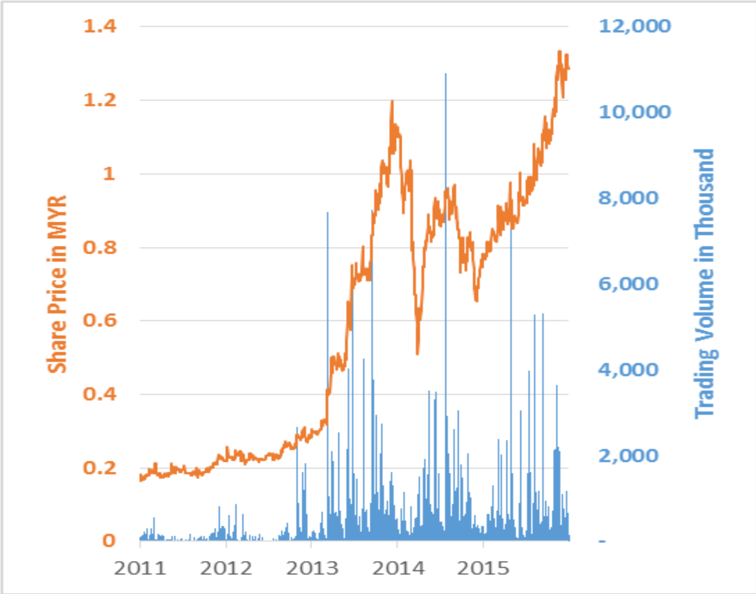
OKA Corporation Berhad

Industrial Product | Concrete manufacturer
Stock Code: 7140.KL Malaysia

NEUTRAL

Current Price	RM 1.32
Target Price	RM 1.43
Est. Upside Potential	8.7%
Market Cap	RM 209.70m
52-week Range	RM 0.83 – RM 1.38
Average Volume	322,410 (Source: FT)
Shares Outstanding	158,866,000
Free float	37.90% (Source: FT)
Beta	0.94
Valuation Basis	Discounted Cash Flow



Source: Yahoo Finance
Please refer to reputable share price providers for more accurate data

Investment Considerations

1) Slowing housing market might be compensated by infrastructure growth

The industry is largely fragmented with large players such as Chin Hin and Lafarge control less than 13% of the market share (Source: IMR report). OKA Berhad does not command any meaningful market share in both domestic and regional market. Uncertainty around the oversupply of housing in Malaysia may be balanced by high domestic infrastructure needs. Limited geographical operations leads to limited exposure to regional development (which we expect will continue to remain active) may weaken its competitiveness. In view of the above, we have factored in a moderate growth in our valuation.

2) Good fundamental with clean balance sheet and strong cash flow generation

Despite the share price has experienced a quantum leap in recent months, we believe it is justifiable given its improved cash flow and fundamental. We compared it with three identified competitors. OKA Berhad outperformed in most of the metrics. Profit and cash flow margins were in double digit range with growing trend. Peer comparable points out that its competitors are quite highly leveraged and their interest coverage, although adequate, weaken their cash flow generation hence giving OKA Berhad an edge as it is currently debt-free and allow excess cash for potential expansion plans and expand into new product range. P/E and EV/EBITDA are currently trading at 9.28x and 5.00x respectively, which we deems as reasonable.

3) Attractive valuation with good upside potential

Although we have a neutral rating on the company, it is largely due to our conservative estimations as well as the market is very likely to trade sideways (as it is currently at new high) until next positive quarterly result comes out, we view the long term prospect favourably given the company is able to sustain its cash flow generation (FFO and FCF margin of no less than 10%) with moderate revenue growth (no less than 4%). Our base case scenario suggests an upside potential of c.9% while best case scenario is c. 40%.

