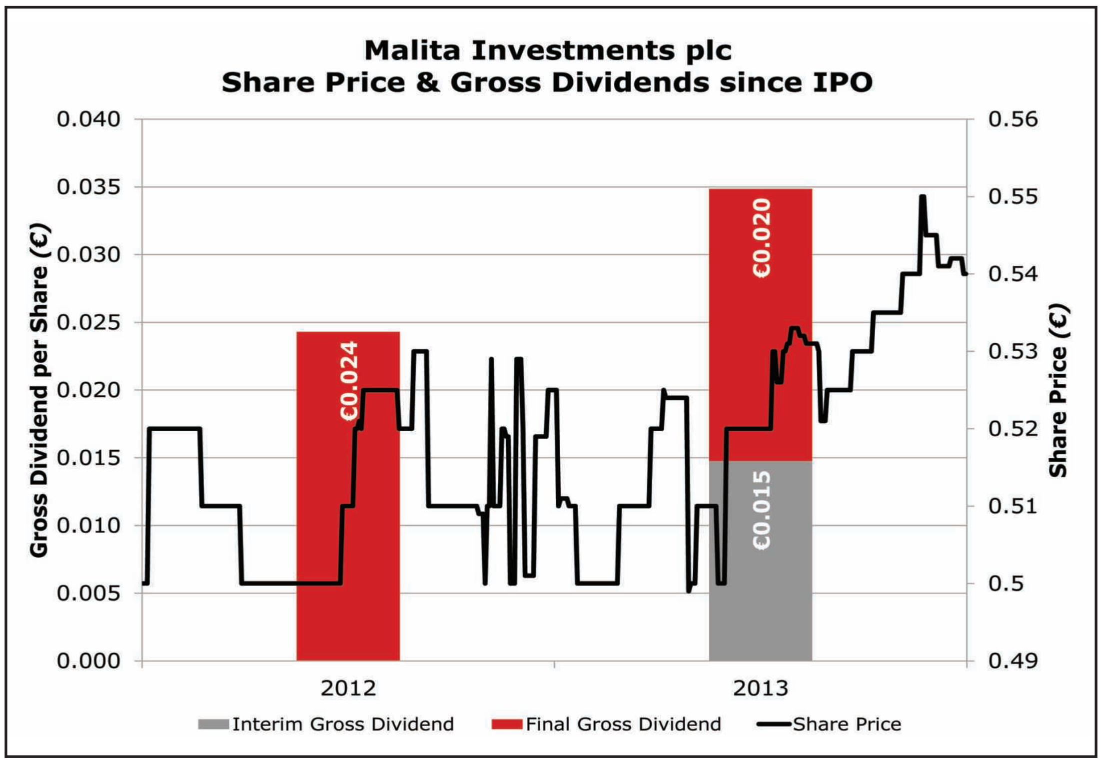
Stock Market Review

Malita Investments meets dividend expectations

Edward Rizzo

Edward Rizzo is a director at Rizzo, Farrugia & Co. (Stockbrokers) Ltd.



The financial reporting season is now in full swing. Various companies with a December year-end have already published their annual financial statements and many others will follow in the coming weeks until the deadline of April 30.

One of the companies that recently issued its financials was Malita Investments plc. It may not have made the headlines on all the media given its profile and business model. However, given that Malita is a newcomer to the market, it is worth analysing whether the company met its financial projections and expectations with shareholders.

During 2013, Malita Investments generated €6.7 million in revenue from the leases over the sites occupied by Malta International Airport (MIA) and the Valletta Cruise Port (VCP) as well as the income arising from the contractual agreements in connection with the Parliament Building and Open-Air Theatre (i.e. the City Gate Project).

The figures for 2012 do not provide a good comparison since in 2012, Malita's revenue streams were only composed of rental income from MIA and VCP. Meanwhile, during 2013, Malita was also in receipt of income related to the City Gate Project in Valletta. Although construction of the open air theatre and Parliament building was delayed, Malita was still in receipt of income due to its contractual agreements with the government. Malita in fact received income by way of the compensation mechanism in accordance with the deed drawn up with the Government dated July 26, 2012, details of which had been included in the prospectus published at the time of the Initial Public Offering in July 2012. The fines received are almost equivalent to the daily rental income due to Malita on completion of the City Gate project so the project delays did not negatively impact Malita's performance. In the company announcement issued on February 26, 2014, the directors reported that while the open air theatre was completed on October 18, 2013, works on the Parliament Building should be finished by the end of the third quarter of 2014.

Malita's board of directors convened a meeting with the financial community a few days after the announcement was issued via the Malta Stock Exchange website. Chairman Kenneth Farrugia explained that the delays were due to a number of factors, namely the complexity of the foundation, some infrastructural works which were passing through the construction site, the specifications of the stone cladding used on the Parliament building – which alone delayed the project by six months – and the wider scope of the project than the original plans due to the demolition of the police station as well as the building previously hosting Bank of Valletta.

