

SATS Ltd

Good turnaround at various levels



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SINGAPORE | TRANSPORT SERVICES | 1Q19 RESULTS

- Revenue and PATMI exceeded our expectation by 6.8% and 5.7% respectively
- Revenue and PATMI met 25.7% and 25.3% respectively of our FY19 estimate
- Inflight kitchen JV with Turkish Airlines has been terminated
- Kunshan central kitchen turned profitable ahead of schedule
- MBCCS has turned profitable as well
- Maintain Accumulate; unchanged target price of \$5.58

Results at a glance

(SGD mn)	1Q19	1Q18	YoY	Comments
Revenue	439	427	3.0%	2.7% higher Food Solutions and 3.4% higher Gateway Services
EBIT	64.9	53.5	21.3%	0.4% higher expenditure; higher margin of 14.8% from 12.5%
Associates/JVs	15.3	15.5	-1.3%	\$0.8mn or 23.5% higher Food Solutions, \$1.0mn or 8.3% lower Gateway Services
PATMI	66.2	57.3	15.5%	Higher margin of 15.1% from 13.4%

Source: Company, PSR

The Positives

+ Higher Food Solutions (FS) revenue driven by higher meal volumes across the Group.

TFK Corp. (inflight kitchen subsidiary based in Tokyo) experienced a 3.1% YoY increase in revenue. However, the higher meal volumes was partially offset by lower pricing, as airline margins are still constrained by strong competition in Asia. Cost of raw ingredients is also expected to continue to increase. Raw materials cost was 10% higher YoY, despite FS revenue increasing by 2.7% YoY.

+ Higher Gateway Services (GS) revenue driven by both Aviation and Non-Aviation; and was the key driver to Group EBIT margin improvement.

There was an increase in air cargo tonnage and flights handled. In addition, the cruise terminal at Marina Bay Cruise Centre Singapore (MBCCS) benefitted from higher ship calls and increased passengers handled. Air cargo is a high operating leverage business which benefited from the higher volumes (better flow through to bottom line), while the cruise centre turned around to profit.

+ 16.9% YoY higher Non-Aviation revenue to S\$60.2 mn (13.7% of Group revenue).

This was due to revenue growth from the Kunshan central kitchen and MBCCS; both of which have turned profitable (refer to further details overleaf).

The Negatives

– Lower associates/JV contribution. This was due to a soft quarter in Indonesia for PT CAS and PT JAS, but partially mitigated by existing and new associates/JVs.

Outlook

The outlook is positive. Passenger volumes in Asia is expected to grow, given the backlog of aircraft on order and airport expansions across the region. MBCCS has turned around and ship calls are expected to be sustained. The Kunshan and Langfang central kitchens are poised to benefit from urbanisation and demand for safe, high-quality food. SATS has been investing in technology to boost productivity in anticipation of higher volumes, with staff cost (variable cost) progressively replaced by depreciation (fixed cost). Impact from a trade war that materialises is limited for now, but would be the key risk to earnings.

Maintain Accumulate; unchanged target price of \$5.58

We like the stock for its regional expansion story and growth initiatives. Our target price gives an implied FY19e forward P/E multiple of 24.7 times.

20 July 2018

Accumulate (Maintained)

LAST CLOSE PRICE	SGD 5.10
FORECAST DIV	SGD 0.180
TARGET PRICE	SGD 5.58
TOTAL RETURN	12.9%

COMPANY DATA

BLOOMBERG CODE:	SATS SP
O/S SHARES (MN):	117
MARKET CAP (USD mn / SGD mn):	4711 / 5718
52 - WK HI/LO (SGD):	5.85 / 4.55
3M Average Daily T/O (mn):	174

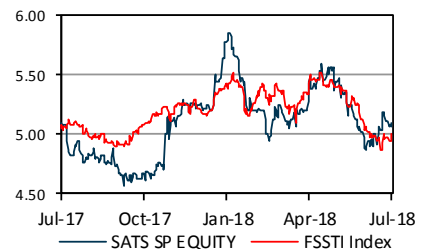
MAJOR SHAREHOLDER (%)

TEMASEK HOLDINGS PTE LTD	39.9%
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PRICE PERFORMANCE (%)

	1MTH	3MTH	1YR
COMPANY	2.0	(7.0)	3.8
STIRETURN	(2.5)	(7.6)	14

PRICE VS. STI



Source: Bloomberg, PSR

KEY FINANCIALS

Y / E Mar	FY 17	FY 18	FY 19e	FY 20e
Revenue (SGD mn)	1729	1725	1712	1746
PATMI, adj. (SGD mn)	234	236	253	271
EPS, adj. (cents)	211	211	22.6	24.3
P/E, adj. (x)	23.3	25.1	22.5	21.0
BVPS (cents)	150	157	162	170
P/B (x)	3.3	3.4	3.1	3.0
DPS (cents)	17.0	18.0	18.0	18.0
Div. Yield (%)	3.5	3.4	3.5	3.5

Source: Company Data, PSR est.

