

Chip Eng Seng Corporation Ltd –

Paring down estimates on construction delays

11 Dec 2008

Recommendation BUY

Bloomberg Code CHIP SP

Share Price S\$0.17

Target Price S\$0.20

Upside Potential 18%

Report Type

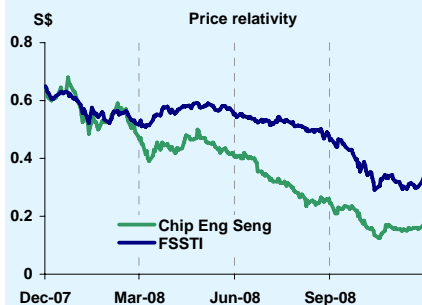
Corporate Updates

Company website

www.chipengseng.com.sg

Stock data

Sector :	Property & Construction
Share Cap :	667.5m shares
Market Cap:	S\$113.5m
Major Shareholders:	
Lim family	32.9%
Citadel Holdings	25.0%
Free float	34.9%



Analyst

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Investment Highlights

Construction segment impacted by S\$9.1m foreseeable losses in 3Q08

The S\$9.1m provision provided for in 3Q08 came on top of the S\$12.3m already provided for in FY07. According to management, the provision was mainly for The Parc and The Suite@Central development projects, which was hit by higher than the projected construction cost.

Updates on property development projects

- Grange Infinite and CityVista Residences slightly delayed by difficult ground conditions but still on track for delivery.** In our 2Q08 results update, we mentioned that the Group recognised 20% upfront upon signing S&P agreement for CityVista Residences, The Parc and Grange Infinite, in line with the Group's revenue recognition policy in FY07. We believe The Parc is on track to meet our forecast of cumulative 35% completion by end of FY08. Our discussion with management revealed that Grange Infinite and CityVista Residences development projects were slightly delayed by difficult ground conditions but is on track for delivery in FY10F. We expect minimal contribution from Grange Infinite and CityVista as the 20% construction progress hurdle rate is unlikely to be crossed. We push back our recognition forecast to cumulative 60% completion, from 65% previously, for the two projects by end of FY09F.
- Removal of sales assumed for the remaining unsold 32 CityVista Residences units.** We previously assumed 100% sales of CityVista's remaining 32 unsold units in FY08. However, in view of the weak property market, we have removed sales from these units.
- Waiting for window opportunities to launch Elias Road development.** We understand from management that Elias Road will be launch-ready by 1Q09. As the project targets are the mass market, management is fairly optimistic that there will be window opportunities to launch the project in FY09. To be conservative, we have removed contribution from Elias Road development from our earnings forecast.

Earnings cut by 39.6~19.7% to S\$44.2~67.6m for FY08~09F respectively

- Revenue cut by 6.9~8.4% for FY08~09F respectively.** We cut our FY08F top line forecast by 6.9% to S\$346.8m as we reduced construction revenue contribution from Grange Infinite and CityVista Residences due to construction delays encountered by Chip Eng Seng. We cut our FY09F top line forecast by 8.4% to S\$336.1m, mainly due to removal of Elias Road development contribution and partly offset by increased in construction revenue contribution from Grange Infinite and CityVista Residences.
- Gross profit cut by 32.4~22.2% for FY08~09F respectively.** We reduced our FY08F forecast by 32.4% to S\$17.0m, after taking into account the unexpected S\$9.1m provision for foreseeable losses recorded in 3Q08. We further cut FY09F's gross profit by 22.2% to S\$5.1m as we forecast a conservative gross profit margin for construction projects.
- Share of profits from associated companies cut by 39.0~21.0% for FY08~09F respectively.** We cut our FY08F forecast by 39.0% to S\$40.6m, due to delay in construction of Grange Infinite and CityVista Residences development projects, resulting minimal contribution as the 20% hurdle rate is unlikely to be crossed. In addition, we removed sales assumed for the remaining unsold 32 CityVista Residences units, leading to lower profit contribution in FY08~09F.

Valuation & Recommendation

Maintain BUY recommendation with price target revised to \$0.20. We continue to value CES using sum-of-the-parts valuation method, valuing its property developments and construction business. We have revalued all of CES's unsold development projects at lower than recently transacted price to assume 100% sales in current market. We rolled forward and revised our earnings multiples, due to reduced contract win visibility, to 3x FY09F construction earnings from 5x FY08F previously. We further apply 60% discount factor to SOTP valuation, taking into account risk of buyers on deferred payment scheme defaulting, deriving our price target of S\$0.20.

Financial snapshot

FYE: Dec (S\$m)	FY06	FY07	FY08F	FY09F
Revenue (S\$ 'm)	165.1	201.2	346.8	336.1
Gross profit (S\$ 'm)	12.6	0.6	17.0	5.1
Net profit (S\$ 'm)	14.7	50.3	44.2	67.6
EPS (Sg cts)	2.4	7.5	6.6	10.1
EPS growth (%)	30.5	210.9	(12.2)	52.9
P/E (x)	7.0	2.3	2.6	1.7
P/B (x)	1.2	0.7	0.6	0.4
ROE (%)	16.5	31.4	22.0	26.3

