

# Quickstep Holdings Limited

## 2Q FY19 quarter update

QHL's update for the December 2018 quarter was, in our view, a bit of a mixed bag. While total sales of A\$15.8m was up (only) a modest 3% on the pcp, quarterly customer receipts were boosted by delayed September quarter customer payments; as a result, customer receipts in the December quarter hit an historical high of A\$18.1m.

Sales were adversely impacted by extended outage of a key machine (PMM) and limited industrial action during the quarter. Production delays from the equipment outage resulted in a A\$3.3m inventory increase (largely raw materials), negatively impacting cash flows. While this inventory is expected to normalise during the second half of FY19 on increased production, management has indicated that the machine outage is likely to impact March 2019 quarter sales. Importantly, however, QHL maintains its guidance of full year revenue growth of +20%, and positive operating cash flow for the full year.

While management states that cost cutting initiatives across all functions at the group's Bankstown and Geelong sites helped increase gross margins in the quarter, we note that admin & corporate costs increased to A\$1.67m in the December quarter from A\$770,000 in the September quarter. We believe this increase stemmed from bonus payments and new business development expenses.

QHL paid down A\$1m in debt during the quarter, reducing the outstanding debt balance (including capitalised interest) to A\$15.5m as at 31 Dec 2018. We imagine that a key challenge for management over the second half of FY19 will be balancing working capital and investment requirements with the group's capital structure. A further A\$1.7m of long-term loans is scheduled for repayment by the end of June 2019, while we believe QHL will be looking to extend its Efic working capital facility (A\$7m) beyond the current draw-down date of 28 June 2019.

### .....two strong positives

During the quarter QHL received A\$1.9m in government funding for the **Chemring flare housing project**, completed the design of the flare housing production process and is currently procuring equipment to establish a cutting-edge focused manufacturing cell. We believe the project will require a further A\$1m in capex with QHL targeting for production to commence in the June 2020 quarter.

QHL has a clear focus on the US market (defence and commercial aerospace segments). Management states that it has a healthy pipeline of new potential business opportunities, and importantly, states that "based on the progress of confidential negotiations (in the US), we anticipate significant **new business awards during FY19**". Announcements over the next few months of material new business contracts could act as significant near-term share price catalysts.

We believe QHL offers significant upside potential relative to our NPV/EPS-derived target price of 15c (unchanged). **Recommendation: Buy (High Risk)**. Risks to our target price and earnings profile include but are not limited to:

- operational performance at the Bankstown manufacturing site,
- JSF parts sales profile (dependent on order timing), timing and quantum of new aerospace business, and the AUD:USD exchange rate,
- timing and quantum of the debt repayment profile & potential refinancing,
- capex and working capital requirements to support increased production and potential new business, key personnel/management risk.

31 January 2019

Share price: A\$0.07

Target price: A\$0.15 (unchanged)

**Target upside: 111%**

Recommendation  
**Buy**

Risk Assessment  
**Higher**

#### Industrial

David Brennan, CFA

Senior Investment Analyst

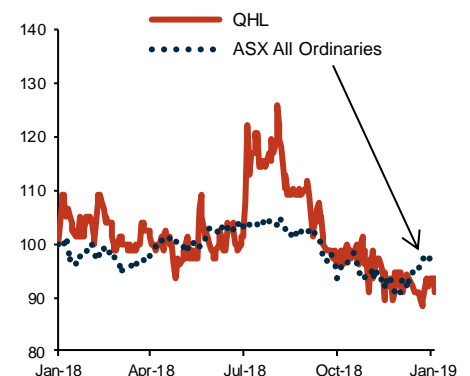
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#### Quickstep Holdings Limited

ASX Code	QHL
52 week range	A\$0.07-A\$0.11
Market Cap (A\$m)	41
Quoted shares (m)	564
Av Daily Turnover (shares)	330k
ASX All Ordinaries	5,874
FY19E BV per share (A\$c)	1.2
EPS FY19E (A\$c)	0.2
Net (Debt)/Cash FY19E (A\$m)	-11

