



AUSTAL LIMITED (ASB)

Record FY20, some uncertainty ahead

Austal Limited (ASB) has delivered FY20 NPAT of \$89.0m, up 45% on FY19 (\$61.4m). A final dividend of 5.0cps has been declared, bringing the full year dividend to 8.0cps, up on FY19 (6.0cps).

EBIT of \$130.4m was up 41% on FY19 (\$92.8m) and compares favourably to guidance issued in May for EBIT of no less than \$125m. This is a very strong result when remembering that original FY20 guidance issued in August 2019 was for EBIT of not less than \$105m.

Supporting the strong reported numbers, cash flow was very strong, resulting in ASB ending FY20 with net cash of \$272m.

Short-term uncertainty into FY21

ASB has elected not to provide FY21 guidance noting the global economic uncertainty and the potential impact of COVID-19.

~150 staff at ASB's Alabama facility have contracted COVID-19. While the majority of these staff have recovered, there remains the risk of ongoing infections and its flow on impacts to productivity and shipbuilding timetables.

Recent volatility in the AUDUSD has also come into the mix. ASB notes that each 1cps move in the FX rate impacts (+/-) EBIT by between \$1.2m-\$1.4m.

Our FY21 EBIT forecast reduces 5% to \$119m from \$124m.

Medium to longer-term outlook remains solid

ASB's order book at FY20 was \$4.3bn down from \$4.9bn at FY19. Contract awards of A\$852m were achieved during FY20, with no major US ship builds being awarded.

Over the medium to longer-term, the outlook continues to be positive. As the LCS program winds down across FY23/24, confidence for future work at ASB's US operations remains high, particularly following the June announcement that the US Government Department of Defense has agreed a US\$50m Defense Production Act (DPA) Agreement with ASB. ASB intends to match the DPA funding with a US\$50m investment of its own, with the total US\$100m used to develop a steel shipbuilding capability at its Mobile shipyard over the next two years.

In this respect ASB has announced the conditional purchase (for sub US\$10m) of 15 acres of additional waterside land and facilities across the river from ASB's existing facilities in Mobile.

Neutral; Price Target \$3.44

ASB's strong balance sheet continues to provide optionality for any potential investment opportunities that may arise. With our price target of \$3.44ps, (down from \$3.71ps previously) sitting in line with the current share price we reduce our recommendation to Neutral from Buy.

ASB.asx
Neutral

24 Aug 2020

Share Price:	\$3.51
Valuation:	\$3.30
12mth price target:	\$3.44

Brief Business Description:

Shipbuilder focussed on the design, construction and maintenance of commercial and defence vessels, with operations in the USA, Australia and throughout Asia.

Hartleys Brief Investment Conclusion:

Well positioned to navigate COVID-19 crisis. Order book provides solid visibility. Future contract wins the key.

Chairman & CEO:

John Rothwell (Non-Exec. Chairman)
David Singleton (MD / CEO)

Top Shareholders:

John Rothwell	9%
Blackrock	5%

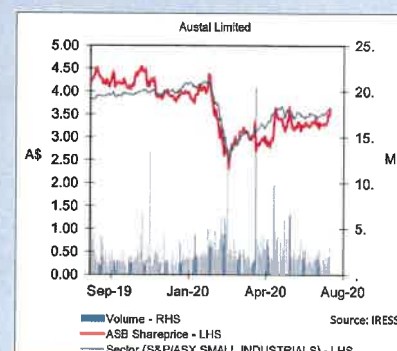
Company Address:

100 Clarence Rd
Henderson WA, 6166

Issued Capital:	359m
- fully diluted	365m
Market Cap:	\$1,260m
- fully diluted	\$1,282m
Net Debt (FY20):	-\$272m

	FY20a	FY21e	FY22e
Revenue	2,086	1,962	1,985
EBIT (A\$m)	130	119	124
NPAT (A\$m)	89.0	82.3	86.1
EPS (cps)	25.0	22.9	24.0
P/E	14.1x	15.3x	14.6x
EV / EBIT	7.9x	8.5x	8.1x
DPS (cps)	8.0	8.0	8.0
Dividend Yield	2.3%	2.3%	2.3%
N.D. / equity	-31%	-31%	-29%

