

# Swing Media Technology Group Ltd

*Improving gearing position*

RECOM	BUY
PRICE/TARGET PRICE	S\$0.06/S\$0.13
MKT CAPITALISATION	S\$27.5m
BOARD	Mainboard
SECTOR	Technology

SWM SP

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**Blank disc specialist.** Swing Media runs a simple operation. The Group derives most of its sales and profit the manufacture and sale of blank DVD-R discs. Over the years, other business such as computer peripherals and movie-related ventures have been eliminated, resulting in a very focused Company

**Turning cash generative again.** The bulk of the Group's capacity expansion has been completed. For the next three years, we do not expect significant capex needs. This leads us to assume that net gearing position will improve and cash balance will also rise over the next few years.

**A series of well-received fund raising.** The Group managed to raise fund for working capital purpose recently, starting off with a warrant issue in January followed by a convertible bond and a new share placement in recent months. The funds raised will alleviate working capital concerns.

**Initiate with BUY and target price of S\$0.13,** based on the average of its past 6 years average P/BV. Our target price implies upside potential of 133.3%. Given minimal capex needs from the next three years, the Company will have an opportunity to build up its cash and seek other business opportunities to bring the Group into the next chapter of its corporate life.

## Financial summary

FYE Mar	2008	2009	2010F	2011F	2012F
Revenue (HK\$ m)	527.4	634.9	700.2	773.5	857.2
EBITDA (HK\$ m)	140.0	147.3	159.7	167.5	176.1
EBITDA margins (%)	26.6	23.2	22.8	21.7	20.5
Pretax profit (HK\$ m)	46.2	49.3	50.0	55.2	61.2
Net profit (HK\$ m)	37.4	38.2	41.0	45.3	50.1
EPS (HK cts)	9.6	8.3	8.5	8.8	9.7
EPS growth (%)	-11%	-14%	2%	4%	11%
P/E (x)	3.0	3.5	3.5	3.3	3.0
FD EPS (HK cts)	9.6	8.3	4.4	4.9	5.4
FD P/E (x)	3.0	3.5	6.6	6.0	5.5
Gross DPS (HK cts)	1.1	0.5	0.5	0.5	0.5
Dividend yield (%)	3.6	1.8	1.8	1.8	1.8
P/NTA (x)	0.3	0.3	0.3	0.3	0.2
ROE (%)	9.5	8.0	7.8	8.0	8.2
Net gearing (%)	41.5	71.2	47.7	34.4	17.8
P/CF (x)	1.1	1.1	1.1	1.2	1.1
EV/EBITDA (x)	3.6	3.4	3.2	3.0	2.9

Source: Company, CIMB-GK estimates

## Market capitalisation & share price info

Market cap	S\$27.5m	Share price perf. (%)	1M	3M	12M
12-mth price range	S\$0.04/S\$0.09	Relative	0.4	2.3	4.6
3-mth avg daily volume	S\$0.06m	Absolute	-	37.5	(21.4)
# of shares (m)	458.9	Major shareholders	% held		
Est. free float (%)	74	Hui family	32.5		
Writs/ICULS o/s (m)	412.8				
Conv. price (S\$)	0.08				

Source: Company, CIMB-GK Research, Bloomberg

## Background

Swing Media is one of Hong Kong's leading manufacturer and supplier in the data storage and IT industries. Their product lines are: DVD-R, CD-R, stampers, chemical dyes, plastic resins and packing materials.

The group's operations are headquartered in Hong Kong with manufacturing facilities based in Hong Kong and Taiwan. Their products are distributed in the PRC, various parts of Asia, Europe and the United States.

Ordinary shares of Swing Media were listed on the SGX-SESDAQ on 1 February 2002 and, the Company was upgraded to the Main Board on 8 March 2004.

