

# Equity Strategy

## Institutional Model Portfolio

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The valuation gap between yield and structural growth has almost fully closed, primarily driven by strong structural growth performance and weak generator/retailers performance. We remain overweight structural growth, but view the tactical opportunity to be less today than it was only a few short months ago. After some relatively dramatic thematic gyrations in the market over the last 12 months, we believe that we are firmly entering stock picking territory.

**Adding to CEN and closing our underweight in generator/retailers after "re-set"**

The strong performance of the generator/retailers at the back end of 2020 has now largely been reversed, and we return to our default position of being slightly overweight. The generator/retailers have sold off almost ~15% year to date or ~25% since the early January peak, and now look valued in-line with recent history relative to the rest of the yield universe. We add +100bps to Contact Energy (CEN) but leave our underweight in Meridian Energy (MEL) given it has the most subdued DPS growth in the sector and as we see near term earnings pressure continuing for some time.

**Reducing overweight in PPH and SKC after strong performance, adding to OCA after weak performance.**

Pushpay Holdings (PPH) and SKYCITY (SKC) were two of the best performing stocks over the last month with limited direct news-flow of significance. We have reduced our over weights in PPH by -100bps and SKC by -50bps. OCA, together with the aged care sector overall, were one of the weakest performers through March and we increase our overweight by +50bps. The aged care sector sold off after the housing policy announcement by the government and while we acknowledge that the announced policies are likely to reduce house price inflation, all else equal, we consider the near term outlook to remain very benign for the aged care sector.

**What worked in March?**

The Institutional model portfolio performed broadly in-line with the benchmark in March (down -8bps). Growth and yield had diverging fortunes with growth's +17bps outperformance directly offset by yield (-17bps). Our REIT's underweight was the main driver of our yield outperformance contributing +15bps while our single largest positive contribution in the month was 'other structural growth' contributing +26bps predominately driven by PPH and Freightways (FRE) at +17bps and +13bps respectively. Offsetting these strong growth contributions was weakness in the aged care sector (-15bps), The a2 Milk Company (-17bps) and Fisher & Paykel Healthcare (-11bps).

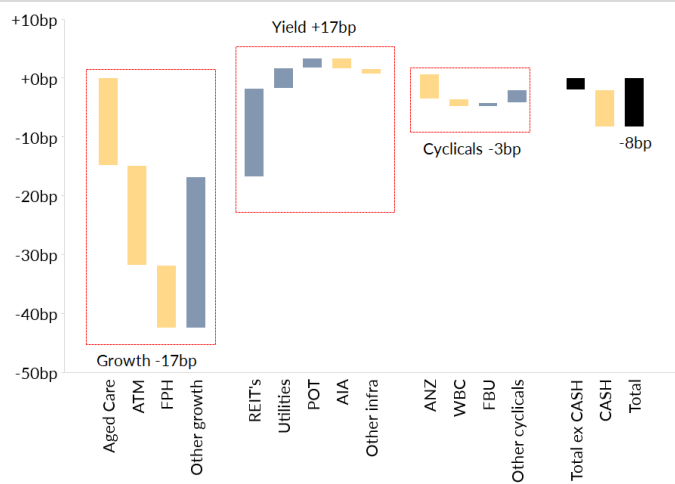
**Figure 1. Portfolio changes**

| Code | Portfolio move | Weighting change | Active weight | Rationale  |
|------|----------------|------------------|---------------|--|
| AIA  | Sell           | -0.50%           | -2.0%         | Increasing underweight in light of full valuation                              |
| PPH  | Sell           | -1.00%           | +0.1%         | Reduce overweight following strong recent share price performance              |
| SKC  | Sell           | -0.50%           | +0.6%         | Trimming overweight reflecting recent performance                              |
| CEN  | Buy            | +1.00%           | +1.5%         | Increasing overweight in line with conviction list trade and sector preference |
| FPH  | Buy            | +1.00%           | -0.5%         | Reducing overweight in light of rating change to NEUTRAL                       |
| OCA  | Buy            | +0.50%           | +0.8%         | Increasing overweight reflecting soft recent performance                       |

