

27 May 2022

Utilities | Utilities

Taliworks Corporation (TWK MK)

Buy (Maintained)

Improving In Tandem With Endemicity; BUY

Target Price (Return):	MYR1.12 (+17%)
Price (Market Cap):	MYR0.96 (USD440m)
ESG score:	3.00 (out of 4)
Avg Daily Turnover (MYR/USD)	0.66m/0.15m

- **Keep BUY, new SOP-derived MYR1.12 TP from MYR1.03, 17% upside with c.7% FY22F yield.** Taliworks' 1Q22 core earnings of MYR10.3m missed our and Street estimates – accounting for just 12.7% and 13% of full-year projections. The variance was mainly due to the higher tax expense amid the expiry of the tax waiver period for the Grand Saga Highway on 31 Dec 2021. An interim DPS of 1.65 sen was declared, for the quarter. We like this company for its defensive earnings base, stable growth outlook, and attractive dividend yield.

- **Results review.** Despite 1Q22 core earnings being lower by 1.5% YoY, revenue and operating profit expanded by >10% YoY. The bulk of this growth was underpinned by the water treatment, supply and distribution business, where turnover and operating profit grew by 7% YoY and 8% YoY. The growth came from higher metered sales of RM36.9m (1Q21: RM35.8m) after reaching 89.9m cu m in 1Q22 (1Q21: 87.3m cu m) in the Sungai Selangor Water Treatment Plant Phase 1 operation.

- **1Q22 average daily traffic (ADT) for Grand Saga and Grand Sepadu Highway** was higher by 18.7% YoY and 3.6% YoY, amid the relaxation of movement restrictions. However, the growth in operating profit for both toll highways during the quarter was capped by higher amortisation of intangible assets. The construction segment also exhibited some growth by recording a revenue of MYR7.7m (1Q21: MYR3.9m) in the quarter, contributed by a project at the Cyberjaya Flagship Zone and the Sungai Rasau Project.

- **Post results, we trim FY22-24F earnings by 6%, 2% and 2%** as we take into account the expiry of the tax waiver for the Grand Saga Highway. Looking ahead, its business units' quarterly earnings should gradually improve – in light of the country's transition into endemicity. We opine that the construction progress for the Sungai Rasau Water Treatment Plant and Water Supply Scheme Phase 1 under Packages 2 and 3 will continue picking up, with work intensity ramping up in FY23-24. Moreover, the contribution of its recently acquired solar assets should provide additional revenues of c. MYR25-30m pa.

- **We roll forward our valuation base to FY23F.** As a result, our TP rises to MYR1.12, after factoring in a 0% ESG premium based on our in-house proprietary ESG methodology. TWK is trading at 11x FY22F EV/EBITDA, about -0.5SD from its 5-year average rolling forward mean – which is attractive, in view of its dividend yield of 7%. Key downside risks include a slower-than-expected economic recovery and negative effects of any change in government policies.

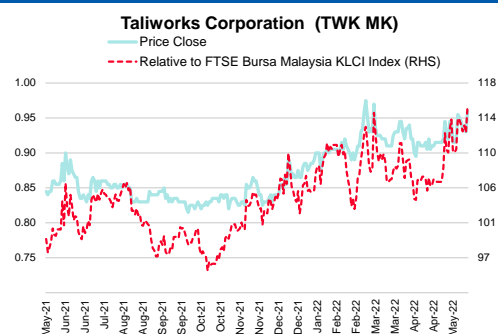
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Share Performance (%)

	YTD	1m	3m	6m	12m
Absolute	11.0	5.5	0.0	14.3	13.6
Relative	12.7	9.0	3.2	12.4	15.9
52-wk Price low/high (MYR)	0.82 – 0.98				



Source: Bloomberg

Overall ESG Score: 3.00 (out of 4)

E: GOOD

TWK integrates environmental management throughout the life cycle of each project. Some practices include tracking, managing and minimising air pollution and greenhouse gas emissions, and waste and effluents generated from across all areas of operations.

