29 December 2023

Technology | Hardware & Equipment

VSTECS (VST MK)

Not Rated

The Leading One-Stop ICT Solution Enabler

Fair Value (Return):	MYR1.88 (43.5%)
Price:	MYR1.31
Market Cap:	USD101m
Avg Daily Turnover (MYR/USD)	0.21m/0.05m

- **MYR1.88 FV based on 10x FY24F P/E.** VSTECS is set to continue its growth momentum into FY24, supported by the digital transformation and technology advancements that sustains the demand for the enterprise segment and boosts the recovery in the consumer sector. 7x FY24F P/E (ex-cash P/E of 5.9x) at -3SD from the 5-year mean offers deep value vis-à-vis peers (trading at 10-20x) and is bound for a re-rating given strong cash generation (with ever-growing capabilities) and recurring income in consulting and software & solution services backed by a healthy 5% yield.
- **Technological advancement.** Delays in the implementation of enterprise systems projects seen in 9M23 should spill-over to growth into FY24, in our view. This is on top of the growing momentum in major networking infrastructure due to the 5G rollout and increasing need of cyber security and cloud computing & services, given the mushrooming of various data centres and artificial intelligence (AI) integration. The public and private sectors are set to continue their usual technology refresh and upgrades in addition to the digitalisation push trends by both the Government and hyper-scalers. VSTECS is also venturing into supplying power solutions to data centres to capture the increasing investments in them here.
- **ICT distribution to recover while enterprise systems remains buoyant.** Both IDC and Gartner predict a recovery in global personal computer (PC) and smartphone shipments into 2024 following two years of contractions. The demand for ICT devices is set to recover after the FY22-23 slumps as the major refresh cycle should come in FY24-25 following the super-cycle in 2020-2021 that elevated the total installed base. Budget 2024 allocations for digital enablement and automation (MYR100m to MSMEs and MYR900m under Bank Negara Malaysia) and accelerated implementation of e-invoicing are the other pull-push factors for ICT products demand.
- **Sustainable growth...** We forecast a 3-year earnings CAGR of 8.6%, supported by product range expansions in the renewables sector, new distributorship, increasing solution services, and government digitalisation efforts. There is growing recurring income from its managed services and software & solutions offerings to meet surging cybersecurity, AI integration, application development, cloud, and consulting services demand.
- **…at undemanding valuations.** We ascribe a 10x target P/E on VSTECS, which is still at a discount to local and international ICT products distribution and solutions peers, and system integrators (trading at 10-20x). While we acknowledge that margins are on the lower end, it is the nature of a trading business and serves as an obstacle for new entrants. The growing competency in its software as a service (SaaS) model, full life-cycle cloud service capabilities, and ever-growing enterprise segment and product range are the re-rating catalysts on top of a dividend yield of c.5% and mid-teens ROEs. Key risks: Weaker-than-expected demand, business failures of one of more ICT principals, slower-than-expected adoption, and receivables risks.

Forecasts and Valuation	Dec-21	Dec-22	Dec-23F	Dec-24F	Dec-25F
Total turnover (MYRm)	2,626	2,771	2,738	3,005	3,305
Recurring net profit (MYRm)	55	60	62	68	76
Recurring net profit growth (%)	49.5	8.5	4.4	8.9	12.6
Recurring P/E (x)	8.53	7.84	7.51	6.89	6.12
P/B (x)	1.2	1.1	1.0	0.9	0.9
P/CF (x)	na	na	5.52	11.88	10.34
Dividend Yield (%)	2.9	4.7	4.8	5.1	5.7
EV/EBITDA (x)	4.95	5.14	4.25	3.75	3.16
Return on average equity (%)	15.5	15.2	14.5	14.3	14.7
Net debt to equity (%)	net cash	net cash	net cash	net cash	net cash

Source: Company data, RHB

Analyst

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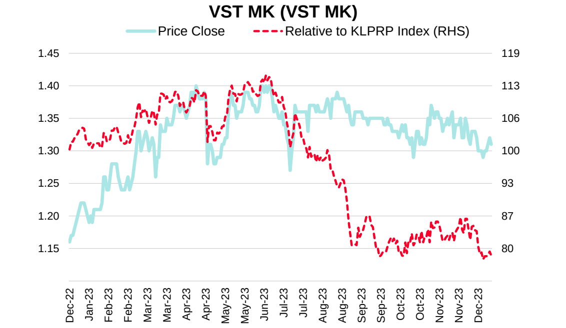
Share Performance (%)

	YTD	1m	3m	6m	12m
Absolute	12.0	(2.2)	(2.2)	(3.0)	11.0
Relative	(22.8)	(3.8)	(0.8)	(28.0)	(23.0)
52-wk Price low/high (MYR)					1.16 – 1.40



Source: Bloomberg

Note:
Small cap stocks are defined as companies with a market capitalisation of less than USD0.5bn.

Financial Exhibits

Asia
Malaysia
Technology
VSTECS
VST MK
Not Rated

Valuation basis

10x P/E on its FY24 earnings

Key drivers

i. Strong ICT demand;
ii. Growing enterprise solutions;
iii. Digital transformation;
iv. Technological advancements.

Key risks

i. Business failure of ICT principals;
ii. Slower-than-expected adoption of ICT;
iii. Slowdown of consumer demand for ICT products;
iv. Receivables risks.

Company Profile

VSTECS is a leading distribution hub for ICT products comprising notebooks, personal computers, smartphones, tablets, wearables, printers, software, network and communication infrastructure, servers, and enterprise software from more than 46 leading principals.

