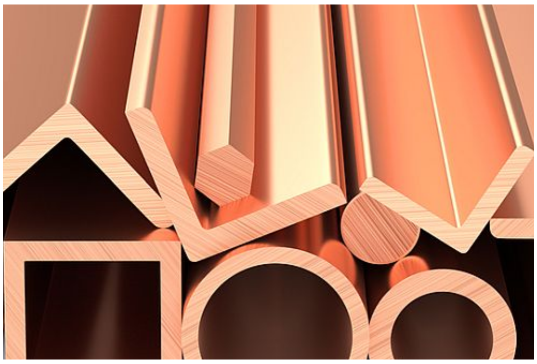
WEEK 49

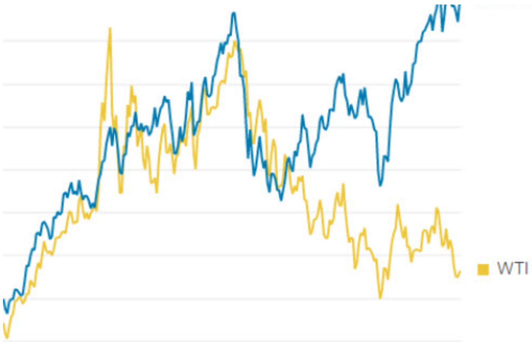
FINANCIAL NEWS, ANALYSIS & DATA

STORIES TO READ FROM FNArena

Monday, 28 November 2022



Material Matters: Critical Minerals, 25 Copper Companies & Commodity Indices



Rudi's View: Regrets, 2022 Delivered A Few

Collins Foods Hits Margin Wall

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FNArena
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AUSTRALIA

City Chic Out Of Vogue

Brokers have given City Chic Collective the chainsaw treatment following yet another disappointing market update

-City Chic Collective has issued yet another disappointing market update
-The average broker target in FNArena's database slumps to $1.56 from $2.45
-Operating margins fall, partly due to elevated fulfilment costs
-Ord Minnett feels margin contraction won't abate in the near term

By Mark Woodruff

The share price for fashion retailer City Chic collective has fallen significantly in the past two trading sessions on the ASX after releasing a year-to-date trading update.

The share price has slumped from $5.50 at the beginning of 2022 to be currently trading around 84 cents.

The company is a multi-channel retailer with an offer that appeals to plus-sized women across a variety of lifestyles. Brands include Avenue, City Chic, Evans, and Navabi.

In reaction to the trading update for July 1 to November 20, **two of the five covering brokers in the FNArena database have downgraded their rating for City Chic and the average target price falls to $1.56 from $2.45**.

Outside of FNArena's daily monitoring, Goldman Sachs lowers its target to $1.55 from $4.25, while Jarden's target falls to $1.17 from $2.09. Both brokers retain a Neutral rating.

Jarden points out consensus was expecting first half year-on-year revenue growth of 14% but management delivered a fall of -2%. US sales fell by -12% on declining traffic for Avenue, while sales in the EMEA region declined by -5% due to macroeconomic headwinds in Europe, according to the broker.

Avenue's growth in web traffic has been flat over the period and Evans' UK visitors have been down -10% year-on-year, explains the analyst.

Given the size of the decline in US and Australian online sales relative to the corresponding web traffic, Jarden assumes conversion rates and average basket sizes were lower.

Management noted competitive pressures have increased the promotional intensity in the Northern Hemisphere, eroding around -400bps of margin year-on-year. Macquarie also notes the twin impact from a mix shift to marketplace sales and elevated return rates in EMEA.

This broker points out a return to a net cash position by 30 June 2023 requires the company to meet its reconfirmed $125-135m inventory target for that date and release requisite working capital. Higher gearing is now expected at the end of December this year in order to lower recently elevated payables.

As weakness in the Northern Hemisphere is set to continue, Macquarie downgrades its rating to Neutral from Outperform. The broker sees limited near-term upside risk and expresses concern elevated stock levels leave the company vulnerable. However, it's felt the customer proposition (oversized women) still stacks up for the longer-term.

Ord Minnett also lowers its rating (to Hold from Buy) and feels **operating margin contraction from weaker demand is unlikely to abate anytime soon.** Contraction in the operating margin is being driven by declining gross profit margins and elevated fulfilment costs, explains the analyst.

Additionally, management incentives to lower inventory are likely to result in further margin erosion, cautions the broker.

<u>Additional broker views</u>

While Buy-rated Citi suggests there are material downside risks to consensus EPS forecasts following the trading update, the business does not appear to be broken and should benefit once pressures on consumers abate. A recent moderation of input cost inflation should also flow through to (and lessen) the cost of goods sold (COGS).

This broker also expects comparisons to the previous corresponding period will become easier.

Morgan Stanley cites some additional positives including an improvement in demand coming into the Black Friday/Xmas trading period. Competition could also ease into the second half of the financial year as peers reduce inventory, while it's felt the company's peak inventory has passed.

At the same time, the broker notes earnings downside risk should the sales trend continue in FY23, and points out the long-term impact on brand equity is unclear.

Many City Chic customers are low-to middle-income earners and are thereby more exposed to the recent higher cost of living, according to UBS. In response, the company has upped online promotional activity at a time when competitor discounting has been elevated, especially in the US, explains the analyst.

Further, as consumers react to the higher cost of living, product returns have increased and therefore increased fulfilment costs, highlights the broker.

Jarden' s Neutral rating is predicated upon ongoing earnings risks and uncertainty around the clearing of the stock oversupply over FY23-FY24.

Before becoming more positive, this broker would need to see evidence of City Chic returning to positive sales growth while being able to clear inventory without a sizeable impact on gross margins.

AUSTRALIA

Fletcher Building Too Cautious, Too Cheap

Predicted New Zealand residential housing cycle decline isn't enough to turn analysts off Fletcher Building, seeing through-the-cycle value in the company.

-New Zealand Residential declines likely to drive headwinds for Fletcher Building in coming years
-Analysts largely feel downside is accounted for in the share price
-Management has put company in much better position compared with previous downturn

By Danielle Austin

Despite predicting New Zealand residential consents to decline over the coming years, Goldman Sachs feels trough valuations for Fletcher Building ((FBU)) may be overdone. The broker considers the New Zealand residential market is at, or nearing, cyclical peaks, and anticipates residential consents to decline -1% over 2022, -14% over 2023 and -15% over 2024.

Despite cyclical headwinds, Goldman Sachs, who this week initiated coverage on Fletcher Building, feels downside is more than accounted for in the current share price.

Residential end market account for 47% of the region's revenue, but the broker expects exposure to non-residential and infrastructure end markets will offer some insulation, with these segments accounting for respectively 27% and 26% of regional revenues.

Residential consents for the year to September are tracking well ahead of the ten year average at 50,700. While the Australian residential market is also expected to face challenges, this segment accounts for only 9% of total revenue.

Goldman Sachs anticipates the current fiscal year will deliver peak earnings and margins for the company, but that group earnings will decline -4% per annum from FY24.

The broker feels this decline is priced into the current share price, and more specifically that the share price accounts for a -40% decline in residential construction demand in New Zealand.

By comparison, Goldman Sachs predicts a -30% peak to trough decline, and that efforts to reduce the fixed cost base and improve product mix on top of efficiencies leaves the company better placed than in prior downturns.

Guidance shows conservatism, brokers see a number of buffers

Within FNArena's daily coverage, brokers are largely in agreement Fletcher Building's guidance for FY23 looks conservative.

This includes Macquarie (Outperform, target price NZ$8.20), which agrees Fletcher Building has materially improved its business since the last cycle peak. This broker particularly highlighted strength in the company's cement division, and notably in its Golden Bay Cement business.

Noting Fletcher Building guides to earnings of NZ$100m in the current fiscal year, Citi (Outperform, target price NZ$6.53) also highlights conservatism in guidance and sees upside risk to its own outlook.

This broker expects growth investment returns and better than anticipated housing activity to flatten the decline over FY24 and FY25. Looking past the year ahead, a strong balance sheet, attractive valuation and potential improvement to the housing outlook all underpin Citi's constructive outlook.

Similar sentiments were echoed by Jarden (Buy, target price NZ$6.30), which is not part of FNArena's daily coverage.

In its last update on Fletcher Building in late August, Jarden noted New Zealand house prices were declining faster than had been expected, driving the broker to assume prices will bottom out by March 2023.

This broker also expects a subsequent earlier return to growth, anticipating banks are well placed to breathe life back into the housing market as the downturn approaches an end. Jarden sees a fundamental undersupply of housing in New Zealand as supporting Fletcher Building's return to upper-mid cycle trading.

Only four of seven daily monitored brokers in Australia cover the company, but all have a positive rating.

Trading around $4.70 on the ASX today, the shares carry the promise of 8.4% and 8.3% yields on current consensus estimates, when translated back into AUD.

