FINANCIAL REVIEW smartinvestor

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HD **Strong fundamentals**

BY TREVOR HOEY - Trevor Hoey uses socio-economic trends to identify stocks with the best potential for growth.

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HOEY'S TOP TEN

TD

Mayne Pharma Group
ASX CODE: MYX

	2012	2013
Rev	$55.4m	$83.7m
Profit	$6.2m	$2.8m
EPS	4.0¢	0.7¢
Div	N/A	N/A
52wk▲	$0.84	
52wk▼	$0.31	
Yield	N/A	
Mkt cap	$417.0m	
P/Eratio	N/A	

RCG Corporation
ASX CODE: RCG

	2012	2013
Rev	$51.3m	$50.7m
Profit	$9.2m	$5.8m
EPS	3.8¢	2.4¢
Div	3.0¢	4.0¢
52wk▲	$0.85	
52wk▼	$0.44	
Yield	5.37%	
Mkt cap	$195.4m	
P/Eratio	30.9	

Select Harvests
ASX CODE: SHV

	2012	2013
Rev	$253.6m	$220.3m
Profit	$4.5m	$2.9m
EPS	7.9¢	5.0¢
Div	8.0¢	12.0¢
52wk▲	$5.59	
52wk▼	$1.35	
Yield	2.18%	
Mkt cap	$318.0m	
P/Eratio	110	

UXC
ASX CODE: UXC
 2012 2013
Rev $560.7m $597.7m
Profit $19.7m $24.0m
EPS 6.4¢ 7.8¢
Div 3.5¢ 5.3¢
52wk▲ $1.28
52wk▼ $0.89
Yield 5.3%
Mkt cap $320.6m
P/Eratio 12.8

Collins Foods
ASX CODE: CKF
 2012 2013
Rev $417.0m $424.7m
Profit $11.4m $16.4m
EPS 14.4¢ 16.2¢
Div 6.5¢ 10.0¢
52wk▲ $1.92
52wk▼ $1.30
Yield 5.46%
Mkt cap $170.2m
P/Eratio 11.3

Royal Wolf Holdings
ASX CODE: RWH
 2012 2013
Rev $138.0m $150.3m
Profit $11.6m $14.7m
EPS 11.6¢ 14.7¢
Div 8.0¢ 9.5¢
52wk▲ $3.82
52wk▼ $2.49
Yield 2.88%
Mkt cap $331.3m
P/Eratio 22.4

KGL Resources
ASX CODE: KGL
 2011 2012
Rev N/A $0.4m
Profit $6.5m $4.0m
EPS 1.2¢ 3.6¢
Div N/A N/A
52wk▲ $0.41
52wk▼ $0.05
Yield N/A
Mkt cap $14.7m
P/Eratio N/A

Aust'n Pharmaceutical Industries
ASX CODE: API
 2012 2013
Rev $3.2bn $3.2bn
Profit $30.3m $24.3m
EPS 6.2¢ 5.0¢
Div 3.0¢ 3.3¢
52wk▲ $0.67
52wk▼ $0.36
Yield 5.42%
Mkt cap $292.9m
P/Eratio 12

PanAust

ASX CODE: PNA
 2011 2012
Rev $565.8m $587.4m
Profit $157.5m $144.3m
EPS 4.8¢ 22.1¢
Div N/A N/A
52wk▲ $3.51
52wk▼ $1.45
Yield 3.88%
Mkt cap $1.1bn
P/Eratio 9.4

WDS
ASX CODE: WDS
 2012 2013
Rev $351.1m $351.7m
Profit $8.5m $8.2m
EPS 5.9¢ 5.7¢
Div 2.8¢ 5.8¢
52wk▲ $0.94
52wk▼ $0.33
Yield 6.73%
Mkt cap $123.8m
P/Eratio 15
Positive drivers for growth are having an impact on companies from sectors as varied as pharmaceuticals, mining and cloud solutions, writes Trevor Hoey.