Financial Summary	FY 13	FY 14	FY 15	FY 16	TTM
Net Profit Margin	*4.26%*	*9.20%*	*9.16%*	*13.49%*	*13.63%*
Return on Equity	*5.82%*	*12.20%*	*12.29%*	*14.95%*	*15.36%*
Price to Net Tangible Assets	*0.66x*	*0.96x*	*1.18x*	*1.11x*	*1.43x*
Price to Earnings	*11.28x*	*7.85x*	*9.63x*	*7.42x*	*9.28x*
EV / EBITDA	*8.45x*	*6.09x*	*6.40x*	*4.54x*	*4.99x*

Analyst	*Jackson Yuen*
Contact	*+44 7400 630 379*
Email	*jacksonyuen1234@gmail.com*
Date	*19/09/2016*

KapitalWise

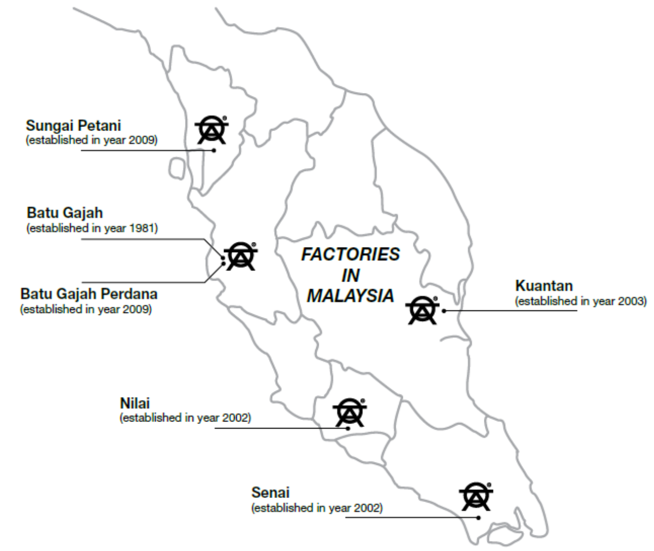
Company Profile

OKA manufactures and sells pre-cast concrete products and ready-mixed concrete. It supplies various concrete products such concrete pipes, large diameter pipe, ready-mixed concrete and Precast Concrete Box Culverts. Operating mainly in Malaysia, with five production plants located in Perak, Johor, Negeri Sembilan, Pahang and Kedah.

Top 5 Shareholders

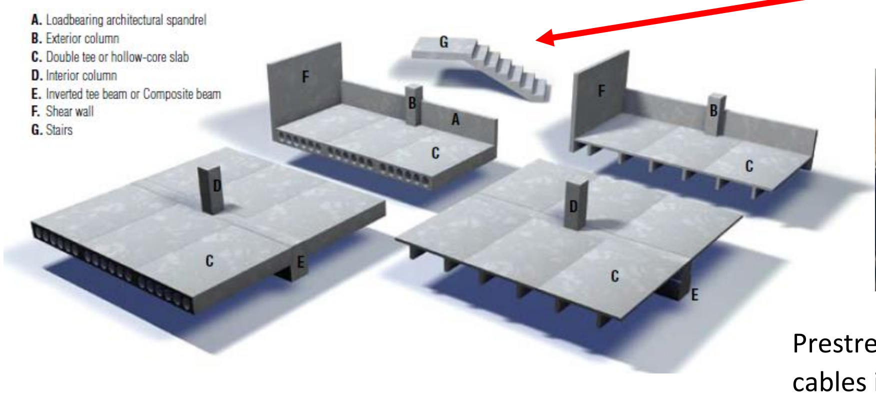
Ong Koon Ann	51.62%
Quah Seok Keng	3.27%
Ong Choo Ian	1.95%
Fong Siling	1.38%
Nik Mohamad Pena Bin Nik Mustapha	1.12%

** As of 30 June 2016*



Precast Concrete Piles – usage can include deep foundation and infrastructure.

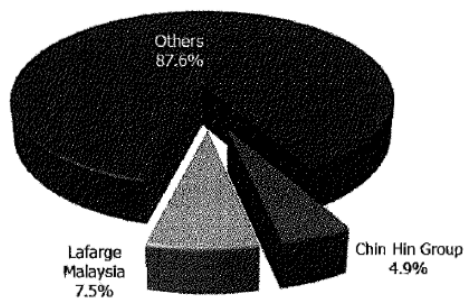
Precast Concrete can be cast into various shapes catering to different building needs.



