FORSYTH BARR

Augusta Capital

NEUTRAL

Funds Management Momentum

Augusta Capital (AUG) has been the leading performer in the listed property sector year-to-date with a return of +46% and we have pulled our rating back from OUTPERFORM to NEUTRAL. The business remains with considerable momentum in terms of deal flow and the establishment of new funds. NEUTRAL.

What's changed?

- **Earnings:** No change
- **Target Price:** Lifted +7% to NZ$1.38
- **Rating:** Downgraded to NEUTRAL

Downgraded to NEUTRAL after a stellar run

AUG has had a strong share price run since we updated our rating to OUTPERFORM (in our research note *'Growth Under Management'* dated 14 June 2019) and we have pulled our rating back to NEUTRAL. AUG has had the sector leading total return of +46% year-to-date.

Upgraded target price

As detailed in our property sector report *'Real Estate reflections'* dated 5 September, we have made changes to our weighted average cost of capital (WACC) assumptions and have adopted our new, firm wide, risk free rate and market risk premium across all of the 10 listed property vehicles that we cover. The new risk free rate is 2%, down from 2.75% and the market risk premium is now 7.5%, down from 7.75%. The net result is a lift in the AUG target price of +7% to NZ$1.38. Given the relatively low asset betas in the listed property sector this has had a material positive impact on our DCF valuations. The level of impact on our target prices is less significant, given our target price is a 50% blend of our DCF valuations and our unchanged NAV valuations. While the lower WACC has lifted our target prices by +7% to +17% it has had little impact on our investment ratings. This is because our investment ratings are relative to the listed property sector, not the wider equity market.

Robust deal outlook continues

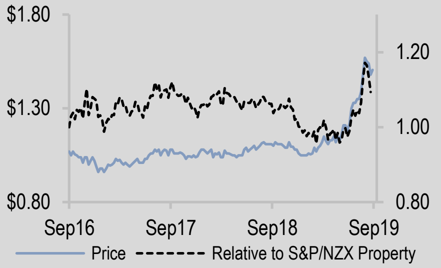
The Tourism Fund is a key focus and this is targeted for launch in late FY20. We also expect progress with a large format retail fund, the Value Add Fund No. 2 and Asset Plus in FY20. AUG has also just announced plans to set up its first residential land development project. AUG is conducting due diligence on a 40ha block just outside of Warkworth. There is potential for up to 800 homes to be developed on the land accompanied with other amenities including a neighbourhood centre. The new fund is likely to be targeted at wholesale investors who are more interested in capital gain over defensive stabilised return, which appeals more to retail investors.

Investment View

AUG remains well positioned to grow across a range of funds management vehicles and has transitioned to a fully funds management business. It remains with an attractive dividend yield, but earnings are potentially more volatile in the near-term as it moves to focus on base management fees versus transaction fees. AUG is an increasingly valuable, well performing and unique funds management vehicle. Our rating is NEUTRAL.

NZX Code	AUG
Share price	NZ$1.51
Target price	NZ$1.38
Risk rating	High
Issued shares	87.5m
Market cap	NZ$132m
Average daily turnover	43.4k (NZ$53k)

Share Price Performance



Financials: March	19A	20E	21E	22E
NPAT* (NZ$m)	7.7	6.3	6.2	5.1
EPS* (NZc)	8.8	7.2	7.1	5.8
EPS growth* (%)	34.1	-18.9	-0.8	-18.9
DPS (NZc)	6.1	6.5	6.5	5.5
Imputation (%)	0	100	100	100

Valuation (x)	19A	20E	21E	22E
EV/EBITDA	10.4	8.5	5.9	6.8
EV/EBIT	10.4	8.5	5.9	6.8
PE	17.0	21.0	21.1	26.1
Price / NTA	2.0	1.6	1.6	n/a
Cash dividend yield (%)	4.1	4.3	4.3	3.6
Gross dividend yield (%)	4.1	6.0	6.0	5.1

