20 August 2021

MARKET UPDATE

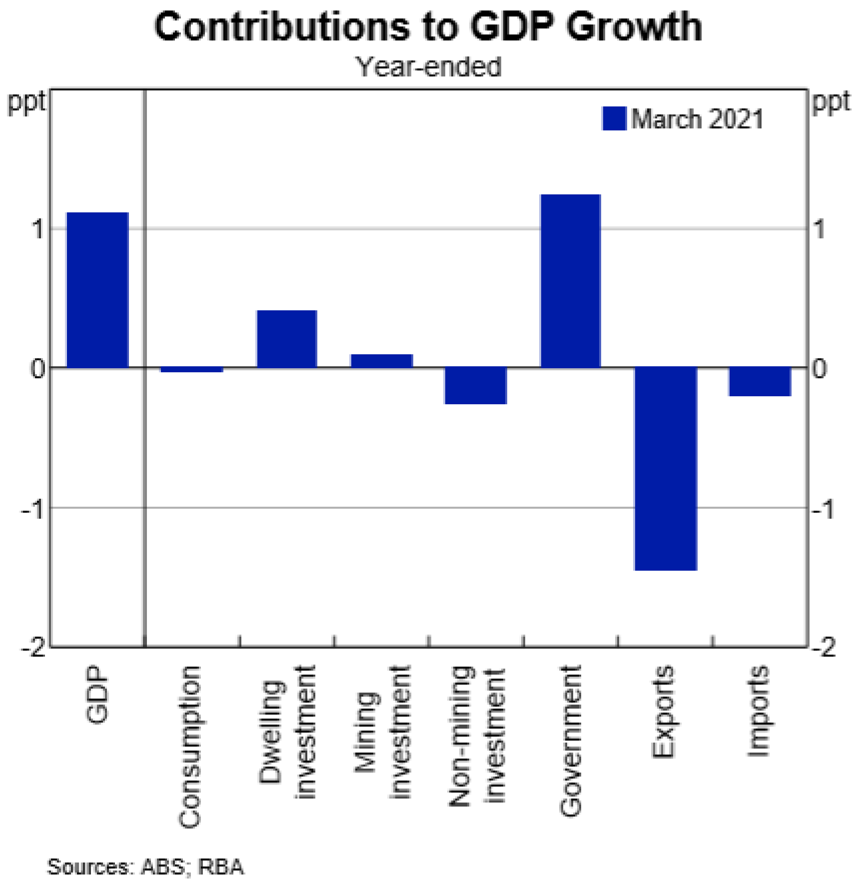
Weekly Update

Woodside want to be the Big Banana

The big news this week was the Woodside Petroleum/BHP Petroleum tie up which I'll get onto later in the report. But the oil and gas space is already consolidating here; first Santos and Oil Search getting together, now Woodside is buying BHP's Petroleum division. Is Beach Petroleum at risk of takeover?

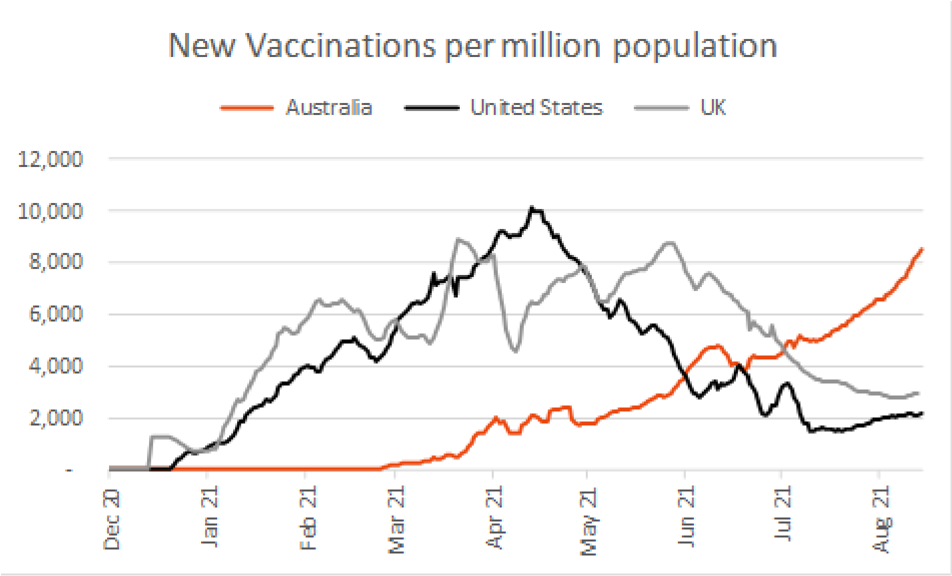
The market slipped for the first time this week since early July, falling 2.2% to 7461. Australia's unemployment rate fell from 4.9% to 4.6%, but the participation rate also fell marginally from 66.2% to 66% and underemployment rose from 7.9% to 8.3%.

