

## INITIATION REPORT

19 February 2011

## Kimlun Corporation Bhd

Price : RM1.77

Market Capitalization : RM405.3 mln

Board : Main Market

Sector : CONSTRUCTION

Recommendation : BUY

Bursa / Bloomberg Code: 5171 / KICB MK  
Stock is Shariah-compliant.

## Key Stock Statistics

FYE Dec	FY09	FY10f
EPS (sen)	13.8	15.8
P/E (x)	12.9	11.2
Net Div/Share (sen)	-	4.7
NTA/Share (RM)	0.67	0.80
Book Value/Share (RM)	0.67	0.80
Issued Capital (mln shares)	229.0	
52-week Hi-Low (RM)	0.865 - 1.85	
<b>Major Shareholders:</b>	<b>%</b>	
Pang Tin	40.4	
Pang Khang Hau	5.8	
Phang Fow	5.0	

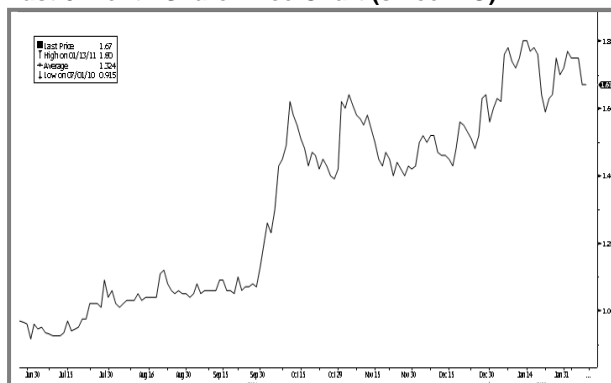
FY09 figures are on proforma basis.

## Per Share Data

FYE Dec	FY08	FY09	FY10f
Book Value (RM)	n/a	0.67	0.80
Cash Flow (sen)	11.5	15.5	15.8
Earnings (sen)	9.7	13.8	15.8
Net Dividend (sen)	-	-	4.7
Payout Ratio (%)	-	-	30.0%
PER (x)	18.3	12.9	11.2
P/Cash Flow (x)	15.5	11.4	11.2
P/Book Value (x)	n/a	2.6	2.2
Dividend Yield (%)	-	-	2.7%
ROE (%)	n/a	20.5%	19.8%
Net gearing	n/a	net cash	net cash

FY08 and FY09 figures are on proforma basis.

## Last 8-Month Share Price Chart (since IPO)



## Investment Highlights / Summary

- **Up and coming engineering and construction services provider** – Kimlun has steadily grown from a small-scale contractor to a full-fledged player capable of both complex building and infrastructure construction. Clientele comprises prominent property developers from public and private sectors, as well as international contractors.
- **Great potential in Industrial Building Systems (IBS).** Kimlun is also a capable IBS builder, complemented by its in-house precast concrete products manufacturing arm. It stands to benefit from the Government's push for more constructions using the IBS method.
- **Bright growth prospects ahead.** We expect Kimlun to be kept busy with the bustling construction activities in Iskandar Malaysia, and the expected rollout of major projects under the 10MP and ETP. Kimlun is a proven supplier of tunnel lining segments for the Singapore MRT projects and would be a likely candidate to supply similar products for our local MRT initiatives.
- **Healthy fundamentals.** Kimlun is in a net cash position post listing, enabling it to scale up operations with ease to meet rising demand. We project the Group to record double-digit earnings growth over the next two years riding on back of the construction boom.
- **Risks** include delays in the award of contracts by its clients and slow rollout of construction projects by the Government, as well as fluctuation in building materials prices.
- **Initiating coverage with a Buy recommendation and a fair value of RM2.02,** derived by pegging our FY11 EPS projection of 18.4 sen against a peer-benchmarked target PER of 11x. We like Kimlun for its i) promising earnings prospects, ii) healthy balance sheet, iii) proven delivery track record, and iv) reputable clientele from both private and public sector.

