

# Trustpower

## 2Q21 Op Stats and 1H21 Result Preview

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### NEUTRAL

Trustpower's (TPW) 2Q21 operating statistics, whilst soft, were slightly better than expected, leading to a minor +NZ\$2m 1H21/FY21 EBITDAF upgrade. 2Q21 retail sales volumes (-9%) and generation (-9%) were both well down on 2Q20, although the weaker retail sales volumes is due mainly to the loss of a high volume low margin customer. TPW will be reporting its 1H21 result on Thursday, 5 November, and we are forecasting 1H21 EBITDAF of NZ\$111m, +NZ\$4m higher than 1H20, with stronger retail margins offsetting softer generation and sales volumes. Our rating is NEUTRAL with TPW's key challenge growing earnings.

NZX Code	TPW	Financials: Mar/	20A	21E	22E	23E	Valuation (x)	20A	21E	22E	23E
Share price	NZ\$7.70	NPAT* (NZ\$m)	74.2	90.7	90.3	85.5	PE	32.6	26.7	26.8	28.3
Target price	NZ\$7.78	EPS* (NZc)	23.6	28.9	28.8	27.2	EV/EBIT	20.9	20.7	20.8	21.8
Risk rating	Low	EPS growth* (%)	-36.4	22.3	-0.4	-5.4	EV/EBITDA	16.2	15.7	15.8	16.3
Issued shares	313.0m	DPS (NZc)	32.5	30.5	30.0	30.0	Price / NTA	2.3	2.3	2.3	2.3
Market cap	NZ\$2,410m	Imputation (%)	100	100	100	100	Cash div yld (%)	4.2	4.0	3.9	3.9
Avg daily turnover	46.2k (NZ\$322k)	*Based on normalised profits					Gross div yld (%)	5.9	5.5	5.4	5.4

#### What's changed?

- **Earnings:** 1H21 & FY21 EBITDAF increased +NZ\$2m to NZ\$111m and NZ\$194m respectively
- **Target price:** Unchanged at NZ\$7.78
- **Rating:** Unchanged at NEUTRAL

#### 2Q21 operating statistics highlights retail growth hard to achieve, but generation price better than expected

Retail growth continues to be hard to achieve with 2Q21 fixed price electricity sales volumes down -9% vs. 2Q20. Commercial time of use volumes is where most of the decline was, due to the loss of a large, low margin customer. Mass market sales volumes fell -0.2%, although this was better than expected. In terms of connection numbers, electricity customers continue to slide, down -1,000 in 2Q21 (-3,000 in 1H21). Telco customer numbers started growing again after a hiatus in 1Q21, up +2,000 to 106,000. Customers with two or more utilities also grew +2,000 with TPW again highlighting the lower churn benefits of a multi-product offering.

With generation volumes again weak (particularly North Island hydro), the main bright spot was a stronger than expected selling price. Hydro generation for 2Q21 was 522GWh, -9% lower than 2Q20 and -10% lower in 1H21. The average price received for generation was NZ\$139/MWh, better than we had been anticipating.

#### 1H21 result (to be released 5 November) expected to be better than 1H20, but still a challenging period

We are forecasting 1H21 EBITDAF of NZ\$111m, +NZ\$4m better than the 1H20. However, that is still below "average" with weak hydro conditions the main issue. Whilst 1H21 generation volumes are softer than 1H20, we expect firm wholesale electricity prices have helped prevent a decline in earnings, and that increased retail margins will be the driver of the lift in earnings. Our dividend forecast is 15.5cps, the same as the 2H20 dividend.

## Trustpower Ltd (TPW)

Priced as at 15 Oct 2020 (NZ\$)

7.70

### 12-month target price (NZ\$)\*

7.78

Expected share price return

1.0%

Net dividend yield

3.9%

Estimated 12-month return

5.0%

### Spot valuations (NZ\$)

1. DCF

7.66

2. Market multiples

7.18

3. Dividend Yield

7.44

### Key WACC assumptions

Risk free rate

1.30%

Equity beta

0.84

WACC

5.4%

Terminal growth

1.5%

### DCF valuation summary (NZ\$m)

Total firm value

3,080

(Net debt)/cash

(665)

