



UNIVERSITY OF AUCKLAND  
**INVESTMENT**  
**CLUB**



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**Jarden is delighted to be sponsoring the UAIC's Stock Pitch Competition for Semester 1 2020. This competition replicates the challenging decisions many of our Jarden employees work through everyday, identifying value opportunities for clients to buy or sell stocks. We hope you enjoy the pitching experience, who knows, if you enjoy it so much, one day you might be publishing a buy/sell report for Jarden!**



## Introducing Jarden

**Connecting insights, people and capital  
to deliver exceptional outcomes.**

Jarden is New Zealand's leading investment and advisory group, offering share broking, portfolio management, investment banking, financial and economic research services.

We are a trusted provider of wealth management and investment advice to individuals, companies, institutions and governments. Our strong local expertise is backed by our strategic alliance with Credit Suisse Group.

For more information on Jarden, please visit our website at [www.Jarden.co.nz](http://www.Jarden.co.nz)

# Introduction



The value of a company is intrinsic to many forms of finance

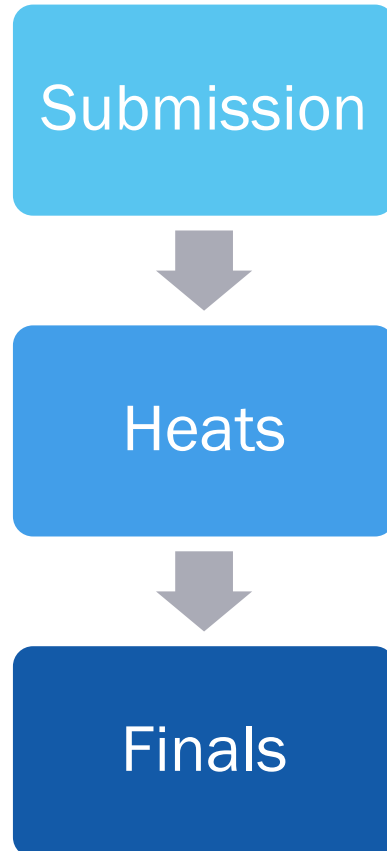
Public entities are valued in multiple ways. Transaction and traditional comps are the most intuitive methods but limit the modelling of new opportunities. At the other end of the spectrum, Discounted Cash Flow (DCF) methods are more thorough but introduce increasing levels of uncertainty from estimating a greater number of parameters.

No matter the method, valuation is a unique combination of art, skill and science.

**In this Competition, you will:**

- ✓ Prepare qualitative and quantitative analysis on a publicly listed company of your choice
- ✓ Use a set of valuation methods to value the equity
- ✓ Present your analysis on the company

# Structure



- ✓ Teams are to consist of 1-4 members.
- ✓ Competitors may be undergraduate and postgraduate students.
- ✓ Competitors must be UAIC members.
- ✓ Team constituents may be a combination of first timers and returning competitors. A team is classified as a **Beginner** or **Experienced** team. An experienced team has two or more members who are senior analysts on the UAIC Investment Committee or competed in the competition previously.
- ✓ Each team will prepare and present qualitative and quantitative analysis on an equity, publicly traded on the NZX or ASX. Presentations are 10 minutes followed by 5 or 10 minutes of Q&A.
- ✓ Qualitative Analysis includes: Business Analysis, Industry Analysis, Current Strategy, Competitive Advantages, Key Risks, and Mitigations.
- ✓ Quantitative Analysis includes: Valuation Techniques e.g. Book Value, Discounted Cash Flows, Comparable Analysis, Key Assumptions, A Comparison between Techniques, Sensitivity Analysis, and Buy/Sell/Hold Recommendation. Teams must do the following as a minimum requirements. **Beginner** teams must do a comparable analysis and may use the attached excel model to complete a DCF. **Experienced** teams must do a DCF and comparable analysis. Experienced teams are expected build on the model provided.
- ✓ Analysis will be summarised in an 8 -10 Slide PowerPoint excluding transition and appendix slides.
- ✓ There are three stages to the competition – Submissions, Heats, and Finals.

# Competition Steps

## Submission

- ✓ Receive competition materials via email 8pm 10<sup>th</sup> May 2020
- ✓ Select a publicly traded entity on the ASX or NZX
- ✓ Attend Tutorial and Workshop at 7pm on 12<sup>th</sup> May 2020 via Zoom
- ✓ Prepare your qualitative and quantitative analysis as a power point presentation
- ✓ Submit slides by 8pm 24<sup>th</sup> May 2020 by emailing [competitions@uaic.co.nz](mailto:competitions@uaic.co.nz) with the subject line: Team [X] – Stock Pitch

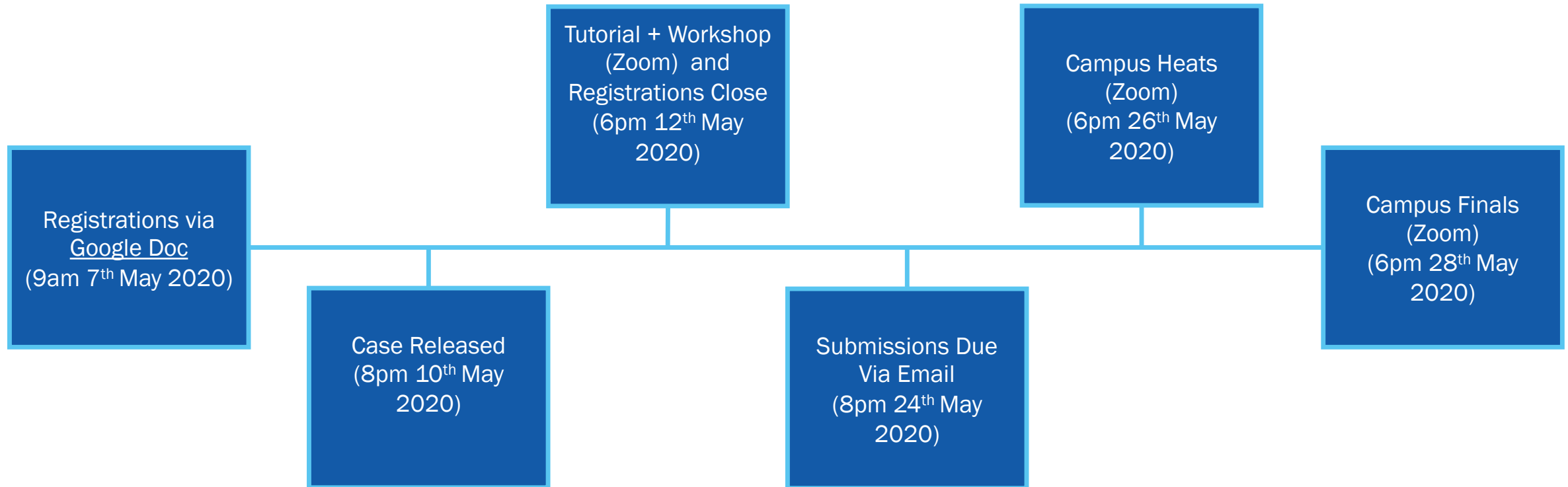
## Heats

- ✓ Six teams in total will be selected to present in the heats
- ✓ Judges will be a combination of Senior Investment Committee Equity Analysts, UAIC Executive and UAIC Alumni
- ✓ Presentations are to take place at 6pm 26<sup>th</sup> May 2020 via Zoom
- ✓ Presentations are 10 minutes followed by 5 minutes of Q&A

## Finals

- ✓ Three teams will be selected to present in the finals
- ✓ Judges will be a combination of UAIC Alumni and Industry Professionals
- ✓ Presentations are to take place at 6pm 28<sup>th</sup> May 2020 via Zoom
- ✓ Presentations are 10 minutes followed by 10 minutes of Q&A

# Timeline



# Prizes



The following prizes will be awarded

## Team Awards

- ✓ Best Overall Team (\$200 Prize)
- ✓ Best Beginner Team (\$100 Prize)
- ✓ Best Valuation (\$50 Prize)
- ✓ Best Qualitative Analysis (\$50 Prize)

## Individuals Awards

- ✓ Best Q&A (\$50 Prize)
- ✓ Best Female Speaker (\$50 Prize)



# Assessment

Qualitative	Description	Score
Business Analysis	<ul style="list-style-type: none"> <li>Demonstrated a fundamental understanding of the business model, market position, value drivers, and product mix</li> </ul>	/10
Industry Analysis	<ul style="list-style-type: none"> <li>Demonstrated a fundamental understanding of industry trends, market composition, and industry factors</li> </ul>	/10
Current Strategy	<ul style="list-style-type: none"> <li>Demonstrated a thorough understanding of the company strategy</li> </ul>	/5
Competitive Advantages	<ul style="list-style-type: none"> <li>Identifies and examines core competencies and competitive advantages</li> </ul>	/5
Key Risk and Mitigations	<ul style="list-style-type: none"> <li>Demonstrated an ability to identify risks, in particular in relation to a post COVID-19 landscape, and justifies mitigation strategies</li> </ul>	/10
Visual Presentation	<ul style="list-style-type: none"> <li>Clear and concise language, well formatted, and excellent use of charts, figures and tables</li> </ul>	/10

# Assessment

Quantitative	Description	Score
Valuation	<ul style="list-style-type: none"> <li>Demonstrates use of appropriate valuation methods with choices justified</li> </ul>	/10
Key Assumptions	<ul style="list-style-type: none"> <li>Identified and explained key assumptions. These include growth, CAPEX, NWC, OPEX, depreciation, amortisation assumptions, WACC, risk free rate, company beta, cost of equity and cost of debt</li> </ul>	/15
Sensitivity Analysis	<ul style="list-style-type: none"> <li>Demonstrated an ability to test the sensitivities of key parameters</li> </ul>	/5
Recommendation	<ul style="list-style-type: none"> <li>A clear recommendation supported by analysis</li> </ul>	/5
Q&A	<ul style="list-style-type: none"> <li>Depth and breadth of knowledge tested. Questions are answered completely, and all answers are consistent with the recommendation</li> </ul>	/15
Oral Presentation	<ul style="list-style-type: none"> <li>Competitors are confident, speak with clarity, and are persuasive</li> </ul>	/10

# Guidelines



Valuing a company can be daunting if you don't know where to start. The most experienced rely on external resources and well defined processes. We have prepared this guide to help inform how to conduct thorough analysis.

This guide outlines:

- ✓ Business Analysis
- ✓ Industry Analysis
- ✓ Strategy and Competitive Advantages
- ✓ Key Risks and Mitigations
- ✓ Key Assumptions
- ✓ Valuation Methods

It is important to tell a story. You are trying to form a narrative, informing the audience why they should follow your recommendation. Your analysis should support this story.

# Business Analysis

- ✓ Include an introduction to the business
- ✓ It is important to identify key metrics. These give a snapshot of the company. A subset of metrics includes: Current Share Price, Market Capitalisation (Current Share Price x The Number of Ordinary Shares Outstanding), Enterprise Value (Market Capitalisation + Total Debt – Cash and Cash Equivalents), Earnings per Share, Price / Earnings Ratios (Price / Earnings = Current Share Price / Earnings per Share). These may be calculated from the balance sheets found in the investors section of the companies website or from financial websites e.g. Yahoo Finance (<https://nz.finance.yahoo.com/>)
- ✓ Useful information includes: Ownership Structure, Operating Locations, Product Mix, Revenue Streams, Cost Structures, Value Chain Position, Board of Directors, Company History
- ✓ Information relating to the business can be found within annual reports, investor presentations and prospectuses, all of which are published on their company website
- ✓ It's important to identify other key qualitative factors which drive value for a business, such as their customer base, target markets, business model, product mix and the structure of their cost base

# Industry Analysis

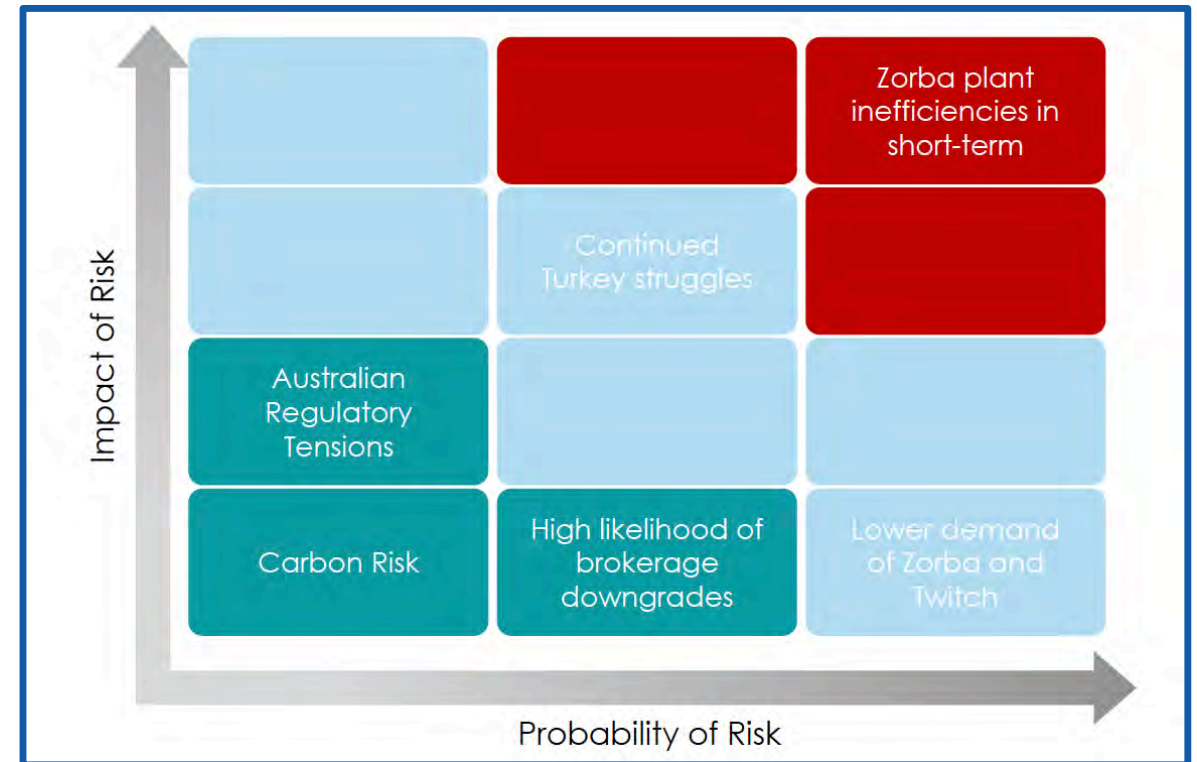
- ✓ It is important to outline the industry of the company you are valuing
- ✓ Important factors to consider include: An industry's maturity, key trends e.g. automation or sustainable movements, relationships with other industries, exposure to risks e.g. climate change, commodity price risks, financial market risk, or trade wars, barriers to entry, incumbents, market size (revenue), industry growth projections etc. This is not an exhaustive list but some examples of what to analyse. You want to pick the most important factors to help tell your narrative.
- ✓ This information can be found in industry reports (PwC, Deloitte, EY, KPMG, Bain & Company, BCG, McKinsey & Company, UBS, Goldman Sachs, Gartner etc) and articles (NBR, AFR, Financial Times, Wall Street Journal, Bloomberg etc)

# Strategy and Competitive Advantage

- ✓ Strategy and Competitive Advantages of your business inform why an investor should pick this business over another. Its important to consider how strategies compare to their competitors
- ✓ Examples of strategies include: growth through the acquisition of smaller companies, launching new products in existing markets, launching existing products in new markets, creating synergies between products, forming partnerships with other businesses etc
- ✓ Examples of competitive advantages include: technological advantages from patents, control on distribution channels, efficiencies from vertically integrated business models, or key relationships with other businesses etc
- ✓ This information can be found in the aforementioned industry reports, annual reports, prospectuses, and presentations

# Key Risks and Mitigations

- ✓ No business is risk free. It is important to identify these risks to inform the valuation and explain how the business minimises these risks
- ✓ Examples of risks and mitigations include: Jet fuel costs rise in the future from production shortages, mitigated by hedging fuel costs. Consumers changing products, mitigated by loyalty schemes etc
- ✓ This information can be found in annual reports, news articles, and industry reports
- ✓ It is important to rank risks, weighted by both impact and probability. Risk matrices are good ways to show which risks are most important to mitigate (Right)



# Key Assumptions

- ✓ Key Assumptions underpin a valuation. It is important to get them right. The following are some of the most important to consider:
- ✓ **Revenue Growth:** Increase/decrease in revenue per annum. Consider growth drivers
- ✓ **Operating Costs:** Set by gross profit margin (Gross Profit/Revenue). This ratio is usually consistent throughout the forecast period unless the business is witnessing cost reductions from economies of scale or external forces driving up costs
- ✓ **Depreciation and Amortisation Rates:** Usually a constant percentage of opening plant, property, and equipment (depreciation) or intangible assets (amortisation). May change if depreciation/amortisation methods change
- ✓ **Accounts Receivable:** Usually a percentage of revenues
- ✓ **Accounts Payable:** Usually a percentage of cost of sales / cost of goods sold
- ✓ **Inventory:** Usually a percentage of cost of sales / cost of goods sold
- ✓ **CAPEX:** Usually a percentage of opening plant, property, and equipment/intangibles



# Key Assumptions

- ✓ **Net Working Capital:** (Accounts receivable + Inventory – Accounts Payable)
- ✓ **Increase in Net Working Capital:** Current Net Working Capital – Previous Net Working Capital
- ✓ **Industry Beta:** Derived from a bottom up methodology using comparable companies or through looking at analysis done by academics e.g. Aswath Damodaran ([http://pages.stern.nyu.edu/~adamodar/New\\_Home\\_Page/datafile/Betas.html](http://pages.stern.nyu.edu/~adamodar/New_Home_Page/datafile/Betas.html))
- ✓ **Risk Free Rate:** Usually the government bond rate matching your forecast period (<https://www.rbnz.govt.nz/statistics/b2> for New Zealand)
- ✓ **Market Return:** Businesses give estimates on what the market return is e.g. (<https://www.pwc.co.nz/pdfs/2019pdfs/cost-of-capital-report-1.pdf> for New Zealand)
- ✓ **Company Tax Rate:** Tax rate for a country e.g. New Zealand is 28%
- ✓ **Long Term Growth Rate:** Assumption on how the business will grow long term. This informs a firm's terminal value

# Valuation Methods

The following websites explain different valuation methods and how to do a sensitivity analysis:

✓ **Discounted Cash Flows:**

<https://www.investopedia.com/terms/d/dcf.asp>

✓ **Comparable Analysis:**

<https://www.investopedia.com/terms/c/comparable-company-analysis-cca.asp>

✓ **Discount Dividend Model:**

<https://www.investopedia.com/terms/d/ddm.asp>

✓ **Sensitivity Analysis:** <https://www.wallstreetmojo.com/sensitivity-analysis-in-excel/>

# Analysis: SGM & MCK



The UAIC Investment Committee perform analysis on equities twice a week. This competition replicates what the committee does on a weekly basis.

Nehaal Ram, Athena Churchill, and Kevin Li analysed Sims Metal Management (SGM) as members of the UAIC Investment Committee.

The analysis on Millennium & Copthorne Hotels NZ Ltd (MCK) was completed by very experienced ex-UAIC Investment Committee members: Jillin Yan, Jenny Liu, Jonathan Chisholm, and James Thwaite. This pitch won the 2018 Stock Pitch Competition

Note: These examples are of a very high quality, both completed by very experienced UAIC Investment Committee Members. It is not the expectation for the competition.

These examples are appended to the back of this competition pack.

# Analysis: Financial Model



UAIC recognises this competition can be quite technical. We have produced a financial model, ‘a black box’, to make the valuation part of the competition less daunting.

This is a basic model to get the mechanics right. We still expect granularity in your analysis e.g. a breakdown of revenue segment growth or the depreciation schedules of different assets.

The narrative you tell using your analysis is most important.

The model will be released following the tutorial held via Zoom at 6pm on the 12<sup>th</sup> of May.

# End of Competition Pack

# Sims Metal Management

Pitched by: Nehaal Ram, Athena Churchill &  
Kevin Li



**SIMS**  
METAL  
MANAGEMENT

## Share Price (5 Years)

### ASX:SGM Adjusted Close



— ASX:SGM Adjusted Close



## Metrics

<b>Current price</b> (24/04/2020)	\$6.25	<b>Market cap</b>	\$1.40B
<b>52 week range</b>	\$5.520 - \$12.980	<b>Enterprise value</b>	\$1.55B
<b>Forward Dividend &amp; Yield</b>	\$0.25 (3.86%)	<b>3Y Historical EPS</b>	0.916

- Founded in 1917, Sims Metal Management Ltd is the largest listed metals recycling company globally
- The company specialises in ferrous and non-ferrous metal recycling, post-consumer electronic goods and municipal waste recycling
- Primary operations are located in the United States, Australia, New Zealand and the UK and 14 other countries
- Processes over 10 million tonnes of end-of-life vehicles, appliances and demolition scrap to be re-used as new steel, aluminium, copper and other commodities

## Investment Thesis

### International Market Dominance

- With over a century of organic growth and M&A, SGM is now the international leader of it's respective sectors

### Attractive industry

- Recycling volumes will continue to increase long-term, SGM is poised to increase EBITDA through international manufacturing & consumption

### Environmental Sustainability

- One of the world's 100 most sustainable companies. Index component of DJ Sustainability Index and renowned for exemplary corporate social responsibility

### Trading at a significant discount to historical averages

- Trade tensions, tailwinds in commodity prices from China and pessimistic market sentiment has affected SGM relative to the ASX200
- Price is 24% discount to intrinsic value due to overinflated market pessimism

## ASX:SGM Adjusted Close





# Sims Metal Management A century's worth of recycling



# 100 YEARS



1917

Albert G Sims starts a scrap metal collection business

1948

Albert G Sims Ltd listed on Australian Stock Exchange

1956

First export sales of steel scrap metal to Japan

1988

Entered the US metals recycling market with acquisition of LMC in California

2005

Merged with Hugo Neu, one of the largest exporters of scrap metal in the US

2007

Formed a joint venture with Adams Steel creating SA Recycling

2008

Acquired Metal Management, one of the largest recyclers in the US

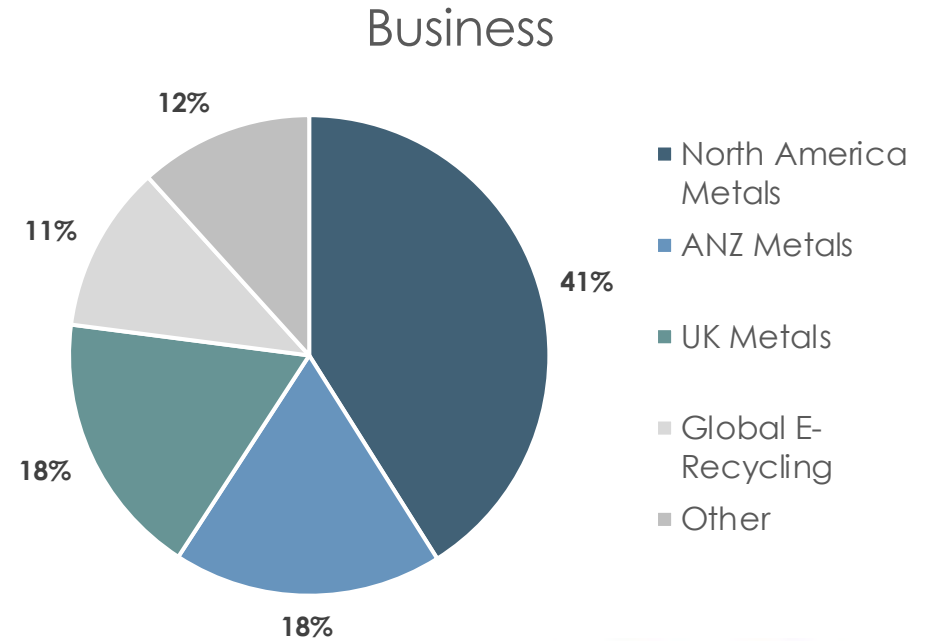
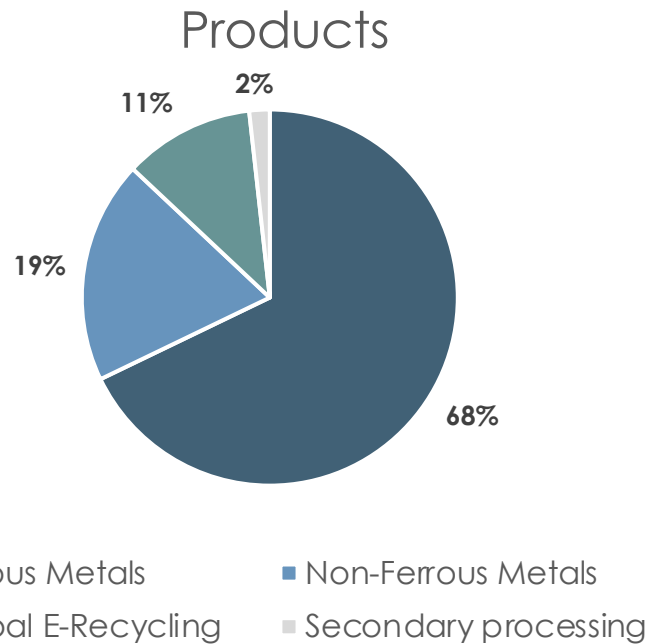
2017

