

18 October 2023

Consumer Cyclical | Gaming

Sports Toto (SPTOTO MK)

Neutral (Maintained)

Taxing Times Ahead

- **Stay NEUTRAL, with new DCF-derived MYR1.55 TP from MYR1.61, 4% upside.** The service tax hike in Budget 2024 was an unexpected setback for the gaming industry. We cut our forecasts accordingly to reflect the increased overall tax burden. While ticket sales are on the rise and inching to pre-pandemic levels, we believe the current at mean valuation is fair and that the market has already factored in the recovery in ticket sales. That said, the stock currently offers an attractive c.7% yield. This report marks the transfer of coverage to Tai Yu Jie.
- **Service tax hike.** In Budget 2024, Prime Minister Dato' Seri Anwar Ibrahim announced that the Government will raise the service tax rate by 2ppts, from 6% to 8%. Given gaming services fall under the taxable category of the Service Tax Act of 2018, this adjustment essentially represents an additional tax burden for the NFOs. However, the quantum is 1-2% of gross sales as the net payable service tax is net of gaming tax, pool betting duty and payout. Note that the NFOs have been absorbing these taxes since the implementation of the Goods and Services Tax (GST) in 2015 and also the service tax continues to apply to the gaming industry following the widening of scope and re-implementation of Sales & Service Tax (SST) in 2018.
- **Impact to earnings.** We understand that reducing the prize payout may not be an ideal strategy nor raising ticket prices as these could potentially lead to decreased sales and a loss of market share to illegal NFOs. Considering the higher tax rate, we cut our FY24F-25F (Jun) earnings by 4-5%, assuming that SPTOTO absorbs all the incremental cost without increasing the ticket price or lowering the prize payout. We also note that while NFOs are eagerly awaiting stricter regulations against illegal operators and the legalisation of online gaming, we believe these policies are currently not a top priority for the Government.
- **Headwinds ahead for HR Owen.** Given the persistently high inflation in the UK (August CPI: +6.7% YoY), HR Owen's margins may continue to face pressure due to rising energy costs, wages, and stock-borrowing expenses. Additionally, the launch of its Hatfield showroom could lead to increased depreciation and higher interest expenses, which are expected to impact FY24F – potentially affecting HR Owen's profitability. That said, SPTOTO's dividends are primarily derived from its lottery business. Hence, the challenges at HR Owen are unlikely to hamper the company's dividend recovery.
- **Keep NEUTRAL.** Post earnings cut, our DCF-derived TP is lowered to MYR1.55 (inclusive of a 2% ESG premium). Our TP implies 11.4x FY24F P/E (close to its mean), or at a slight discount to its closest peer Magnum (MAG MK, NEUTRAL, TP: MYR1.14) to account for its challenging operating environment in the UK (through HR Owen). Key downside risks include unfavourable luck factor, unfavourable policies, and softer-than-expected ticket sales. The converse represents the upside risks.

Forecasts and Valuation	Jun-22	Jun-23	Jun-24F	Jun-25F	Jun-26F
Total turnover (MYRm)	5,229	6,100	5,557	5,716	5,879
Recurring net profit (MYRm)	162	217	184	193	197
Recurring net profit growth (%)	(7.1)	33.9	(15.3)	5.2	1.8
Recurring P/E (x)	12.42	9.28	10.96	10.42	10.23
P/B (x)	2.2	1.9	2.0	1.9	1.9
P/CF (x)	4.96	na	3.22	6.64	6.52
Dividend Yield (%)	5.8	6.0	7.0	8.1	8.4
EV/EBITDA (x)	6.36	6.12	6.12	5.83	5.54
Return on average equity (%)	18.9	22.6	17.6	18.8	18.6
Net debt to equity (%)	71.6	79.0	68.5	66.6	60.8

Source: Company data, RHB

Target Price (Return): MYR1.55 (+4%)
 Price (Market Cap): MYR1.49 (USD416m)
 ESG score: 3.1 (out of 4)
 Avg Daily Turnover (MYR/USD) 1.50m/0.33m

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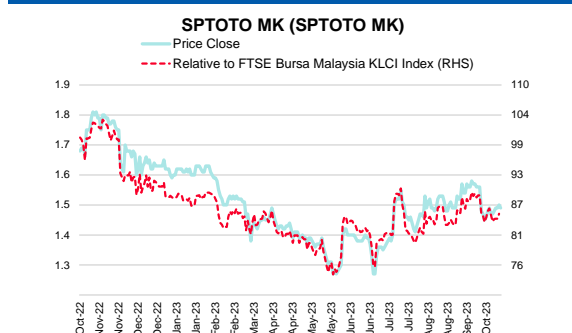


