

SATS Ltd

Growth has been priced in; wait for better entry point



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SINGAPORE | TRANSPORT SERVICES | FY17 RESULTS

22 May 2017

- FY17 revenue in line with our forecast and consensus expectation
- FY17 underlying PATMI missed our forecast by 3.6%, and missed consensus expectation by 4.0%, as 4Q17 underlying PATMI was dragged down by higher costs
- Final dividend rose to 11 cents (our forecast: 10 cents) from 10 cents in FY16
- Total ordinary dividends of 17 cents for FY17, higher than 15 cents from last year

Results at a glance

(SGD mn)	FY17	FY16	YoY	Comments
Food Solutions	973	967	0.6%	Effect of deconsolidation of food distribution revenue transferred to SATS BRF Food JV
Gateway Services	751	726	3.4%	
Corporate	5.6	4.9	14.3%	
Revenue	1,729	1,698	1.8%	Would have increased 4.5%, if not for the deconsolidation of food distribution revenue transferred to SATS BRF Food JV
EBIT	231	215	7.4%	Better margin of 13.3% from 12.6%, effect of the above mentioned deconsolidation
Associates & JVs	65.2	48.0	36%	Higher contributions from both Food Solutions and Gateway Services, particularly Food Solutions which included the \$15mn negative goodwill and \$1.7mn profit contribution from Evergreen Sky Catering Corporation
PATMI	258	221	16.9%	
Underlying PATMI	234	218	7.4%	FY17 adjusted for gain on disposal of assets held for sale, negative goodwill for Evergreen Sky Catering and loss on divestment/dilution of interest in associates FY16 adjusted for net gain from transfer of business to a JV

Source: Company, PSR

FY17 margin and profit was dragged down in 4Q17

FY17 EBIT margin of 13.3% was better than the 12.6% achieved in FY16. However, there was YoY weakness in 4Q17 EBIT margin of 10.8% from 11.9%. This was in contrast to the first three quarters of FY17, which experienced YoY higher margin that was driven by the deconsolidation of the lower-margin food distribution business to the SATS BRF joint-venture. 4Q17 operating cost was higher due to a few factors – higher wage pressure (due to service increment and lower government subsidies), higher company premises and utility expenses (due to non-renewal of rebates by Changi Airport Group) and higher other costs. Consequently, 4Q17 underlying PATMI was only 1.8% YoY higher. (9M17 underlying PATMI was 9.1% YoY higher.)

Associates received a \$15 million boost in 4Q17

FY17 headline spike of 36% YoY in associates/JV profits was due to a \$15 million negative goodwill recognised in 4Q17. SATS now holds a 25% stake in Evergreen Sky Catering Corporation (ESCC) after acquiring a further 10% stake. The stake in ESCC has now been reclassified from long-term investment to an associate; and the negative goodwill was a result of deemed increase in value of the original investment. Share of profit of associates/JV growth would have been flat at 1.0% YoY, in the absence of this item.

Maintain "Neutral" rating, with higher target price of S\$5.08 (previous: S\$4.73)

SATS Ltd (SATS) has been growing both organically and inorganically. Our price target gives an implied FY18e forward P/E multiple of 23.2x. We are upbeat on the long-term growth for SATS, but we find valuations unattractive at current level. Investors should look to accumulate on price weakness.

Neutral (Maintained)

LAST CLOSE PRICE	SGD 5.29
FORECAST DIV	SGD 0.170
TARGET PRICE	SGD 5.08
TOTAL RETURN	-0.8%

COMPANY DATA

BLOOMBERG CODE:	SATS SP
O/S SHARES (MN) :	115
MARKET CAP (USD mn / SGD mn) :	4245 / 5898
52 - WK HI/LO (SGD) :	5.39 / 4.05
3M Average Daily T/O (mn) :	2.51

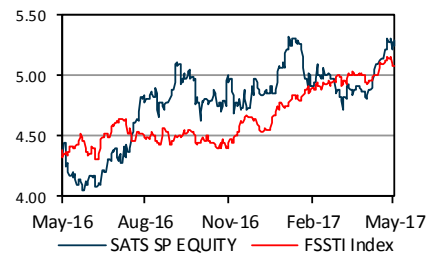
MAJOR SHAREHOLDER (%)

