Maybank IB Research

Shariah Compliant

Industrials

Malaysia

Frontken Corp. Bhd (FRCB MK)

3Q19 within expectations

BUY

Share Price	MYR 1.98
12m Price Target	MYR 2.35 (+19%)
Previous Price Target	*MYR 1.85*

TP raised 27%; Maintain BUY w/total return of 19%

3Q19 core net profit was in-line with our expectation and 9M19 73% of our and consensus' full-year estimates. We raise our FY19-21E earnings by 2-7% and our TP by 50sen (27%) to MYR2.35 pegged to a higher 28.0x FY20E PER (2 SD above historical mean) from 23.5X FY20E PER (+1.5 SD). Reiterate BUY premised on strong, resilient earnings of the semiconductor segment (i.e. deployment of 5G) and increasing O&G work orders from its key customer.

Lifted by volume pick-up and improved margin

Excluding marginal net one-off gains, 3Q19 core net profit was MYR19.0m (+31% YoY, +15% QoQ), bringing 9M19 core earnings to MYR51.0m (+55% YoY). 3Q19 bottomline was largely driven YoY by: (i) the semiconductor segment, where work orders increased at its Singapore unit due to an overall pick-up in industry volume; and (ii) improved core net profit margin of 22% (3Q18: 17%) attributed to better efficiency / cost control and favourable sales mix. This, however, was offset by its Taiwan unit, where business decreased from the TFT-LCD portion of the business, and a slowdown at its Malaysia and Philippines units. We note that O&G work orders have remained stable.

Revised up earnings forecasts by 2-7%

We nudge up our FY19/20/21 earnings estimates by 2%/7%/6% after assuming higher work orders at the semiconductor segment (i.e. at the Singapore and Taiwan units) and O&G segments (i.e. ramp-up of repair and maintenance works for its key customer's new equipment).

Expecting order ramp-ups in Taiwan

Notably, Frontken's key Taiwanese customer has guided for improved near-term performance - in anticipation of higher demand and new orders for its advance high-performance chips. This is in-line with the rollout of the 5G wireless networks in 2020. We believe the increase in production of the upcoming, newer chips (i.e. the 5nm and 7nm nodes) would boost high-value-work orders for Frontken.

FYE Dec (MYR m)	FY17A	FY18A	FY19E	FY20E	FY21E
Revenue	297	327	395	461	505
EBITDA	65	92	119	144	165
Core net profit	36	53	70	88	101
Core EPS (sen)	3.4	5.1	6.7	8.4	9.7
Core EPS growth (%)	98.8	50.0	32.0	25.1	15.0
Net DPS (sen)	0.5	1.5	2.0	2.5	2.9
Core P/E (x)	13.6	13.8	29.5	23.6	20.5
P/BV (x)	1.7	2.3	5.5	4.8	4.1
Net dividend yield (%)	1.1	2.1	1.0	1.3	1.5
ROAE (%)	11.0	17.2	20.1	21.7	21.5
ROAA (%)	8.5	12.0	14.7	16.6	17.0
EV/EBITDA (x)	6.3	6.7	16.3	13.4	11.6
Net gearing (%) (incl perps)	net cash	net cash	net cash	net cash	net cash
Consensus net profit	-	-	69	79	88
MKE vs. Consensus (%)	-	-	1.4	12.0	15.3

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Company Description

Frontken specialises in engineering and precision cleaning services, mostly for semiconductors and O&G markets in Taiwan, Singapore and Malaysia.

