

1 March 2021

Utilities | Utilities

Taliworks Corporation (TWK MK)

Buy (Maintained)

8% Yield Still Attractive Despite Rising Bond Yield

Target Price (Return): MYR0.98 (18.1%)
 Price: MYR0.83
 Market Cap: USD411m
 Avg Daily Turnover (MYR/USD) 1.25m/0.31m

- **Keep BUY and SOP-derived MYR0.98 TP, 18% upside and c.8% FY21F yield.** FY20 core earnings were within our expectations but beat consensus. A fourth interim dividend of 1.65 sen was declared during the quarter, bringing total FY20 DPS to 6.6 sen (+26% YoY vs FY19's 5.25 sen). We expect similar in FY21, supported by decent cash flow generation across Taliworks Corp's concession-based assets. We continue to like the stock for its defensive earnings base, stable growth outlook, and attractive c.8% FY21F yield.
- **In line with expectations.** TWK booked a 4Q20 core net profit of MYR15.1m (+51% YoY, -10% QoQ), bringing FY20 core earnings to MYR58m (+28% YoY) – at 98% our but missed Street's at 93%. In deriving our 4Q20 core net profit, we stripped out items related to investments designated at fair value through profit or loss (FVTPL). The loss allowance on trade receivables and amount due from contract customers, as well as fair value changes totalled c.MYR0.6m.
- **4Q20 revenue from the water segment was lower YoY/QoQ**, largely due to a drop in metered sales on the back of operational disruptions caused by odour pollution in Klang and cessation of the Langkawi operations. Following the latter, we expect revenue contributions from this segment to narrow to c.53% in FY21 (FY20: 71%).
- **While toll highways saw lower 4Q20 average daily traffic (ADT)** on travel restrictions under the CMCO, share of JVs increased 18% YoY (>100% QoQ) on higher toll compensation of MYR17m. This was cushioned by higher amortisation of intangible assets due to a significant reduction in the projected traffic volume due to the MCO. Note: Amortisation is a non-cash adjustment and does not impact future cash flow. However, a lower traffic volume forecast may adversely impact valuations. For now, we make no adjustments to Grand Sepadu's valuations (valued at 5 sen/share), pending management's clarification.
- **No changes to our key assumptions**, as FY20 results were in line with expectations. Our FY21F-22F earnings shift c.2% after reflecting the latest financial figures. We have yet to include the potential contributions for the recently acquired solar assets to our earnings forecast, pending completion of the deal slated for 1H21. Nevertheless, we impute the solar assets into our SOP, based on the purchase price that is netted off against TWK's cash position – no changes to TP. It currently trades at 9.7x FY21F EV/EBITDA, about -1.3SD from its 5-year average rolling forward mean.
- **Risks.** Unfavourable tariff revision outcomes, a broad-based economic slowdown, deteriorating asset quality that give rise to higher operating costs, and escalating waste management costs that drag TWK into losses.

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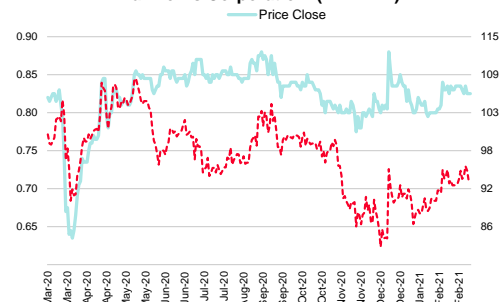
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Share Performance (%)

	YTD	1m	3m	6m	12m
Absolute	(1.2)	3.1	3.1	(4.6)	(1.2)
Relative	1.8	2.9	5.2	(6.4)	(6.7)
52-wk Price low/high (MYR)				0.64 – 0.88	

Taliworks Corporation (TWK MK)



Source: Bloomberg

Overall ESG Score: 3.0 (out of 4)

E: Good

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

S: Good

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

G: Good

Whilst some elements of integrated reporting have been embodied in the annual report, on the whole there are no integrated reports based on the parameters set out by the International Integrated Reporting Council. Aside from that, only 16% of the board is represented by women directors and the remuneration committee does not provide an oversight on senior management's remuneration. 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 capitalisation of less than USD1bn.

