

Z Energy

More Small Steps — September 2020 Volumes

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OUTPERFORM

Z Energy (ZEL) reported strong September 2020 sales volumes, up +5% on September 2019 (excluding jet and marine volumes) and +14% on August 2020. One of the most encouraging aspects is that all of the petrol and diesel markets had volume increases. Nevertheless, in our view ZEL needs several more months to demonstrate to the market it has turned the corner. ZEL remains a long-term value play. We retain our OUTPERFORM rating and an NZ\$4.35 target price.

NZX Code	ZEL	Financials: Mar/	20A	21E	22E	23E	Valuation (x)	20A	21E	22E	23E
Share price	NZ\$2.74	NPAT* (NZ\$m)	102.2	33.3	97.6	120.4	PE	10.7	42.8	14.6	11.8
Target price	NZ\$4.35	EPS* (NZc)	25.6	6.4	18.8	23.1	EV/EBIT	11.4	25.3	12.4	10.5
Risk rating	Medium	EPS growth* (%)	-47.8	-74.9	n/a	23.4	EV/EBITDA	6.3	9.5	6.8	6.3
Issued shares	520.1m	DPS (NZc)	16.5	0.0	25.0	25.0	Price / NTA	n/a	6.0	4.3	4.0
Market cap	NZ\$1,425m	Imputation (%)	100	100	100	100	Cash div yld (%)	6.0	0.0	9.1	9.1
Avg daily turnover	1,151k (NZ\$3,891k)	*Based on normalised profits					Gross div yld (%)	8.4	0.0	12.7	12.7

Strong sales volumes with all key categories performing well

Total September 2020 ZEL volumes, (excluding severely COVID-19 impacted jet & marine volumes) were up +5% on the pcp, with the increase in diesel volumes the stand-out feature. Retail diesel volumes were up +9%, due to strong small/medium enterprise volume growth, and commercial diesel volumes were up +13% due to a significant contract win. Petrol volumes were flat overall, although given Auckland was at Alert Level 2/2.5 for the whole month, we see this as a positive outcome. With August 2020 impacted by the increased Alert Level, September 2020 volumes compare well, with all fuel categories, except marine, up between +8% and +19%.

2Q21 retail volumes were -2% lower than 2Q20 due to the Auckland move to Alert Level 3, but commercial volumes were up +7%. ZEL's 2Q21 volumes were better than expected across most product categories. Retail volumes were +1% higher than forecast and commercial diesel volumes +4% better.

MBIE importer margins steady through September and remain ahead of the lows of 2019

MBIE importer margins were steady in September 2020. The blended petrol/diesel margin was ~28.5cpl, +1.5cpl up on August and +3.6cpl higher than September 2019 which was the second worst month in 2019 behind October.

Minor lift to forecast 1H21 and FY21 earnings

We have lifted our 1H21 and FY21 EBITDAF forecast +NZ\$2m to NZ\$93m and NZ\$241m respectively, due to the better than expected September 2020 volumes. The better than expected volumes were the driver of the forecast uplift — we have made no changes to our margin assumptions.

ZEL is reporting its 1H21 result on Wednesday, 4 November, and our 1H22 EBITDAF forecast of NZ\$93m is in the middle of ZEL's NZ\$85m to NZ\$100m 1H21 guidance range. In our view, ZEL still has plenty of work to do to get investors back onside. The 1H21 result will be an important milestone with a key focus being 2H21 guidance — delivering a 2H21 result in line with, or better than, current market expectations will be critical if ZEL is to regain market confidence. However, making that goal more challenging is the refinery which is impacting its competitiveness in the retail market. The refinery's move to a simplified mode (in essence cutting production capacity) is not helpful to ZEL as it increases the break-even gross refining margin.

