

AFT Pharmaceuticals

NZ\$12m Equity Raise

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RESEARCH INSIGHTS

AFT Pharmaceuticals (AFT) has announced that it is undertaking an NZ\$12m equity raise to retire one of AFT's working capital facilities, improve free cash flow and provide more flexibility to fund future anticipated growth. The equity raise, at a floor price of NZ\$3.65 per share, consists of (1) an underwritten NZ\$10m placement, and (2) a non-underwritten NZ\$2m Share Purchase Plan (SPP). In addition, AFT are undertaking a secondary sale of shares, being: (1) ~NZ\$3.5m worth of shares held by the Atkinson Family Trust, and (2) 16m of existing shares held by Capital Royalty Group (CRG), representing ~1.3% and 100% of current holdings respectively.

NZX Code	AFT	Financials: Mar/	20A	21E	22E	23E	Valuation (x)	20A	21E	22E	23E
Share price	NZ\$4.70	NPAT* (NZ\$m)	2.9	12.3	18.3	27.6	EV/EBITDA	40.3	26.7	17.8	12.2
Issued shares	100.5m	EPS* (NZc)	3.0	12.2	18.2	27.5	EV/EBIT	44.2	28.7	18.7	12.7
Market cap	NZ\$472m	EPS growth* (%)	n/a	n/a	48.9	50.8	PE	n/a	38.4	25.8	17.1
Avg daily turnover	25.4k (NZ\$96k)	DPS (NZc)	0.0	0.0	0.0	0.0	Price / NTA	n/a	n/a	29.4	11.4
		Imputation (%)	0	0	0	0	Cash div yld (%)	0.0	0.0	0.0	0.0
		*Based on normalised profits					Gross div yld (%)	0.0	0.0	0.0	0.0

Capital raise – strengthening the balance sheet

The proceeds of AFT's NZ\$12m capital raise will be used to retire one of its working capital facilities. This is expected to:

- Reduce annual interest costs: AFT expects interest costs to be reduced by ~NZ\$0.85m per annum.
- Lower gearing: Pro-forma FY20 net debt will reduce to NZ\$25m (from NZ\$37m), lowering net debt to expected FY21 EBITDA to 1.5x (prior 2.3x), based on the company's guidance mid-point.
- Provide more flexibility to fund future anticipated growth.

AFT has indicated an immediate focus on targeting net debt of NZ\$23–28m, which this raising is expected to achieve, while the potential for a dividend policy will be assessed in FY22.

Secondary sale – materially lifts the free float

AFT's two majority shareholders, the Atkinson Family Trust and CRG, have taken the opportunity on the back of "significant investor interest" to sell down. This will substantially increase free float from ~11% to ~31%.

- **The Atkinson Family Trust:** This is the investment vehicle for AFT's founders, and current executives, Hartley and Marree Atkinson and has not sold a share since the 2015 Initial Public Offering (IPO). The sell-down is ~1.3% of its current holding. The Atkinson Family Trust will remain the largest shareholder post transaction at ~69%, and indicated no current intention to sell further shares.
- **CRG:** Is selling ~16m shares, or 100% of its holding in AFT. CRG has been an AFT shareholder since 2014 (pre-IPO), however, the CRG fund where AFT is held has moved out of its investment phase, with CRG now returning capital to investors.

Forsyth Barr Limited is a Joint Lead Manager of the Placement and SPP and Forsyth Barr Group Limited an Underwriter of the Placement and will receive fees in connection with those roles.

Our forecasts for FY21E and beyond have not been updated to reflect the announcement.

AFT Pharmaceuticals (AFT)

Priced as at 10 Jun 2020 (NZ\$)

4.70
Research Insights

Forsyth Barr Research Insights focuses on qualitative rather than quantitative assessments of an equity investment.

We do not provide valuation, target prices or investment ratings for companies in the Research Insights series. It is targeted at selected smaller cap stocks with typically higher risk attributes, or those under transitional coverage.

Our earnings and cashflow forecasts, together with key valuation and ratios provided on this page should assist investors in determining the relative valuation merits of the company.

