

CTOS Digital Berhad (CTOS MK)

Post-briefing update

Maintain BUY

Following the analyst briefing, we remain upbeat on CTOS' earnings trajectory in the coming quarters ahead. The subsiding Omicron could translate to accelerating new activations for its Commercial segment, while ARPU across its segments may trend better on VAS upselling. Expectation on the final decision of its pioneer tax status application, however, has been pushed back to 2H22. We maintain our earnings forecast and MYR2.17 TP, based on 2.3x PEG multiple.

Additional commentary on 1Q22 performance

The good: 1) Revenue from Key Account segment grew by 23% YoY in 1Q22 due to higher ticket size from higher take-up rate on its VAS, 2) D2C revenue grew by 29% YoY despite the introduction of eCCRIS in Feb, reflecting strong proposition of CTOS' credit solutions, and 3) EBITDA margin improved 1.1ppt sequentially to 39.4% due to operating leverage, partially offsetting the higher staff and IT-support cost. The bad: 1) Revenue performance from Commercial - MY was the weakest at just +3% YoY due to subdued new account activation as Omicron spiked in Jan and Feb, but recovered noticeably towards the end of 1Q22.

Update on its tax relief situation

Management clarified that there are two stages to its tax relief situation. Under the Grandfathering and Transitional Guidelines, the tax relief for the first 5-year period was cut short, resulting in an incremental RM4.1m tax incurred in 2H21. Management has applied for the relief during this transitional period, and anticipates a positive outcome by May 2022. The latter part is the second 5-year pioneer status, in which the application is pending the final approval by MDEC/MOF. Approval would grant a further RM4.3m in tax write-backs as at end-1Q22 and normalisation in the tax rate thereafter. Despite the optimism, the management expects the final outcome to take up to 6 months to materialise. We maintain our 1% effective tax rate assumption for FY22E.

Key growth drivers intact

Management remained upbeat on its business prospects, with key growth drivers being 1) higher take-up rate on its VAS across both Key Account and Commercial customers, improving upward ARPU trend, 2) tapping on its associates to cross-sell its services, 3) higher financial awareness among the retail market that leads to higher conversion to paying accounts, and 4) new growth avenue from proliferation of digital moneylenders and digital banks. At 41.1x FY22E, it is trading at a slight discount to its 9-month average of 43x.

| FYE Dec (MYR m) | FY20A | FY21A | FY22E | FY23E | FY24E |
|------------------------------|-------|----------|-------|----------|----------|
| Revenue | 140 | 153 | 176 | 201 | 227 |
| EBITDA | 54 | 65 | 77 | 89 | 103 |
| Core net profit | 43 | 50 | 85 | 100 | 116 |
| Core EPS (sen) | 1.9 | 2.3 | 3.7 | 4.3 | 5.0 |
| Core EPS growth (%) | 8.4 | 16.0 | 63.9 | 16.8 | 16.3 |
| Net DPS (sen) | 0.0 | 1.2 | 2.0 | 2.4 | 2.8 |
| Core P/E (x) | na | 80.2 | 41.4 | 35.4 | 30.5 |
| P/BV (x) | na | 12.9 | 6.5 | 6.3 | 5.7 |
| Net dividend yield (%) | na | 0.7 | 1.3 | 1.6 | 1.8 |
| ROAE (%) | 73.2 | 20.8 | 20.6 | 18.4 | 19.6 |
| ROAA (%) | 31.0 | 15.6 | 17.2 | 15.2 | 16.4 |
| EV/EBITDA (x) | 67.6 | 60.9 | 43.9 | 37.4 | 32.0 |
| Net gearing (%) (incl perps) | 91.6 | net cash | 2.3 | net cash | net cash |
| Consensus net profit | - | - | 80 | 95 | 109 |
| MKE vs. Consensus (%) | - | - | 7.3 | 4.8 | 6.4 |

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BUY

| | |
|-----------------------|-----------------|
| Share Price | MYR 1.53 |
| 12m Price Target | MYR 2.17 (+43%) |
| Previous Price Target | MYR 2.17 |

Company Description

CTOS Digital is a credit rating agency, principally involved in the business of credit reporting, digital related services, and investment holding.

