Empowering Energy Efficiency

SOLAR DISTRICT COOLING GROUP BERHAD

Fair Value: RM 0.60 (+58%)

Company Description

Solar District Cooling Group Berhad ("SDCG") principally involved in the provision and maintenance of building management systems ("BMS"), solar thermal systems, other systems & equipment and other energy services.

Investment Highlight

- **Renewal of Ministry of Health ("MOH") hospital support services concession:** The concession which covers maintenance services for all 148 MOH hospitals and institutions, managed by five concession companies, will expire on March 31, 2025. Among these five companies, several are major clients of SDCG. According to the New Straits Times, the government pays RM1.3 billion ("bn") annually to these companies for hospital support services. If MOH increases the budget or awards additional contracts to SDCG's major clients, the Group stands to benefit from it.

- **Government green energy-related policies and incentives:** In response to environmental, social, and governance ("ESG") initiatives, the government has implemented a range of policies and incentives, including the National Energy Policy ("NEP"), the National Energy Transition Roadmap ("NETR"), Green Technology Tax Incentives comprises Green Investment Tax Allowance ("GITA") and Green Income Tax Exemption ("GITE"), and various financing schemes. These measures are expected to incentivize more businesses to invest in renewable energy ("RE") and energy efficiency programs.

- **Growing investment in data centres:** Malaysia has attracted billions of dollars in data centre investments from tech giants such as Google, Nvidia, and Microsoft. As energy consumption is a significant concern for companies aiming to reduce costs, ensuring an uninterrupted power supply is crucial. Given SDCG's involvement in BMS and chiller maintenance, the company is well-positioned to benefit from this growing demand.

- **Strong profit margin:** SDCG has achieved a robust profit margin over the past few years, ranging from 13.49% to 27.80% from FY2020 to FY2023. This margin is notably higher compared to peers in the BMS segment, indicating effective cost control by management. We anticipate that the margin will remain stable moving forward.

Valuation / Recommendation

We derive a fair value of RM0.60 based on 26x multiple to its FYE2025F EPS of 2.30 sen. The IPO aims to raise approximately RM45.10 million ("mn") from the issuance of 118.67mn new shares. A total of 62.36% of proceeds will be utilised for capital expenditure, 28.10% is allocated for general working capital, while the remaining 9.54% of the proceeds will be utilised for listing expenses.

As of FYE2023, the Group's current ratio is above 1x at 4.74x reflecting a strong capacity to repay its current liabilities. In terms of funding ability, SDCG shows healthy ability, given the low gearing ratio below 1x at 0.05x. With the strong inflow of investments from multinational companies, along with the government's supportive policies, we anticipate sustained growth in the group's performance over the long term.

IPO TIMELINE	
Opening Date	28 Aug 2024
Closing Date	6 Sep 2024
Listing Date	19 Sep 2024
IPO Price (RM)	0.38
Expected Return	57.89%
Market/ Sector	Industrial Products & Services
Bursa Code	0321

IPO Details	Shares(mn)
Public Issue	118.67
Enlarged share	423.82
	RM(mn)
Market Cap	161.05
Shariah compliant	Yes

Substantial Shareholders	Shares(mn)	(%)
Edison Kong	274.64	64.80
Eileen Liuk	30.52	7.20

Utilisation of IPO Proceeds	RM(mn)	(%)
Purchase of Materials	18.70	41.47
General Working capital	12.67	28.10
Tender Bonds/ Performance Bonds	5.00	11.09
Capital Expenditure	2.52	5.59
Expansion of Headquarters	1.90	4.21
Estimated listing expenses	4.30	9.54
Total	**45.09**	**100.00**

Allocation	Shares(mn)	(%)
Public Issue		
Malaysian Public via balloting process:		
• Public investors	10.60	2.50
• Bumiputera public investors	10.60	2.50
Eligible Parties	21.19	5.00
Placement to selected investors	76.29	18.00
Total	**118.67**	**28.00**
Total enlarged share capital upon listing	**423.82**	

