

# PGG Wrightson

## Farmer Activity Subdued

**PGG Wrightson (PGW) reaffirmed its FY20 earnings outlook at its Annual Meeting signalling operating EBITDA in excess of NZ\$30m, assuming normal trading conditions, which is consistent with our forecasts. However, 'normal trading conditions' may be optimistic given (1) subdued farmer confidence levels and (2) a tighter credit backdrop are both likely to weigh on farm investment. There are pockets of growth such as Fruited and expansion of its livestock receivables product but we believe the risk to our earnings estimates is to the downside.**

### Trading update

PGW has reiterated earlier commentary, guiding to operating EBITDA in a normal year in excess of NZ\$30m (FY20E NZ\$31m). Given the importance of the Spring trading period and the second half weighting of the Agency business, it remains too early to provide firm guidance. An update is expected at its half year result in February. We currently view risks as weighted to the downside, with headwinds from low farmer confidence, tighter lending requirements, and Government policy uncertainty.

Following the sale of the Seed & Grain business, PGW's Board continues to review its strategy. In the meantime a number of growth opportunities have been highlighted which centre on technology implementation, such as expanding its ecommerce offering, its online livestock trading platform *bidr*, and its Go products.

### Divisional outlook

- **Retail** — It's a mixed outlook for the Retail business with subdued farmer confidence likely to weigh on farm investment, however, commodity prices are largely robust and ongoing orchard development should continue to be a positive tailwind for its Fruited business. We forecast limited growth in the Retail business.
- **Water** — The Water business remains challenged, in our opinion, given depressed on farm irrigation spend. However, PGW has recently undertaken cost measures, reducing headcount and footprint, with the benefits to accrue in FY20. Additionally, its Advanced Irrigation Systems has a healthy pipeline of landscape irrigation projects.
- **Agency** — Mycoplasma Bovis concerns are likely to continue to weigh on livestock trading activity. Commodity prices remain mixed with high red meat prices offset by low wool prices. We expect to see a slight recovery in activity, assuming normal seasonal trends, with growth to be driven by PGW's livestock receivables product, Go. Additional balance sheet headroom provides capacity to increase investment in this business.

### Dividend policy reaffirmed

Following a review of its dividend policy, which has been left unchanged, PGW's board expects to pay a 1H20 dividend of "no less than 8cps", in line with our 1H20E forecast (FY20E 16cps).

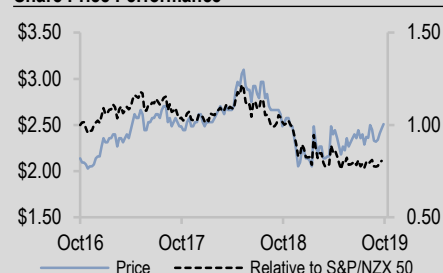
### Investment View

PGW offers investors leverage to New Zealand agri-business markets, with a particular focus on rural services. Low farmer confidence driven by a combination of political and operating uncertainty, in addition to a tightening credit outlook, is likely to weigh on sector investment in the near-term.

## RESEARCH INSIGHTS<sup>#</sup>

NZX Code	PGW
Share price	NZ\$2.51
Issued shares	75.5m
Market cap	NZ\$189m
Average daily turnover	62.1k (NZ\$144k)

### Share Price Performance



Financials: June	19A	20E	21E	22E
NPAT* (NZ\$m)	9.4	15.2	17.6	18.2
EPS* (NZc)	12.4	20.1	23.3	24.1
EPS growth* (%)	-45.3	62.0	15.8	3.5
DPS (NZc)	15.0	16.0	18.0	20.0
Imputation (%)	100	100	100	100

Valuation (x)	19A	20E	21E	22E
EV/EBITDA	6.7	3.2	6.3	6.0
EV/EBIT	10.8	4.5	8.5	8.3
PE	20.2	12.5	10.8	10.4
Price / NTA	0.5	1.2	1.2	n/a
Cash dividend yield (%)	6.0	6.4	7.2	8.0
Gross dividend yield (%)	8.3	8.9	10.0	11.1

\*Historic and forecast numbers based on underlying profits

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<sup>#</sup>Forsyth Barr **RESEARCH INSIGHTS** targets selected smaller cap stocks or those under transitional coverage and focuses on qualitative rather than quantitative assessments. We do not provide investment ratings or target prices on these stocks.

