Stobart Group Business Analysis And Cash Flow Estimation

Contents

Stobart Group Overview

The Stobart Group has 3 divisions.

Air division – Southend Airport

It owns the Southend Airport that you can say is near London. They also own the Carlisle Lake District Airport and the Teesside International Airport but I don't think the last two matter that much. They have also bought 30% of FlyBe, the failed airline but for less than a million. It will be rebranded under Virgin.

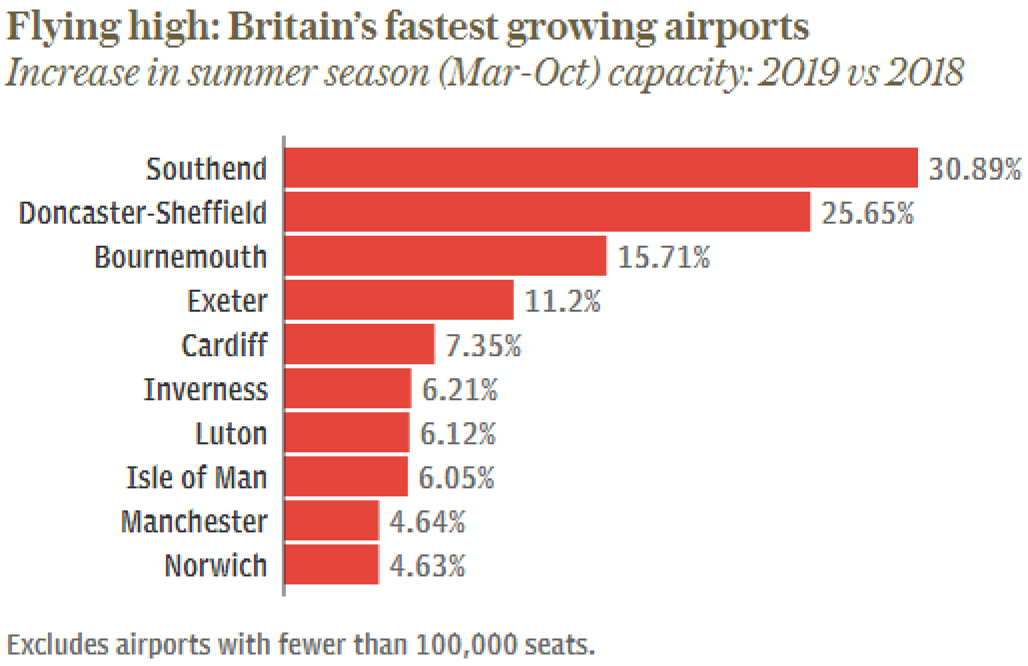
The Southend Airport is 51 minutes from London Liverpool street with 6 trains per hour.

They acquired the airport in December 2008 for £21 million – a good time to buy things. Since then they invested more than £150 million and will be investing more so that the airport can reach 5 million passengers by 2023, from the current 1.5 million. Consequenly the plan is to grow it to 10 and then 20 million.

Stobart's CEO on Youtube:

