NEW ZEALAND EQUITY RESEARCH | PROPERTY | HEALTHCARE PROPERTY
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Vital Healthcare
1H21 — Healthy Result, Healthy Valuation

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NEUTRAL

Vital Healthcare Property (VHP) reported a solid 1H21 ahead of our expectations, largely due to better net rental income. VHP's strong top line was largely driven by acquisitions and development income. VHP also tweaked DPS guidance slightly and now expect to pay 4.5cps in 2H21 taking FY21 distributions to 8.88cps. We expect VHP's portfolio to continue to provide investors with a defensive property exposure, with good distribution growth prospects underpinned by developments (we forecast growth of 3% per annum to FY23); however, this is largely in the share price in our view. With VHP trading broadly in line with our NZ$3.15 12-month target, we lower our rating from OUTPERFORM to NEUTRAL.

NZX Code	VHP
Share price	NZ$3.10
Target price	NZ$3.15
Risk rating	n/a
Issued shares	515.6m
Market cap	NZ$1,598m
Avg daily turnover	271.2k (NZ$756k)

Financials: Jun/	20A	21E	22E	23E
NPAT* (NZ$m)	46.8	54.9	60.8	62.6
EPS* (NZc)	10.4	11.1	11.8	12.0
EPS growth* (%)	7.2	6.8	6.4	2.3
DPS (NZc)	8.8	8.9	9.2	9.6
Imputation (%)	100	100	100	100
*Based on normalised profits				

Valuation (x)	20A	21E	22E	23E
PE	29.9	28.0	26.3	25.7
EV/EBIT	28.9	26.6	24.5	23.0
EV/EBITDA	28.9	26.6	24.5	23.0
Price / NTA	1.3	1.2	1.1	1.1
Cash div yld (%)	2.8	2.9	3.0	3.1
Gross div yld (%)	4.0	4.1	4.3	4.4

What's changed?

- **Earnings:** We lift our FY21–23 AFFO +7%/+7%/+5% reflecting updated FX and lower tax, our DPS forecasts are largely unchanged
- **Rating:** Downgrade to NEUTRAL (from OUTPERFORM)

Portfolio metrics remain supportive

Headline metrics of VHP's portfolio remain very solid, reporting occupancy of 99.1% and a weighted average lease expiry of 19.0 years. Like-for-like net property income grew 1.5% and rent reviews delivered a +2.1% uplift. 98% of leases are subject to structured rent reviews. Revaluation gains saw VHP's NTA lift to NZ$2.55 (FY20: NZ$2.38).

Development pipeline to drive growth

Gearing reduced to 32.4% (FY20 38.7%) with VHP having raised capital to fund its c.NZ$360m of committed developments (NZ$225m spend to complete). VHP stated it has a further NZ$560m of potential developments within its current portfolio. Development is likely a more attractive capital allocation option vs. buying assets on market given current demand for property with long lease terms and the medical sub-setor. This activity should provide 1) better NTA (revaluation of current projects will add +9cps once complete), and 2) stronger earnings growth (current projects, acquisitions, and divestments will increase net rental income by ~+20%) and is an integral part of VHP reaching its +2–3% per annum distribution growth targets.

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 +54bp increase in our WACC which, while partly offset by our earnings changes, lowers our DCF by c.6%. This impact is broadly offset by a 4% lift in our NAV driven by higher property values.

FORSYTH BARR

Vital Healthcare Property Trust (VHP)

Priced as at 25 Feb 2021 (NZ$)	3.10

12-month target price (NZ$)*	**3.15**
Expected share price return	1.6%
Net dividend yield	2.9%
Estimated 12-month return	4.6%

Spot valuations (NZ$)	
1. DCF	3.25
2. NAV	2.90

Key WACC assumptions	
Risk free rate	2.30%
Equity beta	0.68
WACC	4.6%
Terminal growth	1.8%

DCF valuation summary (NZ$m)	
Total firm value	2,510
(Net debt)/cash	(808)
Less: Capitalised operating leases	0
Value of equity	1,638

