SIAS RESEARCH

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Initiation Report

Keong Hong Holdings Limited

Well Managed Business with Growth Potential

Keong Hong Holdings Limited (KH) is a construction service provider in Singapore. We like this company for its forward revenue visibility, healthy balance sheet and its range of growth options. KH intends to grow by pursuing complex projects of higher value, taking on overseas projects and investing in property development projects. The variety of growth avenues gives KH the potential to deliver long term growth – beyond that of its existing order book. ***Initiate Coverage with an Increase Exposure rating.***

Key Highlights:

Positive Revenue Prospects: KH is currently executing four construction projects with a combined value of some S$456m of revenue to be recognized from FY2013 to FY2015. We further expect KH to continue garnering new projects, which will benefit FY2014 revenue. KH recognized S$167.4m of revenue in FY2012. Its order book suggests that the company should deliver revenue growth in FY2013.

Twin Waterfalls 99% Sold: KH's sole property development project is almost fully sold with only 2 units left. This project is a JV between KH and Fraser Centrepoint Limited. Twin Waterfalls is expected to net the company about S$18.5m in either FY2014 or FY2015. KH is riding on its success in Twin Waterfalls to partner with another company for its second property development investment.

Healthy Balance Sheet: Moreover, KH maintains a healthy balance sheet with a cash balance of S$56.1m as of end FY2012. Debt is held at the associate level for the development of Twin Waterfalls, which is already close to fully sold, thus paving the way for KH to invest in its next project at Sembawang. The construction business itself is cash flow positive and free of debt. According to the management, they have over the years developed relationships with repeat customers who repay timely. On the whole, KH comes across as a well-managed business with potential for positive growth.

Increase Exposure

- Intrinsic Value S$0.715
- Prev Close S$0.540

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	12.4

Source: Company, SIAS Research

Key ratios (FY13F)	
PER	4.3
P/BV	1.4
Return on Common Equity	34.9%
Return on Assets	14.7%
Gross Debt to Common Equity	0%

Source: SIAS Research

Indexed Price Chart

Green (FSSTI)
White (Keong Hong)

Source: Bloomberg

52wks High-Low	*S$0.540 /S$0.280*
Number of Shares	*160.0m*
Market Capitalization	*S$86.4m*

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Company Background

Keong Hong Holdings Limited (KH) is a homegrown construction company established in 1983 and listed on the SGX Catalist Board in December 2011.

- Its principal activities can best be described as the provision of building construction services to both the private and public sectors in residential, commercial, industrial and institutional projects. Other than plain vanilla conventional construction contracts, KH also takes on additional and alteration works, as well as design-and-build projects.

- KH's customers comprise of main contractors, project consultants and property developers and owners. Repeat customers include Keppel Land Group, Frasers Centrepoint Limited and MCL Land Ltd.

- KH has a BCA grading of A1 for general building projects. This means that KH can tender for public sector construction projects of unlimited value, under the general building workhead, with no restrictions for private sector projects.

Figure 1: Some of Recently Completed Projects

The Parvis: 248-unit condominium at Holland Hill
Joint development by MCL Land and Ho Bee
TOP in Aug 2012
Contract Value: S$142.9m

8@Woodleigh: 330-unit condominium at Woodleigh Close
Developed by Fraser Centrepoint Limited
TOP in Jul 2012
Contract Value: S$73.9m

The Residence Maldives: 94-villa resort hotel in the Maldives
Developed by Bonvest Group
Opened in Sep 2012 (Completed Jun 2012)
Contract Value: S$83.6m

Source: Company Presentation Slides

Figure 2: Wide Spectrum of Completed Projects – Across Different Types of Projects (e.g. Design & Build, Additional & Alteration) and Segments (e.g. Residential & Commercial)

Description	Contract Value (S$m)	Completion Date	Project Type
Design & Build Projects			
8@Woodleigh	73.9	Aug-12	Residential
Martin Places Residences	125.7	Sep-11	Residential
IBIS Hotel Project	46.3	Jan-09	Commercial
The Esta	74.3	Nov-08	Residential
The Belvedere	43.4	Oct-07	Residential
The Linc	13.7	Jan-06	Residential
Overseas Projects			
Kooddoo Airport	7.7	Sep-12	Institutional
The Residence Resort	83.6	Jun-12	Commercial
Condominium Projects			
The Parvis	142.9	Sep-12	Residential
Sunville	11.7	Apr-05	
Butterworth 8	44.9	Apr-04	
The Edgewater	11.7	Nov-03	
Palm Gardens	147.9	May-00	
Parc Vista	120.6	May-98	
Commercial / Industrial Projects			
Sime Darby Performance Centre Main building works for 6-storey motor vehicle service centre & ancillary motor vehicle showroom, offices and storage	38	Aug-08	Commercial
Vicplas - 8 storey factory building with a basement carpark	12.5	Dec-01	Industrial
Artform - 2 storey factory building with mezzanine floor and 1st storey ancillary office at Senoko Way	6.6	Jul-01	Industrial
Institutional / HDB Projects			
Mount Alvernia Hospital Sisters' Accommodation Sisters' Accommodation as an extension to the existing Mount Alvernia Hospital	6.1	Dec-05	Institutional
Pasir Laba Army Camp - Camp Redevelopment (Phase 3)	17.8	Apr-02	Institutional
SengKang N3 C17 - Building and electrical works at Sengkang neighbourhood North Zone 3	28.3	Jun-01	HDB
Additional & Alteration Projects			
6-storey extension and A&A works to SIM	100	Sep-11	Institutional
A&A works to 4th storey and B3 to B1 of Tampines Mall Shopping Centre	6.9	Sep-04	Commercial
Fitting out works at Fuji Xerox	2.7	Aug-04	Commercial
A&A works to existing factory comprising of a 3 storey technical and training centre with ancillary office	5.4	Oct-02	Industrial
Avaplas - Extension of factory and A&A Works	2.4	Jul-01	Industrial
Terrace Housing			
Springside (Phases 6A, 7A & 7B)	24.6	Dec-03	Residential
Summerlea Green	20.1	Jun-98	
Springside (Phase 1 to 5)	47.6	Nov-97	

