (COPD), asthma, pulmonary and cystic fibrosis and occupation diseases such as silicosis.

4D's algorithms assess the nature of air movements through the lungs, which can indicate the type of disease based on where exactly the airflow is deficient.

Prof Fouras describes healthy lungs as "boring", in that air flows in and out uniformly.

"As soon as you have an illness it upsets the pattern," he says.

The four-dimensional data shows exactly where the air is flowing in the lungs and - worryingly – where it's not. For instance, pulmonary fibrosis will result in a lot of flow near the heart, but only a little at the edges.

And those poor veterans? Those with toxic exposures have lungs that "look like a patchwork quilt of small little problems everywhere".

LVAS has entered the building

4D's imaging software is called XV LVAS (as in lung ventilation analysis). The company has also developed physical scanners, in a consortium called the Australian Lung Health Initiative (ALHI).

In May 2020, the US Food and Drug Administration granted the XV LVAS clearance for imaging any lung indication, while Australia's Therapeutics Goods Administration followed suit in September last year.

A key point is that 4D is a software-based company and clients don't need the circa $650,000 scanners to be able to use its imaging. "We are an absolute, straight-up-and-down software-as-a-service company," Prof Fouras says.

He likens 4D to Microsoft, which sells laptops and such but will always be known as a software company.

Having said that, the scanners are useful for high-throughput clinics because they are faster and produce less radiation. The resulting abbreviated procedure also means they're more useful for wiggly kids and older people.

The scanners are yet to be approved but in March this year the first unit was launched at Sydney's Prince of Wales Hospital, by then Federal Health Minister (and now feather duster) Greg Hunt.

Founded by 4D Medical, the ALHI includes the University of Adelaide, the South Australian Health and Medical Research Institute, The University of New South Wales and the Royal Melbourne Hospital.

<u>Getting in bed with I-Med</u>

Coming back to the software, in June 2022, 4D signed a nationwide contract with I-Med Radiology Network, Australia's largest medical imaging chain with more than 250 clinics.

The two companies will also form a Lung Centre of Excellence, "to enable world class research and development activities to advance diagnostic imaging".

The three-year deal formalises an existing commercial arrangement.

The I-MED platform is predicated on an automated platform, by which the low-value x-ray images will be run through 4D's software without any human intervention.

Prof Fouras says seven I-Med sites to date - those with higher standard x-ray equipment - have turned on the LVAS software.

"We're broadening that rollout," Prof Fouras says. "As we progress it will also be compatible with CT and the vast majority have CT equipment."

<u>In the clinic</u>

Prof Fouras describes clinical studies as the "fundamental pillar" of its commercialisation strategy.

The company lists eight active advanced studies, with results expected soon.

In May 2022, attendees at the American Thoracic Society's international conference in Los Angeles were treated to the findings of a completed chronic obstructive pulmonary disease (COPD) imaging study, overseen by investigators from John Hopkins and the University of Miami.

The study enrolled 15 COPD sufferers and showed that XV LVAS was up to the task.

Melbourne's Alfred Hospital is taking the "interesting" approach of analysing about 40 lung transplant patients who have undertaken no fewer than 17 diagnostic procedures.

"Our test is being put head-to-head with all 17 of those, so it is the most comprehensive study by far," Prof Fouras says.

A US military trial focuses on veterans who have come back with constrictive bronchiolitis.

X-rays and computed tomography (CT) scans can't detect this ailment, because it affects the smallest airways of two millimetres or less.

Instead, suspected sufferers need to undergo a biopsy, which is not only painful but could involve a three-day hospital stay and the high risk of complications.

Management is confident the results will show good results on both specificity (false positives) and sensitivity (false negatives).

It is estimated that up to 10% of the 3.5m US veterans might have constrictive bronchiolitis, while they are also three times more likely to have a tobacco smoking-related illness.

"*Constrictive bronchiolitis is the most problematic toxic exposure [for veterans], but COPD also common and we have that covered too.*"

The company is also keenly interested in silicosis; the disease suffered by artisans such as stonemasons who have not masked up.

Finances and performance

The hardware (the scanners) were kindly funded by the Federal Government's Medical Research Future Fund (MRFF), to the tune of $28.9m over five years.

But with 4D required to match the funds, the company last year raised $40m in a placement and $6m in a share purchase plan.

The funding will cover the work required to support a marketing application to the US Food and Drug Administration, but 4D pays for the cost of commercialising the scanners and any other regulatory submissions.

In the June 2022 quarter, the company reported cash of just over $51m, with $15m of MRFF funding yet to be received.

4D's June quarter customer receipts of $207,000 are modest, but should get a wiggle-on given the "material" I-Med deal,

Shortly after listing, 4D shares peaked at $2.60 and in late June this year slumped to a low of 36 cents.

Nutting out the pricing

Prof Fouras says 4D's underlying philosophy is to 'democratise' the availability of the scanning. But to get into influential public sites, more clinical data is required and reimbursement is fiddly.

In Australia, the scan is likely to cost around $150 a pop, on top of the core - Medicare subsidised - x-ray imaging of a similar quantum.

"Our intent it to be very accessible and inexpensive," Prof Fouras says.

"The basic paradigm in healthcare is that if you are 10% better you can charge 25% more and we want to be twice as good at half the price," he says.

"Not only is it ethically the correct thing to do, but the pathway to the best profitability in the long term."

Commercially, Prof Fouras says I-Med was the "by the far the most effective place for us to put our efforts in Australia".

In the US, Veteran Affairs has agreed on US$171 ($250) per scan. Multiply that by 3.5m vets and that's an addressable market of - tap, tap - US$600m.

He says feedback to date suggests that few patients consider the out-of-pocket cost to be excessive.

Dr Boreham's diagnosis:

Prof Fouras says 4D's research and development budget of $10m is overshadowed by the likes of Siemens, which spends EUR4bn ($5.8bn) a year in its laboratories.

"We are an ant on a cork in the ocean and Siemens is the cruise liner coming on fast," he says.

Still on the maritime analogy, 4D looks to be enough nautical miles ahead so as not to be crushed by a larger 'vessel'. The company's boffins are already developing technology to measure blood flow though the lungs, with an announcement expected "in coming weeks".

