

Malaysia Company Focus

MKH Bhd

Bloomberg: MKH MK| Reuters: METR.KL

Refer to important disclosures at the end of this report

DBS Group Research . Equity

11 Sep 2014

BUY RM3.70 KLCI : 1,870.85

Price Target: 12-Month RM5.70

Reason for Report: Company update

Potential Catalyst: Strong earnings delivery

AllianceDBSvs Consensus: First to cover

Analyst

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Price Relative



Forecasts and Valuation

| FY Sep (RM m) | 2013A | 2014F | 2015F | 2016F |
|-----------------------------|-------|-------|-------|-------|
| Revenue | 688 | 759 | 948 | 1,339 |
| EBITDA | 183 | 194 | 264 | 382 |
| Pre-tax Profit | 136 | 170 | 238 | 355 |
| Net Profit | 103 | 119 | 171 | 256 |
| Net Pft (Pre Ex.) | 119 | 119 | 171 | 256 |
| EPS (sen) | 24.7 | 28.4 | 40.8 | 61.1 |
| EPS Pre Ex. (sen) | 28.4 | 28.4 | 40.8 | 61.1 |
| EPS Gth (%) | 38 | 15 | 44 | 50 |
| EPS Gth Pre Ex (%) | 96 | 0 | 44 | 50 |
| Diluted EPS (sen) | 24.7 | 28.4 | 40.8 | 61.1 |
| Net DPS (sen) | 7.5 | 8.3 | 8.3 | 12.5 |
| BV Per Share (sen) | 272.4 | 249.2 | 281.7 | 334.4 |
| PE (X) | 15.0 | 13.0 | 9.1 | 6.1 |
| PE Pre Ex. (X) | 13.0 | 13.0 | 9.1 | 6.1 |
| P/Cash Flow (X) | 14.2 | 7.4 | 11.2 | 9.4 |
| EV/EBITDA (X) | 10.7 | 9.9 | 7.3 | 5.0 |
| Net Div Yield (%) | 2.0 | 2.3 | 2.3 | 3.4 |
| P/Book Value (X) | 1.4 | 1.5 | 1.3 | 1.1 |
| Net Debt/Equity (X) | 0.4 | 0.3 | 0.3 | 0.2 |
| ROAE (%) | 12.0 | 11.9 | 15.4 | 19.8 |
| Earnings Rev (%): | | 0 | 0 | 0 |
| Consensus EPS (sen): | | 29.0 | 38.0 | 61.0 |
| Other Broker Recs: | | B: 2 | S: 0 | H: 0 |

ICB Industry: Real Estate

ICB Sector: Real Estate Investment & Services

Principal Business: MKH is an established township developer in Kajang/Semenyih and Greater Klang Valley. Its 16k ha oil palm estates in Indonesia has started to contribute significantly

Source of all data: Company, AllianceDBS, Bloomberg Finance L.P.

Unjustified sell-down

- **Strong fundamentals grossly overlooked**
- **Growth pace picking up strongly; 3-year earnings CAGR of 29% over FY13-16**
- **Maintain high-conviction BUY with RM5.70 TP**

Oversold! MKH's share price has plunged 15% from its peak, partly driven by weaker-than-expected 3QFY14 results. In our view, the stock is grossly oversold as its solid fundamentals remain intact. We maintain MKH as our high-conviction pick with RM5.70 TP based on SOP. MKH is one of the few stocks under our coverage with visible growth prospects. After all, MKH is a proven developer with an uninterrupted 25-year profit track record – a feat unrivalled by most of its peers!

Robust demand from affordable homes. While overall sentiment in the property market remains weak, we believe MKH will be the least vulnerable to the slowdown given its focus on affordable housing which targets genuine buyers. This is evident from its record-breaking property sales, bucking the trend of lower sales among its peers. MKH's unbilled sales of RM690m is at an all-time high, and demand remains unabated in KL South largely due to the attractively priced affordable homes. Potential incentives for first-time home buyers in the upcoming Budget 2015 could further boost its property sales going forward.

Strongest FFB production growth. Plantation is another key growth driver for MKH. 9MFY14 FFB volume grew 36% y-o-y, resulting in an impressive 190% growth in 9MFY14 plantation pretax profit. We acknowledge the weak CPO prices at this juncture, but its exponential 3-year FFB volume CAGR of 20% will more than offset the bearish prices.