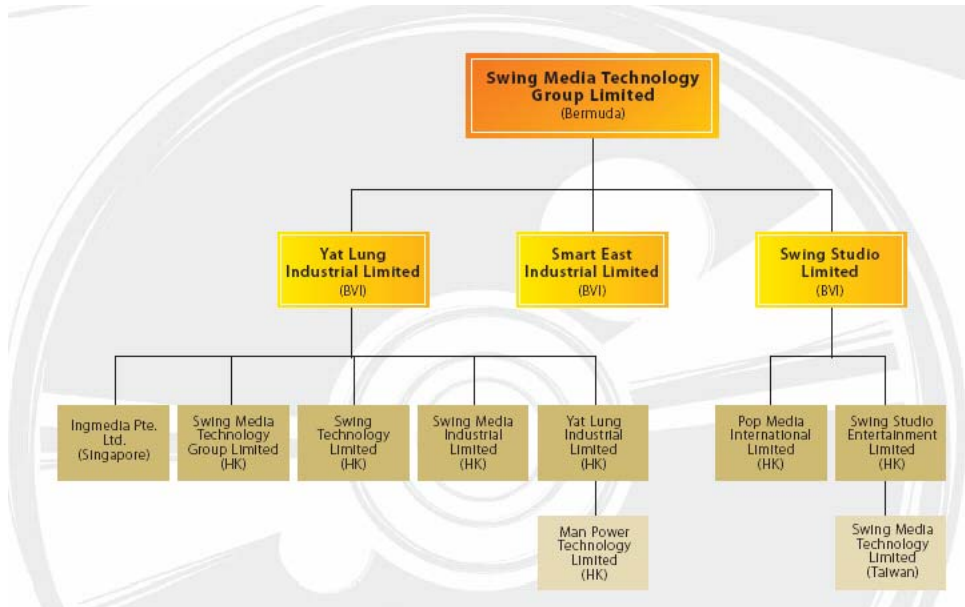
### Products and Services

**Optical discs.** Production of blank DVD-R is the core business of the Group. These are produced in their high-tech factory in Taiwan as well as Hong Kong.

**Plastic resins, chemical dyes and packing material.** The Group also trades plastic resins, stampers, chemical dyes and packing materials to support their production of DVD-R as well as sell these chemicals and materials to third parties. As CD-R is a matured technology and is being gradually replaced by DVD-R, Swing Media does not manufacture CD-R any more. Its CD-R requirements are purchased from external suppliers.

The Group sells its products to importers with the top 5 customers accounting for an estimated 40% of sales.

Figure 1: Group structure



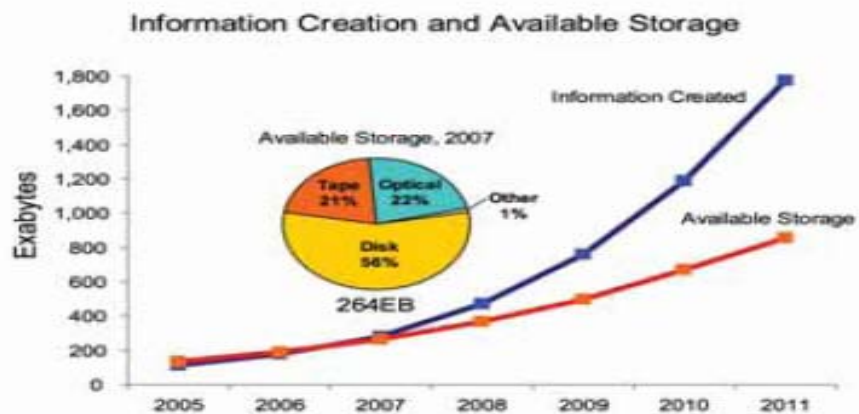
Source: Company, as at 31 March 2008

## Industry outlook

**Storage.** According to IDC, the development of storage media and the generation of content are part of a virtuous cycle, whereby increased storage capacity, encourages data storage of content, which in turn generates more content, and so on (Figure 2). Three of the main reasons for growth of media storage are, 1) the protection of personal information, 2) the ease of mobility and portability of information and 3) trickle down effects resulting from the mobility of storage; mobile storage and devices with local storage, subsequently require access to networked storage.

Optical media is one of the 3 mediums of data storage. Optical media has the benefit of mobility, the presence of no movable parts), and reasonable cost per mega byte of storage. As the demand for storage space increases, we expect the demand for optical discs to grow. This growth will be distributed unevenly across the technological spectrum, with older technologies being displaced by newer advancements; a decline in the demand of CDs, steady demand for DVDs and increasing demand for Blu-ray discs.

Figure 2: Information Creation and Available Storage



Source: IDC, 2008

**Media and Entertainment.** The media and entertainment sector is traditionally immune to economic downturns. With less income and more uncertainty, consumers are likely to cut back on discretionary spending, in favour of cheaper alternatives like home entertainment. Thus, the demand for CDs and DVDs required to store such material will not be affected significantly.

