

Kingsmen Creatives

PRICE S\$ 0.195
Buy
Key Stock Statistics

NRA EPS Est. 2004	3.4
P/E on NRA Est. 2004	5.7
NRA EPS Est. 2005	4.6
P/E on NRA Est. 2005	4.3
Dividend/Share	0.75
Dividend yield (%)	3.9
Shs. Outstg. (m)	101.09
Market capitalisation \$m	19.7
Avg. daily vol (m)	0.0351
Book Value/Share	0.12
Shareholders:	
Benedict Soh	25.3%
Simon Ong	25.3%

Per share data

Year:	2001	2002	2003	2004F	2005F
Book Value (S\$)	na	0.08	0.12	0.13	0.18
Cash Flow (cts)	na	3.6	2.0	4.1	5.3
Earnings (cts)	na	4.1	1.8	3.4	4.6
Dividend (cts)	na	na	0.75	1.0	1.0
Payout Ratio	na	na	38.7%	23.4%	17.4%
PER (x)	na	4.7	10.9	5.7	4.3
P/CF (x)	na	5.4	10.0	4.8	3.7
P/BV (x)	na	2.6	1.6	1.5	1.1
Dividend yield %	na	na	3.9%	5.1%	5.1%
ROE (%)	na	55.0%	12.5%	25.5%	25.5%

P&L analysis (\$m)

	2001	2002	2003	2004F	2005F
Revenue	45.26	60.84	53.48	71.01	82.27
Operating Profit	1.93	4.42	2.54	5.53	7.17
Depreciation	0.17	0.33	0.44	0.64	0.74
Interest Expense	0.08	0.06	0.08	0.20	0.30
Pretax Profit	1.99	4.25	2.13	5.18	6.93
Effective tax rate	26.9%	18.9%	25.7%	26.7%	25.6%
Net Profit	1.45	3.30	1.53	3.46	4.64

Margins

	2001	2002	2003	2004F	2005F
Gross	28.9%	26.6%	27.8%	28.2%	28.3%
Operating	4.3%	7.3%	4.7%	7.8%	8.7%
Pre tax	4.4%	7.0%	4.0%	7.3%	8.4%
Net	3.2%	5.4%	2.9%	4.9%	5.6%

Acquisition of IT network services company and Kingsmen Affiliates:

- Kingsmen is buying a 40% stake in Ascend Computer Rental that will enhance the group's position in providing integrated marketing communications services to clients.
- The cash payment of \$0.85m for Ascend will be made in four stages and on Ascend achieving minimum pretax profit for the next 3 years.
- The group is also acquiring 90% of Kingsmen Indochina, 25% of Kingsmen Korea and 30% of Kingsmen Nikko. Total purchase consideration is \$3.17m of which \$2.942m will be paid in cash and the remaining through issue of 1.094m new shares at \$0.21 each.
- The acquisition price of the three Kingsmen Affiliates is a good 25% discount compared to appraised valuation.
- Both acquisitions take effect retrospectively from 1 Jan 04 and will have a positive impact on FY04 earnings.
- The stock is currently at very low forward PE multiples of 4-6x. We are maintaining our Buy rating.

Acquisition of Ascend Computer

Kingsmen has signed an agreement to acquire a 40% stake in Ascend Computer Rental Pte Ltd for \$850,000.

Ascend's expertise lies in providing IT network services for events such as conferences, seminars and exhibitions and therefore will be a good fit to Kingsmen's business operations.

The acquisition will be funded internally. The total consideration is payable in four stages with the first payment of \$366,750 to be made on the date of Agreement and subsequent payments made on condition of Ascend achieving minimum pretax profit of \$450,000 for FY04, \$1.6m for FY04 and FY05 and \$2.4m for FY04, FY05 and FY06.

Based on the audited net profits attributable to the 40% stake acquired of \$103,082 for the 6-month period ended 31 Dec 03, total consideration for the acquisition works out to a net PER of 4.1x which is reasonable.

