



Market Watch

July 2017

4 July 2017

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Editor's Note

According to metal Bulletin, the price for benchmark iron ore (62% Fe, CFR China) hit just shy of US\$65/t on 30 June 2017, up 21.8% from a mid-June low of US\$53.36/t. With a bull market defined as a gain of +20%, iron ore is – out of nowhere – in a bull market! This leads us to thinking if this represents the “starting gun” for investors to get back into commodities.

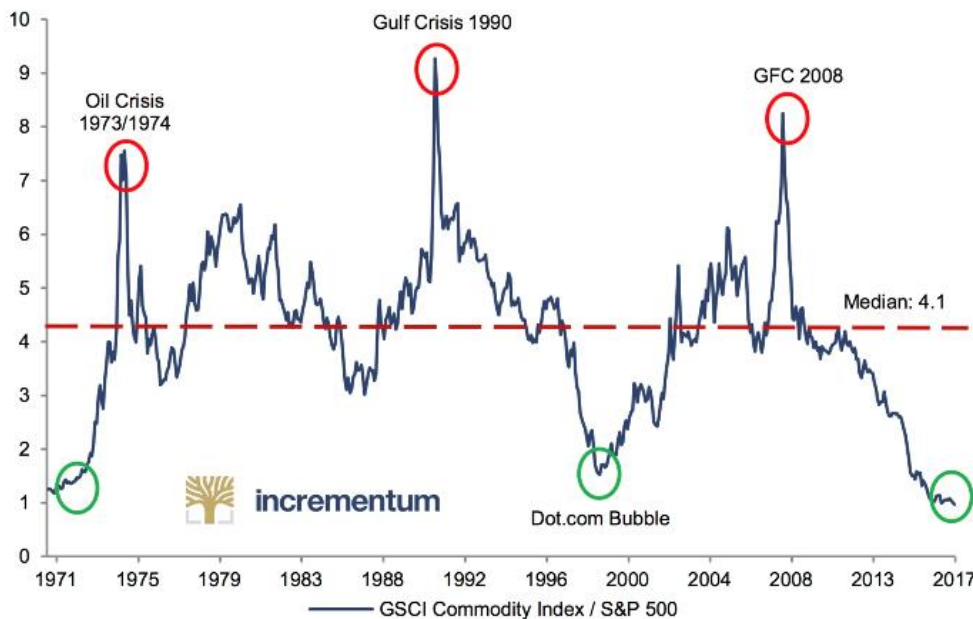
At first sight, the relative valuation of commodities to equities does seem extremely low. In relation to the S&P500, the GSCI Commodity Index is currently trading at its lowest level in fifty years. Also, the ratio is significantly below the long-term median of 4.1 (see chart below). However, we are not convinced that the ratio indicates that commodity prices (bulk, base metal, energy, precious metals) are cheap relative to equities. Rather, we believe that this ratio - along with elevated PER multiples – is evidence that equities (certainly in the US) are in over-valuation territory.

After nine years of unconventional quantitative easing (QE) policy, the Federal Reserve is now setting out a new path for quantitative tightening (QT). It is hard to believe that the unwinding of long-standing policies, which had the express purpose of inflating asset prices, will not negatively impact (contract) equity markets. Nevertheless, we note press reports quoting policymakers stating that the transition will be so gradual that it need not be disruptive; Philadelphia Fed President Harker even described the process as being “as boring as watching paint dry”. We shall see!



Alan Hill
Executive Chairman, State One Stockbroking

GSCI/S&P500 ratio: equities expensive, commodities cheap?



Source: Incrementum

Stock Picks

HT&E Limited (offers growth at reasonable price)

Westpac Banking (offers attractive dividend yield after bank sector sell-off)

