

24 May 2006

PRICE | \$1.07 Regional Express Holdings Ltd | REX

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Fully diluted shares

on issue | 115.0M

Market cap | A\$123M

Performance & Valuation

Last Price | \$1.07

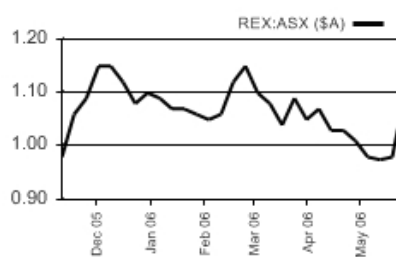
52 wk hi/low | \$1.18 / \$0.95

12 month price target³ | \$1.60

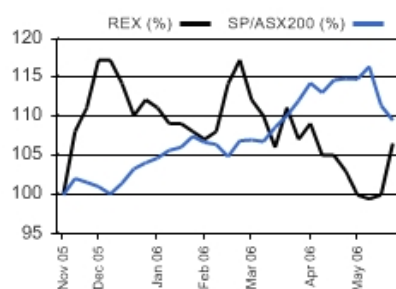
Valuation | \$1.57

Valuation methodology | DCF

Share price performance



REX versus SP/ASX200



A promising 3Q06 result

Key points

- REX reported a very solid 3Q06 result, with NPAT of \$12M (IFRS) for the nine months to 31 March 2006.
- Load factors continue to improve as do operating efficiencies.
- Passenger numbers are ahead of budget and up 12% Y-o -Y.
- Air Link-REX has achieved a combined market share above QantasLink in Dubbo.
- Prospectus forecasts for FY06 look set to be comfortably achieved with 79% of NPAT already booked and the 4Q is traditionally stronger than the 3Q.

Comment

- The threat of a change in the competitive dynamic in SA has not eventuated and the company still records some of its best operating statistics in the Adelaide-Port Lincoln route.
- Charter activities were strong and driven by a combination of factors, including the strong resources market.
- Nominally, the third quarter (from January to March) is a weak period for airlines and the 3Q06 was no exception for REX. This was combined with the nauseating paradigm of spiralling fuel costs.
- Notwithstanding, REX performed strongly and has locked in 79% of its FY06 earnings in the first nine months, as forecast in its Prospectus. This figure does not factor in any uplift provided by the further increase in fuel levies announced in April 2006.
- Based on what we consider to be an exceptional result, we have increased our FY06 earning forecast by 10% to \$21.2M (AGAAP).

Investment View

Our (very favourable) view on REX remains unaltered and, if anything, has been reinforced by this result. Moreover, on any comparable basis, REX generates margins and returns that are not matched by almost any airline in the world.

The challenge for the company, however, is that investors don't like airlines and no matter how good it gets there is still broad reticence to invest in airline stocks in this country. This view is not universal and other markets are less risk adverse to the vagaries of the airline industry. It is conceivable (and our fond hope) that continuing results of this measure by REX will result in the company being re-rated.

Earnings Summary

Y/E Jun	2005A	2006F	2007F	2008F
Revenue - A\$M	137.1	150.6	163.0	177.2
EBITDA - A\$M	16.2	24.0	28.2	34.4
NPAT (reported) A\$M	13.5	21.2	20.5	24.5
NPAT (normalised) A\$M ¹	13.5	21.2	20.5	24.5
EPS (diluted) - cents ²	16.9	19.9	17.9	21.3
EPS (diluted) - % chg	n/a	18.1	(10.5)	19.2
PER (diluted) - x ²	6.3	5.4	6.0	5.0
DPS - cents	0.0	3.0	7.0	9.0
Dividend Yield - %	0.0	2.8	6.5	8.4
Franking - %	0	0	50	100