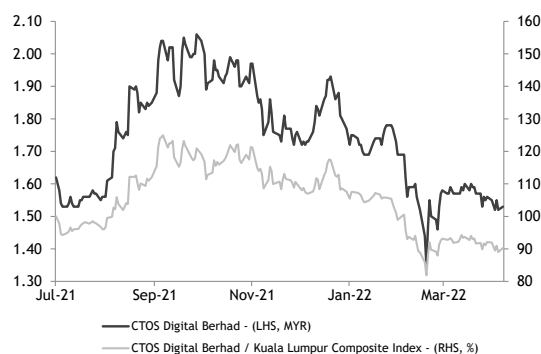
Statistics

| | |
|------------------------|--------------------|
| 52w high/low (MYR) | na/na |
| 3m avg turnover (USDm) | 1.9 |
| Free float (%) | 52.6 |
| Issued shares (m) | 2,310 |
| Market capitalisation | MYR3.5B USD811M |

Major shareholders:

| | |
|-----------------|-------|
| Inodes | 30.3% |
| Chung Tze Keong | 4.5% |
| Chung Tze Wen | 4.5% |

Price Performance



| | -1M | -3M | -12M |
|-----------------------|-----|------|------|
| Absolute (%) | (3) | (11) | na |
| Relative to index (%) | (2) | (16) | na |

Source: FactSet

Abbreviations:

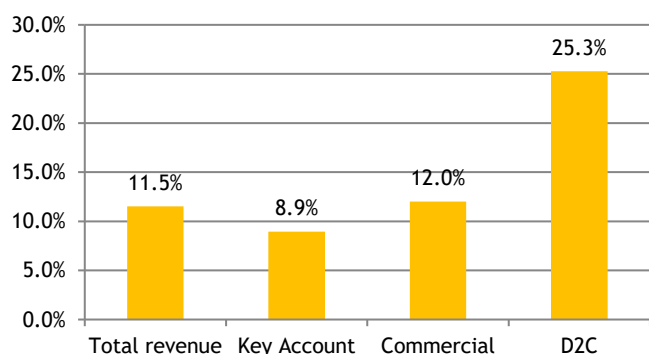
VAS= Value-added services
SME= Small and medium enterprises
FI= Financial institutions
UNSGD= UN Sustainable Development Goals
ppt= percentage points

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Value Proposition

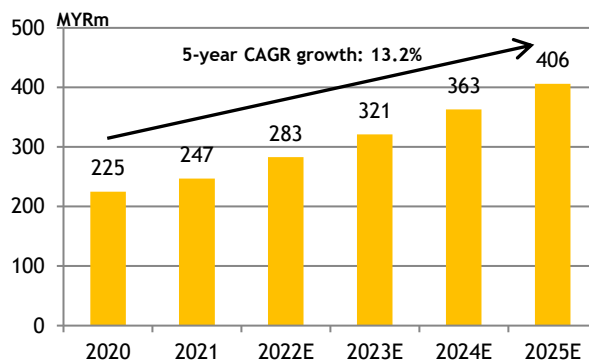
- CTOS Digital is the market leading credit reporting agency in Malaysia with a 71.2% revenue market share in 2020, while 24.825%-owned BOL is the largest company information bureau in Thailand, with an estimated 59% market share.
- With over 30 years of experience, the company has an extensive database of about 15m consumer profiles and 8m company and business profiles. CTOS Digital is said to have one of the largest trade reference databases in Malaysia.
- CTOS Digital caters to three types of customers: Key Accounts, Commercial and Direct-to-Consumer (“D2C”). The growth in number of accounts is the highest for D2C at 20-30% per annum, followed by Commercial at 15-20% p.a.

