

27 December 2019

Technology | Electronic Equipment, Instrument

VSTECS (VST MK)

Not Rated

Prospective Growth Across The Board

Fair Value	MYR1.78
Price:	MYR1.48
Market Cap:	USD64.1m
Avg Daily Turnover (MYR/USD)	1.02m/0.25m

- **FV of MYR1.78 implying 10x FY20F P/E, +2SD from 5-year forward mean** – is justified, premised on 14% FY18-20F earnings CAGR, established wide network with diverse customer base, widening of ICT distribution coverage, timely launches by adapting to changing consumer preference, rising adoption of digitalisation that should lift demand for ICT products and services. Our valuation is lower than average regional peers P/E of 17x, given the smaller market cap.
- **One-stop shop ICT supplier with established network.** As an information and communications technology (ICT) supplier, VSTECS has a long track record with >40 leading ICT principals and extensive network of >6,600 resellers. FY18 revenue is mainly from ICT distribution segment (70%), whereby notebooks, personal computers (PCs) and smartphones etc are distributed to resellers. Enterprise systems segment (28%), whereby server, storage and software are distributed mainly to system integrators and corporate dealers. The remaining 2% is ICT services – networking infrastructure and cybersecurity services.
- **Beef up on ICT distribution coverage.** VSTECS has nationwide distribution network to distribute global ICT brands. Since 2017, it has also expanded into virtual reality and drone products. In 2019, it started to distribute laptops by global gaming leading brand, Micro-Star International Co Ltd (MSI), to help increase market share in e-sports and consumer electronics. It also focusing on the e-commerce sector by growing business-to-business (B2B) platform and manage principals' business-to-commerce (B2C) brand stores via partnership with local e-commerce marketplaces, ie Lazada, Shopee and PrestoMall. Online contribution is c.10% of sales, and we believe it could grow.
- **Increasing focus on IoT, big data analytics and security open up opportunity for enterprise systems and ICT services.** By riding on changing consumer trend towards the Internet of Things (IoT) market, VSTECS is in partnership with Rubrik Inc and Hortonworks Inc to tap into cloud data management and big data analytics to launch new products in enterprise systems segment. Also, Nasdaq-listed Splunk Inc, specialising in software and solutions for big data analytics, has appointed VSTECS as its official distributor. In FY18, enterprise systems and ICT services rose 19% and 11% YoY. VSTECS has also tapped into digital transformation and mobile solution business through its 40% associate, I.S.A. Technologies SB. We believe the timely reaction to market preference could help in customer retention and secure new customers.
- **External measures to drive adoption of digitalisation could spur demand.** The Government has allocated MYR3bn (Budget 2019) and MYR2bn (Budget 2020) for the Industry Digitalisation Transformation Fund to accelerate the adoption of smart technology such as driving automation, robotics and artificial intelligence. We believe this could help stimulate demand for ICT products and services. There is a potential increase in demand in preparation for the implementation of 5G services nationwide, in our view, as ICT devices and enterprise infrastructure have to be upgraded in order to be compatible.
- **Consistent dividend payout.** Save for FY15 when a special dividend was declared in conjunction with its 30th anniversary, it has declared c.33-37% of PAT as dividends in the last five years. Assuming FY19F-20F dividend payout ratio at 35%, we expect FY19F-20F DPS of 5.6-6.2 sen, or 4% yield. We believe there is room for a higher payout, given its net cash position with no debts.
- **Risks:** Prolonged weakening of global demand, obsolescence of technology devices, and discontinuation of distributorship.

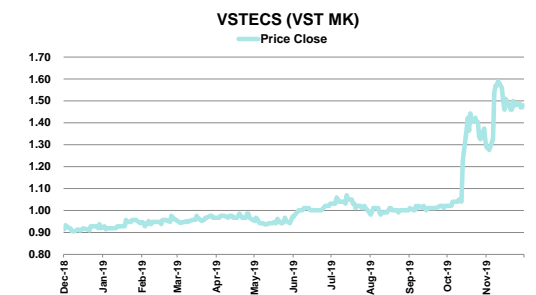
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Share Performance (%)

	YTD	1m	3m	6m	12m
Absolute	54.2	10.4	45.1	49.5	59.1
Relative	59.3	9.7	44.2	53.9	63.9
52-wk Price low/high (MYR)	0.93 – 1.67				



