Latent potential

Jaks is emerging as a credible player in the property business, and management views this segment as a key earnings-growth driver going forward. Management is still looking to achieve financial closure of the Hai Duong IPP, after a RM140m investment in this project. Shares of Jaks are trading below book value of RM1.03.

Property segment: a key revenue driver, according to management

Jaks has been quietly building up itself to be a property player of decent size. With unbilled sales of RM730m, management expects this segment to drive the company's revenue growth going forward. Jaks has 2 major property developments in the pipeline that are worth about RM3bn, and is actively exploring for new landbank to sustain future growth.

Construction segment provides steady revenue stream

Over the years, Jaks has actively expanded into the construction segment, in particular for road infrastructure and water-related infrastructure projects. The group has a healthy construction work order book of RM1.5bn and we expect ongoing efforts to replenish its construction work order book to provide the group with a steady revenue source of income.

Water pipe business still has latent potential

The water-pipe business contributes less than 20% of Jaks's revenue but management believes there is still latent potential in the business. Management believes once the legal issues between the state and federal governments are sorted out, this would kick start the country's pipe replacement programme.

Vietnam venture still in the gestation phase

Management is confident about seeing financial closure for the group's power project in Vietnam over the longer term. However, we do note that the project comes with its associated risks. Thus far, Jaks has invested about RM140m in the project, and there could be an impairment charge if management is unable to monetise the project.

Valuation: shares trading below book value

Since posting losses in FY11, Jaks has notably seen a significant turnaround in earnings. In terms of valuation, shares of Jaks are trading below book value of RM1.03. Management attributes this to having long been out of investors' radar (only 1 sell-side analyst) as most would have lost patience over the long drawn out water-restructuring saga in Selangor and repeated delays for financial closure of its Hai Duong IPP.

Earnings & Valuation Summary

FYE 31 Dec	2010^	2011^	2012^	2013	2014
Revenue (RMm)	257.3	326.7	376.4	586.4	491.1
EBITDA (RMm)	15.1	(5.6)	22.8	42.7	73.8
Pretax profit (RMm)	4.4	(19.2)	8.2	19.8	53.9
Net profit (RMm)	2.4	(23.1)	2.0	10.7	34.1
EPS (sen)	0.5	(5.2)	0.6	1.7	3.2
PER (x)	>100	Nm	>100	36.8	19.8
Core net profit (RMm)	2.3	3.0	2.8	7.5	14.0
Core EPS (sen)	0.5	0.7	0.6	1.7	3.2
Core EPS growth (%)	(>100)	30.4	(7.4)	>100	86.1
Core PER (x)	>100	92.9	>100	36.8	19.8
Net DPS (sen)	-	-	-	-	-
Dividend Yield (%)	-	-	-	-	-
EV/EBITDA (x)	21.4	Nm	21.7	20.7	13.5
Chg in EPS (%)	-	-	-	-	-
Affin/Consensus (x)	-	-	-	-	-

Source: Company, Affin Hwang estimates
^ FYE 31 October; FYE changed to December from 2013

Company Note

JAKS Resources

JAK MK
Sector: Utilities

RM0.63 @ 8 Apr 2015

NON-RATED

Price Performance

	1M	3M	12M
Absolute	+7.8%	+45.9%	+18.1%
Rel to KLCI	+4.5%	+36.7%	+18.6%

Stock Data

Issued shares (m)	438.4
Mkt cap (RMm)/(US$m)	278.4/76.7
Avg daily vol - 6mth (m)	3.0
52-wk range (RM)	0.38-0.85
Est free float	76%
BV per share (RM)	1.06
P/BV (x)	0.60
Net cash/(debt) (RMm) (4Q14)	(431.3)
ROE (2014)	3.0%
Derivatives	Nil
Shariah Compliant	No

Key Shareholders

Ang Lam Poah	7.4%
Original Invention	5.0%
Dimensional Fund	4.1%

Source: Affin Hwang, Bloomberg

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No longer dependent on the water business

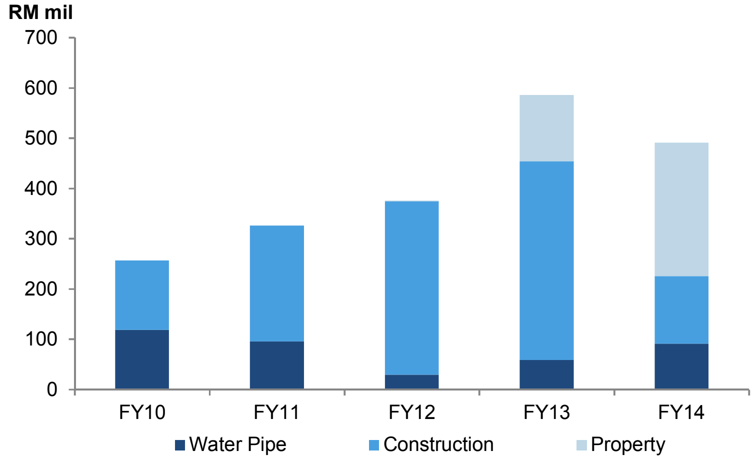
Property segment: a key revenue driver, according to management