TEMA SEK HOLDINGS PTE LTD	41.0%
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PRICE PERFORMANCE (%)

	1M TH	3M TH	1YR
COMPANY	8.9	6.5	24.0
STIRETURN	3.6	4.8	20.0

PRICE VS. STI



Source: Bloomberg, PSR

KEY FINANCIALS

Y/E Mar	FY 16	FY 17	FY 18e	FY 19e
Revenue (SGD mn)	1,698	1,729	1,695	1,737
PATMI, adj. (SGD mn)	218	234	244	268
EPS, adj. (cents)	19.67	21.08	21.91	24.00
P/E, adj. (x)	20.6	23.3	24.1	22.0
BVPS (cents)	141.1	151.7	166.5	183.4
P/B (x)	2.9	3.2	3.4	3.2
DPS (cents)	15.0	17.0	17.0	18.0
Div. Yield (%)	3.7	3.5	3.2	3.4

Source: Company Data, PSR est.

VALUATION METHOD

DCF (WACC: 7.0%, Terminal g: 2.0%)

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Our narrative for SATS Ltd

SATS will remain a regional food and aviation player, with organic revenue growth driven mainly by air traffic demand. Inorganic growth will mainly come from partnerships in businesses similar to existing ones, as well as adjacent business lines, resulting in investments in Associates & JVs. Capital reinvestment in technology to raise operating leverage and allow the company to scale up.

How our narrative connects to our valuation inputs

- **Food Solutions revenue:** Mid-single digit growth, slightly lower than Gateway Services, as Food Solutions revenue is a blend of the Aviation (faster growth) and Non-aviation (slower growth).
- **Gateway Services revenue:** Mid-single digit growth, in line with aviation demand, and slightly higher growth than Food Solutions.
- **Aviation revenue:** Near term aviation revenue muted at low-single digit growth, but reaching mid-single digit growth in steady state.
- **Non-aviation revenue:** Lower growth than Aviation revenue, at low-single digit growth that is in line with population growth, as this is mainly Food Solutions.
- **Group revenue:** FY18 Group revenue expected to be lower YoY because of sale of 4% stake in Asia Airfreight Terminal Company Limited (AAT) and 51% stake in SATS HK Limited (SATS HK). Management guided that the sales would be completed within the next two quarters. Impact to revenue would be ~\$45 million, as AAT and SATS HK will be deconsolidated to associated companies.
- **Margins:** Slight erosion in operating margin in the near-term, but subsequently expanding, due to gains in scale through the use of technology and automation (operating leverage). Compression in operating margin offset by higher contribution from Associates & JVs, resulting in stable net profit margin.
- **Associates & JVs:** Increasing contribution to the bottom-line as more partnerships are formed. Cash being deployed into forming Associates & JVs, as reflected on the balance sheet and cash flow statement, with cash inflow from dividends.
- **Capital reinvestment:** Higher than historical average in the next two years, reflecting the push to add technology and automation, then normalising to slightly higher than depreciation.

Revenue expectations by Business and Industry

	Aviation	Non-Aviation
Food Solutions	Fastest revenue growth within SATS, driven by demand in air travel.	Institutional food catering, substantially from Singapore Armed Forces (SAF). Expect lowest revenue growth within SATS.
Gateway Services	Consists of passenger and cargo handling. Expect passenger handling to be higher growth compared to cargo handling.	Contribution from Marina Bay Cruise Centre Singapore (MBCCS).

Source: PSR

Discounted cash flow intrinsic valuation

We value SATS using a discounted free cash flow to firm (FCFF) model.

FCFF valuation

Y/E Mar (\$\$ mn)	FY18e	FY19e	FY20e	FY21e	FY22e
Cash flow from operations	238	281	279	301	314
Add: Interest expense x (1 - tax rate)	1	1	1	1	1
Add: Dividends from associates and JVs	39	45	51	57	62
Less: Net capital expenditure	(85)	(85)	(80)	(80)	(80)
Free Cash Flow to Firm	193	242	251	279	297
<i>PV of FCFF</i>	<i>180</i>	<i>212</i>	<i>205</i>	<i>213</i>	<i>211</i>

