

CODAN LIMITED

BUY
Growth on ~12x P/E with ~\$30m net cash
Technology Hardware & Equipment / Electronic Equipment & Instruments
1 November 2018

COMPANY UPDATE

Ticker	CDA
Stock Price	\$3.00
Target Price	\$3.64
Forecast Capital Return	21.3%
Forecast Dividend Yield	5.3%
Estimated Total Return - 12 Mth Forward	26.7%

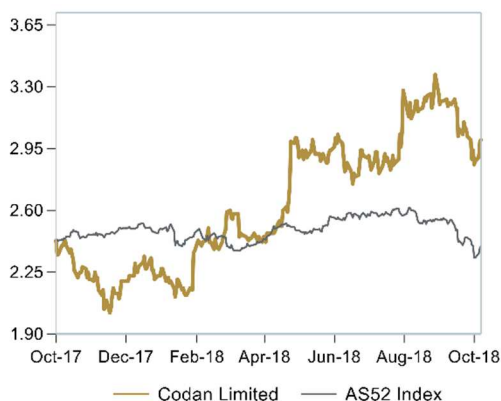
Company market data

Market Cap.	\$534.6m
Free Float (%)	61.8
Enterprise Value	\$506.9m
52 Week Range	\$2.02 - \$3.37
Shares Out.	178.2m

Estimates changes	2018a	2019e	2020e	2021e
Core NPAT - <i>old</i>	39.8	43.0	41.6	46.6
Core NPAT - <i>new</i>	39.8	44.0	41.9	46.6
% Change	0.0	2.4	0.8	0.0
Core EPS dil. (€) - <i>old</i>	22.1	23.8	23.1	25.9
Core EPS dil. (€) - <i>new</i>	22.1	24.4	23.3	25.9
% Change	0.0	2.4	0.8	0.0
DPS (€) - <i>old</i>	15.5	13.5	13.1	14.7
DPS (€) - <i>new</i>	12.5	15.0	14.4	16.0
% Change	(19.4)	11.7	9.8	8.9

All figures are in AUD unless otherwise specified.

Share price performance

Codan Limited vs. AS52 (rebased index)


Analyst

Ronan Barratt
+61 2 8288 5426
ronan.barratt@moelisaustralia.com

EVENT

FY18 AGM. Key commentary included:

- “Have made a good start to the year”
- Expect NPAT “in the range of \$20m-\$22m” for 1H FY19 (vs. MOE \$21.8m), however this assumes sales of gold detectors slow to “base-business levels” in 2Q FY19.
- Metal Detection “has started FY19 very strongly” primarily due to opening new markets.
- Mining Technology: CAT and BHP works are “progressing well”. Management expect Minetec sales “to be around \$15m in FY19” and believe business “could double in size over the next few years”.
- Radio Communications: “made a good start to the year and will deliver a stronger result in FY19” (vs. FY18).
- Defence: Revenue expected in FY20.

We note that CDA has flagged its CEO “will be selling up to 100,000 shares between now and Christmas to meet some personal tax liabilities”

IMPACT

We upgrade our FY19 NPAT estimates by 2.5% to \$44.0m to reflect the better than estimated 1Q FY19.

INVESTMENT VIEW

The FY18 result highlights the benefits of CDA’s strong product investments (~\$20m p.a.) undertaken over recent years, with contributions now made from a growing range of new products & markets.

We view CDA’s ~12x FY19 P/E as attractive given:

- Growth being experienced across all business divisions, with Minetec division yet to be monetised.
- High Returns on Invested Capital (~25% ROIC).
- Proven track record of re-investing capital at high rates of return (~66% Return on Incremental Capital across FY16-FY19e).
- ~\$30m net cash balance sheet providing scope for acquisitions or enlarged dividends (not included within our estimates).
- Earnings diversifying across both product & geography.
- Proven depth of product replacement cycle in Metal Detection with strong barriers to entry (African distribution channels, technology IP).

 Maintain **BUY** rating. **\$3.64** target price.