Source: Company Prospectus

Key Financial Summary

FYE Dec (RMmn)	2022A	2023A	2024F	2025F	2026F
Revenue	18.65	26.62	31.41	39.27	**47.12**
Gross Profit	10.68	14.35	16.94	21.17	**25.40**
Pre-tax Profit	6.46	8.68	10.24	12.80	**15.36**
Core Net Profit	5.18	6.35	7.78	9.73	**11.68**
Core EPS (Sen)	1.22	1.50	1.84	2.30	**2.76**
P/E (x)	31.07	25.38	20.69	16.55	**13.79**
DPS (Sen)	1.49	0.47	0.00	0.00	**0.00**
Dividend Yield (%)	3.91	1.24	0.00	0.00	**0.00**

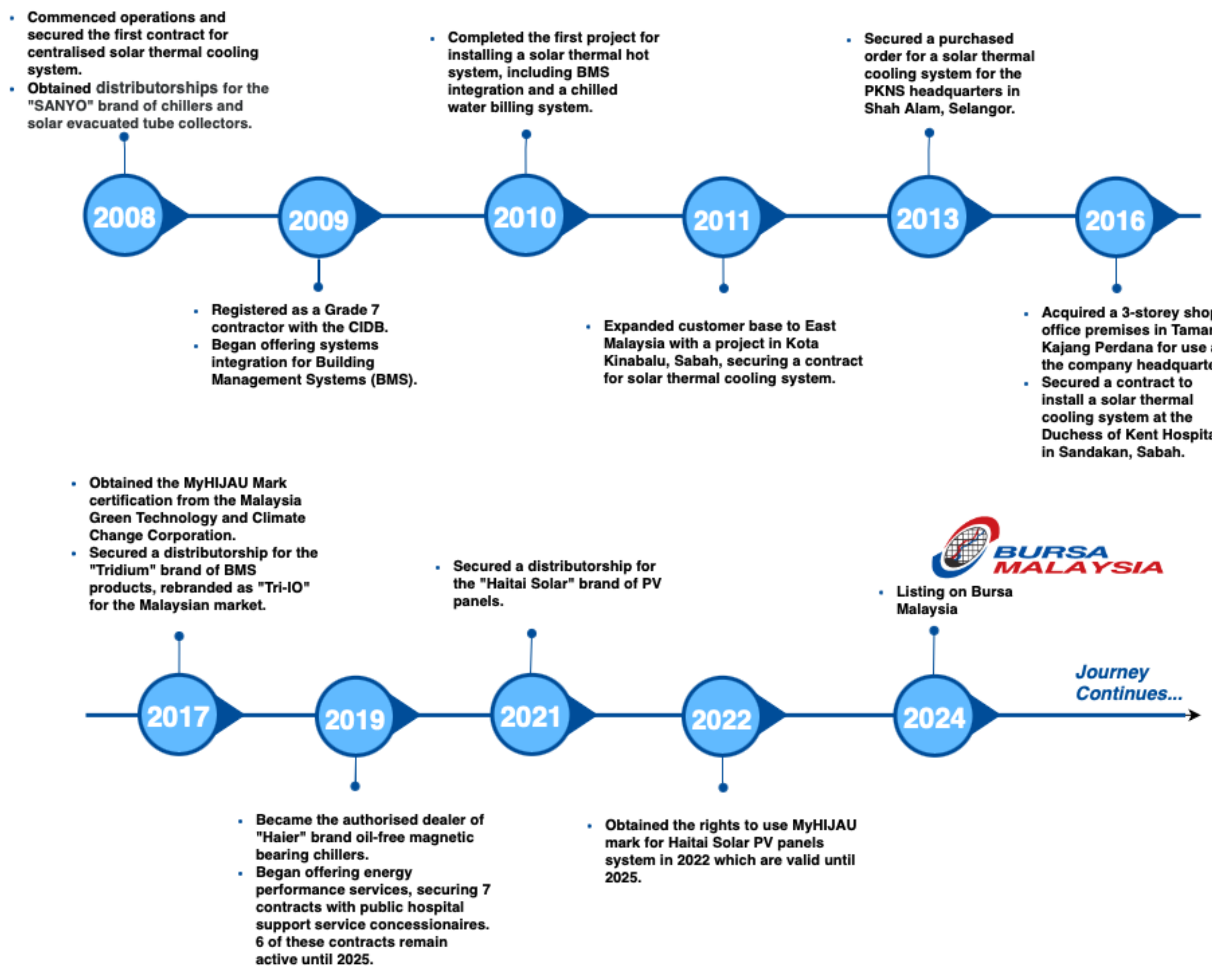
Source: Company Prospectus, Eco Asia Research Estimates
EPS, P/E and DPS from 2022A to 2023A (pre-IPO) are on pro-forma basis for comparative purposes only.

