Colts

A research initiative by Canaccord Genuity

HRL Holdings (HRL:ASX)

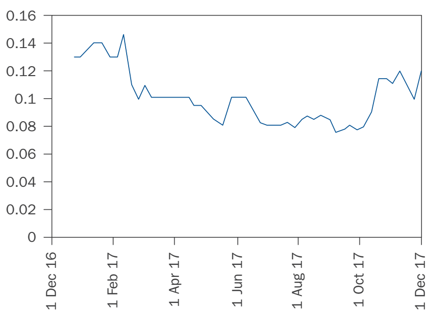
Transformational acquisition

Key Facts	
Company Code	HRL:ASX
Closing Price (20/12/17)	A$0.12
Price Target	A$0.18
Date of Report	21/12/17
Company Website	www.hrlholdings.com
Analyst	Warren Jeffries

Company Statistics	
12-Month Range	A$0.08 - A$0.15
Market Cap (A$Mil)	$56.7m
Issued Shares	493.4m
Issued Options	4.8m
Cash (A$Mil)	A$4.7m

Major Shareholders	%
Viburnum Funds Pty Ltd	16.8%
Kevin Maloney (Tulla Group)	12.4%
Terry Cooney	7.4%
Adam Smith AM	5.2%

Share Price Performance



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If you have received this indirectly, please click **here** to receive future research on HRL and other Colt companies.

Disclaimer: Canaccord Genuity (Australia) Limited has received a fee as the Lead Manager to the HRL Holdings capital raisings announced on 16 February 2017 and 16 October 2017.

HRL Holdings (HRL.ASX) has completed the acquisition of Analytica Laboratories after shareholders recently voted in favor of a $15m capital raising to fund what we believe will be a transformational earnings accretive acquisition for the group. On the back of the Analytica acquisition we have increased our FY18 and FY19 EPS by 9% and 13.5% respectively.

Key points

Strategic and transformation deal – The acquisition of Analytica will provide HRL with new capabilities into higher value markets which include environmental and food / agriculture testing, and comes shortly after HRL entered the geotechnical testing market via the acquisition of Morrison's in March 2017. HRL now has established, and vertically integrated, laboratory testing capabilities within the hazardous materials, geotechnical services and now higher value environmental and food/ agricultural markets, operating at scale in both Australia and New Zealand.

Market opportunity materially lifts – the acquisition of Analytica now exposes HRL to ~50%, from ~12%, of the broader environmental services market which is estimated at ~A$4bn in Australia. With regards to New Zealand we estimate a similar opportunity in a market estimated to be ~NZ$1bn (A$0.95bn). Both the Australian and New Zealand markets have a number of larger established participants with global operations, in addition to a long tail of smaller, local operators that lack scale and a vertically integrated solution. As a result the opportunity exists for HRL to establish themselves as a dynamic, mid-market player in both Australia and New Zealand.

Platform established to leverage expansion – with operations largely established through the acquiring of private companies, HRL has had to also invest in a corporate overhead to support these businesses. We believe HRL now has its corporate overhead and platform established, and will be able to leverage earnings from organic and acquisition growth going forward.

Acquisition Metrics – HRL will pay up to NZ$29m for Analytica with initial consideration of NZ$18m (Cash NZ$13.3m; scrip NZ$5.7m) which will represent 6x maintainable EBITDA of NZ$3m. Analytica vendors are also able to be paid an earn-out of up to NZ$11m in the 12-month period post settlement. An additional $1m has also been paid for Analytica's 26% holding in CAIQtest Pacific, a business co-founded by Analytica to pre-test export product locally before shipping to China.

EPS upgrades – With the Analytica acquisition effective from 1 December 2017, we have upgraded our FY18 and FY19 EPS forecasts to 0.8cps (up 9%) and 0.9cps (up 13.5%) respectively. Based on our forecasts HRL is trading on a FY18 PER of 16x and FY19 PER of 13.5x which is a significant discount to peers.

Valuation and recommendation – on the back of the Analytica acquisition we have increased our DCF Valuation and Target Price to $0.18cps, from $0.12cps. We are mindful that HRL is at an early stage of its evolution, however the business has now established a sound business platform from which to deliver sustainable earnings growth. Our recommendation remains a BUY for HRL.

