Week

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Stories To Read From FNArena

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Contents

Confidence Grows In Janus Henderson

Growth drivers for Janus Henderson are tracking ahead of most expectations and brokers are more confident regarding the outlook.

-Cost profile appears higher going forward -Business now more exposed to less-favourable trends for active equities -Merged organisation better able to leverage capabilities via global collaboration

By Eva Brocklehurst

In its September quarter update, Janus Henderson ((JHG)) indicated integration efforts are moving ahead of expectations, upgrading synergy targets from the recent merger by US$15m to US$125m. Furthermore, brokers note flow trends into the company's funds are looking more positive.

UBS suggests that a return to positive net inflows will be supported by ongoing improvements in investment performance, higher assets under management and fee margins, as well as the upgraded cost synergy targets. The broker acknowledges cost growth is elevated but expects this to normalise in the current quarter. In addition, upgraded merger synergy targets should assist the outer-year margins.

Deutsche Bank is a little more cautious regarding the flow outlook, as positive net flows of $700m included a $1.8bn institutional equity mandate. This suggests core equity flows remain weak despite the generally improved performance. The broker remains encouraged by the potential for stronger long-term growth post the merger of two well-regarded US and UK/Australian active managers, but believes the risk/return is balanced.

The business is more exposed to less favourable trends for active equities and mutual fund vehicles and there is more downside risk in a bear equity market scenario. On the other hand, the combined organisation should better leverage its active management capabilities via global collaboration. Hence, Deutsche Bank maintains a wait-and-see approach and a Hold rating.

Citi suggests the strong performance in the equity market since September 30 has offset the impact on earnings from the miss to its expectations. The company potentially offers superior growth versus many of its peers and the broker lifts its rating to Buy from Neutral.

Bell Potter also believes the company is proving the merits of the merger. In addition, closing funds under management were 3.4% ahead of expectations, resulting in a meaningful upgrade to estimates and a recalibration of the growth trajectory. The broker, not one of the eight monitored daily on the FNArena database, has a Buy rating and $63 target.

Credit Suisse found the results disappointing because of lower performance fees and higher expenses. A miss on cost estimates reflects a higher cost profile going forward. Nevertheless, the broker concedes the outlook is more positive, as the company has upgraded its synergy target and this will add 2% to FY19 earnings per share.

Cost Synergies

Credit Suisse is concerned about costs and, relative to forecasts, suspects synergies are not flowing through to earnings as much as they should. There were US$70m in synergies achieved in the September quarter, mostly related to compensation, yet comparable growth was 14% and total cost growth 10%.

Consequently, the broker's earnings estimates are negatively affected by a mix of restated costs and/or lower net synergies. There is some valuation support relative to Australian managers but Credit Suisse suspects rising regulatory costs may still impose some risk.

This doesn't concern Morgan Stanley, which notes the synergy upgrade and positive flows ensued despite the limited tailwinds from cross selling into the new geographies that are being opened up by the global platform. Hence, the broker suggests there is a case for a re-rating and retains an Overweight recommendation.

Morgan Stanley considers the valuation compelling and will look for the catalysts that should start playing out now, such as improving flows, stronger investment performance, new products and delivering on cost synergies. The broker acknowledges the market is still forming its view on the merged entity but believes the risks are skewed to the upside.

Morgan Stanley is more confident that there will be a return to positive flows at the former Henderson retail funds as well as a better INTECH performance.

Citi acknowledges comparable expenses need to come down, and suggests that, with synergies and the outsourcing to BNP Paribas in the first quarter of 2018, expenses should fall. The broker notes management fee margins are continuing to climb because of a favourable mix.

Also, the rally in equity markets post September 30, if sustained, should be supportive. Citi had expected the synergy target would be upgraded, although this still remains shy of its US$130m estimate.

Dai-ichi

Morgan Stanley suspects the market is missing the fact the business is evolving into a truly global platform, supported by the company's relationship with Dai-ichi Life Insurance, and points out that a one-stop asset manager increases the relevance for larger clients that are reducing their asset manager panels.

Dai-ichi has publicly stated it intends to increase its stake in the company to at least 15% from the current 9% and Citi suggests there is a reasonable chance the stake will be raised in the current quarter.

The database shows four Buy ratings and two Hold. The consensus target is $51.47, suggesting 6.5% upside to the last share price.

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Xero Rally Doesn't Add Up For Brokers

Accounting software business Xero has rallied sharply in the year to date and most brokers believe the share price now exceeds valuation by a large measure.

-Overly optimistic assumptions suggested in the share price -Scale in North America required for ultimate success -Move to sole ASX listing unconventional, not expected to change valuation

By Eva Brocklehurst

Xero ((XRO)) posted a maiden positive earnings in the first half, although an unexpected decision to de-list from the NZ Stock Exchange in favour of a sole ASX listing is suspected behind a negative reaction in the share price, which fell -2% post the result. The company also suggested that after cash break-even is achieved, it will reinvest in growth. Strong subscriber growth in Australia and a continued ramp-up in the UK are the highlights of the results.

The company may be one of the fastest-growing software as a service (SaaS) businesses globally, with dominant positions in New Zealand and Australia, but the stock has appreciated by around 90% since the beginning of the year.

As a result UBS downgrades to Sell from Neutral. To justify valuations above NZ$35 requires overly optimistic assumptions on market share, in the broker's opinion, as well as a reduction in churn and acceleration in revenue growth. Macquarie agrees that an aggressive set of valuation assumptions is not enough to justify a positive stance on the stock, and downgrades to Underperform.

UBS expects momentum on the cloud to continue and translate into strong market share but this strength is likely to be shared with MYOB ((MYO)). Moreover, while growth off the base can accelerate and a sustainable presence be built, failure to do so quickly will pose difficult questions regarding investment.

Credit Suisse also downgrades, to Underperform from Neutral, and suggests the main question posed by recent strength in the share price is whether further upside can emerge in the near term and, on this subject, strategically, not much has changed. The company's dominant in Australasia and has a firm position in the UK, with technology advantages that can be monetised in time.

Nevertheless, the model is not completely de-risked and scale in North America is still required for ultimate success. While adopting more optimistic forecasts, Credit Suisse finds its valuation still well shy of the current share price and suspects the market is ascribing significant value to long-dated growth for which further evidence is required.

Citi remains focused on the longer term. The broker found core business trends solid, with a first half gross margin of 80.1% slightly above expectations amid better subscriber growth in Australasia. Mild share gains are envisaged versus competitor MYOB.

The broker continues to forecast positive free cash flow in FY19, a key inflection point for the stock, and removes its "High Risk" rating given ongoing improvements in the financial profile and ample cash. The broker remains attracted to the company's first mover dominance of cloud accounting in Australasia and the high growth outlook.

Customer Growth Preference

Citi suspects average revenue per unit growth is more of a story for FY19, as management has limited price increases given the new products being launched. Macquarie also notes the company's intention to pursue customer growth rather than near-term profits and suggests the cost to acquire each new customer is the number to focus on when reviewing the efficiency of sales and marketing expenditure.

The company has reduced its cash burn, moderating growth in product development investment over the past two years. Macquarie considers this aspect more important than whether the business is breaking even at the net profit level. The broker gives the company the benefit of the doubt and retains a strong growth outlook in its forecasts.

NZX

The company plans to remove its NZ Stock Exchange listing by the end of January 2018, stating this will focus all liquidity on one market and should make trading the shares easier. The company will move to a sole primary listing on the ASX as of February 5, arguing the ASX has a deeper pool of capital and expertise. Brokers were surprised by the decision, with Macquarie stating it is unconventional and perhaps should have been done after a formal poll was carried out.

Deutsche Bank suggests this is a significant loss to the NZX. Typically, when a company moves its listing, it creates some churn in the shareholder register. NZ-based individuals and institutions currently hold 37% of the shares and Xero now accounts for 3.5% of the benchmark NZX50 index.

Deutsche Bank does not expect the change of primary venue will result in a meaningful increase in valuation, with the stock already been priced consistently with valuations for other platforms. UBS points out that Xero will become an Australian listed company with an NZ domicile and NZ dollar reporting, and remains sceptical there is a valuation arbitrage based on location or size of the primary listing exchange.

There are three Sell ratings now on FNArena's database versus none prior to Xero's results. There is one Hold remaining (Deutsche Bank) and one Buy (Citi).

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Iress Susceptible To De-Rating

Citing a delay in the timing of client decisions, Iress has downgraded 2017 guidance. Brokers are somewhat underwhelmed by the outlook.

-Downgrade not driven by a single project or region -Susceptible to de-rating, hence needs to deliver on 2018 growth forecasts -Returns from acquisitions failing to live up to expectations

By Eva Brocklehurst

Financial services business Iress ((IRE)) has downgraded guidance, acknowledging two recently-acquired businesses are performing below expectations. The company, citing a delay in the timing of client decisions and an increase in its cost base, has revised 2017 revenue guidance to $435-440m, which implies 12-13% growth and, at the mid point, suggests a -6% downgrade to consensus forecasts.

