

1 March 2023

Industrials | Engineering & Construction

UEM Edgenta (UEME MK)

Buy (Maintained)

Margin Dragged by Higher Cost; Keep BUY

- **Maintain Buy, with a lower DCF-derived TP of MYR1.20 from MYR1.37, c.7% yield.** UEM Edgenta's 2022 core earnings was below our and Street's expectations due to higher operating costs, despite a robust pick-up in the infrastructure solutions division. Management remains cautiously optimistic on 2023 amid cost-inflation pressure. UEME is steadfast in adopting cost-optimisation measures and deploying tech-enabled solutions to navigate through the headwinds. Our TP incorporates 4% ESG premium as the company's ESG score is above the country median.
- **Results overview.** 4Q22 core earnings came in at MYR11m (-36.5% QoQ, -57.7% YoY), bringing the full-year 2022 total to MYR54.4m, -9.1% YoY. This accounted for 83% and 89% of our and consensus' full-year estimates. The weaker-than-expected result was mainly dragged by mounting cost pressure. A stronger fourth quarter led its full-year topline to exceed both our and consensus estimates by 5% and 8%. The infrastructure services revenue grew 15% YoY, due to a higher work order, and billable works for the maintenance of major expressways being recognised. Healthcare support, which accounted for 57% of 2022's total revenue, declined 5% YoY – likely because of the absence of COVID-19-related revenues. Last year, UEME secured MYR1.36bn of new contracts (of which 60% were healthcare-related), representing 30% YoY increase from 2021 and slightly above the management's MYR1.2-1.3bn target.
- **Margin and outlook.** The group's core margin eased 2.2ppt YoY to 5.8% in 4Q22. This is attributed to the higher staff cost (ie implementation of minimum wages), as well as a spike in raw material prices – including bitumen, used for road maintenance and chemical products for cleaning. UEME expects to offset the negative deviation by adopting a greater degree of automation, growing its value-added services, and establishing hard-service offerings in its international markets like Singapore and Taiwan. While we are optimistic for the recovery of most pandemic-affected operations, we are similarly cognizant of the heightened operating costs.
- **We cut FY23F-24F earnings by 6-4% to account for the rising cost environment for the group's healthcare and infrastructure segments.**
- **Valuation.** We maintain our BUY rating for UEME with a lower DCF-derived TP of MYR1.20 after our earnings adjustment. Apart from being a key proxy to the reopening of borders, we also like the company for its commitment to a 50-80% dividend payout, as well as its current bargain valuation. UEME is currently trading at 9x 12-months forward P/E, below its 5-year mean 22x. Our TP incorporates 4% ESG premium as UEME's ESG score stood in line with the country median.

Forecasts and Valuation	Dec-21	Dec-22	Dec-23F	Dec-24F	Dec-25F
Total turnover (MYRm)	2,292	2,524	2,639	2,803	2,966
Recurring net profit (MYRm)	60	54	83	92	102
Recurring net profit growth (%)	33.7	(9.0)	51.8	11.1	11.3
Recurring EPS (MYR)	0.07	0.07	0.10	0.11	0.12
DPS (MYR)	0.04	0.05	0.06	0.08	0.09
Recurring P/E (x)	13.07	14.37	9.46	8.52	7.65
P/B (x)	0.51	0.49	0.49	0.48	0.47
Dividend Yield (%)	4.5	5.0	6.9	8.2	9.1
Return on average equity (%)	1.6	2.9	5.2	5.7	6.2
Net debt to equity (%)	net cash	net cash	net cash	net cash	net cash

Source: Company data, RHB

Target Price (Return):	MYR1.20 (27.2%)
Price (Market Cap):	MYR0.94 (USD174m)
ESG score:	3.22 (out of 4)
Avg Daily Turnover (MYR/USD)	0.32m/0.07m

