COMPANY RESEARCH
31 JANUARY 2024

Zespri
2024 Licence Release (FY25)

ZGL has approved the release of 250 hectares of SunGold Kiwifruit in CY2024 (FY25). This is a reduction from the 500 hectares signalled by ZGL in the 2023 Outlook document published in December 2022. ZGL plans to release 350ha in CY2025, and then 350 to 500ha from CY26-28, subject to annual review.

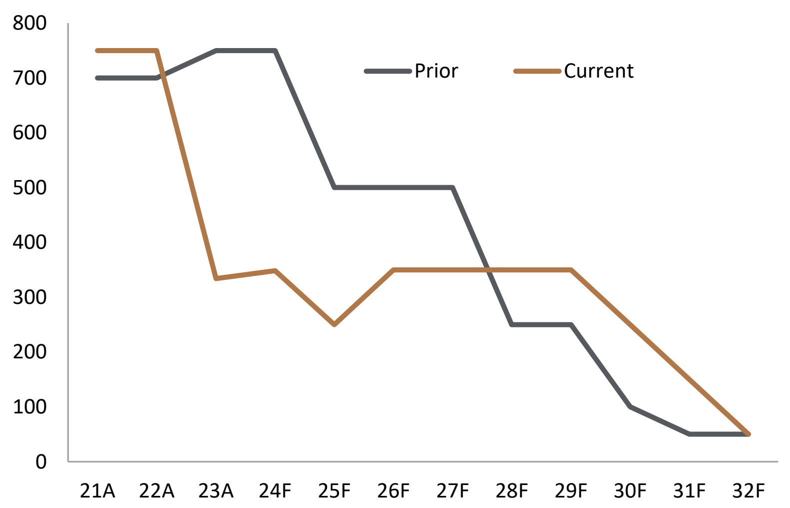
ZGL will not release any RubyRed Kiwifruit licence in CY2024. The Board expects to release 100 hectares of RubyRed Kiwifruit licence in CY25 and expects to release between 100-300 hectares each year from CY26 through to CY28, subject to annual review.

Lower for longer

We forecast that ZGL will release 2,100 hectares of SunGold through to FY2032. Previously we expected the release schedule would be higher hectares in the early years before tapering off around FY2028.

After two difficult seasons, rising interest rates and rising on-orchard costs, we expected CY2022 would mark a high point for SunGold pricing (median price of $801k/hectare). We analysed a payback period of 5-6 years (from full production) for Gold3 and calculated a price range per hectare of $432K to $742.5K. If ZGL were to release 500 hectares or above, we expect the price per hectare to fall below the mid-point of our calculated range. By keeping supply lower for longer, we believe the price will remain around the mid-point or higher ($590k). We have updated our forecast for licence releases to 350 hectares from FY26 – FY29, with a more gradual tapering to 50 hectares in FY32.

SunGold Hectares Released Forecast



Source: Company data, Craigs Investment Partners

Despite a further reduction in released hectares this year, potentially resulting in higher auction prices, we maintain our estimate for Gold3 at $590k/hectare. Anticipating full subscription for the CY2024 licence release, we project revenue from the Gold3 tender process, which will contribute to FY25 results, to be c$147.5m, reflecting a 30% decrease from 2023.

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Key data

Code	ZGL
Current price	NZ$4.50
FY23 PE ratio	3.5x
LTM net div yield	18.5%
Market cap (m)	NZ$825m

Private Wealth Research

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NZX Firm

Updated 5-year Outlook

Compared with ZGL's outlook released in 2023, ZGL has trimmed its total volumes with the most significant decline observed in green and offshore volumes, while SunGold experiences a comparatively modest decrease. ZGL expects FY28 volumes of c260m trays. ZGL expects c208m from NZ (145m SunGold) and c52m non-NZ supply. ZGL maintains its 2025 (FY26) revenue goal of $4.5bn, but on volumes of 230m trays (was 265m).

ZGL has also lowered target demand to 316 million trays by 2028 (was 398m) and 458m trays by 2033 (was 611m). The reasons considered by ZGL Management for the lower future demand forecasts versus prior year were:

- Weather events and quality issues led to lower volumes in 2022 and 2023.
- ZGL captured less demand than anticipated in those seasons, which has an impact on future growth being captured.
- Post-COVID-19, the macroeconomic environment with high inflation has impacted shopper disposable income and demand for premium products.

The lower demand forecast is important as ZGL likes to build market demand ahead of supply and will reduce/increase the number of hectares released, as they have done in 2024, to maintain the balance between supply and demand.

