BELL POTTER

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Uniti Group (UWL)

Getting off the fence

Recommendation
Buy (Hold)
Price
$3.82
Target (12 months)
$4.50 (unchanged)

GICS Sector

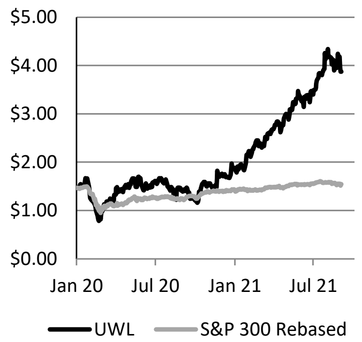
Telecommunication Services

Expected Return	
Capital growth	**17.8%**
Dividend yield	**0.0%**
Total expected return	**17.8%**
Company Data & Ratios	
Enterprise value	**$2,879m**
Market cap	**$2,625m**
Issued capital	**687.3m**
Free float	**90%**
Avg. daily val. (52wk)	**$9.6m**
12 month price range	**$1.155 - $4.39**

Price Performance

	(1m)	(3m)	(12m)
Price (A$)	4.21	3.35	1.41
Absolute (%)	-8.08	15.52	174.47
Rel market (%)	-5.76	15.05	150.86

Absolute Price



SOURCE: IRESS

No change in forecasts

There is no change in our forecasts which we last updated just over a month ago at the release of the FY21 result. We continue to forecast underlying EBITDA of $146.3m in FY22 which equates to strong growth of 56% and is driven by a mix of organic growth and full 12 month contributions from acquisitions completed in 1HFY21 (i.e. Opticomm, Telstra Velocity and Harbour ISP). We then forecast continued strong growth in underlying EBITDA of 16% in FY23 which is all organic (i.e. we assume no more acquisitions in our forecasts). Note we do not forecast any capital management initiatives in our short to medium term forecasts (i.e. dividends or share buybacks) though the company has flagged this is under consideration.

Investment view: $4.50 PT unchanged, Upgrade to BUY

There is similarly no change in our PT of $4.50 given the lack of change in our forecasts and we also only updated it in late August. At this PT the total expected return is >15% so we upgrade our recommendation from HOLD to BUY. (Note the TER includes any forecast dividend yield but, as mentioned, we do not forecast any dividends in FY22 though there is potential for some.) We see the recent pullback in the share price below $4.00 as a buying opportunity given the outlook is unchanged and one reason for the pullback – the charging of director Vaughan Bowen for insider trading – does not in our view have any material impact on the company.

More positives than negatives

In our view the potential positive catalysts for Uniti over the next several months far outweigh the potential negatives from the charging of Vaughan Bowen. The potential catalysts include a strong trading update at the AGM in November, an announcement on capital management, a strong 1HFY22 result in February and perhaps even a takeover offer (given we believe Uniti is a target). The potential negatives are some customers cancel their services – something we believe the company is watching closely but has yet to occur – and some shareholders with a strong ESG bias decide to sell (a lack of industry super funds on the register suggest the risk of this is low).

Earnings Forecast

Year end 30 June	**2021e**	**2022e**	**2023e**	**2024e**
Total revenue (A$m)	160.5	239.0	271.4	306.0
Underlying EBITDA (A$m)	93.7	146.3	169.8	193.8
Underlying NPAT (A$m)	49.3	79.3	96.1	113.9
EPS (diluted) (cps)	7.7	11.2	13.4	15.7
EPS growth (%)	-15%	45%	19%	17%
PER (x)	49.3	34.1	28.5	24.3
Price/CF (x)	28.7	23.0	19.8	17.6
EV/EBITDA (x)	30.7	19.1	16.0	13.6
Dividend (¢ps)	0.0	0.0	1.5	3.5
Yield (%)	0.0%	0.0%	0.4%	0.9%
ROE (%)	6.0%	8.8%	9.5%	10.2%
Franking (%)	0%	0%	100%	100%