## Background

### Corporate profile.

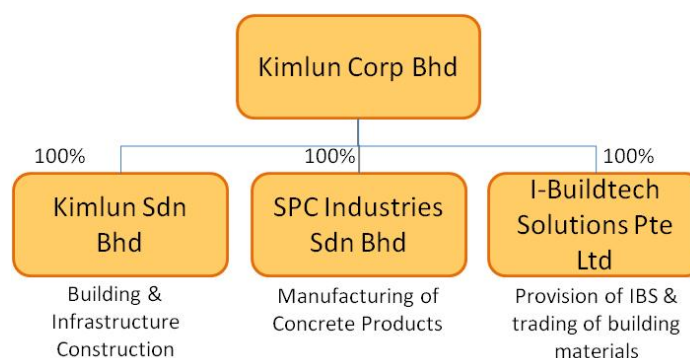
#### Engineering and construction services provider

Johor-based Kimlun Corporation Bhd (Kimlun) is an investment holding company, with its three wholly-owned subsidiaries primarily involved in the provision of engineering and construction services. In particular, the Group specializes in infrastructure and building construction, project management, industrial building systems and manufacture of precast concrete products. Kimlun was listed on the Main Market of Bursa Malaysia on 29 June 2010.

Kimlun Group was founded by two brothers, Mr. Pang Tin and Mr. Phang Piow in 1977 as a small-scale construction company handling projects with value of under RM20 mln. Over the years, it has steadily grown and by 2008, Kimlun moved up the value chain to undertake larger scale building and infrastructure construction with contract value in excess of RM100 mln each. To complement its construction arm, the Group also started manufacturing of concrete products in 2002.

Presently, Mr. Pang Tin sits on the board of directors as the Executive Chairman while Mr. Phang Piow serves as a Non-Independent Non-Executive Director. The position of CEO and Executive Director is helmed by a professional engineer, Mr. Sim Tian Liang. Out of the five Executive Directors, we note that three (including Mr. Sim) are professional managers with no family relationships to the founders.

### Corporate structure.



**Business.** Kimlun's core businesses are divided into two:- Engineering and Construction Services, and Manufacturing of Concrete Products.

#### Capable of both building and infrastructure construction

#### Engineering and Construction Services

Kimlun is a CIDB-registered Grade 7 contractor with the capability of undertaking construction of low and high-rise residential projects, commercial and industrial buildings, as well as infrastructure works such as flyovers, interchanges, roads and drainages. Priding itself as a one-stop centre, it also provides conceptual planning, design and engineering consultancy to its customers.

Between January 2006 and December 2009, the Group has recognized revenue of RM1.3 bln from its construction division. Given its strong foothold in Johor, most of the projects are in the southern Johor state although it has also completed projects in other places such as Selangor. Some of the notable projects completed by Kimlun in recent years include:-

**Notable completed projects**

Projects	Clients	Contract Value (RM mln)	Completion Year
1,500 units of Apartments, Nusajaya, Johor	Iskandar Regional Development Authority	142.8	2011
Perling Interchange, Johor	SP Setia Group	71.0	2008
Jusco Bukit Indah, Johor	WCT Group	35.0	2008
Carrefour Cheras, Selangor	Melati Ehsan Group	39.3	2009
438 houses at Sierra Perdana, Johor	Mah Sing Group	33.1	2009
Yongnam Factory, Nusajaya, Johor	Yongnam Group	13.4	2008

Source: Company

**Construction orderbook in excess of RM800 mln**

As at December 2010, the Group's outstanding construction orderbook is in excess of RM800 mln, and it has tendered for another RM600 mln worth of projects. We understand from management that historically, Kimlun's success rate is between 20%-25%.

Some of Kimlun's current major on-going projects are:-

Projects	Clients	Contract Value (RM mln)
<b>Building Projects</b>		
1,760 units of apartments & some commercial properties, Plentong, Johor	Tebrau Teguh Group	118.8
Marlborough College, Iskandar Malaysia, Johor	MRCB Group	70.0
2 blocks of 25-storey serviced apartments & ancillary buildings,	SP Setia Group	64.8
172 units of apartments & ancillary buildings, Nusajaya,	UEM Land	37.2
205 linked houses, Pulau, Johor	UEM Land	27.2
276 houses in Bandar Kangkar Pulau, Johor	Keck Seng	28.1
<b>Infrastructure Projects</b>		
Elevated Interchanges, JB Inner Ring Road, Johor	Iskandar Investment	124.1
Interchange at Pontian Link Expressway, Johor	Bandar Nusajaya Development	19.8

Source: Company

From the tables above, it is evident that Kimlun boasts a set of respectable clientele from both private sector, Government and Government-Linked Companies (GLC). Management noted that private sector and GLC clients contribute approximately 75% to construction revenue while the remaining comes from Government sector. We believe this is a good mix of clientele instead of being heavily dependent on Government projects.

