

## Fully Valued S\$0.21 STI : 3,819.78

Price Target : 12-Month S\$ 0.14

Reason for Report : Company Update

Potential Catalyst: Margin improvement in North Asian distribution business

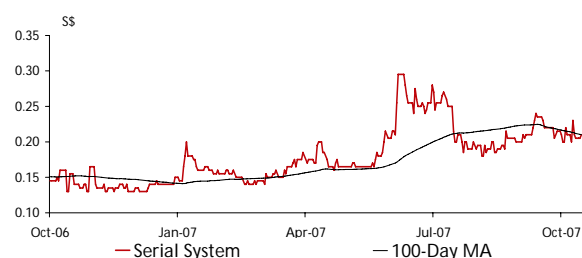
## ANALYST

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## FORECASTS AND VALUATION

FY Dec (\$\$ m)	2005A	2006A	2007F	2008F
Turnover	303.7	364.4	410.0	451.0
EBITDA	(0.2)	(1.4)	(1.0)	11.3
Pre-tax Profit	(5.1)	(4.1)	1.9	6.9
Net Profit	(6.0)	(5.0)	1.8	5.9
Net Pft (Pre Ex.)	(6.0)	(7.0)	(5.3)	5.9
EPS (S cts)	(2.0)	(1.4)	0.5	1.5
EPS Gth (%)	48	(31)	(134)	234
Diluted EPS (S cts)	(1.9)	(1.1)	0.4	1.3
Net DPS (S cts)	0.0	0.9	2.7	1.0
BVPer Share (S cts)	22.3	22.3	20.9	19.7
PE (X)	(10.7)	(15.4)	45.7	13.7
P/Cash Flow (X)	(13.4)	(35.0)	20.0	10.4
EV/EBITDA (X)	(552.7)	(78.8)	(109.1)	10.3
Net Div Yield (%)	0.0	4.1	12.9	4.8
P/Book Value (X)	0.9	0.9	1.0	1.1
Net Debt/Equity (X)	0.5	0.4	0.3	0.5
ROAE (%)	(7.6)	(6.1)	2.2	7.6

## SHARE PRICE CHART



## AT A GLANCE

Issued Capital (m shrs)	374
Mkt. Cap (S\$m/US\$m)	79 / 54
Major Shareholders	
Derek Goh Bak Heng (%)	37.9
Goi Seng Hui (%)	11.3
Free Float (%)	50.8
Avg. Daily Vol. ('000)	419

Earnings Rev (%)	2007: 52.4	2008: 198.7
Consensus EPS (S cts)	2007: -	2008: -
Variance vs Cons (%)	2007: -	2008: -

Sector : Technology

Bloomberg/Reuters Code: SERL SP/SERL.SI

Principal Business: Distributor of electrical and electronics components

## SGX MAS Research Incentive scheme

## Serial System

## Margins continue to be challenged

➤ **Story:** 2H07 revenues expected to be 10% higher y-o-y but we expect the Group to report losses of around S\$2.2m in 2H07. FY07 earnings should still be positive, owing to exceptional gains in 1H07. FY08 prospects look brighter, on the back of profit guarantees from subsidiaries.

➤ **Point:** Margins declined in 1H07 and competitive pressures are likely to remain for the rest of the year. Further expenses may be incurred to strengthen distribution network in Greater China. EPS growth is also limited by dilution resulting from proposed rights cum warrants issue.

➤ **Relevance:** Valuations for the counter look stretched currently. With NTA per share declining to S\$0.19, our recommendation is maintained at Fully Valued with an unchanged target price of S\$0.14, based on 0.8x P/BV.

**2H07 revenues expected to be higher y-o-y.** We project revenues in 2H07 to grow by about 10% y-o-y to more than S\$190m and FY07 revenues to register a 12.5% increase to S\$410m. This will mainly be driven by increased distribution revenue from North Asia (comprising China, Taiwan and South Korea), which now constitutes about 90% of revenue. Margins, however, will continue to be depressed as the distribution business remains competitive and the Group incurs greater operating expenses to strengthen channels in North Asia.

