

9 October 2018

Malaysia

EQUITIES

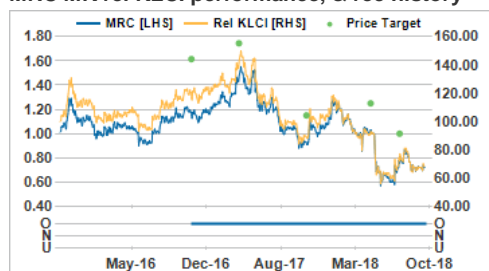
MRC MK Outperform
Price (at 09:27, 09 Oct 2018 GMT) RM0.73

Valuation	RM	0.89-1.05
- Sum of Parts		
12-month target	RM	1.00
Upside/Downside	%	+37.9
12-month TSR	%	+39.9
Volatility Index		High
GICS sector		Capital Goods
Market cap	RMm	3,186
Market cap	US\$m	762
30-day avg turnover	US\$m	2.9
Number shares on issue	m	4,395

Investment fundamentals

Year end 31 Dec		2017A	2018E	2019E	2020E
Revenue	m	2,823.7	1,676.3	1,718.9	2,188.3
EBITDA	m	319.6	264.1	275.4	342.9
EBIT	m	246.5	206.4	212.3	260.8
Reported profit	m	167.6	131.1	150.7	174.5
Adjusted profit	m	101.2	131.1	150.7	174.5
EPS rep	sen	5.9	3.0	3.4	4.0
EPS rep growth	%	-50.7	-49.0	14.9	15.7
EPS adj	sen	3.6	3.0	3.4	4.0
EPS adj growth	%	4.5	-17.4	14.9	15.7
PER rep	x	12.4	24.3	21.1	18.2
PER adj	x	20.0	24.3	21.1	18.2
Total DPS	sen	1.8	1.3	1.5	1.8
Total DPS growth	%	-27.1	-28.6	20.0	16.7
Total div yield	%	2.4	1.7	2.1	2.4
ROA	%	2.8	2.2	2.4	2.7
ROE	%	2.6	2.7	3.0	3.4
EV/EBITDA	x	15.6	18.9	17.3	13.8
Net debt/equity	%	52.8	37.5	40.2	47.0
P/BV	x	0.7	0.6	0.6	0.6

MRC MK rel KLCI performance, & rec history



Note: Recommendation timeline - if not a continuous line, then there was no Macquarie coverage at the time or there was an embargo period.

Source: FactSet, Macquarie Research, October 2018
(all figures in MYR unless noted)

Analysts

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MRCB

Ending the year on a high note

Key points

- ▶ We are maintaining our TP and rating of RM1.00 and Outperform, respectively.
- ▶ The EDL divestment is expected to be concluded in the coming weeks.
- ▶ We believe MRCB is a strong contender for the MRT2 re-tendering.

Event

- We maintain our Outperform rating on MRCB following our recent engagement with management. Despite maintaining our TP at RM1.00, we have adjusted our FY18–20E earnings estimates by -4%/-17%/-17%, respectively. The change in earnings has impacted the fair value rather insignificantly, as a majority of the earnings revision comes from the construction division, which makes up only 18% of MRCB's valuation.

Impact

- **EDL sale to be concluded in the coming weeks ahead of the Budget 2019 announcement.** According to management, the negotiations with MoF have reached the final stages. We expect the government to compensate MRCB at face value for EDL's outstanding bonds plus the total equity injections that MRCB has given to EDL – as such, the divestment value could reach up to RM1.3bn, with, at best, zero profit to be recognised by MRCB. More important, we believe, this will lighten MRCB's balance sheet and reduce its gross debt by c.RM1.1bn.
- **Bukit Jalil land sale to EPF is under final review by Ministry of Economic Affairs.** According to management, the RM1.1bn land sale to EPF is currently pending the approval of the Ministry of Economic Affairs. Management added that MRCB has met all of the condition precedents (CPs) of the sale contract, and they believe there should not be any further hiccups for the deal to conclude by year-end. Separately, management is looking to conclude the sale of Celcom Tower (with completion end-FY18E; 100% pre-tenanted) to the highest bidder over the next six months. Based on our estimates, Celcom Tower could fetch a value of at least RM358mn.
- **MRT2 contract slashed; potential bidder for the tunnel package.** Since there is no quantum guided by the government on MRCB's [MRT2 contract reduction](#), we are cutting MRCB's MRT2 contract value by 23%, in line with the total cost cut of the MRT2 above-ground package. After seamlessly executing the [LRT3 cost-cutting measures](#), we believe MRCB could be one of the strong contenders to bid for the remaining MRT2 tunnel package, after Gamuda-MMC's role was [terminated](#) by the government.

