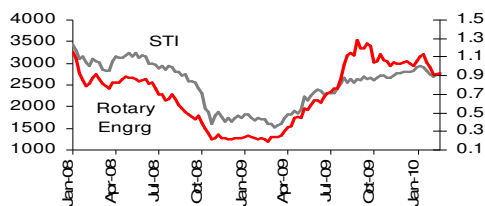


26 February 2010

Maintain

**BUY**

Previous Rating: BUY

**Current Price: S\$1.00**
**Fair Value: S\$1.44**


Reuters Code	ROTE.SI
ISIN Code	R07
Bloomberg Code	RTRY SP
Issued Capital (m)	568
Mkt Cap (S\$m/US\$m)	568 / 403
Major Shareholders	
Chia Kim Piow	29.14%
Oman Investment Fund	21.4%
Free Float (%)	39.0%
Daily Vol 3-mth ('000)	2,817
52 Wk Range	0.230 - 1.300

(S\$ m)	FY08	FY09	FY10F	FY11F
Revenue	520.1	551.9	594.0	565.5
Gross profit	123.5	129.9	128.4	132.3
EPS (cts)	9.0	9.6	10.3	11.6
PER (x)	11.2	10.5	9.7	8.6
P/NAV (x)	2.8	2.3	2.0	1.8

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## Rotary Engineering Ltd

### 4Q09 surpasses expectations

**4Q09 surpasses expectations.** Rotary Engineering (Rotary) delivered a good set of 4Q09 results. The group reported revenue of S\$147.0m (down 1.6% YoY but up 35.2% QoQ), gross profit of S\$45.7m (up 3.9% YoY and 65.7% QoQ) and net profit of S\$26.2m (up 36.0% YoY and 143.9% QoQ). For the full year, revenue improved 6.1% to S\$551.9m, while net profit gained 6.7% to S\$54.2m, beating our forecast by 29%. If not for a non-recurring S\$5.7m debt provision, net profit would have grown by a larger 17.9% to S\$60.0m. A final dividend of 3.8 S cents has been declared, implying a yield of 3.8%.

### Good 4Q09 margins, but guidance remains cautious.

Rotary's 4Q09 profit margins beat our estimates and management's guidance on higher productivity and realisation of cost savings as several projects were completed during the quarter. Gross profit margin hit 31.1% (vs. 29.4% in 4Q08 and 25.4% in 3Q09); while net profit margin swelled to 17.8% (vs. 12.9% in 4Q08 and 9.9% in 3Q09). Despite achieving robust profit margins in 4Q09, management continued to guide for a cautious 18% - 20% gross profit margin in FY10, citing keen competition as well as lagged effect from lower-margin projects secured during the credit crunch, which may continue to weigh on the group's earnings.

### Earnings visibility buoyed by all-time high order book.

The group's order book remains robust at S\$1.3b (vs. S\$1.36b as of 3Q09) with visibility stretching till 2013, buoyed mainly by its landmark S\$1.1b SATORP project. We understand that SATORP has been making good progress and started contributing to the group's earnings in 4Q09. We expect SATORP to give its earnings a bigger boost from 2H10 onwards as the project goes into full swing. However, receivables days are expected to lengthen as collections may be slower due to red tape involved with the massive scale of the SATORP project. Nevertheless, management allayed concerns over potential bad debts associated with SATORP, alluding to low Saudi Arabian sovereign risk.

**Maintain BUY.** Tendering activity is likely to heat up as more projects come on stream along with the economic recovery. Rotary remains active in pursuing more projects in Asia and the Middle East, and any news of contract wins could serve as near-term catalysts for the stock. We have raised our earnings projections and lift our valuation peg to 14x (from 13x) in view of the improving outlook, deriving a fair value estimate of S\$1.44 (previously \$1.37). Maintain **BUY**.