Profit and Loss Account (NZ\$m)	2019A	2020A	2021E	2022E	2023E	Valuation Ratios	2019A	2020A	2021E	2022E	2023E
Sales revenue	85.1	105.6	124.8	150.4	183.5	EV/EBITDA (x)	72.1	40.3	26.7	17.8	12.2
Normalised EBITDA	7.0	12.6	18.9	28.2	41.1	EV/EBIT (x)	75.6	44.2	28.7	18.7	12.7
Depreciation and amortisation	(0.3)	(1.1)	(1.3)	(1.4)	(1.4)	PE (x)	n/a	>100x	38.4	25.8	17.1
Normalised EBIT	6.6	11.5	17.6	26.9	39.7	Price/NTA (x)	n/a	n/a	>100x	29.4	11.4
Net interest	(8.4)	(8.3)	(3.2)	(2.4)	(1.3)	Free cash flow yield (%)	-1.3	1.2	1.4	2.2	3.4
Associate income	(0.5)	(0.1)	0	0	0	Net dividend yield (%)	0.0	0.0	0.0	0.0	0.0
Tax	(0.2)	(0.2)	(2.2)	(6.1)	(10.7)	Gross dividend yield (%)	0.0	0.0	0.0	0.0	0.0
Minority interests	0	0	0	0	0						
Normalised NPAT	(2.4)	2.9	12.3	18.3	27.6	Capital Structure	2019A	2020A	2021E	2022E	2023E
Abnormals/other	0	9.8	0	0	0	Interest cover EBIT (x)	0.8	1.4	5.6	11.0	30.3
Reported NPAT	(2.4)	12.7	12.3	18.3	27.6	Interest cover EBITDA (x)	0.8	1.5	6.0	11.6	31.4
Normalised EPS (cps)	(2.5)	3.0	12.2	18.2	27.5	Net debt/ND+E (%)	n/a	n/a	n/a	n/a	n/a
DPS (cps)	0	0	0	0	0	Net debt/EBITDA (x)	5.0	2.9	1.6	0.7	0.1
Growth Rates	2019A	2020A	2021E	2022E	2023E	Key Ratios	2019A	2020A	2021E	2022E	2023E
Revenue (%)	4.9	24.0	18.2	20.6	21.9	Return on assets (%)	10.4	13.2	18.5	25.1	32.1
EBITDA (%)	n/a	81.2	50.1	49.1	45.7	Return on equity (%)	-47.7	16.9	41.6	38.3	36.6
EBIT (%)	n/a	73.3	53.3	52.3	47.7	Return on funds employed (%)	22.7	22.0	25.4	30.6	38.3
Normalised NPAT (%)	n/a	n/a	>100	48.9	50.8	EBITDA margin (%)	8.2	11.9	15.2	18.7	22.4
Normalised EPS (%)	n/a	n/a	>100	48.9	50.8	EBIT margin (%)	7.8	10.9	14.1	17.8	21.6
Ordinary DPS (%)	n/a	n/a	n/a	n/a	n/a	Capex to sales (%)	4.1	3.3	2.4	2.0	1.6
						Capex to depreciation (%)	3,013	426	359	350	342
Cash Flow (NZ\$m)	2019A	2020A	2021E	2022E	2023E	Imputation (%)	0	0	0	0	0
EBITDA	7.0	12.6	18.9	28.2	41.1	Pay-out ratio (%)	0	0	0	0	0
Working capital change	(4.7)	1.0	(4.0)	(6.0)	(10.2)						
Interest & tax paid	(3.7)	(6.1)	(5.3)	(8.5)	(12.1)	Operating Performance	2019A	2020A	2021E	2022E	2023E
Other	(1.1)	1.5	0	0	0	Revenue breakdown					
Operating cash flow	(2.5)	9.0	9.6	13.6	18.9	Australia	50.3	61.4	73.7	84.8	97.5
Capital expenditure	(3.5)	(3.5)	(3.0)	(3.0)	(3.0)	New Zealand	26.8	30.1	31.9	33.5	34.5
(Acquisitions)/divestments	0	0	0	0	0	SE Asia	2.1	4.9	5.0	5.8	6.3
Other	0	0	0	0	0	Rest of World	5.9	9.1	14.1	26.4	45.1
Funding available/(required)	(6.0)	5.5	6.6	10.6	15.9	Total revenue	85.1	105.6	124.8	150.4	183.5
Dividends paid	(0.1)	(0.1)	0	0	0	incl license income of	1.2	3.8	3.0	3.0	3.0
Equity raised/(returned)	0	0	0	0	0	Gross profit	40.7	48.3	57.7	69.6	84.5
(Increase)/decrease in net debt	(6.1)	5.4	6.6	10.6	15.9	Gross margin (%)	47.8	45.7	46.3	46.3	46.0
						Other income	2.2	0.5	0.1	0.1	0.1
Balance Sheet (NZ\$m)	2019A	2020A	2021E	2022E	2023E	Expenses breakdown					
Working capital	29.2	30.4	34.4	40.4	50.6	Selling & distribution	(26.5)	(26.2)	(27.3)	(28.3)	(29.2)
Fixed assets	0.4	0.3	0.3	0.3	0.3	General & admin costs	(7.2)	(9.1)	(10.5)	(12.0)	(13.3)
Intangibles	8.2	27.0	29.4	31.8	34.1	R&D expenses	(2.6)	(2.0)	(2.5)	(2.5)	(2.5)
Right of use asset	0	3.7	3.7	3.7	3.7	Total SG&A	(36.3)	(37.3)	(40.2)	(42.9)	(44.9)
Other assets	3.7	1.2	1.2	1.2	1.2						
Total funds employed	41.6	62.6	69.0	77.5	90.0	EBIT (pre abnormals)	6.6	11.5	17.6	26.9	39.7
Net debt/(cash)	34.8	37.1	30.5	19.9	4.0						
Lease liability	0	4.0	4.7	5.4	6.2						
Other liabilities	1.7	4.3	4.3	4.3	4.3						
Shareholder's funds	5.1	17.3	29.6	47.9	75.5						
Minority interests	0	0	0	0	0						
Total funding sources	41.6	62.6	69.0	77.5	90.0						

