AmInvestment Bank

SURIA CAPITAL HOLDINGS

(SURIA MK EQUITY, SURI.KL)

02 October 2023

Positive on upcoming port tariff revision

Company report

BUY

(Upgraded)

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Rationale for Report: Company Update

Price	**RM1.52**
Fair Value	**RM1.85**
52-week High/Low	RM1.55/RM0.99

Key Changes

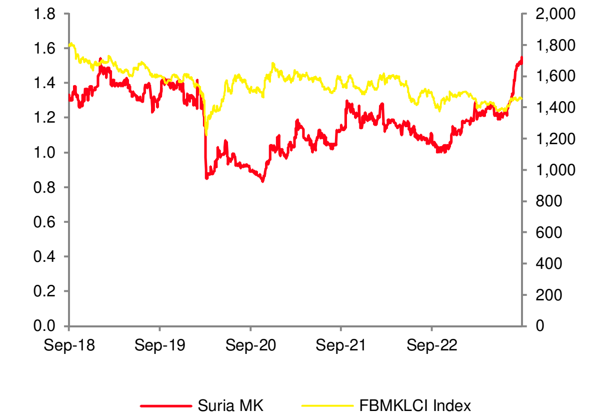
Fair value	↑
EPS	⇔

YE to Dec	FY22	FY23F	FY24F	FY25F
Revenue (RM mil)	302.0	318.4	328.2	339.6
Core net profit (RM mil)	48.7	61.9	63.3	65.1
FD Core EPS (sen)	14.1	17.9	18.3	18.8
FD Core EPS growth (%)	2.4	27.1	2.2	2.7
Consensus Net Profit (RM mil)	-	62.9	64.5	66.0
DPS (sen)	4.0	6.3	6.4	6.6
PE (x)	10.8	8.5	8.3	8.1
EV/EBITDA (x)	4.3	4.0	3.1	3.1
Div yield (%)	2.6	4.1	4.2	4.3
ROE (%)	5.1	5.2	5.1	5.1
Net Gearing (%)	nm	nm	nm	nm

Stock and Financial Data

Shares Outstanding (million)	345.8
Market Cap (RM mil)	536.0
Book Value (RM/share)	3.41
P/BV (x)	0.5
ROE (%)	5.1
Net Gearing (%)	-
Major Shareholders	Warisan Harta (45.4%) Urusharta Jamaah (5.1%) Yayasan Sabah (3.7%)
Free Float	45.8
Avg Daily Value (RM mil)	0.3

Price performance	3mth	6mth	12mth
Absolute (%)	29.2	25.0	39.6
Relative (%)	22.2	23.1	43.6



Investment Highlights

- **We upgrade Suria Capital to BUY from HOLD with a higher DCF-derived fair value (FV) of RM1.85/share (from RM1.40/share previously), which implies a FY24F PE of 10.1x, 0.8 standard deviation above its 5-year average of 8.5x. There is no FV adjustment for ESG based on our 3-star rating.**

- **Suria's higher DCF stems mainly from lowering our WACC assumptions to 7.7% from 9.9% previously on a more conservative equity market returns of 10% (from 13.5% previously). For now, we maintain our forecasts following a meeting with management recently.**

- **Management is hopeful for a positive port service tariff revision by the end of the year, which has been unchanged since Sabah ports' privatisation in 2004. This is supported by administrative orders to raise some services, of which certain crane charges have been hiked by 50% YoY. Assuming a conservative port service tariff rise of 10%, we estimate that FY24F net profit could be raised by a substantive 33%.**

- **Suria is positive on its strategic location as a transshipment hub for the Brunei-Indonesia-Malaysia-Philippines East ASEAN Growth Area, focusing on intra-Asian trade with China and the Far East. Hence, the relocation of Indonesia's capital city from Jakarta to Nusantara encompassing 260,000 hectares in East Kalimantan will be positive for the region's throughput over the longer term.**

- **Hence, Sabah Ports has entered a strategic collaboration with global port/logistics operator, DP World (DP), which is expected to draw in substantive foreign direct investments into free economic zones, logistics hubs and industrial parks, with an immediate focus on Sepangar Bay Container Port.**

- **By leveraging on DP's network of multinational logistic operators and in-house feeder operation, Feedertech together with the state's abundant natural resources and low wage structure, Suria aims to increase throughput for outbound cargo, of which 85% are empty currently.**

  The group is planning to expand its Sepangar Bay port for container, oil terminal jetty and conventional cargo terminal with a RM900mil federal government allocation since 2021. By FY25F, Suria expects to spend RM150mil on port equipment and cranes to support the port expansion projects, which is in line with our capex assumptions.

