

28 May 2018

Power Root Bhd FY18 Sunk by One-Offs

FY18 core PATAMI of RM23.8m (-32%) missed our estimate from weaker local and export sales and higher-than-expected expenses incurred from structural exercises. YTD dividend of 9.5 sen is within expectation. A stronger MYR environment may benefit domestic demand but could adversely impact export returns while the proposed bonus and warrants issue could improve stock liquidity. Downgrade to MARKET PERFORM with a lower TP of RM1.50 (from RM1.65).

FY18 below expectations. FY18 core net earnings of RM23.8m missed our estimates, making up 83% of our initial RM28.7m expectation. Weaker sales performance was aggravated by higher-than-expected operating expenses. An interim dividend of 0.5 sen was declared, amounting to total FY18 payments to 9.5 sen. This is closely within our 10.0 sen estimate.

YoY, 12M18 sales of RM424.6m (+6%) improved mainly due to growth in export numbers by 13%. Domestic demand, however, declined by 5% from lower consumer spending. While heavy marketing expenses were previously incurred in the Middle East, checks with management also indicated towards internal restructuring expenses and provisions in 2H18. It was also exposed to higher raw material costs as the group neared the end of its high-level hedged raw material inventories. During the year, the group was adversely affected by write-downs and impairments mainly in efforts to consolidate client portfolios. The group had also impaired its land in the UAE following the relocation of its potential construction site for its MENA plant. Minus this adjustment, group core EBITDA still registered a 40% decline. Core PATAMI ended at RM23.8m (-32%) following the above adjustments for write-offs and impairments.

QoQ, 4Q18 sales of RM80.6m fell by 30% as export demand decreased by 42%, possibly due to exporters seeking to reduce inventory in anticipation of the pending fasting season as c.70% of the group's exports are derived predominantly from Middle Eastern countries. Core LATAMI of RM1.6m is likely to have been led by the same abovementioned reasons.

Is the worst over? In terms of sales, domestic volume is expected to recover as management following through the zero-rated GST would reduce shelf prices. At the meantime, the stronger MYR should also benefit consumer spending. The opposite could be said on the export market. Still, we anticipate better volume growth to be helmed from this segment given stronger foreign spending potential. Cost-wise, better production expenses could be expected as raw material hedges should be at more favourable levels currently. However, the recent surge in operating expenses may be a cause of concern as despite being seen as one-off, may potentially lead to further spillage across the year.

Post results, we reduce our FY19E earnings by 6.5% mainly from toning down our sales assumptions and a potential spill over of restructuring expenses from 4Q18 into FY19. Additionally, we introduce our FY20E numbers. (refer to overleaf for details of the announced bonus issue and free warrants)

Downgrade to MARKET PERFORM with a lower TP of RM1.50 (from RM1.65, previously). The lower TP is in line with the weaker earnings assumptions on an unchanged 15.0x FY19E PER, currently in line with the stock's -1SD over its 3-year mean. While capital upside may appear limited, the stock has consistently provided solid dividend yields with FY18/FY19 expected to generate 6.6%/7.3% returns.

Risks to our call include: (i) lower-than-expected sales, (ii) prolonged exposure to high costs, and (iii) lower-than-expected dividend payments.

MARKET PERFORM

cum-Price/ex-Price: RM1.51/RM1.08

cum-TP/ex-TP: RM1.50/RM1.07

Expected Capital Gain: -RM0.01 -0.7%
Expected Divd. Yield: RM0.10 +6.6%
Expected Total Return: RM0.09 +5.9%

KLCI Index 1,797.40

Stock Information

Bloomberg Ticker	PWRT MK Equity
Bursa Code	7237
Listing Market	Main Market
Shariah Compliant	Yes
Shares Outstanding	323.6
Market Cap (RM m)	488.7
Par value per share (RM)	0.20
52-week range (H)	2.57
52-week range (L)	1.15
Free Float	44%
Beta	0.9
3-mth avg daily vol	752,320