3-year revenue CAGR (2018-2021) by customer type



Source: Company

Industry outlook



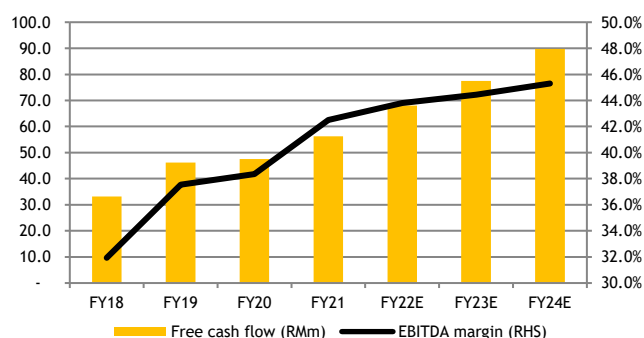
Source: IDC Market Research

- According to IDC Market Research (Malaysia) Sdn Bhd (“IDC”), the revenue of the credit reporting industry in ASEAN totalled MYR991m in 2020.
- IDC estimates the size of Malaysia’s credit reporting industry to be MYR225m in 2020 (i.e. 23% the size of the ASEAN market).
- The domestic market expanded at a 5-year CAGR (2016-2020) of 12.9%, and IDC predicts that it will continue to grow in revenue at a 5-year CAGR (2021E-2025E) of 13.2%.
- IDC projects 2021E-2025E revenue CAGR of 28.2% in respect of Malaysia’s total addressable market. High growth sectors with a CAGR of 40% from 2016-2025E would be automotive, media technology, insurance, real estate, retail and healthcare.

Financial Metrics

- We project a 3-year (FY20-FY23E) core net profit CAGR of 33%, driven primarily by growth across all customer segments and average revenue per customer (i.e. from new offerings, new verticals, more value-added products).
- Our forecasts have imputed annual customer/account growth of 15-20% for the Commercial and D2C segments, -2% for the Key Account segment.
- We expect profit margins to improve as the group is able to enjoy greater economies of scale (i.e. improving revenue and relatively stable costs).
- 60% dividend payout policy with low capital expenditure (“capex”) requirements. Free cash flow generation is estimated to range between MYR56m-90m in FY21-FY24E.

FCF and EBITDA margins (FY18-FY23E)



Source: Company, Maybank IBG Research

Swing Factors

Upside

- Greater marketing efforts amid an improved economic situation would drive accounts growth.
- The launch of new digital solutions and the penetration of new sectors will spur faster adoption and demand for CTOS Digital’s services.
- Expansion into new regional markets or potential synergistic M&As that could further broaden the group’s reach and market share.

Downside

- Slower-than-expected economic growth, particularly as a result of an extended COVID-19 pandemic that leads to more severe lockdowns, as this would negatively impact demand, particularly from SMEs.
- Breaches in security/compliance that could result in the revocation of its CRA Certificate or breaches to the Personal Data Protection Act.
- The entry of new players into the credit reporting space that could eventually erode the group’s market share.

| | |
|----------------------------------|----|
| Risk Rating & Score ¹ | na |
| Score Momentum ² | na |
| Last Updated | na |
| Controversy Score ³ | na |

Business Model & Industry Issues

- CTOS provides credit assessment services of business entities and individuals. The company operates in a highly regulated industry, governed by the CRA Act 2010 and Personal Data Protection Act (PDPA). It has a paramount responsibility to operate the vast credit information and personal data of its clients with the highest level of integrity, security, & transparency.
- Its business model is susceptible to Social and Governance issues, as the business revolves around the processing of highly sensitive data of businesses and individuals, which are susceptible to cybersecurity threats that could have serious financial and reputational repercussions in any events of data breach.
- The management of CTOS promotes good governance and transparency in its strategic decisions and business direction. Its business model also promotes greater financial awareness, literacy and inclusion, which is positive to the society.
- Traction on its sustainability journey has been encouraging i.e. CTOS was recently included in FBM EMAS Index in Dec-21, and is aiming to be included in FTSE4Good Index by 2022.

Material E issues

- CTOS' products and services can be channelled digitally to its clients, therefore given its highly digitalised operations, the group has minimal needs for paperwork and physical travelling, and hence a relatively low overall carbon footprint. The group however has 8 physical service centre premises across both Peninsular and East Malaysia.
- The group aims to have better disclosure on its sustainability practices on the upcoming 2021 Annual Report.

Material S issues

- CTOS runs a financial education programme all year-round across both online and offline mediums to provide financial education to the public. It also runs public campaigns by providing free access to MyCTOS Score Report for a few months in 2020 in order to drive the financial awareness amongst the public.
- Through its credit assessment products, the underserved segment could likely have better access to credit.
- The group aims to have better disclosure on its sustainability practices on the upcoming 2021 Annual Report.

