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Kathmandu Holdings
FY20 Preview — Wave Watching

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OUTPERFORM

Kathmandu Holdings (KMD) reports its FY20 result on Wednesday, 23 September 2020, — KMD has likely benefited from favourable category trends and pent up consumer activity during its key sales period; we reiterate our OUTPERFORM. With reasonable insight into FY20 trading, KMD has guided to FY20 Underlying EBITDA in excess of NZ$70m (Forsyth Barr NZ$71m), we expect focus to be on outlook comments and look for 1) its experience in Victoria amid a second COVID-19 wave, 2) margins and success of cost-out initiatives, and 3) an update on Rip Curl and its integration into the group.

NZX Code	KMD
Share price	NZ$1.19
Target price	NZ$1.50
Risk rating	High
Issued shares	649.2m
Market cap	NZ$773m
Avg daily turnover	1,657k (NZ$1,964k)

Financials: Jul/	19A	20E	21E	22E
NPAT* (NZ$m)	56.8	36.4	40.4	71.4
EPS* (NZc)	17.6	5.6	6.2	11.0
EPS growth* (%)	4.8	-68.0	11.0	76.6
DPS (NZc)	16.0	0.0	3.0	7.0
Imputation (%)	100	100	100	100
*Based on normalised profits				

Valuation (x)	19A	20E	21E	22E
PE	6.8	21.2	19.1	10.8
EV/EBIT	9.5	17.5	13.0	7.8
EV/EBITDA	8.0	11.5	9.1	6.1
Price / NTA	6.9	5.3	4.6	4.0
Cash div yld (%)	13.4	0.0	2.5	5.9
Gross div yld (%)	18.7	0.0	3.5	8.2

Key areas of interest

- **Rip Curl —** With a nine month contribution in the current period, Rip Curl remains fairly new to investors. An update on group integration, wholesale channel experience, and order book will be of interest.
- **Online and Melbourne experience —** Online sales surged amid COVID-19 disruption, and online sales penetration remained elevated through lower Alert Levels. Over the six weeks to 28 June, online sales represented >20% of direct to consumer sales (~10% penetration pre COVID-19). KMD has since partnered with Uber to offer same-day delivery, launching in Melbourne first, with experience and roll out plans of interest.
- **Margin implications —** The company signalled it expects FY20 gross margin to be at the bottom end of its target 61% to 63% range, as inventory control and strong sales activity have reduced the need to participate in elevated discounting activity. Foreign exchange headwinds may weigh on margin into FY21. We look for colour on any further margin impact from new initiatives.
- **Recent trading —** We suspect KMD has been a beneficiary of timing (relative to other retailers) with a post-lockdown spending surge coinciding with its key winter sales period. Category spend data suggests outdoor retailers should be outperforming general retail. Fluid social distancing restrictions in key markets create a level of uncertainty, albeit first quarter represents a seasonally weak period for KMD.
- **Expansion strategy —** KMD is targeting international expansion of its Kathmandu brand through the wholesale channel. We suspect COVID-19 has likely slowed progress, growth ambitions/priorities from here would be of interest.

Conference call 10:30am NZT 23 September; Dial in details 0800 453 055 (Australia 1800 558 698), conference ID 10009441.

Figure 1. FY20 result expectations (NZ$m)

	FY19	FY20E	% chg	Consensus
Revenue	545.6	737.2	35%	735.9
EBITDA	**99.6**	**71.1**	**-29%**	**71.5**
NPAT	56.8	36.4	-36%	29.1
EPS (cps)	17.6	5.6	-68%	6.7
DPS (cps)	12.0	-	-100%	1.0

Source: Bloomberg, Forsyth Barr analysis

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Kathmandu (KMD)

Priced as at 15 Sep 2020 (NZ$)	**1.19**

12-month target price (NZ$)*	**1.50**
Expected share price return	26.1%
Net dividend yield	3.1%
Estimated 12-month return	29.1%

Key WACC assumptions	
Risk free rate	2.00%
Equity beta	1.16
WACC	10.4%
Terminal growth	1.5%