Z Energy (ZEL)

Priced as at 12 Oct 2020 (NZ\$) **2.74**

12-month target price (NZ\$)*	4.35
Expected share price return	58.8%
Net dividend yield	5.3%
Estimated 12-month return	64.1%

Key WACC assumptions	
Risk free rate	1.30%
Equity beta	0.88
WACC	5.8%
Terminal growth	-5.0%

Spot valuations (NZ\$)	
1. DCF	5.07
2. Dividend Yield	3.71
3. Market Multiple	4.00

DCF valuation summary (NZ\$m)	
Total firm value	3,368
(Net debt)/cash	(733)
Less: Capitalised operating leases	0
Value of equity	2,635

Profit and Loss Account (NZ\$m)	2019A	2020A	2021E	2022E	2023E
Sales revenue	5,450	4,987	3,040	3,944	4,055
Normalised EBITDA	435	366	241	314	339
Depreciation and amortisation	(122)	(163)	(151)	(143)	(137)
Normalised EBIT	312	203	91	171	202
Net interest	(51)	(66)	(57)	(47)	(45)
Associate income	(1)	0	0	0	0
Tax	(61)	13	(9)	(35)	(44)
Minority interests	(2)	(16)	(9)	(8)	(7)
Normalised NPAT	196	102	33	98	120
Abnormals/other	(16)	(42)	0	0	0
Reported NPAT	180	60	33	98	120
Normalised EPS (cps)	49.0	25.6	6.4	18.8	23.1
DPS (cps)	43.0	16.5	0	25.0	25.0

Growth Rates	2019A	2020A	2021E	2022E	2023E
Revenue (%)	19	-8	-39	30	3
EBITDA (%)	-3	-16	-34	30	8
EBIT (%)	-10	-35	-55	88	18
Normalised NPAT (%)	-7	-48	-67	>100	23
Normalised EPS (%)	-7	-48	-75	>100	23
Ordinary DPS (%)	33	-62	-100	n/a	0

Cash Flow (NZ\$m)	2019A	2020A	2021E	2022E	2023E
EBITDA	435	366	241	314	339
Working capital change	(159)	268	(113)	(51)	(4)
Interest & tax paid	(161)	(124)	(74)	(90)	(98)
Other	223	(194)	(4)	(4)	(4)
Operating cash flow	338	316	51	169	233
Capital expenditure	(55)	(102)	(46)	(46)	(47)
(Acquisitions)/divestments	(28)	21	0	0	0
Other	4	(29)	(32)	(32)	(32)
Funding available/(required)	259	206	(27)	91	154
Dividends paid	(152)	(203)	0	(47)	(130)
Equity raised/(returned)	(1)	0	343	0	0
(Increase)/decrease in net debt	106	3	316	44	24

Balance Sheet (NZ\$m)	2019A	2020A	2021E	2022E	2023E
Working capital	358	119	236	287	290
Fixed assets	830	819	790	762	736
Intangibles	668	786	730	681	638
Right of use asset	0	282	282	282	282
Other assets	161	253	249	249	249
Total funds employed	2,017	2,259	2,287	2,261	2,195
Net debt/(cash)	827	1,083	751	691	651
Lease liability	0	299	299	299	299
Other liabilities	270	275	268	260	251
Shareholder's funds	902	600	976	1,027	1,017
Minority interests	18	2	(7)	(15)	(23)
Total funding sources	2,017	2,259	2,287	2,261	2,195

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

Valuation Ratios	2019A	2020A	2021E	2022E	2023E
EV/EBITDA (x)	4.9	6.3	9.5	6.8	6.3
EV/EBIT (x)	6.9	11.4	25.3	12.4	10.5
PE (x)	5.6	10.7	42.8	14.6	11.8
Price/NTA (x)	4.3	n/a	6.0	4.3	4.0
Free cash flow yield (%)	19.9	15.0	0.4	8.6	13.1
Net dividend yield (%)	15.7	6.0	0.0	9.1	9.1
Gross dividend yield (%)	21.8	8.4	0.0	12.7	12.7

