


**DMG & Partners Research**  
**CONSTRUCTION**

Selena Leong  
 +65 6232 3898  
 selena.leong@sg.oskgroup.com

Terence Wong, CFA  
 +65 6232 3896  
 terence.wong@sg.oskgroup.com

**Construction**

Kian Ann Engineering is one of the world's largest independent distributors of heavy machinery parts and diesel engine components. It has the capacity to carry >1.3m items covering >270 brands like Caterpillar, Volvo and Kobelco and distributes to >50 countries.

**Stock Profile/Statistics**

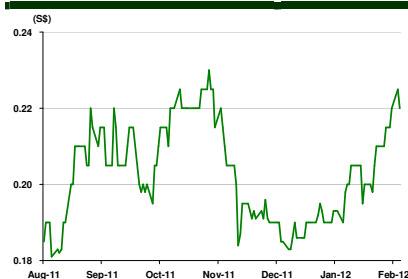
Bloomberg Ticker	KAE SP
STI	2,987.41
Issued Share Capital (m)	438.1
Market Capitalisation (\$m)	96.4
52 week H   L Price (\$)	0.235   0.17
Average Volume ('000)	307.9
YTD Returns (%)	15.8
Net gearing (x)	0.04
Altman Z-Score	3.39
ROCE/WACC	1.31
Beta (x)	0.90
Book Value/share (S¢)	33.66

**Major Shareholders (%)**

Lau Hung Swee & Sons	27.24%
Low Han Cheong	12.85%
Lau Hwee Beng	10.19%

**Share Performance (%)**

Month	Absolute	Relative
1m	15.79%	7.41%
3m	0.00%	-5.56%
6m	18.92%	14.99%
12m	0.00%	3.77%

**6-month Share Price Performance**

**2QFY12 Results Review**

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<b>KIAN ANN ENGINEERING</b>	<b>BUY</b>	<b>↕</b>
<b>Price</b>	<b>S\$0.22</b>	
<b>Previous</b>	<b>S\$0.31</b>	
<b>Target</b>	<b>S\$0.31</b>	

**Organic growth continues**

Kian Ann Engineering's (KA) 2QFY12 earnings were in line with our expectations. Earnings jumped 10.7% YoY, reaching S\$4.5m, on the back of a 3.4% YoY rise in revenue, higher interest income, FX gain and lower other operating expenses. Trading at 5.1x FY12 earnings, we believe the stock is undervalued when compared against its construction-related and heavy equipment peers at 6.5x CY12 earnings. Based on a target P/E of 7x FY12 earnings (5-year historical average), we value KA at a TP of S\$0.31, implying a 40.9% upside.

**2QFY12 earnings within expectations.** KA's 2QFY12 earnings jumped 10.7% YoY to S\$4.5m, largely attributable to FX gain, higher interest income and lower other operating expenses. 2QFY12 revenue grew 3.4% YoY on the back of broad-based growth from 1) Indonesia (+13% YoY), 2) Other Asean Countries (+8.3% YoY), 3) Singapore (+1.8% YoY), 4) Other Asian Countries (+0.3% YoY) and 5) Non-Asian Countries (+19% YoY, largely on the back of growth from Australia, Papua New Guinea, Brazil and United Kingdom), hitting S\$42m due to strong demand from the mining and infrastructure sectors. The above increase in sales was partially offset by Malaysia's sales (-11.3% YoY) due to lower demand from the forestry sector. Gross margins eased 0.9ppt YoY to 27.4%, on the back of competitive pressure. Nonetheless, at this level, gross margin is still above its historical average of ~25%.

**Higher interim dividend declared.** KA has declared an interim dividend of 0.33S¢, versus last year's 0.325S¢. KA's dividend policy is to payout at least 25% of earnings in dividends to shareholders each year.

**Expanding warehouse capacity.** KA is adding 7,600sqm of gross floor area at its Changi South warehouse. Construction has commenced in Dec 2011 and is expected to complete by 2QFY13. This extension would boost KA's total warehousing space by ~46% to more than 24,200sqm, allowing KA to increase its competitive edge via the distribution of an increased range of parts to cater to its clients.