Profit and Loss Account (NZ$m)	**2019A**	**2020A**	**2021E**	**2022E**	**2023E**
Sales revenue	97.7	98.8	108.0	116.7	123.6
Normalised EBITDA	**80.3**	**82.0**	**90.5**	**98.1**	**104.3**
Depreciation and amortisation	0	0	0	0	0
Normalised EBIT	**80.3**	**82.0**	**90.5**	**98.1**	**104.3**
Net interest	(29.9)	(28.0)	(25.7)	(26.1)	(30.0)
Associate income	0	0	0	0	0
Tax	(7.6)	(7.2)	(9.8)	(11.1)	(11.7)
Minority interests	0	0	0	0	0
Normalised NPAT	**42.9**	**46.8**	**54.9**	**60.8**	**62.6**
Abnormals/other	50.6	11.4	76.8	55.1	40.9
Reported NPAT	**93.4**	**58.1**	**131.8**	**115.9**	**103.5**
Normalised EPS (cps)	9.7	10.4	11.1	11.8	12.0
DPS (cps)	8.8	8.8	8.9	9.2	9.6

Valuation Ratios	**2019A**	**2020A**	**2021E**	**2022E**	**2023E**
EV/EBITDA (x)	28.6	28.9	26.6	24.5	23.0
EV/EBIT (x)	28.6	28.9	26.6	24.5	23.0
PE (x)	32.1	29.9	28.0	26.3	25.7
Price/NTA (x)	1.3	1.3	1.2	1.1	1.1
Free cash flow yield (%)	0.3	-2.5	-7.1	-4.6	2.6
Net dividend yield (%)	2.8	2.8	2.9	3.0	3.1
Gross dividend yield (%)	4.0	4.0	4.1	4.3	4.4

Capital Structure	**2019A**	**2020A**	**2021E**	**2022E**	**2023E**
Interest cover EBIT (x)	2.7	2.9	3.5	3.8	3.5
Interest cover EBITDA (x)	2.7	2.9	3.5	3.8	3.5
Net debt/ND+E (%)	41.4	42.8	37.5	39.3	38.1
Net debt/EBITDA (x)	9.1	9.9	8.9	9.3	8.8

Growth Rates	**2019A**	**2020A**	**2021E**	**2022E**	**2023E**
Revenue (%)	7.8	1.1	9.4	8.1	5.9
EBITDA (%)	5.6	2.1	10.3	8.4	6.3
EBIT (%)	5.6	2.1	10.3	8.4	6.3
Normalised NPAT (%)	-6.9	9.1	17.5	10.7	3.0
Normalised EPS (%)	-8.9	7.2	6.8	6.4	2.3
Ordinary DPS (%)	2.2	0.0	1.4	4.0	3.9

Key Ratios	**2019A**	**2020A**	**2021E**	**2022E**	**2023E**
Return on assets (%)	4.2	3.9	3.8	3.8	4.0
Return on equity (%)	4.2	4.3	4.1	4.3	4.2
Return on funds employed (%)	3.9	3.8	3.8	3.7	3.7
EBITDA margin (%)	82.2	83.0	83.8	84.0	84.4
EBIT margin (%)	82.2	83.0	83.8	84.0	84.4
Capex to sales (%)	36.3	85.2	157.3	116.6	18.4
Capex to depreciation (%)	n/a	n/a	n/a	n/a	n/a
Imputation (%)	100	100	100	100	100
Pay-out ratio (%)	91	85	80	78	80

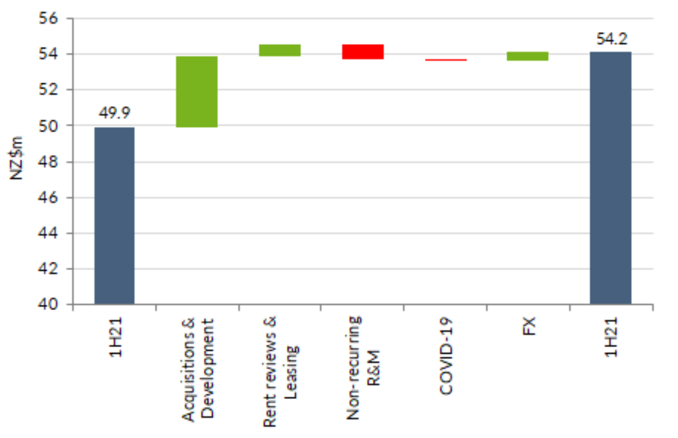
Cash Flow (NZ$m)	**2019A**	**2020A**	**2021E**	**2022E**	**2023E**
EBITDA	**80.3**	**82.0**	**90.5**	**98.1**	**104.3**
Working capital change	(1.9)	(1.3)	(0.1)	0.0	0.0
Interest & tax paid	(37.8)	(36.3)	(33.8)	(35.1)	(39.4)
Other	0	0	0	0	0
Operating cash flow	**40.6**	**44.4**	**56.6**	**63.0**	**65.0**
Capital expenditure	(35.5)	(84.1)	(169.9)	(136.1)	(22.7)
(Acquisitions)/divestments	(23.5)	(65.2)	1.9	0	0
Other	(42.2)	79.3	0	0	0
Funding available/(required)	**(60.5)**	**(25.6)**	**(111.4)**	**(73.1)**	**42.3**
Dividends paid	(32.7)	(33.5)	(37.4)	(40.9)	(41.7)
Equity raised/(returned)	0	0	155.3	0	0
(Increase)/decrease in net debt	**(93.2)**	**(59.2)**	**6.4**	**(114.0)**	**0.6**