Capital Structure	2019A	2020A	2021E	2022E	2023E
Interest cover EBIT (x)	6.1	3.1	1.6	3.7	4.5
Interest cover EBITDA (x)	8.5	5.5	4.2	6.7	7.6
Net debt/ND+E (%)	55.4	72.4	48.8	45.1	44.0
Net debt/EBITDA (x)	1.9	3.0	3.1	2.2	1.9

Key Ratios	2019A	2020A	2021E	2022E	2023E
Return on assets (%)	11.0	6.7	3.0	5.5	6.6
Return on equity (%)	21.3	17.0	3.4	9.7	12.1
Return on funds employed (%)	15.8	13.2	4.2	8.0	9.8
EBITDA margin (%)	8.0	7.3	7.9	8.0	8.3
EBIT margin (%)	5.7	4.1	3.0	4.3	5.0
Capex to sales (%)	1.0	2.0	1.5	1.2	1.2
Capex to depreciation (%)	85	126	57	58	60
Imputation (%)	100	100	100	100	100
Pay-out ratio (%)	88	65	0	133	108

Operating Performance	2019A	2020A	2021E	2022E	2023E
Product volumes (m litres)					
Petrol	1,165	1,099	959	1,054	1,049
Diesel - retail	454	445	413	456	454
Diesel - commercial	812	769	760	774	793
Other fuels	1,193	1,120	435	730	875
Supply - domestic	544	537	507	540	542
Sub-total	4,168	3,970	3,074	3,554	3,713
Supply - industry & export	280	67	141	165	169
Total Fuels	4,448	4,037	3,215	3,719	3,881
Retail service stations	343	334	331	330	333
Petrol/service station (m litres)	3.60	3.41	3.00	3.31	3.28
Diesel/service station (m litres)	1.32	1.30	1.22	1.37	1.37
Gross profit (NZDm)					
Fuels	700	666	553	582	590
Refining	54	37	(29)	10	32
Non-fuels	81	76	70	78	81
Flick Electric	1	2	6	8	10
Gross profit	836	781	600	679	714
Fuels gross margin (cpl)	16.8	16.8	18.0	16.4	15.9
Fuels margin incl refining (cpl)	17.0	17.4	16.3	15.9	16.0
Fuels margin excl supply (cpl)	18.0	17.7	16.9	16.5	16.6
Non-fuels revenue/station (NZD 000)	397	373	350	392	404

September 2020 fuel volumes

Figure 1. September 2020 fuel volumes

m litres	Sep-19	Aug-20	Sep-20	% chg vs. pcg	% chg vs. prior mth	Commentary
Volumes by brand/product						
Petrol - Z	59	54	60	2%	15%	Three large Caltex sites rebadged as Z – flat on a combined Z/Caltex basis
Petrol - Caltex	27	24	26	-4%	12%	
Petrol - Domestic supply	11	10	11	-1%	12%	Good performance vs. Sep-19 given Alert Level impacts
Diesel - Z	24	24	26	10%	13%	Strong performance vs. Sep-19 due to increased SME market volumes
Diesel - Caltex	11	12	12	9%	8%	Strong performance vs. Sep-19 due to increased SME market volumes
Diesel - Domestic supply	33	31	33	2%	10%	
Diesel - Commercial	62	65	70	13%	12%	Increase vs. Sep-19 due to contract win, increase vs. Aug general market activity
Other - Jet	66	19	22	-66%	19%	Improvement in jet vs. August as flights to/from Auckland return
Other - Marine	7	3	1	-79%	-56%	Marine continues to be very weak for Z
Other - Bitumen & other	10	6	10	1%	89%	
Total ZEL excl export	310	248	273	-12%	14%	Improvement on prior month helped by move down Alert Levels
Industry & Export	1	22	14		-35%	Aug 20 included big export sale of marine fuel as well as Nelson terminal sales
Total ZEL	311	271	288	-8%	10%	
Volumes by category						
Total Z	83	78	87	4%	15%	Three Caltex sites have rebranded as Z over past 12 months
Total Caltex	38	36	38	0%	11%	+ Caltex lapping a weak pcg, immediately after AA Smartfuel ending
Total retail petrol (excl supply)	86	78	86	0%	14%	
Total retail diesel (excl supply)	35	36	38	9%	11%	
Total Domestic supply	44	41	44	1%	11%	
Total retail (incl supply)	165	155	169	2%	13%	
Total commercial	145	93	104	-28%	16%	
Total volumes	310	248	273	-12%	14%	

