under the radar report
SMALL CAPS

ISSUE 625
07 NOVEMBER 2024

# FORGET THE NOISE, INVEST IN FUNDAMENTALS

**A stock price is governed by two things: sentiment and fundamentals. However uncertain the world seems to be, an investor's aim is to look at this and realise what is factored into a valuation and how a company's future stream of income measures up. We cover real businesses, rather than those based on concepts. These businesses have real assets and generate real revenues and real earnings.**

We are not looking at the company's prices on 20 times sales, where you really don't know what you're getting. These stocks are more common in the US, where the bull market has been stronger for longer and there has been more experience of totally transformative stories, like Amazon, like Tesla, like Apple, like Nvidia…

But Australia has particular advantages, especially when it comes to commodities and extraction. We have exposure to great stories like **Fortescue Metals (FMG)**, **Pilbara Minerals (PLS)**, **Paladin Energy (PDN)**, and Poseidon Nickel for those old enough to remember. **BHP** was once a small cap.

Moreover, resources provide exposure for the future and rare earths is an essential component for magnets used in batteries for EVs and robots.

The most important point in any market or indeed in any investment, is the price you pay.

In our analysis, we highlight that the price of the flagship rare earth neodymium praseodymium (NdPr) is showing positive signs, which is being reflected in the rebounding **Lynas Rare Earths (LYC)** shares, which have returned over 20% in the past 12 months as they approach $8. Don't worry! Our valuation is higher than current levels and is based on significant increases the company flagged in its resource and reserve mineral estimates.

Investing in resources is essential, but to do this you have to be confident that you're not paying too much and be prepared to take profits when sentiment is positive.

**Richard Hemming**
**Head of Investments**

## the issue

### CRITICAL MINERALS ANALYSIS

Rare Earths
Demand for rare earths will only increase as countries and economic blocs such as the European Union, move to increase self-sufficiency for critical minerals.

| | |
|---|---|
| LYNAS RARE EARTHS (LYC) | SPEC BUY |
| ARAFURA RARE EARTHS (ARU) | HOLD |

### RESEARCH TIP UPDATES

AVA has improved its quality, while MDR is a work in progress and RFG is turning its business around.

| | |
|---|---|
| AVA RISK GROUP (AVA) | SPEC BUY |
| BEAMTREE HOLDINGS (BMT) | HOLD |
| MEDADVISOR (MDR) | SPEC BUY |
| RETAIL FOOD GROUP (RFG) | SPEC BUY |

### BEST STOCKS TO BUY NOW

These stocks are the quality companies that we believe offer great return potential for the risks faced. Check them out online.

**We cover real businesses, rather than those based on concepts. These businesses have real assets, and generate real revenues and real earnings.**

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# CRITICAL MINERALS ANALYSIS

**China is the key to the rare earths market, dominating mining and processing. Rare earths are particularly important for magnets used to power EVs and robots. Demand for rare earths will only increase as countries and economic blocs such as the European Union, move to increase self-sufficiency for critical minerals.**

## A RARE EARTHS REBOUND

**5-year chart of Neodymium, the rare earth used for permanent magnets for EVs and robots, in Chinese Yuan**


Rare earths have been hit by oversupply by the Chinese. The price has moved to below the cost of production, and is increasing to more sustainable levels on increasing demand for EVs.

SOURCE: Trading Economics

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# CRITICAL MINERALS ANALYSIS Cont.

## CRITICAL MINERALS

Rare earth magnets are essential components for two of the fastest growing industries, electric vehicles and wind power. A rare earth magnet in an electric motor makes a lighter, cheaper, longer-range vehicle. It provides strength and heat resistance in a wind turbine.

## PRICES FORECAST TO CONTINUE TO RISE

The bellwether rare earth is neodymium praseodymium (NdPr) used in EVs and robots. While prices are considerably lower than during mid-2022, the fundamentals are moving in favour of the commodity going up. The NdPr oxide China domestic price was US$94/kg in the September quarter of 2022 versus US$139 in the March quarter of 2022.

Consultants expect China supply to be reduced, with current growth of 2.5% a year up until 2028 and then slowing to growth of 0.5% a year thereafter, which is a combination of reducing mine life and deteriorating economics. In contrast, demand is forecast to double over the next decade, as the need for batteries for EVs grows.

Moreover, this trend is underway. After weakness for most of calendar 2024, rare earth prices recovered slightly at the end of the September quarter. Reasons include a reduction in China's rare earth imports and the economic challenges faced by many rare earths producers at low price levels.