Profit and Loss Account (NZ$m)	**2018A**	**2019A**	**2020E**	**2021E**	**2022E**
Sales revenue	497.4	545.6	737.2	921.5	989.6
Normalised EBITDA	**89.8**	**99.6**	**71.1**	**93.3**	**138.5**
Depreciation and amortisation	(15.0)	(15.3)	(24.3)	(28.4)	(29.5)
Normalised EBIT	**74.8**	**84.3**	**46.8**	**64.9**	**108.9**
Net interest	(1.1)	(2.9)	(4.3)	(6.7)	(6.2)
Associate income	0	0	0	0	0
Tax	(23.1)	(23.7)	(6.1)	(17.7)	(31.3)
Minority interests	0	0	0	0	0
Normalised NPAT	**50.7**	**56.8**	**36.4**	**40.4**	**71.4**
Abnormals/other	0	0.8	0	0	0
Reported NPAT	**50.7**	**57.6**	**36.4**	**40.4**	**71.4**
Normalised EPS (cps)	16.7	17.6	5.6	6.2	11.0
DPS (cps)	15.0	16.0	0	3.0	7.0

Growth Rates	**2018A**	**2019A**	**2020E**	**2021E**	**2022E**
Revenue (%)	11.7	9.7	35.1	25.0	7.4
EBITDA (%)	26.7	10.9	-28.6	31.3	48.4
EBIT (%)	31.2	12.7	-44.5	38.6	67.9
Normalised NPAT (%)	33.2	12.2	-35.9	11.0	76.6
Normalised EPS (%)	28.4	4.8	-68.0	11.0	76.6
Ordinary DPS (%)	15.4	6.7	-100.0	n/a	>100

Cash Flow (NZ$m)	**2018A**	**2019A**	**2020E**	**2021E**	**2022E**
EBITDA	**89.8**	**99.6**	**71.1**	**93.3**	**138.5**
Working capital change	6.4	(8.8)	29.4	(10.5)	(0.3)
Interest & tax paid	(20.6)	(29.1)	(10.4)	(24.4)	(37.5)
Other	0	0	0	0	0
Operating cash flow	**75.6**	**61.7**	**90.0**	**58.4**	**100.6**
Capital expenditure	(16.7)	(15.7)	(24.3)	(28.4)	(33.7)
(Acquisitions)/divestments	(82.7)	(22.3)	(368.0)	0	0
Other	(22.2)	22.3	7.0	0	0
Funding available/(required)	**(46.0)**	**46.0**	**(295.2)**	**29.9**	**66.9**
Dividends paid	(27.2)	(33.9)	0	(19.5)	(45.4)
Equity raised/(returned)	48.7	0	384.0	0	0
(Increase)/decrease in net debt	**(24.5)**	**12.1**	**88.8**	**10.4**	**21.5**

Balance Sheet (NZ$m)	**2018A**	**2019A**	**2020E**	**2021E**	**2022E**
Working capital	52.6	62.4	161.4	171.9	172.2
Fixed assets	63.5	60.3	106.7	106.7	110.8
Intangibles	390.3	386.1	595.8	595.8	595.8
Right of use asset	0	0	0	0	0
Other assets	27.3	5.0	31.5	31.5	31.5
Total funds employed	**533.7**	**513.8**	**895.2**	**905.8**	**910.2**
Net debt/(cash)	31.4	19.3	73.0	62.6	41.1
Lease liability	0	0	0	0	0
Other liabilities	82.0	52.4	80.2	80.2	80.2
Shareholder's funds	420.4	442.1	742.0	763.0	788.9
Minority interests	0	0	0	0	0
Total funding sources	**533.7**	**513.8**	**895.2**	**905.8**	**910.2**

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

Spot valuations (NZ$)	
1. DCF	1.44
2. Sum of the parts	1.30
3. n/a	n/a

DCF valuation summary (NZ$m)	
Total firm value	1,009
(Net debt)/cash	(73)
Less: Capitalised operating leases	
Value of equity	936

