ANALYST OUTLOOK FOR FY21.

Our analysts share their outlook and top stock picks for FY21.

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BANKS & GENERAL INSURERS.

TS Lim

Our FY2021 top three picks possess strong risk management capabilities and defensive qualities including healthy balance sheets and surplus capital that could be returned to shareholders. These companies have undergone massive transformation over the years to improve the quality and consistency of their earnings.

Our selection comprises one diversified financial (MQG), one major bank (CBA) and one regional bank (MYS). The operating environment remains positive for MQG (e.g. capitalising on rising global demand for asset and risk management services and infrastructure/green investments) while CBA and MYS appear well-placed given sound underlying fundamentals to capitalise on postpandemic opportunities.

Macquarie Group (MQG)

MQG remains our top stock pick. Underlying earnings numbers were strong despite having none of the huge prior year asset sales – and if COVID-19 related charges are excluded, profit would have been 4% higher in FY20. MQG's annuity-style and markets-facing activities continue to work well, being capital efficient in ensuring capital can be shifted to activities with higher incremental returns. Capital management flexibility is also characterised by a final dividend in FY20 that was entirely funded by non-bank activities. In essence, MQG remains a longer term "Cash and Growth" story with $25bn equity yet to be deployed in infrastructure and other assets.

Buy, Price Target $135.00

Commonwealth Bank (CBA)

FY20 profit will be dragged down by COVID-19 but underlying income should be stable and costs are expected to be well-managed. The balance sheet remains in good shape with sufficient capital, funding and provisions, and sound overall asset quality. The announced sales of interests in Colonial First State and the Indonesian life business should lift CET1 to 11.4-11.5% and place CBA ahead of its domestic peers and near the top end of the global "unquestionably strong" club. Excluding COVID-19 and other provisions, underlying organic capital generation in 3Q20 was strong at +12bp and we still think there is scope for CBA to declare a small 2H20 dividend of 100¢ in August.

Buy, Price Target $72.00

MyState (MYS)

Our positive view is based on few distractions facing the bank, an organic growth strategy that is profitable, future-focused and built around a scalable, digital platform. MYS is an approved lender in both the government's Coronavirus SME Loan Guarantee and First Home Loan Deposit schemes, which should provide a lending backstop to underpin organic revenues. Cost discipline remains a key value lever (restructuring benefits should start to flow in 2H20) and the long term aspiration of ~60% CIR is unchanged. We also take comfort in the quality of its lending book, with arrears well below industry levels by at least 90bp.

Buy, Price Target $4.50

DIVERSIFIED FINANCIALS & FINTECH.

Lafitani Sotiriou

AMP (AMP)

We believe the worst is over. AMP's Life sale provides a meaningful capital injection, for the company to complete its transformation project which includes $140m in post-tax synergies and to potentially embark on a share buyback, organic and inorganic growth opportunities. The company has largely repriced its front and back book, and is on track to be 80% through its remediation program this year, with the Royal Commission impact largely factored in.

Trio of Fund Managers (JHG, PDL, PPT)

We recommend Buying a trio of Fund Managers for exposure to a sector that is relatively cheap, still paying healthy dividends, and set to experience meaningful positive mark-to-markets in the June quarter given equity market gains are around 17% during the period in both Australia and MSCI index. More specifically, JHG is the cheapest, with a meaningful buyback and high cash generation, PDL's performance fees are set to return and PPT has the Trillium acquisition and Corporate Trust growth to look forward to.

Afterpay (APT)

APT remains a key pick despite its strong run. We believe the stock remains in an upgrade cycle, with the next catalyst being the June quarter update due out around mid-July. We believe a key to Afterpay's continued success will be its ability to further its integrations with other key e-commerce and payment infrastructure players in the market with its one-to-many strategy (i.e. integrate with a key piece of infrastructure and the growth can accelerate). Key examples include its integrations being worked on with Visa, Mastercard, eBay (possible outside of Australia), and Wix (a competitor to Shopify). Further, it has geographic expansion it is chasing, with Canada flagged to launch before the end of this calendar year.

Life 360 (360)

Life360 (360) is our other high conviction pick which has languished in its share price performance of late. We see 360 as one of the few microcaps on the ASX with a true global footprint, with approximately 28m monthly active users. We see a catalyst being its new product launch which is set for around July this year with new pricing and features to be announced.

LISTED INVESTMENT COMPANIES (LICs) & TRUSTS (LITs).

Will Gormly

2020 has reminded investors to expect the unexpected whilst remaining vigilant and flexible with their investment portfolios.

Stalling economic growth from the global pandemic has resulted in a wide variety of administrative actions from each country and state. Geographical diversification is as important now as it has ever been, and our top picks focus on how to easily gain access to diversified equity portfolios via high quality global LIC/LITs.

The FY21 top picks are MFF Capital Investments Limited (MFF) which has delivered superior long-term performance and now holds a large cash balance, Magellan Global Trust (MGG) which provides access to a high quality manager of leading global companies, and WCM Global Growth Limited (WQG) which invests in global quality companies with a rising competitive advantage and a corporate culture that supports the expansion of this moat.

MFF Capital Investments Limited (MFF)

MFF's primary focus is to invest in large listed international companies that have attractive business characteristics at a discount to their assessed intrinsic values. The Company has provided shareholders with a net total return of over 18% p.a. over the past 10 years, as at 31 May 2020. Over the same period the MSCI World Index (in AUD) returned 11.9% p.a. The portfolio is highly concentrated, with the top holdings at the end of May being Visa (18.6%) and MasterCard (17.2%). Net cash as a percentage of investment assets and cash had grown to 46.7%, at 12 June 2020. At this time MFF traded at a 1.9% discount to the pre-tax NTA. As a result of large profitable realisations of investments, MFF continues to pay large tax instalments which ultimately decreases the NTA. However, shareholders will benefit from the pass through of franking credits attached to future dividends, and the franking credit balance has grown significantly in 2020 to an estimated ~$100m. We calculate MFF's indirect cost ratio at ~0.41% and the Company does not incur a performance fee.

