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PWR Holdings (PWH)

Outlook remains very good

Recommendation

Buy (unchanged)

Price

\$3.46

Target (12 months)

\$4.50 (unchanged)

GICS Sector

Automobiles and Components

Expected Return

Capital growth	30.1%
Dividend yield	2.4%
Total expected return	32.5%

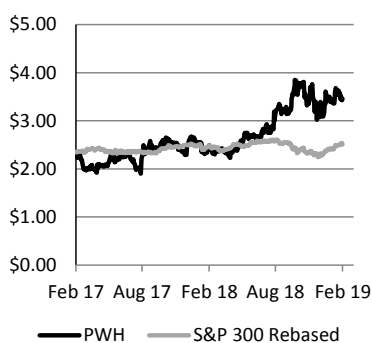
Company Data & Ratios

Enterprise value	\$343.2m
Market cap	\$346.0m
Issued capital	100.0m
Free float	61%
Avg. daily val. (52wk)	\$451,715
12 month price range	\$2.18 - \$4.04

Price Performance

	(1m)	(3m)	(12m)
Price (A\$)	3.42	3.32	2.34
Absolute (%)	1.17	4.22	47.86
Rel market (%)	-3.43	-3.99	45.28

Absolute Price



SOURCE: IRESS

Beat in revenue, miss in NPAT

1HFY19 NPAT grew 53% to \$3.1m but was 12% below our forecast of \$3.6m. The miss was driven by a much lower EBITDA margin than we were expecting (20.3% vs 26.2%) while revenue was actually higher than our forecast (\$24.8m vs BP \$23.6m). Gross cash flow was up a strong 55% to \$3.7m which was c.73% of EBITDA so cash flow conversion was reasonable. The interim dividend of 1.6c was slightly ahead of our forecast of 1.5c.

No FY19 guidance but “on track for growth”

PWR does not provide guidance. The company did say, however, it is “on track for growth” in both 2HFY19 and FY20. PWR also said there are no significant changes in expected timing or volumes for OEM programs and there will be some revenue from these in FY19 but the majority is expected in FY20 and FY21.

Modest EPS changes

We have downgraded our FY19 EPS forecast by 4% but there is little or no change in our FY20 and FY21 EPS forecasts. The downgrade in our FY19 EPS forecasts has been driven by a reduction in our EBITDA margin forecast and an increase in our D&A forecast but has been partially offset by a reduction in our effective tax rate forecast. We continue to forecast strong EPS growth over the next three years of 25%, 29% and 21%.

Investment view: PT unchanged at \$4.50, Maintain BUY

We have updated each valuation we use in the determination of our price target for the earnings changes as well as market movements and the time creep. There are no changes in the key assumptions we apply in each valuation which are a 50% premium in the relative valuations and a 10,0% WACC and 4.5% terminal growth rate in the DCF. The net result, however, is no change in our PT of \$4.50 which is a 30% premium to the current share price so we maintain the BUY recommendation.

Earnings Forecast

Year end 30 June	2018	2019e	2020e	2020e
Total revenue (A\$m)	51.9	63.3	74.0	84.7
EBITDA (A\$m)	16.3	21.2	27.2	33.0
NPAT (A\$m)	11.0	13.8	17.8	21.5
EPS (diluted) (cps)	11.0	13.8	17.8	21.5
EPS growth (%)	19%	25%	29%	21%
PER (x)	31.5	25.1	19.5	16.1
Price/CF (x)	24.7	27.9	18.4	15.5
EV/EBITDA (x)	19.8	16.4	12.7	10.5
Dividend (€ps)	7.3	8.4	10.0	11.9
Yield (%)	2.1%	2.4%	2.9%	3.4%
ROE (%)	23.7%	26.3%	29.1%	30.0%
Franking (%)	100%	100%	100%	100%

SOURCE: BELL POTTER SECURITIES ESTIMATES

1HFY19 Result

A summary of the 1HFY19 result is shown below.