Y/E Jun 30	2018a	2019e	2020e	2021e
EBITDA	70.6	81.0	78.3	85.4
EV/EBITDA	7.2x	6.3x	6.5x	5.9x
Core NPAT	39.8	44.0	41.9	46.6
Core EPS (Diluted) (€)	22.1	24.4	23.3	25.9
P/E	13.5x	12.3x	12.9x	11.6x
EPS growth	(12.3%)	10.3%	(4.7%)	11.2%
DPS (€)	12.5	15.0	14.4	16.0
Yield	4.2%	5.0%	4.8%	5.3%
DPS growth	(3.8%)	20.3%	(4.5%)	11.7%
Dividend Payout Ratio	56.4%	61.6%	61.7%	62.0%

All figures are in AUD.

EARNINGS ESTIMATES

MOE earnings estimates are set out below.

The only key change to our prior estimates relates to an additional ~\$1m of EBIT for the Metal Detection business to reflect the better than expected 1Q FY19.

Figure 1: Earnings Estimates

	FY17a	FY18a	1H19e	2H19e	FY19e	FY20e
EBIT						
Metal Detection	62	64	29	31	60	54
<i>Margin</i>	42%	39%	39%	39%	39%	37%
Radio	20	7	9	9	17	18
<i>Margin</i>	28%	12%	24%	24%	24%	23%
Mining Technology	0	1	1	1	2	5
<i>Margin</i>	5%	8%	10%	10%	10%	16%
Corporate	-20	-18	-9	-11	-19	-21
<i>% Group Sales</i>	-9%	-8%	-7%	-8%	-8%	-8%
Group EBIT	62	54	30	30	60	57
<i>Group EBIT Margin</i>	27%	23%	25%	24%	24%	22%
NPAT	45	40	22.3	22.4	44.0	41.9
EPS	25.2	22.1	12.4	12.4	24.4	23.3
DPS	13.0	12.5	7.5	7.5	15.0	14.4
Valuation						
EV/FCF					12.4 x	9.9 x
Return on Invested Capital					26%	24%
P/E					12.1 x	12.7 x
EV/EBITDA					6.3 x	6.5 x

Source: Company, Moelis Analysis.

Profit and Loss (\$m)	2017a	2018a	2019e	2020e	2021e
Revenue	226.1	229.9	244.2	257.3	280.5
<i>Growth</i>	33.4%	1.7%	6.2%	5.3%	9.0%
EBITDA	75.7	70.6	81.0	78.3	85.4
<i>Growth</i>	80.4%	(6.7%)	14.7%	(3.3%)	9.1%
Dep'n & Amort	(14.1)	(16.7)	(21.4)	(21.8)	(22.5)
EBIT	61.6	53.9	59.6	56.5	62.9
<i>Growth</i>	110.7%	(12.5%)	10.5%	(5.2%)	11.4%
Net Interest Expense	(0.9)	(0.7)	0.7	0.8	1.1
Profit Before Tax	60.7	53.2	60.3	57.3	64.1
Tax	(16.0)	(13.3)	(16.3)	(15.4)	(17.4)
<i>Tax Rate (%)</i>	26.3%	25.1%	27.0%	26.9%	27.2%
Minorities	0.0	0.0	0.0	0.0	0.0
NPAT (Underlying)	44.7	39.8	44.0	41.9	46.6
<i>Growth</i>	112.0%	(10.9%)	10.5%	(4.7%)	11.2%
One-Off Items	0.0	0.0	0.0	0.0	0.0
NPAT (Reported)	44.7	39.8	44.0	41.9	46.6
EPS (Underlying) (€)	25.2	22.1	24.4	23.3	25.9
<i>Growth</i>	111.9%	(12.3%)	10.3%	(4.7%)	11.2%

Balance Sheet (\$m)	2017a	2018a	2019e	2020e	2021e
Cash	21.4	27.7	29.0	41.3	55.3
Inventory	31.0	31.6	37.6	39.9	43.7
Current Receivables	20.6	29.8	32.5	34.5	37.8
PPE	12.0	12.5	13.8	15.1	16.5
Intangibles	140.4	146.4	146.9	148.2	150.9
Other	0.0	0.0	0.0	0.0	0.0
Total Assets	232.7	254.3	266.1	285.4	310.5
Current Payables	36.6	46.3	45.1	47.9	52.5
ST Debt	0.0	0.0	0.0	0.0	0.0
LT Debt	0.0	0.0	0.0	0.0	0.0
Provisions	7.7	7.8	10.0	10.6	11.6
Other	52.8	52.4	51.2	54.0	58.5
Total Liabilities	67.7	66.2	67.2	70.6	76.1
Net Assets	165.0	188.1	198.9	214.8	234.5
Equity & Reserves	105.9	107.0	100.7	100.2	101.8
Retained Profits	59.1	81.0	98.2	114.6	132.6
Shareholders' Equity	165.0	188.1	198.9	214.8	234.5
Minorities	0.0	0.0	0.0	0.0	0.0
Total Equity	165.0	188.1	198.9	214.8	234.5

