



# Small Cap Stocks Down Under

📖 *Who in the world am I? Ah, that's the great puzzle!* 📖

- Charles Dodgson (1832 - 1898), Author of Alice's Adventures in Wonderland



**BELL  
FINANCIAL  
GROUP**

The Bell of profit  
sounds for us

**STEAMSHIPS  
TRADING  
COMPANY**

A slowly sinking ship

**MCPHERSON'S**

Not beautiful enough

# BELL FINANCIAL GROUP

The Bell of profit sounds for us

---

Stocks Down Under rating: ★★☆☆

**ASX: BFG**

**Market cap: A\$ 571M**

**Dividend yield: 5.9% (100% Franked)**

**52-week range: A\$1.015 / A\$2.02**

**Share price: A\$ 1.78**

Headquartered in Victoria is a company whose name might ring a bell. The Bell Financial Group is a provider of stockbroking and financial advisory services to private, institutional, and corporate clients. The company operates through 14 offices in Australia, New York, London, Hong Kong, and Kuala Lumpur. Bell's stock finished 2020 strong, ending up 160% from its March low of \$0.65 per share. However, it is currently going through a slight pullback, which we believe is a call to action.

[READ MORE](#)

# STEAMSHIPS TRADING COMPANY

A slowly sinking ship

---

Stocks Down Under rating: ★★

**ASX: SST**

**Market cap: A\$ 292M**

**Dividend yield: 2.5% (0% Franked)**

**52-week range: A\$9.00 / A\$10.00**

**Share price: A\$ 9.40**

Headquartered in Port Moresby, Papua New Guinea, is a company whose fate seems tied to the economy of its host country. The Steamships Trading Company's name mind brings back memories of a bygone era where steamships were the main mode of water transport. Unfortunately, we believe this is actually an accurate representation as the company has not seen revenue growth since 2014, a bygone era. Compounding the problem is the decline in profits from 2012 through 2020. Unfortunately, we believe last year's increase in profits was a one-off and this temporary gain will not help right the ship.

[READ MORE](#)

# MCPHERSON'S

Not beautiful enough

---

Stocks Down Under rating: ★★

**ASX: MCP**

**Market cap: A\$ 182M**

**Dividend yield: 7.4% (100% Franked)**

**52-week range: A\$1.12 / A\$3.40**

**Share price: A\$ 1.41**

McPherson's, one of Australia's leading suppliers of health and beauty products, calls Kingsgrove, New South Wales, its home. This company and management are currently embroiled in something that is often far from beautiful, a takeover battle. Gallin has submitted a bid to purchase 100% of outstanding shares for \$1.34 per share, a discount of 5.3% to its latest closing price of \$1.41. Management is against this purchase and is fighting it, but we are not so sure there's enough value underneath this company's makeup.

[READ MORE](#)

# BELL FINANCIAL GROUP

The Bell of profit sounds for us

Stocks Down Under rating: ★★★★★

ASX: BFG

Market cap: A\$ 571M

Dividend yield: 5.9% (100% Franked)

52-week range: A\$1.015 / A\$2.02

Share price: A\$ 1.78

Headquartered in Victoria is a company whose name might ring a bell. The Bell Financial Group is a provider of stockbroking and financial advisory services to private, institutional, and corporate clients. The company operates through 14 offices in Australia, New York, London, Hong Kong, and Kuala Lumpur. Bell's stock finished 2020 strong, ending up 160% from its March low of \$0.65 per share. However, it is currently going through a slight pullback, which we believe is a call to action.

## Share price chart



Source: Tradingview

## Some advice on Funds Under Advice

Like any company involved in Bell Financial's industry, the amount of Funds Under Advice (FUA) and its growth are arguably more important than its profit and revenue. The greater the FUA, the more potential the company has for profit in the near future. Additionally, when a company has a significant amount of FUA, it becomes easier to take on additional funds as investors rarely like to be the first money in. Therefore, it becomes a lot easier to convince investors to part with their money when they see Bell's FUA of \$63.9bn. This 2020 amount represented a 9% increase year-over-year. Bell keeps its financial year in line with the calendar year.

