

# Singapore Company Guide

## Silverlake Axis

Version 7 | Bloomberg: SILV SP | Reuters: SLVX.SI

Refer to important disclosures at the end of this report

DBS Group Research . Equity

15 May 2020

### BUY

Last Traded Price ( 14 May 2020): S\$0.25 (STI : 2,522.31)  
Price Target 12-mth: S\$0.38 (51% upside) (Prev S\$0.48)

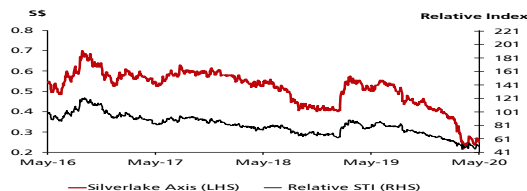
#### Analyst

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### What's New

- 3Q20 net profit below expectations on weaker margins
- No material disruptions from COVID-19; secured RM65m new contracts in 3Q20
- Cut FY20F/21F earnings by 18%/19% on lower gross margin assumptions
- Maintain BUY with lower TP of S\$0.38; current valuations attractive at -1SD level

#### Price Relative



#### Forecasts and Valuation

FY Jun (RMm)	2018A	2019A	2020F	2021F
Revenue	542	681	694	707
EBITDA	167	277	265	274
Pre-tax Profit	147	285	215	244
Net Profit	134	246	153	174
Net Pft (Pre Ex.)	134	190	153	174
Net Pft Gth (Pre-ex) (%)	(84.2)	41.7	(19.7)	13.8
EPS (S cts)	1.63	2.99	1.86	2.11
EPS Pre Ex. (S cts)	1.63	2.31	1.86	2.11
EPS Gth Pre Ex (%)	(84)	42	(20)	14
Diluted EPS (S cts)	1.63	2.99	1.86	2.11
Net DPS (S cts)	2.85	1.77	1.11	1.27
BV Per Share (S cts)	6.36	7.21	7.78	8.67
PE (X)	15.3	8.4	13.5	11.8
PE Pre Ex. (X)	15.3	10.8	13.5	11.8
P/Cash Flow (X)	14.2	6.3	16.8	10.5
EV/EBITDA (X)	9.5	5.4	5.6	5.1
Net Div Yield (%)	11.4	7.1	4.5	5.1
P/Book Value (X)	3.9	3.5	3.2	2.9
Net Debt/Equity (X)	CASH	CASH	CASH	CASH
ROAE (%)	16.0	44.0	24.8	25.7
Earnings Rev (%)			(18)	(19)
Consensus EPS (S cts):			2.43	2.53
Other Broker Recs:		B: 1	S: 0	H: 2

Source of all data on this page: Company, DBS Bank, Bloomberg Finance L.P

### Attractive valuations

**Attractive valuations supported by high recurring revenue.** We cut FY20-21F earnings for Silverlake Axis (Silverlake) by 18-19% on lower gross margin assumptions, as we expect the smaller contract wins to have lower licensing revenue and thereby narrower margins. We continue to like Silverlake for its high recurring revenue proportion that forms at least 60% of total revenue, with attractive yield of about 4-5%, on a 60% payout ratio. At the current level, Silverlake is trading at attractive PE of 13.5x for FY20F and 11.8x for FY21F, near its -1SD level of its average 4-year forward PE.

**Larger projects challenging on economic uncertainties, smaller ones to fill the gap.** There is an increasing trend to spend on incremental enhancements as opposed to the larger one-off projects. Though the deal pipeline is healthy at c. RM1.5bn, the award of larger contracts in excess of RM100m has been slow. To close the gap, the group is targeting smaller contracts of c.RM10m each and these include digital contracts which are generally smaller in size. We expect this trend to continue in 4Q20. With these smaller contracts, orderbook backlog is maintained at close to RM300m.

**Where we differ:** We remain optimistic on Silverlake's business given its market leader position in the core banking solutions, and Insurtech.

**Potential catalyst:** Securing more and bigger-value contracts.

#### Valuation:

**Maintain BUY with lower TP of S\$0.38.** We reduced our FY20F/21F earnings by 18%/19%, mainly on lower gross margin assumptions. As such, our TP is reduced to S\$0.38 (vs S\$0.48 previously), pegged to its 4-year average PE level of 20x.