### *Industrial Building Systems (IBS)*

A proponent of efficient building technologies, Kimlun has further ventured into IBS in 2009, having recognized the tremendous growth opportunities in this area. IBS is a modern construction technique in which components are manufactured in a controlled environment (on or off site), transported, positioned and assembled into a structure with minimal site works. Advantages from this technique include shorter construction time, improved site management and safety, reduced workforce requirement, and better quality from consistency in standardized forms of pre-cast concrete and prefabricated steel structures. All these factors lead to a more efficient and cost effective construction cycle.

#### **Secured RM260 mln of IBS projects within a 12-month period**

Within a year since venturing into IBS construction, Kimlun has secured two large IBS projects in Johor worth a combined RM260 mln:- i) the construction of 1,500 units of apartments in Nusajaya with contract value of RM142.8 mln; and ii) the construction of 1,760 units of apartments, some commercial properties and other ancillary buildings in Plentong with contract value of RM118.8 mln. The Group has successfully completed the construction of the 1,500 units of apartments in Nusajaya in January 2011 – which was a mere 16 months from commencement. By comparison, construction of high-rise apartments using conventional method may take between 30 and 36 months to complete.

Future project opportunities using IBS are abound, underpinned by i) our Government's mandate that IBS components to make up no less than 70% in all new Government buildings effective 2008, and ii) our Government's ongoing efforts to reduce dependency on foreign workers.

### **Manufacturing of Concrete Products**

#### **Manufactures both standard and custom-made precast concrete products**

Complementing Kimlun's construction division is the manufacturing arm, which produces both standard and custom-made precast concrete products. The table below lists some of the products manufactured by the Group:-

<b>Standard Precast Products</b>	<b>Customized Precast Products</b>
Reinforced precast concrete box culverts and U-shape drain	Reinforced precast concrete bathrooms
Reinforced concrete pipes culverts	Reinforced precast concrete tunnel lining segments
Reinforced concrete L-shape retaining walls	Reinforced precast concrete cladding pipes
Reinforced concrete manholes	Reinforced precast concrete jetty component

The bulk of sales from the manufacturing division are exported to Singapore. Most notably is Kimlun's precast concrete tunnel lining segments that are used for Singapore's Mass Railway Transit (MRT) network expansion. According to management, there are only a few players who have the capability to manufacture the precast concrete tunnel lining segments. And currently, there are three companies actively supplying the tunnel lining segments to the Singapore MRT projects. Apart from Kimlun, the other two are MTD ACPI Engineering Bhd and Hong Leong Asia Ltd. In the past, Kimlun had supplied precast concrete products for two hotels under the Resorts World Sentosa in Singapore, and precast concrete building components to some contractors in Singapore.

#### **Clients for concrete products are reputable international contractors**

Kimlun's clients for the precast concrete products consist of reputable international contractors such as Shimizu Corp. (Japan), Shanghai Tunnel Engineering (China), SK Engineering & Construction (South Korea) and McConnell Dowell South East Asia (Australia).

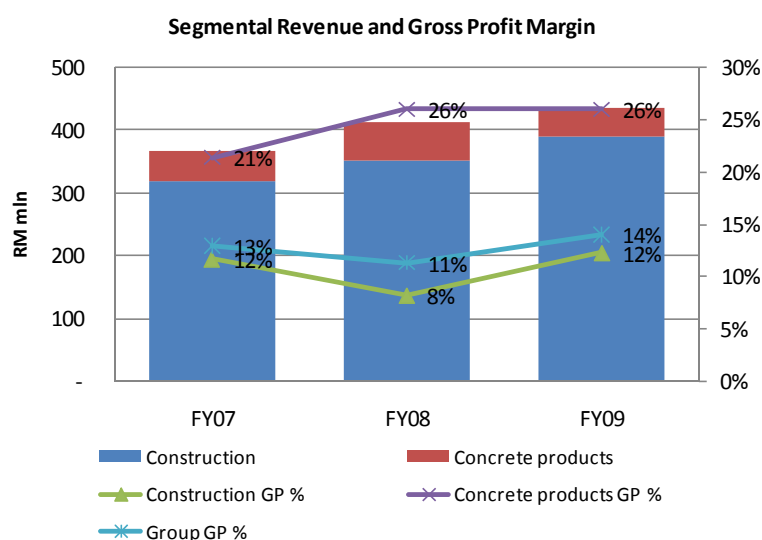
The group's current outstanding manufacturing orderbook is at circa RM80 mln, and has tendered for jobs worth some RM200 mln. For MRT tunnel lining segment tenders, management noted that the success rate is relatively high at approximately 70% due to small number of competent players capable of producing this product, as well as Kimlun's proven track record in meeting international contractors' requirements.

