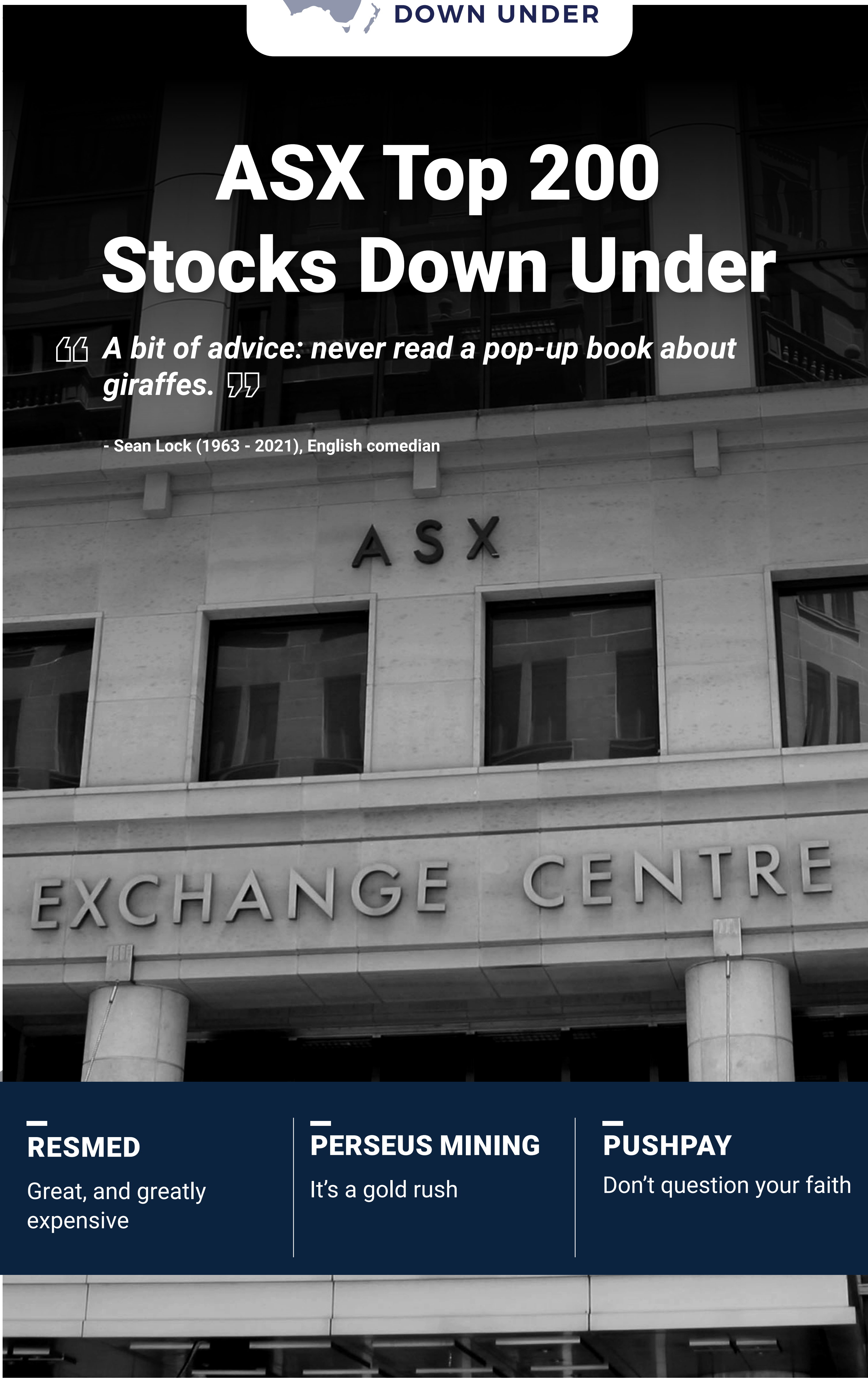
STOCKS DOWN UNDER

29 NOVEMBER 2021



ASX Top 200 Stocks Down Under

> *A bit of advice: never read a pop-up book about giraffes.*

- Sean Lock (1963 - 2021), English comedian

RESMED

Great, and greatly expensive

PERSEUS MINING

It's a gold rush

PUSHPAY

Don't question your faith

RESMED

Great, and greatly expensive

Stocks Down Under rating: ★★

ASX: RMD
Market cap: A$66.1BN
Dividend yield: 0.4% (0% Franked)

52-week range: A$23.48 / A$40.79
Share price: A$35.30

ResMed is a US company now based out of California but it was born and raised in Sydney in the 1980s. A legend of modern healthcare, ResMed mixes medical devices and cloud computing to provide mostly in-home care to people suffering from sleep apnea, Chronic Obstructive Pulmonary Disease (COPD), and other respiratory disorders. The last time we covered the company in May 2020, our main issue was not the business model. Instead, our issue was that the stock was too expensive. This issue remains and it has only gotten worse.

