

# Kiwi Property Group

## Downgrade to NEUTRAL

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### NEUTRAL

While Kiwi Property Group (KPG) has already been significantly re-rated down by the market, the near term news flow will remain problematic and there are large uncertainties for the retail outlook, the impact on specialty rents in particular, and rent relief to retain tenants. While KPG has lower than average gearing at around 29%, it also has a lower than average gearing covenant at 45% but still has substantial gearing headroom. Imminent portfolio revaluations for the year ending March will be of high interest. NEUTRAL.

NZX Code	KPG	Financials: Mar/	19A	20E	21E	22E	Valuation (x)	19A	20E	21E	22E
Share price	NZ\$0.88	NPAT* (NZ\$m)	99.9	104.0	112.9	114.3	EV/EBITDA	13.8	13.5	12.5	12.0
Target price	NZ\$1.29	EPS* (NZc)	7.0	7.1	7.2	7.2	EV/EBIT	13.8	13.5	12.5	12.0
Risk rating	Medium	EPS growth* (%)	-6.2	1.6	1.5	0.5	PE	12.5	12.3	12.1	12.1
Issued shares	1432.8m	DPS (NZc)	7.0	7.1	7.1	7.2	Price / NTA	0.6	0.6	0.6	0.6
Market cap	NZ\$1,254m	Imputation (%)	100	100	100	100	Cash div yld (%)	7.9	8.1	8.2	8.3
Avg daily turnover	1,626k (NZ\$2,455k)	*Based on normalised profits					Gross div yld (%)	11.3	11.5	11.7	11.8

### Retail in the eye of the storm

KPG has the largest retail holdings in the LPV sector by a considerable margin. Its last stated position was only 20% pure retail with the balance comprising its new classification of mixed use for its three major shopping centres and its office assets. While specialty leasing can be problematic in a downturn, these are in fairly dominant centres in most cases which will hold up relatively better than weaker centres that have been struggling for some time. The near term risks are rent relief to keep tenants going for when centres fully re-open, rental levels and occupancy over the next 12 months, and what property valuers say near-term.

### Downgraded to NEUTRAL

KPG has been caught in the retail sentiment fallout in recent weeks with a dramatic share price correction. The near term news flow will remain problematic and there are large uncertainties for the retail/consumer outlook. KPG also has one of the highest dividend payout rates in the sector. Having lower than average sector gearing is helpful for KPG with its capital raise late in the cycle. Figure 1 has a summary of sector gearing and Figure 2 highlights the indicative gearing head room. However, it will be difficult for KPG to divest any of its assets should it want to improve liquidity and the retail sector has arguably the most asset value downside in the near term. We remain confident of the longer term positioning of the large mixed use assets and its key office assets but see downside for its other pure retail assets. We have not changed forecasts at present, but have lowered our NAV to NZ\$1.14 and this has dropped our target price to NZ\$1.29.

**Kiwi Property Group Limited (KPG)**

Priced as at 26 Mar 2020 (NZ\$)

**0.88**
**12-month target price (NZ\$)\***
**1.29**

Expected share price return	46.6%
Net dividend yield	8.1%
Estimated 12-month return	54.7%

**Spot valuations (NZ\$)**

1. DCF	1.67
2. NAV	1.14
n/a	n/a

**Key WACC assumptions**

Risk free rate	2.00%
Equity beta	0.67
WACC	5.1%
Terminal growth	1.5%

**DCF valuation summary (NZ\$m)**

Total firm value	3,499
(Net debt)/cash	(992)
Less: Capitalised operating leases	0
Value of equity	2,482