**Minority share buyout.** Management has recently embarked on a consolidation drive and is buying out the minority shareholders in 3 group companies – Serial Microelectronics (HK) (“SMHK”), Serial Microelectronics Ltd, Taiwan (“SMTW”) and Tong Baek Trading (“TBT”) for a total purchase consideration of S\$4.3m. This will be satisfied by issuing 15.48m new shares at a price of S\$0.28 per share.

**Profit guarantees.** The purchase consideration is based on 7 times the profit warranty for FY08 for the respective companies. The minority shareholders have guaranteed that SMHK, SMTW and TBT will respectively achieve FY08 net profit of S\$3.80m, S\$1.37m and S\$3.65m.

**Share base diluted.** The company had earlier proposed an interim cum special dividend of 2.7 cents per share and a rights-cum-warrants issue. Dividends will be paid out from the gains on sale of stake in Wintech and excess Sec 44 tax credits. The special dividend of 1.7 cents per share can be used by shareholders to subscribe to the rights cum warrants issue, thereby converting some of the company's reserves into share capital and also raising working capital, in the event of conversion of warrants, up to a maximum of S\$10.2m. However, the issue could be more than 70% dilutive.

**Maintain Fully Valued, TP S\$0.14.** Further to impairment and provisioning losses, NTA/ share has reduced to S\$0.19 and current valuations at 1.1x P/BV look stretched. We maintain our Fully Valued recommendation at TP S\$0.14, based on 0.8x P/BV.

## Company Focus

## Serial System

### Income Statement (\$\$ m)

FY Dec	2005A	2006F	2007F	2008F
Turnover	303.7	364.4	410.0	451.0
Cost of Goods Sold	(270.2)	(328.6)	(375.1)	(408.1)
<b>Gross Profit</b>	<b>33.5</b>	<b>35.8</b>	<b>34.8</b>	<b>42.8</b>
Other Opg (Exp)/Inc	(37.5)	(37.8)	(37.3)	(33.7)
<b>EBIT</b>	<b>(4.0)</b>	<b>(2.0)</b>	<b>(2.4)</b>	<b>9.2</b>
Other Non Opg (Exp)/Inc	0.0	0.0	0.0	0.0
Associates & JV Inc	1.3	(1.1)	(0.4)	0.2
Net Interest (Exp)/Inc	(2.4)	(3.0)	(2.4)	(2.4)
Exceptional Gain/(Loss)	0.0	2.0	7.1	0.0
<b>Pre-tax Profit</b>	<b>(5.1)</b>	<b>(4.1)</b>	<b>1.9</b>	<b>6.9</b>
Tax	(0.9)	(0.4)	(0.3)	(1.2)
Minority Interest	0.0	(0.5)	0.2	0.1
Preference Dividend	0.0	0.0	0.0	0.0
<b>Net Profit</b>	<b>(6.0)</b>	<b>(5.0)</b>	<b>1.8</b>	<b>5.9</b>
Net profit before Except.	(6.0)	(7.0)	(5.3)	5.9
EBITDA	(0.2)	(1.4)	(1.0)	11.3
Sales Gth (%)	(3.2)	20.0	12.5	10.0
EBITDA Gth (%)	(107.5)	630.7	(32.3)	(1,269.1)
EBIT Gth (%)	(11.3)	(50.1)	21.5	(477.1)
Effective Tax Rate (%)	N/A	N/A	17.0	17.0

