Week
24

Stories To Read From FNArena

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Contents

Australia

Commodities

FYI

Fortescue Stirs Atlas Iron Speculation

Fortescue Metals has amassed a 19.9% stake in Atlas Iron and does not intend to support the current deal with Mineral Resources, unleashing speculation as to its true intentions.

-Hard to envisage why Fortescue would want low-grade iron ore -Is it intending to keep tonnage out of the market? -Could Fortescue use Atlas Iron as a launch pad for other minerals?

By Eva Brocklehurst

Fortescue Metals ((FMG)) has stirred the iron ore pot, amassing a 19.9% interest in Atlas Iron ((AGO)). Moreover, the company does not intend to support the proposed scheme of arrangement between Atlas Iron and Mineral Resources ((MIN)) on current terms.

Atlas Iron is predominantly an iron ore producer, with three operations in the north of the Pilbara. With the reserve grade for its current operations at around 57% iron the company has been a recipient of low-grade discounts.

Hence, theoretically, Fortescue Metals could be interested in the company's iron ore tenements, while Atlas Iron is impeded by the cost of trucking material to Utah Point, where it has port capacity around 13mtpa.

Credit Suisse finds it hard to imagine why Fortescue would want Utah Point as it is sufficiently accommodated at Port Hedland.

Also, given Fortescue has a strategy to create a new higher iron content blend, the broker finds it difficult to envisage any great interest in Atlas Iron's low-grade material.Shaw and Partners likes the Atlas Iron port capacity and allocation and believes this is a handy resource for the right company.

It may enable Fortescue to expand at some future date, incrementally and cheaply. Meanwhile, Fortescue has strong infrastructure and adding some Atlas Iron tonnage would not be a surprise.

Mineral Resources Bid

However, Shaw and Partners suggests the stake has the potential to scuttle the Mineral Resources ((MIN)) tilt at Atlas Iron. The scheme of arrangement for Atlas Iron underway requires 75% of votes and 50% of shareholders to be in favour of the takeover by Mineral Resources.

Morgan Stanley suggests the acquisition of shares by Fortescue Metals may now mean the decision is contingent on how the 31,500 individual shareholders vote.

Fortescue has not provided any reason for the accrued stake but the broker contemplates whether it may be to keep tonnage out of the market. The acquisition of shares is a small amount, around $75m, to pay to potentially restrict existing and any future expansion-related, low-grade tonnage.

Neither Atlas Iron nor Fortescue have indicated whether Fortescue will bid for Atlas.

Alternative Metals

UBS suggests the interest in Atlas Iron could be the result of several factors. While the company has undeveloped resources and -$500m in tax losses, Fortescue's interest may rest with the North West Infrastructure project, a joint venture between Atlas Iron, Brockman Mining ((BCK)) and FerrAus (owned by Atlas Iron).

The JV plans to develop a port facility that has capacity to export 50mtpa from the South-West Creek at Port Hedland. Ownership in Atlas Iron would enable Fortescue Metals to have input into the development and potentially increase its B class tonnage.

UBS suggests this combination could be a win for all parties involved, as Fortescue Metals could increase its tonnage, and the JV partners would be able to use existing infrastructure to access the port instead of developing rail and port infrastructure.

However, Credit Suisse has some other ideas. Atlas Iron has other development opportunities such as Corunna Downs and is also active in the lithium arena.

Atlas Iron has an exploration and DSO offtake deal with Pilbara Minerals ((PLS)) at Pilgangoora. The company holds to prospective tenements in zones of known lithium-tantalum deposits.

The first prospect, Cisco, which Atlas Iron sold down its 51% stake to Pilbara Minerals in 2017, has been noted to host mapped pegmatites alongside tantalum. The other prospect, Pancho, has been confirmed to contain lithium-caesium-tantalum pegmatites. The company is also involved in manganese.

Fortescue Metals has recently told the market it is interested in lithium and base metals. Credit Suisse points out the economics of Atlas Iron's existing iron ore operations are not compelling and discounting for low-grade ores makes the market challenging for producers.

Hence, this situation could imply that Fortescue Metals has set its sights on the potential lithium package. If such is the case, Credit Suisse interprets Fortescue's move as a far more pronounced and proactive step towards diversifying away from iron ore.

Shaw and Partners agrees there could be an opportunity for Fortescue in the lithium portfolio. The broker, not one of the eight monitored daily on the FNArena database has a Buy rating and $6.40 target for Fortescue.

FNArena's database shows six Buy ratings and one Sell (Citi). The consensus target is $5.51, signalling 17.8% upside to the last share price. The dividend yield on FY18 and FY19 forecasts is 5.3% and 5.5% respectively.

See also Could Eliwana Reduce Fortescue's Discount? on June 4 2018.

Lime Shines For Adelaide Brighton

Adelaide Brighton remains constructive regarding demand for both Australian residential and infrastructure materials, maintaining a strong outlook.

-Lime now expected to be stable versus prior guidance for marginally lower volumes -Increasingly positive regarding demand from the alumina sector -No major detrimental effect expected from competition in Queensland

By Eva Brocklehurst

At its investor briefing, Adelaide Brighton ((ABC)) singled out the stability of its lime business and highlighted strong market dynamics and a shift to infrastructure work.

Management is constructive regarding demand from both Australian residential and infrastructure activity and notes a strong improvement in concrete and aggregates in South Australia.

Lime volumes are expected to be stable in FY18, versus prior guidance for marginally lower volumes because of imports. The company is increasingly positive regarding demand from the alumina sector, which has emanated from stronger alumina pricing. The gold sector is also considered healthy.

The main disappointment is the continued delay of the northern connector project in South Australia, Deutsche Bank believes, while expecting this should be more than offset by other projects in the company's pipeline.

Macquarie agrees the market dynamics are favourable and the company is benefiting from a tightening environment. The lime business is a key input, at 11% of revenue, where the company has a premium margin and cash flow attributes.

The company is investing in expanding downstream capacity by acquisition and also via organic growth, such as concrete in Brisbane.

Management has noted that while NSW drove price gains in the past, strength has now developed nationally and Melbourne, in particular, has experienced better price realisation of late.

Macquarie, too, observes a broadening of strength in prices, although spot price improvements appear to be running ahead of contract prices.

Import competition in lime, which represents around 25% of group operating earnings (EBIT) is likely, at least in the near term, to dampen the market, both Deutsche Bank and Morgan Stanley suggest.

Deutsche Bank retains a Hold rating on valuation while Morgan Stanley finds the valuation difficult to justify and maintains an Underweight rating.

Macquarie's Outperform rating is at the other end of the spectrum. The broker likes the investment case, underpinned by solid execution on strategy, amid evidence of improved pricing power and infrastructure support.

Lime

The broker believes Adelaide Brighton has an enviable position in the lime market in Western Australia, providing long-term stable supply to the alumina industry.

The company enjoys the benefit of a low-cost limestone source in the shell sands, extracted 10km offshore. It has a dominant market position in this area and strategically superior assets.

Management intends to pursue further anti-dumping actions to curb lime imports in the Australian market. Once lodged, such actions have a six-month process. Adelaide Brighton does not intend to drop prices to recover lost market share, given the operating leverage in the business.

