FORSYTH BARR

WEALTH MANAGEMENT RESEARCH

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Wealth Weekly
What's on the Menu?

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With tech companies rushing to list on public exchanges, Initial Public Offerings (IPOs) have been a hot topic overseas. That heat hasn't quite extended to the New Zealand market. Meal kit provider My Food Bag IPO'ed at $1.85 in early March and the stock price subsequently dropped as low as $1.52.

My Food Bag a grocery disruptor

We have now initiated coverage on My Food Bag with an OUTPERFORM rating and a 12 month target price of NZ$1.85. MFB offers investors exposure to a developing segment of the defensive food retail space. While the product premise appears similar to that of an online grocer, we believe delivered meal kits are a lifestyle product and offer a value proposition to the customer beyond convenience and price. We see room for My Food Bag to further disrupt the traditional grocery and foodservice markets. We are attracted to 1) the company's strong cash generation, 2) demographic trends towards convenience and online product offerings, 3) future growth opportunities in adjacent markets, and 4) the stock's attractive valuation at a -24% discount to the market.

Themes of the week

We expect near-term upside potential to earnings of Air New Zealand, Auckland Airport and Tourism Holdings as a result of the commencement of two-way, quarantine-free, travel across the Tasman from next Monday. While reopening sentiment is a positive short-term catalyst, we expect the reality of reopening and residual uncertainty about potential border closures at short notice to limit enthusiasm for the stocks, and investor focus will ultimately revert back to fundamentals. Given their valuations, we are NEUTRAL-rated on all three tourism-related transport stocks.

Pacific Edge stock jumped +21% on Friday (bringing it back up to its December peak) after the company announced **the US's largest private health insurer, UnitedHealth, will reimburse Pacific Edge's bladder cancer tests**. The company on Monday announced its long-standing CEO plans to retire in April 2022. Our rating remains OUTPERFORM, but we regard the stock as higher risk.

The momentum/trajectory in Pushpay's business appears to have taken a turn for the worse, with our estimates suggesting a reduction in its share of the top 100 churches and slower growth in customer numbers than competitors. Following a solid run in the share price we have downgraded the stock from NEUTRAL to UNDERPERFORM.

On Wednesday the Reserve Bank of New Zealand (RBNZ) is expected to announce that it will leave the Official Cash Rate (OCR) unchanged at 0.25%. Given the strong global recovery, the market will focus on the commentary that comes with it. Currently, the market is pricing in no OCR hikes in 2021. After rising for two months, wholesale interest rates have stabilised, but further increases wouldn't be a surprise as the US continues to add more fiscal fuel to the economy's recovery fire.

Looking ahead

Earnings season gets underway in earnest this week with several major US banks (JPMorgan Chase, Wells Fargo and Goldman Sachs) due to report earnings on Thursday, NZ time, followed by Bank of America and Citigroup on Friday, together with Pepsico, UnitedHealth Group and Taiwan Semiconductor. US and Eurozone consumer price inflation will be in focus on Tuesday and Thursday,

My Food Bag (MFB.NZ)

A Winning Recipe?

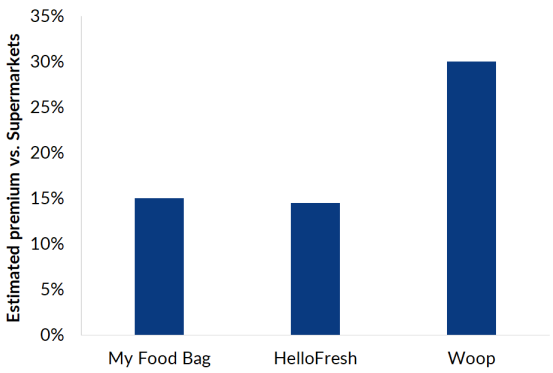
My Food Bag (MFB) is a meal-kit company. It began trading in 2013 and has expanded its service across New Zealand, with deliveries able to reach 86% of New Zealand. MFB makes weekly deliveries of its food boxes, which contain recipes and ingredients to make dinner meals. MFB's broad range of products service an array of nutritional and budget requirements. Its key brands include My Food Bag, Bargain Box, Fresh Start, and ready made meal offering MADE.

Small share of big market

MFB's FY21E annual sales of $189.5m represents 2.5% of the estimated $7.6b market for dinner spending (Figures 2 & 3), or 9% of the NZ$2.2b market after adjusting for a meal-kit utilisation rate of 30% (4 meals a week for 26 weeks a year).

