WEEK 20

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Friday, 15 May 2020

Amcor Yield A Rarity In Current Environment

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CONTENTS

AUSTRALIA

COMMODITIES

FEATURE STORIES

WEEKLY REPORTS

RUDI'S VIEWS

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AUSTRALIA

Firm Outlook For Orica Despite Mine Closures

Orica has reduced the first-half dividend pay-out ratio to 40%, amid the pandemic uncertainty, although brokers assess the second half should reflect a return to better conditions.

-Curtailments at mines largely reflect lockdowns and not weak demand
-No impact on Orica's highest-margin volumes in Australia
-Technology remains Orica's key advantage

By Eva Brocklehurst

There has been a greater impact on the mining services business of Orica ((ORI)) than previously expected from pandemic disruptions, but the company has enough positive aspects going forward to keep most brokers unperturbed.

Upside exists from potential stimulus to infrastructure by governments while downside risk stems from further mining disruptions and slumping commodity prices which may cause mines to close.

However, Morgans cautions that the outlook could worsen still and suggests it is too early to consider an investment in the stock, sticking with a Hold rating. The broker acknowledges the first half result was "reasonable" with the robust Australasian business a highlight.

To date, the company has experienced minimal impact on demand from the pandemic but forced mine closures and operating restrictions globally are having an effect. The most significant disruptions are in Latin America and Europe/Middle East. Australia and PNG are minimally affected, with most mining activity continuing. However, India, Malaysia and the Philippines are experiencing more significant impacts.

Orica has withdrawn its FY20 guidance for operating earnings (EBITDA) to be higher than FY19. Ammonium nitrate volume guidance has also been downgraded and customer demand is expected to return to pre-pandemic levels around November.

First half results were affected by volume losses from the NSW bushfires and -$14m in costs relating to increased east coast gas prices, as well as Burrup arbitration fees. Amid the uncertainty, Orica has reduced the first half dividend payout ratio to 40%. Should the uncertainty dissipate, UBS assesses there is scope for a boost to the final dividend back to 70%.

The reduction in the interim dividend in the first half is likely to be a temporary measure, most brokers agree, depending on whether the current earnings outlook deteriorates further but there is sufficient funding for a worse scenario.

Management expects second half volumes to be -10-15% lower than prior guidance which implies an overall drop of -6-11%. Following the normalisation of global mining activity volume growth should return. Credit Suisse assesses the new volume guidance is reasonable and adequately captures the ongoing impact of the pandemic.

UBS takes a more conservative view on the disruptions as well as manufacturing costs but notes, significantly, there has been no impact on Orica's highest margin volumes in Australia.

It remains to be seen whether the company is being conservative, Morgan Stanley asserts, ascertaining clarity on the earnings outlook would deliver a more positive stance while appreciating the themes behind the explosives market and the company's leadership position.

Orica and Dyno Nobel have forged ahead of competitors, with technology that enables full automation, increasing safety and productivity, Macquarie points out. **March was also a record sales month for radar and laser systems**.

Outlook

Macquarie had anticipated volumes would be weaker but the extent was greater than forecast across Latin America EMEA, Canada and Asia. Putting a positive spin on the results, the broker points out these are Orica's lowest-margin regions relative to the larger and more profitable Asia-Pacific and North America.

Moreover, curtailments reflect the lockdown measures taken rather than soft demand. Hence, the impact should reduce sequentially, in the broker's assessment. Currently mines are restarting in Quebec, South Africa, Colombia and Peru.

The company has also pointed out there is no coal-related demand weakness in Australia or Asia, despite the weaker coal prices, and North America thermal coal is now only 11% of regional volumes with offsets from gold/copper. Macquarie assesses 90% of seaborne thermal coal production remains cash positive. However, there is a risk of curtailments to mining if prices weakened further.

Expectations have been sufficiently re-based for the second half, in Credit Suisse's view, although pricing is an added risk if it turns out to be a multi-year downturn for mining and infrastructure. Infrastructure expenditure could move in either direction, while the broker envisages more downside potential in construction that would affect the quarry segments in the US and Europe

Hence, **expectations for pricing upside may need to be pushed out to 2022**. Citi highlights multi-year contracts with major miners and suspects FY22 may be the "golden year" as long-term contracts typically run for 3-4 years and only a small proportion of annual sales are conducted at spot prices. Hence, material price and earnings growth could emerge in FY22 when around 40% of the contracts come up for renewal.

Orica is well situated to manage the issues, Goldman Sachs believes. The commodity backdrop may be bearish but the broker, not one of the seven stockbrokers monitored daily on the FNArena database, continues to believe the underperformance in the stock over-emphasises the impact and reiterates a Buy rating with a $19.80 target.

Burrup

The Burrup plant is now operational. Orica expects a positive contribution in the second half with production to exceed 100,000t. The plant is expected to be fully operational in FY21 with current contracts. Yet Morgans notes commentary for an average monthly production rate of 20-23,000t means the second half and FY21 will be weaker than previously expected.

Material returns are also expected in FY22 from the SAP system, which is being implemented globally across operations. Orica expects increased productivity and efficiency and a decrease in manual reporting. The launch is in the second half and, given Orica is targeting a 15% return on investment, Citi calculates this implies around $40m of additional earnings in FY22.

The Exsa acquisition has been completed and by the third full year of ownership Orica expects to achieve a

US$18m synergy run rate. Macquarie assesses there is further upside from cross selling as Orica's technology is introduced across that business and the customer base is broadened.

FNArena's database has three Buy ratings and four Hold. The consensus target is $18.16, signalling 10.6% upside to the last share price. Targets range from $15.55 (Morgans) to $20.75 (UBS).

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AUSTRALIA

Macquarie Group To Bounce Back In FY22

Asset realisations are likely to be more difficult for Macquarie Group in the year ahead, along with heightened impairments, but brokers find many reasons why the wide-ranging investment business will prevail once again.

-Robust capital position to take advantage of market dislocation
-Renewables and asset developments differentiate Macquarie Group
-Strong rebound expected in FY22

By Eva Brocklehurst

The uncertainty created by the coronavirus pandemic is affecting Macquarie Group ((MQG)), despite its robust and wide-ranging investment business. Asset realisations are likely to be more difficult in the year ahead, impairments worsen and the commodity outlook is, well, muddy.

UBS assesses lending has become more challenging and further asset impairments cannot be ruled out. Yet most businesses continue to perform well.

Moreover, Macquarie Group has a strong capital position whereby it can take advantage of market dislocation. The group's capital surplus rose to $7.1bn although the final dividend was reduced by -28%, providing a pay-out ratio of 50%.

The final dividend will be funded entirely by the non-bank group. The company will raise additional equity from a discounted dividend reinvestment plan and issue an employees share plan consistent with APRA's guidance.

UBS assesses this will provide **additional capital buffers, should the global economy weaken further.** Additionally, there could be investment opportunities during the current downturn that support the next phase of growth.

The broker points out this is consistent with an "acquisition spree" Macquarie Group undertook following the GFC. However, the current travel restrictions make cross-border acquisitions more difficult in the short term.

Goldman Sachs does not expect the current crisis to be as severe for Macquarie Group, as it has not originated from within the banking system, although notes that around 18% of revenue in FY20 was from performance fees and investment income, a source that will largely disappear in FY21, in keeping with the company's commentary. The broker's base case scenario is for FY21 investment income and performance fees to move close to zero.

Goldman Sachs, not one of the seven stockbrokers monitored daily on the FNArena database, continues to envisage earnings risk in FY21 but assesses the balance sheet and capital position are strong, as evidenced by the 12.2% CET1 ratio and the surplus capital. Still, the range of possible outcomes in FY21 and FY22 remain wide and the broker retains a Neutral rating with a $127.32 target.

Impairments

Higher impairments drove the miss to Morgans' forecasts in FY20 and the divisional commentary points to areas of softness but the broker finds the performance credible against a tough backdrop.

Ord Minnett forecasts a fall in net profit of -10% in FY21 on higher impairments, lower performance fees and lower gains on sale. A strong rebound is expected in FY22, with profit growth of 30% as the pandemic eases and significant liquidity in global markets means the asset chase can begin again.

Credit impairments in FY20 were greater than Morgan Stanley expected, and are likely to rise to around $1.5bn in FY21 while the cycle is far from finished. Moreover, the broker incorporates a drop of -33% in FY21 performance fees and suspects the disruption to private markets is now broader than what occurred in the GFC.

Asset Management

Offsetting this, the equity investment book has grown substantially and the renewables and asset development capabilities differentiate Macquarie Group. In terms of commodities, the broker finds it unclear how much revenue will fall once the volatility eases and whether energy markets remain subdued.

Morgan Stanley retains an Overweight rating, given the compelling long-term growth and an impressive performance in asset management. Despite the bear market, assets under management grew 8% half on half and second half base fees grew around 20%.

The broker considers guidance for flat base fees in FY21 a conservative estimate, noting earnings stability in this division becomes even more attractive during the downturn.

UBS considers it unlikely Macquarie will be able to stem a reduction in revenue in FY21, although the extent is difficult to estimate. Transaction volumes and values for hard asset sales are likely to fall, reducing the ability to generate gains on sale. This will also affect performance fees within the unlisted funds.

The broker notes the company has a **high degree of operating leverage, with an elevated cost-to-income ratio**. The bonus pool could be utilised to insulate some of the pressure. Moreover, discretionary expenditure, travel and entertainment costs are likely to plummet.

Credit Suisse agrees there is an "expense buffer" although envisages downside for the short term amidst multiple constraints around transaction volumes, asset realisations and performance fees, as well as potential for further impairments. Hence the broker downgrades to Neutral from Outperform.

FNArena's database has three Buy ratings, two Hold and one Sell (Citi). The consensus target is $116.25, signalling 4.9% upside to the last share price. The dividend yield on FY21 and FY22 forecasts is 4.1% and 5.2%, respectively.

AUSTRALIA

Scentre Group Stalls First Half Distribution

Scentre Group has decided to forgo a first half distribution to protect the balance sheet, and is waiting for stores to re-open before entering rent relief discussions with tenants.

-Gearing remains elevated, asset values are weakening
-Targeting a -25% reduction in operating expenses
-Business heavily exposed to the likely decline in asset values

By Eva Brocklehurst

The retail environment has perked up in the past couple of weeks and shops are now re-opening at Scentre Group's ((SCG)) shopping centres. Discretionary categories remain soft although staples continue to hold up.

To protect the balance sheet, the company will not pay a first half distribution but still intends to pay a final distribution at the end of 2020 after assessing the impact of the pandemic.

Gearing is elevated, and UBS suggests, in a period in which asset valuations are declining and income is weak, measures will need to be taken to limit the damage to the balance sheet, including the current decision not to pay a first half dividend.

Ord Minnett forecasts a 2020 distribution of 11.9c, which would be down -47% on 2019, while Goldman Sachs does not expect a final distribution, given the company's taxation status.

Removal of the first half distribution payment increases operating earnings per security by around 1% per annum over the medium term, in the broker's calculations. However, the impact on estimates is offset by lower assumed development volumes.

<u>Rentals</u>

Management will also assess the impact on retailers of the store closures before entering into rent relief discussions and will wait for stores to open and foot traffic to return.

The opening of stores is increasing, with 57% of tenants over 70% of the gross lettable area now open. Ord Minnett notes this is well up on the low of 39%, with a sharp rise in the past fortnight, centred on Mother's Day.

Only a minimal number of rent relief packages have been confirmed and Morgan Stanley suggests the desire to wait until stores re-open is a strategic move and explains why the company has been slow to offer deals to tenants.

April rent collections were not disclosed but channel checks suggest 20-30% of specialties paid their rent.

With reference to the tough negotiating positions being taken by some specialty retail chains with regard to non-payment of rent, Goldman Sachs asserts there is an increased likelihood that the company will not reach agreements with retailers.

Still, no specialty retailer accounts for more than 2% of the company's annual rental income. The broker, not one of the seven monitored daily on the FNArena database, has a $3.74 target and Buy rating.

Macquarie notes Scentre Group has a 30% exposure to small-medium enterprises and assumes these tenants receive a -50% rental abatement for a term of six months and assumes a three-month impact before shopping centres return to regular operations.

The company is targeting a reduction in operating expenses of more than -25% during the pandemic, although Morgan Stanley points out 60% of costs are worn by tenants anyway.

The board and senior management will sustain a -20% reduction in fixed remuneration while the roles of 80% of the workforce have been adjusted, in terms of rosters et cetera.

<u>Gearing</u>

To preserve long-term gearing, UBS forecasts a pay-out ratio of 70% that would allow $350m per annum in debt reduction prior to future development plans. This would put the stock on a distribution yield of 7% with minimal growth and still with **considerable uncertainty remaining regarding sustainable rent and valuations**.

While the balance sheet is protected by the non-payment of a distribution, Macquarie still warns the business is exposed to the likely decline in asset values. The broker remains of the view that retail valuations will decline by -15% and, if this happens, then gearing would increase to around 39%.

This would, in turn, increase the need to reduce financial leverage either through asset sales or an equity issue, although the broker observes neither of these strategies is a priority for the company.

The broker understands costs associated with developments are variable and increase in line with activity. Hence, assuming minimal development activity, the likelihood of changes in this area is limited.

The company has extended all bank facilities that were due to mature in 2021 and now has no bank debt maturing until January 2022.

FNArena's database has two Buy ratings, three Hold and one Sell (Citi, yet to comment on the update). The consensus target is $2.49, suggesting 14.8% upside to the last share price. The dividend yield on FY20 and FY21 forecasts is 5.5% and 8.6%, respectively.

AUSTRALIA

Usual Suspects Weigh On Incitec Pivot

Incitec Pivot remains a slave to the usual suspects - cropping conditions, explosives demand and pricing. A capital raising has alleviated some concerns for the balance sheet.

-Low coal prices likely to impact on volumes
-Suspends dividend, defers capital expenditure
-Fertiliser prices expected to weaken

By Eva Brocklehurst

There are limited effects to date from the pandemic on Incitec Pivot ((IPL)) Instead the fertiliser and explosives business remains a slave to the usual suspects - crop conditions, pricing and mining/quarry demand.

First half results was supported by an improved manufacturing performance while the global explosives business, Dyno Nobel, was resilient, delivering a flat earnings outcome despite contract re-pricing and a sharp decline in US coal volumes. US coal is expected to remain weak because of lower electricity demand, while low prices for the Australian coal business could also impact on the company's volumes.

On the positive side, production at the main manufacturing plants was solid and Credit Suisse points out operating rates and safety indicators have improved at both Phosphate Hill and Waggaman.

