



## GUD Holdings

GUD

Buy

\$5.52

### Debt-free by end of FY04 if no suitable acquisitions undertaken

30 July 2003

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GUD has reported a FY03 NPAT of \$27.4m on revenue of \$372m, which was ahead of our expectations. With upside to our forecasts available from an improved turnaround in the drought-impacted Victa operation and bolt on acquisition opportunities, we remain positive on GUD given its strong fundamentals, cashflow generating capability and proven management. Following this result the DCF valuation has increased to \$6.10, thus we retain the Buy recommendation.

- ▶ **1H03 result ahead of BBY forecasts;** GUD reported FY03 NPAT of \$27.4m (pre one-off items) on revenue of \$372m, representing EPS growth of 34% over the period, which was slightly ahead of BBY forecasts with a general improved result from all divisions the driver of upside surprise.
- ▶ **Operating cashflow the highlight within result;** Operating cashflow of \$41.5m was significantly ahead of our expectation of \$30.5m, driven both by improved operating profit and further reductions in working capital. FY04 cashflows are expected to be similar, with management expecting a debt-free balance sheet by the end of FY04 if a suitable acquisition can't be found.
- ▶ **Victa turnaround a key FY04 driver;** Following this result we have upgraded FY04 and FY05 forecasts, with both operating earnings growth and interest expense reduction the primary drivers of earnings growth. Nonetheless, we consider there is upside to our forecasts should drought conditions ease, which is likely to drive lawnmower sales following a 20% contraction of the market in FY03.

Year ending June	2003	2002	%chg
Sales revenue	372	366	2%
EBITDA	54.3	45.4	19%
Dep'n and amort'n	10.0	10.5	-5%
<b>EBIT</b>	<b>44.3</b>	<b>34.9</b>	<b>27%</b>
Net interest expense	3.7	5.3	-29%
Pre-tax profit	40.6	29.6	37%
Tax expense	13.2	8.8	49%
<b>Net profit (pre abn's)</b>	<b>27.4</b>	<b>20.8</b>	<b>32%</b>
Abn's / extra's	-5.6	-14.4	-61%
Reported profit	21.8	6.4	240%
Tax rate (%)	32.5%	29.9%	
<b>EBIT margin (%)</b>	<b>11.9%</b>	<b>9.5%</b>	
<b>EPS</b>	<b>46.0</b>	<b>34.3</b>	<b>34%</b>
DPS	26.0	16.5	58%

#### Company Information

Price		\$5.52
Target Price (12 month)		\$6.10
<b>Difference</b>		<b>+ 11%</b>
Shares (diluted)	61.2M	Market cap. \$338M
High/low (12 month)	\$5.52/\$3.10	Monthly turnover \$11.6M

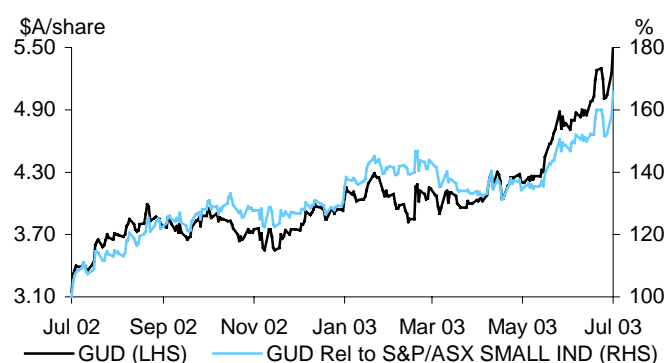
#### Earnings Summary

Year ending Jun	2002	2003	2004F	2005F
NPAT (reported) (A\$M)	20.8	27.4	31.2	34.4
BBY adj NPAT (A\$M)	22.1	28.4	32.2	35.4
EPS (¢)	34.3	46.0	52.6	58.0
PER	16.1 x	12.0 x	10.5 x	9.5 x
EPS Growth	78%	34%	14%	10%
EV / EBITDA	8.3 x	6.6 x	5.9 x	5.4 x
CFPS (¢)	55.3	67.3	67.5	67.1
Price / CF	10.0 x	8.2 x	8.2 x	8.2 x
Dividend (¢)	16.5	26.0	30.0	33.0
Yield	3.0%	4.7%	5.4%	6.0%
Franking	55%	100%	100%	100%
NTA per share	\$1.15	\$1.26	\$1.59	\$1.90

#### Earnings Forecast Changes

	2004F	2005F
NPAT (BBY adj) Change (%)	6%	6%
EPS (BBY adj) Change (%)	6%	6%

#### GUD versus Small Industrials Index





## Organic growth drives FY03 result

### Result ahead of BBY expectations

GUD reported FY03 NPAT of \$27.4m (pre one-off items) on revenue of \$372m, which was slightly ahead of BBY forecasts. Key points to the result were:

