

# Company Focus

# Muhibbah Engineering

Bloomberg: MUHI MK | Reuters: MUHI.KL

Refer to important disclosures at the end of this report

Malaysia Equity Research

3 Apr 2015

**BUY RM2.19** KLCI : 1,831.97

Price Target : 12-Month RM 3.50

Shariah Compliance : Yes

Reason for Report : Post-NDR update

Potential Catalyst: New contract wins, stronger passenger growth

AllianceDBS vs Consensus: We are more in line after consensus downgrade in earnings.

## Analyst

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## Price Relative



## Forecasts and Valuation

FY Dec (RM m)	2014A	2015F	2016F	2017F
Revenue	1,693	1,743	1,767	1,803
EBITDA	159	214	228	258
Pre-tax Profit	145	136	147	174
Net Profit	82	97	106	123
Net Pft (Pre Ex.)	82	97	106	123
EPS (sen)	19.3	22.9	25.1	29.0
EPS Pre Ex. (sen)	19.3	22.9	25.1	29.0
EPS Gth (%)	(6)	19	10	15
EPS Gth Pre Ex (%)	(6)	19	10	15
Diluted EPS (sen)	19.3	22.9	25.1	29.0
Net DPS (sen)	4.5	4.6	5.0	5.8
BV Per Share (sen)	152.4	169.8	190.3	214.3
PE (X)	11.3	9.5	8.7	7.6
PE Pre Ex. (X)	11.3	9.5	8.7	7.6
P/Cash Flow (X)	nm	3.8	7.2	6.8
EV/EBITDA (X)	11.2	7.6	6.9	5.9
Net Div Yield (%)	2.1	2.1	2.3	2.6
P/Book Value (X)	1.4	1.3	1.2	1.0
Net Debt/Equity (X)	0.7	0.5	0.4	0.3
ROAE (%)	13.5	14.2	14.0	14.3

Earnings Rev (%)	0	0	nm
Consensus EPS (sen)	23.0	24.3	28.5
Other Broker Recs:	B: 6	S: 1	H: 0

ICB Industry : Industrials

ICB Sector : Construction & Materials

Principal Business: Construction, cranes manufacturing, shipbuilding and Cambodian Airports concession

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

## Separating wheat from chaff

- Infrastructure division holds most promise
- Airport concession already 63% of market cap
- Favco exploring new revenue streams
- BUY, TP intact at RM3.50

**Infrastructure division most promising.** Muhibbah believes the infrastructure sector is on a multi-year upcycle with potentially RM140bn worth of projects (Table 1) up for grabs. Also, raw material costs are more 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 West Coast Expressway, and is quietly confident of clinching two other jobs with a combined value of RM900m. One is for a local port and the other an overseas job. YTD win is RM277m, and it should close the year better than the RM504m wins in 2014.

**Cambodian airports double capacity.** Effective July, the Siam Reap and Phnom Penh airports will double their existing capacity to 12m passengers. The US\$85m capex was financed by only one year of operating cashflow, which suggests the airports are cash cows. Passenger arrivals reached 5.7m in 2014 (+12 % y-o-y) led by a recovery in Chinese tourists (20% of total; +22% y-o-y). We estimate its 21% stake is worth RM580m (DCF, WACC of 10%, RM/USD3.65 and average passenger growth of 5% until 2040) which is already 63% of its market cap.

**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. We still expect a record year for Favco as it runs down its high-margin peak RM1bn orderbook. It is also exploring supplying cranes to RAPID.

**Separating wheat from chaff - BUY.** We remain convinced the stock had been unfairly sold down for its implied O&G exposure. Petronas has reiterated that RAPID will proceed as planned, and it represents just one of the many projects Muhibbah is looking to capitalise on. At current price, the market is assigning negligible value for the infrastructure, shipyard, Roadcare and Petronas license. BUY for 58% upside to our TP of RM3.50, which is pegged to 15x CY15 EPS (sector average).

