

Company Guide

Muhibbah Engineering

Version 2 | Bloomberg: MUHI MK | Reuters: MUHI.KL

Refer to important disclosures at the end of this report

Malaysia Equity Research

1 Mar 2016

BUY

Last Traded Price: RM2.28 (KLCI : 1,654.75)

Price Target : RM2.90 (27% upside) (Prev RM2.90)

Shariah Compliant: Yes

Potential Catalyst: RAPID, port and other infrastructures projects

Where we differ: Our earnings are broadly in line. Of late, there has been more positive revisions to consensus TP.

Analyst

Chong Tjen San +603 2604 3968 tjensan@alliancedbs.com

What's New

- **4Q15 results in line**
- **Strong earnings from construction segment; improved contributions from shipyard**
- **Maintain BUY with unchanged TP of RM2.90**

Price Relative



Forecasts and Valuation

FY Dec (RM m)	2014A	2015A	2016F	2017F
Revenue	1,693	1,599	1,771	1,933
EBITDA	159	189	229	253
Pre-tax Profit	145	168	159	182
Net Profit	81.6	85.6	106	121
Net Pft (Pre Ex.)	81.6	85.6	106	121
Net Pft Gth (Pre-ex) (%)	(5.6)	4.9	23.7	14.3
EPS (sen)	19.3	20.3	25.1	28.6
EPS Pre Ex. (sen)	19.3	20.3	25.1	28.6
EPS Gth Pre Ex (%)	(6)	5	24	14
Diluted EPS (sen)	19.3	20.3	25.1	28.6
Net DPS (sen)	4.52	4.44	5.01	5.73
BV Per Share (sen)	152	195	229	252
PE (X)	11.8	11.3	9.1	8.0
PE Pre Ex. (X)	11.8	11.3	9.1	8.0
P/Cash Flow (X)	nm	nm	5.3	12.2
EV/EBITDA (X)	11.4	10.2	8.0	7.3
Net Div Yield (%)	2.0	1.9	2.2	2.5
P/Book Value (X)	1.5	1.2	1.0	0.9
Net Debt/Equity (X)	0.7	0.6	0.5	0.4
ROAE (%)	13.5	11.6	11.8	11.9
Earnings Rev (%)		(6)	0	0
Consensus EPS (sen):		22.3	24.3	27.5
Other Broker Recs:		B: 6	S: 0	H: 0

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

Scarcity Premium for Infra 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 license is an advantage. Other contractors do not have this combination to compete 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 passenger traffic +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 earnings given the weak MYR.

Good start for 2016. Muhibbah has won two contracts so far in 2016, one each for its infrastructure and shipyard division. For its infrastructure division, it won a RM137m building contract from PETRONAS Carigali, in which it has a 70% stake, implying a contract value of RM96m. For its shipyard division, it clinched a RM92m contract 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 RM1.7bn comes from infrastructure.

Valuation:

Muhibbah is a BUY with a RM2.90 TP. 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:

A potential risk is non-renewal of its Roadcare concession and unfavourable outcome of the adjudication under the building & Construction Industry Payment Act for Wiggin Island.

At A Glance

Issued Capital (m shrs)	469
Mkt. Cap (RMm/US\$m)	1,069 / 254
Major Shareholders (%)	
Mac Ngan Boon	22.1
Lembaga Tabung Haji	9.6
Free Float (%)	60.7
3m Avg. Daily Val (US\$m)	0.48

ICB Industry : Industrials / Construction & Materials

WHAT'S NEW**Solid end to FY15**

In line. 4Q15 recorded headline net profit of RM20m (-0.6% y-o-y, -13% q-o-q) bringing FY15 profit to RM86m. This was in line with our forecast and consensus estimate.

