

Ag & Vet Weekly



Monday May 25 – Friday May 29, 2020

All the news on ASX-listed agriculture and veterinary companies

- * MAY 29: ASX DOWN, AVW-45 UP: NANOLLOSE UP 6; MGC DOWN 8%
- * DR BOREHAM'S CRUCIBLE: SYNLAIT MILK
- * SELECT H1 REVENUE DOWN 6% TO \$94m, PROFIT DOWN 13% TO \$17m
- * SYNLAIT COVID-19 CUTS FORECAST MILK PRICE
- * MGC: ISRAEL PHASE IIb CANNEPIL EPILEPSY TRIAL
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- * PALLA TERMINATES UK CUSTOMER ACQUISITION; OWED \$3.5m
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- * YARRA FUNDS REDUCES TO 6% OF ELDERS
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- * CRESO REQUESTS 'CAPITAL RAISING' TRADING HALT
- * CANN GLOBAL EXTENDS 'RESEARCH INITIATIVES' SUSPENSION
- * TASSAL APPOINTS JAMES FAZZINO DIRECTOR
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- * PHARMAUST REQUESTS 'SARS-COV-2 PRE-CLINICAL RESULTS' HALT

MARKET REPORT

The Australian stock market was down 1.63 percent on Friday May 29, with the ASX200 down 95.4 points to 5,755.7 points. Sixteen of the AVW-45 stocks were up, 15 fell, nine traded unchanged and five were untraded.

Nanollose was the best, up 0.2 cents or 6.25 percent to 3.4 cents, with 131,371 shares traded. Memphasys rose 6.1 percent; Elders was up 5.1 percent; Apiam, MGC and THC climbed four percent or more; Clover and Wide Open improved more than three percent; Anantara, Cann Group and Pharmaust were up more than two percent; Cannpal, Seafarms and Tassal rose one percent or more; with A2 Milk and Ecofibre up less than one percent.

MGC led the falls, down 0.2 cents or 8.3 percent to 2.2 cents, with 8,122,935 shares traded. Elixinol and Palla fell more than five percent; Next Science and Roots lost more than four percent; Nufarm, Select Harvests and Synlait were down more than three percent; Bega, Costa, Fonterra and Huon shed more than two percent; with Althea, Food Revolution and Regeneus down by more than one percent.

DR BOREHAM'S CRUCIBLE: SYNLAIT MILK

By TIM BOREHAM

ASX code: SM1

NZX code: SML

Share price: \$6.48

Shares on issue: 179,306,908

Market cap: \$1,161.9 million

Chief executive officer: Leon Clement

Board: Graeme Milne (chairman)*, Willem Jan (Bill) Roest**, Dr John Penno, Sam Knowles, Min Ben, Qikai (Albert) Lu, Sihang Yang and former MP Ruth Richardson***

* Mr Milne will step down at the end of the 2020-'21 year (Jul 31, 2021)

** Mr Roest will step down at the end of the 2019-'20 year

*** The last four directors listed are Bright Group representatives

Financials (half year to January 31, 2020)*: revenue \$559 million (up 19%), earnings before interest tax depreciation and amortization \$67.6 million (down 4%), net profit after tax \$26.2 million (down 30%), earnings per share 14.61 cents (down 30%), net debt \$447.4 million (up 55%)

* All figures are in New Zealand dollars. \$NZ1.00 equals \$A0.93

Major identifiable holders: Bright Dairy Holdings 39%, A2 Milk Company 17.39%, Dr Penno 2.85%.

At the risk of offending trans-Tasman relations and jeopardizing the prospect of a Covid-19 free travel 'bubble' between the Anzac** nations, Synlait is not well known by investors on this side of the ditch.

The company - NZ's biggest infant formula maker and the fourth biggest dairy processor - graces the Kiwi bourse but has a secondary ASX listing.

What's better known here is the similarly dual-listed A2 Milk Co, which markets infant milk powder produced by Synlait. Measured by market capitalization, A2 is more than 10 times the size of Synlait.

