

Property For Industry

FY20 Result — Sheds at Capacity

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UNDERPERFORM

Property For Industry (PFI) reported a solid result slightly above our expectations. However, PFI is now one of the most expensive LPVs in the market. While we are attracted to the defensive nature of industrial property and consistent strategic execution by management, we believe this is more than priced in given its current 30% premium to NTA and one of the slimmest gross yields in the sector, reflecting its tightest spread to bonds on record. We believe this leaves little room for relative upside vs. the sector and downgrade our rating to UNDERPERFORM.

NZX Code	PFI	Financials: Dec/	20A	21E	22E	23E	Valuation (x)	20A	21E	22E	23E
Share price	NZ\$2.87	NPAT* (NZ\$m)	45.5	46.0	45.4	46.4	PE	31.5	31.3	31.7	31.0
Target price	NZ\$2.70	EPS* (NZc)	9.1	9.2	9.1	9.2	EV/EBIT	25.6	25.7	27.1	26.5
Risk rating	Low	EPS growth* (%)	6.8	0.7	-1.2	2.1	EV/EBITDA	25.6	25.7	27.1	26.5
Issued shares	501.3m	DPS (NZc)	7.7	8.0	8.0	8.1	Price / NTA	1.3	1.3	1.3	1.2
Market cap	NZ\$1,439m	Imputation (%)	100	100	100	100	Cash div yld (%)	2.7	2.8	2.8	2.8
Avg daily turnover	257.2k (NZ\$647k)	*Based on normalised profits					Gross div yld (%)	3.8	4.0	4.0	4.0

What's changed?

- **Earnings:** AFFO +1.8%/-0.4%/-4.6% in FY21/FY22/FY23 reflecting the sale of Carlaw Park and increased interest costs
- **Target price:** Down -3cps to NZ\$2.70
- **Rating:** Downgraded to UNDERPERFORM from NEUTRAL

Industrial consistency

PFI delivered another solid result, in line with our expectations. AFFO was slightly ahead of forecasts, boosted by lower than expected tax and interest expenses. Corporate costs increased by 14% in the period as PFI hired additional staff to manage increasing compliance requirements and ESG ambitions. Maintenance capex fell -34% in the period due to COVID-19 related stoppages, although this was offset by increased tenant incentives due to activity at Carlaw Park prior to its sale. Portfolio fundamentals remain strong with 99.4% occupancy, WALT of 5.3 years, and pro-forma gearing of 30% sits comfortably below its 35% target. PFI guided to FY21 DPS of 7.85–7.90cps based on 95–100% payout of AFFO.

Transition nearing completion

Following the divestment of Carlaw Park, with settlement expected in December 2021, PFI will be 98% weighted to industrial property and have pro-forma gearing of 26.5%. PFI is nearing completion on its strategic initiative to become a pure-play industrial LPV, with an increased weighting in Auckland. We expect near-term portfolio activity to be driven by acquisitions rather than redevelopments, given its fully leased portfolio has limited near-term opportunities for larger scale redevelopments. Deploying NZ\$100m would lift gearing into the low 30%'s.

Valuation

We make changes to our risk free rate (from 1.3% to 2.3%) and market risk premium (from 6.0% to 5.5%), consistent with our strategy report, Still a One Way Bet? — Updated WACC Assumptions, published 12 February 2021. The net impact of this is a +47bp increase in our WACC which, along with our earnings changes, lowers our DCF by c.5%. This impact is broadly offset by a 5% lift in our NAV driven by higher property values.

Property for Industry Ltd (PFI)

Prised as at 22 Feb 2021 (NZ\$) **2.87**

12-month target price (NZ\$)*	2.70
Expected share price return	-5.9%
Net dividend yield	2.8%
Estimated 12-month return	-3.1%

Key WACC assumptions	
Risk free rate	2.30%
Equity beta	0.71
WACC	4.9%
Terminal growth	1.5%

Spot valuations (NZ\$)	
1. DCF	2.69
2. NAV	2.67
3. n/a	n/a

DCF valuation summary (NZ\$m)	
Total firm value	1,478
(Net debt)/cash	(486)
Less: Capitalised operating leases	0
Value of equity	986

