

1Q14 profits down due to margin compression

Quick Note

1Q14: Consensus earnings cuts ahead due to lower margins; Reduce

WCT's 1Q14 net income of MYR40mn (-19% y-y) formed 33% of our full year estimate (and 21% of the street's forecast) for FY14F. Both construction and property margins were down 3-4pp y-y, which implies that the cost escalation seen in 4Q is going to be prolonged. Forward guidance seems cautious, as WCT only has 1.5 years of construction projects remaining, and the need to win works packages from the West Coast Expressway/Kwasa Land civil works is urgent to sustain construction earnings (53% of overall). Momentum in property launches and take-up is still slow, and WCT risks missing its MYR1.2bn sales target for the year, in our view.

Street earnings cuts ahead, maintain Reduce

We expect the street to cut its full year earnings target for WCT, because based on trends observed over the last 3 years, WCT's earnings tend to be weaker in the final quarter. Additionally, this year, WCT will also not be able to book fair value gains on investment property, which has supported its headline figures in the last few years (since Gateway@KLIA2 is a concession, as per accounting standards, it cannot be revalued each year). Maintain Reduce, as WCT is trading at 20x FY14F earnings, on our estimates. Our bearish thesis is detailed [here](#).

Fig. 1: WCT: 1Q14 results snapshot

In line with estimates

MYR mn	1Q14	Nomura FY14F	1Q as % of NMR FY14F	Consensus FY14F	1Q as % of Cons FY14F
Revenue	467	1,878	25%	1,915	24%
Adj EBITDA	69	255	27%	320	21%
Reported NPATAMI	40	121	33%	193	21%
Adj NPATAMI	40	121	33%	193	21%

Source: Company data, Bloomberg, Nomura estimates

Divisional highlights – Construction & Property weak; Malls strong

Construction

- No job wins in 1Q14. Outstanding external construction order book as at end of 1Q14 = MYR1.78bn, implying a visibility of ~1.5 years.
- Tendering for subcon works in 6 packages of WCE (total MYR2.2bn), Kwasa Land and RAPID civil works. In our view, any project win is a bare minimum requirement at this stage. No significant visibility on Qatar projects.

Property development

- Sales at MYR218mn (18% of FY target), which includes sales by option (due to delayed Advertising Permit and Development License – ADPL). WCT is still maintaining its FY sales target of MYR1.2bn, out of MYR2.3bn new launches, but agrees that it would depend on demand momentum.

Global Markets Research

23 May 2014

Rating Remains **Reduce**

Target price Remains MYR 1.90

Closing price 22 May 2014 MYR 2.22

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Property investment

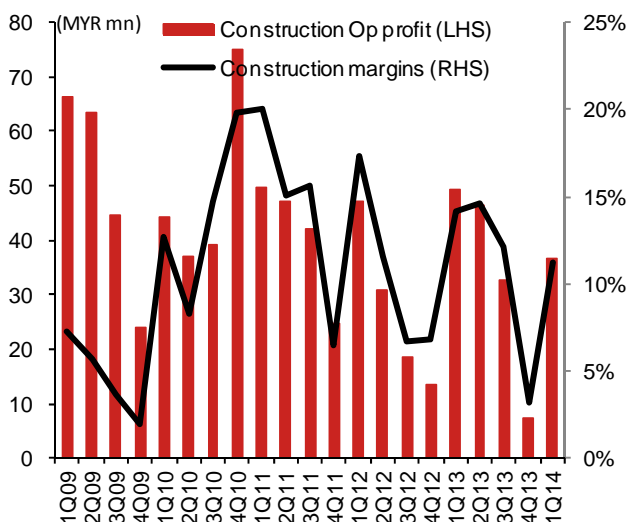
- The strongest segment, with Paradigm Mall generating MYR10mn of profits for WCT, and a small profit expected at Gateway@KLIA2 mall as well (vs expectations of a small loss earlier).
- Premiere Hotel loss making in 1Q14 due to lower occupancy rate (54%).