FX losses are non-cash flow item. We are not overly concerned with the unrealized FX gains/losses which is merely an accounting entry given the marked-to-market requirement on its US\$85m borrowings for the plantation division. This is not unusual to the Indonesian palm oil industry as even world-class plantation giants have US\$ loans.

At A Glance

| | |
|------------------------------|-------------|
| Issued Capital (m shrs) | 419 |
| Mkt. Cap (RMm/US\$m) | 1,552 / 485 |
| Major Shareholders | |
| Chen Choy & Sons Realty (%) | 43.1 |
| Public Bank Grp Off Fund (%) | 9.8 |
| Free Float (%) | 47.1 |
| Avg. Daily Vol.('000) | 685 |

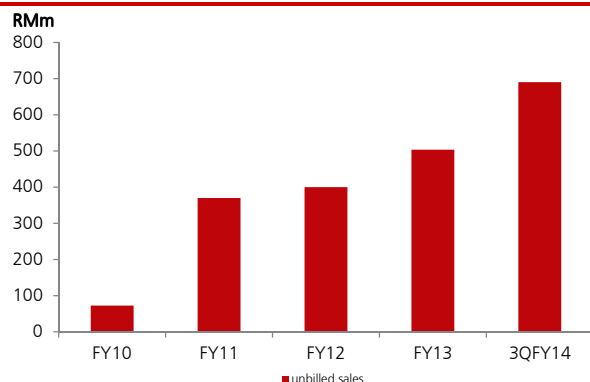
Strong fundamentals remain intact

We believe the robust outlook of MKH has been underestimated. While 3QFY14 earnings were short of our high expectations, its underlying business still registered a commendable performance with 9MFY14 core profit rising 13% y-o-y. We believe the financial results were decent in view of rising cost pressures and weaker sentiment in the property market which have been affecting many other property developers.

MKH's entrenched brand name in the Kajang-Semenyih growth corridor and its stronghold in the affordable housing segment have placed it in an enviable position with its property sales and unbilled sales continuing to chalk new highs. Strong unbilled sales of RM690m (1.45x FY13 property revenue) underpins clear earnings visibility going forward.

MKH is on track to achieve its record high property sales target of RM800m for FY14 (vs RM580m in FY13). It has booked RM548m sales in 9MFY14 and has RM178m of sales (as at Jun14) yet to be recognized. If MKH's strong property sales are anything to go by, the company could be registering even better property sales in FY15 by virtue of its attractively-priced affordable homes.

Record high unbilled sales



Source: AllianceDBS, Company

We believe KL South will provide sustainable and long-term growth prospects for MKH, benefitting from the completion of MRT Line 1 by 2017. With the scarcity of cheap land bank for developers to supply affordable landed homes within Greater KL, this area should attract home-buyers given the relatively lower property prices in KL South even though prices have been increasing rapidly over the past few years.

Promising growth from Plantations

We understand market has been rather concerned with the potential restriction of foreign ownership on Indonesian plantation estates. If the policy is ever implemented, we believe that it is unlikely to be applied retrospectively given the critical importance of the plantation industry to the Indonesian economy. Also, the move will entail various legal ramifications to the Indonesian government.

The impact to MKH will be relatively mild vis-à-vis other plantation players given its much smaller exposure in Indonesia. Also, MKH is likely to fetch premium pricing if its estates are up for sale, given the impressive yield for its still young palms of c.5 years old. Therefore, there is no reason for us to be too worried regarding this potential policy risk in Indonesia.

Meanwhile, MKH has recently upgraded its CPO mill to 90MT/hour to cater to its fast-growing FFB production. FFB output grew 37% q-o-q to 81.7k MT in 3QFY14, taking 9MFY14 FFB volume to 212k MT (78% of our full-year projection). We also expect seasonally higher FFB output in 4QFY14. All in, plantation profit is projected to expand at 3-year CAGR of 61% supported by the favourable palm tree age profile, and account for 27% and 34% of FY14F and FY15F Group earnings, respectively (vs 17% in FY13).

While CPO prices have been declining sharply recently, the exponential FFB volume growth will more than offset the bearish prices. We have imputed conservative CPO prices of RM2,380/RM2,400/RM2,560 for CY2014-2016. Therefore, any rebound in CPO prices will be a major boost to MKH's earnings.