Magellan Global Trust (MGG)

MGG is a Listed Investment Trust that seeks to invest in a focused portfolio of outstanding global companies and seeks to purchase investments when they are trading at a discount to their assessed intrinsic value. Magellan undertakes extensive fundamental analysis on the individual companies and the industries in which they operate. MGG aims to invest in 15 to 35 of the world's best global stocks whilst targeting a 4% p.a. cash distribution yield. As at May 2020, the Fund had returned 12.5% p.a. since inception. This is an outperformance of 1.5% p.a. over the MSCI World Net Total Return Index (AUD) over that period. MGG traded at a 2.7% discount to the NAV at this time and was trading on an annualised 12-month net yield of 3.64%. This provides investors with income diversification whilst still maintaining a current exposure that is weighted towards some of the largest internet & eCommerce, technology, and payments companies.

WCM Global Growth Limited (WQG)

WQG aims to provide access to an actively managed portfolio of quality global companies found primarily in the high growth consumer, technology, and healthcare sectors. The portfolio is managed by WCM Investment Management (WCM), a California-based specialist global equity firm with an outstanding long-term investment track record. WCM's investment process is based on the belief that corporate culture is the biggest influence on a company's ability to grow its competitive advantage or 'moat'. As at May 2020, WQG recorded a 12-month net shareholder return of 19.0% (not adjusted for option dilution), outperforming the MSCI ACWI ex-AUS Index (AUD) by ~8.0%. On 12 June 2020, WQG traded at a 14.2% discount to the NTA before tax and provided shareholders with an annualised unfranked dividend yield of 3.4%. With large weightings in the portfolio towards Information Technology (~24.1%) and Health Care (~23.6%), WQG is well positioned for the post-COVID-19 recovery that seems set to change consumer behaviour. The top position at the end of May was Shopfiy Inc., a Canadian e-Commerce platform for online stores.

AGRICULTURAL & FMCG.

Jonathan Snape

Investments in the Agricultural & FMCG sector should be considered high risk and come with volatility. For this reason we tend to focus on stocks where we see either: a structural uplift in ROIC through the cycle, cyclical growth stories, or counter-seasonal crop exposures.

Our key commodity call for 2020 has been the unwinding of the drought induced dislocation between domestic cattle prices and export meat prices on a normalisation in weather patterns and more recently the normalisation of domestic grain prices to international benchmarks. The three stocks listed below carry varying degrees of exposure to these dynamics.

Inghams Group (ING)

ING is a leading vertically integrated poultry producer (from stock feed to end products) with a market leading position in Australia and the number 2 participant in New Zealand.

We see ING as a second derivative beneficiary of improved seasonal conditions, lifting Australian grain production. We expect a normalisation in cropping volumes to drive a rapid contraction in Australian wheat prices, which should result in a material contraction in feed costs from 2H21e. Between FY16-19 Australian benchmark wheat prices rose ~85% resulting in Australian grain trading at a premium to US wheat three times historical levels. A normalisation in this historical premium is likely to prove a tailwind to earnings in an environment where competing protein prices face upward pressure. We are already seeing a rapid contraction in new season crop prices and expect ING to benefit from this dynamic in Fy21e, at a time when COVID-19 related demand headwinds are likely to be weakening.

Elders (ELD)

ELD is a leading supplier of fertiliser, agricultural chemicals and animal health products to rural and regional Australia, with strong agency positions in livestock, wool and real estate.

The recent share price of ELD has benefited from rainfall and strong cattle prices . However, we continue to see consensus FY21-22e earnings as yet to reflect the annualised benefit of the AIRR acquisition (and synergy realisation), a normalisation in the summer crop (sales flow in 1H21e) or incorporating the scale of upside from integrating three generic portfolios across the combined ELD + AIRR business. We also see upside from migrating independents onto the AIRR platform (~600 independents in the market).

Rural Funds Group (RFF)

Rural Funds Group (RFF) is a listed agricultural REIT with a portfolio covering 50 properties, focused on, almond orchards, vineyards, cattle, cotton and macadamias. Assets in the portfolio are some of the most productive in the industry and leased to high quality tenants including Treasury Wine Estates, Olam, Select Harvests, AACo and Stone Axe Pastoral, with a WALE of 11.3 years. RFF is externally managed by Rural Funds Management (RFM), who have been managing agricultural investments since 1997.

The RFF portfolio continues to transition to natural resources (from 46% to 59% of FY20e revenues), which are appreciating rather than depreciating assets, and towards assets with market linked rental reviews (from 37% to 43% of FY20e revenues). Over time as capex is deployed we expect favourable asset revaluations and growth in rental incomes from newly acquired assets. In addition as the investment in the cattle sector has lifted so too has the exposure the business has to cattle prices, through EYCI rent linkages on some leases.

TECHNOLOGY.

Chris Savage

We continue to be positive on the technology sector in Australia as, in an environment of low interest rates and low growth, we believe there are a number of good quality stocks in the sector with reasonable to strong growth outlooks.

We acknowledge many stocks in the sector have had a strong re-rating over the past few years but believe there is still some value in the sector with a number of good quality stocks on reasonable forward PE ratios. Our goal is to find good quality tech stocks with strong growth outlooks that are currently trading on forward PE ratios of around 25x or less and that, over time, can re-rate up to over 30x as has happened with stocks like WiseTech Global (WTC) and Altium (ALU).

Uniti Group (UWL)

Uniti is a diversified provider of telecommunications services, specialising in fixed-wireless, fibre and specialty telecommunication services. The company has grown rapidly through a number of acquisitions over the past 12 months and is now a strongly profitable and highly cash generative business. Uniti looks set for further strong growth over the next 12 months through both organic growth and the proposed acquisition of Opticomm which is scheduled to go ahead in September or October. The stock looks reasonable value on an FY21 PE ratio of around 25x.

