

**HLIB Research**

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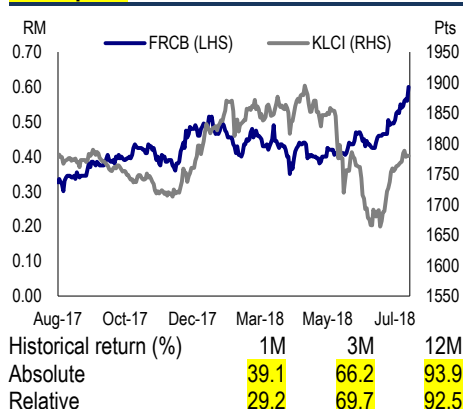
**BUY** (Maintain)

**Target Price:** **RM1.05**
**Previously:** **RM1.05**
**Current Price:** **RM0.83**

|                       |       |
|-----------------------|-------|
| Capital upside        | 26.5% |
| Dividend yield        | 2.6%  |
| Expected total return | 29.1% |

**Sector coverage:** Technology

**Company description:** Frontken is a leading surface engineering service provider in semiconductor and O&G markets.

**Share price**

**Stock information**

|                              |         |
|------------------------------|---------|
| Bloomberg ticker             | FRCB MK |
| Bursa code                   | 0128    |
| Issued shares (m)            | 1,048   |
| Market capitalisation (RM m) | 671     |
| 3-mth average volume ('000)  | 6,960   |
| SC Shariah compliant         | Yes     |

**Major shareholders**

|                         |       |
|-------------------------|-------|
| Dazzle Clean            | 27.8% |
| Ooi Keng Thye           | 14.5% |
| CIMB Group Holdings Bhd | 5.8%  |

**Earnings summary**

|                     | FY17 | FY18f | FY19f |
|---------------------|------|-------|-------|
| FYE (Dec)           |      |       |       |
| PATMI – core (RM m) | 34.3 | 45.5  | 55.0  |
| EPS – core (sen)    | 3.3  | 4.3   | 5.2   |
| P/E (x)             | 25.5 | 19.2  | 15.9  |

# Frontken Corporation

## 3Q18 results: Another record high

Another magnificent quarter as 3Q18 performance lifted 9M18 core net profit to RM35m (+48% YoY) which meets expectations. Declared single dividend of 0.7 sen per share. This outstanding performance was mainly driven by stronger semiconductor contribution while O&G exhibited resiliency with second consecutive quarterly profit in 3Q18. Forecasts were unchanged. Reiterate BUY with unchanged TP of RM1.05.

**Within expectations.** 9M18 revenue of RM239m was translated into a core net profit of RM35m, accounting for 77% of HLIB and street full year forecasts, respectively. 3Q18 results were another all-time high achievement in terms of sales and profitability after outdid its own 2Q18 record performance.

**Dividend.** Declared an interim single dividend of 0.7 (3Q17: none) sen per share. YTD dividend amounted to 0.7 (9M17: 0.5) sen per share.

**QoQ.** Turnover increased 5% to reach RM86m thanks to higher contributions from Taiwan, Malaysia, Singapore and Philippines. This expansion is mainly driven by the semiconductor business segment. After one-off adjustments, core net profit grew 17% to RM15m attributable to lower effective corporate tax rate of 20% vs. 2Q18's 32%.

**YoY.** Top line gained 9% attributable to the growth from semiconductor business, where Taiwan and Singapore improved 4% and 11%, respectively. Malaysia and Philippines also recorded a better performance due to new works secured in light of recovery in the O&G industry. As a result, core earnings ballooned 50% on the back of O&G's turnaround and lower MI with increased stake in AGTC.

**YTD.** Revenue accelerated 10% supported by Taiwan (+12%), Malaysia (+12%) and Singapore (+8%) leveraging on stronger semiconductor demand. After excluding non-core items, bottom line gained 48% to RM35m for the same reason mentioned above.

**O&G recovery.** Record second consecutive quarterly profit with RM1.3m in 3Q18 bringing YTD PAT to RM0.8m. We believe the turnaround story remains intact and this performance is sustainable going forward considering Brent crude price remains stable at high levels.

**Management's prospects.** In view of the encouraging industry forecast, Frontken anticipates that the overall business conditions for 4Q18 to be positive. It will also continue to be vigilant in its cost management and strive to improve on its efficiency. Its priority is to focus on quality to maintain competitiveness.

**Forecast.** Maintain as results were in line.

Reiterate **BUY** with unchanged fair value of **RM1.05**, pegged to 20x of FY19 EPS. We think Frontken is expected to experience multi-year growth ahead on the back of (1) bullish global semiconductor market outlook; (2) robust fab investment (3) leading edge technology; (4) O&G recovery; and (5) strong balance sheet.