Competition

In Queensland, the company has expanded its concrete capacity in an attempt to secure more volume, without disrupting prices. Others are doing the same and Macquarie believes there is an inevitable risk to the market structure, although one Adelaide Brighton should be able to navigate well.

The company is also of the view that there will be no detrimental impact from the capacity expansions by construction material competitors in Queensland, at least in the short term, noting the strongest price increases for concrete in Queensland for the last five years.

FNArena's database shows one Buy (Macquarie), three Hold and two Sell. The consensus target is $6.06, suggesting -10.6% downside to the last share price.

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Brokers Increasingly Confident In Caltex

Caltex has issued profit guidance for the first half that is slightly ahead of expectations and brokers are largely confident in the company's outlook.

-Positive changes emerging with respect to the asset portfolio -Market expectations sufficiently negative such that risk/reward is skewed positively -Volumes will moderate amid increasing vehicle fuel efficiency

By Eva Brocklehurst

The key question for brokers regarding Caltex ((CTX)) is how defensive the stock remains, given the headwinds to volumes from a future with more fuel-efficient cars and electric vehicles.

The company has guided to first half RCOP (replacement cost of sales operating profit) of $295-315m while net debt is expected to increase to $950m because of the Seaoil acquisition.

On an underlying basis supply & marketing was broadly in line with UBS estimates. The broker estimates the market is now valuing this segment at a -25% discount to the ASX 200 industrials ex financials, despite only modestly lower growth.

Guidance is ahead of Ord Minnett's forecasts as refining fell less than expected, while Toyota Fleet Management and Ampol Singapore are boosting underlying supply & marketing earnings.

The broker upgrades to Buy from Hold because of valuation support, upgraded earnings revisions, confidence in refiner margins and the positive changes emerging with respect to the asset portfolio. Estimates for earnings per share (EPS) are lifted by 11.4% for 2018 and 7.4% for 2019.

Ord Minnett is confident that refiner margins will increase in coming months, noting industry competition in transport fuel remains rational. The asset optimisation review is slowly starting to sell retail sites, although neither a retail nor infrastructure sale is expected to be material.

The concerns the broker has centre on the transition in the retail operating model to corporate from franchising, which could create headwinds, while there are uncertainties regarding execution on the convenience roll-out, Foodary.

A loss of Woolworths volumes is possible but the earnings impact and risks are well known, in the broker's opinion. Macquarie agrees with Ord Minnett that meaningful infrastructure divestments following the asset review are unlikely while that the convenience store roll-out has some risks.

Macquarie upgrades, to Outperform from Neutral. The broker argues that supply & marketing has a defensive earnings stream that has consistently grown volumes and earnings.

Market expectations are envisaged sufficiently negative such that the risk/reward is increasingly skewed positively. The broker calculates that the business has de-rated to the extent that it provides compelling valuation on a sum-of-the-parts basis.

Morgan Stanley is less positive, with a view that earnings in marketing & supply will come under pressure. That said, a higher multiple is warranted, versus the stock's long-run PE average of 12x, given a larger footprint and more defensive business.

The establishment of a trading business in Singapore could also support the stock at a premium to the long-run average. Nevertheless, given a reduced earnings forecast for marketing Morgan Stanley maintains an Underweight rating.

Volume Pressures

Macquarie suggests, even with the future entailing more fuel-efficient cars and electric vehicles, earnings growth can be maintained throughout the medium term. Volumes are expected to moderate because of increasing vehicle fuel efficiency, while the impact from electric and autonomous vehicles is likely to be longer dated.

Australia lags many other countries in terms of electric vehicle adoption, with the broker noting only 1000 such vehicles were sold in Australia in 2017.

Macquarie calculates the expected compound growth rate from each of the Caltex product lines and applies it to the transport fuel mix, which suggests 0.7% volume growth per annum.

Furthermore, the shift in mix to higher-margin premium fuels, with premium petrol and diesel now 33% and 38% of the total, respectively, indicates further margin support for Caltex as consumers replace older vehicles with new ones.

Woolworths Fuel

On the protracted issue of the Woolworths ((WOW)) fuel supply volumes Macquarie expects a transaction will likely be completed in some form and, whatever the case, it will be an earnings headwind for Caltex.

The most likely scenario is that BP makes a substantial divestment of assets to a third party, IPO, or a trade sale to a new acquirer with little or no Australian footprint.

Mitigation activities on Caltex' behalf could include terminalling services or supplying part of the volume in certain regions, bolt-on or individual service station acquisitions and cost reductions. Estimates assume a loss of volumes starts in 2019.

While the loss of the Woolworths fuel supply agreement creates risk, UBS suggests that further cost reductions, the uplift from the convenience strategy and recent acquisitions offset this.

The broker calculates Caltex is now trading on around 13x 2018 estimates of EPS, which offers around 6% 3-year compound growth, along with a 4% dividend yield.

FNArena's database shows five Buy ratings, one Hold (Deutsche Bank, yet to update on guidance) and one Sell (Morgan Stanley). The consensus target is $36.49, suggesting 19.2% upside to the last share price. Targets range from $26 (Morgan Stanley) to $40.80 (Credit Suisse, yet to update on guidance).

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Challenger Reallocates For Growth

Challenger is reducing property and increasing fixed income exposure, which will deliver a negative impact on margins and earnings in the near term.

-Near-term cost to earnings but more sustainable future book growth -Opportunity to increase allocation to higher investment grade assets -Changes to means testing rules may be less punitive to lifetime annuity sales

By Eva Brocklehurst

Challenger ((CGF)) is reducing property and increasing fixed income exposure as it juggles its portfolio for the future. This provides for a less capital intensive model and greater ability to fund its own growth. A negative impact is envisaged by brokers for margins and earnings in the near term.

Operating from a more sustainable platform should enable Challenger to better capitalise on the growth opportunity from recent regulatory changes, Citi observes, as it becomes less reliant on equity raisings to support future book growth.

This improved ability to fund growth is the main offsetting positive, the broker adds, and also signals the company is confident in future growth, and appears to be the main motivation for the change rather than relative risk premia.

Although, the broker acknowledges, the current differentials in risk premia make it relatively fortuitous to be planning such a change at this time.

UBS agrees that, while there is a near-term cost to earnings, the decision provides for a more sustainable footing for funding annuity book growth in the longer term and this is a sensible trade-off.

Ord Minnett believes tough market conditions, where yields are being compressed, has forced Challenger to provide an offset by showing considerable book growth.

This implies potentially higher funding costs than might otherwise have been the case and, in such an environment, the broker suspects there may be constrained pre-tax profit growth.

Allocation Changes

Property allocation will be reduced to the mid teens, from 21%, which represents around $700m in asset sales. Challenger believes strong demand from offshore capital is flattening the returns in that asset class.

Once the transition is completed Citi estimates an adverse impact of around -5% to earnings per share from the changed allocation, but in the longer term this is likely to be less.

Citi has previously observed book values are relatively conservative and Challenger should, therefore, be able to achieve a profit on sale from the properties on disposal. Yet, given the disposals are one-off in nature, and there is uncertainty regarding the quantum and timing, no allowances are made in estimates.

With the timing of exact book growth uncertain, Credit Suisse also makes minimal changes to assumptions, downgrading normalised net profit estimates by -3% in FY19 and -4% for FY20. Reported earnings estimates increase 7% in FY19, allowing for investment experience gains.