SOURCE: BELL POTTER SECURITIES ESTIMATES

Earnings and Valuation Changes

No Change in Forecasts

There is no change in our forecasts which we last updated just over a month ago at the release of the FY21 result. We continue to forecast underlying EBITDA of $146.3m in FY22 which equates to strong growth of 56% and is driven by a mix of organic growth and full 12 month contributions from acquisitions completed in 1HFY21 (i.e. Opticomm, Telstra Velocity and Harbour ISP). We then forecast continued strong growth in underlying EBITDA of 16% in FY23 which is all organic (i.e. we assume no more acquisitions in our forecasts). Note we do not forecast any capital management initiatives in our short to medium term forecasts (i.e. dividends or share buybacks) though the company has flagged this is under consideration.

A summary of our key forecasts is shown below.

Figure 1 - Key forecasts

Year end 30 June	FY22e	*Change*	FY23e	*Change*	FY24e	*Change*
Total revenue (A$m)	239.0	*49%*	271.4	*14%*	306.0	*13%*
Underlying EBITDA	146.3	*56%*	169.8	*16%*	193.8	*14%*
Underlying NPAT	79.3	*61%*	96.1	*21%*	113.9	*18%*
Diluted EPS	**11.2c**	***45%***	**13.4c**	***19%***	**15.7c**	***17%***
DPS	0.0c	*NM*	1.5c	*NM*	3.5c	*NM*

SOURCE: BELL POTTER SECURITIES ESTIMATES

$4.50 PT Unchanged

There is similarly no change in our PT of $4.50 given the lack of change in our forecasts and we also only updated it in late August. We continue to apply the same assumptions of a 20x multiple in the EV/EBITDA valuation and an 8.6% WACC and 5.0% terminal growth rate in the DCF.

Our updated calculation of the PT is shown below.

Figure 2 - PT calculation

	Old (as at 24-Aug-21)			New (as at 1-Oct-21)		
	Valuation per share	% weighting	Price target	Valuation per share	% weighting	Price target
Methodology						
EV/EBITDA	$3.99	50%	$2.00	$3.97	50%	$1.99
DCF	$5.00	50%	$2.50	$5.04	50%	$2.52
Total			**$4.50**			**$4.50**

SOURCE: BELL POTTER SECURITIES ESTIMATES

At our $4.50 PT the total expected return is >15% so we upgrade our recommendation from HOLD to BUY. (Note the TER includes any forecast dividend yield but, as mentioned, we do not forecast any dividends in FY22 though there is potential for some.) We see the recent pullback in the share price below $4.00 as a buying opportunity given the outlook is unchanged and one reason for the pullback – the charging of director Vaughan Bowen for insider trading – does not in our view have any material impact on the company.

Uniti Group

Company Description

Uniti Group (Uniti) is a provider of telecommunications services, specialising in fixed-wireless, fibre and telco services. The objective of the company is to provide an alternative solution to the nbn on a national scale and, by operating at costs lower than accessing the nbn, can deliver products that are competitively priced when compared with products provided by nbn retail service providers.

Investment Thesis

We upgrade our recommendation on Uniti from HOLD to BUY. Our investment thesis is based on:

- **Valuation**: Our 12 month price target on Uniti is $4.50. The price target is generated from a blend of two valuation methodologies we apply to the company: EV/EBITDA and DCF. The price target is an 18% premium to the current share price and the total expected return is the same given there is no forecast dividend.
- **Quality board and management**: In our view Uniti has a high quality senior management team and board of directors with extensive experience in the telecommunications industry. For instance, CEO Michael Simmons has over 30 years' experience in the telecommunications sector and was the CEO of both SP Telemedia and Vocus. Similarly, recently appointed director Vaughan Bowen was the founder of M2 Group which was established over 20 years ago.
- **Good cash flow**: Uniti operates businesses that generate good cash flows and has said it will only target acquisitions which also generate good cash flow. The cash flow will be used to fund both organic growth – mainly through investment in the company's network – and also targeted acquisitions.

