

Arvida Group

1H21 Result – Care-Full Management

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NEUTRAL

On balance we walk away broadly encouraged by ARV's 1H21 result despite annuity EBITDA decreasing -11% vs 1H20, ~5% below our expectations. The positives of strong (and transparent) cash generation, confident development guidance and cost discipline outweighed weak underlying earnings driven by lower than anticipated deferred management fee (DMF). ARV has done a meritorious job managing the COVID-19 difficulties to date and our impression from its result is that the focus over the last six months has squarely been on the relating issues for residents and staff, an understandable prioritisation. Looking ahead, we believe the success of the care ORA model will be crucial for the investment case in ARV. We remain NEUTRAL with an unchanged target price of NZ\$1.90.

| NZX Code | ARV | Financials: Mar/ | 20A | 21E | 22E | 23E | Valuation (x) | 20A | 21E | 22E | 23E |
|--------------------|-------------------|------------------------------|------|------|------|------|-------------------|------|------|------|------|
| Share price | NZ\$1.73 | NPAT* (NZ\$m) | 51.7 | 51.2 | 66.3 | 76.5 | PE | 18.1 | 18.3 | 14.1 | 12.3 |
| Target price | NZ\$1.90 | EPS* (NZc) | 9.5 | 9.4 | 12.2 | 14.1 | EV/EBIT | 20.2 | 21.4 | 17.2 | 15.0 |
| Risk rating | Medium | EPS growth* (%) | 2.2 | -0.9 | 29.6 | 15.2 | EV/EBITDA | 18.3 | 19.0 | 15.5 | 13.5 |
| Issued shares | 541.9m | DPS (NZc) | 5.8 | 5.8 | 7.0 | 7.5 | Price / NTA | 1.4 | 1.3 | 1.2 | 1.1 |
| Market cap | NZ\$937m | Imputation (%) | 100 | 100 | 100 | 100 | Cash div yld (%) | 3.4 | 3.4 | 4.0 | 4.3 |
| Avg daily turnover | 613.2k (NZ\$961k) | *Based on normalised profits | | | | | Gross div yld (%) | 4.7 | 4.7 | 5.6 | 6.0 |

What's changed?

- **Earnings:** We reduce our underlying earnings and annuity EBITDA estimates by 2–6% for FY21–FY23

Strong cash discipline encouraging

In a refreshing deviation from recent trends within the aged care sector, ARV reported net debt ~NZ\$30m better vs our expectations driven by a combination of lower capex, higher new sales cash flow and strong working capital management. New sales cash flow was slightly above new sales revenue, a first for ARV. Company commentary also suggests that new sales cash flow should be expected to cover investment cash flow for the remainder of the financial year and as a result we expect overall net debt to remain stable.

DMF an area to watch; tenure in new villages crucial for long term profitability

DMF was substantially weaker than our estimates as a result of a change in valuer assumptions around expected tenure in existing villages in 1Q21. The absolute shortfall was small (~\$1.5m) and we do not believe this adjustment alone to be material to the investment case. However, should this be a recurring phenomenon it could be an indication that resident tenure is longer and therefore profitability lower within ARV's new, higher quality, village stock.

Development pipeline on track, comments around care ORA promising

ARV firmed up its previous FY21 development guidance of 200+ units to now indicate that 247 units will be delivered (199 in 2H21), in-line with "pre COVID" expectations. We estimate ~180 of these will be sold under an ORA and we also increase our medium term development estimates to reflect the strong pipeline. 2H21 will mark the delivery of the first meaningful group of care suites (Copper Crest and Aria Bay), targeted to be sold under the ORA model, the success of which we believe to be critical for the investment case. ARV commented that it was "very pleased" with internal village demand for care suites to date; we expect the first units at Aria Bay to be sold in early CY21. A significant majority of new care being built by ARV is targeting the care suite model and if ARV achieves its target of c. 80% sold under ORA, it could potentially run a cash neutral development business for the next few years.

