

The Star Biz

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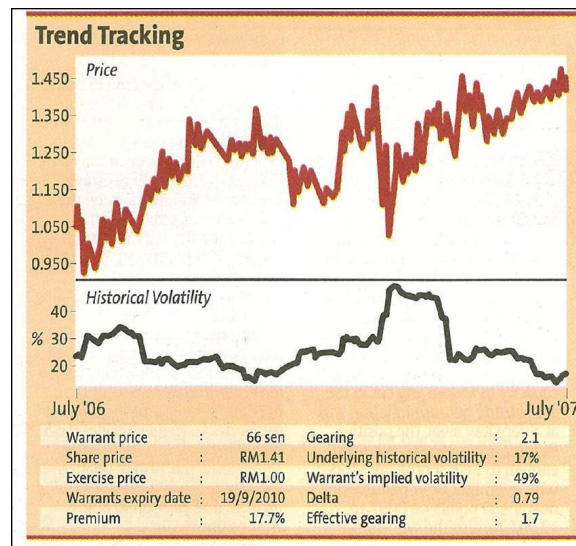
Maemode-WA may trade ahead of results announcement

By ALAN VOON, a warrants specialist

ONE of the most effective ways to trade warrants is to buy ahead of results announcements. This is especially useful when there is some analysts' coverage on the underlying company. When the results announced are above expectations, there are bound to be upgrades and if results are below expectations, the underlying share may come under pressure. Nevertheless, volatility of the underlying share is expected to increase just prior to and after results announcement.

In more developed markets, there are people who trade on just the volatility of the share price.

Malaysian AE Models Holdings Bhd (Maemode) is one such underlying share whose warrants fit the description. The company is expected to announce its latest financial year results by the end of the month and there seems to be a fair amount of anticipation, judging from the interest in the underlying share and the warrant. Nevertheless, the underlying share was trading within a tight range lately, closing at RM1.41 at the time of writing. Maemode-WA was trading at 66 sen.



Maemode is predominantly involved in the design, manufacture, installation and marketing of materials handlings and factory automation systems and components.

The company has been experiencing rapid profit growth over the last couple of years with net profit growth rate in excess of 30%.

For the first nine months of FY07 (ended February), Maemode achieved net profit of RM13.9mil against RM7.9mil recorded in the previous corresponding period. The gain of almost 80% has not gone unnoticed by the research houses. Standard & Poor's and SJ Securities, which cover the company under the CMDF-Bursa Research Scheme, have a buy rating on Maemode with target prices of RM1.80 and RM2.15 respectively in their latest reports. As at February 2007, Maemode's net asset per share was RM1.71 and its earnings per share for first nine months exceeded 14 sen per share.

For traditional break-even analysis, Maemode-WA is trading at a premium of about 17%. This is not high for a growth stock like Maemode as the warrant's expiry is more than three years away. Warrant holders also do not suffer much from non-entitlement of dividend as the company is at a growth phase and does not pay much dividend.

From a trading point of view, Maemode-WA is now trading at an implied volatility of 49%, which is higher than its mother share short-term historical volatility of only 17%.

Maemode's underlying share volatility is close to its 52-week low now and with results announcement soon, an expansion in volatility can be expected. This suggests that the warrant is already anticipating some upward movement in the underlying share.

Maemode-WA has a Delta value of 0.79. This means that for every 10 sen movement in the underlying share, Maemode-WA should move 7.9 sen in theory.

As warrants prices do not move cent-for-cent with the share price, the simple gearing factor is not an accurate measure of actual gearing. We should multiply the simple gearing by the warrant's Delta value to get a more accurate measure of leverage. For Maemode-WA, the effective gearing of is 1.7 times, which is the product of gearing (2.1) and delta (0.79).

With an effective gearing of 1.7 times, Maemode-WA provides traders an out-performance margin of 70% over that of the mother share should Maemode makes an upwards movement. Traders who are bullish on Maemode may consider the warrant if their risk appetite is strong.

If the underlying share ever reaches the target prices mentioned by the brokers, Maemode-WA can indeed be rewarding for its believers.

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