

# Oceania Healthcare

## Good Acquisition, But Why the Extra Money?

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### OUTPERFORM

Oceania Healthcare (OCA) has undertaken an NZ\$100m equity raise at a fixed offer price of NZ\$1.30 (representing a 6.5% discount to the last close price of NZ\$1.39) to fund the purchase of two new sites in Auckland. (1) NZ\$60m for Waterford on Hobsonville Point – a 100 unit (64 villas and 36 apartments) village with two development zones to add ~60 units/care suites, and (2) NZ\$17m for a new Franklin site that currently has 2 hectares of leased land and 4.1 hectares of additional land, the land adjacent to the site offers a further ~215 units and care suites to OCA's development pipeline. The total acquisition price of NZ\$77m leaves an additional ~NZ\$20m to help support further growth opportunities.

NZX Code	OCA	Financials: Mar/	20A	21E	22E	23E	Valuation (x)	20A	21E	22E	23E
Share price	NZ\$1.39	NPAT* (NZ\$m)	42.5	48.5	67.2	74.1	PE	20.1	18.7	14.4	13.2
Target price	NZ\$1.70	EPS* (NZc)	6.9	7.4	9.7	10.5	EV/EBIT	23.5	20.9	14.8	13.5
Risk rating	Medium	EPS growth* (%)	-15.8	7.4	30.2	9.0	EV/EBITDA	18.1	16.8	12.1	11.0
Issued shares	618.1m	DPS (NZc)	3.5	3.5	4.5	5.0	Price / NTA	1.6	1.5	1.4	1.3
Market cap	NZ\$859m	Imputation (%)	0	0	0	0	Cash div yld (%)	2.5	2.5	3.2	3.6
Avg daily turnover	1,278k (NZ\$1,272k)	*Based on normalised profits					Gross div yld (%)	2.5	2.5	3.2	3.6

### What's changed?

- **Earnings:** Near-term increases in earnings reflecting the incorporation of the Waterford village. On an EPS basis we leave our FY22E estimates essentially unchanged but reduce our FY23E EPS slightly.

### What are the balance sheet and earnings impacts?

- **Balance sheet:** The acquisitions in totality are expected to deliver low to mid-single digit NTA accretion per share with the acquisition price for the Hobsonville site (c. NZ\$60m) ~3% below CBRE's valuation, as at 31 March 2020, the main driver of the uplift. The equity raise and acquisitions will result in pro-forma gearing of ~28% down from 32.3% at 1H21.
- **Earnings:** Near-term, OCA expects the Hobsonville Point acquisition to result in low to mid-single digit underlying earnings per share accretion in FY22. We understand that this is based off of the NZ\$60m for the Waterford village. All else equal, we estimate that total EPS accretion including the additional NZ\$40m raised will be at or around zero percent. We assume an NZ\$3-4m annuity EBITDA contribution.

### Waterford village transacted at ~20x annuity EV/EBITDA multiple; a relatively attractive price

At face value, we view the Waterford village as an attractive transaction for OCA and estimate it will contribute ~NZ\$3-4m per annum in annuity EBITDA, predominately arising from increased deferred management fees (DMF) albeit we expect resale gains to become a bigger part of the picture as the village matures (we understand there was only 1 resale in FY20). An ~NZ\$3-4m annuity EBITDA contribution implies a ~20x EV/annuity EBITDA multiple which is relatively attractive in our view and below where the market is currently valuing the aged care stocks.

### Raising equity to buy land and accelerate development raises a few questions

In addition to the c. NZ\$60m raised for the acquisition of the Waterford village, OCA raised an additional c. NZ\$40m to buy a new land site (for NZ\$17m) and to provide "capacity to consider future growth opportunities". Future plans are light on detail but we did not consider OCA over levered prior to the equity raise and expect more details on its accelerated development pipeline at its FY21 result in May.

