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Mainfreight
Q3 Peer Read-through — Blue Skies

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OUTPERFORM

Third quarter results from Mainfreight's (MFT) key global peers show a strong industry rebound following a COVID-19 impacted 2Q20. MFT is due to report its 1H21 result on 11 November 2020, albeit it has already pre-released its estimated revenue (+7% against the prior year) and profit before tax (PBT, +23%) for the period. The company's best-in-class characteristics helped it avoid the revenue decline experienced by the wider industry over the period, and highlights the strong organic growth profile of the business. MFT is trading at a one year forward PE of ~27x, a discount to its closest but significantly larger peers Old Dominion Freight Line (ODFL.O) and DSV Panalpina (DSV.CO). We retain an OUTPERFORM rating.

NZX Code	MFT
Share price	NZ$55.25
Target price	NZ$60.00
Risk rating	Medium
Issued shares	100.7m
Market cap	NZ$5,564m
Avg daily turnover	77.9k (NZ$3,052k)

Financials: Mar/	20A	21E	22E	23E
NPAT* (NZ$m)	148.0	178.6	210.4	233.8
EPS* (NZc)	146.9	177.4	208.9	232.1
EPS growth* (%)	4.9	20.7	17.8	11.1
DPS (NZc)	59.0	70.0	83.6	92.9
Imputation (%)	100	100	100	100
*Based on normalised profits				

Valuation (x)	20A	21E	22E	23E
PE	37.6	31.1	26.4	23.8
EV/EBIT	16.7	20.7	17.7	16.1
EV/EBITDA	14.3	12.7	11.3	10.4
Price / NTA	8.2	7.1	5.5	4.4
Cash div yld (%)	1.1	1.3	1.5	1.7
Gross div yld (%)	1.5	1.8	2.1	2.3

Global peer 3Q20 highlights:

- **Revenue growth returns**: MFT's global peers reported an average revenue increase of +2% against the same quarter in 2019, driven largely by airfreight increases and decelerating rate of revenue decline across seafreight and less-than-truckload (LTL)
- **Airfreight margins continue to grow**: Airfreight rates have experienced another quarter of growth, as supply remains tight due to the reduction in passenger aircraft belly space

Industry rebound

MFT's key global peers have experienced a strong rebound in revenue growth in 3Q20, following the material reduction in freight demand in 2Q20 that came as a result of government restrictions imposed globally. Airfreight experienced another quarter of strong revenue and margin growth, as supply chains remain congested and demand remains elevated for high-yielding, time-sensitive services. LTL revenue growth was flat on the prior year following a large hit in 2Q20, and EBITDA margins improved across all industry segments for MFT's listed peers.

1H21 result on 11 November

Mainfreight (MFT) pre-released its estimated 1H21 result at its recent investor day, reporting revenue and PBT year on year growth of +7% and +23% respectively. There could be some minor variations in the actual results given the estimated nature of September performance based on 'weekly' accounts by branch. MFT has weathered the COVID-19 storm exceedingly well, accelerating market share gains and benefiting from new supply chain outsourcing opportunities.

Implications for MFT

MFT's geographic and business mix exposures are different than that of its key global peers, however, it is influenced by many of the same broader macro factors. We, therefore, believe that the financial performance of its peers provides a useful benchmark for analysing its performance. MFT's strong 1H21 is a further example of its strong growth characteristics.

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Mainfreight Ltd (MFT)

Priced as at 09 Nov 2020 (NZ$)	55.25

12-month target price (NZ$)*	60.00
Expected share price return	8.6%
Net dividend yield	1.4%
Estimated 12-month return	10.0%

Key WACC assumptions	
Risk free rate	1.30%
Equity beta	0.94
WACC	6.3%
Terminal growth	1.0%

Profit and Loss Account (NZ$m)	2019A	2020A	2021E	2022E	2023E
Sales revenue	2,954.1	3,095.4	3,320.8	3,632.1	3,900.1
Normalised EBITDA	**257.0**	**398.7**	**447.7**	**497.3**	**542.0**
Depreciation and amortisation	(53.1)	(57.9)	(174.3)	(179.5)	(191.6)
Normalised EBIT	**203.9**	**340.8**	**273.5**	**317.8**	**350.3**
Net interest	(6.9)	(5.7)	(22.0)	(17.9)	(17.4)
Associate income	0	0	0	0	0
Tax	(53.0)	(26.3)	(71.2)	(83.9)	(93.2)
Minority interests	0	0	0	0	0
Normalised NPAT	**141.1**	**148.0**	**178.6**	**210.4**	**233.8**
Abnormals/other	3.5	(11.2)	0	0	0
Reported NPAT	**137.6**	**159.2**	**178.6**	**210.4**	**233.8**
Normalised EPS (cps)	140.1	146.9	177.4	208.9	232.1
DPS (cps)	56.0	59.0	70.0	83.6	92.9

