

Melati Ehsan

Undervalued turnkey play

NOT RATED

RM1.55

@25/10/07

Mkt.Cap: RM186.0m

Construction & property

Analyst briefing highlights

Melati Ehsan (MEB), a Main Board construction stock held an Analyst Briefing after releasing its 4QFY07 (Aug FY) results yesterday. We came out of the briefing feeling positive about the company's prospects over the next few years in view of its outstanding RM1.4bn construction orderbook and its maiden property venture in Pandamaran, Klang, expected to be launched early next year.

Listed in Mar. MEB was listed on the Main Board in Mar, the first construction stock to be listed on the Main Board in more than three years. Its issued share base is 120m and based on yesterday's closing price, market capitalisation is at RM186.0m.

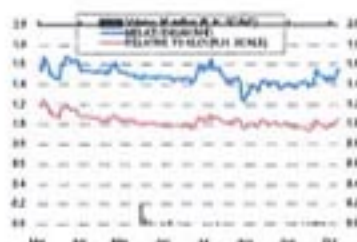
Major shareholder.... Its major shareholder and the main driver of the Group is Managing Director Dato' Yap Suan Chee who holds close to 49% stake in MEB. He has more than 20 years experience in the construction and property industry. Key management include its Executive Director, Ir Tan Hong Hing, who is also the technical director of the Group. Tan is in charge of design, planning and construction projects undertaken by the Group.

Core business is turnkey contractor. MEB is mainly a turnkey contractor, involved in design, planning and management of its construction projects. Most of its construction work is undertaken by a pool of reliable sub-contractors that include Brem Holdings, Ho Hup Construction, Suhati, Istimewa Teguh and Tropical Profile S/B.

Figure 1: MEB outstanding construction orderbook (RMm)

Client	Contract	Period completion	Amount (RMm)	Unbilled at Aug-07 (RMm)
Turnkey property projects				
PKNS	Bayu Perdana, Kota Damansara	Jan07-Dec07	23.8	0.7
PKNS	Bernam Jaya	Sep09-Aug14	55.0	55.0
DBKL	Taman Aman Putra	Oct04-Oct10	523.4	424.5
TTPT	Taman Ehsan Jaya, Johor (house)	Sep06-Dec07	21.3	5.2
TTPT	Taman Ehsan Jaya, Johor (house)	May06-Apr08	31.6	4.1
PKNS	Bayu Perdana, Kota Damansara	May06-Apr09	34.4	30.3
TTPT	Taman Ehsan Jaya, Johor (condo)	May07-Nov08	10.7	8.5
TTPT	Taman Ehsan Jaya, Klang	Dec07-Nov12	500.0	500.0
MDS*	Carrefour, Kota Damansara	Jan08-Aug08	50.0	50.0
Sub-total			1,250.2	1,078.3
Turnkey infrastructure projects				
JPS*	Flood mitigation, Kepala Batas Penang	Jan05-Feb09	168.8	147.7
JKR	Trans Eastern Kedah Interland	Sep05-Aug08	287.0	231.7
TTPT	Taman Ehsan Jaya, Johor (infra)	Sep06-Apr08	11.0	3.1
TTPT	Taman Ehsan Jaya, Johor (infra)	Nov05-Nov07	8.0	1.5
Sub-total			474.8	384.0
Group total			1,725.0	1,462.3

*MDS-Magnificent Diagraph S/B, JPS- Jabatan Pengairan & Saliran, TTPT-Bank Negara's subsidiary



Source: Company

Please read carefully the important disclosures at the end of this publication.

Higher profit margins. Due to its focus on turnkey jobs, MEB's profit margin is higher than the industry's average between 5-10%. We estimate the Group's construction margin ranges between 7-10% for major infrastructure jobs and as much as 20%-30% for high-end property development projects.

Orderbook. Group's orderbook is currently RM1.7bn, of which RM1.5bn remains outstanding. This should keep the company busy over the next 3-4 years. According to MEB, around 20% of its outstanding RM1.4bn orderbook should be recognised in FY08. The Group is also bidding for more than RM1.7bn new jobs and average success rate is around 30%. As such, MEB's orderbook could see a RM500m boost in the next few quarters.

