

# F&P Healthcare

UNDERPERFORM

## 1H20 Preview — Pulse Check

We expect a strong 1H20 result from F&P Healthcare (FPH) on 27 November helped by some one-off boosts and driven by a strong result from Hospital, outweighing pressure in Homecare.

### Key issues to look for in the result

- **1H20 result:** We forecast NPAT of NZ\$121m, up +24% on the prior year or circa +10% adjusting for one-off benefits (minimal litigation spend, FX and NZ's change to R&D tax credit). This is broadly consistent with company guidance.
  - Hospital: We expect a strong result — with growth underpinned by 'new' applications, as adoption grows for nasal high flow oxygen therapy (Optiflow) in particular. Any update on progress outside of the Intensive Care Unit (ICU) is of interest.
  - Homecare: We expect a weak result in the key masks segment (constant currency revenue down -6%) given evident market share gains for competitors' new masks. This is unfavourable to margins. We assume new products are successful in changing this trajectory from FY21; albeit this is reliant on a favourable industry response in what is currently a competitive landscape of well-regarded products.
- **FY20 guidance:** Revised most recently on 14 October. Guidance is for revenue of ~NZ\$1.19bn, NPAT NZ\$255–265m using NZDUSD of 0.63. Our forecasts, and consensus, are at the upper end of this range.
- **FX:** Updated hedging, particularly NZDUSD (c. 50% of revenue in USD).
- **Capex:** Updated timing and progress, with key projects to support growth.
- **New products:** The recent new Homecare mask launch (full face mask, Vitera) takes one question off the table, although we look for further new products in this segment near-term. Any early feedback on Vitera from the key US market will be of particular interest, although it is only ~1 month since regulatory sign-off. We also look for updated commentary on recent new Hospital products.

### Investor briefing — 10am NZST on 27 November

10am NZST (8am AEST) on 27 November. The dial in is 09 913 3622 in NZ (+61 2 9193 3706 in Australia); the conference code is 8908013.

Figure 1. 1H20 result expectations

NZ\$m	1H19	1H20E	% chg	Forsyth Barr
Sales revenue	511.3	562.3	10%	562.3
EBITDA	158.9	187.6	18%	187.6
<b>NPAT</b>	<b>97.4</b>	<b>121.2</b>	<b>24%</b>	<b>121.2</b>
Underlying EPS (cps)	17.0	21.1	24%	21.1
Interim DPS (cps)	9.75	12.30	26%	12.30

Source: Forsyth Barr analysis, Company reports

### Investment View

FPH is a high quality company with an attractive outlook supported by a long runway of organic growth opportunities, particularly in the Hospital segment where clinical evidence continues to build. However, valuation metrics are elevated even when adjusting for growth, relative to global peers, which leaves little room for error. UNDERPERFORM.

NZX Code	FPH
Share price	NZ\$20.47
Target price	NZ\$16.00
Risk rating	Medium
Issued shares	572.8m
Market cap	NZ\$11,725m
Average daily turnover	611.1k (NZ\$9,520k)

### Share Price Performance



Financials: March	19A	20E	21E	22E
NPAT* (NZ\$m)	209.2	262.0	300.2	345.5
EPS* (NZc)	36.5	45.5	51.9	59.4
EPS growth* (%)	9.5	24.7	14.0	14.5
DPS (NZc)	23.3	29.0	34.0	39.0
Imputation (%)	100	100	100	100

Valuation (x)	19A	20E	21E	22E
EV/EBITDA	35.4	29.4	25.3	22.1
EV/EBIT	39.9	33.9	28.7	24.8
PE	n/a	44.9	39.4	34.4
Price / NTA	n/a	n/a	n/a	n/a
Cash dividend yield (%)	1.1	1.4	1.7	1.9
Gross dividend yield (%)	1.6	2.0	2.3	2.6

\*Historic and forecast numbers based on underlying profits

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**Fisher & Paykel Healthcare Corporation (FPH)** Priced as at 22 Nov 2019: NZ\$20.47

