

Silverlake Axis Ltd

Higher OPEX hurt earnings



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SINGAPORE | BANKING | 3QFY23 RESULTS

18 May 2023

- 3QFY23 earnings of RM34.2mn were below our estimates. 9MFY23 earnings were at 64% of our FY23e. The 15% YoY dip in earnings came from higher-than-expected OPEX due to the current inflationary environment and a need to increase staff costs.
- Project-related revenue comprising software licensing and software project services fell 27% YoY. Silverlake recently signed their first multi-million 10-year core and channels digital banking MOBIUS deal with a client in Malaysia, total size of more than RM100mn of which RM30-40mn will be booked in the first year.
- We maintain BUY with an unchanged target price of S\$0.49. We lower FY23e earnings by 7% as we increase operating expenses estimates for FY23e. Our target price is pegged to 21x P/E FY23e. We expect MOBIUS and the recovery in bank IT spending after two cautious pandemic years to be the key growth drivers for the company.

Results at a glance

(RM '000)	3QFY23	3QFY22	YoY	Comments
Software licensing	7,271	20,634	-65%	Decline as the progression of actual project delivery varies from quarter to quarter.
Software project services	25,518	24,061	6%	Increase due to additional revenue recognised from recently closed contracts from countries such as Thailand, UAE, Malaysia and Brunei.
Sale of software and hardware products	1,429	646	121%	Increase due to customers investing into hardware upgrades to enhance their technology infrastructure, with two major hardware deals closed in 9MFY23.
Maintenance and enhancement services	123,528	115,413	7%	Slight uptick due to additional contributions from new maintenance contracts that have become operational.
Insurance ecosystem transactions and services	12,630	10,686	18%	Broad based growth from vehicle claims processing, insurance policies processing, productivity & analytics solution, and integration services segments.
Retail transactions processing	932	460	102%	Higher subscriptions for Silverlake's cloud-based retail solution, AgoraCloud, from both retail and pharmaceutical customers in Malaysia and Singapore.
Total Revenue	171,307	171,901	0%	
Cost of sales	-66,873	-72,944	-8%	
Gross profit	104,434	98,957	6%	Gross profit margin remained consistent at 59% for both periods.
OPEX	-60,995	-53,522	14%	Higher OPEX expected due to the current inflationary environment, with increases seen in staff costs, finance costs and foreign currency exchange loss. Expense over revenue ratio at 30%.
PATMI	34,214	40,025	-15%	

Source: Company, PSR

The Positives

+ Recurring revenue rose 8% YoY. Recurring revenue comprises maintenance and enhancement services, insurance ecosystem transactions and services, and retail transactions processing revenue. Maintenance and enhancement services increased 7% YoY to RM124mn as the dip in enhancement services revenue was more than offset by the increase in maintenance revenue. The decline in enhancement services revenue was mainly due to the timing and progress of contracts fulfilment and delivery, and Silverlake anticipates this will be recognised and booked in the following quarter. Insurance ecosystem transactions and services revenue increased 18% YoY as there was broad-based growth

BUY (Maintained)

CLOSING PRICE	SGD 0.33
FORECAST DIV	SGD 0.01
TARGET PRICE	SGD 0.49
TOTAL RETURN	49.0%

COMPANY DATA

Bloomberg CODE:	SILVSP
O/S SHARES (MN):	2,511.8
MARKET CAP (USD mn / SGD mn):	627 / 841
52 - WK HI/LO (SGD):	0.44 / 0.26
3M Average Daily T/O (mn):	0.45

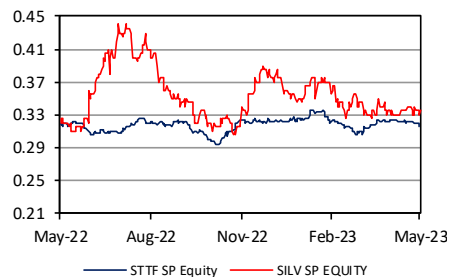
MAJOR SHAREHOLDERS

Peng Ooi Goh	68.0%
NTAsset (Thailand) Co., Ltd.	2.7%

PRICE PERFORMANCE (%)