Company Background

The Group was incorporated in Malaysia under the Act on 25 April 2023 as a private limited company under the name of Solar District Cooling Group Sdn Bhd. On 25 July 2023, it was converted into a public limited company and assumed its present name.

Kejuruteraan Efektif Dinamik Sdn Bhd ("KED"), a wholly owned subsidiary of SDCG, is principally involved in mechanical and electrical works, and project management services. Malaysia accounted for 97.45%, 98.94%, 99.67% and 99.15% of the Group total revenue for the FY 2020, FY 2021, FY 2022 and FP 2023, respectively. The remainder of the revenue was from Singapore for FY 2020 and FY 2021, and Brunei for FY 2022 and FP 2023.

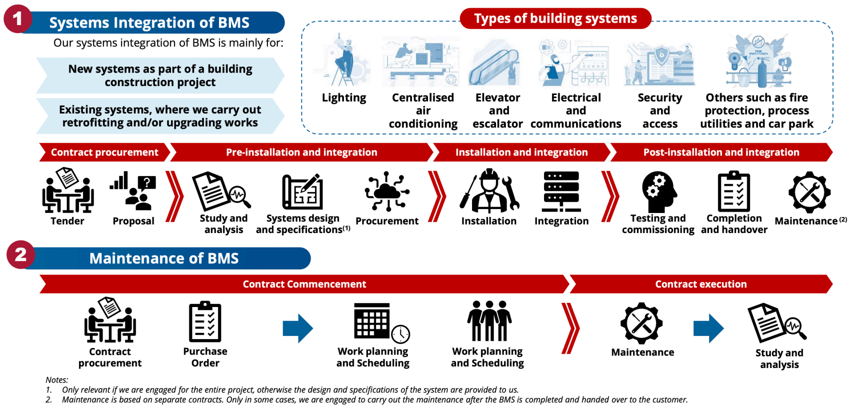
Key Milestones



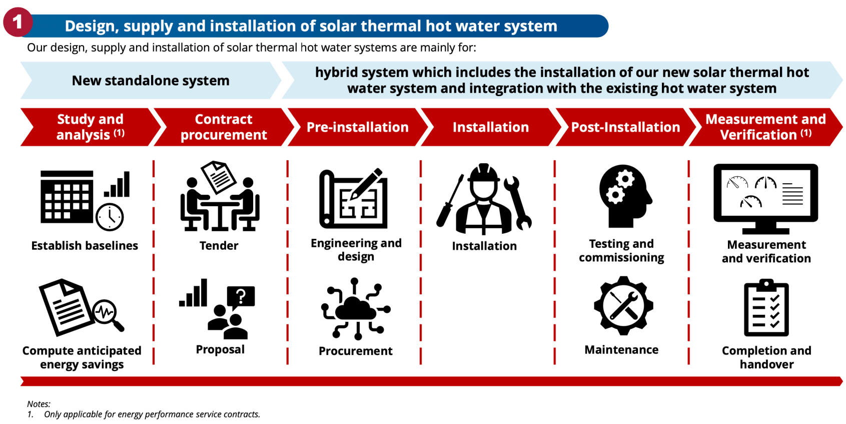
Source: Company Prospectus, SDCG

Principal Activities

Building Management Systems: BMS is designed to provide integrated management, monitoring, and control of building systems, helping operators achieve cost-effective, reliable and safe operations. SDCG also provides maintenance services on a contract basis (recurrent revenue over the contract period), as well as on an ad hoc basis (project based non-recurrent revenue).