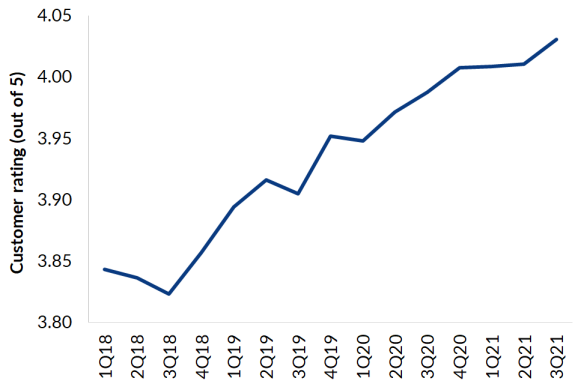
The NZ meal-kit industry is dominated by three players; MFB, HelloFresh (HFG) and Woop. Anecdotes suggest that HFG recently surpassed MFB as the largest player by customer numbers, with Woop holding significantly less share. Supermarket participation in the meal-kit market has been fairly muted to-date. The meal-kit offering commands a varying premium versus the price of an equivalent basket of goods from supermarkets, on our analysis (Figure 1). A premium is justified by: 1) the convenience, 2) the quality (Figure 2), and 3) the recipes. (MFB's analysis suggests its bags are priced in line to below supermarkets).

Figure 1. Meal kit premium to supermarkets



Source: Company websites, Forsyth Barr analysis

Figure 2. Customer meal rating (out of 5)

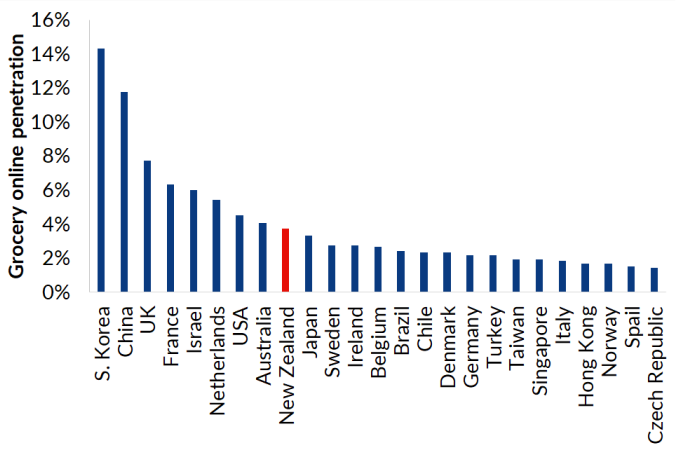


Source: MFB, Forsyth Barr analysis

Activating the customer reservoir

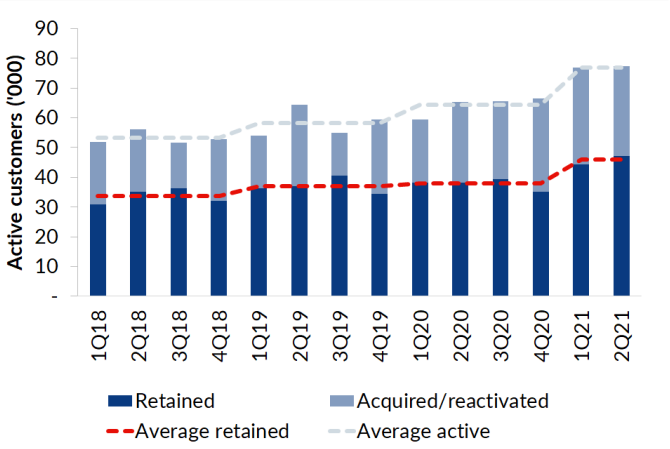
COVID-19 accelerated growth in the customer base, with lockdowns driving, 1) a shift in the share of consumption towards the home, and 2) higher adoption of online grocery (Figure 4). We expect the rapid growth phase of meal-kit adoption has now passed. With MFB having served 85m meals to over 300,000 individual customers (c.17% of New Zealand households) since inception, we expect customer acquisition growth to moderate to a steadier pace.

