

Napier Port

Navigating Choppy Water

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NEUTRAL 

Napier Port (NPH) provided a third quarter volume update, which highlighted COVID-19 related weakness given restrictions on customer activity but a robust recovery since. The company suggests that current volume run-rates are below the prior year with softness in both imports and exports. Third quarter container volumes declined -17%, while bulk cargo (predominantly log exports) was down -24%. NPH's earnings will benefit in the medium term from increased forestry harvesting given the maturing 'wall of wood'; however, its significant capital investment in 6 Wharf will likely dampen financial returns for the foreseeable future. NPH trades at a one year forward EV/EBITDA of ~18x, which, while at a material discount to Port of Tauranga (POT), is fair given its lower return on capital outlook, in our opinion.

NZX Code	NPH	Financials: Sep/	19A	20E	21E	22E	Valuation (x)	19A	20E	21E	22E
Share price	NZ\$3.45	NPAT* (NZ\$m)	19.7	18.5	20.1	24.6	EV/EBITDA	17.4	18.5	17.6	14.2
Target price	NZ\$3.25	EPS* (NZc)	16.3	9.3	10.1	12.3	EV/EBIT	24.8	28.4	26.7	20.4
Risk rating	Medium	EPS growth* (%)	n/a	-43.3	8.7	22.2	PE	21.1	37.2	34.3	28.0
Issued shares	200.0m	DPS (NZc)	2.5	4.5	7.8	9.8	Price / NTA	1.2	2.0	1.9	1.9
Market cap	NZ\$690m	Imputation (%)	100	100	100	100	Cash div yld (%)	0.7	1.3	2.3	2.9
Avg daily turnover	289.5k (NZ\$923k)	*Based on normalised profits					Gross div yld (%)	1.0	1.8	3.1	4.0

What's changed?

- **Earnings:** FY20 NPAT lifted by +8%, due to higher container and log export assumptions
- **Target price:** Raised by 20c to NZ\$3.25

Lockdown impact

With the majority of NPH's cargo deemed non-essential, volumes fell significantly as a result of Alert Level 4. Inventory at the beginning of lockdown meant the port was still able to handle non-essential goods but their supply dried up, consequently the impact was spread through both April and May. Key non-essential cargo included log exports, wood pulp and timber, wool and paper products. While cargo volumes declined during 3Q20, NPH benefited from ~NZ\$2m of wage subsidies from the government which will have helped mitigate the profit impact.

Medium term growth

NPH is due to report 3Q20 earnings in late-August, and at the same time provide full year guidance. Our revised estimates incorporates upgrades to FY20 (due to higher estimates for both log exports and containers), but FY21 and FY22 forecasts are largely unchanged. We expect earnings growth to be a feature over the medium term with a temporary decline in FY23 when 6 Wharf is commissioned, at which time the associated depreciation and interest costs will impact profitability.

Valuation is fair

NPH trades at a one-year forward EV/EBITDA multiple of ~18x, which is a substantial discount to POT (~32x), but a modest premium to other domestic infrastructure players. POT should demand a premium to NPH, in our opinion, as it generates a substantially higher return on capital and has greater growth certainty over the longer term.

Napier Port Ltd (NPH)

