

Stock Digest

Company Note – AWC Bhd

Wednesday, 26 Sep, 2018



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Strengthening Earnings Stream

Highlights

- The shareholders of AWC Bhd have approved of the proposed acquisition of a 60.0% equity stake in Trackwork & Supplies Sdn Bhd for RM43.5 mln as it plans to diversify its existing engineering services business to include rail-related works. The aforementioned proposals are expected to be completed by October this year.
- To recap, Trackwork is mainly involved in supplying track materials and rolling stock, the maintenance of railway tracks, supplying and commissioning of track tools, equipment and machineries as well as supplying depot equipment, tools and track diagnostics and monitoring systems.
- The acquisition also comes with a cumulative net profit guarantee of RM20.0 mln for FY18 and FY19. The acquisition cost of RM43.5 mln will be paid in cash amounting to RM20.0 mln, while the remaining amount will be satisfied via the issuance of new AWC shares in tranches.
- Trackwork's has achieved about RM7.6 mln in net profit as at June 2018 and the group is confident that it will achieve the RM8.0 mln required in FY18, which ends in September. Outstanding orderbook and tenderbook, meanwhile, stood at RM70.0 mln and RM900.0 mln respectively. Upon completion of the acquisition, AWC will consolidate part of the earnings from Trackwork, which is expected to be around RM6.0 mln in FY19-FY20.

Financial Highlights					
FYE June (MYR mln)	2016A	2017A	2018A	2019F	2020F
Revenue	248.5	184.8	304.0	282.7	317.5
EBITDA	31.6	41.6	34.7	37.6	43.4
Net Profit	17.1	22.0	21.4	28.3	31.8
Revenue Growth (%)	94.1	-25.6	64.5	-7.0	12.3
EBITDA Growth (%)	122.7	31.5	-16.5	8.4	15.4
Net Profit Growth (%)	111.9	28.6	-2.9	32.5	12.4
EPS (sen)*	6.0	7.7	7.4	9.9	10.9
P/E(x)	13.7	10.6	10.9	8.3	7.5
DPS (sen)	2.5	2.0	0.5	2.3	2.5
Dividend Yield (%)	3.1	2.5	0.6	2.8	3.1
BVPS (RM)	0.5	0.6	0.7	N/A	N/A
P/BV (x)	1.6	1.4	1.2	N/A	N/A
ROE (%)	14.4	15.6	13.0	N/A	N/A

Based on enlarged share capital of 287.1 mln and 293.1 mln outstanding shares (After adjusting for issuance of shares in relation to Trackwork acquisition)

Source: Company Data, MSSB Research

BUY

Share Price: RM0.815

Target Price: RM1.20

Key Statistics

Stock Information: Engaged in the provision of integrated facilities management services, engineering services and automated pneumatic waste collection systems

Sector: Trading/Services

Industry: Professional & Technical
Specialty Services

Listing: Main Market

Stock Code: 7579

Share Issued (mln): 272.9

Market Capital (RM mln): 219.7

Par Value (RM): N/A

Major Shareholders:

K-Capital Bhd 30.7%

Employees Provident

Fund Board 6.4%

Tan Keng Hee 4.4%

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Prospects

The proposed diversification will provide an additional revenue and income stream for the group and reduce the its reliance on its IFM business as the group expects contributions from rail-related projects to make up more than 25.0% of its net profit in due course. The IFM business has an orderbook of RM704.0 mln, including RM186.0 mln which is attributed to non-concession contracts.

The proposed acquisition also includes a Call/Put option which entails:

- i.) The granting of a **Call option** for AWC to purchase the remaining 40.0% shareholding in Trackwork owned by Trakniaga (shareholder of Trakwork), effective from the expiry of the profit guarantee period (i.e: 30th September 2019) up to the fifth anniversary year of the completion date for the acquisition,
- ii.) The granting of a **Put option** for Trakniaga to require AWC to purchase its remaining 40.0% shareholding in Trakwork, effective up to six months from the expiry of the Call option.

AWC is also withholding a sum of RM18.0 mln from the total RM20.0 mln cash consideration payable to Trakniaga, the vendors of Trackwork, and will release the RM18.0 mln in tranches until the complete payment of the settlement claims owed to **Fajarbaru**.

To recap, the settlement claims relates to a damages claim from Fajarbaru against Gemac and Trackwork on 5th June 2018. We note that Trackwork is not liable for the damages claim following a letter of undertaking and indemnity from Gemac, which states that it will be solely responsible for the full payment of the settlement sum.

We are positive that the new business will provide the group an opportunity to leverage on the untapped railway maintenance industry and utilised its expertise in facilities management and engineering services.

Valuation and Recommendation

Post-acquisition, we expect earnings contributed by Trackwork to bump up our FY19-FY20 EPS estimates by 13.0%-16.9% to 9.9 sen and 10.9 sen respectively. We maintain our **BUY** recommendation on AWC with a higher target price of RM1.20 (from RM0.90) by ascribing a higher target PER of 12.0x to its FY19's EPS of 9.9 sen. Our target PER was adjusted higher to reflect the increase in the share price of **UEM Edgenta Bhd**, its main peer in the IFM business, but also at a discount to the latter due to the AWC's smaller market capitalisation.

Risk to our recommendation and target price include failure to replenish its targeted orderbook and project delays due to the cyclical risks inherent to the construction industry that could lead to unforeseen cost increases and reputational damage. Escalating utility cost and increase in the prices of consumables could also compress the margins of the IFM contracts, while any fluctuation in the cost of raw materials could also impact AWC's margins in the already saturated HVAC market.

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Income Statement					
FYE June (MYR mln)	2016A	2017A	2018A	2019F	2020F
Revenue	248.5	184.8	304.0	282.7	317.5
EBITDA	31.6	41.6	34.7	37.6	43.4
Depreciation & Amortisation	-1.8	-2.5	-2.6	-2.9	-3.3
Net Interest Income/(Expense)	0.3	-0.4	1.4	-1.0	-0.4
Pre-tax Profit	30.1	38.7	33.4	33.7	39.7
Effective Tax Rate	21.4%	20.1%	21.0%	22.0%	22.5%
Net Profit	17.1	22.0	21.4	28.3	31.8
EBITDA Margin	12.7%	22.5%	11.4%	13.3%	13.7%
Pre-tax Margin	12.1%	20.9%	11.0%	11.9%	12.5%
Net Margin	6.9%	11.9%	7.0%	10.0%	10.0%

Source: Company Data, MSSB Research

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