Sensitivity of CPO price to Group's profit

| CPO price | Profit (RMm) | | Profit change % | |
|-----------|--------------|-------|-----------------|-------|
| | FY14F | FY15F | FY14F | FY15F |
| +10% | 128.9 | 185.8 | 8.2% | 8.6% |
| +5% | 124.0 | 178.4 | 4.1% | 4.3% |
| base case | 119.1 | 171.1 | 0.0% | 0.0% |
| -5% | 114.3 | 163.8 | -4.0% | -4.3% |
| -10% | 109.5 | 156.4 | -8.1% | -8.6% |

Source: AllianceDBS, Company

MKH has also set up a FX monitoring committee to manage the volatility of US\$ vs IDR by allocating proceeds from the sales of palm kernels to convert IDR to US\$ when it strengthens. Nevertheless, investors should not be overly concerned on the FX gains/losses given the unrealized nature of the transaction which is an accounting requirement.

Key Assumptions

| FY Sep | 2012A | 2013A | 2014F | 2015F | 2016F |
|----------------------|-------|-------|-----------|-----------|-----------|
| CPO ASP (RM/MT) | N/A | N/A | 2,307.8 | 2,323.2 | 2,444.4 |
| FFB production (MT) | N/A | N/A | 271,681.3 | 340,780.5 | 382,445.0 |
| property sales (RMm) | 423.7 | 580.8 | 728.6 | 796.6 | 1,058.0 |

Sensitivity Analysis

| 2015 | |
|-----------------------|-------------------|
| Property sales +/- 5% | Net Profit +/- 3% |
| CPO price +/- 5% | Net Profit +/- 4% |

Segmental Breakdown

| FY Sep | 2012A | 2013A | 2014F | 2015F | 2016F |
|--------|-------|-------|-------|-------|-------|
|--------|-------|-------|-------|-------|-------|

Revenues (RM m)

| | | | | | |
|---|------------|------------|------------|------------|--------------|
| Property development & Hotel & property | 391 | 476 | 489 | 597 | 949 |
| Trading | 32 | 32 | 34 | 36 | 38 |
| Manufacturing | 63 | 67 | 72 | 78 | 85 |
| Plantation | 13 | 9 | 9 | 10 | 10 |
| Plantation | 45 | 101 | 155 | 227 | 258 |
| Total | 545 | 688 | 759 | 948 | 1,339 |

Riding on two MRT stations in Kajang

Exponential growth driven by young trees

Core EBIT(RM m)

| | | | | | |
|---|------------|------------|------------|------------|------------|
| Property development & Hotel & property | 82 | 115 | 118 | 148 | 233 |
| Trading | 13 | 15 | 15 | 16 | 17 |
| Manufacturing | 4 | 4 | 5 | 5 | 6 |
| Plantation | 1 | 0 | 0 | 0 | 0 |
| Plantation | 0 | 29 | 51 | 89 | 121 |
| Total | 101 | 163 | 190 | 260 | 377 |

EBIT Margins (%)

| | | | | | |
|---|-------------|-------------|-------------|-------------|-------------|
| Property development & Hotel & property | 21.0 | 24.2 | 24.1 | 24.9 | 24.6 |
| Trading | 41.4 | 46.9 | 45.0 | 45.0 | 45.0 |
| Manufacturing | 7.1 | 6.7 | 7.0 | 7.0 | 7.0 |
| Plantation | 8.2 | (2.3) | 1.0 | 1.5 | 1.8 |
| Plantation | 0.5 | 28.3 | 33.2 | 39.4 | 46.8 |
| Total | 18.6 | 23.7 | 25.0 | 27.4 | 28.2 |

Income Statement (RM m)

| FY Sep | 2012A | 2013A | 2014F | 2015F | 2016F |
|---------------------------|------------|------------|------------|------------|------------|
| Revenue | 545 | 688 | 759 | 948 | 1,339 |
| Cost of Goods Sold | (362) | (441) | (416) | (525) | (789) |
| Gross Profit | 183 | 247 | 344 | 422 | 550 |
| Other Opng (Exp)/Inc | (90) | (90) | (154) | (163) | (173) |
| Operating Profit | 93 | 158 | 190 | 260 | 377 |
| Other Non Opg (Exp)/Inc | 0 | 0 | 0 | 0 | 0 |
| Associates & JV Inc | 15 | 11 | 4 | 4 | 4 |
| Net Interest (Exp)/Inc | (22) | (17) | (23) | (26) | (26) |
| Exceptional Gain/(Loss) | 14 | (16) | 0 | 0 | 0 |
| Pre-tax Profit | 100 | 136 | 170 | 238 | 355 |
| Tax | (27) | (29) | (43) | (59) | (89) |
| Minority Interest | 2 | (3) | (9) | (7) | (11) |
| Preference Dividend | 0 | 0 | 0 | 0 | 0 |
| Net Profit | 75 | 103 | 119 | 171 | 256 |
| Net Profit before Except. | 61 | 119 | 119 | 171 | 256 |
| EBITDA | 114 | 183 | 194 | 264 | 382 |

