

DEMCO - DEMCO

Promising earnings growth,
renewable energy as growth driver

Bloomberg | Reuters
DEMCO TB | DEMCO.BK

Thailand Equities Research
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Company Overview

DEMCO's core businesses include transmission line, substation, renewable energy power plant, mechanic and electrical system, energy conservation business, telecommunications, fabrication and distribution of steel structure for transmission line, billboard signs.

- DEMCO reported stellar earnings performance in CY12. Net profit skyrocketed 232.94% y-y to Bt396.03mn and revenue jumped 80.6% y-y to Bt5.94bn.
- In 1QCY13, revenue dropped 52.61% y-y to Bt685.80mn, dragging net profit by 68.70% y-y to Bt24.45mn. Much of the declines were attributable to lower sales of hardware and equipment as well as the delay of 3G network expansion and the deliveries of completed projects.
- For CY13, net profit is projected to accelerate 54.34% y-y to Bt612.73mn with revenue rising 20.79% y-y to Bt7,174.24mn.
- We rate DEMCO a 'BUY' with a target price of Bt15.25/share.

What is the news?

DEMCO registered CY12 revenue of Bt5.94bn, up 80.6% y-y, as revenue from sales business made the big leap of 278.25% y-y. Net profit jumped 232.94% y-y to Bt396.03mn in the same period.

Earnings dropped at faster pace in 1QCY13. Total revenue fell 52.61% y-y to Bt685.80mn, dragged by lower sales of hardware and the delay of 3G network expansion project. As a result, net profit dropped 68.7% y-y to Bt24.45mn.

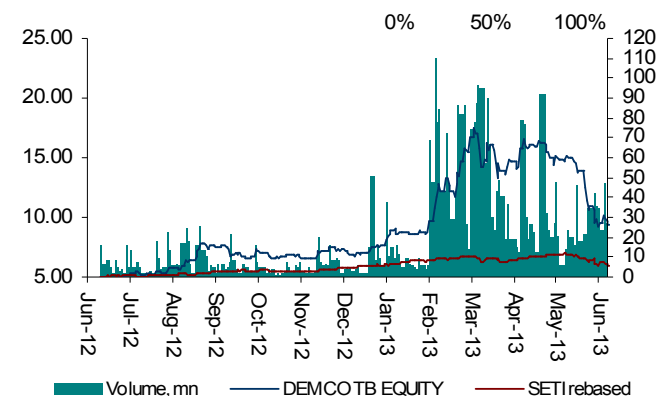
How do we view this?

Despite weak earnings performance in the first quarter, we foresee bullish growth over the remaining course of the year, given sizable backlog of 3G network implementation project and equity income from Huoy Bong 2 and 3. We project total revenue to grow 20.79% y-y to Bt7,174.21mn, contributing to net profit of Bt612.73mn, a jump of 54.34% y-y.

Investment Actions?

We compute price target for DEMCO with sum-of-the-parts (SOTP) to arrive at Bt15.25/share (using DCF to value WEH arriving at Bt4.65 and 18x P/E to value electrical engineering arriving at Bt10.60). We have a 'BUY' call for DEMCO.

DEMCO	1.00	Buy
- Previous Rating	-	Not Rated
Target Price (Bt)	15.25	
- Previous Target Price (Bt)	-	
Closing Price (Bt)	9.05	
Expected Capital Gains (%)	68.5%	
Expected Dividend Yield (%)	4.0%	
Expected Total Return (%)	72.5%	
Raw Beta (Past 2yrs weekly data)	1.40	
Market Cap. (USD mn)	276	
Enterprise Value (USD mn)	303	
Market Cap. (Bt mn)	8,560	
Enterprise Value (Bt mn)	9,342	
3M Average Daily T/O (mn)	30.0	
52 week range	4.718495 - 18.47604	
Closing Price in 52 week range		



Major Shareholders	(%)
1. Mrs. Praphee Puipunthavong	14.3
2. Thai NVDR	5.1
3. Mr. Pradej Kitti-ltsaranon	4.7

CG Report - 2012



(Very Good)

Key Financial Summary

FYE	12/11	12/12	12/13F	12/14F
Revenue (Btmn)	3,289	5,940	7,174	7,985
Net Profit, adj. (Btmn)	116	397	613	795
Net Profit (Btmn)	116	397	613	795
EPS, adj. (Bt)	0.27	0.78	0.85	1.05
EPS. (Bt)	0.27	0.78	0.85	1.05
P/E (X),adj.	34.1	11.6	10.7	8.6
BVPS (Bt)	2.41	3.16	5.04	5.67
P/B (X)	3.7	2.9	1.8	1.6
DPS (Bt)	0.12	0.35	0.34	0.42
Div. Yield (%)	1.3	3.9	3.7	4.7

Source: Bloomberg, PSR est.

