Stocks Down Under

I shave without using shaving cream.

- Jerry Stiller (1927-2020), American comedian, actor and author

SEVEN GROUP HOLDINGS

Mixed bag of growth opportunities

WEBJET

In bed with a smile

SHAVER SHOP GROUP

Silky smooth micro cap gem

SEVEN GROUP HOLDINGS

Mixed bag of growth opportunities

Stocks Down Under rating: ★★★★

ASX: SVW
Share price: A$ 14.00
Market cap: A$ 4.7BN

Sydney-based Seven Group Holdings is a diversified operating and investment group focused on the global media, mining and construction industries. Roughly three-fourths of its assets are in the industrial services industry. This includes WesTrac, one of the largest Caterpillar dealers in the world, which supports customers in Australia's rich iron ore and thermal coal regions. The investment company has a strong balance sheet, which allows it to pursue growth opportunities in core and adjacent businesses. Its market leading businesses combined with founder Kerry Stokes' well-regarded investment acumen bode well for delivering long-term shareholder value.

READ MORE

WEBJET

In bed with a smile

Stocks Down Under rating: ★★★★

ASX: WEB
Share price: A$ 3.25
Market cap: A$ 1.1BN

When we last looked at the Melbourne-based travel company Webjet in Stocks Down Under the world was a very different place. It was 31 January and most investors (including the team here at Stocks Down Under) thought that the Wuhan Coronavirus would just be a re-run of the 2002 SARS outbreak. Webjet was trading at $12.01 and we said it was a 4-star stock. Lee, who is one of our valued Stocks Down Under subscribers, has asked for an update, and we're happy to oblige because at the current level of just over $3.00 we still think this is a 4-star stock…and then some.

READ MORE

SHAVER SHOP GROUP

Silky smooth micro cap gem

Stocks Down Under rating: ★★★★

ASX: SSG
Share price: A$ 0.43
Market cap: A$ 53.7M

Melbourne-based Shaver Shop Group is a specialty retailer of male and female personal grooming products. With 120 owned and franchised stores across Australia and New Zealand in addition to an e-commerce presence, the company is aiming to become the market leader in "all things related to hair removal". Shaver Shop has experienced a downturn during the COVID-19 crisis amid store closures and reduced discretionary spending on certain health and beauty products. Given its booming online business and increasing interest in grooming among men and women (and especially millennials) Shaver Shop, we believe is well positioned to grab market share.

READ MORE

SEVEN GROUP HOLDINGS

Mixed bag of growth opportunities

Stocks Down Under rating: ★ ★ ★ ★

ASX: SVW
Share price: A$ 14.00
Market cap: A$ 4.7BN

Sydney-based Seven Group Holdings is a diversified operating and investment group focused on the global media, mining and construction industries. Roughly three-fourths of its assets are in the industrial services industry. This includes WesTrac, one of the largest Caterpillar dealers in the world, which supports customers in Australia's rich iron ore and thermal coal regions. The investment company has a strong balance sheet, which allows it to pursue growth opportunities in core and adjacent businesses. Its market leading businesses combined with founder Kerry Stokes' well-regarded investment acumen bode well for delivering long-term shareholder value.

Share price chart

Source: Tradingview

Infrastructure spending to support Coates Hire growth

Back in 2008, Kerry Stoke's National Hire Group merged with the hire business of equipment rental company Coates to form Coates Hire. Coates Hire has grown to become Australia's largest industrial and general equipment hire company with over 160 branches nationwide. We believe it has good long-term potential given the domestic outlook for infrastructure spending. Infrastructure activity is forecast to improve starting in FY21 especially in engineering construction and non-residential construction. The current pipeline of committed government projects is robust and includes extensions at Western Sydney Airport, WestConnex, and Snowy Hydro 2.0. Coates Hire has invested in its fleet in anticipation of the increased demand to position itself for market share gains.

Westrac and Coates Hire have been capturing market opportunities and have strong growth prospects ahead, in our view, as they continue to become involved in new mining and infrastructure projects. Westrac should continue to see strong demand for support due to demand for parts and rebuilds. This will be driven by higher mining equipment utilisation, equipment life extensions, and the increasing average age of its customers' fleets. Several major projects are already underway, and the group has additional opportunity through Perth iron ore company FMG's Eliwana and Iron Bridge projects as well as British mining company Glencore's United Wambo joint venture. Automation is another area where Westrac is investing because Australia has the world's largest fleet of autonomous mining equipment. It is planning to build the world's second Caterpillar autonomous training facility in WA.

Beach Energy offers upside

The energy side of the business, Seven Group's next largest segment, includes the fully owned SGH Energy which holds several oil and gas interests including 15% of the Crux LNG Project. It also holds a 28.6% stake in Beach Energy, a leading exploration and production (E&P) business and key gas supplier to the growing east coast market. The stake in Beach Energy has the potential to generate significant upside for the group because growing demand for gas on the East Coast and domestic LNG export opportunities. The 9-well offshore Victorian Otway drilling program launched in March 2020 following a strong interim period when it participated in 105 wells at an 83% success rate. Moreover, the first gas well at Katnook and Black Watch are expected in Q3 and Q4 respectively. Seven Group's Beach Energy investment has a market value of $1.63bn, which is more than twice its book value.