However, it is not entirely clear whether the increase in FUA was due to gains in its portfolios or due to capital being added into the business. However, Bell has been achieving consistent year-over-year growth in FUA through both portfolio profits and new client funds judging by its FUA growth from \$38.8bn in 2016 to \$63.9bn in 2020. FUA growth was evenly spaced at an average of 13% annually compared to the ASX All Ords 7.8% during the same period. Additionally, the number of client accounts has increased each year from 130,000 in 2016 to 207,000 by 2020, i.e., at a rate of at least 14,000 new accounts per year.

## **How do you earn your profit?**

While Bell Financial has offices in Hong Kong, London, New York and Kuala Lumpur, Bell's business operates predominantly in Australia. Total revenue was amounted to \$299m in 2020, an 18% increase year-over-year. Revenue can be broken down into three divisions: rendering of services, finance income and investment income.

Rendering of services is rather simple. It includes brokerage and general fees as well as revenue from the administration of client's portfolios. The vast majority of revenue in 2020 came from general and brokerage fees at \$248m, representing a year-over-year increase of 22%. Most of this revenue is generated by Bell's retail client base. The remaining revenue in this division came from portfolio administration at \$19.3m, representing a 2.2% year-over-year increase. In total, this division accounted for 91% of Bell's total revenues in 2020.

Finance income accounted for \$25m in revenue during 2020, representing a year-over-year increase of 3%. This \$25m in annual revenue accounts for 8% of the total, a decline when compared to 2019's 10% of total revenue.

At \$2.5m investment income only accounted for 0.8% of total income in 2020.

## **A solid dividend investment**

For investors looking for dividend income without the risk of significant capital loss, we believe shares in Bell Financial could be a good choice. The company does not provide any earnings guidance, not unusual during these times, but there are no analyst forecasts available either. Despite this, we believe the current conditions in the capital markets are favourable for companies like Bell that have a solid track record.

Since there are no earnings forecast, we have used 12-month trailing data that value the shares at a P/E ratio of 11.8x, which we think is very reasonable. Based on the company's performance during the difficult times of 2020, when so many other financial industry companies faltered, we believe the Bell's is currently undervalued. Additionally, the company has a fully franked, indicative annual dividend yield of 5.9%. For investors looking for a bit of capital gain and a high dividend yield, we believe Bell Financial is certainly worth a serious look. Four stars from us.

# STEAMSHIPS TRADING COMPANY

A slowly sinking ship

Stocks Down Under rating: ★★

ASX: SST

Market cap: A\$ 292M

Dividend yield: 2.5% (0% Franked)

52-week range: A\$9.00 / A\$10.00

Share price: A\$ 9.40

Headquartered in Port Moresby, Papua New Guinea, is a company whose fate seems tied to the economy of its host country. The Steamships Trading Company's name mind brings back memories of a bygone era where steamships were the main mode of water transport. Unfortunately, we believe this is actually an accurate representation as the company has not seen revenue growth since 2014, a bygone era. Compounding the problem is the decline in profits from 2012 through 2020. Unfortunately, we believe last year's increase in profits was a one-off and this temporary gain will not help right the ship.

## Share price chart



Source: Tradingview

## Fates entwined

The Steamships Trading Company is rather unusual. Unlike most of the companies that we write about, Steamships' business is spread across and exposed to the majority of a country's economy. The country in question here is Papua New Guinea. The company's businesses are broken into four division: Coral Sea Hotels, Pacific Palms Property, logistics and commercial. This covers most of Papua New Guinea's primary industries, such as hospitality, mining, agriculture, home and personal care, logistics and shipping.

According to the World Bank, Papua New Guinea's economy is mostly based around the agricultural, forestry, fishing, and mineral and energy extraction sectors. The agricultural, forestry and fishing sectors employ the majority of Papua New Guinea's labour force. However, the mineral and energy extraction sectors account for the largest portion of the country's export earnings and Gross Domestic Product. The country is currently in a state of emergency due to COVID-19 and that is unfortunately just the beginning. Papua New Guinea is also in the midst of a drug-resistant Tuberculosis epidemic. Since both of these diseases damage the lungs, the population is at a much greater risk of long-term health issues. The Bank of Papua New Guinea has stated that the country's Gross Domestic Product contracted 4% during 2020, the second-largest rate of decline since 1995.

