

15 November 2017

Property | Real Estate

Malaysian Resources Corp

Buy (Maintained)

Smooth Path At EDL

We expect the potential sale of EDL (or compensation from the Government), as well as the disposal of Bukit Jalil land to further improve MRCB's financial position after its recent equity call. In addition, given strong shareholder backing and a larger balance sheet, MRCB is well positioned to win more contracts, especially ahead of the next general elections. We maintain our BUY rating. Post rights issue, our new TP is MYR1.23 (from MYR1.90, 17% upside).

Compensation or disposal of EDL? While the market may not like the recent rights issue exercise, we believe the stock will gain investors' interest again. The abolishment of toll collections at Eastern Dispersal Link (EDL) should be viewed as a strong re-rating catalyst. This announcement during Budget 2018 was timely, just before Malaysian Resources Corp (MRCB) completed its rights issue exercise and the listing of warrants in early Nov.

The removal of toll collections would mean MRCB will either be compensated or ideally the Government could potentially buy back the highway. Either way would benefit MRCB in our view, as the interest expense and amortisation (total of MYR120-130m per year) have taken a toll on the company since 2014. Removing these expense items from the P&L would significantly enhance MRCB's earnings going forward.

Expect strong contract flow in the near term. We expect MRCB to bag some new construction contracts in the coming months, before the next general elections. We think the potential contracts are mainly in construction of infrastructure, and could be quite sizeable. Thus far, it has only secured MYR409m worth of new contracts this year, including the Damansara-Shah Alam Elevated Expressway (DASH) and TNB HQ Campus contracts.

Bukit Jalil land to be transferred by year-end. MRCB will likely receive its 76-acre land in Bukit Jalil by end-2017, after the successful completion of refurbishment works worth MYR1.34bn at the National Sports Complex. Soon after the land transfer, MRCB would be able to monetise the land by disposing it to the joint venture (JV) company that will be 80%-held by EPF. The injection of the land into the JV will enable MRCB to capture some disposal gain as the total consideration of MYR1.43bn implies a land price of MYR430psf vs MYR405psf based on the contract sum (MYR1.34bn).

Balance sheet strengthened post rights issue. MRCB's balance sheet has been significantly strengthened after it raised MYR1.7bn from the recent rights issue. While there will be some funding obligations to be met, such as the construction works in Bukit Jalil and some land acquisitions, the new balance sheet would allow MRCB to explore more construction and development opportunities, compared with 0.99x net gearing as at 1H17.

Maintain BUY. We maintain our BUY rating with a new TP of MYR1.23, based on 25% discount to RNAV. MRCB is an election play. We believe positive news flow on contracts as well as the announcement of the outcome on EDL would buoy investment sentiment on the stock in the coming months.

Target Price:	MYR1.23
Price:	MYR1.05
Market Cap:	USD1,099m
Bloomberg Ticker:	MRC MK

Share Data

Avg Daily Turnover (MYR/USD)	9.87m/2.35m
52-wk Price low/high (MYR)	0.88 - 1.55
Free Float (%)	40
Shares outstanding (m)	2,280
Estimated Return	17%

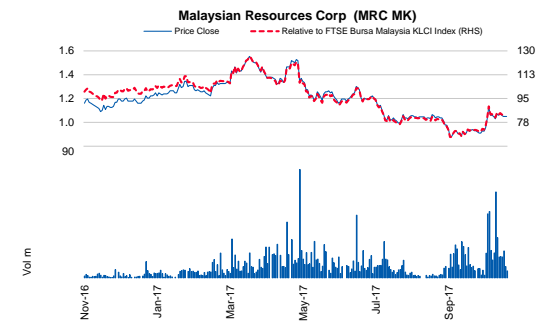
Shareholders (%)

Employees Provident Fund	34.7
Gapurna Sdn Bhd	16.6
Lembaga Tabung Haji	7.4

Share Performance (%)

	YTD	1m	3m	6m	12m
Absolute	(9.6)	12.3	5.5	(30.5)	(9.6)
Relative	(15.4)	13.3	7.4	(28.3)	(17.1)