Arvida Group Limited (ARV)

| | | | | | | | | | | | | |
|--|---------|---------|---------|---------|---------|--------------------------------------|------------------------------------|-------|-------|-------|-------|------|
| Priced as at 24 Nov 2020 (NZ\$) | | | | | | 1.73 | | | | | | |
| 12-month target price (NZ\$)* | | | | | | 1.90 | Spot valuations (NZ\$) | | | | | |
| Expected share price return | | | | | | 9.8% | 1. EV/Annuity EBITDA | | | | | 1.80 |
| Net dividend yield | | | | | | 3.8% | 2. DDM | | | | | 2.00 |
| Estimated 12-month return | | | | | | 13.6% | 3. n/a | | | | | n/a |
| Key WACC assumptions | | | | | | DCF valuation summary (NZ\$m) | | | | | | |
| Risk free rate | | | | | | 1.30% | Total firm value | | | | | n/a |
| Equity beta | | | | | | 0.88 | (Net debt)/cash | | | | | n/a |
| WACC | | | | | | 5.5% | Less: Capitalised operating leases | | | | | n/a |
| Terminal growth | | | | | | 1.5% | Value of equity | | | | | n/a |
| Profit and Loss Account (NZ\$m) | | | | | | Valuation Ratios | | | | | | |
| Sales revenue | 2019A | 2020A | 2021E | 2022E | 2023E | 2019A | 2020A | 2021E | 2022E | 2023E | | |
| Normalised EBITDA | 179.4 | 203.0 | 214.6 | 245.0 | 270.9 | EV/EBITDA (x) | 21.5 | 18.3 | 19.0 | 15.5 | 13.5 | |
| Depreciation and amortisation | 49.6 | 63.3 | 65.2 | 80.7 | 92.5 | EV/EBIT (x) | 23.9 | 20.2 | 21.4 | 17.2 | 15.0 | |
| Normalised EBIT | (5.0) | (5.8) | (7.3) | (8.2) | (9.3) | PE (x) | 18.5 | 18.1 | 18.3 | 14.1 | 12.3 | |
| Net interest | 44.6 | 57.5 | 57.9 | 72.6 | 83.1 | Price/NTA (x) | 1.4 | 1.4 | 1.3 | 1.2 | 1.1 | |
| Associate income | (3.6) | (4.1) | (5.7) | (6.2) | (6.7) | Free cash flow yield (%) | -5.6 | -13.2 | -12.1 | -15.0 | -19.6 | |
| Tax | 0 | 0 | 0 | 0 | 0 | Net dividend yield (%) | 3.1 | 3.4 | 3.4 | 4.0 | 4.3 | |
| Minority interests | (2.3) | (1.7) | (1.0) | 0 | 0 | Gross dividend yield (%) | 4.3 | 4.7 | 4.7 | 5.6 | 6.0 | |
| Normalised NPAT | 0 | 0 | 0 | 0 | 0 | Capital Structure | | | | | | |
| Abnormals/other | 38.6 | 51.7 | 51.2 | 66.3 | 76.5 | Interest cover EBIT (x) | 12.3 | 14.1 | 10.1 | 11.6 | 12.4 | |
| Reported NPAT | 20.4 | (9.0) | 23.2 | 15.6 | 13.9 | Interest cover EBITDA (x) | 13.7 | 15.6 | 11.4 | 12.9 | 13.8 | |
| Normalised EPS (cps) | 59.1 | 42.6 | 74.4 | 82.0 | 90.3 | Net debt/ND+E (%) | 24.9 | 29.7 | 30.3 | 29.5 | 29.8 | |
| DPS (cps) | 9.3 | 9.5 | 9.4 | 12.2 | 14.1 | Net debt/EBITDA (x) | 3.7 | 4.9 | 5.2 | 4.2 | 4.0 | |
| | 5.4 | 5.8 | 5.8 | 7.0 | 7.5 | Key Ratios | | | | | | |
| Growth Rates | | | | | | 2019A | 2020A | 2021E | 2022E | 2023E | | |
| Revenue (%) | 18.0 | 13.1 | 5.8 | 14.2 | 10.6 | Return on assets (%) | 3.4 | 3.0 | 2.7 | 3.0 | 3.1 | |
| EBITDA (%) | 14.7 | 27.7 | 2.9 | 23.8 | 14.5 | Return on equity (%) | 6.9 | 7.1 | 6.6 | 8.1 | 8.8 | |
| EBIT (%) | 14.2 | 29.1 | 0.8 | 25.3 | 14.6 | Return on funds employed (%) | 5.2 | 5.0 | 4.5 | 5.6 | 6.1 | |
| Normalised NPAT (%) | 17.1 | 33.8 | -0.9 | 29.6 | 15.2 | EBITDA margin (%) | 27.6 | 31.2 | 30.4 | 32.9 | 34.1 | |