Iress has indicated the downgrade is not driven by one project or one region, although cited delays in South Africa and lower consulting revenue in Australia.

The company has signalled Financial Synergy & INET are performing below expectations. This is consistent with Deutsche Bank's concerns that Financial Synergy retains a much higher level of project revenues that the company's core business, exposing Iress to higher earnings volatility.

CLSA believes the underwhelming first half result obscured a solid top line in key markets, and remains confident the company can further penetrate the UK market and continue top-line growth in 2018, delivering both margin expansion and earnings growth. CLSA, not one of the eight stockbrokers monitored daily on the FNArena database, has a Buy rating and $14.20 target.

The delays raise some questions for Credit Suisse. The company has consistently indicated that results can be affected by timing and this is particularly the case in the UK, which is growing off a smaller market share base than in Australia.

Hence the broker believes it is prudent to wait and see as, following a weak first half, there is less second half growth than previously hoped. The broker gives the company the benefit of the doubt, expecting growth rates will improve in 2018.

Ord Minnett notes cost growth ran ahead of revenue in the first half, as management indicated some of this was required for the execution of key projects. This was expected to reverse in the second half as revenue came online and cost normalised.

Macquarie calculates revenue guidance would be $10-15m lower if the impact of foreign exchange is included. The main impact in terms of FX is from an adverse movement in the AUD:GBP. Recent changes to segment disclosures make it more difficult for the broker to estimate the impact on segment profit, which the company has indicated would be between $123-128m, implying just 2% growth.

Downside Risks

The broker considers the stock susceptible to a de-rating, as it has missed consensus expectations on two consecutive occasions and recent acquisitions appear to be delivering below expectations. Macquarie asserts, in order for the company to maintain its premium rating relative to the market, it will need to deliver on earnings and revenue growth in 2018.

Although management signalled the majority of the weakness is attributable to timing, Deutsche Bank believes weak underlying momentum, combined with an increased reliance on (lower quality) acquisitions, increases the downside risks. The stock is a high quality business but this is reflected in current pricing, in the broker's opinion.

Over the past seven years the company has deployed more than $600m on acquisitions and Ord Minnett suggests the returns from the businesses are failing to live up to expectations.

Assuming only a flat contribution from existing business since 2010, the broker estimates capital deployed appears to be generating a pre-tax return of only 6%. The broker maintains a Lighten rating, awaiting signs of a sustained recovery in profitability.

FNArena's database shows three Hold ratings and one Sell (Ord Minnett). The consensus target is $11.20, suggesting 2.3% upside to the last share price. This compares with $12.49 ahead of the update.

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

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Brokers Not All Keen On Computershare

Computershare has upgraded guidance, attributing a lift in performance to a stronger contribution from corporate actions in mortgage services. Brokers have taken this in their stride.

-Supported by potential for US tax cuts and tailwinds from rate rises in the northern hemisphere -Several brokers consider the stock's premium to the market difficult to justify -Discrepancy with DealLogic market data

By Eva Brocklehurst

Computershare ((CPU)) has confirmed the suspicions of several brokers that original guidance provided at the FY17 result was conservative. Four months into the first half, the company now expects management earnings will be up 10% in constant currency terms. This compares with prior guidance of 7.5%. The lift in performance is attributed to stronger contributions from corporate actions and mortgage services.

UBS believes the company is executing well and its cost reduction programs and capital management are all delivering, as macro tailwinds from rate rises in the northern hemisphere also begin to emerge. Nevertheless, growth prospects in the medium term are expected to be more modest as these drivers fade.

Initial guidance was always likely to be conservative, Morgans suggests, given benefits from cost reductions and recent acquisitions that flowed into FY18. The broker notes commentary regarding a good start for corporate actions activity is similar to that of peer Link Administration ((LNK)).

Morgans likes the fact management is taking a cautious approach to setting expectations after a long period where downside risk were underestimated. That said, the broker believes the stock is now closer to fair value and maintains a Hold rating.

CLSA was expecting guidance to be upgraded at the first half result but coming earlier than expected, confidence in the underlying momentum of the business has improved. The broker still suspects the company is maintaining a conservative outlook, with further leverage to increases in global interest rates and potential for US tax reform. CLSA, not one of the eight stockbrokers monitored daily on the FNArena database, has an Outperform rating and $17.25 target.

The company has indicated it will be unlikely to buy back shares between January 1 and the payment of the interim dividend in mid March 2018. Computershare will then state the full value of franking credits that are available. Cost reductions are on track with a US$42m cumulative run rate expected by the end of FY18.

Hence, Citi envisages significant upside from further cost reductions, but does not yet allow for this in forecasts. The broker believes that the rally since the company's FY17 result has already incorporated the potential for further upside from US tax cuts and higher interest rates.

Ord Minnett defends the latest guidance, believing it is being driven by the outcome of the first four months of FY18 as opposed to any changes to underlying assumptions. Trends are encouraging and the broker agrees there is potential from an uptick in global interest rates, possible change in US tax rates, and accretive acquisitions.

Corporate Actions

While the company has experienced stronger contributions from corporate actions, using DealLogic data to measure this activity, Deutsche Bank finds activity is down -36% in the company's core markets. To some extent, the broker considers the discrepancy could be explained by some FY17 transactions closing into the first quarter of FY18, and favourable outcomes for clients of Computershare in the deals that have occurred.

Overall, Deutsche Bank retains a cautious stance, given a weak pipeline of deals to be completed over the next six months. The broker retains a Sell rating, with a view that mortgage servicing margins are likely to disappoint over the medium term.

UBS also finds corporate actions revenue at odds with industry data but notes the monthly average value of deals over the first four months of the first half is up 8% versus a particularly weak prior second half period.

In analysing the data Macquarie notes that IPO and M&A activity in recent months was subdued, which signals that while corporate actions revenue improved, mortgage services was the larger contributor to the company's upgrade.

Mortgage Servicing

In mortgage servicing the company expects to generate a 20% pre-tax margin and a 12-14% post-tax cash flow return. Deutsche Bank believes the operating leverage in this business is significantly lower than the guidance. The broker is forecasting 7% pre-tax margins at scale for this division. This margin assumption explains the bulk of the broker's difference with consensus forecasts over the medium term.

Macquarie suspects margin income has supported earnings in recent months and would have provided the additional confidence to upgrade. Still the broker considers the current premium to the market is difficult to justify in the absence of further upgrades.

FNArena's database shows one Buy (Credit Suisse, yet to comment on the update), five Hold and two Sell ratings. The consensus target is $14.28, signalling -10.9% downside to the last share price. This compares with $13.89 ahead of the update. Targets range from $11.50 (Morgan Stanley, yet to comment on the update) to $16.00 (Citi).

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Incitec Pivot Could Stall In FY18

Incitec Pivot has started FY18 from a strong position, as fertiliser prices have improved, the Australian dollar is weaker and the outlook for the US explosives market is buoyant. But brokers are not convinced.

-Strong cash flow the main positive, $300m buyback announced -Gibson Island facing potential closure in 2018/19 -Upside to spot fertiliser prices seen largely factored into share price

By Eva Brocklehurst

FY17 results for Incitec Pivot ((IPL)) were characterised by improved operating rates and market conditions. Volume growth in the Americas explosives division was strong, up 11%, and broadly based across quarry & construction as well as in metals and coal. Q&C accounted for 35% of the Americas explosives revenue in FY17.

A recovery in coal and metals was evident in Asia Pacific. The company cited a -$26m impact from lost production because of the turnaround at Moranbah as well as weather-related events. Asia Pacific fertiliser results included a $19.8m gain on asset sales.

Morgans notes FY18 guidance was not specific but management's outlook is cautiously optimistic and the stock appears fairly valued in the absence of a further appreciation of fertiliser prices.

Strong cash flow was the main positive for brokers, along with reduced capital expenditure requirements as the WALA plant in Louisiana is now up and running well. Hence, the company has announced the much-anticipated $300m share buyback, generally estimated to be around 5% accretive.

Morgans forecasts net profit in FY19 to be relatively flat, assuming Gibson Island is closed because of uneconomical gas prices and US ammonia earnings slide because of a plant shutdown.

Gibson Island plant faces potential closure in 2018/19 but this is a well-known risk in Macquarie's view, although it remains the major strategic/financial issue facing the new CEO over the next 6 to 9 months. The broker finds some heat coming out of the global urea markets after the Indian tender was cancelled but ammonia still appears cheap versus urea at current prices.

CLSA suggests that while FY17 results produced an increase in operating earnings of 17%, this includes items such as volume growth in US explosives and a $20m gas saving at Phosphate Hill, which are variable elements that may be greater than first appear. CLSA expects production of ammonia in Russia to start ramping up and stem a price recovery.

On the other hand, Deutsche Bank believes the company is well-positioned to benefit from improving demand for explosives in North America and Australia as well as from the recent increase in global fertiliser prices and depreciation of the Australian dollar.

