

# Company Focus

# Muhibbah Engineering

Bloomberg: MUHI MK | Reuters: MUHI.KL

Refer to important disclosures at the end of this report

Malaysia Equity Research

16 Jan 2015

**BUY RM1.94 KLCI : 1,745.00**

Price Target : 12-Month RM 3.50 (Prev RM 3.50)

Shariah Compliance: Yes

Reason for Report : Post Conference Update

Potential Catalyst: Contract wins from RAPID

AllianceDBS vs Consensus: We are below consensus

## Analyst

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## Price Relative



## Forecasts and Valuation

FY Dec (RM m)	2013A	2014F	2015F	2016F
Revenue	1,936	1,559	1,750	1,753
EBITDA	206	172	200	216
Pre-tax Profit	133	108	132	144
Net Profit	86	81	97	107
Net Pft (Pre Ex.)	86	81	97	107
EPS (sen)	20.4	19.2	22.9	25.2
EPS Pre Ex. (sen)	20.4	19.2	22.9	25.2
EPS Gth (%)	nm	(6)	20	10
EPS Gth Pre Ex (%)	(43)	(6)	20	10
Diluted EPS (sen)	20.4	19.2	22.9	25.2
Net DPS (sen)	4.5	3.8	4.6	5.0
BV Per Share (sen)	133.2	147.8	166.9	187.6
PE (X)	9.5	10.1	8.5	7.7
PE Pre Ex. (X)	9.5	10.1	8.5	7.7
P/Cash Flow (X)	2.2	52.0	12.5	6.6
EV/EBITDA (X)	7.1	8.8	7.7	6.9
Net Div Yield (%)	2.3	2.0	2.4	2.6
P/Book Value (X)	1.5	1.3	1.2	1.0
Net Debt/Equity (X)	0.6	0.6	0.5	0.4
ROAE (%)	17.0	13.6	14.6	14.2

Earnings Rev (%)	0	0	0
Consensus EPS (sen):	21.6	25.9	27.2
Other Broker Recs:	B: 5	S: 1	H: 1

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.

## Petronas license for free

- Expect infrastructure orderbook to surge
- Beneficiary of strengthening USD
- Market assigning negligible value to construction, shipyard and Petronas license
- BUY, TP RM3.50

**Unfairly driven by oil prices.** Muhibbah's share price continues to be dampened by falling oil prices. It is eyeing sub-contract works in RAPID but is merely a contractor and not an asset owner. We expect it to clinch RM300m-RM1bn of works from RAPID this year with a maiden win by 1QCY15. Its infrastructure division seems to be the weakest link with a RM903m orderbook (one year visibility) but it will also be the fastest growing division. Moreover, Petronas is committed to RAPID and has awarded works to major international EPCC players. Muhibbah's strong marine infrastructure expertise gives it a stranglehold of port projects, such the recent RM135m win at Westport (option for another RM256m). It is also eyeing works for seven highways worth c.RM20bn.

**Two bites of the cherry.** Operationally, Favco and its Cambodian concession have never been stronger with peak orderbook and strong passenger arrivals. We estimate c.65% of FY15F pretax profit (Favco and Cambodian airport concession) will benefit from an appreciating USD, which the market has ignored. 60-70% of Favco's revenue is in USD while 80% of the cost of its cranes is in Ringgit and manufactured at its plant in Senawang. Favco is also seeing increasing use of cranes in the US construction industry, which could make up for a potential slowdown in crane demand in the oil & gas sector. The cash-generating Cambodia airport concession also generates USD revenues and registered a 12% increase in passenger arrivals in 2014.

**Zero value for construction and shipyard.** Valuation is a bargain now, at only 7.7x and 1.2x FY15 PE and P/NTA, respectively. At this level, the market appears to assign negligible value for its infrastructure business, shipyard and Petronas fabrication license. This is after stripping out its 60.3% stake in Favco and DCF value for the Cambodia airport concession. We reiterate our BUY rating and TP of RM3.50 based on 15x FY15F PE (sector average).

