



# CSE Global

(CSE SP/CSES.SI)

## Positive trends; attractive 5.5% dividend yield

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- CSE 4Q18 earnings (excluding one-off items) rose 17% YoY to S\$5.1mn, bringing full-year earnings to S\$20.1mn and above our S\$17.8mn estimates.
- We are positive on CSE's outlook on the back of 13-20% EPS growth in the next 3 years from better industry prospects and from synergies with its new major shareholder.
- Maintain BUY. CSE's valuations are attractive, trading at 12/11/9x 2019/20/21F EPS. We expect downside risks to be mitigated by its above-industry 5.5% dividend yield.

### Financials & Key Operating Statistics

YE Dec (\$\$ m)	2017	2018	2019F	2020F	2021F
Revenue	362.4	376.8	399.4	423.4	448.8
PATMI	-45.1	20.1	22.0	24.8	29.6
Core PATMI	-3.5	18.6	21.5	24.3	29.1
Core EPS	-0.7	3.6	4.2	4.7	5.6
Core EPS grth (%)	-117.1	-629.5	15.4	13.3	19.6
Core P/E (x)	-73.5	13.9	12.0	10.6	8.9
DPS (SGCents)	2.8	2.8	2.8	2.8	2.8
Div Yield (%)	5.5	5.5	5.5	5.5	5.5
Net Margin (%)	-12.5	5.3	5.5	5.9	6.6
Gearing (%)	-8.8	-22.0	-0.5	0.9	-0.6
Price / Book (x)	1.5	1.5	1.4	1.4	1.3
ROE (%)	-25.7	11.7	12.2	13.0	14.4

Source: Company Data, KGI Research

**4Q18 review.** CSE reported a 4Q18 net profit of S\$5.1mn compared to a loss of S\$37.1mn in 4Q17. Excluding the one-off items in 4Q17, core net profit rose 17.1%. 4Q18 gross profit margin rose to a two-year high of 30.2% due to project mix, otherwise average margins in 9M18 was around 27%, which is an improvement from FY17's 26% gross profit margin. It declared 1.5 SG cents final dividend, bringing the full-year dividend to 2.75 SG cents. Although the full-year dividend is similar to the prior year, FY18's 1.50 SG cents final is a step-up from FY17's 1.0 final and 0.50 cents special.

**Healthy order book.** CSE won S\$384mn of new orders in FY18 and closed the year with S\$181mn of net orderbook. The new orders were in line with our expectations and brings its net order book to a similar level as FY15. New order wins bottomed in FY16 at S\$287mn and has been on an uptrend since then. We expect CSE to secure S\$400mn in new orders in FY19F, before stabilising at S\$450 p.a. thereafter.

**Diversification.** The recent order wins of a total combined S\$84mn infrastructure work reinforces our view of CSE's value-added proposition to clients in the infrastructure sector in Singapore and Australia. Our site visit to CSE's Australian facilities in September 2018 (please refer to report published on 8-Oct-18) further strengthened our view of the recovery in Australia's O&G, mining and infrastructure sectors. On future growth, the group is actively looking for earnings accretive acquisitions and is in the process of registering to be a supplier to Petronas.

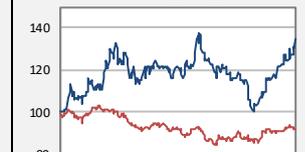
### Buy - Maintain

Price as of 1 Mar 19 (SGD)	0.50	<b>Performance (Absolute)</b>	
12M TP (\$)	0.58	1 Month (%)	11.1
Previous TP (\$)	0.57	3 Month (%)	11.6
Upside, incl div (%)	22%	12 Month (%)	44.1

### Trading data

Mkt Cap (\$mn)	254
Issued Shares (mn)	509
Vol - 3M Daily avg (mn)	1.3
Val - 3M Daily avg (\$mn)	0.6
Free Float (%)	71.5%

### Perf. vs STI Index (Red)



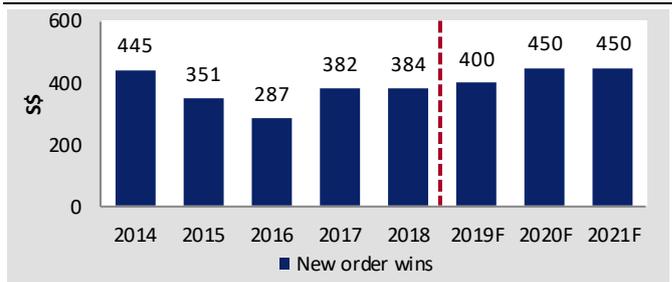
### Major Shareholders

Serba Dinamik	25.0%
Fidelity Mgt & Research	10.1%

### Previous Recommendations

16-Jan-19	BUY \$0.57
8-Oct-18	BUY \$0.57

Figure 1: Order wins - potential to surpass



Source: Company data, KGI Research

**Sustainable 5.5% dividend yield.** CSE It has consistently paid 2.75 SG cents p.a. over the past 5 years. We estimate that CSE can sustain this dividend amount going forward as balance sheet remains in net cash position of S\$38mn while free cash flows are sufficient to cover the annual dividend payout of S\$14mn.

