

Gamuda Bhd (July 2, RM2.74)

BUY: The revised offer by the Selangor government, although 3.4 times higher than the first offer, still fails to meet our expectations. There are still other visible catalysts for this stock, so we reiterate our “buy” call on the company. The revised offer values SPLASH’s water assets at a net equity value of RM1.58 billion, which corresponds to a value of RM632 million for Gamuda’s 40% stake. This falls short of our valuation of RM1.96 billion for all of SPLASH, or equivalent to RM782 million for Gamuda’s 40% stake. Our valuation is based on a discounted cash flow (DCF) method, using a conservative WACC (Weighted Average Cost Of Capital) of 11.7%.

For the deal to stand a chance of being accepted, we believe that any new offer has to be based on a DCF method using a WACC that at least approaches the single-digit level. This is due to its low earnings risks, which justifies a single digit WACC, in our view. We are still positive on Gamuda due to the good outlook for the domestic construction sector. The stock gives good value, being the cheapest at 14 times 2010 earnings against its comparable tier-one peers that are trading at between 15 to 17 times 2010 earnings. — *KAF Research (June 29)*