Key G metrics and issues

- The board currently has 7 members (excluding one Alternate Director), in which 5 of them (71%) are Independent Non-Executive Directors (INEDs), including the Chairman. 3 out of 7 are female directors, meeting the 30% threshold.
- There are 3 members in each of the audit, risk management, remuneration and nomination committees.
- The Alternate Director is the major shareholder's (Inodes) representation on the board.
- The total remuneration of the CEO in FY20 made up 3.6% of the group's FY20 profit after tax.
- PricewaterhouseCoopers is the auditor for CTOS in FY20 and has been the auditor for the group for 6 straight years.
- On 30 September 2021 the CCRIS services was temporarily suspended by the BNM in response to a potential cyber attack threat. As a result, all credit bureaus, including CTOS, were denied access to the CCRIS service until each bureau demonstrated their security prowess. The suspension, specifically for CTOS, lasted for 1.5 months and resulted in a revenue loss of -4.5%.
- While there were no evidences of data breach from said threat, it highlighted the vulnerability of CTOS' reliance on its data partners to provide its services to the market. It also highlights CTOS' governance risks that may emerge from cybersecurity threats.

¹**Risk Rating & Score** - derived by Sustainalytics and assesses the company's exposure to unmanaged ESG risks. Scores range between 0 - 50 in order of increasing severity with low/high scores & ratings representing negligible/significant risk to the company's enterprise value, respectively, from ESG-driven financial impacts. ²**Score Momentum** - indicates changes to the company's score since the last update - a **negative** integer indicates a company's improving risk score; a **positive** integer indicates a deterioration. ³**Controversy Score** - reported periodically by Sustainalytics in the event of material ESG-related incident(s), with the impact severity scores of these events ranging from Category 0-5 (0 - no reports; 1 - negligible risks; ...; 5 - poses serious risks & indicative of potential structural deficiencies at the company).

1. Acquiring additional 9.1% stake in RAM Holdings Bhd

CTOS announced yesterday that it is acquiring additional 910k shares of RAM Holdings Bhd, an equivalent of 9.1% stake, for RM25.06mil. These shares were collectively owned by OCBC Bank (M) Bhd, Affin Bank Bhd and Affin Hwang Investment Bank Bhd. This will bring CTOS' total equity interest in RAM to 17.23%.

This acquisition will be funded via internally generated cash flow and the balance IPO proceeds that were still unutilised, which we estimated to be around RM14.5mil. This acquisition will also allow greater collaboration between CTOS and RAM on leveraging on each other's expertise in credit assessment and analytics, as well as cross-sell across each other's customer base. The impact of this acquisition to FY22E net profit could be marginal at +MYR1mil per annum, as the incremental associate profits of MYR1.3mil may be offset by lower interest income by MYR0.2-0.3mil, per our estimate. We make no changes to our estimates, pending the completion of this acquisition.

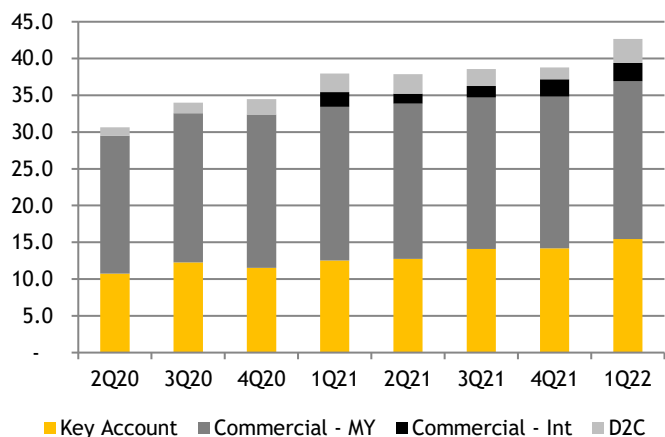
Fig 1: IPO proceeds utilised for acquisitions in 2021

| Date | Acquired entity | Stake acquired | Purchase considerations (RMm) |
|--|------------------------------------|----------------|-------------------------------|
| Jul-21 | RAM Holdings Bhd | 4.60% | 10.1 |
| Aug-21 | Business Online Public Company Ltd | 2.65% | 26.8 |
| Dec-21 | RAM Holdings Bhd | 3.50% | 7.6 |
| Total | | | 44.5 |
| Total proceeds from IPO allocated for acquisitions (RMm) | | | 59.0 |
| Outstanding balance (RMm) | | | 14.5 |

