

Macau Property Opportunities

Beginning to gain traction

21 October 2009

The Macau Property Opportunities Fund has made significant progress since launch, notwithstanding the most brutal of economic backdrops and a relatively immature portfolio. We are now entering a key phase in the development of both Macau and the company. Having just completed on its largest investment and with a number of its projects in the advanced stages of the planning process, we believe it is well positioned for a re-acceleration of growth in the region. We initiate coverage with a BUY recommendation.

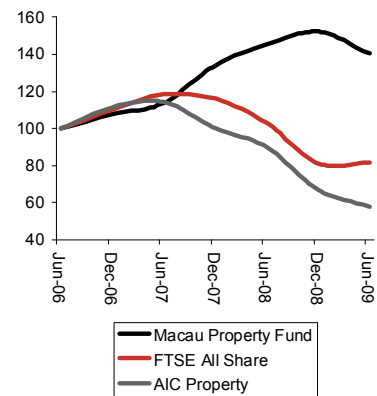
Current market stats at cob 20 October

Price	95p
Adjusted NAV @ 30 June 2009	136p
Discount	30%
Property portfolio as % of NAV	117%
Market capitalisation	£100m
Manager	Sniper Capital Limited
Web page	www.mpofund.com

Source: Fundamental Data

Solid foundations: The compound growth in the NAV since launch in 2006 is 12.2%. Over the same period, the MSCI Far East ex Japan total return index has increased by an annualised 7.9% while the UK property sector has delivered an annualised compound NAV total return of -16% (all sterling adjusted). All properties in the portfolio have been the subject of upward revaluations, and in many cases, these have been significant.

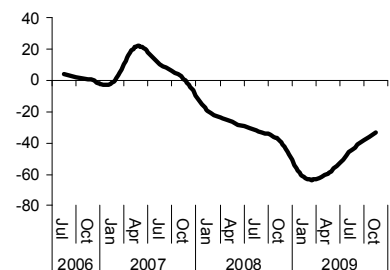
NAV total returns (£ adj, base = 100)



Source: Thomson Financial Datastream

Strategically positioned portfolio: The manager pursues a rigorous investment process and has constructed a balanced property portfolio in terms of the stage of development. While there is some exposure to the retail and logistics sector, there is a strong bias towards residential property. Most notably, the company has a significant investment in the prestigious One Central development, which currently represents 67% of NAV, where it has just taken delivery of 59 units. Given a supply/demand imbalance for ultra-high quality developments in Macau, there is undoubted potential for material upward revaluations of this investment. In recent months, Hong Kong property prices have outperformed and consequently Macau prices now stand close to a 60% discount to their neighbours; the manager expects this to narrow as international and mainland capital flows into Macau. Notably, there has been a significant increase in transactions recently.

Rating (%)



Source: Thomson Financial Datastream

Where is the risk? Given the embryonic characteristics of the local economy we acknowledge the associated risks. That said, with the UK now ranked 37th in terms of overall financial stability in the recent World Economic Forum, and with the LTV of the UK commercial property market at 106%, and with much of the outstanding debt due to be re-financed in the next 18 months (the elephant in the room), and with many UK commercial property funds on demanding premia, we continue to wonder where the real risks lie.

Current discount represents compelling opportunity: Although there has been a strong recovery this year, the shares still trade on a discount of 30% to the end-June NAV (and we would expect the NAV to have made good progress since then). The board is continuing to assess measures to address the current rating and measures include a potential move from the AIM to the main market and/or a dual listing in Hong Kong. In addition, we take comfort that the managers are now one of the largest investors in the fund, and indeed, have been increasing their investment in recent months.

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Macau Property Opportunities Fund

Investment objective

To deliver long-term returns from high quality property developments in carefully selected niche markets in Macau and China's Pearl River Delta.

History

The company raised £105m when launched in June 2006. It is a Guernsey registered closed-end fund traded on AIM.