Source: Bloomberg

Forecasts and Valuation	Dec-16	Dec-17	Dec-18	Dec-19F	Dec-20F
Total turnover (MYRm)	1,823.4	1,838.3	1,632.3	1,698.2	1,789.1
Recurring net profit (MYRm)	30.1	26.3	24.6	28.4	31.9
Recurring net profit growth (%)	(7.2)	(12.9)	(6.3)	15.6	12.2
Recurring P/E (x)	8.4	8.4	7.0	9.3	8.3
P/BV (x)	1.0	0.8	0.6	0.9	0.8
P/CF (x)	65.6	(6.9)	15.3	8.8	7.9
Dividend Yield (%)	4.3	4.1	5.1	3.8	4.2
EV/EBITDA (x)	3.5	4.9	3.8	6.2	5.4
ROE (%)	12.2	9.9	8.8	9.6	10.1
Net debt to equity (%)	(43.0)	(18.5)	(18.9)	(11.4)	(12.9)
Interest coverage (x)	49.9	na	>100	na	na

Source: Company data, RHB

Figure 1: Brands that carried by VSTECs Astar, for distributorship of notebooks, PCs, tablet and smartphones etc



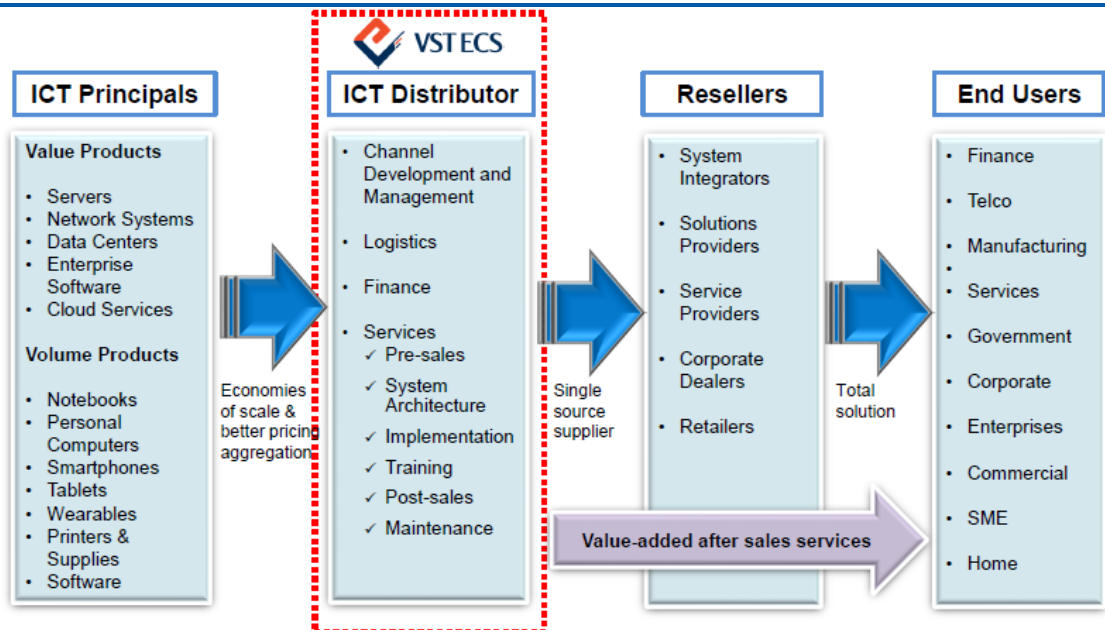
Source: Company data

Figure 2: Major IT brand that partners with VSTECs Pericom, the distributor of enterprise systems and services



Source: Company data

Figure 3: VSTECs' business model



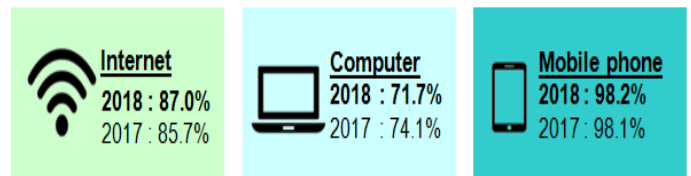
Source: Company data

Figure 4: ICT use by individuals in Malaysia



Source: ICT Use and Access by Individuals and Household Survey, Department of Statistics Malaysia, 2018

