

Kiwi Property Group

Capital Raise Via Dividend Cut

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UNDERPERFORM

KPG has surprised the market and cut its large 2H20 dividend for the six months to 31 March to be prudent and to manage gearing levels. There remains considerable uncertainty with regard to how KPG's retail assets track near-term and also what happens with its FY20 portfolio revaluation, and we expect the news flow to remain challenging. We downgrade our rating to UNDERPERFORM and we have cut our 1H21 dividend forecasts.

NZX Code	KPG	Financials: Mar/	19A	20E	21E	22E	Valuation (x)	19A	20E	21E	22E
Share price	NZ\$0.85	NPAT* (NZ\$m)	99.9	104.0	113.8	116.1	EV/EBITDA	13.5	13.3	12.3	11.8
Target price	NZ\$1.29	EPS* (NZc)	7.0	7.1	7.3	7.4	EV/EBIT	13.5	13.3	12.3	11.8
Risk rating	Medium	EPS growth* (%)	-6.2	1.6	2.6	1.8	PE	12.2	12.0	11.7	11.4
Issued shares	1432.8m	DPS (NZc)	7.0	3.5	5.0	6.7	Price / NTA	0.6	0.6	0.5	0.5
Market cap	NZ\$1,218m	Imputation (%)	100	100	100	100	Cash div yld (%)	8.2	4.1	5.8	7.9
Avg daily turnover	1,675k (NZ\$2,476k)	*Based on normalised profits					Gross div yld (%)	11.7	5.9	8.3	11.3

Retail risks in focus

While KPG's headline portfolio metrics are solid (99.4% occupancy and 5.1 year WALT) a deterioration is expected given its high exposure to retail. Risks include rent relief to keep tenants going until centres fully re-open, rental levels, occupancy, and the speed of recovery. Post GFC, KPG's occupancy declined 230bp over four years. We expect that the deterioration from COVID-19 will be more rapid and of a greater magnitude, particularly in the case of a protracted lockdown. Outcomes within KPG's portfolio will be bifurcated with mixed-use (KPG's good retail) outperforming the remaining retail. Sylvia Park vacancy increased only 70bp post GFC.

Distribution cut with no 2H20 dividend, and we assume a weak 1H21 dividend

KPG's distribution is unique vs. peers as it is paid semi-annually. Given ongoing disruption in 1Q21 we have assumed the 1H21 distribution is reduced by -50%. This retains ~\$80m of capital compared to KPG's GFC capital raise of NZ\$65m (plus a \$120m convertible note). Further, we expect distribution payments to be restarted at a lower level in 2H21, more in line with AFFO, with KPG going into this crisis with one of the highest pay-out ratios. Our FY20-22 EPS lifts +0%/+1%/+2% on lower interest costs but our dividends reduce -50%/-31%/-6%. KPG is reviewing discretionary capex and opex and has reduced employee costs (Board and exec team pay reduced -20%). Our earnings forecasts are under review and in our upcoming *Real Estate Reflections* out later this week, we review the LPV sector dividend outlook.

Downgraded to UNDERPERFORM

KPG has a solid financial position having recently undertaken a capital raise (\$200m in Oct-19) as well as extending the term of its bank facilities (no maturities until FY23). All eyes are now on what happens with KPG's FY20 portfolio revaluation and we expect the news flow to remain challenging.

Kiwi Property Group Limited (KPG)