## Financial Forecast

All items in (RM m) unless otherwise stated

### Income statement

| FYE Dec             | FY16        | FY17        | FY18f       | FY19f       | FY20f       |
|---------------------|-------------|-------------|-------------|-------------|-------------|
| Revenue             | 261.8       | 296.6       | 331.7       | 374.4       | 402.8       |
| COGS                | (210.9)     | (231.9)     | (248.7)     | (278.8)     | (299.3)     |
| EBITDA              | 50.9        | 64.7        | 83.0        | 95.5        | 103.5       |
| D&A                 | (17.2)      | (18.5)      | (17.2)      | (16.4)      | (15.7)      |
| EBIT                | 33.7        | 46.2        | 65.8        | 79.1        | 87.8        |
| Net Interest Income | (0.4)       | (0.1)       | 0.0         | 0.3         | 0.5         |
| Associates          | 0.0         | 0.0         | 0.0         | 0.0         | 0.0         |
| PBT                 | 33.3        | 46.1        | 65.9        | 79.4        | 88.3        |
| Tax                 | (6.1)       | (9.7)       | (15.5)      | (18.7)      | (20.8)      |
| Net Profit          | 27.3        | 36.4        | 50.4        | 60.7        | 67.6        |
| MI                  | (7.2)       | (6.6)       | (4.9)       | (5.7)       | (6.2)       |
| PATAMI              | 20.0        | 29.9        | 45.5        | 55.0        | 61.4        |
| Exceptionals        | (2.2)       | 4.4         | 0.0         | 0.0         | 0.0         |
| <b>Adj PATAMI</b>   | <b>17.8</b> | <b>34.3</b> | <b>45.5</b> | <b>55.0</b> | <b>61.4</b> |
| Basic Shares (m)    | 1,053.0     | 1,053.0     | 1,053.0     | 1,053.0     | 1,053.0     |
| Rep EPS (sen)       | 1.9         | 2.8         | 4.3         | 5.2         | 5.8         |
| Adj EPS (sen)       | 1.7         | 3.3         | 4.3         | 5.2         | 5.8         |
| Adj FD EPS (sen)    | 1.7         | 3.3         | 4.3         | 5.2         | 5.8         |

### Balance sheet

| FYE Dec                       | FY16         | FY17         | FY18f        | FY19f        | FY20f        |
|-------------------------------|--------------|--------------|--------------|--------------|--------------|
| Cash                          | 88.7         | 119.3        | 145.4        | 180.1        | 219.5        |
| Receivables                   | 96.1         | 91.7         | 109.0        | 123.1        | 132.4        |
| Inventories                   | 11.0         | 13.5         | 13.6         | 15.3         | 16.4         |
| Investment                    | 2.0          | 2.0          | 2.0          | 2.0          | 2.0          |
| PPE                           | 152.1        | 150.0        | 142.9        | 136.5        | 130.8        |
| Intangibles                   | 33.8         | 33.8         | 33.8         | 33.8         | 33.8         |
| Other Assets                  | 24.1         | 20.8         | 20.8         | 20.8         | 20.8         |
| <b>Total Assets</b>           | <b>407.8</b> | <b>431.1</b> | <b>467.5</b> | <b>511.5</b> | <b>555.7</b> |
| Payables                      | 73.5         | 79.8         | 88.6         | 99.3         | 106.6        |
| ST borrowings                 | 8.5          | 21.9         | 21.9         | 21.9         | 21.9         |
| LT borrowings                 | 20.3         | 11.5         | 11.5         | 11.5         | 11.5         |
| Other Liabilities             | 10.1         | 11.8         | 11.8         | 11.8         | 11.8         |
| <b>Total liabilities</b>      | <b>112.4</b> | <b>125.1</b> | <b>133.9</b> | <b>144.6</b> | <b>151.9</b> |
| Shareholders' Funds           | 261.6        | 281.6        | 304.3        | 331.8        | 362.5        |
| MI                            | 33.8         | 24.4         | 29.3         | 35.0         | 41.2         |
| Total S/H Equity              | 295.4        | 306.0        | 333.6        | 366.9        | 403.8        |
| <b>Ttl Liab&amp;S/H Funds</b> | <b>407.8</b> | <b>431.1</b> | <b>467.5</b> | <b>511.5</b> | <b>555.7</b> |

