FORSYTH BARR

Napier Port

NEUTRAL

Volumes Support First Port Call

Napier Port's (NPH) year-end volume update suggests it's on track to exceed its pre-listing forecasts for FY19. Log exports and container volumes are above management's forecasts, and therefore suggest the company will report a positive inaugural full year result as a listed company on 19 November 2019. However, actual log exports are not as high as NZ Statistics export data suggests, which means we cut our FY19 earnings estimates modestly. Notwithstanding post-listing share price strength, which now places NPH on a one year forward EV/EBITDA multiple of ~16x, we retain a NEUTRAL rating and an NZ$3.00 target price.

What's changed?

- **Earnings:** FY19E EBITDA: -2%, FY20E: no change

Volume update

NPH's FY19 cargo volumes are modestly ahead of PFI (prospectus financial information) forecasts from the time the company issued its pre-listing product disclosure statement in July 2019. Both containers and log exports are up relative to management's expectations, while other bulk products are lower. Our previous log export forecasts were based on NZ Statistics data, which suggests that volumes were +4% ahead of that reported by NPH. The variance may reflect shipment timing differences. As a result, we lower our FY19 estimates.

WPI risk remains

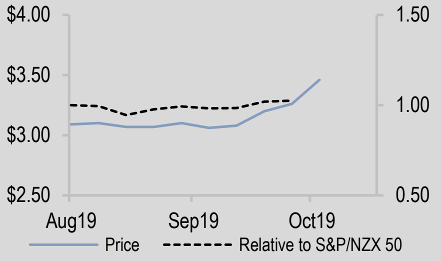
A key risk to NPH remains its contestable WPI (Winstone Pulp International) contract which is currently being touted by other ports. WPI exports wood pulp via rail from Ohakune through NPH. We estimate WPI accounts for ~8% of group revenue and a higher proportion of profitability. We provide no discount to our earnings forecasts or valuation in relation to this contract risk and continue to believe that NPH will retain it.

Valuation; size discount has been eroded

We retain an NZ$3.00 target price. NPH now trades at a one year forward EV/EBITDA of ~16x and PE of ~34x. These both represent sizeable, albeit justifiable, discounts to Port of Tauranga (POT) given the latter's superior growth return on capital profile. In particular, NPH's returns outlook is depressed by the imminent and sizeable 6 Wharf investment. NPH now trades on an enterprise value to invested capital multiple consistent with its larger cap infrastructure peers after adjusting for return on capital differences. The market no longer applies a discount for size or liquidity.

NZX Code	NPH
Share price	NZ$3.46
Target price	NZ$3.00
Risk rating	Medium
Issued shares	200.0m
Market cap	NZ$692m
Average daily turnover	571.7k (NZ$1,723k)

Share Price Performance



Financials: September	18A	19E	20E	21E
NPAT* (NZ$m)	n/a	19.7	20.0	23.8
EPS* (NZc)	n/a	9.8	10.0	11.9
EPS growth* (%)	n/a	n/a	1.5	19.2
DPS (NZc)	0.0	2.5	7.5	9.1
Imputation (%)	0	100	100	100

Valuation (x)	18A	19E	20E	21E
EV/EBITDA	20.6	17.7	16.2	14.4
EV/EBIT	n/a	24.9	23.7	20.6
PE	n/a	35.1	34.6	29.0
Price / NTA	n/a	2.1	2.0	2.0
Cash dividend yield (%)	0.0	0.7	2.2	2.6
Gross dividend yield (%)	0.0	1.0	3.0	3.6

*Historic and forecast numbers based on underlying profits

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Investment View

NPH offers investors exposure to a long term infrastructure asset, which has a favourable catchment in Hawke's Bay. We expect cargo growth momentum to continue over the medium term supported by positive outlooks for both the forestry and pipfruit sectors. NPH's pricing power will be key in improving economic returns following the significant capital investment in a new wharf. While NPH trades at a (justifiably) large earnings valuation discount to Port of Tauranga (POT), we believe it is fairly priced at a modest premium to its smaller sector peers. NEUTRAL.