Less: Capitalised operating leases

Value of equity

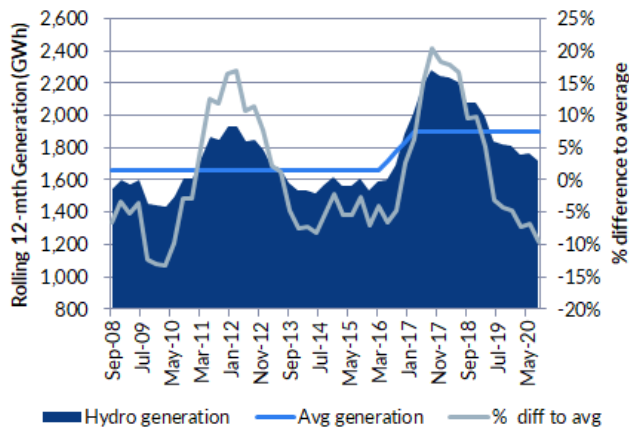
2,399

Profit and Loss Account (NZ\$m)	2019A	2020A	2021E	2022E	2023E	Valuation Ratios	2019A	2020A	2021E	2022E	2023E
Sales revenue	1,030.1	989.9	928.1	893.2	876.6	EV/EBITDA (x)	13.2	16.2	15.7	15.8	16.3
<b>Normalised EBITDA</b>	<b>222.2</b>	<b>186.5</b>	<b>194.4</b>	<b>193.7</b>	<b>187.4</b>	EV/EBIT (x)	16.8	20.9	20.7	20.8	21.8
Depreciation and amortisation	(47.2)	(42.6)	(47.2)	(47.1)	(47.1)	PE (x)	20.7	32.6	26.7	26.8	28.3
<b>Normalised EBIT</b>	<b>175</b>	<b>144</b>	<b>147</b>	<b>147</b>	<b>140</b>	Price/NTA (x)	2.0	2.3	2.3	2.3	2.3
Net interest	(28)	(32)	(26)	(25)	(25)	Free cash flow yield (%)	3.7	3.2	3.9	4.2	4.0
Depreciation capex adjustment	19	(2)	9	8	7	Net dividend yield (%)	9.6	4.2	4.0	3.9	3.9
Tax	(45)	(32)	(36)	(36)	(35)	Gross dividend yield (%)	11.7	5.9	5.5	5.4	5.4
Minority interests	(2)	(3)	(3)	(3)	(3)						
<b>Normalised NPAT</b>	<b>117</b>	<b>74</b>	<b>91</b>	<b>90</b>	<b>85</b>	<b>Capital Structure</b>	<b>2019A</b>	<b>2020A</b>	<b>2021E</b>	<b>2022E</b>	<b>2023E</b>
Abnormals/other/depn adj	(26)	21	(6)	(6)	(5)	Interest cover EBIT (x)	6.8	4.9	6.1	6.3	6.2
<b>Reported NPAT</b>	<b>91</b>	<b>95</b>	<b>84</b>	<b>85</b>	<b>80</b>	Interest cover EBITDA (x)	7.9	5.9	7.4	7.7	7.5
Normalised EPS (cps)	37.1	23.6	28.9	28.8	27.2	Net debt/ND+E (%)	58.6	64.8	66.0	66.6	67.7
DPS (cps)	74.0	32.5	30.5	30.0	30.0	Net debt/EBITDA (x)	2.5	3.3	3.2	3.2	3.4
Growth Rates	2019A	2020A	2021A	2022A	2023A	Key Ratios	2019A	2020A	2021E	2022E	2023E
Revenue (%)	5.2	-3.9	-6.2	-3.8	-1.9	Return on assets (%)	7.2	8.0	7.0	7.0	6.7
EBITDA (%)	-17.6	-16.1	4.3	-0.4	-3.2	Return on equity (%)	9.7	6.9	8.6	8.6	8.3
EBIT (%)	-21.6	-17.8	2.3	-0.4	-4.3	Return on funds employed (%)	7.2	5.6	6.2	6.2	5.9
Normalised NPAT (%)	-17.3	-36.4	22.3	-0.4	-5.4	EBITDA margin (%)	21.6	18.8	20.9	21.7	21.4
Normalised EPS (%)	-17.3	-36.4	22.3	-0.4	-5.4	EBIT margin (%)	17.0	14.5	15.9	16.4	16.0
Ordinary DPS (%)	0.0	-4.4	-6.2	-1.6	0.0	Capex to sales (%)	3.0	4.5	3.3	3.5	3.7
						Capex to depreciation (%)	98	142	92	95	96
Cash Flow (NZ\$m)	2019A	2020A	2021E	2022E	2023E	Imputation (%)	55	100	100	100	100
<b>EBITDA</b>	<b>222.2</b>	<b>186.5</b>	<b>194.4</b>	<b>193.7</b>	<b>187.4</b>	Pay-out ratio (%)	199	138	106	104	110
Working capital change	(47.1)	1.7	(10.2)	(2.0)	(0.4)						
