Small Cap Asean Research

Malaysia Results Review

24 November 2022

Consumer Cyclical | Gaming

Sports Toto (SPTOTO MK)

Buy (Maintained)

A Gamble For Now; Still a BUY At This Juncture

Target Price (Return):	MYR2.10 (30.6%)
Price (Market Cap):	MYR1.61 (USD475m)
ESG score:	3.00 (out of 4)
Avg Daily Turnover (MYR/USD)	1.68m/0.37m

- **Keep BUY and MYR2.10 TP, 31% upside, with 7% yield.** 1QFY23 (Jun)'s results were in line, but DPS disappointed. We maintain our recommendation and TP, but highlight the significant downside risks if the political environment results in a spike in regulatory risks to the number forecast operators (NFOs). In such scenario, a higher risk premium is warranted to reflect Sports Toto's heightened regulatory risks and uncertainties.
- **Within expectations.** SPTOTO enjoyed a favourable luck factor (low prize payout of c.57%) in 1QFY23. Hence, revenue made up 24% of our full-year estimate while the core net profit of MYR68m made up c.30% of our full-year forecast, which we consider to be in line, given that the prize payout may swing from quarter to quarter and the uncertainty in the trajectory of a full recovery in ticket sales. SPTOTO declared an interim DPS of 2 sen, which we deem to be below our full year 12.5 sen estimate, as management looks to preserve cash in light of the ongoing uncertainties. Accordingly, we lower our FY23F DPS to 10.5 sen.
- **Ticket sales are still hovering at c.85% of pre-pandemic levels,** as the illegal NFOs continue to prevent a full recovery. SPTOTO's UK motor vehicle dealer – HR Owen – saw an 11% decline in revenue and 5% drop in EBIT. This was because changing consumer behaviour caused lower spending on used luxury vehicles and supercars, leading to discounts to clear its second-hand inventory. The EBIT margin of c.2% is the normalised level, and should sustain moving forward in our view.
- **Heightened regulatory risks amidst political uncertainty.** At the time of writing, the recently concluded 15th General Election resulted in a hung parliament. Depending on the makeup of the new Government, the shift in the political environment may result in a spike in regulatory risks that could involve additional restrictions on NFOs.
- **Forecasts.** We maintain our earnings estimates as the results were in line. Given that the political landscape remains inconclusive at the moment, we maintain our BUY call and DCF-based MYR2.10 TP – which includes a 0% ESG premium/discount – premised on an attractive FY23F yield of 7%. However, we highlight that if the political outcome turns unfavourable, we may significantly raise SPTOTO's risk premium and WACC, presenting significant downside risks to the stock.
- **Key downside risks** include adverse regulations against the NFOs, the reduction in the number of special draw days, changes in the gaming tax, and the luck factor.

Forecasts and Valuation	Jun-21	Jun-22	Jun-23F	Jun-24F	Jun-25F
Total turnover (MYRm)	4,829	5,233	5,996	6,124	6,252
Recurring net profit (MYRm)	175	162	218	228	238
Recurring net profit growth (%)	37.9	(7.4)	34.8	4.5	4.7
Recurring P/E (x)	12.46	13.46	9.98	9.55	9.12
P/B (x)	2.7	2.4	2.2	2.1	2.1
P/CF (x)	4.34	5.34	11.59	6.39	6.13
Dividend Yield (%)	5.0	5.4	6.5	8.1	9.3
EV/EBITDA (x)	6.76	6.72	5.49	5.28	5.04
Return on average equity (%)	23.4	18.9	23.3	22.8	22.9
Net debt to equity (%)	79.1	70.8	54.9	51.1	47.9