Celebrated 100 years



# Sims Metal Management

## Well segmented revenue base

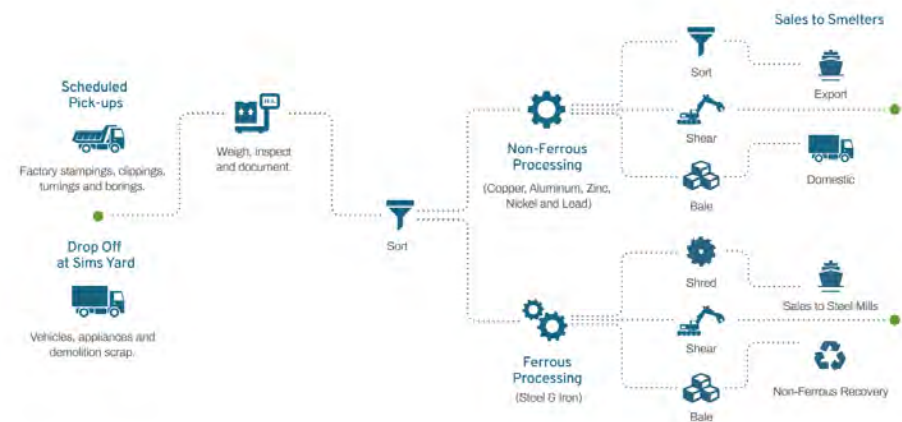


Ferrous Metals – Containing iron, used to make steel

Non-Ferrous Metals – Not containing iron compounds, used to make primarily aluminium

Global E-Recycling – safe disposals and recycling of electronic devices

Secondary processing – municipal recycling, global trading, and energy production

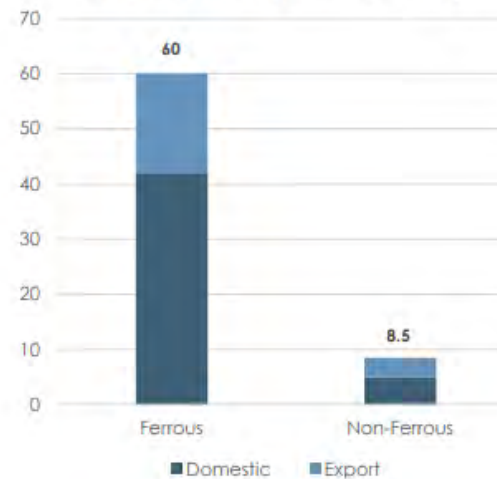


# Sims Metal Management Most Valuable Product – Ferrous Metals

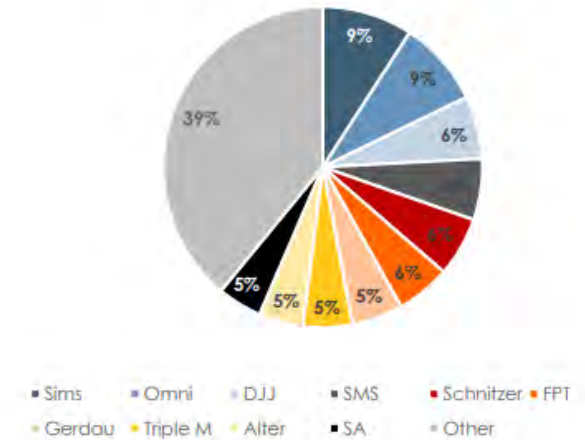


- SGM recycles 9.4m tonnes of ferrous metals, which makes up 67.8% in revenue
- Sourced through metal dealers, peddlers, auto wreckers, demolition firms and other generators of obsolete and industrial metal and turned into steel
- With ferrous production reaching maximum market shares across UK and ANZ, SGM intends to grow the US ferrous metal business ~40% by 2025
- Growth initiatives; feeder yard expansion, bolt on acquisitions, enhance metal yields and improve logistics
- Ready to play in export markets and meet customer demand for higher quality materials

USA Market Size (million tonnes)



Estimated USA Market Share by Volume

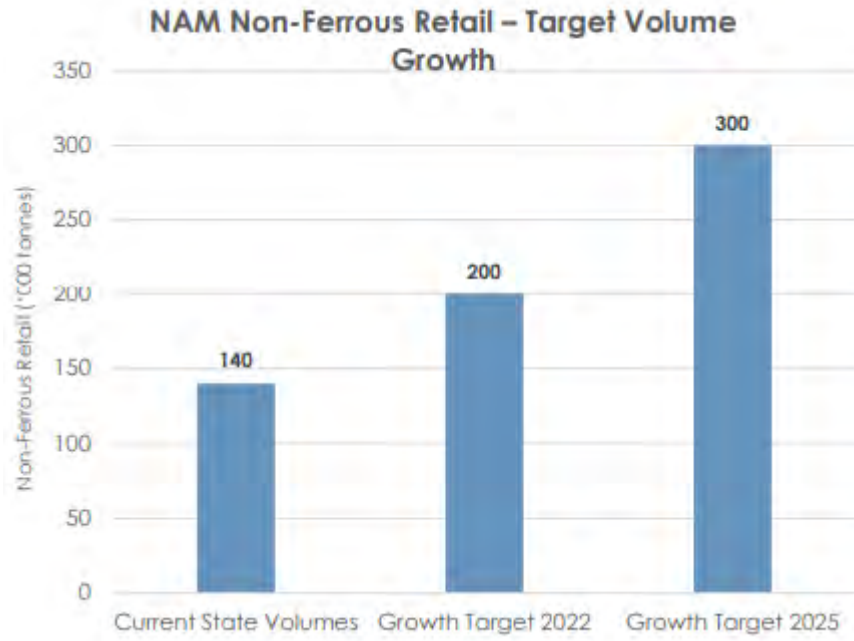


NAM Ferrous - Target Volume Growth



# Sims Metal Management

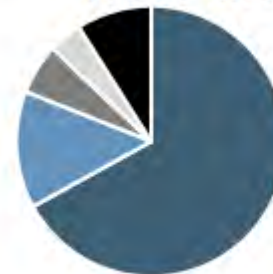
## Next up, Non-Ferrous Metals



- SGM recycles 430k tonnes of non-ferrous metals. These include aluminium, copper, lead and tin
- Double US non-ferrous business by FY2025, whilst continuing geographical diversification
- Growth initiatives; increase buying from source, product diversification, and inorganic opportunities
- FY19 saw a greater fall in non-ferrous shred sales price than shredder feed buy price, leading to lower EBITDA

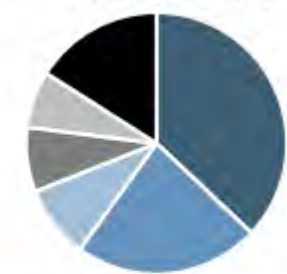


### Non Ferrous Export Sales Volume 1H18



■ China ■ India ■ Korea ■ Pakistan ■ Other

### Non Ferrous Export Sales Volume 1H19

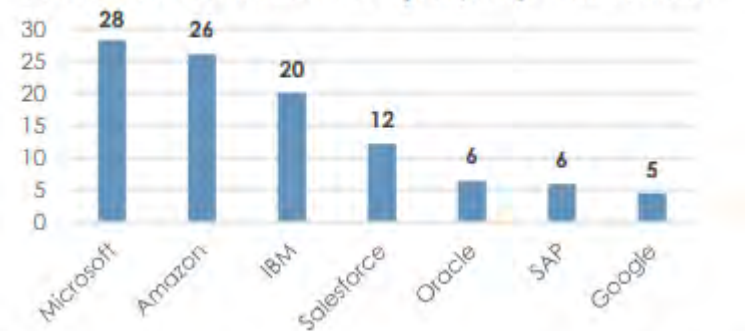


■ China ■ India ■ Malaysia ■ Korea ■ Pakistan ■ Other

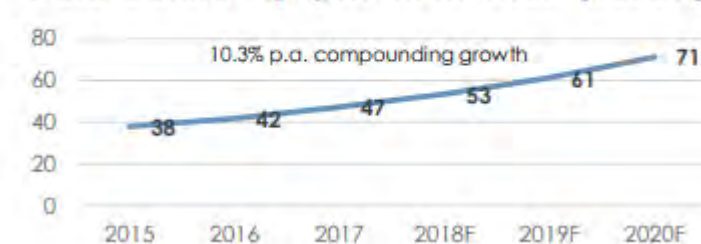
# Sims Metal Management Pioneering the E-Recycling movement

- SGM is ready to grow services for recycling the cloud, with projections for cloud recycling to be 10% by FY25 and being the OEM supplier of choice for recycled plastic
- 3 types of customers; cloud service providers, data centre hardware providers and large corporate clients
- Sims already has established relationships with most of the Fortune 100, and offers synergies with other Sims' lines
- Sim's E-Recycling is a first-mover globally, ready to capture the Infrastructure as a Service (IaaS) segment

**2018 Cloud Revenue<sup>1</sup> (US\$bn) estimated**



**Data Centre Equipment Market<sup>2</sup> (US\$bn)**



# Sims Metal Management

## Well diversified across segments and regions



### Sims Waste to Energy

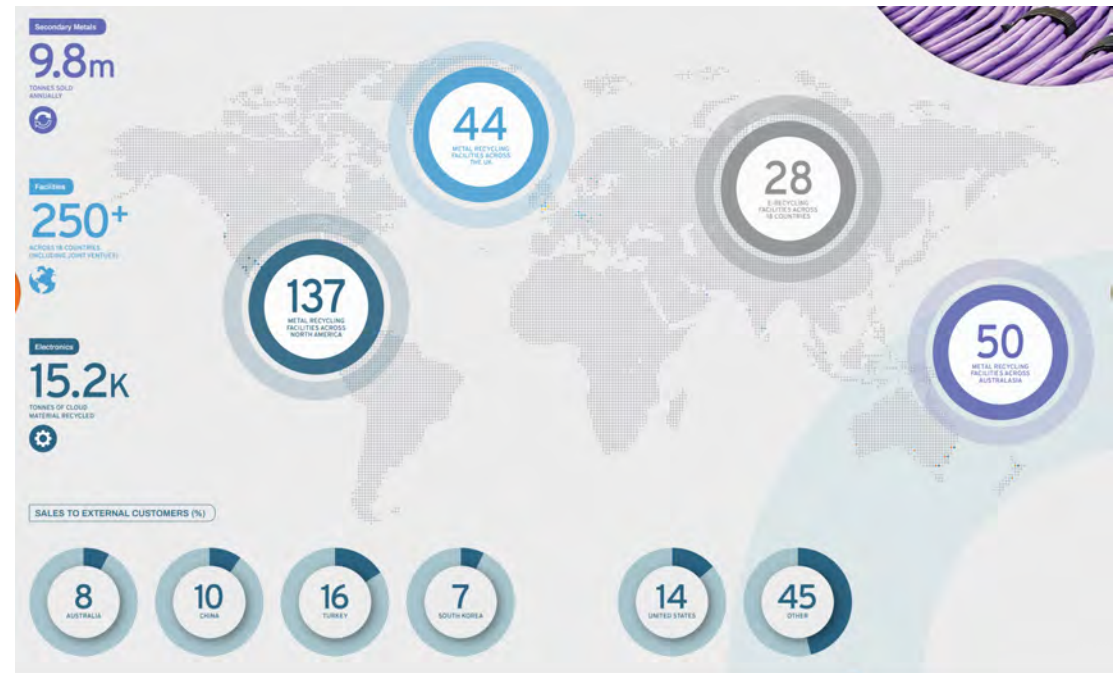
- Sims generate 1.3 millions tonnes of Automotive Shred Residue (ASR) per year that cost remove \$103 million in waste costs per annum
- Pipeline of WtE facilities will remove 75% of ASR costs

### Sims Energy

- Joint Venture with LMS Energy (landfill energy) to turn landfill gas into electricity generation
- Replicating LMS Business model in North America

### Sims Municipal Recycling

- Processes 500k tonnes of curbside material
- Tailwind pressures due to declining volume of plastic materials



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# *Industry*

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*Examining how Sims is underpinned  
by commodities & economies*



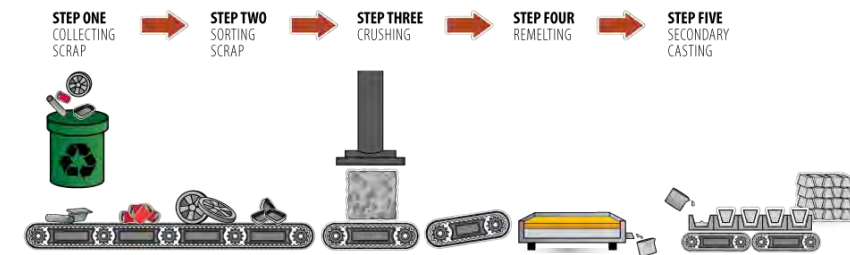
**Commodity Drivers**

- Global demand for recycled copper is projected upwards, driven by Chinese smelter needs
- New copper from a ore mine takes ~10 years, but additional capacity of copper is required for electric vehicles and buses
- Recycled aluminium is required by automobiles, packaging and construction. Aluminium is the second most used material in the automobiles industry
- FY19 saw a greater fall in non-ferrous shred sales price than shredder feed buy price, leading to lower EBITDA

**Economic Drivers**

- Hammered by trade wars, especially with heavy importer involvement i.e. China and Turkey
- Chinese smelters have a growing need for better quality products, hence Zorba Project in Adelaide

**RECYCLING ALUMINIUM**



**FINANCIAL REVIEW**

[Companies](#)   [Manufacturing](#)   [Recycling](#)   [Print article](#)

**Sims profit hit by trade wars, shipping costs**

Liam Walsh Reporter

— **Chanticleer**

**Sims Metals Management might be our biggest ASX trade war casualty**

*Chanticleer is Australia's pre-eminent business column.*



Updated Jan 21, 2019 – 4:39pm, first published at 11.06am

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# Strategy + Competitive Advantage

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Dissecting what makes  
Sims so special

# Sims Metal Management

## Continuing to lead the conversion of waste



- Sims will broaden its participation in the environmental sector to continue being the global leader in metals recycling, convert waste into energy and grow trends in recycling the cloud
- Sims purpose is to create long-term value by providing secure and sustainable management of resources within the circular economy
- This will lead to safer working sites and reductions in earnings volatility and operational risk



# Sims Metal Management

## Well planned to lead recycling

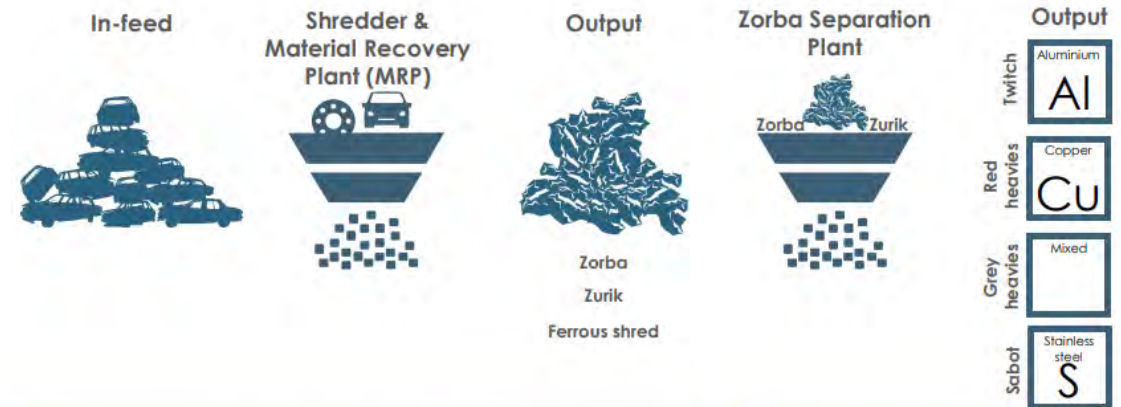


# Sims Metal Management Economic moats revolve around SGM



## Ferrous & Non-Ferrous Metals

- Zorba Separation Plant, national facility to upgrade Zorba and Zurik into smelter ready products
- Solves future demand uncertainty for semi-processed metals, increase in non-ferrous sales and direct sales to smelters

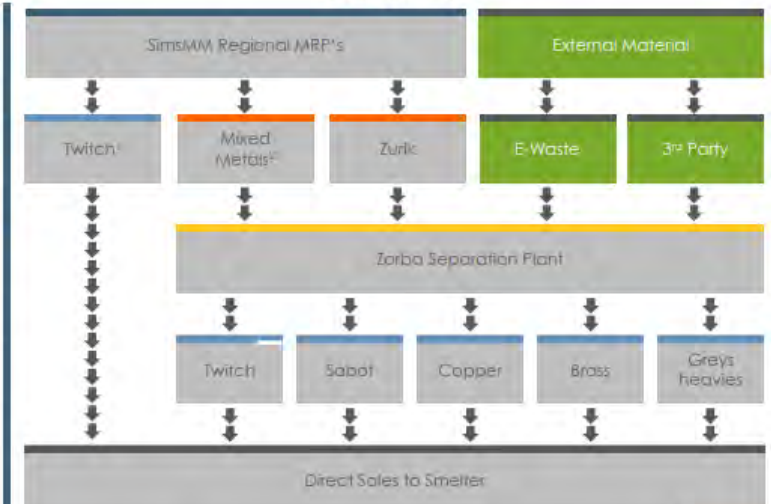


Shredding facility - Gillman      Zorba Separation Plant

### Old Process



### New Process



## E-Recycling

- First-mover advantage in laaS, providing metal recycling, component resale and security governance
- Already established business model, with closed-loop hardware recycling creating a circular economy
- E-Recycling business model is ready for scale and overpassing traditional shredding options



## The past, present and future of recycling

- Sims has business models, capital budgeting plans, expansion methods and R&D pipelines to succeed 30 years into the future
- Megatrends analysis is a reflection of Sims current and future strategy, helping them retain and grow market share

Area	Category	Megatrends	Impact to Sims
Social	Climate Change	Natural disasters are more frequent and violent driven by rising CO <sub>2</sub> emissions	Increased push towards recycled materials to reduce carbon emissions
		Global waste will increase	Higher landfill costs and need for solutions
Environmental	Waste	Advanced materials will change the nature and composition of goods	Increasing value of materials in waste streams and higher importance on separation
		Nuclear reactor decommissioning will generate radioactive waste to be handled	Need for development of economic solutions
		Trade in waste will decline with emphasis placed on management, recycling and reuse	Material separation will occur in the domestic market of material origin
Economic / Business	Water	There will be less plastic pollution with the advent of bio plastics	Declining volume of plastic materials for processing (Municipal)
		Increased demand and declining availability of freshwater in megacities	Need for development of economic solutions
Technological	Energy	Increased pollution of global oceans	Need for development of economic solutions
		Renewables will make up to 50% of the energy capacity growth by 2040	Increased supply of renewables risk cuts to government support from carbon permit sales
Political	Resource Sustainability	Energy storage & peer-to-peer (P2P) energy trading will revolutionise traditional utilities	Potential for easier sale of and purchase of energy at lower prices
		Declining availability of low cost & high grade mines across all commodities and minerals	Higher prices across all commodities and improved economics for material recovery
		Landfills mined for resources & energy	Increased opportunities for material recovery



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# *Risks*

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*How Sims is well equipped  
with operational risks*

**Risks**

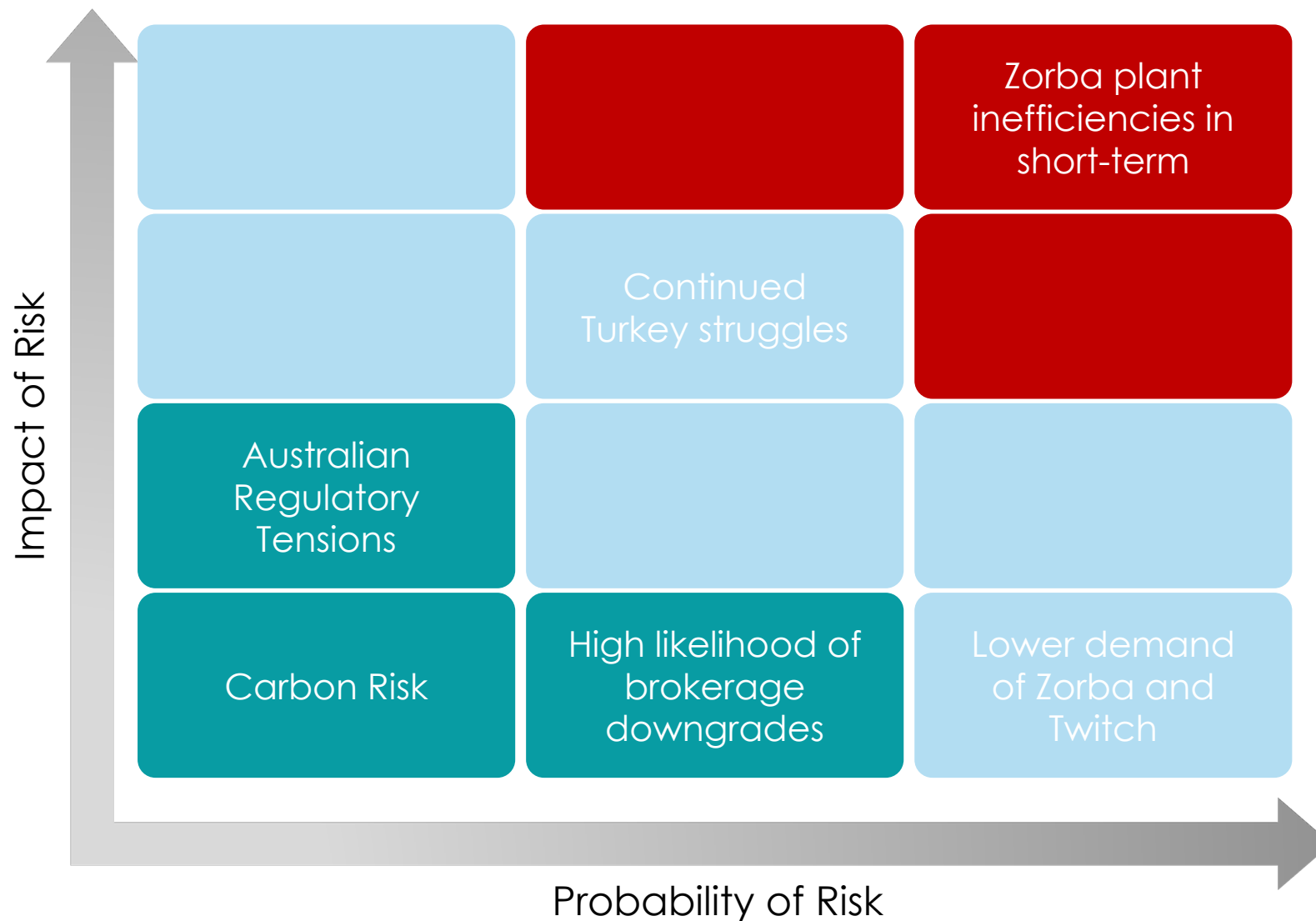
**Mitigations**

1. Significant changes in commodity prices or increased variance
2. Consumer demand shifting to higher quality ferrous and non-ferrous metals
3. Increased national and international freight/shipping costs
4. Increasing complexity of materials in goods
5. Weak cash and working capital movements

1. Short-term fluctuations, accounted for in Cash and Cash Equivalents
2. Zorba Separation Plant enabling the separation and processing of higher quality products
3. Typically recoverable through managing the buy price of metals
4. Zorba Separation Plant enabling the separation and processing of higher quality products
5. Worst case scenarios for cash management, natural hedges in relation to cash flow movements



Sims Metal Management  
Risks that are not mitigated





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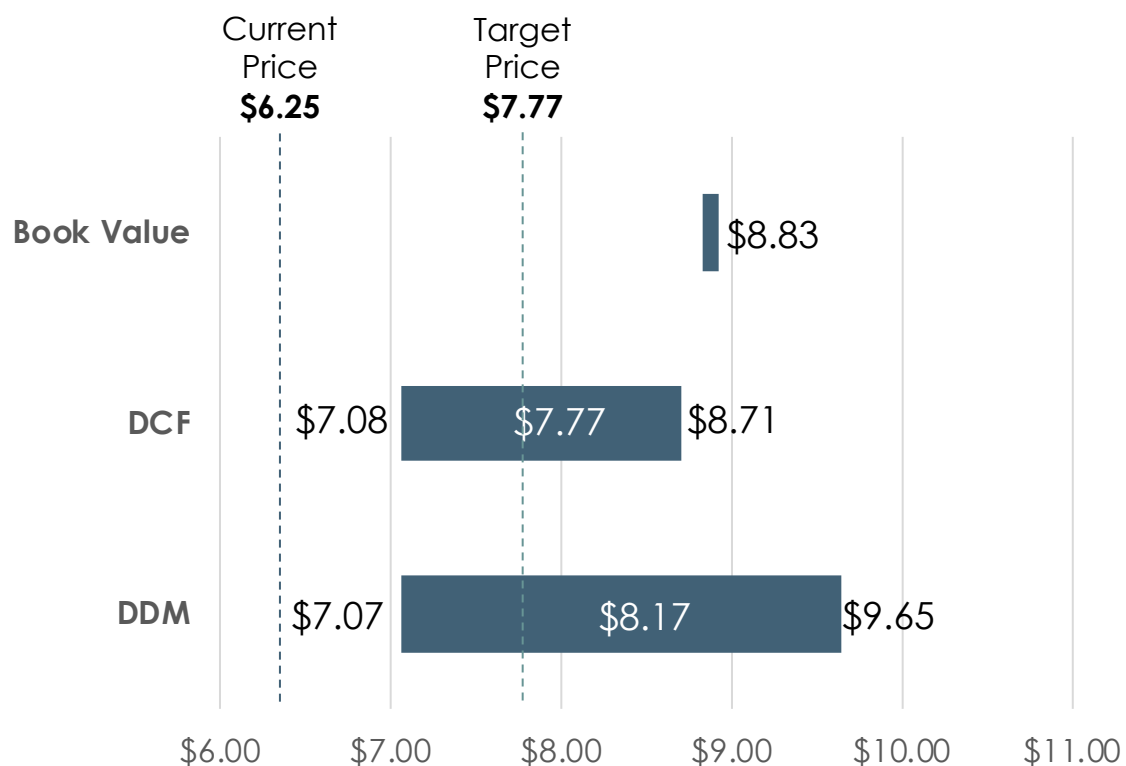
# *Valuing Sims Metal Management*