Growth

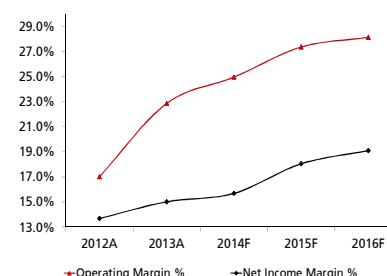
| | | | | | |
|--------------------|-------|------|------|------|------|
| Revenue Gth (%) | 78.2 | 26.2 | 10.3 | 24.8 | 41.3 |
| EBITDA Gth (%) | 105.6 | 59.8 | 6.1 | 36.2 | 44.7 |
| Opg Profit Gth (%) | 169.0 | 69.7 | 20.4 | 36.8 | 45.3 |
| Net Profit Gth (%) | 96.3 | 38.5 | 15.3 | 43.6 | 49.6 |

Margins & Ratio

| | | | | | |
|------------------------|------|------|------|------|------|
| Gross Margins (%) | 33.5 | 36.0 | 45.3 | 44.6 | 41.1 |
| Opg Profit Margin (%) | 17.0 | 22.9 | 25.0 | 27.4 | 28.2 |
| Net Profit Margin (%) | 13.7 | 15.0 | 15.7 | 18.1 | 19.1 |
| ROAE (%) | 9.9 | 12.0 | 11.9 | 15.4 | 19.8 |
| ROA (%) | 5.4 | 6.2 | 6.2 | 8.1 | 10.7 |
| ROCE (%) | 5.4 | 8.4 | 8.5 | 10.8 | 14.2 |
| Div Payout Ratio (%) | 14.6 | 25.3 | 29.3 | 20.4 | 20.5 |
| Net Interest Cover (x) | 4.3 | 9.2 | 8.1 | 9.9 | 14.5 |

Source: Company, AllianceDBS

Margins Trend



Margin lifted by plantation business

Quarterly / Interim Income Statement (RM m)

| FY Sep | 3Q2013 | 4Q2013 | 1Q2014 | 2Q2014 | 3Q2014 |
|-------------------------|-----------|-----------|-----------|-----------|-----------|
| Revenue | 185 | 218 | 182 | 188 | 212 |
| Cost of Goods Sold | (115) | (142) | (118) | (113) | (139) |
| Gross Profit | 70 | 76 | 64 | 76 | 73 |
| Other Oper. (Exp)/Inc | (22) | (16) | (16) | (24) | (23) |
| Operating Profit | 48 | 60 | 49 | 52 | 50 |
| Other Non Opg (Exp)/Inc | 0 | 0 | 0 | 0 | 0 |
| Associates & JV Inc | 0 | 1 | 1 | 1 | 0 |
| Net Interest (Exp)/Inc | (6) | (2) | (5) | (7) | (7) |
| Exceptional Gain/(Loss) | 2 | (33) | (20) | 29 | (22) |
| Pre-tax Profit | 44 | 27 | 25 | 75 | 21 |
| Tax | (12) | (2) | (6) | (19) | (6) |
| Minority Interest | 0 | 0 | (2) | (5) | (3) |
| Net Profit | 32 | 24 | 17 | 51 | 12 |
| Net profit bef Except. | 30 | 57 | 37 | 21 | 34 |
| EBITDA | 48 | 61 | 50 | 53 | 50 |

