ISOTEAM LTD.
(Company Registration No: 201230294M)
(Incorporated in the Republic of Singapore on 12 December 2012)

RESPONSE TO QUERIES FROM THE SECURITIES INVESTORS ASSOCIATION (SINGAPORE) ON THE ANNUAL REPORT FOR FY2021

The Board of Directors (the "**Board**" or "**Directors**") of ISOTeam Ltd. (the "**Company**" and together with its subsidiaries, the "**Group**") refers to the queries raised by the Securities Investors Association (Singapore) in relation to the Company's Annual Report for the financial year ended 30 June 2021 ("**FY2021**") and appends the replies as follows:

Question 1

In the joint message from the chairman and the CEO, it was said that the challenges faced by the group as a result of the pandemic are unlike any that the two of them have encountered in more than 20 years in the business.

The border controls have led to a manpower crunch and the price of essential raw material has increased exponentially due to supply chain disruptions. The COVID safe management measures have also reduced workers' productivity and the group is left to face with the risk of stop-work orders should any of its workers be tested positive for COVID.

Nevertheless, the chairman and CEO maintained that the group has continued to tender for new projects to beef up its order book, "*like what we have always done through both good and bad times*" (page 8 of the annual report).

(i) **Can the board/management help shareholders reconcile the operational risks (as highlighted above and in the joint message) and the group's continued participation in tenders?**

(ii) **How does management determine the tender prices to ensure that tenders, if won, would be profitable and would not result in losses for the group? What are the risks that the group will end up in a situation of "do-more, lose-more" given the risks of stop-work orders and the unpredictable cost pressure in manpower and raw material?**

(iii) **How much flexibility does management include in its contracts to protect the group from external/COVID-19 related costs increases that are beyond the group's control?**

(iv) **The use of drones to inspect the external façades of HDB blocks was highlighted as a means by the group to increase its productivity (page 8). Has management secured all necessary permits for the use of unmanned drones at its construction sites?**

(v) **Does management see any silver lining during the pandemic?**

Company's response

i. The Group is accountable to many stakeholders including our shareholders who expect returns from their investment and also our employees' whose livelihoods depend on the sustainability of the business. As such, we cannot stand still and wait for COVID-19 to be over because that is unlikely to happen any time soon. We have to move forward and keep on tendering for new business while taking the cue from the Government that Singapore will soon reach an endemic stage in the fight against the virus.

We want to maintain a healthy order book at all times and believe that COVID-19 Safe Management Measures will continue to be in practice even when our borders gradually reopen. As such, we have factored in the impact of this operating landscape into our recent tender prices too.

We have to ensure that we do our best to continue our operations within the constraints and limits of COVID-19 restrictions, while taking steps to protect our staff by making sure that they have all the necessary knowledge and protective gear to stay safe while carrying out their duties.

ii. We are unable to disclose our pricing strategy for competitive reasons, safe to say that we take into account material and manpower costs as well as margins. A point to note is that ISOTeam has always pride itself for its track record and reputation for quality workmanship and on-time delivery. This has won our Group many public tenders despite not always being the lowest tenderer because we believe that our customers recognise our worth.

Since the outbreak, our team and our people are accustomed and well prepared to handle the COVID-19 Safe Management Measures and controls. We are currently exploring a few Government channels to recruit more new foreign workers for certain categories of projects. Early indications are encouraging and we hope that will ready the Group to take on new projects in the future.

iii. We do our best to negotiate for more favourable terms with suppliers of raw materials but this is not easy as it depends on market forces. To manage overall costs, we also review expenses that we have more control over and this includes staff costs. In FY2021, the C-suite level executives as well as business unit heads all took pay cuts to help the Group to tide through this difficult period while adopting a 'zero retrenchment' policy as we view our people as the greatest asset of ISOTeam.

iv. The use of drones for building inspection is widely supported by the Government. In fact public organisations like the HDB and JTC have already commenced using drone-captured images and AI for building inspection and predictive maintenance. The tenders for each project come with the necessary permits. On 22 October 2021, we announced a collaborative agreement with a technology partner to deploy AI and drone technology for building façade inspections.

v. It has definitely accelerated digital transformation and spurred us to explore more areas where we can leverage technology to reduce our costs as well as our reliance on manpower while increasing operational efficiency. During the lockdown period, we used the time to upgrade an app which we developed in-house that allows our project supervisors to oversee worksites without having to be physically present. Our project supervisors had also trained with our technology partner to operate drones during that period. Together with the app, we are able to operate the drones remotely. This reduced travelling time as they can now conduct more site inspections per day and at higher frequencies.

