

SMRT Corp (MRT SP)

Transport - Transportation

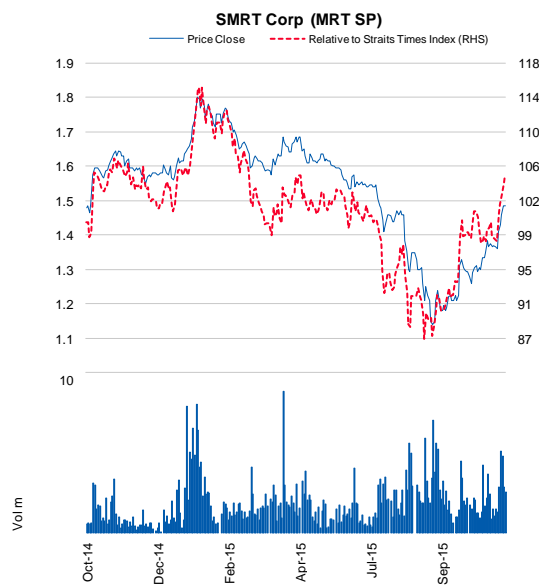
Market Cap: USD1,625m

Sell (Maintained)

 Target Price: **SGD1.10**

 Price: **SGD1.49**

Trading At Stretched Valuations

 Macro ◆◆◆
 Risks ◆◆
 Growth ◆
 Value ◆


Source: Bloomberg

Avg Turnover (SGD/USD)	3.30m/2.36m
Cons. Upside (%)	-7.4
Upside (%)	-25.9
52-wk Price low/high (SGD)	1.14 - 1.80
Free float (%)	45
Share outstanding (m)	1,524
Shareholders (%)	
Temasek Holdings	54.2
Allianz SE	1.5
JPMorgan	0.9

Share Performance (%)

	YTD	1m	3m	6m	12m
Absolute	(6.0)	16.0	1.7	(11.1)	(0.7)
Relative	3.3	8.2	9.6	2.1	4.7

1HFY16 profit of SGD46m (-4% YoY) was in line with our estimates. Rail business continues to report losses amidst elevated maintenance cost, while bus operation continues to benefit from low diesel cost. We raise FY17F profit by 3% to account for improved bus operating margin. Keep SELL with a revised SGD1.10 TP (from SGD1.05, 26% downside) amidst a dismal FY16F profit growth, lofty valuations and the low possibility of rail financing framework reforms anytime soon.

- ◆ **Non-fare businesses are the saviour.** SMRT's 1HFY16 (Mar) fare business revenue (72% of total revenue) grew 5% YoY to SGD476.1m, aided by higher ridership for rail and bus businesses. However, the overall fare business reported an operating loss of SGD5.3m as elevated costs related to rail business pushed margins into negative territory. SMRT still managed to report an overall operating profit of SGD60.2m (-4% YoY), thanks to strong profit growth from non fare businesses, like taxi (+32% YoY), rental (+7% YoY) and advertising (+14% YoY).
- ◆ **Outlook for fare business is weak.** SMRT guided that maintenance expenses related to rail business will remain elevated next year. The company disclosed that maintenance expenses related to rail business, which accounted for 41% of its rail revenue, is expected to reach 50% in next year. At the same time, the finalised 1.9% reduction in bus and rail fares could impact revenue growth for SMRT's bus and rail businesses. While we expect its bus business to remain profitable amidst low fuel costs, it may not offset the weak rail operations.
- ◆ **Rail financing reforms may not happen soon.** SMRT continues to discuss with the authorities on the transition to a new rail financing framework. While we believe these reforms will have to be implemented eventually, we do not expect them to be implemented until the regulators complete the ongoing bus reforms by Sep 2016.
- ◆ **Valuations are stretched.** SMRT is trading at 22.2x FY17 P/E with a PEG of 1.6x. Our DCF-based SGD1.10 TP, based on a WACC of 7.4% and LT growth of 1%, assumes no implementation of rail reforms. Our TP implies 18.3x FY16 P/E, which is in line with its P/E during FY10-11 when SMRT delivered a 0-1.2% EPS growth.

