

Tilt Renewables

For Sale – One Careful Owner, Great Prospects

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NEUTRAL 

Almost a year to the day after Tilt Renewables (TLT) announced the sale of Snowtown 2, Infratil has announced a strategic review of TLT that may result in the sale of the whole business. Following several unsolicited enquiries, IFT has decided to test the market. Given the interest in renewable electricity assets and IFT's capital position, the chances of a sale are better than 50%, in our view. We expect IFT would require a price above NZ\$5.00 to entice them to sell, and our analysis suggests that should be achievable. We have lifted our target price by +NZ\$1.00 to NZ\$5.00, the bottom of our estimated NZ\$5.00 to NZ\$6.50 sales price range as a sale is not guaranteed and TLT is an illiquid stock. Following the strong share price reaction to the strategic review, we retain our NEUTRAL rating.

NZX Code	TLT	Financials: Mar/	20A	21E	22E	23E	Valuation (x)	20A	21E	22E	23E
Share price	NZ\$4.55	NPAT* (NZ\$m)	49.8	52.8	61.7	63.1	PE	42.9	32.4	27.7	27.1
Target price	NZ\$5.00	EPS* (NZc)	10.6	14.0	16.4	16.8	EV/EBIT	37.1	73.9	n/a	n/a
Risk rating	Low	EPS growth* (%)	-32.6	32.4	16.9	2.2	EV/EBITDA	14.2	21.8	18.2	18.6
Issued shares	376.2m	DPS (NZc)	0.0	0.0	0.0	0.0	Price / NTA	1.8	1.6	1.6	1.7
Market cap	NZ\$1,712m	Imputation (%)	0	0	0	0	Cash div yld (%)	0.0	0.0	0.0	0.0
Avg daily turnover	43.0k (NZ\$146k)	*Based on normalised profits					Gross div yld (%)	0.0	0.0	0.0	0.0

What's changed?

- **Target price:** Increased +NZ\$1.00 to NZ\$5.00

What could TLT sell for? Thinking about cost of equity, Snowtown 2 transaction and MCY/MEL trading multiples

We are of the view NZ\$5.00 is a minimum. We have considered three approaches all of which support that as a minimum sales price.

Implied cost of equity not unreasonable: Our TLT DCF value is NZ\$3.66, but that assumes nothing for development, assumes a cost of capital of 5.5% which includes a 0.25% liquidity discount and a risk free rate of 1.3% (vs. ~1.0% currently). To achieve an NZ\$5.00 DCF value (and still assume nothing for development upside), you have to assume a ~5.7% cost of equity. In an environment where MCY and MEL are trading on sub-4.0% gross dividend yields, that is not a difficult assumption for a potential acquirer.

Snowtown 2 sales multiple supports NZ\$5.63 price: Last year, TLT sold Snowtown 2 on a EV/EBITDAF multiple of 15.9x, which is a +5% premium to the average CEN/MCY/MEL EV/EBITDA multiple at the time. Applying the same +5% premium to the current FY22 CEN/MCY/MEL EV/EBITDAF multiple, derives a TLT value of NZ\$5.63.

Renewable electricity multiples support NZ\$5.00+ price: 100% renewable electricity generators MCY & MEL are trading on record highs, aided by their attractive ESG credentials. TLT ticks the same boxes and using those businesses as compcos derives a multiple price between NZ\$5.00 and NZ\$6.50 (rounded to nearest 10cps).

Who could buy it?

There appears to be no shortage of buyers of renewable electricity assets in Australia, ranging from wealth funds to asset owner/operators, both Australian and further afield. Snowtown 2 was sold to investment funds, whereas the most recent transaction of listed wind developer/operator, Infigen (IFN) was sold to Spanish generator/retailer Iberdrola. IFN sold on a +64% premium to its pre-takeover premium and an Asian renewables consortium were the first bidders, highlighting the price discovery power of a sales process.