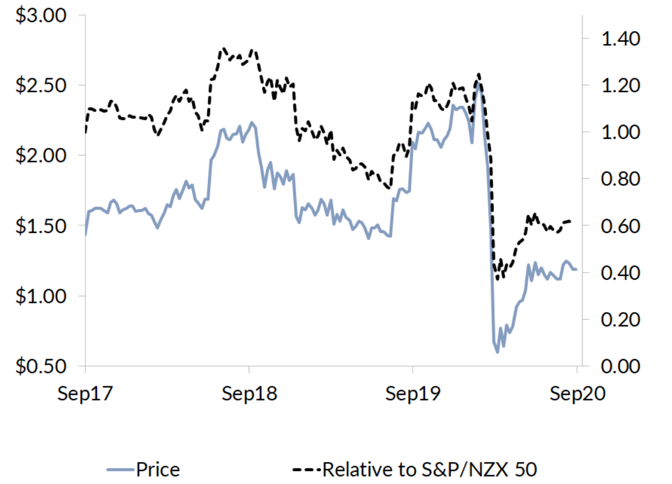
Valuation Ratios	**2018A**	**2019A**	**2020E**	**2021E**	**2022E**
EV/EBITDA (x)	8.8	8.0	11.5	9.1	6.1
EV/EBIT (x)	10.6	9.5	17.5	13.0	7.8
PE (x)	7.1	6.8	21.2	19.1	10.8
Price/NTA (x)	12.0	6.9	5.3	4.6	4.0
Free cash flow yield (%)	7.6	6.0	8.5	3.9	8.7
Net dividend yield (%)	12.6	13.4	0.0	2.5	5.9
Gross dividend yield (%)	17.5	18.7	0.0	3.5	8.2

Capital Structure	**2018A**	**2019A**	**2020E**	**2021E**	**2022E**
Interest cover EBIT (x)	70.6	28.9	11.0	9.7	17.6
Interest cover EBITDA (x)	84.8	34.2	16.7	14.0	22.3
Net debt/ND+E (%)	6.9	4.2	9.0	7.6	4.9
Net debt/EBITDA (x)	0.3	0.2	1.0	0.7	0.3

Key Ratios	**2018A**	**2019A**	**2020E**	**2021E**	**2022E**
Return on assets (%)	12.2	14.2	4.0	5.4	9.0
Return on equity (%)	12.1	13.0	4.9	5.3	9.0
Return on funds employed (%)	13.3	12.9	5.1	5.5	9.2
EBITDA margin (%)	18.0	18.2	9.6	10.1	14.0
EBIT margin (%)	15.0	15.4	6.3	7.0	11.0
Capex to sales (%)	3.4	2.9	3.3	3.1	3.4
Capex to depreciation (%)	112	103	100	100	114
Imputation (%)	100	100	100	100	100
Pay-out ratio (%)	90	91	0	48	64

Operating Performance	**2018A**	**2019A**	**2020E**	**2021E**	**2022E**
Divisional sales (NZ$m)					
New Zealand	143.0	138.6	122.6	128.8	137.9
Australia	333.7	338.7	301.0	308.7	331.8
International (incl Oboz)	20.8	68.3	57.6	61.7	67.8
Rip Curl	0	0	256.0	422.4	452.0
Total store sales	**497.4**	**545.6**	**737.2**	**921.5**	**989.6**
Group gross margin	**63%**	**61%**	**57%**	**57%**	**59%**
Divisional EBITDA (NZ$m)					
New Zealand	35.2	33.9	28.4	26.6	33.5
Australia	57.7	59.5	41.5	42.8	58.7
International (incl Oboz)	1.9	9.1	6.6	8.7	10.0
Rip Curl	0	0	(2.2)	18.6	39.7
Unallocated	(5.0)	(3.0)	(3.3)	(3.4)	(3.6)
Total EBITDA	**89.8**	**99.6**	**71.1**	**93.3**	**138.5**
Divisional EBITDA margin					
New Zealand	25%	24%	23%	21%	24%
Australia	17%	18%	14%	14%	18%
International (incl Oboz)	9%	13%	11%	14%	15%
Rip Curl	n/a	n/a	-1%	4%	9%
Total store sales	**18%**	**18%**	**10%**	**10%**	**14%**

Figure 2. Price performance



Source: Forsyth Barr analysis

Figure 3. Substantial shareholders

Shareholder	Latest Holding
TA Universal	10.2%
Harbour Asset Management & Jarden Securities Limited	8.1%
Briscoe Group	6.8%
ACC	5.2%

