NEW ZEALAND EQUITY RESEARCH | INDUSTRIALS | OEM PRODUCT/COMPONENT MANUFACTURER
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Skellerup Holdings
Industrious Growth

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OUTPERFORM

Skellerup (SKL) has maintained its 1H21 earnings momentum, upgrading its FY21 NPAT guidance which at the mid-point implies growth of +31% on the prior year. Performance has been broad based with both its Industrial and Agri divisions delivering earnings growth. SKL has illustrated strong earnings momentum with a robust pipeline of further growth opportunities. On a 21x 12 month forward PE, it trades at a -12% discount to the market while offering a superior growth profile. We continue to see value and reiterate OUTPERFORM.

NZX Code	SKL
Share price	NZ$4.37
Target price	NZ$4.75
Risk rating	Medium
Issued shares	194.8m
Market cap	NZ$851m
Avg daily turnover	180.5k (NZ$575k)

Financials: Jun/	20A	21E	22E	23E
NPAT* (NZ$m)	29.1	38.1	42.1	43.8
EPS* (NZc)	14.9	19.5	21.6	22.5
EPS growth* (%)	0.0	31.0	10.5	4.1
DPS (NZc)	13.0	15.5	17.0	18.0
Imputation (%)	50	50	50	50
*Based on normalised profits				

Valuation (x)	20A	21E	22E	23E
PE	29.3	22.4	20.2	19.4
EV/EBIT	21.2	16.5	14.9	14.2
EV/EBITDA	16.3	13.4	12.4	11.9
Price / NTA	6.6	6.1	5.6	5.3
Cash div yld (%)	3.0	3.5	3.9	4.1
Gross div yld (%)	3.6	4.2	4.6	4.9

What's changed?

- **Earnings:** FY21E NPAT up +1.6% to NZ$38.1m. We also upgrade our FY22 and FY23 NPAT estimates +2.8% and +2.3% respectively to NZ$42.1m and NZ$43.8m.
- **Target price:** We lift our target price +25cps (+5.6%) to NZ$4.75 on the back of earnings changes and multiple expansion.

FY21 guidance upgraded — Margin profile maintained

SKL delivered its third iteration of FY21 guidance and a third upgrade to market expectations, lifting its NPAT guidance range +8.6% at the mid-pont to NZ$37m to NZ$39m (previously NZ$33m to NZ$37m). Encouragingly, margin expansion achieved in 1H21 has been largely maintained, despite rising cost pressures, and provides further confidence in its sustainability. We expect to see continued strong organic growth in FY22, with commentary suggesting the pipeline of both near and medium-term growth opportunities is healthy. In addition, SKL's healthy balance sheet provides optionality to pursue bolt-on acquisitions. Acquisitive growth is a key lever for SKL and an area it has had recent success in. We suspect this has been impeded by border restrictions, although expect it to return as these restrictions ease.

Firing on all cylinders

- **Industrials** — Key drivers include construction revenue in Australia and global marine foam, which have maintained positive momentum from 1H21. In addition, potable water sales have recovered following a weaker prior period, particularly in the USA .
- **Agri** — Its dairy business has performed well in what is traditionally a seasonal low, as it continues to gain traction in international markets. We believe it is well positioned for a strong Q4 dairy performance and a seasonal high, backed by a favourable backdrop for dairy farmers.

Supply chain congestion a challenge although largely transitional with risks around earnings timing

Supply chain congestion and rising commodity prices have increased cost pressures and created some risks to earnings guidance. However, SKL has illustrated an ability to navigate input cost changes where it has stronger pricing ability, while delays are largely earnings recognition issues, pushing growth into 1H22.

