

# Fletcher Building

## 1H21 Preview — If You Build It...

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### NEUTRAL

Fletcher Building (FBU) reports its 1H21 result on 17 February. On a like-for-like basis we expect a strong set of results underpinned by 1) resilient NZ residential activity, and 2) a material cost base reset. Notwithstanding extended lockdowns, continued strong NZ activity indicators may give management confidence to provide FY21 guidance and we see upside risks to our forecast and consensus (FY21E Forbar NZ\$593m, Bloomberg consensus NZ\$611m).

| NZX Code           | FBU                 | Financials: Jun/             | 20A   | 21E   | 22E   | 23E   | Valuation (x)     | 20A  | 21E  | 22E  | 23E  |
|--------------------|---------------------|------------------------------|-------|-------|-------|-------|-------------------|------|------|------|------|
| Share price        | NZ\$6.34            | NPAT* (NZ\$m)                | 3.0   | 357.8 | 307.8 | 327.0 | PE                | n/a  | 14.6 | 16.9 | 15.9 |
| Target price       | NZ\$5.85            | EPS* (NZc)                   | 0.4   | 43.6  | 37.5  | 39.8  | EV/EBIT           | 39.8 | 12.2 | 13.1 | 12.5 |
| Risk rating        | Medium              | EPS growth* (%)              | -99.2 | n/a   | -14.0 | 6.2   | EV/EBITDA         | 12.0 | 7.7  | 8.0  | 7.7  |
| Issued shares      | 821.2m              | DPS (NZc)                    | 0.0   | 15.0  | 27.0  | 29.0  | Price / NTA       | 2.2  | 2.0  | 1.9  | 1.9  |
| Market cap         | NZ\$5,207m          | Imputation (%)               | n/a   | 100   | 52    | 52    | Cash div yld (%)  | 0.0  | 2.4  | 4.3  | 4.6  |
| Avg daily turnover | 1,821k (NZ\$7,493k) | *Based on normalised profits |       |       |       |       | Gross div yld (%) | n/a  | 3.3  | 5.1  | 5.5  |

#### Key issues to watch for:

- **Strong 1H21:** Supported by cost out and strong NZ construction activity, we forecast like-for-like EBIT (excluding NZ\$90m of restructuring costs) to be +41% to NZ\$308m vs. guidance of NZ\$305–320m on:
  1. Strong NZ residential activity and cost out lifting the NZ core (ex. residential development and construction). With ready-mix concrete volumes +8% yoy in the December quarter we see upside risk to our expectations.
  2. Strong housing demand driving residential development sales volumes and strong house prices growth improving margins (but with some offset from the final sell-down of the lower margin Atlas Quarter development in Christchurch).
  3. Softer activity in Australia reflecting lower apartment and non-residential activity but more than offset by cost out.
- **Expecting full year guidance:** FBU did not provide FY21 guidance with its trading update in November with management cautious on continuation of activity into 2021. Notwithstanding extended lockdowns, strong NZ activity indicators (robust NZ housing demand, NZ residential approvals at record levels, and improving construction sector confidence and employment) may give management enough confidence to provide full year guidance (Forbar FY21E EBIT NZ\$593m).
- **But not a 1H dividend:** FBU has debt covenant relief to cover the lockdown impacted 4Q20 that is applied on a 12-month rolling basis. As such we do not expect FBU to pay a 1H21 dividend with a larger 2H distribution more likely.

#### Investor briefing

Conference call: 11.00am (NZ time), register at: <https://s1.c-conf.com/DiamondPass/10012153-js756q.html>

**Figure 1. FBU 1H21 forecasts**

| NZ\$m                | 1H20  | 1H21  | % chg  |
|----------------------|-------|-------|--------|
| Revenue              | 3,961 | 4,024 | +1.6%  |
| EBIT                 | 219   | 308   | +40.9% |
| Underlying profit    | 107   | 178   | +65.9% |
| Underlying EPS (cps) | 12.8  | 21.4  | +67.2% |
| Dividend (cps)       | 0.0   | 0.0   | n/m    |

