

# Singapore Company Update

## SIA Engineering

Bloomberg: SIE SP | Reuters: SIAE.SI

Refer to important disclosures at the end of this report.

DBS Group Research . Equity

9 Nov 2021

### BUY Upgrade from HOLD

Last Traded Price (8 Nov 2021): S\$2.29 (STI : 3,263.90)  
Price Target 12-mth: S\$2.65 (16% upside) (Prev S\$2.05)

#### Analyst

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#### What's New

- 1HFY22 net profit of S\$25m in line with estimates, no room for dividends though
- Optimism on recovery prospects increase from launch of multiple VTLs in Singapore
- Recovery of air travel over next 2 years should lead to strong earnings rebound in FY23/24
- Upgrade to BUY with higher TP of S\$2.65

#### Price Relative



#### Forecasts and Valuation

FY Mar (S\$m)	2021A	2022F	2023F	2024F
Revenue	443	520	689	872
EBITDA	86.1	113	167	207
Pre-tax Profit	(35.6)	49.9	104	144
Net Profit	(11.2)	51.9	95.5	132
Net Pft (Pre Ex.)	40.3	51.9	95.5	132
Net Pft Gth (Pre-ex) (%)	(79.0)	28.8	84.0	38.0
EPS (S cts)	(1.0)	4.62	8.51	11.7
EPS Pre Ex. (S cts)	3.59	4.62	8.51	11.7
EPS Gth Pre Ex (%)	(79)	29	84	38
Diluted EPS (S cts)	(1.0)	4.59	8.44	11.7
Net DPS (S cts)	0.0	0.0	8.00	10.0
BV Per Share (S cts)	137	141	150	154
PE (X)	nm	49.5	26.9	19.5
PE Pre Ex. (X)	63.8	49.5	26.9	19.5
P/Cash Flow (X)	15.5	60.6	29.7	20.3
EV/EBITDA (X)	23.8	17.6	11.3	8.8
Net Div Yield (%)	0.0	0.0	3.5	4.4
P/Book Value (X)	1.7	1.6	1.5	1.5
Net Debt/Equity (X)	CASH	CASH	CASH	CASH
ROAE (%)	(0.7)	3.3	5.8	7.7
Earnings Rev (%):		2	(16)	-
Consensus EPS (S cts):		3.70	7.10	3.00
Other Broker Recs:		B: 1	S: 1	H: 1

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

### VTLs spur more optimism

#### Investment Thesis:

Upgrade to BUY, play on reopening of borders, though core profitability still some way away. The launch of Vaccinated Travel Lanes (VTL) between Singapore and Malaysia from end-November, in addition to other VTLs, should boost sentiment for the stock, and aid the slow recovery in flight traffic at Singapore Changi Airport, the main base for SIE's line maintenance operations. Accounting for better market sentiment, we raise our valuation pegs and revise up our target price (TP) to S\$2.65. However, note that core earnings turnaround is still a few quarters away. Despite the launch of more VTLs in Singapore, the absence of a domestic aviation market and delays in full opening of international borders in the region will continue to constrain SIE's earnings recovery over the next two quarters, as will the tapering of wage subsidies. Beyond that, earnings recovery in FY23/24 should be more material, as air traffic trends normalise.

Potential M&A target on the table provides excitement. SIE has signed an MoU to explore the acquisition of SR Technics Malaysia, which, if completed, will ensure SIE has a foothold in the higher growth narrow-body aircraft component MRO space, as compared to its current widebody fleet expertise.

Other key upside catalysts include privatisation potential, faster-than-expected rollouts of antiviral pills and speedy restoration of international flights. We are factoring in 20% privatisation premium in our TP.

#### Valuation:

Upgrade to BUY with higher TP of S\$2.65. The TP is based on a blended valuation framework (growth + cash flows).

#### Where we differ:

We remain cautious on the pace of recovery for SIE from the opening of VTLs in Singapore in the near term.

#### Key Risks to Our View:

Downside risk from lack of corporate actions and slower-than-expected opening up of regional borders.

