Investment Watch

Autumn 2021 Outlook

morgans

Welcome

We see the path out of the COVID-19 shock as a "restart" – not a typical business cycle "recovery". The key reasons are the distinct nature of the shock, broad-based pent-up demand and different inflation dynamics. The passage of the US$1.9trn fiscal package and an accelerating vaccination ramp-up magnify these factors, and we believe the restart will likely be stronger than markets expect. Inflation dynamics and improving economic growth will have a significant impact on bond yields – something that investors haven't had to contend with for some time. This quarter we look at what this means for Asset Allocation in 2021. We also look at what the economic restart means for the key industries in the ASX.

Recently published research

Equity strategy – Q2 sector outlook and strategies	31/3
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Recent corporate offers

CommBank PERLS XIII Capital Notes

Commonwealth Bank

Initial Public Offer

Morgans Financial Limited was a Joint Lead Manager to the Initial Public Offer of CommBank PERLS XIII. Strong investor demand for CommBank PERLS XIII has seen the Issuer issue $1.0 billion of Notes under the Broker Firm Offer.

CommBank PERLS XIII will pay floating rate, quarterly gross distributions based on an issue margin of 2.75% p.a. above the 3-month BBSW (expected to be fully franked). CommBank PERLS XIII are expected to list on the ASX on 6 April 2021 under the code CBAPJ.

Macquarie Group Capital Notes 5

MACQUARIE

Initial Public Offer

Morgans Financial Limited was a Joint Lead Manager to the Initial Public Offer of Macquarie Group Capital Notes 5 (MCN5). Due to strong demand from investors, the Issuer has issued $550 million of Notes under the Broker Firm Offer.

MCN5 will pay floating rate, quarterly gross distributions based on an issue margin of 2.90% p.a. above the 3-month BBSW (expected to be partially franked). Macquarie Group Capital Notes 5 are listed on the ASX under the code MQGPE.

Centuria Notes

Centuria

Initial Public Offer

Morgans Financial Limited was a Joint Lead Manager to the Initial Public Offer of ASX listed secured, redeemable notes (Centuria Notes) by Centuria Funds Management Limited as trustee of Centuria Capital No. 2 Fund. Strong investor demand for the Centuria Notes Offer saw the issue raise $190 million. Centuria Notes will pay floating rate, quarterly, compulsory cash interest payments based on an issue margin of 4.25% p.a. above the 3-month BBSW. The Offer proceeds will be used to redeem a series of Wholesale Notes and support Centuria Capital Group's month BBSW. The Offer proceeds will be used to redeem a series of Wholesale Notes and support Centuria Capital Group's REIT co-investment programme, strategic acquisitions and to accelerate the growth of its unlisted property funds division. Centuria Notes are expected to list on the ASX on 21 April 2021 under the code C2FHA.

Micro-X Limited (ASX: MX1) – Placement & Share Purchase Plan

Australian hi-tech company Micro-X Ltd ('Micro-X' or the 'Company'), is a leader in cold cathode x-ray technology for the healthcare and security markets globally. The Company recently completed a $30.5 million placement to institutional and sophisticated investors followed by a $3.5 million share purchase plan (together 'the Offer'). The Offer was conducted at $0.34 per share and Morgans Corporate Limited acted as Joint Lead Manager.

- **Morgans role** – Joint Lead Manager
- **Offer size** – approximately $30.5 million

EQ Resources Limited (ASX: EQR) – Placement

EQ Resources Limited explores for and produces tungsten, gold and other mineral resources in Australia, and is focused on scaling up operations at its world-class high-grade tungsten project at Mt Carbine, North Queensland. The Company recently received $6.5 million of firm commitments in a well-supported placement to institutional and sophisticated investors. The Placement was conducted at $0.032 per share and Morgans Corporate Limited acted as Lead Manager.

- **Morgans role** – Lead Manager
- **Offer size** – approximately $6.5 million

Airtasker Limited (ASX: ART) – Initial Public Offer

Morgans Corporate Limited was Lead Manager to the Initial Public Offer of Airtasker Limited, which successfully raised $83.7 million at $0.65 per share. Airtasker is Australia's leading online marketplace for local services, connecting people and businesses who need work done ('Customers') with people who want to work ('Taskers'). Airtasker delivers a frictionless ecommerce experience for Customers to buy local services and creates flexible working opportunities and income for Taskers. Airtasker is listed on the ASX under the code ART.

- **Morgans role** – Lead Manager
- **Offer size** – approximately $83.7 million
- **ASX listing date** – 23, March 2021

RightCrowd Limited (ASX: RCW) – Placement

RightCrowd Limited develops and sells physical security, safety and compliance software solutions worldwide, and is seeing accelerated demand for its solutions as companies seek to manage the safety and security of their workforce as they "Return to the Workplace". Morgans Corporate Limited was Lead Manager to the successful placement to institutional and sophisticated investors, raising $12.5 million at $0.33 per share.

- **Morgans role** – Lead Manager
- **Offer size** – approximately $12.5 million

Economics – why bond yields must go up

In early March, US treasury bond yields went all the way up to 150 basis points in yield before retreating to 140 basis points. The fact that 150 basis points was a high yield demonstrates where we've been coming from. The US treasury bond, which is the biggest asset class in existence globally, has been around for a long time. It began way back in July 1789 when it was passed by one vote in US house of representatives in Philadelphia. The bill was put up by Alexander Hamilton who is the same guy the musical is about which is now playing in Sydney.

The lowest yield in all of history since that time was last year, which is 231 years. We have been pointing out for the last 9 months about how increasing budget deficits would drive down the US dollar and increase commodity prices and that is more and more true every time we look at the information and do the analysis.

