

Fletcher Building

1H21 Result — Solid Foundations

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NEUTRAL

Fletcher Building (FBU) delivered a strong result, slightly ahead of guidance and our expectations. Underlying EBIT of NZ\$323m was up +47% yoy chiefly due to the benefits of recent cost-out initiatives. The main surprise of the result was the announcement of a 12cps interim dividend, facilitated by updated covenant agreements and underpinned by strong free cash flow. Buoyant construction activity supported volumes in FBU's NZ Core (building products, distribution, concrete) and while Australia was mixed cost out more than offset revenue declines. We maintain our NEUTRAL rating and lift our FY21E underlying EBIT +7% (to NZ\$638m) towards the middle of FBU's NZ\$610m–\$660m guidance range.

NZX Code	FBU	Financials: Jun/	20A	21E	22E	23E	Valuation (x)	20A	21E	22E	23E
Share price	NZ\$6.50	NPAT* (NZ\$m)	3.0	395.5	386.5	387.8	PE	n/a	13.5	13.8	13.8
Target price	NZ\$6.80	EPS* (NZc)	0.4	48.2	47.1	47.2	EV/EBIT	40.6	11.5	10.9	10.8
Risk rating	Medium	EPS growth* (%)	-99.2	n/a	-2.3	0.3	EV/EBITDA	12.3	7.4	7.1	7.0
Issued shares	821.2m	DPS (NZc)	0.0	34.0	34.0	34.0	Price / NTA	2.3	2.1	2.0	2.0
Market cap	NZ\$5,338m	Imputation (%)	n/a	65	53	53	Cash div yld (%)	0.0	5.2	5.2	5.2
Avg daily turnover	1,826k (NZ\$7,559k)	*Based on normalised profits					Gross div yld (%)	n/a	6.5	6.3	6.3

What's changed?

- **Earnings:** Underlying EBIT up +7.5%/+21.3%/+17.0% in FY21/FY22/FY23
- **Target price:** Lifted +95cps (+16%) to NZ\$6.80

Buoyant activity and cost-out underpin 1H21 performance

Performance within the NZ core was supported by strong residential activity, with revenue/EBIT growth of +5%/+35% driven by volume gains and cost-out initiatives. FBU's residential and development division settled 515 units in 1H21 but still expects c.800 sales for FY21 due to production constraints. Australia remains challenging given subdued multi-family and non-residential activity, although cost-out initiatives delivered EBIT margin improvement. Rocla and Iplex recognised respective impairments of NZ\$51m and NZ\$8m, with FBU reiterating its intention to divest Rocla. Legacy projects continue to weigh on FBU's construction division.

Net debt down, dividends resumed

FBU's balance sheet is in good shape. An unwind of inventory and lower capex supported strong free cash flow generation in 1H21. Net debt of NZ\$269m sees FBU's leverage ratio fall to 0.4x, below its 1.0x–2.0x target range. While this level of free cash flow will not be sustained given the requirements of an inventory rebuild (particularly in its building products, concrete, and residential divisions) and capex at its new wallboard plant, it does facilitate a return to dividend payments earlier than we expected with an interim distribution of 12cps (or c.NZ\$100m). Our medium term forecasts see leverage remain at the low end of FBU's target range.

Stronger-for-longer

Given the recent supportive levels of NZ residential consents (and a typical 4–6 month lag between consents and FBU product sales), management has confidence in sustained activity in 2H21 despite a slow start to the half. Medium term we have made larger revisions to our forecasts, reflecting stronger-for-longer NZ residential and a pick-up in activity across the Tasman supported by low interest rates. Our thinking on margins is broadly unchanged, benefits from prior cost out initiatives have never clearly materialised into earnings with savings consumed by inflation and/or margin pressures, and we expect FBU to give back some of its margin gains.

