

Pestech International Bhd

4Q18 Results Disappoint

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4Q18 results were a big let-down which led to its first FY earnings decline, in FY18. However, we remain upbeat on PESTECH for its exciting earnings growth story and believe this quarter's earnings weakness should only be a temporary blip. We cut FY19 earnings estimates by 13% on lower EPC profit margin by 1%, but it remains OUTPERFORM with a revised TP of RM1.95/SoP share.

FY18 missed expectation. A dismal 4Q18 set of results with core loss of RM0.6m brought FY18 core profit to RM62.2m which came 32% below our estimate of RM92.1m, largely due to weaker-than-expected EPC project margin as those projects were in the beginning stages as well as the adjustment on DPL contribution, which had since started concession fees in January. There was no dividend declared for the year which was disappointing as well as we had projected for 3.6 sen NDPS in FY18.

First quarterly losses on DPL adjustment. 4Q18 plunged into core loss of RM0.6m after adjusting for RM7.8m unrealised forex loss and RM32.5m gain on hedging instrument. This was against core profit of RM15.0m in 3Q18. The losses were due to: (i) weaker top-line as the two main Alex Corp's projects were still in foundation stages with minimal work claims, (ii) MRT2's rail electrification was in design stage, which also entailed minimal work claims, and (iii) adjustment of overstated recognition of DPL in 3Q18 after it started receiving concession fees in January. Based on the MI reported in 2H18, the earnings contribution from DPL could be RM5.5m per quarter from c.RM16m previously during the construction period. All these explained the plunge in 4Q18 revenue and the lower bottom-line.

First earnings decline in a financial year. While revenue rose 4% YoY in 4Q18 and surged 66% in FY18, 4Q18 slipped into the red from core profit of RM45.4m and FY18 core profit contracted 30% to RM62.2m from RM89.1m previously. The expansion in top-line was largely due to the inclusion of MRT2 project as well as the start of KVDT project. Furthermore, to note that back then, the Alex Corp job slowed down in 1Q17 pending the upgrade of the 500kV transmission line which was subsequently awarded in early February last year or 3Q17 in PESTECH's financial period. On the other hand, the bottom-line was cramped by the abovementioned DPL adjustment in 2H18 while DPL for the previous financial periods were in construction stages, which recognised higher construction profits.

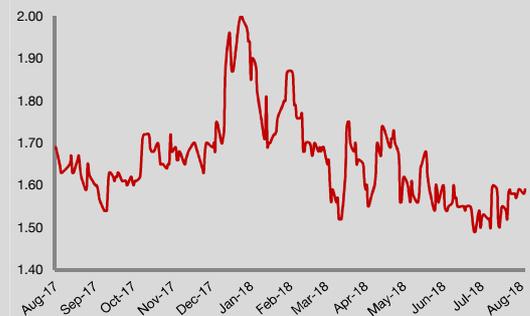
Contracts in hand offer 2-3 years earnings visibility. With the cancellation of East Coast Rail Link (ECRL), the KL-Singapore High-Speed Rail and Gemas-JB double track projects are the only two major electrification projects locally for PESTECH to participate, of which we think the contract sums are fairly huge should it be able to secure them. On the other hand, as the government is looking to upgrade the existing East Coast KTM line to replace the canceled ECRL project, PESTECH should stand a good chance of securing the project based on its track record on the West Coast KTM line. Meanwhile, its current order-book is estimated at RM1.57b which should keep it busy for at least the next 2-3 years.

Maintain OUTPERFORM. We reduce our FY19 earnings estimate by 13% on lower EPC operating margin to 14% from 15% previously while introducing our new FY20 forecast with earnings set to grow by 14%. At the same time, we expect no NDPS for FY19-FY20 as it preserves cash for business expansion. Post-earnings cut, new target price is reduced to RM1.95 from RM2.15 based on SoP valuation. Although 4Q18 earnings were disappointing, we believe it should be back on track from FY19 onwards. Thus, it remains an OUTPERFORM. Risks to our call include failure to replenish order-book and cost over-runs.

OUTPERFORM ↔

Price: RM1.59
Target Price: RM1.95 ↓

Share Price Performance



KLCI	1,826.90
YTD KLCI chg	1.7%
YTD stock price chg	-9.1%

Stock Information

Shariah Compliant	Yes
Bloomberg Ticker	PEST MK
Market Cap (RM m)	1,215.2
Shares Outstanding	764.3
52-week range (H)	2.07
52-week range (L)	1.45
3-mth avg daily vol:	371,887
Free Float	43%
Beta	0.8

Major Shareholders

Lim Ah Hock	33.1%
Lim Pay Chuan	20.2%
Employees Provident Fund	3.3%

Summary Earnings Table

FYE Jun (RM m)	2018A	2019E	2020E
Turnover	843.1	1,000.0	1,100.0
EBIT	119.8	181.0	195.0
PBT	92.6	146.0	162.7
Net Profit (NP)	60.6	90.8	104.2
Core Net Profit	62.2	90.8	104.2
Consensus (NP)		N.A.	N.A.
Earnings Revision (%)		-13.1%	New
Core EPS (sen)	8.1	11.9	13.6
Core EPS growth (%)	-30.2	46.0	14.7
NDPS (sen)	0.0	0.0	0.0
BV/Share (RM)	0.27	0.32	0.38
NTA/Share (RM)	0.27	0.32	0.38
Core PER	19.0	13.4	11.7
PBV (x)	0.00	4.92	4.14
Price/NTA (x)	5.75	4.92	4.14
Gearing (%)	1.35	1.22	0.99
Net Yield (%)	0.0	0.0	0.0

