

ASIAN GEMS CORPORATE HIGHLIGHTS

SATS (SATS SP)

More Palatable Risk-reward Profile After Share Price Decline

In the investor meeting during UOB Kay Hian's Asian Gem Conference, management shared insights and clarified investors' queries about the WFS deal. Following the sharp share price drop after the acquisition announcement, SATS' risk-reward profile is more attractive in our view and suits investors with a longer-term horizon. We upgrade SATS to BUY, with a lower target price of S\$3.08 based on an SOTP valuation, factoring in very conservative valuation metrics for WFS.

WHAT'S NEW

- Management clarifying on the WFS deal.** We attended an investor meeting with SATS Ltd (SATS) during our Asian Gem Conference on 18 Oct 22. 19 institutional investors attended the meeting. During the meeting, management shared more insights about the Worldwide Flight Services (WFS) deal and clarified investors' questions which were focused on the deal background, the due diligence process, potential synergy realisation and the updated financing plan.
- Through private negotiation, not public tendering.** Management shared that, before formally approaching WFS in Nov 21, SATS has been tracking WFS for three years as a potential target. We are glad to know that this WFS acquisition was not through some competitive public tendering process but it was SATS who voluntarily engaged WFS to solicit for a deal. This is important as in a public tendering, bidders face more competitive pressure and have to comply with strict deal timeline; as such there is a higher chance that the winner may end up with an unfavourable valuation or insufficient due diligence.
- Rigorous due diligence.** Management noted that SATS has run a rigorous due diligence process covering the commercial, financial, tax, HR and operation aspects of WFS, involving both internal teams and external consultants and industry experts. The whole process took about five months, which is longer than a typical M&A due diligence duration (usually 2-3 months). The project team has also carefully studied WFS' synergy potential with SATS' existing businesses and concluded that there is scope for SATS, as an industry player, to create and to realise synergistic value from this deal, while noting that WFS has changed hands three times (owned by three private equity firms) since 2006. According to management, up to 40% of estimated S\$100m p.a. (EBITDA level) synergy can be realised in the near term (two years horizon).
- Financing plan.** Recognising the unfavourable market sentiment towards equity raising, management sounds more firm that SATS is inclined to reduce the portion of straight equity financing to below 50% and to make up the rest with hybrid instruments such as (convertible) perpetual securities. This makes sense as these hybrid instruments are treated as equity by financial institutions (lenders) and hence would not weaken SATS' credit profile (which may lead to higher cost of debt). Management also confirmed that any equity offering would be limited to existing shareholders, so as not to dilute the value of existing shareholders after the major share price decline.

KEY FINANCIALS

Year to 31 Mar (S\$m)	2021	2022	2023F	2024F	2025F
Net turnover	970	1,177	1,812	2,163	2,453
EBITDA	120	77	190	325	465
Operating profit	(10)	(43)	25	160	298
Net profit	(79)	20	64	154	266
EPS (S\$ cent)	(7.0)	1.8	5.7	13.7	23.6
PE (x)	n.m.	150.1	47.5	19.9	11.5
P/B (x)	2.0	1.9	1.8	1.7	1.6
EV/EBITDA (x)	21.7	37.2	15.5	9.3	6.6
Dividend yield (%)	0.0	0.0	1.1	3.7	7.0
Net margin (%)	(8.1)	1.7	3.6	7.1	10.8
Net debt/(cash) to equity (%)	(11.9)	(15.0)	(9.4)	(4.7)	(2.9)
ROE (%)	n.a.	1.3	3.9	9.0	14.6

* We have yet to incorporate potential financial impacts from the acquisition of WFS.
Source: SATS, Bloomberg, UOB Kay Hian

BUY

(Upgraded)

Share Price	S\$2.72
Target Price	S\$3.08
Upside	+13.1%
(Previous TP)	S\$ 3.82)

COMPANY DESCRIPTION

Asia's leading provider of food solutions and gateway services with a presence in over 55 locations across 14 countries.