## Company outlook

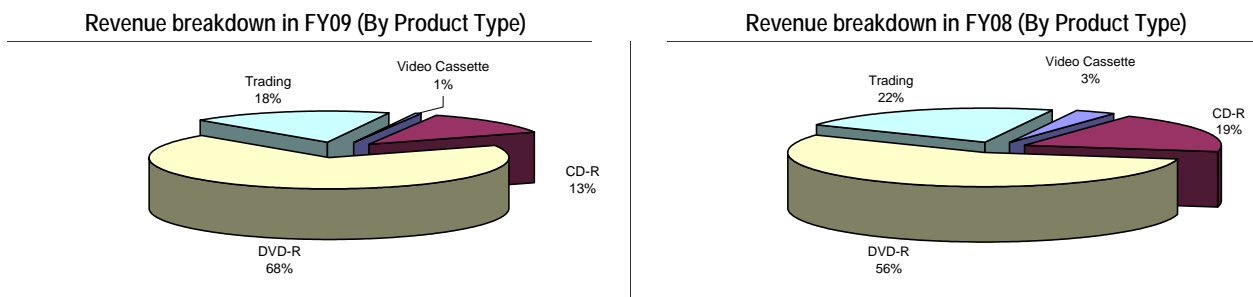
**Still strong.** The economic downturn has led to a consolidation phase in the industry as smaller and weaker players are weeded out. Despite the economic downturn, sales grew 20% yoy. More importantly, revenue and gross profit growth was strongest in China, the biggest geographic segment. Sales revenue in China was up 90% yoy to HK\$389m (FY09) compared to HK\$205m (FY08) while profit before tax rose 60%yoy at HK\$30m (FY09) against HK\$18m (FY08). Its diversified customer base has also been instrumental in helping the Group weather the downturn.

The group has successfully completed several capital raising measures, to improve its working capital and reduce interest costs.

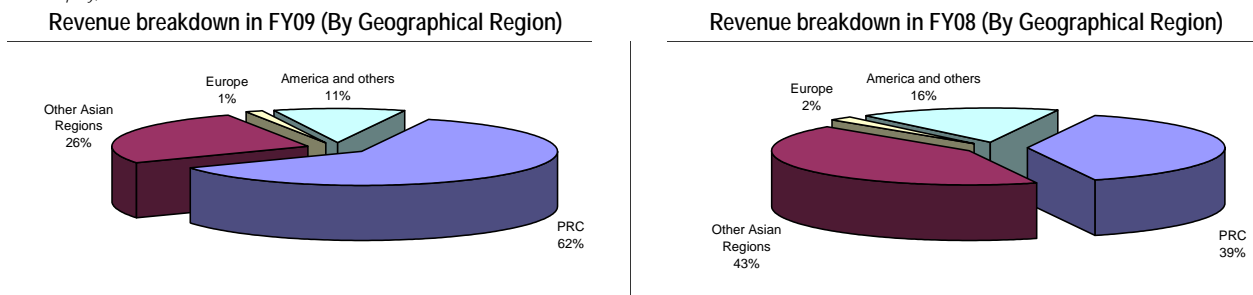
**Demand for DVD-R remains strong.** The Group has received an increase in the number of orders for DVD-R and has upgraded production lines to increase DVD-R production.

Swing Media has completed the bulk of its capacity expansion and given the global economic conditions, the Group will not have any aggressive capex plans for the next few years.

Figure 3: Breakdown



Source: Company, CIMB-GK Research



Source: Company, CIMB-GK Research

Figure 4: SWOT analysis

### Strengths

- Economies of scale.
- Plants are efficient and technologically up to date.
- Experienced management

### Opportunities

- As the industry has matured, there could be acquisition opportunities of smaller players who lack the scale to continue to be competitive in this business
- Dual layer disc could grow in popularity as more content can be compressed into a single disc.

### Weaknesses

- Nature of product offers little differentiation from competitors.
- Dependence on a single product segment.

### Threats

- Rising cost of raw materials, primarily plastic resins.
- Technological improvements in substitute products (Hard disk drives, Solid state drives, "cloud" computing and video streaming).
- Market is highly competitive.
- Proliferation of Internet

Source: Company, CIMB-GK Research

## Risks

**The Group is subject to keen competition** from other manufacturer of similar products in both local and foreign markets, due to the lack of barriers to entry. The products are not significantly differentiated. In the absence of significant technical differences and branding, rivals compete with the Group on manufacturing competency, reliability, quality of products and services, pricing, time-to-market and available production capacity.

**Rapid technological changes.** Optical media has traditionally straddled a middle ground between hard disk drives; which were cheaper per megabyte, but with less portability, due to the presence of moveable parts, and solid state media (e.g. flash drives); which were more durable, but more expensive. Thus improvements in either hard disk drives or solid state media would pose a threat to the optical media industry.

