

Hunza Properties

Laying the groundwork for its transformation

OUTPERFORM	Maintained
RM2.60	@17/08/07
Target: RM4.15	Mkt.Cap: RM352.3m
Property	

HPB MK / HUZZP.KL

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- **In line.** Excluding the RM2.9m revaluation gains on investment properties, Hunza Properties' FY6/07 results came in 1% above our forecast and 8% above consensus. As per previous years and our expectations, a 7.5 sen gross final DPS was recommended for the quarter.
- **Moving towards the mid-high end segment.** FY07 core net profit rose a whopping 84% yoy, thanks to more meaningful contributions from its high-end Mutiara Seputeh and Alila projects. The better product mix is also reflected by the 4% pt expansion in pretax margins enjoyed by its property development division. We expect margins to remain resilient as the group focuses on developing niche, boutique-type developments with quick turnaround times.
- **Attractive dividend yield.** Including the maiden 5 sen gross interim DPS declared in 3Q, FY07 gross DPS totalled 12.5 sen, which matches exactly our projection. This represents an attractive 4.8% yield, against the sector's 4.4% average.
- **Proposing cash call to raise RM80m-100m.** To part finance its future development projects and working capital, the group has proposed a 1-for-4 rights issue together with one free detachable warrant. We are not entirely surprised by this proposal as gearing has been a source of concern for the group. The proposal should lead to some RM4m-5m interest savings and pare down gearing to a more manageable 0.3x. But the 25% increase in its share capital (assuming full exercise of existing warrants and after incorporating the free detachable warrant) could dilute our adjusted FY09-10 EPS by up to 12%.
- **Finetuning FY08-09 earnings and introducing FY10 numbers.** After adjusting for FY07's actual numbers, our FY08-09 earnings projections are tweaked up by 1-2%. Note that our forecasts do not impute the dilutive impact of its proposed cash call exercise as the price has yet to be fixed.
- **Reiterate OUTPERFORM.** Taking into account our earnings revision and the potential dilutive impact of the cash call, we scale back our target price from RM4.80 to RM4.15 based on an unchanged 40% discount to our 20x target CY08 P/E for the sector. Notwithstanding this, Hunza Properties remains our preferred choice among the deep-value developers with Penang exposure. Re-rating catalysts include i) higher-than-expected sales and margins, ii) entry of reputable partners for its Gurney Drive project and iii) land bank acquisitions.

Results comparison

FYE Jun (RM m)	4QFY07	4QFY06	yoy % chg	qoq % chg	4QFY07 Cum	4QFY06 Cum	yoy % chg	Prev. FY07F	Comments
Revenue	69.7	44.3	57.4	56.0	190.0	116.6	62.9	178.6	Higher sales & steady construction progress
Operating costs	(47.3)	(29.1)	62.9	43.6	(131.6)	(81.6)	61.2	(122.8)	Higher cost in line with wider revenue base
EBITDA	22.4	15.2	46.8	90.9	58.4	35.0	66.8	55.8	5% above our full-year projection
EBITDA margin (%)	32.1	34.4			30.7	30.0	2.4	31.3	Higher margins yoy due to a better product mix
Depn & amort.	(0.2)	(0.0)	503.3	(44.5)	(0.8)	(0.9)	(13.3)	(0.7)	7% above our estimate
EBIT	22.2	15.2	45.9	94.8	57.6	34.1	68.9	55.1	
Interest expense	(0.0)	(0.0)	150.0	900.0	(0.0)	(0.0)	(8.7)	(0.1)	Below our forecast
Interest & invt inc	0.1	0.6	(91.4)	(29.2)	0.2	0.7	(66.1)	0.3	Lower-than-expected interest income rate
Exceptionals	2.9	-	nm	nm	2.9	-	nm	-	Revaluation gains on investment properties
Pretax profit	25.1	15.8	59.1	119.3	60.7	34.8	74.5	55.3	Lifted by RM2.9m revaluation surplus
Tax	(8.4)	(4.3)	95.2	178.2	(18.4)	(9.9)	86.7	(14.9)	Higher due to non-deductible expenses
Tax rate (%)	33.4	27.2			30.3	28.3	7.0	27.0	
Minority interests	(0.6)	(2.6)	(75.2)	(17.7)	(2.9)	(5.2)	(43.1)	(4.1)	Lesser earnings recognition from its JV projects
Net profit	16.1	8.9	80.4	110.0	39.4	19.8	99.2	36.3	9% ahead of our estimates
Core net profit	13.2	8.9	47.9	72.2	36.5	19.8	84.5	36.3	1% above our projection
EPS (sen)	13.7	7.8	75.0	103.3	33.6	17.4	93.7	27.6	Higher than expected
Core EPS (sen)	10.7	7.8	36.5	58.5	29.6	17.4	70.3	27.6	In line

Source: CIMB/CIMB-GK Research

Please read carefully the important disclosures at the end of this publication.