#### Relative price performance



## Financial Statements

Year ending June

Profit & Loss Statement (A\$m)	FY18A	FY19E	FY20E	FY21E	FY22E
<b>Sales</b>	<b>59.0</b>	<b>71.1</b>	<b>103.3</b>	<b>124.3</b>	<b>124.3</b>
COGS	(46.7)	(56.1)	(80.6)	(95.7)	(95.7)
Operational/Marketing/Corporate	(7.4)	(7.5)	(7.7)	(7.8)	(8.0)
R&D	(3.7)	(4.0)	(4.0)	(4.0)	(4.0)
Total cash costs	(57.9)	(67.6)	(92.2)	(107.5)	(107.6)
<b>EBITDA</b>	<b>1.2</b>	<b>3.4</b>	<b>11.1</b>	<b>16.8</b>	<b>16.6</b>
Depreciation & Amortisation	(3.0)	(3.0)	(3.0)	(3.0)	(3.0)
<b>Operating profit</b>	<b>(1.8)</b>	<b>0.4</b>	<b>8.1</b>	<b>13.8</b>	<b>13.6</b>
NOI (Grants/Other)	(0.2)	1.9	0.5	0.5	0.5
<b>EBIT</b>	<b>(2.0)</b>	<b>2.3</b>	<b>8.6</b>	<b>14.3</b>	<b>14.1</b>
Interest income	0.2	0.1	0.1	0.0	0.1
Interest expense	(1.1)	(1.1)	(1.0)	(0.6)	(0.2)
Tax expense	0.0	0.0	0.0	0.0	0.0
<b>Reported NPAT</b>	<b>(2.9)</b>	<b>1.3</b>	<b>7.7</b>	<b>13.7</b>	<b>14.0</b>
Exceptional items	0.0	0.0	0.0	0.0	0.0
<b>Underlying NPAT</b>	<b>(2.9)</b>	<b>1.3</b>	<b>7.7</b>	<b>13.7</b>	<b>14.0</b>
EPS Reported (A\$c)	(0.5)	0.2	1.3	2.4	2.4
EPS Normalised (A\$c)	(0.5)	0.2	1.3	2.4	2.4
Dividend payout (%)	na	0%	0%	0%	20%
DPS (A\$c)	0.0	0.0	0.0	0.0	0.5
Dividend Yield (%)	0%	0%	0%	0%	7%
Number of shares - diluted (m)	580	580	580	580	580

Cash Flow Statement (A\$m)	FY18A	FY19E	FY20E	FY21E	FY22E
EBITDA	1.2	3.4	11.1	16.8	16.6
Investment in working capital	(1.0)	(1.2)	(3.1)	(2.0)	0.0
Tax expense	0.0	0.0	0.0	0.0	0.0
<b>Operating Cash Flow</b>	<b>0.2</b>	<b>2.2</b>	<b>8.0</b>	<b>14.8</b>	<b>16.6</b>
Capex	(1.1)	(3.0)	(5.0)	(7.5)	(3.0)
Other investments	0.0	0.0	0.0	0.0	0.0
<b>Investing Cash Flow</b>	<b>(1.1)</b>	<b>(3.0)</b>	<b>(5.0)</b>	<b>(7.5)</b>	<b>(3.0)</b>
Net interest received / (paid)	(0.9)	(1.0)	(0.9)	(0.6)	(0.1)
Debt increase / (repayment)	1.6	0.0	(3.0)	(5.2)	(5.4)
Dividends declared	0.0	0.0	0.0	0.0	(2.8)
Equity raised / (repaid)	0.5	0.0	0.0	0.0	0.0
<b>Financing Cash Flow</b>	<b>1.1</b>	<b>(1.0)</b>	<b>(3.9)</b>	<b>(5.7)</b>	<b>(8.3)</b>
Non-operating & Other	(1.0)	1.9	0.5	0.5	0.5
<b>Inc/(Dec) in Cash</b>	<b>(0.8)</b>	<b>0.0</b>	<b>(0.4)</b>	<b>2.0</b>	<b>5.8</b>