JAKS Resources Bhd (Jaks) has been quietly building up itself to be a property player of decent size and with unbilled sales of RM730m, and management expects this segment to drive revenue growth going forward. The property segment has emerged as Jaks' largest revenue contributor, with property sales worth RM265m booked in 2014.

Jaks has built up its property portfolio quickly, having started with maiden property revenue of RM132m in 2013. With more property projects in the pipeline, management aims to be on par with other niche property players, which typically generate annual sales of between RM300-400m.

Going forward, Jaks has two major property developments in the pipeline that are worth about RM3bn, and is still actively exploring for new land bank to sustain future growth. Both are mixed development projects that would underpin Jaks' earnings base in FY15-16. The first is Pacific Star (GDV of RM1.2bn) and the other project is Jaks USJ 1 (GDV of RM2bn).

Fig 1: Segmental Breakdown



Source: Affin Hwang, Company data

Jaks's foray into the property business can be traced back to its acquisition of a 51% equity interest in MNH Global Assets Management Sdn Bhd (MNH) from Island Circle Development Sdn Bhd for a cash consideration of RM93.2m in 2013. MNH was then developing the RM1.2bn GDV (gross development value) mixed development known as Pacific Place Ara Damansara, Petaling Jaya which was completed in 2014. Having access to key talent was another factor which drove Jaks to acquire a simple majority stake in MNH.

Fig 2: Pacific Place Ara Damansara

Source: Company data

Fig 3: Pacific Star Ara Damansara

Source: Company data

Pacific Star sits at Section 13, Petaling Jaya and had commenced construction in September 2014 (due for completion in September 2016). The project is estimated to command a GDV of RM1.2bn. Pacific Star is a mixed development comprising a 9-storey retail podium, 2 blocks of office towers and 3 blocks of apartment. This was initially a joint venture with Star Publications (Star) but consequently, both parties agreed that Jaks should undertake it on its own. Jaks had acquired the 6-acre land from Star for RM135m and the payment for this consideration would be the construction and transfer of an office tower to Star.

Besides that, Jaks intends to embark on the Jaks USJ 1 project, which involves redeveloping the site of its existing headquarters in Lot 526, Persiaran Subang Permai into a mixed-use development with a GDV of about RM2bn. The proposed development will mainly be comprised of Jaks Tower, 3 blocks of office suites and 6 blocks of service apartments. In addition, there will be a 3-storey commercial podium within the mixed-use development. We understand from management that the project may be launched in 2H15.

Fig 4: Jaks USJ 1

Source: Company data

Construction segment provides a steady revenue stream

Over the years, Jaks has actively expanded into the construction segment, in particular for road infrastructure and water-related infrastructure projects. The group has a healthy construction work order book of RM1.5bn (excluding internal building works for Pacific Place and Pacific Star), and we expect ongoing efforts to replenish its construction work order book to provide the group with a steady revenue source of income.

We note that Jaks has a good track record in bagging road infrastructure projects. Two major road infrastructure projects currently undertaken by the group are the Sadong bridge in Sarawak worth RM211m and road upgrading works near Penang International Airport worth RM208m. Both of these projects are due for completion in 2016.

Jaks is also actively undertaking water-related infrastructure projects. The group is expected to complete the construction of the Besut Dam Reservoir, Terengganu for a contract value of RM345m and is currently busy with the sewage pipe laying work for Puchong and Jinjang worth a combined value of RM636m due for completion in 2017-2018.

Water-pipe business still has latent potential

Government needs to address high non-revenue water issue

While the water pipe business contributes less than 20% of Jak's revenue, management believes there is still latent potential in the business. We note, however, that there could be delays to Selangor's water restructuring, after the state government declined to give a third extension to the master water agreement, which lapsed on 9 March 2015.

We believe that only upon the state and federal governments sorting out the legal issues with regards to the ownership of the Semenyih and Bukit Nanas reservoirs, together with all the water pipelines in Selangor, would the country's pipe replacement programme get kick started. The programme is estimated to be worth close to RM10bn (of which RM1bn is expected to be allocated to Selangor). Selangor has the worst Non-Revenue Water (NRW) in the country, losing nearly RM667mn annually. We note that in Selangor there has been years of under investment in the infrastructure amid a growing population.