Question 2

The chairman and CEO highlighted that the group has always been forward looking and has an enviable track record in many of the Government's infrastructure projects. In FY2021, the group further cemented its partnership with Sunseap Group and completed the deployment installation of the largest floating solar farm in the marine coastal environment at the Straits of Johor, off Woodlands.

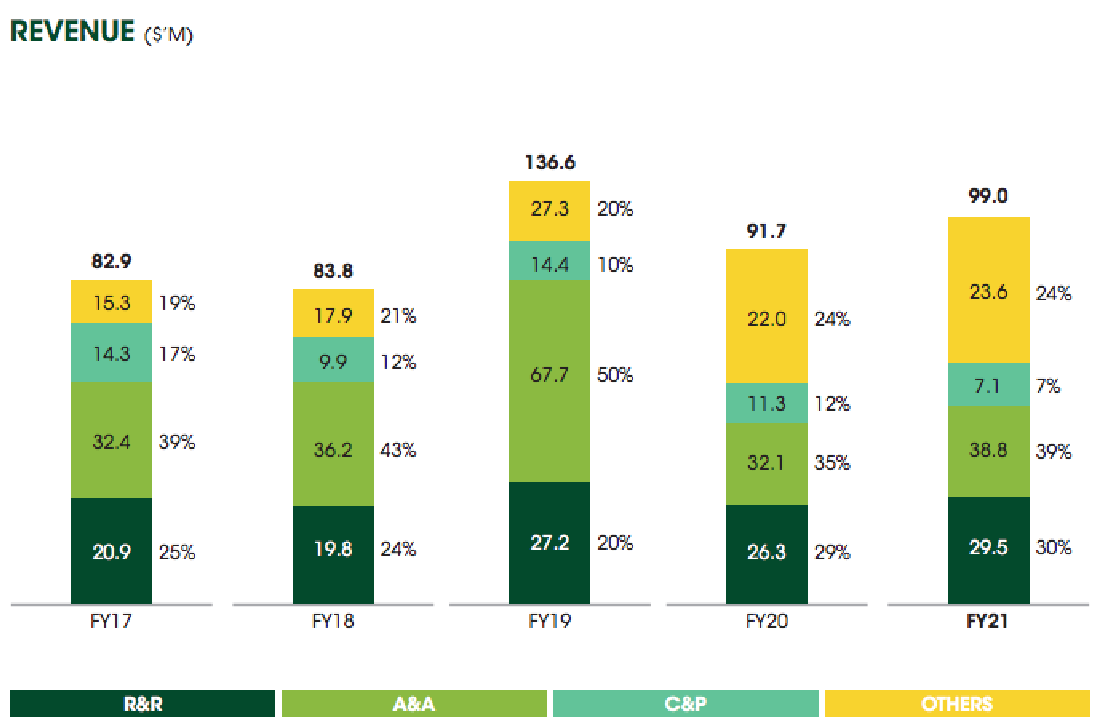
There are also opportunities in:

- URA's Landscaping for Urban Spaces and High-Rises ("**LUSH**") programme
- HDB Green Print programme

- Ongoing public sector infrastructure upgrading projects, including Neighbourhood Renewal Programme; the expanded Home Improvement Programme; and the upgrading of older MRT stations

The group's successful IPO in July 2013 was built on more than a decade of Repairs & Redecoration ("**R&R**") and Addition & Alteration ("**A&A**") experience. Since the IPO, it has diversified into Coating & Painting ("**C&P**") and "**Others**" which included bike sharing, interior design and home retrofitting.