Growth Rates	2019A	2020A	2021E	2022E	2023E
Revenue (%)	12.8	4.8	7.3	9.4	7.4
EBITDA (%)	19.3	55.1	12.3	11.1	9.0
EBIT (%)	21.7	67.1	-19.8	16.2	10.2
Normalised NPAT (%)	25.7	4.9	20.7	17.8	11.1
Normalised EPS (%)	25.7	4.9	20.7	17.8	11.1
Ordinary DPS (%)	24.4	5.4	18.6	19.4	11.1

Cash Flow (NZ$m)	2019A	2020A	2021E	2022E	2023E
EBITDA	**257.0**	**398.7**	**447.7**	**497.3**	**542.0**
Working capital change	0	15.0	17.3	18.2	19.1
Interest & tax paid	(61.4)	(65.0)	(93.2)	(101.7)	(110.6)
Other	1.7	(47.9)	(24.3)	(25.2)	(26.1)
Operating cash flow	**197.4**	**300.8**	**347.5**	**388.6**	**424.3**
Capital expenditure	(103.3)	(160.0)	(80.0)	(165.0)	(165.0)
(Acquisitions)/divestments	14.0	5.0	5.0	5.0	5.0
Other	0.1	(101.6)	(105.7)	(111.0)	(116.5)
Funding available/(required)	**108.3**	**44.1**	**166.9**	**117.6**	**147.8**
Dividends paid	(48.3)	(59.4)	(70.5)	(84.2)	(93.5)
Equity raised/(returned)	0	0	0	0	0
(Increase)/decrease in net debt	**59.9**	**(14.3)**	**96.4**	**144.4**	**170.8**

Balance Sheet (NZ$m)	2019A	2020A	2021E	2022E	2023E
Working capital	74.5	81.3	97.5	106.6	114.5
Fixed assets	666.6	776.6	774.2	853.2	925.8
Intangibles	270.0	284.7	299.7	314.7	329.7
Right of use asset	0	615.3	646.0	678.3	712.2
Other assets	61.7	91.1	88.3	88.3	88.3
Total funds employed	**1,072.8**	**1,848.9**	**1,905.7**	**2,041.1**	**2,170.5**
Net debt/(cash)	123.5	151.6	61.0	(83.4)	(254.2)
Lease liability	0	626.9	658.2	691.1	725.7
Other liabilities	111.0	104.1	104.5	104.5	104.5
Shareholder's funds	838.3	966.3	1,081.9	1,328.9	1,594.5
Minority interests	0	0	0	0	0
Total funding sources	**1,072.8**	**1,848.9**	**1,905.7**	**2,041.1**	**2,170.5**

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

Spot valuations (NZ$)	
1. DCF	59.05
2. PE relative	58.01
3. n/a	n/a

DCF valuation summary (NZ$m)	
Total firm value	8,171
(Net debt)/cash	(195)
Less: Capitalised operating leases	(2,029)
Value of equity	5,946

Valuation Ratios	2019A	2020A	2021E	2022E	2023E
EV/EBITDA (x)	22.3	14.3	12.7	11.3	10.4
EV/EBIT (x)	28.1	16.7	20.7	17.7	16.1
PE (x)	39.4	37.6	31.1	26.4	23.8
Price/NTA (x)	9.8	8.2	7.1	5.5	4.4
Free cash flow yield (%)	1.7	2.5	4.8	4.0	4.7
Net dividend yield (%)	1.0	1.1	1.3	1.5	1.7
Gross dividend yield (%)	1.4	1.5	1.8	2.1	2.3

