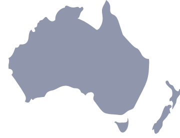


STOCKS DOWN UNDER

14 DEC 2022

ASX Property Stocks Down Under

The market isn't a game or casino; it's a serious thing. And if you're wrong, be prepared to lose.

- Marc Cohodes (b. 1960), Co-manager at Rocker Partners

LENDLEASE

Making cities beautiful today and shareholders richer tomorrow

LENDLEASE

Making cities beautiful today and shareholders richer tomorrow

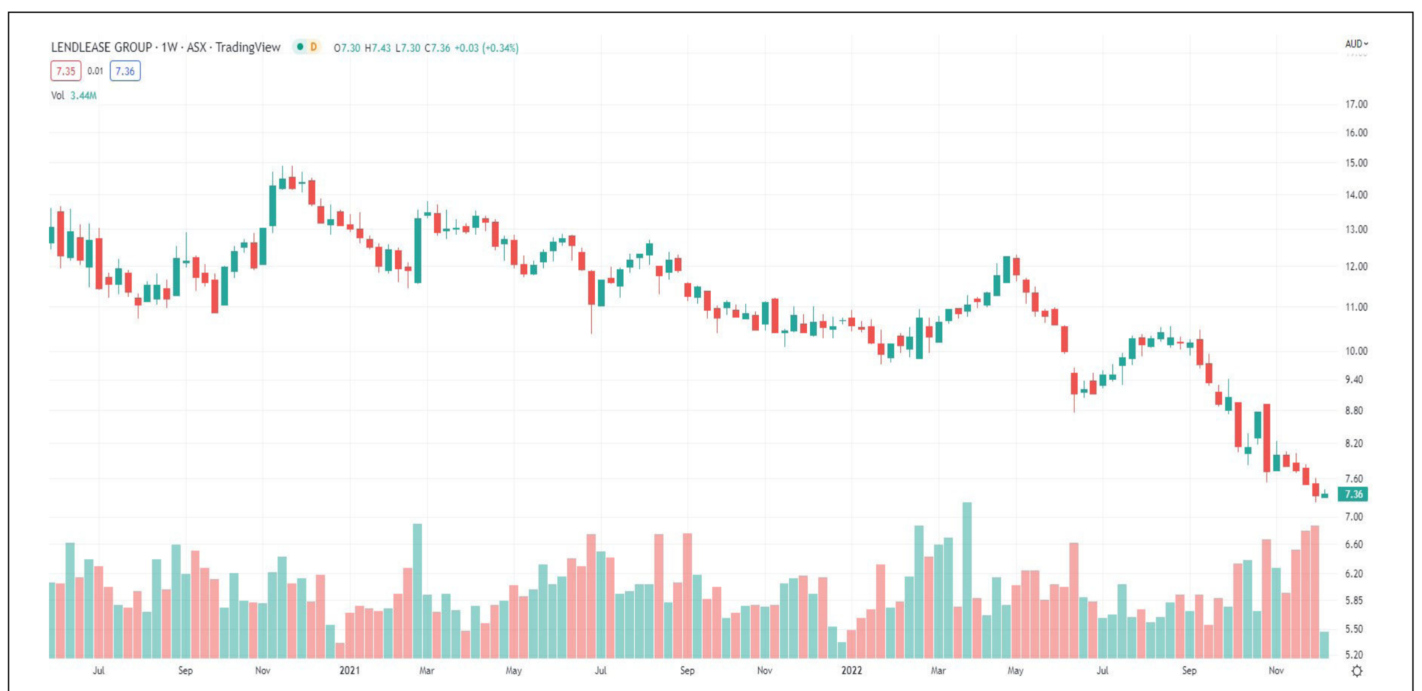
Stocks Down Under rating: ★★★★

ASX: LLC
Market cap: A$5.1BN

52-week range: A$7.22 / A$12.29
Share price: A$7.36

When we last looked at Lendlease Group in this publication on 20 September 2021 the stock was $11.48. Since then, the share price has sunk by about a third, thanks to the way in which difficulties presented by Covid impacted earnings and the 2022 interest rate increases, which have hampered the property sector globally. Better times, however, are probably coming for Lendlease in 2023. We're sticking with our four-star view.