Buy, Price Target $2.25

Infomedia (IFM)

Infomedia is a leading provider of software solutions to the parts and service sectors of the global automotive industry. The company has a solid growth outlook due to good momentum in its Service business and expected rapid growth in its relatively new Data business. The shares have underperformed the sector, however, due to an equity raising in April which was not done in conjunction with an acquisition. We do, however, expect acquisitions to commence in 1HFY21 and for this to provide a catalyst for the share price. The stock looks reasonable value on an FY21 PE ratio of around 25x.

Buy, Price Target $2.00

PWR Holdings (PWH)

PWR is a leading provider of customised cooling solutions to the global motorsports market as well as the wider automotive industry. While it is technically a manufacturer we also see it as a tech company due to the high level of IP in its products. The company has been negatively impacted by COVID-19 – due to the cessation of elite motorsport globally – and we have had to downgrade our FY20 NPAT forecast by around 25%. We do, however, expect a strong recovery in FY21 – due to the recommencement of elite motorsport – and an unusually strong 1HFY21 result which should provide a catalyst for the share price. The stock looks reasonable value on an FY21 PE ratio of around 25x.

Buy, Price Target $5.00

DISCRETIONARY RETAIL & PROFESSIONAL SERVICES.

Sam Haddad

Retail

The COVID-19 pandemic has had some significant impacts on the retail sector, although the key overarching trend that has emerged is the acceleration to online shopping. While the easing of social distancing restrictions will see some unwind of this, we believe there will be some enduring impacts on consumer shopping behaviour.

We believe the outlook for consumer discretionary spending remains highly uncertain. Key risks to consumer demand include: 1) increased unemployment and the outlook for this once JobKeeper unwinds coupled with weak business confidence; 2) the unwind of other government support initiatives such as rent relief and loan deferrals; and 3) a 'second wave' scenario of COVID-19 cases, impacting the recovery of foot traffic in malls.

Our favoured retailers also have a strong balance sheet, flexible cost structure, and low risk inventory model.

Temple & Webster (TPW)

TPW is Australia's largest online only furniture and homewares retailer with >180,000 products on sale from hundreds of suppliers. TPW is the most leveraged retailer to the online shift in our research coverage. The company has a strong balance sheet with ~$29m in net cash at hand, a flexible cost structure and a low risk inventory model with drop-ship accounting for ~80% of revenue. Drop-ship is a capital light and negative working capital fulfilment model where products are sent directly to customers by suppliers, enabling a larger product range, faster delivery times and reducing the need to hold inventory. The drop-ship range is complemented by a private label range which is sourced directly by TPW from overseas suppliers. There are several initiatives underway or in the pipeline to drive sales growth including: adding depth and breadth to the company's core offer; continuing to invest in the trade and commercial segment; adding new adjacent categories; raising brand awareness (TV advertising recently commenced); and the launch of a mobile app.

City Chic Collective (CCX)

CCX is a global multichannel retailer, with almost two-thirds of sales online, specialising in plus-size (size 14+) women's apparel, accessories and footwear. It is a collective of customer-led brands including City Chic, Avenue and Hips & Curves. City Chic appeals to fashion-forward women and its multichannel model comprises: a network of >90 stores across Australia/New Zealand; multiple websites operating in Australasia and USA; and marketplace and wholesale partnerships in the USA and Europe. Avenue targets value-conscious women and Hips & Curves is an intimates brand; both are online only with a significant customer following throughout the USA. We believe CCX is well positioned in this environment given the company's: strong online presence; minimal debt position; flexible supply chain (able to align intake to consumer demand/preferences); and low fixed costs structure (including recent successful rent reductions with landlords). Avenue.com has (as at CCX's 25 May update) traded resiliently during the pandemic. We attribute this to Avenue's strong offering in casual wear which we believe is resonating strongly in the current difficult environment.

Professional services

IPH Limited (IPH)

IPH wholly owns Spruson & Ferguson, Pizzeys, AJ Park, Griffith Hack, Shelston IP and Practice Insight. IPH is the leading Intellectual Property (IP) services group in the Asia-Pacific region, with specialist services spanning the protection, commercialisation, enforcement and management of IP. The group comprises a team of ~1000 staff that services a diverse client base of Fortune Global 500 companies and other multinationals, public sector research organisations, foreign associates and local clients. The key positive factors we see for IPH include: 1) market leader in a sector that has proven relatively resilient through previous economic downturns; 2) strong cash flow generating business (gross conversion >90%); 3) strong and expanding exposure to the high growth Asian IP market; 4) synergy opportunities from recent acquisitions (including XIP and AJ Park); and 5) expansion prospects in new secondary IP markets.

INDUSTRIALS.

Alex McLean, James Filius & Hamish Murray

Carbon Revolution (CBR) (Speculative)

Carbon Revolution (CBR) is an advanced manufacturing company that has developed the only single piece carbon fibre automotive wheels to Original Equipment Manufacturer (OEM) quality standards with commercial adoption across several major OEM models.

COVID-19 left CBR exposed to the closure of key customer factories in the US, Italy, Canada and Spain, delaying the production of end-vehicles and disrupting the delivery of finished wheels.

With all customer factories now reopened and some manufacturers, like Ferrari, planning to catch up lost production in the second half of CY20, CBR is positioned to return to more normalised volumes in 1QFY21.

In our view, CBR should continue to rerate if the company can achieve the pre-COVID volumes implied by prospectus forecasts in FY21e. Longer-term, we continue to like CBRs first mover advantage, Intellectual Property, and ability to generate material revenues off relatively low implied vehicle volumes.