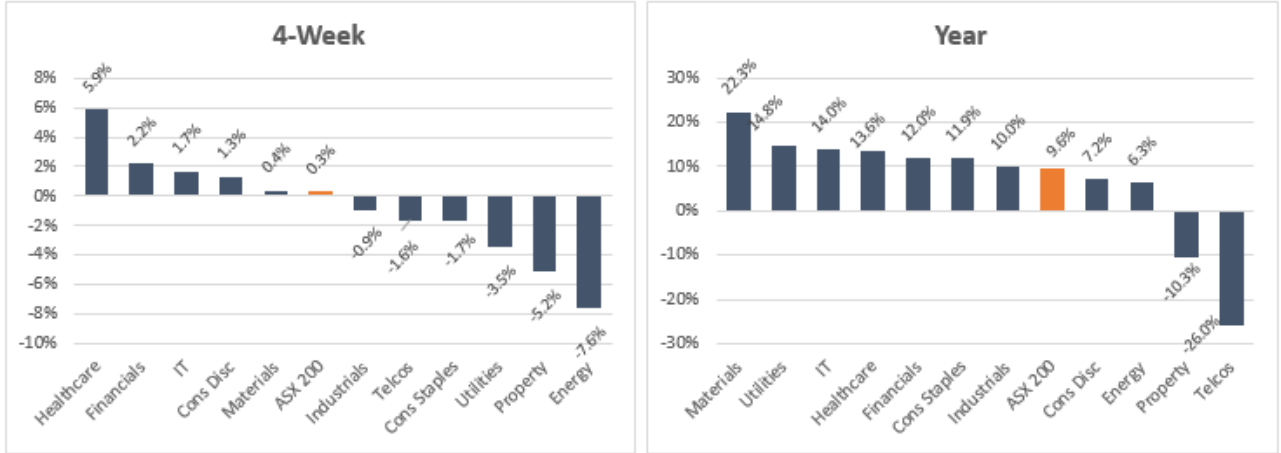
Resolute Mining (best value in ASX large cap gold space)

Buddy Platform (IoT monitoring system could be a game changer)

PepinNini Minerals (fully-funded lithium explorer in Argentina, drill results soon)

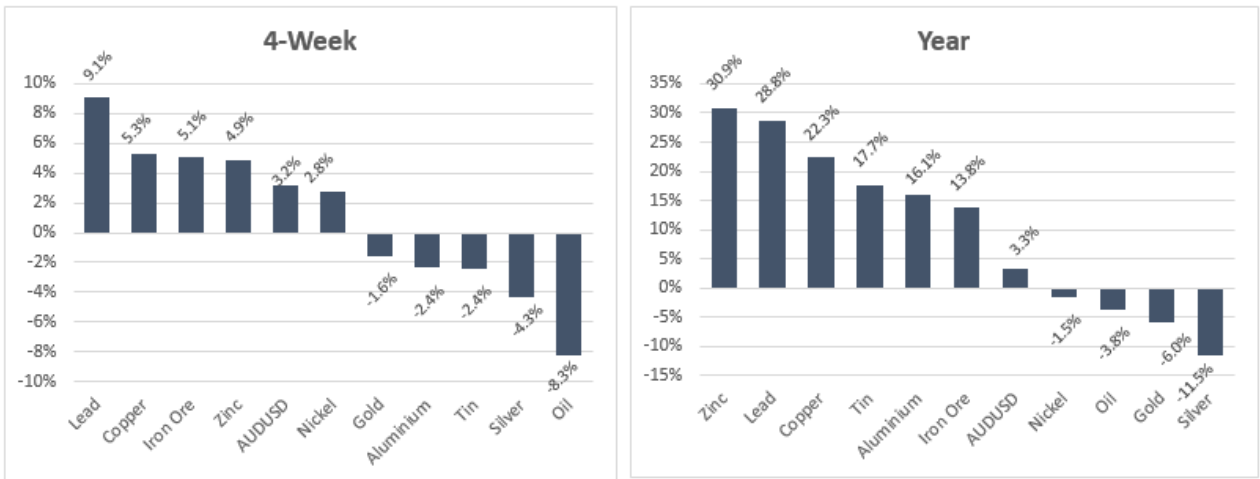
Locality Planning Energy (fully funded to triple electricity sales by mid-2020)

