

OKP Holdings Limited

Smooth Road Ahead

OKP Holdings Limited (OKP) reported another strong set of 3Q FY11 results. PATMI increased by 8.2% YoY to S\$4.9m while gross profit margin improved from 19.4% a year ago to 32.4% this quarter. With an estimated net order book of >S\$250m and sustainable margin improvement from design-and-build projects, we continue to be bullish on OKP. **Maintain Increase Exposure based on an intrinsic value of S\$0.980.**

Key Developments:

Higher Margin: 3Q FY11 gross margin reached 32.4%, substantially higher than 19.4% in 3Q FY10, due to cost savings in design-and-build projects, better project management and tighter cost control. Net profit grew by 8.2% YoY to S\$4.9m while revenue declined by 30.4% YoY to S\$25.5m in 3Q FY11. The lower reported revenue was due to the substantial completion of existing projects, while newly secured *design-and-build* contracts are still in their early stages and are expected to contribute more significantly in the coming quarters.

Strong Core Business: OKP won two contracts in August 2011 with a total value of S\$51.75m. Including these two contracts, OKP has won public sector contracts worth a total of S\$152.0m in 2011 thus far – more than replacing the S\$119.3m “CTE widening” contract that has already been 93% completed. Revenue contribution from these newer contracts should pick up in the coming quarters as work at these projects pick up pace.

New Business Coming Up? China Sonangol International (S) Pte Ltd (CSIS) raised its stake in OKP from 9.23% to 14.15% by buying 15 million vendor shares at S\$0.66 for a total consideration of S\$9.9m with the management retaining a combined 57.1% stake in OKP. This move demonstrates both the management and CSIS's commitment to OKP's growth and we suspect that another collaboration may be in the horizon. We noted that OKP recently incorporated a new subsidiary OKP Land Pte. Ltd in early October for investment holding and property development purposes.

Increase Exposure

- Intrinsic Value S\$0.980
- Prev Close S\$0.550

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 recently formed a JV to enter the private property construction segment.

Financial Highlights

(Y/E Dec) S\$ m	FY09	FY10	FY11F
Revenue	130.0	139.9	114.7
Gross Profit	23.4	29.5	37.5
Earnings	14.4	17.0	23.1
EPS (S cts)	6.1	6.5	8.2

Source: Company, SIAS Research

Key ratios (FY11F)

PER	6.7
P/BV	2.0
Return on Common Equity	29.6%
Return on Assets	15.8%
Gross Debt to Common Equity	2.1%
Current ratio	2.2

Source: SIAS Research

Indexed Price Chart

Green (FSSTI)

White (OKP)



Source: Bloomberg

52wks High-Low[^] S\$0.685 /S\$0.4898
 Number of Shares 304.77m
 Market Capitalization S\$167.6m
[^]adjusted for warrants conversion

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On a Dual Lane Carriageway

Contribution from Current Projects to Ramp Up: In April this year, OKP won the S\$61.7m contract to build a road interchange at the TPE/Sengkang West Road/Seletar Aerospace Way intersection. This project is targeted to be completed in October 2014 and is only 7% finished thus far. Accordingly, revenue contribution from projects typically follows the “S” curve, where work is ramped up after the initial planning, design and application approvals have been completed.

In August 2011, OKP won the S\$46.8m contract to improve Alexandra Canal between Zion Road and Kim Seng Road from PUB with work commencing from September 2011 to 1Q 2014. Including the S\$28.5m LTA contract to widen Old Choa Chu Kang Road, these three projects are more than sufficient to replace the S\$119.3m CTE widening contract that is nearing completion. The company won S\$152.0m public sector contracts this year.

While the company could have won more contracts by bidding more aggressively, we like OKP’s prudence in tender participation, which has helped the company manage growth and improve profitability. Thus far, we have seen how higher value “design-and-build” projects have led to sustained high profitability for OKP.

But Order Book Will Still Grow: Coming up is a project to expand the CTE/TPE/SLE interchange. While the results of this tender, which closed at the end of September 2011, are not out yet, we are optimistic of OKP’s chances given that it is already executing projects for both the TPE and CTE and should have some advantage in terms of design and project management. The value of this project should be similar to other expressway works, such as the current S\$61.7m TPE project, if not higher.

