John Laing Group

Interims

Reset and refocus

Investment companies

COVID-19 and a further cut to power price assumptions saw NAV per share fall to 309p in H120 (FY19: 337p). However, PPP performed well, bidding momentum has picked up recently and John Laing Group (JLG) expects 'modest' NAV growth in H2. New CEO Ben Loomes highlighted digital connectivity and energy transitions as potential future investment themes, and will set out further details in November. We cut our FY20 NAV per share forecast by 14% to 308p. The share price stands at an 8% discount to FY20e NAV per share.

Year end	NAV/share (p)	EPS* (p)	DPS (p)	P/NAV (x)	P/E (x)	Yield (%)
12/18	323	63.1	9.5	0.9	4.5	3.3
12/19	337	20.4	9.5	0.8	13.9	3.4
12/20e	308	(14.6)	8.2	0.9	N/A	2.9
12/21e	315	5.9	9.8	0.9	48.3	3.5

Note: *EPS are normalised, excluding amortisation of acquired intangibles, exceptional items and share-based payments.

H1: PPP solid but offset by renewables and COVID-19

The 8% fall in NAV in H1 to 309p was 6% pre-dividend and would have been 10% without an FX tailwind. PPP (74% of total PV) made a 3% positive contribution to NAV, but renewables (26%) was affected by a further cut to long-term power price assumptions and transmission issues in Australia (-16p). COVID-19 had a relatively modest direct impact (-4p) but prompted a reduction to short-term macro assumptions (-8p) and reduced value enhancements (just +3p vs +16p in H119).

Portfolio development slows but pipeline intact

Operational performance during the period was robust without any continuity issues and short delays to only two construction projects. Understandably, procurement processes were affected by COVID-19, reducing JLG's investment activity to just £2m. However, the pipeline remains intact. The company has seen no project cancellations and bidding activity has picked up since June. Disposal activity held up better (£88m vs £137m in H119), with the company selling five assets (four in renewables) and proceeds in line with book value.

Forecast: Cutting FY20e NAV per share to 308p

JLG guides to a modest rise in underlying NAV/share in H2 vs H1. We model a 9p increase, but assume it will be offset by FX (-8p) and reduced a further 2p by the interim dividend. Our FY20 NAV/share is 308p (-14% vs March estimate). Forecasting FY21 is tougher in the current macro climate, but management believes valuations are now conservative, and the yield on secondary PPP should prove resilient in a downturn and attractive to potential buyers. We estimate an NAV/share of 315p (a 20% cut) based on a 17p a lift in asset value and a 9.8p dividend.

Valuation: 8% discount to NAV per share

At 284p, JLG trades at an 8% discount to FY20e NAV/share and close to the bottom of its historical range. Yet its core PPP portfolio continues to generate value and, with renewable valuations reset and exposure falling, the worst could be behind it. We expect CEO Ben Loomes to set out the details of a new strategy addressing both digital connectivity and energy transition themes in November. Both areas look set to benefit from a substantial boost in infrastructure spending.

26 August 2020

Price	**284p**
Market cap	**£1,400m**

Net debt (£m) at H120	£105m (re-presented accounts), £431m (Edison calculation based on statutory accounts)
Shares in issue	493m
Free float	99%
Code	JLG
Primary exchange	LSE
Secondary exchange	N/A

Share price performance

%	1m	3m	12m
Abs	(7.9)	(19.3)	(20.1)
Rel (local)	(7.2)	(20.9)	(7.5)
52-week high/low		401p	280p

Business description

John Laing Group is an originator, active investor in, and manager of greenfield infrastructure projects. It operates internationally and its business is focused on the transport energy, social and environmental sectors.

Next events

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H120: Contrasting performance

PPP opportunity remains, momentum has picked up since June

JLG remains confident in the long-term opportunity in its core PPP (Public Private Partnerships) business (74% of Portfolio Value). These assets performed well in H1, contributing a 3% growth to NAV (1% in constant currency) despite a downward adjustment to near-term inflation assumptions prompted by COVID-19. Operational performance in key projects was robust, with no impact on continuity for availability assets, delivery of key projects largely on track and volume-related activities (13% of PPP PV) recovering following the extreme falls in traffic seen during the early phases of lockdown.