Earnings and target price revision

- TP maintained while FY18–20E earnings revised by -4%/-17%/-17%, respectively.

Price catalyst

- 12-month price target: RM1.00 based on a Sum of Parts methodology.
- Catalyst: Divestments of EDL and Bukit Jalil land.

Action and recommendation

- Outperform rating is reiterated.

Analysis

The changes to our earnings estimates mainly come from the decelerating recognition of the LRT3 project in FY18E, coupled with the cut in estimates from the property division following the weaker-than-expected results in 2Q18. We believe our FY19/20 estimates are behind consensus, mainly due to the difference in assumptions for the new LRT3 contract as well as the pace of the earnings recognition.

Given that MRCB will be busy closing the divestment deals before FY18E draws its curtain, we believe there will be no new order wins for the construction division in the remaining months of FY18E. As such, we forecast MRCB to end FY18E with zero order wins. We assume order wins of RM1bn in FY19–21E. We are also revising MRCB's MRT2 contract to RM465mn from RM604mn to account for the new cost-reduction measures.

Previously, we assumed EDL to be divested at the face value of the bonds plus the interest costs in FY18E. In our new assumptions we have added the equity injections from MRCB to EDL as part of the compensation, per guidance by MRCB. As such, we are increasing the EDL sale value to c.RM1.3bn from RM1.1bn.

Fig 1 MRCB's valuation – 82% Property; 18% Construction; 0% Others

Business Division	Valuation Method	Stake	Value (RM 'mil)	Old Value (RM 'mil)	Change (%)
Property Development	RNAV at 50% discount to RNAV	Mixed	901	926	-3%
Investment Properties	12m forward NOI @ cap rate	Mixed	681	681	0%
Construction	10x PER on FY19E PAT	100%	309	424	-27%
Construction PDP fees	DCF @ 6.8% WACC	Mixed	165	165	0%
Parking Services	12m forward NOI @ cap rate	100%	205	205	0%
Security Services	8x PER on FY18E PAT	100%	11	11	0%
Concession	DCF @ 6.8% WACC	100%	0	0	n/m
MRCB-Quill REIT	Market Value	33%	397	397	0%
REIT Manager	12x PER multiple of FY19E PAT	41%	30	30	0%
Gross SOTP			2,700	2,839	-5%
(+) Cash proceeds from Bukit Jalil land	Sold 61 acres of land at RM430psf		1,141	1,141	0%
(+) Cash proceeds from Kia Peng land	Sold 1.9 acres of land at RM3,973psf		323	323	n/m
(+) Cash proceeds from Semarak City land	Sold 70% stake of the Semarak City land		100	100	n/m
(+) Sale of EDL	Assume at par value of Sukuks + FY18 interest costs		1,289	1,139	13%
(-) Estd. net Debt as at end of FY18	Net debt excluding the concession, investment properties & property development debts		-1,146	-1,172	-2%
(+) Cash from warrants B conversion	Exercise price at RM1.25		0	0	n/m
SOTP			4,408	4,371	1%
Number of shares (mil)			4,387	4,387	0%
Fair value (RM)			1.00	1.00	1%
Implied PE			29x		

Source: Company data, Macquarie Research, October 2018

Fig 2 Scenario analysis of MRCB's fair value assumptions

Item	Bear Case	Base Case	Bull Case
Fair Value (RM)	0.89	1.00	1.05
Upside/(Downside)	21.9%	36.5%	43.8%
Dividend	1.8%	1.7%	1.8%
TSR	23.7%	38.2%	45.6%