## Rotary's Key Financial Data

<b>Rotary Results</b> Year Ended 31 Dec (\$ m)	<b>4Q08</b> (S\$m)	<b>4Q09</b> (S\$m)	<b>% Chg</b> (YoY)	<b>3Q09</b> (S\$m)	<b>% Chg</b> (QoQ)
Revenue	149.4	147.0	-1.6%	108.8	35.2%
Gross profit	44.0	45.7	3.9%	27.6	65.7%
Operating expenses	-17.8	-16.9	-5.0%	-13.3	27.2%
EBIT	26.2	28.8	10.0%	14.3	101.4%
Other expenses/income	-0.8	0.2	N.M.	-0.8	N.M.
PBT	25.4	29.0	14.4%	13.5	114.5%
Tax	-4.9	-5.5	11.5%	-2.8	93.9%
PAT	20.5	23.6	15.1%	10.7	120.0%
Minority Interest	-1.2	2.6	N.M.	0.0	N.M.
Net profit	19.2	26.2	36.0%	10.7	143.9%

## Rotary's Key Financial Data

<b>EARNINGS FORECAST</b>					<b>BALANCE SHEET</b>				
Year Ended 31 Dec (\$m)	FY08	FY09	FY10F	FY11F	As at 31 Dec (\$m)	FY08	FY09	FY10F	FY11F
Revenue	520.1	551.9	594.0	565.5	Cash and cash equivalents	157.8	132.4	148.3	190.5
Gross profit	123.5	129.9	128.4	132.3	Other current assets	199.2	259.3	279.3	265.8
Operating expenses	-51.3	-63.2	-50.5	-45.2	Property, plant, equipment	65.6	78.4	88.0	96.4
EBIT	72.1	66.7	77.9	87.0	Total assets	455.1	497.4	543.4	581.3
Other income	-2.4	-1.5	-0.6	-0.6	Debt	7.8	7.4	12.0	12.0
PBT	69.8	65.3	77.3	86.4	Current liabilities excluding debt	229.4	225.4	228.6	223.7
Tax	-15.5	-13.2	-16.2	-18.1	Total liabilities	238.7	234.7	242.4	237.6
PAT	54.3	52.1	61.0	68.3	Shareholders equity	204.5	247.0	282.9	323.4
Minority interest	-3.4	2.2	-2.4	-2.3	Total equity	216.4	262.7	301.0	343.7
Net profit	50.9	54.2	58.7	66.0	Total equity and liabilities	455.1	497.4	543.4	581.3

<b>CASH FLOW</b>					<b>KEY RATES &amp; RATIOS</b>				
Year Ended 31 Dec (\$m)	FY08	FY09	FY10F	FY11F		FY08	FY09	FY10F	FY11F
Op profit before working cap.	82.7	87.8	88.3	98.6	EPS (\$ cents)	9.0	9.6	10.3	11.6
Working cap, taxes and interest	-6.0	-93.7	-34.2	-10.8	NAV per share (\$ cents)	36.0	43.5	49.8	56.9
Net cash from operations	76.7	-5.9	54.0	87.8	EBIT margin (%)	13.9%	12.1%	13.1%	15.4%
Purchase of PP&E	-25.0	-24.0	-20.0	-20.0	PBT margin (%)	13.4%	11.8%	13.0%	15.3%
Investing cash flow	-24.8	-2.7	-20.0	-20.0	Net profit margin (%)	9.8%	9.8%	9.9%	11.7%
Financing cash flow	-49.0	-15.8	-18.2	-25.6	PER (x)	11.2	10.5	9.7	8.6
Net cash flow	3.0	-24.5	15.9	42.3	Price/NAV (x)	2.8	2.3	2.0	1.8
Cash at beginning of year	154.4	157.4	132.9	148.8	Dividend yield (%)	2.3%	3.8%	4.0%	4.5%
Cash at end of year	157.4	132.9	148.8	191.1	ROE (%)	24.9%	22.0%	20.7%	20.4%
Cash and cash equivalents	157.8	132.4	148.3	190.5	Net gearing (%)	Net Cash	Net Cash	Net Cash	Net Cash

Source: Company data, OIR estimates

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**SHAREHOLDING DECLARATION:**

The analyst/analysts who wrote this report holds NIL shares in the above security.

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OCBC Investment Research's (OIR) technical comments and recommendations are short-term and trading oriented.

- However, OIR's fundamental views and ratings (Buy, Hold, Sell) are medium-term calls within a 12-month investment horizon. OIR's Buy = More than 10% upside from the current price; Hold = Trade within +/- 10% from the current price; Sell = More than 10% downside from the current price.

- For companies with less than S\$150m market capitalization, OIR's Buy = More than 30% upside from the current price; Hold = Trade within +/- 30% from the current price; Sell = More than 30% downside from the current price.

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