Priced as at 15 Jul 2020 (NZ\$)						3.45						
12-month target price (NZ\$)*						3.25	Spot valuations (NZ\$)					
Expected share price return						-5.8%	1. DCF					3.12
Net dividend yield						2.1%	2. Invested capital multiple					3.07
Estimated 12-month return						-3.7%	3. n/a					n/a
Key WACC assumptions						DCF valuation summary (NZ\$m)						
Risk free rate						2.00%	Total firm value					592
Equity beta						0.72	(Net debt)/cash					31
WACC						6.3%	Less: Capitalised operating leases					0
Terminal growth						1.5%	Value of equity					623
Profit and Loss Account (NZ\$m)						Valuation Ratios						
	2018A	2019A	2020E	2021E	2022E		2018A	2019A	2020E	2021E	2022E	
Sales revenue	91.7	99.6	96.8	104.1	116.8	EV/EBITDA (x)	20.5	17.4	18.5	17.6	14.2	
Normalised EBITDA	37.3	40.5	36.9	40.5	50.1	EV/EBIT (x)	n/a	24.8	28.4	26.7	20.4	
Depreciation and amortisation	n/a	(12.0)	(12.9)	(13.8)	(15.2)	PE (x)	n/a	21.1	37.2	34.3	28.0	
Normalised EBIT	n/a	28.5	23.9	26.7	35.0	Price/NTA (x)	n/a	1.2	2.0	1.9	1.9	
Net interest	n/a	(0.5)	0.1	1.3	(0.8)	Free cash flow yield (%)	n/a	1.7	-5.4	-7.5	-6.7	
Associate income	n/a	(1.1)	(0.1)	0	0	Net dividend yield (%)	0.0	0.7	1.3	2.3	2.9	
Tax	n/a	(8.1)	(4.3)	(7.8)	(9.6)	Gross dividend yield (%)	0.0	1.0	1.8	3.1	4.0	
Minority interests	n/a	0	0	0	0	Capital Structure						
Normalised NPAT	n/a	19.7	18.5	20.1	24.6	Interest cover EBIT (x)	n/a	57.4	n/a	n/a	45.0	
Abnormals/other	n/a	13.0	(1.9)	0	0	Interest cover EBITDA (x)	n/a	81.5	n/a	n/a	64.5	
Reported NPAT	n/a	6.8	20.1	20.1	24.6	Net debt/ND+E (%)	27.5	-10.3	7.9	19.2	28.8	
Normalised EPS (cps)	n/a	16.3	9.3	10.1	12.3	Net debt/EBITDA (x)	2.2	n/a	0.8	2.1	3.0	
DPS (cps)	0	2.5	4.5	7.8	9.8	Key Ratios						
Growth Rates							2018A	2019A	2020E	2021E	2022E	
Revenue (%)	5.8	8.6	-2.9	7.5	12.2	Return on assets (%)	n/a	7.7	5.9	5.5	6.3	
EBITDA (%)	4.4	8.6	-8.9	9.7	23.9	Return on equity (%)	n/a	5.9	5.4	5.6	6.7	
EBIT (%)	n/a	n/a	-16.0	11.4	31.1	Return on funds employed (%)	0.0	8.9	6.9	5.8	6.1	
Normalised NPAT (%)	n/a	n/a	-6.0	8.7	22.2	EBITDA margin (%)	40.6	40.7	38.1	38.9	43.0	
Normalised EPS (%)	n/a	n/a	-43.3	8.7	22.2	EBIT margin (%)	n/a	28.6	24.7	25.6	29.9	
Ordinary DPS (%)	n/a	n/a	79.4	73.7	26.2	Capex to sales (%)	n/a	17.5	71.0	82.1	73.6	
Cash Flow (NZ\$m)							2018A	2019A	2020E	2021E	2022E	
EBITDA	37.3	40.5	36.9	40.5	50.1	Capex to depreciation (%)	n/a	145	531	618	566	
Working capital change	n/a	1.2	0	0	0	Imputation (%)	0	100	100	100	100	
Interest & tax paid	n/a	(15.6)	(5.8)	(6.5)	(10.3)	Pay-out ratio (%)	n/a	15	48	77	80	
Other	n/a	3.2	0.1	0	0	Operating Performance						
Operating cash flow	n/a	29.3	31.2	34.0	39.8	Revenue (NZ\$m)						
Capital expenditure	n/a	(17.4)	(68.7)	(85.4)	(85.9)	Container Services		58.0	61.2	60.7	65.9	71.3
(Acquisitions)/divestments	n/a	(0.1)	(0.1)	0	0	Bulk Cargo		29.0	32.3	29.3	34.5	38.9
Other	n/a	(79.9)	(1.1)	0	0	Cruise		2.6	3.7	4.2	1.1	4.0
Funding available/(required)	n/a	(68.0)	(38.7)	(51.4)	(46.1)	Sundry		0.4	0.2	0.4	0.4	0.4
Dividends paid	n/a	(54.0)	(11.0)	(15.2)	(17.2)	Property		1.9	2.2	2.1	2.1	2.1
Equity raised/(returned)	n/a	234.0	(0.3)	0	0	Total revenue		91.8	99.6	96.8	104.1	116.8
(Increase)/decrease in net debt	n/a	112.0	(50.0)	(66.6)	(63.3)	Container volumes (TEU'000)						
Balance Sheet (NZ\$m)							2018A	2019A	2020E	2021E	2022E	
Working capital	2.8	0.7	0.3	1.0	1.2	Dry		107	106	98	106	109
Fixed assets	309.6	317.2	383.1	454.7	525.4	Reefer		53	58	57	60	62
Intangibles	1.3	1.1	1.8	1.8	1.8	Empties		100	103	100	106	109
Right of use asset	0	0	0.7	0.7	0.7	Other		7	4	7	7	7
Other assets	8.8	8.4	8.2	8.2	8.2	Total containers		267	271	262	279	287
Total funds employed	322.6	327.4	394.0	466.4	537.2	Bulk cargo (m tonnes)						
Net debt/(cash)	80.6	(31.2)	29.6	85.4	148.7	Log exports		2,208	2,581	2,250	2,650	3,000
Lease liability	0	0.9	0.7	0.7	0.7	Other exports		177	167	137	153	166
Other liabilities	29.6	22.2	19.8	19.8	19.8	Imports		686	656	558	625	662
Shareholder's funds	212.4	335.5	344.0	360.4	367.9	Total bulk cargo volume		3,071	3,404	2,945	3,428	3,828
Minority interests	0	0	0	0	0	NOTE: EBITDA referenced on this page reflects pro-forma EBITDA						
Total funding sources	322.6	327.4	394.0	466.4	537.2							