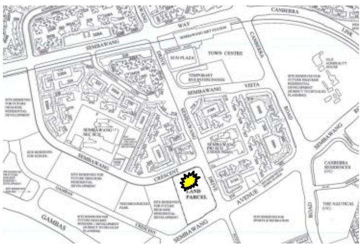
Source: Company Data

Figure 3: On-Going Projects

Paterson 2: 89-unit condominium at Paterson Road
Developed by Bukit Sembawang View
Target Completion: February 2014
Contract Value: S$70.5m
Construction Progress: Superstructure completed up to 5th floor as per 2012 annual report, with architectural and mechanical and electrical services installation progressing at basement 1 and 2.

Terrasse: 414-unit condominium at Serangoon
Developed by MCL Land
Target Completion: May 2014
Contract Value: S$110.5m
Construction Progress: 65% of the basement cast has been completed and the advanced block superstructures have reached the attic roof level, as per 2012 annual report.

Twin Waterfalls: 728-unit EC at Punggol
Jointly developed by Frasers Centrepoint Limited and KH
Target Completion: Dec 2014
Contract Value: S$162.5m
Construction Progress: Piling works have been completed and four tower blocks have already progressed to superstructure levels, ranging from the second to fourth storey, as per 2012 annual report.



LATEST PROJECT
Executive Condominium at Sembawang Crescent / Sembawang Drive
Jointly Developed by JBE Holdings Pte Ltd and KH
Launch Date: 2H 2013
Target Completion: 2015
Contract Value: S$149.9m
Construction Progress: To commence construction 4Q CY2013 (1Q FY2014)

Source: Company Presentation Slides, Announcements and www.hdb.gov.sg

Positive Revenue Prospects

On-Going Projects Provide Revenue Visibility: KH has four construction projects at the moment. They are Paterson 2, Terrasse, Twin Waterfalls and an executive condominium development in Sembawang. These four projects have a combined contract value of about S$470m to be recognized in FY2013, FY2014, FY2015 and early FY2016 (or S$152m per year). In comparison, KH recognized revenue of S$167.4m in FY2012. Therefore, KH's existing projects form a strong foundation for the company to drive growth via new contract wins over the next two to three years.

S$21m of work done at Paterson 2 and Terrasse have already been recognized as FY2012 revenue, leaving about S$160m of contract value from these two contracts to be recognized over FY2013 and FY2014. The construction of Twin Waterfalls seemed to be at the early stage at the end of FY2012 and we assume that the full S$162.5m will be recognized over FY2013 to FY2015.

We assume that the latest executive condominium project at Sembawang will be completed by end 2015, stretching to 1Q FY2016. We assume that about 90% of the contract value of S$149.9m will be recognized in FY2014 and FY2015. FY2016 is beyond our forecast horizon and we will add FY2016 forecasts at a later date.

In all, our forecasts assume a further S$51.7m and S$146.2m of revenue contribution for FY2014 and FY2015 from new projects in the future. As Paterson 2 and Terrasse (worth S$160.0m in total) will be completed in FY2014, KH need only replace these projects with contracts worth S$197.9m to meet our forecasts.

Figure 4: Order Book Analysis and Revenue Projection

	Contract Value	Recognized in FY2012	Balance	FY2013	FY2014	FY2015
Paterson 2	70.5	21	160.0	138.7	21.3	0.0
Terrasse	110.5					
Twin Waterfalls	162.5	0	162.5	62.1	81.3	19.1
EC @ Sembawang	149.9	0	149.9	0.0	66.6	66.6
Total	493.4	21	472.4	200.8	169.2	85.7
Expected Contribution from New Projects				0.0	51.7	146.2
Forecast Revenue				200.8	220.9	232.0
Implied Year-on-Year Growth				20.0%	10.0%	5.0%

In formulating our yearly revenue forecasts, we input a projected growth rate and reconciled the output revenue against expected construction progress to arrive at the expected contribution from new projects as a check for reasonableness. Expected construction progress is formulated on a "straight-line" basis with slight adjustments to take into account faster progress midway through a project.

Source: SIAS Research

Expect Healthy Project Pipeline: We further assert that KH should be able to renew or even grow its order book on a timely basis given its efforts to increase staff count and positive industry conditions.