(** Australia and New Zealand Army Corps)

But Synlait is seeking to change its behind-the-scenes status with a recent acquisition that delivers a portfolio of well-known consumer brands.

On April 1, the company settled the acquisition of Dairyworks, after the Office of Overseas Investment (OOI) - the equivalent of Australia's Foreign Investment Review Board - gave the nod.

OOI permission was needed because Synlait is majority foreign owned, with China's Bright Dairy accounting for 39 percent of the register and the Sydney-headquartered A2 another 17 percent.

Unveiled in October last year, the \$NZ112 million (\$AUD104 million) Dairyworks purchase delivers more than 500 cheese, butter, ice cream and milk powder products under the Dairyworks, Deep South, Alpine and Rolling Meadow names.

The operations of the Christchurch-based Dairyworks dovetail with key assets of the primary cheese processor Talbot Forest, which Synlait bought last year.

CEO Leon Clement says the rationale for buying Dairyworks is udderly clear: "to come closer to the consumer and own more of the value chain".

Dairyworks accounts for half the Kiwi cheese market and half the butter market and has a presence on Australian supermarket shelves.

Synlait has been in expansionary mode on other fronts as well, having acquired 28 hectares of land at Pokeno in the Waikato district on the upper North Island for \$NZ156 million in early 2018.

Happily, the site now houses a \$NZ260 million, state-of-the-art formula plant.

Sadly, Synlait is in the midst of a legal dispute over restrictive covenants attached to the property, which the company presumed would be removed. In fact, the country's High Court DID remove them, but at the behest of a neighbor who was protecting quarrying interests, the Court of Appeal overturned the 'de-covenanting' in May 2019.

Synlait then won leave to appeal in the Supreme Court, which after a coronavirus related delay, will hear the case on June 3. If Australian readers are puzzled, the Kiwi Supreme Court - not the High Court - indeed is the supreme court in the land.

But let's get track on back.

Mooving with the times

Founded by thirty-something dairy scientists, John Penno and dairy farming couple Ben Dingle and Juliet Maclean in 2000, Synlait was based on one 3,000-cow dairy property, Robindale Farm.

The 2007 acquisition of Dunsandel Dairies moved the company into processing, with the first milk produced in 2008.

In 2012, Chinese mob Shanghai Pengxin struck a deal to buy the original farming operation Synlait Farms from the founders. The Overseas Investment Office approved the deal in early 2015 and the business now operates as Purata Farms.

Synlait listed on the New Zealand bourse in July 2013 and the ASX in November 2017.

In 2013, the company signed its first supply contract with A2 Milk and in 2015, Synlait acquired 25 percent of Sichuan New Hope Nutritionals and later signed a deal to supply infant formula exclusively for New Hope's Akara brand.

Synlait's next great leg-up came in 2017 when it bought the Auckland based NZ Dairy Company, which delivered the company's second blending and packing plant.

A former senior honcho with Fonterra - the world's biggest dairy company - Mr Clement replaced Dr Penno as CEO in August 2018. Dr Penno remains on the board.

A2 strategy remains on track

As well as strengthening its brand presence in its current pursuits, Synlait is interested in expanding into sports nutrition and "functional creams" (those providing a health benefit).

But the A2 aspect remains a key differentiator. For the uninitiated, specially bred A2 cows produce milk without the A1 beta-casein protein, with (disputed) health benefits including easier digestion.

The term A2 Milk is patented by the A2 Milk Company - and fiercely protected. But the A2 cows are naturally, rather than genetically, modified and, like 5G, have nothing to do with causing the coronavirus.

The Synlait supply agreement with A2 milk was recently expanded and extended, to July 2025 at the earliest.

Synlait also makes milk and cream for Foodstuffs, a large NZ co-operative retailer, on a white label basis (an appropriate use of the term indeed).

Reducing the carbon hoofprint

Synlait has a dedicated research and development facility at Palmerston North, with a targeted R&D spend of 1.5 percent of revenue.

