

Natural Cool Holdings Ltd

Company Visit Update

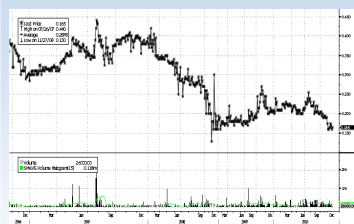
Maintain BUY

Current Price S\$0.170
20 December 2010

Fair Value S\$0.235

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Historical Chart



Source: Bloomberg

Stock Statistics

Market Cap	S24.4m
52-HI	S\$0.255
52-LOW	S\$0.155
Avg Vol (1 yr)	48,618
Shares	143.4m
Outstanding	
Free Float	77.6m

Key Indicators

ROE	-1.8%
ROA	-0.4%
P/BK	0.73x
Gearing	1.27x

Major Shareholders

Ang Choon Cheng	12.07%
Chen Choon Khee	10.84%
Tsng Joo Peng	8.05%
Ecube Electric Pte Ltd	5.86%

Growth underpinned by strong construction pipeline

- Return to profitability in FY10.** After incurring losses in FY09, Natural Cool (NC) is expected to return to profitability in FY10. An exceptional gain of S\$9.5m from the sale & leaseback of 29 Tai Seng Place expected in 2HFY10 and the disposal of loss-making building materials division in FY09 will lift FY10 bottomline. FY10 to FY12 growth will also be underpinned by core business expansion in the switchgear business through newly acquired Titans Power Holdings Group (Titans) and strong construction demand. The aircon business will also benefit from domestic real estate boom.
- Strengthened balance sheet.** Cash proceeds of S\$53m from the sale & leaseback of 29 Tai Seng Place will allow NC to meet a property loan obligation of about \$19.7m attached to property and improve the firm's gearing. There is also the likelihood that management will return part of the proceeds to shareholders.
- Benefit from strong construction pipeline.** NC has a market share of about 85% of all HDB upgrading works in Singapore. The ongoing upgrading work plans by HDB will benefit NC with a flow of projects in light of proven track record and relationship with the Town Council. Government efforts to provide more public housing to meet increasing public and private demand also augur well for NC. HDB will ramp up the supply of new public flats from about 23,000 in 2010 to another 30,000 flats in 2011 if strong home demand persists. Simultaneously, the government land sale (GLS) program will also yield about 13,900 and 14,300 new homes under the 2H2010 and 1H2011 GLS program respectively. The strong construction pipeline over the next three to five years will underpin growth for NC, which derives about 94% of its revenue from the local construction industry.
- Listing switchgear business on GEM in Hong Kong; likely to command higher valuations.** There are plans to spin off the switchgear business into a wholly owned subsidiary, Gathergates Holdings, with the intention of listing the firm on the Growth Enterprise Market (GEM) in Hong Kong. The proposed listing will raise funds for the Group's future expansion plans in Asia and address the liquidity issue of NC shares. Management is awaiting approvals from the stock exchanges in Hong Kong and Singapore and listing is likely to take place in 1HFY2011.
- Valuations and Recommendations.** Taking into account an enhanced valuation on the switchgear business through the GEM listing, we value the switchgear and aircon businesses at PER of 14x (FY11F) and 5x (FY11F) respectively, translating to a fair value of S\$0.235. This represents a 38% upside. **Maintain BUY.**

Key Financial Data (mil)					
YE: 31 Dec	FY08	FY09	FY10F	FY11F	FY12F
Sales	107.9	123.7	132.6	137.0	141.8
Gross Profit	25.4	29.5	29.5	28.1	29.5
Net Profit	2.3	-0.5	8.3	2.7	2.9
EPS (cents)	2.0	-0.4	5.8	1.6	1.7
EPS growth (%)	-42.0%	n.m.	n.m.	-71.4	5.7%
PER	8.7	n.m.	2.9	10.3	9.7
DPS (cents)	0.0	0.0	0.0	0.0	0.0
Div Yield (%)	0.0%	0.0%	0.0%	0.0%	0.0%

Source: Company, NRA estimates

Company Update

Switchgear Division

Support 85% of HDB upgrading works. The switchgear division distributes low-voltage switchgear products to the public and private sectors of the real estate market. The Group is particularly strong in the public housing market and supports 85% of all HDB upgrading works in Singapore. With 590 blocks in 58 Housing Board sites islandwide picked for improvement works by the Housing Board under the new upgrading scheme (announced in February 2008), the ongoing upgrading works augurs well for NC, providing the firm with a steady flow of projects in light of proven track record and relationship with the Town Council.