But what also happens is that those budget deficits increase the real demand for capital, and when you push up the real demand for capital, you will push up real long term interest rates. We believe inflation will edge up from here but the real demand for capital will remain strong for the next couple of years because of improving American economic growth. We anticipate GDP growth in the US economy this year at 4.5% or better and it's likely growth in the world economy will be the best growth for a couple of decades in this year alone.

We've updated the models for bond yields for US treasuries, for Australian ten-year bonds, and for German ten-year bonds. Firstly the US treasury bond is the benchmark bond for all the bonds around the world. Every bond prices itself relative to the US treasury bond, so if we look at all that we have almost 40 years of data in the model and one of the things that is included in the model as well as inflation is US budget deficits. When we run that model and it explains just about 90% of model variation we find that the equilibrium yield for US treasury bonds is 2.92%.

So we think there is further upside in US treasury bonds and we end up with a very positive yield curve. The Fed has indicated that it's not going to raise rates any time in the next couple of years, but long-term interest rates will go up and you'll have an upward sloping yield curve. That means there's a high return for people making investments in the real US economy. The real US economy is the one that builds cars, builds computers, builds highways, and employs people. We believe unemployment will fall from just over 6% to 3% in a few years. That will be back at the same kind of low levels of unemployment that saw US treasury at 2.92%. We see Australian treasury yields increasing about 130 basis points to 2.7%, our bond yields will also be about twice what they currently are.

The real surprise is in Europe because most benchmark bond yields in the major Euro area economies are in negative territory. But what we discovered is that those Euro area yields are also extremely sensitive to budget deficits and budget deficit in the Euro area went from pretty much nothing all the way up to 8% over the last year and this year comes back to 6%. Now that's tiny in comparison to the US but is very large in comparison to where budget balances have been in the Euro area for the last 20 years. So our equilibrium level for the lowest level of yielding bonds which is the German 10-year bond which is currently trading below zero we've got that going up to an equilibrium yield of 38 basis points.

So over the next couple of years we expect to see a major sell-off in US treasuries, Australian treasuries and European treasuries. It will take yields to much higher levels than they are now at levels that apart from last year would be very low compared to history.

Outlook for the ASX and AUD

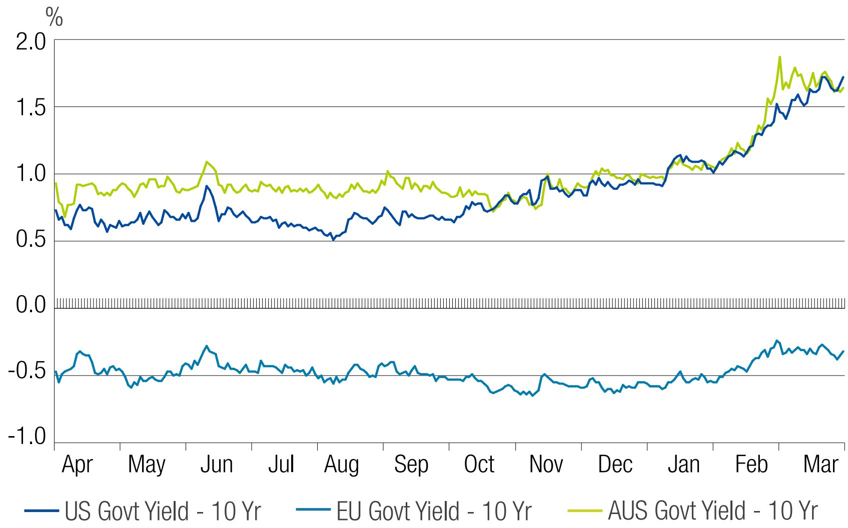
After falling sharply in 2020, earnings for companies with the ASX 200 have begun to rise sharply in 2021. We expect earnings to continue to rise through the rest of the year and into 2022. The share price of companies within the ASX 200 continues to rise in anticipation of that future improvement in earnings.

This means that the ASX 200 is now moderately overvalued relative to our model of fair value. On 30 March the ASX 200 at 6768 points, is 448 points in excess of our model estimate of 6320 points. This modest level of overvaluation means that stock selection becomes increasingly important to identify points of entry.

The last two years have seen enormous fiscal stimulus to the US economy. A US Budget deficit of 14.9% of GDP in 2020 Is being followed by a further deficit of 14.7% of GDP in 2021. These deficits should have the result over the next year of forcing the US$ down against a broad range of currencies.

We expect the US$ to generally weaken against currencies such as The Pound Sterling and the Euro. We also expect it to weaken against the Australian dollar. It is possible that we will see the Australian dollar rise to 90 cents US$ over the period ahead. Remember this is because the US$ is going down. It is not only the A$ that will be going up.

Benchmark US, Euro Area and Australia Bond Yields



Source: Morgans, Factset

Over the next couple of years we expect to see a major sell-off in US treasuries, Australian treasuries and European treasuries.

For more economic coverage subscribe to our podcasts

Equity strategy – positioning for an economic restart

Despite the ASX 200 up +3.2% and Small Ords +2.3% in the first quarter of 2021 very few companies are trading higher post their February result. Performance has been concentrated in the reopening/cyclical sectors (Financials, Resources, Energy, Consumer Services, Travel). It's hard to argue against the market not moving higher from here given the avalanche of good news but corporate outlook commentary suggests companies and investors will take a cautious approach over the next few months - taking time to assess the impact of the sudden end to the fiscal/support measures (JobKeeper, Homebuilder scheme, and mortgage loan deferrals).

We see further upside in Banks/Financials driven by improving economic conditions, strong capital positions, sector over-provisioning and rising yields (Westpac, Macquarie). An overweight exposure to commodities (energy, metals, softs) via Resources/Ag stocks is supported by improving demand, supply-side constraints, investor fears of inflation and expected USD weakness (BHP, Santos, Strandline, Nufarm). Our Best Ideas profile several domestic cyclicals and small caps supported by their lower relative valuations and leverage to domestic activity (Corporate Travel, Sydney Airport, People Infrastructure). Market volatility also gives us the opportunity to target high quality names on weakness (CSL, Magellan, Next DC).

