

Metlifecare

FY20 Result — End of a Long Journey?

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NEUTRAL 

Metlifecare (MET) has reported an FY20 result largely in-line with last year's result, ahead of expectations, with small beats across the board. These results again highlight the strong performance by the aged care operators during and immediately after the COVID-19 lockdown period. However, near-term focus is squarely on the Scheme Implementation Agreement (SIA) where APVG (an entity owned by EQT Infrastructure) has agreed to acquire all MET's shares for NZ\$6.00 per share. The NZ\$6.00 offer represents a 5.5% discount to the midpoint of the current independent adviser range (NZ\$5.80–NZ\$6.90 per share) and a 1% premium to the current share price.

NZX Code	MET	Financials: Jun/	19A	20E	21E	22E	Valuation (x)	19A	20E	21E	22E
Share price	NZ\$5.92	NPAT* (NZ\$m)	90.5	72.6	69.8	85.6	EV/EBITDA	14.9	18.6	18.9	15.7
Target price	NZ\$6.00	EPS* (NZc)	42.4	34.1	32.7	40.1	EV/EBIT	15.8	20.0	20.6	16.9
Risk rating	High	EPS growth* (%)	3.8	-19.8	-3.9	22.7	PE	13.9	17.4	18.1	14.8
Issued shares	213.3m	DPS (NZc)	11.0	0.0	7.0	8.0	Price / NTA	0.9	0.8	0.7	0.7
Market cap	NZ\$1,263m	Imputation (%)	0	0	0	0	Cash div yld (%)	1.9	0.0	1.2	1.4
Avg daily turnover	1,314k (NZ\$7,460k)	*Based on normalised profits					Gross div yld (%)	1.9	0.0	1.2	1.4

Scheme timetable

The scheme is scheduled to be put to a shareholder vote at a special meeting on 2 October 2020. Should shareholders accept the scheme, which we expect, it is scheduled to be implemented in late October/early November 2020, provided all conditions under the SIA are satisfied. We have not changed our forecasts, acknowledging the new Scheme Implementation Agreement to acquire 100% of MET's shares for NZ\$6.00 announced in early July. Our target price remains in line with the scheme offer price of NZ\$6.00.

What did we learn from the results?

Fundamentals may not be in focus with respect to MET's near-term performance, however, the result re-enforced our view that the aged care sector has emerged from the COVID-19 crisis strong. MET's result was only the 2nd "full" COVID-19 impacts read through on calendar Q2, after SUM on 17 August, the reported numbers coupled with management commentary suggests that demand in June was largely back to normal while July and August have been above last year's level. Separately, we note that MET, much like SUM expects construction costs to reduce, although that was not quantified. MET expects the high construction costs experienced in FY19/20, combined with likely flattish price realisation, will weigh on development margins in FY21. This comment wasn't echoed in as much clarity by the other aged care operators.

Why do we think that the SIA will pass?

We take the view that the Scheme Implementation Agreement is likely to pass for three reasons; (1) the NZ Superannuation fund, with a 20% holding, has released a statement that they will vote in favour; (2) we estimate that the group of hedge funds that worked behind the scenes and in the media to garner support for a revised bid has the backing of a further c. 25% of share holders; and (3) acquisition through an SIA has a relatively low barrier to be approved: 75% of votes cast need to approve the SIA and over 50% of total shares on issue needs to vote in favour. The 2nd criteria is largely fulfilled with the known supporters, for the SIA to fail on the first criteria you need both a high degree of voting and for a (likely large) majority of those to vote against. If the SIA does not pass, we would expect a much smaller share price reaction than when the first deal fell through, as the sector has performed well since Nov 19.

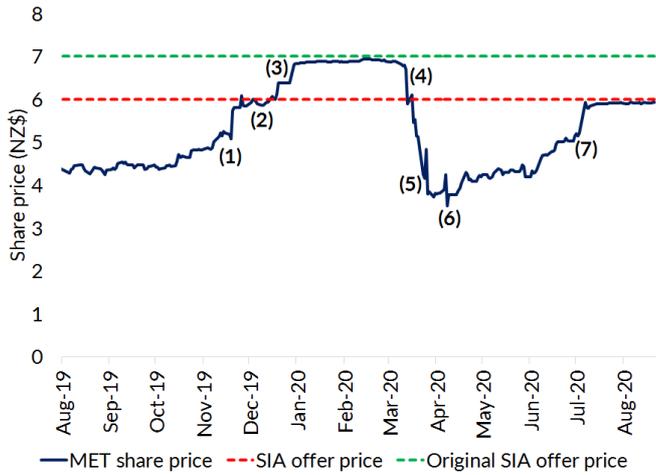
Metlifecare Limited (MET)