## Oceania Healthcare Limited (OCA)

Priced as at 23 Mar 2021 (NZ\$)

1.39

### 12-month target price (NZ\$)\*

1.70

Expected share price return

22.3%

Net dividend yield

3.2%

Estimated 12-month return

25.5%

### Spot valuations (NZ\$)

1. EV/Annuity EBITDA

1.80

2. DDM

1.60

3. n/a

n/a

### Key WACC assumptions

Risk free rate

2.30%

Equity beta

0.88

WACC

6.7%

Terminal growth

1.5%

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

Total firm value

n/a

(Net debt)/cash

n/a

Less: Capitalised operating leases

n/a

Value of equity

n/a

Profit and Loss Account (NZ\$m)	2019A	2020A	2021E	2022E	2023E	Valuation Ratios	2019A	2020A	2021E	2022E	2023E
Sales revenue	233.5	241.7	226.5	292.2	310.0	EV/EBITDA (x)	16.8	18.1	16.8	12.1	11.0
<b>Normalised EBITDA</b>	<b>63.1</b>	<b>63.1</b>	<b>68.4</b>	<b>92.3</b>	<b>101.4</b>	EV/EBIT (x)	19.7	23.5	20.9	14.8	13.5
Depreciation and amortisation	(9.5)	(14.5)	(13.5)	(17.0)	(18.9)	PE (x)	16.9	20.1	18.7	14.4	13.2
<b>Normalised EBIT</b>	<b>53.6</b>	<b>48.6</b>	<b>55.0</b>	<b>75.3</b>	<b>82.5</b>	Price/NTA (x)	1.4	1.6	1.5	1.4	1.3
Net interest	(3.5)	(6.2)	(6.5)	(8.1)	(8.4)	Free cash flow yield (%)	28.9	27.4	31.3	38.2	40.4
Associate income	0	0	0	0	0	Net dividend yield (%)	3.4	2.5	2.5	3.2	3.6
Tax	0	0	0	0	0	Gross dividend yield (%)	3.4	2.5	2.5	3.2	3.6
Minority interests	0	0	0	0	0						
<b>Normalised NPAT</b>	<b>50.1</b>	<b>42.5</b>	<b>48.5</b>	<b>67.2</b>	<b>74.1</b>	<b>Capital Structure</b>	<b>2019A</b>	<b>2020A</b>	<b>2021E</b>	<b>2022E</b>	<b>2023E</b>
Abnormals/other	(4.7)	(56.1)	(0.7)	(6.9)	(9.7)	Interest cover EBIT (x)	15.3	7.9	8.5	9.3	9.8
<b>Reported NPAT</b>	<b>45.4</b>	<b>(13.6)</b>	<b>47.7</b>	<b>60.3</b>	<b>64.4</b>	Interest cover EBITDA (x)	18.1	10.2	10.6	11.4	12.1
Normalised EPS (cps)	8.2	6.9	7.4	9.7	10.5	Net debt/ND+E (%)	28.9	35.7	27.0	29.6	29.3
DPS (cps)	4.7	3.5	3.5	4.5	5.0	Net debt/EBITDA (x)	3.9	4.9	3.5	3.2	3.0
Growth Rates	2019A	2020A	2021E	2022E	2023E	Key Ratios	2019A	2020A	2021E	2022E	2023E
Revenue (%)	5.2	3.5	-6.3	29.0	6.1	Return on assets (%)	3.8	3.2	3.1	3.8	3.8
EBITDA (%)	-0.9	-0.1	8.5	34.8	9.9	Return on equity (%)	8.2	7.7	7.4	9.5	10.1
EBIT (%)	-2.4	-9.3	13.0	37.0	9.6	Return on funds employed (%)	5.7	4.8	4.8	6.4	6.8
Normalised NPAT (%)	-3.9	-15.2	14.2	38.7	10.3	EBITDA margin (%)	27.0	26.1	30.2	31.6	32.7
Normalised EPS (%)	-3.9	-15.8	7.4	30.2	9.0	EBIT margin (%)	23.0	20.1	24.3	25.8	26.6
Ordinary DPS (%)	0.0	-25.5	0.0	28.6	11.1	Capex to sales (%)	65.9	56.3	57.4	53.0	51.6