Financial summary (MYR)	Dec-21	Dec-22	Dec-23F	Dec-24F	Dec-25F
Recurring EPS	0.15	0.17	0.17	0.19	0.21
DPS	0.04	0.06	0.06	0.07	0.07
BVPS	1.05	1.15	1.26	1.39	1.53
Return on average equity (%)	15.5	15.2	14.5	14.3	14.7

Valuation metrics	Dec-21	Dec-22	Dec-23F	Dec-24F	Dec-25F
Recurring P/E (x)	8.53	7.84	7.51	6.89	6.12
P/B (x)	1.2	1.1	1.0	0.9	0.9
FCF Yield (%)	(4.5)	(5.1)	17.5	7.6	8.4
Dividend Yield (%)	2.9	4.7	4.8	5.1	5.7
EV/EBITDA (x)	4.95	5.14	4.25	3.75	3.16
EV/EBIT (x)	5.27	5.34	4.40	3.93	3.36

Income statement (MYRm)	Dec-21	Dec-22	Dec-23F	Dec-24F	Dec-25F
Total turnover	2,626	2,771	2,738	3,005	3,305
Gross profit	139	150	159	174	194
EBITDA	75	80	82	89	102
Depreciation and amortisation	(5)	(3)	(3)	(4)	(6)
Operating profit	71	77	79	85	96
Net interest	1	(0)	1	2	2
Pre-tax profit	74	80	84	91	102
Taxation	(19)	(20)	(21)	(23)	(26)
Reported net profit	55	60	62	68	76
Recurring net profit	55	60	62	68	76

Cash flow (MYRm)	Dec-21	Dec-22	Dec-23F	Dec-24F	Dec-25F
Change in working capital	0.6	(78.3)	(79.5)	20.4	(31.0)
Cash flow from operations	(20.9)	(22.2)	84.8	39.4	45.2
Capex	0.0	(1.8)	(3.0)	(4.0)	(6.0)
Cash flow from investing activities	9.5	0.1	(3.7)	(4.8)	(7.0)
Dividends paid	(13.4)	(15.0)	(22.4)	(23.7)	(26.7)
Cash flow from financing activities	(14.3)	(3.9)	(25.8)	(24.7)	(24.4)
Cash at beginning of period	98.3	72.7	46.6	101.9	111.8
Net change in cash	(25.7)	(26.1)	55.3	9.9	13.9
Ending balance cash	72.7	46.6	101.9	111.8	125.7

Balance sheet (MYRm)	Dec-21	Dec-22	Dec-23F	Dec-24F	Dec-25F
Total cash and equivalents	73	47	102	112	126
Tangible fixed assets	6	5	6	5	5
Total investments	24	26	26	27	28
Total assets	688	700	732	799	877
Short-term debt	0	0	1	2	3
Total long-term debt	0	14	9	5	4
Total liabilities	312	288	281	304	332
Total equity	376	411	451	495	545
Total liabilities & equity	688	700	732	799	877

Key metrics	Dec-21	Dec-22	Dec-23F	Dec-24F	Dec-25F
Revenue growth (%)	30.2	5.5	(1.2)	9.8	10.0
Recurrent EPS growth (%)	50.1	8.9	4.4	8.9	12.6
Gross margin (%)	5.3	5.4	5.8	5.8	5.9
Operating EBITDA margin (%)	2.9	2.9	3.0	3.0	3.1
Net profit margin (%)	2.1	2.2	2.3	2.3	2.3
Dividend payout ratio (%)	24.3	37.1	36.0	35.0	35.0
Capex/sales (%)	0.0	0.1	0.1	0.1	0.2
Interest cover (x)	325	151	229	259	282

Source: Company data, RHB

Investment Thesis

The 1-stop ICT solutions enabler. VSTECS has established track records in the ICT world for the past 35 years, with long-term established relationships with 46 world-leading ICT principals. It has been a distribution partner with brands such as HP Malaysia, IBM, Apple, and Cisco for more than 10 years. VSTECS now has a comprehensive portfolio across consumer and enterprises solutions in hardware, software, training, consulting, and value-added services. The close working relationship and market-leading position with the major ICT principals provides the group with an insight into the latest trends in ICT technology, better rebates, and – therefore – enabling it to make more strategic decisions. VSTEC's market-leading position, coupled with its infrastructure readiness (sales channel, balance sheet, support, logistics, and value-added services) are essential in securing new distributorships as well as extending current ones.

In recent years, the group has also widened its products range under the ICT distribution segment to start distributing IoT home appliances involving televisions, refrigerators, and air conditioner (to name a few), as well as renewable energy infrastructure and solutions with Schneider Electric's uninterruptible power supplies that are sold under VSTEC's flagship brand APC. Notably, the group also distributes Smart-Mi products to retail physical stores such as Senheng and Harvey Norman as well as through Senheng owner Senheng New Retail's (SENHENG MK, NR) super-apps and other e-commerce channels. VSTECS now distributes and resells various cloud solutions from IBM, Microsoft Azure, Huawei Cloud, AWS, and Alibaba Cloud and is looking to complete the offerings by working on to on-board another major hyper-scaler.

As compared to its local peers, VSTECS represents a broader range of ICT devices brands and has its own warehouse and logistics solutions to store and distribute all stock-keeping units (SKUs). Some of the group's principals are giving more SKUs, which we see is a testament to its established distribution track records. VSTECS is authorised by some principals – eg HP, Lenovo Group, and Asus Computer International – to distribute their products through their official physical stores, and e-branded stores in online shopping platforms Lazada and Shopee. Supported by its broad range of products, high efficiency, and better credit terms, VSTECS has gained a bigger market share in distributing ICT products to its network of more than 4,600 resellers.

For the enterprise segment, the group is the preferred partner for all the major systems integrators such as Cloudpoint Technology (CLOUDPT MK, NR), Heitech Padu (HEIT MK, NR), Infoline Tec Group (INFOTEC MK, NR), Infomina (INFOM MK, NR), Mesiniaga (MESI MK, NR), and SNS Network Technology (SNS MK, NR). Revenue for the enterprise segment is now on par and even surpassed the ICT distribution segment as largest contributor, thanks to the robust demand from the financial institutions, telecommunications companies, and the public sector. Various technological advancement also contributed to the increasing demand for networking devices, cybersecurity, and cloud computing, in our view.