Priced as at 26 Aug 2020 (NZ\$)						5.92						
12-month target price (NZ\$)*						6.00	Spot valuations (NZ\$)					
Expected share price return						1.4%	1. Acquisition valuation					6.00
Net dividend yield						1.2%	2. n/a					n/a
Estimated 12-month return						2.6%	3. n/a					n/a
Key WACC assumptions						DCF valuation summary (NZ\$m)						
Risk free rate						1.30%	Total firm value					n/a
Equity beta						0.91	(Net debt)/cash					n/a
WACC						7.6%	Less: Capitalised operating leases					n/a
Terminal growth						1.5%	Value of equity					n/a
Profit and Loss Account (NZ\$m)						Valuation Ratios						
Sales revenue	2018A	2019A	2020E	2021E	2022E	2018A	2019A	2020E	2021E	2022E		
Normalised EBITDA	195.4	212.9	199.8	202.1	225.8	EV/EBITDA (x)	14.8	14.9	18.6	18.9	15.7	
Depreciation and amortisation	91.4	98.0	81.1	78.4	94.6	EV/EBIT (x)	15.6	15.8	20.0	20.6	16.9	
Normalised EBIT	(4.2)	(5.8)	(5.9)	(6.2)	(6.6)	PE (x)	14.5	13.9	17.4	18.1	14.8	
Net interest	87.2	92.2	75.2	72.1	88.0	Price/NTA (x)	0.9	0.9	0.8	0.7	0.7	
Associate income	(0.1)	(1.6)	(2.5)	(2.4)	(2.4)	Free cash flow yield (%)	-5.0	-9.0	3.5	0.5	1.6	
Tax	0	0	0	0	0	Net dividend yield (%)	1.7	1.9	0.0	1.2	1.4	
Minority interests	0	0	0	0	0	Gross dividend yield (%)	1.7	1.9	0.0	1.2	1.4	
Normalised NPAT	87.2	90.5	72.6	69.8	85.6	Capital Structure						
Abnormals/other	0	0	0	0	0	Interest cover EBIT (x)	>100x	56.7	29.6	30.5	36.7	
Reported NPAT	87.2	90.5	72.6	69.8	85.6	Interest cover EBITDA (x)	82.2	31.5	31.9	33.1	39.5	
Normalised EPS (cps)	40.9	42.4	34.1	32.7	40.1	Net debt/ND+E (%)	8.7	15.7	12.4	12.2	11.5	
DPS (cps)	10.0	11.0	0	7.0	8.0	Net debt/EBITDA (x)	1.5	2.8	2.9	3.1	2.5	
Growth Rates						Key Ratios						
Revenue (%)	2018A	2019A	2020E	2021E	2022E	2018A	2019A	2020E	2021E	2022E		
EBITDA (%)	5.3	8.9	-6.1	1.2	11.7	Return on assets (%)	2.7	2.6	2.1	1.9	2.1	
EBIT (%)	6.1	7.1	-17.2	-3.4	20.7	Return on equity (%)	5.9	6.1	4.4	4.0	4.7	
Normalised NPAT (%)	13.3	5.6	-18.4	-4.0	22.0	Return on funds employed (%)	5.7	5.4	4.1	3.7	4.3	
Normalised EPS (%)	6.1	3.9	-19.8	-3.9	22.7	EBITDA margin (%)	46.8	46.0	40.6	38.8	41.9	
Ordinary DPS (%)	24.2	10.0	-100.0	n/a	14.3	EBIT margin (%)	44.6	43.3	37.6	35.7	39.0	
Cash Flow (NZ\$m)						Operating Performance						
EBITDA	2018A	2019A	2020E	2021E	2022E	2018A	2019A	2020E	2021E	2022E		
Working capital change	91.4	98.0	81.1	78.4	94.6	Revenue (NZ\$m)						
Interest & tax paid	18.8	22.6	50.1	90.5	95.5	Village/care fees		59.9	65.4	67.4	69.1	73.4
Other	0.7	(0.6)	(2.5)	(2.4)	(2.4)	Management fees		55.2	58.9	64.5	71.3	78.5
Operating cash flow	111.0	119.9	128.6	166.5	187.6	Fair value m'ment in Investment Property (NZ\$m)						
Capital expenditure	(173.8)	(232.9)	(84.9)	(160.7)	(167.3)	Realised		78.7	88.4	67.7	61.5	73.7
(Acquisitions)/divestments	0	0	0	0	0	Unrealised		0	0	0	0	0
Other	1.1	(0.0)	0	0	0	Total revenue		195.4	212.9	199.8	202.1	225.8
Funding available/(required)	(61.7)	(113.1)	43.8	5.8	20.4	Key Drivers						
Dividends paid	(19.3)	(22.4)	0	(14.9)	(17.1)	Sales - new units		98	116	119	94	120
Equity raised/(returned)	0	0	0	0	0	Ave unit price - new sales (NZ\$000)		655	690	717	739	754
(Increase)/decrease in net debt	(81.0)	(135.4)	43.8	(9.1)	3.3	Sales - resold units		343	354	296	305	339
Balance Sheet (NZ\$m)						Portfolio						
Working capital	2018A	2019A	2020E	2021E	2022E	Apartment/units		4,391.0	4,478.0	4,548.0	4,688.0	4,838.0
Fixed assets	3,237.4	3,477.0	3,623.6	3,839.5	4,073.9	Beds		388.0	440.0	440.0	500.0	540.0
Intangibles	1.2	1.0	1.0	1.0	1.0							
Right of use asset	0	0	0	0	0							
Other assets	10.8	10.8	10.8	10.8	10.8							
Total funds employed	3,198.3	3,471.0	3,617.0	3,830.9	4,064.3							
Net debt/(cash)	140.5	275.8	232.0	241.1	237.8							
Lease liability	0	0	0	0	0							
Other liabilities	1,589.7	1,710.2	1,739.6	1,857.3	2,002.4							
Shareholder's funds	1,468.1	1,485.0	1,645.5	1,732.5	1,824.0							
Minority interests	0	0	0	0	0							
Total funding sources	3,198.3	3,471.0	3,617.0	3,830.9	4,064.3							