- **Underpinned by improving long-term prospects, Suria currently trades at an attractive FY24F PE of 8.5x, below its 5-year peak of over 12x while offering a decent and sustainable dividend yield of 4%.**

POISED FOR A SUBSTANTIVE RE-RATING

- ***Upgrade to BUY on higher fair value of RM1.85***

We upgrade Suria Capital to BUY from HOLD with a higher DCF-derived fair value (FV) of RM1.85/share (from RM1.40/share previously), which implies a FY24F PE of 10.5x, 1 standard deviation above its 5-year average of 8.5x. There is no FV adjustment for ESG based on our 3-star rating.

Underpinned by improving long-term prospects, Suria currently trades at an attractive FY24F PE of 8.5x, below its 5-year peak of over 12x while offering a decent and sustainable dividend yield of 4%.

Suria's higher DCF stems from lowering our weighted average cost of funds (WACC) to 7.7% from 9.9% previously on a more conservative equity market returns of 10% (13.5% earlier). For now, we maintain our forecasts following a meeting with management recently.

- ***Positive port rerating catalyst***

Management is hopeful for a positive port service tariff revision by the end of the year, which has been unchanged since Sabah ports' privatisation in Sep 2004. This is supported by administrative orders to raise some services, of which certain crane charges have been hiked by 50% YoY.

Recall that the review of its tariff rates was approved in principle by the state cabinet in 2020 for implementation at a later date while the concession period has already been extended on 22 Nov 2022 by another 30 years from 2034 to 31 Aug 2064.

Assuming a conservative port service tariff rise of 10%, we estimate that FY24F net profit could be raised by a substantive 33%.

- ***Strategic transshipment hub for BIMP region***

Suria is positive on its strategic location (Exhibit 1) as a transshipment hub for the Brunei-Indonesia-Malaysia-Philippines (BIMP) East ASEAN Growth Area, focusing on intra-Asian trade with China and the Far East (Exhibit 2).

Hence, the relocation of Indonesia's capital city from Jakarta to Nusantara encompassing 260,000 hectares in East Kalimantan will be positive for the region's throughput over the longer term.