VALUATION METHOD

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

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Appendix

Here are the key takeaways from Management sharing of updates.

Mutual agreement to terminate Memorandum of Agreement for inflight catering JV with Turkish Airlines

- Istanbul New Airport will be opening in October and poses operational risks for participants in moving from Istanbul Atatürk Airport
- Turkish Airlines was not able to terminate its existing agreement with the incumbent caterer; so SATS has decided that it is not beneficial to proceed with the catering agreement
- Sunk costs such as travel expenses have been immaterial and were expensed in prior quarters, with no additional expenses to be expected

Marina Bay Cruise Centre Singapore (operator JV with Creuers del Port de Barcelona)

- Seasonal business, but Management has visibility over the next twelve months and is confident that volume will sustain for the rest of the year
- Cruise centre was losing money, but has now turned around with the increase in ship calls and margins have exceeded the Aviation Gateway segment
- About half of the improvement in Gateway Services EBIT was due to the improvement at the cruise terminal
- Singapore is an attractive cruise destination for its good weather, local itineraries, airport for people to fly in and marine maintenance facilities

Kunshan central kitchen on outskirts of Shanghai, China (JV with Yihai Kerry)

- Was expected to be profitable after three years, but has already turned profitable after two years of operations

Langfang central kitchen on outskirts of Beijing, China (recently announced JV with WI Kitchen, a subsidiary of Wilmar)

- Will carry out the exact same business as the Kunshan central kitchen – large scale food catering and developing menus for food service chains
- Catering of meals in small batches to sample at restaurants and tweak the taste before progressively ramping-up production
- Food/sauces will be delivered in bulk to customers' distribution centres and customers will use their own logistics supply chain to distribute to restaurants

Impact from possible trade war

- Air cargo business could be impacted; but so far no impact has been observed
- Nonetheless, SATS has low exposure to direct cargo between China and USA
- AAT (ground handler JV based in Hong Kong) has exposure to China

Financials

Income Statement

Y/E Mar, SGD mn	FY16	FY17	FY18	FY19e	FY20e
Revenue	1,698	1,729	1,725	1,712	1,746
EBITDA	285	304	305	307	324
Depreciation & Amortisation	(70)	(74)	(79)	(82)	(83)
EBIT	215	231	226	225	240
Net Finance (Expense)/Inc	2.4	3.4	3.3	2.5	2.2
Other items	2.2	9.9	20.7	-	-
Associates & JVs	48	65	71	85	93
Exceptional items	(2.1)	-	-	-	-
Profit Before Tax	265	309	322	313	335
Taxation	(47)	(48)	(56)	(50)	(53)
Profit After Tax	218	261	266	263	283
- Non-controlling interest	(2.2)	2.9	4.0	10.5	11.3
PATMI, reported	221	258	262	253	271
Underlying PATMI	218	234	236	253	271

Per share data (cents)

Y/E Mar	FY16	FY17	FY18	FY19e	FY20e
EPS, reported	19.9	23.2	23.4	22.6	24.3
EPS, adj.	19.7	21.1	21.1	22.6	24.3
DPS	15.0	17.0	18.0	18.0	18.0
BVPS	139	150	157	162	170

Cash Flow

Y/E Mar, SGD mn	FY16	FY17	FY18	FY19e	FY20e
CFO					
PBT	265	309	322	313	335
Adjustments	28	5	1	(6)	(12)
WC changes	17	38	(25)	12	(6)
Cash generated from ops	310	352	298	319	318
Others	(37)	(43)	(53)	(51)	(54)
Cashflow from ops	273	309	246	269	264
CFI					
CAPEX, net	(49)	(86)	(98)	(85)	(85)
Divd from associates & JVs	34	42	25	55	60
Others	(41)	(75)	(109)	(77)	(77)
Cashflow from investments	(56)	(120)	(182)	(106)	(102)
CFF					
Share issuance, net	(1.7)	4.3	(13.4)	-	-
Loans, net of repayments	0.4	(6.7)	(0.6)	(10.0)	(10.0)
Dividends	(156)	(179)	(192)	(201)	(201)
Others	0.5	8.7	8.8	-	-
Cashflow from financing	(157)	(173)	(197)	(211)	(211)
Net change in cash	60	17	(134)	(49)	(48)
Effects of exchange rates	0.6	2.0	(1.6)	-	-
CCE, end	490	508	373	325	277