Source: Forsyth Barr analysis

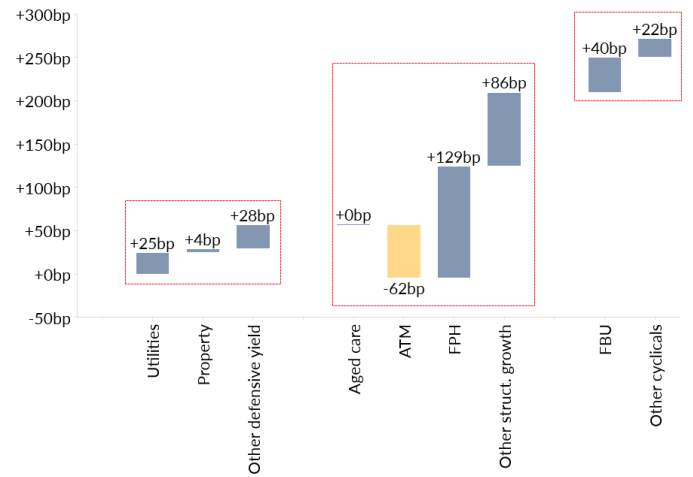
## Charts of interest

**Figure 2. March performance broadly in-line with the benchmark**



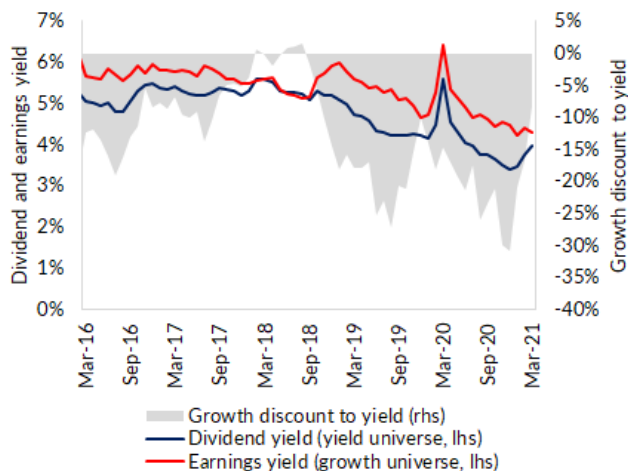
Source: Forsyth Barr analysis

**Figure 3. A strong rebound month for the S&P/NZX 50**



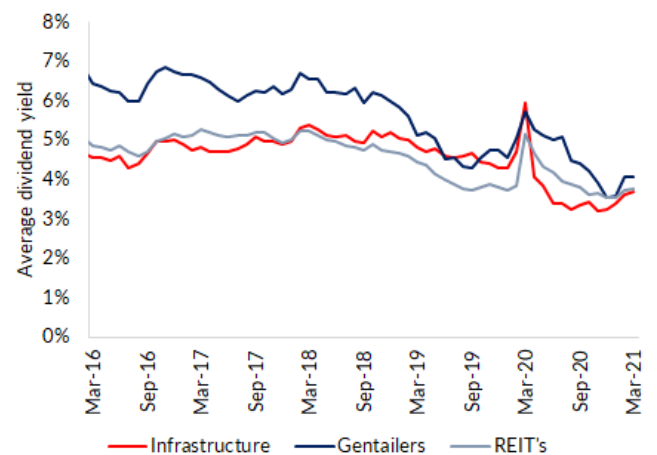
Source: Forsyth Barr analysis

**Figure 4. Yield discount relative to growth is starting to close...**



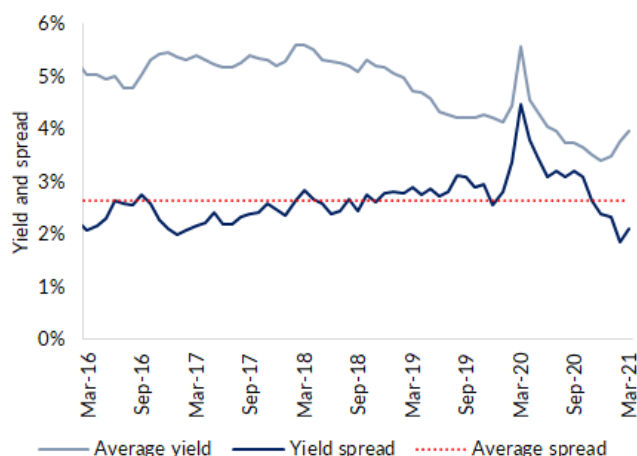
Source: Forsyth Barr analysis, Thomson Reuters

**Figure 5. ...driven by all three yield buckets**



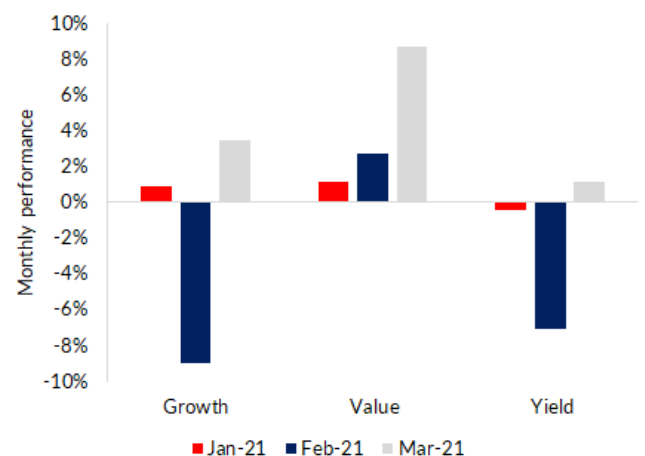
Source: Forsyth Barr analysis, Thomson Reuters

