

## NEW ECONOMY CONFERENCE HIGHLIGHTS

### VSTECs (VSTECs MK)

New Data Centre Initiatives Set To Supercharge VSTECs' Growth

We expect a stronger 2H24, boosted by higher contributions from VMware, along with new revenue from Google Pixel and AWS cloud services, as well as shipments of AI related DC equipment. The stock will also benefit from Budget 2025, which allocates significant funds to promote digitalisation in Malaysia. A key inflection point may occur with the government's rollout of new DC incentives, which could potentially supercharge VSTECs' growth by unlocking its TAM. Maintain BUY. Target price: RM5.02.

#### WHAT'S NEW

- Expect a stronger 2H24.** Recall that VSTECs reported a core net profit of RM29.4m (-4% yoy), accounting for only 40% of our full-year estimate due to the slower rollout of public sector projects in 1H24. Despite this, there was notable growth in the ICT distribution segment (+19% yoy) in 1H24, driven by the strong uptake of Starlink (thousands of units monthly) and a resurgence in PC demand indicating the start of the replacement cycle for devices bought during the pandemic. We expect earnings to catch up in 2H24, supported by: a) the rollout of Google Pixel in Aug 24, with thousands of units delivered since Sep 24, b) new AWS cloud service contributions following its data centre (DC) launch in Aug 24, c) increased contribution from VMWARE under a new agreement (doubling effect), d) shipments of AI-related DC equipment in 3Q24, e) steady adoption of Starlink with the potential rollout of Starlink Mini in 4Q24, and f) seasonally stronger consumer and enterprise spending in 2H24.
- New DC incentives: A strategic inflection point.** The Malaysian government is currently restructuring its incentive packages for DC investments to prioritise high-value activities that bring broader economic benefits. Treasury Secretary General Datuk Johan Mahmood Merican highlighted concerns that while DCs involve significant capex, they often do not create enough high-skilled jobs and can strain electricity and water resources. To address this, the government will introduce a new investment incentive framework by mid-25, using a "scorecard" approach to assess projects based on factors like job creation, local business linkages, sustainability, and alignment with strategic economic sectors. These incentives will be backed by a RM1b strategic fund designed to cultivate local talent and promote high-value activities in the E&E and AI sectors, ensuring long-term economic benefits. We believe this could be an inflection point for VSTECs, as it will further accelerate its DC equipment and GPU server deals by multiple folds, growing from the current tens of millions of ringgit.
- Beneficiary of Budget 2025.** While details remain sketchy, VSTECs stands to benefit significantly from Budget 2025, which allocates substantial funds from both the Ministry of Education (MoE) and the Ministry of Digital to enhance digitalisation and internet coverage across Malaysia. The MoE's record allocation of RM64.1b includes RM635m for infrastructure upgrades and expanded internet access in public universities, as well as RM270m for improving internet coverage in higher education institutes, rural schools, and AI education initiatives. Meanwhile, the Ministry of Digital is set to receive RM1.3b to promote the digital economy, alongside capital allowances for e-invoicing implementation that encompass ICT equipment and software purchases.

#### KEY FINANCIALS

Year to 31 Dec (RMm)	2022	2023	2024F	2025F	2026F
Net turnover	2,770.6	2,727.2	3,035.6	3,413.8	3,868.3
EBITDA	79.5	82.7	89.0	111.8	135.9
Operating profit	76.6	79.6	92.2	113.4	136.9
Net profit (rep./act.)	59.7	67.4	72.9	89.5	107.9
Net profit (adj.)	59.4	62.0	72.9	89.5	107.9
EPS (sen)	16.7	17.4	20.4	25.1	30.3
PE (x)	19.3	18.5	15.8	12.8	10.6
P/B (x)	2.8	2.5	2.3	2.1	1.9
EV/EBITDA (x)	14.0	12.5	11.6	9.0	7.3
Dividend yield (%)	1.9	2.0	2.2	3.9	3.3
Net margin (%)	2.1	2.3	2.4	2.6	2.8
Net debt/(cash) to equity (%)	(8.1)	(25.7)	(23.1)	(25.2)	(25.4)
Interest cover (x)	151.4	62.7	72.6	89.4	107.8
ROE (%)	14.5	14.8	14.5	16.3	17.4