Solar Thermal Systems and Energy Saving Services: It is primarily designed for heavy hot water users, such as hospitals. The group focuses on solar thermal hot water systems that harness sunlight directly to heat water. In some cases, their services also include retrofitting fluorescent lighting with light-emitting diode ("LED") lighting to further reduce electricity consumption. This segment of the services is dedicated on helping customers to save energy and reduce the carbon footprint of their operations.

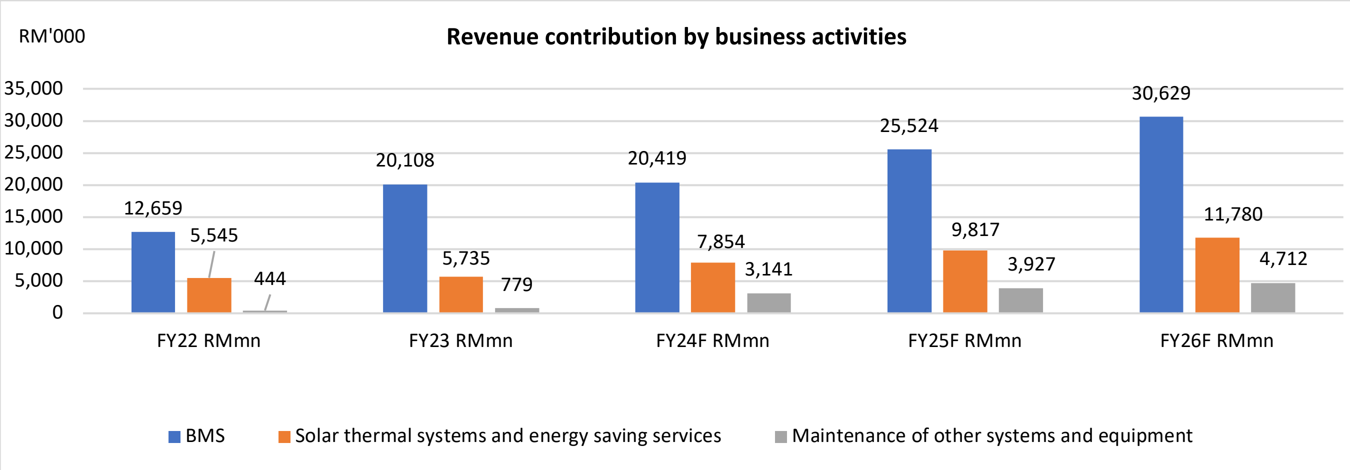


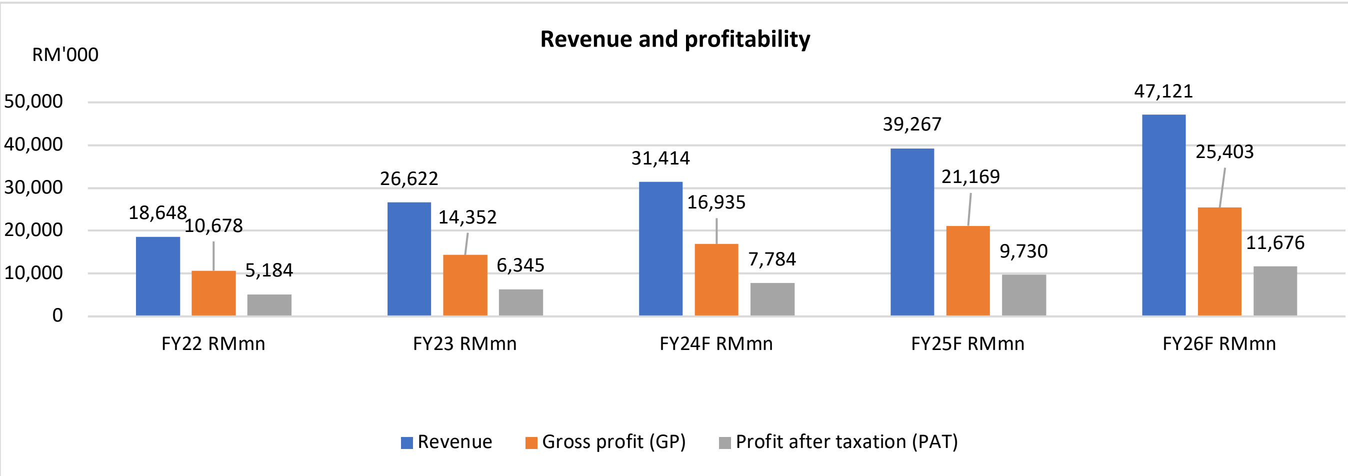
Maintenance of Other Systems and Equipment: The group also provides maintenance for systems like gas-fired chillers and chilled water systems, whether installed by the group or by third-party providers.

