

## ISDN Holdings Limited

## Overweight

Current Price	<b>S\$0.197</b>
Fair Value	S\$0.320
Up / (downside)	62.4%

## Stock Statistics

Market cap	S\$77.8m
52-low	S\$0.171
52-high	S\$0.275
Avg daily vol	853,262
No of share	394.7m
Free float	62%

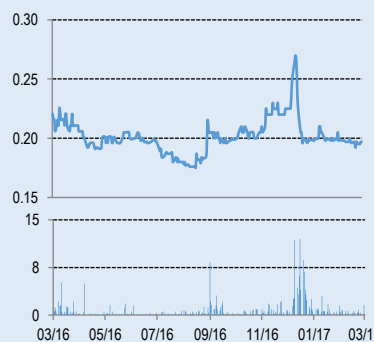
## Key Indicators

ROE 17F	6.4%
ROA 17F	6.3%
P/NAV	0.61x
Net gearing	Net cash

## Major Shareholders

Teo Cher Koon	33.2%
Karl Walter Braun	5.1%

## Historical Chart



Source: Bloomberg

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## Rebound in Business Raises Value Proposition

- **Share price has lagged despite positive developments.** Since 2H 2016, China has enjoyed a rebound in its manufacturing sector with the Caixin Manufacturing PMI first rising above 50 points to 50.6 in July last year and to 51.7 in February. Likewise, ISDN's results have tracked the stronger sentiment with revenue growing by 10% year-on-year in 3Q16 and 30% in 4Q16. The healthy top-line growth has helped to offset lower gross margin, leading PATMI to rebound by 62% to S\$2.9m in 4Q16. Despite these developments, ISDN's share price has fallen to S\$0.197 since reaching a high of S\$0.275 on 10 January before its listing on the HKSE on 12 January.
- **Beneficiary of stronger demand from semiconductor and infrastructure sectors.** ISDN's motion control products are also used in the manufacture of semiconductor equipment. These end uses account for about 20% of ISDN's revenue. In addition, ISDN supplies high end locks and hinges that are used in railway and transportation systems. In general, we estimate that revenue from ISDN's motion control engineering solutions segment will grow by 10% in FY17 and assume 5% revenue growth for the other segments, cumulating in group revenue growth of approximately 9% to S\$281.6m in FY17.
- **FY17F earnings revised higher by 25% to S\$8.6m.** However, PATMI is expected to jump by 67% from S\$5.2m in FY16 to S\$8.6m in FY17 on economies of scale and the absence of IPO expenses of S\$3.5m and FX losses of S\$0.7m incurred in FY16. The decline in profitability in FY16 was also partially due to a drop in gross margin from 28% in FY15 to 25% as customers resisted higher selling prices. We expect gross margin to stabilize at around 25% over our forecast horizon of FY17 to FY18 with revenue growth adding S\$5.8m to gross profit in FY17. In addition, ISDN only has S\$0.4m of IPO expenses to be recorded in FY17, implying a reduction in admin costs by around S\$2.5m in FY17 after accounting for cost inflation.
- **41% of mkt cap backed by net cash.** As of 31 December 2016, ISDN had net cash of S\$25.0m. Adding in S\$7m of net proceeds from the listing of new shares in Hong Kong, ISDN has about 8.1 cents of net cash per share, equivalent to 41% of its share price of S\$0.197 which includes 0.3 cents of dividend payable on 5 June 2017. Based on the same peer group as per our November 2016 report, ISDN's current share price lags its peer group average in terms of P/E, P/B and EV/EBITDA despite its stronger net cash balance sheet. Benchmarking ISDN against the peer average trading multiples, we arrived at a valuation of S\$0.319 to S\$0.392 (mean of S\$0.346). To be prudent, we pegged our valuation of ISDN at 14.66x FY17F EPS or at S\$0.320 (revised higher from S\$0.300 previously) with an Overweight (high-average return / low risk) rating.