## CONCLUSION: LYNAS IS IN THE BOX SEAT

**Lynas Rare Earths (LYC)** is one of the world's few rare earths producers outside China. According to the group, NdPr oxide price increased to US$48/kg in the company in the past few months from US$46.5 at the start of the year. NdPr are classified as light rare earths. Lynas also produces other rare earths, including dysprosium (Dy) and terbium (Tb) which are classified as heavy rare earths and are in shorter supply. We also cover Arafura (ARU) in this report, which is not in production yet.

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# LYNAS RARE EARTHS

**SECTOR** METALS_MINING **INDUSTRY** RARE EARTHS

## Critical Minerals Analysis

**What's New?**
The ramp-up of the new processing plant in Kalgoorlie, Mt Weld, commenced in June and continues with Rare Earth carbonate shipped to Malaysia and processed at Lynas's plant. Exciting times! What is more exciting is that the stock is rebounding to above our initial buy price, having returned 20% over the past 12 months. Lynas also announced significant increases in its mineral resources and reserves, further boosting our confidence.

**Bull Points**
· Rare earth magnets essential in EVs and wind turbines
· Non-China rare earths production and IP

Bear Points
· EV production has slowed
· Rare earths prices is still low

**Analysis:** Lynas is a vertically integrated producer of rare earths, which has experienced difficulties in the production process over recent years. The company has managed to resolve problems and is now benefiting from rising demand for rare earths, only now being reflected in rising prices (see associated note). Despite recent strong returns, our confidence is picking up in the value for investors as rare earths live up to their potential.

Production levels in 1Q25 were managed in line with market demand. Total 1Q25 rare earth oxide production was 2,722 tonnes with total NdPr production of 1,677 tonnes. Sales receipts in 1Q25 were $127.5m, up 8.5% relative to 4Q24.

Lynas continued to progress with its growth project target to increase production capacity to 10.6 k tonnes NdPr capacity in FY25. This included work on optimising and improving recoveries across all sites, from mine to the finished product.

In Kalgoorlie, work was focused on quality and cost performance. This will support Lynas Malaysia's downstream processing performance as it ramps up in 2Q25.

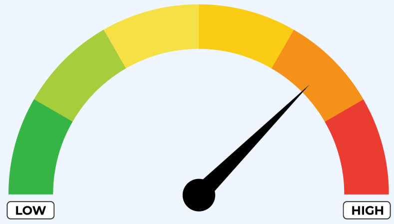
In the US, project activities continued for its US-located Rare Earths Processing Facility.

**Portfolio Risk Rating:** Rare earths remains a boom bust commodity, which is mitigated by Lynas's cash reserves and profitability, despite historic low rare earth prices. Projects being derisked as Mt Weld, Kalgoorlie and Malaysia sites are commissioned and integrated.

RADAR RATING: Production growth as sites expanded and new products were introduced. Strong leverage to rare earths price recovery. Special position as a non-China supplier.

RADAR RATING: **SPEC BUY**

## RISK RATING



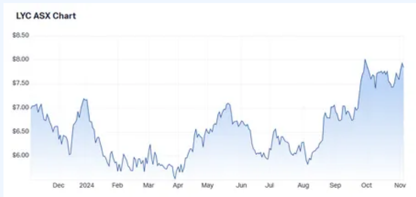

ASX CODE **LYC**

CURRENT PRICE **$7.945**

MARKET CAP $7.43BN

DIVIDEND YIELD 0%*

NET CASH ($M) 352M

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# ARAFURA RARE EARTHS

**SECTOR** METALS_MINING **INDUSTRY** RARE EARTHS

## Critical Minerals Analysis

**What's New?**
Arafura is preparing for a final investment decision and commencement of Nolans rare earths project construction in the Northern Territory, originally targeted for late last year. Having completed the debt funding component of over US$1.0bn (A$1.5bn) in July, the company is now negotiating to secure US$800m+ (A$1.2bn) in equity funding, which is multiples of the current market capitalisation.

**Bull Points**
· Rare earths price recovering
· Government policy backing

**Bear Points**
· Lead time of 3 years
· FID has been put back by 6 months

**Analysis:** Funding remains an issue for the project, with the equity placement completing arrangements before the final investment decision can be made. The project has been delayed but remains globally significant and in a politically stable area. The project has the approvals but still remains at least three years away before production.

Initial negotiations for the final equity funding component are with customers and institutional investors. Arafura is prioritising certainty over speed and the total funding is at US$1,887m.