Notes: Accounts presented under AGAAP

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

Regional Express Holdings Ltd | 24 May 2006



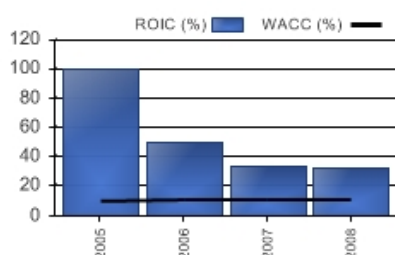
Valuation

Methodology: DCF¹

Key assumptions

Beta	1.3
WACC %	11.2
Forecast period years	10.0
Risk premium %	5.5
PV cash flows \$M	160.0
less net debt/(add cash) \$M	(20.0)
add equity adjustments ²	0.0
Total	180.0
Fully diluted shares on issue M ²	115.0
Value per share \$	1.57

Return on invested capital



Ratio analysis

Year end Jun	05A	06F	07F
Revenue growth %	0.0	9.8	8.2
EBITDA growth %	n/a	48.1	17.5
EBITDA margin %	11.8	15.9	17.3
EBIT margin %	9.0	13.0	14.6
Tax rate %	0.0	5.9	30.0
ROA %	31.0	24.8	24.0
ROE %	96.8	37.6	24.5
Net debt/equity %	0.5	(27.3)	(32.7)
Net interest cover x	17.7	n/a	n/a
Capex to deprec'n %	397.4	315.3	131.1
NTA per share \$	0.23	0.66	0.79

Multiple analysis

Year end Jun	05A	06F	07F
Market cap M	115		
Net debt (cash) \$M	(20.0)		
Options \$M	0.0		
Enterprise value \$M	95.0		
EV/EBITDA x	5.9	4.0	3.4
EPS c	16.9	19.9	17.9
P/E x	6.3	5.4	6.0
Cashflow / Share c	(7.4)	17.2	22.5
Price / NTA x	4.6	1.6	1.4

Shares outstanding

Year end Jun	05A	06F	07F
Basic M	80.0	115.0	115.0
Other M	0.0	0.0	0.0
Fully diluted M	80.0	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	2006F	2007F	2008F
Profit & Loss Summary A\$M				
Operating revenue	137.1	150.6	163.0	177.2
Invest & other income	0.0	0.0	0.0	0.0
EBITDA	16.2	24.0	28.2	34.4
Depreciation/Amort	(3.8)	(4.4)	(4.4)	(5.4)
EBIT	12.4	19.6	23.9	29.0
Net Interest	(0.7)	0.9	1.3	1.6
Pre-tax profit	11.7	20.6	25.2	30.6
Tax expense	0.0	(1.2)	(7.6)	(9.2)
Minorities/Assoc./Prefs	1.8	1.8	2.9	3.1
NPAT	13.5	21.2	20.5	24.5
Non recurring items	0.0	0.0	0.0	0.0
Reported profit	13.5	21.2	20.5	24.5
add goodwill/non recurring	0.0	0.0	0.0	0.0
Adjusted profit	13.5	21.2	20.5	24.5
Cashflow Summary A\$M				
EBITDA	16.2	24.0	28.2	34.4
Working capital changes	0.0	(2.5)	(0.1)	(0.3)
Interest and tax	(0.6)	(3.0)	(2.3)	(6.8)
Other operating items	(21.5)	(0.3)	0.0	0.0
Operating cashflow	(5.9)	18.2	25.9	27.2
Required capex	(15.1)	(13.7)	(5.7)	(7.1)
Maintainable cashflow	(21.0)	4.5	20.2	20.1
Dividends/Other	0.0	0.0	(6.3)	(6.9)
Acq/Disp	6.4	(13.2)	(5.0)	(9.7)
Other investing items	4.2	(2.8)	0.0	0.0
Free cashflow	(10.4)	(11.5)	8.8	3.5
Equity	0.0	35.0	0.0	0.0
Debt inc/(red'n)	4.6	(3.7)	(8.8)	(3.5)
Balance Sheet A\$M				
Cash & deposits	4.5	21.5	30.3	33.8
Inventories	3.0	3.4	3.8	4.2
Trade debtors	7.3	6.6	6.6	6.6
Other curr assets	4.5	1.3	1.3	1.3
Total current assets	19.3	32.8	42.0	45.8
Prop., plant & equip.	24.5	34.9	41.3	52.7
Non-curr intangibles	0.0	0.7	0.7	0.7
Non-curr investments	1.9	13.9	16.8	19.9
Other non-curr assets	4.6	12.7	12.7	12.7
Total assets	50.3	95.1	113.6	131.9
Trade creditors	12.4	15.7	16.0	16.0
Curr borrowings	0.5	0.5	0.5	0.5
Other curr liabilities	13.5	0.9	4.8	5.6
Total current liab.	26.4	17.0	21.3	22.1
Borrowings	4.1	0.0	0.0	0.0
Other non-curr liabilities	1.2	1.2	1.2	1.2
Total liabilities	31.7	18.2	22.5	23.3
Minorities/Convertibles	0.0	0.0	0.0	0.0
Shareholders equity	18.6	76.9	91.1	108.7