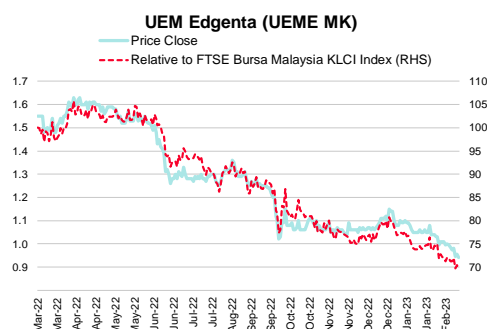
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Share Performance (%)

	YTD	1m	3m	6m	12m
Absolute	(17.6)	(10.5)	(11.3)	(28.3)	(39.8)
Relative	(14.8)	(7.6)	(9.1)	(25.2)	(30.2)
52-wk Price low/high (MYR)	0.94 – 1.63				



Source: Bloomberg

Overall ESG Score: 3.22 (out of 4)

E: EXCELLENT

UEME's facilities management solutions undertakes green building initiatives for its portfolio projects, resulting in energy savings of 20-30% on average and reduced carbon emissions. The group has 10 GBI-certified buildings under its management.

S: GOOD

Offers comprehensive training programmes for every employee and contractor from the various business divisions. Emphasis is placed on the Edgenta Stars Engagement programme by facilitating engagement between divisional leaders and staff at all levels.

G: EXCELLENT

Balanced board composition of 60:40 independent / non-independent directors. The male to female ratio is in line with the Malaysian Code on Corporate Governance requirement of 30%. UEME has active engagements with the media and investors' communities.

Note:

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

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Financial Exhibits

Asia	Financial summary (MYR)	Dec-21	Dec-22	Dec-23F	Dec-24F	Dec-25F
Malaysia	Recurring EPS	0.07	0.07	0.10	0.11	0.12
Industrials	EPS	0.03	0.06	0.10	0.11	0.12
UEM Edgenta	DPS	0.04	0.05	0.06	0.08	0.09
UEME MK	BVPS	1.85	1.90	1.93	1.97	2.00
Buy	Return on average equity (%)	1.6	2.9	5.2	5.7	6.2
	Return on average assets (%)	0.9	1.6	2.8	3.1	3.4
Valuation basis	Valuation metrics	Dec-21	Dec-22	Dec-23F	Dec-24F	Dec-25F
DCF FCFF	Recurring P/E (x)	13.07	14.37	9.46	8.52	7.65
	P/B (x)	0.5	0.5	0.5	0.5	0.5
Key drivers	Dividend Yield (%)	4.5	5.0	6.9	8.2	9.1
i. Benefiting from regional growth in integrated facilities management market;	EV/EBITDA (x)	3.06	2.42	2.34	2.02	1.74
ii. Increase in Government's budget allocations for healthcare services.						
Key risks	Income statement (MYRm)	Dec-21	Dec-22	Dec-23F	Dec-24F	Dec-25F
i. Cutbacks in infrastructure activities;	Total turnover	2,292	2,524	2,639	2,803	2,966
ii. Margin compression;	Gross profit	310	340	351	375	393
iii. Loss of recurring income from non-awarding / non-renewal of facilities' management contracts.	EBITDA	163	192	182	193	205
	Depreciation and amortisation	(87)	(82)	(80)	(81)	(81)
	Operating profit	75	110	102	112	124
	Net interest	(21)	(21)	(21)	(20)	(20)
	Pre-tax profit	61	94	105	116	129
	Taxation	(35)	(48)	(23)	(25)	(27)
	Reported net profit	24	46	83	92	102
	Recurring net profit	60	54	83	92	102
Company Profile	Cash flow (MYRm)	Dec-21	Dec-22	Dec-23F	Dec-24F	Dec-25F
UEM Edgenta is the leading asset management and infrastructure solutions company in Malaysia. Its expertise in these fields covers consultancy services and solutions across healthcare, infrastructure, and property & facility.	Change in working capital	(57)	88	(4)	(4)	(4)
	Cash flow from operations	45	104	180	189	199
	Capex	(43)	(43)	(66)	(70)	(74)
	Cash flow from investing activities	(78)	(45)	(66)	(70)	(74)
	Dividends paid	(36)	(39)	(54)	(64)	(71)
	Cash flow from financing activities	(58)	(20)	(114)	(94)	(101)
	Cash at beginning of period	678	600	609	639	663
	Net change in cash	(91)	39	(0)	25	23
	Ending balance cash	587	639	609	663	687
	Balance sheet (MYRm)	Dec-21	Dec-22	Dec-23F	Dec-24F	Dec-25F
	Total cash and equivalents	629	707	736	761	784
	Tangible fixed assets	167	146	132	121	114
	Intangible assets	699	701	701	701	701
	Total investments	103	73	73	73	73
	Total other assets	237	248	248	248	248
	Total assets	2,855	2,907	2,932	2,957	2,984
	Short-term debt	385	131	131	131	131
	Total long-term debt	58	328	318	308	298
	Total liabilities	1,316	1,323	1,320	1,317	1,314
	Shareholders' equity	1,536	1,580	1,609	1,636	1,667
	Minority interests	4	4	3	3	3
	Total equity	1,539	1,584	1,612	1,640	1,670
	Total liabilities & equity	2,855	2,907	2,932	2,957	2,984
	Key metrics	Dec-21	Dec-22	Dec-23F	Dec-24F	Dec-25F
	Revenue growth (%)	13.0	10.1	4.6	6.2	5.8
	Recurring net profit growth (%)	33.7	(9.0)	51.8	11.1	11.3
	Recurrent EPS growth (%)	33.7	(9.0)	51.8	11.1	11.3
	Gross margin (%)	13.5	13.5	13.3	13.4	13.3
	Recurring net profit margin (%)	2.6	2.2	3.1	3.3	3.4
	Dividend payout ratio (%)	146.7	86.0	65.0	70.0	70.0

