11 June 2018

Finding Diamonds In The Rough

Our Best Investment Ideas

We have always actively sought out "Diamonds In The Rough" among the companies under coverage in our ASEAN + Hong Kong footprint. We used a bottom-up fundamental analysis and screened for companies that met four criteria:

1. **ROEs of 15% or above;**
2. **Increasing margins;**
3. **Trading below the average market multiples;**
4. **Reasonable corporate governance.**

The table below shows our 16 "diamonds".

Our methodology uses a fundamental bottom-up analysis, coupled with RHB's on-the-ground insights.

Our sector analysts provided their assessments of the average market multiples for the respective sectors that the companies operated in. As one of the criteria is "trading below the average market multiples", it means these stocks are out of favour currently.

In parallel, the list was further refined based on our assessments of each company's potential to widen its margins, without compromising on the ROE while having reasonable corporate governance.

Previous strong absolute returns. In our former three "Diamonds In The Rough" reports – from 2016, 2017, and at the beginning of 2018 – our search resulted in a list of stocks that exhibited strong absolute returns:

- *Finding Diamonds In The Rough*
- *RHB Thematic - Uniquely RHB - Some See Coal, We See Diamonds*
- *Regional Diamonds the 3rd: Our Best Investment Ideas*

Our findings this time have resulted in a list of 16 stocks shown below. This list represents companies that our analysts believe can have robust earnings growth due to the sector- or company-specific reasons. In the table below, we show these companies in alphabetical order.

We have BUY recommendations on all these counters, and our level of conviction is shown in their potential upside returns. As it takes a while for coal to turn into diamonds, we consider that – given time – all the companies in the list below should show healthy absolute returns.

The pages that follow show a brief description of why we consider these companies picked have "diamond"-type characteristics, presented per each country in our coverage universe.

Company Name	Rating	Price	Target	% Upside (Downside)	P/E (x) Dec-18F	P/B (x) Dec-18F	Yield (%) Dec-18F
APAC Realty	BUY	SGD0.90	SGD1.35	50.7	10.7	2.2	5.6
Astra International	BUY	IDR6,975	IDR8,450	21.1	14.5	2.1	3.7
Bermaz Auto	BUY	MYR2.22	MYR2.55	14.9	13.9	5.2	5.4
China State Construction	BUY	HKD9.66	HKD13.20	36.6	7.2	1.0	3.9
Chinasoft International	BUY	HKD6.68	HKD7.77	16.3	18.5	2.2	-
Cocoaland	BUY	MYR2.34	MYR3.02	29.1	13.9	2.0	4.3
Dialog	BUY	MYR3.38	MYR3.92	16.1	44.2	6.3	-
GSS Energy	BUY	SGD0.15	SGD0.25	68.9	10.6	1.5	1.9
Gudang Garam	BUY	IDR70,075	IDR91,100	30.0	16.0	2.9	3.7
Japan Foods Holding	BUY	SGD0.51	SGD0.63	23.8	14.0	2.4	4.1
Major Cineplex	BUY	THB27.25	THB31.00	13.8	27.0	3.8	4.0
Serba Dinamik	BUY	MYR3.30	MYR4.07	23.3	11.4	3.5	2.6
Shimao Property	BUY	HKD25.10	HKD30.00	19.5	6.8	1.0	5.9
Singapore Exchange	BUY	SGD7.26	SGD9.00	24.0	19.9	7.1	4.5
SKP Resources	BUY	MYR1.60	MYR2.04	27.7	13.3	3.2	3.8
TISCO Financial	BUY	THB86.25	THB104.00	20.6	9.7	1.8	6.2

Source: Company data, RHB (Data as of 4 Jun 2018)

"Rough diamonds may sometimes be mistaken for worthless pebbles"

Thomas Browne

Some See Coal, We See Diamonds

Source: RHB

Our four criteria used to discover the diamonds:

1. ROEs of 15% or above;
2. Increasing margins;
3. Trading below sector valuations;
4. Reasonable corporate governance.

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Country heads (in alphabetical order):

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Malaysia

Figure 1: Diamonds from Kuala Lumpur

Company	Ticker	Rating	Target	Share price	Market cap (USDm)	P/E (x)		P/BV (x)		EV/EBITDA (x)		ROAE (%)		Net margin (%)	
						FY18F	FY19F	FY18F	FY19F	FY18F	FY19F	FY18F	FY19F	FY18F	FY19F
Bermaz Auto^	BAUTO MK	BUY	2.55	2.16	629.2	11.9	9.5	4.9	4.3	8.4	6.6	43.2	48.1	8.3	8.7
Cocoaland Holdings	COLA MK	BUY	3.02	2.31	132.8	13.7	12.6	2.0	1.9	7.0	6.4	14.9	15.3	13.5	13.6
Dialog	DLG MK	BUY	3.92	3.28	4,646.6	44.3	41.5	6.4	5.8	32.8	35.1	15.0	14.6	12.3	14.2
Serba Dinamik	SDH MK	BUY	4.07	3.33	1,228.7	11.5	10.1	3.5	2.8	9.4	7.9	34.6	31.2	13.3	13.5
SKP Resources^	SKP MK	BUY	2.04	1.52	477.5	12.0	9.8	3.0	2.6	7.4	6.1	26.7	28.3	6.2	6.4

Note: Data as at 4 Jun 2018
Note 2: ^FY18F & FY19F valuations refer to those of FY19F & FY20F
Source: RHB, Bloomberg

Bermaz Auto (BAUTO MK, BUY, TP: MYR2.55)

Bermaz Auto (Bermaz) is involved in the distribution, retailing and after-sales service of Mazda vehicles in Malaysia. Bermaz also distributes Mazda vehicles and spare parts in the Philippines through subsidiary Bermaz Auto Philippines (BAP) to appointed dealers. Through its associates – 30%-owned Mazda Malaysia (MMSB) and 29%-owned Inokom Corp (Inokom) – the company is involved in the assembly of Mazda's CKD vehicles, which are marketed to local and regional markets.

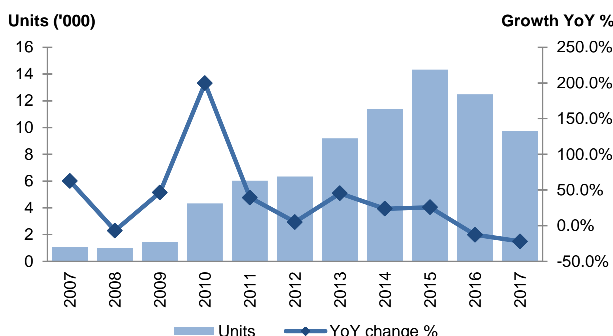
We expect high ROEs of 29-48% for FY18-20, in addition to dividend yields of 3.9-7.9%. Bermaz registered a solid 9MFY18 (Apr) performance after its net profit grew 82.3% QoQ and 61.2% YoY. This was supported by robust Mazda sales volumes in Malaysia (+13.7% QoQ, +49.6% YoY) and the Philippines (+18.6% QoQ, +68.9% YoY). The all-new *CX-5* launched in Malaysia in Oct 2017 was the key driver of sales, while margins improved from favourable forex rates.

Likely margin expansion on new models introduced and higher assembly volumes. Bermaz has two new models in the pipeline set for launch this year: the new Mazda *6* and *CX-8* 7-seater SUV. The latter is to be assembled locally by mid-2019 and will be exported to regional markets thereafter. The *CX-8* could be a game changer for Mazda in the Philippines, where we expect strong market share gains in the SUV segment. Assuming Bermaz achieves a modest 5% share of the SUV market there, this should bring additional sales of 3,000 units pa (FY18F: 5,200 units). High production volumes of this model are also likely to translate into strong associate contributions from MMSB and Inokom. Adding this to the strong sales currently being driven by the *CX-5* SUV, we expect Bermaz's earnings growth to be sustainable.

Trading below sector valuation. BUY, with a SOP-derived TP of MYR2.55, which values its domestic earnings at 13.5x FY19F – this is below the sector average P/E of 15.3x – and the business in the Philippines at 15x FY19F earnings. Bermaz offers a rare blend of earnings growth and attractive yields. It also has strong growth potential on the back of expanding product offerings.