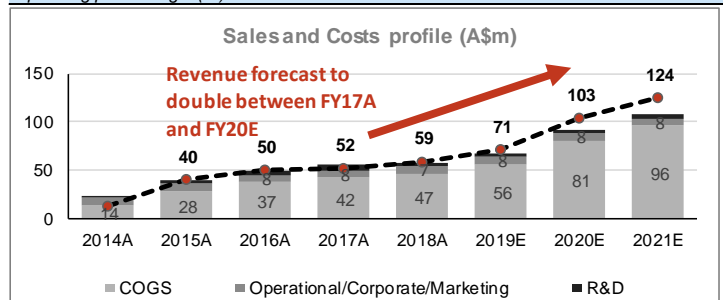
Balance Sheet (A\$m)	FY18A	FY19E	FY20E	FY21E	FY22E
Cash & Deposits	2.9	2.9	2.5	4.5	10.3
Receivables	4.5	5.3	7.7	9.3	9.3
Inventories	10.0	12.1	17.6	21.1	21.1
Other Current Assets	1.6	1.6	1.6	1.6	1.6
PPE and Exploration & Development	13.2	13.2	15.2	19.7	19.7
Deferred tax asset	0.0	0.0	0.0	0.0	0.0
Other Non Current Assets	0.0	0.0	0.0	0.0	0.0
<b>Total Assets</b>	<b>32.2</b>	<b>35.1</b>	<b>44.7</b>	<b>56.3</b>	<b>62.1</b>
Payables and other current Liabilities	12.5	14.2	19.1	22.2	22.2
Short Term Debt	5.7	5.7	1.7	0.0	0.0
Long Term Debt	7.9	7.9	8.9	5.4	0.0
Other Non Current Liabilities	0.3	0.3	0.3	0.3	0.3
<b>Total Liabilities</b>	<b>26.4</b>	<b>28.1</b>	<b>29.9</b>	<b>27.9</b>	<b>22.5</b>
<b>Total Equity</b>	<b>5.8</b>	<b>7.0</b>	<b>14.7</b>	<b>28.4</b>	<b>39.6</b>
Net (Debt)/Cash	(10.7)	(10.7)	(8.1)	(0.9)	10.3

Major Shareholders	%	Date
Washington H Soul Pattinson	15.9	
Deakin University	5.9	Jul-18
State One Stockbroking	2.9	

Source: Company, IRESS, State One Stockbroking forecasts

Performance drivers	FY18A	FY19E	FY20E	FY21E	FY22E
<b>Parts sold / delivered</b>					
C-130J/LM-100J shipsets	24	24	26	28	28
F-35 JSF parts	1,500	2,105	2,650	2,720	2,720
... JSF fuselage	1,040	1,250	1,580	1,640	1,640
... JSF VTF	460	855	1,070	1,080	1,080
<b>Revenue composition (A\$m)</b>					
Aerospace - existing contracts	57.3	68.1	84.0	87.3	87.3
C-130J/LM-100J	19.4	17.3	18.7	20.2	20.2
F-35 JSF	37.9	50.8	65.3	67.2	67.2
... JSF fuselage	29.4	35.0	45.3	47.0	47.0
... JSF VTF	8.5	15.8	20.0	20.2	20.2
Aerospace - new business	0.0	1.3	12.0	24.0	24.0
<b>Total Aerospace (Bankstown)</b>	<b>57.3</b>	<b>69.5</b>	<b>96.0</b>	<b>111.3</b>	<b>111.3</b>
Automotive	0.4	0.0	2.9	7.3	7.3
X-Ray	1.3	1.6	2.4	3.6	3.6
Engineering/Other	0.0	0.0	2.0	2.0	2.0
<b>Non-Aerospace (Geelong)</b>	<b>1.7</b>	<b>1.6</b>	<b>7.3</b>	<b>12.9</b>	<b>12.9</b>
<b>Group revenue (A\$m)</b>	<b>59.0</b>	<b>71.1</b>	<b>103.3</b>	<b>124.3</b>	<b>124.3</b>
YoY revenue growth	14%	20%	45%	20%	0%
COGS as % revenue	79%	79%	78%	77%	77%
Operations/Other costs as % revenue	13%	11%	7%	6%	6%
R&D as % revenue	6%	6%	4%	3%	3%
Total costs as % revenue	98%	95%	89%	86%	87%

