



# Market Watch

## December 2017

1 December 2017

[marketwatch@amscot.com.au](mailto:marketwatch@amscot.com.au)

### Editor's Note

On 6 November 2017, the benchmark ASX 200 Index hit 6,000 for the first time since January 2008, as investors piled into energy and mining stocks. Resource sector stocks found favour on the back of big upward moves in the underlying commodity prices. While gains in individual commodity price are being driven by specific factors i.e., Lithium and Cobalt -> electric vehicle (EV) growth, Zinc -> supply constraints, Oil -> OPEC production cuts, commodity prices as a whole are also moving higher against a broad backdrop of an improving global economic outlook. Infrastructure continues to be an important driver of commodity demand in China, while the rest of the developed world (US, Europe) is enjoying a rare moment of synchronized economic growth. In addition, sector heavyweights like Rio Tinto and BHP being rewarded for cutting costs and returning cash to shareholders. Perhaps the fears of “waves of supply” a few years ago – particularly relating to iron ore – have forced companies to rethink the strategy of building up new capacity every time prices rise. So far in this upward leg of the commodity price cycle, the supply response has been muted.

However, after running strongly, it looks like the larger mining stocks (excluding gold) are fully valued. We calculate that the 14 largest non-gold mining stocks offer an average total return of only 2% (2.6% dividend yield, -0.6% capital return). **At this juncture, iron ore play Fortescue Metals (FMG) offers the highest total return (c27%) as calculated from its IRESS consensus target price and FY18E dividend yield. Nickel play Western Areas (WSA) and lithium play Orocobre (ORE) appear full valued, offering negative total returns of ~16%. See table below.**

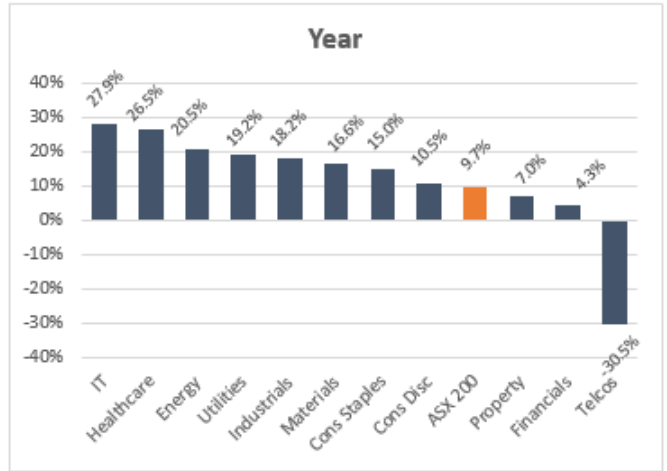
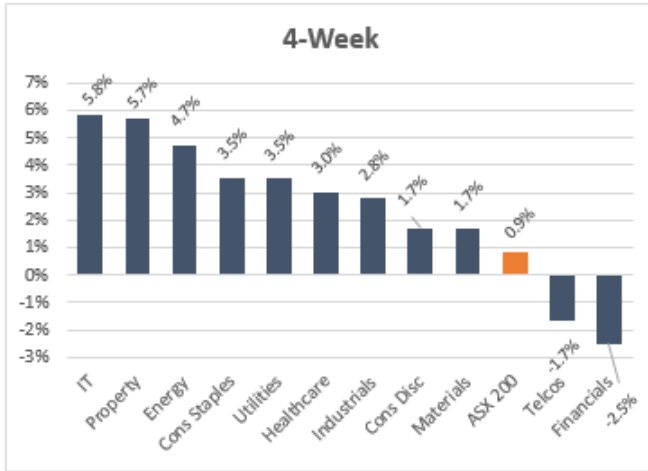
### Forecast total return for ASX 200 Mining stocks (excluding gold)

