

George Kent (BUY ↔; EPS ↑)

INDUSTRY: OVERWEIGHT

EARNINGS EVALUATION

6 December 2016

Price Target: RM3.77 (↔)

Share price: RM2.80

An explosive quarter
Results

- GKent reported 3QFY17 results with revenue of RM122.1m (-26% QoQ, +26% YoY) and core earnings of RM23.7m (+27% QoQ, 3QFY16: RM0.4m). The significant YoY earnings increase for the quarter was due to a low base witnessed last year due to cost of variation orders (VOs) incurred (but this was subsequently recognised in 4QFY16).
- Cumulative 9M core earnings (ex. forex) totalled RM58.2m, surging almost 3-folds YoY. This strong growth was attributed to (i) 51% revenue increase, (ii) PBT margin expansion from 10% to 18.3% and (iii) lower base last year due to a weak 3Q as earlier elaborated.

Deviation

- 9M earnings made up 94% of our full year forecast which is above our expectation. The surprise results were due to (i) stronger-than-expected engineering margins given continued VO works for the LRT extension and (ii) higher-than-projected JV contribution associated with LRT3 PDP.

Dividends

- A 2nd interim dividend of 2 sen was declared. Coupled with the 1st interim dividend (paid in Nov), this brings cumulative FY17 dividends to 5 sen (FY16: 3.5 sen).

Highlights

- **Engineering continues to deliver.** The engineering division saw 9M revenue grew +61% YoY while PBT margins expanded from 13.5% to 19%. The latter factor was likely due to the balance of works execution for the Ampang LRT extension along with the continued recognition of VOs.
- **Orderbook remains sizable.** With YTD job wins at RM771m, GKent's orderbook stands at RM5.9bn. This translates to a superior cover ratio of 14.4x on FY16 construction revenue, the highest in our sector coverage.
- **Metering sustains despite forex hit.** While the metering division saw 9M revenue grow by +26% YoY, PBT increased by a smaller magnitude of +6% as margins contracted from 24.3% to 20.6%. This was largely due to realised forex loss this year as opposed to gains in the previous year.

Risks

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

Forecasts

- In view of the strong results, we raise FY17 by 14% after incorporating higher engineering margins. FY18 earnings are increased by a smaller magnitude of 2% in view of potential margin normalisation next year (FY19 unchanged).

Rating
Maintain BUY, TP: RM3.77

- 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 28%, above industry ROE of 20.9% and net cash position of RM0.58/share (21% of market cap).

Valuation

- While FY18 earnings has been raised, our SOP based TP is unchanged at RM3.77 given the slightly lower net cash balance. Our TP implies FY17-18 ex. cash P/E of 16.8x and 15x respectively.

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KLCI	1625.0
Expected share price return	34.6%
Expected dividend return	3.4%
Expected total return	38.0%

Share price

Information

Bloomberg Ticker	GKEN MK
Bursa Code	3204
Issued Shares (m)	376
Market cap (RM m)	1,051
3-mth avg. volume ('000)	2,446
SC Shariah-compliant	No

Price Performance

	1M	3M	12M
Absolute	4.5	29.2	118.8
Relative	6.0	34.3	124.5

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	FY17E	FY18F	FY19F
Revenue		536	605	556	502
EBITDA		65	98	73	64
EBIT		61	94	69	60
Profit Before Tax		61	99	100	101
Core PATAMI		40	71	80	84
vs Consensus (%)		-	-	-	-
Core EPS (sen)		10.7	18.9	21.2	22.3
P/E (x)		26.2	14.8	13.2	12.6
P/E ex cash (x)		20.8	11.7	10.4	9.9
Net DPS (sen)		5.6	9.4	10.6	11.1
Net DY (%)		2.0	3.4	3.8	4.0
BV per share		0.86	0.95	1.06	1.17
P/B (x)		3.3	2.9	2.6	2.4
ROE (%)		13.2	20.9	21.1	20.0
Net Gearing (%)		CASH	CASH	CASH	CASH

HLIB

Figure #1 Quarterly results comparison

FYE Jan (RM m)	3QFY16	2QFY17	3QFY17	QoQ (%)	YoY (%)	Comments
Revenue	96.9	164.8	122.1	-25.9%	26.0%	QoQ: Lower due to quarterly volatility on engineering works booked. YoY: Higher as more LRT ext balance of works done.
EBIT	5.4	23.1	27.2	17.4%	405.2%	
Finance cost	(0.9)	(0.7)	(0.7)	12.8%	-16.4%	
Associates & JVs	0.5	2.1	3.1	48.4%	520.1%	LRT3 PDP contributes but mainly on reimbursables.
PBT	5.0	24.6	29.6	20.2%	491.8%	
PAT	0.4	18.7	23.7	26.7%	<i>n.m.</i>	
PATMI - core	0.4	18.7	23.7	26.7%	<i>n.m.</i>	Strong YoY surge due to low base effect.
PATMI - reported	12.1	20.5	24.9	21.5%	106.4%	RM12m forex gains last year.
EPS - core	0.1	5.0	6.3			
EBIT margin (%)	5.5%	14.0%	22.2%			Margin expansion from VOs booked for LRT ext.
PBT margin (%)	5.2%	14.9%	24.2%			
Company						