**Figure 6. Yield spread closing slightly**



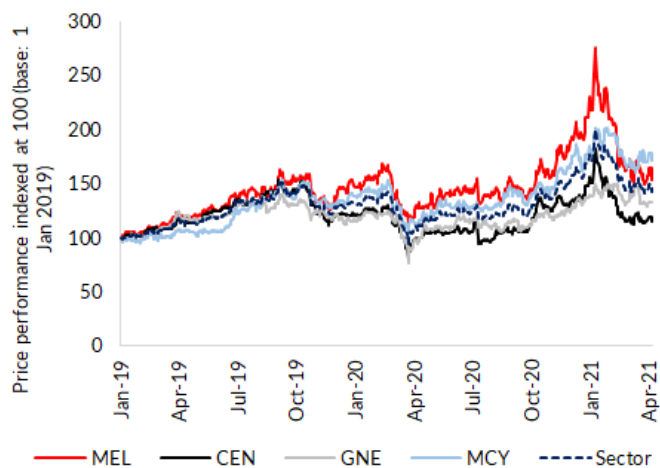
Source: Forsyth Barr analysis, Thomson Reuters

**Figure 7. A strong quarter for our value universe**



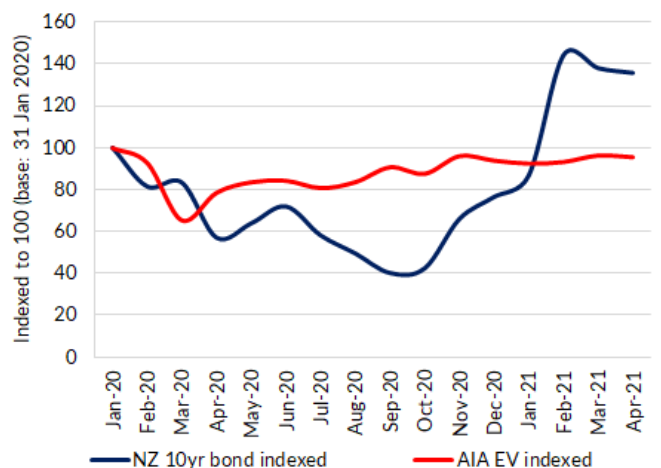
Source: Forsyth Barr analysis, Thomson Reuters

Figure 8. Gentailer performance indexed at 1 January 2019



Source: Forsyth Barr analysis, Thomson Reuters

Figure 9. NZ 10yr bond vs AIA EV



Source: Forsyth Barr analysis, Bloomberg

## Institutional model portfolio

The Forsyth Barr institutional model portfolio is outlined in Figure 11. We incorporate 28 stocks together with a ~2.1% nominal cash holding. All portfolio holdings are ~1.0% or more, unless (1) we are adding new positions, or exiting positions in less liquid stocks, or (2) existing positions are diluted by relative underperformance.

Figure 10. The Forsyth Barr Institutional model portfolio

| Market breakdown         | Benchmark     | Active weight | Portfolio     |
|--------------------------|---------------|---------------|---------------|
| <b>Defensive Yield</b>   | <b>49.8%</b>  | <b>-5.9%</b>  | <b>43.9%</b>  |
| Utilities                | 14.9%         | +0.2%         | 15.2%         |
| Property                 | 9.0%          | -5.5%         | 3.6%          |
| Other defensive yield    | 25.8%         | -0.6%         | 25.2%         |
| <b>Structural Growth</b> | <b>40.5%</b>  | <b>+6.2%</b>  | <b>46.7%</b>  |
| Aged care                | 8.4%          | +0.8%         | 9.2%          |
| Other structural growth  | 32.1%         | +5.4%         | 37.5%         |
| <b>Cyclicals</b>         | <b>9.7%</b>   | <b>-2.4%</b>  | <b>7.2%</b>   |
| Cash                     | 0.0%          | +2.1%         | 2.1%          |
| <b>Total</b>             | <b>100.0%</b> | <b>0.0%</b>   | <b>100.0%</b> |