Fig. 1: HRL Holdings Limited (HRL) Canaccord Genuity forecasts

Profit & Loss ($m)	2017A	2018F	2019F	2020F
Sales Revenue	**13.6**	**28.7**	**35.5**	**37.0**
EBITDA	**1.5**	**5.7**	**8.4**	**8.9**
Depreciation	-0.3	-1.5	-2.1	-2.1
EBITA	**1.2**	**4.2**	**6.3**	**6.8**
Amort - Intangibles	-0.5	-1.8	-2.3	-2.1
EBIT	**0.6**	**2.4**	**4.0**	**4.7**
Net Interest Expense	-0.1	-0.1	-0.1	-0.1
NPBT	**0.5**	**2.3**	**4.0**	**4.6**
Tax expense	-0.1	-0.7	-1.2	-1.3
OEI	0.0	0.0	0.0	0.0
NPAT - Pre NRI's	0.4	1.7	2.8	3.3
NPAT - normalised	**0.8**	**2.9**	**4.4**	**4.8**
Significant items	-0.3	0.0	0.0	0.0
NPAT - reported	**0.1**	**1.7**	**2.8**	**3.3**

Valuation ratios	2017A	2018F	2019F	2020F
EPS (cps) - underlying	0.2	0.4	0.6	0.7
EPS (cps) - normalised	0.4	0.8	0.9	1.0
PER (x)	27.3	16.0	13.5	12.4
PER Rel - All Ind.	60%	-1%	-11%	-14%
PER Rel - Small Ind.	38%	-10%	-14%	-17%
Enterprise Value ($m)	29.4	54.5	57.5	57.5
EV / EBITDA (x)	19.5	9.6	6.8	6.5
EV / EBIT (x)	45.8	22.8	14.2	12.3
DPS (cps)	0.0	0.0	0.0	0.0
Dividend Yield (%)	0.0%	0.0%	0.0%	0.0%
Franking (%)	0%	0%	0%	0%
CFPS (cps)	0.2	0.7	1.3	1.4
P / CFPS (x)	56.8	17.9	9.3	8.8

Cash Flow ($m)	2017A	2018F	2019F	2020F
Operating EBITDA	**1.5**	**5.7**	**8.4**	**8.9**
- Interest & Tax Paid	0.6	0.7	1.3	1.4
+/- change in Work. Cap.	-1.0	-1.3	-0.8	-0.7
- other	-0.7	0.3	0.0	0.0
Operating Cashflow	**0.5**	**3.3**	**6.4**	**6.7**
- Capex	-0.3	-1.4	-1.8	-1.3
- other	-0.0	0.0	0.0	0.0
- acquisitions	-6.2	-12.0	-7.5	-5.5
Free Cashflow	**-6.1**	**-10.1**	**-2.9**	**-0.0**
- Ord Dividends	0.0	0.0	0.0	0.0
- Equity /other	7.9	14.9	0.0	0.0
Net Cashflow	**1.8**	**4.8**	**-2.9**	**-0.0**
Cash at beginning of period	0.4	0.7	5.0	2.6
+/- borrowings / other	-1.5	-0.5	0.5	0.5
Cash at end of period	**0.7**	**5.0**	**2.6**	**3.0**

Profitability ratios	2017A	2018F	2019F	2020F
EBITDA Margin (%)	11.1	19.8	23.8	24.0
EBITA Margin (%)	8.6	14.6	17.9	18.3
EBIT Margin (%)	4.7	8.3	11.4	12.7
ROE (%)	2.8	5.4	8.3	9.0
ROA (%)	6.5	13.5	16.9	16.7
ROIC (%)	8.3	14.4	15.2	14.5

Balance Sheet ratios	2017A	2018F	2019F	2020F
Net Debt (cash)	0.1	-4.7	-1.7	-1.7
Net Gearing (%)	cash	cash	cash	cash
Interest Cover (x)	15.2	104.8	cash	cash
NTA per share ($)	0.0	0.0	0.0	0.0
Price / NTA (x)	2.5	2.6	2.9	2.9
Shares on issue	244.2	493.4	493.4	493.4
EFPOWA (m) - fully diluted	179.6	390.8	493.4	493.4