Buy (Speculive.), Val. $2.42ps

Corporate Travel (CTD)

CTD is a corporate travel service provider with operations in Australia & New Zealand, North America, the UK and Asia. CTD's business model revolves around its customer value proposition which combines superior client service and technology solutions to deliver return on investment and cost savings to corporate clients. In our view, we see CTD continuing to leverage this value proposition, further increasing its market share both domestically and internationally. Despite the uncertainty facing the outlook for global travel, we remain attracted to CTD as a pure play on the corporate travel market, exposure to domestic travel (c.60% of total turnover) and ability to operate profitably off a low base due to its lean operating model driven by automation.

Buy, Price Target $13.75

Emeco Holdings (EHL)

Emeco Holdings (EHL) is a leading provider of earthmoving equipment rental and maintenance services to the Australian mining industry.

EHL is exposed to the Australian mining production cycle that has remained relatively resilient to date. The resilience of mining production was reflected in the company's strong FY20e guidance, which had only minor impacts from increased operating costs relating to COVID-19, plus some headwinds relating to east coast coal markets. We expect further coal related headwinds to impact the company in FY21e, although this looks priced in, while increased exposure to underground gold mining and the strength of iron ore should partially offset any coal weakness.

EHL's high funding costs present some additional risk, although we expect the company to close FY20e with close to $100m in cash which could be used to amortise debt, while a partial refinancing of the senior notes remains an option if credit markets continue to improve. At just 8.5x FY21e underlying P/E, EHL looks oversold on a normalised basis.

Buy, Price Target $1.52

Johns Lyng Group (JLG)

Johns Lyng Group (JLG) is an integrated building services group that primarily delivers insurance building and restoration services (IB&RS), and commercial building services across Australia. With JLG anticipated to deliver a strong FY20 result benefiting from insurance panel wins, increased job volumes and acquisitions which will see JLG enter the Strata Management market, we believe that the company is well positioned as we enter FY21e, for the following reasons:

1. JLGs core IB&RS remains relatively insulated from COVID-19 trading restrictions owing to its "essential service" status.
2. The company enters FY21e with a full job order book resulting from record insurance job registration volumes arising from 6 recent catastrophic weather events including East coast bushfires, and QLD & NSW hailstorms. During the calendar year to May 2020, JLG has registered ~55,000 jobs, which compares to ~61,000 jobs in CY19, which we believe positions the company strongly for work completions in FY21e; and

Alex McLean, James Filius & Hamish Murray

3. We anticipate that the benefits of JLGs integration and cross sell of services into the Strata management market will begin to emerge over the course of FY21e, which will deliver additional revenue gains and improved operating leverage across the business.

Overall we see JLG as a well-funded and strongly positioned business to deliver solid organic growth during FY21e. We see the potential for the business to grow into its multiple as it expands its footprint within the strata management market, with opportunities for strategic acquisitions in this space likely to be highly EPS accretive.

Buy, Price Target $2.90

Mader Group (MAD)

Mader Group (MAD) is a leading provider of specialised contract labour for maintenance of heavy mobile equipment in the resources industry.

MAD has experienced some disruption from COVID-19, having had to temporarily suspend its international division (~5% of FY20e revenues), although it's FY20e guidance range suggests continued growth in Australia and the US has offset the majority of the lost International revenue.

We continue to forecast below trend growth in FY21e given possible headwinds in east coast coal markets (17% of 3Q20 revenue). However, strong growth in its home market of Western Australia (64% of 3Q20 revenue) and North America (6% of 3Q20 revenue) means MAD's growth prospects look cheap at 8.7x FY21e P/E.

Buy, Price Target $1.18

Rhipe (RHP)

RHP provides cloud-based subscription software and service licenses to a growing channel of IT service providers across Asia Pacific (APAC). Software subscriptions are distributed at a wholesale level from world leading software vendors such as Microsoft, Citrix and Symantec. We believe RHP remains well positioned to deliver a solid full year result for FY20 despite the uncertainty facing markets due to its lean operating model and exposure to the digital economy. Ultimately, we believe the cloud computing megatrend – RHP's key structural growth driver - remains intact in a post COVID-19 world and supports RHP's long-term growth outlook. We see two positive catalysts for the stock over the medium term: (1) RHPs entry into the Japanese market starting to become a reality; and (2) $60m net cash position will be used on complementary acquisitions to improve FY21 EPS by up to +50%.

Buy, Price Target $2.30

RESOURCES & ENERGY.

Peter Arden, David Coates & Stuart Howe

The FY21 outlook has been materially altered by the emergence of the COVID-19 pandemic and the implementation of social and economic restrictions to contain it.

For base metals this has certainly had an impact on the demand outlook. Major global economies have been pushed into negative growth and technical recessions. Key indicators of consumption such as manufacturing PMI's have shown rates of contraction not seen for a decade or more. However, the flip side of this has been supply disruption in both the scrap market and dominant metal producing jurisdictions – particularly in South America. This has resulted in forecasts for the supply-demand balance in the market remaining relatively tight. A further mitigating factor has been stimulus packages announced by Governments which have included significant infrastructure programs. Notably, while China as an end user consumes 'just' ~50% of global copper production, the single largest copper metal user globally, China Grid (State power utility) has had its development budget increased by 10%.

The gold price in early 2020 continued to benefit as a portfolio diversifier, but this kicked up a gear with the risks of the COVID-19 pandemic boosting the safe haven trade and what has been a steady stream of fiscal and monetary policy announcements that have added to gold's appeal as a store of wealth. "Whatever it takes" stimulus packages from Central Banks to support market liquidity have raised currency debasement as a thematic and a further attraction for investors to increase exposure to gold. Low interest rates and negative real interest rates, together with the US dollar falling back from its highs, round out an extremely supportive gold price environment.

Energy policy and energy technology are recurring themes for a post COVID-19 economic recovery.

We have a positive medium term outlook for domestic gas markets. The ACCC Gas inquiry 2017-25 continues to highlight the risk of a supply shortfall in east coast markets over the medium term, particularly in southern states. This shortfall is driven by declining Bass Strait supply, increased reliance on Queensland coal seam gas and restrictions with respect to developing new supply. Strong term prices for gas sales out 24+ months also reflect this expected supply deficit.

