

## 1300 Smiles (ONT)

### RECOMMENDATIONS

Rating	<b>BUY ▲</b>
Risk	Medium
Price Target	<b>\$7.10</b>
Share Price	\$6.00

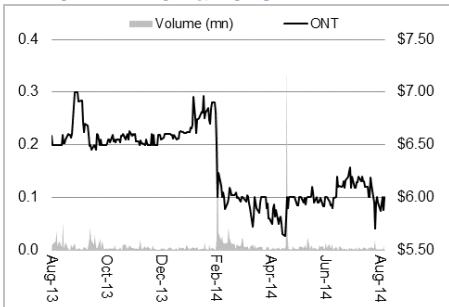
### SNAPSHOT

Monthly Turnover	\$0.4mn
Market Cap	\$139mn
Shares Issued	23.7mn
52-Week High	\$7.25
52-Week Low	\$5.35
Sector	Health Care

### BUSINESS DESCRIPTION

1300 Smiles Limited (ONT) provides dental surgeries, practice management and other administrative services to self-employed dentists. It also provides general dentistry services to patients. 1300SMILES enables the delivery of services to patients by providing the use of dental surgeries, practice management and other services to self-employed dentists who carry on their own dental practices. The administrative and corporate services headquarters is in Townsville.

### 12-MONTH PRICE & VOLUME



### RESEARCH ANALYST

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### Disclosure

The author owns no shares in ONT.

### COMPANY REPORT

#### Starting to smile again

- FY14:** Reported NPAT of A\$5.0m (-22% pcp) versus our forecast of A\$5.9m. The key difference to our forecast was due to around A\$0.6m in stamp duty on acquisition costs that were expensed in 2H14 that we had not expected, and higher D&A charges than forecast. 2H14 fully franked dividend of A8cps making a total for FY14 of A14.5cps representing a payout ratio of 69% (FY13:69%).
- Key takeaways:** 1) stronger revenue growth than expected in 2H14 as the business recovered from the cessation of the Chronic Disease Dental (CDDS) scheme in late 2012; 2) business development expenses included a 2H14 one-off A\$0.6m charge for stamp duty on recent acquisitions which ONT was unable to capitalise; 3) very strong margin performance despite lower revenue base.
- Revenue:** FY14 revenue growth trends were negatively impacted by the cessation of the CDDS in FY13. However, FY14 revenue was stronger than we expected. Most importantly over-the-counter revenue (which represents the gross fees paid by clients) decreased to A\$43.3m (-11% pcp) with a significant improvement from the -26% pcp run-rate at 1H14. Also, reported revenue (ONT's share) decreased to A\$31.8m (-12% pcp) which again showed a significant pick-up from the run-rate of -30% pcp at 1H14. The result includes six months contribution from the new Child Dental Benefits Scheme (CDBS) and about one month from the BOH Dental Group (BOH) acquisition which ONT management rate highly.
- Expenses:** FY14 Group EBITDA margin of 30.4% (FY13: 30.9%) with a 2H14 margin of 29.4% retarded by the one-off stamp duty on acquisitions costs. What is noticeable is that ONT has been able to broadly hold margins on a materially lower revenue base post the cessation of the CDDS.
- Financial position:** Balance sheet remains strong; no debt and A\$1.4m cash.
- Outlook:** Outside of broad industry fundamentals such as favourable labour supply and increasing acquisition opportunities we would highlight: 1) the flow through of the CDBS into FY15 revenues – we estimate it could add around 5-10% to ONT's FY14 revenue base; 2) a full year inclusion of BOH which is expected to add at least A\$1.2m in EBITDA in FY15; and 3) commencement of the A\$1.3bn Adult Dental Care scheme in July 2015.
- Changes to forecasts:** Downgrade FY15 and FY16 forecasts by 10% although this largely flows for higher assumed D&A charges. Modest changes to EBITDA forecasts.
- Investment view:** BUY maintained with revised DCF valuation of A\$7.10 (prev. A\$7.13) and price target of A\$7.10 (prev. A\$7.15). ONT has now survived the material fall in industry revenues through FY13 and FY14 in good shape. We now expect FY13/14 to be the low watermark for industry revenues before a rebound in FY15. ONT looks set to be a beneficiary of this rebound. We expect further acquisitions to also augment growth from here.

