

The View From The Outer

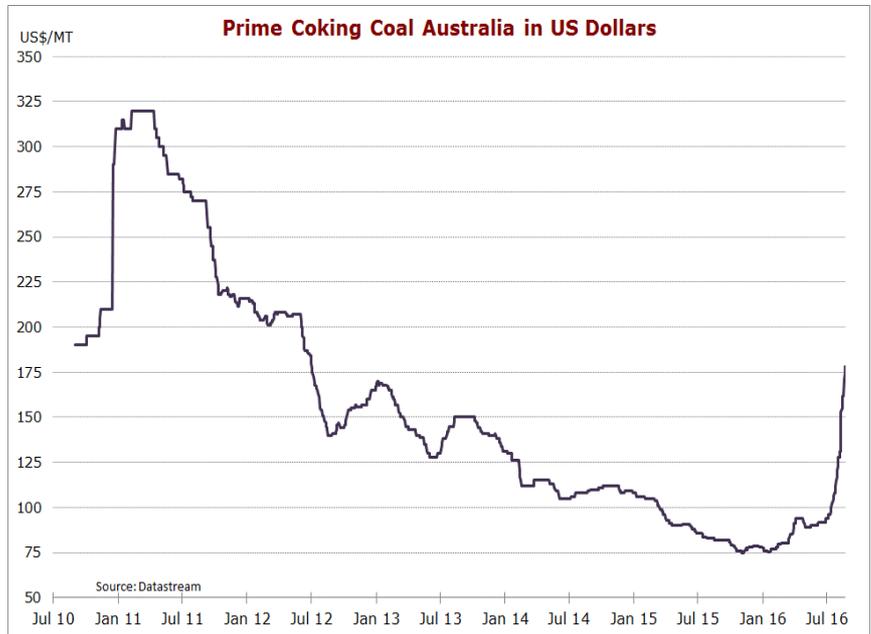
David Jarman – Chief Investment Officer

Friday 22 September, 2016

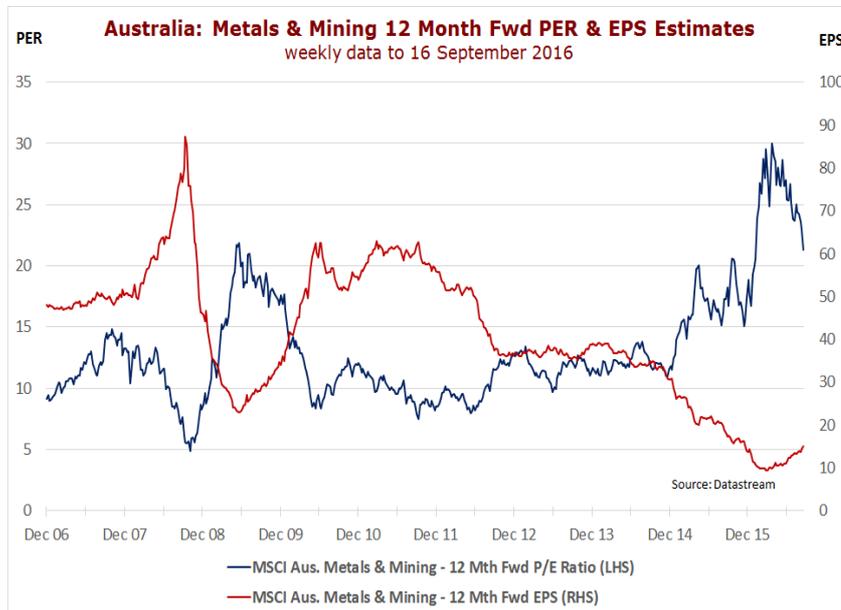


An observation on the Metals & Miners

Resource sector outperformance has been dramatic since most commodity prices troughed in early 2016. The impact of China's fiscal stimulus in response to the pace of the slowdown through 2015 has been more supportive and longer lasting than generally expected. Consensus rolling 12 month EPS estimates of the Metals & Miners are now ~60% above the low in late March, but off a very low base and only back to the level that was expected back in December 2015. Spot commodity prices initially rallied sharply off the depressed levels of early 2016 and have since continued to remain above expectations. Monthly roll forward is also a factor.



Of course the outlook varies by commodity, with the supply side the important swing variable. This underscores our



negative view on the iron ore price for example. We maintain negative research recommendations on BHP Billiton, Fortescue Metals and Rio Tinto. We also maintain an underweight recommendation towards the resource sector.

We acknowledge the risk that earnings estimates are likely to continue to be revised up if spot prices remain at current levels (that is, as analysts put through "reality adjustments" to nearer term earnings). For those who wish to increase resources exposure on such a view, our preference is

South32 (positive recommendation). From amongst the major companies, South32 stands out as the most leveraged company to the two commodities that have shown the most dramatic recent price increases: Coking Coal (see chart above right) and Manganese.

RESEARCH RECOMMENDATION DEFINITIONS

Positive	Stock is expected to outperform the S&P/ASX 200 over the coming 24 months
Neutral	Stock expected to perform in line with the S&P/ASX 200 over the coming 24 months
Negative	Stock is expected to underperform the S&P/ASX 200 over the coming 24 months
Speculative Buy	Stock has limited history from which to derive a fundamental investment view or its prospects are highly dependent on event risk, <i>eg.</i> Successful exploration, scientific breakthrough, high commodity prices, regulatory change, etc.
Suspended	Stock is temporarily suspended due to compliance with applicable regulatory and/or Evans & Partners policies in circumstances where Evans & Partners is acting in an advisory capacity.
Not Rated	Stock is not included in our investment research universe.

Research Criteria Definitions

Recommendations are primarily determined with reference to how a stock ranks relative to the S&P/ASX 200 on the following criteria:

Valuation	Composite of Rolling 12 month prospective multiples and discounted cash flow (DCF), or DCF for resource stocks.
Earnings Outlook	Forecast 2 year EPS growth.
Earnings Momentum	Percentage change in the current consensus EPS estimate for the stock (rolling 1 year forward basis) over the consensus EPS estimate for the stock 3 months ago.
Shareholder Returns	Composite of forecast ROE (rolling 1 year forward basis) and the percentage change in ROE over 2 years.
Debt Servicing Capacity	Rolling 12 month EBIT Interest Cover ratio.
Cyclical Risk	Qualitative assessment of the 2 year outlook for a stock/industry's profit cycle.
Industry Quality	Qualitative assessment of an industry's growth/returns potential and company specific management capability
Financial Transparency	If we don't understand it, we won't recommend it.

For stocks where Evans & Partners does not generate its own forecasts, Bloomberg consensus data is used. Analysts can introduce other factors when determining their recommendation, with any material factors stated in the written research where appropriate.

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