

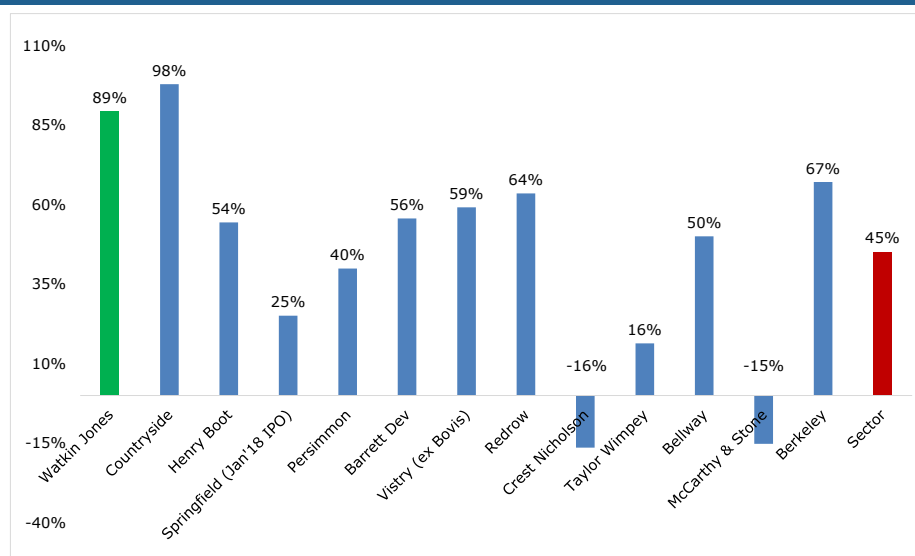
Consistently high achiever

14th January 2020

It's sometimes easy for investors to get caught up in the latest 'buzz doing the rounds', and lose sight of the big picture. Namely finding quality stocks that can out-perform across the economic cycle. Cue Watkin Jones, a developer/manager of large scale, multi occupancy accommodation, who - since IPO'ing at 100p in March 2016 - has delivered a total return of 163% (28.6% IRR):- split 142p capital appreciation and 21p dividends.

All derived organically and with less volatility than the sector average (see appendices) - despite being buffeted last year as Woodford Inv. Mgt disposed of its entire 13% stake.

3 year share price performance vs UK housebuilders



Source: Equity Development

'Golden era' for BtR has only just begun

Indeed **WJG's earnings predictability** was once again centre stage in today's prelims, with **PBT coming in at £52.3m** (+4.5% vs £50.1m LY) - **slightly above our estimates** of £51.0m. **All student beds (2,609) & Build-to-Rent units (159) scheduled for delivery in FY20 have been forward sold.** And over the coming years, this resilience should improve further, as the organisation transitions more towards BtR from PBSA, whose share of gross profits is anticipated to decline to 53% (£70m) by FY24 vs 67% in FY19 (see page 3).

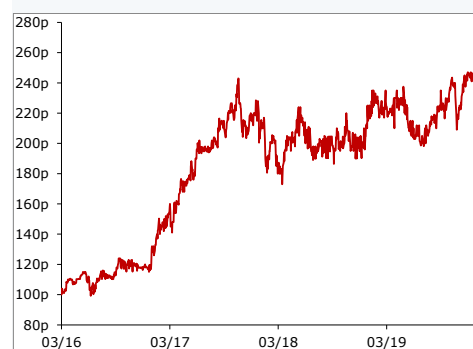
In terms of the numbers, **group turnover climbed 3.2% to £374.8m** (£363.1m LY), with **the dividend hiked 9.9% to 8.35p** (7.6p LY & 2x covered), reflecting **robust cashflows** and **closing net funds of £76.8m** (£80.2m LY), equating to 30p/share.

Elsewhere **gross profits rose 6.0% to £76.8m** (margin 20.5%) with **PBSA delivering the lion's share at £51.6m** (vs £60.7m LY), but ably supported by BtR (£13.2m vs £1.0m LY), residential housing (£7.7m vs £4.4m) and Fresh lettings (£4.6m vs £4.5m). EBIT margins ticked up to 14.0% (13.7%) thanks to tight cost control, with adjusted EPS climbing 4.6% to 16.7p (16.0p).

Company Data

EPIC	AIM:WJG
Price (previous close)	242p
52 week Hi/Lo	248p/198p
Market cap	£621m
ED valuation/share	300p
Net cash (Sept'19)	£76.8m
Sharecount	255.7m
Daily volume	250k

Share Price (p)



Source: Share Cast

Company Description

Watkin Jones is the **UK's leading developer and manager of 'residential for rent'**, with a focus on purpose built student accommodation (PBSA) and residential build to rent (BtR).

Both areas are expanding, supported by strong fundamentals - enabling the firm to leverage its reputation & industry expertise, along with operating a forward sale, low risk, cashflow positive and capital light model.

The residential property & agency lettings business (Fresh) is also set to become a growth engine.

Next news: AGM February 2020

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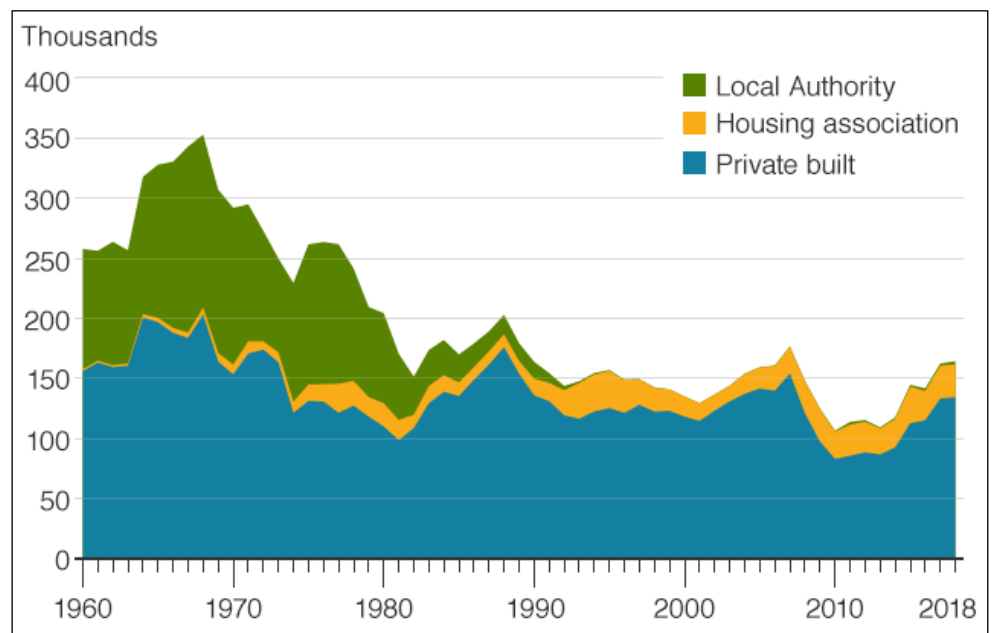
Chronic shortage of UK housing

Strategically, this **divisional reweighting makes perfect sense**, given the opportunities within the BtR industry. At the end of Sept'19, there were 148,046 such homes in the UK at varying stages of construction, up 19.8% from LY (source: British Property Federation) – & worth in aggregate c. £10.6bn.

However ultimately, [Savills reckon BtR](#) could tip £542bn - corresponding to 1.7m homes, or approx. 1/3rd of the country's private rented sector (PRS). The vast majority of which are owned by buy to let (BTL) landlords, who are being squeezed by tax hikes (eg stamp duty) and stricter building regulations.

Politically too there is cross-party support. The Conservatives' manifesto promised at least another 1m new homes over the next 5 years (target 300k/yr) – with BtR playing a central role. Not only alleviating the acute lack of rental properties, but also allowing people to move easily between jobs (re mobility), regenerating inner-city areas and upgrading dilapidated accommodation.

Chronic shortage of new homes being built in the UK

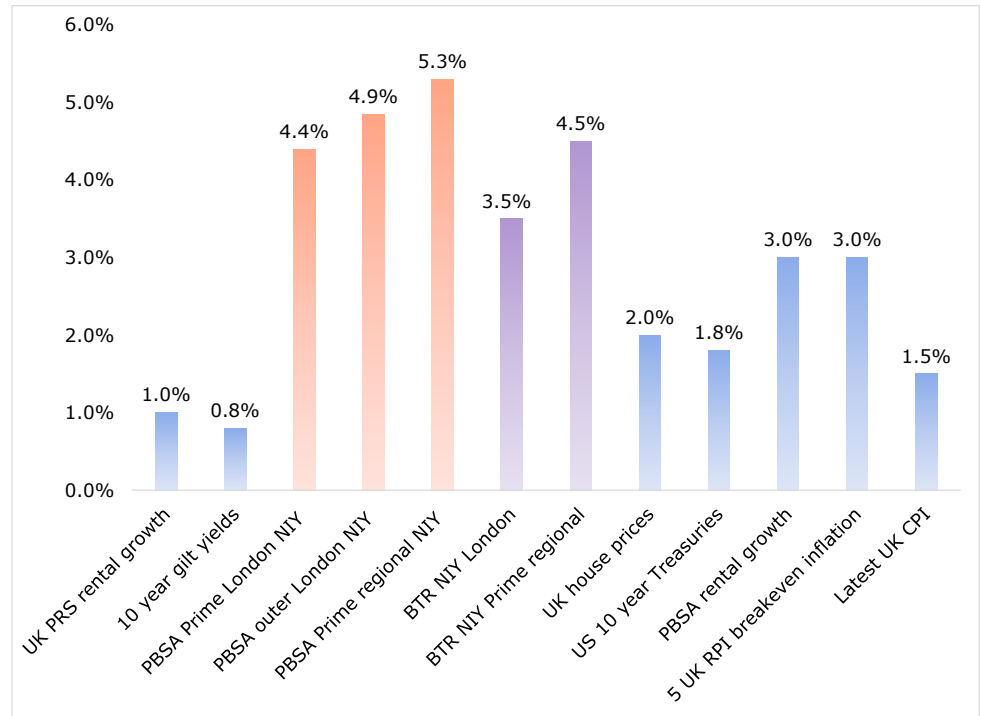


Source: BBC

Professional money still pouring into BtR & PBSA

Sure, net rental yields on prime BtR locations of 3.25% to 4.25% might not seem particularly rich. Yet equally, when compared to >\$10 trillion of negative yielding bonds, BtR churns out some of the best risk-adjusted returns available for property & income investors alike (see below).