Upside risk exists for growth opportunities in Australia, and Credit Suisse believes recent updates from federal Treasury are more than encouraging.

Macquarie agrees that, while the recent share price performance has eroded some of the valuation upside, the benign credit environment and favourable regulatory backdrop shall continue to support the company's current multiple.

Within the fixed income portfolio, Challenger will maintain its target of 25% non-investment-grade fixed income assets. Within investment grade it envisages an opportunity to increase the allocation to AAA and AA-rated assets.

Citi has previously pointed out the relatively high exposure to the lowest investment-grade (BBB) rating and believes the improved credit quality of the book is a further, small step towards de-risking the overall business model.

Regulatory Changes

New rules regarding means testing introduced in the federal budget are also likely to be slightly positive, Citi suggests, especially once lifetime annuities are combined with allocated pensions.

The broker flags that, for some reason, Challenger sought to play this down, as it indicated that new rules would result in outcomes that are broadly consistent with the old rules.

Changes to the means testing rules are also potentially less punitive to lifetime annuity sales than Morgans previously thought. The broker likes the Challenger story for the longer term but views the stock trading at fair value.

Citi also points out Challenger appears set to be the first in Australia to launch active ETFs and this makes it well placed to offer an increasingly diverse range of product. Fixed interest will be the first asset class in this area with others to follow in time.

Ord Minnett believes growth in the company's lifetime annuities will increase as a result of budget and regulatory changes, but cautions that these account for only 16% of the annuity sales today, and annuities worldwide have been unpopular in the absence of tax benefits or compulsion.

FNArena's database shows three Buy ratings, three Hold and two Sell. The consensus target is $12.23, suggesting -2.6% in downside to the last share price. Targets range from $9.50 (Ord Minnett) to $13.60 (Citi).

Material Matters: Iron Ore, Lithium & Cobalt

A glance through the latest expert views and predictions about commodities. Iron ore; lithium; cobalt; and energy.

-Preference for higher grade iron ore to continue -Lithium surplus building -Reign of cobalt may be short lived -Energy industry fundamentals improving

By Eva Brocklehurst

Iron Ore

Iron ore shipments from Port Hedland lifted 2.0% to 45.0mt in May, a new record for the month and only second to the record level of exports achieved last December. Around 80-85% of Port Hedland's iron ore exports are directed to China.

Commonwealth Bank analysts point to iron ore prices slipping in May because of this rising seaborne supply. Australian iron ore is particularly singled out in surplus, which helps explain why the 62% iron benchmark fell.

The analysts also note that lower steel prices are discouraging China's steel mills from procuring additional iron ore. China's steel demand is expected to slow to around 1.5% in 2018, from 2.5% in 2017.

The risk to the forecasts is to the downside, particularly if demand from China's property and infrastructure sectors slips further. Seaborne markets are expected to add more than enough to meet China's growth expectations.

The analysts expect iron ore prices to trend lower to US$55/t by the December quarter. Support should come from healthy steel margins and a structural preference is likely to be retained for higher grade ores.UBS also notes that steel prices and spreads remain high. The broker observes iron ore inventory at ports has lifted, despite another lift in steel output to all-time highs and this points to higher usage of scrap.

The broker expects seasonally stronger iron ore supply and an easing of seasonal demand could weigh on the market in the months ahead and a higher & steeper cost curve will come into play.

Benchmark prices have been range bound while low-grade discounts are stubborn at just above 40%, the broker points out.

Port stocks could lift further because of seasonally stronger iron ore supply as well as anecdotally stronger scrap usage. UBS considers the recent moderation in some of these iron ore signals warrants close monitoring.

Lithium

Citi has moderated its forecasts for the adoption of electric vehicles because of regulation, supply/infrastructure constraints and push-v-pull demand. This reduces expectations for lithium demand growth slightly to around 16% to 2025.

Meanwhile, the supply wave continues to build and prices are expected to fall further, to US$14,000/t in 2019 and US$12,000/t in 2020.

Unrisked supply from existing producers has potential to meet forecasts, so the question for Citi is how much market share will they be prepared to cede to new entrants, against defending prices. This is particularly relevant, given the low incentive price for additional production for some producers because of latent capacity.

On a risked basis the broker forecasts supply growth of 18% per annum which means a surplus will build over the next few years and then begin to tighten by mid next decade, as electric vehicle adoption rates gain momentum. Citi also notes a large divergence in price over 2018, with hydroxide holding up despite the fall in industrial grade.

The broker expects around 80% of the incremental lithium demand will emanate from electric vehicle batteries, which supports hydroxide producers. This could drive an increased premium for product quality and favour incumbent producers.

Cobalt

Hallgarten notes the surge in cobalt is based on the growth in electric vehicles, in the mistaken belief that cobalt is irreplaceable in the mix, and the fact there is a permanent shortage of the material because it has main source is in the Democratic Republic of the Congo.

The analysts suggest that while having an automobile industry made Japan and Korea into first world economies, the bankruptcy of various Western car companies in the last 20 years signals there may be less attraction for China to have an automotive industry than many imagine.

Hallgarten is more comfortable by the day with a short call on cobalt without paying any attention to the speculation. The broker accepts the chaos and lack of clarity in the DRC may signal higher prices but also suspects the reign of cobalt will be short lived, with yet more reasons ensuing to replace cobalt in battery formulations.

Energy

Morgan Stanley has upgraded its industry view for the energy sector to Attractive. The broker believes the downside risks that plagued the industry in 2017 are easing. Prices will likely remain volatile but the upside risk centres on the under-investment across the industry since 2014, combined with strong demand.

Energy cycles typically play out in years, not months, and the broker notes it is less than 12 months since the cyclical lows of mid 2017. At the same time, LNG fundamentals are improving.

This is considered to be good for the majority of the stocks Morgan Stanley covers, as oil prices drive cash flows from existing assets.

LNG fundamentals will also set up brownfield expansion opportunities, although risks continue, including the average contract tenure of new LNG contracts.

The average contract size is reducing, which means more buyers are required to underpin new projects. The broker expects established players like Woodside Petroleum ((WPL)) are best placed, given scale and long-standing customer relationships.

The broker's key Overweight energy stocks include Woodside, Origin Energy ((ORG)), Beach Energy ((BPT)) and FAR ((FAR)).

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Are Coal Prices Topping Out?

Supply and demand factors have induced a jump in coal prices in recent months but analysts are not convinced the high levels are here to stay.

-Downward trajectory for thermal coal in particular likely in 2019 -Disruption to shipments of Australian coking coal supporting prices currently -China's policy could still be successful in bringing down coal prices

By Eva Brocklehurst

Coal stockpiles in China have dwindled at both ports and utilities, causing prices to rise sharply. Analysts contemplate the latest surge in seaborne prices and the structural factors underpinning their longer-term forecasts.

Morgan Stanley envisages a sharp reversion to the mean for coal prices in 2019. The broker estimates prices could drop -39% versus spot and structurally weaker long-term demand is one of the drivers.

The fact that long-term demand is less appealing could also keep investors away, exacerbating the trend. The broker notes little to no investment taking place in new dedicated rail and port infrastructure, which have long pay-back periods, and capital expenditure on new mines is limited in the big export coal producing basins in Australia, South Africa, Colombia and North America.

