EDISON

# Ocean Wilsons Holdings

## Look beyond near-term challenges

Investment companies

**Ocean Wilsons' (OCN) main investment is its controlling interest in Wilson Sons (WSON), the Brazilian maritime services company. Against a background of negative macro newsflow from Brazil, WSON has proved relatively resilient and stands to benefit from a resumption of growth both domestically and internationally. OCN's international investment portfolio provides a balance to WSON and is run with a long-term approach. OCN's shares trade at a significant discount to a look-through valuation and offer a yield of 4.6%.**

| Year end | Revenue (US$m) | PBT* (US$m) | EPS* (c) | DPS (c) | P/E (x) | Yield (%) |
|---|---|---|---|---|---|---|
| 12/13 | 660.1 | 100.5 | 107.1 | 60.0 | 13.1 | 4.3 |
| 12/14 | 633.5 | 78.5 | 65.6 | 63.0 | 21.4 | 4.5 |
| 12/15e | 627.4 | 80.4 | 80.1 | 65.0 | 17.5 | 4.6 |
| 12/16e | 663.8 | 103.7 | 128.1 | 67.0 | 10.9 | 4.8 |

Note: PBT and EPS exclude exceptional items

## First quarter resilience

OCN provided an update and WSON reported Q1 figures in May. The result at WSON was ahead of consensus expectations, with revenues down 4.3% but EBITDA 13.3% ahead (pro forma including the Offshore JV). The slower Brazilian economy held back Container Terminals, but Towage Shipyards and Offshore were ahead, showing the benefits of diversity. OCN's update indicated that the investment portfolio value was 1.9% above the end-2014 value.

## Outlook

Immediate prospects in Brazil are challenging with the economy set to contract in 2015 and inflation running at over 8%. Difficulties at Petrobras also increase uncertainties for the oil-related parts of WSON, although long-term contracts provide some protection. None of this is new to the market and, positively, WSON is also geared to the global economy and volumes of international trade where long-term growth seems likely to prevail. Currency moves have affected near-term earnings (Brazilian real weakness), but WSON earns over 40% of revenues in US dollars, broadly neutralising the negative effect at the EBITDA level. Cash flow at WSON has benefited from the end of an investment cycle in 2013 and this should become more evident once the trading background becomes more positive.

## Valuation: Wide discount, attractive yield

We think assessing OCN's share price relative to a look-through NAV valuation is the most relevant measure given the business comprises an operating company and investment portfolio. On this basis (see page 10) the shares trade at a discount of around 26%. Although this is within the range at which it has traded historically, it nevertheless suggests potential for a significant re-rating once the newsflow from Brazil becomes more positive. With WSON seemingly conservatively valued relative to peers on earnings and EBITDA multiples, there could be upside here also. In the meantime shareholders are rewarded with a yield of 4.6%.

**26 June 2015**

| | |
|---|---|
| **Price** | **892.10p** |
| **Market cap** | **£316m** |
| | £1/US$1.57 |
| Net debt (US$m) at end FY14 | 296 |
| Shares in issue | 35.4m |
| Free float | 49.9% |
| Code | OCN |
| Primary exchange | LSE |
| Secondary exchange | Bermuda |

### Share price performance


| % | 1m | 3m | 12m |
|---|---|---|---|
| Abs | (3.8) | 0.6 | (26.1) |
| Rel (local) | (1.0) | 2.2 | (28.6) |
| 52-week high/low | | 1,230.0p | 850.0p |

### Business description

Ocean Wilsons is an investment holding company based in Bermuda. It has a controlling shareholding in a quoted maritime services company in Brazil and holds a portfolio of international investments.

### Next events

| | |
|---|---|
| Interim results | September 2015 |

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***Ocean Wilsons Holdings is a research client of Edison Investment Research Limited***

# Investment summary

## Company description: Investment with a long view

Ocean Wilsons is a Bermudan investment company with two main assets: a controlling interest in Wilson Sons (WSON), a quoted Brazilian maritime services and port terminal company, and an international investment portfolio. Based on a look-through NAV, which includes the market value of WSON, the split is 60/40 between Wilson Sons and the investment portfolio. Both are managed with the aim of generating growth over the long term.

## Valuation: Wide discount to look-through value

OCN shares are trading at a discount of c 25% to a look-through value that includes the market value of the stake in WSON (page 10 for detail). We have compared WSON's valuation with a comparator group of local and international companies operating ports and shipping businesses. P/E and EV/EBITDA valuations for WSON appear modest by comparison.

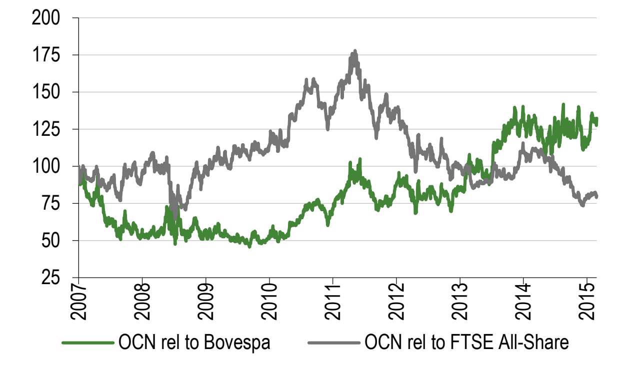
## Sensitivities: International trade, oil, Brazil

Although WSON is a Brazilian business, it reports in US dollars and has over 40% of its revenues in dollars. Expenses are mainly incurred in Brazilian reals and the net effect of exchange rate changes at the EBITA level is muted as a result, which means that from an investor perspective WSON and hence to a large extent OCN are US dollar-related plays rather than being primarily Brazilian real influenced. The accounting for foreign exchange movements (see page 9) can make the reported progression of earnings more lumpy but, over time, the underlying performance of the business is likely to be more stable.