*Historic and forecast numbers based on underlying profits

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Augusta Capital Ltd (AUG) Priced as at 04 Sep 2019: NZ$1.50 March year end

Forsyth Barr valuation			
Valuation methodology		Blend of 50% DCF & 50% Adj NAV	
12-month target price (NZ$)*	**1.38**	**Spot valuations (NZ$)**	
Expected share price return	-8.3%	1. DCF	1.39
Net dividend yield	4.3%	2. Adj NAV	1.29
Estimated 12-month return	-4.0%	3. n/a	n/a
Key WACC assumptions		**DCF valuation summary (NZ$m)**	
Risk free rate	2.00%	Total firm value	113.2
Equity beta	0.81	(Net debt)/cash	6.2
WACC	6.6%	Value of equity	107.0
Terminal growth	1.5%	Shares (m)	87.5

Profit and Loss Account (NZ$m)	**2018A**	**2019A**	**2020E**	**2021E**	**2022E**
Sales revenue	18.9	22.0	19.2	19.2	17.8
Normalised EBITDA	**10.3**	**11.7**	**8.7**	**8.6**	**7.4**
Depreciation and amortisation	-	-	-	-	-
Normalised EBIT	**10.3**	**11.7**	**8.7**	**8.6**	**7.4**
Net interest	(2.8)	(1.5)	(0.3)	(0.3)	(0.8)
Associate income	-	-	-	-	-
Tax	(1.8)	(2.4)	(2.0)	(2.0)	(1.5)
Minority interests	-	-	-	-	-
Normalised NPAT	**5.8**	**7.7**	**6.3**	**6.2**	**5.1**
Abnormals/other	(4.8)	(0.8)	(0.7)	(0.1)	(0.1)
Reported NPAT	**1.0**	**7.0**	**5.6**	**6.1**	**4.9**
Normalised EPS (cps)	6.6	8.8	7.2	7.1	5.8
DPS (cps)	5.6	6.1	6.5	6.5	5.5

Growth Rates	**2018A**	**2019A**	**2020E**	**2021E**	**2022E**
Revenue (%)	-0.8	16.6	-12.8	-0.3	-7.1
EBITDA (%)	-5.3	13.1	-25.9	-1.1	-13.1
EBIT (%)	-5.3	13.1	-25.9	-1.1	-13.1
Normalised NPAT (%)	-14.4	34.1	-18.9	-0.8	-18.9
Normalised EPS (%)	-14.4	34.1	-18.9	-0.8	-18.9
DPS (%)	2.3	8.9	6.1	0.0	-15.6

Cash Flow (NZ$m)	**2018A**	**2019A**	**2020E**	**2021E**	**2022E**
EBITDA	**10.3**	**11.7**	**8.7**	**8.6**	**7.4**
Working capital change	(4.3)	0.3	(0.2)	0.0	0.2
Interest & tax paid	(5.2)	(4.8)	(2.4)	(2.3)	(2.4)
Other	-	-	-	-	-
Operating cash flow	**0.8**	**7.2**	**6.0**	**6.2**	**5.2**
Capital expenditure	(0.2)	(0.3)	-	-	-
(Acquisitions)/divestments	(3.2)	31.0	14.8	(15.0)	(0.7)
Other	(5.3)	(1.6)	-	-	-
Funding available/(required)	**(7.9)**	**36.3**	**20.8**	**(8.8)**	**4.6**
Dividends paid	(4.8)	(5.3)	(5.7)	(5.7)	(5.0)
Equity raised/(returned)	-	-	-	-	-
Increase/(decrease) in net debt	**12.7**	**(31.0)**	**(15.1)**	**14.4**	**0.5**