Source: VSTECs, Bloomberg, UOB Kay Hian

## BUY

(Maintained)

Share Price	RM3.22
Target Price	RM5.02
Upside	+55.9%

#### COMPANY DESCRIPTION

VSTECs is the leading distributor of ICT products to consumers and enterprises in Malaysia. Founded in 1985, the Group distributes a wide range of ICT products to both consumer and enterprise and provides IT services in the form of pre-sales, integration, and post-sales in support of the brands represented. The three business segments are ICT Distribution, Enterprise Systems, and ICT Services.

#### STOCK DATA

GICS sector	ICT Distributor
Bloomberg ticker:	VST MK
Shares issued (m):	356.6
Market cap (RMm):	1,148.1
Market cap (US\$m):	262.1
3-mth avg daily t'over (US\$m):	1.4

#### Price Performance (%)

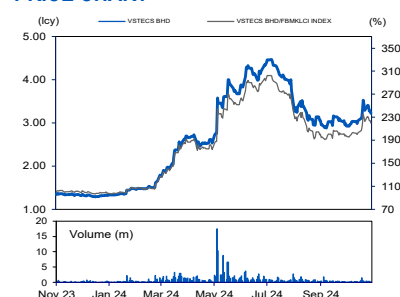
52-week high/low	RM1.28/RM4.52			
<b>1mth</b>	<b>3mth</b>	<b>6mth</b>	<b>1yr</b>	<b>YTD</b>
5.6	(19.5)	22.9	145.8	143.9

#### Major Shareholders

VSTECs Holding Ltd	45.6
Sengin Sdn Bhd	12.2
Dasar Technologies Sdn Bhd	8.6

FY24 NAV/Share (RM)	1.
FY24 Net Cash/Share (RM)	0.42

#### PRICE CHART



Source: Bloomberg

#### ANALYST(S)

**Ku Wei Xiang**  
+603 2147 1916  
weixiang@uobkayhian.com

**Desmond Chong**  
+603 2147 1980  
desmondchong@uobkayhian.com

### STOCK IMPACT

- Margin and market share expansion through new distributorship agreement with VMWARE.** Under the new agreement, VSTECS will now have a 100% market share for the distribution of VMWARE solutions in Malaysia (from the previous 50%) with improved margins from service components. Additionally, VSTECS will expand its role to provide technical support capabilities for selected products and customers. We gathered that 20-30% of the VMWARE solution distribution will potentially translate to post-sales ICT services, which typically have better margins. With these factors in play, management expects the contribution from VMWARE to grow by multiple legs, despite having to incur talent acquisition cost from absorbing service personnel. Note that VMware holds a market share of about 80% in server virtualisation, which has been instrumental in charting VSTECS's growth as a distributor.
- Potential order from colocation DCs for IT equipment.** This order has yet to be reflected in our valuation. Unlike hyperscale DCs that procure their IT equipment directly, VSTECS targets the colocation DCs market, which typically secures its IT equipment from VSTECS. IT equipment encompasses networking, storage, and servers. According to C\_TEC and the US Chamber of Commerce, approximately 73% of initial DC capex is attributed to IT equipment. Based on our channel checks, the estimated cost of IT equipment per megawatt (MW) is RM40m-50m. With 200MW of colocation DCs currently under construction, this presents a total addressable market (TAM) of around RM10b. It is worth noting that VSTECS holds a market share of 50% in the enterprise systems distribution in Malaysia, indicating a significant opportunity in this blue-ocean market segment. Note that the majority of colocation DCs in Malaysia are still in the construction and mechanical and electrical (M&E) phase. VSTECS has already engaged in this phase by providing UPS systems and smart cooling systems. Typically, this phase takes 1-2 years to complete before transitioning to the installation of IT equipment.

