

ShawandPartners

The Research Monitor

March Quarter 2019

inside this issue

M&A ruled supreme in 2018

Franking credits &

corporate balance sheets

Credit markets

Oil market dynamics

+ stock picks

Q4 2018 Performance

The Australian Share Market, as measured by the S&P/ASX 300 Index, recorded its worst quarter since 2011, falling 9.2% on a price basis and by 8.4% including dividends in the December 2018 quarter.

Weak Q3 GDP growth figures published in early December added to the woes caused by global trade concerns and the path of US monetary policy for Australia's share markets.

Among Australian equity sectors, only one sector posted positive returns during the quarter – Transportation – where Transurban (TCL), the largest constituent of this sector posted a 3.8% gain. **Other defensive sectors performed relatively well, with the Utilities sector down only 3.1% after dividends and the Real Estate sector down only 1.7% after dividends.**

Many REITs trade ex-dividend at the end of the quarter which helped boost returns. There are no fewer than 34 companies in the ASX300 index and the best, Shopping Centres Australasia Property Group (SCP) posted a 6.3% gain. The worst, Lendlease Group (LLC) posted a 40.8% loss.

The largest component of the S&P/ASX 300 Index is the Banks Sector (23.5% index weight), which fell 8.0% in price terms and -6.0% including dividends, ending the period over which banks have underperformed the index. Similarly, the second largest sector, Materials (18.1% index weight) fell only 5.1% including dividends, with bellwether BHP down only 1.2%.

Energy sector returns were negative following a steep fall in the oil price. West Texas Intermediate oil prices fell 38.2% in the quarter and this dragged the sector down 21.6% after dividends, with heavyweight Woodside Petroleum (WPL) down 18.8%. **The worst performing sector was Media and Entertainment, down 24.9%** due to big falls in Nine Entertainment (NEC), Domain Group (DHG) and Seven West Media (SWM) down 38.9%, 36.3% and 45.0% respectively.

Global equity markets also performed poorly in the December quarter, with the World Index down 12.8%, Japan down 17.3%, Europe down 13.2% the US S&P500 down 14.0% and NASDAQ down 17.5%.

Bond markets provided a safe haven against the equity market weakness with the Bloomberg AusBond Composite (0+Y) index up 2.2% and Bank Bills returning 0.5%. The spread between 90-day bank bills and cash rose again from 44 basis points at the end of September to 59 basis points at the end of December – a sign of tightening credit conditions. The same spread was 29.5 points at the start of the year.

Measures of housing activity continued to show weakness, suggesting the broader economy is coming off the boil somewhat, although a lower currency is likely to provide some cushioning effect.

The Australian dollar has fallen for five consecutive quarters. Market measures of risk or volatility, are elevated suggesting investors are uncomfortable with the likely path of inflation, interest rates, growth and trade.

The Banks sector, the largest component of the S&P/ASX 300 Index, fell 8.0%.

Sector	Performance	Market Cap
↓ Banks	-5.96%	361,980
↓ Materials	-5.05%	279,568
↓ Real Estate	-1.71%	109,783
↓ Pharmaceuticals, Biotech & Life Sciences	-9.08%	87,221
↓ Energy	-21.62%	83,376
↓ Diversified Financial	-14.23%	76,286
↑ Transportation	1.87%	72,178
↓ Insurance	-8.84%	57,906
↓ Food & Staples Retailing	-6.31%	54,177
↓ Retailing	-14.02%	50,878
↓ Health Care Equipment & Services	-7.45%	48,233
↓ Consumer Services	-15.77%	45,069
↓ Telecommunication Services	-10.94%	41,110
↓ Commercial & Professional Services	-13.97%	37,718
↓ Software & Services	-14.14%	34,082
↓ Food Beverage & Tobacco	-8.30%	32,949
↓ Utilities	-3.11%	30,735
↓ Capital Goods	-19.88%	13,604
↓ Media & Entertainment	-24.87%	13,144

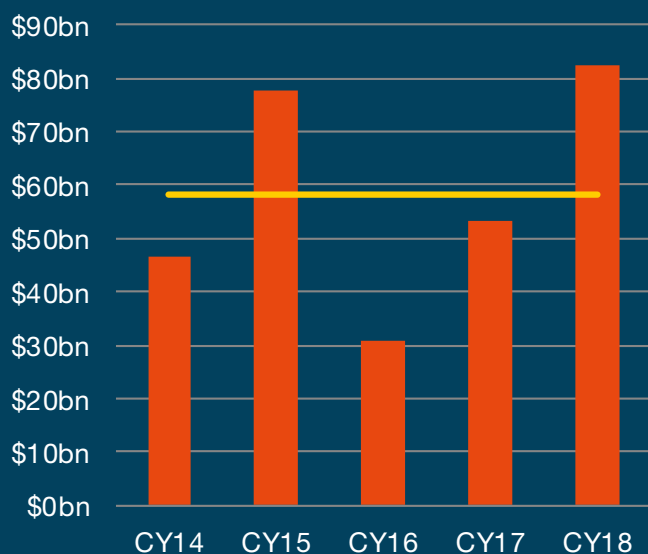
M&A ruled supreme within Australia in 2018

M&A ruled supreme in Australia in 2018 with deal value volumes at an eight year high and announced proposed deals topping over \$200bn during a volatile year for global and domestic equity markets. During CY18 there was over \$80bn in announced inbound takeover offers for ASX listed companies (or 84 offers in total inclusive of smaller companies) as predators flocked to the Australian bourse.

The usual suspects were involved in announced transactions including a large number of PE firms and industry competitors undertaking consolidation. 2018 did however see a number of new acquirers and structures making their presence known in the market. Such examples include the largest Australian Industry Super Fund in Aus Super becoming an active participant in M&A as the fund launched multiple hostile takeover offers on Healthscope and Navitas in partnership with management and/or private equity.



Value of announced inbound ASX listed takeover bids in CY18



— Total value of announced ASX takeovers
— 5 Year average

Source: FactSet and Shaw and Partners

Jonathon Higgins

Analyst

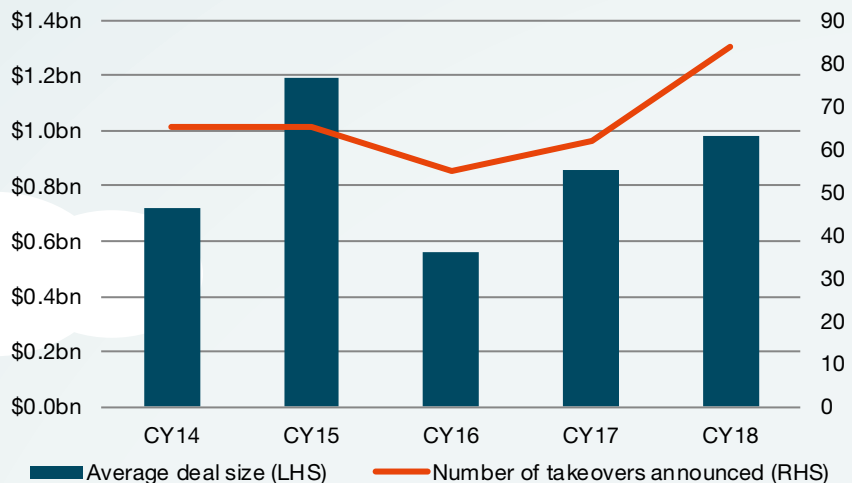
M&A ruled supreme within Australia in 2018

This is a new phenomenon within Australian equity markets and looks to be multiple years behind similar strategies employed by large funds in Canada and Northern Europe. Typically, industry funds in Australia have handed out mandates and been passive investors of PE firms in the search for such M&A returns.

Will the pool of constantly growing mandatory super fund contributions cause our investment industry to morph substantially continuing a growing theme of internalisation? Inbound interest from Asian investment funds in takeovers of Australian companies continued a recent thematic with multiple bids for infrastructure and critical assets such as APA group and AWE demonstrating interest in Australia as a source of sustainable returns.

Takeovers and movement of primary exchange listings overseas continued a recent thematic of removing capitalisation from Australia's largest indices (ASX 200) as our index concentrated further and popular multi-billion dollar companies were lost. This included companies such as Amcor and Westfield (now merged with Unibail Rodamco). Coles was demerged from Wesfarmers during the year with this being the largest spinoff in ASX history. This resulted in the streamlining of both vehicles into more pure play businesses and begun what could be a process of breaking up one of the last great conglomerates in Wesfarmers.