Expected strong construction pipeline will underpin growth. Increasingly, NC also supports new HDB projects, private housing and commercial projects. To meet increasing demand from first-time home-buyers for HDB flats, HDB will be releasing more public housing. Simultaneously, the government will also increase the supply of government land sites for private homes to ensure a stable private property market. The expected strong construction pipeline over the next three to five years will underpin growth for NC, which is currently, the second largest player in the switchgear industry. Some of the firm's recent project involvements include HDB project, HDB The Pinnacle @Duxton and condominium projects at Jalan Kechil, Upper Serangoon Road and Icon. Significant commercial project involvements include Shanghai Stock Exchange building in Shanghai (PRC), Overseas Union House and Change Alley Aerial Plaza at Collyer Quay. NC is also awaiting results for the award of projects including the Marine Life Park at Resorts World Sentosa.

Has capability to support mega projects. NC's acquisition into Titans Power Holdings (Titans) in June 2009 has enabled NC to manufacture and distribute a wide range of low voltage switchgear products, which are commonly used in residential and commercial projects. These included winning a S\$7mil contract to supply and deliver low voltage switchboards to Resorts World at Sentosa, which was successfully completed in early 2010.

Since early 2009, NC has shifted the switchgear manufacturing operations from Singapore to Malaysia. The lower costs of operation in Malaysia will further help sustain the division's gross profit margin of about 20%.

NC also has distribution rights on switchgear products of third-party brands including Larsen and Toubro, Hyundai and KAM, to cater to customer needs and to provide the firm with higher competitive edge in the switchgear industry.

Listing switchgear business in Hong Kong; likely to command higher valuations. NC is planning to spin off the switchgear business into a wholly owned subsidiary, Gathergates Holdings (GG), with the intention of listing the firm on the Growth Enterprise Market in Hong Kong. The proposed listing will raise funds for the Group's future expansion plans in Asia and address the weak liquidity of NC shares. Management is awaiting approvals from the stock exchanges in Hong Kong and Singapore and listing is likely to take place in 1HFY2011.

Aircon Division

Retail customers and trading business offer regular cash flow. The aircon division is expected to enjoy healthy growth from aircon installation and maintenance & repair services from retail customers as well as trading of aircon systems and spare parts with trading partners on the back of healthy domestic economic growth. These customers generally have good credit standing, providing regular cash flow to NC. However, contributions from these customers are volatile, as retail customers are quick to scale back non-essential expenditures while business activities of trading partners slow down, when the general economic conditions deteriorates.

Longer-term commercial projects provide more stable revenue. In addition, NC provides aircon systems installation services and integrated project (IP) services for commercial projects such as factories, offices, schools, etc. As the typical contract term of IP services are longer, it provides NC a relatively stable source of revenue. One of the IP services involves infrastructure maintenance of aircon, lifts, etc for NTU.

Margins from this division tend to be relatively stable in the region of 20%.

Property-related deals

Disposal gain of S\$9.5m expected in 2HFY10. NC completed the sale & leaseback of 29 Tai Seng Place in August 2010 to Mapletree Logistics Trust for a consideration of S\$53.0m. Under the deal, NC will leaseback the property for a duration of 10 years at an annual rent of between S\$4.5m to S\$5.3m to house its operations at the premises. Also, NC is expected to recognise a one-off disposal gain of about S\$9.5m in 2HFY10.

Impact on cash flow is minimal. Currently, NC occupies about 25% of the premise, which enjoys 95% occupancy rate, and sub-leases out the remaining floor space to third-party tenants. As the sub-leased rental revenue partially offsets the rental NC incurs through the sale & leaseback arrangement, the impact on cashflow is not significant.

Strengthened balance sheet. The disposal cash proceeds of S\$53m will allow NC to meet a property loan obligation of about \$19.7m attached to Tai Seng Place and improve the firm's gearing.

Further, NC is expected to conclude the disposal of 20 Benoi Crescent, a two-storey detached factory, for a consideration of S\$11.8m by 1QCY2011. The deal will be positive on cash flow and is expected to result in disposal gains of about \$94,000 in 1HFY11.

