

Pestech International

A Strong Close To FY16

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FY16 results beat expectations substantially owing to a write-back of tax provision for DPL. Even without this, underlying numbers were still impressive led by top line growth and margin expansion, thanks to the DPL project. We remain positive on PESTECH and comfortable with our earnings forecasts on the back of current order book and tender book prospects. OUTPERFORM maintained for its explosive earnings growth story with a revised price target of RM2.00.

FY16 above. 4Q16 results came in above expectations with full-year FY16 core profit of RM66.1m beating house/street's estimates by 22%/18% largely due to lower-than-expected taxation after a write-back of tax provision in 4Q16 following the confirmation of Diamond Power (DPL) receiving a 9-year tax exempt status. As such, effective tax rate in FY16 was 6% as opposed to our assumption of 18%. There was no dividend declared in 4Q16, but we believe a final dividend would be announced at a later date.

Earnings helped by lower taxation. Sequentially, 4Q16 core net profit surged 178% to RM31.0m from RM11.2m in 3Q16 while revenue leapt 55% to RM190.7m from RM123.4m previously. The substantial jump in earnings was largely due to the said write-back of tax provision for DPL. In addition, the improved earnings were also attributed to higher revenue where work progress for DPL and Samajaya were higher. Work progress for DPL was 53% in 4Q16 from 36% in 3Q16 while Samajaya's completed job done hit 64% from 55% previously. However, work progress for Alex Corp was slow at 65% from 63% in 3Q16 as PESTECH slowed down the project pending a potential job upgrade request by the client.

DPL a booster too. A comparison to the corresponding period last year, 4Q16 core earnings tripled from RM10.1m while FY16 core profit doubled from RM32.6m last year. Besides the tax provision write-down mentioned above, the remarkable results were also attributed to the start of DPL project, which was reflected in its top line, which soared 114% in 4Q16 while FY16 revenue hike 71% to RM508.7m from RM297.5m previously. The DPL project contributed c.RM228m revenue to the group in FY16. Based on RM26.7m MI in FY16 which largely accounted for DPL, the tax-exempt net margin for DPL was c.29%. Even applying a 20% Cambodian corporate tax, net margin is still 23%, which is quite impressive as opposed to PESTECH's target margin of 9%-11% for new project tenders.

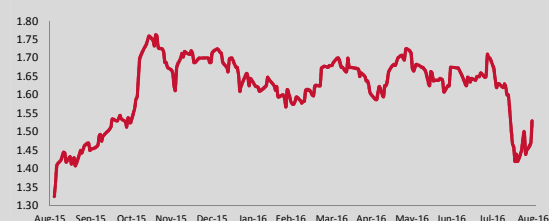
Outlook remains upbeat. With DPL expected to be ready by end-2017, PESTECH is expected to enjoy low taxation rate at least in FY17 for the EPC earnings coupled with higher profit margin. From its current tender book of RM1.45b, it aims to secure at least three projects by this year-end; one local rail electrification project and two Cambodian projects of which it stands a high chance of securing. This will help to replenish the declining order book of RM840m as of end-Jun from RM1.11b three months ago. In view of strong DPL EPC's margin and lower taxation, we upgraded our FY17 estimates by 13% while FY18 forecasts revised upward slightly by 1%, mainly on cash flow adjustment.

Maintain OUTPERFORM. We believe the recent weakness in its share prices, which is in line with the overall weak sentiment for small to mid-cap stocks, presents a great accumulation opportunity for exciting stock with explosive earnings growth story. After another record year in FY16, it will not stop here and expects to escalate to new heights in FY17 with its current order book in hand. We continue to rate the stock as OUTPERFORM with higher price target of RM2.00/SoP share post-earnings revision from RM1.88/SoP share previously. Risks to our call include failure to replenish order book and cost over-runs.

OUTPERFORM ↔

Price: **RM1.53**
Target Price: **RM2.00** ↑

Share Price Performance



KLCI	1678.06
YTD KLCI chg	-0.9%
YTD stock price chg	-10.8%

Stock Information

Shariah Compliant	Yes
Bloomberg Ticker	PEST MK
Market Cap (RM m)	1,142.0
Issued shares	746.4
52-week range (H)	1.77
52-week range (L)	1.30
3-mth avg daily vol:	1,009,954
Free Float	43%
Beta	0.9

Major Shareholders

AH HOCK LIM	33.3%
PAY CHUAN LIM	20.3%
NORGES BANK	3.8%

Summary Earnings Table

FYE Jun (RM m)	2016A	2017E	2018E
Turnover	508.7	600.0	695.0
EBIT	111.7	137.4	146.6
PBT	105.8	115.1	116.9
Net Profit (NP)	72.8	76.4	89.7
Core Net Profit	66.1	76.4	89.7
Consensus (NP)		68.2	79.1
Earnings Revision (%)		+13.4	+0.8
Core EPS (sen)	35.4	10.2	12.0
Core EPS growth (%)	102.9	15.6	17.4
NDPS (sen)	3.0	3.1	3.6
BV/Share (RM)	1.66	0.48	0.56
NTA/Share (RM)	1.66	0.48	0.56
Core PER	18.9	14.9	12.7
PBV (x)	4.04	3.18	2.71
Price/NTA (x)	4.04	3.18	2.71
Gearing (%)	0.92	0.85	0.41
Net Yield (%)	0.4	2.0	2.4