Forecasts and Valuations	Mar-13	Mar-14	Mar-15	Mar-16F	Mar-17F
Total turnover (SGDm)	1,119	1,164	1,236	1,289	1,349
Reported net profit (SGDm)	83	61	90	89	102
Recurring net profit (SGDm)	83	61	90	89	102
Recurring net profit growth (%)	(30.6)	(26.1)	47.1	(1.1)	14.0
Recurring EPS (SGD)	0.05	0.04	0.06	0.06	0.07
DPS (SGD)	0.03	0.02	0.03	0.03	0.03
Recurring P/E (x)	27.1	36.8	25.0	25.3	22.2
P/B (x)	2.94	2.82	2.63	2.50	2.35
P/CF (x)	8.67	9.65	7.94	7.65	7.05
Dividend Yield (%)	1.7	1.3	1.8	2.0	2.2
EV/EBITDA (x)	7.96	9.90	8.71	8.89	8.42
Return on average equity (%)	10.7	7.8	10.9	10.1	10.9
Net debt to equity (%)	8.2	59.4	78.6	84.0	87.1
Our vs consensus EPS (adjusted) (%)				(0.4)	1.5

Source: Company data, RHB

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Figure 1: SMRT's 2QFY16 results review (FYE Mar - SGDm)

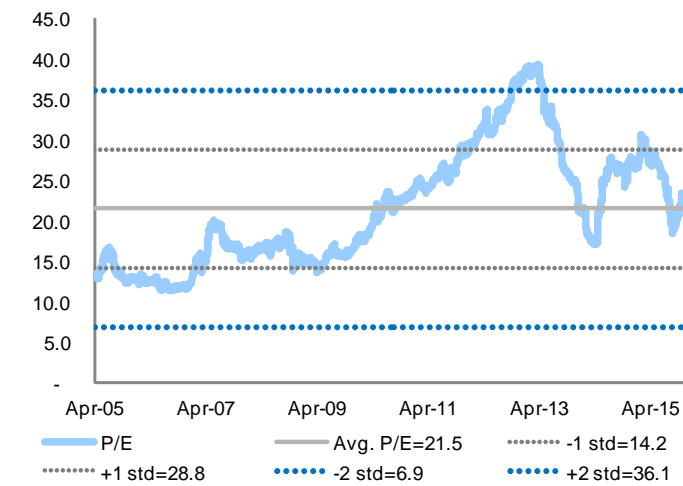
Income statement	2QFY14	3QFY14	4QFY14	1QFY15	2QFY15	3QFY15	4QFY15	1QFY16	2QFY16	YoY %Chg	QoQ %Chg	1HFY15	1HFY16	YoY %Chg
Train	160.5	156.3	153.5	157.9	165.2	161.8	159.3	167.6	169.6	3%	1%	323.1	337.2	4%
LRT	2.7	2.5	2.5	2.5	2.5	2.4	2.4	2.6	2.7	8%	2%	4.9	5.3	7%
Bus	55.2	57.3	51.7	58.1	60.7	59.1	60.3	61.4	63.2	4%	3%	118.8	124.6	5%
Fare based revenue	218.4	216.1	207.7	218.4	228.4	223.2	222.0	231.6	235.5	3%	2%	446.9	467.1	5%
Taxi	32.4	32.9	34.3	34.4	35.1	36.6	36.8	37.8	37.6	7%	-1%	69.5	75.4	8%
Rental	24.2	24.8	25.1	25.8	30.1	32.3	32.1	32.9	33.3	11%	1%	56.0	66.2	18%
Advertising	8.6	10.8	8.1	9.4	9.4	9.9	7.5	8.8	11.0	17%	25%	18.7	19.8	6%
Engineering	6.6	8.6	27.3	2.8	3.7	3.7	5.1	2.4	3.5	-4%	48%	6.5	5.9	-9%
Other services	6.1	-	(12.8)	6.3	7.3	7.5	7.6	6.8	7.8	7%	14%	13.6	14.7	8%
Non fare based revenue	77.9	77.2	81.9	78.7	85.5	90.0	89.2	88.7	93.2	9%	5%	164.3	182.0	11%
Total revenue	296.3	293.3	289.5	297.1	314.0	313.2	311.2	320.3	328.8	5%	3%	611.1	649.1	6%