Source: Company data, RHB

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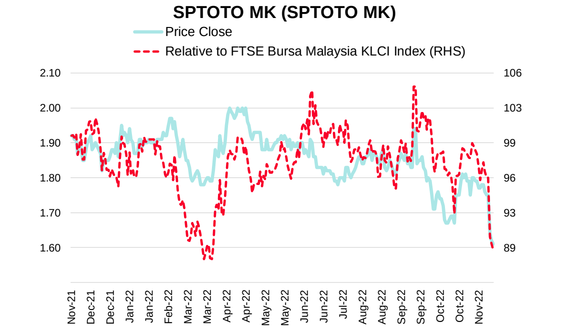
Share Performance (%)

	YTD	1m	3m	6m	12m
Absolute	(15.3)	(8.0)	(11.5)	(15.7)	(16.2)
Relative	(7.4)	(7.8)	(8.9)	(9.3)	(11.0)
52-wk Price low/high (MYR)					1.61 – 2.00



Source: Bloomberg

Overall ESG Score: 3.00 (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

SPTOTO 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
Malaysia
Consumer Cyclical
Sports Toto
SPTOTO MK
Buy

Valuation basis

We use Discounted Cash Flow methodology to derive the target price. Key assumptions are:

i. WACC: 8.8%;
ii. Terminal growth: 0.5%.

Key drivers

i. Ticket sales;
ii. Luck factor.

Key risks

i. Adverse regulations against the NFOs;
ii. Changes in gaming taxes;
iii. Weaker-than-expected overseas contributions;
iv. Reduction in the number of special draw days.

Company Profile

Sports Toto is one of the largest number forecast operators (NFOs) in Malaysia. It also has a presence in the Philippines' gaming market.

Financial summary (MYR)	Jun-21	Jun-22	Jun-23F	Jun-24F	Jun-25F
Recurring EPS	0.13	0.12	0.16	0.17	0.18
DPS	0.08	0.09	0.11	0.13	0.15
BVPS	0.60	0.66	0.72	0.76	0.78
Return on average equity (%)	23.4	18.9	23.3	22.8	22.9

Valuation metrics	Jun-21	Jun-22	Jun-23F	Jun-24F	Jun-25F
Recurring P/E (x)	12.46	13.46	9.98	9.55	9.12
P/B (x)	2.7	2.4	2.2	2.1	2.1
FCF Yield (%)	19.8	12.4	5.4	12.4	13.1
Dividend Yield (%)	5.0	5.4	6.5	8.1	9.3
EV/EBITDA (x)	6.76	6.72	5.49	5.28	5.04
EV/EBIT (x)	8.18	8.36	6.60	6.39	6.19

Income statement (MYRm)	Jun-21	Jun-22	Jun-23F	Jun-24F	Jun-25F
Total turnover	4,829	5,233	5,996	6,124	6,252
Gross profit	823	1,115	1,277	1,304	1,332
EBITDA	386	389	457	473	492
Depreciation and amortisation	(67)	(77)	(77)	(82)	(91)
Operating profit	319	312	380	390	401
Net interest	(44)	(65)	(56)	(51)	(46)
Pre-tax profit	283	272	332	347	363
Taxation	(96)	(101)	(109)	(114)	(120)
Reported net profit	181	161	218	228	238
Recurring net profit	175	162	218	228	238

Cash flow (MYRm)	Jun-21	Jun-22	Jun-23F	Jun-24F	Jun-25F
Change in working capital	81	2	(172)	(30)	(31)
Cash flow from operations	502	407	188	341	355
Capex	(71)	(138)	(70)	(70)	(70)
Cash flow from investing activities	(156)	(113)	(70)	(70)	(70)
Dividends paid	(87)	(47)	(142)	(176)	(203)
Cash flow from financing activities	(393)	29	(306)	(315)	(338)
Cash at beginning of period	308	364	559	567	497
Net change in cash	(47)	323	(188)	(44)	(52)
Ending balance cash	268	675	371	522	445

Balance sheet (MYRm)	Jun-21	Jun-22	Jun-23F	Jun-24F	Jun-25F
Total cash and equivalents	364	559	567	497	433
Tangible fixed assets	629	554	547	535	514
Total investments	324	301	305	309	312
Total assets	2,864	3,112	3,181	3,146	3,108
Short-term debt	551	280	236	206	176
Total long-term debt	505	956	900	850	800
Total liabilities	1,989	2,155	2,144	2,052	1,973
Total equity	875	957	1,038	1,095	1,135
Total liabilities & equity	2,864	3,112	3,181	3,146	3,108