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*Looking at SGM with a  
quantitative lens*

# Sims Metal Management

## Valuation methods suggests undervaluation



### Key Assumptions

BV of NTA 30/06/2019  
Interim Report FY20

8.32 – 10.32% WACC,  
1.50 – 3.50% TGR

8.32 – 10.32% Cost of Capital,  
1.63 – 3.63% Dividend Growth

Method	Description	Positives	Limitations
<b>DCF</b>	SGM by 5 Year DCF	<ul style="list-style-type: none"> <li>✓ Accounts for SGM's stability of cash flows</li> <li>✓ Conservative for SGM</li> </ul>	<ul style="list-style-type: none"> <li>× Sensitive to a number of inputs</li> <li>× Equity Beta is skewed by current market conditions</li> </ul>
<b>DDM</b>	Gordon growth model	<ul style="list-style-type: none"> <li>✓ Doesn't account for current market conditions</li> <li>✓ Stable dividend history</li> </ul>	<ul style="list-style-type: none"> <li>× Doesn't factor intangibles, retention and asset-based business</li> </ul>
<b>Book Value</b>	Book NTA	<ul style="list-style-type: none"> <li>✓ Proxy of liquidation value</li> </ul>	<ul style="list-style-type: none"> <li>× Disregards earnings and capex</li> </ul>

# Sims Metal Management

## Our DCF indicates a valuation of \$1.6B



	FY19A	FY20F	FY21F	FY22F	FY23F	FY24F
Revenue	6,650	6,861	6,993	7,084	7,154	7,202
Operating Expenses	(6,371)	(6,571)	(6,696)	(6,781)	(6,846)	(6,890)
EBITDA	279	290	297	303	308	311
Less: D&A	(133)	(143)	(146)	(149)	(153)	(156)
EBIT	146	147	151	153	155	156
Taxation Expense	(66)	(31)	(32)	(33)	(33)	(33)
Plus: D&A	133	143	146	149	153	156
<b>Unlevered Net Income + D&amp;A</b>	<b>214</b>	<b>258</b>	<b>265</b>	<b>270</b>	<b>275</b>	<b>278</b>
<b>CAPEX</b>	<b>(207)</b>	<b>(176)</b>	<b>(180)</b>	<b>(182)</b>	<b>(184)</b>	<b>(185)</b>
<b>Δ OWC</b>	<b>30</b>	<b>(175)</b>	<b>(11)</b>	<b>(8)</b>	<b>(6)</b>	<b>(4)</b>
FCFF		(92)	74	81	85	89
Terminal Value						1,431
Share of Cash Flows After Valuation Date		<b>(23)</b>	<b>74</b>	<b>81</b>	<b>85</b>	<b>1,520</b>
Valuation Period		0.25	1.25	2.25	3.25	4.25
Discount Factor		0.98	0.89	0.82	0.75	0.68
Present Value		(23)	66	66	64	1,041
Net Present Value (EV)	1,214					
Net Debt	362					
<b>Equity Value</b>	<b>1,576</b>					
Shares Outstanding	203					
<b>Implied Price Per Share</b>	<b>\$7.77</b>					
Current Price Per Share	\$6.25					
Upside/(Downside)	24.37%					

### Key Assumptions

9.32% WACC

3.17% EBITDA as % of Revenue Margin Start

2.57% CAPEX as % of Revenue

9.99% D&A as % of PPE & IA

2.50% Terminal Growth Rate

### DDM

\$0.53 2019 Dividend, 2.53% Growth Rate

\$8.13 Implied Price by DDM

Sims Metal Management  
 Changes in assumptions still deliver a discount



		Long Term Growth Rate				
		1.50%	2.00%	2.50%	3.00%	3.50%
<b>WACC</b>	8.32%	\$7.95	\$8.35	\$8.81	\$9.36	\$10.02
	8.82%	\$7.53	\$7.86	\$8.25	\$8.71	\$9.25
	9.32%	\$7.16	\$7.44	<b>\$7.77</b>	\$8.16	\$8.60
	9.82%	\$6.83	\$7.08	\$7.36	\$7.69	\$8.06
	10.32%	\$6.54	\$6.76	\$7.00	\$7.28	\$7.60

		Dividend Growth Rate				
		1.63%	2.13%	2.63%	3.13%	3.63%
<b>WACC</b>	9.24%	\$7.11	\$7.64	\$8.26	\$8.98	\$9.83
	9.49%	\$6.88	\$7.38	\$7.96	\$8.63	\$9.41
	9.74%	\$6.67	\$7.14	<b>\$7.68</b>	\$8.30	\$9.02
	9.99%	\$6.47	\$6.91	\$7.42	\$8.00	\$8.67
	10.24%	\$6.28	\$6.70	\$7.18	\$7.72	\$8.34

## Investment Thesis

### International Market Dominance

- With over a century of organic growth and M&A, SGM is now the international leader of it's respective sectors

### Attractive industry

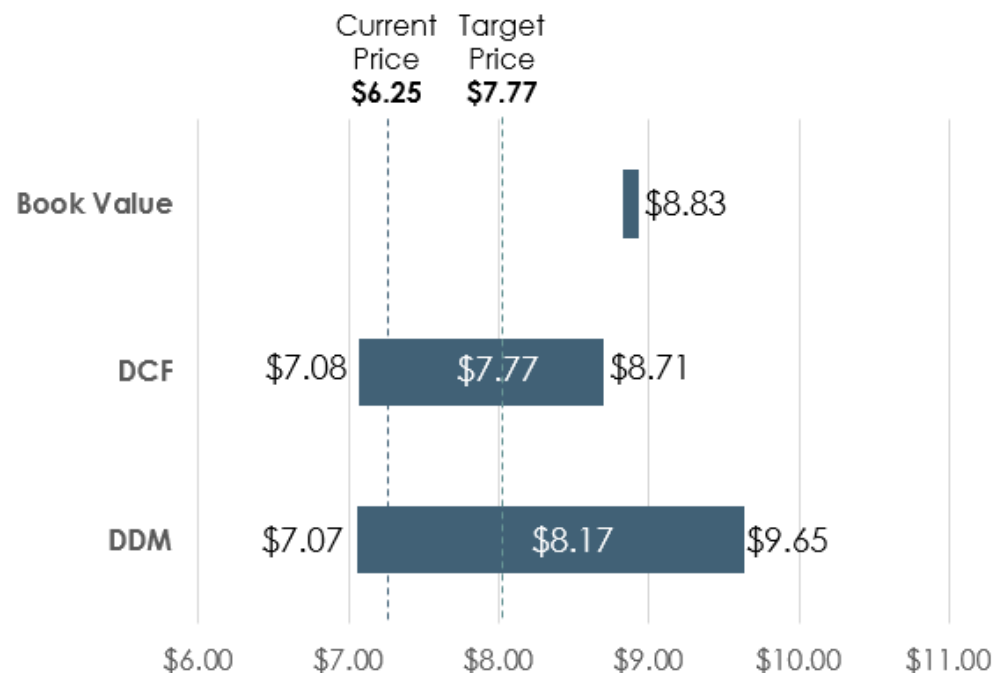
- Recycling volumes will continue to increase long-term, SGM is poised to increase EBITDA through international manufacturing & consumption

### Environmental Sustainability

- One of the world's 100 most sustainable companies. Index component of DJ Sustainability Index and renowned for exemplary corporate social responsibility

### Trading at a significant discount to historical averages

- Trade tensions, tailwinds in commodity prices from China and pessimistic market sentiment has affected SGM relative to the ASX200
- Price is 24.37% discount to intrinsic value due to overinflated market pessimism



# Sims Metal Management

Pitched by: Nehaal Ram



**SIMS**  
METAL  
MANAGEMENT



CABLE BOX by WC WENDT MTB



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# Appendices

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1. [Statement of Comprehensive Income](#)
2. [Statement of Financial Position](#)
3. [Statement of Cash Flows](#)
4. [COVID-19 Impact and Response](#)
5. [ANZ + NA Competitors](#)
6. [Asset Efficiencies](#)
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# Sims Metal Management

## Statement of Comprehensive Income



### Consolidated Statements of Comprehensive Income

For the year ended 30 June 2019

	Note	2019 A\$m	2018 A\$m
Profit for the year		152.6	203.5
<b>Other comprehensive income:</b>			
<i>Items that may be reclassified to profit or loss:</i>			
Changes in the fair value of cash flow hedges, net of tax	20	0.8	(2.2)
Foreign exchange translation differences arising during the period, net of tax	20	69.1	62.0
Recycling of foreign currency translation reserve on increase in ownership interest of joint arrangement, net of tax		–	(1.3)
<i>Item that will not be reclassified to profit or loss:</i>			
Re-measurements of defined benefit plans, net of tax		(5.8)	2.9
<b>Other comprehensive income for the year, net of tax</b>		<b>64.1</b>	<b>61.4</b>
<b>Total comprehensive income for the year</b>		<b>216.7</b>	<b>264.9</b>

The consolidated statements of comprehensive income should be read in conjunction with the accompanying notes.

### 3 – REVENUE AND OTHER INCOME

	2019 A\$m	2018 A\$m
<b>Sales revenue</b>		
Ferrous secondary recycling	4,505.4	4,381.6
Non-ferrous secondary recycling	1,271.4	1,215.6
Recycling solutions	746.5	758.4
Secondary processing and other services	116.7	92.4
	<b>6,640.0</b>	<b>6,448.0</b>
<b>Other revenue</b>		
Interest income	1.2	1.9
Rental and dividend income	9.0	8.0
	<b>10.2</b>	<b>9.9</b>
<b>Total revenue</b>	<b>6,650.2</b>	<b>6,457.9</b>
Net gain on commodity derivatives	10.4	–
Net foreign exchange gain	1.2	–
Net gain on disposal of property, plant and equipment	5.4	1.4
Gain on acquisition of interest of a joint arrangement	–	10.1
Net gain on revaluation of financial assets at fair value through profit or loss	0.4	0.5
Government grants	2.5	1.0
Insurance Recoveries	16.5	–
Third party commissions	3.4	1.4
Management Fees	1.7	2.1
Other	6.1	4.9
<b>Total other income</b>	<b>47.6</b>	<b>21.4</b>

# Sims Metal Management

## Statement of Financial Position



### Consolidated Statements of Financial Position

As at 30 June 2019

	Note	2019 A\$m	2018 A\$m
<b>Current assets</b>			
Cash and cash equivalents	17	382.9	339.1
Trade and other receivables	8	386.7	461.7
Inventories	9	442.8	567.0
Other financial assets	16	17.5	18.9
Assets classified as held for sale	31	0.1	2.1
<b>Total current assets</b>		<b>1,230.0</b>	<b>1,388.8</b>
<b>Non-current assets</b>			
Investments in joint ventures	24	312.7	267.4
Other financial assets	16	18.1	16.7
Property, plant and equipment	10	1,267.2	1,155.8
Retirement benefit assets	15	2.7	7.7
Deferred tax assets	12	160.9	166.8
Intangible assets	11	193.8	198.6
<b>Total non-current assets</b>		<b>1,955.4</b>	<b>1,813.0</b>
<b>Total assets</b>		<b>3,185.4</b>	<b>3,201.8</b>
<b>Current liabilities</b>			
Trade and other payables	13	536.0	645.1
Borrowings	18	0.2	1.6
Other financial liabilities	16	2.5	6.5
Current tax liabilities		19.5	30.4
Provisions	14	100.5	110.8
<b>Total current liabilities</b>		<b>658.7</b>	<b>794.4</b>
<b>Non-current liabilities</b>			
Payables	13	13.8	13.6
Borrowings	18	35.2	39.4
Deferred tax liabilities	12	115.2	89.1
Provisions	14	60.9	75.0
Retirement benefit obligations	15	2.9	1.6
<b>Total non-current liabilities</b>		<b>228.0</b>	<b>218.7</b>
<b>Total liabilities</b>		<b>886.7</b>	<b>1,013.1</b>
<b>Net assets</b>		<b>2,298.7</b>	<b>2,188.7</b>
<b>Equity</b>			
Contributed equity	19	2,750.2	2,767.8
Reserves	20	236.3	147.6
Accumulated deficit	20	(687.8)	(726.7)
<b>Total equity</b>		<b>2,298.7</b>	<b>2,188.7</b>

The consolidated statements of financial position should be read in conjunction with the accompanying notes.

# Sims Metal Management Statement of Cash Flows



## Consolidated Statements of Cash Flows

For the year ended 30 June 2019

	Note	2019 A\$m	2018 A\$m
<b>Cash flows from operating activities</b>			
Receipts from customers (inclusive of goods and services tax)		6,860.6	6,555.1
Payments to suppliers and employees (inclusive of goods and services tax)		(6,473.5)	(6,265.6)
		387.1	289.5
Interest received		1.2	1.9
Interest paid		(6.5)	(8.4)
Insurance recoveries		15.8	—
Dividends received from joint ventures	24	23.4	29.2
Income taxes paid		(60.9)	(60.1)
<b>Net cash inflows from operating activities</b>	17	<b>360.1</b>	<b>252.1</b>
<b>Cash flows from investing activities</b>			
Payments for property, plant and equipment		(197.1)	(176.1)
Payments for businesses, net of cash acquired	22	(9.4)	(56.3)
Payments for increase in ownership interest of joint venture		—	(38.4)
Payments for other financial assets		(3.2)	(2.9)
Proceeds from sale of property, plant and equipment		6.1	4.6
Proceeds from sale of assets held for sale		7.2	4.7
Proceeds from sale of other financial assets		2.3	1.9
Proceeds from repayment on third party loans		—	0.1
<b>Net cash outflows from investing activities</b>		<b>(194.1)</b>	<b>(262.4)</b>
<b>Cash flows from financing activities</b>			
Proceeds from borrowings		1,613.1	854.9
Repayment of borrowings		(1,617.2)	(817.9)
Fees paid for loan facilities		(0.2)	—
Repayment of finance leases		(1.6)	(2.2)
Payments for ordinary shares bought back	19	(19.3)	—
Proceeds from issue of ordinary shares		1.7	35.4
Dividends paid	6	(107.9)	(106.8)
<b>Net cash outflows from financing activities</b>		<b>(131.4)</b>	<b>(36.6)</b>
<b>Net increase/(decrease) in cash and cash equivalents</b>		<b>34.6</b>	<b>(46.9)</b>
Cash and cash equivalents at the beginning of the financial year		339.1	378.5
Effects of exchange rate changes on cash and cash equivalents		9.2	7.5
<b>Cash and cash equivalents at the end of the financial year</b>	17	<b>382.9</b>	<b>339.1</b>

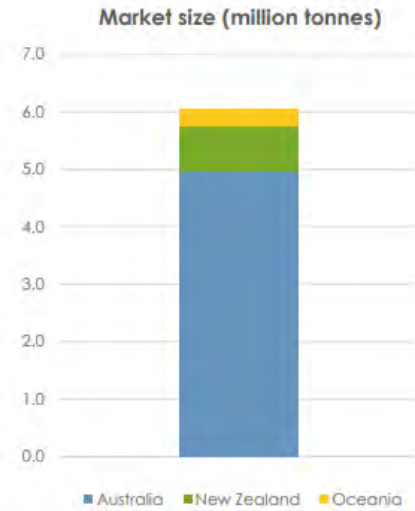
The consolidated statements of cash flows should be read in conjunction with the accompanying notes.

## COVID-19

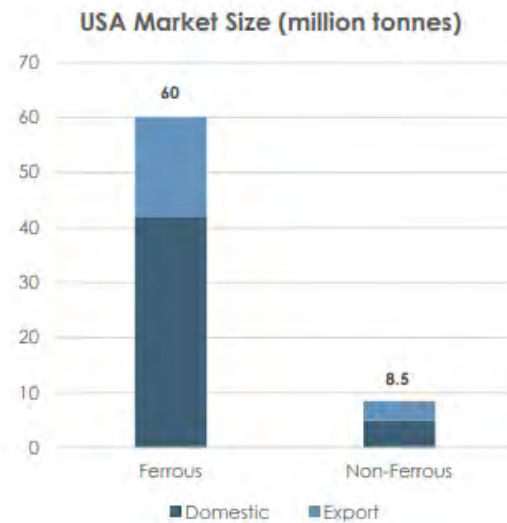
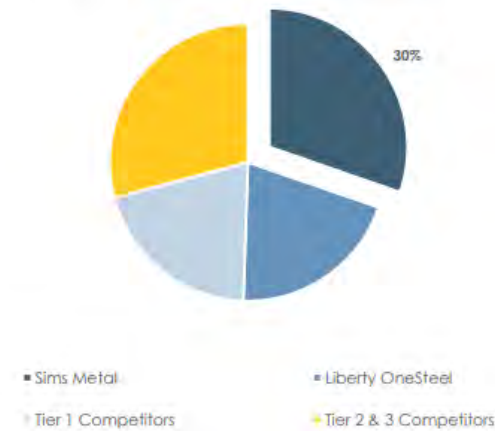
- Sims has stopped taking third-party scrap in UK
- Sims Pacific Metals branches closed until 20<sup>th</sup> of April
- Excess inventories of processed metals are rising fast without any shipping
- Aluminium prices are decreasing

## COVID-19 Response

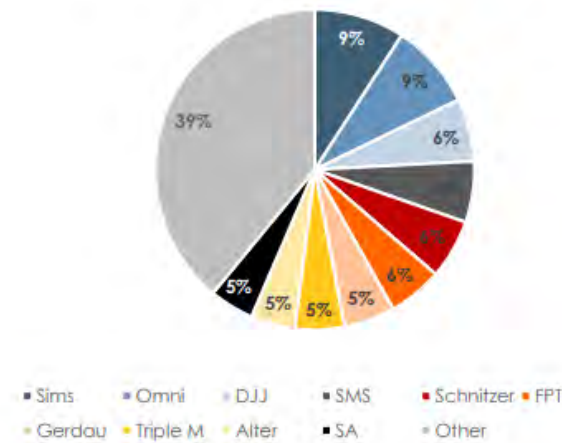
- Prices are indeed trading at four-year lows, but this isn't the same lows as the GFC
- Suppliers of car-makers are still taking deliveries, other consumers are starting to request more primary metal to compensate for decline in scrap supply
- Typically recoverable through managing the buy price of metals
- Dividend is still going to be paid out, Sims has the cash reserves to weather this out



**Estimated Australian market share by volume**

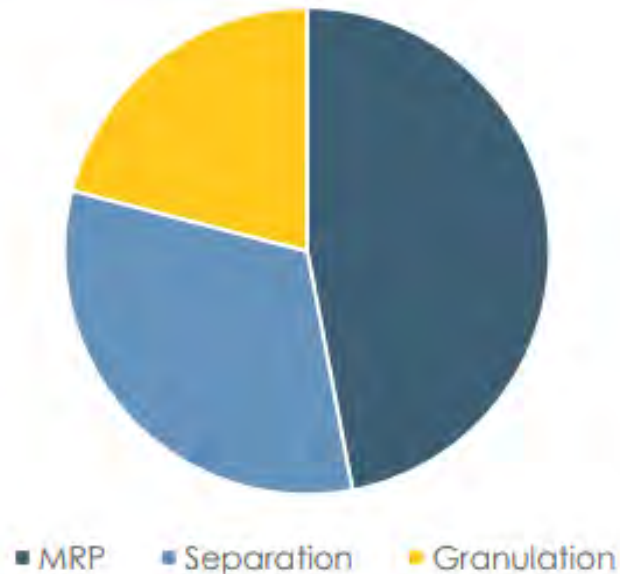


**Estimated USA Market Share by Volume**



Sims Metal Management  
How Sims is becoming more effective

\$27 million FY19 EBIT from quality initiatives



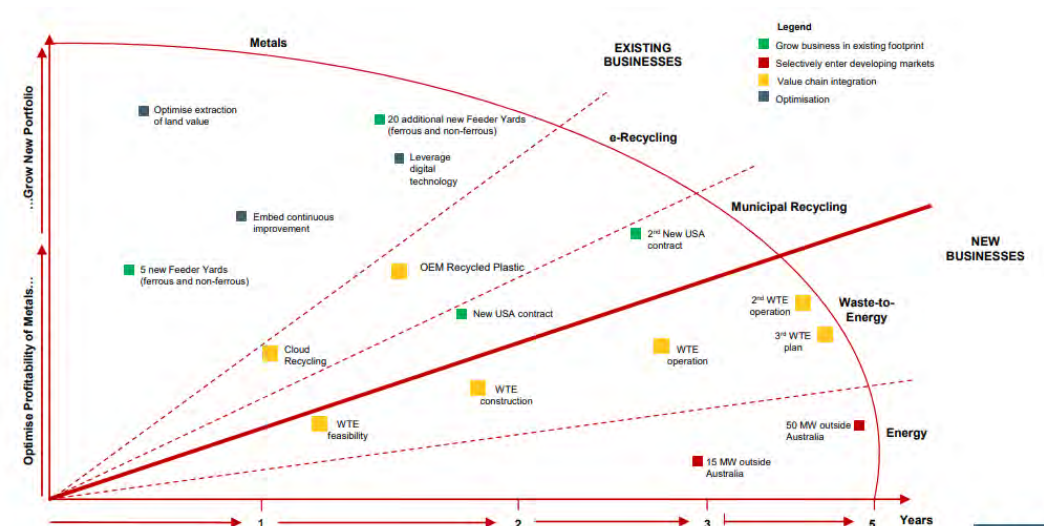
- Operation of copper granulation and zorba separation plants providing geographic and customer optionality for differentiated product
- Furnace ready twitch/heavies product from zorba separation plant provides price premium
- Flexibility to adjust product output depending on customer needs