Management is confident that Jaks is in a good position to win more water-pipe jobs, despite operating its plant at low utilisation. Jaks has a good historical track record and is ready to ramp up utilisation of its existing plant at a moment's notice. In fact, Jaks recently won the award for Package 5 of the supply and installation of pipes for the Langat 2 water treatment plant for a contract sum of RM55m. The contract is for a duration of 24 months and is expected to be completed by January 2017.

Vietnam venture still in gestation phase

Still some time to go to achieve financial closure to Vietnam IPP

Management is still confident about seeing financial closure for the group's power project in Vietnam over the longer term. However, we do note that this project comes with its associated risks. Recall that Jaks has a long chapter in the group's history from its investment in the US$2.0bn 2x600MW coal-fired thermal power plant in Hai Duong Province Vietnam (IPP – Independent Power Plant) that will cost a total of US$2.0bn. The concession term of the IPP is 25 years.

After 6 years, Jaks has yet to achieve financial closure to its Vietnam IPP investment. However, management is hopeful about the entry of a credible and financially-sound partner in the near term. If this materialises, Jaks's management expects to receive earnings contribution from the Hai Duong IPP starting in 2020, given that construction will likely take about 5 years.

Thus far, Jaks has invested about RM140m in the project. If Jaks is both unable to achieve financial closure before the deadline and secure a further extension to the deadline, one of the risks it faces is the possibility of an impairment charge in relation to the investments already sunk into this project.

Recall that on 28 October 2014, Jaks had requested that the Ministry of Industry and Trade of Vietnam (MOIT) extend the required date for completion of the preconditions (including the achievement of financial closure) of the Hai Duong IPP to 31 October 2015. So far, we understand that the RM140m spent has been mostly for preparation of the main plant site and project infrastructure work such as the main access road.

According to management, achieving financial closure is the only major outstanding issue remaining to get the Hai Duong IPP up and running. Management said all the necessary project documents for the Hai Duong IPP such as the Build-Operate-Transfer (BOT) contract, Power Purchase Agreement (PPA), coal supply agreement and the land lease agreement have been executed. Besides that, the site for the main plant has been officially handed over following clearance work and land compensation.

Below book value

Valuation: shares trading below their book value

Since 2011, Jaks has notably seen a significant turnaround in earnings and management expects the earnings growth momentum to continue on the back of higher property sales and stable construction revenue. The group recorded a strong 3-year FY11-14 core earnings CAGR of 67.5%. Note that the loss of RM23.1m in FY11 stemmed primarily from the adoption of Financial Reporting Standards 136, which resulted in a goodwill impairment of RM25.9m. Otherwise, we calculate Jaks recorded core net profit of RM3.0m in FY11.

Shares of Jaks are trading well below book value of RM1.03. Management attributes this to a lack of sell-side coverage (only 1 sell-side analyst), which has led to the stock having long been out of investors' radar as most would have lost patience over the long drawn out water restructuring saga in Selangor and the repeated delays for financial closure of its Hai Duong IPP.

In terms of milestones for the future, management is hopeful to see: i) financial closure of its Hai Duong IPP; ii) more water-related and other construction project wins; and iii) the eventual conclusion of the water services industry restructuring which would pave the way for a nationwide water-pipe replacement program.

Risks

Downside risks

Management sees the following as risk factors: 1) delay or inability to secure a partner to achieve financial closure for the Vietnam IPP; 2) softer-than-expected property sales; 3) lack of replenishment for construction order book; and 4) a protracted water-restructuring scenario in Selangor.

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BUY	Total return is expected to exceed +10% over a 12-month period
HOLD	Total return is expected to be between -5% and +10% over a 12-month period
SELL	Total return is expected to be below -5% over a 12-month period
NOT RATED	Affin Hwang Investment Bank Berhad does not provide research coverage or rating for this company. Report is intended as information only and not as a recommendation

The total expected return is defined as the percentage upside/downside to our target price plus the net dividend yield over the next 12 months.

OVERWEIGHT	Industry, as defined by the analyst's coverage universe, is expected to outperform the KLCI benchmark over the next 12 months
NEUTRAL	Industry, as defined by the analyst's coverage universe, is expected to perform inline with the KLCI benchmark over the next 12 months
UNDERWEIGHT	Industry, as defined by the analyst's coverage universe is expected to under-perform the KLCI benchmark over the next 12 months

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