

ISDN Holdings Limited

Overweight

Current Price	S\$0.198
Fair Value	S\$0.300
Up / (downside)	51.5%

Stock Statistics

Market cap	S\$70.2m
52-low	S\$0.168
52-high	S\$0.280
Avg daily vol	1,053,503
No of share	354.7m
Free float	33%

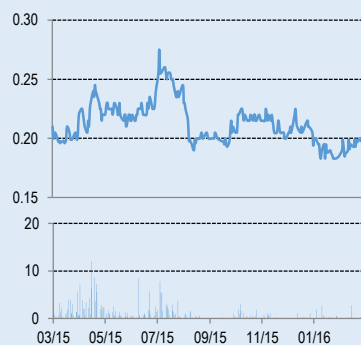
Key Indicators

ROE 16F	7.9%
ROA 16F	4.4%
P/NTA	0.79x
Net gearing	Net cash

Major Shareholders

Teo Cher Koon	36.5%
Tan Thiam Chye	8.0%
Karl Walter Braun	5.6%

Historical Chart



Source: Bloomberg

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Higher Margin Reflects Strong Core Business

- **Earnings within expectations despite lower revenue.** ISDN Holdings Limited's (ISDN) 4Q15 net profit attributable to shareholders came in at S\$1.8m, or just 11.3% lower than our forecast of S\$2.0m, despite revenue falling by 10% year-on-year to S\$51.4m. We deem the 4Q15 variance in net profit as within expectations, given that full year net profit attributable to shareholders of S\$8.7m was just 3.3% lower than our forecast of S\$9.0m.
- **Higher gross margin reflects strong underlying business.** The surprise improvement in gross margin from 26.1% in 3Q15 and 27.3% in 4Q14 to 30.4% in 4Q15 is a reflection of strength of ISDN's products. Most likely, some of the more resilient and higher margin industries such as the pharmaceutical and medical devices markets helped to drive performance. Moreover, clients from these industries are stickier due to safety and reliability requirements.
- **Revenue from other markets to help mitigate slowdown in PRC.** Revenue from the PRC fell by 16% or S\$7.0m year-on-year in 4Q15, suggesting that the slowdown in China is starting to affect ISDN. Outside of the PRC, revenue grew by 11.4% or S\$1.4m year-on-year. Growth was to some extent driven by the acquisition of new clients in Vietnam. Putting things in perspective, ISDN's growth in 2014 was particularly strong, with revenue growing by S\$57m or 33% that year, compared to average revenue growth of S\$3.4m or 2% per annum during 2011, 2012 and 2013.
- **Revising forecasts to reflect higher risks.** In view of the situation in 4Q15, we revised FY16 revenue growth to just 5% compared to 10% previously. That said, we maintain our assumption of 27% gross margin. Full year 2015 gross margin was actually 27.8%. In all, we now expect FY16 net profit attributable to shareholders to be around S\$9.8m, down from the previous estimate of S\$10.3m. We caution that 1Q16 performance may be weak, as our sources indicate slower activity and longer holidays in factories in China.
- **Longer term outlook remains intact – valuation maintained.** Longer term, we still see the upgrading of China's manufacturing industry as a potential growth driver. In the interim, ISDN is well supported by stable demand from key industries, growth from new businesses (e.g. hydropower in Indonesia) and in regions outside of China (e.g. Vietnam). Financially, ISDN is protected by net cash buffer of 6.9 cents per share, equivalent to 35% of its share price. To some extent, we feel that ISDN's share price has adjusted to reflect current conditions, being 8% lower from our last update. On balance, we still see ISDN as undervalued. Accordingly, we maintain our valuation at S\$0.30, valuing the company at 8.4x FY16 P/E excluding cash.

Key Financial Data (S\$ m, FYE Dec)	2014	2015	2016F	2017F	2018F
Sales	230.5	236.0	247.7	272.4	299.6
Gross Profit	61.5	65.6	66.1	72.2	79.4
Net Profit	7.5	8.7	9.8	11.0	12.6
EPS (cents)	2.1	2.5	2.8	3.1	3.6
EPS growth (%)	59.2	17.0	12.3	12.6	14.3
PER (x)	9.4	8.1	7.2	6.4	5.6
NTA/share (cents)	23.3	25.0	25.4	27.1	5.7
DPS (cents)	0.4	0.4	0.4	0.4	0.4
Div Yield (%)	2.0	2.0	2.0	2.0	2.0

Source: Company, NRA Capital forecasts

ISDN Holdings Limited

Cash flow strengthened in 2015. Other than being in a net cash position, ISDN's net operating cash flow actually strengthened in 2015, with the company reversing from a net operating cash out flow of S\$0.9m in 2014 to a net operating cash inflow of S\$6.6m in 2015. In particular, the company achieved a positive net operating cash flow of S\$3.1m in 4Q15, in spite of a net profit attributable to shareholders of only S\$1.8m. The improved cash flow was partially due to tight working capital management as the company collected S\$5.0m of trade and other receivables and reduced inventory by S\$7.6m in 2015.

