

## FEATHERSTONE

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## GREAT OAKS FROM ACORNS

Small stocks can produce some big returns for investors prepared to look beyond the blue-chip zone.

As analysts and the media focus on the main event during profit season – blue-chip company earnings – your columnist heads straight to the undercard: medium and small-cap enterprises. And even further down to micro-cap results written up as “briefs” in newspapers and barely covered by analysts and sharebrokers. The ones where the chief executive is surprised to be interviewed about the result.

The 20 stocks in the table are hardly “briefs”. Most are well-established profitable small and medium-size companies followed by institutional investors. This is why they made this column’s list of 20 top stock ideas published in early March. Small stocks were then as popular as American investment bankers as the financial crisis turned many small-caps into micro-caps – and a few into dead-caps.

What a difference a few months make. The average gain in the 20 stocks is about 35 per cent – just above the rise in the S&P/ASX 200 index since March 2 – but below the gain in the Small Ordinaries index. Relative performance was hurt by the low number of small resource stocks in the table. Still, look through the list and some top performers emerge: Super Cheap Auto, RR Australia, Iress Market Technologies, Blackmores, Corporate Express, Seek, Navitas, ARB Corporation and Northern Iron.

Others such as IMF Australia and Slater & Gordon had big rallies in the first quarter of this year as investors warmed to the prospect of more bear-market-inspired class actions.

Three stocks lost ground during the period: Infomedia and Reflex Holdings were down slightly and gold producer St Barbara halved from its March 2 price. Funds management investor

Treasury Group rose sharply but is still a few dollars shy of its price when first covered in this column. WHK Group, another wealth-management stock this column plumped for too early last year, gained slightly.

Enough of looking backwards. The challenge is deciding which stocks in the table have run too far and whether underperformers should be dumped for fresh blood. The profit season, when it finishes, will provide vital clues.

Super Cheap Auto, for example, is a well-run retailer with an excellent franchise, but it just looks a touch pricey at \$4.29. Navitas, a long-time column favourite, also looks fully valued, although this column said the same thing when the stock was \$2.50.

Vitamins group Blackmores is due for a bigger pause after such a strong rally as is employment portal Seek and emerging iron ore producer Northern Iron.

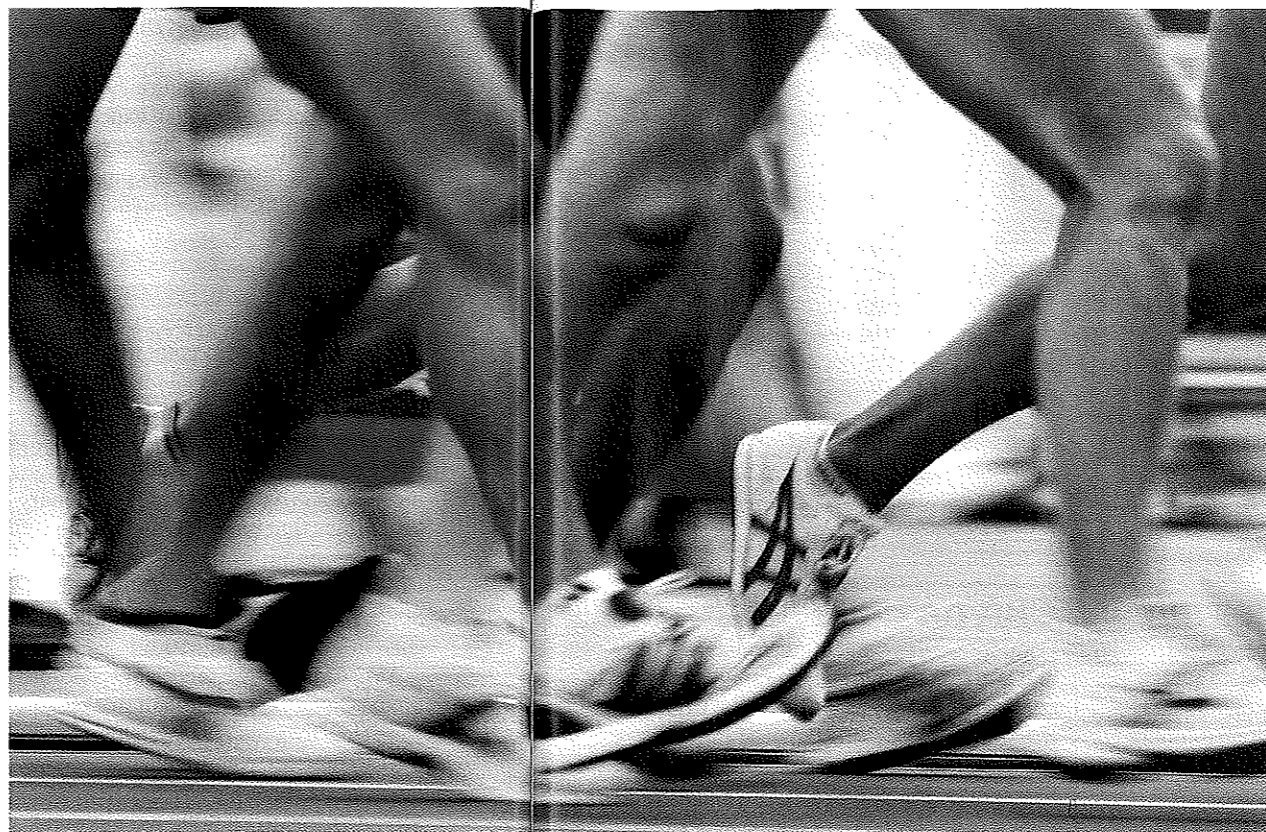
The column will stick with these stocks for now and instead dump the laggards: Infomedia, Reflex, Select Harvests and St Barbara. Better opportunities are elsewhere, even though all are good companies.