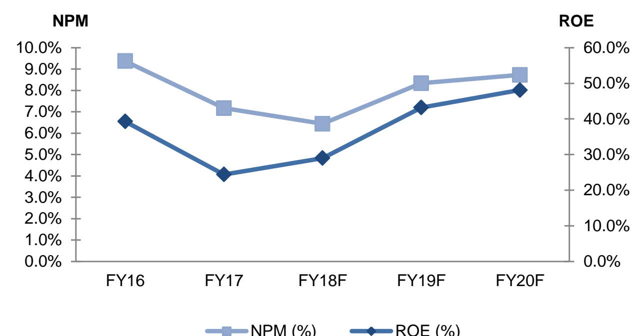
Reasonable corporate governance. We see no corporate governance issues. Ernst & Young has been its independent (and sole) auditor since its listing in 2013. We also note that independent non-executive directors constitute two-thirds of the current board.

Figure 2: Mazda sales volumes



Source: Company data, RHB

Figure 3: ROE (%) and NPM (%) comparisons



Source: Company data, RHB

Cocoaland (COLA MK, BUY, TP: MYR3.02)

Cocoaland manufactures mainly chocolates, hard candy, fruit gummies, cookies, wafers, snacks and beverages. The group was listed on the Second Board of Bursa Malaysia Securities in 2005, and has – since then – delivered an uninterrupted earnings record.

Its in-house products have strong brand equity in both the domestic and foreign markets which include countries like China, Hong Kong, Saudi Arabia and Singapore. The group also has expertise in contract manufacturing, serving several reputable multinational corporations (MNCs).

We forecast commendable ROEs of 14.9% and 15.3% in FY18 and FY19 vs 13.7% in FY17. We believe earnings growth will be driven by robust demand for its gummies and snack products, particularly in the export market.

Cocoaland also has plans to add a new production line, which should lift gummy production capacity to 14,200 tonnes – from 9,200 tonnes – once operational in late 2019. This will likely sustain earnings growth over the longer term, in our view.

On top of that, we are forecasting prospective dividend yields of 4.3-4.7% in FY18-20. We believe the decent yields will be supported by a healthy operating cash flow and sturdy balance sheet.

We expect margins to improve moving forward, driven by higher economies of scale on the back of growing sale volumes. The higher contribution from its in-house products should also aid margins expansion, as Cocoaland’s margins are higher than those of the contract manufacturing business.

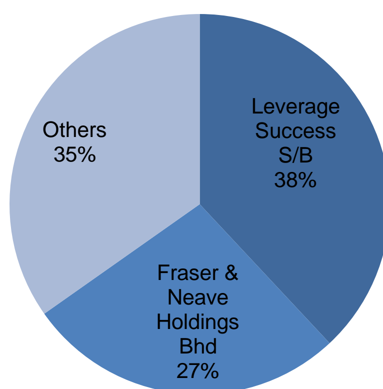
Meanwhile, we also expect continuous efforts in automation, which are likely to further improve operating efficiency.

Trading below sector valuation at 13x FY19F P/E vs 22x for the Bursa Malaysia Consumer Product Index. We believe the sizeable discount can be attributed to the group’s relatively smaller market capitalisation and profit base.

Reasonable corporate governance. The group has managed to apply the principles, while the extent of compliance is within the best practices advocated by the Malaysia Code on Corporate Governance (MCCG). We are not aware of any corporate governance issues.

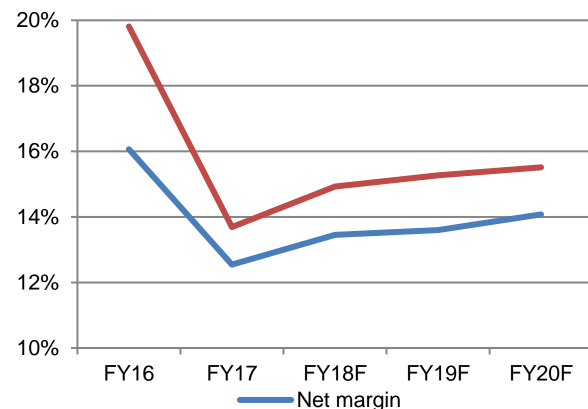
Risks to our recommendation include lower-than-expected sales and higher-than-expected input costs.

Figure 4: Shareholding structure



Source: Company data, RHB

Figure 5: ROE and NPM comparison



Source: RHB

RHB

Dialog (DLG MK, BUY, TP: MYR3.92)

Dialog is a tank terminal operator and engineering, procurement, construction and commissioning (EPCC) contractor in Malaysia focusing on mid-stream and downstream oil & gas industry.

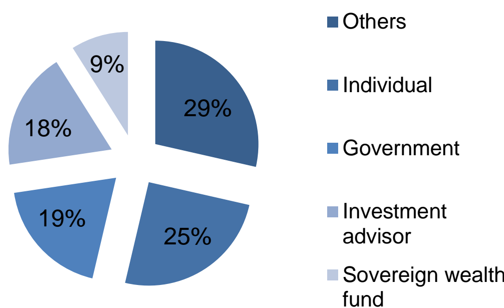
Dialog's ROEs of 15% are the result of its higher-than-expected associate contributions, given its minority stake in multiple tank terminals. We believe the company exhibits a strong understanding in this business, as it was also the EPCC contractor for the tank terminals. The lease agreements with its clients are usually long term and recurring in nature, therefore providing a solid earnings base.

Stronger associate contribution driving margins. We expect NPM to expand in the next few years due to increasing expected associate contribution from its tank terminals, driven by the completion of Pengerang Phase 2 in 2019. NPM for the group is estimated to expand to 14.9% in FY20, as a result of the mentioned capacity expansion. GPM is expected to be relatively stable in FY18-20 due to anticipated consistent margins from its EPCC business, which should contribute a big proportion to its topline.

Trading below sector valuation. Dialog Group is mainly involved in the downstream segment of the oil & gas industry; it has diversified operations and thus it is harder to assign it to an overall sector. We value some of its parts at multiples below those of its respective sectors. On an absolute basis its valuation is rich at 44.9x FY18F P/E. However, given that the stock has recently been included in the FBM KLCI list of 30 component stocks, more institutional investors would probably prefer to stay invested or add their positions in the Dialog. That aside, the group's position as the biggest proxy to growth in Refinery and Petrochemical Integrated Development (RAPID) project in Pengerang – which could grow another 10 years if more future project phases are sanctioned – adds, in our view, to the justification of its valuation.

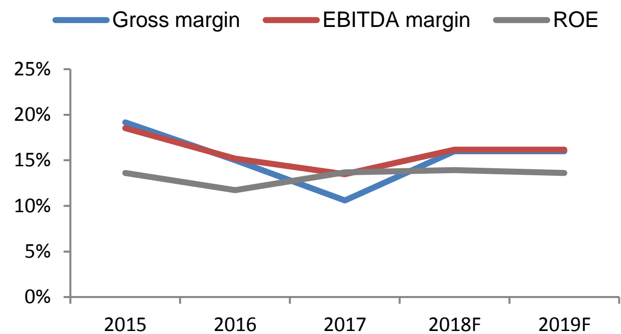
Reasonable corporate governance. The group has not had a restatement in financials or change of auditors. Chairman Tan Sri Ngau Boon Keat's interest is aligned to that of the shareholders of the company with his 19.2% stake held in Dialog. The board of directors has eight members, of which three are independent directors – this is to ensure that corporate governance remains intact.

Figure 6: Shareholding structure (%)



Source: RHB, Bloomberg

Figure 7: Chart margins and ROE profiles



Source: Company data, RHB

Serba Dinamik (SDH MK, BUY, TP: MYR4.07)

Serba Dinamik is an energy engineering player with a track record and international clientele base in operations & maintenances (O&M) services. Its bread and butter maintenance business focuses on plant maintenance services in general (power plants, refineries and petrochemical facilities).

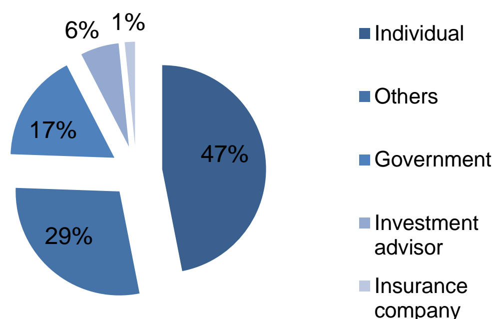
Stellar ROE of 35.6% posted in FY17 and we believe its performance to be sustained at this level in FY18-20. We believe the high ROE generated is due to its O&M business, of which a minimal asset base is required (consisting of mainly simple workshops and equipment) resulting in manageable capex requirements for business to generate reasonable returns. In addition, its efficiency in labour cost management has also contributed to better margins.