ASX 200: sector performance over past four weeks and year



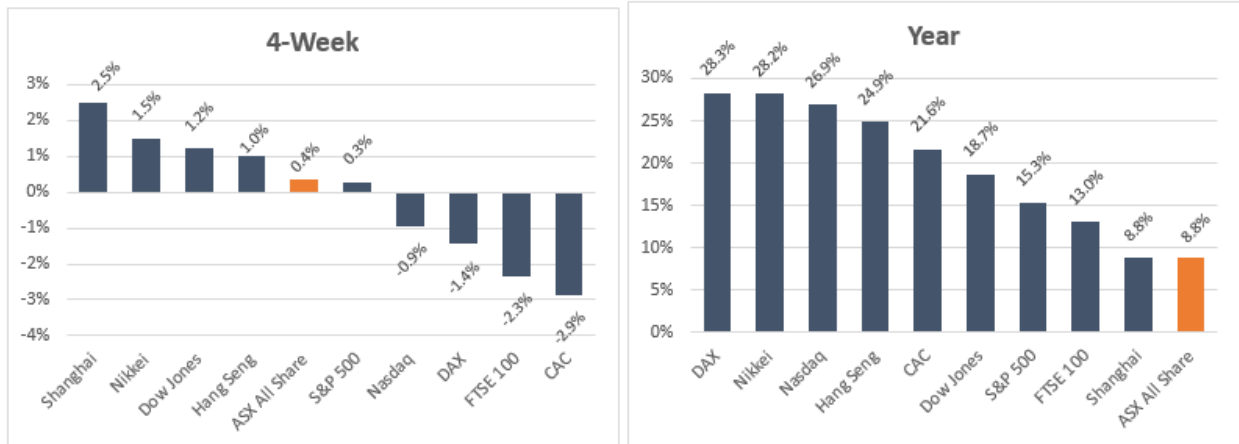
Source: IRESS, compiled by State One Stockbroking

Commodities and AUDUSD: performance over past four weeks and year



Source: IRESS, compiled by State One Stockbroking

World Indices: performance over past four weeks and year (local currency)

