

Contact Energy

Expected 1H21 Result all but Confirmed

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NEUTRAL

Contact Energy's (CEN) December 2020 operating performance has confirmed a solid 1H21 EBITDAF result of ~NZ\$246m, +NZ\$25m more than 1H20. At the 1H21 result on 15 February we expect most focus to be on CEN's revised dividend guidance (we are forecasting the FY21 dividend to be 36cps, -3cps lower than FY20) and whether it will confirm the construction of its 150MW Tauhara geothermal project (we expect it will).

NZX Code	CEN	Financials: Jun/	20A	21E	22E	23E	Valuation (x)	20A	21E	22E	23E
Share price	NZ\$8.83	NPAT* (NZ\$m)	248.5	242.2	242.0	234.7	PE	25.4	26.1	26.1	26.9
Target price	NZ\$9.10	EPS* (NZc)	34.7	33.8	33.8	32.8	EV/EBIT	31.8	36.5	33.0	30.6
Risk rating	Low	EPS growth* (%)	-10.4	-2.6	-0.1	-3.0	EV/EBITDA	16.3	16.2	16.1	16.0
Issued shares	715.5m	DPS (NZc)	39.0	36.0	36.0	36.0	Price / NTA	2.8	3.1	3.3	3.5
Market cap	NZ\$6,318m	Imputation (%)	64	70	45	50	Cash div yld (%)	4.4	4.1	4.1	4.1
Avg daily turnover	1,341k (NZ\$9,460k)	*Based on normalised profits					Gross div yld (%)	5.5	5.2	4.8	4.9

1H21 Expectations

- **Reporting date:** Monday, 15 February 2021
- **1H21 EBITDAF:** NZ\$246m, +NZ\$25m (+11%) higher than 1H20
- **1H21 dividend:** 15.0cps, -1cps (-6%) lower than 1H21

CEN's December 2020 operating statistics confirm 1H21 EBITDAF result

Whilst we calculate December 2020 EBITDAF was NZ\$31m, -NZ\$3m lower than the pcg, it completes a solid 1H21. We calculate 1H21 EBITDAF was +NZ\$25m (+11%) higher than 1H20 at NZ\$246m. 1H21 was a story of two quarters, with 1Q21 EBITDAF +NZ\$36m greater than 1Q20 whereas 2Q21 was -NZ\$10m lower than 2Q20. The driver of the movements is once again hydro generation. 1H21 hydro generation was +100GWh greater than 1H20, but 1Q21 was +210GWh greater and 2Q21 -110GWh less than their corresponding quarters.

Retail performance was solid. Whilst sales volumes have declined (mass market sales were down -2.5%) this was offset by increased retail prices such that we estimate the retail contribution was flat.

Dividend guidance and Tauhara the key points of focus at the 1H21 result

The two key things of note we expect from the 1H21 result are 1) revised dividend guidance now it has been confirmed NZAS is staying open to at least 31 December 2024 and 2) confirmation that CNE's Tauhara geothermal plant will get the go ahead to commence construction. Our interim dividend forecast is 15cps, -1cps lower than the 1H20 dividend. The reduced dividend has nothing to do with 1H21 earnings (which are going up) but is a function of our FY21 dividend forecast of 36cps and ensuring the 1H/2H split proportion is maintained. Our 36cps dividend forecast is -3cps lower than the FY20 dividend and reflects the expected underlying earnings decline with CEN now receiving less from NZAS.

We expect CEN to push go on its NZ\$600m 150MW Tauhara geothermal project. We expect CEN to also indicate it will debt fund the project, as CEN has significant balance sheet capacity and can issue hybrid bonds (up to ~NZ\$500m), half of which will be treated as equity by S&P for credit rating purposes.