Fletcher Building (FBU)

Priced as at 17 Feb 2021 (NZ\$) **6.50**

12-month target price (NZ\$)* **6.80**

Expected share price return 4.6%

Net dividend yield 5.2%

Estimated 12-month return 9.8%

Key WACC assumptions

Risk free rate 2.30%

Equity beta 1.31

WACC 7.4%

Terminal growth 2.0%

Spot valuations (NZ\$)

1. DCF 6.50

DCF valuation summary (NZ\$m)

Total firm value 8,889

(Net debt)/cash (325)

Less: Capitalised operating leases (3,224)

Value of equity 5,341

Profit and Loss Account (NZ\$m)

	2019A	2020A	2021E	2022E	2023E
Sales revenue	9,307.0	7,309.0	7,846.3	8,114.5	8,344.7
Normalised EBITDA	830.0	530.0	992.3	1,028.1	1,043.7
Depreciation and amortisation	(199.0)	(370.0)	(354.6)	(359.1)	(369.3)
Normalised EBIT	631.0	160.0	637.7	668.9	674.4
Net interest	(118.0)	(149.0)	(109.9)	(108.5)	(113.3)
Associate income	0	0	0	0	0
Tax	(133.0)	4.0	(115.6)	(156.9)	(157.1)
Minority interests	13.0	12.0	16.7	17.0	16.2
Normalised NPAT	367.0	3.0	395.5	386.5	387.8
Abnormals/other	(203.0)	(199.0)	(115.0)	0	0
Reported NPAT	164.0	(196.0)	280.5	386.5	387.8
Normalised EPS (cps)	43.1	0.4	48.2	47.1	47.2
DPS (cps)	23.0	0	34.0	34.0	34.0

Growth Rates

	2019A	2020A	2021E	2022E	2023E
Revenue (%)	-1.7	-21.5	7.4	3.4	2.8
EBITDA (%)	>100	-36.1	87.2	3.6	1.5
EBIT (%)	>100	-74.6	>100	4.9	0.8
Normalised NPAT (%)	n/a	-99.2	>100	-2.3	0.3
Normalised EPS (%)	n/a	-99.2	>100	-2.3	0.3
Ordinary DPS (%)	n/a	-100.0	n/a	0.0	0.0

Cash Flow (NZ\$m)

	2019A	2020A	2021E	2022E	2023E
EBITDA	830.0	530.0	992.3	1,028.1	1,043.7
Working capital change	(404.0)	(58.0)	(201.1)	(200.9)	(34.2)
Interest & tax paid	(156.0)	(215.0)	(176.0)	(171.8)	(412.5)
Other	(117.0)	84.0	(95.0)	0	0
Operating cash flow	153.0	341.0	520.2	655.4	597.1
Capital expenditure	(348.0)	(240.0)	(200.0)	(445.0)	(325.0)
(Acquisitions)/divestments	1,262.0	6.0	0	0	0
Other	0	(171.0)	(163.7)	(156.8)	(150.1)
Funding available/(required)	1,067.0	(64.0)	156.5	53.5	122.0
Dividends paid	(68.0)	(128.0)	(98.5)	(312.1)	(279.2)
Equity raised/(returned)	(81.0)	(147.0)	0	0	0
(Increase)/decrease in net debt	918.0	(339.0)	58.0	(258.5)	(157.2)

Balance Sheet (NZ\$m)

	2019A	2020A	2021E	2022E	2023E
Working capital	1,384.0	1,158.0	1,186.1	1,300.9	1,337.1
Fixed assets	1,754.0	1,555.0	1,579.7	1,833.9	1,947.5
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	1,201.4	1,044.5	1,126.0
Total funds employed	5,084.0	6,576.0	6,426.2	6,556.7	6,711.4
Net debt/(cash)	325.0	687.0	572.5	785.2	913.7
Lease liability	0	1,549.0	1,477.6	1,407.4	1,338.7
Other liabilities	586.0	633.0	480.0	394.0	396.0
Shareholder's funds	4,141.0	3,500.0	3,689.1	3,763.1	3,856.0
Minority interests	32.0	35.0	35.0	35.0	35.0
Total funding sources	5,084.0	6,404.0	6,254.2	6,384.7	6,539.4

Valuation Ratios

	2019A	2020A	2021E	2022E	2023E
EV/EBITDA (x)	7.2	12.3	7.4	7.1	7.0
EV/EBIT (x)	9.5	40.6	11.5	10.9	10.8
PE (x)	15.1	>100x	13.5	13.8	13.8
Price/NTA (x)	1.8	2.3	2.1	2.0	2.0
Free cash flow yield (%)	-3.7	1.9	6.0	3.9	5.1
Net dividend yield (%)	3.5	0.0	5.2	5.2	5.2
Gross dividend yield (%)	3.5	n/a	6.5	6.3	6.3

Capital Structure

	2019A	2020A	2021E	2022E	2023E
Interest cover EBIT (x)	5.3	1.1	5.8	6.2	6.0
Interest cover EBITDA (x)	7.0	3.6	9.0	9.5	9.2
Net debt/ND+E (%)	7.3	16.4	13.4	17.3	19.2
Net debt/EBITDA (x)	0.4	1.3	0.6	0.8	0.9