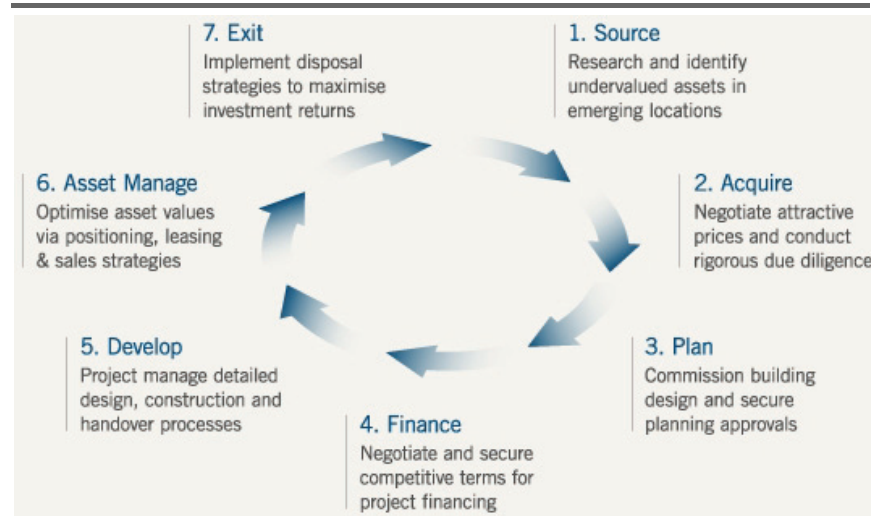
Management

Sniper Capital Limited has managed the company since launch. It was established in 2004 to capitalise on the many property development and investment opportunities offered by Macau's growing economy. The property portfolio has since been expanded to include the Western Pearl River Region of Southern China.

The founding partners are Tom Ashworth and Martin Tacon and the team consists of 20 dedicated professionals, who are responsible for design, engineering, environmental and construction management. Sniper Investments, an investment vehicle associated with the manager has increased its shareholding significantly in recent months and it now owns 4.5% of the shares in issue.

The focus is on the identification of undervalued property opportunities in emerging and high growth niche markets. Such sectors are typically where larger developers are less active and where a lack of local expertise excludes most foreign investors. One of the manager's core strengths is the ability to exploit mispriced opportunities and create added value through imaginative development skills and active asset management. The projected IRR's of the current portfolio range between 20% and 25%. During the investment phase the managers looked at 130 potential projects and invested in just five.

Managers pursue a rigorous investment process



Source: Sniper Capital

Web page – www.snipercapital.com

Management fee/contract

The management fee is 2% per annum of net assets. There is a performance fee of 20% of the increase in NAV above a hurdle (based on the placing price at launch, compounded at 10%). The performance fee is also subject to a high watermark.

There is also a super performance fee of 15% of the excess return over a super performance hurdle – this is the placing price, compounded at 25%. This is also subject to a high watermark.

The management contract is terminable on one years' notice. A continuation vote will be proposed at the AGM in 2014.

Macau

Macau is a Special Administration Region of China and operates under the policy of "one country, two systems"; the transfer of sovereignty was completed in December 1999. Macau is located in the Pearl River Delta, which has a population of 60m, produces a third of Chinese exports and has the highest per capita GDP in China. In December, Macau will celebrate the 10th anniversary of the handover, and it will also appoint a new Chief Executive Officer, Fernando Chui Sai On, a pro-Beijing businessman.

Macau is the only location in China where gambling is legal and this has been a key component of the spectacular economic growth in the past 10 years. In just a few years, Macau has established itself as the top gambling destination in the world. Its annual gaming revenues exceeded Las Vegas for the first time in 2006 and since that time, these two destinations have experienced widely different fortunes.

Earlier this year, the Chinese government loosened visa restrictions to allow mainland tourists to visit Macau once a month rather than once every six months. There has been a strong recovery in gaming revenues in recent months; in the third quarter, revenue was 22% ahead of the comparable period in 2008. Meanwhile, hotel occupancy in August was 80%, the highest level since the end of 2007. The administration is looking to diversify the economy and in the past couple of years, there have been a number of convention centres and high-end shopping centres opened.

In recent weeks, the profile of Macau has been raised further through a number of IPO's; Wynn Resorts has raised US\$1.9bn, while Las Vegas Sands has applied for a Hong Kong IPO, which may take place as early as next month and raise up to US\$2.5bn. Over the next few years, there are plans to open several new casinos.

Additionally, there are several infrastructure projects planned. In addition to the expansion of the airport and a permanent ferry terminal, work will start shortly on a bridge linking Macau to Hong Kong and also a mass transit system within Macau.