COMMODITIES

Material Matters: Critical Minerals, 25 Copper Companies & Commodity Indices

A glance through the latest expert views and predictions about commodities: critical minerals; 25 copper exposures and commodity indices.

-Lithium and other critical minerals
-25 copper exposures for the energy transition
-Rebalancing projections for commodity indices

By Mark Woodruff

Lithium and other critical minerals

The International Energy Agency estimates that demand for critical minerals will increase by more than 300% by 2030.

Critical minerals are essential metals and non-metals which include lithium, cobalt, copper, nickel, zinc and rare earth minerals.

Nickel and cobalt are important for long range electric vehicles (EVs), zinc is needed to build infrastructure for renewable energy generation and copper is pivotal in the electrification of energy systems, points out ANZ Bank.

As well as their importance for EVs and renewable energy generation, critical minerals are used in energy storage, transport, electronics, defence, agriculture and telecommunications.

ANZ points out **Australia has an abundance of critical minerals and currently produces almost half of the world's lithium supply**, is the second largest producer of cobalt and the third largest producer of zinc.

Industry supply of lithium is limited, notes ANZ, in a demand environment where rechargeable batteries consume about three-quarters of world supply and EV battery demand has been rising sharply. Supply could be at risk not only due to scarcity but also from trade issues and other factors.

Despite a minor fall in lithium prices over the last few weeks on rumours of an EV production downgrade in China, ANZ observes prices are around record highs and should remain elevated, with perhaps some moderation.

By contrast, **Morgan Stanley suggests a material lithium price correction is on the cards for 2023**, **due to decelerating demand growth.** However, it's thought a longer-term supply shortfall may become the bottleneck, which could ultimately slow the transition to EVs.

This broker raises its long-term lithium price forecast by 70%, to a still-below-consensus US$12,000/t, though the range of potential outcomes is wider than for any other commodity under Morgan Stanley's coverage. Longer-term price risk is considered skewed to the upside, given the broker's view of constrained supply.

Interestingly, the analysts suggest demand substitution is unlikely in the foreseeable future, as lithium remains the best metal to carry ions.

For the short term, Morgan Stanley expects a China carbonate price of US$67,500/t in the first half of 2023 and US$47,500/t in the second half, with the latter price suggesting -35% downside to the current spot price.

Apart from a general over-production of batteries in China, subsidies for battery electric vehicle (BEV) penetration will be partially phased out, which the broker expects will slow growth in 2023. Geopolitical and consumer affordability/inflationary issues are also expected to weigh.

Prima facie, current and potential projects suggest longer-term supply of lithium shouldn't be an issue.

However, Morgan Stanley points to complexities involved in extracting, and especially, processing lithium. Recent history has shown developing (greenfield) lithium brine/mineral projects is technically challenging and project delays have been quite common.

Apart from difficulties in unlocking supply in some first-time producing countries (notably Africa), the broker suggests headwinds may arise elsewhere from community pushbacks and permitting challenges. In addition, more projects will be run by inexperienced new entrants/junior miners, with sometimes unproven (at scale) extraction techniques.

Adjustments to older project data to incorporate lithium industry cost escalation also contributes to Morgan Stanley's 70% upward revision to its long-term price forecast.

Underpinning Morgan Stanley's supply shortfall thesis, its lithium supply forecast model indicates the global BEV market can only sustain a sales penetration rate of 33% versus the broker's base case penetration estimate of 43%.

25 copper exposures for the energy transition

Canaccord Genuity sees structural demand growth potential for copper, driven by new energy technologies and the broader energy transition.

The broker highlights 17 emerging explorers/developers with exposure to this growth potential, but as yet do not fall under its research coverage.

For those companies within Canaccord's coverage, readers may refer to the FNArena website for a summary of the broker's latest research on producers OZ Minerals ((OZL)), Sandfire Resources ((SFR)) and 29Metals ((29M)).

Developers and explorers may also be found, and include Develop Global ((DVP)), Eagle Mountain ((EM2)), New World Resources ((NWC)), Peel Mining ((PEX)) and Titan Minerals ((TTM)).

Of the **17 emerging copper prospects identified by Canaccord**, a research summary from other brokers may also be garnered via the FNArena website for AIC Mines ((A1M)), Coda Minerals ((COD)), Cyprium Metals ((CYM)), KGL Resources ((KGL)) and Sunstone Metals ((STM)).

The remaining companies identified by Canaccord are at different stages of development and may loosely be divided by region.

Those advancing existing projects domestically include Caravel Minerals ((CVV)) in WA and Carnaby Resources ((CNB)) near Mt Isa in Queensland. Hammer Metals ((HMM)) is also exploring around Mt Isa, where it has recently extended its flagship Kalman deposit.

Rex Minerals ((REX)) has one of the largest mineral resources among ASX-listed developers at its Hillside project in South Australia, while Hillgrove Resources ((HGO)) is developing its Kanmantoo copper-gold just

55kms from Adelaide.

Also in SA, Havilah Resources ((HAV)) owns the Kalkaroo and Mutooroo projects, while over in NSW, Magmatic Resources ((MAG)) is an early-stage explorer, which recently had success in discovering its Corvette prospect.

Heading off overseas, Canaccord notes exploration efforts by Alvo Minerals ((ALV)) in Brazil and the three projects being advanced by American West Metals ((AW1)) in North America. Cobra ((CBE)) has also recently uncovered copper mineralisation at its Ngami project in Botswana.

Xanadu Mines ((XAN)) has two advanced exploration projects in Mongolia, while Cobra ((CBE)) recently uncovered copper mineralisation in Botswana.

If you prefer Hot Chili ((HCH)), the company is undertaking a pre-feasibility study for its top-ten undeveloped global copper resource, the Costa Fuego project in Santiago, Chile.

Rebalancing projections for commodity indices

Citi plans to rerun its calculations of target weights for the Bloomberg Commodity (BCOM) Index and the S&P GSCI Index in January 2023, closer to rebalancing time, though makes some preliminary forecasts on flow impacts.

The BCOM index is a financial benchmark that reflects commodity futures price movements, while the GSCI index also serves as a benchmark for investment in the commodity markets and as a measure of commodity performance over time.

From an investor perspective, these types of futures tracking commodity funds are a cheap solution to gain exposure to commodities. During the rebalancing in January gainers will be sold and losers bought in order to reset the target weights.

Crude oil should have the largest target weight in the BCOM index in 2023 (at 15% for Brent and WTI combined), according to the analysts, followed by gold (14.85%) and Henry Hub natural gas (7.94%).

As natural gas has seen outsized gains, and thus has much higher live weights in both indices, Henry Hub natural gas will require a gigantic outflow of -$8.7bn to bring down its weights to be in line with the targets, notes Citi.

Meanwhile, Brent and WTI should see inflows of $2.7bn and $2.2bn, respectively.

The energy sector target weights for the GSCI Index should gain 8.8% year-on-year, offset by lower weights for all other commodity sectors, predicts the broker. This is not considered surprising as energy prices have been significantly outperforming all other commodity sectors, and target weights for the index are calculated on production value.

Industrial and precious metals, the two worst performing commodity sectors this year, should see the largest rebalancing inflows to bring weights back in line with target levels for both indices.

ESG FOCUS

ESG Focus: Eye On Green Energy

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

ESG focus: ASX300 Eye Green Energy (2)

Fossil-fuel energy inflation hugged the spotlight in 2022 masking strong green-energy investment - a period in which green hydrogen came of age.

-Green energy hits a tipping point
-Global demand for green energy companies steps up
-Big money, big players, big action
-Renewables, green hydrogen and new nuclear hold pole position
-Green methanol and ethanol have a seat at the table
-Hydrogen vs batteries; the final battleground

By Sarah Mills

Green energy approached a tipping point in the year, in which most of the technological blocks and pricing points required to progress the transition fell into place.

Renewables (solar, wind, hydro and geothermal) are now an established part of energy production. Prices are plummeting but grid stability has proved intractable.

Enter green hydrogen, which is now competitive with fossil fuel prices thanks to the Ukraine conflict (at least in the lab).

In the real world, transport and storage remain a sticking point, but green hydrogen is at the point that, with investment and regulatory support by way of subsidies and tariffs, it offers a solution for grid stability, and prices are expected to fall precipitously from here.

Green methanol, or methanol from waste also received large financial commitments from big capital in 2022, particularly as a fuel of choice in shipping, and the world’s first green-hydrogen steel has been delivered.

Nuclear energy was included in Europe’s taxonomy under certain conditions.

Combined, these factors have brought the blueprint for the transition into focus.

This is for a world fired by renewable energy, with green hydrogen the preferred fuel for grid stability and any application requiring a more explosive fuel (such as aviation, heavy industry such as steel, and long, heavy haulage and shipping).