Terminal value

PV of terminal value **6,051**
4,314

Firm value

5,336

Add: net cash 323

Equity value **5,659**

Number of ordinary shares (mn) 1,115

Price target (\$\$) **5.08**

Assumptions

Cost of capital (equity & debt) 7.0%

Terminal growth rate 2.0%

Source: PSR

Financials

Income Statement

Y/E Mar, SGD mn	FY15	FY16	FY17	FY18e	FY19e
Revenue	1,753	1,698	1,729	1,695	1,737
EBITDA	246	285	304	300	322
Depreciation & Amortisation	(68)	(70)	(74)	(76)	(79)
EBIT	178	215	231	224	244
Net Finance (Expense)/Inc	0.4	2.4	3.4	2.4	2.3
Other items	(1.6)	2.2	9.9	-	-
Associates & JVs	48	48	65	60	69
Exceptional items	(0.1)	(2.1)	-	-	-
Profit Before Tax	225	265	309	287	315
Taxation	(34)	(47)	(48)	(45)	(48)
Profit After Tax	191	218	261	242	267
- Non-controlling interest	(5.0)	(2.2)	2.9	(2.0)	(0.7)
PATMI, reported	196	221	258	244	268
Underlying PATMI	196	218	234	244	268

Per share data (cents)

Y/E Mar	FY15	FY16	FY17	FY18e	FY19e
EPS, reported	17.5	19.9	23.2	21.9	24.0
EPS, adj.	17.5	19.7	21.1	21.9	24.0
DPS	14.0	15.0	17.0	17.0	18.0
BVPS	137.3	141.1	151.7	156.5	163.4

Cash Flow

Y/E Mar, SGD mn	FY15	FY16	FY17	FY18e	FY19e
CFO					
PBT	225	265	309	287	315
Adjustments	27	28	70	13	7
WC changes	21	17	38	(17)	8
Cash generated from ops	273	310	417	284	331
Others	(36)	(37)	(43)	(46)	(50)
Cashflow from ops	236	273	374	238	281
CFI					
CAPEX, net	(61)	(49)	(86)	(85)	(85)
Divd from associates & JVs	89	34	42	39	45
Others	30	(41)	(75)	(76)	(77)
Cashflow from investments	58	(56)	(120)	(122)	(116)
CFF					
Share issuance, net	(49.1)	(1.7)	4.3	-	-
Loans, net of repayments	(0.5)	0.4	(6.7)	(10.4)	(20.0)
Dividends	(146)	(156)	(179)	(189)	(189)
Others	(4.4)	0.5	8.7	-	-
Cashflow from financing	(200)	(157)	(173)	(200)	(209)
Net change in cash	95	60	82	(84)	(45)
Effects of exchange rates	(4.8)	0.6	2.0	-	-
CCE, end	430	490	574	489	445

Source: Company, Phillip Securities Research (Singapore) Estimates

*Forward multiples & yields based on current market price; historical multiples & yields based on historical market price.

Balance Sheet

Y/E Mar, SGD mn	FY15	FY16	FY17	FY18e	FY19e
ASSETS					
PPE	552	517	539	551	560
Intangibles	166	164	158	155	152
Associates & JVs	465	546	671	772	876
Investments	15	22	36	36	36
Others	30	27	20	20	20
Total non-current assets	1,227	1,276	1,423	1,533	1,643
Inventories	19	22	22	22	22
Accounts Receivables	283	277	271	271	275
Prepayments	17	18	17	18	18
Cash	411	490	506	421	377
Others	63	22	40	42	41
Total current assets	793	830	857	774	733
Total Assets	2,020	2,106	2,279	2,307	2,377
LIABILITIES					
Short term loans	16	110	10	20	20
Accounts Payables	287	309	331	316	328
Others	43	51	69	69	69
Total current liabilities	346	470	410	405	417
Long term loans	90	1	98	78	58
Others	67	70	80	80	80
Total non-current liabilities	156	70	178	158	138
Total Liabilities	502	541	588	563	555
EQUITY					
Non-controlling interest	77	74	88	86	85
Shareholder Equity	1,441	1,491	1,604	1,658	1,736

