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Stories To Read From FNArena
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More Upside To Come For Link

Costs and depreciation marred the first half result for Link Administration, although brokers are confident that synergies for Link Asset Services should continue working in the company's favour.

-More positive outcome expected from legislative changes -Long-term upside from expansion in Link Asset Services and PEXA -Market share captured by industry funds expected to be permanent

By Eva Brocklehurst

Synergy benefits provided most of the growth for Link Administration ((LNK)) in the first half while many of the risks feared by brokers, such as Brexit, failed to score a material negative.

Admittedly, costs and depreciation were higher than Citi and many others forecast but are expected to be temporary. SuperPartners and Link Asset Services synergies should contribute more fully in the second half.

Therefore, the growth story is largely intact. Moreover, changes to super account consolidation should favour Link Administration. Citi also expects a resumption of growth in higher-margin revenue should allow margin expansion to resume in the second half.

Morgan Stanley observes the main concerns that drove a sell-off after the November AGM have eased. These include softness in project fees, which turned out to be temporary as activity rose strongly in the second quarter, and European earnings, despite the Brexit-related headwinds.

Macquarie is pleased that synergy targets of at least GBP15m have been reaffirmed for Link Asset Services and will not be revised downwards following the sale of CPCS, which had been seen as a risk. On the other hand cash flow conversion was very weak and margin trends across divisions were also soft.

Revenue was better while expenses were weaker than CLSA expected, and the improvement in revenue was related to growth in expensed funds administration. Still, the the outlook is now more complex. Issues centre on UK transaction revenue, elevated costs and the need to invest in the business.

CLSA reduces estimates for FY19 operating earnings by -2.6%, with slightly higher negative revisions in the outer years. Still, the broker, not one of the eight monitored daily on the FNArena database, is positive about the stock and retains a Buy rating and $8.50 target.

Deutsche Bank is concerned about the next three years as the business faces account consolidation and lost earnings from the sale of its UK trustee business, as well as margin pressure and downgrades to Sell from Hold as a result.

Ord Minnett goes the other way and upgrades to Accumulate from Hold. While funds administration earnings were weak, the broker notes a pick-up in revenue while a more positive outcome can be expected from legislative changes. The broker finds the current PE multiples undemanding and believes the stock should be a defensive exposure against structural change stemming from the Hayne Royal Commission.

Morgans downgrades estimates by -7-8% on a combination of lower revenue and earnings margin assumptions. The broker notes integration synergies are heavily skewed to the second half and finds the current trading multiple undemanding, not fully capturing the longer-term upside from expansion in Link Asset Services and PEXA, the online property exchange network.

PEXA

Brokers generally assess upside stemming from traction in PEXA as this business becomes a meaningful contributor to earnings. However, while PEXA is likely to make a positive contribution, Citi does not expect this until FY20, and it will be even later before the contribution become sufficient to offset funding costs. PEXA appears unaffected by the impact of the downturn in the housing market.

Credit Suisse believes Link Administration can provide 10% earnings growth over the next 3-4 years, although this may not be linear. Growth should be supported by M&A, synergies, price increases and higher growth in industry funds membership.

Still, D&A is likely to remain elevated into the future and this provides a permanent downgrade to the net profit outlook. UBS agrees with that assessment but suggests, while a step up in D&A is likely, improved revenue momentum and synergy realisation should leave the outlook relatively unchanged.

Regulatory Changes

Management has confirmed legislation for inactive accounts has been passed by the Senate. The definition for such accounts has been adjusted and this will partly reduce the revenue impact on Link Administration.

Morgan Stanley was cautious about funds administration because the business is currently over earning and the number of super accounts is likely to decline, fast tracked by the proposed reforms. However, several developments have changed the way the broker assesses the outlook and these are largely positive.

The first is the delay of 6-12 months in super reforms and the fact these have been watered down, as the definitions have been relaxed. Moreover, a shift into industry funds is afoot and Morgan Stanley believes this structural. Industry funds, historically, have been poor at retaining members that are approaching the pension phase, but have now built retirement products which compete with retail and SMSF offerings.

The Hayne RC has also triggered a mass exodus from bank and insurer-owned funds. The market share captured by industry funds should, therefore, be a permanent feature and help Link enjoy more than 3% growth in members over the medium term, in the broker's view.

The fact that the company's largest client, AustSuper, is raising its administration fee by 50% means that Morgan Stanley is more confident Link will be able to renegotiate contract terms. Other funds are expected to follow.

Credit Suisse also has become increasingly confident that Link will be able to offset any headwinds from the regulation of super account memberships. The broker believes Link Administration can provide 10% earnings growth over the next 3-4 years, although this may not be linear. Growth should be supported by M&A, synergies, price increases and higher growth in industry funds membership.

FNArena's database shows seven Buy ratings and one Sell (Deutsche Bank). The consensus target is $8.06, signalling 14.3% upside to the last share price. Targets range from $6.30 (Deutsche Bank) to $8.60 (UBS).

See also, Link Renews Focus On Core Business on February 4 2019.

Treasury Wine Increasingly Confident

Treasury Wine Estates is increasingly confident, reiterating expectations for 25% growth in FY19 earnings and guiding to a further 15-20% growth in FY20.

-Expects to increase products sourced in France -Needs to absorb double-digit lift in Penfolds inventory -Weak cash conversion disappoints brokers

By Eva Brocklehurst

Strong margins in Asia and a positive mix towards luxury wine underpin the outlook for Treasury Wine Estates ((TWE)). Guidance for FY19 earnings (EBITS) growth of 25% has been reiterated as well as the margin target of 25% over time. FY20 guidance is for earnings growth of 15-20%.

Macquarie suspects this early guidance for FY20 was provided because of market uncertainty about the low volumes in the 2017 vintage, which will be released from FY20. Further afield, FY21 risks are skewed to the upside because of the anticipated release of the high-quality 2018 vintage, while 2019 is expected to be even higher quality and higher volumes.

CLSA believes strong growth in luxury wine augurs well for future earnings. Guidance was lower than expected for FY20, although management has signalled stronger growth is more likely in FY21-22. The broker, not one of the eight monitored daily on the FNArena database, has a Buy rating and $23 target.

Considering the extended growth phase, and reviewing PE history, Credit Suisse is confident the company can reach its growth targets, upgrading to Outperform from Neutral.

Yet Morgan Stanley questions whether earnings growth can really re-accelerate in FY21, suspecting it more likely that longer-term earnings growth slows. While inventory of luxury wines is rising the broker believes customer demand is more relevant to the earnings outlook. Profit growth is likely to remain strong but, in the absence of M&A, the broker struggles to envisage any acceleration.

The company is expecting to grow product sourced in France from the original Maison de Grand Esprit as well as Beaulieu Vineyard and Penfolds. Treasury Wine has indicated that demand for Beaulieu Vineyards has been exceptionally strong, and intends to acquire two small wineries in France as well as a number of premium brands and increase productivity with its own throughput.

The company has confirmed demand for Penfolds remain strong and sourcing will be extended to France and the US as well. Treasury Wine is keen to walk away from commercial volumes in Asia in an effort to optimise its mix.

China

The company's business represents around 8% of imported value share in China and expansion in distribution of more than 50% is forecast over the next three years. UBS believes the market has underestimated the growth and potential penetration in China.

Credit Suisse, in acknowledging the need to absorb the double-digit lift in supply of Penfolds luxury wine, remains confident that, as expansion in China deepens, plenty of growth is on offer. Morgans also points to the significant opportunity to grow the market share by increasing breadth and depth of distribution in China.

Cash Conversion

The one area that disappointed brokers was the weak cash conversion. The company has pointed to the timing of sales in Asia and the US and unfavourable FX translation of US working capital balances as the cause.

Also, Asian earnings margins have moderated as Treasury Wine invests in new brands. American margins declined to 18.5% in the first half while European EBITS margins were flat and affected by short-term pricing pressure.

While acknowledging the reasons behind the weak cash conversion, Morgan Stanley is becoming concerned that the company is stretching its key brands and potentially leaving them exposed. UBS also suggests, while comfortable with the company's explanation, achieving cash conversion of 60-70% in FY19 will be a challenge

Goldman Sachs was disappointed with the cash flow, and the fact net debt increased materially. Has the share price run ahead of fundamentals? Goldman Sachs, not one of the eight monitored daily on the database, believes the valuation is not aligned with execution risks.

Moreover, the sustainability of working capital, the ability to fund dividends and investments out of cash flow, as well as the reliance on new brands are items of concern. Hence, there is not enough in the result to underpin the elevated valuation, and the broker downgrades to Sell from Neutral, with a target of $13.70.

Citi agrees with this assessment, calculating Treasury Wine is 20% more expensive on a free cash flow yield basis versus peers, underscoring its Sell rating.

Americas

UBS questions the size of the US opportunity, suspecting upside is not being priced into the stock from the company's change in its route to market. Around 40% of distribution has changed so far. Transition costs associated with the change are expected to ease in the second half and support improved margins.

Hence, UBS believes the change in route to market could capture a 180-425 basis points margin opportunity in the Americas. The company is also open to acquisitions in the US, at the right price.

Credit Suisse believes North America should provide much more to growth in FY20, as one-off transition costs related to the new distribution model drop away. The company is also hopeful that a 19 Crimes whiskey could add material earnings benefit. Moreover, the broker notes the US business has a high-margin direct-to-consumer channel which responds well to great vintages, such as the one in 2018.

There are four Buy ratings, three Hold and one Sell (Citi) on the database. The consensus target is $17.74, suggesting 12.4% upside to the last share price. Targets range from $14.90 (Citi) to $19.85 (Credit Suisse).

Whitehaven Coal Marked For Capital Returns

Higher expenditure and lower production cast a shadow over Whitehaven Coal's first half result. Yet, brokers observe the market is likely to set this aside amid the potential for capital returns.

-Rise in coal volumes and firm prices likely to offset increased costs -Narrabri needs to demonstrate it can overcome the challenges -Plans to sell more coking coal from Maules Creek

By Eva Brocklehurst

Whitehaven Coal ((WHC)) surprised brokers, as cash was run down over the first half to a larger-than-expected extent. Higher expenditure on exploration had not been flagged in the lead-up to the interim results. A combination of more money being spent on exploration, plant and higher receivables meant a much lower level of free cash flow. Cash flow was around -$100m below UBS estimates.

A downgrade to production is coupled with an increase in cost guidance and, ultimately, increased capital expenditure. Deutsche Bank notes each factor is small in isolation but has cumulatively dented short-term confidence, given a significant shareholder return was also absent. The company paid an interim dividend of $0.15 a share and a special dividend of $0.05 a share.

Market interest in capital management should now rebuild, Morgans believes, as the board has form in skewing the dividend to the second half as it seeks greater certainty around capital movements.

Citi forecasts an ordinary dividend at a 50% pay-out plus a special dividend of $0.10 per half in the second half and through FY20. Thereafter, capital expenditure for Vickery is expected to ramp up and, hence, special dividends will be deferred. On this basis, the broker estimates Whitehaven Coal will offer an aggregate dividend of $0.46 a share in FY20.

Costs have risen by around $13/t since the first half of FY18, the vast majority being structural, although Macquarie suspects some relief is likely as volumes rise again in the second half.