Forecasts and Valuation	Dec-19	Dec-20	Dec-21F	Dec-22F	Dec-23F
Total turnover (MYRm)	377	318	317	321	328
Recurring net profit (MYRm)	45	58	61	71	62
Recurring net profit growth (%)	35.3	28.0	4.8	17.3	(13.3)
Recurring P/E (x)	36.75	28.70	27.38	23.34	26.91
P/B (x)	1.6	1.7	1.9	2.0	2.2
P/CF (x)	2.59	25.56	12.03	11.78	12.22
Dividend Yield (%)	6.4	8.0	8.0	8.0	8.0
EV/EBITDA (x)	8.01	12.19	9.73	9.77	10.71
Return on average equity (%)	7.3	6.0	6.6	8.3	7.8
Net debt to equity (%)	net cash	net cash	net cash	net cash	0.1

Source: Company data, RHB

Financial Exhibits

Asia	Financial summary (MYR)	Dec-19	Dec-20	Dec-21F	Dec-22F	Dec-23F
Malaysia	Recurring EPS	0.02	0.03	0.03	0.04	0.03
Utilities	DPS	0.05	0.07	0.07	0.07	0.07
Taliworks Corporation	BVPS	0.51	0.48	0.44	0.41	0.37
TWK MK	Return on average equity (%)	7.3	6.0	6.6	8.3	7.8
Buy						
	Valuation metrics	Dec-19	Dec-20	Dec-21F	Dec-22F	Dec-23F
Valuation basis	Recurring P/E (x)	36.75	28.70	27.38	23.34	26.91
SOP Valuation	P/B (x)	1.6	1.7	1.9	2.0	2.2
	FCF Yield (%)	38.4	3.9	8.0	8.2	7.9
Key drivers	Dividend Yield (%)	6.4	8.0	8.0	8.0	8.0
i. Stable operations;	EV/EBITDA (x)	8.01	12.19	9.73	9.77	10.71
ii. Favourable outcome on tariff hikes;	EV/EBIT (x)	9.99	16.22	12.75	12.85	14.56
iii. Lower losses at associate companies.						
	Income statement (MYRm)	Dec-19	Dec-20	Dec-21F	Dec-22F	Dec-23F
Key risks	Total turnover	377	318	317	321	328
Risk to our calls include:	Gross profit	148	117	124	125	113
i. Unfavourable outcome on tariff revisions;	EBITDA	180	129	162	165	153
ii. Restrictive cash flows from associates and JVs, given the step-up repayments of bonds/sukuk;	Depreciation and amortisation	(36)	(32)	(39)	(39)	(40)
iii. Deteriorating asset quality giving rise to higher operating costs;	Operating profit	144	97	124	125	113
iv. A broad-based economic slowdown;	Net interest	(25)	(21)	(19)	(17)	(16)
v. Escalating waste management costs that drag the company into losses.	Pre-tax profit	110	79	110	114	104
	Taxation	(23)	(15)	(22)	(23)	(21)
	Reported net profit	76	59	61	71	62
	Recurring net profit	45	58	61	71	62
Company Profile						
TWK is a pure-play infrastructure company primarily engaged in water treatment, supply, and distribution. This involves management, operations & maintenance (O&M) of water treatment plants, and water distribution systems. It is also engaged in highway toll concessionaires (in the O&M segment), engineering & construction, and waste management.						
	Cash flow (MYRm)	Dec-19	Dec-20	Dec-21F	Dec-22F	Dec-23F
	Change in working capital	523	(49)	(2)	(1)	4
	Cash flow from operations	643	65	138	141	136
	Capex	(3)	(0)	(5)	(5)	(5)
	Cash flow from investing activities	(541)	226	52	52	53
	Dividends paid	(97)	(157)	(100)	(133)	(133)
	Cash flow from financing activities	(120)	(277)	(146)	(171)	(170)
	Cash at beginning of period	90	73	65	109	132
	Net change in cash	(17)	14	44	23	19
	Ending balance cash	73	87	109	132	151
	Balance sheet (MYRm)	Dec-19	Dec-20	Dec-21F	Dec-22F	Dec-23F
	Total cash and equivalents	658	451	445	418	387
	Tangible fixed assets	12	9	9	9	9
	Total investments	291	277	275	274	273
	Total assets	2,354	2,075	2,033	1,972	1,908
	Short-term debt	40	30	30	30	30
	Total long-term debt	428	358	358	358	358
	Total liabilities	1,061	867	898	899	906
	Total equity	1,293	1,208	1,135	1,074	1,002
	Total liabilities & equity	2,354	2,075	2,033	1,972	1,908
	Key metrics	Dec-19	Dec-20	Dec-21F	Dec-22F	Dec-23F
	Revenue growth (%)	0.8	(15.7)	(0.3)	1.2	2.3
	Recurrent EPS growth (%)	35.3	28.0	4.8	17.3	(13.3)
	Gross margin (%)	39.2	37.0	39.1	39.0	34.3
	Operating EBITDA margin (%)	47.7	40.6	51.3	51.3	46.6
	Net profit margin (%)	20.2	18.7	19.2	22.2	18.8
	Capex/sales (%)	0.9	0.1	1.6	1.6	1.6
	Interest cover (x)	5.78	4.57	6.61	7.25	7.15