On the other side of the world, China's supply-side reforms continue to exert a constraining effect on domestic supply. Yet China's power demand has increased by around 10%, while in India coal is being diverted to the power sector from the industrial sector to avert a shortage over the summer months.

Morgan Stanley suggests the challenges around demand over the longer term will prevent the equity market from re-rating these, currently excellent, cash flows from thermal coal in particular.

The broker notes, globally, Glencore has a most exposure to thermal coal, at around 33% of 2019 spot operating earnings (EBITDA). The broker estimates that Anglo-American and BHP Billiton ((BHP)) generate 23% and 16% respectively from coking (steelmaking) coal and 15% and 6% respectively from thermal (electricity) coal.

Coking Coal

Amid fresh concerns around the potential disruption to shipments of top-grade coking coal from Australia, prices have risen sharply, topping US$200/t recently. However, demand is observed to have softened over the year to date and the strong prices are providing incentives for alternative sources of high-grade coal.

Morgan Stanley suggests prices will be supported through June and July as the industry struggles to recover from cyclone-affected trade last year. Damage caused by cyclones to Aurizon's ((AZJ)) rail has continued to hamper exports.

The company originally focused on the Blackwater line that feeds the Port of Gladstone, where shipments are down 4% in the year to date, and has now shifted to the Goonyella line, which supports the 50mtpa Hay Point and 80mtpa Dalrymple Bay terminals. Significant disruption from maintenance is expected in June-July, which is typically a strong season for Australia's exports.

The shortfall in Australian exports, Morgan Stanley points out, is being offset globally by strong exports from Mongolia and the US, to some extent. US steel mills have been directed to lift purchases of US coking coal in order to reduce the country's trade deficit and this further supports seaborne prices.

Meanwhile, China is growing the use of scrap in steelmaking and its strict environmental controls mean local coke production has fallen. This has driven a decline in demand for coking coal and lower import volumes. Nevertheless, the several factors feeding into China's steel mill productivity suggest that demand for top-quality coking coal will continue to support the seaborne trade.

While Morgan Stanley expects Australia's supply disruption to cause significant upside risk to existing coking coal price forecasts, as reductions in Chinese steelmaking next winter come to bear, prices are expected to resume a downward trend.

Thermal Coal

Spot seaborne thermal coal prices are at the highest level since March 2012, responding to shortages in China. Warmer temperatures have boosted coal power generation, while environmental checks and rail maintenance have weighed on domestic supply.

Commonwealth Bank analysts highlight that official and independent sources are at odds on China's actual coal output. What is evident is that maintenance at China's largest coal-dedicated Daquin railway has weighed on the transport of domestic supply while policy makers have reimposed import restrictions at southern and eastern imports in April, exacerbating shortages.

In May, multiple measures were outlined to address the shortages, including increasing oversight of the sector to limit speculation and hoarding, perceived to artificially change prices, and to reduce the share of China's coal power generation to 58% in 2020, from 64% in 2015.

Policy makers have also reiterated their target band for domestic coal prices. While seaborne prices appear to have shrugged off the negative implications of import restrictions, the analysts believe that prices will eventually fall as policies take effect. They now forecast thermal coal prices to fall to US$77/t by the second quarter of 2019.

Since China started targeting coal prices in early 2017, the analysts note domestic prices have seldom moved into the target band, which is RMB500-570/t and equivalent to US$67-77/t. This band is well below spot prices of around RMB640/t.

However, it may be too early to consider the policy a failure. The analysts reluctance to make that call is reflected in China's goals to eliminate outdated coal capacity and improve the industry's profitability.

This has led to the elimination of 290mtpa of capacity, above the reduction target of 250mtpa. With the environmental backdrop, and the government maintaining efforts to bring down domestic coal prices, the analysts suspect the policy might still be successful in coming months.

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Weekly Ratings, Targets, Forecast Changes

By Rudi Filapek-Vandyck, Editor FNArena

Guide:

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

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

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

Summary

Period: Monday June 4 to Friday June 8, 2018 Total Upgrades: 6 Total Downgrades: 15 Net Ratings Breakdown: Buy 44.81%; Hold 39.59%; Sell 15.60%

It was the week before the long weekend. It was also the first week of June, which marks the end of the financial year in Australia and the period tends to carry its own characteristics ranging from portfolio re-shufflings to tax loss selling. It is also the time when companies 'fess up whether expectations are likely to be met for the year, or not.

In recent times this is equally turning into a period when many an ASX-listed entity organises an Investor Day, to get the masses outside of the ivory tower as excited about future growth avenues as the leaders are on the inside.

The Australian share market looked a bit shaky in the second half of May, but managed to catch up with more positive sentiment towards global risk assets in the first week of June. Only to be met by a wave of stockbroking analysts' downgrades for ASX-listed stocks.

For the week ending Friday, 8th June 2018, FNArena registered no less than 15 downgrades versus only six upgrades. Three of the downgrades were for resources stocks. Two of those are named BHP and Rio Tinto. Clearly, expectations for continuation of the upgrade cycle for the sector remain very much alive and that's also the reason behind both upgrades by JPMorgan/Ord Minnett.

On the negative side, we registered two downgrades for Wesfarmers, post investor day, as well as for Inghams Group, hamstrung by the sudden CEO departure.

Increases to target prices remain rather benign, considering Galaxy Resources leads the week's gainers with a lift of 5%, followed at arm's length by BHP, Domino's Pizza, and Rio Tinto. Domino's Pizza plans to drop the "pizza" part in order to broaden its appeal.

Noticeable reductions in consensus targets occurred for Regis Healthcare, Monadelphous, Santos, and Transurban.

Hardly any increases were registered for earnings forecasts, but there were plenty of negative adjustments with Metcash (yes, them again) grabbing the week's wooden spoon as forecasts suffered -27% after yet another write-down. Atlas Arteria (formerly known as Macquarie Atlas) saw estimates decline by -6.7%. Mineral Resources, RCR Tomlinson, and CommBank all experienced declines in forecasts during the week.

For the week ahead, macro-economics will take centre stage, along with REA Group holding its AGM, and with Challenger, Link Administration and Goodman Group hosting investor days.

Upgrade

BHP BILLITON LIMITED ((BHP)) Upgrade to Accumulate from Hold by Ord Minnett .B/H/S: 7/1/0

Ord Minnett expects strong prices are required to incentivise new supply to come on line in the iron ore and coal markets. This leads the broker to upgrade long-term forecasts to US$60/t for iron ore, US$140/t for hard coking coal and US$77/t for thermal coal.

Ord Minnett does not believe the sector is replenishing its project pipeline and that supports commodity prices. Therefore, the consensus upgrade cycle is likely to continue over the medium term. Moreover, low debt across the sector and a favourable macro backdrop are supportive of strong shareholder returns.

BHP is upgraded to Accumulate from Hold. Target is raised to $38 from $30.

CYBG PLC ((CYB)) Upgrade to Outperform from Neutral by Credit Suisse .B/H/S: 2/2/1

The bank has announced a 7% increase to its preliminary offer to acquire Virgin Money, noting the takeover panel and the board have agreed to extend the final bid deadline to June 18. Credit Suisse now believes the deal is more likely to proceed to a final offer.