Profit and Loss Account (NZ\$m)	2019A	2020A	2021E	2022E	2023E
Sales revenue	79.7	79.6	80.9	76.3	77.9
Normalised EBITDA	74.6	73.8	74.1	69.4	70.9
Depreciation and amortisation	0	0	0	0	0
Normalised EBIT	74.6	73.8	74.1	69.4	70.9
Net interest	(19.0)	(18.2)	(18.0)	(13.9)	(13.5)
Associate income	0	0	0	0	0
Tax	(13.1)	(10.1)	(10.2)	(10.1)	(11.1)
Minority interests	0	0	0	0	0
Normalised NPAT	42.5	45.5	46.0	45.4	46.4
Abnormals/other	133.7	68.0	13.1	10.4	20.3
Reported NPAT	176.2	113.5	59.0	55.8	66.6
Normalised EPS (cps)	8.5	9.1	9.2	9.1	9.2
DPS (cps)	7.6	7.7	8.0	8.0	8.1

Growth Rates	2019A	2020A	2021E	2022E	2023E
Revenue (%)	4.8	-0.1	1.6	-5.7	2.0
EBITDA (%)	4.5	-1.1	0.4	-6.3	2.1
EBIT (%)	4.5	-1.1	0.4	-6.3	2.1
Normalised NPAT (%)	1.8	7.0	1.0	-1.2	2.1
Normalised EPS (%)	1.8	6.8	0.7	-1.2	2.1
Ordinary DPS (%)	0.7	1.3	3.4	0.6	1.4

Cash Flow (NZ\$m)	2019A	2020A	2021E	2022E	2023E
EBITDA	74.6	73.8	74.1	69.4	70.9
Working capital change	1.8	(1.0)	0.1	(0.4)	0.1
Interest & tax paid	(28.1)	(37.7)	(28.1)	(24.0)	(24.5)
Other	0	0	0	0	0
Operating cash flow	48.4	35.2	46.1	45.0	46.5
Capital expenditure	(16.1)	(24.5)	(5.5)	(5.6)	(5.7)
(Acquisitions)/divestments	(10.3)	(58.2)	44.5	0	0
Other	0.7	5.0	0	0	0
Funding available/(required)	22.8	(42.6)	85.0	39.4	40.8
Dividends paid	(37.7)	(31.4)	(41.2)	(40.1)	(40.6)
Equity raised/(returned)	0	0	0	0	0
(Increase)/decrease in net debt	(14.9)	(74.0)	43.8	(0.7)	0.3

Balance Sheet (NZ\$m)	2019A	2020A	2021E	2022E	2023E
Working capital	(7.2)	(3.8)	(3.8)	(3.6)	(3.7)
Fixed assets	1,476.2	1,631.5	1,605.6	1,621.6	1,647.6
Intangibles	29.1	29.1	29.1	29.1	29.1
Right of use asset	0	0	0	0	0
Other assets	13.8	20.0	20.0	20.0	20.0
Total funds employed	1,511.9	1,676.8	1,650.8	1,667.1	1,693.0
Net debt/(cash)	411.8	486.2	442.4	443.1	442.9
Lease liability	0	0	0	0	0
Other liabilities	45.9	53.8	53.8	53.7	53.7
Shareholder's funds	1,054.3	1,136.8	1,154.6	1,170.3	1,196.4
Minority interests	0	0	0	0	0
Total funding sources	1,511.9	1,676.8	1,650.8	1,667.1	1,693.0

* 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)	24.7	25.6	25.7	27.1	26.5
EV/EBIT (x)	24.7	25.6	25.7	27.1	26.5
PE (x)	33.7	31.5	31.3	31.7	31.0
Price/NTA (x)	1.4	1.3	1.3	1.3	1.2
Free cash flow yield (%)	2.2	0.7	2.8	2.7	2.8
Net dividend yield (%)	2.6	2.7	2.8	2.8	2.8
Gross dividend yield (%)	3.8	3.8	4.0	4.0	4.0