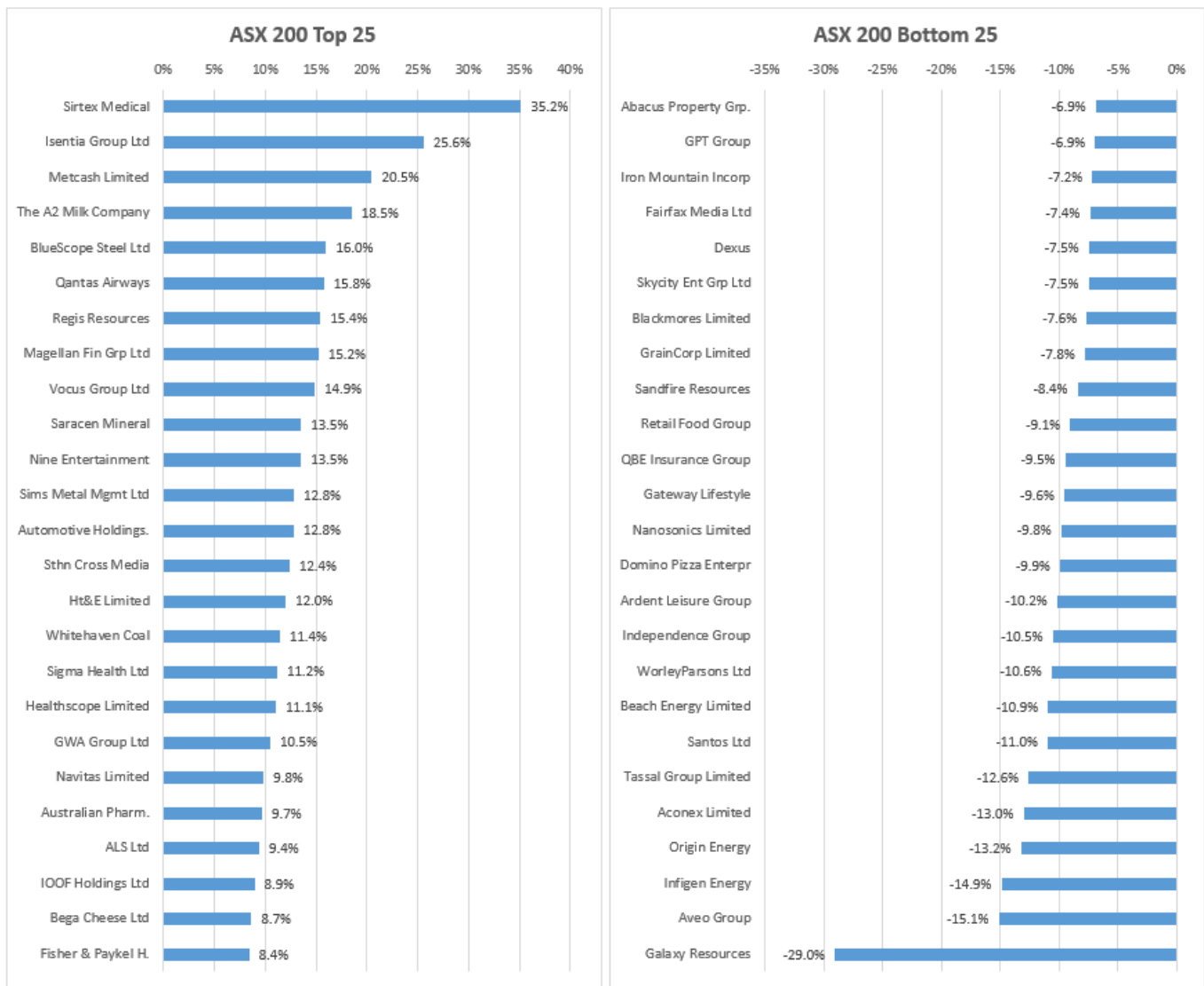


Source: IRESS, compiled by State One Stockbroking

Commentary

- The FTSE/ASX 200 Index posted a lackluster 0.3% gain in June; the standout sector was Healthcare (+5.9%), with Energy (-7.6%) and Property (-5.2%) coming under pressure from weaker prices and mounting concern over the domestic property valuations.
- Oil fell 8.3% in June on the back of healthy US production; iron ore gained 5.1% - although the steel raw material is still down 18% YTD. Base metals posting +ve gains with lead (Pb) up an impressive 9.1%.

ASX 200: top 25 and bottom 25 performing stocks over the past four weeks (% gain/loss)



Source: IRESS, compiled by State One Stockbroking

- **Top performer:** Sirtex Medical (ASX: SRX) +35% as the group rebases business with impairments of intangible assets, and implements cost cutting initiatives including a 15% staff reduction.
- **Worst performer:** Galaxy Resources (ASX: GXY) -29% following a broad sell-off of the lithium miners and despite positive production and shipment updates from the group's Mt Cattlin operations.

Month in review - events that caught our eye in June 2017



Trump pulls the US out of the Paris Climate Accord. German Chancellor Angela Merkel says "we can't wait for the last man on Earth to be convinced by climate change".



Eight people killed and dozens injured during a car and knife Islamist terrorist attack at London Bridge and Borough Market.



UK Prime Minister's decision to hold a snap election to boost the Conservative Party's standing ahead of critical Brexit talks backfires as she ends up with 12 fewer seats. The surprise gainer is the Labour Party.



Several Gulf countries including Saudi Arabia snap diplomatic and economic ties with Qatar. Issues include Qatar's alleged support of the Muslim; 12-point list includes demand that Qatar shuts the Al-Jazeera news service.



Ten Network (ASX:TEN) placed into voluntary administration after billionaire shareholders Bruce Gordon and Lachlan Murdoch pulled their support as guarantors for a key \$200m loan.



Global liquor giant Diageo to pay up to US\$1 billion to buy the tequila brand "Casamigos", co-founded by movie star George Clooney only four years ago.



South Australia takes a lead from the Federal Government and imposes a separate bank levy on the "Big 4" banks plus Macquarie. The new state levy is expected to raise some \$370m over 4 years (vs \$6.2bn federal bank levy).



Rio Tinto shareholders overwhelmingly back Yancoal's US\$2.69bn offer for its Coal & Allied coal operations in the Hunter Valley (NSW) over Glencore's marginally lower US\$2.68bn bid.



Hedge fund Anchorage Capital Group to gain control of debt-stricken law firm Slater & Gordon (ASX:SGH) in a deal that sees a complete clean-out of the board including long-serving CEO Andrew Grech.



State One Stock Picks

HT&E Limited (HT1)

Sector: Media

Market Cap: A\$791m

Share price: A\$2.56

IRESS target price: A\$3.22

Recommendation: Buy

26% upside to IRESS consensus target price plus 3.5% dividend yield = 30% total return.

We believe recent weakness in the share price could be due to market disappointment on confirmation that - contrary to media speculation - HT1 is not buying QMS Media. Trading on a FY17E PER of 11.2x (on IRESS consensus EPS of A\$0.22), and with 10% EPS growth forecast to FY18E, we believe APN is a standout GARP stock (Growth At Reasonable Price).

Westpac Banking (WBC)

Sector: Financials

Market Cap: A\$102.3bn

Share price: A\$30.48

IRESS target price: A\$33.61

Recommendation: Buy

10% upside to IRESS consensus target price plus 6% dividend yield = 16% total return.