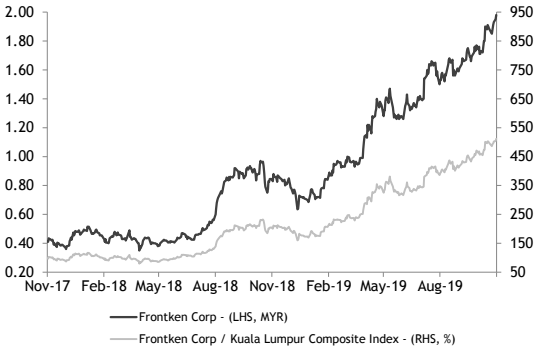
Statistics

52w high/low (MYR)	1.98/0.64
3m avg turnover (USDm)	2.4
Free float (%)	47.6
Issued shares (m)	1,053
Market capitalisation	MYR2.1B USD502M

Major shareholders:

Dazzle Clean Ltd	27.8%
Ooi Keng Thye	14.5%
CIMB-Principal Asset Management	5.2%

Price Performance



	-1M	-3M	-12M
Absolute (%)	12	32	134
Relative to index (%)	9	33	150

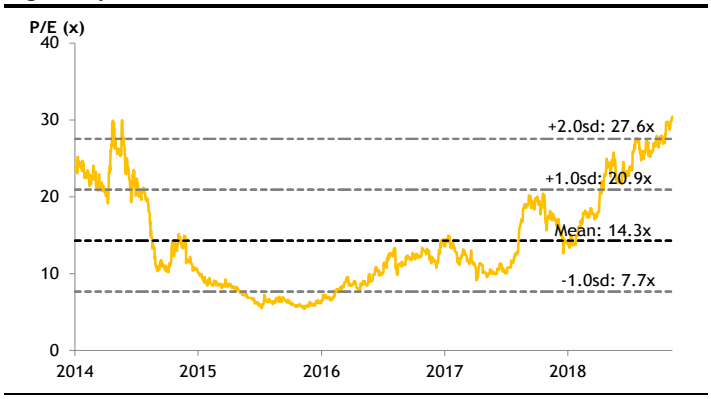
Source: FactSet

Fig 1: Results summary

FYE Dec (MYR'm)	Quarterly					Cumulative		
	3Q19	3Q18	%YoY	2Q19	%QoQ	9M19	9M18	%YoY
Revenue	87.0	85.9	*1.4*	80.1	*8.6*	251.0	238.6	*5.2*
EBITDA	**29.4**	**23.5**	***24.9***	**27.4**	***7.4***	**83.2**	**60.6**	***37.3***
Depreciation	(4.6)	(4.2)	*9.2*	(4.6)	*(1.0)*	(14.1)	(13.0)	*7.9*
Other income	1.2	1.1	*9.2*	0.3	*337.4*	2.5	3.4	*(28.0)*
EBIT	**26.0**	**20.5**	***27.3***	**23.0**	***13.1***	**71.6**	**51.0**	***40.4***
Finance income	0.3	0.3	*7.8*	0.3	*(4.8)*	0.8	0.6	*32.2*
Finance costs	(0.2)	(0.1)	*88.8*	(0.2)	*(4.1)*	(0.6)	(0.5)	*29.4*
Associate profit/loss	-	0.0	*NM*	-	*NM*	-	0.1	*NM*
Pretax profit	**26.1**	**20.6**	***26.5***	**23.1**	***13.1***	**71.8**	**51.2**	***40.2***
Tax expense	(5.6)	(4.1)	*37.2*	(5.3)	*6.9*	(17.1)	(14.2)	*20.6*
Minority interest	(1.4)	(1.3)	*6.2*	(1.3)	*9.4*	(1.4)	(1.3)	*6.2*
Net profit	**19.0**	**15.2**	***25.4***	**16.5**	***15.3***	**51.0**	**33.6**	***51.8***
Net profit ex-EI	**19.0**	**14.5**	***31.2***	**16.5**	***15.3***	**51.0**	**33.0**	***54.6***
Basic EPS (sen)	1.82	1.45	*25.5*	1.58	***15.2***	4.87	3.20	*52.2*
