12 January 2023

Construction & Engineering | Construction

Vestland

A Formidable Design & Build Services Provider

Fair Value (Return):	MYR0.37 (+12%)
IPO Price:	MY0.33
Closing Application Date:	16 Jan 2023
Indicative Listing Date	31 Jan 2023

- **FV of MYR0.37 on 10x FY23F P/E.** Vestland intends to raise MYR56.1m from the public issue of 170m new shares. These proceeds will mainly be used to fund working capital, to further strengthen its design & build segment, which fetches greater added value in terms of better project oversight and cost management. Future earnings should be anchored by its diverse portfolio in private and government projects, spanning across the residential (high-rise property) and non-residential (police camps and warehouses) segments.
- **Commendable orderbook growth prospects.** The group has MYR947.4m worth of work orders in hand as at 28 Nov 2022 (the latest practicable date or LPD), translating into an orderbook/revenue cover ratio of 5.5x (higher than the 3x mean for the stocks under our coverage) based on FY21 revenue. Around 69% of its total outstanding orders are made up of high-margin (c.3-5ppts higher than build-only projects in terms of gross profit margin) design & build projects, followed by the build segment (23%) and civil engineering works (8%). Job replenishment prospects are backed by the group's tenderbook of MYR2.1bn (estimated success rate of 30-35%) as at the LPD, of which 55.2% comprises design & build projects – these include industrial properties such as warehouses for Armani Group and Sime Darby (SIME MK, BUY, TP: MYR2.80).
- **Earnings estimates.** We are projecting a 5-year earnings CAGR of 43.5% for Vestland, largely in tandem with its stronger orderbook replenishment and project mix. We think that Vestland should be able to retain its existing clients and attract new ones, due to its capability in design & build construction services that command better margins. Recurring net profit margins are expected to be at 8.1-8.5% in FY23-24, taking into account yearly replenishment order assumptions of MYR750m for the period.
- **Valuation.** We ascribe a FV of MYR0.37, based on a target 10x FY23F P/E. For peer comparison purposes, we chose small to mid-cap construction players such as, Kerjaya Prospek (KPG MK, BUY, TP: MYR1.44), MGB (MLG MK, BUY, TP: MYR0.64), Gabungan AQRS (AQRS MK, BUY, TP: MYR0.46), and Inta Bina (INTA MK, NR). We believe that this target valuation of 10x is justified, as it is within our range ascribed to the majority of small to mid-cap contractors under our coverage. The target valuation, being at the high end of the 8-10x range ascribed to small and mid-cap contractors, takes into consideration its earnings growth potential of over 50% YoY in FY23F, backed by better job replenishment prospects – particularly for the design & build segment.
- **Key downside risks:** Being dependent on foreign workers, fluctuation in the prices of building materials, disruptions in operations due to COVID-19, and the loss of key management personnel.

Analyst

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Company Description

Vestland is principally involved in the construction of residential and non-residential buildings.These residential and non-residential projects are further divided into the: i) build segment, and ii) design & build segment. A small portion of the group's business is in civil engineering works which the group ventured into back in FY21.

IPO Details

Public Issue of shares (m)	170.0
Offer for sale of existing shares (m)	70.8
Shares outstanding (m)	944.3
Implied market cap (MYRm)	311.6

Major Shareholders (%)

Datuk Liew Foo Heen	85.0
Wong Sai Kit	15.0

Utilisation of IPO Proceeds	MYRm
Acquisition of new head office/refinancing of borrowings for acquisition of the new head office	7.5
Performance bonds and/or cash deposits for construction projects	10.8
Working capital	33.5
Estimated listing expenses	4.3
TOTAL	**56.1**

Additional Data

Listing Market	Ace
Bursa Code	0273

Forecasts and Key Data	Dec-20	Dec-21	Dec-22F	Dec-23F	Dec-24F
Total turnover (MYRm)	97.1	171.1	298.8	414.4	499.0
Gross Profit (MYRm)	14.3	23.5	43.3	64.2	74.9
EBITDA (MYRm)	12.3	17.9	32.1	49.7	57.0
Recurring net profit (MYRm)	8.4	11.3	22.3	35.3	40.5
Recurring net profit growth (%)	26.3	34.2	98.4	58.2	14.6
Net margin (%)	8.6	6.6	7.5	8.5	8.1
Recurring EPS (MYR)	0.01	0.01	0.03	0.04	0.04
Recurring P/E (x)	30.5	24.0	11.4	8.8	7.7
Dividend yield (%)	0.0	0.0	0.0	2.8	3.2
Net debt to equity ratio (x)	0.5	0.3	Net Cash	Net Cash	Net Cash

Source: Company data

Note:
Small cap stocks are defined as companies with a market capitalisation of less than USD0.5bn.