Staff costs	(118.5)	(119.6)	(111.5)	(119.0)	(123.0)	(120.3)	(121.2)	(128.9)	(131.3)	7%	2%	(242.0)	(260.2)	8%
Depreciation of PP&E	(45.3)	(45.8)	(47.8)	(47.4)	(49.4)	(52.3)	(54.1)	(53.5)	(53.6)	9%	0%	(96.7)	(107.2)	11%
Amortisation of asset-related grants	2.5	2.5	2.4	2.4	2.5	2.4	2.7	2.5	2.5	1%	2%	4.9	4.9	1%
Repairs and maintenance costs	(29.8)	(27.4)	(29.3)	(28.2)	(29.9)	(29.3)	(34.4)	(33.8)	(31.2)	4%	-8%	(58.2)	(65.0)	12%
Electricity and diesel costs	(43.7)	(38.8)	(38.1)	(39.8)	(40.0)	(36.0)	(34.9)	(34.6)	(36.0)	-10%	4%	(79.7)	(70.6)	-11%
Impairment costs	-	-	-	-	-	-	-	-	-	na	na	-	-	na
Other operating expense	(51.0)	(54.8)	(55.8)	(48.6)	(53.1)	(60.4)	(61.4)	(60.5)	(64.0)	20%	6%	(101.7)	(124.5)	22%
Total operating costs	(285.8)	(283.8)	(280.1)	(280.6)	(292.9)	(295.9)	(303.3)	(308.9)	(313.6)	7%	2%	(573.5)	(622.5)	9%
Other operating income	9.5	10.6	12.4	12.8	12.2	13.7	19.3	16.3	17.4	42%	7%	25.0	33.6	35%
Operating income	20.0	20.1	21.9	29.3	33.3	31.0	27.1	27.7	32.5	-2%	17%	62.6	60.2	-4%
Finance costs	(2.6)	(2.6)	(2.6)	(2.8)	(3.4)	(3.2)	(3.1)	(3.1)	(3.2)	-8%	1%	(6.2)	(6.3)	1%
Interest and investment income	0.4	0.4	(0.1)	0.5	0.3	0.5	0.3	0.4	0.2	-21%	-43%	0.8	0.7	-21%
Share of results of an associate	(0.4)	(0.2)	0.3	0.1	0.0	(0.2)	1.0	0.7	1.4	8488%	88%	0.1	2.1	1383%
Profit before tax	17.4	17.6	19.6	27.2	30.2	28.1	25.4	25.7	31.0	3%	20%	57.4	56.7	-1%
Income tax	(3.1)	(3.5)	(2.8)	(4.9)	(5.4)	(5.6)	(4.6)	(5.5)	(5.2)	-3%	-6%	(10.2)	(10.7)	5%
Profit after tax	14.3	14.1	16.7	22.3	24.8	22.6	20.8	20.2	25.8	4%	28%	47.1	45.9	-2%
Minority Interest	0.1	0.1	0.2	0.1	0.4	(0.0)	0.0	(0.0)	(0.0)	na	na	0.5	(0.1)	na
Profit for equity holders	14.4	14.3	16.9	22.4	25.3	22.5	20.8	20.1	25.7	2%	28%	47.6	45.9	-4%
Margins														
Operating margin (%)	6.8%	6.9%	7.6%	9.9%	10.6%	9.9%	8.7%	8.6%	9.9%			10.2%	9.3%	
Net margin (%)	4.9%	4.9%	5.8%	7.5%	8.0%	7.2%	6.7%	6.3%	7.8%			7.8%	7.1%	