Narrabri

The company has again downgraded expectations for Narrabri. The downgraded guidance and $35m in capital expenditure to upgrade the chocks makes Morgans question the long-term production and cost profile of the mine. Several other brokers agree there needs to be a couple of trouble-free quarters of output at Narrabri to allay concerns. Narrabri comprises 21% of Morgans' valuation by operating assets.

Macquarie suggests, as the final stage of the longwall 108 is being left out to avoid the volcanic intrusion, there will, ultimately, be a benefit to earnings. Still, this is the third year in a row the company has cut production estimates for Narrabri, although an expected lift in FY20 could be an offset.

However, Deutsche Bank observes the option to buy an additional 7.5%, dependent on the Narrabri South exploration process, looks less likely to proceed in 2019.

The slump in the share price the wake of the results reflects continued issues at Narrabri, Credit Suisse asserts, and the next 18 months will be critical in order to demonstrate that Narrabri can navigate the challenges. Still, the company has delivered $800m in returns to shareholders over the past 18 months and, with no material expenditure required until Vickery commences, this is likely to feature.

Vickery

A formal process to sell down a stake to offtake customers at Vickery is to be launched in the next 12 months as the company envisages owning just 80% of the project. Deutsche Bank assesses the market is attributing nothing to Vickery or the Winchester South expansion. The plans for the Vickery have been pushed out to FY21 and the company has highlighted a likely legal challenge to the mine.

A statement of intent is expected in the near term for Winchester South and an initial reserve statement is expected in August. Deutsche Bank includes Winchester South in its valuation, at a 50% risk weight or $0.20 a share. In regard to Winchester South, Bell Potter expects the company will increase its value leverage to metallurgical coals, a positive factor.

Maules Creek

The company is developing a new product strategy for Maules Creek, a return to the previous owner's 50% semi-soft metallurgical (coking) coal target, which will result in lower volumes and yields, and higher costs. The offset is the higher margins that should be forthcoming. The run rate of 13mtpa is still on track for the end of FY19 and Credit Suisse assumes an 88% yield.

Deutsche Bank notes the rise in unit costs at Maules Creek is based on the strategy to sell more coking coal, which requires washing. There is also a temporary increase in costs because of greater haul distances at Maules Creek, which will cease when in-pit dumping commences.

Management expects coal demand will remain strong and, even with the downgrades from the loss of tonnage and higher costs, higher prices will offset most of the losses.

Morgans suspects the best margins are behind the business, as costs are creeping higher and Whitehaven Coal's operating reputation has taken a knock. Still, the stock appears cheap and, with a capital management story still intact, the broker maintains an Add rating.

Bell Potter believes the market has over-reacted, noting the strong balance sheet and a production growth profile which should support shareholder returns. The broker, not one of the eight monitored daily on the FNArena database, has a Buy rating and $6.20 target, believing its recommendation is also supported by the strong outlook for seaborne coal prices.

CLSA, also not one of the eight, is a little more concerned about the outlook. The broker notes price realisations were mixed in the half-year, with thermal coal surprisingly weak because of low caloric value sales.

In any other market the broker envisages the stock would have been sold off more, but with thermal coal pricing above US$110/t the market is shrugging off the latest figures because of the attractive free cash flow yield and capital return upside. CLSA has an Outperform rating and $5.80 target.

The database shows seven Buy ratings and one Hold (Macquarie) for Whitehaven Coal. The consensus target is $5.21, suggesting 16.6% upside to the last share price. The dividend yield on FY19 and FY20 forecasts is 9.3% and 6.9% respectively.

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Is Cochlear Too Expensive?

Cochlear's services and upgrade business is expected to feature over the rest of the year, until the company reasserts its leadership in product innovation and new implant growth gets back on track.

-Pressure on Cochlear to develop its own MRI-compatible implant -Brokers suggests risks are not properly reflected in the share price -Flat implant unit sales expected to materialise again in the second half

By Eva Brocklehurst

Cochlear Ltd ((COH)) has hit a speed bump, sustaining market share losses in the US and confronting funding caps and reimbursement issues in Western Europe. While implant unit growth stalled in developed markets in the first half, the services business was robust and featured demand for N7 processor upgrades.

Competitor, Advanced Bionics, has surprised the market by taking market share in new implants with its MRI-compatible offering. The dramatic slowdown in Cochlear's unit sales in the last months of 2018, signals to brokers that market share will erode until the company can provide an MRI-compatible unit of its own.

Morgan Stanley notes the Advanced Bionics Ultra 3D implant was not launched until September 2018 and, therefore, expects unit growth for Cochlear will deteriorate further as market share losses persist. Still, the broker has seen market share vary on the back of product cycles before, pointing out the company benefited recently from being the first to market smart phone compatible products.

It is not clear whether Cochlear has a competitive solution as yet, which reminds Wilsons that the market leader sometimes gets caught napping. The broker observes the Sycle business has made a slow start but its technological solutions should play a role in standardising and implementing candidate criteria. Wilsons, not one of the eight stockbrokers monitored daily on the FNArena database, downgrades to Hold, with a target of $188.

CLSA points out it may take six months to develop a competitive product and a further six months to obtain approvals. As a result, the broker has reduced implant volume growth forecasts to 3.7% from 6.2%. This is somewhat offset by increased growth expectations for upgrades and accessories. CLSA, also not one of the eight, understands the business is investing for growth but considers the stock expensive. An Underperform rating and $176.65 target are maintained.

Cochlear faces a tough year but Ord Minnett expects the setback will prove temporary, as the company is almost certain to respond with a new offering by early 2020. The broker is confident MRI compatibility will be offered with the next implant as functionality is well-established.

However, such developments cannot be rushed and Ord Minnett suspects the benefits will not be realised until FY21. The broker is reminded of the risk inherent in the business and believes this is not appropriately reflected in the current share price. While earnings growth is likely to be maintained, declining unit sales and uncertainty over the IP legal case could test investor nerves.

Services

Services revenue was up 28%, with a strong uptake of the recently-launched N7 sound processor. The company has indicated this uptake is in line with the previous generation processor.

Morgans expects services will do the heavy lifting for FY19 and, as it is early in the N7 upgrade cycle, strong growth is likely. The broker acknowledges investors will question the company's competitiveness and R&D leadership, and there are risks to the downside as growth in the installed base stagnates.

Outlook

Citi found a lot to like about the results, although downgrades to Neutral from Buy. Specifically, implant sales in emerging markets increased by over 15%. Citi assumes no implant volume growth in the Americas in the second half but expects market share growth will return.

The broker considers the long-term investment thesis positive, as the company has a leading position in a growing market which has high barriers to entry. Still, near-term valuation upside is limited. The company has maintained FY19 net profit guidance of $265-275m and expects to maintain net margins by adapting investment to revenue growth.

Credit Suisse drops its rating a notch as well, to Underperform. The broker believes the next 6-12 months will be challenging and market share losses will be amplified in the second half and into FY20. Flat implant unit sales are expected to materialise again in the second half, as the company cycles a strong comparable period.

Unit sales growth is then forecast to recover to 6% in FY20. In such an environment, the broker believes the stock is overvalued, as Cochlear trades at a 36% premium to its global medical device peers on an enterprise value/EBITDA basis.

Macquarie agrees the valuation is elevated, noting the stock also lacks appeal on a PE/growth basis relative to domestic healthcare stocks. Investment in sales and marketing and R&D should be supportive in the longer term but the current share price implies growth rates ahead of base case forecasts.

The company has increased expenditure on its manufacturing facility in China, to $36m, and this is expected to be completed by the end of FY20. The company has also made an investment in Nyxoah, the medical device business which is developing a hypoglossal nerve stimulation therapy for the treatment of obstructive sleep apnoea.

FNArena's database shows four Hold ratings and four Sell. The consensus target is $168.11, signalling -4.8% downside to the last share price. Targets range from $155 (Ord Minnett) to $190 (Citi).

Material Matters: Steel, Coking Coal And Copper

A glance through the latest expert views and predictions about commodities. Better market conditions for steel and scrap, but price rises for cobalt and nickel are questioned, while copper looks poised.

-Traders and China stimulate demand for steel and scrap -Coking coal and nickel increases likely to be short-lived -Copper set to rise, but cobalt softens as supply increases -Increase in light oils limits potential for Brent rise

By Nicki Bourlioufas

Steel and scrap find support from traders and China

Prices for steel and scrap have improved after a decline at the end of 2018 and Morgan Stanley predicts the stronger market will continue in the first half of 2019. Morgan Stanley analysts expect steep prices will be supported by trader restocking and improved sentiment due to Chinese stimulus measures, but say uncertainty around trade tariffs make the second half unpredictable. The analysts also suggest scrap prices have bottomed, with the next move likely to be up.

The price for US hot rolled coil (HRC) steel has declined by -26% since it reached a spot price of US$1,015 per tonne in July 2018. In January 2019, the US HRC spot price was US$750/t. The East Asia HRC price has fallen -20% since reaching a spot price of US$624/t in March 2018. The price touched a low of US$484/t in early January 2018, but recovered by a modest 4% to reach a spot price of US$505/t this month.

Morgan Stanley expects scrap prices to trade in a range of US$300-US$350/t in the short term. The analysts are encouraged by recent Turkish restocking on top of the iron ore price rise. The combination of the two, they believe, is likely to provide a short-term boost to scrap collections and prices.

Morgan Stanley has retained its overweight rating on BlueScope Steel ((BSL)), though its price target has been lowered to $19.50. While steel prices have declined from the peak experienced in 2018, the analysts believe there is upside to prices in the shorter term, though rising iron ore prices may place pressure on BlueScope Steel's Australasian operations short term. Longer term they continue to hold the view the industry remains attractive.

Morgan Stanley has retained an overweight recommendation on Sims Metal Management ((SGM)) with its price target raised to $12.50. “We continue to believe in the long-term structural shifts that surround the environment SGM operates in. While scrap prices declined during the end of CY18, recent green shoots in key scrap price indices are encouraging. We believe that favourable short- and long-term dynamics are not reflected in the current SGM share price.”

Coking coal and nickel make shaky gains

Two key inputs to steel production, coking coal and nickel, are rising, but Macquarie Wealth Management analysts have doubts over whether the increases can be sustained. Macquarie notes tha, after falling -15% at the end of 2018, the spot price for top-grade hard coking coal has recovered to more than A$200/t Free On Board (FOB). The catalyst for the improvement is supply disruptions in Queensland after heavy rains forced the closure of the Abbot Point terminal at the beginning of February.

But the Macquarie team says the improvement is likely to be temporary. The analysts point to the global correction in steel margins and the end of the dispute between rail freight operator Aurizon Holdings ((AZJ)) and the Queensland Competition Authority. The resolution should pave the way to a recovery in Australian supply this year, suggest the analysts.

Nickel has risen 18% in 2019 to US$12,735/t, partly due to speculation of reduced supply from Vale, the world’s leading producer of the metal. Morgan Stanley says the dam disaster at Vale’s Brazilian iron ore mine has heightened concern about the company’s Onca Puma nickel mine in the Amazon basin, which was suspended last year on November 18 on environmental concerns.

Investors are also worried that the disasters may have implications for the wider Brazilian nickel industry, and they have doubts over whether Vale can fulfill its long-term plan to raise its global nickel output to 400kt/year from 244kt/year.