**PGG Wrightson (PGW)**

Priced as at 22 Oct 2019: NZ\$2.51

June year end

**Research Insights**

Forsyth Barr Research Insights focuses on qualitative rather than quantitative assessments of an equity investment.

We do not provide valuation, target prices or investment ratings for companies in the Research Insights series. It is targeted at selected smaller cap stocks with typically higher risk attributes, or those under transitional coverage.

Our earnings and cashflow forecasts, together with key valuation and ratios provided on this page should assist investors in determining the relative valuation merits of the company.

<b>Valuation Ratios</b>	<b>2018A</b>	<b>2019A</b>	<b>2020E</b>	<b>2021E</b>	<b>2022E</b>
EV/EBITDA (x)	9.5	6.7	7.1	6.3	6.0
EV/EBIT (x)	11.9	10.8	9.8	8.5	8.3
PE (x)	11.1	20.2	12.5	10.8	10.4
Price/NTA (x)	0.7	0.5	1.2	1.2	1.2
Free cash flow yield (%)	-6.6	-34.6	2.3	6.5	7.4
Net dividend yield (%)	12.0	6.0	6.4	7.2	8.0
Gross dividend yield (%)	16.6	8.3	8.9	10.0	11.1
Imputation (%)	100	100	100	100	100
Pay-out ratio (%)	132	121	80	77	83

<b>Capital Structure</b>	<b>2018A</b>	<b>2019A</b>	<b>2020E</b>	<b>2021E</b>	<b>2022E</b>
Interest cover EBIT (x)	4.0	2.5	13.6	15.7	16.7
Interest cover EBITDA (x)	5.0	4.0	18.7	21.4	22.9
Net debt/ND+E (%)	37.2	-109.1	16.7	15.9	14.9
Net debt/EBITDA (x)	4.9	n/a	1.1	0.9	0.9

<b>Profit and Loss Account (NZ\$m)</b>	<b>2018A</b>	<b>2019A</b>	<b>2020E</b>	<b>2021E</b>	<b>2022E</b>
Sales revenue	808.7	809.3	823.4	837.7	851.3
<b>Normalised EBITDA</b>	<b>34.5</b>	<b>24.4</b>	<b>31.4</b>	<b>35.5</b>	<b>36.8</b>
Depreciation and amortisation	(6.9)	(9.4)	(8.7)	(9.5)	(9.9)
<b>Normalised EBIT</b>	<b>27.6</b>	<b>15.1</b>	<b>22.7</b>	<b>26.1</b>	<b>26.9</b>
Net interest	(6.9)	(6.1)	(1.7)	(1.7)	(1.6)
Associate income	-	-	-	-	-
Tax	(3.6)	0.4	(5.9)	(6.8)	(7.1)
Minority interests	-	-	-	-	-
<b>Normalised NPAT</b>	<b>17.1</b>	<b>9.4</b>	<b>15.2</b>	<b>17.6</b>	<b>18.2</b>
Abnormals/other	(8.1)	122.4	-	-	-
<b>Reported NPAT</b>	<b>9.0</b>	<b>131.8</b>	<b>15.2</b>	<b>17.6</b>	<b>18.2</b>
Normalised EPS (cps)	22.7	12.4	20.1	23.3	24.1
DPS (cps)	30.0	15.0	16.0	18.0	20.0

<b>Key Ratios</b>	<b>2018A</b>	<b>2019A</b>	<b>2020E</b>	<b>2021E</b>	<b>2022E</b>
Return on assets (%)	3.6	2.7	6.0	6.8	6.8
Return on equity (%)	6.0	2.4	9.0	10.1	10.1
Return on funds employed (%)	5.3	8.1	8.4	9.3	9.4
EBITDA margin (%)	4.3	3.0	3.8	4.2	4.3
EBIT margin (%)	3.4	1.9	2.8	3.1	3.2
Capex to sales (%)	2.3	2.0	1.8	1.5	1.4
Capex to depreciation (%)	265	176	169	132	120