READ MORE

PERSEUS MINING

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Stocks Down Under rating: ★★★★

ASX: PRU
Market cap: A$2.1BN

52-week range: A$1.06 / A$1.85
Share price: A$1.69

When we last covered the Perth-based gold miner Perseus Mining on 7 May 2020, we cited the increasing price of gold and the company's potential to mine a larger quantity as the reason to invest in the company. Over a year later, not a lot has changed and the company is still going strong. With its three mines operating at full capacity and the gold price expected to hold in the coming years, Perseus may be the modern equivalent of a gold rush.

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Share price chart

Source: Tradingview

COVID is slowly going to bed, but sleep apnea is not

Let us give you a primer on ResMed. This company develops machines that allow patients diagnosed with sleep apnea to receive the care and monitoring they need. Considering that over 80% of sleep apnea is undiagnosed, the company has plenty of avenues to pursue growth, both in the number of devices sold and in the scope of its SaaS division.

COVID was a blessing for ResMed because the demand for ventilators and masks shot up and the company produced as much as it could, with a corresponding improvement in margins. Revenue increased from US$2.61bn in FY19 to US$2.96bn in FY20, and gross margins went from 57.3% to 58.1%. In turn, net income (what they call 'Net Profit After Tax' here in Australia) went from US$405m to US$622m, a 53% increase.

For FY21 the results were a little more subdued. With vaccinations on the rise and the need for ventilators and masks dwindling, the company's primary focus once again switched to its core business. While revenues still increased by 8%, to almost US$3.2bn, net income fell to US$475m. Say what? Well, gross margins decreased, from 58.1% to 57.5%, but what really happened was the tax rate returned to more like normal. Hence the big decline in net income. Leaving that issue aside, FY21 was a return to business as usual for ResMed, where 'business as usual' means robust top-line growth as more and more people find out they have sleep apnea and end up in ResMed's growing patient population.

When competitors falter, ResMed rises

We stated that around 80% of people with sleep apnea are undiagnosed. However, awareness of the issue is increasing. The case we made in May 2020 is still accurate: The company is helping both healthcare companies and patients save money, and the need for in-home care continues to rise.

ResMed's Continuous Positive Airway Pressure (CPAP) machines continue to be the most lucrative business. In 4Q21 (ended June), the company reported that it could not meet the demand for its devices. As the need for the machines rises, so does demand for the company's cloud-based services that allow monitoring of patients. However, the global chip shortage and freight constraints has recently lead to rising costs, and while management is trying to increase production capacity, shortages for its components could last well into FY23.

The increase in demand comes hot on the heels of Philips Respironics, one of the company's main competitors, announcing a recall of its CPAP machines due to chemicals in the foam of their machines possibly breaking down and causing long term health issues.

Due to all this, the demand for ResMed's products is expected to stay high in the next couple of years, and it shows in the analyst estimates.

Valuation very demanding

ResMed experienced rising revenues through most of FY21. While management stated in the FY21 results announcement that they expected their company to grow steadily through FY22, the market is currently expecting a lot of growth. Like, revenue growth of 20% and EBITDA growth of 21% on consensus (ResMed itself doesn't report 'EBITDA' in its regular quarterly reports, so the analysts need to calculate it themselves). ResMed's Selling, General & Administrative expenses decreased in FY21 and are expected to continue to decline. 1Q22 was a strong start for FY22, with revenue rising 19% on a constant currency basis to US$904m. But one quarterly slipup, and this stock might be in trouble.

The company's FY22 EV/EBITDA multiple on consensus is a very high 29.1x. We described a forward EV/EBITDA of 23.5x as too high when we last covered the company and we mentioned that only an EBITDA growth of 25% per year would be able to justify such a valuation. Right now, the projected EBITDA growth rate is 21% for FY22, but the multiple is much higher. Consequently, we still rate the company as two stars. ResMed has an impeccable outlook, but it's just too expensive for us. ResMed would be a great investment opportunity if a share price correction were to occur, just like last time.