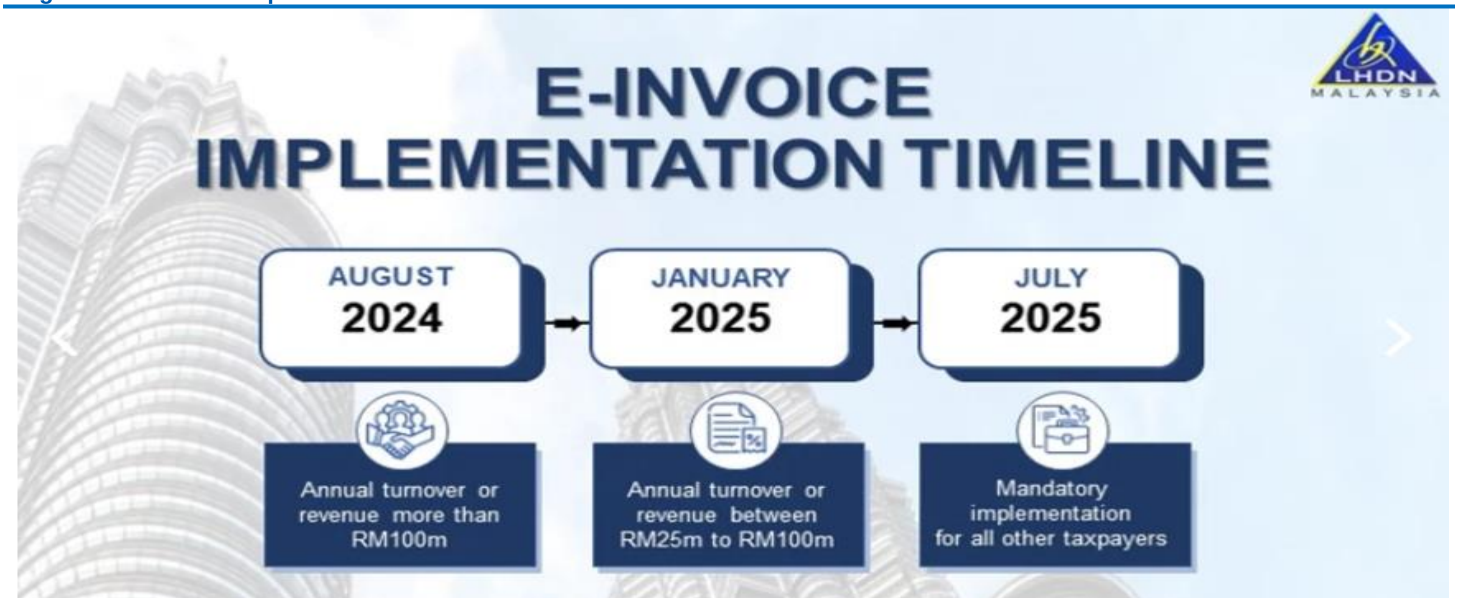
Figure 1: Various brands carried under VSTECS

Source: Company data

Accelerated digitalisation. VSTECS is expected to benefit from government initiatives to drive ICT adoption in the country through the 12th Malaysia Plan (12MP) – this is part of the Government's efforts to shift Malaysians towards a more technologically literate, thinking workforce. In line with the focus under the New Industrial Master Plan 2030 and 12MP, the development of digital- and technology-based industries and accelerating government technology adoption may entail additional capex spending by the Government on IT infrastructure, equipment, and the upgrading of school facilities.

Additionally, there is also the implementation of mandatory electronic invoicing or e-Invoices by the Inland Revenue Board or LHDN for businesses with an annual revenue of more than MYR100m by 1 Aug 2024. This will be followed by businesses with annual revenues of more than MYR50m and MYR25m by 1 Jan 2025. All other businesses must adopt e-invoices by 1 July 2025. Note: There was an accommodative Budget 2024 allocation of MYR100m for digitalisation grants – offering up to MYR5k for more than 20k MSMEs – as well as a MYR900m loan fund under Bank Negara Malaysia established to encourage automation and digitalisation among SMEs.