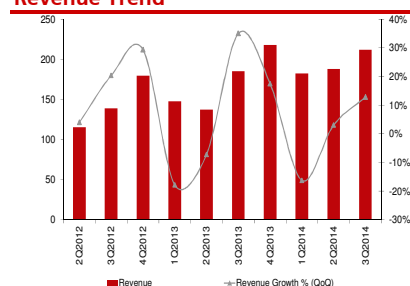
Growth

| | | | | | |
|--------------------|-------|--------|--------|-------|--------|
| Revenue Gth (%) | 35.1 | 17.5 | (16.2) | 3.1 | 12.8 |
| EBITDA Gth (%) | 88.8 | 27.3 | (18.6) | 6.4 | (4.9) |
| Opg Profit Gth (%) | 91.6 | 25.4 | (19.4) | 6.3 | (3.3) |
| Net Profit Gth (%) | 155.0 | (25.2) | (30.8) | 203.1 | (77.1) |

Margins

| | | | | | |
|------------------------|------|------|------|------|------|
| Gross Margins (%) | 37.8 | 35.0 | 35.3 | 40.2 | 34.3 |
| Opg Profit Margins (%) | 26.0 | 27.7 | 26.7 | 27.5 | 23.5 |
| Net Profit Margins (%) | 17.4 | 11.1 | 9.2 | 26.9 | 5.5 |

Revenue Trend

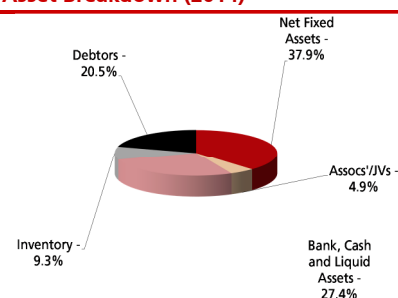


FX losses arising from US\$ borrowings for its Indonesian plantation business

Balance Sheet (RM m)

| FY Sep | 2012A | 2013A | 2014F | 2015F | 2016F |
|-------------------------------|--------------|--------------|--------------|--------------|--------------|
| Net Fixed Assets | 163 | 163 | 243 | 323 | 403 |
| Invt in Associates & JVs | 50 | 28 | 32 | 36 | 40 |
| Invt&Devt Properties | 238 | 264 | 264 | 264 | 264 |
| Other LT Assets | 564 | 713 | 763 | 784 | 806 |
| Cash & ST Invt | 110 | 123 | 175 | 178 | 205 |
| Dev Props held for sale | 129 | 280 | 203 | 257 | 386 |
| Inventory | 43 | 41 | 60 | 75 | 105 |
| Debtors | 94 | 113 | 132 | 164 | 232 |
| Other Current Assets | 370 | 561 | 522 | 623 | 851 |
| Total Assets | 1,495 | 1,851 | 1,998 | 2,207 | 2,568 |
| ST Debt | 193 | 107 | 107 | 107 | 107 |
| Creditor | 140 | 182 | 195 | 243 | 344 |
| Other Current Liab | 26 | 40 | 73 | 90 | 120 |
| LT Debt | 307 | 415 | 415 | 415 | 415 |
| Other LT Liabilities | 55 | 152 | 152 | 152 | 152 |
| Shareholder's Equity | 775 | 951 | 1,044 | 1,181 | 1,402 |
| Minority Interests | (2) | 3 | 11 | 19 | 29 |
| Total Cap. & Liab. | 1,495 | 1,851 | 1,998 | 2,207 | 2,568 |
| Non-Cash Wkg. Capital | 204 | 339 | 254 | 289 | 387 |
| Net Cash/(Debt) | (391) | (399) | (346) | (344) | (317) |
| Debtors Turn (avg days) | 62.6 | 54.9 | 58.7 | 57.0 | 54.0 |
| Creditors Turn (avg days) | 109.7 | 137.6 | 165.4 | 152.2 | 135.7 |
| Inventory Turn (avg days) | 28.0 | 35.8 | 44.1 | 46.7 | 41.6 |
| Asset Turnover (x) | 0.4 | 0.4 | 0.4 | 0.5 | 0.6 |
| Current Ratio (x) | 1.3 | 2.1 | 1.9 | 1.8 | 1.9 |
| Quick Ratio (x) | 0.6 | 0.7 | 0.8 | 0.8 | 0.8 |
| Net Debt/Equity (X) | 0.5 | 0.4 | 0.3 | 0.3 | 0.2 |
| Net Debt/Equity ex MI (X) | 0.5 | 0.4 | 0.3 | 0.3 | 0.2 |
| Capex to Debt (%) | 18.1 | 33.4 | 15.3 | 15.3 | 15.3 |
| Z-Score (X) | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 |

Asset Breakdown (2014)