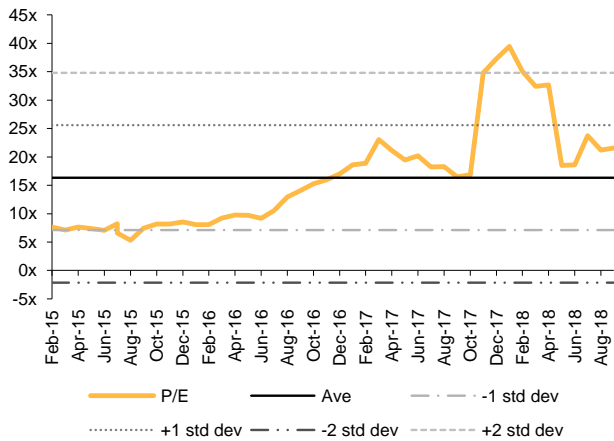
Assumptions

Property discount to RNAV	60%	40%	30%
Cumulative orderbook replenishment in FY18-20E	RM1bn	RM2bn	RM3bn
Construction PER	8x	10x	12x

Note: Compared against share price as at 9 October 2018.

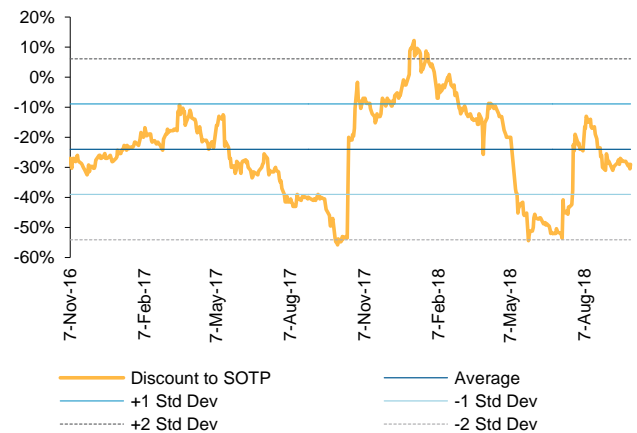
Source: Bloomberg, Macquarie Research, October 2018

Fig 3 MRCB's rolling fwd PER



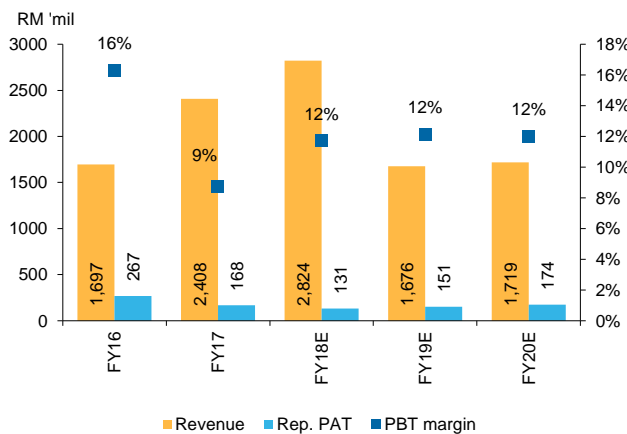
Source: Bloomberg, Macquarie Research, October 2018

Fig 4 MRCB's discount to SOTP



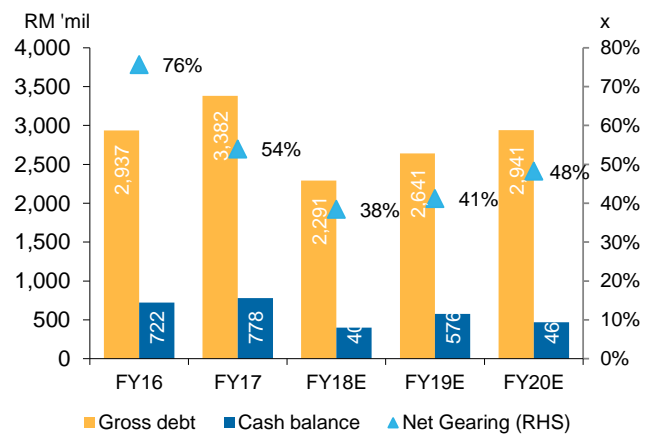
Source: Bloomberg, Macquarie Research, October 2018