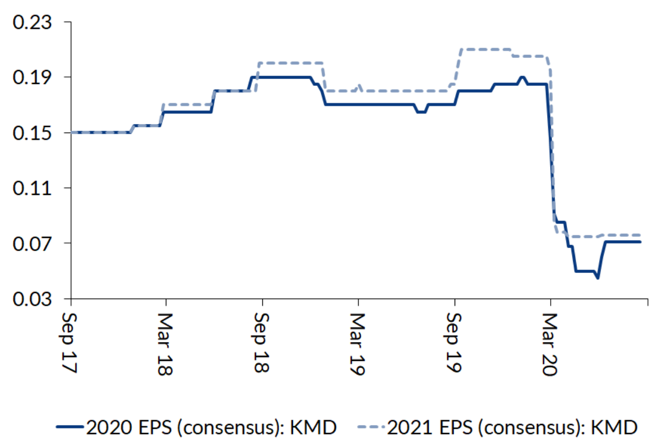
Source: NZX, Forsyth Barr analysis, NOTE: based on SPH notices only

Figure 4. International valuation comparisons

Company	Code	Price	Mkt Cap	PE		EV/EBITDA		EV/EBIT		Cash Yld
(metrics re-weighted to reflect KMD's balance date - July)			(m)	2020E	2021E	2020E	2021E	2020E	2021E	2021E
Kathmandu Holdings	**KMD NZ**	**NZ$1.19**	**NZ$773**	**21.2x**	**19.1x**	**11.1x**	**8.5x**	**16.9x**	**12.2x**	**2.5%**
SUPER RETAIL GROUP	SUL AT	A$10.59	A$2,391	18.6x	14.1x	6.6x	6.3x	15.2x	11.6x	4.5%
VF CORP	VFC US	US$73.21	US$28,526	>50x	>50x	22.0x	29.0x	42.2x	46.4x	2.7%
COLUMBIA SPORTSWEAR CO	COLM US	US$90.99	US$6,019	35.2x	32.7x	16.5x	16.4x	27.3x	25.5x	0.9%
DICK'S SPORTING GOODS INC	DKS US	US$57.30	US$5,106	15.6x	13.8x	8.5x	10.3x	19.0x	15.5x	2.2%
PREMIER INVESTMENTS	PMV AT	A$19.00	A$3,016	22.6x	22.3x	12.0x	12.1x	18.5x	19.2x	3.5%
MICHAEL HILL INTL *	MHJ NZ	A$0.45	A$175	<0x	7.7x	2.3x	1.9x	11.1x	4.5x	6.2%
BRISCOE GROUP *	BGP NZ	NZ$4.20	NZ$934	14.6x	15.2x	7.5x	7.0x	8.7x	8.9x	5.1%
THE WAREHOUSE GROUP *	WHS NZ	NZ$2.05	NZ$711	9.6x	20.3x	4.7x	6.9x	7.1x	14.2x	2.9%
			Compco Average:	**19.4x**	**18.0x**	**10.0x**	**11.2x**	**18.6x**	**18.2x**	**3.5%**
EV = Current Market Cap + Actual Net Debt			**KMD Relative:**	**10%**	**6%**	**11%**	**-24%**	**-9%**	**-33%**	**-28%**

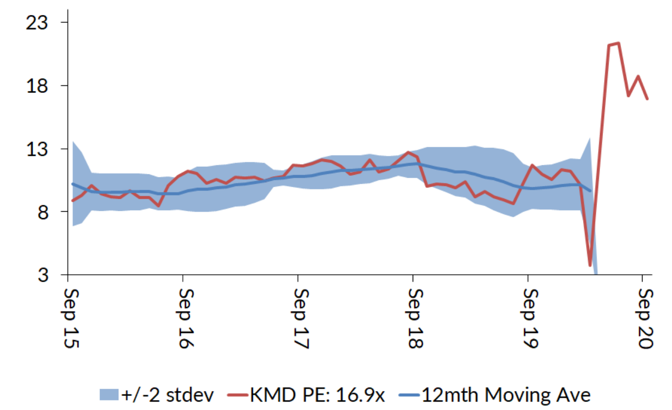
Source: *Forsyth Barr analysis, Bloomberg Consensus, Compco metrics re-weighted to reflect headline (KMD) companies fiscal year end

Figure 5. Consensus EPS momentum (NZ$)



Source: Forsyth Barr analysis

Figure 6. One year forward PE (x)



Source: Forsyth Barr analysis

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