under the radar report

SMALL CAPS

ISSUE 258
7 SEP 2017

BLOCKBUSTER REPORTING SEASON FINALE

The big takeout from this reporting season was just how difficult it has been to impress investors after the run on the ASX All Ordinaries, which has seen the broadest index almost double since the depths of the financial crisis back in early 2009.

The good news is that Under the Radar's tips have performed well in the main. We've had some disappointments, but overall management have been delivering on the promises they've made to us in the past few years. Names like Macquarie Telecom (MAQ), BSA (BSA), MNF (MNF), Money3 (MNY), GR Engineering (GNG), Southern Cross Engineering (SXE), RCR Tomlinson (RCR) and Tassal (TGR) come to mind.

The stocks we cover in today's report operate in a vast array of industries, and we have a number of buy recommendations. There continues to be value in the long tail of the some 1,800 or so companies listed on the ASX which have market capitalisations of less than $500m.

It's important to remember that the competitive edge retail investors have in the markets is at the smaller end. This is because fund managers are not able to get enough stock to make a difference to their billion dollar portfolios and consequently these companies are largely ignored by them and by the broker community.

We're able to find stocks that are under the radar and are often very cheap. Growth isn't a problem when you're a company whose market cap is close to $100m. It is when your market cap is in the billions.

We also make a comment on what you can do with your portfolio if you're particularly worried about the mindset of Kim Jong Un and Donald Trump. Let's face it, who isn't? ■

Richard Hemming
Editor

the issue

Small Talk

"In a desert of current income, NZME's dividend tap may run out eventually, but it is no mirage."

THE IDLE SPECULATOR, UNDER THE RADAR REPORT

99% of all financial news relates to the 40 to 50 biggest companies. So what about the rest? They're Under the Radar.

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WHERE DO INVESTORS RUN WHEN KOREA GETS OUT OF CONTROL?

Under the Radar advocates both a defensive and offensive attitude to portfolio construction for those subscribers worried about the problem of North Korea.

KNOWN UNKNOWNS AND UNKOWN UNKNOWNS

Given the unpredictable nature of the two main protagonists, the North Korean crisis is shaping up as one of the most unsettling geopolitical events for investors, not to mention greater humanity, in decades.

It's impossible to know how the escalating tensions will be resolved, but the answers probably are (a) very badly or (b) not at all.

In any case, investors should not ignore the disturbing situation when it comes to constructing their portfolios. Global share markets have held up reasonably well since North Korea in July fired a long-range missile into the Sea of Japan. But with revelations that the rogue nation may possess a hydrogen bomb and intercontinental ballistic missile capabilities, the sternest test may be yet to come.

Not surprisingly the gold price has risen over the last month, by 6% to around $US1336 an ounce. But the safe harbour metal is still below its 2011 record high of $US1890/oz. and was trading at $US1350/oz. a year ago.

The firming price is partly related to a weaker $US. Non-precious metals, notably copper, have rallied as well amid reports that the global economy is strengthening.

SANCTIONS OVER MISSILES

Given the apocalyptic consequences of a North Korean attack on its near neighbours of South Korea and Japan, a US-led defensive strike on the hermit kingdom is considered to be long odds.

At the risk of understatement, China's role as North Korea's immediate neighbour and only ally further complicates things. Talking of complicating things, Donald Trump's rhetoric has turned from fire and fury analogies to trade sanctions against parties that support North Korea with commodities such as food and oil.

The key party of course is China, which is Australia's most important export partner for raw materials and a key source of other income such as education services.

If China's trade to the US is curtailed, the effects would be felt not just by our iron ore and coal miners but value added providers such as Blackmores and Bellamy's.

producers, Northern Star Resources (NST) and Evolution Mining (EVN) on our buy list. We've also got the global producer OceanaGold (OGC) as a Spec Buy. All have been performing well.

PLAYING OFFENCE WITH DEFENCE

The flipside to the North Korean imbroglio is that western countries are likely to boost their defence budgets relative to GDP. In the case of the US, Donald Trump promised a massive defence expansion even before he was elected in December.

A surprising number of ASX small caps are directly exposed to defence spending both here and in the US. Take one of Under the Radar's long time favourites, the ship builder Austal (ASB), which makes ships for the $6.4bn US littoral combat program, as well as patrol boats for the Australian Navy.

> **IF CONDITIONS DETERIORATE FURTHER AND THE MARKET PANICS, THERE MAY BE FEW PLACES TO HIDE. UNDER THE RADAR HAS BEEN ADVOCATING A SMALL EXPOSURE TO GOLD STOCKS FOR SOME TIME NOW AS A HEDGE AGAINST DISASTROUS SCENARIOS.**

Specialist carbon components Quickstep Holdings (QHL) supplies parts for the massive Joint Strike Fighter program, although the company's performance has disappointed over the years. We cover QHL on page 12.

Other examples are the drone manufacturers Xtek (XTE), Orbital (OEC) and Department 13 (D13). Elsewhere the defence space includes the fire retardant material producer Alexium International (AJX) and the defence and aerospace technology group Electro Optic Systems (EOS).

In theory, these stocks should do well although execution remains the key. Because of the sensitivities, defence stocks can take years to procure. ■

PLAYING DEFENCE WITH GOLD

If conditions deteriorate further and the market panics, there may be few places to hide. Under the Radar has been advocating a small exposure to gold stocks for some time now as a hedge against disastrous scenarios. Given gold is sold in US dollars, Australian gold producers are benefiting from the weakening AUD over the past 5 years, which has assisted in lowering their costs relative to offshore competition.

