

# Plover Bay Tech (1523 HK)

## Disruptive Tech Trading At a Discount

Plover Bay (PB) designs and markets SD-WAN routers and software, providing a cost-effective and mobile alternative to conventional wide-area network for enterprise users. We forecast 55% YoY net profit growth in FY16 based on 21% YoY revenue growth and margin improvement from higher mix from software licenses. We believe PB's shares are undervalued at its current 11x FY16F P/E vs 15x average of US-listed network equipment peers and offers 6% yield.

### SD-WAN: A Disruption To Conventional Enterprise Networks

Software-defined wide area network (SD-WAN) is at an early growth phase and IDC (research firm) projects the market to grow 90% CAGR to US\$6bn in 2015-2020. SD-WAN offers large cost savings over conventional WAN infrastructures and can be deployed rapidly in remote sites. As a pure-play SD-WAN vendor, PB had ~6% revenue share and ranked fifth among ~30 SD-WAN vendors in 2015. Its products are mostly found in the automobile, transportation, maritime, education and public safety industries instead of the crowded enterprise market.

### Lean Structure With Strong Profitability And Cash Flows

PB focuses on product and software development and user support with a team of 120 engineers in Hong Kong and outsources manufacturing to a Taiwanese OEM. Its products are sold globally through over 400 3rd party distributors (usually network solution companies) under the brands Pepwave and Peplink. PB also provides cloud-based services (SpeedFusion and InControl) that allow end-users to easily configure and manage their SD-WAN, providing recurring software license fees. Licensing accounted for 26% of total revenue in 1H16. Leveraging on its asset-light structure and focus on specialized verticals instead of the highly competitive enterprise market, PB has been able to deliver ~20% net profit margin and strong free cash flows in the past while most startup peers suffered from losses. For FY16, we expect 55% YoY core net profit growth driven by 21% YoY revenue growth and margin improvements from higher mix in software licenses. PB intends to drive future growth by adding distributors and enhancing its software products to deliver more value add to existing verticals. Growth by M&A is also possible, given strong net cash post-IPO and a highly fragmented SD-WAN market.

### Trades At Discount To US Peers And Offers Strong Potential Yield

We believe PB is attractive at 11x FY16F P/E & 6% yield on our forecast, below the 15x P/E range of US-listed network equipment peers. Given PB's established brand name in the US and strong profitability, an M&A offer by a large incumbent network equipment vendor could be a share price catalyst, in our view. **Key risks** are (1) ASP decline due to competition and (2) uncertainty over US trade policies as US accounts for close to 50% of revenues in 1H16.

Figure 1: Financial Summary

Year to Dec 31 (USDt)	FY13A	FY14A	FY15A	FY16F
<b>Revenue</b>	<b>13,306</b>	<b>17,946</b>	<b>21,860</b>	<b>26,450</b>
Operating Profit	3,012	4,289	5,142	8,071
<b>Underlying Profit</b>	<b>2,565</b>	<b>3,743</b>	<b>4,358</b>	<b>6,760</b>
<b>Underlying EPS (USD)</b>	<b>0.003</b>	<b>0.005</b>	<b>0.006</b>	<b>0.008</b>
Underlying EPS growth (%)	0.0	45.9	16.4	36.2
P/E (x)	25.3	17.3	14.9	10.9
P/B (x)	9.8	9.8	9.1	2.9
Dividend Yield (%)	2.0	5.7	4.3	6.0
<b>Net debt/equity (%)</b>	<b>(54.1)</b>	<b>(48.2)</b>	<b>(67.8)</b>	<b>(94.9)</b>
ROE (%)		56.8	63.6	41.5

Source: Company data, Guosen Securities (HK) Research

Hong Kong TMT  
Technology

07 February 2017 Non rated

Target price N/A

Last price (7 Feb 17) HKD0.67

Upside/downside (%)

HSI 23331.57

Mkt cap (HKDm/USDm) 670/86.4

52 week range (HKD) 0.40 - 0.70

Avg trading volume daily (USDm) 0.59

Free float (%) 25

Source: Bloomberg

### Performance



Source: Bloomberg

Performance	1M	3M	12M
Absolute (%)	31.4	42.6	
Absolute (USD, %)	31.3	42.5	
Relative to HSI (%)	27.7	40.2	

Source: Bloomberg

### Company background

Plover Bay Technologies Limited designs, develops, markets and sells both wired and wireless SD-WAN router products and services. The Company offers its products and services to numerous industries around the world including the transportation, retail, and education markets.