Napier Port Ltd September year end

Forsyth Barr valuation			
Valuation methodology		DCF and invested capital muliple	
12-month target price (NZ$)*	**3.00**	**Spot valuations (NZ$)**	
Expected share price return	-13.3%	1. DCF	2.85
Net dividend yield	2.2%	2. Invested capital multiple	2.85
Estimated 12-month return	-11.1%	3. n/a	n/a
Key WACC assumptions		**DCF valuation summary (NZ$m)**	
Risk free rate	2.50%	Total firm value	549
Equity beta	0.72	(Net debt)/cash	21
WACC	6.4%	Value of equity	569
Terminal growth	1.5%	Shares (m)	200

Profit and Loss Account (NZ$m)	**2017A**	**2018A**	**2019E**	**2020E**	**2021E**
Sales revenue	86.7	91.7	98.0	102.5	110.9
Normalised EBITDA	**35.7**	**37.3**	**40.3**	**40.9**	**46.0**
Depreciation and amortisation	n/a	n/a	(11.7)	(12.9)	(13.8)
Normalised EBIT	n/a	n/a	**28.6**	**27.9**	**32.1**
Net interest	n/a	n/a	(0.7)	0.1	0.9
Associate income	n/a	n/a	(1.1)	(0.1)	-
Tax	n/a	n/a	(8.0)	(7.9)	(9.3)
Minority interests	n/a	n/a	-	-	-
Normalised NPAT	n/a	n/a	**19.7**	**20.0**	**23.8**
Abnormals/other	n/a	n/a	13.6	-	-
Reported NPAT	n/a	n/a	**6.1**	**20.0**	**23.8**
Normalised EPS (cps)	n/a	n/a	9.8	10.0	11.9
DPS (cps)	n/a	n/a	2.5	7.5	9.1

Growth Rates	**2017A**	**2018A**	**2019E**	**2020E**	**2021E**
Revenue (%)	19.3	5.8	6.8	4.6	8.2
EBITDA (%)	24.1	4.4	8.0	1.5	12.4
EBIT (%)	n/a	n/a	n/a	-2.3	15.0
Normalised NPAT (%)	n/a	n/a	n/a	1.5	19.2
Normalised EPS (%)	n/a	n/a	n/a	1.5	19.2
Ordinary DPS (%)	n/a	n/a	n/a	>100	21.7

Cash Flow (NZ$m)	**2017A**	**2018A**	**2019E**	**2020E**	**2021E**
EBITDA	**35.7**	**37.3**	**40.3**	**40.9**	**46.0**
Working capital change	n/a	n/a	-	-	-
Interest & tax paid	n/a	n/a	(15.6)	(7.8)	(8.3)
Other	n/a	n/a	0.7	(1.8)	-
Operating cash flow	n/a	n/a	**25.4**	**31.2**	**37.6**
Capital expenditure	n/a	n/a	(24.8)	(69.7)	(85.4)
(Acquisitions)/divestments	n/a	n/a	(0.2)	(0.1)	-
Other	n/a	n/a	(53.9)	(12.6)	(16.2)
Funding available/(required)	n/a	n/a	**(53.5)**	**(51.2)**	**(63.9)**
Dividends paid	n/a	n/a	(54.0)	(11.0)	(16.2)
Equity raised/(returned)	n/a	n/a	156.0	(0.3)	-
Increase/(decrease) in net debt	n/a	n/a	**(102.4)**	**51.0**	**63.9**

Balance Sheet (NZ$m)	**2017A**	**2018A**	**2019E**	**2020E**	**2021E**
Working capital	0.7	2.8	2.3	0.3	1.1
Fixed assets	307.2	309.6	324.8	383.1	454.7
Intangibles	1.7	1.3	1.5	1.8	1.8
Other assets	8.1	8.8	8.9	8.7	8.7
Total funds employed	**317.7**	**322.6**	**337.5**	**393.8**	**466.2**
Net debt/(cash)	83.3	80.6	(21.9)	29.6	93.5
Other non current liabilities	29.2	29.6	23.2	20.5	20.0
Shareholder's funds	205.1	212.4	336.3	343.8	352.7
Minority interests	-	-	-	-	-
Total funding sources	**317.7**	**322.6**	**337.5**	**393.8**	**466.2**

Valuation Ratios	**2017A**	**2018A**	**2019E**	**2020E**	**2021E**
EV/EBITDA (x)	n/a	20.6	17.7	16.2	14.4
EV/EBIT (x)	n/a	n/a	24.9	23.7	20.6
PE (x)	n/a	n/a	35.1	34.6	29.0
Price/NTA (x)	n/a	n/a	2.1	2.0	2.0
Free cash flow yield (%)	n/a	n/a	0.1	-5.6	-6.9
Net dividend yield (%)	0.0	0.0	0.7	2.2	2.6
Gross dividend yield (%)	0.0	0.0	1.0	3.0	3.6
Imputation (%)	0	0	100	100	100
Pay-out ratio (%)	n/a	n/a	25	75	76