Figure 3. Online grocery penetration (pre COVID-19)



Source: Euromonitor, Statista, Forsyth Barr analysis

Figure 4. MFB quarterly active customers



Source: Forsyth Barr analysis

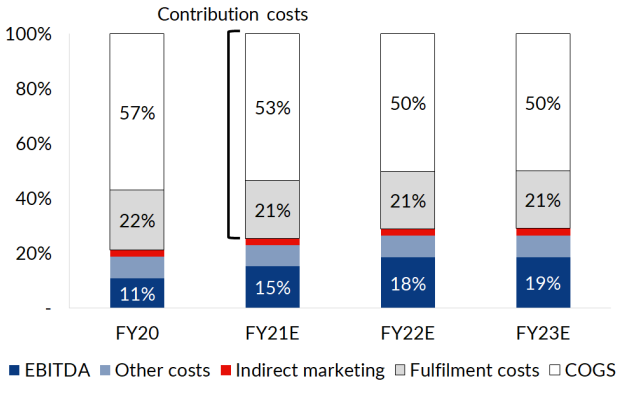
Growth will be dictated by MFB's ability to maximise sales to its customer reservoir. We view shifts towards more flexible (My Choice) and goal based (Fresh Start) offerings as key drivers of the strategy.

Future growth opportunities include using its brand to cross sell and expand into additional channels or product categories. These represent significant market opportunities beyond our three-year forecast period, representing upside to our base valuation.

Margin expansion significant, but not out of step with peers

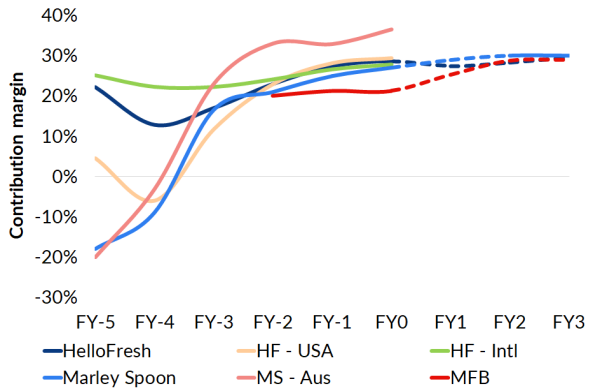
The company expects to be able to grow near-term earnings primarily by expanding its profit margins through 1) improved product pricing, 2) favourable product mix changes, and 3) better procurement contract terms which are expected to unleash a material reduction in cost per bag. The expect uplift in margins is in line with those seen at global meal-kit peers (Figures 5 & 6).

Figure 5. Cost/margin breakdown over forecast period



Source: MFB, Forsyth Barr analysis

Figure 6. Contribution margin following similar trends



Contribution margin = selling price minus variable cost per unit

Source: MFB, Forsyth Barr analysis

Valuation attractive

Comparison of valuations with internationally listed meal-kit companies are complicated by their differing growth stages. MFB currently trades on a 12 month forward price/earnings multiple of 17.5x on our estimates, a -24% discount to the market median (22.9x), which we view as attractive given MFB's growth characteristics and strong cash generation.

For our in-depth analysis on MFB, see our initiation report, *A Winning Recipe? - Initiate at OUTPERFORM*, published on 8 April 2021.

Figure 7. MFB SWOT (Strengths, Weaknesses, Opportunities, Threats)

Strengths	**Weaknesses**
Wide product offering	Lack of track record as listed company
Strong brand	Price conscious target audience
Recyclable packaging	Smaller basket size and more limited choice relative to supermarkets
Customer service	Susceptible to food safety and brand risks
Supports local businesses	
Opportunities	**Threats**
Online grocery penetration growing	Moderate barriers to entry
Different meals (lunch/breakfast)	Supply chain risks
Society growing increasingly health conscious	Commodity price pressure
Buying power improves with scale	Growth in other alternatives (Uber eats)
Potential to enter other markets or add new products	Competition is large and well capitalised

Source: Forsyth Barr analysis

Themes of the Week

NZ Equities

Transport & Tourism Sectors — Breathing Life into the Trans-Tasman Bubble

We anticipate a strong demand response to the inflating of the travel bubble, particularly from the visiting friends and relatives (VFR) cohort. Pent up demand will also be a driver of the leisure segment. But we expect overall trans-Tasman traffic to be at a modestly lower level than pre COVID-19 because of the government's "flyer beware" message, reluctance by vulnerable people to risk infection, and the lack of travellers accessing international connections beyond the Tasman.

Pure-Tasman passengers (excluding transferring passengers) represented ~30% of **Auckland Airport's (AIA)** total international passengers in FY19. The high incremental margin of aeronautical and commercial activities at airports means that a meaningful increase in passenger numbers will drive a significant improvement in profitability. We estimate a monthly loss of ~-NZ$4m could swing to ~NZ$16m net profit per month for AIA in a scenario of Tasman demand returning to pre COVID-19 levels, driven by aeronautical and retail income. Assuming the bubble evolves into a broader aviation recovery, there should no longer be any concerns over AIA's next covenant test at 30 June 2022. Our rating on AIA remains NEUTRAL.