Strong quarter for construction and shipyard. Muhibbah booked a stronger quarter for its construction arm with 4Q15 pretax profit surging to RM42.4m, which more than doubled y-o-y and q-o-q. This was on the back of stronger margins of 8.7% vs 3.5% in 3Q15 and 1.7% in 4Q14. The crane business under Favelle Favco showed a weaker growth with pretax profit of only RM21m (-24.8% y-o-y, -47.4% q-o-q). This brings 12M15 pretax profit to RM792m which was slightly lower than RM798m reported in 12M14. Meanwhile, shipyard pretax profit surged to RM11m in 4Q15 (vs RM2.1m in 3Q15). Growth in 2016 will be buoyed by its recent win from the Ministry of Transport.

FY15 associate profit (largely its Cambodian airport concession) was up 30% y-o-y. This was driven by strong traffic volume growth of 13% y-o-y to RM6.5m passengers. Contribution was also lifted by an appreciating USD.

Declared 4.0 sen DPS. In tandem with the record profit, a DPS of 4.0 sen was declared. This implies a decent net dividend yield of 1.9%.

Maintain BUY, TP RM2.90. We maintain our BUY call on Muhibbah with SOP- derived TP of RM2.90.

Quarterly / Interim Income Statement (RMm)

FY Dec	4Q2014	3Q2015	4Q2015	% chg yoy	% chg qoq
Revenue	457	394	432	(5.4)	9.7
Other Oper. (Exp)/Inc	(424)	(354)	(403)	(5.0)	13.8
Operating Profit	32.6	39.5	29.0	(10.9)	(26.6)
Other Non Opg (Exp)/Inc	0.0	0.0	0.0	nm	nm
Associates & JV Inc	16.6	14.4	20.0	20.6	38.8
Net Interest (Exp)/Inc	(7.4)	(3.5)	(8.0)	(7.7)	nm
Exceptional Gain/(Loss)	0.0	0.0	0.0	nm	nm
Pre-tax Profit	41.7	50.5	41.0	(1.7)	(18.7)
Tax	(10.2)	(11.1)	(1.5)	(85.1)	(86.3)
Minority Interest	(11.3)	(16.3)	(19.4)	71.6	19.1
Net Profit	20.2	23.0	20.1	(0.6)	(12.8)
Net profit bef Except.	20.2	23.0	20.1	(0.6)	(12.8)
EBITDA	68.2	65.9	62.9	(7.8)	(4.6)
Margins (%)					
Opg Profit Margins	7.1	10.0	6.7		
Net Profit Margins	4.4	5.8	4.6		

Source of all data: Company, AllianceDBS Research

CRITICAL DATA POINTS TO WATCH

Earnings Drivers:

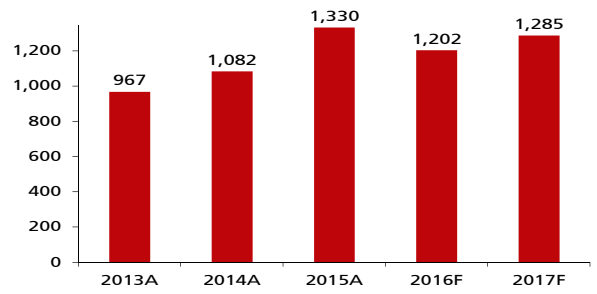
Stronger earnings growth ahead. We expect Muhibbah to deliver stronger earnings growth in FY16. With its Petronas license and marine-based expertise, Muhibbah is poised to clinch more RAPID contracts in 2016. Within our construction universe, Muhibbah stands out as an excellent proxy to the 11th MP mega projects. Based on this, we are projecting FY16 earnings to come at RM106m (+24% y-o-y) and RM121m (+14% y-o-y) for FY17. 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 RM2.5bn implying comfortable cover of 1.5x FY16F. 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 RM140bn worth of projects up for grabs. Also, raw material costs are rather benign now with cement and steel prices 5% and 15% cheaper y-o-y, respectively. 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 one win from Petronas Carigali.