Source: Bloomberg



Source: Bloomberg

Forecasts and Valuations	Dec-15	Dec-16	Dec-17F	Dec-18F	Dec-19F
Total turnover (MYRm)	1,697	2,408	2,483	2,605	3,012
Reported net profit (MYRm)	326	267	88	125	151
Recurring net profit (MYRm)	221	267	88	125	151
Recurring net profit growth (%)	436.1	20.8	(67.1)	42.6	20.5
Recurring EPS (MYR)	0.12	0.14	0.03	0.03	0.03
DPS (MYR)	0.03	0.03	0.01	0.01	0.01
Recurring P/E (x)	8.4	7.7	41.3	40.0	33.2
P/B (x)	0.83	0.77	0.95	0.94	0.92
P/CF (x)	2.1	4.5	na	7.2	19.8
Dividend Yield (%)	2.4	2.6	1.0	1.0	1.2
EV/EBITDA (x)	8.1	7.0	13.9	13.6	13.4
Return on average equity (%)	15.3	10.3	2.1	2.4	2.8
Net debt to equity (%)	123.8	73.1	29.1	19.9	31.4
Our vs consensus EPS (adjusted) (%)			(36.5)	(37.5)	(29.7)

Source: Company data, RHB

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Financial Exhibits

Financial model updated on : 2017-11-14.

Asia	Financial summary	Dec-15	Dec-16	Dec-17F	Dec-18F	Dec-19F
Malaysia	Recurring EPS (MYR)	0.12	0.14	0.03	0.03	0.03
Property	EPS (MYR)	0.18	0.14	0.03	0.03	0.03
Malaysian Resources Corp	DPS (MYR)	0.03	0.03	0.01	0.01	0.01
Bloomberg MRC MK	BVPS (MYR)	1.27	1.36	1.10	1.12	1.14
Buy	Weighted avg adjusted shares (m)	1,773	1,965	3,460	4,776	4,776
Valuation basis	Valuation metrics	Dec-15	Dec-16	Dec-17F	Dec-18F	Dec-19F
25% discount to RNAV	Recurring P/E (x)	8.4	7.7	41.3	40.0	33.2
Key drivers	P/E (x)	5.7	7.7	41.3	40.0	33.2
New property sales, asset disposals, new construction contracts	P/B (x)	0.83	0.77	0.95	0.94	0.92
Key risks	FCF Yield (%)	(81.1)	12.1	(44.3)	5.2	(11.0)
Weaker-than-expected market conditions	Dividend Yield (%)	2.4	2.6	1.0	1.0	1.2
	EV/EBITDA (x)	8.1	7.0	13.9	13.6	13.4
	EV/EBIT (x)	8.7	7.7	18.1	17.0	16.7
Company Profile	Income statement (MYRm)	Dec-15	Dec-16	Dec-17F	Dec-18F	Dec-19F
Malaysian Resources Corp Bhd (MRCB) is engaged in construction (niche strength in environmental projects), property development and investment and toll road operations. It is known for its transit-oriented developments, eg KL Sentral, Bukit Jalil City, Kwasa Damansara and Penang Sentral.	Total turnover	1,697	2,408	2,483	2,605	3,012
	Gross profit	160	236	92	216	225
	EBITDA	590	593	347	457	518
	Depreciation and amortisation	(43)	(57)	(80)	(91)	(102)
	Operating profit	547	536	267	366	416
	Net interest	(185)	(176)	(155)	(193)	(202)
	Income from associates & JVs	8	33	34	36	38
	Pre-tax profit	370	393	146	209	252
	Taxation	(6)	(74)	(37)	(52)	(63)
	Minority interests	(38)	(52)	(22)	(31)	(38)
	Recurring net profit	221	267	88	125	151
	Cash flow (MYRm)	Dec-15	Dec-16	Dec-17F	Dec-18F	Dec-19F
	Change in working capital	493	115	(976)	484	(1)
	Cash flow from operations	893	459	(820)	695	253
	Capex	(2,402)	(210)	(791)	(433)	(802)
	Cash flow from investing activities	(2,774)	(256)	(791)	(562)	(802)
	Proceeds from issue of shares	(7)	457	0	0	0
	Dividends paid	(45)	(44)	(59)	(19)	(28)
	Cash flow from financing activities	(355)	(37)	(59)	(19)	(28)
	Cash at beginning of period	661	522	722	2,569	3,238
	Net change in cash	(2,236)	165	(1,670)	114	(577)
	Ending balance cash	(1,576)	687	(948)	2,682	2,662
	Balance sheet (MYRm)	Dec-15	Dec-16	Dec-17F	Dec-18F	Dec-19F
	Total cash and equivalents	524	724	2,571	3,241	2,668
	Tangible fixed assets	3,748	3,900	4,611	4,953	5,652
	Intangible assets	317	253	253	253	253
	Total investments	5	34	34	34	34
	Total other assets	325	399	468	254	358
	Total assets	7,090	7,752	11,109	11,489	11,944
	Short-term debt	1,042	806	706	706	706
	Total long-term debt	2,345	2,131	3,431	3,631	3,731
	Other liabilities	146	161	201	201	201
	Total liabilities	4,777	4,727	5,721	5,989	6,311
	Shareholders' equity	2,260	2,926	5,266	5,348	5,442
	Minority interests	53	99	121	153	190
	Total equity	2,313	3,025	5,387	5,500	5,632
	Net debt	2,863	2,213	1,566	1,096	1,769
	Total liabilities & equity	7,090	7,752	11,109	11,489	11,944
	Key metrics	Dec-15	Dec-16	Dec-17F	Dec-18F	Dec-19F
	Revenue growth (%)	12.0	41.9	3.1	4.9	15.6
	Recurrent EPS growth (%)	415.6	9.0	(81.3)	3.3	20.5
	Gross margin (%)	9.4	9.8	3.7	8.3	7.5
	Operating EBITDA margin (%)	34.8	24.6	14.0	17.6	17.2
	Net profit margin (%)	19.2	11.1	3.5	4.8	5.0
	Dividend payout ratio (%)	13.5	22.1	22.1	22.1	22.1
	Capex/sales (%)	141.6	8.7	31.9	16.6	26.6
	Interest cover (x)	2.44	2.49	1.37	1.57	1.72

