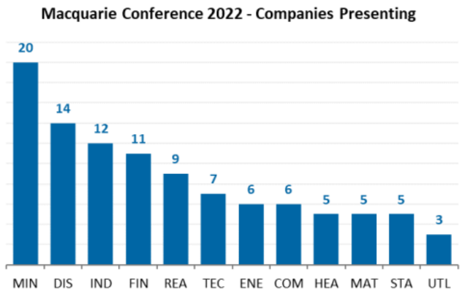
Research

6 May 2022 Australia

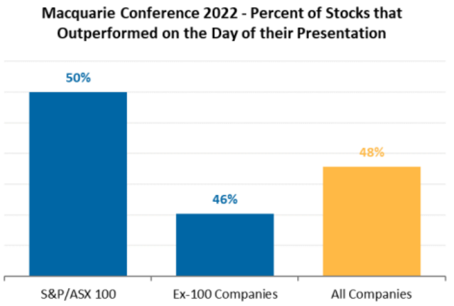
EQUITIES

103 companies presented at the 2022 Macquarie Australia Conference



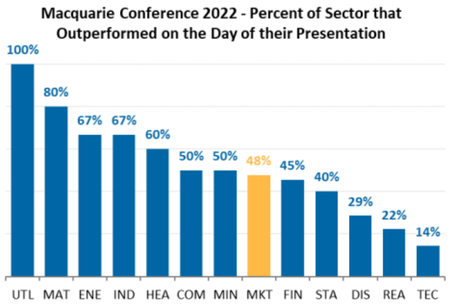
Source: Macquarie Research, May 2022

Slightly more stocks underperformed than outperformed after presenting, with weaker results in small caps



Source: Macquarie Research, May 2022

Materials stocks tended to outperform on the day of their presentation, while Technology stocks underperformed



Source: FactSet, Macquarie Research, May 2022

Australian Equity Strategy
Macquarie Conference 2022 Wrap

Key points

- 103 companies presented at the Conference, back to pre-COVID levels.
- Inflation was the key theme and companies believe they are well positioned to pass on cost rises, but investors tend to be more cautious.
- With the RBA starting to hike rates during the conference, favour stocks that benefit like CPU, not those with headwinds (housing/autos/retail).

Event

- We highlight some of the key takeaways from the 24th Macquarie Australia Conference, which saw 103 companies accounting for 31% of the All Ords by market capitalisation present to investors over May 3-5, 2022. The conference was again an in-person event, and for many the interactions during the breaks were also a key reason to attend the conference.

Impact

- **Cost inflation the key macro takeaway from the conference**. Last year one-quarter of companies talked about rising input costs. This year most if not all companies talked about inflation. Labour cost pressures appear to be a bigger issue this year, as labour markets are tight, skilled labour is hard to find and COVID continues to drive a higher level of absenteeism. While border reopening and reduced COVID restrictions will help to improve labour availability over time, it looks like wage growth is likely to accelerate.
- **Most companies are optimistic on their ability to pass on higher costs** given the economy is still growth and consumer balance sheets are still in good shape. The pool of savings accumulated during the pandemic was often seen as providing a buffer to support consumer spending despite the challenges from inflation and rising interest rates. Investors tend to be more sceptical on the ability of companies to continue to pass on cost increases as policy tightening slows growth. Discretionary stocks were often seen as poorly positioned by investors given the prospect of a slowing housing cycle due to RBA rate hikes and the fading COVID spending boom. Stocks like TCL with contract-based inflation offsets are likely to be better positioned as the cycle slows, but inflation remains elevated (i.e. a stagflation scenario).
- **Resources well positioned.** If the war in Eastern Europe is not going to end anytime soon, this provides some support for commodity prices. The resource companies at the conference tended to be among the most optimistic, supported by high commodity prices. FMG and PLS for example are still seeing strong demand from China despite COVID lockdowns, while DDH and IMD are also seeing strong activity continuing. There is also an expectation of further stimulus in China which will support commodities. For more on this theme, see **The Bull Case for Australia** (Part 1 and Part 2).