Fig 5 FY18–20E PBT margins will be anchored by the fees from project management contracts



Source: Company data, Macquarie Research, October 2018

Fig 6 Net gearing to pick up once Kwasa Damansara project kicks off in FY19E



Source: Company data, Macquarie Research, October 2018

Fig 7 Change in estimates

RM 'mil	New Estimates			Old Estimates			Difference		
	FY18E	FY19E	FY20E	FY18E	FY19E	FY20E	FY18E	FY19E	FY20E
Revenue	1,676	1,719	2,188	2,013	1,987	2,561	-17%	-13%	-15%
EBIT	206	212	261	216	236	298	-4%	-10%	-13%
PBT	197	209	263	282	252	313	-30%	-17%	-16%
PAT	131	151	174	137	182	211	-4%	-17%	-17%
EPS (sen)	3.0	3.4	4.0	3.1	4.2	4.8	-4%	-17%	-17%

Source: Company data, Macquarie Research, October 2018

Fig 8 MQ vs consensus

RM 'mil	Macquarie			Consensus			Difference		
	FY18E	FY19E	FY20E	FY18E	FY19E	FY20E	FY18E	FY19E	FY20E
Revenue	1,676	1,719	2,188	2,142	2,273	2,564	-22%	-24%	-15%
EBIT	206	212	261	180	211	269	15%	1%	-3%
PBT	197	209	263	237	246	300	-17%	-15%	-12%
PAT	131	151	174	130	162	192	1%	-7%	-9%
EPS (sen)	3.0	3.4	4.0	3.1	4.1	5.0	-4%	-16%	-20%

Source: Bloomberg, Macquarie Research, October 2018

Macquarie Quant View

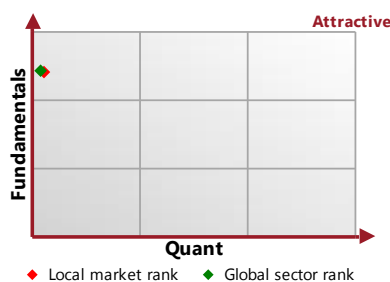
The Quant View page below has been derived from models that are developed and maintained by Sales and Trading personnel at Macquarie. The models are not a product of the Macquarie Research Department.

The quant model currently holds a strong negative view on MRCB. The strongest style exposure is Growth, indicating this stock has good historic and/or forecast growth. Growth metrics focus on both top and bottom line items. The weakest style exposure is Quality, indicating this stock is likely to have a weaker and less stable underlying earnings stream.

1955/2002

Global rank in Capital Goods

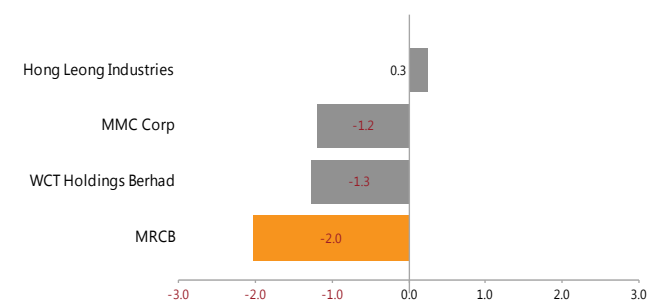
% of BUY recommendations	56% (5/9)
Number of Price Target downgrades	0
Number of Price Target upgrades	0



Displays where the company's ranked based on the fundamental consensus Price Target and Macquarie's Quantitative Alpha model.
Two rankings: Local market (Malaysia) and Global sector (Capital Goods)