Balance Sheet (NZ$m)	**2018A**	**2019A**	**2020E**	**2021E**	**2022E**
Working capital	1.5	(0.2)	(0.5)	(0.5)	(0.7)
Fixed assets	85.3	31.5	0.7	0.6	0.5
Intangibles	21.7	20.2	20.2	20.2	20.2
Other assets	25.3	42.2	72.2	87.2	87.9
Total funds employed	**133.7**	**93.6**	**92.7**	**107.5**	**107.9**
Net debt/(cash)	37.5	6.2	(9.0)	5.4	5.9
Other non current liabilities	12.1	1.3	1.3	1.3	1.3
Shareholder's funds	84.2	86.1	100.3	100.7	100.6
Minority interests	-	-	-	-	-
Total funding sources	**133.7**	**93.6**	**92.7**	**107.5**	**107.9**

Valuation Ratios	**2018A**	**2019A**	**2020E**	**2021E**	**2022E**
EV/EBITDA (x)	14.2	10.4	8.5	5.9	6.8
EV/EBIT (x)	14.2	10.4	8.5	5.9	6.8
PE (x)	22.8	17.0	21.0	21.1	26.1
Price/NTA (x)	2.1	2.0	1.6	1.6	1.6
Free cash flow yield (%)	0.4	5.2	4.6	4.7	4.0
Net dividend yield (%)	3.7	4.1	4.3	4.3	3.6
Gross dividend yield (%)	5.2	4.1	6.0	6.0	5.1
Imputation (%)	98	0	100	100	100
Pay-out ratio (%)	85	69	91	91	95

Capital Structure	**2018A**	**2019A**	**2020E**	**2021E**	**2022E**
Interest cover EBIT (x)	3.7	7.8	25.4	26.6	8.9
Interest cover EBITDA (x)	3.7	7.8	25.4	26.6	8.9
Net debt/ND+E (%)	30.8	6.7	-9.9	5.1	5.5
Net debt/EBITDA (x)	3.6	0.5	n/a	0.6	0.8

Key Ratios	**2018A**	**2019A**	**2020E**	**2021E**	**2022E**
Return on assets (%)	7.3	11.4	8.6	7.4	6.4
Return on equity (%)	6.9	9.0	6.3	6.2	5.0
Return on funds employed (%)	0.0	0.0	0.0	0.0	0.0
EBITDA margin (%)	54.7	53.0	45.0	44.7	41.8
EBIT margin (%)	54.7	53.0	45.0	44.7	41.8
Capex to sales (%)	1.3	1.4	0.0	0.0	0.0
Capex to depreciation (%)	n/a	n/a	n/a	n/a	n/a

Operating Performance	**2018A**	**2019A**	**2020E**	**2021E**	**2022E**
Net revenue by segment:					
Net rental income	5.7	3.0	-	-	-
Distribution income	1.8	1.8	4.4	5.4	5.5
Total yield income	**7.4**	**4.7**	**4.4**	**5.4**	**5.5**
Offeror Fees	3.7	5.9	4.0	2.5	1.5
Underwriting fees	1.5	2.1	1.4	1.4	0.8
Total up-front deal fees	**5.2**	**8.0**	**5.4**	**3.9**	**2.3**
Base management fees	4.2	5.2	6.4	7.1	7.7
Transactional income	2.1	4.1	3.1	2.7	2.3
Total recurring fees	**6.3**	**9.3**	**9.4**	**9.9**	**10.0**
Total net rental income	**18.9**	**22.0**	**19.2**	**19.2**	**17.8**
New deal operating metrics					
New deals completed (assets)	351	180	272	170	100
New deals completed (equity raised)	126	255	129	102	60
Equity underwritten by AUG	47%	36%	36%	45%	45%
Syndicates wound-up (assets)	125	232	75	50	25
Funds under management					
Directly held properties	84	31	-	-	-
Syndications	1,416	1,532	1,699	1,849	1,956
Other properties	96	96	96	96	96
Value Add fund no.1	74	-	-	-	-
Asset Plus	180	133	190	190	190
Industrial Fund	-	-	-	-	-
Total FUM	**1,851**	**1,792**	**1,985**	**2,135**	**2,242**

* Forsyth Barr target prices reflect valuation rolled forward at cost of equity less the next 12-months dividend

Investment summary

Augusta Capital (AUG) is making good progress transitioning its business model from property investment to funds management. The key focus for AUG is getting its balance sheet utilised so it can replace the rental income lost from property sales. Recent periods have shown record activity levels, and growing earnings off this high base is challenging. AUG's funds management business makes it very different from the other listed property vehicles and gives it less capital intensive growth prospects, albeit at higher risk. In our property sector report *'Real Estate Reflections'* dated 5 September we adopted our new Research team risk free rate of 2% and market risk premium of 7.5% which increased the AUG target price by +7%. NEUTRAL.