<b>Profit and Loss Account (NZ\$m)</b>	2018A	2019A	2020E	2021E	2022E	<b>Valuation Ratios</b>	2018A	2019A	2020E	2021E	2022E
Sales revenue	191.7	180.8	185.6	197.8	205.2	EV/EBITDA (x)	13.0	13.8	13.5	12.5	12.0
<b>Normalised EBITDA</b>	<b>171.2</b>	<b>160.0</b>	<b>164.7</b>	<b>176.4</b>	<b>183.4</b>	EV/EBIT (x)	13.0	13.8	13.5	12.5	12.0
Depreciation and amortisation	0	0	0	0	0	PE (x)	11.8	12.6	12.4	12.2	12.2
<b>Normalised EBIT</b>	<b>171.2</b>	<b>160.0</b>	<b>164.7</b>	<b>176.4</b>	<b>183.4</b>	Price/NTA (x)	0.6	0.6	0.6	0.6	0.6
Net interest	(42.4)	(37.5)	(36.3)	(35.7)	(38.2)	Free cash flow yield (%)	-0.4	-5.5	-4.6	5.1	7.9
Associate income	0	0	0	0	0	Net dividend yield (%)	7.8	7.9	8.0	8.1	8.2
Tax	(25.4)	(22.6)	(24.4)	(27.8)	(30.8)	Gross dividend yield (%)	11.1	11.3	11.4	11.6	11.8
Minority interests	0	0	0	0	0						
<b>Normalised NPAT</b>	<b>103.4</b>	<b>99.9</b>	<b>104.0</b>	<b>112.9</b>	<b>114.3</b>	<b>Capital Structure</b>	<b>2018A</b>	<b>2019A</b>	<b>2020E</b>	<b>2021E</b>	<b>2022E</b>
Abnormals/other	(16.7)	(38.2)	(46.0)	(46.1)	(48.9)	Interest cover EBIT (x)	4.0	4.3	4.5	4.9	4.8
<b>Reported NPAT</b>	<b>120.1</b>	<b>138.1</b>	<b>150.0</b>	<b>159.0</b>	<b>163.2</b>	Interest cover EBITDA (x)	4.0	4.3	4.5	4.9	4.8
Normalised EPS (cps)	7.5	7.0	7.1	7.2	7.2	Net debt/ND+E (%)	31.2	32.6	29.1	28.9	28.7
DPS (cps)	6.9	7.0	7.1	7.1	7.2	Net debt/EBITDA (x)	5.3	6.2	5.7	5.5	5.3
<b>Growth Rates</b>	<b>2018A</b>	<b>2019A</b>	<b>2020A</b>	<b>2021A</b>	<b>2022A</b>	<b>Key Ratios</b>	<b>2018A</b>	<b>2019A</b>	<b>2020E</b>	<b>2021E</b>	<b>2022E</b>
Revenue (%)	5.4	-5.7	2.6	6.6	3.7	Return on assets (%)	5.6	4.9	4.8	5.0	5.1
EBITDA (%)	4.4	-6.5	3.0	7.1	4.0	Return on equity (%)	5.2	4.9	4.5	4.7	4.7
EBIT (%)	4.4	-6.5	3.0	7.1	4.0	Return on funds employed (%)	4.7	4.3	4.1	4.2	4.2
Normalised NPAT (%)	7.6	-3.4	4.2	8.5	1.2	EBITDA margin (%)	89.3	88.5	88.7	89.2	89.4
Normalised EPS (%)	0.4	-6.2	1.6	1.5	0.5	EBIT margin (%)	89.3	88.5	88.7	89.2	89.4
Ordinary DPS (%)	1.9	1.5	1.4	1.4	1.4	Capex to sales (%)	58.7	93.9	88.7	27.0	8.4
						Capex to depreciation (%)	n/a	n/a	n/a	n/a	n/a
<b>Cash Flow (NZ\$m)</b>	<b>2018A</b>	<b>2019A</b>	<b>2020E</b>	<b>2021E</b>	<b>2022E</b>	Imputation (%)	100	100	100	100	100
<b>EBITDA</b>	<b>171.2</b>	<b>160.0</b>	<b>164.7</b>	<b>176.4</b>	<b>183.4</b>	Pay-out ratio (%)	92	99	99	99	100
Working capital change	2.1	3.4	3.0	4.7	3.1						
Interest & tax paid	(65.1)	(63.4)	(60.7)	(63.5)	(69.1)	<b>Property Statistics</b>	<b>2015A</b>	<b>2016A</b>	<b>2017A</b>	<b>2018A</b>	<b>2019A</b>
Other	0	0	0	0	0	<b>Retail portfolio</b>					
<b>Operating cash flow</b>	<b>108.2</b>	<b>100.0</b>	<b>107.0</b>	<b>117.6</b>	<b>117.4</b>	No. properties	7	9	9	4	4
Capital expenditure	(112.6)	(169.8)	(164.6)	(53.3)	(17.3)	WALT (years)	3.4	3.9	3.8	3.6	3.3
(Acquisitions)/divestments	62.3	67.3	0	0	0	Occupancy rate (%)	99.3%	99.1%	99.1%	99.4%	99.4%
Other	(6.4)	(2.6)	0	0	0	Cap rate (%)	6.97%	6.69%	6.52%	6.25%	7.53%
<b>Funding available/(required)</b>	<b>51.4</b>	<b>(5.1)</b>	<b>(57.7)</b>	<b>64.2</b>	<b>100.1</b>	<b>Office portfolio</b>					
Dividends paid	(88.5)	(81.5)	(76.9)	(83.4)	(113.6)	No. properties	5	5	5	4	4
Equity raised/(returned)	157.0	0	180.0	0	0	WALT (years)	7.6	8.2	10.1	10.1	9.3
<b>(Increase)/decrease in net debt</b>	<b>119.9</b>	<b>(86.6)</b>	<b>45.5</b>	<b>(19.2)</b>	<b>(13.5)</b>	Occupancy rate (%)	96.1%	97.4%	97.8%	99.3%	98.7%
						Cap rate (%)	6.80%	6.44%	6.13%	5.76%	5.45%
<b>Balance Sheet (NZ\$m)</b>	<b>2018A</b>	<b>2019A</b>	<b>2020E</b>	<b>2021E</b>	<b>2022E</b>	<b>Mixed-use portfolio</b>					
Working capital	(43.2)	(47.1)	(48.4)	(51.6)	(53.5)	No. properties				4	4
Fixed assets	3,052.0	3,207.4	3,416.3	3,514.3	3,579.3	WALT (years)				4.0	4.1
Intangibles	0	0	0	0	0	Occupancy rate (%)				100.0%	99.5%
Right of use asset	0	0	0	0	0	Cap rate (%)				5.72%	5.71%
Other assets	4.4	5.9	5.9	5.9	5.9	<b>Total portfolio</b>					
<b>Total funds employed</b>	<b>3,013.2</b>	<b>3,166.2</b>	<b>3,373.9</b>	<b>3,468.6</b>	<b>3,531.8</b>	WALT (years)	4.5	5.1	5.6	5.3	5.2
Net debt/(cash)	902.8	991.8	946.3	965.4	978.9	Occupancy rate (%)	98.4%	98.7%	98.8%	99.6%	99.3%
Lease liability	0	0	0	0	0	Cap rate (%)	6.92%	6.61%	6.40%	6.11%	5.99%
Other liabilities	116.3	123.5	123.5	123.5	123.5	NTA per share (NZ\$)	1.214	1.345	1.390	1.392	1.431
Shareholder's funds	1,994.1	2,050.9	2,304.0	2,379.7	2,429.3						
Minority interests	0	0	0	0	0						
<b>Total funding sources</b>	<b>3,013.2</b>	<b>3,166.2</b>	<b>3,373.9</b>	<b>3,468.6</b>	<b>3,531.8</b>						

