

Keong Hong Holdings Limited

Strategic Alliances & New Markets

*Keong Hong Holdings Limited (Keong Hong) announced on 20 Aug a S\$5m investment in structural steel works and tunnelling specialist Kori Holdings Limited (Kori). We see this transaction as a start towards the formation of a strategic alliance between both companies, to extract synergies such as the pooling of expertise to bid for more complex projects. For Keong Hong, this move may be a route to enter into public transportation infrastructure projects. **Maintain Increase Exposure.***

Terms of Investment: Keong Hong will be subscribing a S\$5m 5.0% pa three-year bond, convertible at any time before maturity, into 10.71% of the enlarged share capital of Kori at S\$0.42 per share. Kori traded at S\$0.46 on 20 Aug. Kori intends to use the funds to acquire similar businesses as part of its expansion plan.

About Kori: Kori is a SGX listed company with a market capitalization of S\$45.6m as of 20 Aug. It has previously participated in various MRT projects as a subcontractor providing tunnelling and strutting works and is tendering for project(s) related to the Thomson MRT Line. For 1H FY13 ended Jun 2013, Kori reported PATMI of S\$3.55m on revenue of S\$35.1m.

Extracting Synergies: The announcements made by both companies mentioned about the possibility of realization any potential synergies that can arise from two complementary businesses. Keong Hong has historically been a builder of various properties, including residential, commercial, industrial and institutional projects, and has more recently started taking partial stakes in property development projects. Kori, on the other hand, is in the civil and structural engineering business.

Our View: While it is still too early for us to know exactly how closely both companies will be working together, we are favourable of moves to tap onto new expertise and thus facilitate entry into new project types to form new growth drivers. In turn, concentration risk on the property sector can be reduced. We updated our forecasts to factor in this investment, but kept our valuation of Keong Hong unchanged pending further developments.

Increase Exposure

- Intrinsic Value S\$0.715
- Prev Closing S\$0.580

Main Activities

Keong Hong Holdings Limited is a provider of a broad range of building construction services to both private and public sectors for residential, commercial, industrial and institutional projects. The company's track record includes projects in Singapore and the Maldives, as well as a property development in Singapore. .

Financial Highlights

(Y/E Sep) S\$m	FY11	FY12	FY13F
Revenue	189.5	167.4	200.8
Gross Profit	13.8	29.4	30.1
EBIT	12.2	23.9	23.8
PATMI	9.4	19.8	19.9
EPS (S cts)	5.9	12.4	12.8

Source: Voyage Research Estimates

Key ratios (FY13F)

PER	4.5
P/BV	1.4
ROE	34.9%
Debt/Equity	0.0%
Current ratio	1.7

Source: Voyage Research Estimates

Indexed Price Chart

Green (FSSTI)
White (Keong Hong)



Source: Bloomberg

52wks High-Low	59.0 cents/ 34.54 cents
Number of Shares	156 m
Market Capitalization	S\$90.5m

Analyst:

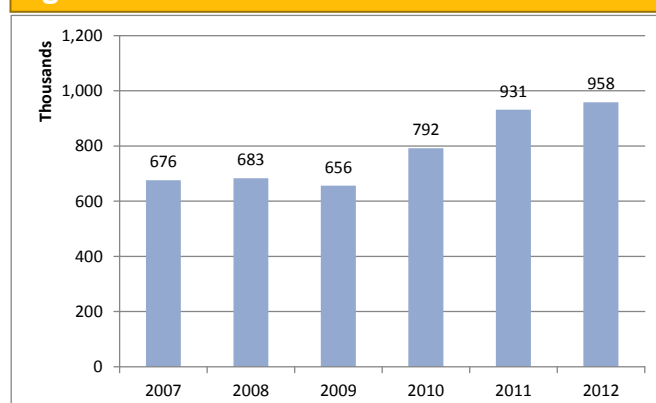
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New Project in the Maldives: Prior to the announcement of the convertible bond, Keong Hong had on 1 Aug announced that it had entered into agreements with the Maldives government to develop a tourist hotel and resort, as well as expand and develop the Kooddoo airport, in the Gaafu Alifu Atoll, Maldives, with the intention to sublease or sell the rights to operate the facilities to third parties upon their completion.

The lease rental works out to about US\$1.25m per annum over 50 years for the hotel and resort and US\$24k per annum over 25 years for the airport. The airport will take 18 months to be built, while the hotel and resort will be built over five years.

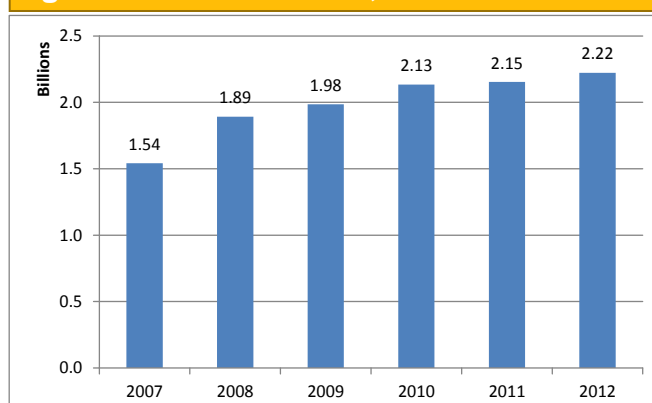
Keong Hong had previously constructed a resort development at the same atoll in the Maldives. The project was secured in 2009 and completed in 2012 at an approximate contract value of S\$83.6m. The size of this latest project is undisclosed. However, Keong Hong may fund this project with co-investors, instead of relying totally on its own resources.

