

Malaysia Company Guide

Muhibbah Engineering

Version 4 | Bloomberg: MUHI MK | Reuters: MUHI.KL

Refer to important disclosures at the end of this report

DBS Group Research . Equity

1 Jun 2016

BUY

Last Traded Price: RM2.19 (KLCI : 1,626.00)

Price Target : RM3.10 (42% upside)

Potential Catalyst: Chunkier higher margins wins, higher order for cranes

Where we differ: Our earnings are below consensus

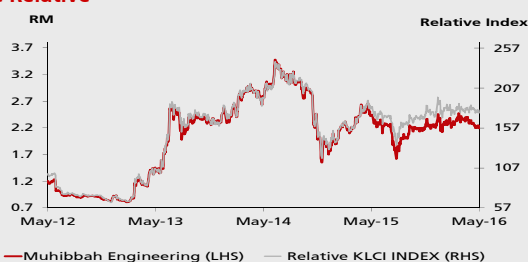
Analyst

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What's New

- 1Q16 results within expectations
- Gunning for more RAPID projects
- Shipyard orders could surprise on the upside
- BUY, TP of RM3.10 based on SOP

Price Relative



Forecasts and Valuation

FY Dec (RM m)	2015A	2016F	2017F	2018F
Revenue	1,605	1,754	1,781	1,707
EBITDA	251	225	251	267
Pre-tax Profit	165	149	177	195
Net Profit	86.0	99.8	117	128
Net Pft (Pre Ex.)	86.0	99.8	117	128
Net Pft Gth (Pre-ex) (%)	5.4	16.1	17.1	9.7
EPS (sen)	18.2	20.7	22.6	24.7
EPS Pre Ex. (sen)	18.2	20.7	22.6	24.7
EPS Gth Pre Ex (%)	5	13	9	10
Diluted EPS (sen)	36.5	20.7	22.6	24.7
Net DPS (sen)	3.98	4.13	4.51	4.95
BV Per Share (sen)	175	199	204	224
PE (X)	12.0	10.6	9.7	8.9
PE Pre Ex. (X)	12.0	10.6	9.7	8.9
P/Cash Flow (X)	33.5	13.6	9.4	7.0
EV/EBITDA (X)	7.9	9.0	8.3	7.6
Net Div Yield (%)	1.8	1.9	2.1	2.3
P/Book Value (X)	1.2	1.1	1.1	1.0
Net Debt/Equity (X)	0.6	0.5	0.4	0.3
ROAE (%)	11.7	11.2	11.6	11.6
Earnings Rev (%):		0	0	0
Consensus EPS (sen):		22.0	25.3	29.5
Other Broker Recs:		B: 6	S: 0	H: 0

Source of all data: Company, AllianceDBS Research, Bloomberg Finance L.P

Scarcity premium infrastructure proxy

Scarcity premium. Muhibbah is an ideal proxy to the 11th Malaysian Plan given its expertise in three core areas: i) civil engineering; ii) marine-based construction, and iii) offshore and onshore fabrication works, where its Petronas licence offers an advantage. Other contractors do not have this combination to vie in the competitive civil engineering space.

Cash cow: Cambodia airport concession. Siam Reap and Phnom Penh airports have doubled their capacity to 12m passengers. Passenger arrivals grew 13% to 6.5m passengers in FY15. We estimate its 21% stake in the Cambodia airport concession is worth RM677m (DCF, WACC 10%, RM/USD4.15, and average passenger traffic growth of 5% p.a. until 2040), which is already 63% of the stock's market capitalisation. Revenues are also in USD which is a boost to its earnings given the weak MYR.

Good start for 2016. Contract flows so far for 2016 have been promising. For its infrastructure division, it has won two contracts, a RM137m building contract from PETRONAS Carigali, in which it has a 70% stake, implying a contract value of RM96m and a smallish contract for the Phnom Penh airport expansion. For its shipyard division, it clinched a RM92m contact win from the Ministry of Transport to undertake the design and construction of Multi-Purpose Vessel for the Malaysia Marine Department. Its total outstanding orderbook is now RM2.5bn, of which RM1.75bn comes from infrastructure.

