

Singapore

ADD (no change)

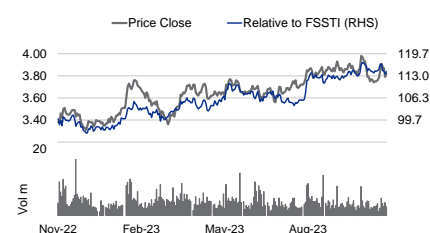
Consensus ratings*: Buy 11 Hold 3 Sell 0

Current price:	S\$3.82
Target price:	S\$4.27
Previous target:	S\$4.27
Up/downside:	11.8%
CGS-CIMB / Consensus:	1.5%
Reuters:	STEG.SI
Bloomberg:	STE SP
Market cap:	US\$8,761m
	S\$11,899m
Average daily turnover:	US\$10.59m
	S\$14.42m
Current shares o/s:	3,122m
Free float:	49.0%

*Source: Bloomberg

Key changes in this note

- FY23-25F core EPS trimmed by 0.4-1.1% in view of management's lowered Satcom EBIT guidance.



Source: Bloomberg

Price performance	1M	3M	12M
Absolute (%)	0.3	2.7	13.7
Relative (%)	1.3	8.1	14.7

Major shareholders

	% held
Temasek Holdings	50.0
Capital Group	5.0
BlackRock	1.8

Analyst(s)



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ST Engineering

Set for a stronger FY24F

- STE guided for weaker yoy FY23F USS EBIT. We expect margin rebound in FY24F on ramp-up of major projects and streamlined Satcom costs.
- We think FY24-25F Aerospace EBIT margins could sustain at 9-10%, on stronger operating leverage and improving PTF profitability.
- Order book remained elevated at S\$27.5bn as of 3Q23. Reiterate Add, with an unchanged TP of S\$4.27, based on blended valuation (Fig 2).

Decent revenue growth led by aerospace, while order wins tapered

ST Engineering's (STE) 3Q23 revenue of S\$2.4bn (-5% qoq, +9% yoy) was in line, with 9M23 revenue forming 75% of both our and Bloomberg consensus' FY23F forecasts. Commercial Aerospace (CA) revenue was the key driver (+27% yoy), while Urban Solutions & Satcom (USS) recorded slight yoy growth (+6% yoy). 3Q23 order wins tapered to S\$2.2bn (-53% qoq, -54% yoy), with all three segments seeing yoy declines.

USS: margins likely to rebound in FY24F; Satcom review ongoing

STE guided for FY23F USS EBIT to be positive but lower yoy, largely due to lower-than-expected Satcom revenue from delayed customer spending and ongoing transformation challenges. We are not too concerned of the lowered guidance as we had already baked in weak USS EBIT contribution in FY23F. Regarding the ongoing lawsuits against New York City's congestion pricing plan, we do not foresee any material delays impacting subsidiary TransCore's portion of the project (US\$500m) as TransCore will continue to recognise revenue based on project milestones set forth by the Metropolitan Transportation Authority (MTA). We expect USS to see a strong margin rebound in FY24F, on: 1) a ramp-up of major projects (e.g. Taiwan rail mobility projects, US tolling contracts), and 2) optimised costs following Satcom transformation.

Positive Aerospace trends; PTF on track to EBIT breakeven

Maintenance, repair, and overhaul (MRO) revenue grew yoy (amount undisclosed) in 3Q23, driven by both airframe and engine & component (E&C). Hangar utilisation is close to maxed out, while E&C shops' utilisation saw qoq improvement to 85%. STE continued to ramp up nacelle production rates in 3Q23, while passenger-to-freighter (PTF) conversion is on track to achieving EBIT breakeven by end-FY23F, according to STE. Expansion plans are on track, with: 1) Guangzhou hangar commencing in 1Q24F, and 2) Ezhou, Singapore, and Pensacola hangars commencing in 2025F.