FYE Jun (\$m)	FY09	FY10	FY11	FY12F	FY13F
Turnover	134.8	149.4	162.3	178.5	196.4
Net profit	11.5	13.2	16.8	19.1	21.1
% chg YoY	3.5%	15.2%	26.6%	13.8%	10.7%
Consensus net profit	-	-	-	19.3	19.7
EPS (S¢)	2.6	3.0	3.8	4.4	4.8
DPS (S¢)	0.7	1.0	1.1	1.1	1.1
Div Yield	3.2%	4.5%	5.0%	5.0%	5.0%
ROE (%)	10.0%	10.7%	12.4%	12.9%	13.0%
ROA (%)	6.5%	7.6%	8.9%	9.0%	9.1%
P/E (x)	8.4	7.3	5.7	5.1	4.6
P/B (x)	0.8	0.7	0.7	0.6	0.6

Source: Company data and DMG estimates

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## Results Table (\$m)

Year Ended Jun	2QFY11	2QFY12	% Chge YoY	1QFY12	% Chge QoQ	Comments
Revenue	40.6	42.0	3.4%	44.2	-5.0%	Up YoY driven by increase in sales from Indonesia, Non-Asian Countries, Other Asean countries, offset by a decline in Malaysia's sales.
Cost of Sales	-29.0	-30.5	4.9%	-31.7	-3.8%	
Gross Profit	11.6	11.5	-0.6%	12.5	-8.1%	
Rental Income	0.1	0.1	9.5%	0.1	1.1%	
Other income	0.1	0.5	607.9%	0.2	123.2%	
Distribution costs	-3.6	-3.3	-7.2%	-3.4	-2.5%	Down YoY due to higher reversals of impairment loss for trade related debts, offset by higher employment cost and higher allowance for inventories obsolescence.
Administrative expenses	-2.4	-2.7	11.9%	-2.4	9.0%	
Other operating expenses	-0.5	-0.2	-57.1%	-0.5	-51.2%	Up YoY due to higher employment cost.
Operating Profit	5.3	6.0	12.7%	6.6	-9.4%	Lower YoY largely due to net FX gain in this quarter.
Finance Costs	-0.1	-0.2	34.8%	-0.2	7.5%	
Share of profit/(loss) from joint venture companies/ associates	0.0	0.0	-	0.0	-	
Profit before Taxation	5.2	5.8	12.1%	6.4	-9.9%	
Taxation	-0.9	-1.1	26.4%	-1.0	14.4%	
Minority Interests	0.2	0.1	-28.8%	0.2	-21.3%	
Net profit attributable to shareholders	4.1	4.5	10.7%	5.3	-14.0%	

Source: Company data

## FINANCIALS

Year End Jun (\$m)					
Income Statement					
	FY09	FY10	FY11	FY12F	FY13F
Revenue	134.8	149.4	162.3	178.5	196.4
Cost of sales	(99.3)	(111.4)	(116.2)	(128.6)	(142.4)
Other income	0.6	1.7	1.4	1.7	1.7
Operating Expenses	(22.3)	(22.3)	(26.1)	(27.6)	(29.1)
Other credits / (charges)	0.0	0.0	0.0	0.0	0.0
Finance costs (net)	(1.4)	(0.7)	(0.6)	(0.7)	(0.7)
Profit before tax	12.3	16.6	20.8	23.5	26.0
Tax	(0.7)	(3.0)	(3.2)	(3.6)	(4.0)
Profit including minority interest	11.6	13.6	17.6	19.8	21.9
Minority interest	0.1	0.4	0.8	0.7	0.8
Profit attributable to equity holders	11.5	13.2	16.8	19.1	21.1

Balance Sheet					
	FY09	FY10	FY11	FY12F	FY13F
Cash	20.4	27.7	23.3	37.9	55.2
Other current assets	121.5	118.0	136.4	140.6	145.0
Fixed assets	24.1	23.8	23.7	23.6	23.5
Non-current assets	5.7	5.3	18.1	20.6	19.5
Total assets	171.8	174.7	201.5	222.7	243.2
Current liabilities (excl. debt)	22.1	26.2	34.2	38.4	40.1
Debt	27.9	16.4	22.6	23.5	24.5
Other long term liabilities	1.1	1.2	1.3	2.4	3.1
Total liabilities	51.0	43.9	58.1	64.3	67.7
Shareholders equity	119.2	128.9	140.5	154.8	171.1
Minority interest	1.6	1.9	2.8	3.6	4.4
Total equity	120.8	130.9	143.4	158.4	175.5
Total equity and liabilities	171.8	174.7	201.5	222.7	243.2