STOCK DATA

GICS sector	Industrials
Bloomberg ticker:	SATS SP
Shares issued (m):	1,124.2
Market cap (S\$ m):	3,057.8
Market cap (US\$m):	2,151.7
3-mth avg daily t'over (US\$m):	10.8
Price Performance (%)	

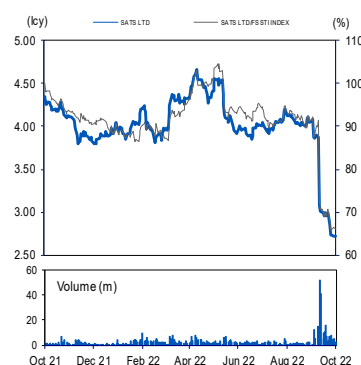
52-week high/low S\$ 4.67/S\$ 2.72

1mth	3mth	6mth	1yr	YTD
(32.8)	(32.0)	(37.2)	(37.5)	(30.1)

Major Shareholders

	%
Temasek Hldgs	40.0
-	-
-	-
FY23 NAV/Share (S\$)	1.49
FY23 Net Debt/Share (S\$)	0.13

PRICE CHART



Source: Bloomberg

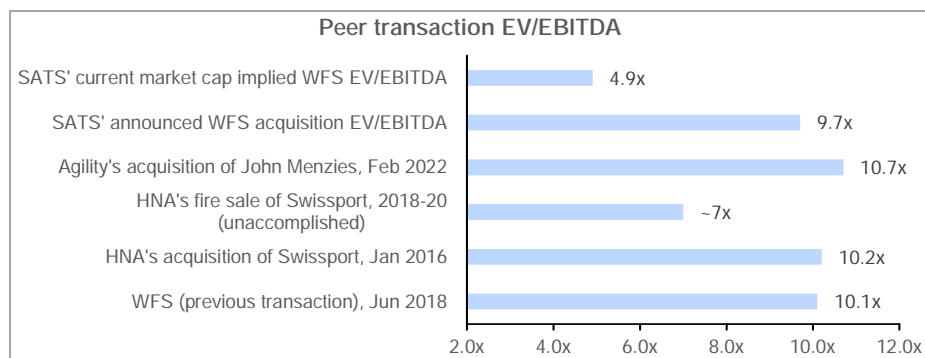
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STOCK IMPACT

- **After the sharp share price decline, ...** Since SATS' first trading halt (on 21 September) related to the WFS deal, SATS' share price has declined 33% from S\$4.06 before the trading halt to S\$2.72 (the closing price on 18 October); this is likely due to the market's unfavourable view towards the deal and the weak sentiment towards the equity raising plan. During this period, S\$1.5b worth of SATS' market cap has been evaporated; this is equivalent to about 45% of WFS' acquisition enterprise value of S\$3.1b.
- **...risk-reward profile of SATS is more attractive.** Assuming SATS' existing business is still worth the value as it was and attributing all market cap drop to the deal of WFS, the market is now effectively valuing WFS at an enterprise value of S\$1.6b (being transaction enterprise value of S\$3.1b less SATS' market cap drop of S\$1.5b). This means, if one buys SATS at the current price, he is effectively paying only 4.9x EBITDA (based on WFS' 12-month EBITDA ended Mar 22) for the WFS deal, instead of the original transaction EV/EBITDA multiple of 9.7x. The effective 4.9x EV/EBITDA looks attractive, considering that: a) this is pre synergy, and b) WFS is the top global air cargo handler.
- **In the context of past peer transactions, the implied 4.9x EV/EBITDA valuation is also very cheap.** While SATS' original acquisition EV/EBITDA of 9.7x for WFS was already not excessive against past peer transactions, the effective 4.9x EV/EBITDA for WFS implied by SATS' current share price is much lower than the historical peer transaction range, usually between 10.1x-10.7x. One special case to note is HNA Group's previous transaction of Swissport, a Swiss aviation service company of similar size to WFS but focuses more on the ground handling services (which SATS does not want to acquire; instead SATS likes the more scalable cargo handling businesses which forms 80% of WFS' revenue). HNA Group acquired Swissport back at 2016 at 10.2x EBITDA but sought for a fire sale a few years later (but failed) after HNA ran into financial distress. HNA's fire sale valuation for Swissport was at about 7x EBITDA by our estimate.