29 August 2018

Income Statement								
Y/E : Jun (RM m)	4Q FY18	3Q FY18	Q-o-Q Chg	4Q FY17	Y-o-Y Chg	12M FY18	12M FY17	Y-o-Y Chg
Turnover	119.3	260.9	-54%	114.6	4%	843.1	508.2	66%
EBITDA	23.0	28.4	-19%	68.0	-66%	124.7	152.6	-18%
Depreciation	(1.2)	(1.2)	2%	(1.4)	-9%	(4.9)	(5.0)	-2%
EBIT	21.7	27.2	-20%	66.6	-67%	119.8	147.6	-19%
Interest expense	(4.1)	(9.5)	-57%	(4.2)	-2%	(27.3)	(11.6)	134%
Associates	0.0	0.0	0%	0.0	0%	0.0	0.0	0%
Pretax profit	17.6	17.7	0%	62.4	-72%	92.6	136.0	-32%
Taxation	(1.4)	(2.2)	-39%	(11.6)	-88%	(14.2)	(15.7)	-10%
Profit after tax	16.3	15.4	5%	50.9	-68%	78.4	120.2	-35%
Minority interest	1.8	(6.2)	-129%	(9.2)	-120%	(17.8)	(29.3)	-39%
Net profit	18.1	9.2	97%	41.7	-57%	60.6	90.9	-33%
Core net profit	(0.6)	15.0	-104%	45.4	-101%	62.2	89.1	-30%
EPS (sen)	2.4	1.2	97%	5.5	-57%	2.4	1.2	97%
NDPS (sen)	0.0	0.0	0%	0.0	0%	0.0	0.0	0%
NTA/share (RM)	0.22	0.20	9%	0.19	15%	0.22	0.19	15%
EBITDA margin	19%	11%		59%		15%	30%	
EBIT margin	18%	10%		58%		14%	29%	
Pretax margin	15%	7%		54%		11%	27%	
Effective tax rate	8%	13%		19%		15%	12%	

Source: Company

Valuation - New				
	RM m	RM/Share	%	Valuation Basic
Project and Product Businesses	1,378.9	1.81	93%	CY19 15x PER, 3-year mean
Cambodia BOT	107.1	0.14	7%	FCFF @ 7.2% discount rate
	1,486.0	1.95	100%	
No of shares	764.3			
SoP per share	RM1.95			

Source: Kenanga Research

Valuation - Old				
	RM m	RM/Share	%	Valuation Basic
Project and Product Businesses	1,537.2	2.01	93%	CY19 15x PER, 3-year mean
Cambodia BOT	107.1	0.14	7%	FCFF @ 7.2% discount rate
	1,644.3	2.15	100%	
No of shares	764.3			
SoP per share	RM2.15			

Source: Kenanga Research

Peer Comparison

Name	Last Price	Market	Shariah	Current	Revenue Growth		Core Earnings Growth		PER (x) - Core Earnings			PBV (x)		ROE (%)	Net Div.Yld. (%)	Target	Rating
	(RM)	Cap (RM'm)	Compliant	FYE	1-Yr. Fwd.	2-Yr. Fwd.	1-Yr. Fwd.	2-Yr. Fwd.	Hist.	1-Yr. Fwd.	2-Yr. Fwd.	Hist.	1-Yr. Fwd.	1-Yr. Fwd.	1-Yr. Fwd.	Price (RM)	
MALAKOFF CORP BHD	0.965	4,743.4	Y	12/2018	-2.4%	-5.3%	-34.7%	-0.1%	15.6	23.9	23.9	0.8	0.8	3.3%	4.1%	1.20	OP
PESTECH INTERNATIONAL BHD	1.59	1,215.2	Y	06/2019	18.6%	10.0%	46.0%	14.8%	19.5	13.4	11.7	2.6	2.2	18.0%	0.0%	1.95	OP
TENAGA NASIONAL BHD	15.72	89,261.0	Y	12/2018	3.7%	5.8%	10.9%	7.9%	14.6	13.2	12.2	1.5	1.4	11.3%	3.0%	17.90	OP
YTL POWER INTERNATIONAL BHD	1.14	8,751.8	N	06/2018	6.9%	2.4%	-10.4%	9.3%	12.2	14.7	13.4	0.6	0.7	4.8%	4.4%	1.10	OP
Simple Average					6.7%	3.2%	2.9%	8.0%	15.5	16.3	15.3	1.4	1.3	9.4%	2.9%		

Source: Bloomberg, Kenanga Research

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Stock Ratings are defined as follows:**Stock Recommendations**

OUTPERFORM : A particular stock's Expected Total Return is MORE than 10%
MARKET PERFORM : A particular stock's Expected Total Return is WITHIN the range of -5% to 10%
UNDERPERFORM : A particular stock's Expected Total Return is LESS than -5%

Sector Recommendations***

OVERWEIGHT : A particular sector's Expected Total Return is MORE than 10%
NEUTRAL : A particular sector's Expected Total Return is WITHIN the range of -5% to 10%
UNDERWEIGHT : A particular sector's Expected Total Return is LESS than -5%

*****Sector recommendations are defined based on market capitalisation weighted average expected total return for stocks under our coverage.**

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