Mercury Securities Sdn Bhd

RESULTS REPORT

22 Feb 2013

PBA Holdings Berhad		***Market Price:***	*RM0.87*
		Market Capitalisation:	*RM288.2m*
		Board:	*Main Market*
Recommendation:	*HOLD*	***Sector:***	*Trading / Services*
Target Price:	*RM0.90*	***Stock Code/Name:***	*5041 / PBA*

Analyst: *Edmund Tham*

KEY FINANCIALS

Key Stock Statistics	2013F
Earnings/Sh. (sen)	10.0
P/E Ratio (x)	8.7
Net Dividend/Share (sen)	3.8
NTA/Share (RM)	2.14
Book Value/Share (RM)	2.14
Issued Capital (mil shares)	331.3
52-weeks share price (RM)	0.865 – 0.98
Major Shareholders:	%
.State Secretary, Penang	54.96
.Perbadanan Pembangunan P.P.	9.99
.	

**RM0.50 par value*
**2013 figures are our estimates*

Ratios Analysis	2010	2011	2012	2013F
Book Value/Sh. (RM)	1.96	2.06	2.08	2.14
Earnings/Sh. (sen)	7.9	13.8	8.7	10.0
Net Dividend/Sh. (sen)	3.0	3.5	3.8	3.8
Div. Payout Ratio (%)	37.9	25.4	42.9	37.6
P/E Ratio (x)	11.0	6.3	9.9	8.7
P/Book Value (x)	0.44	0.42	0.42	0.41
Dividend Yield (%)	3.4	4.0	4.3	4.3
ROE (%)	4.0	6.7	4.2	4.7
Net Gearing (or Cash)(x)	0.01	(0.01)	(0.01)	(0.02)

** Net Gearing figure here includes the amount owed by PBA to the Penang State government*

P&L Analysis (RM mil)	2010	2011	2012	2013F
FY end: Dec 31				
Revenue	198.5	236.3	244.6	256.2
Operating Profit	29.5	39.9	21.5	23.5
Depreciation	(38.2)	(49.7)	(48.2)	(49.1)
Interest Expenses	(0.02)	(0.05)	0.00	0.00
Pre-tax Profit (PBT)	30.8	42.4	23.7	25.9
Effective Tax Rate (%)	14.9	n.m.	n.m.	n.m.
Net Profit after Tax	26.2	45.7	29.0	33.2
Operating Margin (%)	14.8	16.9	8.8	9.2
Pre-tax Margin (%)	15.5	17.9	9.7	10.1
Net Margin (%)	13.2	19.3	11.8	13.0

**n.m.=not meaningful due to tax credits*
**Op.profit=EBIT+Other Income*

PERFORMANCE – 4Q/FY12

4Q/ 31 Dec	4Q12	4Q11	yoy %	3Q12	qoq%
Rev (RMm)	62.3	56.1	10.9	60.0	3.7
EBIT (RMm)	(2.7)	(3.8)	28.3	(1.7)	(59.1)
NPAT (RMm)	7.1	16.7	(57.6)	3.2	123.5
EPS* (sen)	2.1	5.1	(57.6)	1.0	123.5

12M/ 31 Dec	FY12	FY11	yoy %
Rev (RMm)	244.6	236.3	3.5
EBIT (RMm)	11.0	21.4	(48.6)
NPAT(RMm)	29.0	45.7	(36.6)
EPS* (sen)	8.7	13.8	(36.6)

^EBIT excludes Other Income; NPAT=net profit after tax.
**based on 331.3 million shares*

"Q4 – revenue in-line, NPAT below"

PBA's 4Q/FY12 revenue (for quarter ended 31st December 2012) was in-line with our earlier expectations but NPAT was below. This was the same scenario as in the past 2 quarters.