Key Financial Data (S\$ m, FYE Dec)	2015	2016	2017F	2018F	2019F
Sales	235.3	258.5	281.6	295.6	310.4
Gross Profit	65.7	65.0	70.4	73.9	77.6
Net Profit	8.7	5.2	8.6	9.2	10.9
EPS (cents)	2.5	1.45	2.18	2.3	2.8
EPS growth (%)	17.0	(40.9)	49.8	6.6	19.4
PER (x)	8.0	13.6	9.1	8.5	7.1
NTA/share (cents)	25.0	26.7	26.0	26.3	27.0
DPS (cents)	0.4	0.3	0.4	0.5	0.6
Div Yield (%)	2.0	1.5	2.0	2.4	2.8

Source: NRA Capital forecasts

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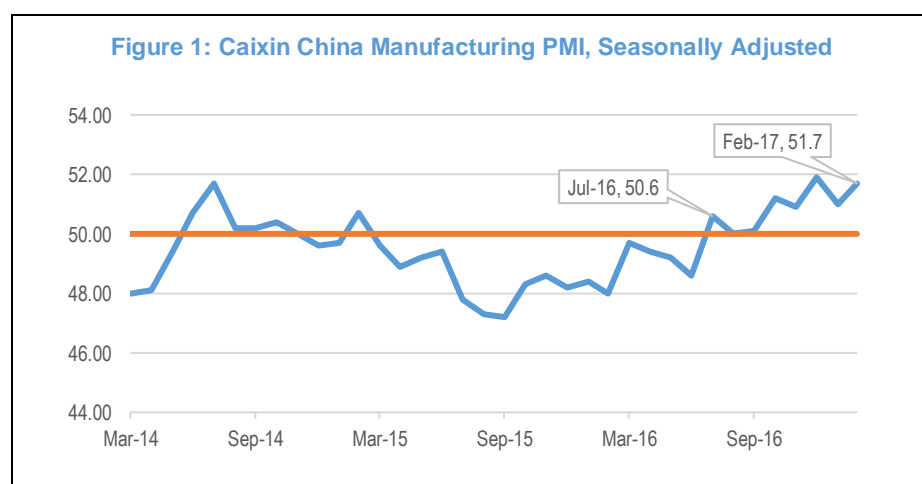
## Results Comparison

FYE Dec (\$\$ m)	4Q16	4Q15	yoy % chg	3Q16	qoq % chg	Prev. 4Q16F	Comments
Revenue	67.1	51.6	30	71.0	-6	56.3	Above expectations; 19% positive variance
Gross profit	16.8	15.7	7	17.1	-2	13.7	
Gross margin (%)	25.1	30.5		24.1		24.4	In line
Operating expenses	(11.7)	(11.6)	1	(13.9)	-15	(9.7)	Higher than expected due to IPO expenses
EBITDA	5.1	4.2	22	3.2	58	4.0	
EBITDA margin (%)	7.6	8.1		4.5		7.2	
Depn & amort.	(0.6)	(0.6)	2	(0.5)	16	(0.8)	
EBIT	4.5	3.6	25	2.7	65	3.3	
Interest expense	(0.2)	(0.2)	1	(0.1)	17	(0.2)	
Interest & invt inc	1.4	(0.7)	nm	0.3	400	(1.5)	S\$0.9m of FX gain in 4Q16
Associates' contrib	0.3	0.1	249	0.5	-47	(0.1)	
Exceptionals	0.0	0.0	na	0.0	na	0.0	
<b>Pretax profit</b>	<b>6.0</b>	<b>2.8</b>	<b>118</b>	<b>3.4</b>	<b>77</b>	<b>1.6</b>	
Tax	(1.1)	(0.8)	34	(1.5)	-30	0.2	
Tax rate (%)	17.7	28.9		45.1	-61	(14.3)	
Minority interests	(2.0)	(0.2)	1,248	(1.2)	74	(0.4)	
<b>Net profit</b>	<b>2.9</b>	<b>1.8</b>	<b>62</b>	<b>0.7</b>	<b>319</b>	<b>1.4</b>	
EPS (cts)	0.82	0.51	61	0.63	30	0.39	

