

Toll company set to release results

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Toll road operator Transurban is set to release its results tomorrow, with some critics saying the company has not learned from mistakes of the past.

Transcript

TICKY FULLERTON, PRESENTER: Toll road operator Transurban releases its interim results tomorrow and investors will no doubt be keen to see the company's strategy for managing its large debts and increasing distributions.

Transurban polarises opinions. Some predict a bright future on the back of high-quality assets such as the Melbourne CityLink Road, while others believe that it hasn't learned from its past mistakes.

Andrew Robertson reports.

ANDREW ROBERTSON, REPORTER: There's an old saying on the stock market that in the long term, price follows value. If that's true, many investors don't think highly of the value of heavily-indebted toll road operator Transurban.

ROGER MONTGOMERY, MONTGOMERY INVESTMENT MANAGEMENT: It's still in business because the revenue is sufficient to meet the expenses and also the dividends that they're paying, but if interest rates were to go up a lot, then clearly that debt burden - the feeling of that debt becomes more acute.

ANDREW ROBERTSON: That long-term debt stands at nearly \$5.5 billion after a decade-long expansion program. The drive to get bigger brought nine years of, at times, heavy losses which finally ended with last year's profit of \$59 million. Return on equity is just 1.5 per cent after many years of being negative.

Tellingly, Transurban's share price has gone up just 20 per cent since February 2001.

STEVEN JOHNSON, FUND MANAGER, THE INTELLIGENT INVESTOR: My argument is that it would have gone up 60, 70 per cent if they had just stuck to that original asset that they had owned.

But they've bought assets in US, they've bought assets all around Australia, and they participated in that infrastructure boom at the top when prices were extremely high, and that has cost security holders a lot of money.

ANDREW ROBERTSON: Transurban began life as the owner of Melbourne's CityLink tollway, the asset Steve Johnson believes should have been its soul focus. It's now either the owner or a big stakeholder in Sydney's M2, M5 and M7 motorways, as well as the Lane Cove Tunnel and the Eastern Distributor. And there are two motorways in the United States.

ROGER MONTGOMERY: The biggest issue is that the company owns roads that ultimately have to be handed back to the Government debt-free at some point in the future. So, they have to do a number of things: maintain the dividends, they have to grow revenue sufficient to actually either maintain the dividends or grow the dividends, and they have to pay down that debt, otherwise they'll end up holding the debt, but not the road.

ANDREW ROBERTSON: Like Roger Montgomery, Steven Johnson is a fund manager who refuses to invest in Transurban. His biggest fear is that chief executive Chris Lynch is paid \$6 million a year, a pay packet he may feel the need to justify with more big expansionary deals, which will either further dilute security holder interests or add to the mountain of debt, or both.

STEVEN JOHNSON: I still don't think this board has really learnt the lessons of the mistakes of the past 10 years. No-one wants to sit there and be on the board of a business that's really boring - or not many people want to do that, anyway. That's what we need this board to do now: is just to sit there, collect the cash and hand it over to shareholders.

ANDREW ROBERTSON: But Transurban does have its fans, such as Austock's securities infrastructure analyst Andrew Chambers, who rates the company his key pick for 2011. He says most of Transurban's acquisitions have been sensible.

ANDREW CHAMBERS, INFRASTRUCTURE ANALYST, AUSTOCK SECURITIES: They spend billions of dollars upfront to produce cash flow streams that will last 30 or 40 years, and hence you get significantly more cash generation than you do accounting profits in the early life of the asset.

ANDREW ROBERTSON: A view supported by Transurban's latest annual report which showed free cash flow, which is cash available after paying all expenses plus the costs of investing in the business, had jumped 27 per cent to \$356 million.

It's the reason why Andrew Chambers believes the statutory profit numbers reported by Transurban, which paint a very different picture, are misleading.

ANDREW CHAMBERS: A classic example would be when Transurban owned half of the M7 and Macquarie Infrastructure Group owned half of the M7, you've obviously got the same asset ownership, and yet Transurban would report losses on that through their accounts and MIG would report profits when they revalued it upwards. So, you've got exactly the same asset with two completely different statutory outcomes.

ANDREW ROBERTSON: Andrew Chambers is expecting a significant upward re-rating in Transurban's securities over the next 18 months to two years.

TICKY FULLERTON: And we'll be talking to Transurban's CEO Chris Lynch on tomorrow night's program.