COVID-19 has resulted in delays in the bidding process. JLG invested just £2m in H120 and expects minimal investment activity in H2. However, it has seen no project cancellations and activity levels have picked up since June. It has added three new short-listed projects in the US (an express lanes project in Georgia and the I-495 investment programme in Maryland, and one further unnamed project) and is a preferred bidder on the ViA15 road project in the Netherlands. The combined pipeline of preferred and short-listed deals for JLG rose by £129m in H1 from £443m to £572m. While the PPP opportunity in the UK and Europe is mature, JLG sees significant growth opportunities in Australia and North America. Since IPO, average realisations in PPP have exceeded the original investment by more than three times.

The company is currently in discussions to sell its IEP East project, which could modestly boost NAV in H2. In addition, it believes the yield of its secondary PPP should prove both relatively resilient to an economic downturn and attractive to potential buyers in a low inflation environment.

Offset by renewables

As highlighted in the trading statement, renewable performance was weak in H1. The combination of specific project performance issues in solar and biomass (-16p), a further cut to long-term power price assumptions (-14p) and transmission issues (-2p) resulted in a 29p (-7%; -9% in constant currency) reduction to NAV per share. The reduction to valuation predominantly affected assets with short PPAs (Purchase Price Agreements) that are therefore more exposed to merchant power prices in the long term. JLG disposed of £70m of renewable assets in H1 at prices marginally ahead of book value. The combination of the decision not to invest further in renewables, lower valuations and disposals has seen the value of the renewable portfolio shrink by £190m (31%) in six months. Renewables now account for just 26% of PV, down from 34% in FY19.

Reset and refocus

New CEO Ben Loomes highlighted the themes of digital connectivity and energy transition as additional areas JLG will look to invest in under his tenure. Both are expected to be growing markets. Infrastructure spending will be needed to both accelerate the shift to low carbon and enhance productivity, and cash-strapped governments will be looking to attract private capital to help stimulate the economy post-COVID-19. These are also areas where he has personal investment experience.

Aside from fleshing out the details of the opportunity, the strategic review will aim to establish what resources the company will need to execute on this plan. With a strong reputation for investment in greenfield projects and substantial cash available (net available financial resources of £311m at H1), JLG is well positioned, but building out in these areas will require additional capability. The full outcome of the strategic review is expected in November and we will look to preview some of the issues in a forthcoming note.

Forecast and valuation: Is an 8% discount to NAV sustainable?

JLG is guiding to a 'modest' rise in underlying NAV per share in H2 vs H120. We model a 9p increase (lower than in previous years),but assume this will be largely offset by an 8p adverse move in FX. Both the Australian dollar and US dollar (NAV exposure of 34% and 29%, respectively) have moved against the company since June. Factoring in the 2p interim dividend payment, our FY20 NAV per share of 308p represents a cut of 51p or 14% from our previous forecast (see NAV growth despite challenges). The disposal of IEP East, JLG's largest primary asset (valued at over 5% of total NAV), could deliver modest upside to this figure if achieved.

Forecasting FY21 is more speculative in the current macro climate. The impact of lower asset acquisitions during FY20 is likely to limit growth in value creation, but management believes that its lowered valuations (in renewables particularly) are now conservative and the PPP assets should prove both resilient in an economic downturn and attractive to potential buyers. We forecast a 17p (5%) rise in underlying NAV per share and, factoring in a 9.8p dividend, a reported NAV per share for FY21 of 315p.

On our new forecasts and with the shares at 284p, JLG trades at an 8% discount to our forecast FY20 NAV per share. Historically, JLG's share price has traded between a 25% premium to NAV per share and a 15% discount, so the current valuation is certainly towards the bottom of the range. Given a recent history of relatively weak execution, a discount is potentially understandable, but, between its 2015 IPO and December 2019, JLG delivered 14% compound annual growth in NAV per share (including dividends paid). Increasing investor interest in the new strategy plus further disposals (at or above book value) of its renewable assets could be a catalyst for share price appreciation.