Priced as at 06 Apr 2020 (NZ\$)						0.85										
12-month target price (NZ\$)*						1.29	Spot valuations (NZ\$)									
Expected share price return						51.8%	1. DCF					1.67				
Net dividend yield						6.0%	2. NAV					1.14				
Estimated 12-month return						57.8%	n/a					n/a				
Key WACC assumptions						DCF valuation summary (NZ\$m)										
Risk free rate						2.00%	Total firm value					3,504				
Equity beta						0.67	(Net debt)/cash					(992)				
WACC						5.1%	Less: Capitalised operating leases					0				
Terminal growth						1.5%	Value of equity					2,487				
Profit and Loss Account (NZ\$m)						Valuation Ratios										
Sales revenue	2018A	2019A	2020E	2021E	2022E	2018A	2019A	2020E	2021E	2022E	2018A	2019A	2020E	2021E	2022E	
Normalised EBITDA	191.7	180.8	185.6	197.8	205.2	171.2	160.0	164.7	176.4	183.4	12.7	13.5	13.3	12.3	11.8	
Depreciation and amortisation	(42.4)	(37.5)	(36.3)	(34.5)	(35.8)	0	0	0	0	0	12.7	13.5	13.3	12.3	11.8	
Normalised EBIT	0	0	0	0	0	171.2	160.0	164.7	176.4	183.4	11.4	12.2	12.0	11.7	11.4	
Net interest	(42.4)	(37.5)	(36.3)	(34.5)	(35.8)	0	0	0	0	0	0.6	0.6	0.6	0.5	0.5	
Associate income	0	0	0	0	0	(42.4)	(37.5)	(36.3)	(34.5)	(35.8)	-0.4	-5.7	-4.7	5.3	8.4	
Tax	(25.4)	(22.6)	(24.4)	(28.1)	(31.5)	0	0	0	0	0	8.1	8.2	4.1	5.8	7.9	
Minority interests	0	0	0	0	0	(25.4)	(22.6)	(24.4)	(28.1)	(31.5)	11.5	11.7	5.9	8.3	11.3	
Normalised NPAT	103.4	99.9	104.0	113.8	116.1	0	0	0	0	0	Capital Structure					
Abnormals/other	(16.7)	(38.2)	(46.0)	(46.1)	(48.9)	103.4	99.9	104.0	113.8	116.1	2018A	2019A	2020E	2021E	2022E	
Reported NPAT	120.1	138.1	150.0	159.9	165.0	(16.7)	(38.2)	(46.0)	(46.1)	(48.9)	4.0	4.3	4.5	5.1	5.1	
Normalised EPS (cps)	7.5	7.0	7.1	7.3	7.4	120.1	138.1	150.0	159.9	165.0	4.0	4.3	4.5	5.1	5.1	
DPS (cps)	6.9	7.0	3.5	5.0	6.7	7.5	7.0	7.1	7.3	7.4	31.2	32.6	29.1	26.9	26.5	
Growth Rates						Key Ratios										
Revenue (%)	2018A	2019A	2020A	2021A	2022A	2018A	2019A	2020E	2021E	2022E	2018A	2019A	2020E	2021E	2022E	
EBITDA (%)	5.4	-5.7	2.6	6.6	3.7	5.6	4.9	4.8	5.0	5.1	5.6	4.9	4.8	5.0	5.1	
EBIT (%)	4.4	-6.5	3.0	7.1	4.0	5.2	4.9	4.5	4.7	4.6	4.7	4.3	4.1	4.2	4.2	
Normalised NPAT (%)	4.4	-6.5	3.0	7.1	4.0	4.7	4.3	4.1	4.2	4.2	89.3	88.5	88.7	89.2	89.4	
Ordinary DPS (%)	7.6	-3.4	4.2	9.4	2.0	89.3	88.5	88.7	89.2	89.4	89.3	88.5	88.7	89.2	89.4	
	0.4	-6.2	1.6	2.6	1.8	EBIT margin (%)	89.3	88.5	88.7	89.2	89.4	88.5	88.7	89.2	89.4	
	1.9	1.5	-49.3	40.8	35.8	Capex to sales (%)	58.7	93.9	88.7	27.0	8.5	58.7	93.9	88.7	27.0	8.5
						Capex to depreciation (%)	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a
						Imputation (%)	100	100	100	100	100	100	100	100	100	100
						Pay-out ratio (%)	92	99	50	68	91	92	99	50	68	91
						Property Statistics						2015A	2016A	2017A	2018A	2019A
						Retail portfolio										
						No. properties						7	9	9	4	4
						WALT (years)						3.4	3.9	3.8	3.6	3.3
						Occupancy rate (%)						99.3%	99.1%	99.1%	99.4%	99.4%
						Cap rate (%)						6.97%	6.69%	6.52%	6.25%	7.53%
						Office portfolio										
						No. properties						5	5	5	4	4
						WALT (years)						7.6	8.2	10.1	10.1	9.3
						Occupancy rate (%)						96.1%	97.4%	97.8%	99.3%	98.7%
						Cap rate (%)						6.80%	6.44%	6.13%	5.76%	5.45%
						Mixed-use portfolio										
						No. properties									4	4
						WALT (years)									4.0	4.1
						Occupancy rate (%)									100.0%	99.5%
						Cap rate (%)									5.72%	5.71%
						Total portfolio										
						WALT (years)						4.5	5.1	5.6	5.3	5.2
						Occupancy rate (%)						98.4%	98.7%	98.8%	99.6%	99.3%
						Cap rate (%)						6.92%	6.61%	6.40%	6.11%	5.99%
						NTA per share (NZ\$)						1.214	1.345	1.390	1.392	1.431

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

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. **UNDERPERFORM.**

Business quality

- **Property fundamentals solid, reflecting strength of assets:** Portfolio metrics going into the current slowdown were 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

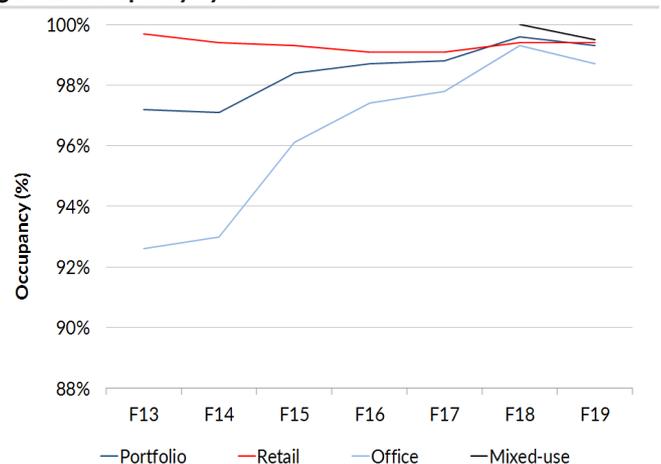
- **Retail exposure:** KPG is facing a soft economic environment and competitive pressures from e-commerce growth, coupled with the significant amount of Auckland retail development coming online at Commercial Bay and Westfield, Newmarket, which is impacting KPG's Auckland based malls.
- **CBD office 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 1. Sector and regional portfolio exposure