**Valuation & Action:** CSE is currently trading at 13/11/9x 2019/20/21F EPS, which is attractive in our view given its solid balance sheet, asset light model and stable recurring free cash flows. We thus maintain our **BUY** recommendation and believe that average EPS growth of around 16% p.a. over the next 3 years is achievable on the back of improving industry dynamics.

**Risks:** Margin pressure due to competition and lower-than-expected new order wins. Foreign exchange risks due to its exposure to USD, AUD and EUR.

## Investment Thesis

We believe markets may be undervaluing CSE's key businesses as we see several positive trends that could cause a share price re-rating over the next few quarters:

- There has been a dramatic increase in US oil production, a majority from shale production such as in the Permian basin. Hence, we see significant upside to margins and earnings from its US operations, which mainly serves the O&G sector.
- CSE's infrastructure business has been a bright spot, contributing S\$15mn or around 55-77% of EBIT in FY2017 and FY2018. It is currently working and bidding for mining and infrastructure projects in Australia. After our site visit to Australia, we are more confident of the growth prospects of CSE in the country as it has made significant inroads into the 2-way radio communications through its acquisitions.
- Re-entry into the Middle East with its new shareholder, Serba Dinamik, which could boost its order book. CSE scaled down its Middle East operations in past years due to issues with clients' payment. But with Serba Dinamik now as a strong partner, CSE would be in a better position to once again capitalise on the world's largest oil producing region.

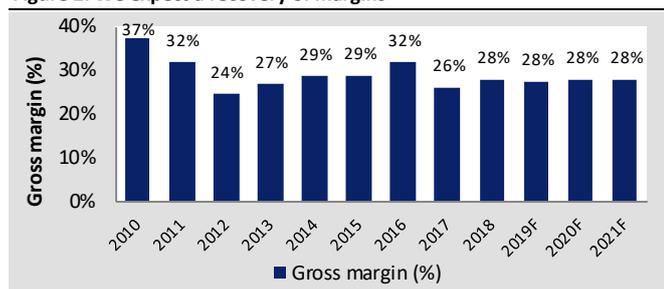
## Valuations

A peer comparison study may not accurately capture the value that CSE should be trading at, given the wide mix of geographical segment (SG, US, AU and potentially in MENA) that it operates in and the business mix that it has.

As such, our valuation method for CSE involves a blended use of historical P/E and P/B multiples with a heavier weighting on P/B for now. The reason for giving P/B multiple a heavier weight is that the company may only hit full earnings growth potential in FY2020F, where we expect O&G capex and opex to recover to levels that would benefit CSE's core business and provide a meaningful margin uplift.

**Improving margins.** Gross profit margins in FY2017 declined to 26% from an average of 30% during FY2010 to FY2015 and recently recovered to 28% in FY2018. Although the O&G service industry is still plague by overcapacity, we are seeing indications that supply and demand is balancing. Thus, it is not unreasonable to expect gross margins to stabilise at around 28% or higher going forward.

Figure 2: We expect a recovery of margins



Source: Company data, KGI Research

**Blended P/E and P/B valuations.** We applied a 20% discount to the +1SD multiples of CSE's 10-year historical average for both P/E and P/B valuation metrics, and derived a fair value of \$0.53 based on 12.5x 2019F P/E and \$0.62 based on 2.1x 2019F P/B. Our blended TP based on 40% weighting for P/E and 60% on P/B valuation resulted in a fair value of \$0.58. Including an attractive dividend yield of 5.5%, we derive total potential upside of 22%.