Figure 1 - 1HFY19 result summary

Year end 30 June	Result vs PCP			Result vs Forecast		Comment
	1HFY18	1HFY19	Change	1HFY19e	Variance	
Revenue (A\$m)	20.4	24.8	22%	23.6	5%	5% beat in revenue driven by higher than expected PWR revenue
Other income	0.3	0.3	0%	0.3	20%	
Total expenses	-16.8	-20.0	19%	-17.6	14%	Opex higher than forecast
as % of revenue	-82.7%	-80.9%		-74.8%		
EBITDA	3.8	5.0	31%	6.2	-19%	19% miss in EBITDA driven by higher than expected opex
Depreciation	-0.7	-1.1	71%	-0.9	24%	Depreciation higher than expected
Amortisation	0.0	0.0	NM	0.0	NM	
EBIT	3.2	3.9	23%	5.3	-26%	26% miss in EBIT
Net interest expense	-0.1	0.5	NM	0.0	NM	Net interest revenue rather than expense
Profit before tax	3.1	4.4	43%	5.3	-17%	17% miss in PBT
Income tax expense	-1.0	-1.3	25%	-1.7	-26%	Lower income tax expense than forecast
NPAT	2.1	3.1	52%	3.6	-12%	12% miss in NPAT
EBITDA margin	18.8%	20.3%	153bps	26.2%	-589bps	EBITDA margin c.590bps below our forecast
Effective tax rate	-33.0%	-28.7%	425bps	-32.5%	378bps	Effective tax rate c.380bps below our forecast
NPAT margin	10.1%	12.7%	257bps	15.1%	-243bps	
Weighted average fully diluted shares	100.0m	100.0m	0%	100.0m	0%	
Diluted EPS	2.1c	3.1c	52%	3.6c	-12%	12% miss in diluted EPS
Interim dividend	1.1c	1.6c	45%	1.5c	7%	Interim dividend above our forecast
Franking	100%	100%		100%		
Payout ratio	53%	51%		42%		Payout ratio above our forecast

SOURCE: COMPANY DATA AND BELL POTTER SECURITIES ESTIMATES

The key take-outs of the result were:

- 5% beat in revenue:** Revenue grew 22% to \$24.8m which was 5% above our forecast and the beat was driven by higher than expected revenue from the core PWR business (\$19.4m vs BP \$17.2m). The beat in PWR more than offset the lower than expected revenue in C&R Racing (\$5.3m vs \$6.4m).
- 19% miss in EBITDA:** EBITDA grew 31% to \$5.0m but was 19% below our forecast of \$6.2m and the miss was driven by higher than expected opex (\$20.0m vs BP \$17.6m). The key driver of the higher than expected opex was an increase in staff numbers particularly in 2QFY19.
- 12% miss in NPAT:** NPAT grew 52% to \$3.1m which was 12% below our forecast and the lesser miss at NPAT relative to EBITDA was due to net interest revenue of \$0.5m (we forecast no revenue or expense) and also a lower effective tax rate than forecast (28.7% vs BP 32.5%).
- Reasonable cash flow:** While not shown in the figure above, gross cash flow grew a strong 55% to \$3.7m which was c.73% of EBITDA so cash flow conversion was reasonable. Capex was, as flagged, unusually high at \$4.7m and, combined with dividends and tax paid, net cash decreased by c.\$8.9m for the six months and the company took on an additional \$3.5m in debt.
- Interim dividend of 1.6c:** The interim dividend increased 45% to 1.6c which was modestly higher than our forecast of 1.5c. The payout ratio was 51% which was broadly consistent with 1HFY18.

Earnings and Valuation Changes

Modest EPS Changes

We have downgraded our FY19 EPS forecast by 4% but there is little or no change in our FY20 and FY21 EPS forecasts. The downgrade in our FY19 EPS forecasts has been driven by a reduction in our EBITDA margin forecast and an increase in our D&A forecast but has been partially offset by a reduction in our effective tax rate forecast. We continue to forecast strong EPS growth over the next three years of 25%, 29% and 21%.

A summary of the changes in our key forecasts is shown below. There are no changes in our DPS forecasts given the modest or negligible changes in our EPS forecasts. Our DPS forecast equate to a payout ratio of b/w 55-60% which is consistent with the company's stated payout ratio policy of b/w 40-60%.

Figure 2 - Change in key forecasts

Year end 30 June	FY19e			FY20e			FY21e		
	Old	New	Change	Old	New	Change	Old	New	Change
Total revenue (A\$m)	60.9	63.3	3.9%	71.2	74.0	4.0%	81.4	84.7	4.0%
EBITDA	22.4	21.2	-5.6%	27.5	27.2	-1.1%	33.0	33.0	0.0%
NPAT	14.3	13.8	-4.0%	17.8	17.8	0.0%	21.5	21.5	-0.1%
Diluted EPS	14.3c	13.8c	-4.0%	17.8c	17.8c	0.0%	21.5c	21.5c	-0.1%
DPS	8.3c	8.4c	1.2%	10.0c	10.0c	0.0%	11.9c	11.9c	0.0%

SOURCE: BELL POTTER SECURITIES ESTIMATES

PT Unchanged at \$4.50

We have updated each valuation we use in the determination of our price target for the earnings changes as well as market movements and the time creep. There are no changes in the key assumptions we apply in each valuation which are a 50% premium in the relative valuations and a 10,0% WACC and 4.5% terminal growth rate in the DCF.

