

15 May 2019

ISOTEAM (ISO SP)

Time For a Relook On Strong 3Q; Raise To BUY

Construction & Engineering | Construction

Buy (from Neutral)

Target Price (Return)	SGD0.29 (+32%)
Price:	SGD0.22
Market Cap:	USD45.8m
Avg Daily Turnover (SGD/USD)	0.1m/0.1m

- **Upgrade to BUY with a higher DCF-backed TP of SGD0.29 from SGD0.23**, 32% upside, 2% FY20F (Jun) yield. 3Q19 revenue more than doubled to SGD30.4m on the back of improved performance across all business segments. PATMI was up 251.5% YoY to SGD1.7m from SGD0.5m. We expect to see continuous improvement into FY20F. As such, we are lifting our PATMI forecast to SGD5.8m for FY19 from the initial SGD3.2m; and 8-10% growth for FY20F-21F.
- **Time to relook.** In the last quarter's results review, we wrote that there could be upside potential from improved margins from new contracts as well as successful cost control initiatives. We await further evidence. Indeed, the group revised its tendering strategy and continuously pursuing new business leads has borne fruit. We are increasing our FY19F-2F PATMI by 79%, 39%, 21% and 8% respectively.
- **12-15% gross margin the "new norm".** The company had in the past achieved gross margins of above 20%. However, due to the competitive landscape, it is inevitable that the group has to reduce its prices in order to beat its competitors and win more projects. We like management's implementation of strategies to achieve the strong set of results. Latest 3Q19 and 9M19 gross profit margins were 15.7% and 14.4%. Going forward, we expect gross profit margin to remain stable and lean towards the high end of 12-15%.
- **Orderbook holding up strong.** As at 30 Apr 19, the group orderbook remains strong at SGD128.8m (2Q19: SGD132.8m). We estimated the orderbook consists of a significant portion of the projects from the public sector and these orders would continue to drive group revenue in the next few quarters.
- **Upgrade to BUY** with higher DCF-backed TP of SGD0.29 (WACC: 5%, TG: 0%). We think that this is the time to relook at this counter as we see improvement in ISOTEAM's financial results and are optimistic that the improved performance would continue due to its various initiatives.
- **Key downside risks** are reduced order intake, lower margins and a negative outlook of the building maintenance & estate upgrading industry in Singapore.

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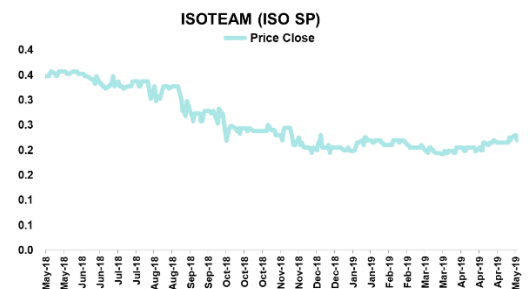


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Share Performance (%)

	YTD	1m	3m	6m	12m
Absolute	10.0	11.1	0.0	(8.3)	(37.1)
Relative	5.0	14.4	0.9	(14.3)	(27.6)
52-wk Price low/high (SGD)					0.18 - 0.36



Source: Bloomberg

Forecasts and Valuations	Jun-17	Jun-18	Jun-19F	Jun-20F	Jun-21F
Total turnover (SGDm)	82.9	83.8	143.4	152.6	160.2
Recurring net profit (SGDm)	6.4	1.9	5.8	6.5	7.1
Recurring net profit growth (%)	(30.1)	(70.7)	207.5	12.0	9.8
Recurring P/E (x)	9.7	33.0	10.7	9.6	8.7
P/BV (x)	1.1	1.0	1.0	0.9	0.8
P/CF (x)	(14.8)	(20.9)	(30.7)	2.9	5.4
Dividend Yield (%)	3.0	0.8	2.0	2.2	2.4
EV/EBITDA (x)	6.2	13.4	8.4	6.8	6.2
ROE (%)	11.7	1.3	8.0	8.1	8.3
Net debt to equity (%)	11.2	24.7	39.6	19.3	14.6
Interest coverage (x)	15.2	1.5	6.8	7.3	7.9

Source: Company data, RHB

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Figure 1: 3Q19 results summary

FYE Jun (SGDm)	3QFY19	3QFY18	YoY +/- %	2QFY19	QoQ +/- %	Remarks
Revenue	30.4	14.7	106.30%	45.9	-33.80%	Revenue contribution from all business segments increased significantly
Gross Profit	4.8	3.2	48.00%	5.3	-9.70%	
Gross Profit Margin	15.70%	21.90%		11.50%		Margin decreased YoY due to lower margin projects
Profit before Tax	1.7	0.3	403.60%	1.7	-0.80%	
Net Profit	1.4	0.2	628.10%	1.3	10.10%	
PATMI	1.7	0.5	251.50%	1.3	29.80%	
PATMI Margin	5.60%	3.30%		2.80%		

Source: Company data, RHB

Figure 2: DCF valuation

	Total (SGDm)	FY19F	FY20F	FY21F	FY22F	Terminal Value
EBIT		7.3	7.9	8.5	9.2	
EBIT(1-T)		5.9	6.3	6.8	7.4	
Capex		(5.0)	(5.0)	(5.0)	(5.0)	
Depreciation & Amortisation		3.4	3.6	3.7	3.9	
Change in Non-cash WC		(12.8)	9.8	(0.6)	(1.6)	
FCFF		(8.5)	14.7	4.9	4.6	95.5
Present Value of FCFF		(8.1)	13.4	4.3	3.8	79.1
Total FCFF	92.4					
Add: Cash	12.2					
Less: Value of Debt	(23.8)					
Target Equity Value	80.8					
No. of shares (basic)	283.6					
Intrinsic Share Price (SGD)	0.29					

Source: Company data, RHB

Figure 3: WACC

<u>Cost of Equity</u>		<u>Cost of Debt</u>	
Expected market return	8.7%	Pre-Tax Cost of Debt	2.9%
Risk free	2.5%	1 - Effective Tax Rate	74%
Beta	0.6	Weight	38%
Weight	62%		
WACC (Estimated)	4.8%		

Source: Company data, RHB

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