InsiderAsia

by Asia Analytica

3Q FY2016 results update

1 Dec 2016

Muhibbah Engineering (M) Bhd

- 9-months results in line, boosted by tax benefits
- Provisions of RM15.6m at Favco drag operating earnings
- Concessions, RM1.7b orderbook to sustain earnings
- Oil prices recovering, attractive valuations. Maintain BUY

BUY

Share price
RM2.20

Market capitalization
RM1,057 million

Board
Main

Indices
FBM Emas Syariah,

Sector
Construction

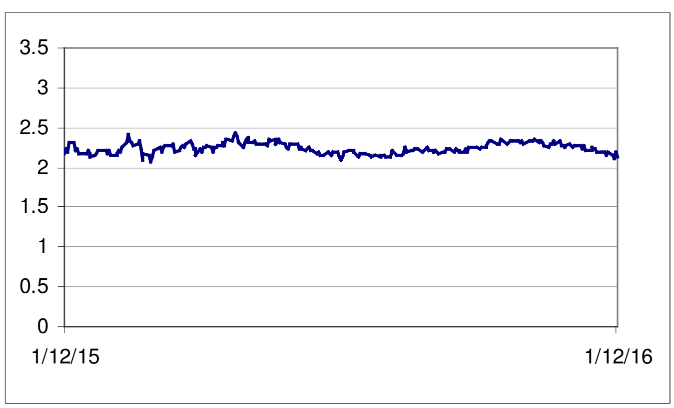
Stock code
5703

By
The Research Team

Key stock statistics	FY Dec15	FY Dec16E
EPS (sen)	18.7	20.1
P/E (x)	11.8	11.0
DPS (sen)	5.0	5.0
NTA/share (RM)	1.75	1.86
Issued capital (mil)	480.5	
52-week price range (RM)	2.08 -2.52	

Major shareholders (%)	
Mac Ngan Boon	20.7%
Lembaga Tabung Haji	9.6%

Share Price Chart



9M FY2016 Results highlights

Year end Dec (RM mil)	9M-2016	9M-2015	% chg
Turnover	1,273.0	1,314.1	(3.1)
Pre-tax profit	104.4	127.3	(18.0)
Tax	(11.0)	(29.9)	(63.3)
Minority interests	(20.2)	(31.9)	(36.5)
Net profit	73.1	65.5	11.6
EPS (sen)	15.43	14.43	
Pre-tax profit margin (%)	8.2	9.7	
Net profit margin (%)	5.7	5.0	

Muhibbah Engineering's results for the third quarter and the first nine months of FY Dec 2016 were within our expectations, although largely boosted by a tax write-back. Net profit for 9M2016 of RM73.1 million came in at 76% of our full year forecast of RM96.8 million.

For 3Q2016, Muhibbah posted net profit of RM22.6m million, broadly similar to RM23 million a year ago, despite a 28.8% decline in revenue to RM385 million, the latter mainly due to timing issues of project revenue recognition.

For the first nine months of 2016, net profit rose 11.6% to RM73.1 million, although pre-tax profit declined 18% to RM104.4 million while revenue fell 3.1% RM1.273 billion.

The disproportionate growth in net profit was due to lower effective taxes, as Favelle Favco received tax incentives. Favco reported a net tax write-back of RM4.3 million in 3Q2016, which resulted in it achieving net profit of RM23.2 million for the quarter. Muhibbah as a group reported a tax write-back of RM5.3 million in 3Q2016, which reduced its 9-month effective tax rate from 24% to 11%.

The tax write-back aside, Muhibbah was operationally affected by weaker earnings at Favco and its concession businesses.

Favco saw its pre-tax profit more than halved from RM40.4 million to RM18.7 million due to impairment on receivables of RM15.6 million. Favco supplies about 80-90% of its cranes to the oil & gas industry, and has been affected by the oil & gas industry's downturn.

For 3Q2016, Muhibbah's after-tax contributions from associates declined 15.4% y-y to RM12.2 million. This reflects its concession business, comprising an effective 21% stake in the three Cambodian airports (Phnom Penh, Siem Reap and Sihanoukville), and a 21% stake in Roadcare (M) Sdn Bhd, which holds a 10-year concession (valid until 2026) for the maintenance of over 7,000 km of federal roads in central peninsular Malaysia.

Outlook and recommendation

We maintain our **BUY** recommendation and forecasts. We continue to like Muhibbah for its attractive valuations, well-diversified earnings base, with medium term earnings visibility backed by its RM1.65 billion order-book.

Following OPEC's move to cut output, crude oil prices have again reached the US$50 per barrel mark. With signs of oil prices having bottomed out and starting to recover, the outlook for Muhibbah's oil & gas related businesses, particularly Favco and other oil and gas related capex, should improve.

