

F&P Healthcare

3Q21 Surge; All Eyes on the Vaccine

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UNDERPERFORM

F&P Healthcare (FPH) provided a strong 3Q21 trading update, with the magnitude and duration of COVID-19 tailwinds (once again) larger than expected for its Hospital products. Data points and industry anecdotes point to similar trends for respiratory peers and competitors. It has been difficult to accurately forecast the upside, and we expect it to be equally difficult to pre-empt the magnitude and timing of the demand slowdown, driven by the (hopeful) success of vaccine rollouts, starting with high risk groups. We expect to see a decline in earnings as Hospital hardware and IV consumables demand fades from elevated COVID-19 boosted levels, even when giving FPH the benefit of the doubt that growth in Optiflow consumables can continue from current levels. There remain a lot of unknowns and there is risk the market overcapitalises current earnings. We see better risk/reward elsewhere in the NZ market and global Healthcare sector.

NZX Code	FPH	Financials: Mar/	20A	21E	22E	23E	Valuation (x)	20A	21E	22E	23E
Share price	NZ\$35.10	NPAT* (NZ\$m)	287.3	549.4	431.9	467.5	PE	70.2	36.8	47.0	43.6
Target price	NZ\$33.00	EPS* (NZc)	50.0	95.5	74.7	80.5	EV/EBIT	53.2	26.8	34.6	31.9
Risk rating	Medium	EPS growth* (%)	37.0	90.8	-21.7	7.8	EV/EBITDA	45.8	24.6	30.6	28.3
Issued shares	575.5m	DPS (NZc)	27.5	48.0	51.0	56.0	Price / NTA	22.3	16.6	15.1	13.8
Market cap	NZ\$20,201m	Imputation (%)	100	100	100	100	Cash div yld (%)	0.8	1.4	1.5	1.6
Avg daily turnover	892.6k (NZ\$27,783k)	*Based on normalised profits					Gross div yld (%)	1.1	1.9	2.0	2.2

What's changed?

- **Earnings:** FY21/22/23E NPAT revised +20%/+6%/+2% – reflecting larger COVID-19 near-term tailwinds for revenue.
- **Target price:** Revised to NZ\$33, +3%, in line with medium-term earnings revisions.

A higher COVID-19 peak boosts 3Q revenue

FPH reported 9m21 revenue growth of +73% on the prior year in constant currency, an acceleration on 1H21 of +61%. Hospital remains the standout, with exceptional growth in both Hardware, +446% (vs 1H21 +383%), and Consumables +54% (1H21 +44%). Homecare revenue, +6%, was broadly consistent with expectations. Higher COVID-19 hospitalisations has driven strong demand for FPH's Hospital products, which are used as a front-line therapy for COVID-19. We were expecting an acceleration in Consumables growth in 3Q21, given recent hospitalisation data and industry anecdotes, while the elevated Hardware demand has continued to surprise us (and industry participants) on the upside in both magnitude and duration. We expect to see strong operating leverage to the bumper 3Q result, which was well ahead of FPH forecasts, with limited additional SG&A and R&D costs.

Earnings path from here?

FPH has removed FY21 guidance, with monthly data points still highly volatile. We expect slower reported growth in 4Q21 as FPH begins to cycle the start of the virus in China. There is no doubt it will be an extraordinary year, however attention is firmly on where to thereafter? The extent and duration of COVID-19 tailwinds has been difficult to forecast to date, and exceeded all expectations as hospitalisations have climbed globally. However, with vaccine rollouts recently commenced in a number of countries (prioritising those groups most at risk of hospitalisation), coupled with continued control measures, we expect to see demand slow over the next 12 months. Israel is one of the most advanced in the vaccine rollout, having vaccinated ~29% of its population to date since late December 2020 (one dose) and more than 80% of those 60 years+, so will be a key market to watch. Figure 6 highlights progress, with early signs of a change in the trajectory of new COVID-19 case numbers, which have been in decline in recent weeks.

