CCZ EQUITIES RESEARCH

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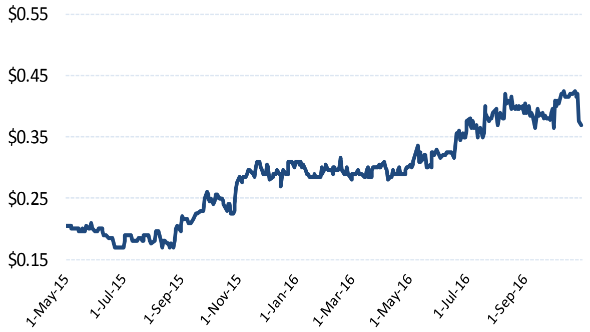
GALE Pacific(GAP): Several tailwinds to keep earnings sailing in the right direction

Share price: $0.37 Market cap: $110.1m Price target: $0.50 BUY Recommendation

Year end June	2015A	2016A	2017E	2018E	2019E
Sales ($m)	148.0	173.3	188.1	200.2	210.4
EBITDA ($m)	17.9	22.2	25.1	27.1	29.3
Adj NPAT ($m)	6.8	10.2	11.4	12.9	14.1
Adj EPS (cps)	2.3	3.4	3.8	4.3	4.7
EPS growth	(93%)	51%	11%	13%	9%
PER (x)	16.2	10.7	9.7	8.5	7.8
DPS (cps)	1.0	1.8	2.0	2.3	2.5
EV/EBITDA	7.1x	5.4x	4.4x	3.8x	3.1x
P/Cash Flow	25.4x	6.3x	5.8x	5.5x	4.9x



Gale Pacific is a manufacturer and distributor of a range of shade cloth, lining, glass and related products to the retail, vehicle storage, infrastructure, hotel and agricultural markets. The four brands are Coolaroo (shade cloth & sail related products), Everton (pool fencing), Zone Interiors (window furnishings & home wares) and Gale Pacific (commercial grain covers, waterproof liners, shade cloths & vehicle protection among others). The Coolaroo brand accounts for an estimated ~55% of FY16 group revenue, Gale Pacific is ~ 29%, Everton is ~9% and Zone ~7%. By area, Australasia is the core geographical segment accounting for 56% of FY16 revenues, followed by the Americas at 31% and MENA region at 9%. We estimate that 70% of group sales are generated via retail channels and 30% via commercial customers.

Coolaroo is a category leader, with an estimated 80% share of the outdoor sail/shelter shelf space in Bunnings. In FY16 Bunnings accounted for 36%/$62m+ sales to GAP. With products in 14 different aisles, the Australia/NZ operation has been a clear beneficiary of Bunnings 11% sales CAGR since FY11. **Closure of the Masters Hardware chain and positive Bunnings outlook implies continued medium term growth in the store footprint and sales volumes, putting a stiff breeze behind the Coolaroo brand.**

Gale Pacific leverages a manufacturing facility near Shanghai, China to produce 75% of products. The facility employs 450 staff and has been extensively upgraded to support product quality, increase flexibility and capacity. Management has opted to exit the manufacturing of some low volume/non-core product lines and outsource to 3rd parties. We see further opportunity to narrow the production line, reduce inventory lead times and improve EBITDA margins. **CCZ estimates that group EBITDA margins could improve by 1%-2% by FY19e through more efficient manufacturing processes.**

Gale Pacific is through a 2-year re-structuring program inclusive of management changes, reducing the core branded product lines from 14 down to 4 and rationalisation right through the supply chain. AGM outlook statement indicates a modest increase in revenue and profitability during first half FY17. **There is potential for a trade sale of the small but profitable Everton Glass business, which could recycle $6m-$10m of capital back into GAP**. Opportunity for bolt on acquisitions of complementary outdoor product ranges in Australia and the Americas is accentuated by existing sales channels and a strong balance sheet. CCZ estimates that GAP trades on a free cash yield of 12% in FY17e. **FY17e P/E of 9.7x is a significant discount to the peer group 17.1x.** Initiate coverage with a BUY recommendation and $0.50 price target.

Investment Case: 6 reasons why we are buyers of GAP

Alignment with the Bunnings/Coolaroo growth outlook

Bunnings represents 36% or $62.4m of group revenues in FY16. Bunnings sales CAGR between FY11 and FY16 has been 11%. Gale Pacific's retail product mix has been a clear beneficiary of Bunnings in-store execution, new store openings and capacity to hold market share. We understand that GAP has zero product coverage in Masters. CCZ site visit identified 14 separate Bunnings isles stocking Coolaroo, Zone, Everton products. Coolaroo has an estimated ~80% exclusivity over the outdoor shade and sail isle. Leverage to Bunnings track record of ~20 new store openings per annum, expansion into UK & Ireland and dominant market share supports the quality of GAP revenue streams. Closure of the Masters chain is likely to have created some short term pressure on discounting and inventory overhang. We believe that this effect will have likely cycled out by the January 2017.

Supply chain improvements delivering margin upside to core selling regions

The main manufacturing base is in Beilun, China supplying ~75% of the products sold (by revenue) across the GAP brands. Product lines include commercial shade fabrics knitted in China, manufacturing of Scrim fabrics prior to waterproofing in Australia. The Chinese facility is wholly owned and the company continues to invest in manufacturing efficiency and capacity. Employing 450 staff, the labour intensive facility can be improved further to reduce inventory lead times, reduce variable costs and provide better support to selling regions.

The transition to one global Microsoft Dynamics IT platform has taken place already with the exception of China. Another ~$1m needs to be spent integrating this into China during FY17-FY18. We believe this will bring closer alignment between each selling region and the manufacturing hub, ultimately improving margins in Australia/NZ, MENA and the Americas. Inventory carrying value was $44m at FY16. Group EBITDA improvement of 1%-2% is possible by FY19 with a more efficient supply chain. Current forecasts include 0.6% margin expansion between FY16 and FY19.

Gale Pacific are through a 2-year re-structuring process under MD Nick Pritchard – top line and margin upside is still being realised.

The strategy has entailed reducing the number of brands to 4 (from 14), simplifying the product range to focus on profitable segments, geographic rationalisation and closer alignment of each selling regions. Recent management changes in the Americas and group supply chain are consistent with the new strategic direction.

In Australia, warehouses have been consolidated while in the Americas the company continues to evaluate future manufacturing and warehousing options. The company has put in place incentives for the top 20 executives. Metrics include EBIT and cash conversion as the STI benchmark while EPS improvement remains as the LTI target.

Offshore market growth in USA/MENA driven by the Coolaroo and Commercial products.

Coolaroo is a dominant category player in the outdoor sail and coverage market. A big driver of Australian residential and commercial sales has been the adoption of overhead sun shelters in schools, public playgrounds and homes. There is a prevailing view that this dynamic has not fully played out in the USA, supporting a strong forward pipeline. The Coolaroo product is well represented in big box home and hardware stores and clubs including Wal-Mart, Lowe's and Home Depot. Representation to date has been a small share of the Southern States. We see 4%-5%+ sales growth in the US residential category.

Possibility to sell smaller, non-core brand?