Dividends

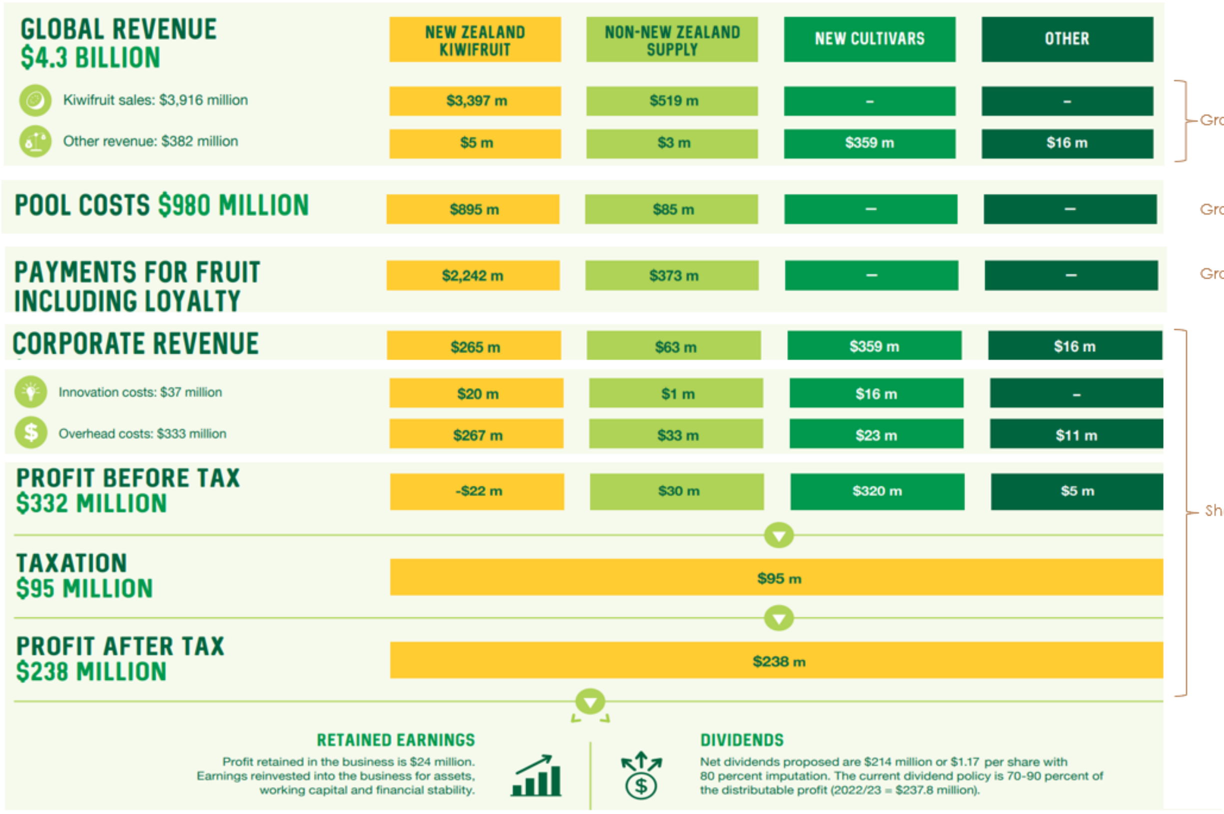
ZGL has four primary streams of income which flow through to dividends.

1) **New Zealand Kiwifruit:** ZGL's core business is the the purchase, marketing, development of markets for New Zealand grown kiwifruit for export, and kiwifruit research and development.
2) **Offshore Kiwifruit:** To maintain the competitive advantage of NZ kiwifruit in global markets, through the Zespri Global Supply (ZGS) program, ZGL allows offshore producers to grow Zespri-owned Gold3 during NZ's off-season. ZGL purchases this Gold3, along with Hayward that meets its strict quality and safety standards, and markets it for a profit.
3) **Zespri Plant Variety Right royalty income:** When a new variety of kiwifruit is commercialised, there is a royalty paid to ZGL. For the varieties that exist today, the royalty (which is charged to grower pool costs) is 3 percent on net sales. Net sales is defined as Gross Sales of kiwifruit less promotional rebates, claims and discounts. This royalty is made up of two components: 1.35 percent of this royalty is paid to Plant & Food Research and 1.65 percent of the royalty income goes to ZGL. ZGL has the PVR Rights in NZ to SunGold until Nov 2038 (USA until 2030).
4) **Zespri Plant Variety Right licences:** ZGL limits the supply of Gold3 by controlling the allocation of new hectares through auctions, with high demand leading to prices for a Gold3 licence reaching as high as $801,000 (including GST) per hectare.

