

George Kent (BUY ↔; EPS ↔)
INDUSTRY: OVERWEIGHT
EARNINGS EVALUATION
28 September 2016
Price Target: RM3.25 (↑)
Share price: RM2.51
A strong showing
Results

- GKent reported 2QFY17 results with revenue of RM164.8m (+44% YoY, +34% QoQ) and core earnings (ex. forex) of RM18.7m (+223% YoY, +19% QoQ). Cumulative 1HFY17 core earnings of RM34.5m soared 140% YoY.

Deviation

- 1H earnings were above expectations at 67% of our full year forecast. This was due to the upside surprise for engineering margins and JV profits (from the LRT3 PDP).

Dividends

- An interim dividend of 3 sen was declared.

Highlights

- **Best of both worlds for engineering.** The engineering division experienced the best of both worlds with 1H revenue growing +85% and PBT margins expanding from 15.2% to 16.7%. We reckon that this was largely due to the balance of works for the LRT Ampang extension (i.e. ongoing system upgrades and depot remodelling) as well as recognition of certain variation orders (VOs). Looking forward into 2H, we see the possibility of a downward normalisation in margins should less VOs be recognised. This is somewhat evident QoQ with PBT margins normalising from 20.8% to 13.7%.
- **Sitting on a superior orderbook.** GKent has managed to secure RM494m worth of contracts YTD, consisting of the MRT2 track works. On potential job wins in the near term, GKent has a Letter of Intent (LOI) for a hospital job in Putrajaya worth RM300-350m which could materialise to an award by year end. GKent's orderbook is currently at a record high of RM5.4bn, implying a superior cover of 13.2x on FY16 construction revenue (highest ratio within our coverage).
- **Steady metering contribution.** PBT for metering remained steady in 1H (+3% YoY) as higher revenue (+19% YoY) was offset by margin contraction from 22.5% to 19.6% due to the stronger ringgit against the US dollar. Potential catalysts for this division include securing the metering supply tenders for the states of Malacca and Selangor.

Risks

- Any possible delays in the LRT3 would be the key risk.

Forecasts

- While 1H results appear to be above expectation, we have chosen to take the conservative stance and retain our forecasts. This is in view of the potential downward normalisation in engineering margins for 2H as the LRT extension balance of works approaches completion.

Rating
Maintain BUY, TP: RM3.25 (ex. bonus)

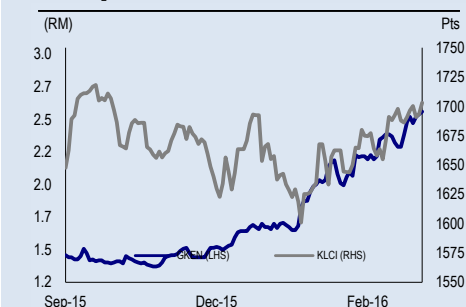
- GKent is a key rail play with exposure to the LRT extension, LRT3 and MRT2. It also boasts solid financials with 3-year earnings CAGR of 26%, above industry ROE of 15.4% and net cash position of RM0.64/share (25% of market cap).

Valuation

- Our SOP based TP is raised slightly from RM3.21 (ex. bonus) to RM3.25 as we update for its latest net cash balance.

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KLCI	1664.7
Expected share price return	29.5%
Expected dividend return	2.2%
Expected total return	31.7%

Share price

Information

Bloomberg Ticker	GKEN MK
Bursa Code	3204
Issued Shares (m)	376
Market cap (RM m)	943
3-mth avg. volume ('000)	2,716
SC Shariah-compliant	Yes

Price Performance	1M	3M	12M
Absolute	15.3	71.4	105.1
Relative	16.6	68.3	98.1

Major shareholders

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

Summary Earnings Table

FYE Jan (RM m)	FY16	FY17F	FY18F	FY19F
Revenue	536	563	438	450
EBITDA	65	77	60	59
EBIT	61	73	56	55
Profit Before Tax	61	74	87	96
Core PATAMI	40	52	70	80
vs Consensus (%)	-	-	-	-
Core EPS (sen)	10.7	13.8	18.7	21.2
P/E (x)	23.5	18.2	13.4	11.8
P/E ex cash (x)	17.5	13.6	10.0	8.8
Net DPS (sen)	5.6	6.9	9.3	10.6
Net DY (%)	2.2	2.7	3.7	4.2
BV per share	0.86	0.93	1.02	1.13
P/B (x)	2.9	2.7	2.5	2.2
ROE (%)	13.2	15.4	19.2	19.8
Net Gearing (%)	CASH	CASH	CASH	CASH

HLIB

Figure #1 Quarterly results comparison

FYE Jan (RM m)	2QFY17	2QFY16	1QFY17	YoY (%)	QoQ (%)	Comments
Revenue	164.8	114.7	123.0	43.7	34.0	YoY and QoQ growth largely driven by engineering from the LRT extension balance of works.
EBIT	23.1	10.5	20.8	121.0	11.1	See margin commentary.
Finance cost	(0.7)	(0.5)	(0.5)	26.1	28.5	
Associates & JVs	2.1	0.4	0.7	410.4	201.3	YoY and QoQ growth driven by LRT3 PDP fees.
PBT	24.6	10.4	21.0	137.3	17.0	
PAT	18.7	5.8	15.7	222.7	19.0	
PATMI - core	18.7	5.8	15.7	222.7	19.0	
PATMI - reported	20.5	8.5	15.0	142.1	36.7	Includes forex impact.
EPS - core	5.0	1.5	4.2			
EBIT margin (%)	14.0	9.1	16.9			YoY: Higher as more VOs recognised. QoQ: Lower due to normalisation of margins as less VOs recognised.
PBT margin (%)	14.9	9.0	17.1			
Company						