Earnings and cash flow outlook

- **Funds management growth:** AUG is building its track record for executing on larger deals. Following the Industrial Fund and St George's Bay road deals, we expect AUG's FUM to grow to above NZ$2bn in FY20E. AUG is also looking to launch a tourism related fund in 3Q20E.
- **Asset Plus (APL) externalisation:** AUG purchased APL's management rights for NZ$4.5m, which has lifted its FUM +NZ$180m (NZ$125m after asset sales) and generated NZ$0.9m in recurring management fees. AUG is implementing a 'yield plus growth' strategy for APL.
- **Syndication pipeline:** While AUG has been successful in growing its recurring management fees it is still reliant on up-front deal fees.

Business quality

- **Focus solely on funds management:** AUG's last directly held asset has been sold. The sale has settled and provides substantial balance sheet capacity for warehousing, co-investment in new funds, and underwriting.

Financial structure

- **Balance sheet becoming more fluid:** AUG's funds management activities have resulted in a more unpredictable balance sheet. We assume gearing of ~15–20% over the medium-term, which is ~35–40% on a look-through basis incorporating the underlying gearing in AUG's co-investments.

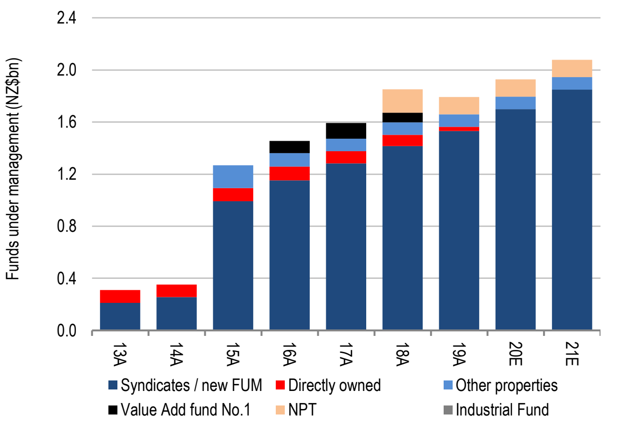
Risks factors

- **Acquiring new stock for investment products:** This is the largest challenge for AUG's funds management business given a highly competitive property market.
- **In syndication demand:** An economic slowdown, rising interest rates, or a decrease in investor sentiment are catalysts for this.

Company description

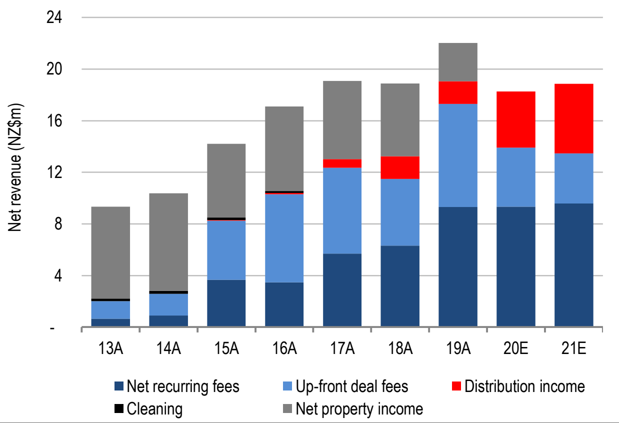
Augusta Capital Limited (AUG) was listed on the NZX in December 2006, as Kermadec Property Fund. In March 2012, it acquired the funds management businesses from Augusta Funds Management and internalised its management structure. In April 2014, AUG acquired KCL Property for $15m, which increased total property under management by ~$750m to ~$1.6bn. AUG has transitioned its business to focus solely on funds management.