Synlait's R&D activities have an 'environmental, social and governance' (ESG) focus, with commitments to tree planting, reducing energy and water usage and best-practice employment.

Earlier this year, the company spent \$NZ25.7 million to buy adjacent farmland at Dunsandel, partly to get better control over water rights and partly to do field research on sustainable farming methods.

It's the sort of company where "Saint" Jacinda Arden would be happy to plant a ceremonial tree - and indeed, New Zealand's Labour Prime Minister has done just that.

Recognizing Synlait's sustainability credentials, the ANZ Bank last year agreed to convert an existing \$NZ50 million facility into the country's first environmental social governance (ESG) loan.

An ESG loan offers incentives such as reduced interest for appropriate behavior - such as prime ministerial endorsed tree plantings.

Finances and performance

Synlait saw its half year revenue rise 19 percent to \$NZ559 million in the first half, with output rising 8.5 percent to 46.7 million kilograms of milk solids.

Revenue hit the \$NZ1 billion mark for the first time in the 2018-'19 year.

During the half year to January 31, 2020, sales of consumer-packaged infant formula rose 22 percent to 21,571 tonnes, but with Chinese sales off the pace on the back of "market consolidation".

The company has said it has not seen any Covid-19 supply chain disruption, but was monitoring the situation "very closely".

Sales of powders and creams declined 18 percent to 46,259 tonnes, owing to delayed deliveries.

The most recent purchases aside, Synlait has undertaken \$NZ470 million of "growth projects" over the last 24 months,

The expansions mean that Synlait's net debt has risen to \$NZ447.4 million from \$NZ287.8 million a year ago.

Late last year, the company issued a \$NZ180 million subordinated fixed rate bond listed on the NZ exchange.

The 3.83 percent coupon on these instruments might have seemed a bit mealy then, but no-one would complain now with the official Kiwi cash rate at 0.25 percent.

The increased interest and depreciation costs meant that Synlait's net profit fell 30 percent to \$NZ26.2 million.

In February, management guided full-year net profit to \$NZ70 million to \$NZ85 million, compared with \$NZ82.2 million in 2018-'19. Given the previous guidance was for earnings to go onwards and upwards, the stock drooped by 20 percent.

Over time, Synlait shares have traded as low as \$2.90 (December 2016) and as high as \$12.22 (September 2018). Over the last year they have drifted from the \$10 level.

Dr Boreham's diagnosis:

Despite the Chinese flavor of Synlait's register, China only accounted for eight percent of revenue during the half year, while NZ and Australia accounted for 35 percent and 24 percent respectively.

While missing out on links in the value chain, there's an argument for Synlait doing most of its China business via A2 Milk, which seems to be doing better than investors expected.

Still, broker Morgans questions the terms of last year's extension deal, which Synlait dubbed as being in line with the "ongoing competitive pricing regime".

The firm says: "We think the market will continue to question Synlait's bargaining power with A2 Milk and this is likely to continue to weigh on investor sentiment."

While infant formula has walked off the shelves during recent panic buying sprees, the China is characterized by tight margins and a consolidating market. It doesn't help that couples haven't indulged in rampant procreation despite the nation's one child policy being relaxed to allow two kids.

As with Bubs Australia, which we covered last time around, Synlait is waiting on all important product registration for its formula from the State Administrative Market Regulation (SAMR) for the Akara and Pure Canterbury infant formula lines.

Jacinda Arden is not the only visitor to grace Synlait's facilities: late last Chinese minister Xiao Yaqing, the big cheese responsible for the SAMR, popped his head into Pokeno for a look-see.

In early April, broker Select Equities upgraded Synlait from a 'sell' to a 'hold'.

"We remain a little cautious in light of the lack of significant new customers in the short to medium term, although we are reassured by Synlait's efforts to remedy this and to utilize recently expanded capacity."

Broker Bell Potter also rates the company a 'hold', with an uninspiring \$5 a share valuation.

Your humble columnist reckons it's all a matter of price: Synlait stock is trading on a multiple of around 16 times expected current year earnings, compared with A2 milk on roughly 35 times. ASX-listed processor Bega Cheese trades on a multiple of circa 40 times.