As the stock has de-rated by -10% since a preliminary offer was announced the broker upgrades to Outperform from Neutral. Target is $6.

DULUXGROUP LIMITED ((DLX)) Upgrade to Neutral from Sell by Citi .B/H/S: 0/4/2

Following a site visit to the company's new Merrifield paint plant, and some weakness in the share price, Citi analysts have upgraded to Neutral from Sell. Price target has gained 10c to $7.60.

The analysts describe the new plant as "a world-class, highly automated operation with significant new product capabilities". They see upside potential for future revenues.

In addition, the company's strategic roll-out of Craig & Rose and Selleys brands in the UK market remains intact post the exit by Wesfarmers ((WES)). Here too Citi analysts see upside potential. All in all, they think DuluxGroup offers a solid platform for sustained growth, albeit with the notion the upside is likely to remain capped by weak indicators for new housing in Australia.

ESTIA HEALTH LIMITED ((EHE)) Upgrade to Outperform from Neutral by Macquarie .B/H/S: 2/2/0

Macquarie remains cautious about the aged care sector, as operating headwinds are unlikely to be alleviated in the short term. Estia Health remains the broker's preferred pick, having the most attractive distribution profile.

A conservative greenfield development book will reduce earnings drag in the near term, the broker suggests. Macquarie transfers coverage to another analyst. Upgrade to Outperform from Neutral. Target is raised to $3.60 from $3.37.

GALAXY RESOURCES LIMITED ((GXY)) Upgrade to Buy from Neutral by UBS .B/H/S: 3/1/0

The company has updated the definitive feasibility study for the Sal de Vida project and announced the sale of the northern tenements to help fund its development.

Capital expenditure guidance is lifted to US$474m. The agreement with POSCO for the sale of the northern tenements provides over half of this requirement.

UBS upgrades to Buy from Neutral. Continued de-risking of Sal de Vida could provide further upside, in the broker's view. Target is raised to $3.95 from $3.10.

RIO TINTO LIMITED ((RIO)) Upgrade to Accumulate from Hold by Ord Minnett .B/H/S: 8/0/0

Ord Minnett expects strong prices are required to incentivise new supply to come on line in the iron ore and coal markets. This leads the broker to upgrade long-term forecasts to US$60/t for iron ore, US$140/t for hard coking coal and US$77/t for thermal coal.

Ord Minnett does not believe the sector is replenishing its project pipeline and that supports commodity prices. Therefore, the consensus upgrade cycle is likely to continue over the medium term. Moreover, low debt across the sector and a favourable macro backdrop are supportive of strong shareholder returns.

Hence, Rio Tinto is upgraded to Accumulate from Hold. Target is raised to $96 from $78.

Downgrade

AINSWORTH GAME TECHNOLOGY LIMITED ((AGI)) Downgrade to Underperform from Neutral by Macquarie .B/H/S: 0/0/2

Macquarie suggests the FY19 growth outlook is challenging as new games are underperforming and there is low visibility on the sales to Churchill Downs and Novomatic. The broker's new pre-tax profit forecasts assume another step down in earnings.

Macquarie acknowledges that its forecasts are materially below consensus but highlights the high operating leverage and extremely low visibility.

Earnings per share estimates are cut by -26%. Rating is downgraded to Underperform from Neutral. Target is reduced to $0.95 from $1.05.

AGL ENERGY LIMITED ((AGL)) Downgrade to Neutral from Outperform by Credit Suisse .B/H/S: 3/4/0

Credit Suisse acknowledges that expectations for a moderate passing through of wholesale prices to end consumers in FY19 is unrealistic. Large customers are increasingly being offered below-market prices in exchange for committing to larger volumes and duration.

Moreover, government pressure, competition and a recent fall in both electricity and REC futures mean the expected increase in retail prices may not eventuate. Credit Suisse downgrades to Neutral from Outperform. Target is reduced to $23.25 from $26.00.

ATLAS ARTERIA ((ALX)) Downgrade to Hold from Add by Morgans .B/H/S: 4/2/0

Morgans continues to expect a strong rise in distributions over coming years, driven by growth in APRR operating earnings, a reduction in debt servicing and legislated tax cuts in France. Dulles Greenway will also pay first distributions after exiting lock-up in FY21.

Morgans reduces the target to $6.53 from $6.90, mainly as a result of updating AUD/EUR to current spot rates and also increasing the 2018 performance fee estimate while incorporating the new debt facility.

As a result, and because of the share price strength, the broker downgrades to Hold from Add.

ACCENT GROUP LIMITED ((AX1)) Downgrade to Reduce from Hold by Morgans .B/H/S: 1/0/1

Morgans has reviewed forecasts for Accent Group. The broker increases assumptions around store roll-out and margin given the improved hedging position and the move away from blanket discounting.

Nevertheless, a steep premium has now been factored into the stock and the broker is mindful of the competition intensity. Rating is downgraded to Reduce from Hold. Target is raised to $1.39 from $1.05.

CLEANAWAY WASTE MANAGEMENT LIMITED ((CWY)) Downgrade to Hold from Add by Morgans .B/H/S: 3/3/0

The company has indicated the China Sword policy restricting the import of contaminated recycling waste has impacted FY18 operating earnings (EBITDA) by -$3-6m. The Queensland government's landfill levy is not expected to have a material impact.

While Morgans remains attracted to the stock, the rating is downgraded to Hold from Add because of strength in the share price. Target is raised to $1.78 from $1.68.

INGHAMS GROUP LIMITED ((ING)) Downgrade to Hold from Add by Morgans and Downgrade to Neutral from Outperform by Macquarie .B/H/S: 2/4/0

Morgans has reviewed its investment thesis in the light of strong appreciation in the share price. The broker continues to expect the company to provide an impressive FY18 result.

Moreover, Morgans remains impressed with management's ability to significantly de-leverage the balance sheet in far from perfect operating conditions.

The broker downgrades forecasts for FY18-20 in the light of several emerging headwinds. Nevertheless, rolling forward the valuation, the target increases to $4.20 from $4.05. Rating is downgraded to Hold from Add, given less than 10% upside to the new target.

CEO, Mick McMahon, will be stepping down at the FY18 results. The transition has come earlier than Macquarie expected. The share price reaction has reflected this development and the strong regard in which the CEO is held, the broker suggests.

There is no change to the FY18 outlook, with feed cost increases being recovered via prices, both under contract and on the spot market.

While valuation is undemanding, the broker suggests uncertainty over new management is likely to persist until a permanent CEO arrives and there is clarity on the FY19 outlook.

Rating is downgraded to Neutral from Outperform. $4.00 target retained.

JUMBO INTERACTIVE LIMITED ((JIN)) Downgrade to Hold from Add by Morgans .B/H/S: 0/1/0

The company has flagged a strong trading period and expects total transaction value of around $182m for FY18. Morgans notes good cost control has also been in evidence, particularly in the low jackpot environment.

Forecasts have been upgraded and the broker currently sits ahead of guidance, given management's conservative track record.

With the stock trading above valuation, the broker downgrades to Hold from Add. Investors are expected to be rewarded over the next few years with a forecast 6%-plus gross dividend yield. Target has risen to $4.81 from $4.30.