Margins to tick higher. We expect NPM to expand in the next few years due to increasing expected associate contributions from the Kota Marudu (Sabah) and Tanzania chlor-alkali plants in FY19. NPM is expected to expand gradually to 13.6% in FY20 from 12.7% in FY17. GPM, however, is expected to decline slightly to 16.6% in FY20 from 17% in FY17 due to higher expected EPCC revenue contributions – which typically fetch lower margins when compared to the O&M segment – to its revenue mix.

Trading below sector valuation. Due to its diversified operations**,** it is a bit harder to define an exact sector for this company; also, we value the stock through SOP. A recent sell-down, possibly due to uncertainty caused by the recent political changes, is in our view unjustified, given that the company secures its contracts through its own merits. 11.4x FY18F P/E looks very attractive, and it is lower when compared to bigger peers such as Dialog, which trades at P/Es above 40x. Plans to build a maintenance hub in Pengerang places Serba Dinamik in a good position to be another proxy to Petronas' RAPID project in the next 10 years.

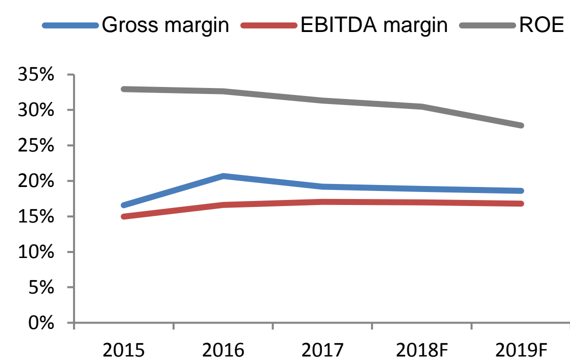
Reasonable corporate governance. It has not had a restatement in financials or change of auditors. CEO Dato' Mohd Abdul Karim Abdullah is also a major shareholder, with 22.9% stake. Out of its seven board members, five are independent non-executive directors.

Figure 8: Shareholding structure (%)



Source: RHB, Bloomberg

Figure 9: Chart margins and ROE profiles



Source: Company data, RHB

SKP Resources (SKP MK, BUY, TP: MYR2.04)

SKP Resources (SKP) is a leader in plastics contract manufacturing with over 40 years of manufacturing experience in the electrical and electronics plastics industry. Starting out as Sin Kwang Plastics, it established its roots in Johor Bahru in 1974 with only two injection moulding machines.

Today, SKP is a stalwart in the region, with more than 1m combined sq ft of plastic manufacturing facilities in Johor Bahru, housing more than 250 of the latest injection moulding machines. It also has a workforce of 2,500, which is still growing as operations expand to meet the needs of its clients.

We forecast ROEs of 26.7% and 28.3% in FY19 and FY20 vs 25.1% in FY18. We believe earnings growth will continue to be underpinned by robust orders from major key customers on the back of solid demand for its products in the global market.

We also expect more new orders to be secured from its existing and new customers. This is given SKP's proven track record and established expertise in the electronic manufacturing services industry.

A sturdy balance sheet would also allow the company to expand its production capacity to capture potential higher orders in future.

Likely margin expansion. We believe SKP's margins can improve, given the higher economies of scale on the back of higher sales.

Meanwhile, the higher stage of automation to reduce the labour force should also further improve operating efficiency.

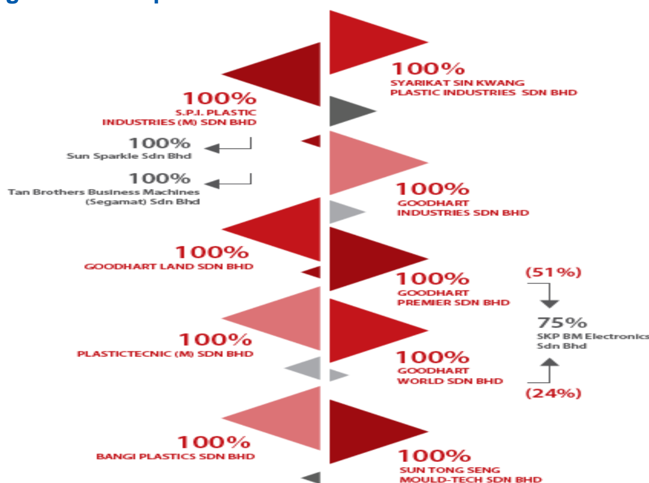
SKP is trading at c.12x FY19F P/E, which is lower than the sector average FY19F P/E of c.13x. We believe the discount could be attributed to the relatively smaller market capitalisation and profit base, as well as the trading liquidity.

We deem SKP as having reasonable corporate governance. Its board comprises six directors, with three who are independent, non-executive directors.

The extent of compliance is within the best practices advocated by the MCCG. We are not aware of any corporate governance issues.

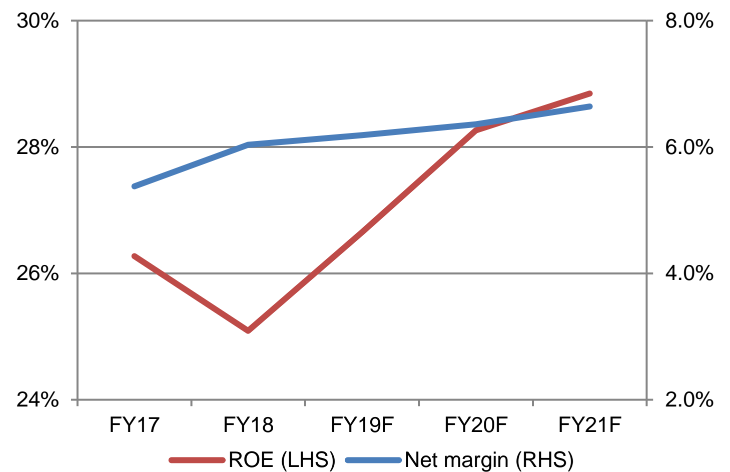
Risks to our recommendation include lower-than-expected new orders and higher-than-expected operating costs.

Figure 10: Corporate structure



Source: Company, RHB

Figure 11: ROE and NPM comparisons



Source: RHB

Thailand

Figure 12: Diamonds from Bangkok

Company	Ticker	Rating	TP	Share price	Mkt Cap (USDm)	P/E (x)		P/B (x)		EV/EBITDA (x)		ROAE (%)		Net margin (%)	
						FY18F	FY19F	FY18F	FY19F	FY18F	FY19F	FY18F	FY19F	FY18F	FY19F
Major Cineplex Group PCL	MAJOR TB	Buy	31.0	27.0	756.8	24.7	25.0	3.9	3.9	8.3	7.8	15.8	15.6	10.9	10.0
Tisco Financial Group PCL	TISCO TB	Buy	104.0	87.0	2,182.2	10.5	9.7	2.0	1.8	n.a.	n.a.	19.8	19.8	4.3	4.2

Note: Data as at 6 Jun 2018
Source: RHB, Bloomberg

Major Cineplex (MAJOR TB, BUY, TP: THB31)

Major Cineplex is a leader in the cinema business in Thailand with more than 723 cinema screens in 137 locations. The company also has a c.80% market share in terms of box office revenue in the kingdom. It also has other businesses, which including bowling, karaoke, ice skating and retail spaces.

Video streaming is unlikely to be a big disruptive force to the domestic cinema industry or Major Cineplex over the next few years. Indirectly, however, consumers may spend less time outside their homes – this would then affect not only the movie industry, but also retailers and the entertainment industry in general.

ROE above 15%. Major Cineplex manages its ROEs well, and the ratio has stayed above 15% since 2013.

Net margins at c.10%. NPMs may appear slim, as the cinema business is capital-intensive with high depreciation & amortisation costs for cinema theatres and movie licenses. In 2018, we expect Major Cineplex's revenue to continue to grow by 4.9% YoY, driven by:

i. 70-80 additional screens both locally and overseas, including two hip flagship locations at the Icon Siam in Bangkok and Aeon Mall 2 in Phnom Penh, Cambodia;

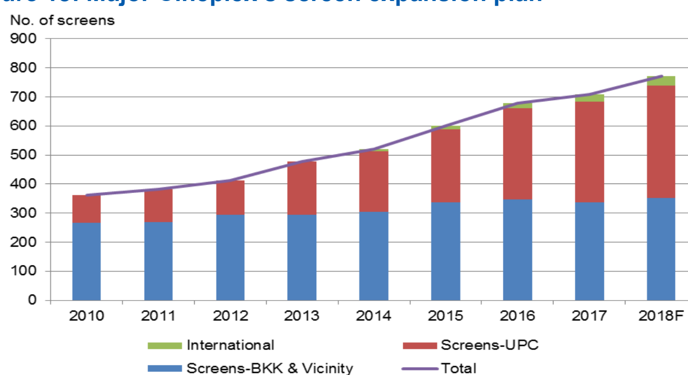
ii. Interesting movie line-ups from both international and Thai studios.

