

UPDATE REPORT

8 June 2018

<b>Name of PLC:</b> N2N Connect Berhad (N2N)		<b>PLC Website:</b> <a href="http://www.n2nconnect.com">www.n2nconnect.com</a>	
<b>Business Summary:</b> Provision of enterprise-wide integrated e-commerce securities trading solutions to stock broking firms and banks.			
<b>Top Three Shareholders:</b> N2N Connect Holdings Sdn Bhd		29.2%	
Nikkei Inc		11.4%	
Quick Corp		11.4%	
<b>Market / Sector:</b>	ACE/ Trading & Services	<b>Stock Code:</b>	0108
		<b>Bloomberg Ticker:</b>	N2N:MK
<b>Market Capitalisation:</b>	RM 660.5m	<b>Recommendation:</b>	HOLD
<b>Target Price:</b>	RM1.10	<b>Expected Capital Gain:</b>	-9.8%
<b>Current Price:</b>	RM 1.22	<b>Expected Div Yield:</b>	2.4%
		<b>Expected Total Return:</b>	-7.4%
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Key Stock Statistics	2016	2017	2018F	2019F
EPS (sen)	2.0	4.1	5.3	5.3
P/E (x)	60.2	29.5	23.1	23.1
EPS ex-EI (sen)	1.9	2.6	4.3	5.3
P/E ex-EI (x)	62.7	46.4	28.3	23.1
Net Dividend/Share (sen)	0.8	0.8	2.9	3.0
NTA/Share (RM)	0.34	0.24	0.39	0.41
Book Value/Share (RM)	0.37	0.40	0.52	0.54
Issued Capital (mil shares)	476.4	477.1	579.8	579.8
52-weeks Share Price Range (RM)				0.67-1.24
Estimated free float				25.8%
Average volume (shares)				4.20m

Per Share Data	2016	2017	2018F	2019F
Year-end 31 Dec				
Book Value/Share (RM)	0.37	0.40	0.52	0.54
Operating CF/Share (sen)	2.3	6.8	7.3	7.4
EPS (sen)	2.0	4.1	5.3	5.3
Net Dividend/Share (sen)	0.8	0.8	2.9	3.0
P/E (x)	60.2	29.5	23.1	23.1
P/Cash Flow (x)	52.8	18.0	16.7	16.6
P/Book Value (x)	3.3	3.1	2.4	2.3
Dividend Yield (%)	0.7	0.7	2.4	2.4
Payout Ratio (%)	40.4	19.6	55.0	56.0
ROE (%)	6.6	13.0	12.5	10.0
Net Gearing (%)	(18.4)	(14.8)	(30.6)	(29.4)


P&L Analysis (RM mil)	2016	2017	2018F	2019F
Revenue	41.8	97.3	111.6	119.1
EBITDA	18.7	35.2	46.2	46.1
Depreciation & amort	(7.4)	(10.3)	(12.2)	(12.7)
Net interest income	0.5	0.3	(0.7)	(0.1)
EI *	0.5	8.7	5.6	-
Pre-tax Profit	11.8	25.2	33.3	33.3
Net Profit	11.7	24.0	30.6	30.6
EBITDA Margin (%)	44.7	36.2	41.4	38.7
Pre-tax Margin (%)	28.2	25.9	29.9	27.9
Net-Margin (%)	28.1	24.6	27.5	25.7

1. Investment Highlights/Summary

- N2N proposed to issue private placement of 52m new ordinary shares in N2N, to SBI Holdings. Inc (SBI) at an issue price of RM1.25 per placement share. The placement is expected to be implemented in a single tranche and to be completed by 2Q18.
- While the discussion with SBI is undergoing and yet to be finalised, we believe the proposed business alliances will likely be complementary to the existing business of N2N and will expedite N2N's plans to build its "Asia Trading Hub" that would connect all their panel brokers across 8 to 12 countries.
- We do not expect the placement to have any material effect on the earnings in the near-term. Post adjustment, our earnings estimates are slightly higher due to higher interest income. Post adjustment of placement shares, our EPS for FY18-19E reduce from 5.5-5.6sen to 5.3sen.
- HOLD recommendation and TP remain unchanged. We will revisit with an upgrade if N2N succeeds in expanding into new markets as well as in holistically growing its regional trade connection platform. Our TP is based on unchanged target P/E of 20x, implying a PEG ratio of 1x, underscored by the company's 4-year core earnings CAGR of 25.9% (FY13-FY17) and positive forward earnings outlook.