### INVESTMENT SUMMARY

Year End: 30 June		2013 (A)	2014 (A)	2015 (E)	2016 (E)	2017 (E)
Revenue	\$mn	36	32	39	46	53
EBITDA	\$mn	11.2	9.7	12.8	14.9	17.3
EBIT	\$mn	9.0	7.4	10.3	11.9	13.8
Reported Profit	\$mn	6.4	5.0	7.3	8.5	9.8
Adjusted Profit	\$mn	6.4	5.0	7.3	8.5	9.8
EPS (Reported)	¢	26.9	21.1	30.8	35.8	41.4
EPS (Adjusted)	¢	26.9	21.1	30.8	35.8	41.4
EPS Growth	%	1.1	-21.7	46.1	16.3	15.7
PER (Reported)	x	22.3	28.5	19.5	16.8	14.5
PER (Adjusted)	x	22.3	28.5	19.5	16.8	14.5
Dividend	¢	18.5	14.5	19.0	21.5	25.0
Yield	%	3.1	2.4	3.2	3.6	4.2
Franking	%	100	100	100	100	100

## Financial summary

1300 Smiles Ltd											
<b>Analyst:</b>	Nick Caley					<b>Rating:</b>	<b>BUY</b>				
<b>Date:</b>	29-August-2014					<b>Price Target:</b>	\$7.10				
<b>Share Price (\$A):</b>	\$6.00					<b>Valuation:</b>	\$7.10				
<b>Year End:</b>	30 June					<b>Upside/(Downside):</b>	18%				
<b>Risk:</b>						Medium					
<b>Market Capitalisation A\$m:</b>						\$139					
<b>PROFIT &amp; LOSS (A\$m)</b>	<b>FY13A</b>	<b>FY14A</b>	<b>FY15E</b>	<b>FY16E</b>	<b>FY17E</b>	<b>EARNINGS</b>	<b>FY13A</b>	<b>FY14A</b>	<b>FY15E</b>	<b>FY16E</b>	<b>FY17E</b>
<b>Total Revenue</b>	<b>36.2</b>	<b>31.8</b>	<b>39.5</b>	<b>45.9</b>	<b>53.1</b>	EPS - Basic	26.9	21.1	30.8	35.8	41.4
Consumables	5.3	3.5	4.3	5.0	5.8	EPS - Diluted	26.9	21.1	30.8	35.8	41.4
Employee Expenses	15.0	11.9	15.0	17.4	20.2	EPS Growth (%)	1%	-22%	46%	16%	16%
Property Expenses	2.2	2.3	3.0	3.4	4.0	DPS	18.5	14.5	19.0	21.5	25.0
Operating Expenses	2.2	3.3	3.9	4.6	5.3	Franking (%)	100	100	100	100	100
Corp.& Admin.Expenses	0.3	1.1	0.4	0.5	0.5	Payout Ratio (%)	69%	69%	62%	60%	60%
<b>Total Cash Operating Exp.</b>	<b>25.0</b>	<b>22.1</b>	<b>26.6</b>	<b>31.0</b>	<b>35.8</b>	<b>VALUATION</b>	<b>FY13A</b>	<b>FY14A</b>	<b>FY15E</b>	<b>FY16E</b>	<b>FY17E</b>
<b>EBITDA</b>	<b>11.2</b>	<b>9.7</b>	<b>12.8</b>	<b>14.9</b>	<b>17.3</b>	P/E (x)	22.3	28.5	19.5	16.8	14.5
Depreciation & Amortisation	2.1	2.3	2.6	3.0	3.5	EV/EBIT (x)	14.6	18.9	13.5	11.3	9.5
<b>EBIT</b>	<b>9.0</b>	<b>7.4</b>	<b>10.3</b>	<b>11.9</b>	<b>13.8</b>	EV/EBITDA (x)	11.9	14.5	10.8	9.0	7.6
Finance Costs	0.1	0.0	0.0	0.0	0.0	Dividend Yield (%)	3.1%	2.4%	3.2%	3.6%	4.2%
Net Interest Expense	0.1	0.0	0.0	0.0	0.0	Price/Book (x)	5.1	4.9	4.4	3.9	3.5
<b>Net Profit Before Tax</b>	<b>8.9</b>	<b>7.4</b>	<b>10.3</b>	<b>11.9</b>	<b>13.8</b>	Price/NTA (x)	9.7	17.3	12.9	10.0	7.9
Income Tax Expense	2.6	2.4	3.0	3.5	4.0	Price/Cash/Flow per Share (x)	16.5	17.4	14.4	12.4	10.7
<b>Net Profit After Tax</b>	<b>6.4</b>	<b>5.0</b>	<b>7.3</b>	<b>8.5</b>	<b>9.8</b>	<b>GROWTH</b>	<b>FY13A</b>	<b>FY14A</b>	<b>FY15E</b>	<b>FY16E</b>	<b>FY17E</b>
<b>BALANCE SHEET (A\$m)</b>	<b>FY13A</b>	<b>FY14A</b>	<b>FY15E</b>	<b>FY16E</b>	<b>FY17E</b>	Total Rev. Growth (% pcp)	-1%	-12%	24%	16%	16%