There is potential for management to assess options relating to a trade sale of the non-core glass business Everton. Everton was acquired in 2013 for just under $4m, has a goodwill carrying value of ~$3m and in FY16 generated estimated revenues of ~$16m. Sale price of $6m-$10m, would release funding back into the GAP business for distribution to shareholders or alternatively to support the balance sheet. We see GAP's potential for acquisitions in Australia or other geographies that can better leverage the Asian manufacturing/local distribution model, more specifically acquisitions focussed on the higher margin commercial segment.

GAP's commercial product range represents ~30% of the group revenue mix and has generally higher margins than residential channels.

Average commercial EBITDA margins are ~15% on CCZ expectations. Levels of customisation are higher and the requirement for product innovation creates a barrier to entry. GAP have historically maintained a healthy R&D budget and established partnerships with technical bodies including Deakin University to manufacture grain covers from recycled materials. Launch of the Commercial Heavy 430 sail product is another example of innovation. Greater compliance, insurance and safety requirements in industries from vehicle storage to horticulture to construction have created a backdrop conducive to top line commercial growth in FY17-FY19.

Growing the commercial footprint is a clear focus of management in Australia, Americas and MENA. Commercial services customers directly and through distributors. Combined with supportive industry conditions – ABARE crop upgrades, regional irrigation and infrastructure spending, school/public space sun safety – we see the commercial segment as a significant driver of earnings forecasts in FY17e.

Company Overview

Gale Pacific manufactures and distributes a range of shade cloth, industrial lining, glass and related products to the retail, construction, hotel and agricultural markets. The four brands are Coolaroo (shade clothe and sales), Everton (fencing and screens), Zone Interiors (window furnishings and home wares) and Gale Pacific (commercial grain covers, waterproof liners, shade cloth and vehicle protection).

Four key brands in the portfolio

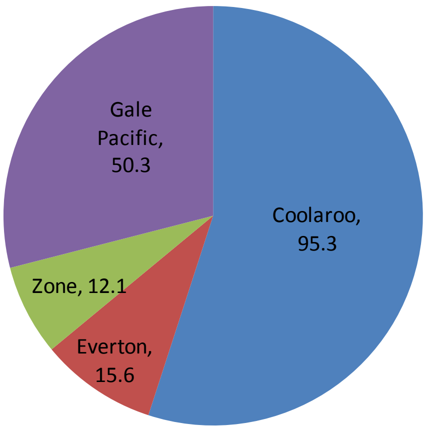
Source: Company reports

CCZ estimates that the Coolaroo brand accounts for ~55% of FY16 revenue, Gale Pacific ~29%, Zone ~7% and Everton ~9%. Australia and New Zealand is the main geographical segment accounting for 56% of FY16 revenues, followed by the Americas (USA) at 31%. An estimated 70% of sales are generated by residential product lines and 30% are generated by commercial markets.

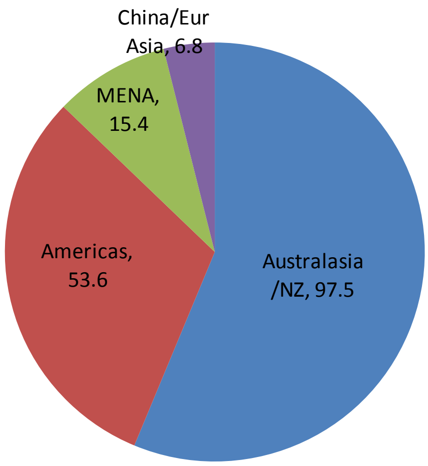
The company is headquartered in Braeside, Victoria, where it runs the only manufacturing plant in the southern hemisphere producing three-layer, single-pass process fabrics. A distribution facility co-exists 20 minutes away in Dandenong.

Gale Pacific employs over 600 staff, including 140 people throughout Australia and New Zealand and 6 staff in Dubai selling into the Middle East North Africa segment. The EurAsia sales office is run out of Shanghai with the global manufacturing facility located nearby in Beilun. Combined, the Shanghai and Beilun facilities employ ~460 staff. USA facilities include 45 employees with head office and small scale manufacturing in Orlando and a small scale manufacturing facility and distribution point in California.

FY16 revenue by brand $m



FY16 revenue by geography $m



Source: CCZ Equities, Company reports

Core customers in all geographies

Source: Company reports

Product Lines

Coolaroo: CCZ estimates $95.3m FY16 revenues, 100% residential

Brand summary: Coolaroo is the prominent Australian brand in shade related products servicing residential segments – entertaining areas, portable shades and garden spaces. The residential market is the main sales channel and Australia is the biggest sales market. Coolaroo is also available worldwide.

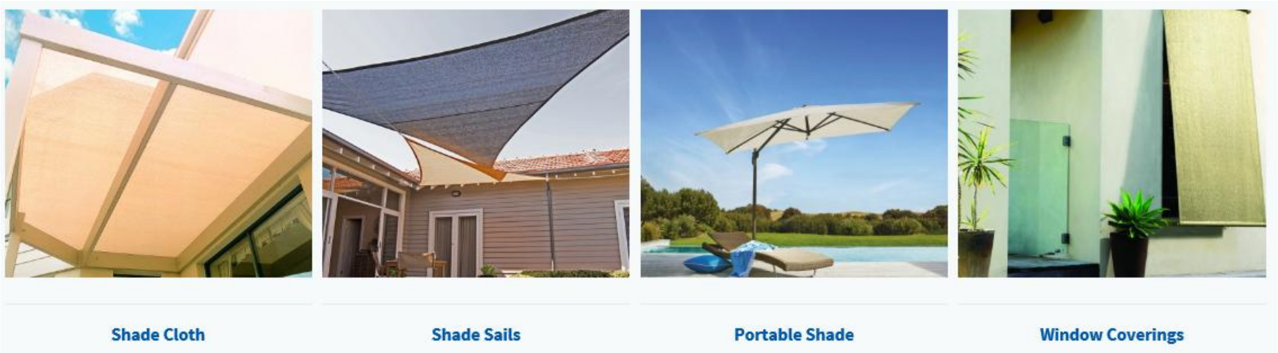
Core sales channels: Exist throughout Australia, New Zealand and the USA. Hardware chains Bunnings (240 stores), Mitre 10 (300 stores), Home Hardware (350 stores), Thrifty Link (130 stores), and Stratco (55 stores) – amongst others – represent the core retail distribution channels in Australia. Most Bunnings stores include a full aisle comprising Coolaroo products. Offshore distribution points include home centres (Lowe's, Home depot, Wal-Mart), clubs (Sam's, Costco) as well as online distribution (Amazon, Blinds.com). The home centres and clubs operate across 4,000+ locations in the USA – although Coolaroo products are only represented in a small subset currently. Domestic market share ~50% residential.

Product Mix: Estimated ~40 different products. Category leader in Sails.

Main competition: Domestic product brands Shelta, Marquee and Private Label. US retailers selling house brands at a 10% discount to Coolaroo products.

CCZ sustainable growth expectations: Domestic revenue growth GDP +1%-2% premium for trend towards sun safety for residential customers (entertainment areas and playgrounds). Sensitivities include discretionary spending, Bunnings stores openings, excess Masters inventory clearing, renovation market and trend towards sun safety in residential environments.