Cashflow (\$m)	2017a	2018a	2019e	2020e	2021e
EBITDA	75.7	70.6	81.0	78.3	85.4
Net Interest	(0.8)	(0.5)	0.7	0.8	1.1
Tax	(1.5)	(22.6)	(20.9)	(15.4)	(17.4)
Δ in Working Capital	2.2	(0.1)	(9.9)	(1.6)	(2.5)
Other	14.4	0.8	2.2	0.6	1.0
Operating Cash Flow	89.9	48.2	53.0	62.8	67.6
<i>Growth</i>	86.5%	(46.4%)	10.0%	18.4%	7.6%
Capex	(23.7)	(22.0)	(23.2)	(24.4)	(26.6)
Acquisitions	0.0	0.0	0.0	0.0	0.0
Divestments	0.0	0.0	0.0	0.0	0.0
Other	0.0	(0.5)	0.0	0.0	0.0
Investing Cash Flow	(23.7)	(22.5)	(23.2)	(24.4)	(26.6)
Equity Raised	0.0	0.0	0.0	0.0	0.0
Dividends Paid	(17.7)	(19.6)	(28.5)	(26.1)	(27.0)
Net Borrowings	(26.9)	0.0	0.0	0.0	0.0
Other	0.0	0.0	0.0	0.0	0.0
Financing Cash Flow	(44.7)	(19.6)	(28.5)	(26.1)	(27.0)
FX / Non Cash Items	0.0	0.1	0.0	0.0	0.0
Change in Cash	21.6	6.3	1.3	12.3	14.0
Free Cash Flow	51.9	26.2	41.4	50.6	54.3

Valuation Summary	
Current Mkt Capitalisation	534.6
Shares on Issue	178.2
Last Price	3.00
12 Mth Target Price	3.64
Total Estimated 12 Mth Return	26.7%
12 Mth Fwd Capital Return	21.3%
12 Mth Fwd Dividend Yield	5.3%

Valuation Ratios	2017a	2018a	2019e	2020e	2021e
EPS (Underlying) (€)	25.2	22.1	24.4	23.3	25.9
<i>Growth</i>	111.9%	(12.3%)	10.3%	(4.7%)	11.2%
P/E (x)	11.9x	13.5x	12.3x	12.9x	11.6x
Small Industrials (ex Fin's)	16.5x	16.5x	15.1x	12.3x	16.5x
Premium / (Discount)	(28.0%)	(18.1%)	(18.7%)	4.9%	(29.9%)
EV/EBITDA (x)	6.7x	7.2x	6.3x	6.5x	5.9x
Small Industrials (ex Fin's)	11.0x	11.0x	10.7x	9.8x	9.1x
Premium / (Discount)	(39.1%)	(34.7%)	(41.5%)	(34.3%)	(35.0%)
DPS (€)	13.0	12.5	15.0	14.4	16.0
<i>Growth</i>	116.7%	(3.8%)	20.3%	(4.5%)	11.7%
Yield (%)	4.3%	4.2%	5.0%	4.8%	5.3%
Payout Ratio (%)	51.5%	56.4%	61.6%	61.7%	62.0%
Franking (%)	100.0%	100.0%	100.0%	100.0%	100.0%
NTA	24.6	41.7	52.1	66.6	83.5
NTA/Share (\$)	0.14	0.23	0.29	0.37	0.46

Performance Ratios	2017a	2018a	2019e	2020e	2021e
ROA	19.2%	15.7%	16.5%	14.7%	15.0%
ROE	27.1%	21.2%	22.1%	19.5%	19.9%
ROIC	31.6%	25.2%	21.9%	23.8%	25.6%
Net Debt (Cash) (\$m)	(21.4)	(27.7)	(29.0)	(41.3)	(55.3)
Net Debt/EBITDA (x)	(0.3x)	(0.4x)	(0.4x)	(0.5x)	(0.6x)
ND/(ND + Equity) (%)	(14.9%)	(17.3%)	(17.1%)	(23.8%)	(30.9%)
Interest Cover (x)	84.6x	76.9x	186.1x	94.8x	77.2x
Working Capital	(1.0)	8.0	15.8	16.7	18.3
Working Capital/Sales (%)	(0.5%)	3.5%	6.5%	6.5%	6.5%

