

SMR Technologies

Recommendation: **STRONG BUY**

Stock Code: 0117

Bloomberg: SMRT MK

Price: MYR0.25

12-Month Target Price: MYR0.37

Date: February 29, 2008

Board: Mesdaq

Sector: Technology

GICS: Information Technology/Application Software

Market Value - Total: MYR24.5 mln

Summary: SMR Technologies (SMR) is primarily engaged in the business of designing, developing, consulting and implementing human capital or human development systems and solutions.

Analyst: Desmond Ch'ng, ACA



Results Review & Earnings Outlook

- SMR's 2007 results were marginally (6%) above expectations, largely on account of stronger-than-expected revenue in 4Q07.
- 2007 revenue surged 56% YoY, driven by increased software sales to new clients and new markets during the year. On a segmental basis, Malaysia accounted for 49% of revenue, while the U.S., Middle East and Europe accounted for 17%, 13% and 11% respectively.
- Gross operating margin improved to 63.4% from 62.1% in 2006, a function of higher sales and better product mix. Operating margin, however, dipped to 33.8% from 36.3%. Costs came in higher due to (i) higher depreciation on its new office premise; (ii) higher amortization of products; (iii) start-up costs for unbilled projects and (iv) higher A&P for greater market reach.
- SMR's U.S. 25% joint venture, Smartha, featured with a maiden, but negligible start-up loss of MYR0.05 mln. Overall net profit thus grew by a lower quantum of 15.7% YoY. No dividends were declared for 2007 (1 sen in 2006).
- We trim our 2008 net profit forecast by a marginal 1.3% mainly on account of a higher tax rate. We introduce our 2009 net profit forecast of MYR7.9 mln.

Recommendation & Investment Risks

- We maintain our Strong Buy call on SMR, but with a lower 12-month target price of MYR0.37 versus MYR0.41 previously. Valuations remain attractive with the stock trading at a prospective 2008 PER of 3.5x and an historical P/NTA of 0.7x.
- Our target price is based on a forward 2008 PER of 5.2x (5.7x previously), which represents a 30% discount to current valuations for Hexaware Technologies (Hexaware) (HEXW IN, INR79.20, Not Ranked). Hexaware is a Mumbai-based global provider of IT and process outsourcing services, with HR-IT services being part of the varied services it offers. The discount is to reflect SMR's smaller market capitalization relative to Hexaware's.
- SMR operates in a market that offers much potential for growth, especially since it has built up credentials with large domestic companies and foreign multinationals in a wide range of industries. Bottomline growth going forward thus very much depends on just how quickly it can garner new clients while penetrating new markets e.g. the U.S. market through Smartha.
- Risks to our recommendation and target price include: (i) increasing competition from domestic and global peers, (ii) technological advancements and SMR's R&D capability in maintaining the relevance of its product; and (iii) higher-than-expected costs from new market penetration.

Key Stock Statistics

FY Dec.	2007	2008E
Reported EPS (sen)	6.6	7.1
PER (x)	3.7	3.5
Dividend/Share (sen)	0.0	0.0
NTA/Share (MYR)	0.28	0.35
Book Value/Share (MYR)	0.34	0.41
No. of Outstanding Shares (mln)	100.0	
52-week Share Price Range (MYR)	0.23 - 0.45	
Major Shareholders:	%	
Dr. Palaniappan a/l Ramanathan Chettiar	56.4	
Kumpulan Sentiasa Cemerlang	13.2	

Per Share Data

FY Dec.	2005	2006	2007	2008E
Book Value (MYR)	0.02	0.20	0.34	0.41
Cash Flow (sen)	4.1	7.1	7.3	7.8
Reported Earnings (sen)	3.6	5.7	6.6	7.1
Dividend (sen)	0.0	1.0	0.0	0.0
Payout Ratio (%)	0.0	17.4	0.0	0.0
PER (x)	6.8	4.3	3.7	3.5
P/Cash Flow (x)	6.0	3.4	3.3	3.1
P/Book Value (x)	10.2	1.2	0.7	0.6
Dividend Yield (%)	0.0	4.1	0.0	0.0
ROE (%)	NA	27.7	21.9	19.2
Net Gearing (%)	0.0	0.0	0.0	0.0

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Quarterly Performance

FY Dec. / MYR mln	4Q07	4Q06	% Change
Reported Revenue	6.8	2.8	>100
Reported Operating Profit	2.5	1.1	>100
Depreciation & Amortization	NA	NA	NA
Net Interest Income / (Expense)	0.3	0.0	NM
Reported Pre-tax Profit	2.4	1.1	>100
Reported Net Profit	2.3	1.0	>100
Reported Operating Margin (%)	36.3	40.0	-
Reported Pre-tax Margin (%)	35.2	40.0	-
Reported Net Margin (%)	33.8	37.6	-

Source: Company data

Profit & Loss

FY Dec. / MYR mln	2006	2007	2008E	2009E
Reported Revenue	12.2	18.9	22.3	25.7
Reported Operating Profit	5.8	6.9	7.4	8.3
Depreciation & Amortization	-1.8	-1.3	-1.3	-1.4
Net Interest Income / (Expense)	0.2	0.4	0.0	0.1
Reported Pre-tax Profit	5.8	6.8	7.3	8.1
Effective Tax Rate (%)	1.1	2.3	2.5	2.5
Reported Net Profit	5.7	6.6	7.1	7.9
Reported Operating Margin (%)	47.9	36.3	33.3	32.2
Reported Pre-tax Margin (%)	47.8	36.0	32.5	31.5
Reported Net Margin (%)	47.3	35.2	31.7	30.8

Source: Company data, S&P Equity Research

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Buy: Total return is expected to outperform the total return of the KLCI or KL Emas Index respectively, over the coming 12 months, with shares rising in price on an absolute basis.

Hold: Total return is expected to closely approximate the total return of the KLCI or KL Emas Index respectively, over the coming 12 months with shares generally rising in price on an absolute basis.

Sell: Total return is expected to underperform the total return of the KLCI or KL Emas Index respectively, over the coming 12 months and share price is not anticipated to show a gain.

Strong Sell: Total return is expected to underperform the total return of the KLCI or KL Emas Index respectively, over the coming 12 months by a wide margin, with shares falling in price on an absolute basis.

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For residents of Malaysia. All queries in relation to this report should be referred to Alexander Chia, Desmond Ch'ng or Ching Wah Tam.

Recommendation and Target Price History

Date	Recommendation	Target Price
New	Strong Buy	0.37
31-Dec-07	Strong Buy	0.41