Tactics through abnormal markets

Ultimately we think investors need to be nimble across multiple themes (value, growth, yield, commodities, tech) as a bumpy road to recovery is likely to see valuations move through over-valued and under-valued territory. Equity investors need to consistently review their exposures, and to not be afraid to re-cycle profits into relatively cheaper opportunities which are regularly presenting in the current climate.

> The most likely outcome is that the virus is brought under control next year and the global economy continues to recover, which we think will help fuel further increases in equity markets.

Key sector outlooks

Category	Sector	Sector Rating (– to +)	Best Ideas	Analyst Overview
Financials	Banks	Improving	WBC	Recent results from the Banks have vindicated our positive views and we still think the market is too pessimistic on anticipated bad debts and asset quality. Capital and provisioning strength support the earnings and dividend outlook which should sustain the market's ongoing rotation into Banks which is well underway.
	Diversified Financials	Improving	MQG MAI MFG Z1P QBE KSL	A positive outlook is shaped by the economic recovery, improving macro settings (growth vs loose monetary policy) and improving sector risk appetite. A steady lift in bond yields would be broadly positive for the sector.
Defensives	Cons. Staples	Neutral	COL ING BGA	Demand looks set to remain solid as consumers and workers spend more time at home, however peak pandemic driven growth is behind us and the defensive nature of the sector may see it underperform during a cyclical recovery.
	Healthcare	Neutral	RMD M7T VHT	Market appetite for the defensive attributes of Healthcare stocks is fluctuating and has arguably peaked as we now recover from the health emergency. Nonetheless, several compelling and structurally driven opportunities remain.
	Telco	Positive	TPG NXT	Sentiment has turned the corner now that the NBN is practically complete, helping to settle down customer migration. Telcos also see an improving outlook in mobile as competitive activity becomes more rational.
	Infra and Utilities	Neutral	SYD DBI	Providers of critical services with regulated revenues (AST, SKI), resilient demand (AGL), or long-term take-or-pay contracts (APA) should remain in-demand. Ultimately, ultra-low interest rates can plausibly intensify the appeal of strong cash generators (SYD, TCL) once their volumes recover.
	A-REITs	Neutral	WPR AVN AQR HDN	Capital performance will fluctuate with bond rate expectations but REITs continue to offer attractive distribution yields to investors with the sector average around 5.5%.
Cyclicals	Consumer Disc.	Neutral	CTD BRG LOV APE UNI ALL BBN JIN	Ironically, the economic re-start poses a threat to consumer discretionary share prices. This is both from a valuation/sentiment perspective initially and from an earnings impact as consumer spending patterns find a new base. Significant value does remain in consumer services, particularly in Travel.
	Industrials	Improving	IPL PPE AQZ ANN ACF	Many companies maintained operations through various restrictions due to the essential nature of their products and services. We expect this resilience to continue in 2021, though the rising AUD is a headwind to watch.
	Online media	Deteriorating	FDV BKG	The end of lockdowns, permanent shifts in consumer behaviour and various governments in stimulatory mode will likely support further improvements in the end markets for the online leaders. This looks captured in near record share prices and we prefer smaller cap exposures.
	Agri-culture	Positive	GNC NUF	Following successive years of drought, far improved seasonal conditions and strengthening soft commodity prices (economic reflation, USD weakness) combine to offer strong sector tailwinds in 2021.
Resources	Metals & Mining	Improving	BHP STA RMS	An overweight exposure to commodities/Resources is supported by: improving demand in-line with the post-pandemic recovery; a highly resilient Chinese economy; genuine supply-side constraints influenced by capital discipline; emerging inflationary forces and US dollar weakness.
	Energy	Positive	STO KAR SXY	Our conviction in a sustainable oil market recovery is growing helped by steadily improving demand (global growth), declining inventories, US shale issues and a weakening US dollar. This paints a bullish 1-2 year outlook.

Negative   Deteriorating   Neutral   Improving   Positive

For more, see our Sector outlooks and strategies

Asset allocation – positioning for reflation

The tug of war between stronger economic growth, inflation and higher bond yields will guide asset allocation in 2021. We see the rapid rollout of the COVID-19 vaccine, accommodative monetary policy and additional fiscal support as underpinning risk assets over the next 6-12 months.