Source: Company Prospectus, SDCG

Revenue and Profitability

The Group's revenue from FYE2022 to FYE2023 was mainly derived from its BMS services that contributed 75.56% of total revenue – as of FYE2023. Revenue contributions by business activities as well as the revenue and profitability from FYE2022 to FYE2023, FYE2024F, FYE2025F and FYE2026F are as below:





Source: Company Prospectus / Eco Asia Research Estimates

Future Plans

SDCG's future plans and business strategies are as below:

1. Expand the Headquarters:

- Expansion of the Headquarters by constructing a new extension on the remaining vacant land, which will increase the built-up area of existing Headquarters from 8,320 square feet ("sq. ft.") to approximately 13,000 sq. ft.

2. Purchase new tools and equipment:

- Purchase the following additional tools, equipment and vehicles to enhance productivity and service delivery.
- Pick-up trucks, Forklift, Drones with thermal sensor and Panel cleaning equipment.

3. ICT software enhancement:

- Intend to subscribe additional Internet of Things ("IoT") software, such as Solar irradiance database, Computer-aided design ("CAD") software, Specialised design software, Energy system simulation software and Accounting software.

4. Address opportunities in Solar PV systems:

- Intend to commence the solar photovoltaic ("PV") system business based on the power purchase agreement ("PPA") mode of operation, which the group has installed in the past.

Strategic Competitive Advantages and Strengths

Established track record of approximately 17 years to serve as a reference site for prospective customers: The Group started its BMS services in 2009, solar thermal hot water systems in 2010, and energy performance services in 2019. In addition, they have cultivated long-term business relationships with their customers. SDCG track record provides them with the platform to serve their existing customers as well as prospective new customers to sustain and grow their business.

Solar thermal hot water system assists companies to reduce their carbon footprint: The solar thermal hot water system uses sunlight to directly heat the water, while other hot water systems use either diesel, Liquefied Petroleum Gas ("LPG"), or electricity. The use of RE in their solar thermal hot water system would appeal to prospective customers who are seeking to reduce their carbon footprint and improve their environmental responsibilities.

Technical expertise and certifications to meet customers' requirements: The Group has the expertise to meet customer requirements in providing and maintaining BMS, solar thermal systems, and energy-saving services. Their relevant registrations, including as an Energy Service Company ("ESCO") and with the Energy Commission Malaysia @ Suruhanjaya Tenaga ("ST"), Grade 7 contractor and Grade 4 contractor with Construction Industry Development Board ("CIDB"), and the Ministry of Finance ("MOF"), demonstrate their capability to fulfil customer needs.

Own brands to help facilitate brand awareness and customer loyalty: SDCG has key equipment and software for BMS, including Direct Digital Control ("DDC") and central controllers manufactured by a third party, which are rebranded and marketed under their 'Tri-IO' brand. They also have their brand of solar thermal collectors, manufactured by a third party, that is rebranded and marketed under the Group 'SDC' brand.

Key Risks

Termination or suspension of contracts: Any termination or suspension of contracts before completion may negatively impact SDCG's financial performance by preventing them from recovering costs and losing potential revenue and profit.

