Malaysia

MARKET DATELINE ● PP 7767/09/2010(025354)

RHB Research Institute Sdn Bhd
A member of the RHB Banking Group
Company No: 233327 -M

Corporate Highlights

Visit Note

20 January 2010

M'sian Resources Corp

Property The Key Driver Going Forward

Share Price	:	RM1.56 (cum-rights)
Fair Value	:	RM1.66 (ex-rights)
Recom	:	**Trading Buy** (Maintained)

Table 1 : Investment Statistics (MRCB; Code: 1651) **Bloomberg: MRC MK**

FYE Dec	Turnover (RMm)	Net Profit# (RMm)	EPS# (sen)	Growth (%)	PER (x)	C.EPS* (sen)	P/CF (x)	P/NTA (x)	ROE (%)	Net Gearing (%)	GDY (%)
2008	788.6	(56.6)	(6.2)	nm	22.6	-	(6.7)	1.8	(8.9)	0.6	0.0
2009f	1,003.8	32.8	3.6	nm	43.2	3.0	25.1	1.8	4.9	0.6	0.8
2010f	1,276.5	96.4	7.1	96.2	22.0	6.0	24.8	1.6	12.6	Net cash	0.8
2011f	1,325.6	104.1	7.6	8.0	20.4	7.0	24.3	1.5	12.0	Net cash	0.8

Main Market Listing /Non-Trustee Stock/Syariah-Approved Stock By The SC *#Excluding EI* ** Consensus Based On IBES*

- **Federal land.** MRCB re-confirmed that it is keen on the Federal land parcels but acknowledged that "it is up to the Government to decide on which entity it will award the land to", and at this point, "the Government remains very tight-lipped". We maintain our view that MRCB's proposed 1-for-2 rights issue at RM1.12 per right share (going ex on 28 Jan 2010) to raise up to RM508.3m gross proceeds is a prelude to these land deals.
- **Property turnover to overtake construction in FY12/11.** MRCB expects its property turnover to increase from 30-40% of group turnover in FY12/09-10, to in excess of 50% by FY12/11, with the construction work on several components of KL Sentral gaining momentum. We believe the "natural progression" or "transformation" of MRCB from a largely construction-dependent group to a largely property-dependent group (whether this is intended or not) will be made easier with new property projects on the Federal land.
- **Forecasts.** FY12/10-11 net profit forecasts are raised by 31-32%, having reflected interest savings arising from the rights proceeds. However, FY12/10-11 EPS are reduced by 12-13%, having reflected dilution from an enlarged share base.
- **Risks.** The risks include: (1) New construction contracts secured in FY12/10 coming in below our target of RM500m p.a.; and (2) Rising input costs.
- **Sector's best case priced in.** On the big picture, while a rosy picture for the construction sector has been priced in based on the current rich valuations, it is still far from being a reality, especially so after a slew of negative developments including reduced gross development expenditure in 2010, Dong's devaluation, the Dubai credit crisis and the seemingly declining dominance of the big boys in large-scale projects. We believe the market has under-appreciated two other key risks as well, namely: (1) Possible delays in project implementation; and (2) Sub-par margins due to stiff competition.
- **Maintain Trading Buy.** However, MRCB has a new irresistible angle on its property business, i.e. the possibility of bagging prime Federal land parcels in KL. We are rationalising down MRCB's indicative fair value by 3% from RM1.71 to RM1.66 (ex-rights) based on "sum of parts", having reflected: (1) The dilution from the rights issue; and (2) The change in our valuation methodology for KL Sentral from PER to DCF to reflect the more entrenched recovery in the property sector in general.

Issued Capital (m shares)	907.6
Market Cap(RMm)	1,415.9
Daily Trading Vol (m shs)	11.4
52wk Price Range (RM)	0.74-1.74
Major Shareholders:	**(%)**
EPF	30.6

FYE Dec	FY09	FY10	FY11
EPS Revision (%)	-	-12	-13
Var to Cons (%)	+20	+18	+9

Share Price Chart

Relative Performance To FBM KLCI

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Property The Key Driver Going Forward

- **Highlights.** The key highlights from MRCB's presentation during RHB's GLC Day on 19 Jan 2010 are:
  1. MRCB re-confirmed that it is keen on the Federal land parcels but acknowledged that the Government has yet to formally make a decision on the award of the land; and
  2. MRCB sees itself transforming from a largely construction-dependent group to a largely property-dependent group by FY12/11.

- **Federal land.** MRCB re-confirmed that it is keen on the Federal land parcels but acknowledged that "it is up to the Government to decide on which entity it will award the land to", and at this point, "the Government remains very tight-lipped". Recall, it was reported that MRCB is close to securing Federal land parcels namely: (1) 150 acres in Jalan Cochrane (worth RM817m based on the going rate of RM100-150 psf); and (2) 20-30 acres in Jalan Ampang Hilir near the Jalan U-Thant area (worth RM272m based on the going rate of RM250 psf). During an analysts' briefing in Nov 09, MRCB actually hinted that there could be more, including some small pockets of federal land in the KLCC area. We maintain our view that MRCB's proposed 1-for-2 rights issue at RM1.12 per right share (going ex on 28 Jan 2010) to raise up to RM508.3m gross proceeds is a prelude to these land deals.

