

## Serial System Ltd

1H11 results update

## Overweight

**Current Price** **S\$0.137**  
22 August 2011

**Fair Value** **S\$0.20**

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## Historical Chart



Source: Bloomberg

## Stock Statistics

|                           |           |
|---------------------------|-----------|
| <b>Market Cap</b>         | S\$112.5m |
| <b>52-HI</b>              | S\$0.185  |
| <b>52-LOW</b>             | S\$0.123  |
| <b>Avg Vol (1 yr)</b>     | 2,060,865 |
| <b>Shares Outstanding</b> | 821.3m    |
| <b>Free Float</b>         | 428.4m    |

## Key Indicators

|                    |       |
|--------------------|-------|
| <b>ROE 11F</b>     | 13.7% |
| <b>ROA 11F</b>     | 5.5%  |
| <b>P/BK</b>        | 1.15x |
| <b>Net gearing</b> | 0.74x |

## Major Shareholders

|                           |       |
|---------------------------|-------|
| <b>Derek Goh Bak Heng</b> | 36.9% |
| <b>Goi Seng Hui</b>       | 11.6% |

## Spot on

- **Earnings estimate spot on.** Despite 2H10 sales coming in 15% below our expectation, Serial System's net profit of S\$7.1m was spot on due mainly to higher-than expected investment income, forex hedging gain and lower-than-expected taxation. 1H11 results represent 43% of our full-year forecast.
- **Sales increased by 7% yoy to S\$396m in 1H11.** The growth was driven largely by the healthy demand for electronics products in most of the Asian market. South and South East Asia increased 22% yoy while North Asia (comprising Greater China, South Korea and Taiwan) grew by 4% yoy. Sales from North Asia accounted for 85% of the group's total sales for 1H11 (87% in 1H10) with China covering 55%.
- **Gross margins decreased by 0.6% pt yoy to 9% in 1H10** due to the highly competitive electronics industry and strengthening in Asian currencies. Including the S\$0.7m forex gain and higher financial cost, pretax dropped 9% yoy but net profit increased 10% yoy after lower taxation.
- **S\$17m negative free cash flow generated in 1H11** due mainly to higher working capital and expansion requirements (CCC days increased by 18 days hoh to 70 days). Including the new acquisition of Intraco Technology Pte Ltd, its net gearing increased from 44% as at end-Dec10 to 74%. The board declared a higher 0.3 cts interim dividend as compared to 0.28 cts in previous years.
- **What we like...** Serial continues to gain market share, in USD term, its sales actually grew 18% yoy in 1H11, while the global chip sales in the 2Q were down 2% qoq and 0.5% yoy, according to the Semiconductor Industry Association (SIA). TDR is still in the works despite the uncertain market sentiment. The Chairman, Mr Derek Goh continues to purchase shares from open market. An attractive dividend yield. **...and what we don't like.** Lower-than-expected gross profit margin and high gearing building up (107% gross gearing as at end-Jun11), however, we understand this is natural for a distribution business.
- **Maintain forecasts and Overweight call.** Despite the lower-than-expected 1H11 sales and margin, we have kept our FY11-13 number relative unchanged after we lower our taxation forecast. Our fair value remains unchanged at S\$0.20, still based on 10x FY11 PER. Group offers an attractive yield at 7%. **Maintain Overweight.**

## Key Financial Data

| (S\$ m, FYE Dec)         | 2009  | 2010  | 2011F | 2012F | 2013F   |
|--------------------------|-------|-------|-------|-------|---------|
| <b>Sales</b>             | 556.5 | 746.2 | 858.2 | 944.1 | 1,038.6 |
| <b>Gross Profit</b>      | 48.6  | 69.4  | 77.2  | 85.0  | 88.3    |
| <b>Net Profit</b>        | 7.5   | 16.2  | 16.8  | 18.5  | 17.2    |
| <b>EPS (cents)</b>       | 1.0   | 2.0   | 2.0   | 2.3   | 2.1     |
| <b>EPS growth (%)</b>    | 7.2   | 90.7  | 3.6   | 10.3  | (6.8)   |
| <b>PER (x)</b>           | 13.3  | 7.0   | 6.7   | 6.1   | 6.5     |
| <b>NTA/share (cents)</b> | 10.9  | 12.0  | 13.3  | 14.6  | 15.8    |
| <b>DPS (cents)</b>       | 0.5   | 1.0   | 0.9   | 1.0   | 0.9     |
| <b>Div Yield (%)</b>     | 3.7   | 6.9   | 6.7   | 7.4   | 6.9     |