	1MTH	3MTH	1YR
COMPANY	(1.5)	(8.3)	5.4
STTF RETURN	(1.1)	(1.1)	4.6

PRICE VS. STTF



Source: Bloomberg, PSR

KEY FINANCIALS

Y/E Jun, RM (mn)	FY21	FY22	FY23e	FY24e
Revenue	626.1	736.5	795.5	859.1
EBITDA	146.4	210.2	223.1	256.7
Net Profit	143.1	182.2	194.5	226.3
EPS (SGD cents)	1.8	2.2	2.3	2.7
P/E (X)	18.8	15.4	14.7	12.6
Dividend Yield	1.6%	2.1%	3.0%	3.0%
ROE	13.6%	18.7%	17.0%	16.9%
ROA	10.5%	12.2%	12.7%	13.8%

Source: Company, PSR

VALUATION METHOD

21x PE Multiple FY23e

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across all segments, from vehicle claims processing, insurance policies processing, productivity and analytics solutions, and integration services. Revenue from retail transactions processing surged 102% YoY mainly due to higher subscriptions for Silverlake's cloud-based retail solution, AgoraCloud, from both retail and pharmaceutical customers in Malaysia and Singapore.

+ Order backlog healthy. Silverlake has a long track record and a proven client base in Southeast Asia. Three of the 5 largest Southeast Asia-based financial institutions use its core banking platform, and it has largely retained all its clients since bringing them on board its platform. Silverlake's project pipeline is healthy, at RM1.8bn (2QFY23: RM1.8bn), with a record contract wins of RM259mn in 3QFY23 and an order backlog of RM261mn on the verge of closing in 4QFY23. Furthermore, Silverlake has recently secured their first multi-million 10-year core and channels digital banking MOBIUS deal with a client in Malaysia. Silverlake is beginning to close more deals and is witnessing an uptick in inquiries about its financial services market solutions and capabilities.

The Negatives

- OPEX rose 14% YoY. Operating expenses were 14% higher YoY mainly due to the current inflationary environment and a need to support long-term growth and sustainability. The increase was across all segments, with increases in staff costs due to additional headcount, increase in finance costs due to a revolving credit facility drawdown, increase in foreign currency exchange losses due to the fluctuation of foreign currencies, and higher costs for internal and external branding activities as markets opened up. Nonetheless, the expense over revenue ratio was kept at 30%.

- Project-related revenue fell 27% YoY. Software licensing revenue fell 65% YoY to RM7mn. This was mainly due to the progression of actual project delivery varying from quarter to quarter, resulting in a lag in revenue contribution. However, this was offset by software project services revenue increasing 6% YoY to RM26mn as there was additional revenue recognised from recently closed contracts from countries such as Thailand, UAE, and Malaysia. In addition, progressive project revenue recognised from on-going secured projects remained at a stable level.

Outlook

MOBIUS banking platform is the differentiator. Launched in 2020, Silverlake's MOBIUS cloud banking software allows banks to roll out new digital products in a targeted and timely manner. MOBIUS also allows banks to use existing core banking software and propel them to new digital products. Potential uses of MOBIUS include new digital products in credit cards, debit cards, personal loans and deposits. Cloud-based software avoids the need for banks to purchase and manage hardware assets. Silverlake recently signed a deal with one of the largest banks in Thailand and their first multi-million 10-year core and channels digital banking MOBIUS deal with a client in Malaysia. We expect MOBIUS to generate almost RM100mn of orders over the next two years. With the collaboration with the Thailand bank, they have shown the shown the proof of concept and have a significant reference site for MOBIUS and we could see more inquiries for the rest of 2023. There is also a potential for replacing core banking systems with MOBIUS as several legacy core banking systems approach end-of-life, and banks have fewer limitations to adopt a fully cloud based core.

"Annuity" type revenue. Silverlake's recurring maintenance and enhancement revenue contributed to more than 70%/80% of FY22/3QFY23 revenue, and it grew at a CAGR of 4% despite the COVID-19 pandemic. Silverlake's core banking software (Silverlake Integrated Banking Solution or SIBS) and continuous maintenance and enhancement provide a steady stream of recurring business for the group. SIBS provides core accounting and compliance. With the opening of borders and economies in ASEAN, we can expect Silverlake's customers to increase their IT spending to accelerate their digitalization plans to grow.

