KIM ENG

SUNNY SIDE UP

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What's cooking

Telco Sector Update – More is less. According to media reports, ViewQwest, a private company that provides enterprise communications services, has invested S$8m to form its own Operating Company (OpCo) in Singapore. It plans to invest another S$15m over the next two years to widen its coverage. We do not expect it to have a major impact on the incumbent telcos. We remain constructive on Singapore telco stocks as a great defensive choice for volatile times. SingTel and StarHub are our top picks.

gyap@kimeng.com

Hot stock

Eratat Lifestyle Ltd (ERAT SP, $0.120, NOT RATED) – Eratat recently reported a 9.7% YoY increase in its 3Q11 net profit to RMB48.4m despite a revenue decline of 3.8%. It has received confirmed orders worth about RMB380m during the August trade fair, with delivery scheduled for between January and June next year. The stock is trading at consensus valuation of less than 2x FY11 PER.

ericong@kimeng.com

Top news in bite-sized pieces

OVERNIGHT…

- **Wall Street continued its volatile week** with the Dow taking a 1.1% dip in yesterday's trading. Old themes have resurfaced. In Europe, fears have rekindled as aid for Italy may not be forthcoming, and in the US, the debt ceiling "super committee" looks like it is still playing bipartisan hardball a week ahead of the deficit cut deadline.

LOCAL…

- **Singapore's S-chip sector looks set to remain volatile,** as China Sky Chemical Fibre suspended trading of its shares yesterday, as directed by the Singapore Exchange. It has to appoint a special auditor to probe into transactions surrounding repairs and maintenance costs of RMB72m in 2009, as well as several other issues.

Today's market forecast 18 November 2011

RAINY

Last: 2,778.25 (-29.19)
High: 2,816
Low: 2,743

STI TECHNICALS

The STI continues to deteriorate and will likely open in a shaky mood today, with the bias towards the downside. The momentum is negative with RSI below its neutral level. Support is at the 2,650 area.

Overnight market snapshots

Dow Jones	11,770.73	-134.9
Nasdaq	2,587.99	-51.6
FTSE 100	5,423.14	-85.9
CAC 40	3,010.29	-54.6
DAX Index	5,850.17	-63.2

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"The Real Deals" webcast

Ins & Outs of Commercial Property Investment

Speaker: Ooi Yi Tung

In yet another educational session, our property analyst Ooi Yi Tung shares his views on the retail property scene and sheds light on the valuation methods used by the industry.

Watch the video presentation of the hour-long talk (six parts in all) attended by more than 500 property agents on 7 October 2011.

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SINGAPORE

Co. Reg No: 198700034E
MICA (P) : 090/11/2009

Analyst: Gregory YAP 65-64321450 gyap@kimeng.com

Event

The expansion plans of ViewQwest – the first non-telco to have its own Operating Company (OpCo) – to cater to both business and consumer communication and connectivity needs is not expected to have a major impact on the incumbent telcos.

Our View

- According to recent media reports, ViewQwest, a private company that provides enterprise communications services such as Internet connectivity, IT managed services and outsourced telephony business services, has invested S$8m to form its own OpCo in Singapore. With its current coverage only in the central business district since last year, it plans to invest another S$15m over the next two years to extend its coverage islandwide.

- We are not surprised to see more competition rearing up in the local telco scene. After all, one of the stated goals of the Next Generation Nationwide Broadband Network (NGNBN) is to help create a vibrant Retail Service Provider (RSP) space to enable corporates and consumers to benefit from new services. These include multiplay services that combine voice, video and data, as well as cloud computing services that are only possible with high bandwidth. Still, we do not see unfettered competition due to the large capex required.

- We understand ViewQwest is primarily in the business of providing Internet connectivity and IT managed solutions, although it has also recently launched consumer fibre plans at prices that are slightly more expensive than Super Internet. Despite its ambitious NGNBN plans, it does not appear to have the scale or branding necessary to compete in either the corporate or residential segment. In fact, the company appears to be playing catch-up to the incumbents.