#### At A Glance

Issued Capital (m shrs)	1,123
Mkt. Cap (S\$m/US\$m)	2,571 / 1,904
Major Shareholders (%)	
Temasek Holdings Pte Ltd	77.5
Free Float (%)	22.5
3m Avg. Daily Val (US\$m)	0.74
GIC Industry: Industrials / Transportation	



**WHAT'S NEW****Slow operational improvements to date**

2QFY22 net profits in line with expectations, supported by wage support grants. SIE booked net profits of S\$10.5m in 2QFY22, bringing 1HFY22 net earnings to S\$25.0m, accounting for around 50% of our full-year estimate. Excluding around S\$27m of government grants during the quarter, SIE would have incurred a core net loss of around S\$15.4m, which is moderately narrower compared to an estimated net loss (excluding wage subsidies) of S\$24.1m in 1QFY22. For 1HFY22, SIE recognised around S\$64.5m in Jobs Support Scheme (JSS) grants, compared to S\$95.7m recognised in 1HFY21. Thus, excluding JSS, SIE would have incurred a net loss of S\$39.5m in 1HFY22. However, the wage support is only available until early 2022, according to management indications. We believe total government support (from the Enhanced job support scheme and Aviation Workforce Retention Grant) covered 50% of monthly wages during the quarter but will taper down to 30% and 10% over the next two quarters respectively.

**Slight improvement in work volumes in 2QFY22.** Group revenue was at S\$138.2m in 2QFY22, up 32.2% y-o-y (off a low base) and 10.3% q-o-q, led by higher airframe overhaul and line maintenance revenue. Line maintenance activity rose marginally, as the number of flights handled in 2QFY22 only showed a modest uptick to around 26% of pre-crisis levels from 24% in 1QFY22. Meanwhile, base maintenance activity levels were mixed, with the number of light checks declining 9.4% on a sequential basis, while heavy checks increased 19.0% during the same period. Unfortunately, the increase in heavy checks was partly offset by an increase in checks with lower work content. SIE's share of profits from associates and JVs was on-par y-o-y but fell 19% q-o-q, primarily driven by flattish work activity and lower government support.

**No dividend declared.** Like previous semi-annuals, SIE will not be paying out any dividends for this period, though net cash levels remained healthy at c.S\$600m as of end-1HFY22 (up from S\$532m as of end-FY21, as collection trends remained robust). Management has indicated that the resumption of dividends will be contingent on the company achieving profitability without any government grants, which we envisage will not occur in 2HFY22 either. Hence, we are not expecting any dividends to be declared for the full year FY22, similar to FY21. Dividends will likely be restored from 1HFY23 onwards.

**Launch of more VTLs in Singapore should boost activity levels for SIE as more flights resume.** The recently announced and imminent implementation of more VTLs in the near term is a key positive for the stock sentiment wise, though we believe that Singapore's current reopening trajectory is insufficient for SIE to turn profitable in the face of lower government support over the next two quarters. We note that existing VTL countries comprised less than 20% of total traffic in 2019. With Singapore-KL coming in now, that number should be boosted though. Furthermore, international flight activity in Asia Pacific remained muted as of September 2021, with the Delta variant still causing concern across many countries in the region. While there are early signs of the COVID wave ebbing in the region, we foresee that it will take more time for countries in the region to ease travel restrictions, given the COVID-zero strategy adopted by some countries and slow pace of vaccination in some countries in the region.

**Antiviral pill newsflow will be another catalyst for the aviation sector.** Recent positive news flow from Pfizer and Merck regarding their COVID-19 antiviral pills is certainly a game-changer and important for the world to treat the pandemic as endemic, but more time is required for these treatments to become mainstream.

**VTLs may not be adequate to push SIE back into the black (positive core net profits without JSS) immediately, but we see a return in flight activity close to normalcy by FY24.** We do not expect a sharp increase in flight activity levels over the next two quarters. Recovery will be in the medium term - over FY23 and FY24, for flight activity at Changi Airport to gradually return to more than 85% of pre-COVID levels. SIE's line maintenance division will continue to benefit from this, and parent company flights will likely resume at a faster pace than third-party customers. Hence, we are expecting net profit to double in FY23 and grow c.40% in FY24, though still below pre-COVID levels. SIE is also ramping up its internal engine services business by building capabilities for LEAP engines, which should help the growth trajectory. Inorganic growth through acquisitions is currently not factored in but could provide further upside to our earnings estimates.

Upgrade to BUY, SIE is a play on reopening of borders, though core profitability still some way away. Positive market sentiment driving recovery expectations to normalised levels in FY23/24, will lead to a re-rating. We revised up our target price (TP) to S\$2.65. The TP is based on a blended valuation framework (P/E, EV/EBITDA, dividend yield, and DCF). Dividends should be restored from FY23 onwards, in our view.

### Company Background

SIA Engineering (SIE) is a leading regional aircraft maintenance, repair, and overhaul (MRO) company with bases in Singapore and the Philippines. A comprehensive cluster of JVs with renowned OEMs allows it to provide a full suite of MRO services.