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

## Key tables and charts

**Figure 1. Balance Sheet summary**

	As at	Reported gearing	Target gearing	Bank covenant	Bank facilities (NZ\$m)	Issued Bonds (NZ\$m)	Facility capacity (NZ\$m)	Term - bank (years)	Term - bonds (years)	Term - weighted (years)
APL	Mar-20	30.2%	35-40%	50%	75	-	27	2.2	-	2.2
ARG	Sep-19	36.2%	30-40%	50%	535	200	85	2.7	6.3	3.7
GMT	Sep-19	17.9%	25-35%	50%	400	556	400	2.6	4.6	3.8
IPL	Sep-19	40.6%	<48%	65%	270	100	65	1.5	4.1	2.2
KPG	Sep-19	27.4%	25-35%	45%	825	475	303	3.5	3.7	3.6
PCT	Dec-19	25.4%	<37.5%	50%	610	586	322	3.3	5.1	4.2
PFI	Dec-19	28.2%	<40%	50%	300	200	84	3.1	5.1	3.9
SPG	Sep-19	34.4%	38-42%	50%	400	-	67	1.8	-	1.8
VHP	Dec-19	35.1%	na	50%	870	-	225	2.0	-	2.0
<b>Average/total</b>		<b>30.6%</b>		<b>51.1%</b>	<b>4,285</b>	<b>2,117</b>	<b>1,479</b>	<b>2.5</b>	<b>3.2</b>	<b>3.0</b>