Source: Bloomberg

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## Financial forecast

### Looking at 55% core net profit growth in FY16

Figure 2 Earnings forecasts for 2016

FY Dec-31, USD thousands	1H15	2H15	1H16	2H16F	FY15	FY16F
<b>Revenue</b>	<b>10,734</b>	<b>11,126</b>	<b>12,033</b>	<b>14,417</b>	<b>21,860</b>	<b>26,450</b>
YoY	0%	0%	12%	30%	22%	21%
Cost of sales	-4,786	-4,380	-4,110	-5,677	-9,166	-9,787
<b>Gross profit</b>	<b>5,948</b>	<b>6,745</b>	<b>7,923</b>	<b>8,741</b>	<b>12,693</b>	<b>16,664</b>
GPM	55%	61%	66%	61%	58%	63%
Other income	59	10	24	45	69	69
Selling & Distribution	-467	-536	-607	-636	-1,003	-1,243
Admin	-1,284	-1,426	-1,344	-1,777	-2,710	-3,121
Research & Development	-2,034	-1,873	-2,015	-2,282	-3,907	-4,297
Opex / revenue	-35%	-34%	-33%	-33%	-35%	-33%
Listing expenses	-544	-457	-537	-713	-1,001	-1,250
Finance cost	-1	0	-14	-5	-1	-19
<b>PBT</b>	<b>1,677</b>	<b>2,463</b>	<b>3,430</b>	<b>3,372</b>	<b>4,140</b>	<b>6,802</b>
Income tax	-292	-491	-629	-663	-783	-1,292
Tax rate	-17%	-20%	-18%	-20%	-19%	-19%
<b>Net profit</b>	<b>1,385</b>	<b>1,972</b>	<b>2,801</b>	<b>2,709</b>	<b>3,357</b>	<b>5,510</b>
YoY	0%	0%	102%	37%	-10%	64%
Net margin	0%	0%	0%	0%	15%	21%
<i>Adjustments:</i>						
Listing expenses	-544	-457	-537	-713	-1,001	-1,250
<b>Core net profit</b>	<b>1,929</b>	<b>2,429</b>	<b>3,338</b>	<b>3,422</b>	<b>4,358</b>	<b>6,760</b>
YoY	0%	0%	73%	41%	16%	55%
Net margin	18%	22%	28%	24%	20%	26%
Dividend	1,000	998	2,224	2,167	2,800	4,391
Payout ratio	72%	51%	79%	80%	64%	80%
<b>Core EPS (USD)</b>	<b>0.003</b>	<b>0.003</b>	<b>0.004</b>	<b>0.004</b>	<b>0.006</b>	<b>0.008</b>
<u>Share data (million)</u>						
Shares issued	750	750	750	1,000	750	1,000
Weighted avg shares	750	750	750	958	750	854

Source: Company data, Guosen Securities (HK) Research

## Valuation and peer comparison

### PB trades at a discount vs US listed peers

Majority of PB's peers are unlisted startup companies based in the US. Larger unlisted peers include Aryaka, Talari Networks, Silver Peak and Velocloud. Listed peers such as Cisco, Citrix, Brocade and Ubiquiti also offer SD-WAN products, but their revenues from SD-WAN currently make up a minor portion compared to revenues from conventional enterprise routers. Many of these peers offer software-as-a-service (SaaS) or network-as-a-service (NaaS) to enterprise users while PB's revenues are mostly derived from specific industry use cases that require easily deployable mobile internet access. US-listed peers currently trade between 15x 2016 P/E, compared to PB's 11x FY16 P/E.

Figure 3 Peer comparison (7/2/2017)

