

## COMPANY UPDATE

**SATS (SATS SP)**

## Key Takeaways From Investor Conference After FY23 Results

At SATS' investor conference after its FY23 full-year results on 31 May 23, investors' questions were mainly centred on its 4QFY23 performance (profit recovery missed our expectations), cost pressure, air cargo outlook and accounting impact of WFS. With a 9.5% share price drop in the past three days, downside risks for SATS are likely priced in. However, we think it may still take another year for investors to see the true earnings potential of SATS with WFS. Maintain BUY and target price of S\$3.02.

## WHAT'S NEW

- FY23 results a slight miss.** SATS released its FY23 full-year results on 29 May 23. Reported net losses of S\$26.5m were a slight miss from our forecasted net losses of S\$20m. On a qoq basis, total revenue rose marginally by 0.5% to S\$478m in 4QFY23. Food solutions and gateway services revenue rose 0.4% and 0.5% qoq to S\$234m and S\$244m, respectively. Excluding government reliefs, operating loss widened qoq to S\$24.3m in 4QFY23 (3QFY23: S\$17.8m) due to higher operating cost qoq against a largely flat revenue qoq. Excluding all non-recurring items such as government reliefs (S\$19.7m), M&A costs (S\$14.7m) related to the Worldwide Flight Services (WFS) acquisition and gains from disposal of PPE (about S\$10m by our estimate), SATS' 4QFY23 core net losses would have been about S\$5m (3QFY23: S\$2m-3m loss).
- SATS investor conference.** We hosted SATS for a virtual investor conference on 31 May 23. A total of 19 institutional investors were present at the meeting. During the conference, the investors' questions were mainly focused on: a) qoq financial performance comparison for food solutions and cargo operations, b) labour ramp-up and potential cost pass-down, c) air cargo outlook, d) the refinancing of WFS' debts, and e) the accounting treatment for the purchase price allocation (PPA) for the WFS acquisition.
- SATS share price down 9.5% in the past three days.** We think the downside risks of SATS are likely priced in.

## STOCK IMPACT

- 4Q food and cargo performance.** For food solutions (revenue up 0.4% qoq), SATS noted that aviation food revenue continued to improve during 4QFY23 as aviation food volume recovered to 74% of pre-pandemic levels by Mar 23 from the average of 65% in 3QFY23. However, the qoq increase in aviation food revenue was largely offset by a decrease in non-aviation food revenue due to a slower food distribution revenue. On a yoy basis, aviation food revenue rose 129% while non-aviation food revenue was down 14.3%. For cargo operations, air cargo volume handled by SATS declined for a third consecutive quarter, down 9.9% in 4QFY23. Seasonality factors aside (3Q, or the Oct-Dec quarter, is a seasonally stronger than 4Q, or the Jan-Mar quarter), 4QFY23 saw the pandemic outbreak in mainland China and slower global trade demand amid a weak global macroeconomy.

## KEY FINANCIALS

Year to 31 Mar (\$m)	2022	2023	2024F	2025F	2026F
Net turnover	1,177	1,758	5,165	5,469	5,664
EBITDA	77	128	828	984	1,016
Operating profit	(43)	(48)	253	404	430
Net profit (rep./act.)	20	(27)	67	252	286
EPS (S\$ cent)	1.7	(2.2)	4.4	16.6	18.8
PE (x)	147.8	n.m.	58.3	15.6	13.7
P/B (x)	1.8	1.6	1.6	1.5	1.4
EV/adjusted EBITDA (x)	60.1	28.7	11.2	8.8	8.4
Dividend yield (%)	0.0	0.0	0.7	2.6	3.0
Net margin (%)	1.7	(1.5)	1.3	4.6	5.0
Net debt/(cash) to equity (%)	(15.0)	(39.8)	86.1	79.0	73.9
ROE (%)	1.3	n.a.	2.8	10.0	10.5
Consensus net profit	-	-	145	256	308
UOBKH/Consensus (x)	-	-	0.46	0.99	0.93

\* Financial projections for 2024-26F have incorporated impacts from the WFS acquisition.

Source: SATS, Bloomberg, UOB Kay Hian

n.m. : not meaningful; negative P/E reflected as "n.m."

