1Q FY2017 results update

1 June 2017

Muhibbah Engineering (M) Bhd

- 1Q2017 results within expectations
- Large RM2.1b order-book, with RM1b secured this year
- Growing topline, concessions to drive earnings
- Oil prices stabilize, attractive valuations. Maintain BUY

BUY

Share price
RM2.75

Market capitalization
RM1,321 million

Board
Main

Indices
FBM Emas Syariah,

Sector
Construction

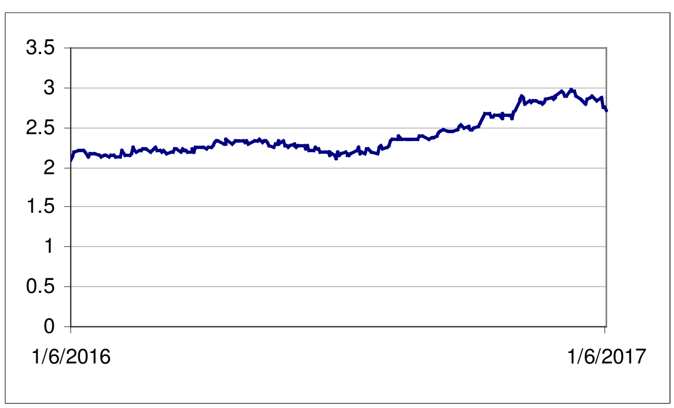
Stock code
5703

By
The Research Team

Key stock statistics	FY Dec16	FY Dec17E
EPS (sen)	22.2	22.2
P/E (x)	12.4	12.4
DPS (sen)	5.5	5.5
NTA/share (RM)	2.04	2.27
Issued capital (mil)	480.5	
52-week price range (RM)	2.09 - 2.99	

Major shareholders (%)	
Mac Ngan Boon	15.3%
Lembaga Tabung Haji	9.6%

Share Price Chart



1Q FY2017 results highlights

Year end Dec (RM mil)	1Q2017	1Q2016	% chg
Turnover	241.5	481.8	(49.9)
Pre-tax profit	48.9	41.7	17.3
Tax	(4.5)	(8.1)	(44.6)
Minority interests	(15.1)	(9.8)	53.9
Net profit	29.3	23.8	23.4
EPS (sen)	6.10	5.06	
Pre-tax profit margin (%)	20.2	8.6	
Net profit margin (%)	12.1	4.9	

Muhibbah Engineering's results for 1Q FY Dec 2017 were squarely within our expectations, with net profit of RM29.3 million for the quarter coming in at 26% of our full year forecast of RM114.7 million.

For the quarter, Muhibbah's net profit rose 23.4% y-y to RM29.3 million, following a 17.3% rise in pre-tax profit to RM48.9 million. The disproportionately higher growth in net profit was helped by lower taxes, but partly mitigated by higher minority interests.

These results were achieved despite a halving in revenue from RM481.8 million to RM241.5 million, which was attributed to timing issues for recognition of its construction infrastructure projects. Recognition for large projects tend to be lumpy, and the company had recently secured a number of projects which are at commencement stage.

The concession business continues to drive Muhibbah's profits. After-tax contributions from associates rose 28.2% y-y from RM26 million to RM33.3 million for the quarter, accounting for virtually all of the company's increase in profits during the quarter.

The associates reflect Muhibbah's concession businesses, which consist of 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.

Favelle Favco, the crane manufacturing arm, saw a 12.9% y-y rise in net profit to RM12.8 million for the quarter, despite a 25.3% decline in revenue to RM114.3 million. While Favco had been affected by its heavy exposure to the oil and gas sector, the recent quarter's profitability growth showed improved margins and cost containment. Favco's orderbook stood at RM612 million as at 17 May 2017, equivalent to over a year of revenue visibility.

Outlook and recommendation

We maintain our **BUY** recommendation and earnings forecasts. We expect Muhibbah's top-line to pick up steam in the coming quarters as the company works through some of its newly secured large projects.

Major projects secured this year include the Second Harbour Basin project at Bintulu port (secured in April 2017, valued at RM584.8 million) and the MANATEQ industrial zone project in Qatar (secured in Jan 2017, valued at RM438.1 million).