Productivity offset the difficult fertiliser market conditions and the buyback should provide some support for the share price. That said, Credit Suisse considers the stock expensive in a market for fertiliser that is likely to weaken in FY18. The broker expects fertiliser prices to weaken throughout 2018 before supply begins to tighten thereafter.

Credit Suisse downgrades to Underperform from Neutral, following the rally in the share price. The broker asserts that the natural inclination of an incoming CEO to reset any deficiencies in the cost base means some conservatism might be warranted in near-term forecasts.

Credit Suisse found it interesting that the company did not call out US domestic steel production as a significant input for FY18, despite the continued recovery expected in that sector.

Buyback

CLSA, not one of the eight stockbrokers monitored daily on the FNArena database, has an Underperform rating and $3.80 target. The broker remains sceptical about the benefits to shareholders of the buyback, estimating accretion is less than 1%, although being small is unlikely to compromise any growth strategies that may be formulated over the next six months.

The strategic direction under a new CEO remains to be seen and, while the buyback will provide technical support, the broker believes exposure to volatile commodities with a high forecasting margin for error has not changed. The risk is that these do not support an upgrade cycle.

The capital management initiative arrived earlier than Citi expected. As near-term markets remain tight and WALA ramps up to full capacity, spot prices imply further upside risks to FY18 estimates. That said, the broker believes much of the price recovery is already priced in.

Morgan Stanley also suspects the earnings trajectory is likely to disappoint. Earnings from explosives have failed to pace volume growth so far and there is little evidence to the broker of underlying leverage in operations. While the company should benefit from the recent rally in fertiliser prices, Morgan Stanley envisages downside risk to spot prices over the near-term. The broker, therefore, struggles to find valuation support above current levels.

FNArena's database shows three Buy ratings, three Hold and one Sell (Credit Suisse). The consensus target is $3.91, signalling -0.5% downside to the last share price. Targets range from $3.49 to $4.22.

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Pact Group Asian Expansion Not Without Risk

Packaging business Pact Group has signalled growth is heading in the right direction, as it acquires two major packaging operations in Asia and a bulk containers reconditioning business in WA.

-Stronger second half to be driven by full contribution from recent expansion/acquisitions -Asia could be an important source of profit in the short term and its percentage of group revenue should rise significantly -To narrow the discount to peers, Macquarie suggests Pact's top-line growth needs to be sustainable

By Eva Brocklehurst

Pact Group ((PGH)) has reiterated expectations for underlying earnings growth in the year ahead and announced the acquisition of major packaging businesses in Asia. The company has some early indications that organic growth is heading in the right direction, despite a slow start to the New Zealand dairy season.

Meanwhile, recent acquisitions and the Woolworths ((WOW)) crate pooling contract are performing to expectations, although energy costs have increased significantly. Morgans points out that the company has had to invest in efficiency programs to mitigate these costs while the company expects a positive $5-7m impact from its operational excellence program in FY18 should be of some help in overcoming rising energy costs and contract extensions.

Management now expects first half operating earnings to be broadly in line with the prior corresponding half, followed by a stronger second half that will be driven by the full contribution from recent acquisitions and crate pooling.

The latest acquisitions include the Asian packaging operations, ex Japan, of Closure Systems International (CSI Asia) and Graham Packaging Co (GPC Asia) from Reynolds Packaging for $142m. While there is potential for growth in Asia relative to more developed areas, brokers note this also comes with higher risk.

Macquarie was expecting FY18 to be a year of consolidation as the company has a number of recent expansions in terms of RPC and contract manufacturing to absorb. Hence, the latest acquisitions increase execution risk, given expansion is occurring on a number of fronts and in multiple geographies.

In the company's favour the broker notes there is a good long-term track record in relation to acquisitions. Macquarie calculates the Asian acquisitions have below-average margins at 12.6% for operating earnings (EBITDA) relative to the group average of 16% in FY17 but there should be an opportunity to improve the former over time.

The company will also acquire ECP Industries for $11.7m, a Western Australian intermediate bulk containers reconditioning business, which operates two sites, and believes this is an attractive entry point for this market.

CLSA believes the acquisitions will put to rest concerns that a stretched balance sheet is undermining the growth strategy. However, to meet forecasts still requires a robust second half. Although the businesses being acquired in Asia are likely to operate in markets that are relatively low growth, CLSA believes they will be an important source of profit for the company in the short term.

Given the critical mass the company will now enjoy in Asia, Asian revenues should rise to around $200m from around $50m currently, or to 12% of group sales from 3%. CLSA, not one of the eight stockbrokers monitored daily on the FNArena database, has an Outperform rating and $6.20 target.

Deutsche Bank considers the Asian acquisitions slightly positive and the synergies reasonable, estimating the company will generate a pre-tax return on capital of 11.2% on the acquisitions. Macquarie finds the valuation undemanding, but in order to close the discount to peers Orora ((ORA)) and Amcor ((AMC)) the company needs to demonstrate a sustainable return to positive top-line growth.

Asian Acquisitions

The Asian platforms are regional leaders in supplying plastic closures and plastic bottles to blue-chip customers in the carbonated soft drinks and health supplements/nutrition industries in Asia. CSI Asia features plastic closures design and manufacturing, with high-speed capping equipment/applications.

GPC Asia produces plastic bottles via injection and extrusion blow moulding using HDPE. The businesses encompass seven manufacturing sites across China, South Korea, Nepal, India and the Philippines.

The acquisitions will be funded via a fully underwritten, 1-for-9 non-renounceable entitlement offer at $5.28 a share to raise $176m. Major shareholder Kin Group and related entities have committed to take up the full entitlement of 39.3% of the offer. Net proceeds will be used to fund the acquisitions, cover costs and provide flexiblity for further investment in growth.

FNArena's database shows five Hold ratings and one Buy (Deutsche Bank). The consensus target is $5.78, signalling -0.5% downside to the last share price.

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Costa Firing But Well Priced

Brokers are unsurprised by a guidance upgrade from fruit&veg producer Costa Group and believe the market is already way ahead.

- Big profit growth upgrade - Largely acquisition driven - Opportunities attractive - Share price is not

By Greg Peel

Fruit & vegetable producer/wholesaler Costa Group ((CGC)) held its AGM yesterday and took the opportunity to upgrade FY18 profit growth guidance to 20% from 10% previously. The upgrade appears material but is largely attributable to Costa recently increasing its stake in Moroccan blueberry producer African Blue to 90%.

Excluding this contribution, Ord Minnett (white-labelling research from JP Morgan) calculates only a 4-5% increase in organic growth guidance. That said, the broker still considers 20% growth to be conservative, given its own forecasts imply 32%. Earnings momentum is strong and Costa offers attractive long term opportunities.

UBS had similarly set a forecast of 30% profit growth and agrees Costa offers significant opportunities in both the near and longer terms.

Not to be left out, Macquarie is forecasting 27%, with 12% represented by African Blue, but sees further upside risk to guidance as the year progresses. Ord Minnett concurs, noting a large earnings skew to the second half is expected this year, of 32/68% by the broker's estimates.

I found my thrill

Export protocol still needs to be out in place, but the Australian government has taken a significant step, Macquarie points out, in placing blueberries on the horticultural market access priority list for negotiation with China. Success would provide both advantages and disadvantages for Costa.

Access to China would be provided for any Australian blueberry producer, Macquarie notes, making Costa's Chinese operations less of a prestige. However, given Costa is by far the largest and most technologically advanced producer, offering superior berries, the broker believes Costa can supply quality berries at a lower cost.

At the AGM management suggested initial Chinese demand has been very promising, with the Chinese showing a preference for high quality, larger sized fruit.

Priced to Perfection

Costa's acquisition drive is not yet over, with avocados offering a potential next step. Brokers agree there's not a lot not to like about the stock, but none of the positives have been lost on the market. On Ord Minnett's estimates, the market is pricing at PEs of 27x for FY18 and 26x for FY19. The company's guidance upgrade was more catch-up than revelation.

UBS believes the upside story is well priced in, leaving little room for error.

Investors should be mindful of the fact Costa is an agricultural producer, brokers point out, thus subject to same vagaries of seasonal and weather-related risks as any farming operation. The company, like everyone else, is also looking at substantial increases in power costs going forward.

UBS has pulled back to Neutral from Buy, lifting its target to $6.80 from $5.70.

Ords has raised its target to $6.43 from $5.01, and already had a Hold rating.

Macquarie still believes there is enough in there to continue backing the stock, and had already set a target of $7.00 prior to the guidance upgrade. The broker has retained that target and an Outperform rating.

That leaves the consensus target among the three FNArena database brokers covering the stock at $6.74, or a mere 0.8% above the current trading price.

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Santos Takeover Far From Certain

The market is abuzz with speculation regarding a bid for Santos but brokers suggest progress on any offer would be difficult and success highly uncertain.