Financial Overview And Valuation

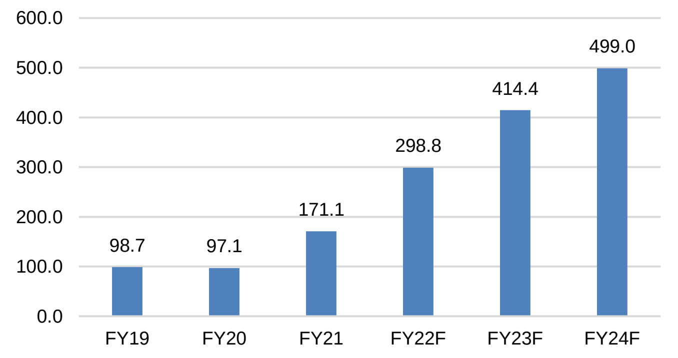
6MFY22 results review. Vestland's 6M22 core net profit of MYR11.6m represented a >150% YoY growth from MYR4.2m in 6M21 – which translated to a higher core net profit margin of 8.3% (6M21: 6.3%). This was mainly attributable to the design & build segment that particularly delivers higher margins compared to normal building projects – which recorded a 327% YoY jump in revenue during 6M22, backed by recognition of work done on projects under the segment, mainly the Beluran Police Camp, Residensi Armani Petaling (Cheras), and Armani Subang Soho amongst others.

Meanwhile, the build segment recorded a revenue growth of only 1.2% YoY in 6M22 to reach MYR45.5m (33% of total revenue). The better progress from projects under the segment such as KKB Academic Building and Student Accommodation, CPL Aromas Pulau Indah and D'vine Residences project helped to partly offset projects that were nearing completion in 6M22, namely the Glenz Mixed Commercial Development project and the Perumahan Penjawat Awam 1 Malaysia or PPA1M Houses project. The civil engineering works segment (where its numbers were only recognised from 2H21 onwards) contributed 1.7% of revenue in 6M22, from six civil engineering works projects which commenced in 2H21 and January.

Net cash position post-IPO. Vestland's latest net gearing ratio stood at 0.1x as at end-6M22, compared with 0.5x and 0.3x in FY20 and FY21. Out of the MYR56.1m the group plans to raise, MYR7.5m or 13.4% of the proceeds have been partly earmarked for the refinancing of borrowings to acquire the new office. With that, we envisage Vestland to be in a net cash position post listing, especially with its latest minimal net gearing levels as of end 6M22.

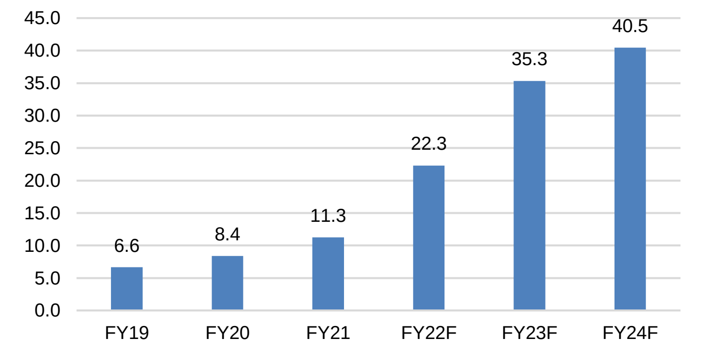
Dividend policy. Presently, Vestland has no formal dividend payout policy in place. The last dividend payment made by the group was back in FY19, with a payout ratio of 31.4%. However, since group is estimated to be in a net cash position post-listing, we do not rule out the possibility of dividends for shareholders. As such, we have pencilled in a 25% dividend payout ratio for FY23-24F which translates into prospective yields of 2.8-3.2% based on the IPO price for the said period.