Banks have been sold off in May on the back of renewed concern over the domestic housing sector and a controversial government levy on liabilities. However, we suggest that banks are now at a more attractive entry point. For investors looking for exposure the "Big 4" banking sector, WBC offers an attractive 6% dividend yield and a total return at 18%.

Resolute Mining (RSG)

Sector: Materials/Gold

Market Cap: A\$877m

Share price: A\$1.18

IRESS target price: A\$1.75

Recommendation: Buy

48% upside to IRESS consensus target price.

After Saracen Minerals' (SAR) strong run in May/June, our preferred play in the large-cap gold space is now 325koz Au producer Resolute Mining (RSG). First ore production at the u/g section at the Syama Mine (Mali) is planned for 2H CY18, while the recently announced Nafolo discovery, adjacent to Syama bodes well for brownfields development. We note Macquarie recently initiated coverage on the stock with a target price of A\$1.80ps.

Buddy Platform (BUD)

Sector: Software & Services

Market Cap: A\$29m (quoted)

Share price: A\$0.094

State One target price: A\$0.21

Recommendation: Spec Buy

Feedback during June quarter pre-sale customer tours in Australia and the US indicate that there is strong appetite for Buddy Ohn - BUD's recently developed real-time electricity, gas, and water consumption monitoring system. The product could be a game changer for the IoT company with potential for significant share price gains as visibility improves on the +ve near-term impact of Buddy Ohn on the group's revenue and profit lines.

PepinNini (PNN)

Sector: Materials / Lithium

Market Cap: A\$7.3m

Share price: A\$0.017

State One target price: N/A

Recommendation: Spec Buy

PNN announced on 30 May that maiden diamond drilling at its Pocitos tenements was delayed by 2-3 weeks as a result of adverse climatic conditions (heavy snow). The share price fell significantly in response. We believe the share was oversold. First sample results (assays) are now expected in late June/early July. Positive results here could act as a significant share price catalyst. Based on peer group EV/t valuations, we value our estimated Maiden Resource at Pocitos of some 1.45Mt of Lithium Carbonate Equivalent (LCE) at US\$45m (A\$60m).

Locality Planning Energy (LPE)

Sector: Utilities

Market Cap: A\$32m

Share price: A\$0.027

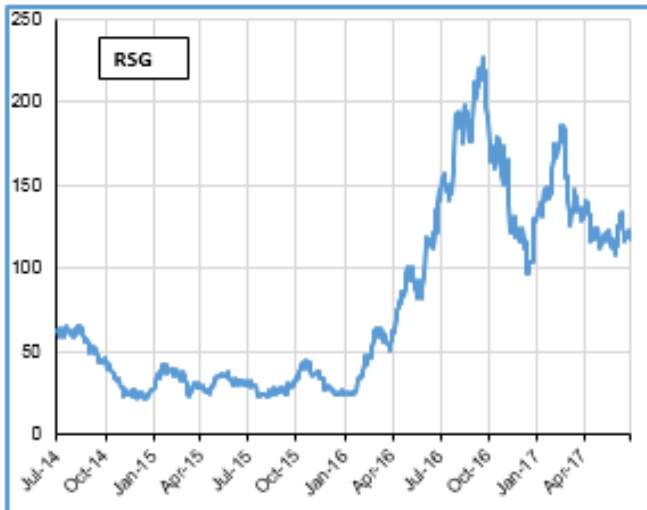
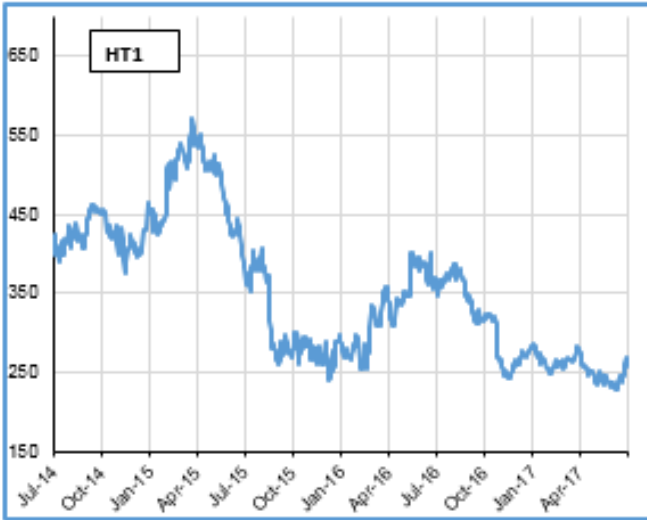
State One target price: A\$0.041

Recommendation: Spec Buy

Recently secured debt facilities with NSW-based Moneytech Finance, has significantly de-risked the group's exciting growth plans; the Queensland-based electricity retailer is targeting to increase billable electricity sales from a current level of ~100GWh to 450GWh by mid-2020. At current sales levels we believe LPE is operationally cash flow neutral.