Key Ratios

	2019A	2020A	2021E	2022E	2023E
Return on assets (%)	8.2	1.8	7.3	7.7	7.7
Return on equity (%)	8.9	0.1	10.7	10.3	10.1
Return on funds employed (%)	8.8	6.2	11.1	10.2	9.7
EBITDA margin (%)	8.9	7.3	12.6	12.7	12.5
EBIT margin (%)	6.8	2.2	8.1	8.2	8.1
Capex to sales (%)	3.7	3.3	2.5	5.5	3.9
Capex to depreciation (%)	175	65	56	124	88
Imputation (%)	0	n/a	65	53	53
Pay-out ratio (%)	53	0	71	72	72

Operating Performance

External revenue (NZ\$m)

	2019A	2020A	2021E	2022E	2023E
New Zealand	5,220	4,466	5,555	5,728	5,804
Australia	2,944	2,740	2,594	2,674	2,824
Rest of World	1,143	103	(303)	(288)	(283)
Total external revenue	9,307	7,309	7,846	8,114	8,345

EBIT (NZ\$m)

	2019A	2020A	2021E	2022E	2023E
Concrete	84	74	113	117	111
Building Products	160	87	199	199	189
Distribution	104	85	118	120	115
Steel	0	0	0	0	0
Construction	47	(147)	35	53	59
Residential / Land Developm't	137	65	135	136	156
Australia	57	33	93	98	103
Divested	82	0	0	0	0
Corporate / other	(40)	(37)	(55)	(56)	(57)
Total EBIT	631	160	638	669	674

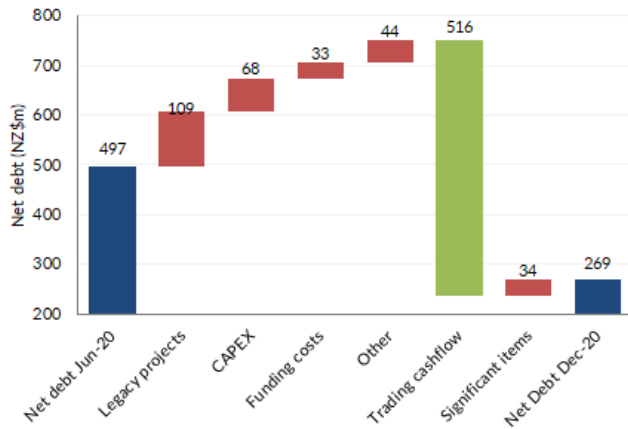
EBIT (NZ\$m)

	2019A	2020A	2021E	2022E	2023E
New Zealand	467	110	542	562	559
Australia	54	42	86	92	96
Rest of World	110	8	10	15	20
Total EBIT	631	160	638	669	674