This is followed by more easily retrofittable green methanol, and biomethanol, and ethanol energy, and “acceptable” nuclear energy (yet to be fully defined for grid stabilisation) as the transition fuels of choice as gas is slowly phased out (most likely from 2030).

Carbon capture remains the dark horse, many doubting its credentials.

Some analysts continue to insist there is a place for the technology despite its failure to prove economic, claiming investment is estimated in the trillions over the decade.

In the US, for example, which has a plethora of old shale gas wells, the storage process is simple enough, but even there, transporting the gas to the wells is costly and the economics are never likely to stack up against renewables, according to most experts.

So this columnist still views carbon capture storage as a lobbying game for government dollars and a potential green-washing tool rather than a genuine solution. Although if climate change were to prove a genuinely imminent threat, it could be used as a desperate measure – particularly for extracting carbon from the air.

Even then, there are far more simple technologies in the making. For example, several companies are examining algae-based solutions, which pump seawater to algae-growing facilities where the algae are extracted and dried (releasing water back into the air) before being buried as land mass, or possibly used as fertiliser.

These technologies are already successful in the lab and, at face value, appear cheap and simple to replicate at scale.

<u>From Here On It's A Race</u>

The International Energy Agency estimates annual renewable energy investment will need to double from its current US$1.4trn a year out to 2030, taking total annual renewable energy investment to US$3.8trn. This compares with COP27's latest target of US$4trn a year (US$6trn at the upper limit).

Scaling green hydrogen is the main game going forward.

This will require government regulation to compete with fossil fuels (in both subsidies, and carbon taxes and tariffs), similar to renewables in the early days, and this is likely to be forthcoming within the next two years.

It will also require the development of off-take markets, much of which is already under way.

Memorandums of Agreements are being signed globally for the delivery of green materials and products. For example, in Australia alone, SSAB has signed deals with mining service provider Schlam and for the use of green steel in its dump trucks, and this is just one of a plethora SSAB has signed around the world.

Conversations around business tables these days are pivoting to the securing of green inputs as major companies seek to protect themselves from a flight of capital. The conversations are going something like "well if you can't deliver green, I will find someone that can, even if I have to pay more".

Many of the memorandums are filled with provisos centred primarily around affordability, but their proliferation provides a strong insight into the mood and focus of corporations as big capital turns its focus to decarbonising downstream markets.

Construction, materials and industrial markets are particularly vulnerable over the next few years and are marked as next off the rank for decarbonising.

As green hydrogen technology evolves, prices are expected to fall -75% by 2030 according to Renew Economy, and reach full price-parity as early as 2025, according to NEL, the world's largest manufacturer of electrolysers.

Goldman Sachs (one of the few to predict the rise of the oil price to above US$100/b from its covid-induced lows) says affordability, government policy and scalability seem to be converging to create "unprecedented momentum" for the clean hydrogen economy.

The analyst estimates green hydrogen's total addressable market could double to US$250bn by 2030 and become a US$1trn a year market by 2050.

It is now likely the world will approach another tipping point between 2030 and 2035 when global decarbonisation in downstream markets gathers pace and the green transition snowballs.

The economics of fossil fuels will fall sharply to a potentially precipitous point without intervention.

Big money attracts big pockets and financial heavyweights are jockeying for position as the new energy barons of the world, some publicly, some stealthily.

In Australia, Fortescue Metals Group ((FMG)) chairman Andrew Forrest has been open about his ambitions to support green hydrogen in a bid to attract the backing of big capital. Michael Cannon-Brookes has been active in the utilities market.

In a move that sent a shudder down the spines of Australia's cosy board corporate board community and their sometimes convenient skills matrices, AGL Energy ((AGL)) shareholders overruled the board to elect directors nominated by Cannon-Brookes.

Meanwhile, as renewables markets matured, markets witnessed a wave of mergers and acquisitions in 2022, which are only expected to accelerate over the decade as the world's would-be barons consolidate their positions and some of the more stealthy players start to emerge.

Demand For Green Energy Steps Up But Ukraine Proves A Brake

The Ukraine conflict turbo-charged the shift to renewables during 2022, as fossil fuel prices soared and the ASX300 sought avenues to cut energy costs and seek energy-price stability, raising demand for green energy.

Efforts in this respect were constrained somewhat by a slowing in growth in green finance markets but this is expected to recover when the Ukraine conflict abates.

While the date is anyone's guess, many are expecting an easing in Ukraine tensions by the European spring.

The Economist surmises that Russian President Vladmir Putin is hoping that a freezing winter may encourage the West to reconsider support, improving withdrawal terms.

The G7's demand for total Russian surrender ain't gunna happen in my view, and is simply jawboning.

Similarly, Ukraine is posturing, saying it will fight to the bitter end to regain its lands, even in the event of a nuclear strike, but already the West is urging the nation to consider future peace terms.

While the conflict also increased the world's appetite for fossil-fuels, IEEFA describes the recent increase in thermal power prices as a "short-term hiccup".

Global Commitments Accelerate

Meanwhile, the world's major nations and trading blocs upped the renewables ante in 2022.

In the US, the Biden Administration launched the Inflation Reduction Act.

In Europe, the push to reduce reliance on fossil fuels became even more pronounced after the Ukraine conflict threw into sharp relief the bloc's vulnerability to Russian gas supply.

In China, the nation's 14th five-year plan for Renewable Energy suggests China's energy generation from wind and solar will need to rise by 150Tw/h a year over 2021 to 2025, compared with 100Tw/h in the previous plan.

Under the plan, about 25% of China's energy will come from non-fossil fuel sources by 2030. At least half of increased electricity demand will be covered by renewables. The nation is also about to embark on an ambitious domestic electric vehicle rollout.

China has a track record for over-performing on renewables targets (in fact for over-performing on most measures), so the risk is to the upside.

The nation's Ministry of Finance also published fiscal and taxation policies this year to support the shift towards carbon neutrality.

To get a feel for the scale of China's investment: in 2021 the country's investment in clean energy constituted more than 30% of total global investment according to the International Energy Agency. The agency expects this trend will continue.

India is also investing heavily in renewables, and International Energy Agency describes the nation's scale of transformation as "stunning".

The IEA reports renewable electricity is growing at a faster rate in India than any other major economy with new capacity additions on track to double by 2025.

"India's sheer size and its huge scope for growth means that its energy demand is set to grow by more than that of any other country in the coming decades, which will support other lower-carbon energy sources and will ensure fossil fuels remain in the mix for some time," says the agency.

"Owing to technological developments, steady policy support and a vibrant private sector, solar power plants are cheaper to build than coal ones."

The IEA expects India to overtake Canada and China in the next few years to become the third largest ethanol market worldwide after the US and Brazil.

According to PV Magazine, India has already surpassed its target of achieving 50% of its energy from non-fossil fuel sources by 2030.

On the demand side, green hydrogen is a major force that promises to massively drive India's clean energy ambitions, says IEEFA.

"Companies such as the Adani group and Reliance Industries have wholeheartedly supported the country's green hydrogen policy, announced in June 2022, and its 5m tonnes p.a. target, with several major commitments," says IEEFA.

On top of transitioning to renewable energy, India is also one of the world's largest producers of modern bioenergy and is likely to lean heavily on green methanol to reduce coal imports, say observers.

Many governments are turning their sights to green hydrogen, including Britain, which is also upping its nuclear-energy capability.

Global Picture Bodes Well For Metals Markets

Rising global investment in renewables and green hydrogen infrastructure will be welcome for iron-ore and copper producers at a time when the Chinese construction market is slowing and the world is forecast to tip into recession.

A recession will conveniently take the pressure off raw materials prices just as demand from the clean energy sector steps up.

Renewables are likely to pick up the slack (assuming a soft landing) as new plants, electrolysers, green hydrogen infrastructure, green steel and electric vehicles start to flow.

The acceleration to renewables should also continue to support battery metals demand until new supply comes on board, or alternative technologies scale up.

China is about to ramp up its domestic electric-vehicle production, which should support battery critical minerals prices over the near term, such as nickel, cobalt, lithium, rare earths, copper and platinum.

Developments In Other Green Energies Downunder

Fortescue Metals' (and others') green hydrogen ambitions and the green commodities boom have overshadowed developments in other green energy markets in Australia.

Several Australian companies have been pivoting towards geothermal and green methanol markets and are worth a mention.

Oil and gas explorer Strike Energy ((STX)) has clean energy ambitions, operating geothermal plants on top of low-carbon urea (fertiliser) manufacturing ambitions, planning to be a net-zero manufacturer by 2030.

The company also announced in May its mid-west Geothermal Power Project in Western Australia's Perth Basin had been independently assessed.

The company is evaluating targets for a pilot program and it received a $2m grant from the Federal Government's Clean Energy Future Initiative.

On the green methanol front, Cleanaway Waste Management ((CWY)) was the major mover in 2022.

