

## Austal Limited

### OPV Contract Win, Underpinning Throughput At Henderson Yard For 15 Years

The Australian Government has announced that the contract for the design of the Offshore Patrol Vessel (OPV) has been awarded to Luerksen. While ASB was not partnered with Luerksen through the tender process, the Government has surprisingly announced that ASB will be involved in the construction of 10 of the 12 Luerksen-designed vessels in WA. Over the course of the next 3 months, ASB will start negotiations with Luerksen and while the economics from these negotiations remain uncertain, we see the Government's announcement as a material positive given the likely underwriting of baseline throughput at ASB's shipyard for the next 15 years.

- Commercial arrangement still yet to be determined.** ASB (along with Civec – CVL SP) will now be involved in the construction of 10 vessels based on the Luerksen design (rather than the Fassmer design which ASB was associated with for its tender into the program). Given the change to the program structure, ASB will now negotiate with Luerksen and the Australian Government regarding the sub-contracting of the construction phase. The expectation is the construction phase contract is ~A\$1.5bn for 12 vessels (ie. A\$125m per vessel), with ASB involved in the build of the final 10 vessels. With regards to margins and ASB/Civec's respective involvement in the construction phase, ASB expects contract negotiations to be finalised in Feb/March 2018.
- Economics not finalised, but baseline activity the material positive.** While it is difficult to ascertain the economics from the Government's announcement given ASB still has to finalise negotiations with Luerksen, the key material positive from the announcement is the underwriting of baseline construction in its Western Australian shipyard for the next 15 years. Shipbuilders are high-fixed-cost businesses, and throughput in the shipyard is critical. While the final details or the construction contract are yet to be determined, we believe the program could underwrite >50% of the capacity at ASB's Henderson yards for the 15 years.

## Overweight

**ASB.AX, ASB AU**

Price: A\$1.84

**Price Target: A\$2.00**

### Australia

#### Emerging Companies

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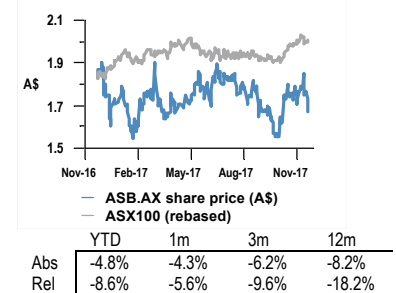
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#### Price Performance



#### Austal Limited (Reuters: ASB.AX, Bloomberg: ASB AU)

Year-end Jun (A\$)	FY16A	FY17A	FY18E	FY19E	FY20E
Revenue (A\$ mn)	1,511	1,324	1,346	1,202	1,229
EBITDA (A\$ mn)	79	90	92	91	93
Net Profit (A\$ mn)	(84)	15	35	35	39
EPS (A\$)	(0.24)	0.04	0.10	0.10	0.11
P/E (x)	NM	41.7	18.1	18.2	16.4
EV/EBITDA (x)	7.2	7.3	7.2	6.7	6.1
DPS (A\$)	0.04	0.04	0.04	0.04	0.04
Dividend Yield	2.2%	2.2%	2.2%	2.2%	2.2%
Normalised EPS (A\$)	0.10	0.09	0.10	0.10	0.11
Normalised EPS Growth	(23.8%)	(5.9%)	8.1%	(0.6%)	11.4%
Normalised PE	18.5	19.6	18.1	18.2	16.4

Source: Company data, Bloomberg, J.P. Morgan estimates.

#### Company Data

Shares O/S (mn)	349
Market Cap (A\$ mn)	643.03
Market Cap (\$ mn)	487.29
Price (A\$)	1.84
Date Of Price	24-Nov-17
Free Float(%)	-
3M - Avg daily vol (mn)	0.44
3M - Avg daily val (A\$ mn)	0.74
3M - Avg daily val (\$ mn)	0.6
ASX100	4930.50
Exchange Rate	0.76
Price Target End Date	30-Jun-18
Price Target (A\$)	2.00

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## Investment Thesis, Valuation and Risks

### **Austal Limited** *(Overweight; Price Target: A\$2.00)*

#### **Investment Thesis**

Austal (ASB) designs and manufactures customized aluminum defense and commercial vessels; its customers include many of the world's leading ferry operators and defense forces.

#### **Valuation**

Our June 2018 share price target of A\$2.00 is based on our DCF valuation of A\$1.79 per share (WACC: 9.8%, Forecast period: 10 years, Terminal value: assumes the company does not generate ROIC above WACC in perpetuity). Our price target is based on the future value of our valuation, less any dividends to be paid between now and the target date.

#### **Risks to Rating and Price Target**

The key risks to our rating and share price target include: 1) Currency movements impacting the translation of foreign earnings and the competitiveness of the company's shipbuilding operations. 2) US budget and allocation of funding to the Department of Defense. 3) General economic environment, impacting the demand for vessels. 4) Operational risk, impacting the margins generated from large capital projects.

