

04 October 2016

George Kent (M) Berhad

Update to Upgrade!

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INVESTMENT MERIT

Since our last report dated 8/8/16, GKENT's (i) share price surged 35%, (ii) 1H17 results outperformed expectations at 56% due to our conservative construction margins, (iii) GKENT with CCCC secured system works package for MRT2 worth RM1.01b and (iv) bonus issue completed with the issuance of 75.1m new shares. Post results, upgrade GKENT's FY17 CNP by 18%. Reiterate our Trading Buy call with higher TP of RM2.80 (from RM2.17) based on SOP and selected GKENT to be our Top 10 Picks in 4QCY16.

1H17 results above expectations. 1H17 CNP of RM35.5m came in above expectations accounting for 56% of our full-year estimate. The positive variance was due to higher-than-expected margins achieved in their engineering division. 3.0 sen dividend declared, which was within our full-year estimates of 8.0 sen. 1H17 CNP was up 93.7% YoY on the back of: (i) stronger revenue (+65.7%) due to higher engineering billings (+85.5%) coupled with stronger construction margins (+2ppt), (ii) higher interest income (+30.4%), (iii) higher contribution from associates and JV (+216.6%), and (iv) lower effective tax rate (-6ppt). 2Q17 CNP was up 36.7% QoQ mainly underpinned by: (i) higher PBT contributions from metering division (+120.4%) on the back of higher metering revenue (+15.7%) with better margins (+12ppt), and (ii) higher contributions of associates/JV (+149.2%).

System works for MRT 2. On 25th of August, GKENT together with CCCC under a 49:51 JV structure managed to secure the Systems Works Package (SSP-SY-204) from MRT Corp S/B worth RM1.01b. The contract entails engineering, procurement, construction testing and commissioning of track works, maintenance vehicles and work trains for MRT 2 (SSP line) slated for completion in 1st May 2021 for Phase 1 and 1st May 2022 for other remaining works. We are mildly positive on the win as although GKENT's 49% portion of c.RM495m is within our orderbook replenishment target of RM700m (making up 70%), we note that GKENT's has outstanding tenders for 2 hospital jobs worth RM700m which we believe is highly achievable based on their track record within the health care sector since 2009. Nonetheless, we choose to keep our FY17 replenishment target of RM700m unchanged for now as the awards for the hospital jobs might cross over into FY18. Post-award, GKENT's outstanding orderbook stands at c.RM1.1b (exclude LRT3 PDP role) providing healthy earnings visibility for the next 2 years.

4-for-1 bonus issue completed. GKENT's proposed 4-for-1 bonus issue was completed on the 22nd of September 2016 with the issuance of 75.1m new shares. Outstanding GKENT shares currently stand at 375.5m.

Earnings Upgrade for FY17! Post outperformance in results, we upgrade FY17 earnings by 18% but make no changes to FY18 earnings after tweaking our conservative FY17 engineering margins higher from 12% to 15%.

Reiterate TRADING BUY and included in our Top 10 picks. Since our last report (8/8/16) GKENT has surged by 35%. After adjustment in earnings and accounting for the new bonus shares, we upgrade GKENT's fair value higher to RM2.80 (from RM2.17) based on new SoP valuations. Within our SoP (*refer back*), we have upgraded our conservative construction division's valuations higher from 10x to 12x FY17 PER in line with peers such as MITRA, GADANG and KERJAYA. We believe the upgrade is justifiable considering: (i) GKENT's strong net cash position, and (ii) superior construction PBT margin of 18% in 1H17, which is above peers' range of 12-17%. However, despite the stronger margin, GKENT's outstanding order book of RM1.1b still trails behind peers' range of RM1.6b to RM2.9b; hence, we believe the 12x FY17 PER for their construction arm is fair. That said, we believe potential re-rating catalyst for GKENT is higher construction contract value for LRT3 of above RM9.0b as this would further increase profitability based on the PDP fees of 6%. We have also selected GKENT to be a Top 10 Picks for our 4QCY16 strategy.

	Rating	Fair Value
Last Price		RM2.55
Kenanga	Trading Buy	RM2.80
Consensus	Buy	RM3.25

Stock Information

Shariah Compliant	Yes
Stock Name	GEORGE KENT (M) BHD
CAT Code	3204
Industry	Industrials
Industry Sub-sector	Industrials Machinery
YTD stock price chg	95.6%
Market Cap (RM m)	957.6
Issued shares (m)	375.5
52-week range (Hi)	2.61
52-week range (Low)	1.18
3-mth avg daily vol:	2,882,049
Free Float	73%
Beta	1.0
Altman's Z-score	2.52