The change in each valuation and the impact on our PT calculation is shown below.

Figure 3 - Change in valuations and impact on PT

Methodology	Old (as at 5-Feb-19)			New (as at 26-Feb-19)		
	Valuation per share	% weighting	Price target	Valuation per share	% weighting	Price target
PE ratio	\$4.53	40%	\$1.81	\$4.46	40%	\$1.79
EV/EBITDA	\$4.59	40%	\$1.84	\$4.53	40%	\$1.81
DCF	\$4.28	20%	\$0.86	\$4.51	20%	\$0.90
Total			\$4.50			\$4.50

SOURCE: BELL POTTER SECURITIES ESTIMATES

The figure shows a modest reduction in the relative valuations and a more material increase in the DCF valuation. Notably all of the valuations are all now very similar. The net result, however, is no change in our PT of \$4.50 which is a 30% premium to the current share price so we maintain the BUY recommendation.

PWR Holdings

Company Description

PWR Holdings (PWR) is a leading provider of customised cooling solutions to the global motorsports market as well as the wider automotive industry. The key products of the company are radiators, intercoolers, oil coolers and heat exchangers for various elite motorsports series including Formula One, NASCAR and Supercars. The company also engineers cooling solutions for automotive OEMs (original equipment manufacturers) and is diversifying into emerging technology applications where cooling solutions are required.

PWR was established in 1998 and head office is in Ormeau, Queensland. All manufacturing is currently done in Ormeau but the company also has a fabrication facility in Indianapolis, Indiana as well as sales and distribution centres in both the US and the UK. Approximately 85% of the company's revenue is generated outside of Australia.

Investment Thesis

We maintain our BUY recommendation on PWR. Our investment thesis is based on:

- **Valuation:** Our 12 month price target on PWR is \$4.50. The price target is generated from a blend of three valuation methodologies we apply to the company: PE ratio, EV/EBITDA and DCF. The price target is a 30% premium to the current share price and the total expected return (which includes the forecast dividend yield) is 32%.
- **Forecast strong growth:** We forecast strong double digit growth in each of the next three years (FY19 to FY21) assuming no further impacts from asset write downs or tax. Note we expect an uplift in underlying growth in FY20 relative to FY19 due to an increasing contribution from OE programs and also the benefits of increased capacity.
- **Diversifying outside of motorsports:** PWR is diversifying its revenue base and increasing its exposure to areas outside of motorsports. For example, emerging technologies represented c.9% of FY18 revenue and is now the third largest area of revenue after motorsports and the automotive aftermarket. OEM is another focus area of the company and represented c.5% of FY18 revenue.

Key Risks

Key downside risks to our estimates and valuation include (but are not limited to):

- **Customer risk:** PWR operates on a purchase order basis with its customers. The loss of, or significant reduction in purchases by, one or more key customers or the cessation of a leading motorsports series or team could lead to a reduction in PWR's revenue and earnings.
- **Product risk:** PWR regularly develops new products and upgrades existing products and any product failures, defects or recalls could affect PWR's reputation, revenue and earnings.
- **Currency risk:** Adverse movements in the GBP or USD against the AUD could have an adverse impact on performance. PWR does not currently hedge against currency risk. The sensitivity of FY16 NPAT for changes in key exchange rates provided in the prospectus was c.+/- \$0.2m for a +/- 1 pence move in the AUD/GBP exchange rate and c.+/- \$0.05m for a 1 cent move in the AUD/USD exchange rate.