The issue is not so much whether to be exposed to the yellow metal, but the nature of the exposure. A tool such as an exchange-traded fund (ETF) will give a de-facto exposure to bullion, while some will want to hold on to the physical gold directly.

Under the Radar's model portfolio includes the ASX listed Gold ETF. The other exposure is via Australian gold producers that are low cost and boast extensive reserves. That's why we have two of our premier

CLEARVIEW WEALTH
Life insurer and wealth manager

Clearview is weathering the tough times in a life insurance sector blemished by scandals over inappropriate advice and unfavourable claims patterns. Plus, there's a longer game panning out for the industry minnow, with 14.9% shareholder Sony Life almost compelled to make a takeover bid by April next year.

Clearview's earnings continue to impress, with full-year underlying earnings growing 12% to $30.4m. In force funds under management and advice grew 9% to $8.9bn. But life insurance earnings only edged up 2% to $24.9m, the result of higher claims provisioning or "reserving" and a non-renewal of customers, or "elevated lapse experience". The latter happened because the company hiked its income protection insurance policies by 10%. This sounds like a prudent measure considering the experience of the likes of AMP which was almost brought asunder by this product.

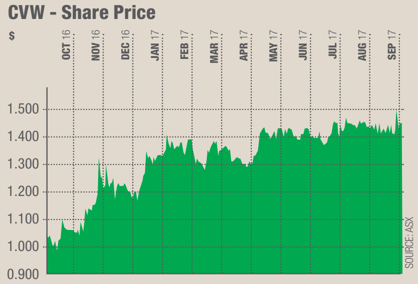
Clearview's flagship product LifeSolutions is gaining traction with independent financial advisers.

On the wealth management side, the number of dealer groups recommending Clearview's products climbed from 9 to 30.

As for the share register, last October the Japan-based Sony Life acquired a 14.9% holding in Clearview, from former suitor Crescent Capital, which retains a 38% stake. But if Sony Life does not bid for Clearview within 18 months, Crescent has the right to regain this holding. In January Clearview and Sony Life entered a "cooperation arrangement" to share knowledge and "work together to drive efficiencies and growth". ■

RADAR RATING: The stock is not cheap on fundamentals, but the strong prospect of corporate action means the downside is limited. As a guide, Sony Life paid $1.48 for its stake a year ago and the value should be well north of that now. It's unusual for a company to be subject to an almost certain takeover offer by a stipulated date and we'll continue to hold for the end game. HOLD.

RADAR RATING **HOLD**
ASX CODE **CVW**
CURRENT PRICE **$1.45**
MARKET CAP **$956M**
NET CASH **$156M**
DIVIDEND YIELD **2%**
TIP DATE **17 APR 2013**
TIP PRICE **$0.44**



FLEETWOOD CORP
Modular accommodation and caravans

After a period in which shareholder activists complained about the lack of dividends, Fleetwood produced a strong performance considering sluggish conditions in the mining accommodation sector.

The company posted full-year net earnings of $9.4m, a welcome turnaround from the previous $11m loss. Underlying EBITDA was $21.9m from $7.2m previously on revenue of $330m, up 16%. The company restored the dividend with a final payout of 5c a share after a three-year absence. The improvement is reflected in the balance sheet as well, with the company reporting $400,000 of net cash compared with net debt of $9.6m last time around.

Management cites stronger demand for fly-in fly-out accommodation and for affordable housing; as well as from the education market, for which it provides portable classrooms.

The company owns the Rio Tinto supported Searipple village in Karratha and the Osprey village in Port Hedland, which is underpinned by an agreement with the

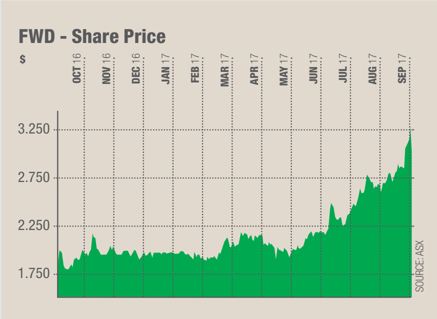
RADAR RATING **TAKE $$$**
ASX CODE **FWD**
CURRENT PRICE **$2.97**
MARKET CAP **$181M**
NET CASH **$0.4M**
DIVIDEND YIELD **3%***
TIP DATE **13 OCT 2015**
TIP PRICE **$1.50**

*Assumes current year payout of 10c a share

West Australian Government. It also supplies buildings for the Victorian education department and the retirement village operator Gateway Lifestyle.

The company owns the Coromal and Windsor caravan brands, which continues to be problematic. The recreational vehicles arm posted an EBIT loss of $6.7m, compared with an $8.1m deficit previously.

RADAR RATING: While the return of a dividend is welcome, that doesn't sway our view that the ongoing improvement is baked into the share price. Management didn't provide any current-year guidance. TAKE PROFITS.



GR ENGINEERING
Mining contractor

The mine builder continues to generate returns in a tricky sector, but its immediate prospects are muddied by two unresolved legal disputes. The first is a $9.9m recovery action against Eastern Goldfields over work performed by GR Engineering on the former's Davyhurst gold project. The second is a dispute with Wolf Minerals, involving allegedly defective work on Wolf's Hemerdon tungsten and tin mine in Devon.

Wolf is trying to access a $12.5m bank guarantee that GR Engineering's UK arm agreed to provide after it won the contract in 2013. On August 17 Wolf said it intended to call on the guarantee because GR has failed to rectify a low-frequency noise defect. GR says the claim is without merit and that it has already received 97% of the total payments due from the project.