Other projects that OKP seems to have shown interest in include the construction of a new dual four-lane road in Bukit Brown, improvement works in the Kallang Area and the construction of vehicular underpass at the Nicoll Highway/Guillemard Road junction. Later in 2H 2012, we will be watching the market for tenders for the North-South Expressway mega project.

Property Development: OKP has also been signaling its intention to enter into property development for some time. With the increased stake by CSIS and its involvement in the local property market, OKP seems to be moving closer to the execution of its intent. We were reassured that, if any investment were to be made, the capital to be committed will be in measured amounts. It seems that the company’s purpose is to participate in growth opportunities on hand with consideration of risks in the property market. We like collaborations with sizeable partners as the resultant developments will be notable in scale without hefty outlays from OKP.

We noted that CSIS is also active in the Indonesian market based on the earlier press release when CSIS raised its stake in OKP. The management is mum (and in fact, non-committal) about opportunities in Indonesia, but we think that CSIS's activities in the region suggest space for further exploration of collaboration opportunities in the long term. Our point is that OKP's potential does not lie solely within the Singapore road infrastructure space depending on how the company manages its network and resources.

Figure 1: OKP's Order Book and Selected Bids

No	Brief Description	Start Date	Est. End Date	Contract Value (\$m)
1	Widening of CTE	30-Jan-09	29-Dec-11	119.3
2	Ad hoc repairs and upgrading of roads I	03-May-10	02-Aug-13	19.4
3	Ad hoc repairs and upgrading of roads II	03-May-10	02-Aug-13	14.9
4	Desilting of Bukit Timah Diversion Canal	26-Jul-10	25-Oct-11	6.0
5	Cleantech Park Phase 1	19-Oct-10	18-Jun-12	14.5
6	Angullia Park Development	22-Dec-10	22-Apr-13	83.5
7	Widening of Old Choa Chua Kang Road	14-Feb-11	13-Feb-14	28.5
8	Sewer Extension – various locations	29-Mar-11	Nov-12	4.2
9	Interchange at TPE (Design-and-Build)	4-Apr-11	3-Oct-14	61.7
10	PUB – Roadside Drains Improvement I	25-May-11	Nov-12	3.4
11	PUB – Roadside Drains Improvement II	4-Jul-11	Jan-13	2.5
12	Sewer – Tuas Avenue South	19-Aug-11	1-Jul-12	4.9
13	Improvement to Alexandra Canal	5-Sep-11	4-Mar-14	46.8

No	Selected Tenders
1	Expansion of CTE/TPE/SLE Interchange

Source: Company Announcements, LTA website, GeBiz, SIAS Research

Results Overview: OKP's 9M FY11 performance was within our expectations in terms of profitability – PATMI came in at 73.6% of our prior full year forecasts. We had underestimated OKP's year-to-date margins by about 2 percentage points. OKP's order book remains rich. Given that it has several projects to be ramped up, we continue to be optimistic about its revenue prospects. Nonetheless, we adjusted our revenue forecast to better factor in OKP's "high margin/medium volume" approach. However, our profit forecast for FY11F and our valuation of OKP remain unchanged.

Figure 2: Results Overview

S\$m	9M FY11	9M FY10	Growth	Prior FY11F	9M % of FY11F
Revenue	86.6	110.2	-21.4%	130.1	66.6%
Gross Profit	28.2	19.5	44.6%	39.0	72.3%
EBIT	20.7	15.1	37.1%	28.0	73.9%
PATMI	17.0	12.3	38.3%	23.1	73.6%
			Chg		Variance
Gross Margin	32.5%	17.7%	14.8%	30.0%	2.6%
EBIT Margin	23.9%	13.7%	10.2%	21.5%	2.4%
Net Margin	19.6%	11.2%	8.5%	17.8%	1.9%

S\$m	3Q FY10	4Q FY10	1Q FY11	2Q FY11	3Q FY11
Revenue	36.6	29.6	32.8	28.3	25.5
Gross Profit	7.1	10.0	8.8	11.2	8.3
EBIT	5.6	5.5	6.4	8.4	5.9
PATMI	4.5	4.6	5.2	6.9	4.9
Gross Margin	19.4%	33.8%	26.7%	39.4%	32.4%
EBIT Margin	15.2%	18.6%	19.6%	29.6%	23.0%
Net Margin	12.3%	15.7%	15.9%	24.3%	19.2%

