



# Kingsmen Creatives Ltd

**AmFraser**

*Growing pains*

(Bloomberg: KMEN SP)

**BUY**

(Maintain)

LAST CLOSE: S\$0.725

FAIR VALUE: S\$0.85

(Previous : \$0.87)

Monday, 21 January 2012

Rationale for report: Company Update

## Financials

YE Dec (S\$m)	2011	2012F	2013F	2014F
Revenue	261.0	291.0	336.1	376.4
Gross Profit	66.7	74.8	87.0	96.8
Pre-Tax Profit	19.8	21.2	24.2	27.1
PATMI	16.3	16.8	19.1	21.5
EPS (S cents)	8.52	8.78	9.99	11.22
DPS (S cents)	4.00	4.00	4.50	5.00
PER (x)	8.51	8.26	7.26	6.46
Div Yield (%)	5.5	5.5	6.2	6.9

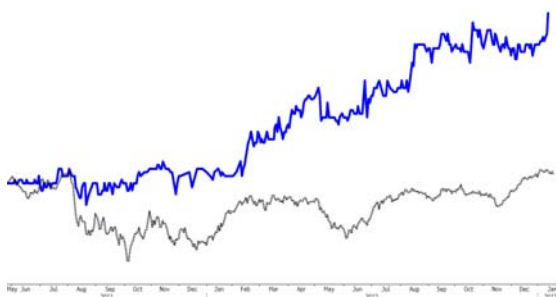
## Key Operating Statistics

	2011	2012F	2013F	2014F
Gross Margin (%)	25.5	25.7	25.9	25.7
Net Margin (%)	6.3	5.8	5.7	5.7
ROE (%)	24.4	22.0	21.7	21.2
ROA (%)	11.5	10.4	10.7	10.5
Net Gearing (%)	Net cash	Net cash	Net cash	Net cash
EV/EBITDA (x)	5.21	3.96	3.20	2.49

## Stock Data

Issued Shares (m)	191.60
Market Cap (S\$m)	138.91
Major Shareholders	Benedict Soh (19.98%) Simon Ong (19.98%)
Free Float	39.00%
52 week lo / hi	\$0.50 / \$0.805

## 12-Month KMEN SP vs. FSSTI



Source: Bloomberg

Kingsmen Creatives released an announcement last Friday pertaining to accounting irregularities found in two subsidiaries—Kingsmen Beijing Co. Ltd (KBJ), a 92.2%-owned subsidiary, and Kingsmen Exhibits Pte. Ltd. (KE), a wholly-owned subsidiary of Kingsmen. The net financial impact to Kingsmen Creatives is a loss of S\$29,000 and S\$1.46mil respectively. After a meet-up with management, we assess Kingsmen's management integrity and operational soundness to be intact. In fact, we think the 7% share price correction last Friday now provides investors with a timely entry point. Maintain **BUY** with fair value of **S\$0.85**.

**What transpired?** 1) The incident at KBJ involved a misappropriation of funds by four employees, resulting in a net unrecoverable loss of RMB146,835, or ~S\$29,000. The loss is likely to have been incurred at the end of FY2012. 2) The second incident at KE involved a larger amount of a net charge of S\$1.46mil to Kingsmen from a commercial settlement agreement between KE and a subcontractor. It has yet to be determined if the charge will be adjusted retrospectively or prospectively, as the audit of KE is still on-going. 3) Kingsmen intends to undertake a review of its internal controls and to develop a comprehensive Group Risk Assurance Framework to enhance its internal control and risk management process.

## Key Impact

- Impact to earnings: S\$29,000 and S\$1.46mil from the two incidents. It has yet to be determined which FY Kingsmen will park the charges under, but when adjusted retrospectively it has no impact to FY13F earnings and our valuation using the PER method (8.5x FY13F EPS).
- There is an immediate impact to cash flow from operations. However, we expect DPS of 4c for FY12 to stay intact.
- We estimate the audit review exercise to cost S\$0.5mil, and have included this in our FY13F estimates. FY13F EPS is reduced to 9.9c, down from previous estimates of 10.2c.