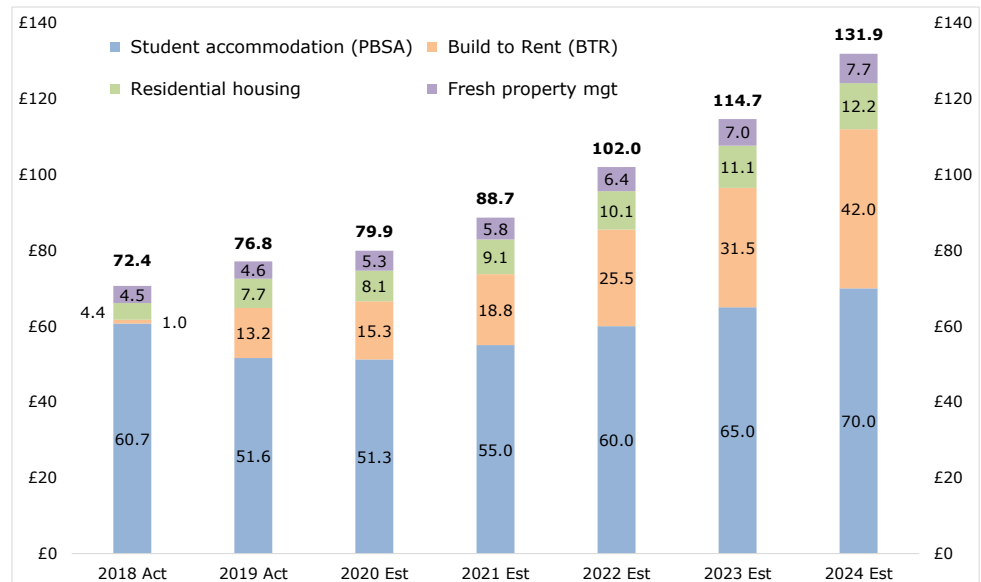
PBSA and BtR generating positive real-returns



Source: Various

So, while in the short term WJG’s EBIT margins are anticipated to remain flat (Est FY20 14.1%), we believe the **compelling fundamentals more than justify the BtR expansion** (see below).

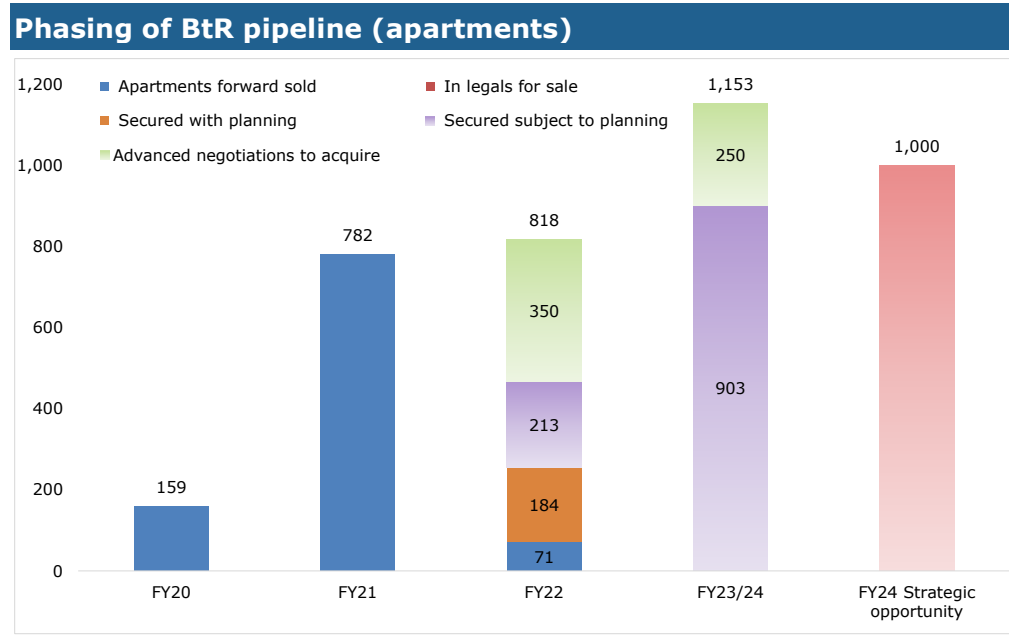
Divisional breakdown of gross profits (£m)



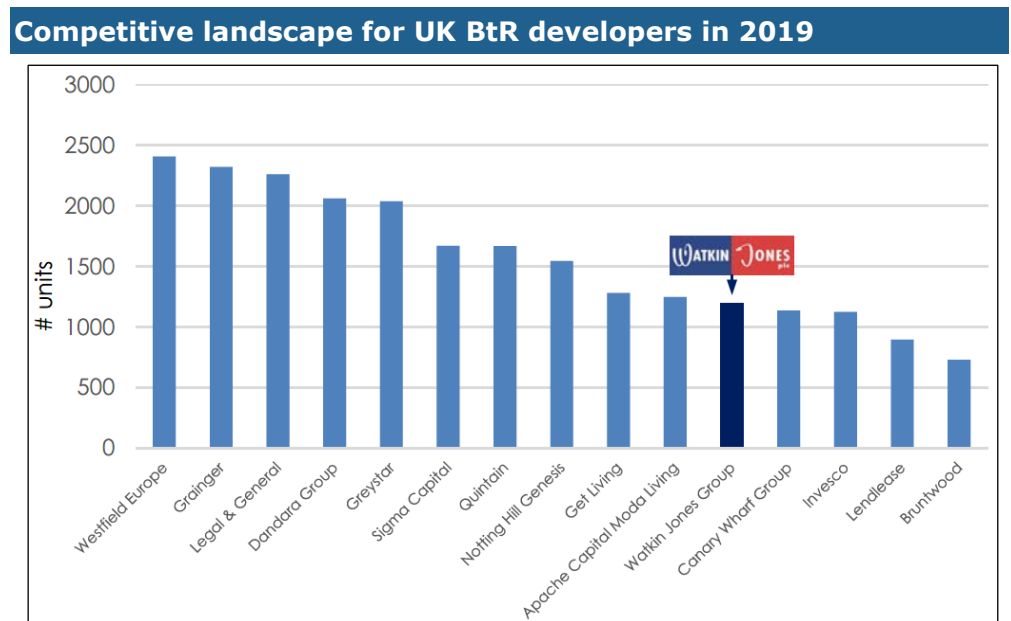
Source: Equity Development

Expanding BtR development pipeline

In fact as at the y/e, **the group had already secured** a large chunk of its portfolio (see below), sporting a pipeline of 9 schemes and 2,312 apartments - of which 1,012 units (5 sites) have been forward sold, and another 184 possess planning.



