

CW Group

One-stop precision engineering solutions provider

to summarize...

- One-stop precision engineering solutions provider headquartered in Singapore
- Strong alliance with leading players KIWA from Japan & DMPG from Germany
- Precision engineering solutions to expand on increased capital since 2012
- Manufacturing business growth in 2013F largely on CNC sales to DMPG
- Core P/E 12.0x for FY12/12A based on HK\$104.7m adjusted net profit

One-stop precision engineering solutions provider headquartered in Singapore. CW Group is a Singapore-headquartered precision engineering solutions provider. As of FY12/12A, around 49% of the group turnover was attributed to precision engineering turnkey solutions. Customers are of international scale from a wide range of industries including aerospace, oil and gas, energy and automotive, including Honeywell, Rolls-Royce, Hamilton Sundstrand and HP. Management indicates that CW Group is a well-positioned turnkey provider that sources equipment from both top-tier and lower-tier equipment suppliers to provide customized solutions in accordance to customer needs, maintaining a balance between total cost and production performance. With key knowhow in precision engineering, CW Group also provides its own range of CNC machining centres and cement production equipments, which contributed 15% and 12% sales in 2012A. Table 1 shows sales breakdown by business segments and margins for 2011A-12A. CW Group was listed on HKEx main board in Apr 2012 at HK\$1.33 per share.

Table 1. Sales breakdown and segment margins

HK\$m	2011A	2012A	Segment margin
Total sales	753.6	818.5	
Precision engineering solutions	351.8	401.3	15% - 25%
Manufacturing and trading			
- Sales of CNC machining centres	71.5	124.6	15% - 25%
- Sales of cement production equipment	159.0	101.8	40% - 50%
- Sales of components and parts	150.8	106.4	5% - 15%
After-sales support service	20.5	86.9	50%+

Source: SBI E2-Capital

Strong alliance with leading players KIWA from Japan & DMPG from Germany. CW Group has strategic relationships with KIWA and DMPG. CW established a JV with KIWA named "KIWA-CW" in Singapore in 2005. In the Shanghai manufacturing base, key products produced are the CNC machining centres under the JV brand name. As for DMPG, CW Group OEM components and parts for certain product series of DMPG CNC machining centres which are then sent to DMPG factory for final processing. A separate facility in Shanghai, CW Group was achieving increasing sales from DMPG since 2H 2012. Contribution of these sales is reflected in the "sales of components and parts" segment. Table 2 shows current production facility location in China.

Table 2. Production facility in China

Brand	Product	Location
KIWA-CW	CNC machining centres	Plant 1, Minhang, Shanghai
OEM of DMPG	CNC machining centres	Plant 2, Minhang, Shanghai
Self-brand	Cement production equipment	Beichen, Tianjin

Source: SBI E2-Capital

Ticker	1132 HK
Rating	Not Rated
Price (HK\$)	2.04
Target Price (HK\$)	n.a.
12m Price Range (HK\$)	1.25 - 2.11
Market cap. (US\$m)	161.2
Daily t/o (US\$m)	0.61
Free float (%)	20.8

Financial summary

Year to Dec	10A	11A	12A
Turnover (HK\$m)	469.5	753.6	818.5
Re. Net Profit (HK\$m)	50.6	68.0	55.1
Re. EPS (HK\$)	-	0.1458	0.0957
P/E (x)	24.9	18.5	22.8
P/B (x)	8.8	5.8	2.2
EV/EBITDA (x)	11.6	10.5	9.7
Yield (%)	-	-	-
ROE (%)	35.5	31.3	9.7
ROCE (%)	48.9	38.9	14.7
N. Gear. (%)	N.Cash	11.0	N.Cash

Source: SBI E2-Capital

	12F	13F	14F
Consensus EPS (HK\$)	-	-	-
Previous earnings (HK\$m)	-	-	-
Previous EPS (HK\$)	-	-	-

Price performance

Year to Dec	1m	3m	12m
Relative to HSI (%)	(0.5)	46.3	34.2
Actual price changes (%)	4.6	46.0	53.8