PERSEUS MINING

It's a gold rush

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When we last covered the Perth-based gold miner Perseus Mining on 7 May 2020, we cited the increasing price of gold and the company's potential to mine a larger quantity as the reason to invest in the company. Over a year later, not a lot has changed and the company is still going strong. With its three mines operating at full capacity and the gold price expected to hold in the coming years, Perseus may be the modern equivalent of a gold rush.

Share price chart

Source: Tradingview

On the wings of Perseus

In Greek mythology, Perseus was a hero with winged sandals that allowed him to move quietly and quickly. Perseus Mining is quite similar in that regard, as it has been on a quiet, but upward trajectory since 2018. Unlike Icarus, however, its wings do not have a chance of melting under the scrutiny of the sun.

Back in May 2020, the Yaouré mine was nearing its first pour. In December that year, the mine was open for business (5 weeks ahead of schedule), with its first commercial production declared at the end of 3Q21. The company has slightly lowered its estimated production capacity from 215,000 ounces a year to over 200,000, but that still makes Yaouré almost as large as the Edikan in Ghana (the company's main cash cow). Moreover, exploration on the fringes of the mine is still underway. It could extend its life beyond eight and a half years as is currently projected.

The company's operations were largely uninterrupted by COVID-19. It produced 257,639 ounces of gold in FY20 at a weighted average All-in Sustaining Cost (AISC) of $972 per ounce, 1% higher than FY19. However, the surge in the gold price led to the company's EBITDA increasing 67% during the same time. Net profit rose from $7.6m to $94.4m as a result.

For FY21, the company continued on its upward trajectory by producing 321,199 ounces at an AISC of $1,016. The increase in the gold price more than made up for the rise in cost, as the company's EBITDA surged by 11% and the profit climbed to $139.4m.

The search for more gold continues

The company is currently in an extremely healthy position. It is on track to produce over 500,000 ounces in FY22 at a margin of at least $400 per ounce. This would mean that the company's net profit would exceed $200m for the year. Still, the company is not resting on its laurels.

In June 2021, Perseus sold its 39% stake in the Napié gold project to Mako Gold, the Brisbane-based gold company, for 13.8m shares in Mako. Perseus now owns 5.1% of Mako, giving Perseus exposure to Mako's multiple projects.

The Napié project is located in the north-central part of Côte d'Ivoire. Drilling is currently ongoing, with the mine showing signs of high-grade, but shallow gold mineralisation. Mako also has permits to explore Korhogo Nord and Ouangolodougou, both located in Côte d'Ivoire. While all of Mako's projects are years away from commercialisation and their potential is unknown, Perseus' small, but significant stake provides an option for the company to continue generating profit after its current mines run dry.

In April 2021, the company reported numerous exciting possibilities for expansion close to their current projects, with gold deposits being discovered at Govisou (3km from Yaouré) and Bagoé (70km from Sissingué). Govisou is an especially promising site for the company as a lot of the equipment from Yaouré could be shifted to the new site once its life ends.Lastly, Perseus announced its plans to acquire Exore Resources in June 2020 in an all-share transaction. Exore shareholders were to receive 1 Perseus share for every 12.79 Exore shares. Exore is a Perth-based mining company with a primary focus on mining gold and lithium. The company is currently exploring numerous potential mining sites (including Bagoé) and is another way for Perseus to plan for the future (as all of its current mines are expected to deplete in eight years or less).

Certainly great for a few years, probably good after that

We expect Perseus to enjoy $200m+ profits for the next few years consistently. The company should be able to reduce its AISC (as its three mines are all fully operational and efficiencies can be found) and continue to produce at a profit of $400+ per ounce. Maybe Perseus can even increase its margins if gold consistently stays above the $1800 per ounce mark.

Beyond that, the company has numerous exploration projects lined up through Exore, Mako and its permits. Of course, we can't be sure if any of those projects would be as profitable as the company's current mines, but early data is quite positive.

In August 2021, the company announced its plans to offer semi-annual dividend payments, with a maiden distribution of $0.015 per share. The company plans to offer an annual yield of at least 1%, with special dividends and share buybacks also to be considered if the situation permits.