## Financial Highlights

### 2-year revenue and net profit CAGR of 8% and 11% respectively

On proforma basis, Kimlun registered a 2-year revenue and net profit CAGR of 9% and 11% respectively. The construction division contributes, on average, between 85%-90% of Group revenue with the remaining from the manufacturing business. Management expects the revenue mix to remain similar over the next few years.

In terms of segmental gross profit (GP) margin, the construction business recorded GP of between 8%-12% while manufacturing GP was much higher, in excess of 20%. We understand from management that the GP margin at the manufacturing arm was higher as the bulk of sales were customized precast concrete products that carry higher profit margins. At the Group level, the GP margin hovered between 11%-14% during the FY07-FY09 period.



In the current financial year, Kimlun achieved 9MFY10 revenue and net profit of RM374.6 mln and RM26.6 mln, which already reached 86% and 84% of FY09's turnover and net profit respectively. 9MFY10 net profit margin stood at 7.1%, which is consistent with the prior year's performance.

### Net cash position, with net cash per share of 32 sen

Following Kimlun's listing, the Group is on a strong financial standing backed by a healthy balance sheet. As at end-Sept 2010, it is in a net cash position, with net cash per share of 32 sen, while NTA per share is at 76 sen. To recap, the Group raised a total of RM62.1 mln from its IPO in June 2010, which will be progressively used for business expansions (inclusive of construction of new plant and purchase of machinery) and working capital needs.

## Earnings Outlook

Kimlun's earnings prospect over the next few years appears to be promising, underpinned by several positive catalysts both in Malaysia and in Singapore.

### Malaysia Market

#### To benefit from 10MP and ETP

We expect Kimlun to gain from the construction boom in the domestic market, arising from the increasing job flows under the 10<sup>th</sup> Malaysia Plan (10MP) and the Economic Transformation Programme (ETP). One particular area where we expect Kimlun to benefit is the implementation of the 150 km MRT project worth approximately RM36 bln. Given the Group's proven expertise in supplying precast tunnel lining segments to Singapore's MRT projects, we believe the chances of it securing jobs for the Malaysian MRT project are bright. Other major initiatives in which Kimlun may benefit include the development of the 3,000 acres of Rubber Research Institute of Malaysia land and the construction of hospitals and affordable housing under the 10MP.

#### Opportunities in Iskandar Malaysia

Meanwhile, there are also tremendous opportunities in the Iskandar Malaysia, Johor, where Kimlun already has an established presence and proven delivery track record. Some of the flagship developments in Iskandar Malaysia include the Danga Bay Integrated Waterfront City, EduCity at Nusajaya, Medini, Bio-Xcell Biotech Park, Puteri Harbour and Pinewood Iskandar Malaysia Studios. We note that in September 2010, Kimlun successfully clinched projects worth some RM70 mln for the construction of the UK's Marlborough College in EduCity.

### Singapore Market

#### Continues to supply tunnel lining segments for Singapore MRT projects

Across the straits, the construction industry in Singapore is thriving as well. Demand for construction services reached SGD25.7 bln in 2010 (+14% yoy) and may grow further to SGD28 bln in 2011. Public sector spending remains the driving force behind the boom, accounting for more than half of the demand. Apart from the construction of public housing, a major key driver would be the expansion of the MRT network in the city-state. We understand there are some 20 rail and related projects open for tender between end-2010 and 2Q2010. In the longer term, there is an estimated SGD50 bln worth of rail lines and expressway projects to be dished out over the next 10 years. We expect Kimlun to remain a key supplier of precast tunnel lining segments for the MRT expansion projects.

Other Singapore public initiatives that may benefit Kimlun include the expected increase in the use of NEWater (reclaimed water) to meet the city-state's water demand, which will lead to higher demand for the Group's precast jacking pipes, cladding pipes and tunnel segments.

### Earnings Prospects

#### Projects double-digit earnings growth in the next two years

Based on the current projects on-hand together with the expected orderbook replenishment, we forecast Kimlun to post double-digit earnings growth over the next two years. We estimate FY10 revenue and net profit at RM490.7 mln (+13% yoy) and RM36.2 mln (+5% yoy) respectively. For FY11, we estimate revenue to surpass the half-billion mark at RM559.5 mln (+14% yoy), accompanied by a projected 16% yoy increase in net profit to RM42.1 mln.