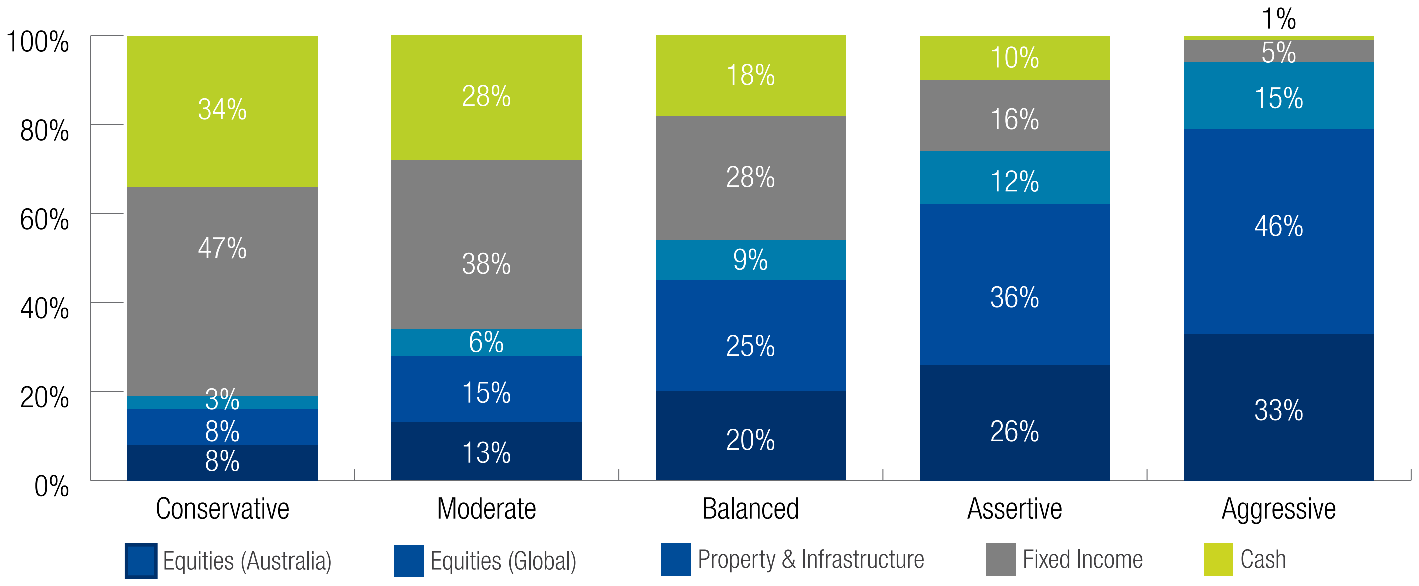
We maintain an overweight position to Equities favouring sectors and regions at the epicentre of the pandemic. We are neutral real assets (property and infrastructure) and maintain our underweight position in cash and income assets.

Although the incoming economic data is likely to remain poor until around mid-2021, we forecast that risk assets will continue to outperform defensive ones comfortably over the next couple of years. We also anticipate that this will be accompanied by a further rotation within risky asset markets – generally favouring the sectors and regions hit hardest at the start of the pandemic. We also expect continued weakness in the US dollar. The two key risks to these forecasts are that: i) the pandemic takes another turn for the worse over the next few months and a vaccine still takes a long time to develop, produce, and distribute; and ii) policymakers withdraw support prematurely, undermining the economic restart and the prospects for risky assets.

A restart rather than simply a recovery

We see the path out of the COVID-19 shock as a "restart" – not a typical business cycle "recovery". The key reasons are the distinct nature of the shock, broad-based pent-up demand and different inflation dynamics. The passage of the US$1.9trn fiscal package and an accelerating vaccination ramp-up in the US and Europe magnify these factors, and we believe the restart will likely be stronger than markets expect. The restart bolsters our pro-risk stance over the next six to twelve months, and makes us lean further into cyclical assets. We are overweight equities, and our preference is for small caps given their lower relative valuations and leverage to domestic activity. We see opportunities in emerging market (EM) equities, and see the recent selloff as an opportunity. We still expect EM equities to benefit from a global cyclical upswing, supported by a weaker USD. Elsewhere we are neutral real assets (property and infrastructure) as we see them offering some insulation against rising inflation down the road. An overweight exposure to commodities is also supported by several drivers including: improving demand in-line with the post-pandemic economic activity; a resilient Chinese economy; genuine supply-side constraints influenced by capital discipline among the majors producers; growing investor recognition of inflationary forces; and expected USD weakness.

Recommended asset allocation and tactical tilts



Source: Morgans

Benchmark long-term asset allocation and tactical tilts

	Conservative	Moderate	Balanced	Assertive	Aggressive	Tactical Tilts
Equities (Australia)	5%	10%	17%	23%	30%	3%
Equities (International)	7%	14%	24%	35%	45%	1%
Property & Infrastructure	3%	6%	9%	12%	15%	0%
Fixed Income	49%	40%	30%	18%	7%	-2%
Cash	36%	30%	20%	12%	3%	-2%

Source: Morgans

Category	Rating – +	Overview
Global Equities		Although we do not expect US bond yields to keep on climbing sharply, we think the recent "rotation" in global stock markets has further to run, given the upbeat prospects for the recovery in economies hardest hit by COVID-19. With governments more willing to deploy fiscal policy and central banks prepared to let inflation run hot, we think the reflationary economic backdrop will continue to favour being invested in global equities. The strengthening AUD will be a headwind for US exposure so tactically we prefer hedged exposures. Longer term as the effects of the pandemic fade, old problems will start to resurface. The biggest challenge facing advanced economies prior to the pandemic was the extremely weak rate of productivity growth across the developed world. This had several causes, including low rates of business investment and the failure of new digital technologies to feed through into broad-based rises in productivity.
Australian Equities		Australian equities have not been immune to rising bond yields in the global reflationary backdrop. Resources, Energy and Financials have benefitted from the bounce back in economic activity. The progress of the vaccine rollout sees Australia achieving herd immunity by October which could lead to earlier than anticipated relaxation of border re-openings. Household balance sheets are in great shape which should continue to support the recovery in consumption. We also see upside risks to dividends as uncertainty from the virus clears keeping payout ratios elevated. We prefer a targeted portfolio approach favouring reflation (Banks, Energy, Resources) and COVID-19 reopening beneficiaries (Travel, Gaming, Traditional Retail).
Fixed Income		We are strategically underweight nominal government bonds as their ability to act as portfolio ballasts are diminished with yields near lower bounds and rising debt levels may eventually pose risks to the low-rate regime. This is part of why we underweight government debt strategically. We prefer inflation-linked bonds as we see risks of higher inflation in the medium term. We are underweight long-term bonds on a tactical basis as we anticipate gradual increases in nominal yields supported by the economic restart. We are also underweight credit on a strategic basis as valuations remain elevated and we prefer to take risk in equities. On a tactical basis, credit, especially investment grade, has come under pressure from tightening spreads, but we still like high yield for income.
Infrastructure		A recovery in broader risk appetite should see infrastructure benefit relatively less than other assets. However, infrastructure is also an inflation-sensitive asset class with the opportunity for upside participation given the pass-through structure of many contracts. If inflation returns on better economic growth, it would be positive for asset class returns. We remain neutral infrastructure with a preference for assets better linked to economic activity such as tollroads, energy and data.
Property		We are neutral on the Australian property sector. While we are seeing some strength in housing and the industrial sub-sectors, the sector is a reopen area investors are shunning thus far. The uncertain environment for commercial real estate is justifiably the reason. Office buildings will likely suffer as companies allow work-from-home options and the population flees large cities. Likewise, the pandemic sped up the adoption of e-commerce, raising questions regarding the amount of needed retail real estate space. Additionally, with significant support measures rolling off in March (JobKeeper, repayment holidays) we could see a spike in bad and doubtful debts.
Cash		We use cash to fund overweight in equities. Holding some cash makes sense, in our view, as a buffer against supply shocks driving both stocks and bonds lower.