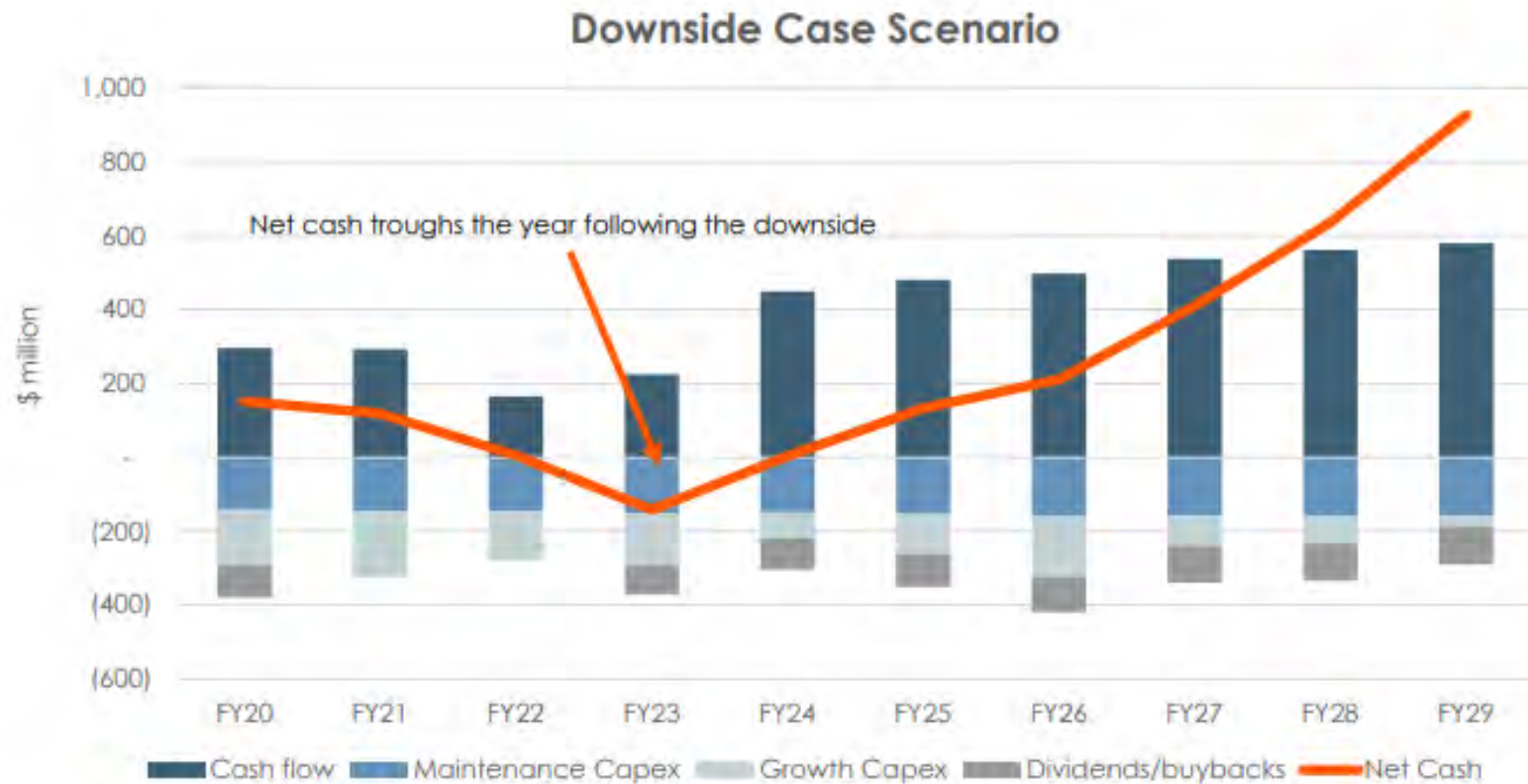


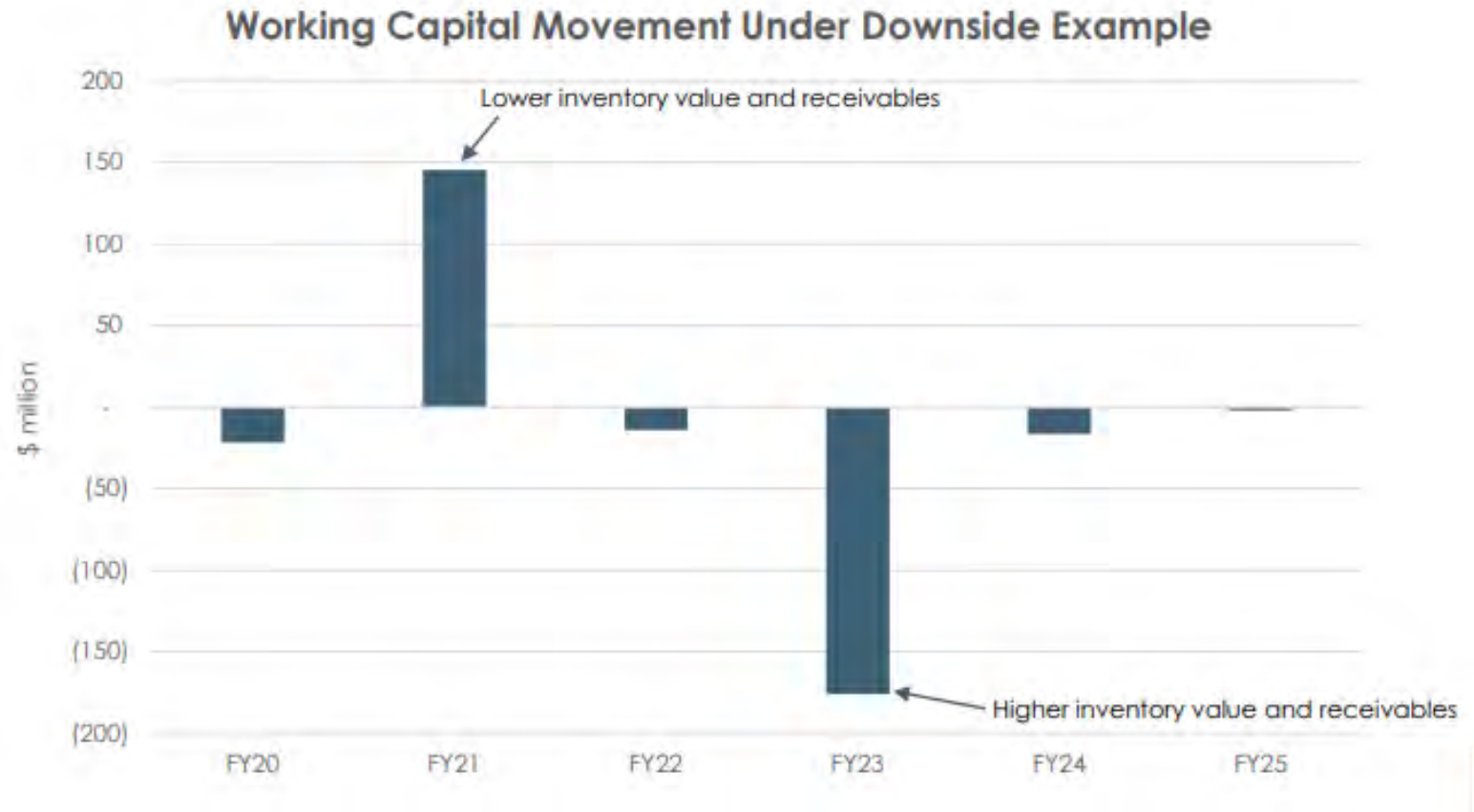
Scenario Forecast Growth  
Capex FY20-FY24



■ North America Metals ■ Sims Waste to Energy ■ Sims Energy



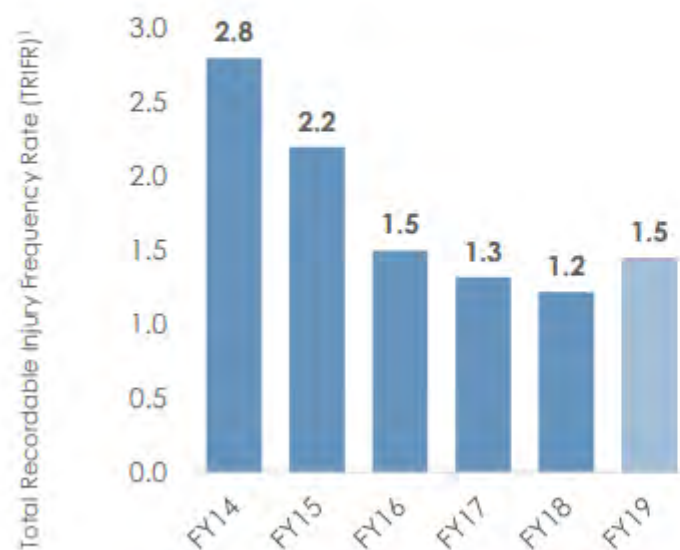




## Employee Health & Safety

Global commitment for zero harm today

### Safety performance



1) Defined as total recordable injuries x 200,000 divided by number of hours worked.

- Safety remains the most important priority for both our employees and the community
- After nearly a decade without a fatality, there were two fatalities in FY19. Immediate actions:
  - Eight weeks of stand-down meetings covering key risks and controls
  - Assessment and continuous improvement of key site traffic plans and maintenance activities
- Global Perception Safety Survey Company-wide underway. Followed by a deep dive into selected sites with both high and low safety perception
- An increase in risk assessments and safety self-audits conducted in FY19, 1,361 and 112,506 respectively, compared to FY18



6

# Sims Metal Management WACC



Market Return			SGM Return			Cost of Equity		Cost of Debt	
Date	S&P/ASX 200 (XJO)	Nominal Return	Date	ASX:NEA	Nominal Return	Inputs		Inputs	
1/1/2016	5005.50	#N/A	1/1/2016	5.8868	#N/A	Beta	1.3463	Cost of debt	6.99%
2/1/2016	4880.90	-2.52%	2/1/2016	5.8347	-0.89%	RF Rate (AS 10Y Bond)	2.50%	Corporate tax rate	30%
3/1/2016	5082.80	4.05%	3/1/2016	7.5018	25.13%	Number of Years	4.0	Outputs	
4/1/2016	5252.20	3.28%	4/1/2016	8.3309	10.48%	Annualised Return	8.81%	After-tax cost of debt	4.89%
5/1/2016	5378.60	2.38%	5/1/2016	7.1797	-14.87%	Market Risk Premium	6.31%		
6/1/2016	5233.40	-2.74%	6/1/2016	6.8721	-4.38%	Outputs			
7/1/2016	5562.30	6.10%	7/1/2016	7.4082	7.51%	Cost of Equity	11.00%		
8/1/2016	5433.00	-2.35%	8/1/2016	8.7527	16.68%				
9/1/2016	5435.90	0.05%	9/1/2016	8.1727	-6.86%				
10/1/2016	5317.70	-2.20%	10/1/2016	8.8055	7.46%				
11/1/2016	5440.50	2.28%	11/1/2016	11.1267	23.40%				
12/1/2016	5665.80	4.06%	12/1/2016	11.4205	2.61%				
1/1/2017	5620.90	-0.80%	1/1/2017	9.9607	-13.68%				
2/1/2017	5712.20	1.61%	2/1/2017	11.2336	12.03%				
3/1/2017	5864.90	2.64%	3/1/2017	11.0021	-2.08%				
4/1/2017	5924.10	1.00%	4/1/2017	11.1259	1.12%				
5/1/2017	5724.60	-3.43%	5/1/2017	12.0576	8.04%				
6/1/2017	5721.50	-0.05%	6/1/2017	13.7310	13.00%				
7/1/2017	5720.60	-0.02%	7/1/2017	14.0566	2.34%				
8/1/2017	5714.50	-0.11%	8/1/2017	13.4777	-4.21%				
9/1/2017	5681.60	-0.58%	9/1/2017	12.1932	-10.02%				
10/1/2017	5909.00	3.92%	10/1/2017	11.9581	-1.95%				
11/1/2017	5969.90	1.03%	11/1/2017	12.8743	7.38%				
12/1/2017	6065.10	1.58%	12/1/2017	14.4813	11.76%				
1/1/2018	6037.70	-0.45%	1/1/2018	15.1332	4.40%				
2/1/2018	6016.00	-0.36%	2/1/2018	16.0240	5.72%				
3/1/2018	5759.40	-4.36%	3/1/2018	13.2600	-18.93%				
4/1/2018	5982.70	3.80%	4/1/2018	15.0815	12.87%				
5/1/2018	6011.90	0.49%	5/1/2018	14.8579	-1.49%				
6/1/2018	6194.60	2.99%	6/1/2018	14.9790	0.81%				
7/1/2018	6280.20	1.37%	7/1/2018	15.0757	6.44%				

# Sims Metal Management Forecast Assumptions



WACC		
<b>Cost of Debt</b>	<b>4.89%</b>	<i>After tax cost of debt</i>
Debt Beta	0	
Equity Beta	1.3463	<i>Linear Regression, 5Y</i>
Risk-Free Rate	2.50%	<i>10Y RBA Bond Rate</i>
Market Premium	6.31%	<i>SGM's 5Y Return (Annualised) - RF Rate</i>
<b>Cost of Equity</b>	<b>11.00%</b>	<i>CAPM</i>
<b>Net Debt</b>	<b>362</b>	<i>Market value of debt</i>
Share Price	6.25	<i>AUD</i>
Shares Outstanding	202.73	<i>FY 2019 Weighted average number of ordinary shares</i>
<b>Market Capitalisation</b>	<b>1,267</b>	<i>Market value of equity</i>
MVD + MVE	1,629	
E/V	0.78	
D/V	0.22	
Corporate Tax Rate	0.30	
<b>WACC</b>	<b>9.32%</b>	<i>CAPM</i>

EBITDA		
EBITDA % of Revenue Margin Start	3.77%	<i>4Y Year Average</i>
EBITDA % of Revenue Margin End	1.27%	<i>4Y Average - Inflation</i>

Revenue		
Revenue Margin Start	3.17%	<i>4Y Year Average</i>
Revenue Margin End	0.67%	<i>4Y Average - Inflation</i>
Effective Tax Rate % of EBIT	21.30%	<i>4Y Year Average</i>

CAPEX		
CAPEX % of Revenue	2.57%	

D&A		
As % of PPE and IA	9.99%	<i>4 Year Average</i>

Working Capital		
Accounts Receivable % of Revenue	5.69%	<i>5 Year Average</i>
Inventory % of Revenue	7.88%	<i>5 Year Average</i>
Accounts Payable % of non D&A Expenses	5.54%	<i>5 Year Average</i>

Long Term Growth Rate		
Terminal Growth Rate	2.50%	<i>Australia 10Y</i>

Dividends		
Return on Equity	3.93%	
Payout Ratio	33.15%	
Dividend Growth Rate	2.63%	

# Sims Metal Management EBIAT, CAPEX, OWC forecasts



Profitability Forecasting		2019	2020	2021	2022	2023	2024
<b>Revenue</b>							
	Revenue	6,650	6861	6993	7084	7154	7202
	Revenue Growth Rate	2.98%	3.17%	1.92%	1.30%	0.99%	0.67%
<b>EBITDA</b>							
	EBITDA	279	290	297	303	308	311
	EBITDA Growth Rate	4.20%	3.77%	2.52%	1.90%	1.58%	1.27%
<b>D&amp;A</b>							
	D&A	(133)	(143)	(146)	(149)	(153)	(156)
	Opening PPE & IA	1,354	1,428	1,461	1,495	1,528	1,559
	D&A as a % of Opening PPE & IA	9.83%	9.99%	9.99%	9.99%	9.99%	9.99%
<b>Operating Expenses</b>							
	COGS & Operational Expenses	(6,371)	(6,571)	(6,696)	(6,781)	(6,846)	(6,890)

Asset Forecasting		2019	2020	2021	2022	2023	2024
<b>Revenue</b>							
	Revenue	6,650	6861	6993	7084	7154	7202
<b>PPE</b>							
	PPE + IA Opening	1,354	1,428	1,461	1,495	1,528	1,559
	Plus: CAPEX	207	176	180	182	184	185
	CAPEX% of Revenue	3.11%	2.57%	2.57%	2.57%	2.57%	2.57%
	Less: D&A	(133)	(143)	(146)	(149)	(153)	(156)
	D&A % of opening PPE & IA	9.83%	9.99%	9.99%	9.99%	9.99%	9.99%
	PPE + IA Closing	1,428	1,461	1,495	1,528	1,559	1,588

# Sims Metal Management EBIAT, CAPEX, OWC forecasts



<b>Working Capital</b>		2019	2020	2021	2022	2023	2024
<b>Revenue</b>							
	Revenue	6,650	6,861	6,993	7,084	7,154	7,202
	COGS & Other Expenses	(6,371)	(6,571)	(6,696)	(6,781)	(6,846)	(6,890)
	EBITDA	279	290	297	303	308	311
<b>Working Capital</b>							
	Accounts Receivables	278	391	398	403	407	410
	Accounts Receivables % of Revenue	4.18%	5.69%	5.69%	5.69%	5.69%	5.69%
	Inventory	443	541	551	558	564	568
	Inventory % of Revenue	6.66%	7.88%	7.88%	7.88%	7.88%	7.88%
	Accounts Payable	328	364	371	376	380	382
	Accounts Payable % of non D&A expenses	5.15%	5.54%	5.54%	5.54%	5.54%	5.54%
	OWC	393	567	578	586	592	596
	ΔOWC	(30)	175	11	8	6	4



DCF		2019	2020	2021	2022	2023	2024
	<b>Unlevered Net Income + D&amp;A</b>						
	Revenue	6,650	6,861	6,993	7,084	7,154	7,202
	Non D&A Expenses	(6,371)	(6,571)	(6,696)	(6,781)	(6,846)	(6,890)
	EBITDA	279	290	297	303	308	311
	Less: D&A	(133)	(143)	(146)	(149)	(153)	(156)
	EBIT	146	147	151	153	155	156
	Taxation Expense	(66)	(31)	(32)	(33)	(33)	(33)
	Plus: D&A	133	143	146	149	153	156
	<b>Unlevered Net Income + D&amp;A</b>	<b>214</b>	<b>258</b>	<b>265</b>	<b>270</b>	<b>275</b>	<b>278</b>
	<b>CAPEX</b>						
	Less: CAPEX	207	176	180	182	184	185
	<b>Working Capital</b>						
	Less: Δ OWC	(30)	175	11	8	6	4
	<b>FCFF</b>						
	Unlevered Free Cash Flows	#N/A	-92	74	81	85	89
	Terminal Value						1431
	Share of Cash Flows After Valuation Date		-23	74	81	85	1520
	Long Term Growth Rate	2.50%					
	Discount Rate	9.32%					
	Period		0.25	1.25	2.25	3.25	4.25
	Discount Factor		0.98	0.89	0.82	0.75	0.68
	Present Value		-22.56	66.47	65.90	63.58	1040.91
	Net Present Value	1214.29					
	Net Debt	361.6					
	Minority Interest	0					
	<b>Equity Value</b>	<b>1575.89</b>					
	Shares Outstanding	202.73					
	<b>Implied Price Per Share</b>	<b>7.77</b>					
	Current Price Per Share	6.25					
	Upside/(Downside)	24.37%					
	Margin Required	12.00%					
	Recommendation	Buy					

SGM Company		
Current Share Price	\$	6.25
Dividend (2018) (D0)		108
Shares Outstanding (000s)		203
Dividend per Share	\$	0.53
Dividend Growth Rate (g)		2.63%
Estimated Dividend 2019 (D1)	\$	0.55
WACC		9.32%
	Price	Upside/(Downside)
Implied Price by DDM	\$ 8.17	30.69%

# Sims Metal Management Comparables



Comparable Companies		Market Data						Financial Data				Multiples							
Region	Exchange/Ticker Company	Price	Shares (M)	Market Cap (M)	Net Debt (M)	Minority Interest (M)	EV (M)	Sales (M)	EBITDA (M)	EBIT (M)	EPS (M)	EV/Sales	EV/EBITDA	EV/EBIT	P/E				
APAC	ASX:SGM Sims Metal Management																		
NA	NYSE:CMC Commercial Metals Company																		
NA	NYSE:ATI Allegheny Technologies Incorporated																		
NA	NASDAQ:STLD Steel Dynamics Inc																		
NA	NASDAQ:SCHN Schnitzer Steel Industries																		
<b>EV / Sales Valuation</b>																			
Sales												0							
Industry Multiple												#NUM!							
Implied Market Cap (M)												#NUM!							
Fair value per share												#NUM!							
<b>EV / EBITDA Valuation</b>																			
EBITDA												0							
Industry Multiple												#NUM!							
Implied Market Cap (M)												#NUM!							
Fair value per share												#NUM!							
<b>EV / EBIT Valuation</b>																			
EBIT												0							
Industry Multiple												#NUM!							
Implied Market Cap (M)												#NUM!							
Fair value per share												#NUM!							
<b>P / E Valuation</b>																			
Earnings												0.00							
Industry Multiple												#NUM!							
Fair value per share												#NUM!							

# Millennium Cophthorne

Jenny Liu  
Jillin Yan  
Jonathan Chisholm  
James Thwaite



# Investment Thesis for MCK

## An established operator

Entrenched hotel operator in the attractive tourism market

## Competitive advantage

International brand recognition, a focus on secondary locations and service expertise

## Attractive industry

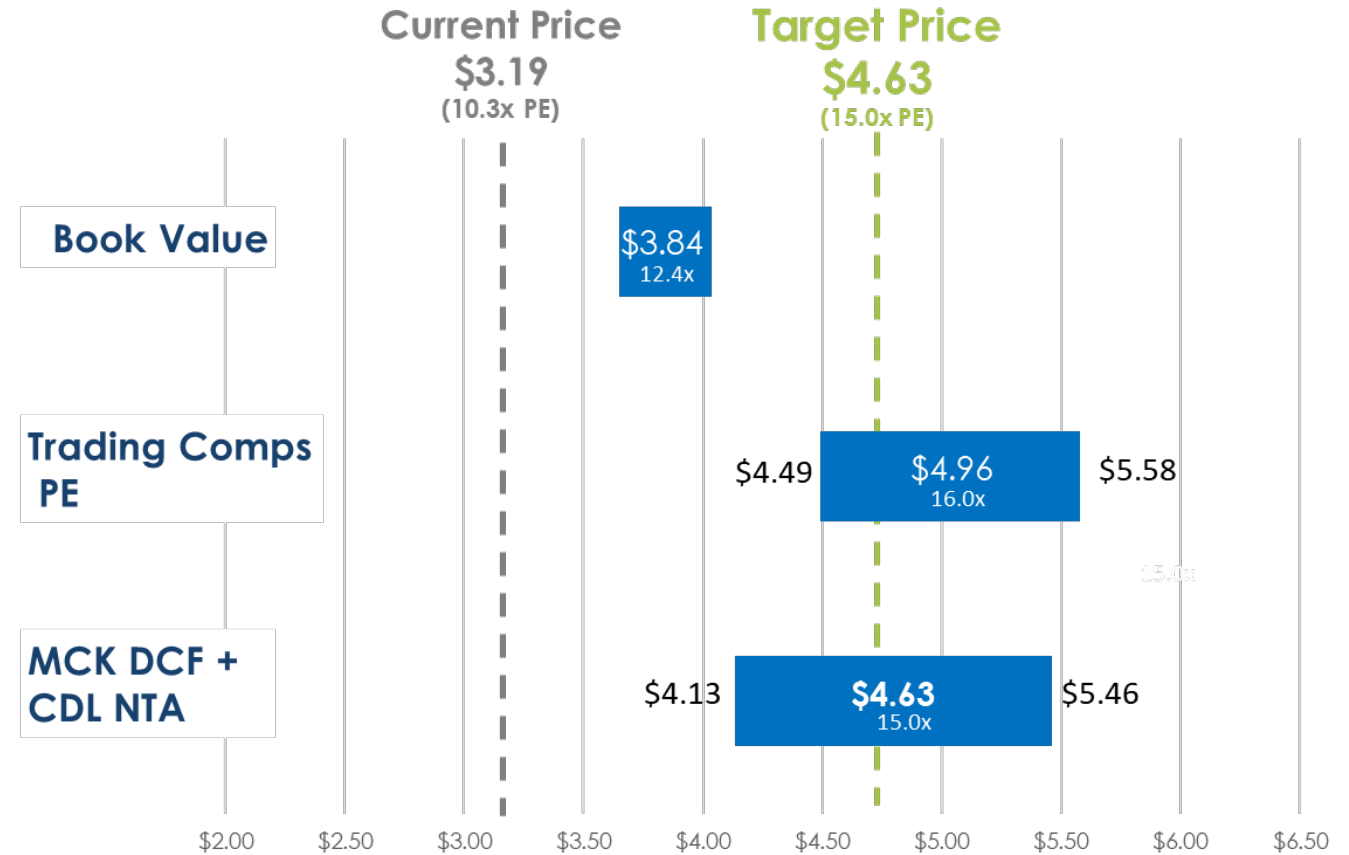
Increase in arrival and tourist spend with constrained hotel supply.

## Underappreciated by the market

Price is 31% discount to intrinsic value due to low free float and lack of broker coverage.

## With clear catalysts to a re-rating

FY18 earnings lift from new hotel openings and ADR growth.