## At A Glance

Issued Capital (m shrs)	432
Mkt. Cap (RMm/US\$m)	946 / 258
Major Shareholders	
Mac Ngan Boon (%)	22.1
Lembaga Tabung Haj (%)	9.6
Free Float (%)	60.7
Avg. Daily Vol.('000)	1,644

**INVESTMENT THESIS**

<b>Profile</b>	<b>Rationale</b>
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.	<p><b>PETRONAS license holder</b></p> <ul style="list-style-type: none"> <li>Recently awarded license will enable more jobs from PETRONAS</li> </ul> <p><b>Beneficiary of RAPID</b></p> <ul style="list-style-type: none"> <li>Stands a good to win jobs there given marine expertise</li> </ul> <p><b>Strong crane division</b></p> <ul style="list-style-type: none"> <li>Record high orderbook under Favelle Favco</li> </ul>
<b>Valuation</b>	<b>Risks</b>
Muhibbah is a BUY with a TP of RM3.50 based on 15x FY15F PE (sector average)	<p><b>Inability to secure new jobs</b></p> <ul style="list-style-type: none"> <li>This will lead to depleting orderbook</li> </ul> <p><b>Project delays</b></p> <ul style="list-style-type: none"> <li>Leading to slower revenue recognition</li> </ul> <p><b>Higher material price</b></p> <ul style="list-style-type: none"> <li>Leading to margin erosion</li> </ul>

Source: AllianceDBS

**Other FAQ at roadshow**

**What is the capacity for the infrastructure division?**

Muhibbah can take on another RM1-2bn worth of new orders before the infrastructure division reaches optimum capacity. Hence, it is also crucial to allocate resources appropriately. This is part of the reason it did not bid aggressively for the RM1bn Pengerang jetty works. The focus will be on margins rather than volume.

**How much more projects are you expecting from RAPID?**

Likely a few hundred million worth this year alone.

**What are margins for different segments in the infrastructure space?**

Generally, oil and gas jobs command 8-9% margins (before forex impact), marine 5-7%, and other civil jobs 4-5%.

**What are margins for tower cranes?**

Margins are comparable at 20% for oil and gas cranes. Repair and maintenance services command higher margins of 20-25%.

**How is the shipyard business doing?**

Current RM57m orderbook comprises just one vessel, with half of the value billed. Given the lean cost structure, the division is still able to make strong profits with just one ship order.

**Table 1 : List of potential projects in Malaysia**

Sector	Projects	RMbn
Oil and gas	Refinery and Petrochemical Integrated Development	97.2
Infra Construction	MRT 2 - Selayang to Putrajaya	25.0
	Highways - DUKE	1.2
	Highways - WCE	5.3
	Highways - SUKE	5.0
	Highways - DASH	4.2
	Highways - EKVE	1.6
Marine/Ports	Northport, Wesport and Samalaju Port	1.0
Total		140.5

Source: Companies, Various Sources, AllianceDBS, DBS Vickers

## Muhibbah Engineering

### Key Assumptions

FY Dec	2013A	2014A	2015F	2016F	2017F
Construction orderbook			550.0	1,000.0	1,200.0
Cranes orderbook			600.0	650.0	600.0
Shipyards orderbook			150.0	150.0	200.0

### Sensitivity Analysis

	2015
+RM500 new wins	Net Profit +7%

### Segmental Breakdown

FY Dec	2013A	2014A	2015F	2016F	2017F
<b>Revenues (RM m)</b>					
Construction	967	1,082	715	1,011	1,040
Cranes	762	798	840	563	565
Ships	207	223	189	193	198
<b>Total</b>	<b>1,936</b>	<b>1,693</b>	<b>1,743</b>	<b>1,767</b>	<b>1,803</b>

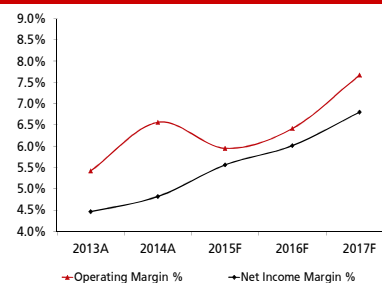
Assumes more contracts from RAPID and other projects