Morgan Stanley says demand for stainless steel is still sluggish. The analysts predict a modest, seasonal pick-up in stainless orders is unlikely to be sufficient to offer long term support for the price of nickel.

Copper rises in tight market, but cobalt is in generous supply

Prices for most base and precious metals are likely to fall slightly, and bulk materials could slide by nearly -20% by the end of 2019, Morgan Stanley says. A notable exception is copper, for which it predicts a price of US$3.12/lb by the end of the year, or “14% upside from spot”.

This will emerge as China’s demand improves, combined with low visible inventories. The copper market is so finely balanced that a rise in demand of “anything above 0%” is sufficient to jolt it into outright deficit, on the analysts' assessment.

The recent spike in the cobalt price has collapsed as the market failed to absorb the increased output by mines in the Democratic Republic of Congo (DRC), Macquarie analysts point out.

The 16-month rally to US$44/lb from US$12/lb was driven by demand from makers of electro voltaic batteries and by the perennial view that “cobalt is a vanishingly scarce resource, mainly found in one challenged central African country”.

But this view has turned out to be something of a misconception. The DRC remains a tough place to operate, but the mega-mines have increased output in response to the price spike. New Chinese and Indian processors that use a range of raw materials have also contributed to the oversupply.

Global shift to light oil limits upside for Brent crude

Morgan Stanley notes OPEC reduced exports in January sharply, bringing the physical oil market into equilibrium, but a shift in the global production slate towards light oil puts a ceiling on Brent and West Texas Intermediate (WTI). Light crudes naturally yield more gasoline and, together with relatively modest growth in demand, this has driven gasoline stocks sharply higher.

Brent futures rose 15% in January - the strongest start in the 31-year history of the Brent contract. But Morgan Stanley predicts Brent will rise only modestly to US$65/b in the second half, although one factor that could drive it higher is the possibility of lower production in Venezuela given US sanctions against oil exports from that country.

Recession Watch: Is Gold Really A Safe Hedge?

By Ole Hansen, Head of Commodity Strategy, Saxo Bank

Applying hedges during periods of economic stagnation or decline can best be compared to taking out an insurance policy to offset, or more likely, to try and mitigate adverse market movements in riskier assets such as stocks, corporate credit and real estate.

Hedging does not come without risks as both the choice of product and timing of when the trade is entered will have a major impact on its potential success.

A good hedge is finding an asset where correlations to other asset classes decreases during recessions. Studies have found that gold's correlation with stocks breaks down during recessions. This means that historically, gold will often move in the opposite direction of stocks during periods of recession. However, the mere fact that the economy enters a recession doesn't necessarily lift the price of gold. It also depends on the behaviour of other markets.

However, in general one can say that during a recession interest rates typically go down while stocks are being hurt by a decline in earnings as consumers' fear of losing their jobs prompts them to save money instead of spending it. While both are likely to provide support, the risk aversion associated with an economic slowdown may trigger a need from investors to reduce exposure across the board. On that basis, an already elevated speculative involvement by hedge funds could trigger selling of gold, purely from the need to reduce exposure.

There have been seven recessions since 1965 and during these periods gold rose during five while only suffering a noticeable decline in one.

One key consideration for gold in the event of a coming recession is the likely policy response, which at the margin almost must prove supportive of the nominal price of the yellow metal. If we look back at the post-global financial crisis response and the US Federal Reserve's multiple iterations of quantitative easing, it is clear that gold rallied whenever it became obvious that the Fed was set to ease policy again – most famously when Fed Chairman Ben Bernanke tipped the markets off that QE2 was on its way in August of 2010 at the Fed's Jackson Hole symposium.

Gold rallied in the ensuing weeks to new highs above $1,265/oz and ran up to its all-time high in USD terms in late 2011. Subsequently, gold slowly began to change its behaviour as the market realised that central bank policy was not bringing the kind of inflation that gold bulls anticipated. By early 2012, the USD was turning around, and the top in gold versus the euro was posted in late 2012 and against the yen in April of 2013, the very week that the Bank of Japan's Kuroda launched his "big bazooka" of quantitative easing.

But that doesn't mean gold is permanently down for the count or that policymakers can't engineer inflation if they really want to. Consider that if the world is indeed going into a new recession now it will be doing so with record levels of debt and at low – and even in some cases – negative interest rates.

With so little policy room to work with and having demonstrated that the "old unconventional" tools of QE and ZIRP [zero interest rate policy] and NIRP [negative interest rate policy] don't work, policymakers will inevitably reach for something new. That something new is likely to include something along the lines of nominal GDP targeting and fiscal forcing of the economy, measures that could prove far more inflationary if the focus is injecting money into the economy that will be spent rather than used to inflate asset prices, which was the chief result from QE and low rates.

In this kind of fiscal forcing or debt monetisation scenario aimed at bringing down the economy's leverage while keeping unemployment low, gold could quickly play its role as something that retains its value relative to other assets. Certainly, the risks given the likely eventual policy response look asymmetric to the upside.

ESG Focus: SASB Takes On The World In 2019

International companies are increasingly adopting industry-specific sustainability accounting standards. This will be a bonus for some companies, but a ball-and-chain for others.

-World's first industry-specific sustainability accounting standards were approved on October 16 -Regulatory requirements and threat of legal action could force listed companies into quick adoption -Financial regulators internationally are not on board as yet -Early adopters include GM, Merck, Nike, Kellogg's, CBRE, and Diageo Groupe

By Sarah Mills

The year 2018 proved a quiet watershed for industries and financial markets. On October 16, the Sustainability Accounting Standards Board (SASB) voted to approve the world's first industry-specific sustainability accounting standards.

This event hardly sounds earthmoving but the repercussions are already rippling through the world: a quiet de-rating of some industry sectors is under way; surveys show chairmen of top corporations are spending more than half their time determining how to incorporate the SASB standards into their companies' annual reports; and investment advisers are actively spruiking ESG options for clients' portfolios.

It has been an extraordinarily ambitious project, led by some of the world's financial heavyweights, and which involved more than six years of research and consultation with the world's leaders of business and industry.

Of course, the accountancy initiative has its detractors, and reporting seasons in 2019 will prove the first test of its success.

SASB, The New Accountancy Framework

For the past several years, ESG (environmental, social and governance) investing had been gaining momentum, but apart from exclusionary investing – which usually targeted the sin stocks: alcohol, weapons, pornography, tobacco and gambling – few industries were caught in the net.

The SASB is determined to change that. Guided by the Standards Advisory Group, comprising global industry leaders, the SASB developed sustainability standards for 77 industries – those standards that have financial materiality to the company.

The SASB has published reporting standards for non-renewables, health care, financials, technology and communications, transportation, automobiles, auto parts, car rental and leasing, airlines, air freight and logistics, marine transportation, rail transportation, mining, coal, pharmaceuticals, road transportation, and more.

The SASB framework is divided into five categories, which the SASB refers to as "dimensions": environment, social capital, human capital, business model and innovation, and leadership and governance.

These dimensions cover issues ranging from health-and-safety, to the industry's environmental footprint, and bribery and corruption.

For example, the pharmaceuticals industry standards include reporting on: access to medicines; drug safety and side effects; safety of clinical trial participants; affordability and fair pricing; ethical marketing; employee recruitment; development and retention; employee health and safety; counterfeit drugs; energy water and waste efficiency; corruption and bribery; and manufacturing and supply-chain quality management.

The logic behind the approach is that companies in industries share the same materiality issues. The SASB has listed these issues for each industry and identified standard metrics for reporting on each, which, by default, obliges corporations to report on them in the US 10K filing form (the annual report without the bells and whistles), the 10Q form (quarterly report) and the 20K form (for foreign organisations).

SASB: Not Mandated, But Mandatory

The beauty of the SASB industry approach is that once the genie is out of the bag, all corporations in all nations with disclosure laws will to some extent be obliged to report on sustainability standards. That encompasses most of the western world, including Australia.

While not mandated by regulators, the SASB standards have the power to prove just as binding, given they are bound by the same disclosure laws governing US securities.

Rule 405 of the US Securities Act and Sections of the Sarbanes Oxley Act, requires disclosure of any information that could have a material quantitative impact on a company's bottom line – an increase or decrease of 5% being the rule of thumb.

The company's board and management must sign certification that the information is accurate and complete and not misleading. Failure to report on the sustainability standards could have serious repercussions.

Not only will investors favour complying corporations; a failure to disclose information that results in a financial loss to shareholders could open the door to investor lawsuits and give enforcers cause to issue sanctions and fines, suspend trading in company stock; and lay criminal charges.

"Could" is the crucial term.

The proof will be in the pudding. Also, it is important to note that under US law, regulatory filings do not require the disclosure of all material information – leaving some discretion and flexibility to companies.

SASB: Regulators Not On Board (Yet)

US companies have, to date, shown resistance to any type of disclosure in ESG regulatory filings. However, it is likely that those backing the SASB, with their substantial financial weight, will be active in prosecuting their agenda and testing their power in the courts.

The SASB is not a governmental body. It is a philanthropic organisation led by international heavyweights and, while its standards have no legal mandate, its industry credentials and ingenious plan have helped it gain strong momentum over the past six years.

Even if its standards do not become "legal" requirements, widespread voluntary acceptance or use within the marketplace could render the SASB standards as functionally obligatory for many companies.

However, regulators have equally proven resistant to the SASB and other non-regulatory bodies that appear to be stepping on their turf.

The US Securities Exchange Commissioner has distanced itself from the SASB standards, saying: "the Commission does not and should not delegate to outside, non-governmental bodies the responsibility for setting disclosure requirements" and that "groups like SASB have no role in the establishment of mandated disclosure requirements."

Just prior to the SASB announcement, ASIC in Australia released a report on climate risk disclosure, recommending that corporations report on risks, but has managed to avoid any mention of SASB in its reports.

For now though, it's a softly, softly approach, based on the premises of co-operation and opportunity. For example, there is a growing international consensus that coal and single-use plastics are public enemies No 1 and 2, and the standards provide a means of grappling with the problem.

Also, the SASB has done much of the thinking around sustainability reporting, saving corporations and industries, which have already made some clumsy and widely differing attempts, the effort. It provides both consistency and global relevance. So for many corporations and investors, it is a gift; for others, it is a ball and chain.

SASB: Early Adoption Is Spreading

At its launch, the SASB said the publication of the standards ushered in a new era for global capital markets in which businesses can better identify and communicate significant opportunities for sustaining long-term value creation.

National Australia Bank, for example, found that 80% of one Chinese company's facilities were located in areas of high water stress and scarcity, and after incorporating it into its valuation model, discounted the share price target by 20%.

Indeed, the standards were well aired and many major corporations have been using the development process to gain a competitive advantage. As far back as 2013, a KPMG survey of the largest companies in 41 countries found that 71% reported on areas of corporate responsibility but reporting varied widely in content, format and detail.

Europe issued a directive in 2014 that corporations with more than 400 employees must also report on non-financial disclosure for sustainability in their reports. In 2017, more than 7,000 European companies reported on environmental, social and employee-related, human rights, anti-corruption and bribery matters.

Closer to home in Australia, the Australian Council of Superannuation Investors and the Financial Services Council have jointly published an ESG Reporting Guide for Australian Companies for several years.