### EARNINGS REVISION/RISK

- Earnings revision: None.**
- Forecasting a three-year revenue/core net profit CAGR of 12%/20%,** on the back of assuming: a) growth of the ICT distribution segment is driven by the resurgence of the PC and notebook cycle and strong Starlink adoption in Malaysia, b) growth of the enterprise services segment is mainly fuelled by the booming DC market in Malaysia, and c) increased ICT services revenue, which commands higher margins, thereby lifting the group's overall margin. Note that we have not yet accounted for any potential orders from colocation DCs for IT equipment.

### VALUATION/RECOMMENDATION

- Maintain BUY with an unchanged target price of RM5.02,** based on 20.0x 2025F PE. Given the lack of local listed peers for valuation benchmarking, we use a 1.0x PEG ratio (compared with 2.0x PEG ratio which was the average peak PEG valuation of tech names during the 2021 tech run), reflecting a three-year net profit CAGR of 20% from 2023. The booming DC industry in Malaysia, reminiscent of the tech bull cycle in 2021, supports this valuation.

### ENVIRONMENTAL, SOCIAL, GOVERNANCE (ESG) UPDATES

<ul style="list-style-type: none"> <li> <b>Environmental</b> <ul style="list-style-type: none"> <li>- Electricity withdrawal from main grid reduced by 20% yoy in 2023.</li> <li>- Solar power constituted 41% of total electricity consumed in 2023.</li> <li>- 26% reduction in paper consumption.</li> </ul> </li> <li> <b>Social</b> <ul style="list-style-type: none"> <li>- Maintaining a 50% male-female composition among total employees.</li> <li>- The group recorded zero work fatalities over the past nine years.</li> <li>- 100% local employees.</li> </ul> </li> <li> <b>Governance</b> <ul style="list-style-type: none"> <li>- Zero confirmed corruption or harassments cases reported.</li> <li>- Zero fines or penalties from regulatory authorities.</li> <li>- 57% of directors are independent.</li> </ul> </li> </ul>
--

### KEY PRINCIPAL RELATIONSHIPS



Source: VSTECS

### INDUSTRIES SERVED AND JOB SCOPE

INDUSTRIES	%	SCOPE
Financial Services	22%	Cloud, Enterprise Software, Cybersecurity
Telco	20%	Telco Equipment, DC & Network Infra
Public sector	18%	DC, Network, Infra & Cybersecurity
Education	12%	Client Computing
Energy	10%	Enterprise Software, Client Computing
Healthcare	8%	DC, hyperconverged computing
Transportation	5%	DC & Network Infra & Cybersecurity
Others	5%	Various

Source: VSTECS

### VSTECS' DC PRODUCTS AND SOLUTIONS

<b>NETWORKING</b> <ul style="list-style-type: none"> <li>Highly scalable up to 400G</li> <li>AI / Machine learning ready</li> <li>Leaders in DC, networking</li> <li>Fast deployment and simple O&amp;M</li> </ul>	
<b>CYBER SECURITY</b> <ul style="list-style-type: none"> <li>Next generation firewall</li> <li>Multi-layered segmentation</li> <li>Full layer 7 protection against malware</li> <li>Leaders in magic quadrant for firewalls</li> </ul>	
<b>SERVERS</b> <ul style="list-style-type: none"> <li>Nvidia certified GPU servers</li> <li>Accelerated computing, energy efficiency</li> <li>Direct water-cooling server</li> </ul>	
<b>STORAGE</b> <ul style="list-style-type: none"> <li>Full flash/hybrid mode available</li> <li>High service, fault tolerant</li> <li>Integration with backup software</li> </ul>	
<b>SOFTWARE</b> <ul style="list-style-type: none"> <li>Virtualisation, resource optimisation</li> <li>High availability, disaster recovery</li> <li>Cloud integration, next gen AI</li> </ul>	
<b>ENERGY</b> <ul style="list-style-type: none"> <li>Modular data centre systems</li> <li>Digital control lithium power UPS</li> <li>Smart cooling system</li> </ul>	