Source: Company data, RHB

No More Toll

Taking out EDL from MRCB

The abolishment of toll collections at EDL that was announced in Budget 2018 came as a surprise, as management has been guiding that it is in the midst of extending the concession period after the failed attempt to dispose of the highway at the end of last year. Recall that MRCB nearly sold EDL last year, as it received two indications of interest in Oct 2016.

One was from PLUS Malaysia Bhd, and another one was a client of ZJ Advisory Sdn Bhd. However, the market was disappointed when negotiations with the two parties fell through months later. As such, we believe that the market has not yet fully appreciated the impact of the announcement during the recent budget.

The removal of toll collections at EDL came on time, just before MRCB completed its fund raising exercise in early Nov. Without the toll collections, this would mean MRCB would either be compensated or in the best-case scenario, the Government would buy back the highway.

Either case should benefit MRCB, in our view. Note that, the total of interest expense and amortisation costs associated with EDL amounted to about MYR120-130m per year. In the case of compensation, we think the Government may reimburse according to the actual or new traffic volume forecasts, as logically both actual and forecast numbers should be higher than the current traffic volume after toll collections stop next year. Management will likely strive for an amount that is enough to cover all the expenses and costs.

Of course, an outright sale of EDL to the Government would be an ideal situation. We understand that the debt linked to the highway is about MYR1.2bn, in addition to some shareholders' advances. Similarly, if MRCB is able to sell the highway to the Government, we think that the management would also strive for a consideration that should be enough to offset all the outstanding debt and shareholders' advances.

In this case, although the surplus to RNAV (if any) is expected to be negligible, the company's balance sheet and P&L would improve significantly by just removing these expenses and debt from its books. Earnings would then truly reflect the company's core operations in construction and property development thereafter.

Expect more contracts ahead of general elections

We expect MRCB to have some new contract wins in the coming months, especially before the next general elections. Currently, the company has an outstanding orderbook of MYR2.25bn (excluding the project delivery partner (PDP) fee for Light Rail Transit Line 3 (LRT3) and all the Kwasa Land projects), including MYR409m worth of new contracts secured this year. While management guided that the current tenderbook is around MYR3bn, we think some potential contracts could be quite sizeable, mainly in construction of infrastructure projects, and some MRT stations.