## Investment Risks

**Slow rollout of Government projects.** Kimlun's earnings growth may be dampened should our Government delays the rollout of the major infrastructure projects under the 10MP and ETP. Nevertheless, projects from the private sector as well as from Singapore would provide some earnings buffer.

**Delays in launches by private property developers.** Kimlun's earnings may be affected in the event i) Government introduces further measures to curb the rising property prices, and ii) banks tighten their credit-lending activities as these may result in property developers holding back new launches.

**Fluctuation in building materials prices.** As with other construction players, Kimlun is susceptible to fluctuations in the prices of building materials such as cement and steel. However, the Group mitigates this risk by having locked in the raw materials at pre-agreed prices with some of its suppliers when necessary and to have clauses in the agreement with certain clients allowing for contract value adjustments in the event of wild fluctuations in building materials prices. In any case, with Kimlun increasingly moving toward the IBS method, the risk of rising raw materials prices eroding profit margins reduce, as faster project completion time means shorter exposure to fluctuations in building materials prices. The undertaking of multiple smaller value building contracts, within any single year, over shorter construction period also helps to mitigate the risks being exposed to extended rising materials prices.

## Valuation

**Peer comparison** We have compared Kimlun against its peers in the construction and engineering sector, and in particular, those under RM500 mln market capitalization. From the table below, its peers are trading at an average PER of 11.6x.

Company	Curr	Share Price	PER (x)	P/BV (x)	Mkt Cap (mln)
Kimlun	RM	1.77	11.2	2.6	382.4
Ahmad Zaki	RM	1.10	11.3	1.3	304.4
Mitrajaya Holdings	RM	1.97	4.1	0.8	252.2
Fajarbaru Builder	RM	1.21	7.4	1.4	209.4
Bina Puri Holdings	RM	1.40	14.5	1.4	150.8
TRC Synergy	RM	1.43	26.5	0.9	272.4
Pintaras Jaya	RM	2.12	5.9	0.8	169.7
<b>Avg excl Kimlun</b>			<b>11.6</b>		

Source: Bloomberg, Company data

We have ascribed a peer-benchmarked target PER of 11x against our FY12 net profit forecast of RM42.1 mln (which translates into FY12 EPS of 18.4 sen) to arrive at our fair value of RM2.02. We note that with the Group intending to payout about 30% of net profit as dividend, the prospective net yield is relatively healthy at 2.7%.

## Recommendation

**BUY recommendation with fair value of RM2.02** We initiate our coverage on Kimlun with a **Buy** recommendation and a fair value of **RM2.02**, reflecting potential share price upside of 14%, backed by an expected net dividend yield of 2.7%.

We like Kimlun for its i) promising earnings growth prospects over the next few years, riding high on the back of the booming construction sector both in Malaysia and Singapore; ii) healthy balance sheet and net cash position, enabling the Group to scale up operations with ease to meet the rising demand for construction services; iii) proven delivery track record; and iv) reputable and diversified clientele from both the private and public sectors.

## P&L Summary

FYE Dec (RM mln)	FY08	FY09	FY10f	FY11f
Revenue	413.3	435.4	490.7	559.5
EBIT	32.0	45.2	51.5	59.9
Net Int Exp	(2.8)	(2.4)	(2.7)	(3.0)
Pre-tax Profit	29.2	42.8	48.9	56.9
Eff. Tax Rate	24.0%	26.4%	26.0%	26.0%
Net Profit	22.2	31.5	36.2	42.1
EBIT Margin (%)	7.8%	10.4%	10.5%	10.7%
Pre-tax Margin (%)	7.1%	9.8%	10.0%	10.2%
Net Margin (%)	5.4%	7.2%	7.4%	7.5%

Note: FY08 & FY09 figures are on proforma basis.

Source: Company, ZJ Research

## Balance Sheet Summary

FYE Dec (RM mln)	FY09	3QFY10
Total Assets	345.7	357.5
Non-Current Assets	59.5	23.3
Current Assets	286.2	334.2
Current Liabilities	185.7	177.0
Long Term Liabilities	6.4	6.1
Share Capital	114.5	114.5
Shareholders' Equity	153.5	174.4

Note: FY09 figures are on proforma basis.

Source: Company, ZJ Research

Analyst: Nicole Tan Yoke Ping ([nicole@zi.com.my](mailto:nicole@zi.com.my))

**RATING GUIDE**

BUY	Price appreciation expected to exceed 10% within the next 12 months
SELL	Price depreciation expected to exceed 10% within the next 12 months
HOLD	Price movement expected to be between -10% and +10% over the next 12 months from current level

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