-Suggested offer price considered low in context of valuation -Potential issues may arise from FIRB -Hony/ENN need to be factored into the prospect

By Eva Brocklehurst

Speculation has filled the void on Santos ((STO)) as the market reacts to press reports that a new bid is about to be forthcoming from Harbour Energy. A cash bid of $5.30 a share is purportedly to be offered in coming weeks.

If it eventuates, the bid would represent a 13% premium to Citi's risked discounted cash flow valuation and imply a US$65/bbl oil price on average. Such a bid is similarly priced to a previous one from Scepter Partners in 2015 at $6.88 a share, which Santos rejected.

However, brokers suggest a deal is now significantly more difficult following the leak of any "preparation" to media, as the share price closed 13% above the level prior to the report. Santos has stated that it is not currently engaged in talks with Harbour Energy but did reject an approach by the private equity consortium in August, at $4.55 a share, on the basis that the indicative price was inadequate and sources of funds uncertain.

Coinciding with the speculation, Santos hosted a three-day visit to the Cooper Basin, Roma and Curtis Island. The main message Citi received from this tour is that the company's culture has changed and the focus is on reducing costs, growing production and improving efficiencies. The broker also found none of the disappointments that have usually accompanied such trips, which supports confidence in a turnaround for the company.

For now, Citi remains cautious about a bid proceeding, calculating a blue-sky value of $6.47 a share from de-risking growth and delivering on further cost reductions, although conceding this is likely to be a multi-year process. This value is conceived at a long-term oil price of US$55/bbl.

Deutsche Bank considers the indicative offer price low in the context of its valuation assessment, which implies a 2% control premium. The main issue for the broker in a transaction of this nature is the Foreign Investment Review Board (FIRB) approval. The FIRB, because of the significant domestic gas assets - these being the Cooper Basin, Western Australia, GLNG and Darwin LNG - would be involved.

The significant turnaround in the company has meant impressive cost reductions and a strengthened balance sheet, supporting Deutsche Bank's Buy rating. The exploration program planned for 2018 is also underpinning solid growth prospects in the Cooper Basin and GLNG.

UBS considers the plum in the Santos portfolio is the company's 13.5% stake in PNG LNG and notes that Total and Woodside Petroleum ((WPL)) have, historically, had an interesting acquiring a stake in this asset. PNG LNG represents 51% of the Santos net asset value. There is large uncertainty around the value of GLNG and the Cooper Basin but UBS acknowledges market sentiment towards these assets is improving.

If nothing else, Credit Suisse suggests Harbour Energy is a credible entity, noting a recent US$3bn acquisition of the Shell North Sea assets. Amid the speculation the broker is left wondering what potential issues may arise from an FIRB perspective. Particularly, given the state of the east coast gas market, what would be the government's view of the operator of both the Cooper Basin and GLNG being acquired by a relatively unknown, foreign entity?

A higher price is needed for Credit Suisse to be happy with the bid. The broker's oil price deck averages around US$54/bbl for the next 18 months so there is scope for upside and, if Santos truly believes in its growth opportunities, there is also scope for considerable de-risking of the valuation. In the broker's calculation at least a 30% premium to valuation is required for serious discussions to occur. So, at around $6.50 a share.

Hony/ENN

An important part of any bid scenario are Hony and ENN, with which Santos entered a strategic relationship in June this year. ENN is expected to be using Santos as its primary investment vehicle in upstream Australasian oil & gas. Collectively the two own 15.1% of the company.

The stake is important as Hony/ENN can counter offer if they so choose. Under a scheme of arrangement, however, 15.1% is not a blocking stake. Deutsche Bank points out that the board is also able to exclude ENN/Hony from any third party offers.

What is Harbour Energy?

Harbour Energy is an investment vehicle managed by US private equity firm EIG, designed to take controlling positions in upstream and midstream companies. Harbour Energy is run by former Shell Power & Gas CEO Linda Cook. The fund is backed mainly by large US pension and sovereign wealth funds. EIG has had a long presence in Australia particularly in Queensland CSG, previously partnering with QGC and, more recently, Senex Energy ((SXY)).

FNArena's database shows four Buy ratings, two Hold and one Sell (UBS) . The consensus target is $4.69, signalling -7.9% downside to the last share price.

Find out why FNArena subscribers like the service so much: "Your Feedback (Thank You)" - Warning this story contains unashamedly positive feedback on the service provided.

Material Matters: China, Alcoa, Oil & Nickel

A glance through the latest expert views and predictions about commodities. China; Alcoa; crude; and nickel.

-Low confidence in demand outlook for steel in China -Analysts doubt sustainability of high alumina margins -Oil prices expected to be well supported in the near term -Stainless steel still the main driver of nickel performance

By Eva Brocklehurst

China

After a visit to China ahead of the winter production reductions for steelmakers, Morgan Stanley observes low confidence in the demand outlook has deterred a build-up in inventory. A re-start of 20-30mt of old electric arc furnace capacity and increased usage of scrap are further bearish points.

The price of iron ore is also expected to weaken as a result. The broker notes both mills and smelters are complying with the winter reductions, confident in the government's capacity to enforce restrictions. Winter maintenance has been rescheduled to coincide with the cuts at aluminium smelters.

The aluminium smelters are arguing that energy consumed to re-start operations offsets the savings gained by the restrictions and are lobbying the government, so Morgan Stanley suggests it remains to be seen what will occur next winter. The shortfall of carbon is seen as a short-term issue, as induction furnaces owners turn to carbon production.

The price hike in alumina is widely believed to be driven by speculators, although both the quality and quantity of Chinese domestic bauxite has declined. Morgan Stanley also met with battery makers preparing to begin mass production of NMC 811 by 2019-20 and notes Chinese domestic lithium supply is improving in both quantity and quality, reducing dependence on imports.

Alcoa

Deutsche Bank held discussions with Alcoa management that centred on the sustainability of Chinese curtailments affecting the global supply chain, as well as the company's capital allocation as free cash flow rises. The broker is more confident in Alcoa's ability to generate free cash flow and, as de-leveraging plays out, valuation should re-rate upwards to the peer group average.

Prices have surged for aluminium and alumina, Deutsche Bank notes, as inventory is ostensibly built up heading into the seasonal capacity shutdowns in China. However, other input costs to aluminium smelting have also risen, such as pitch, carbon and anodes because of some unintended consequences of the permanent capacity closures for both environmental and other grounds.

Hence, the broker suggests the cost-push of higher raw material alumina should theoretically support higher global aluminium pricing.

Deutsche Bank notes that with alumina cash margins well above normal levels, many analysts doubt the sustainability of what is considered to be a "made in China" situation. Given Alcoa is net long alumina, current spot prices, if held constant for 2018, could imply US$934m of incremental operating earnings, or around 37% upside to the broker's 2018 estimates for the company. Similarly, spot aluminium could lead to 5% upside to 2018 estimates.

Crude

ANZ analysts suggest the likelihood of the disruption to oil supply, after the arrests of dozens of government officials in Saudi Arabia, remains low. Still, they believe the events raise the possibility of the country taking a more aggressive stance on production cuts. The risks now lie with curbs remaining in place for longer than expected. Hence, the analysts expect oil prices will be well supported in the short term.

The Crown Prince Mohammed bin Salman is intent on restructuring the economy to be less reliant on oil but significant challenges have arisen as the country's fiscal position deteriorates since the era of US$100/bbl oil ended in 2014. This suggests the prospect of prices falling back below US$50/bbl is unpalatable for Saudi Arabia.

The analysts believe the government would rather over-tighten the market than risk prices falling again. They envisage a heightened probability that a staged approach is taken to the phasing out of the production reduction agreement once it expires. A gradual and more disciplined return to normal production levels would take some risk out of the market over the next 18 months.

Nickel

Nickel prices have staged a remarkable recovery over the past month, Macquarie observes. Although copper, zinc and aluminium remain the best performers among the base metals over 12 months, nickel is catching up. The broker is optimistic about the prospects in coming years but remains cautious about the near-term, because of an ongoing correction in Chinese stainless steel production and a surge in Chinese and Indonesian nickel pig iron production.

While the use of nickel in lithium ion batteries for electric vehicles is rapidly growing as an end use it is still a relatively small application, and Macquarie finds it difficult to believe that this has been the driver of nickel's performance. Primary nickel use in lithium ion batteries for electric vehicles accounted for no more than 10-15,000t of nickel last year and has probably grown to 20-30,000t this year, which is still just over 1% of the total market.

The stainless steel market, in contrast, accounts for over 70% of nickel demand. Also of note, Macquarie ascertains, is significant losses to production from the main nickel producers because of mine and refinery closures. Over the past two years, the broker estimates closures of mines, smelters and refineries have taken over 200,000t of supply from the market.

Meanwhile, the broker estimates, conservatively, China's apparent consumption of stainless steel rose 24% in the September quarter to 6.5mt. Combined, these factors signal why nickel prices have been so strong but also raise fears of a correction in demand before the end of the year.

There are reports from China indicating that stainless mills are losing money at current prices and some are already cutting production. Macquarie observes history shows that two good years are often followed by a slower year. For 2018 the broker is forecasting global growth of 2.2% for stainless steel, versus 5% this year and 8.4% last year.