Action & Recommendations

- **Groups with tailwinds**: Beneficiaries of higher rates (e.g. **CPU**), companies with contract-based pricing power (**TCL**), resources with strong current FCF (**S32**), COVID recovery plays (**CSL**, **DXS**) and defensives with reasonable valuations (**AMC**). **Groups with headwinds**: Beneficiaries of lower interest rates (housing, auto, discretionary retail), COVID beneficiaries and higher beta stocks (cyclicals, small caps and stocks with little to no earnings).

Key takeaways by sector

Financials that benefit from central bank rate hike like CPU are well positioned for growth.

- **Financials**. With the RBA kicking off a new tightening cycle on the first day of the conference, investors are interested in stocks that benefit from higher yields. While not technically a Financial, **CPU** is one of the biggest beneficiaries. The company estimates a 100bps in average interest rates equates to an annualised EPS increase of US 26 cents in margin income, or roughly half last year's EPS. The other financial stocks with positive leverage to higher interest rates that presented include Insurers (**MPL**, **NHF**), Banks (**BOQ**, **AFG**, **PPM**) and Diversified Financials (**CGF**, **HUB**, **EML**). **QAL** argues they should also be on a list of rated beneficiaries as they have a relatively short tenor credit portfolio, allowing funds to take advantage of higher rates. **NHF** noting a strong rebound in Travel sales, with Mar/Apr income 80% of pre-COVID levels and FY22 operating loss at the lower end of expectations. This growth also highlights the travel recovery as international borders reopen.

Rising construction costs and a slowing residential cycle are concerns but rent collectors should be more defensive in a volatile market.

- **Real Estate**. Rising construction costs was a key topic in Real Estate, and managements seemed confident the issue was manageable (higher prices, pre-order materials). That said, while inflation is still rising, this is likely still a concern for investors, especially as we roll forward to future years. A slowing residential outlook following RBA rate hikes and fading COVID-driven demand was also a topic of discussion. **SGP** for one said the near-term outlook was positive given high enquiry levels, but thought rising rates would be a medium-term headwind for price growth and volumes. On Office, **MGR** was seeing an uplift in CBD activity with tenants more confident to sign leases. With Amazon noting excess capacity in its real estate footprint, **GMG** highlighted Amazon was ~5% of their rent and a similar share of development. **GMG** also sees continued demand for industrial property. Historically, REITs have provided some inflation protection from rising rents, but this outcome is questionable in some areas (e.g. office, with high vacancy rates). **DXS** was the best performing real estate stock, as it upgraded FY22 EPS guidance to +2.5% (from +2.0%).

Discretionary stocks are often first to be impacted by RBA hikes and we prefer travel over other areas of the Discretionary sector.

- **Discretionary**. Retailers are positive on the health of the consumer given low unemployment, and the pool of savings built up during COVID. Inflation pressures are coming through, with higher shipping, raw materials and labour costs. Companies are positive on their ability to pass on higher costs given the current health of the consumer. Investors tend to be more sceptical on Discretionary stocks that benefited from the COVID spending boom and their ability to continue to pass on price rises given RBA rate hikes, a weakening housing market and declining real wages. This is likely why some retail stocks underperformed if their update was less than expected. **TPW's** trading update with revenue growth of +23% was slightly below MRE (+25.5%), and has been pressured by the ongoing sell-off in US ecommerce stocks. **JBH** highlighted solid sales growth, but said there were too many uncertainties to give guidance. **ARB** was the worst performer after their presentation, as guidance of $700m in FY22 sales was below expectations, while cost rises and labour availability remain issues. Supply chain issues remain an issue, with companies continuing to hold more inventory as a hedge. Travel continues to see a strong recovery in corporate (**CTD**, **FLT**) and leisure (**FLT**), but **FLT** guidance was still less than hoped and it was the second worst performer.

Media stocks tended to provide positive updates, but the ad cycle often slows with the consumer.

- **Communications**. Media stocks tended to outperform over the conference, often supported by positive trading updates. **OML** was the best performer in media, with 1Q strength (sales +15%) flowing into 2Q as outdoor advertising recovers. **NEC** noted that advertiser sentiment remains positive, but investors are concerned about a slowing ad market following the RBA rate hikes. Following the recent Netflix update (i.e. falling subscriber numbers), **NEC** also highlighted that they see a period of subdued subscriber growth for Stan given it was also a beneficiary of the pandemic. On Telecoms, **TPG** said mobile subscriber net adds had accelerated, while also talking about ARPU growth again.

