4 September 2019

Technology | Software & Services

CSE Global (CSE SP)

Buy (Maintained)

An Electrifying Acquisition; Keep BUY

Target Price (Return)	SGD0.69 (+52%)
Price:	SGD0.455
Market Cap:	USD165m
Avg Daily Turnover (SGD/USD)	0.3m/0.2m

- **Keep BUY with a new DCF-backed SGD0.69 TP from SGD0.61, 52% upside plus c.6% yield.** CSE Global has acquired 100% of Volta – a custom-engineered electrical equipment centres solutions provider – for USD25.1m (SGD34.8m). Volta's net PBT for FY18 was USD4.9m (SGD6.9m) Based on our estimation, this acquisition should add SGD7.8-8.4m and SGD4-4.5m to CSE Global's EBIT and PATMI on an annualised basis. As such, we lift our FY20F-21F earnings 15-17% to SGD29.4m and SGD30.8m.
- **A complementary acquisition.** Volta operates in the oil & gas industry in the US. It provides integration services that deals with power distribution equipment, such as switchgears and motor control centres among others. This is seen as a complementary buy for CSE Global. We understand the latter has partnered with Volta on past projects and, despite the scope and solutions provided being different, the two companies are adjacent to one another. Furthermore, Volta generates a majority of its revenue from the midstream oil & gas sector. This acquisition will allow CSE Global to tap onto Volta's existing network and expand into this midstream space.
- **Accretive acquisition**. For a price tag of SGD34.8m – based on a FY18 net profit before tax of SGD6.9m – this translates into c.6.7x P/E (NPAT), which is highly accretive in nature. However, CSE Global is likely to gear up as a result of the purchase. If we assume the group will undertake the acquisition fully funded by debt, the PAT should be SGD4.1m due to the additional financing costs. This will translate into ~8.4x P/E – which is still an undemanding valuation – and a net gearing ratio of 20% at group level. We understand the business has a good cash flow position – hence, the debt should be taken care of by itself.
- **Acquisition of two properties in the US.** CSE Global has also acquired 100% interest in Volta Properties, which houses two properties, for an aggregate consideration of USD17m (SGD23.6m). These properties are occupied by the newly-acquired subsidiary Volta. The purchase will be funded by both internal funds and bank borrowings. We do not expect the addition to have any material impact to CSE Global's profit & loss statement. However, coupled with the acquisition of Volta, we estimate net gearing at 33%, up from a net cash position previously.
- **We keep our call with a higher DCF-backed TP of SGD0.69,** implying only 11.9x FY20F P/E. CSE Global is currently trading at 9.5x FY19F P/E, with an attractive yield of 6%. Key downside risks include oil price volatility, an economic slowdown, FX risks, declining orders intake, lower margins, and execution risks.

Forecasts and Valuation	Dec-17	Dec-18	Dec-19F	Dec-20F	Dec-21F
Total turnover (SGDm)	362.4	376.8	420.4	476.7	490.9
Recurring net profit (SGDm)	13.3	20.1	24.4	29.4	30.8
Recurring net profit gr (%)	(37.3)	51.2	21.2	20.8	4.4
Recurring P/E (x)	17.4	11.5	9.5	7.8	7.5
P/BV (x)	1.3	1.3	1.3	1.2	1.1
P/CF (x)	na	4.9	31.1	7.0	5.9
Dividend Yield (%)	6.0	6.0	6.0	6.0	6.0
EV/EBITDA (x)	(7.3)	5.6	7.3	5.5	5.0
ROE (%)	7.6	11.7	13.9	15.4	14.8
Net debt to equity (%)	net cash	net cash	33.1	24.5	14.3
Interest coverage (x)	na	31.9	21.4	16.4	22.3

Source: Company data, RHB

Analysts



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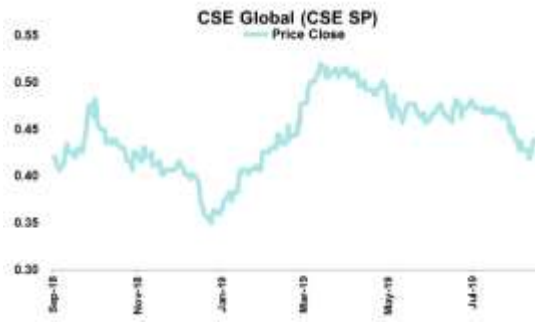


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Share Performance (%)

	YTD	1m	3m	6m	12m
Absolute	19.7	0.0	(4.2)	(9.9)	3.4
Relative	19.0	5.2	(3.2)	(5.9)	7.0

52-wk Price low/high (SGD) 0.37 – 0.56



Source: Bloomberg

Financial Exhibits

Asia

Singapore

Technology

CSE Global

Bloomberg CSE SP

Buy

Valuation basis

DCF-derived TP of SGD0.69 with WACC of 8.4%

Key drivers

i. Elevated oil prices provide potential opportunities;
ii. Strong track record;
iii. Potential acquisitions to fuel growth;
iv. Strong cash flow generation with a solid balance sheet.

Key risks

i. Execution risks;
ii. Unsustainable oil price;
iii. Foreign currency risk;
iv. Legislative issues;
v. Credit risk;
vi. Shortage of talent;
vii. Declining orders intake.

Company Profile

CSE Global is a leading systems integrator that focuses on the provision and installation of a variety of control systems, as well as turnkey telecommunication network and security solutions. It targets the oil & gas, infrastructure, and mining industries.