State One stock picks: share price history (A\$cps)



Source: IRESS, compiled by State One Stockbroking

ASX 200 – Materials Sector Ranking by Total Return

Target Price and FY18E Dividend Yield as per IRESS consensus, share price as at close
 30 June 2017, compiled by State One Stockbroking.

Security	Name	Share Price (A\$)	Target Price (A\$)	Capital upside / (downside) (%)	FY18E DY (%)	Total Return (%)
GXY	Galaxy Resources	1.67	2.91	74.3%	0.0%	74.3%
SYR	Syrah Resources	2.78	4.72	69.8%	0.4%	70.1%
RSG	Resolute Mining	1.21	1.75	44.6%	1.7%	46.3%
ORE	Orocobre Limited	3.46	4.29	24.0%	0.0%	24.0%
SFR	Sandfire Resources	5.66	6.67	17.8%	3.4%	21.2%
IGO	Independence Group	3.15	3.71	17.8%	2.5%	20.3%
OZL	OZ Minerals	7.34	8.38	14.2%	2.0%	16.2%
BHP	BHP Billiton Limited	23.3	26.12	12.1%	3.2%	15.3%
IPL	Incitec Pivot	3.39	3.73	10.0%	3.8%	13.9%
S32	South32 Limited	2.70	2.95	9.3%	4.4%	13.7%
WSA	Western Areas Ltd	2.08	2.32	11.5%	1.0%	12.5%
PGH	Pact Group Hldgs Ltd	6.00	6.47	7.8%	4.5%	12.3%
RIO	Rio Tinto Limited	63.26	68.46	8.2%	3.4%	11.6%
ORA	Orora Limited	2.86	3.08	7.7%	3.8%	11.5%
BKW	Brickworks Limited	13.85	14.89	7.5%	3.9%	11.4%
MIN	Mineral Resources.	10.85	11.45	5.5%	5.4%	11.0%
FMG	Fortescue Metals Grp	5.12	5.45	6.4%	3.1%	9.6%
NCM	Newcrest Mining	20.35	21.74	6.8%	1.4%	8.3%
EVN	Evolution Mining Ltd	2.43	2.59	6.6%	1.6%	8.2%
SBM	St Barbara Limited	2.92	2.95	1.0%	5.5%	6.5%
SAR	Saracen Mineral	1.17	1.22	4.3%	0.9%	5.1%
CSR	CSR Limited	4.23	4.2	-0.7%	5.0%	4.3%
BLD	Boral Limited	6.97	6.87	-1.4%	3.7%	2.3%
FBU	Fletcher Building	7.6	7.33	-3.6%	5.3%	1.7%
JHX	James Hardie Indust	20.42	20.18	-1.2%	2.4%	1.3%
AWC	Alumina Limited	1.91	1.79	-6.3%	7.3%	1.0%
AMC	Amcor Limited	16.28	15.91	-2.3%	2.9%	0.7%
ABC	Adelaide Brighton	5.59	5.31	-5.0%	4.7%	-0.4%
BSL	BlueScope Steel Ltd	13.16	12.92	-1.8%	1.3%	-0.5%
DLX	Duluxgroup Limited	6.98	6.66	-4.6%	3.7%	-0.9%
NST	Northern Star	4.74	4.58	-3.4%	2.3%	-1.1%
NUF	Nufarm Limited	9.63	9.36	-2.8%	1.7%	-1.1%
ILU	Iluka Resources	8.62	8.28	-3.9%	2.0%	-2.0%
RRL	Regis Resources	3.82	3.30	-13.6%	4.2%	-9.4%
SGM	Sims Metal Mgmt Ltd	14.98	12.76	-14.8%	2.7%	-12.1%
ORI	Orica Limited	20.65	17.16	-16.9%	2.9%	-14.0%



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