#### Key Risks to Our View:

Slowdown in IT spending which could lead to lower orderbook; concerns on corporate governance issues.

#### At A Glance

Issued Capital (m shrs)	2,589
Mkt. Cap (S\$m/US\$m)	647 / 455
Major Shareholders (%)	
Goh Peng Ooi	68.0
Ntasian Discovery Master Fund	5.1
HNA Group Co Ltd	5.0
Free Float (%)	21.9
3m Avg. Daily Val (US\$m)	0.74

**GIC Industry :** Information Technology / Software & Services



Live more, Bank less

## WHAT'S NEW

### 3Q20 net profit below expectations on weaker margins

**Lower project related revenue.** Silverlake reported group revenue of RM151.7m in 3Q20, 2% lower y-o-y, mainly due to lower contribution from project-related segments. The completion of a Thailand-based core banking transformation project in 4Q19, as well as lower progressive revenue recognised from a few major contracts secured in Malaysia and Thailand which are nearing completion, led to the overall decrease in project-related revenue. The decrease was partially offset by revenue contribution from the delivery of new core banking implementation contracts secured in Indonesia and Vietnam in 1H20, as well as a technology refresh contract secured in Malaysia in late FY19. The sale of software and hardware products, which is cyclical, was also lower at RM1.2m. For the 9-month period, group revenue recorded a 3% growth to RM506.8m, accounting for 72% of our forecasts.

**Strong recurring revenue.** Recurring revenue segments of maintenance, enhancement services and software-as-a-service recorded a y-o-y growth of 12% to RM120.7m in 3Q20, accounting for 80% of total revenue, and 74% for 9-month FY20.

### Summary of 9-month and 3Q20 results

(RM mln)	9-Mth to 31 Mar		3Q ended 31 Mar	
	9M20	YoY (%)	3Q20	YoY (%)
Revenue	506.8	+3	151.7	-2
Gross profit	304.2	0	82.8	-9
Other income	8.7	-73	2.3	-89
Operating expenses	-147.9	+16	-49.2	-4
Pretax profit	169.6	-19	36.8	-40
Income tax expense	-44.0	+43	-11.3	+36
Net profit	125.6	-29	25.6	-51
EBITDA	218.3	-11	53.4	-27

Source: DBS Bank; Company

### Segmental Revenue

Segment (RM mln)	9-Mth to 31 Mar		3Q ended 31 Mar	
	9M20	YoY (%)	3Q20	YoY (%)
Software licensing	52.5	-21	9.9	-54
Software project	51.2	-24	18.2	-4
svcs				
Maintenance & enhancement svcs	347.6	+10	111.4	+13
Sale of software and hardware	21.6	+294	1.2	-74
Credit and cards processing	4.7	-51	1.6	+12
SaaS – Insurance processing	28.8	+17	9.1	+5

Source: DBS Bank; Company

**Weaker gross margins due to change in revenue mix.** The decrease in gross profit margin to 54.8% in 3Q20, vs 59.0% in 3Q19, was mainly due to a change in revenue mix, in particular, lower software licensing revenue. Nine-month FY20 gross margin was 60%, compared to 62% in 9-month FY19.

**Bottom line affected by lower other income, higher tax rate and higher operating expenses.** A lower other income of RM8.7m was recorded for 9-month FY20. In FY19, the Group reported other income of RM31.7m, which was attributable to the reversal of value-added tax and some disposal gains. The increase in income tax expense was mainly due to the expiry of pioneer status of a Malaysian subsidiary effective 1Q20, higher taxable income from certain subsidiaries, as well as higher withholding tax on overseas revenue. Operating expenses were also 16% higher due to the consolidation of XIT Group that was acquired last year, and also increase in finance costs from the unwinding of discount on contingent consideration payable for acquisitions and infrastructure investment. Overall, 9-month net profit of RM125.6m (-29% y-o-y) accounted for 68% of our FY20 forecasts, below expectations. The 3Q20 net profit of RM25.6m was down 51% y-o-y.