Maiden venture into property development

First project in Klang. MEB is undertaking its maiden property venture in the Klang Valley after acquiring from Bank Negara's subsidiary, TPPT S/B, 99.8 acres of leasehold land in Pandamaran, Klang for RM32m cash. This equates to an average land cost of only RM7.36/psf. This is an attractive purchase for MEB as we understand land values around these areas are currently between RM15-18/psf.

RM500m GDV. The project, Taman Ehsan Jaya would be developed over the next five years. MEB has proposed to build 501 residential units, 320 shop lots, commercial and industrial developments. 8.7 acres has been allocated for commercial development and 6.9 acres of industrial area.

Approvals secured already. Layout plans, earthworks and pre-commencement plans has already been approved by the local municipal. Project's gross development value (GDV) estimated at RM500m. Potential profit is RM150m. Potential profit from this project is RM150m or an average RM30m PBT annually over the next five years. As such, average net profit annually is around RM22m or 18 sen EPS.

No strain on balance sheet due to deferred payment. Funding the RM32m land acquisition would not put a strain on its balance sheet. Firstly, MEB is in a RM17.6m net cash position or 14.6 sen net cash per share. Second, the land would be paid over the next two years. RM5m is to be paid after sales & purchase agreement (SPA), RM10m one year after SPA and remaining RM17m two years after the SPA.

Diversifying into property development a natural step... As MEB is the turnkey contractor for major property development projects like Klang Valley's Kota Damansara and Johor's Taman Ehsan Jaya, we view this Pandamaran property venture as a natural extension from its turnkey construction business. Earnings wise, MEB would benefit from both construction and property earnings from this project.

Figure 2: Map of Taman Ehsan Jaya's Pandamaran project



Source: Company

Valuation and recommendation

Just released FY07 final results. MEB just released its 4QFY07 (Aug FY) results yesterday. FY07 net earning was RM27.1m or 22.6 sen EPS (based on 120m issued share base). The Group has also declared a final 7.5sen gross DPS, expected to be paid in early-08. This equates to an attractive 4.8% gross yield.

Property earnings could be a major boost to Group. Based on its existing construction orderbook, MEB forecast FY08 and FY09 net earnings to grow 11% and 15% respectively. We believe this is rather conservative as its Pandamaran property venture should be a major earnings contributor from FY09 onwards. Average PBT over the next five years from this project is RM30m annually, RM22m net profit or 18 sen EPS. This is compared to MEB's FY07 RM27.1m net earnings.

Attractive valuation and yields. Based on its conservative earnings assumption, MEB is only trading at 6.0x CY 08 P/E and 4.8% gross dividend yield. This is compared to our average 9.9x CY08 P/E for our selected small-mid cap construction stocks. In view of its superior ROE above 20% and gross dividend yield, we are of the view the stock should trade higher than TSR Capital's (similar market capitalisation to MEB) consensus 7.7x CY08 P/E valuation. At 8x-9x CY08 P/E, MEB's share price could be worth between RM2.08-RM2.34.

Figure 3 : Melati Ehsan financial summary

FYE Aug (RM m)	2004*	2005*	2006*	2007
Revenue	81.3	133.2	144.2	173.4
PBT	20.1	23.1	31.8	36.6
Net profit	14.5	16.2	22.7	27.1
EPS (sen)*	12.1	13.5	18.9	22.6
P/E (x)	12.8	11.5	8.2	6.9
DPS (sen)	na	na	na	7.5
Yield (%)	na	na	na	4.8
ROE (%)	na	na	na	17.6
PBT margin (%)	24.7	17.3	22.1	21.1
Net margin (%)	17.8	12.2	15.7	15.6