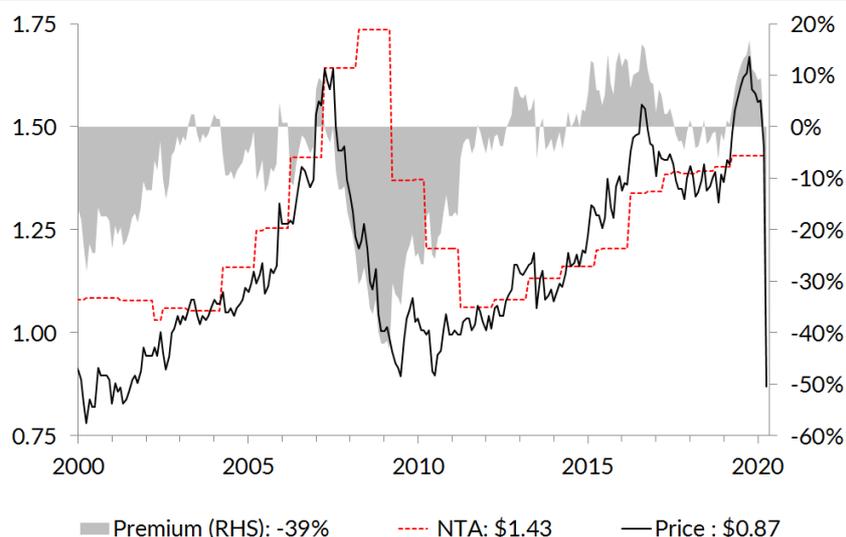
Source: Forsyth Barr analysis, company reports

**Figure 2. Hypothetical asset value declines required to breach banking covenant**

	Reported Gearing	Bank Covenant	Approx Debt Drawn	Approx Asset Value	Minimum Asset Value	Asset Value Decline
APL	30.2%	50%	50.0	160.0	100.0	-40%
ARG	36.2%	50%	650.0	1,790.0	1,300.0	-28%
GMT	17.9%	50%	530.0	2,960.0	1,060.0	-64%
IPL	40.6%	65%	300.0	750.0	470.0	-38%
KPG	27.4%	45%	930.0	3,400.0	2,070.0	-39%
PCT	25.4%	50%	870.0	3,440.0	1,750.0	-49%
PFI	28.2%	50%	430.0	1,520.0	860.0	-44%
SPG	34.4%	50%	300.0	880.0	610.0	-31%
VHP	35.1%	50%	680.0	1,940.0	1,360.0	-30%

Source: Forsyth Barr analysis, Company reports

**Figure 3. KPG long-run price/NTA**



Source: Forsyth Barr analysis

**Figure 4. LPV compco table**

LPV	Code	Rating	Price 26-Mar	Target price	Gross yield	AFFO yield	P/NAV	P/NTA
Asset Plus	APL	UNDERPERFORM	\$0.42	\$0.65	12.4%	7.6%	63%	58%
Argosy Property	ARG	NEUTRAL	\$0.86	\$1.38	10.4%	7.2%	65%	67%
Augusta Capital	AUG	NEUTRAL	\$0.98	\$1.38	9.3%	7.3%	70%	132%
Goodman Property	GMT	NEUTRAL	\$2.19	\$1.92	4.3%	2.9%	115%	127%
Investore	IPL	OUTPERFORM	\$1.50	\$1.85	7.3%	5.0%	90%	88%
Kiwi Property Group	KPG	NEUTRAL	\$0.87	\$1.29	11.7%	7.5%	76%	61%
Precinct Properties	PCT	NEUTRAL	\$1.66	\$1.52	5.4%	3.6%	103%	113%
Property for Industry	PFI	OUTPERFORM	\$2.06	\$2.15	5.4%	3.7%	100%	104%
Stride Property	SPG	NEUTRAL	\$1.35	\$2.18	10.5%	7.0%	66%	69%
Vital Healthcare	VHP	OUTPERFORM	\$2.36	\$2.76	5.5%	3.8%	100%	102%
<b>Core simple average</b>					<b>7.6%</b>	<b>5.1%</b>	<b>90%</b>	<b>91%</b>

Source: Forsyth Barr analysis

## Investment Summary

Kiwi Property Group (KPG) is the largest listed property vehicle in the NZ market. Its diversified asset base of NZ\$3.1bn comprises of 68% retail assets and 32% office assets. Recent sales of non-core assets have improved portfolio quality and made KPG more defensive to softening property market fundamentals. KPG is not immune to the structural headwinds for retail property, with e-commerce growth impacting and now a sharply softer economic outlook. NEUTRAL.

