Dialog Group Berhad

Maintain BUY

(7277 | DLG MK) Energy | Energy Infrastructure, Equipment & Services

Material and labour costs push profits down

Revised Target Price: RM3.28

(previously RM3.70)

KEY INVESTMENT HIGHLIGHTS

- **Earnings came in below our and consensus estimates**
- **Higher revenue from increased activities**
- **Margin impacted by higher material and labour costs**
- **Revise FY23-FY24 downward by 11% and 12%**
- **Maintain BUY with revised TP of RM3.28 per share**

RETURN STATISTICS	
Price @ 16th February 2023 (RM)	**2.88**
Expected share price return (%)	**+31.9**
Expected dividend yield (%)	**+1.2**
Expected total return (%)	**+33.1**

Earnings slipped -0.6%yoy. Dialog Group Bhd (Dialog) reported a marginal slip in net profit by -0.6%yoy but added +1.1%qoq to RM127.2m in 1QFY23. For 6MFY23, earnings dropped -1.5%yoy to RM252.9m, which came in below our one-year estimate at 37%, and consensuses at 40%. The lower earnings were caused by increased cost on the group's operations and current projects. The risks of the Covid-19 pandemic, the Russia-Ukraine conflict, inflationary pressures and manpower constraints, resulted in cost overruns and project losses.

Revenue rose +46%yoy. The group's revenue gained +46.4%yoy and +12%qoq to RM797m in 1QFY23. For 6MFY23, revenue increased +43.7%yoy to RM1.51b. The higher revenue was attributable to the increased engineering, construction and plant maintenance activities in both Malaysian and international operations.

Higher material and labour costs. Dialog's ongoing projects in downstream Malaysia are still impacted by: (i) the COVID-19 pandemic, (ii) the war in Ukraine, (iii) inflationary pressures, and (iv) staffing shortages. These unfavourable events have severely disrupted the supply chain and raised material and labour costs which led to cost overruns and some project losses. Meanwhile, DIALOG Terminals Langsat and Pengerang (5) continued to provide Dialog with a steady income stream, in addition to the higher crude oil prices. However, due to the higher financing and operating costs, the profit contributions from these terminals were lower. Nevertheless, the sale of specialised petroleum products and services to international buyers, as well as the advancement of engineering, construction and maintenance activities in Singapore and fabrications in New Zealand, had contributed positively to its performance.

SHARE PRICE CHART



Share price performance (%)	Absolute	Relative
1 month	-0.4	0.1
3 months	5.7	24.4
12 months	-10.1	-3.3

KEY STATISTICS	
FBM KLCI	1,484.26
Syariah compliant	Yes
FSGBM Index	No
ESG Grading Band	☆☆☆
Issues shares (m)	5642.50
Estimated free float (%)	30.34
Market Capitalisation (RM'm)	14,614.26
52-wk price range	RM1.71 - RM2.89
Beta vs FBM KLCI (x)	1.42
3-mth average daily volume (m)	4.99
3-mth average daily value (RM'm)	12.05
Top Shareholders (%)	
Ngau Boon Keat	19.12
Employees Provident Fund Board	8.50
Kumpulan Wang Persaraan Diperbadan	4.98

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Expansion strategies remain. Dialog will continue to invest in phased capacity expansions for dedicated long-term customers across its midstream portfolio, in line with the longer-term strategy to grow its sustainable and recurring income. For the downstream business, Dialog will continue to leverage on its established track record in integrated technical services comprising Engineering, Procurement, Construction & Commissioning, Plant Maintenance & Catalyst Handling Services, and Specialist Products and Services. Barring unforeseen circumstances, we remain optimistic of Dialog's performance in FY23.

Latest development project. In a separate report, Dialog announced that its indirect wholly owned subsidiary, Dialog Terminals Langsat (3) Sdn. Bhd. (DTL3) will be expanding its terminal operations with the development of storage facilities for renewable products at its terminal in Tanjung Langsat, namely Dialog Terminals Langsat 3 (Project DTL3). Project DTL3 is Dialog's first foray into storage facilities for sustainable and renewable fuel products with a storage capacity of approximately 24,000 m3 connected to truck loading bays and existing marine facilities. This development is largely in response to growing investor interest in low-carbon fuel alternatives and Dialog is expanding its terminal operations to cater for such sustainable and renewable fuel products.

In line with Sustainability Goals. The development of storage facilities for sustainable and renewable products is in line with low-carbon economy transition under Dialog's Climate Change Strategy as part of ongoing efforts to expand product and solution offering to support the growth and development in the sustainable and renewable sector. Additionally, the strengthening of the midstream capabilities will lead to an increase in sources of sustainable and recurring income in the future and reinforces position as a leading integrated technical services provider. The engineering and construction of Project DTL3 will commence immediately and expected to be completed in 4QCY24.

Optimistic for the rest of FY23. As a leading integrated technical service provider that is diversified across the upstream, midstream, and downstream businesses of the energy sector, Dialog will remain focused and steadfast in the pursuit of its key long-term strategies. Dialog is now the 2nd largest independent terminal owner cum operator in Southeast Asia with current operating capacity of RM20m. Challenges remain however, which include: (i) availability of skilled manpower, (ii) technical expertise and (iii) changes in prices of materials.

Revise FY23-FY24 earnings estimates. In consideration that Dialog's 2QFY23 earnings came in below our expectation, we revise our FY23-FY24 earnings forecast downward by -11% and -12% respectively. As such, we also revise our target **price to RM3.28** (previously RM3.70), by pegging a PER of 30.6 sen to an EPS23 of 10.7 sen. The PER is based on the group's 5-year average PER.