Key Risks

Key downside risks to our estimates and valuation include (but are not limited to):

- **Competition risk**: Uniti faces competition from a number of alternative suppliers of broadband internet connectivity services, including resellers of nbn and mobile operators currently delivering 4G cellular services and soon 5G cellular services in these markets. If there is a temporary or permanent shift in the competitive landscape then this could have a negative impact on the financial performance of the company.
- **Supplier risk**: Uniti sources equipment and services from various third parties and a disruption in the supply of, or prices associated with, any of these may have a negative impact on the business.
- **Regulatory risk**: Uniti Wireless uses class license spectrum in the delivery of its services and, in order to do so, is subject to and must comply with laws, regulations and government policies. If changes occur to existing policies and legislation around the use of class licence spectrum – as well as other areas such as declared services – then this could have an adverse impact on the company.

Uniti Group

as at 1 October 2021

Recommendation	Buy
Price	$3.82
Target (12 months)	$4.50

Table 1 - Financial summary

Uniti Group (UWL)

Share price:	$3.82	**Target price:**	$4.50
No. of issued shares:	687.3m	**Market cap:**	$2,625m

Profit & Loss (A$m)					
Year end 30 Jun	**2020**	**2021**	**2022e**	**2023e**	**2024e**
Revenue	**58.2**	**160.5**	**239.0**	**271.4**	**306.0**
Change	*149%*	*176%*	*49%*	*14%*	*13%*
Cost of sales	-13.8	-34.4	-47.8	-54.3	-61.2
Gross profit	**44.4**	**126.1**	**191.2**	**217.1**	**244.8**
Gross margin	*76.2%*	*78.6%*	*80.0%*	*80.0%*	*80.0%*
Expenses (excl. D&A, int.)	**-17.8**	**-32.3**	**-44.9**	**-47.3**	**-51.0**
% of revenue	*-30.7%*	*-20.2%*	*-18.8%*	*-17.4%*	*-16.7%*
EBITDA (underlying)	**26.5**	**93.7**	**146.3**	**169.8**	**193.8**
Depreciation	-4.0	-9.0	-13.5	-14.8	-16.0
Amortisation	-2.9	-12.5	-18.7	-20.6	-22.1
EBIT	**19.7**	**72.3**	**114.1**	**134.4**	**155.7**
Net interest expense	-0.6	-8.0	-8.4	-6.3	-3.9
Pre-tax profit	**19.1**	**64.3**	**105.8**	**128.2**	**151.8**
Income tax expense	7.3	-15.0	-26.4	-32.0	-38.0
NPAT	**26.4**	**49.3**	**79.3**	**96.1**	**113.9**

Cash Flow (A$m)					
Year end 30 Jun	**2020**	**2021**	**2022e**	**2023e**	**2024e**
EBITDA	26.5	93.7	146.3	169.8	193.8
Change in working capital	-4.9	-1.4	-0.3	2.4	2.6
Gross cash flow	**21.6**	**92.4**	**146.0**	**172.3**	**196.4**
Interest received	0.3	0.5	0.0	0.0	0.0
Interest paid	-0.6	-5.6	-2.1	-1.6	-1.0
Tax paid	0.2	-2.6	-26.4	-32.0	-38.0
Operating cash flow	**21.6**	**84.6**	**117.4**	**138.7**	**157.4**
Payments for PPE	-7.5	-26.4	-32.5	-35.0	-37.5
Payments for acquisitions	-165.5	-620.7	-10.0	-25.0	-20.0
Payments for IP	-0.7	-1.2	0.0	0.0	0.0
Investing cash flow	**-176.5**	**-654.9**	**-42.5**	**-60.0**	**-57.5**
Proceeds from loans/grants	0.0	305.6	0.0	0.0	0.0
Proceeds from issue of shares	328.3	179.2	5.0	5.0	5.0
Payment of share issue costs	0.0	0.0	0.0	0.0	0.0
Payment of lease liabilities	-1.0	-1.8	0.0	0.0	0.0
Repayment of loans	-2.5	-44.7	-75.0	-85.0	-100.0
Other financing activities	0.0	0.0	0.0	0.0	0.0
Dividends paid	0.0	0.0	0.0	-3.5	-17.5
Financing cash flows	**324.8**	**438.4**	**-70.0**	**-83.5**	**-112.5**
Net change in cash	**170.0**	**-131.8**	**4.9**	**-4.8**	**-12.5**
Cash at start of period	19.1	189.2	57.3	62.3	57.4
Cash at end of period	**189.2**	**57.3**	**62.3**	**57.4**	**44.9**