Fisher & Paykel Healthcare Corporation (FPH)

Priced as at 22 Jan 2021 (NZ\$) **35.10**

12-month target price (NZ\$)*	33.00
Expected share price return	-6.0%
Net dividend yield	1.4%
Estimated 12-month return	-4.5%

Key WACC assumptions	
Risk free rate	1.30%
Equity beta	0.77
WACC	5.2%
Terminal growth	1.5%

Spot valuations (NZ\$)	
1. DCF	33.78
2. Compco	28.56
3. n/a	n/a

DCF valuation summary (NZ\$m)	
Total firm value	19,667
(Net debt)/cash	0
Less: Capitalised operating leases	(274)
Value of equity	19,393

Profit and Loss Account (NZ\$m)	2019A	2020A	2021E	2022E	2023E
Sales revenue	1,070	1,264	2,017	1,696	1,817
Normalised EBITDA	334	440	818	656	708
Depreciation and amortisation	(42)	(61)	(68)	(76)	(80)
Normalised EBIT	293	379	750	580	628
Net interest	1	(2)	(1)	0	1
Associate income	0	0	0	0	0
Tax	(82)	(83)	(200)	(149)	(161)
Minority interests	0	0	0	0	0
Normalised NPAT	209	287	549	432	467
Abnormals/other	0	0	0	0	0
Reported NPAT	209	287	549	432	467
Normalised EPS (cps)	36.5	50.0	95.5	74.7	80.5
DPS (cps)	23.3	27.5	48.0	51.0	56.0

Growth Rates	2019A	2020A	2021E	2022E	2023E
Revenue (%)	9.1	18.1	59.6	-15.9	7.1
EBITDA (%)	6.3	31.7	85.7	-19.8	7.9
EBIT (%)	8.5	29.6	97.7	-22.6	8.2
Normalised NPAT (%)	10.0	37.3	91.2	-21.4	8.2
Normalised EPS (%)	9.5	37.0	90.8	-21.7	7.8
Ordinary DPS (%)	9.4	18.3	74.5	6.3	9.8

Cash Flow (NZ\$m)	2019A	2020A	2021E	2022E	2023E
EBITDA	334	440	818	656	708
Working capital change	2	(23)	(74)	12	(19)
Interest & tax paid	(83)	(96)	(200)	(148)	(161)
Other	0	0	0	0	0
Operating cash flow	253	321	543	520	529
Capital expenditure	(126)	(156)	(190)	(142)	(177)
(Acquisitions)/divestments	0	0	0	0	0
Other	0	(10)	(7)	(8)	(8)
Funding available/(required)	128	156	346	370	343
Dividends paid	(115)	(146)	(217)	(286)	(311)
Equity raised/(returned)	2	0	0	0	0
(Increase)/decrease in net debt	15	10	129	84	33

Balance Sheet (NZ\$m)	2019A	2020A	2021E	2022E	2023E
Working capital	159	204	278	266	285
Fixed assets	601	711	828	887	975
Intangibles	62	74	89	105	124
Right of use asset	0	25	24	24	23
Other assets	109	137	136	136	135
Total funds employed	931	1,149	1,355	1,418	1,543
Net debt/(cash)	(54)	(42)	(171)	(255)	(288)
Lease liability	0	34	36	38	39
Other liabilities	72	181	184	186	187
Shareholder's funds	913	977	1,306	1,449	1,604
Minority interests	0	0	0	0	0
Total funding sources	931	1,149	1,355	1,418	1,543

* 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)	60.3	45.8	24.6	30.5	28.3
EV/EBIT (x)	68.9	53.1	26.8	34.5	31.9
PE (x)	96.1	70.2	36.8	47.0	43.6
Price/NTA (x)	23.6	22.3	16.6	15.1	13.8
Free cash flow yield (%)	0.6	0.8	1.7	1.9	1.7
Net dividend yield (%)	0.7	0.8	1.4	1.5	1.6
Gross dividend yield (%)	0.9	1.1	1.9	2.0	2.2