High speed access to the internet may pose a threat to physical data storage, in the form of video streaming or "cloud computing", where data is remotely stored and services distributed via web transfers. In video streaming, videos are streamed via high speed broadband networks to the screening devices (e.g. TVs, phones, etc.), bypassing the need for a physical medium to distribute the product. In cloud computing, users pay providers for the services used, bypassing the need to maintain the infrastructure and physical storage of data. As high speed internet, both wired and wireless, becomes more prevalent, physical storage of data will be less relevant. At present, video streaming poses a bigger threat to the optical media industry as cloud computing has not taken off due to technical and economic reasons.

The data storage industry is characterized by the rapidly-changing technology and the frequent emergences of new products. The release of new products, resulting in pricing pressure of older products means the Group has to be guarded against the obsolescence of their products and manage their inventory carefully.

**Rising costs of raw materials.** The main raw materials involved in the manufacturing operations are plastic resins and chemical dye. Plastic resin, a by-product of oil, is subject to the fluctuations of crude. Although the price of crude is significantly lower than its highs of 2008, the price of crude is up approximately 60% for the start of the year at US\$71. This may translate into higher production costs for the Group.

**Foreign exchange transaction and translation risks.** The Group transacts with its suppliers and customers mainly in US\$ and partly in HKD and RMB. This exposes the Group to rapid fluctuations in the exchange rates of the HKD against the US\$ and the RMB.

## Financials

Despite the economic slowdown, profit before tax rose 6.7% yoy, from HK\$46.2m (FY08) to HK\$49.3m (FY09), as sales were up 20% yoy from HK\$527.4m (FY08) to HK\$634.9m (FY09). This is attributed to the global downturn leading to consumers cutting down on more expensive recreational activities, leading to a rise in the consumption of home entertainment products. The key beneficiary being DVDs.

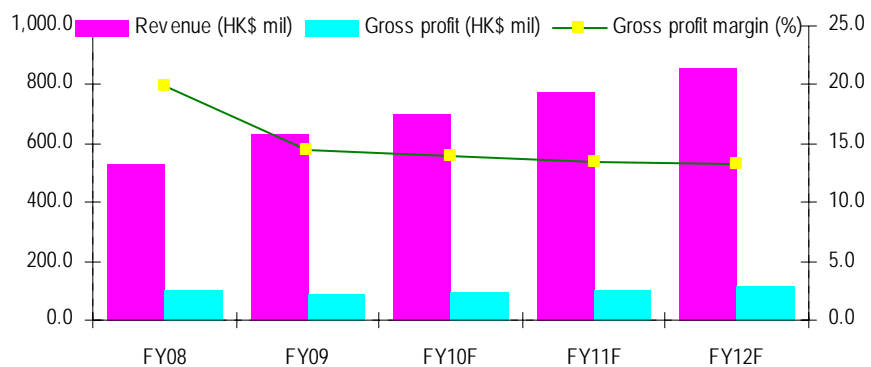
ROE has maintained fairly stable over the last 3 years, hovering around 10%. Cash flow per share has improved yoy to HK\$0.19 per share, but free cash flow remains negative, at –HK\$0.17 per share. Net gearing has increased from 0.42 in FY08 to 0.71 in FY09. The Group has invested heavily in new technology for dual-layer DVDs and expansion of their Taiwan factory to meet increased demand. Cash cycle days have doubled to 215, as most of the new orders received is on month end 90 days terms. However, credit risk is manageable as the largest single customer accounts for only an estimated 8% of the receivables. Due to the back-end loaded nature of orders for FY09, receivable days spiked upwards. Going forward, we expect the situation to normalise and receivables days to decrease, leading to an improvement in working capital.

Although FCF is negative, the current and quick ratios are 1.93 and 1.45 respectively, implying that the company has sufficient cash to cover their immediate and short term liabilities. The Group declared a first and final dividend of 0.10 Scts, payable in cash or script. Going forward, we expect minimal capex plans to lead to a gradual improvement in net gearing.

Sales grew a strong 20% in FY09 as DVD-R sales jumped 48.7% to HK\$436.6m, more than compensating the sales decline in other businesses. Demand for DVD-R grew rapidly in the last quarter of 2008 as more people opted to stay indoors rather than spend money on outdoor entertainment. Home entertainment, in particular movies resulted in a sharp demand for DVD-R products. Given the high storage capacity and better quality of DVD-R, CD-R and video cassettes sales has been gradually declining.