In June, Cleanaway announced it would pursue a $2bn waste-to-energy investment (analysts expect cost will blow out further as the project progresses), planning a permanent $15m increase to annual spending (up 60%).

Cleanaway continued to secure sites for energy-from-waste development projects in Victoria and Qld.

Like clean hydrogen, green methanol (derived from hard-to-recycle waste) infrastructure requires investment but it is considered a good option in many applications in the near term given, despite still releasing carbon emissions into the air.

Shipping giant Maersk established a Danish facility to produce e-methanol late last year, and this year ordered 19 green methanol vessels with dual-fuel engines that can operate on green methanol.

The shipping industry generally is leaning towards green methanol but it is far from a done deal, with ammonia a strong contender pending storage and fuel-cell technology. The main stumbling block is a lack of green methanol.

Meanwhile, a Bill Gates-led fund is also investing in technology that extracts hydrogen molecules from methanol to be used in a fuel cell, one of many innovations in the area.

Outside of shipping and waste-to-electricity, green methanol's markets appear dubious, but it is both a climate and circularity play containing high-quality carbon credits and projects should receive the support of big capital in the medium term.

Uranium is also likely to gain support for now, along with gas, but it could be a rocky road as big interests battle out the specs.

Britain, for example, is backing nuclear energy, but Germany as a major global manufacturer proceeded to close half its nuclear power stations even after the Ukraine conflict, and will be lobbying hard for taxonomy terms that favour its ex-nuclear status.

Observers expect the country may well yet litigate against the European Union's inclusion of nuclear in its green taxonomy, or at least demand more stringent rules on the type of nuclear energy provided, which could prove problematic for the uranium market going forward, if not nuclear energy per se, which is expected to continue providing energy to global grids for some time.

<u>Batteries And Green Hydrogen Fuel Cells – The Final Battle.</u>

All this takes us to the next phase of the green transition – the battle for market share between green hydrogen and battery technology.

At the moment, batteries have a big lead on green hydrogen fuel cells, but now the latter is ready to scale, the pair will be punching it out for market share some time in the 2030s.

Most analysts expect batteries will maintain dominance in land-based sectors such as electric vehicles, and that hydrogen will be used in any segment that requires high bursts of combustive energy, such as aviation and heavy industry.

Expensive battery costs could prove a weakness as hydrogen scales up. Batteries will have to become either more efficient, or use alternative materials, and there are plenty of innovations on the horizon.

All of this will have implications for the critical minerals markets in the second half of the decade and beyond.

Climate Energy Finance director Tim Buckley doubts green hydrogen fuel cells will gain the jump or prove a contender for at least the next decade.

In the long-term, green hydrogen is interesting. It requires expensive, dangerous technology to operate.

One would assume this favours more benign, readily available batteries; but it does increase the barriers to entry and is likely to be attractive to some energy barons from this perspective, in a similar way to existing fossil-fuel infrastructure.

Technological advancements in downstream industries would be the main swing-factor.

Flying cars, for example, are a reality and it is only a matter of time until they become a genuine alternative to wheel-based transport (it would rid the world of one of its greatest sources of plastic pollution).

But electricity doesn't begin to compete with combustible energy as a fuel source in the air. Developments in green hydrogen fuel cells could prove a game changer in this respect if battery costs fail to fall and renewable energy innovation (i.e. efficiency of solar cells and use in dyes for downstream purpose) stalls.

But all of this is mere speculative hot air, so distant is its horizon.

Our next articles take a deeper dive into individual clean energy markets over the next decade.

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RUDI'S VIEWS

Rudi's View: Regrets, 2022 Delivered A Few

In this week's Weekly Insights:

-Final Weekly Insights For 2022
-Regrets, 2022 Delivered A Few
-Conviction Calls

By Rudi Filapek-Vandyck, Editor

Final Weekly Insights For 2022

Weekly Insights is taking a break until January next year, when we start preparing for the February reporting season.

I hope you all enjoyed reading my weekly writings as much as I enjoyed preparing and sharing them.

Merry Festive Season to you all!

Regrets, 2022 Delivered A Few

You just know 2022 has been an eventful, but certainly unusual year when you look back over your shoulder and conclude moving into Overweight cash early has been the best decision made in the year.

As the Federal Reserve in the US, and many central banks around the globe, abruptly reversed course and embarked on probably the steepest tightening path ever witnessed, it seemed appropriate to lift the portfolio percentage in cash to 30%-40%, where it has been until last month.

Cash makes up less than 20% in November, but serious considerations will be made whether it should be higher ahead of what promises to be another volatile reporting season in January-February (US and locally).

A decision to convert part of the portfolio into cash always meets with emotive resistance and fierce rejections among investors. Is it possible to "time" the market (including when to get back in)? Shouldn't investors simply take a long term view and resist the urge to respond negatively during times of extreme volatility?

Certainly, there is a class of investors who holds a strong belief that share markets always recover and post gains in the long run. Those investors have been busy buying more stock upon volatility and weakness this year. Judging from some of the data available, there has been a lot of such buying at lower prices this year.

Contrary to what many might expect, including experienced veteran market commentators, bear markets are never quite the same. 2022 certainly has not been one-on-one comparable with late 2018, 2015-16 or that dreadful 2007-09.

This year, the **FNArena/Vested Equities All-Weather Model Portfolio** found itself quickly on the wrong side of share market momentum. As an investor in long-duration, high quality and growth companies, owning shares in Goodman Group ((GMG)), Hub24 ((HUB)), REA Group ((REA)), Xero ((XRO)) and the likes was never the ideal starting point in early January.

While the pressure from rising bond yields was relentless and inescapable, we take comfort from the fact the portfolio sold shares and substantially lifted the allocation to cash.

But there's another observation that equally deserves to be highlighted: in my research I try to distinguish the higher quality companies from the rest. Not that high or low quality makes a lot of difference during the run-away bull market that preceded this year, but when times got tough, it most definitely did.

Whereas many a prior high-flyer got smashed to pulp in the first half of 2022, personal favourites such as Pro Medicus ((PME)), TechnologyOne ((TNE)) and WiseTech Global ((WTC)) stoically stood their ground, and not simply in a relative sense (though they did fall a lot less than most High PE peers); as we approach the end of the calendar year these stocks are sitting on a net positive return.

Yes, you read that correctly. 2022 has not all been about fossil fuels and large cap financials. One of the regrets for the year is the All-Weather Portfolio went cautious and conservative early, and this included selling out of Pro Medicus, Xero, Breville Group ((BRG)), Charter Hall ((CHC)), Seek ((SEK)) and Hub24.

We did not get back in. With perfect hindsight, there are no silver bullets when it comes to protecting one's capital. In light of next year's plausible ramifications from the international 2022 tightening frenzy, there are reasons to remain cautious on immediate prospects for Xero, Breville and Seek, maybe for Charter Hall too, but this year's regrets definitely include Pro Medicus, WiseTech Global and Hub24 no longer being part of the All-Weather Portfolio.

We will bide our time. Today's eerily calm is unlikely to be representative of what next year will look like for the share market. Opportunities will present themselves, exact timing unknown.

Moving a large percentage of the portfolio into cash is not a panacea for all conditions and circumstances, but my personal contribution to the public debate is that local fund managers saw their return slump to -20% or more, sometimes a lot more, and the All-Weather Portfolio has kept losses this year in the single digits.

Raising the level of cash was specifically aimed at exactly such outcome. Or as I like to respond when receiving questions about it: it's never an attempt to "time" the market; it's aimed at reducing risk. There's a difference between the two.