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

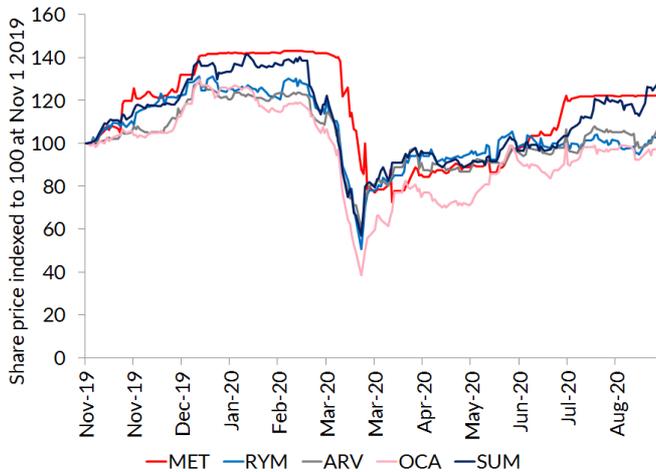
Charts of interest

Figure 1. The market is pricing in near certainty...



Source: Forsyth Barr analysis, Eikon

Figure 3. MET has outperformed average of listed peers by 13% since its undisturbed share price on November 1, 2019



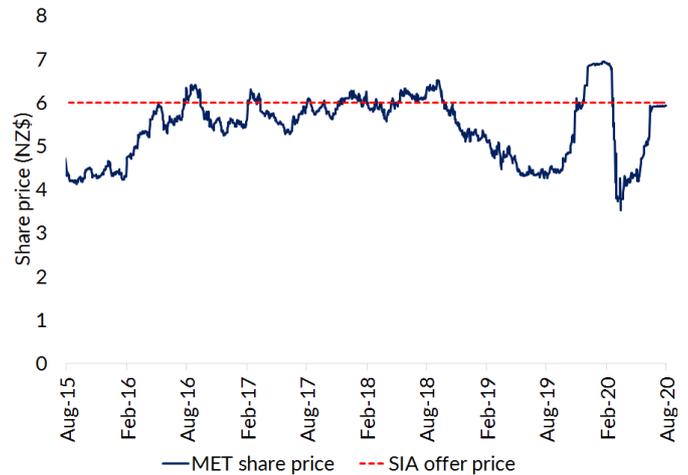
Source: Forsyth Barr analysis, Eikon

Figure 2. ...but we have been here before

Key	Date	Comment
1	20/11/2019	NBIO received from EQT
2	19/12/2019	Offer received at NZ\$6.50 per share
3	30/12/2019	MET board recommends scheme of arrangement of NZ\$7 per share
4	16/03/2020	Speculative commentary around material adverse change (MAC) clause
5	26/03/2020	Speculation continues around MAC
6	8/04/2020	APVG announces intention to terminate SIA based on COVID triggering MAC clause
7	6/07/2020	New NBIO received from EQT
n/a	2/10/2020	SIA voting date
n/a	Late October/early November	Scheme implementation date