Frequency and size of ASX takeovers announced in CY18

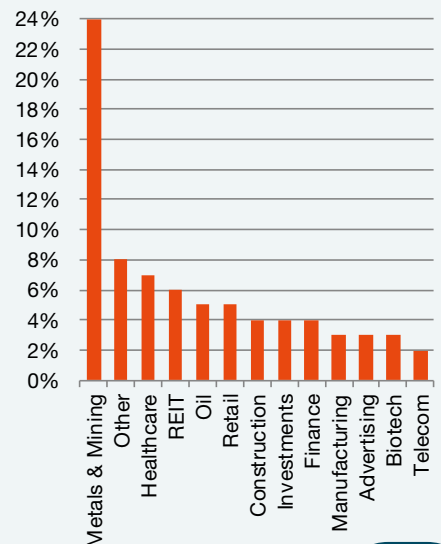


Source: FactSet and Shaw and Partners

Sectors that had inbound interest were those that were looking pretty beaten up from earnings downgrades whilst still enjoying strong long term structural demand dynamics such as Healthcare and Telecommunications. Whilst the largest number of transactions by number was in Metals and Mining, continuing from 2017, as strong balance sheets and a commodity price resurgence resulted in miners and metals producers getting the cheque book out.

Inbound takeovers were the place to be if timed correctly and represented a major source of returns for investors during CY18 with the median premium paid expanding to ~30%. According to BCG (2018 Mergers & Acquisitions Report), acquisitions are being done at increasingly higher multiples than at any time in the last 30 years globally. Equity market multiples have expanded as easy money reigned supreme and global equity multiples rose. Compared with the global M&A performance, on average acquirers were paying ~6% higher premiums in Australia than globally.

Announced M&A by sector on the ASX in CY18 irrespective of size



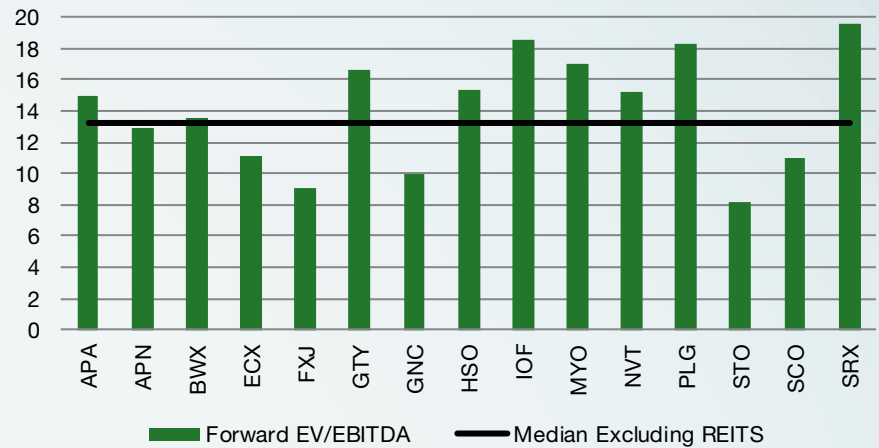
UNIBAIL-RODAMCO-WESTFIELD

2018

2018

According to FactSet Data and implementation documents, the median EV/EBITDA of takeover offers made was at ~13x (excluding REITs) and excluding any market disturbance was at an ~30% premium to the broader market. The median EV/EBITDA multiple for announced takeover offers domestically was at a ~9% discount to globally announced M&A. Lower multiples paid contrasted with higher premiums point towards the apparent favourable equity valuations in Australia when compared with global averages.

Forward earnings multiple proposed to be paid for inbound ASX listed takeovers



Source: FactSet and Shaw and Partners. EV/EBITDA = Enterprise Value / Earnings Before Interest Tax Depreciation and Amortisation



We see a number of industries as having an above average chance of undertaking industry consolidation or becoming targets themselves.

- Financial services – Driven by Royal Commission outcomes on business models, disruption of vertically integrated models and major bank aligned wealth managers being sold or demerged;
- Resources, Metals and Mining – Driven by the strongest corporate balance sheets in history, continuing commodity price strength and earnings need to be replaced from multi-year structural divestments undertaken;
- Healthcare – The increased possibility of an incoming Labor government is likely to increase public healthcare spend, altering the economics of the industry both publicly and privately;
- Aged Care – Public providers are likely to bear the brunt of similar commission outcomes to the Financial Services Royal Commission. Public providers remain likely the best operators in an industry with a structurally strong demand profile at what appear to be cheap multiples;
- Real Estate Investment Trusts – This sector is quickly losing ASX listed participants, however the appetite for long duration returns across a sector trading below five year averages may continue the sector's attractiveness to possible acquirers; and
- Retail – Conditions remain tough in this segment and consolidation opportunities across customer bases remain. Trading on single digit multiples, there is significant earnings uplift available to companies that can mesh together customer bases and unlock cost synergies.

Whilst it is inadvisable to rely on M&A to underwrite investor returns, it does remain a source of ample alpha in the Australian market if employed correctly with the correct timing. We see M&A as a continuing thematic in Australian equity market for a number of reasons, which include:

- Structural changes to industries driven by regulation
- Continuing access to low cost borrowing and investment bank/credit markets appetite for financing
- Depreciating AUD
- Strong corporate balance sheets;
- Lack of domestic growth forcing required industry consolidation for growth in certain industries
- Comparable value of domestic equities when compared with overseas counterparts (in particular the USA).

Early CY19 indications are for a continuing thematic of volatile equity markets, depreciating currency and the most depressed East Coast housing market in a decade. Underlying economic growth remains buoyant, inflation benign and unemployment low. However this may create the perfect environment for a continuation of a buoyant M&A environment in Australia in CY19.

19

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Martin Crabb

Chief Investment Officer



Franking credits and corporate balance sheets

With a Federal Election likely to be held in May 2019, and with the Australian Labor Party well ahead in the polls, investors are likely to focus on the ALP's policy regarding the utilisation of franking credits amongst those investors not paying tax.

The reduction in value that this implies has lead some companies to consider accelerating the distribution of those franking credits ahead of any change in government policy. We have studied listed companies that have a franking account surplus and balance sheet capacity to undertake a distribution of those credits to shareholders via a distribution or other capital management initiatives.

Australian listed companies have a total franking balance of \$49.8bn, which is capable of paying a fully franked dividend of \$166bn. This is against a market capitalisation of \$1.8 trillion, so this equates to 9.1% of the value of Australian listed companies. Note that this figure includes over \$15bn for BHP alone, which will be significantly lower following the recent buyback and dividend. Excluding BHP, the balance is \$34.7bn, the dividend is \$115.5bn and the value is 6.7%.

The listed companies that own a banking licence have a franking account balance of \$8.7bn against a market cap of \$419.6bn, or just over 2%. These companies generate mostly Australian income and can therefore pay franked dividends from current earnings. Excluding these companies from the analysis, the surplus franking account drops to \$25.9bn.

Looking at which companies are in a good position to pay out their excess franking credits, Woodside Petroleum (WPL), Woolworths Group (WOW) and Fortescue Metals (FMG) stand out. WPL has \$2.6bn of franking credits and only \$6.1bn of debt against a market value of \$31bn. Amongst small caps, Energy Resources of Australia (ERA) has net cash of \$395m, a franking balance of \$234m and a market cap of only \$124m.

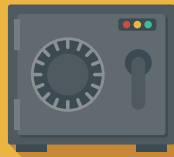
Australian listed companies have a total franking balance of \$49.8bn, which is capable of paying a fully franked dividend of \$166bn.