The Nolans project is 'shovel ready', with construction activities intended to commence once FID has been reached. Project activities are currently limited to those necessary to support finance, critical path activities, compliance and progressing improvement ideas that reduce capital costs, schedule and risk.

The indicative lead time from FID to start-up remains at 37 months. This implies a potential start to production ramp-up in 1H CY28. After start-up, production is planned to ramp up to 4,440 tonnes of NdPr oxide and 474 tonnes of SEG/HRE oxide a year with a long mine life of 38+ years. There is potential for a Phase 2 expansion and a third-party processing hub.

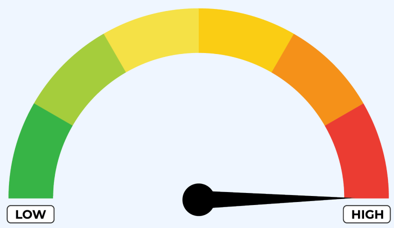
Project capital costs have not changed since the Project Economics update in July 2024. As FID approaches, it is hoped further cost improvements will counteract any cost increases.

**Portfolio Risk Rating:** Almost as risky as it gets, with un unfunded project for a boom bust commodity. Although risk is reduced with debt funding, projected first quartile costs, binding offtake agreements with tier 1 customers, supportive government legislation.

RADAR RATING: High risk but well positioned as a future supplier of non-China rare earths to expanding under supplied markets related to the energy transition and other high tech markets.

RADAR RATING: **HOLD**

RISK RATING



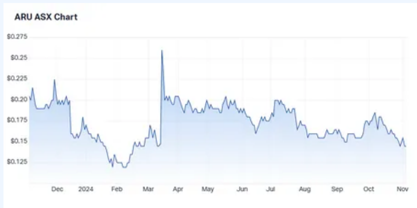

ASX CODE **ARU**

CURRENT PRICE **$0.142**

MARKET CAP $363.5M

DIVIDEND YIELD 0%*

NET CASH ($M) 55M

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# AVA RISK GROUP

**SECTOR** INFORMATION TECH **INDUSTRY** SECURITY DATA SERVICES

## Research Tip Update

**What's New?**
Having bolstered its balance sheet with a $4.3m capital raising @ 13 cents a share, the first quarter result showed improvement in AVA's fundamentals. Sales were a touch under $9m and the company is guiding for $17m in the first half (midpoint) and to generate positive operating earnings (EBITDA). AVA also said, "The second half is expected to be substantially stronger than the first half."

**Bull Points**
· Winning contracts
· Technology for the times

**Bear Points**
· Limited transparency
· Subscale for the opportunity

**Analysis:** This company remains subscale, i.e. revenues are not at the level to generate consistent profit growth. But the quality of the business is slowly improving, an indication of which being the $8.5m sales backlog, which is on top of annualised sales of about $33m, which are forecast to reach $50m in the current fiscal year (FY25), driven partly by its high profile contract with Telstra. If this happens, the share price should appreciate due to 60% gross profit margins delivering profit growth through operating leverage.

There is certainly demand for the group's security services and products from mining, transport and countries, such as Poland, which have common boundaries.

A problem has been long sales lead times. We are encouraged by the new CEO's enthusiasm, validated by the growing sales backlog.

AVA has three divisions, but the key is "Detect", which generates over half of the sales from fibre optic sensing technologies, the main one being Aura Ai-X.

"Access" (15% of sales) sells a locking technology and has a deal with the global giant dormakaba, signed late CY21, unlocking US and Europe.

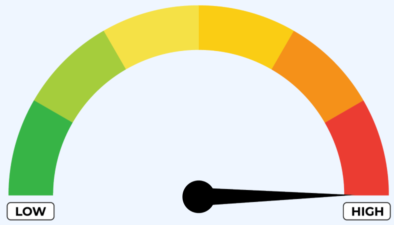
"Illuminate" (25% of sales) develops automatic number plate recognition cameras and perimeter detectors. This business has performed below expectations, resulting in a $1.5m write-down of goodwill.

**Portfolio Risk Rating:** The sales line is thin but is forecast to grow rapidly in the second half or 6 months to 30 June. The capital raising this year and sales backlog deliver confidence, albeit at high risk.

RADAR RATING: This remains a work in progress, but momentum is positive and the shares are cheap.

