



**REDtone International Berhad (REDtone)– Turning “RED” to “BLACK”**

**Recommendation: BUY**

**Share Price: RM0.395**

**FINANCIAL SUMMARY**

FYE 31 May (RM mil)	2011	2012	2013F	2014F
Revenue	90	107	160	187
EBITDA	(2.6)	6.5	30.8	33.0
EBITDA Margin (%)	(2.9)	6.1	19.2	17.7
Pre-tax Profit	(11.0)	3.2	25.9	29.2
Net Profit	(11.7)	2.2	23.3	26.0
EPS (sen)	(2.6)	0.5	5.2	6.0
DPS (sen)	-	-	1.3	1.5
PER (x)	(15.6)	53.3	7.5	6.5
Dividend Yield (%)	-	-	3.3	3.8

**OTHER KEY DATA**

Listing	ACE Market
Issued Cap. (mil, RM0.10 par)	477
Market Cap. (RM mil)	188
52 Week Low/High (RM)	0.45/ 0.23
Net Gearing (%)	-0.2
ROE (%)	11.0
P/BV (x)	2.2
BV/share (RM)	0.2

**Major Shareholders**

	(%)
Indah Pusaka Sdn Bhd	32.8
Berjaya Group Berhad	10.4
Warisan Jutamas Sdn Bhd	7.9

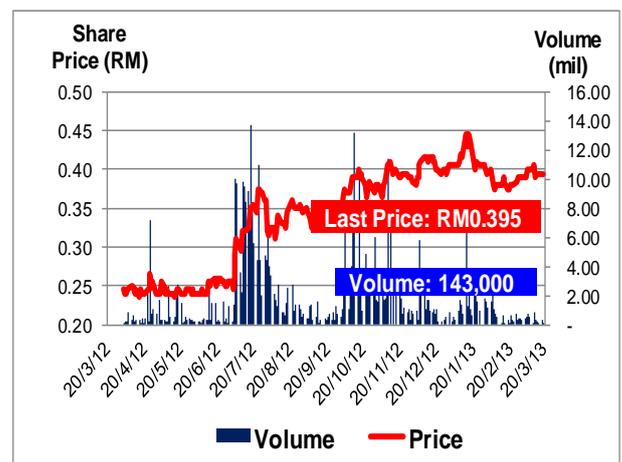
Source: Company, Bloomberg & PCM estimates

Our **BUY** call for REDtone is buoyed by its:

1. Divestiture of its non-core and loss-making businesses
2. Leasing its bandwidth spectrum to Maxis in rolling out the 4G LTE Network
3. Optimistic on getting more government projects
4. Plans to reward its shareholder with minimum 25% dividend payout

REDtone has repositioned itself by weeding out the “dogs” and revamp its focus strategy to data and broadband services, which we believe would be the “cash cow” going forward.

**Price Chart of REDtone (1 Year)**



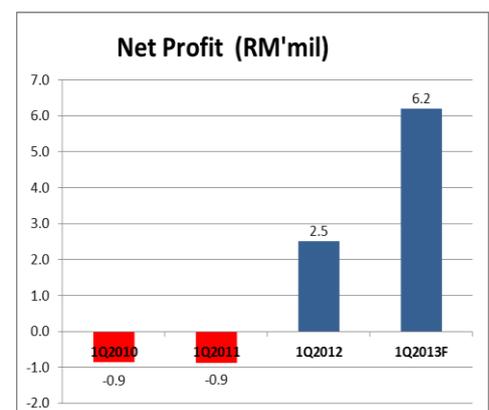
Source: Bloomberg

**Highlights:**

**Background –** REDtone is an ACE Market-listed business telecommunication solutions provider. REDtone has expanded vertically into various related businesses such as VoIP services, WiMAX broadband internet service and mobile virtual network. Over the past few years, REDtone was making losses due to changes in the industry landscape and intense competition. But now REDtone has succeeded in turning around its performance to record its first profitable year since 2008.

**Deconsolidation turned REDtone around –** REDtone recorded a net profit of RM2.5m in 1QFY2012 compared to RM8.7m losses for the same quarter in the preceding year. Its return to profitability was mainly due to improve in operational costs from the deconsolidation of its stakes in three non-core businesses, which are REDtone Multimedia Sdn Bhd, REDtone Software Sdn Bhd and REDtone Mobile Sdn Bhd. With these divestments, we believe REDtone’s earnings moving forward will no longer be overwhelmed by these loss-making businesses. In fact, other divisions of the group are also started to show marked improvement in contributions.