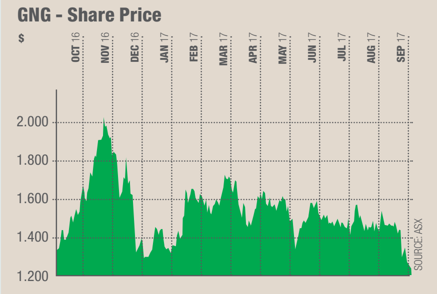
Meanwhile, GR's Supreme Court action against Eastern Goldfields alleges non-payment of amounts owed to GR for its work at Davyhurst. GR suspended works at the mine in May 2017 after "protracted commercial discussions" fell through. Eastern Goldfields was to have been liquidated, but on August 15 the WA Supreme Court set aside the order.

GR voluntarily suspended its shares on August 18, pending clarification. They were reinstated after GR's full-year results were released last Friday. The Wolf matter has resulted in GR "temporarily" suspending its final dividend.

GR's full-year net profit tumbled 33% to $12.9m, on a 6% revenue decline to $238.7m. EBITDA of $16.9m, down 35%, reflected "an increasingly competitive landscape" for GR's services and the market's harsher attitude to pricing the risk of fixed price contracts. Still, GR cites a strong order book with contracted revenue of $240m. The company expects total revenue for 2017-18 of $300 to $330m.

RADAR RATING: GR shares have slipped from $1.30 to $1.25 since being reinstated and have retracted from $1.49 on March 9 when we urged readers to take profits. In theory, the revenue guidance points to improved earnings if the company can at least maintain its margins. A successful (or partly successful) resolution of the Eastern Gold claim implies some upside. TAKE PROFITS.

RADAR RATING **TAKE $$$**
ASX CODE **GNG**
CURRENT PRICE **$1.25**
MARKET CAP **$192M**
NET CASH **$34.2M**
TIP DATE **03 OCT 2013**
TIP PRICE **$0.58**



HILLS

Audio-visual and healthcare equipment

A flurry of restructuring and rationalisation is paying off for the 72-year-old diversified industrial group, which narrowed its reported full-year loss to $7.9m from a $68.3m deficit previously. Group revenue declined 9% to $298m, partly the result of the company's second-half exit from the business of installing satellite dishes on behalf of National Broadband network customers. The results were consistent with management's mid-June guidance; which also said that it expected Hills to profit in the current year.

The debt reduction continues: down to $20m from $21.6m a year ago, with cash increasing to $8.65m from $4m previously.

The group's confidence is because costs fell to $105.6m from $157.6m previously. In particular, the Hills Health Solutions business has improved its profitability. After a tidy up that included divesting its famous clothesline business, Hills now focuses on large-scale deployment of audio and camera systems and bedside nurse call and patient entertainment systems in hospitals. Recent contracts include camera systems for the new Perth Stadium, the NSW Parliament, toll road operator Transurban and property owner Mirvac.

In healthcare, Hills is installing nurse call units for the Joan Kirner Women's and Children's Hospital in Melbourne's west and stage two of Sydney's Blacktown Hospital. As of June 30 Hills had 18,000 beds under management and expects this to grow to 20,000 by June next year. Hills also cites $5m of nurse call work to be completed in 2017-18.

We described Hills as priced for failure when we introduced the stock as a speculative buy on July 20, when the stock traded at a record low of 15.5c. The uptick since then reflects the market's increasing confidence the company is on the right track following years of upheaval and strategy missteps. ■

RADAR RATING: We continue to think the upside is not reflected in Hills' $40m market valuation. But Hills is coming alive. But this play is speculative, given it's hard to tell how strong the envisaged profit rebound will be. SPEC BUY.

RADAR RATING **SPEC BUY**

ASX CODE **HIL**

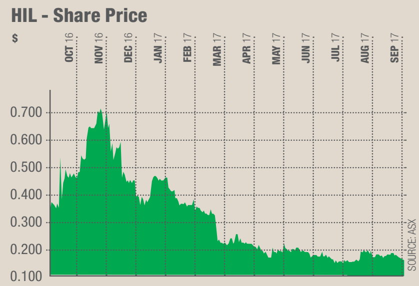
CURRENT PRICE **$0.19**

MARKET CAP **$44M**

NET DEBT **$20M**

TIP DATE **20 JUL 2017**

TIP PRICE **$0.155**



IMF BENTHAM

Litigation funding

Net profit before tax for IMF was in line with the previous year at $25.7m, which barely reflected lumpy legal settlements including two which bookended FY17. Total revenue for the year was $113m, up almost 15%, and these results still reflect the concentration of IMF's case portfolio in a smaller number of larger cases. The group has attempted to limit the concentration by taking on a larger number of smaller cases, but it is still a year or so before the full impact of that strategic change works its way through the company's case load.

Opportunities should arise in the insolvency, family law, corporate funding, whistle-blower and law firm contingent fee funding.

A final dividend of 4 cents was fully franked, and makes 7 cents in total. Dividends are discretionary and depend on successful case conclusions to give management confidence that dividends can be paid without compromising opportunities for growth.

RADAR RATING **HOLD**

ASX CODE **IMF**

CURRENT PRICE **$1.99**

MARKET CAP **$343M**

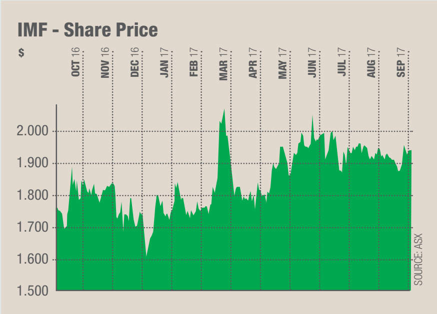
NET CASH **$25M**

TIP DATE **14 NOV 2013**

TIP PRICE **$1.71**

The current concentration of the portfolio has led to a reduction in net cash. Two major cases remain outstanding from previous years and are expected to be concluded in the next two years. The first is the Wivenhoe, relating to the Brisbane flooding; the second is the Westgem case – a major property development collapse in 2010/11 in Perth.