# Millennium Copthorne



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*Industry*

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*Business*

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*Valuation*

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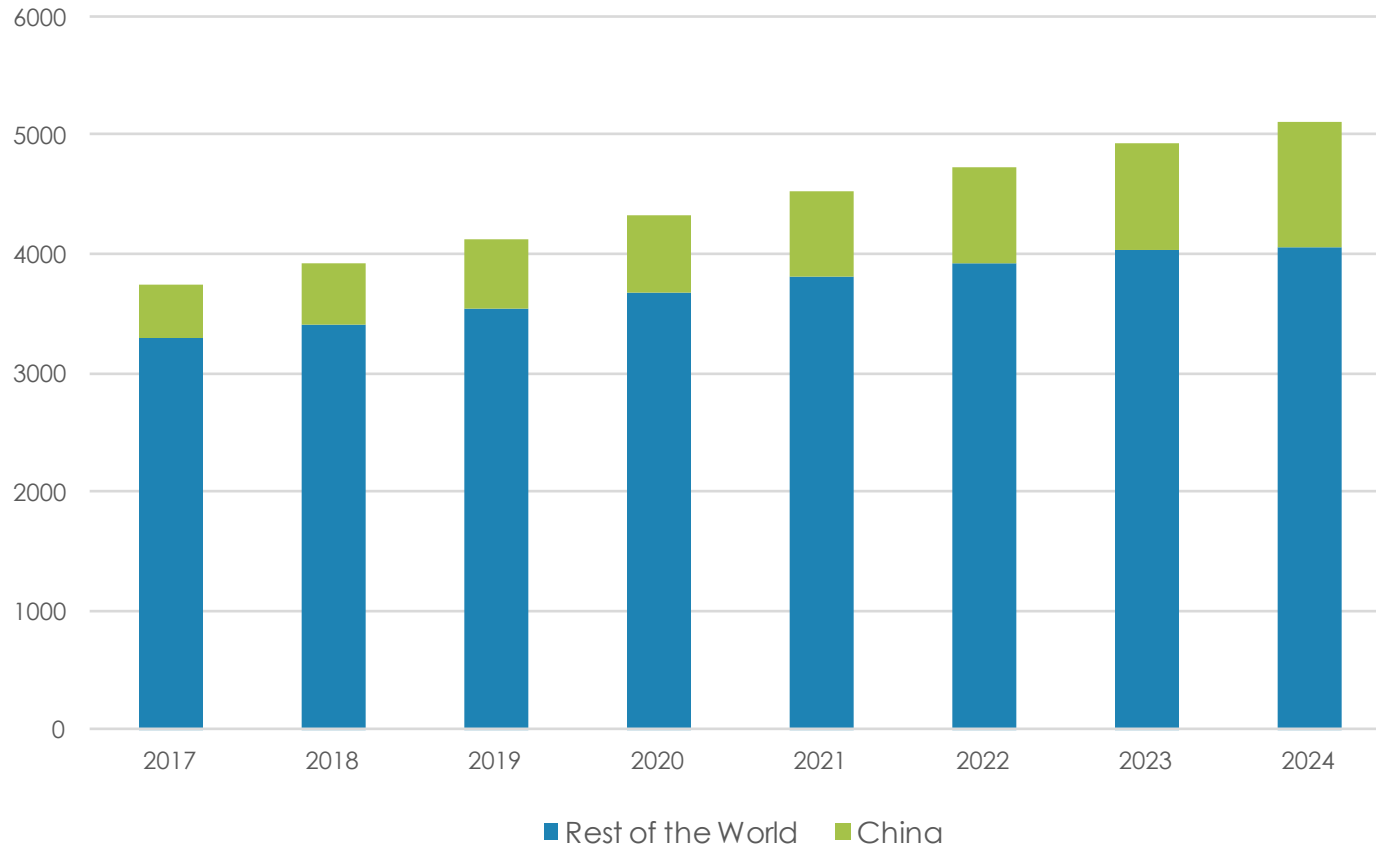
*Industry*

---



# Strong demand from projected growth in tourism arrivals and spend

### International Visitors (in 000's)



**37%**  
Increase in  
international **visitors**

**143%**  
Increase in **Chinese**  
**tourists**



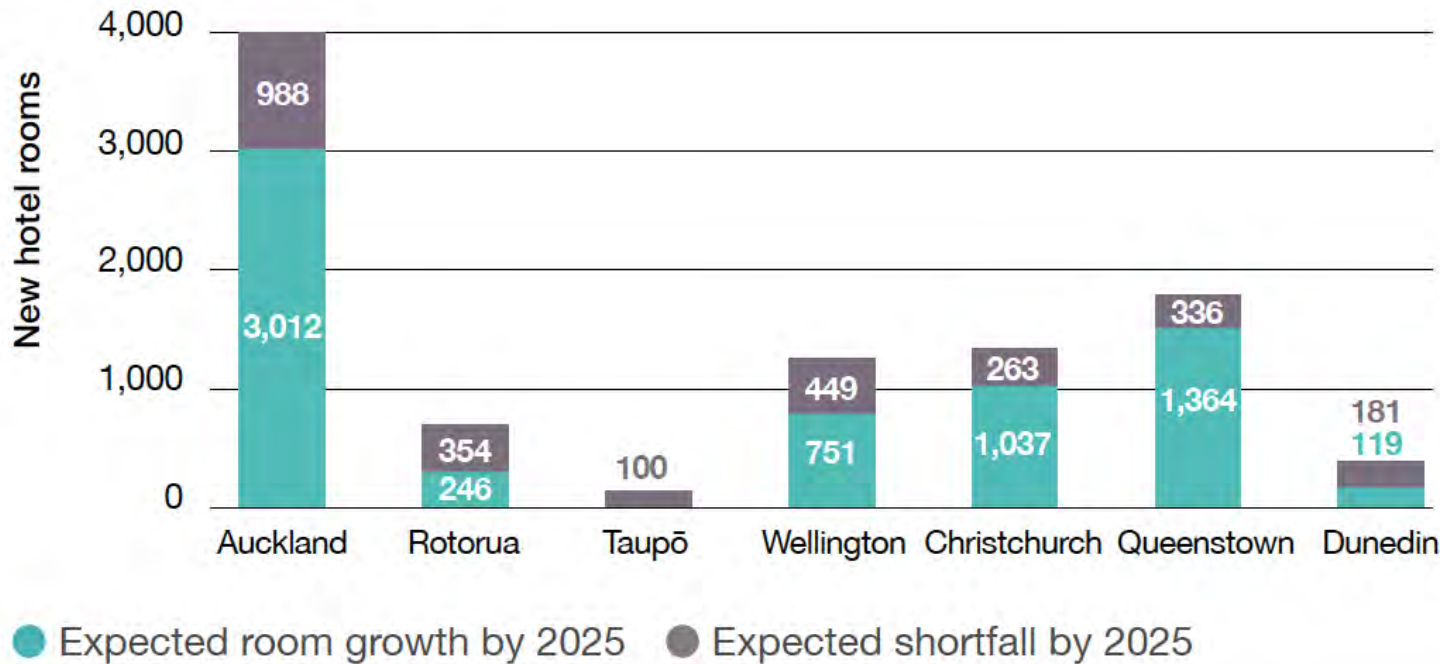
**52%**  
Increase in **spend**



# Undersupply from Historical RMA issues and weak construction pipeline

FIGURE 9:

## New hotel rooms required by 2025 to meet projected demand



- ✓ Estimated hotel supply pipeline remains low across New Zealand
- ✓ Most construction completion dates not till after 2021
- ✓ Shortage is greatest in secondary market

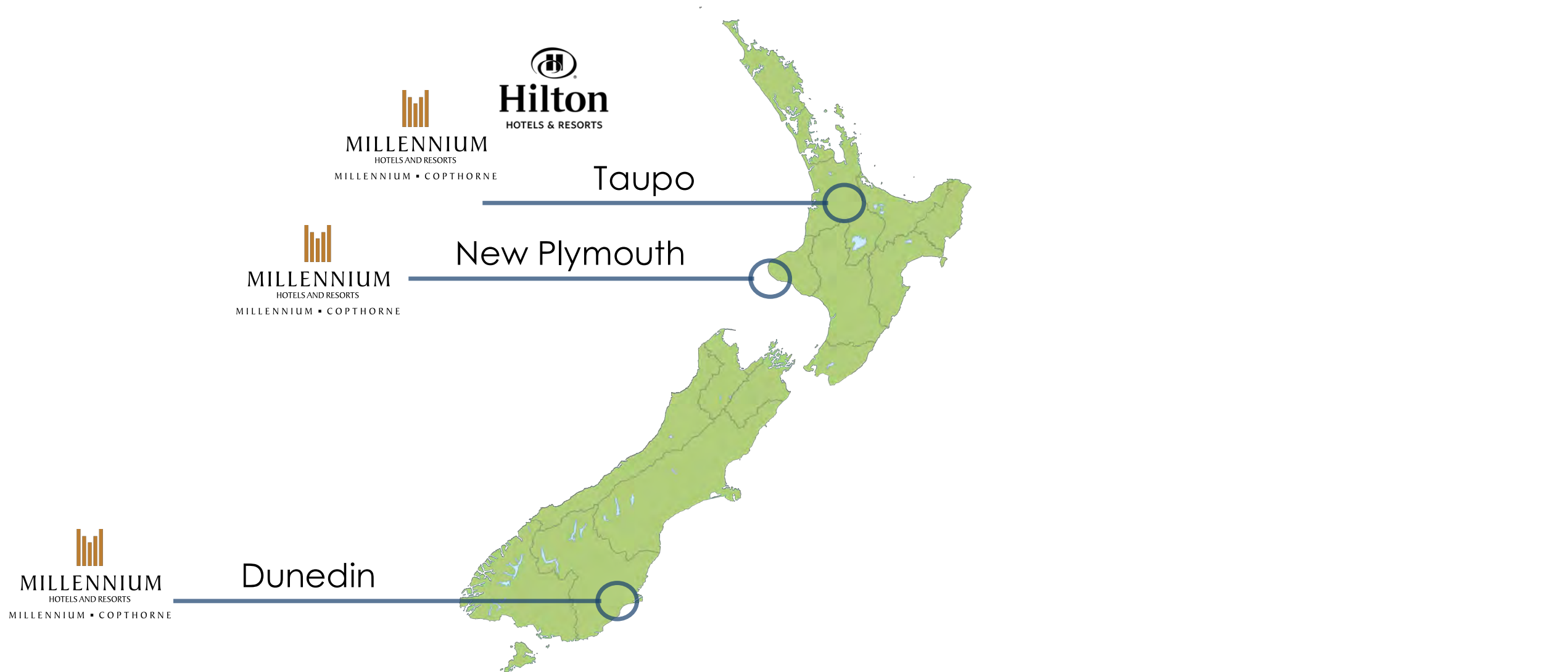
# Auckland features several international brands



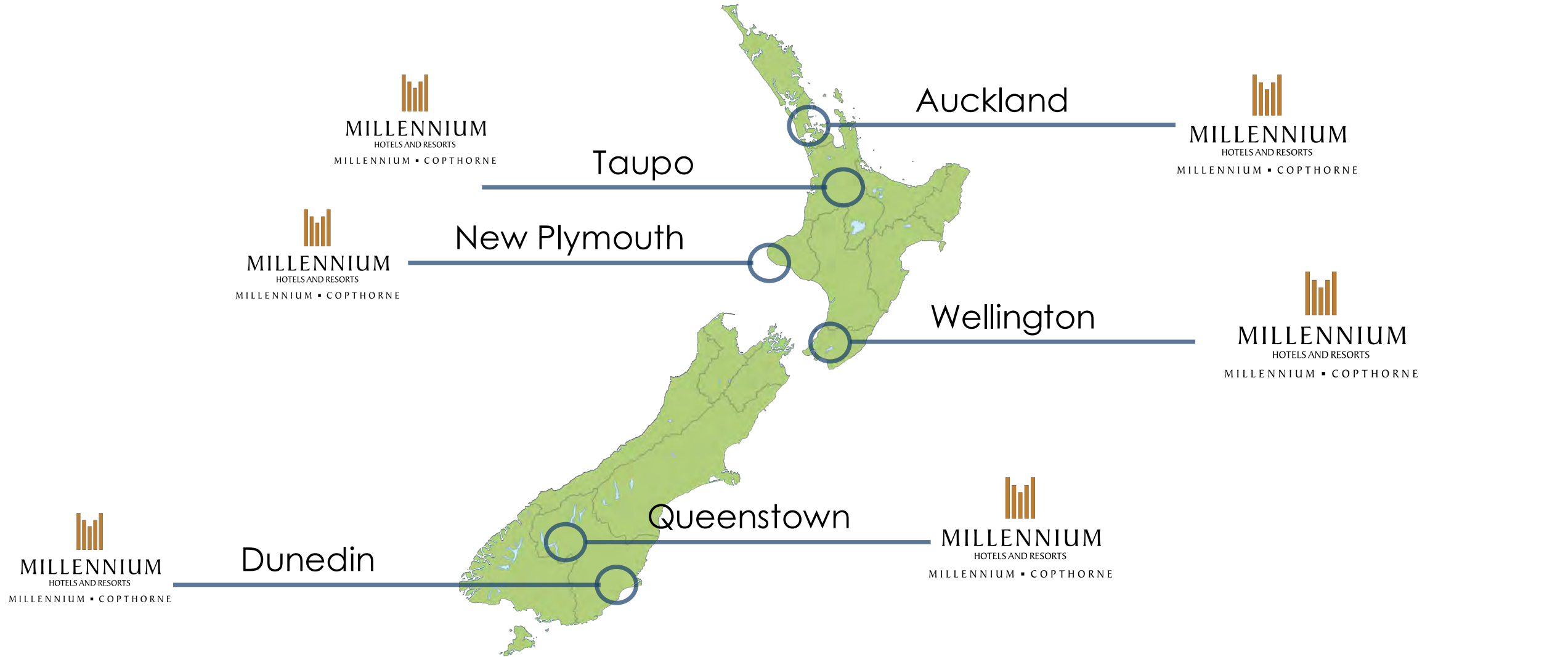
# Less international brands are present in Wellington and Queenstown



# There are minimal international brands in secondary markets



# But MCK is present across New Zealand



# While Airbnb continues to grow, the impact it has on MCK will be minimal



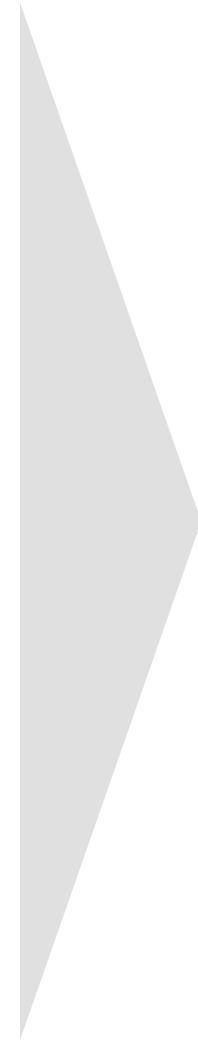
airbnb



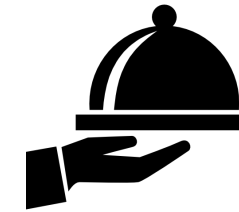
Cheaper Alternative



Unique Experience



MILLENNIUM  
HOTELS AND RESORTS  
MILLENNIUM ▪ COPTHORNE



MCK does not target the lower end market



Tourists from Asia continue to prefer hotels

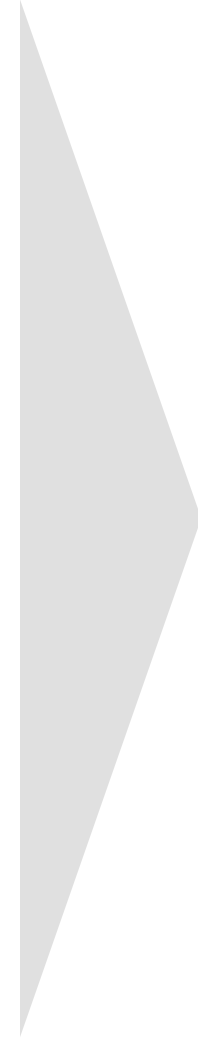
# While Airbnb continues to grow, the impact it has on MCK will be minimal



Cheaper Alternative



Unique Experience



MCK does not target the lower end market

Tourists from Asia continue to prefer hotels





MCK has 21 hotels in New Zealand under the Millennium, Copthorne and Kingsgate brands.



**21**  
**Hotels Nationwide**

14 owned or leased and operated

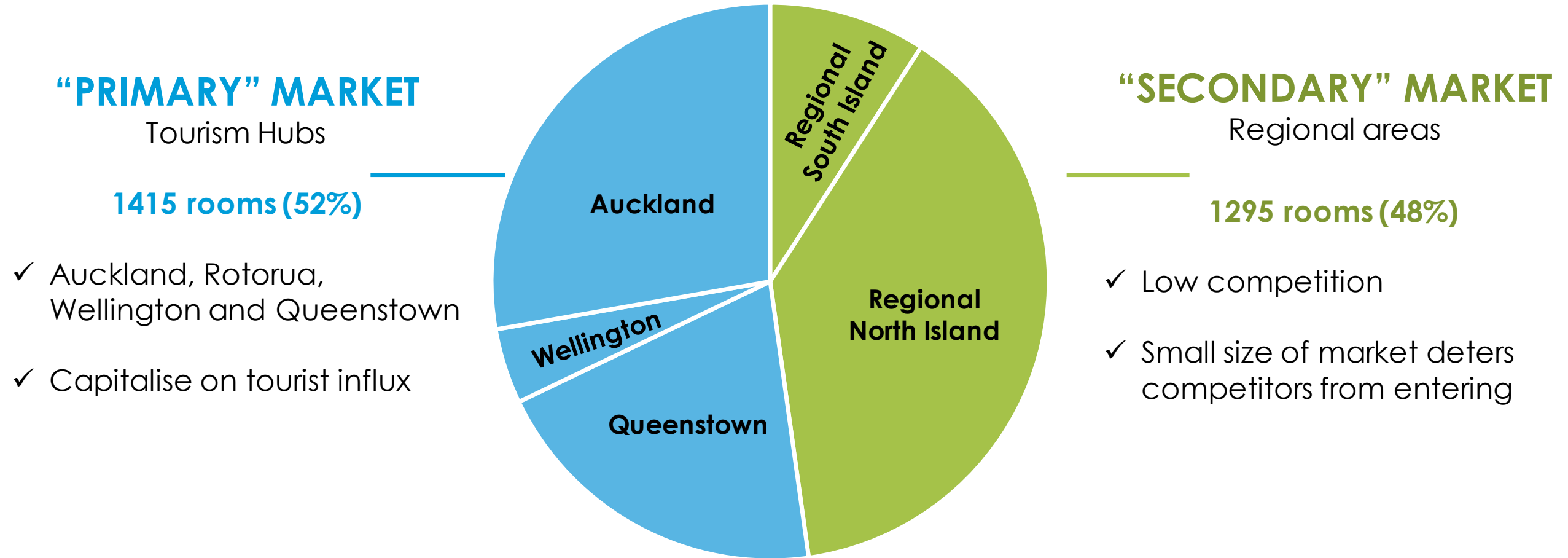
5 franchised

2 managed

Hotel ratings from bookings.com

By operating in both primary and secondary cities, MCK achieves geographic diversification and occupies areas of low competition.

### Number of Rooms by Geographic Market



# MCK caters to different customer segments and geographic markets

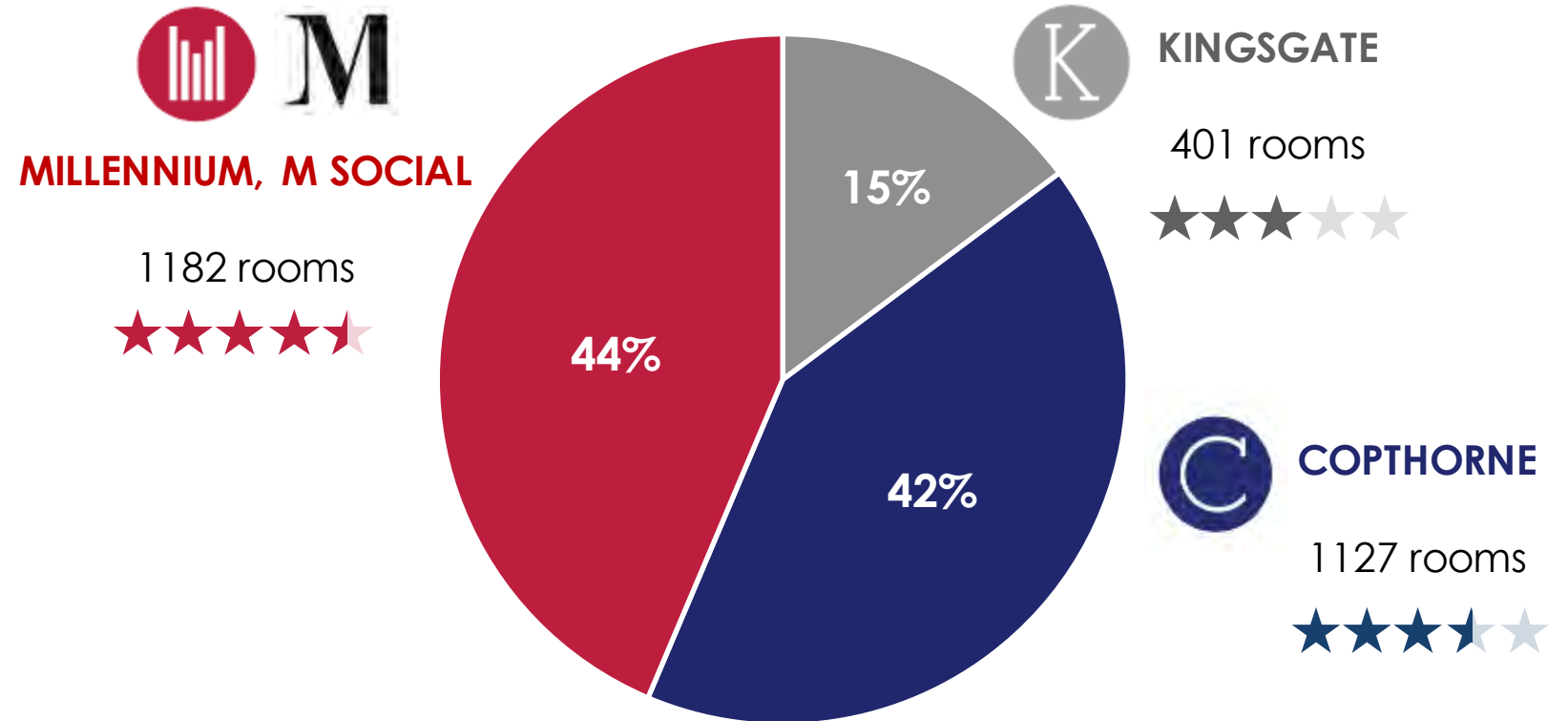
**Segmented** brands cater to different customer groups

Strategic focus on **mid to upper** market, which is underserved relative to demand

Premium and competitive hotels in **primary** markets

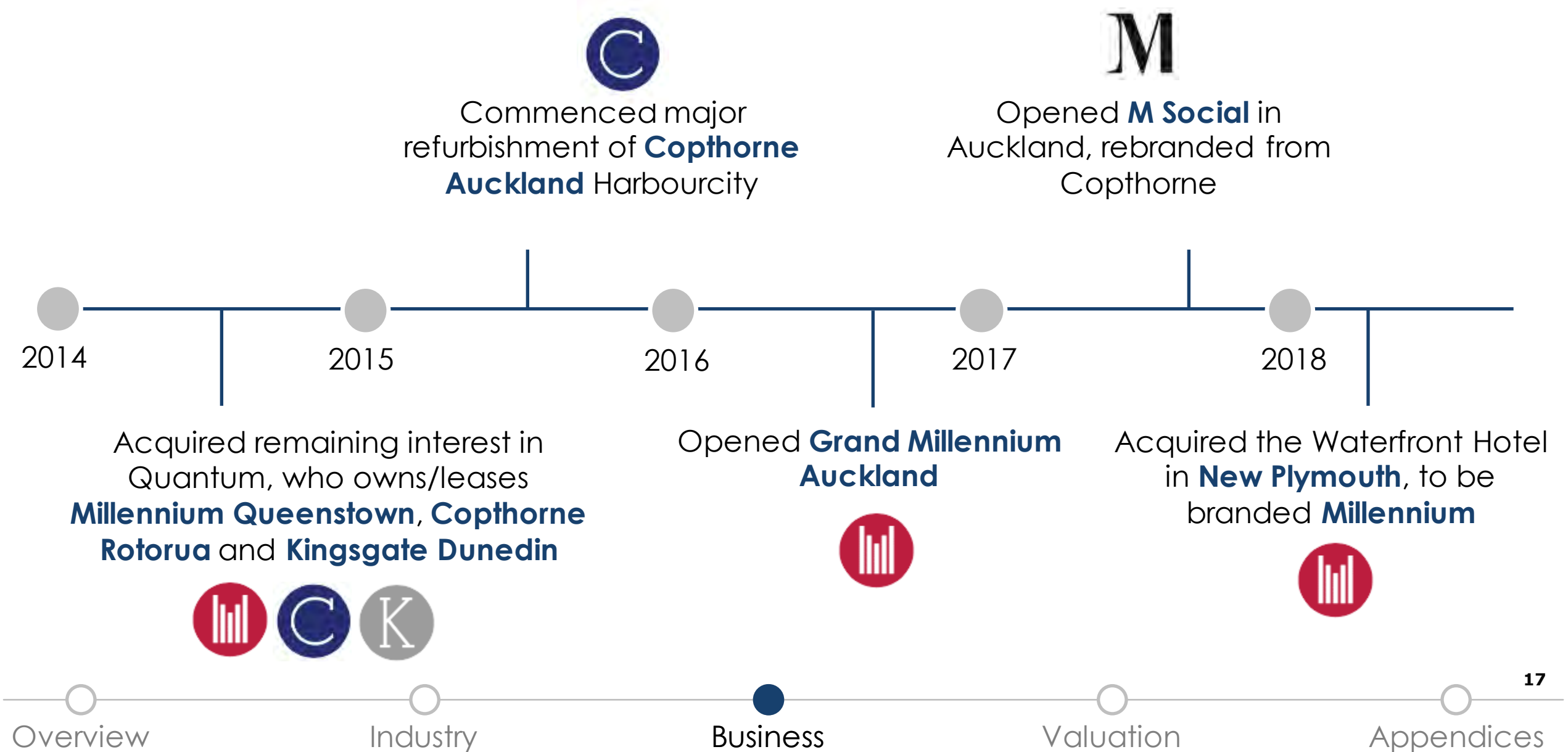
Brand value provides assurance in **secondary** markets

### Number of Rooms by Brand



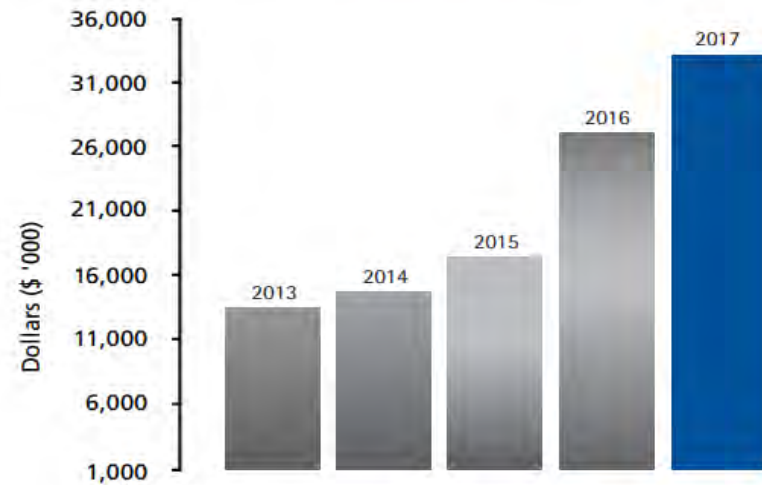
Focus on guest experience and service excellence across all brands

