

# F&P Healthcare

## 1H21 Result – The Final Wave?

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**UNDERPERFORM** 

F&P Healthcare's (FPH) 1H21 result was unsurprisingly dominated by COVID-19, which remains an ongoing and extraordinary tailwind, given its products continue to be used as front-line therapy. There was little in the way of new information to help answer the key question – what does the earnings path look like beyond COVID-19? It is clear monthly volatility in growth is extreme, demand still strong, while visibility is low on the minutiae of useage. FPH is a high quality growth company, however, market expectations are high. We expect growth to be difficult when Hospital equipment sales fade from elevated levels, hospitalisations slow and as FPH begins to cycle larger numbers from late 4Q21. Growing newsflow and progress with a vaccine, along with the likelihood of a low (or non-existent) flu season may also drag. We see better value growth stocks in both the NZ market and globally.

NZX Code	FPH	Financials: Mar/	20A	21E	22E	23E	Valuation (x)	20A	21E	22E	23E
Share price	NZ\$33.55	NPAT* (NZ\$m)	287.3	441.3	405.7	457.9	PE	67.1	43.8	47.8	42.5
Target price	NZ\$32.50	EPS* (NZc)	50.0	76.7	70.2	78.9	EV/EBIT	50.7	32.1	35.2	31.2
Risk rating	Medium	EPS growth* (%)	37.0	53.2	-8.5	12.4	EV/EBITDA	43.7	28.8	30.9	27.7
Issued shares	574.2m	DPS (NZc)	27.5	38.0	40.0	45.0	Price / NTA	21.3	17.0	14.9	13.1
Market cap	NZ\$19,264m	Imputation (%)	100	100	100	100	Cash div yld (%)	0.8	1.1	1.2	1.3
Avg daily turnover	862.9k (NZ\$25,684k)	*Based on normalised profits					Gross div yld (%)	1.1	1.6	1.7	1.9

**What's changed?**

- **Earnings:** FY21E revised to NZ\$441m, +8% and materially above FPH's revised 'guide'. Changes thereafter modest (+1–2%).

**1H21 unsurprisingly stellar; a modest beat vs our expectations**

1H21 can only be described as exceptional. Constant currency (CC) revenue growth of +61% and operating leverage (despite a step-change in freight costs) saw NPAT +87% – with the sharp spike in demand evidently well managed. The unsurprising highlight was Hospital revenue +94% (Hardware +383%; Consumables +44%), although FPH made it clear there is large monthly variability. Our interpretation is a slightly softer finish to 1H21, albeit strong start to 2H21. Homecare has held up, despite some pressures from new patient diagnosis. The 1H21 result was modestly ahead of our expectations primarily from higher Hospital hardware sales.

**A well anticipated upgrade to FPH's 'guide', with tailwinds continuing into 2H21; assumption set still appears conservative**

FPH once again upgraded its FY21 'guide' which came as no surprise given the resurgence of COVID-19 hospitalisations globally. The revised 'guide' is for revenue of ~NZ\$1.72bn and NPAT of NZ\$400–415m, backed by a set of assumptions including that Hospital hardware sales normalise from January 2021 and utilisation levels normalise across 2H21. Whilst the situation is clearly very volatile and difficult to forecast, we (again) view FPH's assumption set as conservative.

**Where to thereafter? Mix differences in 1H21 less favourable than expected**

The path beyond FY21 remains an area of debate and there was little in the way of new information to help better understand the path forward. 1H21 did see mix differences versus our expectations – (1) stronger skew of hardware to traditional humidifiers (850/950), and (2) stronger skew of consumables to traditional IV, where growth was higher than we forecast while new consumables (Optiflow) was weaker. We see heightened IV demand as less sustainable at current levels (we assume at some point ICU demand reverts to 'normal'), whereas Optiflow has a longer runway of opportunity given current penetration is still low.