Balance Sheet	2017A	2018F	2019F	2020F
Cash	0.7	5.0	2.6	3.0
Inventories	0.0	0.0	0.0	0.0
PP&E	1.5	7.4	7.1	6.3
Debtors	3.4	6.0	7.4	8.1
Intangibles	11.7	15.9	21.1	24.5
Other assets	1.6	1.9	1.9	1.9
Total Assets	**18.8**	**36.2**	**40.0**	**43.8**
Borrowings	0.8	0.3	0.8	1.3
Trade Creditors	1.3	2.6	3.2	3.1
Other Liabilities	1.6	1.6	1.6	1.6
Total Liabilities	**3.7**	**4.5**	**5.6**	**6.1**
NET ASSETS	**15.1**	**31.7**	**34.4**	**37.7**

Growth ratios	2017A	2018F	2019F	2020F
Sales revenue ($m)	62.7%	110.7%	23.4%	4.4%
EBITDA ($m)	41.1%	277.2%	48.0%	5.3%
EBIT ($m)	10.3%	272.0%	69.2%	15.9%
NPAT ($m)	12.6%	298.4%	66.7%	18.2%
EPS (cps)	18.9%	70.6%	18.8%	8.3%
DPS (cps)	0.0%	0.0%	0.0%	0.0%

Interim Analysis	1H17A	2H17A	1H18F	2H18F
Revenues	5.5	8.2	10.9	17.9
EBITDA	0.4	1.1	1.6	4.1
EBITDA margin (%)	6.8%	13.9%	14.6%	23.0%
EBITA	0.2	0.9	1.2	2.9
NPAT - normalised	0.1	0.4	1.0	1.9
EPS -normalied	0.1	0.7	0.3	0.5
DPS	0.0	0.0	0.0	0.0

Board of Directors / Substantial Shareholders		
Name	**Shareholding**	**%**
Kevin Maloney - Non-Executive Chairman	61.3	12.4%
Darren Anderson* - Executive Director	43.4	8.8%
John Taylor - Non-Executive Director	1.8	0.4%
Frederick Kempson - Alternative Non-Exec. Director	0.0	0.0%
Substantial Shareholders	**Shareholding**	**%**
Kevin Maloney (Tulla Group)	61.3	12.4%
Viburnum Funds Pty Ltd	82.9	16.8%
Terry Cooney	36.6	7.4%
Adam Smith Asset Management	25.9	5.2%

* Includes family interests. D. Anderson direct holding 21.3m shares

Valuation	2019F
Normalised EBITDA multiple (x)	
EBITDA ($m)	8.4
Target EBITDA multiple (x)	9.1
Net Debt (cash) ($m)	-4.7
Implied Valuation	81.7
Per Share	**$0.17**
Target PE Multiple	
EPS (c)	0.9
PER Target (x)	15.7
Per Share	**$0.15**

Discounted Cash Flow			
Cost of equity	11.0%	WACC	11.0%
Cost of debt	4.8%	Terminal Growth Rate	3.0%
Net Debt/ Net debt + equity	0.7%	**Per Share**	**$0.18**

Source: Canaccord Genuity Estimates

Acquisition of Analytica Laboratories

HRL has completed what we deem a highly transformational acquisition in acquiring the New Zealand based Analytica Laboratories. We see the acquisition as representing a highly strategic and earnings accretive deal for HRL.

On an annualised basis we estimate the acquisition of Analytica will see the combined business deliver FY18 revenues of $33m and EBITDA of $7.3m, against our previous forecasts for HRL to deliver FY18 revenues and EBITDA of $22.1m and EBITDA of $3.2m prior to Analytica.

We note the combined business is forecast to generate annualised FY18 EBITDA margins of 22%, up from 14.7% for HRL prior to Analytica, which reflects the higher value markets Analytica operates in.

Earnings accretion

With the transaction effective from 1 December 2017, we have upgraded our FY18 and FY19 EPS forecasts to 0.8cps (up 9%) and 0.9cps (up 13.5%) respectively.

“We estimate the acquisition of Analytica expands HRL’s addressable market to A$2-$2.5bn domestically.”

