

28 February 2020

Hock Seng Lee Bhd

Riding On Sarawak Infrastructure Wave

By Goh Yin Foo | gohfy@kenanga.com.my

FY19 CNP of RM55.2m (+3% YoY) fell short of expectations, accounting for 84%/91% of our/consensus estimates, mainly due to slower progress billings of construction works and marginally weaker property contributions. HSL plans to bid for the slew of infrastructure projects coming up in Sarawak to add to its existing unbilled order-book of RM2.2b. A direct Sarawak construction proxy, we are upgrading the stock to OUTPERFORM with a higher SoP-derived target price of RM1.77 (implied P/E of 15x on FY20 earnings).

Missed expectations. FY19 CNP of RM55.2m (+3% YoY) is weaker-than-expected, representing 84%/91% of our/consensus estimates. This could be mainly due to: (i) timing delays in recognition of construction works and marginal dip in margins. Consequently, the construction segment posted pretax profit of RM46.6m (+7%) and margin of 7.9% (versus 8.3% in FY18), and (ii) a drop in property earnings, which came in at RM27.9m (-5%) on the back of revenue of RM92.3m (+10%).

Results' highlight. 4QFY19 CNP came in at RM10.1m (-31% QoQ and -12% YoY) as pretax profit contributions from construction (of RM7.7m) and property development (of RM6.1m) were down QoQ. The company has declared a final DPS of 1.4 sen, taking full-year dividends to 2.4 sen (which translates to dividend yield of 1.9%). Balance sheet strength remains strong with net cash of RM81.3m (or approximately 15.0 sen per share) as of end-Dec 2019.

Outlook. Unbilled construction order-book currently stands at RM2.2b (or 3.7 times of last year's construction revenue). There will be opportunities for HSL to win more construction jobs as the Sarawak state plans to award sizeable infrastructure projects on road and water works going forward. Interestingly, perhaps reflecting management's business confidence, in the press statement released in conjunction with the results announcement, HSL has mentioned it plans to retain some capital in anticipation of major new project procurement going forward. We have pencilled in new contract wins of RM800m this year.

Earnings revisions. Post results, we have revised FY20E earnings to RM65m (-17%) and introduce FY21E earnings at RM79m as we tweak our assumptions on the timing of income recognition for its construction works and margins.

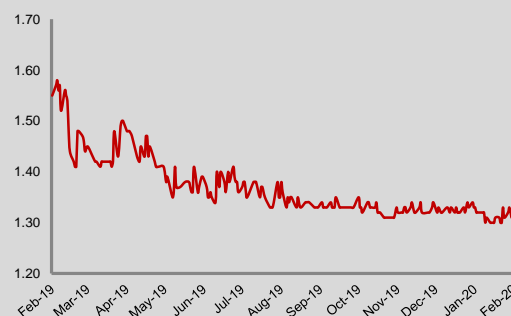
Upgrade to OUTPERFORM with a higher Target Price of RM1.77. Our TP – which is derived from SoP-valuation method (see table overleaf) – implies an underlying FY20E P/E multiple of 15x. The stock – which is currently trading near its eight-year low – is a proxy to the rising construction activities in Sarawak, offering potential total returns of 40%.

Risks to our call include lower-than-expected job wins, delayed construction billings progress and lower-than-expected construction margins.

OUTPERFORM ↑

Price : **RM1.28**
Target Price : **RM1.77** ↑

Share Price Performance



KLCI	1,505.59
YTD KLCI chg	-5.2%
YTD stock price chg	-3.8%

Stock Information

Shariah Compliant	Yes
Bloomberg Ticker	HSL MK EQUITY
Market Cap (RM m)	703.4
Shares Outstanding	549.5
52-week range (H)	1.59
52-week range (L)	1.27
3-mth avg daily vol:	152,970
Free Float	11%
Beta	0.4

Major Shareholders

Hock Seng Lee Enterprise Sdn Bhd	58.5%
Skim Amanah Saham Bumiputera	9.6%
Employees Provident Fund Board	4.5%

Summary Earnings Table

FYE Dec (RM m)	2019A	2020E	2021E
Turnover	684	833	968
EBIT	71	85	102
PBT	74	87	105
Net Profit	55	65	79
Core PATAMI	55	65	79
Consensus (NP)	N.A.	70	77
Earnings Revision	N.A.	-17%	N.A.
Core EPS (sen)	10	11.9	14.3
Core EPS growth (%)	2	0.2	0.2
NDPS (sen)	2.4	2.4	2.9
NTA per Share (RM)	1.5	1.6	1.6
PER (x)	15.8	10.8	9.0
Price to NTA (x)	0.9	0.9	0.9
Debt-to-Equity ratio (x)	0.07	0.05	0.05
Return on Asset (%)	4.9	5.7	5.7
Return on Equity (%)	8.0	8.8	8.8
Net Div. Yield (%)	1.9	1.9	2.2