Both cases could well be very expensive for IMF if they lose, since they would have to pay for the other side's costs. And both are likely to have a material impact on investor sentiment as well as the financial results, and the substantial amounts already invested will increase before reaching the court steps. In order to maintain its position, IMF is obliged to continue to invest despite no certainty as to the eventual outcome and the timing of any financial settlement. ■



RADAR RATING: Even though the valuation is not particularly demanding and we like management and its record, for speculative reasons we don't recommend fresh stock purchases here. We suspect that a decision in either of the two major cases discussed has the potential to create an opportunity to upgrade, and we will be prepared to react quickly when news emerges. HOLD.

MACQUARIE TELECOM

IT services and telecommunications

RADAR RATING **TAKE $$$**

ASX CODE **MAQ**

CURRENT PRICE **$14.60**

MARKET CAP **$307M**

NET CASH **$36.5M**

TIP DATE **12 AUG 2015**

TIP PRICE **$6.51**

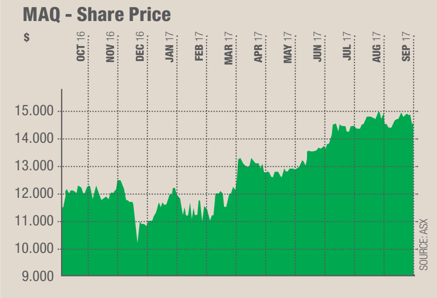
We jumped into Macquarie Telecom at the right time! Our most recent buy call in March when the stock was $11.51 is paying off handsomely and has so far delivered a 30% plus return, when you include the 25c dividend.

This success was underlined by a strong fiscal 2017 result, which exceeded market expectations. The question is, do we hang on?

The company has two revenue streams: a telecom reselling business and hosting or "cloud" services, which includes a division that looks after Australian government departments.

Macquarie Telecom has succeeded in increasing the utilisation of its data centres and transitioning its business away from the billable hours model for servicing companies' IT requirements and towards the software as a service business which is lower margin but more annuity driven. Underlying all this, as management constantly stress, is the group's adherence to customer service as its differentiating feature from other telcos.

While other companies have been outsourcing their customer services to places where labour is cheaper, MAQ has embraced the net performance score systems and an Australian workforce needed to implement it. It's an expensive gamble, and one which seeks to answer this key question in the positive: "Would you recommend MAQ's product to a friend or colleague based on your experience?"



FY17 saw revenues climb 8% to just under $220m, boosting EBITDA 25% to just over $40m, in an illustration of how operating leverage is boosting the group's profits. MAQ has high fixed costs compared to variable costs and as revenues grow, the profits are dropping to the bottom line. Depreciation fell off which boosted NPAT to $14.2m, which was almost triple the prior period. The company continues to pay a final dividend of 25c, delivering 50c for the year (fully franked).

Capital expenditure for the period was $38.5m; while the group expects between $32-35m next year, although it's expecting flat first half profits. The dividend level should be maintained but the big news of the result was that the group is looking at adding to its stable of three data centres. A decision will be made and announced at its AGM in October. ■

RADAR RATING: When we said BUY back in March the stock was trading on a dividend yield of 4.3% and this has come down to 3.4% at current levels; plus there is a probability that it will need to leverage up again in order to build another data centre; and there is the prospect that higher power prices will erode margins. TAKE PROFITS.

MONEY3
Consumer lender

RADAR RATING **SPEC BUY**

ASX CODE **MNY**

CURRENT PRICE **$1.49**

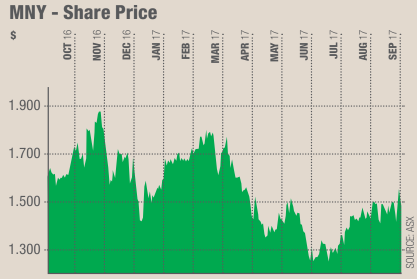
MARKET CAP **$232M**

NET DEBT **$58M**

DIVIDEND YIELD **3.7%**

TIP DATE **4 MAY 2017**

TIP PRICE **$1.44**



Money3's strategy has been to move away from "payday" lending where it lends small amounts of money at high interest rates or where the borrower agrees to repay the loan upon receipt of his or her next wages. Instead it has been focussing on financing second-hand cars, which has been delivering strong returns.

The auto book now accounts for 78% of the lender's total $273m book and Money3 posted a 44.5% surge in net earnings to $29.1m for the full year, on a 13% revenue boost to $109.6m. The bottom line exceeded management's guidance of $27.5m and compares with a first half profit of $13.8m.

The board has rewarded shareholders with a 3.15c a share final dividend, taking the full year payout to 5.65c. Despite this largesse, the dividend still only accounts for 30% of net earnings with management setting a dividend payout ratio of 30-50%. One item to watch is net debt, which has more than doubled and stands at just under $60m. This reflects management's preference to use debt rather than equity to fund the loan book growth.

In moving away from small amount credit contracts, MNY acknowledged the regulatory pressure on the sector was only going to increase. Now, Money3 is using its consumer credit assessment and collecting skills in the used vehicle sector largely abandoned by the banks. The typical vehicle financed is three to eight years old and thus highly depreciated already. About three-quarters of the loans are sourced through a 150-strong broker network.