Skellerup Holdings (SKL)

Priced as at 19 Apr 2021 (NZ$)	4.37

12-month target price (NZ$)*	**4.75**
Expected share price return	8.7%
Net dividend yield	3.8%
Estimated 12-month return	12.5%

Spot valuations (NZ$)	
1. DCF	4.31
2. Relative valuation	4.65
3. n/a	n/a

Key WACC assumptions	
Risk free rate	2.30%
Equity beta	1.10
WACC	7.3%
Terminal growth	1.5%

DCF valuation summary (NZ$m)	
Total firm value	839
(Net debt)/cash	(29)
Less: Capitalised operating leases	(68)
Value of equity	743

Profit and Loss Account (NZ$m)	**2019A**	**2020A**	**2021E**	**2022E**	**2023E**
Sales revenue	245.8	251.4	270.2	286.4	299.7
Normalised EBITDA	**48.9**	**55.3**	**66.5**	**71.7**	**74.7**
Depreciation and amortisation	(7.1)	(12.8)	(12.3)	(12.2)	(12.0)
Normalised EBIT	**41.8**	**42.5**	**54.2**	**59.5**	**62.6**
Net interest	(1.8)	(2.6)	(2.0)	(1.9)	(1.8)
Associate income	0.0	(0.1)	0	0	0
Tax	(11.0)	(10.8)	(14.1)	(15.5)	(17.0)
Minority interests	0	0	0	0	0
Normalised NPAT	**29.1**	**29.1**	**38.1**	**42.1**	**43.8**
Abnormals/other	0	0	0	0	0
Reported NPAT	**29.1**	**29.1**	**38.1**	**42.1**	**43.8**
Normalised EPS (cps)	14.9	14.9	19.5	21.6	22.5
DPS (cps)	13.0	13.0	15.5	17.0	18.0

Growth Rates	**2019A**	**2020A**	**2021E**	**2022E**	**2023E**
Revenue (%)	2.2	2.3	7.5	6.0	4.6
EBITDA (%)	3.6	12.9	20.3	7.8	4.2
EBIT (%)	5.1	1.6	27.5	9.9	5.3
Normalised NPAT (%)	6.5	0.0	31.0	10.5	4.1
Normalised EPS (%)	5.5	0.0	31.0	10.5	4.1
Ordinary DPS (%)	18.2	0.0	19.2	9.7	5.9

Cash Flow (NZ$m)	**2019A**	**2020A**	**2021E**	**2022E**	**2023E**
EBITDA	**48.9**	**55.3**	**66.5**	**71.7**	**74.7**
Working capital change	(8.5)	4.8	(1.4)	(4.3)	(3.6)
Interest & tax paid	(11.5)	(12.1)	(16.1)	(17.4)	(18.8)
Other	0	0	0	0	0
Operating cash flow	**28.9**	**48.0**	**49.0**	**49.9**	**52.2**
Capital expenditure	(4.6)	(4.4)	(5.0)	(5.1)	(5.2)
(Acquisitions)/divestments	(8.2)	(5.8)	0	0	0
Other	0	(4.7)	(4.7)	(4.8)	(4.9)
Funding available/(required)	**16.2**	**33.2**	**39.3**	**40.1**	**42.1**
Dividends paid	(24.3)	(25.3)	(27.3)	(31.2)	(34.1)
Equity raised/(returned)	2.4	0	0	0	0
(Increase)/decrease in net debt	**(5.7)**	**7.9**	**12.1**	**8.9**	**8.0**

Balance Sheet (NZ$m)	**2019A**	**2020A**	**2021E**	**2022E**	**2023E**
Working capital	76.1	73.7	75.1	79.4	83.0
Fixed assets	91.3	87.8	86.0	84.3	82.9
Intangibles	49.5	54.9	54.9	54.9	54.9
Right of use asset	0	21.8	21.8	21.8	21.8
Other assets	7.6	7.0	7.0	7.0	7.0
Total funds employed	**224.4**	**245.2**	**244.7**	**247.4**	**249.6**
Net debt/(cash)	36.6	28.5	16.4	7.5	(0.5)
Lease liability	0	17.8	20.2	20.8	21.3
Other liabilities	9.5	14.4	12.8	12.8	12.8
Shareholder's funds	178.4	184.6	195.4	206.3	216.0
Minority interests	0	0	0	0	0
Total funding sources	**224.4**	**245.2**	**244.7**	**247.4**	**249.6**