Since the majority of costs in the cinema business are fixed, any increase in revenue should enhance its GPM significantly. Hence, we expect core net profit in 2018 to rise by 13.5% to THB903m. Over the next three years, we estimate double-digit earnings growth of 12-13% pa.

Trading below peers. Compared to other media stocks, Major Cineplex is trading below its peers in all categories – ie P/E, P/BV, and EV/EBITDA – while dividend yield is one of the highest. Major Cineplex has three regional peers that operate cinema businesses, namely PVR (PVRL IN, NR), Inox Leisure (INOL IN, NR), and CJ CGV (079160 KS, NR). It is trading below the multiples of these international peers in all categories, while its ROEs and dividend yields are among the highest. We believe Major Cineplex has high growth potential with attractive valuations.

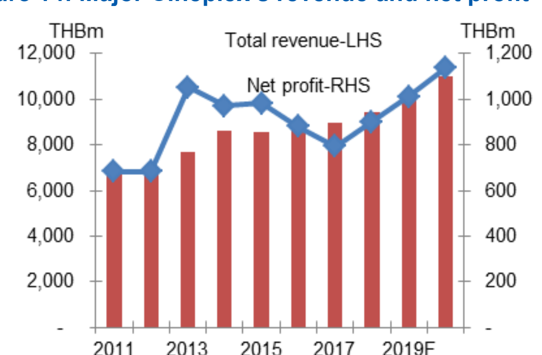
Reasonable corporate governance. The company received a corporate governance score – a measurement of listed local firms rated by the Thai Institute of Directors (IOD) in collaboration with the SET and Office of the Securities and Exchange Commission (SEC) – of 4/5 or 80% (80-89% = very good). Major Cineplex's major shareholder is CEO and founder Mr Vicha Poonwaralak, who holds 29.62% of the outstanding shares. His family was a pioneer in Thailand's cinema industry back in the 1960's. Mr Poonwaralak has almost 25 years of experience in managing the cinema business.

Figure 13: Major Cineplex's screen expansion plan



Source: Company data

Figure 14: Major Cineplex's revenue and net profit



Source: Company data, RHB

Tisco Financial (TISCO TB, BUY, TP: THB104)

Tisco Financial (TISCO) is the holding company of the Tisco Group, which has Tisco Bank as its core business. Tisco Bank engages in the banking business with service areas including retail and SME lending, corporate lending, retail deposit, private banking, bancassurance, cash management and custodian services.

Expanding ROEs. TISCO has been focusing on the efficient management of funding costs to sustain high NIMs. Moreover, with improved asset quality, lower NPL, and higher LLC ratios, we believe pressure on provisions will ease, enabling it to:

i. Lower credit costs;
ii. Boost earnings growth;
iii. Sustain high ROEs.

We expect TISCO's ROEs to continue increasing to 19.8% for FY18F-19F, the highest among peer banks.

Resilient growth ahead, TISCO is likely to remain one of the top auto hire purchase lenders in the country, in our view. We project resilient earnings growth ahead of 17-8% YoY for FY18F-19F, which is higher than its peers' 4-8%.

Growth will likely be driven by:

i. Lower credit costs due to its resilient asset quality;
ii. Efficient cost management that will lead to sustained high NIMs;
iii. Higher fee income growth from bancassurance and asset management fees.

High dividend yield. TISCO has a strong balance sheet with high capital adequacy ratio (CAR) and Tier-1 capital. This ought to enable it to:

i. Support potential growth;
ii. Withstand economic risks;
iii. Sustain high dividend payments.

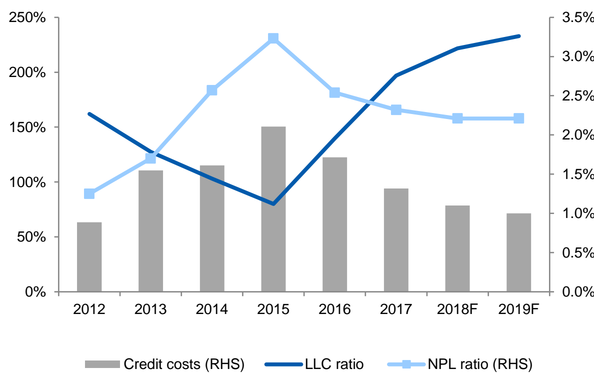
We estimate the group will be able to maintain stable dividend payouts of c.60% and expect yields of 6.4-7% for FY18-19, one of the highest among its peers.

Reasonable corporate governance. TISCO's corporate governance score has been five out of five (ie "Excellence") over the past few years. This score for listed Thai firms is rated by the Thai IOD in collaboration with the SET and the SEC.

The assessment criteria are based on the principles of good corporate governance espoused by the Organisation for Economic Co-operation and Development (OECD), as well as the SET. There are 237 criteria across five categories:

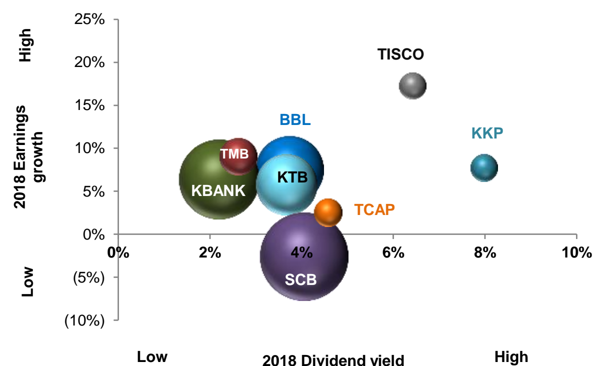
i. Rights of shareholders;
ii. Equitable treatment of shareholders;
iii. Role of stake holders;
iv. Disclosure and transparency;
v. Board responsibilities.

Figure 15: TISCO's NPL and LLC ratios



Source: Company data, RHB

Figure 16: EPS growth and dividend yield among banks



Source: Company data, RHB

Hong Kong/China

Figure 17: Diamonds from Hong Kong/China

Company	Ticker	Rating	Target (LCY)	Share price (LCY)	Market cap (USDm)	P/E (x)		P/BV (x)		EV/EBITDA (x)		ROAE (%)		Net margin (%)	
						FY18F	FY19F	FY18F	FY19F	FY18F	FY19F	FY18F	FY19F	FY18F	FY19F
CHINASOFT INTL	354 HK	BUY	7.77	6.50	2,013	18.0	14.7	2.2	1.9	12.3	10.4	13.8	15.2	6.7	7.2
CHINA STATE CONS	3311 HK	BUY	13.20	9.77	6,312	7.2	6.0	1.1	0.9	4.8	4.1	15.8	17.0	11.4	11.3
SHIMAO PROPERTY	813 HK	BUY	30.00	23.80	10,295	7.9	5.7	1.2	1.1	6.0	4.6	16.5	19.8	12.8	12.3

Note: Data as at 4 Jun 2018
Source: Bloomberg

Chinasoft (354 HK, BUY, TP: HKD7.77)

Chinasoft is a leader in IT services, as well as IT outsourcing services in China. It has in-depth expertise in serving main industries such as government and manufacturing, finance, telecommunications, and high tech. The company also engages in cloud services and owns *JointForce*, an online marketplace that connects programmers and businesses.

ROEs of 15% or more. Chinasoft's decent ROEs are a result of high single-digit NPM as well as financial leverage. We expect the company's ROEs to improve to 14% in FY18 and 15% in FY19 from 12% in FY17 due to improving NPMs.