*All multiples & yields based on current market price

Valuation Method

SOTP: DCF and P/E13 (18X)

Background

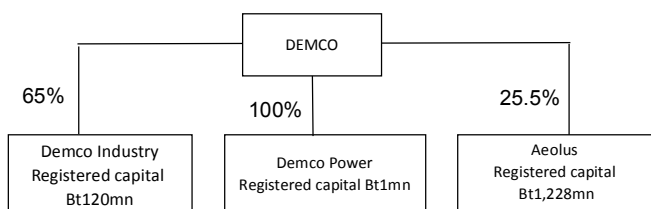
DEMCO was founded on June 1, 1992, with registered capital of Bt6mn. The company has been under the management of well-experienced engineers more than 20 years in electrical engineer work, distribution & transmission line system and substation.

Company Structure

At end-Dec 2012, DEMCO has two subsidiaries: Demco Industry and Demco Power, and one associate Aeolus Power.

1. Demco Industry: DEMCO owns 65% stake in Demco Industry which has the paid-up capital of Bt64mn. Demco Industry's business primarily covers in custom-made high-pressured broiler and installation as well as fabrication of pipe bridge and pipe rack.
2. Demco Power is wholly-owned by DEMCO with registered capital of Bt1mn. Demco Power aims to support the alternative energy business development for DEMCO.
3. Aeolus Power: DEMCO held 27% stake and currently 25.52% after right subcription in 2012. Aeolus is the holding company owns 60% in First Korat Wind (First) and K.R.2, operating in wind farms at Huay Bong 3 and Huay Bong 2. The investment in the alternative energy businesses via Aeolus will contribute to DEMCO consistent equity income in the long term. This move will expand DEMCO's expertise in the renewable energy industry, implying an opportunity to step into the energy industry both in domestic and neighboring countries.

Figure 1: Company structure



Source: Company

Business Overview

DEMCO operates five core businesses; i) design, construction and contract all kinds of electrical engineering works such as transmission line, substation, ii) mechanic and electrical System, iii) energy conservation, iv) telecommunications; and v) fabrication and distribution of steel structure for transmission line, and billboard signs. Overall business can be classified into three categories.

1. Service business

1.1. Electrical engineering designs, constructs and contracts all kinds of engineering works on a turnkey basis for clients in both public and private sectors.

Figure 2: Electrical engineering work



- a) **High voltage transmission line system** is the transmission system from receiving electricity from originating sources such as dam, solar power plants to transmission and substation. Transmission line system can handle 69KV 115KV 230KV and 500KV pressure level.

Figure 3: High voltage transmission line system work



Source: Company

- b) **High voltage substation** receiving electricity from originating sources and transfer electricity pressure to transmission line and power supply system to users. Substation transferring electricity has pressure from 500KV, 230KV, 115KV and 22 KV.

Figure 4: High voltage substation work



Source: Company

- c) **Underground electricity system construction** is the construction of 22KV and 33KV lower pressure cable from substation to users. Underground electricity system is the distribution line and transmission line construction underground. Distribution line construction service is continuously expanding according to increasing customer base.

Figure 5: Underground electricity system construction work



Source: Company

- 1.2. **Renewable energy** designs, contracts and constructs alternative energy plants such as wind farm, solar power plant and biomass power plant.

Figure 6: Alternative energy work



Source: Company

- 1.3. **Telecommunications and signaling systems** covers the design, supply and construction of telecommunications towers and signaling systems; and fiber optic laying for the public sector.
- 1.4. **Mechanical and electrical system (M&E)** designs, constructs and manages mechanical and electric systems and facilities such as electrical system, water management, air-conditioning and ventilation, steam and hot water system, and high pressure piping.

Figure 7: Mechanical and electrical work



Source: Company

- 1.5. **Telecommunications** start from manufacturing and installation for customers who demand for telecommunication tower from government, private sector as well as mobile phone operator and its subcontractor.

Figure 8: Telecommunications work



Source: Company

- 1.6. **Energy Conservation:** In 2003, DEMCO become a registered consultant in energy construction through the Department of Alternative Energy and Energy Conservation. The company participates in the government's energy conservation projects by designing and setting up energy conservation system for government units and large-scale factories.

2. **Sales business** covers in three areas

- 2.1. **Steel structure fabrication** includes steel structure for distribution lines, transmission lines and substations; steel structure for telecommunications work; steel structure for large outdoor billboard. The current steel structure capacity is as high as 12,000 tons per year.

Figure 9: Steel structure production



Source: Company

2.2. Complete set of installation and assembly equipment for telecommunications tower such as self-support tower and Guyed Mast tower.

2.3. Distribution of electrical tools for transmission systems and substations

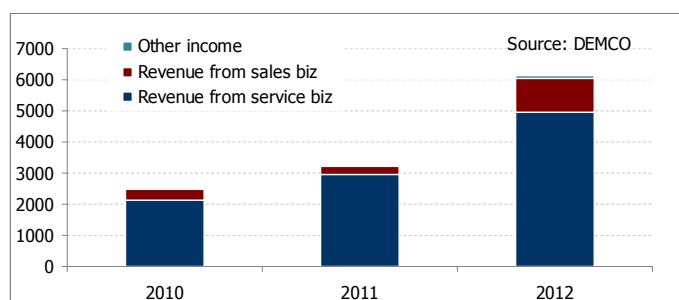
2.4. Distribution of building materials: cement, concrete, steel and paints as well as any materials used in civil works.