Security	Name	Share Price (A\$)	Target Price (A\$)	Capital upside / (downside) (%)	FY18E Dividend (A\$)	FY18E DY (%)	Total Return (%)
FMG	Fortescue Metals	4.56	5.55	21.7%	0.26	5.7%	27.4%
AWC	Alumina Limited	2.21	2.25	1.8%	0.17	7.7%	9.5%
SFR	Sandfire Resources	6.28	6.66	6.1%	0.21	3.3%	9.4%
SYR	Syrah Resources	4.08	4.46	9.3%	0.00	0.0%	9.3%
RIO	Rio Tinto Limited	70.95	74.7	5.3%	2.42	3.4%	8.7%
BHP	BHP Billiton Limited	27.5	28.69	4.3%	0.85	3.1%	7.4%
ILU	Iluka Resources	9.27	9.71	4.7%	0.14	1.5%	6.3%
OZL	OZ Minerals	8.38	8.62	2.9%	0.14	1.7%	4.5%
S32	South32 Limited	3.23	3.08	-4.6%	0.13	4.0%	-0.6%
GXY	Galaxy Resources	3.82	3.79	-0.8%	0.00	0.0%	-0.8%
IGO	Independence Group	4.23	3.75	-11.3%	0.06	1.4%	-9.9%
MIN	Mineral Resources.	19.62	16.83	-14.2%	0.63	3.2%	-11.0%
ORE	Orocobre Limited	6.38	5.38	-15.7%	0.00	0.0%	-15.7%
WSA	Western Areas Ltd	3.08	2.55	-17.2%	0.03	1.0%	-16.2%

Source: IRESS, compiled by State One Stockbroking

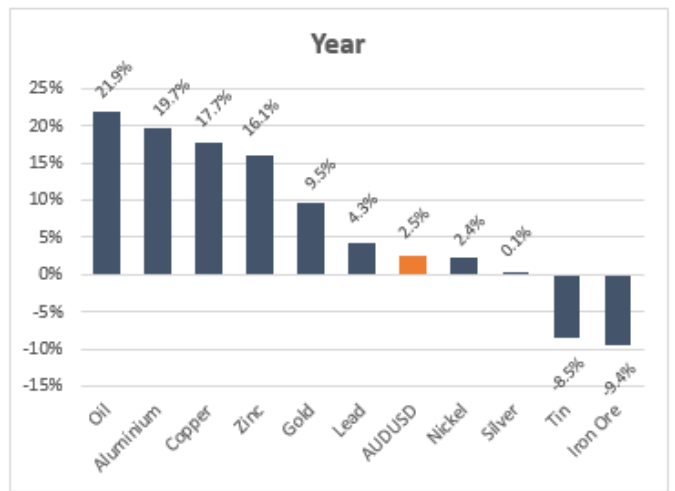
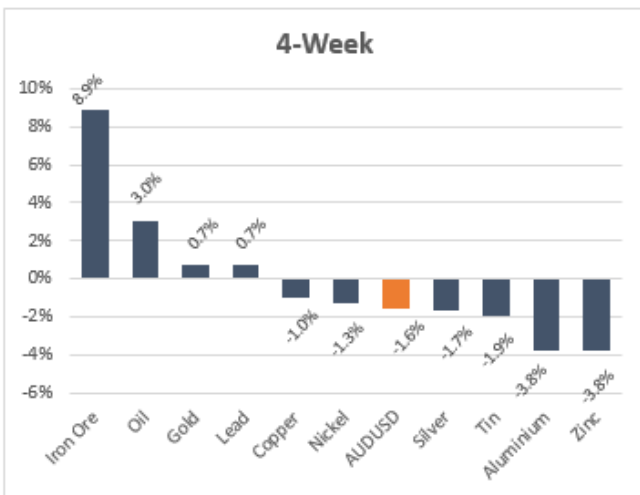
Note: Share prices, target prices and dividend yield as at 1 December 2017