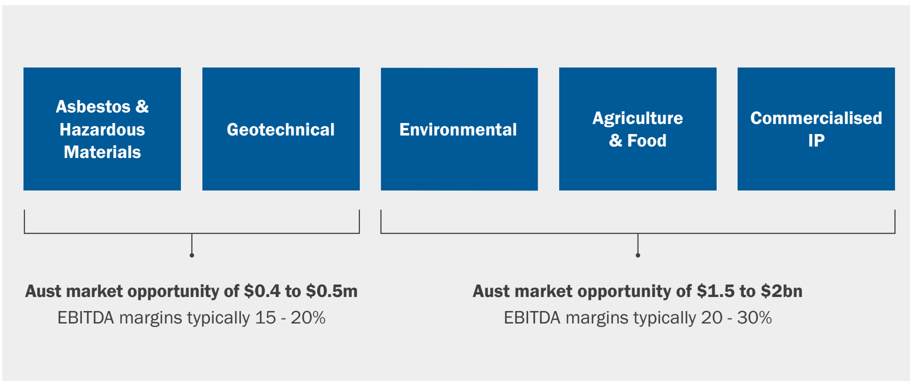
Expanded capabilities and market opportunity

The acquisition of Analytica provides HRL with significant scale across both its Australian and New Zealand operations, while also allowing HRL to expand into new, higher value verticals in environmental and food /agriculture testing.

More specifically Analytica has material market positions within the New Zealand honey and milk dairy industries, both of which it is recognised as a market leader and innovator of high volume, cost effective testing solutions. We note more recent growth opportunities are coming predominantly from environmental (being land & water) and methamphetamine (Drugs of Abuse) testing volumes.

We estimate the acquisition of Analytica expands HRL’s addressable market to A$2-$2.5bn domestically, from ~A$0.5bn previously, while we estimate the opportunity in New Zealand to be approximately NZ$1bn (A$0.95bn).

Fig. 2: Markets & opportunities



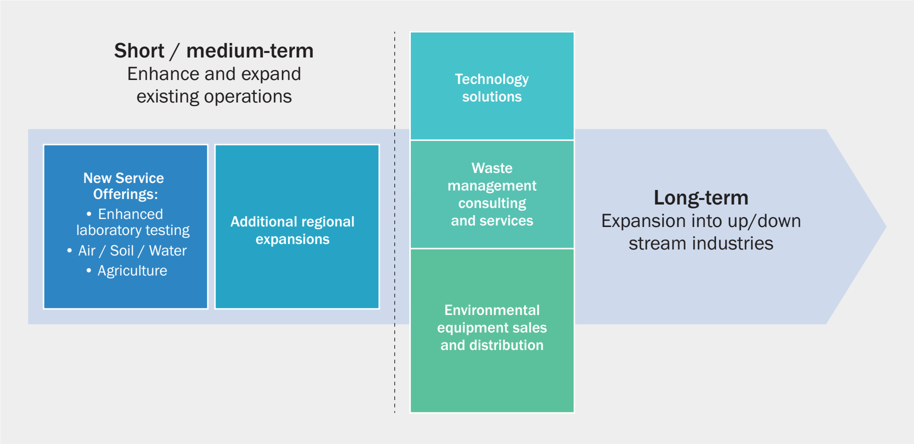
Source: Company Reports

HRL management delivering on growth strategies

We note the move by HRL to acquire Analytica, which has resulted in a move into new markets and an expanded geographical footprint, meets with previous strategic expansion initiatives being targeted by HRL management in the short to medium-term.

Longer-term opportunities to vertically integrate additional capabilities remains very much a part of future strategies to be pursued.

Fig. 3: HRL growth strategies



Source: Company Reports

> "Analytica's ability to innovate and quickly respond to the immediate needs or concerns of its clients has also been a key driver of expansion from the Milk Dairy and Honey sectors and into Environmental (water & land) and Methamphetamine (Drugs of Abuse) testing."

Key acquisition details

HRL will acquire Analytica for up to NZ$29m, with initial consideration of NZ$18m representing an EBITDA multiple of 6x based on Analytica delivering EBITDA of NZ$3m in the first 12-months post settlement, with settlement being 1 December 2017.

Additional earn-out consideration of up to NZ$11m can be achieved based on the following:

- Ongoing service by the Analytica vendors of at least 2-years post settlement;
- Any EBITDA in excess of NZ$3m in the 12-month period post settlement will result in Analytica vendors receiving cash consideration based on a 6x multiple for each NZ$1 of EBITDA greater than NZ$3m, up to NZ$11m (A$10.5m). We note to achieve the maximum earnout of NZ$11m Analytica needs to deliver EBITDA of NZ$4.83m (A$4.6m) in the 12-month period to 1 December 2018.
- Earnout consideration to be paid in cash with 50% to be paid immediately after earnout period ceases, and the balance paid monthly over the following 12-months.