"Higher costs and lower investment income"

The group recorded revenue of RM62.3 million and NPAT of RM7.1 million during 4Q/FY12. Revenue had increased by 10.9% y-o-y while NPAT dropped by 57.6% y-o-y. The increased revenue was mainly due to the increase in water consumption. The decrease in NPAT was mainly due to decrease in investment income and the increase in the administrative and depreciation expenses. We also note the substantial fees paid to the Penang State Government and SPAN (Suruhanjaya Perkhidmatan Air Negara), and the leasing charges paid to PAAB (Pengurusan Asset Air Bhd).

OUTLOOK/CORP. UPDATES

In tandem with the steady growth in the domestic economy (in GDP terms), we expect that the group's **water revenues would grow** as well. Water is a relatively inexpensive expenditure, and we foresee that the demand would grow steadily, including for trade (commercial / industry) users. The influx of FDI (foreign direct investment) into various high-tech and manufacturing sectors within the state of Penang could lead to higher water usage by trade consumers. Nevertheless, PBA's management is aware and mindful of both **economic conditions and escalating costs.**

"Domestic economy holding up"

Malaysia's official government figures show a full year 2012 GDP growth of 5.1% and an expected 2013 GDP growth of 4.5-5.5%. Bank Negara Malaysia (BNM) has still maintained its accommodative overnight policy rate (OPR) at 3.0%. The external environment (particularly in the US, Japan and Europe) has remained lackluster.

PBA's management had planned-well for the coming years, with the implementation of new **trade tariffs** and **WCS** (Water Conservation Surcharge). It has also planned ahead in terms of capital expenditure (capex) and measures needed to lower NRW levels. We are pleased that PBA practises an open-tender system for its infrastructure maintenance work, papers used for billing, safety equipment, stationeries, IT services, CCTVs, machinery procurement and pipe-laying. In the long run, this practice usually leads to improved cost savings.

During FY12, the group's subsidiary company had impaired its assets amounting to RM2.3 million (mainly the Telok Bahang conventional treatment plant which is no longer operational - RM0.2 million and the raw water intake at Sungai Perai - RM1.9 million).

VALUATION/CONCLUSION

"FY12 final dividend – higher than expected"

In January 2013, PBA had paid out an interim single tier dividend of 3.5% amounting to approximately RM5.8 million for its FY12. Now, the BOD had recommended a final single tier dividend of 4.0% amounting to approximately RM6.6 million. This was slightly above our expectations. Meanwhile, we expect that PBA would maintain a dividend payout of around 30% for its FY13.

"Price movement mirrors KLCI"

In 2013 thus far, PBA (-4.4%) has **mirrored the KLCI** (-4.0%). Market conditions have also been volatile during the past year, impacted by the Arab Spring uprisings in the Middle East/North Africa, Sovereign Debt issue in Europe, Debt Ceiling & Fiscal Cliff issues in the US and Tohoku natural disaster in Japan. Nevertheless, as PBA is not a large market-cap stock, this may put a dampener on its market visibility and trading volume.

"Maintain Hold Call"

Based on our forecast of PBA's FY13 EPS and an estimated P/E of 9 times, we set a FY13-end **Target Price (TP) of RM0.90**. Being cautious, we maintain our Hold Call. This TP still offers 3.4% upside from its market price at the date of this report. Our TP for PBA reflects a P/BV of 0.42 times over its FY13F BV/share.

"Undemanding valuations"

We find that PBA's P/E and P/BV valuations are quite undemanding, while it has reasonable ROEs and solid dividend yields. The group's gearing levels were very minimal, subsequently turning into a **net cash position** during its FY11. Furthermore, our Net Gearing computation still includes the amount owed by PBA to the Penang State government.

"Unknown variable – management strategy on the utilization of deferred tax assets"

Our FY13F NPAT forecast takes into account our assumption that PBA's management plans to **recognize some deferred tax assets to offset against its income tax expenses**. Currently, we are unaware of PBA's actual management stance or strategy on this matter. This causes a highly unpredictable variable in forecasting the group's NPAT. During FY12, the group recognised RM14.8 million of its deferred tax assets (unutilised reinvestment allowances).