Financial summary

FYE Jun	2006	2007	2008F	2009F	2010F
Revenue (RM m)	116.6	190.0	254.6	303.7	298.2
EBITDA (RM m)	35.0	58.4	78.6	106.6	130.5
EBITDA margins (%)	30.0	30.7	30.9	35.1	43.8
Pretax profit (RM m)	34.8	60.7	78.2	107.0	130.9
Net profit (RM m)	19.8	39.4	52.9	72.4	85.6
EPS (sen)	17.1	29.1	39.1	53.5	63.3
EPS growth (%)	+21%	+70%	+34%	+37%	+18%
P/E (x)	15.2	8.9	6.7	4.9	4.1
FD EPS (sen)	13.4	28.8	34.0	46.4	54.8
FD P/E (x)	19.4	9.0	7.6	5.6	4.7
Gross DPS (sen)	7.5	12.5	13.5	14.5	15.5
Dividend yield (%)	2.9	4.8	5.2	5.6	6.0
P/NTA (x)	1.6	1.4	1.2	1.0	0.8
ROE (%)	10.6	17.6	19.7	22.7	22.3
Net gearing (%)	72.3	61.0	64.8	53.6	37.2
P/CF (x)	11.2	5.8	5.0	3.7	3.1
EV/EBITDA (x)	11.0	6.9	5.6	4.1	3.1
% change in EPS estimates			1.4	0.9	-
CIMB/Consensus (x)			1.11	1.10	

Source: Company, CIMB/CIMB-GK estimates, Reuters Estimates

Property sales

Property sales summary. During 4Q, the group raked in RM82.4m worth of property sales – almost a threefold increase qoq and a 30% rise yoy. This took FY07 property sales to RM195.8m, 18% above the RM166m achieved in FY06 (Figure 1). For FY07, the Mutiara Seputeh development was the major sales contributor, accounting for an estimated 40% of total sales. As at end-Jun 07, unbilled sales were relatively unchanged from the previous quarter at RM114m.

Figure 1: Property sales summary

	4QFY07	4QFY06	FY07	FY06
	RM m	RM m	RM m	RM m
Bandar Putra Bertam	5.1	23.8	23.5	57.0
Sungai Petani	2.9	2.9	7.7	9.0
Alila	16.0	19.5	45.2	83.0
Mutiara Seputeh	16.6	17.0	77.6	17.0
Gurney Paragon	41.8	-	41.8	-
Total	82.4	63.2	195.8	166.0

Source: Company, CIMB/CIMB-GK Research

Proposed rights issue

Proposing cash call exercise... Hunza Properties has proposed a 1-for-4 rights issue together with one free detachable 5-year warrant. Based on its fully diluted share capital of 157.8m shares, up to 39.4m rights shares will be issued. The pricing, which will be based on the weighted average market price for the five market days prior to the price-fixing date, and entitlement dates have yet to be determined.

... potentially raising RM95m... Based on an indicative issue price of RM2.40, the exercise could raise RM94.6m. RM2.40 represents a discount of about 6% to the RM2.56 theoretical ex-rights price (Figure 2).

Figure 2: Discount of indicative price to theoretical ex-rights price

	RM
Closing share price on 17 Aug 07	2.60
Total cost for 4 shares	10.40
1 rights share @ RM2.40 indicative price	2.40
Total cost for 4 shares + 1 rights share	12.80
Theoretical ex-rights issue price per share	2.56
Indicative price's discount to theoretical ex-rights price	-6%

Source: Company, CIMB/CIMB-GK Research estimates

... to fund transformation plans and more. We are not entirely surprised by this proposal given that the group's gearing level has been a source of concern in the past. Hunza Properties has indicated that the proceeds will be channelled to future

developments and working capital. To recap, the group's earnings profile is set to transform with i) a portfolio of development projects which carry a potential GDV of close to RM2.2bn and ii) a potential source of recurring income from its upcoming RM936m Gurney Drive development, which include among others, a 700,000 sq ft shopping mall and some 55,000 sq ft of retail lots. The proposed exercise is expected to strengthen the group's balance sheet position, which will enable it to carry out a more aggressive expansion.