Health stocks are defensive and CSL is a COVID recovery play, but a key issue for the sector is valuations.

- **Health**. **CSL** was the best performer among the Health stocks. Plasma collections are continuing to improve, with volumes broadly back to pre-COVID levels. Gross margins for CSL had also been impacted by higher donor fees, but margins are expected to recover over the next couple of years as new donors become return donors, improved volumes reduce costs per unit, the benefits of the Rika platform and ongoing efficiencies in collection and manufacturing. **RMD** was an underperformer in Health, as they continue to face supply chain challenges, including electron component/chip shortages that constrain their ability to benefit from a product recall from their competitor.

Staples companies like ELD that benefit from global shortages are well positioned.

- **Staples**. **ELD** seems well positioned in the current environment given the strength of Australia's agriculture sector due to global shortages. Interestingly, there appears to be some caution on fertilizer prices declining in the second half, as happened in 2008. That said, given the war in Eastern Europe may continue for years, this situation may be different and fertilizer prices may remain elevated for longer. While stocks like **ELD** may benefit from global shortages, higher feed costs have been negative for **ING**, along with elevated transport and supply chain costs. That said, **ING** noted that poultry is an attractive protein.

Technology stocks often provided positive updates, but as with health the key risk is high valuations.

- **Technology**. Technology stocks tended to underperform during the conference, as market sentiment towards the sector has been more negative as real yields rise. That said, some provided positive trading updates. **NEA** upgrading Group ACV guidance to the upper end of their $155-160m range. PXA said 3Q volumes were +14% and current FY22 trends suggest they will be at the upper end of their guidance range. **PXA** noted there had been a slowdown in the market in 2H, but activity was still strong.

Resource related companies are likely better positioned to grow given the strength in commodity prices supports activity

- **Industrials**. **CWY** was one of the largest underperformers in the ASX 100 after they provided a negative trading update, warning of a $15-20m impact to FY22 EBITDA from higher fuel prices, flood impacts, equipment failures in the health business and labour availability. **CWY** does have some protection against price increases, but the hedges are not perfect and there can be issues with timing. On **RWC**, investors are concerned about the impact of rising interest rates, but management stressed their products are relatively defensive as they are repair & remodel exposed. **RWC** (+5.4% vs XJO) was the best performing stock in the ASX 100 following their presentation. With investors looking for inflation protection, **TCL** is a standout, as their tolls rise with inflation. That said, investors are concerned about the impact of rising fuel prices and inflation on traffic and the broader flow-on effects on economic growth. The resource related companies such as **IMD** and **DDH** are seeing strong demand, supported by high customer activity levels. **WOR** is seeing their sales pipeline build in response to higher energy prices. **AZJ** noted miners are unable to ramp up production in the short terms in response to higher prices. The lack of supply response supports higher prices.

Materials stocks were among the best performers, supported by positive upgrades and lower valuations

- **Materials** was one of the best performing groups following their presentations with multiple stocks posting solid results, and valuations generally being lower than some other sectors. **ABC** said 1Q22 demand remained strong, with concrete and aggregate volumes +10% and +28%, respectively. **SGM** said 3Q was tracking inline with previous guidance while 4Q had commenced strongly. **SGM** also noted how the company was well positioned in metals recycling, and the attractive growth prospects in non-ferrous. **AMC** also outperformed after its presentation, as high margin areas like Nespresso pods are growing volumes.

Resource companies tended to be optimistic given high commodity prices support high current profitability

- **Resources** companies tended to be more confident, which is not surprising given many are experiencing strong profitability supported by high commodity prices. We believe this is a situation that will continue for some time, supported by the war in Eastern Europe. The COVID lockdowns in China are the key concern for investors, but **FMG** for one said that sales were still strong, with port inventories falling (although finished product inventories have risen). **PLS** also has not seen an impact to lithium demand. FMG also expected stimulus in China to provide support for iron ore demand later in the year. In Energy, **WPL** has seen buying interest in long-term contract supplies had increased significantly after the recent price surges in Europe and Asia. **BPT** have locked in turnkey structures for a large portion of upcoming capex on two big projects, with long lead items secured. But outside of this, costs are rising, and future costs may also be higher.