### ASX 200: sector performance over past four weeks and year



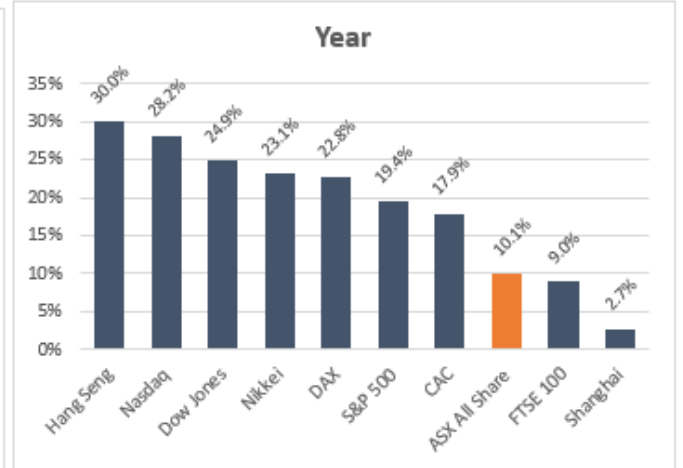
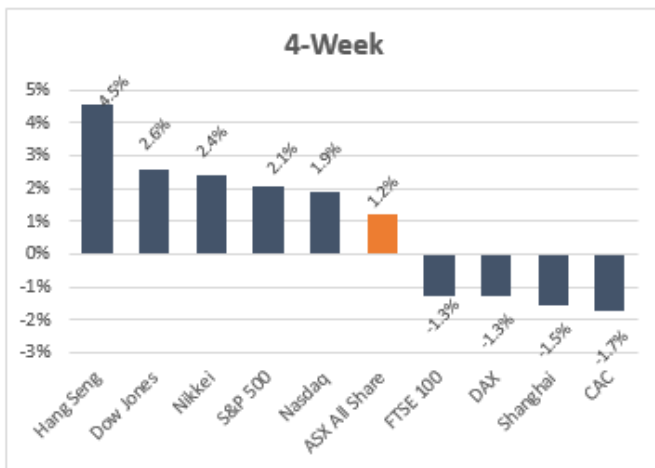
Source: IRESS, compiled by State One Stockbroking