## Austal Limited

## Relative recommendation:

## Overweight

A\$ in millions, year end Jun

Profit And Loss						Valuation Summary					
	FY16	FY17	FY18E	FY19E	FY20E			A\$m	A\$ps		
Revenue	1,511	1,324	1,346	1,202	1,229	Current mkt capitalisation		643.03	1.84		
Revenue growth	5.4%	(12.4%)	1.6%	(10.7%)	2.3%	Price Target				2.00	
COGS	(1,386)	(1,193)	0	0	0	Capital growth to price target				8.6%	
Operating Expenses	(46)	(41)	(1,254)	(1,110)	(1,136)						
<b>EBITDA</b>	<b>79</b>	<b>90</b>	<b>92</b>	<b>91</b>	<b>93</b>						
EBITDA growth	(19.0%)	14.4%	1.5%	(0.4%)	1.9%	Trading Multiples					
EBITDA margin	5.2%	6.8%	6.8%	7.6%	7.6%	FY16	FY17	FY18E	FY19E	FY20E	
Amortisation	(1)	(1)	(1)	(1)	(1)	PE Pre-abnormals	18.5	19.6	18.1	18.2	16.4
Depreciation	(28)	(30)	(30)	(31)	(30)	PE Reported	NM	41.7	18.1	18.2	16.4
<b>EBIT</b>	<b>49</b>	<b>59</b>	<b>60</b>	<b>59</b>	<b>63</b>	EV/EBITDA	7.2	7.3	7.2	6.7	6.1
Other Income	-	-	-	-	-	EV/EBIT	11.5	11.2	11.0	10.3	9.1
Other Expenses	-	-	-	-	-	Key Ratios					
Net Interest	(5)	(6)	(7)	(7)	(4)	FY16	FY17	FY18E	FY19E	FY20E	
<b>Pre-Tax Profit</b>	<b>44</b>	<b>53</b>	<b>53</b>	<b>53</b>	<b>59</b>	Dividend Yield	2.2%	2.2%	2.2%	2.2%	2.2%
Tax	(9)	(20)	(18)	(18)	(20)	Franking	100.0%	100.0%	0.0%	0.0%	0.0%
Tax Rate	20.2%	38.4%	34.0%	34.0%	34.0%	Return on Assets (%)	3.3%	3.3%	3.6%	3.6%	4.1%
Minorities	(0)	0	0	0	0	Return on Equity (%)	7.1%	7.1%	7.5%	7.2%	7.6%
Abnormals (post tax)	(119)	(17)	0	0	0	ROIC (%)	6.0%	5.6%	6.0%	5.9%	6.4%
<b>Reported NPAT</b>	<b>(84)</b>	<b>15</b>	<b>35</b>	<b>35</b>	<b>39</b>	Leverage					
<b>Normalised NPAT</b>	<b>35</b>	<b>33</b>	<b>35</b>	<b>35</b>	<b>39</b>	FY16	FY17	FY18E	FY19E	FY20E	
Growth	(23.1%)	(5.8%)	8.0%	(0.5%)	11.4%	Gearing (Net Debt / Equity)	(11.3%)	10.0%	10.2%	(0.2%)	(8.5%)
End of Period Shares	348	349	350	350	350	Gearing (ND / (ND + E))	(12.7%)	9.1%	9.2%	(0.2%)	(9.2%)
EFPOWA	348	348	348	348	348	Net Debt / EBITDA	(65.5%)	50.8%	53.2%	(1.0%)	(47.8%)
Reported EPS (\$)	(0.24)	0.04	0.10	0.10	0.11	EBIT Interest Cover (x)	8.9	10.4	8.6	9.1	17.8
<b>Normalised EPS (\$)</b>	<b>0.10</b>	<b>0.09</b>	<b>0.10</b>	<b>0.10</b>	<b>0.11</b>	Balance Sheet					
Growth	(23.8%)	(5.9%)	8.1%	(0.6%)	11.4%	FY16	FY17	FY18E	FY19E	FY20E	
DPS (\$)	0.04	0.04	0.04	0.04	0.04	Cash	224	150	150	150	150
Growth	0.0%	0.0%	0.0%	0.0%	0.0%	Receivables	128	100	110	104	106
DPS/EPS payout	NM	90.7%	39.4%	39.6%	35.6%	Investments	-	-	-	-	-
Cash Flow Statement						FY16	FY17	FY18E	FY19E	FY20E	
Net Profit for Cashflow	(121)	59	60	59	63	Inventories	109	170	166	155	159
Depreciation & Amortisation	30	32	31	32	30	Other Current Assets	8	10	11	11	11
Non Cash Items	-	-	-	-	-	<b>Total Current Assets</b>	<b>470</b>	<b>432</b>	<b>437</b>	<b>420</b>	<b>426</b>
Working Capital Changes	213	(108)	5	7	(2)	Net PPE	491	500	523	504	485
Other Operating Cashflows	(6)	(19)	(33)	(23)	(21)	Total Intangibles	9	9	8	8	7
<b>Cashflow from Operating Activities</b>	<b>117</b>	<b>(37)</b>	<b>64</b>	<b>76</b>	<b>70</b>	Other Non Current Assets	43	19	30	30	31
Capex	(39)	(10)	(53)	(12)	(12)	<b>Total Non Current Assets</b>	<b>543</b>	<b>528</b>	<b>561</b>	<b>541</b>	<b>524</b>
Net Acquisitions	0	(45)	0	0	0	<b>Total Assets</b>	<b>1,013</b>	<b>960</b>	<b>998</b>	<b>962</b>	<b>950</b>
Other Investing cashflows	0	0	0	0	0	Creditors	230	155	166	155	159
<b>Investing Cash Flow</b>	<b>(39)</b>	<b>(55)</b>	<b>(53)</b>	<b>(12)</b>	<b>(12)</b>	Current Borrowings	3	10	10	10	10
Inc/(Dec) in Borrowings	11	25	3	(50)	(44)	Current Tax Provisions	0	0	5	6	7
Equity Issued	0	0	0	0	0	Other Current Provisions	42	47	48	49	51
Dividends Paid	(16)	(12)	(13)	(14)	(14)	Other Current Liabilities	32	28	28	28	29
Other Financing Cashflows	0	0	0	0	0	<b>Total Current Liabilities</b>	<b>307</b>	<b>239</b>	<b>257</b>	<b>249</b>	<b>256</b>
<b>Financing Cash Flow</b>	<b>(5)</b>	<b>12</b>	<b>(10)</b>	<b>(64)</b>	<b>(58)</b>	Non Current Creditors	-	-	-	-	-
Net Cash Flow	69	(74)	0	0	0	Non Current Borrowings	170	186	189	140	96
						Deferred Tax Liabilities	0	11	6	6	6
						Other Non Current Provisions	1	3	3	3	3
						Other Non Current Liabilities	78	64	64	64	64
						<b>Total Non Current Liabilities</b>	<b>249</b>	<b>264</b>	<b>262</b>	<b>213</b>	<b>169</b>
						<b>Total Liabilities</b>	<b>556</b>	<b>503</b>	<b>519</b>	<b>462</b>	<b>425</b>
						Equity	115	116	117	117	117
						Other Equity	0	0	0	0	0
						Reserves	101	92	92	92	92
						Retained Profits	242	249	270	291	316
						Outside Equity Interests	0	0	0	0	0
						<b>Total Shareholders Equity</b>	<b>458</b>	<b>457</b>	<b>479</b>	<b>500</b>	<b>525</b>
						Net Debt	(52)	46	49	(1)	(44)