3. Business development: In 2009, DEMCO in collaboration with its partners set up the wind farm project. DEMCO took charge of its area of expertise such as site inspection, wind farm design, procurement, construction and civil and electrical engineering systems while the partner sourced wind turbines and raised funds. DEMCO's move into the renewable energy is considered a well-diversified portfolio to reduce business exposure. Furthermore, this business segment is expected to provide DEMCO consistent equity income in the long term. DEMCO currently has invested in two wind farms (Huay Bong 2 and 3) with capacity of 103.5MW each. Both wind farms already started the commercial run under the 90MW each sales contract with EGAT.

Revenue Structure

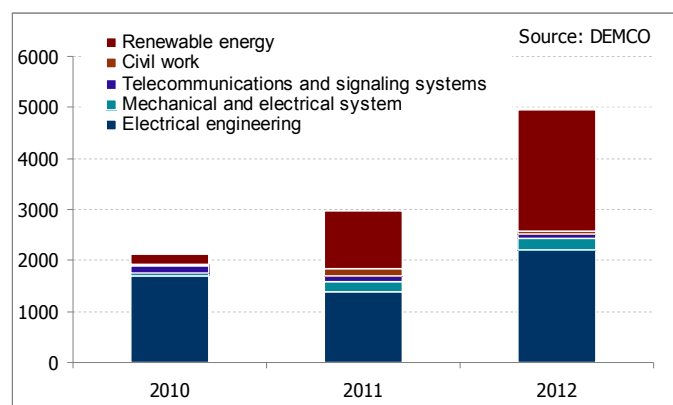
In 2012, DEMCO registered total revenue of Bt5.94bn. The service business segment made up to 81.08% of the total or Bt4.96bn, while the sales business generated 17.76% or Bt1.085bn, increasing notably from the 8.2% growth in 2011 after DEMCO focused to reduce revenue risk exposure and diversify investment portfolio.

Figure 10: Revenue by business segments, 2010-2012



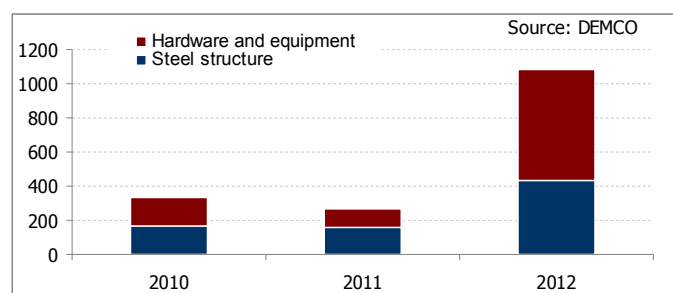
In the service business segment, electrical engineering unit generated the highest revenue; however, revenue contribution from the renewable energy business accelerated sharply in 2011 and exceeded that of electrical engineering in 2012 as a result of the company's revenue diversified strategy. Revenue from renewable energy business made up to 9.25% of total service business revenue in 2010 and the contribution increased notably to 38.16% (or Bt1.13bn) and 48.05% (or Bt2.38bn) in 2011-2012. On the contrary, electrical engineering business made up to 46.39% (or Bt1.37bn) in 2011 but the ratio fell to 44.57% (or Bt2.21bn) in 2012. The reduction in revenue contribution from the electrical engineering business was largely due to the delay and smaller numbers of projects released by the PEA, which turned out to affect positively revenue in CY13.

Figure 11: Revenue contribution in service business segment



In the sales business segment, revenue from this segment accounted for 8.2% of DEMCO's total revenue in 2011 before it increased to 17.76% in 2012 as a result of sales of electrical hardware and equipment and building materials. In 2011, electrical sales generated up to Bt110.83mn or 41.43% of total revenue in the sales business segment, while revenue from steel structure reached Bt156.69mn or 58.57%. In 2012, revenue contribution from these two respective businesses increased to 59.78% (Bt649.08mn) and 40.22% (Bt436.64mn).

Figure 12: Revenue contribution in sales business segment



Key Client Groups

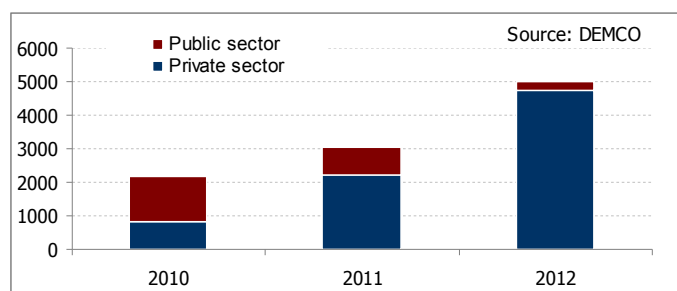
DEMCO's key clients can be divided into two groups.

1. Private sector includes manufacturers, individual power generators (both IPP and SPP), industrial estate, and mobile phone network operators.
2. Public sector covers all state enterprises such as EGAT, CAT, State Railway of Thailand, and etc.