The strong returns the company has achieved on the lending book show there's money to be made, as long as defaults are kept in check, which has so far been the case. ■

RADAR RATING: Money3 trades on an earnings multiple of less than eight times and this should shrink further with expected profit growth in the current year. Key risks to the business are an economic downturn or, alternatively, an interest rate hike. But both scenarios could present opportunities as well as adversities as the banks further lighten their exposure to the sector. SPEC BUY.

NZME
New Zealand newspapers and radio

New Zealand Media's results delivered a flat trading result at the EBITDA and NPAT level from revenue 3% lower at $189m. Revenue was down 5% in the first 6 weeks of the second half, and cost reductions will slow, so earnings will be under pressure. Medium term progress will depend on strategies to restart growth in radio, or reimagine the newspaper experience which will involve improving digital revenue conversion.

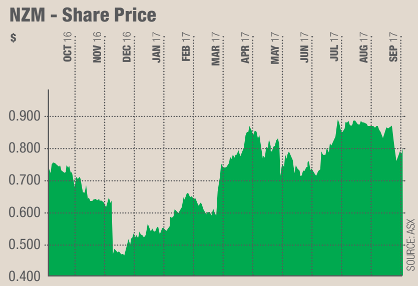
The market reacted poorly to the results, which we think creates another Speculative Buy opportunity essentially because we think these mature media businesses will have a long revenue tail and that corporate activity in some form is more likely than not if the company can't return to growth in its current form. With broad exposure to print media and radio, it is impossible for NZM to avoid the sectoral headwinds arising from the shift of audiences and revenue to digital alternatives, including Facebook and Google.

The bottom line first half result delivered earnings of NZ5c (A4.5c) a share, from which a NZ3.5c dividend will be paid at the end of October. This will be supplemented for Australian shareholders by an additional tax credit of NZ0.6176 cents. The dividend payment will be made shortly after the appeal is heard against the NZCC decision not to permit the Fairfax New Zealand and NZME proposed merger. The nine-day hearing will conclude towards the end of October. ■

RADAR RATING: In a desert of current income, NZM's dividend tap may run out eventually, but it is no mirage. Last year's final dividend was NZ6 cents + tax credit, and if maintained will deliver up to a 12% annual gross yield. Add to that corporate activity potential from two separate proposals or expressions of interest in all or parts of the business. If the NZCC appeal decision goes against the merger, the yield may provide support, and if it goes for the merger, the potential financial benefits are substantial. SPEC BUY

* The Idle Speculator retains a holding in NZM in his SMSF

RADAR RATING **SPEC BUY**
ASX CODE **NZM**
CURRENT PRICE **$0.79**
MARKET CAP **$156M**
NET DEBT **NZ$107M (A$97M)**
TIP DATE **13 JUL 2016**
TIP PRICE **$0.66**



PACIFIC CURRENT
Owner of minority stakes in investment managers

Pacific Current has been a stock where although our initial tips were too early, we were right to identify the clear value proposition that the shares represented. Subscribers who stuck with the recommendation and continued to buy through the trough in sentiment may have been rewarded in the same way as the Under the Radar Report portfolio which is showing returns of over 30% a year on its four share purchases over a couple of years.

A headwind to the company's performance has been the issue of substantial shares to buy the remaining 35% of Aurora Trust to simplify the capital structure. PAC's FY17 results were an underlying profit before tax of $16.6m, while the proposed final dividend of $0.18 per share was in the middle of the forecast range of $0.16-$0.20.

The underlying business performed extremely well in the second half. In terms of valuation, PAC own just over 23% of Aperio, which has US$25bn under management and has grown strongly. There is also a small position in GQG, which has had one of the largest hedge fund launches known. Operating costs, which include sales and distribution staff and administrative overheads, fell 28% as the structural simplification created savings.

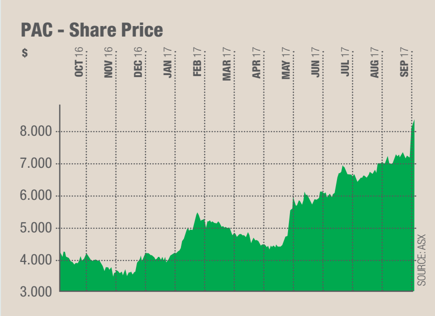
RADAR RATING **HOLD**
ASX CODE **PAC**
CURRENT PRICE **$7.90**
MARKET CAP **$376M**
NET DEBT **$17M**
TIP DATE **27 APR 2016**
TIP PRICE **$4.40**

To profit successfully from stocks which are going through a period of market rejection but may have hidden value, you need first an ability to identify value, and be able to look beyond the market's current preoccupations.

For PAC the issues included poor performance in some of the funds, and our experience is that investment performance comes and goes. Ideally, you want to correctly guess the timing of management's attempts to correct the problems, and it's not always possible to have perfect timing.

As the Under the Radar Report portfolio demonstrates: the sensible approach is to nibble slowly at these stocks as the problems emerge, and circle back to check that the elements of the story that are positive remain intact. While the parts of the story that you like are not outside your expectations, squirrel away a few more shares at lower levels. We made four separate purchases for the portfolio between August 2015 and July 2016. At current prices, our annualised internal rate of return on those purchases is over 34%. Unfortunately, not all our purchases go that well, but we wanted to illustrate how it makes (dollars and) sense to use Under the Radar Report in your investment process. ■

RADAR RATING: We said last time that we suspect the stock is in the relatively early stages of its recovery as institutions become more comfortable with the future direction. Having had PAC on our Best Ideas list at $4 and even below for some time last year, we hope many of our subscribers are profiting from PAC. HOLD.