Operating expenses remain well-controlled. During 4Q15, operating expenses remained almost flat year-on-year, at S\$12.85m. In addition, share of results of associates also turned positive, following a slight loss of S\$30k in 3Q. We have previously explained that the loss in 3Q was mainly one-off due to certain restructuring costs.

Reiterate positive long term outlook. In our previous update, we have highlighted as a key risk the fact that China's economic slowdown may affect ISDN's results in the short term. The results in 4Q15 suggest that this risk is in the midst of materializing. That said, there are still certain contract bidding opportunities for ISDN. Some of ISDN's products such as motion sensors for subway systems are very niche in nature and have limited competition, and may present certain tender opportunities for the company in the near term.

Over in Indonesia, ISDN's key investments, such as the mini-hydropower projects and Bantaeng industrial park, are still in the early phases and will also add on to growth later in 2017 or 2018.

In this update, we also rolled forward our forecasts to 2018. We generally assume that revenue growth will resume to 10% in 2017 and 2018, leading to projected revenue of S\$300m by 2018, and net profit attributable to shareholders of S\$12.6m by then.

A point to note is that ISDN's improving balance sheet and cash flows have actually led to 2015 NTA per share being higher than expected at 25 cents per share (versus forecast of 24.4 cents). Based on our prior valuation multiple of 1.2x NTA, we would have achieved a valuation of S\$0.305. Nonetheless, we have decided to remain conservative and keep valuation at S\$0.300.

Results Comparison

FYE Dec (\$\$ m)	4Q15	4Q14	yoy % chg	3Q15	qq % chg	Prev. 4Q15F	Comments
Revenue	51.4	57.0	-10	64.8	-12	69.1	26% lower than expected due to slowdown in PRC
Operating costs	(47.3)	(54.7)	-14	(60.2)	-9	(64.7)	
EBITDA	4.1	2.3	78	4.6	-50	4.4	Lower, but EBITDA margin higher than expected due to higher gross margin and flat operating expenses.
EBITDA margin (%)	8.0	4.1		7.1		6.4	
Depn & amort.	(0.6)	(0.6)	-3	(0.6)	5	(0.6)	
EBIT	3.5	1.7	106	4.0	-57	3.9	
Interest expense	(0.2)	(0.2)	-10	(0.2)	-9	(0.3)	
Interest & invt inc	(0.7)	1.1	-166	1.3	-17	(0.2)	
Associates' contrib	0.1	0.1	-27	(0.0)	477	0.5	Turned positive despite slight loss in 3Q – earlier than expected
Exceptionals	0.0	0.0	0	0.0	0	0.0	
Pretax profit	2.8	2.7	2	5.1	-47	3.8	Lower than expected by S\$1m due to lower revenue
Tax	(0.8)	(0.7)	15	(1.7)	-60	(0.9)	
Tax rate (%)	28.9	25.8		34.6		24.8	
Minority interests	(0.2)	(0.0)	2,900	(1.3)	-100	(0.8)	
Net profit	1.8	2.0	-9	2.0	0	2.0	Generally, in line with expectations due to lower MI
EPS (cts)	0.5	0.6	-8	0.6	-1	0.6	

