

EBOS Group

1H21 Result — Just What the Doctor Ordered

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OUTPERFORM

EBOS Group (EBO) reported a strong 1H21 result, modestly ahead of our expectations, and confirmed this strength has continued into 2H21. Growth drivers were broad-based, including market share gains, margin expansion/operating leverage, attractive industry growth and a modest net benefit from COVID-19. EBO is a quality business with an impressive track record of execution, a positive growth outlook, defensive product exposures and a conservative balance sheet which offers ample optionality. Recent share price strength has lifted EBO's one year forward PE to ~23x, which we still view as relatively attractive in the NZ market, particularly against defensive peers. Retain OUTPERFORM.

NZX Code	EBO	Financials: Jun/	20A	21E	22E	23E	Valuation (x)	20A	21E	22E	23E
Share price	NZ\$29.11	NPAT* (NZ\$m)	174.0	199.5	215.1	233.7	PE	27.0	24.0	22.2	20.4
Target price	NZ\$31.75	EPS* (NZc)	107.7	121.5	131.0	142.4	EV/EBIT	18.7	17.0	16.0	14.9
Risk rating	Medium	EPS growth* (%)	12.7	12.8	7.8	8.7	EV/EBITDA	14.6	13.6	12.9	12.2
Issued shares	164.1m	DPS (NZc)	77.5	89.0	95.0	103.0	Price / NTA	24.5	19.2	16.0	13.1
Market cap	NZ\$4,778m	Imputation (%)	25	25	25	25	Cash div yld (%)	2.7	3.1	3.3	3.5
Avg daily turnover	284.0k (NZ\$6,516k)	*Based on normalised profits					Gross div yld (%)	2.9	3.4	3.6	3.9

What's changed?

- **Earnings:** Upgraded +2–3% over our forecast horizon. Dividend forecasts lifted +4–6%.
- **Target price:** Lifted to NZ\$31.75. This reflects earnings changes, favourable mix shift (towards segments with higher margins and peer multiples) and higher peer multiples, which outweigh a small lift in cost of capital following revisions to our team inputs.

Key areas of interest

- **Strong result, largely across the board — with Animal Care the key standout**
 - Healthcare: EBITDA up +10%. Growth was above historical averages across core segments, Community Pharmacy and Institutional Healthcare, while Contract Logistics continues to win new business. Consumer Products was the only blemish, primarily due to COVID-19 related pressure (daigou, materially reduced cold & flu season).
 - Animal Care: A stellar period, with EBITDA up +19%. This reflects industry tailwinds, accelerated by COVID-19, including the humanisation of pets, higher spend per pet and increased pet ownership. We expect EBO also increased its market share.
 - Corporate costs: A material step-up to a 'new base', with greater investment in staff and higher insurance premiums.
- **Outlook comments positive:** No FY21 guidance, but 2H21 has started well (growth & trends consistent with 1H21). We also see potential for modest margin expansion — operating leverage and expectations of stronger growth in its higher margin segments.
- **Strong free cashflow generation:** Cash conversion is a key strength and 1H21 was no different. Adjusting for a delay in some capex spend due to COVID-19, we estimate free cashflow growth of ~+30% (vs reported growth of 46%).
- **Net beneficiary of COVID-19 through the period:** COVID-19 materially influenced a number of EBO's businesses, both negatively and positively. On balance EBO was a modest net beneficiary (+2% boost to growth). Nonetheless, we don't expect this to all unwind, with some sustainable changes (e.g. increased pet ownership) and likely reversal of weak/strong areas as consumer mobility increases. Vaccine rollout in Australasian pharmacies may also support foot traffic in-store.
- **Material (and growing) balance sheet headroom:** Gearing is conservative (net debt to EBITDA of 1.0x) and we estimate capacity of A\$500–550m available to deploy. Bolt-on acquisitions has been an area of added value historically (not captured in our valuation). It has been quiet over the past 18 months, however, we understand the pipeline is "healthy" and vendor expectations not a barrier.
- **Dividend — consistent growth continues, payout remains conservative**