Prestress Concrete – Which has high strength cables inside the concrete. It is stronger and is said to allow lesser concrete consumption in its production.

Precast Concrete Pipe – usually use in drainage and sewerage and drainage. It offers nominal diameter ranging from 300mm to 1800mm.

Figure 13: Market Share of Selected Market Players within the Manufacture of Articles of Concrete, Cement and Plaster Segment, 2014



Source: Chin Hin's IPO Prospectus (IMR Report)

The industry has two large players but both are not substantially controlling the market.

Peer Comparable

Chin Hin - Provider of building materials such as ready-mixed concrete, pre-cast concrete and mesh and steel bar.
Sarawak (SCIB) - Concrete products manufacturer, installation of building system components and property trading.
Concrete (CEPCO) - Pre-stressed spun concrete piles and poles manufacturer, also provides other construction related services.

Previous FYE's Result					Current FYE's Result			
*OKA**	*Chin Hin*	*Sarawak*	*Concrete*		*OKA**	*Chin Hin*	*Sarawak*	*Concrete*
				Profitability				
16.37%	6.15%	3.80%	4.37%	*EBITDA Margin*	17.04%	6.19%	9.12%	5.03%
17.96%	7.23%	19.73%	22.14%	*Gross Profit Margin*	22.84%	8.47%	19.96%	22.33%
9.16%	2.48%	-4.55%	-0.55%	*Net Profit Margin*	13.49%	2.52%	0.36%	1.06%
12.29%	13.09%	-5.87%	-0.81%	*Return on Equity*	14.95%	11.57%	0.48%	2.22%
12.11%	3.21%	10.45%	1.36%	*FFO Margin*	18.09%	3.78%	8.89%	8.97%
8.65%	6.79%	-7.25%	0.15%	*FCF Margin*	17.55%	1.67%	-0.20%	5.10%
				Operational Efficiency				
1.06x	1.52x	0.72x	1.53x	*Asset Turnover*	0.93x	1.41x	0.73x	1.05x
3.14%	1.01%	10.45%	0.56%	*Capex / Revenue*	2.93%	1.63%	1.62%	0.43%
				Liquidity				
1.68x	0.83x	0.96x	0.71x	*Acid Test*	2.79x	0.73x	1.46x	1.31x
0.21x	0.26x	0.12x	0.01x	*Cash Ratio*	1.07x	0.36x	0.25x	0.01x
				Leverage				
0.03x	4.94x	6.78x	6.98x	*Debt / EBITDA*	0.00x	5.24x	3.25x	4.05x
231.39x	4.01x	1.96x	2.25x	*EBITDA / Interest*	0.00x	3.62x	4.55x	4.10x
187.00x	3.35x	-3.42x	1.96x	*(EBITDA - Capex) / Interest*	0.00x	2.67x	3.74x	3.75x
2016.65%	22.32%	-28.16%	0.49%	*FCF / Debt*	0.00%	5.16%	-0.67%	24.99%
0.46%	46.22%	18.47%	46.47%	*Debt / Tangible Assets*	0.00%	45.59%	21.66%	21.33%
				Investment Metrics				
9.79x		*neg*	*neg*	*Price to Earning*	7.57x	12.01x	247.97x	34.43x
1.20x		1.22x	0.77x	*Price to Book*	1.13x	1.39x	1.19x	0.76x
0.90x		0.95x	0.52x	*Price to Sales*	1.02x	0.30x	0.90x	0.37x
10.38x		*neg*	351.94x	*Price to FCF*	5.82x	18.08x	*neg*	7.19x
5.26x		30.33x	18.82x	*EV / EBITDA*	4.91x	7.70x	12.18x	11.27x
6.83x		*neg*	48.71x	*EV / EBIT*	6.21x	9.61x	47.08x	17.69x
6.51x		*neg*	21.61x	*EV / (EBITDA - Capex)*	7.24x	6.63x	12.06x	7.96x
0.86x		1.15x	0.82x	*EV / Sales*	0.84x	0.48x	1.11x	0.57x
10.21%		-4.81%	-1.05%	*Net Income Yield*	13.21%	8.33%	0.40%	2.90%
9.64%		-7.67%	0.28%	*FCF Yield*	17.18%	5.53%	-0.22%	13.91%
9.99%		0.00%	1.54%	*(FFO - Capex) / Market Cap***	14.85%	7.11%	8.04%	23.31%
146.51		61.07	80.60	*Market Cap in MYR****	156.17	363.01	59.60	81.49

