STOCKS DOWN UNDER

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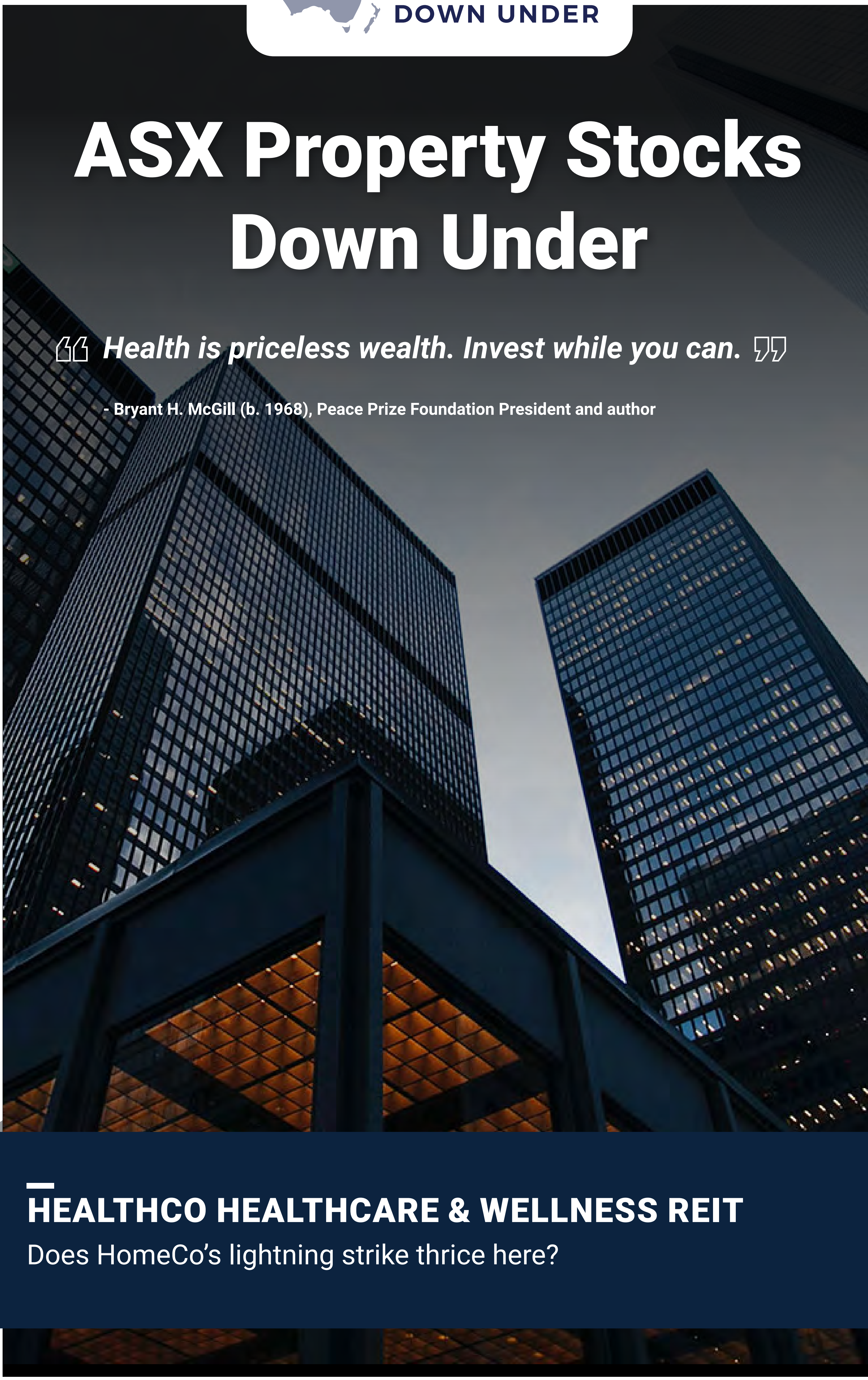
ASX Property Stocks Down Under

"Health is priceless wealth. Invest while you can."

- Bryant H. McGill (b. 1968), Peace Prize Foundation President and author



HEALTHCO HEALTHCARE & WELLNESS REIT

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Stocks Down Under rating: ★ ★

ASX: HCW
Market cap: A$558.7M

52-week range: A$1.61 / A$2.40
Share price: A$1.715

After real estate investor Home Consortium (ASX: HMC) listed itself in 2019, it listed its Daily Needs REIT (ASX: HDN) in 2020, followed by the Healthcare and Wellness REIT (ASX: HCW). Raising $650m at $2 per share, HCW was one of the biggest ASX IPOs of 2021 and the biggest real estate float since Charter Hall Long WALE REIT (ASX: CLW) in 2016. Initially it made a solid gain on debut, particularly for an ASX REIT, but shares have come down in the past six months and have lagged ever since. Why have shares declined and should investors bet on a bounce back?