Balance Sheet (NZ$m)	**2019A**	**2020A**	**2021E**	**2022E**	**2023E**
Working capital	(12.5)	(13.8)	(13.8)	(13.8)	(13.8)
Fixed assets	1,836.4	2,086.3	2,335.7	2,532.4	2,602.0
Intangibles	0	0	0	0	0
Right of use asset	0	0	0	0	0
Other assets	87.7	8.4	8.4	8.4	8.4
Total funds employed	**1,911.7**	**2,081.0**	**2,330.3**	**2,527.0**	**2,596.6**
Net debt/(cash)	728.1	808.3	801.8	915.9	915.3
Lease liability	0	3.8	3.8	3.8	3.8
Other liabilities	153.8	189.9	189.9	189.9	189.9
Shareholder's funds	1,029.7	1,079.0	1,334.8	1,417.4	1,487.6
Minority interests	0	0	0	0	0
Total funding sources	**1,911.7**	**2,081.0**	**2,330.3**	**2,527.0**	**2,596.6**

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

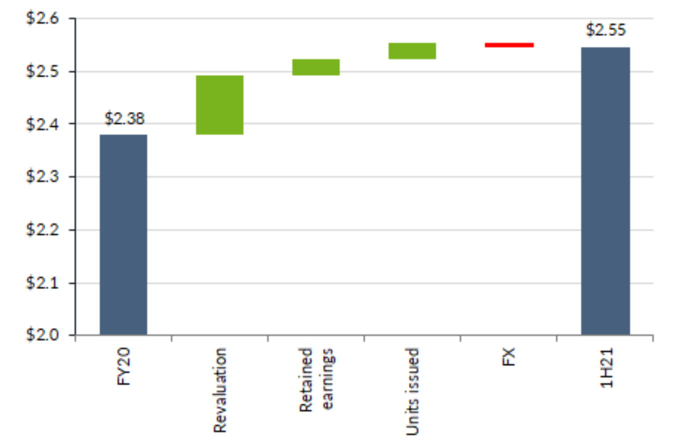
1H21 in charts

Figure 1. Net property income bridge



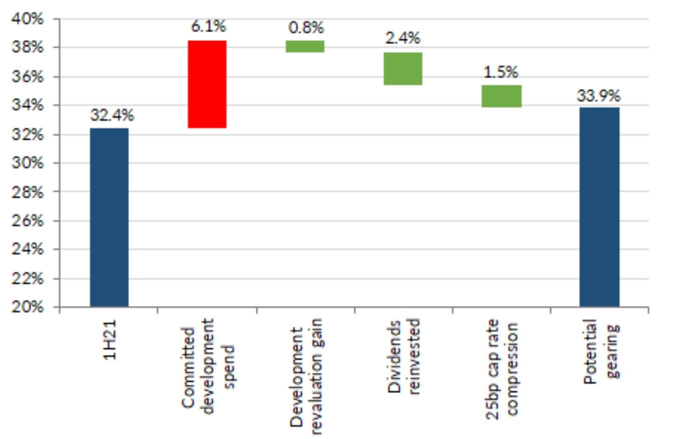
Source: Forsyth Barr analysis

Figure 2. NTA bridge



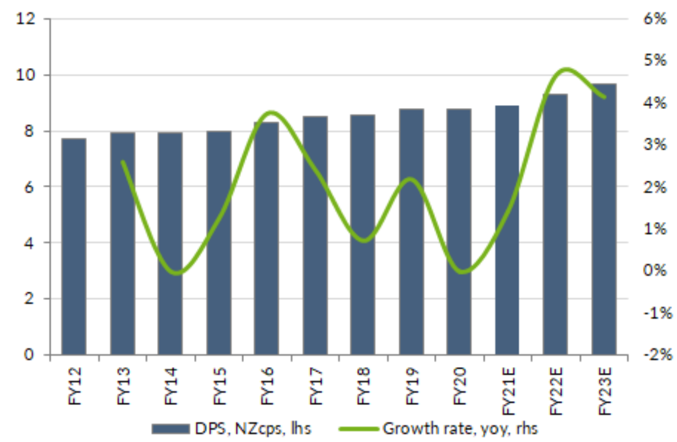
Source: Forsyth Barr analysis

Figure 3. Potential gearing



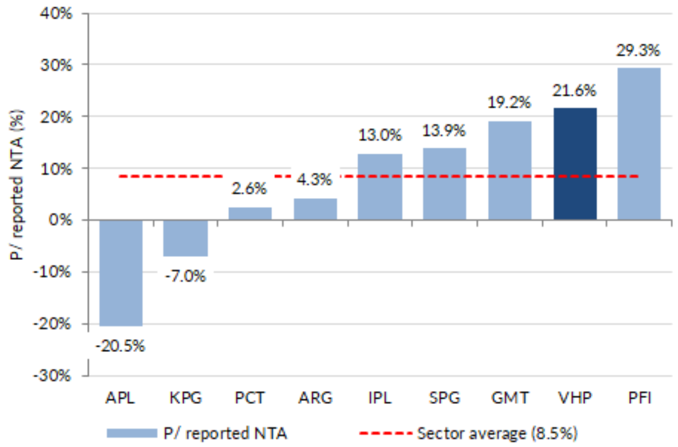
Source: Forsyth Barr analysis

Figure 4. DPS forecasts



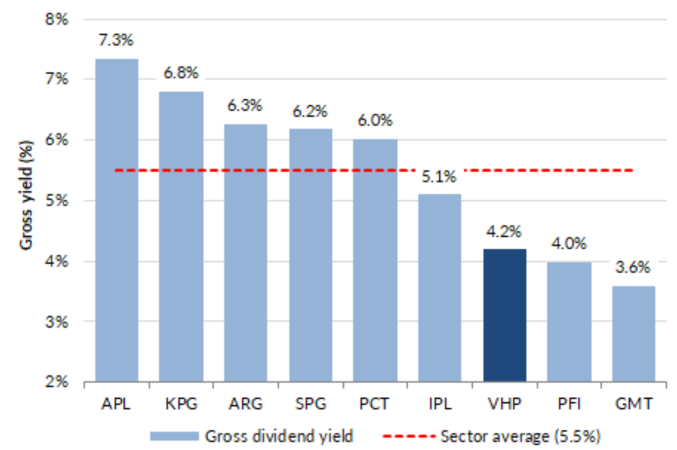
Source: Forsyth Barr analysis

Figure 5. LPV price-to-NTA



Source: Forsyth Barr analysis

Figure 6. LPV gross yield