## At A Glance

Issued Capital (m shrs)	430
Mkt. Cap (RMm/US\$m)	834 / 233
Major Shareholders	
Mac Ngan Boon (%)	22.1
Lembaga Tabung Haj (%)	9.6
Free Float (%)	60.7
Avg. Daily Vol.('000)	3,536

**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

**Market assigning negligible value for infrastructure, shipyard, Roadcare and Petronas license**

	RMm	Remarks
Muhibbah's current market cap	795.5	Market Value
Less : 60.3% stake in Favco	358.3	Market Value
Less : 21% stake in Cambodian airport concession	427.9	DCF based on WACC of 10% until 2040
Residual Value	9.4	Implied value market assigning to infrastructure, shipyard, Roadcare and Petronas fabrication license

Source: AllianceDBS

**RAPID - Potential wins for package 1, 3, 4 and 5**

		Winner	Subcontractor Winner
<b>Package 1</b>	Residue fluid catalytic crackin, LPG Treating, Propylene recovery and caustic neutralisation	CTCI Corp, Chiyoda Corp, Synerlitz (M) Sdn Bhd and MIE Industrial Sdn Bhd	Still bidding
<b>Package 2</b>	Crude distillation, atmospheric desulphurisation and hydrogen collection and distribution unit	Sinopec	KNM
<b>Package 3</b>	Kerosene hydrotreating, diesel hydrotreating, naphtha hydrotreating, cracked naphtha hydrotreating, continuous catalytic reformer, hydrogen production, refinery pressure swing adsorber and saturated gas plant	Técnicas Reunidas S.A. and Técnicas Reunidas Malaysia Sdn Bhd	Still bidding
<b>Package 4</b>	Amine regeneration, sulphur recovery, liquid sulphur feed storage, sulphur solidification, sour water stripping	Petrofac International (UAE) LLC and Petrofac E&C Sdn Bhd	Still bidding
<b>Package 5</b>	Steam cracker complex	Toyo Engineering Corp and Toyo Engineering & Construction Sdn Bhd	Still bidding

Source: AllianceDBS

**Sensitivity Analysis**

+RM500m new wins	<b>2015</b> Net Profit +7%
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**Key Assumptions**

FY Dec	2012A	2013A	2014F	2015F	2016F
Construction orderbook				1,000.0	1,000.0
Cranes orderbook				600.0	650.0
Shipyards orderbook				150.0	150.0
Orderbook replenishment				1,750.0	1,800.0

**Segmental Breakdown**

FY Dec	2012A	2013A	2014F	2015F	2016F
<b>Revenues (RM m)</b>					
Construction	1,669	967	628	722	997
Cranes	696	762	867	840	563
Ships	261	207	64	189	193

Expect some wins from RAPID

Orders from Favco have been strong

<b>Total</b>	<b>2,626</b>	<b>1,936</b>	<b>1,559</b>	<b>1,750</b>	<b>1,753</b>
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**Income Statement (RM m)**

FY Dec	2012A	2013A	2014F	2015F	2016F
Revenue	2,626	1,936	1,559	1,750	1,753
Cost of Goods Sold	(2,354)	(1,723)	(1,381)	(1,547)	(1,543)
<b>Gross Profit</b>	<b>272</b>	<b>213</b>	<b>178</b>	<b>203</b>	<b>210</b>
Other Opng (Exp)/Inc	(96)	(108)	(113)	(116)	(113)
<b>Operating Profit</b>	<b>175</b>	<b>105</b>	<b>64</b>	<b>87</b>	<b>98</b>
Other Non Opg (Exp)/Inc	0	0	0	0	0
Associates & JV Inc	44	47	52	55	59
Net Interest (Exp)/Inc	(9)	(19)	(9)	(11)	(12)
Exceptional Gain/(Loss)	(245)	0	0	0	0
<b>Pre-tax Profit</b>	<b>(35)</b>	<b>133</b>	<b>108</b>	<b>132</b>	<b>144</b>
Tax	(26)	(16)	(11)	(15)	(17)
Minority Interest	(32)	(30)	(16)	(20)	(21)
Preference Dividend	0	0	0	0	0
<b>Net Profit</b>	<b>(93)</b>	<b>86</b>	<b>81</b>	<b>97</b>	<b>107</b>
Net Profit before Except.	152	86	81	97	107
EBITDA	267	206	172	200	216

**Growth**

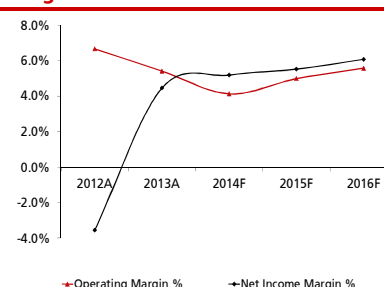
Revenue Gth (%)	29.6	(26.2)	(19.5)	12.3	0.2
EBITDA Gth (%)	57.1	(23.0)	(16.2)	16.2	7.8
Opg Profit Gth (%)	74.4	(40.1)	(38.6)	35.7	12.0
Net Profit Gth (%)	nm	nm	(6.2)	19.5	10.2