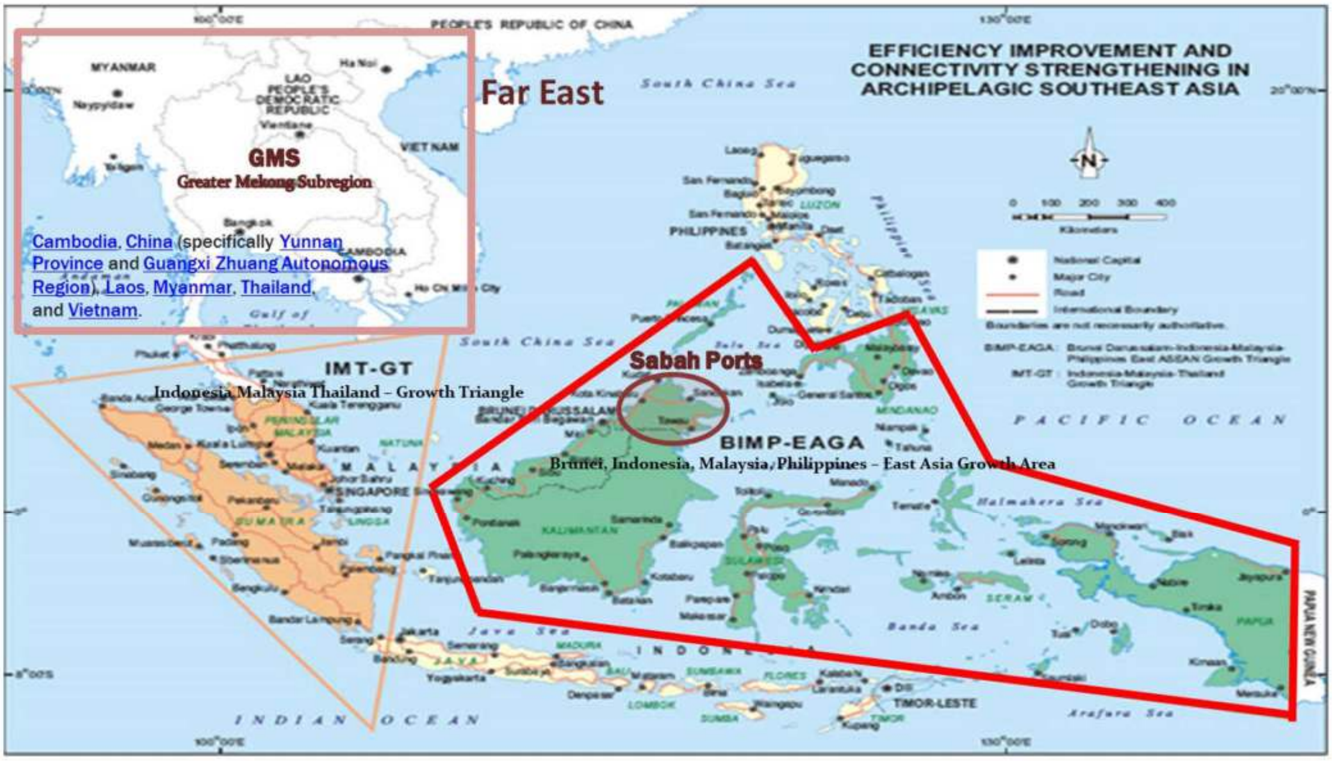
With completion by 2045, the IKN Authority has indicated that the infrastructure for Nusantara's core region has reached a progress stage of 38% currently.

The core region will house the presidential palace, vice presidential palace, office buildings and a hospital together with critical infrastructure for the nation's administrative complex and housing for 1mil civil servants who will be relocated from Jakarta.

- ***Synergistic collaboration with DP World***

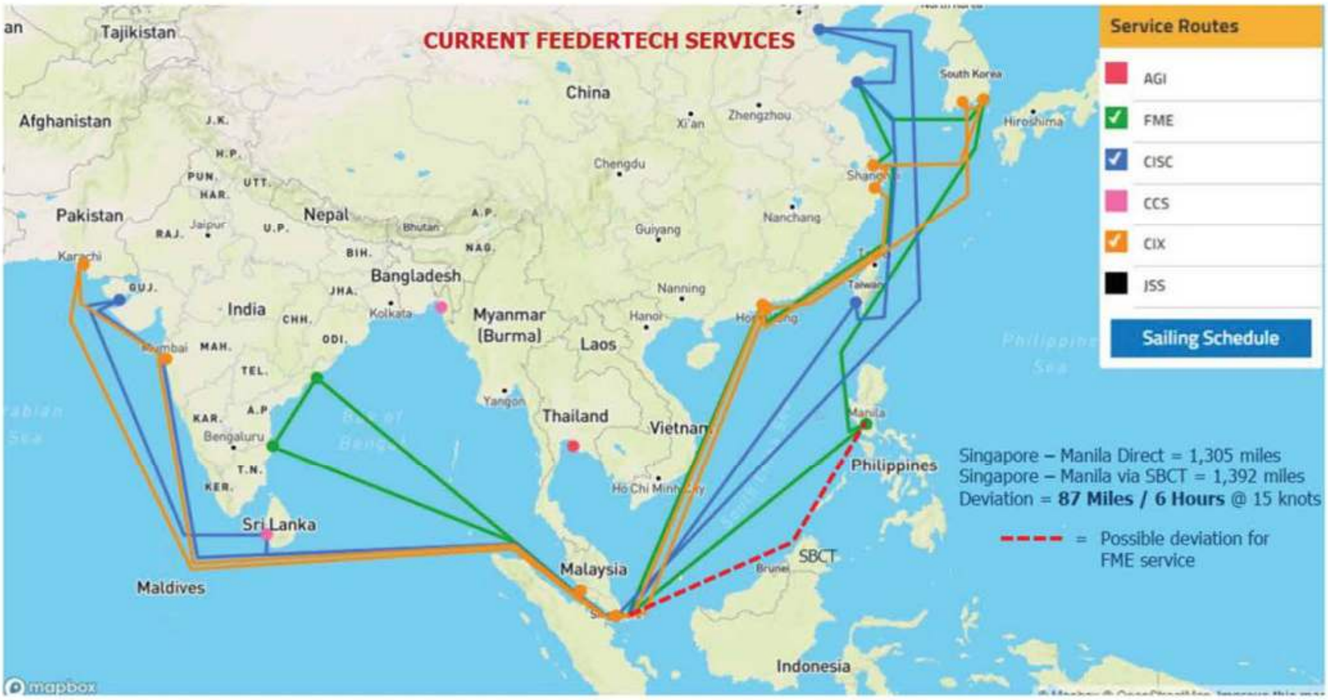
Hence, Sabah Ports has entered into a strategic collaboration with global port/logistics operator, DP World (DP), which is expected to draw in substantive foreign direct investments into free economic zones, logistics hubs