Capital Structure	2019A	2020A	2021E	2022E	2023E
Interest cover EBIT (x)	29.7	60.1	12.4	17.8	20.1
Interest cover EBITDA (x)	37.4	70.3	20.4	27.8	31.1
Net debt/ND+E (%)	12.8	13.6	5.3	-6.7	-19.0
Net debt/EBITDA (x)	0.5	0.4	0.1	n/a	n/a

Key Ratios	2019A	2020A	2021E	2022E	2023E
Return on assets (%)	13.6	14.8	11.6	12.6	13.0
Return on equity (%)	16.8	15.3	16.5	15.8	14.7
Return on funds employed (%)	8.5	9.4	15.2	14.1	14.1
EBITDA margin (%)	8.7	12.9	13.5	13.7	13.9
EBIT margin (%)	6.9	11.0	8.2	8.7	9.0
Capex to sales (%)	3.5	5.2	2.4	4.5	4.2
Capex to depreciation (%)	194	277	46	92	86
Imputation (%)	100	100	100	100	100
Pay-out ratio (%)	40	40	39	40	40

Operating Performance	2019A	2020A	2021E	2022E	2023E
Revenue (NZ$m)					
New Zealand	719	753	783	830	880
Australia	761	797	920	1,029	1,095
USA	725	762	773	847	926
Asia	109	95	114	130	148
Europe	640	689	731	796	852
Total	**2,954**	**3,095**	**3,321**	**3,632**	**3,900**
EBITDA (NZ$m)					
New Zealand	110.6	139.8	146.1	154.8	166.1
Australia	59.3	104.8	148.8	167.6	178.5
USA	38.3	60.4	58.8	67.7	77.4
Asia	9.3	8.3	13.6	15.6	17.7
Europe	39.6	85.4	80.4	91.5	102.2
Total	**257.0**	**398.7**	**447.7**	**497.3**	**542.0**
NZDAUD	0.92	0.95	0.91	0.87	0.88
NZDUSD	0.68	0.65	0.65	0.66	0.67
NZDEUR	0.59	0.58	0.56	0.55	0.55

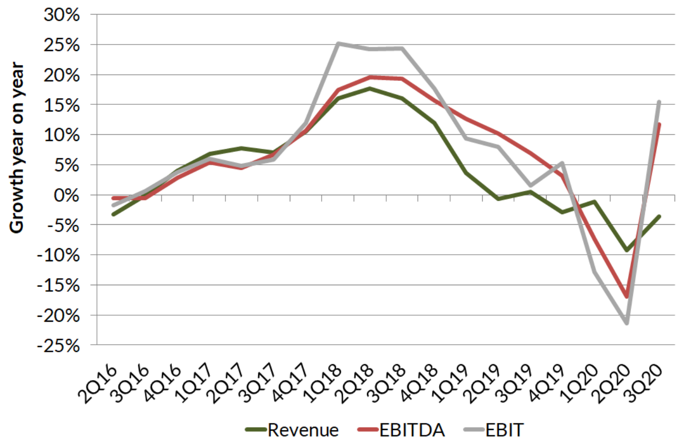
NOTE: IFRS 16 implemented from FY20

Revenue decline stopped

Industry revenue has grown in 3Q20, up +2% on the prior year. This growth follows five consecutive quarters of revenue decline and an industry growth deceleration that began in mid-2018. Airfreight and LTL transport drove revenue growth, up +14% and +1% in 3Q20 compared to the prior year respectively, whilst logistics (warehousing) experienced the largest decline, down -3% on the same period last year.

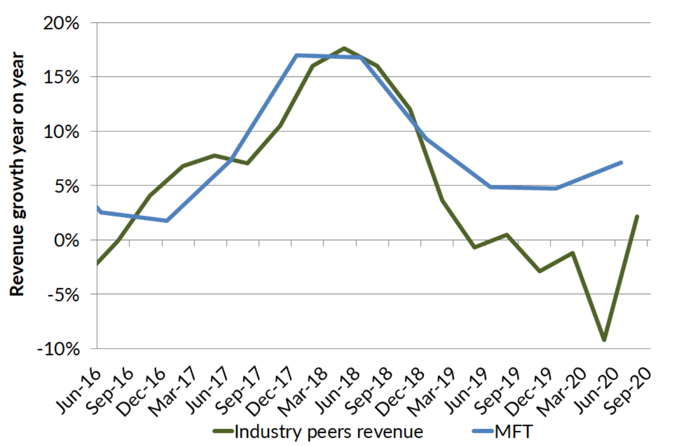
MFT's pre-released 1H21 results show another period of industry outperformance by the company. It has historically been strongly correlated with its global peers, as shown in Figure 2. However, MFT has managed to avoid the revenue decline that many of its peers have experienced in recent years and has continued to grow through COVID-19.