Oil prices have rebounded strongly following a destructive price war between the world's second largest oil producer (Saudi Arabia) and Russia. Recently improved sentiment in the oil sector has been boosted by OPEC+ members complying with production cut arrangements.

Whilst the risk of a second wave of COVID-19 infections that could further slow the global economy remains, that risk is being outweighed by the effects of a compliant OPEC+ and forecasts for gradually recovering global growth. Under this scenario, we see oil prices remaining relatively steady around current levels over the next two years, as global oil inventories are gradually reduced in an improving economic climate.

Battery raw material markets are expected to strengthen as governments and industry promote electric vehicle (EV) take-up and other carbon abatement technologies.

Markets for lithium are expected to return to deficit over a 3-year outlook. Global auto majors have firm plans for major new investments in EV capacity and new models; in cases like Toyota, EVs could become their dominant product by the middle of the decade. Battery cathode manufacturers are planning further capacity expansions in Europe and Asia to meet projected demand in 2022 and 2023. While deferral and possible cancelation of a number of lithium development projects from the combined impacts of falling prices and reduced funding ability will tighten the projected market balance.

The market for high-purity alumina is also expected to be chronically undersupplied as its use is recognised in advancing lithium ion battery efficiency and safety.

RESOURCES & ENERGY.

Peter Arden, David Coates & Stuart Howe

Alpha HPA (A4N)

A4N's HPA First Project is aiming to supply 99.99% high-purity alumina (4N HPA) to the lithium ion battery and LED manufacturing sectors. 4N HPA is a preferred ceramic for coating polyolefin separators in lithium batteries. The market for 4N HPA is expected to grow from around 30ktpa now to 100ktpa by 2028. The HPA first definitive feasibility study supported 10,000tpa production and annual pre-tax cash flow of $133-280m from capex of $308m. Chemical major Orica is partnering with A4N for input supply and by-product offtake. A4N could be in production in 2022 and benefit from supply deficits and strong pricing.

Speculative Buy, Valuation $0.36/sh

Byron Energy (BYE)

BYE continues to advance the growth of oil and gas output with the installation of the SM58 G Platform underway and expected to lead to new production in September 2020. The new platform will also facilitate drilling of multiple exploration wells in the next two years for which the company is now well funded, having recently raised nearly $30m that included a much larger SPP component after strong shareholder support. Our oil price forecasts reflect the improved pricing since May 2020, with our average forecast WTI prices being US$46.45/bbl, US$32.78/bbl and US$38.48/bbl for FY20 to FY22 respectively. Our long term WTI price forecast is US$45/bbl and we see the Louisiana Light Sweet (LLS) crude price (which BYE receives) gradually returning to a modest premium to that over time. While we are forecasting small losses in FY20 and FY22 and a moderate loss for FY21, we see the company's low operating costs enabling it to continue to generate very useful and growing operating cash flows, aided by useful oil price hedging. Our target price is $0.40/share and our recommendation is Buy.

Comet Ridge (COI)

COI is positioned to develop two coal seam gas projects over the next two years. The Mahalo JV (COI 40%) in partnership with Santos and APLNG, is expected to be development-ready by the end of 2020 and will net COI around 1.5mmboe pa in gas sales. Mahalo North (COI 100%) could be fast-tracked to produce 0.6-1.3mmboe pa in the near term, mostly through existing infrastructure. COI also has longer dated gas projects, including in the Gunnedah Basin, which could eventually be tied-in to STO's Narrabri Gas Project.

Speculative Buy, Valuation $0.19/sh

Mincor Resources (MCR)

MCR's Kambalda Nickel Project has significant attraction but it has not been getting anything like the market attention of some recent nickel discoveries despite delivering further high grade Cassini extensions and being a low capex development underpinned by its attractive and strategic concentrate offtake arrangement with BHP. MCR remains well funded (net cash was $51.9m at 31 March 2020) and is making solid progress towards a nickel restart, advancing its debt funding process and readying the very high grade Cassini deposit for development. Provided nickel prices improve and global nickel inventories decline as expected and assuming further easing of COVID-19 restrictions, FID is likely in 3Q20 so nickel processing can potentially restart around late 2021. Our valuation, which incorporates a higher discount rate (12%) to reflect the greater global economic uncertainty of COVID-19, is $0.87/share and our rating is Speculative Buy.

RESOURCES & ENERGY.

Peter Arden, David Coates & Stuart Howe

Nickel Mines (NIC)

In late 2019 NIC achieved the key milestone of the completion of the ramp-up phase at the Hengjaya and Ranger Nickel Projects at the Indonesia Morowali Industrial Park (IMIP) in Sulawesi. All four NPI production lines reached full production and are now operating at ~42-44ktpa Ni in NPI and at all-in costs of ~US$7,800/t, comfortably below our original steady state forecast of US$8,300/t.

Most recently, NIC has exercised its option to acquire an additional 20% interest in the Hengjaya and Ranger RKEF Nickel Projects, lifting its ownership levels of both from 60% to 80%. Due to the US$120m acquisition being funded entirely by equity, NIC retains a very strong balance sheet with just US$65m debt remaining. Attributable production lifts from ~24ktpa Ni in NPI to ~32ktpa Ni in NPI on our current forecasts. On NIC's current production run-rate this is higher, at ~35ktpa Ni in NPI, making NIC the largest pure-play nickel exposure on the ASX. We retain NIC as one of our top picks on the basis of it remaining cheap relative to peers and its pure nickel commodity exposure – one of our preferred base metals.

Buy, Target Price $1.08/sh

Pantoro (PNR)

After a disappointing 2019, PNR is coming off a low share price base with room to deliver on a more conservative mine plan, exploration success at its 50% owned Norseman Gold Project (NGP) and the first outline of its development strategy for that asset. Over the medium term, PNR also stands to benefit from a re-rating upon becoming a multi-mine producer as the NGP comes into production.