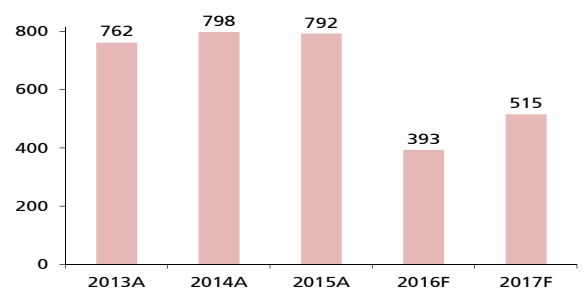
Cambodia airports to double capacity. Effective July, the Siam Reap and Phnom Penh airports will double their existing capacity to 12m passengers. The US\$85m capex has been financed by only one year of operating cashflow, which suggests the airports are cash cows. Passenger arrivals reached 6.5m in 2015 (+13 % y-o-y) led by a 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. Favco has been receiving increasing orders in the US for tower cranes, and is beefing up its maintenance division (c.10% of revenues). This should cushion potentially softer orders for oil and gas cranes. With an orderbook of RM0.7bn, we expect Favco to have decent visibility till early 2017. Recall, it won RM64m worth of new orders in Jan-2016, of which four are for tower cranes and balance two for off-shore cranes. It is also exploring supplying cranes to RAPID.

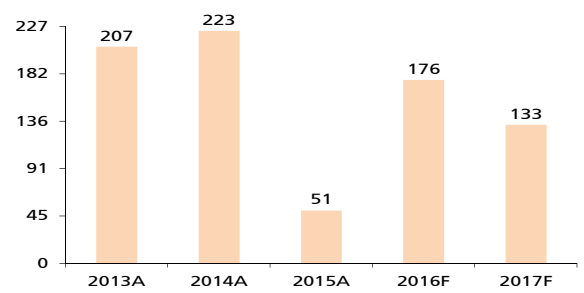
Construction revenue contribution



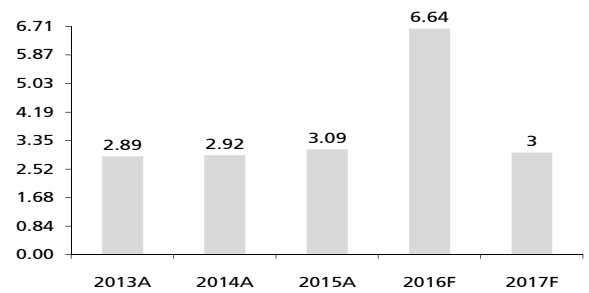
Cranes revenue contribution



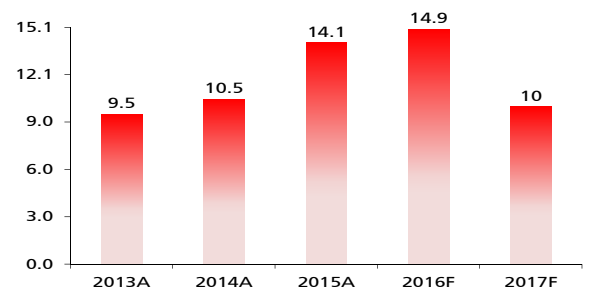
Shipyard revenue contribution



Margins for construction



Margins for cranes



Source: Company, AllianceDBS Research

Muhibbah Engineering

Balance Sheet:

Needs bigger balance sheet. Muhibbah’s shareholder’s funds as at 31 December 2015 stands at RM1bn (including minority interest). We understand the company is aiming to strengthen this further to capitalise on larger contract flows from Petronas. This may be via a private placement or rights issue. Net gearing is still manageable at 0.6x, while its cash generating Cambodia airport concession should provide adequate cash flow.

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 the company to clinch works from RAPID, MRT Line 2, LRT 3, West Coast Expressway and port projects.

Capitalising on Petronas Fabrication License. Muhibbah was awarded the much sought after Petronas license 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.

