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George Kent earnings surge 140% for 1HFY17

▶ Recommendation: Buy

TARGET Price: RM3.25
by Hong Leong Investment Bank Bhd (Sept 28)

▶ GEORGE KENT (M) BHD

FYE JAN	FY16	FY17F	FY18F	FY19F
REVENUE (RM mil)	536	563	438	450
CORE PATAMI (RM mil)	40	52	70	80
CORE EPS (sen)	10.7	13.8	18.7	21.2
PE (x)	23.5	18.2	13.4	11.8

Results

GEORGE Kent (M) Bhd (GKent) reported 2QFY17 results with revenue of RM164.8m (+44% YoY, +34% QoQ) and core earnings of RM18.7m (+223% YoY, +19% QoQ).

Cumulative 1HFY17 core earnings of RM34.5m soared 140% YoY.

Deviation

The company's 1H earnings were above expectations at 67% of our full-year forecast. This was due to the upside surprise for engineering margins and joint-venture profits.

Dividends

An interim dividend of three sen was declared.

Highlights

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 light rail transit (LRT) Ampang extension (ie 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 Mass Rapid Transit Line 2 (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 RM300m-RM350m which could materialise to an award by year end. GKent's orderbook is currently at a record high of RM5.4b, implying a superior cover of 13.2x on FY16 construction revenue.

Steady metering contribution. PBT for metering remained steady in 1H as higher revenue 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'

GKent is a key rail play with exposure to the LRT extension, LRT3 and MRT2. It also boasts solid financials with three-year earnings compound annual growth rate of 26%, above industry ROE of 15.4% and net cash position of RM0.64/share.

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.