# MCK has a strong track record of hotel development and growth



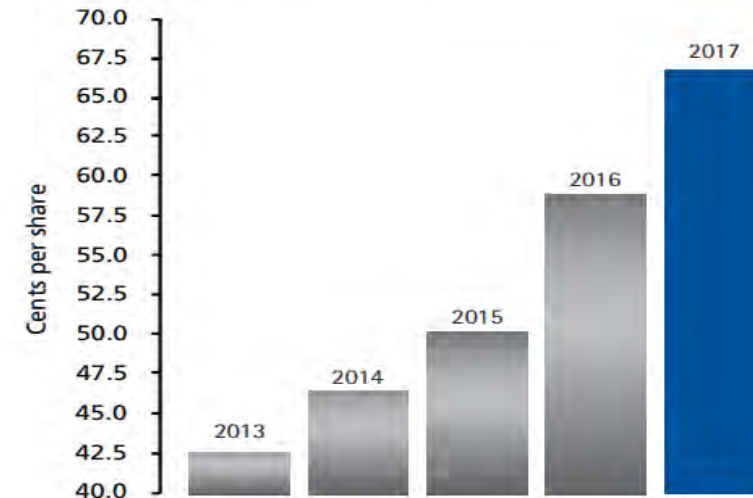
MCK has a 66% stake in CDL Investments, a residential land development company

### Profit



Land development has performed well in the bullish property market

### Net Asset Backing per Share

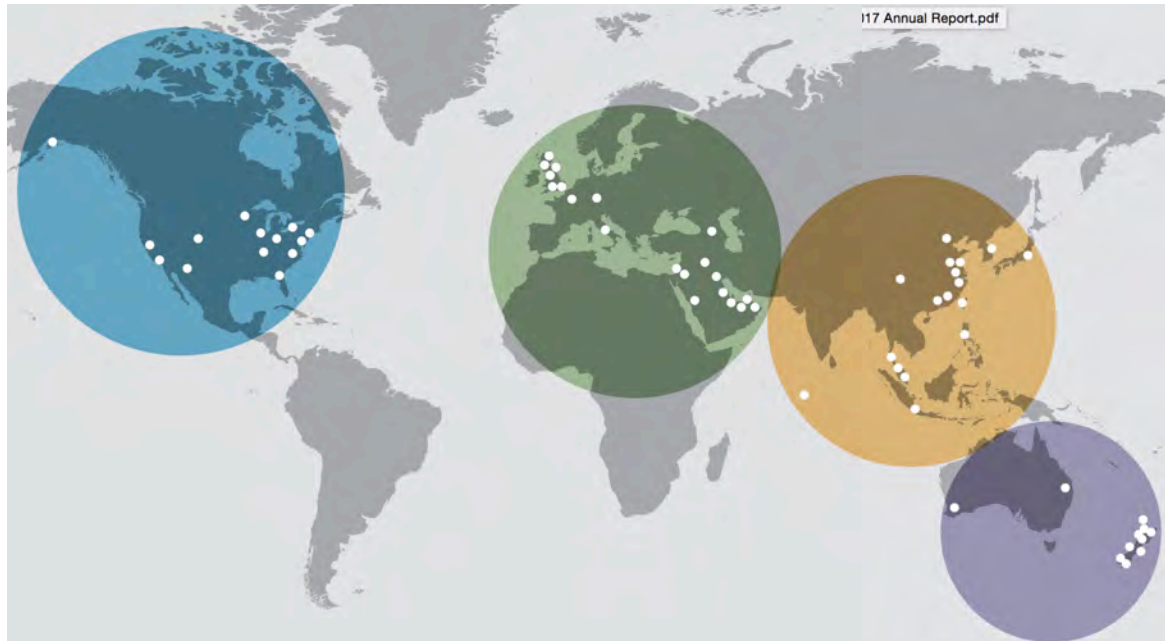


Still has valuable asset backing (land) that can be held through a downturn

Profitable standalone business

## Competitive Advantage

MCK has a competitive advantage in its international brand, management expertise and secondary market presence.



### International Brand

Global presence generates brand awareness which gives advantage over local competitors.

### Strong Management and Service Expertise

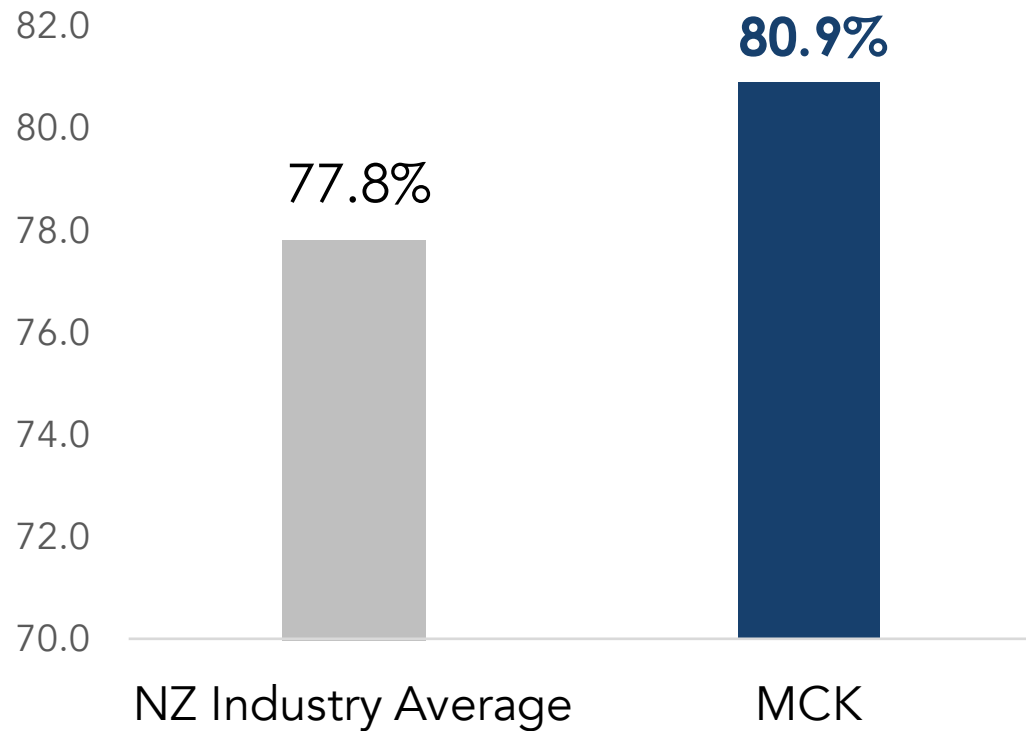
Parent provides experienced and disciplined management leading to service advantage

### First Mover Advantage

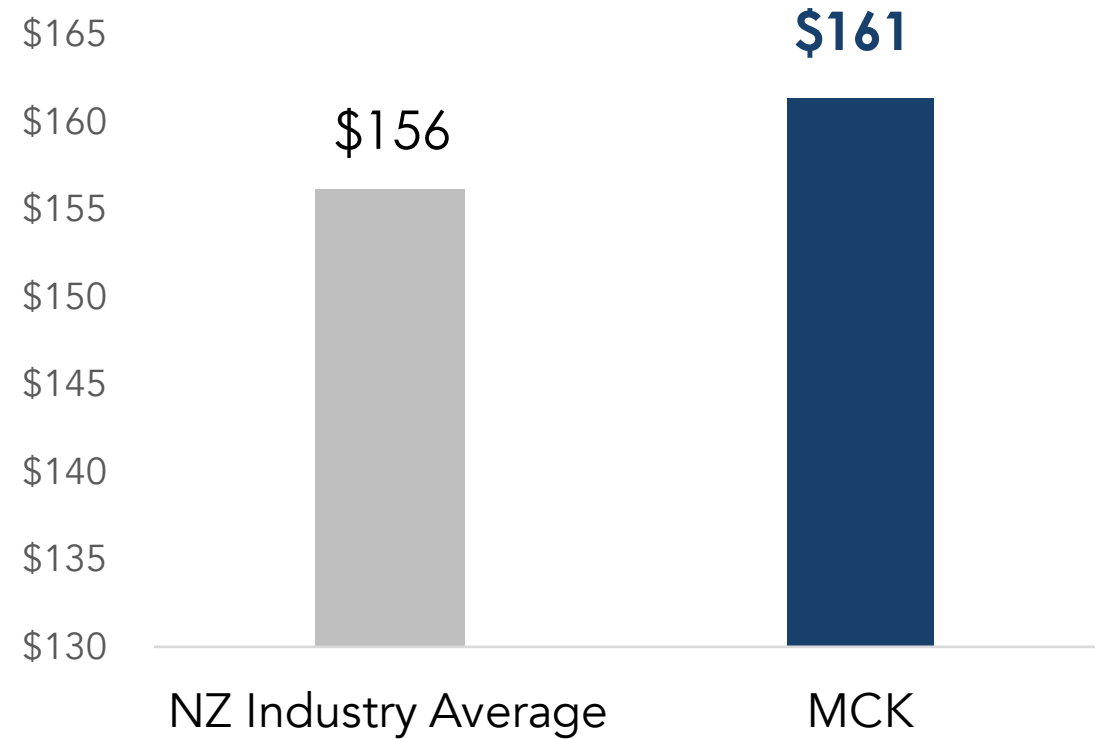
Brand assurance particularly valuable in secondary markets, which attracts minimal attention from competitors

This competitive advantage is manifested in above-industry figures for key drivers.

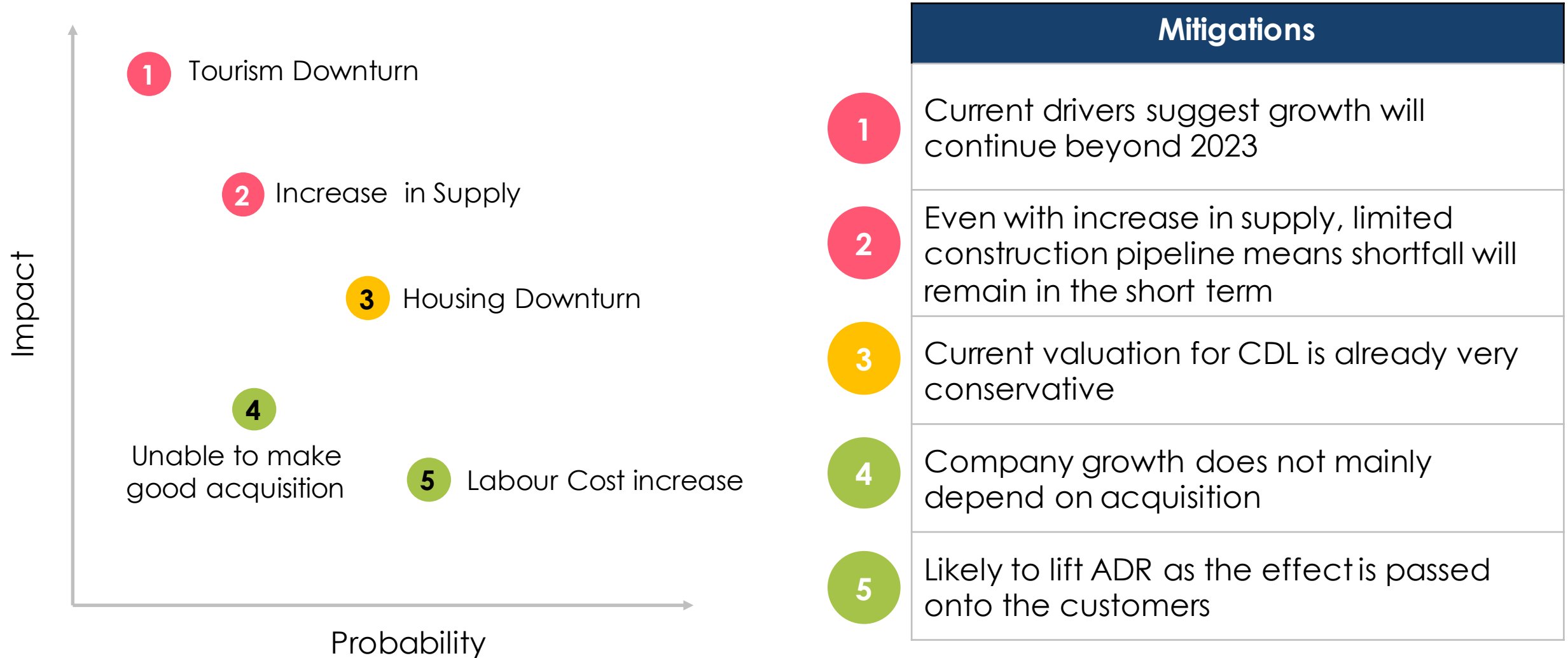
### Occupancy Rate



### Average Daily Rate



# Risks and Mitigations







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*Valuation*

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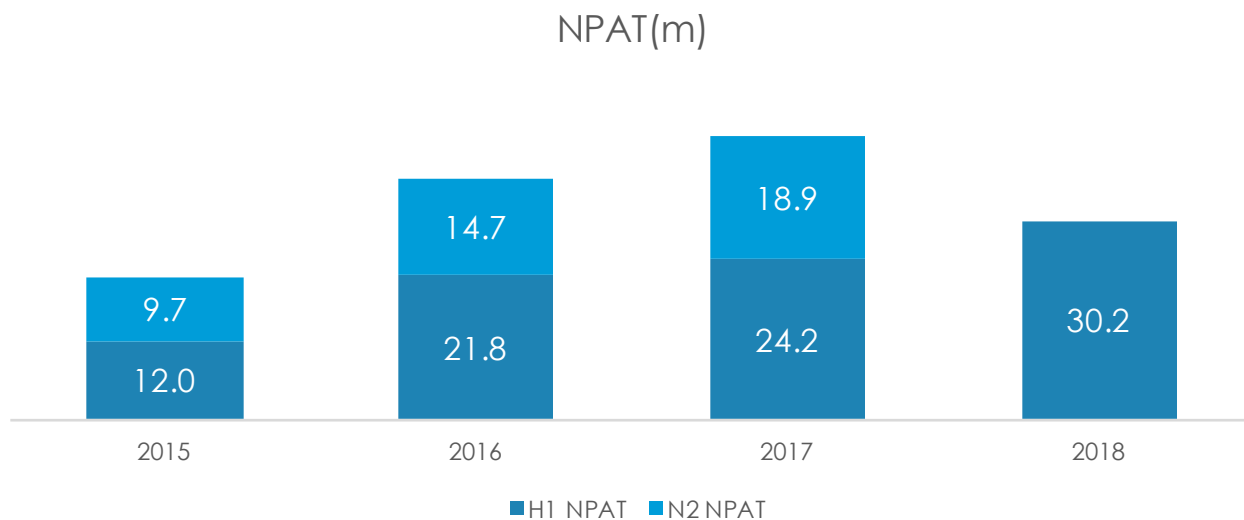
# Despite strong recent performance, current trading multiples are low

\$m NZD	Year ended	Dec-15	Dec-16	Dec-17	June 18(LTM)
Revenue		136.5	172	187.3	210.6
growth			26.0%	8.9%	14.0%
EBITDA		46.5	68.9	79.3	91.3
margin		34.1%	40.1%	42.3%	43.4%
NTA per share		\$2.46	\$3.09	\$3.72	\$3.84

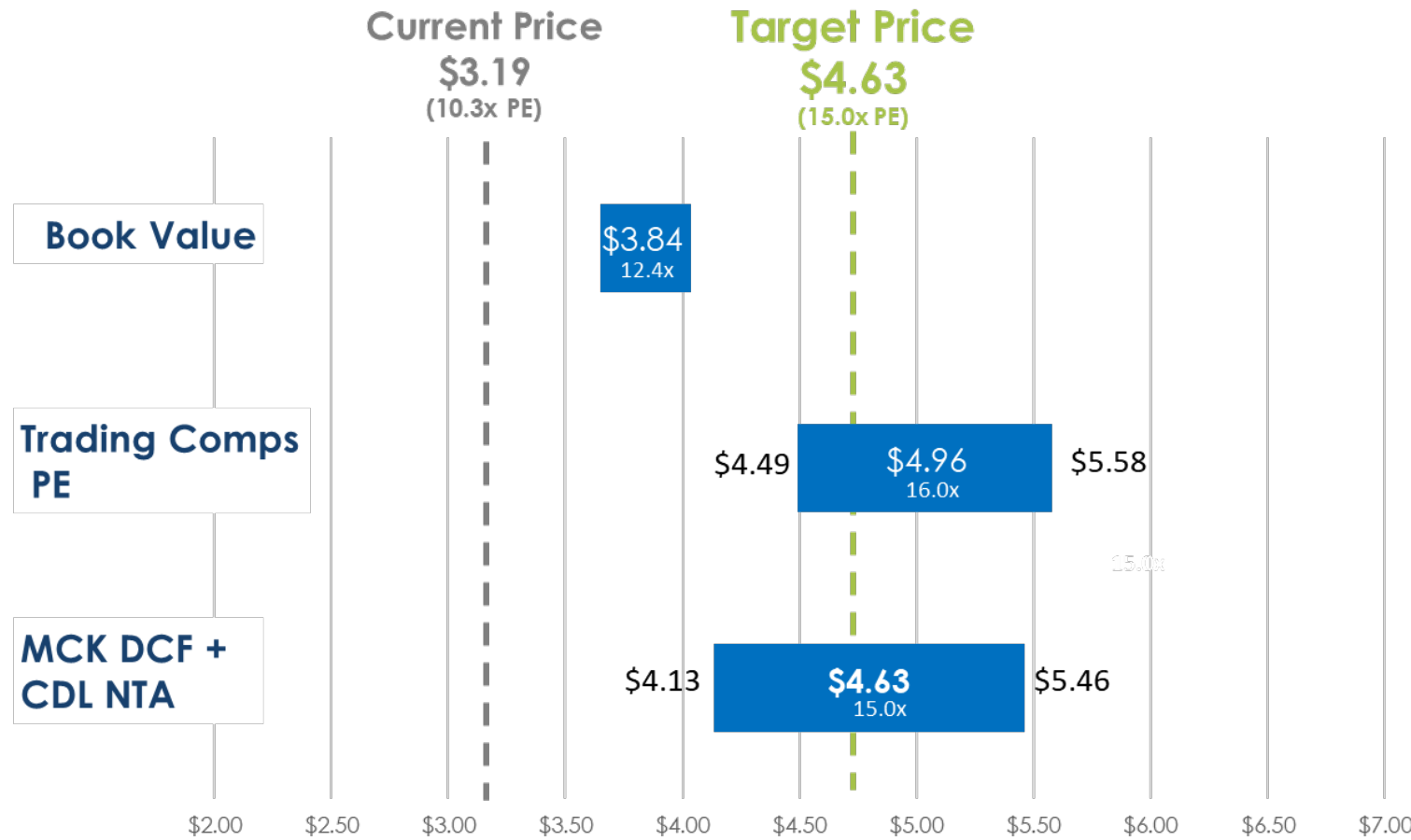
**10.3x**  
Price/Earnings

**0.83x**  
Price/book

**5.9x**  
EV/EBITDA



# Each valuation method suggests the market materially undervalues MCK



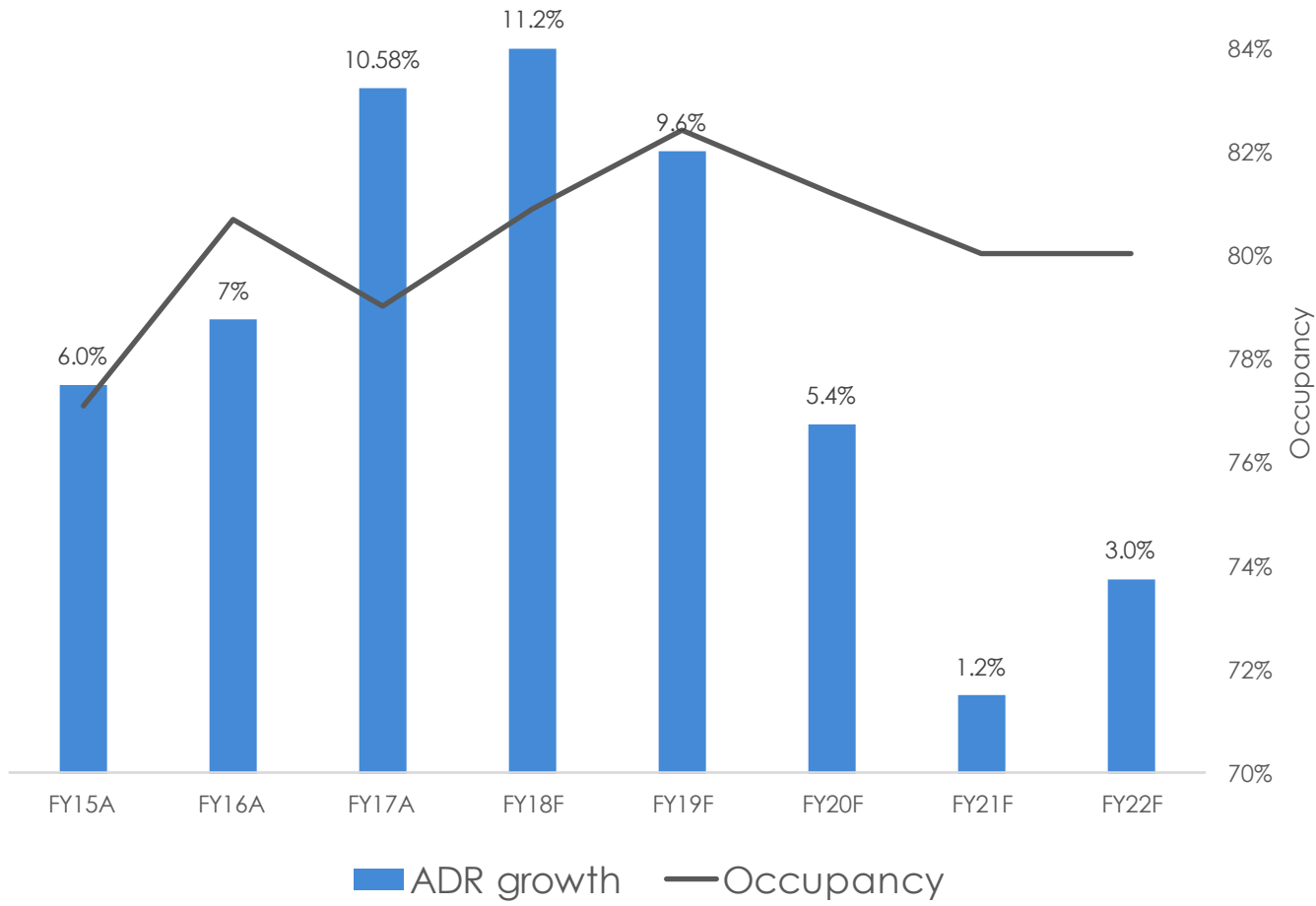
Assumptions
BV of Group NTA 30/06/18 Interim Report FY18
PE range of 14x – 18x from trading comparables
9.1% WACC, 2% TGR \$200m – \$350m CDL value

Current share price is a **31%** discount to intrinsic value

# We have used three valuation methods to assess MCK and prefer SOTP

Method	Description	Positives	Limitations
<b>Sum of the Parts</b>	MCK by DCF CDL by asset value	<ul style="list-style-type: none"> <li>✓ Account for cyclicalities</li> <li>✓ Tourism data widely available</li> <li>✓ Conservative for CDL</li> </ul>	<ul style="list-style-type: none"> <li>✗ Sensitive to a number of subjective inputs</li> </ul>
<b>Trading Comps</b>	PE range for Hotel peers	<ul style="list-style-type: none"> <li>✓ Market value reassurance</li> <li>✓ Less prone to manipulation</li> </ul>	<ul style="list-style-type: none"> <li>✗ Lack of good peers given unique NZ market</li> <li>✗ Relative, not intrinsic value</li> <li>✗ CDL should be valued differently to reflect risk</li> </ul>
<b>Book Value</b>	Book NTA of group	<ul style="list-style-type: none"> <li>✓ Provides good estimate of liquidation value</li> </ul>	<ul style="list-style-type: none"> <li>✗ BV does not recognise MCK strong earnings</li> <li>✗ Limited to most recent balance date</li> </ul>

# Our forecast assumes a strong FY18-19, then allows for a cyclical slowdown



2019-23 Occupancy and daily rate growth taken from NZTE Prospectus

Soft 2019-21 allows for potential slowdown or supply increase

Terminal 80% occupancy in line with historical average

# Our DCF indicates a midpoint valuation for the parent of \$560m

	FY17A	FY18F	FY19F	FY20F	FY21F	FY22F
Total Revenue	108,600	133,698	151,234	157,021	162,258	167,093
Operating expenses	(71,834)	(81,759)	(88,518)	(91,117)	(95,215)	(97,597)
EBITDA	36,766	51,939	62,717	65,904	67,043	69,496
D&A	(6,481)	(6,638)	(6,809)	(6,809)	(7,255)	(7,256)
EBIT	30,285	45,302	55,908	59,095	59,788	62,241
Tax		(12,684)	(15,654)	(16,547)	(16,741)	(17,427)
NOPAT		32,617	40,254	42,549	43,047	44,813
Depreciation		6,638	6,809	6,809	7,255	7,256
Capex		(14,416)	(6,806)	(27,066)	(7,302)	(7,519)
Change in WC		(9,453)	(6,138)	(2,025)	(1,833)	(1,692)
FCFF		15,385	34,119	20,266	41,167	42,858
Discount Factor		0.92	0.84	0.77	0.71	0.65
Terminal Value						613,821
PV of FCFs		14,099	28,654	15,597	29,034	27,699
PV of TV						396,721
EV	511,804					
Net cash	54,625					
<b>Equity Value</b>	<b>566,429</b>					

