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STOCK TO
WATCH



REGIONAL EXPRESS HOLDINGS (REX)

REX – Strong Growth Outlook

BUY

Share Trading Info

ASX Code	REX
Current Share Price (\$)	1.08
52 week trading Low/High (\$)	0.975 / 2.80
Annual Turnover (shares) - m	42.3

Enterprise Value (EV)

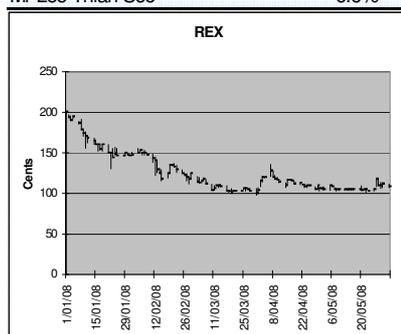
Ordinary Shares m	121.3
Unlisted Options	0.0
Diluted Shares	121.3
Current Market Capitalisation \$m	130.4
(Net Debt)/Cash	15.0
Enterprise Value \$m	115.4

Board & Management

Mr Lim Kim Hai	Executive Chairman
The Hon. John Sharp	Deputy Chairman and Independent Director
Mr Jim Davis	Managing Director
Mr David Miller	Executive Director
Mr Lee Thian Soo	Non-Executive Director
Mr Russel Hodge	Independent Director
Mr Stephen Jermyn	Independent Director

Substantial Shareholders

	Holding
Mr Lim Kim Hai (direct holding)	15.8%
Mr Lim Kim Hai (indirect holding)	4.0%
Mr Tjoa Joe Tiau	11.9%
Mr Lee Thian Soo	6.6%



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Company Overview:

REX is the largest independent regional airline in Australia and holds a monopoly over a majority of the routes it operates in (33 of its 39 routes are solely operated by REX). The company also operates charter and freight flights around Australia through its wholly owned subsidiaries Pel-Air and Airlink. The company's strategy is to achieve passenger and revenue growth through the maximization of seat capacity and flight frequency on high load routes whilst upholding a view of affordable consumer prices.

Event:

Regional Express Holdings (REX) reported 3Q08 operating results.

Key Points:

- **Fuel prices.** REX reported rising fuel costs for 3Q08 compared to 3Q07. The overall fuel cost increase was 23.3% between the two periods and this continues to be a major risk for the future earnings of the company. However, rising fuel costs can be partially passed onto passengers through the fuel ticket levy. The company expects fuel costs to be high for 4Q08. Our view is that that fuel costs may settle to approximately \$120 per barrel from current highs of \$135 per barrel in FY09.
- **Better than expected Net Profit After Tax (NPAT) for 3Q08.** After disappointing 1H08 results where NPAT was down 10% on 1H07 results, the third quarter of 2008 reported a 7.5% rise in NPAT compared to 3Q07. The company's expected view of NPAT for FY08 will be flat and in line with FY07 results (\$23.6 million NPAT with undiluted earnings per share of 20.5 cents).
- **Pilot attrition and network contraction.** Pilot attrition remains a risk to REX operations and earnings. Major issues have arisen due to the lack of back up crews and the >50% pilot attrition impacting network services. REX scaled back a further 3% of network services in response to pilot shortages in 3Q08. The company's 4Q08 view remains that network services may be cut marginally further with an expectation that cadet pilots who entered the Australian Airline Pilot Academy (fully owned and operated by REX) will be available to increase network services from 1H09.
- **Strong growth outlook.** With continued network consolidation, REX expect they will have stronger load factors in 4Q08 than the previous quarters. REX also expect growth targets of 10% in NPAT from

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FY09 onwards as current growth in passenger numbers continues to expand (8.8% increase in 3Q08 compared to 3Q07), the effective management of pilot shortages through the pilot academy and the introduction of new generation aircraft to improve the frequency of network services.

3Q08 Operating Results:

- **NPAT.** 3Q08 results reported that NPAT rose 7.5% from 3Q07. 3Q08 also saw a 7.3% increase in REX Group's passenger revenue as well as a 3.9% increase in other costs and expenses as compared to the March 07 quarter.
- **Load Factors and passenger numbers.** Passenger numbers are higher by 8.8% adding 5.7% to passenger revenues compared to the same period FY07. Load factors decreased by 0.4% to 68.1% for the period of FY08 compared to FY07, however the company's view is that loading factors are expected to be stronger in 4Q08 as network consolidation continues. REX is also aggressively introducing new generation aircraft to maximize flight frequency for its high load routes.
- **Key operating achievements.** REX recorded the second best 3Q08 quarter departure times of all regional carriers as well as the lowest rate of cancellations for the same period.
- **Operating Disappointments in 3Q08.** Pilot attrition remains above 50% for 3Q08. Pilot shortages have resulted in continued network service consolidation (3% over 3Q08). REX addressed this issue with the Australian Airline Pilot Academy (fully owned and operated by REX) which currently has 16 cadets running in the program with another 23 entered in the program in 4Q08. The company's view is that the pilot shortages will be less of an issue in FY09 as they attempt to place 20 new recruits in the program every quarter.

Outlook – 4Q08 and Beyond:

- **Fuel Prices.** REX expects that 4Q08 will maintain high fuel prices leading to a dampening on earnings.
- **Load Factors.** 4Q08 is expected to yield significantly higher loading factors as network consolidation continues throughout 4Q08 in response to pilot shortages.
- **Growth.** In 4Q08, REX will be maximising seat capacity and flight frequency through the phasing out of older aircraft and the introduction of 3 new generation aircrafts. REX expect that the FY08 net earnings will be flat and consistent with the reported FY07 results given that market conditions don't deteriorate significantly for the final quarter.

Recommendation:

- **Buy.** REX expect the FY08 results to be relatively consistent with FY07. The company's longer term forecast is to achieve its 10% NPAT growth in FY09 as passenger numbers continue to rise and Pel-Air Aviation Pty Ltd (wholly owned subsidiary of REX) begins to gain further market share in the Freight and Charter market.

Further, the company has been able to provide between \$0.19 to \$0.30 earnings per share over the past financial years and forecasted fully franked dividends of >6.6 cents per share have been expected by other analysts. As at 1H08, the company had \$4.43 million of debt, owned 22 of its 38 passenger planes and held \$19.4 million in cash, suggesting a strong financial position which is expected to be maintained.

- **REX – Share Buyback.** In addition to the fundamentals of the company being strong, REX is also in the market buying back 12 million shares (approximately 10.1% of shares on issue) of which about 3.99 million have been purchased. Further, Aequus is the broker for the buyback. The fact that the company is buying back shares tends to indicate that REX is undervalued.
- **Management Interest.** Mr Lim Kim Hai, the Executive Chairman of the board, has been purchasing REX since 23 October 2007 where his holding was 19%. As of 12 March 2008, Mr Lim Kim Hai has increased his stake in the company to 19.9%. This point reaffirms the strong outlook for the company.

Disclosure

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