Reiterate Add, with an unchanged TP of S\$4.27

STE expects to recognise more aircraft sales in 4Q23F (none recognised in 3Q23) and reduce its debt further; FY24F weighted average interest cost was guided at mid-3% (assuming 1 more rate hike). Reiterate Add on strong earnings growth over FY23-25F. Our TP is unchanged at S\$4.27, based on blended valuation. Key catalyst: stronger-than-expected USS margins. Key downside risks: project cost overruns, global economic slowdown impacting order wins.

Financial Summary

	Dec-21A	Dec-22A	Dec-23F	Dec-24F	Dec-25F
Revenue (S\$m)	7,693	9,035	9,822	10,487	11,157
Operating EBITDA (S\$m)	1,044	1,181	1,295	1,432	1,537
Net Profit (S\$m)	570.5	535.0	576.9	698.6	816.2
Core EPS (S\$)	0.18	0.15	0.19	0.22	0.26
Core EPS Growth	9.3%	(18.8%)	24.6%	21.1%	16.8%
FD Core P/E (x)	20.87	25.72	20.64	17.05	14.59
DPS (S\$)	0.15	0.16	0.16	0.16	0.16
Dividend Yield	3.93%	4.19%	4.19%	4.19%	4.19%
EV/EBITDA (x)	12.43	14.92	13.50	12.02	11.03
P/FCFE (x)	15.79	17.60	90.08	12.67	13.02
Net Gearing	49%	224%	213%	191%	165%
P/BV (x)	4.94	4.97	4.81	4.45	3.98
ROE	24.3%	19.2%	23.7%	27.1%	28.8%
% Change In Core EPS Estimates			(1.06%)	(0.73%)	(0.44%)
EPS/Consensus EPS (x)			0.98	1.04	1.08

SOURCES: CGS-CIMB RESEARCH, COMPANY REPORTS

Set for a stronger FY24F

Healthy DPS revenue growth, seeing good international demand

3Q23 Defence and Public Security (DPS) revenue was largely in line at S\$973m (-14% qoq, -4% yoy). Excluding the divestment of US Marine, DPS revenue was up 6% yoy, with growth led by Marine, Digital Systems, and Defence Aerospace sub-segments. STE shared that demand for defence projects were particularly strong in Europe and the Middle East; for example, STE said that its ammunition business in Europe and the Middle East was seeing good traction.

Satcom transformation well underway

STE has mostly concluded its workforce reduction exercise for the Satcom division, and expects to incur S\$5m in severance costs for 2H23F (1H23: incurred S\$2m already). As part of the transformation, STE is currently developing next generation platforms for both commercial and defence applications, as well as discussing with satellite operators to understand their future needs. Management disclosed that 3Q23 Satcom revenue was higher than the 1H23 quarterly average, but lower than their original expectations; this prompted the lowered EBIT guidance.

Valuation and recommendation

Reiterate Add. Our TP is unchanged at S\$4.27, still based on equal weight blended valuations (P/E, DCF, and dividend yield). Our P/E TP is based on 20x CY24F P/E, pegged to the group's 15-year trading average. We continue to like STE for its strong earnings growth trajectory over FY23-25F, backed by sustainable strong order win momentum and a massive order book of S\$27.5bn. Catalysts: stronger-than-expected USS margins, and large defence wins. Key downside risks: prolonged margin pressure in USS, project cost overruns impacting margins, and a global economic slowdown impacting order wins.

Figure 1: Results comparison

FYE Dec (S\$)	3Q23	3Q22	yoy % chg	2Q23	qoq % chg	9M23	9M22	yoy % chg	Prev. FY23F	Comments
Commercial Aerospace	982	776	26.6	983	(0.0)	2,838	2,180	30.2	3,488	Growth from both MRO and OEM business
Urban Solutions & Satcom	478	452	5.9	457	4.7	1,369	1,209	13.2	1,912	Likely driven by TransCore
Defence & Public Security	973	1,010	(3.6)	1,135	(14.3)	3,090	3,118	(0.9)	4,314	Lower yoy due to divestment of US marine business. Excluding US marine, revenue was up 6% yoy
Total revenue	2,434	2,237	8.8	2,574	(5.5)	7,297	6,507	12.1	9,714	In line. 9M23 formed 75% of both our and Bloomberg consensus FY23F