In summary, we don't think investors have milked all the upside already but maybe the cream on top isn't as fluffy as it once was.

Disclosure: Dr Boreham is not an agronomist and does not possess a relevant – or irrelevant - doctorate of any sort. His childhood dream was to become a dairy farmer in Saudi Arabia so he could be a ... wait for it ...milk sheikh.

SELECT HARVESTS

Select Harvests says revenue for the six months to March 31, 2020 was down 6.45 percent to \$93,521,000 with net profit after tax down 13.4 percent to \$17,357,000.

Select Harvests said revenue included \$54,200,000 from the almond division, \$72,038,000 from the food division and a loss of \$32,717,000 from its corporate division. The company said it had a fully franked interim dividend of 9.0 cents, with a record date of June 19, 2020 and payable on August 3.

Select Harvests said net tangible assets per share was down 2.63 percent to \$3.33, diluted earnings per share was down 14.3 percent from 21.0 cents to 18.0 cents.

The company said it had cash and cash equivalents of \$1,332,000 at March 31, 2020 compared to \$1,349,000 at March 31, 2019.

Select Harvests fell 22 cents or 3.4 percent to \$6.20 with 747,715 shares traded.

SYNLAIT MILK

Synlait says it has reduced its forecast base milk price from \$NZ7.25 (\$A6.77) to \$NZ7.05 (\$A6.59) for the year to July 31, 2020.

Synlait said its forecast for the year to July 31, 2021 was \$NZ6.00 (\$A5.62).

Synlait chief executive officer Leon Clement said, "the decision to reduce our forecast base milk price for the 2019 to 2020 season is because, in line with other commodities, dairy prices have eased significantly this year and as a result are lower than we were anticipating when the forecast was set in January."

"Covid-19 has created significant global uncertainty," Mr Clement said.

"We don't yet have a clear view of Covid-19's economic impact, but we do know it will impact demand, resulting in our decision to release a conservative opening forecast for the 2020 to 2021 season," Mr Clement said.

The company said it would continue to monitor movements, keep its farmer suppliers up to date and update the final milk price and forecast for the year to July 31, 2021 when it released its full year result in September 2020.

Synlait was down 23 cents or 3.4 percent to \$6.48.

MGC (MEDICAL GRADE CANNABIS) PHARMACEUTICALS

MGC says it has ethics approval for its 103-patient, phase IIb trial of Cannepil for drug resistant epilepsy at Israel's Schneider Children's Medical Center.

MGC said the trial would be a randomized, double-blind, placebo-controlled, parallel design phase IIb study of the safety and efficacy of Cannepil as an "add-on" treatment in children and adolescents with refractory epilepsy, or drug resistant epilepsies.

The company said patients would be aged between one and 18 years of age and receive 12 weeks of treatment, with the first patient treated in September 2020 and the final patient to be treated in October 2021.

MGC managing-director Roby Zomer said that "receiving ethics committee approval for the phase IIb clinical trial of Cannepil is another important milestone for the company".

"Cannepil is one of the company's lead cannabinoid medicine products with a very significant global market opportunity," Mr Zomer said.

"Israel is recognized for its world leading researchers and institutions in relation to cannabis products and we look forward to updating the market as this trial progresses," Mr Zomer said.

MGC was down 0.2 cents or 8.3 percent to 2.2 cents with 8.1 million shares traded.

ELIXINOL GLOBAL

Elixinol says its partially underwritten, one-for- 2.51 retails rights offer at 20 cents a share has raised \$5.6 million, taking the total raised to \$10.9 million.

Earlier this month, Elixinol said it had raised \$5.3 million through the institutional component of its rights offer at 20 cents a share, a 48.1 percent discount to the last closing price on May 5, 2020 (BD: May 5, 6, 2020).

Today, the company said the rights offer was partially underwritten to \$2.8 million and it received applications for \$3.1 million of the hoped for \$5.6 million, with the shortfall to be placed to sub-underwriters by lead manager, Bell Potter Securities.