TOP TEN FRANKING ACCOUNT BALANCES (excluding Banks and BHP)

Code	Company Name	Market Cap	Franking	Net Debt	Franking / Market Cap
WPL	Woodside Petroleum	31,033.43	2,650.95	6,069.17	8.5%
WOW	Woolworths Group Ltd	39,259.03	2,610.00	1,477.00	6.6%
FMG	Fortescue Metals Grp	14,317.19	2,267.57	4,211.95	15.8%
WES	Wesfarmers Limited	36,305.57	978.00	3,315.00	2.7%
CTX	Caltex Australia	6,869.75	936.08	814.40	13.6%
TPM	TPG Telecom Limited	6,012.22	711.00	1,907.90	11.8%
REH	Reece Limited	5,540.93	573.15	-539.89	10.3%
STO	Santos Ltd	12,102.12	520.54	3,467.37	4.3%
SOL	Soul Pattinson (W.H.)	6,291.31	514.09	-568.85	8.2%
RHC	Ramsay Health Care	11,761.13	510.88	3,181.46	4.3%

Steve Anagnos & Cameron Duncan

Co-Heads, Income Strategies

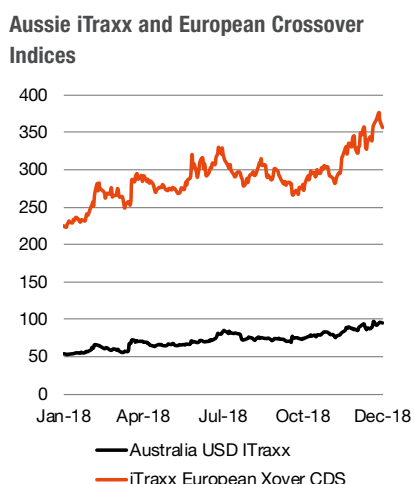


Review and outlook for credit markets



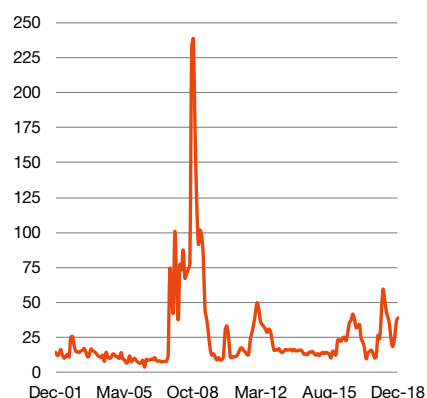
2018 has been a challenging year for a large part of the global credit market, largely as a result of the transition away from quantitative easing to a regime of quantitative and interest rate tightening.

This can be observed by the continual widening in credit spreads both domestically and abroad as seen by the Aussie iTraxx and European Crossover (the 75 most liquid sub-investment grade securities) Indices below, where tighter credit conditions and a higher cost of funds was reflected in Australian iTraxx 5 year CDS spreads, almost doubling in 2018. This together with other factors has the potential to impact markets into 2019.



While CDS spreads are wider, there are no real signs of a crisis like the 2008/9 “Credit Crunch”, with USD Libor OIS indicating a willingness of banks to still freely lend to each other.

USD LIBOR OIS



The outlook for credit is finely balanced and will be driven by creditworthiness and fundamentals on the one hand and technical factors, liquidity and asset allocation on the other.

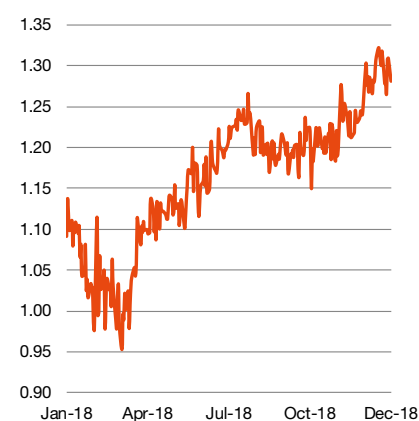
Credit fundamentals are healthy across investment grade and high yield issuers, while the macro backdrop in the US continues to be positive. This is offset by declining demand and sentiment as interest rates rise and we approach the end of the credit cycle.

Solid credit metrics and low default rates persist which we will continue to monitor during the year.

A number of global commentators expect that new investment grade issuance is expected to decline between 5-10% in 2019 after falling by nearly 10% in 2018. About 20% of issuance this past year has been to finance M&A transactions. This is expected to fall next year as higher all-in yields, increased equity volatility and recent tax changes are likely to deter such activity.

Australian corporate cash spreads were less impacted, but still wider over 2018.

AUD BBB yield – AUD SWAP 5 Year



A key driver in Australian credit markets is the recent APRA paper released in November 2018, suggesting that the Australian Banks should raise an additional A\$75 billion of Tier II bonds to meet 'too big to fail' capital requirements. This is in order to comply with global 'total loss absorbing capital' rules intended to limit future taxpayer bail-outs by 'bailing in' private investors.

The release of this paper triggered a sharp widening of the Australian Tier II bond spreads. This may represent three times the \$25 billion of Australian major bank Tier II debt sold over the past four years.

In recent weeks there has been concern that the global market may not be large enough to raise up to 7% of its risk weighted assets via this type of debt. Other alternatives may be considered including Covered Bonds (where the debt is secured by a pool of mortgages) and Tier II debt.

Australian Hybrid securities were very resilient despite weaker bank equity prices and performed strongly as an asset class in 2018.

Solactive Aust Hybrid Securities Index (Net)



The risk reward structure of these securities appealed to a wide range of institutional and retail investors that stayed away from pure equity risk, whilst seeking better than cash like returns.

The focus in 2019 is to monitor the quantitative tightening that will take place in the credit markets, consider the sector versus equities as a diversifier and also focus on the idiosyncratic risk persisting within region, sectors, industries and where the investments sit in the capital structure.

Data source: Bloomberg

Stuart Baker

Senior Analyst – Oil and Gas

Can Saudi Arabia rescue the oil price?

A blue line graph starts at the top left and trends downwards with some minor fluctuations. The line ends in a stylized fuel nozzle, from which a single drop of oil is falling. The background is a textured orange and yellow pattern with large, faint downward-pointing arrows.

Brent oil prices lost 50% in 6 weeks beginning early November, an unprecedented collapse; undoing the recovery underway since the last peak cycle collapse in 2015.

WHAT WENT WRONG?

The seeds of the latest collapse were sown mid-year, as key producers with spare capacity increased production in anticipation of a material loss of supply from November, when USA sanctions were meant to take effect on Iranian output.

Oil traders anticipated up to 1 MMBopd of supply could be at risk, and in the lead-up, Brent oil prices approached US\$90/bbl. However, Saudi Arabia, Russia and onshore USA production ramped-up to fill the hole, then in early November, US congress granted waivers to 8 countries with refining capacity dependent on Iranian crude. Overnight, the sanctions were rendered ineffective, Iranian output had been only minimally impacted, and once again oil-markets faced over-supply.

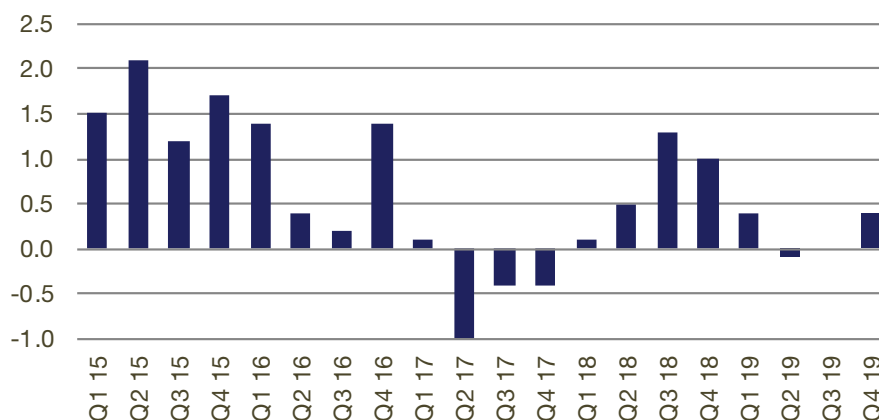
The causes of the subsequent oil price collapse are the same as those behind every other, and that is over-supply. Movements in supply are more dramatic and faster than incremental changes in demand. The rise of EV's and a slowing global economy do not help, but these changes are small in any year relative to the amount of supply that can be dialled up or down due to either market forces, or OPEC actions.

To put figures around this, the difference in demand between strong global growth and a recession is about 0.5-0.7 MMBopd. In contrast, in the past 5 years we have seen OPEC ramp-up or cut supply by 1-1.2 MMBopd. The 2015 oil collapse cost the USA 1MMbopd of output, but the recovery since has added 2MMbopd, in sync with rising oil prices. Civil unrest has affected output in many countries that were once important producers, most visibly in Venezuela where output has halved in 3 years to 1.25 MMBopd currently, with the remaining supply at risk. Thus in trying to gauge when there will be a recovery, we need to remain alert to the supply side from these three key regions.