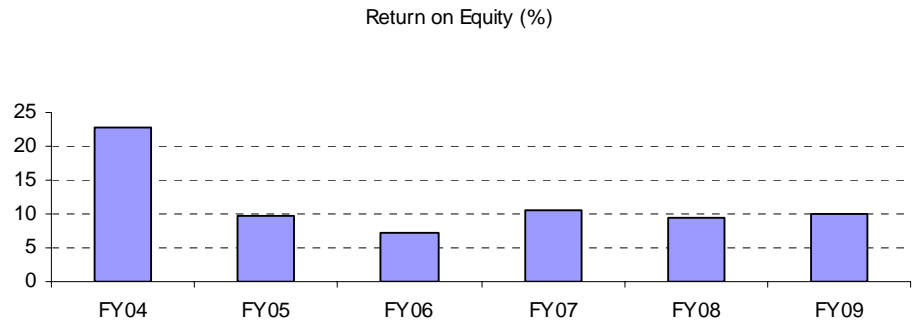
Gross profit margin fell as cost of sales rose due to higher depreciation charges as a result of previous capacity expansion. Going forward, we believe the Company can generate a sustainable sales growth rate of 10% pa. This derives from the fact that the industry has matured with relatively few large scale players still focused solely on blank DVD-R production. Taiwanese competitors such as CMC Magnetics and others have ventured into OLED, solar or other ventures. Due to the commodity nature of the business, we have assumed that gross profit margins will erode gradually over the next three years.

Figure 5: Revenue, profit and gross margin forecasts



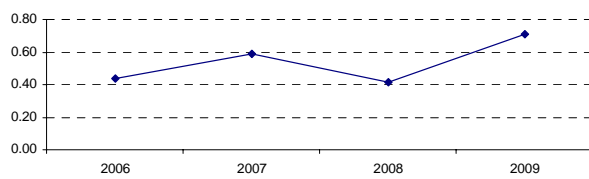
Source: CIMB-GK Research, Company

Figure 6: Return on Equity (%)



Source: CIMB-GK Research, Company

Net Gearing



Cash Cycle Days

	FY06	FY07	FY08	FY09
Accounts Receivable Days	63	65	78	155
Accounts Payable Days	3	2	2	3
Inventory Days	20	18	31	63
<b>Cash Cycle (Days)</b>	<b>80</b>	<b>82</b>	<b>107</b>	<b>215</b>

Source: Company, CIMB-GK Research

In FY09, receivable days spiked up to 155 days. This was due to strong demand in the last quarter as customers switched tightened their budgets and shifted to 'cheaper' form of entertainment such as watching DVDs at home, leading to an increase in demand for discs. The group has been gradually collecting the receivables post balance sheet date.

Figure 7: Capital Raising Exercises

Date	Issue undertaken
27-Sep-08	1 for 1 Renouceable Warrants issue at S\$0.01 each Exercise Price S\$0.08 - 1 Share for 1 Warrant, exercisable within 5 years of issue Up to 470m Warrants offered (412.82m subscribed)
28-Apr-09	18% unsecured convertible bonds on aggregate amount of S\$3.1m Maturing 3 years from issue (Interest is accrued daily, payable semi-annually) Redeemable by Company and bondholders after the 1st year Bonds may be converted to stock in lots of S\$10,000, at a conversion price of S\$0.06 (as of 27 Apr, subject to adjustments)
9-Jun-09	Placement of 30m new shares at S\$0.06 each

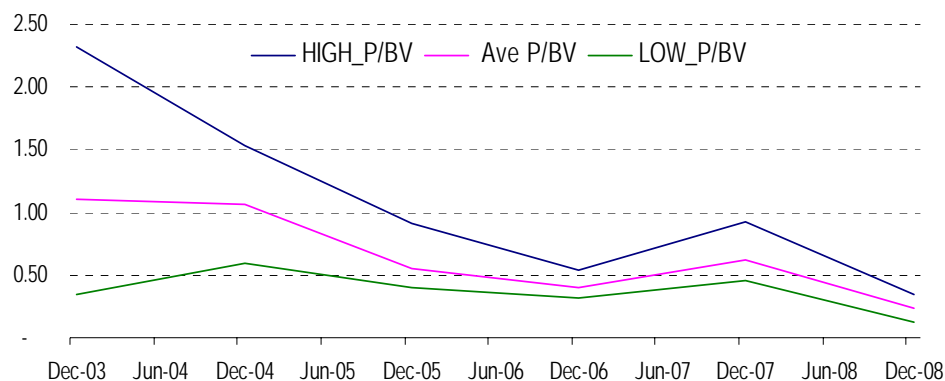
Source: CIMB-GK Research, Company

## Valuation and recommendation

**Initiate with BUY and target price of S\$0.13** This is based on the average of Swing Media's 6 years average P/BV of 0.66x applied to CY09 book value per share of S\$0.20. This translates into an implied CY10 P/E of 8.1x, above the average of its 6 years average P/E but still below the average of the 6 years high P/E.