**No material disruptions from COVID-19; secured RM65m new contracts in 3Q20.** There were no material disruptions to the Group's operations in 9-month FY20 and the Group continued to deliver on existing contracts as well as secured a number of new contracts. A total of RM65m of new contracts was closed in 3Q20. We continue to expect the Group to secure smaller projects in 4Q20 in the range of

**Silverlake Axis**

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RM50-70m. Large deals, however, continue to be a challenge to close, with many being delayed by the movement restriction measures or economic uncertainties. Orderbook backlog remains at close to RM300m.

**Cut FY20F/FY21F earnings by 18%/19%.** We have cut FY20F/21F earnings by 18%/19% mainly on a lower gross margin assumption of 56% (vs 62% previously) as we expect the smaller contracts to have lower licensing revenue, and thereby narrower margins. The impact from the lower gross margins is partly offset by the group's restructuring programmes to rationalise costs and to improve efficiencies from operations.

**Maintain BUY, valuations attractive at -1SD level.** At the current level, Silverlake is trading at an attractive PE of 13.5x for FY20F and 11.8x for FY21F, near its -1SD level of its average 4-year forward PE. TP is adjusted to S\$0.38 (previously S\$0.48), which is pegged to its average PE level of 20x.

We maintain a dividend payout ratio of 60% (similar to 59% in FY19), which works out to a DPS of 1.1 Scts (1.77 Scts in FY19) or yield of 4.5%. Silverlake prefers to conserve cash, especially during the current uncertainties due to COVID-19.

## CRITICAL DATA POINTS TO WATCH

### Critical Factors

#### Contract wins

Order backlog remains close to RM300m currently. Large deals continue to be a challenge to close, with many delayed by the movement restriction measures or economic uncertainties but the group is still able to secure smaller ones to fill the gap. Silverlake can leverage on its market leader position to secure more contracts.

More orders could be in the pipeline, albeit smaller ones, as customers move to equip themselves with the technology to face the challenges of digital disruptions and to compete effectively in the digital economy ecosystem. This should lead to an improvement in project-related revenues (non-recurring revenue) going forward, while we project the maintenance and enhancement services and insurance software-as-a-service (recurring revenue) to expand at a high single digit of about 8-10% to generate a healthy increase in recurring revenues.

#### Capital expenditure for financial institutions

Financial institutions are going through enhancements to avoid being rendered obsolete by the rising Fintech trend. Worldwide Fintech spending is expected to grow at a CAGR of 4.1% during the 2015-2020 period. We expect Silverlake to ride on the Fintech trend.

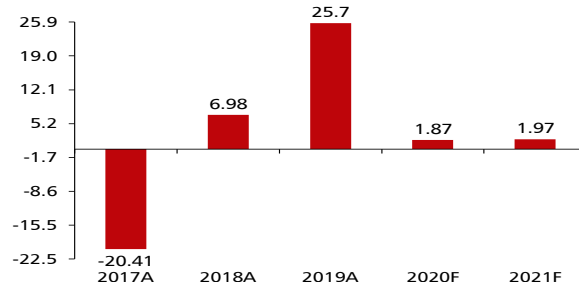
#### M&A to strengthen Silverlake as Fintech innovation accelerator

In the last 10 years, the Group has undertaken seven acquisitions to broaden its suite of business enterprise software solutions and service offerings and strengthen its market position in new markets. However, the Group prefers not to have any interested party transactions (IPT). In the past, IPT with Chairman Mr Goh's private companies had raised concerns on corporate governance issues.

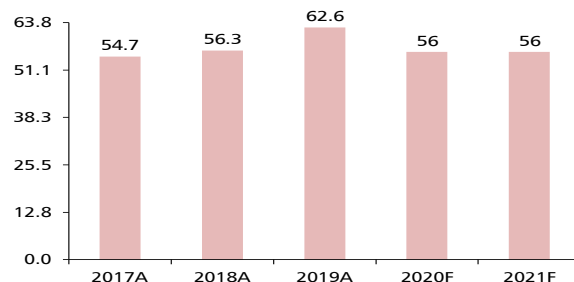
#### Scaling up as an Insurtech market leader

Silverlake's insurance arm, Merimen, generates high recurring income for the Group. Going forward, Merimen's growth is expected to be driven by increased ecosystem participation and cross-selling opportunities. A continuously changing regulatory and operational landscape in the insurance industry will provide opportunities to support growth for Merimen.