Key metrics	Jun-21	Jun-22	Jun-23F	Jun-24F	Jun-25F
Revenue growth (%)	4.2	8.4	14.6	2.1	2.1
Recurrent EPS growth (%)	37.9	(7.4)	34.8	4.5	4.7
Gross margin (%)	17.0	21.3	21.3	21.3	21.3
Operating EBITDA margin (%)	8.0	7.4	7.6	7.7	7.9
Net profit margin (%)	3.8	3.1	3.6	3.7	3.8
Dividend payout ratio (%)	59.6	72.8	65.1	77.1	85.0
Capex/sales (%)	1.5	2.6	1.2	1.1	1.1
Interest cover (x)	5.25	4.80	5.93	6.60	7.31

Source: Company data, RHB

Figure 1: 1QFY23 results review

FYE Jun (MYRm)	1QFY22	4QFY22	1QFY23	QoQ (%)	YoY (%)	Comments
Revenue	**797.6**	**1,461.1**	**1,419.1**	**(2.9)**	**77.9**	
Gaming	*74.2*	*664.9*	*701.2*	*5.5*	*844.7*	Marginal QoQ improvement in ticket sales, but still largely remain at c.85% of pre-pandemic levels, as illegal NFOs continue to retain their market share. Significant YoY improvement as 1QFY22 saw COVID-19 movement restrictions.
Motor	*707.1*	*774.2*	*692.2*	*(10.6)*	*(2.1)*	Softened QoQ due to lower spending on luxury vehicles and supercars, further worsened by HR Owen's discounts to clear used-car inventory.
Others	*16.3*	*22.0*	*25.7*	*16.7*	*57.7*	
EBITDA	**14.4**	**118.0**	**121.0**	**2.6**	**739.9**	
EBITDA margin (%)	*1.8*	*8.1*	*8.5*			
Depreciation	(16.6)	(23.7)	(14.8)	37.6	10.8	
EBIT	**(2.2)**	**94.3**	**106.2**	**12.7**	**(5,024.2)**	
EBIT margin (%)	*(0.3)*	*6.5*	*7.5*			
Gaming	*(26.6)*	*85.8*	*101.3*	*18.1*	*N/M*	Vis-à-vis gaming revenue, gaming EBIT saw a disproportionately larger QoQ increase due to a better luck factor, with a prize payout of c.57% vs long-term historical average of 60%.
Motor	*27.3*	*15.8*	*15.0*	*(5.3)*	*(45.1)*	QoQ, motor EBIT declined slightly less than motor revenue did due to a 0.2ppt increase in margins.
Others	*0.3*	*(3.0)*	*(3.5)*	*(16.4)*	*1,231.6*	
Unallocated corporate expense	*(3.2)*	*(4.3)*	*(6.5)*	*(1.7)*	*>(100)*	
Interest expense	(15.1)	(18.4)	(16.2)	11.8	(7.2)	
Investment income	4.4	4.6	8.9	92.6	100.2	
Associates	0.5	3.3	4.2	28.1	828.4	
EI/Others	0.0	(1.2)	4.6	489.6	N/A	
Pre-tax profit	**(12.4)**	**82.6**	**107.7**	**30.4**	**(968.1)**	
Pre-tax margin (%)	*(1.6)*	*5.7*	*7.6*			
Tax	(2.5)	(35.0)	(33.2)	5.0	(1,251.9)	
Effective tax rate (%)	*(19.8)*	*42.3*	*30.8*			
Minority interest	(2.8)	(1.2)	(1.5)	(23.3)	47.2	
Net profit	**(17.7)**	**46.4**	**73.0**	**57.2**	**(513.1)**	
Core profit	**(17.7)**	**47.6**	**68.4**	**43.7**	**(487.1)**	Within our expectations, given our expectations for prize payout to revert to the historical mean of 60%.
Net margin (%)	*(2.2)*	*3.3*	*4.8*			