Company	Ticker	Price	Mkt cap (USDm)	3-mth avg t/o (USDm)	Hist P/E	FY1 P/E	FY2 P/E	FY1 EPS YoY (%)	FY2 EPS YoY (%)	3-Yr EPS CAGR (%)	PEG	Hist Div Yld (%)	FY1 Div Yld (%)
Plover Bay Tech	1523 HK	0.67	86	0.5	13.5	9.9	n.a.	36.2	n.a.	n.a.	n.a.	5.3	7.3
Brocade Communications	BRCD US	12.48	5,070	74.9	24.0	12.3	12.0	95.2	2.8	25.6	0.5	1.6	1.7
Cisco Systems	CSCO US	31.30	157,118	693.2	14.7	13.2	12.6	11.4	4.7	6.8	1.9	3.0	3.5
Juniper Networks	JNPR US	27.28	10,375	109.0	17.3	12.5	11.7	38.4	6.5	15.5	0.8	1.5	1.6
Ubiquiti Network	UBNT US	63.62	5,225	20.4	25.1	20.9	19.6	20.2	6.5	10.7	1.9	0.0	0.0
<b>Peers average</b>					<b>20.3</b>	<b>14.7</b>	<b>14.0</b>	<b>41.3</b>	<b>5.1</b>	<b>14.7</b>	<b>1.3</b>	<b>1.5</b>	<b>1.7</b>

Source: Bloomberg, Guosen Securities (HK) Research

## Summary financial statements (Year to Dec 31)

<b>Profit &amp; Loss (USDt)</b>	<b>FY13A</b>	<b>FY14A</b>	<b>FY15A</b>	<b>FY16F</b>
<b>Revenue</b>	<b>13,306</b>	<b>17,946</b>	<b>21,860</b>	<b>26,450</b>
Revenue growth (%)	0.0	34.9	21.8	21.0
Cost of sales	(4,655)	(6,910)	(9,166)	(9,787)
<b>Gross profit</b>	<b>8,651</b>	<b>11,036</b>	<b>12,693</b>	<b>16,664</b>
Other income/(expense)	34	306	69	69
Operating expenses	(5,672)	(7,053)	(7,620)	(8,662)
<b>Operating profit</b>	<b>3,012</b>	<b>4,289</b>	<b>5,142</b>	<b>8,071</b>
Operating profit growth (%)	0.0	42.4	19.9	57.0
Other non-operating inc/(exp)	0	0	(1,001)	(1,250)
Finance income	0	0	0	0
Finance expenses	(4)	(4)	(1)	(19)
Associates & JCE	0	0	0	0
<b>Profit before taxation</b>	<b>3,009</b>	<b>4,285</b>	<b>4,140</b>	<b>6,802</b>
Taxation	(444)	(542)	(783)	(1,292)
Non-controlling interests	0	0	0	0
<b>Net profit</b>	<b>2,565</b>	<b>3,743</b>	<b>3,357</b>	<b>5,510</b>
Other Adjustments on UP	0	0	1,001	1,250
<b>Underlying Profit</b>	<b>2,565</b>	<b>3,743</b>	<b>4,358</b>	<b>6,760</b>
Underlying profit growth (%)	0.0	45.9	16.4	55.1
EPS (USD)	0.003	0.005	0.004	0.006
<b>Underlying EPS (USD)</b>	<b>0.003</b>	<b>0.005</b>	<b>0.006</b>	<b>0.008</b>
Underlying EPS growth (%)	0.0	45.9	16.4	36.2
DPS (USD)	1.73	4.94	3.73	5.14
DPS growth (%)	0.0	185	(24.4)	37.7

Source: Company data, Guosen Securities (HK) Research

<b>Balance Sheet (USDt)</b>	<b>FY13A</b>	<b>FY14A</b>	<b>FY15A</b>	<b>FY16F</b>
Fixed assets	446	595	556	518
Associates & JCE	0	0	0	0
Others	56	90	277	486
<b>Non-current assets</b>	<b>502</b>	<b>685</b>	<b>833</b>	<b>1,004</b>
Inventories	2,585	3,651	4,138	4,022
Debtors & prepayments	2,136	3,328	3,857	4,348
Bank deposits & cash	4,133	3,696	6,062	25,174
Others	1,393	816	459	459
<b>Current assets</b>	<b>10,247</b>	<b>11,491</b>	<b>14,516</b>	<b>34,003</b>
Bank & other borrowings	59	60	1,239	1,000
Trade & payables	1,514	1,983	1,045	1,609
Taxation	342	499	516	516
Others	1,503	1,922	4,661	5,461
<b>Current liabilities</b>	<b>3,418</b>	<b>4,464</b>	<b>7,460</b>	<b>8,586</b>
Bank & other borrowings	517	455	0	0
Others	237	660	776	953
<b>Non-current liabilities</b>	<b>754</b>	<b>1,116</b>	<b>776</b>	<b>953</b>
<b>Net assets</b>	<b>6,577</b>	<b>6,596</b>	<b>7,113</b>	<b>25,468</b>
Share capital	0	0	0	1,285
Premium & reserves	6,577	6,596	7,113	24,183
<b>Shareholders' funds</b>	<b>6,577</b>	<b>6,596</b>	<b>7,113</b>	<b>25,468</b>
<b>Non-controlling interests</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>0</b>
<b>Total equity</b>	<b>6,577</b>	<b>6,596</b>	<b>7,113</b>	<b>25,468</b>
<b>BVPS (USD)</b>	<b>0.0</b>	<b>0.0</b>	<b>0.0</b>	<b>0.0</b>