**Fisher & Paykel Healthcare Corporation (FPH)**

Priced as at 25 Nov 2020 (NZ\$)						33.55						
<b>12-month target price (NZ\$)*</b>						<b>32.50</b>	<b>Spot valuations (NZ\$)</b>					
Expected share price return						-3.1%	1. DCF					33.13
Net dividend yield						1.2%	2. Compco					27.25
Estimated 12-month return						-2.0%	3. n/a					n/a
<b>Key WACC assumptions</b>						<b>DCF valuation summary (NZ\$m)</b>						
Risk free rate						1.30%	Total firm value					19,251
Equity beta						0.77	(Net debt)/cash					0
WACC						5.2%	Less: Capitalised operating leases					(207)
Terminal growth						1.5%	Value of equity					19,044
<b>Profit and Loss Account (NZ\$m)</b>						<b>Valuation Ratios</b>						
	2019A	2020A	2021E	2022E	2023E		2019A	2020A	2021E	2022E	2023E	
Sales revenue	1,070	1,264	1,798	1,669	1,848	EV/EBITDA (x)	57.5	43.6	28.8	30.9	27.7	
<b>Normalised EBITDA</b>	<b>334</b>	<b>440</b>	<b>667</b>	<b>620</b>	<b>692</b>	EV/EBIT (x)	65.7	50.7	32.0	35.2	31.2	
Depreciation and amortisation	(42)	(61)	(68)	(76)	(78)	PE (x)	91.9	67.1	43.8	47.8	42.5	
<b>Normalised EBIT</b>	<b>293</b>	<b>379</b>	<b>599</b>	<b>544</b>	<b>614</b>	Price/NTA (x)	22.6	21.3	17.0	14.9	13.1	
Net interest	1	(2)	(1)	(0)	1	Free cash flow yield (%)	0.7	0.9	1.4	1.8	2.0	
Associate income	0	0	0	0	0	Net dividend yield (%)	0.7	0.8	1.1	1.2	1.3	
Tax	(82)	(83)	(157)	(139)	(157)	Gross dividend yield (%)	1.0	1.1	1.6	1.7	1.9	
Minority interests	0	0	0	0	0	<b>Capital Structure</b>						
<b>Normalised NPAT</b>	<b>209</b>	<b>287</b>	<b>441</b>	<b>406</b>	<b>458</b>	Interest cover EBIT (x)	n/a	>100x	>100x	>100x	n/a	
Abnormals/other	0	0	0	0	0	Interest cover EBITDA (x)	n/a	>100x	>100x	>100x	n/a	
<b>Reported NPAT</b>	<b>209</b>	<b>287</b>	<b>441</b>	<b>406</b>	<b>458</b>	Net debt/ND+E (%)	-6.3	-4.5	-11.0	-21.0	-29.9	
Normalised EPS (cps)	36.5	50.0	76.7	70.2	78.9	Net debt/EBITDA (x)	n/a	n/a	n/a	n/a	n/a	
DPS (cps)	23.3	27.5	38.0	40.0	45.0	<b>Key Ratios</b>						
<b>Growth Rates</b>						2019A	2020A	2021E	2022E	2023E		
Revenue (%)	9.1	18.1	42.3	-7.2	10.7	Return on assets (%)	24.2	26.0	33.5	30.0	31.9	
EBITDA (%)	6.3	31.7	51.5	-7.0	11.6	Return on equity (%)	22.9	29.4	36.0	28.9	28.4	
EBIT (%)	8.5	29.6	57.9	-9.1	12.8	Return on funds employed (%)	26.8	33.0	43.4	35.8	38.0	
Normalised NPAT (%)	10.0	37.3	53.6	-8.1	12.8	EBITDA margin (%)	31.2	34.8	37.1	37.2	37.5	
Normalised EPS (%)	9.5	37.0	53.2	-8.5	12.4	EBIT margin (%)	27.3	30.0	33.3	32.6	33.2	
