

Comvita

Honey in the pot

AGM

Comvita (CVT) is on its way to achieving NZ\$400m in sales revenue by FY20. It continues to benefit from locking in its honey supply and the investments it has made in enhanced production facilities and the rationalisation of its channels to market. Guidance for FY16 sales revenue of >NZ\$180m and an increase in NPAT of 35% has seen us increase our forecast FY16 EPS by 4.4% to NZ\$0.355/share and our valuation from NZ\$4.73 to NZ\$7.16. This, together with continued exploitation of operating leverage, should help the company achieve its stated+ objective of year-on-year increases in ROCE above the FY15 level of ~12%.

Year end	Revenue (NZm)	PBT* (NZm)	EPS* (c)	DPS (c)	P/E (x)	Yield (%)
03/14	115.3	12.6	25.5	12.0	22.5	2.1
03/15	152.7	16.3	29.9	13.0	19.2	2.3
03/16e	181.2	21.8	35.5	18.0	16.2	3.1
03/17e	215.5	28.3	46.9	22.0	12.2	3.8

Note: *PBT and EPS are normalised, excluding intangible amortisation, exceptional items and share-based payments.

CEO to step down

CEO Brett Hewlett will retire as CEO from 31 March 2016 and join the board before 31 March 2017. A replacement CEO is expected to be announced before the end of 2015. During his time at the company, Mr Hewlett delivered on a 10-year plan to set the business up for growth and achieve both vertical integration and streamlining of the supply chain. During his tenure, he broadened the management team to achieve the company's objectives.

Building earnings

Demand continues to remain strong and management is actively engaged in maximising product profitability in each of its markets. The process of determining the best path to market is ongoing and we expect that there will be continued emphasis on controlling the sales to the end-customer. This will assist the company in meeting its objective of growing earnings at a greater rate than growth in revenue. In FY15 revenue grew at 32% with growth in NPAT of 27.5% and earnings per share growth of 14.4%. Guidance for FY16 is for 18.7% revenue growth and an increase in NPAT of 35%.

Valuation: Increase to NZ\$7.16/share

The change in revenue and earnings growth assumptions to achieve sales of NZ\$400m by FY20 has increased our DCF-based valuation from NZ\$4.73 to NZ\$7.16. This includes NZ\$0.29 per share contribution from the investment in Derma Sciences. The achievement of this valuation and the implied premium to Capilano Honey (CZZ.AZX) and the NZ market is dependent on delivering to expectations and achieving above market growth rates in earnings per share.

Food & beverages

12 August 2015

Price **NZ\$5.74**

Market cap **NZ\$226m**

NZ\$/US\$0.65

Net debt (NZ\$m) at 31 March 2015 26.1

Shares in issue 39.4m

Free float 83.4%

Code CVT

Primary exchange NZX

Secondary exchange N/A

Share price performance



% 1m 3m 12m

Abs 31.7 39.0 57.9

Rel (local) 29.5 38.4 43.7

52-week high/low NZ\$5.7 NZ\$3.5

Business description

Comvita (CVT) is a manufacturer and marketer of honey-based products and fresh olive leaf extract products. The company products are used for health skin care and medical uses with approximately 80% of its products exported to Australia, Asia, North America and the UK.

Next event

Half year results November 2015

Analysts

Moir Daw +44 (0)20 3077 5700

Finola Burke +44 (0)20 3077 5700

consumer@edisongroup.com

[Edison profile page](#)