To recap – the deferred tax assets were derived from the group's **unutilised reinvestment allowances**. According to the group's latest Interim Financial Report, the unutilised reinvestment allowance of the group available indefinitely for off-setting against future taxable profits amounted to a huge amount of RM410.3 million.

"Impact of new major expenditures"

We are also naturally concerned on the **impact of the "new" major expenditures** – Water Intake Fees (to Penang State government), Leasing Charges (to PAAB) and License Fees (to SPAN - Suruhanjaya Perkhidmatan Air Negara). The timing and quantum of these payments could cause **lumpiness in its quarterly earnings.**

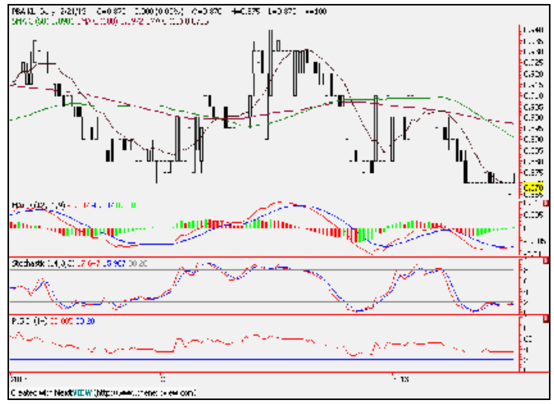
"New" major expenditures

Payee	4Q/FY12 (RM'mil)	FY12 (RM'mil)
State Govt	2.1	8.1
PAAB	3.2	13.0
SPAN	0.6	2.3

Source: PBA

PBA's businesses also face possible **routine risk factors** such as a possible slower rate of economic growth, weak trade consumer demand, foreign exchange fluctuations and rising costs — e.g. electricity tariffs, oil/gas fuel, water treatment chemicals, pipe replacement (probably using steel /ductile iron /copper /asbestos cement /HDPE /others) and bottling (plastic). We also note that PBA holds investments in the equity markets that are managed by external fund management companies. As in any investment, there would be risks from equity market fluctuations as well.

PBA: Share Price



Source: NextView

APPENDIX – "New" Major Expenditures

Water Intake Fees

In June 2011, PBAPP, a wholly-owned subsidiary company of PBA, had been charged by the Penang State Government for **Water Intake Fees** at RM0.03 per cubic metre of production volume with effect from 1st January 2011 (i.e. backdated). This fee is payable for the period 2011-2013.

License Fees

PBAPP had been awarded by the Suruhanjaya Perkhidmatan Air Negara (SPAN) on 2nd June 2011 for **Service & Facility Licenses** issued pursuant to Section 9 of the Water Services Industry Act (WISA) 2006. The License shall be effective from 1st June 2011 to 31st May 2014. The License Fee is calculated based on 1% of the revenue from the sale of water by the subsidiary.

Leasing Charges

On 2nd June 2011, PBAPP had entered into a **Facility Agreement and a Leasing Agreement with Pengurusan Asset Air Bhd** (PAAB) to enable PBAPP to carry out water supply services on the land leased from PAAB. The amount of leasing charges is RM14.56 million per annum for a period of 45 years with effect from 1st August 2011.

The land leased has a net book value of RM655.3 million at the date of the agreements. To recap, PAAB would act as the "debtor" for federal loans. In return, the State of Penang would alienate its water assets to PAAB and in-turn, PAAB would lease it back to PBAPP and thus PBAPP would pay an annual lease to PAAB.

Upon notification by PAAB and subject to PBAPP's ability to secure the costs of fund equivalent or lower than that secured by PAAB and provided the approval of Suruhanjaya Perkhidmatan Air Negara (SPAN) has been obtained, PBAPP shall have the first right to construct, upgrade, and refurbish at its own costs and expense the Water Assets and New Water Assets for water supply services. PBAPP, being the state water operator, would be allowed to focus solely on providing water treatment and distribution services, while the Malaysian Federal Government will be fully responsible for the source work of water supply projects.