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Yovich & Co WEALTH MANAGEMENT

Yovich & Co. Market Update

4th December 2022

As at 2nd December	NZX 50G	All Ords	Shanghai	FTSE	Dow	NASDAQ	NZDAUD	NZDUSD	OCR
Previous Week	11382.56	7447.65	3101.69	7486.67	34347.03	11226.36	0.9246	0.6246	4.25%
Week Close	11641.85	7503.48	3156.14	7556.23	34429.88	11400.25	0.9432	0.6404	4.25%
Change	2.28%	0.75%	1.76%	0.93%	0.24%	1.55%	2.00%	2.54%	0.00%

Global share markets continued their positive momentum last week, with the NZ market up 2.28%, the US S&P 500 Index up 1.13%, the Australian market up 0.75%, and the UK market up 0.93%. Helping the forward momentum were investors' hopes of a downward path for inflation from here, and comments from Federal Reserve Chair Jerome Powell that suggest a 0.50% rate hike this month as opposed to a 0.75% hike. Inflation in Australia fell to 6.9% for the year to October, down from 7.3% in the previous month, and below forecasts.

US interest rates declined during the week, in line with growing belief in the market that inflation has now peaked. The 2-year Treasury rate was down 20bps to 4.25%, and the 10-year Treasury rate was down 14bps to 3.53%. NZ rates also declined, with the 2-year swap rate down 23bps to 5.00%, and the 5-year swap rate down 22bps to 4.40%.

Commodity prices increased during the week, with the Dow Jones Commodity Index up 1.29%, while the Brent Crude oil price also increased by 1.98% to just over US$85, after having fallen from US$98 a month ago. The DXY US Dollar Index continued to fall, down 1.37%, while the NZD gained strength after the 75bp OCR hike last week. This meant that the NZD climbed to above AUD$0.94 and above USD$0.64. With oil prices low compared to during the year, and the NZD gaining strength, this will help to keep imported inflation lower.

The ANZ Business Outlook survey saw confidence fall sharply in November, with the construction sector the most negative, and residential construction intentions at new lows. New home consents were down 12% YoY in October. Stats NZ said consents for standalone homes were down more than a quarter to 1,541. Apartments, at 239 approvals, were down 28%, and planned retirement village units were down 32% at 139 units.

NZ's Tourism Export Council is forecasting the number of international arrivals to exceed 2.1m in the year to May 2023, reaching 63% of pre-Covid levels for the same period, with strength from Australian, US, Britain, Singapore and Canada in particular.

The biggest movers of the week ending 2nd December 2022				
Up			**Down**	
Fisher & Paykel Healthcare	16.41%		Pacific Edge	-8.16%
Synlait Milk	10.03%		Stride Property	-5.84%
Arvida Group	9.57%		Genesis Energy	-3.35%
Oceania Healthcare	7.69%		Investore Property	-3.25%
Summerset Group	6.08%		Ryman Healthcare	-3.07%

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Sector Review – Aged Care / Retirement

The Aged Care / Retirement sector in NZ includes the four NZX-listed companies in the table below:

Company	Current Price	Consensus Target Price	Forward PE Ratio	Forward Dividend Yield
Arvida Group	$1.26	$1.80	9.90	4.70%
Oceania Healthcare	$0.84	$1.27	8.55	6.30%
Ryman Healthcare	$6.64	$10.66	12.73	3.20%
Summerset Group	$9.60	$14.42	12.70	2.30%

Last week we discussed the effect on the share market of the 75bp rise in the OCR, noting that the retirement sector saw heavy falls given that their business model is based largely on the prospect of the housing market. The housing market has declined by about 11% since November 2021 on average, and the RBNZ forecasts a decline of 20% from peak to trough. While this will have a negative effect on the retirement sector, it is not the only influence on the recent poor stock performance, and the decline in values has not been limited to recent weeks. The table below shows the return of the shares year-to-date in 2022, excluding dividends.