### Cash Flow Statement (\$\$ m)

FY Dec	2005A	2006F	2007F	2008F
Pre-Tax Profit	(5.1)	(4.1)	1.9	6.9
Dep. & Amort.	2.5	1.7	1.9	2.0
Tax Paid	(1.6)	(1.1)	(1.0)	(0.3)
Assoc. & JV Inc/(loss)	(1.3)	1.1	0.4	(0.2)
Chg in Wkg.Cap.	(10.9)	(10.5)	(8.4)	(7.6)
Other Operating CF	6.4	0.9	(5.0)	0.0
<b>Net Operating CF</b>	<b>(10.0)</b>	<b>(12.1)</b>	<b>(10.3)</b>	<b>0.9</b>
Capital Exp.(net)	(0.5)	0.0	(2.0)	(2.0)
Other Invts.(net)	(2.3)	16.2	24.8	0.0
Invts in Assoc. & JV	(3.0)	3.2	(3.6)	0.0
Div from Assoc & JV	0.0	1.6	0.0	0.0
Other Investing CF	0.9	(0.3)	0.0	0.0
<b>Net Investing CF</b>	<b>(4.9)</b>	<b>20.7</b>	<b>19.2</b>	<b>(2.0)</b>
Div Paid	(0.6)	0.0	(3.2)	(10.3)
Chg in Gross Debt	12.1	(8.0)	0.0	0.0
Capital Issues	7.0	0.0	4.9	0.0
Other Financing CF	1.8	(2.2)	0.0	0.0
<b>Net Financing CF</b>	<b>20.3</b>	<b>(10.2)</b>	<b>1.7</b>	<b>(10.3)</b>
Net Cashflow	5.4	(1.6)	10.6	(11.4)

### Quarterly / Interim Income Statement (\$\$ m)

FY Dec	2H2005	1H2006	2H2006	1H2007
Turnover	177.0	192.3	172.1	217.9
Cost of Goods Sold	(158.1)	(173.6)	(154.9)	(199.3)
<b>Gross Profit</b>	<b>18.9</b>	<b>18.7</b>	<b>17.1</b>	<b>18.6</b>
Other Oper. (Exp)/Inc	(20.7)	(16.7)	(21.1)	(20.0)
<b>EBIT</b>	<b>(1.8)</b>	<b>2.0</b>	<b>(4.0)</b>	<b>(1.4)</b>
Other Non Opg (Exp)/Inc				
Associates & JV Inc	0.4	1.4	(2.5)	(0.3)
Net Interest (Exp)/Inc	(1.4)	(1.5)	(1.5)	(1.2)
Exceptional Gain/(Loss)	0.0	2.0	0.0	7.1
<b>Pre-tax Profit</b>	<b>(2.8)</b>	<b>3.9</b>	<b>(8.0)</b>	<b>4.2</b>
Tax	(0.7)	(0.2)	(0.2)	(0.3)
Minority Interest	0.2	(0.4)	(0.1)	0.1
<b>Net Profit</b>	<b>(3.2)</b>	<b>3.3</b>	<b>(8.3)</b>	<b>4.0</b>
Net profit bef Except.	(3.2)	1.3	(8.3)	(3.1)
EBITDA	1.1	4.3	(5.8)	(1.0)
Sales Gth (%)	39.7	8.7	(10.5)	26.6
EBITDA Gth (%)	(185.4)	278.1	(233.1)	(83.2)
EBIT Gth (%)	(18.5)	(212.8)	(298.5)	(66.5)
Gross Margins (%)	10.7	9.7	9.9	8.5
EBIT Margins (%)	(1.0)	1.1	(2.3)	(0.6)

Source: Company, DBS Vickers

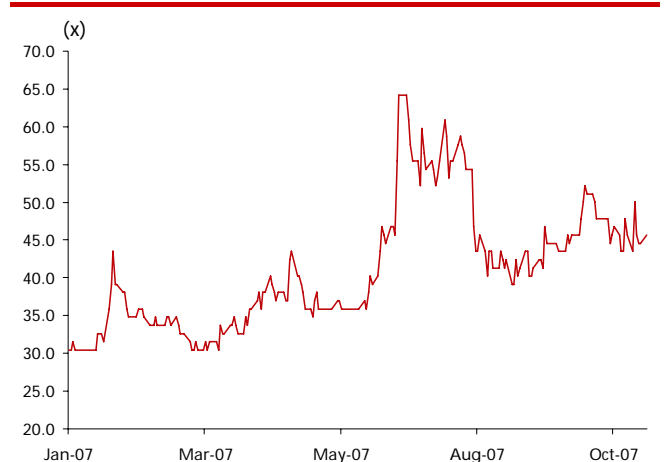
### Balance Sheet (\$\$ m)