** FYE March 2015 and March 2016, respectively*
*** FFO measures the cash flow from operations excluding the changes in working capital*
**** As of financial year end (not average share price), other calculations might differ*

Key Takeaways from peer comparables:

- Based on the 2 FYE results, we can approximately conclude that OKA Berhad has strong cash flow and profit generation. It is worth noted that FYE 16's significant improvement was mainly attributable to lower cost of sales which we need to determine the sustainability in its upcoming financials. Even disregard such improvements, FCF margin of c. 9% and FFO margin of 12% are still considered strong.
- Strong liquidity position with low leverage strengthen its position should there be any adverse in trading conditions
  - The competitors have leverage of above 3x (as measured by Debt / EBITDA) and interest coverage of around 3x to 5x which suggests significant portion of its operating profit goes toward to debt financing hence further weaken its free cash flow generation.
- We do acknowledge that there are many changes since the last FYE (in terms of share price performance) hence readers must understand that the valuation metrics are based historical and not based on the latest share price. Based on the two FYE, OKA has been priced quite cheaply relative to the market despite of its significant strong financial performance relative to peers.

Financial Summary

Valuation Metrics	FY 2011	FY 2012	FY 2013	FY 2014	FY 2015	FY 2016	TTM
Price to Earnings	4.98x	7.07x	11.28x	7.85x	9.63x	7.42x	9.28x
Price to Net Tangible Assets	0.34x	0.37x	0.66x	0.96x	1.18x	1.11x	1.43x
Price to FCF	-19.50x	-19.71x	10.31x	8.74x	10.20x	5.70x	6.44x
Price to Sales	0.25x	0.29x	0.48x	0.72x	0.88x	1.00x	1.27x
EV / EBITDA	3.98x	5.19x	5.56x	4.45x	5.17x	3.90x	4.99x
EV / (EBITDA - Capex)	7.70x	20.93x	8.45x	6.09x	6.40x	4.54x	5.86x

*** Capex used FYE 2015 (no material change in capex in latest quarterly result)*

Metrics	FY 2011	FY 2012	FY 2013	FY 2014	FY 2015	FY 2016	TTM
Liquidity Metrics							
Current Ratio	1.76	1.64	1.82	2.30	2.82	3.86	3.66
Acid Test	0.89	0.92	0.97	1.31	1.68	2.68	2.65
Credit Metrics							
Debt / EBITDA	1.62x	2.06x	1.23x	0.35x	0.03x	0.00x	0.00x
EBITDA / Interest	13.30x	11.19x	17.99x	46.01x	231.39x	n.a	n.a
(EBITDA - Capex) / Interest	6.87x	2.77x	11.84x	33.59x	187.00x	n.a	n.a
Free Cash Flow / Debt	-8%	-8%	35%	138%	2017%	n.a	n.a
Profitability Metrics							
Gross Profit Margin	14.13%	9.88%	11.97%	18.26%	17.96%	22.84%	n.a
Net Profit Margin	5.05%	4.09%	4.26%	9.20%	9.16%	13.49%	13.63%
EBITDA Margin	10.19%	8.83%	10.81%	17.01%	16.37%	20.92%	21.24%
Free Cash Flow Margin	-1.29%	-1.47%	4.66%	8.26%	8.65%	17.55%	19.65%
Return on Assets	4.66%	3.52%	4.10%	9.26%	9.73%	12.52%	12.66%
Return on Equity	6.82%	5.29%	5.82%	12.20%	12.29%	14.95%	15.36%
Key Metrics							
Capex / Sales	4.93%	6.64%	3.70%	4.59%	3.14%	2.93%	3.16%
Net Income / Dividend	3.12x	2.75x	3.15x	6.37x	2.87x	2.93x	n.a
Free Cash Flow / Dividend	-0.80x	-0.99x	3.45x	5.72x	2.71x	3.81x	n.a