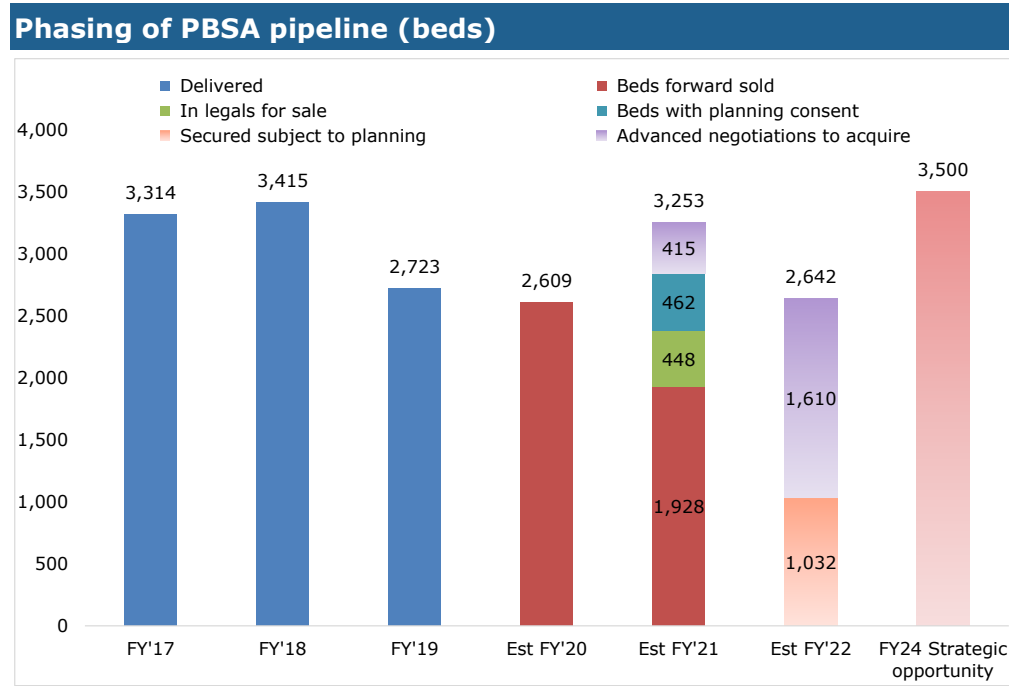
Source: Equity Development



Source: Company

Higher volumes & ASPs to drive PBSA profits

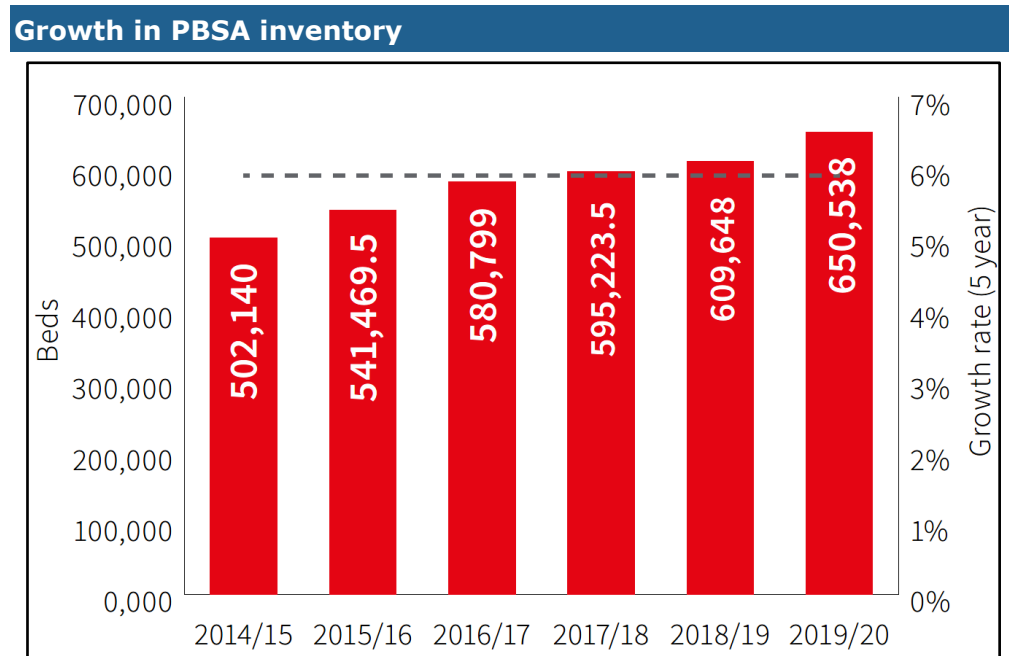
It's little different either in PBSA, **with 7 sites** (2,609 beds) **forward sold for FY20**, alongside another 4 in FY21 (1,928). The total y/e 'forward sold & secured' pipeline comprising 17 developments (6,670 beds), of which 13 (5,447) have planning consent (see below). Elsewhere, there are several other sites in advanced negotiation, which if satisfactorily concluded, would add a further 2025 beds.



Source: Company

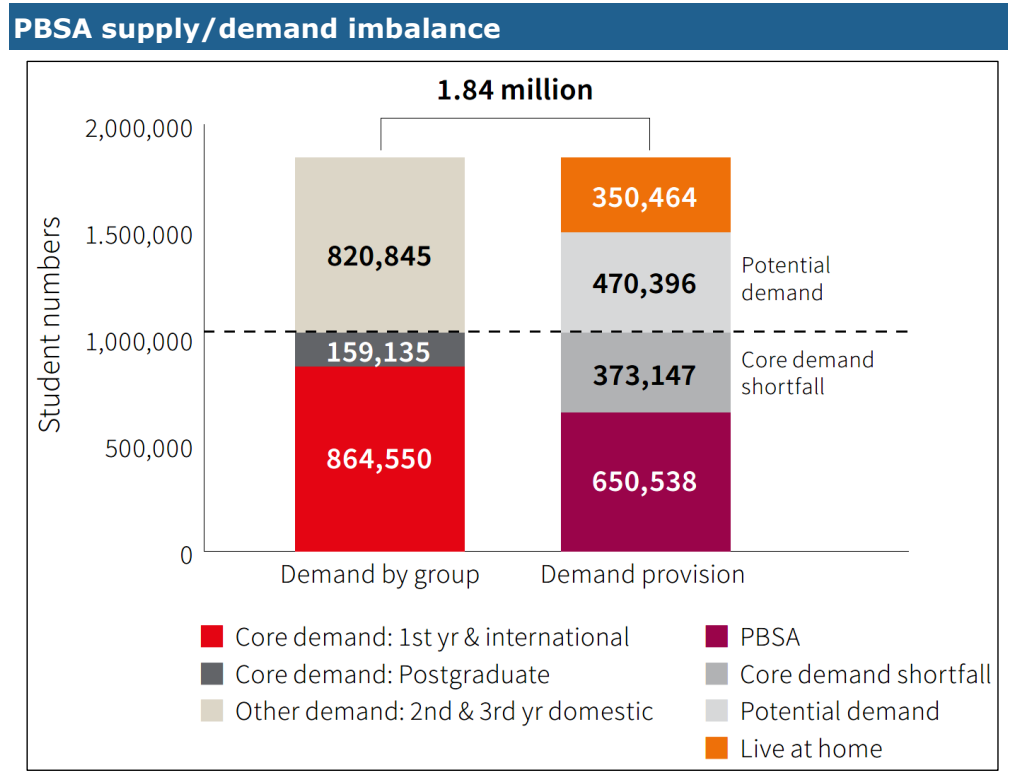
Solid long term growth prospects

Granted the PBSA sector has less run-way ahead than BtR, yet nonetheless it is still ticking along nicely (see below), with around 910k units projected by 2030, representing a 3.4% CAGR.



Source: Jones Lang LaSalle (Dec'19)

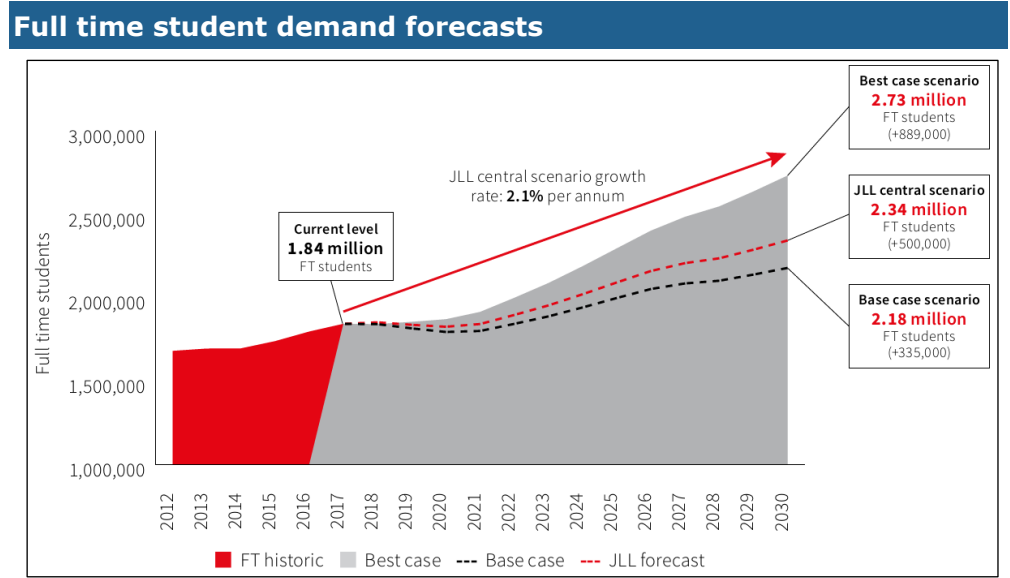
Moreover, there's a **significant demand vs supply imbalance**. For instance, there are only 650k PBSA beds (see above) - split 50:50 university vs corporately owned - compared to 1.1m full time students living away from home, and 864.6k 1st year undergraduates & international students.



Source: Jones Lang LaSalle (Dec'19)

University population set to rise 2.1% CAGR to 2030

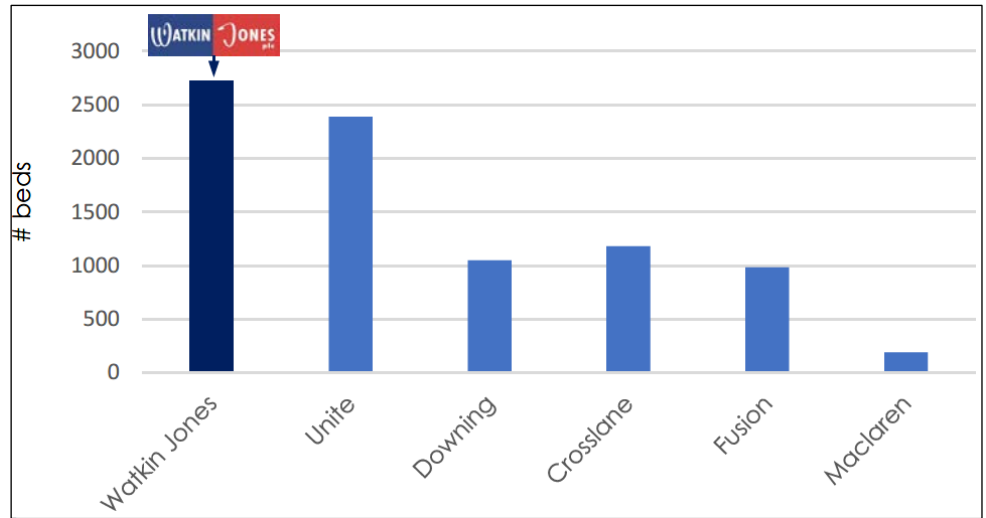
On top, Jones Lang LaSalle predict there will be a further 500k full time students by 2030 (see base case below) – mirroring a rise in 18-year olds from 2021, a moderate lift in participation rates and ongoing demand from overseas. Where the government aims to attract 600k international students by 2030 vs 458.5k in 2017/18 (+31%).