PACIFIC ENERGY

Remote power provider

Apart from contract delays, Pacific Energy is meeting market expectations with a robust slate of new work from resource clients. During the 2016-17 year the off-grid power supplier was awarded 39 megawatts of new contracts, taking the total contracted capacity to 272MW across 21 Australian mine sites. The company also has 6MW of hydro capacity at two sites near Melbourne.

Pacific Energy recorded net earnings of $16.6m, up 6% with underlying EBITDA up 9% to $40m. Revenue climbed 11% to $57.2m. While these numbers met expectations, second-half activity was more subdued because of delayed contract awards on greenfields, or new projects. We remain confident however, because in terms of work in hand, Pacific Energy has the advantage of being weighted to the gold and copper sectors, which are doing well.

As well, managing director Jamie Cullen describes the overall resource sector outlook as "very positive". A highlight of the results was record operating cash flow of $35m, which helped to pay down debt as well as to fund a final dividend of 1.5 cents a share (2.5c a share for the full year).

Under its 'build own and maintain' model, Pacific Energy funds 100% of the cost of a plant but then charges a fixed monthly tariff under a long-term contract. The long-term annuity-style contracts means the company can forecast earnings with some confidence. This model can result in high upfront capital costs, but capex in 2016-17 fell to $19m from $37m previously, with a forecast current-year spend of $15m.

Management forecasts current-year underlying EBITDA of $43-44m, which may seem only a modest increment but is based solely on contracts in hand so is subject to upwards revision. Almost all of these earnings are projected to be from existing sites.

RADAR RATING **BUY**

ASX CODE **PEA**

CURRENT PRICE **$0.62**

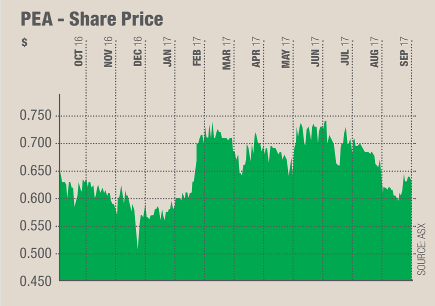
MARKET CAP **$232M**

NET DEBT **$28M**

DIVIDEND YIELD **4%**

TIP DATE **23 MAR 2014**

TIP PRICE **$0.47**



A wildcard is the company's success or otherwise in the more volatile African market, which it entered only a year ago. The company cites 100MW of current tenders across six African projects. ■

RADAR RATING: Pacific Energy shares have delivered for Under the Radar readers over the last two and a half years and we expect they will continue to do so. BUY.

PANORAMIC
Nickel miner

RADAR RATING **HOLD**

ASX CODE **PAN**

CURRENT PRICE **$0.34**

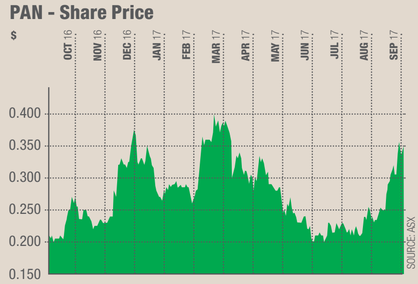
MARKET CAP **$146M**

NET CASH **$8.1M**

TIP DATE **14 JUL 2016**

TIP PRICE **$0.20**

PAN - Share Price



For a miner that is not actually mining for the time being, Panoramic did well to report a break-even full-year result for its mainstay nickel division. Given the poor nickel price, Panoramic mothballed its Lanfranchi mine in November 2015 and then its Savannah mine in May last year.

But during the 2016-17 financial year the company sold a residual 10,719 tonnes already mined at Savannah, yielding 929 tonnes of nickel in concentrate as well as 520t of copper and 44t of cobalt.

This resulted in sales revenue of $9m (previously $92m) offsetting $7.5m of care and maintenance costs. Overall Panoramic reported a $4.7m loss, compared with a $144m deficit previously.

In July, Panoramic released an optimised feasibility study to support the re-opening of Savannah as a short life underground operation. The study is based on a break-even price of $US3.75 a pound, compared with the current price of around $US5.50/lb. (up from $US4.70/lb. a month ago). The cobalt credits are an important part of the economics, with the battery metal projected to contribute 25% of revenue. At $US5/lb. nickel, the company ascribes a net present value of $190m to the project.

Panoramic shares have strengthened by 66% since mid June, as investors speculate that Savannah will be reborn. Management is yet to commit to a re-start, but is certainly optimistic about it happening. A re-opening is costed at around $20m of pre-production costs with a funding requirement of up to $40m. Panoramic was the second biggest nickel producer behind BHP's Nickel West division. ■

RADAR RATING: With the nickel price finally headed the right way, we think Panoramic shares may have some way to go and maintain a hold call. HOLD.

QUICKSTEP HOLDINGS
Carbon composite parts

When companies talk about a year in transition, too often it is a euphemism for another year of losses and flip-flopping on strategy. Quickstep has innovative and promising technology, underpinned by contracts to supply parts to the $300bn F-35 Joint Strike Fighter program and for Lockheed Martin's C-130J (Super Hercules) and commercial LM-100J work horses.

We hope the aircraft can move more nimbly than Quickstep itself, which reported a $6.7 million full-year loss in what management dubs a "transition year in preparation for growth." Underlining this it reported an EBIT loss of $5.7m compared with a $2.2m deficit previously. Sales revenue increased 4% to $51.9m, with higher volumes of JSF parts offsetting a decline in C-130J volumes. Despite that, Quickstep's Bankstown Airport facility in Sydney remains well underutilised.

In February 2015 Quickstep signalled its interest in automotive parts with the appointment of former Futuris Automotive chief operating officer David Marino as CEO. But in April this year Marino departed and under new CEO Mark Burgess, Quickstep has now refocused on aerospace and defence sectors. Burgess says that the company's automotive oriented operations near Geelong will continue, but automotive clearly is not a priority despite some success.