Hong Kong-Zhuhai-Macau Bridge

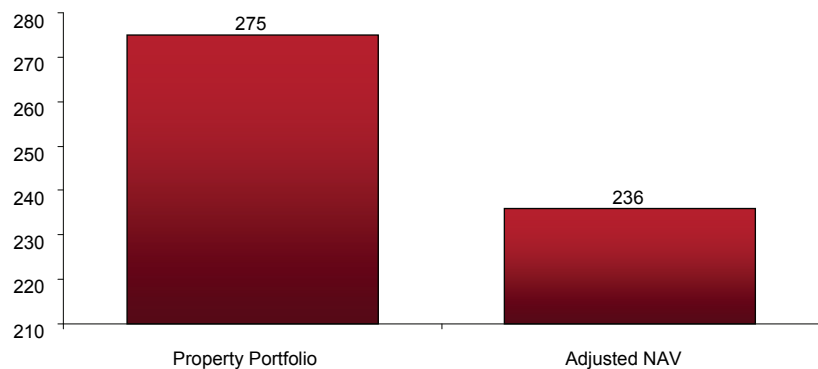
The Hong Kong-Zhuhai-Macau Bridge is a series of bridges and tunnels which will connect Hong Kong to the mainland Chinese city of Zhuhai. The bridge will be 29km long and will reduce road travel between Macau and Hong Kong from 4½ hours to 40 minutes. It is expected that construction will begin shortly and will be completed by 2016. The project will be 42% funded by the governments of Guangdong, Hong Kong and Macau, with the balance from the Bank of China.

Light Rapid Transit System

Macau's Light Rapid Transit will consist of two tracks connecting the Macau Peninsula with Taipa and Cotai. There will be over 20km of track and 21 stations. Work is expected to begin next year, with the first phase operational by 2013.

Balance Sheet

Property portfolio/Adjusted NAV (US\$m)



Source: Company data

The adjusted NAV reflects the fair value of the underlying properties rather than the lower of cost and net realisable value. The portfolio is re-valued every six months by Savills (Macau) Limited.

The company has a US\$82m loan from a consortium of banks led by HSBC. The full amount was drawdown on the handover of One Central. The loan is repayable in four stages: 10% of the principal is due in November 2010 and May 2011, 15% is due in November 2011, with a balloon repayment of 65% in May 2012. Interest is payable at HIBOR (currently 23 basis points) plus 2.4% per annum and there is an annual commitment fee of 80 basis points.

The LTV ratio at the end of June 2009 was 25.5% (the LTV covenant is 55%), and in the third quarter, the cash balance fell from US\$47m to US\$43m.

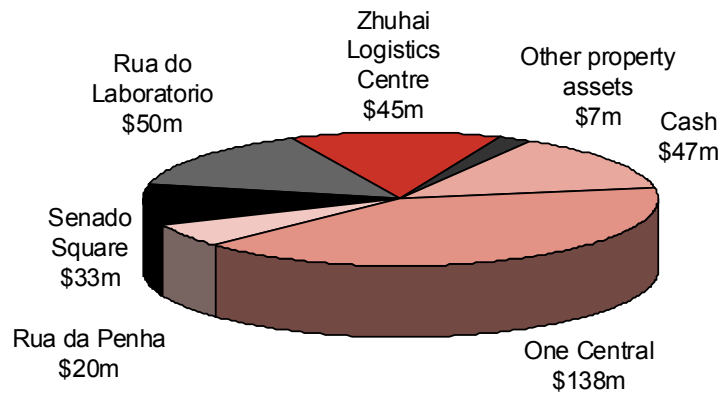
Property portfolio at 30 June 2009

Property investments

Property	Sector	Acquisition date	Projected IRR	Valuation @ 30 June 2009 (\$m)
One Central	Residential - high-end	Nov-06	23	158.8
Rua do Laboratoria	Residential - entry level	Nov-06	20	38.2
Senado Square	Mixed-use	Oct-07	22	33.2
Rua da Penha	Residential - niche	Oct-06	25	21.9
Zhuhai Logistics	Warehousing & Logistics	Aug-08	23	12.9
Other				10.3
Total				275.3