Source: Maybank IBG Research

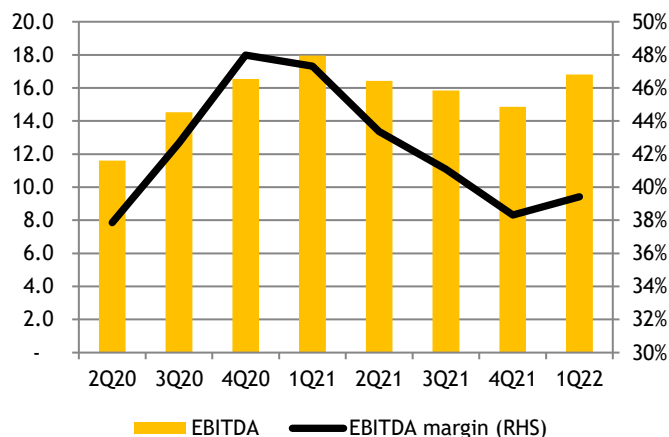
2. Focus charts

Fig 2: Revenue breakdown by segment (MYRm)



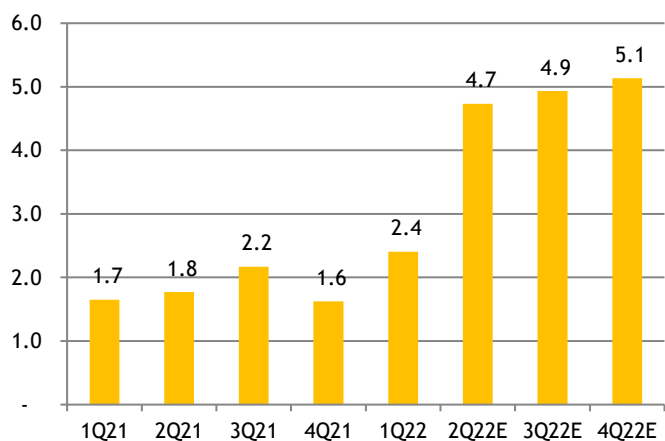
Source: Company, Maybank IBG Research

Fig 3: EBITDA (MYRm) and EBITDA margin



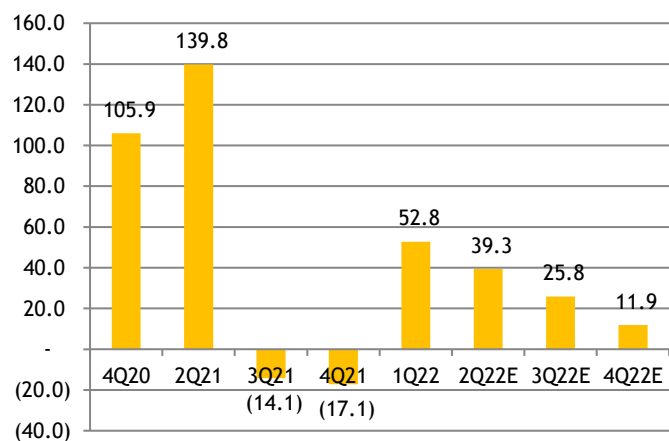
Source: Company, Maybank IBG Research

Fig 4: Associates' profit projection (MYRm)



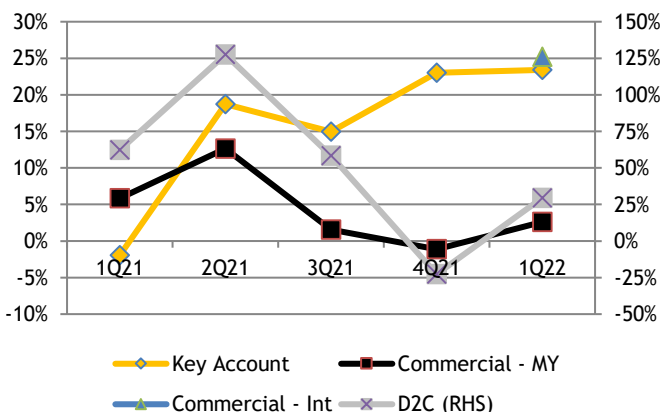
Source: Company, Maybank IBG Research

Fig 5: Net debt/(net cash) trend (MYRm)



