

13 February 2007

# PRICE | \$1.86 Regional Express Holdings Ltd | REX

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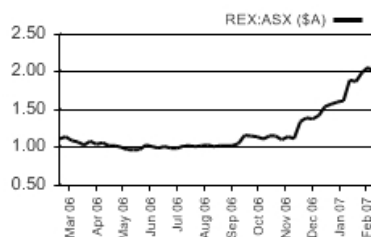
Max Wheeler  
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Fully diluted shares  
on issue | 115M  
Market cap | A\$228.9M

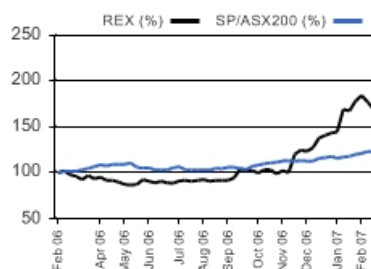
## Performance & Valuation

Last Price | \$1.86  
52 wk hi/low | \$2.15 / \$0.96  
12 mth price target<sup>3</sup> | \$2.07  
Valuation | \$2.04  
Valuation methodology | DCF

## Share price performance



## REX versus SP/ASX200



Tiger, Tiger burning (not so) bright

## Key points

- Tiger Airways has grabbed some press in recent days concerning its mooted launch of discount airline services in Australia.
- If this smacks of déjà vu you are right: Compass (Mark I, II); Impulse Airlines and OzJet (business carrier), etc. It is sobering that over the last 23 years, more than 70 domestic airlines have disappeared in Australia.
- REX has succeeded because the lessons of history have resonated and Government's have realised that irrational exuberance leads to a complete failure of regional airline activity. Eleven of REX's 33 routes are protected by NSW Government legislation.
- Tiger currently operates A320-200 aircraft, with 180 seat configuration. These planes would struggle to land at all but three of REX's destination airports: Ballina, Mildura and Broken Hill.

## Comment

The A320-200's cost US\$35-40M to purchase each and lease costs are around US\$4M pa (around A\$425k per month). Doing some very simple sums, Tiger would pay an average lease cost per passenger (assuming it mirrored REX's current activity) of \$145 for an average ticket price of \$165. That leaves \$20 to cover fuel, labour, etc, etc. And on its mooted \$10 a fare, it loses a minimum of \$135 a passenger.

Tiger may or may not be a success in Australia but it will not be at the cost of REX. Unless Tiger decides to re-invent itself and completely reconfigure its fleet, it is neither rational nor commercial to target any of REX's regional routes. We believe the target market is the domestic/regional routes – Sydney-Darwin/Canberra/Hobart; etc.

## Investment View

One of the most enduring lessons that REX has learnt is that route frequency is one of the most critical success factors in regional Australia. Trying to match REX using 180 seat aircraft is the stuff of fantasy.

We believe this distraction makes for an excellent buying opportunity, particularly ahead of a potentially robust interim result. Moreover, it is conceivable that REX could even become the objet du désir for Tiger to accelerate its thrust into Australia and give Singapore Airline the beachhead it clearly desires.

## Earnings Summary

Y/E Jun	2005A	2006A	2007F	2008F
Revenue - A\$M	142.0	169.7	216.1	258.4
EBITDA - A\$M	10.1	20.9	33.3	42.3
NPAT (reported) A\$M	6.5	15.7	20.7	23.9
NPAT (normalised) A\$M <sup>1</sup>	4.3	13.6	20.7	23.9
EPS (diluted) - cents <sup>2</sup>	7.3	13.3	18.0	20.8
EPS (diluted) - % chg	n/a	82.1	35.2	15.7
PER (diluted) - x <sup>2</sup>	25.5	14.0	10.4	8.9
DPS - cents	0.0	5.0	9.0	10.5
Dividend Yield - %	0.0	2.7	4.8	5.6
Franking - %	0	0	100	100

Notes:

1. Normalised earnings is pre goodwill, amortization and after adding back non-recurring items.

2. Based on normalized earnings.

3. Price target is calculated by moving current valuation one year forward.

# Final results analysis & outlook

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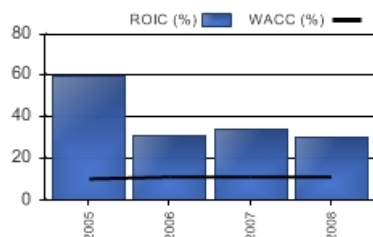


## Valuation

Methodology: DCF<sup>1</sup>

Key assumptions	
Beta	1.3
WACC %	11.2
Forecast period years	10.0
Risk premium %	5.5
PV cash flows \$M	222.1
less net debt/(add cash) \$M	(20.0)
add equity adjustments <sup>2</sup>	(7.5)
Total	234.6
Fully diluted shares on issue M <sup>2</sup>	115.0
Value per share \$	2.04