March year end

Forsyth Barr valuation					Valuation Ratios					
Valuation methodology					2018A 2019A 2020E 2021E 2022E					
Blended DCF/Compco					EV/EBITDA (x)	37.8	35.4	29.4	25.3	22.1
					EV/EBIT (x)	43.4	39.9	33.9	28.7	24.8
<b>12-month target price (NZ\$)*</b> <b>16.00</b>					PE (x)	61.3	56.0	44.9	39.4	34.4
Expected share price return					Price/NTA (x)	>100x	>100x	>100x	>100x	>100x
Net dividend yield					Free cash flow yield (%)	1.4	1.1	1.1	2.3	2.3
Estimated 12-month return					Net dividend yield (%)	1.0	1.1	1.4	1.7	1.9
					Gross dividend yield (%)	1.4	1.6	2.0	2.3	2.6
					Imputation (%)	100	100	100	100	100
					Pay-out ratio (%)	64	64	64	65	66
Key WACC assumptions					Capital Structure					
DCF valuation summary (NZ\$m)					2018A 2019A 2020E 2021E 2022E					
Risk free rate					Interest cover EBIT (x)	>100x	n/a	>100x	>100x	>100x
Equity beta					Interest cover EBITDA (x)	>100x	n/a	>100x	>100x	>100x
WACC					Net debt/ND+E (%)	-7.0	-6.3	-3.6	-11.5	-15.5
Terminal growth					Net debt/EBITDA (x)	n/a	n/a	n/a	n/a	n/a
Profit and Loss Account (NZ\$m)					Key Ratios					
2018A 2019A 2020E 2021E 2022E					2018A 2019A 2020E 2021E 2022E					
Sales revenue					Return on assets (%)	26.3	24.2	25.0	28.3	30.4
<b>Normalised EBITDA</b>					Return on equity (%)	25.0	22.9	25.6	26.2	26.8
Depreciation and amortisation					Return on funds employed (%)	28.0	26.8	27.4	29.9	32.5
<b>Normalised EBIT</b>					EBITDA margin (%)	31.5	30.8	33.3	34.3	34.5
Net interest					EBIT margin (%)	27.5	27.3	28.8	30.2	30.8
Associate income					Capex to sales (%)	8.5	11.7	12.6	4.9	7.1
Tax					Capex to depreciation (%)	238	366	332	141	223
Minority interests					Operating Performance					
<b>Normalised NPAT</b>					2018A 2019A 2020E 2021E 2022E					
Abnormals/other					<b>Sales revenue (NZ\$m)</b>					
<b>Reported NPAT</b>					Hospital					
Normalised EPS (cps)					Growth (%)					
DPS (cps)					Homecare					
					Growth (%)					
<b>Growth Rates</b>					<b>Core products - total</b>					
2018A 2019A 2020E 2021E 2022E					Distributed products					
Revenue (%)					<b>Total sales</b>					
EBITDA (%)					2018A 2019A 2020E 2021E 2022E					
EBIT (%)					Gross profit (NZ\$m)					
Normalised NPAT (%)					Gross margin (%)					
Normalised EPS (%)					R & D costs (NZ\$m)					
DPS (%)					as % of revenue					
					SG&A costs (NZ\$m)					
					as % of revenue					
<b>Cash Flow (NZ\$m)</b>					<b>Cost breakdown and margins</b>					
2018A 2019A 2020E 2021E 2022E					2018A 2019A 2020E 2021E 2022E					
<b>EBITDA</b>					<b>Key line items to call out</b>					
Working capital change					R&D tax credit (incl. as offset to tax)					
Interest & tax paid					Litigation costs within SG&A					
Other					Currency rates					
<b>Operating cash flow</b>					<b>Spot rates</b>					
Capital expenditure					NZDUSD					
(Acquisitions)/divestments					NZDEUR					
Other					<b>Effective rates</b>					
<b>Funding available/(required)</b>					NZDUSD					
Dividends paid					NZDEUR					
Equity raised/(returned)					<b>FX hedging</b>					
<b>Increase/(decrease) in net debt</b>					2020E 2021E 2022E					
					USD cover of expected exposure (%)					
					USD average rate of cover					
					EUR cover of expected exposure (%)					
					EUR average rate of cover					
Balance Sheet (NZ\$m)										
2018A 2019A 2020E 2021E 2022E										
Working capital										
Fixed assets										
Intangibles										
Other assets										
<b>Total funds employed</b>										
Net debt/(cash)										
Other non current liabilities										
Shareholder's funds										
Minority interests										
<b>Total funding sources</b>										