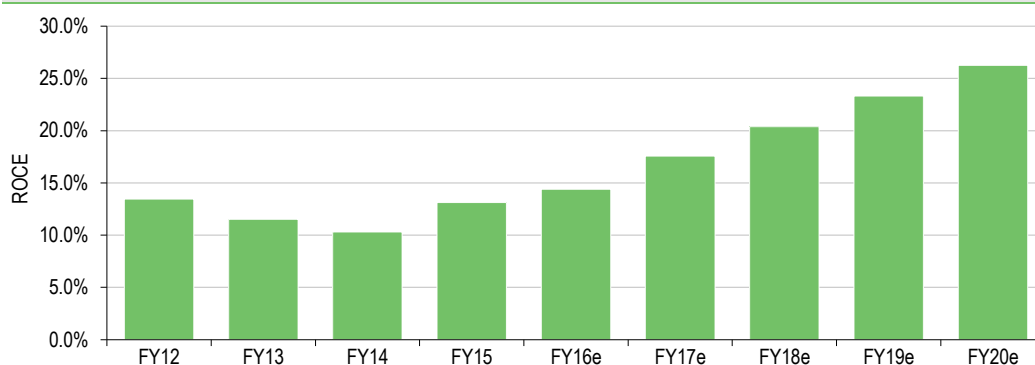
Driving ROCE

In FY15 ROCE increased to 12% from 10.8% in FY14. The journey to build year-on-year increases in ROCE includes the following strategies:

- honey supply: hives owned by CVT supply 30% of honey requirements and a further 20% is secured by contracts with third parties. CVT will continue to work on securing increasing amounts of supply;
- channels to market: determine the most cost-effective method per market;
- rationalising products: focusing on products that produce the highest returns;
- brand: building on the reputation as a premium brand;
- capital expenditure: most of the plant improvements have taken place already, which means that future capital expenditure is expected to be limited to maintenance capex;
- olive leaf extract: it is estimated that space capacity is between 60-70% and, with no lack of supply, there is the opportunity to produce more product and build the market;
- fixed-cost leverage: the EBITDA margin in FY15 was 14.9% compared with FY14 of 13.7%. We expect continued operating leverage with future EBITDA margins close to 16%;
- investment in skilled management team: the company has invested in a skilled management team capable of achieving the company's growth objectives; and
- marketing analysis and initiatives: the appointment of a chief marketing officer has led to market insight work to assist in refining the product offering, which could lead to increased profit margins.

ROCE history and our forecasts for expected future ROCE are set out in Exhibit 1 below.

Exhibit 1: Comvita – ROCE



Source: Comvita annual financial statement (reported), Edison Investment Research (forecasts)

Forecast changes

At the AGM the company was specific about the establishment of the strategy to achieve its FY20 revenue target of NZ\$400m. We have now incorporated this target into our forecasts. We have also increased growth in earnings per share and expect annual earnings per share growth in the forecast period to be at least 20%.

Exhibit 2: CVT – Forecast changes FY16

(NZ\$'000)	Previous	Revised	Variance
Revenue	176.3	181.2	2.7%
EBITDA	26.6	27.5	3.2%
EBITA	22.7	23.6	4.0%
Amortisation	(1.2)	(1.2)	N/M
Associate	-	1.1	N/M
Interest	(1.8)	(1.9)	2.9%
NPBT	20.9	21.8	4.3%
NPAT	13.4	14.0	4.4%
EPS	34.0	35.5	4.3%
DPS	14.0	18.0	28.6%
Revenue growth	11.1%	14.1%	3.0%
EBITDA %	15.1%	15.2%	0.1%

Source: Edison Investment Research

Derma Sciences shareholding

CVT holds 1.098m shares in Derma Science (NASDAQ:DSCI). The share price at 25 May 2015 of US\$6.71 gave a market value of NZ\$10.1m. The share price is currently US\$6.38, which results in a market value of NZ\$10.7m. This adds NZ\$0.29 to the DCF valuation of CVT.

Valuation

Comparative company

The most relevant peer for CVT is Australia-based Capilano Honey (CZZ.ASX). It sells 80% of its product in Australia, where it has >51% market share. It sells to the large supermarket chains and is a packager rather than a supplier. This means margins that are about 400bp below CVT's margins. CVT has superior growth prospects because it controls about 50% of its supply of raw honey and operates at the premium end of the market where it has pricing power. Our DCF of NZ\$6.87 (which excludes the value of the investment in Derma Sciences of NZ\$0.29/share) suggests a P/E of 16.2x in FY16 and a FY16 EV/EBIT multiple of 13.4x. CVT deserves to be trading at a premium to its peer, although the FY16 variance with Capilano Honey and the premium to the NZ market multiples requires the company to continue to deliver on its promises.