Locally, the I-MED deal makes for a promising start, but the US military interest could determine the company's fortunes in the land of the free - albeit wheezing.

Bear in mind that the US military spends more on healthcare than the entire Australian government - even if it is to clean up the mess it made in the first place.

4D cites an overall global market of 377m lung procedures annually, worth US$31bn. Of this, the US accounts for 73m procedures worth almost US$14bn, so the potential is truly breathtaking.

Disclosure: Dr Boreham is not a qualified medical practitioner and does not possess a doctorate of any sort. His boring lungs have never been dubbed the life of the party and he hopes it stays that way.

This column first appeared in Biotech Daily

Biotechdaily.com.au

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

SMALL CAPS

Megaport: Focus Returns To Global Potential

Megaport's FY22 result highlighted significant metrics disclosed for the first time, underpinning broker views of a solid longer term growth story.

-Megaport had pre-released headline numbers
-Official FY22 report provided significant first-time disclosures
-Brokers consider the company a strong longer term prospect

By Greg Peel

Megaport ((MP1)) is very much a new age company that we could describe simply as engaged in cloud connection services, but for a better understanding we'll refer to the description provided to Yahoo:

Megaport Limited provides elastic interconnection services to the enterprises and service providers in Australia, New Zealand, Hong Kong, Singapore, Japan, North America, and Europe. It operates a platform that enables customers to connect their network to other services, as well as creates agile network that connects in multiple regions.

The company also offers Megaport Virtual Edge, an on-demand and vendor-neutral Network Function Virtualization service that enables branch-to-cloud connectivity on Megaport's global software-defined network; internet exchange services; and Megaport Marketplace, an online hub that interconnects service providers and enterprise customers. In addition, it provides cloud connectivity solutions; and virtual routing for cloud networking.

Megaport is very much a technology-based growth stock, yet to show a profit, and as such has been hit hard this year along with all companies (here and in the US) of a similar nature. The share price fell -77% from November last year to June this year.

As a growth stock, Megaport is beholden to bond yields which rose significantly over the period on central bank rate hikes before easing back on recession fears, hence the share price rebounded 106% to a peak in July. In July, the company pre-released headlines numbers from its FY22 earnings result. Yesterday, the official earnings release report provided a lot more colour.

Revenue was up 40% year on year, which reflected significant fixed cost leverage. Gross profit margin (after partnership commissions) grew to 62% from 53%. Operating costs in Australia Pacific and Head Office fell in the second half from the first, implying the company can rationalise costs when required.

The most significant metric was a first time disclosure of life time value versus customer acquisition cost, which came in at 6.3x. Morgans considers more than 3x worthwhile and 6x impressive.

This figure justifies spending aggressively in growth, Morgans suggests, although Megaport still needs to demonstrate progress towards becoming free cash flow positive on current funding – an issue that has led to investor hesitancy.

Management disclosed churn numbers for the first time, highlighting an annual rate of -7% customer churn. In Ord Minnett's view, this is relatively healthy and is backed by 50% customer retention after eight to nine years from Megaport's first two cohorts.

However, the sharp drop-off in Year 1 (average -14%) and Year 2 (average -11%) does suggest the targeting of computer-assisted coding (CAC) could be improved, according to the broker.

Longer Term Story

Morgans (Hold) remains a long-term bull on Megaport and its global potential. The broker expects to see improving sales traction over time as the indirect/channel partners ramp up.

However, experience suggests these things can take longer than anticipated. Consequently, Morgans would like to see several more quarters with incrementally positive sales momentum and declining cash burn to build a base and trend.

Similarly, Ord Minnett (Hold) notes FY22 was an investment year and management said additional time would be required for the benefits of these investments to come through. In this broker's view, there is sufficient time to wait on the sidelines and track Megaport's progress as it pivots to a partner-led sales model.

Macquarie (Outperform) notes regional margin expansion continues to improve, illustrating the longer-term upside from the company's operating leverage. This broker has lowered its earnings forecasts, factoring in the FY22 results, higher travel expense in FY23 and a re-base of currency impact on unit economics assumptions.

But despite moderating its forecast outlook, Macquarie believes the market has continued to underestimate the upside potential of Megaport's operating leverage.

Note that while brokers hold positive longer term views, on a daily basis share price movements have been proving very volatile, reflecting the volatility of bond yields and ever changing sentiment on growth versus value year to date.

Four FNArena database brokers cover the stock. UBS has updated on the result and retained a Buy rating. Citi (Buy) is yet to update. The current consensus target is $11.16, suggesting 27% upside.

Not in the database, Goldman Sachs highlights a stronger near term cost performance and improving disclosure supporting a long term opportunity. Buy with a $10.30 target.

Canaccord Genuity retains Buy with an $11.30 target.

SMALL CAPS

Negative Industry Trends Impact Australian Clinical Labs

FY22 results for Australian Clinical Labs missed expectations and brokers await an uptick in non-covid testing.

-Australian Clinical Labs misses the consensus FY22 forecast
-Higher covid costs and a sluggish base business weigh
-Credit Suisse notes negative structural and behavioural trends
-Brokers assess the FY23 outlook

By Mark Woodruff

It will be difficult for ASX-listed pathology companies like Australian Clinical Labs ((ACL)) to outperform the market when industry earnings should more than halve over the next 12 months.

While holding this view on reduced covid testing going forward, Citi increases its FY23 earnings forecast for the company on higher near-term testing, following FY22 results, though retains its Sell rating and $4.50 price target. A lower margin contributed to a weaker-than-expected result.

FY22 profit was $184m (-5% below the consensus forecast) after adjusting for costs incurred in the Medlab Pathology acquisition last November, while revenue of $996m was 1% ahead of the consensus estimate.

Management maintained its long-term earnings (EBITDA) margin target of 27% (excluding covid), despite an inflationary environment, which Citi attributes to the highly accretive nature of the Medlab acquisition.

Credit Suisse assesses FY22 profit fell below the consensus expectation due to higher covid costs and impacts in the second half from a sluggish base business. **The broker doesn't envisage a quick fix for the impact of structural and behavioural changes on earnings**, and downgrades its rating to Neutral from Outperform, while its target falls to $5.35 from $6.00.