DEMCO focuses on balancing revenue from both groups as a part of revenue diversification and an effort to maintain revenue growth rate and profitability.

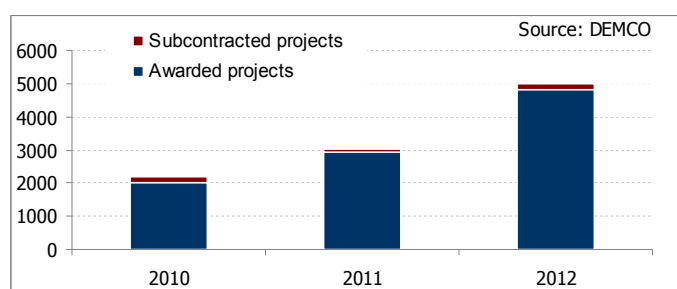
In 2011, service revenue derived from the private and public group accounted for 27.36% and 72.64%, respectively. Revenue proportion from the private sector climbed sharply higher after DEMCO won the bidding project of mass rapid transit in late 2010 and more projects related to alternative energy in 3QCY11. Later in 2012, revenue contribution from the private sector jumped to 95.01%, largely driven by rising demand for renewable energy (wind farms and solar power plant).

Figure 13: Revenue contribution by key client groups



With regards to types of projects, some DEMCO won the bids itself and some were subcontracted. In 2011, the awarded projects accounted for 96% of total projects, increasing from 92% in 2010, after the company expanded the business into renewable energy and high-voltage substation work. In 2012, the proportion of awarded project stayed flat y-y on the back of renewable energy and substation work.

Figure 14: Revenue contribution by type of projects



In the sales business, almost of all sales revenue was derived from the private sector. To reduce revenue risk exposure, DEMCO started to provide steel structure to the public sector from 2008 onwards.

Electrical Engineering Industry Outlook

The Power Development Plan for 2010, covering power output development during 2012-2030, was revised the third time to track the country's resilient economic outlook and infrastructure development plan. This, together with the government's policy to promote and subsidize alternative and renewable energy, will apparently benefit the electrical engineering industry, including the alternative energy. Nonetheless, uncertainty about the government's policy would have adverse impact on the industry growth over the next 1-2 years.

Figure 15: Power Development Plan (Revision 3), 2012-2030

	(MW)	
	PDP 2010 Rev.2	PDP 2010 Rev.3
Total capacity (as of December 2011)	32,744	32,629
Total added capacity during 2012 – 2030	53,874	55,065
Total retired capacity during 2012 – 2030	-17,061	-16,847
Grand total capacity (at the end of 2030)	69,557	70,847

Source: Energy Policy and Planning Office

Figure 16: Comparison of procuring electricity and output in PDP 2010 (Revision 3)

	(MW)	
	PDP 2010 Rev.2	PDP 2010 Rev.3
Back-up production capacity	16.00%	16.10%
CO2 Emission (kg/kWh)	0.3864	0.3826
Capacity ratio		
- Natural gas	47%	54%
- Coal	16%	11%
- Imported fuel	18%	12%
- Renewable energy	6%	14%
- Nuclear	6%	3%
- Hydropower	7%	6%
Production ratio		
- EGAT	49%	43%
- IPP	14%	21%
- SPP and VSPP	13%	11%
- Imported fuel	18%	12%
- Unidentified	6%	13%

Source: Energy Policy and Planning Office

Competitive Advantages

DEMCO's expertise and broad knowledge which has been well recognized by the public sector while its diversified portfolio help reduce revenue exposure and dependency on certain business. The big investment in the renewable energy industry (wind farms and solar power plant) which has contributed consistent equity income in the long term, enables DEMCO to have price competitive against rivals. Furthermore, DEMCO as the registered supplier for the state enterprises (Bangkok Metropolitan Administration, Port Authority of Thailand, EGAT, PEA, and Metropolitan Electricity Authority) allows the company to provide services to various organizations in foreseeable future. The proven successful from both public and private sector has given DEMCO an opportunity to screen out the bidding projects to suite the company's capabilities.

CY12 & 1QCY13 earnings review

Stellar CY12 results driven by strong revenue expansion

DEMCO reported CY12 net profit growth of up to 232.94% to Bt396.03mn from Bt118.95mn in CY11 on the back of solid revenue expansion. Net profit margin nearly doubled to 6.59% from 3.57%.

Total revenue swelled 80.6% to Bt5,939.59mn in CY12 from Bt3,288.79mn in CY11. Core service revenue jumped 64.20% to Bt4,986.41mn in CY12 from Bt3,036.80mn in CY11. Sales revenue skyrocketed 278.25% to Bt953.18mn in CY12 from Bt252.00mn in CY11. Renewable energy and electrical engineering contributed the biggest proportion of core service revenue. In CY12, renewable energy was the biggest revenue earner for DEMCO at Bt2.38bn, followed by electrical engineering at Bt2.21bn as a consequence of bidding delays and a lower number of bidding projects from the Provincial Electricity Authority (PEA). The proportion of sales revenue doubled to 17.76% of total revenue in CY12 from 8.20% in CY11. Electrical hardware/equipment and construction materials took the biggest slice of sales revenue pie at Bt649.08mn in CY12, followed by steel structure fabrication at Bt436.64mn.