Source: Jones Lang LaSalle (Dec'19)

Elsewhere, there are **more people opting for post-graduate courses** (up >1/3rd in 10 years), alongside **many 2nd & 3rd year undergrads now choosing PBSA** in preference to traditional digs.

Competitive landscape for UK PBSA developers in 2019



Source: Company

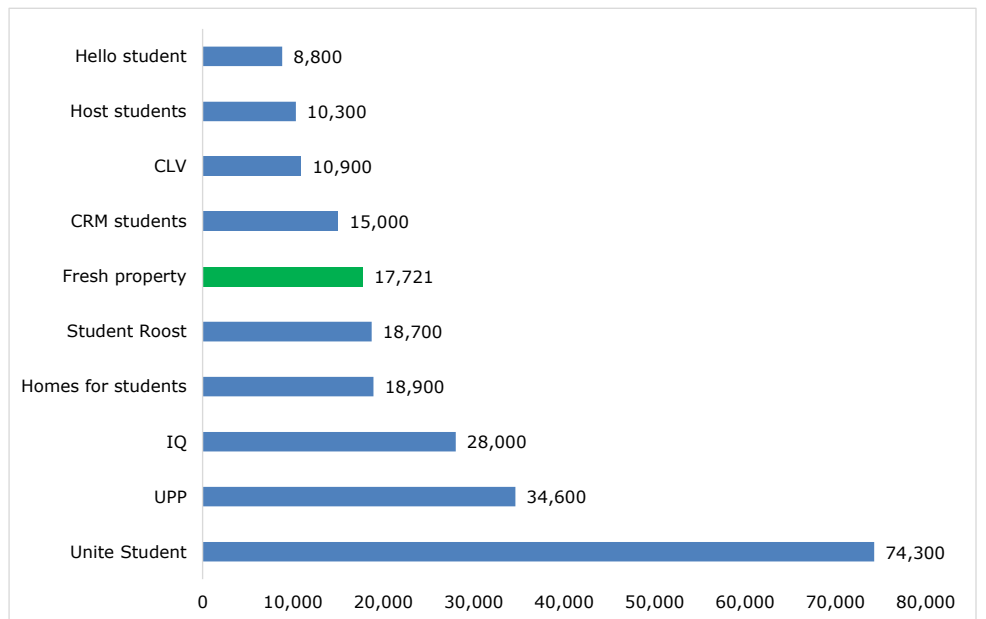
Momentum increasing too in Fresh & home building

Apart from these two growth engines, WJG also operates a successful house-building arm in the North West, which completed 150 sales in FY19 vs 175 LY.

And it's Fresh lettings business (gross margin 61.5%) continues to expand profitably - closing the year with 17,721 student beds (15,421 LY) and BTR apartments under management across 64 schemes (56 LY), of which around half were constructed by 3rd parties.

Further out Fresh has a contracted orderbook of 20,448 units across 66 schemes for FY22, underpinning its recurring revenues.

Top 10 UK PBSA operators



Source: Cushman & Wakefield

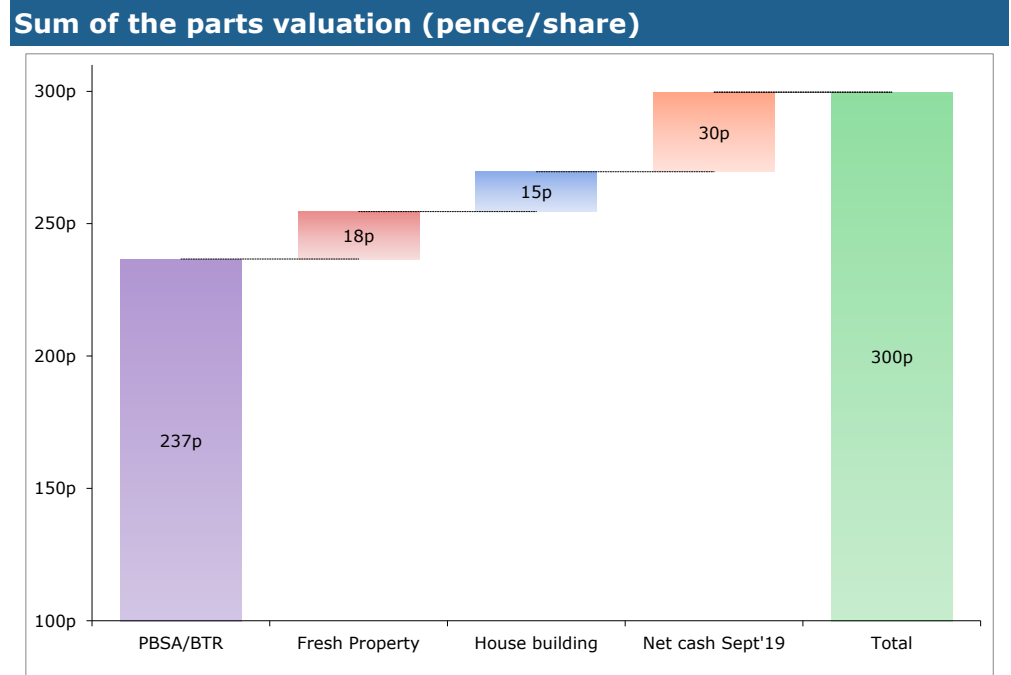
Trading in line with FY20 expectations

So what does this all mean? Well given its robust orderbook, capital-lite model (ie forward funded) and substantial visibility, we believe WJG is well **on track to hit our FY20 gross profit, EBIT and EPS estimates of £79.9m, £55.0m and 17.3p** respectively, together with **lifting the dividend to 8.7p** (3.6% yield). Similarly, there is **no change to the 300p/share valuation** (see below).

At 245p, the stock offers **an earnings yield of 8.2%** (ex cash), which is set to expand into the low double digits from FY22 onwards on the back of dependable earnings/cashflows.

Reiterate our 300p/share valuation

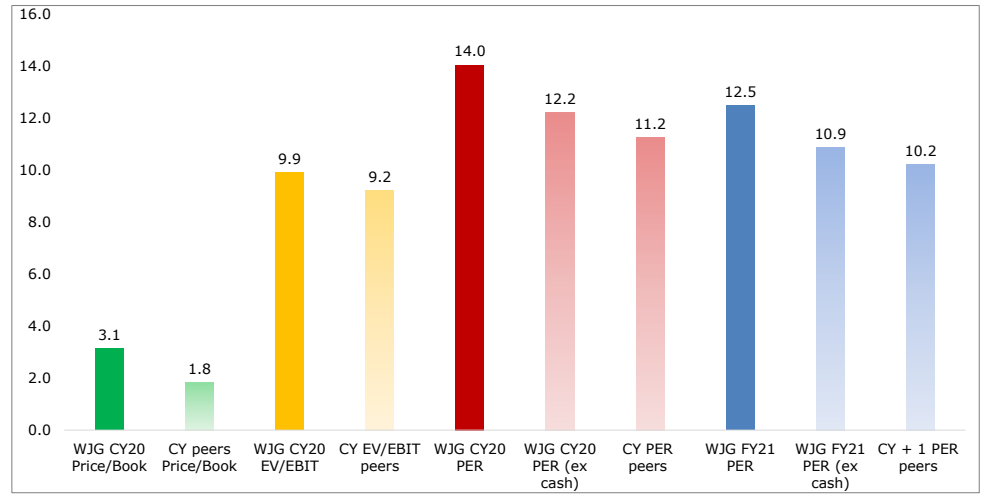
Admittedly the business may not be entirely immune to a recession – albeit equally, **demand for quality UK property remains healthy**, due to a chronic under supply, low unemployment, resilient consumer spend, benign interest rates, rising wages, modest inflation and competitive mortgages.



Source: Equity Development

Consequently, **we believe WJG should continue to trade at a deserved premium** to peers in light of superior cash generation, asset efficiency, sales visibility and risk profile.