## BUY

## (Maintained)

Share Price	S\$2.58
Target Price	S\$3.02
Upside	+17.2%

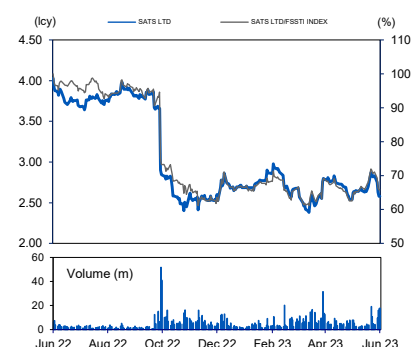
## COMPANY DESCRIPTION

A leading food solutions provider in Asia and a global leader in aviation gateway services.

## STOCK DATA

GICS sector	Industrials			
Bloomberg ticker:	SATS SP			
Shares issued (m):	1,487.3			
Market cap (S\$ m):	3,837.2			
Market cap (US\$m):	2,831.9			
3-mth avg daily t'over (US\$m):	13.3			
<b>Price Performance (%)</b>				
52-week high/low	S\$ 4.03/S\$ 2.38			
<b>1mth</b>	<b>3mth</b>	<b>6mth</b>	<b>1yr</b>	<b>YTD</b>
1.6	(3.6)	2.2	(37.7)	(3.9)
<b>Major Shareholders</b>				
				<b>%</b>
Temasek Hldgs				39.7
-				-
-				-
FY24 NAV/Share (S\$)				1.61
FY24 Net Debt/Share (S\$)				2.44

## PRICE CHART



Source: Bloomberg

## ANALYST(S)

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- Labour cost outlook.** SATS noted that the workforce ramp-up has levelled off with its headcount up only 3.3% qoq in 4QFY23. The current level of headcount should provide sufficient headroom to meet further business volume increase of its existing businesses. Further headcount increase would be mainly for business expansion needs for its new central kitchens in Tianjin, China and Bengaluru, India. When asked about the cost pressure, management shared that the company has been working with its customers and made some progress in passing down some cost pressure. There is still some scope to pass down the cost pressure further especially on the cargo side.
- Cautious about air cargo outlook.** Management noted the softening air cargo outlook in the near term and we note that the tone sounded more cautious than a quarter ago. According to IATA, global air cargo demand is likely to fall 4% yoy in 2023 due to the challenging global macroeconomic environment. To counter the weakness from the external environment, SATS plans to drive productivity through operational excellence and to realise network synergy from the enhanced scale with the WFS integration.
- Benefits from WFS debt refinancing to kick in in FY25.** SATS has more or less completed the refinancing of the debts on WFS' balance sheet. With the lower refinancing interest cost (at about 4.5-5%) than the interest rates of notes previously issued by WFS (ranging from 6.4% to 9.5%), the refinancing would allow SATS to realise over S\$40m interest savings from FY25 onwards (the interest saving for FY24 would be largely negated by an early-redemption cost of about S\$41m by our estimate).
- PPA still under review.** Investors recognised that the PPA related to WFS is a key accounting uncertainty which would affect SATS' reported P/L with the consolidation of WFS (effective from next quarter, ie 1QFY24). We have elaborated the potential impacts of the PPA and other accounting treatments (eg conversion of the WFS accounting to SFRS) in our earlier reports ([13 Mar 23 report](#), [25 Jan 23 report](#)). The CFO shared that the PPA is still under review at the moment and the company will provide more clarity once the review is completed. With the accounting uncertainty in mind, we recommend investors to focus more on SATS' cash P/L performance (which we believe SATS would provide sufficient clarity about) going forward.

#### EARNINGS REVISION/RISK

- We cut our FY24 earnings forecast by 31.6% to S\$67m, but raise our FY25/26 forecasts by 4.2%/2.0% to S\$252m/S\$286m** to reflect the effects of: a) a weaker air cargo demand in the near term, and b) adjusted interest cost saving projection from the WFS debt refinancing (the full redemption came earlier than our previous projections). We note that consensus FY24 forecast is on the high side and is poised for further cuts.
- Key risks include:** a) a prolonged sluggish global trade outlook, b) integration risks between SATS and WFS, and c) possible drags from start-up costs of SATS' new central kitchen investments in the gestation period.