Source: Company reports and J.P. Morgan estimates.

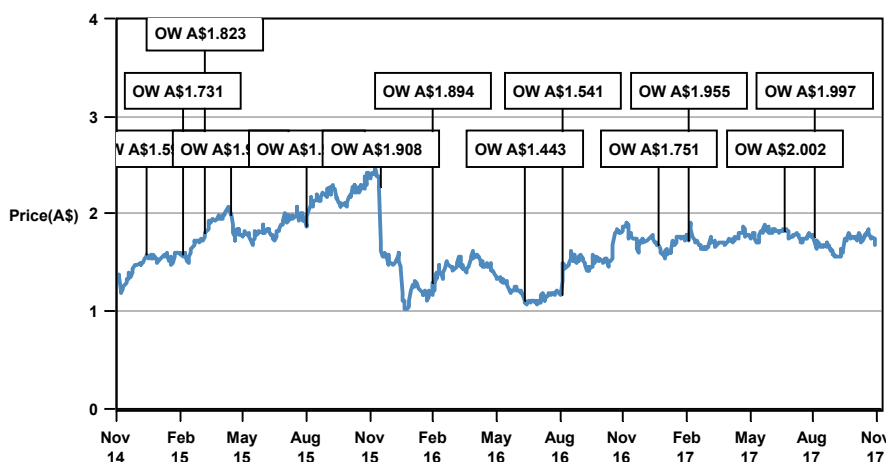
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**Austal Limited (ASB.AX, ASB AU) Price Chart**



Date	Rating	Share Price (A\$)	Price Target (A\$)
08-Jan-15	OW	1.57	1.59
27-Feb-15	OW	1.58	1.73
02-Apr-15	OW	1.82	1.82
07-May-15	OW	1.99	1.96
27-Aug-15	OW	1.87	1.96
10-Dec-15	OW	2.28	1.91
23-Feb-16	OW	1.29	1.89
04-Jul-16	OW	1.11	1.44
29-Aug-16	OW	1.17	1.54
13-Jan-17	OW	1.68	1.75
27-Feb-17	OW	1.72	1.95
14-Jul-17	OW	1.82	2.00
28-Aug-17	OW	1.76	2.00

Source: Bloomberg and J.P. Morgan; price data adjusted for stock splits and dividends. Initiated coverage Feb 12, 2013.

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