Exhibit 3: Capilano Honey

	2013	2014	2015e*	2016e	2017e
P/E (x)					
Comvita	21.6	20.8	19.2	16.2	12.1
Capilano Honey	6.1	11.3	18.1	15.8	14.4
EV/EBIT (x)					
Comvita	29.1	20.2	12.9	10.4	8.0
Capilano Honey	6.4	9.6	12.5	11.1	10.3
Yield (%)					
Comvita	2.5%	2.1%	2.3%	3.1%	3.8%
Capilano Honey	1.3%	1.3%	2.2%	2.6%	2.8%
EBITDA margin (%)					
Comvita	12.7%	13.7%	14.9%	15.2%	15.8%
Capilano Honey	10.2%	9.5%	10.9%	11.2%	11.3%
Sales growth (%)					
Comvita		13.9%	32.5%	18.6%	19.0%
Capilano Honey		19.4%	31.6%	9.1%	6.2%
ROCE					
Comvita	11.5%	10.3%	13.1%	15.0%	18.0%
Capilano Honey		5.6%	9.8%	11.8%	13.7%

Source: Edison Investment Research (financial data), Thomson Reuters (consensus data). Note: *2015 actual for Comvita year ended 31 March 2015, forecast for Capilano Honey for year ended 30 June 2015.

DCF valuation

Our DCF uses forecasts for 10 years, a terminal growth rate of 2.2% and a WACC of 10.7%.

Exhibit 4: Comvita – DCF

(NZ\$m)	2016e	2017e	2018e	2019e	2020e	2021e	2022e	2023e	2024e	2025e	
EBIT (total group incl. assoc)	21.3	27.7	35.0	44.7	57.1	61.8	66.8	68.1	69.5	70.9	
Tax	6.3	8.1	10.1	12.8	16.2	17.5	18.9	19.2	19.6	20.0	
Depreciation	4.9	5.3	5.4	5.6	5.9	6.1	6.4	6.4	6.4	6.4	
Amortisation	1.2	1.1	0.9	0.8	0.7	0.6	0.6	0.6	0.6	0.6	
Maintenance capex	3.1	3.8	4.1	5.2	5.3	5.4	5.5	6.4	6.4	6.4	
Expansionary capex	6.0	3.0	3.0	3.0	3.0	3.0	3.0	3.0	3.0	0.0	
Payment for acquisitions	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
Working capital movement	-2.9	-10.3	-13.9	-20.8	-23.9	-9.9	-10.7	-10.9	-11.1	-11.1	
Free cash flow	9.2	8.9	10.3	9.4	15.4	32.7	35.6	35.5	36.3	40.3	
	2016e	2017e	2018e	2019e	2020e	2021e	2022e	2023e	2024e	2025e	Terminal
Free cash flow	9.2	8.9	10.3	9.4	15.4	32.7	35.6	35.5	36.3	37.0	40.3
Discount	0.903	0.903	0.815	0.736	0.665	0.600	0.542	0.490	0.442	0.399	0.361
Discounted value	8.3	8.0	8.4	6.9	10.2	19.7	19.3	17.4	16.1	14.8	14.5
Terminal value	0	0	0	0	0	0	0	0	0	0	461.2
Sum of PV	129.1										
Terminal value at FY26e	461.2										
Discount factor	0.361										
PV of terminal value	166.3										
PV of enterprise	295.4										
Debt	24.5										
Net value for shareholder	270.9										
Number of shares in issue	39.4										
NPV	\$6.87										

Source: Edison Investment Research. Note: This DCF valuation excludes the market value of Comvita's holding in Derma Sciences, which is NZ\$0.29/share.