Ordinary DPS (%)	9.4	18.3	38.2	5.3	12.5	Capex to sales (%)	11.7	12.3	10.6	6.7	6.8	
<b>Cash Flow (NZ\$m)</b>						2019A	2020A	2021E	2022E	2023E		
<b>EBITDA</b>	<b>334</b>	<b>440</b>	<b>667</b>	<b>620</b>	<b>692</b>	Capex to depreciation (%)	366	322	347	180	198	
Working capital change	2	(23)	(44)	(14)	(28)	Imputation (%)	100	100	100	100	100	
Interest & tax paid	(83)	(96)	(157)	(139)	(156)	Pay-out ratio (%)	64	55	50	57	57	
Other	0	0	0	0	0	<b>Operating Performance</b>						
<b>Operating cash flow</b>	<b>253</b>	<b>321</b>	<b>465</b>	<b>467</b>	<b>508</b>	<b>Sales revenue (NZ\$m)</b>	2019A	2020A	2021E	2022E	2023E	
Capital expenditure	(126)	(156)	(190)	(112)	(126)	Hospital	642	801	1,324	1,145	1,275	
(Acquisitions)/divestments	0	0	0	0	0	Growth (%)	12	25	65	(14)	11	
Other	0	(10)	(7)	(8)	(8)	Homecare	421	457	469	518	567	
<b>Funding available/(required)</b>	<b>128</b>	<b>156</b>	<b>268</b>	<b>348</b>	<b>374</b>	Growth (%)	6	9	2	11	9	
Dividends paid	(115)	(146)	(188)	(225)	(247)	<b>Core products - total</b>	<b>1,064</b>	<b>1,259</b>	<b>1,793</b>	<b>1,664</b>	<b>1,842</b>	
Equity raised/(returned)	2	0	0	0	0	Distributed products	7	5	5	5	5	
<b>(Increase)/decrease in net debt</b>	<b>15</b>	<b>10</b>	<b>79</b>	<b>123</b>	<b>128</b>	<b>Total sales</b>	<b>1,070</b>	<b>1,264</b>	<b>1,798</b>	<b>1,669</b>	<b>1,848</b>	
<b>Balance Sheet (NZ\$m)</b>						2019A	2020A	2021E	2022E	2023E		
Working capital	159	204	248	262	290	<b>Cost breakdown and margins</b>						
Fixed assets	601	711	828	857	896	Gross profit	716	836	1,130	1,104	1,223	
Intangibles	62	74	89	105	124	Gross margin (%)	66.9	66.1	62.9	66.2	66.2	
Right of use asset	0	25	24	24	23	R & D costs	(100)	(119)	(142)	(146)	(161)	
Other assets	109	137	136	136	135	SG&A costs (ex D&A)	(286)	(277)	(321)	(337)	(370)	
<b>Total funds employed</b>	<b>931</b>	<b>1,149</b>	<b>1,325</b>	<b>1,384</b>	<b>1,468</b>	Key line items to call out						
Net debt/(cash)	(54)	(42)	(122)	(244)	(372)	R&D tax credit (incl. as offset to tax)	n/a	13	14	16	18	
Lease liability	0	34	36	38	39	Litigation costs within SG&A	(23)	0	0	0	0	
Other liabilities	72	181	184	186	187	<b>Currency</b>						
Shareholder's funds	913	977	1,226	1,404	1,614	NZDUSD spot rate	0.68	0.65	0.69	0.68	0.67	
Minority interests	0	0	0	0	0	NZDEUR spot rate	0.59	0.58	0.57	0.56	0.56	
<b>Total funding sources</b>	<b>931</b>	<b>1,149</b>	<b>1,325</b>	<b>1,384</b>	<b>1,468</b>	USD hedging - % cover			95	75	40	
								0.65	0.66	0.64		