Source: Company, NRA Capital estimates

## Results comparison

| FYE Dec (S\$ m)      | 1H11       | 1H10       | yoy %<br>chg | 2H10        | hoh %<br>chg | Prev.<br>1H11F | Comments  |
|----------------------|------------|------------|--------------|-------------|--------------|----------------|---|
| Revenue              | 396.3      | 371.0      | 7            | 375.2       | 6            | 465.5          | 15% below expectation   |
| Operating costs      | (386.7)    | (359.9)    | 7            | (364.8)     | 6            | (451.5)        | Below, lower-than-expected sales  |
| EBITDA               | 9.6        | 11.1       | (13)         | 10.5        | (8)          | 14.0           | Below, lower-than-expected sales and margins                            |
| EBITDA margin (%)    | 2.4        | 3.0        |              | 2.8         |              | 3.0            | Below, 0.6% point below our expectation                                 |
| Depn & amort.        | (1.7)      | (1.1)      | 56           | (1.3)       | 26           | (1.2)          | Above, higher capex spending  |
| EBIT                 | 7.9        | 10.0       | (21)         | 9.1         | (13)         | 12.8           | Below, lower-than-expected sales and margins                            |
| Interest expense     | (1.4)      | (0.9)      | 49           | (1.3)       | 12           | (1.6)          | Below   |
| Interest & invt inc  | 2.3        | 0.6        | 301          | 4.5         | (48)         | 0.4            | Above, gain on invt. properties, fin instruments and forex hedging gain |
| Associates' contrib  | 0.1        | 0.2        | (47)         | 0.2         | (59)         | 0.2            | Below   |
| Exceptionals         | 0.0        | 0.0        | 0            | 0.0         | 0            | 0.0            |   |
| <b>Pretax profit</b> | <b>8.9</b> | <b>9.8</b> | <b>(9)</b>   | <b>12.6</b> | <b>(29)</b>  | <b>11.7</b>    | Below, lower-than-expected sales and margins                            |
| Tax                  | (1.5)      | (2.7)      | (42)         | (2.3)       | (31)         | (3.8)          | Below, lower-than-expected taxation                                     |
| Tax rate (%)         | 17.3       | 27.4       |              | 17.9        |              | 32.1           | Lower-than-expected taxation  |
| Minority interests   | (0.3)      | (0.6)      | (54)         | (0.7)       | (57)         | (0.9)          | Below   |
| <b>Net profit</b>    | <b>7.1</b> | <b>6.5</b> | <b>10</b>    | <b>9.7</b>  | <b>(27)</b>  | <b>7.1</b>     | Spot on   |
| EPS (cts)            | 0.9        | 0.9        | (3)          | 1.2         | (27)         | 0.9            |   |

