

3Q FYE DEC 2012 RESULTS REPORT

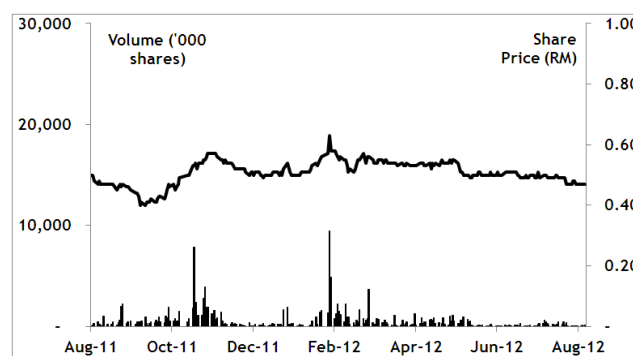
27 November 2012

Name of PLC: <i>Salcon Berhad (Salcon)</i>		Target Price:	RM 0.78
Business Summary : <i>Investment holding company involved in water and wastewater treatment, raw water transfer via concession and O&M contract, as well as water construction</i>			
Major Shareholders :			
<i>Dato' Seri (Dr.) Goh Eng Toon</i>			12.8%
<i>Tan Sri Dato' Tee Tiam Lee</i>			10.8%
<i>(as at 25 April 2012)</i>			
PLC Website : www.salcon.com.my		Recommendation:	Buy
IR Contact : <i>Ms Chern Meng Gaik</i> mgchern@salcon.com.my		Market Capitalisation:	RM232.2m
<ul style="list-style-type: none"> - <i>FBM Small Cap</i> - <i>FBM Emas Shariah</i> 		Current Price :	RM 0.445
		Market / Sector:	Trading/Services
		Stock Code:	8567
Analyst : Lim Boon Ngee			
Tel : +603 2163 3200; Email : bnlim@nra.com.my			

Key Stock Statistics	2010	2011	2012F	2013F
EPS (sen)	5.7	3.1	1.6	2.9
P/E (x)	7.9	14.4	27.6	15.2
Dividend/Share (sen)	1.5	1.5	1.5	1.5
NTA/Share (RM)	0.65	0.79	0.76	0.78
Book Value/Share (RM)	0.68	0.82	0.79	0.81
Issued Capital (mil shares)	473.5	474.3	521.7	521.7
52-weeks Share Price Range (RM)			0.43 - 0.67	

Per Share Data	2010	2011	2012F	2013F
Year-end 31 Dec				
Book Value (RM)	0.68	0.82	0.79	0.81
Operating Cash Flow (sen) (20.1)	(11.9)	(2.1)	10.3	
Earnings (sen)	5.7	3.1	1.6	2.9
Dividend (sen)	1.5	1.5	1.5	1.5
Payout Ratio (%)	26.6	48.6	93.1	51.2
PER (x)	7.9	14.4	27.6	15.2
P/Cash Flow (x)	(2.2)	(3.8)	(21.3)	4.3
P/Book Value (x)	0.7	0.5	0.6	0.6
Dividend Yield (%)	3.4	3.4	3.4	3.4
ROE (%)	8.4	4.1	2.1	3.7
Net Gearing (%)	28.2	22.8	23.9	18.0

P&L Analysis (RM mil)	2010	2011	2012F	2013F
Revenue	549.9	472.5	318.7	384.6
Operating Profit	37.4	38.8	40.4	55.4
Depreciation	(11.7)	(14.0)	(16.8)	(17.7)
Finance, net	(1.1)	(12.6)	(13.9)	(13.8)
Associate	3.6	2.9	4.0	4.0
EI	5.5	-	-	-
Pre-tax Profit	44.1	29.1	30.5	45.6
Effective Tax Rate (%)	(19.5)	(12.7)	(20.0)	(20.0)
Net Profit	26.8	14.6	8.4	15.3
Operating Margin (%)	6.8	8.2	12.7	14.4
Pre-tax Margin (%)	8.0	6.1	9.6	11.9
Net-Margin (%)	4.9	3.1	2.6	4.0

Share Price Chart

1. 3QFY12 Results Highlight

	3QFY12	3QFY11	Chg
	RMm	RMm	%
Revenue	84.2	81.0	3.8
Operating Profit	7.6	6.5	17.5
Net interest expense	(2.6)	(2.2)	16.5
Associates	0.9	0.8	8.3
Pre-tax Profit	5.8	5.0	16.5
Net Profit	0.4	3.2	(87.0)
Operating Margin (%)	9.0	8.0	
Pre-tax Margin (%)	6.9	6.2	
Net-Margin (%)	0.5	4.0	

- While turnover came in marginally higher at RM84.2m, PBT rose by 16.5% to RM5.8m in 3QFY12. However, Salcon experienced a steep drop in net profit to RM0.4m.