Improving margins driven by new businesses. We believe Chinasoft's margins are on an upward trend for the next few years for the following reasons:

i. Its higher-margin new businesses (ie cloud, big data and *JointForce*) are growing much faster than the company's average growth rate. For FY18, revenue from these new businesses is expected to double that of FY17's and reach CNY2bn, accounting for 18% of total revenue compared vs 8% in FY17;

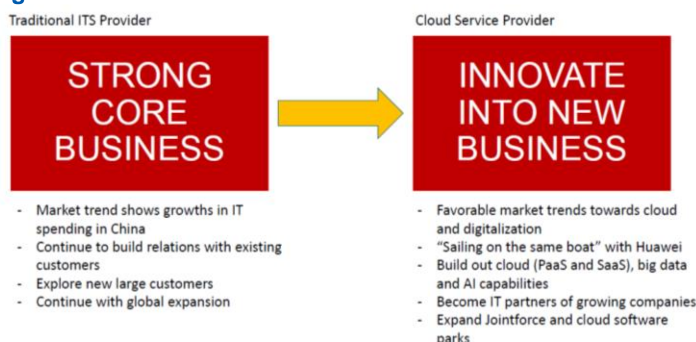
ii. Revenue from largest customer Huawei, which generates lower margins, is expected to have a softer growth outlook over the next couple of years, while business from other large customers with higher margins is still growing strongly;

iii. Chinasoft is building a powerful Software-as-a-Service (SaaS) and *JointForce* platform – it is also embracing artificial intelligence (AI) technology as well. All these initiatives may result in higher efficiency in delivering its IT services and improve margins in the long-run.

Trading below sector valuations. Chinasoft trades at FY18F P/E of 18x, below the sector's 27x. We think the main reason for this discount is its lower margins and the provision of lower-value added services – ie outsourcing or project-based IT services – when compared with pure play software companies such as Kingdee (268 HK, BUY, TP: HKD10.63). However, Chinasoft is on a fast-track to move up the value chain. Its revenue quality is set to improve to a more recurring and high-margin nature. In addition, the firm's earnings CAGR is better than peers at 29% for FY17F-20F, implying PEG of only 0.6x.

Chinasoft has sound corporate governance. The company has not changed its auditor (Deloitte Touche Tohmatsu) since its 2003 IPO. Chairman and CEO Dr Chen Yuhong does not have any side businesses either. Dr Chen – Chinasoft's largest shareholder – only holds 11% in the company. The other major shareholders include reputable IT companies such as Microsoft (4.05%) and Huawei (3.54%).

Figure 18: Chinasoft's transformation into a higher value-added and higher margin business model



Source: Company, RHB

China State Construction (3311 HK, BUY, TP: HKD13.20)

The company focuses on infrastructure construction. It primarily concentrates on Mainland China, Hong Kong and Macau.

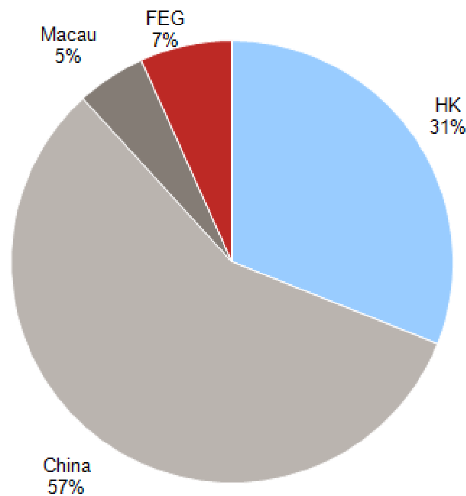
ROEs of 15% or more. China State Construction's (CSCI) strong ROEs (15.8% and 17% in FY18F-19F respectively) are mainly driven by Chinese public-private partnership (PPP) projects with high margins and returns. The company has a strong presence in the PPP market. The attractive returns of such projects should support revenue and earnings growth, as well as margins.

Strong margins driven by social housing. Social housing projects accounted for more than 50% of CSCI's China revenue in 2017 and this was the major reason for its rising GPM. Social housing redevelopment projects should continue to support its revenue, as there are 5.8m units slated for 2018 – this is large enough to support the company's social housing revenue growth. We estimate that CSCI will continue to benefit from social housing projects with relatively good execution and margins because such projects are less impacted by tightening PPP policies.

Trading below sector valuations. CSCI trades at FY18F P/E of 7.2x, below the sector multiple of 12.2x. We think the main reason for this discount lies with concerns over liquidity for PPP projects, given the strict bank loan requirements on such works. However, management is confident that, when compared with its peers that are private companies, its funding capability is stronger. This is because its parent company is a state-owned enterprise and CSCI is not limited by rules that govern such entities.

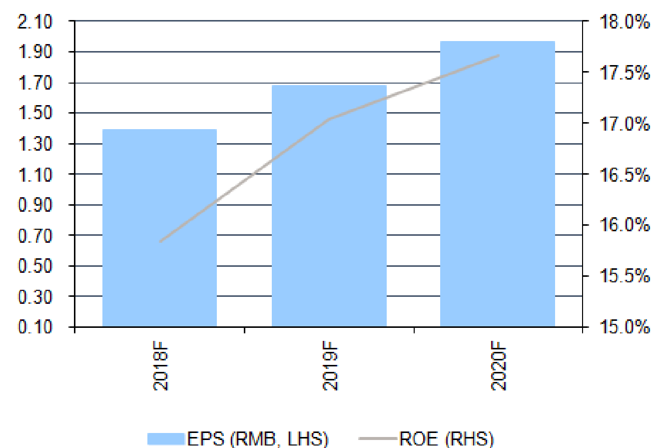
We believe CSCI has sound corporate governance. The company kept its auditor PricewaterhouseCoopers since 2013.

Figure 19: CSCI's revenue breakdown



Source: Company data, RHB

Figure 20: CSCI's EPS (HKD, LHS), ROE (RHS)



Source: Company data, RHB

Shimao Property (813 HK, BUY, TP: HKD30)

Shimao Property focuses on residential, commercial and hotel developments. It primarily concentrates on the Yangtze River Delta (YRD) region, although its presence has now spread to all of China's major regions.

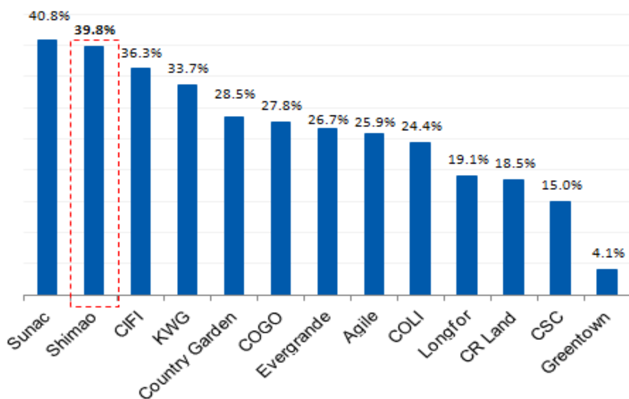
ROEs of 15% or more. Shimao's strong ROEs (16.5% and 19.8% in FY18F and FY19F respectively) are mainly driven by strong sales in Tier-2 cities and improving margins. The company has strong presence in such cities, especially Nanjing, Xiamen and Suzhou, as well as other urban centres in the YRD region. Its sufficient landbank in these key markets of 8.8m sqm GFA (or CNY200bn in terms of saleable value) – and being a widely-recognised expert in the luxury apartment segment – should contribute to strong sales growth in these markets. This, in turn, should support Shimao's asset turnover and ROEs over the next two years.

Widening margins. We anticipate Shimao's recurring NPM to rise to 12.8% in FY18F from 9.8% in FY17, thanks to the booking of surging contracted ASP of CNY16,000 per sqm in FY18F from CNY12,000 per sqm in FY15. As we see it, the negative impact on GPM brought by inventory clearance is over. Instead, its GPM should rebound to 31.2-31.7% over FY18F-20F from 27.6-30.4% during FY16-17.

Trading below sector valuations. Shimao is trading at a 40% discount to end-FY18F NAV, which is wider than its peers' 30% discount to NAV. Given its strong earnings momentum – 39.8% CAGR during FY17F-20F – we believe a premium valuation is justified instead. We believe the market is still underestimating Shimao's potential, both in terms of earnings growth and margins recovery. Our HKD30 TP is based on a 25% discount to end-FY18F NAV of HKD40.