Table 1 - Financial summary

PWR Holdings (PWH)						Share price:	\$3.46	Target price:	\$4.50			
						No. of issued shares:	100.0m	Market cap:	\$346.0m			
Profit & Loss (A\$m)						Valuation data						
Year end 30 Jun	2017	2018	2019e	2020e	2021e	Year end 30 Jun	2017	2018	2019e	2020e	2021e	
Revenue	48.1	51.9	63.3	74.0	84.7	NPAT (A\$m)	9.3	11.0	13.8	17.8	21.5	
Change	2%	8%	22%	17%	14%	Diluted EPS (cps)	9.3	11.0	13.8	17.8	21.5	
Other income	0.7	0.7	0.5	0.5	0.5	Change	0%	19%	25%	29%	21%	
Expenses (excl. D&A, int.)	-34.1	-36.2	-42.6	-47.3	-52.2	P/E ratio (x)	37.3	31.5	25.1	19.5	16.1	
% of revenue	-71%	-70%	-67%	-64%	-62%	CFPS (cps)	8.9	14.0	12.4	18.8	22.4	
EBITDA	14.7	16.3	21.2	27.2	33.0	Price/CF (x)	38.7	24.7	27.9	18.4	15.5	
Depreciation	-1.5	-1.7	-2.3	-2.6	-2.8	DPS (cps)	5.6	7.3	8.4	10.0	11.9	
Amortisation	0.0	0.0	0.0	0.0	0.0	Yield	1.6%	2.1%	2.4%	2.9%	3.4%	
EBIT	13.3	14.7	18.9	24.6	30.2	Franking	100%	100%	100%	100%	100%	
Net interest (expense)/revenue	-0.3	0.0	0.0	0.0	0.1	EV/EBITDA (x)	22.9	19.8	16.4	12.7	10.5	
Pre-tax profit	12.9	14.7	18.9	24.7	30.2	EV/EBIT (x)	25.5	22.1	18.3	14.0	11.5	
Income tax expense	-3.7	-3.7	-5.1	-6.9	-8.8	NTA per share (cps)	26.8	32.4	38.3	46.9	57.5	
NPAT	9.3	11.0	13.8	17.8	21.5	Price/NTA (x)	12.9	10.7	9.0	7.4	6.0	
Change	6%	19%	25%	29%	21%	Performance ratios						
Cash Flow (A\$m)	Year end 30 Jun	2017	2018	2019e	2020e	2021e	Year end 30 Jun	2017	2018	2019e	2020e	2021e
EBITDA	14.7	16.3	21.2	27.2	33.0	EBITDA margin	30.6%	31.5%	33.5%	36.8%	39.0%	
Change in working capital	-1.2	0.3	-3.6	-1.5	-1.8	EBIT margin	27.5%	28.3%	29.8%	33.3%	35.6%	
Gross cash flow	13.5	16.6	17.5	25.7	31.2	Return on assets	20.0%	21.0%	23.5%	26.2%	27.2%	
Interest paid	0.0	0.0	-0.1	-0.1	-0.1	Return on equity	22.7%	23.7%	26.3%	29.1%	30.0%	
Income tax paid	-4.5	-2.6	-5.1	-6.9	-8.8	ROIC	42.9%	43.5%	48.1%	54.0%	62.4%	
Operating cash flow	8.9	14.0	12.4	18.8	22.4	Payout ratio	60.3%	66.4%	61.0%	56.3%	55.5%	
Grant received	0.1	0.1	0.0	0.0	0.0	Effective tax rate	-28.3%	-25.1%	-27.0%	-28.0%	-29.0%	
Interest received	0.0	0.0	0.0	0.1	0.1	Leverage ratios						
Acquisition of subsidiary	0.0	0.0	0.0	0.0	0.0	Year end 30 Jun	2017	2018	2019e	2020e	2021e	
Payments for intangibles	0.0	0.0	0.0	0.0	0.0	Net debt/(cash) (A\$m)	-8.3	-11.6	-8.8	-13.4	-22.5	
Proceeds from sale of PPE	0.2	0.2	0.0	0.0	0.0	Net debt/equity	NM	NM	NM	NM	NM	
Payment for PPE	-3.9	-5.2	-7.5	-5.0	-2.5	Gearing	NM	NM	NM	NM	NM	
Investing cash flow	-3.6	-4.9	-7.5	-4.9	-2.4	Net debt/EBITDA (x)	NM	NM	NM	NM	NM	
Proceeds from issue of shares	0.0	0.0	0.0	0.0	0.0	Net interest cover (x)	NM	NM	NM	NM	NM	
Payments for cost of IPO	0.0	0.0	0.0	0.0	0.0	Segmentals (A\$m)						
Dividends paid	-4.7	-5.8	-7.8	-9.2	-10.9	Year end 30 Jun	2017	2018	2019e	2020e	2021e	
Proceeds from borrowings	0.0	0.0	0.0	0.0	0.0	Revenue (A\$m)						
Repayment of borrowing	0.0	0.0	0.0	0.0	0.0	PWR Performance	31.8	39.1	48.8	57.4	66.0	