Fig. 2: WCT: 1Q14 earnings review

MYR mn	1Q14	1Q13	% chg y-y	4Q13	% chg q-q	FY14F	1Q % of FY14F
Turnover	467	491	(5%)	280	67%	1,878	25%
Construction	327	348	(6%)	233	40%	1,236	26%
Property Development	126	124	2%	33	284%	584	22%
Property Investment & Management	14	19	(29%)	15	(6%)	58	24%
Operating costs	(385)	(400)	(4%)	(247)	55%	(1,564)	25%
Finance costs	(15)	(15)	3%	(20)	(24%)	(96)	16%
Operating profit	67	82	(18%)	26	154%	249	27%
Construction	37	49	(25%)	7	392%	101	36%
Property Development	24	28	(15%)	12	96%	117	20%
Property Investment & Management	7	5	30%	7	(1%)	31	22%
Share of profit in associates / JCE	5	4	16%	8	(41%)	24	19%
Adjusted Pretax profit	57	72	(21%)	14	297%	176	32%
Taxation	(16)	(24)	(31%)	(12)	40%	(55)	29%
MI	0	(1)	NM	(2)	NM	0	NM
Reported NPAT	40	43	(7%)	56	(29%)	121	33%
Adj. NPAT (ex forex, revaluation)	40	49	(19%)	(30)	NM	121	33%
Operating margins (%)	14%	17%	-2 ppt	9%	5 ppt	13%	
Construction	11%	14%	-3 ppt	3%	8 ppt	8%	
Property Development	19%	23%	-4 ppt	37%	-18 ppt	20%	
Property Investment & Management	49%	27%	22 ppt	47%	2 ppt	53%	

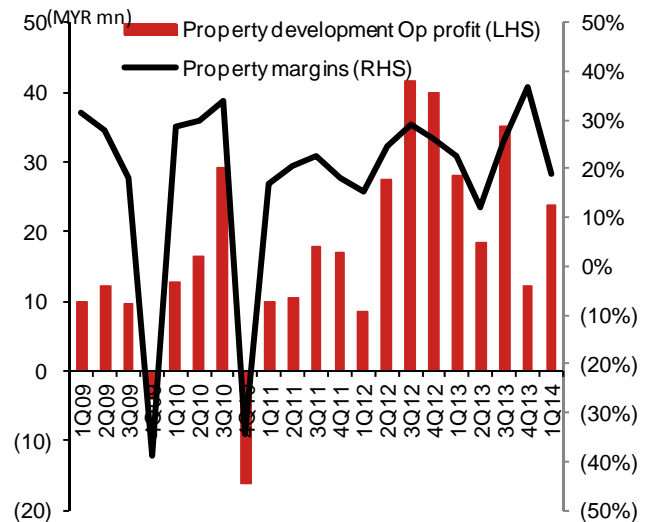
Source: Company data, Nomura estimates

Fig. 3: Construction profit and margins



Source: Company data, Nomura research

Fig. 4: Property development profit and margins



Source: Company data, Nomura research

Fig. 5: WCT: Current orderbook

Gulf States	MYR mn
Government Administrative Office, Qatar	479
New Doha Int'l Airport, Qatar (15%)	2
	481
Malaysia - Civil Engg and Infra	
PLUS Widening	310
Vale Industrial Civil works	4
Tun Razak Exchange	157
Others	15
	486
Malaysia - Building	
KK Medical Centre	203
Putrajaya Commercial Office	308
Ministry of international Trade (MITI)	231
Tuaran Hospital, Sabah	6
Others	70
	818
External orderbook	1,785
Outstanding external orderbook (FY13)	1,785
Orderbook burn rate (FY13)	1,168
IMPLIED CONSTRUCTION EARNINGS VISIBILITY (years)	1.5

Source: Company data, Nomura research

Fig. 7: Property sales in 1Q14 and target launches in 2014

Project	GDV (MYR mn)	1Q14 Sales (MYR mn)
BBT2 - Shop + serviced apartment	394	40
Bandar Parklands, Klang South	143	
Laman Greenville @ Klang South	439	120
Skyz Jelutong	146	
Paradigm Residences	483	60
A-60 Medini North	502	
Paradigm Johor Bahru	193	
One Medini Garden Villa	20	
Total	2,320	218

Source: Company data

Fig. 6: WCT: Tenderbook

Construction Contracts Targets 2014
MALAYSIA (Mgmt: ~MYR1bn, NMR: MYR600mn)
West Coast Expressway
Kwasa Damansara Land Civil Works (PDP)
Petronas RAPID Pengerang Civil Works –Phase 2
KL Sentral Linkway
Putrajaya Buildings
Mass Rapid Transit 2
KK Water Supply Scheme
KL - JB High Speed Rail
Southern Double Track
Hydro Electric Dam in Sarawak
Hydro Electric Dam in Sabah
MIDDLE EAST (Mgmt: ~MYR1bn, NMR: nil)
Qatar Roads and Expressways
Qatar Earthworks and Infrastructure works
Government Office Buildings in Qatar

