HISAKA Holdings Ltd.

Medical Devices Gaining Momentum

Increase Exposure

- Intrinsic Value S$0.580
- Prev Close S$0.475

*HISAKA Holdings Ltd (HISAKA) handed in a credible 1H FY11 results that matched its record setting performance in FY10. We are seeing interesting developments indicating that HISAKA's portable blood warmer system is on track for commercialization. Maintain **Increase Exposure** in anticipation of further positive developments from the medical devices segment (**intrinsic value of S$0.580**).*

Key Developments:

Industry Sources Indicate Growth in FY11F: According to SEMI, demand for semiconductor equipment is expected to grow by >20% in 2011 (pre-Japan Earthquake). We continue to expect positive growth this year as factories restart production.

FY11F Forecasts Maintained: We continue to be positive about HISAKA's outlook given a) positive industry growth outlook, b) alternate parts sourcing measures implemented by the company and c) smooth execution as demonstrated by the company thus far in meeting our expectations.

Medical Devices – A Growth Driver: HISAKA development and production *processes* for the portable blood warmer system received quality management certification last month. This new product is currently undergoing *product* testing to comply with safety/health/environmental standards in export markets and is expected to hit the markets in early 2012.

Valuation Excludes Kicker from Medical Devices: We find it premature to include growth forecasts from the portable blood warmer system into our valuation, but has included the dilutive impact of the 20m (≈12% of capital) new shares to be issued as part of HISAKA's TDR listing. Fund raised will create a new equity pool to fund future developments in the medical devices business, leaving current resources for the main automation and semiconductor components division.

Main Activities

HISAKA Holdings Ltd. provides automation solutions with a focus on the sourcing and manufacturing of mechanical motion and mechatronics integration products. The company has since expanded into the eco-friendly products and medical devices industries.

Financial Highlights

(Y/E Sep) S$ m	FY09	FY10	FY11F
Revenue	34.2	80.9	86.5
Gross Profit	6.3	17.9	19.1
Operating Profit	0.8	10.8	10.9
Earnings	0.7	9.2	9.8
EPS (S cts)	0.35	5.13	5.42

Source: Company, SIAS Research

Key ratios (FY11F)

PER	8.8
P/BV	1.6
Return on Common Equity	22.7%
Return on Assets	17.5%
Gross Debt to Common Equity	0%
Current ratio	4.4

Source: SIAS Research

Indexed Price Chart

Green (FSSTI)
White (HISAKA)

Source: Bloomberg

52wks High-Low	*S$0.525 /S$0.2252^*
Number of Shares	*170.4m*
Market Capitalization	*S$80.95m*

^Fractional prices are due to share buy backs

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Results Analysis

Commendable Set of Results: Coming off a high base in FY10 (ended Sep 2010), HISAKA handed in a worthy set of results for 1H FY11 (ended Mar 2011). 1H FY11 revenue hit S$37.7m or 44% of our full year forecast – well in line with our expectation taking into account industry seasonality.

Understanding Industry Seasonality: The semiconductor equipment industry typically records higher billings from Apr to Sep than in the prior Oct to Mar six-month period. This pattern was upheld in 13 out of the last 19 years, with billings growing by an average of ≈30% more "half year-on-half year" in the Apr to Sep period. Seasonality broke down in only six years, when overall industry demand shrank. Given that the semiconductor equipment industry is still expected to post positive growth in 2011, we expect this pattern to be maintained this year.

Profit Actually Went Up: HISAKA's net profit actually grew by 15.4% or S$0.6m YoY, after excluding inventory and trade receivables related impairment charges and reversals. In 1H FY10, HISAKA benefited from a reversal of S$0.58m on prior impairment charges on inventory and trade receivables. In 1H FY11, impairment charges for these items totaled S$0.13m.

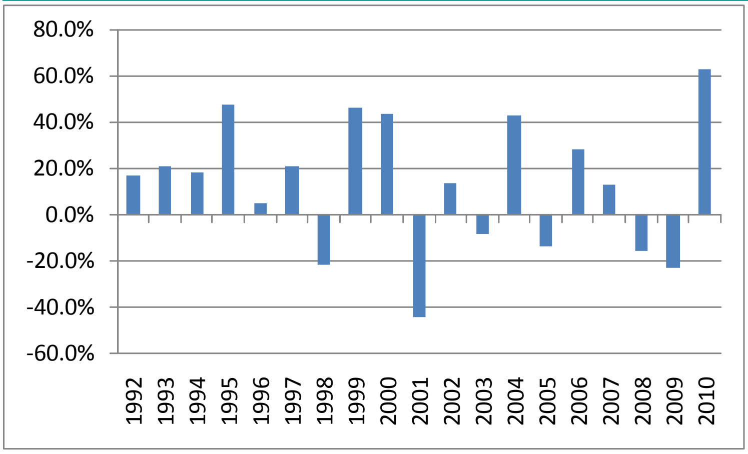
FYI: HISAKA's does not carry electronic items as inventory. As such, obsolescence risk is low. As a policy, HISAKA impairs its inventory and trade receivables based on their age. For instance, inventory that is more than one year old will be impaired at half of their value. However, these charges are reversed when customers pay up the receivable, when demand for the specific inventory is revived, or when the company successfully modifies the item for other uses.