Muhibbah's order-book stood at RM1.65 billion as at 22 Nov 2016, down 10% from RM1.87 billion as at 22 Aug 2016. Of the order-book, RM969 million are for infrastructure construction works, RM634 million for cranes and RM48 million for the shipyard. Some 59% of the order-book is for jobs in Malaysia.

We expect Muhibbah's net profit to grow 13.1% to RM96.8 million in 2016 and 9.2% to RM105.7 million in 2017. Post the proposed (but yet to be implemented) placement exercise, EPS is projected at 20.1 sen and 20.4 sen for 2016-2017, respectively. The stock is currently trading on low P/E multiples of 11 and 10.8 times for 2016-2017, respectively.

The outlook for the oil and gas industry remains challenging, with the prolonged downturn affecting the financials of oil & gas players and curtailing capital spending. On a positive note, crude oil prices have rebounded from lows of US$30 per barrel, and reached US$50 per barrel yesterday on news OPEC had reached a deal to cut oil production.

However, it is also unclear if the uptrend is sustainable as many fear soon-to-be inaugurated President Donald Trump may give more benefits to boost shale production to improve energy self-sufficiency for the US.

While the oil and gas slowdown has affected Favco more than other divisions, Muhibbah's infrastructure construction division has been largely unaffected due to its focus on the US$27 billion RAPID project in Pengerang, for which contracts have been awarded since mid-2015 and construction is ongoing. The refinery is expected to be completed in 2019 and is largely unaffected by Petronas' capex cuts.

In June 2016, Muhibbah entered into an agreement with Perbadanan Setiausaha Kerajaan Pahang for the proposed acquisition of a 99-year leasehold land measuring 500 acres in Kuantan, Pahang, for RM26.45 million, or just RM1.21 psf. The land would be developed into the proposed Kuantan Maritime Hub over a period of 10 years. The acquisition provides an opportunity to develop industrial activities for ship building, ship repair works and major fabrication offshore structure in Kuantan.

The land is strategically located about 20km from Kuantan town, and just 5 km from Kuantan Port, which is owned by IJM Corp and Guangxi Beibu.

Meanwhile, the Cambodian airport concession operations are providing steady earnings and a major growth impetus. Earnings are derived in USD and the airports are benefitting from rising passenger traffic and a recently completed expansion exercise.

Arrivals at the three Cambodian airports have grown a robust 13% per year for the last two years, reaching 6.5 million arrivals in 2015. For the first nine months of 2016, arrivals into the Cambodian airports rose 6% to 5.02 million passengers, led by a 9% growth in Phnom Penh and 3% in Siem Reap.

Future growth will be underpinned by a recently completed capacity expansion at the two main airports and over time, more arrivals at the southern port and beach city of Sihanoukville as more flights are added.

In March 2016, additional terminal buildings for the Phnom Penh and Siem Reap airports were officially opened. This has doubled the collective annual capacity of its three Cambodian airports from 6 to 12 million passengers.

Profit & Loss Analysis

Year end Dec (RM mil)	2014	2015	2016E	2017E
Turnover	1,733.6	1,599.0	1,660.0	1,645.0
EBITDA	178.8	204.5	181.5	213.2
Depreciation	(55.8)	(55.7)	(57.0)	(60.0)
Associates	49.2	62.2	76.0	84.0
Interest income/(exp)	(28.5)	(42.7)	(42.0)	(40.0)
Pre-tax profit	143.7	168.3	158.5	197.2
Tax	(24.8)	(31.4)	(31.7)	(39.4)
Minorities	(37.3)	(51.3)	(30.0)	(52.0)
Net profit	81.6	85.6	96.8	105.7
Operating margin (%)	10.3	12.8	10.9	13.0
Pre-tax margin (%)	8.3	10.5	9.5	12.0
Net margin (%)	4.7	5.4	5.8	6.4
Effective tax rate (%)	17.3	18.7	20.0	20.0

Per Share Data

Year end Dec	2014	2015	2016E	2017E
EPS (sen)	19.2	18.7	20.1	20.4
P/E (x)	11.4	11.8	11.0	10.8
Dividend (sen)	4.0	5.0	5.0	5.0
Dividend yield (%)	1.8	2.3	2.3	2.3
Payout ratio (%)	21	27	25	24
Book value (RM)	1.50	1.75	1.86	1.89
Price/Book value (x)	1.47	1.25	1.18	1.16
Cashflow/share (sen)	29.2	27.7	22.3	25.8
Price/Cashflow (x)	7.7	8.1	10.1	8.7
Gearing (%) (excluding bills payables)	21	18	16	15
ROE (%)	12.7	10.4	10.8	10.8

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