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 November 6 to Friday November 10, 2017 Total Upgrades: 11 Total Downgrades: 12 Net Ratings Breakdown: Buy 41.40%; Hold 43.08%; Sell 15.52%

The strong rally in Australian share prices that started on October 1st has received no support from the local stockbroking research community, other than maybe for miners and energy stocks through increased forecasts. When it comes to price targets and recommendations for individual ASX-listed stocks, however, investors and traders are pretty much left on their own.

The week ending Friday, 10th November 2017, proved no exception. FNArena counted 12 downgrades versus 11 upgrades. Positive news and/or valuation support for stocks like Costa Group, EclipX, Janus Henderson and Magellan Financial was countered by disappointing market updates, but in particular by stretched valuations which are triggering downgrades for companies including Santos (2x), Orica, Xero and, yes, Westpac.

CommBank received both one upgrade to Neutral and one downgrade to Neutral.

Altium, Virgin Australia and Platinum Asset Management all enjoyed target price increases of more than 8%, followed by James Hardie, Downer EDI, Eclipx, Costa Group and Santos which all saw target price increases of at least 5%. Nothing wrong with momentum here, but in most cases it's already in the share price.

The table for negative revisions to target looks a lot more subdued with Sims Metal on top with a -5% reduction, but things get a lot more benign from the second spot onwards.

There is no shortage on positive revisions to profit estimates either, with long suffering Perseus Mining grabbing top spot, followed by EclipX, BT Investment, Virgin Australia, Costa Group, and others. Note the small representation by miners and energy stocks.

On the negative side, we find Janus Henderson, Syrah Resources, Ardent Leisure, National Australia Bank and Orica with noticeable reductions.

AGM season is heating up in Australia and investors can look forward to more results from out-of-season reporters. With a small number of exceptions, it hasn't been great, extending the general feel that also dominated the season in August.

Upgrade

COMMONWEALTH BANK OF AUSTRALIA ((CBA)) Upgrade to Neutral from Sell by Citi .B/H/S: 0/7/1

The Q1 update was better than expected and Citi has pushed up its rating to Neutral from Sell. Target is raised to $76.75 from $76.50.

The analysts are now of the view Australia's number one bank looks to be in good shape, with enough capital momentum to absorb any likely penalty.

See also CBA downgrade.

COSTA GROUP HOLDINGS LIMITED ((CGC)) Upgrade to Outperform from Neutral by Macquarie .B/H/S: 2/1/0

The company will lift its shareholding of African Blue to 90% from 49%. A payment of $68m for the initial 37% share increase will be paid and the remaining 4% is dependent on actual earnings achieved.

Macquarie expects this Moroccan transaction to heighten the chance of an upgrade at the AGM. Costa has previously guided for 10% growth in underlying net profit in FY18.

Macquarie upgrades to Outperform from Neutral. Target is raised to $7.00 from $6.14.

ECLIPX GROUP LIMITED ((ECX)) Upgrade to Buy from Neutral by Citi .B/H/S: 6/0/0

Citi notes the company continues to transform into a diversified financial services business, growing its B2B and B2C platforms.

One lingering concern is that the diversification impresses complexity and reduced visibility. The broker upgrades to Buy from Neutral and increases the target to $4.82 from $4.25.

JB HI-FI LIMITED ((JBH)) Upgrade to Hold from Lighten by Ord Minnett .B/H/S: 1/5/2

Ord Minnett retains concerns regarding the health of the consumer sector and the negative impact of Amazon. Nonetheless, there are emerging signs that, while consumer sentiment will likely remain subdued, wage growth could improve.

The broker is also more confident that the company has attributes which provide some support that is yet to be fully reflected in the share price. Rating is upgraded to Hold from Lighten. Target is raised to $23.00 from $22.50.

JANUS HENDERSON GROUP PLC. ((JHG)) Upgrade to Buy from Neutral by Citi .B/H/S: 4/1/0

It appears earnings missed expectations in the trading update but Citi analysts are of the view the combination of better flows and the strong performance of equity markets at present offers plenty of compensation.

In addition, targeted merger synergies have been lifted to US$125m (still below Citi's forecast of US$130m) by management and the analysts assume the market will see this as a positive.

Citi sees Janus Henderson offering superior EPS growth vis-a-vis peers. Upgrade to Buy from Neutral. Target price lifts to US$39, which converts to $50.75 for Australian investors.

JAMES HARDIE INDUSTRIES N.V. ((JHX)) Upgrade to Buy from Neutral by Citi .B/H/S: 4/2/0

Citi analysts have decided to grant James Hardie the benefit of the doubt. The EBIT margin surprised in the face of cost headwinds, but competitors have been reporting solid volume growth, point out the analysts.

If the stars align this year, this company's margin may well surprise to the upside in FY19, suggest the analysts. Rating upgraded to Buy from Neutral. Target price lifts to $23 from $20.10.

Also, Citi reminds investors Fermacell was offered and declined back in 2008. This year the response was "yes", but execution remains key.

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

Morgans upgrades to Add from Hold because of a recent fall in the share price.

The broker expects the company to continue to signup significant new customers for its Talent Community in coming months. No change to forecasts or $1.10 target are made.

MAGELLAN FINANCIAL GROUP LIMITED ((MFG)) Upgrade to Outperform from Neutral by Credit Suisse .B/H/S: 2/4/0

Funds under management at the end of October were up 8.6%. The strong growth was driven by both positive market movements and net inflows.

The strong market movements were significantly ahead of Credit Suisse assumptions, leading to upgrades of 4% to funds under management.

Rating is upgraded to Outperform from Neutral. Target is raised to $28.25 from $27.00.

PLATINUM ASSET MANAGEMENT LIMITED ((PTM)) Upgrade to Neutral from Underperform by Credit Suisse .B/H/S: 0/1/3

Credit Suisse observes growth in funds under management appears to be particularly strong, with unit prices for the international fund indicating a rise of 6.9% in October.

Both this fund and the Asia fund, which rose 8.9%, are ahead of the broker's normalised growth assumptions.

While the broker considers the trading multiple slightly stretched, the rebound in fund performance could lead to higher net flows and performance fees. Rating is upgraded to Neutral from Underperform. Target rises to $7.00 from $5.90.

SUPER RETAIL GROUP LIMITED ((SUL)) Upgrade to Hold from Lighten by Ord Minnett .B/H/S: 6/1/1

Ord Minnett retains concerns regarding the health of the consumer sector and the negative impact of Amazon. Nonetheless, there are emerging signs that, while consumer sentiment will likely remain subdued, wage growth could improve.

The broker is also more confident that the company has attributes which provide some support that is yet to be fully reflected in the share price. Rating is upgraded to Hold from Lighten. Target is unchanged at $8.

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

Credit Suisse observes capacity discipline appears to be resuming in the domestic airline market. The broker expects a rational approach to continue until the Virgin Australia balance sheet is solid.

No decision on privatisation has been reached. The broker ascribes a two third probability to a privatisation outcome and upgrades to Outperform from Neutral. Target is raised to $0.26 from $0.20.

Downgrade

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

Credit Suisse has downgraded to Neutral from Outperform while bumping up its price target to $12 from $9.50. The analysts explain the downgrade has been inspired by the incredibly strong share price rally in recent weeks.

The analysts believe investors are already pricing in some modest growth contribution from the Dassault partnership.

Price target has been positively impacted by weaker AUD, lower discount rate and modest increases to long-term earnings, explain the analysts. They struggle to justify the current premium.

COMMONWEALTH BANK OF AUSTRALIA ((CBA)) Downgrade to Hold from Add by Morgans .B/H/S: 0/7/1

CBA's result showed an expansion in net interest margin despite the drag from the levy. Morgans has nevertheless reduced forecast earnings due to subdued loan growth.

Capital stood at 10.1% at the end of the period. The sale of the life business will provide a boost but as the bank faces a possibly hefty fine post the Austrac investigation, "a cynic might suggest", to use the broker's words, the bank is deliberately slowing loan growth in order to reach APRA's 10.5% requirement.

$80 target retained, downgrade to Hold.

See also CBA upgrade.

COCHLEAR LIMITED ((COH)) Downgrade to Sell from Neutral by Citi .B/H/S: 0/3/3

Citi analysts agree with the market's view there is ongoing upside bias to this year's profit outlook, but the share price is simply too high.

Hence the downgrade to Sell from Neutral, justified as "due to sky high valuation". Citi highlights there are some risks still, and these are currently not accounted for in the share price rally.

Price target lifts to $160 from $155.

INGHAMS GROUP LIMITED ((ING)) Downgrade to Neutral from Buy by Citi .B/H/S: 4/2/0

Citi is now anticipating weaker poultry volume growth over the next 12 months supported by the view that red meat seems poised to take back market share from poultry given lower prices for red meat.

On that basis earnings estimates have been pared back by -1-2% and the rating has been pulled back to Neutral from Buy. Target price drops -10c to $3.65.