**Maintain BUY; FV of S\$0.85.** We view the incidents as part of Kingsmen's growing pains. It has expanded ferociously—from making just S\$76mil of revenues in FY05 to S\$261mil in FY11, a whopping 36% CAGR. Despite this hiccup, we continue to like Kingsmen's business fundamentals and have assessed Kingsmen's operational soundness and management integrity to be intact.

Our FV of Kingsmen now stands at S\$0.85, an 8.5x FY13F EPS of 9.9c, a slight drop from S\$0.87 after factoring in audit review expenses. We see earnings visibility ahead through its pipeline of store roll-out and themepark contracts over the next few years. In addition, Kingsmen still offers a 5.5% yield based on last close. Investors should be buying into a Kingsmen that has a stronger internal control and governance culture after this incident, as they continue to grow in the region and outgrow their growing pains.

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## YE 31 Dec

<b>INCOME STATEMENTS S\$mil</b>	<b>2010</b>	<b>2011</b>	<b>2012F</b>	<b>2013F</b>	<b>2014F</b>
<b>Revenue</b>	<b>235.2</b>	<b>261.0</b>	<b>291.0</b>	<b>336.1</b>	<b>376.4</b>
Cost of Sales	-169.8	-194.3	-216.2	-249.1	-279.6
<b>Gross Profit</b>	<b>65.4</b>	<b>66.7</b>	<b>74.8</b>	<b>87.0</b>	<b>96.8</b>
Staff salaries & related expenses	-35.4	-37.9	-42.2	-49.1	-55.0
Other expenses	-11.6	-12.0	-12.1	-14.6	-15.5
Other income	2.7	3.9	2.7	2.7	2.7
Depreciation	-1.6	-1.5	-2.1	-2.0	-2.1
<b>Profit from Operations</b>	<b>19.5</b>	<b>19.2</b>	<b>21.1</b>	<b>24.0</b>	<b>27.0</b>
Interest income	0.2	0.2	0.2	0.2	0.2
Interest expense	-0.1	-0.2	-0.2	-0.2	-0.2
<b>Profit before Tax</b>	<b>19.7</b>	<b>19.8</b>	<b>21.2</b>	<b>24.2</b>	<b>27.1</b>
Income Tax	-3.5	-3.1	-3.8	-4.3	-4.9
Non-controlling interests	1.1	0.4	0.6	0.7	0.8
<b>PATMI</b>	<b>15.1</b>	<b>16.3</b>	<b>16.8</b>	<b>19.1</b>	<b>21.5</b>
EBITDA	21.2	20.7	23.2	26.0	29.1
Free Cash Flow	14.3	10.8	24.3	16.7	20.2
Earnings per Share (S cents)	7.93	8.52	8.78	9.99	11.22
Dividends per Share (S cents)	4.00	4.00	4.00	4.50	5.00
Book Value per Share (S cents)	31.28	36.59	41.57	47.83	54.87
<b>BALANCE SHEETS S\$'000</b>	<b>2010</b>	<b>2011</b>	<b>2012F</b>	<b>2013F</b>	<b>2014F</b>
Cash and Cash Equivalents	29.9	33.2	49.2	57.5	68.4
Trade and Other Rec	75.3	95.3	93.2	107.6	120.6
Inventory	0.14	0.06	0.18	0.20	0.23
Property, Plant, Equipment	11.9	11.2	9.6	10.1	10.5
Other Current Assets	15.1	12.8	18.6	21.3	23.5
Other Long-term Assets	13.2	14.5	14.3	14.3	14.3
<b>Total Assets</b>	<b>145.6</b>	<b>167.1</b>	<b>185.1</b>	<b>211.0</b>	<b>237.4</b>
Trade Payables	37.7	40.8	48.0	55.3	62.0
Borrowings: Non-Current	1.9	2.1	2.0	1.9	1.8
Other Current Liabilities	45.3	53.8	55.2	62.1	68.5
Other Long-term Liabilities	1.3	0.9	0.9	0.9	0.9
Total Common Equity	57.1	66.9	76.3	88.2	101.6
<b>Total Liabilities and Equity</b>	<b>145.6</b>	<b>167.1</b>	<b>185.1</b>	<b>211.0</b>	<b>237.4</b>