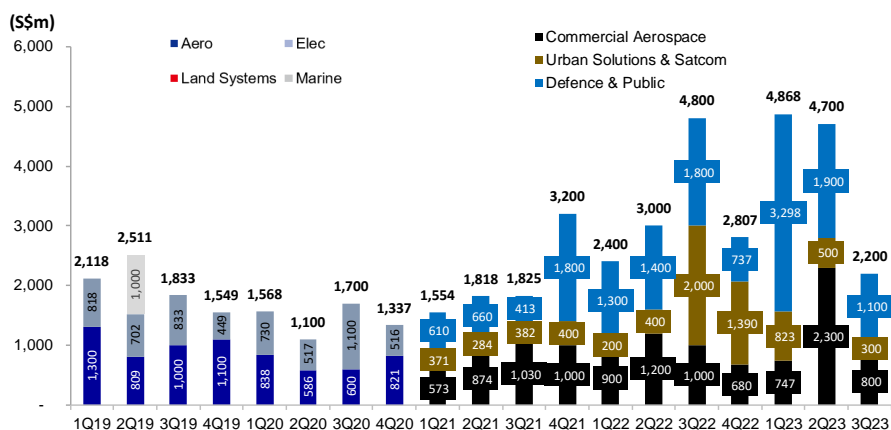
SOURCES: CGS-CIMB RESEARCH, COMPANY REPORTS

Figure 2: Blended valuations (equal weightage)

Method	Value per share (S\$)	Basis
P/E	4.51	20x CY24 EPS
DCF	4.29	WACC 7.7%, LTG 2%
Dividend yield (%)	4.00	4% net yield on FY23F DPS
Average	4.27	