Conservatively expect softer growth for cranes

### Income Statement (RM m)

FY Dec	2013A	2014A	2015F	2016F	2017F
Revenue	1,936	1,693	1,743	1,767	1,803
Cost of Goods Sold	(1,723)	(1,583)	(1,520)	(1,537)	(1,545)
<b>Gross Profit</b>	<b>213</b>	<b>110</b>	<b>223</b>	<b>230</b>	<b>258</b>
Other Opng (Exp)/Inc	(108)	1	(119)	(116)	(119)
<b>Operating Profit</b>	<b>105</b>	<b>111</b>	<b>104</b>	<b>113</b>	<b>138</b>
Other Non Opng (Exp)/Inc	0	0	0	0	0
Associates & JV Inc	47	48	51	54	57
Net Interest (Exp)/Inc	(19)	(14)	(18)	(20)	(21)
Exceptional Gain/(Loss)	0	0	0	0	0
<b>Pre-tax Profit</b>	<b>133</b>	<b>145</b>	<b>136</b>	<b>147</b>	<b>174</b>
Tax	(16)	(34)	(17)	(19)	(23)
Minority Interest	(30)	(30)	(22)	(22)	(28)
Preference Dividend	0	0	0	0	0
<b>Net Profit</b>	<b>86</b>	<b>82</b>	<b>97</b>	<b>106</b>	<b>123</b>
Net Profit before Except.	86	82	97	106	123
EBITDA	206	159	214	228	258
<b>Growth</b>					
Revenue Gth (%)	(26.2)	(12.6)	3.0	1.4	2.0
EBITDA Gth (%)	(23.0)	(22.7)	34.5	6.8	13.1
Opg Profit Gth (%)	(40.1)	5.8	(6.6)	9.3	22.0
Net Profit Gth (%)	nm	(5.6)	18.9	9.6	15.4
<b>Margins &amp; Ratio</b>					
Gross Margins (%)	11.0	6.5	12.8	13.0	14.3
Opg Profit Margin (%)	5.4	6.6	6.0	6.4	7.7
Net Profit Margin (%)	4.5	4.8	5.6	6.0	6.8
ROAE (%)	17.0	13.5	14.2	14.0	14.3
ROA (%)	3.2	2.8	3.1	3.3	3.6
ROCE (%)	3.9	3.5	3.5	3.7	4.0
Div Payout Ratio (%)	21.9	23.4	20.0	20.0	20.0
Net Interest Cover (x)	5.5	8.1	5.7	5.8	6.5

### Margins Trend



Some margin expansion as Muhibbah moves up the value chain

Source: Company, AllianceDBS

**Quarterly / Interim Income Statement (RM m)**

FY Dec	4Q2013	1Q2014	2Q2014	3Q2014	4Q2014
Revenue	632	394	466	376	457
Other Oper. (Exp)/Inc	(588)	(378)	(429)	(351)	(424)
<b>Operating Profit</b>	<b>44</b>	<b>16</b>	<b>37</b>	<b>26</b>	<b>33</b>
Other Non Opg (Exp)/Inc	0	0	0	0	0
Associates & JV Inc	12	15	11	5	17
Net Interest (Exp)/Inc	(9)	0	(3)	(3)	(7)
Exceptional Gain/(Loss)	0	0	0	0	0
<b>Pre-tax Profit</b>	<b>46</b>	<b>31</b>	<b>45</b>	<b>28</b>	<b>42</b>
Tax	(9)	(9)	(14)	0	(10)
Minority Interest	(13)	(2)	(9)	(7)	(11)
<b>Net Profit</b>	<b>25</b>	<b>20</b>	<b>21</b>	<b>20</b>	<b>20</b>
Net profit bef Except.	25	20	21	20	20
EBITDA	68	44	62	45	69

**Growth**

Revenue Gth (%)	32.8	(37.6)	18.3	(19.3)	21.4
EBITDA Gth (%)	63.1	(35.7)	40.6	(27.5)	54.0
Opg Profit Gth (%)	173.3	(63.4)	132.3	(31.1)	27.5
Net Profit Gth (%)	22.1	(17.9)	3.8	(3.1)	0.0

**Margins**

Opg Profit Margins (%)	6.9	4.0	7.9	6.8	7.1
Net Profit Margins (%)	3.9	5.1	4.5	5.4	4.4

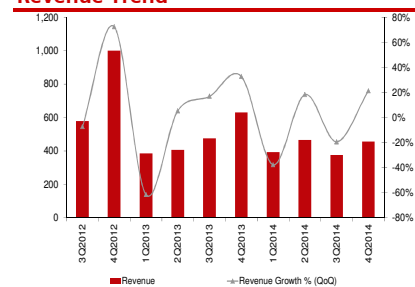
**Balance Sheet (RM m)**

FY Dec	2013A	2014A	2015F	2016F	2017F
Net Fixed Assets	711	725	708	690	670
Invt in Associates & JVs	190	236	284	335	389
Other LT Assets	30	31	31	31	31
Cash & ST Invt	426	601	809	907	1,012
Inventory	207	226	167	168	169
Debtors	1,077	1,334	1,146	1,162	1,185
Other Current Assets	10	13	13	13	13
<b>Total Assets</b>	<b>2,650</b>	<b>3,165</b>	<b>3,157</b>	<b>3,306</b>	<b>3,469</b>
ST Debt	738	1,168	1,198	1,228	1,258
Creditor	948	966	833	842	846
Other Current Liab	9	39	39	39	39
LT Debt	137	69	69	69	69
Other LT Liabilities	62	62	62	62	62
Shareholder's Equity	563	644	717	804	906
Minority Interests	194	217	239	262	290
<b>Total Cap. &amp; Liab.</b>	<b>2,650</b>	<b>3,165</b>	<b>3,157</b>	<b>3,306</b>	<b>3,469</b>