Figure 1: Results Analysis

S$m	1H FY10	1H FY11	Chg	Prior FY11F	1H Act. % of FY11F	Remarks
Revenue	36.6	37.7	3.1%	86.5	43.6%	**In line.** In a good year for the industry, I would expect 1H to account for 40% to 45% of full year numbers.
Gross Profit	7.9	8.2	4.6%	19.1	43.1%	
Net Profit	4.2	4.0	-3.7%	9.8	41.3%	
Inventory & Trade Receivables Charges	0.6	-0.1	-123.0%	-	-	Op. costs were inflated by increased headcount in the technical dept, probably for the medical devices business.
Net Profit (Adjusted)	3.6	4.2	15.4%	9.8	42.6%	
PATMI (As Reported)	4.2	4.0	-3.9%	9.8	41.2%	

Source: Company, SIAS Research

Figure 2: Semiconductor Equipment Billings Growth



Source: SEMI, SIAS Research

Figure 2 shows the % growth in North American companies' global semiconductor equipment billings in the Apr to Sep period of each year, compared to the Oct a year ago to Mar period.

Typically, the Apr to Sep period performs better than the Oct to Mar period.

Building HISAKA's Next Growth Engine

Quality Management Certified: Earlier in April, HISAKA announced that it had officially attained the EN ISO 13485:2003/ AC:2009 certification for the portable blood warmer business. Basically, the certification attests that HISAKA has the quality management system to "consistently meet customer requirements and regulatory requirements" in the areas of "Design and Development, Production, Distribution and Servicing of Portable Blood Warmer System".

Now Certification for Export Markets: HISAKA is currently seeking CE Marking for the portable blood warmer system before bringing the product to the market. The CE (Communauté Européenne) Marking is a "mandatory European marking for various product categories to indicate comformity with the essential health, safety, environmental and consumer protection requirements". Without this marking, HISAKA is unable to export the portable blood warmer to targeted overseas markets, e.g. Europe.

To be Ready Early 2012: In a nutshell, the portable blood warmer system is right now in its final stages of development and we are expecting it to reach the markets in early 2012. By now, it is clear that portable blood warmer system, which was developed jointly with A*STAR, is targeted at both the local and international markets. As a homegrown product, we expect HISAKA to continue receiving support from government agencies in the marketing of the system. If successful, this product will boost HISAKA's growth significantly.

Recap: The blood warmer allows blood to be used for treatment within minutes of removal from storage at low temperatures. Its portability expands the scope of first aid treatments that can be rendered at disaster zones and accident sites.

Figure 3: Product Diagram

Source: Company

Funding the New Growth Engine: In order to move the portable blood warmer system beyond the development stage to commercial production and sales, HISAKA will require funds to purchase equipment as well as working capital to procure raw materials. This explains for the 20m new shares (≈11.7% of existing number of shares) in HISAKA's proposed TDR listing. Ideally, the successful realization of growth in the medical devices business will offset the dilutive impact as a result of the additional shares.

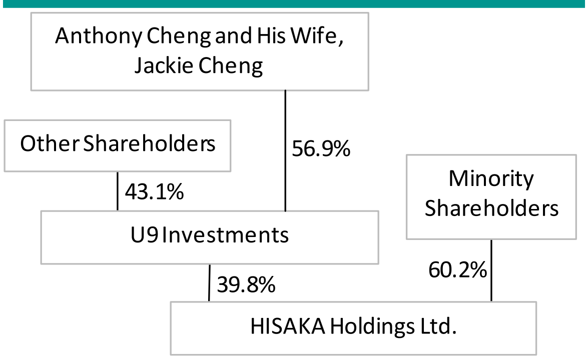
Why Raise Funds with Cash in Bank? In a move to reduce risk, the company's intent is to create a separate pool of equity to fund the medical devices business, while retaining existing funds for its mainstay semiconductor equipment and automation business.

