

BUY

HOLD

SELL

European supply de-risks production

We retain a BUY rating with a 12-month price target of \$4.75 p/share. TPI is a licensed producer of licit narcotics. The industry offers attractive fundamentals, including significant barriers to entry (strict licensing requirements) and solid global consumption growth (~6.0% pa). TPI is well positioned as the only truly independent producer, with first mover advantage on mainland Australian poppy production and significant European raw material supply, as well as a cost-effective extraction process developed over the past decade. With TPI having received its Federal Government manufacturing licence, commissioning of the processing facility and first sales from the relocated facility are the key near-term share price catalysts.

Key points

Raw material supply. TPI has entered a three-year agreement for the supply of poppy straw from a European source. The contract stipulates a small quantity of straw in CY15, increasing to a minimum of 1,000t in CY16 and up to 2,000t in CY17, subject to normal industry regulatory approvals. Depending on the alkaloid content, we estimate this would produce 25-40t of NRM in CY17, which represents 27-44% of our CY17 total NRM production forecast of 91t. We understand the landed cost of the straw is comparable with the product TPI sources domestically. TPI also provided a mixed update on the current domestic poppy crop. While Victorian crop inspections have been positive, Tasmanian production is suffering from dry conditions in the south.

Licence granted. TPI recently confirmed that it has received its Australian Federal Government licence to manufacture at its Victorian facility. TPI is currently finalising the installation of the processing plant and equipment and expects commissioning to occur before the end of CY15.

Forecasts. No changes at this stage. While the new European supply contract de-risks TPI's NRM production growth profile, it is likely to have an immaterial impact on the rate of growth in TPI's contracted sales volumes.

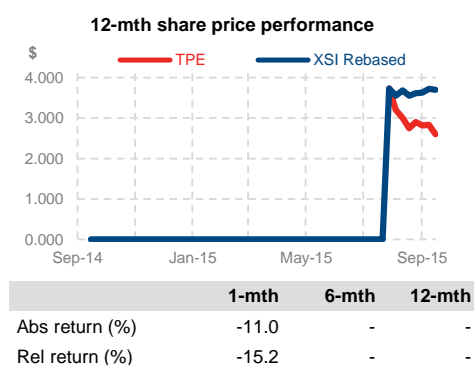
Risks and catalysts

Risks. Reduction in raw material supply; changes to international and/or foreign government conventions; loss of licences; FX movements.

Catalysts. Commissioning of processing plant in Melbourne; ramp-up of NRM production and sales (towards 100t); confirmation of new working capital debt facility; commissioning of API processing capability.

12-mth target price (AUD)	\$4.75
Share price @ 05-Oct-15 (AUD)	\$2.55
Forecast 12-mth capital return	86.3%
Forecast 12-mth dividend yield	0.0%
12-mth total shareholder return	86.3%
Market cap	\$116m
Enterprise value	\$119m
Shares on issue	45m
Sold short	
ASX 300 weight	n/a
Median turnover/day	\$0.1m

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Year-end December (AUD)	FY13A	FY14A	FY15F	FY16F	FY17F
NPAT rep (\$m)	-5.2	-10.7	-10.2	3.9	13.9
NPAT norm (\$m)	-3.7	-5.7	-6.2	3.9	13.9
Consensus NPAT (\$m)			1.0		
EPS norm (cps)		-13.1	-12.6	7.5	27.0
EPS growth (%)			4.0	160.1	258.1
P/E norm (x)		-19.5	-20.3	33.8	9.4
EV/EBITDA (x)	-157.6	-21.6	-22.3	17.7	6.8
FCF yield (%)	0.0	0.0	-18.3	-11.0	3.5
DPS (cps)	0.0	0.0	0.0	0.0	0.0
Dividend yield (%)	0.0	0.0	0.0	0.0	0.0
Franking (%)	0	0	0	0	0