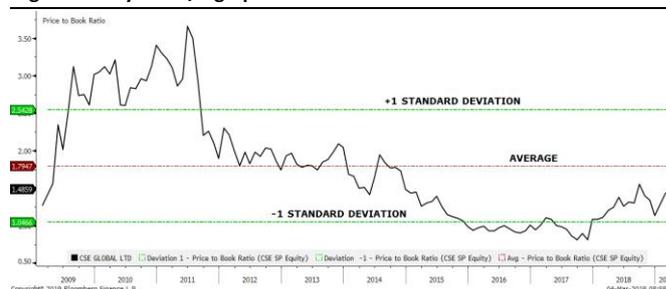
Figure 3: Blended P/E and P/B based valuation for CSE

Blended valuation	Remarks
PE-based TP	\$0.53 Based on 12.5x P/E, 20% disc to +1SD above 10-yr avg
PB-based TP	\$0.62 Based on 2.1x P/B, 20% disc to +1SD above 10-yr avg
Weight P/E	40%
Weight P/B	60% Higher weight to P/B based multiple
P/E	\$0.21
P/B	\$0.37
Blended TP	\$0.58
Upside/(Downside)	17%
Dividend yield	5.5%
Upside, inc div	22%

Source: KGI Research

**P/B valuation still below 10-year average.** Despite improving industry and company fundamentals for CSE, its valuations are still close to 1SD below its 10-year average. We expect valuations to re-rate higher on improving earnings across its three business segments (O&G, Infrastructure and Mining & Mineral).

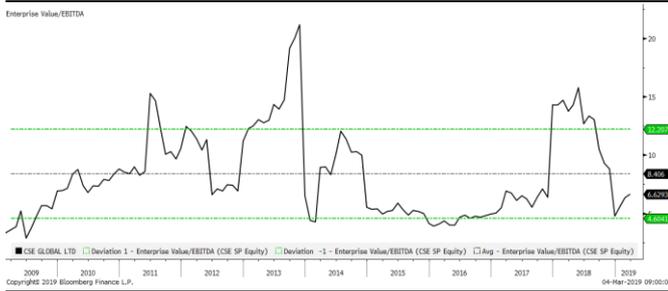
Figure 4: 10-years P/B graph



Source: Bloomberg, KGI Research

## Appendix: Additional charts and tables

Figure 5: CSE's 10-year EV/EBITDA graph



Source: Bloomberg, KGI Research

**CSE's segments.** CSE's diversification into Australia's infrastructure segment managed to offset the decline in O&G and Mining & Minerals. Infrastructure EBIT accounted for 78% of the group's FY2017 EBIT. In FY2018, its infrastructure segment's EBIT has remained stable and overall EBIT was helped by the recovery in its O&G business, particularly in the US.

Figure 6: CSE's segmental operating profit

S\$m	FY 2018	FY 2017	Var %
Oil & Gas	12.0	4.8	152.3%
Infrastructure	14.6	15.1	-3.7%
Mining & Mineral	0.1	(0.2)	N.M.
<b>Total</b>	<b>26.6</b>	<b>19.6</b>	<b>35.7%</b>

Source: Company

YE 31 Dec

INCOME STATEMENT (S\$m)	2017	2018	2019F	2020F	2021F
<b>Revenue</b>	<b>362.4</b>	<b>376.8</b>	<b>399.4</b>	<b>423.4</b>	<b>448.8</b>
Cost of sales	(268.2)	(271.6)	(289.6)	(304.8)	(320.9)
<b>Gross Profit</b>	<b>94.1</b>	<b>105.2</b>	<b>109.8</b>	<b>118.5</b>	<b>127.9</b>
Other operating income/(expenses)	(17.8)	(4.3)	0.0	0.0	0.0
Selling and distribution	(3.8)	(4.3)	(4.0)	(4.2)	(4.5)
Admin	(67.9)	(71.4)	(75.9)	(80.4)	(83.0)
<b>Profit from Operations</b>	<b>4.5</b>	<b>25.1</b>	<b>30.0</b>	<b>33.9</b>	<b>40.4</b>
Finance income/(expenses)	(0.3)	(0.6)	(0.8)	(0.8)	(0.9)
Share of JV results	0.0	0.0	0.0	0.0	0.0
Exceptionals/Investment income	(41.6)	1.5	0.5	0.5	0.5
<b>Profit before Tax</b>	<b>(37.4)</b>	<b>26.1</b>	<b>29.7</b>	<b>33.5</b>	<b>40.0</b>
Income tax	(9.5)	(6.6)	(7.7)	(8.7)	(10.4)
Non-controlling interests	1.7	0.7	0.0	0.0	0.0
<b>PATMI</b>	<b>(45.1)</b>	<b>20.1</b>	<b>22.0</b>	<b>24.8</b>	<b>29.6</b>
PATMI Normalized	(3.5)	18.6	21.5	24.3	29.1