Income Statement

	4Q	3Q	Q-o-Q	6Q	Y-o-Y	12M	12M	Y-o-Y
Y/E : Jun (RM m)	FY16	FY16	Chg	FY15	Chg	FY16	FY15	Chg
Turnover	190.7	123.4	55%	88.9	114%	508.7	297.5	71%
EBITDA	45.4	24.2	88%	20.2	125%	116.1	54.3	114%
Depreciation	(1.1)	(1.1)	-3%	(1.1)	3%	(4.4)	(3.5)	25%
EBIT	44.3	23.1	92%	19.2	131%	111.7	50.7	120%
Interest expense	(6.9)	(2.4)	184%	(1.2)	482%	(12.6)	(4.7)	171%
Associates	0.0	0.0	0%	(0.1)	-100%	0.0	(0.5)	-100%
Exceptional items	(8.6)	1.4	-727%	14.3	-160%	6.8	14.2	-52%
Pretax profit	28.9	22.0	31%	32.2	-10%	105.8	59.7	77%
Taxation	5.7	(3.1)	-287%	(7.9)	-173%	(6.3)	(13.1)	-52%
Profit after tax	34.6	18.9	83%	24.3	42%	99.6	46.6	114%
Minority interest	(12.2)	(6.4)	89%	0.1	N/M	(26.7)	0.1	N/M
Net profit	22.5	12.5	79%	24.4	-8%	72.8	46.7	56%
Core net profit	31.0	11.2	178%	10.1	207%	66.1	32.6	103%
EPS (sen)	3.0	1.7	79%	3.3	-8%	3.0	1.7	79%
NDPS (sen)	0.0	0.0	0%	3.0	-100%	3.0	7.0	-57%
NTA/share (RM)	0.30	0.27	13%	0.32	-4%	0.30	0.32	-4%
EBITDA margin	24%	20%		23%		23%	18%	
EBIT margin	23%	19%		22%		22%	17%	
Pretax margin	15%	18%		36%		21%	20%	
Effective tax rate	-20%	14%		24%		6%	22%	

Source: Company

Valuation - New

	RM m	RM/Share	%	Valuation Basic
Project and Product Businesses	1,415.7	1.90	95%	CY17 16x PER, 3-year mean
Cambodia BOT	78.0	0.10	5%	FCFF @ 7.2% discount rate
	1,493.7	2.00	100%	
No of shares	746.4			
SoP per share	RM2.00			

Source: Kenanga Research

Valuation - Old

	RM m	RM/Share	%	Valuation Basic
Project and Product Businesses	1,325.1	1.78	94%	CY17 16.5x PER, 3-year mean
Cambodia BOT	78.0	0.10	6%	FCFF @ 7.2% discount rate
	1,403.2	1.88	100%	
No of shares	746.4			
SoP per share	RM1.88			

Source: Kenanga Research

Power Utility Comparisons

Company	Price (RM)	Market Cap (RM m)	PER(x)			Est. Div. Yld. (%)	His. ROE (%)	His. P/BV (x)	NP Growth (%)		Target Price (RM)	Rating
			CY15	CY16	CY17				CY16	CY17		
MALAKOF	1.65	8,250.0	18.2	17.5	15.8	4.0	7.6	1.4	3.8	10.8	1.79	MP
PESTECH	1.53	1,142.0	20.7	16.0	13.8	2.0	24.0	5.3	29.3	16.6	2.00	OP
TENAGA	14.74	83,186.8	13.3	12.2	12.1	2.5	12.9	1.7	9.2	0.5	17.50	OP
YTLPOWR	1.49	11,498.9	13.1	13.8	13.5	6.7	7.7	1.0	-4.9	1.8	1.54	MP
	Simple average		16.3	14.9	13.8							
	Weighted average		13.7	12.8	12.6							

Source: Kenanga Research

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

OUTPERFORM	: A particular stock's Expected Total Return is MORE than 10% (an approximation to the 5-year annualised Total Return of FBMKLCI of 10.2%).
MARKET PERFORM	: A particular stock's Expected Total Return is WITHIN the range of 3% to 10%.
UNDERPERFORM	: A particular stock's Expected Total Return is LESS than 3% (an approximation to the 12-month Fixed Deposit Rate of 3.15% as a proxy to Risk-Free Rate).

Sector Recommendations***

OVERWEIGHT	: A particular sector's Expected Total Return is MORE than 10% (an approximation to the 5-year annualised Total Return of FBMKLCI of 10.2%).
NEUTRAL	: A particular sector's Expected Total Return is WITHIN the range of 3% to 10%.
UNDERWEIGHT	: A particular sector's Expected Total Return is LESS than 3% (an approximation to the 12-month Fixed Deposit Rate of 3.15% as a proxy to Risk-Free Rate).

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

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