Investment Actions

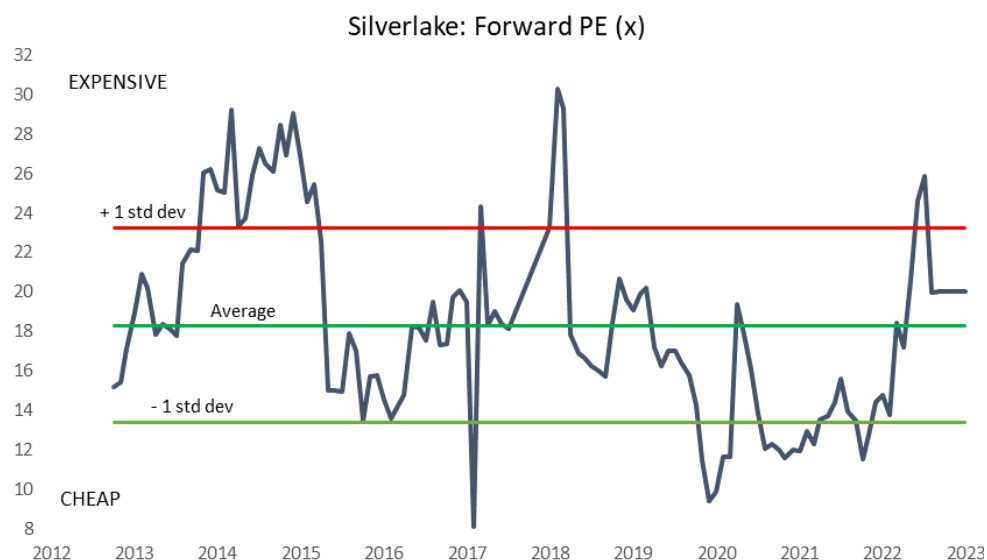
We maintain a BUY rating on Silverlake Axis Ltd with an unchanged target price of S\$0.49. We lower FY23e earnings by 7% as we increase operating expenses estimates for FY23e. Our target price is pegged to 21x P/E FY23e. It is at 13% discount to peer valuations of around 24x PE (Figure 1).

Our target PE of 21x is 15% higher than the historical average PE of 18.3x (Figure 2). In our view, Silverlake should trade at a higher premium to its historical PE with the introduction of MOBIUS and the resumption of bank IT spending after the pandemic.

Figure 1: Global players trading at 24.3x PE – 1 year forward

Company	1 Mth	3 Mth	YTD	Share Px	Mkt. Cap.	PE			P/BV	Dividend	ROE	EV/
	Perf.	Perf.	Perf.	Local Crcy	(US\$ m)	Yr 0	Yr+1	Yr+2	Yr 0	Yield	Yr 0	EBITDA
Core Banking Systems												
Tata Consultancy	4%	20%	2%	2206.80	98,069	19.2	17.0	15.3	8.7	5.2%	46.4%	17.3
Temenos AG	1%	18%	-7%	143.05	11,968	104.6	55.1	50.2	18.2	0.8%	21.0%	19.2
SBM Offshore	1%	29%	-19%	13.37	2,222	4.9	12.4	8.1	0.7	0.0%	15.1%	11.2
Silverlake Axis Ltd	17%	17%	-32%	0.28	524	13.0	12.8	11.8	0.8	7.9%	17.7%	8.8
	6%	21%	-14%		112,784	35.4	24.3	21.3	7.1	3.5%	25.1%	14.1

Source: PSR, Bloomberg

Figure 2: Silverlake's historical average PE is 18x


Source: PSR, Bloomberg

Financials

Income Statement

Y/E Jun, RM '000	FY20	FY21	FY22	FY23e	FY24e
Revenue	663,692	626,123	736,542	795,465	859,102
Gross profit	379,621	376,929	418,614	477,279	515,461
EBITDA	187,231	146,387	210,191	223,088	256,657
Depreciation & amortisation	3,889	3,291	3,762	5,560	7,310
EBIT	183,279	143,079	182,703	194,447	226,266
Net Finance Inc/(Exp)	(30,686)	(11,253)	280	(10,754)	(10,435)
Profit before tax	201,426	186,737	231,858	243,059	282,832
Taxation	(16,754)	(43,658)	(49,154)	(48,612)	(56,566)
Minority interest	3	8	(551)	10	(11)
PATMI	184,676	143,087	182,153	194,457	226,277

