

ISDN Holdings Limited

Ahead of its 2014 Goal

Shortly after our industry report on Indonesia's electricity market (Not Enough Power in Indonesia, 20 June 2013), ISDN reported several encouraging announcements over the last two weeks:

Firstly, the company announced the acquisition of 80% shareholding in three Indonesian energy-related companies, PT Anggocci, PT Parduann and PT Sisira. The first two entities are at the signing stage to construct a 9MW and 10MW hydroelectric plant respectively in Sumatra while the latter has entered into a power purchase agreement to build, own and operate a 4.6MW hydroelectric power plant, also in Sumatra. These three projects can add a total of about 24MW energy production capacity to the Group and opens the company to prospective new projects in Sumatra.

ISDN also announced the issue of 1 warrant for 2 ordinary shares at an issue price of S\$0.02 and exercise price of S\$0.60 – subject to SGX and shareholders' approval. The managing director and president, Mr. Teo agreed to subscribe for all excess warrants. Under the full subscription and exercise of warrants scenario, a maximum of S\$111.6m will be raised. These proceeds are likely to be used to finance the hydropower plant projects in Indonesia as well as potential ventures in Myanmar.

Lastly, ISDN (via its 80% owned PT Potensia Tomini Energi) was awarded a recommendation letter by the Governor of Sulawesi to construct and operate a 126MW hydropower plant at the Laa River. We were very impressed with this contract as the company was previously only engaged in small size hydropower projects and the award of this contract reflects the authority's confidence in ISDN. This contract alone will enable ISDN to meet its 2014's goal of 100MW portfolio size – ISDN has a combined potential hydroelectric capacity of 168MW currently.

The Indonesian hydroelectric projects may generate a total theoretical profit of about S\$42.8m annually, which will be a substantial boost to the company's profitability. We adopt a sum-of-the-parts approach to ISDN, valuing the hydroelectric segment at 11X FY16F profit, Myanmar projects at S\$50m, and existing business at S\$89m. Subsequently, we arrive at a potential price of S\$1.580 per share. We do not include the possibility of new hydroelectric projects into our valuation model and are conservative in setting the success probability of the Myanmar projects.

Whilst ISDN's outlook seems promising, especially with the sizeable projects, we caution that the projects are currently undergoing feasibility studies and the valuation may change if ISDN decides not to proceed with them. Also, there is project execution risk and concern over the speed of land acquisition.

Potential Gem

- Relative Price S\$1.58
- Prev Closing S\$1.215

Main Activities

ISDN is a mechatronics engineering company providing solutions to its motion control and industrial computing customers. The company recently ventured into hydroelectric power plant in Indonesia and has several project proposals in Myanmar.

Financial Highlights

(Y/E Dec)(S\$m)	FY11	FY12
Revenue	165.9	153.5
Gross Profit	48.5	47.4
PATMI	8.4	5.4
Current Assets	94.3	99.7
Non-Current Assets	44.4	43.8
Current Liabilities	43.9	50.7
Non-Current Liabilities	11.0	5.8
Total Equity	83.8	86.9
Operating cash flow	3.5	3.6
Investing cash flow	2.2	(1.3)
Financing cash flow	(6.3)	(5.3)

Source: Company, SIAS Research

Key ratios (Current)

PER (x)	67
P/BV (x)	5.24
ROE (%)	10.0
ROA (%)	6.1
Dividend Yield (%)	0.4

Source: Bloomberg (trailing 12 months), SIAS Research

Indexed Price Chart

Green (FSSTI)
White (ISDN)



Source: Bloomberg

52wks High-Low S\$1.445 / S\$0.108
 Number of Shares 360m
 Market Capitalization S\$437.4m

Analyst:

