Week
14

Stories To Read From FNArena
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Contents

Brokers Back Star Entertainment Expansion

Star Entertainment will accelerate growth projects, leveraging the Asian customer base of strategic partners Far East Consortium and Chow Tai Fook.

-Placement provides certainty to the funding structure, minimising non-gaming capex -Extra investment will support expansion of the company's properties in Queensland and NSW -Dividend policy upgraded to range of 70-90% of normalised profit

By Eva Brocklehurst

Star Entertainment ((SGR)) has cemented its alignment with Far East Consortium and Chow Tai Fook through a 10% placement, raising $490m. The company will be able to accelerate growth projects and leverage the expertise and Asian customer base drawn from the partnership.

Debt will be reduced and capital for new projects won't be redeployed for some time. The company has upgraded its dividend policy, targeting a pay-out range of 70-90% of normalised profit, up from 50% of statutory profit.

The new dividend policy is considered a significant positive. Brokers agree the company is well placed to deliver on a plan to improve its domestic offering by reinvesting in customers and driving tourism.

The partnership makes strategic sense to Morgan Stanley. It may be dilutive in the near term but investors are advised to look through this one-time impact, given the long-term value accretion on offer and improved balance sheet. The dividend yield is now also attractive.

Marketing Alliance

Ord Minnett expects the alliance to drive hotel occupancy and visits to the company's gaming venues. Meanwhile, the new players now have an interest in promoting Star Entertainment through their extensive Asian tourism and leisure networks.

Citi is also favourably disposed towards this initiative, which is expected to better align all parties' interests. Star Entertainment will have access to a six million customer database and expand its scope beyond just the Queens Wharf re-development.

Chow Tai Fook and Far East will acquire 45.8m shares at $5.35 each. Each party will hold a 4.99% position in Star Entertainment. The partners are also applying to the regulator for approval to increase aggregate ownership to reach a maximum of 19.9% and, if approved, this is expected to provide support for the share price.

The partners have agreed to build up to an additional five towers on the Gold Coast and one in Sydney, as well as develop the Metro West project in Sydney and further projects on the Gold Coast.

UBS believes the announcement provides certainty to the company's funding structure, which will be able to maximise returns by minimising non-gaming capital expenditure and still generate increased visits to the properties through additional hotel developments.

While the equity raising is dilutive in the near term, the broker suggests benefits from the marketing alliance and the upside from new projects should drive a value accretive outcome over the medium term.

Morgans pares back valuation but retains an Add rating, expecting the company to deliver solid earnings growth and an attractive income stream for investors. Risks to valuation include the global economic environment, a reduction in consumer spending and regulatory changes.

Capital expenditure and gearing are expected to be on the low side and proceeds from residential sales are likely to offset equity contributions, so Citi currently assumes just $30m net capital expenditure across FY18-22 for existing developments.

The balance sheet was already in reasonable shape but the extra investment provides head room for further investments in Queensland and NSW, CLSA observes. The broker, not one of the eight stockbrokers monitored daily on the FNArena database, has an Outperform rating and $6.13 target.

Trading Update

The company also provided a trading update which signalled revenue for the March quarter was up 18.8%. This is an acceleration on the first half growth of 15.9% , which Citi attributes to ongoing momentum in VIP and initial contributions from The Darling on the Gold Coast. The broker assumes growth will moderate over the second half to around 15% given tougher domestic comparable period.

Morgan Stanley lifts net profit estimates by 1-6% across FY18-20 on lower net interest costs, although lowers earnings per share estimates by -1-5% because of higher weighted average share count. Given the company's attractive growth outlook and dividend yield the broker considers the discount in the stock is unwarranted.

FNArena's database shows seven Buy ratings and one Hold (Credit Suisse, yet to comment on the update) the consensus target is $6.18, suggesting 18.0% upside to the last share price targets range from $5.90 (Credit Suisse) to $6.60 (Citi).

Fourth Bid Lucky For Santos?

While the latest offer for Santos pays for some medium-term growth, brokers are unsure whether the bid will pass official scrutiny.

-Investor investment horizons likely to dictate whether the bid is fair or too low relative to potential upside -FIRB approval may be difficult to obtain because of the national significance of GLNG and Cooper Basin -How can commitments on capital expenditure be assured if the oil price declines again?

By Eva Brocklehurst

A considerably higher bid has emerged for Santos ((STO)), after several in recent weeks, as Harbour Energy returns with an offer that the Santos board finds encouraging, allowing due diligence to proceed.

Santos disclosed that, during late March, Harbour Energy made offers of $6.25/share and $6.37/share before finally launching a $6.50/share indicative bid. This is considerably higher than the offer Harbour Energy made back in August 2017 at $4.55/share.

The $6.50 bid is a 28% premium to the stock's last close and a 30% premium to the one-month volume-weighted average price (VWAP). The US dollar-denominated consideration is US$4.98 a share, comprising a cash component of US$4.70/share and a special fully franked dividend of US$0.28/share.

Harbour Energy's plan to invest heavily in Santos is likely to result in a materially higher valuation than Morgans currently estimates. The broker calculates Harbour Energy is offering 17x 2017 free cash flow and 20x 2P reserves, a steep premium to valuation, but maintains a Reduce rating with an unchanged valuation-derived target of $4.31.

Morgans has always struggled with its valuation of Santos, given the company's opposing priorities of de-leveraging its balance sheet and increasing investment in its diversified operations.

UBS envisages risks around due diligence and remains cautious about the prospect of a firm bid emerging. Due diligence items are likely to revolve around abandonment liabilities as well as the company's participation in the Darwin LNG backfill and PNG LNG expansion. The main variables to the broker's valuation are the oil price and discount rate.

To justify $6.50/share UBS would need to de-risk all growth projects and assume an oil price of US$75/bbl. The broker acknowledges the risk of underperformance in the near term has been lowered by the increased probability of a formal takeover offer and the recent rally in oil prices.

Citi suspects Santos is unlikely to start talking about growth in order to get a higher bid, as the offer is now at a point where the company is willing to engage. Therefore, if the bid fails, the market is unlikely to pay more for growth than previously indicated. Citi believes investor investment horizons will dictate whether they consider the bid to be a fair price, or too low relative to the potential upside.

Gas Demand

The offer only makes economic sense to the buyer if the value of gas reserves and resources in production or in the ground are re-priced substantially higher, Shaw and Partners asserts. The broker suggests the street view of the stock's value is well below the proposed offer, which captures an option on higher gas prices, or higher gas production from projects that are not yet sanctioned.

The broker notes industry activity supports the rising value in Australian gas, noting Woodside ((WPL)) has bought more gas and smaller domestic companies are increasing activities to find, appraise or develop gas. AEM reports also document a drop in supply from fields offshore in Victoria.