Capital Structure	2019A	2020A	2021E	2022E	2023E
Interest cover EBIT (x)	n/a	>100x	>100x	n/a	n/a
Interest cover EBITDA (x)	n/a	>100x	>100x	n/a	n/a
Net debt/ND+E (%)	-6.3	-4.5	-15.0	-21.3	-21.8
Net debt/EBITDA (x)	n/a	n/a	n/a	n/a	n/a

Key Ratios	2019A	2020A	2021E	2022E	2023E
Return on assets (%)	24.2	26.0	40.4	31.4	31.5
Return on equity (%)	22.9	29.4	42.1	29.8	29.1
Return on funds employed (%)	26.8	33.0	53.2	37.1	37.2
EBITDA margin (%)	31.2	34.8	40.6	38.7	39.0
EBIT margin (%)	27.3	30.0	37.2	34.2	34.6
Capex to sales (%)	11.7	12.3	9.4	8.4	9.7
Capex to depreciation (%)	366	322	347	229	271
Imputation (%)	100	100	100	100	100
Pay-out ratio (%)	64	55	50	68	70

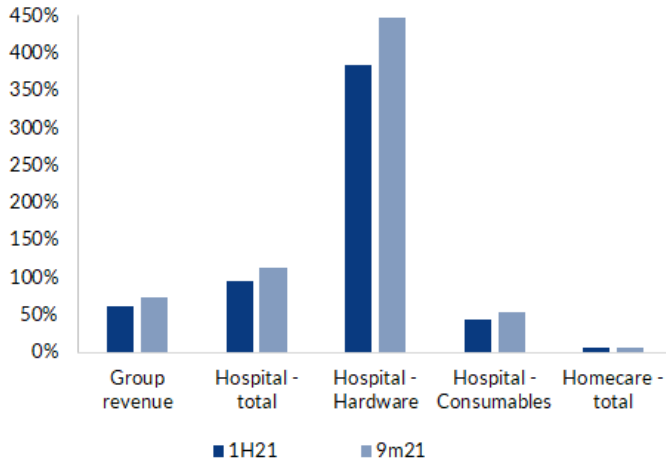
Operating Performance	2019A	2020A	2021E	2022E	2023E
Sales revenue (NZ\$m)					
Hospital	642	801	1,528	1,162	1,230
Growth (%)	12	25	91	(24)	6
Homecare	421	457	483	528	581
Growth (%)	6	9	6	9	10
Core products - total	1,064	1,259	2,011	1,690	1,811
Distributed products	7	5	5	5	5
Total sales	1,070	1,264	2,017	1,696	1,817

Cost breakdown and margins					
Gross profit	716	836	1,281	1,143	1,227
Gross margin (%)	66.9	66.1	63.5	67.4	67.5
R & D costs	(100)	(119)	(142)	(149)	(159)
SG&A costs (ex D&A)	(286)	(277)	(321)	(337)	(360)
Key line items to call out					
R&D tax credit (incl. as offset to tax)	n/a	13	14	17	18
Litigation costs within SG&A	(23)	0	0	0	0

Currency					
NZDUSD spot rate	0.68	0.65	0.67	0.67	0.67
NZDEUR spot rate	0.59	0.58	0.57	0.56	0.56
USD hedging - % cover			95	75	40
USD hedging - average rate			0.65	0.66	0.64