Source: Company results, Forsyth Barr analysis

## Fletcher Building (FBU)

Priced as at 12 Feb 2021 (NZ\$) **6.34**

**12-month target price (NZ\$)\*** **5.85**

Expected share price return -7.7%

Net dividend yield 3.6%

Estimated 12-month return -4.1%

### Key WACC assumptions

Risk free rate 1.30%

Equity beta 1.31

WACC 7.5%

Terminal growth 2.0%

### Spot valuations (NZ\$)

1. DCF 5.93

### DCF valuation summary (NZ\$m)

Total firm value 8,371

(Net debt)/cash (325)

Less: Capitalised operating leases (3,179)

Value of equity 4,867

### Profit and Loss Account (NZ\$m)

|                               | 2019A        | 2020A          | 2021E        | 2022E        | 2023E        |
|-------------------------------|--------------|----------------|--------------|--------------|--------------|
| Sales revenue                 | 9,307.0      | 7,309.0        | 7,858.7      | 7,804.2      | 8,084.2      |
| <b>Normalised EBITDA</b>      | <b>830.0</b> | <b>530.0</b>   | <b>947.8</b> | <b>902.9</b> | <b>936.7</b> |
| Depreciation and amortisation | (199.0)      | (370.0)        | (354.6)      | (351.4)      | (360.1)      |
| <b>Normalised EBIT</b>        | <b>631.0</b> | <b>160.0</b>   | <b>593.2</b> | <b>551.5</b> | <b>576.6</b> |
| Net interest                  | (118.0)      | (149.0)        | (109.4)      | (105.1)      | (104.6)      |
| Associate income              | 0            | 0              | 0            | 0            | 0            |
| Tax                           | (133.0)      | 4.0            | (110.3)      | (125.0)      | (132.2)      |
| Minority interests            | 13.0         | 12.0           | 15.8         | 13.6         | 12.9         |
| <b>Normalised NPAT</b>        | <b>367.0</b> | <b>3.0</b>     | <b>357.8</b> | <b>307.8</b> | <b>327.0</b> |
| Abnormals/other               | (203.0)      | (199.0)        | (90.0)       | 0            | 0            |
| <b>Reported NPAT</b>          | <b>164.0</b> | <b>(196.0)</b> | <b>267.8</b> | <b>307.8</b> | <b>327.0</b> |
| Normalised EPS (cps)          | 43.1         | 0.4            | 43.6         | 37.5         | 39.8         |
| DPS (cps)                     | 23.0         | 0              | 15.0         | 27.0         | 29.0         |

### Growth Rates

|                     | 2019A | 2020A  | 2021E | 2022E | 2023E |
|---------------------|-------|--------|-------|-------|-------|
| Revenue (%)         | -1.7  | -21.5  | 7.5   | -0.7  | 3.6   |
| EBITDA (%)          | >100  | -36.1  | 78.8  | -4.7  | 3.7   |
| EBIT (%)            | >100  | -74.6  | >100  | -7.0  | 4.6   |
| Normalised NPAT (%) | n/a   | -99.2  | >100  | -14.0 | 6.2   |
| Normalised EPS (%)  | n/a   | -99.2  | >100  | -14.0 | 6.2   |
| Ordinary DPS (%)    | n/a   | -100.0 | n/a   | 80.0  | 7.4   |

### Cash Flow (NZ\$m)

|                                        | 2019A          | 2020A          | 2021E         | 2022E         | 2023E          |
|----------------------------------------|----------------|----------------|---------------|---------------|----------------|
| <b>EBITDA</b>                          | <b>830.0</b>   | <b>530.0</b>   | <b>947.8</b>  | <b>902.9</b>  | <b>936.7</b>   |
| Working capital change                 | (404.0)        | (58.0)         | (330.1)       | (63.5)        | (14.8)         |
| Interest & tax paid                    | (156.0)        | (215.0)        | (175.4)       | (168.3)       | (341.6)        |
| Other                                  | (117.0)        | 84.0           | (90.0)        | 0             | 0              |
| <b>Operating cash flow</b>             | <b>153.0</b>   | <b>341.0</b>   | <b>352.3</b>  | <b>671.1</b>  | <b>580.3</b>   |
| Capital expenditure                    | (348.0)        | (240.0)        | (200.0)       | (300.0)       | (425.0)        |
| (Acquisitions)/divestments             | 1,262.0        | 6.0            | 0             | 0             | 0              |
| Other                                  | 0              | (171.0)        | (163.7)       | (156.8)       | (150.1)        |
| <b>Funding available/(required)</b>    | <b>1,067.0</b> | <b>(64.0)</b>  | <b>(11.4)</b> | <b>214.3</b>  | <b>5.2</b>     |
| Dividends paid                         | (68.0)         | (128.0)        | 0             | (229.9)       | (229.9)        |
| Equity raised/(returned)               | (81.0)         | (147.0)        | 0             | 0             | 0              |
| <b>(Increase)/decrease in net debt</b> | <b>918.0</b>   | <b>(339.0)</b> | <b>(11.4)</b> | <b>(15.6)</b> | <b>(224.7)</b> |