MIRVAC GROUP ((MGR)) Downgrade to Sell from Neutral by UBS .B/H/S: 4/1/2

UBS economists are now forecasting a -5% plus fall in house prices over the next 12 months which leads the stock analysts to downgrade Mirvac to Sell. UBS believes Mirvac's best customer, the investor, and best market, Sydney, are likely to be most impacted by credit tightening.

The market is forecasting a soft landing for housing, the broker notes, suggesting positive earnings growth out to FY22. UBS sees downside risk beyond FY19, which is largely pre-sold. Target falls to $2.16 from $2.26.

MYOB GROUP LIMITED ((MYO)) Downgrade to Hold from Buy by Ord Minnett .B/H/S: 1/4/1

The company will not proceed with an acquisition of Reckon ((RKN)), instead investing $80m in R&D and sales and marketing. Ord Minnett concedes this is the right thing to do, as the longer term revenue growth guidance appeared a stretch.

The broker struggles to envisage why investors would increase positions until free cash flow has either bottomed in FY19 or there is clear evidence of improved returns.

Given limited upside to the new target the broker downgrades to Hold from Buy. Target is reduced $2.94 from $3.95.

REGIS HEALTHCARE LIMITED ((REG)) Downgrade to Underperform from Neutral by Macquarie .B/H/S: 2/1/1

RAD inflows from new facilities are likely to mean capital is recycled into developments and will not contribute to net debt reductions in FY19.

Macquarie expects EBITDA growth will be expensed to depreciation & interest payments and result in declines to distributions.

The broker transfers coverage to another analyst and downgrades to Underperform from Neutral. Target is reduced to $3.50 from $4.25.

RAMSAY HEALTH CARE LIMITED ((RHC)) Downgrade to Underperform from Neutral by Credit Suisse .B/H/S: 2/5/1

Credit Suisse believes Ramsay can continue to attract a more complex case mix versus other private hospital operators but will not be immune to a structural slowdown. The broker factors in 3% long-term organic volume growth and 1.5% pricing growth.

This reduces estimates for earnings by an average of -2.5% over the forecast period. The broker considers the stock overvalued and downgrades to Underperform from Neutral. Target is reduced to $56.50 from $68.60.

SANTOS LIMITED ((STO)) Downgrade to Sell from Neutral by UBS .B/H/S: 1/2/3

As part of a general sector review, UBS has decided to downgrade Santos to Sell, preferring Woodside Petroleum ((WPL)) and Origin Energy ((ORG)) instead. Target tumbles to $5.45 from $6.40 for Santos.

UBS has lifted oil price forecasts for the years ahead, but nevertheless finds the Santos share price at present represents a price of US$73/bbl, deemed the highest of all the major energy stocks in Australia, and this is seen as excessive.

WESFARMERS LIMITED ((WES)) Downgrade to Neutral from Outperform by Credit Suisse and Downgrade to Lighten from Hold by Ord Minnett .B/H/S: 0/4/2

Wesfarmers has emphasised more disciplined capital allocation and a higher risk threshold for M&A at its investor briefing. Credit Suisse envisages no lack of internal opportunities to support improved returns on capital over time.

While FY18 earnings appear supported by a strong performance in chemicals and growth in Bunnings and Kmart ,the recent share price appreciation causes the broker to downgrade to Neutral from Outperform. Target is reduced to $47.31 from $47.36.

The company's strategy briefing outlined growth prospects for various divisions. Yet,Ord Minnett finds a lack of valuation support because of the challenges to the Coles business and the risks emerging at Bunnings because of the consumer & housing environment.

There is also the risk of an oversupply of ammonium nitrate for industrial businesses and execution risk at Target that the broker cites. Ord Minnett downgrades to Lighten from Hold and lowers the target to $42.50 from $43.00.