Summary valuation benchmarks vs UK homebuilders



Source: Equity Development

Creation of sustainable shareholder value

CEO Richard Simpson commenting: *"We are pleased to report another year of growth for Watkin Jones, which demonstrates the **strength and resilience of our capital light business model**. Despite the difficult macro environment caused by Brexit-related uncertainty, **the Group has delivered further profitable growth, in line with expectations**.*

*Importantly, for the first time, **build to rent development made a significant contribution to the Group's results and we expect it to become an increasingly important growth driver in the coming years**. Watkin Jones is now firmly positioned as the UK's leading developer and manager of residential for rent schemes.*

***We are positive about the outlook for both the student accommodation and BtR sectors**. There is continued investor appetite in those markets and we are confident in our ability to expand our position as market leader. **We therefore expect to continue to grow the business, in line with our strategy, and believe that the Group has a bright future.**"*

Summary financial projections

Watkin Jones (continuing) (Sept yearend)	2015 Act £'ms	2016 Act £'ms	2017 Act £'ms	2018 Act £'ms	2019 Act £'ms	2020 Est £'ms	2021 Est £'ms	2022 Est £'ms	2023 Est £'ms	2024 Est £'ms
Turnover										
Student (PBSA) accommodation	228.2	237.2	256.1	312.7	246.1	250.0	275.0	300.0	325.0	350.0
Build to Rent (BTR)	0.0	0.0	1.2	3.8	73.6	90.0	125.0	170.0	210.0	280.0
Residential development	15.9	26.3	18.1	30.0	38.1	40.0	45.0	50.0	55.0	60.0
Fresh property management		2.8	6.1	7.3	7.5	8.6	9.4	10.4	11.4	12.6
Other / construction	0.2	0.7	20.4	9.3	9.5	0.0	0.0	0.0	0.0	0.0
Total	244.2	267.0	301.9	363.1	374.8	388.6	454.4	530.4	601.4	702.6
Group revenue growth % YoY	73.5%	9.3%	13.1%	20.3%	3.2%	3.7%	16.9%	16.7%	13.4%	16.8%
Student (PBSA) accommodation		3.9%	8.0%	22.1%	-21.3%	1.6%	10.0%	9.1%	8.3%	7.7%
Build to Rent (BTR)				209.5%	1856.5%	22.2%	38.9%	36.0%	23.5%	33.3%
Residential development	-12.6%	65.3%	-31.3%	65.8%	27.0%	5.1%	12.5%	11.1%	10.0%	9.1%
Fresh property management			116.6%	19.2%	2.2%	15.0%	10.0%	10.0%	10.0%	10.0%
Student (PBSA) accommodation	41.5	48.6	56.6	60.7	51.6	51.3	55.0	60.0	65.0	70.0
Build to Rent (BTR)	0.0	0.0	0.7	1.0	13.2	15.3	18.8	25.5	31.5	42.0
Residential housing	2.7	3.0	3.0	4.4	7.7	8.1	9.1	10.1	11.1	12.2
Fresh property management	0.0	1.7	3.8	4.5	4.6	5.3	5.8	6.4	7.0	7.7
Other	-0.1	0.5	-0.5	1.8	-0.3	0.0	0.0	0.0	0.0	0.0
Group gross profit	44.0	53.8	63.5	72.4	76.8	79.9	88.7	102.0	114.7	131.9
Group % margin	18.0%	20.2%	21.0%	20.0%	20.5%	20.6%	19.5%	19.2%	19.1%	18.8%
Student (PBSA) accommodation	18.2%	20.5%	22.1%	19.4%	21.0%	20.5%	20.0%	20.0%	20.0%	20.0%
Build to Rent (BTR)			56.3%	27.1%	18.0%	17.0%	15.0%	15.0%	15.0%	15.0%
Residential housing	16.6%	11.5%	3.8%	14.6%	20.3%	20.3%	20.3%	20.3%	20.3%	20.3%
Fresh property management		58.9%	49.4%	61.8%	61.5%	61.5%	61.5%	61.5%	61.5%	61.5%
Admin	-10.6	-14.6	-20.8	-22.8	-24.5	-25.0	-26.9	-28.9	-30.7	-33.0
Distribution / other	-1.0	-1.4	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Adjusted EBIT	32.5	37.9	42.7	49.6	52.3	55.0	61.8	73.1	84.0	98.8
% margin	13.3%	14.2%	14.1%	13.7%	14.0%	14.1%	13.6%	13.8%	14.0%	14.1%
EBITDA (incl JV profits)	33.6	41.5	45.2	50.9	53.7	56.4	63.3	74.6	85.6	100.5
% margin	13.8%	15.6%	15.0%	14.0%	14.3%	14.5%	13.9%	14.1%	14.2%	14.3%
Profit from JVs	1.2	3.0	1.4	1.1	0.3	0.0	0.0	0.0	0.0	0.0
Net interest	-0.7	-1.0	-0.9	-0.7	-0.3	-0.3	-0.3	-0.3	-0.3	-0.3
Adj profit before Tax	32.9	39.8	43.3	50.1	52.3	54.7	61.5	72.8	83.7	98.6
Effective tax rate	-19.1%	-20.5%	-17.3%	-18.6%	-18.5%	-19.0%	-19.0%	-19.0%	-19.0%	-19.0%
Adjusted EPS (pence)	10.4	12.4	14.0	16.0	16.7	17.3	19.5	23.0	26.5	31.2
EPS growth rate	138.5%	19.2%	13.1%	13.8%	4.6%	3.8%	12.4%	18.3%	14.9%	17.7%
Net assets per share (p)	44	40	49	60	69	77	87	99	112	127
Net tangible assets per share (p)	44	34	44	54	63	72	82	93	106	122
Dividend (p)		4.0	6.6	7.6	8.4	8.7	9.7	11.5	13.2	15.6
Valuation benchmarks										
P/E ratio	23.4	19.6	17.3	15.2	14.6	14.0	12.5	10.5	9.2	7.8
P/E ratio (excluding net cash)				13.3	12.7	12.2	10.9	9.2	8.0	6.8
Price/Tangible book	5.5	7.1	5.6	4.5	3.8	3.4	3.0	2.6	2.3	2.0
Price/Book	5.5	6.0	4.9	4.1	3.5	3.1	2.8	2.5	2.2	1.9
EV/EBIT	16.8	14.4	12.8	11.0	10.4	9.9	8.8	7.5	6.5	5.5
Return on Equity (y/e adj earnings/NA)	23.5%	30.8%	28.4%	26.6%	24.2%	22.4%	22.3%	23.4%	23.7%	24.5%
Dividend yield		1.6%	2.7%	3.1%	3.4%	3.6%	4.0%	4.7%	5.4%	6.4%
Net cash/(debt)	39.1	32.2	41.0	80.2	76.8	87.9	100.4	115.1	132.1	152.0
Net cash / share (p)	15.3	12.6	16.1	31.4	30.1	34.4	39.2	45.0	51.6	59.3
Sharecount (Ks)	255,269	255,269	255,269	255,269	255,382	255,822	255,922	256,022	256,122	256,222
Shareprice	243p									

Source: Equity Development

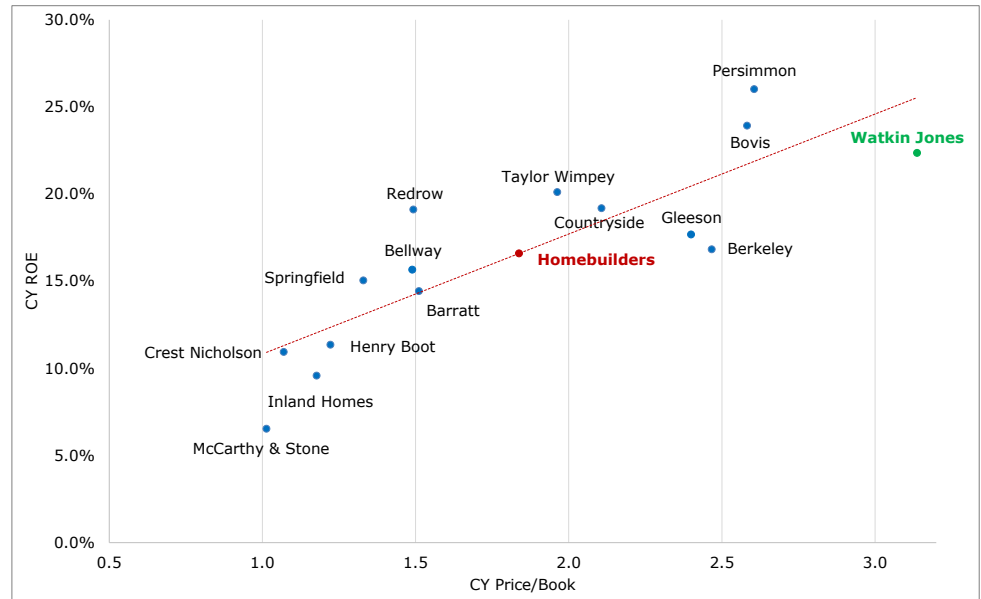
Note: FY19 exceptional charge of £2.6m relates to compensation to CEO for forfeited incentives held with former employer, £2.2m of which was a share based non-cash expense.

Key risks

- Impact of a substantial jump in UK interest rates and/or a recession. This seems unlikely though, given that even the most pessimistic economic forecasts are for >1.5% GDP growth through to 2022.
- Protracted delays in obtaining planning consent, which traditionally has plagued the whole sector.
- Foreign exchange fluctuations could impact demand from international investors, from say Singapore, Hong Kong and China.
- Future access to funding at commercial rates, perhaps in the unlikely event of another banking crisis.
- Generic risks of retention/recruitment of key staff, etc.
- Acquiring land at affordable rates. Availability of skilled labour and associated resources at desired cost levels.
- Withdrawal of government support for house-building (eg H2B, FTBs, stamp duty, etc).
- Brexit, and other possible legislative changes, say concerning building regulations, affordable housing, ground rents, etc
- Less demand from institutional money, if for example bond/gilt yields were to rise materially.