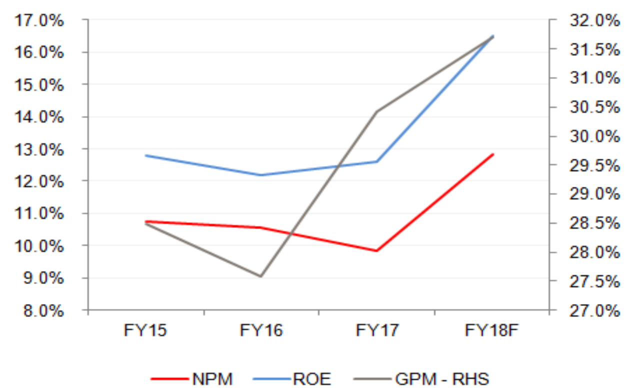
Reasonable corporate governance. Shimao has employed PWC as its independent auditor since its listing in 2006, and there has been no change in auditors up to now. The company has not made any restatements of its income statements since its IPO.

Figure 21: Ranked second in earnings CAGR for 2017-2020



Source: Company data, RHB

Figure 22: Rebounding margins and ROEs



Source: Company data, RHB

Singapore

Figure 23: Diamonds from Singapore

Company	Ticker	Rating	Target	Share price	Market (USDm)	1FY	P/E (x) 1FY	P/E (x) 2FY	P/BV (x) 1FY	P/BV (x) 2FY	EV/EBITDA (x) 1FY	EV/EBITDA (x) 2FY	ROAE (%) 1FY	ROAE (%) 2FY	Net margin (%) 1FY	Net margin (%) 2FY
APAC Realty	APAC SP	Buy	1.35	0.93	246	2018	11.0	10.7	2.3	2.1	6.9	6.2	21%	20%	7%	7%
GSS Energy	GSSE SP	Buy	0.25	0.15	55	2018	10.5	7.9	1.5	1.3	5.8	4.5	15%	18%	6%	7%
Japan Foods	JFOOD SF	Buy	0.63	0.51	66	2019	13.7	12.6	2.4	2.2	5.2	4.5	18%	18%	9%	9%
Singapore Exchange	SGX SP	Buy	9.00	7.28	5,832	2018	20.9	19.1	7.3	7.0	14.9	13.7	35%	38%	43%	44%

Note: Data as at 5 Jun 2018
Source: Bloomberg, RHB

APAC Realty (APAC SP, BUY, TP: SGD1.35)

APAC Realty is one of the leading players in the Asian real estate brokerage industry. It provides real estate brokerage services in Singapore under the *ERA* brand. The group also has exclusive regional master franchise rights for *ERA* in 17 countries within the Asia-Pacific region. Besides brokerage, it also derives revenue from franchise agreements, training, valuation and other ancillary services. *ERA* is the market leader in Singapore residential market, with a market share of 36.3% in terms of overall transaction value.

APAC has superior ROEs of >20% mainly due to a high asset turnover ratio, as the business model is asset light and highly scalable. It is worth noting the company has no debt and a net cash position of SGD64m. In FY17, it reported an ROE of 24.4%. ROEs should remain around the 20% level, as we expect APAC to benefit from the current improvement in residential property volumes.

Net margins to improve on operating leverage. APAC's opex as a percentage of revenue is expected to come down to 5.6% in 2019 from 7.2% in 2016 – the key reason being economies of scale, as opex can be shared across a larger network of agents. About 70% of APAC's operating costs were fixed in 1Q18. As a result, net margins are expected to expand to 6.7% (FY17: 6.5%) in 2019.

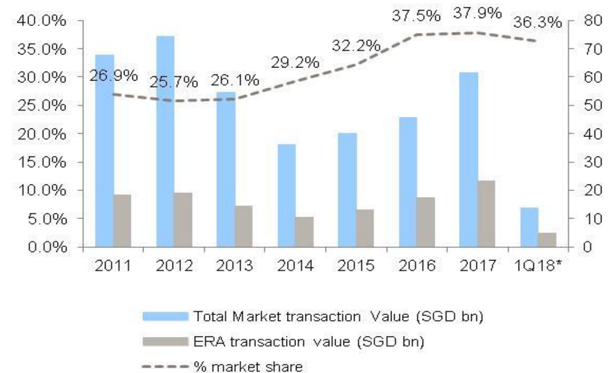
Trading at attractive valuations. APAC is trading at 11x 1-year forward P/E vs 14x for its global industry peers. Possible reasons for the discount could be the potential listing of another Singapore real estate agency on the SGX, and investors' concerns over additional property cooling measures being implemented by the Government. We maintain that APAC is in a strong position to tap the recovery in residential sales. Thus, we believe there is potential for the valuation discount to narrow as residential volumes continue to move higher in coming years.

Good corporate governance. We believe APAC has strong corporate governance. Northstar, a Singapore-based private equity firm that manages more than USD2bn in committed equity capital, is the largest shareholder and owns around 55% of APAC. The management team holds an about 17% stake, indicating an alignment of its interest with shareholders in growing the business.

Figure 24: APAC's gross and net margins

Source: Company data, RHB

Figure 25: APAC's market share in Singapore



Source: Company data, RHB

GSS Energy (GSSE SP, BUY, TP: SGD0.25)

GSS Energy (GSS) has two businesses – oil & gas, and precision engineering (PE). The company, previously known as Giken Sakata (Giken), operated the PE business division and was listed on the SGX in Feb 1993. GSS, which had ventured into the energy business in 2014, took over Giken's listing status in Feb 2015, as the latter became a wholly-owned operating subsidiary of the former. GSS' current twin operations enable the group to build greater resilience and cushion against rising uncertainties in the business environment and global economy.

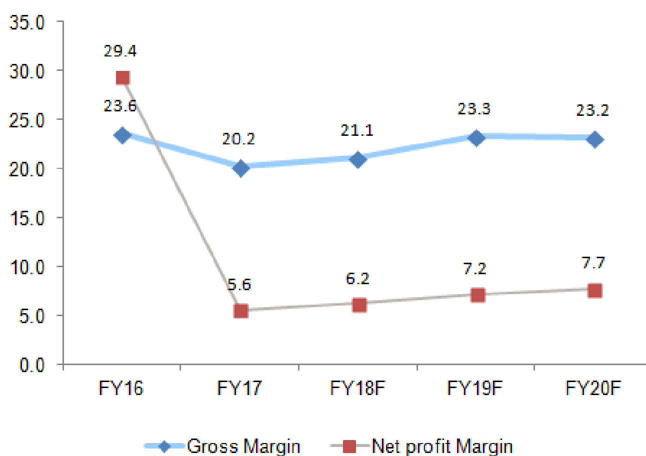
Expanding net margins. GSS' gross and net margins should continue to improve, as we foresee contribution to start coming from its oil & gas segment, which has so far been a drag to its earnings. In addition, the inclusion of new projects in the PE segment should also enhance the operating leverage on its net margins. We expect net margins to slowly trend up to 7.7% in FY20F from 5.6% in FY17.

ROE to slowly trend up above 15%. GSS' ROE witnessed a sharp decline in FY17 since its FY16 ROE included an exceptional gain from the sale of a China-based factory to the local government. Its ROE reached normalised levels in FY17 and is likely to continue trending up. This is due to improvements at its PE business and expected revenue contributions from its oil & gas business, which has been loss-making thus far.

Trading at a lower multiple. Using manufacturing players in Malaysia and Singapore as peer comparisons, we assess that GSS is trading at a lower P/E multiple vs its peers' average. Even if we exclude the Malaysia-listed manufacturers, as they generally trade at a premium to Singapore-listed manufacturers, GSS is still trading at a discount to the peer average. We believe this could be due to investors' concerns about the oil & gas exploration business, which we think should abate once revenue contributions from the energy business kicks in from 2H18.

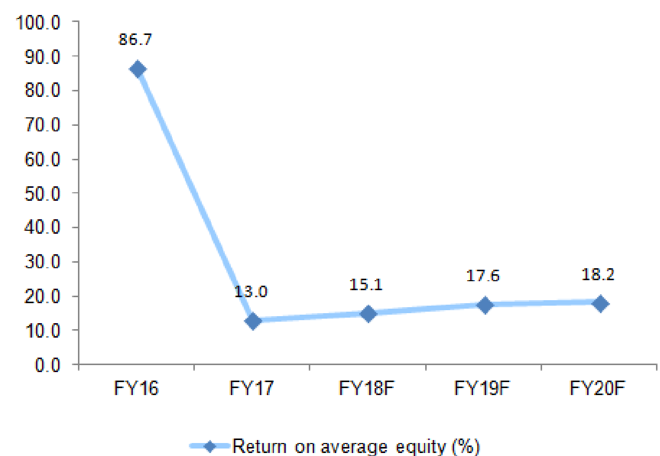
We believe GSS has reasonable corporate governance. Management has displayed transparency and been proactive in dealing with investor and analyst concerns about its energy business.