						Capex to depreciation (%)	1,611	941	965	914	847
						Imputation (%)	0	0	0	0	0
						Pay-out ratio (%)	57	51	47	47	47
Cash Flow (NZ\$m)	2019A	2020A	2021E	2022E	2023E	Operating Performance	2019A	2020A	2021E	2022E	2023E
<b>EBITDA</b>	<b>63.1</b>	<b>63.1</b>	<b>68.4</b>	<b>92.3</b>	<b>101.4</b>	<b>Revenue (NZ\$m)*</b>					
Working capital change	(1.8)	10.4	(8.5)	1.5	1.7	Care fees	156.6	156.4	136.8	173.2	177.8
Interest & tax paid	(3.5)	(6.2)	(6.5)	(8.1)	(8.4)	Management fees	22.3	29.2	31.5	50.1	59.8
Other	37.0	32.1	85.6	87.3	92.5	Other	10.4	10.6	9.0	12.0	12.6
<b>Operating cash flow</b>	<b>94.8</b>	<b>99.4</b>	<b>139.0</b>	<b>173.0</b>	<b>187.2</b>	Gain on resales	15.1	11.5	19.2	23.9	28.1
Capital expenditure	(153.8)	(136.0)	(130.0)	(155.0)	(160.0)	Gain on new sales	29.1	33.9	30.1	33.0	31.6
(Acquisitions)/divestments	0	0	0	0	0	<b>Total revenue</b>	<b>233.5</b>	<b>241.7</b>	<b>226.5</b>	<b>292.2</b>	<b>310.0</b>
Other	0.0	(3.2)	0	(60.0)	0						
<b>Funding available/(required)</b>	<b>(59.0)</b>	<b>(39.8)</b>	<b>9.0</b>	<b>(42.0)</b>	<b>27.2</b>	<b>Key Drivers</b>					
Dividends paid	(28.4)	(22.2)	(24.1)	(31.6)	(35.1)	Sales - new units	133	189	255	274	270
Equity raised/(returned)	1.3	0	80.0	20.0	0	Sales - resold units	177	166	241	290	356
<b>(Increase)/decrease in net debt</b>	<b>(86.1)</b>	<b>(62.0)</b>	<b>65.0</b>	<b>(53.6)</b>	<b>(8.0)</b>	Gross development margin	36%	33%	26%	21%	21%
						Gross resales margin	25%	20%	20%	20%	19%
						Average new sales price (NZ\$000)	609	542	454	574	571
						Average resales price (NZ\$000)	348	354	397	404	416
Balance Sheet (NZ\$m)	2019A	2020A	2021E	2022E	2023E	Portfolio Overview					
Working capital	5.0	6.8	(3.6)	5.0	3.4	ILU's	1,202	1,285	1,370	1,605	1,745
Fixed assets	1,324.4	1,437.8	1,599.3	1,847.4	2,038.5	Care Suites (ORA)	326	440	580	700	830
Intangibles	8.7	10.8	10.8	10.8	10.8	Care Suites (PAC)	216	239	266	256	250
Right of use asset	0	0	0	0	0	Care Beds	2,112	1,882	1,832	1,732	1,632
Other assets	0	0	0	0	0	<b>Total</b>	<b>3,856</b>	<b>3,846</b>	<b>4,048</b>	<b>4,293</b>	<b>4,457</b>
<b>Total funds employed</b>	<b>1,338.0</b>	<b>1,455.4</b>	<b>1,606.6</b>	<b>1,863.2</b>	<b>2,052.8</b>						
Net debt/(cash)	247.4	307.8	242.9	296.5	304.4						
Lease liability	0	13.0	13.0	13.0	13.0						
Other liabilities	480.8	580.2	692.7	846.9	999.3						
Shareholder's funds	609.9	554.4	658.1	706.8	736.0						
Minority interests	0	0	0	0	0						
<b>Total funding sources</b>	<b>1,338.0</b>	<b>1,455.4</b>	<b>1,606.6</b>	<b>1,863.2</b>	<b>2,052.8</b>						