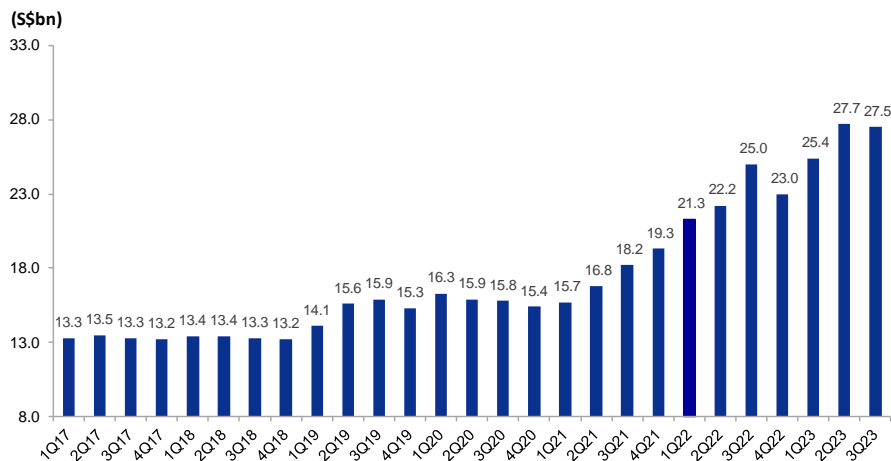
SOURCES: CGS-CIMB RESEARCH ESTIMATES, COMPANY REPORTS

Figure 3: 3Q23 order wins tapered to S\$2.2bn



SOURCES: CGS-CIMB RESEARCH, COMPANY REPORTS

Figure 4: Order book remained elevated at S\$27.5bn as at end-3Q23



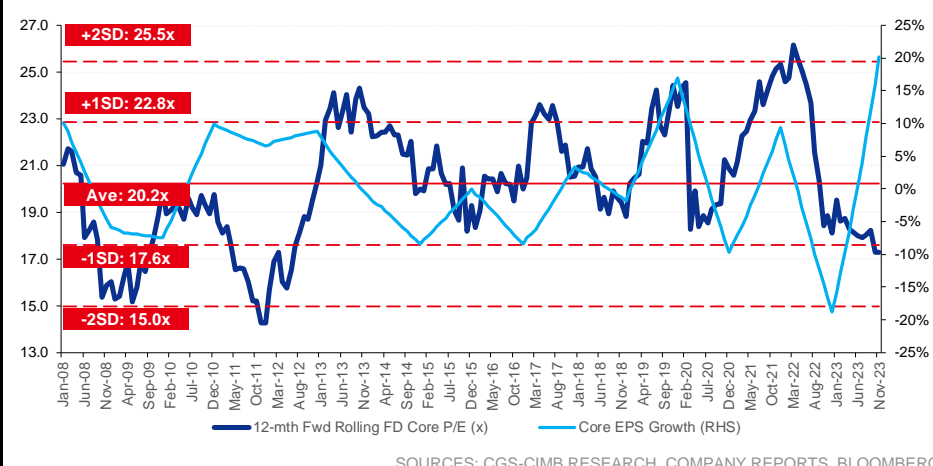
SOURCES: CGS-CIMB RESEARCH, COMPANY REPORTS

Figure 5: Earnings revision

FYE Dec (S\$ m)	New			Old			% change		
	FY23F	FY24F	FY25F	FY23F	FY24F	FY25F	FY23F	FY24F	FY25F
Revenue	9,821.7	10,487.1	11,157.1	9,714.3	10,408.2	11,071.3	1.1%	0.8%	0.8%
Gross profit	2,085.8	2,316.0	2,513.7	2,079.1	2,311.2	2,508.6	0.3%	0.2%	0.2%
EBIT	848.9	992.6	1,103.2	856.2	998.1	1,109.3	-0.9%	-0.5%	-0.5%
Interest expense	(224.9)	(224.9)	(197.2)	(224.9)	(224.9)	(197.2)	0.0%	0.0%	0.0%
Net profit	576.9	698.6	816.2	583.1	703.7	819.9	-1.1%	-0.7%	-0.4%
Core net profit	576.9	698.6	816.2	583.1	703.7	819.9	-1.1%	-0.7%	-0.4%

SOURCES: CGS-CIMB RESEARCH ESTIMATES, COMPANY REPORTS

Figure 6: ST Engineering's 12-month forward rolling FD core P/E (x) vs. EPS growth