### 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)

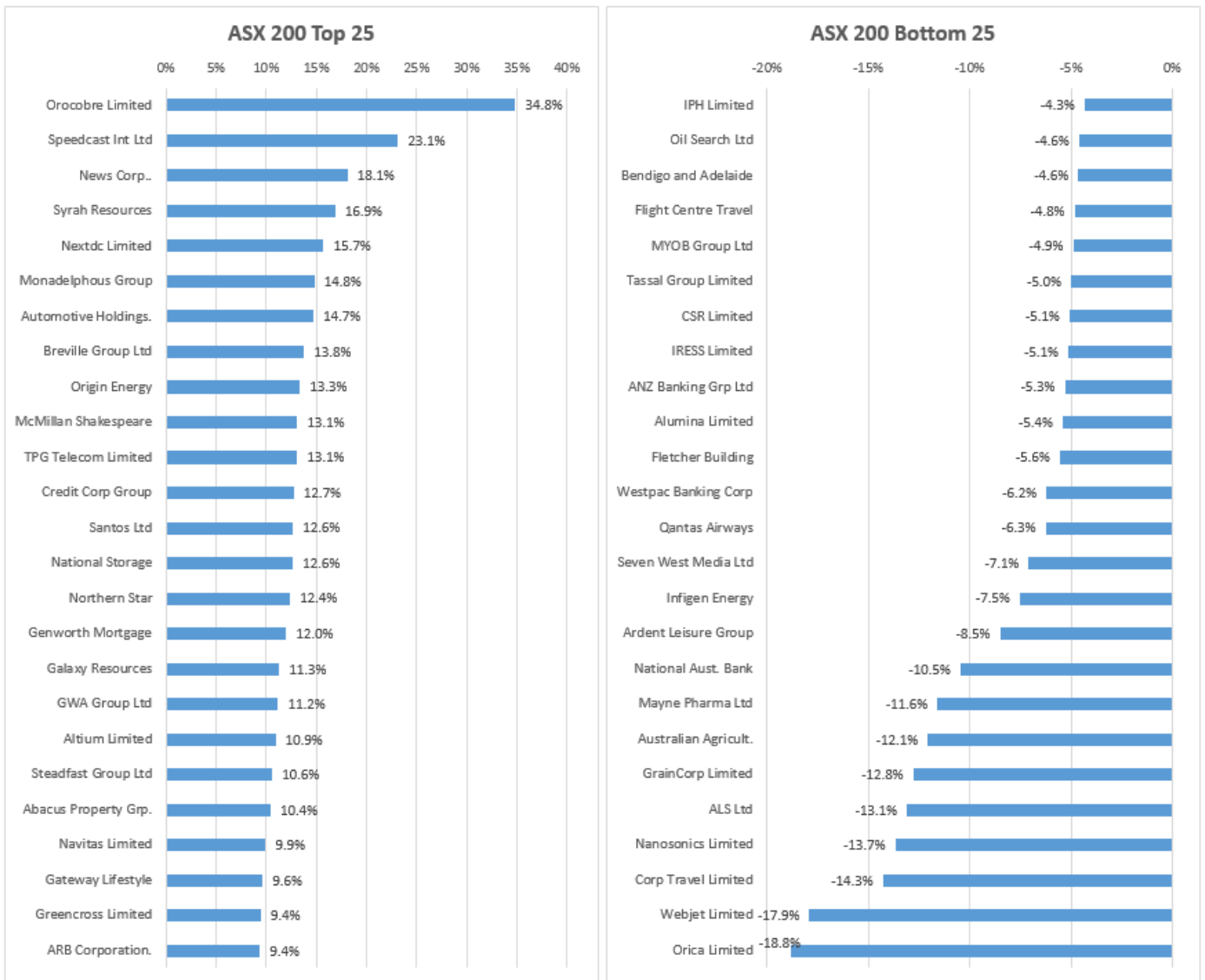


Source: IRESS, compiled by State One Stockbroking

## Commentary

- The FTSE/ASX 200 Index gained +0.9% in November with impressive gains in the IT and Property sectors of +5.8% and +5.7% respectively. Offsetting these gains were losses in two heavyweight sectors - Financials and Telcos - of -2.5% and -1.7%.
- Iron ore was the standout performer in November, with a gain of 8.9%. Over the past 12 months however, iron ore is still down 9.4%. All other commodities performed somewhat lackluster in November (although still up strongly over the year).

### 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:** Orocobre Limited (ASX: ORE) +35% on the back of increased interest in the lithium sector as demand forecasts for electric vehicles are revised up.
- **Worst performer:** Orica Limited (ASX: ORI) fell 19% on the back of an outlook statement indicating that demand conditions in the mining sector could get worse before improving.

## Month in review - events that caught our eye in November



ACCC flags write-down of A\$50bn at NBN in order to allow the beleaguered telecom provider to charge lower prices and offer relief on debt repayments



Saudi Arabia's Crown Prince Mohammed bin Salman arrests 11 senior princes in a series of changes that look to modernise the oil-rich state.



The benchmark ASX 200 Index hits 6,000 on 6 Nov 2017 for the first time since January 2008, on the eve of the GFC, some 10 years ago.



End of an era as Royal Dutch Shell sells its remaining \$3.5bn interest in Woodside Petroleum. Shell had its bid for control of Woodside blocked by the Howard government in 2001.



93-year old Robert Mugabe steps down as President of Zimbabwe after 37 years of rule following an effective military coup.



Australia votes "yes" to support changing the law to allow same-sex couples to marry with 62% responding yes to the SSM postal survey.



Tesla unveils an electric truck capable of travelling 804km with a full 36t load. Customers can put down a US\$5,000 deposit with production beginning in 2019.



Fortescue Metals Group appoints two women to lead the miner – Elizabeth Gaines as CEO and Julie Shuttleworth as deputy CEO. Moves come among a major change in leadership at the group and includes a new COO and CFO.



Government backs down on opposition to Royal Commission into the financial services sector after receiving an email from the heads of the "Big 4" banks that the bank probe should go ahead.

### Do you really know Hybrids?

Hybrids securities are a way for banks and companies to borrow money from investors while paying interest in return. They offer a blend of features of both debt and equities (shares). They are like equities, taking on equity risk but receiving returns like bonds. Some hybrids take on terms and conditions that allow the issuer to exit the deal or suspend the interest payments when they decide. Hybrids may come in forms of very long-term investments and may not show suitability to investors who need to receive a constant return and capital protection.



There are 3 types of hybrids:

1. Convertibles
2. Preference shares
3. Capital notes

*Convertibles* are a debt security that gives either the investor or the issuer the option to convert it into another type of security at a specified date in the future.