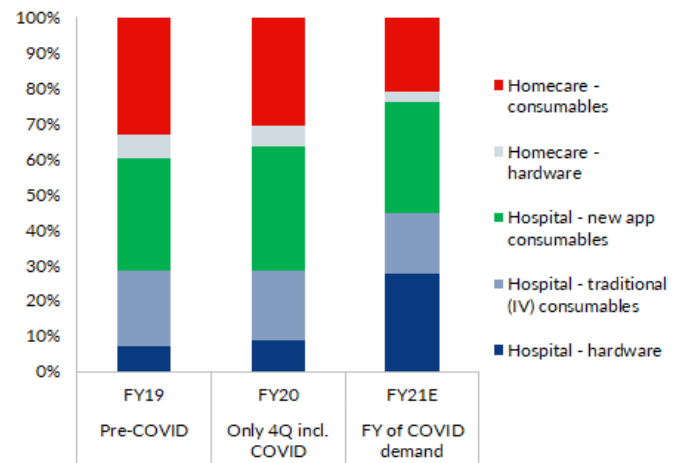
Key charts and tables

Figure 1. FPH constant currency YoY growth



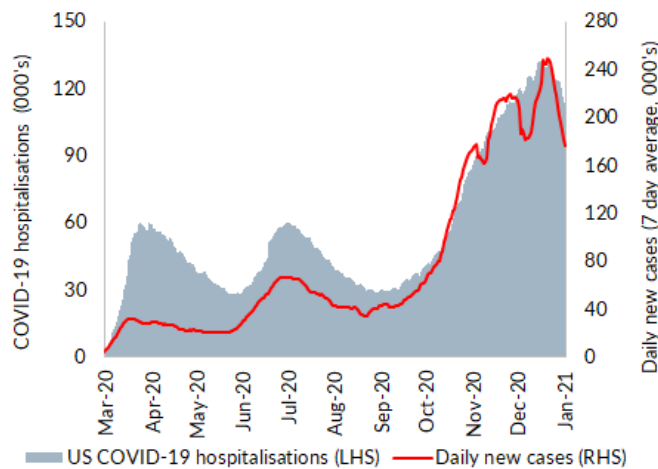
Source: Forsyth Barr analysis, Company reports

Figure 2. FPH revenue breakdown



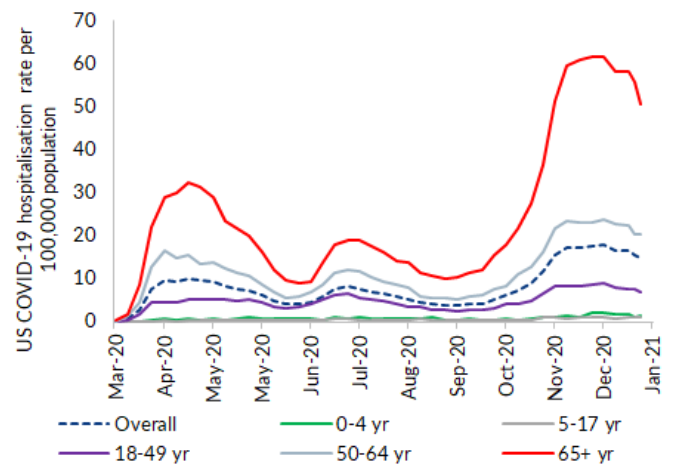
Source: Forsyth Barr analysis, Company reports

Figure 3. US COVID-19 cases and hospitalisations



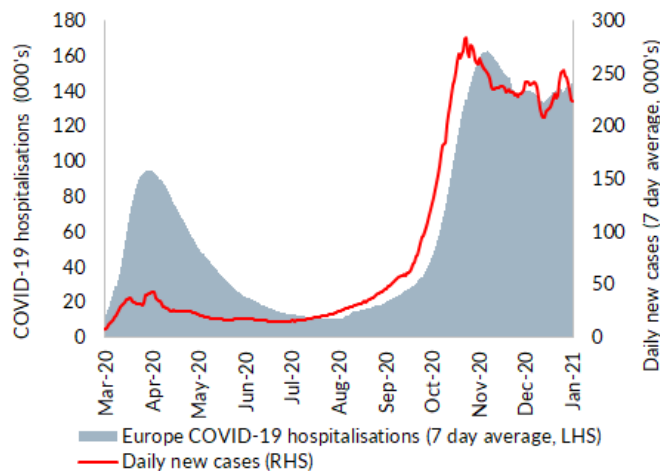
Source: Forsyth Barr analysis, COVID tracking, Our World in Data

