Mercury Securities Sdn Bhd

RESULTS REPORT

08 Nov 2012

ECS ICT Berhad		***Market Price:***	*RM1.10*
		Market Capitalisation:	*RM198.0m*
		Board:	*Main Market*
Recommendation:	*HOLD*	***Sector:***	*Technology*
Target price:	*RM1.06*	***Stock Code/Name:***	*5162 / ECS*

Analyst: *Edmund Tham*

KEY FINANCIALS

Key Stock Statistics	2013F
Earnings/Share (sen)	16.3
P/E Ratio (x)	6.7
Net Dividend/Share (sen)	5.5
NTA/Share (RM)	1.33
Book Value/Share (RM)	1.33
Issued Capital (mil shares)	180.0
52-weeks share price (RM)	0.80 – 1.19
Major Shareholders:	%
-ECS Holdings Ltd	41.0
-Sengin S/B	12.2
-Oasis Hope S/B	8.6
-Dasar Technologies S/B	5.5

Ratios Analysis	2010	2011	2012E	2013F
Book Value/Sh.(RM)	0.82	0.96	1.22	1.33
Earnings/Sh.(sen)	16.1	16.7	15.2	16.3
Net Dividend/Sh. (sen)	5.3	5.3	5.5	5.5
Div. Payout Ratio (%)	33.2	31.8	36.2	33.7
P/E Ratio (x)	6.8	6.6	7.2	6.7
P/Book Value (x)	1.3	1.1	0.9	0.8
Net Dividend Yield (%)	4.8	4.8	5.0	5.0
ROE (%)	19.6	17.5	12.4	12.2
Net Gearing (or Cash)(x)	(0.12)	(0.39)	(0.31)	(0.27)

**Per Share figures adjusted for the 1-for-2 Bonus Issue*

P&L Analysis (RM mil)	2010	2011	2012E	2013F
Year end: Dec 31				
Revenue	1271.5	1250.7	1274.0	1302.4
Operating Profit	41.1	40.8	35.3	37.3
Depreciation	(3.2)	(1.6)	(2.4)	(2.9)
Interest Expenses	(1.9)	(0.4)	(0.0)	(0.0)
Pre-tax Profit (PBT)	39.4	40.9	36.8	39.3
Effective Tax Rate (%)	26.3	26.4	25.6	25.2
Net Profit (NPAT)	28.9	30.1	27.4	29.4
Operating Margin (%)	3.2	3.3	2.8	2.9
Pre-tax Margin (%)	3.1	3.3	2.9	3.0
NPAT Margin (%)	2.3	2.4	2.1	2.3

**RM0.50 par value; 2012-2013 figures are our estimates*
^listed in 2010

PERFORMANCE – 3Q/FY12

3Q/ 30 Sep	3Q12	3Q11	yoy %	2Q12	qoq%
Rev (RMm)	327.9	317.9	3.2	309.3	6.0
EBIT (RMm)	8.3	7.7	8.8	7.0	18.8
NPAT (RMm)	6.5	7.1	(7.3)	5.6	16.4
EPS (sen)	3.6	3.9	(7.3)	3.1	16.4

9M/ 30 Sep	9M/FY12	9M/FY11	yoy %
Rev (RMm)	942.6	908.9	3.7
EBIT (RMm)	26.0	24.5	6.1
NPAT (RMm)	20.3	19.7	2.9
EPS (sen)	11.3	10.9	2.9

**EPS based on 180 million shares*
**NPAT=net profit after tax*

ECS ICT's 3Q/FY12 revenue (for quarter ended 30th September 2012) was within our earlier expectations, while NPAT was below.

"Q3 revenue – within expectations"

During 3Q/FY12, the group recorded revenue of RM327.9 million and NPAT of RM6.5 million. Revenue was higher by 3.2% y-o-y while NPAT was lower by 7.3% y-o-y. The higher revenue was mainly due to the higher contribution from the group's **Enterprise Systems** segment (project transactions on networking products and enterprise software). Nevertheless, the group's lower y-o-y NPAT was mainly due to the lower contribution from its **ICT Distribution** segment.

"Strong contributions from Enterprise Systems"

The group's 9M/FY12 revenue and NPAT was higher by 3.7% and 2.9% y-o-y, respectively.

The improved revenue was mainly due to the Enterprise Systems segment. The improved NPAT was achieved as the increase in profits from the Enterprise Systems segment mitigated the drop in profits from the ICT Distribution segment.

OUTLOOK/CORP. UPDATES

"ICT sector still growing"

According to PIKOM, the National ICT Association of Malaysia, the **information and communications technology (ICT) industry in Malaysia is expected to grow at a rate of between 8-10%** for 2012. As ECS ICT is the market leader in the local ICT distribution business sector, we expect the group to perform positively during 2012 and 2013.