A 5-year snapshot of the breakdown of the group's revenue can be seen on page 6 and reproduced below:



(Source: company annual report)

(i) **Can management elaborate further on the growth drivers in R&R and in A&A? From the Financial highlights, revenue from R&R and A&A increased gradually although there was a big jump in A&A revenue in FY2019 which quickly normalised in FY2020. Has the group consolidated its position in the R&R and A&A markets and gained additional market share?**

(ii) **Is management sufficiently focused on R&R and A&A in the past 3-5 years given the group's ongoing evolution/diversification?**

(iii) **In particular, would management elaborate further on the business case of SG Bike? What is the strategic value of SG Bike? Does management expect SG Bike to turn into a significant revenue and profit generator for the group in the mid-long term? What is the targeted ROI on SG Bike in the board approval process? From the consolidated statement of comprehensive income, the loss attributable to non-controlling interest was $(959,000) (FY2020: $(2.4) million) although the figure would include the results from Zara@ISOTeam Pte. Ltd., SG Bike Pte. Ltd and ISO-Homecare Pte. Ltd..**

(iv) **Similarly, as the group looks for opportunities in new programmes such as LUSH, HDB Green Print, how does management balance the need to participate in new growth areas and the need to be selective in committing management's time and**

capital into segments which have long runway and can scale up meaningfully and profitably?

(v) As a partner "working" with Sunseap, does the group develop and own any intellectual property? For example, in the construction and installation of offshore solar farms, is the group just a sub-contractor carrying out installation according to Sunseap's project plans or does the group offer its expertise to provide Sunseap with a turnkey solution?

(vi) Are there any business opportunities and/or current working relationship with Taisei Oncho Co., Ltd? Taisei Oncho Co., which is headquartered in Tokyo, Japan and listed on the JASDAQ Securities Exchange, is an established mechanical and electrical ("M&E") engineering firm that is primarily involved in design and contract work for air conditioning, plumbing, electrical installation work, maintenance and renovation services. Taisei Oncho holds a 17.94% stake in the company.

(vii) In addition, the company announced that it has plans to restructure its commercial interior design business when it announced the proposed disposal of the Pure Group entities (see Qn 3). Would the board be reviewing the group's diversification strategy and its results, especially in areas with seemingly low barriers of entry (e.g. interior design)? Should the board provide more guidance to management to be more selective in its diversification and only allocate capital to new services where the group can scale up meaningfully (relative to the group's current size)?

(viii) The group currently operates with a headcount of 302 employees (FY2020: 366), following 91 resignations in FY2021 alone (FY2020: 18). How does management ensure that the group has sufficient and experienced human capital to compete effectively in the group's operating segments? How is management looking to address the issue of "*intense competition in the market for a smaller pool labour*" (page 27)?

<u>**Company's response**</u>

i. In a nutshell, R&R and A&A activities are largely driven by Government initiatives and greening trends. The Singapore Green Plan 2030 is a national sustainability movement which seeks to address climate change. The Group's track record and experience in R&R and A&A projects both in the public and private sectors well-positions us for opportunities in these areas.

With the impact of the pandemic, there is a substantial contract backlog situation across most of the Town Councils, mainly pertaining to mandatory upgrading works like R&R or Neighbourhood Renewal Programme ("**NRP**"). As such, we foresee that more contracts or tenders will be called when the COVID-19 situation in Singapore further stabilises.

Government and green initiatives that present opportunities for the Group's R&R and A&A business:

- Town councils, BCA and NParks
  - Mandated repainting of external walls of buildings every five years
  - Mandated inspection of façades of buildings that are over 20 years old every seven years
  - Regular development, maintenance and upgrading of parks
  - NParks to expand cycling network to 1,320km by 2030 which will need to be refurbished from time-to-time

- HDB and NEA
  - Projects to rejuvenate and enhance estate amenities regularly such as the NRP every 12-15 years and Hawkercentre Upgrading Programme.
  - HDB Green Print that promotes green building technology like cool paint and community garden and cycling path network for a greener and cooler neighbourhood