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

Earnings revisions

We make modest changes to our earnings forecasts in FY20 but leave FY21 and FY22 largely unchanged. The near term upgrade reflects higher assumptions for both high margin log exports, and containers. The better than previously anticipated earnings affords to lift our final FY20 dividend expectation to 4.5c. The company cancelled its interim FY20 dividend in light of COVID-19 uncertainty.

Figure 1. Earnings revisions (NZ\$m)

	FY20E			FY21E			FY22E		
	Old	New	Chg	Old	New	Chg	Old	New	Chg
Log exports (JASM)	2,200	2,250	2.3%	2,650	2,650	0.0%	3,000	3,000	0.0%
Containers (TEU)	256	262	2.3%	276	279	1.0%	280	287	2.7%
Sales revenue	94.9	96.8	1.9%	104.1	104.1	0.0%	115.8	116.8	0.8%
EBITDA	35.1	36.9	5.1%	40.2	40.5	0.7%	49.1	50.1	2.1%
Underlying NPAT	17.1	18.5	8.2%	20.1	20.1	0.4%	24.1	24.6	2.0%
Underlying EPS (cents)	8.6	9.3	8.2%	10.0	10.1	0.4%	12.1	12.3	2.0%
DPS (cents)	3.0	4.5	49.5%	7.8	7.8	0.4%	9.7	9.8	1.8%

Source: 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 that industry headwinds as a result of COVID-19 disruption and economic headwinds will impact NPH's earnings through FY20. 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 cashflow 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 varieties 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).