CURRENT STATE OF PLAY

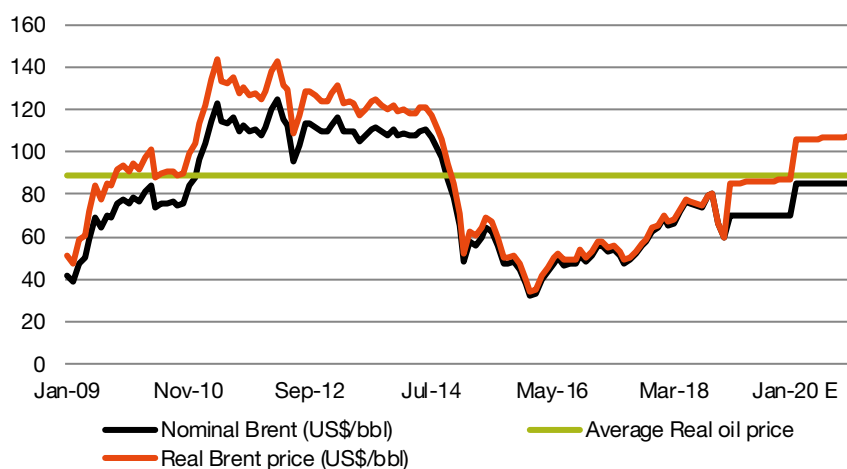
The December 7-8 OPEC meeting promised cuts including Russia of 1.2 MMBopd in total, to begin from January 1 2019. It's too early to assess the level of compliance, but should OPEC make good on its promised cuts, and assuming the latest demand and supply trends in line with December data, then oil markets should begin to tighten in the second quarter.

Quarterly incremental change in inventories (MMbopd)



Source: IEA Monthly Reports, OPEC Monthly, Shaw and Partners estimates.

Brent oil price in real & nominal terms and 10 year average price (US\$/bbl)



Source: NYMEX monthly Brent price, Shaw and Partners estimates.

The current state of play in key supply regions is: (1) OPEC and Russia to reduce production from the 33 MMBopd November level to 31.8 MMBopd beginning January 1, 2019, (2) Production in Venezuela is likely to continue declining in the wake of presidential elections locking in the status quo and (3) US production and activity levels are showing signs of plateauing, due to financial pressures directly related to low oil prices. Slowdown in global growth is anticipated and we assume demand in 2019 is lower than both 2018 and 2017, but demand side effects tend to be incremental.

OUR VALUATION APPROACH

With Brent oil prices currently less than US\$60/bbl, our 2019 estimate of US\$70/bbl looks at risk, and will require evidence of market rebalancing from 2Q to be realised. However, our stock valuations and recommendations are under-pinned by DCF methodology and requires a long-term oil price, not just a one year estimate.

We use a "through the cycle price" which we think reflects the ongoing cost of staying in production and replacing reserves. We assume US\$85/bbl. Lower than this, investment shrinks and eventually so does supply. Higher than this and the industry becomes super-profitable and high-cost supply is stimulated leading to over-supply. By way of comparison, the average nominal Brent oil price over the past decade is US\$79.6/bbl, and in real terms US\$88.9/bbl. Real and nominal price history, and output forecasts for 2019 and 2020 are shown in the figure above.

STOCK SELECTION

Our preference is for low-cost producers that are cash-flow positive at low oil prices and have balance sheets that can support re-investment through the oil price cycle. Woodside ticks all these boxes, while Oil Search comes a close second and we rate both stocks a Buy.

Shaw Managed Accounts

Shaw Managed Accounts are a sophisticated investment and reporting platform incorporating advanced features to assist in the management of your overall investment strategy and portfolio.

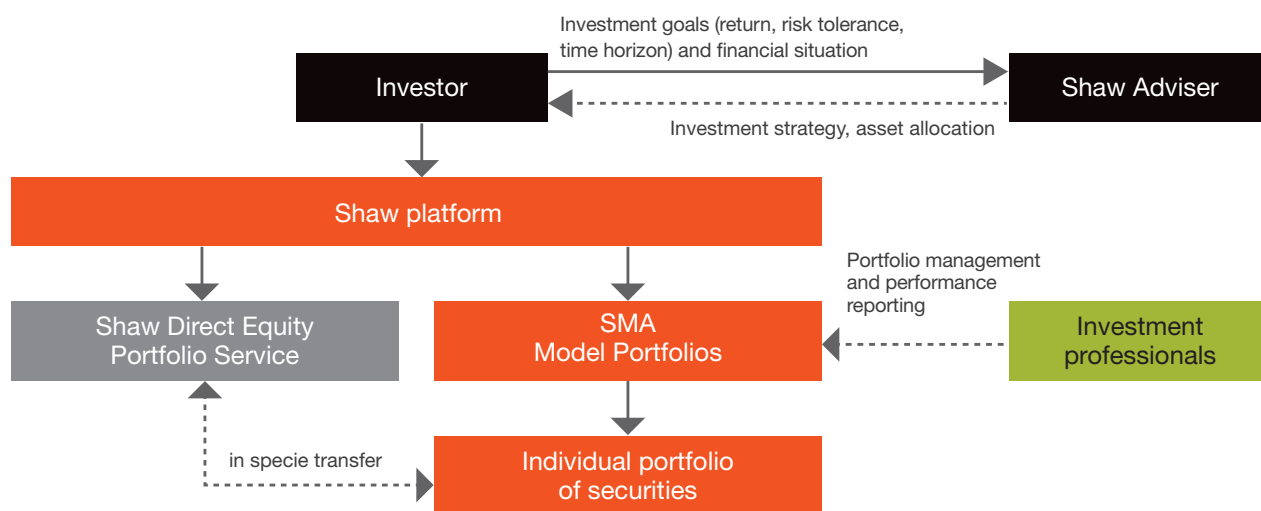
Shaw Managed Accounts are established and offered within the registered managed investment scheme known as the Separately Managed Accounts. Each investor has a separate “account” to which their investments are allocated.

Your account can be constructed by using a range of available investment strategies (referred to as Model Portfolios) that you can select from the investment menu together, with your Shaw and Partners adviser.

Once you decide which Model Portfolios are best suited to your investment needs and objectives, Shaw and Partners will purchase securities to be included in your account so that it reflects the Model Portfolio, or a combination of Model Portfolios.

The Model Portfolios are managed in a disciplined and consistent manner; overseen by a dedicated team of investment professionals with many years of experience in securities markets.

With Shaw Managed Accounts, not only are you the beneficial owner of the portfolio (and shares), you will also enjoy the ownership benefits (such as dividends and franking credits) and have the ability to see the exact make up and market value of the portfolio at any time, via our online service.



Shaw Managed Accounts are positioned between Individually Managed Portfolios and Managed Funds. They offer increased levels of control and transparency, agility and tax optimisation.

Benefits of Shaw Managed Accounts	Professionally managed	Reduced tax administration	Flexibility
Lower trading costs	Portfolio transparency	Performance monitoring	Dividend reinvestment
Powerful online reporting tools	Dividend and franking credit benefits	In specie transfers	No inherited liability
Safe custody of investments	Beneficial ownership	Tax optimisation	Margin Lending capability