Per share data (SGD Cents)

Y/E Dec	FY20	FY21	FY22	FY23e	FY24e
EPS, Reported	2.3	1.8	2.2	2.3	2.7
DPS	0.9	0.5	0.7	1.0	1.0
BVPS	28.5	40.5	36.7	43.0	50.5

Cash Flow

Y/E Jun, RM '000	FY20	FY21	FY22	FY23e	FY24e
CFO					
Profit before tax	201,426	186,737	231,858	243,059	282,832
Adjustments	58,446	80,177	39,284	50,984	52,517
WC changes	10,358	(19,520)	48,254	(44,562)	(19,368)
Cash generated from ops	269,306	246,867	319,557	249,642	316,142
Income tax paid	(54,635)	(47,241)	(48,822)	(48,612)	(56,566)
Cashflow from ops	209,777	196,904	270,295	186,955	245,500
CFI					
Software development	(31,100)	(39,417)	(47,463)	(47,463)	(47,463)
Others	(5,648)	(43,551)	(35,677)	(45,677)	(45,677)
Cashflow from investments	(36,748)	(82,968)	(83,140)	(93,140)	(93,140)
CFE					
Purchase of treasury shares	(56,815)	(20,425)	(178,574)	(29,762)	(4,960)
Loans, net of repayments	90,712	(8,814)	164,355	(10,000)	(10,000)
Dividends paid	(104,814)	(25,840)	(42,944)	(26,600)	(26,600)
Others	(42,707)	(123,516)	(1,755)	(247)	-
Cashflow from financing	(113,624)	(178,596)	(58,918)	(66,609)	(41,807)
Net change in cash	59,404	(64,659)	128,237	27,206	110,552
CCE, end	476,424	407,341	548,935	581,845	697,277

Source: Company, Phillip Securities Research (Singapore) Estimates

Balance Sheet

Y/E Jun, RM '000	FY20	FY21	FY22	FY23e	FY24e
ASSETS					
Trade and other receivables	139,961	138,918	127,644	159,093	171,820
Cash and bank balances	496,743	417,118	558,057	585,262	695,815
Contract assets	57,031	58,594	73,929	79,547	85,910
Total current assets	1,050,543	949,054	1,047,056	1,111,519	1,241,162
PPE & IA	313,595	328,920	352,327	333,686	313,295
Others	104,087	86,282	92,712	85,456	85,456
Total non-current assets	417,681	415,202	445,039	419,142	398,751
Total Assets	1,468,225	1,364,257	1,492,096	1,530,661	1,639,913
LIABILITIES					
Trade and other payables	358,549	76,923	116,993	119,320	128,865
Loans and borrowings	9,660	9,381	7,594	(2,406)	(12,406)
Contract liabilities	116,989	108,821	131,158	135,229	146,047
Others	18,587	35,779	13,830	3,830	(6,170)
Total current liabilities	503,785	230,903	269,575	255,973	256,337
Deferred tax liabilities	61,403	50,167	41,667	41,667	41,667
Non-current loans & borrowings	141,261	16,831	193,328	193,328	193,328
Others	15,108	11,887	12,347	12,347	12,347
Total non-current liabilities	217,773	78,885	247,342	247,342	247,342
Total Liabilities	721,558	309,788	516,917	503,315	503,679
Equity					
Non-controlling interests	60	52	13,118	13,108	13,097
Shareholder Equity	746,667	1,054,468	975,179	1,143,025	1,342,691