The Morgans Strategic Asset Allocation methodology takes a systematic approach in optimising exposure to the various asset classes at different stages of the Economic cycle. Refer to our full publication Asset Allocation Update - Q2 2021 for product recommendations

- Negative
- Deteriorating
- Neutral
- Improving
- Positive

Banks – results far better than expected

Results delivered by the major banks in February were better than our top-of-the-street expectations. We've consequently seen significant upgrades to consensus forecasts for all four majors. Yet we still think the market is too pessimistic, particularly on asset quality.

We see potential for credit loss provision releases for all four major banks over the remainder of this year for reasons previously detailed, but now including: 1) the Federal Government's announcement of targeted stimulus for the tourism sector; 2) the Federal Government's revised SME loan scheme; and 3) further decline in the unemployment rate and strength in the housing market.

Whilst the two key net interest margin headwinds continue to be the low interest rate environment and intense home loan competition, we do expect tailwinds to largely offset these including: 1) potential for continued strong growth in low-cost deposits if the RBA continues its bond buying program; 2) term wholesale funding maturities to be replaced with low-cost deposits and funding from the RBA's Term Funding Facility (TFF); and 3) reductions in term deposit rates.

The credit growth outlook is being supported by the Government's revised SME loan scheme. Furthermore, we believe a lower marginal cost of funding should allow the banks to regain mortgage market share from non-bank lenders.

From a CET1 capital perspective, we view the balance sheets of all four major banks as strong and we see potential for capital management for all four major banks over our forecast period. Capital strength and provisioning strength, together with an improving earnings outlook is supporting the dividend outlook for the sector. As bond yields rise, we expect the opportunity cost of holding low-yielding stocks to rise; this factor should be supportive of major bank valuations as bond yields rise.

Westpac remains our preferred major bank and CBA least preferred.

Ranking	Stock	Recommendation	Share Price	Target Price	Dividend Yield	Gross Yield	12m Forecast TSR
1	WBC	ADD	$24.34	$27.50	5.4%	7.8%	21%
2	ANZ	ADD	$28.17	$31.00	5.1%	6.7%	17%
3	NAB	HOLD	$26.17	$27.00	4.7%	6.6%	10%
4	CBA	REDUCE	$86.00	$68.00	3.7%	5.3%	-16%

Source: IRESS, MORGANS. Data at 31 March 2021.

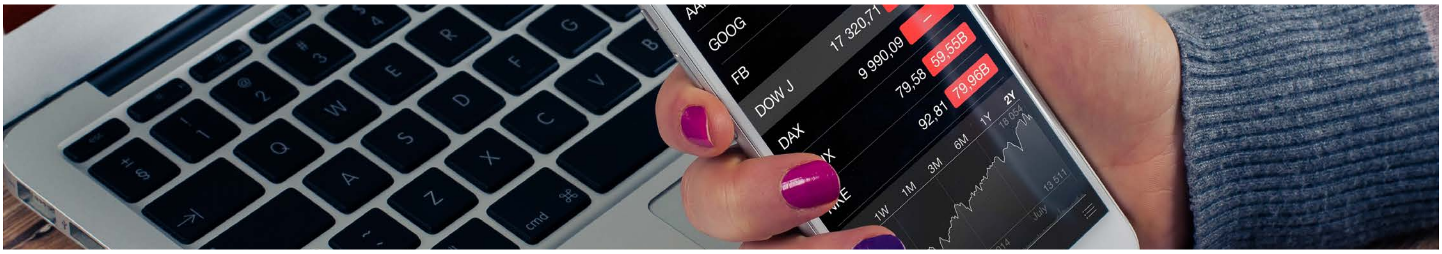
Recent publications

ANZ
ADD TP A$31.00
Further confirmation of positive themes

CBA
REDUCE TP A$68.00
Pleasing with positive read-throughs

NAB
HOLD TP A$27.00
Thematically encouraging

WBC
ADD TP A$27.50
Expect outperformance vs CBA to continue



Diversified financials – macro settings on the improve

The operating backdrop is becoming progressively more positive for the insurance and diversified financials sector. Positive tailwinds in the sector include: lower bad debt risks (for stocks with banking exposures), an improving economic outlook, heightened merger and acquisition activity, generally strong balance sheet positions (post capital raisings and COVID-19 provisions), and a recovery in investment markets and investor sentiment. With a supportive backdrop, valuations are generally reasonable and at a discount to the broader market versus historical averages.

Within the Wealth segment, improved investor sentiment is supportive for the outlook. **Challenger** is benefitting from signs of improving domestic sales trends and the ongoing deployment of excess capital into higher yielding assets to the benefit of margins. The Investment Platforms (**Netwealth, HUB24**) continue to capitalise on a very strong structural tailwind. Recently, some earnings uncertainty (around deposit rate earnings) has crystalised; however we ultimately see this as having a small dampening impact on a sustainable long-term growth profile. HUB24 is our preference in this segment.