<b>Growth Rates</b>	<b>2018A</b>	<b>2019A</b>	<b>2020E</b>	<b>2021E</b>	<b>2022E</b>
Revenue (%)	6.4	0.1	1.7	1.7	1.6
EBITDA (%)	25.7	-29.2	28.6	13.1	3.6
EBIT (%)	23.4	-45.4	51.0	14.6	3.1
Normalised NPAT (%)	46.8	-45.3	62.0	15.8	3.5
Normalised EPS (%)	46.8	-45.3	62.0	15.8	3.5
Ordinary DPS (%)	-20.0	-50.0	6.7	12.5	11.1

<b>Divisional analysis</b>	<b>2018E</b>	<b>2019E</b>	<b>2020E</b>	<b>2021E</b>	<b>2022E</b>
<b>Revenue (NZ\$m)</b>					
Retail & Water	603.8	611.7	620.9	630.2	639.7
Agency	200.6	193.8	198.7	203.7	207.7
Other	4.3	3.7	3.8	3.8	3.9
<b>Revenue</b>	<b>808.7</b>	<b>809.3</b>	<b>823.4</b>	<b>837.7</b>	<b>851.3</b>
<b>Revenue growth (%)</b>					
Retail & Water	7.4	1.3	1.5	1.5	1.5
Agency	1.8	(3.4)	2.5	2.5	2.0
<b>Revenue</b>	<b>6.4</b>	<b>0.1</b>	<b>1.7</b>	<b>1.7</b>	<b>1.6</b>

<b>Cash Flow (NZ\$m)</b>	<b>2018A</b>	<b>2019A</b>	<b>2020E</b>	<b>2021E</b>	<b>2022E</b>
<b>EBITDA</b>	<b>34.5</b>	<b>24.4</b>	<b>31.4</b>	<b>35.5</b>	<b>36.8</b>
Working capital change	(62.3)	(31.0)	(4.9)	(2.2)	(2.1)
Interest & tax paid	(15.8)	(16.9)	(7.6)	(8.5)	(8.7)
Other	49.3	(25.5)	-	-	-
<b>Operating cash flow</b>	<b>5.8</b>	<b>(49.0)</b>	<b>19.0</b>	<b>24.8</b>	<b>26.0</b>
Capital expenditure	(18.3)	(16.5)	(14.7)	(12.5)	(11.9)
(Acquisitions)/divestments	3.5	402.6	-	-	-
Other	(0.8)	-	-	-	-
<b>Funding available/(required)</b>	<b>(9.8)</b>	<b>337.1</b>	<b>4.3</b>	<b>12.3</b>	<b>14.1</b>
Dividends paid	(17.9)	(16.5)	(11.6)	(11.6)	(12.7)
Equity raised/(returned)	-	-	(234.0)	-	-
<b>Increase/(decrease) in net debt</b>	<b>27.7</b>	<b>(320.6)</b>	<b>241.3</b>	<b>(0.7)</b>	<b>(1.4)</b>

<b>EBITDA (NZ\$m)</b>	<b>2018E</b>	<b>2019E</b>	<b>2020E</b>	<b>2021E</b>	<b>2022E</b>
Retail & Water	23.8	19.6	21.7	22.7	23.7
Agency	20.1	15.4	17.9	20.4	20.8
Corporate Overhead	(9.4)	(10.6)	(8.2)	(7.5)	(7.6)
<b>Operating EBITDA</b>	<b>34.5</b>	<b>24.4</b>	<b>31.4</b>	<b>35.5</b>	<b>36.8</b>
<b>EBITDA margins (%)</b>					
Retail & Water	3.9	3.2	3.5	3.6	3.7
Agency	10.0	7.9	9.0	10.0	10.0
<b>EBITDA margin</b>	<b>4.3</b>	<b>3.0</b>	<b>3.8</b>	<b>4.2</b>	<b>4.3</b>