Lower GP visits, higher rates of cancellations/absenteeism and staffing shortages are weighing on earnings, and management estimates an around -$70m "deficit" in non-covid testing, as volumes continue to trail behind pre-covid levels.

More positively, the company is net cash and announced a final dividend of 41cps, which was ahead of expectations held by Credit Suisse. As expected, no FY23 guidance was provided.

The average target price in the FNArena database, set by the two brokers previously mentioned, is $4.93, which suggests 4.3% upside to the prevailing Australian Clinical Labs' share price.

Outside of the daily-update database, Goldman Sachs retains its Buy rating in the wake of FY22 results, though lowers its 12-month target price to $5.70 from $6.50.

The broker notes a sequential slowdown in business-as-usual and covid volumes over June, due to an early and pronounced flu/respiratory virus season. However, July and August are tracking more strongly and the end-of-FY22 slowdown should reverse during early-FY23.

The company remains the preferred exposure of Goldman Sachs to the pathology space, as the stock continues trade at a discount to Sonic Healthcare ((SHL)) and Healius ((HLS)).

The outlook

All brokers highlighted the difficulty of forecasting due to the uncertainty related to covid and non-covid revenue.

Citi expects a recovery in non-covid testing demand in FY23 and feels the fate of the new financial year will also be determined by covid testing revenue and management of operating costs, as well as synergies from the Medlab Pathology acquisition last November.

While Credit Suisse is positive on the medium-term story and believes Australian Clinical Labs can achieve its margin targets, base business volumes need to return for the market to gain confidence on this and management's cost-out execution.

The more positive and Buy-rated Goldman Sachs notes that since the initial public offering in May 2021, the key debate with the stock has been the underlying (ex-Covid) profitability. To-date, it's felt execution has been in-line or better than peers in an industry that continues to face a declining-revenue profile.

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WEEKLY REPORTS

Weekly Ratings, Targets, Forecast Changes - 05-08-22

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

By Mark Woodruff

Guide:

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

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

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

Summary

Period: Monday August 1 to Friday August 5, 2022
Total Upgrades: 4
Total Downgrades: 13
Net Ratings Breakdown: Buy 58.89%; Hold 33.73%; Sell 7.37%

For the week ending Friday August 5 there were four upgrades and thirteen downgrades to ASX-listed companies covered by brokers in the FNArena database.

Pinnacle Investment Management received the largest percentage upgrade to target prices set by brokers last week after the release of FY22 results. UBS noted a 5% better result than forecast and responded by both raising its earnings forecasts and lowering its rating to Neutral from Buy on valuation grounds.

For the same reason, Ord Minnett downgraded its rating to Hold from Accumulate, despite fund flows and funds under management (FUM) exceeding expectations. Morgans noted net inflows slowed over the second half though remained positive and attributed softer retail flows to market conditions rather than performance.

On the other side of the coin, Zip Co had the largest percentage fall in target price set by brokers. Early in the week, Citi downgraded its rating to Sell/High Risk from Neutral/High Risk and halved its target price to $0.70.

These changes were made after the broker's growth forecasts were lowered meaningfully in response to the company tightened risk settings (to reduce bad debts), which is expected to negatively impact total transaction volume.

The broker also holds concerns over management's decision making (following costs of -$60m during the failed Sezzle acquisition), and the likelihood of a capital raise in FY24.

Later in the week, the company reported fourth quarter trading results and unveiled a new strategy to turn around the business operations. Brokers within the FNArena database are yet to express a view on either the results or strategy.

United Malt Group was next on the list for percentage fall in target price last week, after management downgraded earnings guidance only two months after a re-affirmation.

UBS suggested the turnaround revealed a lack of management "visibility" into earnings and operations, and lowered its rating to Neutral from Buy and its target to $3.05 from $4.65. As gearing levels ballooned, questions emerged over the company's ability to deleverage debt levels in FY23.

Morgans also reduced is target to $3.46 from $4.20 and raised the spectre of a structural change to the business, given more normalised earnings now appear to be well below proforma pre-covid levels.

United Malt also headed up the table for the largest percentage fall in forecast earnings. Coming second was Northern Star Resources after UBS strategists downgraded gold price forecasts for FY23-25 by -4%, -5% and -3%, respectively.

The broker felt stocks within the Gold sector are not as cheap as they look, due to both lower company growth ambitions and continued operating and inflation headwinds. Near-term earnings forecasts for stocks under coverage were lowered by -10-15% and price targets reduced on average by -3-5%.

UBS's preferred large cap exposure is Northern Star Resources for its net cash position and strong organic growth pipeline, and the Buy rating was retained, while the target fell to $9.80 from $10.00.

Centuria Office REIT also received forecast earnings downgrades from brokers last week, following lower-than-expected FY23 guidance. While FY22 results were broadly in-line with consensus forecasts, Credit Suisse noted interest costs and higher incentives to grow occupancy rates, alongside declining leasing spreads, are impacting the FY23 outlook.

Morgan Stanley suggested management’s interest rate strategy has not served the REIT well in the current macro environment. Heading into FY23, the average hedge duration is less than one year on the 56% of debt that is hedged.

Despite negative broker adjustments to Zip Co's target price, the company had the only material increase in broker earnings forecasts last week.

The increased earnings forecasts reflect a lower provision for bad debts, given the prior acquisition target Sezzle had higher losses.

Total Buy recommendations take up 58.89% of the total, versus 33.73% on Neutral/Hold, while Sell ratings account for the remaining 7.37.

Upgrade

CENTURIA INDUSTRIAL REIT ((CIP)) Upgrade to Outperform from Neutral by Credit Suisse .B/H/S: 4/2/0

Centuria Industrial REIT reported FY22 result which came in-line with Credit Suisse's expectations.

Notably the FY23 guidance was reduced below the broker's and consensus forecasts due to higher debt costs assumptions, which may prove to be overly conservative.

The price target is adjusted down to $3.42 from $3.75 and the stock is now seen trading at a -30% discount to NTA.

Credit Suisse views the bad news re debt costs as discounted in the price and upgrades to Outperform from Neutral.

PLEXURE GROUP LIMITED ((PX1)) Upgrade to Buy from Speculative Buy by Ord Minnett .B/H/S: 1/0/0

Plexure Group has renegotiated contract with McDonald's, a key customer, and Ord Minnett, in response, believes Plexure will be able to reach EBITDA and cash flow profitability in FY23.