Margin (%)	**3Q19**	**3Q18**	**+/- ppt**	**2Q19**	**+/- ppt**	**9M19**	**9M18**	**+/- ppt**
EBIT	29.9	23.8	*6.1*	28.7	*1.2*	28.5	21.4	*7.1*
Pretax profit	30.0	24.0	*6.0*	28.8	*1.2*	28.6	21.5	*7.1*
Net profit ex-EI	21.9	16.9	*5.0*	20.6	*1.3*	20.3	13.8	*6.5*
Net gearing (x)	**net cash**	**net cash**	**nm**	**net cash**	**nm**	**net cash**	**net cash**	**nm**
Segmental revenue (MYR'm)	**3Q19**	**3Q18**	**%YoY**	**2Q19**	**%QoQ**	**9M19**	**9M18**	**%YoY**
Taiwan	48.7	48.9	*(0.4)*	43.7	*11.6*	137.6	138.4	*(0.6)*
Singapore	19.0	16.0	*18.8*	16.9	*11.9*	52.2	43.3	*20.4*
Malaysia	15.3	15.8	*(3.2)*	15.1	*0.9*	48.4	42.8	*13.1*
Philippines	3.9	5.0	*(20.6)*	4.1	*(4.6)*	12.3	13.1	*(6.6)*
Indonesia	0.1	0.3	*(42.9)*	0.3	*(54.3)*	0.6	0.8	*(28.1)*
Segmental EBIT (MYR'm)	**3Q19**	**3Q18**	**%YoY**	**2Q19**	**%QoQ**	**9M19**	**9M18**	**%YoY**
Taiwan	15.0	13.8	*8.5*	13.0	*14.8*	40.3	35.9	*12.5*
Singapore	7.4	3.9	*87.7*	5.9	*25.3*	18.3	9.1	*99.9*
Malaysia	3.2	1.6	*103.7*	3.4	*(5.1)*	11.1	4.1	*169.4*
Philippines	0.6	0.8	*(33.5)*	0.7	*(24.2)*	2.0	2.2	*(8.5)*
Indonesia	(0.1)	(0.3)	*(78.4)*	(0.0)	*311.8*	(0.2)	(1.0)	*(80.6)*
Segmental EBIT margin (%)	**3Q19**	**3Q18**	**+/- ppt**	**2Q19**	**+/- ppt**	**9M19**	**9M18**	**+/- ppt**
Taiwan	30.7	28.2	*2.5*	29.9	*0.9*	29.3	25.9	*3.4*
Singapore	39.0	24.7	*14.3*	34.8	*4.2*	35.0	21.1	*13.9*
Malaysia	20.8	9.9	*10.9*	22.2	*(1.3)*	23.0	9.6	*13.3*
Philippines	14.0	16.7	*(2.7)*	17.7	*(3.6)*	16.5	16.9	*(0.3)*
Indonesia	NM	NM	*NM*	NM	*NM*	NM	NM	*NM*