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

## 1H21 result – key features

FPH reported a stellar 1H21 result with NPAT of NZ\$225m up +87% in constant currency (CC), modestly ahead of our forecasts.

- **Exceptional period of demand:** COVID-19 tailwinds were evident across its Hospital portfolio, with a marked spike in Hardware demand and strong growth for Consumables across both its traditional business and 'new' applications. Homecare revenue growth was more muted, with headwinds in sleep apnea (particularly new patient diagnosis), albeit strength in 'new' applications.
- **Operating leverage evident,** despite materially lower gross margins (-420bp in CC) due to higher freight costs (including a greater use of air freight). Operating margins up +610bp CC, with SG&A cost growth dwarfed by revenue growth.
- **Balance sheet, cashflow and dividend:** FPH retains a net cash position, with gearing of -7% slightly below its target range (-5% to 5%). Operating and free cash flow were unsurprisingly strong, despite a step-up in capex to support growth. FPH's interim dividend was below our forecasts, with growth materially below profit growth – we forecast a FY21E cash yield of c. 1%.

Figure 1. 1H21 result snapshot (NZ\$m)

	1H20	1H21	% chg	CC* growth	Forsyth Barr	% diff
Total revenue	570.9	910.2	59%	61%	880.3	3%
EBIT	166.0	309.2	86%	95%	292.1	6%
NPAT	121.2	225.5	86%	87%	216.3	4%
EPS	21.1	39.2	85%	86%	37.5	4%
DPS (cps)	12.0	16.0	33%	33%	18.0	-11%

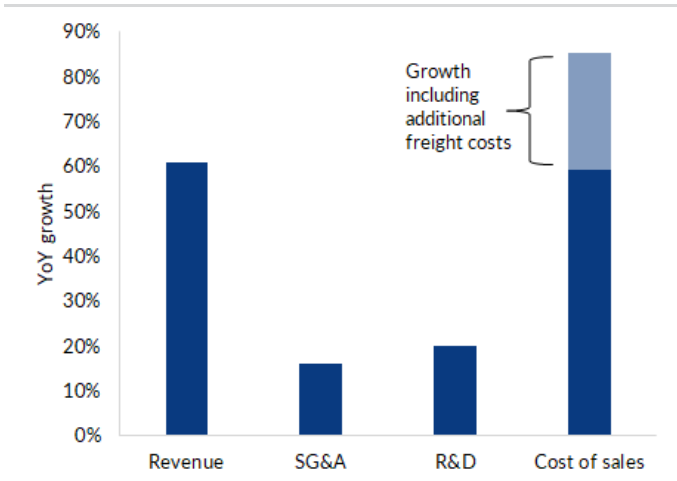
Source: Forsyth Barr analysis, Company reports \*CC = Constant Currency

Figure 2. Divisional detail (NZ\$m)

	1H20	1H21	% chg	CC growth	% of group
Hospital hardware	53.0	252.0	375%	383%	28%
IV consumables	111.2	158.7	43%	44%	17%
'New app' consumables	189.4	270.3	43%	43%	30%
<b>Total Hospital</b>	<b>353.6</b>	<b>681.0</b>	<b>93%</b>	<b>94%</b>	<b>75%</b>
Homecare	214.7	226.2	5%	6%	25%
Distributed / Other	2.6	3.0	15%	16%	0%
<b>Total revenue</b>	<b>570.9</b>	<b>910.2</b>	<b>59%</b>	<b>61%</b>	<b>100%</b>

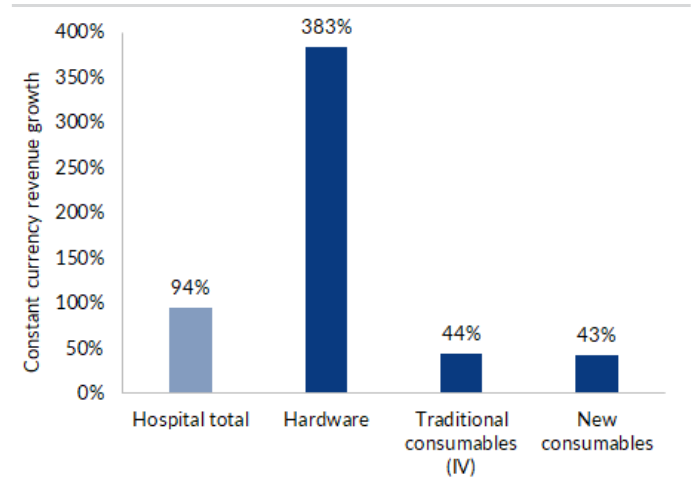
Source: Forsyth Barr analysis, Company reports

Figure 3. Revenue growth outpaces costs in 1H21



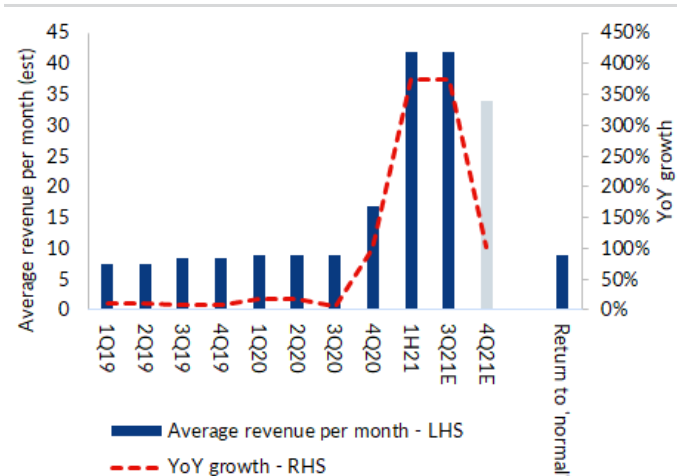
Source: Forsyth Barr analysis, Company reports