Coolaroo residential outdoor shade and sail related products



Source: Company materials

Gale Pacific: CCZ estimates $50.3m FY16 revenues, 100% commercial

Brand summary: Gale Pacific is the main commercial brand providing a variety of tailored products and solutions including architectural and horticultural shade, construction and mining fabrics and products for schools, parks and office developments. Examples include grain and hay covers, vehicle or vegetable shade cloth, shopping centre commercial sails, cricket pitch covers, irrigation and dam liners and fabrics for mining and military/government organisations.

Competitive advantage centres on manufacturing capability, capacity to provide tailor made products on a large scale and R&D initiatives to improve the product set. Examples of product innovation include the partnership with Deakin University to develop grain covers from recycled materials.

Core sales channels: Exist throughout Australia, NZ, MENA, USA (small base). Domestic involves direct to commercial customers and via distributors including Bartlett, Darling Downs Tarpaulins, Blackwoods and Visy while offshore customers include Leeds Trading LLC (MENA) and USA Shade (USA).

Product Mix: Estimated ~80 different product varieties. Category leaders in grain covers and industrial shade cloth.

Main competition: Fragmented offshore markets, Korean and Chinese based manufacturers and imported scrim and knitted cloth products

CCZ sustainable growth expectations: 3%-5% + premium for offshore sales growth based on recent management changes and progress in generating supply chain efficiencies. Sensitivities include the size of the Eastern Australian grain harvest and fresh product production, increased rates of shade clothe installation over vehicle and produce sites, construction, military and mining activity.

Gale Pacific commercial outdoor products

Source: Company materials

Everton: CCZ estimates $15.6m FY16 revenues, 100% commercial

Brand Summary: Everton is available in Australia and New Zealand as it is offered exclusively to Bunnings throughout their 240 retail store network. The products include pool fencing systems, balustrade systems, mirrors, shower screens and splashbacks. Everton glass products hold the classification as “Grade A Toughened Safety Glass”.

Core sales channels: Australia and New Zealand.

Product Mix: Estimated ~70 different product varieties. Category leader in pool fencing.

Main competition: Fragmented markets, highly competitive in commercial and residential brands include Highgrove and Mondella. Dominant position in core Bunnings product lines pool fences, glass accessories and less dominant in shower screen and splashback.

CCZ sustainable growth rate: GDP/retail sales linked, difficult to add a premium to market growth rate.

Everton residential glass and pool related product range

Source: Company materials

Zone Interiors: $12.1m FY16 revenues, 100% residential

Brand Summary: The Zone Interiors retail product line is provided through Bunnings, Mitre 10, Home Timber and Hardware and other independent retailers. The brand consists of window furnishings that include blinds and curtain accessories with some offered as Do It Yourself (DIY) solutions for consumers.

Core sales channels: Australia and New Zealand.

Product Mix: Estimated ~70 different product varieties. Category leader in residential blinds.

Main competition: Fragmented market and Smart and Gummerson brands.

CCZ sustainable growth rate: GDP/retail sales linked, difficult to establish a critical point of difference or add a premium to market growth rate.

Zone residential blind product range

Source: Company materials

Key geographical markets

Market	*Australia/NZ*	*Americas (USA)*	*MENA*	*EurAsia*
Revenue Share FY16	56% - $97.5m	31% - $53.6m	9% - $15.4m	4% - $6.8m
Headcount	140	45	6	460
Core segment	Retail - 70%	Retail - 90%	Commercial - 97%	Retail - 85%
Main Distribution Point	Dandenong distribution , Braeside manufacturing	Los Angeles manufacturing and distribution, Orlando head office and manufacturing	Dubai - UAE	Shanghai sales office, Beilun production facility - China
Main Sales Channels	hardware stores, distributors, direct	Hardware, home centres, clubs, online	Commercial organisations	Manufacturing hub
Core Brand	Coolaroo and Gale Pacific	Coolaroo	Gale Pacific	Coolaroo
Point of Difference	Dominant market share in Coolaroo shade products, customised commercial	Coolaroo brand, (albeit modest starting base)	Commercially Tailored fabrics wide range	Manufacturing facility reduces cost to produce globally
Sensitivities	grain and horticulture, construction, infrastructure, mining	Supply chain management, retail	Regional growth, oil prices	Producing cheaper
Catalysts	Commercial growth, hot weather	Increase brand recognition and commercial footprint	Property cycle	Manufacturing efficiency

Source: CCZ Equities

GAP Timeline from 2008-2016

May 2008 – Restructure and turnaround strategy completed consisting of transferring products to China, implementing retail distribution channels in the US and Europe, implementing a uniform IT system across the company and restructuring the MENA and European businesses

February 2009 – $5m rights issue to replenish working capital requirements and pay down debt

June 2011 – Acquired Zone Hardware and Riva Window Fashions to expand product offering

July 2012 – Upgrade profit guidance to advise record earnings will be achieved

November 2012 – Acquisition of Highgrove (a specialist in home improvement products) for $3.9m.

July 2013 – Riva Window Furnishings was sold for an undisclosed amount after proving to contain a difficult business model and generating operating losses

May 2014 – Peter Landos joins as a Non-Executive Director

August 2014 – Nick Pritchard is appointed to the role of CEO

August 2014 – New strategic plan initiated under Nick Pritchard to exit non-core products and markets

April 2015 – Matt Parker appointed as CFO

June 2015 – Commissioned new operating system and scanning technology in Australia's extrusion coating plant and reduced core brands from 14 to 5

October 2015 – Outlook guidance upgraded for 1H16 NPAT to $2.75m - $3.25m from $0.70m pcp

May 2016 – Implementation of Chinese manufacturing transformation by Cliff Xin-Hua Zhang

March 2016 – Craig Fuller appointed to manage the Australia/New Zealand operations

June 2016 – Lindsay Klebenow appointed to manage the Americas operation

Australia/NZ: Driving the Coolaroo brand, expand commercial channels

Facilities: The main site is the wholly owned extrusion coating plant in Braeside, Victoria. Primary purpose is coating of fabric and paper with resin, forming the basis of water proof tarpaulins, covers and cardboard boxes. The leased retail product distribution centre in Dandenong, Victoria services the distribution of products to customers. Smaller scale facilities in Queensland and Perth for warehousing purposes.

