

**1QFY08 RESULTS UPDATE**
**18<sup>th</sup> June 2008**

## SMR Technologies Berhad

**Price : RM0.26**
**Market Capitalisation : RM26 m**
**Board : MESDAQ**
**Sector : Technology**
**Stock Code: 0117**
**Recommendation : HOLD**

FYE Dec RM '000	Q-o-Q			Y-o-Y	
	1QFY08	4QFY07	% Change	1QFY07	% Change
Revenue	4,893.1	6,795.9	-28.0%	3,377.8	44.9%
EBITDA	786.4	2,150.9	-63.4%	2,102.0	-62.6%
Dep & Amort	(345.4)	303.2		(497.3)	
Net Int (Exp)/Income	(2.5)	(2.2)		-	
Share of loss in Asso co				-	
Pre-tax Profit	438.6	2,400.9	-81.7%	1,604.6	-72.7%
Eff. Tax Rate	8.3%	4.0%		0.0%	
Net Profit	402.1	2,305.3	-82.6%	1,604.6	-74.9%
EPS (sen) - basic	0.4	2.3	-82.6%	1.6	-74.9%
EBITDA %	16.1%	31.6%		62.2%	
Pre-tax %	9.0%	35.3%		47.5%	
Net Margin	8.2%	33.9%		47.5%	
Book Value (RM)	0.34	0.34		0.28	

### 1. 1QFY08 Results – Net profit is only 5% of full year forecast, but read on....

- Sales to existing customers in Malaysia, Australia and Asia were held back pending the launch of a new and upgraded version of its flagship HRDPower software. Sales to Europe and Middle East which were non-existent in 1Q 07, continue to gain momentum from their launch in the middle of last year. Sales to the US has shown tremendous achievement and account for 50% of total revenue in the current quarter. The net impact is thus sales were up 45% y-o-y but down 28% q-o-q.
- The increase in sales to USA, Europe and Middle East was secured by offering the products at discounted prices and via test-marketing. On the hand the cost of their implementation and customization were not only mostly outsourced but also incurred at prevailing market prices. Consequently these maiden projects yielded lower margins of 15-35%.
- According to the company, overall gross margin declined from 48% to 39% q-o-q, whilst administrative expenses rose 14%.
- Thus it was that net profit collapsed by 75% y-o-y and 83% q-o-q as a consequent of the company's deliberate aggressive strategy to secure a beachhead and a global market position in this very competitive industry.
- Balance sheet remains strong and Group's borrowings as at 31 March 2008 consist solely of hire purchase creditors with no other bank borrowings. The group continues to generate positive operating cash flow. The aggressive expansion of the group is reflected in the balance sheet by the sharp rise in trade receivables and drawdown of its cash reserves.
- No dividend has been recommended. The company is proposing a 1 for 3 bonus issue.

## Revenue, Cost & Balance Sheet Analysis

FYE Dec RM '000	Q-o-Q			Y-o-Y	
	1QFY08	4QFY07	% Change	1QFY07	% Change
Sales of Products	4,018.8	5,605.6	-28.3%	2,947.6	36.3%
Consulting & Outsourcing	874.3	1,190.2	-26.5%	430.1	103.3%
<b>Total Sales</b>	<b>4,893.1</b>	<b>6,795.9</b>	<b>-28.0%</b>	<b>3,377.8</b>	<b>44.9%</b>
<b>By Geographical Segment</b>					
Malaysia	1,613.6	2,049.0	-21.3%	3,175.9	-49.2%
Asia	17.6	719.5	-97.6%	77.1	-77.2%
Australia	1.3	3.0	-56.2%	3.0	-56.2%
USA	2,035.7	1,748.6	16.4%	6.9	25152.1%
Middle East	732.0	818.2	-10.5%	-	N.A
Europe	492.8	1,457.5	-66.2%	-	N.A
<b>ADMINISTRATIVE EXPENSES</b>	<b>1,448.1</b>	<b>1,844.5</b>	<b>-21.5%</b>	<b>866.7</b>	<b>67.1%</b>
As % of Sales	29.6%	27.1%		25.7%	
Gross Profit as % of Sales	38.6%	62.5%		72.5%	
<b>Margin Spread</b>	<b>9.0%</b>	<b>35.3%</b>		<b>46.8%</b>	
<b>Trade receivables</b>	<b>7,714.9</b>	<b>6,316.5</b>	<b>22.1%</b>	<b>3,122.6</b>	<b>147.1%</b>
As % of sales	157.7%	92.9%		92.4%	
<b>Trade payables</b>	<b>431.1</b>	<b>259.2</b>	<b>66.3%</b>	<b>0.0</b>	
As % of sales	8.8%	3.8%			
Cash & Deposits	806.5	2,025.5	-60.2%	4,947.0	-83.7%

## Outlook

### In the notes (B3) accompanying the results the management states that;

*“USA and Middle East will continue to be the growth focus of the Group. Despite inflation and expected reduction in spending pattern in the USA for 2008, multinationals has limited options but to budget for talent management and retention activities. As for the Middle East region, the economy will continue to prosper. Both regions will continue to create more potential for the Group's products and services. In the local front, the search for talent has become costly and tedious. Organisations, both the public and private sectors, are moving towards creating and developing their own talents from within.*

*With the launch of a more robust and dynamic version of HRDPower™ version 2 expected in the second quarter of 2008, the Company expects there will be an increase in demand for HRDPower™ version 2 which will also creates additional consulting works for the Group.*

*Based on the abovementioned, the Group expects the financial performance of SMRT for the FYE 31 December 2008 to be better than preceding year.”*

### Our comments:

In FYE07, net profit was RM6.6m compared to 1QFY08 net profit of RM0.4m.