Gross profits surged as much as 113.34% to Bt871.11mn in CY12 from Bt408.32mn in CY11. Gross profit margin expanded to 14.49% in CY12 from 12.42% in CY11. In services business, gross profit soared 80.37% to Bt731.48mn in CY12 from Bt405.55mn in CY11 and gross profit margin climbed to 14.67% in CY12 from 13.35% in CY11. For sales business, gross profit rose a whopping 4,922.66% to Bt139.63mn in CY12 from a mere Bt2.78mn in CY11 and gross profit margin sharply expanded to 14.65% in CY12 from 1.10% in CY11.

Earnings hiccup in 1QCY13

DEMCO reported 1QCY13 earnings drop in both q-q and y-y terms due chiefly to revenue contraction. In this period, total revenue plunged by 52.61% or Bt761.30mn from a year earlier to Bt685.80mn. Service revenue dropped by 47.77% or Bt591.07mn from a year ago to Bt626.24mn as the Huoy Bong 2 wind farm project was finished in 1QCY13 and DEMCO had just started work on its recently signed contracts for construction of solar power plant at Rojana Industrial Park and construction of substations for PEA. Sales revenue tumbled by 88.13% or Bt166.74mn to Bt22.45mn as a result of faltering revenue from sales of electrical hardware/equipment and construction materials and a delay in 3G network investments especially for installation of guy mast towers.

In this period, total gross profits clocked in at Bt88.55mn, down 49.30% from Bt174.67mn in 1QCY12 but total gross profit margin widened to 12.91% from 12.24%. In services business, gross profit shrank 44.22% to Bt97.28mn in 1QCY13 from Bt174.41mn in 1QCY12 but gross profit margin expanded to 15.05% from 14.10%. Sales business swung to a gross loss of Bt8.73mn from a gross profit of Bt0.27mn and its gross profit margin turned to negative 38.88% from positive 0.14%. The gross profit slide was

due chiefly to a drop in revenue from factory work. In sum, net profit plunged 68.70% y-y to Bt24.45mn in 1QCY13 from Bt78.11mn in 1QCY12. DEMCO booked a Bt60.06mn profit from its affiliate Aeolus Power in 1QCY13. Net profit margin dipped to 3.56% in 1QCY13 from 5.40% in 1QCY12.

CY13 & CY14 earnings outlook

CY13 revenue growth outlook of 21% on bright prospects for electrical engineering business and greater revenue stability enhanced by dividend income from wind farm projects

Despite 1QCY13 earnings slowdown, we stick to our forecast that CY13 earnings will be better than CY12 driven by a pipeline of new projects to be tendered and backlog, which would be realized as revenue throughout the year from both sales and services businesses and higher dividend income from Huoy Bong 2 and 3 wind farm projects. Its backlog as of Apr 20, 2013 stood at Bt6,086.11mn. Of the total, (1) Bt1.7bn came from electrical engineering comprising (i) Bt900mn for PEA substations and (ii) the rest Bt700mn for private sector projects: Up to Bt1.3bn out of the total Bt1.7bn is expected to be realized as revenue this year; (2) Bt3.1bn was derived from renewable energy, of which Bt2.6bn is likely to be realized as revenue this year comprising (i) three solar power projects with a capacity of 8 MW each in Ayutthaya Province worth a total of Bt2.3bn, which are slated to be completed in Nov 2013, Jan 2014 and Mar 2014 respectively, (ii) construction of the Bt1.385bn, 90-MW solar power plant in Nakorn Sawan Province, which has been carried out by EA Solar Nakornsawan, a subsidiary of Energy Absolute (EA) with a construction period of eight months and is slated for completion in Dec 2013: Revenue from this project is expected to be fully realized within this year, and (iii) the Bt500mn wind farm project in Khao Kho with construction slated to begin in 3QCY13. In early Jun 2013, DEMCO won contracts worth a total of Bt583.5mn from PEA to construct three new 115kV substations, which include 115kV switchgear, 115-22kV power transformer and computerized control system for Amata City Substation, Eastern Seaboard Substation and Hemaraj Substation in Rayong Province.

Figure 17: Backlog, 2013-2014

Project (Bt mn) as of April 30, 2013	Backlog				
	1QCY13	2Q-4QCY13		2013	2014
	Project value	Number	Project value	Project value	Project value
Electrical engineering	321.52	81	827.67	1149.19	557.5
Mechanical and electrical system (M&E)	22.05	3	41.88	63.93	-
Telecommunications	17.1	18	61.67	78.77	-
Steel structure fabrication	15.4	-	-	15.4	-
Hardware sales	7.05	-	-	7.05	-
Total	383.12	102	931.22	1314.34	557.5
Renewable energy	285.57	7	2319.39	2604.96	587
Electrical engineering projects to be signed	-	2	1491	1491	200
Grand total	675.74	111	4741.61	5410.3	1344.5

Source: Company

Wind farm projects via Wind Energy Holding (WEH)

On May 30, 2013, the shareholders approved to buy 5,263,158 newly issued shares or an equivalent to 5% of all shares of Wind Energy Holding (WEH) at approximately Bt190/share. Total transaction size will be Bt1bn. This investment will yield consistent equity income in the long term and DEMCO will be able to sell the shares at premium when WEH lists in the SET in 2014. In the shorter period of time, DEMCO will benefit from WEH's nine projects on hands with a combined capacity of 690MW, calculating to a total value of approximately Bt6bn at an average of Bt10mn-Bt15mn per MW. Not only domestic market, WEH plans to expand the business into overseas such as Vietnam, India and Europe, estimating 4,000MW in total.

