

19 November 2024

Industrials | Aerospace & Defence

## ST Engineering (STE SP)

**Buy** (Maintained)

### In-Line 9M24, Maintain Growth Expectations; Still BUY

Target Price (Return): SGD5.32 (+19%)  
 Price (Market Cap): SGD4.45 (USD10,340m)  
 ESG score: 3.3 (out of 4)  
 Avg Daily Turnover (SGD/USD) 20.9m/15.5m

- **Reiterate BUY and 5.32 TP, 19% upside and c.4% yield.** 3Q24 revenue of SGD2.8bn (+14% YoY) accounted for 52% of our 2H24F. While the other segments reported YoY revenue growth, urban solutions & satcom (USS) revenue declined 5% amidst the weak satcom business. In line with our expectation, the 3Q24 contract wins momentum has softened with SGD2.2bn (-2% YoY, -29% QoQ) in order wins. We remain upbeat on ST Engineering's revenue and profit momentum and expect it to deliver a 15% profit CAGR and steady dividends in 2023-2026.
- **3Q24: excluding USS, all businesses reported revenue growth.** On a YoY basis, commercial aerospace (CA) and defence & public security (DPS) reported 7% and 31% revenue growth. DPS growth was aided by strong order deliveries for across key sub-segments. CA saw strong growth in the engine MRO business as delay in deliveries of new aircraft has led to airlines using older aircraft for longer. This has in turn led to lower availability of feedstock for passenger-to-freighter (PTF) business. Despite the likelihood of reduced PTF volume in the near term, STE reiterated its mid-single-digit EBIT margin by end 2024 and SGD700m revenue guidance by 2026 for the PTF business. STE's hangars are operating at 90% utilisation levels, and it is repurposing some of its PTF capacity to meet increased MRO demands. STE's hangar capacity will be 20% higher by 2024 and 30% higher by 2026 as compared to pre-COVID-19 levels. For USS, although revenue was down YoY, STE reiterated that the business segment's 2H24 revenue will be higher as compared to the same period last year. CA, DPS, and USS 3Q24 revenue accounted for 55%, 59%, and 42% of our 2H24F.
- **Decent order wins.** STE reported SGD2.2bn of order wins in 3Q24. Only USS registered YoY and QoQ growth in order wins. The company's outstanding orderbook stood at a record high of SGD26.9bn, providing close to 2.5 years of revenue visibility. In addition to order deliveries, the decline in outstanding orderbook was also due to FX translation, as close to a third of the orders are in USD. SGD2.6bn worth of orders are expected to be delivered in 4Q24. This compares with our revenue estimate of SGD2.6bn for the same period.
- **Interim dividend declared; upside from lower interest rates.** STE declared an interim dividend of 4 SG cents. It has an outstanding debt of SGD6bn, of which 63% is at a fixed interest rate. With expectations of lower interest rates in 2025, we estimate that a 100bps reduction in interest costs will boost profit by 2%. We continue to derive our TP using an average of P/E, P/BV, EV/EBITDA, and DCF. It also includes a 4% ESG premium given STE's 3.3 ESG score vs the 3.1 country median.

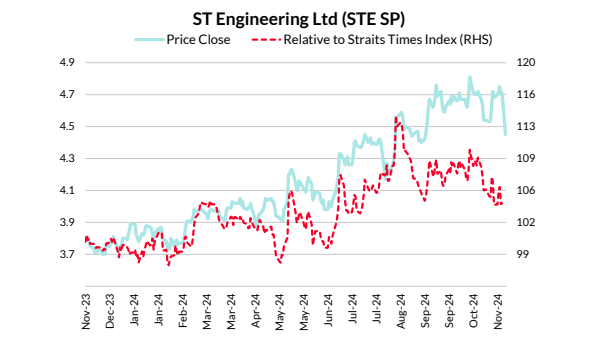
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#### Share Performance (%)

	YTD	1m	3m	6m	12m
Absolute	14.4	(7.5)	(2.4)	5.2	15.0
Relative	(1.2)	(10.4)	(14.1)	(7.8)	(4.8)
52-wk Price low/high (SGD)	3.70 - 4.81				