## Assumptions

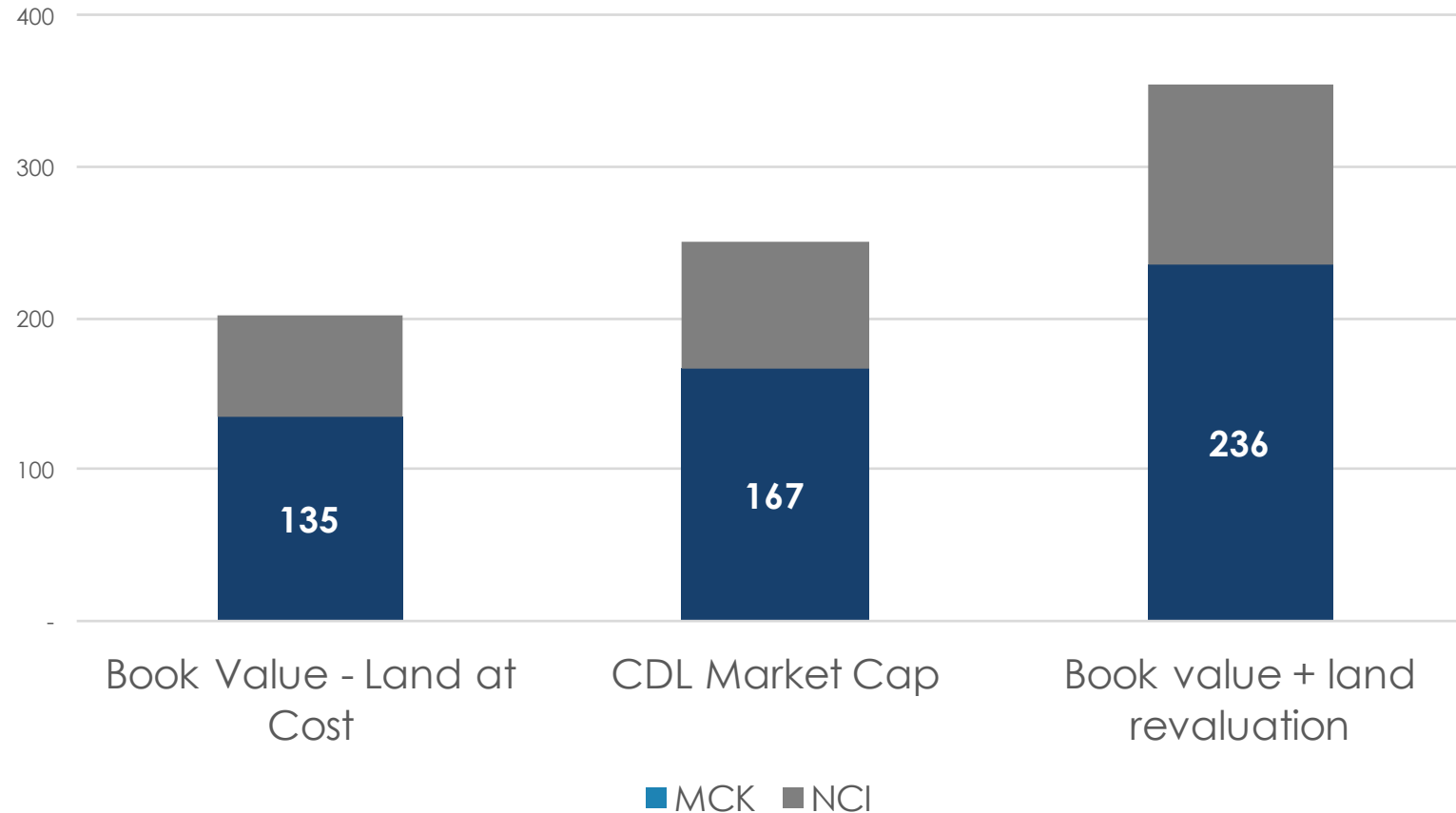
WACC of 9.1%

Maintenance Capex 4.5% of revenue, new rooms \$200k each

2% TGR conservative given long term tourism tailwinds

# Reported asset values provide a valuation range for MCKs CDL stake

NTA value of CDL (\$m NZD)



Book value at cost 30/06/2018

Market Cap of CDL on 03/10/2018

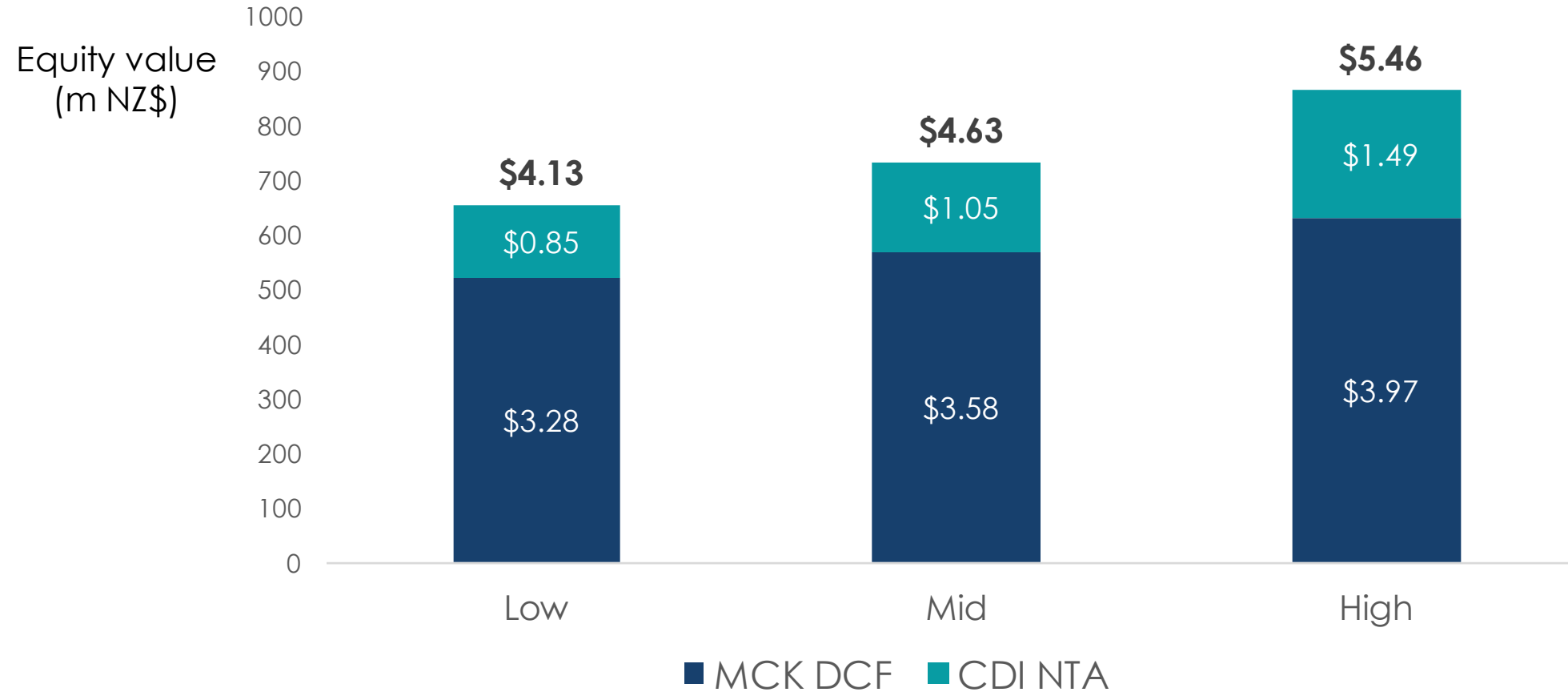
Independent land market valuation of \$276m (Cost \$125m)

**\$135m - \$236m**

Valuation range

Overall our SOTP valuation gives a range of \$4.13 to \$5.46 per share

Valuation range of **\$4.13 - \$5.46** per share





# The stock remains at a 20%+ discount under sensitivity analysis

**Terminal Growth**

		1.50%	1.75%	2.00%	2.25%	2.50%
<b>WACC</b>	8.1%	\$4.97	\$5.09	\$5.22	\$5.36	\$5.51
	8.6%	\$4.70	\$4.80	\$4.91	\$5.02	\$5.15
	9.1%	\$4.47	\$4.55	\$4.64	\$4.74	\$4.85
	9.6%	\$4.26	\$4.34	\$4.41	\$4.50	\$4.59
	10.1%	\$4.08	\$4.15	\$4.21	\$4.29	\$4.36

**Maintenance Capex %**

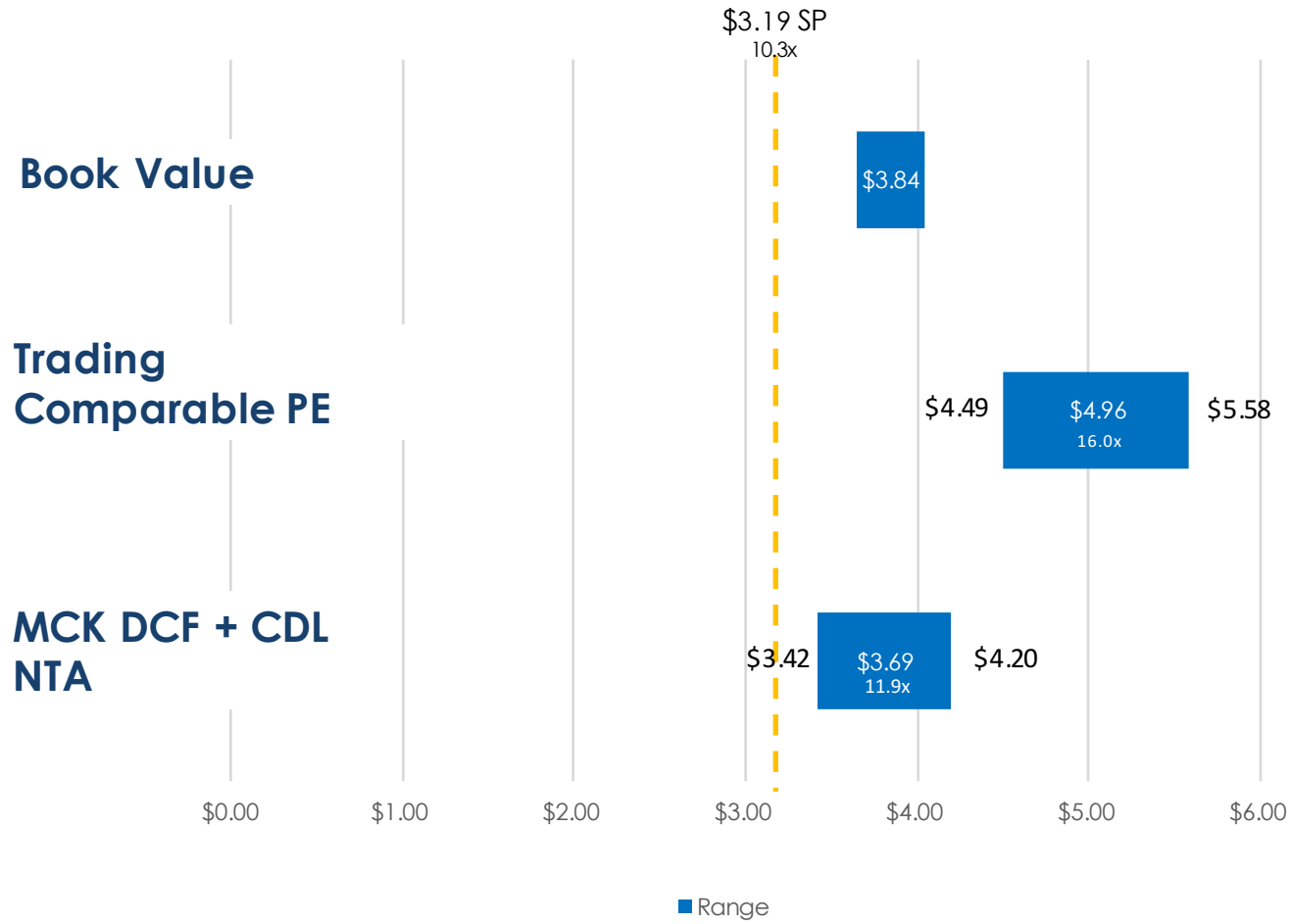
		3.00%	4.00%	4.50%	5.00%	5.50%
<b>Cost Inflation</b>	1.0%	\$4.95	\$4.82	\$4.75	\$4.68	\$4.62
	1.5%	\$4.89	\$4.76	\$4.69	\$4.63	\$4.56
	2.0%	\$4.83	\$4.70	\$4.63	\$4.57	\$4.50
	2.5%	\$4.77	\$4.64	\$4.57	\$4.51	\$4.44
	3.0%	\$4.71	\$4.58	\$4.51	\$4.44	\$4.38

**FY18-23 Daily Rate growth**

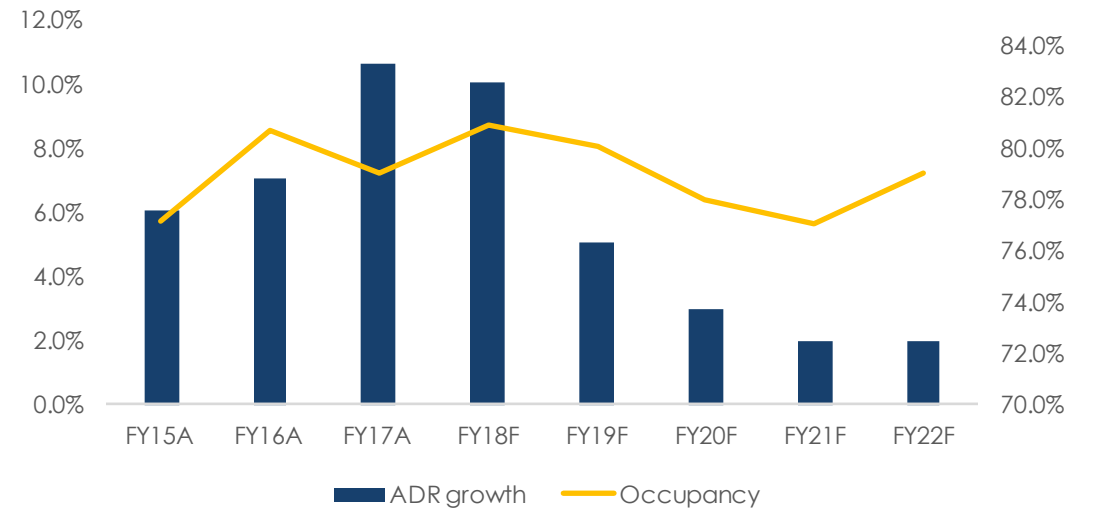
		2.00%	3.50%	5.00%	6.50%	8.00%
<b>Occupancy</b>		\$163.7	\$176.1	\$189.2	\$203.1	\$217.8
	76%	\$4.39	\$4.46	\$4.53	\$4.60	\$4.68
	78%	\$4.41	\$4.48	\$4.55	\$4.63	\$4.71
	80%	\$4.44	\$4.51	\$4.58	\$4.66	\$4.74
	82%	\$4.46	\$4.53	\$4.61	\$4.69	\$4.77
	84%	\$4.48	\$4.56	\$4.63	\$4.72	\$4.80

# A slow-down in tourism still gives a 15% upside on the current price

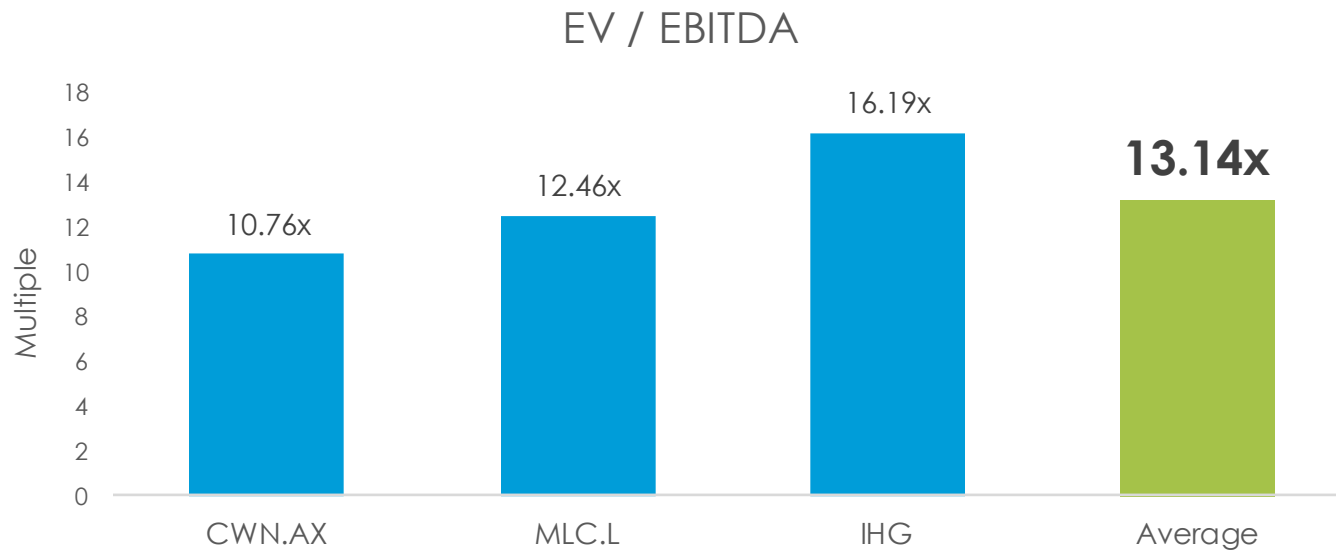
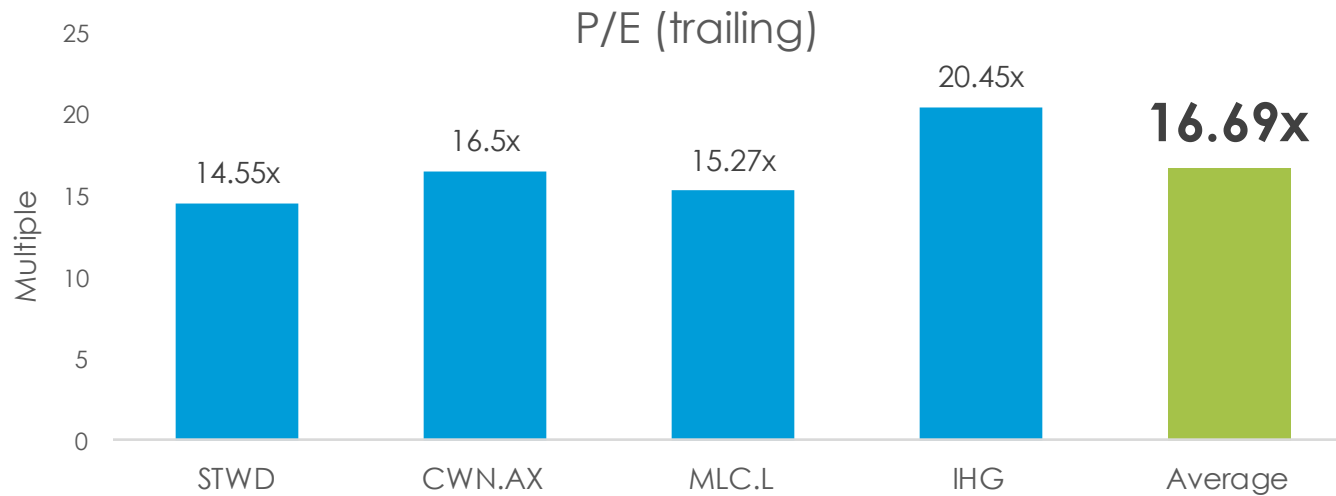
## Tourism Slow-Down Valuation



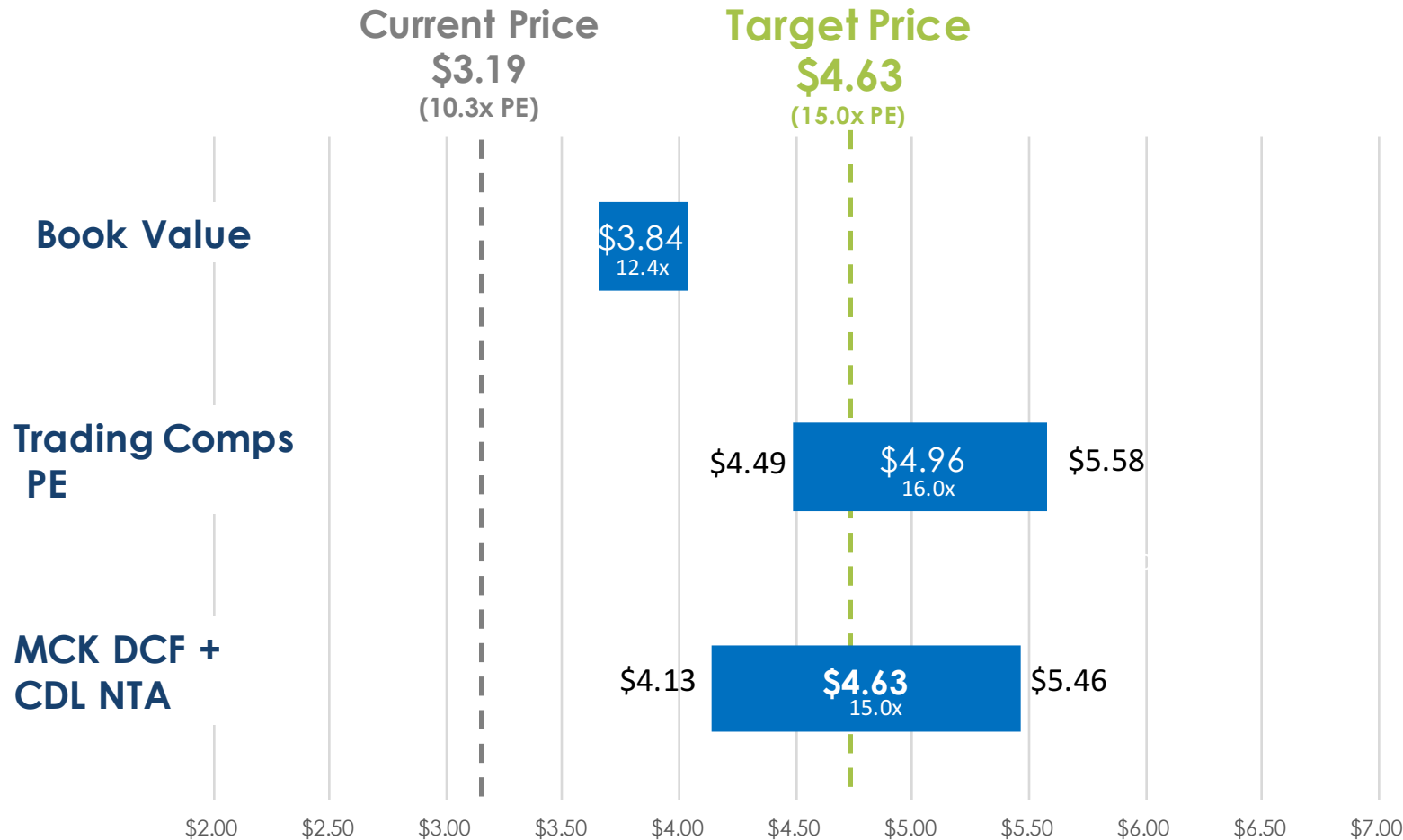
Assumption	Reasoning
ADR growth	Decreases in line with worst case tourism predictions from MFAT
Occupancy falls to 77%	Decreases in line with worst case tourism predictions from MFAT
Other expenses increase to 35% of revenue	Adjusting for the fixed component of other expenses that does not depend on revenue



# Valuation peers suggest around 16x PE or 13x EV/EBITDA



# Each valuation method suggests the market materially undervalues MCK



### Key Assumptions

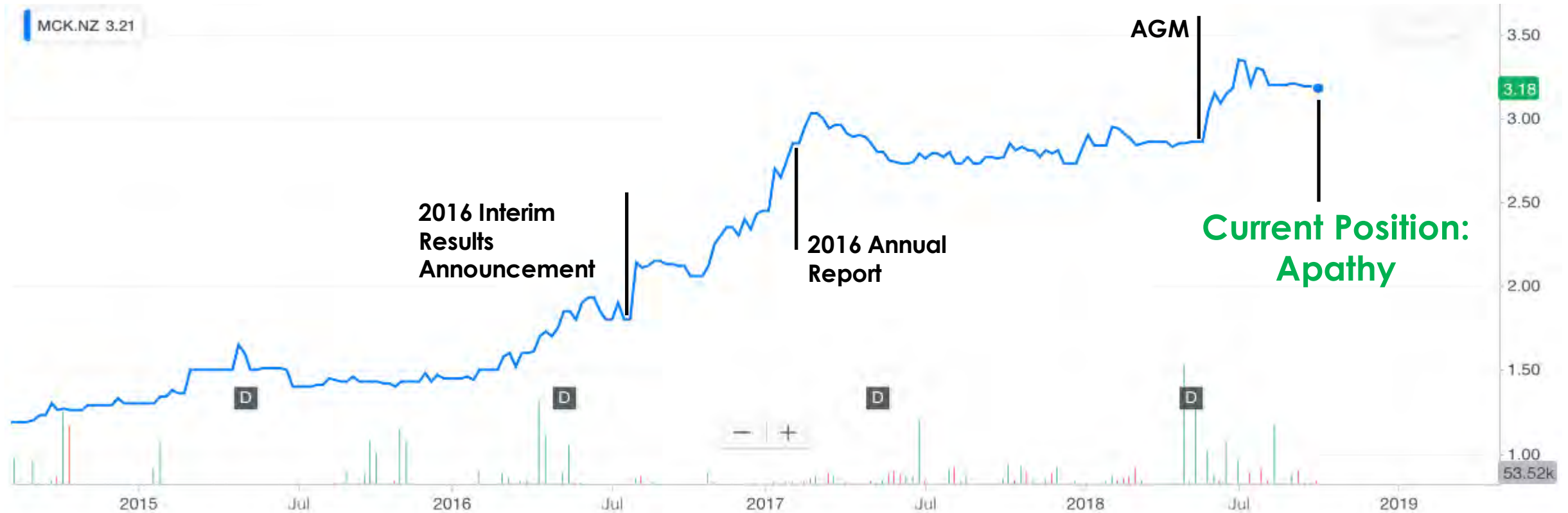
- BV of Group NTA 30/06/18
- Trading peers PE range of 14x – 18x
- 8.6 – 9.6% WACC, 1.75 - 2.25% TGR
- \$200m – \$350m CDL value

# A combination of factors have contributed to the current undervaluation

Factor	Explanation
<b>Low Free Float</b>	70% of the stock is owned by its UK parent, leaving little free float. This means it is overlooked by institutions.
<b>Outside of the NZX50</b>	Stocks outside the main index receive less media and investor attention.
<b>Lack of broker coverage</b>	Lack of broker coverage causes minimal investor attention outside of company announcements.