EBITDA margin (%)	2%	5%	11%	14%	13%
Operating profit margin (%)	-ve	1%	8%	11%	11%



Leverage	FY18A	FY19E	FY20E	FY21E	FY22E
Net Debt/Equity	-185%	-152%	-55%	-3%	cash
Net Debt/Total Assets	-33%	-30%	-18%	-2%	cash
Net interest Cover (x)	na	2.2	9	24	na

Valuation Ratios (x)	FY18A	FY19E	FY20E	FY21E	FY22E
Normalised PER	-ve	32.7	5.4	3.0	2.9
Price/OP Cash Flow	224.9	18.9	5.1	2.8	2.5
EV (A\$m)	51	51	49	41	30
EV/EBITDA	44	15	4	2	2
ROE (%)	na	18%	52%	48%	35%

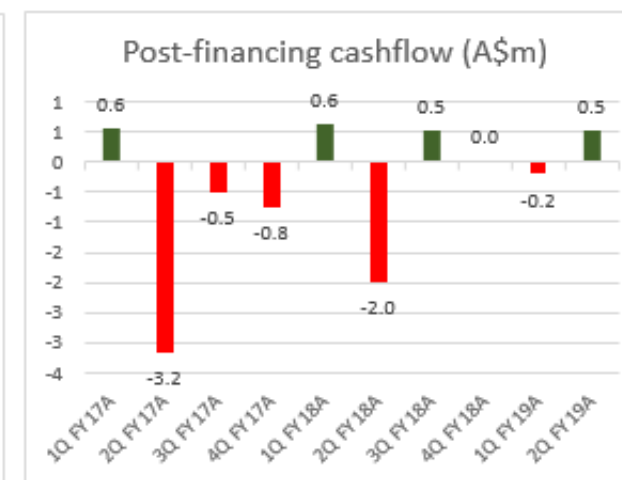
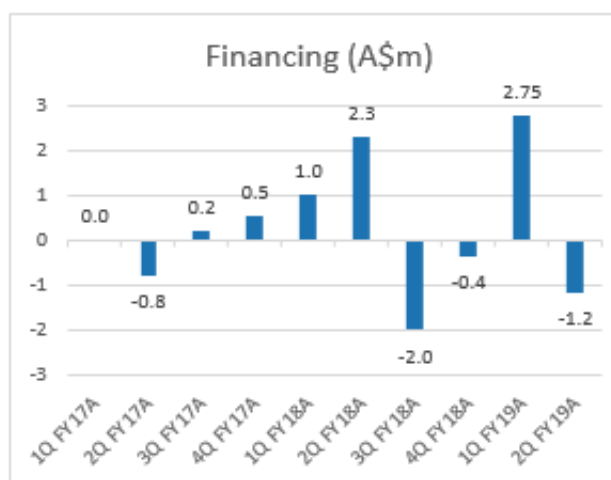
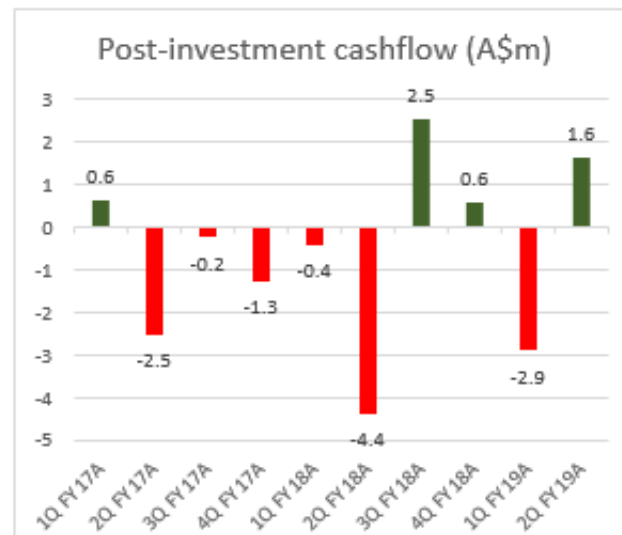
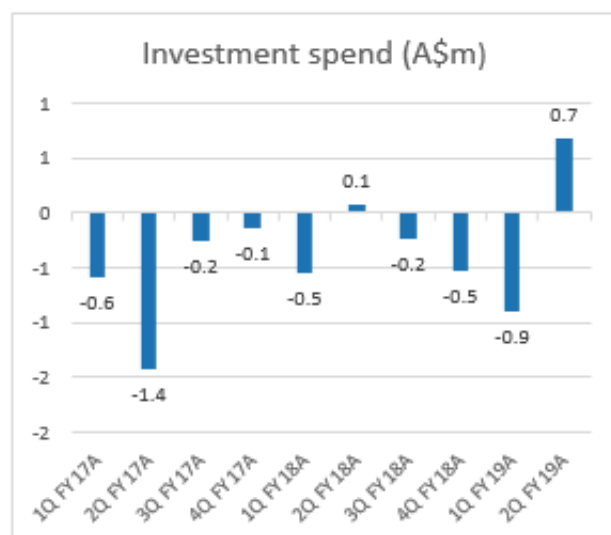
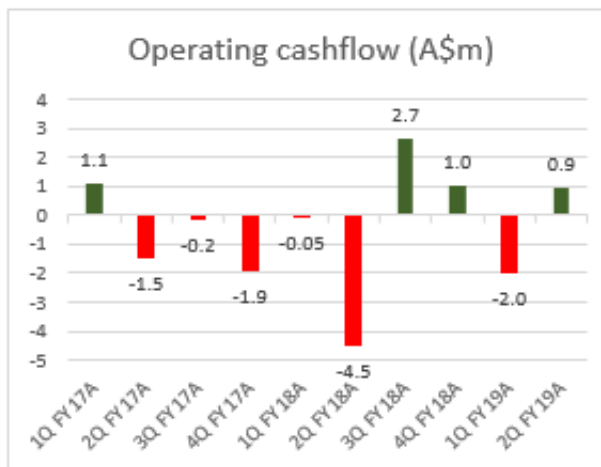
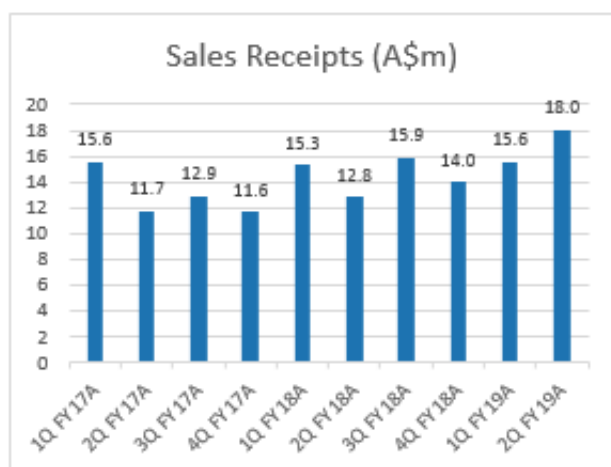
### Weighted Target Price

Valuation method	Target value (A\$)	Weighting (%)	Share price (A\$)		Capital gain (%)
			Target	Current	
Base-case NPV	0.15	50%	0.14	0.071	111%
Base-case EPS/PER	0.14	50%			
"Blue sky" @ 10% of base-case valuation			0.01		
<b>Target Price (A\$)</b>			<b>0.15</b>		

EPS/PER TP based on two-year rolling EPS of A\$1.6c (rounded) and a PE multiple of 8x

**Company Overview:** Quickstep (QHL) is the largest independent aerospace-grade advanced composite manufacturer in Australia. QHL is the sole provider of carbon fibre wing flap parts for the Lockheed Martin C-130J and LM-100J transport planes, and is a parts supplier to Northrop Grumman and BAE/Marand for the JSF F-35.

## Quarterly performance 1QFY17- 2QFY19



Source: Company, compiled by State One Stockbroking

Note: Positive investment spend of A\$0.7m in 2Q FY19 due to A\$1.86m government funding for Chemring project

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