- **Utilities.** **AGL** said the operating environment is robust with elevated pricing. Their cost base is largely fixed with contracted NSW coal and low-cost brown coal.

Fig 11 Macquarie Conference 2022 – highest and lowest returns relative to ASX 200 on day of presentation

Company Name	Code	Return	Rating	Sector
ASX 100 - Highest Relative Return vs ASX 200				
Reliance Worldwide	RWC	5.4	OP	Industrials
Amcor CDI	AMC	4.9	OP	Materials
Lynas Rare Earths	LYC	3.2	OP	Mining
Challenger	CGF	2.3	N	Financials
OZ Minerals	OZL	1.8	N	Mining
Worley	WOR	1.8	OP	Energy
Dexus	DXS	1.7	OP	Real Estate
Transurban Group	TCL	1.5	OP	Industrials
Northern Star Resources	NST	1.4	OP	Mining
CSL	CSL	1.3	OP	Health Care
Evolution Mining	EVN	1.3	UP	Mining
Sonic Healthcare	SHL	1.2	N	Health Care
Nine Entertainment	NEC	0.9	N	Telco & Media
Wesfarmers	WES	0.8	N	Discretionary
Endeavour Group	EDV	0.7	N	Staples
Woodside Petroleum	WPL	0.1	N	Energy
Ex-100 - Highest Relative Return vs ASX 200				
ADBRI	ABC	6.2	OP	Materials
Regis Resources	RRL	5.6	OP	Mining
oOh media	OML	4.6	OP	Telco & Media
St. Barbara	SBM	4.3	OP	Mining
Sims	SGM	3.6	N	Materials
29metals	29M	3.4	OP	Mining
EML Payments	EML	3.0	OP	Technology
HUB24	HUB	2.8	OP	Financials
Contact Energy	CEN	2.5	OP	Utilities
City Chic Collective	CCX	2.2	OP	Discretionary
Lovisa Holdings	LOV	1.9	OP	Discretionary
OceanaGold CDIs	OGC	1.7	OP	Mining
Beach Energy	BPT	1.7	UP	Energy
Ventia Svc Grp	VNT	1.5	OP	Industrials
Austal	ASB	1.1	N	Industrials
Qualitas	QAL	0.9	OP	Real Estate
Seven Group Holdings	SVW	0.8	OP	Industrials
Elders	ELD	0.7	OP	Staples
NIB	NHF	0.7	N	Financials
Australian Finance Group	AFG	0.7	OP	Financials
IPH	IPH	0.7	OP	Industrials
Kelsian Group	KLS	0.6	OP	Industrials
Bellevue Gold	BGL	0.4	OP	Mining