Exhibit 1: Financial summary

Accounts: IFRS, year-end: December, £m	2017	2018	2019	2020e	2021e
Total revenues	196.7	397.0	179.0	6.0	106.3
Cost of sales	0.0	0.0	0.0	0.0	0.0
Gross profit	196.7	397.0	179.0	6.0	106.3
SG&A (expenses)	(58.9)	(66.0)	(68.0)	(65.0)	(66.3)
Other income/(expense)	0.0	(21.0)	0.0	0.0	0.0
Depreciation and amortisation	0.0	0.0	0.0	0.0	0.0
Reported EBIT	137.8	310.0	111.0	(59.0)	40.0
Finance income/(expense)	(11.8)	(14.0)	(11.0)	(13.7)	(10.6)
Other income/(expense)	0.0	0.0	0.0	0.0	0.0
Reported PBT	126.0	296.0	100.0	(72.7)	29.3
Income tax expense (includes exceptionals)	1.5	0.0	0.0	0.0	0.0
Reported net income	127.5	296.0	100.0	(72.7)	29.3
Basic average number of shares, m	367.0	466.9	491.9	493.5	494.4
Adjusted EPS (p)	31.9	63.1	20.4	(14.6)	5.9
EBITDA	137.8	331.0	111.0	(59.0)	40.0
Adjusted NAV (p/share)	281	323	337	308	315
Adjusted Total DPS (p)	8.9	9.5	9.5	8.2	9.8
Balance sheet					
Property, plant and equipment	0.1	0.0	0.0	0.0	0.0
Goodwill	0.0	0.0	0.0	0.0	0.0
Intangible assets	0.0	0.0	0.0	0.0	0.0
Other non-current assets	1,346.9	1,700.0	1,914.0	1,708.8	1,695.6
Total non-current assets	1,347.0	1,700.0	1,914.0	1,708.8	1,695.6
Cash and equivalents	2.5	5.5	2.0	373.0	400.3
Inventories	0.0	0.0	0.0	0.0	0.0
Trade and other receivables	7.6	8.0	6.0	6.0	6.0
Other current assets	0.0	0.0	0.0	0.0	0.0
Total current assets	10.1	14.0	8.0	379.0	406.3
Non-current loans and borrowings	0.0	0.0	4.0	4.0	4.0
Trade and other payables	0.0	0.0	0.0	0.0	0.0
Other non-current liabilities	41.3	42.0	9.0	9.5	9.5
Total non-current liabilities	41.3	42.0	13.0	25.5	13.5
Trade and other payables	17.3	20.0	15.0	15.0	15.0
Current loans and borrowings	173.2	66.0	236.0	515.0	515.0
Other current liabilities	1.4	0.0	0.0	12.0	0.0
Total current liabilities	191.9	86.0	251.0	542.0	530.0
Equity attributable to company	1,123.9	1,586.0	1,658.0	1,520.4	1,558.4
Non-controlling interest	0.0	0.0	0.0	0.0	0.0
Cashflow statement					
Profit before tax	126.0	310.0	111.0	(59.0)	40.0
Net finance expenses	11.8	0.0	0.0	0.0	0.0
Depreciation and amortisation	0.0	0.0	0.0	0.0	0.0
Share based payments	3.0	3.0	4.0	0.0	0.0
Fair value and other adjustments	(189.7)	(369.0)	(174.0)	(22.9)	(120.0)
Movements in working capital	1.6	2.0	(2.0)	0.2	(2.9)
Cash from operations (CFO)	(47.3)	(54.0)	(61.0)	(81.7)	(82.9)
Capex	(0.1)	0.0	0.0	(0.1)	(0.1)
Cash transf. from inv. Held at FV	(1.7)	58.0	74.0	49.1	36.2
Portfolio Investments - Disposals	79.1	(46.0)	(124.0)	190.0	100.0
Cash used in investing activities (CFIA)	77.3	12.0	(50.0)	239.0	136.1
Net proceeds from issue of shares	0.0	210.0	(4.0)	0.0	0.0
Movements in debt	11.0	(106.0)	169.0	279.0	0.0
Other financing activities	(40.1)	(59.0)	(58.0)	(50.1)	(51.6)
Cash from financing activities (CFF)	(29.1)	45.0	107.0	213.8	(25.9)
Currency translation differences and other	0.0	0.0	0.0	0.0	0.0
Increase/(decrease) in cash and equivalents	0.9	3.0	(4.0)	371.0	27.3
Currency translation differences and other	0.0	0.0	0.0	0.0	0.0
Cash and equivalents at end of period	2.5	5.5	2.0	373.0	400.3
Net (debt) cash	(170.7)	(60.0)	(238.0)	(146.0)	(118.7)
Movement in net (debt) cash over period	(10.9)	110.7	(178.0)	92.0	27.3

Source: Company accounts, Edison Investment Research (based on JLG's statutory accounts)

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