1 Mayne Pharma Group

Analysts at Moelis responded swiftly to the company's AGM trading update, increasing earnings per share for 2013-14, 2014-15 and 2015-16 by 8 per cent, 6 per cent and 5 per cent respectively. Not only did Mayne Pharma Group have a better financial result to reflect on, but its outlook had changed markedly.

However, the landscape changed towards the end of 2012 and into 2013 with the acquisition of Metrics and Kapanol. The latter included the trademark, marketing authorisations, technical data and product inventory. This gave Mayne Pharma access to an oral opioid to relieve chronic moderate to severe pain.

Kapanol represents about 6 per cent of the $90 million market in that sphere, but this is growing at an annual rate of about 5 per cent, driven by fundamentals such as an ageing population, increasing incidence of cancer and increased use in non-malignant chronic pain. In a sense it was back to the future for Mayne Pharma as it developed the drug in the 1990s with Glaxo SmithKline, which was the vendor.

The Metrics acquisition, however, was the real game changer, as the company's market capitalisation has increased more than sixfold since its purchase. It gave Mayne Pharma access to the US pharmaceutical market, with a value of $US50 billion.

Management said a key growth driver of its business will be maximising its US retail generics portfolio. Demand for generics is expected to rise in the US because of the ageing population, increasing life expectancy and a steady pipeline of branded products going off-patent.

In July and August Mayne Pharma released three of its own products that are manufactured in Australia for distribution in the US.

Moelis highlighted that 10 generic products now filed with the US FDA have potential end markets totalling $US800 million.

There was also good news from a financial perspective, with management indicating group sales of $45 million for the first four months of 2013-14. This translates into annualised revenue of $135 million, broadly in line with Moelis's forecasts of $136.3 million.

Si view: While Mayne's shares have had a strong run, there are potential share price catalysts in the way of drug development, particularly in the generics base,as well as news about TGA/FDA approvals of products filed for registration.

2 RCG Corporation

Shares in RCG Corporation responded well to news it had acquired both the Saucony wholesale and distribution businesses in Australia and New Zealand and the Podium Sports retail business from Authentics Australia. RCG already has a strong relationship with global footwear manufacturer and distributor Wolverine Worldwide, and in tandem with this transaction has secured a new five-year exclusive Saucony distribution licence.

RCG's managing director Hilton Brett said the acquired businesses would have an annualised positive impact on earnings per share of about 10 per cent. With the **acquisition** being effective from the beginning of December, the positive impact on 2013-14 earnings per share is expected to be 5 per cent after transaction costs.

The **company** has upgraded its targeted earnings per share growth in 2013-14 from 10 per cent to 15 per cent. This revised guidance resulted in consensus earnings per share forecasts for 2014-15 increasing from about 10 per cent to 17 per cent.

The Podium Sports **acquisition** incorporates a nine-store chain of athletic footwear and apparel clearance stores. Brett said any distribution business needs an efficient clearance strategy to protect the business and margins of its premium retail customers, which is the rationale for the Podium **purchase**.

Transactions of this kind should be viewed as a positive by investors, given that it demonstrates management's determination to grow earnings beyond what can be achieved through its store roll-out strategy.

SI view: Saucony has a substantial share of the running and walking footwear apparel market, and has become the second-largest brand by volume sold through the US running specialty channel.

3 Select Harvests

Analysts at Moelis responded positively to Select Harvests' AGM commentary, increasing earnings per share forecasts to above consensus levels based mainly on positive dynamics driving the international almond industry and the impact of the **company**'s recent **purchase** of mature orchards in South Australia.

The broker highlighted that the global supply-demand situation continues to work in the **company**'s favour, with the world's largest producer, California, constrained by prolonged drought. This region accounts for over 80 per cent of world supply.

The good news for Select Harvests is there isn't a quick fix to the problem, suggesting there will be continued upward pressure on prices. Also, the **company**'s orchards are in a more favourable stage of development in terms of providing optimum quality and maximum yields.

