STOCKS DOWN UNDER

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ASX Property Stocks Down Under

"Like a fine wine, you get better with age - as long as you remember when to put a cork in it."

- Gene Perret (1937-2022), Television comedy writer

PEET

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Stocks Down Under rating: ★ ★ ★ ★

ASX: PPC
Market cap: A$536.8M

52-week range: A$0.86 / A$1.20
Share price: A$1.13

It has been rough year for property developers, but not so much for Peet (ASX:PPC) - at least judging by its 5% share price gain in the last 12 months. Peet is no ordinary property stock, it has an integrated platform that facilitates property development, marketing, acquisition and sales. It makes efficient capital arrangements with a diverse set of third parties, which gives it a low-cost portfolio of income generating assets. On top of all this, Peet has a funds management platform, spread across various retail, wholesale and joint venture assets.

Share price chart

Source: Tradingview

A very long-term property developer

Peet's history goes back to 1895, named after founder James Thomas Peet who wanted to help Australians build or buy their own home. It has only been listed since 2004 and has had a turbulent share price that has largely followed the broader property market. But it has managed to defy the bear market, plus fears of supply chain and construction issues, with an 8% gain in the last 12 months. The company will tell you it has gained for several reasons. One is because it is developing in areas where people want to live in now – inner to outer rings of capital cities (especially Brisbane and Perth). Other reasons include strong embedded margins and economies of scale through large land banks. It has a total of 47 projects with a $13.4bn end value.

We also observe that Peet has very long-tenured management. It has been run by Managing Director Brendan Gore for nearly all its listed life – he took over in 2007. Another long-term executive is Non-executive Chairman Tony Lennon. He has been with the company since 1991 and is the largest shareholder with a stake of ~20%.

A good FY22

Peet closed FY22 (the 12 months to 30 June) with a post-tax profit of $52.3m, up 84% and a record for the company. Revenue was $290.7m (up 24%), EBITDA was $86m (up 54%) and cash flow from operations before acquisitions was $80.1m (up 30%). It paid a 6.25c per share dividend, up 79% and representing a payout ratio of 57%.

Looking to operational metrics, Peet sold 3,163 lots and settled on 2,514, representing 70% growth from FY21. It has $930m in contracts on hand value. Highlights of the year included the acquisition of the remaining 50% stake of the Flagstone City project in South-East Queensland that it did not already own and the acquisition of a project in Belconnen, Canberra that will comprise of ~2,650 dwellings.

Peet thinks it is in for good things in FY23

The company did not provide specific guidance for FY23 and there are no consensus estimates given there are no analysts covering the company. You might expect it won't be able to repeat the performance given the retreat of the property market. However, the company said it was well positioned for earnings growth due to upcoming settlements – albeit skewed towards the first half of the year. We note that the company has 73% of its land bank under development, indicating that there is more growth to come in FY23.

Peet is valued at a trailing P/E multiple of 10.5x and a trailing EV/EBITDA of 9.7x. These look reasonable at first glance, although it is always preferable to use forward-looking multiples when available even though they are based on estimates, not actual numbers.

Despite the company's optimism, there are some challenges facing it in the months ahead. Obviously, inflation, interest rates and construction supply chain issues are the most prominent. The company's gearing is reasonable, but nonetheless expected to be above the target range of 20-30%, which the company says is because of construction activity required to deliver on current contracts.

We also note that Peet has a high reliance on first home buyers, accounting for 40% of sales in FY22. Admittedly, this is down from 58% in FY20, but it is still Peet's largest market. The next demographic, second or subsequent buyers, is just 24%. First home buyers will be the most sensitive to rising interest rates.

The company also indicated that construction costs are rising, but believes that rate of construction cost escalation is also expected to moderate. Obviously, this is different from saying that construction costs would stop escalating altogether.

A good long-term pipeline

Investors appear to be shrugging off these issues for now, at least judging by Peet's share price performance. Or perhaps they believe the company's bottom line will not be significantly impacted by them. However, there is the risk that investors could be wrong on the latter front. If so, there could be an adverse share price reaction when investors realise this. Other risks include long-tenured management departing and a slowdown in the sales pipeline due to rising interest rates. In respect of the latter issue, we think this will only be significant if the RBA hikes rates well beyond what the market currently expects – i.e. well higher than 4%.

In the end, Peet has proven itself through all market conditions throughout its history. Consequently, there is little reason to believe that it can't continue to push through the current environment even if it is not all smooth sailing. Four stars.

Pitt Street Research Pty Ltd

3 Spring Street, Sydney, NSW 2000, Australia