

25 August 2017

Technology | Software &amp; Services

## Prestariang

**Buy (Maintained)**

### SKIN May Start In 4Q17

Target Price:	MYR2.29
Price:	MYR1.75
Market Cap:	USD197m
Bloomberg Ticker:	PRES MK

**Prestariang's 1H17 core earnings of MYR9m fell below expectations. That said, we are hoping for a much better showing in 2H17 on potential breakeven of its university, as well as likely commencement of construction revenue recognition under SKIN come 4Q17. We reiterate our BUY call with a lower SOP-based TP of MYR2.29 (from MYR2.63, 31% upside) following our earnings revision and as we update our assumptions for SKIN.**

**2Q17 results review.** 2Q17 numbers are generally higher on both QoQ and YoY basis, lifted by higher off-take at its software and services division, as well as its academy segment. 1H17 core earnings of MYR9m, however, still fell short of both our/consensus expectations at 28/32% of full-year estimates respectively, as overall orders remained slower than expected. A second interim DPS of MYR0.01 was declared, bringing its 1H17 DPS to MYR0.0175 at an implied payout ratio of 94% (vs MYR0.015 in 1H16 at 119% payout).

**Next milestone for the National Immigration Control System (SKIN).** With the concession agreement now signed, we expect Prestariang to fulfil the conditions precedent (including finalising the funding options as well as its potential technical partnership with Thales Group from France) within the next 3-4 months. We estimate that Prestariang may outsource some EUR50-60m worth of works to the latter, which implies 30-40% of the total works involved. With regards to the debt funding, management is currently exploring several options including issuance of Islamic medium term notes or drawdown of term loans at a potential interest rate of 5-7%. As for the equity portion, we believe it could come in the form of some hybrid equity structure such as preference shares or loan stocks. These would likely be convertible into ordinary shares at the SKIN project level in Year 4 when the system officially commissions.

**University to return to the black.** Prestariang's university currently houses 400 students following a major intake in April with 200 sign-ups. We expect this to scale up further to 600 students by end-2017. We reiterate our view that this would likely propel the unit to break even at PBT level by 4Q17. This was after being in the red since its launch in 2013 (2Q17 PBT loss: MYR0.9m).

**Forecasts and risks.** We trim our FY17F-18F EPS by 11-15% after factoring in slower run-rate under its existing contracts as well as lowering our construction revenue recognition. Management guided that SKIN's profit recognition would follow the typical construction S-curve. As such, we foresee a heavier attribution in FY19 (EPS raised by 6%). Key risks include a further slowdown in existing contracts, more delays in new job awards and prolonged losses at its university.

**Maintain BUY** with our SOP-based TP lowered to MYR2.29 (from MYR2.63) following our earnings revision, and as we lowered our margin assumptions for SKIN to reflect our more conservative stance, as we acknowledge that the learning curve could be steep. Given the upside, we continue to advise investors to accumulate the stock as we expect a successful rollout of new initiatives (such as SKIN and EduCloud) over the medium term to mark a paradigm shift for Prestariang in the long run.

#### Share Data

Avg Daily Turnover (MYR/USD)	1.77m/0.41m
52-wk Price low/high (MYR)	1.62 - 2.45
Free Float (%)	50
Shares outstanding (m)	484
Estimated Return	31%

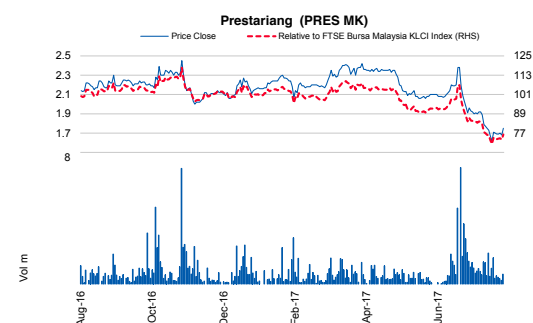
#### Shareholders (%)