Company	Opening Price	Closing Price	% Return
Arvida Group	$1.97	$1.26	-36.0%
Oceania Healthcare	$1.34	$0.84	-38.1%
Ryman Healthcare	$12.25	$6.64	-45.8%
Summerset Group	$13.68	$9.60	-29.8%

The strong growth that we have seen from this sector over past years is due to the development of retirement villages and selling the units via Occupation Right Agreements. There has been huge demand for new villages as supported by demographics in NZ and Australia, and house price inflation has been a benefit to the sector. As such, the sector, especially Ryman and Summerset, have focussed on this growth and this has underpinned the growth in share prices.

With slowing and now negative house price inflation however, investors are focussing much more on sustainable cash flow generation from the other parts of the business, being village services, care, and deferred management fees (DMF), net of maintenance capex. Taking Ryman as an example, despite their half-year results showing a rebound in sales volumes following lockdowns and increased resale margins, the share price dropped significantly. The reason was the increase in debt, which has been driven by the continued focus on development growth taking greater levels of working capital, while at the same time paying a substantial cash dividend with little evidence of free cash flow. The result is higher interest costs, and concerns about interest coverage.

Sector Preferences

Ryman and Summerset remain our favoured exposures to the sector, due to their more attractive growth opportunities, despite the market's hesitancy of developing too aggressively. Ryman has recently introduced a Dividend Reinvestment Plan, which will go some way towards assisting its capital structure, however it may need to either increase its DMF in line with competitors, or lower its dividend in order to sustainably continue its development strategy at current levels.

While Ryman and Summerset face the headwinds of the declining housing market and higher interest costs, and medium-term growth will be affected by the need to realign development growth with cash flow, the recent falls in share prices justify a slower growth rate, and we believe that these prices represent good entry opportunities for what remain quality long-term holdings.

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Investment News

Kiwi Property Group (KPG.NZ) – Half-Year Net Property Income Up 6.3%

Kiwi Property Group's net property income for the first half of FY23 of $100.0m was up 6.3% from the first half of FY22. The increase was assisted by improved performance at Sylvia Park and the release of Covid-19 rental abatement accruals which were not required. Occupancy is at 99.7%, with a weighted average lease term of 4.6 years. The property portfolio value was $3.4b, down from $3.6b as a result of property devaluation. The quarterly dividend was in line with the full-year guidance for FY23 of 5.70cps for the full year.

Current Share Price: $0.93, **Consensus Target Price**: $0.97

Fisher & Paykel Healthcare (FPH.NZ) – Half-Year NPAT Above Guidance - Reactivates Dividend Reinvestment Plan

Fisher & Paykel Healthcare's half-year net profit after tax of $95.9m is down 57% compared to the previous half-year, but is a good result that has beaten previous guidance, given the strong sales during the Covid period. The result reflects stronger revenues. Guidance from the company is that revenue in the second-half of the year will be higher than in the first-half. The interim dividend of 17.50cps is an increase of 3%. The company has also reactivated the dividend reinvestment plan, with a 3% discount.

Current Share Price: $24.05, **Consensus Target Price**: $22.47

Arvida (ARV.NZ) – Half-Year Underlying Profit Up 46%

Arvida's half-year results show underlying profit of $38.9m, up 46% from the previous half-year, reflecting higher development and re-sale margins, but higher costs for care operations. Gearing remains conservative at 28% after the sale of residual land. The target for development in FY23 is 270 units, and FY24 guidance is for 250+ units. An interim dividend of 2.5cps was announced, in line with the previous half-year dividend in FY22.

Current Share Price: $1.26, **Consensus Target Price**: $1.80

Precinct Properties (PCT.NZ) Acquires Pre-Leased Wellington Property

Precinct Properties has acquired 61 Molesworth Street in Wellington, together with a new 24,000sqm office development project to be undertaken on the site. The office space has been leased to the NZ Ministry of Foreign Affairs and Trade (MFAT), and on completion will be a seismically resilient building across 11 levels. The expected total project total cost is around $250m, with the development expected to be completed in Q3 2025.

Current Share Price: $1.275, **Consensus Target Price**: $1.34