While the revenue and expenditure figures were very much in line with projections, the 2013 financial statements also accounted for a €4.7 million uplift in the fair value of investment property. This relates to the MIA and VCP sites. A calculation was performed on the estimated cash flows due to be generated by Malita from ground rents from MIA and VCP until the end of the emphytheusis. Due to a decline in the benchmark 10-year Malta Government Stock yields since the IPO in July 2012, the higher present value attributable to the cash flows receivable by the company in the coming years was material enough for the directors to include this value in the 2013 financial statements.

This fair value adjustment, which is a not a cash movement and therefore not available for distribution to shareholders, boosted the company's profitability. It is worth noting that this could partly be reversed in the future if yields start to rise from current historically low levels.

Operating profit during 2013 surged to €11.05 million compared to the forecasts of €7.9 million, and after accounting for net finance costs of €1.02 million, pre-tax profits amounted to €10.03 million.

The statement of financial position as at December 31, 2013 shows cash balances of €12 million. However, after payments of invoices covering completion works expected in the coming months, Malita's cash position will reduce to circa €3 million. Total shareholders' funds of €82.04 million translate into a net asset value per share of €0.554. Interestingly, the increase in the share price since the IPO largely mirrors the growth in the net asset value per share.

Malita's board of directors also recommended the payment of a final gross dividend of €0.0201 per share (net: €0.0131). However, in terms of the prescribed dividend period disclosed in the prospectus, only 'B' shareholders as at the close of trading on Wednesday March 5, 2014 are eligible to this dividend. As such, the government of Malta which holds the 'A' shares (representing 80 per cent of the total issued share capital), will not be receiving this dividend. The prescribed dividend period stipulated in the prospectus runs until December 31, 2014 and therefore the government will also be foregoing the interim and final dividend in respect of the 2014 financial year.

Once the final dividend for 2013 is approved by shareholders during the upcoming annual general meeting scheduled for Wednesday April 9, it will be paid on Friday April 11.

Combined with the interim gross dividend of €0.0148 per share (net: €0.00962) which was paid to the 'B' shareholders on September 13, 2013, the total gross dividend for 2013 amounts to €0.0349. This is exactly in line with the dividend policy and the estimates disclosed in the July 2012 prospectus at the time of the IPO. This represents a gross dividend yield of 7 per cent on the IPO price of €0.50. At the current market price of €0.54 per share, the gross dividend yield is of 6.46 per cent per annum.

This is the third dividend paid by Malita since its IPO and it is interesting to note the total returns achieved by investors who acquired some shares during the IPO and who still hold on to them. The total return since July 2012 for Malita shareholders works out at 15.7 per cent comprising total net dividends of €0.0385 per share and the increase in the share price of €0.04 to €0.54. This attractive return in less than two years probably remained unnoticed by many market participants but it is an important factor when considering the success or otherwise of the Malita IPO.

Malita's future revenue streams are easily determined given the long-term contracts in place with its tenants. Importantly, rental income increases automatically in line with inflation during specific periods in terms of the lease agreements. This mechanism can be regarded as a natural hedge against inflation which is another important characteristic of Malita's equity offering.

During the recent meeting, Mr Farrugia also discussed the opportunities available to the company to expand its current operations. He in fact disclosed that the company's investment committee is currently performing funding and investment appraisals for two new possible projects. One of the projects is related to national heritage while the other is an urban regeneration project. The chairman noted that the funding required to undertake these projects, amounting to between €10 million and €20 million, could be through a mix of equity and debt financing. Mr Farrugia also felt the need to highlight that any decision on the new projects would not negatively impact the dividend policy of the company. He explained that dividends to shareholders were one of the critical factors being taken into consideration by the investment committee when assessing the viability of new projects.

During the open discussion that took place at the meeting, another interesting aspect was brought up and which had possibly failed to be highlighted at the time of the IPO. The chairman of Malita indicated that the ground rents to be received from MIA and VCP could be revised upwards in the future in the event that any of these companies undertake further investments on the sites owned by Malita. This could provide additional rental income to Malita given the ambitions of both these tenants to expand their present business activities.

The success achieved by Malita since its IPO both in terms of the support from the investing public (especially from institutional investors) as well as in the total returns provided to shareholders should instigate other similar property-related companies to also consider a Stock Exchange listing. Despite the various new bond issues expected to hit the market in the coming months, there is also a need for such property IPOs to satisfy the demand from the ever-growing investor base in Malta.

In addition to Malita, two other companies have similar business models, i.e. Plaza Centres plc and Tigne Mall plc. The business models of companies with sustainable and rising income streams provide a natural hedge against future inflation and there will be a growing need by institutional investors for exposure to investments with such characteristics.

The market now awaits the financial results of Tigne Mall plc in the coming weeks to also verify whether this company too has met its forecasts presented at the time of the IPO last year. It is also expected to initiate dividend payments to shareholders as indicated in the IPO Prospectus.