Source: Bloomberg

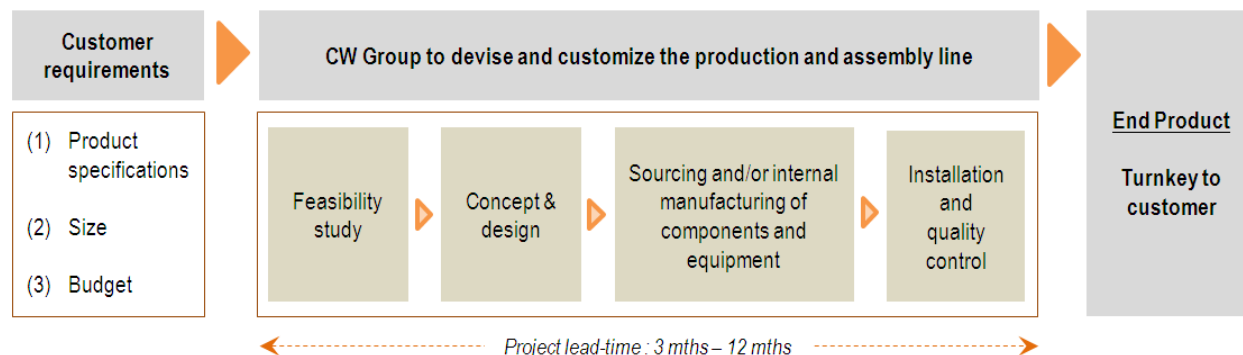
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Precision engineering solutions segment to expand on increased capital since 2012. CW Group expects to enjoy organic growth through recurring sales from existing turnkey solutions clients. Earlier this month, the company announced it signed a HK\$62.5m contract with AME International for engineering turnkey solutions, which is expected to be delivered this year. With the listing status, strengthened capital and increased trade financing & facilities, CW Group may demonstrate considerable growth for the precision engineering segment, in our view. Illustration 1 shows business model of precision engineering solutions of CW Group. While there is usually 10% down payment, the company generally needs to handle 1 production line order with working capital as well as 3-4 engineer and technical staff. CW Group had minimal loan from banks by end of 2012A, the company may gear up to take increasing orders from 2013F onwards.

Illustration 1. Precision engineering solutions business model



- **Cost-plus pricing model**
Stable gross profit margin of 20 – 30%

- Invoices are billed according to project milestones:

Client payment schedule example:

- (1) 10% as down payment
- (2) 80% upon acceptance of machineries
- (3) 10% after completion

Source: CW Group

Manufacturing business growth in 2013F largely on CNC sales to DMPG. In addition to providing precision engineering solutions, CW Group manufactures certain related equipments requiring considerable level of precision. CW Group recorded HK\$124.6m and HK\$101.8m sales from CNC machining centres and cement production equipments in the manufacturing segment. CW Group worked with KIWA in 2005 on CNC vertical machining machines and provided OEM service for DMPG on certain CNC horizontal machining centres since 2011/12. CW Group demonstrated its ability to manufacture components and provide turnkey solutions. On the other hand, in 2007 CW Group acquired 51% interest in the official PRC agent and distributor of Germany Pfister in relation to rotor weighfeeders, which is used in the manufacturing of cement and for coal-fired power plants. Leveraging from key clinker coolers, flow control gates and rotor weighfeeders, CW Group engages in cement production equipments with segment margin as high as 40%-50%. As for 2013F, while cement production equipments and sales related to KIWA may not be especially robust, DMPG may contribute higher sales in 2013F. Since working with DMPG in 2010, CW Group is now the only OEM of DMPG outside its own German facility. While meaningful sales were seen since 2H last year, management expects full year impact in 2013F would drive CW Group manufacturing business. With a 3-year CAPEX plan, we believe CW Group may expand its CNC machining centres production capacity in China or other Southeast Asian countries to capture fast growing orders from DMPG in short-to-medium term.

Table 3. Sales destination of CW Group

HK\$m	FY12/10A	FY12/11A	FY12/12A
China	256.1	246.6	208.0
Asia Pacific Region ex-China			
- Singapore	68.5	111.7	97.1
- Indonesia	24.7	107.5	232.6
- Malaysia	25.7	51.3	42.4
- Thailand	7.7	29.2	55.6
- India	45.2	94.2	82.8
- Hong Kong	n.a.	4.1	22.8
- Others	24.6	3.7	4.9
Europe	12.9	105.2	72.3
Others	4.0	0.1	-
Total	469.5	753.6	818.5

Source: SBI E2-Capital

Financial status and our view. Table 6 and Table 7 show the profit & loss summary and balance sheet summary respectively. As for 2012A, revenue was HK\$818.5m, up 8.6% YoY from 2011A. Gross profit and reported net profit were HK\$223.1m and HK\$55.1m respectively. Taking listing expenses and non-cash CB interest and derivative fair value changes out, adjusted net profit was HK\$104.7m for FY12/12A, up 13.4% YoY from HK\$92m in 2011A. As for the balance sheet, CW Group maintained a strong position with HK\$131.9m net cash. Due to the business nature, CW Group may not be able to provide hard asset to take bank loan especially without a listing status. Heavy trade and other receivables were up to HK\$630m and HK\$300m by the end of 2012A as compared to merely HK\$819m revenue for the year. To gain CAPEX and working capital to further expand the manufacturing segment and turnkey solution segment, CW Group may try to increase trade financing from banks from 2013F onwards.