# MCK only receives limited coverage, leading to step-like price growth

Five-Year Price History



Long periods of apathy

Price increase after announcements

# We see an end to current apathy when the annual report is released

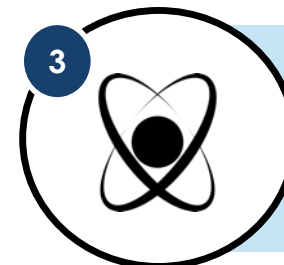
## 2016 Interim Report Publication



1 Full year contribution from new hotels



2 Further dividend increases



3 Strong interim ADR and occupancy continues

# Investment Thesis for MCK

## An established operator

Entrenched hotel operator in the attractive tourism market

## Competitive advantage

International brand recognition, a focus on secondary locations and service expertise

## Attractive industry

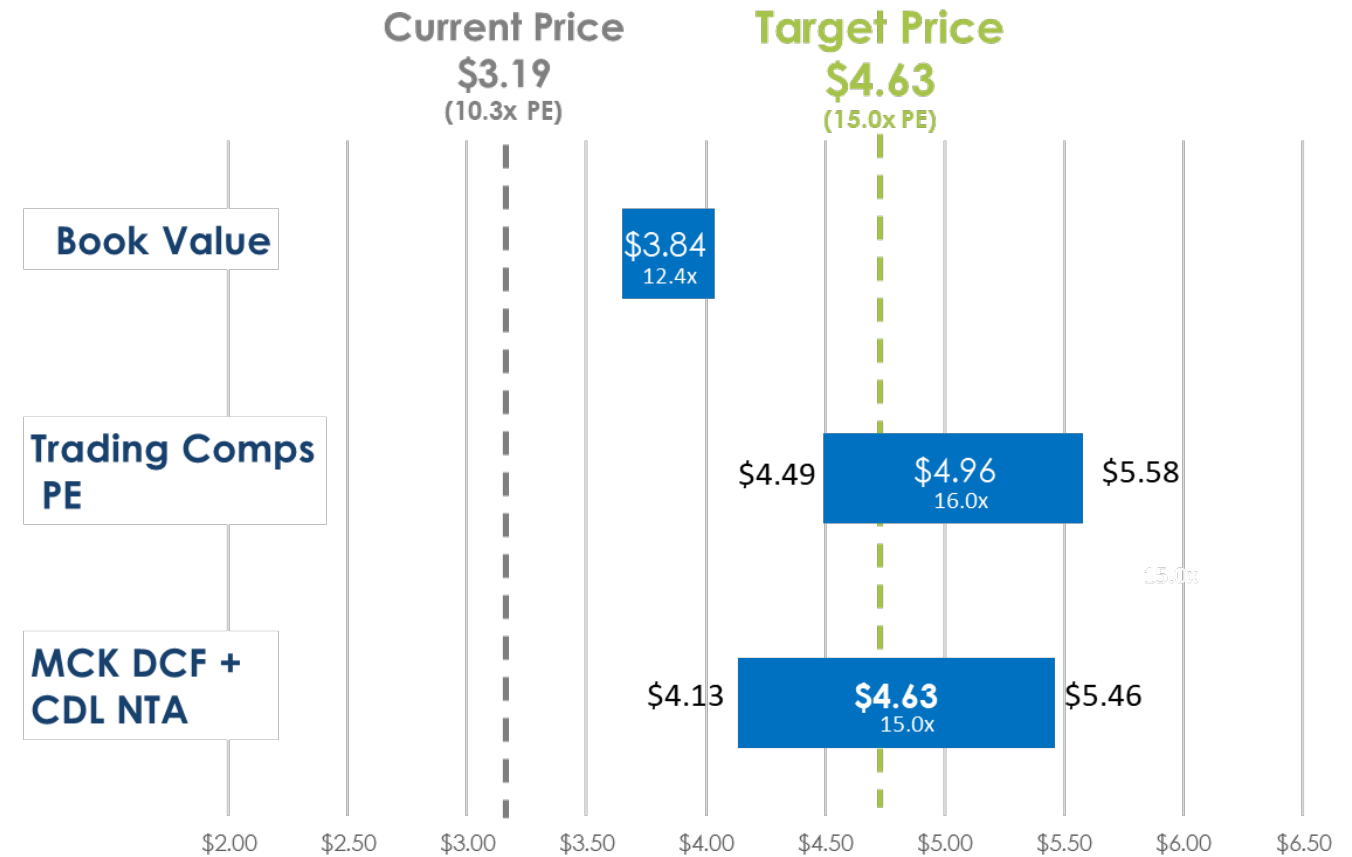
Increase in arrival and tourist spend with constrained hotel supply.

## Underappreciated by the market

Price is 31% discount to intrinsic value due to low free float and lack of broker coverage.

## With clear catalysts to a re-rating

FY18 earnings lift from new hotel openings and ADR growth.





# Appendices

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## Financial

- 31. [Sensitivity Analysis](#)
- 32. [Scenario Analysis – Tourism slowdown](#)
- 40. [DCF Inputs](#)
- 41. [CDL Book Value](#)
- 42. [WACC](#)

## Business and Industry

- 43. [Booking.com ratings](#)
- 44. [Room breakdown](#)
- 45. [Ownership breakdown](#)
- 46. [Occupancy and ADR](#)
- 47. [Auckland bed tax](#)
- 48. [Online aggregators](#)
- 49. [Historic timeline](#)

# DCF Inputs

	FY17A	FY18F	FY19F	FY20F	FY21F	FY22F
Net room growth		143	42	-	100	-
ADR growth	10.58%	11.2%	9.6%	5.4%	1.2%	3.0%
ADR	148.3	164.9	180.7	190.4	192.7	198.5
Occupancy	79.0%	80.9%	82.4%	81.2%	80.0%	80.0%

Staff costs/Av room growth rate	2%	CPI Inflation
Other expenses % revenue	30.0%	Constant
Maint capex % Sales	4.5%	Industry benchmark, matches historical
Capex per net room (\$000s)	200	Industry benchmark
D&A % Beg PPE	2.2%	Constant
Rental revenue growth	2.0%	CPI Inflation
WC % Total revenue	35.0%	Constant
Tax rate	28.0%	NZ Statutory rate
WACC	9.1%	2.6% Rf, 7% MRP, 0.93 Unlev beta
TGR	2.0%	CPI inflation









# CDL Book value composition

Low Valuation - Book						
			Net Assets	202,423		IR18
			Comprised of			
			Development Property		150,601	
			Cash		25,814	
			Bank Deposits		31,000	
			Other		(4,992)	
			MCK share	134,733		

# WACC and EV calculations

			Source
D/EV	0%		IR 18: Net debt (\$54.6m)
Risk Free		2.6%	10y NZ Gov bond
Levered Beta	1.20		NYU Stern – Hotel beta
Unlevered Beta	0.93		NYU Stern – industry gearing 40%
MRP	7%		NZ Treasury
Risk premium		6.5%	
WACC		9.1%	

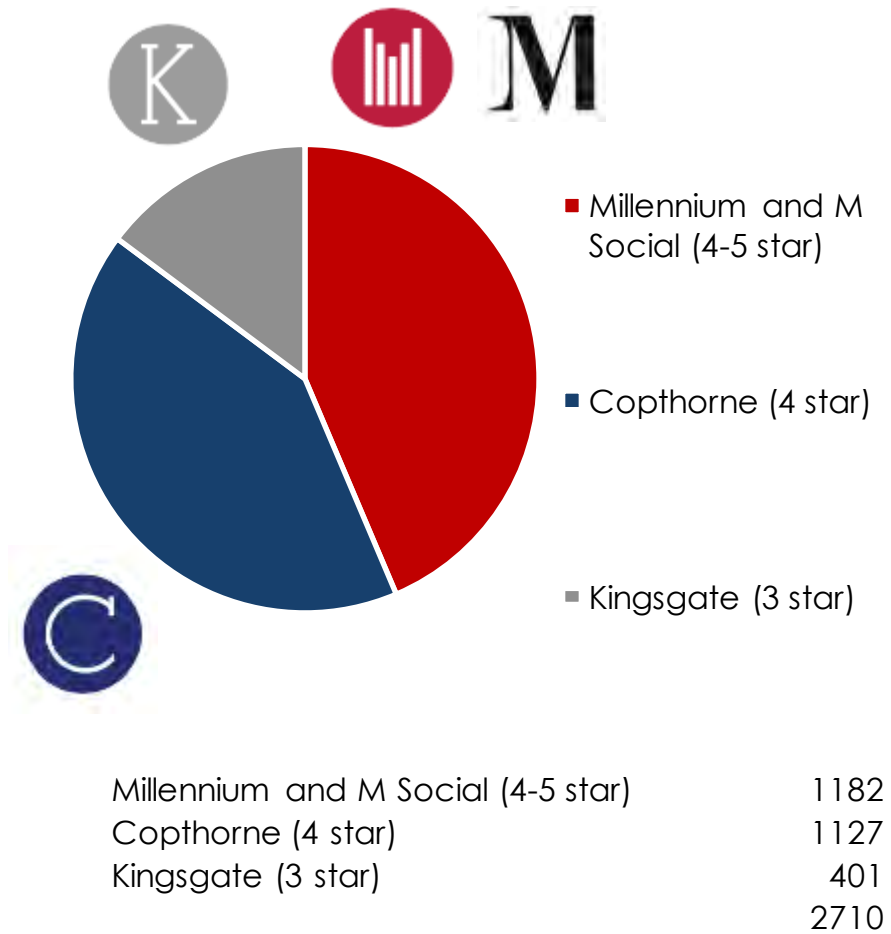
# Booking.com ratings: Average of 8.6 (room weighted)

 <p><b>Copthorne Hotel Wellington, Oriental Bay</b>            Fabulous 8.8            2,586 reviews            Location 9.3            Wellington – Show on map (950 m from centre)            In high demand! Booked 17 times in the last 24 hours            Great Value Today            Family Room – Bigger than most in Wellington            Only 4 rooms left!</p>	 <p><b>M Social Auckland</b> ★★★★★            Auckland – Show on map (700 m from centre)            In high demand! Booked 27 times in the last 24 hours            95% of guest reviewers had their expectations of this property met or exceeded            Double Room            Only 4 rooms left!</p>
 <p><b>Millennium Hotel &amp; Resort Manuels Taupo</b>            Fabulous 8.9            830 reviews            Location 9.3            Taupo – Show on map (3.1 km from centre)            7 people are looking at this moment            In high demand! Booked 11 times in the last 24 hours            Double Room            Only 3 rooms left!</p>	 <p><b>Copthorne Hotel &amp; Resort Lakefront Queenstown</b>            Very good 8.3            1,530 reviews            Queenstown – Show on map (550 m from centre)            6 people are looking at this moment            In high demand! Booked 21 times in the last 24 hours            Great Value Today            Double Room            Only 2 rooms left!</p>
 <p><b>Millennium Hotel New Plymouth, Waterfront</b>            Superb 9.1            796 reviews            Location 9.5            New Plymouth – Show on map (850 m from centre) – Beach nearby            In high demand! Booked 4 times in the last 24 hours            Twin/Double Room            Only 4 rooms left!</p>	 <p><b>Grand Millennium Auckland</b> ★★★★★            Auckland – Show on map (500 m from centre)            Popular now! 10 people are looking at this moment            In high demand! Booked 47 times in the last 24 hours            Double Room            In high demand - only 4 rooms left!</p>
 <p><b>Millennium Hotel Rotorua</b> ★★★★★            Very good 8.2            2,322 reviews            Rotorua – Show on map (800 m from centre)            4 people are looking at this moment            In high demand! Booked 17 times in the last 24 hours            Twin/Double Room            Only 4 rooms left!</p>	 <p><b>Millennium Hotel Queenstown</b> ★★★★★            Very good 8.3            1,699 reviews            Queenstown – Show on map (600 m from centre)            4 people are looking at this moment            In high demand! Booked 22 times in the last 24 hours            Double Room            In high demand - only 4 rooms left!</p>

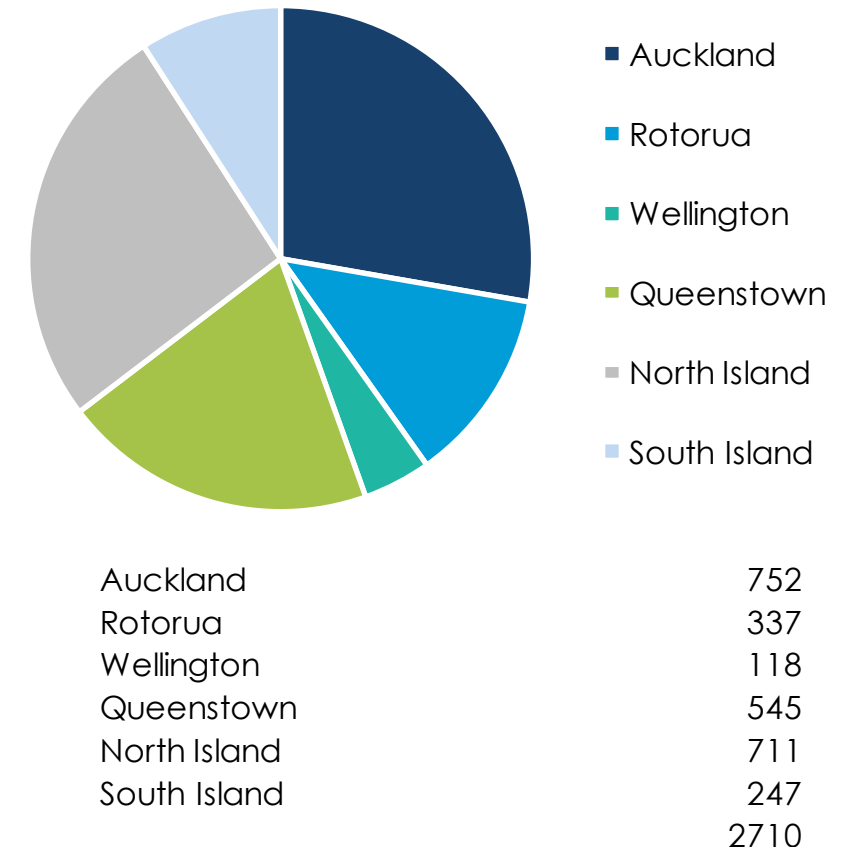
# Number of Rooms

Bay of Islands	Copthorne	180
Hokianga	Copthorne	33
Paihia	Kingsgate	113
Auckland	Millennium	452
Auckland	M Social	190
Auckland	Copthorne	110
Rotorua	Millennium	227
Rotorua	Copthorne	110
Taupo	Millennium	51
New Plymouth	Millennium	42
New Plymouth	Copthorne	60
Wanganui	Kingsgate	41
Palmerston North	Copthorne	89
Wairarapa	Copthorne	102
Wellington	Copthorne	118
Greymouth	Kingsgate	98
Queenstown	Millennium	220
Queenstown	Copthorne	240
Queenstown	Copthorne	85
Te Anau	Kingsgate	94
Dunedin	Kingsgate	55
		2710

No. of Rooms by Brand

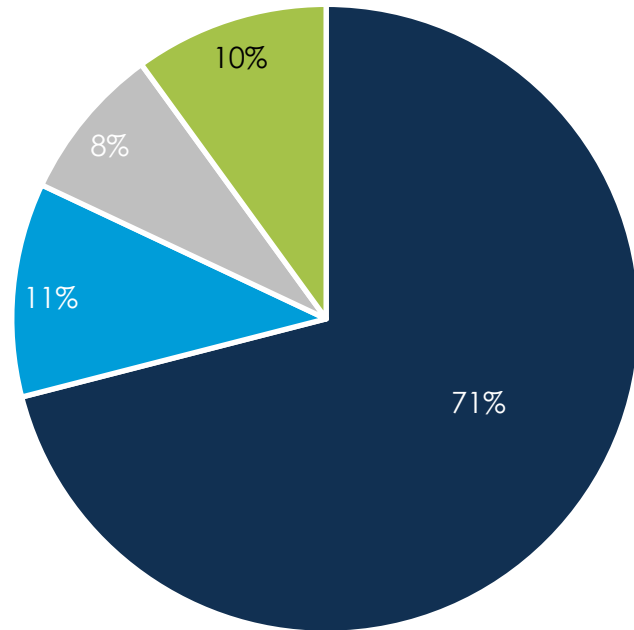


No. of Rooms by Location

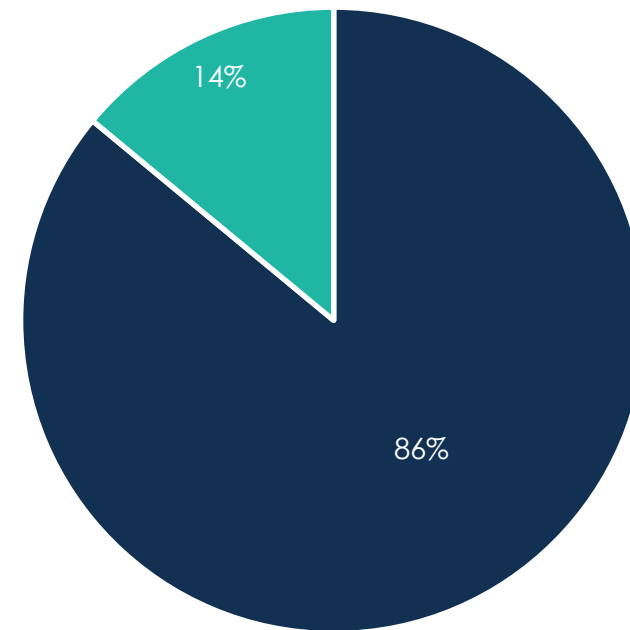


# Ownership Breakdown

Ordinary Shareholders



Preference Shareholders

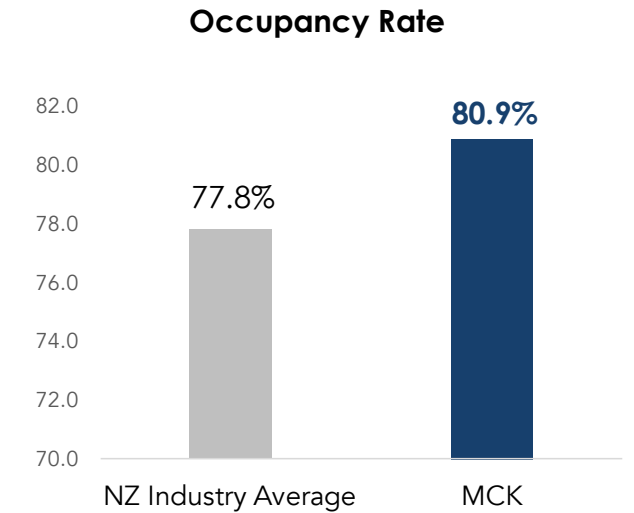


■ Parent ■ Aberdeen Investment Trust ■ Other Institutional ■ Retail

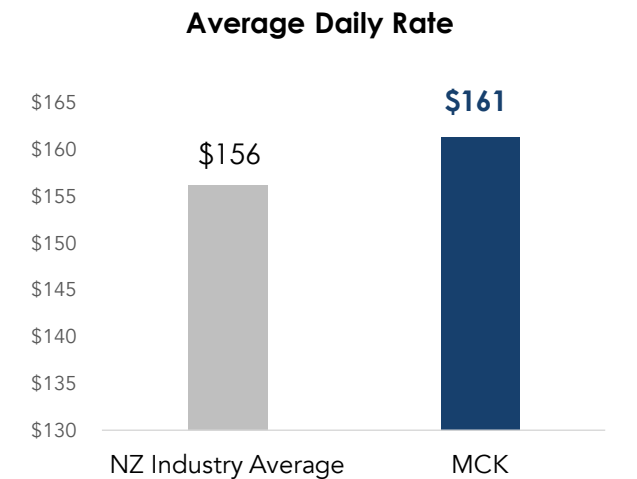
■ Parent ■ Other

# Occupancy Rate and Average Daily Rate Calculation

Occupancy	Industry	Weight	Industry Benchmark	MCK	
	Auckland	86.2	0.277		
	Rotorua	79.2	0.124		
	Wellington	80.1	0.044		
	Queenstown	83.4	0.201		
	Regional North Island	66.7	0.262		
	Regional South Island	69.3	0.091	77.84	80.9
			1.000		



Average Daily Rate	Industry	Weight	Industry Benchmark	MCK	
	Auckland	191.52	0.277		
	Rotorua	123.96	0.124		
	Wellington	176.96	0.044		
	Queenstown	238.7	0.201		
	Regional North Island	90.0	0.262		
	Regional South Island	90.0	0.091	156.08	161.3
			1.000		





# Auckland Bed Tax

● No tax on the **first 28 bed nights**

	Zone		
Tax on	A	B	C
29-135 nights	\$1673	\$1248	\$822
136-180 nights	\$3346	\$2495	\$1645
181-365 nights	\$6771	\$5069	\$3368

## Zone

- A** Albert-Eden, Devonport-Takapuna, Māngere-Ōtāhuhu, Maungakiekie-Tāmaki, Ōrākei and Waitemata
- B** Henderson-Massey, Hibiscus and Bays, Howick, Kaipātiki, Manurewa, Ōtara- Papatoetoe, Puketāpapa, Upper Harbour, Waiheke and Whau
- C** Franklin, Great Barrier, Papakura, Rodney and Waitakere Ranges

Source: Auckland Council / Herald graphic

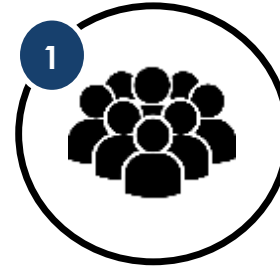


Bed tax primarily impacts Airbnb's, which are currently largely unregulated



The firm has strong presence outside of Auckland, so will be less affected than hotel chains solely based there

# Power of online aggregators



Low barriers to entry mean there are a large number of aggregators, with limited market power



Hotel aggregation was a disrupter in the early 2010s, but less so now – its impact has already been felt

# Historic Timeline

2018 February	Acquired The Waterfront Hotel New Plymouth, to be branded a Millennium Hotel
2018 ongoing	Sale of apartment units at Zenith Residences, Sydney, as leases expire
2017 October	Opened M Social Auckland, rebranded from Copthorne Hotel
2016 September	Opened Grand Millennium Auckland
2015 December	End of franchise arrangements for Kingsgate Hamilton and Kingsgate Whangarei
2015 July	Commenced major refurbishment of Copthorne Hotel Auckland Harbourcity
2015 March	End of franchise arrangement with Kingsgate Wellington
2015 February	Acquired 39% interest KIN Holdings, the holding company for MCK Australia, which include the residential units at Zenith
2014 July	Acquired of remaining 30% interest Quantum, which owns/leases Millennium Queenstown, Copthorne, Rotorua and Kingsgate Dunedin
2013 October	Demolition notice for Copthorne Hotel Christchurch
2012 November	Opened Copthorne Hotel Rotorua, rebranded from former Kingsgate Hotel.