Source: ZEL, Forsyth Barr analysis Note: % change vs. prior month adjusted for number of days in month

2Q21 and 1H21 fuel volumes

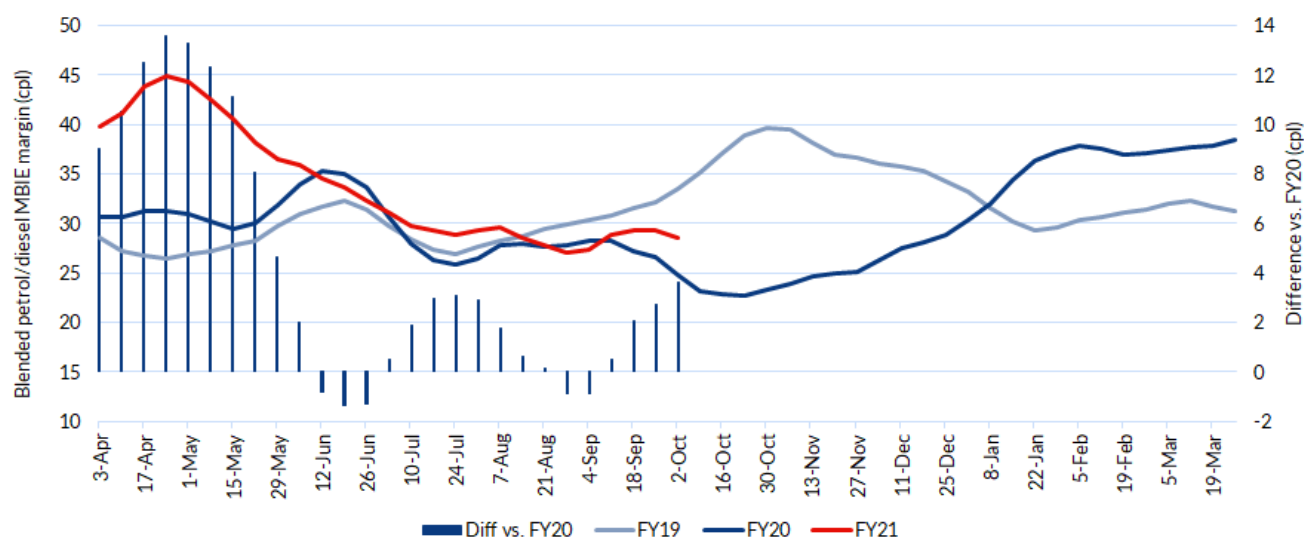
Figure 2. 2Q21 and 1H21 fuel volumes

	2Q20	1Q21	2Q21	% diff	% diff	1H20	1H21	%	Forsyth	
	Sep-19	Jun-20	Sep-20	vs pcg	vs pq	Sep-19	Sep-20	Diff	Barr	% Diff
Volumes (ml)										
Petrol - Z	180	120	177	-2%	47%	368	297	-19%	294	2
Petrol - Caltex	85	50	76	-10%	52%	184	126	-31%	123	3
Petrol - Subtotal	265	170	253	-5%	49%	552	423	-23%	418	5
Diesel - Z	73	54	77	6%	43%	147	131	-11%	132	-1
Diesel - Caltex	34	24	36	5%	49%	71	60	-16%	60	-1
Diesel - Subtotal	107	78	113	6%	45%	218	191	-12%	193	-2
TOTAL Retail	372	248	366	-2%	47%	770	614	-20%	610	3
Diesel - Commercial	186	165	199	7%	20%	377	364	-4%	356	8
Jet/Fuel Oil/Bitumen	261	80	93	-64%	16%	520	173	-67%	169	4
Supply - Domestic	127	102	127	0%	24%	255	229	-10%	223	6
TOTAL Commercial	574	347	418	-27%	21%	1,152	765	-34%	748	17
TOTAL Underlying Volume	946	595	784	-17%	32%	1,922	1,379	-28%	1,358	21
Supply - Industry & Export	24	7	49			26	56		64	-8