Figure 26: GSS' gross & net margins



Source: Company data, RHB

Figure 27: GSS' return on average equity (%)



Source: Company data, RHB

Japan Foods (JFOOD SP, BUY, TP: SGD0.63)

Established in 1997, Japan Foods (JFH) is one of the leading food & beverage (F&B) groups in Singapore, specialising in quality and authentic Japanese cuisine. As at March, the group – together with its sub-franchisees – operated 50 restaurants and food court outlets under various brands in Singapore, Malaysia and Vietnam. It also has interests in 18 restaurants in Hong Kong and China through associated companies.

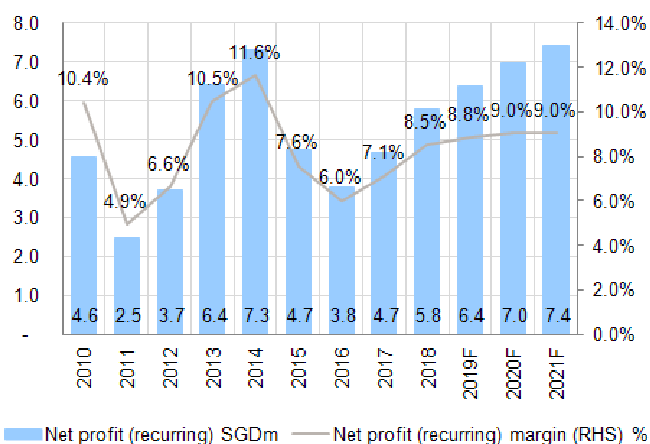
Expect net margin to expand. Improving operational efficiency, using raw materials more effectively, building economies of scale through the setting up of a central kitchen, and achieving greater bulk purchase discounts, are some of the ways how JFH has mitigated the increase in costs and enhanced its gross margins. The group's gross margins have increased to 85% in FY17 from 78% in FY10. While it continues to find ways to further enhance its profit margins, we believe further GPM growth will be small in nature. However, we assess that greater control on selling and distribution expenses, continued focus on improving revenues of its key brands, and slightly higher contributions from its associates, ought to lead to improvements in its NPMs during the forecast period. We expect JFH's net margins to expand to 9% in FY21 from 8.5% in FY18.

Strong ROE, which can improve further. JFH offers a high ROE of 14.9% despite having a net cash balance sheet. Its ROE is among the highest offered by SGX-listed restaurant operators. In addition to superior net margins, the high ROE is also supported by high asset turnover. We assess that strong growth in earnings during FY18F-20F will lead to improvements in its ROEs. We expect ROEs to improve to 17.8% in FY21 from 17.6% in FY18.

Strong corporate governance. JFH's management has a long history with the company. CEO Mr Takahashi Kenichi founded JFH in 1997. The current chief operating officer has been with the company since 1999, while the current CFO has been with the firm since 2008. Transparency in JFH's reporting standards has been noteworthy. We seldom come across companies that provide detailed information on the success and failure of new ventures on a quarterly basis. JFH won the Transparency Award for SMEs at the 18th Securities Investors Association (SIAS) Investors' Choice Awards 2017.

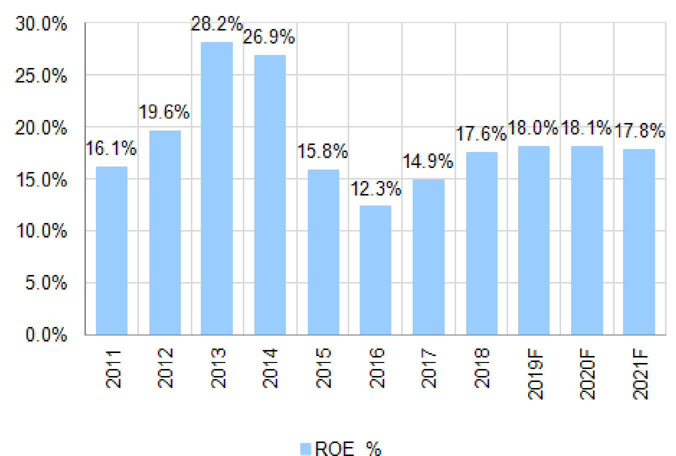
We believe JFH's discount relative to peers is unjustified, given its industry-leading dividend yield, high GPMs, improving ROEs and steady earnings growth prospects.

Figure 28: JFH's net profit and net profit margin outlook



Source: Company data, RHB

Figure 29: JFH's ROE to gradually improve



Source: Company data, RHB

SGX (SGX SP, BUY, TP: SGD9)

Singapore Exchange (SGX) owns and operates Singapore's securities and derivatives exchange and related clearing houses. The company also provides ancillary securities processing and information technology services to participants in the financial sector. Its earnings are dependent on the securities average daily value (SADV).

Margin expansion to come from stronger SADV. Global equity markets witnessed an uptrend in 2017, which contributed to a strong 9% YoY growth in SADV in 2017. Global equity market trading volatility is expected to drive SADV in the coming months. We estimate FY18 SADV of SGD1.20bn, up 7% YoY from FY17. This should drive margin expansion as we move forward – do note that any improvement in SADV (and corresponding growth in revenue) flows almost completely to pre-tax profit.

We are positive on the Bursa-SGX link – which was announced in early Feb 2018. This would enable cross-border clearing and settlement of traded stocks. The implementation is expected to take time and should contribute to SADV growth in the longer term. Note that, in early June, Malaysia's new Government indicated that it will relook at the plans for the trading link. We await further updates.

Earnings downside risk could come from ceasing of Indian derivative product being traded on SGX, the continuation of which is dependent on the outcome of the company's arbitration with India Index Services and Products (IISL) in mid-June. We estimate the impact to be relatively small, as India-related derivatives account for only 4-5% of SGX's revenue.

Mid-30s ROE is superior to regional peers like HKEx's mid-20s and Bursa Malaysia's high-20s. This is due to its superior asset turnover ratio. We forecast ROEs to remain in the mid-to-high 30s for the next 2-3 years – driven by stronger SADV expectations.

Trading at a lower P/E than historical mean. SGX trades at FY19F P/E of 19x, which is lower than the historical 3-year mean of 22.2x. Given expectations of strong growth in SADV, we believe it deserves to trade at a higher FY19 P/E of 24x, 1SD above the 3-year mean of 22.2x.

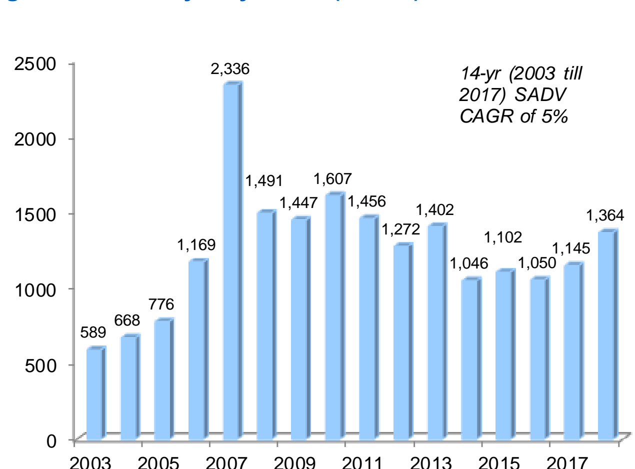
Strong corporate governance. SGX has strong corporate governance. SEL Holdings has a 23% shareholding in the firm. Its shareholding in SGX has been stable over the past few years.

Figure 30: SGX's TP sensitivity

FY19F						
Stkmkt turnover % rise	Base	20	40	60	(20)	(40)
Securities ADV (SGDbn)	1.39	1.67	1.94	2.22	1.11	0.83
Revenue (SGDm)	938	1,004	1,071	1,137	871	805
Net profit (SGDm)	409	462	515	568	356	303
EPS (SGD)	38.2	43.1	48.1	53.0	33.2	28.3
Target PE rating	24	24	24	24	24	24
Target Price (SGD)	9.00	10.17	11.33	12.50	7.84	6.67

Source: Company data, RHB

Figure 31: SGX's yearly SADV (SGDm)



Source: Company data, RHB

Indonesia

Figure 32: Diamonds from Jakarta

Company	Ticker	Rating	Target price	Share price	Market cap (USDm)	P/E (x)		P/B (x)		ROAE (%)		Operating Margin (%)		Net margin (%)	
						FY18F	FY19F	FY18F	FY19F	FY18F	FY19F	FY18F	FY19F	FY18F	FY19F
Astra International	ASII IJ	Buy	8,450	7,000	20,999	13.4	11.6	2.1	1.9	16.5	17.4	10.3	10.5	9.7	10.1
Gudang Garam	GGRM IJ	Buy	91,100	68,500	9,251	15.6	13.4	2.9	2.6	19.2	20.5	13.1	13.2	9.0	9.3

Note: Share price and market cap data as at 4 Jun 2018
Source: Bloomberg, RHB

Astra International (ASII IJ, BUY, TP: IDR8,450)

Astra International is a conglomerate with diversified earnings, which come from its auto, financial, infrastructure, and commodities businesses.