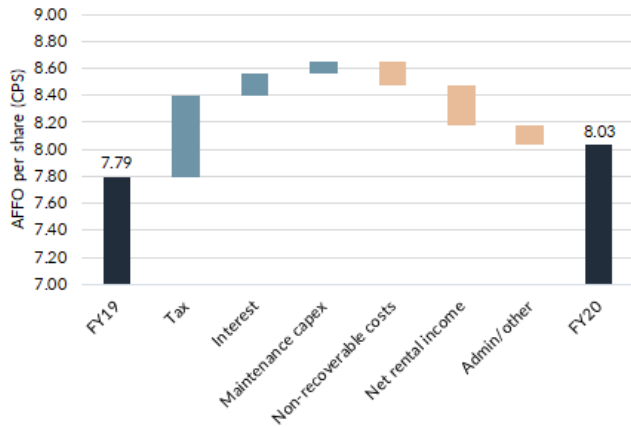
Capital Structure	2019A	2020A	2021E	2022E	2023E
Interest cover EBIT (x)	3.9	4.0	4.1	5.0	5.3
Interest cover EBITDA (x)	3.9	4.0	4.1	5.0	5.3
Net debt/ND+E (%)	28.1	30.0	27.7	27.5	27.0
Net debt/EBITDA (x)	5.5	6.6	6.0	6.4	6.2

Key Ratios	2019A	2020A	2021E	2022E	2023E
Return on assets (%)	4.9	4.4	4.5	4.1	4.2
Return on equity (%)	4.0	4.0	4.0	3.9	3.9
Return on funds employed (%)	4.0	3.8	3.7	3.5	3.4
EBITDA margin (%)	93.6	92.7	91.5	90.9	91.0
EBIT margin (%)	93.6	92.7	91.5	90.9	91.0
Capex to sales (%)	20.2	30.8	6.8	7.4	7.3
Capex to depreciation (%)	n/a	n/a	n/a	n/a	n/a
Imputation (%)	100	100	100	100	100
Pay-out ratio (%)	89	85	87	88	88

Portfolio Summary	2015A	2016A	2017A	2018A	2019A
Investment properties (NZ\$m)	987	1,083	1,211	1,322	1,476
Weighted average lease term (yrs)	5.2	4.8	5.3	5.4	5.4
Occupancy rate (%)	99.6	99.6	99.9	99.3	99.0
Number of properties	84	83	92	94	94
NTA per share (NZ\$)	1.41	1.61	1.63	1.78	2.06

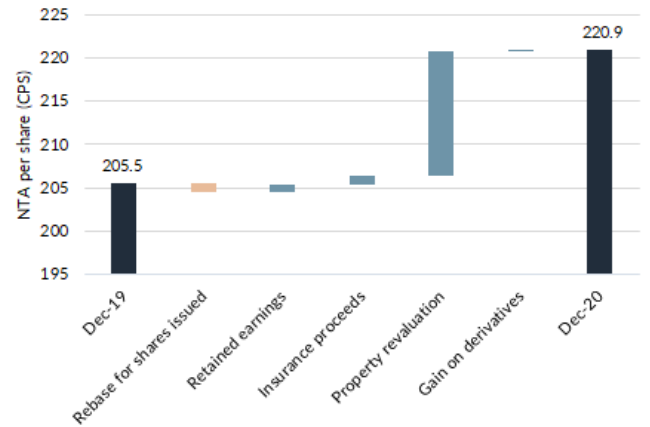
PFI's result in charts

Figure 1. AFFO bridge (CPS)



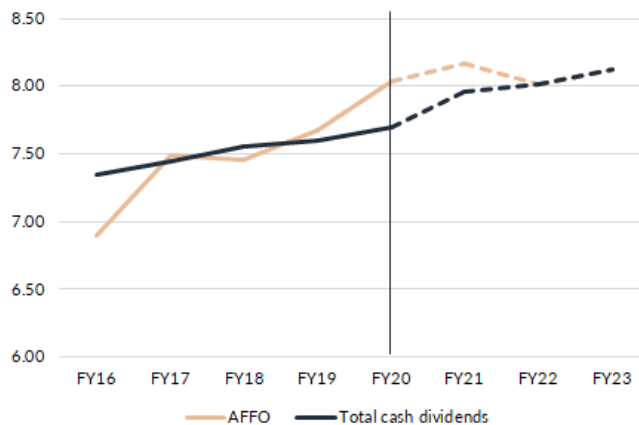
Source: Forsyth Barr analysis, Company reports

Figure 2. NTA bridge (CPS)



