

8 April 2024

Industrials | Aerospace & Defence

## ST Engineering (STE SP)

**Buy** (Maintained)

Updated ESG Data; Unchanged Positive Thesis; BUY

Target Price (Return): SGD4.50 (12.8%)  
 Price (Market Cap): SGD3.99 (USD9,248m)  
 ESG score: 3.3 (out of 4)  
 Avg Daily Turnover (SGD/USD) 15.0m/11.7m

- **Reiterate BUY with SGD4.50 TP, 13% upside, c.4% yield.** We reiterate our positive outlook on ST Engineering, which still has defensive dividends at SGD0.04 per quarter, and strong earnings growth as all business segments witness robust growth. The Commercial Aerospace (CA) segment should see continued growth and margin improvement, while Urban Solutions and Satcom (USS) should see a strong recovery. We estimate a 15% profit CAGR for 2023–2026.
- **Unchanged positive investment thesis.** STE's earnings outlook remains defensive. Its order backlog of SGD27.4bn implies a book-to-bill ratio of 2.7 years. STE expects SGD7.9bn of the orderbook to be delivered in 2024, accounting for 73% of our 2024F revenue estimate. We expect STE to continue paying SGD0.04 per quarter in dividends. We also expect near-term earnings growth to remain strong as its CA business benefits from higher MRO earnings on the back of better aviation traffic, higher nacelle sales, and improved profits for its passenger-to-freighter (PTF) conversion business amidst economies of scale and improvements in the learning curve. The USS unit's earnings should improve as a result of the right-sizing exercise and earnings contribution from its TransCore acquisition. The Defence & Public Security (DPS) business' profitability should be supported by the gradual delivery of its orderbook. A potential decline in interest rates would be positive, as 38% of STE's debt is still exposed to a floating interest rate.
- **2023 sustainability report.** STE achieved a 36% reduction in Scope 1 and 2 greenhouse gas (GHG) emissions over the 2010 base year (2022: 37% reduction, 2030 target: 50% reduction). Total emissions rose 4.9% YoY on the back of higher economic output. However, GHG intensity as a measure of revenue (for its Singapore operations) has been on a consistent decline since 2020. Direct energy consumption saw a 15% YoY decline, while total waste generated fell 22% YoY. However, waste recycling fell to 67% from 75% in 2022. On the social front, most metrics were unchanged, except for the increase in the average number of training hours per employee, which rose 33%. However, the amount contributed to the community declined in absolute terms and also as a percentage of revenue. We also noted a YoY percentage reduction in the number of independent directors on the board. However, the percentage of female directors is on the rise and stands at 23%.
- **No change to estimates; ESG impact on our valuation.** In our ESG analysis, we reduced the score for board independence by one point. However, our overall ESG score remains at 3.3. Our TP includes a 4% ESG premium over the fair value of SGD4.32 as STE's ESG score is two points above the 3.1 country median.

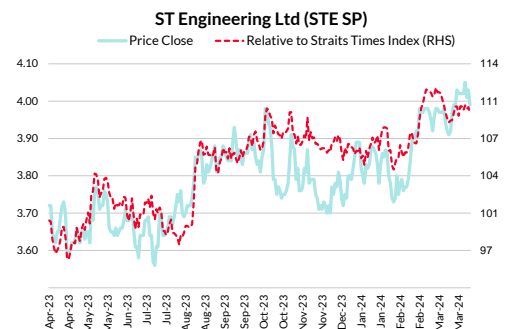
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### Share Performance (%)

	YTD	1m	3m	6m	12m
Absolute	2.6	1.8	5.6	4.2	7.3
Relative	3.3	(1.8)	4.5	2.2	10.3
52-wk Price low/high (SGD)	3.56 – 4.05				



Source: Bloomberg

### Overall ESG Score: 3.3 (out of 4)

#### E: GOOD

In 2023, it reported a 36% reduction in absolute Scope 1 and 2 emissions over the 2010 base year and is on track to meet its target of achieving a 50% reduction in absolute Scope 1 and 2 emissions by 2030 compared to the 2010 base year.

#### S: EXCELLENT

STE serves its communities through a combination of volunteer work and skills-based contributions, as well as in-kind and monetary support. In 2023, it contributed SGD2.3m to community causes. STE promotes the professional and personal development of its employees, as seen by the increase in the average number of training hours per employee.

#### G: EXCELLENT

Despite having exposure to the defence business, STE does not design, produce, or sell anti-personnel mines, cluster munitions, white phosphorus munitions, or their related key components. STE's board comprises 13 directors, of whom 7 are independent (54%), and 3 are female (23%).

