

Primary Health Properties

Accelerating UK & Ireland expansion

BUY (from HOLD)

Target price 120p | Published price 113p

We update our forecasts following PHP's expanded £115m equity placing. The raise provides firepower to deliver the group's ~£155m acquisition pipeline and is marginally accretive to NAV, but dilutive to earnings in the current year. The equity raise places PHP in a strong position to further consolidate the UK primary health property market, accelerate expansion in Ireland and drive further economy of scale benefits within the business. PHP offers long-term predictable returns with low relative risk. The shares trade at a 9% premium to NAV, with a P/E of 22x and DPS yield of 4.8%. We upgrade our recommendation to BUY from HOLD, given upside to our unchanged 120p TP and the benefits of the placing.

£115m gross placing at a 7% NAV premium

We marginally upgrade our NAV forecasts to reflect PHP's expanded £115m gross equity raise at 108p per share, 7% above the last reported NAV (101p). The raise provides firepower to deliver the group's ~£155m acquisition pipeline of primary healthcare properties, but will be dilutive to earnings in the current year by ~6%, reflecting the timing of likely acquisition spend. We make no change to our dividend forecasts.

Figure 1: Summary forecast change

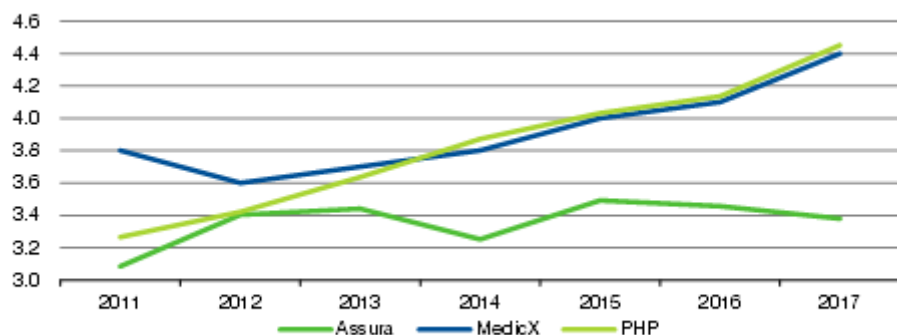
	2018E			2019E			2020E		
	Old	New	Change	Old	New	Change	Old	New	Change
Key assumptions									
True equivalent yield	5.0%	5.0%	0bp	5.0%	5.0%	0bp	5.0%	5.0%	0bp
LFL rental growth	1.4%	1.4%	0bp	1.7%	1.7%	0bp	2.1%	2.1%	-1bp
Income statement									
Gross Rental Income	76.5	76.4	-0%	80.0	82.6	+3%	86.5	89.8	+4%
Growth (%)	5.5%	5.4%	-14bp	4.5%	8.1%	+361bp	8.1%	8.7%	+63bp
Net Operating Income	75.4	75.3	-0%	78.7	81.3	+3%	85.1	88.4	+4%
NOI margin (%)	98.5%	98.5%	+0bp	98.5%	98.5%	0bp	98.4%	98.4%	0bp
EBITDA	67.2	67.0	-0%	69.8	72.3	+4%	76.3	79.4	+4%
PBT, adj	34.1	36.0	+6%	38.9	44.6	+15%	40.9	47.7	+16%
EPRA EPS (p)	5.5	5.2	-6%	5.7	5.6	-1%	5.9	6.0	+1%
DPS (p)	5.4	5.4	0%	5.6	5.6	0%	5.7	5.7	0%
Other									
EPRA NAV	638.9	752.6	+18%	714.6	828.4	+16%	726.3	841.3	+16%
Net (debt) / cash	(807.0)	(723.5)	-10%	(814.2)	(755.6)	-7%	(882.0)	(857.4)	-3%
EPRA NAV (p)	102.9	103.5	+1%	104.0	104.4	+0%	105.4	105.7	+0%
LTV (%)	55.4%	48.7%	-12%	52.9%	47.4%	-10%	54.5%	50.2%	-8%

Source: Liberum

Proceeds to facilitate selective expansion

The proceeds will be used to fund an existing acquisition pipeline of ~£80m in the UK and ~€80m in Ireland. While PHP's acquisition run-rate may be below its larger peer Assura, PHP is focused on acquiring larger practices only; a strategy which we believe will drive superior value in the long term.

Figure 2: Average value per asset (£m)



Source: Liberum, Company

PHP now also owns three properties in Ireland providing an additional attractive market for growth given similar favourable demand and supply dynamics to the UK (ageing population, budgetary constraint on healthcare and an ageing primary care infrastructure). This is backed by a similar low risk, high covenant income stream (largely backed by the Health Service Executive). In contrast to the UK, purchase yields in Ireland have seen less compression and hence represent greater opportunity to sustain higher returns.

As PHP expands we also see further opportunity for it to drive further economy of scale benefits.

LTV falls towards low end of 45-60% target range

Our forecast changes lower LTV from 55% to 49%, towards the low end of the group's 45-65% target. While this may still be high in a sector context, we believe primary care REITs should operate with above average levels of financial gearing given the low risk nature of their income profiles.

Taking share in a low-risk, growth market

We expect PHP's portfolio to benefit from long-term structural growth, driven by a growing and ageing UK population coupled with efforts to improve the efficiency and cost effectiveness of the NHS by expanding the scope of services provided by GPs. The majority of the existing primary care estate is considered unfit for purpose to meet this growing demand. Leases are long-dated and contain upward only rent review provisions. The shares trade at a 9% premium to our CY18E NAV, with a P/E of 22x and DPS yield of 4.8%. We maintain our 120p TP, with the accretion of the placing offset by recent moves in our cost of equity. Given upside to our unchanged target price we move to BUY from HOLD.

Figure 3: Summary Financials & Valuation

Valuation Summary (CY)	2017A	2018E	2019E	2020E
P/NAV (x)	1.12	1.09	1.08	1.07
P/E (x)	21.9	21.8	20.1	18.8
Div Yield (%)	4.6%	4.8%	4.9%	5.0%
EV/Sales (x)	19.5	19.7	20.0	19.5
EV/EBITDA (x)	22.5	22.5	22.9	22.1
EV/EBIT (x)	22.5	22.5	22.9	22.1
FCF Yield (%)	3.3%	4.5%	4.8%	5.2%
Financials (FY - Dec y/e)	2017A	2018E	2019E	2020E
Gross rental income (£m)	72.5	76.4	82.6	89.8
Net rental income (£m)	71.3	75.3	81.3	88.4
Gross to net (%)	98.3%	98.5%	98.5%	98.4%
Adj. EBITDA (£m)	62.6	67.0	72.3	79.4

EBITDA margin (%)	86.3%	87.7%	87.5%	88.4%
Adj. EBIT (£m)	62.6	67.0	72.3	79.4
EBIT margin (%)	86.3%	87.7%	87.5%	88.4%
Adj. net Interest (£m)	-31.6	-31.0	-27.7	-31.8
Adj. PBT (£m)	31.0	36.0	44.6	47.7
Adj. EPRA EPS - diluted (p)	5.2	5.2	5.6	6.0
DPS (p)	5.3	5.4	5.6	5.7
Cover (x)	1.0	1.0	1.0	1.1
Diluted EPRA NAV (p)	100.7	103.5	104.4	105.7
Net cash/(debt) (£m)	-732.7	-723.5	-755.6	-857.4
LTV (%)	53%	49%	47%	50%

Source: Liberum, Company

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