- We believe that these potential land deals may be instrumental to EPF, the largest shareholder of MRCB with a 30.6% stake, agreeing to providing an irrevocable undertaking to subscibe in full its entitlement to the rights issue (that will cost EPF RM156.7m). However, MRCB said that it has won the support from EPF based on, among others, "its ability to knock on the Government's door as a GLC". Moreover, as MRCB has in recent years completed its restructuring and streamlining initiatives, putting itself in a stronger footing to take on new projects, the rights proceeds will definitely come in handy "as and when opportunities present themselves".

- Assuming MRCB is to secure the Federal land parcels, the development concept is likely to be "integrated" with a combination of commercial and residential products. The GDV of the land parcels depends a lot on the land prices asked by the Government. The higher the land price, the higher the GDV MRCB will expect to extract from the land based on a higher plot ratio.

- **Property turnover to overtake construction in FY12/11.** MRCB expects its property turnover to increase from 30-40% of group turnover in FY12/09-10, to in excess of 50% by FY12/11, with the construction work on several components of KL Sentral gaining momentum including:
  1. The RM900m *348 Sentral* office and service apartment on Lot 348;
  2. The RM404m CIMB tower on Lot A;
  3. The RM1,434m MRCB – Pelaburan Hartanah Bumiputera retail mall and office tower on Parcels A & B of Lot G;
  4. The RM859m MRCB – Aseana hotel and office towers on Parcels C & D of Lot G; and
  5. The RM602m low-rise Business Park Sentral.

  We believe the "natural progression" or "transformation" of MRCB from a largely construction-dependent group to a largely property-dependent group (whether this is intended or not) will be made easier with new property projects on the Federal land.

- **Forecasts.** FY12/10-11 net profit forecasts are raised by 31-32%, having reflected interest savings arising from the rights proceeds. However, FY12/10-11 EPS are reduced by 12-13%, having reflected dilution from an enlarged share base.

- **Risks.** The risks include: (1) New construction contracts secured in FY12/10 coming in below our target of RM500m p.a.; and (2) Rising input costs.

- **Sector's best case priced in.** On the big picture, the market appears to have continued to paint in its mind a rosy picture for the sector, i.e. a sustained flow of large-scale projects going forward that will help replenishing or even growing orderbooks of key construction players, putting their earnings back on the growth path again. We believe while this rosy picture has been priced in, it is still far from being a reality, especially so after a slew of negative developments including reduced gross development expenditure in 2010, Dong's devaluation, the Dubai credit crisis and the seemingly declining dominance of the big boys in large-scale projects with low-key small player Gadang Holdings emerging the winner for the Earthwork Package 2 worth RM291.2m of the new permanent LCCT project recently. We believe the market has under-appreciated two other key risks as well, namely: (1) Possible delays in project implementation; and (2) Sub-par margins due to stiff competition.

- **Valuation and recommendation.** However, MRCB has a new irresistible angle on its property business, i.e. the possibility of bagging two prime Federal land parcels in KL, namely: (1) 150 acres in Jalan Cochrane; and (2) 20-30 acres in Jalan Ampang Hilir near the Jalan U-Thant area. We estimate that the land parcels could enhance MRCB's valuation by RM624m or 46sen per share (ex-rights). We are rationalising down MRCB's indicative fair value by 3% from RM1.71 to RM1.66 (ex-rights) based on "sum of parts" (see Table 4), having reflected: (1) The dilution from the rights issue; and (2) The change in our valuation methodology for KL Sentral from PER to DCF to reflect the more entrenched recovery in the property sector in general. Maintain **Trading Buy**.

Table 2: Outstanding Construction Orderbook

Project	Value (RMm)
External	
EDL	542
Bus terminal in Penang Sentral	300
Permai Psychiatric Hospital, Johor	295
Various transmission jobs	158
Upgrading of KL Sentral's road network	119
Various environmental projects	111
Rehabilitation of *Gaya Bangsar*	90
Total	**1,615**
Internal	
Building work: Lot A	214
Building work: Lot 348	351
Building work: Lot G	664
Total	**1,229**