Strong equity market have supported the earnings of fund managers; however sentiment toward **Magellan** has wavered. Investment performance is key for fund managers, however we think the emphasis on very recent underperformance of MFG's global fund (versus a strong cyclical rally) is overdone. We expect heightened M&A activity to persist. **Computershare's** recent acquisition of the Wells Fargo Corporate Trust business looks highly complementary to its existing operations and strongly EPS accretive.

Recent publications

Challenger
ADD TP A$6.72
Momentum should further improve in FY22

HUB24
ADD TP A$25.40
Capturing the long-term

Magellan Financial
ADD TP A$58.26
Bouncing around, but long-term remains solid

Resources and energy – refueling on fundamentals

An overweight exposure to commodities via the Resources sector is a core strategy in 2021. Upside pricing risk to commodities is supported by several drivers including: improving demand linked to post-pandemic recoveries; the strong Chinese economy; supply-side constraints influenced by COVID-19 and capital discipline among the majors; growing investor fear of emerging inflationary forces and anticipated US dollar weakness.

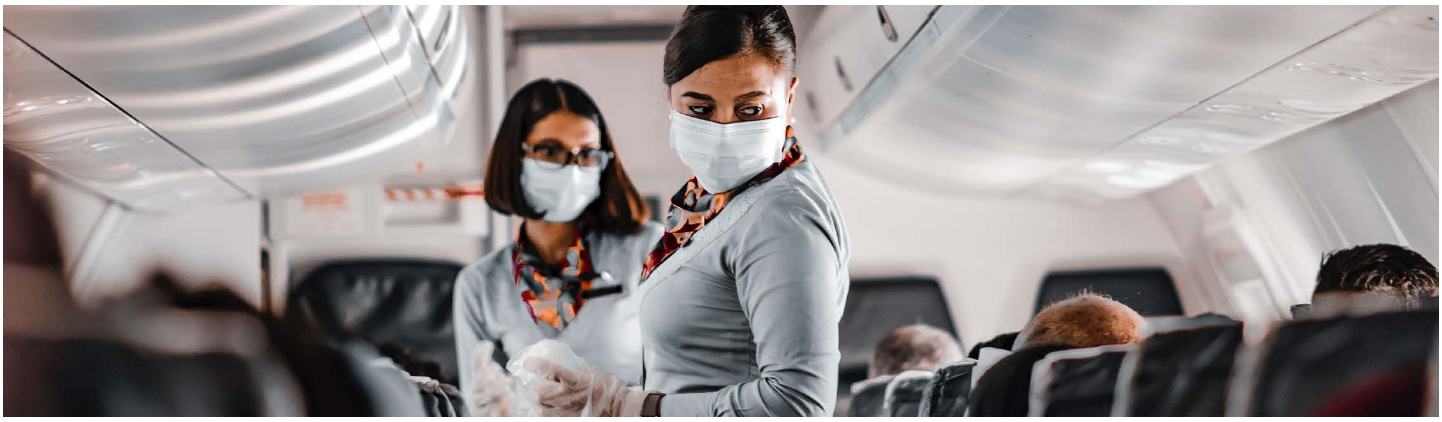
We see further upside in the energy/oil market, with potential for a supply squeeze that could push oil prices through US$80/bbl, as global stockpiles decline, fiscal stimulus continues and recovering US oil activity takes time to translate into added barrels. Volatility is unavoidable, but the fundamentals supporting higher oil prices increase our confidence that investors should buy the dips in energy stocks. Our key energy picks are **Santos, Karoon Energy** and **Senex**.

Strong fundamentals continue to align for copper and nickel demand from green policies. While copper benefits from electrification, we expect it to also benefit from global stimulus given the linkage to economic growth. Declining volumes from the major copper producing centres feed into a declining supply story at the same time as growing demand. We continue to screen opportunities outside the current ASX producers SFR and OZL, but advanced projects are few and far between. **Newcrest** and **Evolution Mining** both see significant copper revenues, with NCM expected to see nearly 30% of its revenue coming from copper in the next 2-3 years in our forecasts. Forecast weakening in the US dollar also offers upside to all gold producers.

Our key pick in the mineral sands space, **Strandline Resources**, is well placed to benefit from global stimulus spending. Titanium and zircon production from its developing Coburn project feed into the paint, pigment and ceramics markets, all strongly linked to construction and economic growth.

Recent publications

Oil & Gas
OPEC paves way for continuing recovery



Travel and tourism - vaccine success and borders reopening see travel stocks soar

The vaccine roll-out is supporting a domestic travel recovery. Capacity at Jetstar is at pre-COVID-19 levels demonstrating strong pent up leisure demand. However Qantas flags capacity at ~60% of pre-COVID-19 levels in the March quarter and ~80% by mid-year. The federal government's aviation support package will further support the recovery with 800,000 domestic fares at half price.

International travel is unlikely for the rest of 2021. New Zealand will provide detail on 6 April around a potential two way travel bubble with Australia that is quarantine free. Demonstrating that air traffic can recover, in China, domestic traffic is now only 3% below pre-COVID-19 levels. With COVID-19 cases now declining in the US and widespread vaccination underway, the travel stats continue to improve. The US President has said that all US adults will have the ability to be vaccinated by the beginning of May.

The March travel rebound has been significant enough that airline executives are recognising light at the end of the tunnel. Domestic traffic volumes are currently 40-45% below pre-COVID-19 levels and further improvement is expected during the all-important summer vacation period.

Overall, traffic across Europe is at about 35% of pre-COVID-19 levels. In the UK, the government had previously said that it may allow international travel from 17 May, however given recent rising cases across Europe and the impact of new variants, this timetable may be pushed out. The UK taskforce is due to publish its recommendations on 12 April. IATA said that daily bookings from UK to Greece and Spain for the summer period more than tripled following the news that UK set out a roadmap to ease lockdown restrictions. While over 50% of all adults in the UK have received at least one dose of the vaccine, Europe in general, has had a much slower rollout. However the European Commission says it remains confident that it can achieve its goal of having 70% of Europe's adult population vaccinated by the end of the summer.