Figure 2: E-Invoice implementation timeline



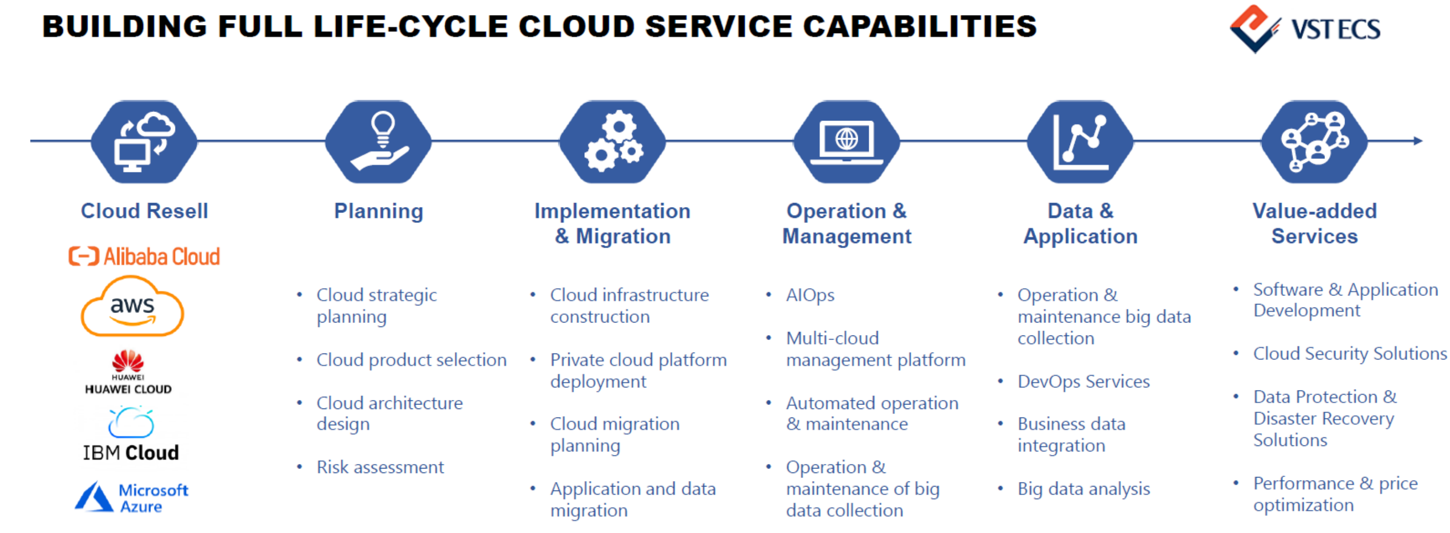
Source: Company data

Technological advancements. Delays in the implementation of enterprise systems projects seen in 9M23 should spill-over into growth in FY24, in our view. This is on top of the growing momentum in major networking infrastructure on the back of the 5G rollout and increasing need for cyber security and cloud computing & services – this is with the mushrooming of various data centres in Malaysia. Both the public and private sectors are expected to continue their usual technology refresh and upgrades on top of the digitalisation trend push by the Government and hyper-scalers. Besides, VSTECS is now venturing into supplying power solutions to data centres to capture the increasing investments in such centres in Malaysia – the group has the distribution rights for Schneider Electric's uninterruptible power supply solutions and offerings.

Growing recurring income from software & IT solutions. VSTECS distributes cloud computing and services including established brands like IBM, Microsoft Azure, Huawei Cloud, AWS, and Alibaba Cloud. Supported by its broad products range, growing cloud subscription, and managed services under the ICT services segment will increase recurring services revenue and provide further earnings visibility, in our view.

VSTECS was also the first local player to facilitate Alibaba Cloud's first private cloud programme with the Sarawak State Government. It also managed to made significant headway into the SME segment via various industries. VSTECS' cloud team, parked under the ICT services unit, is now expected to generate profits in FY24 after a 2-year incubation period and is aiming to grow the segment to reach 5% of group revenue by FY26. Associate firm ISATEC – which focuses on software & IT Solutions in application development, digital workflow, system consulting, cloud computing and process automation – is also gaining traction with various successful end-to-end business process automation application such as KUBE 365.

Figure 3: Cloud service capabilities



Source: Company data

Figure 4: ISATEC's solutions

ISATEC Sdn. Bhd. Is an associate company of VSTECS, a USD 7.9 billion public listed Information Technology group with 53 offices in 6 countries across Asia-Pacific.

Enterprise Software Development

We design and build custom applications, workflow solutions for enterprise collaboration, and mobile application software to meet enterprise needs.

We are a team of business analysts, architects and developers who love to take on complex projects using a wide range of vendor technologies, platforms and tools.

What sets us apart is our passion to deliver a quality product every time!

We have also built Award winning products that have won the hearts of hundreds of customers worldwide. Check them out below:

KUBE | justSAMit | SAMLite asset lifecycle management | ENDORZE

Source: Company data

Valuation re-rating. VSTECS has delivered profits since listing, thanks to its operating efficiency, broad range of established ICT products brands, and experienced management team. The group has also consistently paid dividends every year since its IPO. In the past three years, its dividend payout ratio ranged between 33% and 37%.

Besides the growing competency in its SaaS model, full life-cycle cloud service capabilities, and ever-growing enterprise segment as re-rating catalyst, it also offers a dividend yield of c.5% and mid-teens ROEs. Coupled with a net cash position (MYR71.7m or MYR0.19 per share as at 3Q23), we believe VSTECS' current valuation is unfair when compared with its international and local indirect peers. It is also worth noting that the group has a net cash of MYR396.3m (83% of market capitalisation) after taking into account the working capital positions.

Note: VSTECS' international peer involved in the ICT products distribution and enterprise system businesses here – TD SYNNEX (SNX US, NR) – has a higher net gearing ratio and lower net margin of 1%. SNX trades at a 9.6x P/E multiple on the NYSE. Local ICT products, solutions and system integrator players (who are also VSTECS' clients) such as Cloudpoint Technology, Heitech Padu, Infoline Tec Group, Infomina, Mesiniaga, and SNS Network are currently trading at range of 9-20x P/E multiples vs the group's forward P/E multiple of merely 7x. We consider this unwarranted, given that VSTECS supplies ICT products and enterprise system to these players and commands a considerable market share.

Financial Overview And Valuation

Results highlights. In the last four years, VSTECS has shown a gradual improvement in core earnings with CAGR (2019-2022) of 26.3%. The earnings breakout was mainly attributed to the group's capabilities in distributing ICT products, expansion in enterprise system business, and surging demand of ICT products during the COVID-19 movement control order (MCO). VSTECS benefitted from surging pent-up demand for laptops and computers, and expedition of digitalisation efforts during the MCO's work and study from home trend. During FY22, VSTECS was able to sustain earnings – mainly attributed to higher revenue from enterprise systems segment with more project transactions, which also fetches better margin. There were higher demand for commercial notebook, networking hardware and software, as well as cloud services.

However, 9M23 revenue dipped 8% YoY to MYR1.9bn, mainly due to slowdown in consumer market but was partly mitigated by higher sales from the ICT services segment. 9M23 GP margin expanded 0.5ppts to 5.8% due to lower sales contribution from ICT distribution segment (-22.3% YoY). QoQ, 3Q23 sales rose 6.2% to MYR646.4m, thanks to better seasonality – as 2H benefits from seasonal consumer buying behaviour, with consumers and enterprises tend to utilise their budgets towards the end of the year. That said, 3Q23 core earnings dipped 18.7% QoQ because of higher impairment of financial instruments and lower FX gain.