Based on our conservations with the management, we learnt that KH maintains about five to six bids on an on-going with an average contract size of about S$100m. Moreover, we also found out that KH current has staff strength of 150 versus 116 as at November 2011. The bulk of its staff is in the project management function. Given the increase headcount, we postulate that it is plausible for KH to take on more projects than it is currently executing.

Moreover, government land sales and land acquisitions by developers have led to a rich pipeline of projects for construction companies to bid for. Data from URA, as at 3Q 2012, suggests that there will be close to 100,000 private housing and executive condominium units to be completed from 2013 onwards, with 2015 and 2016 completions exceeding that of 2013 and 2014. We reckon that some of the projects due for completion in 2015 and 2016 may have yet been tendered out and are likely to be available for bidding by contractors in 1H 2013.

Figure 5: Pipeline Supply

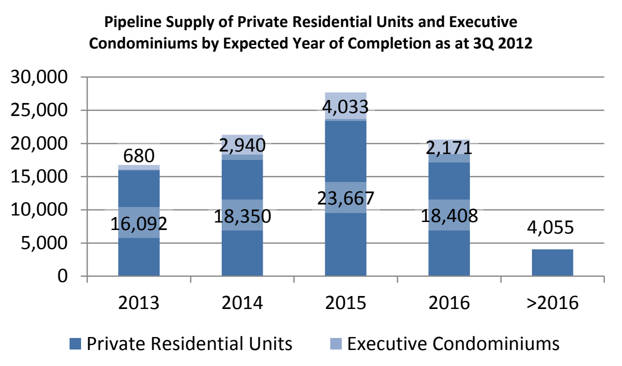
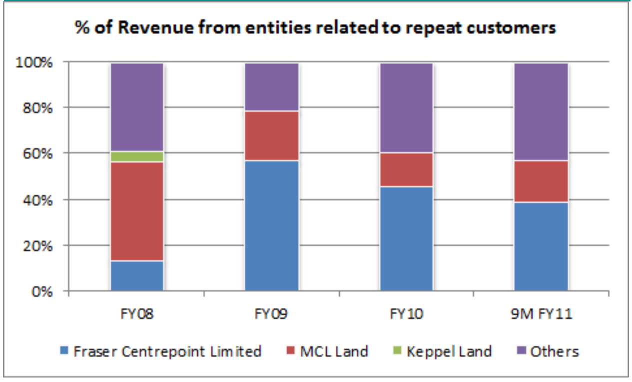


Chart data refers to projects with planning approvals. There is a further 10,070 units not included in the chart.
Source: URA

Figure 6: Leveraging on Repeat Customers



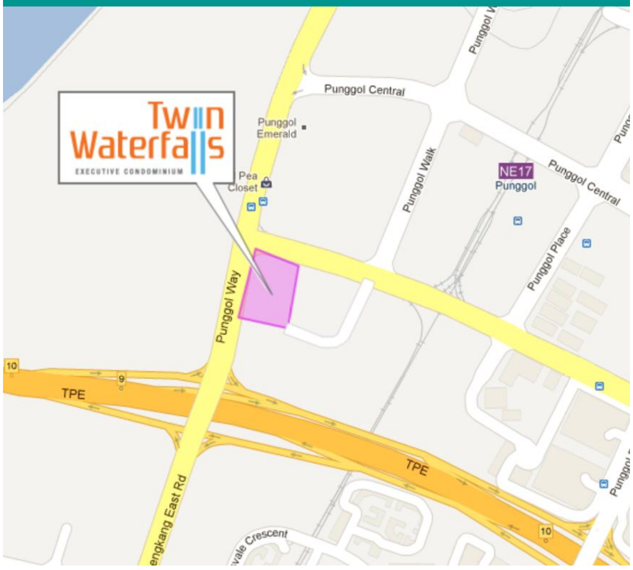
We counted at least five projects related to Keppel Land, three projects related to MCL Land and two projects related to Fraser Centrepoint Limited, based on major completed and on-going projects listed on Pages 92 to 94 of the IPO prospectus.
Source: IPO Prospectus

Twin Waterfalls >99% Sold

Twin Waterfalls is a JV property development project between KH and FCL Tampines Court Pte Ltd, a wholly-owned subsidiary of Frasers Centrepoint Limited. Launched in February 2012, there are only two units left unsold at Twin Waterfalls as at late January 2013. Based on caveats lodged with URA, the average selling price was S$712 per sq. ft. versus a land cost of about S$270 per sq. ft. per plot ratio and construction cost of about S$200 per sq. ft. We estimate that KH's share of profit from this development will be about S$18.5m and will be recognized in FY2014 or FY2015 when the executive condominium is completed in 2014. KH is also the main contractor for the project.

KH's FY2012 net profit attributable to shareholders was S$19.8m. The expected profit of S$18.5m from the development of Twin Waterfalls further supports our view of high growth from KH over the next two to three years.