RADAR RATING: **SPEC BUY**

**RISK RATING**



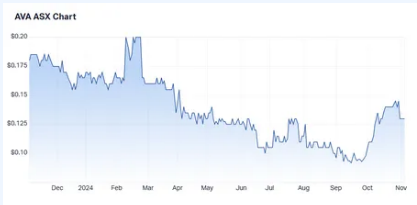

ASX CODE **AVA**

CURRENT PRICE **$0.13**

MARKET CAP $38M

DIVIDEND YIELD 0%*

NET CASH ($M) 5.1M

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# BEAMTREE HOLDINGS

**SECTOR** HEALTHCARE **INDUSTRY** EHEALTH MED TECH

## Research Tip Update

**What's New?**
The shares got a boost this week but remain at half their 60-cent level in mid-2021. The catalyst was first quarter to 30 Sep (1q25) sales showing 16% revenue growth and improving profitability. The e-health provider also reaffirmed FY25 revenue guidance of +20% and for annual recurring revenue of $60m by 2026. Last year's sales totalled just over $27m.

**Bull Points**
· Health data opportunity
· Recurring revenues

**Bear Points**
· Limited cash flow
· Continuous investment needs

**Analysis:** The share price does not factor in the $60m annual recurring revenues FY26. If BMT does get closer, we expect a valuation uplift. As it happened, ARR rose by 21% versus the same quarter last year. Ambitions aside, the fundamentals are still lagging with just over $4m in cash and operating losses, albeit only slightly. The company needs to achieve sustained profitability, which will occur if the top line grows to over $50m. The CEO leaving has damaged the company's credibility.

A key risk in this stock is that, unlike enterprise resource planning software platforms such as SAP and Amazon's AWS, BMT's Clinical Decision Software Support provider RippleDown, as well as its other products PICQ and RISQ are not essential for hospitals. Rather, they are great at improving existing systems.

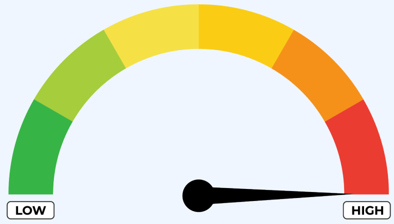
Nevertheless, the opportunity remains because BMT has its foot in the proverbial hospital door. This is why we believe the company can go close to achieving its $50m revenue guidance for FY25/26.

**Portfolio Risk Rating:** Even with interest rates at current levels, a successful software business can be valued as much as 10 times ARR, but risks remain. The financial cushion is thin but should support long-term growth.

RADAR RATING: Cash flow is positive but profitability is limited in the short-term while capabilities are expanded. CEO is leaving at a critical time.

RADAR RATING: **HOLD**

## RISK RATING



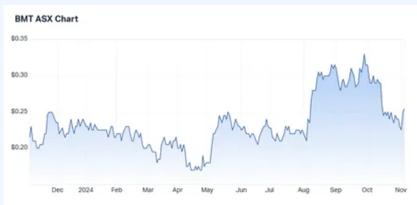

ASX CODE **BMT**

CURRENT PRICE **$0.24**

MARKET CAP $75M

DIVIDEND YIELD 0%*

NET CASH ($M) 4.5M

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# MEDADVISOR

**SECTOR** HEALTHCARE **INDUSTRY** EHEALTH MED TECH

## Research Tip Update

**What's New?**
MedAdvisor is close to where we first recommended the stock earlier this year after the shares declined a third on news that first-quarter revenue grew only 3.5% to $26.3m. This equates to revenues of just over $100m a year, well below the 15% quarter-on-quarter growth implied by the five-year target of $250m in revenue, announced in August. Operating earnings (EBITDA) are expected to grow at 20% a year, but gross profit was actually down 2.5% to just over $15m. The cash on hand is healthy at over $13m and the $15m debt facility has been re-finance at an interest rate of 9.35%, which matures December 2027.

**Bull Points**
· Growth in the US & Australia
· Strong cash flow

**Bear Points**
· Increasing capital expenditure
· Management of rapid US growth

**Analysis:** MedAdvisor remains at the early stages of its growth and as such needs to improve its revenue line to reduce earnings volatility. We knew this, but it doesn't make it easy watching aggressive selling. We regard the company as being on track and that this sell-off provides a buying opportunity.

We said in our previous note that the group's 5-year "aspirational" target was bold to more than double revenues to $250m and to grow earnings at 20-25% a year on a compound basis. But US-based CEO Rick Ratcliff did admit that an acquisition would be required to meet this target. Be that as it may, the first quarter is generally the weakest with marketing relying more on awareness than adherence to prescriptions. The first quarter exposed the twin weaknesses of falling vaccine revenues and gross profit margins bouncing around owing to the transfer from paper-based marketing (mail) to digital (telephone).