S: GOOD

TWK prioritises a work-life balance and, as such, provides for employees' welfare and well-being towards a better integration of life and career. Employee training and development costs were up >100% to MYR1.1m in 2019, while up-to-date health & safety policies are in place.

G: GOOD

While some elements of integrated reporting have been embodied in the Annual Report, overall, it is not an integrated report, based on the parameters set by the International Integrated Reporting Council. Only 16% of board is represented by women, and the Remuneration Committee does not provide oversight on remuneration for senior management. TWK engages a third-party investor relations outfit to facilitate communications with the investment community, with periodic meetings held.

Note:

Small cap stocks are defined as companies with a market capitalization of less than USD0.5bn.

Forecasts and Valuation	Dec-20	Dec-21	Dec-22F	Dec-23F	Dec-24F
Total turnover (MYRm)	318	303	541	689	669
Recurring net profit (MYRm)	58	70	76	86	93
Recurring net profit growth (%)	28.0	21.5	7.7	13.8	7.3
Recurring P/E (x)	33.40	27.49	25.52	22.43	20.90
P/B (x)	2.0	2.1	2.3	2.4	2.3
P/CF (x)	32.64	13.09	21.66	13.76	12.98
Dividend Yield (%)	6.9	6.9	6.9	6.9	6.9
EV/EBITDA (x)	14.12	12.19	11.22	10.76	10.30
Return on average equity (%)	6.0	8.4	8.7	10.5	11.3
Net debt to equity (%)	net cash	net cash	net cash	1.5	2.8

Source: Company data, RHB

Financial Exhibits

Asia	Financial summary (MYR)	Dec-20	Dec-21	Dec-22F	Dec-23F	Dec-24F
Malaysia	Recurring EPS	0.03	0.03	0.04	0.04	0.05
Utilities	DPS	0.07	0.07	0.07	0.07	0.07
Taliworks Corporation	BVPS	0.48	0.45	0.42	0.40	0.41
TWK MK	Return on average equity (%)	6.0	8.4	8.7	10.5	11.3
Buy						
	Valuation metrics	Dec-20	Dec-21	Dec-22F	Dec-23F	Dec-24F
Valuation basis	Recurring P/E (x)	33.40	27.49	25.52	22.43	20.90
SOP	P/B (x)	2.0	2.1	2.3	2.4	2.3
	FCF Yield (%)	3.0	7.6	4.4	7.0	7.4
	Dividend Yield (%)	6.9	6.9	6.9	6.9	6.9
Key drivers	EV/EBITDA (x)	14.12	12.19	11.22	10.76	10.30
i. Stable operations;	EV/EBIT (x)	18.80	15.63	14.65	13.94	13.25
ii. Favourable outcome on tariff hikes;						
iii. Lower losses at associate companies.						
	Income statement (MYRm)	Dec-20	Dec-21	Dec-22F	Dec-23F	Dec-24F
Key risks	Total turnover	318	303	541	689	669
Downside risks to our call include:	Gross profit	124	140	129	137	145
i. Unfavourable outcome on tariff revisions;	EBITDA	129	152	169	178	186
ii. Restrictive cash flow from its associates and JVs, given the step-up repayment of bonds/sukuk;	Depreciation and amortisation	(32)	(33)	(40)	(41)	(42)
iii. Deteriorating asset quality, giving rise to higher operating costs;	Operating profit	97	119	129	137	145
iv. A broad-based economic slowdown;	Net interest	(21)	(19)	(17)	(16)	(14)
v. Escalating waste management costs, dragging the company into losses.	Pre-tax profit	79	114	131	136	145
	Taxation	(15)	(12)	(39)	(33)	(35)
	Reported net profit	59	79	76	86	93
	Recurring net profit	58	70	76	86	93
Company Profile						
Taliworks is a pure-play infrastructure company primarily engaged in water treatment, supply and distribution – which involves management, operations & maintenance (O&M) of water treatment plants and water distribution systems. It is also engaged in highway toll concessionaires (O&M), engineering & construction, and waste management	Cash flow (MYRm)	Dec-20	Dec-21	Dec-22F	Dec-23F	Dec-24F
	Change in working capital	(52)	10	(40)	(4)	(2)
	Cash flow from operations	59	148	89	141	149
	Capex	(0)	(1)	(5)	(5)	(5)
	Cash flow from investing activities	230	70	51	51	(13)
	Dividends paid	(157)	(133)	(100)	(133)	(133)
	Cash flow from financing activities	(277)	(204)	(130)	(170)	(165)
	Cash at beginning of period	73	87	73	73	95
	Net change in cash	12	14	11	22	(28)
	Ending balance cash	85	100	84	95	67
	Balance sheet (MYRm)	Dec-20	Dec-21	Dec-22F	Dec-23F	Dec-24F
	Total cash and equivalents	473	420	370	342	328
	Tangible fixed assets	9	6	6	6	6
	Total investments	277	270	283	291	299
	Total assets	2,075	1,943	2,022	2,022	1,897
	Short-term debt	30	30	33	29	30
	Total long-term debt	358	329	329	329	329
	Total liabilities	867	786	921	969	812
	Total equity	1,208	1,157	1,100	1,053	1,085
	Total liabilities & equity	2,075	1,943	2,022	2,022	1,897
	Key metrics	Dec-20	Dec-21	Dec-22F	Dec-23F	Dec-24F
	Revenue growth (%)	(15.7)	(4.8)	78.7	27.4	(2.9)
	Recurrent EPS growth (%)	28.0	21.5	7.7	13.8	7.3
	Gross margin (%)	38.9	46.2	24.0	19.9	21.7
	Operating EBITDA margin (%)	40.6	50.3	31.3	25.8	27.9
	Net profit margin (%)	18.7	25.9	14.0	12.5	13.8
	Dividend payout ratio (%)	223.7	169.5	175.5	154.2	143.7
	Capex/sales (%)	0.1	0.4	1.0	0.8	0.8
	Interest cover (x)	4.57	6.22	7.51	8.71	10.17