What concerns me though is this next chart.



Almost all GDP growth is attributable to Government expenditure and to a lesser extent, but just as worrying, the housing boom (dwelling investment). Yes the latest figures are only to March, but our GDP growth is unsustainable if we are relying on Government spending to dig us out. We need to make headway elsewhere, and the systematic destruction of business, children's education and everyone's minds and souls in the forever lockdown, sure won't get us there.

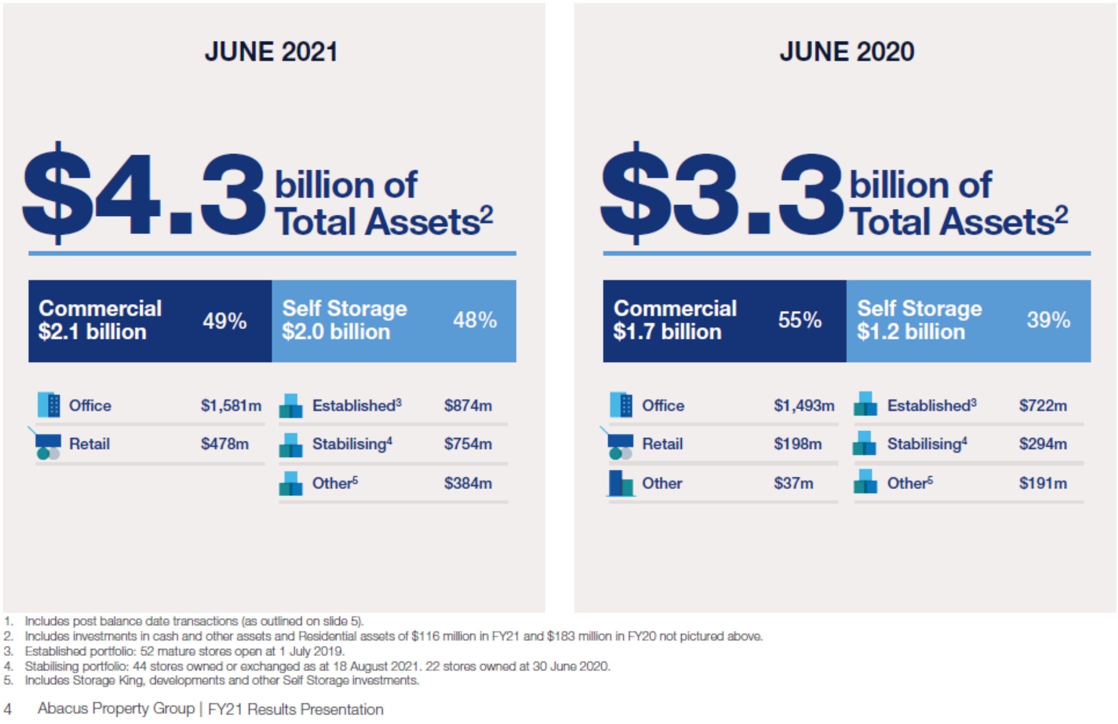
At least our rate of vaccinations is increasing.