Figure 1. Funds under management (NZ$bn)



Source: Forsyth Barr analysis, Company Reports

Figure 2. Net revenue by segment (NZ$m)



Source: Forsyth Barr analysis, Company reports

Figure 3. Substantial Shareholders

Shareholder	Latest Holding
Mark Edward Francis	16.7%
ANZ NZ Investments	13.0%
Kawaroa Trustees	5.7%
ACC	5.4%

Source: NZX, Forsyth Barr analysis, NOTE: based on SSH notices only

Figure 4. International Compcos

Company	Code	Price	Mkt Cap	PE		EV/EBITDA		EV/EBIT		Cash D/Yld
(metrics re-weighted to reflect AUG's balance date - March)			(m)	2020E	2021E	2020E	2021E	2020E	2021E	2021E
Augusta Capital	**AUG NZ**	**NZ$1.51**	**NZ$132**	**21.0x**	**21.1x**	**15.9x**	**16.1x**	**15.9x**	**16.1x**	**4.3%**
Pendal Group	PDL AT	A$6.71	A$2,166	12.4x	11.2x	9.7x	8.7x	10.0x	9.1x	7.6%
Charter Hall Group	CHC AT	A$12.79	A$5,957	22.1x	23.7x	23.7x	19.0x	24.7x	18.9x	3.1%
Cromwell Property Group	CMW AT	A$1.24	A$3,206	15.7x	15.4x	n/a	n/a	n/a	n/a	6.3%
Centuria Capital Group	CNI AT	A$2.15	A$825	17.2x	17.3x	18.3x	14.4x	18.4x	14.4x	4.6%
Goodman Group	GMG AT	A$14.18	A$25,927	22.5x	23.3x	30.8x	21.7x	31.0x	21.4x	2.2%
Magellan Financial Group	MFG AT	A$50.56	A$9,205	23.3x	21.7x	17.8x	16.6x	17.6x	16.2x	4.2%
Platinum Asset Management	PTM AT	A$3.80	A$2,229	14.2x	14.2x	9.7x	9.8x	9.7x	9.7x	7.0%
Stride Property *	SPG NZ	NZ$2.34	NZ$855	22.3x	21.1x	21.0x	19.1x	21.0x	19.1x	4.2%
360 Capital Group	TGP AT	A$1.11	A$256	>50x	n/a	n/a	n/a	n/a	n/a	n/a
			Compco Average:	**18.7x**	**18.5x**	**18.7x**	**15.6x**	**18.9x**	**15.5x**	**4.9%**
EV = Current Market Cap + Actual Net Debt			**AUG Relative:**	**+12%**	**+14%**	**-15%**	**+3%**	**-16%**	**+4%**	**-12%**

Source: *Forsyth Barr analysis, Bloomberg Consensus, Compco metrics re-weighted to reflect headline (AUG) companies fiscal year end

Figure 5. Consensus EPS Momentum

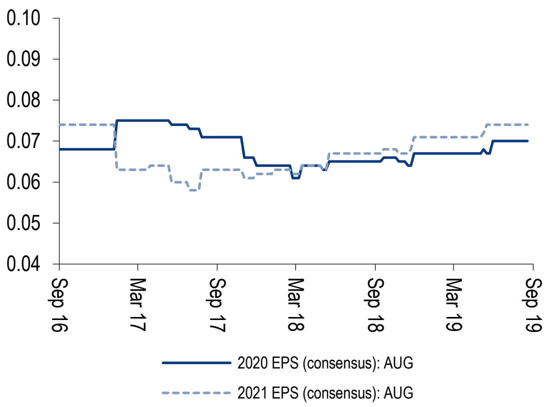


Figure 6. 12 Month Forward PE