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Share Performance (%)

	YTD	1m	3m	6m	12m
Absolute	(8.0)	(3.3)	(0.7)	3.5	(11.3)
Relative	(4.2)	(1.9)	(3.0)	3.2	(15.1)
52-wk Price low/high (MYR)				1.27	1.81



Source: Bloomberg

Overall ESG Score: 3.1 (out of 4)

E: EXCELLENT

The lottery industry generally has low environmental risks. Nevertheless, the group continues to contribute to environmental sustainability by implementing a few initiatives including the usage of recycled paper and energy-saving practices across its premises

S: GOOD

The group is committed to promoting responsible gaming, to prevent both excessive and underage gaming. In terms of employee health and safety, it adopts the best practices in providing a conducive and safe working environment. The group also engages in social activities that contribute to various communities.

G: GOOD

The group has applied and adopted most of the best practices of the Malaysian Code on Corporate Governance. Nevertheless, we note that independent directors comprise less than half of the board, and it has yet to achieve the target of having 30% of women on the board.

Note:

Small cap stocks are defined as companies with a market capitalisation of less than USD0.5bn.

Financial Exhibits

Asia	Financial summary (MYR)	Jun-22	Jun-23	Jun-24F	Jun-25F	Jun-26F
Malaysia	Recurring EPS	0.12	0.16	0.14	0.14	0.15
Consumer Cyclical	DPS	0.09	0.09	0.11	0.12	0.13
Sports Toto	BVPS	0.66	0.79	0.75	0.77	0.79
SPTOTO MK	Return on average equity (%)	18.9	22.6	17.6	18.8	18.6
Neutral						
	Valuation metrics	Jun-22	Jun-23	Jun-24F	Jun-25F	Jun-26F
Valuation basis	Recurring P/E (x)	12.42	9.28	10.96	10.42	10.23
DCF	P/B (x)	2.2	1.9	2.0	1.9	1.9
	FCF Yield (%)	13.3	(10.3)	27.6	11.6	11.9
Key drivers	Dividend Yield (%)	5.8	6.0	7.0	8.1	8.4
i. Ticket sales;	EV/EBITDA (x)	6.36	6.12	6.12	5.83	5.54
ii. Luck factor.	EV/EBIT (x)	7.81	7.36	7.61	7.36	7.09
Key risks	Income statement (MYRm)	Jun-22	Jun-23	Jun-24F	Jun-25F	Jun-26F
Key downside risks include:	Total turnover	5,229	6,100	5,557	5,716	5,879
i. Unfavourable luck factor;	Gross profit	853	1,006	922	955	988
ii. Unfavourable policies;	EBITDA	387	428	397	414	428
iii. Softer-than-expected ticket sales.	Depreciation and amortisation	(72)	(72)	(78)	(86)	(94)
	Operating profit	315	356	319	328	335
The converse represents the upside risks.	Net interest	(64)	(57)	(51)	(46)	(43)
	Pre-tax profit	273	337	276	290	300
Company Profile	Taxation	(103)	(110)	(88)	(93)	(99)
Sports Toto is one of the largest number forecast operators in Malaysia. It also has a presence in the Philippines' gaming market.	Reported net profit	161	222	184	193	197
	Recurring net profit	162	217	184	193	197
	Cash flow (MYRm)	Jun-22	Jun-23	Jun-24F	Jun-25F	Jun-26F
	Change in working capital	3	(491)	304	(32)	(33)
	Cash flow from operations	406	(138)	625	303	309
	Capex	(138)	(70)	(70)	(70)	(70)
	Cash flow from investing activities	(113)	(70)	(70)	(70)	(70)
	Dividends paid	(47)	(122)	(142)	(162)	(169)
	Cash flow from financing activities	29	(301)	(281)	(297)	(300)
	Cash at beginning of period	364	559	621	510	442
	Net change in cash	322	(509)	273	(64)	(61)
	Ending balance cash	674	49	894	446	381
	Balance sheet (MYRm)	Jun-22	Jun-23	Jun-24F	Jun-25F	Jun-26F
	Total cash and equivalents	559	621	510	442	384
	Tangible fixed assets	555	846	472	456	432
	Total investments	301	367	410	435	438
	Total assets	3,113	3,891	3,123	3,112	3,084
	Short-term debt	280	562	300	300	300
	Total long-term debt	964	959	960	900	800
	Total liabilities	2,156	2,752	2,028	1,974	1,906
	Total equity	957	1,139	1,095	1,138	1,177
	Total liabilities & equity	3,113	3,891	3,123	3,112	3,084
	Key metrics	Jun-22	Jun-23	Jun-24F	Jun-25F	Jun-26F
	Revenue growth (%)	8.3	16.6	(8.9)	2.9	2.9
	Recurrent EPS growth (%)	(7.1)	33.9	(15.3)	5.2	1.8
	Gross margin (%)	16.3	16.5	16.6	16.7	16.8
	Operating EBITDA margin (%)	7.4	7.0	7.1	7.3	7.3
	Net profit margin (%)	3.1	3.6	3.3	3.4	3.3
	Dividend payout ratio (%)	73.1	54.8	77.2	83.9	85.8
	Capex/sales (%)	2.6	1.1	1.3	1.2	1.2
	Interest cover (x)	4.84	4.46	5.36	5.94	6.57