Shaw Managed Accounts

Portfolio Performances – December 2018

		1 Mth	3 Mth	6 Mth	1yr	Inception
Shaw Income Goal Portfolio <i>Objective: RBA Cash +3%</i> <i>Inception: Sep-17</i>	Total Portfolio Return	-0.46%	-4.19%	-2.11%	0.04%	3.57%
	Portfolio Objective	0.38%	1.14%	2.29%	4.59%	6.10%
	Excess v Objective	-0.84%	-5.33%	-4.40%	-4.56%	-2.53%
Shaw Balanced Goal Portfolio <i>Objective: RBA Cash +4%</i> <i>Inception: Sep-17</i>	Total Portfolio Return	-0.75%	-5.55%	-3.74%	-0.28%	4.50%
	Portfolio Objective	0.47%	1.39%	2.80%	5.64%	7.50%
	Excess v Objective	-1.22%	-6.94%	-6.54%	-5.92%	-3.01%
Shaw Growth Goal Portfolio <i>Objective: RBA Cash +5%</i> <i>Inception: Sep-17</i>	Total Portfolio Return	-1.92%	-10.36%	-8.01%	-1.61%	6.03%
	Portfolio Objective	0.55%	1.65%	3.32%	6.70%	8.92%
	Excess v Objective	-2.48%	-12.00%	-11.33%	-8.30%	-2.89%
Debt Securities Income Portfolio	Total Portfolio Return	0.76%	1.39%	2.23%	3.27%	3.30%
	<i>Inception: Sep-17</i>					
Hybrid Income Portfolio	Total Portfolio Return	1.18%	0.77%	3.10%	4.40%	7.10%
	<i>Inception: Sep-16</i>					
Australian Equity (Large Cap) - Income	Total Portfolio Return	-0.30%	-7.36%	-6.46%	-3.85%	1.50%
	<i>Inception: Sep-17</i>					
Australian Equity (Large Cap) - Growth	Total Portfolio Return	-0.61%	-12.51%	-10.93%	-1.62%	6.78%
	<i>Inception: Sep-17</i>					
Australian Equity (Large Cap) - Core	Total Portfolio Return	0.81%	-6.50%	-7.18%	-1.15%	9.55%
	<i>Inception: Sep-16</i>					
Australian Equity - Small and Mid Cap	Total Portfolio Return	-3.39%	-13.96%	-12.69%	-7.72%	1.13%
	<i>Inception: Sep-17</i>					
International Equity Portfolio	Total Portfolio Return	-4.47%	-10.63%	-4.90%	-1.92%	5.27%
	<i>Inception: Sep-17</i>					
Shaw Liquid Alternatives Portfolio	Total Portfolio Return	-0.32%	-3.25%	n/a	n/a	-3.53%
	<i>Inception: Aug-18</i>					

Our Preferred Stocks



Commonwealth Bank of Australia (CBA) provides banking and financial services. It offers banking and financial products and services to retail, small business, corporate and institutional clients.



Macquarie Group (MQG) offers banking, financial advisory, investment and funds management services. The company offers financial advice, cash management, wealth management and private banking, life insurance, securities brokerage, corporate debt financing, real estate funds management, real estate development financing, investment funds management and foreign exchange services.

BHP

BHP (BHP) is an international resources company. The company's principal business lines are mineral exploration and production, including coal, iron ore, gold, titanium, ferroalloys, nickel and copper concentrate, as well as petroleum exploration, production, and refining. Dually-listed company with BLT LN.



Fortescue Metals Group (FMG) operates as an iron ore production and sea-borne trading company. It is engaged in the mining of iron ore from its Cloudbreak and Christmas Creek mine sites; and the operation of an integrated mine, rail and port supply chain. The company's projects include Chichester Hub, Solomon Hub, Herb Elliott Port and Rail Expansion.



Oil Search

Oil Search (OSH) explores for and produces gas and oil through operations in Papua New Guinea. The Company's activities are located in the Papuan Highlands which include the Kutubu, Hides, and Gobe oil and gas projects.



Woodside Petroleum (WPL) is an Australian based oil and gas exploration and production company. Key assets are the Pluto, North West Shelf and Wheatstone LNG projects offshore WA. Oil is produced from the Enfield and Vincent FPSO's. Exploration is underway internationally offshore West Africa, Myanmar, and onshore Canada. The company was founded in 1954 and is headquartered in Perth, Australia.



LendLease Group (LLC) designs, develops, and manages property and infrastructure assets. The Company constructs apartments, commercial buildings, government offices, retirement living, and educational facilities. LendLease serves customers worldwide.



Stockland (SGP) is a diversified Australian property group. The Group develops and manages retail centres, residential communities and retirement living assets with a focus on regional centres and outer metropolitan. Stockland also owns a portfolio of Office and Industrial assets. The company was founded in 1952 and is headquartered in Sydney, Australia.



Calix (CXL) is a multi-award-winning Australian technology company that is developing new processes and materials to solve global challenges. The core technology is a world-first, patented "kiln" built in Bacchus Marsh, Victoria that produces "mineral honeycomb" - very highly active minerals.



Flight Centre Travel Group (FLT) operates as a retail travel agency in Australia. The Company operates close to 1200 outlets throughout Australia and internationally including New Zealand, Hong Kong, South Africa, Canada and the United Kingdom. The Company's agencies and brands include Flight Centre, Travel Associates and Student Flights.



IVE Group (IGL) engages in the provision of communication solutions. Its services include creative services, personalised communications, print production, retail display, promotional merchandising, third party sourcing, logistics and fulfilment, managed solutions and data analytics.



Rhipe (RHP) provides software licensing, subscription management tools and cloud computing services. Its software vendors include Microsoft, Citrix, Datacore, McAfee, Red Hat, Trend Micro, Veeam, Zimbra and VMware. The company was founded in 2003 and is headquartered in Melbourne, Australia.

Commonwealth Bank (CBA)

Recommendation	Buy
Risk	Medium
Share Price (as at 17 January 2019)	\$73.21
Target Price	\$78.00
Analyst	Brett Le Mesurier

Share Performance Chart



Source: FactSet, Shaw and Partners

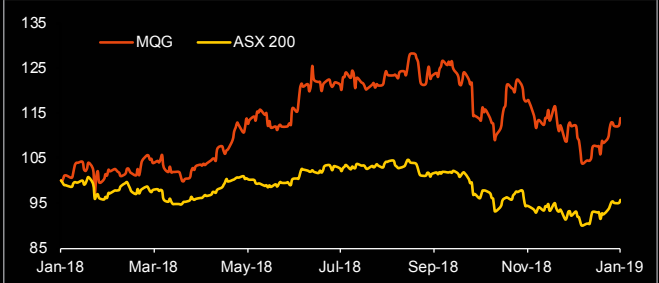
	1 mth	3 mth	12 mth
Relative Performance*	5.1%	8.8%	-9.2%

* Relative Performance is compared to the S&P/ASX 200 Index

Macquarie Group (MQG)

Recommendation	Buy
Risk	High
Share Price (as at 17 January 2019)	\$118.13
Target Price	\$130.00
Analyst	Brett Le Mesurier

Share Performance Chart



Source: FactSet, Shaw and Partners

	1 mth	3 mth	12 mth
Relative Performance*	3.5%	-0.2%	14.9%

* Relative Performance is compared to the S&P/ASX 200 Index

- In the first quarter of FY19, CBA continued the trend it displayed in its FY18 result, which is that home loans are allowed to grow but institutional loans are not. It's a simple wisdom aimed at increasing ROE when growth is problematic.
- As a consequence of this approach, credit risk weighted assets fell by 0.1% from 30/6/18 to 30/9/18. Total loan growth for CBA from 30/6/18 to 30/6/19 will probably be no more than 3%, with home loans being slightly higher than that figure.
- Further wisdom is shown in CBA's renewed interest in household deposits which can alleviate the competitive pricing pressures on new home loans. Household deposits have 2 advantages, being that they typically are cheaper than wholesale funding and are less subject to a sudden price increase, as we have seen with funding linked to bank bills.
- Such an interest in household deposits probably assisted CBA to improve its liquidity and net stable funding ratios during 1Q19.
- Net interest margin (NIM) decline offset the modest growth in average interest earning assets. The NIM decline is estimated to be 4 bps from 2H18 to 1Q19. The home loan repricing which was announced a few months ago should reverse this decline. This would provide the basis for some growth in net interest income from 1Q19 to 2Q19.

- MQG's revenue has been on an upward trajectory for some time. Most recently, there's been acceleration in this trajectory with the causes being more revenue from investments and trading.
- Additionally, MQG has been increasing its investments over the past 2 years and has had a noticeable uplift in the returns on those investments. MQG is expected to earn an average return of 23% p.a. on these investments in FY19 and has earned 22% over the last 4 years.
- MQG announced that the recent Quadrant sale is expected to increase its profit by approximately 5%, being \$150m in FY19. MQG acquired its interest in Quadrant Energy when it bought Apache's Western Australian oil and gas assets in a consortium involving Brookfield Asset Management and private equity funds in April, 2015. The deal size was US\$2.1bn.
- It appears that the Quadrant investment would have provided a return of at least 40% in FY19. This helps explain how MQG could average a 22% p.a. return on its investments over the past four years.
- However, we should not expect such returns to continue in perpetuity as MQG's revenue is highly correlated with the health of the financial markets.
- MQG has a tight capital position which can be improved by a reduction in equity investments and the continuation of the trend of higher future profits.