Financial summary	Dec-17	Dec-18	Dec-19F	Dec-20F	Dec-21F
Core EPS (SGD)	0.03	0.04	0.05	0.06	0.06
EPS (SGD)	-0.09	0.04	0.05	0.06	0.06
DPS (SGD)	0.03	0.03	0.03	0.03	0.03
BVPS (SGD)	0.32	0.34	0.35	0.38	0.41
ROE (%)	7.6	11.7	13.9	15.4	14.8
ROA (%)	-16.5	7.2	7.1	8.8	9.3

Valuation metrics	Dec-17	Dec-18	Dec-19F	Dec-20F	Dec-21F
Core P/E (x)	17.4	11.5	9.5	7.8	7.5
P/B (x)	1.4	1.4	1.3	1.2	1.1
Dividend yield (%)	6.0	6.0	6.0	6.0	6.0
EV/EBITDA (x)	-7.3	5.6	7.3	5.5	5.0

Income statement (SGDm)	Dec-17	Dec-18	Dec-19F	Dec-20F	Dec-21F
Total turnover	362	377	420	477	491
Gross profit	94	105	113	124	128
EBITDA (adj.)	-30	34	40	50	52
Depreciation & amortisation	-37	27	31	41	42
Operating profit	0	-1	-1	-2	-1
Net interest	-60	0	-1	0	0
Pre-tax profit	-37	26	30	39	41
Taxation	-9	-7	-7	-10	-10
Net profit	-47	19	23	29	31
Recurring net profit	13	20	24	29	31

Cash flow (SGDm)	Dec-17	Dec-18	Dec-19F	Dec-20F	Dec-21F
Change in working capital	-23	47	7	33	39
Cash flow from operations	-8	-7	-35	-8	-8
Capex	-10	-7	-85	-8	-8
Cash flow from investing activities	-4	-13	37	-24	-34
Dividends paid	91	47	74	33	34
Cash flow from financing activities	-37	27	-41	1	-3
Cash at beginning of period	47	74	33	34	31
Net change in cash	-23	47	7	33	39
Ending balance cash	-8	-7	-35	-8	-8

Balance sheet (SGDm)	Dec-17	Dec-18	Dec-19F	Dec-20F	Dec-21F
Total cash and equivalents	47	74	33	34	31
Tangible fixed assets	28	28	56	56	56
Intangible assets	28	26	45	43	41
Total investments	1	1	31	31	31
Total other assets	180	139	156	168	171
Total assets	284	269	320	333	331
Short-term debt	31	36	36	36	36
Total long-term debt	0	0	55	45	25
Total liabilities	108	97	145	141	123
Shareholders' equity	174	171	176	191	208
Minority interests	2	1	0	0	0
Total equity	176	172	176	191	208
Total liabilities & equity	284	269	320	333	331

Key metrics	Dec-17	Dec-18	Dec-19F	Dec-20F	Dec-21F
Revenue growth (%)	14	4	12	13	3
Core net profit growth (%)	-37	51	21	21	4
Core EPS growth (%)	-37	52	22	21	4
Gross margin (%)	26	28	27	26	26
Core net profit margin (%)	4	5	6	6	6
Dividend payout ratio (%)	107	70	57	47	45

Source: Company data, RHB

According to CSE Global's announcement on the SGX, Volta is a Texas limited liability company founded in Houston by Bradley Davis in Apr 2005. The company develops, designs, manufactures, and services custom-engineered electrical equipment centres (EECs) that:

i. Distribute, control, and monitor the flow of electrical energy;

ii. Provide protection to motors, transformers, and other electrically powered equipment.

Volta's integration services cover a broad variety of power distribution equipment, including switchgears, motor control centres, and auxiliary equipment. The company integrates all equipment within an EEC to exactly match customer specifications – providing them with the product that fits their unique needs.

Volta currently employs 120 full-time regular employees and an additional 62 full-time people on contract basis.

The seller of Volta Properties is the aforementioned Davis, an independent third party unrelated to any of the directors, substantial shareholders or controlling shareholders, or their respective associates – as defined under the SGX's Listing Manual – of CSE Global. As at the date of this announcement, the seller does not have any shareholding interests, direct or indirect, in the group.

Volta Properties owns 100% interest in two properties at 1616 Gears Road and 1702 Gears Road, both in Houston, Texas. Volta Properties is a Texas limited liability company that leases land, offices and warehouses to Volta. The properties have a land area of 16.7 acres.

Figure 1: CSE Global's DCF valuation

FYE Dec	Total (SGDm)	FY20F	FY21F	FY22F	FY23F	Terminal value
EBIT		41.3	42.3	44.0	46.3	
EBIT(1-T)		**31.0**	**31.8**	**33.1**	**34.8**	
Less: Capex		(7.9)	(7.9)	(7.9)	(7.9)	
Add: Depreciation & amortisation		9.2	9.7	10.3	10.9	
Less: Change in non-cash WC		(5.5)	(1.5)	(1.5)	(2.4)	
FCFF		**26.8**	**32.2**	**34.1**	**35.4**	**419.6**
Present value of FCFF		24.8	27.3	26.7	25.6	303.5
Total FCFF	**407.9**					
Add: Cash	32.8					
Less: Value of debt	(90.9)					
Less: Minority interest	-					
Target equity value	**349.8**					
No. of shares (basic)	508					
Intrinsic share price (SGD)	**0.69**					

Source: Company data, RHB

Figure 2: CSE Global's WACC

Cost of Equity		Cost of Debt	
Expected market return	11%	Pre-Tax Cost of Debt	3%
Risk free	2.5%	1 - Effective Tax Rate	75%
Beta	1	Weight	34%
Weight	66%		
WACC (estimated)	**8.4%**		

Source: RHB

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