

# Chip Eng Seng

**PRICE S\$0.14**
**BUY**
**Key Stock Statistics**

NRA EPS Est. 2005	1.9
P/E on NRA Est. 2005	7.3
NRA EPS Est. 2006	3.7
P/E on NRA Est. 2006	3.8
Dividend/Share	1.5
Dividend yield (%)	11%
Shs. Outstg. (m)	606.8
Market capitalisation \$m	85.0
Avg. daily vol (m)	0.843
Book Value/Share	0.12
Shareholders:	
Lim Family	41.1%

**Per share data**

YE Dec	2002	2003	2004	2005E	2006E
Book Value (S\$)	0.11	0.12	0.12	0.13	0.16
Cash Flow (cts)	1.04	1.99	2.05	2.03	3.81
Earnings (cts)	0.81	1.73	1.83	1.91	3.68
Dividend (cts)	0.75	2.00	1.50	1.50	1.50
Payout Ratio	93%	116%	82%	79%	41%
PER (x)	17.3	8.1	7.7	7.3	3.8
P/CF (x)	13.5	7.0	6.8	6.9	3.7
P/BV (x)	1.3	1.1	1.1	1.1	0.9
Dividend yield %	5.4%	14.3%	10.7%	10.7%	10.7%
ROE (%)	7.2%	14.1%	13.8%	14.5%	23.5%

**P&L analysis (\$m)**

YE Dec	2002	2003	2004	2005E	2006E
Revenue	176.0	159.8	141.8	139.9	178.6
Operating Profit	4.7	11.6	8.1	11.8	17.9
Depreciation	1.1	1.2	0.8	0.8	0.8
Interest Expense	-0.1	-0.2	-0.1	-0.2	-0.2
Pretax Profit	6.5	11.3	12.8	14.5	27.9
Effective tax rate	-38.8%	-24.1%	-18.1%	-20.0%	-20.0%
Net Profit	4.0	8.6	10.4	11.6	22.3

**Margins**

Gross	5.0%	10.5%	8.2%	11.0%	12.2%
Operating	2.6%	7.1%	5.6%	8.3%	9.9%
Pre tax	3.7%	7.1%	9.0%	10.3%	15.6%
Net	2.3%	5.4%	7.4%	8.3%	12.5%

**Still a BUY Despite Lesser Performance**

- 1H05 results was at best flat, with net profit up just 5% from a year ago on the back of a 21% decline in group turnover. Revenue from the construction segment climbed 12%, but was more than offset by a slide of 81% in revenue from the property development arm. Less revenue was realized from the OneFort project during the period and there was no revenue recognition from the other projects.
- We had earlier expected property development projects ShanghaiOne, 40%-owned Riviera Residences and the S\$279m construction contract of The Pinnacle@Duxton (Duxton) to contribute to this year's earnings. However, it is now known that these projects will only start contributing in FY06, with delays in the construction works the likely culprit.
- As a result, we have revised our projections to reflect the delay in revenue recognition from these projects. FY05 turnover is now likely to be more or less flat at S\$140m, while net profit should increase marginally to S\$11.6m, or 1.9ct per share. Assigning a forward PER of 7x, our fair value peg in earlier reports, the stock appears fully valued at the current price of S\$0.14.
- However, we believe there is no material change in the outlook for Chip Eng Seng (CES), and it is just a matter of when the revenue is recognized. While our FY05 EPS is down, our FY06 EPS is now 3.7ct, translating into an undemanding forward FY06 PER of 3.8x.
- We still see the unique investment theme in CES – a recovery play (construction sector) stapled with a REIT, which yields high dividend. Hence we are maintaining our BUY rating.

## 1H05 RESULTS

YE Dec	1H04 (S\$m )	1H05 (S\$m )	YoY %
Building construction	46.77	52.39	12%
Property development	26.63	5.14	-81%
Rental	0.79	0.79	1%
Others	0.51	0.86	69%
<b>Total Revenue</b>	<b>74.70</b>	<b>59.18</b>	<b>-21%</b>
Cost of sales	(68.52)	(52.64)	-23%
<b>Gross profit</b>	<b>6.18</b>	<b>6.54</b>	<b>6%</b>
Other revenue	0.03	0.36	1016%
Selling expenses	(0.09)	(0.26)	184%
Admin expenses	(3.19)	(3.19)	0%
<b>PBIT</b>	<b>2.93</b>	<b>3.45</b>	<b>18%</b>
Interest expense	0.00	(0.05)	NM
<b>Operating profit</b>	<b>2.93</b>	<b>3.39</b>	<b>16%</b>
Associates	2.85	2.78	-3%
<b>Pre tax profit</b>	<b>5.79</b>	<b>6.17</b>	<b>7%</b>
Taxation	(1.20)	(1.34)	12%
<b>Net profit</b>	<b>4.59</b>	<b>4.83</b>	<b>5%</b>