- MND and HDB
  - Ongoing and upcoming upgrading of HDB flats under HIP, Extended HIP and HIP II programmes - there are about 173,000 flats eligible for HIP but are pending selection; another newer batch of 230,000 flats built between 1987 and 1997 under Extended HIP; and another cycle of upgrading under HIP II when flats reach 60-70 years old

- LTA
  - Rejuvenation of aging MRT stations, rail, and bus depots through A&A

The Group's market position in R&R and A&A in Singapore remains stable despite the impact of the COVID-19 pandemic.

ii. R&R and A&A remains our core bread and butter business contributing 68% of revenue in FY2021 (FY2020: 58%). We have since improved our market share in both R&R and NRP segments too.

iii. ISOTeam takes pride in being an eco-conscious company offering green methodologies, services and products that are environmentally sustainable. As articulated repeatedly in the past, SG Bike supports the Singapore's aspiration for a cleaner, greener mode of transportation and also reflects the Group's commitment to sustainability.

R&R and A&A remain the core bread and butter business of the Group in the foreseeable future. Certain investment metrics remain private and confidential to the Board.

iv. There is no crystal ball when it comes to investing. When we consider a new business growth area, the Group always do our homework and is guided by discipline and prudence. Usually the new area is complementary / synergistic to our existing business or fills a gap that we identify in the built environment value chain. Once the new area is identified, we conduct detailed research and analysis before embarking on the plan.

An example is our Green strategy, where the Group saw the potential of the sustainability movement early on and decided to go green in 2010, gradually building our services, capabilities and products around it. While we integrated green programmes in most of our work processes, our first meaningful renewable energy project was secured in 2016 and this was followed by the contract for the largest offshore solar farm in Singapore that was secured in 2019.

v. It is a collaborative partnership where we bring our years of installation experience and expertise to the table. As we are an integrated player with multi-disciplinary capabilities, we can also provide turnkey solution and value add in certain areas such as mechanical and electrical engineering as well as floating systems capabilities.

vi. Taisei Oncho Co., Ltd ("**Taisei Oncho**") which is headquartered in Tokyo, Japan and listed on the JASDAQ Securities Exchange, is an established mechanical and electrical ("**M&E**") engineering firm that is primarily involved in design and contract work for air conditioning, plumbing, electrical installation work, maintenance and renovation services. Taisei Oncho holds a 17.94% stake in the company.

Taisei Oncho provides technical advice for a number of the Group's M&E projects, and there will be other business opportunities for us to work together.

vii. We would like to clarify that the statement "to restructure its commercial interior design business" was in direct and specific reference to the Pure Group entities, which has since been disposed of. The Group is of the view that the Board currently provides adequate guidance and counsel to management in the areas under their purview.

viii. Of the 91 resignations, most of them are foreign talents who returned to their home country and were unable to come back to Singapore due to border control measures. The remaining are from the Pure Group Singapore which we had disposed of.

The shortage of migrant workers is a structural issue due to the entry restrictions imposed by the authorities to curb the spread of COVID-19. While it is challenging, it is also an opportunity for companies in the built environment to think out of the box and shine in the new normal.

As shared in the Joint Chairman and CEO Message on pages 8 to 9 of the Annual Report, we are exploring ways to tap on technology to improve our productivity and manpower deployment in order to reduce our reliance on manual labour.

Some examples cited are the app developed in-house to conduct remote site inspections and the use of drones for external facade inspections. In addition, we have adopted other digitalisation initiatives such as e-Inventory, e-Purchase, e-Marketing, e-Invoice, e-Payment, e-Inspection, e-Report which are relatively less labour intensive.

<u>Question 3</u>

On 12 October 2021, the company announced that the disposal of the Pure Group entities has been completed for $4.5 million in cash. The proposed disposal was first announced on 17 September 2021 and SGX Regco had queried the company over the proposed disposal.

The Pure Group was only just acquired on 21 January 2020 for a consideration of $12.0 million settled in cash (page 106) with an additional $12.0 million to be settled by Consideration Warrants based on the target companies achieving the profit targets.