Economically, trends in world trade, the oil industry and the Brazilian economy are likely to be the main drivers. For the oil-exposed activities, developments at the corruption-hit Petrobras business are important, although long-term contracts and the likelihood of long-term development of Brazil's pre-salt reserves are important mitigants. For the investment portfolio the main exposure is to equities, but this is modified by the fact that it picks managers who take active positions while the portfolio also has unlisted investments such as private equity.

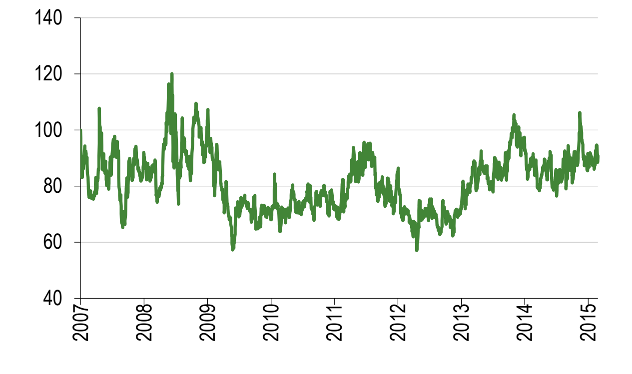
As Exhibit 1 below illustrates, OCN has outperformed the Brazilian Bovespa index reflecting the relative resilience of WSON and the diversifying effect of the investment portfolio. On the other hand, it has not been able to avoid the weakness of the Bovespa relative to the UK market and this is mirrored in OCN's underperformance of the FTSE All-Share index since 2011. Looking ahead, although economic trends in Brazil are currently adverse, much of this is arguably factored into prices potentially providing the basis for a stronger performance relative to the UK market.

**Exhibit 1: OCN relative to Bovespa and FTSE All-Share**




Source: Datastream

**Exhibit 2: OCN relative to WSON – no clear trend**




Source: Datastream

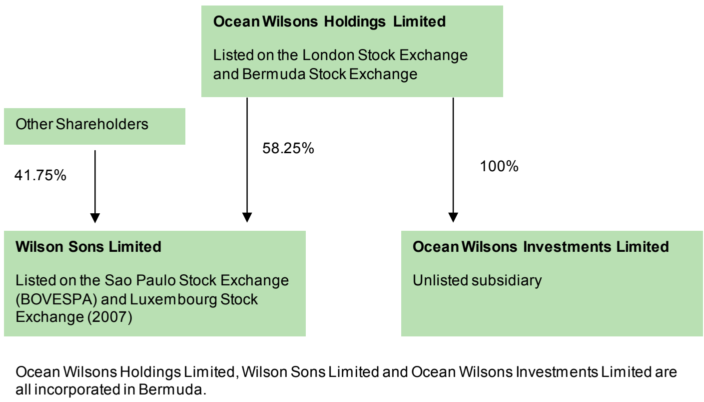
## Company description: Differentiated investments

Ocean Wilsons Holdings (OCN), based in Bermuda, is an investment company with two main assets: a controlling interest in Wilson Sons (WSON), a quoted Brazilian maritime services company, and an international investment portfolio held in its Ocean Wilsons Investments (OWIL) subsidiary. OCN is run with a long-term view allowing WSON to develop without being constrained by short-term targets, while the international portfolio is also managed with the objective of producing long-term capital growth.

The structure of the business is set out in Exhibit 3 below. OCN's main asset is its 58.25% holding in WSON, a company that it fully owned before WSON's initial public offering in May 2007. WSON has a free float of 41.8%, including c 15% owned by funds managed by Aberdeen Asset Management. The IPO was a means of creating a transparent valuation for WSON while the proceeds were invested, constituting the majority of the assets in OWIL's international portfolio, which in turn provides diversification for holders of OCN.

OCN's own shareholder structure includes a 26.4% holding by Hansa Trust, a listed investment trust in which Mr W Salomon and his sister Mrs C Townsend respectively have interests of 26.4% and 25.9% in the voting shares. In addition Mr Salomon and Mrs Townsend respectively have interests in shares representing 12.5% and 11.1% of OCN's share capital. Management of the OWIL portfolio is delegated to Hanseatic Asset Management, part of the Salomon family office. This ownership structure helps underpin the long-term approach taken in managing OCN's assets.

**Exhibit 3: OCN corporate structure**



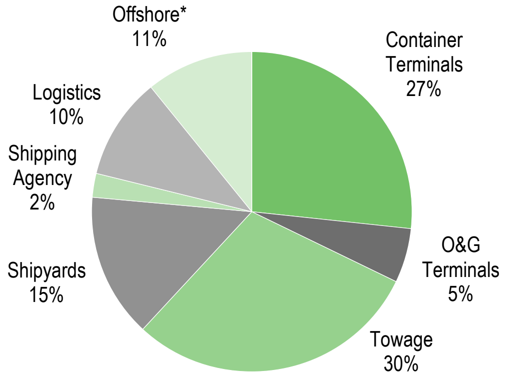

Source: Ocean Wilsons

## Wilson Sons: Brazilian maritime services and ports

Wilson Sons has a range of mainly maritime-related businesses including container terminals, support bases and (via a joint venture) support vessels for the oil and gas industry, towage, a shipyard primarily constructing offshore support vessels and tugs and a logistics activity.