Apart from de-risking the company's future, Ord Minnett also believes Plexure is now in a position to invest in the TASK enterprise
offering, which has continued to generate contract wins and offers a growing addressable market in Australia, Asia Pacific and the US.

On the back of higher forecasts, Ord Minnett has upgraded to Buy from Speculative Buy with the valuation lifting to 56c (new target) from 36c.

SITEMINDER LIMITED ((SDR)) Upgrade to Buy from Neutral by Citi .B/H/S: 3/0/0

SiteMinder's June-quarter result outpaced Citi's forecasts thanks mainly to a beat on transaction revenue growth arising from add-on products and international travel. The broker expects transaction growth will ease as the economy softens, but overall remains positive.

Property growth outpaced Citi but missed consensus; and Citi observes an uptick heading into FY23 and expects net adds will double in FY23 on reopening themes, improved labour dynamics, investment in go-to-market, and the launch of LH Basic.

Cash burn was worse than Citi forecast, albeit in line with guidance relative to revenue, but the broker expects the burn will slow as the company shifts to cheaper jurisdictions (it is moving operations to Manila).

Rating upgraded to Buy from Neutral. Target price rises to $5 from $4.95.

VIRGIN MONEY UK PLC ((VUK)) Upgrade to Outperform from Neutral by Macquarie .B/H/S: 1/0/0

Virgin Money UK's June-quarter result broadly met Macquarie's forecasts, with margin guidance proving a slight beat and triggering earnings upgrades.

The broker notes the company's balance sheet trends and leverage to interest rates lags peers but notes the buyback is strongly accretive.

Mortgage growth was below system but unsecured lending was strong, and the broker notes the company trades at a -50% three-year price to net-tangible-assets discount to big bank peers.

EPS forecasts rise 6% in FY22 and 4% in FY23. Macquarie upgrades to Outperform from Neutral. Target price is $3.95.

Downgrade

AMCOR PLC ((AMC)) Downgrade to Equal-weight from Overweight by Morgan Stanley .B/H/S: 4/3/0

While Morgan Stanley continues to like Amcor's quality and dividend support, growth may be more challenging in FY23, and the stock may be left behind in the event of a risk-on rally by the wider market. The rating is reduced to Equal-weight from Overweight.

The analyst highlights the stock has benefited from the prior risk-off sentiment, with shares outperforming the ASX200 by 17% this year.

Growth challenges in FY23 may derive from the currency, while the analyst observes higher funding costs have begun to emerge. The target price falls to $17.50 from $18.00. Industry view: In Line.

APPEN LIMITED ((APX)) Downgrade to Underperform from Neutral by Macquarie .B/H/S: 0/2/1

Appen's June-half update and FY22 guidance sharply disappointed Macquarie's expectations, due to slower growth, poorer margins, the spectre of more investment and decreased certainty on conversion of forward orders .

Poor operating leverage, combined with an FX hit and lower revenue, drove a crash in margins to 4.6% from 14.3%. Cash generation moved to the red, and guidance lacked clarity and confidence, says the broker.

EPS forecasts are cut -65% to -82% across FY22-FY26.

Rating is downgraded to Underperform from Neutral. Target price falls to $3.50 from $5.70.

ENDEAVOUR GROUP LIMITED ((EDV)) Downgrade to Sell from Neutral by UBS .B/H/S: 2/1/2

Endeavour Group is downgraded to a Sell from Neutral by UBS following the rise in the share price and a deteriorating risk/reward profile for investors.

The broker views the valuation as too stretched with the stock now trading at a similar PER multiple to ((WOW)) with the company's revenues not as defensive as assumed.

UBS highlights moderating retail spending will impact at the same time as Hotels re-opening is slowing and gaming is moving on-line, while inflationary pressures will impact on margins, such as rising labour costs.

Earnings forecasts are reduced by 3.2% for FY23.

A Sell rating and the price target is maintained at $7.20.

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

UBS downgrades its gold price forecasts for FY23-25 by -4%, -5% and -3%, respectively. It's felt stocks within the Gold sector are not as cheap as they look with the combined headwinds of lower company growth ambitions and continued operating and inflation headwinds.

The broker lowers its near-term earnings forecasts by -10-15% and reduces price targets on average by -3-5%.

The rating for Evolution Mining falls to Neutral from Buy and the target price is reduced to $2.80 from $2.90.

FORTESCUE METALS GROUP LIMITED ((FMG)) Downgrade to Sell from Neutral by UBS .B/H/S: 0/4/3

UBS explains Fortescue Metals reported record iron ore shipments of 48.5Mt for the June quarter which came in line with the analyst's estimates.

The company guided for FY23 shipments between 187-193Mt but UBS highlights unit costs and capital expenditure have increased and the broker is waiting for updates on the costs and timelines for FFI and Iron Bridge.

With risks to costs and a cautious iron ore price outlook, UBS considers the risk/reward at this point as too high.

UBS downgrades to a Sell rating from Neutral and the price target is lowered to $15.80 from $16.00.

PINNACLE INVESTMENT MANAGEMENT GROUP LIMITED ((PNI)) Downgrade to Hold from Accumulate by Ord Minnett and Downgrade to Neutral from Buy by UBS.B/H/S: 2/2/0

Ord Minnett comments Pinnacle Investment Management's FY22 performance proved in-line with expectations, but funds under management (FUM) was better-than-expected and so where funds flows.

The broker sees multiple reasons why profitability is poised for improvement, also supported by increased optimism about Affiliates.

Earnings estimates have gone up by 10%-12%. Alas, the share price has moved too, and Ord Minnett feels obliged to now downgrade to Hold from Accumulate.

Price target improved to $11.50 from $9.50.

After a 70% rally off the June low share price, UBS views Pinnacle Investment Management as expensive compared to other asset managers and downgrades the recommendation to Neutral from Buy.

The FY22 result, up 5% was better than the analyst forecast and excluding seed losses ($5.7m) the underlying numbers were strong.

Net inflows moderated in the 4Q22 from the previous quarter, ten boutiques provided $58m in performance fees and investment in Horizon 2 are likely to keep costs elevated.