Our key travel pick remains **Corporate Travel Management.**

Recent publications

Corporate Travel Management
ADD TP A$21.75
Well placed when borders fully reopen

Flight Centre Travel
HOLD TP A$19.21
Better than feared

Property – bond yields, reporting season, outlook mixed depending on asset sub-sector

Recent movement in bond yields has overshadowed the recent result season outcomes. Bond yields have risen from around 1.0% since the beginning of 2021 to around 1.7% but do remain historically low. Year to date the sector (on a total return basis) has substantially underperformed the market although performance has stabilised in March in line with bond yields.

REITs continue to offer attractive distribution yields to investors with the sector average around 5.5%.

Reporting season saw FY21 guidance reiterated or provided for the first time given further clarity on impacts from the Code of Conduct/COVID-19 on earnings. REITs have broadly offered DPS guidance with those providing no specific guidance largely focussed on CBD office/traditional retail malls (e.g GPT Group, Scentre Group and Vicinity). Better than expected results in February were largely driven by lower than forecast rental relief/write-backs (rent collection also trended up) as well as lower interest costs.

NTAs have been largely stable with retail valuation falls not as significant as previous periods and office valuations largely stable. REITs with exposure to office and traditional malls are currently trading at 15-25% discounts to NTA with some REITs including Dexus, Growthpoint and GPT Group announcing buy-backs. We expect that industrial/logistics as well as large format retail, convenience retail and self-storage will likely see some asset appreciation.

The growth REITs (i.e fund managers including Goodman and Charter Hall) reported solid results with improved FY21 guidance however underperformed the market due to rising bond yields although bounced back in March.

While there are ongoing structural headwinds for retail mall operators, based on recent results office metrics largely held up (although incentives are rising, particularly in Sydney and Melbourne CBDs). Leasing activity has picked up over the past six months off lows during COVID-19 which resulted in most weighted average lease expiry profiles remaining stable, however the key focus for many groups remains on near term leases expiring or vacancy.

There has been concern over impacts to office demand from the working from home thematic which accelerated over COVID-19, however we are yet to see any clear impacts. While many business have adopted a hybrid model (home and office) other industry commentary suggests a hub and spoke model may also be a compromise in the future. Tenants will also likely be seeking high-quality, technology enabled and wellness focussed buildings. We expect a successful vaccine rollout will improve sentiment around returning to the office environment as well as increased confidence in economic growth which would likely be positive for office markets.

Industrial/logistics metrics remain resilient with the sector in favour given the growing shift to e-commerce which has accelerated due to the pandemic. There has also been a focus on supply chain resilience given on the back of COVID-19. Commentary suggests that capital demand for the asset class is high which will likely result in further cap rate compression. Recent media reports flag the potential upcoming sale of the Milestone Logistics portfolio currently owned by Blackstone which may provide a guide of current valuations for long WALE industrial/logistic assets.

Overall, balance sheet gearing remains sound with debt costs low. Liquidity also remains high for most REITs with several undertaking capital raisings or asset sales over the past 12 months. Several groups have taken the opportunity to acquire assets/value-add existing assets and grow earnings (e.g. Centuria Industrial REIT, National Storage REIT) and some are using capacity for buybacks (eg Dexus and GPT Group).

On the back of government stimulus (eg Homebuilder) and ongoing record low interest rates, residential has seen strong improvements with margins remaining robust. Key exposures in the large cap environment include Mirvac and Stockland with both groups reinstating FY21 guidance with the results. Some stimulus packages will soon end (eg Homebuilder phase 2) which may lead to some moderation.

Near term unknowns and risks include: 1) movement in bond yields; 2) FY21 earnings impacts from Code of Conduct outcomes; 3) the general economic environment/recovery coming out of COVID-19/end of JobKeeper; and 4) impacts on leasing/rental markets.

Our preferred REITs under coverage are:

- **Specialised** - Waypoint REIT, APN Convenience Retail REIT (service station assets)
- **Diversified** - APN Industrial REIT (industrial/business parks); Home Consortium (funds management, convenience retail and health/ wellness)
- **Office** - Centuria Office REIT (metro office assets)
- **Retail** - Aventus Group (large format retail centres); HomeCo Daily Needs REIT (convenience retail)
- **Industrial** - Centuria Industrial REIT (pure play Australian industrial assets)

Recent initiations

Ansarada – ADD
PT A$1.55

AND is a global provider of cloud-based AI-powered virtual data rooms and material information platforms for secure end-to-end document and process management, supporting material transaction and governance outcomes for businesses throughout their lifecycle.

Booktopia Group – ADD
PT A$3.53

Booktopia is the leading domestic pure play online book retailer in the country, owning the booktopia.com, Angus & Robertson and The University Co-Op brands.

Dalrymple Bay Infrastructure – ADD
PT A$2.57

DBI holds the 99 year lease to the 85mtpa Dalrymple Bay Coal Terminal. DBCT is an open access export terminal located in central Qld servicing customers in the Goonyella coal system.

MAAS Group – ADD
PT A$3.23

MGH is a leading independent Australian construction materials, equipment and services provider with diversified exposures across civil, infrastructure, mining and real estate end markets.

HomeCo Daily Needs REIT – ADD
PT A$1.45

HDN is focussed on the ownership, development and management of convenience based assets. It is managed by HomeCo which was established in 2017 when a consortium acquired the former Masters Home Improvement real estate portfolio from Woolworths.

Morgans best ideas

Our best ideas are those that we think offer the highest risk-adjusted returns over a 12-month timeframe supported by a higher-than-average level of confidence. They are our most preferred sector exposures.

