

# ISDN powers up

Shares in the once-dull engineering firm have sprung to life as it raises funds from the market to build power plants in Myanmar and Indonesia and to pursue other new businesses. Is it too late to get in?

BY FRANKIE HO

**T**ao Cher Kuan, president and the biggest shareholder of ISDN Holdings, couldn't have picked a better time to launch two placements of new shares in his mechatronics engineering group. The stock has been rocketing on heavy volume since March, hitting an all-time closing high of 87 cents in early April. It had been largely inactive for the last couple of years, changing hands for as little as 10.9 cents last August. With the run-up, ISDN's market value swelled to almost \$300 million early this month, from about \$34 million at end-2012.

The stock's performance since then has been extremely choppy, though, with the price fluctuating in a wide range of 64 to 95.5 cents in intraday trade. Even so, the company has been able to raise fresh equity capital on much more attractive terms than it could have just a couple of months ago.

On March 14, ISDN said it would sell 30 million new shares at 24 cents apiece to investors. The exercise was completed three weeks later. The second placement, announced on April 3 and still underway, involves 23.7 million new shares at 43 cents each. The two placements, both launched by UOB Kay Hian, will raise a total of \$18.8 million in net proceeds.

Tao, 54, who now has a stake of about 16% in the company's enlarged share base, claims to know nothing about the reasons behind the huge run-up in ISDN's shares. "The strong rally in the share price definitely caught me by surprise," he tells *The Edge Singapore*. "As far as I'm concerned, I just want to be focused on the business. I'd leave it to the market to decide how we should be perceived."

ISDN has been in the mechatronics engineering business for more than two decades, building motion-control systems for companies in the general automation, semiconductor, textiles and even defence industries. Since 2009, it has been diversifying and expanding its geographical footprint. "I thought of diversifying way before 2009. It has always been my belief not to put all my eggs in one basket," says Tao.

The company's new businesses include the construction and operation of power plants, coal mining and high-tech farming. China has traditionally been its biggest market by revenue, but Southeast Asia is where it will predominantly be building its new businesses. "I've always believed that in business, we should always think outside the box and keep an eye open for opportunities," Tao says. "In Southeast Asia, essential stuff, such as infrastructure, energy and food, offers huge potential for someone like us."

### Entering 'virgin ground'

Most of the money ISDN is raising from the share placements will be used to finance its ventures and push into new business streams. Notably, ISDN inked a non-binding agreement last month with Tin Thwin Mining Co to explore opportunities in developing and running a coal-fired power plant in Myanmar. Tin Thwin, a leading coal supplier in the country, has a government permit to develop a power plant near one of its coal-mining sites. The planned facility is expected to have a production capacity of 540mw of electricity when completed in 2015, according to Tin Thwin's website.

"This will be the largest coal-powered plant in Myanmar," says Tao. ISDN has been studying the market in Myanmar for over a year and Tao became acquainted with Tin Thwin through his business connections. "Myanmar



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is virgin ground at the moment. They have a shortage of everything," he points out.

Tin Thwin's planned facility is one of two coal-powered plants the Myanmar government intends to set up by 2015, Tao notes. By then, the country is expected to have a total of 14 new power plants, of which nine will run on hydropower — energy produced from water.

As it happens, hydropower generation is an area ISDN is exploring in Indonesia. The firm recently took a controlling stake in an entity set up by Malaysian power plant builder Prima Keras. The entity has an 80% stake in PT Prima Keras Energy, which is building a hydropower facility in south Sulawesi. ISDN's intention is to eventually establish several "mini" hydropower plants in Indonesia to produce between 50mw and 100mw of electricity in total, according to Tao. Construction is expected to take 15 to 18 months.

"When we say a mini hydropower plant, it's anything less than 100mw," he says. "We will do a few of such plants." Based on a ballpark investment of US\$1.5 million (\$1.45 million) per megawatt, ISDN will need about US\$75 million to produce up to 100mw of power, he figures. By his estimates, a 100mw plant can generate US\$5 million in revenue annually. "The feedstock [water from the river] is free and the maintenance cost is less than 10% of the annual revenue."

For such infrastructure projects, about 80% of the required capital is likely to come from project financing, with equity-based fund raising taking care of the rest, Tao says. "So, if we can arrange for project financing to fund the bulk of the projects, the company needs



to take care of probably US\$15 million for the 20% equity portion."

Banks that ISDN has spoken with so far are mostly supportive of its venture in Indonesia as they feel that risks associated with building these small-capacity power plants are manageable, he adds. The Indonesian government is also willing to back investors as electricity demand in the country is huge and supply is limited.

The group's strategy for its hydropower business is to acquire controlling stakes in projects in the early stage of development as well as those that are mature but offer what Tao calls "attractive entry values". ISDN may even acquire some of these assets and put them up for public listing.

### Chinese backing

Tao's game plan got a boost recently with state-owned China Huadian Engineering agreeing to work with ISDN on energy projects in Southeast Asia. Both companies inked a memorandum of understanding this month to jointly explore opportunities in the region. The Chinese firm will be ISDN's technology and project development partner in Southeast Asia. The two companies, which have been in talks to work together since last July, will initially focus on ISDN's hydropower project in Sulawesi, and will consider other ventures in Myanmar, Cambodia and Laos.

"I touched base with them about 1 1/2 years ago," says Tao. "We have built up a certain understanding. Besides joint projects, they will also refer project opportunities to us in Southeast Asia, those that they don't want to take up." China Huadian has even given ISDN what he calls a 100% performance bond for the Sulawesi project. "They guarantee they will deliver."