Source: NRA Capital estimates

| <b>Profit &amp; Loss</b> (S\$ m, FYE Dec) | <b>2009</b> | <b>2010</b> | <b>2011F</b> | <b>2012F</b> | <b>2013F</b> |
|---|-------------|-------------|--------------|--------------|--------------|
| Revenue                                   | 556.5       | 746.2       | 858.2        | 944.1        | 1,038.6      |
| Operating expenses                        | (547.7)     | (724.7)     | (836.0)      | (917.2)      | (1,013.2)    |
| EBITDA                                    | 8.8         | 21.6        | 22.3         | 26.9         | 25.4         |
| Depreciation & amortisation               | (1.6)       | (2.4)       | (2.4)        | (2.4)        | (2.4)        |
| EBIT                                      | 7.2         | 19.2        | 19.8         | 24.5         | 23.0         |
| Net interest & invt income                | 1.7         | 2.9         | 2.3          | 1.1          | 0.7          |
| Associates' contribution                  | 0.2         | 0.4         | 0.4          | 0.4          | 0.4          |
| Exceptional items                         | 0.0         | 0.0         | 0.0          | 0.0          | 0.0          |
| <b>Pretax profit</b>                      | <b>9.1</b>  | <b>22.4</b> | <b>22.6</b>  | <b>26.0</b>  | <b>24.1</b>  |
| Tax                                       | (1.3)       | (4.9)       | (4.5)        | (6.1)        | (5.3)        |
| Minority interests                        | (0.4)       | (1.3)       | (1.3)        | (1.4)        | (1.6)        |
| <b>Net profit</b>                         | <b>7.5</b>  | <b>16.2</b> | <b>16.8</b>  | <b>18.5</b>  | <b>17.2</b>  |
| Wt. shares (m)                            | 724.1       | 821.1       | 821.3        | 821.3        | 821.3        |
| Shares at year-end (m)                    | 724.1       | 821.1       | 821.3        | 821.3        | 821.3        |

| <b>Balance Sheet</b> (S\$ m, as at Dec)     | <b>2009</b>  | <b>2010</b>  | <b>2011F</b> | <b>2012F</b> | <b>2013F</b> |
|---|--------------|--------------|--------------|--------------|--------------|
| Fixed assets                                | 6.0          | 15.0         | 17.2         | 18.3         | 19.5         |
| Intangible assets                           | 12.8         | 10.0         | 9.5          | 9.1          | 8.6          |
| Other long-term assets                      | 20.7         | 29.5         | 32.4         | 35.6         | 39.1         |
| <b>Total non-current assets</b>             | <b>39.5</b>  | <b>54.6</b>  | <b>59.1</b>  | <b>63.0</b>  | <b>67.2</b>  |
| Cash and equivalents                        | 20.7         | 31.3         | 37.9         | 36.3         | 36.9         |
| Stocks                                      | 70.1         | 91.7         | 93.7         | 103.1        | 114.0        |
| Trade debtors                               | 63.7         | 93.0         | 106.9        | 116.3        | 128.0        |
| Other current assets                        | 6.4          | 7.8          | 9.0          | 10.4         | 12.1         |
| <b>Total current assets</b>                 | <b>161.0</b> | <b>223.7</b> | <b>247.5</b> | <b>266.1</b> | <b>291.1</b> |
| Trade creditors                             | 49.0         | 72.5         | 79.8         | 89.7         | 98.7         |
| Short-term borrowings                       | 44.3         | 68.5         | 77.2         | 75.5         | 83.1         |
| Other current liabilities                   | 11.0         | 14.4         | 13.5         | 14.8         | 15.0         |
| <b>Total current liabilities</b>            | <b>104.3</b> | <b>155.4</b> | <b>170.5</b> | <b>180.0</b> | <b>196.7</b> |
| Long-term borrowings                        | 2.1          | 11.2         | 12.9         | 14.2         | 15.6         |
| Other long-term liabilities                 | 0.6          | 0.8          | 0.8          | 0.8          | 0.8          |
| <b>Total long-term liabilities</b>          | <b>2.7</b>   | <b>12.0</b>  | <b>13.7</b>  | <b>15.0</b>  | <b>16.4</b>  |
| <b>Shareholders' funds</b>                  | <b>92.0</b>  | <b>108.2</b> | <b>118.5</b> | <b>128.7</b> | <b>138.2</b> |
| Minority interests                          | 1.6          | 2.7          | 4.0          | 5.4          | 6.9          |
| NTA/share (S\$)                             | 0.11         | 0.12         | 0.13         | 0.15         | 0.16         |
| <b>Total Assets</b>                         | <b>200.5</b> | <b>278.3</b> | <b>306.6</b> | <b>329.1</b> | <b>358.2</b> |
| <b>Total Liabilities + S'holders' funds</b> | <b>200.5</b> | <b>278.3</b> | <b>306.6</b> | <b>329.1</b> | <b>358.2</b> |