Muhibbah's orderbook totaled RM2.1 billion as at 24 May 2017, higher than the RM1.7b in Feb 2017, and will underpin earnings in the next few years. The company has demonstrated a strong ability to secure major projects locally and abroad, with a high order-book replenishment rate.

We like Muhibbah for its attractive valuations and resilient earnings base. It enjoys strong recurring income from its concessions balanced by more cyclical income from construction and cranes that provide positive upside surprises.

We expect net profit to grow 8.7% to RM114.7 million in 2017 and 7.7% to RM123.5 million in 2018. After the proposed 10% placement exercise, EPS is projected at 22.2 sen for 2017 and 23.9 sen for 2018. The stock is currently trading on low P/E multiples of 12.4 and 11.5 times for 2017-2018, respectively, and just 1.2x book for 2017.

Apart from its attractive valuations and sustainable earnings base, we also like Muhibbah's growing international stature and its ability to secure high profile international jobs.

In Jan 2017, Muhibbah secured a RM438 million contract from the Qatari government-owned Economic Zones Company of Qatar (Manateq) for the construction of roads and infrastructure works at Um Alhoul Economic Zone (Qatar Economic Zone 3) in Doha, Qatar.

This was Muhibbah's second major contract win from the Qatar government, the first being the building of catering facilities for the Hamad International Airport in Doha. With Qatar embarking on a major infrastructure spending exercise, we would not discount the possibility of more project bids there.

Crude oil prices appear to be stabilizing around the US$50 per barrel mark, providing more stability to the oil and gas sector. A prolonged period of stable prices would help the sector plan for the next phase of capital investments.

While the recent oil and gas slowdown has adversely affected Favco, 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.

Over the longer term, Muhibbah will also be developing a new shipyard in Kuantan with ancillary industrial facilities for ship building, repair and offshore fabrication works.

In June 2016, it announced the acquisition of a 99-year leasehold land measuring 500 acres in Kuantan for RM26.45 million, or just RM1.21 psf. The land, acquired from the Pahang state government, would be developed into the proposed Kuantan Maritime Hub over a period of 10 years. 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. Earnings are derived in USD and the airports are benefitting from rising passenger traffic and a recently completed expansion exercise.

In 2016, arrivals at the three Cambodian airports grew 9% to 7.02 million passengers, following 2 years of robust 13% per year growth.

Future growth will be underpinned by expanded capacity at the two main airports as well as higher arrivals at the southern port and beach city of Sihanoukville as more flights are added. Sihanoukville airport currently only handles direct flights from Siem Reap and charter flights.

Airasia has recently announced flights from Kuala Lumpur to Sihanoukville starting from Aug 2017, with a frequency of 4 flights a week.

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)	2015	2016	2017E	2018E
Turnover	1,707.5	1,918.8	1,900.0	2,065.0
EBITDA	195.7	201.3	229.0	257.2
Depreciation	(65.2)	(69.5)	(73.0)	(75.0)
Associates	86.2	83.8	86.0	90.0
Interest income/(exp)	(38.3)	(44.1)	(40.0)	(44.0)
Pre-tax profit	178.4	171.4	202.0	228.2
Tax	(27.8)	(10.8)	(30.3)	(45.6)
Minorities	(63.0)	(55.1)	(57.0)	(59.0)
Net profit	87.5	105.5	114.7	123.5
Operating margin (%)	11.5	10.5	12.1	12.5
Pre-tax margin (%)	10.4	8.9	10.6	11.0
Net margin (%)	5.1	5.5	6.0	6.0
Effective tax rate (%)	15.6	6.3	15.0	20.0

Per Share Data

Year end Dec	2015	2016	2017E	2018E
EPS (sen)	19.1	22.2	22.2	23.9
P/E (x)	14.4	12.4	12.4	11.5
Dividend (sen)	5.0	5.5	5.5	5.5
Dividend yield (%)	1.8	2.0	2.0	2.0
Payout ratio (%)	27	25	25	23
Book value (RM)	1.79	2.04	2.27	2.45
Price/Book value (x)	1.54	1.35	1.21	1.12
Cashflow/share (sen)	27.5	30.5	30.7	32.4
Price/Cashflow (x)	10.0	9.0	9.0	8.5
Gearing (%) (including bills payables)	83	61	39	32
ROE (%)	10.4	10.8	9.8	9.7

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