All eyes will be peeled to estimate the degree of changes in annual reports for the FY19 reporting season.

The degree of adoption of SASB metrics by the end of the year will be a gauge of its success. Companies such as GM, Merck, Nike, Kellogg’s, JetBlue, CBRE, Diageo Groupe PSA, Schneider Electric, Host Hotels and NRG Energy have already started using the SASB standards.

But they will be the exception rather than the rule. There is not much point reporting on ESG standards if a company has no way of measuring them internally, and it would take at least a year for many corporations to adapt.

Internationally, a keen eye will be peeled to reports from industries with high greenhouse gas emissions and plastics producers, given coal and single-use plastics have weak ESG profiles.

However, all industries have an exposure to emissions emitters and plastics; so all will have to make adjustments through their supply chains. These changes will take many companies years to implement.

Resource-intensive industries such as materials are highly exposed; and industries such as energy and beverages face risks driven by changes in the availability of resources.

Companies in industries that rely on complex global supply chains such as IT manufacturing, auto manufacturing and pharmaceuticals can be affected by extreme weather events anywhere along their supply chain as well as their facilities location. They will also feel the brunt of social investing based on working conditions in their supply chains.

Financiers will need to be more careful about which projects they finance; construction companies will face rising costs; and miners will have to demonstrate state-of-the art water, energy and labour management.

And let’s not mention the sextet of sin: tobacco, alcohol, weapons, gambling, pornography and nuclear energy. Not only will these sectors suffer from exclusion investing but equally from tighter regulations and taxes.

On the flipside, industries and companies that support a circular economy (recycling) will be favoured, and great opportunity exists for innovation that supports a circular economy.

SASB: In Focus

Over the next six months, FNArena will be examining the likely impact of SASB industry reporting standards on Australian companies. Key industries for the Australian economy will include coal, mining, transport and financial services but all industries are likely to feel the impact of the standards at some stage.

For more details, it is possible to download any of the 77 industry-specific standards from the SASB website.

https://materiality.sasb.org/

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 February 11 to Friday February 15, 2019 Total Upgrades: 10 Total Downgrades: 36 Net Ratings Breakdown: Buy 44.60%; Hold 41.17%; Sell 14.23%

Macro and global sentiment continue to support equities, but the local reporting season keeps injecting lots of volatility into the Australian share market as the calendar morphs into the final two weeks of what will yet become a deluge in corporate report releases.

Stockbroking analysts continue to issue more downgrades than upgrades in ratings for individual, ASX-listed entities. The week ending Friday, 15th February 2019 was certainly no exception.

For the eight stockbrokers monitored daily, FNArena counted 36 downgrades for the week, only offset by ten upgrades.

Among those ten, only six moved up to a Buy, including results reporters Aurizon Holdings (2x), Bapcor, Breville, Goodman Group, and Treasury Wine Estates.

There is a lot more to observe in terms of individual stocks and changes in ratings on the flipside of the week's ledger; AMP received two more downgrades, Bendigo and Adelaide Bank accumulated three downgrades, Breville Group combined the one upgrade with two downgrades, Cleanaway Waste Management also received three downgrades, as did Magellan Financial Group, while beaten down Pact Group's sixth profit warning since 2017 was good for yet another two downgrades. Treasury Wine Estates received two downgrades post financial report.

Downgrades reflected a mix of poor results and solid results prompting over-excited share price responses.

All in all, 13 of the 36 downgrades (50%) moved to Sell, including all three downgrades for Bendalaide Bank as well as both downgrades for Pact Group, with Class, Challenger, Newcrest Mining, Stockland and Virgin Australia among those to receive fresh Sell ratings.

In terms of all eight stockbrokers combined, Sell ratings still only represent a little more than 14% of all ratings, while total Buy ratings (44.60%) continue to outnumber total Neutral/Hold ratings (41.17%). Traditionally, when Buy ratings are this far ahead of Neutral/Holds it signals a rather rough time for the share market.

This time around, the signal (if there is one) is more difficult to read as five months of relentless selling in late 2018 have been swiftly followed up by two months of swift recovery. Many a shorter-term focused expert is now calling for a "cooling off" period, at the least, but it remains to be seen whether equity markets are paying attention.

One observation stands, however, and that is this reporting season already is proving incredibly tough to read in terms of share price movements post results releases. More about this in this week's Weekly Insights.

This week's table for positive amendments to valuations and price targets reads like an assembly of companies whose corporate results surprised to the upside, with IDP Education wearing the week's crown (up 35%), followed by Goodman Group (up 15.4%) and Magellan Financial Group (up 15%), followed by Cleanaway Waste Management, Telstra, Tassal Group, and Northern Star.

Challenger tops the week's table for negative adjustments to consensus price target, followed by Unibail-Rodamco-Westfield, Virgin Australia, Bendalaide Bank, Pact Group, and Bapcor.

The table for positive revisions to earnings estimates equally reveals large adjustments, with AGL Energy on top for the week, followed by GBST Holdings, Beach Energy, Goodman Group, South32, and others.

On the flipside, we find Virgin Australia, Aveo Group, Coronado Global Resources, Superloop, Carsales, and others.

Local reporting season genuinely moves into a (much) higher gear this week. If the first two weeks are anything to go by, investors should expect more fireworks, and other types of explosions.

Upgrade

AURIZON HOLDINGS LIMITED ((AZJ)) Upgrade to Equal-weight from Underweight by Morgan Stanley and Upgrade to Neutral from Sell by Citi .B/H/S: 1/6/1

As regulatory uncertainty recedes Morgan Stanley suspects the focus will now shift to the company's legal and capital structure. The broker envisages a modest upside risk from re-basing earnings.

The company appears to have accepted the UT5 final decision and the broker expects FY19 consensus earnings estimates will be downgraded and, instead, FY20 and FY21 will be upgraded.

Morgan Stanley upgrades to Equal-weight from Underweight and raises the target to $4.50 from $4.35. Industry view: Cautious.

First half results revealed a decline in earnings from continuing operations of -16%. Citi forecasts underlying EBIT for the non-network business towards the mid point of management's guidance range of $390-430m.

Citi revises FY19 estimates to reflect the fact Aurizon has chosen to account for the implementation of the UT5 decision in FY19, rather than extend the regulatory uncertainty further. The broker expects an 18% lift in underlying EBIT in FY20.

As a result of the clearer outlook for the network earnings, the broker lifts its rating to Neutral from Sell and raises the target to $4.40 from $3.80.

See also AZJ downgrade.

BAPCOR LIMITED ((BAP)) Upgrade to Add from Hold by Morgans .B/H/S: 4/0/0

Bapcorp's first-half result met the broker. A slowing in trading momentum in the second quarter was cushioned by divisional margin expansion.

Management has revised down guidance to the low end of previous guidance and the broker believes the stock can meet that comfortably, noting fundamentals are firm and expects trading challenges will be temporary.

Broker upgrades to Add from Hold but reduces the target price to $6.54 from $6.90.

BREVILLE GROUP LIMITED ((BRG)) Upgrade to Neutral from Sell by UBS .B/H/S: 1/2/1

First half results were ahead of expectations. UBS notes slower growth in North America was far from weak, still delivering 7.1%, and fears around Australian trading were not realised.

While cash flow was soft, the broker notes working capital is being built up in the UK, the US and Europe.

UBS upgrades to Neutral from Sell, believing there are years of growth ahead in Europe. Target is raised to $14.30 from $11.20.

See also BRG downgrade.

CHARTER HALL LONG WALE REIT ((CLW)) Upgrade to Hold from Lighten by Ord Minnett .B/H/S: 0/2/1

First half results were ahead of estimates.The company has extended its lease to Inghams for the portfolio of chicken processing facilities to 25 years from 16 years.

Ord Minnett estimates the asset's capitalisation rate should firm to 6.5% from 7.25% on acquisition. This adds $0.07 to the net tangible assets per security and increases the weighted average lease expiry.

As a result, Ord Minnett raises the rating to Hold from Lighten and the target to $4.25 from $4.10.

GOODMAN GROUP ((GMG)) Upgrade to Outperform from Neutral by Credit Suisse .B/H/S: 3/2/1

First half results were in line with expectations while guidance has beaten Credit Suisse forecasts. The level of demand for industrial assets remains strong, supported by revaluations, investment and development activity.

The company will reduce its pay-out ratio to the low 50% range in order to sustain higher development work-in-progress in the near term.

The broker expects market conditions to remain positive and upgrades to Outperform from Neutral. Target is raised to $13.22 from $10.84.

LENDLEASE GROUP ((LLC)) Upgrade to Buy from Neutral by UBS .B/H/S: 5/0/0

UBS upgrades Lend Lease to Buy from Neutral, believing the stock to be undervalued given risks have fallen on troublesome projects. It also notes the company is not reliant on Australian residential markets given its global profile and institutional capital partners for all asset classes.

UBS expects an announcement regarding the engineering business when the interim results are published on Friday.

Target price rises to $15.70 from $15.20.

NORTHERN STAR RESOURCES LTD ((NST)) Upgrade to Accumulate from Hold by Ord Minnett .B/H/S: 2/2/3

Ord Minnett believes the market concern around grades is not a major issue and Kalgoorlie operations should reach FY19 guidance. Moreover, medium-term production opportunities could push Kalgoorlie towards 400,000 ounces of gold per annum.

The broker also notes the recent update on Pogo, with December quarter mining rates up 22%, suggests the upside potential is greater than initially assumed.

The broker upgrades to Accumulate from Hold and raises the target to $10.00 from $8.50.

TREASURY WINE ESTATES LIMITED ((TWE)) Upgrade to Outperform from Neutral by Credit Suisse .B/H/S: 4/3/1

The company missed the broker's expectations and cash flow in the first half, although there was a 25% increase in receivables outstanding, much of which was paid down in January.

The broker finds some signs of falling prices in the Penfolds luxury range, and there is a risk that the market may struggle to absorb the double-digit uplift in supply.

However, the continued expansion of the range in China should allow for very strong growth.

Credit Suisse upgrades to Outperform from Neutral and raises the target to $19.85 from $16.45. The company expects to grow operating earnings by 15-20% in FY20.

See also TWE downgrade.

VOCUS GROUP LIMITED ((VOC)) Upgrade to Overweight from Equal-weight by Morgan Stanley .B/H/S: 1/5/2

Morgan Stanley has become bullish on the potential for market share gains in the Australian enterprise segment of Vocus. The broker considers Vocus a turnaround story, upgrading to Overweight from Equal-weight.

While the broker acknowledges the enterprise segment is smaller, it is less competitive and offers sustainable higher margins than the consumer segment.

Target is raised to $4.00 from $2.90. Industry view is In-Line.

Downgrade

AMCOR LIMITED ((AMC)) Downgrade to Neutral from Outperform by Credit Suisse .B/H/S: 5/2/0

First half results demonstrate to Credit Suisse that operations are on track. The broker maintains FY20 and FY21 estimates unchanged.

FY19 estimates for earnings per share are reduced by -3% because of the delay in the closure of the Bemis transaction, relative to earlier expectations.

The recent rally in the share price has closed out excessive near-term returns, in the broker's view, although fundamentals appears solid.

Credit Suisse downgrades to Neutral from Outperform and raises the target to $14.90 from $14.80.