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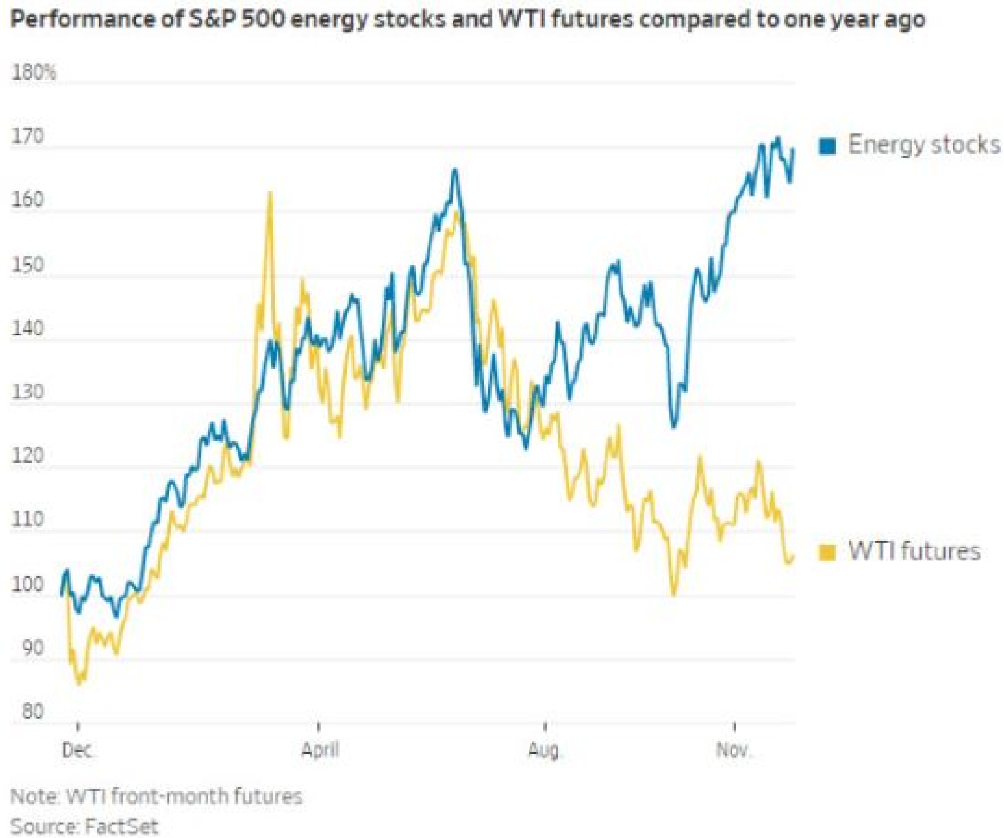
Resources and other heavily levered cyclical companies remain off the menu for the All-Weather Portfolio and that's certainly no help in a year when shares in coal producers quadruple and earnings momentum, including massive dividend payouts, resides with closed shop fossil fuel producers (Ukraine-inspired or otherwise).

Bear market rallies, including the one that is currently still taking place off the October lows, have been fierce and powerful, and they too benefit the lower quality, small cap laggards most.

Somehow I feel we shouldn't be overly disappointed with the small portfolio retreat that will likely mark this year on December 31. Most portfolio constituents and companies on my radar have largely compensated for earlier losses in the opening months, in particular over the two months past.

CSL ((CSL)), for example, is trading in positive territory year-to-date, ex a small dividend, as is Amcor ((AMC)) though the latter made all gains early in the year. Overall, your traditional defensives largely missed out on sustainable market momentum in 2022, including supermarket owners Coles ((COL)), Metcash ((MTS)) and Woolworths ((WOW)).

The largest surprise, however, has been the significant outperformance of energy producers, which is not solely because of LNG exposure and not simply a local phenomenon either. Investors should always be mindful of the fact that share prices in producers do not by default blindly follow the price of the commodity, but this year's de-coupling of share prices when the price of oil succumbed to fears of global demand shrinkage is still remarkable.



There's **no shortage in energy bulls** in today's market, but history shows that gap between the price of oil and share prices in Santos ((STO)), Woodside Energy ((WDS)), et al will close, exact timing unknown, and there are, roughly, two scenarios:

-either the price of oil picks up again and share prices for the sector globally have been proven prescient, confidently focusing on underlying fundamentals rather than short-term volatility in futures markets;

-or share prices will fall to match the price of oil to the downside.

My favourite observation about bear markets is that of **domino stones**; ultimately the last ones standing will also fall. Note, for example, how shares in high flying coal producers quickly lost -25% and more in just a matter of weeks recently. The latest sector to be hit are currently the producers of lithium.

Of course, such short-term sell-offs tell us nothing about the longer-term up-trends, but it is probably wise to keep an eye on what is happening in those smaller markets for what might follow next for your typical fossil fuel energy producer.

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Among the beneficial decisions taken this year is the addition of the Vanguard Australian Property Securities Index ETF ((VAP)) to the Model Portfolio on the belief that, yes, inflation might stick around for longer and central bankers are not yet done with tightening, but **bond yields might have seen their peak already**.

This ETF was added on an implied yield above 5%. According to the Vanguard website, the yield has now shrunk to 4.6% (implying there has been a rally in the price).

Bonds no longer rallying has equally allowed the share price in the HealthCo Healthcare and Wellness REIT ((HCW)) to appreciate from a very beaten-down looking level in weeks past, though volatility remains high on a daily basis, and it has been a disappointing allocation overall.

We haven't lost faith and if next year brings us uncertainty over corporate profits and lower bond yields, we will welcome the prospective 5% in payout, hopefully with some price appreciation on top.

Telstra ((TLS)) remains another yield stock in the portfolio, to date generating a small capital erosion for a prospective 4.3%. Telstra's attraction remains the sale of infrastructure assets, while underlying the shares should benefit from the same bond market dynamics.

The portfolio also stuck with retailer Super Retail ((SUL)) whose come-back is currently in full swing. At just under $11, Super Retail's prospective payout should yield 5.5% in the year ahead, though a lot will depend on whether margins and cash flow can be maintained.

The latter might turn into a crucial question next year, as also suggested yet again by shares in over-sized women's wear retailer City Chic Collective ((CCX)) whose latest profit warning has caused the share price to tank by -50%-plus in two days, after the shares had already lost circa -75% since the all-time peak last year.

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The All-Weather Model Portfolio has had no City Chic experiences this year, which can be interpreted as a vindication of the quality company choices, as well as the decision to reduce risk.

Xero, for example, is still carrying the risk of significant further deterioration in the post-Brexit UK economy, while the geographic exposure to troubled economies stretches further for Breville Group. This is why both are no longer in the portfolio.

Inside the All-Weather Portfolio, companies such as Amcor, CSL, Goodman Group, TechnologyOne, Carsales ((CAR)), etc have mostly stuck with positive guidance for the year ahead. Disappointments have thus largely been macro-related, including negative impact from FX and bond yields.

With one notable exception...

Iress ((IRE)) used to be part of the higher quality ASX listings, which had gone through a tougher period dominated by margin pressures.

The dangers of investing in higher quality companies is that quality generally requires maintenance and constant investment. CSL, as a prime example locally, invests more than $1bn every single year to secure its product pipeline and guarantee future growth.

Iress, it seems, is today but a shadow of its former quality self. I wouldn't be surprised if in years to come, investors rank it in the same basket as the likes of AMP, Lendlease, Myer and Westfield. Maybe they already do and I have simply been too slow in catching up (?).

Compensating for the solidity elsewhere in the Portfolio, Iress has been forced to issue two profit downgrades in the year past. Time to remove this company from my research radar.

The Portfolio sold out of NextDC ((NXT)) early in the year, and returned at much lower price level, only to see the shares take another leg lower. It turned out, investors are worried about a potential capital raising assuming company management is still looking to expand into Asia.

We're comfortable with the market position and longer-term growth dynamics that support the investment thesis in NextDC.

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All in all, the key question that pops up as share markets seem hell-bent on finishing 2022 on a positive note remains: if one became cautious and defensive too early, does that mean the decision itself was wrong, or was it just that the timing was off?

By now, early in the year I would have expected corporate profits had wilted and central bankers would be closer to pause or pivot, but none is the case as we prepare for 2023 (though there's lots of speculation about the latter).

The **market has simply split and polarised in 2022**. While we can all make confident predictions about what might be in store for next year, I think it's important to keep an open mind.

Shorter-term, investors best not forget about the challenges that are hitting corporate margins and profits. Share price action this year has been mostly directed by bond markets and other macro-considerations, including speculation about central banks' stamina.

While the latter will remain with us for longer, investors might be forced to pay attention to corporate challenges in the not-too distant future.

When this happens, I think we'd want to be on the right side.

More Weekly Insights reading:

-Preparing For Bear Market Phase II:

https://www.fnarena.com/index.php/2022/11/24/rudis-view-preparing-for-bear-phase-ii/

-Re-Opening Opportunities In Healthcare:

https://www.fnarena.com/index.php/2022/11/17/rudis-view-re-opening-opportunities-in-healthcare/

-More Choice For Income Hunters:

https://www.fnarena.com/index.php/2022/11/10/rudis-view-more-choice-for-income-hunters/

-Technology's Moment Of Truth:

https://www.fnarena.com/index.php/2022/11/03/rudis-view-technologys-moment-of-truth/

Conviction Calls

Shares in Breville Group have come under pressure this month and the reason seems to be related to market updates by peer companies in the US.

Sector analysts at **Wilsons and Jarden** weighed-in on growing concerns last week.

Wilsons suggested with weakness popping up in Q3 market updades for the likes of Williams Sonoma and Best Buy, this might be an indication the US consumer is simply following into the footsteps of consumers in Europe.

Not colouring the overall picture any rosier, DeLonghi has signalled both increased discounting and strong growth in manual coffee machines, which might be an indication the Italian competitor is grabbing market share from Breville.

Jarden focused on the fact a number of US retailers is sitting on too much inventory; this raises the risk of general price discounting to reduce stock. As part of inventories are supplier funded, Jarden has scaled back its expectations for margins.

