

W A Stockwell

We reiterate our Outperform recommendation on W A Stockwell's 7.25% notes due 2021. The credit outlook is Stable.

Executive summary

- Stockwell Group (Stockwell, Group) has released summary management accounts and a trading update for the financial year ending 30 June 2018. All company releases are available to investors via Stockwell's website. Full audited accounts are expected to be available towards the end of October. Given the limited financial details of the release, we will not update our model until full accounts are available.
- While broadly there is weakness in the property market, our Stable outlook reflects the Group's diversity of business line and expectation of relatively stable credit metrics.
- According to management accounts, Stockwell recorded EBITDA of AUD9.9m in FY18 which compares favourably to our forecast of AUD7.0m. Further, gearing was slightly better than expected at 66.6%, compared to our forecast of 71% (total debt to total tangible assets) – due to lower debt and higher tangible assets.
- In terms of Stockwell's higher risk developments ('Muse' and Boggo Rd - mainly investor stock in inner city Brisbane), remaining units continue to be sold down at around three to four a month. As at August 2018, 12 units were unsold at Boggo Road (out of 75) and 16 were unsold at 'Muse' (out of 116). Project specific debt has previously been repaid for these projects. Stockwell is comfortable selling the remainder at the current rate, and is not in a position where it wants or needs to reduce prices or increase commissions to clear the stock. Residual risks from these projects are therefore considered minimal.
- Stockwell's other two inner Brisbane residential projects, riverfront high to premium owner occupied stock (a market which is still buoyant and generally unaffected by oversupply), are selling well with 64 sold at 'Virtuoso' (out of 77) and 33 sold at 'Encore' (out of 60). These projects are currently under construction. Given the nature of the projects, sales to date and target market, we currently have limited concerns regarding sales or settlement risks.
- Management has provided initial FY19 guidance of AUD10-12m of EBITDA, however we will update our forecasts once it provides a finalised budget, along with full FY18 accounts.

13 September 2018

Recommendation

Outperform

AUD30m 7.75% June 2021

Credit Outlook

Stable

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Key Financials (AUDm)

FYE (30 Jun)	16	17	18M	19F
Revenue	23.0	117.4	80.6	64.9
EBITDA	5.1	10.6	9.9	6.8
Net Debt	233.8	219.4	179.7	166.5
Total Debt/TTA	75%	71%	66.6%	68%

Source: FIIG Securities

Note: TTA denotes Total Tangible Assets, M denotes management accounts. F denotes a FIIG Securities forecast.

Relative value

Issuer	Des.	Fixed/ FRN	Size (AUDm)	Coupon	Maturity	Mid- Price	YTW	YTW Date	Next Call Price	Next Call Date	Recom.
W.A Stockwell	Sen sec	Fixed	30.0	7.75%	29 Jun 21	101.85	7.08%	29 Jun 21	103.0	29 Jun 19	O/P