Source: Forsyth Barr analysis, S&P DJI

**Figure 11. Forsyth Barr institutional model portfolio summary**

| Code | Portfolio weight | Active weight | 12m fwd PE | 12m fwd Cash dividend yield | Rating       |
|------|------------------|---------------|------------|-----------------------------|--------------|
| FPH  | 13.6%            | -0.5%         | 44.2x      | 1.5%                        | NEUTRAL      |
| SPK  | 8.1%             | +1.5%         | 22.7x      | 5.5%                        | OUTPERFORM   |
| ATM  | 6.1%             | +1.2%         | 23.9x      | 0.0%                        | NEUTRAL      |
| CEN  | 5.5%             | +1.5%         | 18.8x      | 5.4%                        | OUTPERFORM   |
| EBO  | 5.5%             | +2.4%         | 23.1x      | 3.1%                        | OUTPERFORM   |
| AIA  | 5.3%             | -2.0%         | n/a        | 0.3%                        | NEUTRAL      |
| MFT  | 5.2%             | +0.6%         | 34.1x      | 1.2%                        | OUTPERFORM   |
| MEL  | 4.6%             | -0.5%         | 32.5x      | 3.2%                        | UNDERPERFORM |
| FBU  | 4.6%             | -0.1%         | 15.2x      | 4.7%                        | NEUTRAL      |
| FRE  | 4.0%             | +2.6%         | 21.0x      | 3.6%                        | OUTPERFORM   |
| IFT  | 3.9%             | -0.0%         | n/a        | 2.4%                        | NEUTRAL      |
| RYM  | 3.9%             | -1.0%         | 25.0x      | 2.0%                        | NEUTRAL      |
| CNU  | 3.1%             | +0.7%         | 73.2x      | 4.3%                        | OUTPERFORM   |
| SUM  | 2.9%             | +0.8%         | 18.9x      | 1.6%                        | NEUTRAL      |
| SKC  | 2.7%             | +0.6%         | 22.7x      | 2.8%                        | OUTPERFORM   |
| MCY  | 2.5%             | -0.6%         | 25.9x      | 3.2%                        | NEUTRAL      |
| GNE  | 2.5%             | +1.1%         | 16.1x      | 4.9%                        | OUTPERFORM   |
| Cash | 2.1%             | +2.1%         | n/a        | n/a                         | n/a          |
| ZEL  | 2.1%             | +0.9%         | 17.0x      | 8.2%                        | OUTPERFORM   |
| KMD  | 1.7%             | +1.0%         | 11.2x      | 4.7%                        | OUTPERFORM   |
| PCT  | 1.5%             | +0.1%         | 23.6x      | 4.0%                        | OUTPERFORM   |
| PPH  | 1.4%             | +0.1%         | 33.2x      | 0.0%                        | NEUTRAL      |
| OCA  | 1.4%             | +0.8%         | 13.2x      | 3.5%                        | OUTPERFORM   |
| SPG  | 1.1%             | +0.3%         | 21.2x      | 4.4%                        | OUTPERFORM   |
| PEB  | 1.0%             | +0.4%         | n/a        | 0.0%                        | OUTPERFORM   |
| ARG  | 0.9%             | +0.0%         | 19.6x      | 4.5%                        | OUTPERFORM   |
| ARV  | 0.9%             | +0.2%         | 13.4x      | 4.2%                        | NEUTRAL      |
| SAN  | 0.9%             | +0.6%         | 18.8x      | 1.6%                        | OUTPERFORM   |
| SKL  | 0.7%             | +0.1%         | 20.9x      | 3.8%                        | OUTPERFORM   |

Source: Forsyth Barr analysis

## Key active weights

We outline our key active weights in Figure 12 where weightings are 1.5% or greater relative to the benchmark.

**Figure 12. Key active weights**

| Code                     | Active weight | Rationale   |
|--------------------------|---------------|---|
| <b>Key over-weights</b>  |               |   |
| FRE                      | +2.6%         | Margin delivery in B2C as a result of 'pricing for effort' initiative and positive industry pricing dynamic provides secular growth opportunity in higher volume growth segment of parcel market.                           |
| EBO                      | +2.4%         | Current valuation metrics are attractive and offer a good entry point for a well-run, defensive company which delivers attractive returns, consistently strong cash conversion and has a solid growth outlook.              |
| SPK                      | +1.5%         | Attractive dividend yield. Relative earnings resilience to COVID-19 crisis and recessionary conditions. Consistently strong execution track record, with solid A- rated balance sheet.                                      |
| CEN                      | +1.5%         | CEN is offering an attractive entry price following recent share price declines. Valuation metrics are undemanding and it offers the best dividend yield after adjusting for expected near-term dividend growth.            |
| <b>Key under-weights</b> |               |   |
| AIA                      | -2.0%         | Increasing under weight on sentiment boost of partial border reopening ahead of fundamental reality setting in. Trading towards the top end of our anticipated trading range based on pre COVID-19 levels of profitability. |
| GMT                      | -1.9%         | Well placed Auckland centric portfolio but trading at a substantial premium to its NTA and wider sector metrics.  |
| POT                      | -1.9%         | Volume headwinds given container capacity constraints, COVID-19 supply chain congestion and cruise industry shut-down. FY21 guidance implies another year of flat/negative earnings.  |
| KPG                      | -1.5%         | Tail of underperforming retail assets with headwinds from growing online sales and weakening consumer spend. KPG's gearing is also towards the top end of its target range.   |