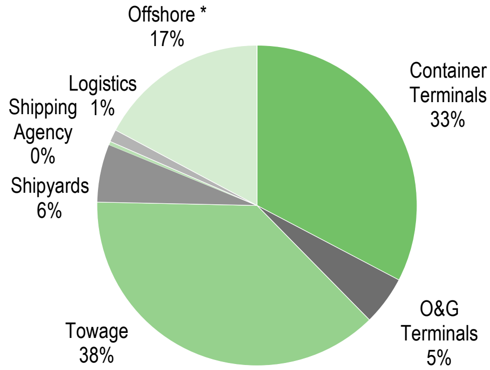
An analysis of revenue and EBITDA is shown in Exhibits 4 and 5 highlighting that the largest contributors are Container Terminals and Towage; taken together these activities accounted for nearly 70% of EBITDA in the 2008-14 period (excluding corporate costs). Revenue in these areas is primarily driven by the volume (rather than value) of international and to a lesser extent domestic trade in Brazil. The explicitly oil and gas exposed activities accounted for about 22% of pro forma EBITDA, while there is also some oil industry-related activity in the towage and shipyards businesses. The sensitivity of these businesses to the lower oil price is significantly mitigated by long-term contracts (the Offshore JV) and the extent to which activities are geared to production rather than exploration activity (see individual business comments below).

**Exhibit 4: Revenue analysis (2014)**




Source: Wilson Sons. Note: *Offshore is pro forma share of JV.

**Exhibit 5: EBITDA analysis (2014)**




Source: Wilson Sons. Note: *Offshore is pro forma share of JV.

## Container terminals

WSON is the third largest container terminal operator in Brazil with two terminals located in the south and north-east of Brazil in the public ports of Rio Grande do Sul and Salvador respectively. The original concession period for these terminals was 25 years and is renewable for a further 25 years in 2022 (Rio Grande) and 2025 (Salvador). The company believes it will be possible to negotiate a satisfactory agreement for renewal of the concessions in due course reflecting legislation that reinforced the rights of existing holders and, in the case of Rio Grande, a regional authority amendment to the contract granting an option for the renewal linked to investment already undertaken. About 60% of Rio Grande's volumes are accounted for by exports, primarily of agricultural products including tobacco, chicken and rice. Salvador is well positioned for trade routes to the US, Europe and the Middle East and stands to benefit from improving infrastructure and long-term growth in the less developed north-eastern region. Principal cargos include chemicals, fruit, juices and metal. In terms of tonnage, Rio Grande accounts for about 70% of the total volume for the two ports and both ports are operating at just above 50% of capacity, indicating significant scope for growth and some margin improvement as utilisation increases. Total volume has grown at an annual rate of 2.1% between 2008 and 2014, including a slowdown during the global financial crisis. Within the total, cabotage (coastal traffic in Brazil) has grown at a compound rate of more than 8%, reflecting secular growth in this transport mode. Volumes of 'full' containers, which are the main source of revenue, have grown at 3.2% in the same period.

## Towage

The 76-strong tug fleet is the largest in Brazil, accounting for 50% of harbour manoeuvres and operating in all Brazil's main ports. The fleet also carries out higher-margin special operations including ocean towing, salvage, and firefighting. Over the last five years special operations have accounted for an average of over 14% of revenue and 12.7% in FY14. The fleet is relatively modern, with an average age of 11 years, and the majority of the ships have azimuth propulsion providing greater towing capacity and manoeuvrability. All domestic Brazilian operators benefit from regulatory protection and access to long-term, low-cost finance from the Fundo da Marinha Mercante, features that seem unlikely to change. The fact that WSON has its own shipyard represents a competitive advantage, both for new tug construction and maintenance. Growth in the number of harbour manoeuvres in 2008-14 was limited, but average deadweights towed increased at a compound rate of 3.4% contributing to revenue growth.

## Offshore support vessels

The 50%-controlled Wilson Sons Ultratug Offshore (WSUT) joint venture operates support vessels (19 in WSUT's own fleet) for offshore oil and gas production and exploration in Brazil. From 2013 this activity was no longer consolidated, instead being equity accounted. Nevertheless, WSON does provide pro forma figures including its 50% share of the business that are helpful in understanding its contribution to the group (17% of EBITDA in FY14). As with the towage activity, regulation provides protection to Brazil-built/flagged vessels, low-cost finance is available and WSUT benefits from the availability of WSON's own shipyard for new vessel construction and maintenance. The fleet is operated under contracts with Petrobras and the fleet has an average unexpired term of five years.

Looking ahead, there is uncertainty surrounding Petrobras's plans and the potential impact of the lower level of oil prices, but the longevity of outstanding contracts provides significant revenue visibility for the WSUT business. Nevertheless, the joint venture has three offshore support vessels on order from China that do not have contracts. The first one is due for delivery at end 2015 with the other two arriving in 2016. Even if the vessels are not contracted in the near term, WSUT would only have 15% of its fleet 'off-hire', which WSON describe as manageable and not unusual in the industry context. Historically, the growth of the business has been rapid with the fleet size and days of operation compounding at 32% since 2008. Growth has moderated somewhat in recent years and will be subject to oil industry development in the near term but, on a medium to long-term view, production from and development of Brazil's pre-salt reserves seems likely to continue to expand, generating further growth at WSUT.

## Oil and gas terminal (Brasco)

Brasco operates a port terminal dedicated to servicing oil platforms. It undertakes the purchase, storage and delivery of supplies such as parts, mud, chemicals and food to offshore platforms; it also receives and processes waste from the platforms. The business was expanded through the acquisition of another business, Briclog, which gave Brasco scope to expand capacity. Given the current oil industry background, take-up of this additional berthing may be sluggish in 2015 and 2016 but on a longer view, as with WSUT's offshore vessels fleet, the requirement for this capacity should ramp up with the development of pre-salt reserves.