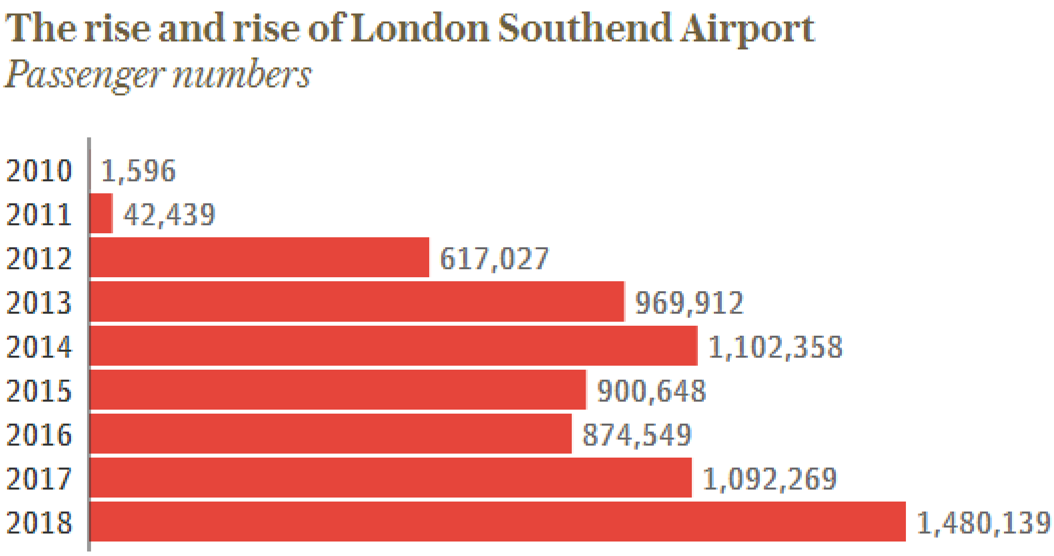
https://www.youtube.com/watch?v=b0HicgEh5WU

It is the fastest growing airport in the UK.



Source: [Telegraph]

First it was EasyJet, FlyBe, now there is also RyanAir, WizzAir etc.; possibly more in the future.



Source: [Telegraph]

They already expect 2.3 million passengers in 2020. On target for 5 million by 2023. They plan to build a new arrivals terminal, more parking and a new hotel to reach EBITDA of £8 per passenger. Currently EBTIDA per passenger is £3.55. Thus, EBITDA of 40 million expected and then higher in the future as passengers grow to 10 and 20 million. If it happens, of course! But, if they reach EBITDA of 40 million, from the current 4 million, over the next

5 years, and then go to 80 million over the other 5 years and reach 10 million passengers, the air division could be more than a 10 bagger.

The risks are there too, don't worry. Stansted has been allowed to grow to 42 million passengers, Gatwick can easily grow to 70 million if they just allow it to use the second runway (it is already there), there is the Heathrow expansion or added runway, Luton is also expanding and investing. So, that is the risk reward and we know how Ryanair and others just take their planes and goodbye. Ryanair has shut down Eindhoven and Bremen and downsized Weeze extremely quickly. I have been to Eindhoven and it was really expanding nicely, Weeze is close to bankruptcy due to Ryan leaving.

I have flown from Southend in 2014 to Amsterdam and it was still a bit shady, but as I see it is growing and more and more people use it. It all depends on the competition between airports and demand. However, on 20 million people, London, 200 million passengers per year should be ok – it is just the 20 million going somewhere 5 times per year – the return flight is another passenger 😊

Energy division – biomass fuel projects

From Stobart:

Stobart Energy is the UK's number one supplier of biomass fuel, with long-term contracts in place to supply two million tonnes per annum of biomass fuel to renewable energy plants.

- The division offers a range of solutions from municipal and commercial waste collection through to delivering fuel to renewable energy plants.
- The division comprises over 300 people delivering a full supply chain solution to renewable energy plants.
- Our goal is to maximise all opportunities to use waste for other purposes including processing end of life waste into renewable fuel..

The energy division should become increasingly cash generative soon, the management says. As of October 2018, 29 out of the 30 energy recovery plants that Stobart Energy supplies have now reached full contractual operational volumes. As a result, the volume of waste managed by Stobart Energy during the period increased by 147,713 tonnes to 805,663 tonnes - equivalent to a run rate of 1.7m tonnes per annum. This represents a 22% increase on the same period last year.

Independent valuation of the division was an equity value of £237m as at 30 June 2019, compared to a starting valuation of £100m as at 30 June 2016.

The target is to reach £12 EBITDA per tonne. At 1.7 million tonnes, the division should make 20 million in EBITDA.

Stobart Rail & Civils

Stobart Rail & Civils is one of the UK's leading providers of innovative and efficient rail and non-rail civil engineering projects. It provides specialist rail, civil and infrastructure engineering and management services to third party customers including Network Rail.