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	FY16	FY17	FY18	FY19e	FY20e
ASSETS					
PPE	517	539	560	566	571
Intangibles	164	158	158	154	151
Associates & JVs	546	671	849	959	1,071
Others	50	56	47	47	47
Total non-current assets	1,276	1,423	1,613	1,726	1,840
Inventories	22	22	23	22	23
Accounts Receivables	277	271	299	282	295
Cash	490	506	373	325	277
Others	22	40	25	25	25
Total current assets	811	839	719	655	619
Total Assets	2,087	2,262	2,332	2,381	2,459
LIABILITIES					
Short term loans	110	10	10	10	10
Accounts Payables	309	331	332	328	335
Others	51	69	61	61	61
Total current liabilities	470	410	403	399	406
Long term loans	1	98	96	86	76
Others	70	80	83	83	83
Total non-current liabilities	70	178	179	169	159
Total Liabilities	541	588	582	568	565
EQUITY					
Non-controlling interest	74	88	133	143	154
Shareholder Equity	1,472	1,586	1,618	1,669	1,740

Valuation Ratios

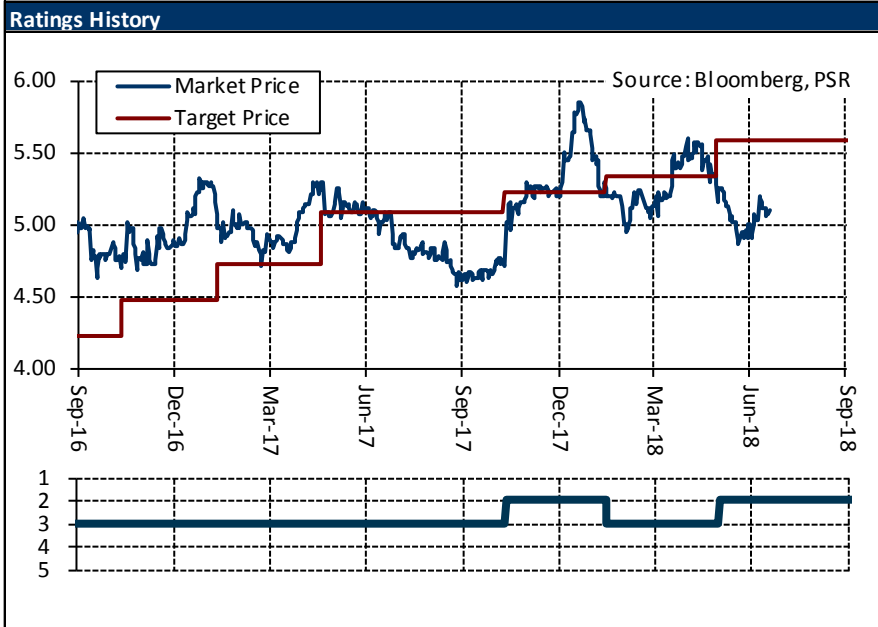
Y/E Mar	FY16	FY17	FY18	FY19e	FY20e
P/E (x), adj.	20.6	23.3	25.1	22.5	21.0
P/B (x)	2.9	3.3	3.4	3.1	3.0
EV/EBITDA (x), adj.	14.4	16.7	18.5	17.8	17.0
Dividend Yield (%)	3.7%	3.5%	3.4%	3.5%	3.5%

Growth & Margins (%)

Growth					
Revenue	-3.1%	1.8%	-0.3%	-0.8%	2.0%
EBITDA	15.8%	6.7%	0.3%	0.8%	5.3%
EBIT	20.6%	7.4%	-1.8%	-0.5%	6.6%
Net Income, adj.	11.4%	7.4%	0.8%	7.0%	7.4%
Margins					
EBITDA margin	16.8%	17.6%	17.7%	18.0%	18.5%
EBIT margin	12.6%	13.3%	13.1%	13.2%	13.8%
Net Profit Margin	12.8%	13.5%	13.7%	14.8%	15.5%

Key Ratios

ROE (%)	15.1%	15.3%	14.7%	15.4%	15.9%
ROA (%)	10.7%	10.8%	10.3%	10.7%	11.2%
Net Debt or (Net Cash)	(379)	(397)	(267)	(228)	(190)
Net Gearing (x)	Net Cash	Net Cash	Net Cash	Net Cash	Net Cash



PSR Rating System

Total Returns	Recommendation	Rating
> +20%	Buy	1
+5% to +20%	Accumulate	2
-5% to +5%	Neutral	3
-5% to -20%	Reduce	4
< -20%	Sell	5

Remarks
 We do not base our recommendations entirely on the above quantitative return bands. We consider qualitative factors like (but not limited to) a stock's risk reward profile, market sentiment, recent rate of share price appreciation, presence or absence of stock price catalysts, and speculative undertones surrounding the stock, before making our final recommendation

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