PNR's balance sheet is debt free and offers full gold price exposure and cash flows that are highly leveraged to the gold price. This is due to its gold production being entirely unhedged (since end April 2020), making it one of just a handful of ASX gold producers with no hedge book.

This puts PNR in a strong positon to fund exploration and development at Norseman in a market that is giving good recognition for exploration success.

Buy, Target Price $0.17/sh

Regis Resources (RRL)

We continue to view RRL as an attractive, reliable gold producer. Consistent operating margins have been maintained across the business. RRL's 1HFY20 EBITDA margin of 50% is competitive with, or ahead of, key industry peers. RRL's ongoing CAPEX is in-line with our expectations and, in our view, represents investment into attractive, capital efficient growth options that leverage off RRL's existing infrastructure – an aspect of its operations that set it apart from many peers. RRL also remains one of the sector leaders for shareholder returns. Its most recent dividend equates to a payout of $40.7m and a payout ratio of 43% of NPAT. While RRL does carry a large hedge book which is out of the money, it is almost entirely spot deferred offering greater flexibility than flat forward sales. We have estimated that over 2HFY20 and FY21 it would result in a realised gold price at a 5.1% discount to a spot price of A$2,700/oz.

Buy, Target Price $5.72/sh

Senex Energy (SXY)

SXY has a strong earnings growth profile as the company builds production from its two Queensland coal seam gas projects. Roma North (1mmboe pa) is now running at design capacity and delivering to the GLNG joint venture under gas sales agreements. Atlas (2mmboe pa) is ramping up production and delivering gas to east coast industrial and utility customers. Both of these projects have expansion potential. SXY has a strong balance sheet with net debt expected to peak in the September 2020 quarter before operating cash flows support rapid deleveraging.

Buy, Target Price $0.33/sh

Peter Arden, David Coates & Stuart Howe

Westgold Resources (WGX)

Although WGX's latest quarterly production was below expectations, gold output and costs are expected to improve in 4Q20 and in the next few years, generating growing free cash flow, particularly as sub-level cave mining at Big Bell moves up to the targeted rate. Big Bell is now expected to build to targeted production by the end of 2020, providing long term, low cost feed that is expected to make it WGX's flagship mine and potentially one of the lowest cost gold mines in Australia if it can achieve its targeted operating parameters. The company has continued to have significant near mine exploration success across its three operations in the Murchison of WA, with recent high grade extensions being made at Great Fingal, Starlight and Trev's Lode. Our target price is $2.65/share and our recommendation is Buy.

HEALTHCARE & BIOTECH.

Tanushree Jain

For the healthcare and biotech sector, COVID-19 has necessitated a shift in focus this year with companies either trying to keep their base businesses on track or trying to make the most of the opportunity in developing treatments, vaccines or diagnostic tests for COVID-19. Companies with COVID-19 tailwinds or neutral impact from COVID-19 are likely to outperform:

1. COVID-19 tailwinds: The pandemic presents an opportunity for companies focused on developing treatments, vaccines or diagnostics.

2. Key COVID-19 challenges: Declines in elective or non-urgent medical procedures and patients seeking non-COVID-19 care; Delay of new trials and enrolment in ongoing trials has been paused; A slowdown in licensing and M&A activity for anything non-COVID-19 related; Review timelines for some non-urgent applications have been delayed by the FDA; Business travel and medical conferences have been impacted; Less face to face meetings with healthcare professionals impacting new product launches and new customer acquisitions. We expect with easing of restrictions all of these activities will resume in FY21, however the pace is likely to be slower than what we saw pre-COVID-19.

We continue to believe that companies that deliver solid, unequivocal data and commercial outcomes in FY21 are likely to be rewarded for their efforts in terms of stock price appreciation and will attract investors and partners/suitors.

Mesoblast (MSB) (Speculative)

Mesoblast is the leading allogeneic regenerative medicine player with one of the most diversified pipelines and several products in late stage. It has strategic licensing agreements with Tasly for China (heart) and Grunenthal for EU and LATAM (back pain). The company is heading towards a transformational 2020, with 3QCY20 expected to be the most important quarter in its history with multiple catalysts. COVID-19 has provided tailwinds with the company developing its Remestemcel-L cell therapy to treat ARDS, a lung disease in ventilator dependent COVID-19 ICU patients linked to high mortality. Initial data from compassionate use was encouraging and now the company is running a pivotal trial in US, expected to read out in 3QCY20. If positive we expect a partnering deal and launch in FY21. Remestemcel-L is also awaiting FDA approval for SR-aGvHD in children, with approval expected by 30th Sep'20 and launch soon after. Revenues from Remestemcel-L for both these indications could see MSB becoming profitable in FY21. The company is also on track to report top-line results from two key Phase 3 trials (advanced heart failure and low back pain) in 3QCY20. The recent capital raising has strengthened its balance sheet, allowing it to proceed with manufacturing scale up for the ARDS opportunity and also have a stronger position in partnering negotiations.

Genetic Signatures (GSS) (Speculative)

Genetic Signatures (GSS) is a specialist molecular diagnostics (MDx) company which is focused on developing multiplexed molecular diagnostic tests for infectious diseases (branded EasyScreen) using its proprietary platform technology, 3Base. These tests help hospitals and pathology laboratories screen for a wide variety of infectious disease pathogens (such as coronavirus) rapidly, accurately and in high volumes. COVID-19 has provided tailwinds, accelerating the company's path to market penetration and customer acquisition in international markets. The company reported record revenues for 3QFY20 driven by initial sales of its COVID-19 test kit in Australia and Europe. Formal regulatory approvals for the Kit in both these markets was received in April. All indications are that 4Q20 will be another record quarter (BPe $5m). US approval for the kit is expected shortly and will a key catalyst. In the short-term COVID-19 revenues will lead the company to profitability in FY21 and in the long term the foothold from equipment placed in EU and US for COVID-19 will fast track the adoption of its other test kits from FY22 onwards. Currently 95% of the company's revenues are from Australia and expansion into Europe and US markets represent significant growth drivers for the company.