42% net gearing as at Jun14

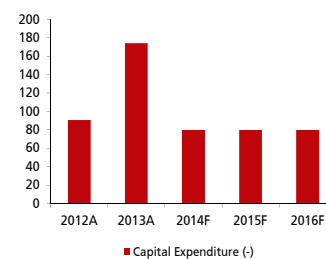
Source: Company, AllianceDBS

Cash Flow Statement (RM m)

| FY Sep | 2012A | 2013A | 2014F | 2015F | 2016F |
|-------------------------|-------------|--------------|--------------|--------------|--------------|
| Pre-Tax Profit | 100 | 136 | 170 | 238 | 355 |
| Dep. & Amort. | 7 | 14 | 0 | 0 | 0 |
| Tax Paid | (29) | (36) | (9) | (43) | (59) |
| Assoc. & JV Inc/(loss) | (15) | (11) | (4) | (4) | (4) |
| Chg in Wkg.Cap. | (53) | (6) | 52 | (53) | (127) |
| Other Operating CF | 9 | 13 | 0 | 0 | 0 |
| Net Operating CF | 20 | 109 | 209 | 138 | 164 |
| Capital Exp.(net) | (91) | (174) | (80) | (80) | (80) |
| Other Invts.(net) | (51) | (24) | (50) | (21) | (22) |
| Invts in Assoc. & JV | 0 | 0 | 0 | 0 | 0 |
| Div from Assoc& JV | 0 | 34 | 0 | 0 | 0 |
| Other Investing CF | 57 | 0 | 0 | 0 | 0 |
| Net Investing CF | (86) | (164) | (130) | (101) | (102) |
| Div Paid | (10) | (13) | (26) | (35) | (35) |
| Chg in Gross Debt | 112 | 49 | 0 | 0 | 0 |
| Capital Issues | 0 | 52 | 0 | 0 | 0 |
| Other Financing CF | 0 | 0 | 0 | 0 | 0 |
| Net Financing CF | 102 | 88 | (26) | (35) | (35) |
| Currency Adjustments | 11 | (20) | 0 | 0 | 0 |
| Chg in Cash | 47 | 13 | 53 | 2 | 28 |
| Opg CFPS (sen) | 17.2 | 27.6 | 37.4 | 45.5 | 69.6 |
| Free CFPS (sen) | (17.0) | (15.5) | 30.7 | 13.9 | 20.1 |

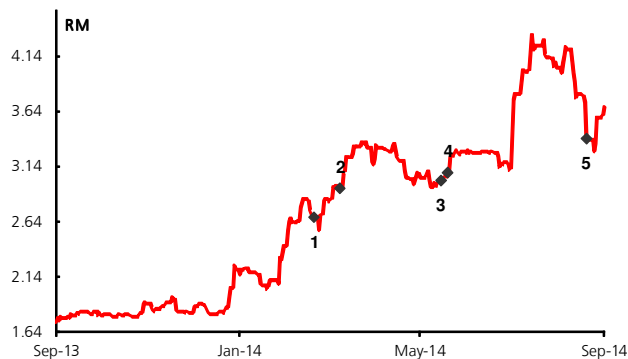
Source: Company, AllianceDBS

Capital Expenditure



Capex for plantation business

Target Price & Ratings History



Note: Share price and Target price are adjusted for corporate actions.

| S.No. | Date | Closing Price | Target Price | Rating |
|-------|-----------|---------------|--------------|--------|
| 1: | 28 Feb 14 | 2.68 | 4.50 | Buy |
| 2: | 17 Mar 14 | 2.94 | 4.50 | Buy |
| 3: | 23 May 14 | 3.02 | 4.88 | Buy |
| 4: | 28 May 14 | 3.08 | 4.88 | Buy |
| 5: | 28 Aug 14 | 3.40 | 5.70 | Buy |

Source: AllianceDBS

AllianceDBS Research recommendations are based on Absolute Total Return* Rating system, defined as follows:

STRONG BUY (>20% total return over the next 3 months, with identifiable share price catalysts within this time frame)

BUY (>15% total return over the next 12 months for small caps, >10% for large caps)

HOLD (-10% to +15% total return over the next 12 months for small caps, -10% to +10% for large caps)

FULLY VALUED (negative total return i.e. > -10% over the next 12 months)

SELL (negative total return of > -20% over the next 3 months, with identifiable catalysts within this time frame)

Share price appreciation + dividends

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