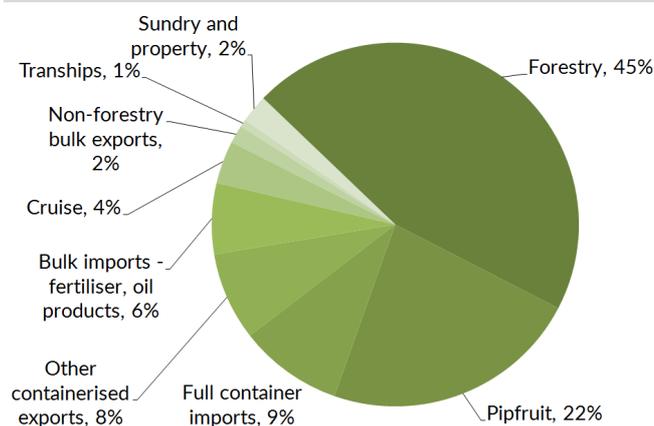
Financial structure

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

Risk factors

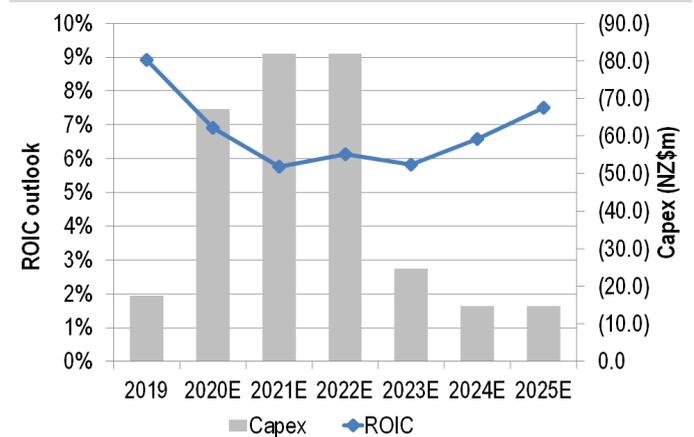
- **Industry sector risk:** Any change in the supply, or demand for NZ forestry/pipfruit could have a material impact on the Ports financial performance.
- **Competition from other ports:** Increased competition from other ports may mean that NPH loses cargo in future, particularly current contestable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

Figure 2. NPH estimated revenue mix (FY19)

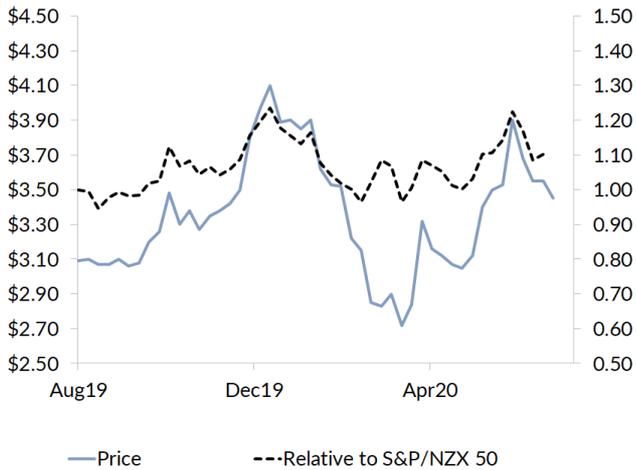


Source: Forsyth Barr analysis

Figure 3. Returns under pressure from 6 Wharf capex



Source: Forsyth Barr analysis

Figure 4. Price performance


Source: Forsyth Barr analysis

Figure 5. Substantial shareholders

Shareholder	Latest Holding
Hawke's Bay Regional Council	55.0%

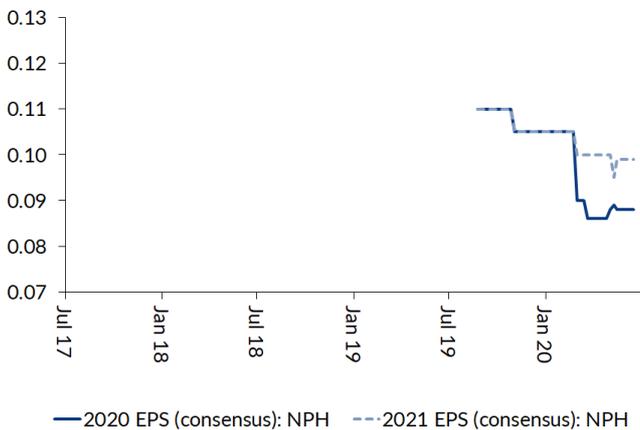
Source: NZX, Forsyth Barr analysis, NOTE: based on SSH notices only

