

Hunza Properties Bhd

At long last

22 October 2009

Syariah-compliant stock

TRADING BUY	Maintained
RM1.47	Target: RM2.03
Mkt.Cap: RM221m/US\$66m	
Property Devt & Invnt	

HPB MK / HUZP.KL

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Rights issue

Hunza Properties (Hunza Prop) has proposed a 3-for-10 rights issue together with one free detachable 5-year warrant. Under the exercise, up to 45,207,697 rights shares will be issued. The issue price will be determined later. Based on an indicative price of RM1.10, the rights are priced at a 20% discount to the theoretical ex-rights price of RM1.38. Relative to yesterday's closing price of RM1.47, the discount is 25%. Overall, we are slightly negative on this development as the stronger balance sheet position post-exercise is more than offset by the EPS dilution concern. According to our estimates, the proposed exercise would likely dilute EPS by an estimated c.32-33%, and lower target price by about 5% to RM1.93 from RM2.03 previously. We are leaving our earnings projections and target price of RM2.03 unchanged pending the determination of the rights issue price. The stock remains a TRADING BUY on the potential re-rating catalysts of the 1) increasing investor interest in the Penang property market, 2) better-than-expected construction progress, and 3) margin expansion from lower building material costs. We view any share price weakness from this announcement as a buying opportunity. Even with the EPS dilution and expected downward revision in target price, valuations remain attractive.

The news

Hunza Prop has proposed to issue up to 45,207,697 new shares on the basis of three rights shares for every ten existing ordinary shares (3-for-10), together with up to 45,207,697 free detachable five-year warrants on the basis of one free warrant for every one rights shares. The company will procure written irrevocable undertaking from its substantial shareholders to subscribe in full their respective entitlements under the proposed exercise. Underwriting arrangements will also be made for the portion which the company is unable to procure written irrevocable undertakings. The issue price will be determined later based on the weighted average market price for the five market days prior to the price-fixing date, and the minimum gross proceeds of RM43m intended to be raised by the company. The exercise price of the warrants will also be determined at the price-fixing date, after taking into consideration the theoretical ex-rights price and the prevailing market conditions. Hunza Prop intends to raise a minimum gross proceed of RM43m from the proposed rights issue with warrants to fund its property development projects, investment properties and/or working capital requirements. The proposed exercise is expected to be completed by 1Q 2010.

Comments

Not entirely a surprise. The proposed rights issue was not entirely a surprise. The company's intention to undertake the rights exercise first came to light in Aug 07, but was subsequently delayed due to unfavourable market conditions. During the recent analyst briefing, management indicated that it intends to proceed with the rights exercise by year-end. The timing seems sensible in view of the improvement in investors' sentiment and the uptick in the stock market.

Theoretical ex-rights price of RM1.38. Based on an indicative price of RM1.10, the rights are priced at a 20% discount to the theoretical ex-rights price of RM1.38 $[(RM1.47 \times 10 + RM1.10 \times 3)/13]$. Relative to yesterday's closing price of RM1.47, the discount is 25%. However, we note that the theoretical ex-all price should be lower than RM1.38 due to the value of the detachable warrant. Assuming a fair value of 22 sen for the warrant, the ex-all price should be closer to RM1.32 $[(RM1.47 \times 10 +$

RM1.10 x 3)/13 – 3 x RM0.22 /10].

Estimated c.32-33% net EPS dilution. The proceeds from the rights issue would help strengthen the company's balance sheet position to help fund its future projects, most notably its Gurney Paragon mall. But we take a slightly negative view given that the proposed rights issue is expected to dilute EPS by an estimated c.32-33%, assuming the proceeds will be used to substitute borrowings. (Figure 1) Post-rights issue, our target price would likely be diluted by about 5% to RM1.93 from RM2.03 previously, assuming full conversion of all warrants after the cash call (Figure 2).