Source: Company data; Westcomb research

Valuation Table

	GFA (sf)	Stake (%)	Sold (%)	Tenure	Valuation (S\$psf)	Capital Value	Gain/ (Loss)
						(S\$'000)	(S\$'000)
Investment Properties							
Market Value of Investment properties						30,706	
Book value of investment properties @31 Dec 2007						(30,706)	-
Development Properties							
NPV of development profits							
Ventuno Balmoral	50,012	100	100	FH	1,350	15,627	
Elias Road Development	456,162	100	0	99yr	550	(497)	
Suite @ Central	223,028	40	100	FH	1,300	13,638	
CityVista Residences	156,644	50	54	FH	2,239	40,331	
The Parc	899,841	50	94	FH	862	70,095	
Grange Infinite	175,803	25	100	FH	2,800	27,448	
Surplus from Singapore residential development properties							166,642
Surplus from Vietnam residential development properties							1,899
Construction Income							
3x FY08F Earnings							1,064
Total Gain/(Loss)							169,605
NAV (as at 31 Dec 2007)							160,272
Total Valuation							329,877
Total Shares issued ('000)							667,514
SOTP valuation per share							0.49
Target price after 60% discount to SOTP valuation							0.20

Source: Company data; Westcomb research

Financial Ratio

Income Statement, FYE 31 Dec

S\$ 'm	FY06	FY07	FY08F	FY09F
Revenue	165.1	201.2	346.8	336.1
COGS	(152.4)	(200.5)	(329.9)	(331.0)
Gross Profit	12.6	0.6	17.0	5.1
Operating Expenses	(5.9)	(9.9)	(11.6)	(12.0)
Other Income	1.5	8.4	0.3	0.3
Operating Profit	8.2	(0.9)	5.7	(6.6)
Share of profits from assoc	8.3	51.9	40.6	76.2
Net Interest income	0.2	1.6	2.5	2.5
Profit before tax	16.7	52.6	48.7	72.1
Income Tax	(2.0)	(2.3)	(4.5)	(4.6)
Net Profit	14.7	50.3	44.2	67.6
Minority Interest	0.0	0.0	0.0	0.0
PATMI	14.7	50.3	44.2	67.6
EPS (Sg cts)	2.4	7.5	6.6	10.1
DPS (Sg cts)	1.5	1.8	0.8	2.0
Book Value per share (Sg cts)	14.7	24.0	30.0	38.5

Cash Flow, FYE 31 Dec

S\$ 'm	FY06	FY07	FY08F	FY09F
Profit before tax	16.7	52.6	48.7	72.1
Adjustments:	(4.9)	(47.5)	(28.3)	(83.2)
Change in working cap.	(32.3)	20.1	(132.5)	46.3
Income tax paid	(2.3)	(1.6)	(4.0)	(4.5)
Net Cash from operations	(22.7)	23.5	(116.1)	30.8
CapEx	(1.1)	(1.6)	(1.6)	(1.6)
Others	(3.1)	(43.6)	2.5	69.9
CF from Investing	(4.2)	(45.1)	0.9	68.3
Dividends Paid	(4.9)	(7.5)	(11.5)	(4.0)
Issuance (Repurchase)	0.0	25.5	0.0	0.0
Net Borrowing (Repayment)	41.9	12.9	119.8	(72.5)
Others	0.0	0.0	(0.0)	0.0
CF from Financing	37.0	31.0	108.3	(76.5)
Change in Cash	10.2	9.4	(6.9)	22.6
Starting Cash Balance	2.9	13.1	22.5	15.6
Ending Cash Balance	13.1	22.5	15.6	38.2

Balance Sheet, as at 31 Dec

S\$ 'm	FY06	FY07	FY08F	FY09F
Property, Plant & Equipment	1.2	2.3	3.1	3.3
Others	94.8	201.6	236.2	245.0
Non Current Assets	96.1	203.9	239.3	248.3
Property held for sale	19.8	14.2	7.1	7.8
Contracts in progress	10.0	10.6	11.1	11.7
Development properties	46.5	30.1	185.0	148.0
Trade and other debtors	30.4	50.6	66.3	61.3
Cash and cash equivalents	13.1	22.5	15.6	38.2
Total Current Asset	119.7	128.0	285.2	266.9
Trade creditors	46.6	65.6	97.2	102.6
Bank borrowings	56.1	5.0	115.0	126.5
Others	7.5	20.0	21.3	22.2
Total current liabilities	110.2	90.7	233.5	251.3
Bank borrowings	16.1	80.1	30.0	6.0
Others	0.2	0.6	60.6	0.6
Total non current liabilities	16.3	80.7	90.6	6.6
Share Capital & reserves	89.1	160.3	200.4	257.3
Minority Interest	0.2	0.2	0.0	0.0
Total Shareholders Equity	89.3	160.5	200.4	257.3

Growth/Ratio (%)	FY06	FY07	FY08F	FY09F
Revenue Growth	65.4	21.9	72.4	(3.1)
Gross Profit Growth	19.1	(94.9)	2,526.2	(69.7)
Net Profit Growth	30.5	242.1	(12.2)	52.9
EPS Growth	30.5	210.9	(12.2)	52.9
DPS Growth	50.0	16.7	(57.1)	166.7
Gross Margin	7.6	0.3	4.9	1.5
Net Margin	8.9	25.0	12.7	20.1
ROE	16.5	31.4	22.0	26.3
ROA	0.1	0.2	0.1	0.1
Net gearing (x)	0.7	0.4	0.6	0.4

Valuation	FY06	FY07	FY08F	FY09F
P/E (x)	7.0	2.3	2.6	1.7
P/B (x)	1.2	0.7	0.6	0.4
Dividend Yield (%)	8.8%	10.3%	4.4%	11.8%

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Trading Buy	: + 10% to + 15% range over the next 3 months
Hold	: +/- 15% range over the next 12 months
Trading Sell	: - 10% to - 15% range over the next 3 months
Sell	: >15% downside over the next 12 months

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