SOURCES: CGS-CIMB RESEARCH, COMPANY REPORTS, BLOOMBERG

Figure 7: Peer comparison

Company	Bbg Ticker	Recom.	Price (lcl curr)	Target Price (lcl curr)	Market Cap (US\$ m)	P/E (x) CY23F	P/E (x) CY24F	P/E (x) CY25F	2-year EPS CAGR (%)	P/BV (x) CY23F	P/BV (x) CY24F	Recurring ROE (%) CY23F	Dividend Yield (%) CY23F
Keppel Corporation	KEP SP	Add	6.26	8.70	8,122	11.2	10.1	9.4	11.8%	0.93	0.90	8.4%	5.7%
Capitaland Investment	CLI SP	Add	2.94	4.30	11,051	19.4	16.3	15.1	37.8%	0.92	0.88	4.9%	4.1%
Integrated global asset management - big cap simple average						15.3	13.2	12.3	24.8%	0.93	0.89	6.6%	4.9%
Seatrium Ltd	STM SP	Add	0.11	0.19	5,424	na	28.8	11.2	na	0.89	0.86	-7.8%	0.0%
Singapore offshore - big cap simple average						na	28.8	11.2	na	0.89	0.86	-7.8%	0.0%
COSCO SHIPPING International S	COS SP	NR	0.13	na	206	na	na	na	na	na	na	na	na
China CSSC Holdings Ltd	600150 CH	NR	25.50	na	15,645	40.9	17.5	12.6	502.7%	2.34	2.07	5.9%	0.8%
China Shipbuilding Industry Co	601989 CH	NR	3.94	na	12,324	197.0	23.2	14.6	na	1.07	1.03	0.4%	0.5%
CSSC Offshore and Marine Engin	600685 CH	NR	22.44	na	3,153	na	na	na	na	na	na	na	na
Yangzijiang Shipbuilding	YZJSGD SP	Add	1.49	1.96	4,334	8.7	7.6	7.0	20.8%	1.59	1.41	19.8%	4.4%
Chinese Shipbuilder simple average						82.2	16.1	11.4	261.7%	1.67	1.50	8.7%	1.9%
Korea Shipbuilding & Offshore	009540 KS	Add	97,100	119,000	5,247	26.0	9.0	5.7	na	0.68	0.62	2.7%	0.0%
Hyundai Mipo Dockyard	010620 KS	Reduce	74,500	83,000	2,272	na	17.9	12.8	na	1.40	1.30	-0.2%	0.0%
Samsung Heavy Industries	010140 KS	Add	7,150	10,900	4,804	96.7	22.7	13.1	na	1.72	1.60	1.8%	0.0%
Hanwha Ocean	042660 KS	Hold	23,700	35,300	3,963	na	23.4	13.2	na	1.57	1.47	-8.0%	0.0%
Sejin Heavy Industries Co Ltd	075580 KS	NR	4,415	na	190	na	na	na	na	na	na	na	na
Korean Shipbuilder simple average						61.4	18.2	11.2	na	1.34	1.25	-0.9%	0.0%
Mitsui E&S Co Ltd	7003 JP	NR	490.0	na	322	2.8	2.6	na	68.0%	0.44	0.40	na	0.2%
Japan Shipbuilder simple average						4.3	2.6	na	68.0%	0.44	0.40	na	0.2%
Brookfield Corp	BN US	NR	32.20	na	52,837	14.2	12.9	8.6	43.2%	1.19	1.18	9.6%	0.9%
US Shipbuilder simple average						14.2	12.9	8.6	43.2%	1.19	1.18	9.6%	0.9%
CSE Global	CSE SP	Add	0.44	0.57	197	12.0	9.2	7.9	83.1%	1.24	1.17	10.5%	6.3%
SATS Ltd	SATS SP	Hold	2.56	2.86	2,809	414.1	61.5	26.3	na	1.78	1.81	0.4%	0.2%
Sembcorp Industries	SCI SP	Add	5.05	6.85	6,616	9.1	9.9	9.8	12.0%	1.93	1.70	23.1%	3.0%
ST Engineering	STE SP	Add	3.76	4.27	8,623	20.3	16.8	14.4	23.8%	4.74	4.38	23.8%	4.3%
SIA Engineering	SIE SP	Hold	2.31	2.51	1,911	23.9	19.7	18.0	41.1%	1.51	1.48	6.5%	3.5%
Industrial/conglomerate / airport services simple average						95.9	23.4	15.3	40.0%	2.24	2.11	12.9%	3.5%

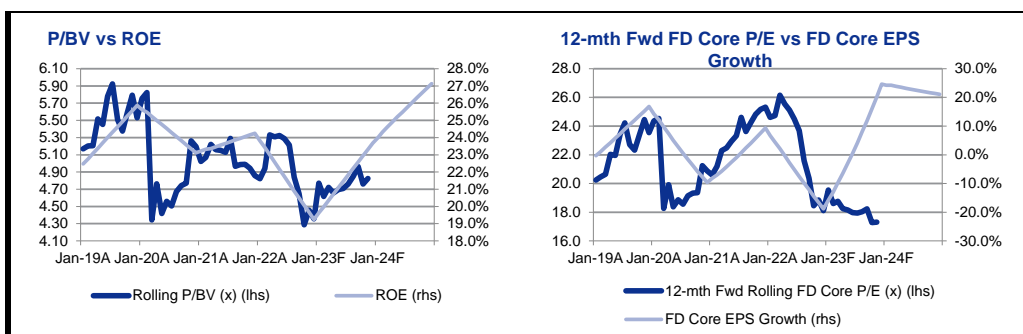
DATA AS AT 10 NOV 2023

SOURCES: CGS-CIMB RESEARCH ESTIMATES, COMPANY REPORTS, BLOOMBERG
Estimates for Not Rated (NR) companies are based on Bloomberg consensus