Figure 7: Location of Twin Waterfalls



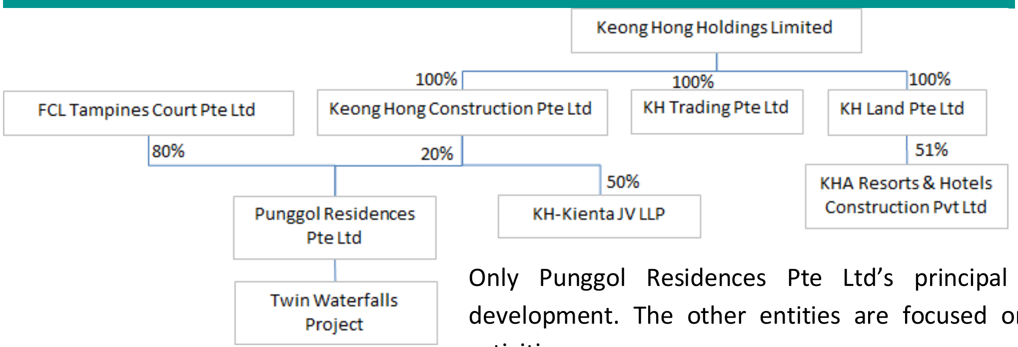
Source: http://www.twinwaterfalls.com

Figure 8: Project Details and Estimates

Tenure	Fresh 99 year lease
Land Area (sqm)	25,164.20
Plot Ratio	3.0
GFA (sqm)	75,492.6
Net Saleable Floor Area (sqm)	71,718.4
ASP (S$ per sq. ft.)	710
Sales Value (S$m)	548.1
Land Cost (S$m)	219.5
Construction Cost (S$m)	162.4
Other Costs (S$m) Est. 10% of sales	54.8
Tax (S$m) @ 17%	18.9
Est. Profit (S$m)	92.5
KH's share (S$m) @ 20% of profit	18.5

Source: SIAS Research

Figure 9: Corporate Structure (Exclude New JV added on 28 Jan 2013)

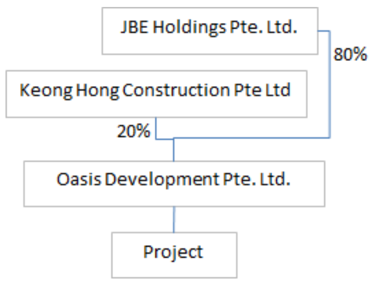


Source: SIAS Research

Only Punggol Residences Pte Ltd's principal activity is in real estate development. The other entities are focused on construction and building activities.

New Property Development Project Added: KH announced on 28 January 2013 that it is entering into a JV with JBE Holdings Pte Ltd (JBE) to jointly develop an executive condominium project at Sembawang Crescent / Sembawang Drive. JBE had earlier won the site on its own in December 2012 and is now roping in KH as the main contractor and joint developer. KH will invest S$0.2m in the JV and own 20% of the project.

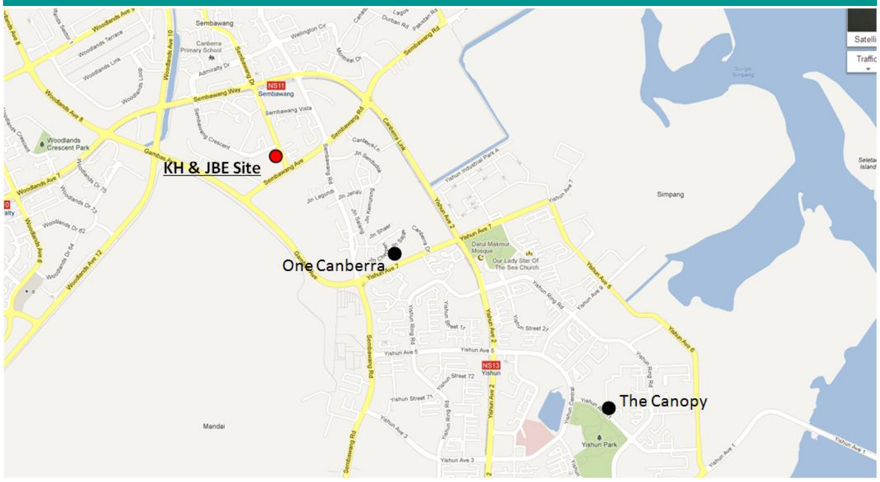
Project Structure



Comparable EC projects in the Yishun and Sembawang area include One Canberra at Yishun Avenue 7 and The Canopy at Yishun Avenue 11. These projects fetched average prices of about S$650 to S$700 per sq. ft, with One Canberra being sold at close to S$750 per sq. ft. for some units. We reckon that the JBE/KH project may fetch average prices of about S$720 per sq. ft., taking into consideration its proximity to the Sembawang MRT station/Bus interchange and Sun Plaza vicinity. Factoring in a rich 10% of sales proceeds for other costs such as professional fees and marketing expenses, we arrived at a conservative net profit estimate of S$6.8m accruing to KH on the completion of the project.

Actual profit may be higher depending on prices obtained when the project is launched in 2H 2013, as we note that private residential projects (non-EC) in the vicinity have fetched substantially higher prices.