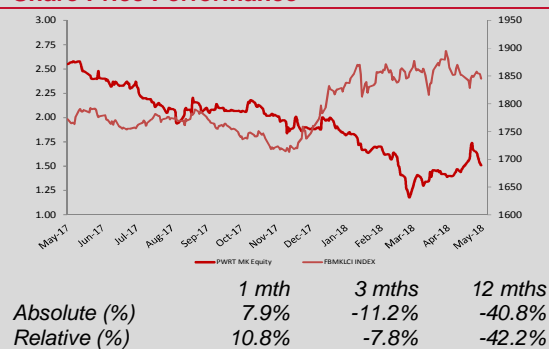
Major Shareholders

Say Swee How	20.3%
Fuei Boon Wong	18.9%
Chee Yen Low	17.1%

Summary Earnings Table

FY Dec (RM m)	2018A	2019E	2020E
Turnover	424.6	449.2	491.9
EBIT	10.1	39.5	51.4
PBT	10.6	38.8	49.8
Net Profit	10.1	35.1	42.2
Core PATAMI	23.8	32.9	42.2
Consensus (NP)	-	-	-
Earnings Revision	-	-6.5%	-
Core EPS (sen)	7.4	10.2	13.1
Core EPS growth (%)	-36.2%	38.2%	28.4%
NDPS (sen)	9.5	10.0	11.0
NTA per Share (RM)	0.65	0.65	0.67
Price to NTA (x)	2.3	2.3	2.3
PER (x)	20.5	14.9	11.6
Debt-to-Equity ratio (x)	0.0	0.4	0.4
Return on Asset (%)	2.7%	9.5%	11.9%
Return on Equity (%)	4.1%	15.7%	19.8%
Net Div. Yield (%)	6.3%	6.6%	7.3%

Share Price Performance



Clement Chua

clement.chua@kenanga.com.my

+603-2172 2645

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Other salient points

1 bonus; 1 free warrant for every 5 shares. The group has announced a proposed issuance of 1 bonus share and 1 free warrant for every 5 existing PWROOT shares at a later determined entitlement date and exercise price. We view the move as a positive on the improved liquidity provided to the stock which is currently tightly held by its founding members. Up to 71,236,337 new shares will be issued from each exercise. The funds raised from the warrants are intended to be utilised for working capital purposes and to repay its debt. Assuming full dilution from the above proposed exercises, the stock's share base would expand to 498.7m shares from 323.6m shares. This would lead to a fully diluted TP of RM1.11.

While the exercise price of the warrants has yet to be determined, based on an indicative exercise price of RM1.4685 per warrant, assuming a 20% conversion of the warrants within FY19E, earnings could improve slightly by c.RM160k from the repayment of debt. Our cum TP will remain unchanged at RM1.50 but a dilution from 20% of the warrants will translate to an ex-TP of RM1.21.

Results Highlights								
	4Q	3Q	QoQ	4Q	YoY	12M	12M	YoY
FYE Mar (RM'm)	FY18	FY18	Chg	FY17	Chg	FY18	FY17	Chg
Turnover	80.6	115.1	-30.0%	91.6	-12.0%	424.6	399.3	6.3%
Adj. EBITDA*	-0.7	13.0	-105.5%	15.8	-104.6%	30.9	51.7	-40.4%
EBIT	-10.1	6.6	-253.7%	13.5	-174.9%	10.1	54.1	-81.3%
PBT/(LBT)	-10.1	6.7	-250.8%	13.7	-174.0%	10.6	54.8	-80.6%
Taxation	0.5	-0.1	491.2%	-3.5	115.4%	-0.6	-7.5	92.3%
Net Profit/(Loss)	-9.6	6.4	-249.4%	10.2	-193.8%	10.1	47.2	-78.7%
Core PATAMI/(LATAMI)	-1.6	11.2	-114.7%	10.0	-116.4%	23.8	34.8	-31.6%
EPS (sen)	-0.5	3.4	-115.1%	2.5	-120.7%	7.0	13.4	-47.4%
DPS (sen)	0.5	2.5		4.0		9.5	11.5	
Adj. EBITDA margin	-0.9%	11.3%		17.2%		7.3%	13.0%	
EBIT margin	-12.5%	5.7%		14.7%		2.4%	13.5%	
PBT margin	-12.6%	5.8%		14.9%		2.5%	13.7%	
PATAMI margin	-2.0%	5.6%		11.2%		2.4%	11.8%	
Effective tax rate	5.3%	2.0%		25.2%		5.4%	13.8%	

Note:

* Adj. EBITDA and Core PATAMI are derived after adjusting for: (i) write offs / (reversals); (ii) foreign exchange losses / (gains) in the respective quarters; and (iii) reversal of bonus provision estimated at RM3.2m.

Source: Company, Kenanga Research

Revenue Segments								
	4Q	3Q	QoQ	4Q	YoY	12M	12M	YoY
FYE Mar (RM'm)	FY18	FY18	Chg	FY17	Chg	FY18	FY17	Chg
Domestic	46.0	55.6	-17.3%	45.2	1.6%	215.6	218.2	-1.2%
Export	34.6	59.5	-41.8%	46.4	-25.3%	209.0	181.1	15.4%
Total	80.6	115.1	-30.0%	91.6	-12.0%	424.6	399.3	6.3%