Meanwhile, the broker points to unsatisfied demand for gas in China that is driving Chinese companies on a global spending spree. Hence, the solution to Australia's gas supply gap is the development of new fields and investment in new infrastructure, although all remaining resources the broker identifies are owned by small companies which lack the capability to meet the shortfall.

Credit Suisse firmly believes that Harbour Energy intends to push more gas through the latent capacity at GLNG. Yet, the broker is overwhelmed by the US$7.75bn debt package Harbour Energy has announced, particularly when coupled with US$2.5bn of Santos corporate debt, which it assumes is retained.

Credit Suisse is also interested in how much the company's tax revenue would reduce, given the interest costs on this pile of debt, and asks how can commitments on capital expenditure be assured if the oil price declines again.

FIRB Hurdle

The conditions on the offer remain the largest hurdle. Foreign Investment Review Board (FIRB) approval may be difficult to obtain given the national significance of GLNG and the Cooper Basin. As Santos is no longer a material east coast gas supplier, UBS expects the FIRB to look at Harbour Energy's plans for the Cooper Basin and WA gas.

Morgans suggests the FIRB could be enticed by the commitment by Harbour Energy to invest heavily in the assets, that could take some pressure of the east coast gas supply balance and partly lower GLNG's reliance on third-party gas. However in a global climate where energy security ranks amongst the highest concerns, the broker suspects this is where the official focus will be.

If Harbour is successful, it would remove the only Australian participant in the GLNG joint venture, while also handing over the controlling interest in the Cooper Basin gas venture to a US fund. This is a critical hurdle to overcome, brokers suggest, for the offer to proceed to a formal bid.

Offer Conditions

The offer is conditional on a minimum 15% of existing Santos shares rolling over into unlisted shares in a special-purpose company that will remain invested in Santos. Morgans is uncertain regarding just how Harbour Energy can achieve a minimum 15% of existing stock staying invested in an unlisted entity.

Conditions also includes binding debt financing commitments, completion of confirmatory due diligence and regulatory approvals, as well as a unanimous recommendation of the bid from the Santos board.

FNArena's database has one Buy rating (Credit Suisse), three Hold and one Sell (Morgans). The consensus target is $5.45, signalling -7.2% downside to the last share price. Targets range from $4.31 (Morgans) to $6.35 (Credit Suisse).

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FNArena Scoop: Metcash, Amazon In Talks

Amazon and Metcash are negotiating a distribution deal to support deliveries of goods to households across Australia

-Contract talks between Amazon Australia and Metcash are advancing -Metcash distribution can substantially strengthen Amazon's delivery capabilities -Metcash also under threat of losing independents as customer

By Rudi Filapek-Vandyck, Editor FNArena

Online commerce giant Amazon and locally based Metcash ((MTS)) are in negotiation to use the latter's distribution network to support Amazon Australia's goods delivery service throughout the country.

According to information received by FNArena, talks between the two companies are advancing while share market speculation suggests Amazon could be interested in acquiring local distribution through either Caltex Australia ((CTX)) or yet to be spun off Coles supermarkets from WA conglomerate Wesfarmers ((WES)).

Metcash, whose logistics and distribution network delivers goods to some 1600 independently owned stores across Australia, is reportedly facing the threat of some independents, such as Drakes Supermarkets in Queensland, potentially switching to digital start-up Irexchange, which offers direct access to suppliers, and has reportedly signed up 350 independents to date.

Amazon Australia launched in early December last year. The company has copped some criticism as its local presence thus far failed to live up to the pre-launch hype, and with its founder and CEO, Jeff Bezos, under personal attack from the US President.

Metcash is probably best known as the support network behind supermarkets operating under IGA and Foodland IGA brands, while its Convenience division provides service to some 150,000 convenience stores, restaurants, small coffee bars and fresh food outlets. The company's corporate website presents Metcash as "Marketing and wholesale distribution business specialising in grocery, liquor, hardware and other fast moving consumer goods."

Metcash also is Australia's second-largest broad range liquor wholesaler, supplying over 2,500 stores including Cellarbrations, The Bottle-O, and IGA Liquor.

Apart from general share market weakness following on from a retreat in US equities since late January, Metcash's share price has come under pressure after the company announced last month its CEO of Supermarkets and Convenience operations, Steven Cain, had accepted a job in home base Melbourne. As it turned out, Cain is returning as the new CEO of major competitor Coles, which he left 14 years ago.

Increased delivery capabilities will substantially strengthen Amazon Australia's intention to build up significant market share in local household spending.

A-REITs Looking More Attractive

Several brokers believe the A-REIT sector is starting to look more attractive as bond yields head lower.

-Spread to bond yields justifies direct real estate carrying values -Attractive investment opportunities although macro headwinds may prevail short-term -Australian specialty retailer margins remain above global peers

By Eva Brocklehurst

Australia's yield curve is flattening and this may be bullish for the relative performance of Australian real estate trusts (A-REIT). Australia's 10-year bond yield has contracted by over -30 basis points since it touched 2.6% on February 5.

Shaw and Partners is not sure why bond yields are heading lower but suggests A-REITs are starting to look attractive. The broker concedes the sector is not immune to the geopolitical headwinds such as trade wars, and whether bond markets stabilise remains to be seen.

What is worth highlighting, in the broker's opinion, is that many of the larger capitalised A-REITs are actually trading at a discount to net tangible assets (NTA). This includes Charter Hall Retail ((CQR)), GPT ((GPT)), Investa Office ((IOF)), Mirvac ((MGR)), Stockland ((SGP)), Scentre Group ((SCG)) and Vicinity Centres ((VCX)).

The sector's weighted average capitalisation rate is around 5.57%, representing a spread over bonds of 2.97%, and this indicates to the broker a sufficient enough buffer to justify direct real estate carrying values.

More importantly, Citi notes the 10-year bond yield is contracting faster than the 3-year yield, creating what it terms as a bull flattening yield environment. Such an environment has recently been positive for A-REITs.

Citi prefers Goodman Group ((GMG)), Charter Hall ((CHC)) and Lend Lease ((LLC)). Goodman is delivering sector-leading growth in earnings per share of 8.2% and the broker believes 6%-plus growth is sustainable in the medium term.

Meanwhile, a good way to get exposure to the office segment is considered to be via Charter Hall, as 43% of the company's assets under management are in office, a segment where Citi observes rental growth is improving.

Moreover, given the company receives fees based on asset values, the broker argues the earnings benefit is more immediate from a recovery in office versus rent-collecting A-REITs.

Citi does not believe Lend Lease will increase its provision of $160-190m taken in the engineering division for underperforming projects. The broker observes the company has progressed more than 50% through these projects and has enough information to make a reasonable assessment of potential future costs.

Buybacks

Shaw and Partners notes buybacks continue at Charter Hall Retail, Dexus ((DXS)), Lend Lease and Mirvac. The broker still believes Vicinity Centres should be buying back its own stock, as it share price is down -8% since the first half results and now trading at a -18% discount to NTA.