Contact Energy Limited (CEN)

Priced as at 21 Jan 2021 (NZ\$)					8.83						
12-month target price (NZ\$)*					9.10	Spot valuations (NZ\$)					
Expected share price return					3.1%	1. DCF				9.07	
Net dividend yield					4.1%	2. Market multiples				8.52	
Estimated 12-month return					7.1%	3. Dividend yield				9.02	
Key WACC assumptions						DCF valuation summary (NZ\$m)					
Risk free rate					1.30%	Total firm value				7,687	
Equity beta					0.84	(Net debt)/cash				(1,201)	
WACC					5.0%	Less: Capitalised operating leases					
Terminal growth					1.5%	Value of equity				6,487	
Profit and Loss Account (NZ\$m)											
	2019A	2020A	2021E	2022E	2023E	Valuation Ratios	2019A	2020A	2021E	2022E	2023E
Sales revenue	2,519.0	2,073.0	2,117.2	2,177.3	2,125.1	EV/EBITDA (x)	14.6	16.3	16.2	16.1	16.0
Normalised EBITDA	518.0	451.0	455.9	458.7	462.8	EV/EBIT (x)	24.1	31.8	36.5	33.0	30.6
Depreciation and amortisation	(205.0)	(220.0)	(253.9)	(234.4)	(220.6)	PE (x)	22.8	25.4	26.1	26.1	26.9
Normalised EBIT	313.0	231.0	202.0	224.4	242.2	Price/NTA (x)	2.7	2.8	3.1	3.3	3.5
Net interest	(70.0)	(55.0)	(56.6)	(62.6)	(75.7)	Free cash flow yield (%)	5.3	3.8	3.8	1.5	-0.7
Depreciation capex adjustment	102	120	137	126	115	Net dividend yield (%)	4.4	4.4	4.1	4.1	4.1
Tax	(72.0)	(46.0)	(40.7)	(45.3)	(46.6)	Gross dividend yield (%)	5.5	5.5	5.2	4.8	4.9
Minority interests	0	0	0	0	0						
Adjusted normalised NPAT	277.5	248.5	242.2	242.0	234.7	Capital Structure	2019A	2020A	2021E	2022E	2023E
Abnormals/other	67	(124)	(137)	(126)	(115)	Interest cover EBIT (x)	4.9	4.8	3.8	3.8	3.4
Reported NPAT	345.0	125.0	104.7	116.4	119.9	Interest cover EBITDA (x)	7.4	8.2	8.1	7.3	6.1
Normalised EPS (cps)	38.8	34.7	33.8	33.8	32.8	Net debt/ND+E (%)	26.2	28.3	30.4	34.8	41.0
DPS (cps)	39.0	39.0	36.0	36.0	36.0	Net debt/EBITDA (x)	1.9	2.3	2.4	2.7	3.3
Growth Rates											
	2019A	2020A	2021A	2022A	2023A	Key Ratios	2019A	2020A	2021E	2022E	2023E
Revenue (%)	10.7	-17.7	2.1	2.8	-2.4	Return on assets (%)	9.8	4.6	4.3	4.7	4.9
EBITDA (%)	8.1	-12.9	1.1	0.6	0.9	Return on equity (%)	6.3	4.9	4.3	5.0	5.4
EBIT (%)	18.6	-26.2	-12.6	11.1	7.9	Return on funds employed (%)	9.3	4.4	4.1	4.5	4.6
Normalised NPAT (%)	21.4	-10.4	-2.6	-0.1	-3.0	EBITDA margin (%)	20.6	21.8	21.5	21.1	21.8
Normalised EPS (%)	21.4	-10.4	-2.6	-0.1	-3.0	EBIT margin (%)	12.4	11.1	9.5	10.3	11.4