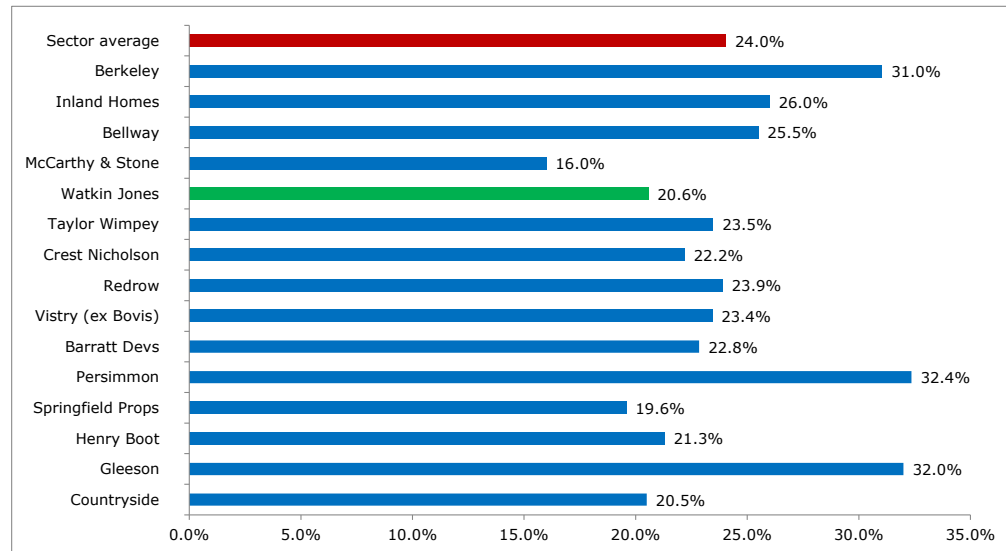
Appendices - Sector valuation metrics and KPIs

Return on Equity vs Price:Book valuation



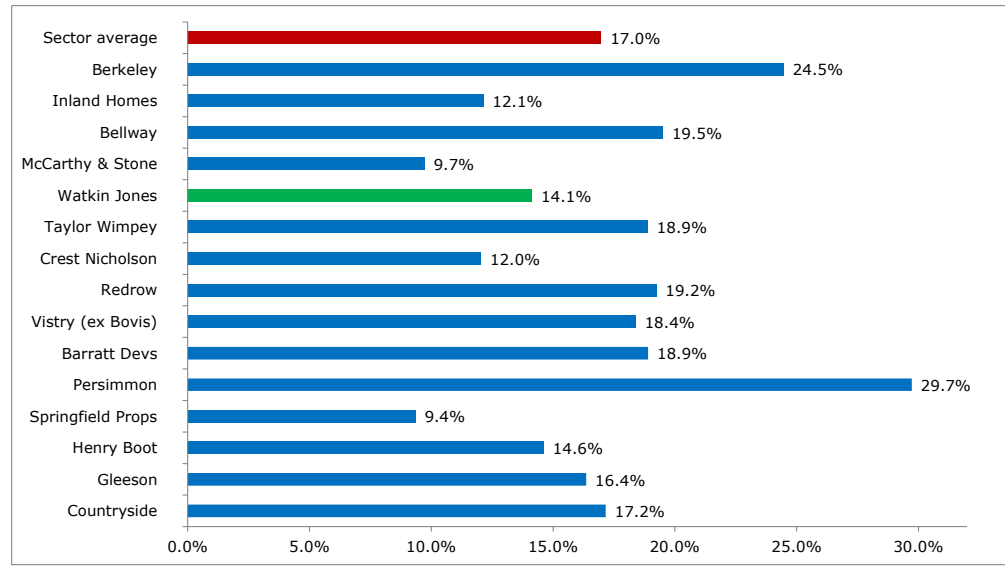
Source: Equity Development.

Current Year (CY) gross profit margins



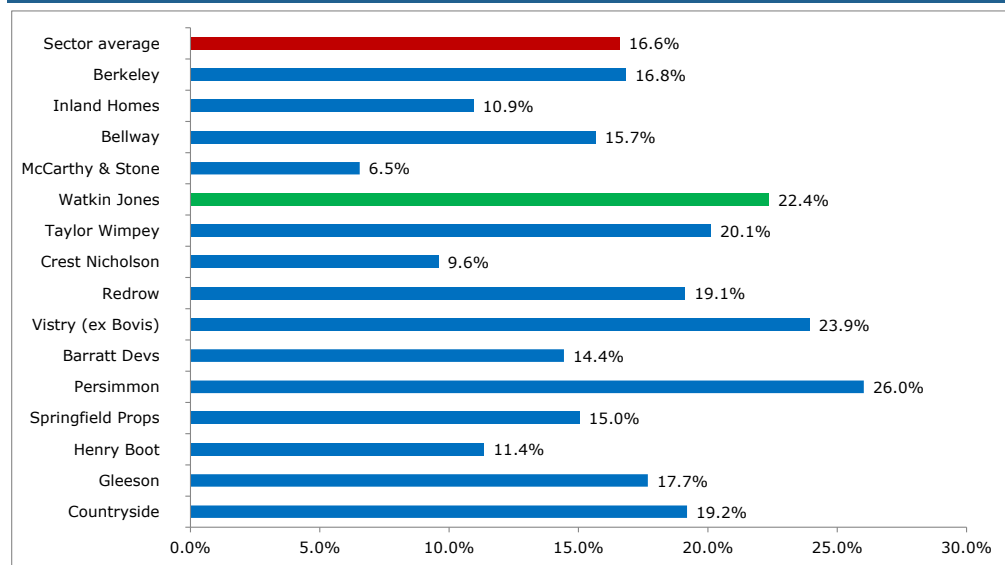
Source: Equity Development : arithmetic average for sector

CY EBIT margins



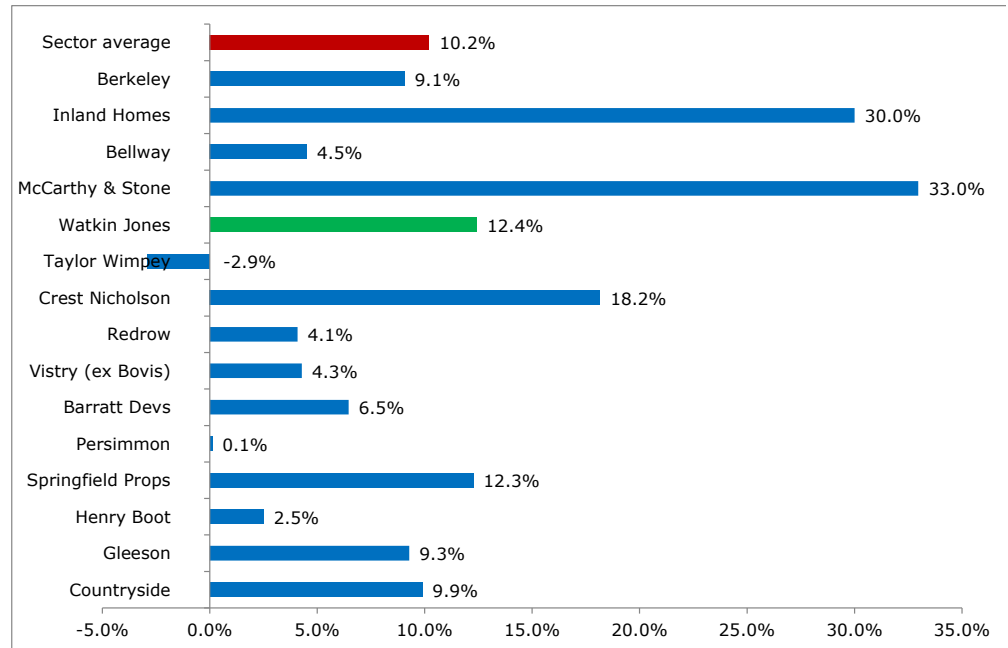
Source: Equity Development, arithmetic average for sector

CY ROE (cal'd from yearend Balance sheet)



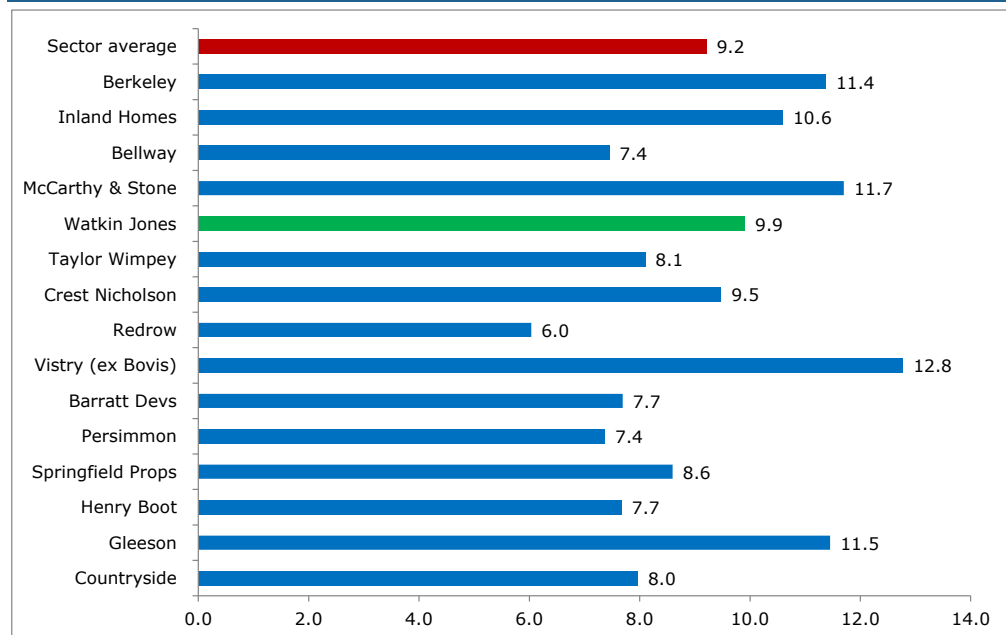
Source: Equity Development, arithmetic average for sector