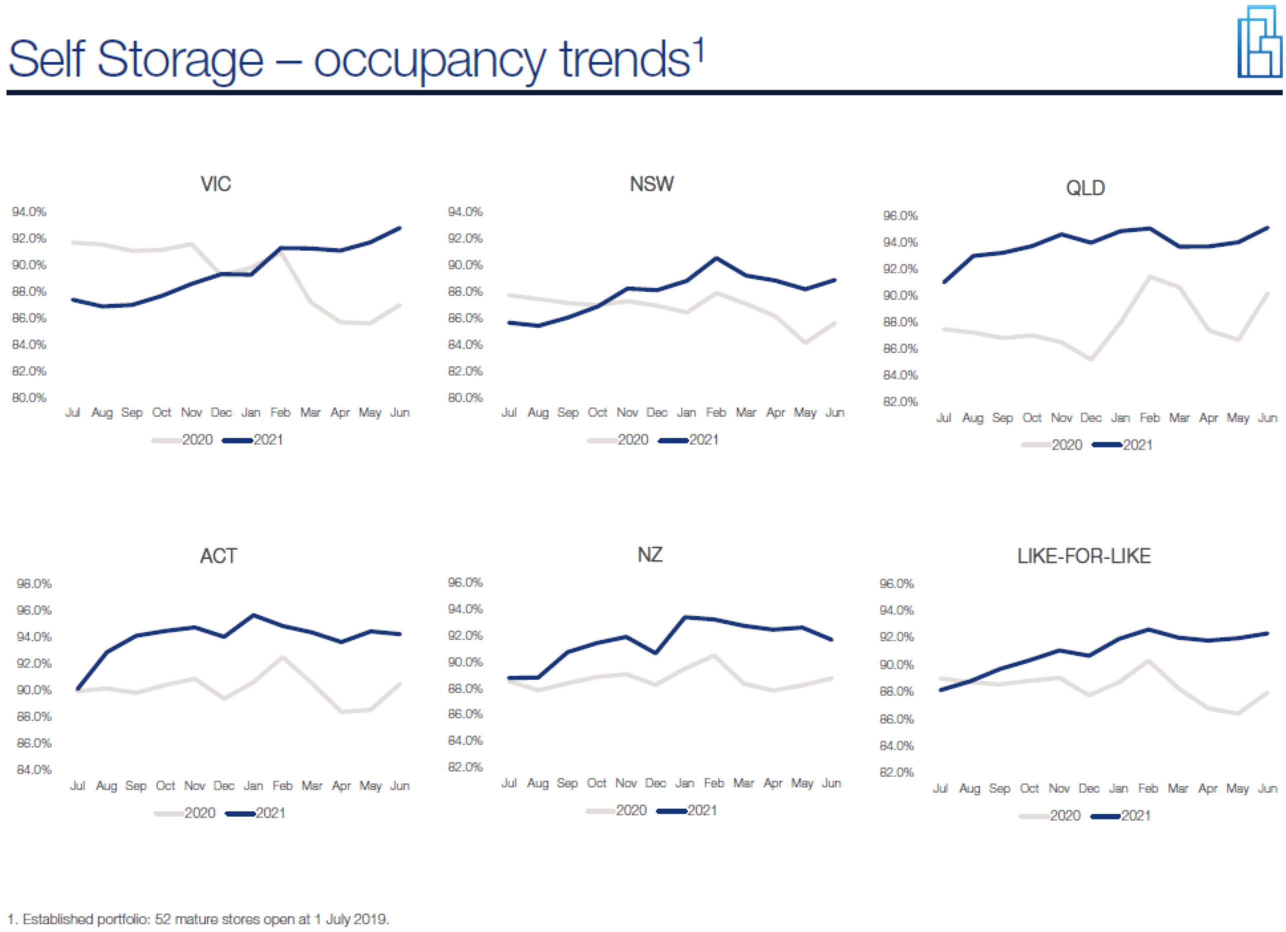
Abacus Property Group (ABP)

ABP, the Storage king and office property group has released a strong result for FY21 this week, achieving a surprisingly large growth in assets and a small lift in distributions versus expectations (albeit down 1 cent from last year).

Total Assets have risen from $3.3bn in FY20 to $4.3bn, lifting NTA to $3.43 due to both valuation increases and acquisitions.



How good is storage unit occupancy levels…



ABP is another of our property groups trading at a discount to a quality asset base, low levels of debt, excellent management and a 5.3% yield.

