

OKP Holdings Limited

It's All About Road Signals

OKP Holdings Limited's (OKP) 2Q FY10 results were within our expectations. OKP's prospects continue to be exciting with the promise of more contract wins to come. We believe that OKP shows value with 36.9% of its share price backed by cash. **Maintain Increase Exposure view with an intrinsic value of S\$0.810**

Fundamental Drivers:

- 2Q FY10 revenue and net attributable profit grew by 17% and 22% compared to the last quarter, as a result of higher percentage of revenue recognized from existing projects. We estimate that up to 50% of OKP's gross order book of S\$312.0m has yet to be recognized as revenue. This gives strong earnings visibility over the rest of FY10 and FY11.
- We expect industry players to submit bids to LTA for some 17 construction contracts related to the Downtown Line Stage 3 project over the next six months. If OKP is successful, we can expect to see its order book double in size.
- OKP recently increased its capacity with the purchase of a factory at Sungei Kadut, which will be used for fabrication works, workshop activities, storage and office purposes. We view this move as a signal of the company's positive growth prospects.

Outlook:

We like OKP for its strong balance sheet, credible set of growth opportunities and powerful execution ability. OKP's unlevered balance sheet provides financial strength to support an expansion of construction activities when contracts are won. At the same time, OKP has developed niches in the road transportation and oil & gas industries, which provide ample contract opportunities. However, shareholders need not worry about margin erosion as Management has emphasized on prudent bidding practices. **Maintain Increase Exposure view - intrinsic value: S\$0.810.**

Increase Exposure

- Intrinsic Value S\$0.810
- Prev Close S\$0.490

Main Activities

OKP Holdings Limited is a civil engineering company specializing in road and expressway construction. It has also diversified into the oil and gas infrastructure sector and had formed a JV to enter the African market in 2009.

Financial Highlights

(Y/E Dec) US\$m	FY08	FY09	FY10F
Revenue	101.8	130.0	139.8
Gross Profit	21.3	23.4	23.8
Earnings	11.6	14.4	15.2
EPS* (US cts)	4.2	6.1	5.9

Source: Company, SIAS Research

Key ratios (FY10F)

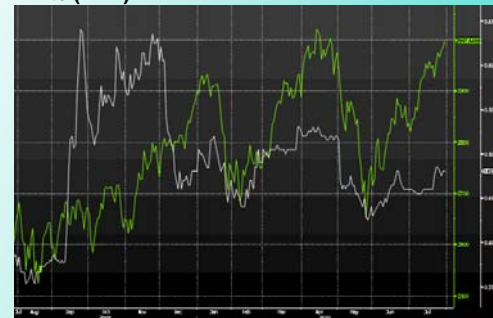
PER	8.2
P/BV	1.7
Return on Equity	22.7%
Gross Debt/ Equity	3.6%
Current ratio	2.0

Source: SIAS Research Estimate

Indexed Price Chart

Green (FSSTI)

White (OKP)



Source: Bloomberg

52wks High-Low*	64.1 S cts / 32.7 S cts
Number of Shares	264.6m
Market Capitalization	S\$129.7m
*Adjusted for bonus issue	

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2Q FY10 Results Update

Results were in line with expectations. OKP's results for the second quarter ended 30 June 2010 were largely within our expectations. 1H FY10 revenue and net attributable profit came in at 52.7% and 51.3% of our FY10F forecasts respectively. 1H FY10 gross margin was lower than expected. Nonetheless, 2Q FY10 gross margin, at 16.8%, was largely unchanged as compared to the first quarter. We updated our forecasts to reflect the lower gross margin, but kept revenue and net margin unchanged.

Strong QoQ growth delivered. On the whole, OKP turned in a good set of results, which showed QoQ growth of 17% and 22% for revenue and net attributable profit respectively. The strong growth was the result of higher percentage of revenue recognized from major construction projects.

Waiting for LTA to call for bids. To date, LTA has asked contractors to submit pre-qualification applications for 17 contracts (up from 11 contracts as of May 2010) related to construction work for the Downtown Line (DTL) Stage 3 project. Construction contracts for MRT stations and associated tunnels typically have a value of S\$250m or more. For example the DTL Stage 2 'Sixth Avenue and Blackmore' contract had a value of S\$320.7m.

According to our sources, contractors have already been pre-qualified for some of these contracts and industry players are waiting for LTA to call for bids. Bidders typically have 90 days to submit their proposals, which will be assessed based on quoted prices and technical specifications. We foresee that these contracts will be awarded within the next 12 months. We had previously anticipated these contracts to be awarded over a period of 12 to 24 months in May this year. Should OKP be successful in its efforts, we may see the company double its order book size.