Forecasts

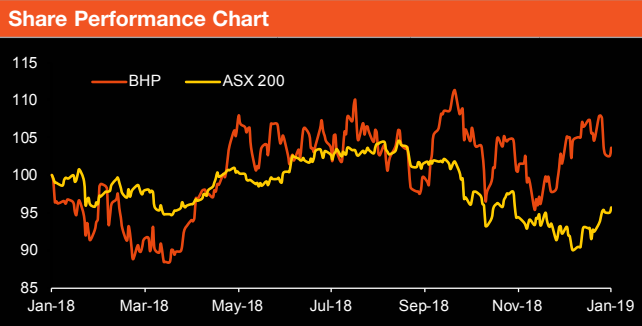
YE 30-Jun	FY18	FY19E	FY20E
Earnings cps	530.6	577.8	606.4
Dividends (AUD) cps	431.0	433.5	454.8
PE x	13.7	12.5	12.0
Yield %	5.9%	6.0%	6.3%
Franking %	100%	100%	100%

Forecasts

YE 31-Mar	FY18	FY19E	FY20E
Earnings cps	758.1	853.4	894.7
Dividends (AUD) cps	525.0	590.3	622.2
PE x	13.6	13.6	12.9
Yield %	5.1%	5.1%	5.4%
Franking %	45%	45%	45%

BHP (BHP)

Recommendation	Buy
Risk	Medium
Share Price (as at 17 January 2019)	\$33.24
Target Price	\$40.00
Analyst	Peter O'Connor



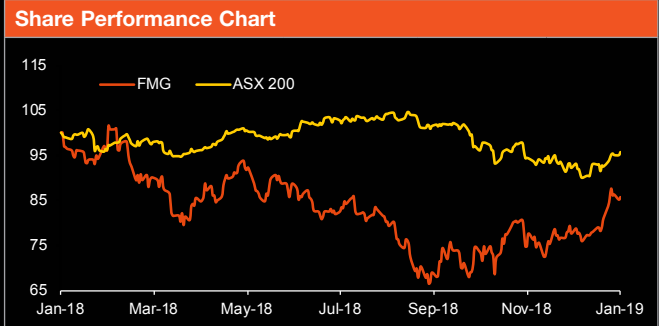
Source: FactSet, Shaw and Partners

	1 mth	3 mth	12 mth
Relative Performance*	-2.0%	-2.3%	6.9%

* Relative Performance is compared to the S&P/ASX 200 Index

Fortescue Metals (FMG)

Recommendation	Buy
Risk	High
Share Price (as at 17 January 2019)	\$4.65
Target Price	\$5.60
Analyst	Peter O'Connor



Source: FactSet, Shaw and Partners

	1 mth	3 mth	12 mth
Relative Performance*	8.9%	19.7%	-11.7%

* Relative Performance is compared to the S&P/ASX 200 Index

Earnings tailwinds following record capital management

- BHP's recent outperformance – underpinned by a record level of capital management initiatives totalled ~US\$10bn over the past several months – is expected to continue into 2019 assisted by commodity tailwinds most notably in the oil division.
- Capital management is projected to continue – albeit at a more normal rate – with a 1H19 dividend of around ~US\$3-3.5bn expected to be declared in February 2019. Beyond the regular dividend stream, BHP is projected to yield ~US\$3-5bn of surplus cashflow in each of the next three years which could be directed to on market buy backs. In this case, and given the deep price discount of BHP's UK share price (~14%), we would expect any further buy backs to be undertaken in the UK.
- Earnings tailwinds – The earnings trend for BHP will likely be higher as FY19 progresses with the current gap between consensus forecasts and spot scenario analysis currently around 10%. The closing of this gap/discount during 2H19 will likely support further share price moves towards our \$40/share target price.
- Operational leverage and latent capacity upside – there still remains significant potential to add low capital intensity growth via unlocking latent capacity in each of iron ore, copper, oil and coal and focussing on lowering unit costs especially in Australian coal and copper.
- Long term growth pipeline – beyond the current earnings outlook BHP continues to restock the long term growth pipeline, with the most recent additions in the high margin US Gulf of Mexico oil unit.

Forecasts			
YE 30-Jun	FY18	FY19E	FY20E
Earnings cps	167.8	164.9	162.8
Dividends (AUD) cps	152.2	275.2	135.6
PE x	14.9	14.3	14.5
Yield %	4.7%	8.4%	4.1%
Franking %	100%	100%	100%

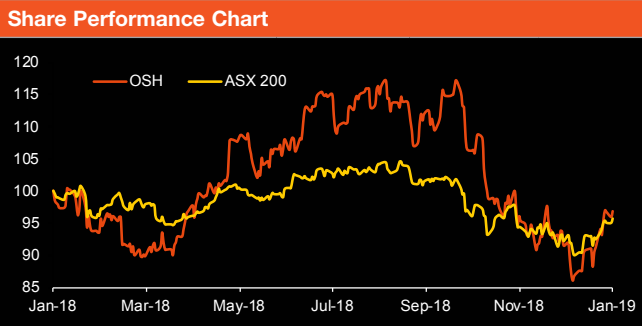
Tailwinds continue into 2019

- Recent FMG outperformance is likely to extend into 2019 with recent industry supply issues (RIO) potentially providing a handy price tailwind.
- FMG should benefit not least because of firmer demand for its product suite, perhaps nudging FY shipments towards the high end of guidance, or that price of the 58% product range will continue to outperform the high grade segment.
- Additional catalysts/triggers for FMG include – December quarter QPR (31 January) and 1H FY19 earnings result (20 February).
- Importantly the DQ report will provide sufficient granularity (selling price US\$/t, price discount, costs, balance sheet etc.) to determine that the quarter and 1H result will likely be better than most people are/were forecasting.
- Who would have thought/forecast that FMG would outperform the Australian market in Q4 2018? FMG added 27% vs 58% Fe price (up 15%) and the Australian market down 4% for a net out performance of ~30%. We expect that the shift in steel maker buying patterns, since March 2018 when the move started back towards “value in use” as opposed to “productivity” will continue against a back drop of a low grade segment that has ~25mt less supply available (given 2018 curtailments) and now RIO's FM on another ~30mt. Worth noting that events like this don't last for extended periods but markets/price can be disrupted for days/weeks and maybe months.

Forecasts			
YE 30-Jun	FY18	FY19E	FY20E
Earnings cps	34.6	38.0	42.7
Dividends (AUD) cps	24.1	34.3	38.7
PE x	9.4	8.5	7.5
Yield %	5.8%	7.7%	8.7%
Franking %	100%	100%	100%

Oil Search (OSH)

Recommendation	Buy
Risk	High
Share Price (as at 17 January 2019)	\$7.75
Target Price	\$10.20
Analyst	Stuart Baker



Source: FactSet, Shaw and Partners

	1 mth	3 mth	12 mth
Relative Performance*	5.7%	-8.3%	-1.0%

* Relative Performance is compared to the S&P/ASX 200 Index

Woodside Petroleum (WPL)

Recommendation	Buy
Risk	High
Share Price (as at 17 January 2019)	\$34.05
Target Price	\$43.70
Analyst	Stuart Baker



Source: FactSet, Shaw and Partners

	1 mth	3 mth	12 mth
Relative Performance*	8.3%	-7.1%	1.6%

* Relative Performance is compared to the S&P/ASX 200 Index

Alaska drilling could trigger a re-rating

- OSH's PNG LNG project has performed beyond design rates and expectations and turned into a solid cash-flow generator, providing the capital base and momentum for expansion.
- Planning for additional three LNG processing trains is advanced and while not yet sanctioned, it's hard to see what could impede future development. Gas reserves have been established and there is alignment between super-major partners (Exxon and Total) and the Government regarding project scope and fiscal terms. Broadly, the three LNG trains would approximately double LNG production from ~2024-2025.
- OSH's strategy to broaden its activities outside of PNG will be tested in early 2019, with the planned drilling of 2 wells on its "Pikka" prospect, onshore in the Alaskan "North slope". This is a prolific oil and gas region and OSH has bought into a multi-hundred million barrel discovered oil resource. The appraisal drilling campaign aims to increase the resource and move to a commercial phase. Development time-lines are much quicker than for LNG, and it's possible this project could deliver substantial oil production volumes from ~2022. We think, wrongly, that the equity market is ambivalent on this potential development and discounting the upcoming drilling campaign. Drilling success could drive a resource / reserve upgrade and would justify a re-rating.