Source: Hartleys Research. *normalised



Author:

Oliver Stevens
Industrial Analyst
Ph: +61 8 9268 2879
e: oliver.stevens@hartleys.com.au

SUMMARY MODEL

Austal Limited (ASB)					Recommendation: Neutral				
Company Information					Profit & Loss (\$m)				
Date	24 Aug 2020			100 Clarence Rd	6/19A	6/20A	6/21F	6/22F	
Share Price	\$3.51			Henderson WA, 6166	Revenue	1,851	2,086	1,962	1,985
52 Week High-Low	\$4.99-\$2.25			Ph: (08) 9410 1111	EBITDA	135.0	176.1	165.2	170.4
Dil. Market Cap (\$m)	\$1,282			www.austal.com	Depn & Amort.	-42.2	-45.7	-46.0	-46.0
Net Debt (\$m)	-\$272				EBIT	92.8	130.4	119.2	124.4
Enterprise Value (\$m)	\$1,010				Net Interest	-7.2	-6.9	-6.4	-6.4
Ordinary Shares	359.1				PBT	85.6	123.5	112.7	117.9
Fully Diluted Shares	365.3				Tax	-24.2	-34.5	-30.4	-31.8
					NPAT	61.4	89.0	82.3	86.1
Price Target	\$3.44				Pre-tax Adjustments	11.0	0.0	0.0	0.0
Upside / Downside	-2%				Adjusted EBITDA	146.0	176.1	165.2	170.4
Dividend Yield - FY20	2%				Adjusted EBIT	103.8	130.4	119.2	124.4
Total Return	0%				Post-tax Adjustments	7.7	0.0	0.0	0.0
					Adjusted NPAT	69.1	89.0	82.3	86.1
Price Target					Reported EPS (basic, wghtd)	17.6	25.0	22.9	24.0
12 Month Price Target	\$3.44				Normalised EPS (dil, wghtd)	19.5	24.7	22.6	23.6
P/E (FY20) at price target - Reported EPS	13.8x				DPS (cps)	6.0	8.0	8.0	8.0
P/E (FY21) at price target - Reported EPS	15.0x				Franking	0%	0%	0%	0%
Div. Yld (FY20) at price target	2.3%				Payout Ratio	30.7%	32.4%	35.5%	33.9%
Div. Yld (FY21) at price target	2.3%								
Multiples (\$/price at \$3.51)					Cashflow Statement (\$m)				
P / E (basic, weighted)	20.0x	14.1x	15.3x	14.6x	6/19A	6/20A	6/21F	6/22F	
P / E (nom, diluted, weighted)	18.0x	14.2x	15.6x	14.9x	Cash from Operations	176.5	182.7	118.5	128.9
					Net Interest Paid	-4.7	-4.7	-6.4	-6.4
Dividend Yield	1.7%	2.3%	2.3%	2.3%	Tax Paid	-7.3	-13.6	-17.3	-15.2
EV/EBITDA multiple	7.9x	5.8x	6.1x	5.9x	Net Operating Cash Flow	164.5	164.5	94.8	107.3
EV/EBIT multiple	11.2x	7.9x	8.5x	8.1x	Capital Expenditure	-41.5	-16.7	-50.0	-70.0
					Acquisitions	-1.6	-1.7	0.0	0.0
Price / Book Value	2.0x	1.7x	1.6x	1.4x	Other (Inc Investments, Asset sales etc)	3.9	0.2	0.0	0.0
Price / NTA	2.0x	1.7x	1.6x	1.5x	Net Investing Cash Flow	-39.2	-18.2	-50.0	-70.0
					Proceeds from Equity Issues	1.0	0.0	0.0	0.0
					Net Change in Debt & Leases	-10.7	-6.7	0.0	0.0
					Dividends Paid	-19.2	-20.6	-28.7	-28.7
					Other	7.7	0.0	0.0	0.0
					Net Financing Cash Flow	-21.3	-27.2	-28.7	-28.7
					Movement in Cash	104.0	119.1	16.0	8.6
Ratios					Balance Sheet (\$m)				
ROE (NPAT / Equity)	10%	12%	10%	10%	6/19A	6/20A	6/21F	6/22F	
ROA (EBIT / Total Assets)	7%	10%	9%	9%	Cash	276	397	413	421
ND / ND + Equity	-19%	-45%	-44%	-41%	Receivables	225	144	136	137
ND / Equity	-16%	-31%	-31%	-29%	Inventories	167	144	135	137
Net Interest Cover (EBIT)	12.8x	18.9x	18.5x	19.3x	Other	13	13	13	13
Revenue growth	33%	13%	-6%	1%	Total Current Assets	681	697	696	708
EBIT growth - Adj.	63%	26%	-9%	4%	Property, Plant & Equipment	588	610	614	638
NPAT growth - Adj.	84%	29%	-8%	5%	Intangibles	21	22	22	22
EPS (dil, wghtd) growth	81%	26%	-9%	5%	Other	37	38	38	38
EBITDA Margin - Adj.	8%	8%	8%	9%	Total Non Current Assets	646	671	675	699
EBIT Margin - Adj.	5%	6%	6%	6%	Total Assets	1,327	1,368	1,371	1,407
					Accounts Payable	202	157	148	149
					Payments in advance	120	95	40	0
					Interest Bearing Liabilities	51	9	5	5
					Provisions	85	80	85	90
					Other	15	9	9	9
					Total Current Liabilities	475	350	287	254
					Accounts Payable	0	0	0	0
					Interest Bearing Liabilities	123	156	160	160
					Other	99	113	113	113
					Total Non Current Liabilities	222	270	273	273
					Total Liabilities	697	619	560	527
					Net Assets	631	749	811	880
					Net Asset Value / Share (\$)	1.79	2.10	2.26	2.45
					NTA / Share (\$)	1.73	2.04	2.20	2.39
					Net Debt (net cash)	-102	-231	-248	-256
Share Data									
Ord Issued shares (m)	353.4	356.7	359.1	359.1					
growth	0.7%	0.9%	0.7%	0.0%					
Weighted ave shares (m)	349.6	356.2	358.7	359.1					
growth	1.0%	1.6%	0.7%	0.1%					
Diluted shares wghtd (m)	354.1	360.8	364.9	365.3					
growth	1.7%	1.9%	1.1%	0.1%					
Directors									
Substantial Shareholders									
John Rothwell (Non-Exec. Chairman)	John Rothwell			9.0%					
David Singleton (MD / CEO)	Blackrock			5.0%					
Giles Everist (NED)									
Sarah Adam-Gedge (NED)									
Chris Indermaur (NED)									
Analyst: Oliver Stevens									
Phone: +61 8 9268 2879									
Sources: IRESS, Company Information, Hartleys Research									