Table 4. Profit and loss summary

HK\$m	FY12/10A	FY12/11A	FY12/12A
Revenue	469.5	753.6	818.5
Cost of sales	(324.2)	(574.1)	(595.5)
Gross profit	145.2	179.5	223.1
Other income and gains	2.1	1.4	3.5
Selling and distribution expenses	(18.8)	(28.0)	(31.1)
Administrative expenses	(27.4)	(34.1)	(68.1)
Other operating expenses	(1.1)	(0.1)	(15.7)
EBIT	100.0	118.0	111.6
Financial costs	(25.5)	(25.5)	(30.8)
Profit before tax	71.4	92.5	80.8
Income tax expenses	(20.7)	(24.5)	(25.6)
Shareholders' profit	50.6	68.0	55.1
Listing expenses	-	(4.2)	(25.6)
Non-cash CB interest & gains / derivative fair value change	(24.1)	(20.1)	(24.0)
Adjusted net profit	74.7	92.3	104.7

Table 5. Balance sheet summary

HK\$m	FY12/10A	FY12/11A	FY12/12A
Non-current assets			
Property, plant and equipment	25.6	33.4	44.5
Goodwill	32.9	34.4	34.7
Other non-current assets	0.9	0.9	0.9
Current assets			
Inventories	20.9	21.7	23.3
Trade receivables	232.5	566.6	630.2
Other receivables	141.9	147.7	299.9
Cash and cash equivalents	115.4	38.8	133.6
Other current assets	5.3	-	-
Non-current liabilities			
Loan and borrowings	3.3	1.6	-
Other non-current liabilities	16.3	21.2	12.7
Current liabilities			
Bank loans and overdraft	20.4	6.5	1.7
Trade payables	160.8	378.2	432.4
Other payables and accruals	141.0	103.7	123.9
Convertible loan	37.5	54.5	-
Derivative liabilities	43.0	43.4	-
Other current liabilities	10.5	17.0	25.8
Equity			
Total equity	142.5	217.3	570.5

Source: SBI E2-Capital

Valuation. At HK\$104.7m adjusted net profit for 2012A, current market capitalization of HK\$1,258m represents P/E of 12.0x for FY12/12A. With possible growth in precision engineering solutions and expected increase in sales to DMPG, we believe FY12/13F P/E could be lower than 10x assuming stable adjusted net margin. While there are precision components manufacturer and equipment producers listed in HK, we believe there is no direct competitor especially with its turnkey solution business. Nevertheless, we believe CW Group continues to spend effort and time to build long-term relationship with leading international enterprises in aerospace, oil and gas as well as automotive industries. CW Group could be able to enlarge its sales in line with clients' expansion plans. Furthermore, with sufficient cash on hand, CW Group could also look into M&A opportunities especially in existing precision component manufacturing universe, in our view.

Table 6. Shareholders of CW Group

Founder William Wong and family	32.1%
Others and public	67.9%
Total	100.0%

Source: SBI E2-Capital

Table 7. HK listed machinery / CNC producers

Company	Ticker	Fiscal Year End	Mkt Cap (US\$m)	Historical	P/E (x)		P/B (x)	ROE (%)
					1-year fwd	1-year fwd		
CW Group	1322 HK Equity	12/2012	161.5	21.2	11.3	9.7	2.2	14.0
Haitian Int'l	1882 HK Equity	12/2012	2,767.8	17.4	15.1	13.1	3.2	19.7
Eva Precision	838 HK Equity	12/2012	331.6	37.3	14.2	10.0	1.3	3.5
Good Friend Int'l	2398 HK Equity	12/2012	139.4	21.1	n.a.	n.a.	1.2	11.2
Cosmo Machinery	118 HK Equity	12/2012	50.9	n.a.	n.a.	n.a.	0.3	(1.7)
Chen Hsong Holdings	57 HK Equity	03/2012	212.3	14.6	13.4	11.9	0.6	4.0
L.K. Technology	558 HK Equity	03/2012	204.4	23.0	7.0	5.4	1.0	4.2

Source: Bloomberg

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