REDtone also removed its hyper-competitive Internet protocol TV from the business and focus on data and broadband services. It will



focus on data and broadband business where contribution from this business segment has been growing steadily from RM3m in FY2009 to RM25m in FY2012. However, its voice business will continue to contribute especially in China, which focuses on the prepaid and reload services with 650k customers as at FY2012. Going forward, REDtone is planning to expand its e-reload platform to cater for China's middle-to-lower income segment prepaid customers' needs.

**Gears on Maxis –** REDtone has signed a 10-year infrastructure and spectrum sharing agreement (NSA) with Maxis Bhd on its 2,600 Mhz spectrum. The agreement allows Maxis to have an optimal capacity on its 4G LTE network. The “assignment” of its spectrum to Maxis also allows REDtone to save about RM390m if they were to roll out its own network. Maxis is paying up-front commitment fee of RM25m which is likely to be recognized by REDtone in the 4QFY2013 or even 1QFY2014. It is also expected to receive 10 years of recurring income payable quarterly based on a scale rate with minimum yearly commitment. According to our sources, on top of the projected RM295m recurring income (about RM29.5m per annum) to be received by REDtone, Maxis will also pay RM1.50 per month for every subscriber to REDtone for the first 2.5m 4G LTE subscribers based on agreed tier pricing structure. Maxis is eyeing 4m - 8m 4G subscribers over the next 5 years.

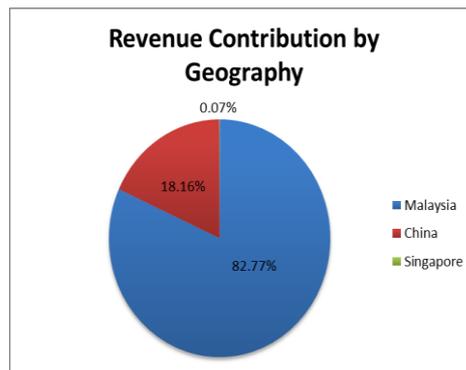
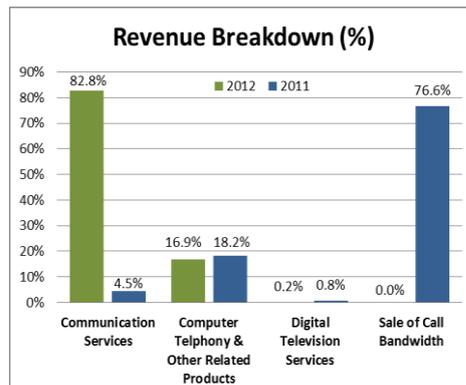
**Awarded RM82.5m worth USP project –** Net profit totaling RM6m was reported by REDtone for 1HFY2013 compared to RM2.1m for the whole FY2012, and we expect the amount to be substantially higher in 2HFY2013. This is mainly due to the RM82.5m worth Universal Service Provider (USP) contract from Malaysian Communications and Multimedia Commission's (MCMC) awarded to REDtone to build, operate and maintain radio access network (RAN) infrastructure in nine rural area in Sabah. The contract is part of MCMC's Time 3 Programme and it made up of an upfront capital expenditure-installation portion (RM49.5m) plus 2-3 years of maintenance services (RM8.25m). Economies of scale from its established presence in Sabah and Sarawak allow Redtone to earn good margin, thus management is expecting more than 30% PBT margin under the USP contract.

Other than USP project, REDtone has submitted another 3 government tenders since last year. In the meantime, it is busy with MyREn (Malaysia Research and Education Network) program and Penang Free WiFi contract which offer good margins. With government speeding up its efforts to provide internet connection to rural areas, REDtone could leverage on its core competency of integrating technologies and initiate more broadband projects which will provides REDtone steady stream of income flow. We expect to see a switch in group revenue mix between the government sector and SME contribution from 30:70 to 60:40.