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

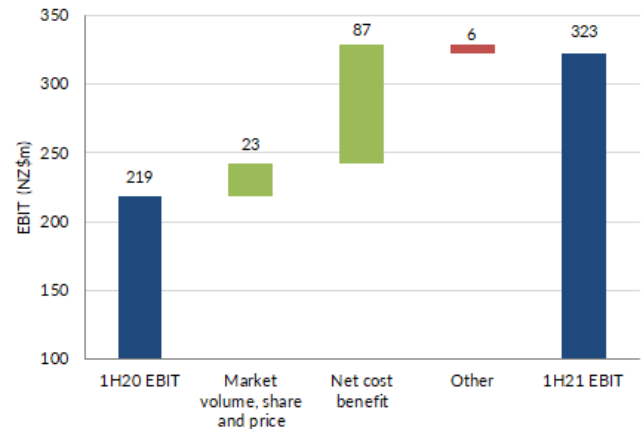
1H21 in charts

Figure 1. Net debt down as CAPEX falls and inventory unwinds



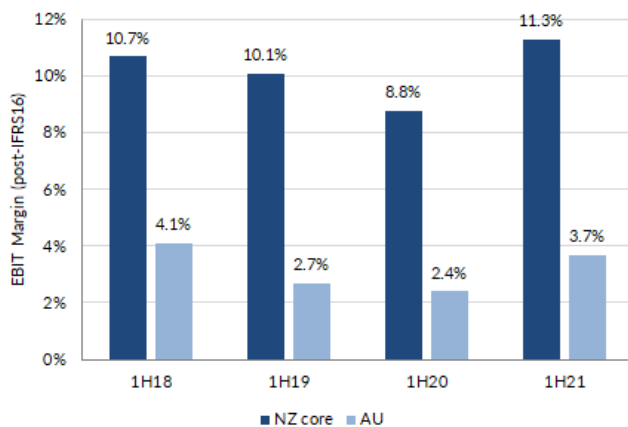
Source: Forsyth Barr analysis

Figure 2. EBIT uplift driven largely by cost out



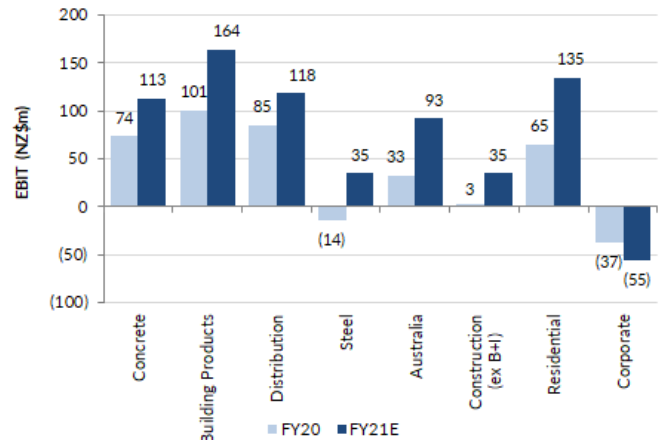
Source: Forsyth Barr analysis

Figure 3. Margin improvement in both NZ and AU



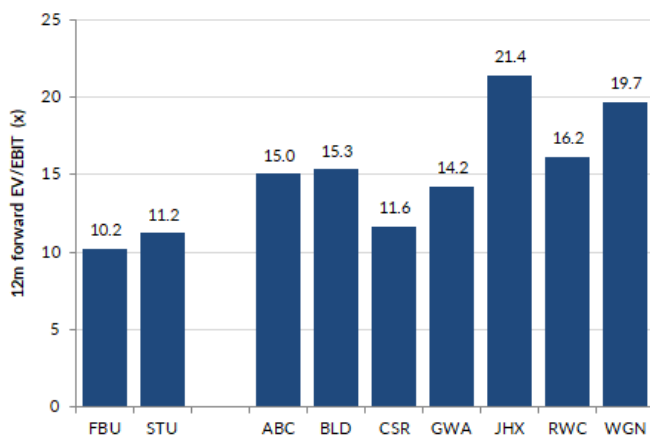
Source: Forsyth Barr analysis

Figure 4. EBIT by division (FY21E vs FY20)



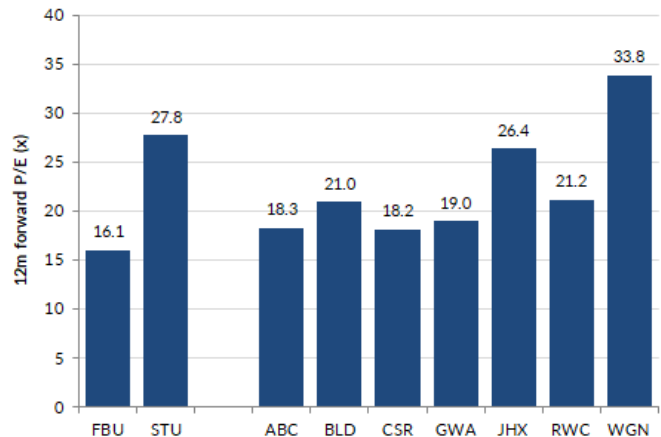
Source: Forsyth Barr analysis

Figure 5. FBU EV/EBIT vs peers



Source: Forsyth Barr analysis, Bloomberg (note: consensus)

Figure 6. FBU P/E vs peers



Source: Forsyth Barr analysis (note: consensus)

