

3Q FYE DEC 2011 RESULTS REPORT

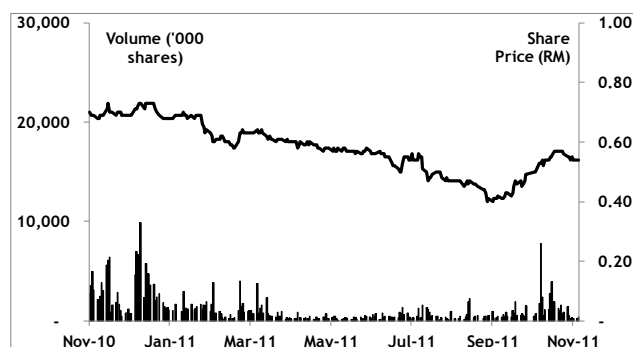
Date: 1 December 2011

Name of PLC: Salcon Berhad (Salcon)		Target Price:	RM 0.75
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 Goh Eng Toon			14.1%
Dato' Tee Tiam Lee			11.8%
(as at 29 April 2011)			
PLC Website : www.salcon.com.my		Recommendation:	Buy
IR Contact : Ms Chern Meng Gaik mgchern@salcon.com.my		Market Capitalisation:	RM 251.0m
- FBM Small Cap - FBM Emas Shariah		Current Price :	RM 0.53
		Market / Sector:	Trading/Services
		Stock Code:	8567
Analyst : Lim Boon Ngee			
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Key Stock Statistics	2009	2010	2011F	2012F
EPS (sen)	4.7	4.5	2.6	5.3
P/E (x)	11.2	11.8	20.7	9.9
Dividend/Share (sen)	1.5	1.5	1.5	1.5
NTA/Share (RM)	0.63	0.62	0.76	0.80
Book Value/Share (RM)	0.66	0.65	0.79	0.83
Issued Capital (mil shares)	467.7	473.5	474.3	474.3
52-weeks Share Price Range (RM)	0.38 - 0.75			

Per Share Data	2009	2010	2011F	2012F
Book Value (RM)	0.66	0.65	0.79	0.83
Operating Cash Flow (sen)	9.3	1.4	14.8	(7.3)
Earnings (sen)	4.7	4.5	2.6	5.3
Dividend (sen)	1.5	1.5	1.5	1.5
Payout Ratio (%)	31.8	33.4	58.6	28.1
PER (x)	11.2	11.8	20.7	9.9
P/Cash Flow (x)	5.7	39.1	3.6	(7.2)
P/Book Value (x)	0.8	0.8	0.7	0.6
Dividend Yield (%)	2.8	2.8	2.8	2.8
ROE (%)	7.4	6.9	3.5	6.6
Net Gearing (%)	n.c.	29.4	8.5	24.6

P&L Analysis (RM mil)	2009	2010	2011F	2012F
Revenue	369.9	418.2	404.0	488.9
Operating Profit	33.6	31.9	30.4	50.8
Depreciation	(10.7)	(14.9)	(20.7)	(23.7)
Finance, net	(4.0)	(3.8)	(6.5)	(4.5)
Associate	3.8	3.6	4.0	4.0
EI	-	5.5	-	-
Pre-tax Profit	33.5	37.2	27.9	50.4
Effective Tax Rate (%)	(22.1)	(22.8)	(25.0)	(25.0)
Net Profit	22.1	21.3	12.1	25.3
Operating Margin (%)	9.1	7.6	7.5	10.4
Pre-tax Margin (%)	9.0	8.9	6.9	10.3
Net-Margin (%)	6.0	5.1	3.0	5.2

Share Price Chart

1. 3QFY11 Results Highlight

	3QFY11	3QFY10	Chg
	RMm	RMm	%
Revenue	81.0	78.0	3.9
Operating Profit	6.9	6.0	14.8
Finance cost	(2.7)	(1.5)	76.7
Associates	0.8	1.0	(20.5)
Pre-tax Profit	5.0	5.5	(8.7)
Net Profit	3.2	2.5	26.3
Operating Margin (%)	8.5	7.7	
Pre-tax Margin (%)	6.2	7.1	
Net-Margin (%)	4.0	3.3	

- Salcon reported a marginal growth in turnover to RM81.0m in 3QFY11. PBT however, was 8.7% lower at RM5.0m. Due to a tax gain, net profit rose by 26.3% to RM3.2m.