Forecasts and Valuation	Dec-22	Dec-23	Dec-24F	Dec-25F	Dec-26F
Total turnover (SGDm)	9,035	10,101	10,876	11,715	12,644
Recurring net profit (SGDm)	482	612	713	840	926
Recurring net profit growth (%)	(15.5)	26.9	16.6	17.7	10.3
Recurring P/E (x)	25.77	20.31	17.42	14.80	13.41
P/B (x)	5.2	5.1	4.7	4.2	3.6
P/CF (x)	18.46	10.54	9.53	8.41	8.60
Dividend Yield (%)	5.5	4.0	4.0	4.0	4.0
EV/EBITDA (x)	15.75	13.37	12.04	10.59	9.73
Return on average equity (%)	22.2	24.1	27.8	29.5	28.7
Net debt to equity (%)	223.6	209.1	192.1	159.1	127.9

Source: Company data, RHB

## Financial Exhibits

<b>Asia</b>	<b>Financial summary (SGD)</b>	<b>Dec-22</b>	<b>Dec-23</b>	<b>Dec-24F</b>	<b>Dec-25F</b>	<b>Dec-26F</b>
Singapore	Recurring EPS	0.15	0.20	0.23	0.27	0.30
Industrials	DPS	0.22	0.16	0.16	0.16	0.16
<b>ST Engineering</b>	BVPS	0.77	0.79	0.85	0.96	1.10
STE SP	Return on average equity (%)	22.2	24.1	27.8	29.5	28.7
Buy						
	<b>Valuation metrics</b>	<b>Dec-22</b>	<b>Dec-23</b>	<b>Dec-24F</b>	<b>Dec-25F</b>	<b>Dec-26F</b>
<b>Valuation basis</b>	Recurring P/E (x)	25.77	20.31	17.42	14.80	13.41
Our TP is derived by using an average of forward P/E, P/BV, EV/EBITDA and DCF of adjusted free cash flows.	P/B (x)	5.2	5.1	4.7	4.2	3.6
	FCF Yield (%)	(0.6)	7.2	5.3	8.3	8.6
	Dividend Yield (%)	5.5	4.0	4.0	4.0	4.0
	EV/EBITDA (x)	15.75	13.37	12.04	10.59	9.73
	EV/EBIT (x)	28.01	21.99	19.02	16.35	14.91
<b>Key drivers</b>	<b>Income statement (SGDm)</b>	<b>Dec-22</b>	<b>Dec-23</b>	<b>Dec-24F</b>	<b>Dec-25F</b>	<b>Dec-26F</b>
i. Strong order wins;	Total turnover	9,035	10,101	10,876	11,715	12,644
ii. Contributions from acquisitions.	Gross profit	1,699	1,973	2,215	2,446	2,630
	EBITDA	1,181	1,382	1,531	1,705	1,812
	Depreciation and amortisation	(517)	(541)	(562)	(600)	(629)
	Operating profit	665	840	970	1,105	1,183
	Net interest	(138)	(210)	(209)	(203)	(189)
	Pre-tax profit	597	704	875	1,030	1,137
	Taxation	(54)	(100)	(140)	(165)	(182)
	Reported net profit	535	586	713	840	926
	Recurring net profit	482	612	713	840	926
<b>Key risks</b>	<b>Cash flow (SGDm)</b>	<b>Dec-22</b>	<b>Dec-23</b>	<b>Dec-24F</b>	<b>Dec-25F</b>	<b>Dec-26F</b>
i. Slower revival in commercial aerospace sector;	Change in working capital	(442)	(101)	(205)	(192)	(332)
ii. Lower-than-expected contribution from acquisitions;	Cash flow from operations	673	1,179	1,304	1,478	1,445
iii. Delay in the implementation of Singapore's smart nation initiative.	Capex	(743)	(279)	(650)	(450)	(380)
	Cash flow from investing activities	(4,571)	(201)	(582)	(371)	(290)
	Dividends paid	(686)	(499)	(498)	(498)	(498)
	Cash flow from financing activities	3,698	(1,226)	(810)	(1,003)	(1,091)
	Cash at beginning of period	816	602	353	265	368
	Net change in cash	(201)	(248)	(89)	104	64
	Ending balance cash	602	353	265	368	432
<b>Company Profile</b>	<b>Balance sheet (SGDm)</b>	<b>Dec-22</b>	<b>Dec-23</b>	<b>Dec-24F</b>	<b>Dec-25F</b>	<b>Dec-26F</b>
ST Engineering (STE) is an integrated engineering group in the aerospace, electronics, land systems and marine sectors. The company has over the years, diversified its businesses and geographical coverage.	Total cash and equivalents	602	353	265	368	432
	Tangible fixed assets	2,076	2,076	2,358	2,401	2,344
	Total investments	468	567	499	421	331
	Total assets	14,964	15,379	15,609	15,775	15,822
	Short-term debt	3,628	2,564	0	0	0
	Total long-term debt	2,907	3,544	6,008	5,708	5,308
	Total liabilities	12,311	12,627	12,620	12,419	12,010
	Total equity	2,653	2,752	2,989	3,356	3,813
	Total liabilities & equity	14,964	15,379	15,609	15,775	15,822
	<b>Key metrics</b>	<b>Dec-22</b>	<b>Dec-23</b>	<b>Dec-24F</b>	<b>Dec-25F</b>	<b>Dec-26F</b>
	Revenue growth (%)	17.4	11.8	7.7	7.7	7.9
	Recurrent EPS growth (%)	(15.5)	26.9	16.5	17.7	10.3
	Gross margin (%)	18.8	19.5	20.4	20.9	20.8
	Operating EBITDA margin (%)	13.1	13.7	14.1	14.6	14.3
	Net profit margin (%)	5.9	5.8	6.6	7.2	7.3
	Dividend payout ratio (%)	128.2	85.0	69.9	59.3	53.8
	Capex/sales (%)	8.2	2.8	6.0	3.8	3.0
	Interest cover (x)	4.47	3.34	4.40	5.16	5.83