The broker's forecast 12-month total shareholder return for the sector is now 15.4%, including a yield of 5.4% based on a weighted average pay-out ratio of 82%. At a stock level, Shaw and Partners envisages attractive investment opportunities although acknowledges the macro headwinds may prevail in the short term.

The broker retains Buy ratings for Vicinity Centres, Stockland, Scentre Group, Centuria Metropolitan ((CMA)), Centuria Capital ((CNI)), Mirvac and Lend Lease.

On a sector relative basis, despite having no Sell ratings, Shaw and Partners believes National Storage ((NSR)), Goodman Group and BWP Trust ((BWP)) are screening expensive.

Retail Rents

CLSA has looked at the impact of declining retail margins on rents for shopping centre owners. Australian specialty retailer margins remain healthy, and above global peers, although at the EBITDA level margins are declining, consistent with tougher trading conditions and rising expenses.

The broker estimates that if gross margins fall -10% and retailers desire to recover earnings, rents need to fall -10%. Assuming a decline of -10% in re-leasing spreads for five years DCF valuations are lowered by -2% on average.

CLSA acknowledges this analysis does not take into account the quality of the portfolio but believes the discounting of A-REITs appears overdone. Preferred retail A-REITs remain Scentre Group and Mirvac.

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US-China Trade Concerns Muddy Oil Outlook

Oil prices may have slipped recently but analysts expect prices will be underpinned over the rest of 2018.

-Uncertainty surrounding US-China trade policies likely cause of recent oil sell-off -However, positive momentum continues and market expected to remain reasonably balanced -US infrastructure constraints, risk of a return to Iran sanctions and Venezuelan cuts supportive

By Eva Brocklehurst

The trigger for a sell-off in oil prices earlier this week appears to be uncertainty surrounding the impact of US policies on markets, amid concerns about growth in global trade.

China instigated a harsh response to US tariffs on steel and aluminium - some tariffs are as high as 25% on US products - which, in turn, resulted in large US companies criticising President Trump's approach and raising fears the long period of sustained growth could be coming to an end.

Citi notes, even though the US-China oil trade balance is improving rapidly, other factors are widening the broader trade deficit. Disruptions to US-China crude, refined product or LNG trade as a form of Chinese retaliation may hurt the US President's attempt to close the US trade deficit.

The impact on the overall US trade deficit is not that clear, as oil and LNG cargoes would likely find a place elsewhere. In 2017 US oil net exports to China averaged around 435,000 b/d, a 140% increase year-on-year from 2016.

Citi suggests the Trump administration will need to push back forcefully on any Chinese move to impose tariffs on energy trade if they want to reduce the deficit. If left unrestricted, US net oil flows to China are likely to increase sharply, as US crude is pricing competitively in Asia and the US does not have spare refining capacity to absorb domestic supply increases.

Despite the recent uncertainty, a decline in oil stockpiles in the US and other advanced economies has been the primary driver of stronger oil prices over the last 8-12 months. Not only are US stockpiles below the five-year average of 2013-2018 for this time of year but even OECD stockpiles are close to the five-year average.

Commonwealth Bank analysts now expect any surplus building in oil markets will be muted this year, while deficit risks are emerging, particularly with a large decline Venezuelan production and the US facing infrastructure constraints.

Previously the analysts believed the end of the OPEC agreement would mean supply came back on line quickly to flood the physical market, weighing on prices. However, the balance of risks suggests OPEC can maintain discipline and now the market is expected to be kept in balance.

Earlier this year Deutsche Bank was concerned US exports would shrink and lead to a weakening of the regional supply-demand picture. Instead, there is been some stability in US exports and a slight widening of the spot spread.

Longer term, Deutsche Bank expects supply to grow faster than US domestic demand and force exports to rise. The broker still envisages positive momentum in the market and finds no reason not to be generally constructive.

Iran

A heightened risk of sanctions being re-applied to Iran is also likely to keep oil prices well bid. The only concern Deutsche Bank has, between now and the end of the year, is for some of the geopolitical risk premium to disappear if a supplemental deal is agreed that addresses President Trump's concerns.

The broker notes recent US government staff appointments could spell trouble for the Iran nuclear containment deal. Withdrawal by the US now appears more likely, given incoming US Secretary of State Mike Pompeo and national security adviser John Bolton have both expressed hawkish views regarding sanctions relief.

Venezuela

Commonwealth Bank analysts suggest over-compliance with production cuts by OPEC members, particularly Venezuela, have helped the oil price rally. While US oil supplies are expected to rise sharply, infrastructure constraints there may pose a problem by August. Prices could break through recent highs, which would mark the highest prices since late 2014.

This outlook is predominantly being driven by the OPEC-led deal to sideline around 1.8% of global supply. Key is Venezuela's collapsing oil production, regarded as the largest unplanned outage in history, that reflects an ongoing economic and debt crisis, US sanctions and lack of funds for investment or maintenance.

Commonwealth Bank analysts are now more positive about the outlook for oil prices and expect Brent crude to average US$65/bbl in 2018 and US$61/bbl in 2019.

Material Matters: Iron Ore, Steel And Gold

A glance through the latest expert views and predictions about commodities. Iron ore; steel; coal; gold; mining strategy; and Myanmar Metals.

-Price curve continues to favour high-grade iron ore producers -Steel prices likely to improve but not re-gain 2017 heights -Gold prices likely to move in line with US dollar until mid 2019 -Firm commodity prices underpin UBS' overweight strategy on miners

By Eva Brocklehurst

Iron Ore

Citi believes quality dominates among iron ore producers. Using a basic iron ore cost curve is not a particularly accurate way to compare producers and the broker takes into account a large number of of factors such as ratios of fine/lump, grades, costs, maintenance, and transport to make more meaningful comparisons.

The outcome indicates that the break-even price curve continues to favour high-grade producers. The curve has shifted lower, mainly based on the quality of premiums being received, but also falling freight rates which have offset inflation pressures. Vale is the biggest beneficiary of the broker's analysis.

Citi retains a Buy rating for Rio Tinto ((RIO)) amid continued upside risk to estimates from spot commodity prices, particularly iron ore. China's environmental curbs have also resulted in the premium for a higher grade ores remaining elevated. While premiums are record levels, Citi believes demand for higher grade ore will moderate and low-grade supply balance will improve with capacity additions.

Deutsche Bank's visit to China has confirmed that some mills are switching to lower-grade 58% iron ore. Modelling for Chinese mills shows an extra RMB100/t in gross profit margins can be obtained by using more 58% iron ore in feed and a further drop in the rebar price, currently RMB3400/t, would accelerate the switch, in the broker's opinion.

This would be incrementally positive for Fortescue Metals ((FMG)). However, Deutsche Bank points out that steel output is boosted by around 5% when using higher-grade iron ore and environmental concerns also influence decision making.