**Margins & Ratio**

Gross Margins (%)	10.3	11.0	11.4	11.6	12.0
Opg Profit Margin (%)	6.7	5.4	4.1	5.0	5.6
Net Profit Margin (%)	(3.6)	4.5	5.2	5.5	6.1
ROAE (%)	(19.2)	17.0	13.6	14.6	14.2
ROA (%)	(3.3)	3.2	3.1	3.6	3.7
ROCE (%)	7.8	3.9	4.1	4.6	4.7
Div Payout Ratio (%)	N/A	21.9	20.0	20.0	20.0
Net Interest Cover (x)	18.7	5.5	7.2	8.3	8.1

Source: Company, AllianceDBS

**Margins Trend**



Higher margins from more marine-based infrastructure works

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

FY Dec	3Q2013	4Q2013	1Q2014	2Q2014	3Q2014
Revenue	475	632	394	466	376
Cost of Goods Sold	0	0	0	0	0
<b>Gross Profit</b>	<b>475</b>	<b>632</b>	<b>394</b>	<b>466</b>	<b>376</b>
Other Oper. (Exp)/Inc	(460)	(588)	(378)	(429)	(351)
<b>Operating Profit</b>	<b>16</b>	<b>44</b>	<b>16</b>	<b>37</b>	<b>26</b>
Other Non Opg (Exp)/Inc	0	0	0	0	0
Associates & JV Inc	12	12	15	11	5
Net Interest (Exp)/Inc	(1)	(9)	0	(3)	(3)
Exceptional Gain/(Loss)	0	0	0	0	0
<b>Pre-tax Profit</b>	<b>27</b>	<b>46</b>	<b>31</b>	<b>45</b>	<b>28</b>
Tax	2	(9)	(9)	(14)	0
Minority Interest	(9)	(13)	(2)	(9)	(7)
<b>Net Profit</b>	<b>20</b>	<b>25</b>	<b>20</b>	<b>21</b>	<b>20</b>
Net profit bef Except.	20	25	20	21	20
EBITDA	42	68	44	62	45

**Growth**

Revenue Gth (%)	16.9	32.8	(37.6)	18.3	(19.3)
EBITDA Gth (%)	(16.9)	63.1	(35.7)	40.6	(27.5)
Opg Profit Gth (%)	(41.1)	173.3	(63.4)	132.3	(31.1)
Net Profit Gth (%)	(3.0)	22.1	(17.9)	3.8	(3.1)

**Margins**

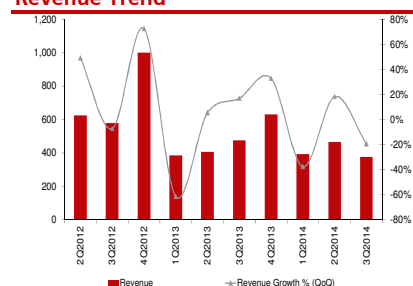
Gross Margins (%)	100.0	100.0	100.0	100.0	100.0
Opg Profit Margins (%)	3.4	6.9	4.0	7.9	6.8
Net Profit Margins (%)	4.2	3.9	5.1	4.5	5.4