**2. Corporate Development**

- N2N proposed to issue private placement of 52m new ordinary shares in N2N, representing 10% of the total number of issued shares in N2N (excluding treasury shares), to SBI at an issue price of RM1.25 per placement share. The proposed private placement does not require further approval except from Bursa Malaysia, given that the general mandate was approved in the shareholders’ 17<sup>th</sup> Annual General Meeting held on 25 May 2018. The placement is expected to be implemented in a single tranche and to be completed by 2Q18.
- Given the placement shares are issued at RM1.25, N2N will raise RM65.05m from the exercise. Bulk of the proceed will be utilised for business alliances with SBI Group, including acquisition of strategic investments or strategic collaboration, joint ventures or alliances with SBI Group. While the discussion with SBI Group is undergoing and yet to be finalised, we believe the proposed business alliances will likely be complementary to the existing business of N2N. According to the announcement, the proposed business alliances involve leveraging on the financial technology and brokerage networks of the parties.
- SBI is a listed company on the First Section of Tokyo Stock Exchange with market capitalisation of RM23.9b. It operates in the financial services business, asset management business and biotechnology-related business segments. We understand that the Group has been investing on digital asset-related ventures possessing high level technology in order to form a robust digital asset ecosystem and many investments were completed as shown in the table below. We believe this is strongly aligned with N2N’s vision and expect it to contribute and expedite N2N’s plans to build its “Asia Trading Hub” that would connect all their panel brokers across 8 to 12 countries.

**Investments and Alliances with Digital Asset-related Ventures** 

Company	Business	Investment	Alliance
CoVenture / U.S.	Digital asset hedge fund management	Done (approx. 6%)	30% acquirement of fund GP under CoVenture, establishment of JV (SBI CoVenture Asset Management)
T1R / U.S.	ICO consultation & financing platform	Done (20%)	Cooperation with the SBI Group ICO businesses
CoolBitX / Taiwan	Cold wallet service development	Done (40%)	Consideration of the use of products in the digital asset ecosystem
Sepior / Denmark	Cloud key management service	Done (49%)	Development of robust smartphone security systems
Everspin / Korea	Development of Dynamic securities	Done (22%)	JV consideration
Obook / Taiwan	E-commerce by blockchain	Done (20%)	JV consideration
Etix / Europe	Data center management	Done (approx. 41%)	Mining base consideration
Othera / U.K.	Securitized receivables by blockchain	Done (20%)	JV consideration
Company S / Switzerland	Cold wallet development	MOU concluded	JV consideration
Company B / Switzerland	Development & provision of wallet app	Adjusting investment	JV consideration
Company N / Malaysia	Global trading hub including cryptocurrency	Adjusting investment	-

Source: SBI’s website

**3. Earnings Outlook**

- We do not expect the placement to have any material effect on the earnings in the near-term. Post adjustment, our earnings estimates are slightly higher due to higher interest income. Growth should be imminent when the borderless trading takes off. Nevertheless, post adjustment of placement shares, our EPS for FY18-19E reduce from 5.5-5.6sen to 5.3sen. Note that we have also excluded the treasury shares. The Company’s balance sheet will also be strengthened further from a net cash position of 0.2x to 0.3x.

**4. Valuation and Recommendation**

- We maintained our HOLD recommendation and TP. We believe the stock is fairly valued for now. We will revisit with an upgrade if N2N succeeds in expanding into new markets as well as in holistically growing its regional trade connection platform. Our TP is based on unchanged target P/E of 20x, implying a PEG ratio of 1x, underscored by the company’s 4-year core earnings CAGR of 25.9% (FY13-FY17) and positive forward earnings outlook.

Share price chart of N2N



### Disclosures/Disclaimer

Investment ratings:

Buy (generally >10% upside over the next 12 months)

Hold (generally negative 10% downside to positive 10% upside over the next 12 months)

Sell (generally >10% downside over the next 12 months)

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