Management said the 2013 crop harvested towards the end of September would be about 12,500 tonnes compared with 5830 tonnes in the previous corresponding period. The average almond price of $6.60 per kilogram is well up on the $5.03 achieved in 2012.

Si view: Early signs of a robust 2014 crop mean the **company** appears to be in good shape, particularly given that price growth of between 10 per cent and 15 per cent is expected.

4 UXC

UXC acquired Keystone Management Solutions in November. According to UXC, ServiceNow is the leading global provider of cloud-based solutions that automate enterprise IT **operations**. The innovation that comes from its platform supports the ability to reach beyond IT **operations**, providing the potential to transform an organisation by automating and standardising business processes.

From an operational perspective, the **acquisition** enhances both the enterprise service management and cloud-based solutions capabilities of the UXC business, increasing subscription-based annuity revenue, an important aspect of the **company**'s business model given that it provides recurring income and earnings predictability. The **acquisition** will expand UXC's exposure to government spending, and analysts at Moelis saw significant financial benefits, upgrading profit forecasts for 2013-14, 2014-15 and 2015-16 by 3 per cent, 8.8 per cent and 8.9 per cent respectively.

Si view: Consideration for the **acquisition** was between $24 **million** and $28 **million**, depending on the achievement of performance and earnings targets. Analysts at Moelis liked the look of the **acquisition**.

5 Collins Foods

Brokers responded positively to Collins Foods proposed $55.6 million purchase of Competitive Foods as it has the potential to provide momentum for a company that has struggled to generate growth because of several factors.

First, Collins' network of KFC stores is relatively mature, and with 125 stores located across its east coast markets, there are limited store roll-out opportunities.

The other challenge is its struggling Sizzler Australia business, which has been going backwards. However, Sizzler China is experiencing above expectations growth following recent restaurant openings, and this is a possible growth catalyst.

But the Competitive Foodsacquisition changes the landscape, increasing the company's number of KFC restaurants from 125 to 169, and providing a strong market presence in Western Australia where it will have 40 stores. This will not only generate revenues in its own right, but also provide a platform for store expansion in a growing market. The acquisition will be fully debt-funded, maximising earnings per share growth which management expects to be in the vicinity of 15 per cent on a normalised full-year basis in 2014-15.

Si view: Before the news, EPS forecasts for 2013-14 and 2014-15 implied growth of 6 per cent and 5 per cent. Moelis upgraded its profit forecasts for 2014-15 and 2015-16 by 14.5 per cent and 16.7 per cent.

6 Royal Wolf Holdings

Analysts at Bell Potter initiated coverage on Royal Wolf Holdings with a 12-month target price of $3.75. The company has recently traded in that vicinity and, based on both its performance since listing in May 2011 as well as its medium-term growth profile, Bell Potter's price target appears well justified.

Royal Wolf is Australasia's largest provider of container solutions, with 33 facilities located throughout Australia and New Zealand and a hire fleet of more than 39,000 containers.

As well as being used for logistical purposes such as freight services, its containers have applications in portable storage and buildings, as well as mining camps. Bell Potter estimates the company has a market share of 35 per cent. Royal Wolf Holdings has been established for 19 years, but It highlighted that in the past five years Royal Wolf has grown its container leasing revenue from 28 per cent of total income to 48 per cent in 2012-13.

The change in revenue mix has led to earnings before interest, tax, depreciation and amortisation margins increasing from 19.3 per cent in 2008-09 to 28 per cent in 2012-13. With this trend set to continue, EBITDA margins could increase to 35 per cent in the medium term.

Si view: Royal Wolf's fleet expansion was evident in its recent quarterly update, with average units on lease for the first quarter of 2013-14 at 32,912, representing utilisation of 82.5 per cent. This was up from about 29,900 in the previous corresponding quarter when utilisation was running at 81.3 per cent.

7 KGL Resources

KGL Resources rallied substantially on the back of extremely promising exploration results in December. This development attracted plenty of attention, with analysts from UBS highlighting the impressive grades returned from drilling at its Jervois project in the Northern Territory.