Early indications suggest **Air New Zealand (AIR)** will initially run its trans-Tasman operation at 70%–110% of pre COVID-19 capacity, depending on the route. We expect AIR will continue to burn cash but at a reduced level of perhaps NZ$15m–NZ$25m per month, about NZ$30m per month below 2H21 guidance. However, the rate of cash burn would deteriorate from October 2021 following the end of the government's PAYE deferral scheme. Losses would continue but the rate of net asset value (NAV) dilution would halve to ~1.5cps per month. The opening of the bubble is a timely boost ahead of AIR's capital raise, which the company has now deferred by up to three months, to sometime before the end of September. On a separate note, the government's letter to AIR's board was a reminder of the government's expectations of the company as a majority shareholder, and a signal of its willingness to become more active in that role if those expectations are not met. Our rating is NEUTRAL.

Tourism Holdings (THL) has less to gain from a trans-Tasman bubble than AIA and AIR. Demand for THL's recreational vehicles (RVs) tends to be concentrated around the summer season and historically came more from long-haul travellers than from Australians. We'd expect THL to increase its Tasman demand profile compared to pre COVID-19 given available capacity, more attractive pricing and its dynamic, commercially minded, sales approach. Consequently, we do expect some increase in demand, which will partially offset material 2H21 losses and further NAV dilution.

Pacific Edge (PEB.NZ) — Further Progress in Battle of David vs Goliath

The announcement that UnitedHealth (UNH), the largest US private health insurer, will cover PEB's Cxbladder Detect and Monitor cancer tests for Medicare Advantage clients (5.7m people), is another important external validation of PEB's potential in the key US market. This follows PEB reaching a commercial agreement with Facey Medical Group, a Californian physician group covering 170,000 patients. We do not know what price UNH and Facey Medical will pay, but expect both to be above the US$760/test paid by public health insurer CMS.

We have not made any changes to our forecasts as our base case forecasts already incorporate progress with private insurers. However, as PEB continues to make further commercial progress this helps to increase our confidence in the revenue path, and lower the risk. There is no short-cut to changing clinical practice and the hard work is far from over. The US market opportunity is extensive and we see PEB as well positioned to capitalise on this.

The range of possible long-term outcomes for PEB is wide. **We expect the share price to continue to be driven by newsflow** — which is likely to be positively skewed as further commercial progress follows recent success. OUTPERFORM.

Pushpay (PPH.NZ) — Debunking the Myths: Downgrade to U/P

During the greatest ever year for demand in church technology, we fully expected PPH to capitalise on its dominant position in the US church payments software market based on its previous track record, positive feedback from customers, its product advantage over competitors, and the growth of the underlying market.

Instead, our recent research suggests that **over the past twelve months PPH has lost significant ground to its competition**. Rival Tithe.ly grew its churches by 12,000 in the same period as PPH grew by 309. On our estimates, PPH's penetration of the top 100

churches has fallen from 58 in July 2020 to 52 as of March 2021. We believe much of this is linked to PPH increasing its already premium price.

We have raised our FY22 revenue growth forecast from +8.6% to +9.9% and increased our target price from NZ$1.75 to NZ$1.83. Following a re-rating of the stock, **PPH now trades on a valuation multiple that looks expensive** considering the level of revenue growth we anticipate. We have downgraded our rating to UNDERPERFORM based on 1) strong share price performance, 2) PPH's focus on the limited Catholic market, 3) customer churn among the top 100 US churches, and 4) increasing competitive pressures.

Fixed Interest

Data dependant Central Banks

The Reserve Bank of New Zealand (RBNZ) meets on Wednesday to review the Official Cash Rate (OCR). While **no change to the current 0.25% OCR is expected**, the accompanying 400-odd words will be of interest to many given the remarkable global recovery underway. Market pricing suggests there will be no OCR hikes in 2021. If things continue on the current trajectory, will 2022 be the year?

Next week the all-important **Q1 inflation figures will be released. Both the RBNZ and the market expect a reading of around +1.0%** (year-on-year), however, where inflation is heading remains the key. The International Monetary Fund (IMF) has revised up its global growth forecasts again after increasing US GDP growth forecasts for 2021 from +5.1% to +6.4%.

Wholesale interest rates are taking somewhat of a breather after a couple of months of hefty rises, however, further increases cannot be ruled out when the US keeps adding to its already incredibly large fiscal stimulus.