Ebos Group Ltd (EBO)

Priced as at 17 Feb 2021 (NZ\$) **29.11**

12-month target price (NZ\$)*	31.75
Expected share price return	9.1%
Net dividend yield	3.2%
Estimated 12-month return	12.3%

Key WACC assumptions	
Risk free rate	2.30%
Equity beta	0.85
WACC	6.0%
Terminal growth	1.5%

Spot valuations (NZ\$)	
1. DCF	31.21
2. Multiple approach	30.32
3. Sum of the parts	29.30

DCF valuation summary (NZ\$m)	
Total firm value	6,178
(Net debt)/cash	(350)
Less: Capitalised operating leases	(640)
Value of equity	5,188

Profit and Loss Account (A\$m)	2019A	2020A	2021E	2022E	2023E
Sales revenue	6,930.4	8,765.5	9,228.7	9,477.1	9,771.2
Normalised EBITDA	261.6	333.6	362.7	375.9	393.2
Depreciation and amortisation	(32.1)	(73.1)	(71.7)	(72.2)	(70.5)
Normalised EBIT	229.5	260.5	290.9	303.7	322.8
Net interest	(25.3)	(30.4)	(25.1)	(23.2)	(20.9)
Associate income	0	0	0	0	0
Tax	(59.9)	(68.5)	(79.8)	(84.1)	(90.6)
Minority interests	(0.1)	(1.0)	(1.0)	(1.0)	(1.0)
Normalised NPAT	144.4	162.5	184.2	197.3	212.3
Abnormals/other	(6.7)	0	(1.5)	0	0
Reported NPAT	137.7	162.5	185.6	197.3	212.3
Normalised EPS (cps)	94.2	100.6	112.2	120.2	129.3
DPS (NZ cps)	71.5	77.5	89.0	95.0	103.0

Growth Rates	2019A	2020A	2021E	2022E	2023E
Revenue (%)	-0.8	26.5	5.3	2.7	3.1
EBITDA (%)	4.6	27.5	8.7	3.6	4.6
EBIT (%)	5.2	13.5	11.7	4.4	6.3
Normalised NPAT (%)	5.2	12.6	13.3	7.1	7.6
Normalised EPS (%)	4.2	6.8	11.5	7.1	7.6
Ordinary DPS (%)	13.5	8.4	14.8	6.7	8.4

Cash Flow (A\$m)	2019A	2020A	2021E	2022E	2023E
EBITDA	261.6	333.6	362.7	375.9	393.2
Working capital change	(62.5)	(0.0)	(5.5)	(23.0)	(12.6)
Interest & tax paid	(80.6)	(99.4)	(104.8)	(107.4)	(111.5)
Other	0	(5.0)	(1.5)	0	0
Operating cash flow	118.5	229.2	250.9	245.5	269.2
Capital expenditure	(34.2)	(29.3)	(31.9)	(50.4)	(40.4)
(Acquisitions)/divestments	(85.9)	(40.4)	(23.0)	0	0
Other	0	(35.7)	(23.8)	(23.7)	(23.4)
Funding available/(required)	(1.5)	123.9	172.1	171.4	205.3
Dividends paid	(103.0)	(118.6)	(136.0)	(143.1)	(153.6)
Equity raised/(returned)	168.2	29.7	0	0	0
(Increase)/decrease in net debt	63.6	35.0	36.2	28.3	51.8

Balance Sheet (A\$m)	2019A	2020A	2021E	2022E	2023E
Working capital	333.0	346.4	351.9	374.9	387.5
Fixed assets	174.5	173.7	195.6	195.6	195.6
Intangibles	1,117.2	1,135.9	1,133.4	1,145.6	1,147.4
Right of use asset	0	222.9	209.0	196.0	183.8
Other assets	122.6	209.2	209.2	209.2	209.2
Total funds employed	1,747.3	2,088.1	2,099.1	2,121.2	2,123.4
Net debt/(cash)	365.7	327.1	290.9	262.5	210.8
Lease liability	0	237.1	235.6	232.9	229.0
Other liabilities	142.3	213.0	213.0	213.0	213.0
Shareholder's funds	1,242.3	1,314.9	1,364.6	1,418.9	1,477.6
Minority interests	(3.1)	(4.1)	(5.1)	(6.1)	(7.1)
Total funding sources	1,747.3	2,088.1	2,099.1	2,121.2	2,123.4