<b>CASHFLOW STATEMENTS \$'000</b>	<b>2010</b>	<b>2011</b>	<b>2012F</b>	<b>2013F</b>	<b>2014F</b>
Profit before Tax	19.7	19.8	21.2	24.2	27.1
Depreciation	3.6	3.4	4.1	2.0	2.1
Change in Working Capital	-0.6	-6.4	5.0	-2.8	-1.9
Income Tax Paid	-3.3	-3.1	-3.8	-4.3	-4.9
<b>Net Cash from Operations</b>	<b>20.3</b>	<b>13.6</b>	<b>26.6</b>	<b>19.0</b>	<b>22.5</b>
(Purchase)/Disposal of PPE	-6.2	-2.8	-2.5	-2.5	-2.5
Other Cash from Investing	-3.6	0.0	0.0	0.0	0.0
(Repayment of debt/finance lease)	-1.8	0.0	-0.3	-0.3	-0.3
(Dividends Paid)	-7.0	0.0	-7.9	-7.9	-8.9
Other Cash from Financing	6.8	0.0	0.0	0.0	0.0
<b>Beginning Cash</b>	<b>20.3</b>	<b>28.0</b>	<b>24.3</b>	<b>40.3</b>	<b>48.6</b>
Foreign Exchange Effect	-0.92	0.51	0.00	0.00	0.00
<b>End Cash</b>	<b>28.0</b>	<b>31.6</b>	<b>40.3</b>	<b>48.6</b>	<b>59.5</b>

\*Ending cash differs from balance sheet cash due to fixed deposits, overdrafts, restricted balances and other items

<b>KEY RATIOS</b>	<b>2010</b>	<b>2011</b>	<b>2012F</b>	<b>2013F</b>	<b>2014F</b>
<b>Profitability</b>					
Gross Margin (%)	27.8	25.5	25.7	25.9	25.7
EBITDA Margin (%)	9.0	7.9	8.0	7.7	7.7
Net Margin (%)	6.4	6.3	5.8	5.7	5.7
ROE (%)	26.4	24.4	22.0	21.7	21.2
ROA (%)	11.7	11.5	10.4	10.7	10.5
<b>Growth (Y-o-Y)</b>					
Revenue (%)	-2.8	11.0	11.5	15.5	12.0
EBITDA (%)	4.0	-2.1	11.9	12.3	11.8
Pre-Tax Income (%)	4.3	0.4	7.1	13.9	12.3
Net Income (%)	3.0	3.5	3.8	13.9	12.3
<b>Financial Structure</b>					
Debt/Equity	0.09	0.07	0.06	0.05	0.04
Net Gearing (%)	-41.5	-40.3	-56.0	-58.2	-61.4
<b>Operational Efficiency</b>					
Days Sales in Receivables	106.9	124.0	107.0	107.0	107.0
Days in Inventory	0.30	0.12	0.30	0.30	0.30
Days in Payables	80.98	76.56	81.00	81.00	81.00
Cash Conversion Cycle	26.2	47.5	26.3	26.3	26.3
Asset Turnover (x)	1.62	1.56	1.57	1.59	1.59
<b>Market Valuation</b>					
Price / Earnings	9.14	8.51	8.26	7.26	6.46
Price / Book	2.32	1.98	1.74	1.52	1.32
Price / Sales	0.59	0.53	0.48	0.41	0.37
Price / Free Cash Flow	0.05	0.07	0.03	0.04	0.04
EV / EBITDA	5.25	5.21	3.96	3.20	2.49

AmFraser Research recommendations are based on a Total Return rating system, defined as follows:

**BUY:** >15% total return over the next 12 months

**HOLD:** -15% to +15% total return over the next 12 months

**SELL:** <-15% total return over the next 12 months

Total Return includes share price appreciation (depreciation) + dividends

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