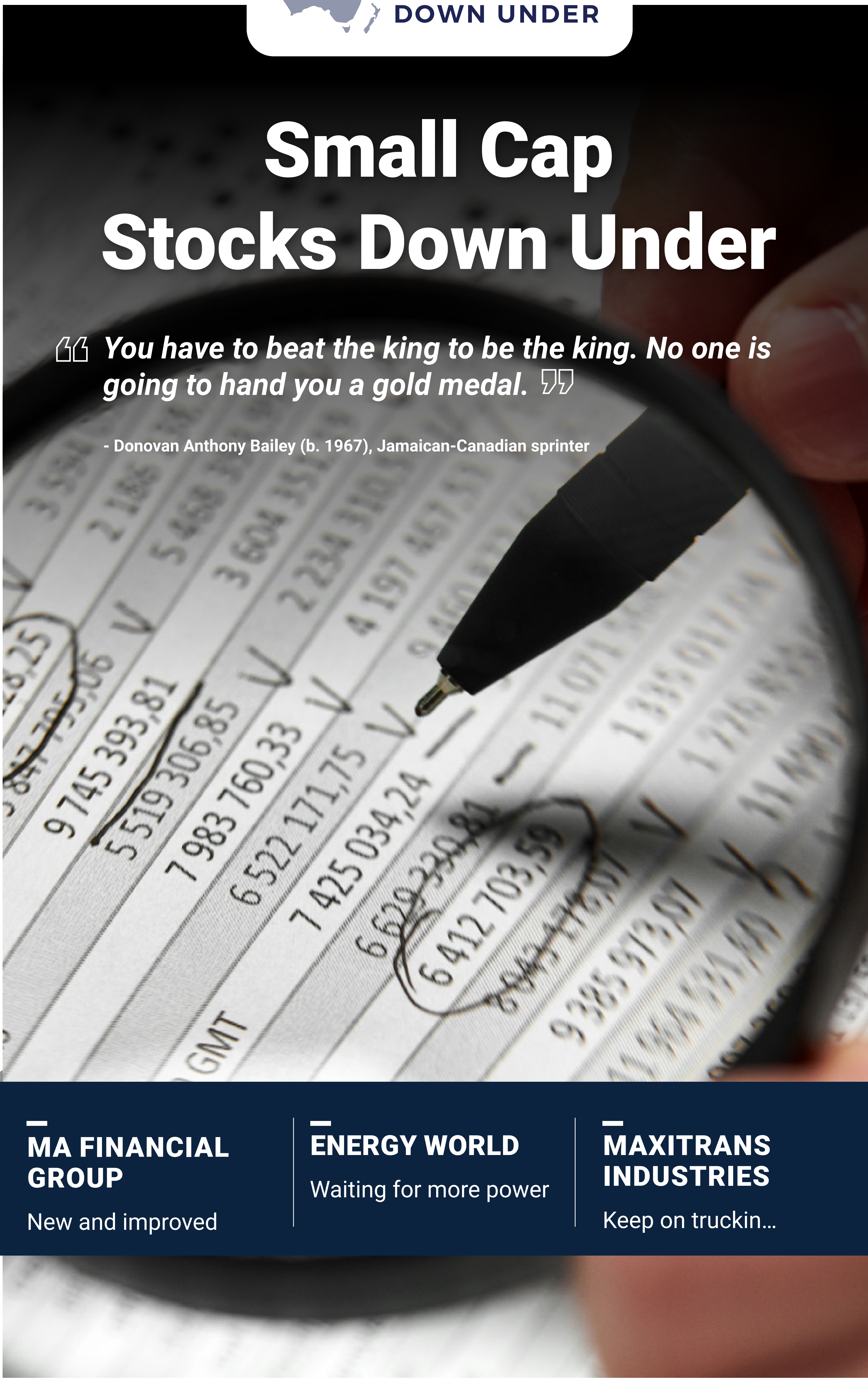
STOCKS DOWN UNDER

10 SEPTEMBER 2021



Small Cap Stocks Down Under

> *You have to beat the king to be the king. No one is going to hand you a gold medal.*

- Donovan Anthony Bailey (b. 1967), Jamaican-Canadian sprinter

MA FINANCIAL GROUP
New and improved

ENERGY WORLD
Waiting for more power

MAXITRANS INDUSTRIES
Keep on truckin...