Nevertheless, margins were weaker, particularly in fertilisers, even as sales were supported by improved weather conditions. UBS remains attracted to the strong position in the explosives markets but the other part of the business, fertilisers, is expected to remain depressed.

The company will raise $600m via an underwritten institutional placement and up to $75m in a share purchase plan, to improve liquidity. This alleviates concerns over the balance sheet for brokers.

Incitec Pivot has also conserved cash by deferring capital expenditure of $40m, suspending the interim dividend and targeting cost savings in the second half of $20m. Morgan Stanley is pleased with the decision to raise capital, believing the business had carried more gearing than was appropriate given the cyclical nature of earnings.

Credit Suisse assesses the **downward pressure on commodity prices and risks to mining & quarry markets limit the upside** for the prospective new investors, and also points to a heightened debate about the extent and timing of a recovery in commodity prices.

Still, there are long-term drivers of value which should re-emerge once the extent of the risks are clearer. Moreover, there is now an opportunity to pursue small bolt-on acquisitions.

Explosives

Dyno Americas explosives earnings were flat in the US, with value-added products offsetting some weakness in coal. Australia and North America are the main explosives markets for Incitec Pivot and there is minimal exposure to Europe, the Middle East or Latin America. Dyno Asia-Pacific also has no thermal coal exposure in Australia.

Morgan Stanley assesses there are limited impact from the pandemic, largely because mine disruptions are predominantly in Latin America where the company is under-represented.

The company's products are classified as essential in its primary markets and Morgan Stanley expects explosives revenue will remain resilient. Nevertheless, **management expects deferrals on technology projects will cost around $7m in FY20**.

A deceleration in the taking up of technology reflects current constraints on mobility and is likely to be temporary, yet Credit Suisse assesses this will change if there is a prolonged downturn in mining profitability.

Fertiliser

Despite the improved cropping conditions across both Australia and the US, UBS believes depressed ammonia/diammonium phosphate prices will weigh on earnings throughout the second half amid excess global supply.

Fertilisers are the "swing factor", Morgan Stanley contends, noting Incitec Pivot has previously announced it will retain its fertiliser business are the best outcome for shareholders.

Fertiliser prices have begun to reflect a bear market in energy and weaker soft commodity prices. Global ammonia prices have dropped recently because of lower demand and lower gas/oil costs. Yet the cost of gas is not low enough to support the sustainability of manufacturing at Gibson Island, Credit Suisse asserts.

Credit Suisse expects fertiliser prices will weaken throughout the second half and Morgan Stanley now forecasts diammonium phosphate and ammonia, ex Tampa, will decline to US$290/t and US$240/t, respectively.

FNArena's database has two Buy ratings and four Hold with a consensus target of $2.73, signalling 31.6% upside to the last share price.

AUSTRALIA

Amcor Yield A Rarity In Current Environment

Amcor has upgraded earnings growth guidance, a rare occurrence in the current environment, and the stock's dividend yield remains a key feature.

-Synergies from Bemis acquisition underpin flexible plastics
-FY20 earnings growth of 11-12% now expected
-Strong dividend yield expected to support the stock

By Eva Brocklehurst

Amcor ((AMC)) has managed to keep its 250 plants across the globe running and supply chain on tap, in order to produce packaging for food and healthcare products with minimal disruption from the pandemic.

The flexibles division has achieved 16% growth in operating earnings (EBITA) in the March quarter amid 1% overall volume growth. Profit per unit increased, which Credit Suisse suspects was driven by the **scale benefits of North American plants and reduced discounting in a period of heightened demand**.

Ord Minnett agrees there was probably some benefit from pandemic-related demand but, nevertheless, highlights pleasing cost controls in flexible plastics, amid significant earnings growth and synergies from the Bemis acquisition.

A mix-shift towards healthcare and other high-value products also helped. Morgan Stanley assesses the benefit of pantry stocking was evident in North America while volumes were constrained by lockdowns in China and India, expected to normalise in the fourth quarter.

Rigid plastics were somewhat mixed, the broker points out, with revenue declining -4% and the division returning to profit growth, albeit supported by restructuring benefits. Credit Suisse had suspected the closures of premises using rigid plastics would affect volumes but this has turned out to be less severe than feared.

There is some uncertainty regarding the extent of panic buying skewed to PET items, such as water, while investors remain concerned about substrate switching, although Morgan Stanley can find no evidence for this to date.

For the first time the company has reported on a quarterly basis, with underlying net profit up 36.5%. Amcor now expects FY20 growth of 11-12%, upgrading from previous guidance of 7-10%.

UBS points out around two thirds of this upgrade is a result of lower borrowing costs. Guidance now implies a strong fourth quarter, which Amcor expects will be supported by seasonal demand in the northern hemisphere.

Morgans continues to find valuation attractive for such a high-quality defensive business. The broker's underlying forecasts remain broadly unchanged for FY20-22, as upgraded assumptions for flexibles are offset by adverse FX movements. Rigids are downgraded because of a softer outlook for beverages.

The lingering concern for Ord Minnett relates to the top-line performance, although if trends in the third quarter can be sustained then multiples should re-rate. There is also **ample opportunity for the company to grow ahead of peers because of Bemis synergies, sustainability efforts and further acquisitions or buybacks**.

Valuation

Morgan Stanley welcomes the delivery of synergies and considers the upgrade to guidance a significant positive development, implying upside to forecasts.

The broker highlights the dividend yield, noting this is an increasingly scarce attribute in the current environment. Similar to the situation post the GFC, Morgan Stanley expects the sustainable and growing yield to be in focus against a backdrop of low interest rates.

UBS also lauds the benefits of the company's geographic spread and its leading position across the global consumer packaging market. Moreover, earnings resilience and a strong dividend yield will support the stock, particularly in an environment where cyclical industrial stocks are facing both downgrade risks and deferred dividends. Still, valuation is a stumbling block and the broker retains a Neutral rating.

FNArena's database has six Buy ratings and one Hold (UBS). The consensus target is $16.46, suggesting 17.6% upside to the last share price. The dividend yield on present FX values for FY20 and FY21 is 5.1% and 5.5%, respectively.

AUSTRALIA

CSR On Firm Footing But Outlook Unclear

CSR has shown only a modest impact from the pandemic and housing downturn so far but caution is urged as the outlook is far from clear.

-Able to withstand a prolonged downturn
-Caution is warranted as timing & extent uncertain
-Hedging efforts put aluminium on a firm footing

By Eva Brocklehurst

CSR ((CSR)) has managed, to date, to shrug off the housing slump and suppressed demand, posting profit and earnings in FY20 that defied more bearish expectations.

There was no final dividend declared, and no FY21 guidance offered, although Credit Suisse notes guidance was not provided at the FY19 result either. The broker does not expect a dividend in FY21 and also notes the company has paused its buyback.

Given the net company's cash position, Morgan Stanley was surprised by the dividend suspension but suspects this may be just the company taking a conservative stance, ahead of potentially difficult conditions later in the year.

Both the lack of a buyback and the dividend suspension are understandable, Ord Minnett asserts, given a weak outlook for building materials. The broker removes dividend estimates for the first half of FY21, while Citi assumes a modest 8.5c will be paid in FY21.

Citi observes the company is trying to create a more variable cost structure in its building product division and, given the net cash position, expects opportunistic acquisitions could be considered over the next year.

Credit Suisse acknowledges the stock has confounded sceptics and upgrades to Neutral. UBS also suspected social distancing measures would have slowed general activity in building to a greater degree but expects a trough in revenue is still to come, forecasting a fall of -18% in FY21.

While the company has indicated it can do more on margins this will depend on the depth of the trough. UBS forecasts margins to trough at 9.3% in FY21. Nevertheless, the broker takes comfort in the balance sheet and the proactive management of costs, allowing the company to withstand a prolonged downturn.

Wilsons was encouraged by the results, which revealed **market share growth and margin resilience in building products**. The broker remains confident that the robust balance sheet, aluminium hedging profile and attractive portfolio of property will provide support. As a result, the broker, not one of the seven monitored daily on the FNArena database, upgrades to Overweight from Market Weight with a target of $4.87.

Building Products

Building product revenues are down just -3% in the first six weeks of FY21. However, CSR's volumes have outperformed the market by more than 10% in FY20 and this is attributed to its product breadth and commercial segment gains.

The company has also indicated it does not expect commercial building projects to slump, pointing to the benefits from increasingly diversifying end market exposure into the commercial market.

Credit Suisse had always expected construction would withstand the early stages of the pandemic but now assumes CSR materially outperforms. That said, an expected -20-30% decline in volumes in residential/commercial construction over the next two years precludes a more positive view.

To Morgan Stanley the key to the outlook is the degree to which the pandemic affects an already-declining housing cycle and, hence, caution is warranted, although upgrades to Equal-weight. Management has signalled it expects an impact from the downturn at some point in FY21 and Morgan Stanley would also expect a risk to volumes as the final stages of the apartment boom ebb way.

Aluminium

Meanwhile, the company's hedging efforts and reduced input costs have put the aluminium business on a firm footing. CSR has hedged 63% of its output at $2826/t versus the spot price of $2250/t. Alongside CSR's updated aluminium price hedging, Credit Suisse now forecast FY21/20 to average realised prices of $2796/t and $2922/t, respectively.

UBS highlights an agile and disciplined trading division that has taken full advantage of the volatile conditions. While accepting investors do not buy CSR for the aluminium business, the broker welcomes the incremental improvements.

The superior hedging position and raw material benefits have contributed to a large upgrade to Ord Minnett's estimates. Further upside is expected to stem from either residential demand or building product prices being better than forecast. Cost relief for electricity at the Tomago smelter could also be supportive.

UBS lowers expectations for aluminium because of lower global demand, although agrees the better-than-expected hedging profile will help to boost earnings in FY21 and FY22.

The database has two Buy ratings and four Hold. The consensus target is $4.05, suggesting 8.7% upside to the last share price.

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AUSTRALIA

Deteriorating Economy Holds Concerns For CBA

Amid a deteriorating economic environment and with high collective provisioning, the final dividend outlook for Commonwealth Bank is unclear.

-Margin management key in a low interest-rate environment
-Volatility in risk-weighted asset inflation of concern
-Final dividend amount/payment uncertain

By Eva Brocklehurst

Commonwealth Bank ((CBA)) provided few surprises in its March quarter update, given much of the speculation in recent weeks has been on the deteriorating economic environment and the impact on bank lending.

The bank saw no income growth in terms of the quarterly average, as a small amount of loan growth was offset by margin decline. Non-interest income fell by -2% because of lower fees and lower markets income.

The bank has sold 55% of its superannuation and investment business, Colonial First State (CFS), to KKR for $1.7bn, which implies a total valuation of $3.3bn. Citi points out this transaction is not a divestment, as both entities are committed to a significant investment program, but the price is "surprisingly strong". A commitment to accelerate investment also suggests wealth management will stay part of the business for the foreseeable future.

Commonwealth Bank has also received final regulatory approval for the divestment of its interest in the Indonesian PT Commonwealth Life, with completion expected in June. This is also expected to provide a small benefit to the bank's capital position.

The main issue for the bank, Macquarie assesses, is margin management in a low interest rate environment. The broker estimates this will provide a material drag on revenue of around -$1.9bn over the next five years.

Commonwealth Bank has outperformed other major banks by over 9%, Morgans notes, since the pandemic outbreak. The broker also ascertains the quality of the retail franchise shows through in this latest update, with above-system growth in both home lending and household deposits. Nevertheless, the stock is expensive and the broker acknowledges other major banks are likely to outperform.

Bell Potter suggests underlying asset quality remains sound, excluding the pandemic-related provisions. There is sufficient capital, funding and the sale of the CFS stake takes the CET1 ratio back to the top end of APRA's preferred range.

UBS regards the CET1 ratio was the most disappointing element of the update, at 10.7% versus a forecast of 11.1%. The asset sales the bank announced are expected to add 66-77 basis points to CET1, which the broker acknowledges will support the ability to maintain a dividend despite the increase in RWA (risk-weighted asset) inflation.

This should allow CBA to also remain above the "unquestionably strong" benchmark for CET1. Macquarie also estimates the bank will still generate around 30 basis points of capital in the fourth quarter adding to the benefit to CET1 from the divestments.

In terms of asset quality, CBA appears slightly less exposed to retail trade and hospitality compared with its peers but Macquarie estimates exposure to the energy sector is much greater. Moreover, while the bank did not provide details of its riskier exposures, the broker understands there is a **large exposure to the air travel industry because of the aeroplane leasing portfolio**.

Credit Provisioning

Collective provisioning for credit risk-weighted assets (CRWA) is now the highest of the major banks, alongside Westpac ((WBC)). From this perspective, Morgans notes these two banks are relatively robust.

The additional $1.5bn in additional collective provisioning takes the total loan loss provisions for CRWA to 1.65%, ahead of peers. Citi suggests economic forecasts from the Reserve Bank of Australia may have had an influence on the bank's decision to top up provisioning.

The volatility in RWA inflation has concerned both Credit Suisse and UBS. The latter highlights the extent to which banks rely on models to estimate credit provisioning, capital adequacy and liquidity and undertake stress tests and notes these models are unproven through the sort of issues currently being experienced, and the market needs to be mindful of this. Both brokers also remove buyback expectations from forecasts because of RWA inflation.

The bank's dominant position in retail lending has enabled a higher pre-provision profit on RWA versus peers, which should underpin strong capital generation. Nevertheless, UBS points out, Commonwealth Bank remains exposed to a deterioration in mass-market credit quality and it is hard to justify an expansion of its multiple given the significant headwinds.

Dividend

Morgan Stanley believes the final dividend is likely to be cut by around -40% to $1.40m while UBS assumes the bank pays a reduced second half dividend of $1.50, representing an 80% pay-out ratio but has little confidence in forecasts because of the variability in several scenarios that could still play out.

At this point, Morgans expects no final ordinary dividend but, as a caveat, suggests that if APRA considers the macro economic outlook is better by the time of the results on August 12 then a final dividend could be declared. In the broker's view, much will centre on the timing of the domestic lockdown being lifted and the percentage of borrowers that remain in hardship.

Valuation

CLSA, not one of the seven stockbrokers monitored daily on the FNArena database, considers valuation may be stretched relative to the other major banks but this is justified because of the strength of the capital position, and the ability to pay dividends while retaining provisioning levels above its peers. There is likely to be mortgage market share growth as well and the broker has a target of $65.10 with an Outperform rating.

Macquarie disagrees and believes the results do not justify the premium valuation. **While the capital position is leading the sector, the gap to peers has narrowed**. Morgan Stanley takes the same angle, emphasising the potential impact of an increase in risk weights remains similar to peers, and believing profit trends, the credit risk profile and dividend prospects do not sufficiently differentiate the bank in order to justify the current premium multiples.