Source: Company data, WHTM estimates, S&P Capital IQ

KEY CHANGES	02-Sep	After	Var %
NPAT: FY15F	-6.2	-6.2	0.0%
norm FY16F	3.9	3.9	0.0%
(\$m) FY17F	13.9	13.9	0.0%
EPS: FY15F	-12.6	-12.6	0.0%
norm FY16F	7.5	7.5	0.0%
(cps) FY17F	27.0	27.0	0.0%
DPS: FY15F	0.0	0.0	0.0%
(cps) FY16F	0.0	0.0	0.0%
FY17F	0.0	0.0	0.0%
Price target:	4.75	4.75	0.0%
Rating:	BUY	BUY	



PRICE TARGET

	Valuation	Price target
WACC post tax (%)	10.5	
PV of FCF forecast (\$m)	169.9	
PV of terminal value (\$m)	152.9	
Enterprise value (\$m)	322.8	
Net debt/(cash) (\$m)	15.7	
Equity value (\$m)	307.1	
Equity value p/sh (\$)	5.97	

Earnings cap (\$)	4.75
FY18 EV/EBITDA (x)	9.5
FY18 PER (x)	10.3

12-mth target (\$) **4.75**

INTERIMS (\$m)

Half-year (AUD)	Jun 14	Dec 14	Jun 15	Dec 15
	1HA	2HA	1HA	2HE
Sales revenue	5.6	1.9	1.1	7.9
EBITDA	0.1	-5.6	-3.6	-1.8
EBIT	-0.6	-6.5	-5.2	-2.7
Net profit	-1.4	-4.4	-5.8	-0.4
Norm EPS	-3.1	-10.0	-12.2	-0.8
EBIT/sales (%)	-11.3	-334.5	-486.6	-33.8
Dividend (c)	0.0	0.0	0.0	0.0
Franking (%)	0.0	0.0	0.0	0.0

FINANCIAL STABILITY

Year-end December	FY14A	FY15F	FY16F
Net debt	17.0	2.9	15.7
Net debt/equity (%)	146.5	8.0	38.7
Net debt/EV (%)	14.3	2.5	13.2
Current ratio (x)	2.0	7.0	2.5
Interest cover (x)	<0	<0	7.3
Adj cash int cover (x)	<0	<0	<0
Debt/cash flow (x)	0.0	<0	<0
Net debt (cash)/share (\$)	0.4	0.1	0.3
NTA/share (\$)	0.3	0.7	0.8
Book value/share (\$)	0.3	0.7	0.8
Payout ratio (%)	0	0	0
Adj payout ratio (%)	0	0	0

EPS RECONCILIATION (\$m)

	FY14A		FY15F	
	Rep	Norm	Rep	Norm
Sales revenue	8	8	9	9
EBIT	-13.5	-7.1	-11.8	-7.9
Net profit	-10.7	-5.7	-10.2	-6.2
Notional earn	0.0	0.0	0.0	0.0
Pref/conv div	0.0	0.0	0.0	0.0
Profit for EPS	-10.7	-5.7	-10.2	-6.2
Diluted shrs (m)	44	44	50	50
Diluted EPS (c)	-24.4	-13.1	-20.5	-12.6

RETURNS

	FY14A	FY15F	FY16F	FY17F
ROE (%)	-98.8	-25.8	10.0	29.3
ROIC (%)	-34.9	-16.1	6.6	17.0
Incremental ROE	-34.9	-2.7	69.7	112.7
Incremental ROIC	-24.4	-2.5	62.5	54.6