Valuation Ratios	**2019A**	**2020A**	**2021E**	**2022E**	**2023E**
EV/EBITDA (x)	18.1	16.0	13.1	12.1	11.6
EV/EBIT (x)	21.2	20.8	16.1	14.6	13.9
PE (x)	29.3	29.3	22.4	20.2	19.4
Price/NTA (x)	6.6	6.6	6.1	5.6	5.3
Free cash flow yield (%)	2.9	5.1	5.2	5.3	5.5
Net dividend yield (%)	3.0	3.0	3.5	3.9	4.1
Gross dividend yield (%)	3.6	3.6	4.2	4.6	4.9

Capital Structure	**2019A**	**2020A**	**2021E**	**2022E**	**2023E**
Interest cover EBIT (x)	23.4	16.5	26.6	31.2	34.6
Interest cover EBITDA (x)	27.4	21.4	32.7	37.6	41.2
Net debt/ND+E (%)	17.0	13.4	7.8	3.5	-0.2
Net debt/EBITDA (x)	0.7	0.5	0.2	0.1	n/a

Key Ratios	**2019A**	**2020A**	**2021E**	**2022E**	**2023E**
Return on assets (%)	16.3	15.0	18.9	20.5	21.3
Return on equity (%)	16.3	15.7	19.5	20.4	20.3
Return on funds employed (%)	14.5	14.5	18.6	20.4	21.0
EBITDA margin (%)	19.9	22.0	24.6	25.0	24.9
EBIT margin (%)	17.0	16.9	20.0	20.8	20.9
Capex to sales (%)	1.9	1.7	1.9	1.8	1.7
Capex to depreciation (%)	64	34	41	42	43
Imputation (%)	50	50	50	50	50
Pay-out ratio (%)	87	87	79	79	80

Operating Performance	**2019A**	**2020A**	**2021E**	**2022E**	**2023E**
Revenue by segment					
Agri	88.8	93.6	103.0	109.1	113.5
Industrial	157.2	157.9	167.4	177.5	186.3
Total revenue (incl. eliminations)	**245.8**	**251.4**	**270.2**	**286.4**	**299.7**
EBIT by segment					
Agri	22.8	25.4	29.9	32.7	34.1
Industrial	22.9	20.9	29.3	31.1	33.1
Total EBIT (incl. overheads)	**41.8**	**42.5**	**54.2**	**59.5**	**62.6**
EBIT margin by segment					
Agri (%)	25.7	27.1	29.0	30.0	30.0
Industrial (%)	14.6	13.2	17.5	17.5	17.8
Total (%)	**17.0**	**16.9**	**20.0**	**20.8**	**20.9**

Earnings changes

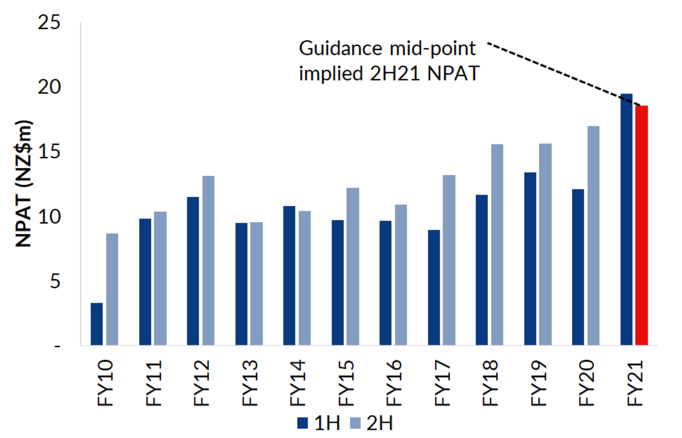
We lift our FY21 NPAT assumption +1.6% to NZ$38m, the mid-point of the updated guidance range (NZ$37m to NZ$39m), driven by an increase to our 2H21 Industrial margin assumption. We also lift FY22 and FY23 NPAT estimates +2.8% and +2.3% respectively to NZ$42.1m and NZ$43.8m, driven by 1) slightly higher margin assumptions, and 2) growth pipeline commentary.