Source: Company data, RHB

Figure 1: TWK's 1Q22 results review

FYE Dec (MYRm)	1Q21	4Q21	1Q22	QoQ (%)	YoY (%)	Comments
Revenue	65.6	72.4	74.8	3.3%	14.1%	Better average daily traffic and higher metered water sales.
EBIT	18.7	17.4	23.4	34.8%	25.4%	
<i>EBIT margin (%)</i>	28%	24%	31%			
Finance cost	(4.7)	(4.8)	(4.5)	6.4%	3.6%	
Share of JV	0.4	0.4	0.5	54.5%	36.4%	
Share of Associate	2.3	0.9	(2.4)	-358.5%	-203.3%	
Pretax profit	16.7	13.8	17.0	23.2%	1.9%	
<i>Pretax margin (%)</i>	25%	19%	23%			
Tax	(3.0)	(1.9)	(5.5)	-199.1%	-86.9%	
Effective tax rate (%)	18%	13%	33%			Higher ETR due to the expiry of the tax waiver period for Grand Saga Highway.
Minority interest	(1.4)	0.2	(0.9)	-552.5%	33.4%	
Net Profit	12.4	12.2	10.6	-13.1%	-14.6%	
Core Profit	11.0	13.2	10.3	-17.4%	-1.5%	Below expectations.
<i>Core net margin (%)</i>	17%	18%	15%			