Credit Suisse also considers there is better value elsewhere while Bell Potter, also not one of the seven, has a Buy rating and $72 target. The database has two Sell ratings, four Hold and one Buy (Citi). The consensus target is $61.38, suggesting 3.8% upside to the last share price. The dividend yield on FY20 and FY21 forecasts is 5.3% and 5.7%, respectively.

AUSTRALIA

Cash-Strapped SMEs Put Pressure On Altium

Increasing stress on small businesses has made customer acquisition and subscriber growth difficult for software designer Altium and achieving FY20 revenue targets now appears unlikely.

-Low probability for achieving FY20 revenue target of US$200m
-Momentum in China still accelerating
-A successful launch of Altium365 may mitigate downward risks

By Eva Brocklehurst

Software designer Altium ((ALU)) has punctured expectations it was withstanding the pandemic-related restrictions, as the North American and European businesses have revealed more stress than previously expected.

This stems from small business customers preserving their cash, which is affecting the conversion of sales in the seasonally stronger months of May and June. The company has noted heightened signs of small businesses "in distress". This has made doing business with new accounts more challenging.

Ord Minnett is one broker that does not assume Designer licence sales will bounce back in July and reduces forecasts for FY21 and FY20 to operating earnings (EBITDA) by -7% and -11% respectively.

While Altium has retained prior subscriber guidance of 50,000 it now describes a low probability to achieving its FY20 revenue target of US$200m. Online sales functions and discounted pricing have been pushed to the fore.

The company has launched extended payment terms and discounted pricing to attract volumes although, Goldman Sachs points out this is unlikely to be material enough to damage the balance sheet. Moreover, UBS asserts a continuation of current momentum would indicate the company is on track to achieve its aspirational revenue target of US$500m in FY25, with 100,000 subscribers.

This view is underpinned by an accelerating presence in China and a more automated sales and subscription platform that drives lower churn. The Nexus business is still closing deals and the pipeline remains firm for the remainder of the fourth quarter.

Also, Tasking has performed well, Goldman Sachs notes, and should be supported by the re-opening of car manufacturing in Europe, while the Octopart website has experienced steady traffic.

The commercialisation of the relationship with Dassault is considered a material catalyst for the short term and, all up, Morgan Stanley believes any short-term decline in the stock is a buying opportunity, retaining an Overweight rating.

UBS highlights a risk that deeper levels of discounting will be required to stimulate demand, although the risk may be partially mitigated through a successful launch of Altium 365, the new cloud platform.

This provides the incremental benefit of remote work and collaboration, which is a the positive. UBS envisages a gradual reduction in discounting through to FY22 and downgrades to Neutral from Buy, given more balanced risk/return metrics.

Goldman Sachs believes the market has already anticipated the risks and would not expect material revisions to FY20 guidance at this stage. However, FY21 revenue forecasts could be under review, although the broker believes 18% growth is achievable albeit likely to be weighted to the second half. Goldman Sachs, not one of the seven stockbrokers monitored daily on the FNArena database, has a $34.55 target with a Neutral rating.

Bell Potter, also not one of the seven, makes several changes to its valuation to allow for a downgrade to earnings estimates and the withdrawal, effectively, of the aspirational revenue target for FY20, retaining a Hold rating with a $35.00 target. The database has two Buy and two Hold ratings. The consensus target is $36.43, suggesting 4.6% upside to the last share price.

See also, Long-Term Opportunity In Altium on March 18, 2020.

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.

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COMMODITIES

Material Matters: Energy, Iron Ore And Base Metals

A glance through the latest expert views and predictions about commodities. Energy, iron ore and base metals.

- Oil demand projected to fall -9% in 2020 with prices stabilising after 2021
- India's economic weakness to aggravate the issues facing coal and LNG
- No material impact on iron ore demand with steel not being so lucky
- All base metals facing surpluses due to demand contraction and different strategy by China

By Angelique Thakur

Crude Oil

Crude oil prices have plummeted -55-60% to date due to weaker demand with transportation, accounting for almost two-thirds of global oil consumption, inflicting the maximum damage.

This was exacerbated by the OPEC-Plus fallout with the subsequent truce, while arresting the price slide, not enough to offset the huge demand loss, note Commonwealth Bank analysts.

The International Energy Agency (IEA) predicts oil demand will fall -9% in 2020, effectively bringing it back to levels seen in 2012. Further, the agency expects oil demand to fall -30%, -26% and -15% for the months of April, May and June.

Commonwealth Bank analysts expect stockpiles to peak by June/July with Brent prices recovering to US$40/bbl by December, moving to US$55/bbl by the end of 2021 and stabilising at US$60/bbl beyond that.

Credit Suisse highlights a near term risk for the sector on the ASX, stating Brent may not be the best price indicator for Australia with energy producers here receiving a lesser price for their oil than indicated by Brent.

Downside risks include bleak demand conditions for the rest of the year along with a second wave of infections renewing lockdowns worldwide.

India and energy markets

Analysts at ANZ Bank point out that, while recovery in China's industrial activity is critical, a prolonged weakness in commodity demand from India, one of the biggest **coal** and **LNG** consumers, cannot be ignored.

India's import demand has been hit considerably due to the lockdown and consequent economic slowdown. What is worrying ANZ analysts is infrastructure spending is taking a back seat in the wake of fiscal constraints, with the government focusing more on providing social assistance.

This would delay a return back to 'normal', comment the analysts, hitting import demand for coal and LNG.

India's power generation declined by -25-35% during the first week of the lockdown along with an increase of 10% in domestic coal production during the first quarter, which together would put pressure on imports. This is significant as India represents about 20% share of the global thermal coal trade.

Prospects might even be worse for the **metallurgical (coking) coal** market, of which India consumes about 20% of global demand, well above China's 14%. The lockdowns have led to a decline in steel production with mills deferring imports earmarked for the second quarter.

The LNG market, in which India's demand contribution is second only to China's, has seen imports dropping -25% over the first three weeks of April.

Overall, ANZ analysts do not see much upside for prices of coal and LNG in the short term.

Iron Ore and Steel

The **iron ore** market, supported by stronger demand in China, has not been materially impacted from the pandemic with prices trading above US$80/t. Analysts at ANZ Bank expect exports from Brazil and Australia to pick up strongly in coming months.

JP Morgan analysts remain concerned about short term demand destruction, anticipating a surplus amounting to 100mt in 2020, most of it expected to be absorbed by China.

China's **steel** output forecast for 2020 has been cut -1.5% by JP Morgan, the first contraction since 2015, due to high inventories and a slump in export demand. Data excluding China is even worse with steel production down -10.6% year on year and 2020 output forecasted at -8.3%.

The analysts also point out the Pilbara operations of Fortescue Metals ((FMG)) are unaffected by covid-19 with the group upgrading guidance.

In terms of 2022 earnings forecast, Citi is positive about both BHP Group ((BHP)) and Rio Tinto ((RIO)), expecting high return on equity (ROE), even while expecting the iron ore price to decline to US$60/t in 2022.

The same cannot be said about BlueScope Steel ((BSL)) and Sims Metal Management ((SGM)) with Citi expecting low ROE and a low margin for both.

Commodity analysts at Citi anticipate higher prices but not much to cheer for Australian producers as the AUD is expected to rise in tandem.

With the AUD expected to strengthen in 2022 to US$0.71, the predicted 16% improvement in the Citi Commodity Index would not translate to much on the ground with any benefit from higher commodity prices effectively eroded by the stronger AUD.

On Citi's assessment, sector performance will have to be driven by dividend growth and capital management rather than relying on earnings momentum alone.

Base Metals

Credit Suisse analysts do not foresee a V-shaped recovery in base metals once the global economy comes out of lockdown.

Rather, plummeting consumer confidence, unemployment and withdrawal of investment by companies point towards creation of a demand gap and the analysts believe the world will enter global recession.

China's copper-intensive 'new infrastructure' projects which include 5G networks, industrial internet and data centres among others are expected to offset any **copper** demand reduction in 2020. But Credit Suisse foresees copper surplus of more than 1mt per annum in the first half of FY21 with demand contraction expected to play spoilsport.

Nickel has a better outlook with analysts at Credit Suisse expecting prices to be around US$5.50/lb for 2020 and, unlike other base metals, expected to increase to US$6/lb in 2021 due to some surplus and rebounding demand.

Overall, the analysts expect huge volume surpluses for all metals this year, predicting a contraction in metal demand similar to that seen during the GFC.

The difference this time would be the strategy adopted by China, which, instead of bailing out commodities like it did during GFC, is resorting to measures like targeted spending, low interest corporate loans, tax relief and consumption vouchers, among others.

FEATURE STORIES

Covid-19: How Will The Recovery Play Out?

As economies begin to tentatively reopen in Australia and across the globe, analysts consider the possible bounce-back scenarios and sector and stock winners and losers.

-Not much to compare to
-The China experience
-Work and play variations
-Falling earnings forecasts
-Winners and losers

By Greg Peel

Lessons From History

While the world has experienced many an economic shock in the past century – the most recent being the GFC – all agree the Covid-19 shock is like nothing ever experienced in our lifetimes, given it is a health-based crisis, not a common or garden financial sector crisis or cyclical blow-off. To make any sort of comparison we have to go back to 1919.

The Spanish flu, which originated in the US and had nothing to do with Spain whatsoever until it arrived in that country before spreading to the UK – hence the (derogatory) label, is not a great comparison, being back in another era altogether, but it's all we've got, and importantly it did feature social distancing and economic shutdowns.

At least for a period. Once restrictions were lifted, multiple outbreaks reappeared – a cautionary tale.

The only viable data in 1919 were generated in Sydney, hence Macquarie has made comparisons to the Covid experience only for NSW, which has been the worst hit state anyway. The broker found that adjusting for population, the Spanish flu produced four hundred times more cases in NSW than Covid, and resulted in three hundred times more deaths.

Notwithstanding a second Covid wave we don't know about yet. And one need only point to technological advances in the meantime, not just medically but in rapid-speed communications, in order to downplay the variation. The Spanish flu tracing app didn't get many takers.

Interestingly, Covid is set to send the country into an economic recession greater than any in our lifetimes in terms of depth, albeit balanced in likely duration. Macquarie can find no evidence of there even being a bear market in 1919. The 2020 pandemic followed (nearly) thirty years of uninterrupted economic growth. In 1917 Australia's GDP fell -3% and in 1918 -4% (bit of a war on). In 1919 the economy actually grew as wartime restrictions were lifted.

So can we learn anything? Not really. Macquarie draws only upon the last two decades to note valuations are high at present, particularly in comparison to contractions over that period. The broker continues to suggest investors upgrade the quality of their portfolios.

For now, Macquarie believes the Australian market will remain range-bound between the March low and April high.

FIFO

While the Covid crisis is unlike no other in our lifetimes, and the Spanish flu is too long ago to be worthy of comparison (other than second wave risk), we can draw upon a more immediate experience – FIFO. Nothing to do with airborne mine workers, but rather First In-First Out.

Australia ramped up to full lockdown in March. In mid-February, lockdowns in China were already being lifted. Not everywhere in the country – lockdowns lingered longer in more impacted provinces – but the experience at the source provides some level of guidance as to what Australia might expect as it, too, begins to gradually reopen.

There are good reasons to question China’s infection rates, Morgans notes, but unquestionable economic trends can be reliably analysed. The broker also suggests that if the virus was still rapidly spreading in China, Beijing would have not pushed for a reopening, and nor could any exponential increase be able to be covered up for a full two months.

The rebound in activity in China was fairly rapid. And the rebound was actually initially held back by the fact the lockdowns had trapped workers who had returned to hometowns for what were meant to be Lunar New Year celebrations. Even so, by early March it was evident, Morgans notes, that mid-February re-openings had led to a substantial recovery in activity across different sectors.

Morgans does not draw upon government-generated monthly data but on real-time indicators such as passenger numbers on subways, long distance travel, property sales and power output. A simple average of these four indicators reveals a 22% increase from 2019 levels after the restart in mid-February, rising to 52% by mid-March.

The recovery has nonetheless been uneven. Power demand has recovered 90% from the level a year ago, reflecting Chinese industrial activity, while service sector activity, as suggested by the other three indicators, has been more subdued. This makes sense, Morgans offers, given services depend more on social interaction and concerns about infection will linger.

If we translate this into Australian terms, Morgans suggests we could see a quick restart for industries such as resources, construction and manufacturing, but a more subdued start for service-oriented industries such as office REITs, travel, entertainment, bricks & mortar retail and non-essential health services.

As policymakers continue to roll out new support measures – both the government and the RBA are basically in “whatever it takes” mode – it is unlikely the pandemic will morph into a full-blown financial crisis, Morgans believes. Yet the ultimate impact on corporate balance sheets remains beholden to the uncertainty of how quickly the virus can be brought under control and thus how quickly economic activity resumes.

Equities are unlikely to stage a sustained recovery, Morgans warns. The stock market may have bounced back 25% but that does not imply investors can stop exercising caution when picking stocks.

The broker continues to favour companies with the strongest competitive/market positions, the strongest balance sheets and offering strategies that are able to adapt to the “new normal” and reposition in order to thrive through an eventual recovery. Investors should hold their nerve, as rare opportunities may present in the coming weeks and months.

To Work and to Play

Citi's economists point out the obvious that different sectors will experience a diversity of recoveries. Adopting a global perspective, Citi divides all sectors roughly into two groups – "work" and "play".

Sectors associated with "play", or "unstructured" activities, include those that suffer most from social distancing, and may experience deeper contraction and/or slower recoveries than those associated with "work" or "structured activities", for which social distancing has less of an impact.

Play sectors include hotels and restaurants, air travel, arts, recreation, personal services and retail.

Work sectors include financial services, business services, and "high tech".

Manufacturing is the odd sector out in global terms (not so much in Australia, where manufacturing is minimal), given the outsized scale of manufacturing in China and Western Europe in particular and the industry globally. The industry comes under the "structured" label, but significant declines in activity due to the virus suggest a longer recovery period.

We could look at this as a social distancing factor, given the necessary proximity of workers on factory floors (unless they're all robots).

Citi's base case scenario is that the global economy bottoms in the June quarter and begins to rebound in the second half of 2020. A more rapid rebound could be seen if economies lift lockdown and social distancing restrictions in the June quarter *and* the lingering fear factor among workers and consumers is low enough as to provide for faster normalisation of activity. This would suggest a V-shaped economic recovery.

More popular among pundits is an expected U-shaped recovery, based on fear lingering into the second half of the year, leading to lengthier disruptions in activity and/or a significant lag in a return to normal consumer demand.