Company Name	Code	Return	Rating	Sector
ASX 100 - Lowest Relative Return vs ASX 200				
ARB	ARB	(11.0)	OP	Discretionary
JB Hi-Fi	JBH	(4.6)	OP	Discretionary
Computershare	CPU	(3.2)	OP	Technology
Mineral Resources	MIN	(3.1)	OP	Mining
Cleanaway Waste Mgmt	CWY	(2.8)	OP	Industrials
South32	S32	(2.6)	OP	Mining
Fortescue Metals Group	FMG	(2.2)	N	Materials
Charter Hall Group	CHC	(2.1)	OP	Real Estate
Bank of Queensland	BOQ	(1.3)	N	Financials
Resmed CDIS	RMD	(1.3)	OP	Health Care
Goodman Group	GMG	(1.1)	OP	Real Estate
Medibank	MPL	(0.8)	N	Financials
Pilbara Minerals	PLS	(0.6)	OP	Mining
Stockland	SGP	(0.6)	N	Real Estate
Lendlease Group	LLC	(0.5)	OP	Real Estate
Mirvac Group	MGR	(0.4)	OP	Real Estate
Treasury Wine Estates	TWE	(0.2)	N	Staples
Downer EDI	DOW	(0.1)	OP	Industrials
WiseTech Glob	WTC	(0.1)	N	Technology
Ex-100 - Lowest Relative Return vs ASX 200				
Flight Centre Travel Grp	FLT	(6.5)	N	Discretionary
Costa Group Holdings	CGC	(6.0)	OP	Staples
Chalice Mining	CHN	(5.8)	OP	Mining
Bravura Solutions	BVS	(4.8)	OP	Technology
Bapcor	BAP	(4.5)	OP	Discretionary
Inghams Group	ING	(3.9)	N	Staples
Liontown Resources	LTR	(3.4)	OP	Mining
Corporate Travel Mgmt	CTD	(2.8)	OP	Discretionary
Pinnacle Invt Mgmt Group	PNI	(2.8)	OP	Financials
Nearmap Ltd	NEA	(2.7)	N	Technology
Pepper Money	PPM	(2.7)	OP	Financials
Sandfire Resources	SFR	(2.5)	OP	Mining
Temple & Webster	TPW	(2.4)	N	Discretionary
Smartgroup	SIQ	(2.4)	N	Industrials
Boss Energy	BOE	(2.2)	OP	Energy
Seven West Media	SWM	(2.1)	OP	Telco & Media
Best & Less	BST	(2.1)	OP	Discretionary
PolyNovo	PNV	(2.0)	OP	Health Care
FINEOS Corporation Holdings DR	FCL	(1.9)	OP	Technology
DDH1	DDH	(1.6)	OP	Mining
Super Retail Group	SUL	(1.6)	N	Discretionary
Fletcher Building Ltd	FBU	(1.5)	OP	Industrials
Imdex	IMD	(1.5)	OP	Mining
Breville Group	BRG	(1.3)	OP	Discretionary
Credit Corp Group	CCP	(0.6)	OP	Financials
De Grey Mining	DEG	(0.4)	OP	Mining
TPG Telecom	TPG	(0.4)	OP	Telco & Media
AUB Group	AUB	(0.2)	OP	Financials
Southern Cross Media Grp	SXL	(0.2)	OP	Telco & Media
Nick Scali	NCK	(0.0)	OP	Discretionary

Source: FactSet, Macquarie Research, May 2022

Important disclosures:

Recommendation definitions

Macquarie – Asia and USA
Outperform – expected return >10%
Neutral – expected return from -10% to +10%
Underperform – expected return <-10%

Macquarie – Australia/New Zealand
Outperform – expected return >10%
Neutral – expected return from 0% to 10%
Underperform – expected return <0%

Note: expected return is reflective of a Medium Volatility stock and should be assumed to adjust proportionately with volatility risk

Volatility index definition*

This is calculated from the volatility of historical price movements.

Very high–highest risk – Stock should be expected to move up or down 60–100% in a year – investors should be aware this stock is highly speculative.

High – stock should be expected to move up or down at least 40–60% in a year – investors should be aware this stock could be speculative.

Medium – stock should be expected to move up or down at least 30–40% in a year.

Low–medium – stock should be expected to move up or down at least 25–30% in a year.

Low – stock should be expected to move up or down at least 15–25% in a year.
* Applicable to select stocks in Asia/Australia/NZ

Recommendations – 12 months
Note: Quant recommendations may differ from Fundamental Analyst recommendations

Financial definitions

All "Adjusted" data items have had the following adjustments made:
Added back: goodwill amortisation, provision for catastrophe reserves, IFRS derivatives & hedging, IFRS impairments & IFRS interest expense
Excluded: non recurring items, asset revals, property revals, appraisal value uplift, preference dividends & minority interests

EPS = adjusted net profit / efpowa*
ROA = adjusted ebit / average total assets
ROA Banks/Insurance = adjusted net profit /average total assets
ROE = adjusted net profit / average shareholders funds
Gross cashflow = adjusted net profit + depreciation
*equivalent fully paid ordinary weighted average number of shares

All Reported numbers for Australian/NZ listed stocks are modelled under IFRS (International Financial Reporting Standards).

Recommendation proportions – For quarter ending 31 Mar 2022

	AU/NZ	Asia	USA	
Outperform	63.27%	69.10%	79.79%	(for global coverage by Macquarie, 6.23% of stocks followed are investment banking clients)
Neutral	30.61%	20.65%	18.09%	(for global coverage by Macquarie, 3.33% of stocks followed are investment banking clients)
Underperform	6.12%	10.25%	2.13%	(for global coverage by Macquarie, 1.16% of stocks followed are investment banking clients)

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