- At operating level, EBIT actually grew by 12.9% to RM6.5m in 3QFY11 as Construction division recorded a small profit of RM0.7m against a loss in 3QFY10. However, EBIT contribution of Concession division was at RM5.5m, 18.7% lower as compared with 3QFY10 of RM6.7m. This was attributed to start-up and procurement expenses.
- As a result of the funding requirement of its concession projects at various stages, interest expense rose to RM2.7m (3QFY11) from RM1.5m (3QFY10).

9MFY11 Results Highlight

	9M 2011	9M 2010	Chg
	RMm	RMm	%
Revenue	292.0	299.6	(2.5)
Operating Profit	21.0	30.3	(30.5)
Finance cost	(6.4)	(5.3)	20.5
Associates	2.2	2.7	(17.0)
EI	-	5.5	n.m.
Pre-tax Profit	16.8	33.1	(49.1)
Net Profit	7.9	21.0	(62.6)
Operating Margin (%)	26.0	38.8	
Pre-tax Margin (%)	20.8	42.5	
Net-Margin (%)	9.7	26.9	

- For 9MFY11, while turnover was slightly lower at RM292.0m, net profit declined by 62.6% to RM7.9m due to the following reasons:
 - Operationally, EBIT of its construction division declined by 20.8% in 9MFY11 to RM5.0m from RM6.4m in 3QFY10;
 - Concession division also experienced a 13.9% decline in EBIT to RM14.9m. This was attributed to start-up and procurement expenses;
 - Higher finance costs to fund the implementation of concession projects; and
 - In addition, Salcon benefited from an exceptional gain from disposal of property amounting to RM5.5m in 2QFY10.

2. Earnings Outlook

- Annualised net profit for 9MFY11 is 40% below our earnings forecast for FY11. Hence, we are downgrading our earnings forecast for FY11. FY11's earnings base is depressed by exceptional items and costs associated to progressive commissioning of its larger-capacity concessions. However, we are still keeping our earnings forecast for FY12.
- Salcon's current profit base especially its China concession has yet to reach its full potential as the larger-capacity concessions such as Changle new WTP (100MLD), Changle Raw Water (100MLD) and Nan An Raw Water (175MLD) will only be commissioned towards end FY11 and early FY12.
- The new WTP and raw water transfer project in Changle County, Shandong Province was successfully completed on 11 Nov 2011, which will contribute positively to the recurring concession income from FY12 onwards. Salcon is now the sole integrated water and wastewater solutions provider ranging from supply and management of raw water resources, production and supply of treated water, provision of customer services, billing and collection as well as wastewater treatment services for the whole of Changle County.

Production Capacity of China Concessions

Concessions	Production Capacity (MLD) as at end-FY		
	FY09	FY10	FY11
Changle Sewage Treatment Plant	40	40	40
Linyi Water Treatment Plant	150	150	150
Haining Water Treatment Plant	150	300	300
Changle Water Treatment Plant (existing/new)	40	WIP	100
Changle Raw Water Transfer Project	WIP	WIP	100
Nan An Raw Water Supply Project	WIP	WIP	175
Yizheng Water Supply Project	-	-	50
Yizheng Sewage Treatment Plant	-	-	50
Changzhou Southeast Industrial WWTP	-	-	30
Total	380	490	995

- Salcon has recently proposed to undertake a 10% private placement for the repayment of the 5-years term loan.

3. Valuation and Recommendation

- We are maintaining our Buy recommendation on Salcon for the earnings growth in FY12-FY13 arising from the doubling in production capacity towards the latter part of FY11. The stock is currently trading at a 30% 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 and the doubling in design capacity of its China concession by end-FY11.

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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