## **A tale of Steamships**

Steamships' four divisions generated PGK540.4m (\$198m) in revenue during 2020, a decline of 7.7% year-over-year. Despite this decline, the company's profit increased an eye-watering 68% year-over-year in 2020. Unfortunately, it is nothing to get excited about. The company utilised previously deferred losses to earn a PGK11.2m tax refund for 2020, compared to the PGK18.9m tax expense incurred during 2019. Therefore, when we look at Steamships' EBITDA result for 2020, we see that through cutting selling, general and administrative expenses due to the COVID-19 state of emergency, management was able to eke out an EBITDA growth of 5.8% (PGK159.6m or \$58.5m). Unfortunately, we don't believe this level of cost cutting can be repeated. As soon as the country is back to normal operations, we expect expense to increase again.

Coral Sea Hotels is the largest hotel group in Papua New Guinea. This division operates eight hotels and one serviced apartment block in the country as well as fast food and beverage businesses like Enzo's and Bonjour Café (located in the Deloitte Tower). Despite management attempting to mitigate the loss of Papua New Guinea's vital tourism industry through investment in its food businesses, this division had an extremely tough 2020. And 2021 is expected to be equally brutal.

Pacific Palms Property is one of the largest property developers and managers in Papua New Guinea. This division did not collapse like Coral Sea Hotels due to its diversification across the country. The division's residential portfolio in the country's capital of Port Moresby performed poorly and commercial operations were hit hard by the country's economic situation. This was compounded by Papua New Guinea's ex-patriate population returning to their home countries. All-in-all, due to the division's exposure to industrial and retail sectors as well as residential properties outside of the capital, 2020 was a flat year for Pacific Palms Property, and the same is expected for 2021.

The logistics division had a strong 1Q20, but things quickly went downhill from there. The country's state of emergency has heavily restricted freight, especially during April 2020. As this division's business operations revolve around the transport and handling of freight, harbour towing, fuel transport and loading and unloading of ships, it struggled during 2020. Despite a small uptick in liner volumes during 4Q20, 2021 is still heavily mired in uncertainty.

The last division is the commercial one made up of Colgate-Palmolive (PNG), a joint venture in which Steamships owns 50%. Due to defensive nature of the oral and personal care categories, the division's operations were effectively flat for 2020. There is no current guidance for 2021 for this division.

## **Uncertainty and poor historical performance**

Management believes 2021 will be another challenging year for both Steamships and Papua New Guinea. We completely agree. COVID-19 is far from over in the country and it is likely that the economic effects of this pandemic will be felt for years to come. Steamships does not offer revenue or earnings guidance, but based on the company's 2020 and historic results, we are not optimistic about its future.

Even with a trailing EV/EBITDA of only 6.3x we believe this stock is overvalued based on the bumpy road ahead. We wish them the best of luck, but it's two stars from us.

# MCPHERSON'S

Not beautiful enough

Stocks Down Under rating: ★★

ASX: MCP

Market cap: A\$ 182M

Dividend yield: 7.4% (100% Franked)

52-week range: A\$1.12 / A\$3.40

Share price: A\$ 1.41

McPherson's, one of Australia's leading suppliers of health and beauty products, calls Kingsgrove, New South Wales, its home. This company and management are currently embroiled in something that is often far from beautiful, a takeover battle. Gallin has submitted a bid to purchase 100% of outstanding shares for \$1.34 per share, a discount of 5.3% to its latest closing price of \$1.41. Management is against this purchase and is fighting it, but we are not so sure there's enough value underneath this company's makeup.

