

30 May 2023

## LGMS

### A Soft Patch, Growth Prospects Intact

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LGMS's 1QFY23 results disappointed on weak project deliveries and higher staff cost arising from increased headcount pursuant to business expansion. Nonetheless, we believe the prospects for cybersecurity service in Southeast Asia remain bright, underpinned by rising adoption of digitalisation amongst businesses and financial institutions. We moderate our FY24-25F net profit forecasts by 11% and 10%, respectively, trim our TP by 12% to RM1.32 (previously RM1.50) but maintain our OUTPERFORM call.

**Below expectations.** LGMS's 1QFY23 earnings of RM1.6m (-46.9% YoY) missed expectations, coming in at only 10% of both our full-year forecast and the full-year consensus estimate. The variance against our forecast came largely from weak revenue recognition and higher operating cost.

**Results' highlights.** YoY, 1QFY23 revenue dipped 20.9% on lower revenue recognition of projects due to lower number of working days in the quarter as a result of long festive breaks. Additionally, the group's seasonality was in play where customers typically exhaust most of their IT budget before starting a new year. The decline was seen across all business segments with the cyber risk management and compliance segment and cyber threat segment falling by double digits. Not helping either, the group saw an untimely uptick in employee benefit expenses as the group expanded its headcount in anticipation for future expansion. As a result, gross profit margins shrank to 30.6% (vs. 54.1%), which led to a 46.9% decline in net profit.

**Still anticipating growth.** The cyber threat landscape continues to evolve with the rapid adoption of 5G and new IT infrastructures, evidenced by the rise in ransomware attacks and cybersecurity challenges. Therefore, we remain sanguine of the continuous increase in demand from the growing addressable market in Malaysia and Southeast Asia. LGMS is venturing into neighbouring countries where cybersecurity awareness is still at the infancy stage. The group is looking to quickly expand its presence in the region to leverage on the increasing awareness as businesses are beginning to prioritise cybersecurity as part of their digital transformation efforts.

**Forecasts.** We reduce our FY23F-24F earnings forecasts by 11% and 10%, respectively.

We moderate our TP by 12% to RM1.32 (from RM1.50) based on an unchanged 25x FY24F PER, in line with peers' forward mean. There is no adjustment to our TP based on ESG given a 3-star rating as appraised by us (see Page 4).

**Investment thesis.** We like LGMS for its: (i) unique exposure to the growing cybersecurity business, (ii) the deep moat around its business given the high barrier to entry created by the tough qualification process as a vendor, and (iii) new proprietary certification software which is expected to be the next earnings driver. Maintain **OUTPERFORM**.

**Risks to our call include:** (i) longer-than-expected gestation period for its regional expansions, (ii) economic downturn resulting in customer lowering budget allocated for cybersecurity, (iii) reluctance to spend on cybersecurity services due to the lack of knowledge and awareness in emerging countries, and (iv) failure to maintain the extensive list of accreditations due to potential loss of critical talent.

## OUTPERFORM ↔

Price: **RM1.10**  
Target Price: **RM1.32** ↓

### Share Price Performance



KLCI 1,404.9  
YTD KLCI chg -6.1%  
YTD stock price chg -2.7%

### Stock Information

Shariah Compliant	Yes
Bloomberg Ticker	LGMS MK Equity
Market Cap (RM m)	501.6
Shares Outstanding	456.0
52-week range (H)	1.45
52-week range (L)	0.57
3-mth avg daily vol:	905,536
Free Float	52.9%
Beta	1.8