Moreover, the group is anticipating strong growth for Ascend. As a 40% associate, its contribution will be equity accounted in the group.

Acquisition of Kingsmen Affiliates

The group has entered into a conditional Share Acquisition Agreement to acquire 90% of Kingsmen Indochina, 25% of Kingsmen Korea and 30% of Kingsmen Nikko which operate similar business to Kingsmen Creatives, that is, three-dimensional communication design and production in Vietnam, Korea and Japan respectively.

Under the first conditional agreement, Kingsmen will acquire 80% of Kingsmen Indochina, 25% of Kingsmen Korea and 30% of Kingsmen Nikko with \$2.942m cash. Under the second conditional agreement, Kingsmen will acquire another 10% of Kingsmen Indochina with the allotment and issuance of 1.094m new shares at an issue price of \$0.21. Total purchase consideration is \$3.17m. The cash consideration will be funded by the proceeds from the IPO.

Comparing the appraised value of the Kingsmen Affiliates under the first share acquisition agreement of \$3.9155m with the cash payment of \$2.942m, Kingsmen is making the 3 acquisitions at a 25% discount to their combined appraised valuation.

The proposed acquisition is a strategic step to strengthen its presence in Asia by leveraging on the Kingsmen International global network. As mentioned in our initiation coverage of the company, the management had planned on acquiring shares of the Kingsmen Affiliates when any of them become sufficiently profitable. Next on the acquisition list would probably be the fast-growing Greater China affiliates, comprising Hong Kong, Taiwan and the PRC, in FY05.

Financial Impact

Both acquisitions take effect retrospectively from 1 Jan 04 and will have a positive impact on earnings. These moves exhibit prudence by management in deploying its IPO proceeds of \$4.7m.

The conditional agreement with Ascend imposed a minimum profit guarantee for the next 3 years and therefore requiring Ascend to deliver strong growth during the period.

Contribution of Kingsmen Indochina as a 90%-owned subsidiary will be consolidated in the group while Kingsmen Korea and Kingsmen Nikko will be equity accounted as associates. Net profit before tax and after tax attributable to the assets acquired were \$0.7m and \$0.53m respectively during FY03. The acquired companies' strength is at par with the group. Gross profit margins for Vietnam, Japan and Korea ranged from 23-30% compared with the group's 28% in FY03. Growth rates of at least 10% are expected. Japan and Korea are recovering from economic recession and the Vietnam will continue to benefit from increased foreign investments.

As a result of the issue of 1.094m new shares for an additional 10% of Kingsmen Indochina under the second conditional agreement, share capital will increase slightly from 100m shares to 101.1m shares.

We are revising our earnings forecast slightly higher. The stock is trading at very low forward PE multiples of 4-6x and we are reiterating our buy rating.

Revised Earnings Forecast (\$m)

Year ended 31 Dec	2001	2002	2003	2004F	2005F
Turnover	45.3	60.8	53.5	71.0	82.3
Cost of sales	(32.2)	(44.6)	(38.6)	(51.0)	(59.0)
Gross Profit	13.1	16.2	14.9	20.0	23.3
Other income	1.1	0.5	1.0	1.2	1.3
Operating expenses	(12.4)	(12.6)	(13.8)	(16.3)	(18.1)
Financial expenses	(0.1)	(0.1)	(0.1)	(0.2)	(0.3)
Financial income	0.3	0.2	0.1	0.1	0.1
Share of profits of associates	-	-	-	0.4	0.7
Pretax profit	2.0	4.3	2.1	5.2	6.9
Taxation	(0.5)	(0.8)	(0.6)	(1.4)	(1.8)
Aftertax profit	1.5	3.5	1.6	3.8	5.2
Minority interest	-	(0.2)	(0.1)	(0.3)	(0.5)
Net Profit	1.5	3.3	1.5	3.5	4.6
EPS(cts)	na	3.3	1.5	3.4	4.6

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