Valuation:

Muhibbah is a BUY with a SOP-derived TP of RM3.10. We value the stock based on SOP as we think it better reflects its diversified business while also capturing its cash-generating Cambodian concession.

Key Risks to Our View:

Delay in project flows and sudden spike in raw material costs could dampen its earnings outlook.

At A Glance

Issued Capital (m shrs)	472
Mkt. Cap (RMm/US\$m)	1,034 / 251
Major Shareholders (%)	
Mac Ngan Boon	22.1
Lembaga Tabung Haji	9.6
Free Float (%)	60.7
3m Avg. Daily Val (US\$m)	0.31

ICB Industry : Industrials / Construction & Materials

Muhibbah Engineering

WHAT'S NEW

Decent start to the year

In-line 1Q16 showing. 1Q16 recorded a headline net profit of RM24m (+2% y-o-y, +18% q-o-q) which was in line with our estimates.

Strong quarter for construction and shipyard. Muhibbah's construction arm saw a strong quarter, with 1Q16 pretax profit up 2.6-fold y-o-y to RM30m. This was on the back of a 3% increase in revenue to RM531m. Hence, 1Q16 margins expanded by close to 1ppt y-o-y to 5.6% but were lower than the 6.6% recorded in 4Q15. The crane business under Favelle Favco showed weaker growth with a pretax profit of RM19m (-38% y-o-y). This is unsurprising as it runs down its orderbook which currently stands at RM604m. Meanwhile, shipyard pretax profit surged to RM2m in 1Q16 vs RM0.6m in 1Q15. We expect growth in the subsequent quarters to be buoyed by its Ministry of Transport contract.

Associates. 1Q16 associate profit (largely its Cambodian airport concession) was up 12% y-o-y to RM18m. This was driven by traffic volume growth of 5% to 2m passengers. In particular, the passenger growth of Phnom Penh airport was still buoyant at 10% while Siam Reap's growth moderated to

just 1%. 2015 saw a passenger growth of 13% y-o-y to RM6.5m passengers. Contribution was also lifted by an appreciating USD.

Maintain BUY, TP RM3.10. We maintain our BUY call on Muhibbah with an SOP-derived TP of RM3.10.

Quarterly / Interim Income Statement (RMm)

FY Dec	1Q2015	4Q2015	1Q2016	% chg yoy	% chg qoq
Revenue	363	432	482	32.6	11.6
Other Oper. (Exp)/Inc	(337)	(403)	(464)	37.6	15.1
Operating Profit	26.3	29.0	18.1	(30.9)	(37.5)
Other Non Opg (Exp)/Inc	0.0	0.0	0.0	nm	nm
Associates & JV Inc	16.3	20.0	18.3	12.2	(8.3)
Net Interest (Exp)/Inc	(3.0)	(8.0)	(2.5)	18.7	69.1
Exceptional Gain/(Loss)	0.0	0.0	0.0	nm	nm
Pre-tax Profit	39.6	41.0	34.0	(14.1)	(17.1)
Tax	(7.6)	(1.5)	(8.1)	7.5	433.4
Minority Interest	(8.7)	(19.4)	(2.1)	(75.5)	(89.0)
Net Profit	23.3	20.1	23.8	2.0	18.3
Net profit bef Except.	23.3	20.1	23.8	2.0	18.3
EBITDA	59.7	62.9	36.5	(38.9)	(42.0)
Margins (%)					
Opg Profit Margins	7.2	6.7	3.8		
Net Profit Margins	6.4	4.6	4.9		