Source: Company data

Fig 2: 1-year forward PER



Source: Bloomberg, Company data, Maybank KE

Fig 3: 1-year forward PBV

Source: Bloomberg, Company data, Maybank KE

Risk statement

There are several risk factors for our earnings estimates, target price and rating for Frontken. A sharp downturn in the global markets for electronics and/or oil & gas will affect the demand for Frontken's services. Additionally, forex volatility, especially USD/MYR, will also affect Frontken's earnings, as ~20%/10% of the Group's revenue/operating profit is denominated in USD.

FYE 31 Dec	FY17A	FY18A	FY19E	FY20E	FY21E
Key Metrics					
P/E (reported) (x)	11.1	12.0	29.5	23.6	20.5
Core P/E (x)	13.6	13.8	29.5	23.6	20.5
P/BV (x)	1.7	2.3	5.5	4.8	4.1
P/NTA (x)	1.7	2.3	6.5	5.5	4.8
Net dividend yield (%)	1.1	2.1	1.0	1.3	1.5
FCF yield (%)	10.1	7.6	2.2	2.3	3.0
EV/EBITDA (x)	6.3	6.7	16.3	13.4	11.6
EV/EBIT (x)	8.8	8.3	18.9	15.1	12.9
INCOME STATEMENT (MYR m)					
Revenue	296.6	327.2	395.4	460.5	504.9
Gross profit	104.8	126.6	161.9	190.8	214.5
EBITDA	64.8	92.5	119.0	144.0	164.6
Depreciation	(18.5)	(17.3)	(16.7)	(17.0)	(17.5)
Amortisation	0.0	0.0	0.0	0.0	0.0
EBIT	46.3	75.2	102.2	127.0	147.1
Net interest income /(exp)	(0.1)	0.3	0.1	0.1	0.2
Associates & JV	(0.1)	0.1	0.0	0.0	0.0
Exceptionals	0.0	0.0	0.0	0.0	0.0
Other pretax income	0.0	0.0	0.0	0.0	0.0
Pretax profit	46.1	75.6	102.3	127.1	147.3
Income tax	(9.7)	(18.6)	(25.5)	(30.5)	(35.3)
Minorities	(6.6)	(4.7)	(6.4)	(8.5)	(10.6)
Discontinued operations	0.0	0.0	0.0	0.0	0.0
Reported net profit	29.9	52.3	70.4	88.1	101.3
Core net profit	35.6	53.4	70.4	88.1	101.3
BALANCE SHEET (MYR m)					
Cash & Short Term Investments	129.3	149.9	174.0	193.1	221.1
Accounts receivable	97.0	113.6	149.1	193.4	239.6
Inventory	13.5	13.7	14.5	19.3	24.2
Reinsurance assets	0.0	0.0	0.0	0.0	0.0
Property, Plant & Equip (net)	150.0	140.4	127.5	118.5	109.0
Intangible assets	33.8	33.8	33.8	33.8	33.8
Investment in Associates & JVs	2.0	0.0	0.0	0.0	0.0
Other assets	5.5	3.7	3.7	3.7	3.7
Total assets	**431.1**	**455.1**	**502.7**	**561.7**	**631.3**
ST interest bearing debt	16.9	4.8	2.7	2.7	2.7
Accounts payable	79.6	81.6	78.1	68.6	61.5
Insurance contract liabilities	0.0	0.0	0.0	0.0	0.0
LT interest bearing debt	11.7	8.9	8.1	8.1	8.1
Other liabilities	17.0	15.0	15.0	16.0	15.0
Total Liabilities	**125.1**	**110.4**	**104.3**	**95.7**	**86.9**
Shareholders Equity	281.6	325.0	374.3	436.0	506.9
Minority Interest	24.4	19.6	24.1	30.0	37.5
Total shareholder equity	**306.0**	**344.6**	**398.4**	**466.0**	**544.4**
Total liabilities and equity	**431.1**	**455.1**	**502.7**	**561.7**	**631.3**
CASH FLOW (MYR m)					
Pretax profit	46.1	75.6	102.3	127.1	147.3
Depreciation & amortisation	18.5	17.3	16.7	17.0	17.5
Adj net interest (income)/exp	0.1	(0.3)	(0.1)	(0.1)	(0.2)
Change in working capital	6.9	(15.9)	(39.8)	(58.6)	(58.2)
Cash taxes paid	(7.9)	(14.2)	(25.5)	(30.5)	(35.3)
Other operating cash flow	5.4	(0.4)	0.0	0.0	0.0
Cash flow from operations	69.0	63.3	53.6	54.9	71.0
Capex	(20.2)	(7.5)	(8.0)	(8.0)	(8.0)
Free cash flow	48.9	55.8	45.6	46.9	63.0
Dividends paid	(7.2)	(10.0)	(23.0)	(29.0)	(33.6)
Equity raised / (purchased)	0.0	0.0	0.0	0.0	0.0
Change in Debt	(0.2)	(17.3)	(2.9)	0.0	0.0
Other invest/financing cash flow	(12.9)	(0.2)	0.1	0.1	0.2
Effect of exch rate changes	(6.4)	0.3	0.1	0.0	0.0
Net cash flow	22.2	28.7	19.9	18.1	29.7