Ordinary DPS (%)	21.9	0.0	-7.7	0.0	0.0	Capex to sales (%)	2.5	4.8	4.0	11.8	20.4
						Capex to depreciation (%)	31	45	33	110	196
Cash Flow (NZ\$m)											
	2019A	2020A	2021E	2022E	2023E	Imputation (%)	64	64	70	45	50
EBITDA	518.0	451.0	455.9	458.7	462.8	Pay-out ratio (%)	101	112	106	106	110
Working capital change	(20.0)	(24.0)	(4.3)	19.7	19.5						
Interest & tax paid	(111.0)	(118.0)	(126.4)	(128.1)	(95.6)	Operating Performance	2019A	2020A	2021E	2022E	2023E
Other	14.0	32.0	0	0	0	Hydro generation (GWh)	4,232	3,752	3,771	3,887	3,887
Operating cash flow	401.0	341.0	325.2	350.4	386.6	Geothermal generation (GWh)	3,257	3,331	3,139	3,324	3,455
Capital expenditure	(63.0)	(100.0)	(85.0)	(257.0)	(433.1)	Thermal generation (GWh)	1,422	1,360	1,279	1,138	977
(Acquisitions)/divestments	382.0	(6.0)	0	0	0	Total Generation (GWh)	8,911	8,443	8,189	8,348	8,319
Other	0	0	0	0	0	GWAP (\$/MWh)	129	100	119	124	105
Funding available/(required)	720.0	235.0	240.2	93.4	(46.5)						
Dividends paid	(251.0)	(280.0)	(279.1)	(257.7)	(257.7)	Gas consumed (PJ)	13.9	13.2	12.2	10.8	9.3
Equity raised/(returned)	0	0	0	0	0	Gas price (\$/GJ)	7.1	6.8	7.1	7.1	6.4
(Increase)/decrease in net debt	469.0	(45.0)	(38.9)	(164.3)	(304.2)						
Balance Sheet (NZ\$m)											
	2019A	2020A	2021E	2022E	2023E	Retail electricity volumes (GWh)	6,554	5,694	5,257	5,287	5,584
Working capital	(3.0)	19.0	21.3	(0.4)	(21.9)	Electricity customers (000)	411	418	401	401	401
Fixed assets	4,097.0	3,999.0	3,833.1	3,858.7	4,074.3	Average usage/customer (MWh)	8.6	8.5	8.3	8.4	8.4
Intangibles	425.0	406.0	406.0	406.0	406.0	Average retail price (\$/MWh)	191	199	207	209	209
Right of use asset	29.0	27.0	27.0	27.0	27.0						
Other assets	132.0	173.0	173.0	173.0	173.0	LWAP (\$/MWh)	136	108	131	136	115
Total funds employed	4,680.0	4,624.0	4,460.4	4,464.3	4,658.4	LWAP/GWAP	1.06	1.08	1.10	1.10	1.09
Net debt/(cash)	990.0	1,036.0	1,074.9	1,239.2	1,543.4						
Lease liability	25.0	22.0	22.0	22.0	22.0	Retail gas volumes (PJ)	3.1	3.0	2.9	2.9	2.9
Other liabilities	883.0	940.0	907.5	883.8	872.1	Gas customers (000)	67	65	64	64	64
Shareholder's funds	2,782.0	2,626.0	2,456.0	2,319.2	2,220.9	Average gas sales price (\$/GJ)	23.6	24.5	25.4	25.7	25.1
Minority interests	0	0	0	0	0						
Total funding sources	4,680.0	4,624.0	4,460.4	4,464.3	4,658.4						