Source of all data: Company, AllianceDBS Research

CRITICAL DATA POINTS TO WATCH

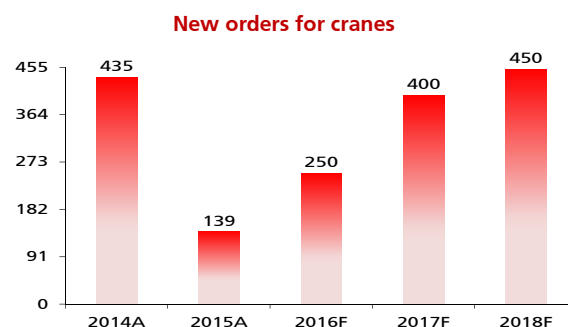
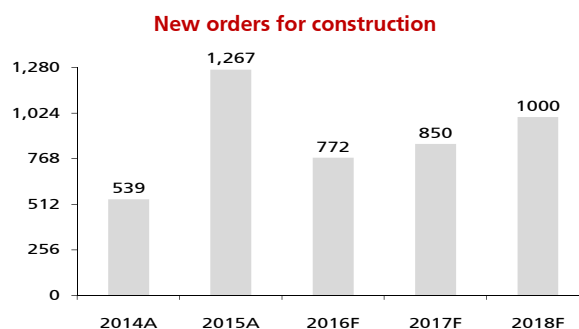
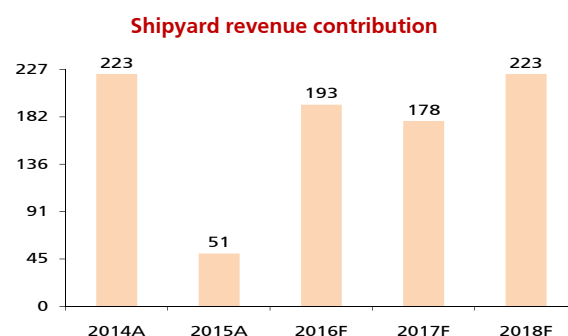
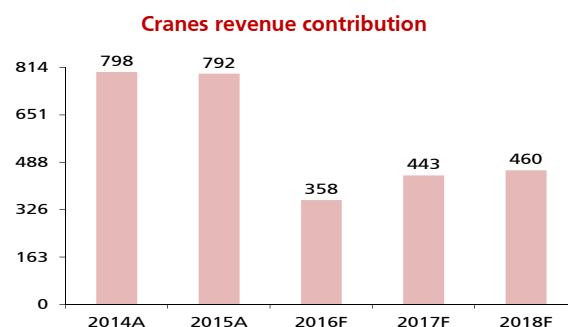
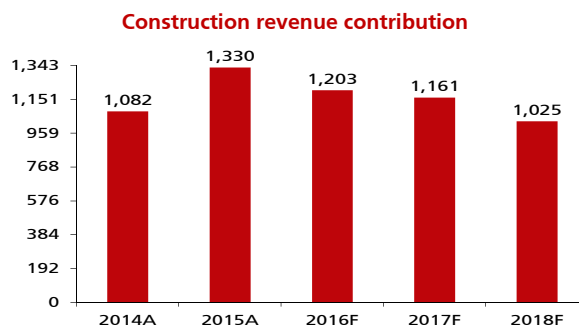
Earnings Drivers:

Stronger earnings growth ahead. We expect Muhibbah to deliver stronger earnings growth in FY16. With its Petronas licence and marine-based expertise, Muhibbah is poised to clinch more RAPID contracts in 2016. Within our construction universe, Muhibbah stands out as an excellent proxy to the 11th MP projects. Given that we are at the start of an upswing for construction awards, we expect new job wins to kick in significantly in 2H16. Overall orderbook stands at RM2.1bn (as at May 2016). We believe this will grow further on the back of its strong execution track record while also anchored by its ability to replenish its orderbook.

Infrastructure division most promising. Muhibbah believes the infrastructure sector is on a multi-year upcycle with potentially RM153bn worth of projects up for grabs (RM100bn RAPID, RM50bn Infrastructure Construction and RM3bn Marine/Ports). Muhibbah will be bidding for major projects such as RAPID, MRT Line 2 and WCE, and is quietly confident of clinching other marine-based projects. So far, 2016 has gotten off to a decent start with two wins – one from Petronas Carigali and the other for Phnom Penh airport expansion.

Cambodia airports to double capacity. Effective July, the Siam Reap and Phnom Penh airports will double their existing capacity to 12m passengers. The US\$85m capex has been financed by only one year of operating cashflow, which suggests the airports are cash cows. Passenger arrivals reached 6.5m in 2015 (+13 % y-o-y), led by the recovery in Chinese tourists. We estimate its 21% stake is worth RM677m (DCF, WACC 10%, RM/USD 4.15, and average passenger growth of 5% p.a. until 2040).

