

SIA Engineering^(SIE SP)

Share Price: SGD3.66

MCap (USD): 2.9B

Singapore

Target Price: SGD3.61 (-1%)

ADTV (USD): 0.8M

Aviation

HOLD

 (Unchanged)

Unwinding the cross-holdings

- Restructuring its engine JVs with Rolls-Royce and HAECO. Net proceeds could lead to special DPS.
- Expect competitive pressures with change in business model.
- Trim TP 4% to SGD3.61 on EPS adjustments. Stock may react positively to the prospect of a special DPS. Maintain HOLD.

Restructuring its engine JVs

SIA Engineering (SIAEC) announced the restructuring of its engine JVs with Rolls-Royce (RR) and HAECO. In essence, SIAEC is divesting its 10% stake in HAESL and a 2% effective stake in SAESL for SGD201.9m in cash. It will book a net gain of SGD186.8m for FY3/16. As part of this restructuring, RR has also replaced its geographic territory based work arrangement with a competitive model, where each engine shop competes for overhaul work. Despite the shift in business model, RR has committed to a pre-determined amount of workload for SAESL from 2016 to 2030.

Near term positive; longer term more competitive

SIAEC could share part of the proceeds with shareholders. Assuming 50% of the proceeds are distributed, it may pay a special DPS of 9.0 SGD cts. Added to our forecasted core DPS of 14.5 SGD cts, FY3/16 payout could come to 23.5 SGD cts, a yield of 6.4%.

While the stock may react positively to the near-term prospects of a special DPS, we see a slight negative from a more competitive business landscape. Under the old regime, all Trent engine maintenance work in the Asia Pacific region is dominated by SAESL and HAESL. In the new regime however, all authorized engine shops can compete to secure maintenance work globally. Nonetheless, we are not overly concerned as the maintenance of Trent engines remains a very niche service offering.

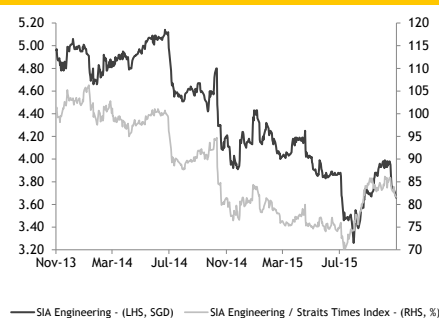
We build in the divestment gain as an exceptional item for FY16 and cut our F17-18E EPS by 4% to remove contributions from HAESL. Our TP is lowered to SGD3.61 (from SGD3.75), based on an unchanged 20x FY3/17 EPS. Maintain HOLD.

FYE Mar (SGD m)	FY14A	FY15A	FY16E	FY17E	FY18E
Revenue	1,178.2	1,120.6	1,140.0	1,178.8	1,218.9
EBITDA	152.6	126.8	139.9	146.3	164.3
Core net profit	265.7	183.3	175.2	202.7	246.2
Core EPS (cts)	23.8	16.3	15.5	17.9	21.8
Core EPS growth (%)	(2.3)	(31.5)	(4.7)	15.7	21.5
Net DPS (cts)	25.0	14.5	23.5	17.0	18.0
Core P/E (x)	15.4	22.5	23.6	20.4	16.8
P/BV (x)	3.0	3.1	2.7	2.8	2.7
Net dividend yield (%)	6.8	4.0	6.4	4.6	4.9
ROAE (%)	20.0	13.6	12.3	13.6	16.6
ROAA (%)	15.9	10.9	9.9	10.9	13.2
EV/EBITDA (x)	32.1	32.2	25.0	24.5	21.7
Net debt/equity (%)	net cash	net cash	net cash	net cash	net cash

Key Data

52w high/low (SGD)	4.43/3.26
3m avg turnover (USDm)	0.8
Free float (%)	22.3
Issued shares (m)	1,121
Market capitalization	SGD4.1B
Major shareholders:	
-Singapore Airlines Ltd.	77.6%
-Matthews Int Capital Management	2.4%
-Capital Research & Management Co.	0.8%

Share Price Performance



	1 Mth	3 Mth	12 Mth
Absolute (%)	(7.1)	7.3	(12.4)
Relative to index (%)	(1.8)	9.8	0.9

Maybank vs Market

	Positive	Neutral	Negative
Market Recs	1	4	1
	Maybank Consensus		% +/-
Target Price (SGD)	3.61	3.85	(6.1)
'16 PATMI (SGDm)	362	175	106.6
'17 PATMI (SGDm)	203	190	7.0