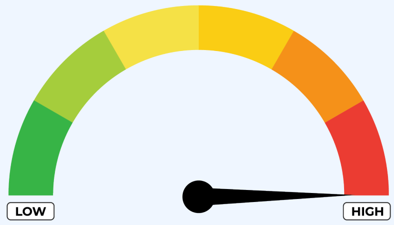
A big factor in the company's favour is technology: THRiV, a patient engagement platform in the US has seen rising demand; to replicate this across the entire business MDR has the "Transformation 360" project.

**Portfolio Risk Rating:** This is very high risk but we have confidence debt continues to be reduced and growth will resume.

RADAR RATING: Early stage with ambitious targets. This is high risk but high reward and based on big pharma's demand for the marketing pipeline MDR provides.

RADAR RATING: **SPEC BUY**

**RISK RATING**



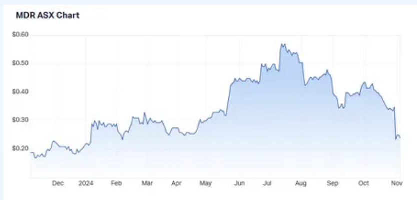

ASX CODE **MDR**

CURRENT PRICE **$0.245**

MARKET CAP $135M

DIVIDEND YIELD 0%*

NET CASH ($M) 3.2M

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# RETAIL FOOD GROUP

**SECTOR** CONSUMER DISCRETIONARY **INDUSTRY** RETAIL

## Research Tip Updates

**What's New?**
After demonstrating a turnaround in operating performance and buying into a new category through the acquisition of Beefy's Pies, RFG is purchasing South Australian coffee franchise chain, CIBO Espresso, for $4m. A 1-for-40 share consolidation is planned for December, after the AGM also approves a change of name from RFG to **Savora Brands**.

**Bull Points**
· Low capital requirements of franchisor business
· Low risk multiple expansion options

**Bear Points**
· Retail slowdown
· Unproved growth initiatives

**Analysis:** With less than $10 average ticket prices, the Cafes business offers affordable treats even in a weak consumer spending environment. The stock is exposed to operating businesses, as well as a more substantial franchise business delivering lower risk returns in the form of fees and revenue shares. FY25 growth is expected to be led by the franchise network and multisite operators.

CIBO has 22 outlets in SA, including 4 company-owned stores, and RFG's intention is to rebrand to Gloria Jean's and has set aside $1.3m in incentives to finance franchisees to make the change, including three multiple franchise operators. Gloria Jean's will get a scale boost from the acquisition to add to the existing 6 GJ stores in SA, and there will be immediate synergies from coffee, which will be supplied from an existing GJ roastery, as well as in cold drinks and network marketing.

The acquisition will produce between $1.2m-$1.8m a year in operating earnings (EBITDA) post synergies, a healthy return. For a relatively small amount, GJ store network is expanded by 15% in an area where they are currently underrepresented. This is a template to demonstrate that the stores can be rebranded, and the synergies delivered quickly.

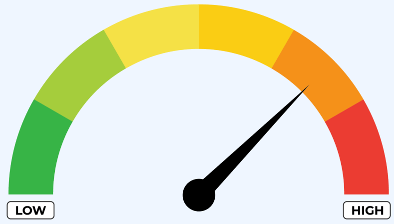
In other initiatives, Donut King Occasions, the online delivery for larger orders, is live in 62% of outlets. RFG is also Beefy's Pies by 5 stores. The sharp increase in employee costs from $32m to $42m in FY24 is due to company-owned stores almost doubling to 62 in FY24.

**Portfolio Risk Rating:** There is debt but a small amount and revenues remain $100m+ while there is a cost focus. Profitability marginal but forecast to improve. The low price point helps this business grow market share amid consumer pressure.

RADAR RATING: Stabilised earnings and partners a core of small businesses. Earnings growth through increased outlet numbers, acquisitions and product extensions.

RADAR RATING: **SPEC BUY**

**RISK RATING**



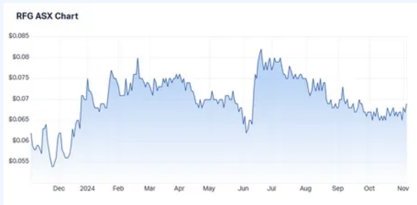

ASX CODE **RFG**

CURRENT PRICE **$0.069**

MARKET CAP $2492M

DIVIDEND YIELD 0%*

NET DEBT ($M) -5.1M

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**99% of all financial news relates to the 40 to 50 biggest companies.**
**So what about the rest? They're Under the Radar.**



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