

28 August 2019

Pestech International Bhd

Strong 4Q19 But Not Good Enough

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Although 4Q19 earnings were up strongly by 58%, it was still not good enough for us as the FY19 results missed our forecast by 9% given the lower-than-expected revenue recognition. Nonetheless, the sizeable order-book of RM1.6b will sustain its earnings growth story for the next two years while the domestic contract flows such as LRT3 and ECRL should keep PESTECH in investors' radar. We keep our OP call but with revised TP of RM1.75.

FY19 missed expectations. 4Q19 results fell short of expectations, although core profit jumped 58% QoQ to RM33.5m, which brought FY19 core profit to RM72.4m, but missed our forecast by 9% due to lower revenue recognition of RM810m vs. our assumption of RM900m on delayed job progress claims for MRT2 where their portion was still at the civil-work stage. However, their Cambodia projects were well on track before the raining season arrived. No dividend was declared for FY19, as expected, as it keeps cash for expansion.

Strong 4Q19 results... 4Q19 core profit jumped 58% QoQ to RM33.5m on the back of 53% hike in revenue over the quarter. The improved results were driven by all projects both local as well as in Cambodia, especially the latter as job progress was at full swing before the raining season arrived in the 2H of the calendar year. So far, the first Alex Corp's project has completed 84% of the job while second project has reached 54% whereas Oddor Meanchey has completed 92% before being due for delivery in Nov this year. Back home, job completion for MRT2 was at 35% while KVDT was at 45% completion. Overall, core profit margin in 4Q19 improved to 11.7% from 9.5% on the back of projects moving to more advanced stage, which fetched higher margins.

...and better YoY results. Compared to the loss-making 4Q18 which was due to early stages for domestic projects such as MRT2 and KVDT coupled with an adjustment of overstated recognition of DPL in 3Q18 after it started concession fees in Jan 2018, 4Q19 results were helped by the abovementioned work progress. YTD, FY19 core profit grew 16% to RM72.4m although revenue slid 4% due to a loss-making 4Q18 mentioned above that dragged the overall FY18 earnings, higher job claims for both local rail electrification project and Cambodian projects in FY19 helped to push up earnings.

Moving into seasonally low season again in 1H20... After completing the traditionally strong period of 2H in FY19, PESTECH is moving into a low season again, especially as work progress slow down in Cambodia as the wet season arrived. However, the impact could not be that apparent as the locally MRT2 and KVDT works are advancing to higher stages, which are likely to mitigate the shortfall. With its RM1.6b order-book, this should keep them busy for the next two years. In addition, we expect contract flow to start kicking in with the revival of KVDT2 and ECRL and PESTECH should stand a good chance of securing these projects as it is the only local firm with rail electrification expertise.

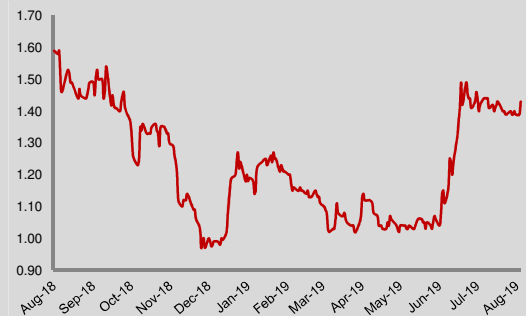
Still have legs; OUTPERFORM retained. Post earnings release, we lowered our FY20 revenue assumption to RM950m as we believe our previous assumption of RM1.1b was too bullish on revenue recognition. Thus, our FY19 estimates are reduced by 13% while we introduce our FY21 forecasts in which we expect earnings to grow 14% on the back of RM1.05b revenue assumption. Although its share price has risen strongly by 44% YTD, we believe the market is still not appreciating the growth potential of this niche utility infrastructure play. As such, we maintain our OUTPERFORM call at a lower SoP-driven target price of RM1.75 from RM2.00 solely on earnings cut.

Risks to our call include: (i) failure to replenish order-book, and (ii) cost overruns.

OUTPERFORM ↔

Price: **RM1.43**
Target Price: **RM1.75** ↓

Share Price Performance



KLCI	1,590.84
YTD KLCI chg	-5.9%
YTD stock price chg	44.4%

Stock Information

Shariah Compliant	Yes
Bloomberg Ticker	PEST MK
Market Cap (RM m)	1,092.9
Shares Outstanding	764.3
52-week range (H)	1.60
52-week range (L)	0.95
3-mth avg daily vol:	1,550,216
Free Float	42%
Beta	1.2