Total Recommendations Recommendation Changes

Broker Recommendation Breakup

Broker Rating Order Company New Rating Old Rating Broker Upgrade 1 BHP BILLITON LIMITED Buy Neutral Ord Minnett 2 CYBG PLC Buy Neutral Credit Suisse 3 DULUXGROUP LIMITED Neutral Sell Citi 4 ESTIA HEALTH LIMITED Buy Neutral Macquarie 5 GALAXY RESOURCES LIMITED Buy Neutral UBS 6 RIO TINTO LIMITED Buy Neutral Ord Minnett Downgrade 7 ACCENT GROUP LIMITED Sell Neutral Morgans 8 AGL ENERGY LIMITED Neutral Buy Credit Suisse 9 AINSWORTH GAME TECHNOLOGY LIMITED Sell Neutral Macquarie 10 ATLAS ARTERIA Neutral Buy Morgans 11 CLEANAWAY WASTE MANAGEMENT LIMITED Neutral Buy Morgans 12 INGHAMS GROUP LIMITED Neutral Buy Morgans 13 INGHAMS GROUP LIMITED Neutral Buy Macquarie 14 JUMBO INTERACTIVE LIMITED Neutral Buy Morgans 15 MIRVAC GROUP Sell Neutral UBS 16 MYOB GROUP LIMITED Neutral Buy Ord Minnett 17 RAMSAY HEALTH CARE LIMITED Sell Neutral Credit Suisse 18 REGIS HEALTHCARE LIMITED Sell Neutral Macquarie 19 SANTOS LIMITED Sell Neutral UBS 20 WESFARMERS LIMITED Neutral Buy Credit Suisse 21 WESFARMERS LIMITED Sell Neutral Ord Minnett Recommendation Positive Change Covered by > 2 Brokers Order Symbol Company New Rating Previous Rating Change Recs 1 JHC JAPARA HEALTHCARE LIMITED -10.0% -38.0% 28.0% 5 2 GXY GALAXY RESOURCES LIMITED 75.0% 50.0% 25.0% 4 3 EHE ESTIA HEALTH LIMITED 50.0% 33.0% 17.0% 4 4 DLX DULUXGROUP LIMITED -36.0% -50.0% 14.0% 7 5 DMP DOMINO'S PIZZA ENTERPRISES LIMITED 38.0% 25.0% 13.0% 8 6 VCX VICINITY CENTRES 50.0% 42.0% 8.0% 5 7 SYD SYDNEY AIRPORT HOLDINGS LIMITED 63.0% 57.0% 6.0% 8 8 RIO RIO TINTO LIMITED 94.0% 88.0% 6.0% 8 9 BHP BHP BILLITON LIMITED 81.0% 75.0% 6.0% 8 Negative Change Covered by > 2 Brokers Order Symbol Company New Rating Previous Rating Change Recs 1 REG REGIS HEALTHCARE LIMITED 25.0% 67.0% -42.0% 4 2 ING INGHAMS GROUP LIMITED 33.0% 67.0% -34.0% 6 3 TCL TRANSURBAN GROUP 63.0% 86.0% -23.0% 8 4 WES WESFARMERS LIMITED -36.0% -14.0% -22.0% 7 5 MND MONADELPHOUS GROUP LIMITED -40.0% -20.0% -20.0% 5 6 CWY CLEANAWAY WASTE MANAGEMENT LIMITED 50.0% 67.0% -17.0% 6 7 ALX ATLAS ARTERIA 67.0% 83.0% -16.0% 6 8 AGL AGL ENERGY LIMITED 36.0% 50.0% -14.0% 7 9 MGR MIRVAC GROUP 29.0% 43.0% -14.0% 7 10 STO SANTOS LIMITED -33.0% -20.0% -13.0% 6 Target Price Positive Change Covered by > 2 Brokers Order Symbol Company New Target Previous Target Change Recs 1 GXY GALAXY RESOURCES LIMITED 3.775 3.563 5.95% 4 2 BHP BHP BILLITON LIMITED 34.128 33.128 3.02% 8 3 DMP DOMINO'S PIZZA ENTERPRISES LIMITED 48.635 47.385 2.64% 8 4 RIO RIO TINTO LIMITED 88.064 85.814 2.62% 8 5 SYD SYDNEY AIRPORT HOLDINGS LIMITED 7.378 7.299 1.08% 8 6 CWY CLEANAWAY WASTE MANAGEMENT LIMITED 1.730 1.713 0.99% 6 7 WES WESFARMERS LIMITED 43.321 42.943 0.88% 7 8 ING INGHAMS GROUP LIMITED 3.950 3.925 0.64% 6 9 JHC JAPARA HEALTHCARE LIMITED 1.824 1.815 0.50% 5 10 DLX DULUXGROUP LIMITED 7.241 7.227 0.19% 7 Negative Change Covered by > 2 Brokers Order Symbol Company New Target Previous Target Change Recs 1 REG REGIS HEALTHCARE LIMITED 4.250 4.500 -5.56% 4 2 MND MONADELPHOUS GROUP LIMITED 15.224 15.886 -4.17% 5 3 STO SANTOS LIMITED 5.542 5.690 -2.60% 6 4 TCL TRANSURBAN GROUP 12.820 13.149 -2.50% 8 5 RHC RAMSAY HEALTH CARE LIMITED 68.236 69.749 -2.17% 8 6 AGL AGL ENERGY LIMITED 24.169 24.561 -1.60% 7 7 ALX ATLAS ARTERIA 6.540 6.638 -1.48% 6 8 VCX VICINITY CENTRES 2.806 2.825 -0.67% 5 9 MGR MIRVAC GROUP 2.361 2.376 -0.63% 7 10 EHE ESTIA HEALTH LIMITED 3.650 3.667 -0.46% 4 Earning Forecast Positive Change Covered by > 2 Brokers Order Symbol Company New EF Previous EF Change Recs 1 EHE ESTIA HEALTH LIMITED 17.167 17.000 0.98% 4 2 WOR WORLEYPARSONS LIMITED 61.368 61.035 0.55% 6 3 AIZ AIR NEW ZEALAND LIMITED 32.011 31.856 0.49% 4 4 LNK LINK ADMINISTRATION HOLDINGS LIMITED 38.440 38.290 0.39% 7 5 CTX CALTEX AUSTRALIA LIMITED 233.586 232.729 0.37% 7 6 MFG MAGELLAN FINANCIAL GROUP LIMITED 129.560 129.360 0.15% 5 7 BSL BLUESCOPE STEEL LIMITED 148.817 148.650 0.11% 6 8 SYD SYDNEY AIRPORT HOLDINGS LIMITED 18.190 18.172 0.10% 8 9 TCL TRANSURBAN GROUP 26.953 26.928 0.09% 8 10 DLX DULUXGROUP LIMITED 38.383 38.350 0.09% 7 Negative Change Covered by > 2 Brokers Order Symbol Company New EF Previous EF Change Recs 1 MTS METCASH LIMITED 15.535 21.535 -27.86% 7 2 ALX ATLAS ARTERIA 30.608 32.808 -6.71% 6 3 MIN MINERAL RESOURCES LIMITED 164.250 173.500 -5.33% 4 4 RCR RCR TOMLINSON LIMITED 24.333 24.900 -2.28% 3 5 CBA COMMONWEALTH BANK OF AUSTRALIA 536.975 544.938 -1.46% 8 6 FPH FISHER & PAYKEL HEALTHCARE CORPORATION LIMITED 34.291 34.758 -1.34% 3 7 HVN HARVEY NORMAN HOLDINGS LIMITED 32.651 33.066 -1.26% 7 8 ALQ ALS LIMITED 34.512 34.890 -1.08% 6 9 REG REGIS HEALTHCARE LIMITED 18.300 18.500 -1.08% 4 10 JHC JAPARA HEALTHCARE LIMITED 7.975 8.033 -0.72% 5 Technical limitations

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

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Uranium Week: Unprecedented Intervention

Donald Trump is looking to take extraordinary measures to save America's coal-fired and nuclear power generators.

-US government to intervene in electricity market -Upbeat mood at nuclear conference -Spot price continues to tick higher

By Greg Peel

While the US oil & gas industry is enjoying a significant resurgence with the advent of new technologies in shale fracking, the US power generation industry is in crisis. Cheap gas means gas-fired power generators are significantly more competitive for the benefit of electricity generation, while renewable sources are enjoying state-based subsidies.

The price of coal is not cheap in relative terms, thanks to demand from China. Hence coal-fired generators, which also take a much longer time to switch and on off than gas-fired, are uncompetitive. So expensive is the cost of nuclear power generation that even with the uranium price at historical lows, nuclear generation is also uncompetitive.

In the absence of support to date, America's legacy nuclear plants are shutting down, or threatening to do so. Plans for new plant construction in many instances remains in limbo.

While Americans may be rejoicing at the availability of cheap, gas-fired electricity, the threat of the death of the coal-fired and nuclear generation industries is a risk to the diversification of US power supply, and to that end, national security – two of Donald Trump's favourite words (just ask Justin Trudeau).

To address the crisis, the president has directed his Energy Secretary to take "immediate steps" to bolster coal-fired and nuclear power plants that are economically challenged, being a matter of both national and economic security.

The plan is not, nevertheless, to provide federal subsidies, but to order electricity grid operators to buy electricity from coal-fired and nuclear plants to ensure they remain in operation. An initial two-year period is being considered, to ensure grid reliability and "promote the national defense and maximise domestic energy supplies".

As uranium industry consultant TradeTech notes, such an order would represent and unprecedented intervention into US energy markets.

Such an order would also result in a step-up in CPI inflation, given the consumer would be the one paying higher electricity prices.

Down in Monterey

Attendees at global commodity-based conferences typically come away feeling more positive as there is a tendency for all involved to "talk up" their prospects. However recent global conferences for the uranium/nuclear fuel markets, of which there are a handful each year, have been largely dour affairs. It's a bit hard to make a silk purse out of the sow's ear that is the market post-Fukushima, as reflected in persistent, historically low uranium prices.

However the mood at last week's World Nuclear Fuel Market conference, held in Monterey, California, was "upbeat and hopeful" according to TradeTech. The theme of this year's conference was "Searching for 'Eureka!' In the midst of a Seismic Shift".

While there are no reports of anyone leaping out of the bath and running naked down the street, fuel buyers and investors alike expressed hope in finding purchases in a challenging market. The "seismic shift" refers to changes in fundamentals of the uranium market in recent years.

One source of hope was confirmation from Kazakhstan's state-owned uranium producer Kazatomprom that it would cut production by -8% in 2018. Kazatomprom is the global swing producer in the uranium market in a similar fashion to OPEC in oil.

OPEC has recently surprised by sticking to its stated production quotas despite a long track record of never having done so before. In 2016, Kazatomprom announced a production cut of -10% in 2017 but managed only just over -5%.