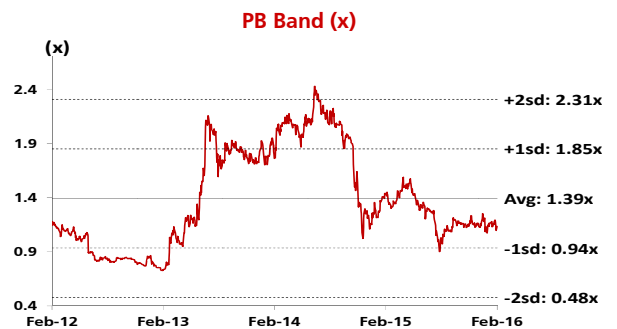
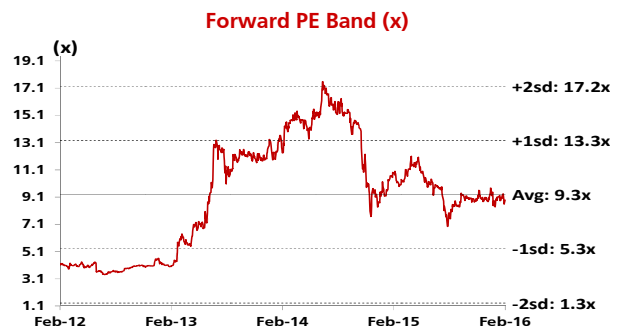
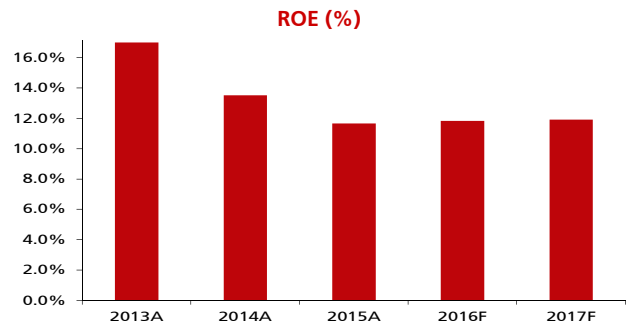
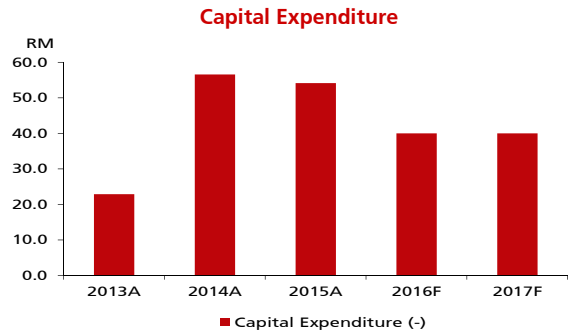
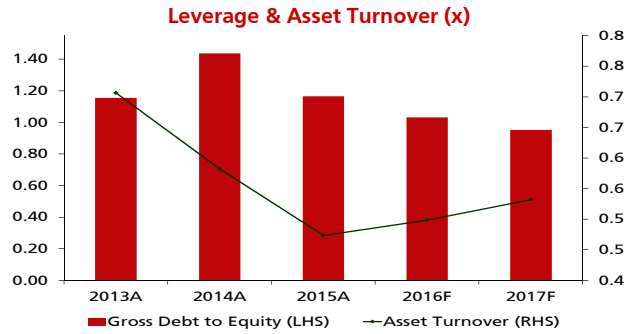
Completed landmark projects. Muhibbah has an impressive track record, having completed a list of landmark projects locally and abroad. Of significance is the LNG Regasification project for Petronas Gas in Melaka and South Klang Valley Expressway.

Key Risks:

A potential risk is non-renewal of its Roadcare concession and unfavourable outcome of the adjudication under the Building & Construction Industry Payment Act for the Wiggan Island project.