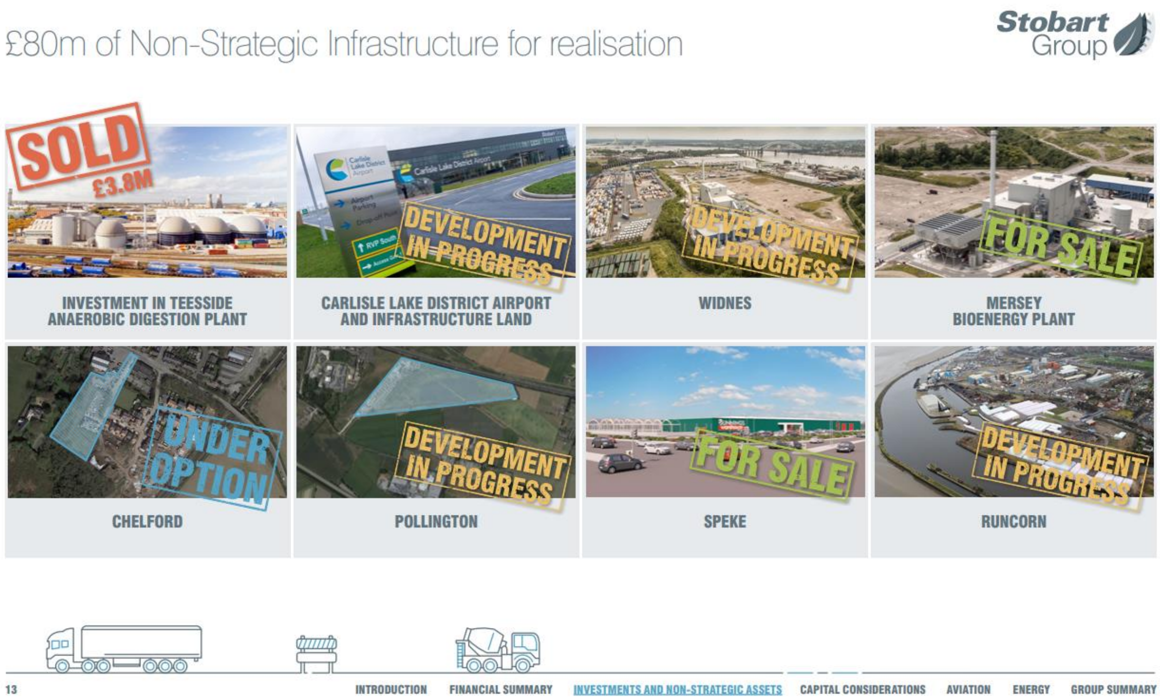
Network Rail has been slow to award work at the start of Control Period 6 (CP6) which has impacted the whole industry. Stobart Rail & Civils is now well positioned to improve its performance once the 6 CP6 issues are resolved. While the division is not material in terms of delivering the Group’s targets, the action undertaken to de-risk and re-focus the business will allow management to realise value from it in the future.

Stake in Eddie Stobart

They sold Eddie Stobart, the logistics business a while ago but still have a small stake that they pledged for their bond issue. Eddie Stobart is close to going bust on accounting issues so they made a good sale and got good money on the bond at a low interest rates of 2.75% for £53 million.

Stakes in non-core infrastructure assets

The company also owns estimated £80 million in infrastructure assets to be realized.



Source: Interim Presentation

Finances and cash flow model

So, let's start with debt. The issued a bond of 53 million, the lease obligations are now treated as debt too, so we are at 216 million.

Debt and gearing

	31 August 2019	28 February 2019
Net debt:		
- asset-backed finance	£147.5m	£97.5m
- IFRS 16 lease obligations	£76.9m	-
- cash	(£7.7m)	(£14.4m)
Total net debt	**£216.7m**	**£83.1m**
Underlying EBITDA[1]/underlying interest	3.1	2.1
Net debt/total assets	35.5%	15.2%
Gearing	88.7%	28.0%

[1] Defined in glossary in note 15

The balance sheet 610 million of assets and 366 million of total liabilities leading to an equity value of 244 million. The market capitalization is 410 million so there is not a book value there.