Source: Company data, RHB

Valuation basis

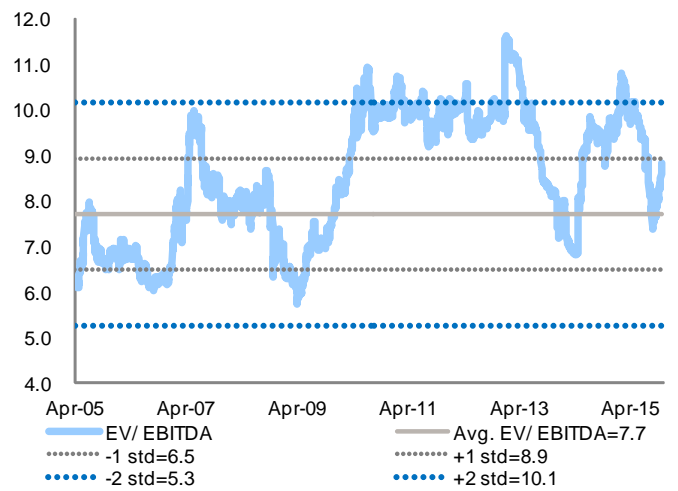
We use a DCF-based valuation to arrive at our SGD1.10 TP. Our WACC of 7.4% is based on a risk-free rate of 2.6% and a risk premium of 8%. We assume long-term growth at 1%. SMRT's weak FY16F earnings, potential headwinds from higher-than-estimated costs and lower revenue growth for fare businesses amidst a 1.9% fare reduction would likely continue to weigh down its share price. While the implementation of reforms in the rail financing framework will be positive for SMRT in the long term, we see limited possibility of the reforms being implemented over the next one year. Hence, we do not factor in any positive contribution from the reforms when deriving our DCF-based TP.

Figure 2: SMRT - 1-year forward P/E



Source: Bloomberg, Company, RHB

Figure 3: SMRT - 1-year forward EV/EBITDA



Source: Bloomberg, Company, RHB

Risks to our rating

Key risks to our rating are: i) a change in the competitive landscape of Singapore's land transport sector due to regulatory liberalisation (eg introduction of new rail operators for new rail lines), ii) lower-than-estimated margins for its bus business, which we believe could partially offset a weak rail business, and iii) higher-than-expected capex or fines.

Financial Exhibits

Profit & Loss (SGDm)	Mar-13	Mar-14	Mar-15	Mar-16F	Mar-17F
Total turnover	1,119	1,164	1,236	1,289	1,349
Gross profit	1,119	1,164	1,236	1,289	1,349
Other operating costs	(1,009)	(1,080)	(1,115)	(1,170)	(1,215)
Operating profit	110	84	121	119	134
Operating EBITDA	261	256	314	318	345
Depreciation of fixed assets	(151)	(171)	(193)	(199)	(211)
Operating EBIT	110	84	121	119	134
Net income from investments	2	1	3	4	5
Interest expense	(7)	(10)	(13)	(15)	(16)
Pre-tax profit	105	75	111	108	123
Taxation	(22)	(13)	(20)	(18)	(21)
Profit after tax & minorities	83	61	90	89	102
Reported net profit	83	61	90	89	102
Recurring net profit	83	61	90	89	102

Source: Company data, RHB

Cash flow (SGDm)	Mar-13	Mar-14	Mar-15	Mar-16F	Mar-17F
Operating profit	110	84	121	119	134
Depreciation & amortisation	151	171	193	199	211
Change in working capital	(19)	(13)	(10)	9	10
Other operating cash flow	37	6	2	2	2
Operating cash flow	279	249	306	329	358
Interest paid	(4)	(10)	(12)	(15)	(16)
Tax paid	(15)	(5)	(9)	(18)	(21)
Cash flow from operations	260	234	285	296	321
Capex	(251)	(652)	(463)	(350)	(350)
Other investing cash flow	(12)	9	8	2	3
Cash flow from investing activities	(262)	(643)	(454)	(348)	(347)
Dividends paid	(109)	(30)	(41)	(43)	(47)
Increase in debt	450	-	189	150	-
Other financing cash flow	13	48	31	-	-
Cash flow from financing activities	353	17	178	107	(47)
Cash at beginning of period	195	546	156	147	211
Total cash generated	351	(391)	9	55	(73)
Forex effects	(0)	0	1	-	-
Implied cash at end of period	546	156	165	202	137