EXHIBIT 1: SABAH'S STRATEGIC LOCATION



Source: Company

EXHIBIT 2: FEEDERTECH SHIPPING ROUTES



Source: Company

and industrial parks, with an immediate focus on Sepangar Bay Container Port.

By leveraging on DP's network of multinational logistic operators and in-house feeder operation, Feedertech together with the state's abundant natural resources and low wage structure, Suria aims to increase throughput for outbound cargo, of which 85% are empty currently.

❑ *Boost from multinational investments into Sabah*

Suria's port throughput, which rose 8.7% QoQ for containers to 107.6mil twenty-foot equivalent units (TEUs) in 2QFY23 (Exhibit 4), will be further boosted by other multinational investments. This includes:

1) China-based Kibing Group's RM2bil Solar New Materials factory in Kota Kinabalu Industrial Park (KKIP) to annually process 1.2mil tonnes of silica sand and solar panels, scheduled for operation next year.

2) SK Nexilis' RM4.2bil KKIP facility to produce 50,000 tons of copper foil for electric vehicle batteries later this year.

❑ *Expanding Sepangar facilities*

Suria has a monopoly on all 8 of the state's ports (Exhibit 3). The group is planning to expand its Sepangar Bay port for container, oil terminal jetty and conventional cargo terminal with a RM900mil federal government allocation since 2021.

The Sepangar Bay Container Port's capacity will be expanded to 1.25mil TEUs from 0.5mil TEUs currently with quay length doubled to 1k metres, draft deepened to 15 metres from 12 metres and cranes increased by 3x to 12 by Feb 2025.

The federal grant includes Sepangar Bay Oil Terminal jetty, which is also being currently extended with completion by next year.

General cargo at Kota Kinabalu port, one of Suria's 8 ports (Exhibit 3), is being planned for relocation to Sepangar Bay Conventional Cargo Terminal (SBCCT), which will also support the oil & gas industry. SBCCT's construction is expected to commence in 2024 with completion over 3 years.

By FY25F, Suria expects to spend RM150mil on port equipment and cranes to support the port expansion projects, which is in line with our capex assumptions.

❑ *Icing on the cake from property development*

Besides port operations, Suria plans to venture into property development via JV with SBC Corporation since 2013 by transforming an old Kota Kinabalu port into an integrated project called Jesselton Waterfront City.

This project encompasses a 7-acre mixed development, 16.3-acre quay, 15-acre Sabah International Convention Centre, 8.3-acre Kota Kinabalu Convention City and 28.9-acre international cruise-cum-mixed development.

Phase II of Jesselton Quay which is to be developed on the remaining 10.3 acres of land is expected to commence by end-2023 with completion targeted in 2030. The group will own the commercial shops within the heritage precinct of Jesselton Quay, scheduled for completion in 2027.

We understand that the 28.9 acres land, consisting of the main wharf of Kota Kinabalu Port and a large portion of the water body, will require reclamation works to be undertaken prior to commencing development.