Source: Company, NRA Capital

**Recovery of key markets to drive growth in 1H 2017.** China remained ISDN's largest market to account for 70% of the company's sales in 2016. During 4Q16, PRC revenue rebounded strongly to grow by 40% year-on-year to S\$47.5m, following flat growth of 1.2% during the first nine months of 2016. Looking ahead, we can expect similar growth rates from China in 2017 owing to demand from the semiconductor and infrastructure industries.<sup>1, 2</sup>

Singapore accounted for 14% of ISDN's revenue and was the second largest market for the group. The electronic and precision engineering sectors were the fastest growing industry clusters in our manufacturing sector this year, clocking growth of 39.8% and 26.2% year-on-year in February. ISDN's products are also used in the manufacture of semiconductor equipment, including those produced by SGX listed semiconductor equipment companies. Strong growth in these sectors should also bode well for ISDN in 2017.

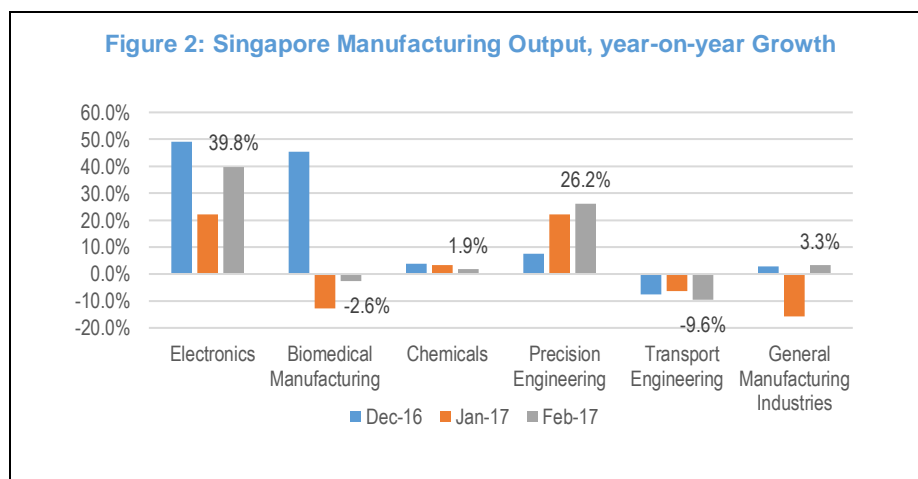


Source: Bloomberg, NRA Capital

<sup>1</sup> <https://www.bloomberg.com/news/articles/2017-03-28/china-s-largest-chipmaker-secures-22-billion-to-expand-globally>

<sup>2</sup> <https://www.bloomberg.com/news/articles/2016-12-29/china-to-have-30-000-kilometer-high-speed-rail-network-by-2020>

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Source: <https://www.edb.gov.sg>, NRA Capital

**Potential catalyst may come from new corporate finance business.** More recently, ISDN announced that it has invested S\$0.1m for 50% of Emmett Capital (Private) Limited. Emmett is an exempt corporate finance adviser lodged with the Monetary Authority of Singapore and was incorporated in 2011. The formation of this joint venture shortly after the company's listing in Hong Kong suggests that it wants to leverage on its access to investors in Singapore and Hong Kong to help its partners tap the capital markets. These partners may include for instance small medium manufacturers that purchase from ISDN, thus forming a one-stop solution that includes both the supply of goods and financial support especially for customers that are expanding.

**First hydropower project to be completed by mid-2018.** The first 4.6MW mini hydropower plant in Sumatra is currently under construction at a projected investment cost of US\$12.6m (on a 100% shareholding basis) and is expected to be completed by mid-2018, with another two plants are slated for completion by mid-2019. We estimate an expected output of 30.2 GWh for a full year of operation at the first plant, which will yield sales of US\$3.6m per annum based on a feed in tariff of US\$0.12 per kWh, with an estimated net profit of S\$0.93m attributable to ISDN each year for its 37.5% stake.

