

CHINA
DEVELOPMENT
FINANCIAL

DISA

(DISA SP/532.SI)

Growth plans on track with more retailers expected to come aboard

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- 4Q18 net losses declined to S\$2.6mn from S\$3.9mn in 4Q17 as technology business continues to pick up speed.
- Growth in 3S codes has exceeded expectations while PoSA codes continue to exhibit strong growth.
- We re-iterate our BUY recommendation and maintain our fair value of S\$0.02 based on DCF valuation.

Financials & Key Operating Statistics

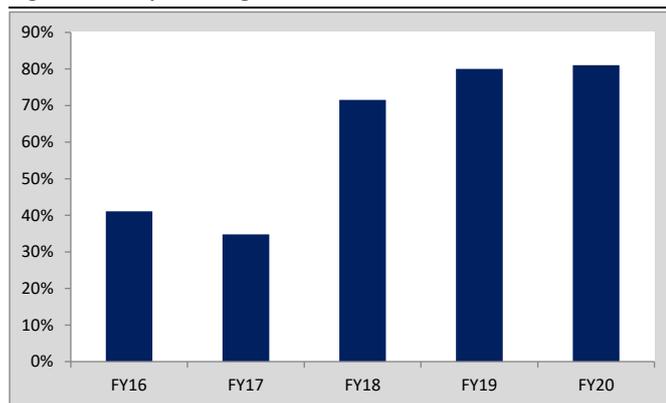
YE Jun SGD (mn)	2018A	2019F	2020F	2021F	2022F
Revenue	0.2	5.9	11.6	23.2	46.3
Operating Profit/Loss	(9.7)	(6.2)	(2.4)	6.1	23.9
Net income	(10.6)	(7.3)	(3.5)	4.2	18.9
EPS (SGD Cents)	(0.3)	(0.1)	(0.1)	(0.0)	0.0
EPS growth (%)	-	-	-	-	3.5
P/E (x)	-	-	-	-	19.3
P/B (x)	2.2	2.7	3.1	2.6	1.6
P/S (x)	336.0	13.6	6.9	3.5	1.7
EV/EBITDA (x)	-	-	-	-	7.9
Debt / Equity	44.5%	34.3%	42.6%	48.3%	41.7%
Net Margin (%)	-	-	-	18.0	40.8
ROE (%)	-	-	-	14.7	47.3

Source: Company Data, KGI Research

Technology Business continues to exhibit strong growth.

Sale of Digital Safety (DiSa) codes rose 87.8% YoY to S\$169,000 in FY18, becoming the main driver of revenue. Revenue contributions from the tech business are now 71% of total revenue compared to 28% in FY17. As a result, gross margins rose to 72% in FY18 as compared to 35% in FY17 and we expect further margins expansion as momentum in the tech business picks up.

Figure 1: Gross profit margins



Source: Company data, KGI Research

3S growth exceeds expectations with more retailers expected to come on-board.

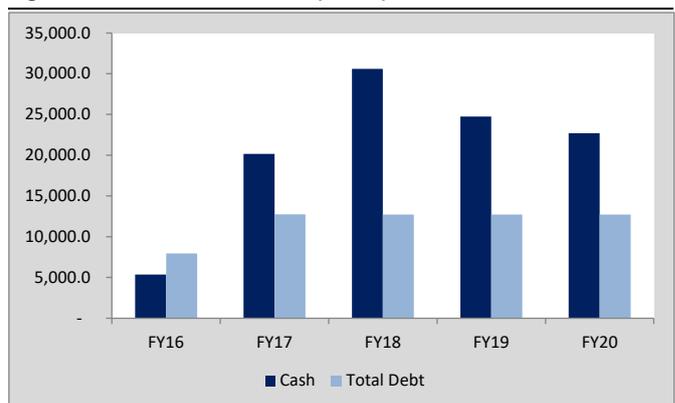
We understand from management that while PoSA code sales continue to gain momentum, sales from 3S (Single Scan Serialisation) has exceeded expectations. As of 26 August 2018, the company has sold more than 4.5 million of codes and going forward, we expect the momentum to continue given that the company is now expecting 2 of the top US retailers to begin implementing proof-of-concept trials in their US stores.

BUY - Maintain

Price as of 30 Aug 18 (SGD)	0.01	Performance (Absolute)	
12M TP (\$)	0.02	1 Month (%)	0.0
Previous TP (\$)	0.02	3 Month (%)	-11.1
Upside (%)	198.4	12 Month (%)	-46.2
Trading data		Perf. vs STI INDEX (Red)	
Mkt Cap (\$mn)	70		
Issued Shares (mn)	10,039		
Vol - 3M Daily avg (mn)	12.8		
Val - 3M Daily avg (\$mn)	0.1		
Free Float (%)	65.9%		
Major Shareholders		Previous Recommendations	
Wang Yu Huei	9.7%	21-Jun-18	BUY \$0.02
Tang Wee Loke	7.0%		
Chng Weng Wah	5.9%		

Operating margins remain weak even as net cash position improves. Operating losses declined 43.8% YoY to S\$9.68mn driven by one-time items, an increase in operating lease and employee benefit expenses as business picks up in the United States. In our view, operating expenses will continue to be a drag on earnings prior to the completion of proof-of-concept trials with other US retailers.