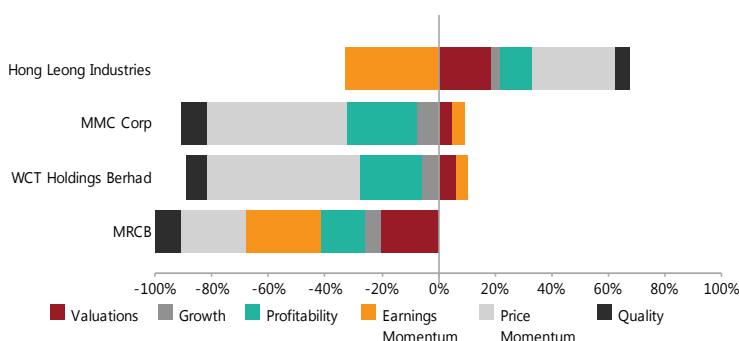
Macquarie Alpha Model ranking

A list of comparable companies and their Macquarie Alpha model score (higher is better).



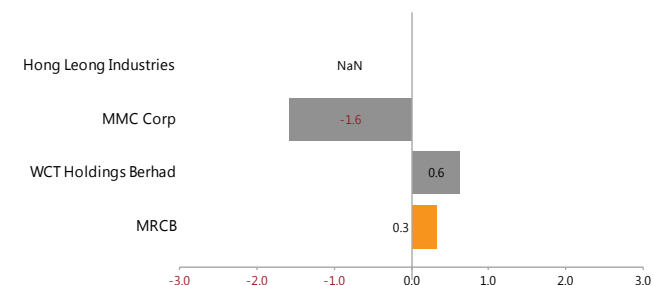
Factors driving the Alpha Model

For the comparable firms this chart shows the key underlying styles and their contribution to the current overall Alpha score.



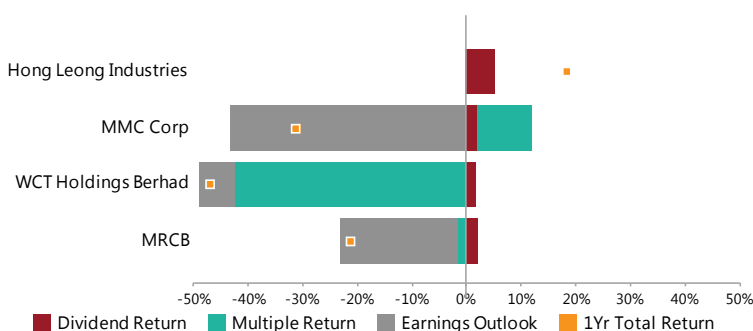
Macquarie Earnings Sentiment Indicator

The Macquarie Sentiment Indicator is an enhanced earnings revisions signal that favours analysts who have more timely and higher conviction revisions. Current score shown below.



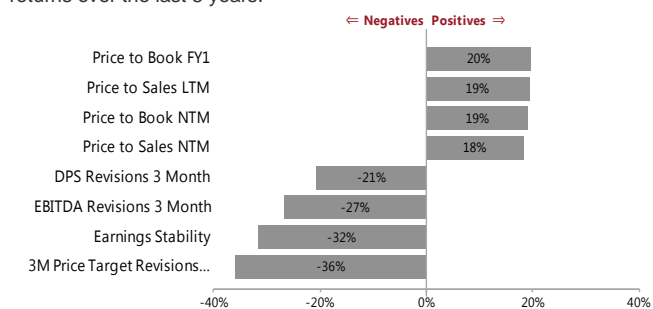
Drivers of Stock Return

Breakdown of 1 year total return (local currency) into returns from dividends, changes in forward earnings estimates and the resulting change in earnings multiple.



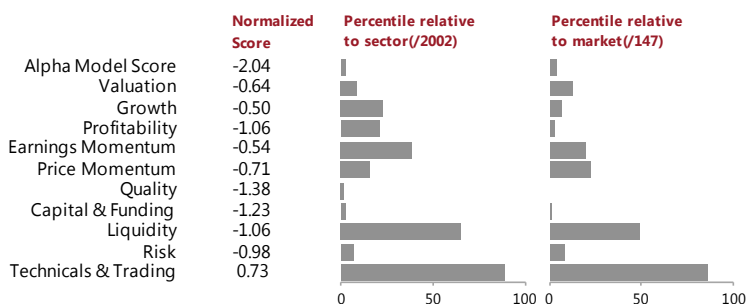
What drove this Company in the last 5 years

Which factor score has had the greatest correlation with the company's returns over the last 5 years.