AMP LIMITED ((AMP)) Downgrade to Neutral from Buy by Citi and Downgrade to Hold from Accumulate by Ord Minnett .B/H/S: 0/7/0

In response to AMP's result and guidance Citi has cut forecast earnings by -3% in FY19 and -13% in FY20, cut its target to $2.50 from $2.80, and downgraded to Neutral (High Risk).

AMP does appear to offer some longer term value, the broker suggests, but an internal focus and rebasing of underlying earnings expectations mean investors will likely require significant patience before returns emerge. And the risk of regulatory action remains.

2018 underlying earnings were in line with guidance. Ord Minnett believes 2019 will be a year of re-building and poses significant challenges.

The broker reduces the rating to Hold from Accumulate, noting the uncertainty in wealth management and the absence of immediate catalysts. Target is reduced to $2.35 from $2.60.

ASX LIMITED ((ASX)) Downgrade to Sell from Hold by Deutsche Bank .B/H/S: 0/2/6

Deutsche Bank saw ASX delivering an interim performance in line with expectations. The analysts point out there is impact from the new accounting standard AASB15, but further out this should reduce the volatility of income recognition, on their assessment.

It's the valuation that is a problem, however, and on that basis the stock is receiving a downgrade to Sell from Hold. Target price falls to $57.60 (was $58.50).

AURIZON HOLDINGS LIMITED ((AZJ)) Downgrade to Neutral from Outperform by Macquarie .B/H/S: 1/6/1

First half results were ahead of expectations. The company has resolved the uncertainty around UT5 which Macquarie notes delivers a strong FY20 outlook, while lowering FY19 estimates.

The broker considers the stock is trading at fair value and surprise on the upside is limited and downgrades to Neutral from Outperform. Target is reduced 4.5% to $4.45.

See also AZJ upgrade.

BENDIGO AND ADELAIDE BANK LIMITED ((BEN)) Downgrade to Underperform from Neutral by Credit Suisse and Downgrade to Sell from Neutral by Citi and Downgrade to Sell from Neutral by UBS .B/H/S: 0/0/6

Credit Suisse downgrades earnings estimates by up to -10% across the forecast horizon on the back of the first half results.

The broker believes the bank will struggle to achieve earnings growth in the near term, given revenue pressures.

Credit Suisse downgrades to Underperform from Neutral and reduces the target to $10.00 from $11.50.

Citi was disappointed with the first half result, which was weak despite a low bad debt expense. Revenue challenges are starting to mount, in the broker's view.

Meanwhile cost growth is unable to adjust to the slower revenue environment. The broker lowers FY19-21 cash estimates for earnings per share by -5-11%.

Rating is downgraded to Sell from Neutral and the target lowered to $9.50 from $11.25.

Bendigo and Adelaide Bank's first-half result missed the broker by 2% and UBS notes underlying trends deteriorated.

Net interest margins remain under pressure, retail and wholesale deposits fell, gross loans were down, and costs were up.

UBS downgrades earnings per share -4%/-9%/-8% across FY19/20/21. The stock is downgraded to Sell from Neutral.

BREVILLE GROUP LIMITED ((BRG)) Downgrade to Accumulate from Buy by Ord Minnett and Downgrade to Underperform from Neutral by Credit Suisse .B/H/S: 1/2/1

First half net profit was ahead of Ord Minnett's forecast. The broker acknowledges Breville is making genuine improvements and its ambitious plans appear to be working.

This is supported by 9% constant currency growth even against tough comparables. Ord Minnett increases the target to $15.08 from $13.69.

While envisaging potential upside for those willing to take a slightly longer view, the broker downgrades the rating to Accumulate from Buy on valuation grounds.

First half results were solid, Credit Suisse notes, and stronger than expected. However, the broker suspects expectations of margin expansion in the medium term are likely to be optimistic.

The broker increases FY19 forecasts by 4%, which implies 12.4% operating earnings (EBIT) growth.

Rating is downgraded to Underperform from Neutral, a valuation-based view given the performance in the share price and considered an opportunity to take profit. Target is raised to $12.59 from $11.69.

See also BRG upgrade.

CITY CHIC COLLECTIVE LTD ((CCX)) Downgrade to Neutral from Buy by Citi .B/H/S: 0/1/0

The company formerly known as Specialty Fashion (now in slimmed down survivor format) reported an interim financial performance some 3% above expectations at Citi. The two key items, according to the analysts, were strong sales growth and steady gross profit margins.

Dividends are back on the agenda, and Citi welcomes the move, adding further capital management may release excess franking credits. Interim dividend of 2.5c was well ahead of Citi's predicted 1.5c, plus shareholders also receive a special 2.5c on top.

Taking it all in, Citi's share price target has risen to $1.45 but the rating is lowered to Neutral from Buy, in reference to the share price rally.

CHALLENGER LIMITED ((CGF)) Downgrade to Sell from Hold by Deutsche Bank .B/H/S: 1/5/1

Slowing sales, falling margins and mounting concerns regarding asset quality have caused Deutsche Bank to sharply revise forecasts lower.

The broker reduces the target to $7.00 and downgrades to Sell from Hold.

CLASS LIMITED ((CL1)) Downgrade to Reduce from Hold by Morgans .B/H/S: 1/1/1

Class's 2019 first-half result met the broker but Morgans downgrades to Reduce from Hold, believing free-cash conversion and rising costs point to challenges ahead.

Previously, the broker set the target price on a discounted valuation basis but has shifted to a blended valuation to reflect political (federal election) and regulatory risk.

Target price falls to $1.34 from $1.48.

COCHLEAR LIMITED ((COH)) Downgrade to Equal-weight from Overweight by Morgan Stanley .B/H/S: 1/4/2

The share price has risen 24% since November and is now trading around 12% above Morgan Stanley's target. As the valuation does not adequately cover the short-term risks Morgan Stanley downgrades to Equal-weight from Overweight and raises the target to $176 from $175.

The broker remains positive on the longer-term outlook, given the eventual evolution of the referral channel to a more retail setting, but notes short-term risks exist, such as a likely weighting to the second half for earnings, which implies a tough hurdle for FY19 guidance. In-Line industry view.

CLEANAWAY WASTE MANAGEMENT LIMITED ((CWY)) Downgrade to Hold from Buy by Deutsche Bank and Downgrade to Neutral from Buy by UBS and Downgrade to Neutral from Outperform by Credit Suisse .B/H/S: 2/4/0

Deutsche Bank analysts describe the interim report as a "good beat across the board". Both revenues and margins surprised to the upside. But it's all in the share price already, which is why the Hold rating is now in place (downgrade from Buy). Target price jumps to $2.33.

First half results beat expectations. The improvement in the business impressed UBS, as both organic growth and underlying operating leverage were stronger than expected.

Momentum should continue into the second half. The broker continues to highlight the defensive characteristics of the business.

Yet, at current levels, this is largely reflected in the share price and the rating is downgraded to Neutral from Buy. Target is raised to $2.30 from $2.15.

First half results were below Credit Suisse estimates. Integration of Toxfree remains on track and the synergy timeline is unchanged.

While the broker likes the business and the opportunities, the shares are considered fully valued for now.

Credit Suisse downgrades to Neutral from Outperform and raises the target to $2.15 from $2.05.

DOWNER EDI LIMITED ((DOW)) Downgrade to Neutral from Outperform by Credit Suisse .B/H/S: 4/1/0

First half net profit was below Credit Suisse forecasts. The broker is perplexed about the change in segment reporting, finding the rationale and lack of advance notice a problem.

Credit Suisse lowers FY19 estimates by -7%, largely because of higher financing and tax expenses. Management also appears cautious on the potential pace of improvement at the Spotless business.

Credit Suisse reduces the target to $7.40 from $8.25 and downgrades to Neutral from Outperform.

FLIGHT CENTRE LIMITED ((FLT)) Downgrade to Hold from Add by Morgans .B/H/S: 3/5/0

Ahead of Flight Centre's result release, Morgans notes recent data points to slowing demand for travel. The travel agent will not be immune to weaker discretionary spending and the broker notes weakness comes at a time cost pressures are mounting.

The broker has decided to "err on the side of conservatism" and shift its forecast to the lower end of guidance, and downgrade to Hold from Add. Target falls to $47.75 from $51.00.

GPT ((GPT)) Downgrade to Neutral from Outperform by Macquarie .B/H/S: 0/6/0

Macquarie downgrades to Neutral from Outperform after the 2018 result. The target is raised to $5.99 from $5.95.

While attracted to the earnings growth in 2019 and the strong balance sheet, which is supported by the potential sale of MLC, the broker points to the difficult retail environment and limited shareholder returns.

The broker observes the company is increasing its weighting to logistics but retail will still remain over 40% of capital.

MAGELLAN FINANCIAL GROUP LIMITED ((MFG)) Downgrade to Neutral from Outperform by Macquarie and Downgrade to Hold from Add by Morgans and Downgrade to Neutral from Buy by UBS .B/H/S: 3/4/0

Magellan's result beat Macquarie by 3%, reflecting well managed costs. The fund manager continues to deliver strong results, the broker notes, and recent performance metrics should support ongoing funds flows.

But the stock is trading at a 21% premium to ASX listed fund managers against a five-year average of 14%. Macquarie thus downgrades to Neutral on valuation grounds. Target rises to $31.75 from $29.00.

Magellan Financial Group's 2019 first-half result outpaced the broker by 4%, as management fee revenue rose 27% on the previous half and a strong performance from core funds.

The broker notes growth potential, pointing to the stock's balance sheet and new products.

But the stock is trading within Morgan's valuation so the stock is downgraded to Hold from Add, looking for a better entry point.

Target price rises to $33.40 from $28.76.

The company continues to experience a significantly stronger investment performance and fund flow trends versus its listed asset management peers.

UBS believes this momentum is now adequately priced into the stock and downgrades to Neutral from Buy.

First half net profit was ahead of estimates, driven largely by funds management profits. Target is raised to $32.30 from $28.90.

NEWCREST MINING LIMITED ((NCM)) Downgrade to Sell from Neutral by UBS .B/H/S: 1/4/3

First half results were in line with forecasts. Newcrest now appears expensive to UBS, trading around 10% above valuation.

The broker believes the premium to the rest of the market is not justified, as production is likely to peak in the next two years.

UBS downgrades to Sell from Neutral and reduces the target to $24.00 from $24.50.

PACT GROUP HOLDINGS LTD ((PGH)) Downgrade to Underperform from Neutral by Macquarie and Downgrade to Reduce from Hold by Morgans .B/H/S: 1/2/2

First half operating earnings (EBITDA) are now expected to be $110m and FY19 guidance is now lowered to $230-245m versus 245m previously.

The company has had a challenging start to the year which includes significant cost headwinds and weaker demand conditions in some sectors.

Macquarie notes there appears to have been limited benefit from price reductions that have recently occurred in resin.

The broker downgrades to Underperform from Neutral, highlighting concerns about the base business, and reduces the target to $3.40 from $3.72.

First half operating earnings (EBITDA) were -5% below Morgan's forecasts. Management has downgraded guidance, affected by the uncertainty surrounding the speed with which revenue and efficiency projects can be delivered and the rate that input costs can be recovered.