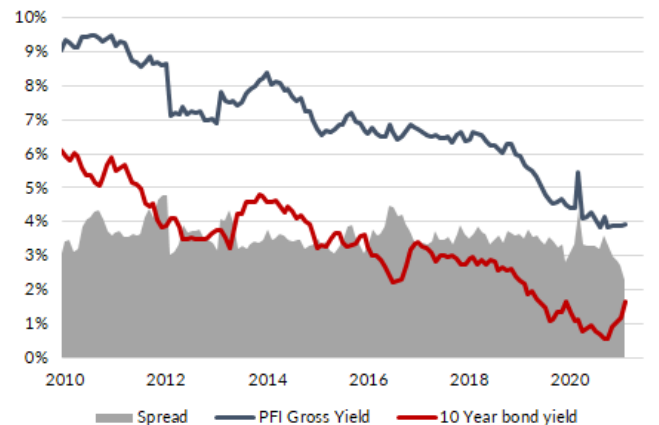
Source: Forsyth Barr analysis, Company reports

Figure 3. AFFO vs DPS



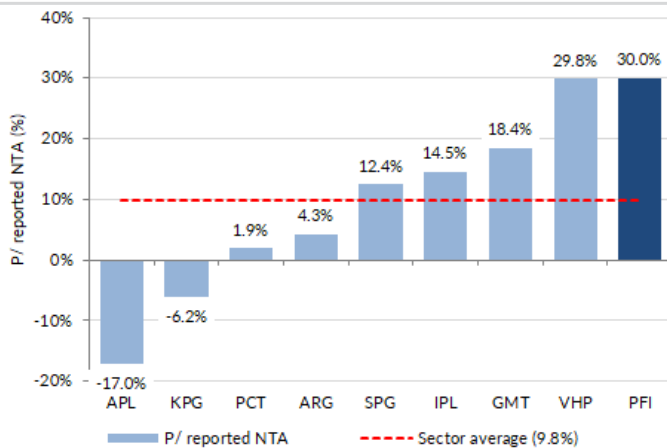
Source: Forsyth Barr analysis, Company reports

Figure 4. PFI gross yield spread to bonds



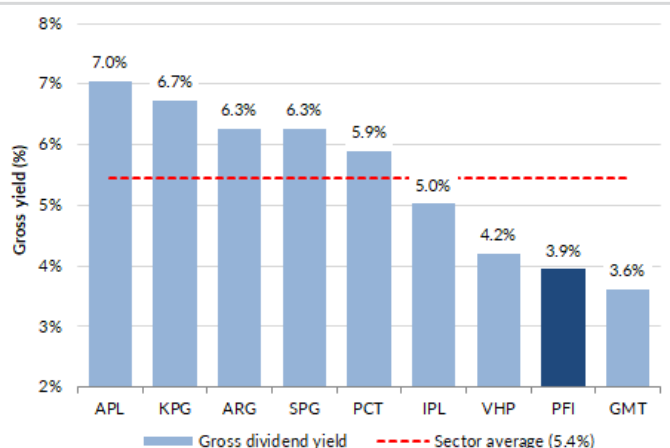
Source: Forsyth Barr analysis, Company reports

Figure 5. LPV price-to-NTA



Source: Forsyth Barr analysis, Company reports

Figure 6. LPV gross yield



Source: Forsyth Barr analysis, Company reports

Result summary

Figure 7. FY20 result summary

Financial period 12 months ending	FY19 12/19	FY20 12/20	Change pcp	Forecast	Var
Underlying profit & loss (NZ\$000s)					
Net income	79,736	79,646	-0.1%	77,459	2.8%
Base corporate costs	(5,273)	(6,026)	14.3%	(5,385)	11.9%
EBITDA	74,628	73,795	-1.1%	71,849	2.7%
Net interest	(19,000)	(18,230)	-4.1%	(17,824)	2.3%
PBT	55,628	55,565	-0.1%	54,025	2.9%
Current tax	(13,106)	(10,066)	-23.2%	(10,133)	-0.7%
NPAT (underlying)	42,522	45,499	7.0%	43,892	3.7%
Amortisation of incentives and other	2,644	2,841	7.5%	2,644	7.4%
Funds from operations (FFO)	45,166	48,340	7.0%	46,536	3.9%
Maintenance capex	(4,476)	(2,977)	-33.5%	(5,122)	-41.9%
Tenant incentives, leasing fees and other	(2,414)	(5,235)	n/m	(3,108)	68.4%
Adjusted funds from operations	38,276	40,128	4.8%	38,306	4.8%
NPAT underlying	42,522	45,499	7.0%	43,892	3.7%
Investment property revaluations	125,193	72,546	-42.1%	(5,122)	n/m
Other non-operating adjustments	8,520	(4,593)	n/m	2,151	n/m
NPAT (reported)	176,235	113,452	-35.6%	40,921	n/m
Weighted shares on issue (000s)	498,723	499,650	0.2%	500,427	-0.2%
NPAT (Forbar) per share (cps)	8.53	9.11	6.8%	8.77	3.8%
FFO per share (cps)	9.06	9.67	6.8%	9.30	4.0%
AFFO per share (cps)	7.67	8.03	4.6%	7.65	4.9%
Dividends (cps)	7.60	7.70	1.3%	7.65	0.7%
Pay-out (NPAT)	89%	85%	-5.1%	87%	-3.1%
Pay-out (FFO)	84%	80%	-5.2%	82%	-3.3%
Pay-out (AFFO)	99%	96%	-3.2%	100%	-4.1%