Figure 1. Forecast changes (NZ$m)

	FY21E			FY22E			FY23E		
	old	new	% chg	old	new	% chg	old	new	% chg
Revenue	270.2	270.2	-	282.9	286.4	1.3%	295.1	299.7	1.6%
EBIT	53.3	54.2	1.6%	57.9	59.5	2.7%	61.3	62.6	2.2%
Normalised NPAT	**37.5**	**38.1**	**1.6%**	**40.9**	**42.1**	**2.8%**	**42.8**	**43.8**	**2.3%**
EPS (cps)	19.2	19.5	1.6%	21.0	21.6	2.8%	22.0	22.5	2.3%
DPS (cps)	15.5	15.5	-	16.5	17.0	3.0%	18.0	18.0	-

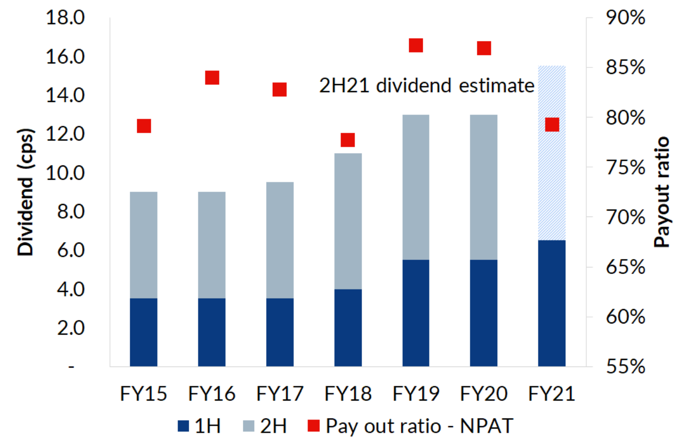
Source: Forsyth Barr analysis

Figure 2. Group NPAT seasonality



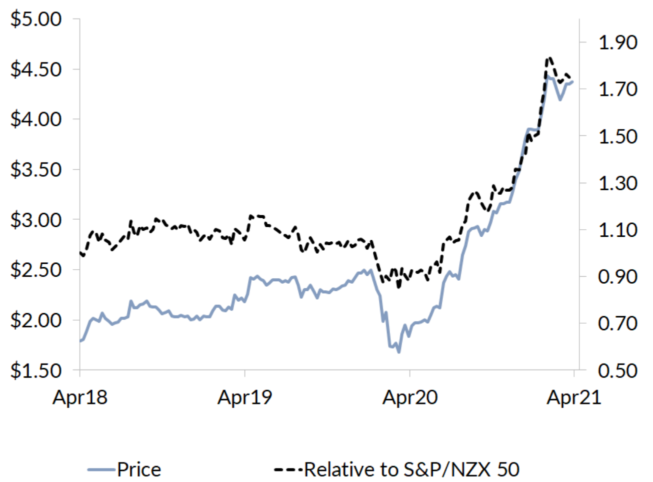
Source: Company reports, Forsyth Barr analysis

Figure 3. Track record of dividend growth



Source: Company reports, Forsyth Barr analysis

Figure 4. Price performance



Source: Forsyth Barr analysis

Figure 5. Substantial shareholders

Shareholder	Latest Holding
Sir Selwyn John Cushing	6.5%
Forsyth Barr Investment Management	5.0%