The aspect of most concern to Morgans is that resin prices have moved in the company's favour over the past four months, which implies the underlying business remains very weak.

The broker suggests investors avoid the stock until the company can demonstrate more stable earnings, and downgrades to Reduce from Hold. Target is lowered to $3.01 from $3.24.

STOCKLAND ((SGP)) Downgrade to Sell from Neutral by UBS .B/H/S: 3/2/1

UBS has downgraded Stockland to Sell from Neutral ahead of its first half result, which the broker expects will reflect the slowdown in the residential, retail and retirement markets.

The broker sees no respite in the market situation and expects deterioration across all core business through FY19.

Target price falls to $3.60 from $3.74.

SPARK INFRASTRUCTURE GROUP ((SKI)) Downgrade to Hold from Accumulate by Ord Minnett .B/H/S: 0/6/1

The Federal Court has found in the Australian Taxation Office's favour regarding the litigation with Victoria Power Networks. Ord Minnett believes the biggest negative is a downgrade to 2019 dividend guidance.

This likely reflects the broader issue, in the broker's view, of distribution network providers funding growth opportunities in unregulated assets while maximising cash returns to investors.

Rating is downgraded to Hold from Accumulate on the target trimmed to $2.50 from $2.55.

SUPER RETAIL GROUP LIMITED ((SUL)) Downgrade to Hold from Add by Morgans .B/H/S: 3/5/0

First half results appear ahead of forecasts but overshadowed by further wage underpayments issues, which Morgans notes are significant. The full result is due on February 14.

The broker lowers estimates by -1-2% in the forecast years and also lowers capital expenditure assumptions. The broker recognises the undemanding valuation but awaits further clarity on the incoming CEO's strategy.

Rating is downgraded to Hold from Add and the target raised to $8.56 from $8.54.

TRANSURBAN GROUP ((TCL)) Downgrade to Neutral from Outperform by Macquarie .B/H/S: 3/4/1

While accounting influenced the first half result, the focus is on cash generation and Macquarie expects the reliance on refinancing as a supplement should diminish in the next two years.

Management has emphasised current project developments and internal opportunities, such as the widening of the M7.

Macquarie makes minor changes to its forecast to reflect weaker traffic at Citylink and marginally lowers the target to $11.89. Rating is downgraded to Neutral from Outperform.

Macro influences are expected to be the major driver of the performance in the near term.

TASSAL GROUP LIMITED ((TGR)) Downgrade to Neutral from Outperform by Credit Suisse .B/H/S: 1/2/0

First half results beat Credit Suisse forecasts, confirming the view that the company will benefit from high harvest volumes and still enjoy strong pricing.

The broker continues to believe the market dynamics for salmon are supportive and believes the targets for prawns, if achieved, will materially boost earnings.

The broker downgrades to Neutral from Outperform as the valuation is back in line with the long-run average. Target is raised to $5.15 from $4.90.

TREASURY WINE ESTATES LIMITED ((TWE)) Downgrade to Equal-weight from Overweight by Morgan Stanley and Downgrade to Hold from Accumulate by Ord Minnett .B/H/S: 4/3/1

Morgan Stanley believes the brand is being stretched more and suspects the need to put away large volumes is likely to slow growth. While America represents a good story, the broker believes this is captured in expectations.

Meanwhile, luxury inventory is rising. As the valuation now appears fair, the broker downgrades to Equal-weight from Overweight. Industry view: Cautious. Price target $17.

First half underlying net profit was below Ord Minnett's forecast. Despite strong execution and EBITS growth, the broker observes growth rates are becoming more dependent on vintage, which affects the multiple.

Moreover, incremental EBITS growth generates less cash and this reduces valuation support. Ord Minnett downgrades to Hold from Accumulate and reduces the target to $17.50 from $20.00.

See also TWE upgrade.

UNIBAIL-RODAMCO-WESTFIELD ((URW)) Downgrade to Underperform from Outperform by Macquarie .B/H/S: 1/2/1

Following the release of 2018 financials, Macquarie has double-step downgraded to Underperform from Outperform. In an initial response to the release, the analysts note 2019 guidance is -8% below their own forecast, and -13% below market consensus.

The underlying weakness can become a genuine problem, point out the analysts, given elevated gearing of the balance sheet. New target $10.88 (was $13.59).

VIRGIN AUSTRALIA HOLDINGS LIMITED ((VAH)) Downgrade to Underperform from Neutral by Credit Suisse .B/H/S: 0/1/2

Management has noted pricing for business travellers has been flat in the past month while the leisure market is down slightly. The company is guiding to at least 7% revenue growth in the third quarter, slowing from the 10% reported in the first half.

While underlying pre-tax profit estimates are reduced by -67% for FY19 Credit Suisse improves forecasts for FY20 and FY21 on lower fuel cost assumptions.

The broker downgrades to Underperform from Neutral and reduces the target to $0.18 from $0.20.

WOODSIDE PETROLEUM LIMITED ((WPL)) Downgrade to Hold from Accumulate by Ord Minnett .B/H/S: 4/4/0

2018 results were below expectations because of higher depreciation and finance costs. Yet, the full year dividend surprised Ord Minnett, implying a 94% pay-out ratio.

Management indicated this was due to stronger cash generation over 2018.

With the stock trading in line with valuation and consensus earnings forecasts appearing optimistic, Ord Minnett downgrades to Hold from Accumulate. Target is steady at $34.50.

Total Recommendations Recommendation Changes

Broker Recommendation Breakup

Broker Rating Order Company New Rating Old Rating Broker Upgrade 1 AURIZON HOLDINGS LIMITED Neutral Sell Citi 2 AURIZON HOLDINGS LIMITED Neutral Sell Morgan Stanley 3 BAPCOR LIMITED Buy Neutral Morgans 4 BREVILLE GROUP LIMITED Neutral Sell UBS 5 CHARTER HALL LONG WALE REIT Neutral Sell Ord Minnett 6 GOODMAN GROUP Buy Neutral Credit Suisse 7 LENDLEASE GROUP Buy Neutral UBS 8 NORTHERN STAR RESOURCES LTD Buy Neutral Ord

Minnett 9 TREASURY WINE ESTATES LIMITED Buy Neutral Credit Suisse 10 VOCUS GROUP LIMITED Buy Neutral Morgan Stanley Downgrade 11 AMCOR LIMITED Neutral Buy Credit Suisse 12 AMP LIMITED Neutral Buy Citi 13 AMP LIMITED Neutral Buy Ord Minnett 14 ASX LIMITED Sell Neutral Deutsche Bank 15 AURIZON HOLDINGS LIMITED Neutral Buy Macquarie 16 BENDIGO AND ADELAIDE BANK LIMITED Sell Neutral Citi 17 BENDIGO AND ADELAIDE BANK LIMITED Sell Neutral UBS 18 BENDIGO AND ADELAIDE BANK LIMITED Sell Neutral Credit Suisse 19 BREVILLE GROUP LIMITED Sell Neutral Credit Suisse 20 BREVILLE GROUP LIMITED Buy Buy Ord Minnett 21 CHALLENGER LIMITED Sell Neutral Deutsche Bank 22 CITY CHIC COLLECTIVE LTD Neutral Buy Citi 23 CLASS LIMITED Sell Neutral Morgans 24 CLEANAWAY WASTE MANAGEMENT LIMITED Neutral Buy UBS 25 CLEANAWAY WASTE MANAGEMENT LIMITED Neutral Buy Credit Suisse 26 CLEANAWAY WASTE MANAGEMENT LIMITED Neutral Buy Deutsche Bank 27 COCHLEAR LIMITED Neutral Buy Morgan Stanley 28 DOWNER EDI LIMITED Neutral Buy Credit Suisse 29 FLIGHT CENTRE LIMITED Neutral Buy Morgans 30 GPT Neutral Buy Macquarie 31 MAGELLAN FINANCIAL GROUP LIMITED Neutral Buy Morgans 32 MAGELLAN FINANCIAL GROUP LIMITED Neutral Buy Macquarie 33 MAGELLAN FINANCIAL GROUP LIMITED Neutral Buy UBS 34 NEWCREST MINING LIMITED Sell Neutral UBS 35 PACT GROUP HOLDINGS LTD Sell Neutral Morgans 36 PACT GROUP HOLDINGS LTD Sell Neutral Macquarie 37 SPARK INFRASTRUCTURE GROUP Neutral Buy Ord Minnett 38 STOCKLAND Sell Neutral UBS 39 SUPER RETAIL GROUP LIMITED Neutral Buy Morgans 40 TASSAL GROUP LIMITED Neutral Buy Credit Suisse 41 TRANSURBAN GROUP Neutral Buy Macquarie 42 TREASURY WINE ESTATES LIMITED Neutral Buy Morgan Stanley 43 TREASURY WINE ESTATES LIMITED Neutral Buy Ord Minnett 44 UNIBAIL-RODAMCO-WESTFIELD Sell Buy Macquarie 45 VIRGIN AUSTRALIA HOLDINGS LIMITED Sell Neutral Credit Suisse 46 WOODSIDE PETROLEUM LIMITED Neutral Buy Ord Minnett Recommendation Positive Change Covered by > 2 Brokers Order Symbol Company New Rating Previous Rating Change Recs 1 BAP BAPCOR LIMITED 100.0% 75.0% 25.0% 4 2 LLC LENDLEASE GROUP 90.0% 70.0% 20.0% 5 3 FNP FREEDOM FOODS GROUP LIMITED 67.0% 50.0% 17.0% 3 4 CLW CHARTER HALL LONG WALE REIT -33.0% -50.0% 17.0% 3 5 GMG GOODMAN GROUP 33.0% 17.0% 16.0% 6 6 VOC VOCUS GROUP LIMITED -13.0% -29.0% 16.0% 8 7 TLS TELSTRA CORPORATION LIMITED -6.0% -21.0% 15.0% 8 8 NST NORTHERN STAR RESOURCES LTD -21.0% -29.0% 8.0% 7 9 OSH OIL SEARCH LIMITED 50.0% 43.0% 7.0% 8 10 STO SANTOS LIMITED 63.0% 57.0% 6.0% 8 Negative Change Covered by > 2 Brokers Order Symbol Company New Rating Previous Rating Change Recs 1 BEN BENDIGO AND ADELAIDE BANK LIMITED -93.0% -42.0% -51.0% 7 2 URW UNIBAIL-RODAMCO-WESTFIELD -13.0% 38.0% -51.0% 4 3 CWY CLEANAWAY WASTE MANAGEMENT LIMITED 33.0% 83.0% -50.0% 6 4 PGH PACT GROUP HOLDINGS LTD -20.0% 20.0% -40.0% 5 5 MFG MAGELLAN FINANCIAL GROUP LIMITED 43.0% 83.0% -40.0% 7 6 PTM PLATINUM ASSET MANAGEMENT LIMITED -100.0% -75.0% -25.0% 4 7 VAH VIRGIN AUSTRALIA HOLDINGS LIMITED -63.0% -38.0% -25.0% 4 8 SUL SUPER RETAIL GROUP LIMITED 31.0% 56.0% -25.0% 8 9 TGR TASSAL GROUP LIMITED 13.0% 38.0% -25.0% 4 10 SGP STOCKLAND 25.0% 42.0% -17.0% 6 Target Price Positive Change Covered by > 2 Brokers Order Symbol Company New Target Previous Target Change Recs 1 IEL IDP EDUCATION LIMITED 14.532 10.742 35.28% 5 2 GMG GOODMAN GROUP 12.448 10.783 15.44% 6 3 MFG MAGELLAN FINANCIAL GROUP LIMITED 32.670 28.885 13.10% 7 4 CWY CLEANAWAY WASTE MANAGEMENT LIMITED 2.248 2.015 11.56% 6 5 TLS TELSTRA CORPORATION LIMITED 3.153 3.000 5.10% 8 6 TGR TASSAL GROUP LIMITED 4.858 4.638 4.74% 4 7 NST NORTHERN STAR RESOURCES LTD 8.443 8.064 4.70% 7 8 VOC VOCUS GROUP LIMITED 3.239 3.101 4.45% 8 9 ASX ASX LIMITED 59.404 57.793 2.79% 8 10 AMC AMCOR LIMITED 15.591 15.216 2.46% 7 Negative Change Covered by > 2 Brokers Order Symbol Company New Target Previous Target Change Recs 1 CGF CHALLENGER LIMITED 7.949 8.989 -11.57% 8 2 URW UNIBAIL-RODAMCO-WESTFIELD 11.810 13.295 -11.17% 4 3 VAH VIRGIN AUSTRALIA HOLDINGS LIMITED 0.188 0.208 -9.62% 4 4 BEN BENDIGO AND ADELAIDE BANK LIMITED 9.600 10.492 -8.50% 7 5 PGH PACT GROUP HOLDINGS LTD 3.772 4.042 -6.68% 5 6 BAP BAPCOR LIMITED 6.985 7.438 -6.09% 4 7 PTM PLATINUM ASSET MANAGEMENT LIMITED 4.215 4.440 -5.07% 4 8 NAB NATIONAL AUSTRALIA BANK LIMITED 27.225 28.363 -4.01% 8 9 ORA ORORA LIMITED 3.520 3.640 -3.30% 8 10 SKI SPARK INFRASTRUCTURE GROUP 2.324 2.400 -3.17% 7 Earning Forecast Positive Change Covered by > 2 Brokers Order Symbol Company New EF Previous EF Change Recs 1 AGL AGL ENERGY LIMITED 191.614 158.057 21.23% 8 2 GBT GBST HOLDINGS LIMITED 13.300 11.350 17.18% 3 3 URW UNIBAIL-RODAMCO-WESTFIELD 153.498 135.521 13.27% 4 4 BPT BEACH ENERGY LIMITED 22.124 20.104 10.05% 5 5 GMG GOODMAN GROUP 55.577 50.577 9.89% 6 6 S32 SOUTH32 LIMITED 33.340 30.696 8.61% 7 7 TLS TELSTRA CORPORATION LIMITED 19.431 17.900 8.55% 8 8 CPU COMPUTERSHARE LIMITED 97.373 91.062 6.93% 8 9 WPL WOODSIDE PETROLEUM LIMITED 223.472 210.758 6.03% 8 10 IEL IDP EDUCATION LIMITED 26.280 24.920 5.46% 5 Negative Change Covered by > 2 Brokers Order Symbol Company New EF Previous EF Change Recs 1 VAH VIRGIN AUSTRALIA HOLDINGS LIMITED 0.100 0.220 -54.55% 4 2 AOG AVEO GROUP 9.733 15.500 -37.21% 3 3 CRN CORONADO GLOBAL RESOURCES 26.890 40.083 -32.91% 3 4 SLC SUPERLOOP LIMITED 3.000 4.000 -25.00% 3 5 CAR CARSALES.COM LIMITED 51.434 57.804 -11.02% 7 6 PGH PACT GROUP HOLDINGS LTD 23.237 25.818 -10.00% 5 7 REA REA GROUP LIMITED 231.029 252.086 -8.35% 7 8 TCL TRANSURBAN GROUP 21.133 22.835 -7.45% 8 9 FNP FREEDOM FOODS GROUP LIMITED 11.300 12.200 -7.38% 3 10 AIZ AIR NEW ZEALAND LIMITED 22.304 24.004 -7.08% 4 Technical limitations