Dr Abu Hasan Ismail	27.3
Retirement Fund Inc (KWAP)	13.1
AIA	9.7

#### Share Performance (%)

	YTD	1m	3m	6m	12m
Absolute	(15.1)	(11.2)	(24.3)	(15.5)	(16.7)
Relative	(23.2)	(12.0)	(24.6)	(20.0)	(22.3)

Source: Bloomberg



Source: Bloomberg

Forecasts and Valuations	Dec-15	Dec-16	Dec-17F	Dec-18F	Dec-19F
Total turnover (MYRm)	115	132	200	443	617
Reported net profit (MYRm)	17.2	8.9	27.5	63.7	78.7
Recurring net profit (MYRm)	17.2	8.9	27.5	63.7	78.7
Recurring net profit growth (%)	(14.8)	(48.4)	209.5	131.6	23.6
Recurring EPS (MYR)	0.04	0.02	0.06	0.13	0.16
DPS (MYR)	0.04	0.03	0.07	0.07	0.07
Recurring P/E (x)	49.2	95.3	30.8	13.3	10.8
P/B (x)	5.00	5.26	5.48	4.59	3.69
P/CF (x)	75	843	37	19	11
Dividend Yield (%)	2.1	1.7	4.0	4.0	4.0
EV/EBITDA (x)	28.9	52.1	21.1	10.0	8.6
Return on average equity (%)	10.2	5.4	17.4	37.6	38.1
Net debt to equity (%)	net cash	net cash	net cash	77.0	164.6
Our vs consensus EPS (adjusted) (%)			(3.1)	1.5	10.4

Source: Company data, RHB

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## Financial Exhibits

Financial model updated on : 2017-08-25.