Source: Forsyth Barr analysis

Result summary and earnings changes

Figure 7. Result summary

Financial period	1H20	1H21	% Chg	Forbar	% Var
Net property income	49.9	54.2	8.5%	51.0	6.2%
Corporate costs	(8.8)	(9.3)	5.7%	(9.5)	-2.2%
EBITDA	**41.1**	**44.9**	**9.1%**	**41.5**	**8.1%**
Interest expense	(14.3)	(13.5)	-5.3%	(12.8)	6.2%
PBT	**26.8**	**31.3**	**16.9%**	**28.7**	**9.0%**
Current tax - reported	(5.0)	(4.2)	-15.5%	(5.3)	-21.2%
NPAT	**21.8**	**27.1**	**24.2%**	**23.4**	**15.9%**
Add:					
Current tax expense/(benefit) on translation of borrowings	.2	.5	n/m	-	-
Amortisation of borrowing costs	.3	.3	18.7%	.3	18.7%
Amortisation of leasing costs and tenant inducements	.5	1.1	n/m	.5	n/m
Other	(.4)	(.1)	-81.0%	-	-
VHP reported FFO	**22.5**	**29.0**	**28.7%**	**24.2**	**19.9%**
Add:					
Non-recurring corporate costs	.3	-	n/m	-	-
Actual capex & leasing from continuing operations	(.8)	(.9)	1.8%	(.8)	1.8%
VHP reported AFFO	**22.0**	**28.1**	**27.9%**	**23.3**	**20.6%**
Less:					
Management incentive fees paid as units	(3.2)	(3.1)	-4%	(3.0)	3%
ForBar AFFO	**18.8**	**25.0**	**33%**	**20.3**	**23%**
EPU	4.85	5.66	16.7%	4.90	15.6%
VHP FFO per unit	5.00	6.05	21.0%	5.05	19.6%
VHP AFFO per unit	4.88	5.87	20.2%	4.88	20.2%