The mixed developments will include service suites, apartments, condo residences, a recreation club, hotels, commercial gallery shoppes, retail mall, car park facilities, a ferry ticketing office and Suria's corporate headquarters office.

SBC will be the project developer while Suria, as the land owner, will gain a minimum net sale of RM300mil or 20% of the project's gross development value of RM1.8bil.

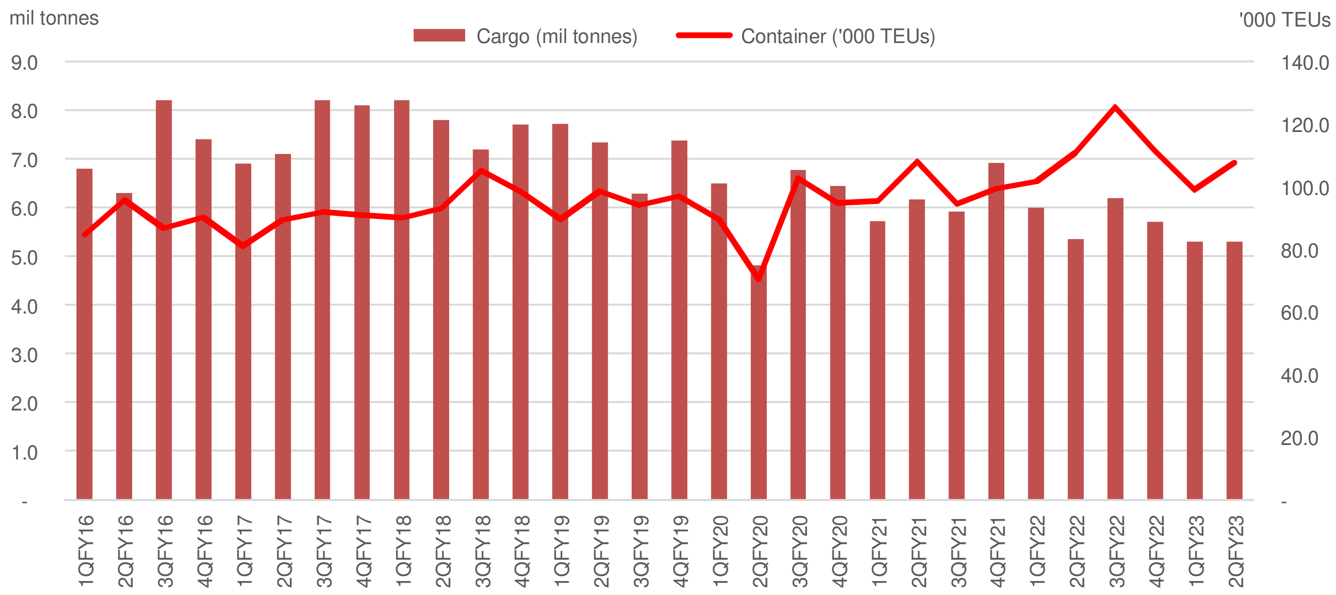
Assuming an initial launch of 20% of GDV, pretax margin of 20% and 3-year development, we estimate a property development accretion of 5% to FY24F group net profit.

For now, we have not incorporated any contribution from this division.

