DESIGN STUDIO GROUP LTD.
(Incorporated in the Republic of Singapore)
(Co. Reg. No.: 199401553D)

RESPONSE TO QUERIES FROM SGX-ST IN RELATION TO COMPANY'S UNAUDITED 4QFY2018 FINANCIAL STATEMENTS ANNOUNCEMENT ON 23 FEBRUARY 2019 (the "COMPANY ANNOUNCEMENT")

The Board of Directors of Design Studio Group Ltd. (the "**Company**", and together with its subsidiaries, the "**Group**") refers to the below queries raised by the Singapore Exchange Securities Trading Limited ("**SGX-ST**"), and wishes to provide its responses as follows:

SGX Query 1

As at 31.12.2018, trade payables had increased significantly due to increases in the 'amount due to third parties' and 'accrued contract cost' respectively. The amount due to third parties increased from $7 million on 31.12.2017 to $19.8 million on 31.12.2018 and 'accrued contract cost' increased from $13.5 million on 31.12.2017 to $45.1 million on 31.12.2018. Please explain what led to the substantial increases in the trade payables due to third parties and accrued contract cost and reasons for the substantial amounts outstanding, respectively.

Company's Response

There was an increase in project activity undertaken in 2018 and more subcontract works contracted to third parties in the projects segment (Singapore, Malaysia and International Business Units). There was also a longer period taking place for the subcontractor work approval and invoicing process – leading to an increase in 'accrued contract cost' and subsequently also to the payment cycle – leading to an increase in the 'amount due to third parties'.

SGX Query 2

As at 31 December 2018, the Company had obtained a bank facility which required the Group to maintain a minimum tangible net worth of $80 million. Despite not being able to meet the minimum requirement of $80 million, the Group stated that "as at to-date, the Group has obtained a waiver from the bank on the breach of loan covenant". Please disclose specific details of the size and maturity date of the bank loan, the interest payable, any other material terms of the bank loan and the terms on which the waiver was granted by the bank.

Company's Response

As at 31 December 2018, the bank loan amounted to S$3.0 million (as disclosed in 1b(ii) Page 8 of the Company's Announcement). It is due on 6 March 2019 with interest chargeable at 1.5% per annum over the Singapore Interbank Offered rate. The loan has been extended till 6 June 2019.

The bank has granted a waiver to the Group on the condition that the Group accepts the revised banking facilities containing a new condition that no dividends are to be paid if the Group is in a net loss after tax in the financial year.

SGX Query 3

The Company reported a loss after tax of $23.9 million in FY2018 from a profit after tax of $1.5 million for FY2017. The Company explained that $19.1 million was due to "one-off items". Please elaborate on how the remaining loss of $6.3 million was incurred in FY2018 noting that revenue actually rose 21.4% to $168.8 million.

Company's Response

The remaining loss of $6.3 million was due to lower margins on projects, impacted by the market conditions in Singapore and project cost overruns. The lower margins on projects along with company operating expenses has led to the Company's loss after tax position.

SGX Query 4

With respect to the Company's reported $19.1 million loss arising from "one-off items" in FY2018, please provide further information on the components of the "one-off" loss, as follows:

a. The Company had explained that a one-off loss of $7 million arose from losses in manufacturing operations due to lower manufacturing activity levels. However, based on segmental information, we note that the manufacturing sector revenue (external customers) decreased by only $2 million from $17.6 million to $15.2 million. Please provide a breakdown of the $7 million loss from "manufacturing operations" and elaborate on the material items which resulted in the significant loss of $7 million.

   Company's Response

   Manufacturing operations largely provide joinery manufacturing services to the Group's internal projects. While the revenue from external customers decreased by only $2 million from $17.6 million to $15.2 million, internal revenue decreased by $24.7m from $42.1m to $17.4m. The significant decrease is due to the Group's project mix where there has been a decrease in residential projects which has a larger joinery scope than commercial and hospitality projects. The overall decrease in manufacturing activity has resulted in higher losses in manufacturing operations due to the higher unrecoverable fixed costs (factory overheads, labour). We are addressing this excess capacity through consolidating our manufacturing operations.

b. "Cost overruns due to delay from a project in United Arab Emirates in FY2018" caused the Company to incur a $6.1 million "one-off" loss. Please elaborate on the reason(s) for the $6.1 million cost overruns; what the project was and why the project resulted in the significant cost overruns.

   Company's Response

   A residential project in Dubai which was meant to have been completed in March 2017, has been delayed by 2 years due to delays by the main contractor in completing their works, including a fire incident which contributed to the delay.

   The delays in hand-over of the site for our performance of work has increased the expenses for completion of the project, which resulted in the significant cost overruns.

c. The Company reported a $3 million "one-off" loss from cost incurred and provisions made relating to the consolidation of the Group's manufacturing operations in FY2018. Please elaborate on the nature of the consolidation of manufacturing operations. What are the $3 million costs incurred due to the consolidation? Please provide a breakdown of the costs incurred and provisions made; and explain why the consolidation of the Group's manufacturing operations is incurring such significant losses and when the consolidation will be completed.