*** Capex used FYE 2015 (no material change in capex in latest quarterly result)*

Income Statement	FY 2011	FY 2012	FY 2013	FY 2014	FY 2015	FY 2016	TTM
Revenue	111.3	121.1	133.1	145.4	163.3	152.9	162.0
y-o-y growth		8.7%	9.9%	9.3%	12.3%	-6.3%	5.9%
Gross Profit	15.7	12.0	15.9	26.6	29.3	34.9	44.0
y-o-y growth		-23.9%	33.2%	66.8%	10.4%	19.1%	25.9%
SG&A	9.3	7.6	8.0	8.8	10.0	10.3	17.2
y-o-y growth		-18.7%	5.8%	9.4%	14.0%	3.4%	66.6%
Net Income	5.6	5.0	5.7	13.4	15.0	20.6	22.1
y-o-y growth		-11.9%	14.6%	135.8%	11.8%	37.9%	7.0%
Recurring Net Income	6.9	3.9	5.6	13.4	15.0	20.6	22.1
y-o-y growth		-42.6%	42.4%	138.0%	12.0%	37.9%	7.0%
EBITDA	11.3	10.7	14.4	24.7	26.7	32.0	34.4
y-o-y growth		-5.8%	34.6%	71.9%	8.0%	19.7%	7.6%

Balance Sheet	FY 2011	FY 2012	FY 2013	FY 2014	FY 2015	FY 2016	MRQ
Tangible Fixed Assets	52.6	64.6	64.1	64.8	63.8	62.8	63.2
Total Non-Current Assets	53.3	65.4	64.6	65.3	64.3	63.3	63.6
Cash and Cash Eqv.	1.2	1.6	1.8	3.6	6.5	28.2	33.3
Total Current Assets	67.3	75.5	73.8	79.1	89.4	101.5	110.8
Total Bank Debts	18.3	22.0	17.8	8.7	0.7	0.0	0.0
Total Current Liabilities	38.2	46.1	40.5	34.4	31.7	26.3	30.3
Total Non-Current Liabilities	0.0	1.0	0.4	0.4	0.4	0.5	0.5
Retained Earnings	20.1	23.2	37.5	48.8	43.3	56.9	61.9
Total Shareholder's Equity	82.4	93.7	97.6	109.7	121.7	138.0	143.7