Source: FIIG Securities, Bloomberg

Note: Indicative prices as of 6 September 2018

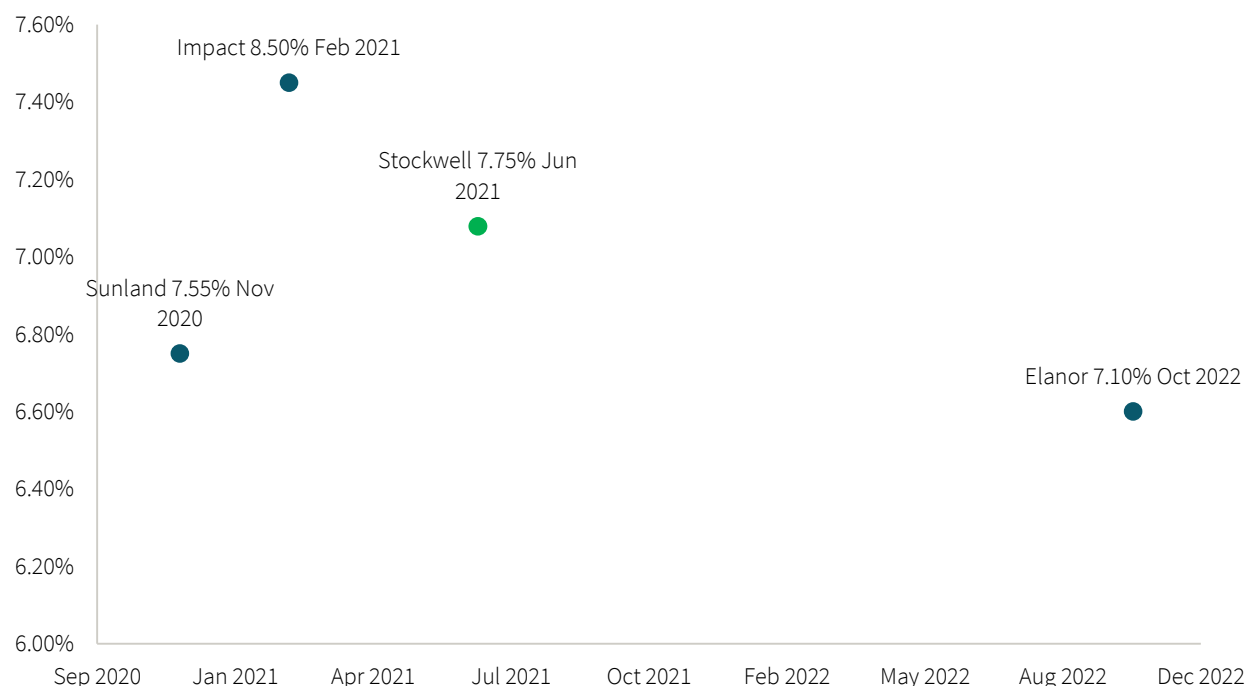
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Relative value

We have an Outperform recommendation on Stockwell's 7.25% Notes due 2021 at the current indicative mid-price of 101.85 and yield to worst of 7.08%. We believe Stockwell will outperform its peers over the next 12 months given its higher yield. While broadly there is weakness in the property market, we currently see limited potential risks in Stockwell's current four inner Brisbane unit developments. Further the Group is diversified and does not solely rely on development income. Earnings are underpinned by stable commercial property investment income and growing property and funds management businesses.

Figure 1: Relative value



Source: FIIG Securities, Bloomberg

Note: Indicative prices as of 6 September 2018

FY18 management results

Stockwell has provided summary FY18 management accounts and a trading update. Full audited accounts will be available towards the end of October. Given the limited details available, we will update our model and forecast at that time. Figure 2 compares FY18 management accounts (FY18M) to our FY18 forecast (FY18F).

According to management accounts, Stockwell recorded EBITDA of AUD9.9m in FY18 which compares favourably to our forecast of AUD7.0m. Further, gearing was slightly better than expected at 66.6%, compared to our forecast of 70% (total debt to total tangible assets) – due to lower debt and higher tangible assets.

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Figure 2: FY18 management accounts compared to FIIG forecasts

P&L summary (AUDm)	FY18M	FY18F	Difference
Total revenue	80.6	87.4	(6.8)
EBITDA	9.9	7.0	2.9
EBIT	7.9	5.1	2.8
Balance sheet (AUDm)	FY18M	FY18F	Difference
Cash	4.4	2.1	2.3
Total debt	184.1	200.5	(16.4)
Net debt	179.7	198.4	(18.7)
Total tangible assets (TTA)	276.6	285.3	(8.7)
Net tangible assets	71.2	65.0	6.2
Credit statistics	FY18M	FY18F	Difference
Total debt/TTA	66.6%	70.3%	3.7ppt
Covenant: Total debt/TTA	75%	75%	