MA FINANCIAL GROUP

New and improved

Stocks Down Under rating: ★★★

ASX: MAF
Market cap: A$ 1BN
Dividend yield: 1% (100% Franked)

52-week range: A$3.45 / A$8.15
Share price: A$ 7.90

Headquartered in Sydney, MA Financial Group, formerly Moelis Australia (see 26 April 2020 report) changed its name on 4 June 2021 in order to better reflect its growth from a primarily corporate advisory and stockbroker to a full-fledged asset manager. Clearly, this change has been a good thing as underlying revenue and EBITDA growth saw strong growth during the first half of 2021, signalling that MA Financial Group is on the rise.

READ MORE

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Stocks Down Under rating: ★★★

ASX: EWC
Market cap: A$ 193M

52-week range: A$0.046 / A$0.159
Share price: A$ 0.074

Headquartered in Sydney, Energy World has been an independent producer, developer and wholesaler of Liquid Natural Gas since 1988. While many companies in this industry like to say they are vertically integrated, Energy World is vertically integrated in the truest sense of the word, operating across the Philippines, Indonesia and Australia, through gas fields, liquification plants, an LNG Hub terminal and natural gas power plants.

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Share price: A$ 3.82

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Share price chart

Source: Tradingview

A brief history

Moelis Australia was founded in 2009 as a joint venture with NYSE-listed Moelis & Company, focusing mainly on investment banking. But the company quickly grew and during FY16, the year before listing on the ASX, the company generated 75% of its revenue from corporate advisory and stockbroking services. But this report is about MA Financial Group, so why the name change? The company has been highly successful in diversifying away from its original industry and as of FY20, 67% of total revenue was generated by its asset management division, not corporate advisory or stockbroking. Therefore, management decided it was best to change the company's name to better outline its main source of revenue.

In fact, the MA Financial Group manages a significant amount of assets, approximately $6.1bn in total as of FY21. This is split roughly between $2.3bn in real estate, $1.5bn in hospitality assets, $1.3bn in credit and $1bn across listed Australian equities, private equity and venture capital assets. This accounts for 13% growth in total Assets Under Management compared to 2020, supported strongly by $1.1bn in gross inflows over the last 12 months ($506m during the first half of 2021).

The original business remains strong

As we mentioned above, MA Financial's original business was advisory and that business, while significantly less important than it used to be, is still going strong. During the first half of 2021, the advisory business generated $27.9m in revenue, representing 16% growth year-over-year. While the division saw 20.4% growth in EBITDA, it also declined in importance from 22% of MA Financial's 1HY20 $24.5m in total EBITDA to 15% of the $44.5m in EBITDA generated during 1HY21.

For those who know the advisory industry, that would have been a glaring red flag if the business contracted or was flat during this period. Why? Because Australia's merger and acquisition industry saw significant action during the second half of 2020 and continued strongly through the first half of 2021. According to The Market Herald, on a year-to-date basis up until 13 August 2021, 35,128 deals were initiated, a 24% increase year-over-year. This trend is widely expected to continue well through the rest of the year.

Moving to the meat of the matter, the asset management division. During the first half of 2021, this division generated $31.6m in revenue, implying 119% growth year-over-year. This was due mostly to Assets Under Management growth of 13% compared to 31 December 2020 and 21% on a year-over-year basis. This led to a sharp rise in base management fees of 28% as well as transaction fees of 211% year-over-year. Even more importantly, the Assets Under Management saw significant gains, leading to 157% growth in performance fees. Clearly, this division is on the rise and when we factor in that 55.7% of Australian active equity funds beat the S&P/ASX 200 benchmark, an extremely rare occurrence these days, we believe this is likely to drive interest in more active asset managers with a proven track record, like MA Financial Group.

Valuation has become stretched

The market is currently expecting EBITDA growth of 15.1% year-over-year, leading to $69.6m in EBITDA for the full year of 2021, which ends on 31 December. We think this is highly unlikely because the first half of 2021 generated $44.5m in EBITDA, or 63.9% of the market's expected 2021 full-year result. If we are to believe the market, MA Financial will see a 30% decline in EBITDA in the second half of 2021 compared to last year's $36m in EBITDA. Please note that "the market" only consists of one analyst estimate. MA Financial is not widely covered by brokers.

We expect continued growth in Assets Under Management throughout the remainder of FY21. Additionally, M&A activity in Australia is expected to stay strong a while longer. Management believes that the first half of 2021 was indicative of the full year momentum stating "increasing certainty in positive business momentum, inclusive of current lockdown impacts".