Because ZGL must act in the best interests of NZ growers as well as their shareholders, it has agreed with NZ growers to target an EBIT margin of 1% on New Zealand Kiwifruit sales, which ensures that most of the returns for NZ kiwifruit are returned to growers through fruit and service payments. ZGL does not have this same relationship with offshore growers and targets an EBIT margin of 3-5% on offshore Kiwifruit. This means that more of the returns for Offshore Kiwifruit are returned to ZGL shareholders through dividends.

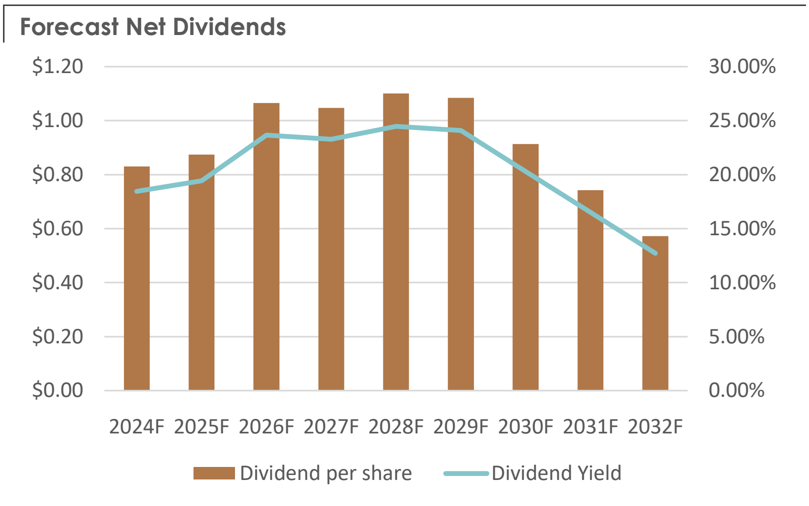
For FY23 ZGL made a loss of $22 million on $3.4 billion revenue for NZ Kiwifruit (normal profit would be c$35 million). ZGL made $30 million for Non-NZ Supply on revenue of $519 million. For FY23, the PVR royalty income to ZGL was $46.7 million. With little overheads/costs for this income stream, most of the PVR royalty income passes to ZGL shareholders through dividends. The largest contributor towards dividend is PVR licence sales. The money from PVR licence sales gets paid out in an interim dividend each August.

Zespri FY23 Profit by Segment



Source: Company data, Craigs Investment Partners

ZGL has a dividend policy of 70% to 90% payout. While the historical payout ratio has typically hovered between 80% and 85%, it increased to 90% following the international accounting changes to SAAS expenditure in FY2022. We forecast the payout ratio to remain at 90% through FY25, then return to 85%.



Source: Craigs Investment Partners

Share Alignment

ZGL announced its first tranche of initiatives designed to strengthen grower shareholding of ZGL. From CY2025, ZGL intends to offer shareholders the ability to reinvest dividend payments as shares, as well as to receive the June loyalty payment as shares. Both initiatives will be on an opt-in basis.

While ZGL has said that it does not intend to conduct a share buyback in relation to dry/overshared shares, it remains to be seen if they will conduct a share buyback in relation to the dividend reinvestment plan.

With less than 50% of growers currently owning shares, we believe industry alignment between growers and shareholders is one of the biggest issues ZGL faces. While there has been strong support in the last two producer votes, they ultimately have been voted down as they haven't met the required support of 75% of growers. We forecast that a successful vote to expand Zespri Global Supply from 5K to 15K hectares of Gold3 would add significant value to ZGL, so the outcome has been disappointing for shareholders.

The initiatives announced so far will help to strengthen grower shareholding of ZGL. This will ultimately help ZGL to respond to changing market conditions, by allowing them to conduct successful producer votes for activities that fall outside its core business.[1]

2024 crop

Indications are that the industry will have a good level of growth for both ZGL Green and SunGold Kiwifruit in CY2024 as it bounces back from the challenges of the last two seasons. The return of El Nino conditions resulted in good budburst, flowering, and strong fruit counts ahead of the 2024 harvest. We expect that volumes will be very significantly higher in CY2024 (182m trays).

Dry overhang

ZGL held a Special Meeting of Shareholders on 14 March 2018 to ask shareholders to consider recommendations that aimed to strengthen grower ownership and control of ZGL. The new constitution introduced dividend restrictions on shareholders who do not grow kiwifruit.