Citi's worst case scenario is one in which monetary and fiscal policy measures fail to overcome the economic impact. This would suggest an L-shaped recovery, which isn't a recovery at all, rather a Depression.

The Earnings Lag

During the GFC, note the strategists at UBS, the stock market's price level troughed when the speed of earnings per share (EPS) forecast downgrades overtook that of the net share price fall. In this crisis to date, the market has rebounded as EPS downgrades have accelerated. This suggests the market is looking through the earnings downside and may have already launched a longer lasting recovery, UBS suggests.

In FNArena's last feature story, *The Outlook For the Economy And Stock Market* (https://www.fnarena.com/index.php/2020/04/29/the-outlook-for-the-economy-and-stock-market/), it was noted that each day brings more and more EPS downgrades from the seven brokers in the FNArena database. However, this does not mean that brokers are downgrading forecasts again and again for the same stocks, as they foresee a grimmer picture than previously assumed, but rather that with some 400 stocks under coverage across seven brokers, and one single factor impacting on *all* stocks one way or the other, re-analysing them all in the face of the virus simply takes time.

And there are many fewer analysts employed by brokers these days as there were before the GFC, implying the one analyst now has more stocks to analyse.

Here we are in May, and still analysts are updating their views and downgrading forecasts and target prices for stocks they last updated in the February result season, back when the virus was clearly just a Chinese problem. There have indeed been some updates leading to forecast *upgrades* on a second review, from initially dire expectations, but the conclusion remains that the accelerating EPS downgrades to which UBS refers is more about catching up across all stocks than applying increasingly negative views. (UBS is one of the seven, by the way.)

And having said that, analysts have admitted that EPS forecasts are a bit of a shot in the dark, in many cases, given the sheer uncertainty of virus impact and duration, and a lack of any guidance from the company itself for the same reason.

Thus if we return to UBS' observation about the GFC – that the market bottomed out when EPS downgrades accelerate -- we must take into account the lag factor in analyst updates.

Nonetheless, the UBS strategists note the recovery for the stock market has been extremely rapid and their own analysis suggests further EPS downgrades ahead. Therefore they believe it makes sense to look for sectors in which valuations and EPS forecasts are further along the process of digesting the crisis.

The sectors which have seen the largest EPS downgrades compared to the GFC (the two crises being very different), and for which price/earnings (PE) ratios have already begun to re-rate are gaming, technology and general industrials. Discretionary retail has also begun to re-rate. Insurance and media also stand out but for these sectors UBS is more cautious.

UBS' analysis suggests the market EPS forecast is likely to see ongoing downgrades for at least the next month (writing a week ago). The strategists' model indicates that insurance, media and transport could still experience larger EPS downgrades ahead.

Clearly the Covid downturn is different to the GFC, notes UBS, and is likely to be more temporary. That means 2021 growth rates should not turn negative the way 2009 growth rates did during the GFC. However, in Australia, consensus EPS forecasts are generally revised lower over the course of the year, with negative revisions accelerating into the August result season, and then again as we approach the February result season the following year.

Another point to note with regard EPS is the sheer number of companies raising fresh capital in response to the crisis. Some have gone to the market out of desperation, some out of caution, and others opportunistically to provide for a chance to pick off the weak from the sector herd as the fallout continues.

New capital implies an increase in "S" – the number of shares on issue – which means EPS will fall if "E" remains constant. Analysts have been downgrading their earnings per share expectations, and then having to downgrade them again given a greater number of shares.

EPS in most cases informs DPS – dividends per share, and thus yield – given most companies distribute on the basis of a payout ratio (of EPS). Some pay fixed values, until adjusting that fixed value, and others pay out more or less dependent on growth plans or otherwise, but for the bulk, payout ratios are the norm.

As EPS falls, so too does DPS on a payout ratio basis (and again on capital raisings). Of course, this observation is all but redundant at a time so many companies have abandoned, suspended, deferred or slashed their dividends, if not just for this period but for the next as well. A combination of lower EPS forecasts, leading to lower analyst target prices, and lower or no dividends, means a big impact on forecast total shareholder return (capital gain plus dividend) for investors.

<u>Reasons to be Cheerful</u>

While UBS is only one of many warning Australia's stock market V-bounce from the March bottom, to roughly half way back, is underestimating the economic realities ahead, which most foresee will trace out more of a U than a V, stockbroker Baillieu remains convinced the economy will indeed V-bounce to match the stock markets' forward-looking expectations.

Baillieu provides five reasons.

First is Australia's world-leading success in containing the virus in just five weeks. Not sure about world-leading – the Kiwis might argue – but certainly right up there. As Baillieu points out, Australia has dramatically outperformed Western peers, with the likelihood of dying from the virus 95x higher in Western Europe and 49x higher in the US than in Australia (as of last week).

Second is Australia has satisfied the criteria for a safe restart, in terms of testing capacity, tracing capability (which admittedly relies on the app) and response capability to new outbreaks, as was successfully tested when a cluster emerged in Burnie in Tasmania.

Add in a strong supply of masks and other PPE, with doctors rather than politicians driving this policy, and we've seen elective surgery recommencing, retailers reopening, states easing restrictions after just 5-6 weeks when longer lockdowns were originally assumed, and other restrictions being reviewed weekly by the National Cabinet. The timeline is consistent, Baillieu offers, with a 2-3 month disruption envisaged by the V scenario.

Four is the unprecedented monetary and fiscal stimulus that has been provided, with monetary support being near instantaneous and fiscal support now flowing to those in need.

Five is the "windfall gain" from the oil price crash. Don't tell the energy sector. Baillieu estimates current lower oil prices should add more than 1% to real GDP, with the first sectors of the economy to restart gaining the greatest cost advantage.

Finally, Australia's high exposure to the FIFO countries. China is one, as mentioned above, but Taiwan, Hong Kong and Japan were also early to go in an early to come out of the crisis in terms of restrictions, and 85% of Australia's exports are sent to Asia.

Baillieu suggests the hardest hit of Australia's sectors will be the key winners from a restart of the economy. These include non-essential retail, pubs, clubs and restaurants, leisure and entertainment, travel and tourism.

From a listed stock perspective, Baillieu highlights three sector winners and two losers as restrictions are eased.

Discretionary retail is a winner, as stores reopen. Not just clothing and electronic goods but cars as well.

Gaming wins, given the two casino owners have seen earnings disappear in the lockdowns while Tabcorp ((TAH)) lost all its pub/club gamblers, albeit picking up some online players.

Domestic tourism and transport wins. Too late to save Virgin Australia, or to ward off deeply discounted capital raisings from the likes of Flight Centre ((FLT)), but Qantas ((QAN)) will rise anew (noting the airline generates more profit from domestic than international), and hotel/leisure businesses such as Event Hospitality & Entertainment ((EVT)) and Village Roadshow ((VRL)) should benefit.

Losers include international travel and tourism, given international travel is likely to remain severely constrained until a vaccine is developed, hopefully by next year. This will still weigh on Qantas, and on Flight Centre and peers.

The other is food retailers. But only in the sense that following their time in the sun even before the lockdowns began, in the days of toilet paper madness, business will now return to normal as the frenzy abates and home eating gives way to eating out once more.

Large parts of the economy will be unaffected by restarts, points out Baillieu, given they have remained "essential" during the crisis. Mining and energy, agriculture, manufacturing and construction have seen little impact form lockdown policies and as such, should see little benefit as lockdowns ease.

Breaking it down further from sectors to industries, Baillieu identifies seven likely to benefit.

Banks. The banks have taken large provisions against anticipated bad debts and following pressure from the regulator, raising capital and/or deferred dividends. Valuations have de-rated to below net tangible asset value, suggesting the downturn is expected to be a capital event as well as an earnings event. By contrast, says Baillieu, a V-shaped recovery should limit such losses, and even a U-shape should not drive the banks into losses.

Beverages. The likes of Coca-Cola Amatil ((CCL)) and Treasury Wine Estates ((TWE)) have still been selling their products through supermarkets and their bottle shops, but these sales are low margin compared with on-the-go drink sales and restaurant wine sales. They will benefit from reopenings.

Discretionary retail. The likes of Premier Investments ((PMV)), Myer ((MYR)), Accent Group ((AX1)), Adairs ((ADH)) and Kathmandu ((KMD)) are all in the process of reopening, which will also aid retail landlords such as Scentre Group ((SCG)) and GPT Group ((GPT)).

Leisure. As suggested, Crown Resorts ((CWN)) and Star Entertainment ((SGR)) will go from zero to slowly back to business, also assisting Aristocrat Leisure ((ALL)), while Tabcorp will see pub punters return.

Transport and infrastructure. Qantas will benefit competitively against whatever version of Virgin Lite might re-emerge. Domestic planes back in the sky and cars on the road will reignite Sydney Airport ((SYD)) and Transurban ((TCL)).

Technology. Many up and coming tech companies have actually benefited from the crisis but the big online classifieds providers have suffered. Thus Seek ((SEK)), REA Group ((REA)), Domain Group ((DHG)) and Carsales ((CAR)) will see business gradually return.

Housing. The housing downturn expected from the virus will come with a lag, as there has been little evidence so far. Record low interest rates will not be able to offset hits to income and confidence. But the earlier the restart, the sooner lower-for-longer rates will provide support.

Baillieu has handily provided a list of ten, flowing on from the above analysis, which the broker calls "Ten stocks for an Australian restart".

They are Commonwealth Bank ((CBA)) and Westpac ((WBC)), Wesfarmers ((WES)) for Bunnings and Officeworks, Star Entertainment, Event Hospitality & Leisure, Qantas, Transurban, Reece ((REH)), for a rebound in plumbing services, Rea Group and Seek.

WEEKLY REPORTS

Weekly Ratings, Targets, Forecast Changes - 08-05-20

By Rudi Filapek-Vandyck, Editor FNArena

Guide:

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

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

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

Summary

Period: Monday May 4 to Friday May 8, 2020
Total Upgrades: 15
Total Downgrades: 15
Net Ratings Breakdown: Buy 49.64%; Hold 41.30%; Sell 9.06%

Upgrades and downgrades for individual ASX-listed companies were in perfect balance for the week ending 8th May 2020.

FNArena counted 15 for each change in recommendation by the seven stockbrokers monitored daily.

Upgrades were mostly reserved for stocks that haven't as yet fully participated in the share market rally, though strong results from the likes of Collins Foods and Pushpay Holdings equally attracted one upgrade to Buy.

Qube Holdings received two upgrades during the week. Only one of the 15 upgrades did not move higher than Hold/Neutral. The recipient is Medibank Private.

On the opposite side of the ledger, JB Hi-Fi stole the show with no less than three downgrades following a strong result release which came with an equally strong share price performance.

Other stocks receiving downgrades include Transurban (2x), Alumina Ltd, ResMed, Seek and coal producer New Hope Corp.

Four of the fifteen downgrades shifted to a fresh Sell.

The week's overview for positive amendments to price targets reveals four stand-outs, led by Fortescue Metals and JB Hi-Fi.

As expected, there is a lot more to observe on the negative side. Virgin Money UK suffered the biggest hit for the week, followed by Austal, Infigen Energy and AP Eagers.

Though the balance is similar for earnings estimates, the news is considerably better with the week's table for most positive revisions showing sizeable increases for the likes of PushPay Holdings, Alacer Gold, Crown Resorts and Tyro Payments.

Negative revisions are still multiple times larger and here Air New Zealand crowned itself the week's biggest loser, followed by Qantas, Virgin Money UK, and AP Eagers.

Out-of-season reporting season in Australia is now in full swing and investors' focus will be firmly focused on

CommBank (trading update, not a financial result), Pendal Group, Amcor and Xero this week.

Upgrade

ADAIRS LIMITED ((ADH)) Upgrade to Add from Hold by Morgans .B/H/S: 2/0/0

A 221% surge in online sales has helped to offset sales losses due to Adairs store closures, netting to total sales down -37% in five weeks, Morgans notes. Stores are set to progressively reopen over May-June, and liquidity is sufficient to ensure no intention to raise capital.

While earnings forecasting remains difficult, the company's liquidity position and online strength lead the broker to increase its target to $2.17 from $1.22, and upgrade to Add from Hold.

AGL ENERGY LIMITED ((AGL)) Upgrade to Add from Hold by Morgans .B/H/S: 1/3/3

Australia's electricity demand looks to be resilient in the face of the virus, Morgans suggests, but the challenge for retailers will be a spike in bad debts. Weaker wholesale prices have not much impacted default retail pricing.

The broker sees increasing value in AGL Energy and Origin Energy. The broker upgrades both to Add from Hold on share price weakness. AGL target falls to $17.15 from $17.39.

BEACON LIGHTING GROUP LIMITED ((BLX)) Upgrade to Add from Hold by Morgans .B/H/S: 2/0/0

Beacon Lighting is the only retailer under Morgans' coverage not to provide a virus-related update. This is possibly because as a trade supplier, Beacon's stores have remained open.

The broker suspects stay-at-home demand may have buffered earnings, supported by a lack of large scale competition.

Consumer sentiment will no doubt remain volatile as the reality of high unemployment and a weak economy hit home, but Morgans upgrades to Add from Hold on valuation. Target falls to 93c from 97c.

COLLINS FOODS LIMITED ((CKF)) Upgrade to Buy from Neutral by UBS .B/H/S: 2/0/0

UBS observes the company's KFC Australia business appears to be one of the better performing fast food operations during this pandemic. The business was an early beneficiary from the easing of lock-down restrictions.

It is also likely to be a beneficiary of domestic car-based holiday activity when this resumes. UBS considers the stock has defensive qualities and the multiples are not overly demanding.

Rating is upgraded to Buy from Neutral and the target reduced to $8.95 from $10.60.

CLEANAWAY WASTE MANAGEMENT LIMITED ((CWY)) Upgrade to Add from Hold by Morgans .B/H/S: 4/2/0

The virus impact on Cleanaway Waste Management's operations has largely netted out to flat, given falls in demand for collections in Commercial & Industrial, other than supermarkets, have been offset by increased residential collections. The company says it's still on track to meet prior FY20 guidance but has withdrawn guidance nonetheless.

Morgans assumes relatively flat earnings across FY20-21 before lifting again from FY22. Target falls to $2.12 from $2.17, upgrade to Add from Hold.

GROWTHPOINT PROPERTIES AUSTRALIA ((GOZ)) Upgrade to Outperform from Neutral by Credit Suisse .B/H/S: 2/1/0

Credit Suisse considers the stock at a relatively attractive entry point for those wanting metropolitan office and industrial exposure. Government tenants contribute 24% of income, listed entities 57% and large private companies 15%.