Company Background

Muhibbah is primarily involved in construction, fabrication of cranes and shipbuilding. These 3 core divisions cater largely for the O&G sector. It also holds a 21% associate stake in 2 concessions, namely the Cambodian airports and Federal road maintenance in Malaysia.



Source: Company, AllianceDBS Research

Key Assumptions

FY Dec	2013A	2014A	2015A	2016F	2017F
Construction revenue contribution	967	1,082	1,330	1,202	1,285
Cranes revenue contribution	762	798	792	393	515
Shipyards revenue contribution	207	223	50.5	176	133
Margins for construction	2.89	2.92	3.09	6.64	3.00
Margins for cranes	9.51	10.5	14.1	14.9	10.0

Segmental Breakdown

FY Dec	2013A	2014A	2015A	2016F	2017F
Revenues (RMm)					
Construction	967	1,082	1,330	1,202	1,285
Cranes	762	798	792	393	515
Ships	207	223	50.5	176	133
Segment 4	0.0	(410)	(574)	0.0	0.0
Others	0.0	0.0	0.0	0.0	0.0
Total	1,936	1,693	1,599	1,771	1,933

Assume more contracts from RAPID and other projects

Conservatively, expect softer growth for cranes

Income Statement (RMm)

FY Dec	2013A	2014A	2015A	2016F	2017F
Revenue	1,936	1,693	1,599	1,771	1,933
Cost of Goods Sold	(1,723)	(1,583)	(1,472)	(1,558)	(1,701)
Gross Profit	213	110	127	212	232
Other Opng (Exp)/Inc	(108)	1.19	0.0	(115)	(121)
Operating Profit	105	111	127	97.2	111
Other Non Opng (Exp)/Inc	0.0	0.0	0.0	0.0	0.0
Associates & JV Inc	46.6	47.8	62.2	68.4	76.6
Net Interest (Exp)/Inc	(18.9)	(13.7)	(20.8)	(6.2)	(5.1)
Exceptional Gain/(Loss)	0.0	0.0	0.0	0.0	0.0
Pre-tax Profit	133	145	168	159	182
Tax	(16.4)	(33.7)	(31.5)	(22.7)	(26.4)
Minority Interest	(29.8)	(30.0)	(51.3)	(30.7)	(34.9)
Preference Dividend	0.0	0.0	0.0	0.0	0.0
Net Profit	86.4	81.6	85.6	106	121
Net Profit before Except.	86.4	81.6	85.6	106	121
EBITDA	206	159	189	229	253
Growth					
Revenue Gth (%)	(26.2)	(12.6)	(5.5)	10.7	9.2
EBITDA Gth (%)	(23.0)	(22.7)	19.0	21.2	10.3
Opg Profit Gth (%)	(40.1)	5.8	14.3	(23.5)	14.1
Net Profit Gth (Pre-ex) (%)	(43.1)	(5.6)	4.9	23.7	14.3
Margins & Ratio					
Gross Margins (%)	11.0	6.5	7.9	12.0	12.0
Opg Profit Margin (%)	5.4	6.6	7.9	5.5	5.7
Net Profit Margin (%)	4.5	4.8	5.4	6.0	6.3
ROAE (%)	17.0	13.5	11.6	11.8	11.9
ROA (%)	3.2	2.8	2.5	3.0	3.3
ROCE (%)	3.9	3.5	2.8	3.9	4.3
Div Payout Ratio (%)	21.9	23.4	21.9	20.0	20.0
Net Interest Cover (x)	5.5	8.1	6.1	15.6	21.7

Source: Company, AllianceDBS Research

Muhibbah Engineering

Quarterly / Interim Income Statement (RMm)