Balance Sheet (A$m)					
Year end 30 Jun	**2020**	**2021**	**2022e**	**2023e**	**2024e**
Cash	189.2	57.3	62.3	57.4	44.9
Current receivables	6.0	15.4	23.9	27.1	30.6
Inventories	0.2	0.0	0.0	0.0	0.0
Other current assets	3.1	3.7	3.7	3.7	3.7
PPE	46.5	234.0	255.5	281.9	308.5
Intangibles - Goodwill	176.0	808.6	813.6	826.1	836.1
Intangibles - Other	30.0	81.3	65.1	50.8	33.7
Right of use asset	3.0	3.8	3.8	3.8	3.8
Total assets	**454.1**	**1,205.6**	**1,229.3**	**1,252.4**	**1,262.7**
Payables	13.1	33.7	41.8	47.5	53.6
Current provisions	3.2	2.6	2.6	2.6	2.6
Current int. bearing liabs.	0.0	0.0	0.0	0.0	0.0
Current contract liabs.	2.3	3.6	3.6	3.6	3.6
Current contingent consid.	4.4	9.4	9.4	9.4	9.4
Non-current provisions	0.1	0.5	0.5	0.5	0.5
Non-current int. bearing liabs.	0.0	261.9	186.9	101.9	1.9
Non-current contract liabs.	0.0	0.0	0.0	0.0	0.0
Non-current contingent consid.	2.7	45.3	45.3	45.3	45.3
Total liabilities	**32.4**	**389.8**	**322.9**	**243.6**	**149.6**
Issued capital	421.8	777.9	782.9	787.9	792.9
Reserves	6.1	14.9	21.2	25.9	28.8
Retained earnings/(losses)	-6.2	23.0	102.3	195.0	291.3
Total shareholders' equity	**421.7**	**815.9**	**906.5**	**1,008.8**	**1,113.1**

Valuation data					
Year end 30 Jun	**2020**	**2021**	**2022e**	**2023e**	**2024e**
NPAT (A$m)	26.4	49.3	79.3	96.1	113.9
Diluted EPS (cps)	**9.1**	**7.7**	**11.2**	**13.4**	**15.7**
Change	*NM*	*-15%*	*45%*	*19%*	*17%*
P/E ratio (x)	**41.9**	**49.3**	**34.1**	**28.5**	**24.3**
CFPS (cps)	7.5	13.3	16.6	19.3	21.7
Price/CF (x)	**51.1**	**28.7**	**23.0**	**19.8**	**17.6**
DPS (cps)	0.0	0.0	0.0	1.5	3.5
Yield	**0.0%**	**0.0%**	**0.0%**	**0.4%**	**0.9%**
Franking	0%	0%	0%	100%	100%
EV/Revenue	41.9	17.9	11.7	10.0	8.6
EV/EBITDA (x)	**91.9**	**30.7**	**19.1**	**16.0**	**13.6**
NTA per share (cps)	49.8	-10.9	4.0	18.9	34.7
Price/NTA (x)	**7.7**	**-34.9**	**95.0**	**20.2**	**11.0**