Figure 1: Discount of indicative price to theoretical ex-rights price

Issued and paid-up share capital (m)	150.69	
3-for-10 rights shares (m)	45.21	
1 free warrant (m)	45.21	
Enlarged share capital (m)	195.90	
Enlarged fully-diluted share capital (m)	241.11	
Current price (RM/share)	1.47	
Illustrative rights price (RM/share)	1.10	
Theoretical ex-rights price (RM/share)	1.38	
	-6.1%	
	FY10	FY11
Projected net profit (RM'm)	38.9	41.1
Add inc from rights proceeds (RM'm)	1.6	1.6
Add inc from warrant proceeds (RM'm)	1.6	1.6
Post-rights net profit (RM'm)	42.1	44.3
EPS before rights issue (sen/share)	25.8	27.3
Fully-diluted EPS post-rights issue (sen/share)	17.5	18.4
EPS dilution (%)	-32.3%	-32.6%
TP before rights issue (RM/share)	2.03	
TP ex-rights issue (RM/share)	1.93	
TP post rights issue-cum rights (RM/share)	2.07	

Source: CIMB Research

Potentially raising close to RM100m. Assuming all rights issue and warrants are exercised at an illustrative exercise price of RM1.10, close to RM100m would be raised. Hunza Prop has indicated that the proceeds will be channelled to fund future developments, investment properties and working capital requirements. But we think that funds raised from the rights issue would likely be channelled to the Gurney Paragon mall. We gather that total construction cost for the mall, including land cost, is estimated at c.RM400m. Construction is expected to commence early next year.

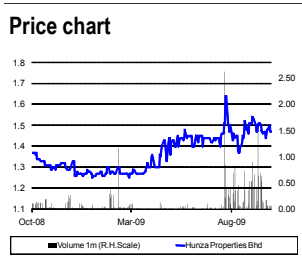
A revised proposal. This proposed exercise differs from the initial proposal revealed two years ago. Previously, the company proposed a 1-for-4 rights issue together with one free detachable warrant.

Valuation and recommendation

Rights issue a needed move? We think that the rights issue is needed in view of this upcoming mall project. Cash flows from its other projects such as the Infinity and Gurney Paragon condo are unlikely to be sufficient to single-handedly fund the construction of the mall. As at end-June 09, the company's gearing stood at c.34%. With the proposed rights issue, gearing will fall to an estimated 26%, which should allow more room for the company to comfortably gear up. We are projecting gearing to rise to 60% next year from 34% as the Gurney Paragon mall starts construction. The proposed exercise would help to partly fund the Gurney Paragon mall which will transform Hunza Prop into a property development cum property investment group upon its expected completion in 2012.

Maintain TRADING BUY. The rights issue and warrants exercise would result in an estimated 32-33% EPS dilution. Nonetheless, the company should emerge with a stronger balance sheet position to fund its future projects post-rights issue. We have left our earnings forecasts and target price of RM2.03 unchanged pending completion

of the rights issue price. Factoring in the dilution of the rights issue and the exercise of the warrants, and keeping our 40% discount to RNAV, we arrive at an ex-rights target price of RM1.93. Notwithstanding the EPS dilution and expected downward revision in target price, valuations remain undemanding. Our CY10-11 P/E's could be bumped up from 5.4-5.7x to 8.3-8.7x, but valuations would still be at a 29% discount to the sector average CY10 P/E of around 12.2x. The lower target price post-exercise still offers attractive upside of 31%, relatively to the KLCI upside of only 11% currently. Maintain TRADING BUY on the stock on the potential re-rating catalysts of the 1) increasing investor interest in the Penang property market, 2) better-than-expected construction progress, and 3) margin expansion from lower building material costs. We view any share price weakness from this announcement as a buying opportunity. Even with the EPS dilution and expected downward revision in target price, valuations remain attractive.



Source: Bloomberg

Financial summary

FYE Jun	2008	2009	2010F	2011F	2012F
Revenue (RM m)	245.3	91.8	173.3	203.2	185.2
EBITDA (RM m)	68.6	40.1	56.0	60.9	55.0
EBITDA margins (%)	28.0%	43.6%	32.3%	29.9%	29.7%
Pretax profit (RM m)	68.3	39.1	53.3	56.9	49.4
Net profit (RM m)	48.4	27.6	38.9	41.1	36.6
EPS (sen)	34.5	18.3	25.8	27.2	24.3
EPS growth (%)	3.1%	(47.0%)	41.2%	5.4%	(10.9%)
P/E (x)	4.3	8.0	5.7	5.4	6.1
Gross DPS (sen)	12.4	7.5	10.0	10.5	10.0
Dividend yield (%)	8.4%	5.1%	6.8%	7.1%	6.8%
P/BV (x)	0.7	0.7	0.6	0.6	0.5
ROE (%)	17.2%	8.7%	11.5%	11.1%	9.2%
Net gearing (%)	21.7%	24.6%	59.9%	59.1%	63.4%
P/FCFE (x)	4.3	(4.0)	69.7	8.3	(7.4)
EV/EBITDA (x)	4.4	8.3	8.5	8.1	9.6
% change in EPS estimates			-	-	-
CIMB/Consensus (x)			1.01	1.05	1.01