FY20 RESULT SUMMARY

Fig. 1: FY20 Result Summary

P&L	FY19	FY20	Chg	1H20a	2H20a
Revenue	1,851	2,086	13%	1,039	1,047
Gross Profit	189.9	239.3	26%	109.2	130.1
Expenses	-68.2	-72.9		-32.7	-40.2
EBITDA	135.0	176.1	30%	84.4	91.8
Depn & Amort.	-42.2	-45.7		-24.4	-21.3
EBIT	92.8	130.4	41%	59.9	70.5
Net Interest	-7.2	-6.9		-2.9	-4.0
PBT	85.6	123.5	44%	57.1	66.5
Tax	-24.2	-34.5		-16.3	-18.2
NPAT	61.4	89.0	45%	40.8	48.2
EPS (basic)	17.6c	25.0c	42%	11.5c	13.5c
EPS (adj., fully diluted)	19.5c	24.7c	26%	11.5c	13.5c
DPS	6.0c	8.0c	33%	3.0c	5.0c
Divisional EBIT					
USA	106.4	123.0	16%	65.6	57.5
Australasia	11.7	30.9	165%	8.2	22.7
Unallocated	-25.3	-23.5	7%	-13.9	-9.6
GP Margin	10.3%	11.5%	1%	10.5%	12.4%
EBIT Margin	5.0%	6.3%	1%	5.8%	6.7%

Source: Hartleys

As expected, ASB delivered an excellent headline result following upgrades to earnings guidance provided during FY20.

