

Boustead stays the course

by Jeffrey Tan

Property and engineering group Boustead Singapore is tackling one of the worst crises in its history – the Covid-19 pandemic. But the conglomerate’s conservative approach under chairman and group CEO Wong Fong Fui should help it weather the storm.

The founding of Boustead Singapore in 1828 makes it one of Singapore’s oldest companies – if not the oldest engineering and property company.

Its continued existence today means that the conglomerate has survived wars, health and economic crises that have occurred in the last two centuries.

These included the 1918 flu pandemic, Second World War, Indonesia-Malaysia Konfrantasi, Asian Financial Crisis, the SARS epidemic and the Global Financial Crisis.

At present, the company faces yet another earth-shattering challenge – the Covid-19 pandemic. Unlike previous crises, the novel corona virus has proven to be a different beast given today’s highly globalised and interconnected world. Its economic impact has been unprecedentedly deep and wide owing to various lockdowns imposed by countries to curb its spread.

Yet, based on its latest financial statements, Boustead seemed to have dodged the Covid-19 bullet. For FY2020 ended March 31, the company’s revenue was up 54.4% y-o-y to \$726.6 million although earnings were down 5% y-o-y to \$30.9 million. NAV per share was also higher at 70.3 cents from 68.2 cents a year ago. And the company had a net cash position of \$162.7 million as at March 31.

To put it into the right perspective, Boustead’s latest financial statements only accounted for its performance and position up till March 31, before Covid-19 hit pandemic proportions. Boustead’s full-year results therefore compared favourably to the awful performance

many Singapore-listed companies posted in the fiscal quarter ended June when Covid-19 was at its worst.

For instance, Keppel Corp recorded a huge impairment of \$930 million, leading it to report a net loss of \$537 million. Sembcorp Industries was weighed down by exceptional items amounting to \$161 million under its energy business and losses posted by its former subsidiary Sembcorp Marine which has been demerged. Jardine Cycle & Carriage’s multiple businesses across Southeast Asia were also hit, sending its earnings and revenue down 30% and 28% y-o-y to US\$301 million (\$413 million) and US\$6.6 billion, respectively.

Without a doubt, Boustead’s earnings for the next quarter should reflect the full effects of the pandemic, given the company does business in 89 countries and territories, most which are still in the grasp of Covid-19.

To be sure, the March collapse in crude oil prices as a result of lower oil demand was also a negative for Boustead’s energy-related engineering business. The suspension of construction activities to halt the spread of Covid-19 also impacted the company’s real estate business via its listed subsidiary Boustead Projects.

Meanwhile, investment and business uncertainties caused by Covid-19 delayed the signing of deals for its geospatial technology solutions. Finally, the company’s fledgling healthcare business is still finding its foot and has yet to make significant contributions to the company.

So, how badly will Boustead perform ahead? And will its diverse set of businesses be able to cushion the impact of Covid-19?

Focus on cash flow

Under its energy-related engineering division, Boustead designs, engineers and supplies process heater systems, waste heat recovery

units, process control systems, and water and wastewater treatment plants. These installations are for the oil and gas, petrochemical and power industries. Through Boustead Projects, the company designs and builds business parks and industrial properties in Singapore, China, Malaysia and Vietnam. Boustead owns 53% of Boustead Projects.

At its geospatial technology division, Boustead is the exclusive distributor of Esri ArcGIS technology, a geographic information mapping software that provides location analytics. Set up just two years ago, the healthcare division provides medical solutions that address age-related chronic diseases and mobility issues. It is also involved in rehabilitative care, sleep care and sports science in Asia Pacific.

Wong Fong Fui, chairman and group CEO of Boustead, says the company's philosophy has always been to stay conservative. The focus of each business is to generate positive cash flow and not hype. "We don't treat the businesses as such," he tells *The Edge Singapore* in an interview.

Nevertheless, each business requires a different strategy given their unique operating environments, adds Wong. For instance, the 2014 crash in crude oil prices led Boustead's energy-related engineering division to change the type of projects it pursues.

It is now focused on maintenance and repair services for existing installations, instead of merely focusing on the design and construction of new plants and equipment. While such jobs are long, tedious and smaller in contract value, Wong says the margins are better and they provide recurring income. He notes that the new focus has helped the division secure record orders, comprising almost three quarters of the \$396 million in total new contracts secured in FY2020.

The exit of some of Boustead's competitors over the last few years have also led to a stronger order book for the division, says Wong. He claims some clients of surviving competitors had switched over to Boustead because they trusted the latter to complete the job. "So, we have benefited from being a conservative and reliable company with a strong balance sheet," he adds.

Wong also says the division's niche has broadly shielded the company from the downturn in the oil industry. In particular, the company's UK-headquartered subsidiary Boustead International Heaters (BIH) had successfully

secured a \$100-million contract to deliver waste heat recovery units for a major energy infrastructure project in Europe. This was BIH's largest contract ever, enabling it to hit a new order book high of \$304 million during FY2020.

Still, the oil industry is mired in a multi-year slump. And things look unlikely to improve any time soon following the recent crash in crude oil prices. The prolonged downturn has led to the divestment of oil-related businesses.