## EARNINGS ESTIMATES

Earnings Forecasts					
YE Dec (S\$m)	2002	2003	2004	2005E	2006E
<b>EBIT</b>	<b>1.8</b>	<b>8.8</b>	<b>8.2</b>	<b>12.0</b>	<b>18.1</b>
Building construction	3.9	3.9	4.9	5.1	6.1
Property development	(1.0)	4.0	2.1	6.0	11.1
Rental	(0.1)	0.7	1.0	0.7	0.7
Others	(0.5)	0.2	0.2	0.2	0.2
Interest expense	(0.1)	(0.2)	(0.1)	(0.2)	(0.2)
Operating profit	1.7	8.6	8.1	11.8	17.9
Associates	4.8	2.7	4.7	2.6	10.0
<b>Pre tax profit</b>	<b>6.5</b>	<b>11.3</b>	<b>12.8</b>	<b>14.5</b>	<b>27.9</b>
Taxation	(2.5)	(2.7)	(2.3)	(2.9)	(5.6)
<b>Net profit</b>	<b>4.0</b>	<b>8.6</b>	<b>10.4</b>	<b>11.6</b>	<b>22.3</b>
Wtd no of shares	490.2	490.9	545.9	606.8	606.8
EPS	0.8	1.8	1.9	1.9	3.7
DPS-regular	0.25	0.50	0.75	0.75	0.75
DPS-special	0.50	1.50	0.75	0.75	0.75
DPS-Total	0.8	2.0	1.5	1.5	1.5

## BALANCE SHEET

### Balance Sheet & Other Fin. Data(\$m)

YE Dec	2002	2003	2004	1H05
Plant and equipment	3.1	1.7	1.3	1.0
Investment property	24.5	24.0	22.8	22.8
Long term assets	35.4	35.5	37.5	35.7
Current assets	134.0	132.8	165.7	130.7
Current liabilities	90.0	82.2	116.0	81.4
Long term liabilities	24.7	24.9	11.6	11.6
Total net assets	54.7	61.2	75.7	73.2
Shareholders funds	54.7	61.1	75.6	73.1
Net debt	12.9	27.1	36.4	13.4
Gearing	23.5%	44.3%	48.2%	18.3%

## RECOMMENDATION

The Building and Construction Authority (BCA) of Singapore reported earlier this month that leading indicators are pointing to a possible upturn in Singapore's construction sector. Employment in the sector registered growth in 2Q05, the first time in 4 ½ years. BCA's forecast value of contracts for 2005 has also been raised S\$0.5b to S\$10.5b – S\$11.5b, on account of higher demand in the private residential sector.

As the S\$279m construction contract for Duxton is now not expected to contribute to CES's FY05 results, growth in CES's construction arm this year is likely to come from its pre-Duxton order book of approximately S\$190m, assuming no new addition.

As for its property development business, we believe delays in the construction of the ShanghaiOne apartments and the Riviera Residences have made it impossible for the group to realize any benefit from these projects for this fiscal year. Therefore earnings for this segment will mainly be coming from the OneFort project and its 30%-owned Grandeur 8 project this year. CES's Glenelg project in Adelaide, Australia, should also be contributing this year but the fact that it was not mentioned in the announcement, leads us to suspect that there could be some delays there as well. We will be meeting up with the management soon and we will do an update when more light is shed on the Australian project.

We still see a unique investment theme in CES – a recovery play (construction sector) stapled to a “REIT” based on its tacit commitment to paying out high dividend funded partially by its investment portfolio. It will only divest its unencumbered investment properties if there is more productive usage of the proceeds. Gross dividend yield based on the last declared dividend is high at 11%. We see no reason why the pay-out can not be maintained.

Although FY05 is now likely to be disappointing, it is due more to timing of project recognition and not a change in the outlook for the company. . Therefore we are basing our recommendation on FY06's results instead. The PE valuation is undemanding, at 3.8x for FY06. Our BUY rating stays. Our initial target price of S\$0.185 is pegged at five times FY06 EPS to account for risks such as construction delays, and will adjust it upwards to our fair forward PER of 7x, once it is certain the income from CES's projects will be recognized accordingly in FY06.

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