The result benefitted from a weaker AUD over the course of FY20. Across FY20 AUDUSD averaged ~0.671 (2H20 ~0.658) down from the FY19 average of ~0.714.

Management noted that ~45% (\$106m) of total revenue growth (\$235m) and ~20% (\$7m) of EBIT growth (\$38m) was attributable to the positive FX impact seen across the year.

- NPAT of \$89.0m was up 45% on FY19 (\$61.4m).
- EBIT of \$130.4m was up 41% on FY19 (\$92.8m) and compared favourably to May 2020 upgraded guidance for EBIT of >\$125m.
- Final dividend of 5.0cps, bringing FY dividend to 8.0cps (FY19 – 6.0cps)

Included in reported PBT numbers were the following:

- R&D tax credits, a regular and ongoing feature, provided an \$11.1m PBT boost (FY19 - \$6.1m).
- ASB also increased the provisions (by an undisclosed amount (FY19 - \$11m)) related to the ongoing cases with ASIC and certain US regulatory authorities. The remaining provision at year end stands at \$11.3m.
- Reversal of other provisions also had a positive impact on the result (we estimate ~\$5m).

DIVISIONAL PERFORMANCE

Fig. 2: Divisional Split

Summary	FY19	FY20	1H19	2H19	1H20	2H20
Total						
Revenue	1,852	2,086	852	1,001	1,039	1,047
Group EBIT	93	130	40	52	60	70
Margin	5.0%	6.3%	4.7%	5.2%	5.8%	6.7%
USA - Overall						
Revenue	1,473	1,604	687	786	805	799
EBIT	106	123	49	57	66	57
Margin	7.2%	7.7%	7.2%	7.3%	8.1%	7.2%
USA - Ships						
Revenue	1,248	1,311	597	651	675	636
EBIT	99	107	42	56	55	52
Margin	7.9%	8.1%	7.1%	8.7%	8.1%	8.2%
USA - Support						
Revenue	225	293	90	135	130	164
EBIT	16	17	7	9	12	5
Margin	7.3%	5.8%	7.7%	7.0%	9.4%	2.9%
USA EBIT - Other	-9	-1	0	-9	-2	1
Australasia						
Revenue	393	497	170	223	241	256
EBIT	12	31	4	8	8	23
Margin	3.0%	6.2%	2.4%	3.4%	3.4%	8.8%

Source: ASB, Hartleys

Group EBIT increased on the back of a strong 2H20, driven by contrasting impacts at a divisional level.

- US Ships Revenue and EBIT were both down in 2H20 notwithstanding the FX tailwind. This may in part be due to the impacts on productivity resulting from COVID-19, with ASB's Mobile facility having reported ~150 COVID cases.
- US Support margins were impacted in 2H20 due to timing associated with certain projects and operational start up difficulties in Singapore; ASB do not expect these issues to repeat.
- Australasian EBIT increased due to improved productivity across ASB's bases. In addition, management advises that EBIT received a ~\$6m boost from non-recurring one-off benefits, including provision releases and non-standard contract variations.