Figure 10: Location of Site



Source: Google Maps, SIAS Research

Figure 11: Project Details and Estimates

Tenure	Fresh 99 year lease	Land Cost (S$m)	211.9
Land Area (sqm)	21,718.40	Construction Cost (S$m)	149.9
Plot Ratio	2.8	Other Costs (est. @ 10% sales)	44.8
GFA (sqm)	60,811.5	Tax	7.0
Net Saleable Floor Area (sqm)		Est. Profit	34.1
Est. at 95% of GFA	57,770.9	KH's share (@ 20% of profit)	6.8
Est. ASP (S$ per sq. ft.)	720		
Sales Value (S$m)	447.7		

Source: SIAS Research

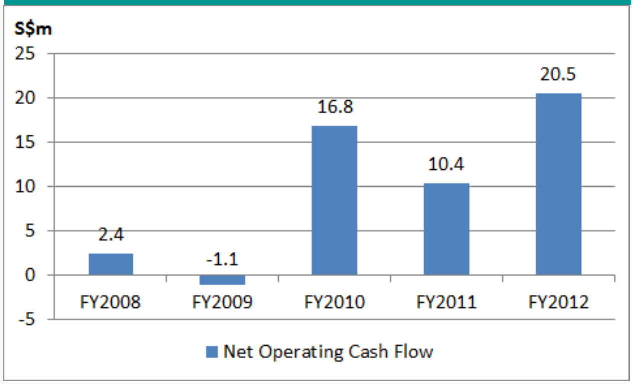
Healthy Balance Sheet and Cash Flow

KH raised net proceeds of about S$5.0m from its IPO in Dec 2011. Net operating cash flows were S$20.5m and S$10.4m for FY2012 and FY2011 respectively. A look at KH's balance sheet revealed that it ended FY2012 with cash of S$57.7m and only S$0.9m of finance lease payables.

Bank borrowings were held at the associate level, by Punggol Residences Pte Ltd, which is the holding company of the Twin Waterfalls project. Punggol Residences Pte Ltd (PRPL) had total liabilities of about S$322.5m and total assets of S$312.2m as of end FY2012. KH's share of gross liabilities totaled S$64.5m or S$2.06m based on net liabilities. PRPL is in a negative liability position as the project was largely funded via bank borrowings with PRPL having only S$1.0m of share capital. The project is expected to be profitable and cash flows from PRPL should improve nearer to completion.

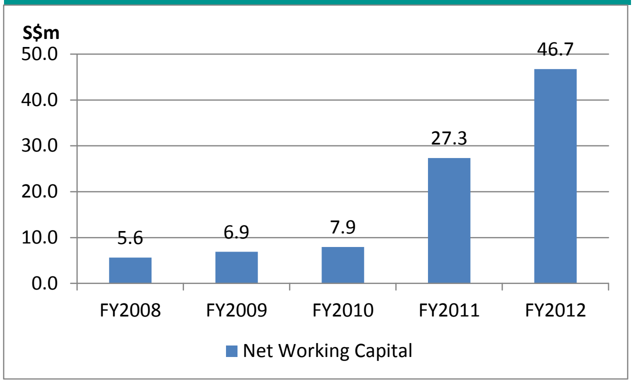
The construction business of KH is cash flow positive and debt free. KH's net working capital position has been relatively healthy as well, rising from S$7.9m in FY2010 to S$46.7m by FY2012. KH's current assets are quite evenly split between cash and receivables and its current cash balance is sufficient to offset 77% of current liabilities.

Figure 12: KH Net Operating Cash Flow



Source: Company Data

Figure 13: Net Working Capital



Source: Company Data

Figure 14: Summary of Current Assets & Liabilities, FY2012

Current Assets	S$m		Current Liabilities	S$m
Financial Assets at FV	0.6		Due to contract customers	29.0
Trade and Other Receivables	62.7		Trade and other payables	40.5
Cash	57.7		Bank borrowings	0.0
Total	121.0		Finance lease payables	0.5
			Current income tax payable	4.3
			Total	74.3

Source: Company Data

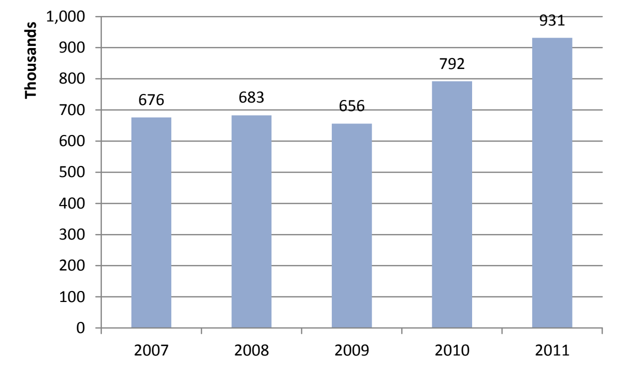
Future Plans for Growth

Thus far, we have established that KH has done relatively well as a construction company with an initial foothold in property development. Our observation is that KH is still pursuing business development in several frontiers to maintain long term growth of the company. These efforts, if successful, lay the foundation for long term enhancement of shareholders' value. These longer term measures can be viewed along three angles – a) Overseas Expansion, b) Expansion into Property Development and c) Competing for Higher Value Projects.

Overseas Expansion: KH secured a project in 2009 to construct a resort development at Falhumaafushi Island at Gaafu Alifu Atoll, Maldives. Thereafter, KH further secured a contract to build an airport on the island to service the resort. These contracts had helped KH diversify its portfolio and gain experience in overseas operations. As far as we understand, KH intends to continue bidding for contracts in the Maldives as and when opportunities are available. This is to leverage on its experience in this country and to export its mature construction know how.