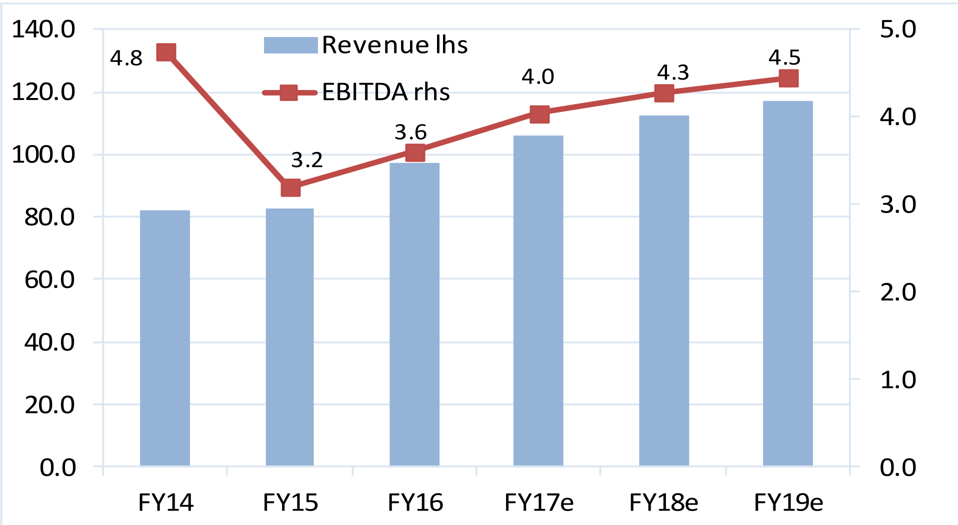
Operational position: The Australian operation has undergone a transformation since FY14, including asset sales and focusing on core residential products with a competitive advantage and high margin commercial categories. We expect the focus on Coolaroo and commercial channels to continue over the forecast period.

Product innovation: Customisation of the product mix is required for many customers and product development is constantly evolving. The Gale Pacific/Deakin University research and development partnership provides an innovative platform that has already provided returns with the development of technology that creates fabric made from recycled grain covers solving the ‘end of life’ disposal issue for grain handlers (technology is pending patent in Australia).

Growth outlook: ~9% revenue growth in FY17, driven by Commercial and Coolaroo.

Margin outlook: Reported EBITDA margins likely to remain stable ~3.8% (before allowing for China manufacturing margin distribution). Resin prices are sitting around 5 year lows with upside risk while product lines have been reduced to focus on higher margin categories.

Australia/NZ product line re-structuring, self help done, back on track



Source: Company reports

Americas: Expanding shelf space, management re-shuffle, reduce inventory times

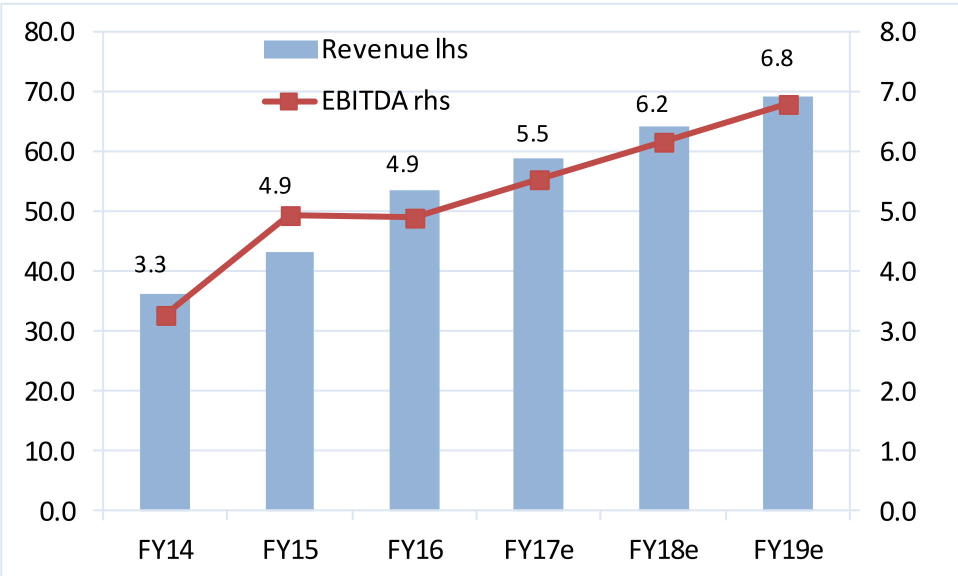
Facilities: Include a small customer window share manufacturing line and warehouse in Los Angeles, California and the head office and small scale custom window share manufacturing facility warehouse in Orlando, Florida. Both facilities are mainly fed with products from the Chinese manufacturing facility for distribution into local retail channels while the commercial sector is serviced out of California. An evaluation of future manufacturing and warehousing options has commenced and there is potential to consolidate the USA operations into a single facility.

Operational Position: The Coolaroo product is represented in many of the main stream hardware home centres, albeit only in a small scale in US channels thus far. Other sales channels include hardware clubs (Sam's and Costco) as well as online distribution (Amazon and Blinds.com among others). Recent management change appointed Lindsay Klebenow as General Manager. We see the growth opportunity in expanding the residential channel footprint in the Southern States, increasing shelf space, plus increased investment into commercial channels. Medium term potential is for a similar Australian 60/40 residential/commercial split.

Growth outlook: ~10% revenue growth in FY17, driven by expansion of shelf space, benefits of recent re-structuring and anticipated growth in the commercial.

Margin outlook: Reported EBITDA margins ~9% can expand by up to 2% over the medium term with operating leverage and most importantly the capacity to get product to customers faster.

Americas: Management changes; wider distribution points is the focus



Source: Company reports

MENA: Building the commercial footprint

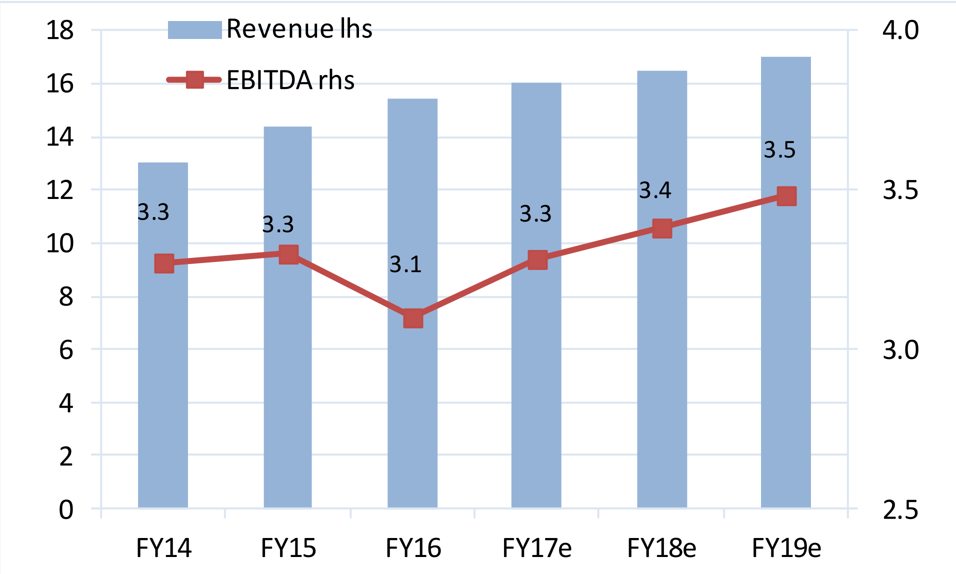
Facilities: The MENA operations are run out of a warehouse and office in Dubai, UAE and serviced almost entirely with commercial products under the Gale Pacific Brands. General Manager Ali Haidar has managed the local operation for 12 years.