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

Valuation Ratios	2019A	2020A	2021E	2022E	2023E
EV/EBITDA (x)	18.6	14.6	13.6	12.9	12.2
EV/EBIT (x)	21.2	18.7	16.9	15.9	14.8
PE (x)	30.5	27.0	24.0	22.2	20.4
Price/NTA (x)	33.5	24.5	19.2	16.0	13.1
Free cash flow yield (%)	1.9	4.5	4.9	4.5	5.3
Net dividend yield (%)	2.5	2.7	3.1	3.3	3.5
Gross dividend yield (%)	2.7	2.9	3.4	3.6	3.9

Capital Structure	2019A	2020A	2021E	2022E	2023E
Interest cover EBIT (x)	9.1	8.6	11.6	13.1	15.4
Interest cover EBITDA (x)	10.3	11.0	14.5	16.2	18.8
Net debt/ND+E (%)	22.7	19.9	17.6	15.6	12.5
Net debt/EBITDA (x)	1.4	1.0	0.8	0.7	0.5

Key Ratios	2019A	2020A	2021E	2022E	2023E
Return on assets (%)	7.2	7.0	7.6	7.8	8.2
Return on equity (%)	11.6	12.4	13.5	13.9	14.4
Return on funds employed (%)	10.9	11.8	12.8	13.2	13.8
EBITDA margin (%)	3.8	3.8	3.9	4.0	4.0
EBIT margin (%)	3.3	3.0	3.2	3.2	3.3
Capex to sales (%)	0.5	0.3	0.3	0.5	0.4
Capex to depreciation (%)	208	51	54	85	71
Imputation (%)	25	25	25	25	25
Pay-out ratio (%)	75	72	73	72	72

Operating Performance	2019A	2020A	2021E	2022E	2023E
Divisional revenue (A\$m)					
Healthcare	6,548.3	8,340.4	8,745.4	8,978.4	9,249.9
Animal Care	382.0	425.1	483.3	498.6	521.3
Total revenue	6,930.4	8,765.5	9,228.7	9,477.1	9,771.2

Divisional EBITDA (A\$m)	2019A	2020A	2021E	2022E	2023E
Healthcare	226.6	290.4	315.8	327.0	341.9
Animal Care	48.3	57.7	68.2	70.8	74.0
Corporate / Other	(13.3)	(14.5)	(21.3)	(22.0)	(22.6)
Total EBITDA	261.6	333.6	362.7	375.9	393.2

Key Healthcare segment revenue (A\$m)	2019A	2020A	2021E	2022E	2023E
Community Pharmacy	3,704.1	5,090.2	5,262.9	5,362.8	5,465.0
% growth	-4.3	37.4	3.4	1.9	1.9
Institutional Healthcare	2,292.7	2,565.1	2,706.2	2,760.3	2,843.1
% growth	2.4	11.9	5.5	2.0	3.0
Contract Logistics	518.0	712.3	819.1	901.0	991.1
% growth	14.0	37.5	15.0	10.0	10.0
Consumer Products	113.9	115.4	108.5	109.6	110.7
% growth	4.9	1.3	-6.0	1.0	1.0

1H21 result takeaways

EBO reported a strong 1H21 result, modestly ahead of our expectations, with underlying profit up +14%. This reflects a strong result for Healthcare and standout performance for Animal Care, which outweighed a material step-up in corporate costs. Free cashflow generation was impressive through the period, as was return on capital at 17.5%.