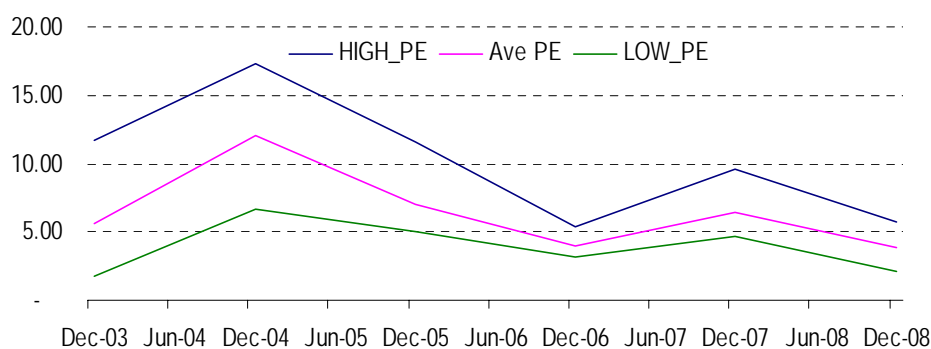
The average 0.66x P/BV parameter that we are using is also in line with the historical average P/BV that its closest competitors are trading at.

Figure 8: Historical P/BV range



Source: CIMB-GK Research, Company

Figure 9: Historical P/E range



Source: CIMB-GK Research, Company

Figure 10: Historical peer comparison

	Bloomberg	CY08 Sales		Core	P/BV	ROE	Div	
	ticker	Mkt cap	S\$m	P/E (x)	(x)	(%)	yield (%)	
		(US\$ m)	(Local)	CY2008	CY2008	CY2008	CY2008	
Swing Media	SWM SP	18.9	98.7	3.6	0.4	9.5	3.1	
DATAPULSE TECH	DT SP	75.6	73.3	6.8	1.4	17.5	16.2	
EASTGATE TECH	EAST SP	10.9	28.1	Loss	1.1	Loss	-	
INTL PRESS SOFTC	IPS SP	22.6	137.0	30.0	0.5	1.7	3.3	
CMC MAGNETICS	2323 TT	630.7	814.3	Loss	0.5	Loss	-	
PRODISC TECH	2396 T	19.0	164.7	Loss	0.1	Loss	-	
RITEK CORP	2349 TT	582.1	578.8	Loss	0.6	Loss	-	
				Simple average	13.5	0.6	9.5	7.6
				Simple average excluding Swing Media	18.4	0.7	9.6	9.8

Source: CIMB-GK Research, Bloomberg



## **Management**

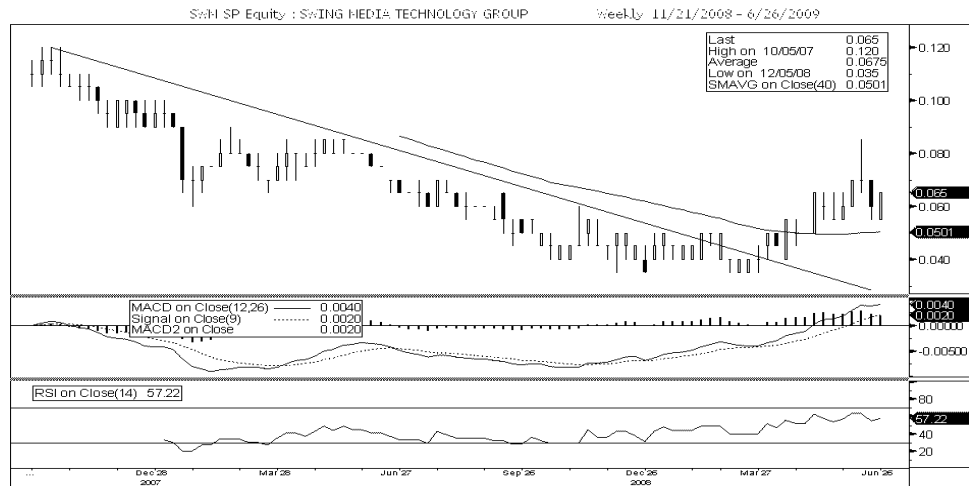
**Mr Hui Yan Sui William** is the Chairman of the Group. He founded the group's core manufacturing business in 1986 and has 22 years of experience in the data storage industry. Mr Hui is active in the marketing aspects of the business and is instrumental in securing most of the customers for the Group. He has been and will continue to be responsible for charting the strategic growth and direction of the business. Prior to establishing Yat Lung Industrial Limited in 1986, he worked as a marketing officer in Beautiful Star Magnetic Limited from 1984 to 1986. Mr Hui is currently an executive committee member (youth group) of Eastern District Industrialists Association, a committee member of the Hong Kong Fujian Charitable Education Fund Limited and the honorary chairman of the Hong Kong Basketball Association.