Major Shareholders

Lim Ah Hock	33.3%
Lim Pay Chuan	19.5%
Prudential Plc	5.2%

Summary Earnings Table

FYE Jun (RM m)	2019A	2020E	2021E
Turnover	810.0	950.0	1,050.0
EBIT	150.4	166.5	179.5
PBT	97.6	116.5	131.1
Net Profit (NP)	80.2	91.1	103.4
Core Net Profit	72.4	91.1	103.4
Consensus (NP)		N.A.	N.A.
Earnings Revision (%)		-12.6	New
Core EPS (sen)	9.5	11.9	13.5
Core EPS growth (%)	16.4	25.7	13.6
NDPS (sen)	0.0	0.0	0.0
BV/Share (RM)	0.28	0.33	0.39
NTA/Share (RM)	0.28	0.33	0.39
Core PER	11.7	12.0	10.6
PBV (x)	3.97	4.28	3.62
Price/NTA (x)	3.51	4.28	3.62
Gearing (%)	1.82	1.38	1.06
Net Yield (%)	0.0	0.0	0.0

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Income Statement

Y/E : Jun (RM m)	4Q	3Q	Q-o-Q	4Q	Y-o-Y	12M	12M	Y-o-Y
	FY19	FY19	Chg	FY18	Chg	FY19	FY18	Chg
Turnover	285.3	222.1	28%	119.3	139%	810.0	843.1	-4%
EBITDA	59.5	39.5	50%	23.0	159%	157.6	124.7	26%
Depreciation	(2.2)	(2.2)	1%	(1.2)	80%	(7.2)	(4.9)	46%
EBIT	57.2	37.3	53%	21.7	164%	150.4	119.8	26%
Interest expense	(15.7)	(13.6)	15%	(4.1)	283%	(52.8)	(27.3)	94%
Associates	0.0	0.0	0%	0.0	0%	0.0	0.0	0%
Pretax profit	41.5	23.7	75%	17.6	136%	97.6	92.6	5%
Taxation	(5.2)	(1.2)	342%	(1.4)	286%	(9.7)	(14.2)	-32%
Profit after tax	36.3	22.5	61%	16.3	123%	87.9	78.4	12%
Minority interest	(2.1)	(0.9)	129%	1.8	-214%	(7.7)	(17.8)	-57%
Net profit	34.2	21.6	58%	18.1	89%	80.2	60.6	32%
Core net profit	33.5	21.2	58%	(0.6)	-5311%	72.4	62.2	16%
EPS (sen)	4.5	2.8	58%	2.4	89%	4.5	2.8	58%
NDPS (sen)	0.0	0.0	0%	0.0	0%	0.0	0.0	0%
NTA/share (RM)	0.23	0.21	8%	0.22	5%	0.23	0.22	5%
EBITDA margin	21%	18%		19%		19%	15%	
EBIT margin	20%	17%		18%		19%	14%	
Pretax margin	15%	11%		15%		12%	11%	
Effective tax rate	13%	5%		8%		10%	15%	

Source: Company

Valuation - New

	RM m	RM/Share	%	Valuation Basis
Project and Product Businesses	1,206.1	1.58	91%	FY20 15.0x PER, 3-year mean FCFF @ 7.2% discount rate
Cambodia BOT	112.5	0.15	9%	
	1,318.6	1.73	100%	
No of shares	764.3			
SoP per share	RM1.75			round to the nearest RM0.05

Source: Kenanga Research

Valuation - Old

	RM m	RM/Share	%	Valuation Basis
Project and Product Businesses	1,410.7	1.85	93%	FY20 14.5x PER, 3-year mean FCFF @ 7.2% discount rate
Cambodia BOT	112.5	0.15	7%	
	1,523.1	2.00	100%	
No of shares	764.3			
SoP per share	RM2.00			round to the nearest RM0.05

Source: Kenanga Research

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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)	
GAS MALAYSIA BHD	2.85	3,659.4	Y	12/2019	2.9%	7.7%	8.2%	2.2%	21.5	19.9	19.5	3.6	3.3	17.3%	4.5%	3.00	MP
MALAKOFF CORP BHD	0.870	4,251.7	Y	12/2019	-0.3%	-0.1%	10.5%	4.5%	19.8	17.9	17.2	0.8	0.8	4.3%	4.5%	1.00	OP
PESTECH INTERNATIONAL BHD	1.43	1,092.9	Y	06/2020	17.3%	10.5%	25.7%	13.6%	11.7	12.0	10.6	4.0	4.3	18.3%	0.0%	1.75	OP
PETRONAS GAS BHD	15.36	30,393.3	Y	12/2019	4.8%	-1.8%	5.7%	-14.7%	16.6	15.7	18.5	2.3	2.2	14.5%	4.4%	15.75	MP
TENAGA NASIONAL BHD	13.60	77,341.7	Y	12/2019	3.2%	1.8%	2.6%	2.0%	14.2	13.8	13.5	1.3	1.3	9.3%	3.6%	13.40	MP
YTL POWER INTERNATIONAL BHD	0.695	5,334.3	N	06/2019	3.4%	2.6%	-1.6%	8.0%	8.0	8.1	7.5	0.4	0.4	4.6%	7.2%	0.880	MP
Simple Average					5.2%	3.5%	8.5%	2.6%	15.9	14.6	14.5	1.8	1.7	11.4%	4.0%		

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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