Loans to related parties	0.0	0.0	0.0	0.0	0.0	C&R Racing	16.3	12.8	14.4	16.6	18.7	
Repayment of finance leases	-0.4	-0.3	0.0	0.0	0.0	Total	48.1	51.9	63.3	74.0	84.7	
Financing cash flows	-5.1	-6.1	-7.8	-9.2	-10.9	Growth						
Net change in cash	0.2	3.1	-2.9	4.6	9.1	PWR Performance	3.4%	23.0%	25.0%	17.5%	15.0%	
Cash at start of period	8.8	9.1	12.1	9.2	13.9	C&R Racing	-1.7%	-21.6%	12.5%	15.0%	12.5%	
Exchange rate impact	0.0	0.0	0.0	0.0	0.0	Total	1.6%	7.8%	21.9%	16.9%	14.4%	
Cash at end of period	9.1	12.1	9.2	13.9	23.0	EBITDA						
Balance Sheet (A\$m)	Year end 30 Jun	2017	2018	2019e	2020e	2021e	PWR Performance	12.9	17.9	20.8	25.5	30.7
Cash	9.1	12.1	9.2	13.9	23.0	C&R Racing	1.7	-0.6	0.7	2.1	2.8	
Current receivables	3.4	4.1	5.1	5.5	6.3	Total	14.7	16.0	21.2	27.2	33.0	
Inventories	7.3	6.8	9.5	11.1	12.7	Margin						
Other current assets	2.5	1.7	1.7	1.7	1.7	PWR Performance	40.7%	45.7%	42.5%	44.5%	46.5%	
PPE	7.9	11.6	16.8	19.2	18.9	C&R Racing	10.2%	-4.9%	5.0%	12.5%	15.0%	
Intangibles - Goodwill	3.1	3.1	3.1	3.1	3.1	Total	30.6%	30.8%	33.5%	36.8%	39.0%	
Intangibles - Other	11.0	11.0	11.0	11.0	11.0	Interims (A\$m)						
Other non-current assets	2.0	2.1	2.1	2.1	2.1	Year end 30 Jun	1HFY18	2HFY18	1HFY19	2HFY19e		
Total assets	46.3	52.5	58.5	67.7	78.8	Revenue	20.4	31.5	24.8	38.5		
Payables	2.9	3.4	3.5	4.1	4.7	Change	9%	7%	22%	22%		
Current borrowings	0.3	0.2	0.2	0.2	0.2	Other income	0.3	0.4	0.3	0.2		
Current employee benefits	1.4	1.6	1.6	1.6	1.6	EBITDA	3.8	12.5	5.0	16.1		
Current provisions	0.1	0.4	0.4	0.4	0.4	Depreciation	-0.7	-1.0	-1.1	-1.2		
Non-current borrowings	0.5	0.3	0.3	0.3	0.3	Amortisation	0.0	0.0	0.0	0.0		
Non-current employee benefits	0.1	0.1	0.1	0.1	0.1	EBIT	3.2	11.5	3.9	15.0		
Non-current provisions	0.0	0.0	0.0	0.0	0.0	Net interest (expense)/revenue	-0.1	0.1	0.5	-0.5		
Total liabilities	5.3	6.0	6.1	6.7	7.3	Pre-tax profit	3.1	11.6	4.4	14.5		
Issued capital	25.9	25.9	25.9	25.9	25.9	Income tax expense	-1.0	-2.7	-1.3	-3.8		
Reserves	0.2	0.5	0.5	0.5	0.5	NPAT	2.1	8.9	3.1	10.6		
Retained earnings/(losses)	14.9	20.1	26.1	34.6	45.2	Change	14%	20%	52%	19%		
Total shareholders' equity	41.0	46.5	52.5	61.0	71.6							

SOURCE: BELL POTTER SECURITIES ESTIMATES

Recommendation structure

Buy: Expect >15% total return on a 12 month view. For stocks regarded as 'Speculative' a return of >30% is expected.

Hold: Expect total return between -5% and 15% on a 12 month view

Sell: Expect <-5% total return on a 12 month view

Speculative Investments are either start-up enterprises with nil or only prospective operations or recently commenced operations with only forecast cash flows, or companies that have commenced operations or have been in operation for some time but have only forecast cash flows and/or a stressed balance sheet.

Such investments may carry an exceptionally high level of capital risk and volatility of returns.

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