

2Q FYE DEC 2012 RESULTS REPORT

17 August 2012

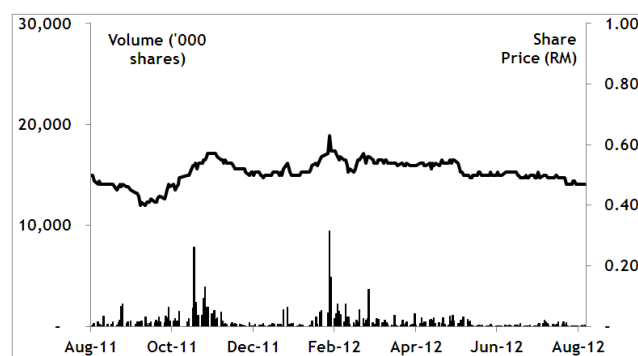
Name of PLC: Salcon Berhad (Salcon)		Target Price:	RM 0.78
Business Summary : Investment holding company involved in water and wastewater treatment, raw water transfer via concession and O&M contract, as well as water construction			
Major Shareholders :			
Dato' Seri (Dr.) Goh Eng Toon			12.8%
Tan Sri Dato' Tee Tiam Lee			10.8%
(as at 25 April 2012)			
PLC Website : www.salcon.com.my		Recommendation:	Buy
IR Contact : Ms Chern Meng Gaik mgchern@salcon.com.my		Market Capitalisation:	RM245.2m
<ul style="list-style-type: none"> - FBM Small Cap - FBM Emas Shariah 		Current Price :	RM 0.47
		Market / Sector:	Trading/Services
		Stock Code:	8567
Analyst : Lim Boon Ngee			
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Key Stock Statistics	2010	2011	2012F	2013F
EPS (sen)	5.7	3.1	1.8	3.1
P/E (x)	8.3	15.2	26.4	14.9
Dividend/Share (sen)	1.5	1.5	1.5	1.5
NTA/Share (RM)	0.65	0.79	0.77	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)				0.38 - 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)	8.6	
Earnings (sen)	5.7	3.1	1.8	3.1
Dividend (sen)	1.5	1.5	1.5	1.5
Payout Ratio (%)	26.6	48.6	84.4	47.7
PER (x)	8.3	15.2	26.4	14.9
P/Cash Flow (x)	(2.3)	(4.0)	(22.3)	5.5
P/Book Value (x)	0.7	0.6	0.6	0.6
Dividend Yield (%)	3.2	3.2	3.2	3.2
ROE (%)	8.4	4.1	2.3	3.9
Net Gearing (%)	28.2	22.8	23.9	20.1

P&L Analysis (RM mil)	2010	2011	2012F	2013F
Revenue	549.9	472.5	318.7	406.0
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)	(14.1)	(13.9)
Associate	3.6	2.9	4.0	4.0
EI	5.5	-	-	-
Pre-tax Profit	44.1	29.1	30.3	45.5
Effective Tax Rate (%)	(19.5)	(12.7)	(20.0)	(20.0)
Net Profit	26.8	14.6	9.3	16.4
Operating Margin (%)	6.8	8.2	12.7	13.6
Pre-tax Margin (%)	8.0	6.1	9.5	11.2
Net-Margin (%)	4.9	3.1	2.9	4.0

Share Price Chart



1. 1QFY12 Results Highlight

	2QFY12	2QFY11	Chg
	RMm	RMm	%
Revenue	69.7	100.6	(30.7)
Operating Profit	7.2	5.8	24.2
Net interest expense	(1.6)	(1.4)	7.4
Associates	0.8	0.9	(7.0)
Pre-tax Profit	6.4	5.2	23.7
Net Profit	0.3	0.4	(32.0)
Operating Margin (%)	10.3	5.7	
Pre-tax Margin (%)	9.2	5.1	
Net-Margin (%)	0.4	0.4	

- Salcon reported a disappointing 2QFY12 results. Turnover for 2QFY12 declined by 30.7% due to lower construction orderbook.

- Salcon recorded a bottomline net profit of only RM0.25m as the strong profit performance of its concession business was offset by loss in its construction division.
- In 2QFY12, construction division recorded an operating loss of RM6.7m due to the lower orderbook as compared with EBIT of RM1.0m in 2QFY11. However, underpinned by higher installation income and expanded capacity of its water and wastewater treatment plants in China, EBIT from concession business mainly its concessions in China, jumped to RM16.4m (2QFY12) from RM5.0m (2QFY11). Group EBIT still improved by 71.3% to RM9.9m in 2QFY12 from RM5.8m in 2QFY11. Due to higher interest expense to fund the implementation of concessions in China, PBT only rose by 23.7% to RM6.4m in 2QFY12.

1HFY12 Results Highlight

	1HFY12 RMm	1HFY11 RMm	Chg %
Revenue	148.7	211.0	(29.5)
Operating Profit	14.5	13.6	6.7
Finance cost	(2.9)	(3.2)	(9.4)
Associates	1.6	1.4	13.8
Pre-tax Profit	13.2	11.8	11.8
Net Profit	2.8	4.7	(40.8)
Operating Margin (%)	20.8	13.5	
Pre-tax Margin (%)	19.0	11.8	
Net-Margin (%)	4.0	4.6	

- For 1HFY12, both turnover and net profit declined by 29.5% and 40.8% to RM148.7m and RM2.8m. This was attributed to lower construction orderbook despite higher profit from concession business.

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
Changzhou Southeast Industrial wastewater treatment plant	-	-	WIP	30	30	operational in 1QFY12
Nan An raw water supply project	WIP	WIP	WIP	175	350	operational in 3QFY12
Wukang water treatment plants	-	-	-	60	60	
Qian Yua water treatment plants	-	-	-	100	100	
Total	380	490	490	1,155	1,330	

- Salcon currently owns 8 water concessions, 2 municipal wastewater concessions and 1 industrial wastewater concession located in Shandong, Fujian, Zhejiang and Jiangsu Province with a total combined capacity of 1,300 MLD. The increased contribution from concession division will help to offset the declining orderbook of construction division.

3. Valuation and Recommendation

- We have reduced our earnings forecast for FY12-13 by 25-45% 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 41% discount to its book value of RM0.80/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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