Tilt Renewables Limited (TLT)

Priced as at 07 Dec 2020 (NZ\$)						4.55					
12-month target price (NZ\$)*						5.00	Spot valuations (NZ\$)				
Expected share price return						9.9%	1. DCF	3.66			
Net dividend yield						0.0%	2. Multiple	3.82			
Estimated 12-month return						9.9%	3. n/a	n/a			
Key WACC assumptions						DCF valuation summary (NZ\$m)					
Risk free rate						1.30%	Total firm value	1,534			
Equity beta						0.86	(Net debt)/cash	(157)			
WACC						5.5%	Less: Capitalised operating leases				
Terminal growth						1.5%	Value of equity	1,377			
Profit and Loss Account (A\$m)						Valuation Ratios					
Sales revenue	2019A	2020A	2021E	2022E	2023E	2019A	2020A	2021E	2022E	2023E	
Normalised EBITDA	193.3	170.2	135.2	183.2	183.1	EV/EBITDA (x)	20.2	18.1	27.8	23.7	24.4
Depreciation and amortisation	(83.6)	(72.5)	(52.0)	(91.3)	(88.7)	EV/EBIT (x)	53.2	47.3	94.6	>100x	>100x
Normalised EBIT	51.2	45.0	21.7	11.4	12.5	PE (x)	28.9	42.9	32.4	27.7	27.1
Net interest	(30.1)	(46.2)	(13.1)	(16.8)	(12.5)	Price/NTA (x)	3.1	1.8	1.6	1.6	1.7
Other	(2.0)	(8.5)	9.7	0	0	Free cash flow yield (%)	4.7	2.6	1.2	5.1	5.1
Tax	(6.9)	(4.7)	(12.3)	1.6	0.0	Net dividend yield (%)	0.3	0.0	0.0	0.0	0.0
Depreciation capex adjustment	55.4	46.9	27.0	59.5	57.5	Gross dividend yield (%)	0.3	0.0	0.0	0.0	0.0
Normalised NPAT	69.0	47.4	48.6	55.7	57.5	Capital Structure					
Abnormals/other	(56.8)	431.1	(20.3)	(59.5)	(57.5)	Interest cover EBIT (x)	1.7	1.0	1.7	0.7	1.0
Reported NPAT	12.2	478.4	28.4	(3.8)	(0.0)	Interest cover EBITDA (x)	4.5	2.5	5.6	6.1	8.1
Normalised EPS (cps)	14.7	10.1	12.9	14.8	15.3	Net debt/ND+E (%)	34.6	-54.6	17.2	10.8	3.3
DPS (cps)	1.1	0	0	0	0	Net debt/EBITDA (x)	2.6	n/a	2.7	1.1	0.3
Growth Rates						Key Ratios					
Revenue (%)	2019A	2020A	2021E	2022E	2023E	2019A	2020A	2021E	2022E	2023E	
EBITDA (%)	22.4	-11.9	-20.6	35.5	0.0	Return on assets (%)	3.3	2.6	1.2	0.7	0.8
EBIT (%)	29.9	-12.8	-37.3	39.4	-1.5	Return on equity (%)	10.5	4.0	5.1	5.9	6.1
Normalised NPAT (%)	91.4	-12.2	-51.8	-47.4	9.3	Return on funds employed (%)	3.6	4.2	1.3	0.8	0.9
Normalised EPS (%)	49.0	-31.3	2.7	14.5	3.2	EBITDA margin (%)	69.7	69.0	54.5	56.1	55.3
Ordinary DPS (%)	-0.6	-31.3	28.2	14.5	3.2	EBIT margin (%)	26.5	26.4	16.0	6.2	6.8
Cash Flow (A\$m)						Operating Performance					
EBITDA	2019A	2020A	2021E	2022E	2023E	2019A	2020A	2021E	2022E	2023E	
Working capital change	134.8	117.5	73.7	102.8	101.2	Australia installed capacity (MW)	440	170	506	506	506
Interest & tax paid	0.6	39.8	(67.9)	(11.0)	(8.0)	NZ installed capacity (MW)	197	197	246	330	330
Other	(41.7)	(57.8)	(7.2)	2.3	1.7	TLT installed capacity (MW)	637	367	752	836	836
Operating cash flow	85.0	50.2	34.5	94.0	94.9	Australia wind generation (GWh)	1,395	1,170	1,242	1,771	1,771
Capital expenditure	(90.8)	(322.9)	(386.8)	(7.0)	(7.1)	NZ wind generation (GWh)	658	664	747	1,119	1,119
(Acquisitions)/divestments	0	455.0	0	0	0	TLT wind generation (GWh)	2,053	1,834	1,989	2,890	2,890
Other	0	(3.9)	(5.5)	(5.5)	(5.5)	Price assumptions					
Funding available/(required)	(5.8)	178.3	(357.8)	81.5	82.3	Australia REC price (A\$/MWh)	78.3	65.2	26.6	24.7	20.7
Dividends paid	(10.6)	0	0	0	0	SA wholesale price (A\$/MWh)	81.0	56.0	39.2	45.3	44.1
Equity raised/(returned)	259.9	(1.1)	(257.5)	0	0	VIC wholesale price (A\$/MWh)		85.8	57.4	55.7	50.7
(Increase)/decrease in net debt	243.5	177.3	(615.4)	81.5	82.3	Australia PPA price (A\$/MWh)	94.8	94.5	56.7	57.8	58.9
Balance Sheet (A\$m)						NZ PPA price (NZ\$/MWh)					
Working capital	2019A	2020A	2021E	2022E	2023E	64.8	63.7	66.8	68.5	69.6	
Fixed assets	14.3	(38.3)	11.5	14.3	14.0	Australia spot sales (GWh)	155	365	750	458	458
Intangibles	0.5	0.5	0.5	0.5	0.5	Australia PPA sales (GWh)	1,239	805	491	1,313	1,313
Right of use asset	0	13.4	124.5	124.5	124.5	Australia spot revenue (A\$m)	34	53	36	22	21
Other assets	114.3	9.0	115.6	115.6	115.6	Australia PPA revenue (A\$m)	117	76	28	76	77
Total funds employed	1,195.9	985.2	1,453.3	1,380.7	1,307.7	Australia revenue (A\$m)	151	129	88	113	111
Net debt/(cash)	346.4	(417.9)	196.4	114.9	32.7	NZ revenue (A\$m)	42	42	47	70	72
Lease liability	22.9	125.5	129.2	129.2	129.2	Australia EBITDAF (A\$m)	109	93	46	57	54
Other liabilities	170.6	94.3	179.6	192.2	201.5	NZ EBITDAF (A\$m)	25	24	28	46	47
Shareholder's funds	656.0	1,183.3	948.2	944.4	944.4						
Minority interests	0	0	0	0	0						
Total funding sources	1,195.9	985.2	1,453.3	1,380.7	1,307.7						