Figure 4. US COVID-19 hospitalisation rates by age bracket



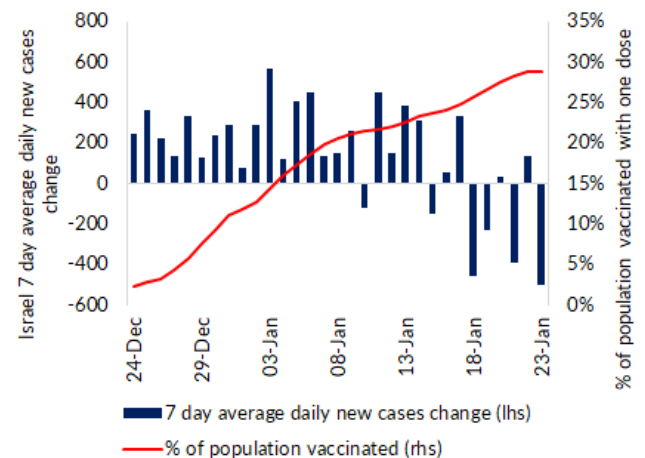
Source: Forsyth Barr analysis, CDC

Figure 5. Europe COVID-19 cases and hospitalisations



Source: Forsyth Barr analysis, Our World in Data

Figure 6. Israel COVID-19 cases vs population vaccinated



Source: Forsyth Barr analysis, Our World in Data

Earnings revisions

Our earnings revisions are summarised below. The key changes are:

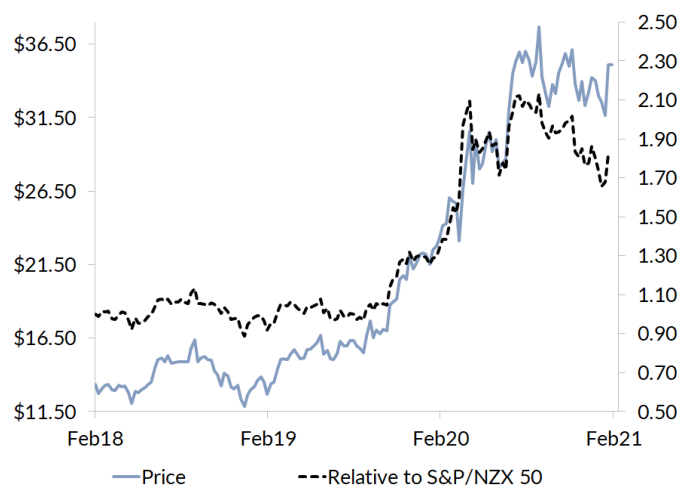
1. **Lifting our COVID-19 hospitalisation assumptions in FY21E and 1H22E** which boosts demand/revenue for FPH's Hospital consumables. We continue to assume the spike in IV consumables is temporary (with a return to 'normal' forecast in FY23E), while assume some durable benefit for Optiflow consumable demand beyond the pandemic given the additional hardware placed and greater awareness.
2. **An increase in short-term Hospital hardware revenue expectations**, to reflect the stronger than anticipated 3Q21. We now assume revenue of NZ\$550m in FY21E (vs NZ\$130m in FY20 and ~NZ\$95m pre COVID). We assume a more modest level of elevated demand in 1H22E, with a return towards 'normal' levels from 2H22E.
3. **A modest lift in dividend payout** – reflecting a larger assumed net cash position following higher COVID-19 tailwinds
4. **Updated FX assumptions**; which has a small negative drag on medium-term earnings.

We lift our target price to NZ\$33.00 (+3%), broadly consistent with our medium-term earnings revisions.

