

RETAIL HOLDINGS NV(RHDGF) - \$8.00 on Aug 30, 2010 by clancy836

			2010	2011
Price:	\$8.00	EarningsPerShare:	\$1.87	\$0.00
Shares Outstanding (in M):	5	P/E:	4.3x	0.0x
Market Cap (in \$M):	42	P/FCF:	0.0x	0.0x
Net Debt (in \$M):	0	EBIT (in \$M):	\$28	\$0
TEV (in \$M):	42	TEV/EBIT:	1.5x	0.0x

Description:

Retail Holdings N.V. (RHDGF) is a retail holding company that arose from the 2000 bankruptcy and liquidation of The Singer Company, a firm in business for almost 160 years which is likely most familiar for its prior role as a sewing machine manufacturer and distributor to the garment industry, but which also founded an extensive network of durable consumer goods retail and manufacturing firms with operations in multiple nations across South and Southeast Asia. First posted by perspicar in 2007, RHDGF still trades at \$8, but is now experiencing several catalysts including an earnings turnaround, expanding market value of its public subsidiaries, and a recent asset sale unlocking significant cash, each pointing to significant upside from current levels.

RHDGF's primary assets consist of a majority stake in Singer Asia (which in turn owns controlling stakes in multiple publicly-traded South Asian durable consumer goods retail and manufacturing subsidiaries further detailed below), in addition to direct ownership of \$25.2 million in 11% notes issued by a KKR affiliate during a 2004 sale of the Singer sewing machine manufacturing operations and trademark, and additional free cash at the holding company level.

The most significant asset is RHDGF's 56.5% ownership of Singer Asia, a holding company with an aggregate \$256 million in revenue which owns majority stakes in publicly-traded subsidiaries in Pakistan, Bangladesh, Thailand, India, and Sri Lanka. Through these entities, Singer operates the single largest retailers of durable consumer and electronic products in both Pakistan and Bangladesh, and is particularly dominant in Sri Lanka, where it holds from 37% to 80% market share nationwide in multiple product categories including televisions, refrigerators, and washing machines. In areas where tariffs or logistics act as barriers to global sourcing, Singer Asia also owns capacity to manufacture or assemble various consumer goods locally, including controlling stakes in two Sri Lanka-based durable goods manufacturing firms, Singer Industries and Regnis PLC. Singer Thailand is the largest direct (door-to-door) retailer of durable consumer goods in that country, and has again become profitable after measures to tighten lending policies at its consumer credit arm. After acquiring additional equity during a 2008 restructuring, Singer now owns a 85.9% stake in Singer India; which now operates principally as a wholesale distributor to the garment industry, but also owns a network of 17 retail stores in major urban centers and is one of only two multinationals with the legal right to operate a nationwide retail operation in India.

In 2003 a 43.2% minority position in Singer Asia was sold to an unrelated private investment fund for \$30 million in cash, which was used to buy back stock and discharge debt and warrants arising from the 2000 Singer bankruptcy exit. This 2003 transaction would value RHDGF's current stake at \$39.4 million, which together with the \$25 million in notes receivable far exceeds the current \$42 million market cap, a reassuring margin of safety using a conservative baseline estimate of private market value. However, after years of successful restructuring, organic revenue growth, and cost controls, Singer Asia has begun to generate significant growth in earnings (magnified by heavy stock buybacks at RHDGF), now making RHDGF deeply undervalued based both on current net income and on a sum-of-the-parts market valuation of its publicly-traded assets.

Earnings Power

Considered purely as a going concern, Retail Holdings appears increasingly attractive, with earnings from continuing operations reaching \$0.80 per share for the last six-month period. CEO Stephen Goodman has historically been very conservative and non-promotional in his communications, but in 2010 midyear comments released earlier this month sounded a much more positive tone, noting a substantial increase in revenue and progress in cost controls, and forecasting net income in excess of \$37.0 million for the current fiscal year, equivalent to earnings per share of more than \$3.25. Backing out a \$1.76 one-time boost to net income expected to occur in the current fiscal quarter on the recently concluded ILFS sale further detailed below, this would still represent annual run-rate operating earnings of \$1.84 per RHDGF share, for a forward P/E of just 4.35.

Subsidiary Market Value

Singer has already begun to gradually monetize its equity positions in publicly-traded subsidiaries as market conditions become favorable, distributing cash to RHDGF shareholders in the form of special dividends and aggressive stock buybacks. During 2009, Singer Asia successfully sold further 5% stakes in Singer Bangladesh and Singer Thailand to the public, and also sold 100% of its unprofitable former Philippines subsidiary. In July 2010 (subsequent to the close of the last reported earnings period), Singer Bangladesh sold its remaining position in a publicly traded consumer finance firm, International Leasing and Financial Services (ILFS), resulting in a boost to net income of \$1.76 per RHDGF share for the coming quarter and a net inflow of \$31.9 million in cash to the RHDGF balance sheet. This cash infusion alone represents nearly three fourths of the current market cap of the entire parent company, though much of this will have likely not yet passed through to the holding company level.

From figures in the latest annual report as of year-end 2009 (not far off 5-year lows for emerging market equities), Singer Asia's publicly-traded holdings had a combined market value of \$128.6 million, of which RHDGF's 56.5% stake represents \$72.7 million, equivalent to \$13.87 per RHDGF share before assigning any value to the additional notes receivable and holding company cash. With a subsequent rebound from depressed levels of 2009, the current market value of Singer shares substantially exceeds even this figure. For example, Singer Bangladesh

has now nearly tripled in market value since RHDGF's last annual report at year-end 2009, likely due to in part to the positive impact of its recent \$32 million sale of ILFC. Singer Sri Lanka has also more than doubled in value with development returning to the island nation after 2009 brought a decisive end to its decades-long civil war, positioning Singer to benefit from its near-monopoly market share in many areas.