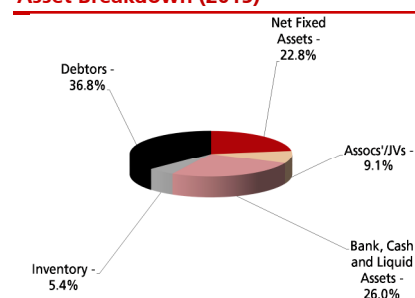
Non-Cash Wkg. Capital	337	567	454	462	482
Net Cash/(Debt)	(449)	(636)	(458)	(390)	(314)
Debtors Turn (avg days)	231.0	259.9	259.6	238.4	237.6
Creditors Turn (avg days)	215.7	220.7	224.8	207.1	208.0
Inventory Turn (avg days)	45.4	49.9	49.0	41.4	41.6
Asset Turnover (x)	0.7	0.6	0.6	0.5	0.5
Current Ratio (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	0.5	0.4	0.3
Net Debt/Equity ex MI (X)	0.8	1.0	0.6	0.5	0.3
Capex to Debt (%)	2.6	4.6	3.2	3.1	3.0
Z-Score (X)	1.4	1.1	1.2	1.2	1.3

Source: Company, AllianceDBS

**Revenue Trend**



**Asset Breakdown (2015)**



Net gearing manageable with low interest rates

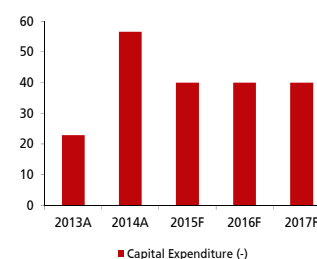
## Muhibbah Engineering

### Cash Flow Statement (RM m)

FY Dec	2013A	2014A	2015F	2016F	2017F
Pre-Tax Profit	133	145	136	147	174
Dep. & Amort.	54	0	59	61	63
Tax Paid	(16)	(34)	(17)	(19)	(23)
Assoc. & JV Inc/(loss)	(47)	(48)	(51)	(54)	(57)
Chg in Wkg.Cap.	223	(258)	114	(8)	(20)
Other Operating CF	21	122	0	0	0
<b>Net Operating CF</b>	<b>368</b>	<b>(73)</b>	<b>241</b>	<b>128</b>	<b>137</b>
Capital Exp.(net)	(23)	(57)	(40)	(40)	(40)
Other Invts.(net)	0	0	0	0	0
Invts in Assoc. & JV	(19)	(46)	0	0	0
Div from Assoc & JV	0	0	0	0	0
Other Investing CF	46	67	0	0	0
<b>Net Investing CF</b>	<b>5</b>	<b>(36)</b>	<b>(40)</b>	<b>(40)</b>	<b>(40)</b>
Div Paid	(19)	(46)	0	0	0
Chg in Gross Debt	(23)	(57)	(40)	(40)	(40)
Capital Issues	0	0	0	0	0
Other Financing CF	5	(36)	(40)	(40)	(40)
<b>Net Financing CF</b>	<b>(37)</b>	<b>(138)</b>	<b>(80)</b>	<b>(80)</b>	<b>(80)</b>
Currency Adjustments	46	67	0	0	0
Chg in Cash	382	(180)	121	8	17
Opg CFPS (sen)	34.3	43.9	30.2	32.2	37.1
Free CFPS (sen)	81.6	(30.6)	47.6	20.8	22.8

Source: Company, AllianceDBS

### Capital Expenditure



### Target Price & Ratings History



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

S.No.	Date	Closing Price	Target Price	Rating
1:	30 May 14	2.80	3.20	Buy
2:	11 Jun 14	3.07	3.20	Hold
3:	13 Jun 14	2.92	3.20	Hold
4:	03 Jul 14	3.04	3.20	Hold
5:	29 Aug 14	3.21	3.20	Hold
6:	03 Sep 14	3.04	3.20	Hold
7:	18 Nov 14	2.25	3.50	Buy
8:	01 Dec 14	1.98	3.50	Buy
9:	16 Jan 15	1.87	3.50	Buy
10:	05 Feb 15	2.00	3.50	Buy
11:	02 Mar 15	2.29	3.50	Buy

Source: AllianceDBS

## DISCLOSURE

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### 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

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