Valuation Ratios

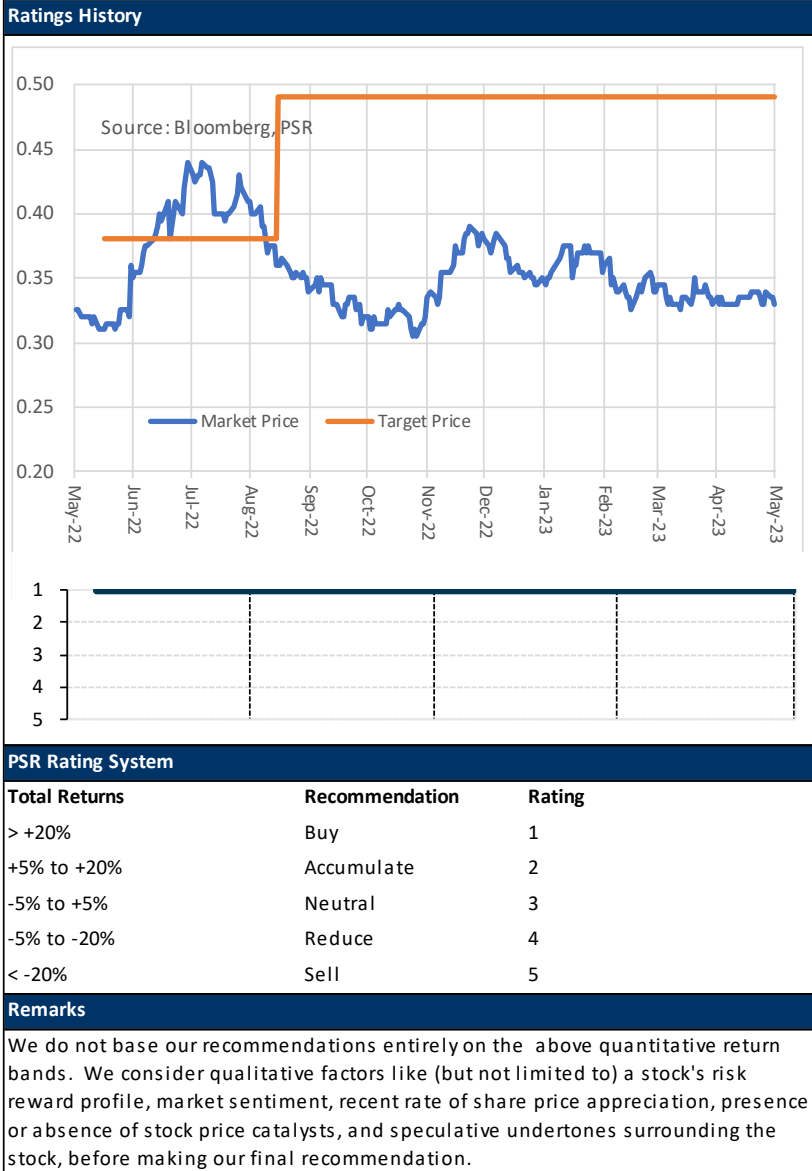
Y/E Dec	FY20	FY21	FY22	FY23e	FY24e
P/E (X)	14.5	18.8	15.4	14.7	12.6
P/B (X)	3.6	2.5	2.9	2.5	2.1
EV/EBITDA (X)	-2.3	-2.4	-2.4	-2.4	-2.6
Dividend Yield (%)	2.8%	1.6%	2.1%	3.0%	3.0%

Growth & Margins

Growth					
Revenue	-2.5%	-5.7%	17.6%	8.0%	8.0%
EBITDA	-25.7%	-21.8%	43.6%	6.1%	15.0%
EBIT	-25.9%	-21.9%	27.7%	6.4%	16.4%
Net profit, adj.	-24.8%	-22.5%	27.3%	6.8%	16.4%
Margins					
Gross margin	57.2%	60.2%	56.8%	60.0%	60.0%
EBITDA margin	28.2%	23.4%	28.5%	28.0%	29.9%
EBIT margin	27.6%	22.9%	24.8%	24.4%	26.3%
Net profit margin	27.8%	22.9%	24.7%	24.4%	26.3%

Key Ratios

ROE (%)	24.7%	13.6%	18.7%	17.0%	16.9%
ROA (%)	12.6%	10.5%	12.2%	12.7%	13.8%
Net Gearing (%)	Net cash	Net cash	Net cash	Net cash	Net cash
Net Debt/EBITDA (X)	-2.3	-2.4	-2.4	-2.3	-2.1



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