Blue Horseshoe loves Seven West Media

The 40%-owned Seven West Media (ASX:SWM) segment is one of Australia's leading diversified media companies. As we wrote in Stocks Down Under on 31 March, we quite like SWM. It has a monthly national audience reach of 17.7m through Seven Network and 8m through 7Digital and has media interests through Chinese private equity funds. Despite having the top free-to-air (FTA) television market share at 38.8%, a decline in FTA television has negatively impacted Seven Network results. Market conditions have soured and FTA ratings suffered amid changing viewership habits that are more focused on digital media. The Metro FTA ad market was down 7% in 1HY20 resulting in 3.2% lower group revenue. Divestment in other media areas has begun as seen with the recent $28m radio assets sale and sale of offshore China media funds.

Flexibility to re-deploy equity portfolio is a strength

The unwinding of Seven Group's investment in China media demonstrates the company's ability to easily deploy its equity portfolio into new investments. Funds invested in offshore Chinese media funds have benefitted from growth in the country's media, entertainment and technology sectors since the initial investment in 2013. As market conditions change and investments lose value, Seven Group has the financial strength and prudence to lock in portfolio gains and rotate into better growth opportunities.

Seven Group's core industrial services business should continue to benefit from a strong outlook for mining production and infrastructure investment. Solid East Coast gas demand and new LNG export projects should also contribute to growth. Management's outlook for FY20 includes underlying EBIT growth in the high single digits. The company looks well positioned to meet or exceed this guidance and to benefit from multiple catalysts in FY21 and beyond. The shares are trading at a P/E of 10.9x and an EV/EBITDA of 7.9x, both for FY21, which starts in July. They offer a yield of around 3%. All in all, we believe the picture for Seven Group looks quite compelling.

WEBJET

In bed with a smile

Stocks Down Under rating: ★★★★

ASX: WEB
Share price: A$ 3.25
Market cap: A$ 1.1BN

When we last looked at the Melbourne-based travel company Webjet in Stocks Down Under the world was a very different place. It was 31 January and most investors (including the team here at Stocks Down Under) thought that the Wuhan Coronavirus would just be a re-run of the 2002 SARS outbreak. Webjet was trading at $12.01 and we said it was a 4-star stock. Lee, who is one of our valued Stocks Down Under subscribers, has asked for an update, and we're happy to oblige because at the current level of just over $3.00 we still think this is a 4-star stock…and then some.

Share price chart

Source: Tradingview

Okay, back in January we were wrong. Coronavirus turned out to be a big deal after all, and yeah, we all know that Covid-19 has been really bad for travel. But get this: Shanghai Disneyland just re-opened on 11 May. To us that was the first major sign globally that travel was set to make a comeback – not with a bang but slowly and steadily. If you want further proof of travel doing a Lazarus check out the 12 May 2020 article by Hillary Leung in Time headlined 'Asia is slowly beginning to reopen travel. Here's what the world could learn'.

If there's one thing that's certain about the modern global economy, it's relentless growth in the number of trips people take both for business and pleasure. Consider that between 2004 and 2018 there wasn't a down year in global air passenger numbers and the average growth in any one year was 5.8%. The end of Covid-19 won't change that. Indeed, we predict faster-than-usual growth in 2021 as people catch up on trips they couldn't take during the Plague Year.

It’s not Webjet, it’s WebBeds

When people do start traveling again en masse, both domestically and internationally, certain companies will be well placed to succeed because of the power of their core businesses. We believe one of them is Webjet. Actually, the company should change its name because Webjet is no long really about its foundation Online Travel Agency, even though that business still makes good money for the company. What you’re really buying this stock for is WebBeds, an online B2B supplier of hotel rooms to the travel trade, which Webjet started from scratch in 2013 and then grew to a very large scale.

WebBeds, which is now around 60% of Webjet’s EBITDA in a normal year, is now the second largest player in the world in B2B accommodation, after the Spanish company Hotelbeds. And being a strong No. 2 brings certain advantages because hotel property owners like not having to kowtow to No. 1 all the time. The December 2019 half yearly result showed how the game works when Webjet was able to talk about market share gains for WebBeds in all regions.

A Crisis is a terrible thing to waste

When you think about it, this Crisis is the best thing to have happened to Webjet since its 1998 founding. Before the acquisition of Destinations of the World in late 2018 Webjet had also bought Sunhotels in 2014 and JacTravel in 2017, so CEO John Guscic and his colleagues know a thing or two about acquisitions and their subsequent integration. In 2020 the price that Webjet will have to pay to acquire other businesses in bed banking is substantially lower than just a few months ago.

And as lesser players are weakened thanks to their businesses being forcibly idled for months on end, Webjet as of last month has $346m in new funding that will keep its own doors open until the end of the calendar year, even under really tight travel restrictions globally. Okay, the deal got done at $1.70 a share, but at that price Webjet will be well placed to reward its shareholders as it comes out of this Crisis stronger.