Steel

Credit Suisse notes downstream demand for steel has finally kicked off in China, as evidenced by trader stocks falling for two weeks. The drawdown started a full month later than in 2017 and the delay caused an erosion in the steel price.

Macro factors suggest steel demand should remain solid in 2018 and the broker cites a senior NDRC economist who has indicated China's infrastructure expenditure will be up 15% and housing supply should remain robust. Nevertheless, steel prices are starting from a lower base this time, which may prevent them regaining last year's heights.

The broker also notes support for a weaker 2018 outlook comes from the possibility that Chinese steel exports may be blocked by other countries following the lead of the US. If this leads to a Chinese steel glut then steel and iron ore prices may soften.

Coal

Coal trains have commenced re-loading at key coking coal ports in Queensland as Tropical Cyclone Iris subsides. Hay Point has started unloading trains and Dalrymple Bay and Abbot Point are expected to begin unloading shortly. The ports were closed Tuesday, despite the cyclone never making landfall. Commonwealth Bank analysts expect the impact on coking coal markets to be minimal.

Gold

The prospect of a potential trade war between China and the US has helped safe-haven demand for gold, as has the weaker US dollar. US 10-year real yields usually have a strong inverse relationship with gold prices but

Commonwealth Bank analysts note this once reliable relationship has broken down recently. The last time the correlation diverged was in 2012.

The analysts observe, surprisingly, the US dollar has emerged as a more reliable correlation with gold prices over the last six months. The analysts suspect gold prices will move in line with the US dollar until mid 2019. After that, US 10-year real yields are expected to become the primary driver of gold prices once again.

Commonwealth Bank analysts upgrade gold price forecasts amid expectations for a weaker US dollar. The gold price is now expected to steadily lift to US$1380/oz by mid 2019.

Mining Strategy

Miners have been able to repair balance sheets, thanks to strong commodity prices in the March quarter, UBS observes. The quarter produced a good return to shareholders in the form of dividends and buybacks as a result.

While cost pressures are forecast to increase for raw materials and labour the broker suspects a firm commodity pricing environment will offset the impact. Most projects being approved, or developed, focused on supply replacement rather than growth.

UBS remains confident in investing in lithium/graphite producers, despite the teething problems. The broker is also watching the geopolitical scene, given a number of announcements made regarding longer-term power and tax issues, such as at Oyu Tolgoi in Mongolia, Rio Tinto's likely equity reduction at Grasberg (imposed by Indonesia), and any impact from US-China trade tensions.

The broker's overweight call on miners is predicated on no trade war occurring. Preferred exposures include BHP Billiton ((BHP)) and Iluka Resources ((ILU)).

Myanmar Metals

Myanmar Metals ((MYL)) has an option to acquire a majority stake in the Bawdwin mine in Myanmar, which Argonaut regards as the best under-explored poly-metallic asset globally. Large-scale mining at the site ceased during World War II leaving intact a high-grade core resource of silver, lead, zinc and copper.

By exercising its option in May, Myanmar Metals would gain a 51% majority stake and operate the mining concession. Argonaut has a Speculative Buy rating and $0.25 target on the stock.

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Weekly Ratings, Targets, Forecast Changes

By Rudi Filapek-Vandyck, Editor FNArena

Guide:

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

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

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

Summary

Period: Monday March 26 to Friday March 30, 2018 Total Upgrades: 7 Total Downgrades: 4 Net Ratings Breakdown: Buy 44.33%; Hold 40.01%; Sell 15.66%

The upgrade cycle for metals and mining stocks remains very much alive and last week four of the six stocks upgraded by stockbroking analysts were resources companies, with Whitehaven Coal the recipient of two upgrades; both to Buy.

But it's no longer a straightforward affair as illustrated by the fact that stockbrokers also issued four downgrades, all to Sell, during the week and three of these downgrades affected recommendations for mining stocks. It's a similar mixed picture for revisions to price targets/individual stock valuations and earnings forecasts.

Six out of the seven upgrades in recommendations moved to Buy. Baby Bunting is the sole non-resources stock featuring amongst stocks being downgraded, illustrating ongoing tough times for discretionary retailers in Australia.

Agri-company Nufarm and Whitehaven Coal top the week's table for upward adjustments to price targets, both enjoying a boost in excess of 3%, but the numbers on the flipside are much heavier with gold miner Perseus Mining enduring a blow of -10%, followed by Fortescue Metals (-5%), and Baby Bunting (-4%).

Fueled by ongoing upgrades for the resources sector, changes to earnings forecasts for the week ending the Thursday before the Easter weekend are eye-catching on both sides of the ledger. On the positive side, Galaxy Resources and Syrah Resources lead the pack with gains of 177% and 161% respectively, followed by Janus Henderson, Brickworks and Alacer Gold.

Suffering heavy negative revisons are Myer (-33%), Perseus Mining (-23%), Sigma Healthcare (-9.5%), Fortescue Metals (-9.4%), Nufarm (-9.3%), and many more others.

In the meantime, macro themes continue to impact on investor sentiment, and are likely to continue to dominate the short term outlook.

Upgrade

APOLLO TOURISM & LEISURE LTD ((ATL)) Upgrade to Add from Hold by Morgans .B/H/S: 1/1/0

The company has acquired Camperco, a motor home rental company operating in Ireland and the UK, for $8.2m. This marks the company's first move into the UK/Ireland rental market and provides options to grow in a substantial market as well as in Europe.

Morgans expects the acquisition to be 5% accretive in FY19/20. Following recent share price weakness the broker upgrades to Add from Hold. Target is raised to $1.98 from $1.93.

CSR LIMITED ((CSR)) Upgrade to Equal-weight from Underweight by Morgan Stanley .B/H/S: 1/4/0

Housing construction is more robust than previously anticipated, which coincides with favourable aluminium pricing. Morgan Stanley upgrades earnings estimates on this basis.

The broker considers the valuation fair and would look for evidence the company is trading at a meaningful discount to its historical multiple, or showing value through the cycle, before adopting a more positive stance.

Rating is upgraded to Equal-weight from Underweight. Target is raised to $5.00 from $4.25. Industry view: Cautious.

IOOF HOLDINGS LIMITED ((IFL)) Upgrade to Buy from Neutral by UBS .B/H/S: 5/0/0

UBS notes the shares have fallen -11% since the October announcement of the acquisition of ANZ Wealth and suggests this reflects concerns regarding earnings attrition from the acquisition.

Nevertheless, the broker expects earnings prospects are better going forward, supported by re-pricing opportunities.

Rating is upgraded to Buy from Neutral, as the broker considers the stock trading at an unwarranted -12% discount to the market by FY21, with an average dividend yield of 6.4% over the interim. Target is raised to $11.50 from $10.75.