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 seven are independent (54%), and three 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)	28.74	22.65	19.43	16.50	14.96
P/B (x)	5.8	5.6	5.2	4.6	4.1
P/CF (x)	20.58	11.76	10.63	9.38	9.59
Dividend Yield (%)	4.9	3.6	3.6	3.6	3.6
EV/EBITDA (x)	16.96	14.41	12.98	11.43	10.52
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)	28.74	22.65	19.43	16.50	14.96
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)	5.8	5.6	5.2	4.6	4.1
	FCF Yield (%)	(0.5)	6.5	4.7	7.4	7.7
	Dividend Yield (%)	4.9	3.6	3.6	3.6	3.6
<b>Key drivers</b>	EV/EBITDA (x)	16.96	14.41	12.98	11.43	10.52
i. New order wins and continuing delivery of order book;	EV/EBIT (x)	30.16	23.69	20.49	17.64	16.12
ii. Sustained improvement in global aviation market;						
iii. Contributions from acquisitions.						
	<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>
<b>Key risks</b>	Total turnover	9,035	10,101	10,876	11,715	12,644
i. Slower revival in commercial aerospace sector;	Gross profit	1,699	1,973	2,215	2,446	2,630
ii. Lower margin from higher costs caused by supply chain issues;	EBITDA	1,181	1,382	1,531	1,705	1,812
iii. Delays in the delivery of order book;	Depreciation and amortisation	(517)	(541)	(562)	(600)	(629)
iv. Lower-than-expected contribution from acquisitions	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>Company Profile</b>						
ST Engineering is an integrated engineering group in the commercial aerospace (CA), urban solutions & satcom (USS), and defence & public security (DPS) sectors. The company has over the years, diversified its businesses and geographical coverage.	<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>
	Change in working capital	(442)	(101)	(205)	(192)	(332)
	Cash flow from operations	673	1,179	1,304	1,478	1,445
	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>Balance sheet (SGDm)</b>	<b>Dec-22</b>	<b>Dec-23</b>	<b>Dec-24F</b>	<b>Dec-25F</b>	<b>Dec-26F</b>
	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.

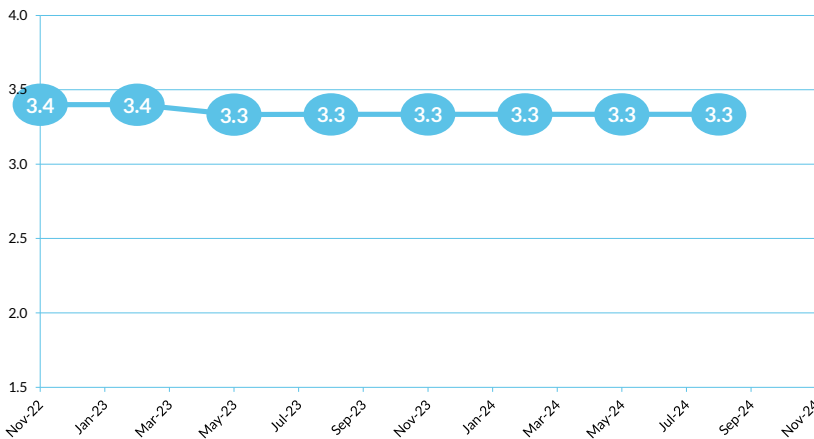
Emissions (tCO <sub>2</sub> e)	Dec-21	Dec-22	Dec-23
Scope 1	36,000	39,000	37,000
Scope 2	78,000	71,000	74,000
Scope 3	1,900	33,000	39,000
Total emissions	115,900	143,000	150,000

Source: Company data, RHB

## Latest ESG-Related Developments

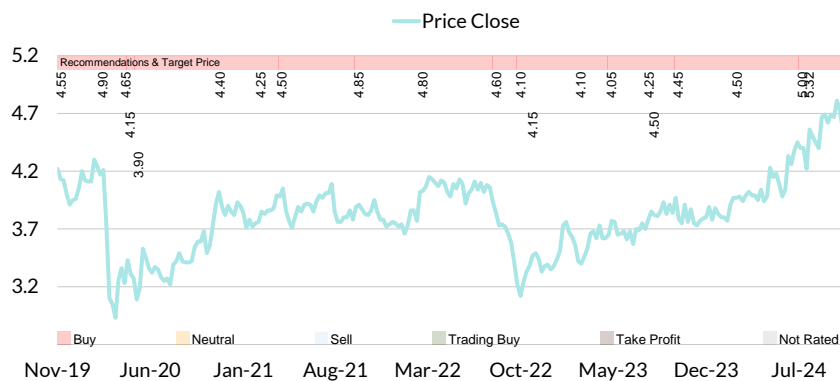
- In 2021, STE set a target to halve its absolute Scope 1 and Scope 2 GHG emissions by 2030 compared to a 2010 base year. In the same year, it also set a target to increase its sustainability linked revenue to more than SGD3bn by 2026.
- In 2022, STE was included in the Dow Jones Sustainability Asia 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
2024-09-18	Buy	5.32	4.69
2024-07-21	Buy	5.00	4.45
2024-04-08	Buy	4.50	3.98
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

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>Take Profit:</b>	Target price has been attained. Look to accumulate at lower levels
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<b>Not Rated:</b>	Stock is not within regular research coverage

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