## Return on invested capital



## Ratio analysis

Year end Jun	06A	07F	08F
Revenue growth %	19.5	27.3	19.6
EBITDA growth %	107.7	59.1	27.0
EBITDA margin %	12.3	15.4	16.4
EBIT margin %	9.9	12.8	12.9
Tax rate %	35.5	30.0	30.0
ROA %	20.6	27.1	28.4
ROE %	24.6	27.6	27.2
Net debt/equity %	(34.3)	(16.6)	(21.7)
Net interest cover x	n/a	n/a	n/a
Capex to deprec'n %	172.7	77.3	87.6
NTA per share \$	0.59	0.72	0.84

## Multiple analysis

Year end Jun	06A	07F	08F
Market cap \$M	229		
Net debt (cash) \$M	(20.0)		
Options \$M	0.0		
Enterprise value \$M	216.4		
EV/EBITDA x	10.3	6.5	5.1
EPS c	13.3	18.0	20.8
P/E x	14.0	10.4	8.9
Cashflow / Share c	26.4	22.6	29.0
Price / NTA x	3.1	2.6	2.2

## Shares outstanding

Year end Jun	06A	07F	08F
Basic M	115.0	115.0	115.0
Other M	0.0	0.0	0.0
Fully diluted M	115.0	115.0	115.0

## Notes:

1. Discounted cash flow. 2. Equity adjustments and shares on issue include all notes and options on issue (if in the money or deemed appropriate).

Year end Jun	2005A	2006A	2007F	2008F
<b>Profit &amp; Loss Summary   A\$M</b>				
Operating revenue	142.0	169.7	216.1	258.4
Invest & other income	0.2	1.4	0.0	0.0
EBITDA	10.1	20.9	33.3	42.3
Depreciation/Amort	(2.6)	(4.2)	(5.6)	(8.9)
EBIT	7.5	16.7	27.7	33.4
Net Interest	(0.6)	0.9	1.1	0.7
Pre-tax profit	6.9	17.6	28.8	34.1
Tax expense	(2.6)	(6.3)	(8.6)	(10.2)
Minorities/Assoc./Prefs	0.0	2.2	0.5	0.0
NPAT	4.3	13.6	20.7	23.9
Non recurring items	2.2	2.1	0.0	0.0
Reported profit	6.5	15.7	20.7	23.9
add goodwill/non recurring	(2.2)	(2.1)	0.0	0.0
Adjusted profit	4.3	13.6	20.7	23.9
<b>Cashflow Summary   A\$M</b>				
EBITDA	10.1	20.9	33.3	42.3
Working capital changes	7.1	3.7	0.1	0.0
Interest and tax	(0.6)	0.9	(5.5)	(9.0)
Other operating items	(13.6)	1.4	(2.0)	0.0
Operating cashflow	2.9	27.0	25.9	33.3
Required capex	(5.9)	(7.3)	(4.3)	(7.8)
Maintainable cashflow	(3.0)	19.7	21.6	25.6
Dividends/Other	0.0	0.0	(5.8)	(10.4)
Acq/Disp	(2.7)	(23.8)	(25.6)	(8.0)
Other investing items	0.2	(4.8)	0.0	0.0
Free cashflow	(5.6)	(8.9)	(9.7)	7.2
Equity	0.2	35.0	0.0	0.0
Debt inc/(red'n)	8.6	(7.0)	9.7	(7.2)
<b>Balance Sheet   A\$M</b>				
Cash & deposits	4.5	23.6	13.9	21.1
Inventories	3.1	4.1	4.1	4.1
Trade debtors	11.7	8.6	8.5	8.5
Other curr assets	0.0	0.0	0.0	0.0
Total current assets	19.4	36.3	26.5	33.7
Prop., plant & equip.	28.9	45.6	69.9	76.8
Non-curr intangibles	0.2	0.8	0.8	0.8
Non-curr investments	0.0	14.3	14.8	14.8
Other non-curr assets	7.0	3.3	3.3	3.3
Total assets	55.4	100.3	115.3	129.5
Trade creditors	21.9	23.5	23.5	23.5
Curr borrowings	0.5	0.0	0.0	0.0
Other curr liabilities	4.6	6.5	6.7	7.3
Total current liab.	27.0	30.0	30.2	30.8
Borrowings	4.1	0.0	0.0	0.0
Other non-curr liabilities	2.0	1.5	1.4	1.4
Total liabilities	33.1	31.5	31.6	32.2
Minorities/Convertibles	0.0	0.0	0.0	0.0
Shareholders equity	22.4	68.8	83.7	97.3

# Final results analysis & outlook

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Year end Jun	2005A	2006A	2007F	2008F
<b>Divisional Summary A\$M</b>				
<b>Revenue</b>				
Division 1	142.0	169.7	196.8	217.5
Air-Link	0.0	0.0	7.0	7.2
PeIAir	0.0	0.0	12.3	33.8
<b>EBITDA</b>				
Division 1	9.9	19.6	30.3	35.6
Air-Link	0.0	0.0	0.9	0.9
PeIAir	0.0	0.0	2.1	5.8
<b>Margin %</b>				
Division 1	7.0	11.5	15.4	16.4
Air-Link	0.0	0.0	12.8	12.8
PeIAir	0.0	0.0	17.3	17.0

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As at the time of writing this report, the author holds shares in Regional Express Limited (REX), which were acquired as part of the REX IPO, in November 2005.

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