OROCOBRE LIMITED ((ORE)) Upgrade to Outperform from Neutral by Macquarie .B/H/S: 6/0/1

After the significant fall in the share price Macquarie upgrades Orocobre to Outperform from Neutral. Target is reduced to $6.80 from $7.15.

SOUTH32 LIMITED ((S32)) Upgrade to Outperform from Underperform by Macquarie .B/H/S: 1/3/3

Macquarie upgrades the price target to $3.70 from $3.10, largely because of significant increases to its long-term manganese ore and thermal coal price forecasts but also from higher long-term aluminium and alumina prices.

The most significant changes are upgrades to manganese ore prices, which have benefited from Chinese environmental reforms.

These price upgrades have transformed the company's longer-term earnings outlook and the broker upgrades to Outperform from Underperform.

WHITEHAVEN COAL LIMITED ((WHC)) Upgrade to Outperform from Neutral by Macquarie and Upgrade to Overweight from Equal-weight by Morgan Stanley .B/H/S: 5/2/1

Macquarie has improved its long-term outlook for the coal price which drives an increase in the target by 10% to $4.60. The changes to coal price forecasts, combined with adjustments to the coal sales mix, have tempered earnings downgrades in the near term.

With the stock now offering a 16% total shareholder return the broker upgrades to Outperform from Neutral.

The company is benefiting from higher coal prices and Morgan Stanley finds value in the equity, despite the rally on repairs to the balance sheet having run its course.

The broker upgrades to Overweight from Equal-weight and raises the target to $5.70 from $5.05. Morgan Stanley believes the company's cash flow and future growth potential underpin compelling value.

The stock also looks cheap versus global thermal coal peers. Industry view: Attractive.

Downgrade

BABY BUNTING GROUP LIMITED ((BBN)) Downgrade to Sell from Neutral by Citi .B/H/S: 2/1/1

One would be inclined to think the pending closure and retreat from Australian soil by competitor Babies R Us (see also Toys R Us) would be a positive development longer term, but Citi analysts point out in the short term this could translate into competitive product being dumped upon Australian consumers at give-away prices.

On that basis, Citi has now decided to downgrade to Sell from Neutral. Target drops to $1.20 from $1.50. On Citi's analysis, there is significant overlap between Baby Bunting stores and stores operated by the failing competitor. Forecasts have been lowered.

FORTESCUE METALS GROUP LTD ((FMG)) Downgrade to Sell from Buy by Citi .B/H/S: 4/2/1

The realisation that price discounts for lower grade iron ore have become more structural than cyclical, balanced 2/3 plus 1/3 by Citi analysts, has led to reduced forecasts, a lower valuation and subsequently a downgrade to Sell from Buy.

The new price target of $4.10 compares with $5.40 previously. There are offsets through early repayment of debt, but in the end the now structural price discount prevails.

NORTHERN STAR RESOURCES LTD ((NST)) Downgrade to Sell from Neutral by UBS .B/H/S: 0/3/4

UBS notes the share price has lifted around 15% since the end of 2017. While continuing to believe the stock is a quality gold name with exploration success, the market is seen paying for this going forward.

Hence, UBS downgrades to Sell from Neutral. As Newcrest ((NCM)) has suffered from another setback at Cadia the broker envisages a rotation into Northern Star, although later in the year flows could return to Newcrest. Target is raised to $6.06 from $5.68.

SANDFIRE RESOURCES NL ((SFR)) Downgrade to Sell from Neutral by UBS .B/H/S: 1/3/3

UBS considers the stock fully valued as the share price is now 36% above the levels of June 30, 2017. While the stock does offer exposure to rising copper prices UBS believes it is too expensive, considering the short four-year mine life at DeGrussa.

While Black Butte offers a longer-term growth option the broker envisages a number of risks in terms of timing, permits and cost. UBS downgrades to Sell from Neutral and raises the target to $6.74 from $6.66.