On June 8, Sembcorp — led by Temasek Holdings — announced the divestment of its stake in Sembmarine. If market consensus is to be believed, Temasek is also trying to pry Keppel Offshore & Marine away from Keppel, although the move was thwarted by the non-fulfilment of a material adverse changer (MAC) pre-condition. So, what is holding back Boustead from divesting its energy-related engineering business?

Wong says he still sees value in the division given that it is an asset-light and people-oriented business. And, if the company had intended to sell it, the timing is not right, he adds. "We have gone through these ups and downs and proven that our methodology seems to be working. Whether it will continue to work, time will tell. But we are lean. We have no [significant] capital and equipment investment," he says.

Despite all the push towards sustainability, Wong is not quick in leading the company to diversify into the renewable energy sector. While he acknowledges that recent advancements in technology have driven down the costs of renewable energy, the opportunities are still small compared to fossil fuel energy sources. And the latter will still constitute a significant portion of the energy mix in the foreseeable future, he adds.

In hibernation

At Boustead Projects, the ill effects of the pandemic were more acutely felt. At the height of the pandemic in 2Q2020, Singapore had reported more than 1,000 Covid-19 cases a day. This was driven largely by the spike in cases among transient workers living in dormitories. As a result, many construction workers were put under quarantine and construction activity came to an almost complete standstill, albeit temporarily.

To be sure, Boustead Projects does not directly employ transient workers. But it relies on subcontractors, most of whom hire foreign

labour. As a result, Wong says Boustead Projects was forced to pause all its local construction projects.

"Basically, we are hibernating. But we still pay for fixed expenses. As long as Singapore cannot control Covid-19 infections among the foreign workers, we are held at ransom. The whole industry is crying, not only us. It is a disaster," he says.

The construction industry has since restarted under Phase Two reopening on June 2 after the "circuit breaker" period – Singapore's version of lockdown. But the process has been slow and gradual. While the subsidiary has obtained approval to restart its construction projects, Wong says that is not the case in practice as many of those working on its projects are still under quarantine.

The need to comply with social distancing measures in the construction industry is an added pain. Wong says a lot of the rules and regulations seem impractical. "I wouldn't criticise and say whether it is right or wrong. It is for the greater good of the society. But it comes at the expense of the construction industry in terms of financial point of view," he laments.

Then there is the risk of subcontractors going bust. If that happens, Boustead Projects would have to seek a replacement to complete its projects. "Their problem will become our problem," he says.

Wong concedes there is little that Boustead Projects can do now. The subsidiary's return to full strength depends largely on the availability of foreign workers and the relaxation of social distancing measures. "We just have to learn how to work and slowly bring activities back to full strength. It won't be immediate," he says.

Still, if it is any consolation, Boustead Projects' overseas operations are faring better. Wong says the subsidiary's project management in China is progressing well despite the social distancing measures. "On the surface, the Chinese appear very stringent on measures to halt Covid-19. But in our experience, they are very practical," he says. The construction projects in Malaysia are also progressing well, he adds, because the country's reliance of foreign construction labour is lesser compared to Singapore's.

Meanwhile, the infection rate among dormitory residents in recent weeks has trickled to double-digits a day, according to the Ministry

of Health. Many of the nearly 54,000 Covid-19 cases involving dormitory residents or 16.7% of the total dormitory resident population have also recovered. This may allow more construction workers to return to work.

Nevertheless, Boustead Projects' next set of financial results will not look "pretty", admits Wong, despite the subsidiary's rental income that may offset some of the impact. This will weigh on Boustead, given that the real estate division in FY2020 contributes almost 60% and 63% to its revenue and earnings.

Marketing boost

Fortunately, Boustead's geospatial technology division may be less impacted by the pandemic compared to the energy-related engineering and real estate division.

According to Yu Loon, Wong's eldest son and executive director and deputy group CEO of Boustead Singapore, governments and related agencies, who form the bulk of clients, are not in the "mood" to sign deals right now. Instead, they are more concerned about not blowing their budgets given the enormous spending on financial relief and aid to prop up their respective economies and industries, he explains.

"There are still feelings of nervousness. It's like they are asking themselves: Should we spend so much money? The longer-term concern is whether they are in a position to spend down the road. They might want the product, but because of all these budget deficits, they want to be careful," says Yu Loon, who was present at the same interview.

In response to the hesitation to sign deals, Yu Loon says the division had tweaked the way it markets its products. It is now promoting the Esri ArcGIS software as a cost-saving and resource-optimisation tool. The software has also been positioned as a disaster response program to help fight the spread of Covid-19. Government health agencies can use the software to map out hospitals with sufficient ventilators and plot them against the vulnerable population. It can also determine the best locations to set up testing sites.

The initial results have been positive. "Recently, it has been better," Yu Loon says. "There is an underlying demand for those services."

The division has also given out free trials of the Esri ArcGIS software to new clients. The hope

is clients will be converted to paid subscribers after using the software. Thus far, the division has not seen new subscribers as the trial period is not over yet, he says.