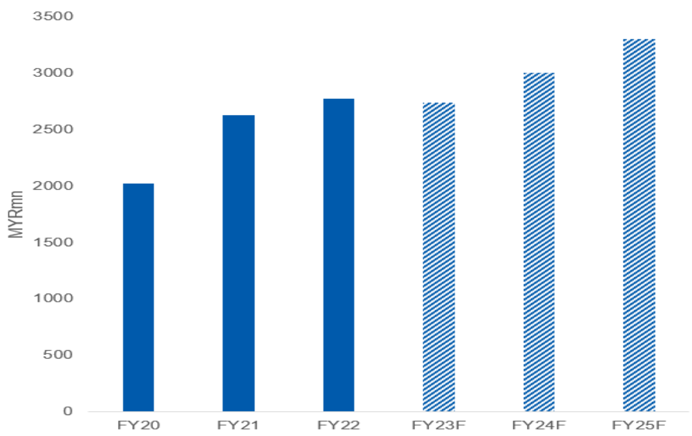
Strong net cash position. VSTECS has been in a net cash position since 2010. The group has a healthy balance sheet with net cash of MYR71.7m or MYR0.15 per share as at 3QFY23. We expect it to remain in a net cash position for FY22-24F.

ROE. Over the past three years, its ROE ranged between 10% and 16%. With the expected increase in FY23-25 earnings, we expect the group's ROE to stay within this range.

Dividends. While it does not have a dividend policy, VSTECS has a track record of paying dividends. From FY20-22, dividends per share ranged from 3.5-6.2 sen – reflecting its strong balance sheet. It intends to distribute dividends of 33% of its annual PATAMI going forward. Hence, we forecast dividend yields of 4.8-5.7% from FY23-25.

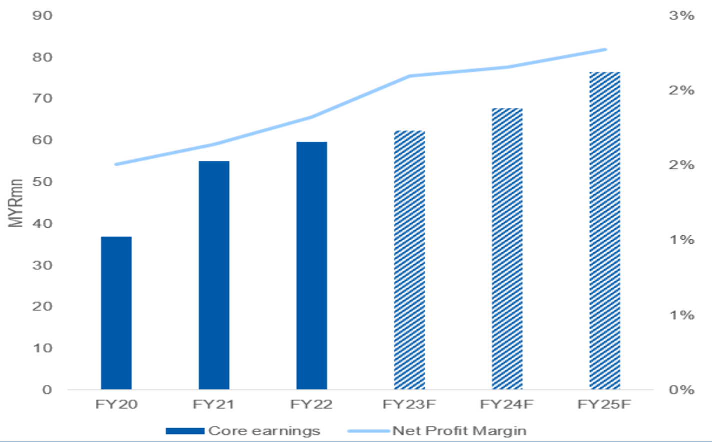
Earnings forecasts. We forecast a 3-year earnings CAGR of 8.6%, supported by expansion of product range, expansion of distribution channels, increasing solution services, and Government's digitalisation efforts. The recurring income grows from its managed services, software, and solutions to meet the surging demand for cybersecurity, AI integration, cloud services, application development, and consulting services. Besides, the 2H of the year usually benefits the group from seasonal consumer buying behaviour, with consumers and enterprises tend to utilise their budgets towards the end of the year, coupled with government initiatives, ie extension of special tax exemptions for purchase of digital devices and Budget 2023 allocations for digital enablement.

Figure 5: Revenue trends



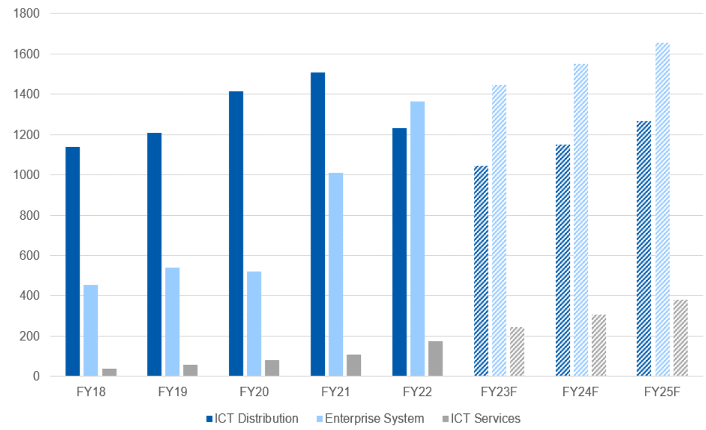
Source: Company data, RHB

Figure 6: Core profit trends



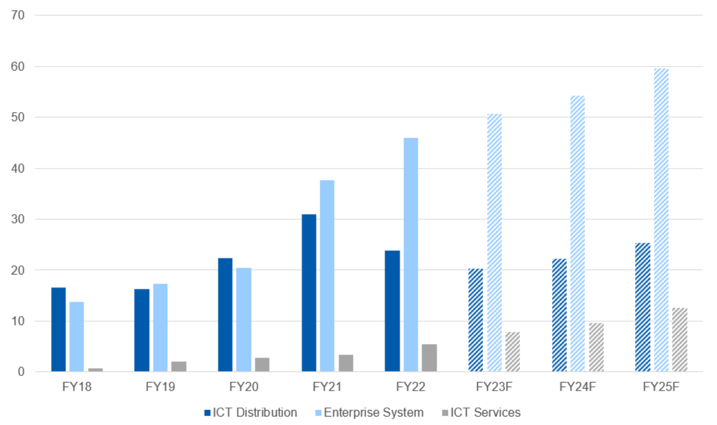
Source: Company data, RHB

Figure 7: Revenue trends by segment



Source: Company data, RHB

Figure 8: PBT trends by segment



Source: Company data, RHB

Fair value. We ascribe a 10x target P/E, which is still at a discount to VSTECS' local and international ICT products distribution, solutions peers, and system integrators – they are trading at a range of 10-20x – as well as its average historical 5-year P/E of 10x-12x. We like the stock for its market-leading position, strong relationships with 46 major ICT brands, and wide sales channel (4,600+ resellers) and support systems (logistics, credit terms, and consulting and services).