Figure 1: Vestland's revenue trend (MYRm)



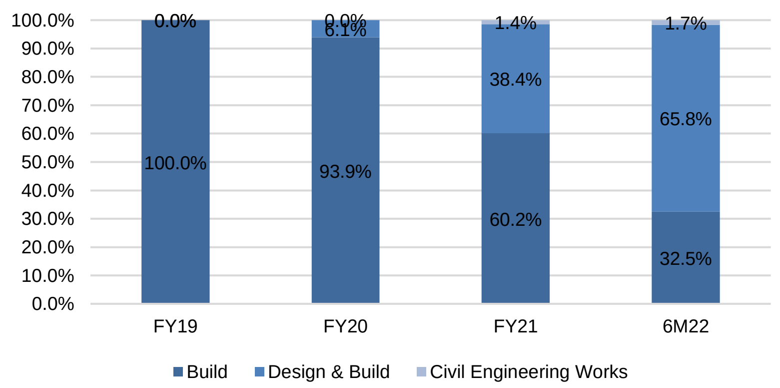
Source: Company data, RHB

Figure 2: Vestland's core net profit trend (MYRm)



Source: Company data, RHB

Figure 3: Vestland's revenue breakdown

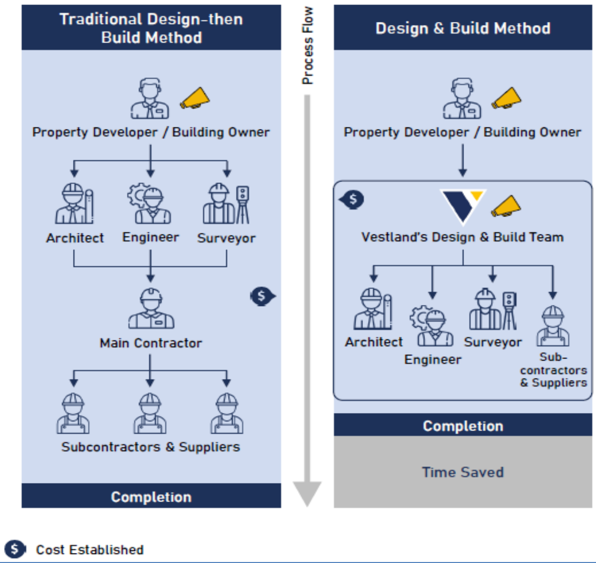


Source: Company data

Earnings forecast. We are projecting a 5-year earnings CAGR of 43.5% for Vestland, largely in tandem with its stronger orderbook replenishment and project mix. We opine that Vestland should be able to retain its existing clients and attract new ones, due to its capability in design & build construction services, which commenced in FY20 when the group secured the Residensi Armani Petaling (Cheras) project worth MYR58m. Since the group is involved in design and conceptualisation from the inception of a project itself – by providing input from the construction perspective under its design & build segment – it enables Vestland to have better coordination and planning with respect to the construction project, including *inter alia*, designing to the allocated budget and having better control over the construction period. The costs of all aspects of the project are taken into consideration early on in the design phase, and the group is able to provide input towards potential cost-saving construction measures, usage of raw materials and speed of construction. This results in higher margins for the design & build segment – leading us to forecast a recurring net margin of 7.5-8.5% for FY22-24.

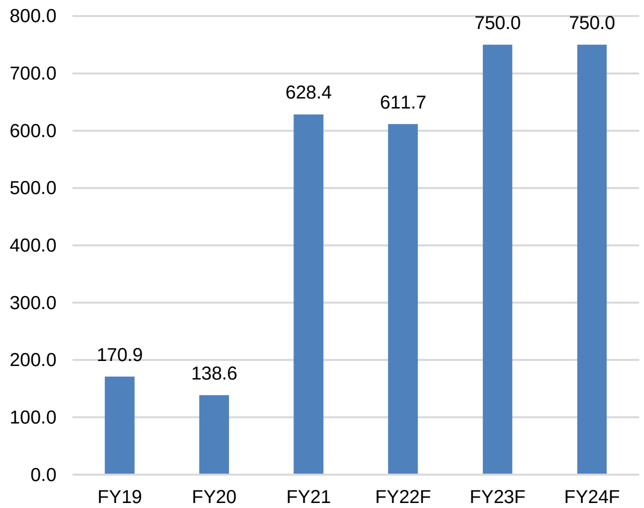
Orderbook prospects. Vestland's latest outstanding construction orderbook of MYR947.4m as of the LPD translates into an orderbook-to-revenue cover ratio of 5.5x (higher than the average of 3x for the stocks under our coverage) based on FY21 revenue. Around 69% of the total outstanding orders are made up of high-margin design & build projects, followed by the build segment (23%) and civil engineering works (8%). The group's tenderbook size stands at MYR2.1bn as at the LPD of which 55.2% is comprised of design & build projects – which includes industrial properties such as warehouses for Armani Group and Sime Darby in addition to the government-related project for the Rumah Keluarga Angkatan Tentera. With an estimated success rate of 30-35%, we impute a job replenishment rate of MYR750m for FY23 and FY24, backed by its design & build expertise.