Favco capitalising on other revenue streams. Total outstanding orderbook now stands at RM604m (as at May 2016) which is sufficient for earnings visibility until early 2017. Out of this amount, 84% is still from offshore cranes (vs peak of 95%). The slowdown in offshore cranes demand is expected to be partly compensated by an increase in demand for tower cranes. Locally, Favelle Favco has won a RM30m contract from UEM-Samsung to build KL 118. Note that Favelle Favco's cranes have been used to build 12 out of the 14 tallest buildings in the world. We understand there may be M&A opportunities given its strong balance sheet with net cash of RM270m as at 31 December 2015.



Source: Company, AllianceDBS Research

Muhibbah Engineering

Balance Sheet:

Needs bigger balance sheet. Muhibbah’s shareholder’s funds as at 31 March 2016 stands at RM1.1bn (including minority interest). The proposed private placement of up to 10% of new shares will help Muhibbah strengthen its capital base. This will help bring net gearing down to c.0.5x from 0.6x as at Dec 2015, while its cash generating Cambodia airport concession should provide adequate cash flow. Based on the minimum and maximum scenario, this is expected to raise up to RM109m to RM112m. The majority of the proceeds amounting to RM75m will be used to pare down borrowings while the balance will be for working capital purposes.

Share Price Drivers:

Complete proxy to Malaysia infrastructure. Muhibbah is a complete proxy to the Malaysian infrastructure space because of its experience in bread-and-butter civil engineering works, as well as niche marine infrastructure and onshore and offshore fabrication works. Hence, we expect it to clinch works from RAPID, MRT Line 2, LRT 3, highway and port projects.

Premium for recurring base. In our view, the market continues to discount the strong cash flow of its concession business, particularly the Cambodian airport concession. Contractors which have a higher degree of relatively assured income such as IJM and Gamuda, which own sizeable toll portfolios, should command premium valuations.

Capitalising on Petronas Fabrication License. Muhibbah was awarded the much sought-after Petronas licence to take on offshore facilities construction and major onshore fabrication works. This suggests better opportunities to bag more Petronas-related jobs (downstream works). It has a 57-acre fabrication yard with a total capacity of 25,000 MT per year, making it the third largest among Petronas-licensed fabricators.

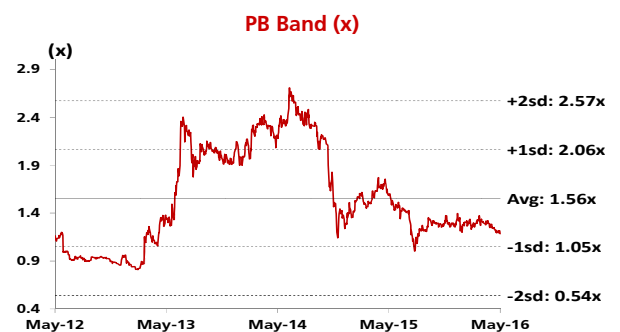
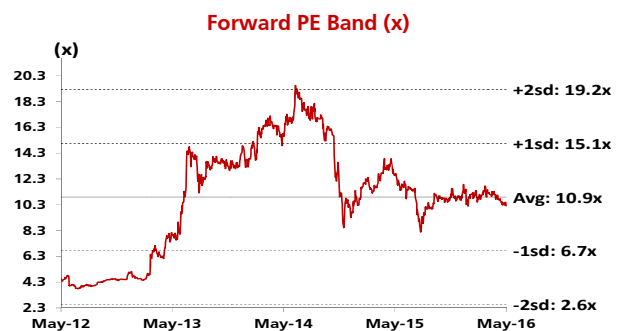
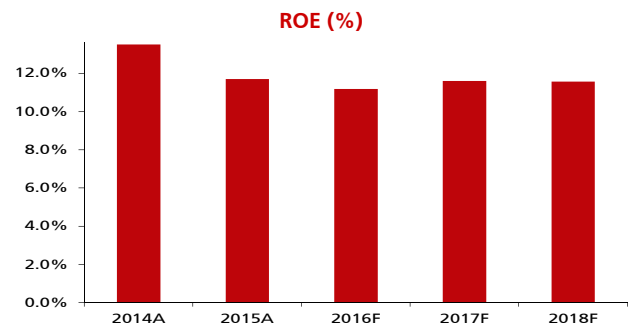
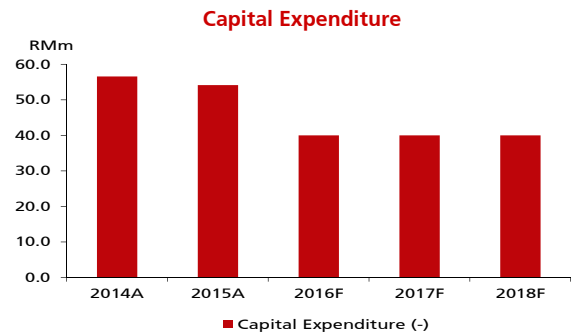
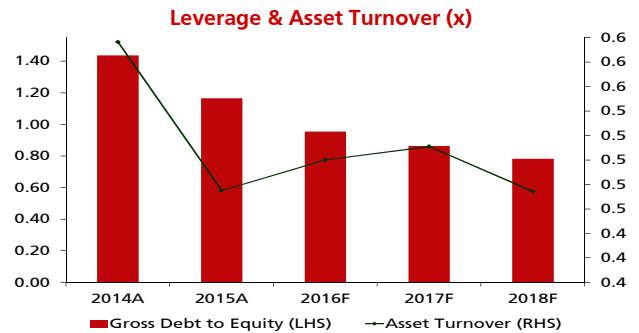
Completed landmark projects. Muhibbah has an impressive track record, having completed a list of landmark projects locally and abroad. Of significance is the LNG Regasification project for Petronas Gas in Melaka and South Klang Valley Expressway.