**Balance Sheet (RM m)**

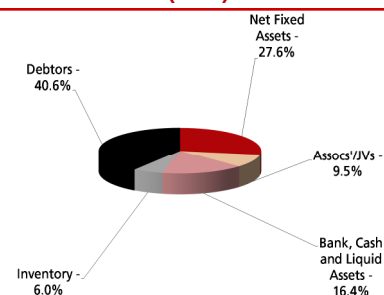
FY Dec	2012A	2013A	2014F	2015F	2016F
Net Fixed Assets	718	711	697	681	663
Invt in Associates & JVs	171	190	241	294	351
Other LT Assets	18	30	30	30	30
Cash & ST Invt	337	426	413	453	547
Inventory	209	207	151	170	169
Debtors	1,374	1,077	1,025	1,151	1,153
Other Current Assets	6	10	10	10	10
<b>Total Assets</b>	<b>2,834</b>	<b>2,650</b>	<b>2,567</b>	<b>2,788</b>	<b>2,924</b>
ST Debt	959	738	768	798	828
Creditor	1,025	948	757	848	845
Other Current Liab	15	9	9	9	9
LT Debt	154	137	137	137	137
Other LT Liabilities	60	62	62	62	62
Shareholder's Equity	454	563	625	705	793
Minority Interests	166	194	210	230	251
<b>Total Cap. &amp; Liab.</b>	<b>2,834</b>	<b>2,650</b>	<b>2,567</b>	<b>2,788</b>	<b>2,924</b>
Non-Cash Wkg. Capital	549	337	421	474	478
Net Cash/(Debt)	(777)	(449)	(492)	(482)	(417)
Debtors Turn (avg days)	194.8	231.0	246.1	226.9	239.8
Creditors Turn (avg days)	162.5	215.7	234.7	196.6	208.3
Inventory Turn (avg days)	32.6	45.4	49.3	39.3	41.7
Asset Turnover (x)	0.9	0.7	0.6	0.7	0.6
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)	1.3	0.6	0.6	0.5	0.4
Net Debt/Equity ex MI (X)	1.7	0.8	0.8	0.7	0.5
Capex to Debt (%)	(6.7)	2.6	4.4	4.3	4.1
Z-Score (X)	1.5	1.4	1.3	1.4	1.4

Source: Company, AllianceDBS

**Revenue Trend**



**Asset Breakdown (2014)**



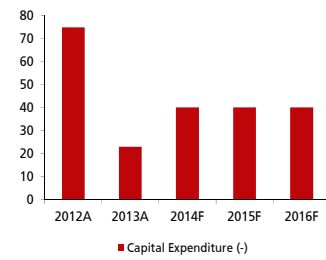
## Muhibbah Engineering

### Cash Flow Statement (RM m)

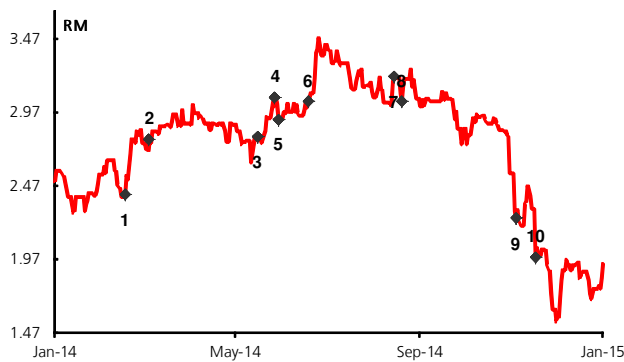
FY Dec	2012A	2013A	2014F	2015F	2016F
Pre-Tax Profit	(35)	133	108	132	144
Dep. & Amort.	48	54	56	57	59
Tax Paid	(26)	(16)	(11)	(15)	(17)
Assoc. & JV Inc/(loss)	(44)	(47)	(52)	(55)	(59)
Chg in Wkg.Cap.	43	223	(84)	(53)	(4)
Other Operating CF	172	21	0	0	0
<b>Net Operating CF</b>	<b>157</b>	<b>368</b>	<b>16</b>	<b>66</b>	<b>124</b>
Capital Exp.(net)	75	(23)	(40)	(40)	(40)
Other Invt.(net)	0	0	0	0	0
Invt in Assoc. & JV	(29)	(19)	0	0	0
Div from Assoc & JV	0	0	0	0	0
Other Investing CF	(94)	46	0	0	0
<b>Net Investing CF</b>	<b>(48)</b>	<b>5</b>	<b>(40)</b>	<b>(40)</b>	<b>(40)</b>
Div Paid	(29)	(19)	0	0	0
Chg in Gross Debt	75	(23)	(40)	(40)	(40)
Capital Issues	0	0	0	0	0
Other Financing CF	(48)	5	(40)	(40)	(40)
<b>Net Financing CF</b>	<b>(3)</b>	<b>(37)</b>	<b>(80)</b>	<b>(80)</b>	<b>(80)</b>
Currency Adjustments	(94)	46	0	0	0
Chg in Cash	12	382	(104)	(54)	4
Opg CFPS (sen)	27.0	34.3	23.7	28.1	30.3
Free CFPS (sen)	54.9	81.6	(5.7)	6.1	19.9

Source: Company, AllianceDBS

### Capital Expenditure



### Target Price & Ratings History



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

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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