The company is also facing higher feed costs but Citi points out due to hedging the impact won't be felt until nine months into the future.

MACQUARIE ATLAS ROADS GROUP ((MQA)) Downgrade to Hold from Add by Morgans .B/H/S: 1/4/0

Following Mac Atlas' solid share price run, Morgans now pulls back to Hold, while noting this week's APRR bond issue suggests the fund will be able to continue to access cheaper funding through to 2019.

The next catalyst will be the French CPI result, which determines APRR toll increases. Target rises to $6.27 from $6.13.

MURRAY RIVER ORGANICS GROUP LIMITED ((MRG)) Downgrade to Hold from Add by Morgans .B/H/S: 0/1/0

The difficult FY17 season has taken its toll on Murray River. Following a stocktake, the company will write-down -$4.3m of the value of its inventory. Morgans understands high-priced clusters suffered quality issues due to the weather and other factors.

The result is a material reduction in the broker's forecast earnings and a more conservative view going forward. Downgrade to Hold. On the positive side, an ex-Costa Group COO will take over as CEO. Target rises to 45c from 43c.

ORICA LIMITED ((ORI)) Downgrade to Sell from Neutral by Citi .B/H/S: 0/5/3

"Running hard to stand still" and "more downside risk in the near term" easily explain why Citi has elected to downgrade to Sell from Neutral. The stock is trading at a 10% premium versus the broader market as investors have been anticipating a recovery in profits, but Citi is not on board.

Forecasts have been cut by -13.5% in FY18 and -6% in FY19 after what is labeled a disappointing FY17 report. Citi thinks ammonium nitrate (AN) will be pushed into surplus in Western Australia from the moment the Burrup AN plant will ramp up.

Citi sees AN not rebalancing until FY20. Incitec Pivot ((IPL)) is preferred. Target drops to $17.

SOUTH32 LIMITED ((S32)) Downgrade to Sell from Hold by Deutsche Bank .B/H/S: 2/5/1

South32 has highlighted additional cost inflation going forward from rising input prices, commodity price-linked contracts and the A$. Deutsche Bank believes costs could rise by as much as 20% in FY18, cutting earnings by -15%.

Meanwhile, the market is valuing the stock based on spot commodity prices and A$ at current levels through to end-FY19, yet the broker believes all of alumina, manganese and coal are expensive based on current cost curves.

Deutsche has thus downgraded to Sell. Target falls to $2.80 from $2.85.

SANTOS LIMITED ((STO)) Downgrade to Sell from Neutral by UBS and Downgrade to Neutral from Buy by Citi .B/H/S: 4/2/2

UBS observes 2018 production guidance is marginally below 2017 while capital expenditure guidance is up 17% at the mid point. The company is expecting a broadly flat output from its five key assets.

While the stock has been an effective way to gain exposure to an oil price recovery the broker believes it is now factoring in an oil price that is 10% above spot and downgrades to Sell from Neutral. Target is raised to $4.05 from $3.85.

Following the strong share price rally, Citi has pulled back its rating to Neutral from Buy. The analysts do highlight Santos remains their favourite exposure in the sector.

The analysts reiterate their view that on implied long term oil price assumptions, the sector in general looks "expensive".

Citi see potential blue-sky value of $6.47 from de-risking growth and delivering further cost-out, but also suggests this is likely to be a multi-year process. In the near term, the analysts continue to see risk to the price of crude oil. Target lifts to $4.71 from $4.30.

Interestingly, the analysts have now scrapped DPS estimates for both 2017 and 2018.

WESTPAC BANKING CORPORATION ((WBC)) Downgrade to Neutral from Outperform by Credit Suisse .B/H/S: 3/5/0

Credit Suisse liked the balance sheet growth in FY17 but did not like the negative tone of the FY18 guidance statements, particularly around revenue.

Following the upgrade of the stock mid 2017 to Outperform as a tactical call on the leverage to Australian mortgage re-pricing, the broker now downgrades to Neutral as the benefits have become embedded and there are emerging margin headwinds.

Target is reduced to $33.50 from $34.00.

XERO LIMITED ((XRO)) Downgrade to Underperform from Neutral by Macquarie .B/H/S: 1/2/1

The company's first half results were in line with Macquarie's forecasts. Xero has also announced its intention to de-list from the NZX. The company intends to focus its liquidity on one market, and the broker observes this should make trading the shares easier.

Following a period of strong price appreciation the broker downgrades to Underperform from Neutral. An aggressive set of valuation assumptions does not generate the valuation that justifies a positive stance, Macquarie believes.

Target is increased to NZ$30 from NZ$23.

Total Recommendations Recommendation Changes

Broker Recommendation Breakup

Broker Rating Order Company New Rating Old Rating Broker Upgrade 1 COMMONWEALTH BANK OF AUSTRALIA Neutral Sell Citi 2 COSTA GROUP HOLDINGS LIMITED Buy Neutral Macquarie 3 ECLIPX GROUP LIMITED Buy Neutral Citi 4 JAMES HARDIE INDUSTRIES N.V. Buy Neutral Citi 5 JANUS HENDERSON GROUP PLC. Buy Neutral Citi 6 JB HI-FI LIMITED Neutral Sell Ord Minnett 7 LIVEHIRE LIMITED Buy Neutral Morgans 8 MAGELLAN FINANCIAL GROUP LIMITED Buy Neutral Credit Suisse 9 PLATINUM ASSET MANAGEMENT LIMITED Neutral Sell Credit Suisse 10 SUPER RETAIL GROUP LIMITED Neutral Sell Ord Minnett 11 VIRGIN AUSTRALIA HOLDINGS LIMITED Buy Neutral Credit Suisse Downgrade 12 ALTIUM LIMITED Neutral Buy Credit Suisse 13 COCHLEAR LIMITED Sell Neutral Citi 14 COMMONWEALTH BANK OF AUSTRALIA Neutral Buy Morgans 15 INGHAMS GROUP LIMITED Neutral Buy Citi 16 MACQUARIE ATLAS ROADS GROUP Neutral Buy Morgans 17 MURRAY RIVER ORGANICS GROUP LIMITED Neutral Buy Morgans 18 ORICA LIMITED Sell Neutral Citi 19 SANTOS LIMITED Neutral Buy Citi 20 SANTOS LIMITED Sell Neutral UBS 21 SOUTH32 LIMITED Sell Neutral Deutsche Bank 22 WESTPAC BANKING CORPORATION Neutral Buy Credit Suisse 23 XERO LIMITED Sell Neutral Macquarie Recommendation Positive Change Covered by > 2 Brokers Order Symbol Company New Rating Previous Rating Change Recs 1 CGC COSTA GROUP HOLDINGS LIMITED 67.0% 33.0% 34.0% 3 2 DOW DOWNER EDI LIMITED 50.0% 25.0% 25.0% 5 3 PTM PLATINUM ASSET MANAGEMENT LIMITED -75.0% -100.0% 25.0% 4 4 VAH VIRGIN AUSTRALIA HOLDINGS LIMITED -38.0% -63.0% 25.0% 4 5 ECX ECLIPX GROUP LIMITED 100.0% 83.0% 17.0% 6 6 MFG MAGELLAN FINANCIAL GROUP LIMITED 33.0% 17.0% 16.0% 6 7 OZL OZ MINERALS LIMITED 38.0% 25.0% 13.0% 8 8 JHX JAMES HARDIE INDUSTRIES N.V. 67.0% 57.0% 10.0% 6 9 SUL SUPER RETAIL GROUP LIMITED 63.0% 56.0% 7.0% 8 10 JBH JB HI-FI LIMITED -13.0% -19.0% 6.0% 8 Negative Change Covered by > 2 Brokers Order Symbol Company New Rating Previous Rating Change Recs 1 ALU ALTIUM LIMITED 33.0% 67.0% -34.0% 3 2 STO SANTOS LIMITED 25.0% 50.0% -25.0% 8 3 MQA MACQUARIE ATLAS ROADS GROUP 20.0% 40.0% -20.0% 5 4 COH COCHLEAR LIMITED -50.0% -33.0% -17.0% 6 5 EPW ERM POWER LIMITED 33.0% 50.0% -17.0% 3 6 ING INGHAMS GROUP LIMITED 67.0% 83.0% -16.0% 6 7 ORI ORICA LIMITED -38.0% -25.0% -13.0% 8 8 SGM SIMS METAL MANAGEMENT LIMITED 20.0% 33.0% -13.0% 5 9 WBC WESTPAC BANKING CORPORATION 38.0% 50.0% -12.0% 8 10 S32 SOUTH32 LIMITED 13.0% 25.0% -12.0% 8 Target Price Positive Change Covered by > 2 Brokers Order Symbol Company New Target Previous Target Change Recs 1 ALU ALTIUM LIMITED 10.200 9.367 8.89% 3 2 VAH VIRGIN AUSTRALIA HOLDINGS LIMITED 0.188 0.173 8.67% 4 3 PTM PLATINUM ASSET MANAGEMENT LIMITED 5.090 4.713 8.00% 4 4 JHX JAMES HARDIE INDUSTRIES N.V. 21.780 20.396 6.79% 6 5 DOW DOWNER EDI LIMITED 7.050 6.680 5.54% 5 6 ECX ECLIPX GROUP LIMITED 4.645 4.417 5.16% 6 7 CGC COSTA GROUP HOLDINGS LIMITED 5.903 5.617 5.09% 3 8 STO SANTOS LIMITED 4.461 4.248 5.01% 8 9 ORI ORICA LIMITED 18.083 17.463 3.55% 8 10 MFG MAGELLAN FINANCIAL GROUP LIMITED 27.893 27.155 2.72% 6 Negative Change Covered by > 2 Brokers Order Symbol Company New Target Previous Target Change Recs 1 SGM SIMS METAL MANAGEMENT LIMITED 14.060 14.883 -5.53% 5 2 IPL INCITEC PIVOT LIMITED 3.700 3.738 -1.02% 7 3 ING INGHAMS GROUP LIMITED 3.775 3.792 -0.45% 6 4 WBC WESTPAC BANKING CORPORATION 33.700 33.800 -0.30% 8 5 S32 SOUTH32 LIMITED 3.179 3.185 -0.19% 8 Earning Forecast Positive Change Covered by > 2 Brokers Order Symbol Company New EF Previous EF Change Recs 1 PRU PERSEUS MINING LIMITED 1.362 0.102 1235.29% 5 2 ECX ECLIPX GROUP LIMITED 27.583 25.017 10.26% 6 3 BTT BT INVESTMENT MANAGEMENT LIMITED 60.383 55.900 8.02% 6 4 VAH VIRGIN AUSTRALIA HOLDINGS LIMITED 0.901 0.866 4.04% 4 5 CGC COSTA GROUP HOLDINGS LIMITED 22.667 21.933 3.35% 3 6 PTM PLATINUM ASSET MANAGEMENT LIMITED 30.250 29.425 2.80% 4 7 STO SANTOS LIMITED 15.374 14.981 2.62% 8 8 WBC WESTPAC BANKING CORPORATION 243.843 238.450 2.26% 8 9 MFG MAGELLAN FINANCIAL GROUP LIMITED 117.450 114.917 2.20% 6 10 OZL OZ MINERALS LIMITED 55.873 54.844 1.88% 8 Negative Change Covered by > 2 Brokers Order Symbol Company New EF Previous EF Change Recs 1 JHG JANUS HENDERSON GROUP PLC. 284.457 318.328 -10.64% 5 2 SYR SYRAH RESOURCES LIMITED -10.344 -9.584 -7.93% 5 3 AAD ARDENT LEISURE GROUP 3.137 3.380 -7.19% 7 4 NAB NATIONAL AUSTRALIA BANK LIMITED 229.363 240.038 -4.45% 8 5 ORI ORICA LIMITED 101.770 105.913 -3.91% 8 6 AQG ALACER GOLD CORP 35.286 36.360 -2.95% 5 7 S32 SOUTH32 LIMITED 24.044 24.699 -2.65% 8 8 KAR KAROON GAS AUSTRALIA LIMITED -7.100 -7.000 -1.43% 3 9 CYB CYBG PLC 31.706 32.060 -1.10% 5 10 TME TRADE ME GROUP LIMITED 23.388 23.648 -1.10% 5 Technical limitations