Key Risks:

Delay in project flows and sudden spike in raw material costs could dampen its earnings outlook.

Company Background

Muhibbah is primarily involved in construction, fabrication of cranes and shipbuilding. These three core divisions cater largely for the O&G sector. It also holds a 21% associate stake in two concessions, namely the Cambodian airports and Federal road maintenance in Malaysia.



Source: Company, AllianceDBS Research

Key Assumptions

FY Dec	2014A	2015A	2016F	2017F	2018F
Construction revenue	1,082	1,330	1,203	1,161	1,025
Cranes revenue contribution	798	792	358	443	460
Shipyards revenue contribution	223	50.5	193	178	223
New orders construction	539	1,267	772	850	1,000
New orders for cranes	435	139	250	400	450

Segmental Breakdown

FY Dec	2014A	2015A	2016F	2017F	2018F
Revenues (RMm)					
Construction	1,082	1,330	1,203	1,161	1,025
Cranes	798	792	358	443	460
Ships	223	50.5	193	178	223
Inter-segment	(369)	(568)	0.0	0.0	0.0
Total	1,734	1,605	1,754	1,781	1,707

Income Statement (RMm)

FY Dec	2014A	2015A	2016F	2017F	2018F
Revenue	1,734	1,605	1,754	1,781	1,707
Cost of Goods Sold	(1,479)	(1,343)	(1,522)	(1,523)	(1,441)
Gross Profit	254	262	231	258	266
Other Opng (Exp)/Inc	(131)	(138)	(135)	(146)	(147)
Operating Profit	123	124	96.3	113	120
Other Non Opng (Exp)/Inc	0.0	0.0	0.0	0.0	0.0
Associates & JV Inc	49.2	62.2	65.3	73.1	79.7
Net Interest (Exp)/Inc	(28.5)	(20.7)	(12.6)	(8.6)	(4.3)
Exceptional Gain/(Loss)	0.0	0.0	0.0	0.0	0.0
Pre-tax Profit	144	165	149	177	195
Tax	(24.8)	(27.8)	(20.9)	(26.0)	(28.9)
Minority Interest	(37.3)	(51.3)	(28.2)	(34.4)	(38.1)
Preference Dividend	0.0	0.0	0.0	0.0	0.0
Net Profit	81.6	86.0	99.8	117	128
Net Profit before Except.	81.6	86.0	99.8	117	128
EBITDA	228	251	225	251	267
Growth					
Revenue Gth (%)	(10.5)	(7.4)	9.3	1.6	(4.2)
EBITDA Gth (%)	10.9	10.1	(10.3)	11.6	6.1
Opg Profit Gth (%)	17.2	0.5	(22.1)	17.1	6.3
Net Profit Gth (Pre-ex) (%)	(5.6)	5.4	16.1	17.1	9.7
Margins & Ratio					
Gross Margins (%)	14.7	16.3	13.2	14.5	15.6
Opg Profit Margin (%)	7.1	7.7	5.5	6.3	7.0
Net Profit Margin (%)	4.7	5.4	5.7	6.6	7.5
ROAE (%)	13.5	11.7	11.2	11.6	11.6
ROA (%)	2.8	2.5	2.8	3.4	3.6
ROCE (%)	2.8	2.8	3.5	4.2	4.6
Div Payout Ratio (%)	23.4	21.8	20.0	20.0	20.0
Net Interest Cover (x)	4.3	6.0	7.6	13.2	28.0