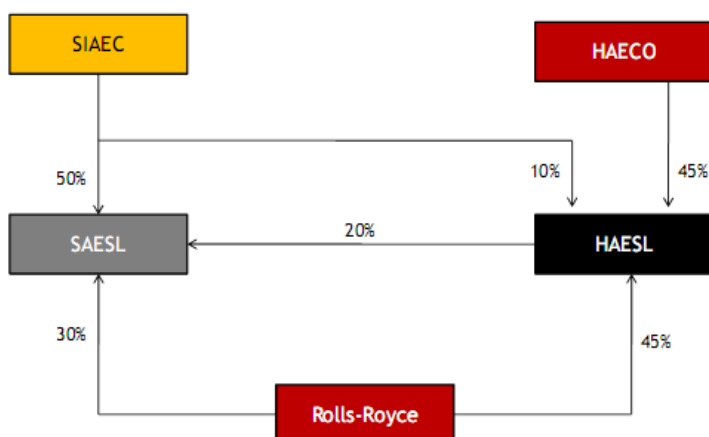
Source: FactSet; Maybank

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Key points:

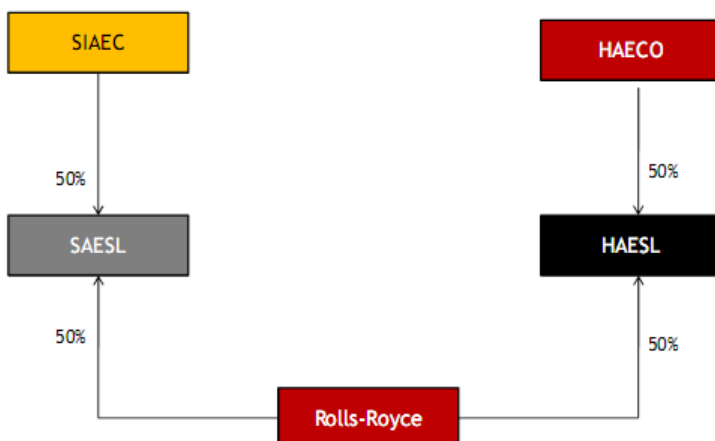
- SIAEC is divesting a 10% stake in HAESL and a 2% effective stake in SAESL for SGD201.9m in cash. This comprises SGD163.8m from the sale of its 10% stake in HAESL and SGD38.1m from the sale of HAESL's stake in SAESL.
- It will book a net gain of SGD186.8m for FY3/16.
- Following the restructuring, SIAEC will also amalgamate the business of SAESL and IECO, which is another 50:50 JV with RR, for better efficiency.
- As part of this restructuring, RR has also replaced its geographic territory based work arrangement with a competitive model, where each engine shop will compete for overhaul work. Despite the shift in business model, RR has committed to a pre-determined amount of workload for SAESL from 2016 to 2030.
- Competitive pressures for SAESL are mitigated by: 1) minimum workload committed by Rolls-Royce; 2) its parent has substantial orders of Trent engines; and 3) only a limited number of engine shops have the capabilities to service these engines.

Figure 1: Before restructuring



Source: Company

Figure 2: After restructuring



Source: Company

FYE 31 Mar	FY14A	FY15A	FY16E	FY17E	FY18E
Key Metrics					
P/E (reported) (x)	15.3	22.4	11.3	20.2	16.7
Core P/E (x)	15.4	22.5	23.6	20.4	16.8
P/BV (x)	3.0	3.1	2.7	2.8	2.7
P/NTA (x)	3.1	3.2	2.8	2.9	2.9
Net dividend yield (%)	6.8	4.0	6.4	4.6	4.9
FCF yield (%)	5.2	4.0	3.8	4.4	5.3
EV/EBITDA (x)	32.1	32.2	25.0	24.5	21.7
EV/EBIT (x)	42.3	48.6	35.8	34.7	29.6

INCOME STATEMENT (SGD m)

Revenue	1,178.2	1,120.6	1,140.0	1,178.8	1,218.9
Gross profit	1,141.2	1,077.8	1,097.8	1,135.6	1,175.0
EBITDA	152.6	126.8	139.9	146.3	164.3
Depreciation	(37.0)	(42.8)	(42.2)	(43.2)	(44.0)
EBIT	115.6	84.0	97.7	103.2	120.3
Net interest income / (exp)	15.1	9.2	8.7	2.5	2.1
Associates & JV	162.6	106.3	85.0	115.9	146.8
Exceptionals	0.0	0.0	186.8	0.0	0.0
Other pretax income	0.7	5.9	2.8	0.0	0.0
Pretax profit	294.0	205.4	381.0	221.6	269.2
Income tax	(23.0)	(20.0)	(16.9)	(16.4)	(19.0)
Minorities	(5.3)	(2.1)	(2.0)	(2.5)	(4.0)
Reported net profit	265.7	183.3	362.0	202.7	246.2
Core net profit	265.7	183.3	175.2	202.7	246.2

BALANCE SHEET (SGD m)