TOTAL	970	602	833	-14%	38%	1,948	1,435	-26%	1,422	13
Z retail (as reported)										
Z retail (as reported)	253	174	254	0%	46%	515	428	-17%	427	1
Caltex retail	119	74	112	-6%	51%	255	186	-27%	184	2

Source: ZEL, Forsyth Barr analysis

MBIE importer margins

Figure 3. Rolling 4-week MBIE blended importer margin



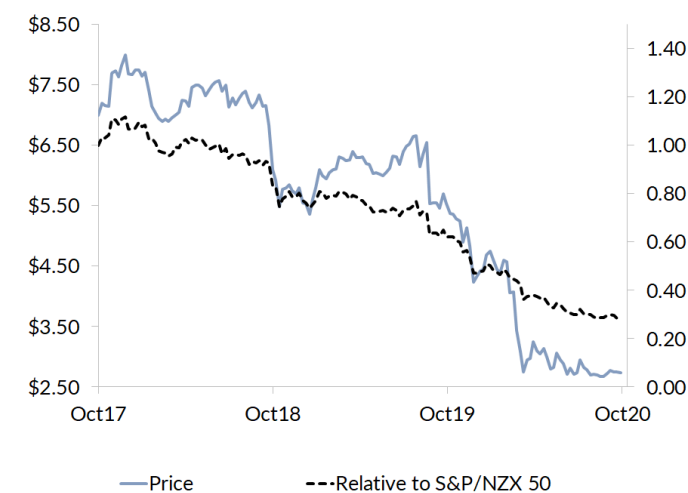
Source: MBIE, Forsyth Barr analysis

Summary forecast changes

Figure 4. Summary forecast changes

	FY21	FY21	%	FY22	FY22	%	FY22	FY22	%
	Old	New	Chg	Old	New	Chg	Old	New	Chg
Gross profit	597	600	0%	678	679	0%	713	714	0%
Operating costs	(358)	(359)	0%	(366)	(365)	0%	(375)	(375)	0%
EBITDAF	239	241	1%	313	314	0%	338	339	0%
EBIT	88	91	2%	170	171	0%	201	202	0%
NPAT (post-minorities)	32	33	7%	97	98	1%	120	120	1%
Dividend (cps)	-	-		25.0	25.0	0%	25.0	25.0	0%
Volumes (excl supply)	3,053	3,074	1%	3,544	3,554	0%	3,699	3,713	0%
Gross margin excl supply (cpl)	18.0	18.0	0%	16.4	16.4	0%	15.9	15.9	0%
Gross margin incl refining (cpl)	16.9	16.9	0%	16.5	16.5	0%	16.6	16.6	0%