Interest & tax paid	(74.8)	(77.1)	(58.2)	(58.1)	(56.8)	<b>Operating Performance</b>	<b>2019A</b>	<b>2020A</b>	<b>2021E</b>	<b>2022E</b>	<b>2023E</b>
Other	20.0	10.9	(0.6)	(0.6)	(0.6)	NZ electricity revenue	861	804	744	702	676
<b>Operating cash flow</b>	<b>120.3</b>	<b>121.9</b>	<b>125.4</b>	<b>133.0</b>	<b>129.6</b>	Gas revenue	29	30	33	35	37
Capital expenditure	(31.1)	(44.7)	(30.9)	(31.7)	(32.3)	Telecommunication revenue	88	98	95	105	111
(Acquisitions)/divestments	8.1	20.2	0	0	0	Other revenue	52	58	56	52	53
Other	0	(6.8)	(6.8)	(6.8)	(6.8)	<b>Total revenue</b>	<b>1,030</b>	<b>990</b>	<b>928</b>	<b>893</b>	<b>877</b>
<b>Funding available/(required)</b>	<b>97.3</b>	<b>90.6</b>	<b>87.8</b>	<b>94.5</b>	<b>90.5</b>	Generation (GWh)	1,995	1,758	1,771	1,896	1,896
Dividends paid	(190.4)	(156.7)	(97.0)	(93.9)	(93.9)	NZ GWAP (\$/MWh)	125	107	123	74	62
Equity raised/(returned)	(1)	(1)	0	0	0						
<b>(Increase)/decrease in net debt</b>	<b>(94.5)</b>	<b>(67.4)</b>	<b>(9.3)</b>	<b>0.6</b>	<b>(3.4)</b>	Mass market sales (GWh)	1,845	1,817	1,834	1,788	1,773
						TOU sales (GWh)	880	826	536	587	590
Balance Sheet (NZ\$m)	2019A	2020A	2021E	2022E	2023E	Spot sales (GWh)	1,021	972	866	933	937
Working capital	(0.3)	(8.2)	15.5	16.3	14.9	<b>Total Sales (GWh)</b>	<b>3,746</b>	<b>3,615</b>	<b>3,235</b>	<b>3,308</b>	<b>3,300</b>
Fixed assets	1,924.7	1,836.4	1,828.5	1,820.9	1,813.2	LWAP (\$/MWh)	131	109	125	76	64
Intangibles	37.0	38.7	37.7	37.4	37.7	LWAP/GWAP	1.04	1.02	1.02	1.03	1.04
Right of use asset	0	35.5	35.5	35.5	35.5						
Other assets	114.8	100.2	86.7	87.9	89.7	Electricity customers (000)	267	266	262	259	256
<b>Total funds employed</b>	<b>2,076.2</b>	<b>2,002.6</b>	<b>2,003.9</b>	<b>1,998.0</b>	<b>1,990.9</b>	Usage/customer (MWh)	6.8	6.8	7.0	6.9	6.9
Net debt/(cash)	557.4	616.7	626.0	625.3	628.7	Revenue/MWh sold (\$)	230	222	230	212	205
Lease liability	0	36.1	36.1	36.1	36.1	Gas customers (000)	39	41	43	44	44
Other liabilities	269.8	249.8	251.9	253.2	253.8	Volume/customer (GJ)	26.5	24.9	25.9	25.9	25.9
Shareholder's funds	1,224.4	1,076.2	1,063.5	1,054.2	1,040.5	Telco customers (000)	96	104	109	114	118
Minority interests	24.6	23.8	26.4	29.1	31.8	Revenue/customer (\$)	963	983	987	997	1,007
<b>Total funding sources</b>	<b>2,076.2</b>	<b>2,002.6</b>	<b>2,003.9</b>	<b>1,998.0</b>	<b>1,990.9</b>						