### Balance Sheet (NZ\$m)

|                              | 2019A          | 2020A          | 2021E          | 2022E          | 2023E          |
|------------------------------|----------------|----------------|----------------|----------------|----------------|
| Working capital              | 1,384.0        | 1,158.0        | 1,315.1        | 1,292.5        | 1,309.3        |
| Fixed assets                 | 1,754.0        | 1,555.0        | 1,579.7        | 1,696.6        | 1,919.4        |
| Intangibles                  | 1,129.0        | 1,133.0        | 1,133.0        | 1,133.0        | 1,133.0        |
| Right of use asset           | 0              | 1,413.0        | 1,326.0        | 1,244.4        | 1,167.8        |
| Other assets                 | 817.0          | 1,317.0        | 1,206.7        | 1,081.7        | 1,126.0        |
| <b>Total funds employed</b>  | <b>5,084.0</b> | <b>6,576.0</b> | <b>6,560.5</b> | <b>6,448.2</b> | <b>6,655.5</b> |
| Net debt/(cash)              | 325.0          | 687.0          | 641.0          | 607.5          | 800.2          |
| Lease liability              | 0              | 1,549.0        | 1,477.6        | 1,407.4        | 1,338.7        |
| Other liabilities            | 586.0          | 633.0          | 460.0          | 374.0          | 376.0          |
| Shareholder's funds          | 4,141.0        | 3,500.0        | 3,774.9        | 3,852.3        | 3,933.7        |
| Minority interests           | 32.0           | 35.0           | 35.0           | 35.0           | 35.0           |
| <b>Total funding sources</b> | <b>5,084.0</b> | <b>6,404.0</b> | <b>6,388.5</b> | <b>6,276.2</b> | <b>6,483.5</b> |

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

### Valuation Ratios

|                          | 2019A | 2020A | 2021E | 2022E | 2023E |
|--------------------------|-------|-------|-------|-------|-------|
| EV/EBITDA (x)            | 7.1   | 12.0  | 7.7   | 8.0   | 7.7   |
| EV/EBIT (x)              | 9.3   | 39.8  | 12.2  | 13.1  | 12.5  |
| PE (x)                   | 14.7  | >100x | 14.6  | 16.9  | 15.9  |
| Price/NTA (x)            | 1.8   | 2.2   | 2.0   | 1.9   | 1.9   |
| Free cash flow yield (%) | -3.7  | 1.9   | 2.9   | 7.1   | 3.0   |
| Net dividend yield (%)   | 3.6   | 0.0   | 2.4   | 4.3   | 4.6   |
| Gross dividend yield (%) | 3.6   | n/a   | 3.3   | 5.1   | 5.5   |

### Capital Structure

|                           | 2019A | 2020A | 2021E | 2022E | 2023E |
|---------------------------|-------|-------|-------|-------|-------|
| Interest cover EBIT (x)   | 5.3   | 1.1   | 5.4   | 5.2   | 5.5   |
| Interest cover EBITDA (x) | 7.0   | 3.6   | 8.7   | 8.6   | 9.0   |
| Net debt/ND+E (%)         | 7.3   | 16.4  | 14.5  | 13.6  | 16.9  |
| Net debt/EBITDA (x)       | 0.4   | 1.3   | 0.7   | 0.7   | 0.9   |