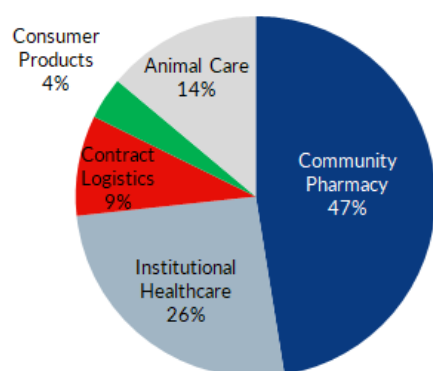
Figure 1. Result snapshot – 1H21

A\$m	1H20	1H21	% chg	Forsyth Barr	Comment
Revenue	4,376.1	4,653.3	6.3%	4,564.3	
Healthcare EBITDA	147.0	161.3	9.7%	154.1	Growth across the board, except Consumer Products. Insto Healthcare the standout
Animal Care EBITDA	28.5	33.9	19.0%	32.0	Structural tailwinds, COVID-19 beneficiary, market share gains & margin expansion
Corporate costs	(7.1)	(11.1)	56.8%	(7.3)	Step-up in insurance, staff (expanded LTI & new employee share scheme). A new base
Total EBITDA	168.4	184.1	9.3%	178.8	Strong period. Net COVID-19 benefit of c. +2% (with positives and negatives)
Underlying NPAT	82.7	94.3	14.2%	92.4	Helped by lower interest costs and amortisation
Underlying EPS (A cps)	51.0	57.5	12.7%	56.3	Share issuance through the period for staff
Dividend (NZ cps)	37.5	42.5	13.3%	40.5	Payout ratio of 69%, broadly in line with prior year. EBO targets >60% of NPAT
Free cashflow	60.5	88.6	46.3%	n/a	Impressive period. Strong profit result, modest stay-in-business capex requirements and some temporary benefit from delayed capex due to COVID-19 (est. ~A\$10m)

Source: Forsyth Barr analysis, Company reports

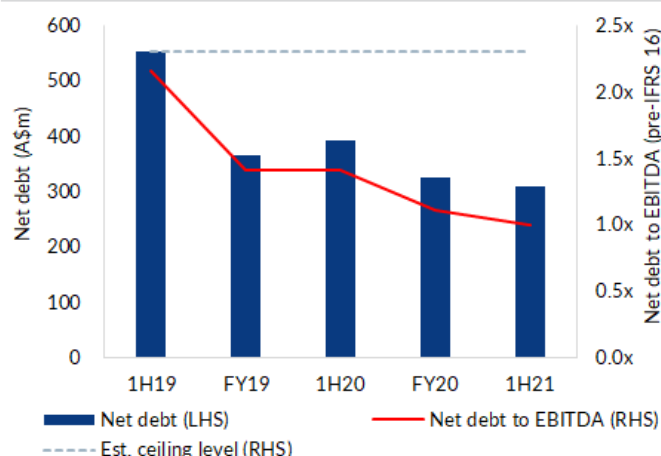
Key charts of interest

Figure 2. Gross operating revenue (GOR) breakdown



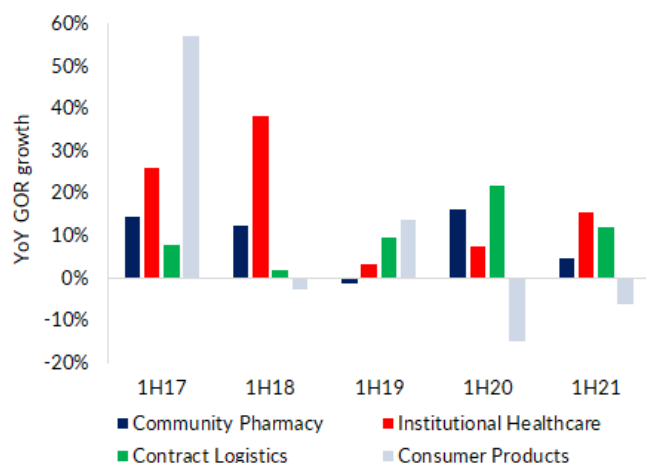
Source: Forsyth Barr analysis, Company reports; GOR = gross profit less inventory write-down