Asia	<b>Financial summary</b>	<b>Dec-15</b>	<b>Dec-16</b>	<b>Dec-17F</b>	<b>Dec-18F</b>	<b>Dec-19F</b>
Malaysia	Recurring EPS (MYR)	0.04	0.02	0.06	0.13	0.16
Technology	EPS (MYR)	0.04	0.02	0.06	0.13	0.16
<b>Prestariang</b>	DPS (MYR)	0.04	0.03	0.07	0.07	0.07
Bloomberg      PRES MK	BVPS (MYR)	0.35	0.33	0.32	0.38	0.47
<b>Buy</b>	Weighted avg adjusted shares (m)	484	484	484	484	484
<b>Valuation basis</b>	<b>Valuation metrics</b>	<b>Dec-15</b>	<b>Dec-16</b>	<b>Dec-17F</b>	<b>Dec-18F</b>	<b>Dec-19F</b>
Prestariang is valued on an SOP basis	Recurring P/E (x)	49.2	95.3	30.8	13.3	10.8
<b>Key drivers</b>	P/E (x)	49.2	95.3	30.8	13.3	10.8
Potential award of new jobs, recovery in orders under its existing contracts	P/B (x)	5.00	5.26	5.48	4.59	3.69
<b>Key risks</b>	FCF Yield (%)	0.9	(0.3)	(4.9)	(18.6)	(30.3)
Further weakness in its university enrolment, delay in securing new jobs	Dividend Yield (%)	2.1	1.7	4.0	4.0	4.0
<b>Company Profile</b>	EV/EBITDA (x)	28.9	52.1	21.1	10.0	8.6
Prestariang provides ICT services focused on professional training and certification with industry partners such as Microsoft, IBM, Oracle and Autodesk. It has also ventured into the provision of training for the oil & gas sector.	EV/EBIT (x)	31.1	59.4	22.3	10.4	8.9
	<b>Income statement (MYRm)</b>	<b>Dec-15</b>	<b>Dec-16</b>	<b>Dec-17F</b>	<b>Dec-18F</b>	<b>Dec-19F</b>
	Total turnover	115	132	200	443	617
	Gross profit	39	32	58	116	154
	EBITDA	25	14	39	103	155
	Depreciation and amortisation	(2)	(2)	(2)	(4)	(4)
	Operating profit	23	12	37	99	151
	Net interest	(0)	(0)	(0)	(7)	(21)
	Pre-tax profit	22	12	36	86	109
	Taxation	(5)	(2)	(4)	(6)	(8)
	Minority interests	0	(0)	(4)	(16)	(22)
	Recurring net profit	17	9	27	64	79
	<b>Cash flow (MYRm)</b>	<b>Dec-15</b>	<b>Dec-16</b>	<b>Dec-17F</b>	<b>Dec-18F</b>	<b>Dec-19F</b>
	Change in working capital	(8)	(10)	(11)	(39)	(28)
	Cash flow from operations	11	1	23	45	77
	Capex	(3)	(3)	(64)	(202)	(333)
	Cash flow from investing activities	26	(0)	(64)	(202)	(333)
	Dividends paid	(11)	(17)	(34)	(34)	(34)
	Cash flow from financing activities	(11)	(18)	18	138	250
	Cash at beginning of period	106	88	58	34	14
	Net change in cash	26	(17)	(24)	(20)	(7)
	Ending balance cash	132	71	34	14	7
	<b>Balance sheet (MYRm)</b>	<b>Dec-15</b>	<b>Dec-16</b>	<b>Dec-17F</b>	<b>Dec-18F</b>	<b>Dec-19F</b>
	Total cash and equivalents	129	109	85	66	59
	Tangible fixed assets	13	12	74	272	602
	Intangible assets	5	7	7	7	7
	Total other assets	1	1	1	1	1
	Total assets	204	198	254	495	863
	Short-term debt	0	0	0	0	0
	Total long-term debt	1	0	52	223	507
	Other liabilities	1	1	1	1	1
	Total liabilities	35	37	95	290	591
	Shareholders' equity	169	161	155	184	229
	Minority interests	0	0	4	21	43
	Total equity	170	162	159	205	272
	Net debt	(128)	(109)	(33)	158	448
	Total liabilities & equity	204	198	254	495	863
	<b>Key metrics</b>	<b>Dec-15</b>	<b>Dec-16</b>	<b>Dec-17F</b>	<b>Dec-18F</b>	<b>Dec-19F</b>
	Revenue growth (%)	46.5	14.4	51.2	121.6	39.5
	Recurrent EPS growth (%)	(14.8)	(48.4)	209.5	131.6	23.6
	Gross margin (%)	33.5	24.5	28.8	26.3	25.0
	Operating EBITDA margin (%)	21.6	10.7	19.4	23.3	25.1
	Net profit margin (%)	14.9	6.7	13.8	14.4	12.8
	Dividend payout ratio (%)	105.4	163.4	123.2	53.2	43.0
	Capex/sales (%)	3.0	2.6	32.2	45.6	54.0
	Interest cover (x)	71.5	27.5	81.1	15.1	7.1

Source: Company data, RHB

**Figure 1: Prestariang's SOP valuation (MYRm)**

SKIN* concession value (m)	628.9
Existing stake in SKIN	70.0%
Value attributable to Prestariang (m)	440.2
<b>Assuming 10% placement of new shares at SKIN level to raise equity funding</b>	
Prestariang's potential stake in SKIN	63.6%
Potential value attributable to Prestariang (m)	400.2
2018F earnings (ex-construction profit from SKIN concession) (m)	35.4
2018F P/E (x)	20
Implied equity value (m)	708.9
Current share base (m)	484.0
TP (MYR)	2.29