Massive sulphides, including an intersection of 18 metres at 17.9 per cent copper equivalent, were delineated and applying its long-term prices on a pre-recovery basis UBS estimated that the primary intersection reports pointed to an in situ value of about $1000 per tonne.

With cash on hand of about $11 million, KGL is financially equipped to continue what to date has been an extremely positive exploration program. Consequently, there could be a string of share price catalysts as the company builds on the current resource, 60 per cent of which is in the indicated category.

The 20,000 metre drilling program designed to increase the size of the resource is only in its relatively early stages.

Si view: In addition to copper, the project could produce by-product credits from silver, gold, lead, zinc and magnetite. The resource includes 170,000 tonnes of copper and 11 million ounces of silver.

8 Aust'n Pharmaceutical Industries

Shares in Australian Pharmaceutical Industries were caught up in a sell-off in early December, shedding more than 15 per cent in the course of a week. Despite management highlighting that it was not aware of any information that could explain the volatile trading, the slide continued.

However, the following week management reported impressive first quarter sales figures for its Priceline and Priceline Pharmacy stores for the 13 weeks to November 30. Sales were up 8.2 per cent compared with the previous corresponding period, and like-for-like sales growth was a strong 5.4 per cent.

API managing director Stephen Roche commented that it was a pleasing start to the year and reflected the trend of stronger retail sales after the September federal election. He said the upbeat figures justified API's continued investment in Priceline.

Consensus estimates for 2013-14 point to earnings per share growth of 9.2 per cent and a dividend of 3.5¢.

Si view: The Priceline pharmacies are vital to API's success, and its share price performance will correlate closely with sales figures. There will be a strong focus on its first half result delivered in April.

9 PanAust

While the 2013 and 2014 earnings and production guidance provided by PanAust in December contained some positive commentary, a clinical assessment along with comparisons with previous broker estimates suggested that the broader picture was materially negative.

The news wasn't well received by analysts at Bell Potter, with the broker downgrading its recommendation from buy to hold, slashing its 12-month price target from $2.50 to $1.80 and downgrading 2014 earnings by 43 per cent.

The broker also highlighted that it had previously forecast a significant improvement in PanAust's free cash flow from 2014, but based on guidance it isn't expecting to see this occur until 2015, highlighting that the **company**'s projects will continue to consume capital in pre-development years, detracting from its ability to repay debt (net debt as at September 30, was $US153 **million**) and support dividend payments.

Si view: Even looking through 2014, the **company** doesn't present as impressive value, trading on a 2015 price-earnings multiple of 8.5 relative to Bell Potter's 12-month share price target of $1.80.

10 WDS

In a major development for WDS, the **firm** was awarded a $143 **million** contract at Aquila Resources' Eagle Downs hard-coking **coal** project at Moranbah in the Bowen Basin. It will start in the first half of 2014, indicating revenues from the two-year contract will be realised predominantly in 2014-15 and 2015-16.

The important factor is the quantum of the contract, as it increases WDS's order book by more than 50 per cent to a record $386 **million**. This represents more than the **company**'s total 2012-13 revenue of about $350 **million**.

The contract provides earnings visibility in a sector littered with casualties and uncertainty, but WDS tends to set itself apart from its peers with exposure to long-term, high-profile **energy** projects – a safer place than the **mining** services sector. This was key to the **firm**'s strong earnings growth in 2012-13, resulting in a near threefold increase in its share price. There is scope for further upside with big-ticket projects in that region going to tender in the next 12 months.

Si view: Anticipated earnings per share growth of 40 per cent a year for the next two years suggests WDS is undervalued. It has a strong balance sheet and robust cash flow, meaning dividends of 6¢ to 8¢ a year.

CO halcyg : Mayne Pharma Group Limited | retcub : RCG Corporation Ltd | rwtapl : Royal Wolf Holdings Ltd. | gnfncr : General Finance Corp.

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