<b>Balance Sheet (NZ\$m)</b>	<b>2018A</b>	<b>2019A</b>	<b>2020E</b>	<b>2021E</b>	<b>2022E</b>
Working capital	303.3	123.7	128.6	130.8	132.9
Fixed assets	124.2	44.7	50.7	53.7	55.7
Intangibles	13.0	14.6	14.6	14.6	14.6
Other assets	40.1	16.1	16.1	16.1	16.1
<b>Total funds employed</b>	<b>480.6</b>	<b>199.2</b>	<b>210.0</b>	<b>215.3</b>	<b>219.4</b>
Net debt/(cash)	169.1	(207.8)	33.5	32.8	31.4
Other non current liabilities	24.1	8.7	8.7	8.7	8.7
Shareholder's funds	285.0	398.3	167.8	173.7	179.3
Minority interests	2.5	-	-	-	-
<b>Total funding sources</b>	<b>480.6</b>	<b>199.2</b>	<b>210.0</b>	<b>215.3</b>	<b>219.4</b>

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

## Investment summary

PGG Wrightson (PGW) offers investors broad leverage to the New Zealand agri-business markets, with a particular focus on rural services. A focus on its core farmer oriented businesses in recent years, including the divestment of non-core businesses, and investment into irrigation assets, has helped realign the company's strategy to its key strengths. This has resulted in earnings growth and lower volatility.

### Business quality

- **Leading NZ rural services company:** PGW has a long history servicing the New Zealand agriculture sector.

### Earnings and cash flow outlook

- **Sheep & Beef prices:** PGW's roots are ingrained in the Sheep & Beef farming communities, and as such its rural supplies and servicing businesses are driven by the success of its sheep and beef farmer clients.
- **Dairy prices:** The dairy pay-out and dairy farmer earnings are linked to global dairy prices. Dairy-related leverage is material, particularly given the company is increasing market share in rural servicing of dairy.
- **Seasonality of earnings:** PGW's Retail and Water earnings are highly seasonal and weighted to the first half, ahead of key milking and growing periods. Agency earnings are also seasonal, although second half weighted. Climatic conditions can have a reasonable impact on seasonal earnings.

### Financial structure

- **Gearing:** Following the sale of its Seed & Grain business and subsequent capital distribution PGW's balance sheet is now more conservatively geared.
- **Strategic review:** PGW's strategic review of its business, capital structure, shareholding structure, and growth opportunities continues. Management highlighted irrigation and other rural services acquisitive options as a possibility.

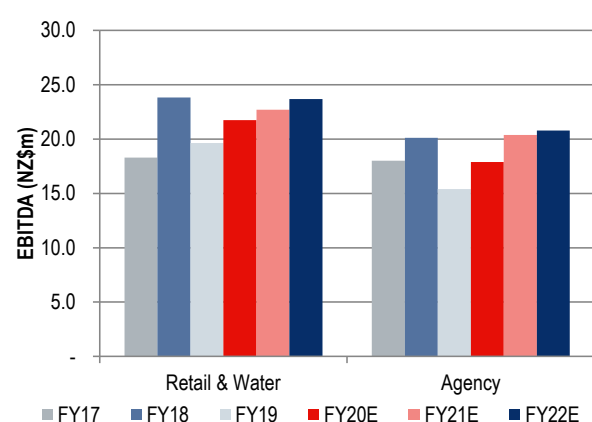
### Risk factors

- **Sustained commodity price collapse:** Dairy prices have recovered; however, risk of commodity price swings for Sheep, Beef, Dairy, and Wool can affect earnings.
- **Competition is robust:** PGW competes heavily against two rural servicing companies, FarmSource (Fonterra-owned) and Farmlands.

### Company description

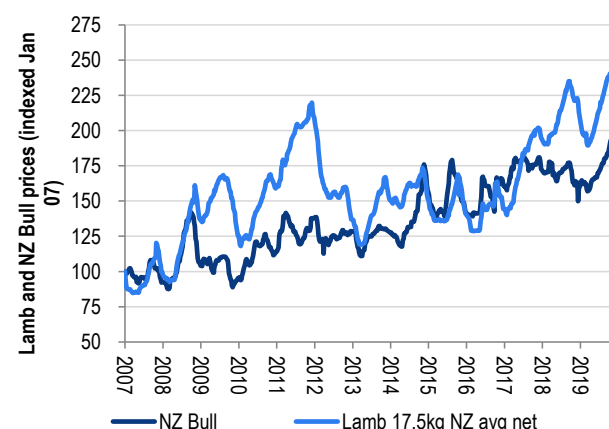
PGW is the leading provider of agricultural services in New Zealand. The business is divided into two segments; Retail & Water and Agency. Retail operations include the PGG Wrightson and Fruited retail networks, with the Water business targeted at irrigation projects. Agency is primarily driven its Livestock trading business, although it also includes contributions from Wool, Real Estate, and Insurance.