Note:\* SKIN = National Immigration Control System

Source: RHB

**Figure 2: Valuation estimate for the SKIN concession (MYRm)**

	Yr 1	Yr 2	Yr 3	Yr 4	Yr 5	Yr 6	Yr 7	Yr 8	Yr 9	Yr 10	Yr 11	Yr 12	Yr 13	Yr 14	Yr 15
Total capex	821.0														
Debt portion	80%														
Interest rate	6%														
EBIT				108.5	108.5	108.5	108.5	108.5	108.5	108.5	108.5	108.5	108.5	108.5	108.5
Depreciation				68.4	68.4	68.4	68.4	68.4	68.4	68.4	68.4	68.4	68.4	68.4	68.4
(-) Tax				(41.3)	(37.7)	(34.1)	(30.5)	(26.9)	(23.3)	(19.7)	(16.1)	(12.6)	(9.0)	(5.4)	(1.8)
(-) Working Capital				0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
(-) Interest repayment				(5.0)	(5.0)	(5.0)	(5.0)	(5.0)	(5.0)	(5.0)	(5.0)	(5.0)	(5.0)	(5.0)	(5.0)
(-) Principal repayment				(59.8)	(59.8)	(59.8)	(59.8)	(59.8)	(59.8)	(59.8)	(59.8)	(59.8)	(59.8)	(59.8)	(59.8)
FCFE				70.8	74.4	78.0	81.6	85.2	88.8	92.4	96.0	99.5	103.1	106.7	110.3
Risk free rate	4.0%														
Market risk premium	4.9%														
Beta (x)	0.70														
<b>Cost of equity</b>	<b>7.4%</b>														
Concession value	628.9														