## 2Q21 operating statistics

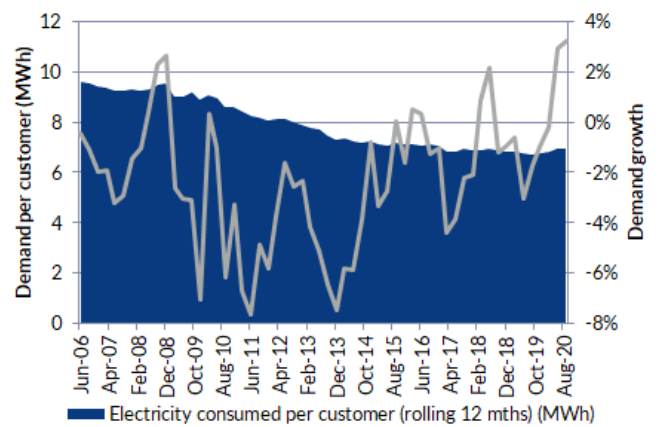
### Generation and sales volumes

Figure 1. Hydro generation volumes still weak



Source: TPW, Forsyth Barr analysis

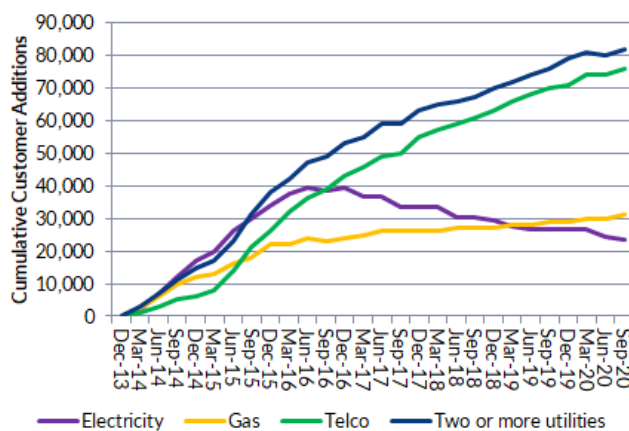
Figure 2. Rolling 12-mth mass market sales per customer



Source: TPW, Forsyth Barr analysis

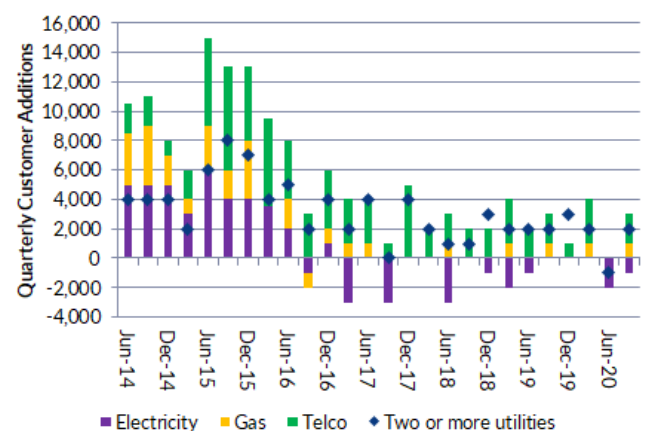
### Customer number growth after launch of triple play offering — weak electricity trend continues

Figure 3. Cumulative customer additions slow down continues



Source: TPW, Forsyth Barr analysis

Figure 4. Modest telco and gas growth, electricity negative



Source: TPW, Forsyth Barr analysis

## 1H21 result preview

Result date is Thursday 5 November.