Cash Flow Metrics	2017a	2018a	2019e	2020e	2021e
FCF/Share (\$)	0.29	0.15	0.23	0.28	0.30
Price/FCPS (x)	10.2x	20.4x	12.9x	10.6x	9.8x
Free Cash Flow Yield (%)	9.8%	4.9%	7.7%	9.5%	10.2%
Gross Cash Conversion	103.1%	101.2%	91.1%	99.8%	99.5%
Capex/Sales (%)	(10.5%)	(9.6%)	(9.5%)	(9.5%)	(9.5%)
Capex/Depreciation (x)	1.7x	1.3x	1.1x	1.1x	1.2x

Margins	2017a	2018a	2019e	2020e	2021e
EBITDA	33.5%	30.7%	33.2%	30.4%	30.5%
EBIT	27.2%	23.5%	24.4%	22.0%	22.4%
NPAT	19.8%	17.3%	18.0%	16.3%	16.6%

Valuation Methodology	
WACC (%)	10.0%
Discounted Cash Flow Valuation	3.42
Sum-of-the-Parts Valuation	0.000
Average Valuation	3.42
12 Mth Target Price	3.64

RESEARCH & SALES RESPONSIBILITIES
Equities

Simon Scott	Head of Equities	+612 8288 5418
Elliot Leahey	Operations Manager	+612 8288 5402
Jack Dyson	Desk Assistant	+612 8288 5401
Jacqui Irons	Corporate Broking	+612 8288 5427

Equities Sales & Trading

Angus Murnaghan		+612 8288 5411
Ian McKenzie		+612 8288 5404
Bryan Johnson		+612 8288 5412
Andrew Harvey		+612 8288 5428
Sam Clark		+612 8288 5410
Rodney Forrest		+612 8288 5403
Mitchell Hewson - <i>Head of Execution</i>		+612 8288 5417
Aaron Payne - <i>Real Estate</i>		+612 8288 5405

Equities Research
Real Estate

Hamish Perks	+612 8288 5419
Edward Day	+612 8288 5424
Ronan Barratt	+612 8288 5426

Industrials

Sean Kiriwan	+618 6555 8602
Sarah Mann	+612 8288 5407
Brendon Kelly	+612 8288 5413

US Distribution Partner - Weeden & Co.

Matthew McCloghry	+1 646 227 5575
<i>mccloghry@weedenco.com</i>	

email: firstname.lastname@moelisaustralia.com

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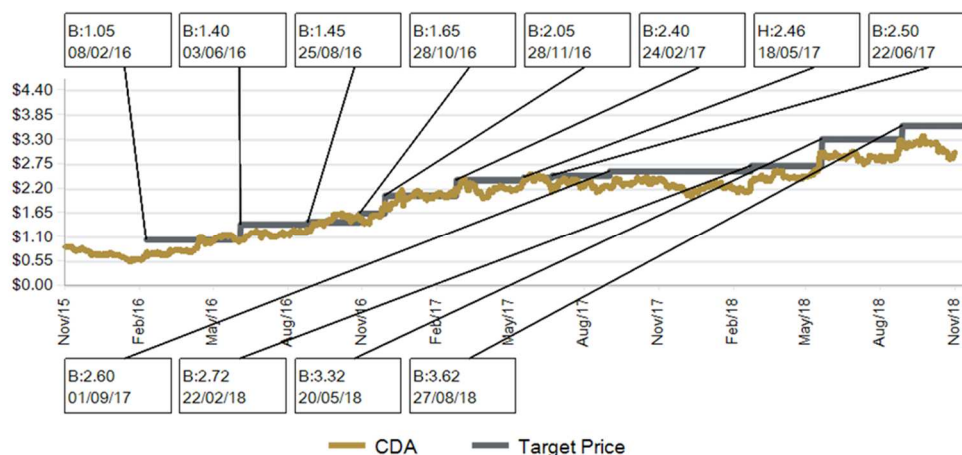
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Distribution of Ratings as at 1 November 2018

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3.8%	39.6%	54.7%

Rating and Price Target History: Codan Limited (CDA) as of 31/10/2018


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