### Key Ratios

|                              | 2019A | 2020A | 2021E | 2022E | 2023E |
|------------------------------|-------|-------|-------|-------|-------|
| Return on assets (%)         | 8.2   | 1.8   | 6.7   | 6.3   | 6.5   |
| Return on equity (%)         | 8.9   | 0.1   | 9.5   | 8.0   | 8.3   |
| Return on funds employed (%) | 8.8   | 6.2   | 10.0  | 8.2   | 8.3   |
| EBITDA margin (%)            | 8.9   | 7.3   | 12.1  | 11.6  | 11.6  |
| EBIT margin (%)              | 6.8   | 2.2   | 7.5   | 7.1   | 7.1   |
| Capex to sales (%)           | 3.7   | 3.3   | 2.5   | 3.8   | 5.3   |
| Capex to depreciation (%)    | 175   | 65    | 56    | 85    | 118   |
| Imputation (%)               | 0     | n/a   | 100   | 52    | 52    |
| Pay-out ratio (%)            | 53    | 0     | 34    | 72    | 73    |

### Operating Performance

#### External revenue (NZ\$m)

|                               | 2019A        | 2020A        | 2021E        | 2022E        | 2023E        |
|-------------------------------|--------------|--------------|--------------|--------------|--------------|
| New Zealand                   | 5,220        | 4,466        | 5,542        | 5,470        | 5,537        |
| Australia                     | 2,944        | 2,740        | 2,613        | 2,608        | 2,817        |
| Rest of World                 | 1,143        | 103          | (297)        | (275)        | (270)        |
| <b>Total external revenue</b> | <b>9,307</b> | <b>7,309</b> | <b>7,859</b> | <b>7,804</b> | <b>8,084</b> |

#### EBIT (NZ\$m)

|                               | 2019A      | 2020A      | 2021E      | 2022E      | 2023E      |
|-------------------------------|------------|------------|------------|------------|------------|
| Concrete                      | 84         | 74         | 110        | 99         | 93         |
| Building Products             | 160        | 87         | 170        | 157        | 147        |
| Distribution                  | 104        | 85         | 112        | 96         | 91         |
| Steel                         | 0          | 0          | 0          | 0          | 0          |
| Construction                  | 47         | (147)      | 32         | 53         | 59         |
| Residential / Land Developm't | 137        | 65         | 133        | 120        | 140        |
| Australia                     | 57         | 33         | 92         | 82         | 105        |
| Divested                      | 82         | 0          | 0          | 0          | 0          |
| Corporate / other             | (40)       | (37)       | (55)       | (56)       | (57)       |
| <b>Total EBIT</b>             | <b>631</b> | <b>160</b> | <b>593</b> | <b>551</b> | <b>577</b> |

#### EBIT (NZ\$m)

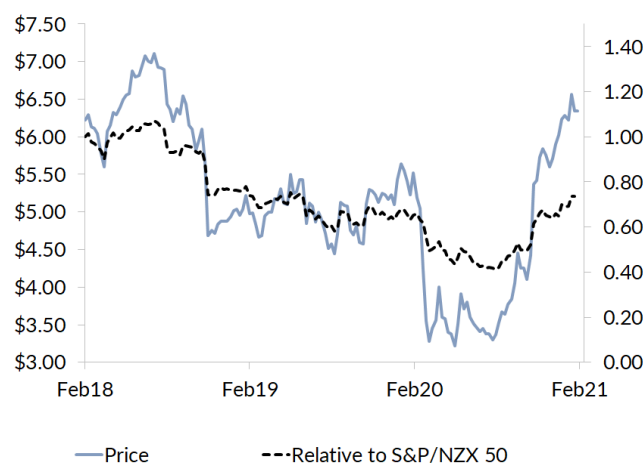
|                   | 2019A      | 2020A      | 2021E      | 2022E      | 2023E      |
|-------------------|------------|------------|------------|------------|------------|
| New Zealand       | 467        | 110        | 491        | 454        | 456        |
| Australia         | 54         | 42         | 85         | 75         | 98         |
| Rest of World     | 110        | 8          | 17         | 22         | 22         |
| <b>Total EBIT</b> | <b>631</b> | <b>160</b> | <b>593</b> | <b>551</b> | <b>577</b> |