Figure #2 Quarterly results comparison

FYE Jan (RM m)	6MFY17	6MFY16	YoY (%)	Comments
Revenue	287.7	173.7	65.7	Engineering grew 85% and metering 19%.
EBIT	44.0	22.5	95.5	Amplified growth due to margin expansion.
Finance cost	(1.2)	(1.2)	(1.1)	
Associates & JVs	2.8	0.9	216.6	Driven by LRT3 PDP fees.
PBT	45.6	22.2	105.5	
PAT	34.5	14.3	140.3	
PATMI - core	34.5	14.3	140.3	1H made up 67% of our full year forecast.
PATMI - reported	35.5	18.3	93.7	
EPS - core	9.2	3.8		
EBIT margin	15.3	13.0		Higher margins due to more VOs recognised.
PBT margin	15.9	12.8		
Company				

Figure #3 SOP based valuation for GKent

SOP Component	Amount (RM m)	Multiple (x)	Valuation (RM m)	Per Share
FY18 core earnings	70	14	982	2.61
Net cash	240	1	240	0.64
SOP Value			1,222	3.25

HLIB estimates

Financial Projections for George Kent

Balance Sheet

FYE Jan (RM m)	FY15	FY16	FY17F	FY18F	FY19F
Cash	164	242	236	272	313
Receivables	246	241	262	204	210
Inventories	42	48	59	46	47
PPE	121	121	119	117	115
Others	33	31	31	31	31
Assets	606	683	707	670	716
Debits	58	27	37	35	32
Payables	256	326	314	245	253
Others	5	8	8	8	8
Liabilities	319	361	360	287	294
Shareholder's equity	287	322	348	383	423

Cash Flow Statement

FYE Jan (RM m)	FY15	FY16	FY17F	FY18F	FY19F
Profit before taxation	41	61	74	87	96
Share of JV and associates	(2)	(2)	(4)	(33)	(43)
Depreciation & amortisation	4	4	4	4	4
Changes in working capital	(92)	69	(44)	2	2
Taxation	(12)	(21)	(23)	(17)	(16)
Others	(4)	16	(0)	24	38
CFO	(67)	127	8	66	81
Net capex	1	3	(2)	(2)	(2)
Others	(2)	(5)	-	-	-
CFI	(1)	(2)	(2)	(2)	(2)
Changes in borrowings	41	(31)	10	(3)	(3)
Issuance of shares	66	2	-	-	-
Dividends paid	(16)	(16)	(21)	(26)	(35)
Others	(88)	13	-	-	-
CFB	4	(33)	(11)	(28)	(38)
Net cash flow	(64)	92	(5)	36	41
Forex	(1)	2	-	-	-
Others	18	(16)	-	-	-
Beginning cash	211	164	242	236	272
Ending cash	164	242	236	272	313

Income Statement

FYE Jan (RM m)	FY15	FY16	FY17F	FY18F	FY19F
Revenue	353	536	563	438	450
EBITDA	44	65	77	60	59
EBIT	41	61	73	56	55
Finance cost	(2)	(3)	(2)	(2)	(2)
Associates & JV	2	2	4	33	43
Profit before tax	41	61	74	87	96
Tax	(12)	(21)	(23)	(17)	(16)
PATMI (core)	28	40	52	70	80
Exceptionals	(0)	10	-	-	-
PATMI (reported)	28	50	52	70	80

Valuation & Ratios

FYE Jan (RM m)	FY15	FY16	FY17F	FY18F	FY19F
Core EPS (sen)	7.5	10.7	13.8	18.7	21.2
P/E (x)	33.3	23.5	18.2	13.4	11.8
EV/EBITDA (x)	15.9	10.8	9.2	11.7	11.9
DPS (sen)	4.2	5.6	6.9	9.3	10.6
Dividend yield	1.7%	2.2%	2.7%	3.7%	4.2%
BVPS (RM)	0.76	0.86	0.93	1.02	1.13
P/B (x)	3.3	2.9	2.7	2.5	2.2
EBITDA margin	12.5%	12.1%	13.6%	13.7%	13.1%
EBIT margin	11.5%	11.4%	12.9%	12.8%	12.2%
PBT margin	11.5%	11.3%	13.2%	19.8%	21.3%
Net margin	8.0%	7.5%	9.2%	16.0%	17.7%
ROE	10.6%	13.2%	15.4%	19.2%	19.8%
ROA	5.1%	6.2%	7.4%	10.2%	11.5%
Net gearing	CASH	CASH	CASH	CASH	CASH

Assumptions

FYE Jan (RM m)	FY15	FY16	FY17F	FY18F	FY19F
Contracts secured	57	4,500	844	300	300

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BUY	Positive recommendation of stock under coverage. Expected absolute return of more than +10% over 12-months, with low risk of sustained downside.
TRADING BUY	Positive recommendation of stock not under coverage. Expected absolute return of more than +10% over 6-months. Situational or arbitrage trading opportunity.
HOLD	Neutral recommendation of stock under coverage. Expected absolute return between -10% and +10% over 12-months, with low risk of sustained downside.
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OVERWEIGHT	The sector, based on weighted market capitalization, is expected to have absolute return of more than +5% over 12-months.
NEUTRAL	The sector, based on weighted market capitalization, is expected to have absolute return between -5% and +5% over 12-months.
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