Broker earnings forecasts have been raised 15% and 17% for FY23 and FY24, respectively.

UBS increases the price target 22% from $10.00 to $12.20.

The recommendation is downgraded to Neutral from Buy on valuation grounds.

QANTAS AIRWAYS LIMITED ((QAN)) Downgrade to Sell from Neutral by Citi .B/H/S: 4/0/2

Citi forecasts lower capacity growth and higher cost per available seat kilometres (CASKs) than the market is expecting, and lowers its rating to Sell from Neutral for Qantas. Higher staffing levels to address on-time performance levels are expected to weigh.

In the short term, the broker expects higher fuel prices and overstaffing will put pressure on margins and decrease capacity. The target falls to $4.28 from $5.47 on earnings revisions, higher capex estimates and lower market multiples.

SWOOP HOLDINGS LIMITED ((SWP)) Downgrade to Hold from Speculative Buy by Morgans .B/H/S: 0/1/0

Swoop Holdings' 4Q results and closing FY22 cash position were in-line with Morgans' expectations, while management guided to beat the upper end of FY22 earnings (EBITDA) guidance.

While the broker now incorporates the Moose Mobile acquisition into FY23 earnings forecasts, the previous 'premium for likely acquisitions' is now removed and the target falls to $0.68 from $1.44. The rating also falls to Hold from Speculative Buy.

TABCORP HOLDINGS LIMITED ((TAH)) Downgrade to Lighten from Hold by Ord Minnett .B/H/S: 2/3/0

Ord Minnett feels Tabcorp Holdings has missed the boat on digital market share by comparison to online bookmakers and downgrades its rating to Lighten from Hold on the prospects for heightened competition.

The broker also increases its capital expenditure estimates and lowers its target to $0.90 from $1.15. News Corp’s ((NWS)) market entry via BetR is expected to increase costs that have so far been necessary for Tabcorp to maintain market share.

TRANSURBAN GROUP LIMITED ((TCL)) Downgrade to Hold from Add by Morgans .B/H/S: 2/4/0

Morgans updates its forecast inflation and interest rate assumptions for stocks within its coverage of the Infrastructure sector.

The broker lowers its rating for Transurban Group to Hold from Add on recent share price strength.

The target falls to $13.90 from $14.42 as the (negative) increase in forward cost of new debt outweighs the (positive) increase in CPI outlook, explains the analyst, given revenues don't adjust as much as the cost of debt.

Morgans expects rapid growth in DPS over coming years from a rebound in traffic.

UNITED MALT GROUP LIMITED ((UMG)) Downgrade to Neutral from Buy by UBS .B/H/S: 3/2/0

United Malt downgrades earnings guidance at the Investor Day, only 2 months after re-affirming guidance which UBS believes raises concerns around management "visibility" into the earnings and operations.

The company highlighted headwinds across the business including crop problems with quality, supply chains and costs and pointed out aims to improve internal forecasting and more dynamic pricing contracts with clients to pass on cost increases.

Gearing levels ballooned and UBS questioned the ability of United Malt to deleverage the debt levels in FY23.

The recommendation is changed to Neutral from Buy in the absence of takeover offer or a turnaround in the earnings outlook.

Adjusting for a downgrade in earnings forecasts of -59%, -35& and -22% for FY22, FY23 and FY24, the target price is lowered to $3.05 from $4.65.

ZIP CO LIMITED ((ZIP)) Downgrade to Sell from Neutral by Citi .B/H/S: 1/1/3

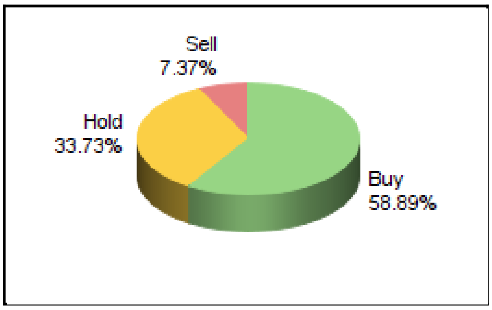
Citi lowers growth forecasts for Zip Co, expecting a fall in net bad debts will hurt time to value and that cash burn could rise in line with cost inflation.

The broker also expects transaction volume to weaken and fears an equity raising could emerge in FY24.

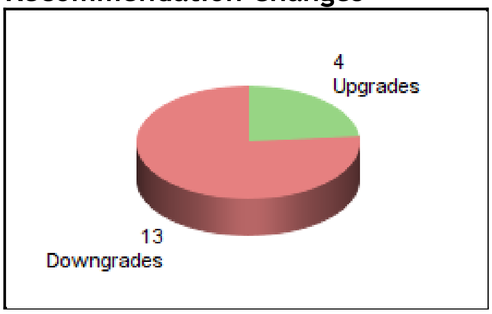
The broker downgrades to Sell, High Risk from Neutral, High Risk.

Target price halves to 70c from $1.40.

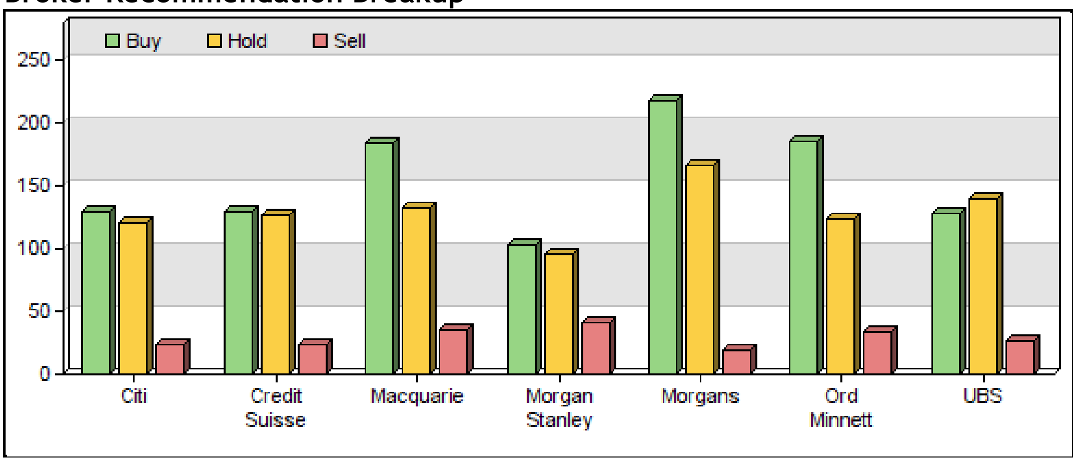
Total Recommendations



Recommendation Changes



Broker Recommendation Breakup



Broker Rating

Order	Company	New Rating	Old Rating	Broker
Upgrade				
1	CENTURIA INDUSTRIAL REIT	Buy	Neutral	Credit Suisse