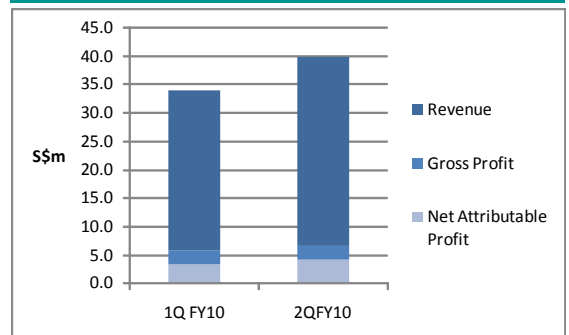
50% of order book yet to be recognized. OKP's gross order book as of July stands at S\$312.0m, up S\$5.9m from S\$306.1m in May. We estimate that up to 50% of its gross order book has yet to be recognized as revenue, giving us earnings visibility up to 2011.

Figure 1: Results within expectations

S\$m	1H FY10	FY10F	%
Revenue	73.7	139.8	52.7%
Gross Profit	12.4	25.9	47.8%
Net Attributable Profit	7.8	15.2	51.3%
Gross Margin	16.8%	18.5%	-1.7%
Net Margin	10.6%	10.9%	-0.3%

Source: Company, SIAS Research

Figure 2: High quarterly growth



Source: Company, SIAS Research

Figure 3: Downtown Line

Downtown Line	Stage 1	Stage 2	Stage 3
Route length	4.3km	16.6km	19.1km
No of stations	6	12	15
Expected completion date	2013	2015	2016

Source: Land Transport Authority, SIAS Research

Meanwhile, significant LTA projects that OKP can bid for include contracts to build an interchange at the TPE/Sengkang West/Seletar Aerospace junction and to widen a section of the Old Choa Chu Kang Road. The former is restricted to contractors of A1 tendering limit, implying a contract value of at least S\$85m. The latter has a contract value of between S\$40m and S\$85m based on its tendering limit.

Capacity expansion at Sungei Kadut. In late May, OKP announced that it was purchasing a detached factory building at Sungei Kadut with a gross floor area of 5,190 sq. m. at a price of S\$3.55m. The property has a remaining lease of about 15 years. OKP intends to use the factory as a fabrication yard, workshop, storage facility and office. We view this move as a positive signal on OKP's prospects. OKP could have simply rented additional factory space for short term capacity needs. OKP is traditionally a prudent company, with low debt levels and a history of conservative bids. The fact that it chose to purchase the property suggests that the company expects itself to undergo a sustained phase of growth.

Net cash per share of 17.7 Singapore cents. OKP ended 2Q FY10 with net current assets of S\$46.8m, which are fully backed by cash of S\$87.4m. Based on OKP's latest number of shares as of 14 June 2010, each share is supported by 17.7 Singapore cents of cash, net of current liabilities - equivalent to 36.9% of its previous closing price of S\$0.480. Excluding net cash per share, OKP is actually trading at 5.0x and 5.1x FY09 and FY10F PER respectively. We opine that this cash hoard gives OKP room to expand its balance sheet and to take on larger projects. Hence, we believe that OKP continues to show value at its current price.

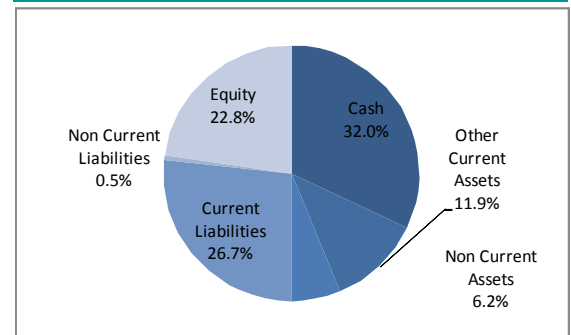
We updated our forecasts and valuation to arrive at an intrinsic value of S\$0.810, based on an updated cost of equity of 11.38% (10.78% as of May 2010). We expect OKP to continue winning new contracts over 2H 2010. **Maintain Increase Exposure view based on an intrinsic value of S\$0.810.**

Figure 4: Sample MRT contracts

Construction Contracts	Value(S\$m)
Landmark Station	230
Bayfront Station	463
Tunnels between Promenade Station & Marina Bay	103
Cross Street Station	225
Chinatown Station	160
Promenade Station	231
Bugis Station	582