Figure 2: Total Cash Vs Total Debt (\$'000)



Source: Company data, KGI Research

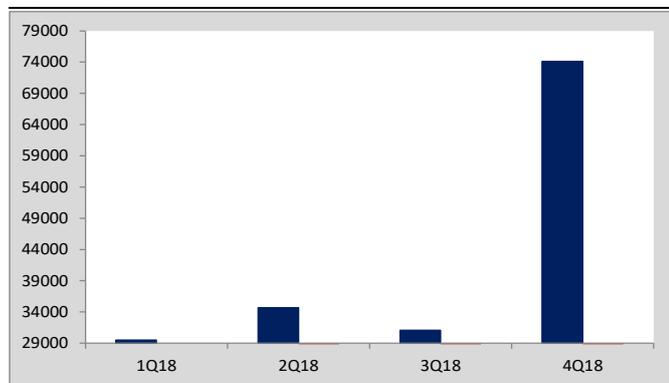
Valuation & Action: We maintain our BUY recommendation with an unchanged TP of \$0.02 after accounting for changes to FCF and increased shares outstanding. Our target price implies a 19.3x 2021F EPS and is based on a DCF model assuming 14.4% WACC and terminal growth rate at 0%.

Risks: Slow user adoption and a breach in DISA's encryption could lead to reputational damages and a decline in revenue. Going concern could become a problem if DISA fails to scale and cover its burn rate.

Results Update - Execution Risks Remain

We believe the latest quarterly earnings are an indication that adoption of the technology is picking up and more suppliers are coming on board as sales of DISA's codes rose 138.5% QoQ to S\$74,112.

Figure 3: Quarterly sales of codes sold



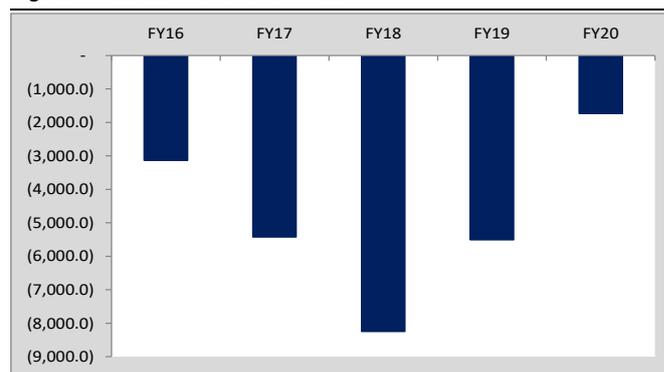
Source: Company data, KGI Research

While momentum has been encouraging, we reiterate that cash burn and execution risks remain high, especially if the company does not get another 2 large US retailers to come on board.

Currently, the firm burns cash at S\$6m to S\$8m a year and has a convertible bond maturing at the end of 2018 but given its strong cash levels, we do not expect the company to run into liquidity issues in the next 1 to 2 years.

Growth of its tech business however, has to remain strong as its cash burn has not improved. Negative free cash flows worsened to S\$8.25mn from S\$5.43mn in FY17.

Figure 4: Free cash flows remain weak



Source: Company data, KGI Research

Figure 5: Quarterly Results

SGD (S\$'000)	4Q17	4Q18	4Q YoY (%)	Comments
Revenue	146	235		
Sale of Codes	46	74	60.9	Code sales driven by more suppliers, as well as faster than expected growth in 3S segment
Gross Profit	130	227		
Gross Margin (%)	89.0	96.6	7.6	Margin Expansion driven by change in product mix as Digital Safety codes becomes main revenue driver
Depreciation and Amortization Expenses	(378)	(411)		
Employee Benefits Expenses	(1,194)	(1,190)		
Legal & Professional Expenses	(128)	(198)		
Operating Lease Expense	(84.0)	(230.0)		
Other Expense	(415.0)	(545.0)		
Operating Profit/Loss	(3,905)	(2,383)	-39.0	
Operating Margin(%)				
Net Profit	(3,964)	(2,616)		

Source: Company data, KGI Research

Figure 6: DCF Valuation

DCF	2018A	2019F	2020F	2021F	2022F	2023F	2024F	2025F
Revenues	169.0	5,850.3	11,605.8	23,162.2	46,298.5	55,552.0	66,659.2	79,989.4
Services Rendered	64.1	33.5	17.5	9.1	4.8	2.5	1.3	0.7
Net revenue	233.1	5,883.7	11,623.3	23,171.3	46,303.3	55,554.5	66,660.5	79,990.1
YoY growth (%)	-	2424.3%	97.5%	99.4%	99.8%	20.0%	20.0%	20.0%
Cost and Operating Expense	(9,917.0)	(12,073.4)	(14,021.4)	(17,039.6)	(22,418.6)	(25,481.8)	(29,088.7)	(33,337.2)
EBIT	(9,683.9)	(6,189.6)	(2,398.1)	6,131.7	23,884.7	30,072.8	37,571.8	46,652.8
FCFF	(6,889.9)	(4,412.6)	(621.1)	7,056.5	21,792.2	26,928.6	33,153.0	40,690.3
YoY growth (%)	-	-	-	-	208.8%	23.6%	23.1%	22.7%
Terminal value								
Implied enterprise value		191,837.1						
Add: Cash		30,594.0						
Less: Debt		12,715.0						
Less: Preferred stock								
Less: Minority interest		-						
Implied equity value		209,716.1						
Diluted Shares Outstanding		10,038,683.4						
Implied target price (S\$)		0.02						
Upside (%)		198%						

Source: Company data, KGI Research

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Rating	Definition
	KGI Securities Research's recommendations are based on an Absolute Return rating system.
BUY	>10% total return over the next 12 months
HOLD	-10% to +10% total return over the next 12 months
SELL	<-10% total return over the next 12 months

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