Shaw and Partners have now taken up coverage of ABP. See latest report below

[Abacus Property Group - A Store of Wealth – Initiation of Coverage - 17 Aug 2021]

Dalrymple Bay Terminal (DBI)

As part of their site expansion, DBI announced the signing of a Memorandum of Understanding (MOU) to study the potential for a hydrogen production and storage export facility at the terminal. Times change and it’s pleasing to see management within a business that’s operated for 40 years profiting from the movement and storage of mineral resources moving into other potential areas of growth.

Early doors but an interesting development.

See link to announcement here.

Carbonxt Group limited (CG1)

After so many years in the wilderness, CG1 is now generating far more demand for their products that remove pollutants and toxins in multiple industrial processes.

Now profitable, CG1 yesterday announced a further rise in revenues and are on target to achieve over $4.2m for this quarter- a 56% rise on the previous $2.7m.

The pandemic certainly impacted CG1’s demand over the past 12 months, but as the US opens up more and more, demand for both Powdered Activated Carbon (PAC) and Activated Carbon (AC) pellets has grown and continues to do so.

CG1’s most recent development, Hydrestor pellets, which are used to remove algal bloom causing phosphorous and nitrogen run-off, is also close to its first commercial arrangement.

See link to announcement here.

Woodside Petroleum (WPL) and BHP

Firstly results.

WPL announced a disappointing result with 1H21 NPAT >20% below consensus due to higher ‘other costs’.

- 1H21 EBITDA $1,531m vs consensus $1,619m
- 1H21 Underlying NPAT $354m vs consensus $464m
- 1H21 Dividend: 30 US cents per share (cps) vs consensus 32cps
- 1H21 Free cash flow $311m vs consensus $401m

BHP announced a pleasing result, record dividend, second highest ever earnings, massive reduction in debt, a removal of their listing in London and a move into potash and battery metals and away from energy.

- FY21 EBITDA US$37.4bn vs consensus US$37.25bn
- FY21 Underlying NPAT US$17.1bn vs consensus US$17.46
- FY21 Dividend: 301 US cps vs consensus 289 US cps
- FY21 Free cash flow US$27.2bn vs consensus US$25.8bn

And the merger

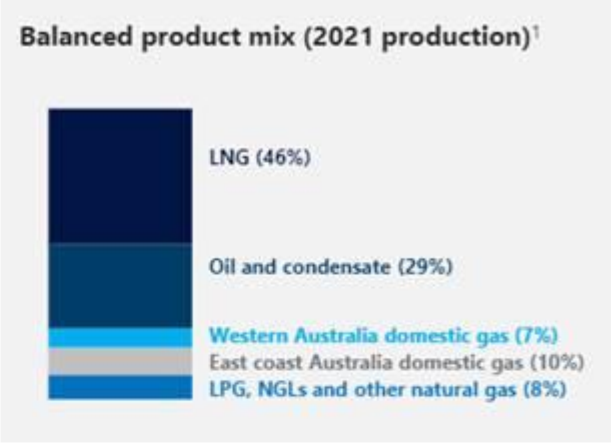
BHP Petroleum / WPL merger - some numbers

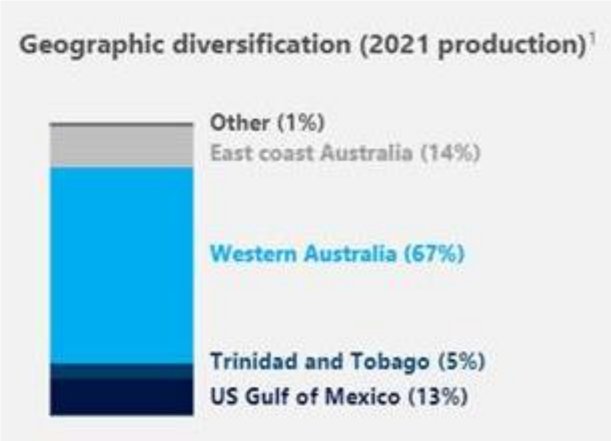
- An all scrip merger owned 52% by WPL shareholders and 48% by BHP shareholders.
- Total market capitalisation of ~A$41B.
- Production of approximately 200 million barrels of oil equivalent (~200mmboe), which places it in the top 10 independents globally.
- Reserves of more than 2Bboe; that’s a 20-year reserves life.
- WPL has highlighted annual synergies of >$US400m.
- WPL gearing will fall to 12%, from 23% currently, and operating cash flows of more than $US3 billion, from revenues that would top $US8 billion.