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

Cost of capital analysis

Figure 1. TLT cost of capital sensitivity

Cost of equity	4.5%	5.0%	5.5%	6.0%	6.5%	7.0%
Cost of capital	3.6%	4.0%	4.3%	4.6%	5.0%	5.3%
DCF value (NZ\$/share)	\$6.82	\$5.92	\$5.23	\$4.69	\$4.25	\$3.88

Source: Forsyth Barr analysis

Figure 2. Notes on cost of capital sensitivity

- Our current TLT DCF of NZ\$3.66 assumes a cost of capital of 5.5%, inclusive of 0.25% liquidity discount and 1.3% risk free rate.
- Our sensitivity analysis removes the liquidity discount and assumes a risk free rate of 1.0%.

Snowtown 2 comparator

Figure 3. TLT on revised Snowtown 2 multiple

Snowtown 2 sale EV/EBITDA	15.9
December 2019 MCY, MEL & CEN EV/EBITDA	15.2
Snowtown 2 premium	5%
FY22E MCY, MEL and CEN average	20.1
Implied multiple using 5% premium	21.0
Implied TLT EV (NZ\$m)	2,276
Equity value (NZ\$m)	2,119
Implied TLT price (NZ\$/share)	\$5.63

Source: Forsyth Barr analysis

Figure 4. Snowtown 2 sale completed on 15.9x EV/EBITDA

Reasons for a higher multiple

- Inclusion of TLT development pipeline
- Interest rates have declined over the past year
- Increased interest in renewables
- Renewable energy certificate prices up +\$A5 to +\$A10/MWh

Reasons for a lower multiple

- ASX futures price down -\$A15 to -\$A20/MWh over the past year

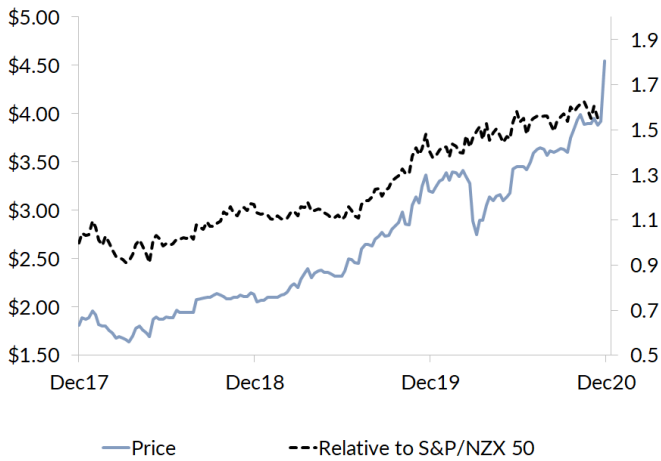
Source: Forsyth Barr analysis

Compco analysis

Figure 5. TLT on MCY/MCY multiples

	Trading multiples		TLT FY22 earnings (A\$m)	Equity value/share	
	MCY (x)	MEL (x)		MCY NZ\$	MEL NZ\$
EBITDAF	19.0	25.8	103	\$4.92	\$6.87
EBITDAF less capex	22.4	28.2	88	\$4.95	\$6.38
Adjusted NPAT	31.9	40.8	56	\$5.00	\$6.39
Average				\$4.96	\$6.55