Looking at revenue from renewable business, DEMCO invested, based on its shareholding proportion, 16.2% each in Huoy Bong 2 and 3, which is expected to contribute equity income of approximately Bt100mn per year each. Huoy Bong 2 and 3 already generated electricity. For Khao Kor, DEMCO is expected to receive about Bt35mn per year based on its proportionally 10% investment in the project. The Khao Kho wind farm has sealed the 25-year power purchase contract with EGAT.

Figure 18: WEH's wind farm projects

Wind farms	Company	PPA (MW)	Capacity	COD	Status
West Huoy Bong 3	Aeolus/ KR2	90	103.5	Feb'13	On stream
West Huoy Bong 2	Aeolus/ FKW	90	103.5	Nov'12	
Khao Kho	Sustainable	60	59.8	2556	PPA signed with EGAT
Watabak	Watabak	60	68	2557	
Korat 02/01	Theparak	90	100	2559	
Korat 02/01	Tropical	90	100	2559	
Korat 02/01	KRS3	90	100	2559	
North Krisana	kWP	90	100	2559	Waiting for PPA signing with EGAT
Korat 02/01	KR1	90	100	2560	
ST 1	Infinite	60	75	2561	
Roi-Et	Roi-Et	60	75	2560	
Mukdaharn	Romklao	60	75	2560	
Total		930	1059.8		

Source: Company

Bullish CY13 net profit growth outlook

Given substantial backlog (Figure 17) and projected revenue from two operating wind farms, DEMCO's CY13 total revenue is projected to grow 20.79% y-y to Bt7,174.21mn. Revenue from service business would grow 21.34% y-y to Bt6,050.58mn while that of sales business would increase 6.08% y-y to Bt1,011.12mn. Electrical engineering work and wind farms are likely the major driver to notable growth in the service business while the expansion of 3G network, requiring DEMCO's Guyed Mast Tower, will help catalyze revenue in the sales business. Gross margin is expected to widen by 1.5% y-y to 14.89%; both businesses are expected to see wider margin with service business rising to 15% and sales business up to 14.25%. For this reason, net profit would jump as much as 54.34% y-y to Bt612.73mn, driven by estimated Bt189.45mn equity income from the wind farms Huoy Bong 2 and 3. Net profit margin would accelerate by 26.87% y-y to 8.5% this year.

CY14 earnings look promising

Total revenue is projected to continue to grow 11.3% y-y to Bt7,984.7mn. Net profit would grow 29.8% y-y to Bt795.4mn with net profit potentially improving to 10% (+26.87% from estimated 8.5% in CY13) as the combined 127.8MW two wind farms (Khao Kho and Watabak) will come on stream.

Capital increase of Bt1.25bn to acquire WEH shares and to list Demco Industry in SET

On May 29, 2013, the shareholder meeting approved to increase capital of Bt317.49mn from the current registered capital of Bt629.04mn by issuing 317.49mn shares at Bt1 par value. Of this not more than 125.80mn new shares are offered to the existing shareholders with a subscription ratio of 5 shares to 1 new share at an offering price of Bt10/share. Each of the 78,629,492 new shares will be reserved for right offering of DEMCO-W5 and DEMCO-W6 at the ratio of 1 warrant to 6 new shares at exercising price of Bt12/share for DEMCO-W5 and Bt15/share for DEMCO-W6. Moreover, up to 28mn shares will be allocated for DEMCO-ESOP3 at an exercising price of Bt15/share and DEMCO-ESOP2 at an exercising price of Bt2.688/share.

Not only would DEMCO enjoy long-term benefits from its investment in WEH, which would be funded by the rights issue, we think the capital raising would also help strengthen its financial standing for further expansion, reduce its leveraging and boost its capability to take more large-scale projects, all of which would bode well for future growth. Despite an estimated 30% dilution effect from the rights issue, we stick to our view that EPS will grow by 8.27% y-y to Bt0.85 in CY13. On a fully diluted basis due to the exercise of DEMCO-W5 and DEMCO-W6, EPS is estimated to be Bt0.84 in CY14, assuming a dilution effect of around 20%, which could be offset by additional cash flow of up to Bt2bn.

There is also a plan to list its subsidiary Demco Industry Co on the Thai stock market in CY14. Currently Demco Industry is in the process of financial, shareholding and investment restructuring to enhance its strength. Demco has formed a joint venture to take on construction contracts for small biomass and biogas power plants, which are likely to increase sharply in the future. Financial advisor for the listing would be appointed in 2QCY13.