Capital Structure	**2017A**	**2018A**	**2019E**	**2020E**	**2021E**
Interest cover EBIT (x)	n/a	n/a	42.9	n/a	n/a
Interest cover EBITDA (x)	n/a	n/a	60.4	n/a	n/a
Net debt/ND+E (%)	28.9	27.5	-7.0	7.9	21.0
Net debt/EBITDA (x)	2.3	2.2	n/a	0.7	2.0

Key Ratios	**2017A**	**2018A**	**2019E**	**2020E**	**2021E**
Return on assets (%)	n/a	n/a	7.7	6.9	6.6
Return on equity (%)	n/a	n/a	5.9	5.8	6.8
Return on funds employed (%)	n/a	n/a	8.8	7.4	6.8
EBITDA margin (%)	41.2	40.6	41.1	39.9	41.5
EBIT margin (%)	n/a	n/a	29.2	27.3	29.0
Capex to sales (%)	n/a	n/a	25.3	68.0	77.0
Capex to depreciation (%)	n/a	n/a	212	538	618

Operating Performance	**2017A**	**2018A**	**2019E**	**2020E**	**2021E**
Revenue (NZ$m)					
Container Services	61	58	60	63	68
Bulk Cargo	22	29	32	32	36
Cruise	2	3	4	5	5
Sundry	0	0	1	0	0
Property	2	2	2	2	2
Total revenue	**87**	**92**	**98**	**103**	**111**
Expenses (NZ$m)					
Employee benefit	26	26	28	31	33
Maintenance	9	9	9	9	10
Other operating expenses	16	19	20	21	22
Total	**51**	**54**	**58**	**62**	**65**
Container volumes (TEU'000)					
Dry	125	102	105	103	106
Reefer	57	58	59	59	61
Empties	99	100	103	102	105
Other	7	7	4	8	8
Total containers	**288**	**266**	**271**	**272**	**280**
Bulk cargo (m tonnes)					
Log exports	1,630	2,208	2,581	2,500	2,800
Other exports	241	177	167	208	216
Imports	634	686	656	609	621
Total bulk cargo volume	**2,505**	**3,071**	**3,404**	**3,317**	**3,638**
Ship visits					
Container	372	329	314	313	313
Bulk	262	298	314	301	301
Cruise	54	57	70	87	90
Total	**688**	**684**	**698**	**701**	**704**

NOTE: EBITDA referenced on this page reflects pro-forma EBITDA

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

Earnings revisions

We lower our FY19 earnings forecasts in light of NPH's year-end volume update. Our forecasts now incorporate company provided actual volumes. The key differences between our previous estimates and actual are as follows:

- **Log exports:** The company reports 2.58MT of log exports vs. our forecast based on Stats NZ export data of 2.70MT. We suspect the difference relates to timing differences around shipment cut-offs between the NZ Stats data (sourced from exporters) and NPH.
- **Containers:** Partially offsetting the lower than expected log exports was a modestly better container outcome. Total containers were 271k TEU compared to our previous forecast of 269k TEU.

Figure 1. Earnings revisions (NZ$m)

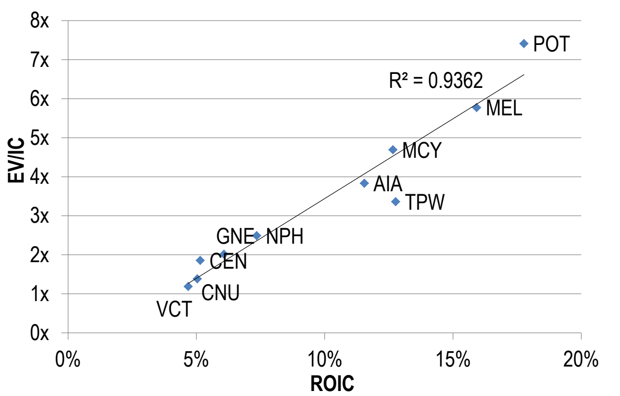
		FY19E			FY20E			FY21E		
	PFI	**Old**	**New**	**Chg**	**Old**	**New**	**Chg**	**Old**	**New**	**Chg**
Log exports (JASM)	2,500	2,700	2,581	-4.4%	2,500	2,500	0.0%	2,800	2,800	0.0%
Containers (TEU)	269	269	271	0.7%	272	272	0.0%	280	280	0.0%
Sales revenue	97.4	99.2	98.0	-1.2%	102.5	102.5	0.0%	110.9	110.9	0.0%
EBITDA	39.8	41.0	40.3	-1.8%	40.9	40.9	0.0%	46.0	46.0	0.0%
Underlying NPAT	**19.2**	**20.4**	**19.7**	**-3.6%**	**20.0**	**20.0**	**0.0%**	**23.8**	**23.8**	**0.0%**
Underlying EPS (cents)	9.6	10.2	9.8	-3.6%	10.0	10.0	0.0%	11.9	11.9	0.0%
DPS (cents)	n/a	2.5	2.5	0.0%	7.5	7.5	0.0%	9.1	9.1	0.0%