*Preference shares* carry a specified dividend rate unlike ordinary shares which pay a variable rate that is decided by the directors of the firm.

*Capital notes debts* are equity-like in features. There is the perpetual debt that has no fixed maturity date. Subordinated debt securities have a ranking in relation to payment of interest and repayment of principal, ranked behind another class or classes of debt. Knock-out debt securities are debt securities that give the issuer or by a third party the right to extinguish the debt securities under certain conditions. The debt securities have a risk weighting or maybe treated as capital, by prudential regulators.

New hybrids are constantly being introduced to meet the needs and requirements of sophisticated investors. Some of these securities are complicated and difficult to define if it is a debt or an equity. Besides it being difficult to understand, another point to note is that some hybrid securities require the investors to take more risk than the potential return would require.



Dawn Chia  
Business Development Manager  
amscot Stockbroking and Advisor Services

## Warnings and Disclosures

These Research products and their contents at all times remain the property of State One Stockbroking Ltd ("State One") and as such cannot be reprinted, distributed, copied, posted on the internet, in part or whole, without written prior approval from State One. The contents of this document constitute General Advice and have been prepared without taking account of your investment objectives, financial situation or needs. Because of that you should, before taking any action to acquire or deal in, or follow a recommendation (if any) in respect of any of the financial products or information mentioned in these documents, consult your own investment advisor to consider whether that is appropriate having regard to your own objectives, financial situation and needs. While State One believes information contained in these documents are based on information which is believed to be reliable, their accuracy and completeness are not guaranteed and no warranty of accuracy or reliability is given or implied and no responsibility for any loss or damage arising in any way for any representation, act or omission is accepted by State One or any officer, agent or employee of State One. If applicable, you should obtain the Product Disclosure Statement relating to any relevant financial product mentioned in this document (which contains full details of the terms and conditions of the relevant financial product) and consider it before making any decision about whether to acquire the financial product. The directors and associated persons of State One may have a long or short interest in the financial products discussed in these documents and they may earn brokerage, commissions, fees and advantages, pecuniary or otherwise, in connection with the making of a recommendation or dealing by a client in such financial products. Additionally, State One may earn fees due to having been appointed advisors to, or may be undertaking or about to commence research relating to any of the companies mentioned here.

Alan Hill  
Executive Chairman  
Phone: +61 8 9288 3388  
[ahill@stateone.com.au](mailto:ahill@stateone.com.au)

Ric Heydon  
Equities & Derivatives Advisor  
Phone: +61 8 9288 3307  
[rheydon@stateone.com.au](mailto:rheydon@stateone.com.au)

Mark Sullivan  
Institutional Dealer  
Phone: +61 2 9024 9134  
[msullivan@stateone.com.au](mailto:msullivan@stateone.com.au)

Thomas Tan  
Equities Advisor  
Phone: +61 2 9024 9131  
[ttan@stateone.com.au](mailto:ttan@stateone.com.au)

Morris Levitzke  
Equities Advisor  
Phone: +61 8 9288 3315  
[mlevitzke@stateone.com.au](mailto:mlevitzke@stateone.com.au)

Graeme Johnson  
Equities & Derivatives Advisor  
Phone: +61 8 9288 3316  
[gjohnson@stateone.com.au](mailto:gjohnson@stateone.com.au)

Yitz Barber  
Equities Advisor  
Phone: +61 2 9024 9107  
[ybarber@stateone.com.au](mailto:ybarber@stateone.com.au)

Tammie Wong  
Equities Advisor  
Phone: +61 2 9024 9133  
[twong@stateone.com.au](mailto:twong@stateone.com.au)

Dawn Chia  
Business Development Manager  
Phone: +61 8 9288 3336  
[Dawn.Chia@stateone.com.au](mailto:Dawn.Chia@stateone.com.au)

David Zhang  
Equities Advisor  
Phone: +61 2 9024 9130  
[dzhang@stateone.com.au](mailto:dzhang@stateone.com.au)

David Brennan  
Senior Investment Analyst  
Phone: +61 2 9024 9142  
[dbrennan@stateone.com.au](mailto:dbrennan@stateone.com.au)