

Analyse this...

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Serial System Ltd

The night is still young – party on

 SERL SP
 BUY; TP: S\$0.175

 Price @4/8/10: S\$0.13
 52-week range (SGD): 0.06 – 0.135
 Market cap – S\$95.1m

Second half should be exciting still

- **Fundamental:** Maintain **BUY**. Target price raised to **S\$0.175** still based on 20% discount to sector CY11 average P/E of 9.7x.
- **Technical:** Prices could climb a while longer towards S\$0.15-0.165.
- 1H results strong with sales driven by North Asia, especially industrial products. 1H net profit of S\$6.5m is almost 87% of FY09 profit. Management expects demand into 2H10 to remain strong with 3Q bettering 2Q performance.
- Interim DPS of 0.28cts is more than doubled that of 1H09. The dividends will be payable on 1st September 2010. Shares go ex-dividend on 17th August.

What's worth watching

- Management's plan is to payout 40-50% of profit with interim dividends representing one third of full year dividend payout. This would suggest still attractive prospective yields 6-8%.
- Taiwan is only 4% of Group sales. Given the scale of the electronics sector in Taiwan, Serial will likely step up efforts increase revenue contribution from Taiwan. Don't expect fire works though as Serial will be sensible and target second/third tier suppliers instead of head on competition with established peers such as WPG.
- In line with plans to grow the Taiwanese business, management may consider a TDR listing to raise funds. In addition, a TDR listing could give greater comfort to Taiwanese banks and make it easier for Serial to partially fund its growth via bank borrowings from Taiwanese banks.

Potential pitfalls

- Serial System is in the distribution business; as such it should not be a surprise to see net gearing rising to 0.6x in 1H10 given the 62% increase in sales. Net gearing in FY09 was 0.3x and in was 0.2x 1H09. We know the risk of high gearing and so does Serial's CEO. Proceeds from conversion of its outstanding warrants by end CY10 and a possible TDR listing should be able to bring the gearing level down again.
- The other risks to watch out for in 2H10 continue to be risk from bad debts, inventory provisioning and the strong Singapore dollar versus the US dollar.

Financial analysis

FYE Dec	2008	2009	2010F	2011F	2012F
Revenue (S\$ m)	510.6	556.5	695.7	820.9	903.0
EBITDA (S\$ m)	11.5	11.8	20.5	24.9	28.1
EBITDA margins (%)	2.3	2.1	2.9	3.0	3.1
Pretax profit (S\$ m)	8.0	9.1	17.2	21.5	24.7
Net profit (S\$ m)	6.0	7.5	13.0	16.3	18.8
EPS (cts)	1.0	1.1	1.8	2.2	2.6
EPS growth (%)	-49%	+13%	+64%	+26%	+15%
P/E (x)	13.5	11.9	7.3	5.8	5.0
FD EPS (cts)	1.0	0.9	1.6	2.0	2.3
FD P/E (x)	13.5	14.4	8.3	6.6	5.7
Gross DPS (cts)	0.6	0.5	0.8	0.9	1.0
Dividend yield (%)	4.3	3.9	6.2	6.9	8.0
P/NTA (x)	1.1	1.2	1.1	1.0	0.9
ROE (%)	7.5	8.6	13.4	15.4	16.1
Net gearing (%)	18.4	27.4	21.1	21.8	16.9
P/ICF (x)	10.6	10.6	6.5	5.2	4.6
EV/EBITDA (x)	10.1	9.8	5.7	4.7	4.1

Source: Bloomberg, CIMB Research

Results summary

	1H10	1H09	yoy chg (%)
Sales (S\$ mil)	371.0	229.1	62.0
Gross profit (S\$ mil)	35.7	20.6	73.4
Operating profit (S\$ mil)	9.8	1.9	406.7
Net profit (S\$ mil)	6.5	1.2	447.5
			Chg (in ppt)
Gross profit margin (%)	9.6	9.0	0.6
Operating profit margin (%)	2.6	0.8	1.8
Net profit margin (%)	1.7	0.5	1.2
			yoy chg (%)
EPS (Sing cts)	0.9	0.2	368.4
Net asset value per share (Sing cts)	13.6	12.1	12.6
Current ratio (x)	1.4	1.8	
Quick ratio (x)	0.9	1.2	
Net gearing (x)	0.6	0.2	
ROE (%)	13.4	2.8	
Receivables days	54	49	
Inventory days	45	39	
Payable days	39	32	
Cash cycle in days	60	56	

Source: CIMB Research, Company

Peer valuation

	Mkt cap (US\$ m)	Core P/E (x)		P/BV (x)		ROE (%)
		CY2010	CY2011	CY2010	CY2010	
Arrow Electronics Inc	2,993	6.7	6.5	0.9	14.4	
Avnet Inc	3,927.7	8.8	7.9	1.3	11.8	
US peer average		7.8	7.2	1.1	13.1	
WPG Holdings Co Ltd	1,981	12.5	11.1	2.8	23.8	
Yosun Industrial Corp	654.6	14.2	13.4	-	-	
Taiwanese peer average		13.4	12.3	1.4	11.9	
Sector average		10.6	9.7	1.2	12.5	

Source: Bloomberg, CIMB Research

About Serial System

- Serial System was established in Singapore in 1988 as a distributor of semiconductors and electronic components in the Asia Pacific region, offering design support, materials planning, inventory management, programming and assembly services.
- The Group also provides technology solutions and aims to add value to its customers with turnkey design, warehousing and logistics services. Products distributed by Serial System are used in the semiconductor, medical, automotive, office automation, telecommunications and consumer electronics industries.
- Serial System has an established presence in key Asian markets such as China, Hong Kong, Malaysia, Korea, Taiwan, Thailand, Philippines, India and Vietnam.

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