KEY ASSUMPTIONS

Year-end December (AUD)	FY13A	FY14A	FY15F	FY16F	FY17F	FY18F
Revenue growth (%)	48.0	-46.2	18.1	266.2	66.6	37.7
EBIT growth (%)	-77.8	231.5	10.1	-157.2	230.4	69.5
EPS growth (%)			-4.0	-160.1	258.1	70.0
Tax rate (%)	30.0	30.0	30.0	0.0	0.0	0.0
ROA (%)		-17.7	-16.6	6.1	16.7	18.5
ROE (%)		-49.4	-17.0	9.6	25.5	32.1
Pharma revenue (\$m)	10.1	4.7	5.6	23.7	42.2	59.2
Poppy seed revenue (\$m)	3.8	2.9	3.4	9.0	12.3	15.9
Gross profit (\$m)	1.8	-0.7	0.8	13.3	24.1	35.0
Gross profit margin (%)	13.1	-9.0	8.5	40.5	44.2	46.6

PROFIT AND LOSS (\$m)

Year-end December (AUD)	FY13A	FY14A	FY15F	FY16F	FY17F	FY18F
Sales revenue	14.1	7.6	8.9	32.7	54.5	75.0
EBITDA	-0.8	-5.5	-5.3	6.7	17.4	28.0
Deprn & amort	1.4	1.6	2.5	2.2	2.5	2.9
EBIT	-2.2	-7.1	-7.9	4.5	14.9	25.2
Net interest expense	3.1	1.0	1.0	0.6	0.9	1.5
Tax	-1.6	-2.5	-2.7	0.0	0.0	0.0
Minorities/pref divs	0.0	0.0	0.0	0.0	0.0	0.0
Equity accounted NPAT	0.0	0.0	0.0	0.0	0.0	0.0
Net profit (pre-sig items)	-3.7	-5.7	-6.2	3.9	13.9	23.6
Abns/exts/signif	-1.5	-5.0	-4.0	0.0	0.0	0.0
Reported net profit	-5.2	-10.7	-10.2	3.9	13.9	23.6

CASH FLOW (\$m)

Year-end December (AUD)	FY13A	FY14A	FY15F	FY16F	FY17F	FY18F
EBITDA	-0.8	-5.5	-5.3	6.7	17.4	28.0
Interest & tax	0.0	0.0	-1.0	-0.6	-0.9	-1.5
Working cap/other	0.8	5.5	-7.9	-8.9	-10.4	-8.6
Operating cash flow	0.0	0.0	-14.2	-2.7	6.0	17.9
Maintenance capex	0.0	0.0	-7.0	-10.0	-2.0	-35.0
Free cash flow	0.0	0.0	-21.2	-12.7	4.0	-17.1
Dividends paid	0.0	0.0	0.0	0.0	0.0	-4.4
Growth capex	0.0	0.0	0.0	0.0	0.0	0.0
Invest/disposals	0.0	0.0	0.0	0.0	0.0	0.0
Other inv flows	0.0	0.0	0.0	0.0	0.0	0.0
Cash flow pre-financing	0.0	0.0	-21.2	-12.7	4.0	-21.5
Funded by equity	0.0	0.0	35.3	0.0	0.0	0.0
Funded by debt	0.0	0.0	-14.0	15.0	-5.0	22.0
Funded by cash	0.0	0.0	-0.1	-2.3	1.0	-0.5

BALANCE SHEET SUMMARY (\$m)

Year-end December (AUD)	FY13A	FY14A	FY15F	FY16F	FY17F	FY18F
Cash	0.0	0.6	0.6	2.9	1.9	2.4
Current receivables	0.0	1.2	1.3	6.5	10.9	15.0
Current inventories	0.0	6.4	10.8	21.6	34.2	44.9
Net PPE	0.0	17.8	23.0	31.1	30.8	63.2
Investments	0.0	0.3	0.3	0.3	0.3	0.3
Intangibles/capitalised	0.0	3.1	2.3	2.1	1.9	1.6
Other	0.0	10.8	8.8	8.8	8.8	8.8
Total assets	0.0	40.2	47.3	73.3	88.7	136.1
Current payables	0.0	2.0	2.7	9.8	16.4	22.5
Total debt	0.0	17.6	3.6	18.6	13.6	35.6
Other liabilities	0.0	9.1	4.3	4.3	4.3	4.3
Total liabilities	0.0	28.6	10.6	32.7	34.2	62.4
Minorities/convertibles	0.0	0.0	0.0	0.0	0.0	0.0
Shareholder equity	0.0	11.6	36.7	40.6	54.5	73.7
Total funds employed	0.0	29.2	40.3	59.1	68.0	109.3



Earnings outlook

A summary of our key forecast assumptions is provided in the table below.