However, they have 20 million EBITDA from energy that is ok and then they have 4 million from the airport that they hope it will become 40 million in 2023 as EBITDA per passenger increases and the number of passengers increase. Let's say that by 2023 they reach 20 million in EBITDA to get a middle number there.

2023 the EBITDA should be 40 million, or 60, but more likely 40. On the increased debt of around 200 million as they will invest more, the interest should be 10 million, D&A should also take at least 10 million per year as they have trucks etc. (especially the energy division). So, in 2023 I can get to 20 million in cash flow approximately to be distributed. That is a 5% dividend.

Ok, they have 80 million in assets to divest and they have been rewarding shareholders with big pay-outs from those divestments in the past. However, that is mostly financial engineering and not something to hang on, especially at this stage.

However, if they reach 60 million in EIBTDA, there could be another 20, 15 after taxes for dividends, that would make it 35, that would give a dividend closer to 8% and growing.

For the six months ended 31 August 2019

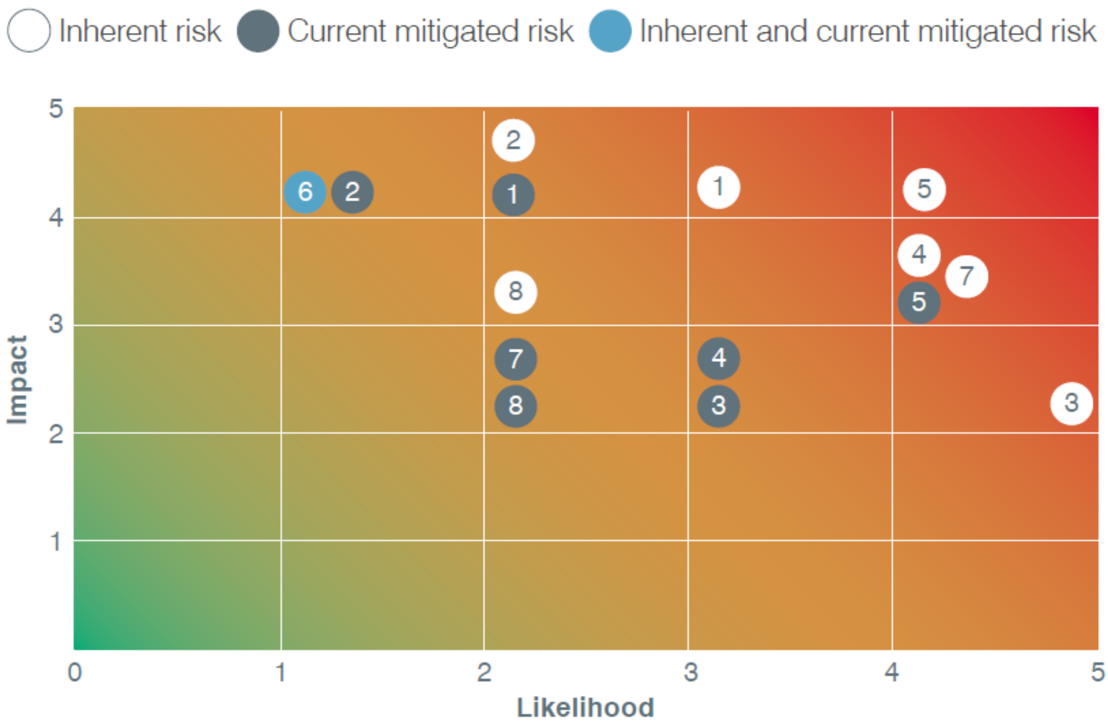
	Notes	31 August 2019 Unaudited £'000	28 February 2019 Audited £'000
Non-current assets			
Property, plant and equipment	10	329,569	262,915
Investment in associates and joint ventures		10,777	10,459
Other financial assets		28,560	44,918
Investment property		3,200	4,000
Intangible assets		88,268	100,482
Net investment in lease		13,763	-
Other receivables		47,012	44,642
		521,149	**467,416**
Current assets			
Inventories		22,740	22,559
Trade and other receivables		56,640	41,271
Cash and cash equivalents	11	7,725	14,432
Assets held for sale		2,082	1,474
		89,187	**79,736**
Total assets		**610,336**	**547,152**
Non-current liabilities			
Loans and borrowings	11	(156,016)	(84,121)
Defined benefit pension scheme		(4,006)	(3,170)
Other liabilities		(10,940)	(11,096)
Deferred tax		(10,021)	(13,560)
Provisions		(14,884)	(25,775)
		(195,867)	**(137,722)**
Current liabilities			
Trade and other payables		(49,699)	(53,648)
Loans and borrowings	11	(16,835)	(13,433)
Exchangeable bonds*	11	(51,559)	-
Corporation tax		(12,412)	(12,412)
Provisions		(8,341)	(5,438)
Liabilities held for sale		(31,447)	(27,545)
		(170,293)	**(112,476)**
Total liabilities		**(366,160)**	**(250,198)**
Net assets		**244,176**	**296,954**
Capital and reserves			
Issued share capital		37,082	37,082
Share premium		324,379	324,379
Foreign currency exchange reserve		(732)	480
Reserve for own shares held by employee benefit trust		(8,759)	(12,154)
Retained earnings		(107,794)	(52,833)
Total Equity		**244,176**	**296,954**