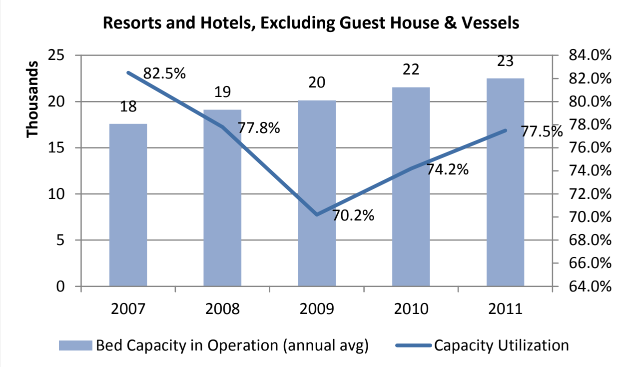
We are hopeful of further opportunities in the Maldives, which has a five year strategic action plan to increase operational tourist bed capacity from 25,000 beds to 35,500 beds over 2013 to 2017. However, we do not foresee aggressive overseas expansion, as we reckon that KH would want to manage its risks judiciously and not overstretch its resources.

Figure 15: Maldives Annual Tourist Arrivals



Source: www.tourism.gov.mv

Figure 16: Maldives Bed Capacity and Utilization



Source: www.tourism.gov.mv

Expansion into Property Development: KH entered the property development market to leverage synergies as both the developer and builder. Being involved in the planning of a project right from the initial stage gives KH the flexibility to envisage and pre-empt potential problems that may arise in the course of construction and early steps taken will result in higher efficiency and better cost management.

On the other hand, lessons gained from the property development business will allow KH to position itself as a solution provider to customers at the construction business, offering feasible solutions from both the developer and contractor's perspective to reduce overall costs and refine specifications.

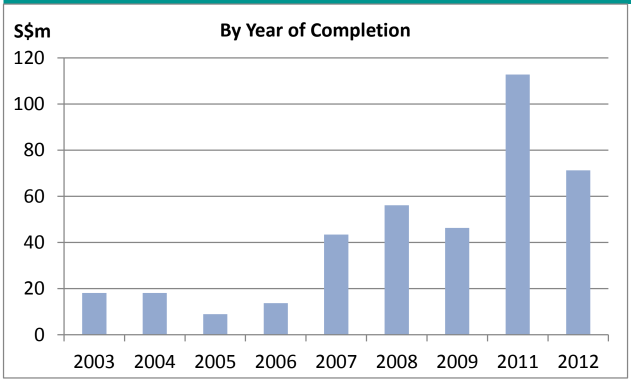
We gathered from our interviews with the management that KH is mindful of current conditions within the property development space. We do not foresee KH going on a land acquisition spree, but will instead continue to take an equity investment in development opportunities that arise, to raise growth and to build property development capabilities over time. The focus, in our impression, remains more on construction. As evidenced by the latest Sembawang EC project, KH only took on a 20% stake for an equity investment of S$0.2m.

Higher Value Projects: We perused through KH's list of major projects in its IPO prospectus and noted that KH has been completing increasingly higher value projects over the years. In 2003, KH completed two major projects with an average value of S$18.15m. By 2012, KH completed four major projects with an average value of S$71.3m. In fact, the total contract value of projects completed in 2011 and 2012 was S$510.9m versus just S$36.3m in 2003.

KH's track record of handling larger projects over time is evidence of the company's project management capabilities and differentiates itself from smaller competitors. Going forward, KH intends to take on more design and build contracts and is exploring ways to move into other segments of the construction industry.

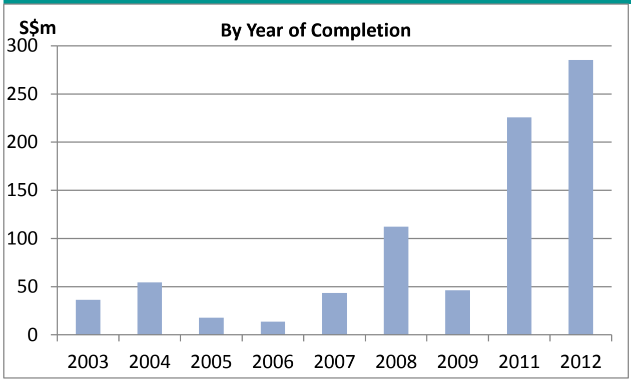
As the government intends to continue expanding the MRT network over the next ten odd years, we asked if KH has an interest in civil engineering. The management explained that they are exploring on how to collaborate with potential partners to take on related jobs, contributing their expertise in areas that are familiar to the company. We opine that any such moves may take some time to materialize, but the response we received implies well-rounded forward planning by the management.