1H21 result summary and earnings revisions

Figure 7. 1H21 result summary

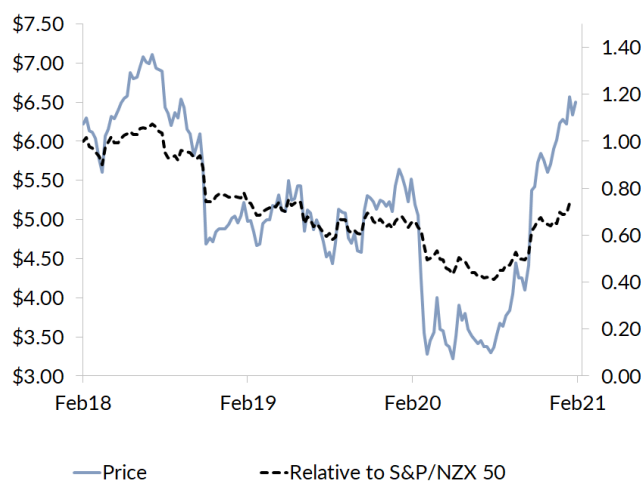
NZ\$m	1H20	1H21	% chg	Forbar	% diff	Comment
External revenue						
Concrete	273	291	6.6%	289	0.7%	Cement revs +17%. RMC volumes +6%, aggregates flat
Building Products (incl. Steel)	507	537	5.9%	526	2.0%	Finishing trades +11%, pipes and steel +3%
Distribution	805	838	4.1%	828	1.2%	Consumer weighted as commercial slowed
Construction	742	620	-16.4%	627	-1.1%	Working through legacy, NZ\$0.4bn remains
Residential and Land Development	224	351	56.7%	424	-17.3%	515 units sold (1H20: 293)
Australia	1,410	1,350	-4.3%	1,329	1.6%	Building products -10%, Pipes -25%, Dist. -3%, Steel +9%
Divested	0	0	n.a.	0	n.a.	
Total revenue	3,961	3,987	0.7%	4,024	-0.9%	
EBIT						
Concrete	49	62	26.5%	61	1.9%	Up +27% on share gains, efficiencies and improved pricing
Building Products	65	83	27.7%	71	17.5%	Pipes EBIT +67% from past restructuring
Distribution	50	60	20.0%	59	1.0%	Margin improved on cost-out despite competition
Steel	1	18	n/m	14	28.6%	Driven by price governance, mix, and labour/property cost reduction
Construction	14	13	-7.1%	12	8.3%	Underpinned by Higgins and Barry Perry Civil
Residential and Land Development	35	62	77.1%	72	-13.5%	Volume and price improvements in resi, LD down due to timing
Australia	35	51	45.7%	49	4.3%	Cost base reduction across the board. Laminex, Oliveri, and Steel benefitted from new products
Other	(30)	(26)	-13.3%	(29)	-10.3%	
EBIT (before significant items)	219	323	47.5%	308	4.7%	
Divestments	0	0	n.a.	0	n.a.	
Significant items (before tax)	(35)	(86)	145.7%	(90)	-4.4%	
EBIT	184	237	28.8%	218	8.5%	
Interest	(70)	(56)	-20.0%	(55)	1.8%	
Net profit before tax	114	181	58.8%	163	10.7%	
Tax	(28)	(57)	103.6%	(46)	24.5%	
Net profit after tax	86	124	44.2%	118	5.3%	
Minorities	(4)	(3)	-25.0%	(5)	-40.0%	
Reported profit	82	121	47.6%	113	7.4%	
Underlying profit	107	195	82.2%	178	9.9%	
Underlying EPS (cps)	12.8	23.7	85.7%	21.4	11.0%	
Dividend (cps)	0.0	12.0	n/m	0.0	n/m	

Source: Forsyth Barr analysis, Company reports

Figure 8. Forecast changes

NZ\$m	FY21E		% chg	FY22E		% chg	FY23E		% chg
	Old	New		Old	New		Old	New	
Revenue	7,859	7,846	-0.2%	7,804	8,114	4.0%	8,084	8,345	3.2%
EBITDA	948	992	4.7%	903	1,028	13.9%	937	1,044	11.4%
EBIT	593	638	7.5%	551	669	21.3%	577	674	17.0%
Underlying NPAT	358	396	10.6%	308	387	25.6%	327	388	18.6%
Underlying EPS (cps)	43.6	48.2	10.6%	37.5	47.1	25.6%	39.8	47.2	18.6%
Dividend (cps)	15.0	34.0	126.7%	27.0	34.0	25.9%	29.0	34.0	17.2%