In the private sector, demand has also seen an “uptick”, although this is from a small base, according to Yu Loon. Companies are using the Esri ArcGIS software as part of their business contingency plans, he notes. “So, these are specific solutions to help businesses keep track of which facilities are affected. Companies are able to determine the best way to manage these facilities and employees from a location point of view,” he says.

‘Very much on the learning curve’

Finally, the healthcare division is still a work in progress. For FY2020, this business generated earnings of only \$844,000, up 16.7% y-o-y, from \$723,000. Revenue came in at \$18.2 million, up 60% y-o-y, from \$11.4 million.

The healthcare division’s less than impressive performance can be attributed to the fact that it started only two years ago. Boustead had fully acquired WhiteRock Incorporation (WRI) for \$19 million in 2018. The latter comprises a group of 16 healthcare entities operating in Singapore, China, Hong Kong, Malaysia and Thailand.

“At the moment, we’re still very much on the learning curve,” says Wong. “The healthcare business is not making much money but neither is it losing money.”

The other reason for the less than impressive performance is the division’s incoherence due to the involvement in different segments of the healthcare industry. According to Yu Loon, WRI’s healthcare entities are involved in many different segments of the healthcare industry, such as rehabilitative care, sleep care, sports science and mobility for the elderly. However, only seven are key operating entities, he points out.

“So, there are various things in there and we’re trying to figure out which to focus on, which are the areas that can be streamlined into a consistent sales and delivery mechanism,” Yu Loon says. “The immediate task at hand is to make it a coherent operating business as opposed to a collection of businesses.”

Wong admits that he has often been asked why Boustead acquired WRI, knowing that he has no prior experience in the healthcare

industry. But he says that the company can acquire the relevant expertise to run and grow the healthcare division.

Wong believes that healthcare is a “sunrise industry” given that the ageing population in Asia will accelerate in the coming years. According to the United Nations Population Fund, one in four people in Asia will be over 60 years old by 2050. The number of 60-year-olds will triple between 2010 and 2050, reaching close to 1.3 billion people.

Yu Loon adds that by having the healthcare division, Boustead will be able to balance its exposure to contract-based businesses, namely the energy-related engineering and real estate divisions. He points out that such businesses often face high risks with low margins. “So, you really got to know your stuff. The risk of any misstep would be horrendous, as we have learned from other occasions,” he says.

Thankfully, that seems not the case for the healthcare business due to its nature and growth prospects. “I think the consequences of missteps are a little bit more affordable,” he says. “The risk is manageable.”

Analysts still positive

Shares of Boustead have endured a rollercoaster ride so far this year. After plunging to a 12-month low of 56 cents in March amid a worldwide sell-down, the stock has regained some lost territory to close at 70.5 cents on Sept 9. But it is still down 6.6% year to date. At that price level, the stock is trading at 11.8 times earnings and 1.04 times book value. The stock has a 12-month trailing dividend yield of 4.3%.

Shares of Boustead Projects, too, reflect a similar movement, closing at 77 cents on Sept 9. Like Boustead, the stock is down 16.3% year to date. At that price level, the stock is trading at 10.9 times earnings and 0.8 times book value. The stock has a 12-month trailing dividend yield of 1.04%.

CGS-CIMB Research, which is the only active analyst covering both companies, is staying optimistic on Boustead. The brokerage reckons that the company’s geospatial technology division will continue to see strong demand from government agencies in Southeast Asia and Australia. It has forecast the division to record pre-tax earnings growth of 7.5% to \$31.9 million in FY2021.

It also reckons that the energy-related engineering division will do well on the back of a strong order backlog despite the low crude oil prices. The brokerage has forecast the division to record pre-tax earnings growth of 61% to \$12.7 million in FY2021.

However, CGS-CIMB believes that Boustead Projects will continue to face headwinds. The research house expects the company to experience a staggered return to normalcy post-circuit breaker, given the labour constraints and new conditions for working in the post-circuit breaker era.

Hence, it expects Boustead Projects to record a 44% drop in revenue in FY2021 due to the slow reopening of the construction industry. CGS-CIMB has also lowered its FY2021 and FY2022 earnings per share forecasts by 38% and 63%, respectively, in view of that.

Nevertheless, the brokerage expects the company's leasing segment to remain "relatively resilient" in FY2021. This is because

most of its industrial properties are single-tenanted and leased to blue-chip MNCs.

"We understand that the rental collection rate remains high, and [the company] is actively working with a handful of tenants affected by Covid-19 to assist them with deferment of rental payments," CGS-CIMB analysts Ong Khang Chuen and Caleb Pang Huan Zhong wrote in a July 14 report.

In fact, the brokerage believes that Boustead Projects could spin-off some of its properties into a real estate investment trust this year or next. "We think such a move could unlock significant value, as [the company]'s investment properties are accounted for at cost less depreciation," say the analysts.

CGS-CIMB has maintained its "add" recommendation for Boustead with an unchanged target price of \$1.00. The brokerage has also kept its "add" call for Boustead Projects, but lowered its target price to 88 cents from 93.1 cents previously.