### Operating cashflow the result highlight

- ▶ **One-off items;** The result included a \$7m pre-tax provision for environmental remediation at the Campsie manufacturing site
- ▶ **Strong operating cashflow;** Operating cashflow of \$41.5m was significantly ahead of our expectation of \$30.5m, driven both by improved operating profit and further reductions in working capital.
- ▶ **15c final dividend;** The 15.0cps final dividend (fully-franked) provided a total of 26.0c for FY03 and represents a payout ratio of ~56%
- ▶ **Low debt levels;** The improved operating cashflow generation decreased net debt to \$21m at the end of the year, representing gearing of only 16%
- ▶ **Continued ROE improvement:** Over the past two years ROE has improved from 10% in FY01 to 23% in FY03 despite the rapid reduction in gearing

## Sunbeam/Victa a standout result given impact of the drought

Table 1 below provides a segment summary of the GUD FY03 result.

**TABLE 1: GUD FY03 SEGMENT RESULT SUMMARY**

### Sunbeam Victa the standout division given impact of drought

		FY03	FY02	% Change	1H03	2H03
Sunbeam Victa	Revenue	201	206	-2%	107	94
	EBIT	20.8	15.9	31%	11.5	9.3
	EBIT Margin	10.3%	7.7%		10.7%	9.9%
Ryco/Wesfil	Revenue	86	84	2%	44	42
	EBIT	15.2	12.7	20%	7.1	8.1
	EBIT Margin	17.7%	15.1%		16.2%	19.3%
Davey	Revenue	72	64	13%	40	32
	EBIT	7.4	5.6	32%	3.9	3.5
	EBIT Margin	10.3%	8.8%		9.7%	11.0%
Lock Focus	Revenue	14	12	9%	7	7
	EBIT	2.1	1.8	17%	1.1	1.0
	EBIT Margin	15.6%	14.5%		15.7%	15.4%
GROUP	Revenue	372.4	365.9	2%	198	174
	EBIT	45.2	34.9	30%	23.2	22.0
	EBIT Margin	12.1%	9.5%		11.7%	12.6%

Source: GUD, BBY

- ▶ **Sunbeam Victa:** The revenue decline of -2% was attributable to the sale of Sunbeam Rural and also the impact of the drought on lawnmower sales. However a strong Christmas and the cost savings arising from the relocation of the Victa factory and offshore sourcing of Sunbeam appliances generated strong margin expansion.
- ▶ **Ryco/Wesfil:** continued to benefit from restructuring initiatives with EBIT margins expanding from 15.1% in FY02 to 17.7% in FY03 (notably with margins of 19.3% achieved in 2H03).
- ▶ **Davey;** was a beneficiary of drought conditions in Australia through increased demand for irrigation and firefighting pumps, and also through an improvement in international sales.



- ▶ **Lock Focus;** Excluding \$0.9m of costs associated with the winding up of Asian operations, the Lock Focus division enjoyed margin expansion despite the impact of competitors in 2H03 arising from the stronger \$A.

## Capital utilisation increasingly important

### Company anticipates continued growth in FY04

**All metrics have seen improvement over past few years**

GUD's operational turnaround has been reflected in improved margins (EBIT margins improving from 7.4% in FY01 to 11.9% in FY03), ROE (10% to 23% in the same period) and a reduction in debt levels (from gearing of 56% to 16%).

Management expects a continuation of this turnaround with further growth anticipated in FY04, both organic (driven by new product releases) and also from ongoing operational improvements.

We have upgraded FY04 and FY05 forecasts by 6% following this result, with a modest improvement in operating earnings and an ongoing reduction in debt the key drivers.

**Victa improvement a key likely FY04 earnings driver**

Nonetheless, should lawnmower markets return to more normal levels when drought conditions ease we consider there is further upside to our FY04 forecasts, more likely in 2H04 than 1H04.

### Debt-free by end of year if no acquisitions are undertaken

**Management anticipate debt-free balance sheet by end of FY04 if no acquisitions found**

Operating earnings growth and further working capital improvements are expected to decrease debt further, with management anticipating a debt-free balance sheet by the end of FY04 in the absence of acquisitions.

The competitive nature of the smaller diversified industrials industry has made identifying acquisition opportunities over the past year that meet GUD's strict acquisition criteria difficult, although management have indicated that they expect to complete an acquisition by the end of FY04.