Source: Forsyth Barr analysis

Figure 4. MET share price over last 6 years



Source: Forsyth Barr analysis, Eikon

Investment Summary

Metlifecare's (MET) share price has risen ~+60% since March following the announcement it had entered into a new Scheme Implementation Agreement (SIA) for the acquisition of all MET shares for NZ\$6.00 per share. The new agreement follows the cessation of the original SIA on April 8 as a result of COVID-19 activating a material adverse change clause. MET has received strong investor support for the new offer price with its largest shareholder (NZ Super at 19.96% interest) agreeing to vote in favour of the agreement. At present, the scheme will likely be implemented in late October/early November. NEUTRAL.

Business quality

- **Development expertise growing:** Development activity underway, including large greenfield projects, provides MET with an opportunity to demonstrate its capability, allowing further upside to our expectations.
- **Care expertise:** The expertise required to successfully operate in the aged care sector is a barrier to entry and a key focus for MET going forward.

Earnings and cashflow outlook

- **Lifting the build rate:** MET is focussed on developing new integrated villages and has a goal of 200+ units and beds. This has dialled back from a goal of 300+ units and beds per annum from FY20 onwards and had a significantly lower build rate in FY20 as it resets its programme. This may be delayed further with the recent COVID-19 lockdown.
- **Leveraged to Auckland market:** With 15 villages in Auckland, MET can capitalise on high house prices and significant levels of embedded value.
- **Recycling capital:** The occupational right agreement (ORA) structure provides MET with the ability to recycle capital into new developments and capture capital gains when units are resold.
- **Positive demographic trends:** There are currently 280,000 people in NZ aged 75 and over, a figure expected to more than double by 2035.

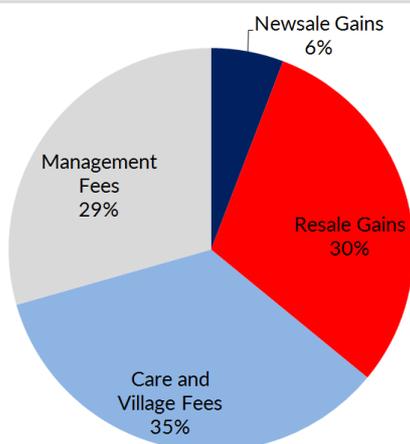
Financial structure

- **Balance sheet robust:** Contrasted with last cycle, MET has a low level of gearing at around 15%, providing ample capacity to workthrough its development pipeline or to provide cover should market conditions slow.

Risk factors

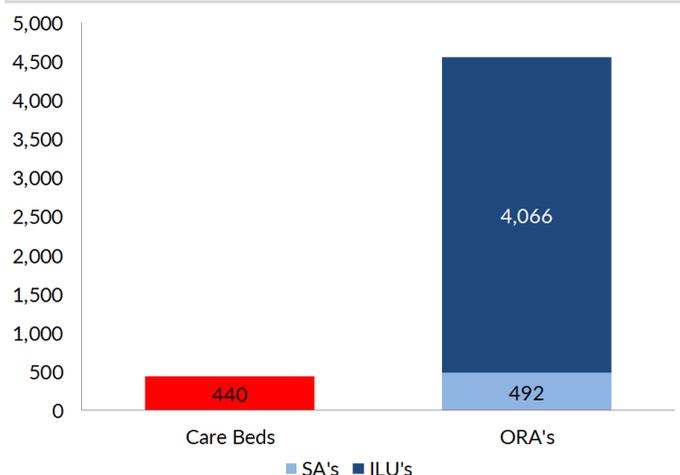
- **Housing market downturn:** Any significant downturn in the slowing Auckland housing market poses a threat to resales and new sales pricing. MET's existing portfolio remains weighted to independent living (lifestyle villages) with a small number of care beds and serviced apartments.
- **Oversupply:** The significant development pipeline in Auckland posed the threat of a short-term oversupply for retirement units, however, we expect this risk to reduce with the softening economic outlook.