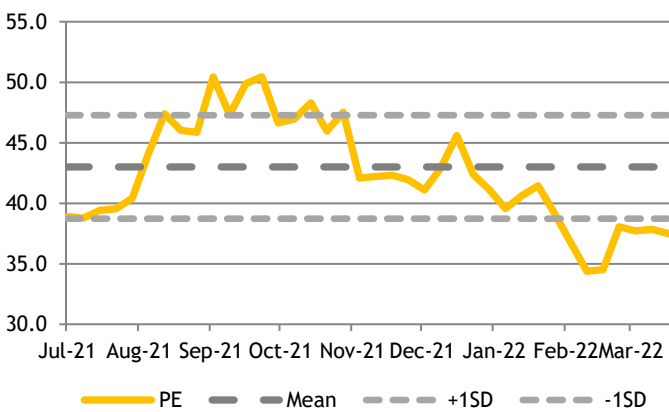
Source: Company, Maybank IBG Research

Fig 6: YoY change in revenue trend by business segment



Source: Company, Maybank IBG Research

Fig 7: PE chart



Source: Bloomberg, Maybank IBG Research

Fig 8: TP derivation

| | |
|---|-------------|
| FY22E EPS (sen) | 3.70 |
| Earnings 2Y CAGR 21-23E (%) | 25.7 |
| PEG ratio (x) - 10% discount to regional median of 2.5x | 2.28 |
| Implied PER at FY22E (x) | 58.6 |
| Value per share (RM) | 2.17 |

Source: Maybank IBG Research

Risk statement

The risks to our investment thesis and earnings estimates are 1) emerging competition from smaller players that may cap business opportunities among new avenues such as challenger banks and digital moneylenders, and 2) increasing cybersecurity threats as adoption of digital economy rises within the region, which may lead to disruption in data access of CTOS' partners and thus impeding the continuity of CTOS' businesses.