Source: Company data, Nomura research

Fig. 8: Shopping malls and hotel occupancy

Paradigm Mall	
Retail space leased	99%
Avg footfalls per day	
Weekday	37,000
Weekend	61,000
Gateway Mall @KLIA2	
Retail space leased	80%
Avg footfalls per day	80,000
Premiere Hotel, Klang	
Occupancy	54%
Avg Room rate per day	MYR 267
Room to F&B Revenue	58 : 42

Source: Company data

Appendix A-1

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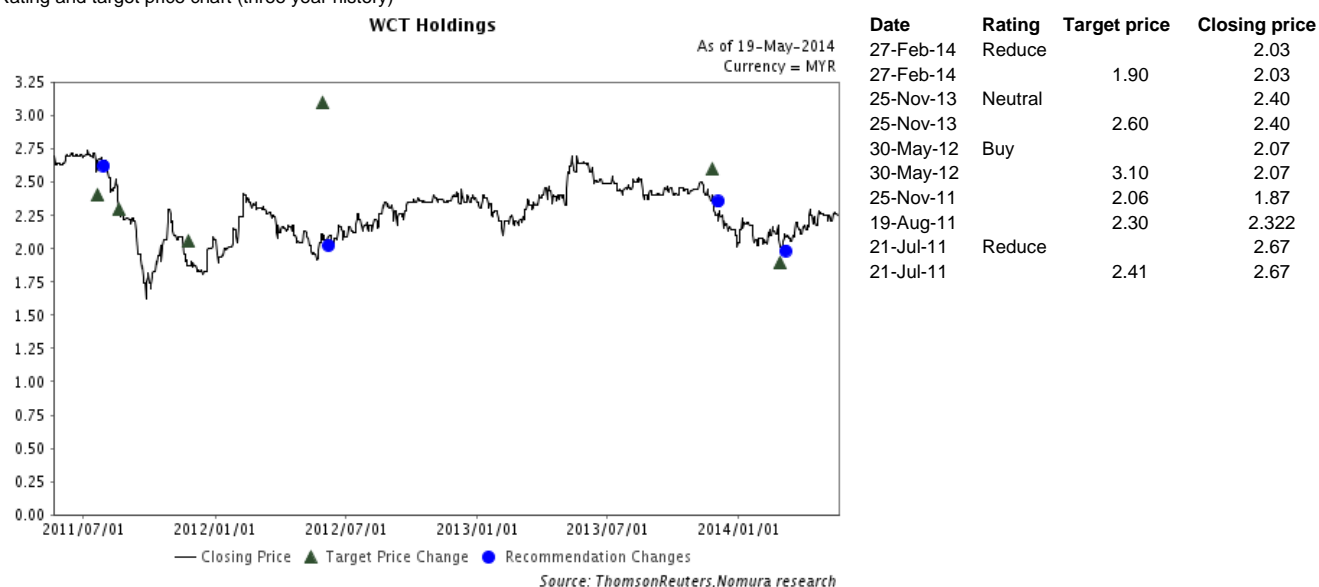
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Issuer	Ticker	Price	Price date	Stock rating	Sector rating	Disclosures
WCT Holdings	WCTHG MK	MYR 2.22	22-May-2014	Reduce	N/A	

WCT Holdings (WCTHG MK)

MYR 2.22 (22-May-2014) Reduce (Sector rating: N/A)

Rating and target price chart (three year history)



For explanation of ratings refer to the stock rating keys located after chart(s)

Valuation Methodology We value WCT using a sum-of-the-parts (SOTP) methodology derived from 1) Construction segment valued at 8.5x PE CY14F 2) NAV of property segment at a 13.4% discount rate; 3) the NAV of investments in malls and hotels at 11% discount rate; 4) NAV of India expressways at 9.2% discount rate; and 5) NAV of KLIA2 IC at 9.4% discount rate. Our SOTP calculation implies a valuation of MYR2.0bn for WCT's businesses. To this we add cash from warrants (~MYR700mn) to arrive at our price target of MYR1.90/share. The benchmark index for this stock is MSCI Malaysia.

Risks that may impede the achievement of the target price Key upside risks to our view stems from 1) New project awards larger than our estimates: We currently build in MYR600mn of total new projects in FY14F/15F/16F each. In case WCT is able to secure projects exceeding our assumed value (like the Kwasa Damansara land civil works, with both having EPF as a major shareholder), there might be upside risk to the stock. 2) Higher-than-expected margins for construction and property development: We have cut our margin assumptions on cost and labour pressures in Malaysia and the Middle East. However, if these were to reverse, it could pose an upside risk. 3) Higher-than-expected property sales 4) Arbitration wins (e.g. the Meydan Racecourse arbitration).

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