Figure 1. Average quarterly revenue of listed peers



Source: Company reports, Forsyth Barr analysis

Figure 2. MFT vs industry peers



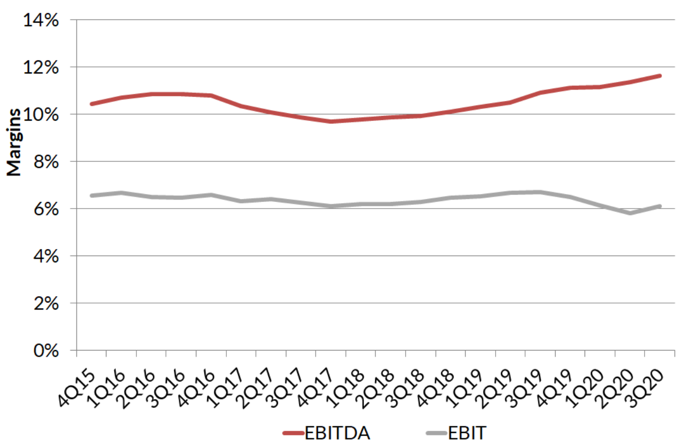
Source: Company reports, Forsyth Barr analysis

Margins expanding

MFT's global peers have reported another quarter of margin growth. All industry segments experienced an improvement in EBITDA margins, although investors need to be wary of the impact of IFRS 16 (accounting for leases) on like-for-like margin comparison. However, MFT's peers have now included IFRS 16 in their reporting for over one year, indicating that current margin expansion is unrelated. LTL margins remain the most attractive in the industry. After several quarters of margin compression, LTL margins expanded in 3Q20. Logistics (warehousing) margins continue to grow albeit logistics is disproportionately impacted by the implementation of IFRS 16.

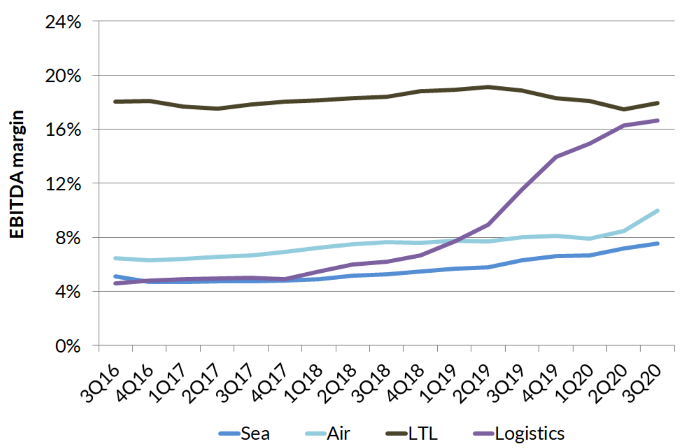
MFT's PBT margins improved in its 1H21, driven by the company's Australia and Asia divisions experiencing strong improvement and supported by a further modest uplift in New Zealand.

Figure 3. 12-month rolling peer group margins



Source: Company reports, Forsyth Barr analysis

Figure 4. 12-month rolling margins by industry sector



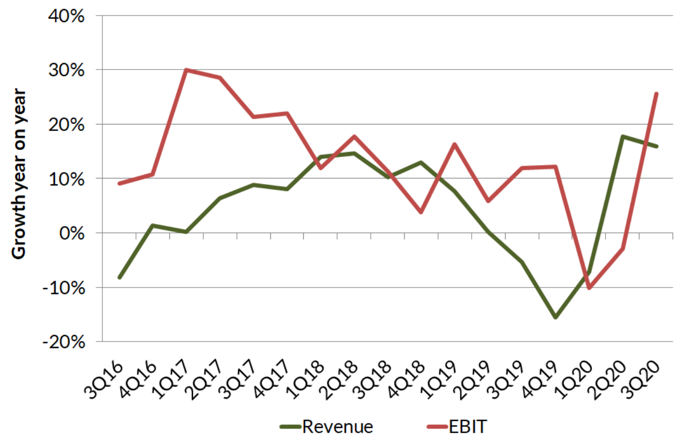
Source: Company reports, Forsyth Barr analysis

Seafreight recovering

Air and sea forwarding have experienced another quarter of margin improvement in 3Q20. Air freight's margin increase is a function of the significant reduction in passenger aircraft related freight capacity. Sea freight rates have improved on key trade lanes helped by an increase in 'blank sailings' by shipping lines.