We note our current forecasts assume Analytica receives its full NZ$11m (A$10.5m)

Analytica Laboratories

Analytica was founded in 2011 by Dr. Terry Cooney with the aim of establishing a chemistry laboratory that would disrupt the market through innovative laboratory services. Dr. Terry Braggins and Mr. Steve Howse joined Analytica soon after as executive directors and equity partners, with Analytica operating out of the Ruakura Research Centre campus where it remains today.

A key point difference for Analytica is the ability to innovate through large scale and automated testing solutions for customers for which both the milk dairy and honey industries were initial beneficiaries in 2013 of high throughput, cost effective routine testing. Analytica's ability to innovate and quickly respond to the immediate needs or concerns of its clients has also been a key driver of expansion from the milk dairy and honey sectors and into environmental (water & land) and methamphetamine (Drugs of Abuse) testing.

Key competitive advantages for Analytica:

- Founders and directors of Analytica are respected operators across industry, academia and government, with significant years of practical experience;
- Highly innovative and responsive to client requirements, while being cost effective in providing high volume testing solutions;
- State of the art facilities are coupled with close academic ties to allow Analytica to provide leading edge testing solutions;
- A market leader in honey and dairy testing in New Zealand, with close commercial ties with MilkTest NZ; and
- Founding Shareholder (26%) of CAIQTest Pacific which is a business established to provide pre-shipment certification testing from New Zealand to the Chinese market.

Key industries and opportunities

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HRL has established capabilities and strong market positioning within the New Zealand honey and milk dairy industries…

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HRL has established capabilities and strong market positioning within the New Zealand honey and milk dairy industries, for which Analytica’s market position was established through innovative, high volume testing and analysis regimes that were provided to clients in a timely and cost effective manner.

While both the honey and milk dairy business remains material to Analytica’ s operations today, the business applicable to both industries is relatively mature against new growth opportunities quickly emerging from environmental and methamphetamine (Drugs of Abuse) markets.

Honey – the market is predominately built around Manuka honey grading given its high value and the Ministry for Primary Industries (MPI) regulatory requirement to test honey for the toxin Tutin, which is widely found in honey from New Zealand.

While there are evolving requirements for new testing in New Zealand for which Analytica is well positioned, the opportunity within honey is relatively mature with Analytica holding a dominant market share within New Zealand. We note also that honey production volumes are also exposed to the variability in weather conditions and some seasonality.

While there is potential longer-term for Analytica to take its capabilities in honey into the Australian market, we make no allowance for such expansion in our forecasts at this stage, and for honey testing revenues to remain largely flat near-term.

Dairy – consists of regular residue testing in liquid milk and to a lesser extent manufactured dairy products. Ongoing work includes testing for residues of detergents used on dairy farms and in processing plants and the animal feed derived toxin, Aflatoxin M1.

The other major category of testing is liquid milk and manufactured products for A2 proteins, used to confirm there is no A1 protein in the milk of the product for quality assurance purposes.

Analytica has established capabilities and volumes within the dairy industry, and two key customers in MilkTest NZ and A2 Corp, liquid milk testing is dominated by MilkTest NZ and manufactured dairy product testing is competitive and as a result a market that Analytica has not entered.

While the Dairy industry represents >20% of Analytica’s business, similar to Honey the opportunity for growth in the New Zealand market is somewhat modest near-term.

Environmental – incorporates a broad scope of tests covering organic and inorganic contaminants found in soil and water. Air testing is the other major category of sample type but is not currently included in Analytica’s scope.

Analytica’s environmental offering was only launched in mid-2016 after a 2-year development period, and is now providing innovated and cost effectively solutions to the industry. Analytica has had rapid take up of its testing services across the broader environmental market, and substantial growth is expected in the short to medium-term with environmental revenues expected to represent ~20% of FY18 revenues, from 11% in FY17.

Competition for environmental testing work comes predominantly from larger players in Hill Laboratories and then Eurofins, however an opportunity for a nimble and innovative local provider represents a clear opportunity for Analytica.