**Figure 3: Financial Estimates for the Hydropower Plant**

Description		Remarks
Plant Capacity	4.6MW	As per page 226 of HKSE listing document
Maximum Output	40.3GWh	4.6MW x 365 days x 24 hours
Efficiency	75%	Assumed
Expected Output	30.2GWh	Max. output x efficiency
Tariff (US\$ per kWh)	0.132	Based on national average production cost in Indonesia <sup>3</sup>
Expected revenue (US\$ m)	3.6	Tariff x expected output
Capex (US\$m)	12.6	As per page 226 of HKSE listing document
Opex/year (US\$m)	-1.26	10% of capex
Tax (US\$m)	-0.6	@25%
Profit (US\$m)	1.8	Revenue, less opex and tax
<b>Attributable to ISDN (US\$m)</b>	<b>0.66</b>	<b>x 37.5%</b>
<b>in S\$m</b>	<b>0.93</b>	<b>USD SGD = 1.4</b>

Source: NRA Capital

<sup>3</sup> <http://www.lexology.com/library/detail.aspx?g=3aeb2405-a78a-46f9-9d4f-a49808cd8b09>

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Figure 4: Pictures of the Mini Hydropower Plant



Source: Obtained from company on 28 March 2017

**Recommendation and valuation.** Overall, we expect ISDN to make PATMI of S\$8.6m for FY17, because of cost savings and revenue growth. Thereafter, we project revenue growth of approximately 5% per annum and 25% gross margin for FY18 and FY19. The mini hydropower plant business is expected to add S\$0.5m and S\$2m to share of results of associates in FY18 and FY19 respectively. Other than the reversion to growth, potential catalysts may also include any new investments or transactions arising from ISDN's new corporate finance joint venture.

Based on a share price of S\$0.197, ISDN trades at only 9.1x FY17 EPS and 0.61x P/BV while its peers trade at a median of 14.66x P/E and 1.0x BV. Pegging our valuation at 14.66x P/E, we value ISDN at S\$0.320 per share. Excluding net cash of 8.1 cents per share, ISDN trades at an even lower multiple of 5.3x P/E. As ISDN's share price has retreated back to "pre-IPO" levels, we reckon that downside risk is low given the net cash balance sheet with the prospective reversion to growth promising of high-average return.

Figure 5: Peer Comparison

Company Name	Mkt Cap (\$m)	Sales (\$m)	3-yr Avg EPS Growth	Ret. On Com. Equity	Net debt to com. Equity	P/E	P/BV	EV/EBITDA
China Metal International Holdings Inc	476.09	420.7	10.2%	13.3%	7.4%	7.81	1.08	4.67
Shanghai Prime Machinery Co Ltd	428.45	1589.5	54.8%	6.3%	66.2%	10.21	0.66	7.41
CHTC Fong's Industries Co Ltd	412.64	556.0	14.1%	14.0%	47.3%	25.02	1.69	15.14
IPE Group Ltd	396.54	151.6	NA	6.1%	NA	19.64	1.45	7.05
EVA Precision Industrial Holdings Ltd	369.83	570.9	97.9%	4.2%	9.6%	39.09	0.82	5.49
Tiangong International Co Ltd	358.56	677.7	-30.5%	1.0%	60.5%	45.74	0.46	11.42
CW Group Holdings Ltd	196.12	429.6	75.0%	15.4%	40.5%	4.97	0.67	6.05
Zhejiang Tengy Environmental Technology Co Ltd	189.21	201.3	67.5%	22.6%	9.8%	7.69	1.53	NA
Yusei Holdings Ltd	145.29	243.1	216.3%	16.0%	49.7%	11.87	1.77	6.49
Austar Lifesciences Ltd	132.46	134.7	NA	-2.9%	NA	NA	1.20	NA
LK Technology Holdings Ltd	130.16	514.0	19.1%	4.6%	69.9%	8.80	0.41	6.24
Good Friend International Holdings Inc	117.94	218.2	37.3%	5.2%	41.3%	14.78	0.79	7.12
Asia Tele-Net & Technology Corp Ltd	80.36	97.5	NA	2.2%	NA	64.71	1.49	26.76
Leeport Holdings Ltd	63.17	127.2	83.9%	6.5%	15.2%	14.66	0.93	27.57
<b>Median</b>	<b>192.66</b>	<b>331.9</b>	<b>54.8%</b>	<b>6.2%</b>	<b>41.3%</b>	<b>14.66</b>	<b>1.00</b>	<b>7.08</b>
<b>ISDN</b>	<b>77.80</b>	<b>258.5</b>	<b>11.7%</b>	<b>6.4%</b>	<b>NA</b>	<b>9.10</b>	<b>0.61</b>	<b>3.40</b>