Operational position: Sail product mix consist of core established product categories being schools, hotels, outdoor areas and shade cloth materials for vehicle storage. Growth is sensitive to buying behaviour in core property, government and wholesale customers for example Leeds Trading. Demand is driven by the property market and thus partly correlated with oil prices and regional sentiment. Realisation of sales from launched products in FY17 should bolster sales and commentary of staff recruitment is a positive forward indicator for the sales pipeline.

Growth outlook: ~4% revenue growth in FY17, given lower regional confidence and property market sentiment.

Margin outlook: Reported EBITDA margins of ~20% are maintainable given the concentration on higher margin commercial products.

MENA: Positive outlook, outperformance tied to regional property conditions



Source: Company reports

EurAsia/China: All about improving manufacturing efficiency

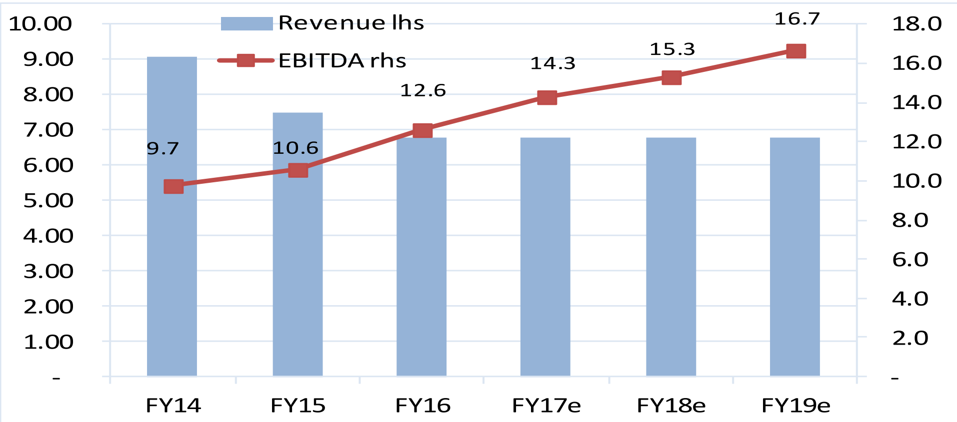
Facilities: EurAsia sales office is based out of Shanghai servicing regional and European customers. Separately, there exists the group's main manufacturing base in Beilun, south of Shanghai in Eastern China. The facility was launched in 2008 and manufacturers 75% of products sold globally. Location allows ease of access to the East China Sea via the Ningbo port for efficient distribution. Fabrics are woven, knitted, cut, sown and packaged to be shipped to GAP warehouses and directly to customers. Carrying Value ~$24m PPE. Of the $3.8m capex in FY16, we believe that ~$1m was spent on a mix of BAU and upgrades to the Chinese facility.

The Chinese facility is wholly owned and the company has recently upgraded the manufacturing, facilities and plant to increase flexibility and capacity. The plant is ISO9001 accredited and uses advanced synthetic textile fibres and textiles. Materials are treated with UV, colour and FR additives, matched to HDPE raw resins. A total of 450 employees work at the facility.

Source: Company materials

Operational position: Opportunity in China is to roll out the Microsoft Dynamics system, improve ordering cycle and reduce inventory lead times. Outsource of non-core, non-scalable product lines to other manufacturers in China has commenced. Upgrade works to support quality and cost improvements has commenced. We very much view this evolution as a 2 year story. The China facility includes a high grade quality inspection system, matched with industry benchmarked testing, machinery and procedures. The challenge/opportunity in China is to reduce complexity, increase automation and create better alignment between the selling regions.

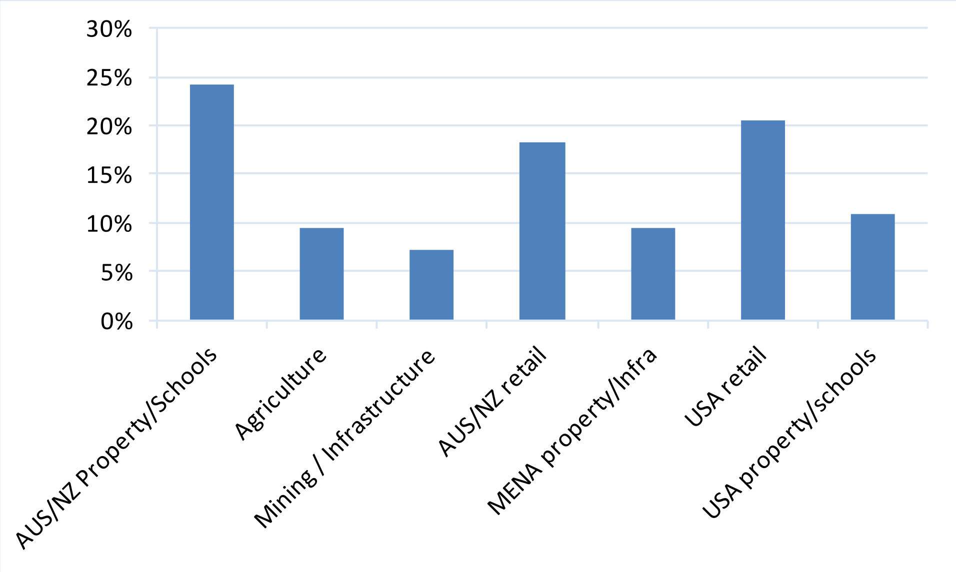
China EurAsia: EBITDA partially distorted by transfer pricing between regions



Source: Company reports

Group sensitivities

Revenue exposure to various segments and markets supportive of FY17 growth



Source: CCZ Equities

Key sensitivities to the top line are the Australia/USA retail and property sectors. We believe that the balance of sensitivities are supportive of top line growth in both residential and commercial product ranges during FY17e. Weighting each segment, balance of factors is >50% probability of a supportive backdrop in FY17e.

Resin represents ~60% of raw material costs and sitting around 2 year lows

Gale Pacific products are manufactured utilising resin as the core ingredient. We believe resin accounts for ~60% of raw materials where oil is a main input for creating resin. Both of these commodities have seen significant decreases in their respective spot prices since 2014 allowing lower COGS and expanded margins for Gale Pacific. The majority of the margin benefit has been recognised in the EurAsia region, before allowing for transfer pricing back into selling regions.

Polyester resin prices have dropped from USD$2,275 in early 2013 to ~USD$1,500 in September of 2016. In $A terms, prices have fallen more modestly, from ~A$2,200 to ~A$2,000.

The resin price volatility is incorporated into customer contracts and trading terms for the majority of large residential and commercial customers. Each of the brands has trading terms with key residential and commercial customers of varying duration. We understand that customer churn rates have been low.