Figure 4: Traditional design-then-build method vs design & build method



Source: Company data

Figure 5: Vestland's historical and estimated job replenishment levels (MYRm)



Source: Company data, RHB

Valuation. Our FV of MYR0.37 is based on a target 10x FY23F P/E. For peer comparison purposes, we chose small- to mid-cap construction players such as Kerjaya Prospek, MGB, Gabungan AQRS and Inta Bina, given their exposure to residential and non-residential building projects. This target valuation of 10x is justified, as it is within our range ascribed to the majority of small- to mid-cap contractors under our coverage. The target valuation being at the high end of the 8-10x range ascribed to small and mid-cap contractors takes into consideration of its earnings growth potential of over 50% in FY23F, backed by better job replenishment prospects – particularly for the design & build segment. Our target P/E of 10x is also derived by applying a c. 20% small-cap discount to the Bursa Malaysia Construction Index's 5-year mean P/E of 12x.

At an IPO price of MYR0.33, the stock is trading at 8.8x FY23F P/E, which is lower than Kerjaya Prospek's and MGB's 9.4-9.9x, but higher than Gabungan AQRS' and Inta Bina's 3.4-6.8x.

Figure 6: Peer comparison

Company	FYE	Mkt Cap (MYRm)	Price 9-Jan-22 (Local Currency)	P/E (x) Actual	P/E (x) 1 Yr Fwd	P/E (x) 2 Yr Fwd	Div. Yld (%) 1 Yr Fwd	ROE (%) 1 Yr Fwd	EV/ EBITDA 1 Yr Fwd	NP Growth (%) 1 Yr Fwd	NP Growth (%) 2 Yr Fwd
Vestland[1]	Dec	311.6	0.33	24.0	14.0	8.8	0.0	32.5	9.3	98.4	58.2
Peers											
Kerjaya Prospek	Dec	1,475	1.17	15.2	11.9	9.4	4.0	10.8	6.0	28.1	26.4
MGB	Dec	314	0.53	11.6	21.4	9.9	1.5	2.9	6.7	-45.8	116.4
Gabungan AQRS	Dec	138	0.26	8.8	4.6	3.4	3.9	6.3	4.5	93.4	34.2
Inta Bina	Dec	123	0.23	10.5	9.4	6.8	4.3	8.9	5.0	12.1	37.4
Mkt. Cap Weighted Avg. (excluding outliers)				**14.0**	**12.7**	**8.9**	**3.6**	**9.2**	**6.0**	**20.3**	**41.3**
Simple Avg. (excluding outliers)				**11.5**	**11.8**	**7.4**	**3.4**	**7.2**	**5.5**	**21.9**	**53.6**

Note: As at 9 Jan 2023
Note 2: [1]Based on indicative IPO price
Source: Bloomberg, RHB

Future Plans And Strategies

Working capital expansion. Gross proceeds worth MYR33.5m or 59.7% of the total gross proceeds have been earmarked by the group for working capital – mainly to pay for subcontractor services (MYR25m) and buy construction materials (MYR8.5m), as these made up >80% of the group's cost of sales in the past three financial years. In terms of projects, the group has identified the Beluran Police Camp (27.5% completed as at LPD) and the D'vine Residences Project (9.5% completed as at LPD) to make use of the working capital raised. Nevertheless, with higher expected job wins backed with new job win targets of MYR750m each year for FY23-24, any excess working capital could be channelled to its future projects in the pipeline. The working capital allocation is expected to enhance the group's liquidity and cash flow, and reduce its reliance on external financing to support the expected growth in its daily operations.

Upsizing its operational facility. In line with the group's business expansion, the group had, on 23 Sep 2021 and 19 Jan 2022, entered into sale-and-purchase agreements with SG Besi Construction to acquire a new head office at the Glenz Mixed Commercial Development Project in Shah Alam, Selangor for MYR9.3m. Construction of the new head office was completed in Mar 2022, and comprises 12 office suites with an aggregated built-up area of 10,803 sq ft. Vestland's current rented premises, in contrast, has an aggregate built-up area of 7,834 sq ft. The number of employees based at its rented office has increased from 25 (as at 31 Dec 2019) to 51 as at the LPD. Therefore, the new head office will accommodate a larger number of workstations for its expanded workforce, as well as additional meeting rooms to facilitate meetings with external parties and external discussions. MYR7.5m or 13.4% of the IPO proceeds will be channelled towards refinancing borrowings for the acquisition of the new head office.