| Normalised EPS (%) | 17.1 | 2.2 | -0.9 | 29.6 | 15.2 | EBIT margin (%) | 24.8 | 28.3 | 27.0 | 29.6 | 30.7 | |
| Ordinary DPS (%) | 6.8 | 8.4 | 0.0 | 20.7 | 7.1 | Capex to sales (%) | 45.7 | 74.2 | 67.5 | 78.1 | 86.3 | |
| Cash Flow (NZ\$m) | | | | | | 1,624 | 2,585 | 1,998 | 2,346 | 2,514 | | |
| EBITDA | 49.6 | 63.3 | 65.2 | 80.7 | 92.5 | Capex to depreciation (%) | 100 | 100 | 100 | 100 | 100 | |
| Working capital change | 8.6 | 24.0 | 7.0 | 28.1 | 17.3 | Imputation (%) | 100 | 100 | 100 | 100 | 100 | |
| Interest & tax paid | (5.9) | (5.8) | (6.7) | (6.2) | (6.7) | Pay-out ratio (%) | 57 | 61 | 61 | 57 | 53 | |
| Other | (22.8) | (54.4) | (34.5) | (51.7) | (53.2) | Operating Performance | | | | | | |
| Operating cash flow | 29.5 | 27.1 | 31.0 | 50.9 | 49.9 | Care fees | 125.6 | 129.5 | 133.5 | 141.4 | 149.7 | |
| Capital expenditure | (82.0) | (150.6) | (144.9) | (191.4) | (233.9) | Management fees | 21.4 | 29.0 | 33.1 | 40.2 | 48.8 | |
| (Acquisitions)/divestments | 12.2 | (104.1) | 116.6 | 171.8 | 196.8 | Other | 5.4 | 5.1 | 5.0 | 5.3 | 5.5 | |
| Other | (3.6) | (7.4) | 1.0 | 1.0 | 1.0 | Invest. property (total gains) | 27.0 | 39.3 | 43.0 | 58.2 | 66.9 | |
| Funding available/(required) | (43.9) | (235.0) | 3.7 | 32.3 | 13.8 | Total revenue | 179.4 | 203.0 | 214.6 | 245.0 | 270.9 | |
| Dividends paid | (22.7) | (29.6) | (31.4) | (37.9) | (40.6) | Key Drivers | | | | | | |
| Equity raised/(returned) | 0 | 141.7 | 0 | 0 | 0 | Sales - new units | 70 | 126 | 140 | 230 | 275 | |
| (Increase)/decrease in net debt | (66.6) | (122.8) | (27.7) | (5.6) | (26.9) | Ave price - new sales (NZ 000's) | 633 | 763 | 854 | 769 | 730 | |
| Balance Sheet (NZ\$m) | | | | | | 258 | 278 | 240 | 320 | 378 | | |
| Working capital | (45.9) | (69.9) | (76.9) | (105.0) | (122.3) | Sales - resold units | 258 | 278 | 240 | 320 | 378 | |
| Fixed assets | 1,190.3 | 1,804.2 | 2,005.5 | 2,260.7 | 2,564.1 | Ave price - new sales (NZ 000's) | 338 | 377 | 415 | 423 | 431 | |
| Intangibles | 54.0 | 36.0 | 36.0 | 36.0 | 36.0 | Gross development margin | 16.9% | 16.2% | 16.0% | 16.0% | 16.0% | |
| Right of use asset | 0 | 0 | 0 | 0 | 0 | Gross resales margin | 22.4% | 22.6% | 24.0% | 22.0% | 22.0% | |
| Other assets | 42.8 | 51.4 | 52.5 | 61.9 | 66.4 | Total portfolio | | | | | | |
| Total funds employed | 1,241.2 | 1,821.8 | 2,017.0 | 2,253.6 | 2,544.2 | Apartments/units | 1,955 | 2,475 | 2,657 | 2,892 | 3,167 | |
| Net debt/(cash) | 185.5 | 308.3 | 336.0 | 341.6 | 368.4 | Beds | 1,722 | 1,688 | 1,753 | 1,753 | 1,773 | |
| Lease liability | 0 | 4.9 | 4.9 | 4.9 | 4.9 | | | | | | | |
| Other liabilities | 496.8 | 778.8 | 903.4 | 1,090.3 | 1,304.4 | | | | | | | |
| Shareholder's funds | 558.8 | 729.8 | 772.8 | 816.8 | 866.5 | | | | | | | |
| Minority interests | 0 | 0 | 0 | 0 | 0 | | | | | | | |
| Total funding sources | 1,241.2 | 1,821.8 | 2,017.0 | 2,253.6 | 2,544.2 | | | | | | | |