### Business quality

- **Property fundamentals strong, reflecting strength of assets:** Portfolio metrics remain strong with WALT and occupancy at 5.1 years and 99.4% respectively. The office portfolio has an impressive WALT of 9.1 years.

### Earnings and cashflow outlook

- **Rental growth:** KPG achieved solid +4.6% 1H20 rental growth driven by strong rent reviews and new leases in the Office and Mixed-use portfolio.
- **Sylvia Park Galleria expansion:** KPG has committed to an NZ\$223m expansion of Sylvia Park with an additional 18,000sqm of retail space, a new cafe court, and 900 additional car parks. KPG has also announced an additional NZ\$35m for design enhancements and additional space to accommodate key retailers. The total cost of the project is NZ\$258m with a development margin of ~NZ \$30m.

### Risk factors

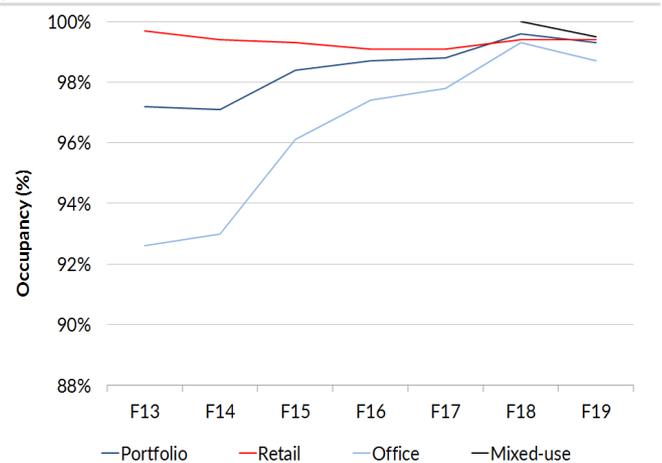
- **Retail exposure:** Competitive pressures from e-commerce growth coupled with the significant amount of Auckland retail development coming online at Commercial Bay and Westfield, Newmarket, are likely to impact KPG's Auckland based malls.
- **CBD office asset volatility:** Rental growth expectations have improved recently with tight supply but remain volatile through the cycle.
- **Rising interest rates:** Higher interest rates make other yield investments more attractive relative to listed property dividend yields.

Figure 5. Sector and regional portfolio exposure

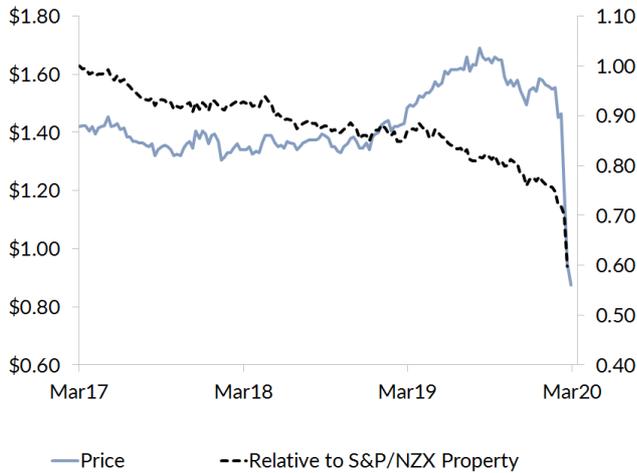
	Auckland	Other North Island	South Island	Total
Industrial	-	-	-	-
Office	22%	7%	-	30%
Retail	45%	17%	9%	70%
<b>Total</b>	<b>68%</b>	<b>24%</b>	<b>9%</b>	<b>100%</b>

Source: Forsyth Barr analysis, Company Reports

Figure 6. Occupancy by sector



Source: Forsyth Barr analysis, Company Reports

**Figure 7. Price performance**


Source: Forsyth Barr analysis

**Figure 8. Substantial shareholders**

Shareholder	Latest Holding
ACC	9.2%
ANZ NZ Investments	8.3%
Salt Funds Management	5.1%
The Vanguard Group	5.1%