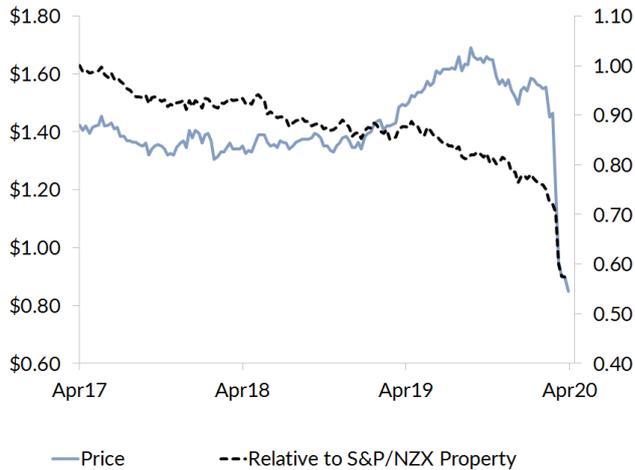
	Auckland	Other North Island	South Island	Total
Industrial	-	-	-	-
Office	22%	7%	-	30%
Retail	45%	17%	9%	70%
Total	68%	24%	9%	100%

Source: Forsyth Barr analysis, Company Reports

Figure 2. Occupancy by sector



Source: Forsyth Barr analysis, Company Reports

Figure 3. Price performance


Source: Forsyth Barr analysis

Figure 4. Substantial shareholders

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

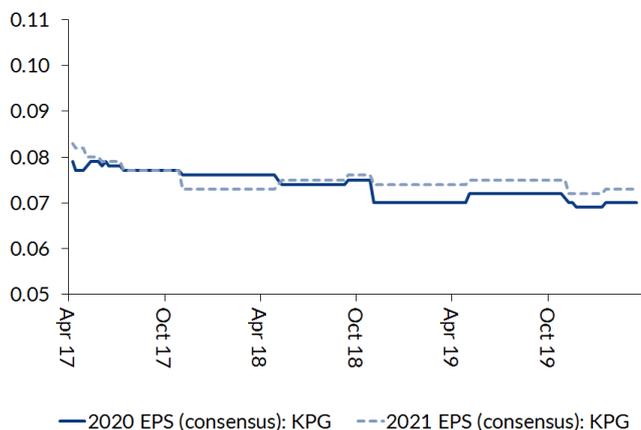
Source: NZX, Forsyth Barr analysis, NOTE: based on SSH notices only

Figure 5. International valuation comparisons

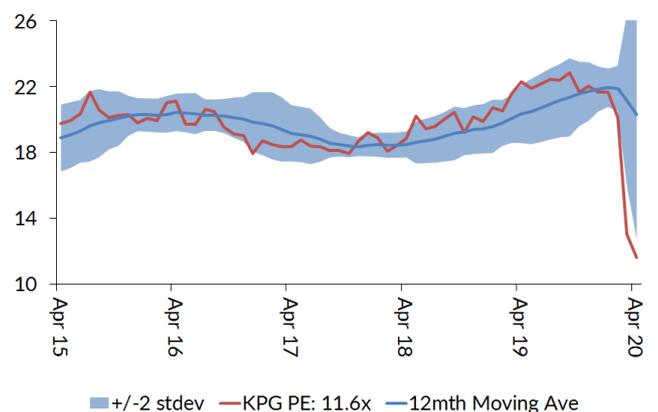
Company	Code	Price	Mkt Cap (m)	PE		EV/EBITDA		EV/EBIT		Cash Yld 2021E
				2020E	2021E	2020E	2021E	2020E	2021E	
Kiwi Property Group	KPG NZ	NZ\$0.85	NZ\$1,218	12.0x	11.7x	13.4x	12.5x	13.4x	12.5x	5.8%
Argosy Property *	ARG NZ	NZ\$0.84	NZ\$695	12.7x	12.2x	14.4x	13.5x	14.4x	13.5x	7.5%
Goodman Property Trust *	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	18.0x	17.0x	18.3x	15.5x	18.3x	15.5x	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	12.2x	14.2x	14.2x	14.2x	14.2x	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%
Compco Average:				18.6x	18.1x	18.0x	16.6x	18.0x	16.6x	5.7%
KPG Relative:				-36%	-35%	-25%	-25%	-25%	-25%	3%

EV = Current Market Cap + Actual Net Debt

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

Figure 6. Consensus EPS momentum (NZ\$)


Source: Forsyth Barr analysis

Figure 7. One year forward PE (x)


Source: Forsyth Barr analysis

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