28 February 2020

Result Highlight

FYE Dec (RM m)	4Q19	3Q19	QoQ	4Q18	YoY	FY19	FY18	YoY
Turnover	187.6	173.8	8%	151.1	24%	683.6	610.4	12%
EBIT	13.6	18.7	-28%	14.9	-9%	70.8	69.9	1%
Net interest exp/inc	0.1	1.1	-88%	0.3	-57%	3.3	2.3	43%
Pretax profit	13.7	19.8	-31%	15.3	-10%	74.1	72.2	3%
Taxation	(3.6)	(5.3)	-32%	(3.7)	-4%	(18.8)	(18.3)	3%
Profit after tax	10.1	14.6	-30%	11.6	-12%	55.3	53.8	3%
Minority interest	0.0	0.0	-	0.0	-	(0.1)	(0.1)	-11%
PATAMI	10.1	14.6	-31%	11.5	-12%	55.2	53.8	3%
Core PATAMI	10.1	14.6	-31%	11.5	-12%	55.2	53.8	3%
DPS (sen)	1.4	0.0		1.4		2.4	2.4	
EBIT margin	7.2%	10.8%		9.9%		10.4%	11.4%	
Pretax margin	7.3%	11.4%		10.1%		10.8%	11.8%	
EPS (sen)	1.8	2.7		2.1		10.0	9.8	
Core EPS(sen)	1.8	2.7		2.1		10.0	9.8	
Effective tax	26.0%	26.5%		24.2%		25.4%	25.4%	

Source: Company, Kenanga Research

Segmental Breakdown

FYE Dec (RM m)	4Q19	3Q19	QoQ	4Q18	YoY	FY19	FY18	YoY
Revenue								
Construction	164.7	149.4	10%	123.2	34%	591.1	526.4	12%
Property development	22.8	24.5	-7%	27.9	-18%	92.3	84.0	10%
Others	0.2	0.0	n.m.	0.0	n.m.	0.2	0.0	n.m.
Total	187.6	173.8	8%	151.1	24%	683.6	610.4	12%
Pretax Profit								
Construction	7.7	11.7	-34%	5.9	31%	46.6	43.6	7%
Property development	6.1	8.2	-26%	9.2	-34%	27.9	29.5	-5%
Others	(0.1)	(0.1)	45%	0.1	-183%	(0.4)	(1.0)	-57%
Total	13.7	19.8	-31%	15.3	-10%	74.1	72.2	3%
Pretax Profit Margin								
Construction	4.7%	7.8%		4.8%		7.9%	8.3%	
Property development	26.6%	33.5%		33.1%		30.3%	35.1%	
Total	7%	11.4%		10.1%		10.8%	11.8%	

Source: Company, Kenanga Research

28 February 2020

Sum-of-parts valuation		
Segment	Value (RMm)	Valuation Basis
Construction	469.7	P/E of 10.7x (at +1SD above 3-year mean)
Property development	357.8	P/BV of 0.94x (-1SD below mean) with inventory adjustment
Others	81.2	P/BV of 0.94x (-1SD below mean)
Net cash / (debt) at holding company	65.9	Per 2018 Annual Report
Aggregate valuation	974.6	
No of shares (m)	549.5	
RNAV per share (RM)	1.77	

