

Smaller names big performers

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But it is unlikely to feel pain to the same degree as its peers. Indeed, in Goldman Sachs JBWere's books, it is the only mining services or contracting stock now worth buying.

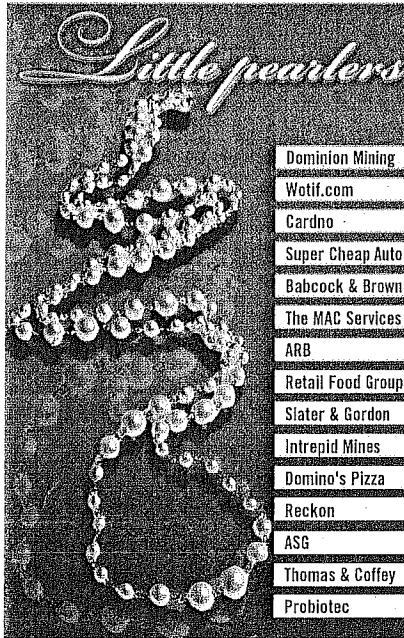
The broker has a 12-month price target of \$1.14 on the group and says the key reason for its positive recommendation is that the company has "hard assets that it can sweat through the downturn and still generate good earnings and cash flow".

Those hard assets are the 3558 rooms it has under ownership and management in Nebo, Coppabella, Moranbah, Middlemount and Dysart, towns in the coalfields of Queensland's Bowen Basin.

Under existing contracts, the company has about another 500 rooms to build in the second half of the financial year.

It is reviewing how many rooms it adds beyond that as capital preservation has become a priority, but analysts still expect dividend payments to progressively increase over the next two years.

The MAC bolstered its balance sheet with a \$45 million capital raising in September and does not have a lot of debt.



Consensus forecasts for small caps that posted solid first-half results

	Full year profit (\$m)		Total dividend (¢)	
	2009	2010	2009	2010
Dominion Mining	42.7	67.8	14.0	15.2
Wotif.com	42.1	47.6	17.2	19.2
Cardno	39.1	43.6	32.3	35.3
Super Cheap Auto	29.2	31.5	13.8	14.8
Babcock & Brown Wind	27.0	26.1	9.0	9.3
The MAC Services Group	25.3	27.9	9.1	9.8
ARB	21.2	23.0	16.0	18.0
Retail Food Group	20.9	24.1	9.8	11.3
Slater & Gordon	17.3	19.9	4.0	4.0
Intrepid Mines	16.7	16.5	0.0	0.0
Domino's Pizza	13.8	16.6	11.9	13.9
Reckon	13.8	15.2	6.8	7.5
ASG	11.5	15.3	4.0	5.5
Thomas & Coffey	10.7	15.1	7.0	9.0
Probiotec	8.9	11.5	2.4	3.0

SOURCE: BLOOMBERG, MACQUARIE RESEARCH, WILSON HTM FORECASTS, EL&C BAILLIET FORECASTS

Probiotec

Probiotec is a small-cap gem that's gone unnoticed by many investors but could be one worth watching for its impressive earnings growth profile. Despite the difficult retailing environment, the minnow pharmaceutical products manufacturer and marketer delivered a hefty 73.5 per cent increase in net profit to \$4.27 million for the half-year to December 31, 2008. Sales revenue also rose 41.3 per cent to \$46.5 million, while the fully franked interim dividend increased by 25 per cent to 1.25¢.

Pengana Capital's Prendergast calls the result an "absolute cracker", given management forecasts had been conservative, predicting a 20 per cent lift on the bottom line.

Ord Minnett senior research analyst Richard Ivers agrees, but notes it is not only the quantum of the earnings growth that was impressive but also the quality of the company's earnings mix.

"They are transitioning towards branded products where they actually own the brand, where the margins are higher and barriers to entry are also higher. So the earnings stream is better quality," he says.

"This was the company's strategy when they listed two years ago and they continue to deliver. It's a much better place to be going forward, to have that more sustainable earnings base."

As well as contract manufacturing pharmaceuticals, Probiotec has a suite of own-brand products, including the Celebrity Slim range of weight-loss products sold through Priceline pharmacies, the Biosource range of vitamin supplements and Milton antibacterial hygiene products.

In the first half, revenue from Probiotec's branded product division increased 86 per cent.

The company is also expecting additional growth this quarter from its "The Biggest Loser Club" range of slimming products, which accompanies the popular television show. Launched in December, the range is stocked in Coles and Woolworths supermarkets across Australia.

Prendergast notes the first-half result could have been even better,

given the costs of building the brand were all absorbed in the first half. He expects the second half to improve as the catch-up effect on earnings from the brand's sales washes through.

Ivers also expects cash flows to improve in the second half for the same reason.

He is forecasting revenues of \$49.7 million over that period, while net profit is expected to be \$4.7 million. Following the interim result, he also raised his fiscal 2009 normalised net profit forecast by 16 per cent to \$8.9 million and fiscal 2010 by 36 per cent to \$11.5 million. His valuation on Probiotec is \$1.70, which compares to yesterday's opening price of \$1.40.

Super Cheap Auto

The diversified retailer is another example where strong management helped to deliver a solid result. Net profit for the 26 weeks to December 27 increased by 8.7 per cent to \$13.6 million, ahead of analyst forecasts. The group also increased its fully franked interim dividend to 6.5¢ from 5.5¢ in the previous corresponding period.