Ng Kian Teck

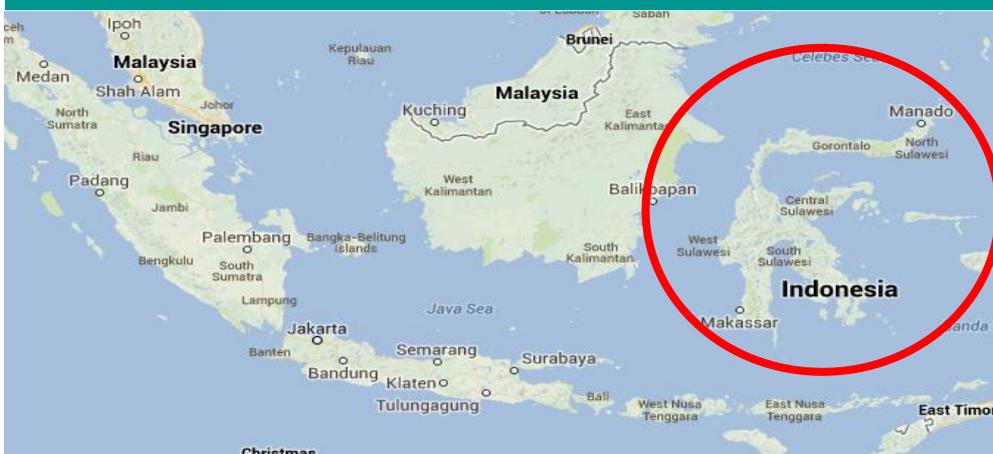
kianteck@siasresearch.com

Tel: 6227 2107

Projects to Date and Info about Sulawesi: ISDN had previously unveiled plans to develop three power plants in Sulawesi with a combined capacity of 18MW. Together with the 24MW projects in Sumatra and 126MW new Sulawesi contract, ISDN’s combined hydroelectric capacity is approximately 168MW. The company also has a mining and coal plant proposal in Myanmar.

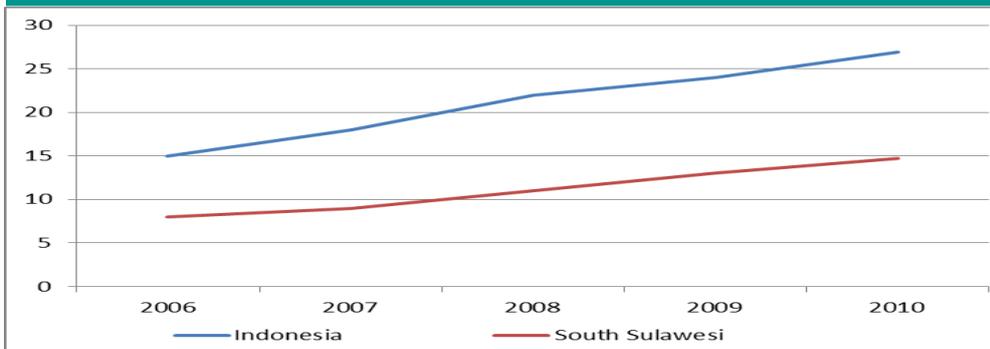
Sulawesi is an island located northeast of Jakarta with population of about 17.4m people. It is primarily divided into five smaller parts with cities like Makassar and Manado. The GDRP (gross domestic regional product) per capita is approximately US\$1,500 while roughly 85% of the population has access to electricity.

Figure 1: Location of Sulawesi



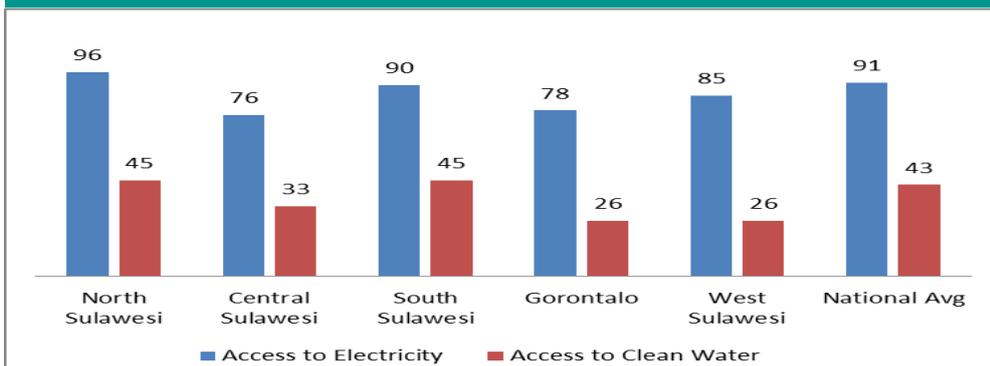
Source: Google Map

Figure 2: GDRP per capita (mn rupiah per capita)