### Major Shareholders

Fong Choong Fook	53.8%
Go Soon Sei	16.1%
UBS AG	4.2%

### Summary Earnings Table

FY Dec (RM m)	2022A	2023F	2024F
Turnover	32.8	39.3	67.0
EBITDA	17.0	19.9	33.2
PBT	15.6	18.5	31.5
Core NP (CNP)	12.6	14.2	24.2
Consensus (NP)	n.a	15.9	27.0
Earnings Revision	n.a	-11%	-10%
EPS (sen)	2.8	3.1	5.3
EPS growth (%)	22.6	12.0	70.6
NDPS (sen)	0.0	0.0	0.0
BVPS (RM)	0.18	0.21	0.27
Price/BV (x)	6.0	5.1	4.1
PER (x)	39.7	35.4	20.8
Net Gearing (x)	0.0	0.0	0.0
ROA (%)	13.8	13.0	17.4
ROE (%)	15.1	14.5	19.8
Dividend Yield (%)	0.0	0.0	0.0



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Result Highlight								
	1Q	4Q	QoQ	1Q	YoY	3M	3M	YoY
FYE Dec (RM m)	FY23	FY22	Chg	FY22	Chg	FY23	FY22	Chg
<b>Revenue</b>	<b>6.2</b>	<b>9.0</b>	<b>-31.1%</b>	<b>7.8</b>	<b>-20.9%</b>	<b>6.2</b>	<b>7.8</b>	<b>-20.9%</b>
GP	1.9	5.2	-63.4%	4.2	-55.2%	1.9	4.2	-55.2%
EBIT	2.2	4.3	-48.1%	4.2	-47.8%	2.2	4.2	-47.8%
PBT	2.2	4.2	-48.4%	4.2	-48.1%	2.2	4.2	-48.1%
Taxation	-0.5	-1.0	45.2%	-1.1	51.3%	-0.5	-1.1	51.3%
Net Profit (NP)	1.6	3.2	-49.4%	3.1	-46.9%	1.6	3.1	-46.9%
<b>Core NP</b>	<b>1.6</b>	<b>3.2</b>	<b>-49.4%</b>	<b>3.1</b>	<b>-46.9%</b>	<b>1.6</b>	<b>3.1</b>	<b>-46.9%</b>
EPS (sen)	0.4	0.7	-49.4%	0.7	-46.9%	0.4	0.7	-46.9%
DPS (sen)	0.0	0.0		0.0		0.0	0.0	
GP margin	30.6%	57.5%		54.1%		30.6%	54.1%	
EBIT margin	35.6%	47.3%		54.0%		35.6%	54.0%	
Pretax margin	35.2%	47.0%		53.6%		35.2%	53.6%	
CNP margin	26.4%	36.0%		39.4%		26.4%	39.4%	
Effective tax rate	-24.9%	-23.4%		-26.5%		-24.9%	-26.5%	

Source: Kenanga Research

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## Malaysian Technology Peers Comparison

