Weak share price lures funds to Fortescue; Iron ore

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Body

Fund managers including Ellerston Capital's Chris Kourtis and brokers are turning bullish on Andrew Forrest's ***Fortescue***, despite the slumping iron ore price weighing heavily on the longtime ASX pariah.

In the past two weeks, four equity research firms - Citi, Morningstar, JPMorgan and Morgans Financial - have upgraded their outlook for the iron ore giant, all citing ***Fortescue***'s beaten-up share price as attractive for investors.

Likewise, Mr Kourtis, portfolio manager at Ellerston Capital, told investors this month he had switched out the fund's holding in BHP for a stake in ***Fortescue***, noting the latter had fallen much harder than its peers this year.

"Following the sharp de-rating, we believe FMG now offers a compelling entry point at current bombed-out levels," Mr Kourtis told investors, adding this was the first time the fund had owned the stock.

Analysis by The Australian Financial Review earlier this year found that ***Fortescue*** was the least-held of the ASX's 10 largest companies by Australian fund managers. That trend appears to have continued, according to a report from JPMorgan, which ranked the miner as the "most unloved" stock among Australian hedge funds.

That may start to change, however, with three buy ratings on ***Fortescue*** shares, marking the most bullish outlook on the stock from analysts in more than 18 months. Morningstar upgraded its ***Fortescue*** rating to hold.

Last week, Citi analysts said the company's 100 per cent iron ore exposure had "proved problematic", but it nonetheless slapped a buy rating on the shares given the historically cheap price.

"[We] upgrade to buy given the depth of the valuation discount rather than our still cautious iron ore view," Citi analysts told investors last week.

The slew of buy ratings follows a 41 per cent decline in ***Fortescue*** shares since the start of the year, outpacing a retreat in iron ore peers BHP and Rio Tinto, which have fallen 21 per cent and 19 per cent respectively in 2024.

The shares have been weighed down by falling iron ore prices, which was down as much as 30 per cent this year on slowing global growth and waning demand from China's property sector.

The weaker commodity price arrives at an already challenging time for ***Fortescue***, which last month delayed its much-hyped push into green hydrogen and continues to battle a federal court case relating to an IP feud with three former executives.

Further, signs that longtime funding partner US-based Capital Group has been selling billions of dollars in shares have also hurt investor confidence in recent weeks.

Despite the headwinds, Mr Kourtis said the bearish outlook was reflected in its already-weak share price.

"Negative sentiment around sluggish but flat Chinese steel demand, elevated China port inventory and an improving iron ore supply outlook from West Africa have weighed on the big three Australian iron ore producers," he said.

"However, we believe the valuation buffer now accounts for much of the risk to spot prices moving below $US100 a tonne."

While the steepening sell-off in iron ore and mining shares - the commodity fell 9 per cent last week to trade well below $US100 a tonne - caught ***Fortescue*** buyers off guard, it was profitable for some hedge funds. Those include Sydney's Sage Capital, which said its short against ***Fortescue*** was the top contributor to returns last month.

Looking ahead, Sage Capital portfolio manager Sean Fenton said he remained bearish on the outlook for iron ore. "We anticipate iron ore and lithium to remain weak due to excess industrial capacity created in China due to domestic policy that encourages the economy to diversify away from housing," he said.

Others also remain cautious, with nine of the 16 equity analysts covering the stock sticking with a sell rating. UBS reiterated its sell recommendation this week, saying the iron ore miner was more exposed to further weakness in the iron ore price than diversified miners BHP or Rio Tinto.

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