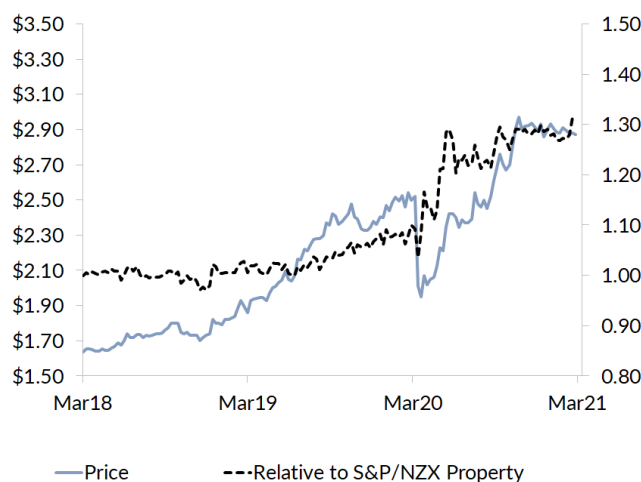
Source: Forsyth Barr analysis, Company reports

Earnings changes

Figure 8. Forecast revisions

NZ\$m	FY21			FY22			FY23		
	Old	New	%	Old	New	%	Old	New	%
Net income	82.7	84.9	2.7%	83.9	80.1	-4.5%	86.0	81.7	-5.0%
Base corporate costs	(9.0)	(10.9)	21.2%	(9.0)	(10.7)	18.2%	(9.2)	(10.8)	17.6%
EBITDA	73.7	74.1	0.5%	74.8	69.4	-7.3%	76.8	70.9	-7.7%
Net interest	(17.9)	(18.0)	0.6%	(17.0)	(13.9)	-18.4%	(15.8)	(13.5)	-14.8%
Current tax	(10.3)	(10.2)	-1.6%	(11.0)	(10.1)	-8.0%	(12.3)	(11.1)	-9.9%
NPAT (underlying)	45.5	46.0	1.0%	46.8	45.4	-3.1%	48.7	46.4	-4.9%
Amortisation of incentives and other	2.8	3.1	12.0%	2.8	2.9	4.1%	2.9	3.0	3.6%
Funds from operations (FFO)	48.3	49.1	1.6%	49.7	48.3	-2.7%	51.6	49.3	-4.4%
Maintenance capex	(5.3)	(5.5)	4.2%	(5.4)	(5.6)	5.0%	(5.4)	(5.7)	5.2%
Tenant incentives, leasing fees and other	(2.8)	(2.6)	-6.3%	(4.0)	(2.5)	-36.1%	(3.6)	(3.0)	-16.5%
Adjusted funds from operations	40.2	40.9	1.8%	40.3	40.2	-0.4%	42.7	40.7	-4.6%
AFFO PS	7.99	8.17	2.1%	8.02	8.01	-0.1%	8.48	8.12	-4.3%
DPS	7.91	7.96	0.6%	8.02	8.01	-0.1%	8.48	8.12	-4.3%