## Earnings forecasts

Figure 2. 1H21E earnings forecasts

| NZ\$m                                  | 1H20         | 1H21         | % chg         |
|----------------------------------------|--------------|--------------|---------------|
| <b>Revenue</b>                         | <b>3,961</b> | <b>4,024</b> | <b>+1.6%</b>  |
| <b>EBIT</b>                            |              |              |               |
| Concrete                               | 49           | 61           | +24.2%        |
| Building Products                      | 65           | 71           | +8.7%         |
| Distribution                           | 50           | 59           | +18.9%        |
| Steel                                  | 1            | 14           | n/m           |
| Construction                           | 14           | 12           | -14.3%        |
| Residential and Land Development       | 35           | 72           | +104.8%       |
| Australia                              | 35           | 49           | +39.6%        |
| Other                                  | (30)         | (29)         | -3.3%         |
| <b>EBIT (before significant items)</b> | <b>219</b>   | <b>308</b>   | <b>+40.9%</b> |
| Significant items (before tax)         | (35)         | (90)         | +157.1%       |
| <b>EBIT</b>                            | <b>184</b>   | <b>218</b>   | <b>+18.7%</b> |
| Interest                               | (70)         | (55)         | -21.4%        |
| <b>Net profit before tax</b>           | <b>114</b>   | <b>163</b>   | <b>+43.4%</b> |
| Tax                                    | (28)         | (46)         | +63.5%        |
| <b>Net profit after tax</b>            | <b>86</b>    | <b>118</b>   | <b>+36.9%</b> |
| Minorities                             | (4)          | (5)          | +25.0%        |
| <b>Reported profit</b>                 | <b>82</b>    | <b>113</b>   | <b>+37.5%</b> |
| <b>Underlying profit</b>               | <b>107</b>   | <b>178</b>   | <b>+65.9%</b> |
| Underlying EPS (cps)                   | 12.8         | 21.4         | 67.2%         |
| Dividend (cps)                         | 0.0          | 0.0          | n/m           |
| <b>Geographical EBIT</b>               |              |              |               |
| New Zealand                            | 166          | 255          | +53.4%        |
| Australia                              | 44           | 49           | +11.1%        |
| Rest of world                          | 9            | 5            | -44.4%        |

Source: Company results, Forsyth Barr analysis

**Figure 3. Price performance**


Source: Forsyth Barr analysis

**Figure 4. Substantial shareholders**

| Shareholder                          | Latest Holding |
|--------------------------------------|----------------|
| Perpetual                            | 8.9%           |
| Schroder Investment Management Group | 7.4%           |
| Commonwealth Bank of Australia       | 6.0%           |
| The Vanguard Group                   | 5.6%           |

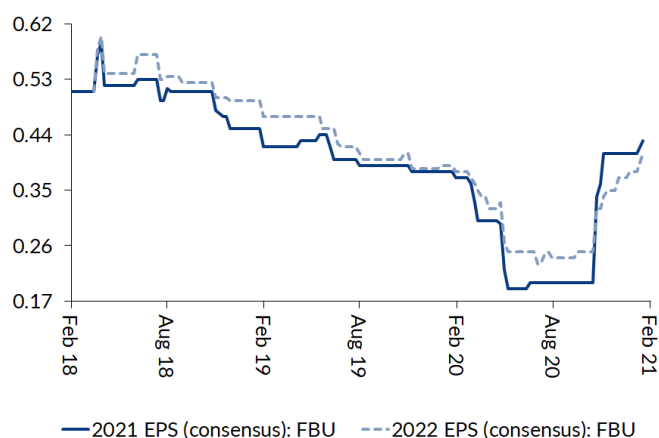
Source: NZX, Forsyth Barr analysis, NOTE: based on SPH notices only