AIP Obtained: HISAKA has already obtained in-principle approval from the Taiwan Stock Exchange to offer and list the equivalent of 60m shares as TDRs, of which 20m will be new shares. The remaining 40m vendor shares currently belong to U9 Investment Pte. Ltd. U9 Investment currently has 67.8m shares in HISAKA, representing a stake of 39.8%. After the TDR listing, U9 Investment will be left with a 16.3% stake in the company. We think that the divestment by U9 Investment is being done with consideration for both existing and future shareholders.

To Unlock Value for the Real Early Birds: U9 Investment is jointly controlled by HISAKA's Chairman Anthony Cheng (and his wife) and CEO Jackie Cheng, but is also made up of four other early investors in HISAKA. The TDR listing will help unlock value for this group of early investors who had been with the company even before its IPO.

An Organized Effort: Of note, U9 Investment is not selling its shares in the open market, but via a non-fungible overseas market listing that can potentially offer an attractive issue price. New shareholders will be able to gain exposure to the second growth pillar that HISAKA is building - in the form of the medical devices business.

Figure 4: Simplified Shareholding Structure

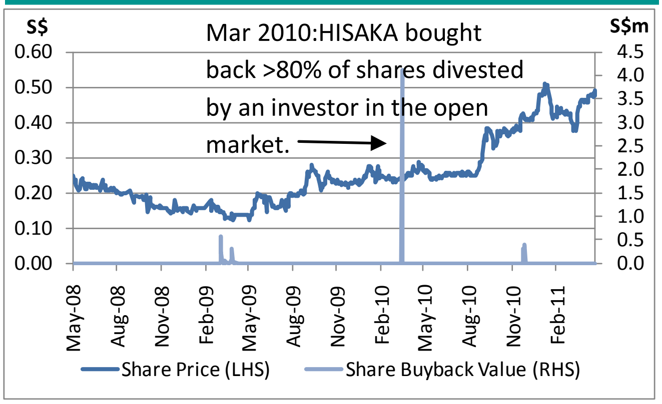


Source: Company, SIAS Research

Shareholding data is as of 7 Dec 2010. The other shareholders of U9 Investments also directly own ≈2% of HISAKA as of 7 Dec 2010.

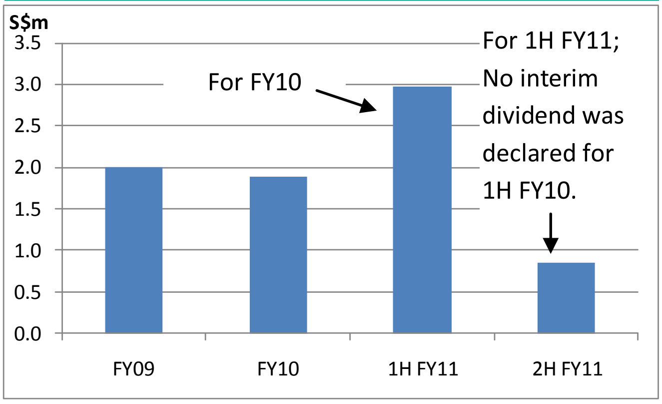
Existing Shareholders Have Also Been Well Rewarded: Since its listing in May 2008, HISAKA has returned S$13.4m to shareholders – S$6.9m in dividends and S$6.6m via share buybacks. On 16 May 2011, HISAKA will return another S$0.9m back to shareholders as dividends for 1H FY11. The funds returned to shareholders have already exceeded HISAKA's net IPO proceeds of S$12.6m three years ago. Furthermore, HISAKA's share price has, as of 28 Apr 2011, appreciated by 108.7% over its IPO price of S$0.23.

Figure 5: Share Price and Share Buybacks since IPO



Source: Company, SIAS Research

Figure 6: Dividends Paid in Each Financial Period



Source: Company, SIAS Research

Growing the Core Business

Still Expect Industry Growth in 2011: HISAKA's core semiconductor equipment components and automation business will continue to remain as a key profit center. SEMI, an industry association, had expected fab equipment spending to grow by 28% in 2011 in a report dated 25 Feb 2011. Given the high growth forecast prior to the Japan Earthquake, we expect the industry to at least show positive growth in 2011.