Figure 5: ICT access by households in Malaysia



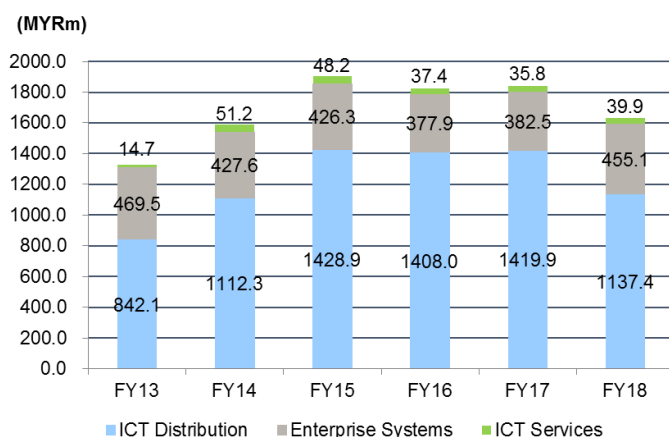
Source: ICT Use and Access by Individuals and Household Survey, Department of Statistics Malaysia, 2018

Figure 6: Overall higher YoY for internet use activities



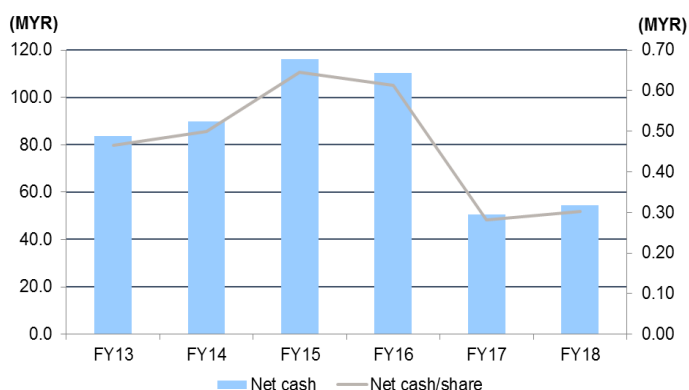
Source: ICT Use and Access by Individuals and Household Survey, Department of Statistics Malaysia, 2018

Figure 7: Revenue by segment



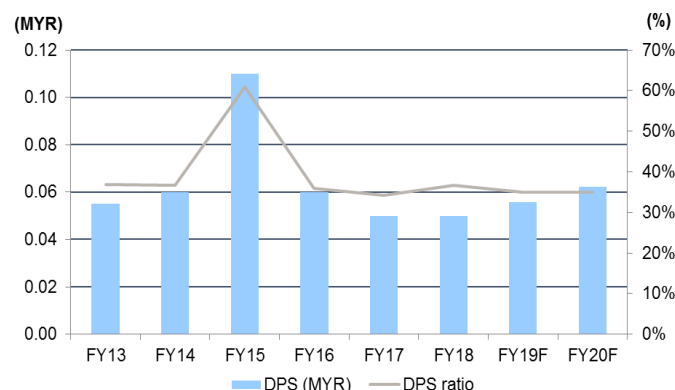
Source: Company data, RHB

Figure 8: Historical net cash



Source: Company data, RHB

Figure 9: Historical and forecasted dividends



Source: Company data, RHB

Figure 10: Peer comparison

Company	FYE	Country	Price	Mkt Cap (USDm)	P/E (x)		Div. Yld (%)	ROE (%)		NP Growth (%)	
			26-Dec-19 (Local Currency)		1 Yr Fwd	2 Yr Fwd	1 Yr Fwd	1 Yr Fwd	1 Yr Fwd	2 Yr Fwd	
International											
Zensar Technologies Ltd^	Mar	IN	171.40	542	11.4	9.5	1.7	16.3	5.8	20.1	
Hand Enterprise Solutions-A	Dec	CH	9.95	1,256	19.5	15.9	0.5	13.0	10.0	22.5	
NS Solutions Corp^	Mar	JN	3650.00	3,155	17.3	16.6	1.8	13.1	18.1	4.4	
Silverlake Axis Ltd^	Jun	SI	0.41	788	15.7	14.8	5.0	33.1	(15.4)	6.1	
TIS INC^	Mar	JN	6500.00	5,209	19.5	18.3	1.3	12.3	13.5	6.7	
Insyde Software Corp	Dec	TA	67.20	85	30.1	27.2	3.0	12.6	28.4	10.5	
Weighted Average					18.3	16.9	1.6	14.3			
Local											
VSTECs	Dec	MY	1.48	64	9.3	8.3	3.8	9.6	15.6	12.2	

Note: ^FY19-20 valuations refer to those of FY20-21

Source: Bloomberg, RHB

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