Figure 4. Hospital revenue growth by the pieces



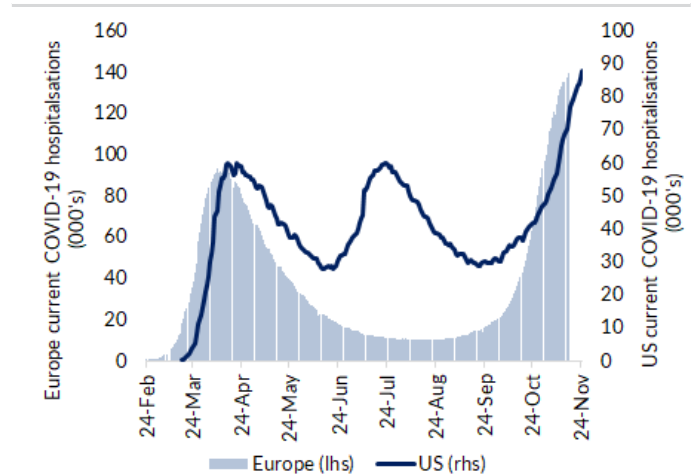
Source: Forsyth Barr analysis, Company reports

Figure 5. Hospital hardware demand profile



Source: Forsyth Barr analysis, Company reports

Figure 6. COVID-19 hospitalisations lifting in key markets



Source: Forsyth Barr analysis, European CDC, US CDC

## Earnings and target price

We lift our FY21E forecasts with higher Hospital revenue and a small lift in margins outpacing the negative impact from the strength in the NZ dollar. Within the Hospital segment we have materially upgraded Hardware sales and lifted IV consumable sales which outweighs lower forecasts for new consumable sales (NIV and Optiflow). Our upgrades are more modest from FY22E. We assume COVID-19 tailwinds continue into 1Q22.

Our revised FY21E NPAT is well ahead of company guidance (NZ\$400–415m), primarily due to higher revenue expectations (NZ\$1.8bn vs FPH 'guide' of ~NZ\$1.72bn) from stronger COVID-19 tailwinds within the Hospital segment for the balance of 2H21.

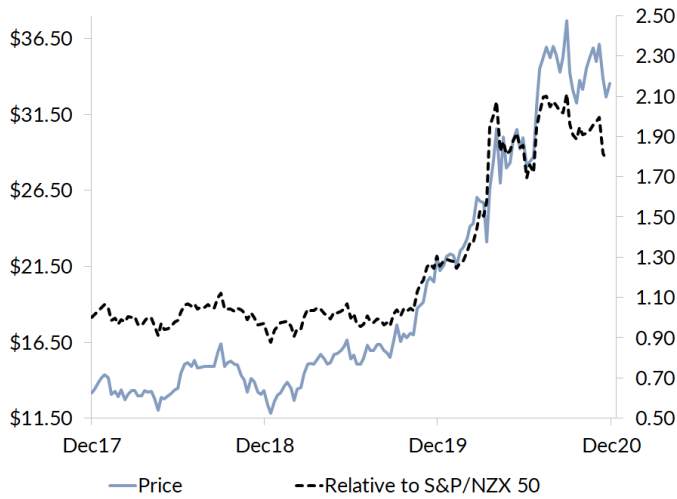
Our target price is unchanged at NZ\$32.50 – with our DCF modestly lower (mix changes in favour of traditional Hospital business less favourable to longer-term forecasts), albeit peer multiples are higher.

**Figure 7. Earnings revisions (NZ\$m)**

NZ\$m	FY20A		FY21E		FY22E			FY23E		
	Actual	Old	New	% chg	Old	New	% chg	Old	New	% chg
Total revenue	1,263.7	1,705.3	1,798.1	5.4%	1,673.0	1,668.9	-0.2%	1,868.4	1,847.6	-1.1%
EBIT	379.3	552.0	598.7	8.3%	537.0	544.4	1.4%	607.3	614.0	1.1%
Normalised Profit	287.3	408.7	441.3	8.0%	399.2	405.7	1.6%	451.8	457.9	1.3%
Normalised EPS (cps)	50.0	71.0	76.7	8.0%	69.1	70.2	1.6%	77.8	78.9	1.3%
Dividend per share (cps)	27.5	39.0	38.0	-2.6%	41.0	40.0	-2.4%	47.0	45.0	-4.3%