All in all, Jarden has moved to Underweight on the stock (downgrade from Neutral) also because of momentum concerns across the EMEA countries, with a reduced price target of $19.20.

Wilsons is still sitting on Market Weight with a price target of $22.10.

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When it comes to seeking exposure to the local **lithium** story, **Macquarie's preferences** are with Mineral Resources ((MIN)) and IGO ((IGO)).

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Goldman Sachs' A&NZ Conviction List consists of 13, all Buy-rated, ASX-listed companies:

-Charter Hall Social Infrastructure REIT ((CQE))
-Elders ((ELD))
-Fisher & Paykel Healthcare ((FPH))
-HealthCo Healthcare & Wellness REIT
-Iluka Resources ((ILU))
-Lifestyle Communities ((LIC))
-NextDC
-Omni Bridgeway ((OBL))

-Qantas Airways ((QAN))
-REA Group ((REA))
-Webjet ((WEB))
-Westpac ((WBC))
-Woolworths Group

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How low 2023? According to the latest investment outlook by **Credit Suisse**, global economic growth next year will slump to 1.6% only. And no major central bank is expected to cut its cash rate.

Credit Suisse believes investors should consider adding fixed income assets to their portfolios.

Other predictions made: the eurozone and the UK will see recessions, while China will experience a growth recession. All regions will start a weak, tentative recovery by mid-year, on the assumption the US manages to avoid a recession.

On freshly updated projections, GDP growth next year in the US is expected to average no more than 0.8%, but to stay positive nevertheless.

Economic growth in Australia is projected to decelerate to 1.6%, in line with international growth, from 4% this year. Local inflation is expected to peak at 8% and to have fallen to 3.5% by year-end next year.

Credit Suisse expects a muted performance for equity markets in the first half next year.

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The latest update on 2023 by **Goldman Sachs** essentially reflects the same blue print outlook as projected by Credit Suisse.

The numbers look slightly different, but Goldman Sachs also sees the US economy narrowly avoiding negative growth (i.e. recession) while the recovery in China is expected to be "bumpy" and underwhelming.

The Federal Reserve is expected to hike by a further 125bp to 5-5.25%. Inflation will come down. No repeat of the 1970s is anticipated. No rate cuts are expected in 2023.

Recessions in Europe and the UK are expected to remain relatively mild.

(This story was written on Monday, 28 November, 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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- Make Risk Your Friend. Finding All-Weather Performers, December 2014 (The follow-up that accounts for an ever changing world and updated stock selection)
- Change. Investing in a Low Growth World. eBook that sells through Amazon and other channels. Tackles the

main issues impacting on investment strategies today and the world of tomorrow.
– Who's Afraid Of The Big Bad Bear? eBook and Book (print) available through Amazon and other channels. Your chance to relive 2016, and become a wiser investor along the way.

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https://www.fnarena.com/index.php/sign-up/

SMALL CAPS

Nanosonics Recovers On Less Negative Sentiment

A turn in sentiment has allowed Nanosonics shares to recover, with (some) broker views turning less negative.

-Post AGM weakness has been followed by a swift recovery for Nanosonic shares
-Company stated sales are tracking up 42% year-on-year, with lower volumes mitigated by higher prices
-Coris continues to present significant opportunity, but details still up in the air

By Danielle Austin

Times have been tough for shares in medical equipment manufacturer Nanosonics ((NAN)) post the all-time record high of $8 achieved during the general market euphoria of late 2020.

Earlier this year, share market turmoil saw the shares temporarily sink below $3 but successful recoveries have pulled the price back to around $4.50 a share.

A general market update at the company's AGM initially triggered renewed selling, but brokers Ord Minnett and Morgans responded with upgrades to respectively Hold and Add, no doubt assisting in the second share price recovery this year.

As far as the actual AGM update was concerned, the company reported a 42% sales increase in the first four months of the fiscal year, or 36% in constant currency terms. Notably, volumes decreased to an average 200 unit sales per month, from a prior average of 250 unit sales per month, with a price increase implemented by Nanosonics offsetting the impact.

The company continues to target sales growth of 20-25% over the year.

Coris launch remains significant opportunity for the company

Analysts remain largely positive on the longer-term opportunity presented by Nanosonics impending Coris device launch. The company remains committed to a launch in 2023, but additional detail is still lacking (and has been a main point of criticism).

The launch will initially be focused in Europe and markets outside the US. The launch has already faced lengthy delays as a result of engineering and chemistry complications, but early data have been promising.

Ord Minnett (upgraded to Hold from Lighten, target price $4.00) expects the strength of the first four months is such that Nanosonics will be able to beat full year sales guidance even while anticipating challenges later in the year.

The broker’s recent upgrade accounts for the potential for Nanosonics to lift FY23 guidance. Ord Minnett anticipates the higher revenue to drive a 60% profit boost for the company.

The broker is optimistic Coris will prove an important new product, and justify the elevated valuation.

The initial post-AGM weakness pushed the share price well below stockbroker Morgans’ target price of $4.91, triggering an upgrade to Add from Hold.

Morgans’ primary concern is around timing of the Coris launch, but expects the device can deliver a significant contribution to revenue and profit once regulatory approvals are secured.

Given lack of visibility around the timing of regulatory approvals, this broker includes only a modest revenue contribution from the yet to be launched device at this stage. Morgans is awaiting the company’s half-year results before adjusting forecasts.

Outside of daily coverage, Canaccord Genuity (target price $4.86) is the only broker to downgrade following Nanosonic’s trading update, shifting its rating to Hold from Buy.

This broker considers realisation of high-risk expectations for Coris to be a longer-term opportunity with uncertain timing. Canaccord anticipates the Coris launch could prove stronger than the launch of Nanosonics’ Trophon, and that Coris could catch up to Trophon in terms of revenue contribution within five years given the better understood infection risk with endoscopes.

Further, this broker suggests the company’s existing relationships could expedite purchasing decisions and see the device become standard of care faster than Trophon.

Citi, which is equally part of FNArena's daily monitoring (unlike Canaccord Genuity), hasn't updated recently. It's last rating was a Sell, kept in place following the release of FY22 financials in August. Citi's target price is $3.85.

Citi is also responsible for FNArena's consensus target remaining below today's share price as its target combined with Ord Minnett's and Morgans' only generates an average of $4.25.

Other brokers covering the company have equally elected not to update post the AGM.

Bell Potter upgraded to Hold earlier this month with a price target of $3.85. Wilsons stuck with Overweight in August, target $5.40. Goldman Sachs sits on Sell, with a price target of $3.40.

SMALL CAPS

Dr Boreham’s Crucible: Actinogen Medical

Actinogen Medical is a biotech with a potentially "gazillion" dollar opportunity in its Alzheimer's drug.

By Tim Boreham

ASX code: ((ACW))

Market cap: $215.7 million

Share price: 12 cents

Shares on issue: 1,797,393,817

Chief executive officer: Dr Steven Gourlay

Board: Dr Geoff Brooke (chair), Dr Gourlay, Dr George Morstyn, Malcolm McComas

Financials (September quarter 2022): revenue nil, cash outflows $3.38 million, cash balance $17.2 million, quarters of available funding: five

Identifiable major holders: Biotech Venture Fund 13.77%, Dr Steve Gourlay 3.7%, Edinburgh University Technology Fund 2.68%, Tisia Nominees (Henderson family) 1.86%, JSC Wealth Management 2.49%.

This column first appeared in Biotech Daily (biotechdaily.com.au)

Actinogen chief Dr Steve Gourlay does not demur on his assessment of the company’s lead drug Xanamem, to treat the notoriously difficult Alzheimer’s disease.

“This is probably going to be the most successful drug in the world’s history because nothing else really works in Alzheimer’s and this appears to do the trick,” he says.

Dr Gourlay’s confidence stems from the drug’s success to date in improving the cognition of patients with Alzheimer’s disease, which is forecast to be the world’s number two killer behind heart disease.

The company is about to launch its biggest clinical effort to date: a phase IIb study enrolling 330 patients with mild to moderate cognitive impairment.

Dr Gourlay rates the trial as having a 70 to 80 percent chance of success, because it uses the same patients and endpoints as a recently-completed smaller study.

But just to hedge its bets, the company is launching a smaller trial to treat cognitive impairment in major depression sufferers.

From actinomycetes to Alzheimer's

Actinogen listed in October 2007 at 50 cents apiece and initially was focused on soil-derived antibiotic-like compounds called actinomycetes (hence the Actinogen name).

Xanamem hails from Edinburgh University, which completed an early-stage trial of a predecessor drug with the $25 million backing of the Wellcome Trust charity.

Clinical development of Xanamem started in 2013.

Actinogen acquired Xanamem by purchasing Corticrine Limited, an arm of Edinburgh University, in August 2014.