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

## Earnings changes

We lift our near-term earnings estimates as we integrate the benefits of the Waterford village, primarily reflected in increased new sales gains and DMF. We remove our FY21E estimates from the below table which are no longer prepared on a like for like basis as we incorporate the impact of OCA's change in balance date from 31 May to 31 March, however, we have made no underlying changes to our FY21E estimates.

**Figure 1. Forecast earnings changes (NZ\$m)**

	FY22E			FY23E		
	Old	New	Change	Old	New	Change
Care fees	173.2	173.2	0.0%	177.8	177.8	0.0%
DMF	47.2	50.1	6.2%	56.5	59.8	5.8%
Village fees	10.4	11.0	5.4%	11.0	11.6	5.4%
Resale gains	23.4	23.9	2.3%	26.9	28.1	4.4%
Newsale gains	30.1	33.0	9.6%	30.8	31.6	2.5%
Other	1.0	1.0	0.0%	1.0	1.0	0.0%
<b>Total revenue</b>	<b>285.3</b>	<b>292.2</b>	<b>2.4%</b>	<b>304.2</b>	<b>310.0</b>	<b>1.9%</b>
Total costs	199.2	200.0	0.4%	207.7	208.6	0.4%
<b>EBITDA</b>	<b>86.2</b>	<b>92.3</b>	<b>7.1%</b>	<b>96.5</b>	<b>101.4</b>	<b>5.1%</b>
Depreciation & amortisation	17.0	17.0	0.0%	18.2	18.9	3.5%
<b>EBIT</b>	<b>69.2</b>	<b>75.3</b>	<b>8.8%</b>	<b>78.2</b>	<b>82.5</b>	<b>5.5%</b>
Net interest	8.1	8.1	0.0%	8.4	8.4	0.0%
<b>Underlying profit</b>	<b>61.1</b>	<b>67.2</b>	<b>10.0%</b>	<b>69.8</b>	<b>74.1</b>	<b>6.2%</b>
 <b>Annuity EBITDA</b>	 <b>56.0</b>	 <b>59.2</b>	 <b>5.7%</b>	 <b>65.6</b>	 <b>69.8</b>	 <b>6.4%</b>
 EPS (cps)	 9.8	 9.6	 -2.0%	 11.1	 10.5	 -5.4%
DPS (cps)	4.5	4.5	0.0%	5.0	5.0	0.0%

Source: Forsyth Barr analysis

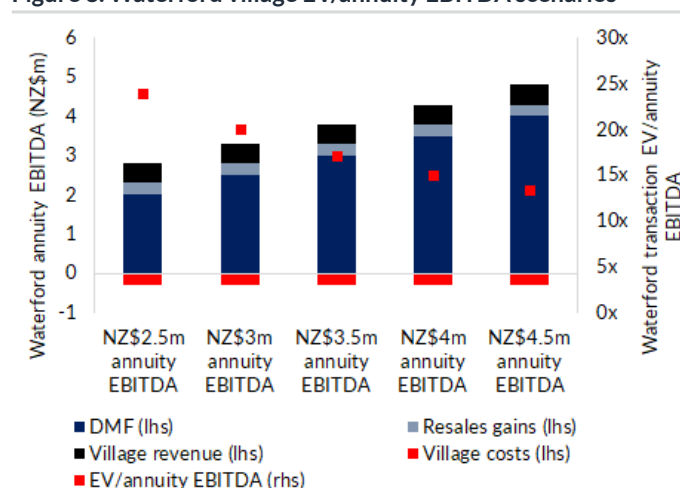
## Figures of interest

**Figure 2. Waterford village potential DMF uplift estimate**

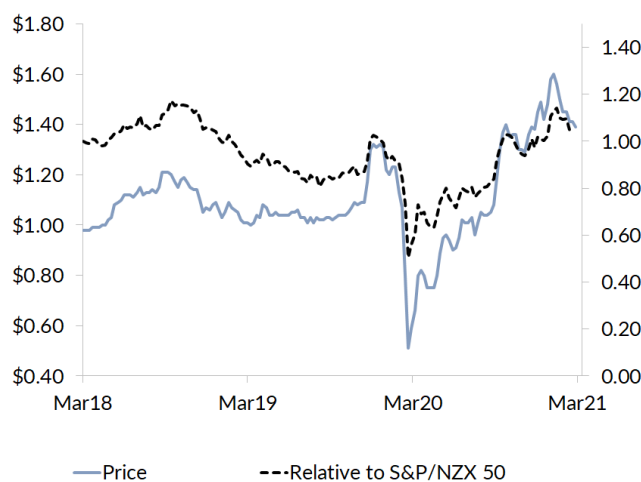
	Villas sold to date	Apartments sold to date	Apartments to be sold
Units sold	64	12	24
Unit price est (000's)	600	1,400	1,400
<b>Total value est (NZ\$m)</b>	<b>38.4</b>	<b>16.8</b>	<b>33.6</b>
DMF %	25%	25%	30%
<b>Total DMF est (NZ\$m)</b>	<b>9.6</b>	<b>4.2</b>	<b>10.1</b>
DMF tenure	7	5	5
<b>Annual DMF est (NZ\$m)</b>	<b>1.4</b>	<b>0.8</b>	<b>2.0</b>