However, even though MA Financial is experiencing a strong 2021, when looking at the recent share price development and the current P/E of 23x for FY22, we can only conclude that the good times have been largely priced in by the market. While we don't see a lot of downside to the shares at the moment, we fail to see much upside either. So, it's three stars from us.

ENERGY WORLD

Waiting for more power

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Source: Tradingview

Philippines, Indonesia and Australia, Oh My!

Energy World has a great ring to it, but it is slightly misleading as the company currently only has operations in the Australasian region of the world. However, don't take that to mean Energy World is not diversified. Although the company only operates in the Philippines, Indonesia and Australia, its operations are heavily diversified throughout the oil, gas and Liquid Natural Gas (LNG) industry spectrum.

Energy World has varying degrees of ownership stakes in a series of oil and gas fields in the region. For example, it owns a 33.3% stake in the PEL 96 Southern Cooper Gas project and a 100% stake in the PL65 Gilmore gas field operation. The company is also developing a 56,000 Tonnes Per Annum (TPA) LNG liquefaction facility, although we have not received an update on this since 1HY21's report. Energy World also controls an 8MW Alice Springs power plant. The Australian division's revenue declined 46.5% during FY21 to US$1.2m. However, since this division only accounts for 1% of FY21's total revenue of US$155.3m, the drop was far from catastrophic.

Indonesia represents the vast majority of Energy World's revenue-generating operations. Out of FY21's total revenue, the Indonesian division generated 99% at US$154m across its two sub-divisions: oil & gas and power. The company's Sengkang gas field and South Sulawesi gas operations generated US$44m in revenue for the oil & gas division during FY21. The South Sulawesi gas operation has long-term viability, with the company receiving a 20-year extension to its operational lease in 2018. In July 2021, Energy World's subsidiary, Energy Equity Epic entered into a Joint Operational Agreement (JOA) with PT Energi Maju Abadi, selling a 49% participating interest in the Sengkang PSC Working Area. Unfortunately, the company has not released details yet on how this agreement will affect its operations and assets. Management has announced that these details will be released with the annual report at the end of September 2021.

The power division generated US$110.1m during FY21 through Energy World's ownership and operation of it's 315MW Senkang combined-cycle gas-fired power plant. Management initiated construction on a 2mTPA LNG liquification plant in Indonesia prior to COVID-19, in a bid to expand its footprint in the power space while extracting additional value from its gas operations. Unfortunately, COVID-19 put a stop to construction and trew up some permitting issues. However, these issues have now been resolved and Energy World has received permission to continue construction, although we do not currently have a timetable for when the project will be completed.

Another major piece of information we are waiting for later in September is an update on the company's submitted proposals to the Sengkang Power Plant's Power Purchase Agreement (PPA). Currently, this agreement is set to expire in October 2022. The application is currently under review and management has stated it expects an update for shareholders later in September 2021. However, with no immediate time pressure, we are not overly concerned.

Where is the Philippines?

The Philippino operations are not faring as well as the Indonesian operations as COVID-19 has shut everything down. The company currently operates the Pajbilao LNG Hub Terminal and Power Plant, and while regular maintenance is allowed, operations are not. The Philippines is one of the harder hit countries when it comes to COVID-19, not least of all because it has an active armed conflict with ISIS making government control all the more difficult. And while the Philippines has dealt with armed insurgencies since it gained independence in 1946, the difference today is there is a global pandemic on, which complicates matters quite considerably. While operations will be able to resume the moment the government gives the green light, we believe it's unlikely that this will any time soon due to the Delta variant that's plaguing the Philippines

A neutral showing

Energy World had a relatively neutral showing during FY21 as far as we can tell from the earnings report published on 31 August 2021. Revenue was down 2.5% year-over-year to US$155.3m and Profit After Tax (PAT) jumped 277.3% to $46.5m. However, the vast majority of the jump in PAT was due to changes in the company's slipform (construction) and EWI loan agreements, rather than improving operations. Effectively, we are currently waiting for a more detailed overview of FY21's operations and hopefully some guidance as to when we can expect to see operations in the Philippines resume and an update on the Sengkang Power Plant PPA application.

With the Delta strain roaming freely in the Philippines, there is a lot of uncertainty surrounding Energy World's local operations and with FY21's declining revenue, we don't believe the stock is worth a punt at its trailing 12-month EV/Revenue ratio of 5x and P/E of 16.4x. So, it's three stars from us.