\* includes bank overdrafts

Source: Company data and DMG estimates

Cash Flow					
	FY09	FY10	FY11	FY12F	FY13F
Operating cash flow before working capital changes	15.5	19.7	22.3	24.6	27.1
Working capital changes	(10.8)	(0.0)	(1.8)	(1.8)	(1.8)
Other operating cashflow	(1.8)	(2.9)	(3.2)	(3.5)	(4.0)
Net cash from operations	2.9	16.7	17.3	19.3	21.4
Net cash from investing activities	(1.1)	(0.6)	(13.6)	(0.2)	(0.2)
Net change in debt	2.6	(5.3)	(3.5)	0.9	1.0
Other financing cashflow	(2.8)	(3.6)	(4.4)	(4.8)	(4.8)
Net cash from financing activities	(0.2)	(8.8)	(7.9)	(3.9)	(3.8)
Net incr. in cash/cash equivalents	1.5	7.3	(4.2)	15.2	17.3
Cash at beginning of year	18.1	19.7	26.9	22.7	37.9
Cash at end of year*	19.7	26.9	22.7	37.9	55.2

Margins	FY09	FY10	FY11	FY12F	FY13F
Gross profit	26.3%	25.4%	28.4%	28.0%	27.5%
Pre-Tax	9.1%	11.1%	12.8%	13.1%	13.2%
Net Profit	8.5%	8.9%	10.3%	10.7%	10.8%

Growth	FY09	FY10	FY11	FY12F	FY13F
Revenue	-10.2%	10.8%	8.7%	10.0%	10.0%
Pre-Tax	-10.7%	34.5%	25.7%	12.5%	10.7%
Net Profit	3.5%	15.2%	26.6%	13.8%	10.7%
Tax rate	5.8%	17.9%	15.5%	15.5%	15.5%

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**Buy:** Share price may exceed 10% over the next 12 months

**Trading Buy:** Share price may exceed 15% over the next 3 months, however longer-term outlook remains uncertain

**Neutral:** Share price may fall within the range of +/- 10% over the next 12 months

**Take Profit:** Target price has been attained. Look to accumulate at lower levels

**Sell:** Share price may fall by more than 10% over the next 12 months

**Not Rated:** Stock is not within regular research coverage

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## DMG & Partners Research Pte. Ltd. (Reg. No. 200808705N)

Kuala Lumpur	Hong Kong	Singapore
<b>Malaysia Research Office</b> OSK Research Sdn. Bhd. 6 <sup>th</sup> Floor, Plaza OSK Jalan Ampang 50450 Kuala Lumpur Malaysia Tel : +(60) 3 9207 7688 Fax : +(60) 3 2175 3202	<b>OSK Securities Hong Kong Ltd.</b> 12 <sup>th</sup> Floor, World-Wide House 19 Des Voeux Road Central, Hong Kong Tel : +(852) 2525 1118 Fax : +(852) 2810 0908	<b>DMG &amp; Partners Securities Pte. Ltd.</b> 10 Collyer Quay #09-08 Ocean Financial Centre Singapore 049315 Tel : +(65) 6533 1818 Fax : +(65) 6532 6211
Jakarta	Shanghai	Phnom Penh
<b>PT OSK Nusadana Securities Indonesia</b> Plaza CIMB Niaga, 14th Floor, Jl. Jend. Sudirman Kav.25, Jakarta Selatan 12920, Indonesia. Tel : (6221) 2598 6888 Fax : (6221) 2598 6777	<b>OSK (China) Investment Advisory Co. Ltd.</b> Room 6506, Plaza 66 No.1266, West Nan Jing Road 200040 Shanghai China Tel : +(8621) 6288 9611 Fax : +(8621) 6288 9633	<b>OSK Indochina Securities Limited</b> No. 1-3, Street 271, Sangkat Toeuk Thla, Khan Sen Sok, Phnom Penh, Cambodia Tel: (855) 23 969 161 Fax: (855) 23 969 171
Bangkok		
<b>OSK Securities (Thailand) PCL</b> 191, Silom Complex Building 16th Floor, Silom Road, Silom, Bangrak, Bangkok 10500 Thailand Tel: +(66) 2200 2000 Fax : +(66) 2632 0191		