Risk factors

The following are potential risks that may affect DEMCO's operating performance.

1. Inconsistent revenue stream: DEMCO has a policy to broaden its client base, maintain a balanced proportion of revenue from public and private sectors as well as branch out into other related businesses which would generate consistent cash flow for DEMCO in the long run.
2. Cost overrun as a result of project delays and changes in materials and equipment prices: To limit risk, DEMCO has signed contracts with suppliers to lock in costs since the start of the bidding.
3. Working capital risks: There have been no working capital problems for DEMCO.

4. FX risk: DEMCO uses FX forward contracts to hedge FX risk.
5. Factors beyond control: DEMCO has all risks insurance coverage for high-value projects or public projects.

In addition to the above risks, there will remain the risk of investment in WEH, electricity output shortfalls from the wind farm projects and penalty for project delays due to work overload. Even though DEMCO has measures and policies to limit and handle the above risks, we believe these risk factors still bear monitoring going forward.

Initiation of coverage with 'BUY' rating and Bt15.25/share target price

In view of current backlog, a pipeline of new projects to be up for bids and other projects in electrical engineering, sales and renewable energy businesses as well as growth opportunities from WEH's wind farm projects, we expect DEMCO to achieve CY13 net profit of Bt612.73mn, up 54.34% y-y. In our view, the sum-of-the-parts (SOTP) methodology is the most appropriate to value DEMCO at Bt15.25/share. The following are assumptions in the valuation model:

We use the discounted cash flow (DCF) methodology to value WEH in view of its stable cash flow. Note that we factor only projects with the already signed PPA into the forecast based on assumptions of a 25-year power supply deal with EGAT with Ft rate of Bt0.4064/kWh and adder of Bt3.5/kWh, an 8% discount rate and a D/E of 1.5x. We fairly value WEH at Bt4.65/share.

Based on the P/E metrics, we assign a historical trailing PER of 18x to construction and electrical engineering businesses to arrive at Bt10.60/share. We initiate coverage of DEMCO with a 'BUY.'

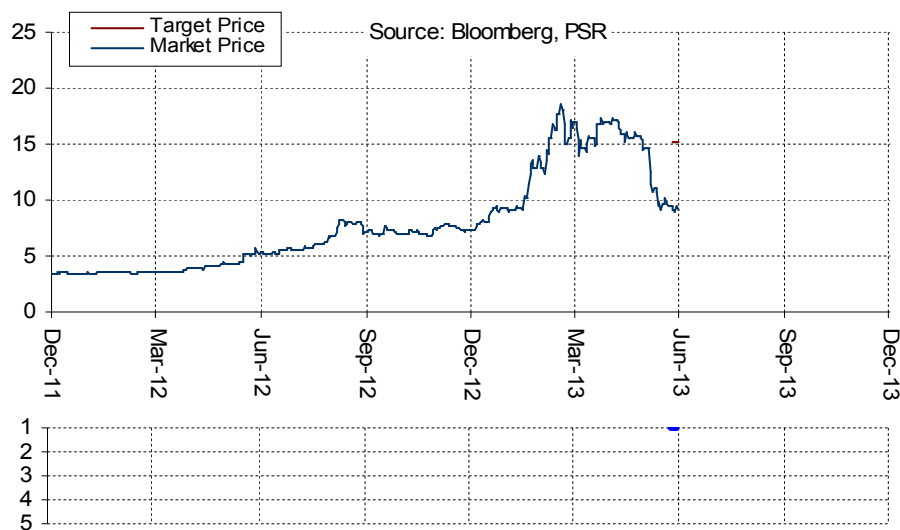
FYEDec	CY10	CY11	CY12	CY13F	CY14F
Valuation Ratios					
P/E (X), adj.	41.1	34.1	11.6	10.7	8.6
P/B (X)	3.8	3.7	2.9	1.8	1.6
EV/EBITDA (X), adj.	57.3	42.4	16.5	14.4	11.2
Dividend Yield (%)	1.7	1.3	3.9	3.7	4.7
Per share data (Bt)					
EPS, reported	0.19	0.27	0.78	0.85	1.05
EPS, adj.	0.22	0.27	0.78	0.85	1.05
DPS	0.15	0.12	0.35	0.34	0.42
BVPS	2.41	2.41	3.16	5.04	5.67
Growth & Margins (%)					
Growth					
Revenue	55.2	31.9	80.6	20.8	11.3
EBITDA	250.6	35.0	157.7	14.5	28.4
EBIT	1598.2	57.2	193.9	15.2	29.4
Net Income, adj.	298.0	34.0	242.0	54.3	29.8
Margins					
EBITDA margin	6.5	6.7	9.6	9.1	10.4
EBIT margin	4.7	5.6	9.2	8.7	10.2
Net Profit Margin	3.6	3.6	7.0	8.8	10.2
Key Ratios					
ROE (%)	7.0	8.4	14.5	15.3	18.7
ROA (%)	2.6	2.9	7.5	9.5	11.8
Net Debt-Cash	46	462	1,097	455	288
Net Gearing(X)	0.0	0.4	0.6	0.1	0.1
Income Statement (Bt mn)					
Revenue	2,493	3,289	5,940	7,174	7,985
EBITDA	163	220	567	649	834
Depreciation & Amortisation	45	35	23	22	23
EBIT	118	185	544	627	811
Net Finance (Expense)/Income	(19)	(41)	(108)	(92)	(77)
Other items	30	34	70	48	40
Profit Before Tax	128	167	494	773	1,009
Taxation	39	48	78	144	194
Profit After Tax	89	119	417	629	816
Non-controlling Interest	16	3	20	17	20
Net Income, reported	74	116	397	613	795
Net Income, adj.	87	116	397	613	795

