STOCKS DOWN UNDER

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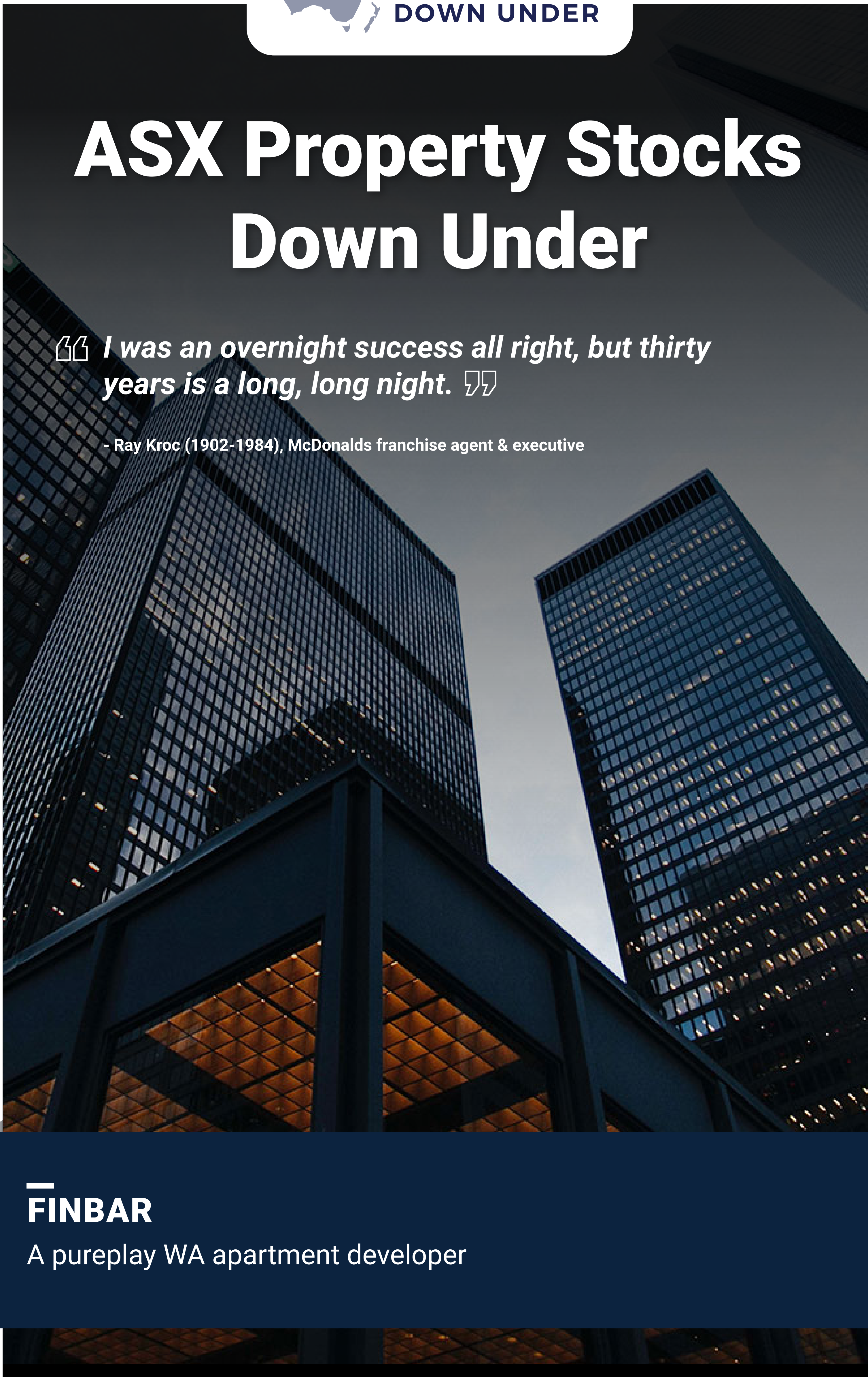
ASX Property Stocks Down Under



I was an overnight success all right, but thirty years is a long, long night.

- Ray Kroc (1902-1984), McDonalds franchise agent & executive

FINBAR

A pureplay WA apartment developer

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Stocks Down Under rating: ★★

ASX: FRI
Market cap: A$212M

52-week range: A$0.76 / A$0.92
Share price: A$x.xx

There's no shortage of ASX property stocks offering exposure to Western Australia, but Finbar Group (ASX: FRI) is one of the few pureplays. The apartment developer is the largest of its kind in Western Australia and is persistent despite several property cycles over the years. It's fair to say it would be somewhat of an icon in the West. But is Finbar a good investment? On its track record alone, you might say it is. Yet we're not so sure it can continue into the future especially considering the volatility of the Perth unit market.