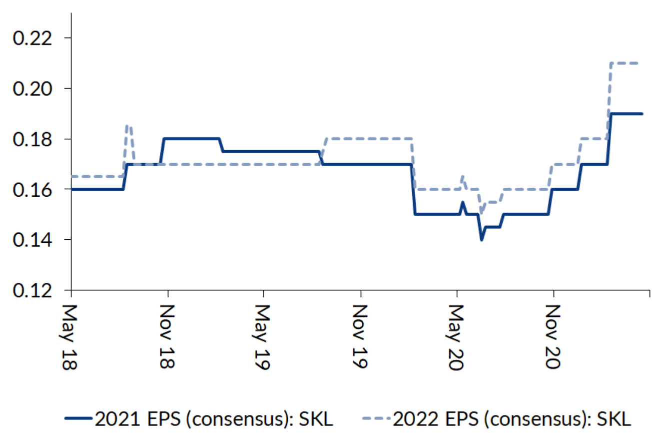
Source: NZX, Forsyth Barr analysis, NOTE: based on SPH notices only

Figure 6. International valuation comparisons

Company	Code	Price	Mkt Cap	PE		EV/EBITDA		EV/EBIT		Cash Yld
(metrics re-weighted to reflect SKL's balance date - June)			(m)	2021E	2022E	2021E	2022E	2021E	2022E	2022E
Skellerup Holdings	**SKL NZ**	**NZ$4.37**	**NZ$851**	**22.4x**	**20.2x**	**13.2x**	**12.3x**	**16.2x**	**14.8x**	**3.9%**
AVON RUBBER PLC	AVON LN	£35.82	£1,111	27.5x	27.8x	25.5x	14.5x	61.6x	19.4x	1.3%
TRELLEBORG AB-B SHS	TRELB SS	kr232.50	kr63,024	20.3x	16.6x	12.9x	10.8x	19.1x	14.4x	2.4%
PGG WRIGHTSON *	PGW NZ	NZ$3.44	NZ$260	15.0x	14.8x	5.1x	5.1x	9.9x	9.8x	5.8%
NUTRIEN	NTR CN	US$70.05	US$39,925	56.3x	25.3x	14.3x	10.8x	39.1x	19.2x	2.7%
METRO PERFORMANCE GLASS	MPG NZ	NZ$0.38	NZ$70	7.1x	8.1x	4.6x	5.1x	9.1x	10.5x	1.2%
STEEL & TUBE HOLDINGS *	STU NZ	NZ$1.07	NZ$178	26.8x	19.6x	5.5x	5.5x	11.6x	10.6x	3.7%
			Compco Average:	**25.5x**	**18.7x**	**11.3x**	**8.6x**	**25.1x**	**14.0x**	**2.9%**
EV = Current Market Cap + Actual Net Debt			**SKL Relative:**	**-12%**	**8%**	**17%**	**42%**	**-35%**	**6%**	**36%**

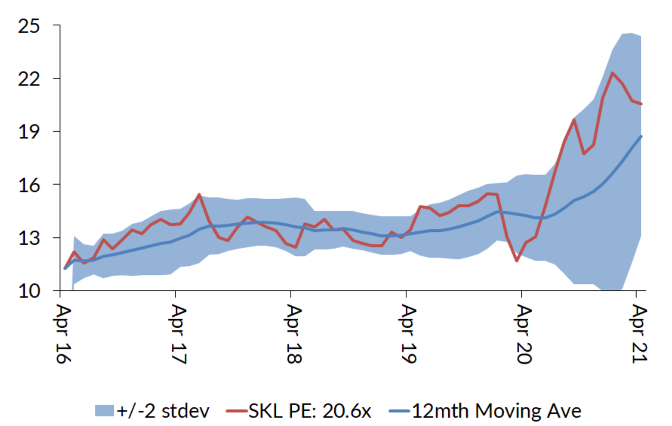
Source: *Forsyth Barr analysis, Bloomberg Consensus, Compco metrics re-weighted to reflect headline (SKL) companies fiscal year end

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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