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

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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 February 14, 2019

After a solid rally, last week saw the ASX200 track sideways in the 6000-6100 range, which it has done so ever since. There has been a lack of macro news of late – the world awaits an outcome on trade – and the local results season has largely netted itself out so far.

But boy have there been some big moves in share price, in either direction.

Last week the season was only just hotting up, with the bulk of reports coming in this week. Next week's Report may thus be interesting, but for now we can note some result-related moves.

There were three short position changes of more than one percentage point last week.

JB Hi-Fi ((JBH)) shorts fell to 12.7% from 14.6% and Bendigo & Adelaide Bank ((BEN)) shorts rose to 7.3% from 6.1%. Both reported earnings. See below.

Domain Group ((DHG)) shorts rose to 6.7% last week from 5.5% the week before. Oh dear. Domain's share price took off on this week's result, with short-covering likely a factor.

And for interest sake we note shorts in Bingo Industries ((BIN)) were little change last week at 5.0%. That stock fell -49% this week on a profit warning, before somewhat recovering in the following sessions.

Weekly short positions as a percentage of market cap:

10%+

SYR 16.8 ING 16.0 GXY 15.2 ORE 13.4 IVC 13.2 MTS 12.8 JBH 12.7 BWX 11.8 MYR 11.2 DMP 11.0 NXT 10.2 BAL 10.1

In: BAL

9.0-9.9

SDA, HVN, PLS

Out: BAL 8.0-8.9%

SUL, IFL

Out: NUF

7.0-7.9%

NUF, MSB, SGM, BEN, AMC, RWC

In: NUF, SGM, BEN, AMC Out: NAN

6.0-6.9%

NAN, BOQ, AMP, DHG, BKL, MND, GMA, RSG, CCP, A2M

In: NAN, DHG Out: AMC, SGM, BEN, SEK, HT1

5.0-5.9%

CGF, WSA, LYC, HT1, AHG, BGA, SEK, A2B, HUB, APT, CLH, PTM, KAR, BIN, CAR, KDR

In: HT1, SEK, CAR Out: DHG, NWS, MLX, ARB

Movers & Shakers

When FNArena first introduced the Short Report, previously in a different format, consumer goods retailer JB Hi-Fi perennially sat towards or at the top of the most shorted list. Result season after result season JB Hi-Fi would beat expectations, but still the shorters persisted.

Eventually, battered and bruised, the shorters retreated, and JB Hi-Fi fell off the 5%-plus table for a period. But the company has since acquired a difficult Good Guys business, and a foreign company by the name of Amazon has appeared on the scene. Suffice to say it didn't take long before JB Hi-Fi was back in its old familiar position, right up the top of the table.

In last week's report I noted JB Hi-Fi shorts fell to 14.6% from 15.6% ahead of Monday's earnings release, which scored a "not bad" and resulted in only a modest share price increase. Last week shorts fell to 12.7% from 14.6%.

In the words of Pete Seeger, when will they ever learn?

When the Hayne Royal Commission was in full swing the smaller regional banks managed to stay out of the spotlight as the Big Four were publically flayed. But they were very much in the spotlight last week when Bendigo & Adelaide Bank delivered a shocker of a result. Rather than take profits, shorters upped the ante increasing the position to 7.3% from 6.1%.

Also at 6.1% the week before was peer Bank of Queensland ((BOQ)). Its shorts ticked up to 6.8% in sympathy with Bendalaide but it was this week BOQ issued a profit warning even more substantial than its peer, resulting in an even more severe market response.

We'll see how it fared in next week's Report.

ASX20 Short Positions (%)

Code Last Week Week Before Code Last Week Week Before AMC 7.1 6.9 RIO 4.2 3.9 ANZ 1.5 1.5 S32 0.5 0.7 BHP 4.5 4.5 SCP 1.1 0.9 BXB 0.3 0.5 SUN 0.9 0.8 CBA 2.4 2.3 TCL 1.5 1.5 COL 2.1 1.9 TLS 0.5 0.5 CSL 0.3 0.2 WBC 2.1 2.1 IAG 0.4 0.3 WES 1.4 1.5 MQG 0.3 0.3 WOW 2.8 2.8 NAB 0.9 0.7 WPL 0.7 0.8 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.

February Reports: Early Resilience & Big Disappointments

In this week's Weekly Insights:

-February Reports: Early Resilience & Big Disappointments -Share Market Outlook: Support & Threats -CSLChallenge: Business As Usual -Rudi On TV -Rudi On Tour

February Reports: Early Resilience & Big Disappointments

By Rudi Filapek-Vandyck, Editor FNArena

Late in January, I had an inkling we might be staring at an unusually savage reporting season locally throughout February.

My concern stemmed from the way investors had responded to early "misses" from the likes of ResMed ((RMD)) and GUD Holdings ((GUD)); it was immediate, harsh and merciless.

Every reporting season generates winners and losers, based upon "beats" and "misses" derived from corporate financials, but this time around share markets have gone through a wild rollercoaster ride, economic data are weak, and weakening, central bankers are reviewing their policy stance, and profit forecasts have been steadily sliding downwards for months.

Judging from the first 100-odd companies in the FNArena universe having reported their financial numbers thus far this month, it would appear the news to date is less bad than feared, if we measure total "beats" versus "misses" or we concentrate on the fact most companies have stuck by a relatively optimistic guidance for the full year.

But market forecasts ex-resources are still steadily sliding south and, on my observation, many companies that release financial reports experience downward pressure on the share price. If not on day one, then most likely in the days following the results release. Surely many an investor -both professionals and retail- has been wondering just how hard it is to successfully maneuver the ins and outs of February this year?

In terms of stockbroker ratings, the bias is very much weighted towards downgrades in recommendations. Total downgrades for the season thus far stand at 44 versus 14 upgrades, and these do not include many more that are not directly related to financial results released.

On Tuesday, when I write these sentences, total tally for the day is seven downgrades against one upgrade to Hold (!). At least on Monday, the balance was three against three (this is an exception though).

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As far as "winners" are concerned, companies including Magellan Financial ((MFG)), IDP Education ((IEL)), Cleanaway Waste Management ((CWY)), Goodman Group ((GMG)), Breville Group ((BRG)), and Altium ((ALU)) have proven that, this time around, they are not impacted by weak conditions and shaky confidence, instead showing off internal resilience and strong growth numbers, leaving both analysts and shorters scrambling to catch up post result.

Each of these companies will feature prominently on the short list of quality positive surprises at the end of the season.

On the other end, the list of negative surprises is already quite a long one, and growing by the day. Today, Tuesday 19 February, share prices for Blackmores ((BKL)) and Emeco Holdings ((EHL)) are both down in excess of -20%. Yesterday, a profit warning from Bingo Industries ((BIN)) caused that share price to fall by -49%.

Investors have equally not been kind to regional lenders Bendigo and Adelaide Bank ((BEN)) and Bank of Queensland ((BOQ)); the latter issued a trading update, Helloworld ((HLO)), Smartgroup Corp ((SIQ)), Bapcor ((BAP)), Automotive Holdings ((AHG)), Carsales ((CAR)), Challenger ((CGF)), Praemium ((PPS)), and numerous others.