Source: Company, Kenanga Research

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Peer Comparison

NAME	Price	Mkt Cap	Hist.	PER (x)		Est. Div. Yld.	Historical ROE	P/BV (x)	Net Profit (RMm)			1Y Fwd Growth (%)	2Y Fwd Growth (%)	Target Price (RM)	Rating
	(25-May-18) (RM)	(RMm)		1Y Fwd	2Y Fwd				Hist.	1Y Fwd	2Y Fwd				
Consumer - Retail															
7-Eleven Malaysia Holdings Bhd	1.51	1,704.6	37.2	36.0	31.9	2.0%	91.6%	25.17	50.1	51.7	58.4	3.2%	12.9%	1.55	MP
Aeon Co (M) Bhd	2.42	3,397.7	32.4	28.5	25.0	1.7%	5.2%	1.73	106.1	119.1	135.9	12.2%	14.1%	2.60	OP
Amway (Malaysia) Holdings Bhd	7.65	1,257.5	23.9	23.2	18.9	3.7%	26.2%	5.88	52.6	54.1	66.7	2.8%	23.2%	8.50	MP
Hai-O Enterprise Bhd	5.27	1,533.2	25.7	18.2	15.0	4.1%	27.1%	5.35	59.4	83.8	101.6	41.0%	21.3%	6.00	OP
MyNews Holdings Bhd	1.55	1,057.3	44.0	37.7	32.3	0.7%	12.2%	4.43	24.0	28.0	32.7	16.6%	16.7%	1.25	UP
Padini Holdings Bhd	5.30	3,486.9	19.3	19.1	16.4	2.2%	27.6%	6.31	180.6	182.5	212.3	1.1%	16.3%	5.25	MP
Parkson Holdings Bhd	0.525	560.3	(4.7)	15.9	10.5	0.0%	-7.7%	0.23	(179.2)	35.8	54.6	-120.0%	52.5%	0.860	OP
Consumer - F&B															
Dutch Lady Milk Industries Bhd	69.90	4,473.6	35.9	31.3	27.5	3.1%	71.5%	43.01	124.6	142.9	162.8	14.7%	13.9%	66.15	MP
Fraser & Neave Holdings Bhd	36.90	13,525.4	33.9	36.6	32.1	1.6%	13.2%	6.34	398.6	369.1	421.0	-7.4%	14.1%	27.00	UP
Nestle (M) Bhd	147.00	34,471.5	53.4	48.1	41.2	2.0%	75.0%	53.87	645.8	716.7	837.6	11.0%	16.9%	114.30	UP
Power Root Bhd	1.51	488.7	20.5	14.9	11.6	6.6%	11.7%	2.34	23.8	32.9	42.2	38.2%	28.4%	1.50	MP
QL Resources Bhd	5.33	8,647.6	41.9	39.8	37.3	0.8%	11.6%	4.79	206.2	217.3	231.6	5.4%	6.6%	3.90	UP
Spritzer Bhd	2.30	482.9	17.6	15.1	14.2	2.6%	8.0%	1.11	23.8	31.8	33.9	33.9%	6.5%	2.50	MP
Consumer - Sin															
British American Tobacco Bhd	31.62	9,028.5	17.3	18.0	16.2	5.3%	128.5%	23.63	522.4	502.8	557.9	-3.7%	11.0%	31.70	MP
Carlsberg Brewery Malaysia Bhd	20.42	6,281.6	28.2	24.3	21.3	4.2%	61.6%	20.88	221.2	257.0	293.8	16.2%	14.3%	18.25	MP
Heineken Malaysia Bhd	23.24	7,020.8	26.0	22.0	19.9	4.5%	63.4%	19.47	270.1	319.0	352.1	18.1%	10.4%	23.30	OP

Source: Bloomberg, Kenanga Research

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Stock Ratings are defined as follows:**Stock Recommendations**

OUTPERFORM : A particular stock's Expected Total Return is MORE than 10%
MARKET PERFORM : A particular stock's Expected Total Return is WITHIN the range of -5% to 10%
UNDERPERFORM : A particular stock's Expected Total Return is LESS than -5%

Sector Recommendations***

OVERWEIGHT : A particular sector's Expected Total Return is MORE than 10%
NEUTRAL : A particular sector's Expected Total Return is WITHIN the range of -5% to 10%
UNDERWEIGHT : A particular sector's Expected Total Return is LESS than -5%

*****Sector recommendations are defined based on market capitalisation weighted average expected total return for stocks under our coverage.**

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Published and printed by:

KENANGA INVESTMENT BANK BERHAD (15678-H)

Level 12, Kenanga Tower, 237, Jalan Tun Razak, 50400 Kuala Lumpur, Malaysia
Telephone: (603) 2172 0880 Website: www.kenanga.com.my E-mail: research@kenanga.com.my

This report is accessible at www.bursamids.com too.



Chan Ken Yew
Head of Research