### Cashflows and balance sheet offer growth options

**Upside to forecasts from acquisitions...**

On our earnings forecasts (which assume eps growth of 14% in FY04) we consider GUD is appropriately priced on a PER:growth basis, however there is upside potential to our forecasts both from an improved Victa turnaround and also from bolt-on acquisitions and the company's strong fundamentals offer a modest rerating potential.

**...capital utilisation important if no acquisitions found**

Additionally, should a suitable acquisition not be found in FY04 we consider there is considerable scope for a higher dividend or continuation of the share buyback.

We highlight that we consider a higher dividend as more likely than a restart of the buyback given the last parcel of shares purchased under the current buyback arrangement was at \$4.05.

Following the above-expectations FY03 result the DCF valuation has increased to \$6.10, thus we continue to recommend GUD as a Buy, with shareprice appreciation anticipated as forecast earnings growth materialises and/or acquisitions undertaken.

## GUD Holdings (GUD:\$5.52)

Buy

## Valuation data

Year ending Jun	2001	2002	2003	2004F	2005F
EPS pre goodwill (¢)	19.3	34.3	46.0	52.6	58.0
P/E ratio	28.7 x	16.1 x	12.0 x	10.5 x	9.5 x
P/E relative *			94	94	92
EPS growth	6%	78%	34%	14%	10%
EPS pre abn's (¢)	17.3	32.3	44.4	51.0	56.4
P/E ratio	31.8 x	17.1 x	12.4 x	10.8 x	9.8 x
P/E relative *			97	97	94
EPS growth	5%	86%	38%	15%	11%
EV / EBIT	16.3 x	10.8 x	8.1 x	7.2 x	6.4 x
EV / EBITDA	11.4 x	8.3 x	6.6 x	5.9 x	5.4 x
CFPS (¢)	19.4	55.3	67.3	67.5	67.1
Price / CF	28.4 x	10.0 x	8.2 x	8.2 x	8.2 x
DPS (¢)	15.0	16.5	26.0	30.0	33.0
Yield	2.7%	3.0%	4.7%	5.4%	6.0%
Franking	100%	55%	100%	100%	100%
NTA per share	\$1.13	\$1.15	\$1.26	\$1.59	\$1.90
Pr / NTA	4.9 x	4.8 x	4.4 x	3.5 x	2.9 x

## Profit and loss (\$M)

Year ending Jun	2001	2002	2003	2004F	2005F
Sales revenue	341.2	365.9	372.4	387.8	399.4
growth over pcp	4%	7%	2%	4%	3%
EBITDA	36.2	45.4	54.3	56.9	58.8
Dep'n and amort'n	9.7	9.2	9.0	9.2	8.3
EBITAg	26.4	36.2	45.3	47.7	50.6
Goodwill amortisation	1.3	1.3	1.0	1.0	1.0
EBIT	25.1	34.9	44.3	46.7	49.6
growth over pcp	4%	39%	27%	5%	6%
Net interest expense	6.5	5.3	3.7	1.6	(0.4)
Pre-tax profit	18.6	29.6	40.6	45.2	49.9
Tax	6.9	8.8	13.2	14.0	15.5
Effective tax rate	37.3%	29.9%	32.5%	31.0%	31.0%
Preference dividends	0.0	0.0	0.0	0.0	0.0
Minorities	0.0	0.0	0.0	0.0	0.0
BBY adjustments	1.3	1.3	1.0	1.0	1.0
BBY adj profit	13.0	22.1	28.4	32.2	35.4
Reported profit (pre abn)	11.7	20.8	27.4	31.2	34.4
One-off items (post tax)	(1.0)	(14.4)	(5.6)	0.0	0.0
Reported net profit	10.7	6.4	21.8	31.2	34.4

## Ratio analysis

Year ending Jun	2001	2002	2003	2004F	2005F
EBITDA / sales	10.6%	12.4%	14.6%	14.7%	14.7%
EBITAg / sales	7.7%	9.9%	12.2%	12.3%	12.7%
EBIT / sales	7.4%	9.5%	11.9%	12.0%	12.4%
Return on assets	10%	15%	21%	22%	23%
Return on equity	10%	17%	23%	24%	23%
Dividend cover	1.3 x	2.1 x	1.8 x	1.8 x	1.8 x
Net debt / (cash) (\$M)	73.0	38.0	20.9	(1.5)	(18.8)
Debt / equity	67%	40%	34%	14%	2%
Net debt / equity	56%	31%	16%	nmf	nmf
Interest cover	3.9 x	6.6 x	11.8 x	nmf	nmf