- Its concession business has grown a lot more meaningful in contribution to the group. This was attributed to commissioning of higher-capacity water and sewage treatment plants. Changle WTP (100MLD), Yizheng WTP (50 MLD) and Yizheng STP (50 MLD) commenced operations in 2QFY12, while the larger-capacity Nan An water supply project was commissioned in 3QFY12. In 3QFY12, concession business grew its EBIT by 87.2% to RM10.2m.
- However, its construction division continued to suffer loss of RM2.2m in 3QFY12 albeit with a smaller loss as compared with 2QFY12's RM6.7m. This was due to lower construction orderbook.
- Group EBIT grew by 33.1% in 3QFY12 to RM8.6m. However, due to higher interest expense to fund the implementation of concessions in China, PBT only rose by 16.5% to RM5.9m in 3QFY12.
- The bottomline net profit only came in at RM0.42m in 3QFY12 due to higher minority interest as its concession businesses are parked under 60%-owned Salcon Water (Asia) Limited and 60%-owned JV company, Darco Environmental Pte Ltd.

9MFY12 Results Highlight

	9MFY12	9MFY11	Chg
	RMm	RMm	%
Revenue	232.8	292.0	(20.3)
Operating Profit	22.1	20.0	10.2
Finance cost	(5.5)	(5.4)	1.3
Associates	2.5	2.2	11.8
Pre-tax Profit	19.1	16.8	13.2
Net Profit	3.2	7.9	(59.6)
Operating Margin (%)	26.2	24.7	
Pre-tax Margin (%)	22.7	20.8	
Net-Margin (%)	3.8	9.7	

- For 9MFY12, the 20.3% decline in turnover was mainly attributed to lower construction orderbook. EBIT of construction division sprang into a loss of RM8.4m (9MFY12) as compared with an EBIT of RM5.0m (9MFY11). However, concession earnings more than doubled to RM35.0m (9MFY12) from RM14.9m (9MFY11).
- The decline in net profit was due mainly to higher minority interest as the bulk of group earnings was derived from concession earnings in which Salcon has a 60% share of the profit.

2. Earnings Outlook

- Beginning FY12, Salcon's larger-capacity concessions such as Changle new WTP (100 MLD) and Changle Raw Water (100 MLD) will start to contribute more significantly to the group. The commissioning of Nan An Raw Water (175 MLD) and completion of the acquisition of Wukang and Qian Yua WTPs will drive earnings in FY13.

Production Capacity of China Concessions (MLD as at end-FY)

	FY09	FY10	FY11	FY12	FY13	
Changle sewage treatment plant	40	40	40	40	40	
Linyi water treatment plant	150	150	150	150	150	
Haining water treatment plant	150	300	300	300	300	
Changle water treatment plant (existing/new)	40	WIP	WIP	100	100	operational in 1QFY12
Changle raw water transfer project	WIP	WIP	WIP	100	100	operational in 1QFY12
Yizheng water supply project	-	-	WIP	50	50	operational in 1QFY12
Yizheng sewage treatment plant	-	-	WIP	50	50	operational in 1QFY12
Nan An raw water supply project	WIP	WIP	WIP	175	350	operational in 3QFY12
Wukang water treatment plants	-	-	-	60	60	JV with Darco
Qian Yua water treatment plants	-	-	-	100	100	JV with Darco
Total	380	490	490	1,125	1,300	

3. Valuation and Recommendation

- We have reduced our earnings forecast for FY12-13 by 7-10% to factor in the lower contribution from construction division.
- However, we are maintaining our Buy recommendation on Salcon for its growing earnings contribution from its concession assets in China. The stock is currently trading at a 42% discount to its book value of RM0.76/share, which does not reflect the promising long-term prospects of its growing concession-based business in China.

Disclosures/Disclaimer

Investment ratings:

Buy (generally >10% upside over the next 12 months)

Hold (generally negative 10% downside to positive 10% upside over the next 12 months)

Sell (generally >10% downside over the next 12 months)

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