FY Dec	4Q2014	1Q2015	2Q2015	3Q2015	4Q2015
Revenue	457	363	410	394	432
Cost of Goods Sold	0.0	0.0	0.0	0.0	0.0
Gross Profit	457	363	410	394	432
Other Oper. (Exp)/Inc	(424)	(337)	(378)	(354)	(403)
Operating Profit	32.6	26.3	32.2	39.5	29.0
Other Non Opg (Exp)/Inc	0.0	0.0	0.0	0.0	0.0
Associates & JV Inc	16.6	16.3	11.4	14.4	20.0
Net Interest (Exp)/Inc	(7.4)	(3.0)	(6.3)	(3.5)	(8.0)
Exceptional Gain/(Loss)	0.0	0.0	0.0	0.0	0.0
Pre-tax Profit	41.7	39.6	37.4	50.5	41.0
Tax	(10.2)	(7.6)	(11.2)	(11.1)	(1.5)
Minority Interest	(11.3)	(8.7)	(6.8)	(16.3)	(19.4)
Net Profit	20.2	23.3	19.3	23.0	20.1
Net profit bef Except.	20.2	23.3	19.3	23.0	20.1
EBITDA	68.2	59.7	56.4	65.9	62.9

Growth

Revenue Gth (%)	21.4	(20.4)	13.0	(4.1)	9.7
EBITDA Gth (%)	52.2	(12.3)	(5.6)	16.8	(4.6)
Opg Profit Gth (%)	27.5	(19.3)	22.5	22.8	(26.6)
Net Profit Gth (Pre-ex) (%)	(0.4)	15.3	(17.3)	19.4	(12.8)

Margins

Opg Profit Margins (%)	7.1	7.2	7.8	10.0	6.7
Net Profit Margins (%)	4.4	6.4	4.7	5.8	4.6

Balance Sheet (RMm)

FY Dec	2013A	2014A	2015A	2016F	2017F
Net Fixed Assets	711	725	785	819	798
Invts in Associates & JVs	190	236	257	321	393
Other LT Assets	29.6	31.0	52.8	52.8	52.8
Cash & ST Invts	426	601	578	730	778
Inventory	207	226	301	213	233
Debtors	1,077	1,334	1,601	1,358	1,483
Other Current Assets	10.1	12.5	18.1	18.1	18.1
Total Assets	2,650	3,165	3,594	3,513	3,756
ST Debt	738	1,168	1,221	1,251	1,281
Creditor	948	966	1,136	854	932
Other Current Liab	8.66	38.8	33.6	33.6	33.6
LT Debt	137	69.3	48.9	48.9	48.9
Other LT Liabilities	61.7	61.9	64.2	64.2	64.2
Shareholder's Equity	563	644	826	966	1,065
Minority Interests	194	217	265	296	331
Total Cap. & Liab.	2,650	3,165	3,594	3,513	3,756
Non-Cash Wkg. Capital	337	567	751	702	768
Net Cash/(Debt)	(449)	(636)	(692)	(569)	(552)
Debtors Turn (avg days)	231.0	259.9	335.0	305.0	268.3
Creditors Turn (avg days)	215.7	220.7	260.6	242.9	199.3
Inventory Turn (avg days)	45.4	49.9	65.4	62.9	49.8
Asset Turnover (x)	0.7	0.6	0.5	0.5	0.5
Current Ratio (x)	1.0	1.0	1.0	1.1	1.1
Quick Ratio (x)	0.9	0.9	0.9	1.0	1.0
Net Debt/Equity (X)	0.6	0.7	0.6	0.5	0.4
Net Debt/Equity ex MI (X)	0.8	1.0	0.8	0.6	0.5
Capex to Debt (%)	2.6	4.6	4.3	3.1	3.0
Z-Score (X)	1.4	1.1	1.2	1.2	1.3

Net gearing manageable with low interest rates

Source: Company, AllianceDBS Research

Cash Flow Statement (RMm)