Source: Forsyth Barr analysis

Figure 9. Price performance


Source: Forsyth Barr analysis

Figure 10. 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%

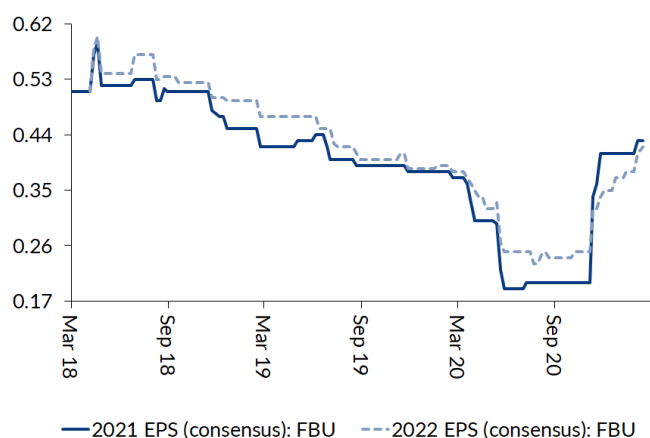
Source: NZX, Forsyth Barr analysis, NOTE: based on SPH notices only

Figure 11. International valuation comparisons

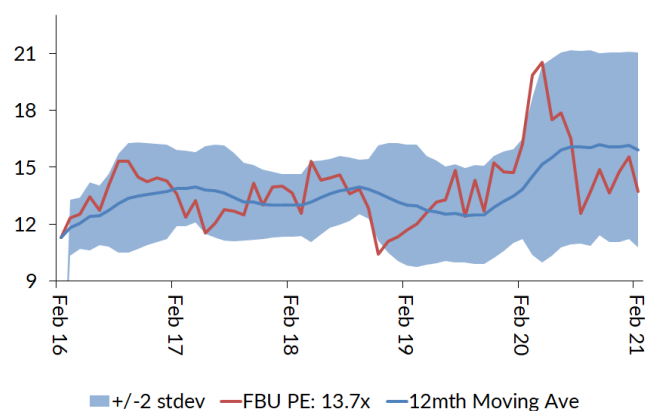
Company	Code	Price	Mkt Cap (m)	PE 2021E 2022E	EV/EBITDA 2021E 2022E	EV/EBIT 2021E 2022E	Cash Yld 2022E
(metrics re-weighted to reflect FBU's balance date - June)							
Fletcher Building	FBU NZ	NZ\$6.50	NZ\$5,338	13.5x 13.8x	6.1x 5.9x	9.4x 9.0x	5.2%
METRO PERFORMANCE GLASS	MPG NZ	NZ\$0.44	NZ\$81	7.6x 9.1x	4.7x 5.4x	9.2x 10.9x	1.1%
STEEL & TUBE HOLDINGS *	STU NZ	NZ\$1.04	NZ\$173	25.3x 23.0x	5.3x 5.4x	11.6x 11.3x	3.8%
ADBRI	ABC AT	A\$2.98	A\$1,944	18.7x 18.6x	9.6x 9.4x	15.4x 15.2x	3.6%
BORAL	BLD AT	A\$5.06	A\$6,202	23.5x 19.2x	9.1x 8.4x	19.0x 16.9x	3.0%
CSR	CSR AT	A\$5.43	A\$2,636	17.2x 18.0x	8.3x 8.6x	11.9x 12.6x	3.8%
WAGNERS HOLDING CO	WGN AT	A\$1.79	A\$335	n/a 30.3x	12.9x 11.7x	25.8x 22.0x	1.6%
GWA GROUP	GWA AT	A\$3.41	A\$901	22.1x 18.7x	13.6x 11.9x	17.0x 14.5x	3.9%
JAMES HARDIE INDUSTRIES-CDI	JHX AT	US\$32.12	US\$14,267	30.1x 25.8x	19.3x 17.2x	23.7x 20.9x	2.3%
REECE	REH AT	A\$16.43	A\$10,614	41.0x 36.8x	18.6x 18.1x	28.1x 27.1x	1.1%
CRH PLC	CRH ID	€37.13	€29,150	19.4x 16.9x	9.6x 9.1x	15.6x 14.2x	2.2%
LAFARGEHOLCIM-REG	LHN SW	CHF50.58	CHF31,154	15.8x 13.6x	7.0x 6.6x	11.6x 10.3x	4.1%
Compco Average:				22.1x 20.9x	10.7x 10.2x	17.2x 16.0x	2.8%
FBU Relative:				-39% -34%	-43% -42%	-45% -44%	89%

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 12. Consensus EPS momentum (NZ\$)


Source: Forsyth Barr analysis

Figure 13. One year forward PE (x)


Source: Forsyth Barr analysis

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