- The leaders in outsourced business communications in Singapore, especially in the area of IP-PBX, the area of focus for ViewQwest, are SingTel (PhoneNet) and StarHub (O.N.E. Phone). Even M1 has had an IP-PBX and Centrex solution for business customers following the advent of NGNBN. We do not view it as a significant competitor for either SingTel or StarHub in the corporate space, while M1 is likely to have stronger branding in the residential space.

Action & Recommendation

Despite the more pervasive NGNBN competition expected, we remain constructive on Singapore telco stocks as a great defensive choice for volatile times. At this point, SingTel and StarHub are our top picks.

HOT STOCK

Eratat Lifestyle Ltd

Analyst: Eric ONG 65-64321857 ericong@kimeng.com

Up-to-date in 60 seconds

Background: Listed on the Singapore Exchange since April 2008, Eratat Lifestyle is mainly engaged in the design, manufacture and distribution of lifestyle fashion footwear and apparel, marketed under its proprietary brand, *ERATAT*. Its products are sold in more than 900 speciality shops across China.

Recent development: We recently attended Eratat's 3Q11 results briefing. Net profit was up 9.7% YoY to RMB48.3m despite a slight revenue decline of 3.8% due to fewer distributors during the period. In addition, gross margin improved by 2.3ppt to 34.5% because of positive sales contribution by higher-margin apparel and an increase in ex-factory ASP of its products.

Key ratios…

Price-to-earnings: 2.2x
Price-to-NTA: 0.35x
Dividend per share / yield: RMB0.03 / 5.0%
Net cash/(debt) per share: S$0.07
Net cash as % of market cap: 61.3%

Source: Bloomberg

Everything else…

Share price	S$0.120
Issued shares (m)	474.913
Market cap (S$m)	57.0
Free float (%)	63.0%
Recent fundraising activities	April 2011: Private placement of 60m new shares @ $0.202/share
Financial YE	31 December
Major shareholders	Lin Jiancheng (25.3%), Ye Sanzhi (6.8%)
YTD change	-50.0%
52-wk price range	S$0.117-0.27

Source: Company

Our View

- **Cash conversion cycle extended.** Starting last year, Eratat allowed its key distributors to set up more direct-owned speciality shops and strengthen their individual distribution network. To support its distributors' growth expansion which typically requires a high initial investment outlay, the group offered longer credit terms. Management said it has not experienced any default so far under this model, as it is usually very selective when it comes to the appointment of its distributors.

- **New order wins.** Separately, Eratat said that it has received confirmed orders amounting to RMB380m during the August trade fair, of which about 37% are for ERATAT Premium products (vs 8% last year). Delivery is scheduled for between January and June next year. We also note that the 2012 Season sales mix of footwear and apparel will be about 25% and 75%, respectively (2011 Season: 51% and 49%, respectively).

- **Enhance ERATAT brand positioning.** Given the encouraging market response after the launch of its ERATAT Premium product range in 2Q11, the group plans to upgrade most of its existing retail shops (currently, about 20% tout the New Premium image). It will support the distributors' efforts to upgrade their older shops by providing renovation subsidies through offsetting against their trade receivables.

- **Victim of S-chip confidence woes.** The stock currently trades at a cheap valuation of less than 2x FY11 PER, based on consensus estimates.

Summary Financials

Year End Dec 31	2008	2009	2010	9M11
Sales (RMB m)	453.0	777.4	787.6	787.2
Pre-tax (RMB m)	80.2	146.8	150.6	186.9
Net profit (RMB m)	70.2	125.9	111.4	138.8
EPS (fen)	24.2	30.8	26.8	30.9
EPS growth (%)	72.8	27.2	-12.7	n.m.
PER (x)	2.5	2.0	2.2	n.m.
Yield (%)	2.5	7.8	5.0	n.m.

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Stephanie Wong
CEO, Kim Eng Research