How it looks on the Alpha model

A more granular view of the underlying style scores that drive the alpha (higher is better) and the percentile rank relative to the sector and market.



Source (all charts): FactSet, Thomson Reuters, and Macquarie Quant. For more details on the Macquarie Alpha model or for more customised analysis and screens, please contact the Macquarie Global Quantitative/Custom Products Group (cpq@macquarie.com)

MRCB (MRC MK, Outperform, Target Price: RM1.00)

Interim Results					Profit & Loss						
		1H/18A	2H/18E	1H/19E	2H/19E		2017A	2018E	2019E	2020E	
Net Property Income	m	754	922	774	945	Net Property Income	m	2,824	1,676	1,719	2,188
Development Income	m	0	0	0	0	Development Income	m	0	0	0	0
Other Revenue	m	0	0	0	0	Other Revenue	m	0	0	0	0
Total Revenue	m	754	922	774	945	Total Revenue	m	2,824	1,676	1,719	2,188
Management Fees	m	0	0	0	0	Management Fees	m	0	0	0	0
Other Expenses	m	-661	-808	-678	-829	Other Expenses	m	-2,615	-1,470	-1,507	-1,927
EBITDA	m	119	145	124	151	EBITDA	m	320	264	275	343
Dep & Amortisation	m	26	32	28	35	Dep & Amortisation	m	73	58	63	82
EBIT	m	93	114	96	117	EBIT	m	247	206	212	261
Net Interest Income	m	-15	-18	-18	-23	Net Interest Income	m	-91	-33	-41	-47
Associates	m	11	13	17	21	Associates	m	25	24	38	50
Exceptionals	m	0	0	0	0	Exceptionals	m	66	0	0	0
Other Pre-Tax Income	m	0	0	0	0	Other Pre-Tax Income	m	0	0	0	0
Pre-Tax Profit	m	89	108	94	115	Pre-Tax Profit	m	247	197	209	263
Tax Expense	m	-23	-28	-24	-30	Tax Expense	m	-66	-51	-54	-71
Net Profit	m	66	80	70	85	Net Profit	m	182	146	155	192
Minority Interests	m	-7	-8	-2	-2	Minority Interests	m	-14	-14	-4	-18
Reported Earnings	m	59	72	68	83	Reported Earnings	m	168	131	151	174
Adjusted Earnings	m	59	72	68	83	Adjusted Earnings	m	101	131	151	174
EPS (rep)	sen	1.3	1.6	1.5	1.9	EPS (rep)	sen	5.9	3.0	3.4	4.0
EPS (adj)	sen	1.3	1.6	1.5	1.9	EPS (adj)	sen	3.6	3.0	3.4	4.0
EPS Growth yoy (adj)	%	-35.8	8.0	14.9	14.9	EPS Growth (adj)	%	4.5	-17.4	14.9	15.7
						PE (rep)	x	12.4	24.3	21.1	18.2
						PE (adj)	x	20.0	24.3	21.1	18.2
EBITDA Margins	%	15.8	15.8	16.0	16.0	Total DPS	sen	1.8	1.3	1.5	1.8
EBIT Margins	%	12.3	12.3	12.4	12.4	Total Div Yield	%	2.4	1.7	2.1	2.4
Earnings Split	%	45.0	55.0	45.0	55.0	Basic Shares Outstanding	m	4,387	4,387	4,387	4,387
Revenue Growth	%	-41.1	-40.2	2.5	2.5	Diluted Shares Outstanding	m	2,861	4,387	4,387	4,387
EBIT Growth	%	-31.7	2.7	2.9	2.9						
Profit & Loss Ratios					Cashflow Analysis						
		2017A	2018E	2019E	2020E		2017A	2018E	2019E	2020E	
Revenue Growth	%	17.3	-40.6	2.5	27.3	EBITDA	m	320	264	275	343