Source: Forsyth Barr analysis

Figure 5. Price performance


Source: Forsyth Barr analysis

Figure 6. Substantial shareholders

Shareholder	Latest Holding
ACC	9.3%
Commonwealth Bank of Australia	6.1%

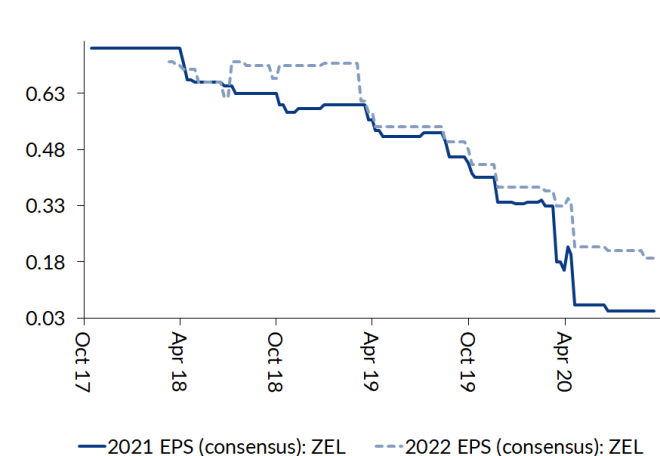
Source: NZX, Forsyth Barr analysis, NOTE: based on SPH notices only

Figure 7. International valuation comparisons

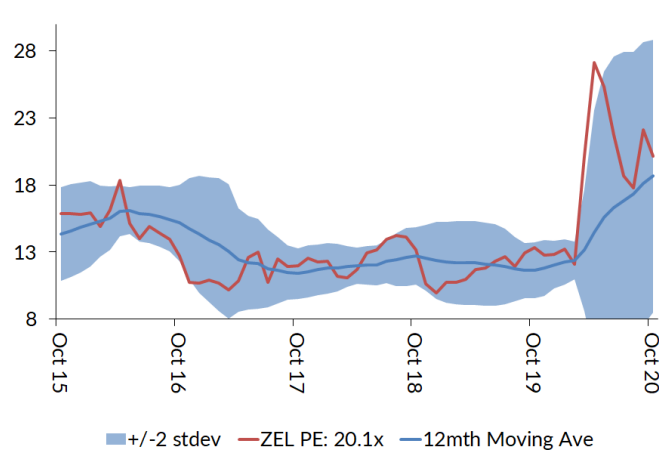
Company	Code	Price	Mkt Cap (m)	PE 2021E	PE 2022E	EV/EBITDA 2021E	EV/EBITDA 2022E	EV/EBIT 2021E	EV/EBIT 2022E	Cash Yld 2022E
(metrics re-weighted to reflect ZEL's balance date - March)										
Z Energy	ZEL NZ	NZ\$2.74	NZ\$1,425	42.8x	14.6x	10.4x	8.0x	27.7x	14.7x	9.1%
SUBURBAN PROPANE PARTNERS LP	SPH US	US\$17.11	US\$1,063	19.0x	14.6x	9.5x	8.9x	19.0x	17.8x	6.3%
AMPOL	ALD AT	A\$24.54	A\$6,128	26.9x	15.3x	10.1x	8.0x	20.4x	13.0x	3.7%
VIVA ENERGY GROUP	VEA AT	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a
CONTACT ENERGY *	CEN NZ	NZ\$7.85	NZ\$5,637	22.7x	26.8x	14.5x	16.2x	31.0x	37.7x	4.1%
MERCURY *	MCY NZ	NZ\$5.36	NZ\$7,302	28.6x	29.1x	17.1x	17.0x	30.2x	31.4x	3.2%
TRUSTPOWER *	TPW NZ	NZ\$7.59	NZ\$2,375	26.7x	25.9x	15.6x	15.3x	20.7x	20.2x	4.0%
MERIDIAN ENERGY *	MEL NZ	NZ\$5.40	NZ\$13,838	30.7x	35.1x	19.9x	22.4x	33.1x	40.3x	3.1%
GENESIS ENERGY *	GNE NZ	NZ\$3.18	NZ\$3,319	18.6x	17.5x	11.7x	12.0x	26.0x	28.6x	4.4%
Compco Average:				24.7x	23.5x	14.1x	14.3x	25.8x	27.0x	4.1%
ZEL Relative:				73%	-38%	-26%	-44%	7%	-46%	122%

EV = Current Market Cap + Actual Net Debt

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

Figure 8. Consensus EPS momentum (NZ\$)


Source: Forsyth Barr analysis

Figure 9. One year forward PE (x)


Source: Forsyth Barr analysis

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