

Wednesday, 3 September 2008

Regional Express Holdings (REX)

A Difficult Year but a Solid Outcome

REX announced strong sales revenue growth of 5.6% to \$211.3m and solid NPAT growth of 5.5% to \$24.3m (2.1% above our expectations) for FY08. REX's FY08 NPAT result was impressive given the various problems incurred by the airline during the year including rapidly increasing aviation fuel prices and pilot poaching by the major airlines (REX's pilot attrition rate in FY08 was 50%). These problems caused capacity reductions and suspensions on various REX's air routes in FY08. REX noted during 2H08 that *"the continued high attrition rate means that our flight schedules remains vulnerable...overall this will see a reduction in planned flying activities of around 3%"*. Therefore, REX's senior operational management have achieved an excellent result in extremely difficult conditions.

Overall, despite pilot losses and difficult trading conditions, REX has maintained solid operational efficiency. In FY08, REX maintained load factors and yield, we believe this improvement will be carried through to FY09.

Details	FY08
ASKs (m)	814
Load Factor	68.1%
Revenue/ASK (c)	26.0
Total cost/ASK (including fuel)	23.8

In FY09 REX will face a less competitive regional airline market. REX's main competitor in South Australia, O'Connor Airlines collapsed towards the end of 1H08. Additionally, REX's main freight competitor Jetcraft, was placed in administration in late 1H08, due to financial problems caused by the unexpected grounding of two of its aircraft and the failure of a major customer. The main reasons for these airline failures are a combination of under-capitalisation, increased operating costs and higher fuel costs.

REX's balance sheet remains asset rich – at the end of FY08 the Company held \$11.7m in net cash, \$75.4m in aircraft and \$40m in property, plant and equipment (including aircraft parts and the corporate headquarters). REX's NTA backing is 90 cps.

REX as part of the company's ongoing capital management program is currently undertaking an on-market share buy-back. REX is seeking to buy-back up to 12 million ordinary shares (approximately 10% of issued capital).

REX is a well-respected regional airline with a conservative business strategy combined with a strong balance sheet. REX operates a fleet of 37 Saab-340 aircraft from Sydney, Melbourne and Adelaide on regional air routes. Our recommendation on REX is accumulate.

In Brief

Recommendations

Short Term:	Accumulate
Long Term:	Accumulate
Risk:	High
Price:	\$1.25
12 Month Price Target:	Under review

Snapshot

Monthly Turnover	\$5.4m
Market Cap	\$131.0m
Shares Issued	117.1m
52 Week High	\$2.79
52 Week Low	\$0.88
Sector	Transportation

Business Description

Regional Express Holdings (REX) is an airline providing regular passenger, charter and freight transport services to regional south-east Australia.

Investment Fundamentals (under review)

Year to 30 June	FY06(a)	FY07(a)	FY08(a)	FY09(e)
NPAT (\$m)	15.7	23.6	24.3	25.0
Adjusted EPS (¢)	13.7	20.4	20.3	21.3
EPS Growth (%)	-	48.9	(0.5)	4.9
PE Ratio (x)	9.1	6.1	6.2	5.9
DPS (¢)	5.0	6.6	6.6	6.6
Div/Yield (%)	4.0	5.3	5.3	5.3
Franking (%)	0.0	100.0	100.0	100.0

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