The broker cannot rule out an equity raising, as sector peers with gearing of over 30% have recently raised equity, largely for defensive reasons, but considers Growthpoint, being internally managed, has less incentive to do so.

Rating is upgraded to Outperform from Neutral and the target is reduced to $3.15 from $4.28.

MEDIBANK PRIVATE LIMITED ((MPL)) Upgrade to Hold from Lighten by Ord Minnett .B/H/S: 1/6/0

Medibank Private has highlighted the benefits from fewer claims, which Ord Minnett suggests is offset by a promise to give much of this back, although this will be difficult to assess.

The broker considers health insurers are defensive exposures in a tough time, particularly if concern around health treatments increase post the pandemic.

The broker expects a low level of claims for some time and notes dividend trends are also favourable. Rating is upgraded to Hold from Lighten. Target is steady at $2.70.

MONASH IVF GROUP LIMITED ((MVF)) Upgrade to Add from Hold by Morgans .B/H/S: 2/0/0

Monash IVF was performing in line with expectations through to late February, but March saw a material slowdown. The government's permission to reopen IVF clinics from April 27 will lead to a gradual return to normal, Morgans suggests.

Monash has raised $80m to clear debt concerns and provide for acquisitions. Target falls to 63c from 83 on dilution. Upgrade to Add from Hold.

NICK SCALI LIMITED ((NCK)) Upgrade to Outperform from Neutral by Macquarie .B/H/S: 2/0/0

Macquarie has been out visiting furniture stores in Sydney -- both Nick Scali and small unlisted competitors -- to find that while sales in some stores were down over -50% at the low point, the last two weeks of April saw a pick-up in foot traffic. Declining housing turnover will nevertheless remain a headwind.

The broker suggests the drop in activity is not as bad as the market is assuming, and a well-managed Nick Scali, with meaningful property ownership, has an opportunity to pick up market share, and larger furniture businesses may end up swallowing up struggling SMEs if the situation gets worse. Upgrade to Outperform from Neutral.

Target falls to $5.20 from $5.30.

ORIGIN ENERGY LIMITED ((ORG)) Upgrade to Add from Hold by Morgans .B/H/S: 5/2/0

Australia's electricity demand looks to be resilient in the face of the virus, Morgans suggests, but the challenge for retailers will be a spike in bad debts. Weaker wholesale prices have not much impacted default retail pricing.

The broker sees increasing value in AGL Energy and Origin Energy. The broker upgrades both to Add from Hold on share price weakness. Origin target rises to $5.50 from $5.15.

ORICA LIMITED ((ORI)) Upgrade to Buy from Neutral by Citi .B/H/S: 3/4/0

Orica has a strong position in the global explosives sector because of its intellectual property, particularly in wireless blasting systems. Citi also notes the diversified earnings are underpinned by multi-year contracts with major miners.

The outlook for end markets remains mixed, but increased strip ratios in the mining industry are favourable for explosive volumes.

As the share price has fallen, and given the assessment of risk around earnings, Citi upgrades to Buy from Neutral. Target is reduced to $19.40 from $24.50.

PEOPLE INFRASTRUCTURE LTD ((PPE)) Upgrade to Add from Hold by Morgans .B/H/S: 2/0/0

People Infrastructure is raising $17.6m at $1.10 to strengthen the balance sheet in the crisis but also to provide for acquisition opportunities which are expected to emerge as a result. Morgans has slashed earnings per share and dividend forecast on dilution.

Target falls to $2.66 from $3.82. But given this still suggests 50% upside, the broker upgrades to Add from Hold.

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

FY20 results were strong. The highlight for Credit Suisse was the acceleration in digital transactions over the last six weeks, reflecting the impact of the pandemic on church attendance.

The broker assumes a strong uplift over FY21 as well, given a structural shift to digital payments. Earnings estimates upgraded 35% for FY21 and 38% for FY22.

Rating is upgraded to Outperform from Neutral and the target is raised to NZ$6.54 from NZ$4.53.

See also PPH downgrade.

QUBE HOLDINGS LIMITED ((QUB)) Upgrade to Buy from Neutral by UBS and Upgrade to Outperform from Underperform by Credit Suisse .B/H/S: 4/2/0

The company will raise $500m in new equity to reduce debt and pursue acquisitions. UBS observes the strategic value of assets and the exposure to compounding freight volumes has not changed as a result of the pandemic.

Hence, the rating is upgraded to Buy from Neutral. Qube Holdings continues to assess funding and ownership options for Moorebank. Target is reduced to $2.70 from $3.15.

Qube Holdings has announced a fully underwritten entitlement offer of $500m, reducing net debt. Following the pandemic Credit Suisse assesses attractive consolidation opportunities should emerge in the logistics sector.

The company has indicated bulk operations, 50% of revenue, are relatively unaffected by the pandemic. The partial sale process of Moorebank is proceeding, although it is likely to be slow, Credit Suisse observes.

The broker upgrades to Outperform from Underperform. Target of $2.80 retained.

Downgrade

AUSTAL LIMITED ((ASB)) Downgrade to Lighten from Hold by Ord Minnett .B/H/S: 2/0/0

Where Austal won a $324m contract to construct patrol boats for the Australian Navy, it also lost out on a US Navy contract with a starting value of US$795m rendering the long-term earnings profile of the company uncertain, comments Ord Minnett.

The outlook for the company would be a balancing act between the shipbuilding contracts from the US and Australia versus a subdued commercial ferry market, suggests the broker.

Rating downgraded to Lighten from Hold with target price decreased to $2.40 from $4.10.

ALUMINA LIMITED ((AWC)) Downgrade to Neutral from Outperform by Credit Suisse .B/H/S: 2/3/1

Credit Suisse suspects a V-shaped recovery is unlikely without a 2009-type stimulus from China to underpin commodity markets. Base metal forecasts have been reduced out to 2022.

Alumina prices are downwardly adjusted in line with a negative outlook for aluminium, which drives material earnings downgrades for Alumina Ltd over the next two years.

Rating is downgraded to Neutral from Outperform and the target lowered to $1.65 from $1.80.

DOMAIN HOLDINGS AUSTRALIA LIMITED ((DHG)) Downgrade to Reduce from Hold by Morgans .B/H/S: 5/0/1

Morgans finds the Domain Holdings share price has run too far and thus the recommendation has been pulled back to Reduce from Hold. Target price remains $2.46 but note the share price is trading well above it.

The analysts do make a point in that if trading conditions reported in April were to last longer than two months, this translates into further downside risk to consensus earnings forecasts and thus also the valuation.

No changes have been made to forecasts.

INFIGEN ENERGY ((IFN)) Downgrade to Hold from Add by Morgans .B/H/S: 1/2/0

Australia's electricity demand looks to be resilient in the face of the virus, Morgans suggests, but the challenge for retailers will be a spike in bad debts. Weaker wholesale prices have not much impacted default retail pricing. The broker sees increasing value in AGL Energy and Origin Energy.

The broker still sees medium-term value in Infigen Energy but with the growth slowing it is difficult to see catalysts in the short term to lift the share price. Downgrade to Hold from Add. Target falls to 57c from 71c.

JB HI-FI LIMITED ((JBH)) Downgrade to Neutral from Outperform by Macquarie and Downgrade to Hold from Add by Morgans and Downgrade to Hold from Accumulate by Ord Minnett.B/H/S: 1/6/0

Following the recent share price performance Macquarie downgrades to Neutral from Outperform. The stock is up 29% since March 23 and has now reached the broker's valuation.

Macquarie remains confident in the short-term outlook for revenue but is becoming more cautious about the medium-term outlook for discretionary expenditure as the economy slows. Target is reduced to $34.80 from $38.80.

JB Hi-Fi had a strong third quarter with meaningful sales growth in the JB Australia and The Good Guys businesses. Morgans believes the trend will continue till early May, further reporting no escalation in costs as well as intact gross margins.

FY20 EPS estimates revised upwards by circa 7% while reduced by -3% for FY21 on account of having to cycle strong comparables next year and potential pull-forward of demand.

Morgans is positive but cautious and downgrades its rating to Hold from Add with target price at $35.67.

Sales growth accelerated in late March and remained strong in April and the beginning of May. Despite JB Hi-Fi being a winning retailer based on category and location, Ord Minnett now envisages less valuation support.

Further upside would require more confidence in the external environment and this is difficult, given rising unemployment. The broker downgrades to Hold from Accumulate while raising the target to $37.00 from $32.50.

MIRVAC GROUP ((MGR)) Downgrade to Neutral from Outperform by Macquarie .B/H/S: 4/2/0

The broker has reviewed how the office space has performed in previous economic downturns since 1990 and now assumes declines in value of -10-15%. Incorporating asset value declines for Mirvac of -12% (office), -18% (retail) and -1% (industrial), the broker cuts its target to $2.21 from $2.68.

Mirvac has a solid balance sheet and a solid track record of returns but the broker sees limited near term upside, rather further downside for residential and greater headwinds for office and retail than are reflected in the share price. Downgrade to Neutral from Outperform.

NEW HOPE CORPORATION LIMITED ((NHC)) Downgrade to Neutral from Buy by Citi .B/H/S: 2/1/1

Coal prices have turned down sharply, with Newcastle thermal coal dropping to US$50/t and spot hard coking coal to US$109/t. The weaker prices reflect the re-start of Richards Bay exports and weaker demand from key markets.

Citi reduces New Hope's FY20 and FY21 operating earnings (EBITDA) estimates by -3% and -14%, respectively. Low coal prices and a stronger Australian dollar remain headwinds.

The broker reduces the target to $1.60 from $1.70 and downgrades to Neutral from Buy.

PUSHPAY HOLDINGS LIMITED ((PPH)) Downgrade to Neutral from Buy by UBS .B/H/S: 2/1/0

UBS notes the share price has risen 21% on the back of the FY20 result. The broker considers the current valuation fairly reflects improved demand but believes it is too early to forecast higher terminal penetration or higher revenue synergies from the CCB cross selling.

Rating is downgraded to Neutral from Buy and the target rises to NZ$5.75 from NZ$5.25.

See also PPH upgrade.

RESMED INC ((RMD)) Downgrade to Lighten from Hold by Ord Minnett .B/H/S: 1/4/1

A strong lift in mask sales meant March quarter revenue was ahead of Ord Minnett's forecast. As expected, strong demand for ventilators in the midst of the pandemic provided a boost.

Beyond the current quarter, the broker expects much weaker economic conditions will weigh on a recovery in core sleep devices, especially in the US where individual health expenditure is more closely correlated to economic conditions.

Rating is downgraded to Lighten from Hold. The target is reduced to $21.90 from $22.60.

SEEK LIMITED ((SEK)) Downgrade to Reduce from Add by Morgans .B/H/S: 3/2/1

Seek's 20% share price appreciation over the last month seems hard to fathom, Morgans suggests, as it has occurred against a backdrop of continuing declines in job ad volumes.

The broker is more bearish, erring on the side of caution given it seems obvious, to Morgans, there will no be a V-shaped recovery in ad volumes.

To that end, the broker retains a $15.55 target and double-downgrades to Reduce from Add.

TRANSURBAN GROUP ((TCL)) Downgrade to Hold from Accumulate by Ord Minnett and Downgrade to Hold from Add by Morgans.B/H/S: 2/3/2

Transurban traffic has been materially impacted, declining -60-70% for its US assets with the toll price falling to US$1.50 from US$8 per trip, observes Ord Minnett.

The traffic growth forecast by the broker for FY20 remains at -11% with DPS forecast for the second half unchanged at $0.12. The broker expects the company to rebalance capital structure at the next acquisition, increasing the dilution risk.

The stock is downgraded to Hold from Accumulate with target price at $13.50.

Transurban has indicated traffic deteriorated in early April but the deterioration has now moderated. Large vehicles continue to be more resilient and weekday traffic stronger than weekends.

Morgans makes slight upgrades to revenue forecasts, which assumes severe traffic weakness until September and a full recovery not occurring until 2022.

Upside may come from traffic recovering quicker than previously assumed as government restrictions are eased.

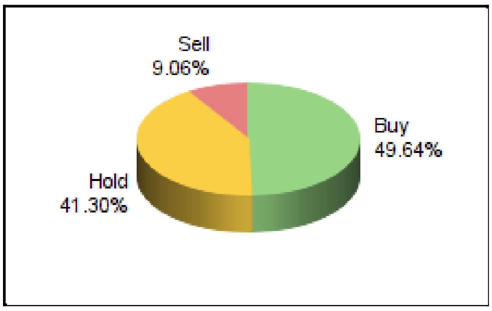
Rating is downgraded to Hold from Add as the potential shareholder returns are compressed to 1% as a result of the share price increase. Target is reduced to $13.52 from $13.71.

VIRGIN MONEY UK PLC ((VUK)) Downgrade to Hold from Add by Morgans .B/H/S: 1/2/0

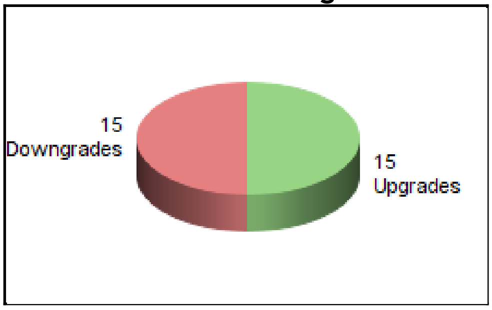
Virgin Money is due to report interim earnings on Wednesday after the bell. Morgans expects the result to beat consensus, but also sees concerns over the outlook for the UK economy continuing to weigh on the share price.

The stock is trading at only 0.3x net tangible assets but the broker sees this as fair, after significantly downgrading forecasts on the virus threat. Risk remains to the downside. Morgans downgrades to Hold from Add. Target falls to $1.44 from $4.23.