Share price chart

Source: Tradingview

In a good place at a good time

HCW is directly managed and 20% owned by Home Consortium. It is targeting five key subsectors which have a total addressable market of $218bn – life sciences & research, hospitals, aged care, primary care & wellness and childcare. In listing HCW, Home Consortium wanted to capitalise on megatrends, such as Australia's aging population and private healthcare. These will require increased investments on healthcare properties - the company reckons $87bn will be needed over the next two decade and funding is indeed coming. For instance, public hospital funding to FY25 will be $134bn, childcare subsidies to FY24 will be $40bn and 80,000 new aged care places will be created by 2030.

HomeCo also hoped to offer something different to REIT investors who have traditionally had lean pickings beyond retail and office investments. It claims to be the only ASX REIT with an exclusive focus on healthcare, although we note some other REITs focus on childcare properties, including Arena REIT (ASX: ARF) and Charter Hall Social Infrastructure REIT (ASX: CQR).

All up, HCW has 40 properties with a fair value of $700m. 50% of HCW's properties are in Queensland, while 29% are in NSW, 18% in Victoria and the remainder in WA. Its biggest tenants include GenesisCare, the Commonwealth and Queensland governments and G8 Education (ASX: GEM). Childcare is its largest subsector by income split at 29%, followed by primary care & wellness properties with 23%. Life sciences, private hospitals and aged care account for 17%, 16% and 7% respectively.

Only days after listing, HCW bought $200m of properties, including the Metro Childcare portfolio, Proxima Southport and Stage One of the Camden Health and Innovation Precinct (the George Private hospital). And it upgraded its NTA to $1.94 per share as well as its occupancy to 98%, cash collection to 100%, WALE to 10 years and full year FY22 FFO (Funds From Operations) to 5.0c. In 1HY22 it achieved FFO of $5.8m, which was 1.8 cents per unit and the company had a net cash position of $56m.

The devils are in the details

Sounds like a good opportunity, doesn't it? But of course, each and every ASX company will go to great lengths to make itself sound like a good opportunity to investors. The market may have different views and seemingly it has in respect of HCW, sending it more than 15% below its IPO price. It appears a lower support level is established at $1.65, but it is too early to say the stock is in an uptrend yet.

We think ESG investors might like this REIT because it is targeting Net Zero emissions by 2028 and is in an ESG friendly space to begin with. However, there are three issues that prevent this company from being a four-star company, in our view.

The first is HCW's valuation. Admittedly, it now trades at a discount to its NTA of ~17%, but it is still high on a forward P/FFO basis at 33.2x. HomeCo Daily Needs REIT (ASX: HDN) trades at just 14.2x and Home Consortium at 19.3x. And looking to HCW's childcare peers, Arena REIT (ASX: ARF) is trading at 26.7x and Charter Hall Social Infrastructure REIT (ASX: CQE) at 20.1x.

Secondly, we note that a significant portion of its future earnings are reliant on construction projects. We can forgive investors who fear supply chain challenges could mean these projects will be delayed. And although HCW's projects are on track at the moment, they still are some months away from completion with Stage 1 of the Camden Health & Innovation Precinct scheduled for completion in 2HY22 and Southport scheduled for the end of FY23. Stages 2 and 3 of Camden aren't scheduled for completion until FY25. Still, HCW's development pipeline will need >$500m in capital investment over time and that's assuming nothing goes wrong in relation to the supply chains, labour shortages or other construction problems. It will need more financing than it has now, either through equity or debt. Meanwhile, there are other REITs with well-established portfolios that will not require capital and, consequently, are safer havens for investors.

Thirdly, lower liquidity. Although HCW is not illiquid in any sense of the word, it has lower liquidity compared to HDN and HMC, arguably due to the factors above.

We think this REIT is one to watch in the years ahead. Investors are likely to be pleased with HCW's announcement yesterday that its portfolio valuation rose by $25m net of capital expenditure which was 4.1%. However, it was behind HDN which made a 4.6% gain (see our 9 March edition for more information on HDN). Ultimately, for the reasons outlined, we think it's a two-star investment at the moment.

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Stocks Down Under gives you an information advantage to better invest and trade in ASX-listed stocks!