*-Proforma, ^ based on 120m shares

Source: Company, CIMB/CIMB-GK estimates, Reuters Estimates

Figure 4 : Sector comparisons

	Bloomberg ticker	Recom.	Price (RM)	Mkt cap (RM m)	Core P/E (x) CY07	CY08	3-yr EPS CAGR (%)	P/NTA (x) CY06	ROE (%) CY07	Div yield (%) CY06	CY08
ACPI	ACP MK	O	2.00	443.0	25.6	8.7	nm	1.7	5.3	13.4	0.5
Hock Seng Lee	HSL MK	NR	5.15	611.3	13.9	12.1	14.6	3.0	13.4	13.6	2.8
TSR Capital	TSRC MK	NR	1.92	197.8	12.8	7.7	192.0	1.3	9.5	15.5	2.1
Mudajaya	MDJ MK	O	3.68	500.5	22.0	11.0	54.6	3.2	11.8	12.1	1.9
Simple average					18.6	9.9	87.0	2.3	10.0	13.7	1.8
Melati Ehsan	MEHB MK	NR	1.55	186.0	6.7	6.0	na	1.7	22.4	20.0	4.8

O = Outperform, N = Neutral, U = Underperform, NR = Not Rated, TB = Trading Buy and TS = Trading Sell
Source: Company, CIMB/CIMB-GK Research, Bloomberg

Appendix

Technical outlook for Melati Ehsan

Rising trading volumes. The stock's trading volume has active in the past few weeks. Share price closed 6 sen higher with 1.2m shares traded yesterday and the stock is showing signs of breaking out. This would be confirmed by strong trading volumes in the immediate term.

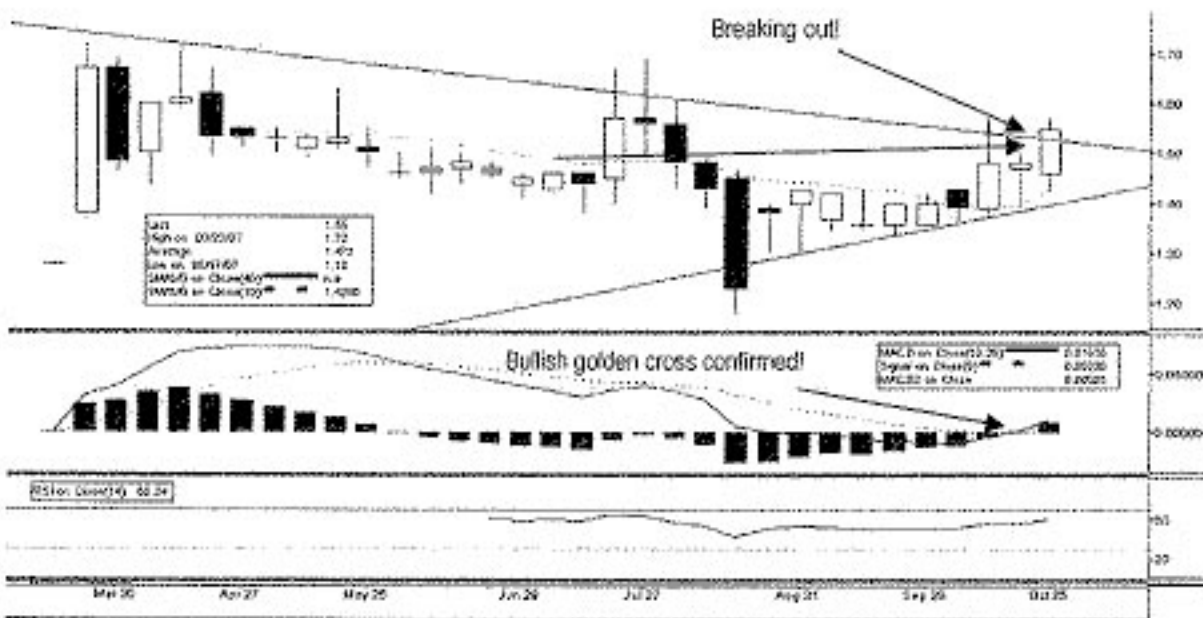
Figure 1 : Melati daily price chart



Source: Bloomberg, CIMB/CIMB-GK

Bullish weekly indicator. Medium term outlook is positive. The stock confirmed its MACD "golden cross" last week and the stock has broken out of its triangle consolidation (since Jun) this week. Next resistance is at RM1.59 and its RM1.72 year-high.

Figure 2 : Melati's weekly price chart



Source: Bloomberg, CIMB/CIMB-GK

Conclusion. The stock is likely in a medium-term uptrend after breaking out of its triangle consolidation since Jun. Confirmation would come from rising trading volumes in the stock over the next 1-2 weeks.

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