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Share price chart

Source: Tradingview

You are passing another Maxi

If you've ever put on your right blinker to overtake one of Linfox's signature red and yellow trucks, you've almost certainly read their ingenious slogan: "You are passing another Fox". But if you're a trucking enthusiast, your eye might pass over the copy, spotting the array of fixtures and parts that go into these complex machines. There are stainless steel mudguards to protect the wheels, ringfeders (yes, that's a word) for fastening all kinds of hubs, and roofing sheets to protect freight from high temperatures and UV rays. At a more mechanical level, hydraulic couplers and dust plugs, air systems and alternators are all working in tandem to power every truck you idly glimpse out the window.

This is MaxiTrans' bread and butter, and it's made the company some powerful friends. Consider, for example, how Boral decided in mid-2020 to change its fleet of ageing side tippers so that they could dispense road base aggregate from the Wellcamp Quarry, 15km west of Toowoomba. Such an order is not placed lightly and, in the end, the best place to go was the geniuses at Derrimut with their AZMEB product. Until mid-2021, MaxiTrans was also a major player in the trailer business — not just the parts, but the rectangular containers that haul freight across the country. Some of their trailer brands will be recognisable to even the most inattentive of drivers. The Maxi-CUBE has been used to transport frozen foods since 1972. And the eyebrow-raising Lusty EMS provides aluminium trailers to haul grain, sand, fertilisers and gravel.

Selling shovels during a goldrush

In 1HY21, the Trailer Solutions business that brought you Maxi-CUBE and Lusty EMS made up two-thirds of revenue and EBITDA, with MaxiParts providing the remaining third. So, why sell the Trailer Solutions Golden Goose? Because it's not golden any more. Despite freight and logistics making up 8.6% of Australia's GDP, the trailer business is volatile, even cyclical. Any time the agricultural industry is hit by drought, for instance, Trailer Solutions suffers. And the business is hampered by high Capex. MaxiTrans has also had tremendous difficulty finding skilled labour for the appropriate trades that work on trailers. Supply chain issues caused by the pandemic are another thorn in MaxiTrans' side. As evidence for these difficulties, Trailer Solutions — not MaxiParts — relied on JobKeeper in both FY20 and FY21, receiving $4.9 million and $4.6 million, respectively.

One suspects that intense competition from the likes of Vawdrey and CIMC Trailers ultimately made MaxiTrans decide to exit. This facet would have been nerve-wracking for investors if it weren't for MaxiTrans' shrewd plan. In the short term, the company intends to execute a series of mergers and acquisitions to consolidate the commercial vehicle aftermarket parts industry. It's the same logic as selling shovels during a gold rush. While Vawdrey and CIMC Trailers duke it out, MaxiTrans will quietly pursue market dominance in the parts sector.

Other factors are promising, too. MaxiTrans has a new e-commerce platform to drive online sales as well as a second Sydney outlet opening as a click and collect option. Most impressive of all is the company's plan for distribution network expansion and development. As a pure play trailer parts distributor, MaxiTrans wants to cover more nodes in the transport network. Any time a mudguard breaks on your truck, a MaxiParts location will be nearby to help you replace it.

Company management are buying in

On 24 August, when non-executive director Gregory Sedgwick bought 28,170 shares at $0.71/share, we took notice. A day later, CEO Dean Jenkins bought 140,000 shares. The Trailer Solutions sale had been announced on 22 July, and in an investor presentation on 26 July, management stressed that the sale would net shareholders a healthy "special dividend" of 0.125 per share, fully franked.

Sure, the presentation was an admission that MaxiTrans had failed to invigorate the trailer business, but management knew that their new focus on consolidation, the sound business plan and the terrific dividend would sway investors. And boy it did. On 27 August, at a shareholder meeting, nearly 99% of the votes were in favour of the sale.

Nice growth expected

Between FY20 and FY21 MaxiTrans' EBITDA nearly doubled. On consensus estimates, EBITDA is expected to halve for FY22, which reflects diminished earnings from the sale of Trailer Solutions. But then EBITDA is expected to climb a solid 9.5% in FY23. On consensus estimates, the EV/EBITDA multiples for FY22 and FY23 are 9.3x and 8.4x, respectively. However, this is before any corporate activity which MaxiTrans has flagged it is actively looking for.

With a more tightly focused business strategy, M&A activity on the horizon and $5.2 million in hand, we believe it's exciting times ahead for MaxiTrans. Exiting Trailor Solutions is logically sound, not a sign the company is lost somewhere along the highway. The next time we write about MaxiTrans they will be MaxiParts, and hopefully, we'll have all made some nice gains. Four stars.

Pitt Street Research Pty Ltd

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