EXHIBIT 3: SURIA'S 8 PORTS

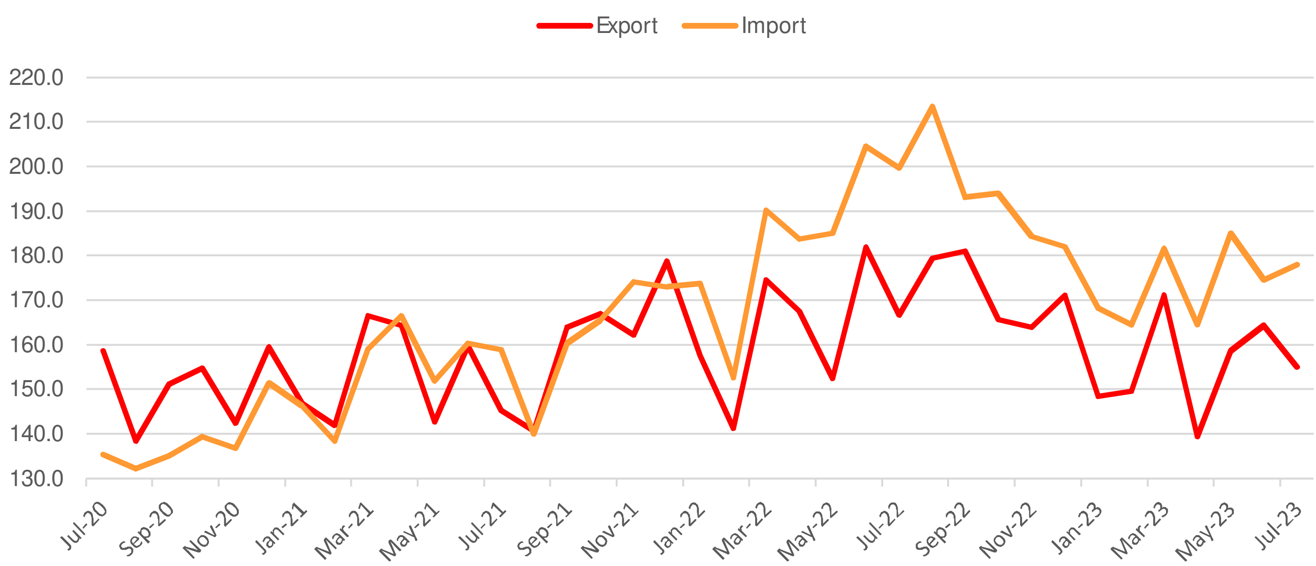
Source: Company

EXHIBIT 4: QUARTERLY THROUGHPUT TREND



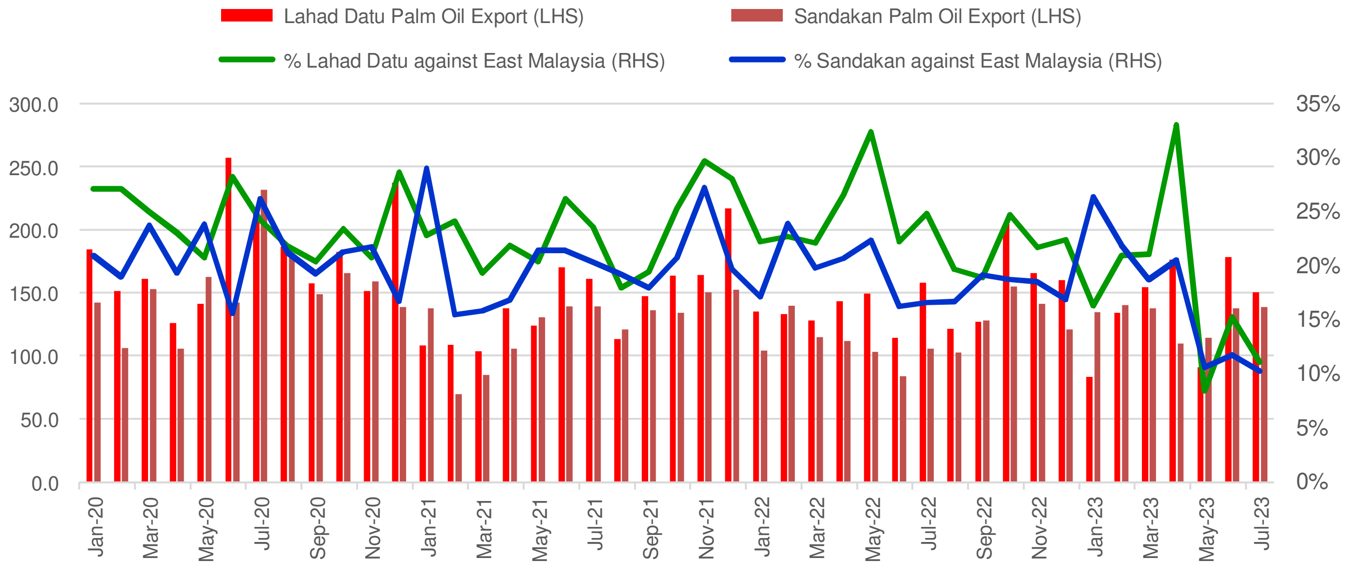
Source: Company

EXHIBIT 5: EXTERNAL TRADE VOLUME INDEX (2010 = 100)