PAST PEER TRANSACTION EV/EBITDA



Source: SATS, UOB Kay Hian

EARNINGS REVISION/RISK

- **No change.** We have yet to incorporate WFS into our financial projection for SATS.

VALUATION/RECOMMENDATION

- **Upgrade SATS to BUY with an SOTP valuation of S\$3.08.** To derive the fair valuation for SATS, We first get the standalone valuation for SATS' existing businesses by DCF (8.0% WACC) and then add the valuation impact of the WFS deal, which in turn is determined by our conservative valuation for WFS (based on 7x EBITDA, very conservatively pegging to the fire sale valuation multiple of Swissport) less the WFS acquisition cost (based on 9.7x EBITDA). We prefer to be conservative in the valuation of WFS, due to: a) the higher risk-free rates today (compared with when SATS negotiated the deal valuation), b) weakening global air cargo outlook in the near term (as highlighted by a few leading air cargo operators including FedEx and DHL), and c) the lack of financial details of WFS. We will review our valuation for SATS pending more clarity on the WFS deal.

SHARE PRICE CATALYST

- **No strong near-term catalyst.** The uncertainties related to the WFS deal may remain an overhang on share price in the near term. Investors in SATS need to adopt a medium-to-long term view. Medium-term catalysts could include: a) SATS successfully integrating WFS and delivering the forecasted synergies and b) improving global air cargo outlook.

AFTER THE STEEP SHARE PRICE DROP OF SATS, MARKET IS EFFECTIVELY VALUING WFS AT 4.9X EBITDA, VS SATS' VALUATION OF WFS AT 9.7X

Before SATS' first trading halt on 21 Sep 22	
SATS share price, as of 20 Sep 22	S\$4.06
SATS # of shares outstanding (mil)	1,122
SATS market cap, as of 20 Sep 22, (a)	S\$4,555m

Post WFS announcement	
SATS current share price, as of 17 Oct 22	S\$2.72
SATS # of shares outstanding (mil)	1,122
SATS market cap, as of 17 Oct 22, (b)	S\$3,052m

SATS mkt cap drop due to WFS, (c) = (b) - (a)	-S\$1,503m
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SATS' acquisition EV for WFS (d)	S\$3,107m
SATS current price implied WFS EV, (c) + (d)	S\$1,604m

WFS base year EBITDA	€232m
€:S\$	1.4

Announced acquisition EV/EBITDA	9.7x
SATS current price implied WFS EV/EBITDA	4.9x

Source: UOB Kay Hian

SOTP VALUATION FOR SATS (FACTORING IN VERY CONSERVATIVE VALUATION FOR WFS)

DCF-based TP for SATS (standalone basis)	S\$3.82
SATS # of shares (mil)	1,122
DCF value of SATS (standalone), (a)	S\$4,286m

UOB Kay Hian's preferred conservative EV/EBITDA multiple for WFS valuation	7.0x
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WFS base year EBITDA	€232m
€:S\$	1.4

UOB Kay Hian's conservative valuation for WFS EV, (b)	S\$2,274m
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SATS' acquisition EV for WFS, (c)	S\$3,107m
Valuation difference, (d) = (c) - (b)	-S\$833m

SATS with WFS acquisition obligation, (a) + (d)	S\$3,453m
SATS # of shares outstanding (mil)	1,122
SATS target price (pre-rights)	S\$3.08

Current price implied upside	13.1%
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Source: UOB Kay Hian