(i) **During the acquisition of the Pure Group entities, the completion date was delayed twice. What were the reasons for the delays in the acquisition? With the benefit of hindsight, could the delays be viewed as an early warning sign that there are difficulties and/or challenges in the due diligence process?**

(ii) **How much of the lower-than-expected financial and operational performance of the Pure Group entities could be attributed to COVID?**

(iii) **The company has provided the seller with contingent consideration arrangement of up to $12.0 million in consideration shares if the Pure Group entities achieved a profit target of $3 million and $5 million in FY2020 and FY2021 respectively. Did the board consider introducing a claw-back mechanism of the $12 million cash payment during the deal negotiation if Pure reports any losses in the financial years ended 30 June 2020 and 30 June 2021?**

(iv) **Instead of a $12.0 million cash payment as the first tranche, did the board try to negotiate for a part-cash and part-shares as the first payment to the seller?**

In Note 16 (page 104 – Investment in subsidiaries), the company has invested more than $52.4 million in subsidiaries and recognised impairment of $15.96 million as at 30 June 2021. This is before the completion of the disposal of Pure Group which took place on 12 October 2021.

The impairment losses on goodwill in the past years are $(2.299) million in FY2021 and $(5.802) million in FY2020 (restated). For the acquisition of Pure, the company recognised goodwill of $12.34 million (page 107).

(v) **Does the board consider it timely to review the group's M&A track record and finetune its acquisition strategy so that M&A leads to long term sustained value-creation for all shareholders?**

(vi) **What is the guidance given by the board to management on deal structuring, especially in ensuring that the group does not overpay for its acquisitions and that the terms are fair and balanced to recognise the upside and to protect the group from the downside?**

Company's response

i. The necessary due diligence process was conducted by the Group's internal teams as well as qualified third parties. As mentioned in the Group's announcement dated 7 January 2020, the Company had performed financial due diligence on the Pure Group entities and had also commissioned an independent professional valuer to undertake a valuation of the entities prior to the acquisition in 2020. However, the due diligence process for the Pure Group's overseas entities took longer than expected.

As such, there is no validity to suggest that the timeline changes were early warning signals.

ii. The COVID-19 pandemic had a significant adverse impact on the global economy and the construction and built environment sectors which the Pure Group operates in were not spared. The Pure Group entities were not able to function normally across their regional operations due to the protracted cross-border lock downs and entry restrictions. This has significantly impacted the financial performance of the Pure Group especially its oversea entities.

iii. The entire purchase consideration was arrived at after negotiations on a willing-buyer and willing-seller basis taking into account, amongst others, a valuation of the Pure Group entities by an independent professional valuer prior to the acquisition in 2020.

A part-cash and part-shares structure was concluded in comparison with other mechanisms. The challenging operating environment since the outbreak of COVID-19 had resulted in Pure Group recording losses for FY2020 and FY2021 and revenue visibility continues to be clouded by the pandemic. As such, the Management and Board are of the view that a disposal was in the best interests of the Group and its shareholders.

iv. The entire transaction to acquire the Pure Group entities was already on a part-cash and part-share basis.

v. Many of the Group's acquisition targets were our sub-contractors that had been part of our growth journey and long-time partners that we had work together with for many years. When we embarked on a strategy to transform into a group with multi-disciplinary capabilities, it made commercial sense to pursue profitable targets with proven track records with whom we already have mutually beneficial relationships.

Until the Covid-19 outbreak, which affected the construction industry severely, our group of companies had been doing well and in fact we hit record highs in both revenue and profit in FY2019.

vi. When setting up the framework for the deal, we consider all but not limited to the following factors:

- Customer and employee contracts
- P/E ratio
- Independent third-party valuation
- Financial and legal due diligence
- Potential synergy
- Forward earning potential in normal business environment

By Order of the Board

Koh Thong Huat
Executive Director and Chief Executive Officer
26 October 2021

This announcement has been prepared by the Company and its contents have been reviewed by the Company's Sponsor, Hong Leong Finance Limited. It has not been examined or approved by the Exchange and the Exchange assumes no responsibility for the contents of this announcement, including the correctness of any of the statements or opinions made, or reports contained in this announcement.

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