ESG in a nutshell		Refinitiv ESG Scores					
		B+ ESG Score	A+ ESG Controversies Score	B+ ESG Combined Score	A- ESG Environment Pillar Score	B ESG Social Pillar Score	B+ ESG Government Pillar Score
<p>We think STE's transformation over the years, steering its focus towards aerospace, smart city, defence and public security segments, has lifted its overall ESG standing away from the historical misconception of being associated with the production of anti-personnel landmines/cluster munitions. Accordingly, its ESG combined score by Refinitiv has improved from a B- since 2015 to B+ in 2022. The current score of B+ is split into E: A (weightage 23.7%); S: B (weightage 43.9%); and G: B+ (weightage 32.4%). Being a Temasek-linked company, STE plays a role in helping Singapore achieve its 2030 Green Plan, in our view.</p>							
<p>Keep your eye on</p> <p>As STE is involved in the defence industry, the transparency of its information could be limited at times in relation to contract wins/tender pipeline. Order book amount disclosed includes defence contracts, but details are not disclosed.</p>	<p>Implications</p> <p>We do not forecast our financials by commercial/defence in nature but based on historical trend of revenue and margin by segments. Significant wins/cancellations of defence contracts could be an upside/downside risk as STE announces its end order book.</p>						
<p>ESG highlights</p> <p>Refinitiv ranked STE slightly better than its Singapore industrial peer (KEP: B+) in 2022. STE scored particularly well in Environment (A), which we believe was due to its emission reduction target achievement. In 2020, its Singapore operations achieved a reduction of 44% in greenhouse gas (GHG) emission intensity, which surpassed its target of a 36% reduction on a business-as-usual basis by 2030F, with 2010 as base year. In 2021, the reduction continued with -30%, and -37% in 2022. Refinitiv ranked STE B+ for Governance in 2022, which we believe was due to the number of independent directors on its board (8, or 67%, of its 12 board directors were independent). We note that this was a decline from 75% in 2021.</p>	<p>Implications</p> <p>STE generally appears to fare well in corporate governance among Singapore corporates, with little controversy in recent years and can be valued at a premium by some investors. We believe that this ties in with our above-Singapore market P/E in our fundamental valuation of STE.</p>						
<p>Trends</p> <p>STE improved in the Environment pillar, based on Refinitiv rankings in 2022, with a score of A (vs. 2018's B+), which was attributed to better resource efficiency (less energy use/million revenue), and lower Co2 emissions. It also improved overtime in its Social pillar in 2022, with a score of B (vs. C+ in 2018), mainly due to the disclosure of its human rights policy — with zero tolerance for unethical labour practices such as child labour, forced labour, slavery and human trafficking in its operations; the group maintained its score in 2020-22.</p>	<p>Implications</p> <p>As STE ramps up its projects in smart cities, it could gain more interest from funds that focus on high E and S scores.</p>						

SOURCES: CGS-CIMB RESEARCH, REFINITIV

BY THE NUMBERS



Profit & Loss

(\$m)	Dec-21A	Dec-22A	Dec-23F	Dec-24F	Dec-25F
Total Net Revenues	7,693	9,035	9,822	10,487	11,157
Gross Profit	1,535	1,699	2,086	2,316	2,514
Operating EBITDA	1,044	1,181	1,295	1,432	1,537
Depreciation And Amortisation	(398)	(517)	(446)	(440)	(434)
Operating EBIT	646	665	849	993	1,103
Financial Income/(Expense)	(36)	(138)	(213)	(211)	(183)
Pretax Income/(Loss) from Assoc.	16	33	51	50	50
Non-Operating Income/(Expense)	12	37	(1)	0	0
Profit Before Tax (pre-EI)	638	597	686	831	970
Exceptional Items	0	0	0	0	0
Pre-tax Profit	638	597	686	831	970
Taxation	(71)	(54)	(103)	(125)	(146)
Exceptional Income - post-tax					
Profit After Tax	567	543	583	707	825
Minority Interests	4	(8)	(6)	(8)	(9)
Preferred Dividends					
FX Gain/(Loss) - post tax					
Other Adjustments - post-tax					
Net Profit	571	535	577	699	816
Recurring Net Profit	571	463	577	699	816
Fully Diluted Recurring Net Profit	571	463	577	699	816