While we acknowledge that margins are on the lower end, it is the nature of the trading business and serves as a stumbling block for new entrants. Management's strong track record in deliver growth and consistent cash flow generation are the other attributes we admire. Notably, the growing competency in its SaaS model, full life-cycle cloud service capabilities, and ever-growing enterprise segment are the re-rating catalysts on top of a dividend yield of c.5% and mid-teen ROEs.

Figure 9: Peer tables

Company	Country	FYE	Mkt cap (USDm)	Price 28-Dec-22 (Local currency)	P/E (x) Actual	P/E (x) 1-yr fwd	P/E (x) 2-yr fwd	Div. yld (%) 1-yr fwd	ROE (%) 1-yr fwd	EV/ EBITDA 1-yr fwd	NP growth (%) 1-yr fwd	NP growth (%) 2-yr fwd
VSTECS	MA	Dec	100	1.31	7.9	7.6	7.0	5.5	15.2	3.4	4.4	8.9
Local peers												
Cloudpoint Technology	MA	Dec	61.6	0.54	20.6	16.9	13.7	0.0	81.0	11.0	21.6	23.4
Datasonic Group	MA	Mar	255.6	0.42	14.9	15.3	15.5	4.8	21.6	8.5	-2.9	-1.3
Microlink Solutions	MA	Mar	203.3	0.88	34.9	19.9	18.4	NA	20.2	15.9	75.8	8.1
SNS Network Technology	MA	Jan	83.9	0.24	8.5	NA	NA	NA	NA	NA	NA	NA
Iris Corp	MA	Mar	53.0	0.08	10.8	NA	NA	NA	NA	NA	NA	NA
Kronologi Asia	MA	Jan	77.0	0.40	13.8	27.5	13.0	NA	3.1	NA	-49.7	111.5
Omesti	MA	Mar	34.6	0.30	1.2	NA	NA	NA	NA	NA	NA	NA
Infoline Tec Group	MA	Dec	58.2	0.74	21.1	14.6	11.4	2.7	37.0	9.8	44.9	27.4
Dataprep Holdings	MA	Dec	22.4	0.14	-5.7	NA	NA	NA	NA	NA	NA	NA
Mesiniaga	MA	Dec	18.2	1.39	12.3	NA	NA	NA	NA	NA	NA	NA
Heitech Padu	MA	Dec	19.1	0.87	-8.5	NA	NA	NA	NA	NA	NA	NA
Infomina	MA	May	220.2	1.69	24.7	22.4	20.0	NA	40.6	14.7	10.1	12.1
Market cap weighted average			**163.0**		**19.1**	**19.3**	**16.7**	**3.7**	**29.6**		**19.4**	**17.8**
Simple average			**92.3**		**12.4**	**19.4**	**15.4**	**2.5**	**33.9**		**16.6**	**30.2**
International peers												
TD SYNNEX	US	Nov	10013.6	108.43	15.4	9.9	9.6	1.3	12.6	7.4	55.3	3.2
Arrow Electronics	US	Dec	6644.3	122.68	4.7	6.9	8.7	N/A	17.2	6.0	-32.5	-21.0
Avnet	US	Jun	4591.2	50.74	6.0	8.6	7.7	2.4	11.2	6.9	-30.9	11.4
Resideo Technologies	US	Dec	2772.8	18.98	9.8	13.8	11.7	N/A	7.9	7.3	-29.1	18.2
ScanSource	US	Jun	1003.2	39.93	11.2	10.7	9.6	N/A	10.3	7.2	4.1	11.9
Wayside Technology Group	US	Dec	N/A	N/A	N/A	N/A	N/A	N/A	16.4	N/A	-18.6	41.1
Bsquare	US	Dec	37.6	1.89	-9.7	N/A	N/A	N/A	N/A	N/A	N/A	N/A
Taitron Components	US	Dec	20.8	3.46	6.5	N/A	N/A	N/A	N/A	N/A	N/A	N/A
Market cap weighted average			**6944.6**		**10.0**	**9.3**	**9.3**	**1.7**	**13.0**	**7.0**	**4.8**	**0.3**
Simple average			**3583.4**		**6.2**	**10.0**	**9.5**	**1.9**	**12.6**	**7.0**	**-8.6**	**10.8**

Source: Bloomberg, RHB

Figure 10: Operating metrics

Company	Revenue 3-year CAGR	Net profit 3-year CAGR	Gross profit margin	EBITDA margin	Net profit margin	Net gearing (latest)
VSTECS	15.4%	26.3%	5.4%	2.9%	2.2%	Net Cash
Local Peers						
Cloudpoint Technology	21.4%	26.3%	27.3%	19.8%	14.5%	Net Cash
Datasonic Group	16.2%	27.9%	54.9%	42.6%	22.2%	Net Cash
Microlink Solutions	9.2%	209.8%	28.7%	19.2%	10.4%	Net Cash
SNS Network Technology	33.2%	68.7%	7.8%	5.4%	3.1%	Net Cash
Iris Corp	15.0%	-17.0%	24.0%	15.8%	6.3%	Net Cash
Kronologi Asia	10.1%	9.6%	19.6%	18.1%	7.8%	Net Cash
Omesti	-22.8%	-290.6%	36.5%	-4.4%	108.9%	22.47
Infoline Tec Group	32.9%	50.5%	36.1%	23.3%	16.6%	Net Cash
Dataprep Holdings	-9.7%	13.5%	24.0%	-41.9%	-61.6%	Net Cash
Mesiniaga	-2.3%	-294.8%	N/A	2.2%	2.2%	Net Cash
Heitech Padu	-6.6%	-209.9%	N/A	2.3%	-3.4%	83.80
Infomina	56.1%	79.4%	29.0%	19.9%	15.9%	Net Cash
Market cap weighted average	**22.5%**	**52.9%**	**33.1%**	**21.2%**	**15.1%**	
Simple average	**12.7%**	**-27.2%**	**28.8%**	**10.2%**	**11.9%**	
International Peers						
TD SYNNEX	37.9%	9.5%	6.3%	2.6%	1.0%	49.89
Arrow Electronics	8.7%	-291.2%	13.0%	6.3%	3.8%	69.37
Avnet	10.8%	63.5%	12.0%	5.1%	2.9%	63.41
Resideo Technologies	8.5%	98.8%	27.7%	13.1%	4.4%	51.13
ScanSource	5.2%	16.0%	11.9%	4.5%	2.4%	33.96
Wayside Technology Group	13.4%	21.5%	17.8%	6.5%	4.0%	Net Cash
Bsquare	-14.9%	-25.1%	14.9%	-9.5%	-10.6%	Net Cash
Taitron Components	7.5%	60.7%	52.2%	28.1%	38.1%	Net Cash
Market cap weighted average	**20.5%**	**-50.5%**	**11.8%**	**5.3%**	**2.6%**	
Simple average	**9.7%**	**-5.8%**	**21.2%**	**7.3%**	**5.2%**	

