Transurban

ASX:TCL

BUY: S$15.70 (+7.00%)

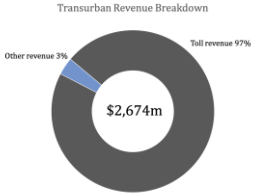
Near-monopoly forging ahead

25th October 2019

NUS INVESTMENT SOCIETY

Company Overview

Figure 1. Transurban revenue breakdown by type



Upcoming Project	Expected completion
395 Express Lanes	late-2019
NorthConnex	2020
New M5 and M5 East (WCX Stage 2)	2020
West Gate Tunnel	2023
Fredericksburg Extension	2023

Transurban is a road operator company that operates toll road networks primarily in Australia. The main source of revenue for Transurban is from tolls, which contributed 96.52% of revenues in 2019. Transurban operates 17 toll roads across Sydney, Melbourne, and Brisbane, Australia, as well as in the Greater Washington Area and Montreal. They currently have eight projects in the pipeline.

(S$ M)	FY18A	FY19A	FY20E	FY21E
Revenue	2,396	2,722	3,071	3,304
Gr Rate (%)	8.71%	13.61%	12.82%	7.59%
Adj. EBITDA	1,775	2,018	2,336	2,515
Margin (%)	74.08%	74.14%	76.07%	76.12%
Adj. Net Income	529	103	124	237
Margin (%)	22.08%	3.78%	4.04%	7.17%
DPS	0.56	0.59	0.62	0.65
Dividend yield	4.0%	4.2%	4.4%	4.6%
Gearing	2.1	1.7	2.3	2.9

12M Industry Outlook

Figure 2: Australian population estimates

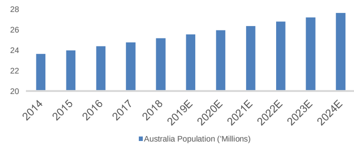
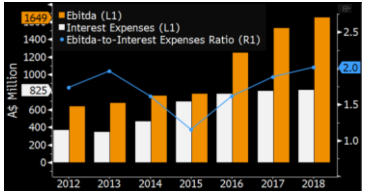


Figure 3: EBITDA against interest expense

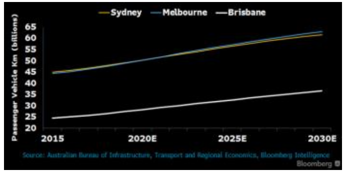


1. **Demand.** Traffic volume underpinned by strong growth in population. Net migration is expected to grow by 250,000 annually with Sydney's population is expected to grow by 90,000 per annum. Passenger vehicle-kilometre growth in 2015-30 could rise 37% in Sydney, 42% in Melbourne and 50% in Brisbane, according to Australia's Bureau of Infrastructure, Transport and Regional Economics
2. **Toll relief** from NSW government expected to increase traffic volume on toll roads. Toll relief provides one free 12-month registration to owners of privately-registered vehicles who have spent $1300 or more on tolls in the previous financial year, or a half-price registration if owners spend $780 or more. An estimated 300,000 are estimated to benefit from this program.
3. **Risk** from interest rate hikes could impact Transurban's ability to refinance its debt, which as of FY19 stands at $19.4bn, representing more than twice its equity. A rise of 100bps in interest rate could affect their post-tax profit by 9.4%. Rising interest rates would also impair the company's ability to raise funds for new infrastructure projects.

Investment Thesis

Figure 4: Future Projects Pipeline

Figure 5: Traffic volume projections



1. **Strong network effect from near monopoly**. Transurban owns 15 out of 19 toll roads in Australia. They are strategically positioned in key routes of major Australian cities (especially Sydney), forming a web around the city centre.
2. **Price Hikes & average daily traffic growth (ADT)**. Transurban is allowed to increase prices by 1% or inflation annually whichever higher, 4 out of 14 of their owned toll roads(~50% of revenue) are able to increase by 4% annually. 80% of revenue are inflation-linked. ADT grew by 2% and should be underpinned by population growth.
3. **Long pipeline of assets**. 3 new project openings in FY20 to further bolster growth with a further 7 projects to open from FY21-25. This is in addition to the 4 Australian projects opened & the acquisition of the M5 tunnel in FY19, which was value & FCF accretive. The upcoming projects further compounds their network effect.

Valuations

Figure 6: Football field

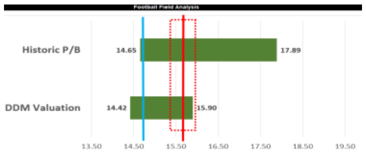


Figure 7: Historic P/B with lookback period of 3Y

We blended a DDM and historic P/B valuation to obtain a target price of $15.70, with 7% upside potential given current price of $14.71

DDM valuation: With Cost of Equity of 6.50% and dividend growth rate pegged to Australia's long-term growth rate of 2.4%

This valuation method gave us a sensitized price range of $14.42 to $15.90 when we fix the Cost of Equity and vary Australia's long-term growth rate.

Historic P/B ratio was used as a secondary valuation method with a lookback period of 3Y. The price range of $14.65 to $17.89 was obtained. We expect reversion to the mean of 4.97x

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