China Huadian, with total assets worth \$208.18 billion (\$26 billion), specialises in generating electricity and alternative forms of energy, such as wind and solar. One of the five biggest state-owned power generation companies in China, it is also involved in water treatment, metallurgy and mining. Another company that ISDN works closely with for its energy projects is New York-listed engineering group Arconis, which it relies on to carry out feasibility studies and tests on the ground.

### 'No venture, no gain'

Tao is also upbeat about ISDN's hydroponics — or high-tech farming — business, which it embarked on two years ago, after he picked up the trade from some friends in Australia. The company completed the pilot phase of its first hydroponics farm, in Malaysia, in January 2011, harvesting 14 varieties of pesticide-free lettuce. "It is proven that this is the right way to do farming, in terms of productivity and quality. It outperforms the conventional way of farming," he says.

ISDN has a similar set-up in Suzhou, China, and plans to establish more farms in other markets in Asia. It expects to spend about \$5.4 million over five years to develop the business, and intends to build at least 10 high-tech farms in Malaysia and China in the initial two years. It took the first step to expand its farming operation by forming a joint venture with Singapore construction firm Ho Lee Group last year to set up these facilities.

In the meantime, ISDN has started selling its crops to supermarkets and hotels in Suzhou. They are even sold on the Internet to people in Suzhou and Shanghai, with delivery by courier. "We spent the last two years making sure the crops are of the right quality and grow at the right productivity rate. Now, we are selling them at a premium price. The supermarket in Shanghai is willing to accept this pricing," Tao says.

ISDN's diversification efforts haven't always gone well, though. In 2009, it tried to get into the waste-to-energy recycling business through a partnership with academic firm several German universities. But the whole venture was eventually shelved. "We have done many rounds of studies. There are still lots of questions unanswered. So, we set our part of business on hold," Tao says.

Also, its coal mining business hasn't really taken off. In February 2011, the company said it would acquire a 21% stake in an Indonesian coal explorer that was supposed to start work on a 3,000ha mining site in Kalimantan. But that entity has yet to commence operation as it has not received a production permit. "It's not too promising because it's taking too long. We are losing interest," Tao says. "We don't have a stake in them yet because it was a proposed investment."

ISDN is not giving up plans for a coal business just yet. It has tied up with another miner in Indonesia to buy coal to resell. It made its maiden shipment this month, exporting about 60,000 tonnes of coal to a buyer in India. It is still on the lookout for opportunities to get its own exclusive source of supply. "I am more in favour of owning a concession and financing production, so that we have exclusive rights to the supply. The current supplier supplies to others besides us," he says.

None of this has deterred him from pressing on with new business ventures in the region. "Risks are forever there. No venture, no gain," he says. "In business, we must take risks, but we take calculated risks." By his reckoning, the potential return from the power generation business that ISDN is pursuing is more than worth the initial investment it is making and even exceeds the potentially higher costs it might have to bear.

"The new ventures have not really taken off yet, so we don't see the impact on margins at the moment. Even if there is any impact, I don't think it will be bad. For the hydroponics business, for instance, the internal rate of return is more than 20%. It's not too bad," he adds.

CONTINUED ON PAGE 28

# Teo hopeful on outlook for ISDN's core business

## FROM PAGE 18 Initial investment of \$10,000

Teo started out as a sales engineer at a Singapore engineering product distribution company from 1981 to 1984, after completing his National Service. In 1987, he set up the company that would eventually become ISDN, with the help of two other individuals who are no longer with the firm. His initial investment in the business was just \$10,000. "I started without any help from my parents or relatives," he says.

The company initially supplied US-made servomotors to Singapore universities and polytechnics for use in teaching aids. It subsequently specialised in developing motion-control systems. In 2005, the company sought a public listing and took on its current name. Today, the engineering business remains the backbone of ISDN. It commands gross margins of up to 30% and was profitable even during the global financial crisis, enabling ISDN to avoid having to lay off workers.

ISDN has about 800 workers, with more than 60% based in China. As the company's employees are mostly skilled workers, rising minimum wages in China haven't had much of an impact on ISDN. It has also been able to keep a lid on operating costs partly because it has its own industrial park, a \$22 million high-tech facility in Wuyang that it completed building in 2010. "Having our own industrial park gives us peace of mind as we don't have to move around. The landlord can increase the rent every year and then, that can be very painful for us," Teo says.

ISDN's revenue fell 7.3% to \$133.5 million last year on the back of slower economic growth in China, which traditionally accounts

for more than 60% of its top line. The lower revenue was a result of an almost 11% fall in sales at the motion-control division, which accounts for more than three-quarters of total revenue. That, coupled with foreign-exchange losses and an absence of one-off disposal gains, pushed 2012 earnings lower by 36% to \$5.4 million.

At end-2012, ISDN had \$24.6 million in cash, of which \$7.8 million was generated from operations last year. Even after subtracting its outstanding bank borrowings as at end-2012, ISDN would still have been in a net cash position of about \$3 million. Its current market value of about \$250 million is 46 times its reported 2012 earnings.

On the outlook for ISDN's core business this year, Teo is hopeful. "I think this year should be promising for the Chinese economy because a new government has just taken over and we see a lot of projects being revived — projects such as railway and infrastructure. We are involved in some of those."

However, in the meantime, are more likely to be concerned about the company's progress with its new ventures, particularly the power generation businesses in Myanmar and Indonesia. While there could be many pitfalls, Teo figures he's steering ISDN down the right path.

"These countries are in great shortage of electricity," he says. "The installed base [of electricity] per capita in Myanmar is only 5% of Singapore's. It's too small. In Indonesia, the government's target is to have 75,000mw of hydroelectricity in the whole country. At the moment, only about 6% has been built. The potential is huge." ■