Figure #2 Quarterly results comparison

FYE Jan (RM m)	9MFY16	9MFY17	YoY (%)	Comments
Revenue	270.6	409.8	51.4%	Mainly on execution of LRT ext.
EBIT	27.9	71.1	155.2%	
Finance cost	(2.1)	(1.9)	-7.7%	
Associates & JVs	1.4	6.0	326.7%	LRT3 PDP role contributes.
PBT	27.2	75.2	176.4%	
PAT	14.7	58.2	296.0%	
PATMI - core	14.7	58.2	296.0%	9M earnings made up 94% of full year forecast.
PATMI - reported	30.4	60.4	98.7%	Includes forex gains.
EPS - core	3.9	15.5		
EBIT margin	10.3%	17.4%		Margin expansion from VOs booked for LRT ext.
PBT margin	10.0%	18.3%		
Company				

Figure #3 SOP based valuation for GKent

SOP Component	Amount (RM m)	Multiple (x)	Valuation (RM m)	Per Share
FY18 core earnings	80	15	1,195	3.18
Net cash	219	1	219	0.58
SOP Value			1,414	3.77

HLIB estimates

Financial Projections for George Kent

Balance Sheet

FYE Jan (RM m)	FY15	FY16	FY17F	FY18F	FY19F
Cash	164	242	237	287	330
Receivables	246	241	282	259	234
Inventories	42	48	63	58	52
PPE	121	121	119	117	115
Others	33	31	31	31	31
Assets	606	683	731	752	763
Debits	58	27	37	35	32
Payables	256	326	329	312	283
Others	5	8	8	8	8
Liabilities	319	361	374	355	324
Shareholder's equity	287	322	357	397	439

Cash Flow Statement

FYE Jan (RM m)	FY15	FY16	FY17F	FY18F	FY19F
Profit before taxation	41	61	99	100	101
Share of JV and associates	(2)	(2)	(8)	(33)	(43)
Depreciation & amortisation	4	4	4	4	4
Changes in working capital	(92)	69	(53)	11	2
Taxation	(12)	(21)	(28)	(20)	(17)
Others	(4)	16	(6)	29	41
CFO	(67)	127	8	90	88
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)	(35)	(40)
Others	(88)	13	-	-	-
CFF	4	(33)	(11)	(38)	(42)
Net cash flow	(64)	92	(5)	50	43
Forex	(1)	2	-	-	-
Others	18	(16)	-	-	-
Beginning cash	211	164	242	237	287
Ending cash	164	242	237	287	330

Income Statement

FYE Jan (RM m)	FY15	FY16	FY17F	FY18F	FY19F
Revenue	353	536	605	556	502
EBITDA	44	65	98	73	64
EBIT	41	61	94	69	60
Finance cost	(2)	(3)	(2)	(2)	(2)
Associates & JV	2	2	8	33	43
Profit before tax	41	61	99	100	101
Tax	(12)	(21)	(28)	(20)	(17)
PATMI (core)	28	40	71	80	84
Exceptionals	(0)	10	-	-	-
PATMI (reported)	28	50	71	80	84

Valuation & Ratios

FYE Jan (RM m)	FY15	FY16	FY17F	FY18F	FY19F
Core EPS (sen)	7.5	10.7	18.9	21.2	22.3
P/E (x)	37.2	26.2	14.8	13.2	12.6
EV/EBITDA (x)	18.8	12.8	8.5	11.4	13.0
DPS (sen)	4.2	5.6	9.4	10.6	11.1
Dividend yield	1.5%	2.0%	3.4%	3.8%	4.0%
BVPS (RM)	0.76	0.86	0.95	1.06	1.17
P/B (x)	3.7	3.3	2.9	2.6	2.4
EBITDA margin	12.5%	12.1%	16.1%	13.1%	12.7%
EBIT margin	11.5%	11.4%	15.5%	12.4%	11.9%
PBT margin	11.5%	11.3%	16.4%	17.9%	20.1%
Net margin	8.0%	7.5%	11.7%	14.3%	16.7%
ROE	10.6%	13.2%	20.9%	21.1%	20.0%
ROA	5.1%	6.2%	10.0%	10.7%	11.0%
Net gearing	CASH	CASH	CASH	CASH	CASH

Assumptions

FYE Jan (RM m)	FY15	FY16	FY17F	FY18F	FY19F
Contracts secured	57	4,500	1,121	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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Industry rating definitions

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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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