Elixinol was down 1.5 cents or 5.4 percent to 26.5 cents with 3.4 million shares traded.

PALLA PHARMA (FORMERLY TASMANIAN POPPY INDUSTRY ENTERPRISES)

Palla Pharma says it ceased negotiations for the acquisition of unnamed "major" UK customer which owes it \$3.5 million for codeine phosphate supplies.

Last month, Palla said the option to acquire the UK customer's business expired on March 31, 2020, but negotiations were continuing (BD: Apr 1, 2020).

Today, the company said it would seek payment for outstanding invoices for codeine phosphate supply totalling GBP1.9 million (\$A3.5 million) to be repaid by the customer, which did not have its relevant licence reinstated.

Palla said that marketing authorizations acquired from the customer were valid and its finished dosage formulation supply would not be interrupted.

The company said it was transferring manufacturing to its Norway site, and expects Norwegian manufacturing approval by October 2020.

Palla said it expected its earnings for the six months to June 30, 2020 to be "significantly stronger" than the earnings for the six months to December 31, 2019.

Palla was down 4.5 cents or 5.7 percent to 75 cents.

PALLA PHARMA (FORMERLY TASMANIAN POPPY INDUSTRY ENTERPRISES)

Palla has told its annual general meeting that it is targeting the \$EUR802 million (\$A1,337.1 million) codeine market, with seven acquired marketing authorizations.

Palla said it hoped to sell codeine combinations in caplet and tablet form initially in the UK, including a 30mg codeine and 500mg paracetamol (30/500mg) caplet, a 30/500mg tablet and an 8/500mg tablet, with first sales expected by January 2021.

The company said it hoped to then target France and Spain in 2021.

Palla said it held marketing authorizations, which accounted for 57 percent of the annual European market, but did not disclose the fraction of the market it expected to win.

MURRAY COD AUSTRALIA

Murray Cod says a large fish death event at Lake Wyangan, near Griffith, New South Wales, is not linked to its operations.

Murray Cod said that NSW Department of Primary Industries Fisheries reported the event had affected Bony Herring, Golden Perch and Murray cod, but happened in a wild fish lake and was likely related to water quality issues.

Murray Cod was up 0.5 cents or 4.55 percent to 11.5 cents.

ELIXINOL GLOBAL

Elixinol says Shanghai Shunho New Materials Technology Co has terminated the \$500,000 purchase of subsidiary Hemp Foods Australia due to the impact of Covid-19. In February, Elixinol said it would sell Hemp Foods to China's Shanghai Shunho, through its subsidiary Yunnan Biological Pharmaceutical for \$500,000 by April 2020, conditional to a three-year licencing agreement appointing Shunho as manufacturer and distributor of its cannabidiol products in China, Hong Kong, Taiwan and Macau (AVW: Feb 3, 2020). The company said Shanghai Shunho had terminated the purchase on May 25, 2020 "due to non-satisfaction of a condition precedent in the [agreement], citing Covid-19 impacts". Elixinol said it would continue to operate Hemp Foods "pending an evaluation of all opportunities to capitalize on [its] strong position".

CANN GROUP, IDT AUSTRALIA

Cann Group says it will supply medical marijuana products manufactured by IDT Australia to Astral Health and Iuvo Therapeutics for distribution in the UK and Europe. Cann said it had a multi-year agreement with the London-based Astral for the supply of a range of IDT's formulated oils, including high tetrahydrocannabinol (THC), high cannabidiol (CBD) and a balanced formulation, with the possibility of additional products to be developed and supplied to Astral over time.

The company said it had a separate three-year agreement with the Neuss, North Rhine-Westphalia, Germany-based Iuvo Therapeutics GmbH to supply IDT's medical marijuana oil formulations and dried marijuana flower material for sale in Germany and other European countries.

The company said it would begin supplying the products under both agreements following regulatory approvals from Australian, UK and European authorities.

