

Corporate Highlights

Sector Update

Construction

Bakun Cost Overrun And LAD Amicably Resolved?

Recom : **Overweight**
(Maintained)

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- ◆ We understand that the cost overrun and LAD issues with regards to the main civil works for the Bakun Hydroelectric Project (Bakun) are close to being amicably resolved.
- ◆ Recall, the RM1.8bn CW2 Package was in 2002 awarded to Malaysia-China Hydro Joint Venture, a consortium consisting of Sime Darby (35.7%), China National Water Resources and Hydropower Engineering Corporation (30%), WCT Engineering (7.7%), MTD Capital (7.7%), Ahmad Zaki Resources (7.7%), Syarikat Ismail Ibrahim Sdn Bhd (7.7%) and Edward & Sons Sdn Bhd (3.5%).
- ◆ For Sime Darby and WCT Engineering, the only two consortium members under our coverage, they in 2004 already provided RM132m and RM25m "foreseeable contract losses" respectively from the project, pending re-negotiation of the contract terms with the project owner, i.e. the Government.
- ◆ We understand that a deal has just been struck between the consortium and the Government whereby:
 1. Close to all cost overrun will be regarded as variation orders (VO);
 2. The VO will not be settled in cash, but in the form of an equity stake in Bakun (or in other words, "payment in kind" in the form of Bakun shares); and
 3. The liquidated and ascertained damages (LAD) arising from late delivery will be waived.
- ◆ If this is true, it will be positive to the consortium members in two ways:
 1. Assuming 80% of the cost overrun is "recoverable", i.e. regarded as VO, Sime Darby and WCT Engineering can write back provisions for cost overrun amounting to RM106m and RM20m respectively. These would boost Sime Darby's FY06/08 net profit by 9% or 4.2sen/share and WCT's FY12/07 net profit by 18% or 8.8sen/share; and

2. No or minimal further provisions for cost overrun from the project as additional cost overrun will likely be regarded as VO as well, while the LAD for late delivery is waived.

- ◆ The latest development, if it is true, will be positive to Sime Darby, WCT Engineering, MTD Capital and Ahmad Zaki Resources. We also understand that some of them may at some point cash out on their effective stakes in Bakun. For the construction sector as a whole, we maintain **Overweight** on the back of the booming construction markets in Malaysia, South Asia and the Gulf states, as well as the buoyant EPC market for power plants globally.

Construction Sector Earnings Table

	FYE	Price (RM/s)	EPS GWTH (%)		PER (x)		EV/EBITDA (x)		P/CF(x)		GDY (%)		Rec
			FY07	FY08	FY07	FY08	FY07	FY08	FY07	FY08	FY07	FY08	
Gamuda	Jul	8.60	-1.7	+>100	39.1	17.2	46.6	16.1	163.3	n.m	1.9	1.9	UP
Hock Seng Lee	Dec	4.08	16.6	25.9	11.8	9.4	6.1	4.7	13.9	10.7	3.7	3.9	OP
Prinsiptek	Dec	1.03	-3.1	35.4	7.5	5.5	8.6	6.2	6.4	5.0	3.4	3.9	OP
MRCB	Dec	2.60	98.5	51.8	30.7	20.2	18.4	16.8	n.m	115.0	0.0	0.0	MP
Zelan^	Jan	12.20	80.3	26.9	23.6	18.6	15.9	12.1	24.0	19.3	1.2	1.2	OP
IJM^	Mar	8.65	16.6	15.5	19.5	16.9	10.5	9.3	n.m	12.2	1.7	1.7	UP
WCT	Dec	7.40	14.5	35.6	15.6	11.5	9.0	6.9	15.7	12.0	2.0	2.0	OP
Sector Avg			21.3	52.2	25.7	16.9							

^ FY07-08 valuations refer to those of FY08-09

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Trading Buy = Short-term positive development on the stock that could lead to a re-rating in the share price and translate into an absolute return of 15% or more over a period of three months, but fundamentals are not strong enough to warrant an Outperform call. It is generally for investors who are willing to take on higher risks.

Market Perform = The stock return is expected to be in line with the KLCI benchmark (+/- five percentage points) over the next 6-12 months.

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Overweight = Industry expected to outperform the KLCI benchmark, weighted by market capitalisation, over the next 6-12 months.

Neutral = Industry expected to perform in line with the KLCI benchmark, weighted by market capitalisation, over the next 6-12 months.

Underweight = Industry expected to underperform the KLCI benchmark, weighted by market capitalisation, over the next 6-12 months.

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