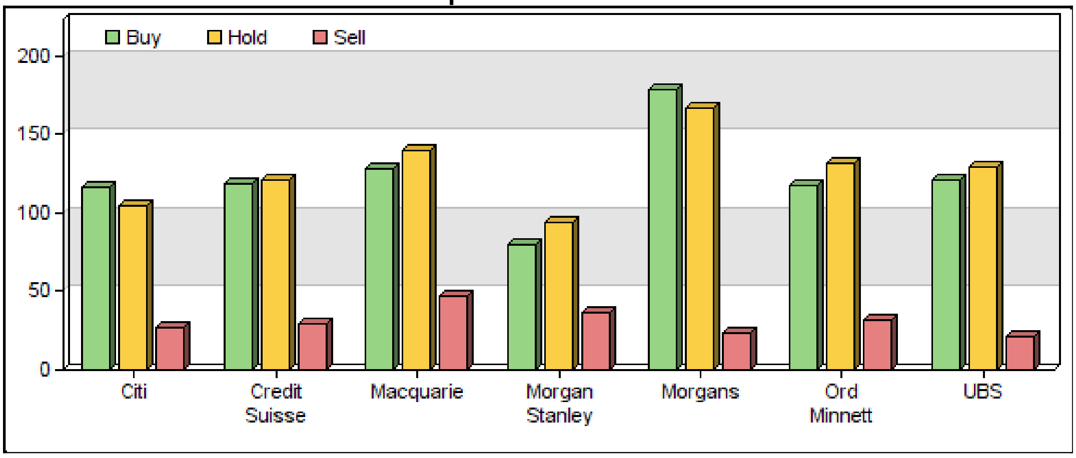
Total Recommendations



Recommendation Changes



Broker Recommendation Breakup



Broker Rating

Order	Company	New Rating	Old Rating	Broker
Upgrade				
1	ADAIRS LIMITED	Buy	Neutral	Morgans
2	AGL ENERGY LIMITED	Buy	Neutral	Morgans
3	BEACON LIGHTING GROUP LIMITED	Buy	Neutral	Morgans
4	CLEANAWAY WASTE MANAGEMENT LIMITED	Buy	Neutral	Morgans
5	COLLINS FOODS LIMITED	Buy	Neutral	UBS
6	GROWTHPOINT PROPERTIES AUSTRALIA	Buy	Neutral	Credit Suisse
7	MEDIBANK PRIVATE LIMITED	Neutral	Sell	Ord Minnett
8	MONASH IVF GROUP LIMITED	Buy	Neutral	Morgans
9	NICK SCALI LIMITED	Buy	Neutral	Macquarie
10	ORICA LIMITED	Buy	Neutral	Citi
11	ORIGIN ENERGY LIMITED	Buy	Neutral	Morgans

12	PEOPLE INFRASTRUCTURE LTD	Buy	Neutral	Morgans
13	PUSHPAY HOLDINGS LIMITED	Buy	Neutral	Credit Suisse
14	QUBE HOLDINGS LIMITED	Buy	Neutral	UBS
15	QUBE HOLDINGS LIMITED	Buy	Sell	Credit Suisse
Downgrade				
16	ALUMINA LIMITED	Neutral	Buy	Credit Suisse
17	AUSTAL LIMITED	Sell	Neutral	Ord Minnett
18	DOMAIN HOLDINGS AUSTRALIA LIMITED	Sell	Neutral	Morgans
19	INFIGEN ENERGY	Neutral	Buy	Morgans
20	JB HI-FI LIMITED	Neutral	Buy	Morgans
21	JB HI-FI LIMITED	Neutral	Buy	Macquarie
22	JB HI-FI LIMITED	Neutral	Buy	Ord Minnett
23	MIRVAC GROUP	Neutral	Buy	Macquarie
24	NEW HOPE CORPORATION LIMITED	Neutral	Buy	Citi
25	PUSHPAY HOLDINGS LIMITED	Neutral	Buy	UBS
26	RESMED INC	Sell	Neutral	Ord Minnett
27	SEEK LIMITED	Sell	Buy	Morgans
28	TRANSURBAN GROUP	Neutral	Buy	Morgans
29	TRANSURBAN GROUP	Neutral	Buy	Ord Minnett
30	VIRGIN MONEY UK PLC	Neutral	Buy	Morgans

Recommendation

Positive Change Covered by > 2 Brokers

Order	Symbol	Company	New Rating	Previous Rating	Change	Recs
1	QUB	QUBE HOLDINGS LIMITED	67.0%	-17.0%	84.0%	6
2	COF	CENTURIA OFFICE REIT	67.0%	33.0%	34.0%	3
3	GOZ	GROWTHPOINT PROPERTIES AUSTRALIA	50.0%	17.0%	33.0%	3
4	ORI	ORICA LIMITED	43.0%	14.0%	29.0%	7
5	APE	AP EAGERS LIMITED	70.0%	50.0%	20.0%	5
6	GPT	GPT GROUP	42.0%	25.0%	17.0%	6
7	CWY	CLEANAWAY WASTE MANAGEMENT LIMITED	58.0%	42.0%	16.0%	6
8	AGL	AGL ENERGY LIMITED	-29.0%	-43.0%	14.0%	7
9	FMG	FORTESCUE METALS GROUP LTD	21.0%	7.0%	14.0%	7
10	ORG	ORIGIN ENERGY LIMITED	64.0%	50.0%	14.0%	7

Negative Change Covered by > 2 Brokers

Order	Symbol	Company	New Rating	Previous Rating	Change	Recs
1	TYR	TYRO PAYMENTS LIMITED	17.0%	75.0%	-58.0%	3
2	JBH	JB HI-FI LIMITED	14.0%	50.0%	-36.0%	7
3	VUK	VIRGIN MONEY UK PLC	33.0%	67.0%	-34.0%	3
4	IFN	INFIGEN ENERGY	33.0%	67.0%	-34.0%	3
5	SEK	SEEK LIMITED	25.0%	58.0%	-33.0%	6
6	NHC	NEW HOPE CORPORATION LIMITED	25.0%	50.0%	-25.0%	4
7	ORA	ORORA LIMITED	14.0%	33.0%	-19.0%	7
8	ASB	AUSTAL LIMITED	50.0%	67.0%	-17.0%	3
9	DHG	DOMAIN HOLDINGS AUSTRALIA LIMITED	58.0%	75.0%	-17.0%	6
10	MGR	MIRVAC GROUP	58.0%	75.0%	-17.0%	6

Target Price

Positive Change Covered by > 2 Brokers

Order	Symbol	Company	New Target	Previous Target	Change	Recs
1	FMG	FORTESCUE METALS GROUP LTD	11.109	10.170	9.23%	7
2	JBH	JB HI-FI LIMITED	35.991	34.531	4.23%	7
3	DHG	DOMAIN HOLDINGS AUSTRALIA LIMITED	3.185	3.060	4.08%	6
4	ORG	ORIGIN ENERGY LIMITED	6.637	6.443	3.01%	7
5	MPL	MEDIBANK PRIVATE LIMITED	2.839	2.831	0.28%	7

Negative Change Covered by > 2 Brokers

Order	Symbol	Company	New Target	Previous Target	Change	Recs
1	VUK	VIRGIN MONEY UK PLC	1.795	3.240	-44.60%	3
2	ASB	AUSTAL LIMITED	2.960	4.117	-28.10%	3
3	IFN	INFIGEN ENERGY	0.610	0.740	-17.57%	3
4	APE	AP EAGERS LIMITED	9.040	10.296	-12.20%	5
5	GOZ	GROWTHPOINT PROPERTIES AUSTRALIA	3.553	3.930	-9.59%	3
6	COF	CENTURIA OFFICE REIT	2.580	2.797	-7.76%	3
7	QUB	QUBE HOLDINGS LIMITED	2.632	2.843	-7.42%	6
8	ORI	ORICA LIMITED	19.086	20.583	-7.27%	7
9	GPT	GPT GROUP	4.773	5.137	-7.09%	6
10	TYR	TYRO PAYMENTS LIMITED	2.933	3.150	-6.89%	3

Earning Forecast

Positive Change Covered by > 2 Brokers

Order	Symbol	Company	New EF	Previous EF	Change	Recs
1	PPH	PUSHPAY HOLDINGS LIMITED	18.757	8.244	127.52%	4
2	AQG	ALACER GOLD CORP	82.470	73.076	12.86%	3
3	CWN	CROWN RESORTS LIMITED	23.963	22.556	6.24%	6
4	TYR	TYRO PAYMENTS LIMITED	-4.700	-5.000	6.00%	3
5	PNI	PINNACLE INVESTMENT MANAGEMENT GROUP LIMITED	14.567	13.833	5.31%	3
6	JBH	JB HI-FI LIMITED	234.771	225.483	4.12%	7
7	WOR	WORLEY LIMITED	88.510	85.510	3.51%	6
8	CTD	CORPORATE TRAVEL MANAGEMENT LIMITED	35.607	34.440	3.39%	6
9	NXT	NEXTDC LIMITED	-4.050	-4.167	2.81%	6
10	SEK	SEEK LIMITED	28.832	28.165	2.37%	6

Negative Change Covered by > 2 Brokers

Order	Symbol	Company	New EF	Previous EF	Change	Recs
1	AIZ	AIR NEW ZEALAND LIMITED	-13.043	-1.004	-1199.10%	3
2	QAN	QANTAS AIRWAYS LIMITED	-15.828	-7.020	-125.47%	5
3	VUK	VIRGIN MONEY UK PLC	22.126	41.649	-46.88%	3
4	APE	AP EAGERS LIMITED	28.104	45.444	-38.16%	5
5	IAG	INSURANCE AUSTRALIA GROUP LIMITED	18.186	26.343	-30.96%	7
6	ANZ	AUSTRALIA & NEW ZEALAND BANKING GROUP	125.143	157.657	-20.62%	7
7	NWS	NEWS CORPORATION	37.248	44.594	-16.47%	4
8	MND	MONADELPHOUS GROUP LIMITED	52.230	61.596	-15.21%	5
9	IGO	IGO LIMITED	26.142	30.290	-13.69%	6
10	AWC	ALUMINA LIMITED	8.125	9.345	-13.06%	6

Technical limitations

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

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WEEKLY REPORTS

Uranium Week: Taking A Breather

After an historic monthly price rise in April, May opened with the spot uranium market calming down.

-Calm descends on uranium market
-Virus hitting global energy demand
-US production crashes

By Greg Peel

In the month of April, the spot uranium price rose almost 24% to mark the largest monthly increase in almost thirty years. In six weeks, the spot price rose 41%, being the fastest rise since 2007. Last week activity settled down.

Indeed, for the first three days of last week, nothing happened, industry consultant TradeTech reports. In the last two days, eight spot market transactions were concluded totalling 800,000lbs U3O8 equivalent. It was a more "normal" week of activity, but well down on volumes of the prior six weeks.

TradeTech's weekly spot price indicator fell -US10c to US$33.80/lb.

Producers and traders remained prominent on the buy-side, with limited interest from utilities. Traders and speculators were the main sellers.

Demand Side

The virus and associated lockdowns are expected to drive global energy demand down -6% in 2020 according to the International Energy Agency's *Global Energy Review*, based on data accumulated over 100 days. Electricity demand is expected to fall -5% to mark the biggest fall in 70 years.

Carbon emissions are expected to fall -8%, positioning renewables for unprecedented growth.

Electricity use declined an -25% per week during the period to April 14 in countries with full lockdowns. Declines in demand, and a small number of reactor outages, drove nuclear power output down -3% in the March quarter.

The EIA suggests a rapid recovery from virus restrictions could put some reactor projects back on pace, taking the expected 2020 decline in nuclear output to just -1%.

The uranium term market was also quiet, again, last week, TradeTech reports. Only a few small transactions were concluded involving late 2021 delivery. Term market demand is currently limited as utilities attempt to manage virus risks at their operating facilities, while others are in the midst of refuelling outages.

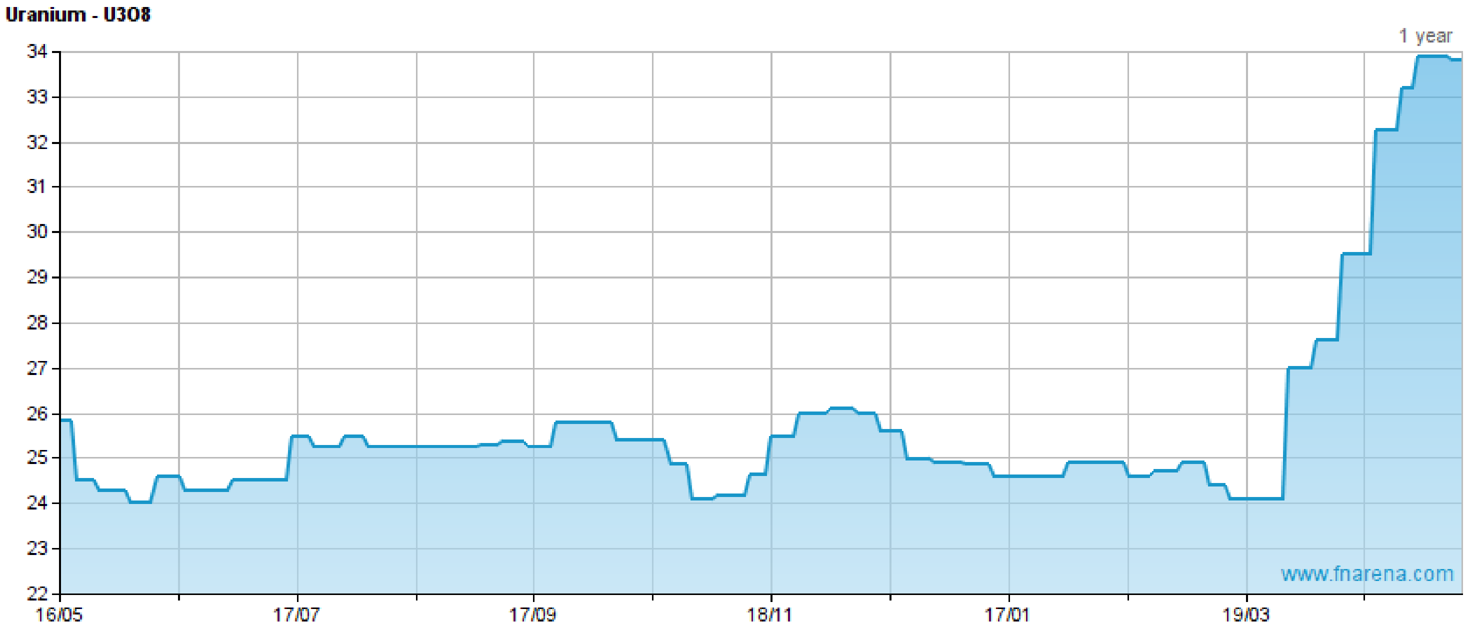
TradeTech's term price indicators remain at US$37.50/lb (mid) and US$39.00/lb (long).

Supply Side

The US Energy Administration last week noted that the March quarter saw the four operating US facilities producing 8098lbs of U3O8 equivalent, down -79% from the December quarter.

Kazahstan's state-controlled Kazatomprom reported production of 13.6mlbs in the March quarter, down -12% from the December quarter and -1% from the previous March quarter.

On the exploration side of the industry, ASX-listed uranium developer Deep Yellow ((DYL)) reported encouraging results from metallurgical test work at its Tumas Project in Namibia. The company will now begin metallurgical testing on the diamond core composites to confirm the positive outcomes returned from the drill sample test work at the project.