Source: Company data, RHB

Figure 1: DCF valuation

FYE Dec	FY23F	FY24F	FY25F	FY26F	FY27F	FY28F	FY29F	FY30F	FY31F	FY32F
EBIT	319.2	328.1	334.7	335.5	334.5	333.8	335.4	337.0	338.0	336.4
EBIT*(1-tax rate)	217.0	223.1	224.3	224.8	224.1	223.6	224.7	225.8	226.5	225.4
Add: D&A	77.7	86.3	93.7	101.3	109.2	117.4	125.8	134.5	143.5	152.7
Less: WC investments (WC Inv)	303.7	-31.8	-33.2	-29.9	-29.4	-23.6	-26.7	-27.0	-28.9	-27.8
Less: Fixed investments (FC Inv)	-70.0	-70.0	-70.0	-70.0	-70.0	-70.0	-70.0	-70.0	-70.0	-70.0
FCFF	528.5	207.6	214.7	226.2	233.9	247.4	253.8	263.3	271.0	280.3
Disc. FCFF	479.1	170.6	160.0	152.8	143.2	137.3	127.7	120.1	112.1	105.1
Terminal value at T=10	2871									
PV of terminal value	1076									
NPV	1706									
Less Debt	-750									
Less Minority Interest	-74									
Equity Value of Firm	2884									
ESG premium/discount	2%									
Fair Value per share	1.55									
Implied FY24F P/E	11.4									
Rf	4.0%									
Beta	1.3									
Risk premium	7.9%									
Rm	11.9%									
TG (%)	0.5%									
CoE	14.2%									
CoD	6.5%									
WACC	10.3%									

Source: RHB

Recommendation Chart

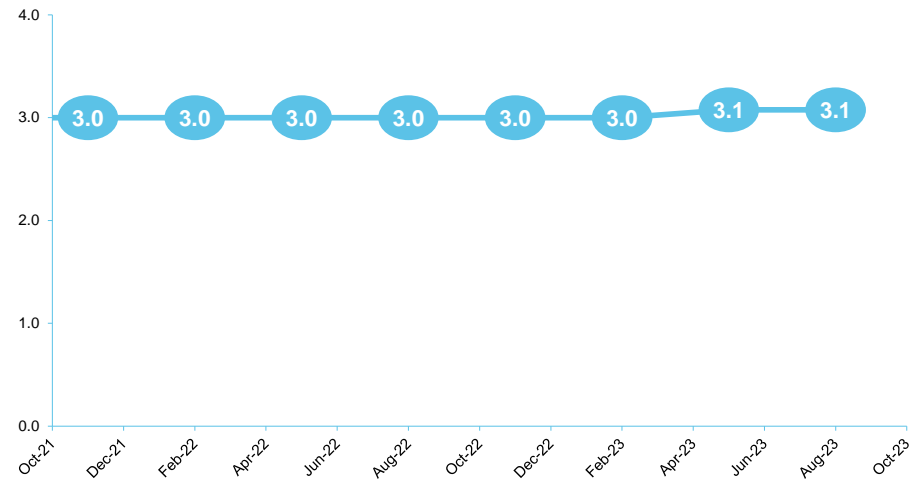


Source: RHB, Bloomberg

Date	Recommendation	Target Price	Price
2023-08-24	Neutral	1.61	1.53
2023-05-24	Neutral	1.42	1.27
2023-04-05	Neutral	1.42	1.43
2023-02-23	Buy	1.75	1.53
2022-12-06	Buy	2.07	1.62
2022-11-24	Buy	2.10	1.70
2022-08-24	Buy	2.10	1.83
2022-08-24	Buy	2.23	1.83
2022-06-01	Buy	2.23	1.88
2022-05-24	Buy	2.20	1.92
2022-04-06	Buy	2.39	1.95
2022-02-23	Buy	2.39	1.90
2021-11-19	Buy	2.34	1.94
2021-11-15	Buy	2.34	2.03
2021-11-09	Buy	2.34	2.06

Source: RHB, Bloomberg

ESG Rating History



Source: RHB

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