Source: Company data, RHB

## Emissions And ESG

### Trend analysis

Although overall emissions have been on the rise on the back of rising economic output, during 2020–2023, STE has reduced GHG intensity as a measure of revenue for its Singapore operations to 10.99 tCO<sub>2</sub>e/SGDm in 2023 from 16.34 tCO<sub>2</sub>e/SGDm in 2020 and 14.82 tCO<sub>2</sub>e/SGDm in 2021.

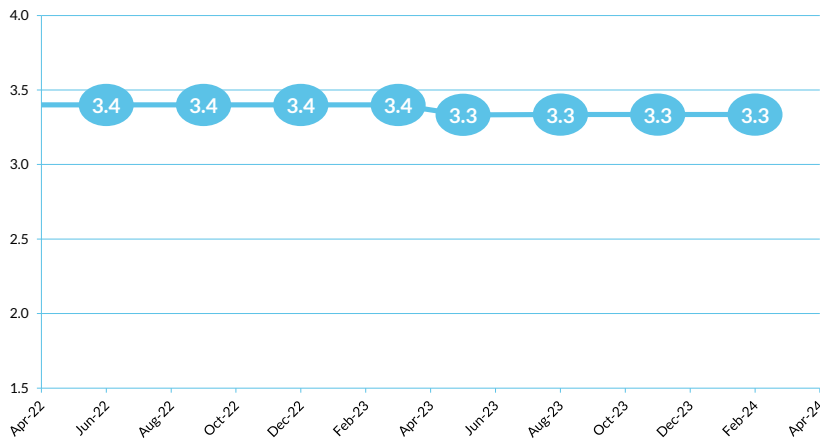
Emissions (tCO <sub>2</sub> e)	Dec-21	Dec-22	Dec-23
Scope 1	36,000	39,000	37,000
Scope 2	78,000	71,000	74,000
Scope 3	1,900	33,000	39,000
Total emissions	115,900	143,000	150,000

Source: Company data, RHB

## Latest ESG-Related Developments

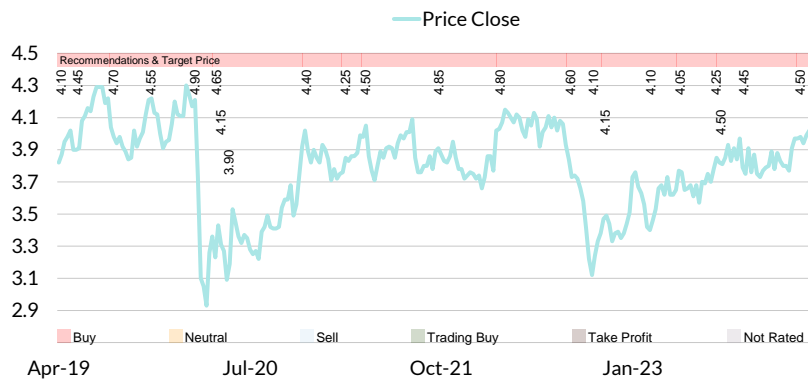
- In 2021, STE set a target to halve its absolute Scope 1 and Scope 2 GHG emissions by 2030 compared to a 2010 base year. In the same year, it also set a target to increase its sustainability-linked revenue to more than SGD3bn by 2026.
- In 2022, STE was included in the Dow Jones Sustainability Asia Pacific Index as identified by S&P Global through the Corporate Sustainability Assessment. It is also a component stock of the iEdge SG ESG Transparency Index and the iEdge SG ESG Leaders Index.
- In 2023, STE implemented an internal shadow carbon price on major capital expenditure, established roadmaps, and embarked on the development of a product carbon footprint for its major products and services.

## ESG Rating History



Source: RHB

## Recommendation Chart



Source: RHB, Bloomberg

Date	Recommendation	Target Price	Price
2024-03-04	Buy	4.50	3.95
2024-02-21	Buy	4.50	3.92
2023-10-23	Buy	4.45	3.75
2023-10-09	Buy	4.45	3.81
2023-08-14	Buy	4.50	3.85
2023-08-02	Buy	4.25	3.70
2023-05-08	Buy	4.05	3.65
2023-02-27	Buy	4.10	3.54
2023-01-18	Buy	4.15	3.45
2022-11-08	Buy	4.15	3.33
2022-10-11	Buy	4.10	3.34
2022-09-23	Buy	4.60	3.66
2022-08-15	Buy	4.60	4.00
2022-02-27	Buy	4.80	3.77
2021-10-04	Buy	4.85	3.88

Source: RHB, Bloomberg

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<b>Buy:</b>	Share price may exceed 10% over the next 12 months
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<b>Not Rated:</b>	Stock is not within regular research coverage

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