Enlarging its construction orderbook. As highlighted earlier, Vestland has an outstanding orderbook of MYR947.4m (4-5 years of earnings visibility) backed by a tenderbook of MYR2.1bn (estimated success rate of 30-35%) as at the LPD. Moving forward, the group plans to grow its orderbook by tapping on its higher-margin design & build segment to address opportunities in both residential and non-residential buildings. It will focus marketing efforts towards prospective customers, while retaining existing ones. Although the design & build method, in general, would result in cost savings for the client (or lower contract values, such attributes would lead to better client retention, which may facilitate in replenishing its orderbook.

Moreover, we take comfort that MYR670m or 58.9% of the MYR1.1bn tendered for design & build projects consist of logistics warehouse projects. As at the LPD, Vestland only has one warehouse-related project – KKIP Warehouse project for Armani Group worth MYR56.1m (12% of the design & build segment orderbook) under its outstanding orderbook. We are upbeat on Vestland's move to focus on more industrial properties such as warehouses, as the industrial property segment has been gaining traction since the country entered into the endemic phase in terms of COVID-19, back in Apr 2022. On further scrutiny, Vestland's design & build tenderbook covers new potential clients such as Sime Darby and Integrasi Momentum – indicating that the group is gradually diversifying its client base from Armani Group, Binastra Construction, and government-related projects. The group also plans to eye more social infrastructure government jobs such as public government offices, schools, hospitals, police, and army facilities.

Vestland's civil engineering works segment, which contributes 7.8% of the group's latest outstanding construction orderbook, serves as a platform for growth. This is because works done for the civil engineering sub-sector in 3Q22 grew for the first time (by 14.6% YoY) after three straight quarters of decline, according to the Department of Statistics Malaysia – implying that the sub-sector is undergoing a recovery. It is worth noting that the civil engineering works that the group is involved in are secured from private parties such as the Habu Cameron Infrastructure project by Armani Group – limiting the risks of reviews or job cancellations arising from government policies.

Figure 7: Impact of adapting the design & build method for the Tanah Rata Cameron Project

	Initially project proposed via Design-then-Build Method (Main Contractor)	Vestland implements its Design & Build Capabilities	
Number of Unit (Nos)	224	288	▲ 28.6%
Net Saleable Area (Sq.ft)	163,912	211,076	▲ 28.8%
Gross Floor Area (Sq.Ft)	393,083	338,702	▼ 13.8%
Gross Development Value (RM) – RM550/sq.ft	94,911,000.00	116,637,400.00	▲ 22.9%
Client's Contract Sum (RM)	61,375,000.00	40,000,00.00	▼ 34.8%
NSA/GFA (%)	42%	62%	▲ 47.6%
Start & End Date	Jan 2022 – Jan 2025		

Source: Company

Figure 8: Vestland's tenderbook breakdown

Project	Client	Location	Value (MYRm)
Build projects			
Army Camp	Government	Lahad Datu, Sabah	580.0
Condominium	Binastra Construction	Kampung Kasipillay , Kuala Lumpur	172.8
PR1MA Housing	Government	Karang, Kuantan, Pahang	120.8
Others	Various	Various	56.5
Total Build projects			**930.1**
Design & build projects			
Rumah Keluarga Angkatan Tentera	Government	Kota Kinabalu, Sabah	450.0
Logistics Warehouse	Sime Darby	Klang, Selangor	350.0
Logistics Warehouse	Armani Group	Kuala Langat, Selangor	230.0
Logistics Warehouse	Armani Group	Pulau Indah, Selangor	90.0
Building works	Integrasi Momentum	Kepong, Kuala Lumpur	24.4
Total Design & Build projects			**1,144.4**
Total tenderbook			**2,074.5**

Source: Company data

Figure 9: Utilisation of IPO proceeds

Details	Amount (MYRm)	Percentage (%)	Estimated timeframe for utilisation upon listing
Acquisition of the new head office / refinancing of borrowings for acquisition of the new head office	7.5	13.4	Within 3 months
Performance bonds and/or cash deposits for construction projects	10.8	19.2	Within 15 months
Working capital	33.5	59.7	Within 12 months
Estimated listing expenses	4.3	7.7	Within 3 months
Total	**56.1**	**100.0**	

Source: Company data

Company Overview

Vestland is principally involved in the construction of residential and non-residential buildings. Residential buildings include apartments and landed residential buildings, while non-residential buildings include mixed-use commercial buildings and offices, industrial buildings, service apartments, hostels and hotels. These residential and non-residential building projects are further divided into the: i) Build segment, and ii) design & build segment. A small portion of the group's business is in civil engineering works which commenced in FY21.