2	PLEXURE GROUP LIMITED	Buy	Buy	Ord Minnett
3	SITEMINDER LIMITED	Buy	Neutral	Citi
4	VIRGIN MONEY UK PLC	Buy	Neutral	Macquarie
Downgrade				
5	AMCOR PLC	Neutral	Buy	Morgan Stanley
6	APPEN LIMITED	Sell	Neutral	Macquarie
7	ENDEAVOUR GROUP LIMITED	Sell	Neutral	UBS
8	EVOLUTION MINING LIMITED	Neutral	Buy	UBS
9	FORTESCUE METALS GROUP LIMITED	Sell	Neutral	UBS
10	PINNACLE INVESTMENT MANAGEMENT GROUP LIMITED	Neutral	Buy	Ord Minnett
11	PINNACLE INVESTMENT MANAGEMENT GROUP LIMITED	Neutral	Buy	UBS
12	QANTAS AIRWAYS LIMITED	Sell	Neutral	Citi
13	SWOOP HOLDINGS LIMITED	Neutral	Buy	Morgans
14	TABCORP HOLDINGS LIMITED	Sell	Neutral	Ord Minnett
15	TRANSURBAN GROUP LIMITED	Neutral	Buy	Morgans
16	UNITED MALT GROUP LIMITED	Neutral	Buy	UBS
17	ZIP CO LIMITED	Sell	Neutral	Citi

Target Price

Positive Change Covered by > 2 Brokers

Order	Symbol	Company	New Target	Previous Target	Change	Recs
1	PNI	PINNACLE INVESTMENT MANAGEMENT GROUP LIMITED	11.420	10.363	10.20%	4
2	SDR	SITEMINDER LIMITED	5.937	5.920	0.29%	3

Negative Change Covered by > 2 Brokers

Order	Symbol	Company	New Target	Previous Target	Change	Recs
1	ZIP	ZIP CO LIMITED	0.712	0.852	-16.43%	5
2	UMG	UNITED MALT GROUP LIMITED	3.932	4.610	-14.71%	5
3	TAH	TABCORP HOLDINGS LIMITED	1.092	1.133	-3.62%	6
4	QAN	QANTAS AIRWAYS LIMITED	5.880	6.078	-3.26%	6
5	CIP	CENTURIA INDUSTRIAL REIT	3.550	3.663	-3.08%	6
6	TLC	LOTTERY CORPORATION LIMITED	5.070	5.200	-2.50%	5
7	AMC	AMCOR PLC	18.592	18.758	-0.88%	7
8	TCL	TRANSURBAN GROUP LIMITED	14.450	14.537	-0.60%	6
9	EVN	EVOLUTION MINING LIMITED	2.771	2.786	-0.54%	7
10	FMG	FORTESCUE METALS GROUP LIMITED	16.829	16.857	-0.17%	7

Earning Forecast

Positive Change Covered by > 2 Brokers

Order	Symbol	Company	New EF	Previous EF	Change	Recs
1	ZIP	ZIP CO LIMITED	-38.540	-44.240	12.88%	5
2	SGR	STAR ENTERTAINMENT GROUP LIMITED	-2.996	-3.240	7.53%	5
3	PNI	PINNACLE INVESTMENT MANAGEMENT GROUP LIMITED	40.925	39.367	3.96%	4
4	TLC	LOTTERY CORPORATION LIMITED	13.182	12.892	2.25%	5
5	NIC	NICKEL INDUSTRIES LIMITED	13.704	13.519	1.37%	4
6	NWS	NEWS CORPORATION	122.065	120.577	1.23%	4
7	ANZ	AUSTRALIA AND NEW ZEALAND BANKING GROUP LIMITED	209.317	207.167	1.04%	6
8	DRR	DETERRA ROYALTIES LIMITED	32.885	32.585	0.92%	5
9	STO	SANTOS LIMITED	119.870	118.879	0.83%	7
10	DHG	DOMAIN HOLDINGS AUSTRALIA LIMITED	9.884	9.814	0.71%	6

Negative Change Covered by > 2 Brokers

Order	Symbol	Company	New EF	Previous EF	Change	Recs
1	UMG	UNITED MALT GROUP LIMITED	6.534	10.800	-39.50%	5

2	NST	NORTHERN STAR RESOURCES LIMITED	21.042	23.868	-11.84%	6
3	COF	CENTURIA OFFICE REIT	16.275	18.175	-10.45%	4
4	SGP	STOCKLAND	30.540	34.060	-10.33%	6
5	ORG	ORIGIN ENERGY LIMITED	28.456	31.093	-8.48%	6
6	GOZ	GROWTHPOINT PROPERTIES AUSTRALIA	25.233	26.567	-5.02%	3
7	OML	OOH!MEDIA LIMITED	7.950	8.323	-4.48%	3
8	GOR	GOLD ROAD RESOURCES LIMITED	9.700	10.133	-4.27%	3
9	CIP	CENTURIA INDUSTRIAL REIT	17.400	18.083	-3.78%	6
10	KAR	KAROON ENERGY LIMITED	12.327	12.791	-3.63%	3

Technical limitations

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

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WEEKLY REPORTS

Uranium Week: Summer Slowdown

Last week saw the uranium spot market into summer holiday mode, ahead of the weekend's passing of important US legislation through the Senate.

-Spot uranium market slows
-Critical US bill passes Senate
-Europe dealing with energy problems

By Greg Peel

As is typical in August, the uranium market slowed to a crawl last week as summer vacations dominated. Industry consultant TradeTech reports only two spot market transactions concluded, totalling 250,000lbs U3O8 equivalent.