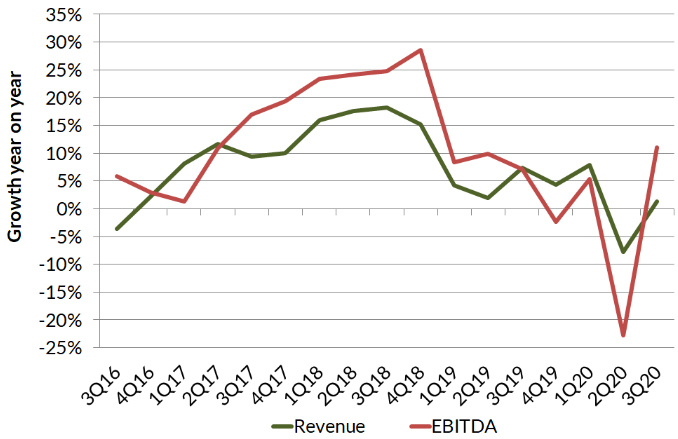
LTL recovered in 3Q20 following a year-on-year revenue decline in 2Q20, its first revenue decline since 2016. LTL margins remain the most attractive in the industry.

Figure 5. Growth in air and sea sector



Source: Company reports, Forsyth Barr analysis

Figure 6. Growth in LTL sector

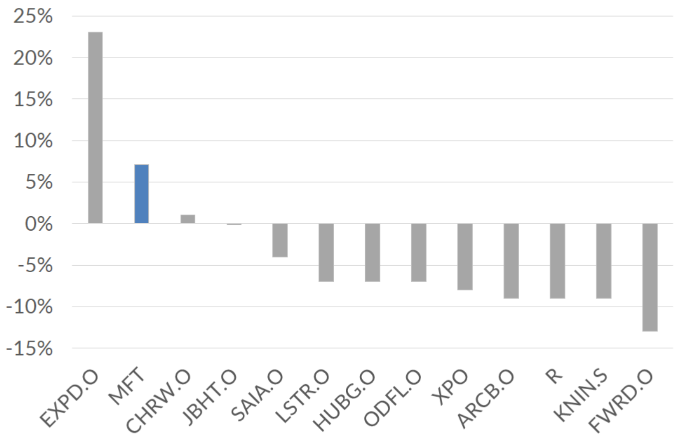


Source: Company reports, Forsyth Barr analysis

Mainfreight 1H21 result

MFT's pre-released result, when compared to the results of its peers, highlights its continued ability to outperform the industry. MFT revenue was up ~+7% in its 1H21, beating all relevant peers, with the exception of Expeditors International (EXPD.O), which benefited significantly from airfreight rate increases.

Figure 7. Comparative 1H21 (6m to Sept 2020) revenue growth



Source: Company reports, Forsyth Barr analysis
Note: MFT 1H21 based on its pre-released estimated revenue

Figure 8. MFT 1H21 earnings forecast (NZ$m)

	1H20	1H21E	Change
Sales revenue	1,500.5	1,607.2	7.1%
Profit before tax	**82.9**	**102.2**	**23.4%**
Reported NPAT	59.1	73.1	23.6%
Underlying NPAT	**59.1**	**73.1**	**23.6%**
Underlying EPS (cents)	58.7	72.6	23.6%
Interim DPS (cents)	25.0	28.0	12.0%

Source: MFT, Forsyth Barr analysis

Our analysis

We have analysed the 3Q20 results reported by relevant global listed peers of MFT. We have made an effort to remove impacts of material M&A in order to ensure a like-for-like comparison between companies and periods. IFRS 16 has had a material impact on some margins, especially in the logistics sector, and we factor this into our conclusions.