Source: Forsyth Barr analysis, Company reports

Figure 8. Price performance



Source: Forsyth Barr analysis

Figure 9. Substantial shareholders

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

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

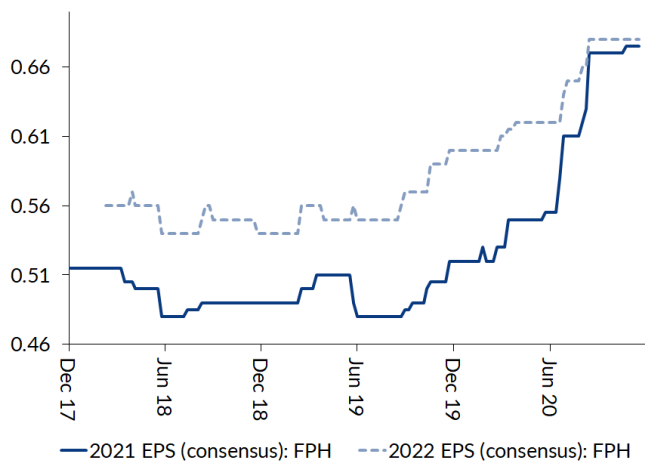
Figure 10. International valuation comparisons

Company	Code	Price	Mkt Cap (m)	PE		EV/EBITDA		EV/EBIT		Cash Yld
				2021E	2022E	2021E	2022E	2021E	2022E	
F&P Healthcare	FPH NZ	NZ\$33.55	NZ\$19,264	43.8x	47.8x	28.8x	31.0x	32.1x	35.3x	1.2%
RESMED INC	RMD US	US\$211.02	US\$30,580	43.3x	39.6x	30.1x	28.1x	35.0x	32.3x	0.8%
TELEFLEX INC	TFX US	US\$370.61	US\$17,258	33.8x	27.8x	26.2x	21.3x	32.1x	25.2x	0.4%
BOSTON SCIENTIFIC CORP	BSX US	US\$33.70	US\$48,256	29.1x	19.8x	21.0x	15.7x	26.1x	17.7x	0.0%
BECTON DICKINSON AND CO	BDX US	US\$231.87	US\$67,212	>50x	17.9x	18.5x	13.9x	36.2x	16.6x	1.7%
<b>Compco Average:</b>				<b>35.4x</b>	<b>26.3x</b>	<b>23.9x</b>	<b>19.8x</b>	<b>32.4x</b>	<b>23.0x</b>	<b>0.7%</b>
<b>FPH Relative:</b>				<b>24%</b>	<b>82%</b>	<b>20%</b>	<b>57%</b>	<b>-1%</b>	<b>54%</b>	<b>67%</b>

EV = Current Market Cap + Actual Net Debt

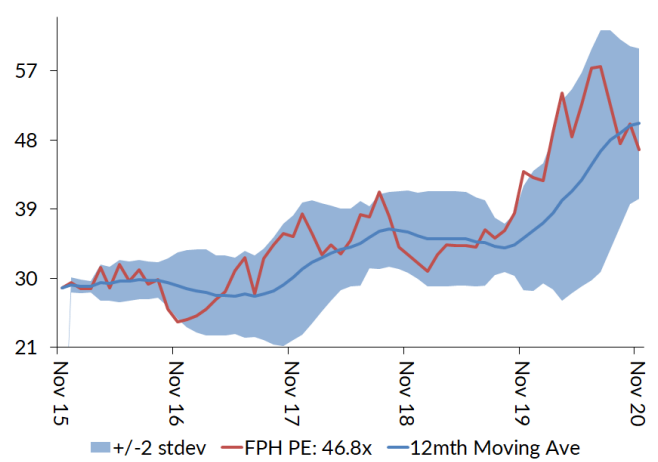
Source: \*Forsyth Barr analysis, Bloomberg Consensus, Compco metrics re-weighted to reflect headline (FPH) companies fiscal year end

Figure 11. Consensus EPS momentum (NZ\$)



Source: Forsyth Barr analysis

Figure 12. One year forward PE (x)



Source: Forsyth Barr analysis

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