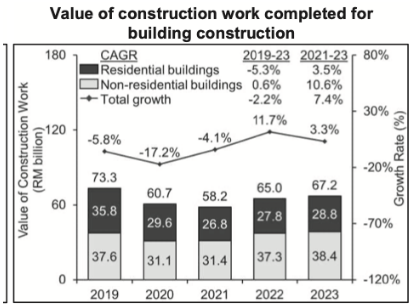
Dependent on retaining and obtaining specific registration and license: Non-compliance with regulations, terms, or conditions can lead to fines, penalties, or the suspension, cancellation, or non-renewal of registrations and licenses. Failure to maintain or renew these licenses could disrupt business operations, limit tender participation, and hinder work or energy performance services, ultimately harming the Group's business and financial performance.

Exposed to Foreign Exchange Rates ("FOREX") fluctuations: The business faces FOREX risk, as some portion of material and service purchases, including subcontractor costs, are made in foreign currencies such as USD, RMB, SGD, and Euro. Unfavourable exchange rate fluctuations against the RM could negatively affect financial performance.

Subject to changes in Government regulations or policies: Any changes in government regulations or policies could impact company ability to secure new energy performance service contracts under financially favourable terms. Such developments could materially affect business growth and potentially have a negative impact on future financial performance.

Industry Outlook

Positive outlook in property sector: Malaysia's Gross Domestic Product ("GDP") increased by 3.7% and the construction sector grew by 6.1% in 2023. The value of completed construction project rose at a compound annual growth rate ("CAGR") of 7.4% from 2021 to 2023. In addition, the supply of propose-built offices expanded at a CAGR of 12.6% during the same period. The current commercial property supply constitutes the foundation market, while future supply presents growth opportunities for operators in the BMS industry.



Future supply of selected high-rise commercial properties

	Purpose-built offices (units)	Serviced apartments (units)
2019	66	300,032
2020	63	300,846
2021	56	320,522
2022	79	304,489
2023	71	278,722
CAGR (2019-23)	1.8%	-1.8%
CAGR (2021-23)	12.6%	-6.7%
Q1 2023	78	303,916
Q1 2024	71	315,315
Growth (Q1'23-24)	-9.0%	3.8%

Future supply= incoming supply + planned supply
(Source: NAPIC)

Energy efficiency initiation by Malaysia Government: Since 2013, local government has promoted energy efficiency in government buildings through energy performance contracts. MOH has been actively implementing high-impact energy projects, either through conventional methods or energy performance contracting in its facilities especially its hospitals – given hospital buildings are one of the high-energy users in the country. By the end of 2022, MOH implemented 44 energy projects in its facilities. SDCG supports these efforts by offering energy performance services to hospital support companies, which bodes well for the Group.

DEFINITION OF RATINGS

Eco Asia Investment Advice uses the following rating system:

STOCK RECOMMENDATION

BUY Total return (price appreciation plus dividend yield) is expected to exceed 10% in the next 12 months.
TRADING BUY Share price may exceed 15% over the next 3 months, however longer-term outlook remains uncertain.
HOLD Share price may fall within the range of +/- 10% over the next 12 months
TAKE PROFIT Target price has been attained. Fundamentals remain intact. Look to accumulate at lower levels.
TRADING SELL Share price may fall by more than 15% in the next 3 months.
SELL Share price may fall by more than 10% over the next 12 months.
NOT RATED Stock is not within regular research coverage.

SECTOR RECOMMENDATION

OVERWEIGHT The Industry as defined by the analyst's coverage universe, is expected to outperform the relevant primary market index over the next 12 months
NEUTRAL The Industry as defined by the analyst's coverage universe, is expected to perform in line with the relevant primary market index over the next 12 months
UNDERWEIGHT The Industry as defined by the analyst's coverage universe, is expected to underperform the relevant primary market index over the next 12 months

Applicability of ratings

The respective analyst maintains a coverage universe of stocks, the list of which may be adjusted according to needs. Investment ratings are only applicable to the stocks which form part of the coverage universe. Reports on companies which are not part of the coverage do not carry investment ratings as we do not actively follow developments in these companies.

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