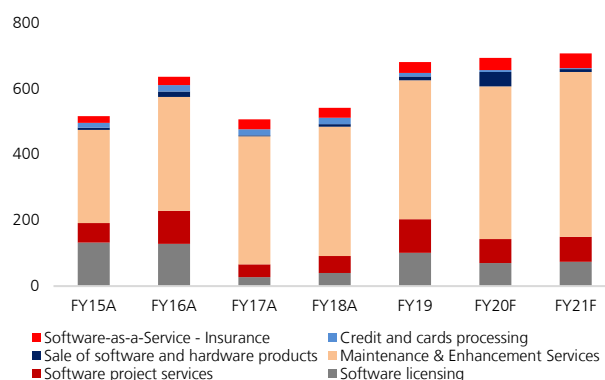
Revenue growth (%)



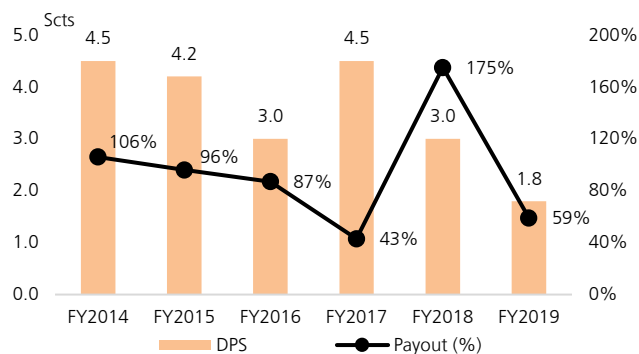
Gross Margins (%)



Revenue Breakdown By Segment (RM mln)



DPS and dividend payout ratio



Source: Company, DBS Bank

## Silverlake Axis

### Balance Sheet:

**Healthy net cash level to support dividend payout.** Silverlake's healthy net cash level has enabled the Group to maintain an attractive dividend payout ratio of about 60%. We expect this trend to continue.

### Share Price Drivers:

#### Growing project orderbook

More orders could be in the pipeline, albeit smaller ones, as customers move to equip themselves with the technology to face the challenges of digital disruptions and to compete effectively in the digital economy ecosystem. This should lead to an improvement in project-related revenues going forward.

#### Dividend payout

Silverlake's healthy net cash level has enabled the Group to maintain an attractive dividend payout ratio of about 60%. We expect this trend to continue. This translates into a dividend yield of about 4-5%. However, given the current economic uncertainties, the Group would prefer to conserve cash.

### Key Risks:

#### Slowdown in IT spending which could lead to a lower orderbook

A slowdown in this industry would lead to financial institutions cutting back on their spending on IT.

#### Concerns on corporate governance issues

Interested party transactions (IPT) with Mr Goh's private companies over the past few years have raised concerns on corporate governance.

#### Exposure mainly in Asia

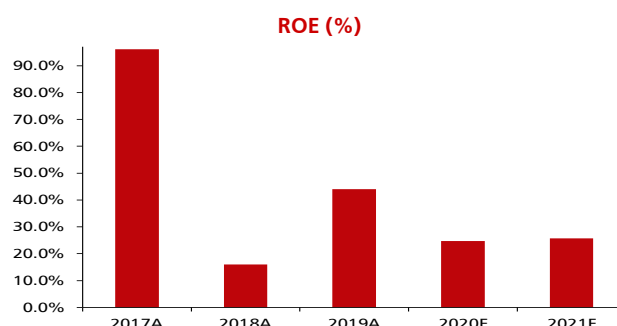
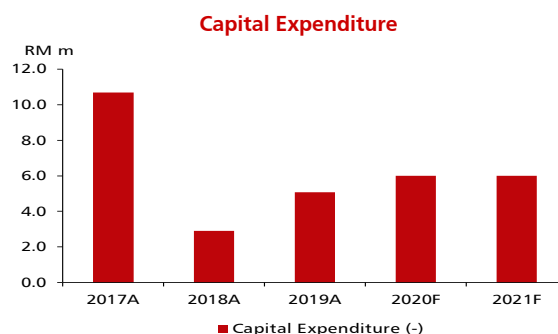
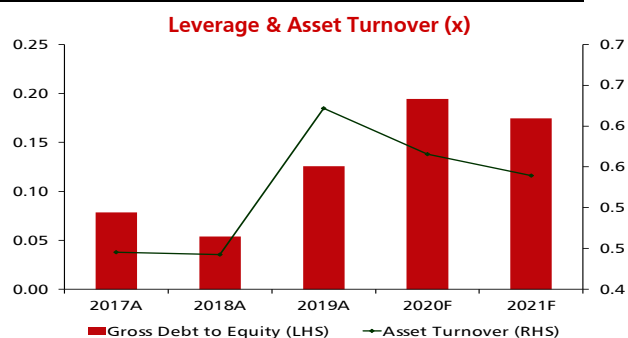
More than 90% of the total revenue is generated from Asia.