## Balance sheet (\$M)

Year ending Jun	2001	2002	2003	2004F	2005F
Cash	14.6	11.1	21.8	21.8	21.8
Receivables	50.2	55.2	49.9	54.3	59.9
Inventories	74.0	57.4	60.0	62.0	63.9
Other	7.9	7.5	5.7	5.7	5.7
<b>Current assets</b>	<b>146.7</b>	<b>131.2</b>	<b>137.3</b>	<b>143.8</b>	<b>151.3</b>
Net PPE	58.6	40.9	37.5	34.3	32.0
Investments	0.0	0.0	0.0	0.0	0.0
Goodwill	12.0	11.2	10.2	9.2	8.2
Other intangibles	46.6	39.9	40.6	39.6	38.6
Other	3.7	6.1	6.7	6.7	6.7
<b>Non-current assets</b>	<b>120.8</b>	<b>98.1</b>	<b>95.1</b>	<b>89.9</b>	<b>85.6</b>
<b>Total assets</b>	<b>267.5</b>	<b>229.3</b>	<b>232.4</b>	<b>233.7</b>	<b>236.9</b>
Debt	87.6	49.0	42.6	20.3	3.0
Provisions	11.5	22.3	22.9	25.9	27.9
Other	37.6	36.3	40.0	42.7	43.9
<b>Total liabilities</b>	<b>136.7</b>	<b>107.6</b>	<b>105.6</b>	<b>88.8</b>	<b>74.8</b>
Equity / reserves	118.6	111.9	108.0	108.0	108.0
Retained profits	12.1	9.8	18.8	36.9	54.1
<b>Total s/h funds</b>	<b>130.7</b>	<b>121.7</b>	<b>126.8</b>	<b>144.9</b>	<b>162.1</b>
Minorities	0.1	0.1	0.0	0.0	0.0
<b>Total funds emp.</b>	<b>267.5</b>	<b>229.3</b>	<b>232.4</b>	<b>233.7</b>	<b>236.9</b>

## Cashflow (\$M)

Year ending Jun	2001	2002	2003	2004F	2005F
EBIT	25.1	34.9	44.3	46.7	49.6
Net interest paid	(6.2)	(5.3)	(3.7)	(1.6)	0.4
Dep'n and amort'n	11.0	10.5	10.0	10.2	9.3
Tax paid	(3.4)	(3.4)	(9.0)	(13.2)	(14.0)
<b>Gross cash from op'ns</b>	<b>26.5</b>	<b>36.7</b>	<b>41.5</b>	<b>42.2</b>	<b>45.2</b>
(Inc) / dec in wk'g cap	(13.4)	11.3	6.5	(3.8)	(6.2)
Other	0.1	(12.3)	(6.5)	3.0	2.0
<b>Operating cashflow</b>	<b>13.2</b>	<b>35.7</b>	<b>41.5</b>	<b>41.3</b>	<b>41.1</b>
growth over pcp	-56%	170%	16%	-1%	-1%
<i>Investing cashflows</i>					
Capital expenditure	(3.9)	(7.9)	(7.6)	(7.0)	(7.0)
Asset sales	1.4	10.9	4.3	2.0	2.0
Investments	0.0	0.0	0.0	0.0	0.0
Divestments	0.0	12.5	0.0	0.0	0.0
<i>Financing cashflows</i>					
Equity raised	(4.2)	(6.9)	(4.7)	0.0	0.0
Dividends paid	(8.8)	(9.5)	(12.2)	(13.9)	(18.7)
<b>Chg in loans</b>	<b>17.2</b>	<b>(38.7)</b>	<b>(6.4)</b>	<b>(22.4)</b>	<b>(17.3)</b>
Other non-op flows	(0.4)	(1.7)	(4.2)	0.0	0.0
<b>Net chg in cash</b>	<b>14.0</b>	<b>(3.8)</b>	<b>10.9</b>	<b>0.0</b>	<b>0.0</b>

## Interims (\$M)

Half yearly	1h01	2h01	1h02	2h02	1h03
Sales revenue	183.5	157.8	192.7	173.1	198.0
EBITDA	22.8	13.4	22.8	22.6	28.0
EBIT	17.3	7.9	17.4	17.5	23.2
BBY adj profit	10.0	3.0	11.1	11.0	15.2
Reported profit	9.4	2.3	10.5	10.3	14.7
EBIT / sales	9.4%	5.0%	9.0%	10.1%	11.7%
EPS (¢)	14.6	4.5	17.1	17.2	24.6
DPS (¢)	7.5	7.5	7.5	9.0	11.0
% of FY sales	53.8%	46.2%	52.7%	47.3%	53.2%
% of FY EBIT	68.7%	31.3%	49.8%	50.2%	52.3%

\* Relative to BBY growth companies universe



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