Source: FIIG Securities, Company reports

Notes: M denotes management accounts. F denotes a FIIG Securities forecast

Operational update

In terms of Stockwell's higher risk developments ('Muse' and Boggo Rd stage two - mainly investor stock in inner city Brisbane), practical completion was reached in August 2017 and September 2017 respectively. As at August 2018, 12 units were unsold at Boggo Road (out of 75) and 16 were unsold at 'Muse' (out of 116). Stockwell is comfortable selling the remainder down at the current rate, and is not in a position where it wants or needs to reduce prices or increase commissions to clear the stock. Residual units continue to be sold down at around three to four a month. All project specific debt for 'Muse' and Boggo Road has been repaid. Remaining risks from these projects are therefore considered limited.

Unlike the investor offering at 'Muse' and Boggo Road, Stockwell's other two inner Brisbane residential projects target the owner occupier market with larger floor plans and better fitouts. In Brisbane, this market is still buoyant and generally unaffected by oversupply. These projects are currently under construction with forecast completion in early 2019 for 'Virtuoso' and in late 2019 for 'Encore'. Sales are solid with 64 sold at 'Virtuoso' (out of 77) and 33 sold at 'Encore' (out of 60) as at August 2018. Given the nature of the projects, sales to date and target market, we have limited concerns regarding sales or settlement risks.

Stockwell has provided the following commentary regarding its activities

'Solana Lifestyle Resort – Bribie Island: First homes and civil works, including construction of underground infrastructure and roads, were completed during the quarter. The Resort was officially opened in June, followed closely by settlement of the first homes and residents moving in. The Resort will ultimately comprise up to 200 homes, delivered over six stages.

'Encore' – 50 Ferry Road, West End: Construction of our premium owner-occupier project, Encore, commenced in May with completion due in the first half of the 2020 financial year. The sales campaign continues to progress well.

'Virtuoso' – West End: Construction and selling continued throughout the quarter. By the end of June, the sixth out of seven floor slabs had been poured. Forecast completion in early 2019 remains unchanged since previous reports, and to date over \$100m in sales have been achieved.

Muse and Boggo Road: The current marketing strategy continues to generate sales at a pleasing rate in what is a very competitive environment. Only a small number of apartments in the Muse and Boggo Road projects remain unsold, and finalisation of these projects is expected in the 2019 financial year.

Future retail development: During the quarter, contracts were exchanged for the purchase of a DA-approved neighbourhood shopping centre site. Development of the centre will commence in late 2018, with contribution to financial results commencing from the 2019 financial year. Further detail will be available in the coming quarter, following settlement of the site.

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Shopping Centres and Stockwell Property Management: *Our existing retail assets continue to trade robustly, owing largely to their limited reliance on discretionary spending. Our focus is on carefully managing and quickly filling any vacancies, and monitoring performance of our tenants so as to ensure the health of each centre.*

Stockwell Residential Management: *The residential property management business continues to perform well. In what is a competitive rental market we have maintained very low rates of vacancy in the properties we manage, while actively working to grow sources of revenue for the business. The business model is under constant review to ensure it is operating as efficiently as possible while maintaining the best service for our clients, and we continue to see enhanced returns as a result."*

Company background

W.A. Stockwell Pty Ltd (WAS) is the parent company of the Stockwell Group, a Queensland based diversified property group with over 60 years' experience in property development, property investment and design and construction across the residential, retail and commercial property sectors.

WAS is owned 50/50 by Mark Stockwell and Michael Kelso, who are the two Directors of WAS and acquired the business in 1994 from Mark's parents. Both have over 25 years of experience in the Queensland property market. The Stockwell Group employs approximately 50 people, with the majority of construction work outsourced to design and construction contractors under fixed-price, fixed-time construction contracts.

The Stockwell Group comprises three business divisions:

1. Property investments: Retail investment properties, which provide recurring revenues to the Group.
2. Property development projects: Acts as landowner, developer, joint venture partner and if required, builder.
3. Operations: Development management (from acquisition to sales and delivery), funds management, and property management across the residential, retail and commercial sectors.

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