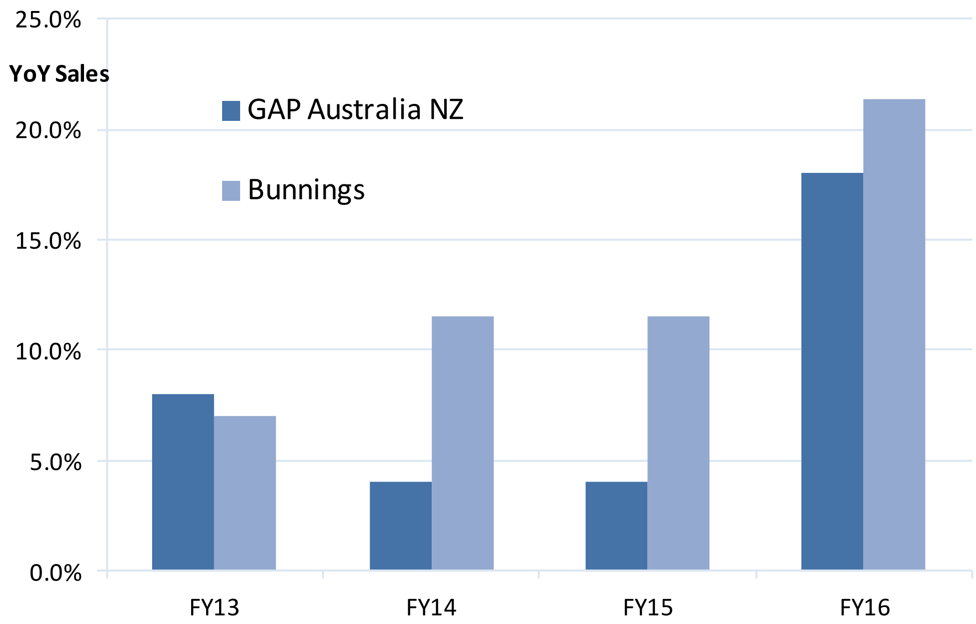
Alignment with category leader Bunnings Warehouse

In FY16, Bunnings Australia/NZ represented ~36% of group revenues. Gale Pacific's product range is represented in 14 different aisles within Bunning's 240 store footprint across Australia.

Bunning's store openings and sales CAGR of 11% since FY11 has provided a positive sales platform for the GAP product suite.

GAP sales staff conducts periodic training of Bunnings sales staff, aisle maintenance, business reviews and place orders within Bunnings stores to support product growth.

Bunnings is the biggest sensitivity within GAP, supportive of growth



Source: Company reports, CCZ Equities

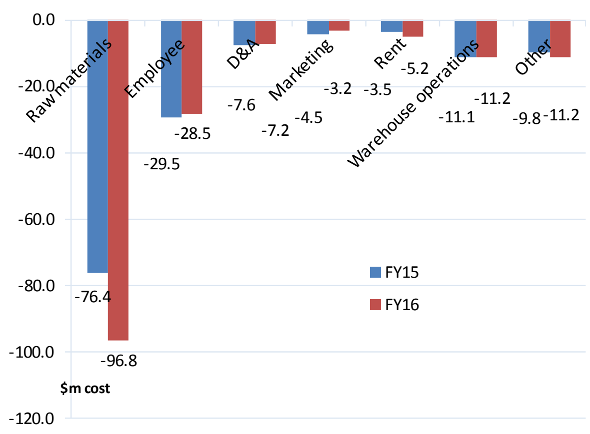
Financials

Revenue recognition occurs at the point of sale, where the customer has taken delivery of the goods. Amounts disclosed as revenue are net of sales returns and trade discounts.

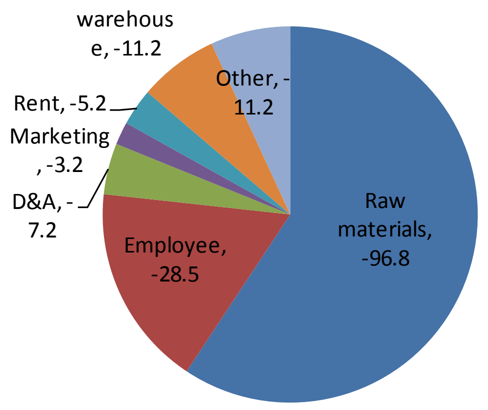
Cost control and operating leverage assisted EBITDA margin expansion in FY16. Raw material and employee costs are the key expense line items.

CCZ estimates a variable/fixed cost ratio of 70%/30% indicating a moderate level of operating leverage. The key to margin leverage is therefore in lower variable production costs through system and manufacturing efficiencies.

FY16 14% cost growth



Manufacturing a key sensitivity to margins



Source: CCZ Equities, Company reports

Operating cash flow conversion from EBITDA was 80% in FY16. This was assisted by reduced debtor days from 67 to 64, lower inventory days from 97 to 94 and increased in creditor days from 32 to 41.

The working capital cycle is a core focus point for management, in particular, cutting down inventory days and increasing speed to market for newly manufactured products.

FY16 closed out with gross debt of $32m and operating lease commitments of $7.7m. Net Debt is $8m. On current earnings projections, we have GAP net cash being positive during FY17.

FY16 NTA of $0.26m with PPE of $30.4m, of which the Chinese manufacturing facility accounts for c80%.

FY16 capex of $3.8m on PPE and $0.7m on intangible operating systems. We see ~$5m capex as a likely run-rate going forward, $3m maintenance and $2m growth, inclusive of $1m system investment likely for FY17.

Board Profile

David Allman – Chairman and Non-executive Director: David was the Managing Director of McPherson's Limited from 1995 to 2009 and prior to that was Managing Director of Cascade Group Limited for 7 years. Before this David held senior positions with Elders IXL Limited and Castlemaine Tooheys Limited. David holds a degree in engineering and prior to obtaining general management positions held managerial roles in production management, finance and marketing. David is Chairman of Muir Engineering Pty Ltd and the Company's Nomination Committee whilst also being a member of the Audit and Risk and Remuneration Committees.

Nick Pritchard – Group Managing Director: Having joined in August of 2013 following 11 years of senior management he led the Australian/New Zealand Gale Pacific business until being appointed Managing Director a year later. Nick developed the Coolaroo brand along with many of the company's highly successful products. Prior to joining Gale Nick held leadership positions at Newell Brands for 11 years where he led all business segments.

Peter Landos – Non-executive Director: Peter is the Chief Operating Officer of the Thorney Investment Group of Companies, which he has been since September 2000. Having previously worked at Macquarie Bank Limited, Peter has extensive business and corporate experience specialising in capital market transactions. Peter is a member of the Company's Nomination, Risk, Audit and Remuneration Committees.

John Murphy – Non-Executive Director: John was the Managing Director of Investec Wentworth Private Equity Limited from 2002 until 2011. He is currently a Director of Ariadne Australia Limited. In the three years prior to joining Gale Pacific John was a Director of Clearview Wealth Limited, Kresta Holdings Limited, Redflex Holdings Limited and Vocus Communications Limited.

Executive Management Profile

Matt Parker – Chief Financial Officer: Joined Gale Pacific in April 2015. Former roles include Ford Australia, Nissan, Cadbury Schweppes and CFO of Paragon Care.

Bruno Marotta – GM Supply Chain: Joined GALE Pacific in October 2014 and has over 30 years of experience in the supply chain management. Former roles include the American Tool Company and Newell Rubbermaid.

Craig Fuller – GM Australia/NZ: Joined GALE Pacific in March 2016 and has 25 years experience in sales, marketing, engineering and general management. Role included Alesco Corporation and Bunnings Trade.