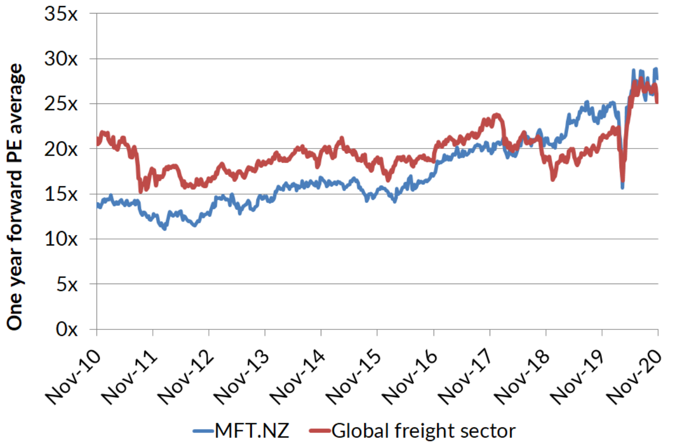
Where divisional disclosure allows we segment each company's results to provide a view on each market sector.
Listed industry peers included in our analysis are:

- Old Dominion Freight Line (ODFL.O)
- ArcBest (ARCB.O)
- Saia (SAIA.O)
- DSV (DSV.CO)
- Kuehne und Nagel (KNIN.S)
- Expeditors International (EXPD.O)
- CH Robinson (CHRW.O)
- JB Hunt (JBHT.O)
- Forward Air Corp (FWRD.O)
- XPO Logistics (XPO)
- Hub Group (HUBG.O)
- Ryder Systems (R)
- Landstar System (LSTR.O)

Valuation comparison

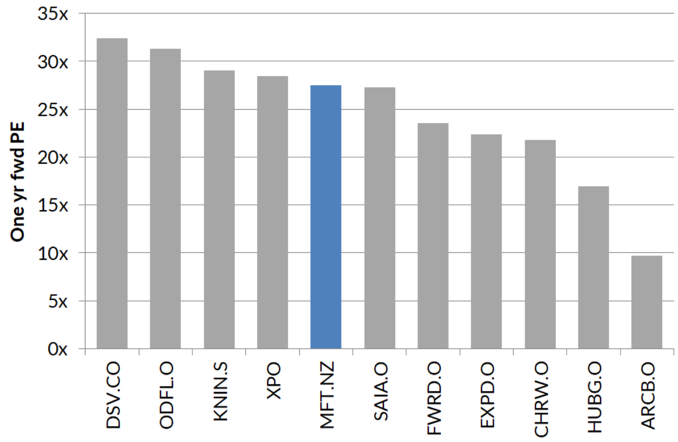
MFT is currently trading at ~27x one year forward PE, placing it above the combined average of its global industry peers (Figure 9), however, its closest (albeit larger) peers ODFL and DSV are trading at a valuation premium to MFT (Figure 10).

Figure 9. MFT vs average of industry peers



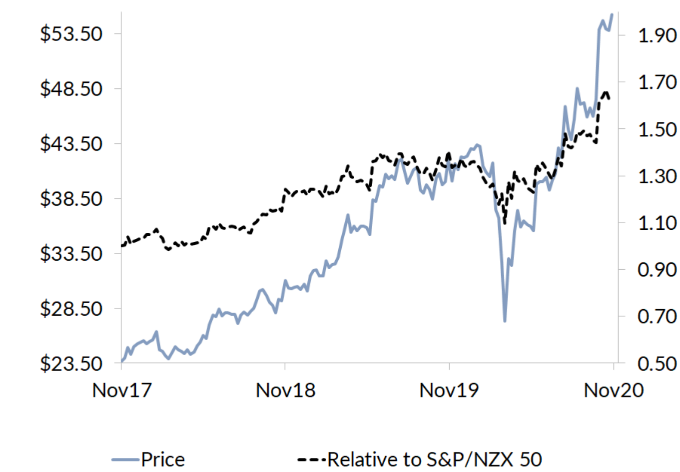
Source: Eikon, Forsyth Barr analysis

Figure 10. MFT global peer valuations



Source: Eikon, Forsyth Barr analysis

Figure 11. Price performance



Source: Forsyth Barr analysis

Figure 12. Substantial shareholders

Shareholder	Latest Holding
Rorohora No. 2 Trust	16.3%
Harbour Asset Management & Jarden Securities Limited	5.6%
Fisher Funds Management	5.1%