Source: Forsyth Barr analysis

## NZ market in charts

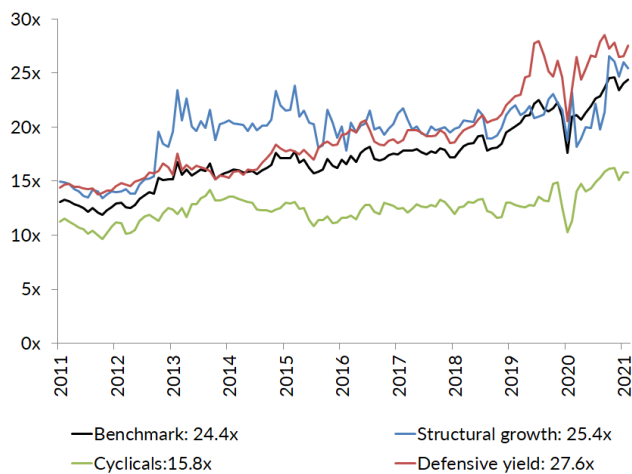
### Valuation

**Figure 13. Market valuation metrics (based on consensus earnings estimates)**

| Thematic          | 12mth Fwd PE |              | 12mth Fwd EV/EBITDA |              | 12mth Fwd cash div. yield |             |
|-------------------|--------------|--------------|---------------------|--------------|---------------------------|-------------|
|                   | Ave.         | Wghtd. Ave.  | Ave.                | Wghtd. Ave.  | Ave.                      | Wghtd. Ave. |
| Cyclicals         | 15.8x        | 15.5x        | 6.6x                | 6.6x         | 3.3%                      | 3.8%        |
| Defensive Yield   | 27.6x        | 29.7x        | 16.3x               | 15.2x        | 3.6%                      | 3.5%        |
| Structural Growth | 25.4x        | 32.5x        | 13.3x               | 13.8x        | 1.9%                      | 1.6%        |
| <b>Market</b>     | <b>24.4x</b> | <b>29.6x</b> | <b>13.7x</b>        | <b>13.8x</b> | <b>3.0%</b>               | <b>2.7%</b> |

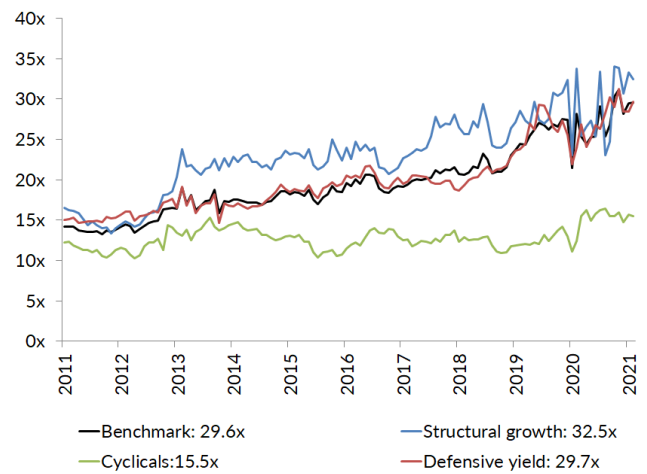
Source: Forsyth Barr analysis, Bloomberg

**Figure 14. Consensus 12m fwd PE – average**



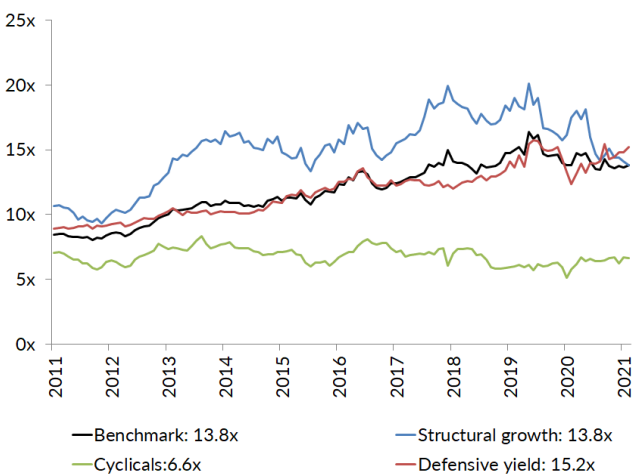
Source: Forsyth Barr analysis, Bloomberg