| FYE 31 Dec | FY20A | FY21A | FY22E | FY23E | FY24E |
|-------------------------------------|--------------|--------------|--------------|--------------|--------------|
| Key Metrics | | | | | |
| P/E (reported) (x) | na | 91.4 | 39.4 | 33.7 | 29.0 |
| Core P/E (x) | na | 80.2 | 41.4 | 35.4 | 30.5 |
| P/BV (x) | na | 12.9 | 6.5 | 6.3 | 5.7 |
| P/NTA (x) | na | 17.4 | 7.6 | 7.2 | 6.5 |
| Net dividend yield (%) | na | 0.7 | 1.3 | 1.6 | 1.8 |
| FCF yield (%) | na | 1.5 | 2.5 | 3.0 | 3.5 |
| EV/EBITDA (x) | 67.6 | 60.9 | 43.9 | 37.4 | 32.0 |
| EV/EBIT (x) | 78.9 | 70.2 | 48.0 | 40.1 | 34.0 |
| INCOME STATEMENT (MYR m) | | | | | |
| Revenue | 140.5 | 153.2 | 175.5 | 200.6 | 226.6 |
| EBITDA | 53.9 | 65.1 | 76.9 | 89.2 | 102.6 |
| Depreciation | (7.3) | (7.7) | (5.4) | (4.9) | (4.6) |
| Amortisation | (0.4) | (0.9) | (1.0) | (1.2) | (1.6) |
| EBIT | 46.2 | 56.5 | 70.4 | 83.0 | 96.5 |
| Net interest income / (exp) | (4.0) | (5.3) | (1.3) | (1.0) | (0.6) |
| Associates & JV | 1.8 | 7.2 | 17.2 | 24.1 | 27.5 |
| Exceptionals | (2.3) | (6.1) | 0.0 | 0.0 | 0.0 |
| Other pretax income | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 |
| Pretax profit | 41.7 | 52.3 | 86.4 | 106.1 | 123.4 |
| Income tax | (2.4) | (9.3) | (1.0) | (6.4) | (7.4) |
| Minorities | 1.2 | 0.6 | 0.0 | 0.0 | 0.0 |
| Discontinued operations | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 |
| Reported net profit | 40.5 | 43.6 | 85.4 | 99.7 | 116.0 |
| Core net profit | 42.8 | 49.6 | 85.4 | 99.7 | 116.0 |
| BALANCE SHEET (MYR m) | | | | | |
| Cash & Short Term Investments | 26.4 | 17.1 | 46.3 | 91.4 | 143.4 |
| Accounts receivable | 28.2 | 25.2 | 28.8 | 32.9 | 37.2 |
| Inventory | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 |
| Property, Plant & Equip (net) | 16.9 | 14.7 | 13.3 | 12.4 | 11.8 |
| Intangible assets | 49.6 | 79.2 | 78.2 | 77.0 | 75.4 |
| Investment in Associates & JVs | 150.8 | 172.9 | 413.4 | 413.4 | 413.4 |
| Other assets | 4.1 | 51.5 | 51.5 | 51.5 | 51.5 |
| Total assets | 276.0 | 360.6 | 631.5 | 678.6 | 732.7 |
| ST interest bearing debt | 132.3 | 0.0 | 58.2 | 58.2 | 58.2 |
| Accounts payable | 17.1 | 21.9 | 21.6 | 24.4 | 27.2 |
| LT interest bearing debt | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 |
| Other liabilities | 11.0 | 31.0 | 31.0 | 31.0 | 31.0 |
| Total Liabilities | 160.3 | 52.8 | 110.8 | 113.6 | 116.3 |
| Shareholders Equity | 110.8 | 307.7 | 520.8 | 565.1 | 616.4 |
| Minority Interest | 5.0 | 0.0 | 0.0 | 0.0 | 0.0 |
| Total shareholder equity | 115.7 | 307.7 | 520.8 | 565.1 | 616.4 |
| Total liabilities and equity | 276.0 | 360.6 | 631.5 | 678.6 | 732.7 |
| CASH FLOW (MYR m) | | | | | |
| Pretax profit | 41.7 | 52.3 | 86.4 | 106.1 | 123.4 |
| Depreciation & amortisation | 7.7 | 8.6 | 6.4 | 6.1 | 6.2 |
| Adj net interest (income)/exp | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 |
| Change in working capital | (1.2) | (1.0) | (4.4) | (6.6) | (7.2) |
| Cash taxes paid | (2.1) | (3.3) | (1.0) | (6.4) | (7.4) |
| Other operating cash flow | 3.5 | 5.5 | 2.2 | 7.4 | 8.0 |
| Cash flow from operations | 49.6 | 62.2 | 89.7 | 106.6 | 123.0 |
| Capex | (4.7) | (2.0) | (4.0) | (4.0) | (4.0) |
| Free cash flow | 44.9 | 60.2 | 85.7 | 102.6 | 119.0 |
| Dividends paid | (10.5) | (41.0) | (46.2) | (55.4) | (64.7) |
| Equity raised / (purchased) | 0.0 | 220.0 | 173.8 | 0.0 | 0.0 |
| Change in Debt | 107.4 | (138.6) | 58.2 | 0.0 | 0.0 |
| Other invest/financing cash flow | (122.1) | (108.5) | (242.2) | (2.0) | (2.3) |
| Effect of exch rate changes | (0.2) | 0.2 | 0.0 | 0.0 | 0.0 |
| Net cash flow | 19.4 | (7.8) | 29.2 | 45.1 | 52.0 |