Major Shareholders

Star Wealth Investment Limited	14.0%
Swee Bee Tan	7.7%
Hectomic Ltd	5.0%

Financials

FYE Jan (RM'm)	2016A	2017E	2018E
Revenue	538.1	663.8	533.4
EBIT	60.1	99.7	79.4
Net Profit (NP)	50.3	74.7	100.5
EPS (sen)	13.4	19.9	26.8
BV/Share (RM)	0.9	1	1.2
PER	20.9	14.1	10.5
Price/BV (x)	3.3	2.9	2.4
Net Gearing (x)	-0.7	-0.8	-0.9
DPS (sen)	5.6	8	6.7
Dividend Yield (%)	2.00%	2.80%	2.40%

Quarterly

Financial Data	4Q16	1Q17	2Q17
Revenue	267.5	123.0	164.8
PBT	28.0	20.3	26.4
Net Profit (NP)	19.9	15.0	20.5
EPS (sen)	6.6	5.0	5.5
EPS Growth (QoQ)	65%	-24%	10%
Rev. growth (QoQ)	176%	-54%	34%
PBT Margin	10%	16%	16%

Peers Comparisons	PER (FY17)	Div. Yld (%)	Mkt Cap (RM'm)
KERJAYA	10.9	2.1	1167
MITRA	9.8	3.1	916
GADANG	7.4	2.3	742
Average	9.4	2.5	942
GKENT	14.1	2.8	958
FBMKLCI	15.1	3.3	993b

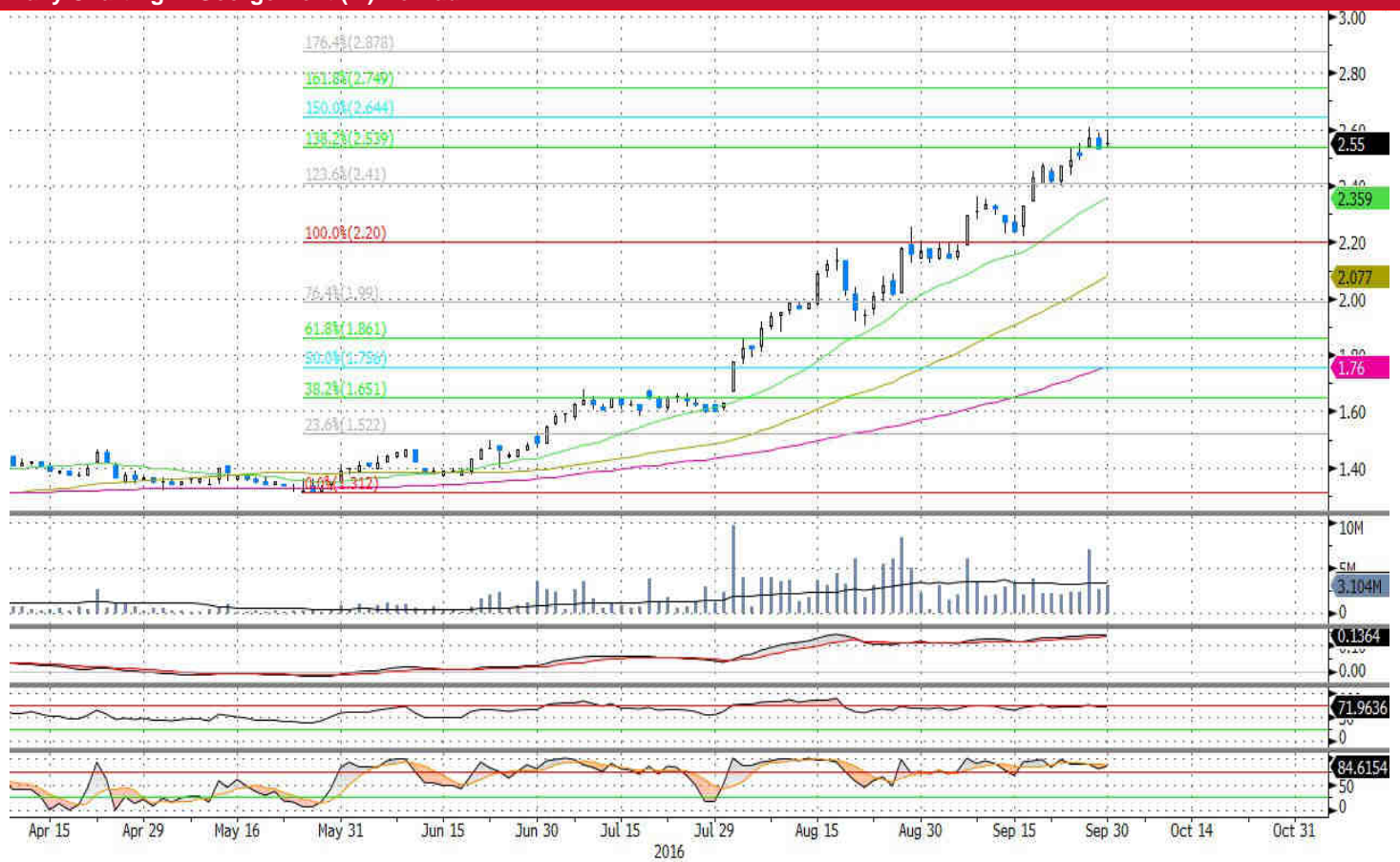
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Sum of Parts Valuation

