SIAS RESEARCH

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Update Report

Ryobi Kiso Holdings Ltd.

Adopting a Long Term View

Ryobi Kiso Holdings Ltd (Ryobi) reported 2Q FY13 (ended Dec 2012) net profit attributable to shareholders of S$0.3m on revenue of S$40.3m. Ryobi is continuing to execute its strategy of expanding in Vietnam and Australia, thus diversifying out of Singapore. We adjusted our net profit estimates to incorporate Ryobi's performance in 1H FY13. We maintain that Ryobi should see higher profitability as it grows its revenue base and gains economies of scale in the process. ***Maintain Increase Exposure.***

Key Highlights:

Results Overview: 2Q FY13 revenue (S$40.4m) was lower than that of 1Q FY13 (S$53.7m). The decline could be explained via the completion of certain projects in 1Q FY13 and the year-end holiday season in Australia in 2Q FY13. As a result, PATMI fell by S$0.6m from 1Q FY13.

Gunning for Long Term Growth: Since July 2012, Ryobi has secured more than ten contracts in Australia. We perceive that Ryobi could have delivered quarterly revenue growth by taking on more higher risk or lower priced projects in Singapore, but has instead chosen to spend effort in developing its business in Vietnam and Australia. Ryobi is currently executing more than ten projects in Singapore and has five on-going projects in Australia.

From a longer term perspective, this move makes sense in two ways – a) the Australian piling industry offers higher margin and b) Ryobi has the advantage of more advanced construction technologies in Vietnam. If successful, Ryobi avoids head on competition in Singapore, while building the foundations for growth in new markets.

Order Book: Ryobi's net order book stood at S$85.1m as at 31 Dec 2012 and is comparable to that of S$90.3m as at 30 Sep 2012. The net order book size is still higher than the S$70m to S$80m range observed from end 2010 to end 2011. Since 1 January 2013, Ryobi has garnered an additional S$18m of contracts.

Increase Exposure

- Intrinsic Value S$0.179
- Prev Close S$0.133

Main Activities

Ryobi Kiso Holdings Ltd. provides piling services and ground engineering solutions. Its projects include both public and private sectors' infrastructure and building developments. Ryobi's customers include government bodies, statutory boards, property owners, developers and main contractors.

Financial Highlights

(Y/E Jun) S$ m	FY12	FY13F	FY14F
Revenue	153.3	176.3	185.1
Gross Profit	19.1	21.2	24.1
EBIT	4.8	4.8	6.9
PATMI	3.4	2.9	4.7
EPS (S cts)	0.44	0.39	0.62

Source: Company, SIAS Research

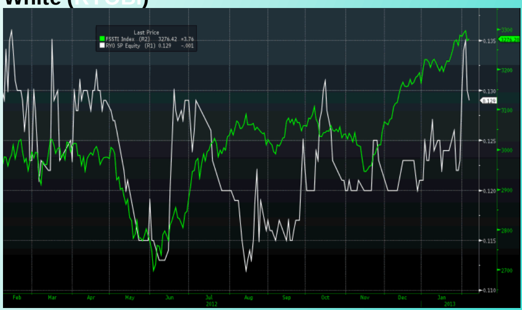
Key ratios (FY14F)

PER	21.3
P/BV	0.85
Return on Common Equity	4.0%
Return on Assets	2.1%
Gross Debt to Common Equity	0.36
Current ratio	1.56

Source: SIAS Research

Indexed Price Chart

Green (FSSTI)
White (RYOBI)



Source: Bloomberg

52wks High-Low	*S$0.138 /S$0.112*
Number of Shares	*749.3m*
Market Capitalization	*S$99.65m*

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Revenue is In-Line with Expectations: 2Q FY13 revenue, though lower than that of 1Q FY13, was actually within our expectation of at least S$40m. We reckon that quarterly revenue of at least S$40m is reasonable for the next two quarters, given the stable order book. In all, we forecast FY13F revenue to be S$176.3m. We lowered gross margin forecasts to 12% for FY13F, in line with 12.1% observed for 1H FY13. The net outcome is a lower forecast net profit to shareholders of S$2.92m for FY13F versus S$3.36m for FY12. The lower net profit forecast takes into account lower year-on-year PATMI for 1H FY13 (S$1.1m) versus 1H FY12 (S$2.3m).

Stage Set for Rebound in FY14F? However, the stage is set for a rebound in FY14F. Based on the reasonable assumptions of 5% revenue growth, 1% point increase in gross margin to 13% and 5% increase in operating expenses, we estimate that FY14F PATMI will be S$4.7m. As forecasted net margin will rise from 1.7% in FY13F to 2.5% in FY14F, a slight improvement in piling rates and gross margin going forward will lead to a substantially higher net margin.

We opine that a rebound in Ryobi's margin is more likely in FY14F than in FY13F as wage pressure and labour shortage is relatively acute in the local construction industry at this juncture. As a subcontractor, Ryobi is more susceptible to this risk than main contractors. Ryobi will most probably have to build its revenue base in Australia and wait for construction prices in Singapore to further adjust for higher labour costs.

Lengthening of Forecast Horizon: Looking at Ryobi's financial performance, we decided that our usual three-year forecast horizon will not be sufficient to fully capture the upside out of Ryobi's growth plans, as well as any subsequent upside in piling rates. Based on our assessment of the current situation, Ryobi's growth should be more obvious from FY14F onwards. Therefore, we extended the final year of explicit forecasts from FY15F to FY17F, adopting a five-year forecast horizon. The outcome is an expected positive economic profit only in FY17F. Previously, we had expected so-called "economic turnaround" in FY15F.