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

**Figure 2. Result expectations in more detail**

<b>NZ\$m</b>	<b>1H19</b>	<b>1H20E</b>	<b>% chg</b>	<b>Forsyth Barr</b>
Total revenue	511.3	562.3	10.0%	562.3
Cost of sales	(169.7)	(187.2)	10.3%	(187.2)
Gross profit	341.6	375.1	9.8%	375.1
R&D costs	(45.7)	(50.6)	10.7%	(50.6)
SG&A costs	(137.0)	(137.0)	-0.1%	(137.0)
<b>Total EBITDA</b>	<b>158.9</b>	<b>187.6</b>	<b>18.1%</b>	<b>187.6</b>
Deprec & Amort.	(22.4)	(26.6)	19.0%	(26.6)
Operating EBIT	136.5	161.0	17.9%	161.0
Other income	2.5	0.0	-100.0%	0.0
<b>Total EBIT</b>	<b>139.0</b>	<b>161.0</b>	<b>15.8%</b>	<b>161.0</b>
FX gain/loss	(3.4)	4.0	n/a	4.0
Net interest	0.3	(1.1)	-451.9%	(1.1)
Profit before tax	135.9	163.9	20.6%	163.9
Tax (net of R&D tax credit)	(38.5)	(42.7)	10.8%	(42.7)
<b>NPAT</b>	<b>97.4</b>	<b>121.2</b>	<b>24.5%</b>	<b>121.2</b>
Underlying EPS (cps)	17.0	21.1	24.0%	21.1
Interim DPS (cps)	9.75	12.30	26.2%	12.3
<b>Divisional breakdown</b>				
Hospital / RAC	297.3	355.3	19.5%	355.3
Homecare / OSA	211.1	204.8	-3.0%	204.8
Distributed / Other	2.9	2.3	-21.6%	2.3
<b>Total sales</b>	<b>511.3</b>	<b>562.3</b>	<b>10.0%</b>	<b>562.3</b>

Source: Forsyth Barr analysis, Company reports

## Investment summary

F&P Healthcare (FPH) has developed specialised expertise in heated humidification that forms the basis of its strong market position in the hospital and growing presence in homecare. It has progressively widened its addressable market through 'new' applications which is a key driver of an attractive, long-term, double-digit profit growth outlook. Valuation metrics are elevated even when adjusting for growth, relative to global peers, leaving little room for error. **UNDERPERFORM.**

### Business quality

- **Track record:** FPH has created value through continued product innovation and progressively widening its addressable market with 'new' applications of its technology to serve more patient groups and provide more products per patient.
- **Strong market position:** FPH's business model is supported by a high portion of recurring revenue (>85%) and strong global market position (including c. 70% share in the invasive ventilation market; c. 15% in sleep apnea and growing presence in areas where FPH is working to change clinical practice).
- **Attractive industry backdrop:** FPH operates in markets with high barriers to entry and where adoption curves are long. Structural trends are also supportive (ageing population, global focus on lowering healthcare costs and improving diagnosis rates).

### Earnings and cash flow outlook

- **Slower near-term constant currency revenue growth:** Increasingly reliant on the Hospital segment, with Homecare under pressure following a period of new product hiatus. Changing this trajectory is reliant on new products being successful.
- **Long-term growth thesis attractive:** FPH has a long runway of organic growth opportunities, particularly in the Hospital segment where clinical evidence continues to build for 'new' applications.

### Financial structure

- **Balance sheet:** FPH's target gearing range of -5% to +5% ensures flexibility for events like product recalls or hedging opportunities. We expect it to remain in a net cash position near-term.

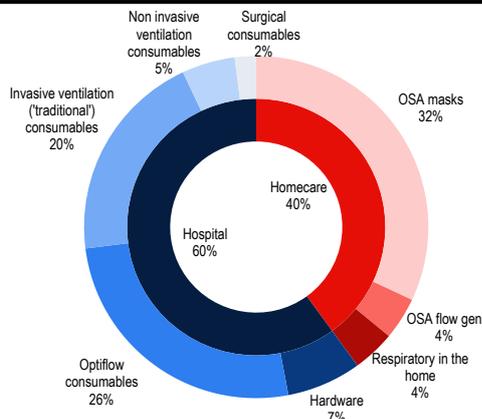
### Risks factors

- **Change in technology or medical treatments:** May result in some products becoming obsolete or cause it to incur costs to implement new technologies. There is some risk mitigation given FPH's diversified offering.

### Company description

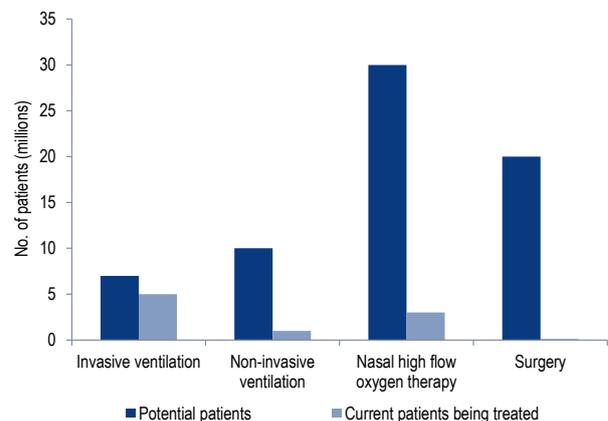
FPH designs, manufactures and markets heated humidifiers for use in respiratory care and humidified airflow generators for obstructive sleep apnea (OSA), along with associated single and multi-use accessories. FPH has a strong global market share in respiratory care following over 30 years in the market. The company leveraged its expertise in humidification products into the OSA market. It has a market share of 10%-15% and is the third player behind ResMed and Phillips Respironics. FPH has a range of over 2,700 products and accessories and sells its products globally.

