

Codan Signals Hope Amidst Mining Gloom

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-Business forming a base?

-FY16 to be "ahead" of FY15

-Valuation considered cheap

Despite the gloom and doom prevailing in the mining industry, communications and mine technology supplier Codan (CDA) offers a glimmer of hope that the market is forming a base. The company's first half result missed expectations but both Moelis and Canaccord Genuity detect growth on the horizon.

Bright spots include a strong start to the second half for metal detection. Radio communications revenue fell 21%, largely on the timing of HF Radio (HFR) sales, and was the key factor in the 5.0% fall in overall revenue. In contrast, metal detection revenue was up 24%, underpinned by the launch of the GPZ 7000 and GO-FIND products during the half year.

Land Mobile Radio (LMR) and HF Radio earnings are improving and expected to be better in the second half. Instability and conflict in a number of the company's markets is seen producing an increase in demand for HFR.

Management stopped short of providing definitive guidance but indicated FY16 profit should be ahead of FY15. On this basis, Canaccord Genuity is more confident that the second half will be stronger. The broker's revised estimates imply second half earnings of \$18.2m versus \$14.7m in the first half. Earnings per share estimates are lowered to 8.5c for FY16 and to 10.3c for FY17.

The company's mining technology is still in development but management expects to break even in the second half. Canaccord is of the view that the stock is undervalued, trading on a FY16 enterprise value/earnings multiple of 3.9 and prospective dividend yield of 6.1%. Base line earnings are estimated at around \$30m. Given the current price relative to the broker's \$1.02 target, lowered from \$1.12, a Buy rating is maintained.

Net profit was up 17%, on an underlying basis, Moelis observes, while margins improved to 23%. The company declared a 2c fully franked interim dividend. The broker welcomes the upbeat commentary from the company, which suggests its performance should be better in the second half. This should be led by a strong order book for HF radios and a small surge in gold detection requirements in parts of Africa.

Moelis also maintains a Buy rating and target of \$1.05, estimating a total return of 54% and a 6.5% fully franked dividend yield. The broker suspects, with stable earnings in the first half, that the company has found an earnings base.

This broker, too, considers the multiples undemanding and believes Codan offers value in its turnaround story while there is a free option on any African effect on metal detector sales beyond the broker's estimates.

As the company is intent on driving demand for its GPZ 7000 into Africa, Moelis expects upside if any gold rush or demand surge occurs. The company has noted strong demand for GPX 4500 units in Chad, which suggests a meaningful contribution to earnings in the second half and a chance to clear out excess inventory.

Meanwhile, cost cutting is in train on project and non-critical engineering staff considered discretionary expenditures, until the market recovers and demand increases.