Source: Company data, RHB

Figure 2: TWK's 1Q22 segmental results

FYE Dec (MYRm)	1Q21	4Q21	1Q22	QoQ (%)	YoY (%)	Comments
Revenue						
Water treatment, supply and distribution	42.1	43.2	45.2	4.7%	7.4%	Improvement in metered water sales.
Construction	3.9	6.5	7.8	19.3%	98.0%	Recognition for Sungai Rasau projects started.
Toll highway	18.3	21.5	20.6	-4.1%	12.4%	
Others	1.3	1.3	1.3	0.0%	0.0%	
EBIT						
Water treatment, supply and distribution	14.5	11.5	15.7	36.3%	8.0%	
Construction	(0.9)	0.8	0.0	-95.2%	104.1%	
Toll highway	7.7	5.1	8.9	75.5%	15.8%	ADT for Grand Saga and Grand Sepadu was up 18.7% YoY and 3.6% YoY, but was capped by the amortisation of intangible assets.
Others	(2.6)	(0.0)	(1.2)	nm	54.0%	
EBIT Margins						
Water treatment, supply and distribution	34%	27%	35%			
Construction	-23%	12%	0%			
Toll highway	42%	24%	43%			

Source: Company data, RHB

Figure 3: Taliworks' SOP valuation

Highway assets	Stake	FY23F FCFE	Per share	Remark
Grand Saga	51%	627.8	0.31	WACC of 6.3%, concession up to 2045, with four toll rate hikes assumed.
Grand Sepadu (45% economic benefit)	45%	114.1	0.06	WACC of 6.3%, concession up to 2032, with two toll rate hikes assumed.
Water assets	100%	433.8	0.22	WACC of 6.3%, concession up to 2036, with a contracted base supply rate assumed. No extension to the Langkawi water asset.
Waste management asset	35%	352.3	0.17	WACC of 6.3%, concession up to 2033.
		P/E		
Construction	100%	12.0	0.08	We think that this target P/E is fair, as it is within the range ascribed to construction peers under our coverage.
Solar Assets	100%	220.8	0.09	WACC 7.0%, 13 years remaining for the concession.
Net Debt		338.0	0.45	Adjusted to exclude net debts included in FCFE calculation for Grand Saga and the water assets.
No. of shares (m)		2,015.8		
Intrinsic value per share		2,098.9	1.12	
0% ESG discount/premium			0.00	
Target price			1.12	

Source: Company data, RHB

Recommendation Chart

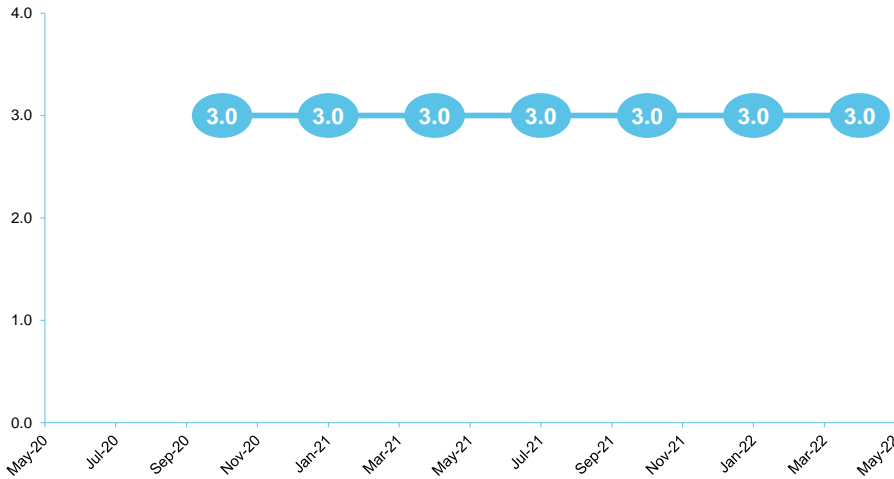


Source: RHB, Bloomberg

Date	Recommendation	Target Price	Price
2022-02-23	Buy	1.03	0.93
2021-11-16	Buy	0.98	0.86
2021-05-20	Buy	0.94	0.85
2020-08-21	Buy	0.98	0.87
2020-07-02	Buy	0.97	0.86

Source: RHB, Bloomberg

ESG Rating History



Source: RHB

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