**Figure 15. Consensus 12m fwd PE – weighted average**



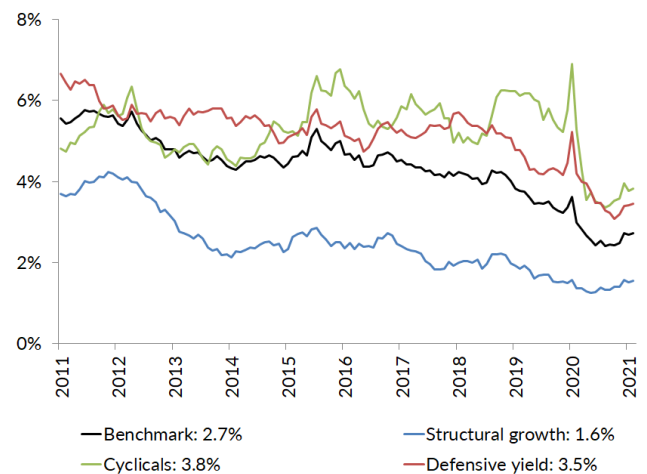
Source: Forsyth Barr analysis, Bloomberg

**Figure 16. Consensus 12m fwd EV/EBITDA – weighted average**

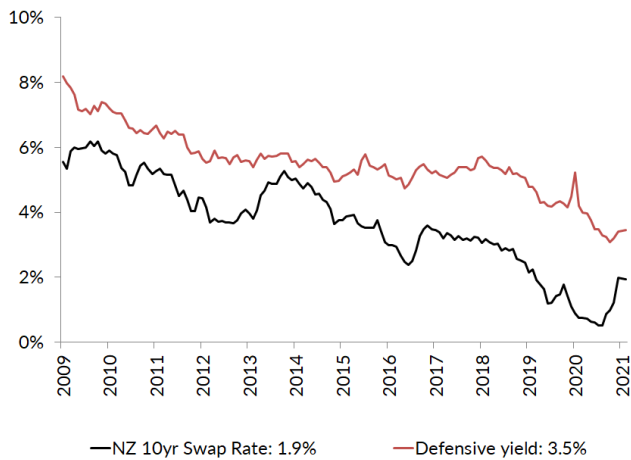


Source: Forsyth Barr analysis, Bloomberg

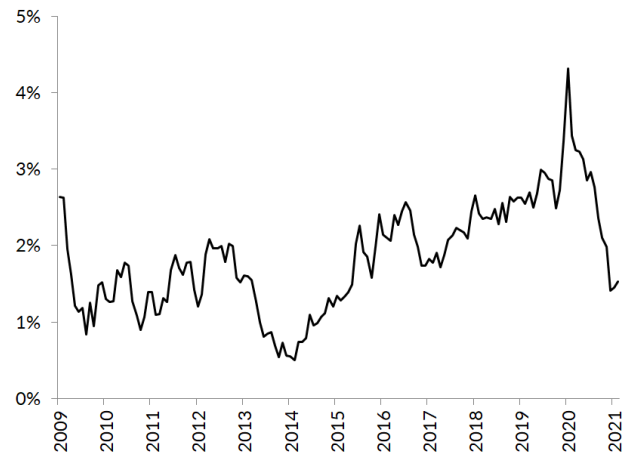
**Figure 17. Consensus cash dividend yield – weighted average**



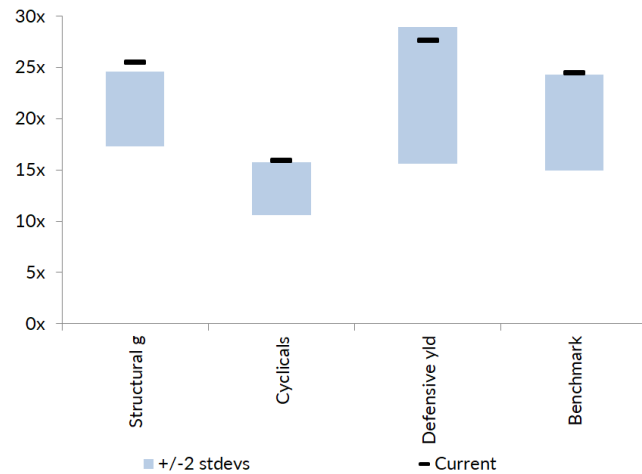
Source: Forsyth Barr analysis, Bloomberg