Share price chart



Source: Tradingview

A healthy development pipeline

If you want to know why Lendlease is a long-term growth company in the property space, just look at some of the developments that it is undertaking right now. In America Lendlease will be working with Google over a fifteen-year period on four new neighbourhoods around the Silicon Valley localities of San Jose, Sunnyvale and Mountain View. In the Italian city of Milan, a 110-hectare mixed-use development called Milano Santa Giulia will see 3,400 homes go up alongside a new commercial office, retail, and entertainment district between now and 2034. And over in Singapore Lendlease is working with SingTel on a redevelopment of the Comcentre building that will complete in 2028.

What all these developments have in common is that they are large, multi-year, and iconic, and Lendlease is adding to their number all the time. Currently, the development pipeline is a healthy A$117bn spread over 47 projects, which should guarantee a decade's worth of earnings growth and then some.

Helping make global cities competitive

Comcentre, near Singapore's world-famous Orchard Road shopping area, is a good example of how Lendlease gets deals other property companies can't get. SingTel wants to recycle the capital tied up in Comcentre into more valuable opportunities. In June it announced that its 49% redevelopment partner would be Lendlease. The two companies will replace the current 32-storey building with two 20-storey buildings with Grade A

office space. The buildings themselves, however, won't be nearly as important as the precinct. Think Sydney's Barangaroo, a Lendlease flagship development from the last decade, only in a warmer climate. It will cost around S$3bn, but Lendlease will have upside on the valuable new real estate and get a heck of a lot of design, engineering and construction work in the meantime.

Lendlease is the best in the business globally at these kind of multi-year 'placemaking' developments, because it's got all the core competencies in-house, in both its Development and Construction businesses. And it's got financial strength to back it up, with a debt-light balance sheet that was only 7.3% geared at the end of FY22.

So long as there are cities looking to move up the urban value chain through major precinct redevelopment – and in 2022 you'd be hard pressed to find a city that isn't – Lend Lease will a serious global property company. Throw in the massive property investments in Lendlease's aegis – $44bn in Funds Under Management and $30bn in Assets Under Management – and this company has a lot of room to grow.

A stock below its Corona Crash lows

You wouldn't know Lendlease is a growth stock, however, from the share price. It was over $20 in August 2018, but dropped to half of that at the bottom of the 2020 Corona Crash, and it's continued to languish since then. We argue that Lendlease has gotten this low for two reasons. Firstly, earnings have been hampered by Covid and its aftermath, and secondly, no one wants to invest in property companies with interest rates going up everywhere.

Sure, FY22 was not a great year for Lendlease, with core operating profits after tax falling 27% to $276m, driven by a 61% decline in Development EBITDA and a 24% decline in Construction EBITDA. However, it's not hard to see how this happened. Part of the decline in Development earnings had to do with One Sydney Harbour, a luxury residential development project of 808 apartments in the Barangaroo South precinct of Sydney that had artificially inflated earnings in FY21. And the rest of the decline had to do with Covid. For both development and construction, the way in which the virus was managed in places where Lendlease was working tended to interfere with construction work, which in turn interfered with the timing of project completions. The second half of FY22 was much better - Development EBITDA recovered from $39m in the first half to $142m in the second half.

Bring on FY24

Lendlease is flagging that the current FY23 might still be tough – it fears that it will only get 1.5-2.5% EBITDA margins in Construction when it would like to get 2-3%. And it isn't expecting the Development business to shoot the lights out either, with Return on Invested Capital of only 4-6%. It does, however, expect to do much better in FY24.

FY23, however, will not be a total disaster. Remember, this company has made some serious cost savings, in the order of A$160m per annum. Development Work in Progress rose to a record $18.4bn by the end of FY22 and at that time the company still held $10.5bn in 'backlog revenue' for the Construction business. No wonder, then, that on consensus numbers Lendlease is expected to growth overall EBITDA by a respectable 11% in FY23 before it jumps 58% in FY24.

For all that, Lendlease is now trading at an EV/EBITDA multiple of only 6x consensus for FY24. That explains why several directors have been buying on-market in recent days – 4 of which bought over $100,000. For investors with the same kind of risk appetite and a bit of patience (albeit a different kind to that of a pre-revenue company), Lendlease remains four stars for us.

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