Figure 3. Gearing low, with ample headroom



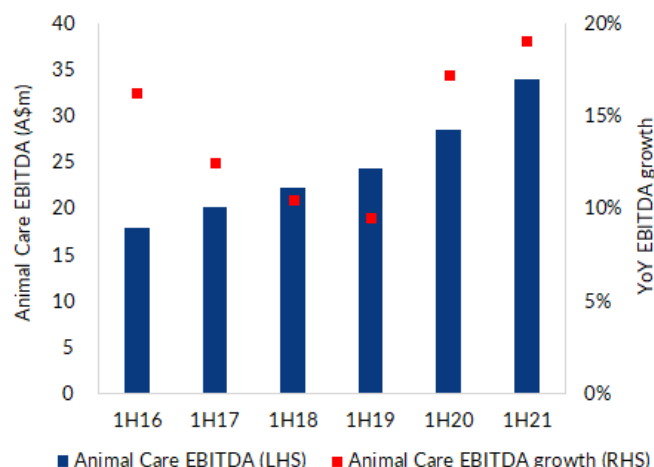
Source: Forsyth Barr analysis, Company reports

Figure 4. Strong healthcare growth in key segments

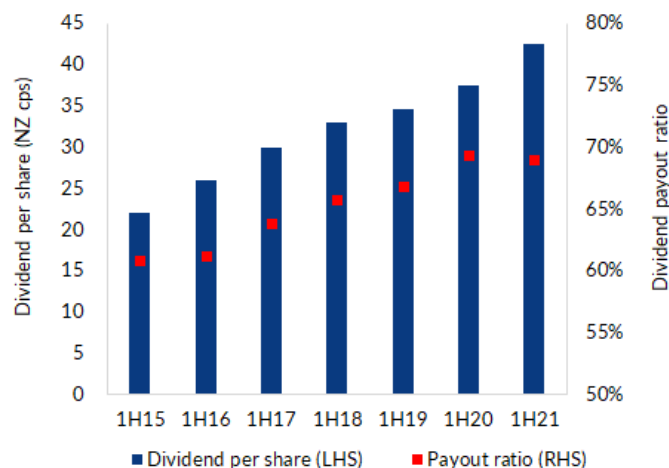


Source: Forsyth Barr analysis, Company reports

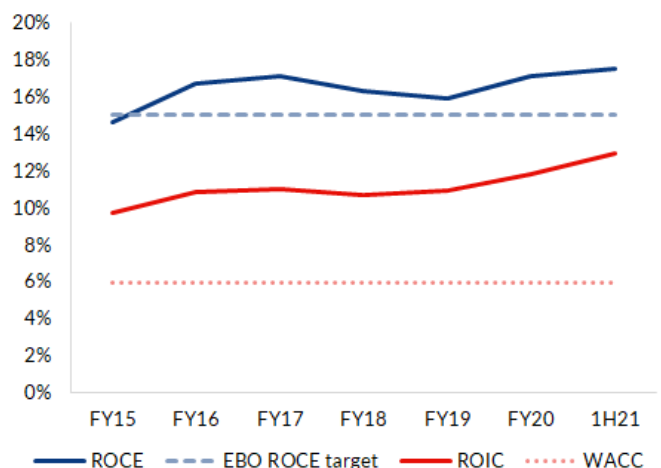
Figure 5. Animal Care (once again) the standout performer



