Investing Ideas: AKN MTECH shares gain from SMS, merger

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Investors who missed out on the initial public offering (IPO) of AKN Messaging Technologies (AKN MTECH) must be kicking themselves hard today. And there will be many. Unlike the subscription rates observed in a fervent market like now, AKN MTECH shares only saw an oversubscription rate of 0.33 times when it made its IPO last December.

Indeed, no one would have thought a Mesdaq Market listing could offer such tremendous upside in such a short period, as witnessed these past nine months.

AKN MTECH shares rose to a new high of RM3.90 last Tuesday, a surge of almost nine times above its offer price of 45 sen in January. Justified or just plain insane?

According to the analysts and fund managers shoring up the frenzy, there's a lot more room for AKN MTECH's share price to grow. "There's still some mileage for the stock. SMS [short message service] content provision is extremely positive and they are going regional now," says Goh Han Hau, senior fund manager at Allianz General Insurance. Between the two research houses tracking the stock, namely AmResearch and GK Goh Securities, both are calling "buys" with target prices of RM4.32 and RM4.50, respectively.

Daniel Tang of GK Goh reports that the target price for AKN MTECH was raised after the company announced the merger between AKN MTECH and its Hong Kong business partner, Messaging Techologies (MTECH) HK.

The deal will see AMT acquiring 83% of MTECH HK through an exchange of 8.74 million new AKN MTECH shares at RM2 each for 4.79 million shares of HK$1 each in MTECH HK. Having only begun operations in August 2001, MTECH HK was still making losses in the financial years (FYs) ended March 31, 2002 and 2003 but is expected to turn profitable by FY2004. For the first five months of the current financial year, MTECH HK recorded a net profit of HK$277,428 or RM133,000. Analysts expect MTECH HK to begin contributing to AKN MTECH's bottom line for its financial year ending June 2005.

It is through the merger that analysts see vast opportunities for the company. MTECH HK, which is now one of the top three third-party mobile content providers on the island, is the bridge to the lucrative Chinese market which currently has 250 million mobile phone users. For a business of managing mobile messaging flows through its gateway and developing content either for client and subscribers, growth is a matter of increasing the frequency or volume of mobile messaging.

"Even in a city like Shanghai, it can take months to activate a fixed line but only a few hours to activate a mobile phone. So it is a pretty good move for them to go into China," says one observer. And going by recent figures of the largest cellular operator in China, China Mobile, the trend in mobile messaging is certainly picking up.

For the first half of FY2003, new business revenues accounted for 8.3% of total revenue. Of this additional revenue, 55.1% came from SMS, 27.5% from value-added services, and 17.4% from other data businesses. This compares against the previous year's breakdown where SMS accounted for 48.5% of new business revenue, 36.1% for value-added services and 15.4% from other data businesses.

AKN MTECH's penetration into China has yet to take place, however. AmResearch notes that the company is in the process of negotiating joint ventures with China Mobile and China Unicom.

"We gather the company will seal the agreements this month but rollout services will only commence in the second quarter of 2004 after the setting up of infrastructure," writes Fiona Leong in a recent report. "We project that by FY2006, AKN MTECH will tap only 0.5% of China's market given competition and its geographically diverse mobile subscriber base. This may be conservative as MTECH HK's track record in Hong Kong reinforces our expectation that the group will perform well in China," predicts Tang of GK Goh.

Indeed, AKN MTECH has earned itself a credible reputation among the local investment community, lending support to the interest in its shares. Fund managers also note its managing director Lim Seng Boon's apparently exceptionally ability in "executing strategy and tying up deals."

One fund manager admits to not being especially familiar with the competitive environment in China but is content with just "taking the company's word for it".

"Their credibility has been a help. They have been delivering on the promised growth and numbers," she says. Back in Malaysia, AKN MTECH says it will focus on growing revenue from its corporate segment which typically offers better margins. Within the next two years it hopes to raise corporate revenue contribution to 40% from the current 15%.

Analysts forecast of net profit for financial year ending June 30, 2004, ranges from RM14.8 million to RM15.09 million. This represents growth of at least 159% from the previous year's profit of RM5.7 million.

The growth forecasts for subsequent years continue to be spectacular. In FY2005 and FY2006, GK Goh projects net profit of RM24.3 million and RM34.6 million, respectively, while AmResearch sees the company raking in RM25.8 million and RM33.4 million, respectively.

Because of its expected high earnings per share (EPS) growth - typical of Mesdaq companies - at least for the next two years, analysts have valued AKN MTECH using the price-earnings (PE) to growth ratio or PEG. The PEG is the PE ratio divided by the annual EPS growth and takes into account other factors such as brand name and human capital that affect the growth of a company. A lower PEG usually indicates that a stock is undervalued.

GK Goh's target price of RM4.50, is based on a valuation of 0.75 times PEG and an 81% compounded annual growth rate in its EPS for FY2003 to FY2005. Similarly, AmResearch has a PEG of 0.5 times and an EPS CAGR of 75% for FY2004 to FY2006.