## Shipyards, logistics, agency

The shipyard activity is located in Guarujá, close to the Santos and Campos oil basins and is therefore well-sited for the construction and maintenance of offshore support vessels. Over the last five years it has delivered 17 tugs and 11 offshore service vessels including both third-party and Wilson Sons orders. The order book includes six third-party vessels but this only extends to the first half of 2016, after which time the focus would be on maintenance and internal work (10 tugs on order at end March 2015) to sustain activity. As with the other oil and gas exposed businesses, the longer-term outlook should be more favourable and the location and facilities of the shipyard mean it is well placed to bounce back from a potential softening of activity.

Logistics activities include bonded warehouses, logistics centres and transport for international and domestic customers. The focus of the business is on bonded warehouses and related services, with a number of low-margin operations dedicated to specific customers being ended in recent periods. This has affected near-term results, as has increased competition for the bonded warehouse in São Paulo state.

The agency business is a long-established independent shipping agent operating in the main Brazilian ports. Relatively small in WSON, the agency's revenues have been reduced recently as shipping lines have taken this function in house.

## Wilson Sons revenue and EBITDA evolution

Exhibit 6 below shows the development of revenues and EBITDA over the last six financial years including the WSUT JV on a pro forma basis. The period shown includes the impact of the financial crisis and fluctuations in currency including, for 2014, a weakening of the Brazilian real and softer international trade. Nevertheless, over this period EBITDA compounded at a rate of 8.4% based on revenue growth of 6.1%. This in part reflects a period of significant investment in the business between 2007 and 2014 with capex totalling over $1bn.

The largest EBITDA contributor, Towage, grew at 7.9% per annum while Containers, in part affected by currency in 2014 saw more modest growth of 3.5%. Notable are the development of the Offshore and Shipyards contributions over the period shown. This longer-term record provides some context for some of the near-term challenges for the Brazilian economy and the oil industry discussed in the Outlook section.

**Exhibit 6: Wilson Sons revenue and EBITDA analysis**

| | 2008 | 2009 | 2010 | 2011 | 2012 | 2013 | 2014 |
|---|---|---|---|---|---|---|---|
| **Net revenues** | | | | | | | |
| Container Terminal | 155.5 | 148.7 | 178.8 | 203.5 | 189.5 | 227.4 | 189.6 |
| O&G Terminal (Brasco) | 15.0 | 26.7 | 49.2 | 68.3 | 37.9 | 42.7 | 39.0 |
| Towage | 147.1 | 145.7 | 156.2 | 167.4 | 179.1 | 196.6 | 211.0 |
| Shipyards | 52.5 | 27.4 | 43.3 | 56.7 | 61.8 | 100.3 | 103.4 |
| Shipping Agency | 17.6 | 15.2 | 17.6 | 20.3 | 24.6 | 24.5 | 17.1 |
| Logistics | 89.3 | 75.8 | 102.4 | 140.5 | 108.2 | 96.8 | 73.4 |
| Corporate | -0.3 | 0.2 | | | | | |
| Offshore* | 21.6 | 38.1 | 28 | 41.4 | 47 | 54.4 | 76.9 |
| **Total** | **498.3** | **477.8** | **575.5** | **698** | **647.9** | **742.8** | **710.4** |
| **EBITDA** | | | | | | | |
| Container Terminal | 60.6 | 49.0 | 61.4 | 74.6 | 75.4 | 75.5 | 74.4 |
| O&G Terminal (Brasco) | 2.8 | 9.3 | 14.9 | 16.7 | 9.3 | 10.7 | 11.3 |
| Towage | 54.5 | 61.3 | 53.4 | 61.4 | 62.4 | 74.6 | 85.8 |
| Shipyards | 6.2 | 9.9 | 6.1 | 15.3 | 14.0 | 21.8 | 13.3 |
| Shipping Agency | 3.3 | 2.3 | 0.8 | 2.7 | 4.9 | 4.1 | 0.8 |
| Logistics | 6.6 | 7.1 | 13.1 | 24.5 | 13.2 | 18.2 | 2.8 |
| Corporate | -24.2 | -29.7 | -41.5 | -43.1 | -38.1 | -22.2 | -28.4 |
| Offshore* | 12.9 | 19.2 | 13.1 | 11.3 | 16 | 23.1 | 39.2 |
| **Total** | **122.7** | **128.4** | **121.3** | **163.3** | **157.1** | **205.9** | **199.3** |

Source: Wilson Sons. Note: *Offshore is pro forma share of JV.

## Ocean Wilson Investments

OWIL's portfolio is managed by Hanseatic Asset Management on an unconstrained global basis with the aim of achieving long-term returns while emphasising preservation of capital. Reflecting this, performance is measured against an absolute rather than equity benchmark (one-year US dollar LIBOR plus 2%). The portfolio is invested across four silos: public equities, private assets (mainly private equity), market-neutral funds and bonds/other. Cash is managed so that future commitments to private equity funds can be met. Given the long-term time horizon, the manager expects that equities (public and private) will constitute the majority of the investments. Also, most investments are made through collective funds and partnerships to access specific management expertise with the benefit of Hanseactic's longstanding network of contacts in the asset management industry and fund selection capability.

### Investment approach

Hanseatic regards manager selection as key to the management of the portfolio. Meetings with potential managers can be prompted by top-down views on which areas are most attractive or referrals from Hanseatic's network. Hanseactic favours funds where selections are made on the basis of strong conviction with a willingness to take unconventional decisions. Full due diligence is undertaken including an assessment of qualitative factors such as the integrity and motivation of a fund manager in addition to normal inspection of performance records and documentation. After inclusion in the portfolio investments are monitored, with particular attention paid to any signs of style drift or changes in personnel.

The approach is compared with endowment funds given the emphasis on real returns, an indefinite time horizon and broad diversification. As shown in Exhibit 7, there is a significant private equity component and Hanseatic believes outsized returns can be earned from such investments reflecting illiquidity and the opportunity for managers to exploit less efficient pricing.