Source: Company, AllianceDBS Research

Muhibbah Engineering

Quarterly / Interim Income Statement (RMm)

FY Dec	1Q2015	2Q2015	3Q2015	4Q2015	1Q2016
Revenue	363	410	394	432	482
Other Oper. (Exp)/Inc	(337)	(378)	(354)	(403)	(464)
Operating Profit	26.3	32.2	39.5	29.0	18.1
Other Non Opg (Exp)/Inc	0.0	0.0	0.0	0.0	0.0
Associates & JV Inc	16.3	11.4	14.4	20.0	18.3
Net Interest (Exp)/Inc	(3.0)	(6.3)	(3.5)	(8.0)	(2.5)
Exceptional Gain/(Loss)	0.0	0.0	0.0	0.0	0.0
Pre-tax Profit	39.6	37.4	50.5	41.0	34.0
Tax	(7.6)	(11.2)	(11.1)	(1.5)	(8.1)
Minority Interest	(8.7)	(6.8)	(16.3)	(19.4)	(2.1)
Net Profit	23.3	19.3	23.0	20.1	23.8
Net profit bef Except.	23.3	19.3	23.0	20.1	23.8
EBITDA	59.7	56.4	65.9	62.9	36.5

Growth

Revenue Gth (%)	(20.4)	13.0	(4.1)	9.7	11.6
EBITDA Gth (%)	(12.3)	(5.6)	16.8	(4.6)	(42.0)
Opg Profit Gth (%)	(19.3)	22.5	22.8	(26.6)	(37.5)
Net Profit Gth (Pre-ex) (%)	15.3	(17.3)	19.4	(12.8)	18.3

Margins

Opg Profit Margins (%)	7.2	7.8	10.0	6.7	3.8
Net Profit Margins (%)	6.4	4.7	5.8	4.6	4.9

Balance Sheet (RMm)

FY Dec	2014A	2015A	2016F	2017F	2018F
Net Fixed Assets	725	785	819	798	776
Invt in Associates & JVs	236	257	318	386	461
Other LT Assets	31.0	52.8	52.8	52.8	52.8
Cash & ST Invt	601	578	522	583	681
Inventory	226	301	250	250	257
Debtors	1,334	1,601	1,441	1,464	1,403
Other Current Assets	12.5	18.1	18.1	18.1	18.1
Total Assets	3,165	3,594	3,421	3,553	3,649
ST Debt	1,168	1,221	1,146	1,146	1,146
Creditor	966	1,136	876	876	829
Other Current Liab	38.8	33.6	33.6	33.6	33.6
LT Debt	69.3	48.9	48.9	48.9	48.9
Other LT Liabilities	61.9	64.2	64.2	64.2	64.2
Shareholder's Equity	644	826	960	1,056	1,161
Minority Interests	217	265	293	328	366
Total Cap. & Liab.	3,165	3,594	3,421	3,553	3,649
Non-Cash Wkg. Capital	567	751	800	823	815
Net Cash/(Debt)	(636)	(692)	(673)	(612)	(514)
Debtors Turn (avg days)	253.7	333.8	316.6	297.7	306.5
Creditors Turn (avg days)	245.4	300.2	251.7	219.4	226.6
Inventory Turn (avg days)	55.5	75.3	69.0	62.7	67.4
Asset Turnover (x)	0.6	0.5	0.5	0.5	0.5
Current Ratio (x)	1.0	1.0	1.1	1.1	1.2
Quick Ratio (x)	0.9	0.9	1.0	1.0	1.0
Net Debt/Equity (X)	0.7	0.6	0.5	0.4	0.3
Net Debt/Equity ex MI (X)	1.0	0.8	0.7	0.6	0.4
Capex to Debt (%)	4.6	4.3	3.3	3.3	3.3
Z-Score (X)	1.1	1.2	1.2	1.3	1.3