Key additions this month include **Frontier Digital** and **Dalrymple Bay Infrastructure.**

Refer to our **Updated Best Ideas** for more www.morgans.com.au/stockpicks

Company	Sector	Size	Risk	Price	12m price target	Dividend yield	Gross yield	12m TSR
Aristocrat Leisure (ALL)	Consumer Discretionary	Large	Moderate	$34.35	$37.31	1.3%	1.3%	10%
Coles Group (COL)	Consumer Staples	Large	Lower	$16.01	$19.45	3.9%	5.5%	25%
Santos (STO)	Energy	Large	Moderate	$7.10	$8.30	1.3%	1.3%	18%
Macquarie Group (MQG)	Financials	Large	Moderate	$152.83	$162.30	3.5%	4.2%	10%
QBE Insurance Group (QBE)	Financials	Large	Moderate	$9.62	$10.08	4.0%	5.1%	9%
Westpac Banking Corp (WBC)	Financials	Large	Lower	$24.41	$27.50	5.4%	7.8%	18%
BHP Group (BHP)	Materials	Large	Moderate	$45.30	$42.20	5.6%	8.0%	-1%
Sydney Airport (SYD)	Industrials	Large	Moderate	$6.19	$6.86	0.0%	-	11%
TPG Telecom Ltd (TPG)	Communication Services	Mid	Moderate	$6.33	$8.11	1.8%	2.6%	30%
Magellan Financial Group (MFG)	Financials	Mid	Moderate	$45.17	$58.26	4.5%	6.0%	34%
Ansell (ANN)	Health Care	Mid	Moderate	$39.24	$44.45	2.5%	2.5%	16%
ResMed Inc (RMD)	Health Care	Mid	Moderate	$25.25	$30.09	0.8%	0.8%	20%
NEXTDC (NXT)	Information Technology	Mid	Moderate	$10.42	$14.02	0.0%	-	35%
Incitec Pivot (IPL)	Materials	Mid	Moderate	$2.91	$3.25	2.7%	3.3%	14%
Lovisa (LOV)	Consumer Discretionary	Small	Moderate	$14.33	$17.95	1.8%	2.6%	27%
Corporate Travel (CTD)	Consumer Discretionary	Small	Moderate	$19.61	$21.75	0.0%	-	11%
Eagers Automotive (APE)	Consumer Discretionary	Small	Moderate	$13.98	$15.05	3.6%	5.1%	11%
Frontier Digital Ventures (FDV)	Communication Services	Small	Higher	$1.38	$1.64	0.0%	-	19%
Booktopia Group (BKG)	Consumer Discretionary	Small	Moderate	$2.45	$3.53	0.0%	-	44%
Breville Group (BRG)	Consumer Discretionary	Small	Moderate	$27.00	$33.90	1.0%	1.4%	27%
Jumbo Interactive (JIN)	Consumer Discretionary	Small	Moderate	$12.68	$14.78	2.6%	2.6%	19%
Baby Bunting Group (BBN)	Consumer Discretionary	Small	Moderate	$5.56	$6.39	2.4%	3.5%	17%
Universal Store (UNI)	Consumer Discretionary	Small	Moderate	$6.40	$8.37	4.1%	4.1%	35%
Bega Cheese (BGA)	Consumer Staples	Small	Moderate	$6.35	$6.80	1.7%	2.4%	9%
GrainCorp (GNC)	Consumer Staples	Small	Moderate	$5.25	$6.15	3.9%	4.6%	21%
Inghams (ING)	Consumer Staples	Small	Moderate	$3.34	$4.10	4.4%	6.2%	27%
Senex Energy (SXY)	Energy	Small	Higher	$2.90	$4.30	0.0%	-	48%
Karoon Energy (KAR)	Energy	Small	Higher	$1.08	$1.70	0.0%	-	57%
Mainstream Group (MAI)	Financials	Small	Moderate	$1.21	$1.20	0.4%	0.4%	0%
Zip Co (Z1P)	Financials	Small	Higher	$7.38	$12.10	0.0%	-	64.0%
Kina Securities (KSL)	Financials	Small	Higher	$0.93	$1.64	10.6%	10.6%	87.1%
Volpara (VHT)	Health Care	Small	Higher	$1.30	$1.94	0.0%	-	48.9%
Mach7 Technologies (M7T)	Health Care	Small	Higher	$1.32	$1.68	0.0%	-	26.9%
Acrow (ACF)	Industrials	Small	Higher	$0.37	$0.53	5.4%	7.8%	48.7%
People Infrastructure (PPE)	Industrials	Small	Moderate	$3.73	$4.22	3.6%	5.1%	16.7%
Alliance Aviation Services (AQZ)	Industrials	Small	Higher	$3.93	$5.25	1.6%	2.3%	35.2%
Dalrymple Bay Infra. (DBI)	Industrials	Small	Moderate	$2.20	$2.55	8.3%	8.3%	24.2%
Nufarm (NUF)	Materials	Small	Moderate	$5.31	$5.10	0.4%	0.6%	-3.6%
Strandline Resources (STA)	Materials	Small	Higher	$0.20	$0.44	0.0%	-	120.0%
Ramelius Resources (RMS)	Materials	Small	Higher	$1.48	$2.27	1.3%	1.3%	54.9%
HomeCo Daily Needs (HDN)	Real Estate	Small	Moderate	$1.27	$1.45	3.3%	3.3%	17.6%
APN Conv. Retail REIT (AQR)	Real Estate	Small	Lower	$3.42	$4.01	6.4%	6.4%	23.6%
Aventus Group (AVN)	Real Estate	Small	Moderate	$2.88	$2.90	5.9%	5.9%	6.5%
Waypoint REIT (WPR)	Real Estate	Small	Lower	$2.51	$2.94	6.3%	6.3%	23.3%

Source: Morgans. Data as at 31 March 2021.

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