Source: Forsyth Barr analysis

Figure 6. Price performance


Source: Forsyth Barr analysis

Figure 7. Substantial shareholders

Shareholder	Latest Holding
Infratil	65.3%
Mercury NZ Ltd	20.0%

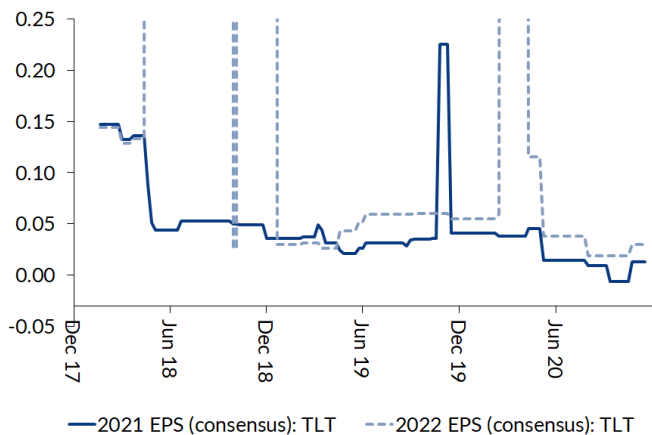
Source: NZX, Forsyth Barr analysis, NOTE: based on SPH notices only

Figure 8. International valuation comparisons

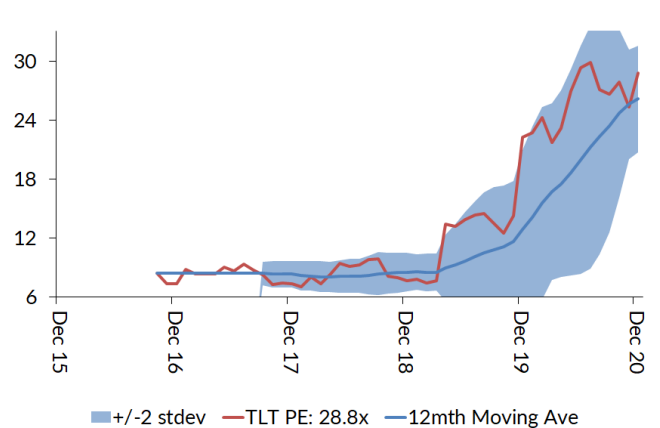
Company	Code	Price	Mkt Cap (m)	PE		EV/EBITDA		EV/EBIT		Cash Yld 2022E
				2021E	2022E	2021E	2022E	2021E	2022E	
Tilt Renewables	TLT NZ	NZ\$4.55	NZ\$1,712	32.4x	27.7x	16.0x	11.2x	54.4x	>75x	0.0%
TRUSTPOWER *	TPW NZ	NZ\$7.42	NZ\$2,322	27.8x	29.2x	15.3x	15.5x	19.9x	20.5x	4.0%
CONTACT ENERGY *	CEN NZ	NZ\$8.02	NZ\$5,763	23.2x	27.3x	14.8x	16.5x	31.6x	38.4x	4.0%
GENESIS ENERGY *	GNE NZ	NZ\$3.40	NZ\$3,548	19.8x	18.8x	12.3x	12.3x	27.1x	28.1x	4.1%
MERIDIAN ENERGY *	MEL NZ	NZ\$6.50	NZ\$16,657	36.2x	42.0x	23.1x	26.2x	38.0x	46.6x	2.6%
MERCURY *	MCY NZ	NZ\$6.40	NZ\$8,719	34.1x	34.8x	19.9x	19.9x	35.3x	36.7x	2.7%
INFIGEN ENERGY	IFN AT	A\$0.93	A\$903	n/a	n/a	9.8x	n/a	19.0x	n/a	n/a
Compcop Average:				28.2x	30.4x	15.9x	18.1x	28.5x	34.1x	3.5%
TLT Relative:				15%	-9%	1%	-38%	91%	n/a	-100%

EV = Current Market Cap + Actual Net Debt

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

Figure 9. Consensus EPS momentum (NZ\$)


Source: Forsyth Barr analysis

Figure 10. One year forward PE (x)


Source: Forsyth Barr analysis

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