Source: Land Transport Authority, SIAS Research

Figure 5: Strong Balance Sheet



Source: Company, SIAS Research

Figure 6: Economic Profit Valuation Model

	FY10F	FY11F	FY12F	FY13F	FY14F
Construction (S\$m)	117.8	143.3	172.0	202.1	232.4
Maintenance (S\$m)	22.0	24.2	26.6	29.3	32.2
Revenue (S\$m)	139.8	167.5	198.6	231.3	264.6
EBIT (S\$m)	18.0	21.5	26.6	30.9	35.3
Tax on EBIT (S\$m)	-2.8	-3.4	-4.1	-4.8	-5.5
NOPLAT (S\$m)	15.2	18.2	22.5	26.1	29.8
Invested Capital (S\$m)	62.4	78.7	93.1	110.9	128.6
% of Debt	4.3%	3.4%	2.9%	2.9%	2.9%
% of Equity	95.7%	96.6%	97.1%	97.1%	97.1%
WACC	10.97%	11.06%	11.11%	11.11%	11.11%
Capital Charge (S\$m)	6.8	8.7	10.3	12.3	14.3
Economic Profit (S\$m)	8.4	9.5	12.1	13.7	15.5
Terminal Value (S\$m)					184.5
Discount Rate	0.95	0.85	0.77	0.69	0.62
Present Value (S\$m)	8.0	8.1	9.3	9.5	9.6
Book Value (S\$m)	60		Risk Free	2.05%	
Explicit Value (S\$m)	44.5		Beta	1.03	
Terminal Value (S\$m)	114.9		Market RP	9.06%	
Value of Firm (S\$m)	218.9		Cost of Equity	11.38%	
Number of Shares (m)	269.8		Cost of Debt	1.95%	
Value per share (S\$)	0.810		LT Growth	2.50%	

Number of shares is based on the enlarged share capital after the exercise of warrants not owned by majority shareholders Or Kim Peow Investments Pte Ltd and China Sonangol International (S) Pte Ltd.

Source: SIAS Research

Figure 7: Peer Comparison

Peers	PER	P/BV	ROE	ROA	Debt/Equity
Yongnam Holdings Ltd	6.7	1.5	23.9%	8.6%	84.8%
Lian Beng Group Ltd	6.5	1.1	14.8%	5.1%	98.0%
Hock Lian Seng Holdings Ltd	5.3	1.9	39.5%	14.2%	0.0%
Koh Brothers Group Ltd	7.9	0.6	6.9%	1.9%	160.6%
Lum Chang Holdings Ltd	3.8	0.8	9.2%	4.6%	21.5%
Tiong Seng Holdings Ltd	3.3	1.4	51.5%	11.3%	42.5%
Average	5.6	1.2	24.3%	7.6%	67.9%
OKP	7.9	2.1	29.2%	14.5%	4.6%

Source: SIAS Research Estimate

Figure 8: Financial Forecasts and Estimates

	FY07	FY08	FY09	FY10F	FY11F	FY12F	FY13	FY14
Revenue	124.7	101.8	130.0	139.8	167.5	198.6	231.3	264.6
Gross Profit	21.8	21.3	23.4	23.8	28.5	33.8	39.3	45.0
Operating Profit	12.4	11.6	15.8	17.5	21.0	26.1	30.4	34.8
Net Profit	10.9	9.5	14.4	15.2	18.2	22.5	26.1	29.8
Attributable to Shareholders								
Total Current Assets	63.2	63.0	105.8	116.5	130.9	156.4	190.5	228.6
Total Non-Current Assets	13.7	13.9	16.6	18.7	21.0	23.8	26.9	30.5
Total Current Liabilities	40.1	33.3	61.2	57.6	60.0	70.4	81.7	93.5
Total Non-Current Liabilities	2.7	2.8	1.7	1.5	1.5	1.5	1.5	1.5
Total Equity	34.2	40.7	59.5	76.0	90.4	108.2	134.3	164.1
Cash from Operating Activities	13.0	15.8	44.6	10.3	15.6	30.8	32.6	40.5
Cash from Investing Activities	-1.9	-0.2	-5.0	-4.6	-5.3	-6.1	-7.0	-8.1
Cash from Financing Activities	-0.8	-5.1	2.6	1.3	-3.8	-4.7	0.0	0.0
Net change in cash	10.3	10.5	42.3	7.0	6.5	20.0	25.5	32.4
Receivable Days	83.7	111.0	73.1	73.1	73.1	73.1	73.1	73.1
Payable Days	158.2	118.7	248.7	200.0	183.7	183.7	183.7	183.7
ROE (%)	38.8%	25.6%	29.2%	22.7%	22.0%	22.7%	21.6%	20.0%
ROA (%)	17.5%	12.3%	14.5%	11.8%	12.7%	13.5%	13.1%	12.5%
Debt/Equity	11.1%	10.3%	4.5%	3.6%	3.0%	2.5%	2.0%	1.6%
Current Ratio	1.6	1.9	1.7	2.0	2.2	2.2	2.3	2.4
EPS (S cents)	7.36	4.21	6.06	5.89	6.74	8.32	9.66	11.04
BV/Share (S cents)	21.3	25.6	23.1	28.0	33.3	39.9	49.6	60.6
PER	6.5	11.4	7.9	8.2	7.1	5.8	5.0	4.3
P/BV	2.3	1.9	2.1	1.7	1.4	1.2	1.0	0.8

Source: Company, SIAS Research

Rating Definition:

Increase Exposure – The current price of the stock is significantly lower than the underlying fundamental value 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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