Source: Bloomberg, RHB

Company Overview

VSTECS is a leading distribution hub for ICT products in Malaysia. The group purchases hardware and software from multiple international leading ICT principals ie HP, Cisco, and Microsoft, and distributes them to resellers – typically comprising of system integrators, solutions providers, service providers, corporate dealers, and retailers. Some of the products commonly purchased by resellers include PCs, notebooks, smartphones, tablets, printers, software, network and communication infrastructure, servers, and enterprise software.

The group's business segments comprise of the following:

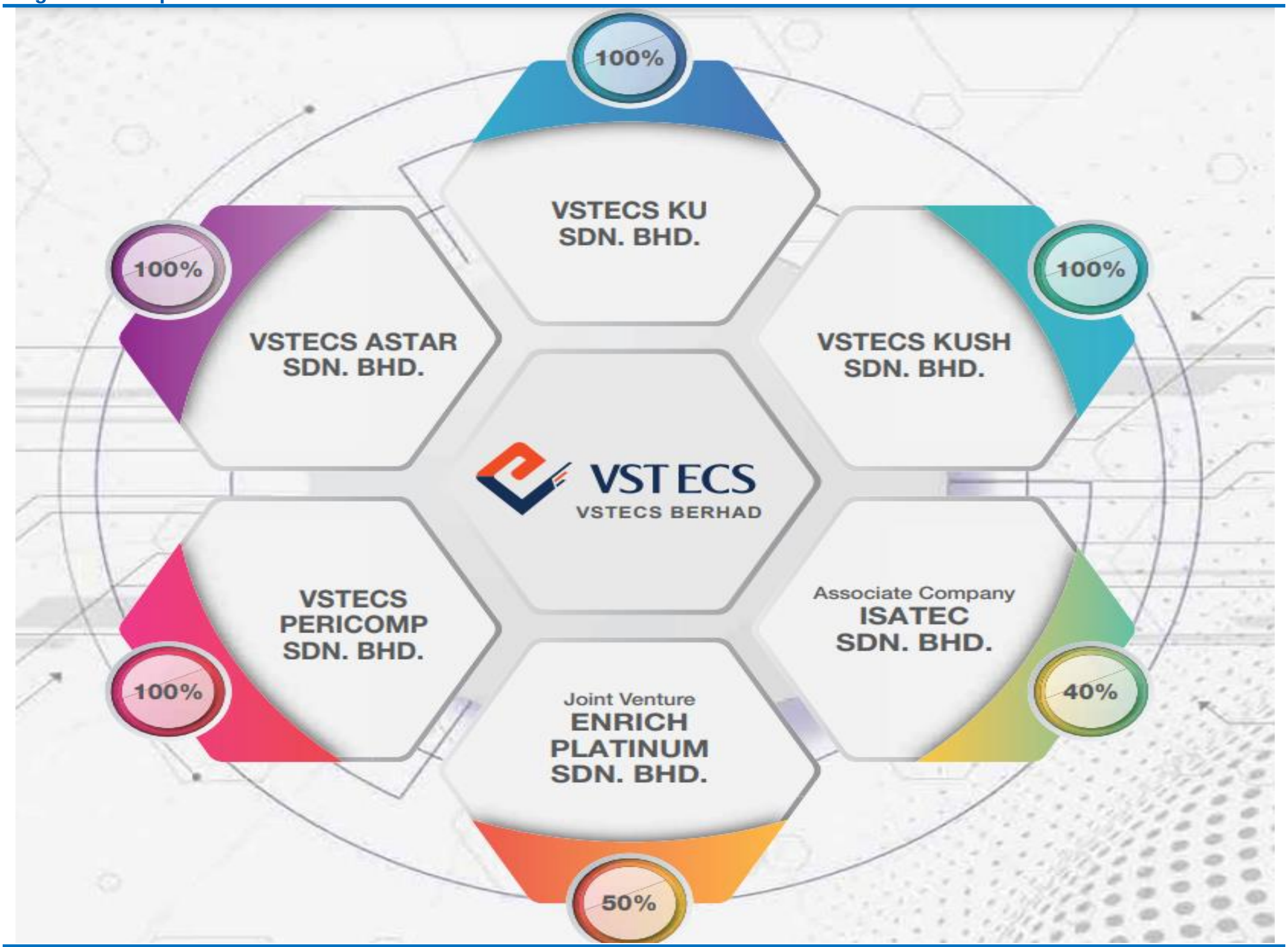
i. **ICT distribution (44.4% of FY22 revenue):** Distribution of volume ICT products to resellers, comprising mainly of retailers;

ii. **Enterprise systems (49.3% of FY22 revenue):** Distribution of enterprise ICT products to resellers, comprising mainly of system integrators and corporate dealers;

iii. **ICT services (6.3% of FY22 revenue):** Provisioning of ICT systems and services.