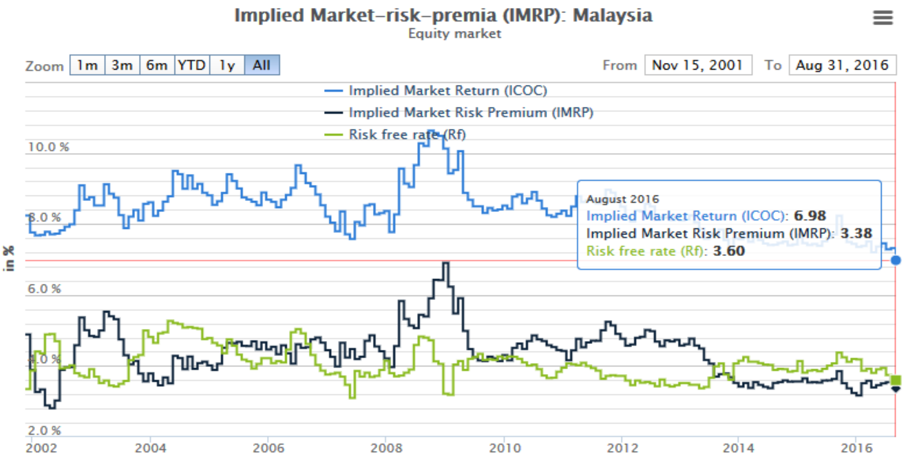
Cash Flow	FY 2011	FY 2012	FY 2013	FY 2014	FY 2015	FY 2016	TTM
Cash Flow from Operations	4.0	6.3	11.1	18.7	19.2	31.3	n.a
Changes in Working Capital	- 6.3	- 1.6	- 0.7	- 4.2	- 0.5	3.6	n.a
Cash Flow from Investing							
Capex	5.5	8.0	4.9	6.7	5.1	4.5	n.a
Cash Flow from Financing							
Dividends paid	1.8	1.8	1.8	2.1	5.2	7.0	n.a
Debt Borrowing	3.9	4.9	-	0.9	-	-	n.a
Equity Issuance	-	-	-	-	2.0	2.2	n.a
Fund from Operations*	10.4	7.9	11.9	22.9	19.8	27.7	n.a
Free Cash Flow	- 1.4	- 1.8	6.2	12.0	14.1	26.8	n.a

** Cash flow from Operations minus the changes in working capital*

Valuation

For valuation, we believe the company will continue to generate satisfactory cash flow from its operations. Since FYE 2012, the company improved its cash flow generation significantly and sustained its free cash flow margin above 5% and surged to almost 18% in FYE 2016 from 8.65% in FYE 2015 thanks to its lower cost of sales (down from 82% to 77%). To be conservative, we have adjusted accordingly and based on historical margin as there was no information on the cost of sales for us to assess the sustainability.

Cost of Equity



Discount Rate	
Risk Free	3.60%
Adjusted Beta	0.96
Equity Risk Premium	3.38%
Cost of Equity	6.85%

Cost of Equity calculated using CAPM is 6.85%. However, we believe that 10% for such a small cap stock is deem acceptable. 10% is a subjective estimation made by us, so the readers are advised to interpret our estimation with care.

Discounted Cash Flow

Base Case Scenario	FY 2017	FY 2018	FY 2019	FY 2020	FY 2021	FY 2022	FY 2023	FY 2024
EBITDA	23.9	24.5	28.4	29.3	31.1	33.0	34.8	36.7
Tax	-5.0	-5.2	-6.4	-6.7	-7.0	-7.3	-7.6	-8.0
Others	-0.3	-0.3	-0.3	-0.4	-0.4	-0.4	-0.4	-0.4
- / + WC	2.6	0.5	-0.9	2.2	1.4	2.8	1.3	0.7
CFO	21.2	19.4	20.8	24.5	25.1	28.1	28.1	29.0
Capex	-6.3	-5.7	-5.9	-6.1	-6.4	-6.7	-7.0	-7.3
FCF	14.9	13.7	14.9	18.4	18.7	21.4	21.0	21.7
Terminal Value								310.2
Discount Rate @ 10%	0.91	0.83	0.75	0.68	0.62	0.56	0.51	0.47
Present Value	13.6	11.3	11.2	12.5	11.6	12.1	10.8	144.7
Sum of PV	227.9							
Shares Outstanding	158.9							
Fair Value Per Share	1.43							
Current Share Price	1.32							
Upside Potential	8.7%							

Our EBITDA calculation did not take into the effect of interest expenditure since the company is currently debt-free and we believe there is a minimal need for debt raising since the company generates its cash flow organically (judging from its fund of operations which has sustained above 7% since 2011). Should there be any debt raising in the upcoming financials, we expect the interest expenses would not materially affect the cash flow.