### Cashflow Analysis

| FYE Dec             | FY16          | FY17          | FY18f         | FY19f         | FY20f         |
|---------------------|---------------|---------------|---------------|---------------|---------------|
| EBITDA              | 50.9          | 64.7          | 83.0          | 95.5          | 103.5         |
| Tax Paid            | (6.7)         | (7.9)         | (15.5)        | (18.7)        | (20.8)        |
| WC Changes          | 1.1           | 6.9           | (8.7)         | (4.9)         | (3.2)         |
| Other               | (0.9)         | 5.3           | 0.0           | 0.3           | 0.5           |
| <b>CFO</b>          | <b>44.4</b>   | <b>69.0</b>   | <b>58.8</b>   | <b>72.2</b>   | <b>80.1</b>   |
| <b>FCF</b>          | <b>16.7</b>   | <b>48.9</b>   | <b>48.8</b>   | <b>62.2</b>   | <b>70.1</b>   |
| CAPEX (CF)          | (27.7)        | (20.2)        | (10.0)        | (10.0)        | (10.0)        |
| Acquisitions        | (7.4)         | (13.3)        | 0.0           | 0.0           | 0.0           |
| Other               | 0.1           | 1.3           | 0.0           | 0.0           | 0.0           |
| <b>CFI</b>          | <b>(35.0)</b> | <b>(32.1)</b> | <b>(10.0)</b> | <b>(10.0)</b> | <b>(10.0)</b> |
| Dividend            | 0.0           | (5.2)         | (22.7)        | (27.5)        | (30.7)        |
| Debt changes        | (14.4)        | 0.0           | 0.0           | 0.0           | 0.0           |
| Other               | (4.1)         | (3.2)         | 0.0           | 0.0           | 0.0           |
| <b>CFF</b>          | <b>(18.5)</b> | <b>(8.4)</b>  | <b>(22.7)</b> | <b>(27.5)</b> | <b>(30.7)</b> |
| <b>Net Cashflow</b> | <b>(9.1)</b>  | <b>28.6</b>   | <b>26.1</b>   | <b>34.7</b>   | <b>39.4</b>   |

### Quarterly financial summary

| FYE Dec             | 3Q18        | 4Q17        | 1Q18       | 2Q18        | 3Q18        |
|---------------------|-------------|-------------|------------|-------------|-------------|
| Revenue             | 78.6        | 80.4        | 70.9       | 81.8        | 85.9        |
| COGS                | (60.8)      | (62.0)      | (55.3)     | (58.0)      | (61.2)      |
| EBITDA              | 17.8        | 18.4        | 15.6       | 23.8        | 24.7        |
| D&A                 | (4.8)       | (4.7)       | (4.5)      | (4.3)       | (4.2)       |
| EBIT                | 13.0        | 13.7        | 11.1       | 19.5        | 20.5        |
| Net Interest Income | (0.1)       | (0.1)       | (0.1)      | 0.0         | 0.2         |
| Associates          | 0.0         | 0.0         | 0.0        | 0.0         | 0.0         |
| PBT                 | 12.9        | 13.6        | 11.0       | 19.5        | 20.6        |
| Tax                 | (2.1)       | (2.4)       | (3.8)      | (6.2)       | (4.1)       |
| Net Profit          | 10.8        | 11.3        | 7.2        | 13.3        | 16.5        |
| MI                  | (1.6)       | (1.4)       | (0.9)      | (1.2)       | (1.3)       |
| PATAMI              | 9.2         | 9.8         | 6.3        | 12.1        | 15.2        |
| Exceptionals        | 0.8         | 0.9         | 0.8        | 0.7         | (0.2)       |
| <b>Adj PATAMI</b>   | <b>10.0</b> | <b>10.7</b> | <b>7.1</b> | <b>12.8</b> | <b>15.0</b> |
| Basic Shares (m)    | 1,053.0     | 1,053.0     | 1,053.0    | 1,053.0     | 1,053.0     |
| Rep EPS (sen)       | 0.9         | 0.9         | 0.6        | 1.1         | 1.4         |
| Adj EPS (sen)       | 0.9         | 1.0         | 0.7        | 1.2         | 1.4         |
| Adj FD EPS (sen)    | 0.9         | 1.0         | 0.7        | 1.2         | 1.4         |

### Valuation Ratios

| FYE Dec            | FY16  | FY17  | FY18f | FY19f | FY20f |
|--------------------|-------|-------|-------|-------|-------|
| PER (x)            | 43.6  | 29.3  | 19.2  | 15.9  | 14.2  |
| Core PER (x)       | 49.1  | 25.5  | 19.2  | 15.9  | 14.2  |
| FD PER (x)         | 49.1  | 25.5  | 19.2  | 15.9  | 14.2  |
| DPS (sen)          | 0.0   | 0.5   | 2.2   | 2.6   | 2.9   |
| Net DY (%)         | 0.0   | 0.6   | 2.6   | 3.1   | 3.5   |
| Book/share (sen)   | 24.8  | 26.7  | 28.9  | 31.5  | 34.4  |
| P/Book (x)         | 3.3   | 3.1   | 2.9   | 2.6   | 2.4   |
| FCF/share (sen)    | 1.6   | 4.6   | 4.6   | 5.9   | 6.7   |
| FCF yield (%)      | 1.9   | 5.6   | 5.6   | 7.1   | 8.0   |
| Mkt Cap            | 874.0 | 874.0 | 874.0 | 874.0 | 874.0 |
| Net Cash(Debt)     | 60.0  | 85.8  | 111.9 | 146.6 | 186.0 |
| EV                 | 814.0 | 788.2 | 762.1 | 727.4 | 688.0 |
| EV/EBITDA (x)      | 16.0  | 12.2  | 9.2   | 7.6   | 6.6   |
| ROE (%)            | 6.8   | 12.2  | 14.9  | 16.6  | 16.9  |
| Current Ratio (x)  | 2.4   | 2.2   | 2.4   | 2.6   | 2.9   |
| Quick Ratio (x)    | 2.3   | 2.1   | 2.3   | 2.5   | 2.7   |
| Interest Cover (x) | 29.4  | 49.7  | 70.7  | 85.0  | 94.3  |