Name	Rating	Last Price (RM)	Target Price (RM)	Upside (%)	Mkt Cap (RM'm)	Shariah Compliant	Current FYE	Core EPS (sen)		Core EPS Growth		PER (x) – Core Earnings		PBV (x)	ROE (%)	Net Div. (sen)	Net Div. Yld (%)
								1-Yr. Fwd.	2-Yr. Fwd.	1-Yr. Fwd.	2-Yr. Fwd.	1-Yr. Fwd.	2-Yr. Fwd.	1-Yr. Fwd.	1-Yr. Fwd.	1-Yr. Fwd.	1-Yr. Fwd.
D&O GREEN TECHNOLOGIES BHD	UP	3.89	2.68	-31.11%	4,815.1	Y	12/2023	7.8	10.7	-1.0%	37.9%	50.0	36.3	5.2	10.7%	1.3	0.3%
GHL SYSTEMS BHD	OP	0.800	1.05	31.25%	907.5	Y	12/2023	3.0	3.4	21.3%	12.9%	26.7	23.7	1.7	6.5%	0.0	0.0%
INARI AMERTRON BHD	MP	2.47	2.46	-0.40%	9,220.3	Y	06/2023	9.0	10.2	-14.1%	13.1%	27.5	24.3	3.7	13.3%	8.6	3.5%
JHM CONSOLIDATION BHD	MP	0.740	0.800	8.11%	445.4	Y	12/2023	5.3	5.9	40.0%	10.6%	13.9	12.6	1.3	9.8%	0.5	0.7%
KELINGTON GROUP BHD	OP	1.40	1.92	37.14%	900.2	Y	12/2023	8.7	9.0	1.1%	3.2%	16.1	15.6	3.2	21.3%	2.4	1.7%
KESM INDUSTRIES BHD	MP	7.00	6.91	-1.29%	301.1	Y	07/2023	(15.8)	1.2	-3500.0%	-92.6%	N.A.	565.0	0.9	-1.9%	7.5	1.1%
LGMS BHD	OP	1.10	1.32	20.00%	501.6	Y	12/2023	3.1	5.3	12.7%	70.4%	35.4	20.8	5.1	15.7%	0.0	0.0%
M'SIAN PACIFIC INDUSTRIES BHD	UP	27.12	15.26	-43.73%	5,394.1	Y	06/2023	41.8	105.8	-74.7%	153.3%	64.6	25.6	2.7	4.1%	35.0	1.3%
NATIONGATE HOLDINGS BHD	OP	1.23	1.40	13.82%	2,550.9	Y	12/2023	5.0	6.1	20.4%	22.8%	24.7	20.1	7.8	37.1%	0.3	0.2%
OPPSTAR BHD	MP	2.00	1.82	-9.00%	1,272.4	N	03/2024	4.5	6.1	34.0%	36.3%	44.8	32.9	8.1	19.3%	1.1	0.6%
P.I.E. INDUSTRIAL BHD	OP	3.29	4.05	23.10%	1,263.5	Y	12/2023	22.5	25.3	22.0%	12.5%	14.6	13.0	2.0	14.6%	7.0	2.1%
SKP RESOURCES BHD	UP	1.02	1.20	17.65%	1,593.6	Y	03/2023	9.7	7.9	-11.1%	-17.9%	10.5	12.9	1.8	17.8%	4.8	4.7%
UNISEM (M) BHD	MP	2.99	2.75	-8.03%	4,823.1	Y	12/2023	8.9	13.8	-41.2%	55.7%	19.4	17.4	2.0	5.9%	6.0	2.0%
Simple Average										-24.2%	28.7%	29.4	22.8	3.5	13.4%		1.4%

Source: Kenanga Research

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**Stock ESG Ratings:**

	Criterion	Rating				
<b>GENERAL</b>	Earnings Sustainability & Quality	★	★	★		
	Corporate Social Responsibility	★	★	★		
	Management/Workforce Diversity	★	★	★	☆	
	Accessibility & Transparency	★	★	★		
	Corruption-Free Pledge	★	★	★		
	Carbon-Neutral Initiatives	★	★	☆		
<b>SPECIFIC</b>	Occupational Health & Safety	★	★	★	★	
	Protection of Customer Data	★	★	★	★	
	Cybersecurity	★	★	★	★	
	Energy Efficiency	★	★	★		
	Digital Transformation	★	★	★		
<b>OVERALL</b>		★	★	★		

☆ denotes half-star  
 ★ -10% discount to TP  
 ★★ -5% discount to TP  
 ★★★ TP unchanged  
 ★★★★ +5% premium to TP  
 ★★★★★ +10% premium to TP

**Stock Ratings are defined as follows:****Stock Recommendations**

OUTPERFORM : A particular stock's Expected Total Return is MORE than 10%  
 MARKET PERFORM : A particular stock's Expected Total Return is WITHIN the range of -5% to 10%  
 UNDERPERFORM : A particular stock's Expected Total Return is LESS than -5%

**Sector Recommendations\*\*\***

OVERWEIGHT : A particular sector's Expected Total Return is MORE than 10%  
 NEUTRAL : A particular sector's Expected Total Return is WITHIN the range of -5% to 10%  
 UNDERWEIGHT : A particular sector's Expected Total Return is LESS than -5%

**\*\*\*Sector recommendations are defined based on market capitalisation weighted average expected total return for stocks under our coverage.**

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