Figure 5. FY20 revenue mix

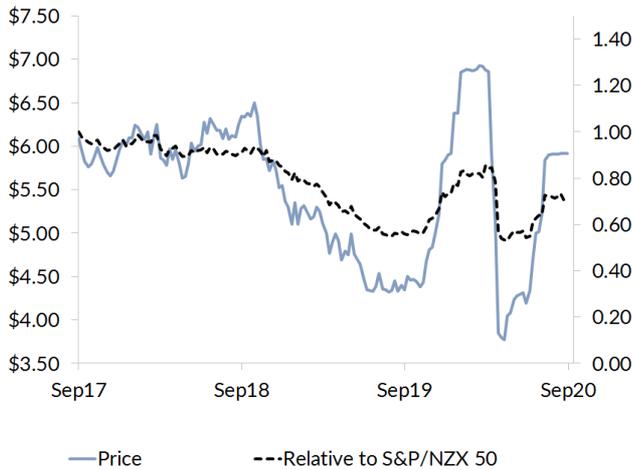


Source: Forsyth Barr analysis, Company reports

Figure 6. Portfolio as at 30 June 2020



Source: Forsyth Barr analysis, Company reports

Figure 7. Price performance


Source: Forsyth Barr analysis

Figure 8. Substantial shareholders

Shareholder	Latest Holding
New Zealand Superannuation Fund	19.9%
UBS	13.3%
Maso Capital Partners Limited	5.4%
JPMorgan Chase & Co. and its affiliates	5.3%
Credit Suisse	5.2%

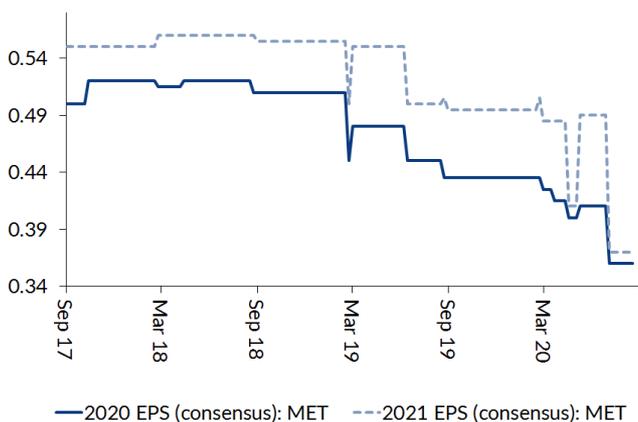
Source: NZX, Forsyth Barr analysis, NOTE: based on SPH notices only

Figure 9. International valuation comparisons

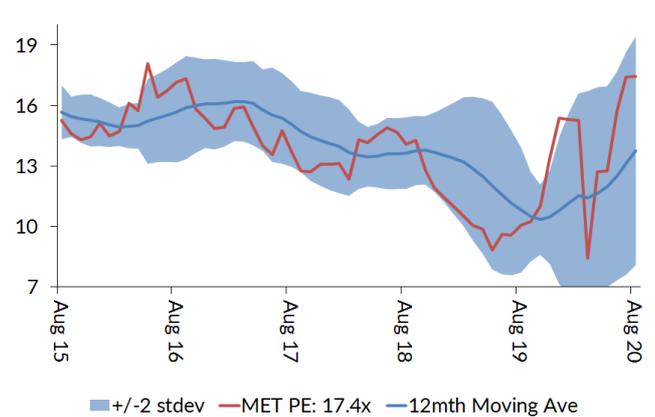
Company	Code	Price	Mkt Cap (m)	PE 2020E	PE 2021E	EV/EBITDA 2020E	EV/EBITDA 2021E	EV/EBIT 2020E	EV/EBIT 2021E	Cash Yld 2021E
(metrics re-weighted to reflect MET's balance date - June)										
Metlifecare	MET NZ	NZ\$5.92	NZ\$1,263	17.4x	18.1x	19.0x	19.6x	20.5x	21.3x	1.2%
RYMAN HEALTHCARE *	RYM NZ	NZ\$13.36	NZ\$6,680	27.7x	26.4x	28.9x	27.1x	32.0x	30.0x	1.9%
SUMMERSET GROUP *	SUM NZ	NZ\$8.61	NZ\$1,964	19.0x	18.2x	19.0x	17.7x	20.4x	18.9x	1.8%
OCEANIA HEALTHCARE *	OCA NZ	NZ\$1.03	NZ\$641	14.6x	13.1x	14.8x	13.1x	19.2x	16.8x	3.9%
ARVIDA GROUP LIMITED *	ARV NZ	NZ\$1.63	NZ\$884	17.1x	19.6x	19.2x	19.4x	21.6x	22.7x	2.9%
Compco Average:				19.6x	19.3x	20.5x	19.3x	23.3x	22.1x	2.6%
MET Relative:				-11%	-6%	-7%	2%	-12%	-4%	-55%

EV = Current Market Cap + Actual Net Debt

Source: *Forsyth Barr analysis, Bloomberg Consensus, Compco metrics re-weighted to reflect headline (MET) 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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