**Exhibit 7: OWIL portfolio structure**

| End December | 2013 (%) | 2014 (%) | 2014 ($m) |
|---|---|---|---|
| Global equities | 61.6 | 57.4 | 144.6 |
| Private assets | 23.1 | 29.7 | 74.7 |
| Market neutral funds | 8.0 | 3.3 | 8.4 |
| Bonds/other (including cash) | 7.3 | 9.6 | 24.0 |
| **Total** | **100.0** | **100.0** | **251.7** |

Source: Ocean Wilsons

Further analysis in Exhibit 8 confirms the diversification of the portfolio, demonstrates its international character (only 0.2% UK) and shows that the ability to invest in less liquid funds/assets has been employed (c 70% of assets have less than daily liquidity). The 'other' category under the geographical heading includes 7.4% in debt investments and 5.2% in commodity equities and commodities.

**Exhibit 8: Portfolio allocation and liquidity analysis (% at end December 2014)**

| Allocation | % | Geographical/other | % | Underlying liquidity | % |
|---|---|---|---|---|---|
| Private equity | 20.1 | North America | 14.0 | Daily | 28.1 |
| Cash | 6.0 | Japan | 4.7 | Weekly | 6.0 |
| Market neutral | 3.3 | Europe | 8.6 | Monthly | 23.3 |
| High-yield corporate (dev. mkt.) | 3.6 | Global (developed) | 15.8 | Quarterly | 8.2 |
| Long/short hedge funds | 20.7 | Asia Pacific ex-Japan | 18.3 | Half-yearly | 3.6 |
| Long-only equities | 36.7 | Emerging mkts (ex-Asia) | 6.9 | Fixed life-in investment period | 12.9 |
| Private debt | 5.7 | Global emerging mkts | 4.6 | Fixed life investment period complete | 16.8 |
| Private real assets | 3.9 | Cash | 6.0 | Other | 1.1 |
| | | Other | 21.1 | | |
| | **100.0** | | **100.0** | | **100.0** |

Source: Ocean Wilsons

### Performance

Portfolio performance (to end 2014) has been ahead of the absolute benchmark for all periods shown in Exhibit 9, kept pace with the world indices over 10 years and outperformed the developed world index since inception in 2000. Performance in 2014 illustrated the benefit of the portfolio's diversification across different asset categories with the 4.7% overall return resulting from a negative return of 2.1% on bonds/other more than balanced by strong performances from private assets (8.5%) and market-neutral funds (6.9%) while the global equities silo produced a 4.1% return, similar to the All Country World Index.

**Exhibit 9: OWIL portfolio annualized cumulative returns to end 2014**

| (%) | One year | Three year | Five year | 10 year | Since inception* |
|---|---|---|---|---|---|
| Portfolio | 4.7 | 7.1 | 4.3 | 6.1 | 7.5 |
| Benchmark | 2.6 | 2.9 | 2.9 | 4.5 | 3.9 |
| MSCI World (Developed) Index | 4.9 | 15.5 | 10.2 | 6.0 | 4.0 |
| MSCI All Country World Index | 4.2 | 14.1 | 9.2 | 6.1 | N/A |
| MSCI Emerging Markets Index | -6.5 | 4.0 | 1.8 | 8.4 | 9.7 |

Source: Ocean Wilsons. Note: *Inception 1 November 2000.

## First quarter update

OCN issued a first quarter update and WSON reported its Q1 figures in mid-May.

WSON reported revenues down 4.3% but EBITDA up +13.3% (both including the Offshore JV on a pro forma basis). Negative influences on revenues included the weaker Brazilian real, softer container terminal volumes (down 7.3% on the same period in 2014) and reduced dedicated operations in Logistics. EBITDA resilience reflected in part the offsetting effect of Brazilian real on costs and there were also strong performances in Towage, Shipyards and the Offshore JV. At the net income level foreign exchange depreciation gave rise to negative items relating to net monetary assets and deferred tax, resulting in a loss ($8.1m) compared with a profit in the previous year period ($24.3m).

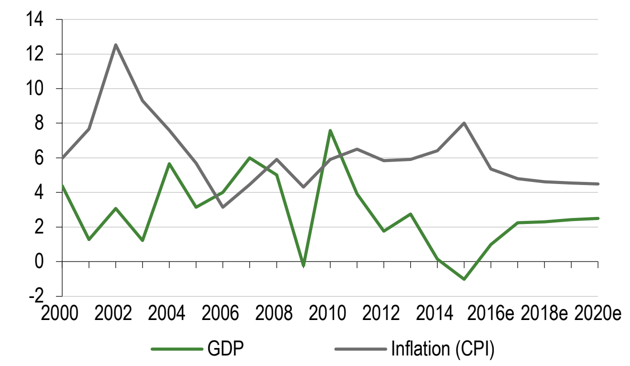
Ocean Wilsons additionally announced that at the end of April the investment portfolio, including cash, was 1.9% ahead of the year end level at $256.4m.