Ali Haidar – GM MENA: Joined GALE Pacific in August 2004 and has recently been given the responsibility to lead the company’s focused expansion in the MENA region.

Lindsay Klebenow – GM Americas: Joined GALE Pacific in June 2016. Prior roles include Culligan, Newell Rubbermaid, Stanley Black and Decker and Elkay.

Cliff Zhang – GM China Manufacturing: Joined GALE Pacific in May 2016 to lead the company’s manufacturing transformation with a focus on further reducing product costs and improving service.

Valuation

Our $0.50 valuation is based on a DCF methodology utilising a WACC of 11.5%, terminal growth rate of 2% and Beta of 1.3.

Peer Analysis

We have established a peer group analysis including companies sensitive to retail, property, agricultural and manufacturing sectors. Larger peers average ~17x P/E on FY17e estimates. Applying a discount for market cap and liquidity we believe that a P/E rating of 13x-14x is appropriate for GAP at this point in the life cycle, which justifies a share price of $0.50+ within the next 12 months.

Peer Group Comparable	Ticke	Price	Market Cap $m	FY16 P/E	FY17E P/E	FY18E P/E	FY16 EV/EBITDA	FY17E EV/EBITDA	FY18E EV/EBITDA
Pact Group	PGH	$6.69	$2,002	20.5x	18.5x	16.6x	11.4x	8.1x	7.4x
Graincorp	GNC	$7.94	$1,817	38.2x	18.7x	15.0x	12.6x	5.5x	4.9x
Breville	BRG	$9.30	$1,210	24.1x	22.5x	20.4x	14.1x	13.6x	12.4x
GUD Holdings	GUD	$10.62	$911	-21.9x	17.1x	15.6x	14.2x	9.6x	8.9x
Fantastic Holdings	FAN	$3.46	$357	16.7x	16.5x	15.3x	14.9x	9.5x	8.9x
Tamawood	TWD	$3.93	$100	12.5x	12.9x	11.6x	9.3x	8.2x	7.4x
McPhersons Ltd	MCP	$1.06	$110	9.5x	7.6x	6.7x	5.6x	5.6x	5.1x
Gale Pacific	GAP	$0.37	$110	10.7x	9.7x	8.5x	5.4x	4.4x	3.8x
Mean (ex GAP)				**14.2x**	**16.3x**	**14.4x**	**11.7x**	**8.6x**	**7.9x**
Median (ex GAP)				**16.7x**	**17.1x**	**15.3x**	**12.6x**	**8.2x**	**7.4x**

Source: CCZ Equities, Bloomberg, Company Reports

Investment Risks

- **Customer Concentration:** Approximately 36% of the Group's external revenue was derived from sales to one customer in the Australasian region during FY16.

- **Resin Input Costs:** Key inputs are oil and high-density polyethylene (HDPE) resin. Both commodities have been trading at spot prices around multi-year lows in USD terms during 2016. This may place downward pressure on COGS if prices increase against a natural $A backdrop. The company does incorporate resin prices into customer contracts. CCZ estimates that if resin prices increased by 10%, over a 6 month period following this price rise the company would be able to recover ~80% of the margin squeeze from customers.

- **Currency Risk:** Majority of FX transactions are denominated in USD, followed by NZD, UAE Dirham and Chinese Renminbi. Based on currency exposure, if the Australian dollar strengthened by 10%/weakened by 10% against these foreign currencies with all other variables held constant, the Group's profit before tax for the year would have been $308,000 higher/lower for FY16.

- **Seasonality:** The business is exposed to seasonality in both the Northern and Southern hemisphere. Residential channels experience a sales spike during the warmer months. With the largest share of revenues generated in Australia/NZ and within the Coolaroo brand, 1H/2H group revenue split was 48%/52% in FY16.

- **Manufacturing cost pressure:** Wages and general cost of doing business in China have risen and further cost pressure is likely within the manufacturing activities unless efficiencies can be generated.

Gale Pacific Limited (GAP.AX)

Analyst: Ian Munro e: imunro@ccz.com.au p: + 61 3 8605 7902
Publication Date: 2 Nov 2016

STOCK INFORMATION	Share Price (AUD)	$ 0.370	Market Cap (AUD)	110.1m
Gale Pacific manufacturers and distributes a range of shade cloth, industrial lining, glass and related products to the retail, construction, hotel and agricultural markets. The four brands are Coolaroo (Shade cloth & sails), Everton (Pool fencing), Zone Interiors (window furnishings, home wares) and Gale Pacific (Commercial grain covers, waterproof liners, shade cloths, vehicle protection etc). The Coolaroo brand accounts for ~55% of revenue, Gale Pacific is 29%, Zone is ~7% each and Everton is ~9% of the total. Australasia is the core geographical segment accounting for 56% of FY16 revenues, followed by the Americas at 31%.			Shares (listed)	297.5
	Target Price (AUD)	**$ 0.50**		
	Recommendation	**BUY**	Year End	30-Jun
	1yr TSR Potential	40.5%	Market Cap ($m)	110.1

RETURN ANALYSIS	2015A	2016A	2017E	2018E	2019E
Adj EPS (cps): weighted shares	**2.3**	**3.4**	**3.8**	**4.3**	**4.7**
adj EPS %	(93%)	51%	11%	13%	9%
Weighted ordinary Shares (m)	297.5	297.5	297.5	297.5	297.5
Diluted shares at year end (m)	299.8	301.2	301.2	301.2	301.2
reported EPS (cps):	**1.7**	**3.4**	**3.8**	**4.3**	**4.7**
PE on adj EPS	**16.2x**	**10.7x**	**9.7x**	**8.5x**	**7.8x**
PE - Emerging Co. Ex 100	19.0x	18.2x	16.9x	15.7x	14.6x
PE Relative	(15%)	(41%)	(43%)	(46%)	(47%)
PEG ratio x	-0.17	0.21	0.86	0.65	0.82
Dividend (AUD cps)	1.00	1.75	2.00	2.25	2.50
Franking	0%	0%	0%	0%	0%
Dividend Yield	**2.7%**	**4.7%**	**5.4%**	**6.1%**	**6.8%**
Payout Ratio	44%	51%	52%	52%	53%
EV/EBITDA	**7.1x**	**5.4x**	**4.4x**	**3.8x**	**3.1x**
EV/EBIT	**12.5x**	**7.9x**	**6.5x**	**5.4x**	**4.5x**
adj EBITDA/Sales	11.9%	12.5%	13.1%	13.3%	13.7%
adj EBIT/Sales	6.9%	8.7%	9.1%	9.4%	9.6%
ROE	**6.9%**	**10.3%**	**10.7%**	**11.4%**	**11.8%**
ROIC (operating)	**11.1%**	**11.4%**	**14.2%**	**17.5%**	**18.4%**
ROFE	568%	14%	16%	18%	20%

