

**Company Result**

**SCH Group Berhad**

*A lacklustre start*

24 January 2017

**HOLD**

**Maintained**

<b>Share Price</b>	<b>RM0.175</b>
<b>Target Price</b>	<b>RM0.18</b>

**Company Description**

SCH Group Berhad, through its subsidiary, imports, distribute and supplies industrial spare parts for quarry equipment.

**Stock Data**

Bursa / Bloomberg code	0161 / SCHG MK
Board / Sector	ACE / Industrial
Syariah Compliant status	Yes
Issued shares (m)	412.13
Par Value (RM)	0.10
Market cap. (RMm)	72.14
52-week price Range	RM0.16 – 0.26
Beta (against KLCI)	0.82
3-m Average Daily Volume	0.44m
3-m Average Daily Value <sup>^</sup>	RM0.08m

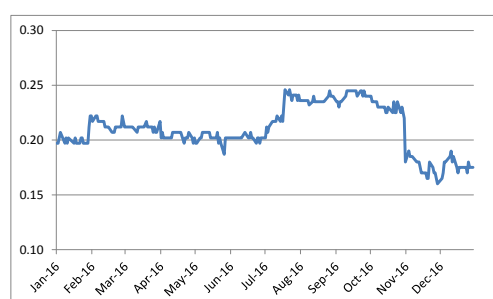
**Share Performance**

	1m	3m	12m
Absolute (%)	9.4	-2.8	-14.6
Relative (%)	5.8	-26.8	-17.0

**Major Shareholders**

	%
Mong Ling Lau	14.28
Sin Chin Wong	10.44
Yoon Hin Yeen	9.19

**Historical Chart**



Source: Bloomberg

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**Result**

- **Below expectation.** SCH Group Berhad (SCH) managed to return to the black with a 1QFY17 net profit of RM0.4m from a net loss of RM0.4m in 4QFY16. However, for yoy basis, the Group achieved lower net earnings, tumbling 66.7%. Overall, the 1Q net profit significantly fell short of our forecast, which accounted for 7% of our full year earnings estimate.

**Comment**

- **No sign of relief for its major earnings contributor, quarry M&E.** Sales of quarry M&E were down substantially, -87.5% yoy and -50.0% qoq, with continued sluggish property market coupled with cautious spending of quarry operators amid prevalent weakening of Ringgit resulted in higher import costs for their new and reconditioned machineries. We have witnessed revenue contribution of the quarry M&E to the Group's topline further deteriorated to 6.0% from 34% a year ago and 13% from previous quarter. This also explained the weaker yoy results for the Group with total revenue down by 28.2% yoy and further aggravated by proportionately higher fixed cost in respect of administrative expenses and sales & distribution expenses as PBT margin declined 7.4ppts to 7.1% from 14.5% last year.
- **Quarry spare parts cushioned the downfall.** SCH achieved better qoq results thanks to the quarry industrial products and spare parts (+14.8% qoq) which played a critical role in aiding the Group to chalk up higher revenue (+6.3% qoq) and GP margin (+5.1ppts) hence pulling out the Group from the red in 4QFY16. We believe the higher sales of quarry spare parts was mainly due to higher wear and tear as quarry operators hold on to their aging M&E under current economic uncertainties instead of replacing a new one which are more costlier.
- **Mild recovery seen in 2H.** The Group foresees sizeable orders flowing in during 2Q-3QCY17, underpinned by take-off of several mega infrastructure projects such as MRT2, LRT3, Pan Borneo Highway, DASH, SUKE, EKVE. Hence, it would lift the Group's topline and bottomline starting 3Q/4QFY17 onwards with stronger earnings expected in FY18.
- **On the prowl for new growth drivers.** In order to further enhance its presence in the quarry industry, SCH plans to expand its quarry product range by introducing new products such as foundry casting parts to accommodate different industrial needs. In addition, the Group also intends to increase its penetration in the mining industry by engaging in quarry engineering services with the provision of designing, steel fabrication, installation and

commissioning of quarry plants. We do not rule out the possibility of SCH acquiring a small-scale premix plant and/or mining concessionaire to fast-track its ambitious plan.