While Healius ((HLS)) proved you can put a different name on a perennially disappointing business, but the underlying operations will still keep issuing profit warnings. Pact Group ((PGH)), can you imagine, has issued its sixth profit warning since May 2017, its second over the past three months.

One pleasant surprise is some retailers are managing to withstand general scepticism, releasing relatively resilient numbers accompanied by cautiously optimistic outlooks; think JB Hi-Fi ((JBH)), Nick Scali ((NCK)), and City Chic

Collective ((CCX)). The real question here remains, of course, is it sustainable? What if consumers further tighten their belts? Can online competition be held at bay indefinitely?

Both results from Unibail-Rodamco-Westfield ((URW)) and Vicinity Centres ((VCX)) revealed risks are rising for retail landlords. Equally important: investors bamboozled by an apparent easy yield on offer, but no growth, beware.

Companies including Medibank Private ((MPL)), Computershare ((CPU)) and Insurance Australia Group ((IAG)) have equally shown resilience, but their path forward remains too clouded for many.

As mentioned, early disappointments have come out in spades. They include high quality, long-term sustainable growth companies, and popular market darlings REA Group ((REA)), Carsales, Bapcor, ResMed, Cochlear ((COH)), Transurban ((TCL)), possibly even CSL ((CSL)) - see also further below.

For many of these consistent (out)performers, the pattern from past reporting seasons often means share prices respond negatively to results releases, but they pick up later when the market's attention shifts from short term disappointment to longer term fundamentals. Observe, for example, how shares in REA Group are by now well ahead of where they were prior to the interim report release, despite management issuing rather sober guidance for H2.

Irrespective, market sentiment can be fickle and not always as predictable as history suggests. I for one will be watching these share prices from close distance, also because they still make up the core of the FNArena/Vested Equities All-Weather Model Portfolio.

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Combining all of the above, analysts at CommSec have calculated profit growth for ASX200 members that have reported to date averages 7%, which is far from bad, but the average EPS growth would be less as companies pay for acquisitions through issuing extra shares.

CommSec has also calculated average growth in operational costs for these companies is above 9%, which provides a firm indication about one of the key problems that is surfacing this reporting season: companies might still be selling more products and services, but their costs are rising fast.

Rising costs are equally a problem for resources companies, Whitehaven Coal ((WHC)) comes to mind, but at least miners and energy producers are enjoying an upward boost to forecasts because of higher-for-longer prices for their product. Looking into the details thus far, this seems to apply more for miners than for oil and gas producers, at least thus far.

Financials, including banks, are not doing so well. Among industrials, traditional media companies stand out in a negative way, as also illustrated by the profit warning of Seven West Media ((SWM)) on Tuesday.

Deutsche Bank strategists, who have been mildly positively surprised by reporting season thus far, report only about half (50%) of companies reporting have triggered a downgrade in estimates post report against an average of 56% for past reporting seasons.

Citi strategists who had earlier suggested the average growth forecast for the Australian market ex-resources and ex-banks might end in the negative by month's end (from an underlying EPS growth forecast of circa 1.5%), are now suggesting that number could possibly remain above zero.

The average EPS growth forecast for banks has now fallen to only 1% for FY19. For resources companies the growth forecast has increased to an average 13.5%, to be followed by 2% growth for FY20 (but this far out such forecasts are very "rubbery").

For the share market ex-banks and ex-resources the average EPS growth forecast has now shrunk to 1.3% from 1.5% before February. But let's face it, it's early days still, and history suggests the real bad news more often than not hides inside the tail end of the season.

Maybe not this time around. Citi strategists, for one, are growing more optimistic. They have retained their forecast for the ASX200 to end the calendar year at around 6300.

Investors should note FNArena maintains an All-Year Round Australian Corporate Results Monitor, with daily updates throughout the February results season:

https://www.fnarena.com/index.php/reporting_season/

For an in-depth review of potential "beats" and "misses" this season:

https://www.fnarena.com/index.php/2019/02/07/february-reporting-season-preview/

Share Market Outlook: Support & Threats

The OECD Composite of Leading Indicators, designed to show the status of global economic momentum and turning points in the business cycle, has now fallen for thirteen months straight, to a deeper negative reading in December, the latest update available.

Should investors pay attention, and why aren't financial markets paying more attention, and acting more in line with what the OECD momentum indicator is signalling?

Well, arguably, continuous weakness in the OECD CLI had been one of the factors behind the savage turn in share markets' momentum and direction last year, on top of the realisation that earnings forecasts in the US, and elsewhere, needed a major reset to the downside.

Come calendar 2019 and investors are now taking guidance from the Federal Reserve pausing its tightening, while central banks elsewhere (UK, eurozone, China, Australia, New Zealand, etc) are believed to be ready to reintroduce supportive policies and measurements, if and when necessary.

Watch this space if the negative OECD CLI trend continues for much longer.

As far as corporate profit growth is concerned, it is true the short term outlook is negative in the US, but market expectations are for a major rebound in the second half of the calendar year.

Add continued optimism about a pending deal between the Trump trade deal negotiators and the Chinese regime, and there seem to be plenty of reasons for investors globally to ignore those pesky economic indicators, which, if anything, seem to confirm the global economy late in 2018 did experience quite the noticeable deceleration in spending and momentum.

Don't be surprised if financial markets continue to ignore the many calls about short term overbought momentum and time for a retreat in share prices for a while longer.

In fact, in light of the events post mid-September last year (to the downside) and post Christmas (to the upside), I think financial markets globally have done their utmost best to make a mockery out of "experts" trying to predict what might happen next.

There is an old saying that ultimately, financial markets are there to keep investors humble. I don't think it's a big stretch to conclude many an investor has been humbled over the past six months or so.

Just about everybody except Magellan Financial's Hamish Douglass, I feel inclined to add, a little bit tongue-in-cheek.

Global bond markets are now offering lower yields, meaning government debt the world around is back to being priced for slower growth ahead, and still no inflation. This too, for the time being, is supporting equity markets.

Thus in a general, macro sense the general context has quickly returned positive for equities, which is why the ASX200 is trying to re-conquer the 6100 mark on Monday (hands up, who had predicted this at the start of the year?), but on a micro level, the slowdown that is apparent from economic indicators and global bond markets is having a major impact on individual companies.

This is why the first half of the local reporting season month that is February has been so tricky for many an investment portfolio (see also above).

Returning to the economic signals, it is easy to see why the more bearish inclined investors are jumping up and down predicting much lower equity markets in due course. The aforementioned OECD CLI hasn't shown a negative stretch of its current length (13 months in succession) in 2.5 years.

Year-on-year, the index is down -1.3%, which is the most negative read since July 2009, when quantitative easing was helping economies climbing out the quagmire of the GFC. Not making matters any less worrisome, is the observation that 95% of countries included are now contracting on a year-on-year comparison, marking the worst geographic breadth since May 2012, when Europe was on the verge of imploding.

What is most remarkable, however, is that one year ago closer to 80% of countries were still enjoying an expansion in their CLI. A big thanks to Glushkin Sheff's David Rosenberg for putting together these quick milestones. No wonder the world got into a sudden shock last year; the reversal in underlying momentum has been nothing short of phenomenal.

Equity markets might be broadly supported within the current context, there is good reason not to allow one's self to become overly complacent, however. As pointed out by Citi's US strategist Tobias M Levkovich last week, thus far the weakening US economy had been offset by the fact that lending standards were holding up.

Not any more, if we rely on the most recent senior loan officers' survey, which revealed quite the dramatic decline in commercial and industrial credit conditions.

Typically, this SLO Survey leads human, working capital and physical investment by nine months. Therefore, if the February 4 update is now indicative of a new, deteriorating environment for US credit, industrial activity might turn out rather soft later in the year, and this contrasts with current analysts' forecasts, which are partially underpinning supportive sentiment.

Summarising all of the above, I'd say it's probably both too late and too early to get spooked by the rapid loss in momentum for the economy in the USA and globally, but it's at the same time inappropriate to extrapolate events and share market moves during the first seven-eight weeks of the fresh calendar year indefinitely into the future.

CSLChallenge: Business As Usual

In January I launched the CSLChallenge, see for more info here:

https://www.fnarena.com/index.php/2019/01/14/rudis-view-join-the-csl-challenge/

In recent days I received questions from eager shareholders whether they can expect an update from my hand any time soon, now the company has publicly released its interim financials. I did promise I would provide regular updates on the company, also including sector peers Cochlear ((COH)), disappointing investors on Tuesday, and ResMed ((RMD)).

To go straight to the core of the matter: CSL's interim performance was solid, yet not as good as many were expecting, and while guidance for the full year has been tightened towards the upper end of the prior communicated range, some of the short term traders were positioned for something better.

Hence there was only one way to go for the share price, and that is down.

The underlying market disappointment with the published numbers is probably best illustrated by the observation FNArena's consensus price target for the shares has fallen to a smidge below $204 from near $211.50 ahead of the market update.

Had this occurred in August last year, when CSL shares were changing hands for $230, last week's earnings miss would have led to a severe share price shellacking. This time around, however, a few dollars were shaved off, and that was it.

For those investors who joined the CSLChallenge and get restless and uncertain by these events, I suggest you stop listening to the small army of doom & gloom forecasters, of which a few have tried to give me a hard time via Twitter even before the result was out, and simply seek comfort in the fact this is not the first time CSL has missed analysts expectations.

These things happen. Leading a global biotech company such as is CSL is quite the complex endeavour, and there are challenges, and changes, and unforeseen circumstances on a near daily basis.

On occasion, such events put pressure on the share price in the short term. Longer term, however, it is the quality of the operations, the company's track record and reliability, and the inner strength of the business that will continue supporting the share price.

I note, for example, a change in sentiment at Deutsche Bank (Hold, price target $198) where the analysts were disappointed the financial performance of CSL's core business (Behring, plasma) had not been stronger in the six months to December. That feeling of disappointment seems to have disappeared since competitor Shire (owned by Japan's Takeda) released its quarterly sales report.

Now the overruling view at Deutsche Bank is that CSL's performance wasn't so bad at all. Shire is believed to have lost market share to CSL, with the latter's Haegarda sales outperforming Shire's competing product Cinryze.

The about face at Deutsche Bank firms my view the disappointment from last week's interim results should not linger for long. In an overall environment where most companies in Australia, outside resources, find it extremely hard to grow profits, and in particular to continue growing profits in the face of rising headwinds, CSL's ongoing profit growth remains a jewel in the Australian share market crown.

It is only a matter of time before this again translates into a rising share price, of that I remain convinced.

Rudi On TV

My weekly appearance on Your Money is now on Mondays, midday-2pm, but due to the February reporting season I shall remain absent both on Monday, 18th February and on 25th February.

Rudi On Tour In 2019

-ASA Inner West chapter, Concord, Sydney, March 12 -ASA Sydney Investor Hour, March 21 -ASA Toowoomba, Qld, May 20 -U3A Investor Group Toowoomba, Qld, May 22 -AIA Adelaide, SA, June 11 -AIA National Conference, Gold Coast, Qld, 28-31 July -AIA and ASA, Perth, WA, October 1

(This story was written on Monday and Tuesday 18-19 February 2019. It was published on the Tuesday in the form of an email to paying subscribers at FNArena, and again on Thursday as a story on the website).

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