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

WEEKLY REPORTS

The Short Report - 14 May 2020

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

Summary:

Week ending May 7, 2020.

After what looked like a window-dressing rally to end the month of April, last week the ASX200 opened May with a -5% plunge before recovering around half of that loss.

Activity on the short side of the market continues to dwindle as the index appears to have become range-bound after its snap-back rally. Not one position changed by a percentage point or more last week.

The one highlight of the week was perennial short favourite JB Hi-Fi ((JBH)) dropping out of the 10%-plus shorted club, just, and only on a small tick down. That now leaves only three – yes, count them: three! – stocks on the entire ASX left 10% shorted or more (not counting Speedcast, now in administration).

This Report has never seen so few double-digit shorted stocks in its history. And podium topper Myer ((MYR)) is only on 14% when history suggests number one should always be around 20% shorted.

Other than that, we might notice that travel agents are back in the shorters' cross-hairs, amidst talk of international borders perhaps not being reopened this year. Corporate Travel Management ((CTD)) has crept up to over 8% shorted and Flight Centre ((FLT)), having raised capital, has reappeared in the 5% bracket.

Webjet ((WEB)) dropped out the week before, so we'll keep an eye out for its return, possibly, as well.

Weekly short positions as a percentage of market cap:

10%+
MYR 14.0
GXY 13.3
ORE 11.8

Out: JBH

9.0-9.9

JBH, PLS, CUV, Z1P, ING

Out: SUL

8.0-8.9%

BOQ, SUL, CTD

In: CTD Out: PGH

7.0-7.9%

BEN, PGH, NEA, PPT, SEK, CGF, HVN, NCZ

In: PGH, CGF, HVN Out: CTD

6.0-6.9%

MTS, SGM, HVN, MYX

Out: CGF, HVN, MYX

5.0-5.9%

MYX, GWA, CLH, FLT, LYC, NEC, PNV, SYR, BUB, RSG, AMP, CLQ, IFL, BKL

In: MYX, FLT Out: LOV

Movers & Shakers

Movers & Shakers will return when things settle down.

ASX20 Short Positions (%)

Code	Last Week	Week Before	Code	Last Week	Week Before
AMC	1.2	1.2	NCM	0.4	0.4
ANZ	0.5	0.7	RIO	2.3	2.4
BHP	4.7	4.8	SCG	0.5	0.7
BXB	0.2	0.2	SUN	0.7	0.5
CBA	0.6	0.7	TCL	0.8	0.8
CSL	0.2	0.3	TLS	0.2	0.2
GMG	0.8	0.6	WBC	0.6	0.7
IAG	0.5	0.6	WES	0.5	0.6
MQG	0.4	0.4	WOW	0.4	0.6
NAB	0.5	0.5	WPL	1.4	1.5

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

Guide:

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

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

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

IMPORTANT INFORMATION ABOUT THIS REPORT

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

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

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

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

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

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

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

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

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WEEKLY REPORTS

The Wrap: Domestic Tourism Revival & Engineers Under Pressure

Weekly Broker Wrap: Domestic tourism; migration; fund managers; E&C; consumer stocks.

- Australians looking for recreation may boost domestic tourism by 7%
- Migration expected to decline in the short term but the bark is worse than the bite
- Colonial First State deal could imply valuation upside for IOOF Holdings, AMP
- Plunging new E&C contracts due to uncertain economic outlook
- Consumer-led recovery in small and mid-cap players to kick off one quarter earlier than expected
- Online marketplace stocks still look expensive, even after the market correction

By Angelique Thakur

Hopes pinned on revival in domestic tourism

Australians made 11m international trips over the last year, spending more than $50bn. Citi analysts expect the current situation with borders closed will have people shifting towards domestic tourism, boosting the sector spending by 7%.

Ardent Leisure ((ALG)) and Village Roadshow ((VRL)) are likely to experience a boost in their theme parks division, though Citi is still cautious about Village Roadshow's cinema division due to adoption of premium/subscription-based video services during the lockdown.

A portion of the $50bn is also expected to be channelled into retail spending. Citi expects more demand for Coles ((COL)) and Metcash ((MTS)) along with a boost in performance of auto stocks like Super Retail Group ((SUL)), Bapcor ((BAP)) and GUD Holdings ((GUD)).

People are expected to prefer to drive rather than fly. This makes for a gloomy outlook for Flight Centre ((FLT)).

Migration woes with a twist

Even though March 2020 saw positive net migration, a collapse in net overseas migration looks certain with expected incoming migrants reduced by -330,000 for the next 18 months, coupled with reports of -300,000 tourists/temporary residents having left Australia by mid-April, report analysts at UBS.

The Government expects net migration to decline sharply, in excess of -30% in FY20, with an -85% fall in FY21, rebounding by 2021-end if borders are re-opened by end of 2020.

Here, Accent Group ((AX1)) and Myer ((MYR)) will be impacted due to a drop in purchases by international tourists, anticipate Citi analysts.

The situation is not as dire as it appears as the amount Australians spend overseas is almost 50% more than the amount non-residents spend in Australia, assure UBS analysts, and would more than offset any adverse impact from the loss in international travel.

In the medium to long term, given lower covid-19 infection and death rates here in comparison with most countries, UBS feels Australia would remain an attractive destination for migrants in the medium to long term.

Potential upside valuation for IOOF and AMP

The Commonwealth Bank ((CBA)) announced a 55% stake sale in Colonial First State (CFS) to KKR & Co. in a deal worth nearly $1.7bn. For now, the two giants will jointly manage CFS but Credit Suisse analysts expect the bank would give up its holding in future.

The analysts do not consider this move to be a game-changer for the platform industry and anticipate no material impact on Hub24 ((HUB)) or Netwealth Group ((NWL)) in terms of attracting flows.

The Colonial First State deal was valued at $3.3bn and indicates valuation upside for both IOOF Holdings ((IFL)) and AMP ((AMP)), with IOOF's business doing much better than CFS's as per 2019 performance, note the analysts. Both stocks are rated as Outperform by Credit Suisse analysts.

Nosedive in new contracts in Engineering & Construction

Bell Potter highlights new contracts awarded to engineers and other providers of services to the construction industry didn't reach higher than $56m in April (by Decmil Group ((DCG)) and Saunders International ((SND))), indicating a steep -90% fall from the $543m registered in March.

Bell Potter analysts draw a direct relationship with the high economic uncertainty, meaning companies are struggling for survival rather than growth.

Both oil & gas producers along with commodities producers have cut or are planning to opt for material cuts in production. The analysts at Bell Potter expect long lasting project deferrals with contractors likely to see margins materially impacted.

The analysts note the disconnect between the stimulus-propped financial markets and deteriorating economic fundamentals and believe that any rebound in the short-term would be fraught with risk.

Consequently, investors are advised to approach investments in this sector with a long-term mind set, focusing on companies with strong balance sheets and a good track record.

Of the 19 companies in Bell Potter's E&C Index, only three have maintained guidance and paid interim dividends. A focus on essential services ensuring relatively resilient revenue makes Service Stream ((SSM)) Bell Potter's favourite choice.

A consumer-led recovery

With Australia faring better than expected in dealing with covid-19, Goldman Sachs analysts have expedited their economic recovery forecast and expect a consumer-led recovery to commence during the third quarter, one quarter earlier than anticipated (expected GDP contraction of -10% for the second quarter remains intact).

The analysts are positive about a number of retail players like the Breville Group ((BRG)) with very strong fundamentals, City Chic Collective ((CCX)) playing well in its niche category and GUD Holdings, a defensive option benefited by a fall in new car sales.

The Reject Shop ((TRS)) is another potential candidate due to anticipated strong sales growth with people preferring cheaper goods in the present environment, a new management team on top of a stronger balance sheet.

Online marketplace stocks still not cheap

Leading online marketplace stocks have fallen -26% from all-time highs of January leading one to wonder if they are ripe for the picking.

Analysts at Morgans look at four primarily online businesses and their answer is in the negative, believing that share prices post the correction aren't appealing enough.

The analysts consider REA Group ((REA)) shares have already having priced in the property market recovery expected in FY21. They thus believe the stock offers only modest upside from the current price.

For Seek ((SEK)), investors have priced in a steep recovery in job ads from early FY21, which the analysts consider overly optimistic. They recommend waiting for the price to fall below $15.

Market forecasts for Carsales ((CAR)) are based on a gradual recovery scenario and the stock appears to offer best value out of the lot while Domain Holdings ((DHG)), assuming a rapid V-shaped recovery in property markets, looks overvalued.

Overall, the analysts feel that while these stocks have retreated from January highs, share prices are still a tad too high.

Morgans urges investors should wait for another share market correction before taking the plunge.

RUDI'S VIEWS

Rudi's View: Investing For Income, The Smart Way

Dear time-poor investor: the impact from this year's tragedy for income investors is worse because of faulty strategies

In this week's Weekly Insights:

-Investing For Income: The Smart Way
-It's A Relief Rally

Investing For Income: The Smart Way

By Rudi Filapek-Vandyck, Editor FNArena

Bad news hits the weakest the hardest.

Australian investors already endured a rather disappointing latter half of 2019 when companies, including banks and resources companies, announced sizeable cuts to dividends.

It shows not all was well even before the covid-19 pandemic spread across the globe and forced countries into lockdown.

Now 2020 is shaping up as the worst year on record in Australia as far as corporate profits and shareholder dividends are concerned, in particular hitting those shareholders hard whose strategy is aimed at receiving sustainable income from the share market.

However, the truth, no matter how painful for those impacted, is that many of those investors blissfully ignored the very basic number one rule when making investment decisions:

(to quote Warren Buffett from a long time ago)

-Rule number one: never lose money
-Rule number two: never forget rule number one

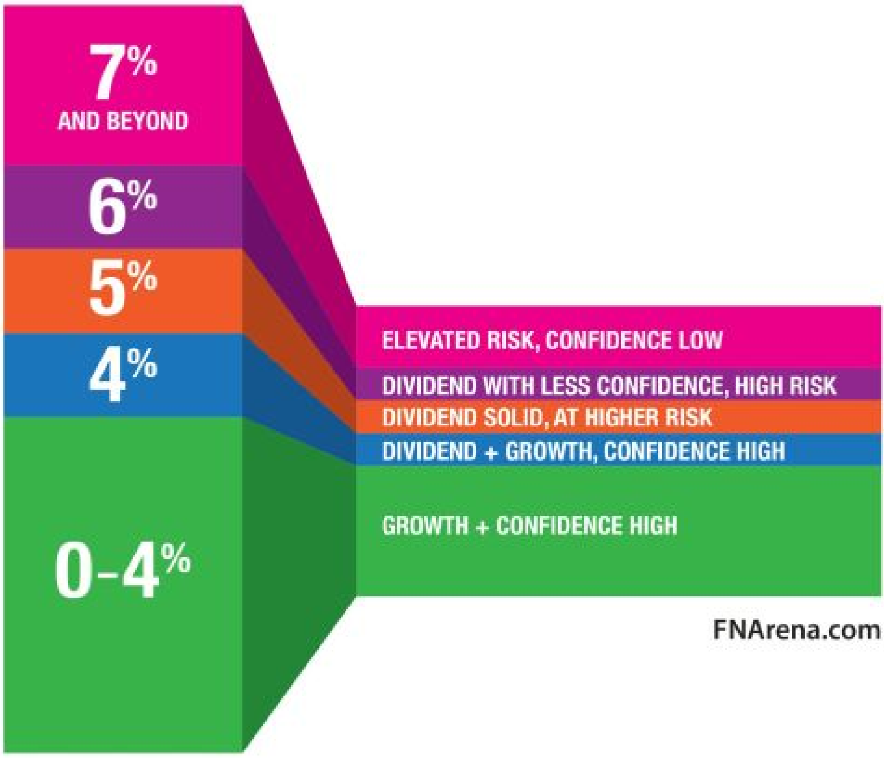
What the great legend from Omaha tried to tell us all through this seemingly facetious and simplistic two-rule mockery is that successful investing is about "*managing*" risk; not about "*taking*" risk or ignoring it.

And many an Australian investor, including, sadly, their financial advisors, have ignored the risk that comes with investing in high yielding stocks on the share market for far too long.

Many now facing serious budgeted income shortfall would not necessarily have realised, but buying 5% or 6% yielding equities (forward looking) in the share market pre-corona implies a serious step up on the overall risk ladder.

This is because government bonds, theoretically the ultimate low risk financial instrument available beyond cash under the mattress, are now yielding so little, financial markets have pulled back all yields across instruments and markets accordingly.

Years ago already, I tried to illustrate this process through the diagram below (first published in 2015).



The validity of this general assessment of risk as implied by stock market pricing of securities follows through the observation that most cuts in dividends last year and in 2020 are from the higher yielding cohort on the ASX.

Plus most dividend cuts announced tend to be much larger than for lower yielding equities.

Investors would be wise not to underestimate this process of absorbing the fall-out from the lockdowns and the subsequent economic recession still has a lot longer to run.

Dividends will still be absent and cut next year and in some cases maybe even in 2022.

Maybe this is as good as any time to pause and reflect on what went wrong, and set out on a better strategy for the future.

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A **faulty income strategy starts with the wrong focus**. Priority number one, for all kinds of investors, no matter experience, age or specific strategies, is to look after your capital.

Step number two is to adopt a total return strategy whereby everything is taken into account, including costs, fees and taxes.

Step number three is to incorporate potential income.

Too many investors, panicked by the change in the yield/income landscape post 2012, ignored the natural order for setting up a robust investment portfolio and moved straight to step number three. And many an advisor failed to inform or educate their clients otherwise.

Even prior to last year's dividend cuts, and this year's Bear Market for equities, the failings of strategies with a sole or extreme focus on income "right now" had already revealed themselves in spades.

Look no further than the fact three of the Major Four banks' share prices had lost about one third of their value since April 2015, prior to sinking near GFC lows in March this year.

Many a stock held for the sole attraction of the dividend has fared a lot worse, including the likes of AMP, G8 Education and, indeed, Telstra.

Even those investors hiding behind the fact they purchased their initial shares many moons ago at much lower prices still cannot deny that any strategy providing income while the capital base erodes away is not a good strategy.

Especially not when after the fall in capital comes the realisation there will not be a dividend at all this year, or a substantially reduced pay-out.

A much better strategy is one that incorporates the one key element that separates equities from bonds and other income providing investment products: growth.

Investors should consider there are two ways for creating income from owning shares: one is through dividends, the second is via selling at a higher level than the purchase price.

The best way to combine both key share market characteristics is through adopting a wholistic approach: by constructing a portfolio that combines growth with income and income with growth.