Exhibit 5: Financial summary

	NZ\$000s	2014	2015	2016e	2017e	2018e
31 March		IFRS	IFRS	IFRS	IFRS	IFRS
PROFIT & LOSS						
Revenue		115,283	152,702	181,171	215,539	261,709
Cost of Sales		(54,924)	(81,150)	(93,853)	(111,403)	(134,896)
Gross Profit		60,359	71,552	87,318	104,136	126,813
EBITDA		15,785	22,804	27,462	34,076	41,408
Operating Profit (before amort. and except.)		13,192	19,934	23,616	30,075	37,383
Intangible Amortisation		(1,527)	(1,777)	(1,195)	(1,056)	(933)
Exceptionals		0	0	0	0	0
Other		0	0	0	0	0
Operating Profit		11,665	18,157	22,421	29,019	36,450
Net Interest		(564)	(3,668)	(1,852)	(1,817)	(1,871)
Profit Before Tax (norm)		12,628	16,266	21,763	28,258	35,512
Profit Before Tax (FRS 3)		11,101	14,489	20,568	27,202	34,579
Tax		(3,129)	(4,245)	(6,582)	(8,705)	(11,065)
Profit After Tax (norm)		7,972	10,244	13,987	18,498	23,514
Profit After Tax (FRS 3)		7,972	10,244	13,987	18,498	23,514
Average Number of Shares Outstanding (m)		31.3	34.6	39.4	39.4	39.4
EPS - normalised (c)		25.5	29.9	35.5	46.9	59.6
EPS - normalised and fully diluted (c)		25.5	29.6	35.5	46.9	59.6
EPS - (IFRS) (c)		25.5	29.6	35.5	46.9	59.6
Dividend per share (c)		12.0	13.0	18.0	22.0	26.0
Gross Margin (%)		52.4	46.9	48.2	48.3	48.5
EBITDA Margin (%)		13.7	14.9	15.2	15.8	15.8
Operating Margin (before GW and except.) (%)		11.4	13.1	13.0	14.0	14.3
BALANCE SHEET						
Fixed Assets		93,277	106,615	110,644	112,396	114,587
Intangible Assets		40,558	43,112	41,917	40,862	39,929
Tangible Assets		39,174	48,417	52,541	54,057	55,756
Investments		13,545	15,086	16,186	17,478	18,901
Current Assets		55,469	93,107	90,182	101,202	116,222
Stocks		27,156	44,519	40,068	47,584	57,652
Debtors		22,362	28,895	30,445	36,221	43,980
Cash		2,865	19,420	19,396	17,125	14,317
Other		3,086	273	273	273	273
Current Liabilities		(21,276)	(32,418)	(26,634)	(29,583)	(33,531)
Creditors		(20,721)	(30,388)	(24,604)	(27,553)	(31,501)
Short term borrowings		(555)	(2,030)	(2,030)	(2,030)	(2,030)
Long Term Liabilities		(35,388)	(48,625)	(48,625)	(48,625)	(48,625)
Long term borrowings		(28,800)	(43,483)	(43,483)	(43,483)	(43,483)
Other long term liabilities		(6,588)	(5,142)	(5,142)	(5,142)	(5,142)
Net Assets		92,082	118,679	125,568	135,391	148,653
CASH FLOW						
Operating Cash Flow		11,347	19,409	24,578	23,734	27,529
Net Interest		(1,774)	(2,926)	(1,852)	(1,817)	(1,871)
Tax		(1,052)	(4,513)	(6,582)	(8,705)	(11,065)
Capex		(11,301)	(8,897)	(9,071)	(6,809)	(7,148)
Acquisitions/disposals		(5,024)	(23,557)	0	0	0
Financing		9,454	24,723	0	0	0
Dividends		(3,983)	(3,976)	(7,098)	(8,675)	(10,252)
Net Cash Flow		(2,333)	263	(24)	(2,271)	(2,808)
Opening net debt/(cash)		24,157	26,490	26,093	26,117	28,388
HP finance leases initiated		0	0	0	0	0
Other		0	134	(0)	0	0
Closing net debt/(cash)		26,490	26,093	26,117	28,388	31,196

Source: Comvita financial statements, Edison Investment Research

Edison, the investment intelligence firm, is the future of investor interaction with corporates. Our team of over 100 analysts and investment professionals work with leading companies, fund managers and investment banks worldwide to support their capital markets activity. We provide services to more than 400 retained corporate and investor clients from our offices in London, New York, Frankfurt, Sydney and Wellington. Edison is authorised and regulated by the Financial Conduct Authority (www.fsa.gov.uk/register/firmBasicDetails.do?sid=181584). Edison Investment Research (NZ) Limited (Edison NZ) is the New Zealand subsidiary of Edison. Edison NZ is registered on the New Zealand Financial Service Providers Register (FSP number 247505) and is registered to provide wholesale and/or generic financial adviser services only. Edison Investment Research Inc (Edison US) is the US subsidiary of Edison and is regulated by the Securities and Exchange Commission. Edison Investment Research Limited (Edison Aus) [46085869] is the Australian subsidiary of Edison and is not regulated by the Australian Securities and Investment Commission. Edison Germany is a branch entity of Edison Investment Research Limited [4794244]. www.edisongroup.com