CY + 1 EPS growth



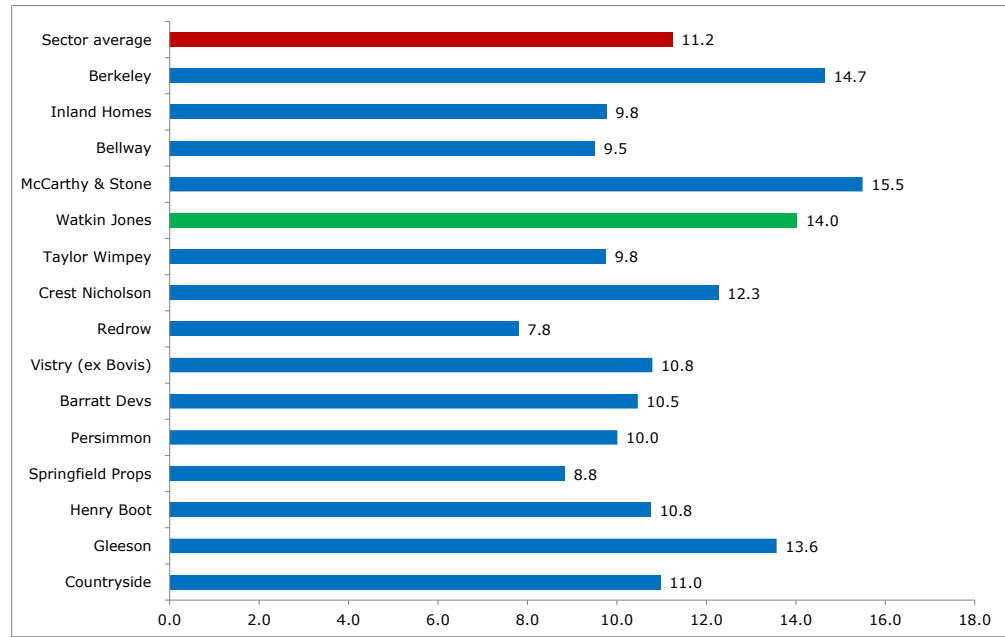
Source: Equity Development, arithmetic average for sector

CY EV/EBIT multiples vs peers



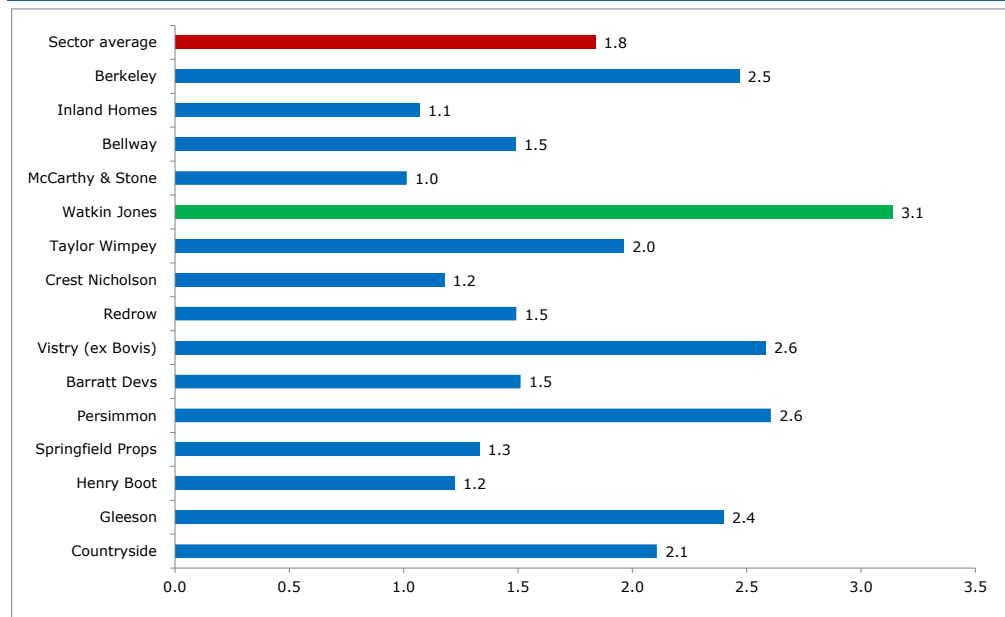
Source: Equity Development : arithmetic average for sector

CY PER multiples vs peers



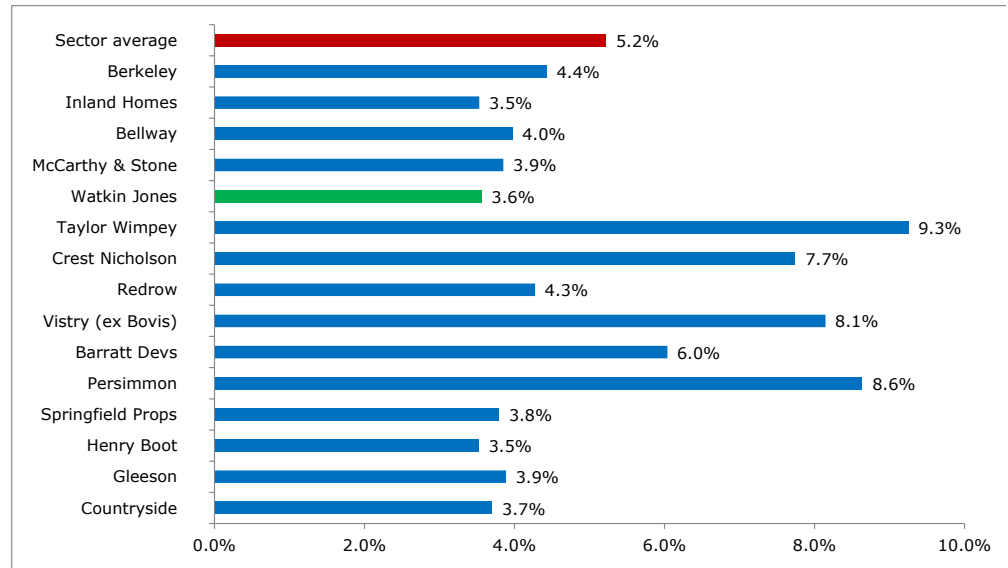
Source: Equity Development : arithmetic average for sector

CY Price : Book



Source: Equity Development, arithmetic average for sector

CY dividend yield vs peers



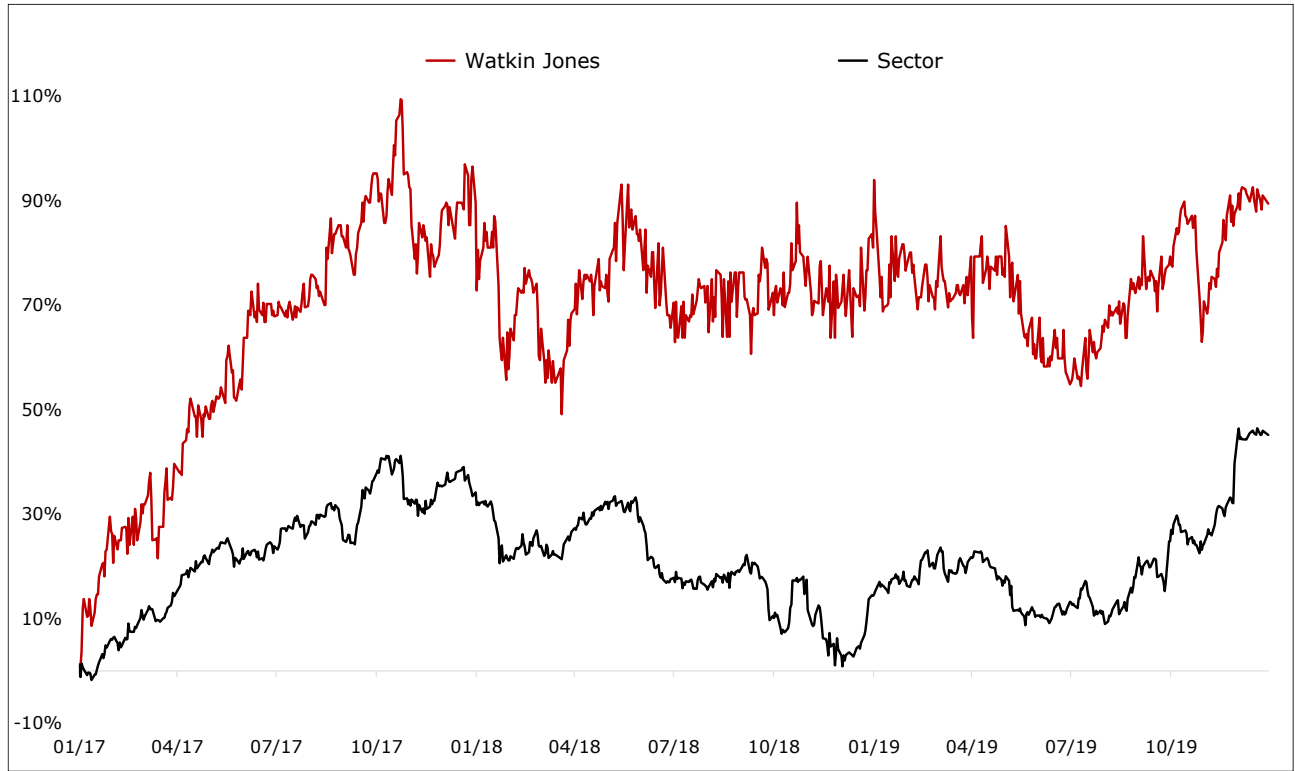
Source: Equity Development : arithmetic average for sector