### Environment, Social, Governance:

As a technology service provider, e-waste treatment is of utmost importance. Silverlake has established an E-waste Policy to facilitate its in-house e-waste management, to reduce operational cost and increase resource efficiency. Processes and procedures have been instituted and are being constantly reviewed and revised to ensure effective corporate governance.

### Company Background

Silverlake Axis (Silverlake) is the market leader in core banking software in ASEAN where it deploys its proprietary software to major organisations in banking, insurance, payments, retail and logistics industries. It is also an Insurtech market leader in providing collaborative and information exchange platforms for the insurance industry.



Source: Company, DBS Bank

## Key Assumptions

FY Jun	2017A	2018A	2019A	2020F	2021F
Revenue growth (%)	(20.4)	6.98	25.7	1.87	1.97
Gross Margins (%)	54.7	56.3	62.6	56.0	56.0

## Segmental Breakdown

FY Jun	2017A	2018A	2019A	2020F	2021F
<b>Revenues (RMm)</b>					
Software Licensing	26.8	40.0	101	70.5	74.0
Software Project Services	389	51.8	103	72.0	75.6
Maintenance & Enhancement Svcs	39.1	392	422	464	501
Sale of Software & Hardware Pdts	18.8	8.04	11.0	44.2	8.83
Others	3.43	19.6	11.0	5.49	2.75
<b>Total</b>	<b>506</b>	<b>542</b>	<b>681</b>	<b>694</b>	<b>707</b>

## Income Statement (RMm)

FY Jun	2017A	2018A	2019A	2020F	2021F
Revenue	506	542	681	694	707
Cost of Goods Sold	(229)	(237)	(255)	(305)	(311)
<b>Gross Profit</b>	<b>277</b>	<b>305</b>	<b>426</b>	<b>388</b>	<b>396</b>
Other Opng (Exp)/Inc	675	(143)	(171)	(148)	(146)
<b>Operating Profit</b>	<b>952</b>	<b>162</b>	<b>255</b>	<b>241</b>	<b>250</b>
Other Non Opng (Exp)/Inc	0.0	0.0	0.0	0.0	0.0
Associates & JV Inc	(7.7)	(15.9)	(1.7)	0.0	0.0
Net Interest (Exp)/Inc	2.80	1.51	(23.8)	(26.0)	(6.0)
Exceptional Gain/(Loss)	0.0	0.0	55.6	0.0	0.0
<b>Pre-tax Profit</b>	<b>947</b>	<b>147</b>	<b>285</b>	<b>215</b>	<b>244</b>
Tax	(101)	(13.1)	(39.2)	(62.3)	(70.9)
Minority Interest	0.0	0.0	0.01	0.0	0.0
Preference Dividend	0.0	0.0	0.0	0.0	0.0
<b>Net Profit</b>	<b>846</b>	<b>134</b>	<b>246</b>	<b>153</b>	<b>174</b>
Net Profit before Except.	846	134	190	153	174
EBITDA	963	167	277	265	274
<b>Growth</b>					
Revenue Gth (%)	(20.4)	7.0	25.7	1.9	2.0
EBITDA Gth (%)	205.1	(82.7)	65.9	(4.4)	3.6
Opg Profit Gth (%)	220.3	(83.0)	57.7	(5.4)	4.0
Net Profit Gth (Pre-ex) (%)	208.9	(84.2)	41.7	(19.7)	13.8
<b>Margins &amp; Ratio</b>					
Gross Margins (%)	54.7	56.3	62.6	56.0	56.0
Opg Profit Margin (%)	188.1	29.8	37.4	34.7	35.4
Net Profit Margin (%)	167.1	24.7	36.1	22.0	24.5
ROAE (%)	96.1	16.0	44.0	24.8	25.7
ROA (%)	74.4	11.0	22.4	12.4	13.2
ROCE (%)	85.1	13.9	24.5	16.8	16.1
Div Payout Ratio (%)	43.0	175.0	59.3	60.0	60.0
Net Interest Cover (x)	NM	NM	10.7	9.3	41.7