Opthea (OPT) (Speculative)

Opthea is a Melbourne-based biopharmaceutical company focused on the development of therapies for the treatment of eye diseases. Its drug OPT-302 is targeting wet age-related macular degeneration (wet AMD) and Diabetic Macular Edema (DME), an attractive market with two standard of care (SOC) anti-VEGF-A drugs generating US$10bn+ revenue. Last year results from OPT-302's Phase 2b wet AMD trial demonstrated strong vision gain with OPT-302 combination over SOC Lucentis alone (results were statistically significant) and led to a strong re-rating of the stock. The meaningful additional efficacy offered by OPT-302 and its potential to be combined with any anti-VEGF-A agent makes the company a strong candidate for takeover or partnering. An earlier stage Phase 2A trial in DME which reported recently has extended the safety data of the drug now with the second SOC drug Eylea and provided signals that the drug has biological activity in a second indication. We continue to expect a strategic transaction in FY21 (we model a US$1.4bn deal). While the company believes the results from the DME trial warrant exploring its drug in larger trials in DME, its primary focus remains on wet AMD, where it has solid, unequivocal data. Phase 3 trials for wet AMD are on track to initiate recruitment in Dec'20.

HEALTHCARE.

John Hester

The quality of Australian Biotechnology continues to improve with numerous companies now at the commercialisation phase or in late stage clinical development.

Oncosil Medical, Avita Medical and Volpara Health Technology are three of our best. The common thread to each is outstanding management. In each case the CEO and direct reports have built careers in large pharmaceutical companies or technology and hence their market knowledge is deep. Each company's earnings are protected by significant patents, trade secrets and other forms of intellectual property protection.

Oncosil Medical (OSL) (Speculative)

Oncosil Medical is a commercial stage drug developer and is expected to commence generating revenues in 2H CY2020 at the rate of $25,000 per sale. The first indication is for the treatment of locally advanced pancreatic cancer where Oncosil (in combination with systemic chemotherapy) extended overall survival from 8.5 months to 16 months and also increased the rate of surgical resection from 7% to 24%. The safety profile of the drug is outstanding with no serious adverse events being recorded during a recent clinical trial. Product launch is expected to occur in the UK and Germany later this calendar year with 16 hospitals targeted for training in the initial roll out. The company recently raised capital to fund the launch. The European business unit will be run by Mr Nigel Lange, formerly the head of Sirtex in the same region.

Avita Medical (AVH) (Speculative)

Avita Medical is commercialising Recell for the treatment of severe burns. This Australian technology was developed by Dr. Fiona Wood and was approved by the FDA for use in the United States in 2018. The company has moved quickly to expand adoption with more than 70 specialist burns centres in the US now familiar with its use. The average selling price is US$6,500 and the product is sold via a direct sales force of approximately 20 FTE's. Avita intends to expand the indication for Recell into trauma wounds, vitiligo, chronic wounds and facial rejuvenation in the years ahead. The combined addressable market is expected to be ~US$2bn. Several of these projects are under way and in the clinic. The company will be redomiciled to the United States from 1 July 2020 and maintain a secondary listing on the ASX where its CDI's will be listed.

Volpara Health Technologies (VHT)

Volpara Health Technologies is a medical technology company focussed on the early detection of breast cancer by improving the quality of screening using artificial intelligence. The company utilises technology originating from the University of Oxford designed to provide objective data on breast tissue density – a key risk marker for breast cancer. The vast majority of the revenues are earned in the United States although the core Volpara density product is approved in more than 50 countries around the globe. The product suite is delivered via a Software as a Service (SaaS) business model to various independent or corporate mammography providers. Since the SaaS model began in 2016 the company has increased the product suite from the single breast density assessment tool to a complete suite of products covering all aspects of risk assessment and accuracy for a mammography practices.

EMERGING COMPANIES.

Damien Williamson

PointsBet (PBH) (Speculative)

Founded in Melbourne in 2015, PBH commenced operations as an Australian corporate bookmaker in February 2017. The May 2018 decision by the US Supreme Court to overturn the Professional and Amateur Sports Protection Act (PASPA) has provided the opportunity for PBH to expand its corporate bookmaking business into the US market, as individual states introduce legislation to permit both online wagering and sports betting.

To apply for a US online sports betting licence, PBH is required to partner with a licensed operator in the form of a casino or racetrack. PBH currently partnerships in 12 US states with a combined population of 94m. PBH accepted its first customer bet in New Jersey in January 2019, Iowa in August 2019 and Indiana in March 2020. PBH is currently the 4th largest online bookmaker of the 17 operating in New Jersey after reporting 5.6% share of online sports wagering turnover in the March 2020 quarter. PBH is targeting a launch in Illinois in July 2020, followed by Colorado in the December 2020 quarter, and Michigan in the March 2021 quarter.

PBH's domestic business has been a major beneficiary of the continuation of Australian racing during the lockdown period, as well as the shift to online wagering, resulting from the forced closure of TAB outlets, pokies and casinos. The trading update for the 55 days spanning 1 April – 25 May 2020 has seen PBH report Group Net Win of $18.5m split $18.2m Australia, $0.3m US, matching the entire 2Q20 Net Win of $18.0m and 3Q20 of $18.8m. On a daily basis, Group Net Win has surged to >$336k for 4Q20, versus ~200k in 2Q20 and 3Q20, and $80k in 4Q19.