### Interim Income Statement (\$m)

FY Mar	1H2021	2H2021	1H2022	% chg yoy	% chg hoh
Revenue	223	220	264	18.2	19.8
Cost of Goods Sold	(250)	(218)	(270)	8.0	24.1
<b>Gross Profit</b>	<b>(27)</b>	<b>2</b>	<b>(7)</b>	<b>75.4</b>	<b>nm</b>
Other Oper. (Exp)/Inc	0	0	0	-	-
<b>Operating Profit</b>	<b>(27)</b>	<b>2</b>	<b>(7)</b>	<b>(75.4)</b>	<b>(403.5)</b>
Other Non Opg (Exp)/Inc	0	0	0	-	-
Associates & JV Inc	28	12	27	(5.5)	133.4
Net Interest (Exp)/Inc	1	0	0	-	-
Exceptional Gain/(Loss)	(41)	(11)	0	99.5	(98.1)
<b>Pre-tax Profit</b>	<b>(38)</b>	<b>3</b>	<b>20</b>	<b>nm</b>	<b>686.4</b>
Tax	11	5	5	(51.2)	4.4
Minority Interest	8	0	0	(99.5)	-
<b>Net Profit</b>	<b>(19)</b>	<b>8</b>	<b>25</b>	<b>nm</b>	<b>220.9</b>
Net profit bef Except.	22	19	25	17.4	34.3
EBITDA	39	14	52	32.7	279.8
<b>Margins (%)</b>					
Gross Margins	(12.2)	1.0	(2.5)		
Opg Profit Margins	(12.2)	1.0	(2.5)		
Net Profit Margins	(8.5)	3.5	9.5		

Source of all data: Company, DBS Bank

### Company operating statistics at the Singapore base

	1QFY21	2QFY21	3QFY21	4QFY21	1QFY22	2QFY22	y-o-y change	q-o-q change
Flights handled at Changi Airport by line maintenance	4,952	6,320	7,807	8,648	9,755	10,990	74%	13%
Number of heavy checks performed at Singapore base	15	9	16	20	21	25	178%	19%
Number of light checks performed at Singapore base	54	55	53	61	85	77	40%	-9%
Fleet size managed by fleet management business	86	82	79	80	79	77	-6%	-3%

Source: Company

**Blended valuation summary**

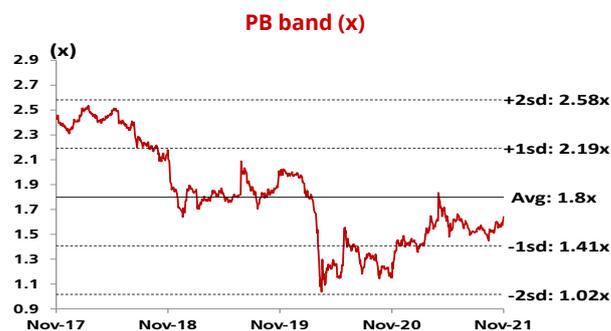
Method	Basis (FY22/23 blended)	Peg	Equity Value (S\$m)	Comments
P/E	73.7	24.0	1769	Peer valuations
EV/EBITDA	68.7	14.0	2386	Peer valuations
DCF			3408	7.4% WACC, 2% terminal growth
<b>Average (S\$m)</b>			<b>2521</b>	
Share cap			1123	
<b>Value per share (S\$)</b>			<b>2.20</b>	
Add: Privatisation Premium			20%	
<b>Target price (S\$)</b>			<b>2.65</b>	

Source: DBS Bank estimates

**Historical PE and PB band**



Source: Bloomberg Finance L.P., DBS Bank estimates



Source: Bloomberg Finance L.P., DBS Bank estimates

**Key Assumptions**

FY Mar	2020A	2021A	2022F	2023F	2024F
Airframe overhaul and line	879	377	443	590	761
Fleet management revenue	88.4	51.7	48.0	64.0	72.0
Engine & component	26.4	14.7	29.4	35.3	38.8
Profit from associates & JVs	128	39.9	62.3	81.0	89.1