1H21 forecast

Figure 1. 1H21 EBITDAF forecast

	1H20	1H21	Chg
	\$m	\$m	%
Wholesale elec sales	589	602	2%
Retail elec sales	450	447	-1%
Retail gas sales	42	42	0%
Steam	17	17	0%
Broadband	7	14	100%
Other Revenue	5	6	20%
Total Revenue	1,110	1,128	2%
Electricity purchases	(365)	(386)	6%
Other direct costs	(422)	(393)	-7%
Indirect operating costs	(102)	(103)	1%
EBITDAF	221	246	11%

Source: Forsyth Barr analysis

Figure 2. 1H21 forecast below EBITDAF

	1H20	1H21	Chg
	NZ\$m	NZ\$m	%
EBITDAF	221	246	11%
Depreciation & Amortisation	110	127	15%
Operating EBIT	111	119	7%
Chg in value of fincl instrmnts	2	-	
Net Interest	(28)	(28)	0%
Pretax	85	91	7%
Tax	(26)	(26)	0%
REPORTED PROFIT	59	65	10%
Abnormal items	(1)	-	
Normalised profit	58	65	13%
Normalised EPS	8.0	9.1	13%
Dividend per share	16.0	16.0	0%

Source: Forsyth Barr analysis

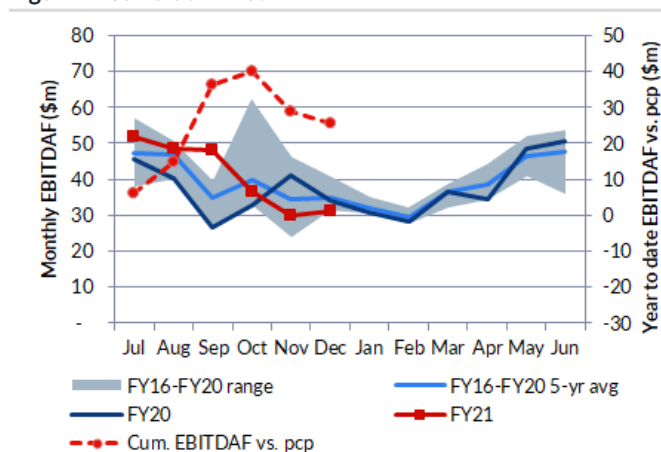
December 2020 operating performance summary

Figure 3. December 2020 operating performance

	Dec-19	Dec-20	Difference		Year to date		Difference	
	NZ\$m	NZ\$m	NZ\$m	%	FY20	FY21	NZ\$m	%
Trading performance	0	1	1		23	23	0	-1%
Cost of generation	(21)	(21)	0	-1%	(171)	(174)	(2)	1%
Contracted wholesale sales	49	45	(4)	-8%	351	380	29	8%
Wholesale	28	25	(3)	-10%	203	230	26	13%
Retail	8	8	0		30	30	0	-1%
Corporate costs (estimated)	(2)	(2)	0		(13)	(13)	0	0%
Estimated EBITDAF	34	31	(3)	-9%	220	246	26	12%