EBITDA Growth	%	-17.1	-17.3	4.3	24.5	Tax Paid	m	-86	-51	-54	-71
EBIT Growth	%	-23.7	-16.3	2.9	22.8	Chg in Working Capital	m	-1,594	-200	-66	-309
EBITDA Margins	%	11.3	15.8	16.0	15.7	Net Interest Paid	m	-165	-33	-41	-47
EBIT Margins	%	8.7	12.3	12.4	11.9	Other	m	399	0	0	0
Net Profit Margins	%	3.6	7.8	8.8	8.0	Operating Cashflow	m	-1,127	-21	114	-85
Payout Ratio	%	48.3	41.8	43.7	44.0	Acquisitions	m	-583	0	0	0
EV/EBITDA	x	15.6	18.9	17.3	13.8	Capex	m	-176	-177	-133	-153
EV/EBIT	x	19.9	23.6	21.7	17.5	Asset Sales	m	1	2,441	0	0
						Other	m	-284	0	0	0
Balance Sheet Ratios						Investing Cashflow	m	-1,042	2,264	-133	-153
ROE	%	2.6	2.7	3.0	3.4	Dividend (Ordinary)	m	-60	-38	-55	-66
ROA	%	2.8	2.2	2.4	2.7	Equity Raised	m	1,732	0	0	0
ROIC	%	3.5	2.0	2.3	2.6	Debt Movements	m	452	-1,091	350	300
Net Debt/Equity	%	52.8	37.5	40.2	47.0	Other	m	-83	30	31	32
Interest Cover	x	2.7	6.2	5.2	5.5	Financing Cashflow	m	2,041	-1,098	326	266
Price/Book	x	0.7	0.6	0.6	0.6						
Book Value per Share		1.1	1.1	1.1	1.2	Net Chg in Cash/Debt	m	56	-347	206	-75
						Free Cashflow	m	-1,303	-198	-19	-237
					Balance Sheet						
		2017A	2018E	2019E	2020E		2017A	2018E	2019E	2020E	
Cash	m	778	401	576	469	Cash	m	778	401	576	469
Receivables	m	3,045	873	754	899	Receivables	m	3,045	873	754	899
Inventories	m	154	94	80	87	Inventories	m	154	94	80	87
Investments	m	1,211	1,245	1,278	1,311	Investments	m	1,211	1,245	1,278	1,311
Fixed Assets	m	614	772	881	992	Fixed Assets	m	614	772	881	992
Intangibles	m	226	313	313	313	Intangibles	m	226	313	313	313
Other Assets	m	4,272	4,929	5,339	5,739	Other Assets	m	4,272	4,929	5,339	5,739
Total Assets	m	10,301	8,626	9,221	9,811	Total Assets	m	10,301	8,626	9,221	9,811
Payables	m	1,748	1,056	1,201	1,366	Payables	m	1,748	1,056	1,201	1,366
Short Term Debt	m	2,491	1,282	1,432	1,532	Short Term Debt	m	2,491	1,282	1,432	1,532
Long Term Debt	m	891	1,009	1,209	1,409	Long Term Debt	m	891	1,009	1,209	1,409
Provisions	m	242	242	242	242	Provisions	m	242	242	242	242
Other Liabilities	m	0	0	0	0	Other Liabilities	m	0	0	0	0
Total Liabilities	m	5,372	3,589	4,084	4,549	Total Liabilities	m	5,372	3,589	4,084	4,549
Shareholders' Funds	m	4,824	4,918	5,014	5,122	Shareholders' Funds	m	4,824	4,918	5,014	5,122
Minority Interests	m	104	119	123	140	Minority Interests	m	104	119	123	140
Total S/H Equity	m	4,929	5,037	5,136	5,263	Total S/H Equity	m	4,929	5,037	5,136	5,263
Total Liab & S/H Funds	m	10,301	8,626	9,221	9,811	Total Liab & S/H Funds	m	10,301	8,626	9,221	9,811

All figures in MYR unless noted.