Source: Forsyth Barr analysis

Figure 9. Price performance


Source: Forsyth Barr analysis

Figure 10. Substantial shareholders

Shareholder	Latest Holding
ANZ NZ Investments	7.3%
ACC	5.3%

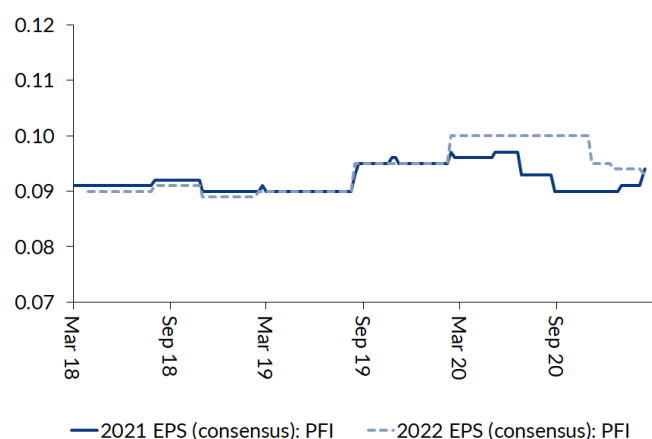
Source: NZX, Forsyth Barr analysis, NOTE: based on SPH notices only

Figure 11. International valuation comparisons

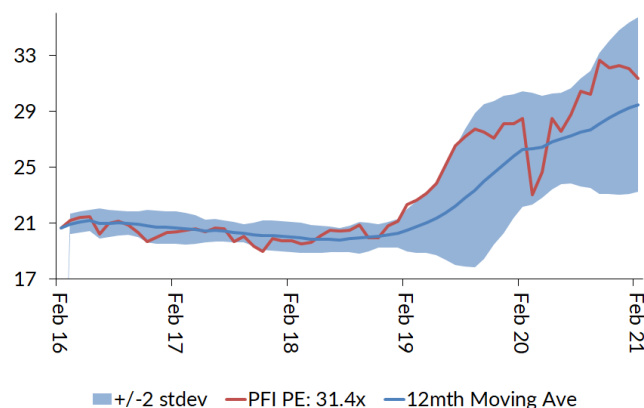
Company	Code	Price	Mkt Cap	PE		EV/EBITDA		EV/EBIT		Cash Yld	
(metrics re-weighted to reflect PFI's balance date - December)				2021E	2022E	2021E	2022E	2021E	2022E	2022E	
Property For Industry	PFI NZ	NZ\$2.87	NZ\$1,439	31.3x	31.7x	26.0x	27.7x	26.0x	27.7x	2.8%	
ARGOSY PROPERTY *	ARG NZ	NZ\$1.52	NZ\$1,272	20.6x	20.3x	20.8x	20.0x	20.8x	20.0x	4.3%	
GOODMAN PROPERTY TRUST *	GMT NZ	NZ\$2.18	NZ\$3,033	32.0x	31.2x	25.7x	24.5x	25.7x	24.5x	2.6%	
INVESTORE *	IPL NZ	NZ\$2.20	NZ\$810	26.4x	24.9x	21.3x	20.3x	21.3x	20.3x	3.7%	
KIWI PROPERTY GROUP *	KPG NZ	NZ\$1.22	NZ\$1,907	19.2x	17.9x	18.2x	17.2x	18.2x	17.2x	4.9%	
ASSET PLUS *	APL NZ	NZ\$0.36	NZ\$135	23.3x	31.6x	28.4x	36.3x	28.4x	36.3x	5.1%	
PRECINCT PROPERTIES NZ *	PCT NZ	NZ\$1.61	NZ\$2,109	25.0x	24.6x	25.8x	24.3x	25.8x	24.3x	4.1%	
STRIDE PROPERTY *	SPG NZ	NZ\$2.35	NZ\$1,111	22.1x	21.9x	29.0x	27.6x	29.0x	27.6x	4.2%	
VITAL HEALTHCARE *	VHP NZ	NZ\$3.09	NZ\$1,593	28.0x	26.7x	26.2x	24.4x	26.2x	24.4x	3.1%	
Compco Average:				24.6x	24.9x	24.4x	24.3x	24.4x	24.3x	4.0%	
EV = Current Market Cap + Actual Net Debt				PFI Relative:	27%	27%	6%	14%	6%	14%	-30%

EV = Current Market Cap + Actual Net Debt

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

Figure 12. Consensus EPS momentum (NZ\$)


Source: Forsyth Barr analysis

Figure 13. One year forward PE (x)


Source: Forsyth Barr analysis

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