Source: Company data, RHB

Financial Exhibits

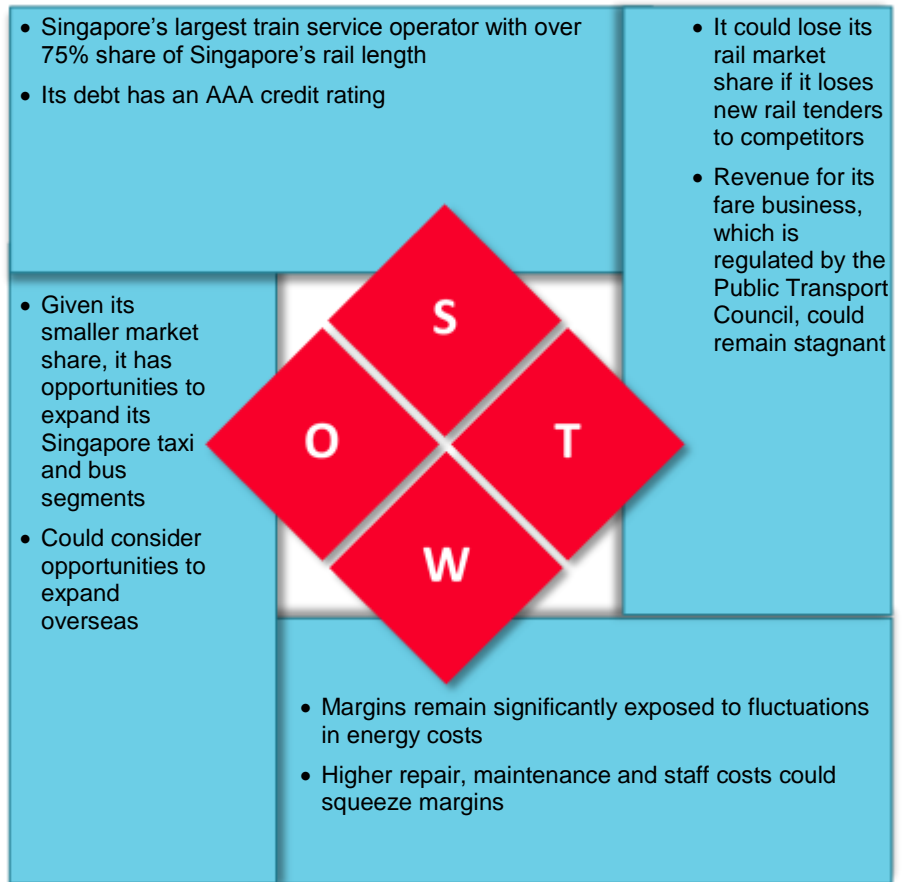
Balance Sheet (SGDm)	Mar-13	Mar-14	Mar-15	Mar-16F	Mar-17F
Total cash and equivalents	546	161	147	211	135
Inventories	60	84	81	84	88
Accounts receivable	86	99	168	175	183
Other current assets	-	-	9	9	9
Total current assets	692	344	405	479	416
Total investments	83	73	76	78	80
Tangible fixed assets	1,436	1,642	2,042	2,183	2,311
Intangible assets	14	14	14	14	14
Total non-current assets	1,532	1,729	2,132	2,275	2,405
Total assets	2,224	2,073	2,537	2,755	2,822
Short-term debt	2	156	9	9	9
Accounts payable	577	355	568	588	610
Other current liabilities	54	54	63	63	63
Total current liabilities	633	566	640	659	682
Total long-term debt	607	480	813	963	963
Other liabilities	216	225	226	227	216
Total non-current liabilities	823	705	1,038	1,189	1,179
Total liabilities	1,456	1,271	1,678	1,849	1,861
Share capital	167	168	169	169	169
Retained earnings reserve	600	631	681	728	783
Other reserves	1	2	9	9	9
Shareholders' equity	768	802	860	906	961
Minority interests	0	(0)	(1)	(1)	(1)
Other equity	0	0	(0)	(0)	(0)
Total equity	769	802	859	906	960
Total liabilities & equity	2,224	2,073	2,537	2,755	2,822