Having shot up US$3.00/lb the week before, TradeTech's weekly spot price indicator eased by -US$1.00 to US$47.75/lb.

In term markets, attention was focused on the August 1 deadline for responses to the US Department of Energy's requests for proposal to supply its planned strategic uranium reserve.

TradeTech's term market indicators remain at US$51.50/lb (mid) and US$53.00/lb (long).

The spot price shot up last week on news Democrat Senate leader Chuck Schumer and Senator Joe Manchin had reached an agreement on the make-up of the Inflation Reduction Act. With Manchin on board, the only stumbling block would be Senator Kyrsten Sinema who, like Manchin, has a track record of dissent. But after tweaking a couple of elements Sinema, too, came on board.

The Senate vote on the weekend was thus 50/50, with the vice president using her casting vote. The legislation must now pass the House, but given a Democrat majority that should not be an issue.

The Inflation Reduction Act is viewed as a significant achievement for the US nuclear industry. The measure would invest US$369bn into energy and climate change programs, with the goal of reducing carbon emissions by -40% by 2030.

Clean energy tax credits would drive the majority of those emission reductions, including a production tax credit for existing nuclear power plants and a tax credit for investment in new zero-carbon electricity facilities, including nuclear power plants.

<u>Change of Heart</u>

Following the Fukushima disaster, the then German government started the clock on a phase-out of nuclear power in the country. Three plants remain in operation.

Last week, German Chancellor Olaf Scholz said it might "make sense" to extend the life of those plants, despite the fact they only account for only a small proportion of German electricity generation.

Europe's energy security situation, heading into winter, is dire.

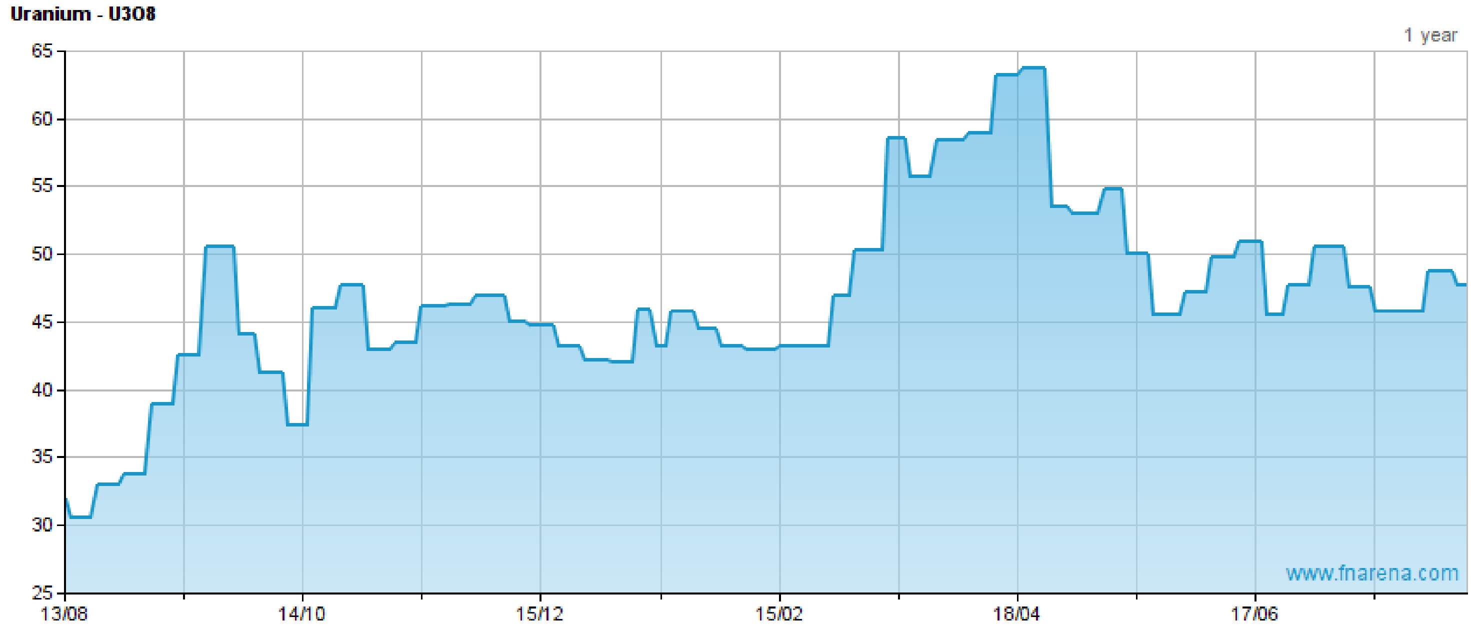
Ukraine has had to disconnect its Zaporizhzhia nuclear power plant – the largest in Europe – from the grid due to Russian bombing nearby. One missile hit electricity infrastructure. Of course, disconnecting the plant does nothing to alleviate the risk implicit in a direct hit.

But it's not just Putin causing problems for European power.

Last week, France, which derives 70% of its power from nuclear and is generally a power exporter, was challenged by record summer heat which led to higher river water temperatures. This places nuclear power facilities that use river water for cooling at risk of closure.

<u>Uranium companies listed on the ASX:</u>

ASX CODE	DATE	LAST PRICE	WEEKLY % MOVE	52WK HIGH	52WK LOW	P/E	CONSENSUS TARGET	UPSIDE/DOWNSIDE
BKY	08/08/2022	0.3500	0.00%	$0.64	$0.14			
BMN	08/08/2022	2.1900	▲ 3.35%	$2.29	$0.12			
BOE	08/08/2022	2.5600	▲ 6.38%	$3.10	$0.14		$2.600	▲1.6%
ERA	08/08/2022	0.2500	▼- 4.00%	$0.58	$0.16			
PDN	08/08/2022	0.7700	▲ 5.56%	$1.12	$0.42	-79.2	$0.800	▲3.9%
PEN	08/08/2022	0.2100	▲ 5.26%	$0.35	$0.12			
VMY	08/08/2022	0.1900	0.00%	$0.33	$0.09			



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

WEEKLY REPORTS

The Short Report - 11 Aug 2022

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

Summary:

By Greg Peel

Week Ending August 4, 2022.