DISCLAIMER

Copyright 2015 Edison Investment Research Limited. All rights reserved. This report has been commissioned by Comvita and prepared and issued by Edison for publication globally. All information used in the publication of this report has been compiled from publicly available sources that are believed to be reliable, however we do not guarantee the accuracy or completeness of this report. Opinions contained in this report represent those of the research department of Edison at the time of publication. The securities described in the Investment Research may not be eligible for sale in all jurisdictions or to certain categories of investors. This research is issued in Australia by Edison Aus and any access to it, is intended only for "wholesale clients" within the meaning of the Australian Corporations Act. The Investment Research is distributed in the United States by Edison US to major US institutional investors only. Edison US is registered as an investment adviser with the Securities and Exchange Commission. Edison US relies upon the "publishers' exclusion" from the definition of investment adviser under Section 202(a)(11) of the Investment Advisers Act of 1940 and corresponding state securities laws. As such, Edison does not offer or provide personalised advice. We publish information about companies in which we believe our readers may be interested and this information reflects our sincere opinions. The information that we provide or that is derived from our website is not intended to be, and should not be construed in any manner whatsoever as, personalised advice. Also, our website and the information provided by us should not be construed by any subscriber or prospective subscriber as Edison's solicitation to effect, or attempt to effect, any transaction in a security. The research in this document is intended for New Zealand resident professional financial advisers or brokers (for use in their roles as financial advisers or brokers) and habitual investors who are "wholesale clients" for the purpose of the Financial Advisers Act 2008 (FAA) (as described in sections 5(c) (1)(a), (b) and (c) of the FAA). This is not a solicitation or inducement to buy, sell, subscribe, or underwrite any securities mentioned or in the topic of this document. This document is provided for information purposes only and should not be construed as an offer or solicitation for investment in any securities mentioned or in the topic of this document. A marketing communication under FCA Rules, this document has not been prepared in accordance with the legal requirements designed to promote the independence of investment research and is not subject to any prohibition on dealing ahead of the dissemination of investment research. Edison has a restrictive policy relating to personal dealing. Edison Group does not conduct any investment business and, accordingly, does not itself hold any positions in the securities mentioned in this report. However, the respective directors, officers, employees and contractors of Edison may have a position in any or related securities mentioned in this report. Edison or its affiliates may perform services or solicit business from any of the companies mentioned in this report. The value of securities mentioned in this report can fall as well as rise and are subject to large and sudden swings. In addition it may be difficult or not possible to buy, sell or obtain accurate information about the value of securities mentioned in this report. Past performance is not necessarily a guide to future performance. Forward-looking information or statements in this report contain information that is based on assumptions, forecasts of future results, estimates of amounts not yet determinable, and therefore involve known and unknown risks, uncertainties and other factors which may cause the actual results, performance or achievements of their subject matter to be materially different from current expectations. For the purpose of the FAA, the content of this report is of a general nature, is intended as a source of general information only and is not intended to constitute a recommendation or opinion in relation to acquiring or disposing (including refraining from acquiring or disposing) of securities. The distribution of this document is not a "personalised service" and, to the extent that it contains any financial advice, is intended only as a "class service" provided by Edison within the meaning of the FAA (ie without taking into account the particular financial situation or goals of any person). As such, it should not be relied upon in making an investment decision. To the maximum extent permitted by law, Edison, its affiliates and contractors, and their respective directors, officers and employees will not be liable for any loss or damage arising as a result of reliance being placed on any of the information contained in this report and do not guarantee the returns on investments in the products discussed in this publication. FTSE International Limited ("FTSE") © FTSE 2015. "FTSE®" is a trade mark of the London Stock Exchange Group companies and is used by FTSE International Limited under license. All rights in the FTSE indices and/or FTSE ratings vest in FTSE and/or its licensors. Neither FTSE nor its licensors accept any liability for any errors or omissions in the FTSE indices and/or FTSE ratings or underlying data. No further distribution of FTSE Data is permitted without FTSE's express written consent.