October 2018 — Over the Horizon Market Commentary by David Offer

October was a very tough month for the Australian share market, with the All Ordinaries index falling 402 points (6.5%) to close at 5,913 points. Share market weakness has continued into November, with our market off a further 1.3% at the time of writing.

From our market high of 6,481 points in August, at the current market level of 5,837 points, we are down 10% in value over the last 3 months. There has been no shortage of concerns aired by share market commentators. Internationally, there have been fears of potential adverse ramifications for global growth stemming from the US China trade war, rising interest rates and more recently Brexit. Domestically, the implications of substantially tighter lending practices being imposed on our major banks at the same time the East Coast property market is looking vulnerable is starting to play on investor minds.

We are not as bearish on the outlook of a number of listed businesses as implied by their current depressed share prices. For your interest, we provide a summary of some of our core share purchases being made at this time. We believe that for many businesses, including those we have listed below, current depressed share prices are providing a decent margin of safety for investors looking to make an investment into these businesses.

ASX 100 Companies

Company	Price	Target Price	Forecast 2019 PE Ratio	Forecast 2019 Dividend Yield
AGL Energy	$18.36	$20.00	12X	6.3% - 80% franked
AGL is an essential product provider that is conservatively geared and presently trading on historically low earnings multiples and above market average dividend yield. AGL's earnings are likely to moderate over the medium term due to government intervention to reduce retail electricity prices and the closure of the Liddell coal-fired power station in 2022. These earnings headwinds should be partly muted by investment in growth projects and cost-out initiatives. AGL generates strong free cash flow and has conservative financial leverage, putting it in a good position to deal with any earnings headwinds as well as potentially make capital investments or return capital to shareholders. RESEARCH				
Amcor	$13.50	$16.11	14.5X	4.8% - unfranked
Amcor is the global leader in flexible packaging, rigid plastic containers and specialty cartons and supplies its products to some of the largest global brands including Coca Cola and Nestle. Amcor focuses on high value packaging for consumer staples and as such has defensive attributes. The business has enjoyed steady margin growth and this should continue with the recent acquisition of Bemis, which should facilitate significant cost savings through synergies. Amcor is trading on undemanding earnings multiples at this time and, should the merger with Bemis progress as planned, we expect the shares will be re-rated. RESEARCH				

Company	Price	Target Price	Forecast 2019 PE Ratio	Forecast 2019 Dividend Yield
Boral	$5.37	$7.15	11.7X	4.85% - 50% franked
Boral is a well-run business that is trading on an undemanding earnings multiple. While the share price has recently been sold down due to concerns relating to the slowing East Coast property market, we view the Company's outlook as reasonably favourable. In Australia, this is due to significant future planned infrastructure spending (refer to Chart). In the US, off the back of a strong economy and given housing starts in the US have lagged long term averages in recent years, we believe that at some point there will be a catch up period in US housing construction. RESEARCH				
Crown Resorts	$11.74	$15.00	18.9X	5.1% - 60% franked
Crown is a well-run business that has defensive attributes that include monopoly casino licenses in WA and VIC, owning its casino and hotel buildings (substantial net tangible assets) and no net debt at this time (debt will again build as the Sydney casino nears completion). Crown is well positioned for long term growth with an eventual recovery in the WA economy assisting its WA operations and opening of Sydney casino, expected in 2021. Likewise, Crown is well positioned to cater for expected ongoing growth in inbound Asian tourists to Australia. RESEARCH				
Lend Lease	$14.00	$17.20	17.3X	3% - unfranked
Lend Lease focuses on large urban renewal projects in major capital cities. The business is vertically integrated, enabling the generation of income from each stage of the process: deal structuring and financing, developer fees, construction fees and fund management fees. We view Lend Lease's vertical integration and ability to provide complete urban renewal solutions as a key competitive advantage. All of Lend Lease's divisions have strong pipelines of work and the Company is steadily expanding its global footprint. The Company has nominal debt and, to date, we view the Company as having been conservatively managed and run well. The key risk relating to Lend Lease is execution risk; as highlighted by the recent announcement of unexpected losses on several engineering projects. We hope Lend Lease learns from recent engineering cost overruns and applies lessons learnt to the other aspects of its business. Lend Lease's profits should rebound sharply in 2020 and for that year the Company is on a prospective PE ratio of just 10X and dividend yield of 5.3%. RESEARCH				
Origin Energy	$7.00	$9.11	10.6X	2.85% - unfranked
Origin's balance sheet restoration is now largely complete and the Company will soon be in a position to resume paying distributions. After reaching recent highs of $10.00 a share, we consider $7.00 to once again be an attractive entry price into the Company. Origin is trading on undemanding earnings multiples and is generating significant additional annual cash flow over reported profits, which is masked by high depreciation and amortisation charges. While energy retailers may be facing peak earnings in the short term, we believe that in Origin's instance this is more than offset by the attractive outlook for its LNG operations. RESEARCH				
Sonic Health	$21.89	$25.50	18.5X	3.8% - 30% franked
Sonic is the market leader for pathology services in Australia and is implementing its industry consolidation model within the US and Europe. Offering diagnostic medicine, the Company offers an essential service that, being preventative in nature, should continue to receive Government support into the future. As the market leader within the markets it operates, SHL achieves significant economies of scale; the result being lower costs to the consumer while still maintaining adequate profit margins. We view recent share price weakness as a buying opportunity. RESEARCH				