Source: Company, AllianceDBS Research

Cash Flow Statement (RMm)

FY Dec	2014A	2015A	2016F	2017F	2018F
Pre-Tax Profit	144	165	149	177	195
Dep. & Amort.	55.8	65.2	63.7	65.5	67.3
Tax Paid	(24.8)	(27.8)	(20.9)	(26.0)	(28.9)
Assoc. & JV Inc/(loss)	(49.2)	(62.2)	(65.3)	(73.1)	(79.7)
Chg in Wkg.Cap.	(258)	(174)	(48.8)	(22.5)	7.35
Other Operating CF	59.9	64.1	0.0	0.0	0.0
Net Operating CF	(72.9)	30.8	77.7	121	161
Capital Exp.(net)	(56.6)	(54.1)	(40.0)	(40.0)	(40.0)
Other Invt.(net)	0.0	0.0	0.0	0.0	0.0
Invt in Assoc. & JV	(45.6)	0.0	0.0	0.0	0.0
Div from Assoc & JV	0.0	0.0	0.0	0.0	0.0
Other Investing CF	66.6	60.7	0.0	0.0	0.0
Net Investing CF	(35.6)	6.56	(40.0)	(40.0)	(40.0)
Div Paid	(18.9)	(19.1)	(18.7)	(20.0)	(23.4)
Chg in Gross Debt	362	32.9	(75.0)	0.0	0.0
Capital Issues	(13.7)	19.6	0.0	0.0	0.0
Other Financing CF	(46.4)	(93.5)	0.0	0.0	0.0
Net Financing CF	283	(60.2)	(93.7)	(20.0)	(23.4)
Currency Adjustments	0.0	0.0	0.0	0.0	0.0
Chg in Cash	175	(22.8)	(56.1)	61.2	97.9
Opg CFPS (sen)	39.3	43.4	26.2	27.7	29.7
Free CFPS (sen)	(27.5)	(5.0)	7.80	15.7	23.4

Source: Company, AllianceDBS Research

Target Price & Ratings History



Note: Share price and Target price are adjusted for corporate actions.

S.No.	Date	Closing Price	Target Price	Rating
1:	01 Jun 15	2.42	3.50	BUY
2:	21 Jul 15	2.28	3.40	BUY
3:	01 Sep 15	1.79	2.90	BUY
4:	04 Sep 15	1.93	2.90	BUY
5:	30 Nov 15	2.23	2.90	BUY
6:	15 Dec 15	2.22	2.90	BUY
7:	14 Jan 16	2.36	2.90	BUY
8:	01 Mar 16	2.25	2.90	BUY
9:	04 Apr 16	2.37	2.90	BUY
10:	04 May 16	2.28	2.90	BUY
11:	12 May 16	2.27	3.10	BUY

Source: AllianceDBS Research

AllianceDBS Research recommendations are based on an Absolute Total Return* Rating system, defined as follows:

STRONG BUY (>20% total return over the next 3 months, with identifiable share price catalysts within this time frame)

BUY (>15% total return over the next 12 months for small caps, >10% for large caps)

HOLD (-10% to +15% total return over the next 12 months for small caps, -10% to +10% for large caps)

FULLY VALUED (negative total return i.e. > -10% over the next 12 months)

SELL (negative total return of > -20% over the next 3 months, with identifiable catalysts within this time frame)

Share price appreciation + dividends

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