Figure 17: Avg. Value of Major Projects



Source: Company Data

Figure 18: Total Value of Major Projects



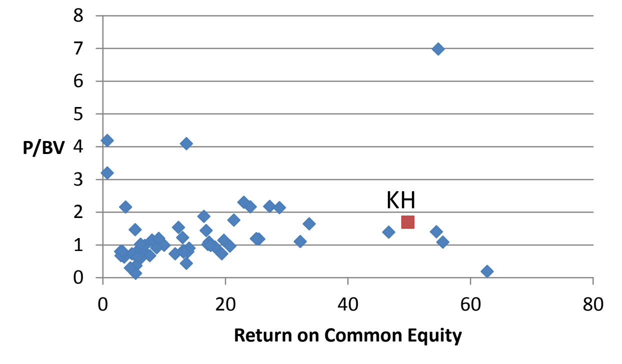
Source: Company Data

Attractive Valuation

For FY2012, KH reported net attributable profit growth of 111.2% and a return on common equity of 49.8%. However, KH trades at 4.4x FY2012 P/E and 1.7x P/BV based on a share price of S$0.540. We find such multiples conservative compared to other companies within the industry.

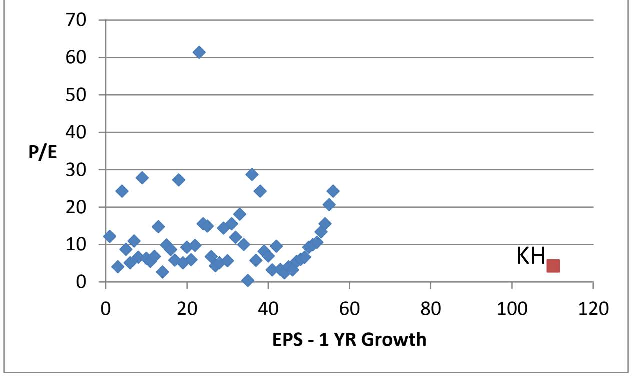
We obtained the return on equity and one-year earnings per share growth rate of SGX listed companies classified under the same category as KH based on the Bloomberg Industry Classification System and noted that KH stands out for its relatively conservative market multiples. The median company trades at 9.2x current P/E and 1.0x P/BV. The median EPS growth rate and ROE are 4.2% and 13.2% respectively.

Figure 19: P/BV versus ROE



Source: Bloomberg

Figure 20: P/E versus EPS Growth



Source: Bloomberg

Our valuation model values KH at S$0.715 per share based on a terminal growth rate of 2% and a cost of equity of 10.2%. This translates to 5.75x FY2013 P/E, which seems fairly conservative compared to KH's peers. Our valuation also implies an upside of 32.4% compared to the price of S$0.530.

Figure 21: Sample Peer Comparison (as at 25 January 2013)

	Mkt Cap (S$m)	P/E	P/BV	EPS Growth (%)	ROE (%)
Chip Eng Seng Corp Ltd	464.1	6.5	1.1	-29.3	17.3
Lian Beng Group Ltd	222.5	5.4	0.9	8.0	18.3
Tiong Seng Holdings Ltd	187.7	6.8	0.9	-11.9	14.1
Koh Brothers Group Ltd	134.1	9.2	0.7	82.2	7.6
KSH Holdings Ltd	149.7	5.8	1.0	-21.6	17.6
Wee Hur Holdings Ltd	380.2	27.7	4.1	20.8	13.7
Average	**256.4**	**6.7**	**0.9**	**5.5**	**15.0**
Keong Hong Holdings Ltd	84.8	4.3	1.7	110.2	49.8

Source: Bloomberg

Risks

Changes in Raw Material Prices: In pricing a contract, KH is exposed to risks such as cost overruns due to raw material price fluctuations. Some construction companies mitigate raw material price risk by procuring supplies shortly after being awarded a contract, or by passing these costs to subcontractors. According to the management, the price of most raw materials have stabilized lately while cement costs have inched up somewhat. Therefore, raw material costs do not seem to be a major risk to watch out for at this juncture.

Labor Costs and Availability: We opine that labor costs and availability present a larger risk to the company – a point that KH mooted in its results announcement dated November 2012. Our channel checks with some construction companies suggest that labor availability is being challenged by higher work volume versus limited local supply of construction professionals and the government’s move to tighten foreign worker supply.

KH is mitigating this risk via productivity improvements. In FY2012, the company invested in new plant and machinery, including boom lift, JCB telescopic handler, crane tower and scissor lifts. KH asserted that the adoption of technology and the mechanization of its work processes have raised construction productivity by 25% to 35%. Long term solutions come in the form of KH’s collaboration with SIM and BCA to offer scholarships for diploma students and undergraduates to attract local talent.

Revenue/Sales Volatility: KH recognizes construction revenue based on the percentage-of-completion method and manages two to three major projects at any one point in time. As a result, the completion of one project may cause short term fluctuations in revenue recognized if progress at a newer project has yet to ramp up as fast even though the company may have successfully renewed its order book.

Revenue from the Twin Waterfalls project will be recognized on completion and will thus contribute towards FY2014 or FY2015 results depending on the actual date of completion. The Twin Waterfalls is slated to be completed by December 2014 (FY2015). However, it is also possible that it be completed before end Sep 2014 for recognition in FY2014. To be conservative, we assumed that the Twin Waterfalls will be completed in FY2015.