Source: Company Announcements, SIAS Research

Figure 3: Economic Profit Valuation Model

	FY11F	FY12F	FY13F	FY14F
Revenue (S\$m)	114.7	129.0	148.4	170.6
EBIT (S\$m)	28.0	31.5	35.1	40.4
Tax on EBIT (S\$m)	-4.9	-5.5	-6.1	-7.0
NOPLAT (S\$m)	23.1	26.0	29.0	33.3
Invested Capital (S\$m)	71.2	70.6	80.7	94.2
% of Debt	2.6%	2.6%	2.3%	2.0%
% of Equity	97.4%	97.4%	97.7%	98.0%
WACC	11.5%	11.5%	11.5%	11.5%
Capital Charge (S\$m)	8.2	8.1	9.3	10.9
Economic Profit (S\$m)	14.9	17.9	19.7	22.5
Terminal Value (S\$m)				255.4
Discount Rate	0.95	0.85	0.76	0.68
Present Value (S\$m)	14.1	15.2	15.0	15.4
Book Value (S\$m)	68.9		Risk Free	1.9%
Explicit Value (S\$m)	59.7		Beta	1.1
Terminal Value (S\$m)	174.3		Market RP	9.1%
Value of Firm (S\$m)	303.0		Cost of Equity	11.73%
Number of Shares (m)	309.1		Net Cost of Debt	1.76%
Value per share (S\$)	0.980		LT Growth	2.50%

The number of shares assumes the full conversion of all remaining warrants. OKP currently has only 4.34m warrants outstanding.

Source: SIAS Research

Figure 4: Financial Forecasts and Estimates

	FY08	FY09	FY10	FY11F	FY12F	FY13F	FY14F
Revenue	101.8	130.0	139.9	114.7	129.0	148.4	170.6
Gross Profit	21.3	23.4	29.5	37.5	42.2	48.5	55.8
Operating Profit	11.6	15.8	19.7	28.0	31.5	35.1	40.4
Net Profit	9.5	14.4	17.0	23.1	26.0	29.0	33.3
Attributable to Shareholders							
Total Current Assets	63.0	105.8	131.2	112.4	117.7	130.1	144.8
Total Non-Current Assets	13.9	16.6	21.9	26.4	31.0	36.6	43.2
Total Current Liabilities	33.3	61.2	82.8	51.2	50.4	56.8	64.8
Total Non-Current Liabilities	2.8	1.7	1.3	0.9	0.9	0.9	0.9
Total Equity	40.7	59.5	68.9	87.0	97.4	109.0	122.3
Cash from Operating Activities	15.8	44.6	39.1	8.0	11.0	49.5	27.3
Cash from Investing Activities	-0.2	-5.0	-8.1	-7.0	-8.3	-9.9	-11.7
Cash from Financing Activities	-5.1	2.6	-8.3	-13.9	-15.6	-17.4	-20.0
Net change in cash	10.5	42.3	22.8	-12.8	-12.9	22.3	-4.5
Receivable Days	111.0	73.1	71.3	71.3	71.3	71.3	71.3
Payable Days	118.7	248.7	290.5	180.0	180.0	180.0	180.0
ROE (%)	25.6%	29.2%	26.5%	29.6%	28.2%	28.1%	28.8%
ROA (%)	12.3%	14.5%	12.3%	15.8%	18.1%	18.4%	18.8%
Debt/Equity	10.3%	4.5%	2.7%	2.1%	1.9%	1.7%	1.5%
Current Ratio	1.9	1.7	1.6	2.2	2.3	2.3	2.2
EPS (\$ cents)	4.21	6.06	6.50	8.16	8.54	9.50	10.94
BV/Share (\$ cents)	25.6	23.1	25.3	28.0	31.4	35.2	39.6
PER	13.1	9.1	8.5	6.7	6.4	5.8	5.0
P/BV	2.1	2.4	2.2	2.0	1.8	1.6	1.4

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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