Smaller Emerging Companies

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<tr><th>Company</th><th>Price</th><th>Target Price</th><th>Forecast 2019 PE Ratio</th><th>Forecast 2019 Dividend Yield</th></tr>
<tr><td>ARQ Group</td><td>$2.17</td><td>$2.80</td><td>12.8X</td><td>5% - fully franked</td></tr>
<tr><td colspan="5">ARQ has recently been sold down due to underperformance in its Small to Medium Business division. This stemmed from management issues resulting in a loss of sales momentum and cancellation of services by a major telco. Management has taken responsibility for this loss of momentum and is confident these issues are in the process of being addressed. ARQ is forecasting EBITDA growth of between 7% - 15% in 2019 and 10% - 20% in 2020. With low gearing, a degree of recurring revenue and operating within a growing market with a blue chip client base, ARQ is a sound company that has good growth prospects. As such we consider ARQ undervalued and, if the Company delivers on it’s forecasts, should be re-rated. COMPANY PRESENTATION</td></tr>
<tr><td>Estia Health</td><td>$2.16</td><td>$2.80</td><td>12.7X</td><td>7.4% - fully franked</td></tr>
<tr><td colspan="5">Estia has been sold down on the back of the recent Federal Government announcement of a new Royal Commission into Aged Care, with the market concerned that this Royal Commission could be as damaging as the current Banking Royal Commission for participants. We view this as unlikely. Estia has largely avoided adverse publicity to date with past market weakness due to issues relating to previous management that are now in the past. Estia is trading on a high sustainable yield and has minimal gearing. The Company should be able to grow profits modestly into the future and as such the Company appears to be oversold at this time. COMPANY PRESENTATION</td></tr>
<tr><td>Dacian Gold</td><td>$2.26</td><td>$2.58</td><td>13.1X</td><td>No dividend in 2019</td></tr>
<tr><td colspan="5">Dacian Gold is an emerging Goldfields gold producer that is presently ramping up production at Mt Morgans, which is expected to generate 200,000oz pa once operating at capacity for AISC of approximately A$1,000/oz. Mine life is expected to be greater than 10 years. Mt Morgans is essentially a number of mines (both above and below ground) within close proximity of a 2.5 Mtpa processing plant and gas-fired Power Station. Management have indicated that each of these mines (Cameron Well, Westralia Mine Area and Jupiter Mine Area) have substantial growth options and have hinted at a long term production goal of 300,000oz pa. With Dacian having a debt repayment profile of less than 2 years and prospective 2020 forward PE ratio of less than 6X and dividend yield of 5%, we believe there is scope for a substantial re-rating in share price. RESEARCH</td></tr>
<tr><td>Pioneer Credit</td><td>$3.03</td><td>$4.00</td><td>9.5X</td><td>5.9% - fully franked</td></tr>
<tr><td colspan="5">Pioneer has enjoyed strong profit growth over the last 5 years. Essentially a debt collector, Pioneer works hard to establish relationships with its ‘clients’ to the extent that in many instances the relationship with the ‘client’ continues post the repayment of outstanding debt. Pioneer is well regarded within the industry and with Banks unwilling to aggressively recoup outstanding loans due to risking adverse publicity, is well placed to grow its outstanding loan book as well as cross sell other products to its ‘clients’ into the future. Management are experienced and have significant shareholdings in the Company. COMPANY PRESENTATION</td></tr>
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Company	Price	Target Price	Forecast 2019 PE Ratio	Forecast 2019 Dividend Yield
SG Fleet	$3.05	$4.08	10.5X	6.9% - fully franked
SG Fleet has generated strong profit growth year on year since the Company first listed in 2014; growing its EPS from 16.7 cents in 2015 to 26.3 cents in 2018. SGF sees reasonable growth within its core markets but with all debt repaid is now looking to make an acquisition. Recent share price weakness shows little for the strong growth in profits over recent years and suggests the market is concerned about what any new acquisition will entail. Failing a successful acquisition, SG Fleet could consider an on market share buyback to further boost EPS growth in future years. We are mindful the Federal Government could consider changes to existing arrangements concerning the packaging of motor vehicles by employees but consider any such changes a low probability at this time. COMPANY PRESENTATION				

If you would like to discuss any of the above or any other aspect of your investment portfolio, please do not hesitate to contact our office.

Finally, for those investors on a zero tax rate and who participated in the RIO Tinto off-market buyback, you enjoyed a great outcome, selling your shares for an effective sale price of $95.50 when including franking credits. (Franking credits will be refunded when you lodge your 2018/19 taxation return.) We are open to repurching holdings in RIO should the shares weaken back below $75. BHP has also recently annouced an off-market buyback and once again, for those investors who can benefit, we will be looking to participate in this off-market buyback during December.

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