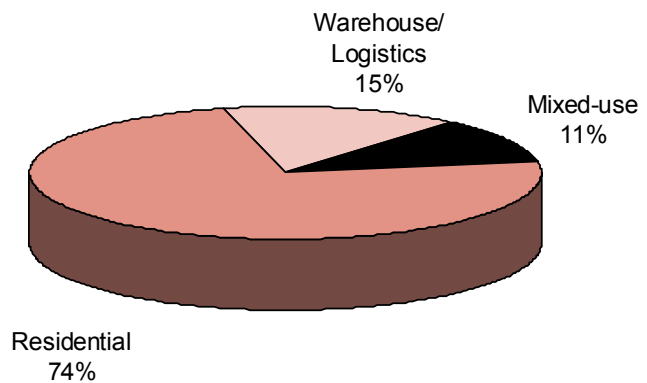
Source: Company data

Portfolio composition (based on total commitment costs)



Source: Company data

Sector exposure (based on total commitment costs)



Source: Company data

One Central Residences

End-June valuation: US\$159m, 67% of NAV

One Central Residences was developed by Hong Kong Land and Shun Tak Holdings and is Macau's premier mixed-used development. It comprises seven high quality residential towers, a Mandarin Oriental Hotel (which will open shortly) and a shopping centre, aimed at the upper end of the market.

The company acquired the whole of Tower Six, comprising 59 units, in November 2006 and it also owns 25 individual units in the rest of the development. Tower Six was handed over in August 2009 and the manager is now looking to further enhance these units. They are working with a highly regarded Japanese design company, Glamorous Co. Ltd, to advise on the interior design.

It is expected that all units in Tower Six will be available for lease by the end of this year and the managers are already in discussions with several potential corporate tenants. The transaction was partly financed by the \$82m loan mentioned above.

The handover of the other 25 units is currently underway and the manager will look to adopt an opportunistic strategy with regards to timing of exit. These units are typically located on higher floors and accordingly they will command a premium.

The end-June valuation of Tower Six represents a valuation of cHK\$5,800 per square foot (eqUS\$750 or eq£460). We would note that this headline number is boosted by five "special" units in Tower Six, which command premiums of 80-100% above that of standard units. The managers expect cash rich mainland buyers to drive prices higher by the end of the year.

Rua do Laboratorio

End-June valuation: US\$38m, 16% of NAV

Originally acquired in November 2006, the managers are currently seeking planning permission to demolish the existing building and replace it with a high rise residential block targeting the entry level market. Earlier this year, the Macau SAR government introduced a package of incentives designed to help first-time buyers (including a subsidised mortgage) and broaden demand for mass-market residential properties.

Located in Northern Macau, this property is close to the Chinese border and residents will have easy access to Zhuhai. In addition, the property will be close to the Light Rapid Transit system, when it becomes operational. The original cost was \$21m and the projected development cost is a further \$29m, representing a total commitment of \$50m.

The managers are hoping to begin construction in the next few months with building completed by the end of 2011. It is the intention to pre-sell these units, beginning in the first half of that year.

Senado Square

End-June valuation: US\$33m, 14% of NAV

Senado Square is a mixed-use development project located in the heart of Macau's tourist district. The original investment was made in October 2007 and the intention is to construct a multi-level retail complex. The project is at the advanced planning stage with demolition of the existing site and construction scheduled for the next few months. The managers expect building work to be completed in 2011 at which point they will look to lease up the units and then sell.

The site was acquired for \$16m with projected development costs of a further \$17m.

Rua da Penha

End-June valuation: US\$22m, 9% of NAV

The company is looking to re-develop this property, which is a low-level residential block; when completed, the target buyer will be local residents looking to upgrade. The project is at the advanced stages of planning and it is hoped that construction will begin early in the New Year, with completion by end-2010/early-2011.

The existing property was acquired in October 2006 for \$8.6m, with a further \$11.4m planned for development costs.

Zhuhai Logistics Centre

End-June valuation: US\$13m, 5% of NAV

The company made its first investment in mainland China, in a government supported development area, in August 2008. The intention is develop this 1.1m square foot site into warehouse facilities and accommodation for local workers, the project is scheduled to be completed in 2011/2. The site will be well located to benefit from the Hong Kong-Zhuhai-Macau bridge.