What impresses most market watchers is the group's control of working capital and inventory, which has helped cash flow increase by 74 per cent to \$46.6 million.

"They managed inventory spectacularly and that was a standout that came through the cash flow and the operating cash flow," Perennial's Oshry says.

"It's a tribute to good management, I must say. That's what it has to come down to and a credit to how they have managed their way through this period."

A key to the group's success, market watchers say, is how the group is managing its brands. Super Cheap's operations encompass the mature Super Cheap Auto stores, as well as the growing Boating, Camping, Fishing (BCF) stores and the more embryonic Goldcross Cycles business. Oshry notes that the group is trying to perfect the Goldcross concept before rolling it out nationally, something that has worked for the other two brands.

Wilson HTM institutional adviser Simon Robinson also ties the group's success to the fact that each brand concept is worked through

and tested before any expansion. "It's not aggressive growth for growth's sake. It is very well managed," he says.

Robinson says that Super Cheap also "hits the criteria on a range of factors", while ABN Amro analyst Josephine Little calls it a company that is "doing all the right things".

"We believe Super Cheap has been built to have a greater level of resilience in times such as these," she says.

"Combine this with a management team that is delivering on core initiatives to rein in costs and working capital requirements and you have a compelling investment case, in our view."

She is forecasting normalised earnings per share growth of 11.1 per cent in fiscal 2009 and 13.3 per cent in fiscal 2010. Dividends are forecast to be 13¢ and 14¢ in the same respective periods. The target price is \$2.90, which compares to Super Cheap's opening price yesterday of \$2.40.

ARB Corp

The manufacturer and distributor of four-wheeler-drive accessories fits into the "gems" category for its solid track record of posting consistent earnings growth.

And ARB is confident it can continue to deliver, despite facing some tough macro-economic conditions, after posting double-digit earnings and revenue growth in the first half.

A mixture of organic growth, additions of new stores and the acquisition of the Thule car-rack systems business last October helped

the company achieve a 16.6 per cent lift in total revenue to \$96 million for the six months to December 31. Interim net profit rose 13.7 per cent to \$10.5 million, while its interim dividend also increased to 6.5¢ fully franked, from 6¢.

"It all comes down to superior management," Perpetual's Cunningham says.

"Going forward they have got positives and negatives but I think it is a prime example of what superior management brings to a company."

As an after-market car parts and service company, ARB faces an obvious head wind if car sales decline and consumer confidence continues to wane.

On the plus side, it should benefit from the lower Australian dollar (it has US operations), the federal government's stimulus package, lower fuel prices, lower interest rates and a falling steel price.

Cunningham expects ARB to post a fairly flat second half, due to the mixture of these pros and cons.

ARB itself, while not giving clear guidance, also says it is "well placed" to address the uncertain environment thanks to its strong brands, strong distribution channel and healthy balance sheet.

At December 31, 2008, ARB had net debt of \$8.2 million.

Macquarie Research gives ARB a tick of approval amid some tough conditions, rating the stock "Outperform".

"ARB is a well-managed company with an enviable track record," it says.

"The balance sheet remains lightly geared and, while near-term demand is set to soften, it has the

brands, distribution and product development capabilities for us to remain comfortable with its longer-term growth trajectory."

Macquarie is forecasting earnings per share growth of 9.4 per cent in fiscal 2009 and 5.2 per cent in fiscal 2010.

Dividends are expected to be 16¢ and 18¢ in those respective periods.

Thomas & Coffey

The minnow industrial contractor is one of the select number of services defying the economic downturn, posting a healthy 49 per cent increase in interim profit to \$4.7 million.

The group, which provides a range of building project management, engineering project management and industrial trade services, says its industry specialisation strategy, diverse customer portfolio and low debt levels have contributed to the earnings increase.

The group also boosted its dividend by 25 per cent to 2.5¢ a share, fully franked.

Souls Funds Management's Stephens says Thomas & Coffey is a company with "lots of options for growth."

"The attraction to a business like that is they are in a sweet spot in terms of size," he says.

"They can pick up slightly larger contracts, which for the big players might not be worth going for, and some players might not be as focused on service. The business over the last couple of years has a renewed focus on adding value to customers."

While Thomas & Coffey does not give specific earnings guidance, it says it expects fiscal 2009 profit after tax to exceed that of 2008 before recent acquisitions.

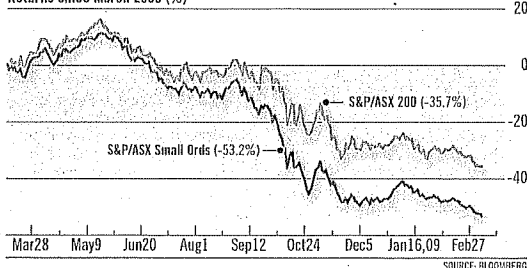
Last year the group strengthened its presence in the aluminium sector with the acquisitions of Holcan and Pintab and also expanded its presence in the Hunter Valley of NSW through the purchase of contracting group Laing O'Rourke.

It says that, despite challenging conditions in the sector, it is "well placed" to develop its market position, while it should also benefit from increased outsourcing as companies cut costs.

Souls' Stephens says growth

Heading south

Returns since March 2008 (%)



SOURCE: BLOOMBERG