Source: Forsyth Barr analysis

Valuation

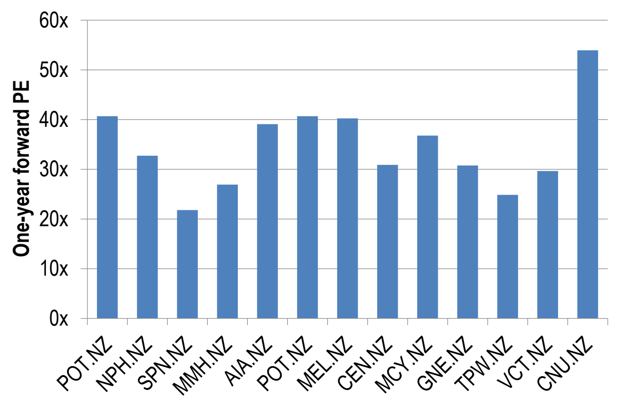
We make no changes to our target price of NZ$3.00. This incorporates a -20% size discount relative to NPH's larger cap infrastructure players within our EV/IC valuation framework. Figure 2 suggests that the market is not imposing any size discount on NPH.

Figure 2. No longer a size discount for NPH



Source: Eikon, Forsyth Barr analysis

Figure 3. Infrastructure players aren't cheap



Source: Eikon, Forsyth Barr analysis

Investment summary

Napier Port (NPH) is New Zealand's fourth largest container terminal and sixth largest bulk cargo port. The majority of its cargo is export and its productive hinterland drives most of its throughput with key trades including forestry and pipfruit. The Port is building a new wharf to ease congestion and provide greater capacity for growth. While it trades at a material discount to Port of Tauranga, we believe current valuation levels are fair in light of its lower return on capital and longer term growth outlook. NEUTRAL.

Business quality

- **Long term infrastructure:** NPH is the gateway for Hawke's Bay favourable catchment of exports. Land transport costs provide a barrier to entry for other ports.
- **Pricing power:** NPH has a track record of being more aggressive with its approach to pricing than other NZ ports. We expect it to enhance returns following its 6 Wharf investment in part through higher pricing.

Earnings and cash flow outlook

- **Wall of wood:** Hawke's Bay has approximately 134,000 ha of planted forests. Due to the significant tree planting in the 1990s, particularly among smaller private forest owners, harvest volume should increase materially over the next five years (the 'wall of wood').
- **Pipfruit:** Hawke's Bay is NZ's largest region for producing pipfruit. The emergence of new apple varietals and ongoing tree planting programmes by the larger growers provide a favourable outlook.
- **6 Wharf:** NPH's significant investment in a new container wharf will provide capacity for longer term growth but will act as a headwind to earnings over the medium term given the associated costs (i.e. depreciation and interest).

Financial structure

- **Rising debt levels:** NPH is currently cum-capex and will experience a leveraging up of its balance sheet over the medium term.