**Income Statement (\$m)**

FY Mar	2020A	2021A	2022F	2023F	2024F
Revenue	994	443	520	689	872
Cost of Goods Sold	(926)	(468)	(534)	(668)	(819)
<b>Gross Profit</b>	<b>67.7</b>	<b>(25.0)</b>	<b>(13.8)</b>	<b>21.2</b>	<b>52.7</b>
Other Opng (Exp)/Inc	0.0	0.0	0.0	0.0	0.0
<b>Operating Profit</b>	<b>67.7</b>	<b>(25.0)</b>	<b>(13.8)</b>	<b>21.2</b>	<b>52.7</b>
Other Non Opng (Exp)/Inc	0.0	0.0	0.0	0.0	0.0
Associates & JV Inc	128	39.9	62.3	81.0	89.1
Net Interest (Exp)/Inc	6.60	1.00	1.42	1.77	2.55
Exceptional Gain/(Loss)	2.30	(51.5)	0.0	0.0	0.0
<b>Pre-tax Profit</b>	<b>205</b>	<b>(35.6)</b>	<b>49.9</b>	<b>104</b>	<b>144</b>
Tax	(14.0)	16.0	0.0	(10.4)	(14.4)
Minority Interest	3.30	8.40	2.00	2.00	2.00
Preference Dividend	0.0	0.0	0.0	0.0	0.0
<b>Net Profit</b>	<b>194</b>	<b>(11.2)</b>	<b>51.9</b>	<b>95.5</b>	<b>132</b>
Net Profit before Except.	192	40.3	51.9	95.5	132
EBITDA	272	86.1	113	167	207
<b>Growth</b>					
Revenue Gth (%)	(2.6)	(55.4)	17.4	32.6	26.4
EBITDA Gth (%)	11.2	(68.3)	31.8	47.3	23.7
Opg Profit Gth (%)	19.2	(136.9)	(44.8)	(253.4)	148.8
Net Profit Gth (Pre-ex) (%)	6.5	(79.0)	28.8	84.0	38.0
<b>Margins &amp; Ratio</b>					
Gross Margins (%)	6.8	(5.6)	(2.7)	3.1	6.0
Opg Profit Margin (%)	6.8	(5.6)	(2.7)	3.1	6.0
Net Profit Margin (%)	19.5	(2.5)	10.0	13.9	15.1
ROAE (%)	12.3	(0.7)	3.3	5.8	7.7
ROA (%)	10.1	(0.6)	2.8	4.9	6.2
ROCE (%)	3.7	(1.5)	(0.8)	1.1	2.6
Div Payout Ratio (%)	46.4	N/A	0.0	94.0	85.1
Net Interest Cover (x)	NM	NM	NM	NM	NM

Source: Company, DBS Bank

**Interim Income Statement (\$\$m)**

FY Mar	1H2020	2H2020	1H2021	2H2021	1H2022
Revenue	513	481	223	220	264
Cost of Goods Sold	(475)	(451)	(250)	(218)	(270)
<b>Gross Profit</b>	<b>37.3</b>	<b>30.4</b>	<b>(27.2)</b>	<b>2.20</b>	<b>(6.7)</b>
Other Oper. (Exp)/Inc	0.0	0.0	0.0	0.0	0.0
<b>Operating Profit</b>	<b>37.3</b>	<b>30.4</b>	<b>(27.2)</b>	<b>2.20</b>	<b>(6.7)</b>
Other Non Op (Exp)/Inc	0.0	0.0	0.0	0.0	0.0
Associates & JV Inc	53.4	74.5	28.4	11.5	26.8
Net Interest (Exp)/Inc	3.70	2.90	1.20	(0.2)	(0.3)
Exceptional Gain/(Loss)	2.40	(0.1)	(40.5)	(11.0)	(0.2)
<b>Pre-tax Profit</b>	<b>96.8</b>	<b>108</b>	<b>(38.1)</b>	<b>2.50</b>	<b>19.7</b>
Tax	(10.0)	(4.0)	10.9	5.10	5.32
Minority Interest	0.80	2.50	8.20	0.20	0.04
<b>Net Profit</b>	<b>87.6</b>	<b>106</b>	<b>(19.0)</b>	<b>7.80</b>	<b>25.0</b>
Net profit bef Except.	85.2	106	21.5	18.8	25.2
EBITDA	128	142	39.2	13.7	52.0
<b>Growth</b>					
Revenue Gth (%)	0.2	(6.1)	(53.7)	(1.3)	19.8
EBITDA Gth (%)	(4.3)	11.1	(72.4)	(65.1)	279.8
Op (Exp) Profit Gth (%)	5.7	(18.5)	(189.5)	(108.1)	(403.5)
Net Profit Gth (%)	6.3	21.2	(117.9)	(141.1)	220.9
<b>Margins</b>					
Gross Margins (%)	7.3	6.3	(12.2)	1.0	(2.5)
Op (Exp) Profit Margins (%)	7.3	6.3	(12.2)	1.0	(2.5)
Net Profit Margins (%)	17.1	22.1	(8.5)	3.5	9.5