Figure 5. 1H21 result preview comments

6 Months Ending Sept (NZ\$m)	1H20	1H21F	Change	Commentary
Electricity	448	407	-9%	Decline mainly due to lower sales volumes
Other	92	91	-1%	
<b>Total Revenue</b>	<b>539</b>	<b>498</b>	<b>-8%</b>	
Costs	(432)	(387)	-10%	Lower opex due to lower sales volumes
<b>EBITDAF</b>	<b>107</b>	<b>111</b>	<b>4%</b>	Slight increase on 1H20 due to expected retail margin improvement
Depreciation and amortisation	(20)	(24)	19%	Inclusion of lease depreciation
<b>EBIT</b>	<b>87</b>	<b>87</b>	<b>0%</b>	
Fair value gains/(losses)	(12)	0		We do not forecast fair value movements
One-off items	(2)	0		
Net interest	(17)	(13)	-22%	Decline due to lower interest rates
<b>Pretax Profit</b>	<b>56</b>	<b>74</b>	<b>33%</b>	
Tax	(17)	(21)	22%	
<b>REPORTED PROFIT</b>	<b>39</b>	<b>53</b>	<b>38%</b>	
Minority interests	(1)	(1)		
<b>Profit Attributable to Shareholders</b>	<b>38</b>	<b>53</b>	<b>39%</b>	
Abnormal items	11	0		1H20 abnormal is after-tax fair value adjustment
<b>NORM PROFIT</b>	<b>49</b>	<b>53</b>	<b>9%</b>	
Earnings per share (cps)	15.5	16.9	9%	
Dividend per share (cps)	17.0	15.5	-9%	1H21 dividend forecast consistent with 2H20 dividend
NZ generation (GWh)	989	945	-4%	
FPVV electricity sold (GWh)	1,443	1,301	-10%	Big drop in time of use sales due to loss of high volume, low margin customer

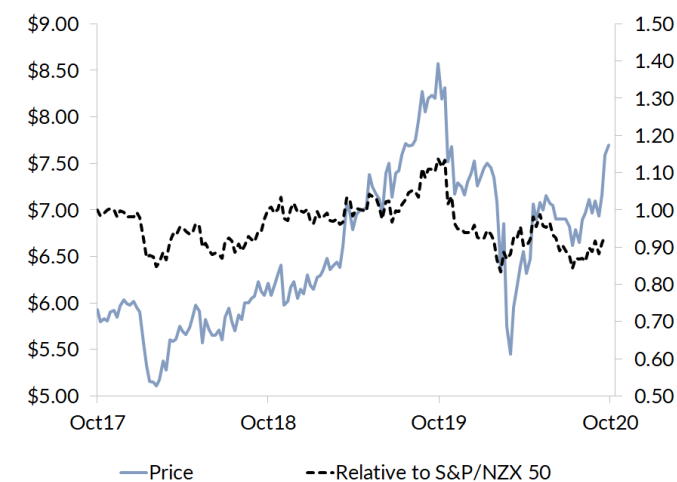
Source: Forsyth Barr analysis

## Summary forecast changes

Figure 6. Summary forecast changes

	FY21 Old	FY21 New	Chg	FY22 Old	FY22 New	Chg	FY23 Old	FY23 New	Chg
	\$m	\$m	%	\$m	\$m	%	\$m	\$m	%
Revenue	947	928	-2.0%	921	893	-3.0%	906	877	-3.3%
<b>EBITDAF</b>	<b>192</b>	<b>194</b>	<b>1.2%</b>	<b>195</b>	<b>194</b>	<b>-0.8%</b>	<b>189</b>	<b>187</b>	<b>-0.7%</b>
EBIT	145	147	1.7%	148	147	-1.1%	142	140	-0.9%
NPAT	85	87	1.8%	89	87	-1.9%	85	83	-2.0%
Normalised Profit	83	84	1.8%	86	85	-1.9%	82	80	-2.1%
DPS	30.5	30.5	0.0%	30.0	30.0	0.0%	30.0	30.0	0.0%
Generation volumes (GWh)	1,776	1,771	-0.3%	1,896	1,896	0.0%	1,896	1,896	0.0%
Generation sales price (\$/MWh)	\$119.6	\$122.5	2.4%	\$74.0	\$74.0	0.0%	\$61.5	\$61.5	0.0%
Retail sales (GWh)	2,519	2,369	-5.9%	2,543	2,375	-6.6%	2,533	2,363	-6.7%