**Mr Hui Yan Moon** was appointed as the Chief Executive Officer ("CEO") of the Group on 19 May 2003. His responsibilities include overseeing operations, finance and administrative functions and marketing activities of the Group. He joined the Group in 1995 after graduation and over the years, Mr Hui set up the Group's finance and administrative operations. He was also responsible for setting up the group's manufacturing facility in Hong Kong. He holds a Bachelor degree (first class honours) in Business Administration from Baruch College, City University of New York in 1995 and was awarded a scholarship by the New York State Society of Certified Public Accountants. Mr Hui has also obtained the Executive Master degree of Business Administration from Tsinghua University, China in 2007.

**Mr Chan Hon Chung Johnny** was appointed as Executive Director on 1 September 2004. Mr Chan is also the Chief Financial Officer and Joint Company Secretary of our Group since 19th May 2003. Mr Chan is responsible for the financial and administrative matters as well as the secretarial work of the Group. Mr Chan joined the Group in January 2003. Before joining the Group, Mr Chan has been working in banking industry for 14 years including international and local banks like ABN AMRO Bank, Standard Chartered Bank and The Bank of East Asia. Mr Chan holds a Bachelor of Science degree in Finance from Brigham Young University, USA and a Master degree in Professional Accounting from the Hong Kong Polytechnic University.

*Source: Company*

## Technical view



- Technical **BUY**.
- The stock has been rising steadily since breaking out above its long term resistance trend line in April. The long-legged doji 3 weeks ago suggests that a temporary top is in place.
- Both indicators have stayed positive, suggesting that this run still has legs but probably after a minor correction. The RSI has yet to reach overbought levels, further supporting the positive view.
- Hence, investors would be better off buying on weakness. Support is seen at S\$0.055-0.06 while resistance is at S\$0.08-0.09.

## Financial tables

<b>PROFIT &amp; LOSS (HK\$ m, FYE Mar)</b>	<b>2008</b>	<b>2009</b>	<b>2010F</b>	<b>2011F</b>	<b>2012F</b>
Revenue	527.4	634.9	700.2	773.5	857.2
Operating expenses	(387.4)	(487.5)	(540.5)	(606.0)	(681.2)
EBITDA	140.0	147.3	159.7	167.5	176.1
Depreciation & amortisation	(67.5)	(79.8)	(83.3)	(86.3)	(89.3)
EBIT	72.5	67.6	76.4	81.2	86.7
Net interest & invt income	(26.3)	(18.2)	(26.4)	(26.0)	(25.6)
Associates' contribution	-	-	-	-	-
Exceptional items	-	-	-	-	-
<b>Pretax profit</b>	<b>46.2</b>	<b>49.3</b>	<b>50.0</b>	<b>55.2</b>	<b>61.2</b>
Tax	(9.0)	(11.2)	(9.0)	(9.9)	(11.0)
Minority interests	0.2	0.0	-	-	-
<b>Net profit</b>	<b>37.4</b>	<b>38.2</b>	<b>41.0</b>	<b>45.3</b>	<b>50.1</b>
Wt. shares (m)	387.6	458.9	483.9	515.1	515.1
Shares at year-end (m)	458.9	458.9	515.1	515.1	515.1