Source: Company data, Macquarie Research, October 2018

Important disclosures:

Recommendation definitions

Macquarie – Australia/New Zealand

Outperform – return >3% in excess of benchmark return
 Neutral – return within 3% of benchmark return
 Underperform – return >3% below benchmark return

Benchmark return is determined by long term nominal GDP growth plus 12 month forward market dividend yield, which is currently around 9%.

Macquarie – Asia/Europe

Outperform – expected return >+10%
 Neutral – expected return from -10% to +10%
 Underperform – expected return <-10%

Mazi Macquarie – South Africa

Outperform – expected return >+10%
 Neutral – expected return from -10% to +10%
 Underperform – expected return <-10%

Macquarie - Canada

Outperform – return >5% in excess of benchmark return
 Neutral – return within 5% of benchmark return
 Underperform – return >5% below benchmark return

Macquarie - USA

Outperform (Buy) – return >5% in excess of Russell 3000 index return
 Neutral (Hold) – return within 5% of Russell 3000 index return
 Underperform (Sell) – return >5% below Russell 3000 index return

Volatility index definition*

This is calculated from the volatility of historical price movements.

Very high–highest risk – Stock should be expected to move up or down 60–100% in a year – investors should be aware this stock is highly speculative.

High – stock should be expected to move up or down at least 40–60% in a year – investors should be aware this stock could be speculative.

Medium – stock should be expected to move up or down at least 30–40% in a year.

Low–medium – stock should be expected to move up or down at least 25–30% in a year.

Low – stock should be expected to move up or down at least 15–25% in a year.

* Applicable to Asia/Australian/NZ/Canada stocks only

Recommendations – 12 months

Note: Quant recommendations may differ from Fundamental Analyst recommendations

Financial definitions

All "Adjusted" data items have had the following adjustments made:

Added back: goodwill amortisation, provision for catastrophe reserves, IFRS derivatives & hedging, IFRS impairments & IFRS interest expense
 Excluded: non recurring items, asset revals, property revals, appraisal value uplift, preference dividends & minority interests

EPS = adjusted net profit / efpowa*

ROA = adjusted ebit / average total assets

ROA Banks/Insurance = adjusted net profit / average total assets

ROE = adjusted net profit / average shareholders funds

Gross cashflow = adjusted net profit + depreciation

*equivalent fully paid ordinary weighted average number of shares

All Reported numbers for Australian/NZ listed stocks are modelled under IFRS (International Financial Reporting Standards).

Recommendation proportions – For quarter ending 30 September 2018

	AU/NZ	Asia	RSA	USA	CA	EUR	
Outperform	51.56%	59.51%	45.05%	46.88%	67.86%	46.70%	(for global coverage by Macquarie, 3.70% of stocks followed are investment banking clients)
Neutral	33.20%	28.92%	37.36%	47.70%	25.00%	42.73%	(for global coverage by Macquarie, 2.04% of stocks followed are investment banking clients)
Underperform	15.23%	11.57%	17.58%	5.42%	7.14%	10.57%	(for global coverage by Macquarie, 0.47% of stocks followed are investment banking clients)

MRC MK vs KLCI, & rec history



(all figures in MYR currency unless noted)

Note: Recommendation timeline – if not a continuous line, then there was no Macquarie coverage at the time or there was an embargo period.

Source: FactSet, Macquarie Research, October 2018

12-month target price methodology

MRC MK: RM1.00 based on a Sum of Parts methodology

Company-specific disclosures:

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Date	Stock Code (BBG code)	Recommendation	Target Price
26-Jul-2018	MRC MK	Outperform	RM1.00
30-Apr-2018	MRC MK	Outperform	RM1.25
19-Oct-2017	MRC MK	Outperform	RM1.15
30-Mar-2017	MRC MK	Outperform	RM1.75
07-Nov-2016	MRC MK	Outperform	RM1.61

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