Cann Group chief executive officer Peter Crock said the company had shown "an ability to supply a broad range of products from specific medicinal cannabis cultivars to unique finished product formulations that meet our customers' specific end-market requirements". "Our manufacturing arrangements with IDT Australia ensure we can meet the high [good manufacturing practice] standards that reputable distributors in overseas markets such as the UK and Europe require," Mr Crock said.

In a separate announcement, IDT chief executive officer Dr David Sparling said that the export agreements were "great news for IDT".

"Expanded export channels allow us to scale-up our manufacturing and supply operations even further and the parties can leverage off IDT's experience exporting [current good manufacturing practice] pharmaceutical products to Europe and our dealings with the European regulators," Dr Sparling said.

Cann Group was up 2.5 cents or 2.2 percent to \$1.17.

IDT was unchanged at 17.5 cents.

THC (THE HYDROPONICS CO) GLOBAL GROUP

THC says it has prescribed the first Australian-produced full-spectrum marijuana product for Australian patients.

THC said that it would produce marijuana product produced from isolate for a schedule four high purity option over the coming weeks.

THC was up 1.5 cents or four percent to 39 cents.

ELDERS

Yarra Funds Management says it has reduced its substantial shareholding in Elders from 11,208,792 shares (7.20%) to 9,595,626 shares (6.16%).

The Melbourne-based Yarra Funds said that between March 25 and May 22, 2020 it bought 6,860 shares for \$58,104 or \$8.47 a share and sold 1,620,026 shares for \$13,985,804 or \$8.63 a share.

Elders was up 48 cents or 5.1 percent to \$9.95 with 1.8 million shares traded.

ELDERS

Perpetual says it has reduced its substantial shareholding in Elders from 11,202,937 shares (7.20%) to 9,354,632 shares (6.01%).

The Sydney-based Perpetual said that between May 11 and 21, 2020 it sold 1,848,305 shares for prices ranging between \$9.31 and \$10.21 a share.

CRESO PHARMA

Creso has requested a trading halt "until the completion and announcement of the ... capital raising".

Trading will resume on June 2, 2020 or on an earlier announcement.

Creso last traded at 6.8 cents.

CANN GLOBAL

Cann Global has requested a second extension to its voluntary suspension, following a trading halt "regarding current research initiatives" (BD: May 18, 20, 2020).

Cann Global said it expected an announcement to be made by June 2, 2020.

Cann Global last traded at 0.7 cents.

TASSAL GROUP

Tassal says it has appointed James Fazzino as a non-executive director.

Tassal said Mr Fazzino was a director of APA Group and Rabobank Australia and was the chair of Implant Solutions and Manufacturing Australia.

The company said that previously Mr Fazzino was an Incitec Pivot managing director.

Tassal said Mr Fazzino held a Bachelor of Economics.

Tassal was up six cents or 1.5 percent to \$4.02 with 1.3 million shares traded.

PALLA PHARMA

Palla Pharma says it has appointed Mertons Corporate Services' Mark Licciardo as company secretary, replacing Jaime Pinto, effective from today.

COSTA GROUP

Costa says its chief executive officer Harry Debney intends to retire within the next nine months having been with the company for 10 years.

Costa said it would enact a plan to establish an assessment and recruitment process for Mr Debney's replacement, with consideration to both internal and external candidates.

Costa was down eight cents or 2.4 percent to \$3.22 with two million shares traded.

PHARMAUST

Pharmaust has requested a trading halt “pending an announcement regarding disclosure of preliminary results from the Sars-Cov-2 pre-clinical trial”.

In April, Pharmaust said that Melbourne’s Water and Eliza Hall Institute would test the effects of monepantel on Covid-19 infections.

The company has been trailing the sheep worm treatment on dogs for cancer and earlier this month said that one dog of seven with naïve B cell lymphoma had a 60 percent reduction in tumor size (BD: Apr 17, May 12, 2020).

Trading will resume on June 2, 2020 or on an earlier announcement.

Pharmaust closed up 0.2 cents or 2.1 percent to 9.7 cents.