Source: Company data, RHB

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Figure 1: Results snapshot

FYE Dec (MYRm)	4Q21	2Q22	4Q22	QoQ (%)	YoY (%)	FY21	FY22	YoY (%)	Comments
Revenue	698.4	627.7	710.5	13.2	1.7	2,292.4	2,523.6	10.1	Increase YoY due to healthcare support and infrastructure services divisions
Gross profit	84.7	86.0	95.1	10.5	12.2	310.3	331.5	6.8	
<i>Gross margin</i>	<i>12.1%</i>	<i>13.7%</i>	<i>13.4%</i>			<i>13.5%</i>	<i>13.1%</i>		
Other income	12.8	7.1	27.2	284.6	111.3	36.0	50.0	38.7	
Other expenses	(69.9)	(69.5)	(80.0)	15.0	14.4	(271.0)	(280.4)	3.5	
Finance costs	(4.9)	(4.9)	(6.2)	25.7	25.9	(20.9)	(20.8)	(0.6)	
Share of results of associates	10.5	4.4	2.5	(44.0)	(76.7)	24.2	13.5	(44.0)	
El/Others	(5.8)	(6.4)	10.0	nm	nm	(17.8)	(8.5)	nm	
Pretax profit	33.3	23.0	38.5	67.5	15.6	78.6	93.8	19.4	
<i>Pretax margin (%)</i>	<i>4.8%</i>	<i>3.7%</i>	<i>5.4%</i>			<i>3.4%</i>	<i>3.7%</i>		Lower margin because of escalated operating costs
Tax	(13.0)	(12.1)	(17.4)	43.9	33.7	(35.2)	(48.1)	36.7	
Effective tax rate (%)	39.1%	52.8%	45.3%			44.8%	51.3%		
Minority interest	(0.2)	0.0	(0.1)	(400.0)	(72.1)	(1.4)	0.2	(116.8)	
Net profit	20.0	10.9	21.0	93.1	4.7	42.0	45.9	9.2	
Core profit	25.9	17.2	11.0	(36.5)	(57.7)	59.8	54.4	(9.1)	Below expectation. Accounted for 83% and 89% of our and Street estimates.
<i>Core net margin (%)</i>	<i>3.7%</i>	<i>2.7%</i>	<i>1.5%</i>			<i>2.6%</i>	<i>2.2%</i>		

