



Outthink. Outperform.

Seasonally slow quarter

HSS achieved net profit of RM3.2m (-56% qoq) in 1Q17, accounting for 19% of our RM16.7m estimate in FY17. This is within our expectation as HSS experiences a slow start traditionally early in the year like the rest of the construction industry. Revenue declined 20% qoq to RM29.3m (4Q16: RM36.7m) due to slower progress for ongoing projects during the festive period. We maintain our BUY call on HSS with a TP of RM1.20 based on CY18E PER of 15x, giving a potential upside of 33%. Net cash of RM24.7m or RM0.08/share supports net yield of 1.9% in FY17E, reasonable for a growth company.

Slow quarter traditionally

There is no comparative 1Q16 figures as HSS just listed in August 2016. Hence, only qoq change is available. Revenue declined 20% qoq to RM29.3m (4Q16: RM36.7m) as we are comparing the strongest fourth quarter to the weakest first quarter traditionally. The decline is attributable to slow progress for ongoing projects due to the festive period. Meanwhile, EBIT saw a sharp contraction of 53% qoq to RM9.8m due to higher other operating expenses (+44 qoq). Net profit declined 56% qoq to RM3.2m due to high tax rate of 30.6% in 1Q17 as there were non-deductible expenses.

Within our expectation and no changes in earnings forecasts

Net profit of RM3.2m in 1Q17 comprises 19% of our RM16.7m estimate in FY17E. This is within our expectation as 1Q is seasonally weak quarter. We maintain our earnings forecasts assuming HSS will secure additional contracts worth RM150m in 2017. We expect better performance in subsequent quarters, given its high outstanding order book of RM406m.

Maintain BUY with unchanged TP of RM1.20

We maintain our BUY call and target price of RM1.20, giving potential upside of 33%. Our TP is based on CY18E PER of 15x, a discount of about 20% to the weighted average PER of 18.6x for global peers. Its net cash of RM24.7m or RM0.08/share supports our assumed dividend payout ratio of 30% in FY17E. Net yield of 1.9% is reasonable for a growing company.

Key downside risks to our call

i) Litigation actions from MAHB and MRCB, but they are insured by Professional Indemnity Insurance (PII) up to RM10m per annum, ii) earnings lag due to timing of contract wins; iii) execution risks involved in its expansion plans; iv) slowdown in construction contract awards.

Earnings & Valuation Summary

FYE 31 Dec	2015A	2016A	2017E	2018E	2019E
Revenue (RMm)	121.5	139.0	147.2	226.4	274.9
EBITDA (RMm)	13.0	19.4	25.2	34.1	39.4
Pretax profit (RMm)	13.7	19.9	25.9	35.7	41.5
Net profit (RMm)	10.1	14.0	18.3	25.3	29.4
EPS (sen)	4.0	5.0	5.7	7.9	9.2
PER (x)	23.4	18.7	16.2	11.7	10.1
Core net profit	9.8	14.3	18.3	25.3	29.4
Core EPS (sen)	3.9	4.5	5.7	7.9	9.2
Core EPS growth (%)	7.6	16.5	28.0	38.0	16.2
Core PER (x)	24.1	20.7	16.2	11.7	10.1
Net DPS (sen)	0	0.6	1.7	2.4	2.8
Dividend Yield (%)	0	0.7	1.9	2.6	3.0
EV/EBITDA (x)	18.4	14.0	9.9	7.3	6.0
Chg in EPS (%)			0.0	0.0	0.0
Affin core/Consensus (x)				NA	NA

Source: Company, Bloomberg, AffinHwang estimates

Results Note

HSS Engineers

HSS MK

Sector: Engineering Construction

RM0.90 @ 26 May 2017

BUY(maintain)

Upside: 33%

Price Target: RM1.20

Previous Target: RM1.20



Price Performance

	1M	3M	12M
Absolute	-9.1%	+59.8%	-
Rel to KLCI	-9.2%	+53.3%	-

Stock Data

Issued shares (m)	319.1
Mkt cap (RMm)/(US\$m)	285.6/66.9
Avg daily vol - 6mth (m)	2.5
52-wk range (RM)	0.39-1.02
Est free float	78.2%
BV per share (RM)	0.25
P/BV (x)	3.63
Net cash/(debt) (RMm) (1Q17)	24.7
ROE (2017E)	20%
Derivatives	Nil
Shariah Compliant	No

Key Shareholders

Datuk Ir Kunasingam	31.3%
Dato' Ir Nitchiananthan	2.7%

Source: Company, Bloomberg

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Fig 1: Results comparison

FYE 31 Dec (RMm)	2Q16	3Q16	4Q16	1Q17	% QoQ	Comment
Revenue	33.6	36.5	36.7	29.3	(20.2)	The decline is attributable to slower progress for ongoing projects due to the festive period. Traditionally, the weakest quarter.
Op costs	(28.2)	(33.7)	(26.5)	(24.4)	(8.0)	
EBITDA	5.5	2.8	10.1	4.8	(52.3)	A sharp contraction of 53% qoq to RM9.8m due to higher other operating expenses (+44 qoq).
<i>EBITDA margin (%)</i>	16.2	7.7	27.6	16.5	(11.1ppt)	
Depn and amort	(0.4)	(0.4)	(0.4)	(0.3)	(25.1)	
EBIT	5.1	2.4	9.8	4.6	(53.3)	
Interest income	0.1	0.2	0.3	0.4	48.4	
Interest expense	(0.4)	(0.4)	(0.3)	(0.3)	21.6	Higher tax rate than the statutory tax of 24%, mainly due to lower profit achieved in the first quarter and recurring non-deductible expenses such as legal fees.
Associates	0.0	0.1	(0.0)	0.1	NA	
Forex gain (losses)	0.0	0.0	0.1	(0.0)	NA	
Exceptional items	0.0	0.0	(0.2)	(0.1)	(60.5)	
Pretax profit	4.8	2.3	9.6	4.5	(53.0)	
Core pretax	4.8	2.3	9.7	4.7	(52.1)	
Tax	(1.5)	(0.8)	(2.5)	(1.4)	(45.3)	
<i>Tax rate (%)</i>	31.8	36.3	25.9	30.6	4.7ppt	
Net profit	3.3	1.5	7.1	3.2	(55.7)	
Core net profit	3.2	1.5	7.2	3.3	(54.4)	
EPS (sen)	1.3	0.6	2.5	1.0	(60.7)	

Source: Affin Hwang, Company data

Equity Rating Structure and Definitions

BUY	Total return is expected to exceed +10% over a 12-month period
HOLD	Total return is expected to be between -5% and +10% over a 12-month period
SELL	Total return is expected to be below -5% over a 12-month period
NOT RATED	Affin Hwang Investment Bank Berhad does not provide research coverage or rating for this company. Report is intended as information only and not as a recommendation

The total expected return is defined as the percentage upside/downside to our target price plus the net dividend yield over the next 12 months.

OVERWEIGHT	Industry, as defined by the analyst's coverage universe, is expected to outperform the KLCI benchmark over the next 12 months
NEUTRAL	Industry, as defined by the analyst's coverage universe, is expected to perform inline with the KLCI benchmark over the next 12 months
UNDERWEIGHT	Industry, as defined by the analyst's coverage universe is expected to under-perform the KLCI benchmark over the next 12 months

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