Source: NRA Capital estimates

ISDN Holdings Limited

Profit & Loss (\$\$ m, FYE Dec)	2014	2015	2016F	2017F	2018F
Revenue	230.5	236.0	247.7	272.4	299.6
Operating expenses	(214.3)	(218.0)	(229.1)	(251.9)	(277.1)
EBITDA	16.3	18.0	18.6	20.5	22.5
Depreciation & amortisation	(2.2)	(2.2)	(2.3)	(2.3)	(2.3)
EBIT	14.1	15.8	16.4	18.2	20.2
Net interest & invt income	0.1	0.6	1.5	1.8	2.4
Associates' contribution	1.1	0.8	0.9	1.0	1.1
Exceptional items	0.0	0.0	0.0	0.0	0.0
Pretax profit	15.2	17.2	18.7	21.0	23.7
Tax	(4.6)	(5.3)	(5.6)	(6.3)	(7.1)
Minority interests	(3.1)	(3.2)	(3.3)	(3.7)	(4.0)
Net profit	7.5	8.7	9.8	11.0	12.6
Shares at year-end (m)	354.7	354.7	354.7	354.7	354.7
Balance Sheet (\$\$ m, as at Dec)	2014	2015	2016F	2017F	2018F
Fixed assets	31.4	35.6	39.3	43.0	40.7
Intangible assets	11.7	11.7	11.7	11.7	11.7
Other long-term assets	6.8	7.2	7.4	7.6	7.8
Total non-current assets	49.9	54.4	58.4	62.3	60.2
Cash and equivalents	37.5	39.1	42.7	44.8	(20.0)
Stocks	34.6	40.9	43.5	48.0	52.8
Trade debtors	68.0	73.1	76.8	84.4	92.9
Other current assets	0.0	0.0	0.0	0.0	0.0
Total current assets	140.1	153.1	163.1	177.2	125.7
Trade creditors	45.1	51.9	55.3	61.0	67.1
Short-term borrowings	13.1	14.1	12.4	10.9	12.0
Other current liabilities	1.5	1.5	5.6	6.3	13.4
Total current liabilities	59.7	67.5	73.3	78.2	92.5
Long-term borrowings	0.6	0.7	0.5	0.5	0.5
Other long-term liabilities	0.0	0.0	0.0	0.0	0.0
Total long-term liabilities	0.6	0.7	0.5	0.5	0.5
Shareholders' funds	112.1	119.7	124.7	134.3	62.4
Minority interests	17.7	19.5	22.9	26.5	30.5
NTA/share (\$\$)	0.23	0.25	0.25	0.27	0.06
Total Assets	190.0	207.5	221.4	239.5	185.9
Total Liabilities + S'holders' funds	190.0	207.5	221.4	239.5	185.9
Cash Flow (\$\$ m, FYE Dec)	2014	2015	2016F	2017F	2018F
Pretax profit	15.2	17.2	18.7	21.0	23.7
Depreciation & non-cash adjustments	3.4	4.7	(1.8)	1.5	(70.0)
Working capital changes	(15.7)	(10.0)	(3.4)	(6.8)	(6.8)
Cash tax paid	(3.8)	(5.3)	(1.5)	(5.6)	(6.3)
Cash flow from operations	(0.9)	6.6	12.0	10.0	(59.3)
Capex	(4.1)	(6.0)	(6.0)	(6.0)	(6.0)
Net investments & sale of FA	(0.4)	(0.5)	0.0	0.0	0.0
Others	0.1	0.4	0.0	0.0	0.0
Cash flow from investing	(4.4)	(6.1)	(6.0)	(6.0)	(6.0)
Debt raised/(repaid)	0.0	1.5	(1.9)	(1.5)	1.1
Equity raised/(repaid)	(1.4)	0.0	0.0	0.0	0.0
Dividends paid	(1.4)	(1.4)	(1.4)	(1.4)	(1.4)
Cash interest & others	4.0	1.3	1.0	1.0	1.0
Cash flow from financing	1.2	1.5	(2.3)	(2.0)	0.6
Change in cash	(4.1)	2.0	3.6	2.0	(64.7)
Change in net cash/(debt)	(4.1)	0.5	5.5	3.6	(65.8)
Ending net cash/(debt)	23.8	24.3	29.8	33.4	(32.4)
KEY RATIOS (FYE Dec)	2014	2015	2016F	2017F	2018F
Revenue growth (%)	32.7	2.4	5.0	10.0	10.0
EBITDA growth (%)	46.5	10.8	3.6	10.0	10.0
Pretax margins (%)	6.6	7.3	7.6	7.7	7.9
Net profit margins (%)	3.2	3.7	4.0	4.0	4.2
Effective tax rates (%)	30.4	31.0	30.0	30.0	30.0
Net dividend payout (%)	19.0	16.3	14.5	12.9	11.3
ROE (%)	6.7	7.3	7.9	8.2	20.2
Free cash flow yield (%)	(7.1)	0.9	8.5	5.7	(93.0)

Source: Company, NRA Capital forecasts

ISDN Holdings Limited

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