Valuation at 17.9 S cents: The net result is an intrinsic value of S$0.179 per share. We do not change our input cost of equity as Ryobi's share buybacks have incidentally capped downside risk. Ryobi's share price traded within a 52 week range of S$0.112 to S$0.138. Ryobi bought back 5.1m shares in the quarter ended 31 Dec 2012, equivalent to about 0.67% of its shares oustanding as at end Jun 2012 (end FY12).

A sidenote is the effect of Ryobi's share buybacks and bank borrowings on its capital structure. The cost of Ryobi's capital employed is increasingly shifted from its shareholders to banks, thus justifying a somewhat higher P/E multiple.

Initial Contribution from Property Investment: In 2Q FY13, Ryobi recognized an initial contribution of S$5k from property investment, as the company completed some of the industrial units at the "Ryobi Tech Hub" within the Ascendas Protrade Singapore Tech Park. Contribution from property investment will gradually increase as more units are completed and leased out. We await for further information regarding this business.

Figure 1: 2Q FY13 Results Overview

Y/E Jun	1Q FY12	2Q FY12	3Q FY12	4Q FY12	1Q FY13	2Q FY13
Revenue	28.4	40.3	40.9	43.7	53.7	40.4
Gross Profit	3.8	4.3	5.3	5.7	7.0	4.3
Operating Profit	1.1	1.6	0.9	1.3	0.8	0.6
Net Attributable Profit	0.5	1.4	0.7	0.7	0.9	0.3
EBITDA	4.2	4.8	4.1	4.5	4.3	4.2
Gross Margin	13.5%	10.7%	13.0%	13.0%	13.1%	10.7%
Net Margin	1.8%	3.5%	1.7%	1.6%	1.7%	0.8%
EBITDA Margin	14.8%	11.9%	10.0%	10.3%	8.0%	10.4%

Source: Company Data, SIAS Research

Figure 2: Economic Profit Valuation Model

S$m	FY13F	FY14F	FY15F	FY16F	FY17F
Revenue	176.3	185.1	194.4	204.1	214.3
EBIT	4.8	6.9	10.1	12.5	15.2
Tax on EBIT	-0.6	-0.9	-1.3	-1.3	-1.3
NOPLAT	4.2	6.0	8.8	11.2	13.8
Invested Capital	164.8	161.9	164.3	168.0	172.8
% of Debt	28.5%	26.3%	25.9%	25.4%	24.7%
% of Equity	71.5%	73.7%	74.1%	74.6%	75.3%
WACC (%)	6.6%	6.7%	6.8%	6.9%	6.9%
Capital Charge	10.9	10.9	11.1	11.6	12.0
Economic Profit	-6.7	-5.0	-2.3	-0.4	1.9
Terminal Value					38.3
Discount Rate	0.97	0.91	0.85	0.79	0.74
Present Value	-6.5	-4.5	-2.0	-0.3	1.4
Book Value	117.9		Risk Free Rate		1.5%
Explicit Value	-12.0		Beta		1.0
Terminal Value	28.3		Risk Premium		6.5%
Value of Equity	134.2		Cost of Equity		8.0%
Number of Shares (m)	749.3		Cost of Debt		3.7%
Value per share (S$)	0.179		LT Growth		2.0%

Source: SIAS Research

Figure 3: Financial Forecasts and Estimates

S$m	FY10	FY11	FY12	FY13F	FY14F	FY15F	FY16F	FY17F
Revenue	120.8	123.3	153.3	176.3	185.1	194.4	204.1	214.3
Gross Profit	46.7	27.4	19.1	21.2	24.1	27.2	30.6	34.3
Operating Profit	33.9	12.2	4.8	4.8	6.9	10.1	12.5	15.2
PATMI	27.4	7.8	3.4	2.9	4.7	7.5	9.6	11.9
Total Current Assets	110.5	107.5	115.5	118.9	133.7	143.3	152.5	163.5
Total Non-Current Assets	72.5	91.5	93.8	102.1	94.0	90.1	87.8	84.8
Total Current Liabilities	50.2	48.0	66.6	81.1	85.5	87.5	89.5	91.6
Total Non-Current Liabilities	17.9	31.9	24.8	20.5	20.5	20.5	20.5	20.5
Total Equity	114.9	119.2	117.9	119.3	121.7	125.4	130.2	136.2
Cash from Operating Activities	16.6	-4.3	8.3	27.8	13.4	36.0	0.8	41.5
Cash from Investing Activities	-27.9	-20.6	-8.3	-20.3	-10.0	-10.0	-10.0	-10.0
Cash from Financing Activities	27.2	10.5	-8.5	-5.8	-2.3	-3.7	-4.8	-6.0
Net Change in Cash	15.9	-14.5	-8.4	1.7	1.1	22.3	-14.0	25.6
Inventory Days	1.0	2.0	2.0	3.0	3.0	3.0	3.0	3.0
Receivable Days	111.8	156.3	160.0	160.0	150.0	120.0	120.0	120.0
Payable Days	192.9	122.3	90.0	120.0	120.0	120.0	120.0	120.0
Return on Common Equity	35.5%	6.8%	2.9%	2.5%	4.0%	6.2%	7.7%	0.1
Return on Assets	18.8%	4.6%	2.1%	1.4%	2.1%	3.2%	4.1%	0.0
Gross Debt / Common Equity	0.16	0.37	0.41	0.37	0.36	0.35	0.34	0.3
Current Ratio	2.20	2.24	1.73	1.47	1.56	1.64	1.70	1.8
EPS (S cents)	4.18	1.02	0.44	0.39	0.62	1.00	1.28	1.6
BV / Share (S cents)	14.7	15.3	15.1	15.4	15.7	16.2	16.9	17.7
PER	3.2	13.0	30.2	34.2	21.3	13.3	10.4	8.4
P/BV	0.90	0.87	0.88	0.86	0.85	0.82	0.79	0.75

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 theirexposure 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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