Includes S\$64.5m  
wage subsidies

**Balance Sheet (\$\$m)**

FY Mar	2020A	2021A	2022F	2023F	2024F
Net Fixed Assets	328	241	216	191	166
Invts in Associates & JVs	617	602	618	639	663
Other LT Assets	62.5	40.4	40.4	40.4	40.4
Cash & ST Invts	520	616	664	771	834
Inventory	274	137	160	213	269
Debtors	60.3	34.8	40.8	54.1	68.5
Other Current Assets	144	139	139	139	139
<b>Total Assets</b>	<b>2,006</b>	<b>1,810</b>	<b>1,879</b>	<b>2,047</b>	<b>2,179</b>
ST Debt	27.2	28.8	28.8	28.8	28.8
Creditor	194	168	197	261	349
Other Current Liab	19.7	12.4	2.80	13.2	17.2
LT Debt	85.2	55.3	55.3	55.3	55.3
Other LT Liabilities	18.5	1.20	1.20	1.20	1.20
Shareholder's Equity	1,629	1,534	1,586	1,681	1,723
Minority Interests	32.2	10.6	8.60	6.60	4.60
<b>Total Cap. &amp; Liab.</b>	<b>2,006</b>	<b>1,810</b>	<b>1,879</b>	<b>2,047</b>	<b>2,179</b>
Non-Cash Wkg. Capital	265	130	140	131	110
Net Cash/(Debt)	407	532	580	687	749
Debtors Turn (avg days)	26.0	39.2	26.6	25.2	25.7
Creditors Turn (avg days)	88.7	166.4	142.1	138.7	147.6
Inventory Turn (avg days)	105.9	188.9	115.7	112.9	116.6
Asset Turnover (x)	0.5	0.2	0.3	0.4	0.4
Current Ratio (x)	4.1	4.4	4.4	3.9	3.3
Quick Ratio (x)	2.4	3.1	3.1	2.7	2.3
Net Debt/Equity (X)	CASH	CASH	CASH	CASH	CASH
Net Debt/Equity ex MI (X)	CASH	CASH	CASH	CASH	CASH
Capex to Debt (%)	33.2	15.0	47.6	47.6	47.6
Z-Score (X)	5.7	6.5	5.9	5.9	5.9

Source: Company, DBS Bank

## Cash Flow Statement (\$m)

FY Mar	2020A	2021A	2022F	2023F	2024F
Pre-Tax Profit	205	(35.6)	49.9	104	144
Dep. & Amort.	76.1	71.2	65.0	65.0	65.0
Tax Paid	(18.1)	(12.7)	(9.6)	0.0	(10.4)
Assoc. & JV Inc/(loss)	(128)	(39.9)	(62.3)	(81.0)	(89.1)
Chg in Wkg.Cap.	(51.0)	126	(0.6)	(1.4)	16.8
Other Operating CF	7.50	57.1	0.0	0.0	0.0
<b>Net Operating CF</b>	<b>91.1</b>	<b>166</b>	<b>42.4</b>	<b>86.6</b>	<b>127</b>
Capital Exp.(net)	(37.3)	(12.6)	(40.0)	(40.0)	(40.0)
Other Invs.(net)	0.0	0.0	0.0	0.0	0.0
Invs in Assoc. & JV	4.80	0.0	0.0	0.0	0.0
Div from Assoc & JV	84.0	29.5	46.0	59.9	65.8
Other Investing CF	10.9	6.00	0.0	0.0	0.0
<b>Net Investing CF</b>	<b>62.4</b>	<b>22.9</b>	<b>6.05</b>	<b>19.9</b>	<b>25.8</b>
Div Paid	(123)	(56.1)	0.0	0.0	(89.8)
Chg in Gross Debt	(34.3)	(30.0)	0.0	0.0	0.0
Capital Issues	0.0	0.0	0.0	0.0	0.0
Other Financing CF	(1.9)	(3.7)	0.0	0.0	0.0
<b>Net Financing CF</b>	<b>(159)</b>	<b>(89.8)</b>	<b>0.0</b>	<b>0.0</b>	<b>(89.8)</b>
Currency Adjustments	4.00	(2.6)	0.0	0.0	0.0
Chg in Cash	(1.9)	96.3	48.4	106	62.7
Opg CFPS (S cts)	12.6	3.57	3.83	7.83	9.78
Free CFPS (S cts)	4.79	13.6	0.21	4.15	7.72

Source: Company, DBS Bank

## Target Price &amp; Ratings History



S.No.	Date of Report	Closing Price	12-mth Target Price	Rating
1:	01 Feb 21	1.87	1.80	HOLD
2:	26 Jul 21	2.08	2.05	HOLD

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

Source: DBS Bank

Analyst: Suvro SARKAR

Jason SUM, CFA

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

Completed Date: 9 Nov 2021 07:10:47 (SGT)

Dissemination Date: 9 Nov 2021 07:34:33 (SGT)

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

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