So it's hope with a grain of salt.

Ticking Up

The upbeat mood was reflected last week in early buying which sent to the uranium spot price up a full dollar to US$24.00/lb mid-week. It proved a bit of an overshoot nonetheless, and by week's end TradeTech's spot price indicator was back at US$23.25/lb, up US25c on the prior week.

Six transactions were concluded totalling 650,000lbs U3O8 equivalent.

No transactions were concluded in term markets. TradeTech's term price indicators remain at US$26.50/lb (mid) and US$28.00/lb (long).

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The Short Report

Guide:

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

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

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

Summary:

Week ending June 7, 2018

Last week saw the ASX200 in rally mode, led by resources, as a risk-on mood seemed to permeate. The market then stalled for the long weekend and of yesterday, it was back to risk-off again.

Again we saw, last week, not a lot of movement in short positions. There's a bit of red towards the low end of the table but nothing substantial, with one exception.

MYOB ((MYO)) saw its share price plunge -8% last Thursday. Short positions jumped to 7.1% from 5.7%. See below.

We note, for the sake of interest, that at the very bottom of last week's table is Gateway Lifestyle Group ((GTY)) on 5.0% shorted. Yesterday's takeover offer for the company sparked a 15% share price jump.

Weekly short positions as a percentage of market cap:

10%+

SYR 19.8 DMP 16.3 JBH 15.6 GXY 14.1 MYR 13.5 NAN 12.4 AAC 11.9 ORE 11.9 VOC 11.8 GXL 11.4 IGO 11.2 NWS 11.0 IVC 10.9

No changes

9.0-9.9

HT1, GEM

Out: MYX 8.0-8.9%

HVN, MYX, MTS, BIN, AAD, PLS, IPH, GMA

In: MYX, GMA Out: MLX

7.0-7.9%

RFG, FLT, TPM, IFL, BGA, WEB, BKL, QUB, MLX, SFR, BWX, ING, MYO

In: MLX, BWX, ING, MYO Out: GMA, APO

6.0-6.9%

RSG, MOC, CSR, SEK, TGR, KAR, PRY, BAP, BEN, ALX*

In: BEN, ALX Out: ING, BWX

5.0-5.9%

NSR, AHG, NUF, SUL, CCP, NXT, APT, IMF, JHC, BOQ, GTY

In: APT Out: MYO, ALX, BEN

* Note:Atlas Arteria ((ALX)) is the new name for Macquarie Atlas Roads (MQA).

Movers & Shakers

Last week MYOB ((MYO)) announced it was pulling out of its bid to acquire the accountant group assets of rival Reckon ((RKN)). Analysts assumed ACCC requirements for approval rendered the acquisition unviable. Instead, MYOB will invest the money it had put aside in organic growth.

Analysts believe it seems sensible not to proceed, but have downgraded earnings forecasts as a result of the lost opportunity. Two downgrades to Hold or equivalent ratings reflect a view it's a hard road now ahead, organically, for MYOB.

Morgan Stanley went one step further when it took the opportunity to initiate coverage of the stock with an Underweight rating. In the new world of disruption, where software-as-a-service (SaaS) is king, the broker believes it will be the fast movers eating the slow movers rather than the big eating the small.

To that end, Morgan Stanley suggests Xero ((XRO)) is set to be the winner in the space, despite MYOB's entrenched longevity.

One might argue that once upon a time, MYOB appeared to "disrupt" the cosy world of accountants and bookkeepers.

MYOB's share price fell -8% on the news and short positions rose to 7.1% from 5.7%.

ASX20 Short Positions (%)

* Replaces AMP

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

IMPORTANT INFORMATION ABOUT THIS REPORT

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

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

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

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

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

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

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

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

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The Wrap: EVs, Health Insurance & Real Estate

Electric vehicles; health insurance; credit crunch; and real estate listings.

-High barriers still exist to electric vehicle take-up -Health insurer margins may come under pressure with Labor's proposed 2% cap -Continued weakness in home loan growth suggests credit tightening playing out -Longer "live" listings unlikely to benefit REA Group and Domain

By Eva Brocklehurst

Electric Vehicles

Cars that can drive for long distances without charging are being produced. So why has demand not taken off? This is the question Citi asks and suggests four main barriers to adoption exist before consumers will fully embrace the technology.

These include the range of travel, support infrastructure, battery degradation and cost. Looking at current demand, the broker finds the very early stages of adoption exist, with battery electric vehicles and plug-in hybrids making up just 1% of new car sales globally.

In order for penetration to truly increase demand, "pull" factors will need to take over. In this scenario, the broker suggests consumers need to believe the utility of such vehicles is higher than conventional vehicles and the price of batteries needs to come down enough so that a cost parity is reached.

Moreover, a network of charging stations will need to be installed to alleviate fears of "plug-in" being unavailable. Citi's base case scenario is for 10% battery electric vehicle penetration by 2030 and Europe and China remain the largest markets.

Health Insurance

Macquarie reviews the growth trends in claims across the private health insurance market and finds additional work days add pressure to the margin outlook. Traditionally, the re-pricing mechanism is pushed by costs so claims owing to additional work days would lead to higher premium increases.

This would keep margins relatively consistent. However, in the context of Labor's proposed 2% price cap for two years, should it form government after the next federal election, claims experience would not influence future price rises and margins could come under pressure.

Macquarie estimates the one-off impact could be around -100 basis points for both Medibank Private ((MPL)) and nib Holdings ((NHF)) in FY20, prior to any favourable claims trends and additional cost reduction efforts.

Credit Crunch

Home loans are the main indicator that UBS is watching for signs that its credit tightening thesis is playing out. Continued weakness in home loans growth in April suggests this is occurring even before the full impact of any macro prudential efforts.

The broker continues to expect loans growth to fall by -20% and credit growth to slow enough to be flat over the next year. House prices are expected to be down more than -5%. This suggests the Reserve Bank of Australia is likely to maintain the cash rate at current levels until the second half of 2019.

The total value of home loans, ex refinancing, declined in April by -0.4% after a -4.8% drop in March. The year-on-year level improved slightly but remains negative at -5.8%.

The prior lift in home loans was a driver of booming house prices so, in expecting loan growth to fall further as tighter lending standards come into force, UBS expects house prices to continue to decline.

First home buyers remain the brightest spot, amid support from stamp duty exemptions, and this segment's share of total loans has increased to around 12%, the highest since October 2012.

Real Estate Listings

Does the cooling housing market affect REA Group ((REA)) and Domain Group ((DHG))? UBS suggests the logic that these parties will benefit from a cooling market because listings remain on the market for a longer time is flawed.

Longer-time-on-market has historically been viewed as an offset to lower new listings but analysis signals this may not be the case. Even if there is a correlation, UBS suggests there tends to be a lag. In certain years, particularly in Sydney, when house price growth has stalled there was an initial improvement in new listings.

However, as house price growth remained consistently weak the supply and new listings eventually normalised and began to fall. The broker emphasises it is not forecasting a housing downturn or a sustained fall in residential new-listing volumes.

UBS also notes that internationally, the number one player has proven more resilient through industry shocks, as when agents/vendors are forced to rationalise spending they tend to choose the number one player over the number two.

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