Source: Company, Kenanga Research

28 February 2020

Peer Comparison

Name	Last Price (RM)	Market Cap (RM'm)	Shariah Compliant	Current FYE	Revenue Growth		Core Earnings Growth		PER (x) - Core Earnings			PBV (x)		ROE (%)	Net Div Yld (%)	Target Price (RM)	Rating
					1-Yr. Fwd.	2-Yr. Fwd.	1-Yr. Fwd.	2-Yr. Fwd.	Hist.	1-Yr. Fwd.	2-Yr. Fwd.	Hist.	1-Yr. Fwd.	1-Yr. Fwd.			
STOCKS UNDER COVERAGE																	
GAMUDA BHD	3.61	9,071.2	Y	07/2020	33.5%	9.7%	-25.2%	-19.3%	11.1	14.8	18.4	1.1	1.1	7.3%	3.3%	4.70	OP
GEORGE KENT (MALAYSIA) BHD	0.860	458.8	Y	01/2020	-22.2%	10.1%	-43.0%	18.0%	6.1	10.7	9.1	1.0	0.9	9.0%	4.7%	0.970	MP
HOCK SENG LEE BERHAD	1.28	703.4	Y	12/2020	21.8%	16.2%	18.2%	21.5%	15.8	10.8	9.0	0.9	0.8	8.8%	1.9%	1.77	OP
IJM CORP BHD	1.99	7,222.6	Y	03/2020	4.9%	8.6%	-32.6%	13.9%	17.3	25.6	22.5	0.7	0.7	2.8%	1.5%	2.15	MP
KERJAYA PROSPEK GROUP BHD	1.27	1,563.7	Y	12/2020	33.7%	18.8%	12.6%	20.6%	10.4	9.3	7.7	1.6	1.4	16.4%	N.A.	1.50	OP
KIMLUN CORP BHD	1.09	370.4	Y	12/2019	-9.3%	-1.5%	11.5%	-4.0%	6.1	5.4	5.7	0.5	0.5	9.7%	4.3%	1.60	OP
MITRAJAYA HOLDINGS BHD	0.255	224.7	Y	12/2019	-4.8%	-52.3%	-46.2%	-130.0%	N.A.	N.A.	N.A.	0.3	0.4	-17.0%	0.0%	0.110	UP
MUHIBBAH ENGINEERING (M) BHD	1.66	802.5	Y	12/2019	9.9%	-3.4%	-21.4%	28.5%	5.5	7.0	5.5	0.7	0.7	9.8%	3.1%	2.35	OP
SUNWAY CONSTRUCTION GROUP BHD	1.86	2,398.2	Y	12/2020	42.9%	3.9%	30.4%	4.0%	18.6	14.3	13.8	4.0	3.7	26.6%	3.9%	2.15	OP
WCT HOLDINGS BHD	0.685	961.4	Y	12/2020	0.8%	-0.2%	-29.6%	4.5%	7.7	11.0	10.5	0.3	0.3	2.7%	0.0%	0.750	MP
Simple Average					11.1%	1.0%	-12.5%	-4.2%	10.6	12.1	11.3	1.1	1.0	7.9%	2.5%		
CONSENSUS ESTIMATES																	
AHMAD ZAKI RESOURCES BERHAD	0.325	193.8	Y	06/2020	N.A.	N.A.	N.A.	N.A.	13.2	N.A.	N.A.	0.4	N.A.	N.A.	N.A.	N.A.	SELL
BINA PURI HOLDINGS BHD	0.080	30.5	Y	06/2020	N.A.	N.A.	N.A.	N.A.	N.A.	N.A.	N.A.	0.1	N.A.	N.A.	N.A.	N.A.	SELL
GABUNGAN AQRS BHD	1.05	518.1	Y	12/2019	-9.3%	58.2%	-17.7%	53.5%	8.5	10.3	0.0	1.0	1.1	11.3%	4.0%	1.62	BUY
GADANG HOLDINGS BHD	0.595	433.2	Y	05/2020	3.8%	0.1%	33.9%	14.2%	9.8	7.3	0.0	0.5	0.5	7.6%	1.3%	0.687	NEUTRAL
JAKS RESOURCES BHD	1.39	905.1	Y	12/2019	80.6%	-50.3%	683.9%	-42.4%	59.0	7.5	0.0	0.9	0.9	15.0%	0.0%	1.20	NEUTRAL
MUDAJAYA GROUP BHD	0.455	268.4	N	12/2019	N.A.	N.A.	N.A.	N.A.	N.A.	N.A.	N.A.	1.8	N.A.	N.A.	N.A.	N.A.	SELL
PINTARAS JAYA BHD	3.02	500.9	Y	06/2020	41.6%	2.6%	107.5%	3.3%	19.2	9.2	0.1	1.5	1.4	16.4%	6.6%	3.88	NEUTRAL
PESONA METRO HOLDINGS	0.200	139.0	Y	12/2020	7.1%	-9.7%	111.7%	-10.7%	12.6	5.9	0.0	0.7	N.A.	11.4%	5.0%	0.290	BUY
PROTASCO BHD	0.355	172.2	Y	12/2020	3.4%	11.7%	97.8%	2.5%	28.7	14.5	0.0	0.5	0.5	3.6%	3.9%	0.315	NEUTRAL
TRC SYNERGY BHD	0.390	187.4	Y	12/2020	12.1%	4.6%	55.9%	27.2%	9.5	6.1	0.0	0.5	N.A.	9.6%	5.1%	0.500	NEUTRAL

Source: Bloomberg, Kenanga Research

28 February 2020

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.**

This document has been prepared for general circulation based on information obtained from sources believed to be reliable but we do not make any representations as to its accuracy or completeness. Any recommendation contained in this document does not have regard to the specific investment objectives, financial situation and the particular needs of any specific person who may read this document. This document is for the information of addressees only and is not to be taken in substitution for the exercise of judgement by addressees. Kenanga Investment Bank Berhad accepts no liability whatsoever for any direct or consequential loss arising from any use of this document or any solicitations of an offer to buy or sell any securities. Kenanga Investment Bank Berhad and its associates, their directors, and/or employees may have positions in, and may effect transactions in securities mentioned herein from time to time in the open market or otherwise, and may receive brokerage fees or act as principal or agent in dealings with respect to these companies.

Published and printed by:

KENANGA INVESTMENT BANK BERHAD (15678-H)

Level 17, 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