We consider calendar 2020 a lost year. But looking at FY22, that starts in July next year, you can currently get Webjet for a P/E of just 15.1x and an EV/EBITDA of 8.4x. We believe that’s not expensive for a digital business with a track record of strong growth as solid as Webjet’s.

SHAVER SHOP GROUP

Silky smooth micro cap gem

Stocks Down Under rating: ★★★★

ASX: SSG
Share price: A$ 0.43
Market cap: A$ 53.7M

Melbourne-based Shaver Shop Group is a specialty retailer of male and female personal grooming products. With 120 owned and franchised stores across Australia and New Zealand in addition to an e-commerce presence, the company is aiming to become the market leader in “all things related to hair removal”. Shaver Shop has experienced a downturn during the COVID-19 crisis amid store closures and reduced discretionary spending on certain health and beauty products. Given its booming online business and increasing interest in grooming among men and women (and especially millennials) Shaver Shop, we believe is well positioned to grab market share.

Share price chart

Source: Tradingview

Healthy demand for health and beauty products

The health and beauty industry is witnessing a growing interest in overall health and beauty. Strong market demand for salon quality personal care products that can be applied in the home is based on an underlying desire on the part of consumers to look and feel good. One of the most prevalent trends, especially among millennials, is the increasing acceptance for men to have health and beauty regimens that are similar to those that have existed in women for decades-- things like hair trimming, hair removal and skin care.

The Shaver Shop brand is a strong asset for the company because it has been solely focused on the health and beauty sector for more than 30 years. It offers a wide range of products including electric shavers, clippers, trimmers, hair styling, female hair removal and wet shave items. No direct competitors offer such variety. It aims to establish itself as an expert in the products it sells by providing a superior customer service experience. Given its well-established supplier relationships, Shaver Shop gains exclusive access to many new products. Brand awareness is strong and the company has a good reputation with consumers.

Buying back franchises, adding new stores

The company has tried unsuccessfully to implement a franchise business model. It is instead buying back franchises as part of its organic growth strategy rather than making acquisitions. A modest number of new stores are being opened and at the same time remaining franchises are being bought back at attractive earnings multiples. E.g. in early FY20, Shaver Shop bought two franchises in the Hornsby (NSW) and Doncaster (VIC) shopping centres.

This two-pronged approach will allow it to gradually expand its geographic footprint while maintaining a consistent retail presence and customer experience. Shaver Shop's goal is to reach over 140 stores across Australia and New Zealand.

Building off the momentum of 2HY19, the results for 1HY20 were strong as the company delivered record sales and EBITDA. Sales increased 12.3% to $107.5m driven by a 61% surge in online sales. EBITDA grew 16.8% to $12.9m aided by a gross margin that was about 100 basis points lower than 1HY19, but still a robust 41.7%. Shaver Shop had a low level of gearing prior to the coronavirus crisis in addition to a net cash position of $8.4m. The combination of its conservatively managed balance sheet and robust operating cash flow supported the Board's decision to increase its dividend by 7.6% in 2019.

As economic conditions improve post-COVID-19, we believe Shaver Shop has the potential to capitalise on new sales channels. As part of its omni-channel strategy, physical stores will remain at the core because its products are very personal in nature and often require guidance from in-person experts. This is an advantage over many competitors that operate online-only businesses. Shaver Shop is now entering the next chapter of its history in trying to replicate its store success on its e-commerce platform. Management has said it expects the online side of the business to grow to 18% to 20% of overall sales over the next three to five years. We believe the company should be able to easily surpass this target considering online sales were already 17.6% of total network sales in 1HY20.

Large and growing market opportunity

Shaver Shop has significant room for growth in the years ahead, in our view, because the personal grooming and hair removal market is large and expanding. Based on its current product offerings, the company estimates the combined retail sales of its market segments to be over $1bn annually in Australia alone. Meanwhile, the New Zealand market is experiencing solid growth of its own.

Shaver Shop's history in the health and beauty space, brand recognition and strong supplier relationships place it in a unique position, in our view, to gain market share as the industry continues to grow.

The shares offer a dividend yield of almost 11%, trade at a low P/E multiple of 5.9x and an EV/EBITDA of 5x FY21. Although this is a micro-cap company, it looks rather beautiful at current levels.

Pitt Street Research Pty Ltd

95 Pitt Street, Sydney, NSW 2000, Australia

Pitt Street Research Pty Ltd is founded on more than 40 years of combined experience researching companies in a range of different sectors.

Stocks Down Under (Pitt Street Research AFSL 1265112) provides actionable investment ideas on ASX-listed stocks. The Content has been prepared for general information purposes only and is not (and cannot be construed or relied upon as) personal advice nor as an offer to buy/sell/subscribe to any of the financial products mentioned herein. No investment objectives, financial circumstances or needs of any individual have been taken into consideration in the preparation of the Content. Financial products are complex, entail risk of loss, may rise and fall, and are impacted by a range of market and economic factors, and you should always obtain professional advice to ensure trading or investing in such products is suitable for your circumstances, and ensure you obtain, read and understand any applicable offer document