Source: Worldbank

Figure 3: Electricity Connectivity in Sulawesi



Source: Susenas Data

Higher Profitability Ahead?: The 126MW project upgraded our view towards ISDN, due to the projected substantial incremental value. Based on the assumptions in our previous industry report, a 10MW plant may generate approximately US\$2m profit annually and hence, a total production capacity of 168MW may represent a potential yearly profit of about US\$33.6m or S\$42.8m. We reckon that a lower tariff rate for such huge project may be mitigated by cost savings.

Valuation: We are applying a sum-of-the-parts approach to value ISDN. The hydroelectric segment is valued at 11X FY15F profit while the Myanmar projects have a prospective value-add of S\$50m (based on 5% probability of a S\$1bn estimated value-add, thus we are being conservative). Also, we value the company’s existing business at its book value of S\$89m. In all, we arrive at a potential value of S\$579.8m, after deducting S\$40m for the additional financing needed for the new hydropower project. The valuation works out to a pre-warrant issuance price of S\$1.580.

More Upcoming Projects?: The valuation did not factor in the possibility of new hydropower projects in Indonesia, which we reckon is highly possible given the recommendation letter for the new 126MW hydropower plant. The government is also keen to bring in more private investments to solve the electricity shortage issues. There may also be positive news on the Myanmar projects and these potential projects can be financed by the recent warrant issuance.

Projects under Feasibility Studies: Though we are impressed with ISDN’s capability of securing sizeable hydroelectric projects, we note that these projects are still in feasibility studies stage. In the event that the above projects are approved, investors should also be mindful of the execution risk and the speed of land acquisition which will affect the timing and magnitude of returns.

Figure 4: SOTP Valuation

Item	Valuation
Value of Indonesia hydroelectric projects	470.8
Value of Myanmar projects	50
Existing Business	89
Capital requirement for hydroelectric project	-40
Valuation	569.8
Shares Outstanding	360
Value per share	1.58

Source: Company

Rating Definition:

Increase Exposure – The current price of the stock is significantly lower than the underlying fundamental value. Readers can consider increasing their exposure in their portfolio to a higher level.

Invest – The current price of the stock is sufficiently lower than the underlying fundamental value of the firm. Readers can consider adding this stock to their portfolio.

Fairly Valued – The current price of the stock is reflective of the underlying fundamental value of the firm. Readers may not need to take actions at current price.

Take Profit – The current price of the stock is sufficiently higher than the underlying fundamental value of the firm. Readers can consider rebalancing their portfolio to take advantage of the profits.

Reduce Exposure - The current price of the stock is significantly higher than the underlying fundamental value of the firm. Readers can consider reducing their holdings in their portfolio.

IMPORTANT DISCLOSURE

As of the date of this report, the analyst and his immediate family may own or have positions in any securities mentioned herein or any securities related thereto and may from time to time add or dispose of or may be materially interested in any such securities. Portfolio structure should be the responsibility of the investor and they should take into consideration their financial position and risk profile when structuring their portfolio. Investors should seek the assistance of a qualified and licensed financial advisor to help them structure their portfolio. This research report is based on information, which we believe to be reliable. Any opinions expressed reflect our judgment at report date and are subject to change without notice. This research material is for information only. It does not have regards to the specific investment objectives, financial situation and the particular needs of any specific person who may receive or access this research material. It is not to be construed as an offer, or solicitation of an offer to sell or buy securities referred herein. The use of this material does not absolve you of your responsibility for your own investment decisions. We accept no liability for any direct or indirect loss arising from the use of this research material. We, our associates, directors and/or employees may have an interest in the securities and/or companies mentioned herein. This research material may not be reproduced, distributed or published for any purpose by anyone without our specific prior consent.