<b>BALANCE SHEET (HK\$ m, FYE Mar)</b>	<b>2008</b>	<b>2009</b>	<b>2010F</b>	<b>2011F</b>	<b>2012F</b>
Fixed assets	475.3	497.9	444.6	388.3	299.0
Intangible assets	-	-	-	-	-
Other long-term assets	-	-	5.0	0.6	-
<b>Total non-current assets</b>	<b>475.3</b>	<b>497.9</b>	<b>449.6</b>	<b>388.9</b>	<b>299.0</b>
Cash and equivalents	106.3	46.0	156.5	214.7	303.9
Stocks	46.7	94.5	84.4	93.8	104.2
Trade debtors	135.4	269.7	273.1	301.7	334.3
Other current assets	34.5	62.2	63.0	73.5	85.7
<b>Total current assets</b>	<b>322.9</b>	<b>472.4</b>	<b>577.1</b>	<b>683.6</b>	<b>828.1</b>
Trade creditors	3.2	5.4	5.6	6.2	6.9
Short-term borrowings	153.3	247.4	247.4	247.4	247.4
Other current liabilities	10.7	31.9	21.0	19.8	21.9
<b>Total current liabilities</b>	<b>167.3</b>	<b>284.7</b>	<b>274.0</b>	<b>273.4</b>	<b>276.2</b>
Long-term borrowings	140.4	154.0	170.0	170.0	170.0
Other long-term liabilities	39.3	32.5	35.8	39.6	43.9
<b>Total long-term liabilities</b>	<b>179.7</b>	<b>186.5</b>	<b>205.8</b>	<b>209.6</b>	<b>213.9</b>
<b>Shareholders' funds</b>	<b>451.0</b>	<b>499.2</b>	<b>546.9</b>	<b>589.6</b>	<b>637.1</b>
Minority interests	0.2	0.0	-	-	-
NTA/share (HK\$)	0.98	1.09	1.06	1.14	1.24

<b>CASH FLOW (HK\$ m, FYE Mar)</b>	<b>2008</b>	<b>2009</b>	<b>2010F</b>	<b>2011F</b>	<b>2012F</b>
Pretax profit	46.2	49.3	50.0	55.2	61.2
Depreciation & non-cash adjustments	94.7	101.4	109.7	107.9	129.7
Working capital changes	(41.5)	(203.6)	5.8	(46.8)	(53.5)
Cash tax paid	(0.3)	1.1	(11.2)	(9.0)	(9.9)
Others	(26.3)	(18.2)	(26.4)	(26.0)	(25.6)
<b>Cash flow from operations</b>	<b>72.8</b>	<b>(70.0)</b>	<b>127.9</b>	<b>81.3</b>	<b>101.9</b>
Capex	(136.9)	(107.6)	(30.0)	(30.0)	(30.0)
Net investments & sale of FA	-	-	-	-	-
Others	-	-	(5.0)	4.4	10.0
<b>Cash flow from investing</b>	<b>(136.9)</b>	<b>(107.6)</b>	<b>(35.0)</b>	<b>(25.6)</b>	<b>(20.0)</b>
Debt raised/(repaid)	(7.1)	100.9	16.0	(0.0)	-
Equity raised/(repaid)	79.7	19.3	9.3	-	-
Dividends paid	(4.3)	(5.2)	(2.6)	(2.6)	(2.6)
Cash interest & others	-	-	(5.0)	5.0	10.0
<b>Cash flow from financing</b>	<b>68.2</b>	<b>114.9</b>	<b>17.7</b>	<b>2.4</b>	<b>7.4</b>
<b>Change in cash</b>	<b>4.1</b>	<b>(62.7)</b>	<b>110.6</b>	<b>58.1</b>	<b>89.3</b>
<b>Change in net cash/(debt)</b>	<b>11.3</b>	<b>(163.6)</b>	<b>94.6</b>	<b>58.1</b>	<b>89.3</b>
Translation & others	-	(4.5)	-	-	-
<b>Ending net cash/(debt)</b>	<b>(187.3)</b>	<b>(355.4)</b>	<b>(260.8)</b>	<b>(202.7)</b>	<b>(113.4)</b>

<b>KEY RATIOS (FYE Mar)</b>	<b>2008</b>	<b>2009</b>	<b>2010F</b>	<b>2011F</b>	<b>2012F</b>
Revenue growth (%)	17.1	20.4	10.3	10.5	10.8
EBITDA growth (%)	29.4	5.2	8.4	4.9	5.1
Pretax margins (%)	8.8	7.8	7.1	7.1	7.1
Net profit margins (%)	7.1	6.0	5.9	5.9	5.8
Interest cover (x)	2.7	3.7	2.9	3.0	3.3
Effective tax rates (%)	19.4	22.7	18.0	18.0	18.0
Net dividend payout (%)	14.0	6.9	6.3	5.7	5.2
Ave Debtors turnover (days)	86	116	141	136	135
Ave Stock turnover (days)	32	41	47	42	42
Ave Creditors turnover (days)	2	2	3	3	3

Source: CIMB-GK Research

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**HOLD:** The stock's total return is expected to range between +15% and -15% over the next three months.

**SELL:** The stock's total return is expected to be -15% or worse over the next three months.

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**NEUTRAL:** The industry, as defined by the analyst's coverage universe, has either (i) an equal number of stocks that are expected to have total returns of +15% (or better) or -15% (or worse), or (ii) stocks that are predominantly expected to have total returns that will range from +15% to -15%; both over the next three months.

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