Source: Company data, RHB

Results At a Glance

Figure 1: TWK's FY20 results

FYE Dec (MYRm)	4Q19	3Q20	4Q20	QoQ (%)	YoY (%)	FY19	FY20	YoY (%)	Comments
Revenue	105.5	82.6	74.9	-9%	-29%	377.1	317.9	-16%	Lower contributions across all business segments.
EBIT	0.6	27.2	18.0	-34%	3,088%	144.3	96.9	-33%	
EBIT margin (%)	1%	33%	24%			38%	30%		
Finance cost	(7.0)	(5.2)	(5.2)	-1%	25%	(25.0)	(21.2)	15%	
Share of JV	3.4	0.5	4.0	689%	18%	5.3	4.7	-11%	Lower ADT due to the MCO.
Share of associate	(6.4)	0.1	2.4	1,958%	137%	(15.1)	(1.9)	88%	Higher toll compensation of MYR16.97m received in 4Q, offset by the higher amortisation of intangible assets during the quarter due to significant reduction in the projected traffic volumes due to the MCO.
Pre-tax profit	(9.4)	22.6	19.1	-16%	302%	109.5	78.5	-28%	
Pre-tax margin (%)	-9%	27%	25%			29%	25%		
Tax	(6.6)	(3.9)	(3.7)	3%	44%	(23.1)	(15.0)	35%	
Effective tax rate (%)	-70%	17%	20%			21%	19%		
Minority interest	(2.7)	(2.5)	0.4	115%	114%	(10.3)	(4.0)		
Net profit	(18.8)	16.2	15.7	-3%	183%	76.2	59.5	-22%	
Core profit	10.0	16.9	15.1	-10%	51%	45.3	57.9	28%	In line with our expectations.
Core net margin (%)	9%	20%	20%			12%	18%		

Source: Company data, RHB

Figure 2: TWK's FY20 segmental results

FYE Dec (MYRm)	4Q19	3Q20	4Q20	QoQ (%)	YoY (%)	FY19	FY20	YoY (%)	Comments
Revenue									
Water treatment, supply and distribution	63.1	56.4	49.8	-12%	-21%	254.9	225.5	-12%	4Q20 saw lower metered sales for SSP1 due to disruptions of operations caused by odour pollution in Klang and the cessation of Langkawi operations. Upward revision of construction revenue in the Langat 2-Package 7 project. Lower ADT at Grand Saga highway on travel restrictions.
Construction	18.7	3.2	4.5	39%	-76%	34.5	12.7	-63%	
Toll highway	22.5	21.6	19.3	-11%	-14%	89.4	74.4	-17%	
Others	1.3	1.3	1.3	0%	0%	5.3	5.3	0%	
EBIT									
Water treatment, supply and distribution	(9.9)	19.0	13.8	-27%	239%	109.5	74.8	-32%	Derived from dividend from investments designated at FVTPL and reversal of loss allowance on trade receivables, net off the additional provision for restoration costs recognised.
Construction	2.0	(0.2)	1.1	585%	-43%	1.3	0.5	-60%	
Toll highway	11.1	10.6	5.6	-47%	-49%	43.8	31.0	-29%	
Others	(2.6)	(2.2)	(2.6)	-17%	0%	(10.3)	(9.5)	8%	
EBIT Margins									
Water treatment, supply and distribution	-16%	34%	28%			43%	33%		
Construction	11%	-7%	25%			4%	4%		
Toll highway	49%	49%	29%			49%	42%		Higher amortisation of intangible assets on lower projected traffic volumes.

Source: Company data, RHB

Figure 3: TWK's SOP valuation

Highway assets	Stake	FY21F FCFE	Per share	Remark
Grand Saga	51%	645.4	0.32	WACC 6.3%, concession up to 2045 with four toll rate hikes assumed.
Grand Sepadu (45% economic benefit)	45%	108.8	0.05	WACC 6.3%, concession up to 2032 with two toll rate hikes assumed.
Water assets	100%	412.0	0.20	WACC 6.3%, concession up to 2036 with contracted base supply rate assumed. No extension to the Langkawi water asset.
Waste management asset	35%	333.9	0.17	WACC 6.3%, concession up to 2033.
P/E				
Construction	100%	12.0	0.00	
Solar assets			0.09	Purchase price of MYR180.35m.
Remaining unallocated FY21F net debt		296.9	0.15	Adjusted to exclude net debts included in FCFE calculation for Grand Saga and the water assets.
Number of shares		2,015.8		
SOTP		1,991.4	0.98	

Source: Company data, RHB

Recommendation Chart



Source: RHB, Bloomberg

Date	Recommendation	Target Price	Price
2020-08-21	Buy	0.98	0.87
2020-07-02	Buy	0.97	0.86

Source: RHB, Bloomberg

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Trading Buy:	Share price may exceed 15% over the next 3 months, however longer-term outlook remains uncertain
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Analyst	Company
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