Figure 6. International valuation comparisons

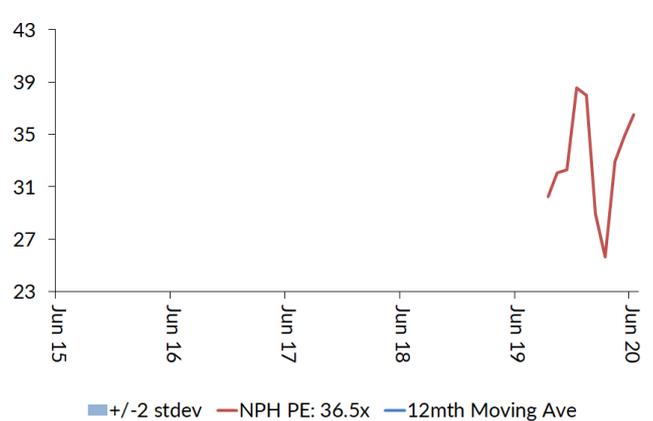
Company	Code	Price	Mkt Cap (m)	PE		EV/EBITDA		EV/EBIT		Cash Yld 2021E
				2020E	2021E	2020E	2021E	2020E	2021E	
(metrics re-weighted to reflect NPH's balance date - September)										
Napier Port	NPH NZ	NZ\$3.45	NZ\$690	37.2x	34.3x	17.9x	16.3x	27.5x	24.7x	2.3%
PORT OF TAURANGA *	POT NZ	NZ\$7.68	NZ\$5,224	>50x	49.1x	33.3x	30.6x	40.3x	36.8x	1.9%
QUBE HOLDINGS	QUB AT	A\$2.72	A\$5,123	42.0x	38.5x	24.8x	22.2x	45.6x	40.5x	1.9%
GLOBAL PORTS INV-GDR REG S	GLPR LI	US\$3.12	US\$596	11.6x	6.0x	6.1x	5.6x	7.8x	6.9x	1.5%
HAMBURGER HAFEN UND LOGISTIK	HHFA GR	€14.86	€1,081	29.3x	18.8x	6.0x	5.3x	13.1x	10.8x	3.9%
WESTSHORE TERMINALS INVESTME	WTE CN	C\$16.90	C\$1,101	8.5x	11.5x	6.0x	7.6x	6.7x	8.9x	5.1%
MITSUBISHI LOGISTICS CORP	9301 JP	¥2714.00	¥238,725	19.3x	16.4x	11.2x	10.9x	n/a	n/a	2.3%
EUROKAI KGAA	EUK2 GR	€29.00	€360	33.0x	23.5x	7.5x	7.2x	10.9x	10.0x	n/a
AUCKLAND AIRPORT *	AIA NZ	NZ\$6.08	NZ\$8,946	<0x	<0x	41.7x	68.8x	>75x	>75x	0.2%
SYDNEY AIRPORT	SYD AT	A\$5.35	A\$12,090	<0x	>50x	31.3x	25.7x	>75x	60.5x	3.0%
Compcop Average:				24.0x	23.4x	18.7x	20.4x	20.7x	24.9x	2.5%
NPH Relative:				55%	46%	-4%	-20%	33%	-1%	-9%

EV = Current Market Cap + Actual Net Debt

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

Figure 7. Consensus EPS momentum (NZ\$)


Source: Forsyth Barr analysis

Figure 8. One year forward PE (x)


Source: Forsyth Barr analysis

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