

Key data

Code	ZGL
Current price	NZ\$6.50
FY22 PE ratio	4.7x
Gross div yield	24.5%
Market cap (m)	NZ\$1,191m

Zespri

5-year Outlook and 2022 wrap

Zespri annual 5-year Outlook

While acknowledging short-term headwinds and challenges facing the industry, Zespri remains bullish about the mid to long term prospects for the industry. Zespri forecasts an increase in total NZ Supply of Class 1 (export) kiwifruit from 164m trays in the 2022 harvest season to 229m trays in 2027. This is equivalent to a 39% increase in volume and includes commercial volumes of Zespri RubyRed from 2025.

The macro-level trends for the next five years include several positive factors in terms of consumer and consumption trends that support kiwifruit sales:

- **Population changes:** a burgeoning global middle class will lead to increased disposable income and willingness to try new and different foods.
- **Consumer and shopper trends:** health and wellbeing, environmental sustainability, e-commerce, and growth in global snacks are all trends that place Zespri in a strong position as a 'healthy' food brand.
- **Fruit category trends:** the global fruit category is forecast to grow at a CAGR of 5.8% over the next five years. Demand for kiwifruit is strong and growing, with more people wanting to buy kiwifruit because of its taste, health benefits, and because it's grown in a way which is good for the environment and its communities.
- **Growth opportunity for Zespri Kiwifruit:** there is significant headroom for growth with kiwifruit representing less than a one percent share of the global fruit bowl.

Zespri Green Kiwifruit (Hayward)

Supply of Green is forecast to decline to 55m trays in 2027/28, down from 60m trays in 2022/23. This is in part due to the ringfencing of 600 hectares of SunGold licence over the next 3 years (200 ha per annum) for Green cutover. Converting Green to Gold3 will have the benefit of increasing supply of the higher value Gold3 fruit, while the corresponding decrease in Green volume will help offset short term supply chain and logistical challenges (picking/packing, storage and transport). A reduction in Green supply will also benefit those remaining growers, where a higher sale price will help combat rising orchard costs.

SunGold 2023 licence release

Zespri has approved the release of 350 hectares of SunGold Kiwifruit and 150 hectares of RubyRed Kiwifruit licence in 2023. New in 2023 is the ringfencing of 200 hectares of SunGold licence for Green cutover. The 200 hectares cutover pool auction will be run first, with the 150 hectares unrestricted pool auction held after. Eligible green growers will be able to bid in either or both pools, effectively having two chances to bid.

Zespri also announced an update to the licence release mechanism. In response to feedback from growers, the licence bidding mechanism will change from closed tender to an ascending price open auction. The revised auction format aims to address key grower concerns around price equity (all bidders pay the same price), and transparency (knowing what 'the market' is doing during the process).

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We expect 2022 will mark a high point for SunGold pricing (median price of \$801k/hectare). We analysed a payback period of 5-6 years for Gold3 and calculated a price range per hectare of \$432K to \$742.5K. We have used a mid-point value of \$590k/hectare to estimate future sales of Gold3. While we haven't revised our estimate for the 2023 auction, we expect the cutover pool will be priced lower than the unrestricted pool. The auction is scheduled to be run in late April - early May. With the attractive economics of SunGold, we expect demand for the cutover pool will be high and both auctions to be fully subscribed.

Hi-cane

In December, the Environmental Protection Authority (EPA) announced its revised recommendation into the use of hydrogen cyanamide, commonly known as Hi-Cane. The EPA continues to recommend a ban on Hi-Cane, but now proposes this ban in ten years' time instead of its original recommendation of five years. While a 10-year period does give more time to find alternative Green varieties and/or alternative budbreakers, a ban will have a significant impact on growers and the industry. Zespri and NZKGI both oppose the ban and continue to build a case for maintaining the use of Hi-Cane.

Kiwifruit Breeding Centre

Established in 2021 as a dedicated joint venture company in partnership with Plant & Food Research, the Kiwifruit Breeding Centre is focused on speeding up the development of new varieties to create more value for growers and attract new consumers to the category through better products. This includes consideration of a new future Green cultivar. Several new Green varieties were approved for trial with growers in 2022. The earliest these cultivars would likely be available commercially is in 2027. If Hi-Cane is banned, it will have profitability implications for Green growers in some regions. There is an opportunity for Zespri to find a new Green variety which will provide growers a viable alternative should the EPA's recommendation stand.

ZGS Update / Industry alignment

While there was strong support for the expansion of Gold3 planting overseas, it was ultimately voted down as it didn't meet the required support of 75% of growers. We had forecast that a successful vote here could have added \$0.90-1.74 to ZGL's share price based on current margins, so the outcome is disappointing for shareholders.

This is the 2nd Producer Vote in a row that has been voted down. With less than 50% of growers now being shareholders, industry alignment between growers and Zespri shareholders is an issue. As the issuing of new shares is currently an in-depth process requiring a Product Disclosure Statement each time, Zespri will likely look to list on the NZX (2H 2023) and become an NZX Continuous Issuer (1H 2024). Having this mechanism in place will provide options for alignment such as the stapling of shares to future licence releases, or to introduce a dividend reinvestment plan.

Quality

Quality costs for the 2022 growing season are around \$500 million, illustrating the importance of addressing fruit quality issues quickly. Of longer-term concern is the market impact of the quality issues and the effect on the Zespri brand, and consumer/retailer confidence. In response to fruit quality issues experienced, a seven-point quality action plan was launched by the Industry Advisory Council (IAC) in October.