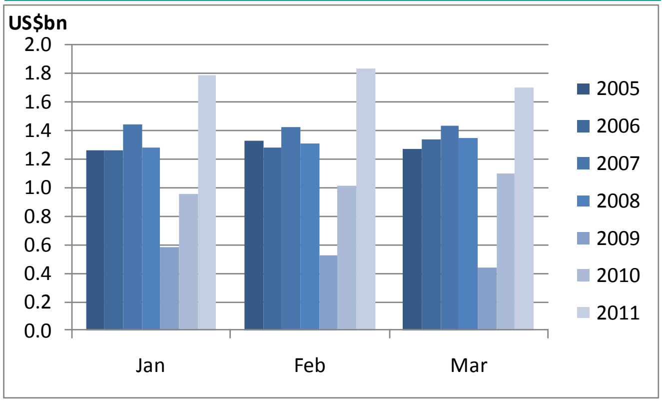
Quake Related Component Shortages Are Being Dealt With: Although Japan factory output fell by 15.3% in Mar due to the earthquake, production is expected to recover by ≈7% in total over Apr and May as factories restart operations. Most of HISAKA's Japanese suppliers have already resumed operations at affected factories, although production levels may take some time to stabilize.

In the meantime, HISAKA has already started sourcing from secondary suppliers in Korea and Taiwan, subjected to the approval of its customers. HISAKA's current order backlog has been lengthened by one to two months as a result of the supply disruptions. In fact, HISAKA's results may enjoy a bump up later on, when more parts are available for it to raise production and reduce backlog.

Not Resting on Laurels: HISAKA only spent S$0.37m and S$0.45m in FY09 and FY10 respectively investing in PPE. Adding in proceeds from the disposal of PPE, the company only spent a net S$0.46m in PPE over both years. The management shared with us that they are constantly looking for opportunities, but will consider proposals carefully, preferring to make staggered investments.

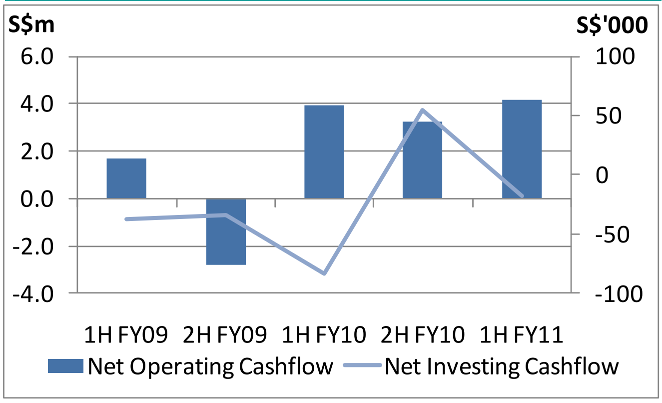
HISAKA had S$16.6m of cash as of end Mar 2011 and no bank borrowings (other than S$4k of financial leases). This translates to more than adequate headroom for the company to gear up its balance sheet to grow the semiconductor equipment parts and automation business.

Figure 7: Industry Billings Still Growing



North American Semiconductor Equipment Makers Global Billings
Source: SEMI, SIAS Research

Figure 8: HISAKA's Strong Cashflow



Source: Company, SIAS Research

Forecasts and Valuation

We keep our FY11F forecasts on HISAKA unchanged with 1H FY11F results largely in line with our projections. Thus far, HISAKA has been meeting our expectations, particularly for FY10 and 1H FY11F. We are expecting existing recovery efforts by both HISAKA and its suppliers to help the company to cope with seasonally higher demand in 2H FY11F.

Nonetheless, downside risks against our view include: a) a slower than anticipated recovery in supply and b) further foreign exchange losses due to the depreciating USD. HISAKA manages its foreign currency risk primarily through natural hedging. Residual exposure is hedged using forwards. The company has raised its hedged exposure to better manage this risk.

We are adjusting our revenue growth forecast for FY12F and FY13F to 15% and 20% respectively (previously 10% annually). We felt that our previous forecasts were too conservative. A demand spike in FY10 had stretched HISAKA's resources, in terms of inventory. Subsequently, the Japan Earthquake had most likely negated some of the new supply brought in to cope with the higher demand. However, we anticipate the full alleviation of these issues in FY12F and FY13F to provide HISAKA with a growth spurt later on.

At the moment, we find it premature to explicitly incorporate growth estimates from the medical devices and eco-friendly products businesses. Upside risk will stem from the successful commercialization of a blockbuster product.

To be conservative, we have already incorporated the additional 20m shares to be listed and estimated proceeds of S$9.5m (03 May 2011 Close of S$0.475 x 20m shares) into our valuation model. (However, we must note that the TDR listing has yet to be finalized.) Consequentially, we arrived at an intrinsic value of S$0.580 or 10.7x FY11F PER. We are maintaining our Increase Exposure call on the anticipation of further positive developments from the medical devices business.