Year end Jun	2005A	2006F	2007F	2008F
Divisional Summary A\$M				
Revenue				
REX	137.1	146.6	155.9	169.7
Air link	0.0	4.0	7.2	7.5
EBITDA				
REX	16.2	23.8	27.0	32.9
Air link	0.0	0.2	1.3	1.5
Margin %				
REX	11.8	16.2	17.3	19.4
Air link	0.0	5.0	17.3	19.4

1 | Result detail

Comment

Rex's 3Q06 result provides continued assurance that the business is very much on track to meet (and most likely exceed) its Prospectus forecasts.

Nine months to 31 March 2005	YTD06 (\$M)	YTD05 (\$M)	Prospectus ² (\$M)	Achieved
Revenue ¹	115.9	96.1	144.7	79%
EBITDAR	24.7	14.8	33.1	75%
PBT	17.0	7.0	21.5	79%
NPAT	12.0	6.2	15.1 ³	79%
EPS	12.0c	11.0c	n/a	n/a

Source: REX

Notes: 1. Including fuel levy recovery based on pre April 2006 levy surcharge. 2. Based on A-IFRS 3. Under AGAAP, REX will book a \$4.8M tax benefit against its FY06 tax expense. The resulting FY06 NPAT as presented in its Prospectus was forecast to be \$19.7M.

The highlights of the result were:

Revenue and associates

Revenue

- Passenger revenue contributed 99%, or \$109M of total revenue. We note this figure does not include the increased fuel levy which was announced on 28 April 2006.
- YTD there was an 12% increase in passenger numbers, from 771K in the previous period to 864K in the current period, with load factors increasing to 66.2% from 65.8% pcp.
- The average fare (excluding fuel levy) is A\$101 showing a 6% decline pcp. We note that such a decline was budgeted by REX in its Prospectus.

Air Link

- The pro rata contribution made by Air Link (100% owned - Air Link was purchased on 30 November 2005) for the nine months to 31 March 2006 was revenue of \$5.8M and PBT of \$560K.
- Since its marriage to REX, Air Link has performed strongly and in March 2006, its (combined with REX) market share in Dubbo surpassed QantasLink.
- With much improved distribution, it was noted that Air Link is enjoying significantly improved load factors (up 11% points to 70.3%) and passenger numbers (up 35% to 31K). Moreover, charter activity has also experienced a marked improvement, notably due to increased resources activity.

Pel-Air

The 50% owned associate, Pel-Air, acquired 1 July 2005, delivered modest 5% earnings growth, delivering PBT of \$4M for the nine months to 31 March 2006. REX re-affirmed that the business was very much on track to meet Prospectus budget and that it was intending to introduce a SAAB to bolster charter activity.

Costs

- Improved productivity resulted in cost per available seat kilometre (ASK) falling 2% from 19.8 cents to 19.2 cents. Based on REX data, REX operated on (by far) the greatest PBT/Revenue margin (15% 3Q06) than any of its peers (for instance, over the same period, Virgin Blue operated on a PBT/Revenue margin of 11%).

Fuel costs remain a primary expense. With its average fleet size expanding to 29 aircraft and with sustained rises in fuel prices (REX does not hedge its fuel costs) fuel as a % of total expenses increased by 4% points to 19.6% for the nine month period.

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

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