Dr Bill Ketelbey joined the company as CEO in December 2014. Dr Ketelbey was involved in developing Aricept, which remains the leading Alzheimer's treatment despite being developed almost 30 years ago.

Dr Gourlay succeeded Dr Ketelbey in early 2021.

Dr Gourlay previously worked in senior roles at Genentech and then with Dr Geoff Brooke (now Actinogen chairman) at GBS Venture Partners.

Dr Gourlay returned to the US and with some "Genentech mates" and took on novel small molecule development at Principia Biopharma in San Francisco. They progressed two small molecules from pre-clinical to phase III and floated the company on the Nasdaq in 2018, before selling out to Sanofi for $US3.7 billion in 2020.

All about Xanamem

Xanamem inhibits production of cortisol, a naturally occurring stress hormone. Elevated cortisol levels are thought to be a cause of both Alzheimer's and mild cognitive impairment (which can often lead to the former).

The drug acts by inhibiting an enzyme called the 11 beta HSD1. To achieve this, any drug first must negotiate the blood-brain barrier, the organ's natural defence against foreign agents.

Dr Gourlay stresses the drug is not based on amyloid mechanisms, on which most of the other Alzheimer's drug developers have focused.

"The drug has the potential to be rapidly cognitive enhancing, improving memory in a few weeks," Dr Gourlay says.

"It is potentially disease modifying and may well be an anti-depressant as well."

So far more than 300 volunteers and patients have been treated without any safety concerns, for up to 12 weeks.

"We have seen a positive effect on attention and working memory and cognition in two independent, placebo-controlled trials in healthy, older volunteers," he says.

Actinogen also has a quiescent secondary program underway to treat Fragile X syndrome, a genetic condition resulting from the mutation of the X chromosome in new-borns.

Out of the poo after Xanadu

Actinogen's prospects looked far from upbeat in May 2019, when the results of its then key trial, Xanadu, proved a 'box office' flop in the same way as the 1980 musical of the same name (and vale Olivia Newton-John).

The company's shares lost four-fifths of their value after the results showed Xanamem worked no better than placebo, on a 185-patient sample of mild Alzheimer's sufferers.

The data from Xanadu was re-examined using a modern blood test to choose the patients with amyloid-based, 'real' Alzheimer's disease.

Strong signals of protection against cognitive decline were evidenced in these 34 patients, who had elevated levels of the biomarker phosphorylated tau, or p-Tau. P-Tau is not an Asian religion, but a protein blood biomarker indicative of Alzheimer's.

The prophylactic effect was measured by a US Food and Drug Administration-approved endpoint called the Clinical Dementia Rating Scale-Sum of Boxes (CDR-SB).

A so-called functional endpoint, CDR-SB assesses patients on six criteria and rates them on a scale of 0.5 to 3.0 ranging from questionable impairment to severe dementia.

Twice as many Xanamem-treated patients had stable or improved disease relative to placebo, meaning there was a 60 to 80 percent reduction in disease progression over 12 weeks.

Put in context, the injectable drug called Lecanemab had a 27 percent reduction in disease over 18 months. Pundits expect the FDA to approve the drug.

Alzheimer's v Dementia

"There are 500,000 people in Australia with dementia," Dr Gourlay says. "Two thirds of people with dementia have Alzheimer's, which means they have amyloid in the brain.

"But others might have Lewy body dementia, strokes, fronto-temporal dementia or strokes."

Given that, the original Xanadu trial certainly had at least one-third of patients with non-Alzheimer's dementia - and maybe even more. Those patients typically do not progress over a short period such as 12 weeks, whereas Alzheimer's sufferers do.

Dr Gourlay says the company's approach is "not data dredging, but the real deal" using a rigorous new protocol.

"One of the reasons I took the job is that I looked at the clinical results from that study in detail," he says.

"I knew the 10-milligram dose had been proved to be active and there were some sub-groups where patients really benefited. We have now proved that very clearly".

More trials, more validation

In April this year, the company reported the top-line results from a phase Ib dose ranging component of a study, called Xanamia.

There's a lot of science-y stuff in the presentation, but the digestible bottom line is that Xanamem was safe and effective for dosages at or below 10 milligrams.

The results confirmed the findings of an earlier, smaller trial called Xanahes.

Mamma Mia! It's Xanamia

The next whopper stage is the Xanamia phase IIb trial to study improvements in cognitive ability for patients with biomarker-confirmed early Alzheimer's.

The placebo-controlled study aims to sign up 330 patients over multiple countries, including Australia, with enrolment starting in early 2023.

"We are quite optimistic about enrolment because it is a simple oral drug taken once a day, not a complicated antibody infusion," Dr Gourlay says.

Describing Xanamia as a quasi-phase III trial, Dr Gourlay hopes the US Food and Drug Administration (FDA) will view it as a pivotal trial for registration purposes, although a second phase III effort would be required.

Results are expected towards the end of 2024.

Tackling the black dog

The company expects to start enrolling a 160-patient proof-of-concept depression trial within the next month or so, with results in late 2023 or early 2024.

“We didn’t want to put all the eggs in one basket and having a second indication makes the story just that much bigger,” Dr Gourlay says.

He says that while anti-depressants might improve mood, they do nothing for the “foggy thinking” of Alzheimer’s patients.

“The hope is that Xanamem might have a dual action in improving depression and cognitive impairment,” he says.

Proving efficacy with depression could pave the way for Xanamem to be used in other psychiatric conditions, such as schizophrenia.

Aduhelm underwhelms

Controversially, the FDA last year approved Biogen’s Alzheimer’s drug Aduhelm (aducanumab), which had only just entered phase I trials.

In doing so, the agency snubbed the view of its own 10-member expert committee, with three of them quitting (one of them dubbed the decision “the worst drug approval in recent history”).

Aduhelm targets the build-up of amyloid plaque in the brain after its formation.

Dr Gourlay opines that Biogen was overly ambitious charging $US56,000 for a drug with accelerated - rather than full - FDA approval.

Biogen is trying again with the aforementioned Lecanemab, which has been subject to an 1,800-patient study.

The FDA is expected to approve the treatment, which involves an antibody infusion every two weeks.

Finances and performance

Actinogen had $13 million of cash at the end of September quarter, with research and development tax incentive received in October taking the tally to around $17 million.

Cash burn will step up as the trials progress (September quarter outflows were $3.38 million).

Not surprisingly, partnerships are a source of non-dilutive funding, as are grants.

US research house Edison estimates Actinogen will burn $39 million in 2023-24 and will need $390 million to fund both clinical programs to global marketing approvals.

The company last raised equity ($12.4 million) in December last year.

Over the last year Actinogen shares have traded between four cents (mid-June this year) and 19 cents (early November last year).

Historically the shares peaked shortly after listing in October 2007, at 55 cents and plumbed to a nadir of one cent in September 2019.

Dr Boreham’s diagnosis:

Despite drug companies throwing not just the kitchen sink but the bath as well at the problem, Alzheimer’s is as intractable problem as ever.

What drugs are approved for Alzheimer's disease?

Aducanumab (as it’s generically known) is the only disease-modifying medication currently approved to treat Alzheimer's.

“Whichever way you look at it, it is a gazillion dollar opportunity,” Dr Gourlay says.

He notes that three independent trials have shown that Xanamem works. If the FDA agrees and eventually approves the drug, Actinogen will be worth many billions of dollars - even “gazillions” - rather than the current

$220 million.

While Dr Gourlay rates Xanamia as a 70 to 80 percent chance of success, he's a realist who believes there's a 50 percent chance of the drug actually getting to market.

“Some US [Alzheimer's drug developers] are worth $US2.5 billion and they don't have anywhere near the amount of data that we have,” Dr Gourlay says.

Meanwhile, Edison ascribes only a 10 percent chance of marketing success, while Bell Potter concurs that it's more a 50-50 bet. Nonetheless, Edison values Actinogen shares at 36 cents - thrice the level they're at now - while Bells plumps for a more conservative 15 cent valuation.

So, take your pick.

Disclosure: Dr Boreham is not a qualified medical practitioner and does not possess a doctorate of any sort – as far as he can remember.

SMALL CAPS

Collins Foods Hits Margin Wall

Collins Foods has not surprised with its half year result, but updated guidance suggests anticipated second half margin recovery is no longer expected.

-Results differ region to region for Collins Foods' first half
-European margins suffering from impacts of elevated labour and energy costs
-Implemented price increases aim to offset pressures, with further increases being carefully considered
-Previously anticipated second half margin recovery looks unlikely to emerge

By Danielle Austin

While Collins Foods' ((CKF)) first half results demonstrate strong ongoing demand in its Australia, Germany and Netherlands businesses, costs in Europe continue to challenge the company.