Cash & Short Term Investments	535.7	463.7	665.9	583.0	596.9
Accounts receivable	222.5	184.2	203.0	209.9	217.1
Inventory	106.9	124.6	127.3	129.3	131.7
Reinsurance assets	0.0	0.0	0.0	0.0	0.0
Property, Plant & Equip (net)	337.2	344.1	353.5	359.2	365.7
Intangible assets	54.3	61.5	64.9	68.2	71.4
Investment in Associates & JVs	435.9	463.9	472.2	484.9	502.3
Other assets	14.6	14.6	0.0	0.0	0.0
Total assets	1,707.1	1,656.6	1,886.7	1,834.6	1,885.1
ST interest bearing debt	8.2	9.3	9.3	9.3	9.3
Accounts payable	246.1	229.8	260.3	268.7	274.5
Insurance contract liabilities	0.0	0.0	0.0	0.0	0.0
LT interest bearing debt	13.6	23.9	23.9	23.9	23.9
Other liabilities	49.0	44.0	44.0	44.0	44.0
Total Liabilities	316.6	307.0	337.5	345.9	351.7
Shareholders Equity	1,360.9	1,324.9	1,524.3	1,463.5	1,507.9
Minority Interest	29.6	24.7	24.9	25.2	25.6
Total shareholder equity	1,390.5	1,349.6	1,549.2	1,488.6	1,533.4
Total liabilities and equity	1,707.1	1,656.6	1,886.7	1,834.6	1,885.1

CASH FLOW (SGD m)

Pretax profit	294.0	205.4	381.0	221.6	269.2
Depreciation & amortisation	37.0	42.8	42.2	43.2	44.0
Adj net interest (income)/exp	0.0	0.0	0.0	0.0	0.0
Change in working capital	(20.6)	(5.1)	9.0	(0.5)	(3.7)
Cash taxes paid	(23.6)	(23.3)	(16.9)	(16.4)	(19.0)
Other operating cash flow	0.0	0.0	0.0	0.0	0.0
Cash flow from operations	113.0	96.1	134.8	129.4	141.6
Capex	(72.8)	(53.2)	(55.0)	(52.2)	(53.8)
Free cash flow	212.6	164.9	156.6	180.4	217.3
Dividends paid	(244.9)	(269.0)	(162.6)	(263.5)	(201.9)
Equity raised / (purchased)	30.3	17.2	0.0	0.0	0.0
Perpetual securities	0.0	0.0	0.0	0.0	0.0
Change in Debt	16.1	8.8	0.0	0.0	0.0
Perpetual securities distribution	0.0	0.0	0.0	0.0	0.0
Other invest/financing cash flow	171.1	123.0	285.0	103.4	128.0
Effect of exch rate changes	0.0	5.1	0.0	0.0	0.0
Net cash flow	12.8	(77.1)	202.2	(82.9)	13.9

FYE 31 Mar	FY14A	FY15A	FY16E	FY17E	FY18E
Key Ratios					
Growth ratios (%)					
Revenue growth	2.7	(4.9)	1.7	3.4	3.4
EBITDA growth	(6.4)	(16.9)	10.3	4.6	12.3
EBIT growth	(9.7)	(27.3)	16.3	5.6	16.6
Pretax growth	(1.0)	(30.1)	85.5	(41.8)	21.5
Reported net profit growth	(1.6)	(31.0)	97.5	(44.0)	21.5
Core net profit growth	(1.6)	(31.0)	(4.4)	15.7	21.5
Profitability ratios (%)					
EBITDA margin	13.0	11.3	12.3	12.4	13.5
EBIT margin	9.8	7.5	8.6	8.8	9.9
Pretax profit margin	25.0	18.3	33.4	18.8	22.1
Payout ratio	nm	88.6	72.8	94.1	82.0
DuPont analysis					
Net profit margin (%)	22.6	16.4	31.8	17.2	20.2
Revenue/Assets (x)	0.7	0.7	0.6	0.6	0.6
Assets/Equity (x)	1.3	1.3	1.2	1.3	1.3
ROAE (%)	20.0	13.6	12.3	13.6	16.6
ROAA (%)	15.9	10.9	9.9	10.9	13.2
Liquidity & Efficiency					
Cash conversion cycle	nm	nm	nm	nm	nm
Days receivable outstanding	65.5	65.3	61.1	63.1	63.1
Days inventory outstanding	nm	nm	nm	nm	nm
Days payables outstanding	nm	nm	nm	nm	nm
Dividend cover (x)	1.0	1.1	1.4	1.1	1.2
Current ratio (x)	3.1	3.0	3.5	3.1	3.1
Leverage & Expense Analysis					
Asset/Liability (x)	5.4	5.4	5.6	5.3	5.4
Net debt/equity (%)	net cash	net cash	net cash	net cash	net cash
Net interest cover (x)	na	na	na	na	na
Debt/EBITDA (x)	0.1	0.3	0.2	0.2	0.2
Capex/revenue (%)	6.2	4.7	4.8	4.4	4.4
Net debt/ (net cash)	(513.9)	(430.5)	(632.7)	(549.8)	(563.7)

Source: Company; Maybank

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