* Forsyth Barr target prices reflect valuation rolled forward at cost of equity less the next 12-months dividend

Investment Summary

AFT Pharmaceuticals (AFT) is a growing multinational pharmaceutical company that develops, markets and distributes an extensive portfolio of proprietary and licensed pharmaceutical products across a wide range of therapeutic categories. AFT has seen success to date developing and bringing products to market, primarily underpinned by over-the-counter product growth in Australia. The company is targeting further growth in its local markets but also through global expansion for its marquee Maxigesic product. AFT operates in an intensely competitive and highly regulated environment where delays to timelines are also commonplace.

Business quality

- **Strong track record:** AFT has a track record of revenue growth since inception and a growing track record of success and external validation, particularly in licensing agreements with third parties.
- **Experienced management team:** AFT's founders, Hartley and Marree Atkinson remain heavily involved in the business and are highly incentivised to drive performance with a 69% stake. The flipside is low liquidity for the stock given low free float.

Earnings and cashflow outlook

- **Australasia:** This is the key source of revenue currently. The company is looking to grow through (1) bringing new products to market from its large pipeline, and (2) operating leverage.
- **Global expansion:** Execution and success in International markets is the key growth engine for AFT. A key near-term priority is continuing to increase the number of countries where Maxigesic, and its line extensions, are sold.

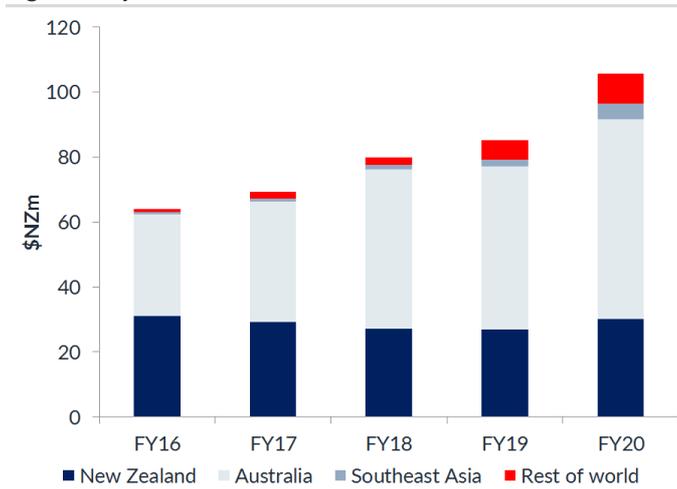
Financial structure

- **Recent debt refinancing, capital raise and return to profitability in FY20:** AFT expects this to deliver a material reduction in debt levels and interest costs. AFT has indicated an immediate focus on targeting net debt of NZ\$23-28m, while the potential for a dividend policy will be assessed in FY22.

Risk factors

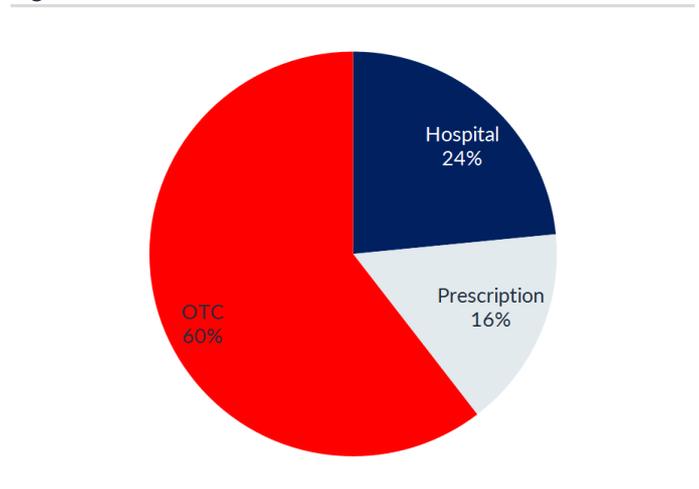
- **Regulation:** This can include changes in the backdrop, timing delays and/or unfavourable decisions.
- **Intellectual property (IP):** Details are opaque and vary between markets. Expiration of patents or IP infringement by competitors is a key risk.
- **Competition:** AFT operates in a highly competitive market. Any price discounting and/or superior product development could disrupt the market.