Mainly due to impairment loss by joint venture entity, Silverlake HGH

Fair value adjustment for past acquisitions

Accounting adjustments tax reversal, disposal gain

High payout ratio in FY18 from proceeds of GIT sale

Source: Company, DBS Bank

## Quarterly / Interim Income Statement (RMm)

FY Jun	2Q2019	3Q2019	4Q2019	1Q2020	2Q2020
Revenue	169	154	189	164	191
Cost of Goods Sold	(60.9)	(63.1)	(67.8)	(59.2)	(74.5)
<b>Gross Profit</b>	<b>108</b>	<b>91.0</b>	<b>121</b>	<b>105</b>	<b>116</b>
Other Oper. (Exp)/Inc	(20.8)	(23.8)	(39.4)	(42.1)	(33.1)
<b>Operating Profit</b>	<b>87.3</b>	<b>67.2</b>	<b>82.1</b>	<b>63.1</b>	<b>83.1</b>
Other Non Opg (Exp)/Inc	0.0	0.0	0.0	0.0	0.0
Associates & JV Inc	(0.9)	(0.1)	(0.4)	0.97	0.42
Net Interest (Exp)/Inc	(5.8)	(6.2)	(6.0)	(7.3)	(7.5)
Exceptional Gain/(Loss)	0.0	0.0	0.0	0.0	0.0
<b>Pre-tax Profit</b>	<b>80.6</b>	<b>60.9</b>	<b>75.7</b>	<b>56.8</b>	<b>76.0</b>
Tax	(13.0)	(8.3)	(8.2)	(9.6)	(23.2)
Minority Interest	0.0	0.00	0.00	0.00	0.01
<b>Net Profit</b>	<b>67.5</b>	<b>52.6</b>	<b>67.5</b>	<b>47.2</b>	<b>52.8</b>
Net profit bef Except.	67.5	52.6	67.5	47.2	52.8
EBITDA	91.8	73.6	88.2	72.6	92.3

## Growth

Revenue Gth (%)	1.4	(8.8)	22.8	(13.1)	16.0
EBITDA Gth (%)	16.5	(19.7)	19.8	(17.7)	27.1
Opg Profit Gth (%)	18.5	(23.0)	22.1	(23.1)	31.7
Net Profit Gth (Pre-ex) (%)	16.6	(22.0)	28.1	(30.0)	11.9

## Margins

Gross Margins (%)	63.9	59.0	64.2	64.0	60.9
Opg Profit Margins (%)	51.6	43.6	43.3	38.4	43.6
Net Profit Margins (%)	40.0	34.2	35.6	28.7	27.7

## Balance Sheet (RMm)

FY Jun	2017A	2018A	2019A	2020F	2021F
Net Fixed Assets	19.1	20.4	14.9	16.2	17.6
Invt in Associates & JVs	0.0	9.67	8.62	8.62	8.62
Other LT Assets	228	223	317	341	330
Cash & ST Invt	701	498	623	685	773
Inventory	0.0	0.0	0.97	0.0	0.0
Debtors	145	139	134	137	140
Other Current Assets	349	117	83.6	83.6	83.6
<b>Total Assets</b>	<b>1,441</b>	<b>1,007</b>	<b>1,182</b>	<b>1,271</b>	<b>1,352</b>
ST Debt	89.3	25.4	11.3	11.3	11.3
Creditor	66.3	68.0	70.7	18.3	18.7
Other Current Liab	79.7	115	140	184	192
LT Debt	1.60	2.93	63.1	113	113
Other LT Liabilities	46.5	272	305	305	305
Shareholder's Equity	1,158	523	592	640	712
Minority Interests	0.10	0.08	0.06	0.06	0.06
<b>Total Cap. &amp; Liab.</b>	<b>1,441</b>	<b>1,007</b>	<b>1,182</b>	<b>1,271</b>	<b>1,352</b>
Non-Cash Wkg. Capital	348	72.4	7.94	18.6	12.4
Net Cash/(Debt)	610	470	549	560	648
Debtors Turn (avg days)	116.2	95.6	73.3	71.4	71.3
Creditors Turn (avg days)	100.1	113.7	109.7	57.7	23.5
Inventory Turn (avg days)	N/A	N/A	0.8	0.6	N/A
Asset Turnover (x)	0.4	0.4	0.6	0.6	0.5
Current Ratio (x)	5.1	3.6	3.8	4.2	4.5
Quick Ratio (x)	3.6	3.1	3.4	3.9	4.1
Net Debt/Equity (X)	CASH	CASH	CASH	CASH	CASH
Net Debt/Equity ex MI (X)	CASH	CASH	CASH	CASH	CASH
Capex to Debt (%)	11.8	10.3	6.8	4.8	4.8
Z-Score (X)	4.4	4.7	4.5	4.4	4.4