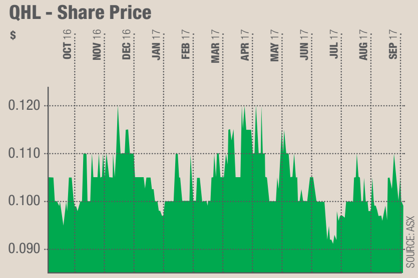
Burgess says the company's R&D investment of $5.5m will be trimmed and "more focused, more market oriented and with a more aggressive commercialisation path."

As at balance date the company had cash of $3.7m, down from the previous $7.6m. ■

RADAR RATING: We downgraded the stock to a hold at 11c in early August last year. The company continues to pay its bills and there remains potential. It's bottom drawer advanced composite material. HOLD.

RADAR RATING **HOLD**
ASX CODE **QHL**
CURRENT PRICE **$0.097**
MARKET CAP **$55M**
NET DEBT **$8.3M**
TIP DATE **27 JAN 2014**
TIP PRICE **$0.21**

QHL - Share Price



SDI
Dental supplies

Unfavourable currency movements and flat sales of amalgam material have put a bite on the local supplier of dental materials that sells to more than 100 countries.

Because SDI incurs costs in A$ but sells in mainly US$, Euros, Brazilian Real and pound sterling, it is especially vulnerable to a strengthening Australian dollar. Of course an alternative explanation is that the 45-year old manufacturing stalwart is simply in a rut that management cannot address.

SDI reported a $5.6m full-year profit, 26% lower, on flat sales of $74.1m. The profit included $500,000 of unrealised currency losses. The highlight was the 27% reduction in debt to $4.1m from $5.7m previously. Free cash flow slipped to $4m from $4.4m but was solid.

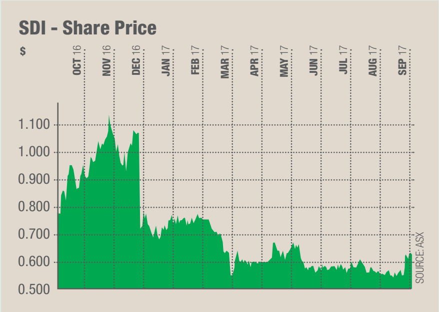
SDI's sales reflect that demand for amalgam material (the grey filling used for back molars) is in steady decline. But sales of more aesthetic materials such as glass ionomers are climbing, as is demand for tooth-whitening ingredients.

Up until now, the demand for the new age materials has not been enough to offset the amalgam decline. With aesthetics and whiteners now accounting for 60% of sales, top

RADAR RATING **TAKE $$$**
ASX CODE **SDI**
CURRENT PRICE **$0.64**
MARKET CAP **$77M**
NET CASH **$1.6M**
DIVIDEND YIELD **3.6%**
TIP DATE **9 JUL 2014**
TIP PRICE **$0.50**

line growth eventually should be restored although perhaps not in the current year. Management holds high hopes for a new product called Radii Xpert, a light to cure fillings that will contribute to sales from September.

RADAR RATING: SDI is yet to regain its vim since a severe profit warning in November last year that saw the stock lose one-third of its value in a day. But at least conditions haven't worsened since then. We continue to recommend TAKE PROFITS.



SERVCORP
Serviced office provider

We have been covering Servcorp since Under the Radar Report's first year. The stock more than doubled over a couple of years, but more recently has come back, as competition in the sector has increased and some operational missteps have come into consideration. The company had pre-announced a disappointing result, EPS rose 3% to 41.4 cents, based on profit before tax of $48.2m. A 13c final dividend makes 26c total, 50% franked.

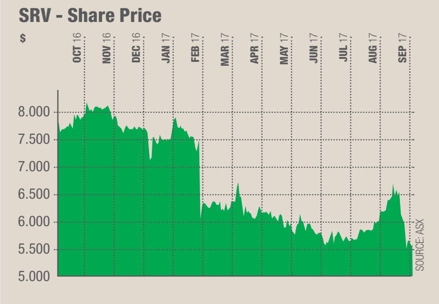
Competitor WeWork is a fast growing start-up that provides shared workspaces to a hip and trendy crowd. Softbank (the Japanese telecoms giant) and its $93bn "Vision" fund agreed a couple of weeks ago to invest US$4.4bn in WeWork, valuing the 7-year-old start-up at around $17bn. WeWork claims to have 150,000 members across its 160 locations, and generates $1bn in revenue. As a well-connected "unicorn" start-up, Goldman Sachs and JP Morgan Chase are also among its investors.

Servcorp has over 5000 offices worldwide across 155 floors, a number which has almost doubled over the last 6 years, and 15,000 "members". The company still has $108m cash on its balance sheet, but underperformed in New York in the past financial year. The occupancy level is around 75%, and its efforts in the current financial year will be aimed towards improving occupancy rather than investing in new space. The company has also invested in systems and community initiatives which are designed to offer clients flexibility, and mimic some of the features valued by clients attracted to competitive offerings.

The company has issued a relatively wide pre tax FY18 forecast of $45m-$55m, indicating there is plenty of financial leverage to occupancy levels. A FY18 forecast dividend of $0.26 offers a 4.5% yield, though the franking may not be available. The Moufarrige family, led by Chief Executive Alf, occupy a number of executive positions as well as their 50% plus stake. Although this can be seen through a negative lens, family control and executive involvement didn't prevent the Lowys and the Murdochs from building global empires, although there are many more examples which did not have the same success!