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

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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 November 9, 2017

Last week saw the ASX200 bolt up from just above 5900 to peak out at 6050. One might have expected the break-out of the longstanding 6000 barrier to spark some covering from nervous shorts, or indeed that the sharp rise might have been aided by short-covering, but the table below shows little evidence of such.

Ups and downs are minimal and only represent bracket creep. There is one exception however.

It's been a while since I've highlighted battery-related mining stocks in this Report, for the simple reason their share prices are very volatile and as such so are their weekly changes in short position. As they are among the most shorted stocks in the market, changes of one percentage point or more are less relevant on a weekly basis.

But last week saw decent reductions in shorts for both Galaxy Resources ((GXY)) and Orecobre ((ORE)). See below.

Another move to note, which is not substantial in the wider picture but worth highlighting nonetheless, is that shorts in National Bank ((NAB)) doubled last week, to 1.4% from 0.7%, in the wake of a poorly received earnings result.

Weekly short positions as a percentage of market cap:

10%+

SYR 21.3 IGO 19.9 DMP 16.6 JBH 16.0 HSO 14.6 RFG 12.6 ORE 11.5 WSA 11.4 MTS 10.9 ACX 10.6 AAD 10.5 MYR 1049 APO 10.3

Out: HVN

9.0-9.9

HVN, MYX, SHV Out: GXY

8.0-8.9%

HT1, NWS, FLT, JHC, RIO, QIN, VOC, GXY, MND

In: GXY, JHC, VOC, MND Out: NXT

7.0-7.9%

TPM, NXT, NSR, GXL, SEK, GTY

In: NXT Out: VOC, JHC, MND

6.0-6.9%

MYO, AHG, BEN, BAP, ING, BKL, AAC

Out: ISD, SAR

5.0-5.9%

TAH, ISD, CSR, MOC, KAR, GMA, NEC, WHC, SUL, IFL, SAR, PRU, IPD, ABC, QUB

In: ISD, SAR Out: FXL

Movers and Shakers

Late last month a broker report put a bomb under all battery-related commodities, and subsequently share prices of the miners of those commodities. The report suggested global growth in demand for electric vehicles will outpace the growth in production of metals used in EV batteries, including lithium, cobalt, graphite and nickel.

The share prices of Australia's lithium miners went for a run, after having already run hard for some time on the battery story. Short-covering was evident, given battery-related miners are over-represented in the 10% plus shorted club.

Shorts in Galaxy Resources fell to 8.2% from 9.6% and shorts in Orocobre fell to 11.5% from 12.9%.

Still atop the table, graphite mine developer Syrah Resources ((SYR)) saw its shorts fall to 21.3% from 22.2%. But it was this week that Syrah presented to a UBS conference and sparked a 10% one-day share price jump.

The report did little to change shorters' views on the two major nickel miners Independence Group ((IGO)) and Western Areas ((WSA)). Their extensive short positions are little changed.

The issue with National Bank was not so much a "miss" on earnings, given that was down to a drop in market trading profits suffered by all the banks, but an announced significant increase in investment in FY18 that will drag heavily on earnings.

Drag on earnings and you drag on dividends. NAB shorts doubled post result to 1.4% from 0.7%. Commonwealth Bank ((CBA)) shorts remained at 0.9%, ANZ Bank ((ANZ)) saw a tick up to 0.7% from 0.6% and Westpac ((WBC)) copped an increase to 1.6% from 1.4%.

ASX20 Short Positions (%)

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

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

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

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

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

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

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

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

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

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The Wrap: Health, Retail, Super Advice & Asia

Weekly Broker Wrap: private health; banks & retail exposure; retailers; retail A-REITs; Amazon; superannuation advice; Asia.

-Private health insurance coverage continues to decline putting pressure on private hospital operators -Little in the way of good news for Australian apparel retailers -Reduced profitability for retail tenants factored into retail A-REITs -Success at Amazon Marketplace initially expected at the expense of eBay -Asian construction boom supporting strong inflows of manufacturing investment

By Eva Brocklehurst

Private Health

APRA has published September data for the private health industry, with 4.3% growth in insurance premiums noted in the year to September and 3.7% growth in benefits paid. Industry margins were 14.4% and at the highest level since 2011. Deutsche Bank notes the offset for higher margins and strong premium growth is that customer numbers remains soft.

The number of hospital-only persons insured has fallen to 11.3m while total persons insured is up 40 basis points to 13.5m. Given strong population growth, the penetration rate slipped to 54.7% in the September quarter. There remains a skew towards older members in private health insurance, with those aged over 65 growing 3.5% while members under 65 down -0.9%.

Opinions among brokers regarding recently announced reforms to help affordability vary from negative to marginally positive. UBS continues to envisage long-term fundamentals are broadly unchanged and volumes are not expected to return to trend inside 12 months in the private hospitals sector.

Citi forecasts first half growth in Australian hospital business of 7% for Ramsay Health Care ((RHC)) and 4% for Healthscope ((HSO)) and suspects, as the number of people with private health insurance is declining, pressure on revenue for private hospital operators will continue.

Macquarie believes the hospital sector is already factoring in a lower volume growth environment, amid headwinds from reduced private health insurance participation as well as weaker utilisation. The broker retains an Outperform rating for Ramsay Health Care and Neutral for Healthscope.

Bell Potter notes lower hospital utilisation is generally good for the operating margins of insurers but believes, in the current environment, it remains very tough to grow policy holder bases. The offset to low claims inflation for the consumer should be the thin premium increases in April 2018. The broker considers Medibank Private ((MPL)) is better value in this segment at present. Nib ((NHF)) has been a strong performer but the broker does not consider its valuation enough to justify current levels.