Includes software development expenditure, proprietary software and goodwill from acquisitions

Source: Company, DBS Bank

## Silverlake Axis

## Cash Flow Statement (RMm)

FY Jun	2017A	2018A	2019A	2020F	2021F
Pre-Tax Profit	947	147	285	215	244
Dep. & Amort.	18.3	21.3	24.0	24.0	24.0
Tax Paid	(101)	(20.0)	(40.2)	(62.3)	(70.9)
Assoc. & JV Inc/(loss)	7.70	15.9	1.72	0.0	0.0
Chg in Wkg.Cap.	(224)	271	58.5	(53.9)	(2.3)
Other Operating CF	(431)	(291)	(3.6)	0.0	0.0
<b>Net Operating CF</b>	<b>217</b>	<b>145</b>	<b>325</b>	<b>123</b>	<b>195</b>
Capital Exp.(net)	(10.7)	(2.9)	(5.1)	(6.0)	(6.0)
Other Invt.(net)	2.83	0.0	16.2	0.0	0.0
Invt in Assoc. & JV	0.0	(0.8)	(52.7)	0.0	0.0
Div from Assoc & JV	0.0	0.20	0.0	0.0	0.0
Other Investing CF	209	295	(30.2)	0.0	0.0
<b>Net Investing CF</b>	<b>201</b>	<b>292</b>	<b>(71.7)</b>	<b>(6.0)</b>	<b>(6.0)</b>
Div Paid	(237)	(387)	(152)	(105)	(101)
Chg in Gross Debt	11.6	127	37.1	50.0	0.0
Capital Issues	0.0	0.0	0.0	0.0	0.0
Other Financing CF	(17.5)	(305)	(17.9)	0.0	0.0
<b>Net Financing CF</b>	<b>(243)</b>	<b>(564)</b>	<b>(133)</b>	<b>(55.1)</b>	<b>(101)</b>
Currency Adjustments	20.4	11.2	17.7	0.0	0.0
Chg in Cash	196	(116)	138	61.6	88.2
Opg CFPS (S cts)	5.36	(1.5)	3.24	2.15	2.40
Free CFPS (S cts)	2.51	1.73	3.89	1.42	2.30

Source: Company, DBS Bank

## Target Price &amp; Ratings History



S.No.	Date of Report	Closing Price	12-mth Target Price	Rating
1:	15 May 19	0.52	0.63	BUY
2:	26 Aug 19	0.50	0.60	BUY
3:	15 Nov 19	0.43	0.57	BUY
4:	14 Feb 20	0.38	0.48	BUY

Note: Share price and Target price are adjusted for corporate actions.

Source: DBS Bank

Analyst: Lee Keng LING



DBS Bank recommendations are based on an Absolute Total Return\* Rating system, defined as follows:

**STRONG BUY** (>20% total return over the next 3 months, with identifiable share price catalysts within this time frame)

**BUY** (>15% total return over the next 12 months for small caps, >10% for large caps)

**HOLD** (-10% to +15% total return over the next 12 months for small caps, -10% to +10% for large caps)

**FULLY VALUED** (negative total return, i.e., > -10% over the next 12 months)

**SELL** (negative total return of > -20% over the next 3 months, with identifiable share price catalysts within this time frame)

*\*Share price appreciation + dividends*

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Sources for all charts and tables are DBS Bank unless otherwise specified.

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