RADAR RATING: We will keep a close eye on Servcorp, and talk to the company around the time of the AGM to see if we can upgrade further. While the operating performance of the company is under pressure, and it is speculative when performance may improve, the net cash and the annual dividend together amount to enough to support a SPEC BUY recommendation.

RADAR RATING **SPEC BUY**
ASX CODE **SRV**
CURRENT PRICE **$5.38**
MARKET CAP **$529M**
NET CASH **$108M**
TIP DATE **15 AUG 2013**
TIP PRICE **$3.53**



SOUTHERN CROSS ELECTRICAL ENGINEERING

Electrical contractor

The 2017-18 year was a period of divergent two halves for the once resources-focused electrical contractor, with a much better second stanza following a forgettable first half. Encouragingly, the company enters the current year with a record order book of $480m compared with only $55m at the start of the year, with $400m of additional projects tendered for. The contracts in hand are expected to generate revenue of $350m in the current year.

A positive feature of the result was that net cash increased to $40.3m from $25m post the Heyday acquisition. As expected, the company will not pay a dividend but $20.8m of franking credits means it has a strong incentive to resume payouts.

Southern Cross reported a bottom line $400,000 loss for the year on revenue of $200m, 3.7% lower. Underlying EBITDA of $6.8m was 44% lower, excluding a $5.4m gain from earn outs now not payable to the vendors of the Datatel telco business acquired mid last year for $6.2m. With the resources sector stabilising, Southern Cross managed second half underlying earnings of $4.1m and underlying EBITDA of $8.2m.

The breakdown of the Southern Cross order book shows the extent of its diversification: only $70m (14%) of the $480m order book is attributable to the resources sector, with $235m (49%) from the commercial sector and $115m (24%) from public infrastructure and defence. In the 2016-17 year, almost half of the company's revenue derived from resources.

Still, Southern Cross remains materially exposed to the resources sector with projects for BHP Billiton's and Rio Tinto's iron ore divisions, as well as the Wheatstone LNG project. While stabilising, iron ore conditions remain subdued. The LNG work will flow through to the current year, there's "low visibility" on contracts thereafter.

Through Datatel, Southern Cross is involved in the rollout of the national broadband network and has suffered because of delays. The company's non-resources projects include Perth's Mitchell Freeway, four NSW solar farms and the air force's Tindal base in the Northern Territory.

In February the company bought the Sydney based Heyday5 for $54m, thus strengthening it eastern seaboard industrial presence. This business is performing well, evidenced by a $9.25m earn-payment due next month.

We have been positive on the company over the last two years, but downgraded to a hold at 62.5c on August 10 following a share rally from 45c in early May. The bolstered order book is encouraging, but it remains to be seen whether the work translates to renewed profit margins (the gross margin in 2016-17 fell to 12.1% from 16.1% previously). ■

RADAR RATING: While the company looks to be emerging from a problematic period, we would prefer to see more earnings visibility before we upgrade. HOLD.

RADAR RATING **HOLD**

ASX CODE **SXE**

CURRENT PRICE **$0.70**

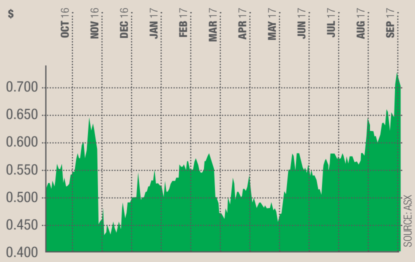
MARKET CAP **$112M**

NET CASH **$40.3M**

TIP DATE **29 JUL 2015**

TIP PRICE **$0.36**

SXE - Share Price



TOX FREE SOLUTIONS

Waste manager

The acquisitive waste manager has signalled that it will pause any further acquisitions and focus on coaxing more from its existing operations, which is welcome given organic growth rates have lagged and gearing has increased.

Following an underwhelming first half, Tox posted a 4% rise in underlying net earnings to $24.1m, on a 26% revenue increase to $496.1m. Underlying EBITDA climbed 14% to $82.8m, within the guided range of $82-83m.

The WA-based Tox is an unfolding story of reducing reliance on work from the resources sector, in favour of building an industrial presence on the eastern seaboard. To do this Tox has executed a number of acquisitions, most recently the $186m purchase in October last year of Daniels Health, the country's biggest manager of medical waste. Tox earlier last year bought NSW water recycler Worth Corp for $70m. Both were funded by debt and equity that has pushed overall net borrowings up to $157.3m from $102.8m previously.

In FY17 54.5% of revenue derived from non-resources activities in 2016-17, up from 52% a year earlier and 40% five years ago. While the acquisitions are performing well, the integration process has affected margins and management forecasts a modest 4% increase in EBIT for the current year. ■

RADAR RATING: Tox operates in a $4bn a year market that can only grow further as populations and waste management regulations increase. We like this company for the long-term but there is a great deal of debt and the shares on issue have climbed very quickly, which reflects the fast paced acquisition led growth. SPEC BUY.

RADAR RATING **SPEC BUY**

ASX CODE **TOX**

CURRENT PRICE **$2.48**

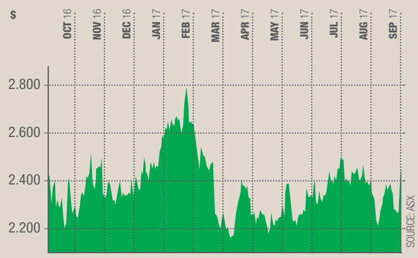
MARKET CAP **$432M**

NET DEBT **$157M**

TIP DATE **2 NOV 2016**

TIP PRICE **$2.33**

TOX - Share Price



99% **of all financial news relates to the 40 to 50 biggest companies. So what about the rest? They're Under the Radar.**

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