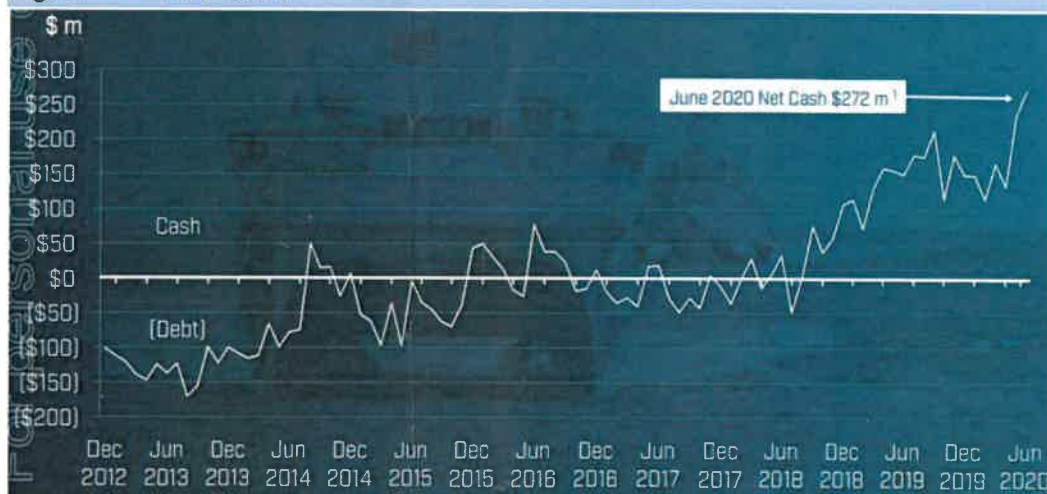
BALANCE SHEET & CASH FLOW

- Operating cash flow was again strong at \$164.5m
- Net cash at end FY20 was \$272m, well up on FY19 (\$151m).
- ASB notes that given the uncertainty surrounding COVID-19 potential impacts that it is comfortable maintaining a strong cash balance.

In addition, ASB will be committing ~US\$50m to expand its US steel shipbuilding capability and continues to evaluate other potentially significant investment opportunities.

The option to repay some of its outstanding Go Zone Bond debt (\$124m) will also be considered during 1H21.

Fig. 3: Net Cash



Source: ASB

FORECASTS

Fig. 4: Forecasts

Forecast Changes	FY20	FY21 old	FY21 new	Chg
Revenue	2,086	2,032	1,962	-3%
EBITDA	176.1	175.9	165.2	-6%
Depn & Amort.	-45.7	-51.0	-46.0	
EBIT	130.4	124.9	119.2	-5%
Net Interest	-6.9	-5.8	-6.4	
PBT	123.5	119.1	112.7	-5%
Tax	-34.5	-32.2	-30.4	
NPAT	89.0	87.0	82.3	-5%
EPS (basic)	25.0c	24.4c	22.9c	-6%
EPS (adj., fully diluted)	24.7c	24.0c	22.6c	-6%
DPS	8.0c	8.0c	8.0c	0%
EBITDA Margin	8.4%	8.7%	8.4%	
EBIT Margin	6.3%	6.1%	6.1%	
Tax Rate	28.0%	27.0%	27.0%	
AUDUSD rate	0.670	0.670	0.700	
Dividend Payout Ratio	32.4%	33.4%	35.5%	

Source: Hartleys

- ASB's order book at FY20 was \$4.3bn down from \$4.9bn at FY19. Contract awards of A\$852m were achieved during FY20, with no major ship builds being awarded in the US.
- ASB has not provided earnings guidance for FY21, noting the company is alert to the potential impact of COVID-19.

Our FY21 forecasts are reduced by ~5% as we wind back our US revenue and margin assumptions slightly, combined with the negative impact of increasing our AUDUSD forecast from 0.67 to 0.70 (current spot 0.718).

On the conference call management noted that each 1c change in exchange rate impacted Group EBIT by between \$1.2m - \$1.4m (positively and negatively).

VALUATION & PRICE TARGET

VALUATION & PRICE TARGET

We capitalise our FY21 earnings expectations to derive our Price Target of \$3.44ps, down from \$3.71ps previously.

Fig. 5: Price Target

ASB			
FY21 EPS (cps)	22.9		
PER	15.0x		
Valuation	\$3.44		

Implied Multiples at Target	FY20	FY21	FY22
EV/EBITDA	6.0x	6.0x	5.6x
EV/EBIT	8.1x	8.4x	7.7x
PER	13.8x	15.0x	14.4x
Dividend Yield	2.3%	2.3%	2.3%

Source: Hartleys

In regard to valuation, our methodology remains consistent. Our valuation remains at \$3.30 / share (Figure 6).