Figure 1. 5 year revenue breakdown



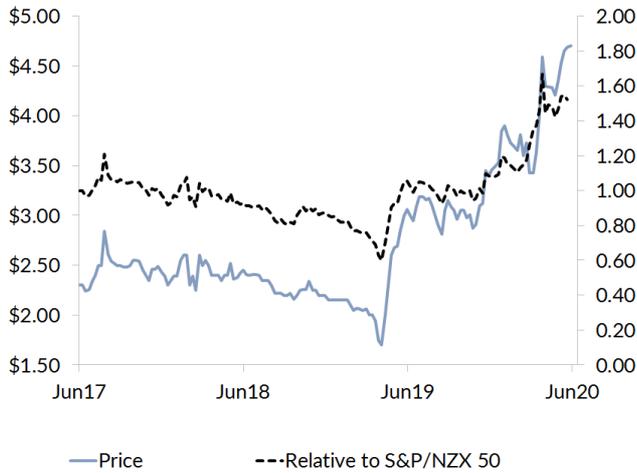
Source: Forsyth Barr analysis

Figure 2. FY20 distribution channel breakdown



Source: Forsyth Barr analysis

Figure 3. Price performance



Source: Forsyth Barr analysis

Figure 4. Substantial shareholders (pre sell down)

Shareholder	Latest Holding
Atkinson Family Trust	75.3%
The CRG Persons	16.0%

Source: NZX, Forsyth Barr analysis, NOTE: based on SSH notices only

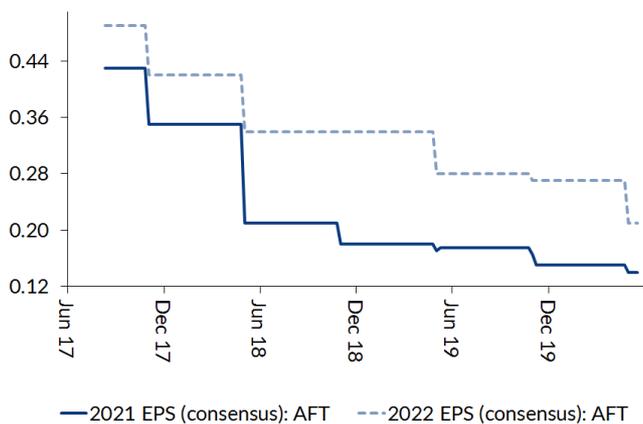
Figure 5. International valuation comparisons

Company	Code	Price	Mkt Cap (m)	PE		EV/EBITDA		EV/EBIT		Cash Yld	
				2021E	2022E	2021E	2022E	2021E	2022E		
(metrics re-weighted to reflect AFT's balance date - March)											
AFT Pharmaceuticals	AFT NZ	NZ\$4.70	NZ\$472	38.4x	25.8x	26.9x	18.1x	28.9x	19.0x	0.0%	
PROBIOTEC	PBP AT	A\$1.86	A\$139	13.8x	11.4x	9.0x	7.9x	11.3x	9.6x	3.8%	
GLAXOSMITHKLINE PLC	GSK LN	£16.43	£82,412	13.8x	13.2x	9.9x	9.5x	12.2x	11.7x	4.9%	
SANOFI	SAN FP	€90.46	€113,627	14.4x	13.2x	11.1x	10.0x	14.2x	12.9x	3.8%	
PFIZER INC	PFE US	US\$36.21	US\$201,141	12.7x	11.8x	11.0x	10.4x	13.0x	n/a	4.4%	
JOHNSON & JOHNSON	JNJ US	US\$145.96	US\$384,545	18.4x	15.9x	14.0x	12.3x	15.8x	13.6x	2.9%	
BAYER AG-REG	BAYN GR	€67.45	€66,265	9.3x	8.4x	8.4x	7.7x	13.2x	11.8x	4.6%	
ROCHE HOLDING AG-GENUSSCHEIN	RHHVF US	CHF347.20	CHF301,940	n/a	15.7x	12.0x	11.4x	13.5x	12.7x	2.8%	
MERCK & CO. INC.	MRK US	US\$82.26	US\$207,633	15.0x	13.5x	11.4x	10.3x	13.4x	11.9x	3.1%	
				Compco Average:	13.9x	12.9x	10.8x	9.9x	13.3x	12.0x	3.8%
				AFT Relative:	176%	100%	149%	82%	117%	58%	-100%

EV = Current Market Cap + Actual Net Debt

Source: *Forsyth Barr analysis, Bloomberg Consensus, Compco metrics re-weighted to reflect headline (AFT) companies fiscal year end

Figure 6. Consensus EPS momentum (NZ\$)



Source: Forsyth Barr analysis

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