**Figure 18. Defensive yield cash dividend yield vs. 10yr bond**


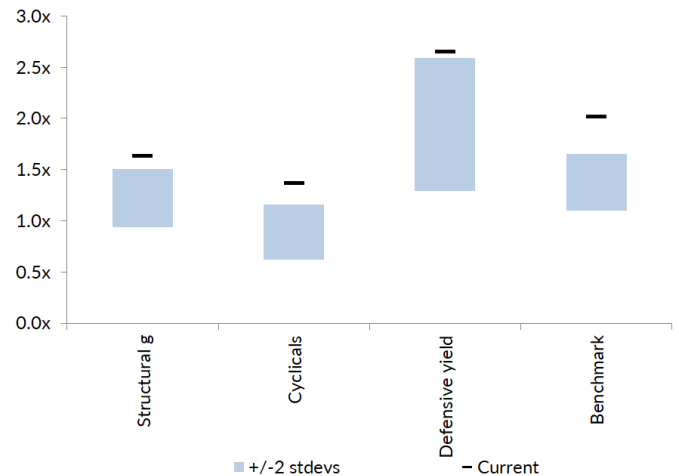
Source: Forsyth Barr analysis, Bloomberg

**Figure 19. Defensive yield cash div yield and 10yr bond diff**


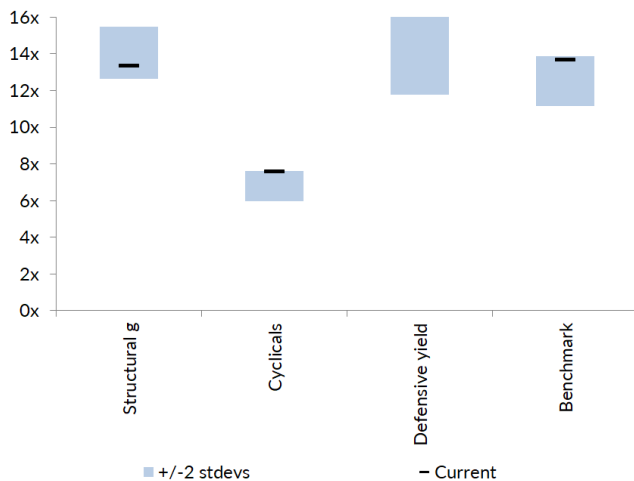
Source: Forsyth Barr analysis, Company reports

**Figure 20. Consensus 12m fwd PE vs. historic (five year) average**


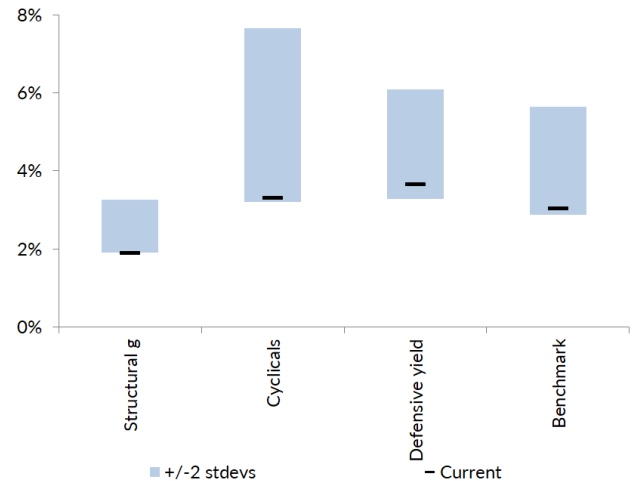
Source: Forsyth Barr analysis, Bloomberg