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

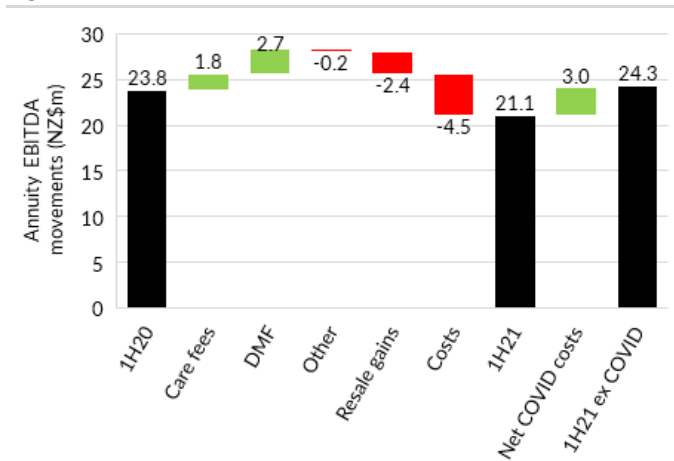
1H21 Result Summary

Figure 1. Earnings revisions (NZ\$m)

| | FY20A | | | | FY21E | | | FY22E | | | FY23E | | |
|-----------------------------|--------------|--------------|--------------|------------|--------------|--------------|------------|--------------|--------------|------------|-------|-----|----------|
| | Actual | Old | New | % change | Old | New | % change | Old | New | % change | Old | New | % change |
| Care fees | 129.5 | 136.2 | 133.5 | -2% | 143.6 | 141.4 | -2% | 149.6 | 149.7 | 0% | | | |
| DMF | 29.0 | 35.4 | 33.1 | -6% | 41.5 | 40.2 | -3% | 49.8 | 48.8 | -2% | | | |
| Resale gains | 23.7 | 26.7 | 25.1 | -6% | 31.5 | 31.7 | 1% | 36.8 | 36.7 | 0% | | | |
| Newsale gains | 15.6 | 17.9 | 17.9 | 0% | 26.5 | 26.5 | 0% | 33.4 | 30.1 | -10% | | | |
| Other | 5.1 | 5.0 | 5.0 | 0% | 5.3 | 5.3 | 0% | 5.5 | 5.5 | 0% | | | |
| Total revenue | 203.0 | 221.3 | 214.6 | -3% | 248.3 | 245.0 | -1% | 275.2 | 270.9 | -2% | | | |
| Total costs | 139.6 | 153.9 | 149.5 | -3% | 165.2 | 164.3 | -1% | 178.6 | 178.5 | 0% | | | |
| EBITDA | 63.3 | 67.4 | 65.2 | -3% | 83.0 | 80.7 | -3% | 96.6 | 92.5 | -4% | | | |
| Depreciation & amortisation | 5.8 | 8.1 | 7.3 | -10% | 8.5 | 8.2 | -4% | 8.8 | 9.3 | 5% | | | |
| EBIT | 57.5 | 59.4 | 57.9 | -2% | 74.5 | 72.6 | -3% | 87.7 | 83.1 | -5% | | | |
| Net interest & tax | 5.8 | 6.4 | 6.7 | 5% | 6.5 | 6.2 | -4% | 6.7 | 6.7 | -1% | | | |
| Underlying profit | 51.7 | 53.0 | 51.2 | -3% | 68.0 | 66.3 | -2% | 81.0 | 76.5 | -6% | | | |
| Annuity EBITDA | 47.7 | 49.5 | 47.3 | -5% | 56.5 | 54.2 | -4% | 63.1 | 62.3 | -1% | | | |
| DPS (cents) | 5.8 | 5.8 | 5.8 | 0% | 6.2 | 7.0 | 13% | 7.0 | 7.5 | 7% | | | |

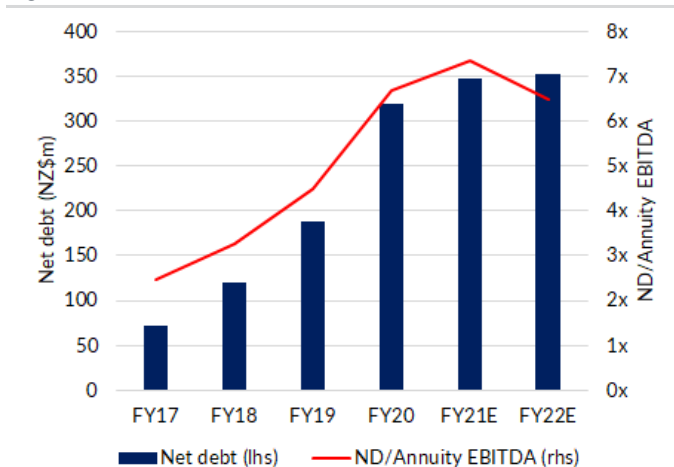
Source: Forsyth Barr analysis, Company reports