**Shareholders expect to receive dividend –** REDtone has not paid any dividend to its shareholders in the past five years. With the improved cash flow, REDtone has recently approved a dividend policy of minimum 25% of net profit. With estimated RM23m net profits in FY2013 and RM27m in FY2014, REDtone could conceivably distribute 1.3sen dividend per share in FY2013 and 1.5sen in FY2014, implying net yield of 3.3% - 3.8% at the prevailing price of 39sen per share.

**Recommendation:-**

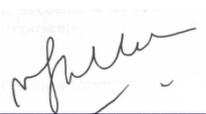
We turn positive on REDtone after its divestments of non-yielding subsidiaries, long-term partnership with government and most importantly, 4G rollout with Maxis brings them handsome recurring incomes for the next 10 years. With the new 4G ecosystem which promises blazing-fast data transmission speeds, we expect it would increase the engagement and more monetization opportunities for REDtone as the demand for high speed broadband is amplifying hastily, in conjunction with wide adoption of smart phone and table services. Valuation-wise, its forward PER of 7.9x is attractive for its strong cash flow from Maxis. Therefore, we recommend a BUY on REDtone.



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For Phillip Capital Management Sdn Bhd

  
**Nona Salleh**  
 Executive Chairperson

**APPENDIX  
LIST OF STOCKS RECOMMENDED SINCE 2011**

<b>Our Picks – 2011/12</b>						
<b>No</b>	<b>Stock</b>	<b>Date</b>	<b>Price*</b>	<b>Price @ 20/03/13</b>	<b>% Change</b>	<b>Comments</b>
1	CIMB	9 Mar 11	RM 7.71	RM7.17	-7.0%	Hold. Avoid before election date announcement.
2	TRC	20 Apr 11	RM0.586	RM0.53	-9.6%	Buy. Price falling back to bottom.
3	Bstead	4 Aug 11	RM4.245	RM4.91	15.7%	Buy/Hold. Back to RM4.90 support
4	Dialog	19 Aug 11	RM2.354	RM2.34	-0.6%	Long Term Buy. Trading near it support of RM2.30.
5	Yinson	13 Sep 11	RM1.129	RM2.31	104.6%	Buy/Hold. Technically strong tested new high of RM2.35.
6	Eng Kah	18 Nov 11	RM 3.09	RM3.33	7.8%	Medium Term Buy. RM3.40 support broken, next support of RM3.20 is strong.
7	Prestariang	14 Dec 11	RM0.565	RM1.17	107.1%	Buy/Hold. Perceived political risk is high as it has substantial contracts from government.
8	Padini	21 Mar 12	RM1.39	RM1.94	39.6%	Buy/Hold. Will concentrate on Brand Outlet in general market.
9	MPHB	27 April 12	RM2.58	RM3.64	41.1%	Buy. Listing will be on again after SC agree to property valuation at a later date
10	Top Glove	17 May 12	RM4.20	RM5.51	31.2%	Hold. Intend to expand its nitrile production aggressively.
11	Genting	30 May 12	RM9.965	RM9.61	-3.6%	Buy/Hold. Price recovered from low.
12	Airport	8 June 12	RM5.56	RM5.62	1.1%	Hold. Trading between RM5.20 floor and RM5.90 ceiling.
13	RHB Cap	31 July 12	RM7.31	RM8.57	17.2%	Buy. We don't think there is a need to privatise RHB Cap but merger with MBSB is possible.
14	OCC	6 Aug 12	RM0.435	RM0.50	14.9%	Still a Buy. Entrance of a GLC with 5% stake will boost sentiment.
15	Pantech	18 Aug 12	RM0.628	RM0.73	16.2%	Buy. Do not rule out possible acquisition to grow its business further.
16	POS	19 Oct 12	RM3.10	RM4.15	33.9%	Buy. Not looking back after breaching RM3.70 resistance
17	DRB	30 Nov 12	RM2.40	RM2.54	5.8%	Medium-Term Buy. Merger of Proton Edar and EON will save cost.
18	Telekom	7 Dec 12	RM5.46	RM5.25	-3.8%	Hold. Valuation is getting expensive from recent results.
19	MBSB	24 Jan 13	RM2.25	RM2.74	21.8%	Still a Buy. Surprise market with 18 sen special div from Section 108

*\*Price adjusted for dividend, bonus and rights*