FY Dec	2005A	2006F	2007F	2008F
Net Fixed Assets	17.1	15.4	15.8	16.0
Invts in Assocs & JVs	38.1	0.0	3.2	3.4
Other LT Assets	12.6	35.0	9.9	9.7
Cash & ST Invts	14.5	12.9	23.6	12.1
Other Current Assets	114.0	121.6	136.6	150.1
<b>Total Assets</b>	<b>196.5</b>	<b>184.9</b>	<b>189.1</b>	<b>191.3</b>
ST Debt	34.6	32.3	32.3	32.3
Other Current Liab	54.5	53.8	59.7	66.5
LT Debt	19.9	15.0	15.0	15.0
Other LT Liabilities	1.6	0.7	0.7	0.7
Shareholder's Equity	81.5	81.2	79.7	75.3
Minority Interests	4.3	1.9	1.7	1.6
<b>Total Cap. &amp; Liab.</b>	<b>196.5</b>	<b>184.9</b>	<b>189.1</b>	<b>191.3</b>
Non-Cash Wkg. Cap	59.6	67.8	76.9	83.6
Net Cash/(Debt)	(40.1)	(34.4)	(23.7)	(35.2)

### Rates & Ratios

FY Dec	2005A	2006F	2007F	2008F
Gross Margin (%)	11.0	9.8	8.5	9.5
EBITDA Margin (%)	(0.1)	(0.4)	(0.2)	2.5
EBIT Margin (%)	(1.3)	(0.5)	(0.6)	2.0
Net Profit Margin (%)	(2.0)	(1.4)	0.4	1.3
ROAE (%)	(7.6)	(6.1)	2.2	7.6
ROA (%)	(3.4)	(2.6)	0.9	3.1
ROCE (%)	(3.4)	(1.6)	(1.8)	7.0
Div Payout Ratio (%)	N/A	N/A	587.1	65.1
Interest Cover (x)	(1.7)	(0.7)	(1.0)	3.8
Debtors Turn (avg days)	57.5	61.5	57.3	57.9
Creditors Turn (avg days)	41.9	50.4	49.9	51.8
Inventory Turn (avg days)	58.1	60.7	61.5	62.8
Current Ratio (x)	1.4	1.6	1.7	1.6
Quick Ratio (x)	0.9	0.9	1.0	0.9
Net Debt/Equity (X)	0.5	0.4	0.3	0.5
Capex to Debt (%)	0.8	(0.1)	4.2	4.2
N.Cash/(Debt)PS (S cts)	(11.0)	(9.4)	(6.2)	(9.2)
Opg CFPS (S cts)	0.3	(0.4)	(0.5)	2.2
Free CFPS (S cts)	(3.4)	(3.3)	(3.2)	(0.3)

### PE Chart (x)



DBSV recommendations are based on an Absolute Total Return\* Rating system, defined as follows:

**STRONG BUY** (>20% total return over the next 3 months, with identifiable share price catalysts within this time frame)

**BUY** (>15% total return over the next 12 months for small caps, >10% for large caps)

**HOLD** (0-15% total return over the next 12 months for small caps, 0-10% for large caps)

**FULLY VALUED** (negative total return i.e. > -10% over the next 12 months)

**SELL** (negative total return of > -20% over the next 3 months, with identifiable catalysts within this time frame)

*Share price appreciation + dividends*

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