| <b>Cash Flow</b> (S\$ m, FYE Dec)   | <b>2009</b>   | <b>2010</b>   | <b>2011F</b>  | <b>2012F</b>  | <b>2013F</b>  |
|-------------------------------------|---------------|---------------|---------------|---------------|---------------|
| Pretax profit                       | 9.1           | 22.4          | 22.6          | 26.0          | 24.1          |
| Depreciation & non-cash adjustments | 5.9           | 6.6           | 5.1           | 2.9           | 3.5           |
| Working capital changes             | (16.7)        | (36.2)        | (11.7)        | (12.2)        | (17.4)        |
| Cash tax paid                       | (2.1)         | (1.1)         | (4.5)         | (3.0)         | (3.8)         |
| Others                              | 0.0           | 0.0           | 0.0           | 0.0           | 0.0           |
| <b>Cash flow from operations</b>    | <b>(3.7)</b>  | <b>(8.3)</b>  | <b>11.4</b>   | <b>13.8</b>   | <b>6.4</b>    |
| Capex                               | (5.8)         | (9.8)         | (3.1)         | (2.1)         | (2.1)         |
| Net investments & sale of FA        | (4.0)         | (5.2)         | 0.0           | 0.0           | 0.0           |
| Others                              | (0.2)         | (1.1)         | (0.3)         | (0.3)         | (0.3)         |
| <b>Cash flow from investing</b>     | <b>(10.0)</b> | <b>(16.1)</b> | <b>(3.5)</b>  | <b>(2.5)</b>  | <b>(2.5)</b>  |
| Debt raised/(repaid)                | 16.1          | 33.3          | 10.4          | (0.4)         | 9.0           |
| Equity raised/(repaid)              | 6.3           | 8.7           | 0.0           | 0.0           | 0.0           |
| Dividends paid                      | (2.5)         | (4.9)         | (7.5)         | (8.3)         | (7.7)         |
| Cash interest & others              | (0.9)         | (2.1)         | (4.3)         | (4.3)         | (4.5)         |
| <b>Cash flow from financing</b>     | <b>19.1</b>   | <b>35.0</b>   | <b>(1.4)</b>  | <b>(13.0)</b> | <b>(3.3)</b>  |
| <b>Change in cash</b>               | <b>5.4</b>    | <b>10.6</b>   | <b>6.6</b>    | <b>(1.6)</b>  | <b>0.7</b>    |
| <b>Change in net cash/(debt)</b>    | <b>(10.7)</b> | <b>(22.7)</b> | <b>(3.9)</b>  | <b>(1.2)</b>  | <b>(8.3)</b>  |
| <b>Ending net cash/(debt)</b>       | <b>(25.6)</b> | <b>(48.3)</b> | <b>(52.2)</b> | <b>(53.4)</b> | <b>(61.7)</b> |

| <b>KEY RATIOS</b> (FYE Dec) | <b>2009</b> | <b>2010</b> | <b>2011F</b> | <b>2012F</b> | <b>2013F</b> |
|-----------------------------|-------------|-------------|--------------|--------------|--------------|
| Revenue growth (%)          | 9.0         | 34.1        | 15.0         | 10.0         | 10.0         |
| EBITDA growth (%)           | (11.4)      | 144.8       | 3.2          | 20.9         | (5.6)        |
| Pretax margins (%)          | 1.6         | 3.0         | 2.6          | 2.8          | 2.3          |
| Net profit margins (%)      | 1.3         | 2.2         | 2.0          | 2.0          | 1.7          |
| Interest cover (x)          | 5.2         | 18.6        | 11.2         | 10.6         | 9.9          |
| Effective tax rates (%)     | 14.1        | 22.1        | 20.0         | 23.5         | 22.0         |
| Net dividend payout (%)     | 49.5        | 48.2        | 45.0         | 45.0         | 45.0         |
| Debtors turnover (days)     | 38.3        | 38.3        | 42.5         | 43.2         | 42.9         |
| Stock turnover (days)       | 39.8        | 43.6        | 43.3         | 41.8         | 41.7         |
| Creditors turnover (days)   | 24.7        | 29.7        | 32.4         | 32.8         | 33.1         |

Source: Company, NRA Capital Estimates

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