Source: Forsyth Barr analysis, Company reports

Figure 6. Consistent dividend growth; conservative payout


Source: Forsyth Barr analysis, Company reports

Figure 7. Attractive returns through time


Source: Forsyth Barr analysis, Company reports

Earnings revisions and valuation

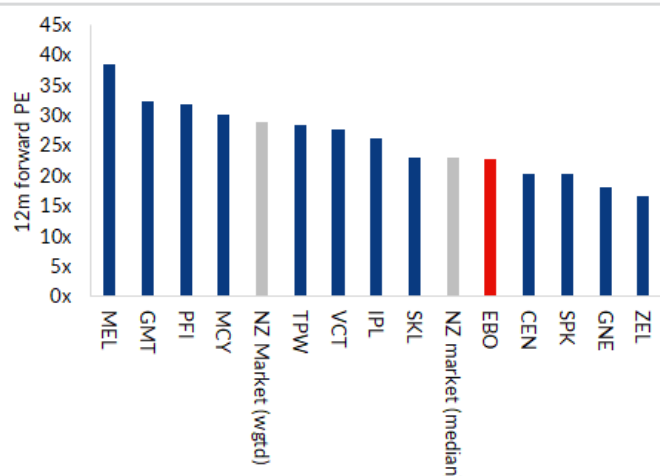
We have made modest earnings upgrades of c. +2–3% across our forecast horizon. This reflects upgrades to both Healthcare and Animal Care, which outweighs a material step-up in corporate costs. Within the Healthcare division we lift Institutional Healthcare and Community Pharmacy, while downgrade Consumer Products. The other key change is to lift our dividend expectations/payout given EBO's strong balance sheet position.

Figure 8. Earnings revisions (A\$m)

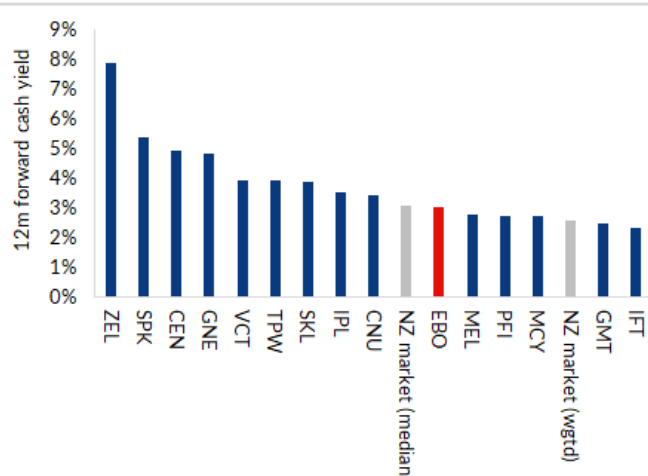
A\$m	FY20A Actual	FY21E Old	FY21E New	% Chg	FY22E Old	FY22E New	% Chg	FY23E Old	FY23E New	% Chg
Revenue	8,766	9,142	9,229	0.9%	9,392	9,477	0.9%	9,660	9,771	1.1%
EBITDA	333.6	354.2	362.7	2.4%	368.5	375.9	2.0%	383.4	393.2	2.6%
EBIT	260.5	282.5	290.9	3.0%	297.8	303.7	2.0%	312.7	322.8	3.2%
Underlying NPAT	162.5	181.4	187.1	3.1%	193.9	197.3	1.7%	206.5	212.3	2.8%
Underlying EPS (cps)	100.6	112.3	114.0	1.5%	120.1	120.2	0.1%	127.8	129.3	1.2%
Dividend (NZ cps)	77.5	85.0	89.0	4.7%	91.0	95.0	4.4%	97.0	103.0	6.2%

Source: Forsyth Barr analysis

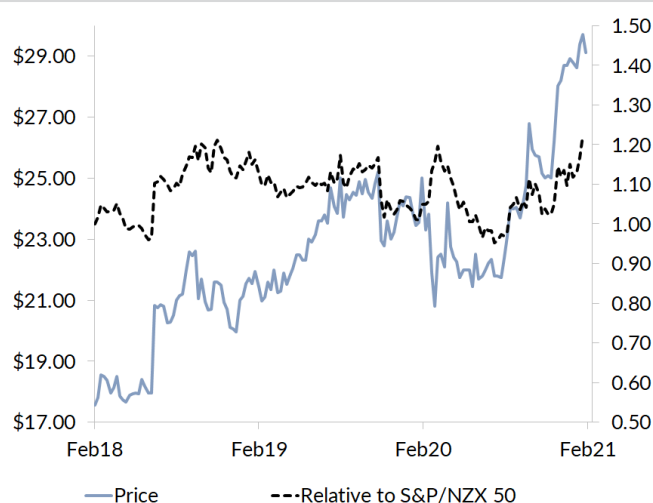
We lift our EBO target price to NZ\$31.75 (from NZ\$29.00). This reflects earnings revisions, favourable business mix shifts (towards segments with higher margins and peer multiples) and higher peer multiples since our last report. This outweighs a small lift in our WACC (to 6.0% from 5.6%) following changes to our team inputs, given higher interest rates – refer our strategy report, *Still a One Way Bet? – Updated WACC Assumptions*, published 12 February 2021.