Source: Company data, RHB

Figure 2: DCF valuation

	FY23F	FY24F	FY25F	FY26F	FY27F	FY28F	FY29F	FY30F	FY31F	FY32F	Terminal
NOPAT	73	82	92	100	105	109	114	120	125	129	
+ D&A	80	81	81	81	81	81	80	80	80	80	
- Change in NWC	(4)	(4)	(4)	(4)	(4)	(4)	(5)	(5)	(5)	(5)	
- CAPEX	(66)	(70)	(74)	(77)	(79)	(82)	(85)	(88)	(91)	(94)	
Free cash flow to firm (FCFF)	84	89	95	101	102	104	105	107	110	110	1,215
Discount factor	0.92	0.83	0.75	0.68	0.61	0.55	0.50	0.45	0.41	0.37	0
PV of FCFF	77	74	71	68	62	57	53	48	45	41	447
Risk-free	4.0%										
WACC	11%										
Terminal growth	2%										
Enterprise value (MYR m)	1,043										
- Minority	4										
- Debt	-449										
Cash	707										
Add: Associates											
Healthcare support (8x FY23 P/E)	120										
PFS & Asset consultancy (5x FY23 P/E)	40										
Equity value (MYR m)	1,464										
Holding company discount	35%										
No of shares (m)	832										
Intrinsic value (MYR)	1.14										
ESG discount/premium	0.05										
Target price (MYR)	1.20										

Source: RHB

Recommendation Chart

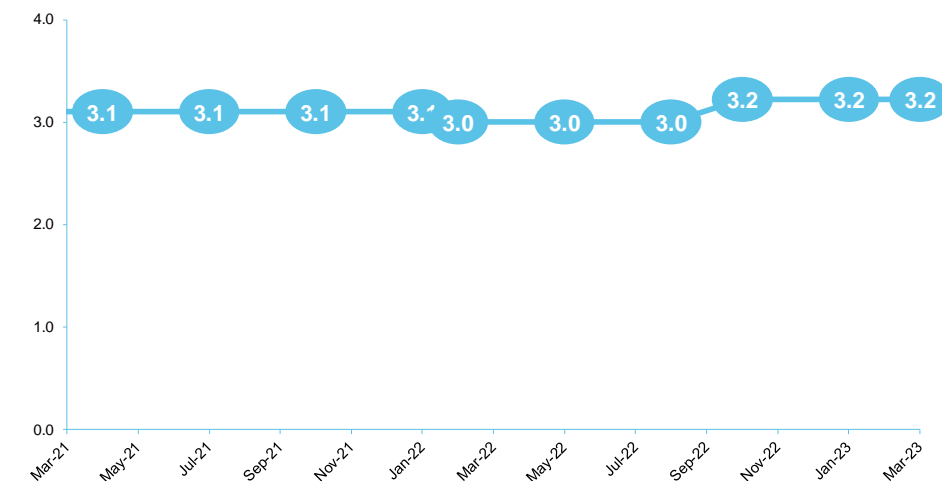


Source: RHB, Bloomberg

Date	Recommendation	Target Price	Price
2022-11-30	Buy	1.37	1.06
2022-10-31	Buy	1.46	1.08
2022-02-28	Neutral	1.70	1.56
2022-02-25	Neutral	1.50	1.57
2021-11-26	Buy	2.96	1.64
2021-08-26	Buy	2.35	1.73
2021-06-03	Buy	2.35	1.71
2021-05-28	Buy	2.35	1.69
2021-03-03	Buy	2.05	1.67
2021-02-26	Neutral	1.85	1.69
2020-11-26	Neutral	1.85	1.90
2020-08-27	Buy	2.75	2.14
2020-07-10	Buy	2.75	2.04
2020-05-22	Neutral	2.70	2.20
2020-02-27	Buy	3.60	2.55

Source: RHB, Bloomberg

ESG Rating History



Source: RHB

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