Total Recommendations Recommendation Changes

Broker Recommendation Breakup

Broker Rating Order Company New Rating Old Rating Broker Upgrade 1 APOLLO TOURISM & LEISURE LTD Buy Neutral Morgans 2 CSR LIMITED Neutral Sell Morgan Stanley 3 IOOF HOLDINGS LIMITED Buy Neutral UBS 4 OROCOBRE LIMITED Buy Neutral Macquarie 5 SOUTH32 LIMITED Buy Sell Macquarie 6 WHITEHAVEN COAL LIMITED Buy Neutral Macquarie 7 WHITEHAVEN COAL LIMITED Buy Neutral Morgan Stanley Downgrade 8 BABY BUNTING GROUP LIMITED Sell Neutral Citi 9 FORTESCUE METALS GROUP LTD Sell Buy Citi 10 NORTHERN STAR RESOURCES LTD Sell Neutral UBS 11 SANDFIRE RESOURCES NL Sell Neutral UBS Recommendation Positive Change Covered by > 2 Brokers Order Symbol Company New Rating Previous Rating Change Recs 1 S32 SOUTH32 LIMITED -29.0% -57.0% 28.0% 7 2 WHC WHITEHAVEN COAL LIMITED 44.0% 19.0% 25.0% 8 3 IFL IOOF HOLDINGS LIMITED 100.0% 80.0% 20.0% 5 4 NUF NUFARM LIMITED 71.0% 57.0% 14.0% 7 5 ORE OROCOBRE LIMITED 71.0% 57.0% 14.0% 7 Negative Change Covered by > 2 Brokers Order Symbol Company New Rating Previous Rating Change Recs 1 SM1 SYNLAIT MILK LIMITED -100.0% -67.0% -33.0% 3 2 NWS NEWS CORPORATION 20.0% 50.0% -30.0% 5 3 FMG FORTESCUE METALS GROUP LTD 43.0% 71.0% -28.0% 7 4 BBN BABY BUNTING GROUP LIMITED 25.0% 50.0% -25.0% 4 5 PRU PERSEUS MINING LIMITED 50.0% 67.0% -17.0% 4 6 SXY SENEX ENERGY LIMITED 29.0% 43.0% -14.0% 7 7 NST NORTHERN STAR RESOURCES LTD -57.0% -43.0% -14.0% 7 8 WSA WESTERN AREAS NL -33.0% -20.0% -13.0% 6 9 SFR SANDFIRE RESOURCES NL -29.0% -17.0% -12.0% 7 10 RRL REGIS RESOURCES LIMITED -43.0% -33.0% -10.0% 7 Target Price Positive Change Covered by > 2 Brokers Order Symbol Company New Target Previous Target Change Recs 1 NUF NUFARM LIMITED 9.783 9.440 3.63% 7 2 WHC WHITEHAVEN COAL LIMITED 4.656 4.506 3.33% 8 3 S32 SOUTH32 LIMITED 3.310 3.224 2.67% 7 4 IFL IOOF HOLDINGS LIMITED 12.160 12.010 1.25% 5 5 NST NORTHERN STAR RESOURCES LTD 5.473 5.411 1.15% 7 6 WSA WESTERN AREAS NL 3.008 2.990 0.60% 6 Negative Change Covered by > 2 Brokers Order Symbol Company New Target Previous Target Change Recs 1 PRU PERSEUS MINING LIMITED 0.528 0.593 -10.96% 4 2 FMG FORTESCUE METALS GROUP LTD 5.379 5.693 -5.52% 7 3 BBN BABY BUNTING GROUP LIMITED 1.645 1.720 -4.36% 4 4 ORE OROCOBRE LIMITED 7.241 7.399 -2.14% 7 5 NWS NEWS CORPORATION 21.268 21.557 -1.34% 5 6 RRL REGIS RESOURCES LIMITED 3.826 3.867 -1.06% 7 7 SFR SANDFIRE RESOURCES NL 7.120 7.150 -0.42% 7 Earning Forecast Positive Change Covered by > 2 Brokers Order Symbol Company New EF Previous EF Change Recs 1 GXY GALAXY RESOURCES LIMITED 19.280 6.950 177.41% 5 2 SYR SYRAH RESOURCES LIMITED 4.582 -7.399 161.93% 5 3 JHG JANUS HENDERSON GROUP PLC. 370.009 296.473 24.80% 5 4 BKW BRICKWORKS LIMITED 126.425 110.475 14.44% 4 5 AQG ALACER GOLD CORP 5.645 4.999 12.92% 4 6 MIN MINERAL RESOURCES LIMITED 180.175 160.250 12.43% 4 7 SM1 SYNLAIT MILK LIMITED 38.735 35.326 9.65% 3 8 MGX MOUNT GIBSON IRON LIMITED 2.767 2.533 9.24% 3 9 AWC ALUMINA LIMITED 18.110 16.773 7.97% 5 10 IGO INDEPENDENCE GROUP NL 16.780 15.697 6.90% 6 Negative Change Covered by > 2 Brokers Order Symbol Company New EF Previous EF Change Recs 1 MYR MYER HOLDINGS LIMITED 2.990 4.476 -33.20% 6 2 PRU PERSEUS MINING LIMITED 1.125 1.467 -23.31% 4 3 SIG SIGMA HEALTHCARE LIMITED 5.230 5.783 -9.56% 4 4 FMG FORTESCUE METALS GROUP LTD 50.751 56.030 -9.42% 7 5 NUF NUFARM LIMITED 44.551 49.124 -9.31% 7 6 NCM NEWCREST MINING LIMITED 60.656 64.172 -5.48% 8 7 NHC NEW HOPE CORPORATION LIMITED 27.890 29.490 -5.43% 3 8 NWS NEWS CORPORATION 61.098 63.877 -4.35% 5 9 WSA WESTERN AREAS NL 8.678 8.993 -3.50% 6 10 BBN BABY BUNTING GROUP LIMITED 9.525 9.775 -2.56% 4 Technical limitations

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

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Uranium Week: High Turnover, Weak Price

The spot uranium market saw its second highest monthly turnover in March, but still prices slip away.

-Volumes up -Prices down

By Greg Peel

This week's report is relatively brief given last week's Good Friday holiday.

In the week prior, the US Department of Energy announced it would suspend periodic sales of government held uranium which were being used to fund the clean-up of the Portsmouth enrichment facility, removing 1.6mlbs of supply from the market. The market's initial response was unsurprisingly positive.

But it was short-lived. Ongoing concerns regarding other issues, including trade wars, potential buy-US quotas for US utilities and uncertainty surrounding the impact of recent production cut announcements from major producers continue to weigh on sentiment. Despite the DoE news, industry consultant TradeTech's weekly spot price indicator fell -US65c to US$21.00/lb last week.

The end-March price is down -US50c from the end-February price.

The volume of trading in March was nevertheless the second highest on record. There were 48 transactions completed in the month, totalling 6.3mlbs U3O8 equivalent. The number of yearly spot transactions nearly doubled since 2012.

Not that it's done much for the price.

Traders and intermediaries continued to dominate both sides of the market in March, but 20% of the buy side was represented by utilities, which is at least an improvement.

Term markets have remained relatively quiet due to the uncertainty facing US utilities. TradeTech's term price indicators have again ticked down, to US$25.50/lb from US$25.75/lb (mid) and to US$28.00/lb from US$29.00/lb (long)

The Short Report

Guide:

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

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

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

Summary:

Week ending March 29, 2018

It was all downhill last week for the ASX200 as the US/China tit-for-tat trade war fired up, before escalating this week. In the process, the prior strong support level of 5800 was breached, and that level has now become resistance.

It was also one of the dullest weeks ever on record in terms of short position movements. Perhaps Easter holiday plans were more pressing.

Notably, there is not one sign of green on the table below. I can't remember that ever happening before. Nonetheless, all the red moves represent minimal bracket creep.

For the sake of anything to report, we can note Myer ((MYR)) keeps jumping in and out of the 10% plus shorted club each week but basically remains around 10% shorted as the share price slips away.

The share price of embattled Retail Food Group ((RFG)) continues to plummet yet the shorters remain unmoved.

Shorts in electronic payment disruptor Afterpay Touch ((APT)) continue to climb each week, slowly, now placing the stock in the 7% shorted bracket. Yesterday the company provided a preliminary quarterly update and the stock fell -6%.

The company is upgrading its procedures to prevent under-age usage, which will represent a cost. The founders' shares are about to come out of escrow.

That's about it. No Movers & Shakers this week.

Weekly short positions as a percentage of market cap:

10%+

SYR 20.5 DMP 17.1 JBH 16.7 GXY 14.2 HSO 13.9 IGO 12.0 VOC 11.7 MYR 11.0 RFG 10.8 MYX 10.8 NAN 10.5 HT1 10.2

In: MYR

9.0-9.9

ORE, FLT, APO, AAC, NWS

Out: MYR

8.0-8.9%

BWX, AAD, HVN, PLS

No changes

7.0-7.9%

MTS, TGR, APT, GMA

In: APT

6.0-6.9%

BAP, TPM, BEN, GXL, IVC, ING, BGA, SUL, QUB

In: IVC, BGA, SUL

5.0-5.9%

KAR, CSR, IFL, SEK, JHC, AHG, RSG, WEB, RIO, IPH, MOC, MLX, GEM

In: IPH, MOC Out: IVC, BGA, SUL

Movers & Shakers

See above.

ASX20 Short Positions (%)

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

IMPORTANT INFORMATION ABOUT THIS REPORT

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

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

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

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

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

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

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

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

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The Wrap: Tax, Housing, Trade And Banks

Weekly Broker Wrap: Corporate tax cut; house prices; trade wars; and banks.