We see further momentum to PBH from:

- Resumption of NRL on 28 May and AFL on 11 June
- NBA, MLB and NHL working towards a season resumption in July
- Minimal near term impact from reopening of TABs, Pokies and Casinos: given restricted access from social distancing, while some TAB customers may permanently shift betting to online bookies.
- Customer leakage from Sportsbet / BetEasy merger: Following the completion of the merger of Flutter (Sportsbet) and The Stars Group (BetEasy) on 5 May, PBH's domestic business is likely to benefit from BetEasy being absorbed into Sportsbet.

Resimac (RMC)

RMC is one of Australia's leading non-bank mortgage providers, servicing over 50,000 customers with principally funded assets under management of $11.4bn. Resimac is the pioneer of securitisation of Australian residential mortgages with its first Australian Residential Mortgage-Backed Security (RMBS) issuance dating back to 1988 under the name Fanmac. To date, RMC has issued ~$30bn across 50 domestic and international RMBS issues. RMC does not have the overhead of maintaining an extensive nationwide branch network, rather relationships with over 85% of Australia's mortgage brokers, where customer service and a quick approvals process have been key factors for RMC increasing originations.

The 1H20 Normalised Net Profit of $26.9m represented an increase of 85.5% versus the $14.5m reported in 1H19, driven by an increase in Net Interest Margin from 1.27% to 1.58%, 21% growth in its principally funded mortgage book, and cost to income ratio reducing from 57% to 42%.

With a majority of its funding consisting of domestic floating rate Residential Mortgage Backed Securities (RMBS) priced at a margin to 1 month bank bill, RMC has also benefitted from the three 25bp RBA cuts between June-October 2019, followed by a further two in March 2020. RMC profitability remains highly sensitive to movements in the net interest margin, where we estimate a 1bp improvement in the net interest margin increases RMC's FY20 net profit by ~$1.1m.

While RMC has noted ~6% of customers have requested COVID-19 hardship payment moratoriums, the company has not revised its 2H20 net profit guidance of matching the 1H20 result, given the net interest margin tailwind provided by the current 1 month bank bill of 0.09% being 0.16% lower than the RBA Cash Rate of 0.25%.

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Bell Potter Securities acted as Co-Manager to CBA PERLS XII Capital Notes (CBAPI, October 2019) and MQG's Capital Notes 2 (MBLPC, May 2020) received fees for that service.

T S Lim, authoring analyst, holds long positions in CBA, CBAPH, CBAPI, MBLPC, MQG, MQGPC, MQGPD.

Lafitani Sotiriou, authoring analyst, holds long positions in JHG, PDL, APT and 360.

Jonathan Snape owns shares in SM1 and SHV.

Bell Potter Securities acted as Lead Manager of UWL's capital raisings in August and December 2019 and received fees for those services. Bell Potter Securities and its associates have a net long position of 0.5% or more of the issued capital of UWL.

Bell Potter Securities acted as lead manager for GSS' A$35m capital raise in 4QCY19 and received fees for that service.

Bell Potter Securities acted as lead manager for MSB's A$75m capital raise in Oct'19 and A$138m capital raise in May'20 and received fees for that service.

Bell Potter acted as Lead Manager of A4N's $3.5m placement in July 2019 and received fees for that service.

Bell Potter Securities acted as Lead Manager to the $55m Placement of June 2019 and Joint Lead Manager to the $231m Entitlements Issue of June 2020 for NIC and received fees for that service.

Bell Potter Securities acted as Lead Manager for the $14m placement and underwriter for the $11.4m rights issue in December 2019 and as Lead manager for the $16m placement in May 2020 for BYE and received fees for that service.

John Hester owns 20,000 shares in Avita Medical.

Bell Potter Securities Limited acted as Lead Manager to the PBH IPO in Jun 2019 and Institutional Placement and Entitlement Offer in Oct 2019 and received fees for these services.

Bell Potter Securities acted as the Lead Manager on MAD's SEP'19 IPO and received fees for that service.

Bell Potter Securities acted as a Joint Lead Manager on CBR's Nov'19 IPO and Mar'20 Capital Raising and received fees for that service.

Exploration Risk Warning:

The stocks of resource companies without revenue streams from product sales should always be regarded as speculative in character. Since most exploration companies fit this description, the speculative designation applies to all exploration stocks. The fact that the intellectual property base of an exploration company lies in science and is generally only accessible to the layman in a limited summary form adds further to the riskiness with which investments in exploration companies ought to be regarded. Stocks with 'Speculative' designation are prone to high volatility in share price movements. Exploration and regulatory risks are inherent in exploration stocks. Exploration companies engage in exploration programs that usually have multiple phases to them where positive results at some stages are not indicative of ultimate exploration success and even after exploration success, there is often insufficient economic justification to warrant development of an extractive operation and there is still significant risk that even a development project with favourable economic parameters and forecast outcomes may fail to achieve those outcomes. Investors are advised to be cognisant of these risks before buying such a stock.

Biotechnology Risk Warning:

The stocks of biotechnology companies without strong revenue streams from product sales or ongoing service revenue should always be regarded as speculative in character. Since most biotechnology companies fit this description, the speculative designation also applies to the entire sector. The fact that the intellectual property base of a typical biotechnology company lies in science not generally regarded as accessible to the layman adds further to the riskiness with which biotechnology investments ought to be regarded. Stocks with 'Speculative' designation are prone to high volatility in share price movements. Clinical and regulatory risks are inherent in biotechnology stocks. Biotechnology developers usually seek US FDA approval for their technology which is a long and arduous three phase process to prove the safety, effectiveness and appropriate application or use of the developed drug and even after approval a drug can be the subject of an FDA investigation of subsequently discovered possible links between the drug and other diseases not previously diagnosed. Furthermore, the Australian exchange listed biotechnology sector is subject to influence by the global biotechnology sector, particularly that in the USA. Consequently, Australian exchange listed biotechnology stocks can experience sharp movements, both upwards and downwards, in both valuations and share prices, as a result of a re-rating of the sector both globally and in the USA, in particular. Investors are advised to be cognisant of these risks before buying such a stock.

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