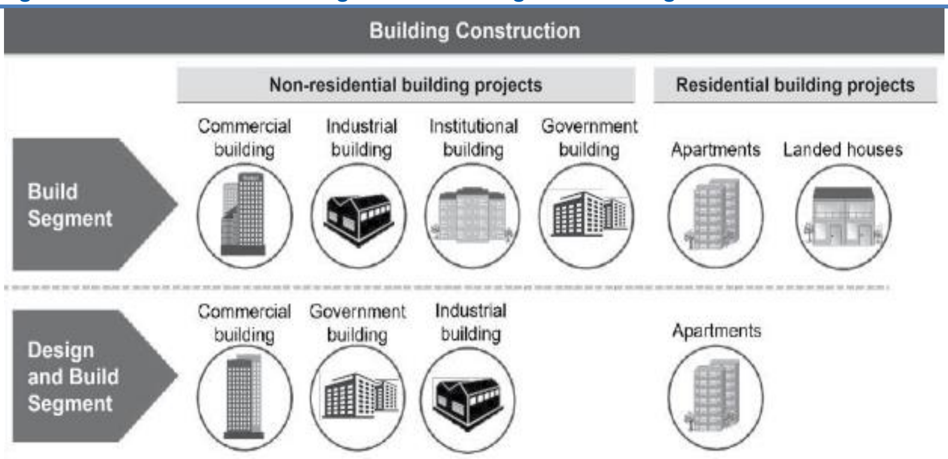
i. **Building construction – build (60.2% of FY21 revenue)**. As a contractor for building construction projects, Vestland is responsible for the overall project including project management and planning, appointment of subcontractors, procurement of labour and materials, and monitoring the stages of construction works to ensure completion of works up to project handover to the customer;

ii. **Building construction – design & build (38.4% of FY21 revenue).** As a design & build contractor, Vestland handles the overall project management as well as planning and coordinating the design aspects of the project, covering the technical specifications to meet the building compliance requirements, in addition to the coordination of the relevant submissions to the authorities. Under the design & build contracts, external architects and relevant professionals such as, amongst others, town planners, land and quantity surveyors, geotechnical consultants and engineers are appointed either by the customers or directly by Vestland, to work under the group's supervision. The design & build method is further facilitated by its cloud-based construction software, Speedbrick, which digitalises procurement processes to monitor material price trends and excessive material ordering. This also helps to reduce its reliance on manpower by freeing up 1,500 hours per month (Figure 12);

iii. **Civil engineering works (1.4% of FY21 revenue)**. Civil engineering works are mainly earthworks and rock hacking works which involve site clearance, excavation and backfilling, as well as levelling, earth compacting and slope stabilisation. These types of works usually command a lower margin as it involves lesser specialisation and lesser skilled works.

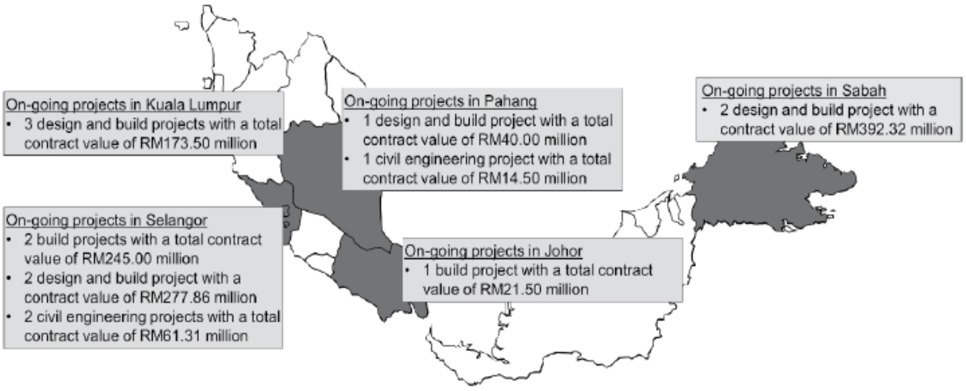
Geographically, Vestland has projects in East and West Malaysia across a few states. More than 50% of the group's orderbook comes from projects in Selangor, followed by Sabah – which contributes 31%. The remaining projects are from Kuala Lumpur, Pahang and Johor.