Source: Company, RHBRI

Table 3: Outstanding KL Sentral Projects

Project	Location	GDV (RMm)	Project Period
1. CIMB tower	Lot A	404	2009-2011 (Under construction)
2. MRCB-KFH-Quill office suites	Lot B	1,015	2010-2013
3. MRCB-CMY's St Regis Hotel & Residences	Lot C	1,500	2011-2014
4. MRCB-CapitaLand-Quill condos	Lot D	1,200	2010-2013
5. Low-rise Business Park Sentral	Lot E	602	2009-2011 (Under construction)
6. MRCB-Pelaburan Hartanah Bumiputera retail mall & office tower	Parcels A&B, Lot G	1,434	2009-2012 (Under construction)
7. MRCB-Aseana hotel & office towers	Parcels C&D, Lot G	859	2009-2012 (Under construction)
8. MRCB-Gapurna office & service apartments (*348 Sentral*)	Lot 348	900	2009-2012 (Under construction)
9. Six office towers	Lot F	2,300	2012-2016
Total		**10,214**	

Source: Company, RHBRI

Table 4: Valuation Based On "Sum Of Parts"				
Project/Business	**RMm**	**RM/share**	**Methodology**	**Key Assumptions**
Construction/Property ex-KL Sentral	635.7	0.47	PER	10x FY12/10 net profit, in line with our benchmark 1-year forward target PER for the construction sector of 10-14x.
KL Sentral	799.2	0.59	DCF	Remaining GDV of RM10.2bn, project life of seven years, PBT margin of of 15% (lower than 30% for similar developments to reflect JV partners' shares of profits on certain projects), tax rate of 25% and the benchmark discount rate of 10% for property projects.
Potential prime Federal land in KL (assume 70%)	624.4	0.46	DCF	Estimated GDV of RM5.7bn, project life of seven years, PBT margin of 30%, tax rate of 25% and the benchmark discount rate of 10% for property projects.
DUKE (30%)	74.8	0.05	DCF	Project IRR of 15%, equity IRR of 38.8% (debt-equity ratio of 70:30 and average before-tax funding cost of 6.5%), and discount rate that is equivalent to MRCB's cost of equity of 22.4%. DUKE in its entirety carries an NPV of RM249.4m. MRCB's 30% share is therefore RM74.8m.
EDL (100%)	120.5	0.09	DCF	Project IRR of 13%, equity IRR of 32.1% (debt-equity ratio of 70:30 and average before-tax funding cost of 6.5%), and discount rate that is equivalent to MRCB's cost of equity of 22.4%.
Total	**2254.6**	**1.66**		

Table 5: Earnings Forecasts				
FYE Dec	**FY08a**	**FY09F**	**FY10F**	**FY11F**
Turnover	788.6	1,003.8	1,276.5	1,325.6
Turnover growth (%)	-12.7	27.3	27.2	3.9
EBITDA	53.6	68.5	125.9	130.1
EBITDA margin (%)	6.8	6.8	9.9	9.8
Depreciation	-8.5	-8.5	-8.5	-8.5
Net Interest	-72.1	-23.2	11.2	17.3
Associates	-15.1	0.0	0.0	0.0
EI	0.0	0.0	0.0	0.0
Pretax Profit	-42.2	36.8	128.6	138.9
Tax	-19.6	-4.0	-32.1	-34.7
PAT	-61.7	32.8	96.4	104.1
Minorities	5.1	0.0	0.0	0.0
Net Profit	-56.6	32.8	96.4	104.1

Source: Company data, RHBRI estimates

Table 6: Forecast Assumptions			
FYE Dec	**FY09F**	**FY10F**	**FY11F**
Construction EBIT margin (%)	4.9	7.5	7.6
New orderbook secured (RMm)	239*	500	1,000

**Actual*

Chart 1 : MRCB Technical View Point

- MRCB lost its upward momentum after crossing successfully to above the RM1.33 important level in Jun and began forming a Major Wedge Formation on the chart.
- The stock broke out from the wedge in early Jan 2010 near RM1.33 and soared beyond the crucial resistance of RM1.60, before touching a high of RM1.80 in recent trading.
- However, the subsequent steep pullback has pressed it back to below RM1.60 of late.
- Critically, investors should expect a retracement to the support near RM1.33, if it fails to rebound quickly to above RM1.60 level in the near term. A higher resistance is at RM1.90.

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Stock Ratings

Outperform = The stock return is expected to exceed the FBM KLCI benchmark by greater than five percentage points over the next 6-12 months.

Trading Buy = Short-term positive development on the stock that could lead to a re-rating in the share price and translate into an absolute return of 15% or more over a period of three months, but fundamentals are not strong enough to warrant an Outperform call. It is generally for investors who are willing to take on higher risks.

Market Perform = The stock return is expected to be in line with the FBM KLCI benchmark (+/- five percentage points) over the next 6-12 months.

Underperform = The stock return is expected to underperform the FBM KLCI benchmark by more than five percentage points over the next 6-12 months.

Industry/Sector Ratings

Overweight = Industry expected to outperform the FBM KLCI benchmark, weighted by market capitalisation, over the next 6-12 months.

Neutral = Industry expected to perform in line with the FBM KLCI benchmark, weighted by market capitalisation, over the next 6-12 months.

Underweight = Industry expected to underperform the FBM KLCI benchmark, weighted by market capitalisation, over the next 6-12 months.

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