

FINANCIAL REVIEW

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The relentless march of the ASX's growth darlings



The market is evenly split on whether the momentum names face a rocky earnings season.

by [Vesna Poljak](#)

A handful of stocks are commanding multiples of more than 40, 70 and 100 times forecast earnings, the surest sign that the ASX's technology sector is experiencing a melt-up and possibly even bubble-like tendencies just weeks ahead of the annual earnings season.

WiseTech Global, Appen, Altium, Xero and Afterpay Touch Group have become the faces of a new generation of market darlings that are putting light years between the value and growth spectrums of the market. Aconex was part of the same club of favourites [but Aconex was acquired by Oracle late last year](#) – demonstrating the acute risk of shorting high-growth names in the Australian market.

While some fund managers have backed them enthusiastically, the performance of these stocks invokes uneasy parallels with junior explorers in the last mining boom.

With the results season only four weeks away, the market is evenly split over whether earnings risk could pose a challenge to the software as a service (SaaS) and consumer technology plays.



WiseTech Global CEO Richard White. The memory of WiseTech's 15 per cent plunge in February's interim reporting season after it fell short of market consensus should serve as a warning of how quickly sentiment can turn against the market's richest names. *Jessica Hromas*

"It's all about momentum and not so much about the earnings," said fund manager Simon Conn from Investors Mutual. With the Australian market failing to attract sizeable and varied floats beyond [Friday's Viva Energy](#), and a rush of takeovers narrowing the field in small caps, there is arguably an imbalance of demand and supply for the right names.

"We've got a small basket of stocks which have growing businesses, it's just that the valuations people are ascribing are way above what a prudent investor should pay for these at this stage of their evolution," Mr Conn said.

Serve as a warning

But the [memory of WiseTech's 15 per cent plunge in February's interim reporting season](#) after it fell short of market consensus should serve as a warning of how quickly sentiment can turn against the market's richest names. On Thursday the stock added 93¢ or almost 6 per cent to \$17.09. It is up 21 per cent year to date and 52 per cent since its February low.

Aconex was another stock which attracted price volatility around its results.

"My analogy would be the mining boom where the specy mining companies used to do very well before they actually mined anything," said Steve Black, [co-manager of the Pengana Emerging Companies Fund](#). "There's little intrinsic valuation support from which to draw from. It captures the imagination of investors – 'what could they be worth?'. In a world where the FAANG stocks are running hard, it's not that surprising."

The FAANGs or Facebook, Apple, Amazon, Netflix and Google look cheap next to their Australian counterparts. They trade at an average multiple of 37 times forecast earnings, although there are alternative ways of valuing the tech universe such as enterprise value-to-sales or revenue multiples.

On an earnings multiple, the data centre operator NextDC is the most expensive stock in the S&P/ASX 200 Index, according to Bloomberg data. The stock trades on a forward price-earnings multiple of 133 times.

ASX tech sector performance also leaves the FAANGs in the shade; the NYSE index of the same name is up 32.5 per cent in US dollar terms year-to-date. "They're companies that are unlikely to disappoint in the very short term as whilst the valuations are obviously in the stratosphere, they could well deliver in the reporting season, which is only a month away," Mr Black said. "Until you can value them properly, they become speculative stocks, in our view."

New names

As well as lighting up the bourse, the Australian tech contingent has introduced new names to the ranks of [Australia's wealthiest](#), according to the 2018 Rich Bosses list.

Elsewhere, shares of Appen are up 49.6 per cent this year to \$12.43, Altium 58.4 per cent to \$21.04, Xero 59.8 per cent to \$45.80 and Afterpay 81.7 per cent to \$10.85.

"At these prices the shares are priced to perfection so any disappointment [around results] will be taken pretty harshly," said Mr Conn.

That is exacerbated by the Australian market's ability to be captured by momentum.

As a factor, momentum has been a reliable source of outperformance.

Last month, UBS downgraded Altium to a "sell" on valuation grounds, citing its then enterprise value-to-earnings before interest, tax, depreciation and amortisation (EV/EBITDA) multiple of 38 times, up 80 per cent over 12 months. On a scatterplot of Australian and global SaaS peers, WiseTech and Altium were outliers measured on both EV/EBITDA and enterprise value-to-sales.