ForBar AFFO per unit	4.17	5.22	25.2%	4.25	22.8%
DPU	8.50	8.10	-4.7%	7.90	2.5%

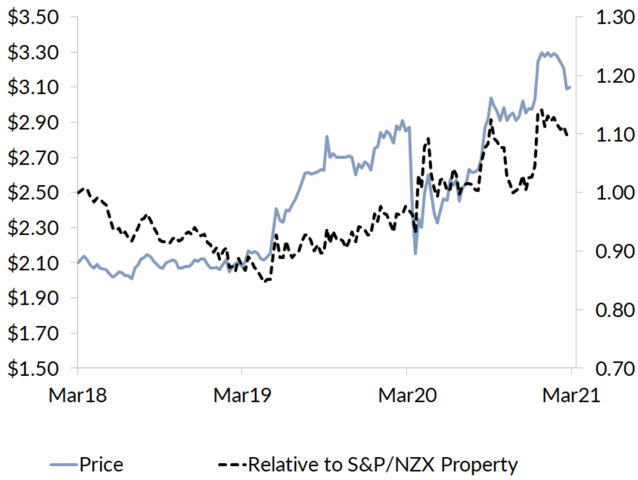
Source: Forsyth Barr analysis, Company reports

Figure 8. Earnings changes

		2021E			2022E			2023E	
	Old	New	% chg	Old	New	% chg	Old	New	% chg
Net income	105.9	108.0	2.0%	114.0	116.7	2.4%	120.9	123.6	2.3%
Corporate costs	(17.5)	(17.5)	0.2%	(18.6)	(18.6)	0.4%	(19.2)	(19.3)	0.6%
EBITDA	**88.4**	**90.5**	**2.4%**	**95.5**	**98.1**	**2.7%**	**101.6**	**104.3**	**2.6%**
Net interest	(25.5)	(25.7)	0.8%	(25.8)	(26.1)	1.2%	(28.6)	(30.0)	4.9%
Current tax	(9.7)	(9.8)	1.4%	(11.0)	(11.1)	1.6%	(11.7)	(11.7)	-0.2%
NPAT	**53.2**	**54.9**	**3.3%**	**58.7**	**60.8**	**3.6%**	**61.4**	**62.6**	**2.1%**
Maintenance capex	(1.0)	(1.0)	-	(1.1)	(1.1)	0.3%	(1.2)	(1.2)	0.7%
ForBar AFFO	**46.4**	**49.7**	**7.2%**	**50.6**	**54.5**	**7.7%**	**52.6**	**55.7**	**5.9%**
EPS (cps)	10.71	11.06	3.3%	11.36	11.77	3.6%	11.80	12.05	2.1%
AFFO (cps)	9.46	10.14	7.1%	9.92	10.67	7.6%	10.25	10.84	5.8%
DPS (cps)	8.87	8.88	0.1%	9.22	9.23	0.1%	9.63	9.59	-0.4%

Source: Forsyth Barr analysis

Figure 9. Price performance



Source: Forsyth Barr analysis

Figure 10. Substantial shareholders

Shareholder	Latest Holding
Northwest	25.8%
Forsyth Barr Investment Management	9.2%
ACC	5.0%