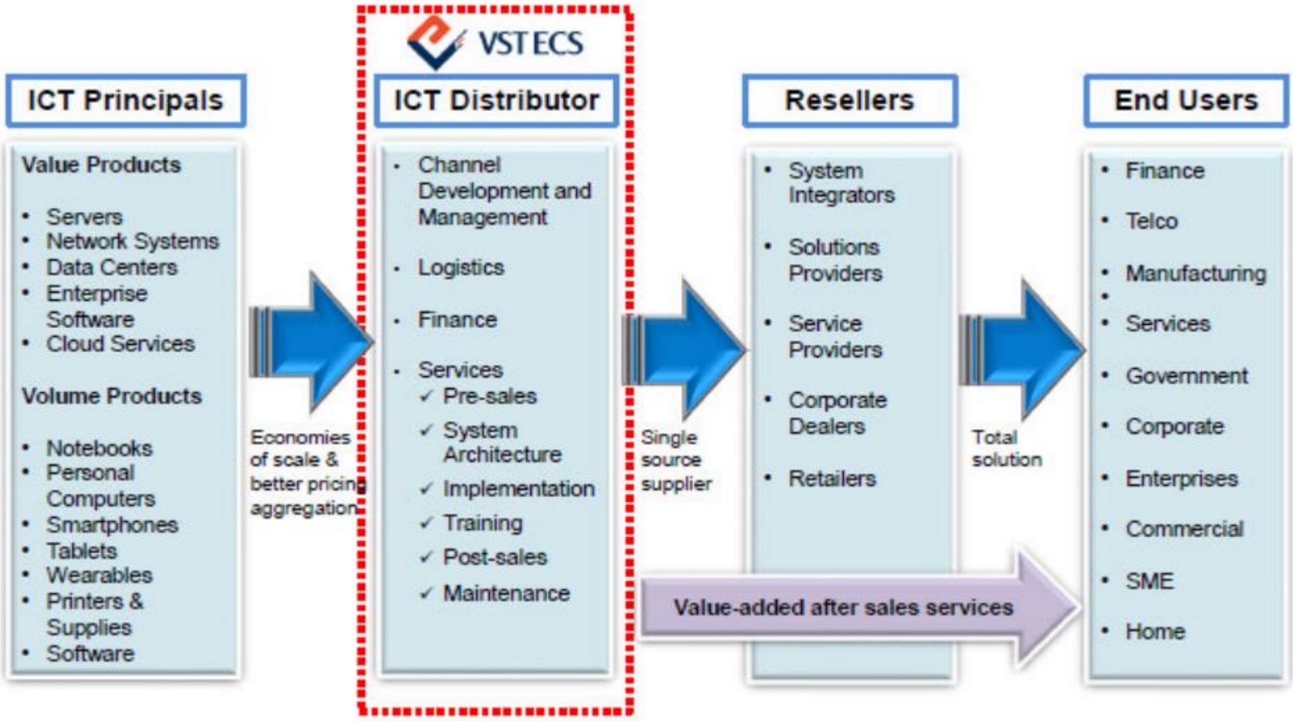
VSTECS is led by an experienced management team. CEO Soong Jan Hsung contributed significantly to the group in becoming the leading ICT hub in Malaysia. Chan Puay Chai, the group CFO, has over 20 years experiences in financial planning and control, financial compliances, credit management, risk management, and other financial and management related functions. They are supported by the rest of the senior management team, who all have over 20 years of experience in the field.

Figure 11: Corporate structure



Source: Company data

Figure 12: Business model



Source: Company data

Figure 13: ICT products

Source: Company data

Key Risks

Business failure of ICT principals. As a distributor, VSTECS faces the risk of losing distributorship from its ICT principals, ie HP, Dell, Alibaba Cloud, and Microsoft Azure. However, we think the risk of losing distributorship is unlikely to happen in the near term as VSTECS has been working very well with its principals, with some even providing the group with higher market share in Malaysia in terms of stocks compared to other companies. To mitigate the risk, VSTECS will continue to maintain good business relationship with its principals, and capabilities in distribution and after-sales services.

Slower-than-expected adoption of ICT. A slower-than-expected adoption of ICT in Malaysia could also slacken VSTECS' growth in ICT products and enterprise system businesses. In the current high interest rate environment, some enterprises might pause or slow the pace of digitalising business processes. On a brighter note, this could partly be offset by the hybrid working environment, awareness of cybersecurity importance, increasing need of data storage, and the arrival of 5G services. To mitigate the risk, VSTECS monitors government initiatives and the macro environment closely, and reacts swiftly to the demands of the market.

Slowdown of consumer demand for ICT products. We do see a slowdown in consumer demand for ICT products like laptop and computers as most consumers and enterprises have already bought new devices during the pandemic to cater to the work and study from home trend. The risk is inevitable and might impact VSTECS' ICT distribution business (top revenue generator) if not managed properly. Luckily, in the current year, the group managed to obtain a large share from government initiatives, especially in the education sector. Going forward, VSTECS will work closely with the Government in digitalisation-related initiatives.

Exposure to FX risk. As a distributor, VSTECS usually earns a fixed margin in MYR, depending on the volume and quantity regardless of the FX fluctuation, except for c.26% of inventory purchased in USD. To mitigate the FX risk, the group practises hedging forward its USD-denominated purchases by fixing the currency exchange rates on payment due dates or purchasing forward currency contracts. This practice ensures stability in the costing of its trade purchases irrespective of currency market fluctuations. Historically, VSTECS managed to navigate through the appreciation of USD environment (in 2016 and 2017), when the USD rose to USD4.6/MYR and the group still achieved GPM of 3.8% in its distribution of ICT products segment.

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