Forecasts			
YE 31-Dec	FY17	FY18E	FY19E
Earnings cps	19.8	24.7	37.8
Dividends (AUD) cps	12.4	15.7	26.5
PE x	30.8	21.9	14.3
Yield %	1.6%	2.2%	3.5%
Franking %	0%	0%	0%

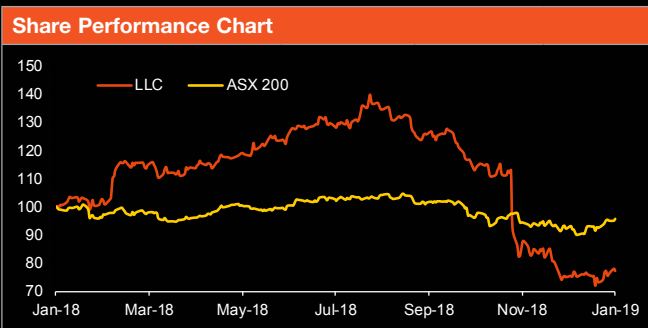
Resilient through the oil cycle

- Despite the late year oil price collapse, WPL should still record strong second half 2018 earnings, cashflow and dividend growth, due to strong oil prices in 3Q and lags in LNG prices. Fiscal discipline since the 2014 oil price collapse insulates WPL from low oil prices and we estimate profit break-even in 2019 to be ~US\$26/bbl.
- Debt levels are not onerous. We estimate net debt at year end 2018 to approximate US\$2.6bn. WPL has sufficient balance sheet strength and liquidity to maintain the 80% dividend payout ratio, as well as prepare for the next suite of developments.
- WPL is the only major domestic energy company with production growth in 2019 and 2020, due to Wheatstone LNG operating at capacity and expected completion of the Greater Enfield project in mid 2019. Longer dated projects have progressed too, with Pluto2 expansion and the Senegal SNE oil project both entering detailed design phases in December 2018. We anticipate oil production from SNE in 2022 and Pluto2 mid decade.

Forecasts			
YE 31-Dec	FY17	FY18E	FY19E
Earnings cps	121.5	154.4	205.5
Dividends (AUD) cps	127.8	172.1	230.4
PE x	21.3	15.8	11.9
Yield %	3.8%	5.3%	6.7%
Franking %	100%	100%	100%

Lendlease (LLC)

Recommendation	Buy
Risk	Medium
Share Price (as at 17 January 2019)	\$12.13
Target Price	\$18.31
Analyst	Peter Zuk



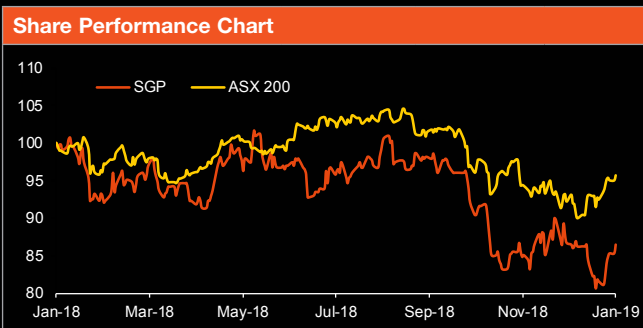
Source: FactSet, Shaw and Partners

	1 mth	3 mth	12 mth
Relative Performance*	2.2%	-32.6%	-22.9%

* Relative Performance is compared to the S&P/ASX 200 Index

Stockland (SGP)

Recommendation	Buy
Risk	Low
Share Price (as at 17 January 2019)	\$3.70
Target Price	\$4.69
Analyst	Peter Zuk



Source: FactSet, Shaw and Partners

	1 mth	3 mth	12 mth
Relative Performance*	0.3%	-4.9%	-13.1%

* Relative Performance is compared to the S&P/ASX 200 Index

Deep value has emerged. Resolution of engineering division is a catalyst

- We remain attracted to LLC despite the recent aggressive sell-off following the recently announced \$350m after-tax impairment charge taken against its Engineering business. The Engineering business has been a drag on LLC's overall Construction division margin for quite some time, and investors are now at the point where they would prefer to see this division sold or spun-out of the broader business.
- The Investment division remains strong, and LLC's track record in growing external assets under management (AUM) is quite impressive – with AUM now at \$30.1bn, which provides predictable annuity income.
- LLC's leverage to the global urbanisation thematic remains strong. Its development workbook stands at \$71.1bn, which should provide not only "one off" development profits, but also facilitate growth in external AUM.
- We believe the market is unfairly capitalising expectations of further impairments in perpetuity. We see deep value in the stock, but acknowledge that a share price re-rating may not occur until the outcome of LLC's strategic review of its Engineering business is complete.

Forecasts			
YE 30-Jun	FY18	FY19E	FY20E
Earnings cps	137.1	86.4	139.6
Dividends (AUD) cps	69.0	43.3	69.8
PE x	14.4	14.0	8.6
Yield %	3.5%	3.6%	5.8%
Franking %	0%	0%	0%

Sentiment working against it, but downside risk to its dividend is low

- Worth noting is that our existing FY19 FFO/share estimate of 37.5¢ is at the low end of guidance. SGP is guiding to 5-7% FFO growth in FY19, with our estimate reflecting ~5.2% growth.
- Stress testing our FY20 estimates – We currently show FFO/share of 38.6¢, being +2.9% growth on our FY19 estimates. Focusing on SGP's Residential business, if the division revisits the result of FY13 (which was its worst year for Residential earnings over the past 10-12 years), then our FFO/share would fall by ~26% to 28.6¢. This assumes Residential revenue of \$1,016m and EBITDA of \$180m (vs. \$1,891m and \$435m in FY18). This in turn also assumes that SGP maintains its capital employed in Residential rather than scaling back the business and redeploying that capital elsewhere.
- Slowly executing on its divestment strategy – To date, SGP has sold \$113m of Retail assets, against its target of \$400m. Proceeds can be used to keep buying back stock, given that it is trading at a 13% discount to NTA.
- While the stock is highly out of favour by the equities market, we see deep value in SGP. As we have written previously, a re-rating is likely reliant on positive newsflow that may not come until at least the Feb 2019 reporting season or possibly later. In the meantime, SGP offers an attractive forecast DPS yield of 7.6%, and we see little downside risk to it meeting its FY19 DPS guidance.

Forecasts			
YE 30-Jun	FY18	FY19E	FY20E
Earnings cps	31.6	32.8	33.7
Dividends (AUD) cps	26.5	27.6	28.6
PE x	12.5	11.3	11.0
Yield %	6.7%	7.4%	7.7%
Franking %	0%	0%	0%

Calix (CXL)

Recommendation	Buy
Risk	High
Share Price (as at 17 January 2019)	\$0.74
Target Price	\$0.90
Analyst	Darren Vincent

Share Performance Chart



Source: FactSet, Shaw and Partners

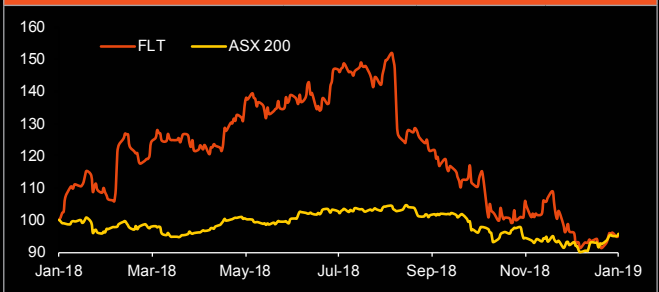
	1 mth	3 mth	12 mth
Relative Performance*	1.7%	4.8%	n/a

* Relative Performance is compared to the S&P/ASX 200 Index

Flight Centre (FLT)

Recommendation	Buy
Risk	Medium
Share Price (as at 17 January 2019)	\$44.11
Target Price	\$65.00
Analyst	Darren Vincent

Share Performance Chart



Source: FactSet, Shaw and Partners

	1 mth	3 mth	12 mth
Relative Performance*	-5.1%	-13.0%	-0.2%

* Relative Performance is compared to the S&P/ASX 200 Index

2019 is expected to build on the achievements of 2018

- In 2018 CXL delivered steady progress across its portfolio of products produced using its unique calcification technology. Based on the progress made, the simplicity of its technology, the validation its commercial MgO products provide and the substantial corporate and government interest in its pipeline products, we expect it will continue to deliver positive news flow through 2019. Below we discuss three of its unique products.
- ACTI-Mag for odour control – ACTI-Mag has been generating strong growth in a price competitive Australian market since 2013 with low customer churn. We had been looking for evidence that it could continue to expand into international markets. This came through in 2018 when CXL received its first purchase order from a West Coast US client. CXL also has multiple ACTI-Mag biogas trials underway in Thailand.
- BOOSTER-Mag crop protection – CXL has 3 Material Transfer Agreement's for BOOSTER-Mag with global crop protection companies. European trials continued through 2018 with highly encouraging results.
- Construction of CXL's LEILAC Project, a technology for capturing CO₂ released in cement and lime production, funded by the European Commission is under construction at Heidelberg Cement's Lixhe cement plant in Belgium. It is on time and budget for commissioning in April 2019. Initial results proving up, complete separation of CO₂ are expected shortly after that and evidence of longer term reliability is expected in 12 months.