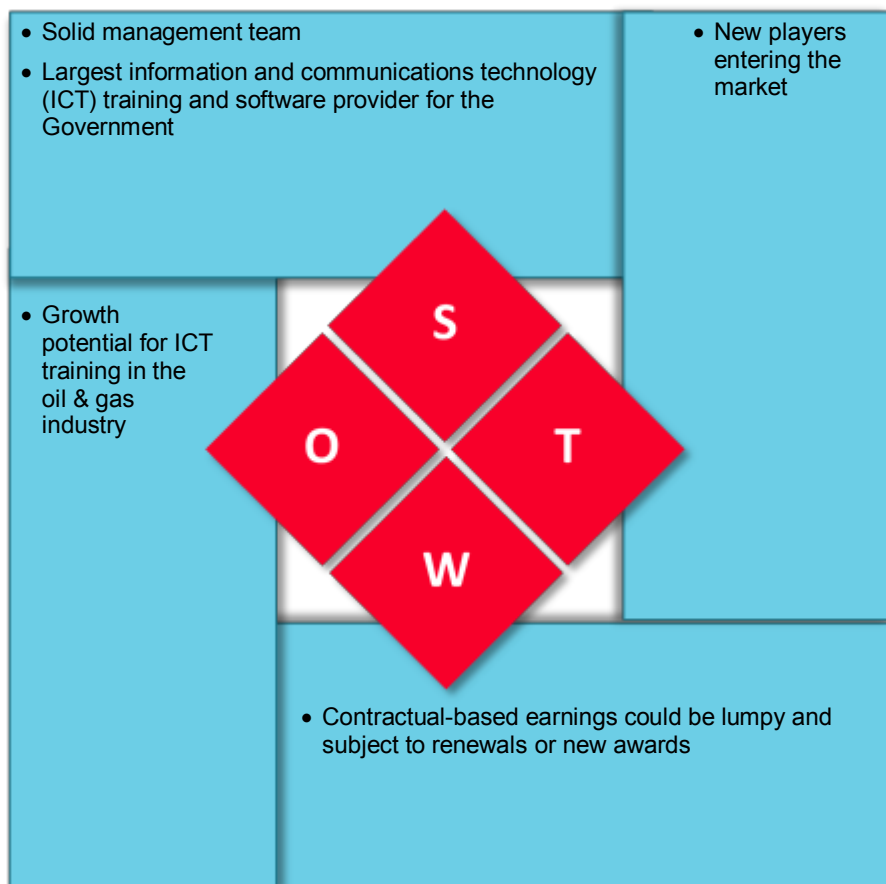
Source: RHB

Figure 3: Prestariang's quarterly results review

FYE Dec (MYRm)	2Q16	1Q17	2Q17	QoQ (%)	YoY (%)	1H16	1H17	YoY (%)	Comments
<b>Revenue</b>	<b>48.8</b>	<b>43.9</b>	<b>55.2</b>	<b>25.8</b>	<b>13.1</b>	<b>89.5</b>	<b>99.1</b>	<b>10.7</b>	1H17 topline growth driven by higher contributions from its software and services division
<b>EBITDA</b>	<b>5.1</b>	<b>4.4</b>	<b>7.6</b>	<b>73.2</b>	<b>49.7</b>	<b>9.3</b>	<b>12.0</b>	<b>28.2</b>	Profitability too improved on higher economies of scale
<i>EBITDA margin (%)</i>	<i>10.4</i>	<i>10.0</i>	<i>13.7</i>			<i>10.4</i>	<i>12.1</i>		
Depreciation	(0.4)	(0.4)	(0.5)	9.4	11.5	(0.8)	(0.9)	6.5	
<b>EBIT</b>	<b>4.7</b>	<b>4.0</b>	<b>7.1</b>	<b>80.0</b>	<b>53.1</b>	<b>8.5</b>	<b>11.1</b>	<b>30.4</b>	
<i>EBIT margin (%)</i>	<i>9.5</i>	<i>9.0</i>	<i>12.9</i>			<i>9.5</i>	<i>11.2</i>		
Interest expense	(0.0)	(0.1)	(0.0)	(78.7)	2,800.0	(0.1)	(0.2)	184.5	
Interest income	0.0	0.0	0.0	Nm	Nm	0.0	0.0	Nm	
Associates	0.0	0.0	0.0	Nm	Nm	0.0	0.0	Nm	
EI/Others	0.4	0.0	0.0	Nm	(100.0)	0.6	0.0	(100.0)	
<b>Pretax profit</b>	<b>5.0</b>	<b>3.8</b>	<b>7.1</b>	<b>85.7</b>	<b>41.1</b>	<b>9.1</b>	<b>10.9</b>	<b>20.2</b>	
<i>Pretax margin (%)</i>	<i>10.3</i>	<i>8.7</i>	<i>12.8</i>			<i>10.1</i>	<i>11.0</i>		
Tax	(1.3)	(0.6)	(1.4)	125.1	3.2	(2.3)	(2.0)	(15.8)	
<i>Effective tax rate (%)</i>	<i>26.3</i>	<i>15.8</i>	<i>19.2</i>			<i>25.7</i>	<i>18.0</i>		
Minority Interest	0.0	0.0	0.1	Nm	Nm	0.0	0.1	Nm	
<b>Net profit</b>	<b>3.7</b>	<b>3.2</b>	<b>5.8</b>	<b>80.9</b>	<b>56.9</b>	<b>6.7</b>	<b>9.0</b>	<b>33.9</b>	Below both our/consensus expectations at 28/32% of full-year estimates respectively. Second interim DPS of MYR0.01 was declared, bringing 1H17 DPS to MYR0.0175.
<b>Core profit</b>	<b>3.3</b>	<b>3.2</b>	<b>5.8</b>	<b>80.9</b>	<b>74.6</b>	<b>6.1</b>	<b>9.0</b>	<b>47.9</b>	
<i>Net margin (%)</i>	<i>6.8</i>	<i>7.3</i>	<i>10.5</i>			<i>6.8</i>	<i>9.1</i>		

Source: Company data, RHB

## SWOT Analysis



## Recommendation Chart



Date	Recommendation	Target Price	Price
2017-07-19	Buy	2.63	2.19
2017-07-07	Buy	2.60	2.12
2017-05-23	Buy	2.60	2.35
2017-02-23	Buy	2.57	2.18
2016-11-21	Buy	2.57	2.45
2016-10-25	Neutral	2.01	2.19
2016-06-28	Neutral	1.96	1.99
2016-05-26	Neutral	2.30	2.28
2016-02-26	Neutral	2.70	2.83
2015-11-26	Neutral	2.48	2.52

Source: RHB, Bloomberg

Source: RHB, Bloomberg

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