**Figure 21. 12m fwd PEG vs. historic (five year) average**


Source: Forsyth Barr analysis, Bloomberg

**Figure 22. 12m fwd EV/EBITDA vs. historic (five year) average**


Source: Forsyth Barr analysis, Bloomberg

**Figure 23. 12m fwd cash div. yield vs. historic (five year) average**


Source: Forsyth Barr analysis, Bloomberg

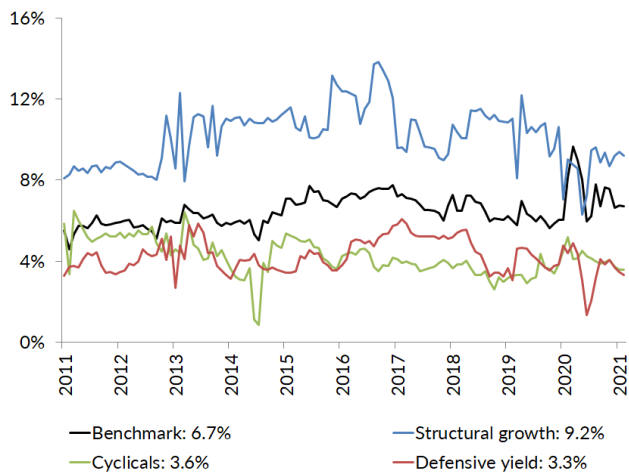
## Earnings

**Figure 24. Market earnings estimates (based on consensus earnings estimates)**

| Thematic          | 12-24mth Revenue growth |             | 12-24mth EBITDA growth |             | 12-24mth EPS growth |             | 12-24mth OCF growth |             |
|-------------------|-------------------------|-------------|------------------------|-------------|---------------------|-------------|---------------------|-------------|
|                   | Ave.                    | Wghtd. Ave. | Ave.                   | Wghtd. Ave. | Ave.                | Wghtd. Ave. | Ave.                | Wghtd. Ave. |
| Cyclicals         | 3.6%                    | 2.5%        | 6.4%                   | 4.3%        | 8.3%                | 4.8%        | 10.6%               | 7.2%        |
| Defensive Yield   | 3.3%                    | 1.7%        | 5.0%                   | 3.7%        | 6.8%                | 6.3%        | 4.1%                | 1.3%        |
| Structural Growth | 9.2%                    | 9.7%        | 12.3%                  | 11.4%       | 13.7%               | 12.3%       | 18.5%               | 20.5%       |
| <b>Market</b>     | <b>6.7%</b>             | <b>5.8%</b> | <b>7.6%</b>            | <b>7.3%</b> | <b>9.1%</b>         | <b>8.8%</b> | <b>9.5%</b>         | <b>6.9%</b> |

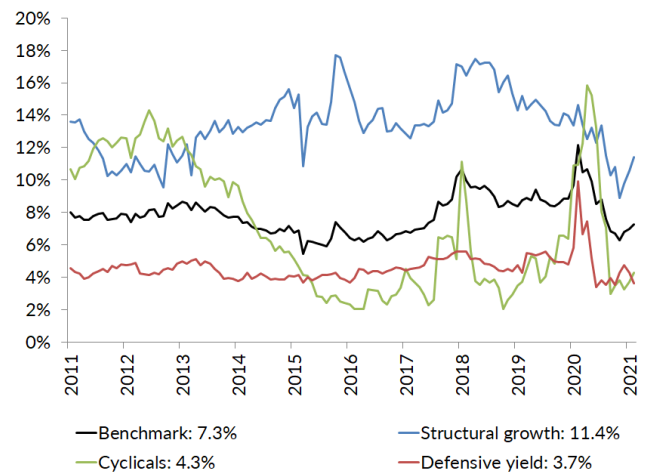
Source: Forsyth Barr analysis, Bloomberg

**Figure 25. 12-24m revenue growth – average**



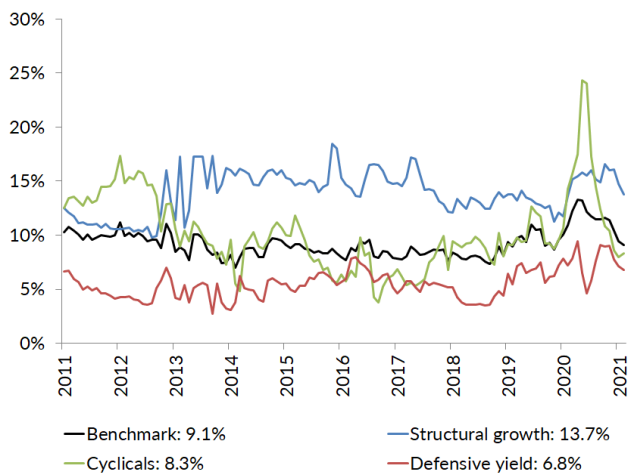
Source: Forsyth Barr analysis, Bloomberg

**Figure 26. 12-24m EBITDA growth – weighted average**



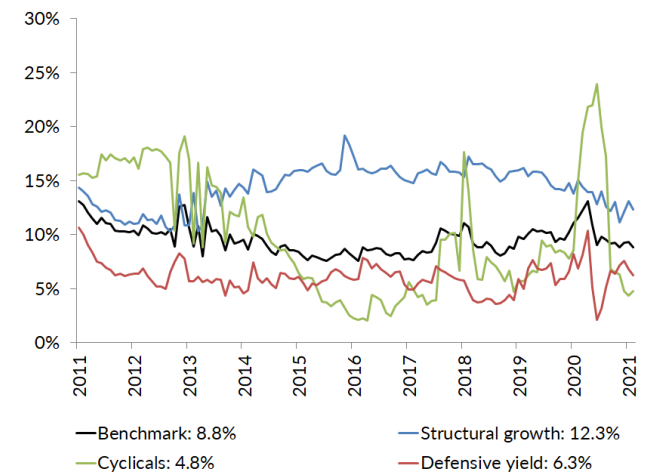
Source: Forsyth Barr analysis, Bloomberg

**Figure 27. 12-24m EPS growth – average**



Source: Forsyth Barr analysis, Bloomberg

**Figure 28. 12-24m EPS growth – weighted average**



Source: Forsyth Barr analysis, Bloomberg

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