Furthermore, the rising quantity of mobility devices in the market will increase users' needs for more internet bandwidth. As such, this higher demand for **Enterprise Systems** products for building broadband infrastructure benefits ECS ICT. The ICT industry is expected to maintain its positive expansion, aided by the federal government's programmes such as the **Economic Transformation Plan** (ETP) and Government Transformation Plan (GTP).

Malaysia's official government figures expect 2012 GDP growth of 4.5-5.0% and 2013 GDP growth of 4.5-5.5%. Bank Negara Malaysia (BNM) has still maintained its accommodative overnight policy rate (OPR) at 3.0%. The weak external environment (particularly in the US and Europe) has resulted in weak export numbers. The cautious consumer and business sentiment has somewhat slowed the growth rate of ICT spending in Malaysia.

ECS ICT has been pursuing growth in terms of its **Enterprise Systems** segment and expanding its overall **range of products and vendors**. The group is however interested only in brands and products that it believes will be accepted well by the domestic market. Recently, the group signed a new contract with **Huawei Technologies (M) S/B** to distribute its entire range of enterprise products and solutions. Meanwhile, the group is also pursuing initiatives in the area of **Cloud Computing**.

"Tablets, UltraBooks & Smartphones to drive growth in ICT Distribution segment"

For the remainder of FY12 and FY13, we are hopeful that the group would obtain positive growth in contributions from its **Ultrabook, Smartphone and Tablet PC** segments. This would offset any further weakness in revenues from Desktop PCs, Notebooks and Netbooks. ECS ICT is recording steady growth in its sales of Tablet PCs (brands such as Apple, Samsung, Asus and Lenovo) and Ultrabooks (brands such as Asus, HP, Dell and Lenovo). The group had been appointed by Asus to distribute the new Google Nexus 7 Tablet PC in Malaysia. According to GfK, Malaysia is the largest market for Tablet PCs in Southeast Asia, with sales of USD374 million in 2011.

"First foray into Smartphone distribution – with Huawei"

ECS ICT has now launched its first foray into the distribution of Smartphones – i.e. with Huawei (which is among the top mobile phone brands in China). With this launch, the group would be distributing Huawei's Ascend P1 Smartphone in Malaysia.

We view this as an **exciting new business area for the group**, as we are well aware that the Smartphone market is enjoying strong sales demand. Nevertheless, there is a plethora of Smartphone brands and models available for consumers to choose from. According to Nielsen in May 2012, nearly 60% of Malaysian mobile phone users were likely to upgrade their phones before the end of 2012 and that 80% of these were likely to purchase a Smartphone. The Smartphone penetration rate in Malaysia is said to be around 27%, meaning that there is still much room for growth in market size.

VALUATION/CONCLUSION

"Interim Dividend declared"

The group's Board of Directors (BOD) had declared a single tier interim dividend of 6% or 3 sen per share of 50 sen each for its FY12 ending 31st December 2012. The dividend will be paid on 12th December 2012 for shareholders registered as at 28th November 2012. For full years 2012 and 2013, we expect the group's dividend payout to be at least 30% of its net earnings.

Thus far, ECS (+32.0% YTD) has **outperformed the KLCI** (+7.3% YTD) in 2012. During the past year, global equity markets have been impacted by events such as the "sovereign debt" situation in Europe, the Tohoku natural disaster in Japan, the "debt ceiling" issue in the US and also the "Arab Spring" upheavals in the Middle East/North Africa. As ECS is not an especially large market-cap stock, this may put a dampener on its market visibility and trading volume. Nevertheless, the **recently completed 1-for-2 bonus issue** should have improved the stock's liquidity somewhat.

"Maintain Hold Call"

Based on our cautious forecast of ECS' FY13 EPS and estimated P/E of 7 times, we set a **FY13-end Target Price (TP) of RM1.06.** This TP represents a Hold Call and is close to the market price on the date of this report. Our TP for ECS reflects a P/BV of 0.87 times over its FY13F BV/share.

Our TP and Hold Call takes into account the stock's **positive price movement** during the year and also our **cautious view on the overall macroeconomic environment.** We would upgrade our Call on the group once it sustains a <u>stronger earnings growth</u> performance.

ECS ICT is **well placed to maintain its market leadership position** – given its growing portfolio of ICT products, extensive distribution infrastructure, partnerships with numerous key ICT principals, high operational efficiency, strong technical support team and effective financial management systems.

We find that ECS ICT's P/E and P/BV valuations are undemanding. Additionally, the group's dividend yield and ROE are also reasonably attractive. The group has been in a net cash position since its FY10 and has successfully **paid-off all its borrowings during its FY11.**

Typical for any ICT business, ECS' future earnings performance could be affected by – possible fluctuations in economic conditions, business and consumer sentiment. Possible routine risk factors include foreign exchange translation, increased peer competition, issues with account receivables, increased inventory turnover days, slim margins, short product life cycle and low market acceptance level of various ICT products.

ECS: Share Price

Source: NextView