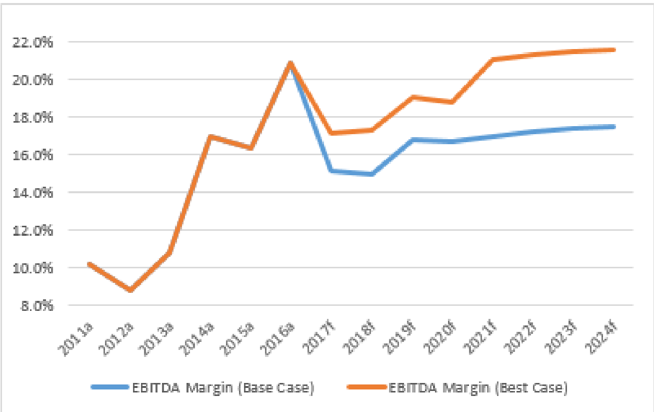
Growth in the base case scenario range from 3% to 4.5% (gradually increase), and Terminal Growth of 3%.
At 10% discount rate, discounted cash flow model suggests an upside potential of 8.7%.

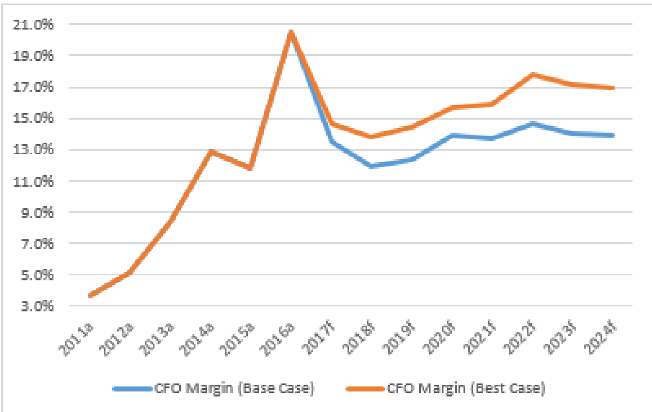
Capex / Sales is around 3.5% to 4% which is higher than the competitors observed (refer to peer comparable).

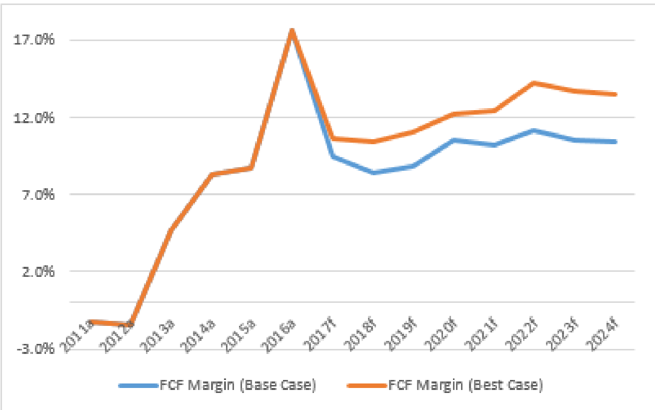
Best Case Scenario	FY 2017	FY 2018	FY 2019	FY 2020	FY 2021	FY 2022	FY 2023	FY 2024
EBITDA	27.2	28.7	33.0	34.0	39.8	42.2	44.7	47.2
Tax	-5.9	-6.4	-7.6	-8.0	-9.4	-9.9	-10.4	-10.9
Others	-0.3	-0.3	-0.3	-0.4	-0.4	-0.4	-0.4	-0.4
- / + WC	2.2	0.9	0.1	2.8	-0.1	3.2	1.8	1.2
CFO	23.3	22.9	25.0	28.4	29.9	35.2	35.7	37.0
Capex	-6.4	-5.8	-6.0	-6.3	-6.6	-6.9	-7.3	-7.6
FCF	16.9	17.1	19.0	22.1	23.3	28.2	28.4	29.4
Terminal Value								420.0
Discount Rate @ 10%	0.91	0.83	0.75	0.68	0.62	0.56	0.51	0.47
Present Value	15.4	14.1	14.3	15.1	14.5	15.9	14.6	195.9
Sum of PV	299.8							
Shares Outstanding	158.9							
Fair Value Per Share	1.89							
Current Share Price	1.32							
Upside Potential	42.9%							