An earnings-dilutive deal... Although the exercise could lead to interest savings of RM4m-5m annually, it will also increase the group's share capital base by 25% from 135.5m to 169.4m shares. The expansion of the share base could dilute our FY09-10 EPS estimate by up to 17% (Figure 3). On a fully diluted basis, the dilutive impact is even higher at 27% due to a 50% swelling of the share base (Figure 4).

... which also lowers target price... The exercise also has the effect of lowering our target price from RM4.80 to RM4.15, based on an unchanged 40% discount to our 20x target P/E for the sector.

Figure 3: Impact of Hunza Properties' cash call exercise on FY09-10 basic EPS figures

	FY09	FY10
Existing basic net profit (RM m)	72.4	85.6
Revised net profit post exercise (RM m)	76.1	89.2
Issued & paid-up share capital as at end-Jul 07 (m)	135.5	135.5
Share base as at end-Jul 07 (m)	135.5	135.5
1-for-4 rights shares (m)	33.9	33.9
Enlarged share base post exercise (m)	169.4	169.4
Revised basic EPS (sen)	44.9	52.7
Existing basic EPS (sen)	53.5	63.3
% of dilution	-16%	-17%

Source: CIMB/CIMB-GK Research

Figure 4: Impact of Hunza Properties' cash call exercise on FY09-10 FD EPS figures

	FY09	FY10
Existing fully diluted net income (RM m)	73.2	86.3
Revised fully diluted net income post exercise (RM m)	81.0	94.1
Issued & paid-up share capital as at end-Jul 07 (m)	135.5	135.5
Assuming full exercise of Warrants A (m)	22.2	22.2
Fully diluted share base as at end-Jul 07 (m)	157.7	157.7
1-for-4 rights issue (m)	39.4	39.4
Free detachable Warrants B (m)	39.4	39.4
Enlarged fully diluted share base post exercise (m)	236.6	236.6
Revised fully diluted EPS (sen)	34.2	39.8
Existing fully diluted EPS (sen)	46.4	54.8
% of dilution	-26%	-27%

Source: Company, CIMB/CIMB-GK Research

... and RNAV/share estimate. Assuming full conversion of all warrants after the cash call, our RNAV/share estimate will be lowered from RM4.31 to RM3.42 owing to the larger share base (Figure 5).

Figure 5: Hunza Properties' RNAV computation

Project	Size/units	Market value (RMpsf)	Stake	Value (RMm)
Bandar Putra Bertam, Seberang Perai	484	7.50	70%	110.7
Sungai Petani, Kedah	393	3.00	100%	51.4
Alila, Penang	9	45.00	100%	17.6
Mutiara Seputeh	12	90.00	100%	47.0
Gurney Drive	10	250.00	100%	108.9
Surplus value from shopping mall & retail lots				182.7
Fixed assets				145.0
Associated company				0.0
Net current asset less dev. prop.				58.2
Total long term borrowings				(135.5)
Proceeds from warrants conversion & rights issue				222.5
Total revised RNAV				808.6
Fully diluted no. of shares post cash call exercise (m)				236.6
Revised RNAV per share (RM)				3.42
Existing RNAV per share (RM)				4.31
% revision				-21%

Source: Company, CIMB/CIMB-GK Research

Gearing to improve. As at end-Jun 07, Hunza Properties' net gearing stood at 0.6x, an improvement from last FY's 0.7x. Assuming that this exercise is completed by FY6/08, FY09-10 net gearing should improve from 37-54% to 17-29%. Assuming full conversion of all warrants, gearing could be pared to the 4-11% level over the same period.

Valuations still attractive. Notwithstanding the earnings dilution and downward revision in our target price, valuations remain undemanding. Although our CY08-09 P/Es could be bumped from 5.1-6.5x to 7.0-7.5x, these ratings are still at a 46% discount to the 14x sector average. Also, if we were to strip out the value of the free detachable warrant from the share price, CY08-09 P/Es would be lower at 6.5-7.0x. This level represents a 50% discount to the sector average.

Our deep-value choice. Among its peers, Hunza Properties is still forecast to deliver one of the highest net profit growth (30% 3-year CAGR) and CY08 ROEs at 21%.

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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.

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