Source: Company, CIMB Research, Bloomberg

Figure 2: Share price adjustment

	RNAV	Discount Factor	TP
Current RNAV	3.38	40%	2.03
Ex-rights fully-diluted RNAV	3.21	40%	1.93

Source: CIMB Research

Figure 3: RNAV table

Project	Size/units	Market value (RMpsf)	Stake	Value (RMm)
Bandar Putra Bertam - Residential	435.6	10.00	70%	132.8
Bandar Putra Bertam - Commercial	48.4	40.00	70%	59.0
Sungai Petani, Kedah	393.0	3.00	100%	51.4
Alila, Penang	5.0	175.00	100%	38.1
Mutiara Seputeh	12.0	90.00	100%	47.0
Gurney Drive	3.5	400.00	100%	61.0
Infinity	3.0	200.00	90%	23.5
Alila II, Penang	9.6	175.00	80%	58.5
Surplus value from shopping mall & retail lots				186.1
Surplus value from Phase 3's office lots				14.0
Fixed assets				48.0
Net current asset less dev. prop.				44.5
Total long term borrowings				(86.2)
Proceeds from rights issue and warrants conversion				122.3
Total revised RNAV				800.1
Fully diluted no. of shares post cash call exercise (m)				236.7
Revised RNAV per share (RM)				3.38
Target price @ 40% discount to RNAV/share estimate				2.03

Source: CIMB Research

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NEUTRAL: The stock's total return is expected to be within +/-5% of a relevant benchmark's total return.

UNDERPERFORM: The stock's total return is expected to be below a relevant benchmark's total return by 5% or more over the next 12 months.

TRADING BUY: The stock's total return is expected to exceed a relevant benchmark's total return by 5% or more over the next 3 months.

TRADING SELL: The stock's total return is expected to be below a relevant benchmark's total return by 5% or more over the next 3 months.

SECTOR RECOMMENDATIONS

OVERWEIGHT: The industry, as defined by the analyst's coverage universe, is expected to outperform the relevant primary market index over the next 12 months.

NEUTRAL: The industry, as defined by the analyst's coverage universe, is expected to perform in line with the relevant primary market index over the next 12 months.

UNDERWEIGHT: The industry, as defined by the analyst's coverage universe, is expected to underperform the relevant primary market index over the next 12 months.

TRADING BUY: The industry, as defined by the analyst's coverage universe, is expected to outperform the relevant primary market index over the next 3 months.

TRADING SELL: The industry, as defined by the analyst's coverage universe, is expected to underperform the relevant primary market index over the next 3 months.

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STOCK RECOMMENDATIONS

OUTPERFORM: Expected positive total returns of 15% or more over the next 12 months.

NEUTRAL: Expected total returns of between -15% and +15% over the next 12 months.

UNDERPERFORM: Expected negative total returns of 15% or more over the next 12 months.

TRADING BUY: Expected positive total returns of 15% or more over the next 3 months.

TRADING SELL: Expected negative total returns of 15% or more over the next 3 months.

SECTOR RECOMMENDATIONS

OVERWEIGHT: The industry, as defined by the analyst's coverage universe, has a high number of stocks that are expected to have total returns of +15% or better over the next 12 months.

NEUTRAL: The industry, as defined by the analyst's coverage universe, has either (i) an equal number of stocks that are expected to have total returns of +15% (or better) or -15% (or worse), or (ii) stocks that are predominantly expected to have total returns that will range from +15% to -15%; both over the next 12 months.

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TRADING BUY: The industry, as defined by the analyst's coverage universe, has a high number of stocks that are expected to have total returns of +15% or better over the next 3 months.

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