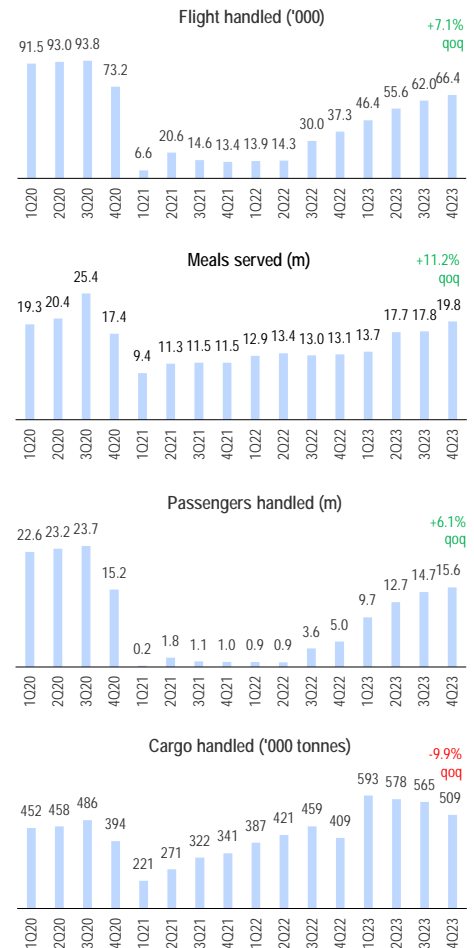
#### VALUATION/RECOMMENDATION

- Maintain BUY with an unchanged target price of S\$3.02.** Our target price is conservatively based on a 9.7x FY25 (normalised year) EV/adjusted EBITDA, pegged SATS' reported acquisition multiple of WFS and equivalent to 1.7SD below SATS' historical mean EV/EBITDA of 12.8x in 2014-19.
- Downside risk likely priced in.** SATS' current price of S\$2.56 implies a FY25 EV/ adj. EBITDA of 8.8x, 2.2 SD below its historical mean. It also implies a FY25 PE of 15.6x on reported earnings and 13.6x on cash earnings (based on our estimate by incorporating SATS' preliminary guidance on the WFS PPA and SFRS conversion). With the recent share price drop, SATS' valuation is undemanding with downside risks likely priced in.
- Patience needed; FY24 a year of consolidation.** While we expect SATS to see some earnings improvement in FY24, we reckon that its FY24 earnings would be still at a very subdued level vs its long-term earnings potential, due to: a) SATS' passenger-related businesses still on the recovery track in FY24, b) weak cargo outlook for both SATS and WFS, c) benefits of debt refinancing having not kicked in, and d) possibly some unfavourable accounting items from the WFS consolidation. FY25 is likely the year that the market can feel the true earnings potential of SATS with WFS.

#### SHARE PRICE CATALYST

- Successful integration of WFS and delivery of the forecasted synergy (medium term).**

#### QUARTERLY OPERATING STATISTICS OF SATS



Source: SATS

#### EV/EBITDA VALUATION FOR SATS

As of end-FY24	Value (\$m)	Note
Enterprise value	6,905	pegged to 9.7x FY25 adj. EBITDA
less: Net debt	2,225	
less: MI	184	
Total equity fair value	4,496	
Enlarged share base (m)	1,487.3	
Target price	S\$3.02	

Source: UOB Kay Hian,

#### HISTORICAL EV/EBITDA BAND OF SATS



Source: SATS, UOB Kay Hian, Bloomberg

### PROFIT & LOSS

Year to 31 Mar (\$m)	2023	2024F	2025F	2026F
Net turnover	1,758.3	5,165.3	5,468.5	5,663.5
EBITDA	127.8	828.3	984.1	1,016.4
Deprec. & amort.	175.8	575.6	580.4	586.0
EBIT	(48.0)	252.7	403.6	430.5
Total other non-operating income	(32.5)	0.0	0.0	0.0
Associate contributions	45.4	44.1	51.5	53.0
Net interest income/(expense)	(8.7)	(198.3)	(148.5)	(139.3)
<b>Pre-tax profit</b>	<b>(43.8)</b>	<b>98.5</b>	<b>306.6</b>	<b>344.2</b>
Tax	5.2	(28.1)	(46.9)	(48.9)
Minorities	12.1	(3.1)	(7.6)	(9.8)
<b>Net profit</b>	<b>(26.5)</b>	<b>67.2</b>	<b>252.1</b>	<b>285.6</b>