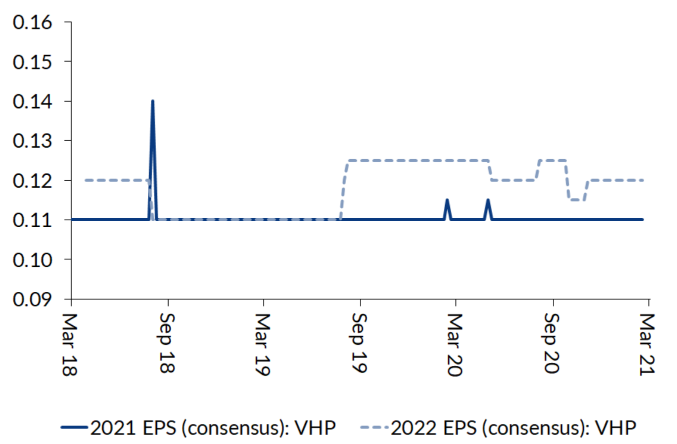
Source: NZX, Forsyth Barr analysis, NOTE: based on SPH notices only

Figure 11. International valuation comparisons

Company	Code	Price	Mkt Cap	PE		EV/EBITDA		EV/EBIT		Cash Yld
(metrics re-weighted to reflect VHP's balance date - June)			(m)	2021E	2022E	2021E	2022E	2021E	2022E	2022E
Vital Healthcare	**VHP NZ**	**NZ$3.10**	**NZ$1,598**	**28.0x**	**26.3x**	**26.6x**	**24.5x**	**26.6x**	**24.5x**	**3.0%**
ARGOSY PROPERTY *	ARG NZ	NZ$1.46	NZ$1,218	19.4x	19.7x	21.0x	19.7x	21.0x	19.7x	4.5%
GOODMAN PROPERTY TRUST *	GMT NZ	NZ$2.18	NZ$3,033	32.3x	31.6x	26.5x	25.0x	26.5x	25.0x	2.5%
INVESTORE *	IPL NZ	NZ$2.20	NZ$810	27.7x	25.5x	22.4x	20.6x	22.4x	20.6x	3.6%
KIWI PROPERTY GROUP *	KPG NZ	NZ$1.20	NZ$1,883	20.6x	18.0x	19.8x	17.2x	19.8x	17.2x	4.9%
ASSET PLUS *	APL NZ	NZ$0.36	NZ$137	18.0x	28.3x	25.3x	32.6x	25.3x	32.6x	5.0%
PRECINCT PROPERTIES NZ *	PCT NZ	NZ$1.60	NZ$2,095	25.0x	24.7x	26.2x	25.2x	26.2x	25.2x	4.1%
PROPERTY FOR INDUSTRY *	PFI NZ	NZ$2.88	NZ$1,441	31.5x	31.5x	26.1x	26.9x	26.1x	26.9x	2.8%
STRIDE PROPERTY *	SPG NZ	NZ$2.26	NZ$1,069	20.8x	21.3x	30.2x	27.0x	30.2x	27.0x	4.4%
			Compco Average:	**24.4x**	**25.1x**	**24.7x**	**24.3x**	**24.7x**	**24.3x**	**4.0%**
EV = Current Market Cap + Actual Net Debt			**VHP Relative:**	**15%**	**5%**	**8%**	**1%**	**8%**	**1%**	**-25%**

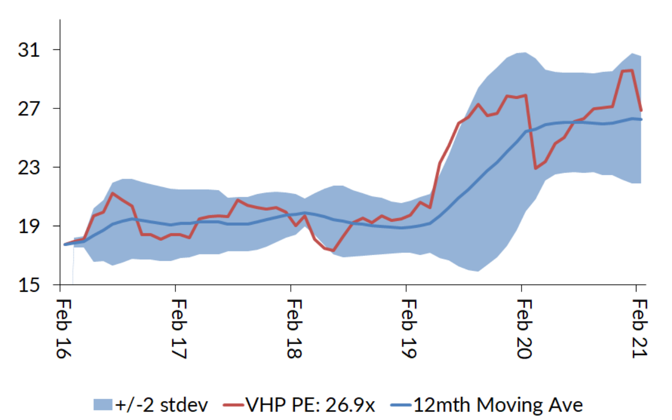
Source: *Forsyth Barr analysis, Bloomberg Consensus, Compco metrics re-weighted to reflect headline (VHP) companies fiscal year end

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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OUTPERFORM	NEUTRAL	UNDERPERFORM
44.2%	**36.5%**	**19.2%**

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