The table has four new stocks: Wridgways, Salmat, Servcorp and RCG Corporation. Two more speculative companies, Universal Biosensors and TFS Corporation, have

## TOP SEEDS: 20 PROMISING SMALL STOCKS

	Stock	ASX code	March 1 price \$	August 17 \$	Change %
1	Treasury Group	TRG	2.60	5.80	123.08
2	Northern Iron	NFE	0.85	1.87	120.00
3	Seek	SEK	2.56	4.84	89.06
4	Super Cheap Auto	SUL	2.43	4.29	76.54
5	RR Australia	RRA	0.45	0.71	59.55
6	ARB Corporation	ARP	2.70	4.18	54.81
7	IRESS Market Tech.	IRE	5.17	7.83	51.45
8	Blackmores	BKL	11.79	17.75	50.55
9	IMF Australia	IMF	0.99	1.45	45.73
10	Corporate Express	CXP	2.73	3.95	44.69
11	Navitas	NVT	2.29	3.16	37.99
12	The Reject Shop	TRS	10.30	14.00	35.92
13	SAI Global	SAI	2.29	2.88	25.76
14	Invocare	IVC	4.60	5.46	18.70
15	WHK Group	WHG	0.89	1.05	17.98
16	Slater & Gordon	SGH	1.50	1.71	14.00
17	Select Harvests	SHV	3.05	3.29	7.87
18	Infomedia	IFM	0.38	0.36	-5.26
19	Reflex Holdings	RDF	2.39	2.20	-7.95
20	St Barbara	SBM	0.42	0.21	-50.00
	Average gain				40.52
	Median gain				41.34

Source: BRW



Best foot forward:  
Rally for The Athletes  
Foot owner RCG

also caught this columnist's eye in the past few months. They are on the radar for future inclusion as are a few other micro-caps – certain to make the “briefs” columns when they report. More on them once their profits are announced.

Here are the four inclusions:

## 1. Wridgways

The transport services company has rallied from \$1.60 in March to \$2.38 and may have further to run as the economy strengthens. A provider of relocation services to companies and wealthier individuals, Wridgways is highly leveraged to the economy. More corporate activity means more executives being relocated around Australia and overseas. A pick-up in housing sales, especially in dearer suburbs, is also good news. Wridgways may benefit more later in the economic cycle as companies move staff around. The prospect of a decent acquisition, possibly in Asia, also appeals. Wridgways, largely debt free, has performed better during the recession than many expected – companies downsizing in recession also create plenty of work for removalists to relocate executives. Wridgways' full-year profit, due this month, will be closely watched.

Gary Hershorn/Reuters

## 2. Servcorp

The serviced office provider has jumped from \$2.20 in March to \$3.39, but still looks reasonable value for long-term investors. Servcorp shares were dumped when global recession crimped office space demand. Servcorp has \$92 million in cash, making it well placed to take advantage of sharply lower leasing costs for its serviced offices overseas. The timing can scarcely be better for Servcorp's planned expansion into New York in early 2010 and possibly Chicago, Atlanta and London. Servcorp should benefit later in the economic cycle as more activity among smaller enterprises leads to more demand for serviced office accommodation. Profits for this year and next may be down as the fallout from global recession affects earnings. Watch for Servcorp to pounce on opportunities for faster growth as demand recovers.

## 3. Salmat

The direct marketing company, featured here in May, has rallied in the past four weeks. Investors liked Salmat's defensive qualities during the economic downturn as more companies moved away from expensive brand advertising towards tactical advertising such as the product catalogues that Salmat distributes. But big investors are now focusing more on companies with greater cyclical exposure. The real story is the transformation that new chief executive, Grant Harrod, can engineer in Salmat. Harrod has a good record as chief executive of Corporate Express Australia and hopes are high he can deliver more success at Salmat.

## 4. RCG Corporation

The owner of The Athlete's Foot (Australia) has rallied as investors warmed to the surprisingly strong performance of its shoe franchise and RCG's large cash holding. RCG paid \$US6.2 million this month for long-term agreements for The Athlete's Foot in Australia and New Zealand that remove ongoing licence fees. This will boost 2009-10 profit by \$1.2 million and provide higher returns than cash. The big payoff may be removing tight restrictions on competing with The Athlete's Foot, making RCG better placed for another acquisition – possibly in the footwear industry – that can leverage The Athlete's Foot's technology, systems and customer base. BRW