Source: Bloomberg, NRA Capital. Extracted on 27 March 2017

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Figure 6: Valuation Matrix

	P/E	P/BV	EV/EBITDA
Median (as per peer comparison table)	14.66	1.00	7.08
FY17 Est. PATMI (S\$m)	8.59		
Current NAV + S\$7.0m of net proceeds		128.20	
FY17 Est. EBITDA (S\$m)			20.95
Enterprise value			148.3
Adjustment to value of equity			7.17
Value of equity	125.95	128.51	155.50
Number of shares			394.69
<b>Value per share</b>	<b>0.319</b>	<b>0.326</b>	<b>0.394</b>
Mean value per share	0.346		

Source: NRA Capital



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<b>Profit &amp; Loss</b> (S\$ m, FYE Dec)	<b>2015</b>	<b>2016</b>	<b>2017F</b>	<b>2018F</b>	<b>2019F</b>
Revenue	235.3	258.5	281.6	295.6	310.4
Operating expenses	(217.2)	(243.5)	(260.6)	(273.7)	(287.4)
EBITDA	18.1	15.0	20.9	22.0	23.1
Depreciation & amortisation	(2.2)	(2.1)	(2.2)	(2.3)	(2.4)
EBIT	15.9	12.9	18.8	19.7	20.7
Net interest & invt income	0.5	1.1	0.8	0.5	0.5
Associates' contribution	0.8	0.4	0.8	1.3	3.3
Exceptional items	0.0	0.0	0.0	0.0	0.0
<b>Pretax profit</b>	<b>17.2</b>	<b>14.3</b>	<b>20.3</b>	<b>21.5</b>	<b>24.5</b>
Tax	(5.3)	(4.3)	(6.1)	(6.5)	(7.3)
Minority interests	(3.2)	(4.9)	(5.6)	(5.9)	(6.2)
<b>Net profit</b>	<b>8.7</b>	<b>5.2</b>	<b>8.6</b>	<b>9.2</b>	<b>10.9</b>
Shares at year-end (m)	354.7	354.7	394.7	394.7	394.7
<b>Balance Sheet</b> (S\$ m, as at Dec)	<b>2015</b>	<b>2016</b>	<b>2017F</b>	<b>2018F</b>	<b>2019F</b>
Fixed assets	35.6	27.7	36.3	34.0	31.6
Intangible assets	11.7	11.7	11.7	11.7	11.7
Other long-term assets	7.2	13.6	14.0	14.4	14.9
<b>Total non-current assets</b>	<b>54.4</b>	<b>53.0</b>	<b>62.0</b>	<b>60.1</b>	<b>58.1</b>
Cash and equivalents	39.1	38.7	33.1	45.2	66.0
Stocks	40.9	38.9	50.9	53.4	56.1
Trade debtors	73.1	86.3	87.5	91.9	96.5
Other current assets	0.0	0.0	0.0	0.0	0.0
<b>Total current assets</b>	<b>153.1</b>	<b>163.9</b>	<b>171.5</b>	<b>190.5</b>	<b>218.5</b>
Trade creditors	51.9	65.5	64.6	67.9	71.3
Short-term borrowings	14.1	13.2	7.0	7.4	7.8
Other current liabilities	1.5	1.6	6.1	6.5	13.8
<b>Total current liabilities</b>	<b>67.5</b>	<b>80.3</b>	<b>77.8</b>	<b>81.7</b>	<b>92.8</b>
Long-term borrowings	0.7	0.4	0.4	0.4	0.4