Company's Response

The manufacturing facilities in the Group located in China, Malaysia and Singapore were consolidated to China and Singapore only - the China manufacturing facility which will service the Group's geographical footprint has the largest capacity in the Group, with the latest, state-of-the-art equipment; while, the Singapore manufacturing facility has been upgraded and tailored to service the Singapore and Malaysia markets respectively.

The breakdown of $3 million of cost incurred and provision made for Malaysia in FY2018 is as follows:

Staff redundancy	$0.5 million
Impairment of fixed assets	$0.3 million
Impairment on inventories	$0.9 million
Provision of lease commitment	$0.6 million
Reversal of deferred tax assets	$0.7 million
	$3.0 million

The consolidation is targeted to be completed in Q2 2019.

d. A "one-off" loss of $1.1 million arose from the Group's closure of underutilized showrooms in Malaysia and in the PRC in FY2018. Please provide a breakdown of those costs. Please also disclose:

  i. the size of these showrooms and why they were underutilized when revenue from the Malaysia geographical segment increased by 30% in FY2018 to $58.9 million;

  ii. when did the Company close the respective showrooms;

  iii. what were the showrooms respectively utilized for prior to closure; and

  iv. reasons for the closure of the showrooms.

Company's Response

The $1.1 million consists of provision for remaining lease for showrooms, disposal of assets and staff redundancy cost. The showrooms were used to showcase the different lines of products and workmanship to existing and potential customers and were also tailored for retail customers. The showrooms were underutilised as they were tailored for retail customers, while the Group's core business is major projects and developments and it did not meet the targeted sales that the Company aimed to achieve. The showrooms were closed in Q4 2018.

The Malaysia showroom is approximately 5,000 sq.ft and the China showroom is approximately 32,000 sq.ft.

e. The Company further incurred a "one-off" loss of $1.9 million in FY2018, arising from defects and commercial settlement for completed projects. Please disclose:

i. details of the commercial settlement and the nature of the defects;

ii. how the $1.9 million settlement was determined;

iii. the identity of the contractor and whether the contractor was a related party.

<u>Company's Response</u>

$1.9m of defects and commercial settlement relates to corrective works to residential projects which have been completed by the Group, mostly in prior years. The $1.9m cost is based on a combination of actual costs incurred, a provision based on estimated corrective costs or commercial settlement reached with the client. $1.8m of the $1.9m relates to contracts with non-related parties. The remaining $0.1m relates to a hospitality project with a related party in the International BU.

<u>SGX Query 5</u>

In FY2018, the Group's revenue increased by 21.4% to $168.8 million, with higher revenue recorded across the Singapore, Malaysia and International business segments. Please disclose the Group's projects and provide details on how these projects resulted in the 21.4% increase in revenue for FY2018.

<u>Company's Response</u>

The Group's increased revenue comes from an increase in commercial and hospitality projects which had an increase in revenue of $68.7m, from $81.4m in FY2017 to $150.1m in FY2018. There was also a decrease in residential projects of $41.9m from $60.6m in FY2017 to $18.7m.

<u>SGX Query 6</u>

In FY2018, the Group's Malaysia BU segment's liabilities increased to $27 million from $9.7 million in FY2017. Please explain the factors leading to this significant increase of $17.3 million in liabilities in the Malaysia BU segment.

<u>Company's Response</u>

The factors leading to the significant increase of $17.3 million in liabilities in the Malaysia BU segment was due to increase in trade creditors and accrued contract cost. Please refer to our response to Query 1 above for the factors leading to an increase in trade creditors and accrued contract costs.

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SGX Query 7

We note that the Group's International BU segment's liabilities increased from $2.9 million in FY2017 to $17.2 million in FY2018. Please explain the factors leading to this significant increase of $14.3 million in liabilities in the International BU segment, despite the small increase in revenue from $20.4 million in FY2017 to $22.4 million in FY2018.

Company's Response

The factors leading to the significant increase of $14.3 million in liabilities in the International BU segment was due to increase in trade creditors and accrued contract cost. Please refer to our response to Query 1 above for the factors leading to an increase in trade creditors and accrued contract costs.

SGX Query 8

The Group's Manufacturing BU segment's liabilities increased by $0.6 million from $8.5 million in FY2017 to $9.1 million in FY2018. However, FY2018 revenue from the Manufacturing BU segment decreased by $27.2 million, from $59.8 million in FY2017 to $32.6 million in FY2018. Please account for the significant fall in FY2018 revenue for the Manufacturing BU's segment.

Company's Response

The significant decrease in manufacturing revenue is due to the decrease in manufacturing for the Group's internal projects. The Group's project mix has seen a decrease in residential projects which has a larger joinery scope than commercial and hospitality projects.

SGX Query 9

Based on the United Arab Emirates' segment results, the Group reported a significant loss in revenue in FY2018, from $21.2 million in FY2017 to only $7.5 million in FY2018. Please explain what led to the significant decrease of $13.7 million in revenue in the UAE, leaving aside the cost overruns of $6.1 million for FY2018.

Company's Response

The significant decrease of $13.7 million in revenue is mainly due to lower revenue recognised in line with less work completed for a residential project in FY2018 as compared to FY2017.

By Order of the Board

Hazel Chia
Company Secretary

5 March 2019