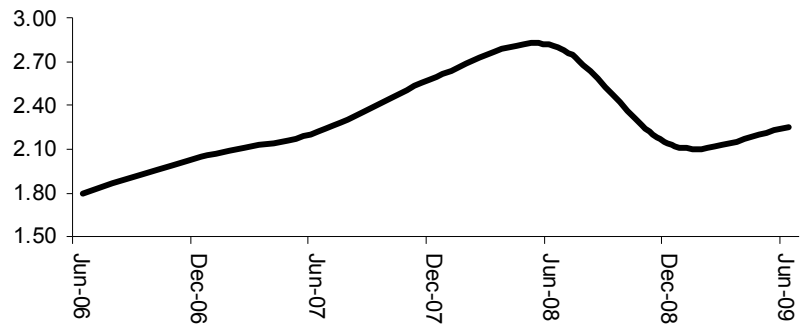
The original acquisition cost \$11m while additional development costs will be around \$34m.

Other Property Assets

End-June valuation: US\$10m, 4% of NAV

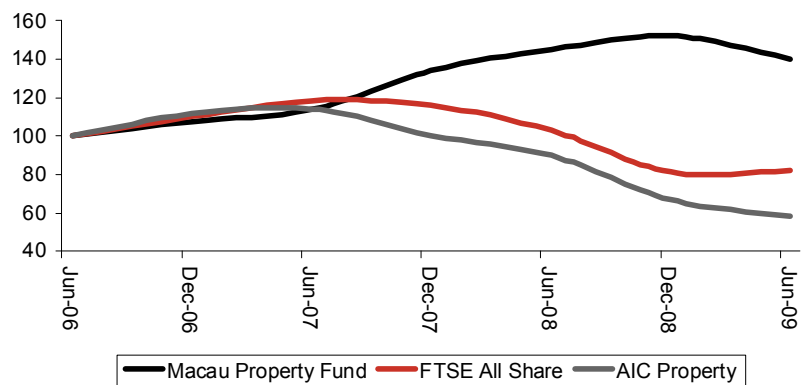
Performance

Macau Property Fund – adjusted NAV (\$ per share)