## Share price chart



Source: Tradingview

## Yes, your camera is on

As people were stuck at home for most of 2020, skin, hair and body product sales effectively cratered. One of the funnier parts of worldwide COVID-19 lockdowns was the constant stream of video call mess-ups. For example, on 15 April 2020, Broward County, Florida Judge Dennis Bailey published a letter requesting that attorneys show up to work wearing clothes. The judge felt this was necessary after one attorney showed up to a video meeting without a shirt on and another was still under the covers in bed, wearing pyjamas. This rather funny example is just one of many, with a more recent and extreme example being a Canadian MP who accidentally appearing naked during a parliamentary sitting on 16 April 2021. It seems people feel more secure and confident behind a computer screen. With this newfound confidence, why would you spend time and money to put on makeup?

## **A mixed bag of results**

The majority of McPherson's revenue being generated in Australia (87%), the company still suffered from declining sales during 1HY21, with total sales down 4% year-over-year to \$101.7m. There were some bright spots in the form of the essential beauty and household essentials divisions. The essential beauty division grew 13%, generating \$32.9m in revenue as beauty accessories and cotton consumables sales rebounded. As people continue to come back to the office, we are confident that this division will continue to see stable revenue growth over the next 12 months.

Unfortunately, the skin, hair and body division declined 36% year-over-year, eating up the other division's gains. We certainly expect this division to see improvements over the next 12 months as consumers return to work. However, management was struggling to achieve strong revenue growth before COVID-19. Therefore, it is uncertain if our growth prediction will be permanent or just a temporary bump as sales growth more or less normalises after the initial rebound.

Here's the rub for 2HY21 and FY22. Household essentials grew 7% year-over-year to \$32.4m during 1HY21 on the back of increases in food preparation, food preservation and household waste disposal. As consumers in Australia have begun eating out more, we are not confident that this division will retain the sales it gained over the last 12-month period.

## **The takeover**

On 25 March 2021, Gallin released to the market an unconditional purchase offer to McPherson's shareholders of \$1.34 per share. Gallin held 4.95% of McPherson's outstanding shares at the time, but it's far from happy with McPherson's management. Gallin Director Nick Perkins said, "McPherson's is a business that has lost its way and is in urgent need of reinvigoration across its strategy, governance and leadership. The company's performance has disappointed shareholders for some time despite owning a number of quality, attractive brands across key consumer markets."

The issue is, we are finding it hard to disagree with Gallin's assessment. Before COVID-19, McPherson's was having plenty of operational problems. Revenue declined 25% year-over-year during FY18 and was flat during FY19. Management has struggled to right the ship and investors have a lot of uncertainty to look forward to as Australia emerges from COVID-19.

The market's current projections reflect this with EBITDA growth only expected to be 6% during FY22 and 9.8% during FY23. At these expected growth rates, by the end of FY23 EBITDA will be 10.9% below FY20's \$30.3m. We find it hard to see how shareholders would not be better off taking Gallin's offer of \$1.34 per share from a valuation and management quality perspective.

## **Not enough value under the makeup**

McPherson's shareholders have a lot of uncertainty to look forward to over the next couple of years. Firstly, from an operational standpoint, they will need to wait and see if management can right the ship, even after COVID-19. And secondly, the possibility of Gallin's takeover being successful. Management has come out against this deal and the number of shareholders that opt to sell to Gallin is expected to be released shortly after 10 May 2021, when the current offer closes.

If we assume Gallin's offer fails, we believe the shares will be due for a correction as we believe its valuation is too high given current earnings estimates. Using the market consensus EBITDA estimates we mentioned above, FY21, FY22 and FY23 EV/EBITDA ratios are currently at 9x, 8.4x and 7.7x, respectively. When we compare this to the fact that FY23's expected EBITDA will still be 10.9% below FY20s, we find this valuation a bit hard to swallow, especially after an outside entity valued the company 5.3% lower than it is currently trading at. All in all, there's not enough value under McPherson's makeup for us, two stars.



## 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.

You are receiving this email because you subscribed to our Stocks Down Under newsletter.

All rights reserved. No part of this publication may be reproduced or transmitted in any form or by any means, electronic, mechanical, photocopying, recording or otherwise, without prior written permission from Pitt Street Research Ltd Pty. All intellectual property relating to the Content vests with Pitt Street Research unless otherwise noted.

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