FY Dec	2013A	2014A	2015A	2016F	2017F
Pre-Tax Profit	133	145	168	159	182
Dep. & Amort.	54.2	0.0	0.0	63.7	65.5
Tax Paid	(16.4)	(33.7)	(31.5)	(22.7)	(26.4)
Assoc. & JV Inc/(loss)	(46.6)	(47.8)	(62.2)	(68.4)	(76.6)
Chg in Wkg.Cap.	223	(258)	(174)	49.1	(65.8)
Other Operating CF	21.0	122	0.0	0.0	0.0
Net Operating CF	368	(72.9)	(98.8)	181	79.0
Capital Exp.(net)	(22.9)	(56.6)	(54.1)	(40.0)	(40.0)
Other Invt.(net)	0.0	0.0	0.0	0.0	0.0
Invt in Assoc. & JV	(19.0)	(45.6)	0.0	0.0	0.0
Div from Assoc & JV	0.0	0.0	0.0	0.0	0.0
Other Investing CF	46.5	66.6	60.7	0.0	0.0
Net Investing CF	4.62	(35.6)	6.56	(40.0)	(40.0)
Div Paid	(7.8)	(18.9)	(19.1)	(18.7)	(21.2)
Chg in Gross Debt	(239)	362	32.9	30.0	30.0
Capital Issues	18.9	(13.7)	19.6	0.0	0.0
Other Financing CF	(50.7)	(46.4)	(93.5)	0.0	0.0
Net Financing CF	(278)	283	(60.2)	11.3	8.82
Currency Adjustments	(4.5)	0.0	0.0	0.0	0.0
Chg in Cash	89.6	175	(152)	152	47.9
Opg CFPS (sen)	34.3	43.9	17.7	31.2	34.3
Free CFPS (sen)	81.6	(30.6)	(36.2)	33.4	9.24

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:	02 Mar 15	2.29	3.50	BUY
2:	03 Apr 15	2.22	3.50	BUY
3:	08 May 15	2.55	3.50	BUY
4:	01 Jun 15	2.42	3.50	BUY
5:	21 Jul 15	2.28	3.40	BUY
6:	01 Sep 15	1.79	2.90	BUY
7:	04 Sep 15	1.93	2.90	BUY
8:	30 Nov 15	2.23	2.90	BUY
9:	15 Dec 15	2.22	2.90	BUY
10:	14 Jan 16	2.36	2.90	BUY

Source: AllianceDBS Research

DISCLOSURE

Stock rating definitions

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 > -10% over the next 12 months
SELL	-	negative total return of > -20% over the next 3 months, with identifiable catalysts within this time frame

Commonly used abbreviations

Adex = advertising expenditure	EPS = earnings per share	PBT = profit before tax
bn = billion	EV = enterprise value	P/B = price / book ratio
BV = book value	FCF = free cash flow	P/E = price / earnings ratio
CF = cash flow	FV = fair value	PEG = P/E ratio to growth ratio
CAGR = compounded annual growth rate	FY = financial year	q-o-q = quarter-on-quarter
Capex = capital expenditure	m = million	RM = Ringgit
CY = calendar year	M-o-m = month-on-month	ROA = return on assets
Div yld = dividend yield	NAV = net assets value	ROE = return on equity
DCF = discounted cash flow	NM = not meaningful	TP = target price
DDM = dividend discount model	NTA = net tangible assets	trn = trillion
DPS = dividend per share	NR = not rated	WACC = weighted average cost of capital
EBIT = earnings before interest & tax	p.a. = per annum	y-o-y = year-on-year
EBITDA = EBIT before depreciation and amortisation	PAT = profit after tax	YTD = year-to-date

DISCLAIMER

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Wong Ming Tek, Executive Director

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AllianceDBS Research Sdn Bhd (128540 U)
19th Floor, Menara Multi-Purpose, Capital Square, 8 Jalan Munshi Abdullah, 50100 Kuala Lumpur, Malaysia.
Tel.: +603 2604 3333 Fax: +603 2604 3921 email : general@alliancedbs.com