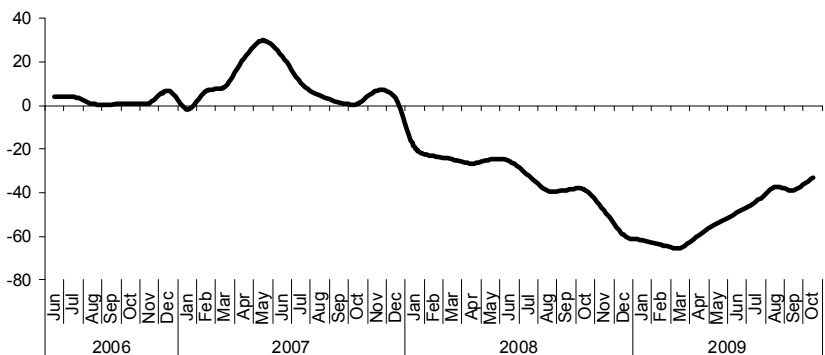
Source: Company data

NAV total return (£) – Macau Property Fund vs FTSE All Share/AIC Property



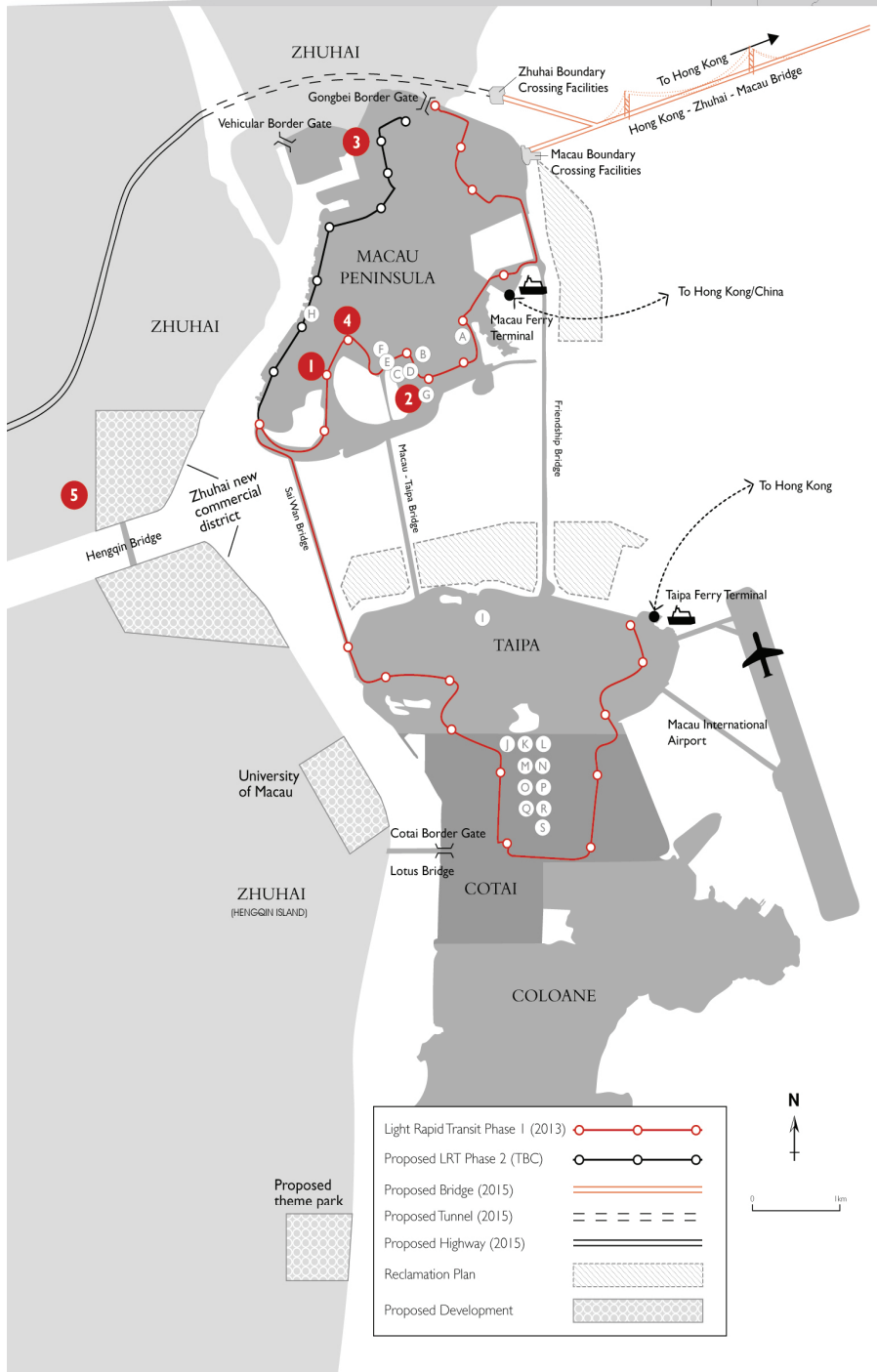
Source: Company data/Thomson Financial Datastream

Discount



Source: Fundamental Data

MACAU AND SURROUNDING AREA



- MPO'S KEY PROPERTIES**
- 1 Rua da Penha
 - 2 One Central
 - 3 Rua do Laboratório
 - 4 Senado Square
 - 5 Zhuhai Logistics Centre

- MAJOR CASINOS ON MACAU PENINSULA**
- A Sands Macao (2004)
 - B Starworld (2006)
 - C Wynn Macao (2006)
 - D Wynn Encore (2010)
 - E Lisboa (1970)
 - F Grand Lisboa (2007)
 - G MGM Grand Macau (2007)
 - H Ponte 16 (2008)

- MAJOR CASINOS ON COTAI**
- I Altira Macao (2007)
 - J Galaxy Mega Resort (2010)
 - K Venetian Macao (2007)
 - L City of Dreams (2009)
 - M Four Seasons (2008)
 - N Shangri-La*
 - O Far East Consortium*
 - P Sheraton & St. Regis*
 - Q Macao Studio City*
 - R Hilton & Conrad*
 - S Fairmont & Raffles*
- * Under planning

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Recommendations	Buys	Sells	Hold/Neutral
Percentage of Total	47%	17%	36%
Percentage of which in Corporate Client stocks	13%	0%	5%

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