Methamphetamine / Drugs of Abuse (DoA) – testing is currently focused on analysis of surface wipe samples for methamphetamine and related compounds (amphetamine, ephedrine and pseudoephedrine). With new testing capabilities launched in 2016, DoA testing is a material part of Analytica’s operations and the opportunity for continued growth is strong from both the mass market, with work being derived from social housing providers, while growing opportunities are coming from private property owners at the point of sale or in conjunction with changing tenancy of rental properties.

We note that for a number of years now Analytica has undertaken outsourced methamphetamine testing for HRL’s Precise Consulting operation in New Zealand. Competition is predominantly from Hill Laboratories in New Zealand, and we note that Eurofins has not entered the New Zealand market with a localised service despite being prominent in Australia.

Other areas of growth / potential

- **Miscellaneous** – represents adhoc contract research work for existing clients, with projects associated with the A2 protein becoming the most prominent.

- **Food origin** – Analytica has a contract with a leading product trace origin company to provide testing and analysis of trace elements in food and medical samples. Product source trace testing provides a service to verify food origin using telltale 'fingerprints' derived from the chemical compositions of plants, soils, water and the feed animals products have consumed. While the contract is relatively modest currently, we expect it will continue to represent ~4% of group revenues going forward.
- **Timber** – timber testing relates to the analysis of timber preservatives in treated timber samples and prepared sample extracts. Analytica provides a cost effective method for a local laboratory, and while the recent move into timber has provided new growth, off a low base will represent only ~3% of group revenue.
- **Dairy A1/A2 phenotyping** – this is an emerging business opportunity using milk samples to provide a fast and low cost classification of dairy cows for their ability to produce the A2 beta casein protein. The opportunity exists here to extend the capability in the future into the establishment of a rapid genotyping service to provide similar information for non-lactating animals such as young stock or dry cows. Coming off a very modest base in FY18 the business is expected to grow to ~2% of group revenues by FY19.

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The opportunity exists here to extend the capability in the future into the establishment of a rapid genotyping service to provide similar information for non-lactating animals such as young stock or dry cows.

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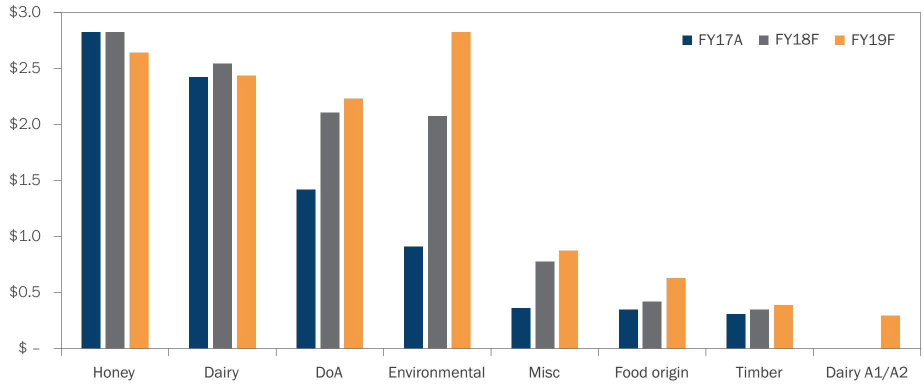
Fig. 4: Analytica revenues ($m) FY17A to FY19F

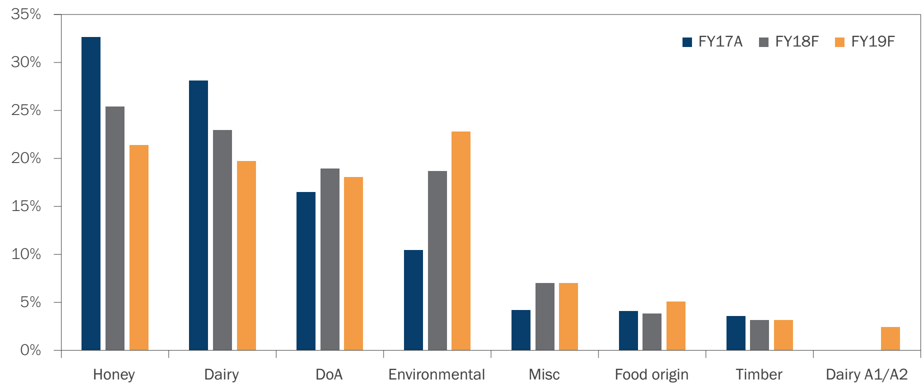


Source: Company Reports

Revenue growth in the medium term for Analytica is forecast to be underpinned from environmental and methamphetamine (DoA) opportunities being realised.