VALUATION SUMMARY							
Models (AUD/share)		**DCF - Key Inputs**			**DDM - Key Inputs FY15**		
DCF	0.50	WACC		11.5%	Retention Ratio		56%
DDM	0.25	Cost of Equity		11.5%	Expected Growth		5.2%
PE	0.60						
Weighted Avg	**0.50**	**PE - Key Inputs**	**2016**	**2017E**	**2018E**		**2019E**
		Target PER relative	90%	90%	90%		90%
Valuation Weighting		Discount Rate	102%	97%	92%		88%
DCF	100.0%	PV of EPS	0.56	0.58	0.61		0.63
DDM	0.0%	PV of Dividend	0.02	0.02	0.02		0.02
PE	0.0%	PE Valuation	0.58	0.60	0.63		0.65

PROFIT & LOSS (AUD'm)	2015A	2016A	2017E	2018E	2019E
Revenue	**148.0**	**173.3**	**188.1**	**200.2**	**210.4**
Operating Cost	(132.7)	(156.3)	(166.9)	(177.1)	(185.1)
EBITDA (adj)	**17.9**	**22.2**	**25.1**	**27.1**	**29.3**
Depreciation	(6.9)	(6.2)	(6.9)	(7.1)	(7.3)
Amortisation	(0.8)	(1.0)	(1.1)	(1.1)	(1.7)
D&A (total)	(7.6)	(7.2)	(8.0)	(8.2)	(9.1)
EBIT (adj)	**10.23**	**15.06**	**17.12**	**18.83**	**20.21**
Net Interest	(1.76)	(1.54)	(0.85)	(0.42)	(0.05)
Pre-Tax Profit	**8.5**	**13.5**	**16.3**	**18.4**	**20.2**
Other Significants (after tax)	(1.6)	0.0	0.0	0.0	0.0
Tax	(1.7)	(3.3)	(4.9)	(5.5)	(6.0)
effective tax rate	20%	24%	30%	30%	30%
Reported NPAT	**5.2**	**10.2**	**11.4**	**12.9**	**14.1**
Underlying NPAT	**6.8**	**10.2**	**11.4**	**12.9**	**14.1**
Income Growth	*10%*	*19%*	*8%*	*6%*	*5%*
EBITDA Growth	*2%*	*25%*	*13%*	*8%*	*8%*
EBIT Growth	*(40%)*	*47%*	*14%*	*10%*	*7%*
Underlying PBT Growth	*(50%)*	*60%*	*20%*	*13%*	*9%*
Reported NPAT Growth	*9,152%*	*98%*	*11%*	*13%*	*9%*

BALANCE SHEET (AUD'm)	2015A	2016A	2017E	2018E	2019E
Cash	17.8	24.6	17.9	11.9	22.2
Receivables	27.1	30.2	32.5	34.6	36.3
Pre-payments (AWS capacity)	0.8	1.0	1.0	1.0	1.0
Other	43.7	44.6	44.2	44.2	44.2
Current assets	**89.4**	**100.3**	**95.4**	**91.5**	**103.6**
Fixed Assets (VMWare)	34.9	30.4	28.0	25.5	27.1
Intangibles	25.3	25.2	24.0	23.6	22.5
Other	0.0	4.4	4.4	4.4	4.4
Non-Current Assets	**60.2**	**60.0**	**56.5**	**53.6**	**54.1**
Total Assets	**149.6**	**160.4**	**151.9**	**145.1**	**157.7**
Creditors	12.9	19.6	21.1	22.5	23.6
Short term debt	33.6	13.2	5.0	5.0	5.0
Current tax liability	2.2	2.8	2.8	2.8	2.8
Employee Benefits	1.8	3.6	3.6	3.6	3.6
Current Liabilities	**50.5**	**39.1**	**32.5**	**33.8**	**35.0**
Debt LT	0.8	19.5	12.7	(2.3)	(2.3)
Other & Employee benefits	0.5	2.1	2.1	2.1	2.1
Total Liabilities	**51.8**	**60.8**	**47.3**	**33.6**	**34.8**
Total Shareholder Funds	**97.8**	**99.6**	**104.7**	**111.4**	**122.9**
Total Funds Employed	114.4	107.8	104.5	102.3	103.4
Liquidity and leverage ratios					
NTA per Share $	0.24	0.25	0.27	0.30	0.34
Net Debt (cash) $m	16.7	8.2	(0.1)	(9.1)	(19.5)
Net Debt (cash) / (Net debt + Equity)	15%	8%	(0%)	(9%)	(19%)
Cash Balance $ per share	0.06	0.08	0.06	0.04	0.07
Intangible / EBITDA	1.42	1.13	0.96	0.87	0.77
Net Debt (cash) / EBITDA	(1.0x)	(0.2x)	(0.2x)	(0.5x)	(0.8x)

CASHFLOW (AUD'm)	2015A	2016A	2017E	2018E	2019E
Gross Cash Flow	15.5	19.6	19.4	21.1	23.2
Change in Working Capital	(11.1)	(1.8)	(0.3)	(0.7)	(0.6)
Operating Cash Flow	**4.4**	**17.8**	**19.1**	**20.4**	**22.6**
Capex (PPE)	(4.0)	(3.8)	(4.5)	(4.6)	(4.7)
Capex (Intangible)	(2.6)	(0.7)	(0.7)	(0.7)	(0.7)
Free Cash Flow	**(2.2)**	**13.3**	**13.9**	**15.1**	**17.2**
Free CFPS (cents)	**(0.7)**	**4.4**	**4.6**	**5.0**	**5.7**
Price / Free CFPS	(51x)	8.4x	8.0x	7.4x	6.5x
Operating cash / EBITDA	24%	80%	76%	75%	77%
Operating CFPS (cents)	**1.5**	**5.9**	**6.3**	**6.8**	**7.5**
Price / Operating CFPS	25.4	6.3	5.8	5.5	4.9
Capex / Depreciation	0.4x	0.1x	0.1x	0.1x	0.1x
Operating Cash Yield %	4%	16%	17%	18%	20%
Free Cash Yield %	-2%	12%	12%	14%	15%

SEGMENT INFORMATION	2015A	2016A	2017E	2018E	2019E
Australia / New Zealand					
revenue $m	82.7	97.5	106.3	112.7	117.2
% growth	0.9%	17.8%	9.0%	6.0%	4.0%
Americas					
revenue $m	43.4	53.6	59.0	64.3	69.4
% growth	20%	24%	10%	9%	8%
MENA					
revenue $m	14.4	15.4	16.0	16.5	17.0
% growth	11%	7%	4%	3%	3%
China Manufac / Eurasia					
revenue $m	7.50	6.80	6.80	6.80	6.80
% growth	-17%	-9%	0%	0%	0%
Corporate Costs	-4.15	-1.96	-2.01	-2.05	-2.10

SUBSTANTIAL SHAREHOLDERS		Interim Results	1H16	2H16
Shareholder	**Holding**	Revenue	82.4	90.9
1. Thorney Holdings Pty Ltd	26.8%	EBITDA adj	8.2	14.0
2. Windhager Holding AG	14.1%	NPAT adj	3.2	7.0
3. JP Morgan Nominees	6.8%	EPS (c) adj	1.1	2.4
		DPS (c) adj	0.8	1.0
		EBITDA margin %	10.0%	15.4%
		Operating Cash Flow $m	1.50	16.31

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