The company reported revenue growth of 15.0% across all divisions. By division, KFC Australia increased 10.6% on the previous comparable period underpinned by same store sales growth of 5.1%, while KFC Europe rose 31.9% underpinned by same store sales growth of 10.4%. Performance from Germany and the Netherlands bolstered the result, with the regions delivering same store sales growth of 14.6% and 9.2% over the half respectively.

However margins in Europe have been heavily impacted by cost pressures amid elevated wages, energy and commodity pricing. These same pressures are largely expected to impact over the coming year, with the company guiding to a group margin decline of -2-3 percentage points over FY23, remaining flat in FY24.

In the days since the release of the result, Collins Foods' share price has taken a tumble. While analysts have largely found the composition of the company's result as expected, commentary suggesting margin recovery over the coming half was more surprising, and, Morgans (Add, target price $9.50) believes, the reason for the share price decline.

The company had previously guided that margin recovery would emerge in the second half, but a reduction in full year guidance suggests Collins Foods is now not anticipating a near-term rebound. The company now guides to margins for KFC Australia of 15-16%, down from 16-17%, and for KFC Europe to decline -2-3 percentage points, from a previous -1-2 percentage points.

Better cost environment would improve outlook

Alongside Morgans, both UBS and Macquarie cover Collins Foods. While both Morgans and Macquarie are equivalent Buy-rated, UBS has opted for an equivalent Hold rating. Between them these brokers have an average target price of $8.73, with a range of $8.20 to $9.50.

Material price increases were implemented for KFC Netherlands during November, noted UBS (Neutral, target price $8.50), and for KFC Australia in September. The broker assumes the Australian business will likely require an additional price increase in December or January to offset the impact of ongoing chicken pricing renegotiations.

UBS remains constructive on Collins Foods' longer-term story, and sees potential for the cost environment to improve over FY24. The broker would like to see signs of abating cost pressures or stronger price increases to support a more positive outlook.

Macquarie (Outperform, target price $8.20) expects cost pressures will remain a headwind for Collins Foods in the near to medium term, but also anticipates consumer spending is likely to slow as the impact of rising rates hits households.

Outside of the FNArena database, Wilsons (Overweight, target price $11.49) similarly noted margin contraction was ahead of expectations, and that the revised margin guidance suggests a deeper and longer impact from cost inflation than had been previously anticipated.

Similar sentiments were made by Canaccord Genuity (Hold, target price $7.50) and Jarden (Neutral target price $8.50). The former highlighted the company remains committed to putting the customer first, and this value proposition continues to weigh on margins.

WEEKLY REPORTS

The Short Report - 01 Dec 2022

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

Summary:

By Greg Peel

Week Ending November 24, 2022.

From the sublime to the ridiculous.

Two weeks ago shorters executed such a frenzy of position shuffling one might have thought it was the last week before Christmas, although the shock low US CPI likely sparked a rethink. This week brought a similar local CPI result, but last week it all went dead quiet in Short Land.

You have to go to the bottom of the table to find any changes. No stock saw a short position increase, no stock saw a change of one percentage point or more, and the list of stocks shorted by 5% or more was cut by four.

The ASX200 ground its way quietly higher over the week.

After yesterday's stunning local CPI numbers, and last night's confirmation (basically) of a 50 point-only hike this month from the Fed chair, perhaps the action will pick up again this week amongst the shorters.

But for now, that's all folks.

Weekly short positions as a percentage of market cap:

10%+
BET 15.2
FLT 14.7
SQ2 12.5
DMP 11.4
MP1 10.4

No changes

9.0-9.9

SYA, PPT, NAN

No changes

8.0-8.9%

BRG, LKE, SBM, TPW

No changes

7.0-7.9%

ZIP

No changes

6.0-6.9%

NXT, BRN, VUL, AWC, JBH, CCX, CUV, BGL

Out: IEL

5.0-5.9%

IEL, PBH, GOR, ARB, KGN, NIC, ABB, JHG, EVN, CGC, BLD, APX, PME, BOQ, MFG, ING, CHN, PNV, PNI, ADH

In: IEL Out: JRV, RSG, ASM, PDN

Movers & Shakers

Nothing.

ASX20 Short Positions (%)

Code	Last Week	Week Before	Code	Last Week	Week Before
ALL	0.5	0.7	NAB	0.8	0.9
ANZ	0.6	0.8	NCM	0.5	0.6
BHP	0.3	0.4	RIO	0.6	0.6
CBA	1.6	1.7	STO	0.4	0.5
COL	0.3	0.3	TCL	0.9	0.9
CSL	0.5	0.6	TLS	0.2	0.3
FMG	2.2	2.2	WBC	1.7	1.9
GMG	0.9	0.8	WDS	1.5	1.8
JHX	1.1	1.2	WES	1.7	1.7
MQG	0.6	0.7	WOW	0.7	0.6

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.

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WEEKLY REPORTS

In Brief: House Prices, Banks, Equities

Weekly broker wrap: house price declines, strong bank reporting season, domestic equities outperform.

-ANZ predicts an -18% peak to trough decline in house prices over 2023
-Following a positive banking reporting season, deposit competition and mix is critical to industry outlook
-Domestic equitiy market outperforms global market year-to-date

By Danielle Austin

Domestic housing trough expected in the year ahead

Rate-driven house price declines are impending, if predictions out of ANZ Bank are to be believed (among others). Anticipating the cash rate to rise to its highest level in a decade at 3.85% in the next year, the bank believes house prices are concurrently on track to fall -18% over the coming year, ahead of a recovery in 2024.

The bank expects the cash rate will peak in May, and that the impact on house pricing will be fully evident by the end of the year. It anticipates mortgage rates will begin to fall late in 2023, driving a 5% recovery in house prices in 2024.

Since peaking in March, house prices across capital cities have already declined a combined -6%. Sydney has taken the largest fall, sliding -10%, while prices in Adelaide and Perth have remained largely resilient to date.

ANZ highlighted that reduced borrowing capacity remains the largest drag on house pricing currently. Should the cash rate reach 3.85%, the bank predicts a reduction in borrowing capacity of more than -30%. While housing finance has fallen -24% from its peak, it remains 28% above pre-covid levels.

Should ANZ’s model prove correct, it assumes a current tight rental market, rising immigration and low unemployment all help mitigate housing demand weakness. The bank does note risk that house prices fall less than expected, which it expects would drive less softening of consumer spending and subsequently an extended tightening cycle and prolonged pressure on house pricing.

Banks insulated from asset competition to benefit as rates normalise

The recent bank reporting season was one of the more positive in recent years, noted JP Morgan, but evolution of deposit competition and mix are crucial to the industry outlook.

Rate leverage saw bank net interest margins surprise to the upside across the majority of the industry, with National Bank ((NAB)) a notable exception. This drove strong half-on-half net interest income growth and positive commentary around net interest exit-margins.

Short-term, JP Morgan anticipates net interest margins for most banks will peak in the first half of the current financial year, followed by a gradual decline. If JP Morgan's assumption that the Reserve Bank will issue a further four rate hikes proves true, the broker anticipates banks that are better insulated from asset competition will to appeal to investors.

This outlook plays into JP Morgan's industry preferences, with Macquarie Group ((MQG)), National Bank and Judo Capital ((JDO)) making up the broker's top picks. These are followed by ANZ Bank ((ANZ)), Bendigo and Adelaide Bank ((BEN)), Bank of Queensland ((BOQ)) and Commonwealth Bank ((CBA)).

The broker assumes a gross loans loss rate of between -9 and -11 basis points across the majors in the first half, and between -15 and -17 basis points in the second half. JP Morgan made marginal downgrades across its banking coverage, with net profit assumptions declining -1-2% in FY23 but largely unchanged in FY24 and FY25. Excluding Commonwealth Bank, JP Morgan continues to find valuations relatively cheap.

Domestic equities outperform on a relative basis, key sectors underpin further growth

Australian equities are proving comparatively resilient to global equity movements, which Wilsons attributes to strong earnings performance and a unique sector mix. While the domestic equity market has declined -3% year-to-date, it has outperformed the global equities market which has reported a steeper -11% decline.

The broker highlighted three factors underpinning the outlook for Australian equities, firstly being performance of the information technology sector. According to Wilsons, this sector was the largest contributor to the relative outperformance of the domestic equity market against the global equity market in the last year, and will continue to be key to relative outperformance in the coming year.

Secondly is performance of the materials and bank sectors, which were also key contributors to relative outperformance in the last year. The broker expects Australian equities could be well placed to continue to perform well in the coming year should the materials and banking sectors continue to do well. As usual, the mining sector remains crucial to domestic growth, but the volatile for key commodities, particularly iron ore, remains uncertain. Wilsons describes the mining sector as a key swing factor for its outlook.

Thirdly is performance of the Australian dollar. While the broker does not predict huge upside to the Australian dollar, it does note a decent lift in the Australian dollar could impact absolute returns on global equities.

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