Source: Forsyth Barr analysis

**Figure 7. Price performance**


Source: Forsyth Barr analysis

**Figure 8. Substantial shareholders**

Shareholder	Latest Holding
Infratil	51.0%
TECT Holdings	26.8%

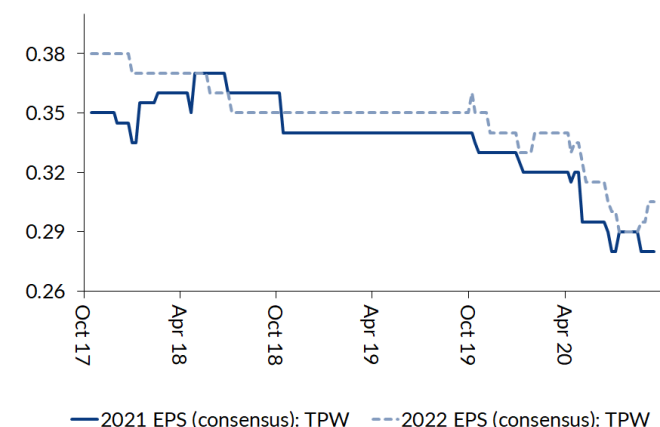
Source: NZX, Forsyth Barr analysis, NOTE: based on SPH notices only

**Figure 9. International valuation comparisons**

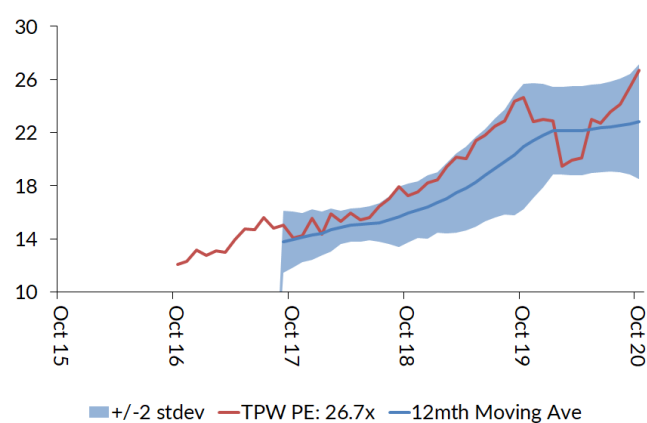
Company	Code	Price	Mkt Cap (m)	PE 2021E	PE 2022E	EV/EBITDA 2021E	EV/EBITDA 2022E	EV/EBIT 2021E	EV/EBIT 2022E	Cash Yld 2022E
(metrics re-weighted to reflect TPW's balance date - March)										
Trustpower	TPW NZ	NZ\$7.70	NZ\$2,410	26.7x	26.8x	15.6x	15.6x	20.6x	20.6x	3.9%
CONTACT ENERGY *	CEN NZ	NZ\$8.03	NZ\$5,767	23.3x	27.4x	14.8x	16.5x	31.6x	38.4x	4.0%
GENESIS ENERGY *	GNE NZ	NZ\$3.20	NZ\$3,339	18.7x	17.7x	11.8x	12.1x	26.1x	28.7x	4.4%
MERIDIAN ENERGY *	MEL NZ	NZ\$5.48	NZ\$14,030	31.2x	35.6x	20.1x	22.7x	33.5x	40.8x	3.1%
MERCURY *	MCY NZ	NZ\$5.45	NZ\$7,418	29.0x	29.6x	17.3x	17.3x	30.7x	31.9x	3.1%
AGL ENERGY	AGLAT	A\$13.41	A\$8,352	12.3x	16.0x	5.8x	6.7x	9.7x	12.5x	6.2%
ORIGIN ENERGY	ORG AT	A\$4.37	A\$7,696	37.7x	14.4x	22.4x	5.1x	5.1x	15.7x	5.1%
Compc Average:				25.4x	23.4x	15.4x	13.4x	22.8x	28.0x	4.3%
TPW Relative:				5%	14%	1%	17%	-10%	-26%	-10%

EV = Current Market Cap + Actual Net Debt

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

**Figure 10. Consensus EPS momentum (NZ\$)**


Source: Forsyth Barr analysis

**Figure 11. One year forward PE (x)**


Source: Forsyth Barr analysis

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