FYE 31 Dec	FY17A	FY18A	FY19E	FY20E	FY21E
Key Ratios					
Growth ratios (%)					
Revenue growth	13.3	10.3	20.8	16.5	9.6
EBITDA growth	26.9	42.8	28.6	21.0	14.3
EBIT growth	36.8	62.4	36.0	24.2	15.9
Pretax growth	38.4	63.9	35.3	24.2	15.9
Reported net profit growth	49.0	75.0	34.8	25.1	15.0
Core net profit growth	98.8	50.0	32.0	25.1	15.0
Profitability ratios (%)					
EBITDA margin	21.8	28.3	30.1	31.3	32.6
EBIT margin	15.6	23.0	25.9	27.6	29.1
Pretax profit margin	15.6	23.1	25.9	27.6	29.2
Payout ratio	17.5	30.1	30.0	30.0	30.0
DuPont analysis					
Net profit margin (%)	10.1	16.0	17.8	19.1	20.1
Revenue/Assets (x)	0.7	0.7	0.8	0.8	0.8
Assets/Equity (x)	1.5	1.4	1.3	1.3	1.2
ROAE (%)	11.0	17.2	20.1	21.7	21.5
ROAA (%)	8.5	12.0	14.7	16.6	17.0
Liquidity & Efficiency					
Cash conversion cycle	(0.3)	(4.4)	18.3	58.5	100.7
Days receivable outstanding	120.3	115.8	119.6	133.9	154.4
Days inventory outstanding	23.0	24.4	21.7	22.5	26.9
Days payables outstanding	143.5	144.6	123.1	97.9	80.7
Dividend cover (x)	5.7	3.3	3.3	3.3	3.3
Current ratio (x)	2.2	2.8	3.7	4.9	6.4
Leverage & Expense Analysis					
Asset/Liability (x)	3.4	4.1	4.8	5.9	7.3
Net gearing (%) (incl perps)	net cash	net cash	net cash	net cash	net cash
Net gearing (%) (excl. perps)	net cash	net cash	net cash	net cash	net cash
Net interest cover (x)	nm	na	na	na	na
Debt/EBITDA (x)	0.4	0.1	0.1	0.1	0.1
Capex/revenue (%)	6.8	2.3	2.0	1.7	1.6
Net debt/ (net cash)	(100.7)	(136.3)	(163.2)	(182.2)	(210.2)

Source: Company; Maybank

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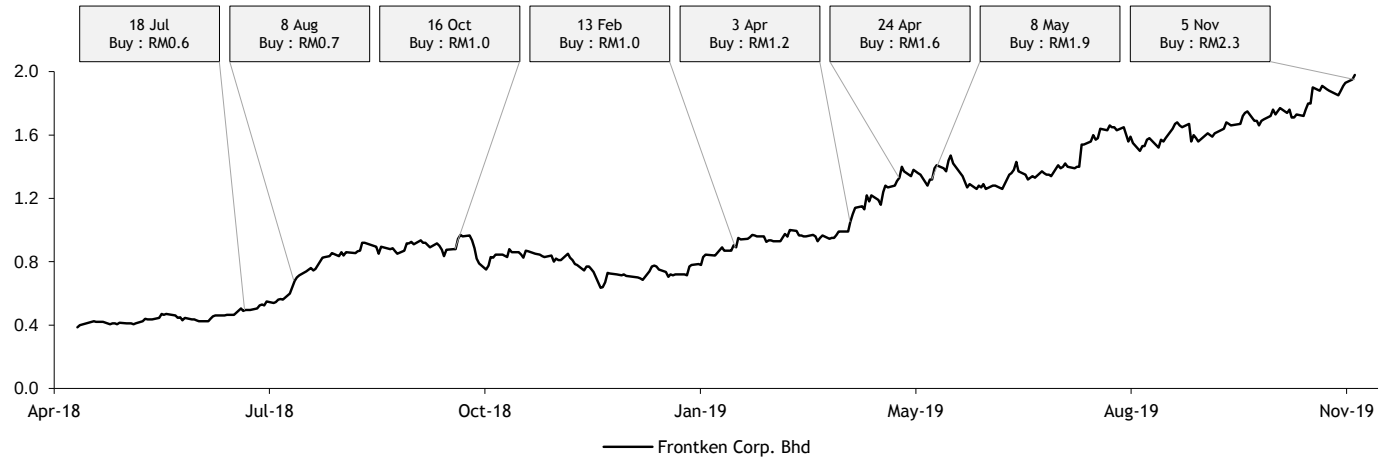

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