Source: Company data, RHB

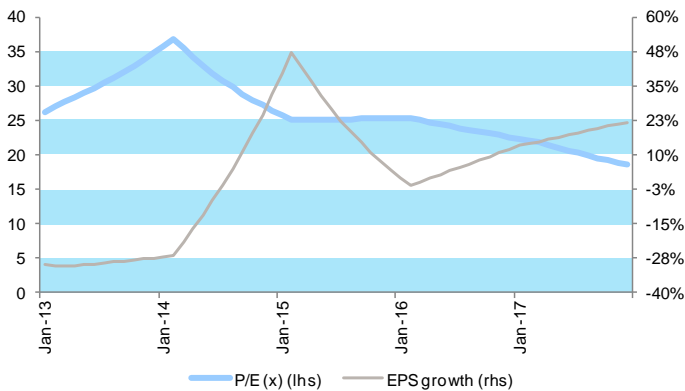
Key Ratios (SGD)	Mar-13	Mar-14	Mar-15	Mar-16F	Mar-17F
Revenue growth (%)	5.9	4.0	6.2	4.3	4.6
Operating profit growth (%)	(25.9)	(23.6)	43.4	(1.7)	12.8
Net profit growth (%)	(30.6)	(26.1)	47.1	(1.1)	14.0
EPS growth (%)	(30.6)	(26.3)	47.1	(1.1)	14.0
BVPS growth (%)	(2.9)	4.1	7.2	5.4	6.0
Operating margin (%)	9.8	7.2	9.8	9.2	9.9
Net profit margin (%)	7.4	5.3	7.3	6.9	7.6
Return on average assets (%)	4.2	2.9	3.9	3.4	3.7
Return on average equity (%)	10.7	7.8	10.9	10.1	10.9
Net debt to equity (%)	8.2	59.4	78.6	84.0	87.1
DPS	0.03	0.02	0.03	0.03	0.03
Recurrent cash flow per share	0.17	0.15	0.19	0.19	0.21

Source: Company data, RHB

SWOT Analysis

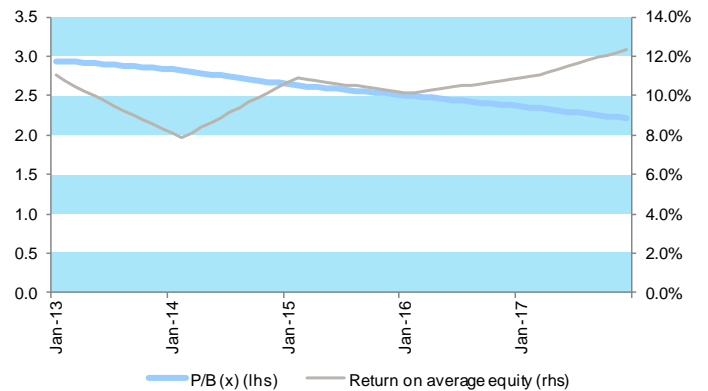


P/E (x) vs EPS growth



Source: Company data, RHB

P/BV (x) vs ROAE



Source: Company data, RHB

Company Profile

SMRT Corporation Limited (SMRT) operates Singapore's largest Mass Rapid Transit (MRT) and Light Rail Transit (LRT) systems. The company also provides bus, taxi, charter hire services, and consultancy and project management services. SMRT rents taxis and leases commercial space, kiosks and advertising panels at the MRT and LRT stations as well as in trains, buses and taxis.

Recommendation Chart



Source: RHB, Bloomberg

Date	Recommendation	Target Price	Price
2015-08-23	Sell	1.05	1.21
2015-05-04	Neutral	1.72	1.65
2015-01-30	Neutral	1.80	1.75
2014-11-03	Neutral	1.50	1.58
2014-07-31	Sell	1.24	1.58
2014-05-02	Sell	1.00	1.25
2014-01-29	Sell	1.04	1.17
2013-10-25	Sell	1.11	1.29
2013-07-31	Sell	1.25	1.42
2013-05-02	Sell	1.25	1.42

Source : RHB, Bloomberg

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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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