Figure 9: Economic Profit Valuation Model

S$m	FY11F	FY12F	FY13F
Revenue	86.5	99.5	119.4
EBIT	10.9	12.5	15.0
Tax on EBIT	-1.7	-1.9	-2.3
NOPLAT	9.2	10.6	12.7
Invested Capital	41.0	45.9	51.5
% of Debt	0	0	0
% of Equity	100%	100%	100%
WACC (%)	12.04%	12.04%	12.04%
Capital Charge	4.9	5.5	6.2
Economic Profit	4.3	5.1	6.5
Terminal Value			66.3
Discount Rate	0.89	0.80	0.71
Present Value	3.8	4.0	4.6
Book Value (A)	40.8	Risk Free	2.45%
Explicit Value (B)	12.5	Beta	1.0
Terminal Value (C)	47.2	Market RP	9.59%
Total (A+B+C)	100.5	Cost of Equity	12.04%
Add proceeds from TDR Issue^	9.5	Cost of Debt	5.0%
Value of Firm	110.0	LT Growth	2.0%
Number of Shares (m)	190.4	(170.4+20m) shares	
Value per share (S$)	**0.580**		

^Based on the assumption that HISAKA's TDRs will be issued at an equivalent price of S$0.475 per share. S$0.475 x 20m = S$9.5m.

Source: SIAS Research

Figure 10: Financial Forecasts and Estimates

	FY08	FY09	FY10	FY11F	FY12F	FY13F
Revenue	56.3	34.2	80.9	86.5	99.5	119.4
Gross Profit	12.3	6.3	17.9	19.1	22.0	26.4
Operating Profit	5.0	0.8	10.8	10.9	12.5	15.0
Net Profit	3.9	0.7	9.2	9.8	11.2	13.3
Attributable to Shareholders						
Total Current Assets	45.3	39.7	48.8	53.6	63.0	71.1
Total Non-Current Assets	4.4	4.6	5.1	4.5	4.5	4.4
Total Current Liabilities	9.1	6.4	12.9	12.2	16.0	17.3
Total Non-Current Liabilities	0.2	0.1	0.2	0.2	0.2	0.2
Total Equity	40.4	37.7	40.8	45.7	51.3	58.0
Cash from Operating Activities	6.16	1.16	7.41	13.92	2.15	14.53
Cash from Investing Activities	-0.42	-0.07	-0.03	0.06	-0.46	-0.45
Cash from Financing Activities	7.95	-3.53	-6.04	-4.90	-5.59	-6.65
Net change in cash	13.69	-2.44	1.35	9.07	-3.91	7.42
Inventory Days	115	136	43	42	42	42
Receivable Days	108	161	94	95	95	95
Payable Days	104	94	50	60	60	60
ROE (%)	12.5%	1.7%	23.5%	22.7%	23.1%	24.4%
ROA (%)	8.4%	1.4%	18.8%	17.5%	17.8%	18.6%
Debt/Equity	0.3%	0.1%	0.0%	0.0%	0.0%	0.0%
Current Ratio	5.0	6.2	3.8	4.4	3.9	4.1
EPS (S cents)	2.42	0.35	5.13	5.42	5.87	6.99
BV/Share (S cents)	20.1	19.9	23.6	29.0	31.9	35.4
PER	19.6	135.7	9.3	8.8	8.1	6.8
P/BV	2.4	2.4	2.0	1.6	1.5	1.3

EPS and BV/Share have been adjusted to take into account the new shares to be issued. Other income statement, balance sheet and cashflow statement items have not been adjusted.

Source: Company, SIAS Research

Rating Definition:

Increase Exposure – The current price of the stock is significantly lower than the underlying fundamental value. Readers can consider increasing their exposure in their portfolio to a higher level.
Invest – The current price of the stock is sufficiently lower than the underlying fundamental value of the firm. Readers can consider adding this stock to their portfolio.
Fairly Valued – The current price of the stock is reflective of the underlying fundamental value of the firm. Readers may not need to take actions at current price.
Take Profit – The current price of the stock is sufficiently higher than the underlying fundamental value of the firm. Readers can consider rebalancing their portfolio to take advantage of the profits.
Reduce Exposure - The current price of the stock is significantly higher than the underlying fundamental value of the firm. Readers can consider reducing their holdings in their portfolio.

IMPORTANT DISCLOSURE