Figure 10: Vestland's build segment and design & build segment



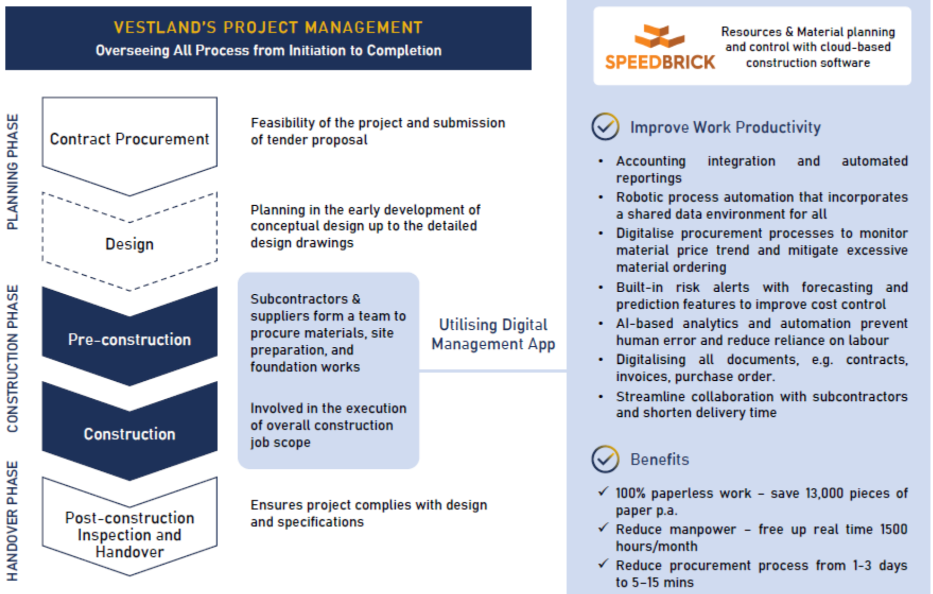
Source: Company

Figure 11: Vestland's geographical exposure in Malaysia



Source: Company

Figure 12: Vestland's project management flow for design & build projects



Source: Company

Supplier base. Vestland is not heavily dependent on any suppliers as the subcontracted services and materials are widely available and can be sourced from other suppliers. It also does not enter into any long-term agreements with its subcontractors and suppliers as its subcontractors' and suppliers' contracts are usually on a contract-to-contract basis which is based on the requirements of the relevant construction. This is evident through the purchases from Makin Juta only comprising 7.6% of the group's total purchases – despite the former having a 10-year business relationship with Vestland. Moreover, none of its top five suppliers of Vestland have a percentage of purchases that exceed 10%.

Figure 13: Vestland's major suppliers in FY21

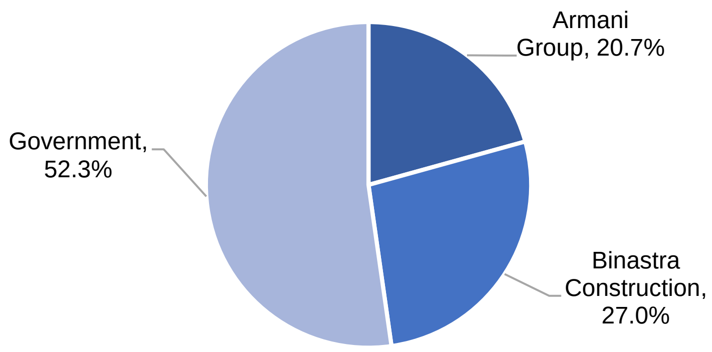
Supplier	Products Sourced	Percentage of total purchases (%)	Length of business relationship (years)
Fastcoll Corporation	Subcontracted air conditioning, mechanical ventilation and electrical services	7.8	2
Makin Juta	Manufacturing and trading of steel products and construction materials and transport services	7.6	10
Visibina	General trading, building cleaning and laundry services and general contractor	4.5	1
TA Furniture & Projects	Manufacture and marketing of furniture products	3.9	<1
Buildcon Concrete	Manufacture and sale of ready mixed concrete and related services	2.3	6