According to consensus estimates, EBITDA is set to grow by almost 58% in FY22 and by 11% in FY23. On those growth rates, we believe Perseus is very attractively valued at EV/EBITDA multiples of 4.3x for FY22 and 3.9x for FY23, especially since we are expecting gold to move higher in the next little while on the back of global inflationary pressures. Keeping all this in mind, we believe Perseus is a four-star investment, as it should provide stable income at a very reasonable valuation. Not to mention that it has the potential for growth through its current exploratory projects.

PUSHPAY

Don't question your faith

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Share price chart

Source: Tradingview

Take me to church

PushPay is a donor platform that allows non-profit organisations, such as churches, to accept donations from their members in a seamless and hassle-free manner. Although the company was formed in New Zealand, its primary userbase is in the US, with a substantially larger church-going population than New Zealand. While the US is not the most religious country by any measure, it does have people who are more serious about their faith (and are willing to spend money to prove it) than almost anywhere else.

Considering the company's financial performance, it is currently on its way to heaven. In FY21, revenues surged to NZ$249m from NZ$214m the year prior. The company has been regularly outperforming management's guidance for total payments volume processed (per month) and has been signing new churches and faith-focused organisations to its platform every month.

After announcing a four-for-one stock split in November 2020 (a testament to the massive increase in share price in recent years), PushPay successfully completed a bookbuild of NZ$97.9m in December 2020, attracting interest from numerous high-profile institutions in the process.

The most significant decision taken by the company in 2021 has been the acquisition of Resi Media in August 2021 for $150m, with $110m to be paid in cash and the rest in PushPay stock. Resi Media is a streaming company that services over 70% of the 100 largest churches in the US (as per Outreach magazine). We think that Resi is a perfect fit for PushPay, as their complementary product offerings should allow PushPay to cross-sell services and access a broader customer base in the US.

Beyond the US

COVID-19 was a blessing for the company because it helped push religious communities, usually rigid in their way of life, to the internet. With religious centres open once again in the vast majority of the US, the company can continue to leverage its market penetration (and Resi's customer base in remote areas) to continue to increase its customer base.

In the long-term, declining church attendance is something to worry about for PushPay. In the last decade, the percentage of people who never attend religious services in the US increased from 11% to 17%. However, we believe the company can counteract this by moving into other countries with a sizeable religious presence, such as Russia. Not to mention that there are numerous opportunities in religions other than Christianity if the company was to expand its horizons. That said, PushPay still has ample room to grow in the US Christian community.

On top of that, the company can turn itself into a media provider or a social network of sorts for religious communities. For instance, PushPay could consolidate the faith-focused network services industry through targeted acquisitions, using a single sales and marketing engine to push multiple services and products.

A company to worship

We believe PushPay is a company that ticks all the right boxes. Its operating margin, already at a very high 65% in FY20, increased to 68% in FY21. Its EBITDAFI (F for foreign exchange losses and I for impairments) increased by more than 133% during the same year and net profit experienced a rise of 95%.

Its total customers rose from 10,896 to 14,095 (1HY22), an increase of 29%. However, we mentioned previously that subscription fees form only a tiny percentage of the company's revenue (28% for FY20). PushPay relies on transaction fees for most of its revenues instead and during 1HY22, total processing volume increased 9% to US$3.5bn.

Now, through the acquisition of Resi Media, the company has another critical revenue stream that is expected to add at least $13m to its annual recurring revenue through its 3,300+ customers.

We mentioned previously that the US has over 300,000 churches with at least 500 members and PushPay has only scratched the surface of America's faith market. That still holds today and the company can use a combination of sales and acquisitions to increase its customer base in a space where the competition is not as fierce as the wider payments processing industry.

However, it is important to note that 1HY22's results were rather poor due to increases in operating costs (mainly direct third-party costs). This led EBITDAFI to increase only 1%, while revenue increased 9%. This is why the stock took it on the chin on 10 November.

Consensus estimates show the company's revenue reaching NZ$330m in FY23, which starts in April. EBITDA is expected to grow by 16.3% to $94m, while the stock is currently trading at 16.9x for FY23. So, for the next little while, we believe PushPay is fairly valued. So, it's three stars for us until the company can show substantial EBITDA growth again at a more attractive valuation.

Pitt Street Research Pty Ltd

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