Source: Forsyth Barr analysis, Company reports

**Figure 3. Waterford village EV/annuity EBITDA scenarios**



Source: Forsyth Barr analysis,

**Figure 4. Price performance**


Source: Forsyth Barr analysis

**Figure 5. Substantial shareholders**

Shareholder	Latest Holding
ANZ NZ Investments	7.4%
Harbour Asset Management & Jarden Securities Limited	5.3%
ACC	5.1%

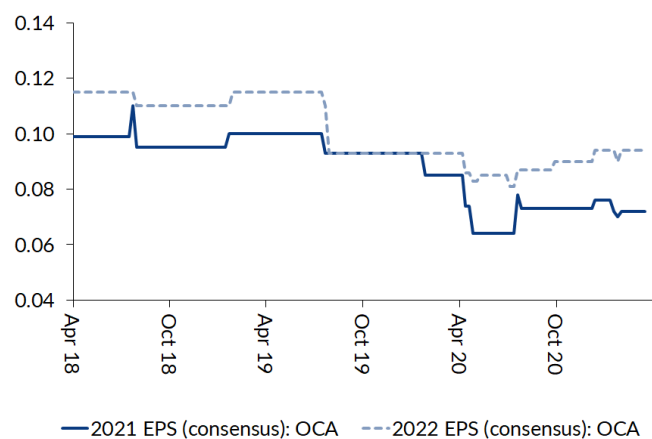
Source: NZX, Forsyth Barr analysis, NOTE: based on SPH notices only

**Figure 6. International valuation comparisons**

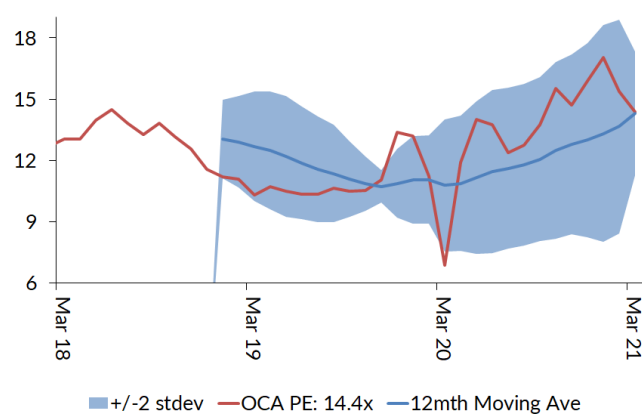
Company	Code	Price	Mkt Cap (m)	PE 2021E	PE 2022E	EV/EBITDA 2021E	EV/EBITDA 2022E	EV/EBIT 2021E	EV/EBIT 2022E	Cash Yld 2022E
(metrics re-weighted to reflect OCA's balance date - March)										
Oceania Healthcare	OCA NZ	NZ\$1.39	NZ\$859	18.7x	14.4x	17.1x	12.6x	21.2x	15.5x	3.2%
RYMAN HEALTHCARE *	RYM NZ	NZ\$15.69	NZ\$7,845	32.7x	25.8x	32.5x	26.0x	36.6x	29.0x	1.9%
SUMMERSET GROUP LIMITED *	SUM NZ	NZ\$12.74	NZ\$2,923	27.1x	20.4x	27.3x	20.7x	29.2x	22.0x	1.5%
ARVIDA GROUP LIMITED *	ARV NZ	NZ\$1.73	NZ\$939	18.3x	14.1x	19.1x	15.4x	21.5x	17.2x	4.0%
Compco Average:				26.0x	20.1x	26.3x	20.7x	29.1x	22.7x	2.5%
OCA Relative:				-28%	-29%	-35%	-39%	-27%	-32%	30%

EV = Current Market Cap + Actual Net Debt

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

**Figure 7. Consensus EPS momentum (NZ\$)**


Source: Forsyth Barr analysis

**Figure 8. One year forward PE (x)**


Source: Forsyth Barr analysis

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