Dividends will cease seven years after the change for shareholders who were not producing at the time the constitution was updated. Consequently, there are 15.9 million dry shares that will convert to Class B shares on 14 March 2025.

With c12% of stock converting to Class B over the coming 15 months, we expect selling pressure to increase towards the back end of this year. ZGL has announced they do not intend to conduct a share buyback in relation to dry shares.

CEO resigns to take up a new role

ZGL's CEO Dan Mathieson will leave ZGL to take up a new position as President of the Americas for global berry company Driscoll's.

Mr Mathieson has been at ZGL for 21 years, almost seven of those as CEO. With the industry poised to deliver one of its largest-ever crops, he will remain at ZGL to

[1] As outlined in the Kiwifruit Export Regulations 1999

oversee the 2024 harvest and start of the sales season and until a new CEO is appointed.

Hi-Cane

The Environmental Protection Authority (EPA) hearing for Hi-cane has been moved to February 2024. 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. ZGL has fast-tracked trials of new green cultivars which are less reliant on Hi-Cane to try and ensure alternatives for Hayward growers, both should Hi-Cane be banned and as part of its overall breeding programme objective to find a new green cultivar.

Historical financial information ($nzd)

	FY19a	FY20a	FY21a	FY22a	FY23a	FY24f	FY19-24 CAGR
	31-Mar-19	31-Mar-20	31-Mar-21	31-Mar-22	31-Mar-23	31-Mar-24	
NZ Kiwifruit	2,599	2,755	3,185	3,356	3,239	2,718	0.9%
Non-NZ Kiwifruit	312	369	474	539	519	609	14.3%
Sale of PVR licences	193	215	307	437	308	213	2.0%
PVR Royalty income	28	33	39	45	47	46	10.4%
Other Revenue	10	15	14	17	18	14	6.4%
Revenue	**3,142**	**3,386**	**4,019**	**4,394**	**4,131**	**3,601**	**2.76%**
Growth %	*28.4%*	*7.8%*	*18.7%*	*9.3%*	*-6.0%*	*-12.8%*	n/a
Cost of Goods sold	-2,603	-2,769	-3,180	-3,562	-3,468	-2,944	2.5%
Gross Profit	**539**	**618**	**840**	**832**	**663**	**657**	**4.03%**
Growth %	*53.1%*	*14.5%*	*36.0%*	*-0.9%*	*-20.2%*	*-1.0%*	n/a
Selling General & Admin Exp.	-273	-308	-324	-351	-380	-400	7.9%
Other Expenses	-20	-50	-79	20	31	-30	8.5%
EBIT	**246**	**259**	**437**	**501**	**315**	**226**	**-1.67%**
Net Interest Income	5	5	1	3	12	12	16.6%
Other Non-Operating Exp.	4	14	-45	2	4	-2	n/m
Net Profit before Tax	**256**	**277**	**387**	**505**	**331**	**236**	**-1.56%**
Income Tax	76	76	110	144	93	67	-2.4%
Net Profit	**180**	**201**	**277**	**362**	**239**	**169**	**-1.22%**
Growth %	*76.6%*	*11.7%*	*41.1%*	*27.6%*	*-34.0%*	*-29.2%*	n/a
Earnings per share	0.99	1.10	1.55	1.97	1.30	0.92	-1.3%
Free cash flow	145	332	365	410	106	172	3.5%
Dividend per share	0.92	0.94	1.33	1.78	1.17	0.83	-2.0%
Net debt (cash)	-193	-293	-385	-414	-398	-398	15.6%
Key metrics	**2019**	**2020**	**2021**	**2022**	**2023**	**2024**	**FY19-24 Change**
Gross Margin	17.2%	18.2%	20.9%	18.9%	16.1%	18.2%	+100 bps
EBIT Margin	7.8%	7.6%	10.9%	11.4%	7.6%	6.3%	-150 bps
Free cash flow margin	4.6%	9.8%	9.1%	9.3%	2.6%	4.8%	+20 bps
EPS growth	76.0%	11.2%	41.1%	27.6%	-34.0%	-29.2%	n/a
Dividend payout ratio	93%	86%	86%	90%	90%	90%	n/a
Return on Equity	94.1%	90.1%	117.0%	125.8%	74.0%	53.5%	-4060 bps
Net Debt/EBITDA	-0.8x	-1.1x	-0.9x	-0.8x	-1.2x	-1.7x	-

Source: Company data, Craigs Investment Partners

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