Other long-term liabilities	0.0	0.0	0.0	0.0	0.0
<b>Total long-term liabilities</b>	<b>0.7</b>	<b>0.4</b>	<b>0.4</b>	<b>0.4</b>	<b>0.4</b>
<b>Shareholders' funds</b>	<b>119.7</b>	<b>121.2</b>	<b>134.7</b>	<b>142.0</b>	<b>150.8</b>
Minority interests	19.5	14.9	20.6	26.5	32.7
NTA/share (S\$)	0.25	0.27	0.26	0.26	0.27
<b>Total Assets</b>	<b>207.5</b>	<b>216.8</b>	<b>233.5</b>	<b>250.6</b>	<b>276.7</b>
<b>Total Liabilities + S'holders' funds</b>	<b>207.5</b>	<b>216.8</b>	<b>233.5</b>	<b>250.6</b>	<b>276.7</b>
<b>Cash Flow</b> (S\$ m, FYE Dec)	<b>2015</b>	<b>2016</b>	<b>2017F</b>	<b>2018F</b>	<b>2019F</b>
Pretax profit	17.2	14.3	20.3	21.5	24.5
Depreciation & non-cash adjustments	4.7	3.2	0.9	12.7	19.2
Working capital changes	(8.2)	(0.9)	(14.3)	(3.9)	(4.1)
Cash tax paid	(5.3)	(4.3)	(1.6)	(6.1)	(6.5)
<b>Cash flow from operations</b>	<b>8.4</b>	<b>12.4</b>	<b>5.3</b>	<b>24.3</b>	<b>33.1</b>
Capex	(5.9)	(2.5)	(10.8)	(10.8)	(10.8)
Net investments & sale of FA	(2.3)	(4.0)	0.0	0.0	0.0
Others	0.3	0.4	0.0	0.0	0.0
<b>Cash flow from investing</b>	<b>(8.0)</b>	<b>(6.1)</b>	<b>(10.8)</b>	<b>(10.8)</b>	<b>(10.8)</b>
Debt raised/(repaid)	1.1	(1.1)	(6.2)	0.3	0.4
Equity raised/(repaid)	0.0	0.0	7.4	0.0	0.0
Dividends paid	(1.4)	(1.4)	(1.2)	(1.6)	(1.8)
Cash interest & others	1.5	(4.1)	(0.2)	(0.2)	(0.2)
<b>Cash flow from financing</b>	<b>1.2</b>	<b>(6.6)</b>	<b>(0.1)</b>	<b>(1.4)</b>	<b>(1.6)</b>
<b>Change in cash</b>	<b>1.6</b>	<b>(0.4)</b>	<b>(5.6)</b>	<b>12.1</b>	<b>20.7</b>
<b>Change in net cash/(debt)</b>	<b>0.5</b>	<b>0.7</b>	<b>0.6</b>	<b>11.8</b>	<b>20.4</b>
<b>Ending net cash/(debt)</b>	<b>24.3</b>	<b>25.0</b>	<b>25.6</b>	<b>37.4</b>	<b>57.8</b>
<b>KEY RATIOS</b> (FYE Dec)	<b>2015</b>	<b>2016</b>	<b>2017F</b>	<b>2018F</b>	<b>2019F</b>
Revenue growth (%)	2.1	9.9	8.9	5.0	5.0
EBITDA growth (%)	11.6	(17.5)	40.0	5.0	4.9
Pretax margins (%)	7.3	5.5	7.2	7.3	7.9
Net profit margins (%)	3.7	2.0	3.0	3.1	3.5
Effective tax rates (%)	31.0	29.9	30.0	30.0	30.0
Net dividend payout (%)	16.3	20.6	18.5	20.0	20.0
ROE (%)	7.3	4.3	6.4	6.4	7.2
Free cash flow yield (%)	3.2	12.7	(7.0)	17.4	28.8

Source: NRA Capital forecasts

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