The end result should be a strategy that is much more protected against negative developments, including capital erosion, while offering growth of capital and income instead.

A truly superior outcome.

Sounds too good to be true? I've done the ground work over the past five years. I can report from first hand experience it's not a theoretical chimera. Get the basics right and you too can grow your capital while enjoying a steady income.

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Past research indicated the share market's sweet spot lays between 4%-4.5% in forward looking dividend yield (see also the diagram earlier).

But because of the significant drop in global bond yields, I believe the optimal point where risk, income, growth and return meet on the ASX is probably now around 3%.

Even with franking credits added on top, 3% won't be sufficient for most retirees and pensioners. So we have to be smart and add-in growth.

Growth adds two key features to our portfolio: share prices for companies that grow rise to a higher level plus today's dividend payouts will be higher in the future as well when supported by growth.

By combining income with growth, a portfolio that today yields 3% (for the portfolio as a whole) can yield 4%, then 5%, and more as time goes by.

In the meantime, the capital inside the portfolio grows to a higher level and investors can sell a portion each year to make up for the initial shortfall in income from dividends.

In case you are still not 100% convinced, I'll meet you half-way.

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A simple ETF (Exchange Traded Fund) that mimics the ASX200 Accumulation index would have done a better job than owning large overweight portfolio positions in banks and energy companies and retail REITs and the like over the years past.

The ASX200 combines CSL with CBA and other financials, BHP, Woodside, JB Hi-Fi, and others (200 stocks in total) for an average dividend yield of circa 4%.

Assuming most investors are aiming for 6% plus franking, they would have to sell circa 3% initially each year to generate the same income (there are some costs to take into account as well). Dividends received through an ETF equally apply for franking credits.

Starting in January 2015, such a basic index following strategy would have generated the following returns (ex-dividends)

-2015: -2.13%
-2016: +6.98%
-2017: +7.05%
-2018: -6.90%
-2019: +18.38%

The above returns are ex-costs, but ETFs are low cost and it is not inconceivable costs will only go down in the future. Also, because of the significant underperformance by yield stocks in recent years the average dividend yield for the ASX200 has actually been closer to 4.5%, which makes the past return from an index ETF even more attractive.

Even without the spectacular outcome in 2019, anybody can instantly see (I hope) a simple ETF would have provided a superior total return than your average ill-conceived, dividend-oriented strategy over the past five years.

Because of the heavy overweight positions for the banks, Telstra and other large cap dividend paying stocks in the index, we'd have to assume that a carefully constructed portfolio with less exposure to the share market's weak spots can generate an even better outcome.

The **FNArena/Vested Equities All-Weather Model Portfolio**, which has been managed and run in accordance with this smart income principle in mind, has done better than an index ETF over the period, including this year when losses incurred are significantly lower.

On Friday, the All-Weather Portfolio return for the running financial year (starting July 1, 2019) moved into positive territory. The ASX200 Accumulation index is still down -16.35%.

For the record, here are the returns from the All-Weather Portfolio for the past five years (including dividends, pre-fees):

-2015: +7.20%
-2016: +4.12%
-2017: +13.80%
-2018: +0.75%
-2019: +21.31%

Admittedly, constructing a low-risk basket of stocks during a time when dividends are being deferred, reduced or cancelled, and when company profits are expected to fall by most since the GFC is more of a challenge this year, but I'd still maintain the outcome from combining growth with dividends will be superior over the years to come.

Note: Part Two of this week's Weekly Insights, to be published on Friday, will focus on dividend stocks with sustainable payouts.

It's A Relief Rally

The liveliest discussion on social media over the weeks past has been whether the equity markets' upswing from the March lows will prove to be sustainable or not.

In what might yet prove to be a telling sign, the bearish warnings (with conviction) have virtually disappeared and the bulls are making fun out of everyone who still carries doubt and hasn't joined in as yet.

On my observation, equity markets are now shifting into the next phase whereby money flows into stocks that have been lagging thus far. This, I believe, will make markets increasingly vulnerable to negative news or developments.

It's not necessarily something that will break the uptrend, but it might, at some point, the longer it continues.

Within this context I note the market strategist at **Longview Economics**, up until recently rather bullish about global equities, is now cautioning that markets are setting themselves up for major disappointment.

Longview suggests the pandemic-induced supply-side shock to the global economy will soon be replaced with a demand-side shock as investors come to realise the V-shaped recovery that is being priced-in the longer this rally continues, will actually look a lot more like a U-shape.

For this rally to be the real deal that ends the Bear Market and starts a new Bull Market, Longview argues it has to be reflected in other market signals such as high yield bond spreads, 10-year benchmark government bonds, banks share prices, transportation stocks, the JPMorgan emerging market currency index, et cetera.

Right now, highlights the strategist, none of these additional market signals backs up the optimism that is conquering the minds and hearts of investors in equities.

Conclusion?

[The] "message is that this rally is a relief rally – and not the start of a new bull market."

(This story was written on Monday 11th May, 2020. It was published on the day in the form of an email to paying subscribers, and again on Thursday as a story on the website).

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

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

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RUDI'S VIEWS

Rudi's View: Reliable Dividends On The ASX

Dear time-poor investor: a line-up of reliable & sustainable dividend paying companies on the ASX

In this Rudi's View:

-Reliable Dividends On The ASX
-Rudi Talks

Reliable Dividends On The ASX

By Rudi Filapek-Vandyck, Editor FNArena

In Part One of this week's Weekly Insights I, hopefully, convinced you all that owning a basket of stocks that happen to offer a high yield, with or without franking, is not the smartest investment strategy.

Part Two zooms in on where to find reliable yield in a covid-19 impacted Australian share market.

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The share market absolutely loves companies that grow their dividends consistently over a long period of time.

There are two ways to achieve this. Either a business continues to grow its sales and cash profits, which then allows for dividends to rise while keeping the payout ratio steady.

In the absence of such a straightforward concept, company boards can also "manufacture" growth.

Investors do not always pay attention to the finer details, and thus companies who don't have the luxury of a booming business with growing revenues can still achieve growth through, for example, lifting the pay-out ratio or raising capital or taking on debt.

The banks and Telstra, two of the main Go-To destinations on the ASX for income-hungry investors, have exactly done that at various stages over the decade past.

It's not a sign of a healthy set-up, but desperate investors and desperate boards simply went along with it in the hope the band aid could cover up the underlying wound for much longer.

There is another way of creating growth and that is by slashing the dividend by a large percentage; say -50% or more.

After that, growing the dividend becomes a lot easier in the subsequent years. It doesn't necessarily mean the business has to rediscover its prior mojo, just a little bit of normalisation out of the deep quagmire should suffice.

I don't think Telstra has reached this point as yet, but the banks look like they are setting themselves up for just such a scenario.

It's a bit early given we are still in the embryonic stage of the 2020 recession and banks have only just started to defer and reduce their dividends, but maybe in twelve months from today, they might be in a position to announce higher dividends compared to this year.

In the right context and with the right market sentiment, that might just be all investors need to hear. And given dividends will likely have been cut dramatically this year, the banks' story about growing dividends can easily last 3-4 years without a booming context for the sector overall.

(Nobody cares by then that dividends had to be slashed first. The share market is forward looking, remember?)

In the short to medium term, of course, banks have nothing but negative news to share with their shareholders even though this is not a situation of their own making.

One thing once again stood out this week and that is CommBank ((CBA)) showing everyone why its shares trade, and will continue to trade, at a sizeable premium to the rest of the sector, through the release of a relatively resilient quarterly performance update.

I've said and written this many times over in the past I-don't-know-how-many-years, the lower yield with the premium share price does not mean CBA is "expensive" or that the other banks are more attractive.

On a risk-reward balanced view, it's the exact opposite. And investors once again have been presented with the evidence.

The observation to add here is the relative gap between CBA shares and the rest of the sector has blown out considerably, which might weigh on the CBA share price short-term and/or allow the other banks to close the gap (exact timing unknown).

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Talking about providing more evidence, packaging titan Amcor ((AMC)) equally caught investors' attention with its quarterly update this week.

Amcor has been a proud member since inception of my small selection of All-Weather Performers in Australia, and it goes without saying it pleases me enormously when management at the helm continues to defy short-sellers and naysayers.

As pointed out by sector analysts since the release, Amcor stands out in the 2020 context as a reliable, sustainable payer of dividends to shareholders, and the board doesn't need to slash this year's dividend first in order to secure growth.

The odds are very much in favour of Amcor not paying out less than last year, at a time when many others are cutting or not paying out anything at all.

On current FX values (the company is now US listed and its prime currency is the US dollar) as well as on current analysts' forecasts, shareholders can expect to receive 5.4% in dividends in 2021.

There is no franking, of course, but then investors whose focus is solely on franking credits are receiving a few extra (and harsh) lessons this year.

With such a prospective yield, one would have to assume Amcor is now one of the Dividend Champions on the ASX.

As can be quickly established via the Sentiment Indicator on the FNArena website, there are a few dozen companies on the ASX that at face value offer higher yield, but few would have Amcor's low risk profile attached to those forecasts.

Having established the above, I quickly ran through my lists on the All-Weather Performers section on the website, and I think it's only fair to point out that Amcor has become the highest yield stock in my little personal universe.

Other stocks on my lists that equally pay out a relatively high yield include (ex-Amcor) Orora ((ORA)), Iress ((IRE)), Brambles ((BXB)), Macquarie Group ((MQG)), Charter Hall ((CHC)), and Coles ((COL)).

For full disclosure: the FNArena/Vested Equities All-Weather Model Portfolio owns shares in Viva Energy REIT ((VVR)), specifically for its reliability and relatively low risk profile, which thus far has been borne out by the REITs consistent payout and overall performance.

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One stand-out reliable dividend payer in the domestic infrastructure space is pipeline owner APA Group ((APA)).

APA listed in 2000 and paid its early shareholders 11c plus a little bit of franking in FY01. That dividend has grown by more than 300% to 47c in FY19.

Current market forecasts expect APA Group to pay out 50c for the running FY20 (of which the interim has already been paid out) and 52c next financial year.

As such, APA with ambitions both in renewable energy and in the US market, combines reliability and growth.

Only twice over the past twenty years did the dividend fall in comparison with the year prior; in FY04 and in FY08.

To my knowledge, none of its peers in Australia is able to match this achievement (see also AusNet Services further below).

If market forecasts prove correct, the securities are currently yielding in excess of 4.5%.

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According to quantitative analysts at Morgan Stanley, there is a sweet spot in the yield/dividend paying space on the ASX. It's where yield and growth meet and combine with company quality.

Sounds complicated? Nah. Just a lot of filters to determine where is the optimal risk-reward for yield seeking investors.

According to the team, the current sweet spot comprises of Fortescue Metals ((FMG)), Coca-Cola Amatil ((CCL)), BHP Group ((BHP)), Cochlear ((COH)), Rio Tinto ((RIO)), Ansell ((ANN)), JB Hi-Fi ((JBH)), Sonic Healthcare ((SHL)), Wesfarmers ((WES)), Woolworths ((WOW)), AGL Energy ((AGL)), and Coles.

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Strategists at stockbroker Morgans recently lined up their Best Ideas for investors seeking for income through the share market.

This led to a selection of 15 stocks: JB Hi-Fi, Coles, Woolworths, Amcor, Orora, Aurizon Holdings ((AZJ)), BHP Group, Rio Tinto, APN Convenience Retail REIT ((AQR)), Viva Energy REIT, Centuria Industrial REIT ((CIP)), APA Group, AusNet Services ((AST)), Spark Infrastructure ((SKI)), and AGL Energy ((AGL)).

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Equity strategists at JP Morgan equally published their Top Ten in Dividend Picks on the ASX.

The ten stocks selected are: Fortescue Metals, Vicinity Centres ((VCX)), BHP Group, GPT Group ((GPT)), Origin Energy ((ORG)), National Australia Bank ((NAB)), Macquarie Group, Amcor, Telstra, and Iress.

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In mid-April already, analysts at UBS highlighted which dividends they thought looked safe and which ones were most likely due for a reduction this year.

Even though almost a full month has passed since, I am still adding their conclusions as it further underlines the quality of the research.

UBS's most preferred Go-To dividend stocks are: Aurizon Holdings, AusNet Services, Metcash ((MTS)), Coles, APA Group and Woolworths.

Other stocks that offer reliable dividend streams include AGL Energy, Amcor, Brambles ((BXB)), BWP Trust ((BWP)), Clover Corp ((CLV)), CSL ((CSL)), Inghams Group ((ING)), Kogan ((KGN)), Magellan Financial ((MFG)), ResMed ((RMD)), Rural Funds Group ((RFF)), Seven Group Holdings ((SVW)), Telstra, and Wesfarmers.

Companies most likely to reduce, defer or cancel their dividends this year, on UBS's assessment, include SkyCity Entertainment ((SKC)), Sydney Airport ((SYD)), JB Hi-Fi, Scentre Group ((SCG)), Challenger ((CGF)) and Vicinity Centres.

In addition, the analysts believed dividends from the following list of companies looked at risk on a twelve months' view: Alumina Ltd ((AWC)), ANZ Bank ((ANZ)), National Australia Bank, Northern Star ((NST)), OZ Minerals ((OZL)), QBE Insurance ((QBE)), Servcorp ((SRV)), Stockland ((SGP)), Western Areas ((WSA)), and Westpac.

Lastly, the analysts also identified companies whose franking balances were nearly depleted, and thus dividends might still be paid, but the percentage in franking credits attached seems due for a haircut.

Shareholders should thus expect lower franking benefits from dividends paid out by Domain Holdings ((DHG)), Genworth Mortgage Insurance Australia ((GMA)), Nine Entertainment ((NEC)), IVE Group ((IGL)), Link Administration ((LNK)), Lovisa Holdings ((LOV)), Monadelphous ((MND)), Perpetual ((PPT)), and Village Roadshow ((VRL)).

Since the UBS update, banks have reduced or deferred their dividend, while National Australia Bank and QBE Insurance raised additional capital.

One infrastructure operator that is regularly mentioned as a trustworthy, reliable dividend payer, AusNet Services, recently surprised through management preparing investors for a dividend reduction in FY21, and possibly a capital raising on top.

Part Three in this Special on dividends will appear in next week's Weekly Insights.

Rudi Talks

Audio interview about the smarter way to build an income generating portfolio of equities:

bit.ly/2Z0Lq1z

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

P.S. I - All paying members at FNArena are being reminded they can set an email alert for my Rudi's View stories. Go to My Alerts (top bar of the website) and tick the box in front of 'Rudi's View'. You will receive an email alert every time a new Rudi's View story has been published on the website.

P.S. II - *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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