* In accordance with IAS 1 it is necessary for the secured guaranteed exchangeable bonds (Bonds), issued on 3 May 2019, to be presented as a current liability because the Group does not have an unconditional right to defer

Main risks

1. Loss of customer due to concentration – think Ryanair leaving
2. Licence and regulation breach

3. Cyber or crime attack, data breach
4. Health and safety
5. BREXIT
6. Incidents at airport
7. Fire or floods
8. Market dynamics



Source: Annual report

For me, the biggest risk is slower than expected growth of Stansted. Brexit can have a big impact on airline decision making and you can easily see less growth or even a decline on the airport.

The waste management seems stable with 28 plants where it should be diversified in case we have local financing issues in the UK.

The stock

I somehow have a strange feeling this stock will double soon. The EBITDA is already at 25 million, put a 15 valuation on that and you get 375 million that is close to where we are now. However, if they just grow EBITDA to 40 million, that is already 600 million plus future potential growth.

For me to be interested, I would need to see the dividend yield in 2023, on a conservative estimation of 40 million EBITDA, to be at 10% at least. Thus, the stock should fall to 60 or something like that. Highly unlikely.

Western stocks are expensive, and everything is priced accordingly. This could do well over time, but there are risks and it is priced accordingly.

Don't get confused by the high price a year ago, they divested a lot and paid hefty dividends.

And here is where they lose me:

Share movements and dividends

	2019	2018
Interim per share	6.0p	13.5p
Final per share	3.0p	4.5p
Total dividend per share	**9.0p**	**18.0p**

The Board has proposed a final dividend of 3.0p per share which, subject to the approval of shareholders at the AGM, will be payable to investors on the record date of 21 June 2019, with an ex-dividend date of 20 June 2019, and will be paid on 31 July 2019.

On 18 January 2019, the Group issued 16,492,884 shares at a price of 150p per share to Cyrus Capital Partners LP, raising £24.7m.

During the year, the Group purchased 1.5 million treasury shares for net consideration of £3.4m. Subsequently, 7.0 million treasury shares were transferred to the employee benefit trust and no shares were held in treasury at the year end.

They issue shares at 150p and buy back at 226p 😊 That is genious.

I really wanted to find something nice out of all of these FTSE work, but it is better to be avoided ☹

The environment is so focused on pleasing the market, chasing returns etc. instead of focusing on the business. Paying dividends and raising money, what???!?!?!?!?!?!?!

The risk of it all it too high to just bet that their airport growth estimations are right. It could happen for sure, but how can I know that now??

Going to the next sector ☹