Figure 1: Maldives Tourist Arrivals



Source: <http://www.tourism.gov.mv/>

Figure 2: Maldives GDP, current US\$



Source: <http://databank.worldbank.org/>

Our View: We are of the view that it is premature to factor this project into our forecasts and valuation model as its potential value is conditional upon factors such as the ultimate project ownership structure and the quality of co-investors. However, the quantum of this project will most likely be substantial.

On the whole, these two developments i.e. investment in Kori and new project in the Maldives are evidence that Keong Hong has been actively developing new growth platforms, besides expanding into property development in Singapore. These three business areas are also consistent with our expectations of the company's future plans when we initiated coverage on Keong Hong in Jan 2013. We look forward to further developments to provide the basis for us to make further adjustments to our forecasts and valuation.

Figure 3: Economic Profit Valuation

S\$ m	FY13F	FY14F	FY15F
Revenue	200.8	220.9	232.0
EBIT	23.8	26.7	18.9
Tax on EBIT	-4.0	-4.5	-3.2
NOPLAT	19.7	22.1	15.7
Invested Capital	116.5	129.6	145.2
% of Debt	56.1%	49.8%	44.4%
% of Equity	43.9%	50.2%	55.6%
WACC (%)	8.0%	8.3%	8.5%
Capital Charge	9.4	10.7	12.3
Economic Profit	10.4	11.4	3.4
Terminal Value			53.5
Discount Factor	0.9	0.9	0.8
Present Value	9.6	9.7	2.7
Book Value	50.0	Risk Free Rate	2.5%
Explicit Value	22.0	Beta	1.0
Terminal Value	41.9	Market RP	7.7%
Value of Equity	114.0	Cost of Equity	10.200%
Number of Shares (m)	160.0	Cost of Debt	5.4%
Value per share (S\$)	0.715	LT Growth	2.0%

Source: Voyage Research

Figure 4: Financial Forecast and Estimate

	FY10	FY11	FY12	FY13F	FY14F	FY15F
Revenue	124.8	189.5	167.4	200.8	220.9	232.0
Gross Profit	10.1	13.8	29.4	30.1	33.1	25.5
EBIT	9.7	12.2	23.9	23.8	26.7	37.4
PATMI	8.2	9.4	19.8	19.9	22.3	31.2
Total Current Assets	83.9	110.9	121.0	130.9	150.9	181.1
Total Non-Current Assets	10.8	5.0	4.9	11.0	11.8	7.5
Total Current Liabilities	76.0	83.6	74.3	76.9	82.2	86.1
Total Non-Current Liabilities	2.9	0.9	0.4	0.1	0.1	0.1
Total Equity	15.8	31.4	51.2	64.9	80.5	102.4
Cash from Operating Activities	16.8	10.4	20.5	17.1	22.2	35.8
Cash from Investing Activities	2.8	7.1	-2.5	-7.0	-2.0	-2.0
Cash from Financing Activities	-7.1	-2.9	8.5	-6.8	-6.7	-9.4
Receivable Days	118	120	145	120	120	120
Payable Days	137	124	134	90	90	90
Return on Common Equity	53.1%	41.6%	49.8%	34.9%	31.1%	34.5%
Return on Assets	10.9%	10.4%	15.8%	14.7%	14.6%	17.8%
Gross Debt / Common Equity	23.4%	5.6%	1.7%	0.0%	0.0%	0.0%
Current Ratio	1.1	1.3	1.6	1.7	1.8	2.1
EPS (S cents)	5.1	5.9	12.4	12.8	14.3	20.0
BV/Share (S cents)	9.7	18.4	31.3	41.0	51.0	65.0
P/E	11.4	9.8	4.7	4.5	4.1	2.9
P/BV	6.0	3.2	1.9	1.4	1.1	0.9

Source: Voyage Research

Rating Definition:

Increase Exposure – The current price of the stock is significantly lower than the underlying fundamental value. Readers can consider increasing their exposure in their portfolio to a higher level.

Invest – The current price of the stock is sufficiently lower than the underlying fundamental value of the firm. Readers can consider adding this stock to their portfolio.

Fairly Valued – The current price of the stock is reflective of the underlying fundamental value of the firm. Readers may not need to take actions at current price.

Take Profit – The current price of the stock is sufficiently higher than the underlying fundamental value of the firm. Readers can consider rebalancing their portfolio to take advantage of the profits.

Reduce Exposure – The current price of the stock is significantly higher than the underlying fundamental value of the firm. Readers can consider reducing their holdings in their portfolio.

IMPORTANT DISCLOSURE:

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