-Proposed tax cut to have minimal impact in short-medium term -Property market uncertainty to continue over 2018 -Governments expected to be wary of escalating trade wars -Higher levels of due diligence on mortgages likely to be asked of the banks

By Eva Brocklehurst

Corporate Tax Cut

The Australian government's proposed corporate tax cut, to 25% from 30%, will be far less influential than the recently implemented US tax cuts, UBS suggests.

It is materially smaller, delayed and staggered, and to be phased in from 2023 to 2027. Moreover, Australia's imputation system arguably also makes a corporate tax rate cut less relevant, although the broker points out it is not irrelevant.

In the long run a corporate tax cut is likely to have a net positive impact on the economy but the immediate impact on the forecast horizon is considered minimal. UBS believes tax cuts are supportive for business investment and overall GDP because, historically, shifts in company profits are a key driver of business investment.

If there is a change of government the broker concedes it possible there could be a lower tax rate co-existing with the Australian Labor Party's proposed imputation rebate. The impact of both pieces of legislation would be to make the pre-payment of excess franking balances more attractive.

House Prices

House prices fell for a sixth consecutive month in March and are now down -3.5% annualised. While there appears to be little flow through to broader conditions, Morgan Stanley believes risks are building over 2018.

Building activity has held up versus expectations, so far, while consumer confidence also remains slightly above trend, even in housing-specific indicators. Meanwhile regulatory scrutiny for the banking system, and by association the mortgage market, is likely to remain elevated for much of 2018.

Further regulatory tightening of credit, and and increasing stock of properties to be settled amid uncertainty regarding government housing policy are all factors that are likely to be challenging over 2018. This makes Morgan Stanley cautious regarding the broader economy in 2018, giving the leveraged exposure to the property market.

Protectionism

Escalating trade wars between the US and China could lead to stagflation for the global economy, although Citi suggests risks appear contained with regard a full-blown trade war.

The real-time response of financial markets to the erecting of trade barriers, including sharp falls in share prices, provides a signal for governments to be wary of escalating measures.

Tariff increases by the US, China and the EU of 10 percentage points would result, in the broker's calculations, in a reduction to global GDP of -2% from the base-line level after one year, moderating to -1.5% after three years. The impact on Australia's GDP would be a reduction of -0.5% after one year and -1.25% after three years.

The Productivity Commission has looked at the consequences for Australia of a trade war, including a 15 percentage point increase in tariffs globally. In this pessimistic scenario, economic activity is calculated to be more than -1 percentage point lower while employment would be reduced by -100,000 and almost 30% of households would experience a drop in purchasing power of at least -4%.

Citi believes these modelled results represent a worst-case scenario because the current trade battle is largely between the US and China and does not include the EU, and Australia still has access to both markets.

Banks

The latest financial aggregates data from the Reserve Bank indicates credit growth is still being buoyed by housing. Housing credit increased by 0.5% in February and 6.2% over the 12 months to February.

System credit growth is tracking slightly ahead of Credit Suisse' projections, reflecting very resilient housing credit. Business credit increased by 0.1% and 3.6% over the 12 months while personal credit fell by -0.2% and contracted by -1.1% over the 12 months.

Morgan Stanley observes investor mortgages slowed further in February and the latest quarterly approvals show interest-only loan flows are just 16% versus the 30% threshold. Both trends are negative for margins, the broker asserts. Morgan Stanley expects around 4% growth in mortgage volumes for the major banks in 2018 despite efforts to lift both investor property lending and interest-only loans.

Meanwhile, the ACCC has released its interim report on residential mortgage price competition. The report finds that idiosyncratic discounting by banks makes it hard for price discovery for prospective borrowers and poses this as one of the reasons for the prevalence of mortgage brokers.

The inquiry concluded that the "no-frills" residential mortgages are not always the cheapest. A lack of vigorous price competition was also noted. Credit Suisse believes increased transparency is a likely outcome of this inquiry but recommendations are likely to fall short of regulated pricing.

The first round of the Royal Commission into Financial Services was more severe than UBS anticipated. Irresponsible lending was a key finding. The broker expects a higher level of due diligence will be recommended for banks. In particular, banks may need to undertake a detailed assessment of each customer's living expenses and over-stated income will require extra validation.

UBS has estimated the impact of higher household living expenses on borrowing ability, using bank home loan calculators and benchmarks. The calculation is then re-run using what the broker considers are more realistic living expenses. UBS found borrowing limits provided by the bank calculators fell by -35% as a result.

Bank returns on equity are nearly -2 percentage points lower than they were 20 years ago. Credit Suisse notes, while there is similar leverage, there are substantially lower income contributions, offset by better expense ratios.

With bad debts at cyclical lows the broker believes the banks will need to focus on capital optimisation and expenses if they are going to hold current margins. In this environment, the broker prefers banks with established productivity programs and National Australia Bank ((NAB)) is the top pick.

Sino Gas Expected To Prevail In Linxing

Brokers remain confident Sino Gas & Energy can prevail amid tough negotiations with joint venture partners in Linxing, China.

-China's need for foreign expertise should ensure a successful outcome to negotiations -Main area of contention is the definition of exploration and development costs -Stock may underperform in the near term although overdue payments should be forthcoming

By Eva Brocklehurst

Sino Gas & Energy ((SEH)) is in the process of concluding commercial negotiations with its SGE joint venture partner, CUCBM, and an in-principle agreement to the overall development plan has been received.

2017 results missed expectations because of higher costs at the operations in China. Macquarie considers this a minor hiccup and the prevailing wheeling and dealing more about the company entering the final hard part of negotiations.

In the short term, Sino Gas still plays a critical role in supplying gas in China for the future. Maintaining a conservative outlook for production, the broker envisages substantial upside through extended terms.

The ongoing dispute involves a subsidiary, SGE, in which Sino Gas holds a 49% interest, and China New Energy 51%, and resulted in US$7.8m in gross gas sale payments from CUCBM being overdue at the end of 2017.

This is expected to increase by an additional US$9.8m over the first quarter of 2018. The main area of contention has been the differentiation between exploration and development costs.

Given different recovery calculations apply, depending on whether costs are applied to exploration or development, this has had a bearing on the valuation of the project and initial cash flow for Sino Gas.

Amid negotiations, CUCBM, which has a 30% stake in Linxing, withheld gas sale proceeds from the joint bank account maintained with SGE, which has a 64.75% stake. (CBM Energy has 5.25%). Sino Gas has now received assurances from CUCBM that US$8.6m will be paid once the cost allocation principles have been finalised.

Macquarie believes Sino Gas desires to, at least, maintain the value of its holding in the project, which relates to the expiry of the Linxing PSC and the SGE working interest, as well as the aforementioned delays to payments. The broker retains an Outperform rating and 20c target.

Gas Demand

Chinese gas demand was up 15% in 2017 and growth is not expected to slow materially in 2018 as coal to gas switching continues, Canaccord Genuity observes.