We note our revenue growth forecasts for Analytica make no allowance at this stage for revenue synergies that may come from the current HRL footprint in Australia, however these could be reasonably expected longer-term.

Fig. 5: Analytica revenue splits FY17A to FY19F



Source: Company Reports

A broadening of the revenue mix and reduced reliance on honey and milk dairy for growth is being driven by new environmental and methamphetamine (DoA) volumes, and both of these opportunities appear at the early stage of a strong medium-term growth outlook.

CAIQTest Pacific – 26% owned by Analytica

CAIQTest Pacific has been established to expedite the export of goods from Australasia to China through pre-shipment certification of goods locally for fast and low risk release on arrival. Currently focused on the dairy export market, CAIQTest Pacific has ~45 test established methods that are relevant to dairy products, using Chinese methods as per Chinese national standards.

The laboratory has been accredited in New Zealand from IANZ (International Accreditation New Zealand) and the MPI, in addition to accreditation from CNAS (Chinese National Accreditation Service for Conformity Assessment) which is the national accreditation body of China, and gaining CNAS accreditation for a non-Chinese laboratory can be considered unique.

While we understand there is no specific requirements in China to use any given laboratory for the testing of imported goods, given the accreditations and part ownership of the CAIQTest Pacific laboratory by CAIQTest (the Chinese Academy of Inspection and Quarantine) in Beijing, there is a high level of endorsement and trust in CAIQTest Pacific and its testing regimes.

> “On the back of the Analytica acquisition we have increased our normalised EPS forecasts for FY18 and FY19 to 0.8cps (up 9%) and 0.9cps (up 13.5%) respectively.”

CAIQTest Pacific currently operates out of the same facilities as Analytica, located in the Ruakura Research Centre campus in Hamilton, New Zealand, with a subsidiary registered in Australia. CAIQTest Pacific commenced testing on a backlog of work in August 2017 for dairy product being exported out of New Zealand. While we have made no assumptions around the timing of profitability of CAIQTest Pacific, and its potential contribution to HRL earnings, we do believe there is potential for the business to a material contributor longer-term should export markets remain favorable, and subsequent expansion opportunities be realised.

We note the pending infant formula registration rules in China to ensure imported product meets a minimum standard of nutritional needs for children, which are expected to be implemented from 1 January 2018. The MPI believes that most New Zealand manufactures have either applied or are on track to apply to have their brands registered by 1 January 2018 for the Chinese market.

Financial impact - Analytica

With the acquisition effective from 1 December 2018, we are forecasting Analytica to deliver FY18 revenues of A$6.7m and EBITDA of A$2.4m, which does skew earnings towards 2H18. We have assumed an exchange rate of NZD:AUD $1.05.

Our existing forecasts for HRL pre Analytica remain unchanged for FY18 revenues of A$22.1 m and EBITDA of A$3.2m. Consolidated FY18 revenues for HRL are now $28.7m (up 30%) and EBITDA $5.7m (up 75%), while FY19 revenues and EBITDA increase to $35.5m (up 53%) and $8.4m (up 141%) respectively. On the back of the Analytica acquisition we have increased our normalised EPS forecasts for FY18 and FY19 to 0.8cps (up 9%) and 0.9cps (up 13.5%) respectively. We expect the combined HRL/Analytica will remain in a net cash position in the medium-term, and future earn-out payments are forecast to be largely funded from existing cash reserves and cash generation. HRL have a current debt facility of $1.3m which it can also draw down on.