Merger timeline and key risk

- WPL is aiming to execute a full sale agreement by Oct-21, shareholder approvals early 2022 & completion by 2Q22.
- The key risk is WPL shareholders may reject the merger. They will need 75% shareholder approval for the merger to proceed. Shareholder approval risk is partly mitigated by the option BHP has to sell its interest in Scarborough for $1bn.

WPL's product mix

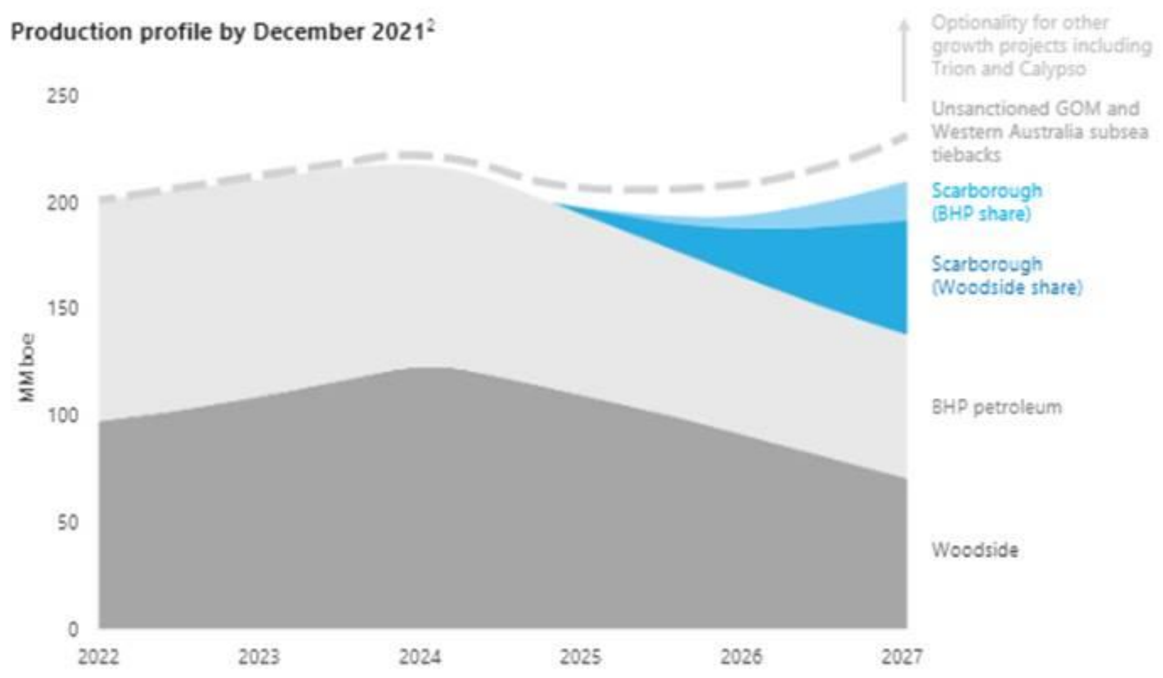




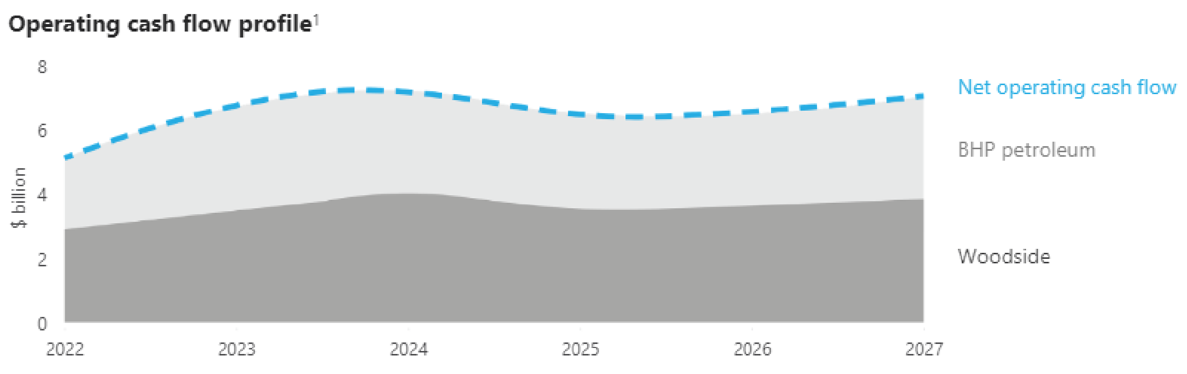
I like the deal. It looks good for BHP as they are pursuing their goal of exiting fossil fuels and focusing on battery metals, potash and iron ore in the future. It's good for WPL as they access world class petroleum assets, excellent cashflow to bridge their cashflow deficit over the coming 3 years and reduce their gearing to 12%.

Both stocks have been flogged; BHP down 15% over the last week and WPL 11%. I've been anticipating weakness in BHP for some time due to the declining iron ore price, but this sell down is beyond the speed of even my pessimistic thoughts and seems more to do with the cancellation of the listing in the UK.

BHP looks to be getting back to a price where it belongs and WPL looks excessively cheap.



WPL's production/cashflow profile



Beach Energy Limited (BPT)

BPT FY21 - production is decreasing, capex and costs are increasing