# Outlook

## Near-term macro challenges, internal focus on efficiency

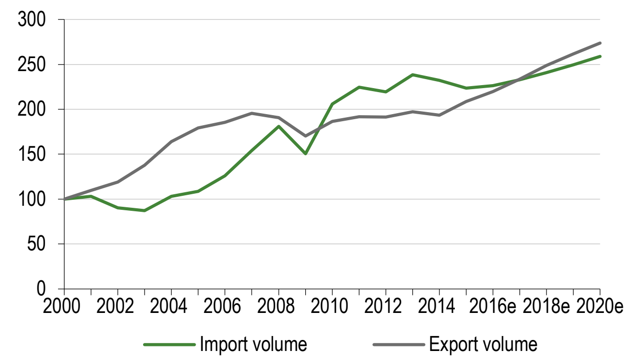
The macro background in Brazil remains difficult with the planning ministry projecting a 1.2% contraction in GDP in 2015, the currency down c 15% year to date versus the US dollar and inflation running at over 8%. The government is taking measures to try to move to a primary fiscal surplus and the central bank has set interest rates to contain inflation, both of which will tend to add to the pressure on consumer spending. Additionally, the sharp reduction in the oil price and the crisis faced by Petrobras as a result of the corruption scandal have contributed to uncertainty in the economic outlook and specifically for WSON's oil-related activities. Exhibit 10 illustrates the unfavourable trend in growth and inflation, but also indicates the IMF's expectation that these trends could become more favourable over the next five years. Also pertinent to WSON is the trend in world trade and Brazilian imports and exports. As Exhibit 11 shows, import volumes have and are expected (IMF estimates) to suffer, but export volumes have been less affected with both expected to strengthen on a five-year view, helped in the near term by the weak currency.

**Exhibit 10: Brazil GDP growth and inflation (%)**




Source: IMF World Economic Outlook

**Exhibit 11: Brazil import and export volumes**




Source: IMF World Economic Outlook

In the short term WSON has said that it is focusing on improving operational efficiency and from a cash flow perspective is projecting capital spending of $110-120m this year compared with a peak of $227m in 2011. For the OWIL portfolio, the manager has acknowledged that market volatility could increase and, while noting the valuations of emerging markets may be attractive on a long view, in the near term developed markets are seen as a more attractive option. Against an uncertain market backdrop, the diversity of fund investments with active managers has the potential to provide diversification and a differentiated performance.

## Forecast comments

We have reintroduced estimates for OCN following a change in analyst and these are summarised at the end of this note in Exhibit 14.

- We look for 2015 revenue to be similar to 2014 with modest underlying growth offset by weakness in the Brazilian currency. While we have allowed for some further weakness in the real in 2016 (c 6%), we still look for growth of around 6%.
- Our operating profit estimate is for virtually unchanged operating profit of $90.5m in FY15 helped by lower real-denominated costs, while for FY16 we look for 8% growth to $97.7m.
- Pre-tax profit and earnings per share estimates are subject to variations in the foreign exchange-related items, which change significantly with rates (see below). As an indication we have assumed exchange losses on net monetary items of $21.3m and $10.7m for FY15/16 respectively compared with the loss of $17.6m for 2014. Our earnings per share estimates are 80.4c and 128.1c for FY15 and FY16 respectively compared with 65.6c reported for FY14.
- Financially, our estimates suggest a modest net cash outflow this year followed by a move to positive net cash flow in 2016. Most of the outstanding debt (Exhibit 15) is long-term and on favourable interest rates so interest cover (operating profit/finance cost) is expected to increase from 3.8x for 2015e to 4.8x for 2016e. Net debt/equity at end 2014 was 39% or 72% including the share of WSUT joint venture debt, and these ratios seem unlikely to change significantly over the forecast period.

### Currency sensitivity

OCN uses the US dollar as its functional and reporting currency and the WSON subsidiary estimated that it had 47% of US dollar revenues and 10% of US dollar costs in FY14. As a result, a weaker Brazilian real affects just over half of revenues in dollar terms, but has a favourable impact on margin because 90% of costs are paid in reals. OCN and WSON indicate that the net effect on EBITDA is roughly neutral.

There are, however, additional accounting effects that result in greater volatility in reported earnings. These are best explained in a paper prepared by Keith Middleton, which is available on OCN's website but include the profit and loss line relating to net monetary items, which reflects exchange translation movements primarily relating to working capital; movements on debt, which are included in finance costs; and deferred tax adjustments relating to loans and fixed assets.[1]

Beyond these immediate accounting impacts there are also the potential economic repercussions that changing exchange rates may have on the Brazilian economy and trade flows.

## Dividend policy

The company's policy is to pay the full dividend received from WSON in the period and a percentage of the average capital employed in the investment portfolio, as determined by the board. Dividends are set in US dollars and paid annually. The dividend relating to FY14 was 63c comprising 47.8c relating to the WSON dividend and 61% of the net income from the portfolio. WSON has a stated policy of paying approximately 50% of net profit as a dividend, but has exceeded this in FY14 (payout just over 100%) reflecting a desire to increase the payment to shareholders and the fact that an investment cycle has been completed, benefiting cash flows accordingly.

[1] For a Brazilian tax calculation a weaker real could, for example, generate a deferred tax loss related to US dollar loans and reduce the deferred tax credit relating to property plant and equipment: this would be reflected in the WSON/OCN P&L tax charge.

## Management

The board comprises six non-executive and one executive director, Keith Middleton, finance director, who joined the company in 1996 having worked for a number of international companies. José Francisco Gouvêa Vieira has been chairman since 1997 and a director of OCN since 1991; he is chairman of WSON and director of a number of other companies. William Salomon, deputy chairman, joined the group in 1995 and is a director of WSON, chairman of Hanseactic Asset Management and a non-executive director of Hansa Trust. Christopher Townsend was appointed as a non-executive director in 2011 and is investment director of Hansa Capital GmbH. The three independent non-executive directors are: Andrés Rozental (senior independent director), who is also a non-executive of Wilson Sons and has a number of directorships of Mexican companies; Colin Maltby, who joined the board in 2013 has a number of other directorships including BACIT; and Andrey Berzins, appointed in 2014, who is also a non-executive director of Aberdeen Asia Income Fund.

## Valuation: Wide discount suggests opportunity

In this section we consider where the OCN share price stands in relation to a look-through NAV and set the WSON valuation (based on consensus expectations) in the context of a peer group. The look-through NAV comprises the market value of WSON shares together with the latest valuation of the OWIL investment portfolio. This is illustrated in Exhibit 12 and shows the shares trading at a 26% discount to the look-through NAV.