Source: PSR est.

FYE Dec	CY10	CY11	CY12	CY13F	CY14F
Balance Sheet (Bt mn)					
Cash	165	201	204	368	484
ST Investments	0	0	0	0	0
Accounts Receivables	320	587	1,178	1,581	1,669
Inventories	192	216	205	296	331
Others	897	1,569	1,216	1,052	1,052
Total current assets	1,574	2,572	2,803	3,297	3,537
PPE	291	307	315	327	338
Intangibles	11	10	9	9	9
Associates & JVs	0	604	1,174	2,315	2,592
Investments	41	66	66	66	66
Others	52	98	71	198	198
Total non-current assets	395	1,085	1,635	2,914	3,202
Total Assets	1,969	3,656	4,439	6,211	6,739
Short term loans	180	632	1,278	803	753
Accounts Payables	265	891	628	869	970
Others	443	991	722	674	674
Total current liabilities	888	2,514	2,629	2,346	2,397
Long term loans	31	31	22	19	19
Others	0	35	41	40	40
Total liabilities	919	2,580	2,691	2,405	2,456
Non-controlling interest	21	18	38	36	36
Shareholder Equity	1,029	1,058	1,709	3,770	4,247
Cashflow Statements (Bt mn)					
CFO					
PBT	113	164	493	735	989
Adjustments	76	110	211	(69)	(128)
Cash from ops before WC changes	189	275	704	666	861
WC changes	(174)	262	(865)	(131)	(23)
Cash generated from ops	14	536	(161)	535	838
Taxes paid, net	(52)	(69)	(137)	(176)	(194)
Interest paid	(19)	(39)	(105)	(90)	(77)
Cashflow from ops	(57)	429	(404)	270	568
CFI					
CAPEX, net	(18)	(26)	(23)	(26)	(34)
Dividends from associates & JVs	0	0	0	0	0
Dividends/Interest from Investments	0	0	0	0	0
Purchase/sale of investments	(0)	0	(0)	(0)	0
Investments in subs & associates	0	(615)	(583)	(1,000)	0
Others	(23)	(82)	23	(162)	(38)
Cashflow from investments	(40)	(723)	(583)	(1,188)	(72)
CFF					
Share issuance	463	26	280	1,620	0
Purchase of treasury shares	(113)	(52)	96	210	0
Loans, net of repayments	(16)	404	743	(510)	(50)
Dividends to minority interests	0	0	0	0	0
Dividends to shareholders & capital reduction	(102)	(35)	(129)	(227)	(318)
Others	0	0	0	0	0
Cashflow from financing	232	343	991	1,093	(368)
Net change in cash	135	48	4	175	127
Effects of exchange rates	0	0	0	0	0
CCE, end	165	201	204	368	484

Source: PSR est.

Ratings History



Phillip Group Rating System

Total Returns	Recommendation	Rating
> +20%	Buy	1
+5% to +20%	Accumulate/Trading Buy	2
-5% to +5%	Neutral	3
-5% to -20%	Reduce/Trading Sell	4
> -20%	Sell	5

Remarks

We do not base our recommendations entirely on the above quantitative return bands. We consider qualitative factors like (but not limited to) a stock's risk reward profile, market sentiment, recent rate of share price appreciation, presence or absence of stock price catalysts, and speculative undertones surrounding the stock, before making our final recommendation

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Sasikorn Charoensuwan, CFA, CAIA Rutsada Tweesaengsakulthai	Capital Market Investment Analyst#9744 Securities Investment Analyst#17972	662 635 1700#480 662 635 1700#482	Consumer, Commerce ICT, Energy, Health Care
Danai Tunyaphisitchai, CFA	Capital Market Investment Analyst #2375	662 635 1700#481	Construction Materials, Property Development
Naree Apisawaittakan	Securities Investment Analyst #17971	662 635 1700#484	Agro & Food, Electronics
Siam Tiyanont	Securities Investment Analyst #17970	662 635 1700#483	Transportation, Media & Publishing, Tourism
Ornmongkol Tantitanatorn	Capital Market Investment Analyst #34100	662 635 1700#491	Automotive, Energy, Packaging
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Results Presentation

Score Range	Number of Logo
Less than 50	No logo given
50 - 59	
60 - 69	
70 - 79	
80 - 89	
90 - 100	

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