Forecasts			
YE 31-Dec	FY18	FY19E	FY20E
Earnings cps	(3.1)	0.0	2.0
Dividends (AUD) cps	0.0	0.0	0.0
PE x	(25.6)	nm	38.7
Yield %	0.0	0.0	0.0
Franking %	0%	0%	0%

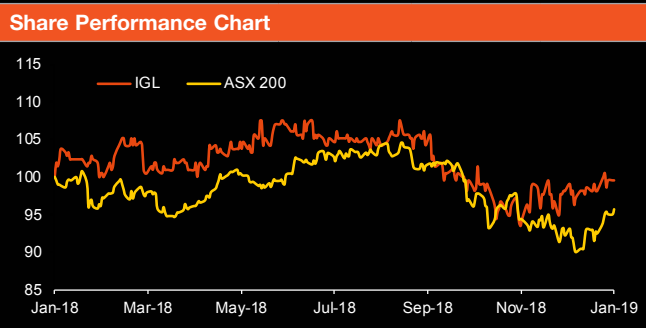
Strategic initiatives continue to be implemented

- FLT's shareprice has come back from a high of \$70.53 to \$44.11 over the last six months despite solid operational advancement continuing, which we see as likely to help underpin ongoing long term growth.
- In December 2018 FLT announced the acquisition of Casto Travel, a corporate travel provider based in San Francisco that generates US\$120m of transactions. The acquisition is significant in that it reflects the strength and confidence FLT now has in its US corporate business which is now delivering strong results from the US\$300bn market that provides long term growth potential, as does FLT's global corporate business which now accounts for half group earnings.
- FLT also announced in December that it had taken a 10 year lease on a hotel in Legian, Bali. The lease is significant in that it reflects ongoing implementation of FLT's vertical integration strategy designed to capture greater margin share where it knows it can consistently deliver travellers. FLT now has 22 properties under either lease or management rights.
- FLT report further merger and acquisition opportunities are being considered as it continues to target growth opportunities across key sectors and to boost productivity.
- Cost savings from FLT's transformation program are coming through and are expected to continue for the next few years. FLT reported 7% productivity gains with its 1H18 result an important signal that it is delivering on expectations re its business transformation programme which has tight cost control and the removal of unprofitable businesses at its core.

Forecasts			
YE 30 Jun (AUD)	FY18A	FY19E	FY20E
Earnings cps	261.7	291.1	312.3
Dividends cps	167.0	183.9	197.6
PE x	24.3	15.2	14.1
Yield %	2.6%	4.2%	4.5%
Franking %	100%	100%	100%

IVE Group (IGL)

Recommendation	Buy
Risk	Medium
Share Price (as at 17 January 2019)	\$2.17
Target Price	\$2.80
Analyst	Jonathon Higgins

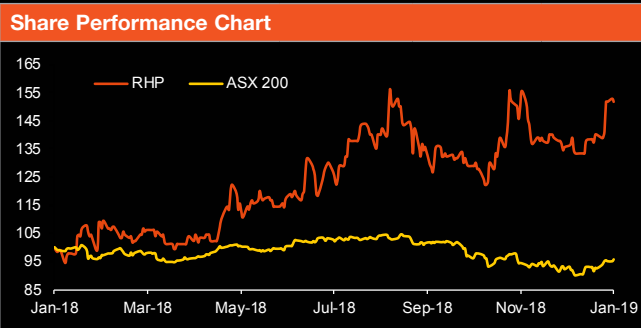


	1 mth	3 mth	12 mth
Relative Performance*	0.9%	1.4%	-1.4%

* Relative Performance is compared to the S&P/ASX 200 Index

Rhipe (RHP)

Recommendation	Buy
Risk	High
Share Price (as at 17 January 2019)	\$1.33
Target Price	\$1.55
Analyst	Jonathon Higgins



	1 mth	3 mth	12 mth
Relative Performance*	9.4%	14.5%	51.4%

* Relative Performance is compared to the S&P/ASX 200 Index

Via the stairs to a competitor

- IGL represents one of the cheapest ways to access a market leading business with Michael Porter 101 principles on the ASX, with the business being a market leader or top 3 competitor across all 10 products and services that the group offers.
- We see the returns profile of IGL somewhat similar to a REIT, with customers enjoying multi-year relationships (top 20 average over 7 years) and the majority of customers 60%+ utilising more than one product and service. This diversification of revenues across customers, geography, length of tenure, product type and industry results in a diversified and sustainable earnings stream.
- Earnings uplift for FY19 is underwritten by a modern asset base, quantifiable synergies from previous acquisitions undertaken and work already won and announced.
- Across this earnings stream we expect IGL's dividend yield of 8.6% fully franked in 2019 to support the current share price and likely exceed the cost of equity in the current climate.
- IGL has undertaken a path of undertaking required industry consolidation and removing excess capacity. Looking forward to FY20, the de-leveraging story and growing free cash flow profile, we hypothesise, will support capital growth.

Forecasts			
YE 30-Jun	FY18	FY19E	FY20E
Earnings cps	24.9	25.9	27.4
Dividends (AUD) cps	15.5	18.1	19.2
PE x	9.2	8.2	7.8
Yield %	6.8%	8.5%	9.0%
Franking %	100%	100%	100%

Public cloud has multi business potential

- Rhipe (RHP) is one of the largest wholesalers of cloud based products for software vendors within the Australian and New Zealand markets. Its key vendors include Microsoft, Symantic, Citrix among others. RHP has grown strongly and now has operations across a number of APAC countries and is leveraging its 'born in the cloud' competitive channel strategies.
- RHP represents one of the only direct ways to access ASX listed Microsoft leverage, with Microsoft putting in one of the top US listed share performances in CY18 and taking the mantle of largest company globally, as sales have transitioned to SAAS style earnings of which RHP is driving in APAC.
- RHP's share price has temporarily dislocated from an earnings upgrade cycle and strong overall momentum as volatile markets have ruled supreme. Against this backdrop RHP is trading on a cash adjusted forward PER of ~20x with conservative earnings guidance provided for FY19 (in our opinion)
- RHP has multiple growth irons in the fire with public cloud beginning to dominate across the business with the run-rate of growth in O365 CSP doubling from FY18 into FY19 and Azure (Amazon Web Services competitor) becoming increasingly more material. With Azure and CSP having the potential to be bigger businesses than existing private cloud segment of RHP, we see a positive multi-year structural story continuing to emerge across an entity with operating leverage.

Forecasts			
YE 30-Jun	FY18	FY19E	FY20E
Earnings cps	3.6	5.7	6.9
Dividends (AUD) cps	2.0	2.8	3.5
PE x	33.1	23.8	19.5
Yield %	1.7%	2.1%	2.6%
Franking %	100%	100%	100%

RECOMMENDATION DEFINITIONS

RATING CLASSIFICATION

Buy	Expected to outperform the overall market
Hold	Expected to perform in line with the overall market
Sell	Expected to underperform the overall market
Not Rated	Shaw has issued a factual note on the company but does not have a recommendation

High	Higher risk than the overall market – investors should be aware this stock may be speculative
Medium	Risk broadly in line with the overall market
Low	Lower risk than the overall market.

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