<b>Current Assets</b>						Cash Op. Exp. Growth (% pcp)	-2%	-12%	21%	16%	16%
Cash	8.1	1.4	3.9	7.2	11.5	EBITDA Growth (% pcp)	1%	-14%	33%	16%	16%
Receivables	0.8	1.5	1.5	1.5	1.5	EBIT Growth (% pcp)	-2%	-18%	39%	16%	16%
Other	0.2	0.1	0.1	0.1	0.1	NPBT Growth (% pcp)	2%	-18%	39%	16%	16%
<b>Total Current Assets</b>	<b>9.0</b>	<b>2.9</b>	<b>5.5</b>	<b>8.8</b>	<b>13.0</b>	NPAT Growth (% pcp)	3%	-22%	46%	16%	16%
<b>Non Current Assets</b>						<b>MARGINS &amp; RETURNS</b>	<b>FY13A</b>	<b>FY14A</b>	<b>FY15E</b>	<b>FY16E</b>	<b>FY17E</b>
Receivables	1.8	2.1	2.1	2.1	2.1	EBITDA Margin (%)	31%	30%	33%	33%	33%
Property, Plant & Equipment	8.7	12.0	12.2	12.1	11.8	EBIT Margin (%)	25%	23%	26%	26%	26%
Intangibles	13.3	21.0	21.5	22.0	22.5	NPBT Margin (%)	25%	23%	26%	26%	26%
Deferred Tax	0.5	0.5	0.5	0.5	0.5	ROIC (%)	42%	38%	76%	68%	61%
Other	0.4	0.3	0.3	0.3	0.3	ROE (%)	23%	17%	24%	25%	26%
<b>Total Non Current Assets</b>	<b>24.8</b>	<b>35.9</b>	<b>36.6</b>	<b>37.0</b>	<b>37.1</b>	ROA (%)	18%	14%	18%	19%	20%
<b>Total Assets</b>	<b>33.8</b>	<b>38.8</b>	<b>42.1</b>	<b>45.8</b>	<b>50.2</b>	Effective Tax Rate (%)	29%	32%	29%	29%	29%
<b>Current Liabilities</b>						<b>GEARING</b>	<b>FY13A</b>	<b>FY14A</b>	<b>FY15E</b>	<b>FY16E</b>	<b>FY17E</b>
Payables	4.2	5.8	5.8	5.8	5.8	Net Debt (A\$m)	-8	-1	-4	-7	-11
Loans & Borrowings	0.0	0.0	0.0	0.0	0.0	Net Debt/Equity (%)	-29%	-5%	-12%	-20%	-28%
Income Tax	0.9	0.9	0.9	0.9	0.9	<b>OPERATING</b>	<b>FY13A</b>	<b>FY14A</b>	<b>FY15E</b>	<b>FY16E</b>	<b>FY17E</b>
Employee Benefits	0.0	0.6	0.6	0.6	0.6	No Of Dental Centres	25	25	27	29	31
Other	0.2	0.2	0.2	0.2	0.2	Average No Of Dental Centres	24	24	26	28	30
<b>Total Current Liabilities</b>	<b>5.3</b>	<b>7.4</b>	<b>7.4</b>	<b>7.4</b>	<b>7.4</b>	Revenue Per Ave.Centre A\$m	\$1.492	\$1.323	\$1.518	\$1.639	\$1.770
<b>Non Current Liabilities</b>						<b>CASH FLOW (A\$m)</b>	<b>FY13A</b>	<b>FY14A</b>	<b>FY15E</b>	<b>FY16E</b>	<b>FY17E</b>
Payables	0.0	1.5	1.5	1.5	1.5	<b>Cash at Start</b>	<b>13.5</b>	<b>8.1</b>	<b>1.4</b>	<b>3.9</b>	<b>7.2</b>
Loans & Borrowings	0.0	0.0	0.0	0.0	0.0	Cash Flow from Ops	8.6	8.2	9.9	11.5	13.3
Provisions	0.6	0.7	0.7	0.7	0.7	Cash Flow From Investing	-1.9	-11.3	-3.3	-3.4	-3.6
<b>Total Current Liabilities</b>	<b>0.6</b>	<b>2.2</b>	<b>2.2</b>	<b>2.2</b>	<b>2.2</b>	Cash Flow From Financing	-12.2	-3.6	-4.0	-4.7	-5.4
<b>Total Liabilities</b>	<b>5.9</b>	<b>9.6</b>	<b>9.6</b>	<b>9.6</b>	<b>9.6</b>	Net Cash Flow	-5.4	-6.7	2.5	3.3	4.2
Contributed Capital	15.5	15.5	15.5	15.5	15.5	<b>Cash At End</b>	<b>8.1</b>	<b>1.4</b>	<b>3.9</b>	<b>7.2</b>	<b>11.5</b>
Reserves	0.0	0.0	0.0	0.0	0.0						
Retained Earnings	12.5	13.7	17.0	20.7	25.1						
Minority Interests	0.0	0.0	0.0	0.0	0.0						
<b>Total Equity</b>	<b>28.0</b>	<b>29.2</b>	<b>32.5</b>	<b>36.2</b>	<b>40.6</b>						

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