Performance ratios					
Year end 30 Jun	**2020**	**2021**	**2022e**	**2023e**	**2024e**
EBITDA margin	**45.6%**	**58.4%**	**61.2%**	**62.6%**	**63.3%**
Return on assets	5.8%	4.1%	6.5%	7.7%	9.0%
Return on equity	**6.3%**	**6.0%**	**8.8%**	**9.5%**	**10.2%**
Payout ratio	0.0%	0.0%	0.0%	10.8%	21.5%
Effective tax rate	38.3%	-23.4%	25.0%	25.0%	25.0%

Leverage ratios					
Year end 30 Jun	**2020**	**2021**	**2022e**	**2023e**	**2024e**
Net debt/(cash) (A$m)	-187.2	253.3	173.3	93.2	5.7
Net debt/equity	**NM**	**31%**	**19%**	**NM**	**NM**
Gearing	NM	24%	16%	NM	NM
Net debt/EBITDA (x)	NM	2.7	1.2	NM	NM
Net interest cover (x)	33.1	9.1	13.7	21.5	39.8

Segmentals (A$m)					
Year end 30 Jun	**2020**	**2021**	**2022e**	**2023e**	**2024e**
Revenue					
Consumer & Business Enablem	24.0	43.6	54.5	58.6	61.5
Wholesale & Infrastructure	22.4	105.4	171.8	199.0	229.7
Specialty Services	21.0	30.8	34.7	38.1	41.0
Total revenue	67.6	180.9	262.0	296.7	333.2
Intercompany sales	-9.4	-20.5	-23.0	-25.3	-27.2
Consolidated revenue	**58.2**	**160.5**	**239.0**	**271.4**	**306.0**
EBITDA					
Consumer & Business Enablem	4.8	4.5	5.5	5.9	6.2
Wholesale & Infrastructure	14.5	78.6	131.4	154.2	178.0
Specialty Services	11.8	20.0	22.5	23.8	24.6
Unallocated	-4.5	-9.3	-13.1	-14.1	-15.0
Total EBITDA	**26.5**	**93.7**	**146.3**	**169.8**	**193.8**
EBITDA margin					
Consumer & Business Enablem	*19.9%*	*10.2%*	*10.0%*	*10.0%*	*10.0%*
Wholesale & Infrastructure	*65.0%*	*74.5%*	*76.5%*	*77.5%*	*77.5%*
Specialty Services	*56.0%*	*64.8%*	*65.0%*	*62.5%*	*60.0%*
Total EBITDA margin	***39.2%***	***51.8%***	***55.8%***	***57.2%***	***58.2%***

Interims (A$m)				
Year end 30 Jun	**1HFY20**	**2HFY20**	**1HFY21**	**2HFY21**
Revenue	**22.0**	**36.2**	**54.6**	**105.9**
Cost of sales	**-7.5**	**-6.3**	**-12.4**	**-22.0**
Gross profit	**14.6**	**29.8**	**42.2**	**83.9**
Gross margin	*66.0%*	*82.5%*	*77.3%*	*79.2%*
Expenses (excl. D&A, int.)	**-7.4**	**-10.5**	**-12.9**	**-19.4**
EBITDA (underlying)	**7.2**	**19.3**	**29.3**	**64.5**
Depreciation	-2.0	-2.0	-2.9	-6.1
Amortisation	-0.7	-2.2	-3.6	-8.8
EBIT	**4.6**	**15.1**	**22.7**	**49.6**
Net interest expense	-0.3	-0.3	-1.4	-6.6
Pre-tax profit	**4.2**	**14.8**	**21.3**	**43.0**

SOURCE: BELL POTTER SECURITIES ESTIMATES

Recommendation structure

Buy: Expect >15% total return on a 12 month view. For stocks regarded as 'Speculative' a return of >30% is expected.

Hold: Expect total return between -5% and 15% on a 12 month view

Sell: Expect <-5% total return on a 12 month view

Speculative Investments are either start-up enterprises with nil or only prospective operations or recently commenced operations with only forecast cash flows, or companies that have commenced operations or have been in operation for some time but have only forecast cash flows and/or a stressed balance sheet.

Such investments may carry an exceptionally high level of capital risk and volatility of returns.

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