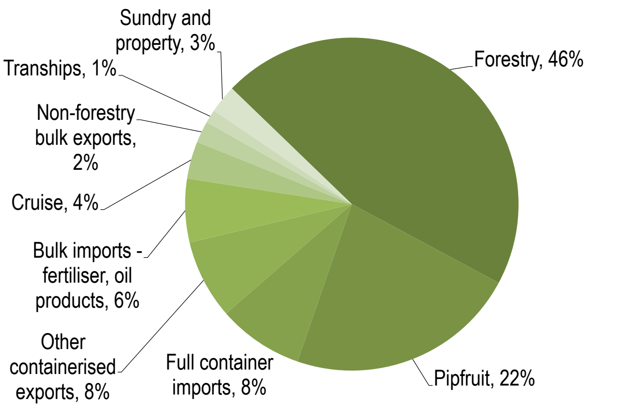
Risks factors

- **Industry sector risk:** Any change in the supply, or demand for NZ forestry/ pipfruit could have a material impact on the Port's financial performance.
- **Competition from other ports:** Increased competition from other ports may mean that NPH loses cargo in future, particularly current contestable cargo.

Company description

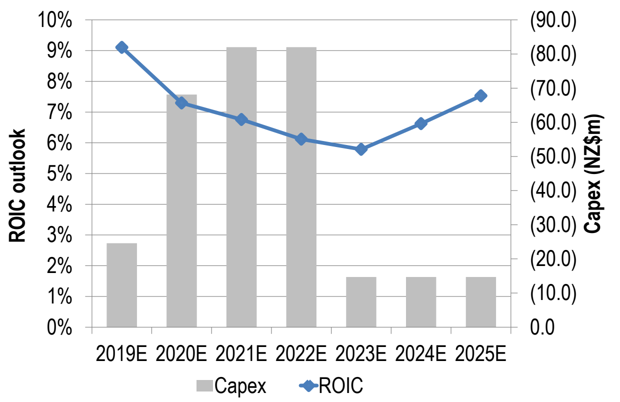
Napier Port is New Zealand's 4th largest container terminal and the 5th largest port, as measured by cargo tonnage. Cargo is export driven accounting for ~79% of throughput in FY18. Key export commodities include forestry product (logs, sawn timber, and pulp) and pipfruits (apple and pears).

Figure 4. NPH estimated revenue mix (FY19E)



Source: Forsyth Barr analysis

Figure 5. Returns under pressure from 6 Wharf capex



Source: Forsyth Barr analysis

Figure 6. Substantial Shareholders

Shareholder	Latest Holding
Hawke's Bay Regional Council	55.0%

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

Figure 7. International Compcos

Company	Code	Price	Mkt Cap	PE		EV/EBITDA		EV/EBIT		Cash D/Yld
(metrics re-weighted to reflect NPH's balance date - September)			(m)	2019E	2020E	2019E	2020E	2019E	2020E	2020E
Napier Port	**NPH NZ**	**NZ$3.46**	**NZ$692**	**35.1x**	**34.6x**	**19.2x**	**18.9x**	**27.0x**	**27.6x**	**2.2%**
Mitsubishi Logistics Corp	9301 JP	¥2764.00	¥243,123	20.3x	19.4x	11.7x	11.4x	24.3x	24.3x	2.3%
Westshore Terminals Investment Corp	WTE CN	C$21.85	C$1,506	11.4x	11.3x	8.5x	8.2x	9.3x	9.2x	2.9%
Hamburger Hafen und Logistik AG	HHFA GR	€23.18	€1,686	15.5x	14.9x	6.4x	6.1x	10.7x	10.3x	3.9%
Global Ports Investments PLC	GLPR LI	US$2.80	US$535	<0x	5.9x	6.0x	5.5x	8.1x	7.0x	0.0%
Eurokai GmbH & Co KGaA	EUK2 GR	€33.60	€444	10.3x	12.1x	5.5x	6.3x	8.2x	9.8x	n/a
Auckland Airport *	AIA NZ	NZ$8.92	NZ$10,837	39.4x	40.1x	23.4x	23.1x	28.8x	29.0x	2.5%
Sydney Airport	SYD AT	A$8.73	A$19,718	>50x	47.2x	22.1x	21.1x	32.9x	30.8x	4.6%
Qube Holdings	QUB AT	A$3.30	A$5,365	29.5x	36.5x	16.9x	19.7x	24.9x	32.6x	1.8%
Port of Tauranga	POT	NZ$6.48	NZ$4,408	42.9x	41.1x	27.8x	26.5x	33.0x	31.1x	2.4%
			Compco Average:	**24.2x**	**25.4x**	**14.2x**	**14.2x**	**20.0x**	**20.5x**	**2.5%**
EV = Current Market Cap + Actual Net Debt			**NPH Relative:**	**+45%**	**+36%**	**+35%**	**+33%**	**+35%**	**+35%**	**-15%**

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