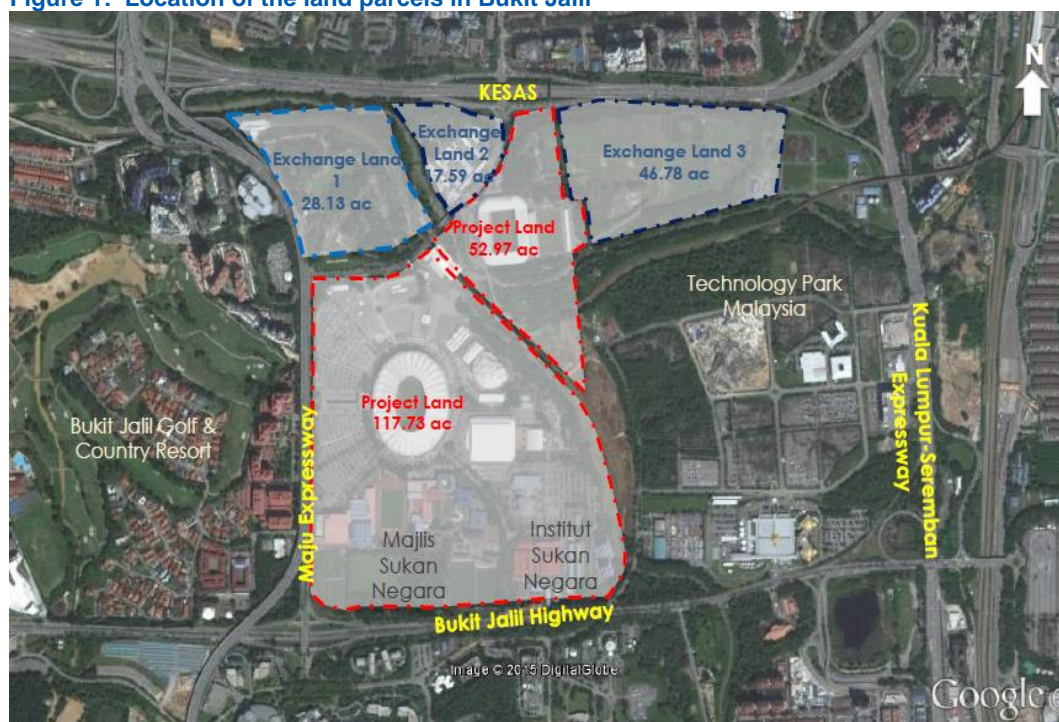
Meanwhile, there could be upside to MRCB's PDP fees for LRT3. We understand from industry sources that the total cost could be around MYR12-13bn, and will likely surpass management's initial guidance of MYR9bn, as MYR8.65bn worth of contracts have already been awarded for the project thus far. Assuming a final cost of MYR12bn, this would translate into a PDP fees of MYR360m over a 5-year period, about 33% higher compared to the initial estimate of MYR270m.

Receiving Bukit Jalil land soon

Apart from the recent rights issue, as well as the potential disposal of EDL, the impending transfer of the 76-acre land in Bukit Jalil is another effort to enhance the company's balance sheet. After the successful handover of the National Sports Complex before the SEA Games in Aug, MRCB is expected to receive the land parcels in 2H17.

According to management's plan, soon after the land transfer, MRCB will be able to monetise the land by injecting it into a JV company, in which EPF will have an 80% stake and MRCB 17% by effective interest (the balance 3% is held by Rasma Contractors Sdn Bhd). We think this is strategic, as MRCB will be able to undertake the property development project that is worth MYR20.7bn GDV, with EPF being the funding partner. At the same time, it could pocket some gain upon the land disposal. According to the announcement, the total consideration of MYR1.43bn (or MYR430 psf) for the land to be injected into the JV is 6% higher than the contract value of MYR1.34bn (or MYR405 psf) for the stadium refurbishment work.