### Earnings Outlook/Revision

- **We slash our net earnings forecasts for FY17F to RM4.0m from RM5.5m in view of weaker sales of quarry M&E and lower margin achieved. However, we maintain our FY18F earnings forecast in anticipation of stronger earnings rebound.**

### Valuation & Recommendation

- **Maintain HOLD with a target price of RM0.18 (after adjusting for recent bonus issue of warrant).** Our fair value for SCH is pegged at 14.7x FY2018F FD PE. This is in the range of upcycle PE of small cap stocks in view of prevailing construction boom which is expected to benefit the quarry and mining sectors. Any positive earnings surprise would warrant re-rating of the stock and prompt our call upgrade.

**Figure 1: Quarterly Figures**

Year to 31 Aug (RMm)	1QFY17	4QFY16	1QFY16	qoq %	yoy %
Revenue	8.4	7.9	11.7	6.3	-28.2
Gross Profit	3.3	2.7	4.5	22.2	-26.7
PBT	0.6	-0.6	1.7	n.a.	-64.7
Net Profit	0.4	-0.4	1.2	n.a.	-66.7
Gross margin (%) / ppt	39.3	34.2	38.5	5.1	0.8
PBT margin (%) / ppt	7.1	-7.6	14.5	n.a.	-7.4

Source: Company, JF Apex

**Figure 2: Financial Summary**

FYE 31 Aug	FY2014	FY2015	FY2016	FY2017F	FY2018F
	(RMm)	(RMm)	(RMm)	(RMm)	(RMm)
Revenue	65.4	59.6	37.1	45.5	61.6
Gross Profit	24.6	22.8	14.3	17.0	24.8
PBT	10.3	9.2	2.3	5.7	9.8
Taxation	-3.2	-2.7	-0.8	-1.7	-2.9
PAT	7.2	6.5	1.6	4.0	7.0
Reported Net Profit	7.2	6.5	1.6	4.0	7.0
Core Net Profit	9.2	6.5	1.6	4.0	7.0
GP margin	37.6%	38.3%	38.5%	37.4%	40.3%
PBT margin	15.7%	15.4%	6.2%	12.5%	16.0%
Effective tax rate	-31.1%	-29.3%	-34.8%	-29.0%	-29.0%
Revenue growth	6.7%	-8.9%	-37.8%	22.8%	35.2%
Gross profit growth	15.5%	-7.3%	-37.3%	19.2%	45.7%
PBT growth	-1.9%	-10.7%	-75.0%	147.5%	73.0%
Net profit growth	-6.5%	-9.7%	-75.4%	152.6%	73.0%
Core earnings growth	19.5%	-29.3%	-75.4%	152.6%	73.0%
EPS (sen)	1.7	1.6	0.4	1.0	1.7
FD EPS (sen)	1.3	1.1	0.4	0.7	1.2
P/E (x)	10.0	11.1	45.1	17.8	10.3
FD P/E (x)	13.9	15.3	49.5	23.4	14.3
DPS (sen)	1.00	1.50	0.35	0.75	1.00
Dividend payout	57.3%	95.1%	90.2%	76.5%	58.9%
Dividend Yield	5.7%	8.6%	2.0%	4.3%	5.7%
Net gearing / (cash)	-7.6%	-11.2%	-4.2%	-15.1%	-32.1%
ROE	11.6%	10.1%	2.6%	4.8%	7.2%
ROA	8.2%	8.3%	2.1%	4.0%	6.0%
BV/share (sen)	0.2	0.2	0.2	0.2	0.2
P/B (x)	1.2	1.1	1.2	1.0	0.9

Source: Company, JF Apex

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**JF APEX SECURITIES - RESEARCH RECOMMENDATION FRAMEWORK**
**STOCK RECOMMENDATIONS**

- BUY** : The stock's total returns\* are expected to exceed 10% within the next 12 months.
- HOLD** : The stock's total returns\* are expected to be within +10% to – 10% within the next 12 months.
- SELL** : The stock's total returns\* are expected to be below -10% within the next 12 months.
- TRADING BUY** : The stock's total returns\* are expected to exceed 10% within the next 3 months.
- TRADING SELL** : The stock's total returns\* are expected to be below -10% within the next 3 months.

**SECTOR RECOMMENDATIONS**

- OVERWEIGHT** : The industry as defined by the analyst is expected to exceed 10% within the next 12 months.
- MARKETWEIGHT** : The industry as defined by the analyst is expected to be within +10% to – 10% within the next 12 months.
- UNDERWEIGHT** : The industry as defined by the analyst, is expected to be below -10% within the next 12 months.

\*capital gain + dividend yield

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