As economic data is released and vaccine success stories evolve, the "data dependant" US Federal Reserve may hold the key to long-term interest rates around the globe.

Research Worth Reading

New Zealand

Power Points — Pressures Rising — April 2021

We see increasing pressures in the electricity sector, with hydro storage levels declining to their lowest level for this time of year (58% of average) since the wholesale electricity market began, and this is being reflected in wholesale and near-term futures prices (both above NZ$230/MWh). Whilst we believe the electricity market is generally performing as expected, we also expect regulators and politicians are keeping a close watch on the sector. The other area of focus is the S&P Global Clean Energy Index, which is set to rebalance after close on 16 April, resulting in unprecedented selling by ETF index trackers of Contact Energy (CEN) (~72m shares) and Meridian Energy (MEL) (~100m shares). Overall, we are neutral on the sector. That said, our preferred pick, Contact Energy (CEN), is attractive. It is trading on undemanding multiples and has a healthy and growing gross dividend yield of 6.5% (OUTPERFORM). Genesis Energy (GNE) is also rated OUTPERFORM and is in the best position to take advantage of current dry hydro conditions. Our least preferred stock is Meridian Energy (MEL) (UNDERPERFORM). Whilst recent price declines mean MEL offers better value than it has for a while, it faces a tough finish to FY21 and dividend growth is likely to be muted. (Published by Forsyth Barr)

Real Estate Reflections — Internalisations — Have They Delivered?

The listed property vehicles (LPVs) were flat and underperformed the broader S&P/NZX 50 in March, with higher bond yields continuing to weigh on investor sentiment. Precinct's (PCT - OUTPERFORM) internalisation of its management contract was the most notable event in the sector this month and in this report we review the operating cost performance of other internalised LPVs. Our analysis suggests that internalisations delivered shareholder value, however, benefits vs. prior externally managed structures are slowly being eroded by cost creep. Also, the pricing of PCT's internalisation highlights the value of management contracts in the current market, with Stride Property Group (OUTPERFORM - the only LPV that incorporates an asset management platform of scale) being the key beneficiary in the sector. (Published by Forsyth Barr)

Australia

Amcor (AMC.AX) — North America beverage data

North America beverage volumes remain a key focal point for AMC, and Nielsen released data for the four weeks to 27 March. Sales volumes in the period were lower year-on-year in both the beverages and packaged food segments. But this reflects pantry-loading in March last year, while on a two-year stack basis, sales volumes were solidly higher. In Ord Minnett's view, the near-term outlook for AMC has turned more negative as tougher comparable numbers for food and beverage packaging begin, while at the same time demand for healthcare packaging may remain subdued as COVID-19 weighs on demand for medical devices and pharmaceutical products. In addition, Ord Minnett flagged that input costs are likely to remain a temporary headwind. ACCUMULATE. (Published by Ord Minnett)

Aristocrat Leisure (ALL.AX) — Game performance and earnings revisions

Ord Minnett has conducted a detailed review of ALL's game performance using Apptopia metrics and the company's library of games. Ord Minnett's key finding was that downloads and daily average user (DAU) numbers of social casino apps (Lightening Link and Cashman Casino) during the first half of FY21 performed better-than-category. This has more than offset fewer downloads of social casual games, such as RAID, although in-game monetisation and bookings in this category have tracked progressively higher despite fewer downloads. Ord Minnett's FY21 earnings forecast has increased +5.8%. ALL has strong recurring revenues and has been consistently gaining market share in North America gaming operations. Ord Minnett sees further digital growth and capital management opportunities, coupled with strong execution by management. Real money gaming (RMG) remains an opportunity and Ord Minnett continues to believe the risk-reward balance is attractive at these levels. ACCUMULATE. (Published by Ord Minnett)

Macquarie Group (MQG.AX) — APRA action for breaches of reporting standards

The Australian Prudential Regulation Authority (APRA) announced it was taking action against MQG in response to multiple material (historical) breaches of APRA's prudential and reporting standards related to intra-group funding arrangements between 2018 and 2020. APRA will require MQG to add: 1) an operational capital overlay of A$500m; 2) a 15% add-on to the net cash outflow

component of its liquidity coverage ratio (LCR) calculation; and 3) a 1% adjustment to the available stable funding component of its net stable funding ratio (NSFR) calculation. MQG's capital, liquidity and funding metrics are already well above regulatory minimum requirements. ACCUMULATE. (Published by Ord Minnett)