Figure 1. EBITDA contribution (NZ\$m) ex-overheads



Source: PGW, Forsyth Barr analysis

Figure 2. Sheep and beef price indicators



Source: AgriHQ, Forsyth Barr analysis

**Figure 3. Substantial Shareholders**

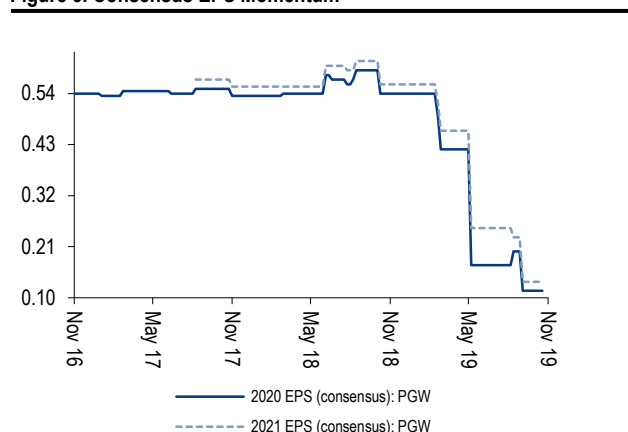
Shareholder	Latest Holding
Agria (Singapore) Pte	44.3%
H&G	6.4%

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

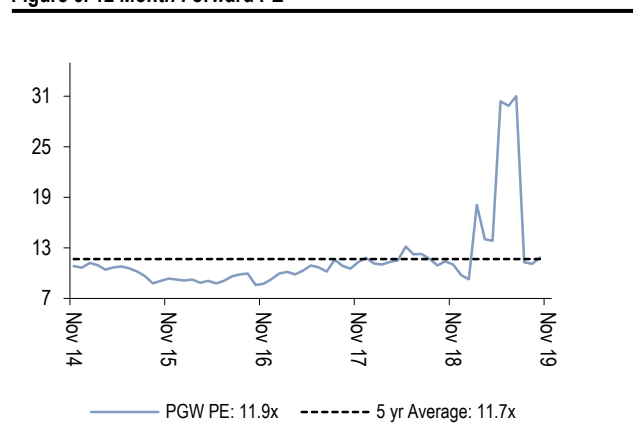
**Figure 4. International Compcos**

Company	Code	Price	Mkt Cap	PE	EV/EBITDA	EV/EBIT	Cash D/Yld
			(m)	2020E	2021E	2020E	2021E
<i>(metrics re-weighted to reflect PGW's balance date - June)</i>							
<b>PGG Wrightson</b>	<b>PGW NZ</b>	<b>NZ\$2.51</b>	<b>NZ\$189</b>	<b>12.5x</b>	<b>10.8x</b>	<b>&lt;0x</b>	<b>&lt;0x</b>
Elders	ELD AT	A\$6.08	A\$861	10.9x	9.3x	10.8x	8.8x
GrainCorp	GNC AT	A\$7.62	A\$1,744	15.0x	21.8x	19.1x	12.0x
Ridley Corp	RIC AT	A\$1.06	A\$330	15.8x	13.9x	7.8x	6.8x
Ruralco Holdings	RHL AT	A\$4.40	A\$469	15.2x	14.3x	8.4x	8.0x
<b>Compcos Average:</b>				<b>14.2x</b>	<b>14.8x</b>	<b>11.5x</b>	<b>8.9x</b>
<b>PGW Relative:</b>				<b>-12%</b>	<b>-27%</b>	<b>n/a</b>	<b>n/a</b>
<b>EV = Current Market Cap + Actual Net Debt</b>							
							<b>+97%</b>

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

**Figure 5. Consensus EPS Momentum**


Source: Forsyth Barr analysis

**Figure 6. 12 Month Forward PE**


Source: Forsyth Barr analysis

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