Credit Suisse does not believe reforms will alter current affordability issues: as long as private health insurance premiums inflate at a rate faster than wages growth, and with an alternative service provider in the form of the public hospital system, the decline in participation will continue along with lower levels of private hospital utilisation.

Banks & Retail Exposure

Credit Suisse benchmarks major bank exposures to retail trade through the prism of increased online retailing. Exposure levels range from 1.1% for Commonwealth Bank ((CBA)) to 2.3% for ANZ Bank ((ANZ)). Broadly half of this is in the sub-sector of personal & household goods.

National Australia Bank ((NAB)) has stated that its exposure to personal & household goods is dominated by pharmacy retailers followed by apparel and furniture & homewares. Retail trade asset quality trends were mixed in the second half of FY17.

Commonwealth Bank reported a higher troublesome & impaired ratio at 2.2% versus 1.9% in the first half, while National Australia Bank reported a lower impaired & past-due ratio of 0.79% versus 0.98%. Westpac ((WBC)) reported an increased stress ratio of 3.02% versus 2.51% but a lower impaired ratio of 0.31% versus 0.40%.

Retailers

Macquarie analyses the most recent income statements from apparel & footwear retailers, finding two thirds reported negative top-line growth, suggesting profitability has been trending down over the last few years and remains challenging. While the prospect of closing underperforming stores should lift near-term performance in some networks, the broker envisages little in the way of good news for Australian apparel retailers.

In the last few years headwinds in the form of a lower Australian dollar have likely affected gross margins, given the relative inability to pass this cost on via higher prices. Macquarie suggests this is exacerbated by the arrival of recent low-price international retailers such as Zara, H&M and Uniqlo. The pending arrival of Amazon will also mean elevated discounting continues.

Operating earnings margins of unlisted retailers are also observed to be at all-time lows, compressing to 0.5% in FY16 from 6.5% in FY11. In contrast listed retailers, such as Premier Investments ((PMV)), Specialty Fashion ((SFH)) and Noni B ((NBL)) have experienced improvements in operating margins over the same period.

Retail A-REITs

As profitability headwinds persist, a number of retailers have been closing less productive stores and Macquarie calculates store count is down around -1% year-on-year. The broker expects this trend to continue, particularly among unlisted retailers.

While profitability for retail tenants remains under pressure the broker believes this is already factored into the share prices of the retail A-REITs. The broker retains Vicinity Centres ((VCX)) as its preferred domestic retail landlord while Westfield ((WFD) is offering the highest total shareholder return, 19%, across the broader coverage.

Amazon Summit

Morgan Stanley attended the Amazon Marketplace summit, where the company has announced its fee structure. Sellers will be charged $49.95 plus GST per month and then a 6-15% referral fee which varies by category. This is the price for the Marketplace offer and does not include fulfilment by Amazon.

By comparison eBay charges monthly fees of zero (no store) up to $549.95 per month (store with unlimited products) and a variable fee of between 4.8% and 10.9%. Initially, the broker suggests that success in Amazon's Marketplace will come at the expense of eBay's business, although at first glance it appears Amazon is offering a more "premium" model.

No timeline was provided for the launch in Australia. The company has stressed the importance of fulfillment by Amazon, citing a case study in the US where the cost for sellers of shoes is just US$4-5, a significant saving as it includes picking, packing, returns, enquiry handling and freight.

Superannuation & Advisors

Bell Potter notes structural changes occurring in the superannuation sector, with a continued move away from the big integrated players. Around 82 advisers left the main four banks and AMP ((AMP)) in October. Over the last year advisers are reduced by -8.3% for the large five players, and AMP has lost the most.

The broker does not observe anything to arrest this decline and considers the trend supports a Sell rating on AMP and IOOF ((IFL)). The broker retains a Buy ratings for the independent operators that are benefiting from the changes, including Praemium ((PPS)) and Onevue Holdings ((OVH)).

Asia

Southeast Asian markets, led by the "tiger cubs" of Indonesia, Malaysia, Philippines, Thailand and Vietnam are among the world's fastest growing. These countries need to invest heavily in infrastructure, such as transport and utilities and, across the region, governments are embarking on ambitious programs.

BIS Oxford Economics suggests, until now, the pace of these infrastructure projects has been limited by significant constraints on public finance since the GFC, but growth has resumed and is set to provide a stronger foundation. Rising living standards will also fuel demands for better quality housing and public facilities, including healthcare and education.

The analysts at BIS Oxford Economics observe this is attracting a strong flow of inward business investment from both local and multinational manufacturers, supported by a supply of still relatively cheap labour. Over the next five years construction investment in Asia is expected to average US$1.61 trillion per year.

The positive prospects in Southeast Asia are underpinned by China's external investment in construction such as its "one belt one road" initiative. The analysts also note India's construction sector investment is currently the third largest in Asia, after China and Japan, matching that of the UK.

BIS Oxford Economics notes India's annual construction investment, expected to jump by almost one third, adds more momentum to an Asia-wide building boom that look set to last through the next decade and beyond.

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EclipX On The Right Road

By Michael Gable

With the S&P/ASX 200 Index clearing the 6000 mark, and sentiment looking positive running into Christmas, it is best to make hay while the sun shines. One of our recent picks which has performed solidly is Eclipx Group ((ECX)). It is undergoing some profit taking after a good run, so while it takes a breather here, we'll use this opportunity to take another look at the company's fundamentals and determine where it might be heading based on the charts.

Our previous charting commentary on ECX was back in September when it broke the downtrend and triggered a "buy". We expected the stock to move to a new high "in the next month or so". It has managed to head to its previous peak a bit quicker than expected. Now it is at these levels, we expect it to congest here as profit taking kicks in, trading between about $4 and $4.30. Once that has completed, then the stock should be ready to move to a new high and continue trending higher.

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Treasure Chest: The Outlook For Gold

Fed tightening, US tax reform and elevated speculative positions all make the gold price potentially vulnerable in the December quarter.

- Gold beholden to US monetary/fiscal developments - Gold positions elevated - Chinese demand the swing factor

By Greg Peel

The US dollar gold price was weaker in the December quarters of 2016 and 2015 on expectations of Fed tightening, a subsequently stronger US dollar and rising US bond yields. As we enter the December quarter of 2017, Macquarie's commodities analysts see a very similar picture.

The Fed delivered rate increases in both of the past two Decembers and the market is currently pricing in a 97% chance of 2017 being no different. But despite popping several basis points last night, the US ten-year yield has not much risen this year given low inflation and persistently low yields in both Europe and Japan.

Rather, the US yield curve has flattened, meaning short term yields have risen on Fed expectations but longer term yields have not. Even if US inflation were to start picking up, the same would have to occur in other regions, where to date QE remains stubbornly in place despite economic growth, or US yields will remain beholden to differentials.

Macquarie believes the US will see inflation return in 2018 but unlike past December quarters, the analysts do not necessarily see the US dollar rising ahead of a Fed rate hike. The difference this time is politics. In particular, were Trump's tax plan to be stalled, and so far a year's delay on a corporate rate cut looks ever more a possibility, the dollar is more likely to fall than rise.

And it is possible the Fed would then be forced to hold off as well.

This would be positive for gold, which otherwise is not seeing much geopolitical support these days, despite the North Korea threat and more recently, Saudi Arabia stirring up the Middle East. Were a tax bill to be passed, without a time delay, then it would not look good for gold.

Demand/Supply

The other influence on the gold price, beyond monetary policy, is of course actual demand. This can be split into two categories – speculative, represented by positions held in gold exchange traded funds in the US and Europe, and physical, represented by jewellery and coin/bar buying in China and India in particular.

Central bank buying/selling should also be included but things have been very quiet on that front for some time.

The West dominates speculative flows and the East dominates physical flows. Speculative positions are currently elevated, which puts gold in a vulnerable position, Macquarie suggests. RBC Capital Markets notes that while the US has the biggest gold ETFs, flows into ETFs in Europe have been stronger of late.

China and India represent more than 50% of global jewellery/coin/bar demand. Europe and North America have seen declining demand over past years and even India is now seeing a downward trend. This leaves China as the primary driver, both Macquarie and RBC acknowledge.

Gold price weakness in the December quarters of 2016 and 2015, on Fed speculation, was eventually overcome heading into the (solar) New Year by Chinese physical demand, Macquarie notes, ahead of the popular gift-giving period of Chinese (lunar) New year early in the calendar. While there is no reason to suspect 2018 will be any different, Macquarie does note Chinese demand in the September quarter 2017 was actually weak by previous years' standards.

On the other hand, mine production and scrap supply were weaker in the September quarter 2017 compared to 2016. But while this implies a tighter market, the balance remained in a large surplus. It is this surplus that leads Macquarie to highlight gold's vulnerability in the face of monetary/fiscal developments ahead.

RBC is forecasting a December quarter average gold price of US$1265/oz (current spot ~US$1275) and a 2017 average of US$1256/oz.

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