**Exhibit 12: Ocean Wilsons share price discount to a look-through NAV**

| | (p) | (£m) |
|---|---|---|
| Last OWIL value per Ocean Wilsons share (end April 2015) | 461.8 | 163.3 |
| Wilson Sons market value per Ocean Wilsons share (25 June 2015) | 747.7 | 264.4 |
| **Ocean Wilsons look-through value** | **1,209.5** | **427.7** |
| Ocean Wilsons share price/market cap (25 June 2015) | 897.5 | 317.4 |
| **Discount** | **-26%** | **-26%** |

Source: Ocean Wilsons, Datastream, Edison Investment Research

Turning to a comparison of WSON's valuation, Exhibit 13 shows a selection of local and global port and shipping companies with consensus-based P/E and EV/EBITDA multiples. WSON's earnings and EBITDA multiples are noticeably below both the simple and (not shown) weighted averages. Its EV/EBITDA multiples are closer to the Brazilian comparators. There are potential shortcomings with the comparison, which includes variable liquidity of the stocks, the range of forecasts and differences between the companies listed. Nevertheless, this at least lends support to the idea that Wilson Sons is not expensively rated in relation to peers.

**Exhibit 13: Selected Wilson Sons comparator valuations**

| | Mkt cap (US$m) | P/E FY1 (x) | P/E FY2 (x) | EV/EBITDA FY1 (x) | EV/EBITDA FY2 (x) | Price to book (x) |
|---|---|---|---|---|---|---|
| **Wilson Sons** | **714** | **19.2** | **10.7** | **4.5** | **3.9** | **1.5** |
| Santos Brasil | 534 | 23.1 | 17.7 | 6.7 | 5.9 | 1.1 |
| JSL (BRA) | 759 | 21.4 | 15.6 | 6.4 | 5.5 | 2.2 |
| China Merchants (HKG) | 10,809 | 17.5 | 15.8 | 19.6 | 18.0 | 1.2 |
| Dalian Port (HKG) | 4,491 | 21.5 | 20.1 | 21.0 | 19.7 | 1.0 |
| Far Eastern Shipping (RUS) | 169 | N/A | 14.3 | 11.6 | 8.2 | N/A |
| Hamburger Hafen (GER) | 1,511 | 21.7 | 18.9 | 5.6 | 5.4 | 2.7 |
| NCB Holdings (MYS) | 436 | 48.6 | 38.0 | 8.2 | 7.5 | 1.2 |
| Port Of Tauranga (NZL) | 1,618 | 30.3 | 28.6 | 19.6 | 18.3 | 2.9 |
| Sinotrans (HKG) | 3,149 | 12.8 | 11.4 | 9.1 | 8.5 | 1.5 |
| **Total/average** | **24,191** | **24.0** | **19.1** | **11.2** | **10.1** | **1.7** |

Source: Bloomberg. Note: Prices as at 26 June 2015.

### Exhibit 14: Financial summary

| US$m | 2012 | 2013 | 2014 | 2015e | 2016e |
|---|---|---|---|---|---|
| Year end 31 December | | | | | |
| **PROFIT & LOSS** | | | | | |
| Revenue | 610.4 | 660.1 | 633.5 | 627.4 | 663.8 |
| Cash costs | (469.2) | (492.4) | (479.3) | (467.3) | (494.4) |
| EBITDA | 141.2 | 167.7 | 154.2 | 160.1 | 169.4 |
| Intangible Amortisation | (55.9) | (58.7) | (65.1) | (69.6) | (71.7) |
| Operating Profit | 85.3 | 109.1 | 89.1 | 90.5 | 97.7 |
| Profit/loss on property, plant and equipment | (0.5) | 10.0 | 0.3 | 0.0 | 0.0 |
| Share of results of JVs | 0.7 | 2.4 | 7.1 | 7.3 | 8.4 |
| Investment revenue | 18.3 | 17.8 | 17.0 | 15.4 | 15.4 |
| Other gains and losses | 16.4 | 13.7 | 6.2 | 12.5 | 13.3 |
| Finance costs | (9.9) | (21.9) | (23.6) | (24.1) | (20.3) |
| Exchange gains/losses on monetary items | (11.6) | (30.6) | (17.6) | (21.3) | (10.7) |
| Profit before tax | 98.6 | 100.5 | 78.5 | 80.4 | 103.7 |
| Income tax | (33.7) | (42.2) | (41.9) | (34.2) | (38.7) |
| Non-controlling interests | (23.6) | (20.4) | (13.4) | (17.8) | (19.7) |
| Earned | 41.3 | 37.9 | 23.2 | 28.3 | 45.3 |
| Average number of shares m | 35.4 | 35.4 | 35.4 | 35.4 | 35.4 |
| EPS (c) | 116.7 | 107.1 | 65.6 | 80.1 | 128.1 |
| Dividend per share (c) | 42.0 | 60.0 | 63.0 | 65.0 | 67.0 |
| EBITDA Margin (%) | 23.1 | 25.4 | 24.3 | 25.5 | 25.5 |
| Operating Margin (%) | 14.0 | 16.5 | 14.1 | 14.4 | 14.7 |
| **BALANCE SHEET** | | | | | |
| Fixed Assets | 695.6 | 768.1 | 819.6 | 849.7 | 868.4 |
| Intangible Assets | 45.0 | 84.3 | 73.6 | 63.8 | 57.5 |
| Tangible Assets | 650.7 | 683.8 | 746.0 | 785.9 | 811.0 |
| Current Assets | 615.2 | 564.4 | 493.0 | 490.7 | 526.4 |
| Stocks | 37.5 | 29.1 | 32.5 | 32.1 | 34.0 |
| Debtors | 199.5 | 150.8 | 96.2 | 95.3 | 100.8 |
| Cash | 136.7 | 106.5 | 103.8 | 87.1 | 98.9 |
| Other | 241.6 | 278.0 | 260.5 | 276.1 | 292.7 |
| Current Liabilities | (213.2) | (175.8) | (133.7) | (132.9) | (137.4) |
| Creditors | (176.5) | (136.2) | (81.0) | (80.3) | (84.8) |
| Short term borrowings | (36.7) | (39.5) | (52.6) | (52.6) | (52.6) |
| Long Term Liabilities | (354.1) | (386.6) | (411.6) | (413.8) | (422.8) |
| Long term borrowings | (326.9) | (339.2) | (347.2) | (349.6) | (357.7) |
| Other long term liabilities | (27.1) | (47.4) | (64.3) | (64.2) | (65.1) |
| Net Assets | 743.6 | 770.1 | 767.3 | 793.7 | 834.6 |
| **CASH FLOW** | | | | | |
| Operating Cash Flow | 154.9 | 148.7 | 150.5 | 160.1 | 165.0 |
| Net Interest | (0.5) | 1.7 | (0.6) | (2.7) | (2.9) |
| Tax | (31.9) | (27.3) | (29.5) | (32.9) | (27.3) |
| Capex | (101.5) | (88.2) | (101.0) | (113.0) | (98.0) |
| Acquisitions/disposals | 0.0 | (10.2) | (26.7) | 0.0 | 0.0 |
| Financing (including divs from JV) | (2.3) | (45.9) | 17.9 | 10.0 | 10.0 |
| Dividends | (22.5) | (23.9) | (34.5) | (40.6) | (43.2) |
| Net Cash Flow | (3.8) | (45.2) | (23.8) | (19.1) | 3.6 |
| Opening net debt/(cash) | 223.2 | 227.0 | 272.2 | 296.1 | 315.1 |
| Other | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 |
| Closing net debt/(cash) | 227.0 | 272.2 | 296.1 | 315.1 | 311.5 |