Maintain BUY. All in, we are maintaining our **BUY** call on Dialog, with a revised **target price of RM3.28.** The general outlook on the oil market is expected to be robust in 2023 as demand for oil recovers fully from the impact of the Covid-19 pandemic in China, as well as in EU, where energy is in high demand since the sanctions on Russian oil products. As such, we reiterate our positive stance on Dialog for the remainder of FY23, mainly for its: (i) growing potential for its storage tank farm business in PDT and DLT, (ii) strong prospects for its upstream and downstream sector, and (iii) new initiatives to contribute to the environment and to support the government's sustainability goals.

INVESTMENT STATISTICS

Financial year ending 30th June (in RM'm unless otherwise stated)	2021A	2022A	2023F	2024F	2025F
Revenue	1,609.9	2,319.0	3,151.8	3,339.0	3,536.8
EBIT	621.4	590.4	932.3	939.7	961.8
Pretax Profit	595.0	550.3	672.9	685.0	706.7
Profit After Tax	543.1	505.9	610.9	620.5	635.2
PATAMI	**543.1**	**508.0**	**605.9**	**615.5**	**630.2**
EPS (sen)	9.6	8.9	10.7	10.9	11.2
EPS growth (%)	-14.0%	-7.3%	20.3%	1.6%	2.4%
PER (x)	41.2	44.4	30.6	30.1	29.4
Dividend per share (sen)	3.1	3.1	3.8	3.8	3.9
Dividend yield (%)	0.8%	0.8%	1.1%	1.2%	1.2%

Source: Company, MIDFR

Table 1: Dialog's 2QFY22 Results Summary

Financial year ending 30th June (in RM'm unless stated otherwise)	Quarterly results					Cumulative results		
	2QFY22	1QFY23	2QFY23	QoQ (%)	YoY (%)	6MFY22	6MFY23	YoY (%)
Revenue	544.5	711.7	797.0	12.0	46.4	1,049.9	1,508.7	43.7
Operating Expenses	(476.0)	(664.0)	(750.1)	13.0	(10.6)	(914.9)	(1,414.2)	54.6
Other Operating Income	9.3	12.0	13.0	8.4	(49.5)	19.2	25.1	30.5
Fair value gain on disposal of JV	-	-	-	-	-	-	-	
JCE	68.4	84.1	97.4	15.8	42.4	141.9	181.5	28.0
Finance Costs	(6.8)	(16.4)	(17.5)	6.5	158.1	(13.9)	(33.9)	143.2
Profit Before Tax	139.5	127.4	139.9	9.8	0.3	282.2	267.3	-5.3
Tax expense	(11.3)	(7.2)	(8.8)	23.1	(21.9)	(23.0)	(16.0)	-30.3
Profit After Tax	128.1	120.2	131.1	9.0	2.3	259.2	251.3	-3.0
Minority Interests	0.3	(5.6)	3.9	(170.5)	1,453.4	2.5	(1.6)	-166.6
PATAMI	127.9	125.8	127.2	1.1	(0.6)	256.7	252.9	-1.5
Normalised PATAMI	127.9	125.8	127.2	1.1	(0.6)	256.7	252.9	-1.5
EPS (sen)	2.3	2.2	2.3	0.9	(0.9)	4.6	4.5	-1.5
DPS (sen)	2.3	3.4	2.3	(33.8)	(0.9)	4.6	5.7	24.2
				+/(-) ppts				*+/(-) ppts*
PBT Margin (%)	29.8	23.8	17.9	(5.9)	(11.9)	37.0	23.7	-13.2
Tax Rate (%)	9.6	7.4	5.6	(1.8)	(4.0)	8.7	8.1	-0.7
Net Margin (%)	26.5	22.4	17.7	(4.7)	(8.9)	33.7	21.9	-11.8

Source: Company, MIDFR

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MIDF AMANAH INVESTMENT BANK: GUIDE TO RECOMMENDATIONS	
STOCK RECOMMENDATIONS	
BUY	Total return is expected to be >10% over the next 12 months.
TRADING BUY	Stock price is expected to *rise* by >10% within 3-months after a Trading Buy rating has been assigned due to positive newsflow.
NEUTRAL	Total return is expected to be between -10% and +10% over the next 12 months.
SELL	Total return is expected to be <-10% over the next 12 months.
TRADING SELL	Stock price is expected to *fall* by >10% within 3-months after a Trading Sell rating has been assigned due to negative newsflow.
SECTOR RECOMMENDATIONS	
POSITIVE	The sector is expected to outperform the overall market over the next 12 months.
NEUTRAL	The sector is to perform in line with the overall market over the next 12 months.
NEGATIVE	The sector is expected to underperform the overall market over the next 12 months.
ESG RECOMMENDATIONS* - source Bursa Malaysia and FTSE Russell	
☆☆☆☆	Top 25% by ESG Ratings amongst PLCs in FBM EMAS that have been assessed by FTSE Russell
☆☆☆	Top 26-50% by ESG Ratings amongst PLCs in FBM EMAS that have been assessed by FTSE Russell
☆☆	Top 51%- 75% by ESG Ratings amongst PLCs in FBM EMAS that have been assessed by FTSE Russell
☆	Bottom 25% by ESG Ratings amongst PLCs in FBM EMAS that have been assessed by FTSE Russell

* ESG Ratings of PLCs in FBM EMAS that have been assessed by FTSE Russell in accordance with FTSE Russell ESG Ratings Methodology