To gain further clarity on the discount to market value given management's ongoing monetization of assets, I reviewed the current market capitalizations of principal Singer subsidiaries as reported on websites of the respective national stock exchanges. Below is a table of recent market caps converted to US dollars at current exchange rates and adjusted for Singer Asia's percentage equity stake in each subsidiary. (These are quick back-of-the-envelope calculations as of 8/22/10 based on the data I found, and I'd welcome corrections from anyone with more information.)

Singer Pakistan Ltd 610,639,114 rupees PKR = \$7.14MM * 0.703 Singer Asia equity stake = \$5.01MM USD
Singer Sri Lanka PLC 12,445,835,264 rupees LKR = \$110.7MM * 0.875 equity = \$96.86MM USD
Singer Thailand PLC 864 million baht THB = \$27.38MM * 0.485 equity = \$13.27MM USD
Singer India 33 crore rupees = 330 million rupees INR = \$7.09MM * 0.859 equity = \$6.09MM USD
Singer Bangladesh Ltd 15051 million BDT = \$218MM * 0.75 equity = \$163.5MM USD

\$284.73MM * 0.56516 RHDGF stake in Singer Asia = \$160.92MM

Divided across 5.24 million shares outstanding, current market value of Retail Holdings' stakes in its major publicly traded subsidiaries would come to \$30.71 per RHDGF share, again before considering the additional value of notes receivable and cash at the holding company level. In business for well over a century and continuing to own a variety of wide-ranging retail, manufacturing and credit operations across South and Southeast Asia, the Singer portfolio of companies may contain further assets with additional hidden value to be unlocked over the course of an orderly liquidation, with one case in point being the recent windfall from sale of shares in ILFC.

KSIN Notes

At the holding company level, RHDGF also directly owns \$25.2MM in 11% notes payable by KSIN, a private equity vehicle formed by Kohlberg Kravis Roberts to buy out the Singer sewing machine manufacturing operations and trademark in 2004. KSIN had let the notes slip into default during the credit crisis in 2009, but in May of this year fully cured the default by bringing payments current, and agreed to a rise in interest rate from 10% to 11% in exchange for extending note maturity to September of 2011. Given the attractiveness of Singer Asia these notes can simply be viewed as an added call option; but as credit conditions continue to stabilize, if KSIN is able to refinance and cash out the remaining principal at maturity next year, RHDGF shareholders would benefit from an immediate \$4.81 per share cash infusion, likely stimulating another substantial special dividend that would dramatically reduce the cost basis of any investment made near current prices.

Net Cash Position

Although some debt is incurred by the retail subsidiaries for working capital purposes and is reported on the consolidated balance sheet, this is non-recourse to the holding companies and there is no debt owed by either Singer Asia or RHDGF itself. As of year-end 2009 there was an additional \$1.9 million of free cash at Retail Holdings and \$12.0 million at Singer Asia. These figures were not broken out in the most recent June 2010 semiannual supplement, so it's hard to forecast a precise value for current holding company cash, but given this month's US\$31.9 million sale of ILFS shares by Singer Bangladesh, some significant additional net cash will likely pass to the holdcos even after considering RHDGF's pending \$0.80/share special dividend, again adding a further margin of safety to an already attractive situation.

Management and Capital Allocation

CEO Stephen Goodman owns a 19.6% position in RHDGF common stock, strongly aligning his interests with shareholders. Management constantly reiterates that its plan is to maximize the value of Singer Asia, monetize its investment, and distribute the rewards to shareholders.

"Pending the offering or sale of Singer Asia, realization of the principal and interest on the KSIN Notes and the ultimate liquidation of the Company, ReHo's strategy is to minimize holding company personnel and cost of administration and to use the cash in excess of requirements to purchase Shares and to pay dividends and distributions to shareholders."

Since 2003, RHDGF has showed a consistent and commendable focus on share repurchases and dividends, buying back and retiring over 3.6 million shares and leaving the current total at just 5.24 million outstanding. RHDGF has also issued special cash dividends totaling \$1.95 per share between 2007 and 2009, and recently announced another special distribution of \$0.80 per share in June 2010. Compensation has also been reasonable, with 12 Singer officers and directors taking home a combined \$1.9 million in FY2009, actually down over 10% from the prior year.

Risks

Recurrent weakness in the global economy and credit markets could create risk for Singer Asia and the KSIN notes, although the company certainly weathered the recent downturn well. After delisting several years ago to save on prohibitive Sarbanes-Oxley costs, RHDGF is currently traded on the Pink Sheets, but continues to issue audited annual reports and unaudited semiannual reports to shareholders (all past and recent filings can be downloaded at <http://www.retailholdings.com/disclosureStatements.php?yearID=20>). Trading is obviously illiquid; this idea is most suitable for individual investors who, like me, attempt to generate very high returns from carefully selected personal investments. I own shares in RHDGF, and may buy or sell shares without further notice.

Catalyst:

Continued share buybacks and cash distributions by value-focused and incentivized management

Continued monetization of publicly traded assets, contraction of extreme holding company discount to market value

Maturity of \$25.4 million notes receivable in 2011 could generate \$4.81/share additional cash inflow and distribution

\$31.9 million sale of ILFS stock by Singer Bangladesh makes more cash available for dividends/buybacks and boosts RHDGF net income by \$1.76/share in the coming quarter