Source: VSTECS

### PROFIT & LOSS

Year to 31 Dec (RMm)	2023	2024F	2025F	2026F
<b>Net turnover</b>	2,727.2	3,035.6	3,413.8	3,868.3
EBITDA	82.7	89.0	111.8	135.9
Deprec. & amort.	(3.1)	(3.1)	(1.6)	(1.0)
EBIT	79.6	92.2	113.4	136.9
Associate contributions				
Net interest income/(expense)	(1.3)	(1.3)	(1.3)	(1.3)
<b>Pre-tax profit</b>	82.8	95.9	117.8	142.0
Tax	(15.4)	(23.0)	(28.3)	(34.1)
Minorities	0.0	0.0	0.0	0.0
<b>Net profit</b>	67.4	72.9	89.5	107.9
Net profit (adj.)	62.0	72.9	89.5	107.9

### BALANCE SHEET

Year to 31 Dec (RMm)	2023	2024F	2025F	2026F
Fixed assets	3.7	1.6	1.0	1.0
Other LT assets	57.1	57.1	57.1	57.1
Cash/ST investment	150.9	149.9	171.4	190.7
Other current assets	600.3	673.4	760.2	865.9
<b>Total assets</b>	812.0	882.0	989.7	1,114.6
ST debt	2.5	1.7	1.7	1.7
Other current liabilities	315.6	331.5	389.0	437.5
LT debt	0.0	0.0	0.0	0.0
Other LT liabilities	4.1	9.1	14.6	20.9
Shareholders' equity	456.4	503.8	548.6	618.7
Minority interest	0.0	0.0	0.0	0.0
<b>Total liabilities &amp; equity</b>	812.0	882.0	989.7	1,114.6

### CASH FLOW

Year to 31 Dec (RMm)	2023	2024F	2025F	2026F
<b>Operating</b>	107.6	25.6	67.4	58.1
Pre-tax profit	82.8	95.9	117.8	142.0
Tax	(22.8)	(23.0)	(28.3)	(34.1)
Deprec. & amort.	1.7	3.1	1.6	1.0
Working capital changes	49.4	(55.4)	(29.3)	(57.2)
Other operating cashflows	(1.8)	8.1	7.2	7.4
<b>Investing</b>	0.3	(1.0)	(1.0)	(1.0)
Capex (maintenance)	(3.0)	(1.0)	(1.0)	(1.0)
Investments	0.0	0.0	0.0	0.0
Proceeds from sale of assets	0.1	0.0	0.0	0.0
Others	3.1	0.0	0.0	0.0
<b>Financing</b>	(3.6)	(25.6)	(44.8)	(37.8)
Dividend payments	(22.1)	(25.5)	(44.8)	(37.8)
Issue of shares	0.0	0.0	0.0	0.0
Proceeds from borrowings	(0.8)	(1.3)	(1.3)	(1.3)
Loan repayment	0.0	0.0	0.0	0.0
Others/interest paid	0.6	(0.1)	(0.1)	(0.1)
<b>Net cash inflow (outflow)</b>	104.3	(1.0)	21.6	19.2
<b>Beginning cash &amp; cash equivalent</b>	46.6	150.9	149.9	171.4
Changes due to forex impact	0.0	0.0	0.0	0.0
<b>Ending cash &amp; cash equivalent</b>	150.9	149.9	171.4	190.7

### KEY METRICS

Year to 31 Dec (%)	2023	2024F	2025F	2026F
<b>Profitability</b>				
EBITDA margin	3.0	2.9	3.3	3.5
Pre-tax margin	3.0	3.2	3.4	3.7
Net margin	2.3	2.4	2.6	2.8
ROA	8.3	8.3	9.0	9.7
ROE	14.8	14.5	16.3	17.4
<b>Growth</b>				
Turnover	(1.6)	11.3	12.5	13.3
EBITDA	4.0	7.6	25.6	21.5
Pre-tax profit	3.4	15.8	22.8	20.5
Net profit	13.0	8.1	22.8	20.5
Net profit (adj.)	4.5	17.5	22.8	20.5
EPS	4.5	17.5	22.8	20.5
<b>Leverage</b>				
Debt to total capital	0.3	3.8	3.4	3.0
Debt to equity	0.0	6.6	6.1	5.4
Net debt/(cash) to equity	(25.7)	(23.1)	(25.2)	(25.4)
Interest cover (x)	62.7	72.6	89.4	107.8