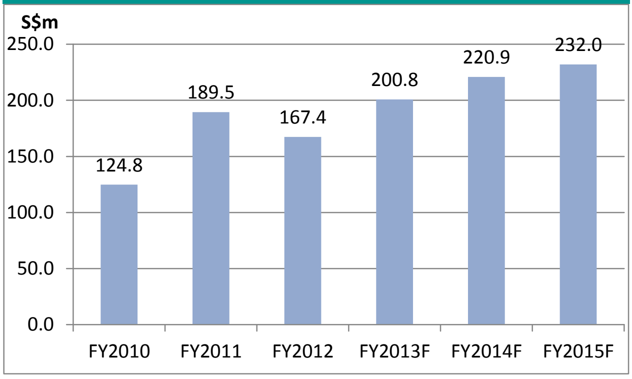
There is uncertainty over how well KH’s latest property development investment at Sembawang will sell and what prices it will fetch. We are of the view that this project will ultimately still be profitable. To mitigate risks from this source, we did not incorporate the results of this project into our forecasts and valuation.

Financials and Forecasts

KH ended FY2012 with record net profit of S$19.8m attributable to shareholders, up 111.2% versus that of FY2011. The increase in profitability came about in spite of lower revenue of S$167.4m against S$189.5m for FY2011 (down 11.7%). The decrease in revenue and higher profitability was due to the completion of certain higher margin projects.

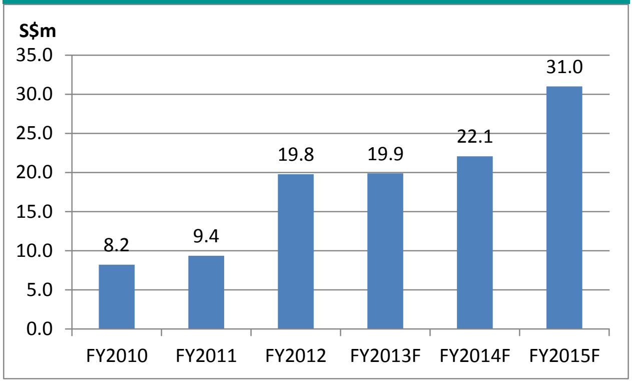
We expect revenue to resume its growth track in FY2013 as KH has three ongoing projects that are expected to ramp up pace this year. KH's gross margin was 17.6% in FY2012. We expect gross margin to be around 15% in FY2013 and FY2014 and operating expenses to be around S$6.3m to S$6.6m annually. Operating expenses including other income was S$5.3m in FY2012. As a result, we forecast FY2015 net profit to be S$31.0m, including S$18.5m of contribution from property development.

Figure 22: Reported & Forecast Revenue



Source: Company, SIAS Research

Figure 23: Reported & Forecast PATMI



Source: Company, SIAS Research

KH declared an interim dividend of 0.5 S cent and a final dividend of 1.5 S cents and a special dividend of 1.5 S cents for FY2012. The overall payout works out to 28.2% of FY2012 EPS. We forecast that KH will maintain a payout of around 30%, which works out to about 4 S cents for FY2013 and 5.8 S cents by FY2015.

In our valuation of KH, we incorporated debt held at the associate level, for property development, as part of the company's invested capital. We varied our cost of equity estimate by 1% point and terminal growth rate assumption 1% point to arrive at a valuation range of S$0.600 to S$0.900. Our valuation of S$0.715 works out to a discount of 4.7% from the midpoint of this valuation range.

Figure 24: 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	129.5	144.9
% of Debt	56.1%	49.8%	44.5%
% of Equity	43.9%	50.2%	55.5%
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			53.9
Discount Factor	0.9	0.9	0.8
Present Value	9.6	9.8	2.7
Book Value	50.0	Risk Free Rate	2.5%
Explicit Value	22.1	Beta	1.0
Terminal Value	42.2	Market RP	7.7%
Value of Equity	114.4	Cost of Equity	10.2%
Number of Shares (m)	160.0	Cost of Debt	5.4%
Value per share (S$)	0.715	LT Growth	2.0%

Source: SIAS Research

Key Investment Thesis: We like the basic forward visibility that KH provides with its order book, leaving upside risk to how fast KH can add new projects. From the longer term perspective, KH has a strong balance sheet to leverage on for future ventures, of which possible moves have already been mapped out by the company. The realization sustained growth in our view should help to bring about value discovery.

Figure 25: Financial Forecasts and Estimates

	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	22.1	31.0
Total Current Assets	83.9	110.9	121.0	135.9	155.8	180.8
Total Non-Current Assets	10.8	5.0	4.9	6.0	6.8	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	80.4	102.1
Cash from Operating Activities	16.8	10.4	20.5	17.1	22.0	35.6
Cash from Investing Activities	2.8	7.1	-2.5	-2.0	-2.0	-2.0
Cash from Financing Activities	-7.1	-2.9	8.5	-6.8	-6.6	-9.3
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%	30.8%	34.3%
Return on Assets	10.9%	10.4%	15.8%	14.7%	14.5%	17.7%
Gross Debt / Common Equity	23.4%	5.6%	1.7%	0.0%	0.0%	0.0%
Current Ratio	1.1	1.3	1.6	1.8	1.9	2.1
EPS (S cents)	5.1	5.9	12.4	12.4	13.8	19.4
BV/Share (S cents)	9.7	18.4	31.3	40.0	49.6	63.2
P/E	10.6	9.2	4.4	4.3	3.9	2.8
P/BV	5.5	2.9	1.7	1.4	1.1	0.9

Source: Company, SIAS 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.

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