The company has extended its gas services agreement at Linxing by another year at US$7.23/mcf, up from US$6.4/mcf. This was slightly ahead of the broker's expectation in US dollar terms, despite a stronger renminbi.

Production for the March quarter averaged 24mmscf/d. The company has signalled that it still expects commissioning of Linxing North in the September quarter.

Previous Negotiations

Citi, maintaining a Buy rating and 27c target, notes the last time a partner withheld payment the Sino Gas share price declined to 3c per share. That particular instance was characterised by a dispute about whether SGE should be paid at all for Sanjiaobei pilot production, and the stalemate resulted in production being shut in.

This time the dispute centres not on whether a payment is warranted, but rather on the precise mechanism to release payments. Citi observes deteriorating sentiment could mean Sino Gas underperforms in the near term but suspects payment will be forthcoming over the coming months.

Canaccord Genuity believes perceptions of heightened sovereign risk are offset by the progress being made at both Linxing and Sanjiaobei as well as the company's previous success in dealing with its SGE partner (PetroChina) at Sanjiaobei. Prior gas shortages in winter and China's need for foreign capital and expertise to increase indigenous gas supplies are also supportive of a successful outcome.

Liquidity is not considered at risk, given existing cash flow and undrawn debt from the Macquarie facility. Sino Gas finished the year with US$28m in cash and US$1.6m in joint venture cash balances. The US$100m facility with Macquarie is drawn down at just US$10m.

Canaccord Genuity believes it is too early to tell whether there will be any tweaking of the Macquarie facility as a result of the negotiations at Linxing. The broker retains a Buy rating and 24c target.

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Orthocell: Next Big Thing In Tissue Engineering?

Regenerative medicine pioneer Orthocell closes in on market payday.

-Orthocell's new product, CelGro, has received approval to be marketed in Europe -The company is producing solid sales in cell-culture therapies -Established products still have plenty of growth potential

By Nicki Bourlioufas

Tennis elbow, golfer's elbow, rotator cuff tears, osteoarthritis – it's a world of pain out there, but advances in regenerative medicine by a young Australian company are offering relief to millions of people around the world, as well as the prospect of significant gains for investors.

Orthocell ((OCC)) is a regenerative medicine company focused on regenerating mobility for patients by developing products for the repair of a variety of soft tissue injuries. Orthocell has two well-established medical products on the market, plus a new breakthrough technology that specialist analysis house NDF Research says "may deliver the big payday this financial year". The company also has two projects in the pipeline that promise continued growth for the stock over the medium to long term.

[Please Note: NDF Research discloses that Orthocell commissioned and paid for the preparation of its report. NDF Research, which is led by founder and senior analyst, Stuart Roberts, is an equity research firm based in Sydney, Australia, which focuses on Life Science companies that are publicly traded on the Australian Stock Exchange. NDF believes that ASX-listed companies have been largely overlooked in the global life sciences boom that began in late 2008, partly because of insufficient quality research. NDF's goal is to provide such research, and introduce investors around the world to potential future billion-dollar companies from Australia.]

Orthocell's new product, CelGro, has recently received CE Mark approval, which allows it to be marketed and distributed in the European Union. US approval is expected soon. NDF Research estimates CelGro's potential market is well in excess of US$2bn.

Orthocell's established products still have plenty of growth potential. NDF Research says Orthocell's foundation product, Ortho-ACI – which costs US$10,000 per procedure – probably has a US$300m-350m opportunity across Orthocell's target market.

The company's other commercially available product, Ortho-ATI, costs US$4,500 per patient, suggesting it represents a US$6.5bn opportunity for rotator cuff repairs alone.

NDF Research's target price for the company is $1.75 per share. This is the midpoint between its base case of $0.89 and its optimistic case of $2.63. Orthocell has recently been trading around the $0.30 mark.

Orthocell stakes its claim in regenerative medicine field

Regenerative medicine uses drugs and biotechnology to harness the power of stem cells and related growth factors to repair damaged bone and soft tissues, such as tendons and cartilage.

NDF Research says Orthocell, like other publicly traded biotech and medical device companies working in the field, has been undervalued because of the controversy around the ethical use of stem cells and because many therapies are still in clinical development.

Orthocell's Ortho-ACI provides a therapy known as "autologous chondrocyte implantation". This uses cartilage cells (chondrocytes) taken from the patient themselves (autologous) and engineered in the lab before they are implanted back into the patient. Ortho-ACI has been used in more than 480 patients since 2010 to treat conditions such joint injuries.

Its product Ortho-ATI uses implants of autologous tendon cells (tenocytes) for treating conditions such as to hamstring, Achilles Tendon and Anterior Cruciate Ligament injuries.

NDF Research says Ortho-ATI is "a market-leading product" as it is the first – and still the only – product that draws on regenerative medicine to repair damaged tendons.

Both Ortho-ACI and Ortho-ATI have approval from the Therapeutic Goods Administration. Ortho-ATI is soon to be the subject of a study to assess its safety and effectiveness compared to corticosteroid injection in the treatment of rotator cuff tendinopathy and tear. The research is being undertaken in collaboration with DePuy Synthes Products, Inc, part of Johnson & Johnson Medical Device Companies.

Collagen 'scaffold' for tissue growth will drive stock price

Most exciting, says NDF Research, is Orthocell's new product CelGro. This uses high-purity, natural collagen to build a "scaffold" that supports the growth of new tissue at the site of an injury. Such scaffolds can be used to support healing in a variety of orthopaedic, reconstructive and surgical applications.

NDF Research says CelGro is "arguably one of the best tissue repair scaffolds yet invented" and is "unique" in that it is "completely acellular" and has ideal mechanical properties and the right "integration profile" to hasten in-growth of tissue. As well, it has a tunable "degradation profile" – that is, it can be set to biodegrade once the new tissue is in place.

NDF Research says receiving the CE Mark has taken the risk out of CelGro. Further regulatory approvals for CelGro in other jurisdictions, such as the US, and across other indications, such as nerves and ligaments, will provide key catalysts for Orthocell's share price.

Products in pipeline take a different tack

Orthocell's commercially available products are autologous therapies. Such patient-derived therapies are relatively expensive, because each dose needs to be manufactured individually. Even so, NDF Research says, Orthocell's autologous therapies are cost-effective, because they are "fit for purpose" and work better than current alternatives that are commercially available.

The alternative is "allogeneic therapies", which use cells taken from an unrelated donor, rather than the patient. These generally cost less because they can be bought "off the shelf". Orthocell's is exploring this possibility with the two products it now has in early research. These are the "Lab-Grown Tendon" project, in which human tendons grown in a bioreactor may be used in tendon repair, and the "Cell Factories" project. NDF Research says these projects "have the potential to become the Next Big Things in tissue engineering".

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