ROEs of 15% or more. We see Astra's FY18F ROE improving to 16.5% from FY17's 16% thanks to widening NPMs for its heavy equipment and mining contractor divisions. Four weather forecasters – Indonesian Agency for Meteorology, Climatology and Geophysics (BMKG), Japan Agency for Marine-Earth Science and Technology (Jamstec), Bureau of Meteorology/Predictive Ocean Atmosphere Model for Australia (BoM/POAMA) and National Centres for Environmental Predictions/National Oceanic and Atmospheric Administration NCEP/NOAA – all share the same view. They believe *La Nina* ended in April and the weather has normalised at least until October. This should lift mining contracting volumes.

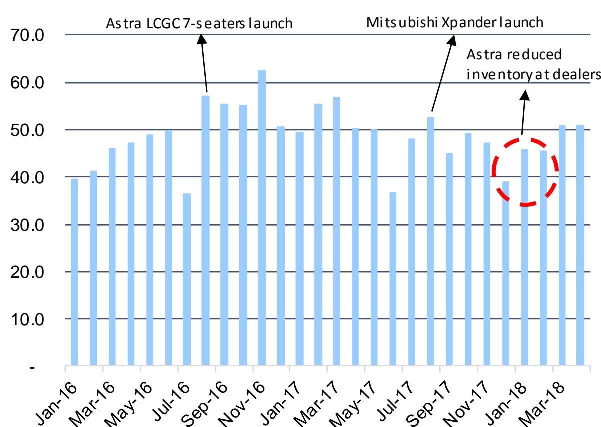
For the auto division YTD-April, Astra's two-wheel (2W) vehicle wholesales were better than expected. Furthermore, we expect four-wheel (4W) vehicles wholesales to pick up from a low base in Dec 2017. Management said its 4W vehicles inventory was already at a healthy level, which led to monthly car wholesales numbers to normalise in April.

Widening margins. We expect Astra's widened FY18F EBIT margins to be driven by heavy equipment and coal mining contractors. Management is confident that better weather – which has been improving since April – should enable Astra's heavy equipment and coal mining contracting division's EBIT margins to improve. We do see its auto EBIT margin remaining stable, but this is no thanks to the intense competition in the 4W vehicles industry, especially the low-MPV market.

Trading below the sector valuation. The counter is attractively trading at around -2SD from its average forward P/E. Its share price declined about 15% YTD, making its valuation more attractive. A key risk to our call is the competition in the 4W market, which likely to remain intense. At current levels, though, we see this as being been priced-in.

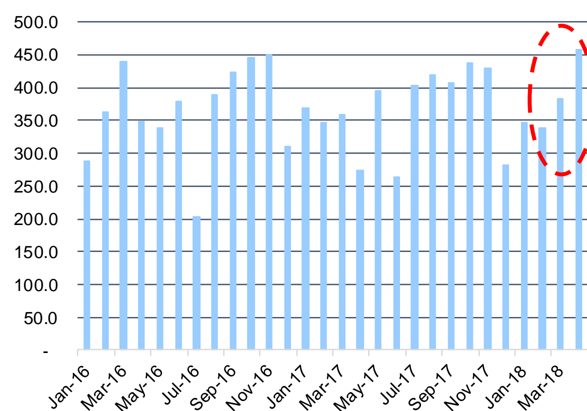
Good corporate governance. Astra is well known for its good corporate governance. Financial statements are audited by PWC and the firm has well-managed information flows to avoid insider trading. Management is also staffed by professionals. Jardine Cycle & Carriage is the majority shareholder (50.1%), with the remainder as free float.

Figure 33: Astra's 4W sales ('000 units)



Source: Association of Indonesian Automotive Industries (Gaikindo), Company data, RHB

Figure 34: Astra's 2W sales ('000 units)



Source: Indonesian Motorcycle Industries Association (AISI), Company data, RHB

Gudang Garam (GGRM IJ, BUY, TP: IDR91,100)

Gudang Garam is a leading producer of *kretek* cigarettes, the clove cigarette synonymous with Indonesia. It is the second-largest cigarette producer in Indonesia just behind HM Sampoerna (Sampoerna), a subsidiary of Philip Morris International.

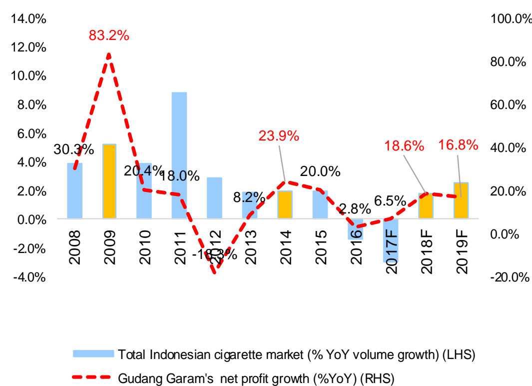
Gudang Garam has consistently had ROEs above 15% for years. This was the result of a combination of decent EBITDA margins (at around 15%) and leverage ratios – its asset/equity has always been higher than 1.5x, as the company utilises bank loans to fund its working capital for tobacco leaf purchases. Gudang Garam plans to maintain its leverage ratio at similar levels in the years ahead. Its asset turnover is relatively stable at around 1.2x, as its inventory days outstanding is relatively high at around 230 days. This results in a cash conversion cycle of between 220-240 days.

Widening margins. We estimate NPM to expand slightly in the years ahead to higher than 9%. This is on higher economies of scale, as its sales volume should increase in the years ahead.

Trading below the valuation of Sampoerna. Gudang Garam trades at 15.6x FY18F P/E, which is much lower than its competitor Sampoerna's 32.5x. We understand the latter's high ROE of around 40% – vs the former's around 18% – should result in a higher P/E multiple. However, we think the significant difference between the two is unjustified, considering that Gudang Garam is likely to book faster earnings growth than Sampoerna over the next two years. This is because the market for machine-made full flavour *kretek*, which is Gudang Garam's main expertise, is in a growing trend.

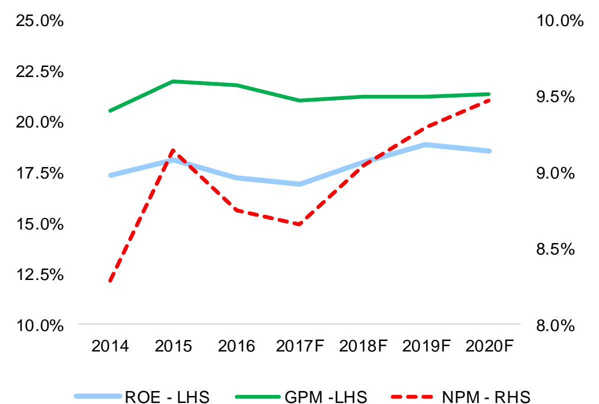
Reasonable corporate governance. The company is managed and overseen by president director Mr Susilo Wonowidjojo and president commissioner Mrs Juni Setiawati Wonowidjojo. Its other directors and commissioners are all professionals, and the firm has been audited for years by KPMG.

Figure 35: Gudang Garam's cigarette volume and earnings growth should improve in 2018 and 2019 as it did during the previous election years (2009 and 2014)



Source: Company data, RHB

Figure 36: Chart margins and ROE profiles



Source: RHB, Company data

RHB Guide to Investment Ratings

Buy: Share price may exceed 10% over the next 12 months
Trading Buy: Share price may exceed 15% over the next 3 months, however longer-term outlook remains uncertain
Neutral: Share price may fall within the range of +/- 10% over the next 12 months
Take Profit: Target price has been attained. Look to accumulate at lower levels
Sell: Share price may fall by more than 10% over the next 12 months
Not Rated: Stock is not within regular research coverage

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