Figure 3. Revenue breakdown by segment (est.)



Source: Company reports, Forsyth Barr analysis

Figure 4. Global market penetration in RAC / Hospital segment



Source: Company reports, Forsyth Barr analysis

**Figure 5. Substantial Shareholders**

Shareholder	Latest Holding
The Capital Group Companies	6.4%
The Vanguard Group	5.3%
BlackRock Investment Management	5.0%

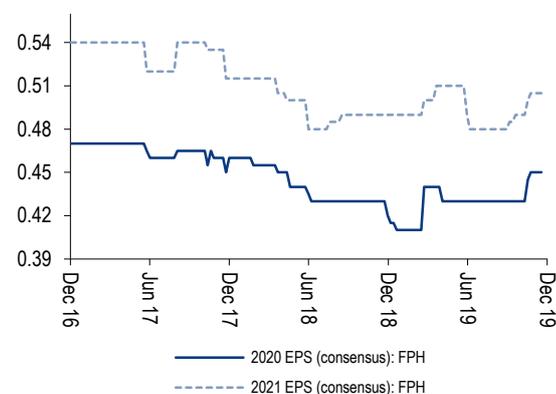
Source: NZX, Forsyth Barr analysis, NOTE: based on SSH notices only

**Figure 6. International Compco's**

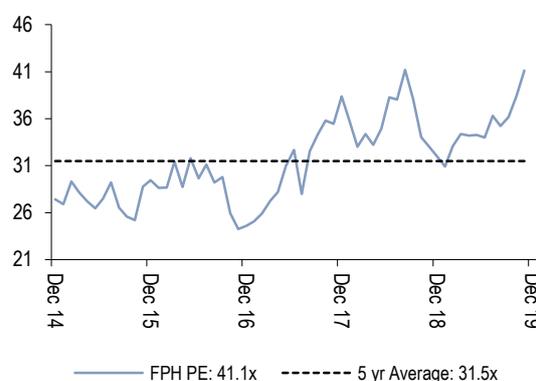
Company	Code	Price	Mkt Cap	PE		EV/EBITDA		EV/EBIT		Cash D/Yld
<i>(metrics re-weighted to reflect FPH's balance date - March)</i>										
			(m)	2020E	2021E	2020E	2021E	2020E	2021E	2021E
<b>F&amp;P Healthcare</b>	<b>FPH NZ</b>	<b>NZ\$20.47</b>	<b>NZ\$11,725</b>	<b>44.9x</b>	<b>39.4x</b>	<b>29.4x</b>	<b>25.2x</b>	<b>33.9x</b>	<b>28.6x</b>	<b>1.7%</b>
ResMed Inc	RMD US	US\$146.43	US\$21,055	40.4x	33.3x	25.5x	22.5x	30.5x	26.1x	1.1%
Teleflex Inc	TFX US	US\$350.46	US\$16,225	30.6x	26.6x	21.7x	19.3x	27.1x	24.2x	0.4%
Boston Scientific Corp	BSX US	US\$42.25	US\$58,882	26.1x	22.9x	20.7x	18.3x	23.9x	20.9x	n/a
Becton Dickinson and Co	BDX US	US\$249.37	US\$67,318	41.4x	18.8x	18.1x	14.2x	33.5x	17.3x	1.5%
<b>Compco Average:</b>				<b>34.6x</b>	<b>25.4x</b>	<b>21.5x</b>	<b>18.6x</b>	<b>28.7x</b>	<b>22.1x</b>	<b>1.0%</b>
<b>FPH Relative:</b>				<b>+30%</b>	<b>+55%</b>	<b>+37%</b>	<b>+36%</b>	<b>+18%</b>	<b>+30%</b>	<b>+65%</b>

*EV = Current Market Cap + Actual Net Debt*

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

**Figure 7. Consensus EPS Momentum**


Source: Forsyth Barr analysis, Bloomberg

**Figure 8. 12 Month Forward PE**


Source: Forsyth Barr analysis

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