Valuation Ratios

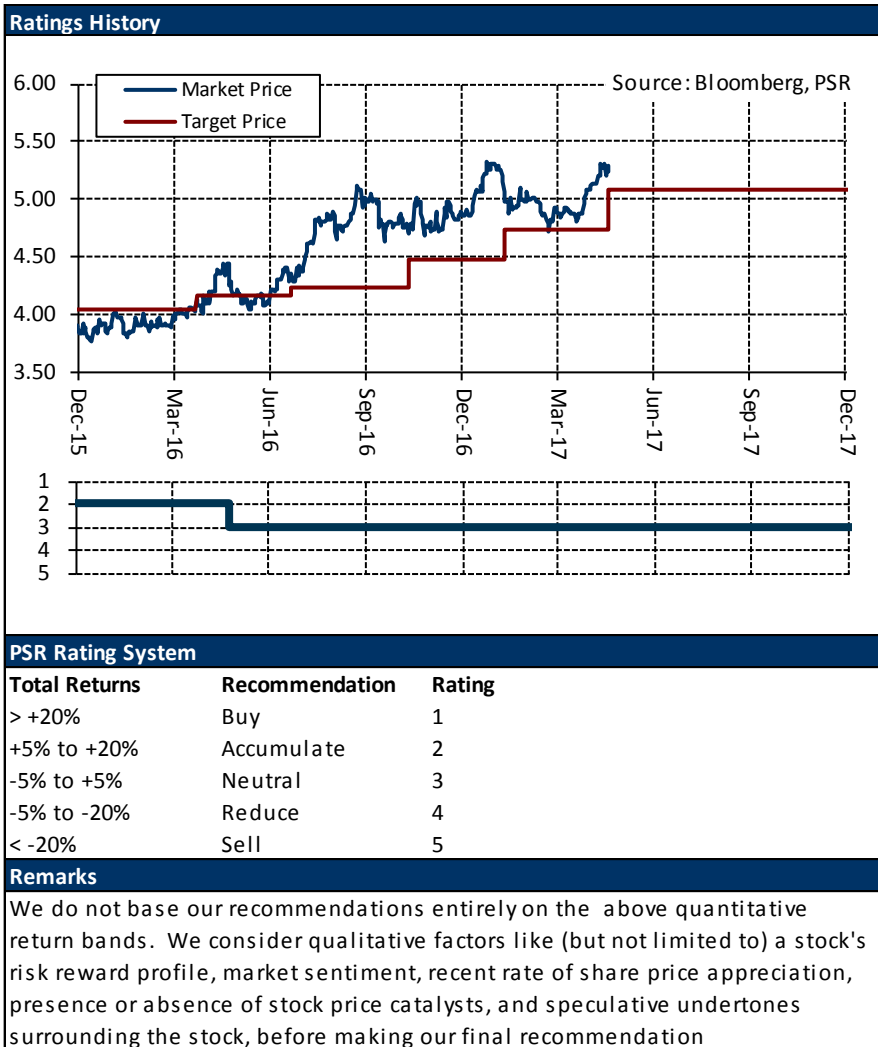
Y/E Mar	FY15	FY16	FY17	FY18e	FY19e
P/E (x), adj.	17.8	20.6	23.3	24.1	22.0
P/B (x)	2.3	2.9	3.2	3.4	3.2
EV/EBITDA (x), adj.	12.8	14.4	16.7	18.5	17.4
Dividend Yield (%)	4.5%	3.7%	3.5%	3.2%	3.4%

Growth & Margins (%)

Growth					
Revenue	-1.9%	-3.1%	1.8%	-2.0%	2.5%
EBITDA	-0.8%	15.8%	6.7%	-1.2%	7.3%
EBIT	4.1%	20.6%	7.4%	-2.8%	8.6%
Net Income, adj.	7.0%	11.4%	7.4%	4.2%	9.5%
Margins					
EBITDA margin	14.0%	16.8%	17.6%	17.7%	18.6%
EBIT margin	10.2%	12.6%	13.3%	13.2%	14.0%
Net Profit Margin	11.2%	12.8%	13.5%	14.4%	15.4%

Key Ratios

ROE (%)	13.7%	14.9%	15.1%	15.0%	15.8%
ROA (%)	9.7%	10.6%	10.7%	10.6%	11.4%
Net Debt or (Net Cash)	(306)	(379)	(397)	(323)	(299)
Net Gearing (x)	Net Cash	Net Cash	Net Cash	Net Cash	Net Cash



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