Source: Company data, RHB

Figure 2: DCF valuation

FYE Jun (MYRm)	2023F	2024F	2025F	2026F	2027F	2028F	2029F	2030F	2031F	2032F
EBIT	379.8	390.5	401.1	402.0	402.8	403.7	404.6	405.4	406.3	404.2
EBIT x (1-Tax)	254.5	261.6	268.7	269.3	269.9	270.5	271.1	271.6	272.2	270.8
(+) Depreciation & amortisation	77.0	82.5	91.3	98.8	106.5	114.6	122.8	131.4	140.2	149.3
(-) Capex	(70.0)	(70.0)	(70.0)	(70.0)	(70.0)	(70.0)	(70.0)	(70.0)	(70.0)	(70.0)
(-) Working capital requirements	(172.1)	(29.8)	(30.7)	(25.6)	(26.0)	(26.3)	(26.6)	(27.0)	(27.3)	(27.7)
Free cash flow	89.4	244.3	259.3	272.5	280.5	288.7	297.3	306.1	315.1	322.5
NPV of free cash flow	82.2	206.5	201.5	194.7	184.3	174.5	165.1	156.3	148.0	139.3
Key assumptions										
Terminal growth	0.5%									
Terminal value	1,825.0									
WACC	8.8%									
Beta	0.97									
Expected market return	11.9%									
Risk-free rate	4.0%									
Cost of equity	11.6%									
Equity weighting	59.8%									
Cost of debt	6.5%									
Effective tax rate	30.0%									
Firm value	3,477.4									
(-) net debt	(569.7)									
(-) minority interests	(66.2)									
Equity value	2,841.5									
Fair Value per share (MYR)	**2.10**									
ESG premium/discount	0%									
TP per share (MYR)	**2.10**									

Source: Company data, RHB

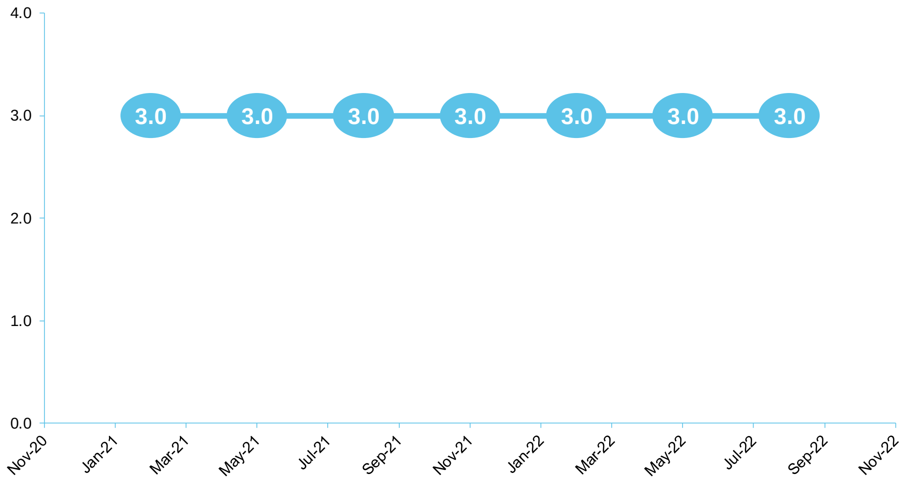
Recommendation Chart

Source: RHB, Bloomberg

Date	Recommendation	Target Price	Price
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
2021-09-14	Buy	2.36	2.03
2021-08-22	Buy	2.36	1.97
2021-08-05	Buy	2.23	1.92
2021-05-21	Buy	2.34	2.00
2021-05-12	Buy	2.34	2.02
2021-02-24	Buy	2.49	2.14

Source: RHB, Bloomberg

ESG Rating History



Source: RHB

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