BALANCE SHEET (US\$m)	2017	2018	2019F	2020F	2021F
Cash and cash equivalents	46.9	74.1	67.2	73.8	86.1
Trade and other receivables	159.6	116.2	162.5	172.2	182.6
Inventory	14.6	16.5	11.7	12.3	12.9
Other current assets	3.0	3.7	3.7	3.7	3.7
<b>Current Assets</b>	<b>224.1</b>	<b>210.5</b>	<b>245.1</b>	<b>262.1</b>	<b>285.3</b>
Property, plant and equipment	28.0	28.2	28.4	28.2	27.4
Other non-current assets	31.8	30.4	31.8	33.2	34.6
<b>Non-current Assets</b>	<b>59.8</b>	<b>58.6</b>	<b>60.2</b>	<b>61.3</b>	<b>62.1</b>
<b>Total assets</b>	<b>283.9</b>	<b>269.1</b>	<b>305.3</b>	<b>323.4</b>	<b>347.4</b>
Trade and other payables	70.5	56.4	62.4	65.6	69.1
Borrowings (current)	31.4	36.1	53.8	57.1	60.5
Other current liabilities	2.9	3.4	8.2	9.2	10.9
<b>Current Liabilities</b>	<b>104.8</b>	<b>95.9</b>	<b>124.4</b>	<b>131.9</b>	<b>140.4</b>
Borrowings (non-current)	0.0	0.0	0.0	0.0	0.0
Other non-current liabilities	3.4	0.8	0.8	0.8	0.8
<b>Non-current liabilities</b>	<b>3.4</b>	<b>0.8</b>	<b>0.8</b>	<b>0.8</b>	<b>0.8</b>
Shareholders equity	174.0	171.2	179.0	189.6	205.0
Non-controlling interests	1.8	1.1	1.1	1.1	1.1
<b>Total Equity</b>	<b>175.8</b>	<b>172.3</b>	<b>180.1</b>	<b>190.7</b>	<b>206.1</b>
<b>Total Liabilities and Equity</b>	<b>283.9</b>	<b>269.1</b>	<b>305.3</b>	<b>323.4</b>	<b>347.4</b>

CASH FLOW STATEMENT (US\$m)	2017	2018	2019F	2020F	2021F
Net income before tax	(37.4)	26.1	29.7	33.5	40.0
Depreciation & non cash adjustments	24.3	(3.9)	20.2	14.2	14.7
Change in Working Capital	(6.5)	27.5	(35.3)	(6.8)	(7.2)
Income Tax Paid	(2.6)	(1.7)	(2.9)	(7.7)	(8.7)
Interest Paid	(0.8)	(0.8)	(1.1)	(1.1)	(1.2)
<b>CF from operating activities</b>	<b>(23.0)</b>	<b>47.2</b>	<b>10.7</b>	<b>32.1</b>	<b>37.6</b>
Purchase/Disposal of PPE	(8.3)	(6.7)	(8.0)	(8.0)	(8.0)
Other CFI	(8.5)	(0.9)	0.0	0.0	0.0
<b>CF from investing activities</b>	<b>(10.5)</b>	<b>(7.2)</b>	<b>(8.0)</b>	<b>(8.0)</b>	<b>(8.0)</b>
Dividends Paid	(14.2)	(14.2)	(14.2)	(14.2)	(14.2)
Debt Raised / (Repaid)	0.0	4.7	17.7	3.2	3.4
Equity Raised / (Bought Back)	0.0	0.0	0.0	0.0	0.0
Other Cash from Financing	0.0	(3.3)	0.0	0.0	0.0
<b>CF from financing activities</b>	<b>(3.8)</b>	<b>(12.7)</b>	<b>3.5</b>	<b>(11.0)</b>	<b>(10.8)</b>
Net increase in cash & cash equiv.	(43.9)	20.7	(0.4)	6.6	12.2
FX effects	(6.6)	(6.6)	(6.6)	(6.6)	(6.6)
Beginning Cash	90.8	46.9	67.6	67.2	73.8
<b>Ending Cash</b>	<b>46.9</b>	<b>67.6</b>	<b>67.2</b>	<b>73.8</b>	<b>86.1</b>

**KGI's Ratings****Rating Definition**

KGI Securities Research's recommendations are based on an Absolute Return rating system.

**BUY** >10% total return over the next 12 months

**HOLD** -10% to +10% total return over the next 12 months

**SELL** <-10% total return over the next 12 months

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