Figure 9. PE vs defensive peers; broadly aligned to NZ market


Source: Forsyth Barr analysis

Figure 10. Solid, mid-pack yield (albeit not fully imputed)


Source: Forsyth Barr analysis

Figure 11. Price performance


Source: Forsyth Barr analysis

Figure 12. Substantial shareholders

Shareholder	Latest Holding
Sybos Holdings	18.7%
Harbour Asset Management & Jarden Securities Limited	5.2%

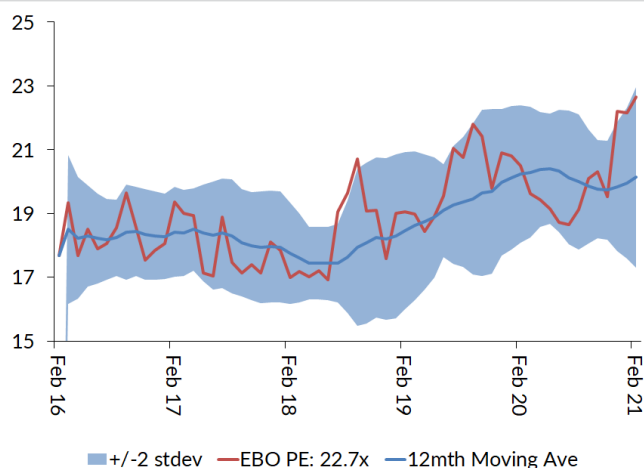
Source: NZX, Forsyth Barr analysis, NOTE: based on SPH notices only

Figure 13. International valuation comparisons

Company	Code	Price	Mkt Cap (m)	PE 2021E	PE 2022E	EV/EBITDA 2021E	EV/EBITDA 2022E	EV/EBIT 2021E	EV/EBIT 2022E	Cash Yld 2022E
(metrics re-weighted to reflect EBO's balance date - June)										
EBOS Group	EBO NZ	NZ\$29.11	NZ\$4,778	24.0x	22.2x	13.2x	12.5x	16.4x	15.5x	3.3%
AUSTRALIAN PHARMA INDUS	API AT	A\$1.22	A\$599	0.1x	13.0x	6.3x	5.4x	<0x	10.3x	5.1%
SIGMA HEALTHCARE	SIG AT	A\$0.69	A\$726	23.0x	18.4x	11.2x	9.6x	17.1x	14.1x	4.3%
MCKESSON CORP	MCK US	US\$180.88	US\$28,781	10.4x	9.6x	8.0x	7.6x	9.2x	8.6x	1.0%
AMERISOURCEBERGEN CORP	ABC US	US\$103.71	US\$21,230	7.6x	11.1x	4.5x	6.8x	5.3x	7.7x	1.8%
HENRY SCHEIN INC	HSIC US	US\$69.95	US\$9,987	20.7x	17.6x	12.8x	11.1x	16.5x	13.8x	n/a
PATTERSON COS INC	PDCO US	US\$32.61	US\$3,147	16.8x	16.0x	12.6x	11.9x	14.2x	13.4x	3.2%
SINOPHARM GROUP CO-H	1099 HK	CN¥18.84	CN¥58,793	8.1x	7.2x	6.5x	6.1x	7.2x	6.8x	4.1%
Compco Average:				12.4x	13.3x	8.8x	8.4x	11.6x	10.7x	3.3%
EBO Relative:				93%	67%	49%	50%	42%	45%	0%

EV = Current Market Cap + Actual Net Debt

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

Figure 14. One year forward PE (x)


Source: Forsyth Barr analysis

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