Figure 2. 1H21 annuity EBITDA movements



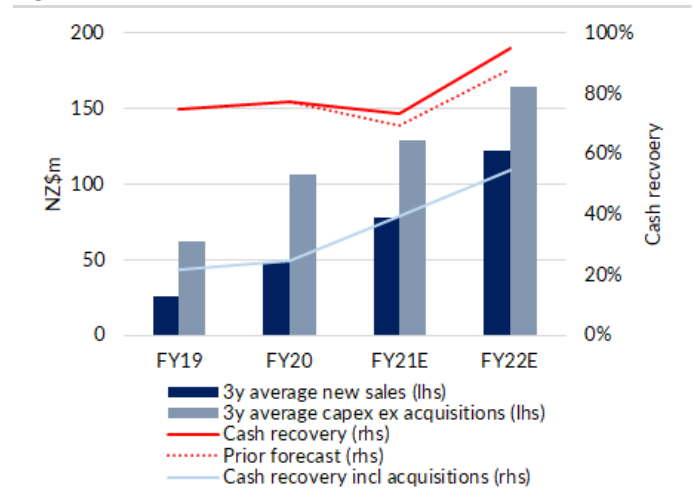
Source: Forsyth Barr analysis, Company reports

Figure 4. ND/Annuity EBITDA



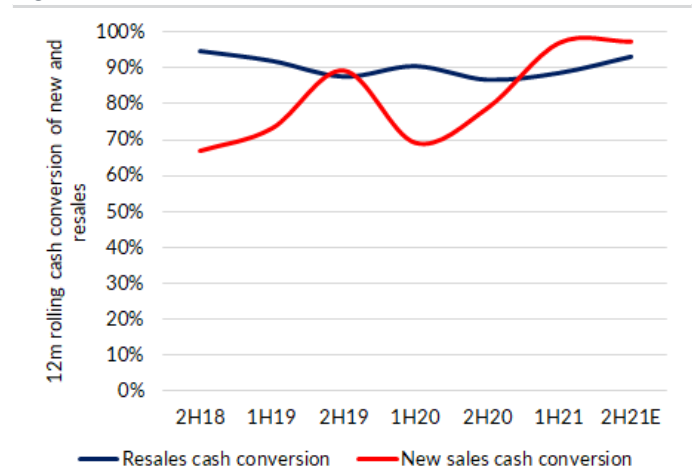
Source: Forsyth Barr analysis, Company reports

Figure 3. Cash recovery of capex

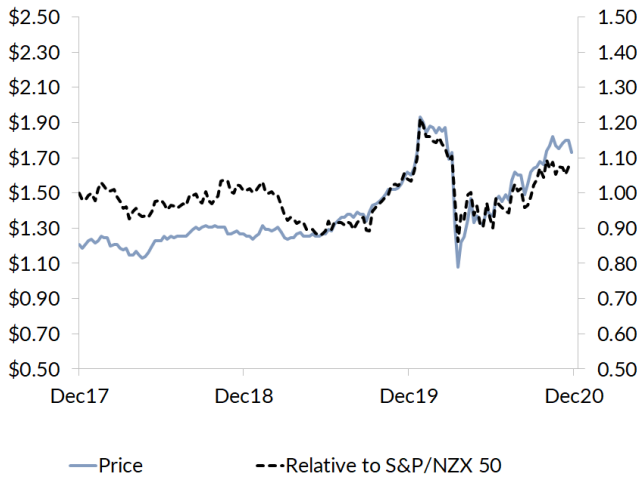


Source: Forsyth Barr analysis, Company reports

Figure 5. Cash conversion of new and resales



Source: Forsyth Barr analysis, Company reports

Figure 6. Price performance


Source: Forsyth Barr analysis

Figure 7. Substantial shareholders

| Shareholder | Latest Holding |
|------------------------------------|----------------|
| Forsyth Barr Investment Management | 9.4% |
| Generate Investment Management | 5.1% |