Cash Flow

(\$m)	Dec-21A	Dec-22A	Dec-23F	Dec-24F	Dec-25F
EBITDA	1,044	1,181	1,295	1,432	1,537
Cash Flow from Inv. & Assoc.	(16)	(33)	(51)	(50)	(50)
Change In Working Capital	137	(442)	(53)	(55)	(157)
(Incr)/Decr in Total Provisions					
Other Non-Cash (Income)/Expense					
Other Operating Cashflow	105	216	275	275	247
Net Interest (Paid)/Received	(44)	(142)	(213)	(211)	(183)
Tax Paid	(112)	(108)	(103)	(125)	(146)
Cashflow From Operations	1,114	673	1,150	1,266	1,249
Capex	(312)	(763)	(200)	(200)	(200)
Disposals Of FAs/subsidiaries					
Acq. Of Subsidiaries/investments					
Other Investing Cashflow	(102)	(3,809)	(118)	(126)	(134)
Cash Flow From Investing	(414)	(4,571)	(318)	(326)	(334)
Debt Raised/(repaid)	54	4,575	(700)	0	0
Proceeds From Issue Of Shares	0	0	0	0	0
Shares Repurchased	(33)	(26)	0	0	0
Dividends Paid	(468)	(686)	(500)	(500)	(500)
Preferred Dividends					
Other Financing Cashflow	(168)	(165)	(225)	(225)	(197)
Cash Flow From Financing	(615)	3,698	(1,425)	(725)	(697)
Total Cash Generated	86	(201)	(592)	215	218
Free Cashflow To Equity	754	677	132	940	915
Free Cashflow To Firm	748	(3,750)	1,057	1,165	1,112

SOURCES: CGS-CIMB RESEARCH, COMPANY REPORTS

BY THE NUMBERS... cont'd

Balance Sheet

(\$m)	Dec-21A	Dec-22A	Dec-23F	Dec-24F	Dec-25F
Total Cash And Equivalents	816	602	9	225	443
Total Debtors	1,067	1,152	1,292	1,408	1,582
Inventories	1,261	1,684	1,759	1,858	1,965
Total Other Current Assets	2,213	2,689	2,701	2,711	2,721
Total Current Assets	5,356	6,127	5,761	6,202	6,711
Fixed Assets	1,794	2,076	2,069	2,062	2,056
Total Investments	519	545	595	645	695
Intangible Assets	1,993	5,291	5,171	5,064	4,970
Total Other Non-Current Assets	854	924	924	924	924
Total Non-current Assets	5,159	8,837	8,759	8,696	8,646
Short-term Debt	560	3,628	2,328	2,328	2,328
Current Portion of Long-Term Debt					
Total Creditors	2,613	2,826	2,967	3,112	3,221
Other Current Liabilities	1,507	1,551	1,583	1,609	1,634
Total Current Liabilities	4,680	8,005	6,879	7,048	7,183
Total Long-term Debt	1,555	2,907	3,507	3,507	3,507
Hybrid Debt - Debt Component					
Total Other Non-Current Liabilities	1,612	1,399	1,399	1,399	1,399
Total Non-current Liabilities	3,168	4,306	4,906	4,906	4,906
Total Provisions	0	0	0	0	0
Total Liabilities	7,847	12,311	11,785	11,954	12,089
Shareholders' Equity	2,413	2,398	2,475	2,674	2,991
Minority Interests	255	255	261	269	277
Total Equity	2,668	2,653	2,736	2,943	3,268