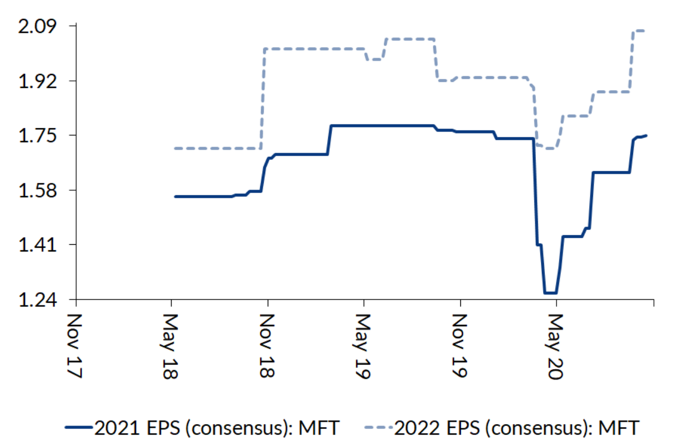
Source: NZX, Forsyth Barr analysis, NOTE: based on SPH notices only

Figure 13. International valuation comparisons

Company	Code	Price	Mkt Cap	PE		EV/EBITDA		EV/EBIT		Cash Yld
(metrics re-weighted to reflect MFT's balance date - March)			(m)	2021E	2022E	2021E	2022E	2021E	2022E	2022E
Mainfreight	**MFT NZ**	**NZ$55.25**	**NZ$5,564**	**31.1x**	**26.4x**	**12.8x**	**11.5x**	**20.9x**	**18.0x**	**1.5%**
FREIGHTWAYS *	FRE NZ	NZ$8.95	NZ$1,482	20.9x	17.7x	9.8x	8.7x	14.9x	12.4x	4.3%
OLD DOMINION FREIGHT LINE	ODFL US	US$207.02	US$24,290	35.6x	30.1x	20.0x	17.5x	25.9x	22.5x	0.3%
DSV PANALPINA A/S	DSV DC	kr1118.50	kr257,255	38.8x	30.4x	19.9x	17.7x	28.3x	24.2x	0.4%
C.H. ROBINSON WORLDWIDE INC	CHRW US	US$90.62	US$12,319	24.2x	21.1x	17.3x	15.2x	19.9x	17.1x	2.4%
KUEHNE + NAGEL INTL AG-REG	KNIN SW	CHF196.80	CHF23,616	31.2x	28.4x	13.4x	13.1x	23.8x	21.9x	2.2%
EXPEDITORS INTL WASH INC	EXPD US	US$88.32	US$14,950	22.4x	22.0x	14.7x	14.7x	15.8x	15.6x	1.2%
			Compco Average:	**28.9x**	**25.0x**	**15.9x**	**14.5x**	**21.4x**	**19.0x**	**1.8%**
EV = Current Market Cap + Actual Net Debt			**MFT Relative:**	**8%**	**6%**	**-19%**	**-21%**	**-2%**	**-5%**	**-17%**

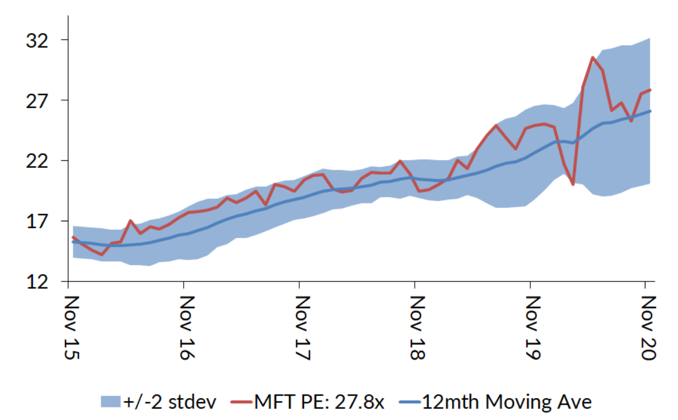
Source: *Forsyth Barr analysis, Bloomberg Consensus, Compco metrics re-weighted to reflect headline (MFT) companies fiscal year end

Figure 14. Consensus EPS momentum (NZ$)



Source: Forsyth Barr analysis, Bloomberg

Figure 15. One year forward PE (x)



Source: Forsyth Barr analysis

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OUTPERFORM	NEUTRAL	UNDERPERFORM
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