South32 (S32.AX) — SAEC sale update

S32 announced further details on the South African Energy Coal (SAEC) transaction: 1) The upfront payment by Seriti will be nominal and the deferred consideration mechanism has been removed. 2) S32 will now need to pay US$200m towards rehabilitation costs via 10 annual instalments (about US$175m discounted). 3) S32 will lend US$50m to Seriti to fund loss-making mining areas. Additionally, S32 will guarantee a US$120m facility that Seriti has entered into with a South African bank. BUY. (Published by Ord Minnett)

International

Apple (AAPL.O) — Focus on Capital Deployment & iPhone Share Gains

AAPL's shares have underperformed the broader markets but this follows significant outperformance in 2020. Aside from broader macro rotation from growth to cyclical stocks, underperformance can be attributed to news flow on order cuts (mainly tied to iPhone 12 mini) and uncertainty around iPhone demand momentum, as well as antitrust concerns that could potentially derail Services growth momentum and negatively impact earnings. Citi's checks continue to suggest underlying demand fundamentals across consumer tech demand and App Store remains robust. Citi views the regulatory concerns as headline risks that are unlikely to be resolved soon. Looking ahead, Citi believes AAPL's shares are attractive given the revenue diversification, unique product and service set, strong cash flow generation, potential to enter other large markets (electric vehicles) and shareholder returns. BUY. (Published by Citi)

Roche (ROG.S) — Raising faricimab Forecasts on Stellar US Survey Feedback. Remain Buy.

Citi's recent survey of 52 US retinal surgeons reflected a far greater knowledge and enthusiasm for ROG's faricimab than Citi had previously expected following the phase III non-inferiority data. Citi's survey suggests that ROG's faricimab is set to take c.35-40% market share in wet age-related macular degeneration, primarily at the expense of Regeneron's Eylea (39% falling to 14%). Citi has increased its faricimab sales forecasts from c.CHF500m to c.CHF3b (consensus c.CHF1.5b). Citi has increased its core EPS forecasts c. +7% in 2029, with significant faricimab revisions partially offset by anticipated increases in core tax rate given the Biden administration's proposed tax reforms. BUY. (Published by Citi)

Sanofi (SASY.PA) — Still liking the risk/reward; new disclosures and Cleveland Clinic feedback worth flagging

Despite recent outperformance, Citi still likes the risk/reward offered by Sanofi. Citi continues to argue a transition from perennial value trap to growth at a reasonable price is underway, underpinned by a robust balance sheet and group structure that has scope to unlock significant value. Citi believes the key issues holding the shares back are poor perceptions of the drug development pipeline, and the market viewing mRNA technology as a disruptor rather than growth driver for Vaccines. Citi sees scope for this to change through 2021 on the back of data read-outs. Citi forecasts a 2020-25 EPS compound annualised growth rate of +12%, underpinned by the Dupixent/Vaccines growth story driving +500bps of EBIT margin expansion. BUY. (Published by Citi)

Calendar

Figure 8. Calendar

Date	New Zealand	Australia	International
13-Apr	NZIER Business Confidence (1Q) NZIER QSBO Capacity Utilisation (1Q)	NAB Business Confidence (Mar) HIA New Home Sales	UK: GDP UK: Manufacturing Production (Feb) EU: German ZEW Economic Comment (Apr)
14-Apr	Electronic Card Retail Sales (Mar) Permanent/Long-term Migration (Feb) RBNZ Interest Rate Decision	Westpac Consumer Sentiment (Apr)	US: Core CPI (Mar)
15-Apr	External Migration & Visitors (Feb) Food Price Inflation (Mar)	Melbourne Institute Inflation Expectations Employment Change (Mar) Unemployment Rate (Mar) Participation Rate (Mar)	US: Crude Oil Inventories Goldman Sachs 1Q21 JPMorgan Chase 1Q21 Wells Fargo 1Q21
16-Apr	Business NZ PMI (Mar) NZME AGM		US: Retail Sales (Mar) US: Initial Jobless Claims US: Philadelphia Fed Manufacturing Index (Apr) CN: GDP (1Q) CN: Industrial Production (Mar) EU: CPI (Mar) Bank of America 1Q21 BlackRock 1Q21 Citigroup 1Q21 PepsiCo 1Q21 Taiwain Semiconductor 1Q21 UnitedHealth Group 1Q21
17-Apr	CFTC NZD Speculative Net Positions	CFTC AUD Speculative Net Positions	US: Building Permits

Source: Forsyth Barr analysis

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