PROFIT & LOSS

Year to 31 Mar (\$m)	2022	2023F	2024F	2025F
Net turnover	1,176.8	1,812.1	2,163.3	2,453.2
EBITDA	77.1	190.2	325.0	465.2
Deprec. & amort.	119.7	165.0	165.0	166.8
EBIT	(42.6)	25.2	160.0	298.3
Total other non-operating income	12.2	18.4	0.0	0.0
Associate contributions	17.1	23.5	31.5	38.2
Net interest income/(expense)	(13.8)	(10.7)	(7.0)	(6.7)
Pre-tax profit	(27.1)	56.4	184.5	329.9
Tax	31.4	1.1	(30.6)	(58.3)
Minorities	16.1	7.0	0.0	(6.0)
Net profit	20.4	64.5	153.9	265.6

BALANCE SHEET

Year to 31 Mar (\$m)	2022	2023F	2024F	2025F
Fixed assets	902.4	998.9	1,095.5	1,192.4
Other LT assets	1,093.9	1,085.6	1,080.0	1,076.6
Cash/ST investment	786.0	578.1	493.9	460.7
Other current assets	510.0	591.7	682.6	759.6
Total assets	3,292.3	3,254.4	3,351.9	3,489.3
ST debt	143.1	101.4	101.4	101.4
Other current liabilities	487.5	502.9	513.9	525.6
LT debt	694.8	625.7	625.7	625.7
Other LT liabilities	133.2	133.2	133.2	133.2
Shareholders' equity	1,602.6	1,667.1	1,753.6	1,873.3
Minority interest	231.1	224.1	224.1	230.1
Total liabilities & equity	3,292.3	3,254.4	3,351.9	3,489.3

CASH FLOW

Year to 31 Mar (\$m)	2022	2023F	2024F	2025F
Operating	62.3	129.7	204.5	331.5
Pre-tax profit	(27.1)	56.4	184.5	329.9
Tax	(17.0)	1.1	(30.6)	(58.3)
Deprec. & amort.	119.7	165.0	165.0	166.8
Associates	(17.1)	(23.5)	(31.5)	(38.2)
Working capital changes	(0.3)	(66.3)	(79.9)	(65.4)
Non-cash items	19.5	18.4	0.0	0.0
Other operating cashflows	(15.4)	(21.4)	(3.0)	(3.4)
Investing	31.1	(199.5)	(194.1)	(191.5)
Capex (maintenance)	(77.9)	(218.2)	(218.2)	(220.4)
Investments	80.6	0.0	0.0	0.0
Proceeds from sale of assets	0.7	0.0	0.0	0.0
Others	27.7	18.7	24.1	29.0
Financing	(189.3)	(138.1)	(94.6)	(173.2)
Dividend payments	0.0	0.0	(67.3)	(145.9)
Issue of shares	0.0	0.0	0.0	0.0
Proceeds from borrowings	21.1	0.0	0.0	0.0
Loan repayment	(182.0)	(110.8)	0.0	0.0
Others/interest paid	(28.4)	(27.3)	(27.3)	(27.3)
Net cash inflow (outflow)	(95.9)	(207.9)	(84.2)	(33.2)
Beginning cash & cash equivalent	879.8	786.0	578.1	493.9
Changes due to forex impact	2.1	0.0	0.0	0.0
Ending cash & cash equivalent	786.0	578.1	493.9	460.7

KEY METRICS

Year to 31 Mar (%)	2022	2023F	2024F	2025F
Profitability				
EBITDA margin	6.5	10.5	15.0	19.0
Pre-tax margin	(2.3)	3.1	8.5	13.4
Net margin	1.7	3.6	7.1	10.8
ROA	0.6	2.0	4.7	7.8
ROE	1.3	3.9	9.0	14.6
Growth				
Turnover	21.3	54.0	19.4	13.4
EBITDA	(36.0)	146.8	70.9	43.1
Pre-tax profit	n.a.	n.a.	227.2	78.8
Net profit	n.a.	216.1	138.7	72.6
Net profit (adj.)	n.a.	216.1	138.7	72.6
EPS	n.a.	215.8	138.7	72.6
Leverage				
Debt to total capital	31.4	27.8	26.9	25.7
Debt to equity	27.9	21.2	20.2	19.0
Net debt/(cash) to equity	(15.0)	(9.4)	(4.7)	(2.9)

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