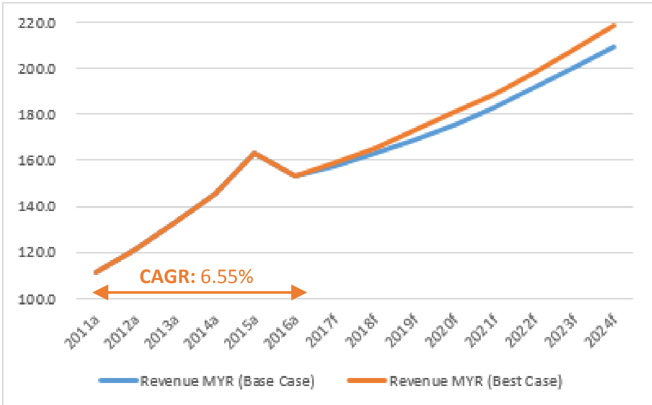
Under the best case scenario, the growth rate range from 4% to 5% with higher cash flow margins. Terminal Growth is also same as base case scenario (3%). If the company can sustain its current cash flow generation and moderate growth, the upside potential is a lot higher than current price (suggested upside of over 40%).

We recognised that some investors might be quite optimistic with the growth prospects of OKA Berhad (and growth rate of 3.5% to 5% might be too pessimistic). We aim to be conservative to reduce our error in forecasting and any large negative deviation from the fast growth will be offset by our low estimation.









The above charts are showing the historical margins (for example, 2011a = 2011 actual result whereas 2017f = forecast for FY 2017). Blue line is base case scenario where Orange line represents best case scenario.

With regards to the cash flow assumptions, we believe our best case is easily achievable given its low estimation. And its share price has already experienced a quantum leap, thus we believe the market might be cautious and the outlook is neutral in short term.

Key Investment Risks

Slowdown in the housing market

Housing market still plays an important role in construction sector of which any potential slowdown would lead to lower demand. With the company low geographical diversification, it could potentially lose out and not being able to benefit from any regional growth.

Heighten competition = weaker profit margin.

Any slowdown would intensify the competition and lower the prices to attract volume. We believe the firm is well position to weather this storm with low leverage and strong liquidity. However, significant deterioration in cash flow generation will be a high risk.

Surge in domestic power and fuel price

Power and fuel price represent a significant cost to the production of cement and concrete (said to be c. 30%). Hence, any significant surge would lead to lower profit margin. To counter this potential effect, our cash flow forecasting has been greatly reduced.

Temporary weaker quarterly result

The market may react aggressively to slightly poor quarterly result as the share price surged significantly which the investors may be cautious on growth prospects. Our model assumes a moderate growth given the concrete is a mostly used material especially during the economic development.

Investment Ratings

Buy = Share price may exceed 15% over the next 12 months
Neutral = Share price may fluctuate within the range of ± 15% over the next 12 months
Sell = Share price may fall more than 15% over the next 12 months

Investment Research Disclaimers

The opinions and views expressed in this report are solely of the analyst.

Any projections or estimations may not be accurate. Market conditions and assumptions could result in materially different outcomes.

Past performance is not necessarily an indicative of future performance and the analyst will not accept for any loss arising from information contained in this report.

This report is not intended as an offer to buy or sell the securities discussed.

Seek independent advice to understand the investment risk arising from taking investment actions based on this report. Consider your unique circumstances (such as time horizon, liquidity and risk tolerance) before investing as not all investment are suitable for every investor.

The analyst currently has no financial interests with the company analysed in this report. The company has not paid the analyst to write this research.

The analyst currently has no shareholding in the company analysed in this report.

The analyst may invest in the company analysed in the future but will only do so after 48 hours of publishing of this report.

Background of the analyst

- *Currently working as a Credit Analyst in the Bank of East Asia, analysing retail, corporate and syndicated loans in various industries.*
- *Passed Level 3 of the CFA Program.*
- *Distinction in MSc Banking and Finance from the University of Sussex.*
- *First Class Honours in BA Accounting from the University of Portsmouth.*