Key Ratios

	Dec-21A	Dec-22A	Dec-23F	Dec-24F	Dec-25F
Revenue Growth	7.5%	17.4%	8.7%	6.8%	6.4%
Operating EBITDA Growth	10.1%	13.2%	9.6%	10.6%	7.3%
Operating EBITDA Margin	13.6%	13.1%	13.2%	13.7%	13.8%
Net Cash Per Share (S\$)	(0.42)	(1.90)	(1.87)	(1.80)	(1.73)
BVPS (S\$)	0.77	0.77	0.79	0.86	0.96
Gross Interest Cover	13.53	4.47	3.77	4.41	5.60
Effective Tax Rate	11.1%	9.1%	15.0%	15.0%	15.0%
Net Dividend Payout Ratio	82.1%	93.4%	86.6%	71.5%	61.2%
Accounts Receivables Days	50.17	44.82	45.41	47.11	48.90
Inventory Days	74.99	73.27	81.23	81.01	80.73
Accounts Payables Days	143.2	135.3	136.7	136.1	133.7
ROIC (%)	11.6%	11.9%	7.6%	9.0%	10.1%
ROCE (%)	14.0%	9.7%	9.7%	11.6%	12.5%
Return On Average Assets	5.85%	5.25%	5.18%	6.03%	6.48%

Key Drivers

	Dec-21A	Dec-22A	Dec-23F	Dec-24F	Dec-25F
Commercial Aerospace sales (S\$m)	2,464.8	2,991.2	3,641.3	3,921.7	4,162.4
Urban Solutions & Satcom sales (S\$m)	1,190.5	1,772.2	1,898.9	2,077.2	2,289.9
Defence & Public Security sales (S\$m)	4,037.5	4,271.7	4,281.6	4,488.2	4,704.8

SOURCES: CGS-CIMB RESEARCH, COMPANY REPORTS

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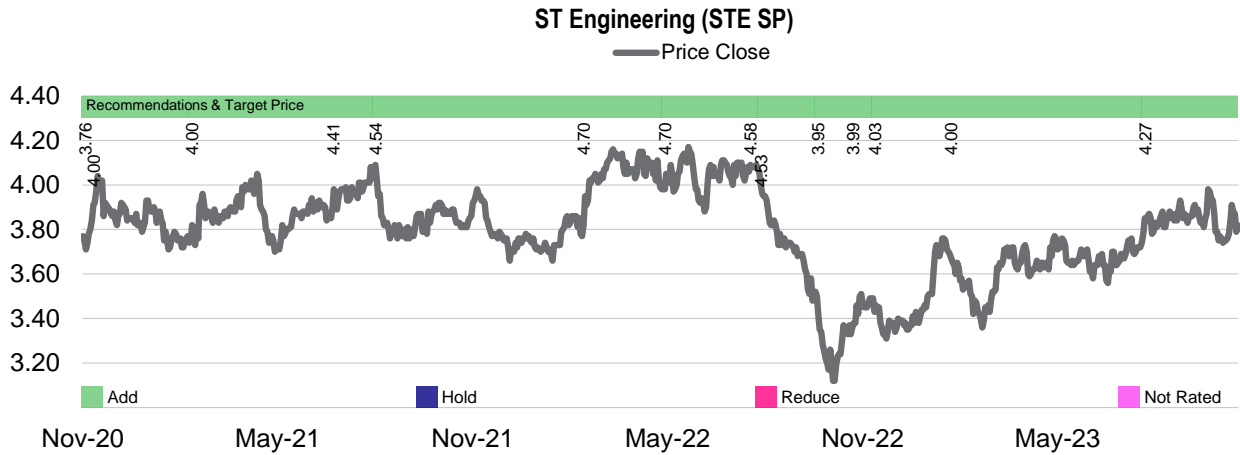
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Distribution of stock ratings and investment banking clients for quarter ended on 30 September 2023		
634 companies under coverage for quarter ended on 30 September 2023		
	Rating Distribution (%)	Investment Banking clients (%)
Add	66.7%	0.9%
Hold	23.7%	0.0%
Reduce	9.6%	0.2%

Spitzer Chart for stock being researched (2 year data)



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