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	1,836.3	2,016.7	9.8%	1,673.5	1,695.8	1.3%	1,846.0	1,816.6	-1.6%
EBIT	379.3	622.7	749.7	20.4%	547.0	580.3	6.1%	614.7	628.0	2.2%
Normalised Profit	287.3	458.4	549.4	19.9%	407.6	431.9	6.0%	458.4	467.5	2.0%
Normalised EPS (cps)	50.0	79.7	95.5	19.9%	70.5	74.7	6.0%	79.0	80.5	2.0%
Dividend per share (cps)	27.5	40.0	48.0	20.0%	45.0	51.0	13.3%	50.0	56.0	12.0%

Source: Forsyth Barr analysis

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%

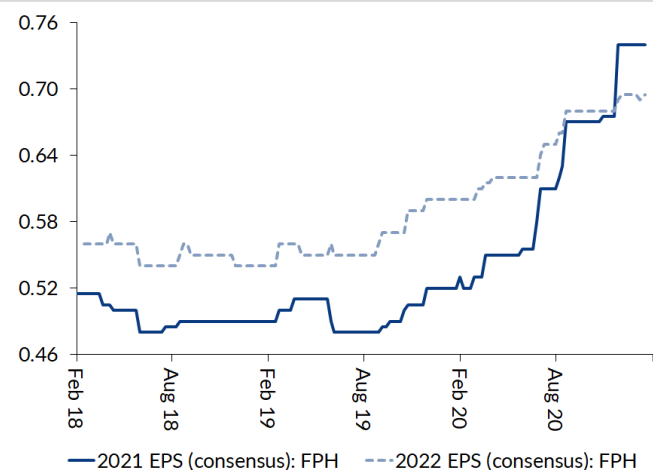
Source: NZX, Forsyth Barr analysis, NOTE: based on SPH notices only

Figure 10. International valuation comparisons

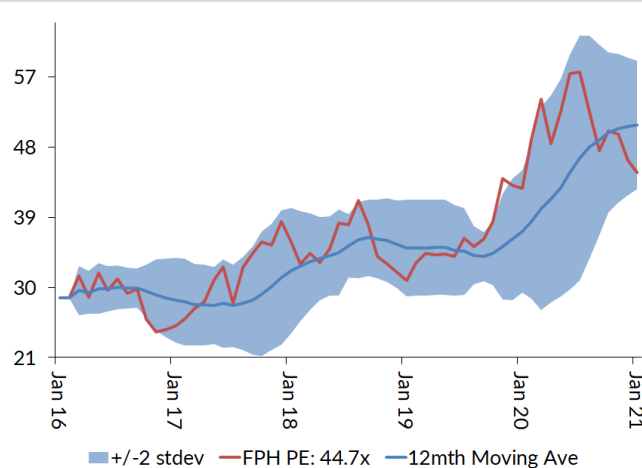
Company	Code	Price	Mkt Cap (m)	PE 2021E 2022E	EV/EBITDA 2021E 2022E	EV/EBIT 2021E 2022E	Cash Yld 2022E
(metrics re-weighted to reflect FPH's balance date - March)							
F&P Healthcare	FPH NZ	NZ\$35.10	NZ\$20,201	36.8x 47.0x	24.6x 30.7x	26.9x 34.7x	1.5%
RESMED INC	RMD US	US\$211.62	US\$30,667	43.6x 40.0x	30.1x 28.2x	35.1x 32.3x	0.8%
TELEFLEX INC	TFX US	US\$388.37	US\$18,085	35.4x 29.5x	27.5x 23.0x	35.1x 28.0x	0.4%
BOSTON SCIENTIFIC CORP	BSX US	US\$36.33	US\$52,022	13.7x 21.7x	22.5x 17.9x	35.8x n/a	n/a
BECTON DICKINSON AND CO	BDX US	US\$261.74	US\$76,127	>50x 20.2x	20.1x 15.4x	40.3x 18.4x	1.5%
Compco Average:				30.9x 27.8x	25.1x 21.1x	36.5x 26.2x	0.9%
FPH Relative:				19% 69%	-2% 46%	-26% 32%	65%

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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