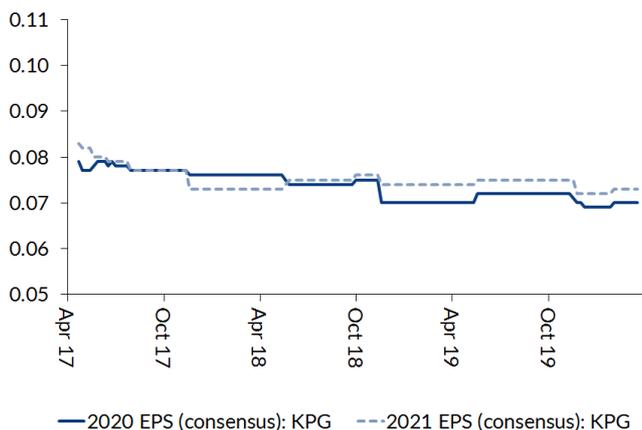
Source: NZX, Forsyth Barr analysis, NOTE: based on SSH notices only

**Figure 9. International valuation comparisons**

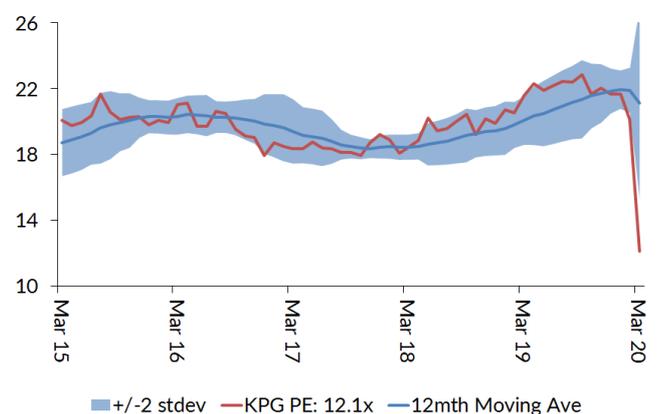
Company	Code	Price	Mkt Cap (m)	PE		EV/EBITDA		EV/EBIT		Cash Yld 2021E
				2020E	2021E	2020E	2021E	2020E	2021E	
<b>Kiwi Property Group</b>	<b>KPG NZ</b>	<b>NZ\$0.88</b>	<b>NZ\$1,254</b>	<b>12.3x</b>	<b>12.1x</b>	<b>13.6x</b>	<b>12.7x</b>	<b>13.6x</b>	<b>12.7x</b>	<b>8.2%</b>
Argosy Property *	ARG NZ	NZ\$0.84	NZ\$695	12.7x	12.2x	14.4x	13.5x	14.4x	13.5x	7.5%
Goodman Property Trust *	GMT NZ	NZ\$2.05	NZ\$2,841	30.4x	29.8x	26.8x	24.4x	26.8x	24.4x	3.2%
Investore *	IPL NZ	NZ\$1.41	NZ\$429	17.4x	17.1x	18.3x	18.1x	18.3x	18.1x	5.4%
Asset Plus *	APL NZ	NZ\$0.42	NZ\$68	10.9x	11.6x	8.4x	9.1x	8.4x	9.1x	8.6%
Precinct Properties NZ *	PCT NZ	NZ\$1.47	NZ\$1,931	22.6x	21.6x	24.4x	20.2x	24.4x	20.2x	4.3%
Property For Industry *	PFI NZ	NZ\$1.76	NZ\$878	20.5x	20.1x	17.3x	17.2x	17.3x	17.2x	4.4%
Stride Property *	SPG NZ	NZ\$1.30	NZ\$475	12.4x	11.7x	14.2x	13.0x	14.2x	13.0x	7.6%
Vital Healthcare *	VHP NZ	NZ\$2.05	NZ\$928	21.1x	20.1x	20.0x	18.9x	20.0x	18.9x	4.4%
<b>Compcpo Average:</b>				<b>18.5x</b>	<b>18.0x</b>	<b>18.0x</b>	<b>16.8x</b>	<b>18.0x</b>	<b>16.8x</b>	<b>5.7%</b>
<b>KPG Relative:</b>				<b>-33%</b>	<b>-33%</b>	<b>-24%</b>	<b>-24%</b>	<b>-24%</b>	<b>-24%</b>	<b>44%</b>

EV = Current Market Cap + Actual Net Debt

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

**Figure 10. Consensus EPS momentum (NZ\$)**


Source: Forsyth Barr analysis

**Figure 11. One year forward PE (x)**


Source: Forsyth Barr analysis

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