### BALANCE SHEET

Year to 31 Mar (\$m)	2023	2024F	2025F	2026F
Fixed assets	900.2	2,315.1	2,380.1	2,426.9
Other LT assets	1,050.7	3,997.4	3,962.2	3,927.6
Cash/ST investment	2,148.4	383.6	375.1	345.6
Other current assets	574.4	1,140.5	1,162.8	1,185.6
<b>Total assets</b>	<b>4,673.7</b>	<b>7,836.6</b>	<b>7,880.2</b>	<b>7,885.6</b>
ST debt	54.1	101.1	101.1	101.1
Other current liabilities	552.3	1,109.9	1,120.7	1,131.6
LT debt	1,424.3	3,912.2	3,712.2	3,512.2
Other LT liabilities	128.2	128.2	128.2	128.2
Shareholders' equity	2,333.6	2,400.8	2,626.1	2,810.8
Minority interest	181.2	184.3	191.9	201.7
<b>Total liabilities &amp; equity</b>	<b>4,673.7</b>	<b>7,836.6</b>	<b>7,880.2</b>	<b>7,885.6</b>

### CASH FLOW

Year to 31 Mar (\$m)	2023	2024F	2025F	2026F
<b>Operating</b>	<b>79.6</b>	<b>594.5</b>	<b>771.2</b>	<b>810.4</b>
Pre-tax profit	(43.8)	98.5	306.6	344.2
Tax	(2.7)	(28.1)	(46.9)	(48.9)
Deprec. & amort.	175.8	575.6	580.4	586.0
Associates	(45.4)	(44.1)	(51.5)	(53.0)
Working capital changes	8.0	(1.4)	(11.5)	(11.9)
Non-cash items	(33.9)	0.0	0.0	0.0
Other operating cashflows	21.6	(6.0)	(6.0)	(6.0)
<b>Investing</b>	<b>(57.9)</b>	<b>(2,153.8)</b>	<b>(258.1)</b>	<b>(239.6)</b>
Capex (maintenance)	(119.4)	(298.6)	(298.6)	(281.1)
Investments	(0.1)	(1,890.7)	0.0	0.0
Proceeds from sale of assets	28.6	0.0	0.0	0.0
Others	33.0	35.5	40.5	41.5
<b>Financing</b>	<b>1,340.0</b>	<b>(205.6)</b>	<b>(521.5)</b>	<b>(600.4)</b>
Dividend payments	0.0	0.0	(26.9)	(100.8)
Issue of shares	0.0	0.0	0.0	0.0
Proceeds from borrowings	752.9	720.0	0.0	0.0
Loan repayment	(106.4)	(635.7)	(200.0)	(200.0)
Others/interest paid	693.5	(289.9)	(294.6)	(299.5)
<b>Net cash inflow (outflow)</b>	<b>1,361.7</b>	<b>(1,764.8)</b>	<b>(8.5)</b>	<b>(29.5)</b>
<b>Beginning cash &amp; cash equivalent</b>	<b>786.0</b>	<b>2,148.4</b>	<b>383.6</b>	<b>375.1</b>
Changes due to forex impact	0.7	0.0	0.0	0.0
<b>Ending cash &amp; cash equivalent</b>	<b>2,148.4</b>	<b>383.6</b>	<b>375.1</b>	<b>345.6</b>

### KEY METRICS

Year to 31 Mar (%)	2023	2024F	2025F	2026F
<b>Profitability</b>				
EBITDA margin	7.3	16.0	18.0	17.9
Pre-tax margin	(2.5)	1.9	5.6	6.1
Net margin	(1.5)	1.3	4.6	5.0
ROA	n.a.	1.1	3.2	3.6
ROE	n.a.	2.8	10.0	10.5
<b>Growth</b>				
Turnover	49.4	193.8	5.9	3.6
EBITDA	65.8	548.1	18.8	3.3
Pre-tax profit	n.a.	n.a.	211.3	12.3
Net profit	(229.9)	n.a.	275.0	13.3
EPS	(226.8)	n.a.	275.0	13.3
<b>Leverage</b>				
Debt to total capital	37.0	60.8	57.5	54.5
Debt to equity	45.6	100.9	85.5	73.3
Net debt/(cash) to equity	(39.8)	86.1	79.0	73.9

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