### Other Ratios

| FYE Dec               | FY16   | FY17   | FY18f  | FY19f  | FY20f  |
|-----------------------|--------|--------|--------|--------|--------|
| Sales Growth (%)      |        | 13.3   | 11.8   | 12.9   | 7.6    |
| EBITDA Growth (%)     |        | 27.1   | 28.3   | 15.1   | 8.3    |
| EBIT Growth (%)       |        | 37.1   | 42.4   | 20.2   | 10.9   |
| PBT Growth (%)        |        | 38.4   | 42.7   | 20.5   | 11.3   |
| Net Profit Growth (%) |        | 33.4   | 38.4   | 20.5   | 11.3   |
| EBITDA Margin (%)     | 19.4   | 21.8   | 25.0   | 25.5   | 25.7   |
| EBIT Margin (%)       | 12.9   | 15.6   | 19.9   | 21.1   | 21.8   |
| PBT Margin (%)        | 12.7   | 15.6   | 19.9   | 21.2   | 21.9   |
| Net Profit Margin (%) | 10.4   | 12.3   | 15.2   | 16.2   | 16.8   |
| Net Debt/Equity (%)   | N Cash | N Cash | N Cash | N Cash | N Cash |
| CAPEX/Sales (%)       | 10.6   | 6.8    | 3.0    | 2.7    | 2.5    |

**Figure #1**      **Quarterly results comparison**

| FYE Dec (RM m)     | 3Q17 | 2Q18 | 3Q18 | QoQ   | YoY   | 9M17  | 9M18  | YoY   |
|--------------------|------|------|------|-------|-------|-------|-------|-------|
| Revenue            | 78.6 | 81.8 | 85.9 | 5.0%  | 9.2%  | 216.2 | 238.6 | 10.3% |
| EBITDA             | 17.8 | 23.8 | 24.7 | 3.7%  | 38.8% | 46.3  | 64.1  | 38.4% |
| EBITDA Margin      | 22.6 | 29.1 | 28.8 |       |       | 21.4  | 26.9  |       |
| EBIT               | 13.0 | 19.5 | 20.5 | 5.2%  | 57.9% | 32.5  | 51.1  | 57.0% |
| PBT                | 12.9 | 19.5 | 20.6 | 5.8%  | 59.8% | 32.5  | 51.2  | 57.5% |
| PAT                | 10.8 | 13.3 | 16.5 | 24.5% | 53.2% | 25.1  | 37.0  | 47.1% |
| Reported PATMI     | 9.2  | 12.1 | 15.2 | 25.7% | 65.3% | 20.0  | 33.6  | 67.6% |
| Core PATMI         | 10.0 | 12.8 | 15.0 | 16.7% | 50.2% | 23.5  | 34.9  | 48.0% |
| Reported EPS (sen) | 0.9  | 1.1  | 1.4  | 25.7% | 65.3% | 1.9   | 3.2   | 67.6% |
| Core EPS (sen)     | 0.9  | 1.2  | 1.4  | 16.7% | 50.2% | 2.2   | 3.3   | 48.0% |

*Bursa, HLIB Research*

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## Stock rating definitions

|                     |   |
|---------------------|---|
| <b>BUY</b>          | Expected absolute return of +10% or more over the next 12 months.   |
| <b>HOLD</b>         | Expected absolute return of -10% to +15% over the next 12 months.   |
| <b>SELL</b>         | Expected absolute return of -10% or less over the next 12 months.   |
| <b>UNDER REVIEW</b> | Rating on the stock is temporarily under review which may or may not result to a change from the previous rating. |
| <b>NOT RATED</b>    | Stock is not or no longer within regular coverage.  |

## Sector rating definitions

|                    |   |
|--------------------|---|
| <b>OVERWEIGHT</b>  | Sector expected to outperform the market over the next 12 months.           |
| <b>NEUTRAL</b>     | Sector expected to perform in-line with the market over the next 12 months. |
| <b>UNDERWEIGHT</b> | Sector expected to underperform the market over the next 12 months.         |