**Figure 5. International valuation comparisons**

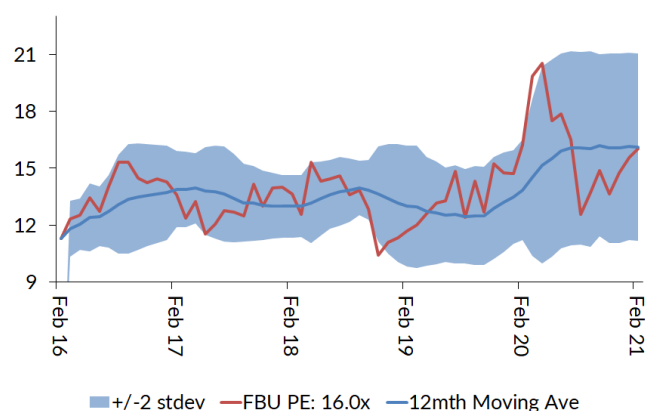
| Company                                                    | Code   | Price     | Mkt Cap (m) | PE 2021E | PE 2022E | EV/EBITDA 2021E | EV/EBITDA 2022E | EV/EBIT 2021E | EV/EBIT 2022E | Cash Yld 2022E |
|------------------------------------------------------------|--------|-----------|-------------|----------|----------|-----------------|-----------------|---------------|---------------|----------------|
| (metrics re-weighted to reflect FBU's balance date - June) |        |           |             |          |          |                 |                 |               |               |                |
| Fletcher Building                                          | FBU NZ | NZ\$6.34  | NZ\$5,207   | 14.6x    | 16.9x    | 6.2x            | 6.5x            | 9.9x          | 10.7x         | 4.3%           |
| METRO PERFORMANCE GLASS                                    | MPG NZ | NZ\$0.45  | NZ\$83      | 7.8x     | 9.4x     | 4.8x            | 5.5x            | 9.3x          | 11.1x         | 1.1%           |
| STEEL & TUBE HOLDINGS *                                    | STU NZ | NZ\$1.08  | NZ\$179     | 26.3x    | 23.9x    | 5.5x            | 5.6x            | 12.0x         | 11.7x         | 3.7%           |
| ADBRI                                                      | ABC AT | A\$3.09   | A\$2,016    | 19.3x    | 19.1x    | 9.7x            | 9.6x            | 15.9x         | 15.6x         | 3.5%           |
| BORAL                                                      | BLD AT | A\$5.06   | A\$6,202    | 24.3x    | 19.1x    | 9.1x            | 8.5x            | 19.2x         | 17.0x         | 3.1%           |
| CSR                                                        | CSR AT | A\$5.64   | A\$2,738    | 17.9x    | 18.7x    | 8.6x            | 8.9x            | 12.3x         | 13.1x         | 3.7%           |
| WAGNERS HOLDING CO                                         | WGN AT | A\$1.94   | A\$363      | n/a      | 32.9x    | 13.6x           | 12.4x           | 27.3x         | 23.2x         | 1.4%           |
| GWA GROUP                                                  | GWA AT | A\$3.71   | A\$980      | 23.8x    | 21.0x    | 15.1x           | 13.3x           | 18.8x         | 16.3x         | 3.6%           |
| JAMES HARDIE INDUSTRIES-CDI                                | JHX AT | US\$31.70 | US\$14,080  | 30.2x    | 25.6x    | 19.2x           | 17.0x           | 23.4x         | 20.6x         | 2.3%           |
| REECE                                                      | REH AT | A\$16.50  | A\$10,659   | 41.1x    | 36.9x    | 18.7x           | 18.2x           | 28.2x         | 27.2x         | 1.1%           |
| CRH PLC                                                    | CRH ID | €36.00    | €28,262     | 18.8x    | 16.5x    | 9.3x            | 8.8x            | 15.2x         | 13.8x         | 2.3%           |
| LAFARGEHOLCIM-REG                                          | LHN SW | CHF49.72  | CHF30,624   | 15.6x    | 13.4x    | 7.0x            | 6.5x            | 11.4x         | 10.2x         | 4.2%           |
| Compco Average:                                            |        |           |             | 22.5x    | 21.5x    | 11.0x           | 10.4x           | 17.6x         | 16.3x         | 2.7%           |
| FBU Relative:                                              |        |           |             | -35%     | -21%     | -43%            | -37%            | -43%          | -35%          | 57%            |

EV = Current Market Cap + Actual Net Debt

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

**Figure 6. Consensus EPS momentum (NZ\$)**


Source: Forsyth Barr analysis

**Figure 7. One year forward PE (x)**


Source: Forsyth Barr analysis

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|-------------------|----------------|---------------------|
| <b>44.2%</b>      | <b>38.5%</b>   | <b>17.3%</b>        |

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