On the revenue side, there is the 2Q launch of HRDPower2. We believe that SMR cannot sustain its 1Q strategy of aggressive sale blitz for the rest of this year as the balance sheet is unable support another heavy working capital increases – without having recourse to external financing.

Thus to maintain profits at last year's level the company will need to recover its gross margin. We understand from the management that this will be achieved by;

1. Converting the USA/Europe test sites into sales
2. Focussing on more tenders/consortium or major projects rather than retail which demands higher resource consumption.
3. Refocussing back on higher value overseas sales for increased gross margins
4. With the launch of HRDPower™ Release 2, with more features and flexibility of purchase, the Marketing efforts will restart to get back the momentum of previous years
5. Entering into new strategic alliances (like the recent acquisition of a related training business) to spread out costs.
6. Sourcing of new funding via placements to finance further working capital requirement

Of the above, the success rate of converting test sites into sales and the success of HRDPower™ Release 2 would be the main determinants of the extent that margins can recover in the current year.

Given the dismal 1Q results we do not expect that minority shareholders would be partial to any new cash calls and, at current share price, the effect could potentially be disastrously dilutive to EPS in the long term.

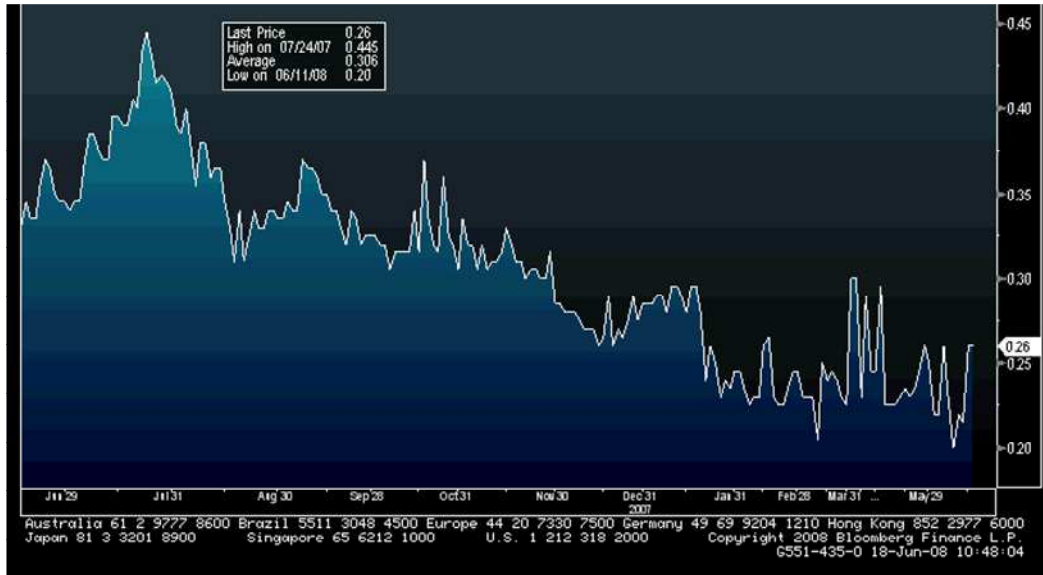
## 2. Recommendation

- Based on management feed back we maintain our profit forecast but downgrade our fair value P/E from 8 to 6. We still regard this collapse in margin to be a temporary phase and a necessary consequence of the learning curve.
- Our fair valuation is accordingly revised to RM0.44 against current price of RM0.23. The current price is a 20% discount to NTA, however until a trend reversal is evident in the 2Q results we revise our recommendation to a HOLD.

FYE Dec	FY07	FY08f
EPS (sen)	6.65	7.35
P/E (x)	3.5	3.1
Dividend/Share (sen)	1.0	
NTA/Share (sen)	28.77	
Book Value/Share (Sen)	34.15	
Issued Capital (m shares)	100.0	
52-week Hi-Low (RM)	0.175 - 0.48	
<b>Major Shareholders:</b>	<b>%</b>	
Special Flagship Holdings S/B	42.0	
Kumpulan Sentiasa Cemerlang S/B	13.2	

<i>P&amp;L Analysis (RM m)</i>			
FYE DEC	FY06	FY07	FY08f
Revenue	12.2	18.9	22.7
EBITDA	7.5	8.1	8.9
Amort of dev cost & IP	-0.5	-0.6	-0.7
Depreciation	-1.3	-0.7	-0.7
Net Int Income/Exp	0.2	0.0	0.0
Pre-tax Profit	5.8	6.8	7.6
Eff. Tax Rate	1.7%	2.3%	3.0%
Net Profit	5.7	6.6	7.4
EBITDA %	61.5%	42.9%	39.4%
Net Margin	46.7%	35.2%	32.6%
Sales Growth	53.0%	55.0%	20.0%

SMR Technologies' last 12-month share price chart



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**RATING GUIDE**

BUY	Price appreciation expected to exceed 10% within the next 12 months
SELL	Price depreciation expected to exceed 10% within the next 12 months
HOLD	Price movement expected to be between -10% and +10% over the next 12 months from current level

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