| FYE 31 Dec | FY20A | FY21A | FY22E | FY23E | FY24E |
|--|-------|----------|-------|----------|----------|
| Key Ratios | | | | | |
| Growth ratios (%) | | | | | |
| Revenue growth | 8.8 | 9.0 | 14.6 | 14.3 | 13.0 |
| EBITDA growth | 11.2 | 20.8 | 18.1 | 16.0 | 15.1 |
| EBIT growth | 9.5 | 22.3 | 24.7 | 17.9 | 16.2 |
| Pretax growth | 1.0 | 25.6 | 65.0 | 22.9 | 16.3 |
| Reported net profit growth | 3.9 | 7.5 | 96.1 | 16.8 | 16.3 |
| Core net profit growth | 8.4 | 16.0 | 72.1 | 16.8 | 16.3 |
| Profitability ratios (%) | | | | | |
| EBITDA margin | 38.4 | 42.5 | 43.8 | 44.4 | 45.3 |
| EBIT margin | 32.9 | 36.9 | 40.1 | 41.4 | 42.6 |
| Pretax profit margin | 29.7 | 34.2 | 49.2 | 52.9 | 54.5 |
| Payout ratio | 0.0 | 59.7 | 51.5 | 52.9 | 53.1 |
| DuPont analysis | | | | | |
| Net profit margin (%) | 28.8 | 28.4 | 48.7 | 49.7 | 51.2 |
| Revenue/Assets (x) | 0.5 | 0.4 | 0.3 | 0.3 | 0.3 |
| Assets/Equity (x) | 2.5 | 1.2 | 1.2 | 1.2 | 1.2 |
| ROAE (%) | 73.2 | 20.8 | 20.6 | 18.4 | 19.6 |
| ROAA (%) | 31.0 | 15.6 | 17.2 | 15.2 | 16.4 |
| Liquidity & Efficiency | | | | | |
| Cash conversion cycle | nm | nm | nm | nm | nm |
| Days receivable outstanding | 36.2 | 62.7 | 55.4 | 55.4 | 55.7 |
| Days inventory outstanding | nm | nm | nm | nm | nm |
| Days payables outstanding | nm | nm | nm | nm | nm |
| Dividend cover (x) | nm | 1.7 | 1.9 | 1.9 | 1.9 |
| Current ratio (x) | 0.3 | 1.8 | 1.1 | 1.5 | 2.0 |
| Leverage & Expense Analysis | | | | | |
| Asset/Liability (x) | 1.7 | 6.8 | 5.7 | 6.0 | 6.3 |
| Net gearing (%) (incl perps) | 91.6 | net cash | 2.3 | net cash | net cash |
| Net gearing (%) (excl. perps) | 91.6 | net cash | 2.3 | net cash | net cash |
| Net interest cover (x) | 11.5 | 10.7 | 55.5 | 82.8 | nm |
| Debt/EBITDA (x) | 2.5 | 0.0 | 0.8 | 0.7 | 0.6 |
| Capex/revenue (%) | 3.4 | 1.3 | 2.3 | 2.0 | 1.8 |
| Net debt/ (net cash) | 105.9 | (17.1) | 11.9 | (33.2) | (85.2) |

Source: Company; Maybank IBG Research

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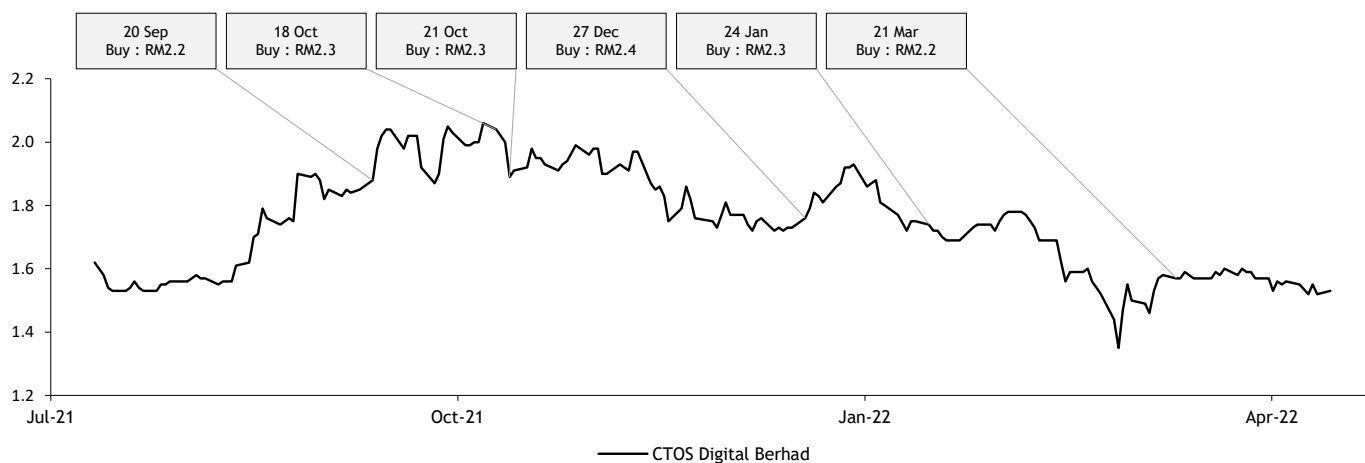
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