Division	Market Cap (RM'm)	% of SoP
Metering - 8x FY17 PER (comparable with ENGTEX)	97.7	12%
Construction - 12x FY17 PER (in line with peers i.e. KERJAYA, MITRA, GADANG of 12-13x)	749.6	71%
PDP NPV (WACC at 10%) with an applied discount of 30%	107.5	10%
Net Cash (1Q16) with an applied discount of 43% in line with PTARAS	95.9	12%
Total	1050.7	
Shares Outstanding	375.5	
Target Price	2.80	

Source: Bloomberg, Kenanga Research

Daily Charting – George Kent (M) Berhad



Comment: GKENT has been trading on an uptrend trajectory since early June 2016, with the underlying outlook still positive amid being supported by all its up trending moving averages. Should the bulls remain in play, the stock could set sight to retest its immediate resistance level of RM2.64 (R1) with next overhead levels capped at RM2.75 (R2)/RM2.88 (R3). Nonetheless, RSI and Stochastic indicator are suggesting that the stock could be topping at this point, depicted by the overbought condition seen by the respective indicators. Taking the above into consideration, we advocate interested investors to adopt a more conservative approach by setting sight to buy on any share price weakness, preferably any dips closer towards the RM2.40 (S2) level. Key support levels are tied at RM2.53 (S1)/RM2.40 (S2)/RM2.20 (S3).

Source: Kenanga Research

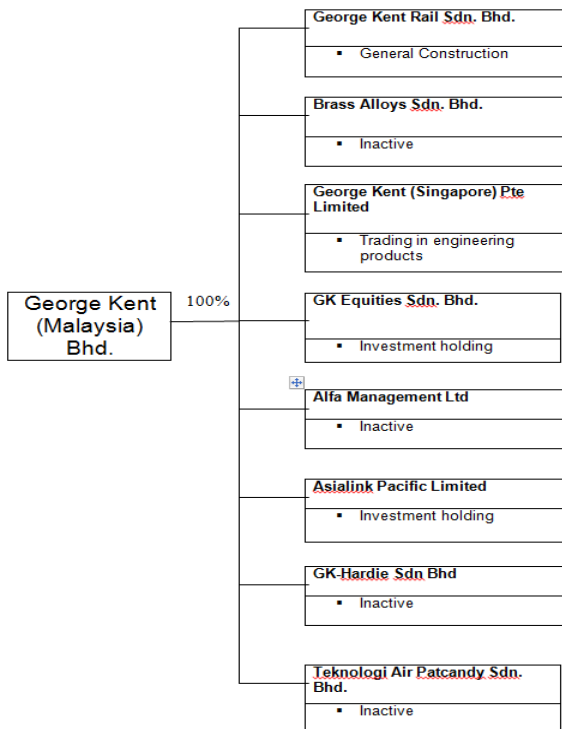
About the stock:

Name : George Kent (M) Berhad
Bursa Code : GKENT
CAT Code : 3204

Key Support & Resistance level

Resistance : RM2.64 (R1) RM2.75 (R2) RM2.88 (R3)
 Support : RM2.53 (S1) RM2.40 (S2) RM2.20 (S3)
 Outlook : Bullish

CORPORATE STRUCTURE



BUSINESS OVERVIEW

- George Kent has its origin in Penang as a service branch office of George Kent Limited, U.K. in 1936. The company set up a manufacturing plant on a 4-acre site in Shah Alam in July 1968. Four years later, George Kent was listed on the Kuala Lumpur Stock Exchange (KLSE).
- George Kent underwent expansion when it moved to a 17-acre modern and integrated manufacturing facility in Puchong, Selangor in January 1997.
- George Kent is a world-renowned and leading manufacturer of water meters, valves and fittings and brass products, exporting to more than 40 countries in several continents including Singapore, Vietnam, Thailand, Cambodia, Indonesia, Philippines, Papua New Guinea, Australia, Hong Kong, Sri Lanka, Kenya, South Africa, Colombia and the United Kingdom.

BUSINESS SEGMENTS

- **Engineering:** Includes water supply infrastructure, rail transportation and hospitals. Have undertaken various projects and has accumulated valuable experience in the turnkey design and build as well as conventional construction of water-treatment plants. The engineering division has also kept the Group in a forward-moving course as it has enabled the Group to deliver more than 30 projects in the water infrastructure, water works and services, rail transportation and healthcare sectors.
- **Metering:** Includes metering, industrial products, industrial process manufacturing and OEM.

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