Source: Company data, Guosen Securities (HK) Research

<b>Financial Ratios</b>	<b>FY13A</b>	<b>FY14A</b>	<b>FY15A</b>	<b>FY16F</b>
Gross profit margin (%)	65.0	61.5	58.1	63.0
Operating profit margin (%)	22.6	23.9	23.5	30.5
Underlying profit margin (%)	19.3	20.9	19.9	25.6
Net debt/equity (%)	(54.1)	(48.2)	(67.8)	(94.9)
Net debt/total assets (%)	(33.1)	(26.1)	(31.4)	(69.1)
Current ratio (%)	300	257	195	396
Dividend payout (%)	50.7	98.9	64.2	65.0
Interest cover (x)	828	969	3,934	424
Dividend cover (x)	2.0	1.0	1.6	1.5
Acct. receivable turnover days		55.6	60.0	56.6
Acct. payable turnover days		92.4	60.3	49.5
Inventory turnover days		164.7	155.1	152.2
Cash cycle days		127.9	154.8	159.3
<b>Dupont Analysis</b>	<b>FY13A</b>	<b>FY14A</b>	<b>FY15A</b>	<b>FY16F</b>
Tax burden (%)	85.3	87.3	81.1	81.0
Interest burden (%)	99.9	99.9	80.5	84.3
Operating profit margin (%)	22.6	23.9	23.5	30.5
Asset turnover (x)		1.6	1.6	1.1
Leverage ratio (x)		1.7	2.0	1.5
<b>ROA (%)</b>	<b>32.7</b>	<b>31.7</b>	<b>26.8</b>	
<b>ROE (%)</b>	<b>56.8</b>	<b>63.6</b>	<b>41.5</b>	

Source: Company data, Guosen Securities (HK) Research

<b>Cashflow (USDt)</b>	<b>FY13A</b>	<b>FY14A</b>	<b>FY15A</b>	<b>FY16F</b>
EBIT	3,012	4,289	5,142	8,071
Depreciation & amortization	201	244	332	520
Interest expense	(4)	(4)	(1)	(19)
Change in working capital	(221)	(1,134)	(712)	1,166
Tax paid	(103)	(358)	(777)	(1,292)
Other operating cashflow	187	52	(965)	(1,250)
<b>Operating activities</b>	<b>3,073</b>	<b>3,089</b>	<b>3,018</b>	<b>7,196</b>
Capex	(238)	(352)	(215)	(320)
<b>Free cash flow</b>	<b>2,835</b>	<b>2,736</b>	<b>2,803</b>	<b>6,876</b>
Disposal of non-current assets	2	0	0	0
Associates & JCE (net)	0	0	0	0
Interest received	13	7	0	0
Dividends received	0	0	0	0
Other investing cashflow	204	476	(700)	(370)
<b>Investing activities</b>	<b>(19)</b>	<b>130</b>	<b>(915)</b>	<b>(690)</b>
New loans raised	0	0	1,239	(239)
Repayment of loans	0	0	0	0
Dividends paid	(1,300)	(3,701)	(2,800)	(3,222)
Other financing cashflow	13	66	1,764	16,067
<b>Financing activities</b>	<b>(1,287)</b>	<b>(3,635)</b>	<b>203</b>	<b>12,607</b>
<b>Inc/(dec) in cash</b>	<b>1,766</b>	<b>(416)</b>	<b>2,306</b>	<b>19,112</b>
Cash at beginning of year	2,365	4,133	3,696	6,062
Foreign exchange effect	1	(20)	60	0
<b>Cash at end of year</b>	<b>4,133</b>	<b>3,696</b>	<b>6,062</b>	<b>25,174</b>

Source: Company data, Guosen Securities (HK) Research

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