Market Capitalisation of peers

	Shareprice	Mrk Cap (Millions)	CY net cash / (debt) Millions	Enterprise Value (Millions)
Countryside	475p	£2,138	£66	£2,072
Gleeson	965p	£528	£24	£504
Henry Boot	312p	£416	£15	£401
Springfield Props	137p	£132	-£42	£174
Persimmon	2,720p	£8,671	£1,021	£7,650
Barratt Devs	762p	£7,759	£690	£7,069
Vistry (ex Bovis)	1,310p	£2,825	£169	£2,656
Redrow	765p	£2,694	£124	£2,570
Crest Nicholson	426p	£1,095	-£33	£1,128
Taylor Wimpey	201p	£6,593	-£148	£6,741
Watkin Jones	243p	£621	£77	£545
McCarthy & Stone	141p	£760	£24	£736
Bellway	3,900p	£4,828	£172	£4,656
Inland Homes	85p	£177	-£100	£277
Berkeley	4,850p	£6,635	£960	£5,675

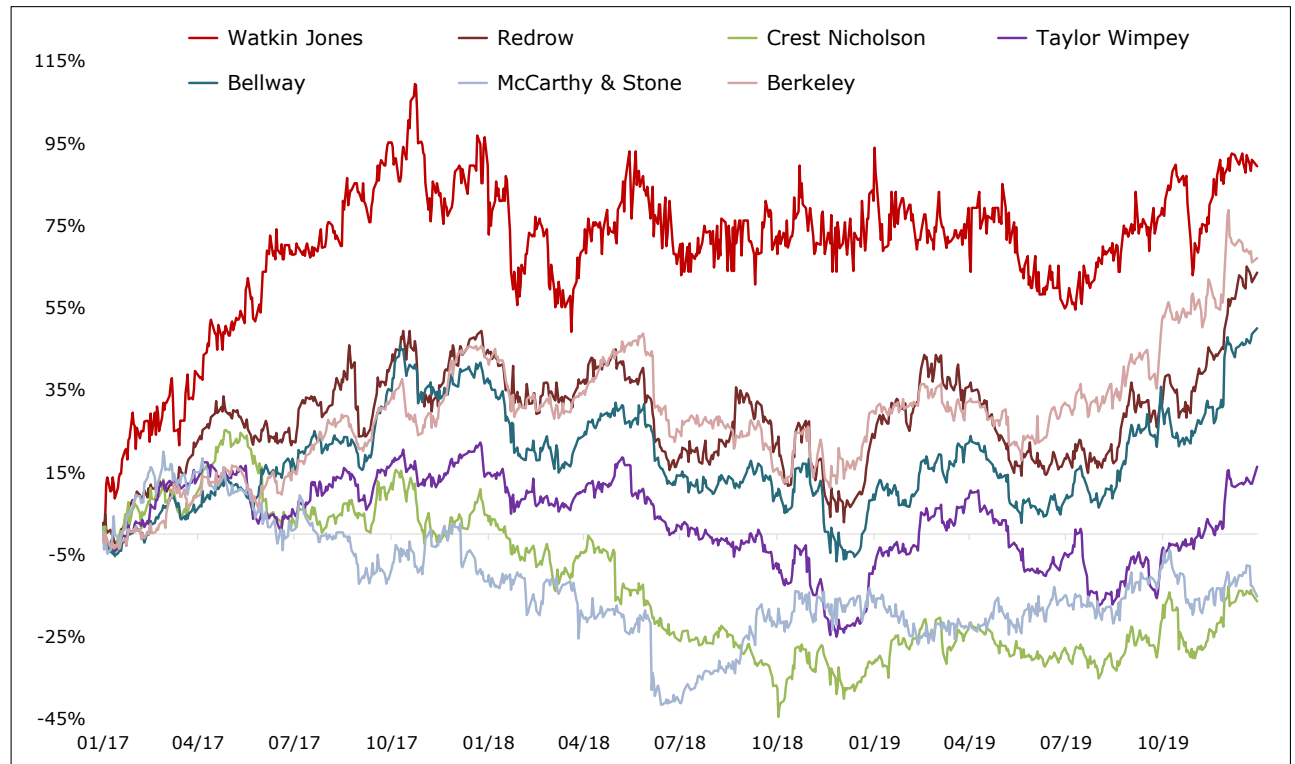
Source: Equity Development :

3 year shareprice movement vs house building sector



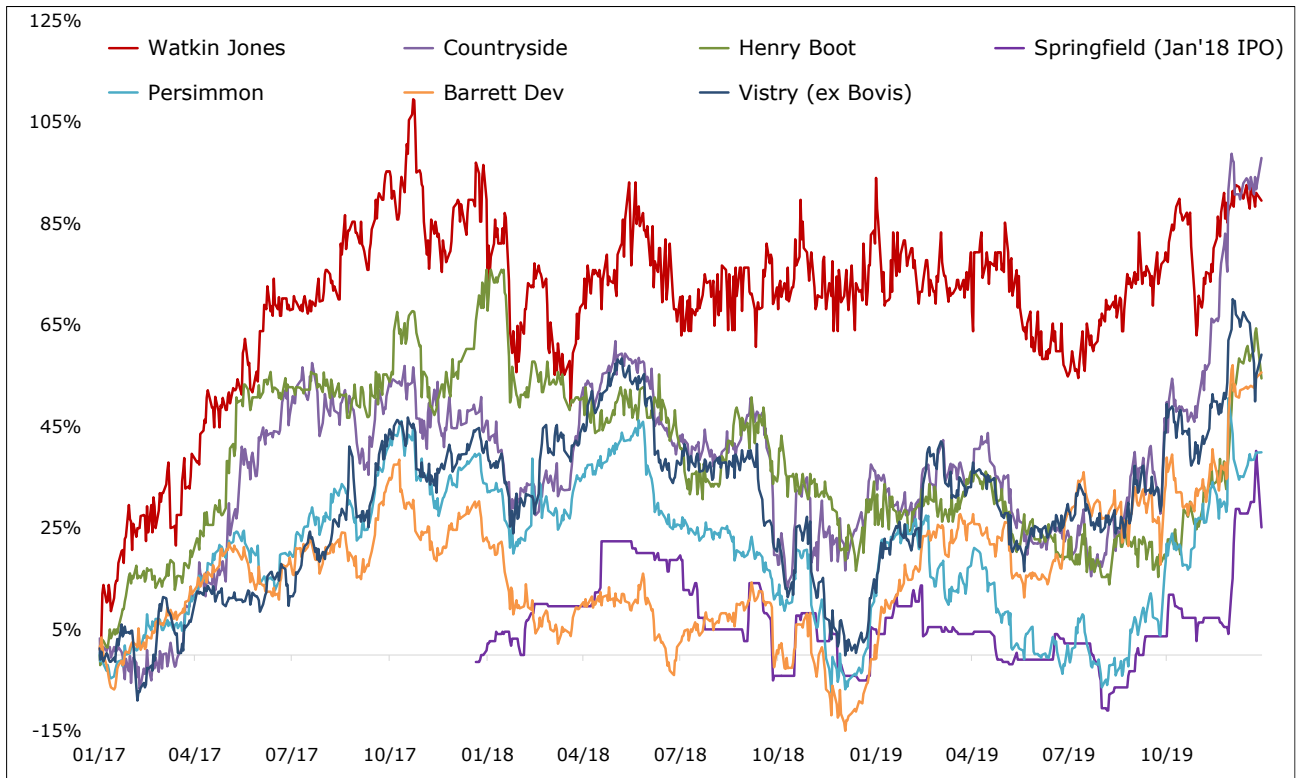
Source: Equity Development : arithmetic average for sector

3 year shareprice movement vs peers



Source: Equity Development : arithmetic average for sector

3 year shareprice movement vs peers



Source: Equity Development : arithmetic average for sector

Pipeline breakdown by sites

PBSA	Beds	Completion	Planning Status
Little Patrick Street, Belfast	430	2020	Granted
Forest Road, London	353	2020	Granted
Albion Way, London	283	2020	Granted
Whitefriars, Coventry	778	2020	Granted
Swansea	245	2020	Granted
Military Road, Canterbury	197	2020	Granted
Liverpool Road, Chester	323	2020	Granted
Kelaty, Wembley, London	599	2021	Granted
Cathedral Street, Glasgow	422	2021	Granted
Rockingham Street, Sheffield	691	2021	Granted
Dundee Street, Edinburgh	216	2021	Granted
Wilder Street, Bristol	348	2021	Granted
Bath Lane, Leicester	462	2021	Granted
Birmingham	608	2022	Pending
Exeter	154	2022	Pending
Edinburgh	270	2022	Pending
Bath	191	2022	Pending

BTR	Beds	Completion	Planning Status
Bournemouth	159	2020	Granted
Reading	315	2021	Granted
Wembley	301	2021	Granted
Sutton	166	2021	Granted
Leicester	184	2022	Granted
Sheffield	71	2022	Granted
Hove	213	2022	Pending
Woking	336	2023	Pending
Birmingham	567	2023	Pending

Source: Company



Investor Access

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