Profit & Loss					
YE 31 December (S\$m)					
	2008A	2009A	2010F	2011F	2012F
Revenue	107.9	123.7	132.6	137.0	141.8
Cost of Sales	(82.5)	(94.3)	(104.5)	(108.3)	(112.3)
Gross Profit	25.4	29.5	28.1	28.8	29.5
Operating Income	2.4	2.0	10.7	2.2	2.3
Administrative expenses	(13.7)	(19.3)	(19.6)	(20.3)	(20.9)
Marketing & distribution exp.	(5.0)	(5.6)	(5.8)	(6.0)	(6.2)
Other operating expenses	(3.1)	(1.5)	(1.2)	(0.2)	(0.3)
Accreditation of negative goodwill	-	-	-	-	-
Operating Profit	6.0	5.1	12.2	4.5	4.4
Net interest	(1.8)	(3.0)	(2.5)	(1.4)	(1.1)
Exceptional Items	-	-	-	-	-
Profits from Associated Co.	-	-	-	-	-
Pre-tax Profit	4.1	2.1	9.7	3.1	3.4
Income tax	(1.4)	(1.0)	(1.7)	(0.5)	(0.6)
Loss from discontinued operations	(0.4)	(1.8)	-	-	-
Minority Interests	0.0	0.3	0.2	0.2	0.1
Net Profit	2.4	(0.5)	8.3	2.7	2.9

Source: Company, NRA estimates

Balance Sheet					
YE 31 December (S\$m)					
	2008A	2009A	2010F	2011F	2012F
Cash & Fixed Deposit	4.8	8.0	39.6	57.3	56.9
Trade Receivables	43.0	38.1	40.0	41.7	43.5
Inventory	18.9	18.6	20.0	22.2	22.8
Other current assets	30.9	-	-	-	-
Current Assets	97.6	64.7	99.6	121.2	123.2
Property, Plant and Equipment	17.0	48.4	15.7	15.2	14.5
Investment properties	14.4	12.7	12.4	0.7	0.7
Others	1.2	3.9	3.9	3.9	3.9
Non-current Assets	32.6	65.0	32.0	19.8	19.1
Bank Borrowings	27.0	7.1	6.5	5.8	5.3
Trade Payable	57.1	47.3	51.5	54.9	57.9
Others	1.1	1.0	0.9	8.2	7.4
Current Liabilities	85.3	55.4	58.9	68.9	70.5
Bank Borrowings	14.7	41.1	19.0	17.1	15.4
Others	1.1	1.0	13.5	12.2	10.8
Non-current Liabilities	15.9	42.1	32.5	29.3	26.2
Shareholder's Equity	29.1	32.1	40.2	42.8	45.6

Source: Company, NRA estimates

Cash Flow					
YE 31 December (S\$m)					
	2008A	2009A	2010F	2011F	2012F
Cash flow from Operating activities					
Pre-tax profits	2.3	(0.8)	9.7	3.1	3.4
Adjustments	5.1	7.0	(3.4)	1.7	1.8
Operating cash flow before working capital	7.4	6.2	6.3	4.8	5.1
Changes in working capital	(5.4)	4.0	0.9	(0.6)	0.6
Tax paid & others	(0.4)	(1.0)	(1.7)	(0.5)	(0.6)
Net cash generated from operations	1.6	9.2	5.5	3.7	5.2
Cash flow from investing activities					
Acquisition of subsi., net of cash	0.0	0.4	2.0	2.2	1.5
Proceeds from disposals	1.4	2.5	54.1	11.8	-
Others	(33.4)	(11.0)	(3.1)	(2.6)	(2.5)
Net cash from investing activities	(31.9)	(8.1)	53.1	11.4	(0.9)
Cash flow from financing activities					
Loans	29.7	8.8	(27.0)	0.4	(2.3)
Others	0.0	(3.7)	(1.5)	0.6	(1.5)
Net cash from financing activities	29.7	5.1	(28.5)	1.0	(3.8)
Net change in cash	(0.5)	6.2	30.1	16.1	0.4
Cash balance at beginning of year	0.2	(0.3)	7.9	39.5	57.2
Other adjustments	1.5	1.9	1.6	1.5	(0.8)
Cash balance at end of year (net of OD & adjms)	(0.3)	7.9	39.5	57.2	56.8

Source: Company, NRA estimates

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