Source: Company data

Manageable business concentration risk. Based on its latest outstanding orderbook of MYR947.4m, 52.3% comes from the government-related jobs. Nevertheless, it is important to note that the government jobs were secured from various government-linked companies, namely Hawa Teknik for the Beluran Police Camp, Splendid Forte for Selangor Cyber Valley phase 1, and Perbadanan Perwira Harta Malaysia (ultimately held by Lembaga Tabung Angkatan Tentera) for the TUDM Army Camp Packages 2 and 3 and the Malaysia Armed Forces Package project. Henceforth, Vestland's outreach in the government job space is fairly spread across many types of developments facilities. As for private jobs, Binastra Construction and Armani Group account for 27% and 20.7% of Vestland's outstanding orderbook – with Armani Group representing three customers (by virtue of being a common shareholder) that include Mercu Majuniaga, SG Besi Construction, and Tafi industries.

As mentioned earlier, Vestland plans to focus on more social infrastructure jobs under the purview of the Ministry of Defence and the Ministry of Public Works such as public government offices, schools, hospitals, police and army facilities.

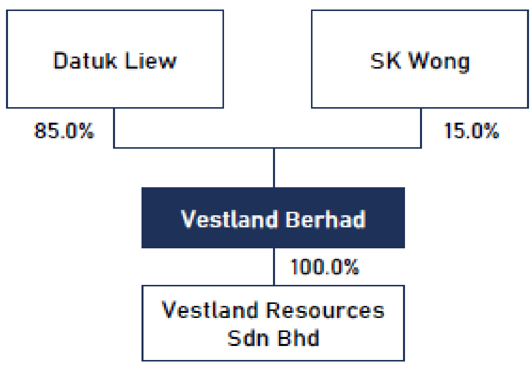
Figure 14: Vestland's outstanding orderbook breakdown based on customers



Source: Company data

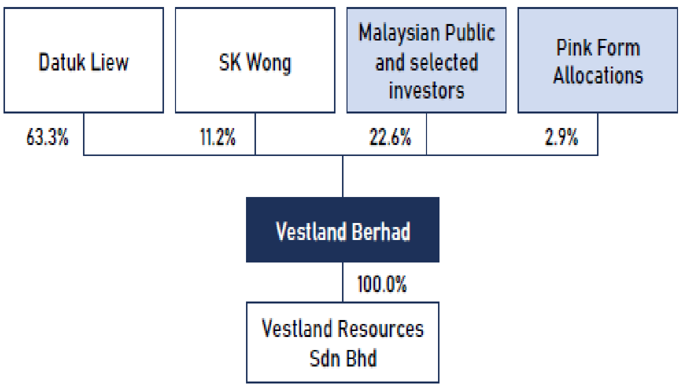
Management team. Vestland has an experienced management team headed by Group Managing Director Datuk Liew Foo Heen who has approximately 20 years of experience in the construction industry. He is supported by Wong Sai Kit, the group's executive director who brings with him approximately 22 years of experience in construction. Wong assists Liew in the overall management and operation of the group, as well as overseeing the overall operations of construction projects. They are supported by key senior management team members who come with relevant tertiary education qualifications and experience in their respective fields – these range ranging from finance matters, project tendering, project management and implementation to contract matters, procurement and human resource management.

Figure 15: Group structure pre-IPO



Source: Company data

Figure 16: Group structure post-IPO



Source: Company data

Key risks

i. Interruptions or delays caused by outbreak/spread of COVID-19 infections, sudden and unexpected equipment failures, fires and other environmental factors including natural disasters;

ii. Loss of key senior management personnel may have an unfavourable or material impact on the group's operations and future growth of the business. This may ultimately affect its financial performance, especially if Vestland is not able to replace or attract suitable talent in a timely manner;

iii. All of the group's construction site workers are contractual foreign workers, reflecting a high dependence on foreign workers. Therefore, any disruption or scarcity in supply of foreign workers due to changes in immigration policies by the Government or any other factors may adversely affect business operations;

iv. Risks arising from price fluctuations in construction materials such as steel, concrete and cement which constitute 30% of cost of sales;

v. Risk of cost overruns for its projects, as they are mainly based on a fixed contract value. For a fixed contract value, as we are unable to pass the increases in cost to its customers, any unanticipated cost increases during the project execution and construction period would adversely affect the group's financial performance;

vi. The group is dependent on the services and quality of its subcontractors to perform certain works for construction projects. Any failure by a subcontractor to fulfil its contractual obligations may lead to delays in completion of the project, thereby resulting in penalties being imposed on the group by customers. If the group is unable to claim such penalties from its subcontractors, this could impact its financial position.

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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