Figure 1: Location of the land parcels in Bukit Jalil



Source: Company

Refreshing the balance sheet

In the past, MRCB's balance sheet was constrained by debt associated with EDL. Therefore, the ability to undertake more sizeable construction and property development projects was fairly limited. As a result, the company called for a 1-for-1 rights issue with one free rights warrants for every five rights shares subscribed in March. The exercise was completed in early Nov, and MRCB successfully raised about MYR1.7bn from the equity call.

Its balance sheet has been significantly strengthened, with an estimated net gearing of around 0.3x (from 0.99x as at 1H17) post rights issue. We believe its balance sheet would be even stronger if EDL can be sold to the Government. The proceeds, potentially worth about MYR1.1bn, from the injection of the Bukit Jalil land into the JV mentioned earlier would also come in handy. In our view, with a more solid balance sheet, MRCB would have greater financial capability to undertake more jobs going forward, such as the Bandar Malaysia high-speed rail terminal project.

Valuations

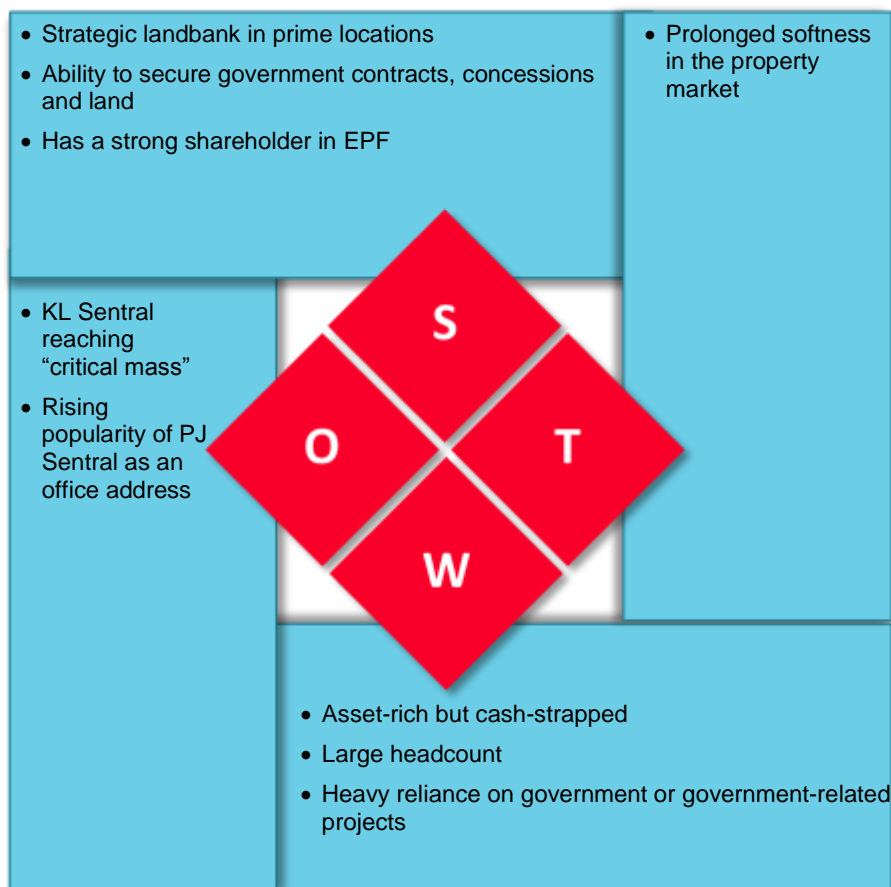
Our new TP is MYR1.23, based on 25% discount to RNAV. We maintain our BUY rating on the stock. MRCB is an election play, and we believe it is well positioned to win more contracts that could be announced before the general elections, given its strong shareholder backing, and larger balance sheet. Upcoming news flow on new contract wins and updates on EDL are expected to clear the stock overhang after the recent rights issue, in our opinion.