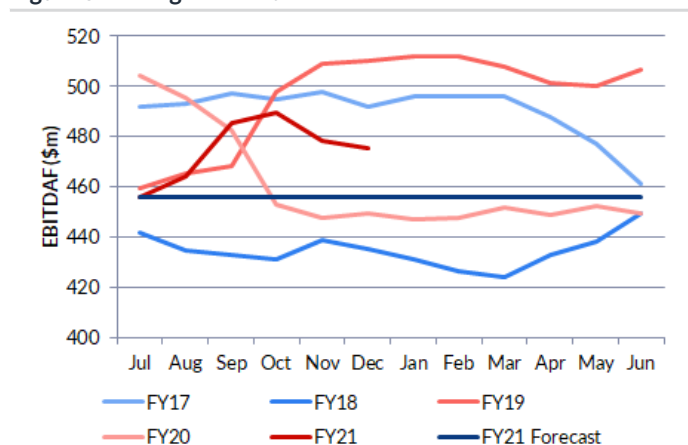
Source: CEN, Forsyth Barr analysis

Figure 4. Calculated historic EBITDAF

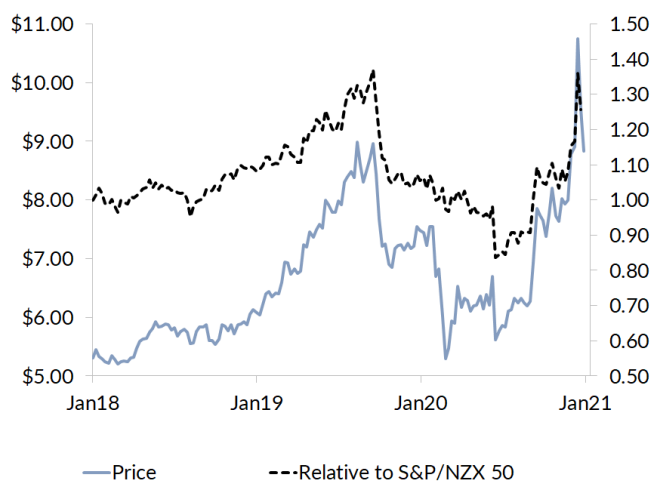


Source: CEN, Forsyth Barr analysis

Figure 5. Rolling 12-month EBITDAF



Source: CEN, Forsyth Barr analysis

Figure 6. Price performance


Source: Forsyth Barr analysis

Figure 7. Substantial shareholders

Shareholder	Latest Holding
BlackRock Investment Management	14.3%

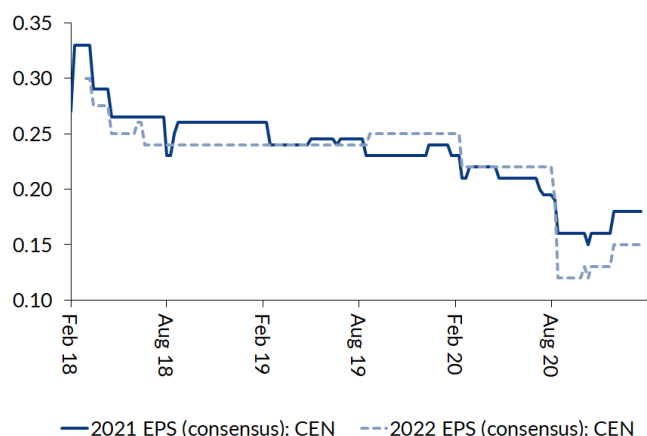
Source: NZX, Forsyth Barr analysis, NOTE: based on SPH notices only

Figure 8. International valuation comparisons

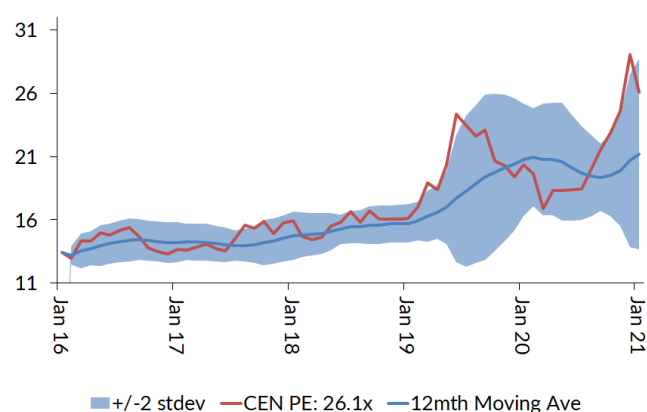
Company	Code	Price	Mkt Cap (m)	PE 2021E	PE 2022E	EV/EBITDA 2021E	EV/EBITDA 2022E	EV/EBIT 2021E	EV/EBIT 2022E	Cash Yld 2022E
(metrics re-weighted to reflect CEN's balance date - June)										
Contact Energy	CEN NZ	NZ\$8.83	NZ\$6,318	26.1x	26.1x	16.1x	16.0x	36.4x	32.8x	4.1%
GENESIS ENERGY *	GNE NZ	NZ\$3.60	NZ\$3,757	19.9x	17.1x	12.4x	11.5x	26.0x	23.5x	4.9%
MERIDIAN ENERGY *	MEL NZ	NZ\$7.44	NZ\$19,066	47.2x	46.4x	28.9x	27.9x	50.9x	47.3x	2.3%
MERCURY *	MCY NZ	NZ\$6.90	NZ\$9,400	34.8x	31.9x	20.7x	18.8x	36.5x	31.8x	2.7%
TRUSTPOWER *	TPW NZ	NZ\$8.75	NZ\$2,739	32.6x	28.5x	17.3x	15.7x	22.6x	20.1x	3.9%
AGL ENERGY	AGLAT	A\$11.86	A\$7,389	13.7x	19.5x	6.0x	7.0x	10.7x	14.7x	5.0%
ORIGIN ENERGY	ORG AT	A\$5.07	A\$8,929	21.7x	16.1x	6.4x	5.8x	22.6x	20.1x	4.8%
Compco Average:				28.3x	26.6x	15.3x	14.5x	28.2x	26.3x	3.9%
CEN Relative:				-8%	-2%	6%	11%	29%	25%	4%

EV = Current Market Cap + Actual Net Debt

Source: *Forsyth Barr analysis, Bloomberg Consensus, Compco metrics re-weighted to reflect headline (CEN) 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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