Source: External Trade Indices, Department of Statistics Malaysia

EXHIBIT 6: EXPORT OF PALM OIL VIA LAHAD DATU AND SANDAKAN



Source: Economics and Industry Development Division, Malaysian Palm Oil Board

EXHIBIT 7: PB BAND CHART

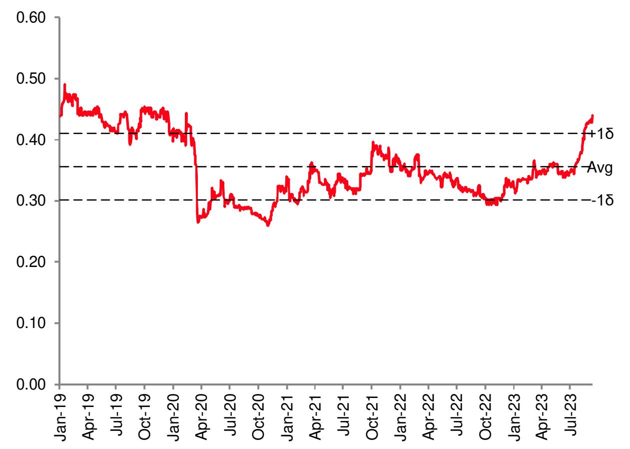


EXHIBIT 8: PE BAND CHART

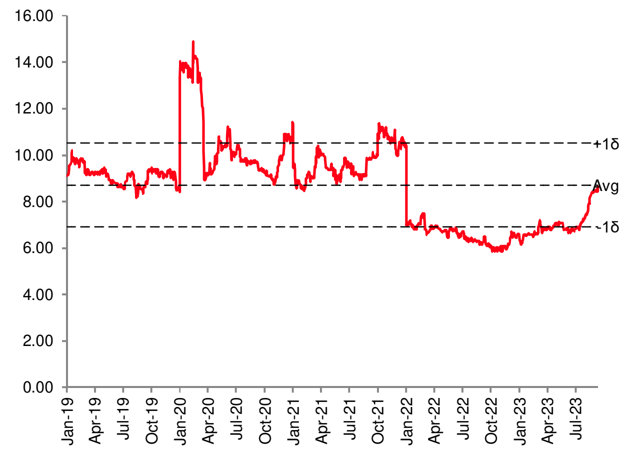


EXHIBIT 9: ESG RATING

Overall	★	★	★		
Zero-carbon initiatives	★	★	★	★	
Pollution control	★	★	★	★	
Sustainable industrialisation	★	★	★		
Diversity and inclusion	★	★	★		
Employee welfare	★	★	★	★	
Corporate social responsibilities	★	★	★	★	
Accessibility and transparency	★	★			
Supply chain auditing	★	★			

*We accord a discount/premium of **-6%, -3%, 0%, +3%** and **+6%** on fundamental fair value based on the overall ESG rating as appraised by us, from 1-star to 5-star*

Source: AmInvestment Bank

EXHIBIT 10: FINANCIAL DATA

Income Statement (RM mil, YE 31 Dec)	FY21	FY22	FY23F	FY24F	FY25F
Revenue	251.3	302.0	318.4	328.2	339.6
EBITDA	**104.3**	**112.9**	**128.8**	**163.6**	**165.9**
Depreciation/Amortisation	(48.6)	(59.0)	(44.7)	(47.0)	(49.4)
Operating income (EBIT)	55.7	53.9	84.1	116.6	116.5
Other income & associates	-	-	-	-	-
Net interest	10.9	2.7	(2.6)	(33.2)	(30.9)
Exceptional items	(8.0)	10.4	-	-	-
Pretax profit	**58.6**	**67.0**	**81.5**	**83.3**	**85.6**
Taxation	(19.1)	(7.9)	(19.6)	(20.0)	(20.5)
Minorities/pref dividends	-	-	-	-	-
Net profit	39.5	59.1	61.9	63.3	65.1
Core net profit	**47.6**	**48.7**	**61.9**	**63.3**	**65.1**