Figure 2: RNAV estimate

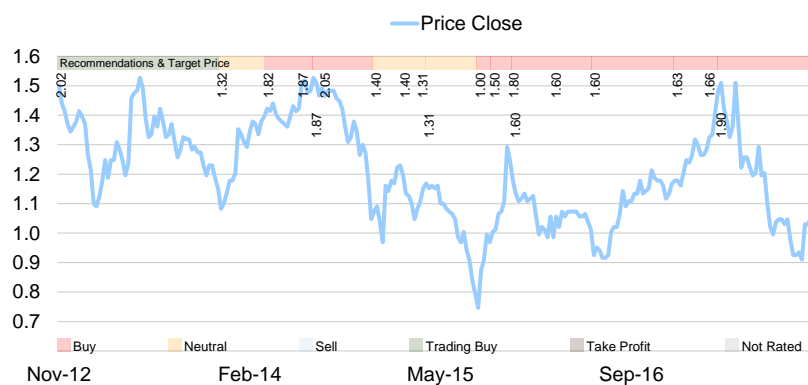
Ongoing Development	Acres	GDV (MYR m)	Stake	NPV @ 11%
Q Sentral Office Tower	1.9	1,228	66%	20.7
Seri Iskandar - Phase 2	245.0	321	70%	5.1
PJ Sentral - Celcom Tower	2.3	428	100%	21.2
9 Seputeh, Old Klang Road	8.0	795	100%	20.7
Penang Sentral Phase 1-2	6.0	590	100%	37.1
Penang Sentral Phase 3-7	16.7	2,100	70%	86.1
KL Sentral - Lot F	5.7	2,993	100%	259.7
Semarak City, Setapak	27.4	2,977	100%	126.4
Lot 349, KL Sentral (service apartments)	4.9	1,413	100%	104.2
Suria Subang	3.2	401	100%	21.1
Selbourne 2, Shah Alam	2.4	198	100%	10.9
PJ Sentral - Tower 1	-	700	100%	43.8
PJ Sentral - Tower 5	-	455	100%	28.5
Seri Iskandar - Phase 3	159.0	350	70%	11.7
Rahman Putra - Phase 1	5.5	84	100%	5.1
Rahman Putra - Phase 2	4.1	175	100%	9.6
Rahman Putra - Phase 3	4.6	307	100%	15.3
Kwasa Sentral	64.1	8,606	70%	178.5
Lot 94 Jalan Kia Peng	1.9	1,012	100%	41.2
Pulai, Johor	67.5	770	100%	25.9
Cyberjaya City	113.3	5,350	70%	82.3
Bukit Jalil KL Sports City	76.1	20,700	17%	98.8
PJ Sentral - Nilaitera	7.8	1,656	100%	88.1
Canegie, Melbourne	1.0	305	100%	22.4
Subtotal		54,911		1,364.3
Investment / For Sale properties	Location	Mkt value (MYR m)	BV (MYR m)	Net surplus (MYR m)
Ascott Residences	KL Sentral	268.0	96.8	128.4
Plaza Alam Sentral	KL Sentral	147.0	74.3	54.6
Kompleks Sentral	Segambut	52.0	30.1	16.4
Subtotal				199.3
Others	FV based on RHB's TP (MYRm)	BV (MYR m)	Equity value/surplus (MYRm)	
Construction (16x 1-year forward earnings)				580.4
31% MQ REIT	402.3	264.0		138.3
LRT 3 PDP (based on DCF)				206.2
Kwasa Damansara PDP for infra works				79.1
Shareholders Funds (excl. construction)				2,835.82
Proceeds from rights issue				1,732.15
Total RNAV				7,135.57
Share base				4,365.45
RNAV per share				1.63
Discount				25%
Target Price (MYR)				1.23

Source: RHB

SWOT Analysis



Recommendation Chart



Source: RHB, Bloomberg

Date	Recommendation	Target Price	Price
2017-03-27	Buy	1.90	1.45
2017-02-28	Buy	1.66	1.24
2016-12-12	Buy	1.63	1.17
2016-12-01	Buy	1.60	1.11
2016-08-26	Buy	1.60	1.11
2016-05-31	Buy	1.60	1.01
2016-05-27	Buy	1.60	1.01
2016-02-23	Buy	1.60	1.04
2015-12-04	Buy	1.60	1.11
2015-11-20	Buy	1.60	1.18

Source: RHB, Bloomberg

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