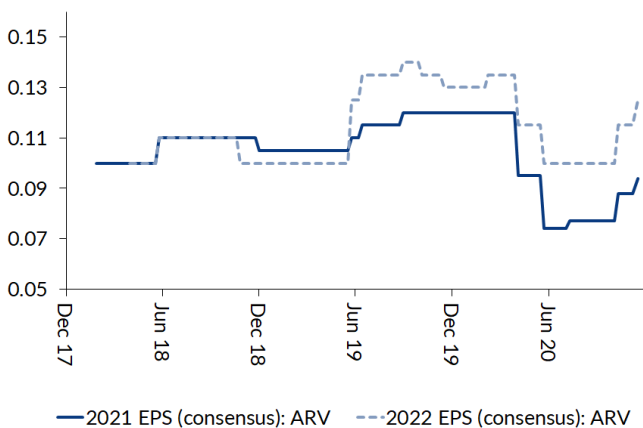
Source: NZX, Forsyth Barr analysis, NOTE: based on SPH notices only

Figure 8. International valuation comparisons

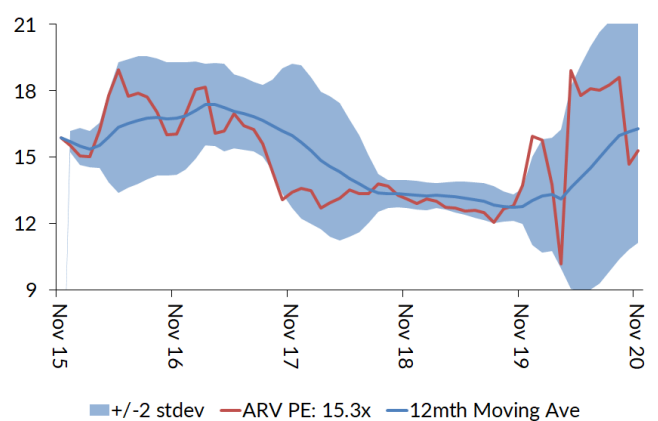
| Company | Code | Price | Mkt Cap (m) | PE | | EV/EBITDA | | EV/EBIT | | Cash Yld |
|---------------------------|--------|-----------|-------------|--------------|--------------|--------------|--------------|--------------|--------------|-------------|
| | | | | 2021E | 2022E | 2021E | 2022E | 2021E | 2022E | |
| Arvida Group Limited | ARV NZ | NZ\$1.73 | NZ\$937 | 18.3x | 14.1x | 19.1x | 15.4x | 21.5x | 17.2x | 4.0% |
| RYMAN HEALTHCARE * | RYM NZ | NZ\$15.13 | NZ\$7,565 | 31.5x | 24.8x | 31.6x | 25.3x | 35.5x | 28.1x | 2.0% |
| SUMMERSET GROUP LIMITED * | SUM NZ | NZ\$10.51 | NZ\$2,405 | 22.7x | 17.9x | 21.3x | 17.1x | 22.9x | 18.3x | 1.6% |
| METLIFECARE * | MET NZ | NZ\$5.98 | NZ\$1,272 | 18.1x | 15.7x | 19.6x | 17.2x | 21.2x | 18.6x | 1.3% |
| OCEANIA HEALTHCARE * | OCA NZ | NZ\$1.30 | NZ\$810 | 16.7x | 13.9x | 15.7x | 13.5x | 20.1x | 16.9x | 3.4% |
| REGIS HEALTHCARE | REG AT | A\$1.82 | A\$547 | >50x | 30.9x | 7.7x | 8.1x | 14.5x | 14.6x | 1.2% |
| JAPARA HEALTHCARE | JHC AT | A\$0.79 | A\$211 | <0x | 31.5x | 10.9x | 11.3x | >75x | >75x | 2.2% |
| ESTIA HEALTH | EHE AT | A\$1.95 | A\$508 | 21.0x | 22.3x | <0x | 6.6x | 7.7x | 11.8x | 4.4% |
| Compco Average: | | | | 22.0x | 22.4x | 17.8x | 14.1x | 20.3x | 18.0x | 2.3% |
| ARV Relative: | | | | -17% | -37% | 7% | 9% | 6% | -5% | 75% |

EV = Current Market Cap + Actual Net Debt

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

Figure 9. Consensus EPS momentum (NZ\$)


Source: Forsyth Barr analysis

Figure 10. One year forward PE (x)


Source: Forsyth Barr analysis

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