Balance Sheet (RM mil, YE 31 Dec)	FY21	FY22	FY23F	FY24F	FY25F
Fixed assets	859.3	882.9	920.5	960.3	1,002.3
Intangible assets	-	-	-	-	-
Other long-term assets	219.0	295.4	295.4	295.4	295.4
Total non-current assets	**1,078.3**	**1,178.4**	**1,215.9**	**1,255.7**	**1,297.7**
Cash & equivalent	79.9	114.4	573.5	535.1	497.9
Stock	10.6	29.6	8.8	9.0	9.2
Trade debtors	115.8	24.6	70.3	71.9	73.7
Other current assets	115.2	132.2	132.2	132.2	132.2
Total current assets	**321.5**	**300.8**	**784.8**	**748.2**	**713.0**
Trade creditors	12.7	9.9	9.0	9.1	9.3
Short-term borrowings	-	6.5	300.6	279.6	260.1
Other current liabilities	53.1	60.1	60.1	60.1	60.1
Total current liabilities	**65.8**	**76.5**	**369.6**	**348.8**	**329.5**
Long-term borrowings	10.3	59.3	247.7	230.4	214.4
Other long-term liabilities	190.9	165.2	165.2	165.2	165.2
Total long-term liabilities	**201.2**	**224.5**	**412.8**	**395.6**	**379.5**
Shareholders' funds	**1,132.7**	**1,178.0**	**1,218.3**	**1,259.5**	**1,301.7**
Minority interests	-	-	-	-	-
BV/share (RM)	3.28	3.41	3.52	3.64	3.76

Cash Flow (RM mil, YE 31 Dec)	FY21	FY22	FY23F	FY24F	FY25F
Pretax profit	58.6	67.0	81.5	83.3	85.6
Depreciation/Amortisation	48.6	59.0	44.7	47.0	49.4
Net change in working capital	(8.5)	(21.6)	(25.9)	(1.7)	(1.8)
Others	(23.7)	(21.2)	(16.9)	13.2	10.3
Cash flow from operations	**75.0**	**83.3**	**83.4**	**141.9**	**143.6**
Capital expenditure	(35.2)	(33.0)	(82.3)	(86.8)	(91.5)
Net investments & sale of fixed assets	(17.0)	(37.9)	-	-	-
Others	6.5	(40.8)	3.4	17.2	16.1
Cash flow from investing	**(45.7)**	**(111.7)**	**(78.8)**	**(69.5)**	**(75.4)**
Debt raised/(repaid)	(8.4)	24.7	482.3	(38.2)	(35.6)
Equity raised/(repaid)	-	-	-	-	-
Dividends paid	(13.1)	(8.3)	(21.7)	(22.2)	(22.8)
Others	(13.5)	40.7	(6.1)	(50.4)	(46.9)
Cash flow from financing	**(35.0)**	**57.1**	**454.6**	**(110.8)**	**(105.3)**
Net cash flow	**(5.8)**	**28.7**	**459.1**	**(38.4)**	**(37.2)**
Net cash/(debt) b/f	65.7	59.9	88.6	547.7	509.3
Net cash/(debt) c/f	59.9	88.6	547.7	509.3	472.1

Key Ratios (YE 31 Dec)	FY21	FY22	FY23F	FY24F	FY25F
Revenue growth (%)	10.2	20.2	5.4	3.1	3.5
EBITDA growth (%)	6.7	8.2	14.1	27.0	1.4
Pretax margin (%)	23.3	22.2	25.6	25.4	25.2
Net profit margin (%)	15.7	19.6	19.5	19.3	19.2
Interest cover (x)	nm	nm	31.9	3.5	3.8
Effective tax rate (%)	32.5	11.8	24.0	24.0	24.0
Dividend payout (%)	35.0	8.8	35.0	35.0	35.0
Debtors turnover (days)	151	85	54	79	78
Stock turnover (days)	14	24	22	10	10
Creditors turnover (days)	18	14	11	10	10

Source: Company, AmInvestment Bank Bhd estimates

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