Key forecast assumptions								
Y/E: 31 Dec		FY12	FY13	FY14	FY15e	FY16e	FY17e	FY18e
Area harvested	ha	1,700	2,100	1,200	2,020	5,000	6,275	7,450
Yield	kg p/ha	10.5	10.9	10.8	12.0	13.4	14.6	15.0
NRM production volume	tonnes	17.9	22.9	13.0	24.2	67.1	91.3	111.6
- change (YoY)	%	n/a	27.8%	(43.3%)	86.6%	177.4%	36.1%	22.1%
NRM sales volume	tonnes	17.9	22.9	10.1	9.9	40.3	68.5	94.8
- change (YoY)	%	n/a	27.8%	(55.8%)	(1.9%)	305.9%	70.2%	38.4%
Seed sales volume	tonnes	1,094	1,398	792	1,478	3,905	5,074	6,198
- change (YoY)	%	n/a	27.8%	(43.3%)	86.6%	164.2%	29.9%	22.1%
NRM price (p/kg)	AUD	414	443	468	563	588	600	597
- change (YoY)	%	n/a	7.1%	5.6%	20.2%	4.6%	2.0%	(0.5%)
Seed price (p/t)	AUD	1,875	2,740	3,623	2,279	2,313	2,429	2,558
- change (YoY)	%	n/a	46.1%	32.2%	(37.1%)	1.5%	5.0%	5.3%
Grower costs	\$ p/kg	n/a	202	316	198	186	186	186
NRM processing costs	\$ p/kg	n/a	200	200	275	180	162	146

Source: TPE & WHTM.



TPI Enterprises Limited (TPE)

BUSINESS DESCRIPTION

TPI Enterprises Limited (TPE) is one of nine licensed suppliers of licit narcotics (specifically morphine, oripavine, codeine and thebaine) to the global pharmaceutical sector. TPI has spent the past 10 years developing its water-based, solvent-free extraction process while acquiring multiple international, national, state and territory licences.

INVESTMENT THESIS

TPI is a licensed producer of licit narcotics. The industry offers attractive fundamentals, including significant barriers to entry (strict licensing requirements) and solid global consumption growth (~6.0% pa). TPI is well positioned as the only truly independent producer, with first mover advantage on mainland Australian poppy production and significant European raw material supply, as well as a cost-effective extraction process developed over the past decade. With TPI having received its Federal Government manufacturing licence, commissioning of the processing facility and first sales from the relocated facility are the key near-term share price catalysts.

REVENUE DRIVERS

- NRM production (area, yield)
- NRM, API and poppy seed prices

MARGIN DRIVERS

- Production volume
- Crop yields
- Processing costs

KEY ISSUES/CATALYSTS

- Commissioning of processing plant in Melbourne
- Ramp-up of NRM production and sales (towards 100t)
- Confirmation of new working capital debt facility
- Commissioning of API processing capability

RISK TO VIEW

- Reduction in raw material supply
- Changes to international and/or foreign government conventions
- Loss of licences
- FX movements

BALANCE SHEET

- 1H15 net cash: \$6M

BOARD

- Peter Robinson – Non-Executive Chairman
- Jarrod Ritchie – Managing Director
- Todd Barlow – Non-Executive Director

MANAGEMENT

- Jarrod Ritchie – MD
- Peter Varnay – CFO

CONTACT DETAILS

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Recommendation structure and other definitions

Definitions at <http://www.wilsonhtm.com.au/Disclosures>

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