Fig. 6: Financial forecast changes

	FY18F				FY19F			
($m) - unless stated	**Orig**	**Analytica**	**Rev**	**%Δ**	**Orig**	**Analytica**	**Rev**	**%Δ**
Sales Revenue	22.1	6.7	28.7	30.2%	23.1	12.3	35.5	53.3%
EBITDA	3.2	2.4	5.7	75.4%	3.5	4.9	8.4	140.8%
EBITDA margin	14.7%	36.7%	19.8%	34.8%	15.1%	40.0%	23.8%	57.1%
Depreciation	-0.7	-0.8	-1.5	114.3%	-0.7	-1.4	-2.1	196.9%
EBITA	2.5	1.6	4.2	64.7%	2.8	3.5	6.3	126.7%
Amort - Intangibles		-0.8	-1.8	80.0%		-1.3	-2.3	130.0%
EBIT	1.5	0.8	2.4	54.9%	1.8	2.2	4.0	124.9%
NPBT	1.4	0.9	2.3	66.6%	1.7	2.2	4.0	129.0%
Tax expense	-0.4	-0.2	-0.7	58.2%	-0.5	-0.7	-1.2	129.0%
NPAT - Pre NRI's	1.0	0.7	1.7	70.1%	1.2	1.6	2.8	129.0%
NPAT - normalised	1.7	1.2	2.9	72.4%	1.9	2.5	4.4	129.4%
EPS - normalised	0.7	0.1	0.8	8.9%	0.8	0.1	0.9	13.5%

Source: Company reports, CGAu & Factset estimates (Market cap in $M)

Pro-forma earnings

Analytica is forecast to deliver annualised FY18 revenues of A$11m (NZ$11.6m) and EBITDA of A$4m (NZ$4.2m). On a pro-forma basis we estimate this has resulted in FY18 EPS increasing by 5.5% to 0.7cps, with earnings skewed to the 2H as new business ramps up. For FY19 our forecasts assume Analytica delivers EBITDA of A$4.9m (NZ$5.2m), which includes the expectation that Analytica achieve their maximum earn-out payment of NZ$11m (A$10.5m).

"HRL is currently trading on a material discount to our broader-based peer group for FY18 and FY19 on both a PER and EV/EBITDA basis."

Fig 7: Pro-forma forecast changes

	FY17A			FY18F			FY19F
	HRL	Analytica	Combined	HRL	Analytica	Combined	Combined
Revenues	21.2	8.7	29.9	22.1	11.0	33.1	35.5
EBITDA	2.7	3.2	5.9	3.2	4.0	7.3	8.4
EBITDA %	13%	37%	20%	15%	37%	22%	23.8%
EBITA				2.2	2.6	4.8	6.8
EBIT				1.5	1.1	2.6	4.0
NPBT				1.4	1.1	2.5	4.0
NPAT				1.0	0.8	1.8	2.8
NPAT - normalised				1.7	1.9	3.6	4.4
EPS - normalised				0.7		0.7	0.9
EPS accretion						5.5%	13.5%

Source: Company reports, CGAu & Factset estimates (Market cap in $M)

Valuation & Target Price – $0.18 cps

On the back of the Analytica acquisition we have increased our DCF valuation and Target Price to A$0.18cps, from A$0.12cps.

Our DCF Valuation methodology incorporates a WACC of 11.0% (from 11.2%) which is derived from a 4.25% risk free rate, a 1.35x beta and a 5.0% equity risk premium. For NVL we have assumed a terminal growth rate of 3%, up from 2.5% given the higher growth segments HRL are now exposed to through Analytica.

Peer group comparison

Fig. 8: Peer group metrics

		Market	PER		EV/EBITDA	
Company		Cap (Loc)	FY18 (x)	FY19 (x)	FY18 (x)	FY19 (x)
ALQ-AU	ALS LIMITED	3453.9	24.3	19.9	12.8	11.1
BVI-FR	BUREAU VERITAS	10022.3	24.1	22.9	13.6	12.9
ERF-PAR	EUROFINS SCIENTIFI	9061.7	42.1	33.3	18.9	15.8
ITRK-GB	INTERTEK GROUP	8247.1	26.7	25.0	15.6	14.5
SGSN-SWX	SGS SA	18893.5	28.0	24.4	15.3	14.1
	Median		26.7	25.0	15.3	14.1
HRL-AU	HRL HOLDINGS LTD	56.7	16.0	13.5	9.6	6.8
	Premium / (disc't) - median		-40%	-46%	-37%	-52%

Source: Company Reports, Canaccord Genuity estimates / Prices as at 1 August 2017

Against a broader peer group of businesses operating in the environmental testing and services market sector globally, and based on consensus estimates for peers, HRL is currently trading on a material discount to our broader-based peer group for FY18 and FY19 on both a PER and EV/EBITDA basis.

We do note however that our peer group are businesses that operating across a broader spectrum of industries to HRL, while they are also larger in size with a significantly expanded and established global capability, however should HRL execute positively on their currently opportunity, we see that discount reducing in the medium-term.

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