Source: Ocean Wilsons, Edison Investment Research

### Exhibit 15: Ocean Wilsons debt structure

| US$m | 2012 | 2013 | 2014 | 2015e | 2016e |
|---|---|---|---|---|---|
| Short-term debt and finance leases | 36.7 | 39.5 | 52.6 | 52.6 | 52.6 |
| Long-term debt and finance leases | 326.9 | 339.2 | 347.2 | 349.6 | 357.7 |
| **Total debt** | **363.7** | **378.8** | **399.9** | **402.3** | **410.4** |
| Cash and cash equivalents* | 156.7 | 139.5 | 127.8 | 111.1 | 122.9 |
| **Net debt** | **207.0** | **239.2** | **272.1** | **291.1** | **287.5** |
| Share of JV debt | 208.5 | 250.9 | 257.4 | | |
| **Net debt including WSUT joint venture share** | **415.5** | **490.1** | **529.5** | | |
| OCN net debt/equity | 28% | 31% | 35% | 37% | 34% |
| OCN + WSUT JV share net debt/equity | 56% | 64% | 69% | | |

Source: Ocean Wilsons, Edison Investment Research. *Note: cash and cash equivalents in this table include short-term investments held in Wilson Sons which are intended to fund operations in Brazil.

**EDISON**

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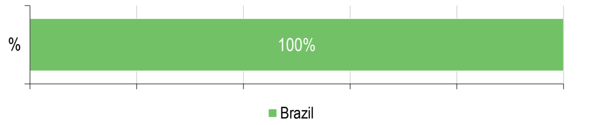
**Revenue by geography**




**Management team**

**Chairman: José Francisco Gouvêa Vieira**

Mr Gouvêa Vieira has been the managing director of Gouvêa Vieira Advogados since 1971. He has been a director of Ocean Wilsons since 1991 and chairman of the board since 1997. He is also chairman of Wilson Sons and a member of the boards of several companies, including PSA Peugeot Citroen do Brasil and Concremat Engenharia.

**Independent non-executive director: Andrés Rozental**

Mr Rozental is a political and economic consultant to Mexican and foreign companies. He was a Mexican diplomat for more than 35 years, holding a number of senior ambassadorial diplomatic posts. He is a director of Wilson Sons, chairman of ArcelorMittal Mexico, a director of ArcelorMittal Brazil and on the Advisory Board of Kansas City Southern de Mexico.

**Deputy chairman: William Salomon**

Mr Salomon was chairman of Rea Brothers, then deputy chairman of the investment division of Close Brothers from 1999. He is a director of Wilson Sons, chairman of Hanseatic Asset Management (the OWIL investment manager), senior partner in Hansa Capital Partners, chairman of New India Investment Trust and a director of Hansa Trust.

**Finance director: Keith Middleton**

Mr Middleton worked for a number of international companies before joining Ocean Wilsons Holdings in 1996. He is currently the executive director of Ocean Wilsons Holdings and is a member of the New Zealand Society of Accountants.

| Principal shareholders (end 2014) | (%) |
|---|---|
| Hansa Trust | 26.4 |
| Codan Trust Company Limited and Helen Cooper (Mr W. Salomon has an interest in these shares) | 12.5 |
| Peter A S Pearman and Codan Trust Company Limited (Mrs C. Townsend has an interest in these shares) | 11.1 |
| Utilico Emerging Market Utilities | 6.7 |

**Companies named in this report**

Santos Brasil (STBP11 BZ), JSL (JSLG3 BZ), China Merchant (144 HK), Dalian Port (2880 HK), Far Eastern Shipping (FESH RM), Hamburger Hafen (HHFA GR), NCB Holdings (NCB MK), Port of Tauranga (POT NZ), Sinotrans (598 HK).