Fig. 6: Valuation - Sum of Parts

Sum of Parts	EBIT (\$m)	Multiple	US \$0.6bn	US \$0.9bn
Australasia	20	13x	260	260
Overhead	-25	10x	-250	-250
US - current book - NPV ₅			269	269
US - annual revenue - FY23+			800	1,200
Enterprise Value			1,080	1,480
Plus net cash (adj.)			106	106
Equity Value			1,186	1,586
Per Share			\$3.30	\$4.42

Source: Hartleys

NB. Our adjusted net cash figure is calculated using FY20 reported net cash (\$231m) adding back the 'debt' related to the CCPB financing agreement (\$41m) and then deducting progress payments made in advance (\$95m) and an additional \$70m (~\$US50m) representing ASB's commitment to extend its steel shipbuilding capability over the next two years.

Under the above US annual revenue scenario we make the following assumptions:

- EBIT margins of 7.0%
- USD/AUD exchange rate of 0.70.
- Tax rate of 25%.
- Discount rate of 5.0%

Fig. 7: Key assumptions and risks for valuation

Assumption	Risk of not realising assumption	Downside risk to valuation if assumption is incorrect	Comment
Austal USA generates ~US\$600m of annual revenue from FY23 forward.	Moderate	Moderate	With the US Navy looking to have 355 vessels by 2030, we expect Austal USA to have a number of opportunities which will aid in delivering revenue of around this level.
US EBIT margins of 7% going forward.	Moderate	Moderate	The ability to generate sustainable margins is dependent on operational efficiencies being achieved. At the start of new vessel programs this is higher risk given the nature of first in class vessel builds.
Sustainable EBIT of \$20m from Australasian operations.	Moderate	Low	Recent investments in capacity expansions coupled with the RAN contract success provides a foundation for this level of earnings to be achieved on an ongoing basis.
Conclusion	<p>ASB is well-positioned at present, it has a strong order book and with a balance sheet in good shape to take advantage of any opportunities that may come its way. We see risks to ASB, including, but not limited to:</p> <ul style="list-style-type: none"> - US Federal Authorities Investigation. In January 2019 ASB announced that the company's US division was assisting US regulatory authorities with investigations into a number of areas of ASB's US operations. ASB's 2020 Annual Report notes "While the Group is not aware of any wrongdoing or all of the specific matters currently being investigated, it is possible that these proceedings could lead to civil or criminal penalties, damages, and / or suspension or debarment from future US Government contracts..." - ASIC Investigation. Also announced in January 2019, ASB advised that it was assisting with an investigation by ASIC related to announcements regarding earnings from the LCS program. - Vessel delivery postponement. ASB notes that due to COVID-19 the delivery schedule for one of its vessels has seen a material delay, which has triggered a potential cancellation right. ASB notes that the client has advised on numerous occasions that it has no intention of cancelling the contract. If, however, the client did cancel the contract, ASB would be required to repay Euro64.2m (~\$A106m) in milestone payments received to date, with ASB then taking possession of the vessel for resale. - US Navy concentration. The US Navy is by far the largest individual client of ASB. Any changes to US Navy policy, budget and / or any other decision that impacts on ASB's current and potential future work with the Navy, could impact the company materially. - AUD/USD Exchange Rate. With a significant portion of ASB's earnings derived from its US operations, translation of earnings to AUD is materially influenced by the prevailing exchange rate. - Ability to continually fill the order book. The ship building industry is by its nature dependent on large orders. ASB, as it has needed to do throughout its history, will need to continually replenish its order book. Timing of orders can also influence period to period swings in earnings and cash flow. - Contract delivery. Contracts typically contain terms for delivery dates and specifications. Inability to meet these terms could impact financially and reputationally on ASB. 		

Source: Hartleys