The rally continued last week for Wall Street and the ASX200 in the wake of a Fed hint the next rate hike may only be 50 points. Since then we've had a strong US jobs number and lower CPI.

We can see from the preponderance of red below that the rally has not deterred the shorters on a net basis. There were only two short position changes of one percentage point or more last week, in opposite directions.

The week before last, EML Payments ((EML)) dropped -28% in one day after the Irish central bank, which investors had assumed EML had now satisfied, came back wanting more.

The stock has since rallied back but it seemed enough for some shorters to take profits on the way. EML shorts fell to 7.9% from 9.0%.

Megaport ((MP1)) had been rallying solidly up until early last week when it ran into profit-taking and then became very volatile on a daily basis. Short positions increased to 8.1% from 6.6%.

Bad move. Megaport reported earnings this week and shot up 10% on the day.

Weekly short positions as a percentage of market cap:

10%+
FLT 15.0
BET 12.3
SQ2 11.5
NAN 11.2
LKE 10.8

No changes

9.0-9.9

RRL

Out: EML

8.0-8.9%

ZIP, MSB, MP1

In: MP1 Out: PNV

7.0-7.9%

EML, ING, PNV, IEL, CCX, WEB, BGL

In: EML, PNV, WEB

6.0-6.9%

VUL, PBH, PDN, CUV, CXO, SBM, DEG, KGN, 92E, TPW, PNI

In: SBM, 92E Out: MP1, WEB

5.0-5.9%

BRG, AMA, NEA, ADH, BOQ, NHC, APX, FFX, OBL, JBH, PME, IMU, ASM

In: BRG, APX, ASM Out: SBM, SYR

Movers & Shakers

All covered above.

ASX20 Short Positions (%)

Code	Last Week	Week Before	Code	Last Week	Week Before
ALL	0.2	0.2	NAB	0.9	0.8
ANZ	0.7	0.6	NCM	0.2	0.2
BHP	0.3	0.3	RIO	0.8	0.8
CBA	1.0	0.9	STO	0.2	0.2
COL	0.6	0.6	TCL	0.4	0.4
CSL	0.3	0.4	TLS	0.1	0.1
FMG	1.7	1.6	WBC	1.2	1.2
GMG	0.8	0.7	WDS	1.0	1.0
JHX	0.4	0.4	WES	0.9	0.9
MQG	0.5	0.6	WOW	0.6	0.5

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

Guide:

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

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

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

IMPORTANT INFORMATION ABOUT THIS REPORT

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

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

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

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

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

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

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

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

WEEKLY REPORTS

In Brief: China Economy, Travel, Casinos, Meal Delivery

Weekly broker wrap: China economy stalls, travel industry recovery, gambling shakeup, meal delivery heats up

-China economy faces difficulties as zero-covid policy continues
-Travel industry recovery continues, with Australia benefitting from reopening of key markets
-Mandatory precommitments to be issued across electronic gaming machines in Victorian casinos
-More consumers using meal delivery services post-lockdowns

By Danielle Austin

A weak quarter for China drives full year downgrades

Oxford Economics has described the second quarter as dismal for the Chinese market, noting the nation's zero-covid policy appears set to hinder private sector growth as long as it in place. Results from the quarter have seen Oxford Economics decrease its 2022 growth forecast for China to 3.2% from a previous 4.0%.

The economists believe stable economic recovery in the region is dependent on the removal of the zero-covid policy, noting China failed to announce any additional stimulus funding in July, although does continue to attempt to reduce supply-side disruptions.

Oxford continues to expect an increase in quarter-on-growth in the second half, noting the cut to the full year growth forecast reflects the weaker second quarter while forecasts for the third and fourth quarters are largely retained.

Consumers prioritise travel spend amid ongoing industry recovery

Recovery continues in both the domestic and international travel industries, with JP Morgan finding consumer demand remains strong despite mitigating macroeconomic factors. Australia Pacific continues to lag other regions, but the broker highlighted meaningful improvement since the reopening of key domestic markets Japan and China.

Australian domestic passenger volumes as reported in June are now just -2.9% below pre-pandemic levels, up from a -5.9% pre-pandemic lag in May, while globally passenger volumes have recovered 70.8% of pre-pandemic levels and domestic flights are 81.4% of pre-pandemic levels.

Notably, the broker highlighted read-throughs from the US second quarter reporting season suggest consumers are continuing to prioritise travel spend and forward bookings are optimistic.

Gambling precommitments shake up industry

With the Victorian Government announcing its intentions to proceed with a further twelve recommendations submitted in the Victorian Casino enquiry, the analysts at Barrenjoey note new laws will see patrons set limits on their spend through mandatory precommitments.

The recommendation, which will see mandatory precommitments on all electronic gaming machines, will be implemented at Crown casino before the end of the year, and Barrenjoey expects this increases the likelihood of mandatory precommitments being adopted nation-wide. With mandatory precomittments being discussed for the last decade, Barrenjoey expects successful adoption in Victoria could encourage other states to follow suit.

Following implementation, vendors will be required to place a maximum limit on how much they intend to spend on machines. As a result in the inquiry punters will also be capped to a $1000 cash spend at the casino in any 24 hours and be required to use casino issued cards, which Barrenjoey notes was an expected step in the move towards cashless gaming.

Further, disciplinary action penalties for vendors have increased at least tenfold, with a new maximum fine of $100m.

Meal delivery services boom in covid shutdowns

Meal delivery services have emerged as a beneficiary of the pandemic lockdowns, with data from Roy Morgan demonstrating a lift in consumers accessing delivery services including UberEats, Menulog, DoorDash, HelloFresh and Deliveroo.

Roy Morgan analysts found the number of Australians using meal delivery services have almost doubled since early 2020 to over 7m from a previous 3.6m. The data highlighted UberEats as the clear market share leader, now used by 3.5m Australian consumers compared to 2.3m in early 2020.Segmentally, the research found those aged 31-46 were most likely to be using meal delivery services, with 45.8% using a meal delivery service in an average three months, followed by consumers aged 14-31 where 43% of consumers were accessing the platforms. Geographically, consumers closer to capital cities are more likely to utilise these services, while New South Wales and Victoria, the states who suffered the longest lockdowns, had the highest number of users.

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