A difficult year for Beach Energy which sees the stock trading close to four-year lows. The company reported Underlying NPAT of $363m (-37% on previous corresponding period-pcp) and a NPAT of A$317m (impacted by A$117m of pre-tax impairments on its South Australian assets).

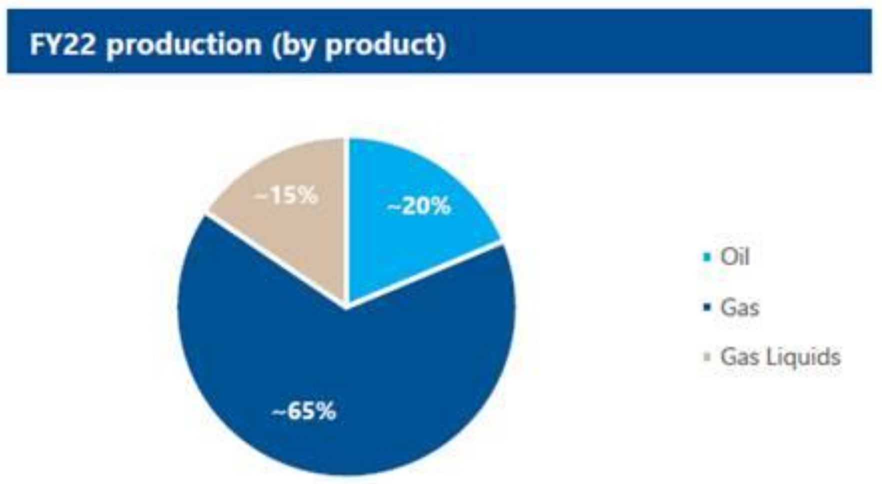
The weaker result vs pcp is driven by lower sales volumes (-6% vs pcp to 26.1mmboe). The lower sales volumes are primarily attributed to weaker production from its flagship Western Flank asset (-12% yoy to 8.5mmboe), which was flagged in a business update in April. Weaker production from Western Flank also led to an increase in unit production costs for the year (US$10.2/bbl from US$9.0/bbl).

The final dividend of 1cps is in line with consensus expectations, and the balance sheet is steady with net debt of A$48m (from A$46m 1H21).

FY22 guidance is for weaker production and increased capex and costs.

This result was not unexpected, but the magnitude of the selldown is vastly more excessive than I anticipated.

BPT has fallen from a market capitalisation of $5bn to $2.5bn since January as a result of these Western Flank issues, and although lacking in near term growth, a Price/Earnings (PE) ratio of 6 times is too cheap.



Have a great weekend,

Ben and the team

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