Share price chart

Source: Tradingview

The "Wild" West

Finbar is one of the ASX's oldest property stocks, first listing in 1994 and recording perpetual profits since then. It has continued building apartments in Western Australia through resources booms and busts. Units are sold off the plan or during construction. The majority of Finbar's apartments have been in Perth, particularly in the CBD and inner suburbs. But in 2010, it built an apartment complex in the Pilbara city of Karratha and it retained the apartments for rental income for several years thereafter.

The Perth property market is very volatile because its fortunes hinge on the fate of the resources sector. In the down times, prices fall and people move interstate. The "bust" between 2011 and 2016 led to prices falling 15-30% and a significant 'brain drain' from Perth. Mining booms have typically led to the opposite. It has been over two years since we covered Finbar – we last did so in one of our first editions of Stocks Down Under in January 2020. At the time, no one would have forseen the disruption that COVID-19 would cause.

The hard border inhibits growth

Western Australia has had among the strictest border policies in the world – even locking out its own residents and typically with little to no prior notice. On one hand, the border worked at keeping the virus at bay and helped the mining and resources sector operate with little interruption. But the border restricted the 'brain gain' that would otherwise have occurred. And, eerily similar to the eastern states, the apartment market in Perth lagged houses, again due to border closures, but also due to strong demand for houses. The handful of development disasters, such as the Mascot Towers arguably didn't help would-be apartment buyers either.

In fact, in the first twelve month of the pandemic (the twelve months to 31 March 2021), Perth's median unit price only grew by 0.5%, well behind the 4% growth in Perth's median house price. There were some periods when sales volumes were high and even outpaced houses. For instance, in the March quarter of 2021, sales volume for Perth units grew 58%, ahead of houses, which only grew 35%. But even though growth in unit prices improved, they continued to lag. In the 12 months to 31 March 2022, unit prices grew 5.6%, well behind the 11.4% national average.

Finbar maintained its profitability throughout the pandemic, continuing a streak that extends over 25 years now. However, after recording an $11.7m NPAT and $154.7m in revenue in FY19, Finbar's revenue and profit fell to $154.3m and $7.1m respectively in FY20. In FY21, Finbar's profit rebounded somewhat, to $8.9m, but its revenue fell again, to $102.0m. In its most recent annual report, the company admitted there was decreased demand and projects were being delayed due to a rise in development costs and financial backers being more cautious – requiring a pre-determined level of pre-sales before proceeding.

Prior to the pandemic, nearly 20% of Finbar's sales were to foreign buyers, but it goes without saying this market was eliminated. The 7% foreign buyer duty, introduced prior to COVID, also hasn't helped market sentiment and it looks like the levy is here to stay.

A solid pipeline, but how will the market go?

Still, it isn't all doom and gloom for Finbar. In 1HY22, it made a half yearly net profit of $9.6m, up 138% from the prior corresponding period, although its operating net profit was just $4.6m - the former figure was inflated by the value of its Pelago investment. It has a healthy pipeline, with $642m in projects under construction and a total residual pipeline of $1.42bn. The Dianella and Sabina developments, lying in Perth's southern suburbs, accounted for two thirds of its 1HY22 earnings.

It has three projects under construction – Applecross, Civic Heart and AT238 – one being marketed off-the-plan, five properties with development approval and two others in planning. And the company has a healthy cash balance of over $49m.

2022 looking promising

In its 1HY22 report the company said 2022 had begun strong with 57 sales worth $33.5m being achieved across all projects. But it remains to be seen what impact the removal of border restrictions will have on the market. It is likely that supply chain disruptions and labour shortages will ease. If people return to WA in droves – particularly from overseas - the unit market might pick up. But it is likely arrivals could be cancelled out by departures and we are about to enter a cycle of rising interest rates. We do note that gross rental yields in Perth are 5.5% for units, the highest in Australia. But this won't be as much benefit for Finbar as it would for a company like Mirvac (ASX: MRG) that holds onto newly built apartments and leases them out.

All things considered, there is a lot to like about Finbar, including its 26-year run of profitability and its significant pipeline. But it has exposure solely to one property market and is trading at a 23.1x trailing P/E ratio (which we think is high given what we have outlined).

All things considered, Finbar gets two stars from us. We like Finbar's track record, but we would rather not have all our 'eggs in one basket' especially in respect of a property market that goes through more booms and busts than other places in Australia and even with the current boom is lagging other markets in Australia.

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Stocks Down Under gives you an information advantage to better invest and trade in ASX-listed stocks!