

HLIB Research

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HOLD (Maintain)

Target Price: RM2.40

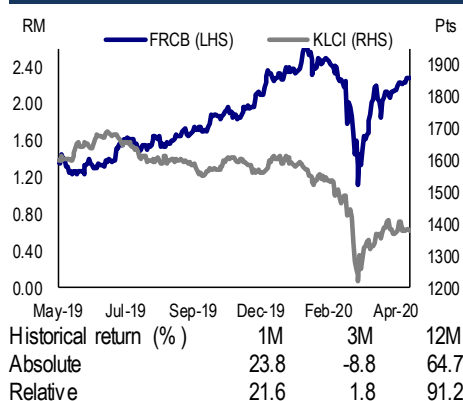
Previously: RM2.40

Current Price: RM2.29

Capital upside	4.8%
Dividend yield	1.3%
Expected total return	6.1%

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)	2,400
3-mth average volume ('000)	9,253
SC Shariah compliant	Yes

Major shareholders

Dazzle Clean	27.8%
Ooi Keng Thye	15.1%
Kenanga Unit Trust	3.5%

Earnings summary

FYE (Dec)	FY19	FY20f	FY21f
PATMI – core (RM m)	69.6	82.4	90.2
EPS – core (sen)	6.6	7.8	8.6
P/E (x)	34.6	29.3	26.7

Frontken Corporation

Best 1Q ever

Frontken's 1Q20 core net profit of RM16m (-14% QoQ, +6% YoY) matched expectations. Sequential weakness was mainly due to seasonality. On the YoY basis, bottom line growth outpaced top line expansion attributable to relentless focus on operational excellence. Amid Covid-19 outbreak and plunge in crude oil price, Frontken is cautiously optimistic on its business outlook. Forecasts and TP of RM2.40 (pegged to 28x of FY21 EPS) are unchanged. Maintain HOLD.

Within expectations. 1Q20 core net profit of RM16m (-14% QoQ, +6% YoY) yielded no surprise, accounting for 20% and 19% of HLIB and consensus full year estimates, respectively. 1Q is seasonally the weakest quarter and we expect Covid-19 to have limited impact on its operations. Forex gain of RM671k was adjusted to arrive at our core net profit.

Dividend. None (1Q19: none).

QoQ. Turnover fell 5% attributable to seasonal weakness due to lesser business days. In terms of sales breakdown, Taiwan (+1%) and Philippines (+3%) gained while Singapore (-12%), Malaysia (-17%) and Indonesia (-26%) shrunk. In turn, core net profit contracted by 14% due to higher effective corporate tax rate (1Q20: 26.3% vs. 4Q19: 20.0%). This includes the surtax provision on AGTC's undistributed earnings.

YoY. Revenue saw a marginal growth of 1% driven by Taiwan's semiconductor (+15%) and Indonesia's O&G (+92%) businesses, but largely neutralized by the declines in Singapore (-4%), Malaysia (-28%) and Philippines (-9%). The contractions were mainly due to the slowdown in O&G segment. In addition, the MCO due to the Covid-19 pandemic has resulted in even lesser working days. However, bottom line expanded at a faster pace of 10% to RM16m thanks to better profit margin resulting from the continual efficiency improvement across the group.

Semiconductor. Generated 82% (FY19: 78%) of group revenue in 1Q20. Frontken anticipates the business condition will be challenging amidst global uncertainties and downside risks due to heightened global concerns over Covid-19 impact on the world economy. However, it is cautiously optimistic that performance for the remaining months will be satisfactory provided the global economy is able to restart within the expected time frame.

O&G. Accounted for the remaining 18% of group turnover in 1Q20. The outbreak and the plunge in crude oil price has added a major layer of uncertainty to the market outlook and it will need to remain vigilant in FY20 while standing ready to embrace new opportunities for profitable growth in an evolving market landscape.

Forecast. Unchanged as results are in line.

Maintain **HOLD** with unchanged TP of **RM2.40**, pegged to 28x of FY21 EPS. While still like Frontken for its multi-year growth ahead on the back of: (1) sustainable global semiconductor market outlook, (2) robust fab investment, (3) leading edge technology (7nm and below), and (4) strong balance sheet (net cash of RM234m or 22.2 sen per share); these positives seems rather priced in at current valuations.

Financial Forecast

All items in (RM m) unless otherwise stated

Income statement

FYE Dec	FY18	FY19	FY20f	FY21f	FY22f
Revenue	327.2	339.9	376.8	404.7	424.9
COGS	(234.7)	(226.2)	(251.4)	(270.2)	(283.7)
EBITDA	92.6	113.7	125.4	134.5	141.2
D&A	(17.3)	(17.8)	(16.0)	(15.2)	(14.7)
EBIT	75.3	95.9	109.4	119.2	126.5
Net Interest Income	0.3	0.4	1.3	1.8	2.2
Associates	0.0	0.0	0.0	0.0	0.0
PBT	75.6	96.3	110.8	121.0	128.7
Tax	(18.6)	(22.0)	(23.3)	(25.4)	(27.0)
Net Profit	57.0	74.2	87.5	95.6	101.7
MI	(4.7)	(5.1)	(5.1)	(5.4)	(4.9)
PATAMI	52.3	69.2	82.4	90.2	96.7
Exceptionals	2.2	0.5	0.0	0.0	0.0
Adj PATAMI	54.4	69.6	82.4	90.2	96.7
Basic Shares (m)	1,053.0	1,053.0	1,053.0	1,053.0	1,053.0
Rep EPS (sen)	5.0	6.6	7.8	8.6	9.2
Adj EPS (sen)	5.2	6.6	7.8	8.6	9.2
Adj FD EPS (sen)	5.2	6.6	7.8	8.6	9.2

Balance sheet

FYE Dec	FY18	FY19	FY20f	FY21f	FY22f
Cash	133.0	197.2	257.6	322.8	391.4
Receivables	106.8	86.3	95.7	102.7	107.9
Inventories	13.7	15.1	16.8	18.0	18.9
Investment	0.0	0.0	0.0	0.0	0.0
PPE	140.4	145.5	139.5	134.2	129.5
Intangibles	33.8	33.8	33.8	33.8	33.8
Other Assets	27.4	37.9	37.9	37.9	37.9
Total Assets	455.1	515.7	581.3	649.5	719.4
Payables	82.4	84.0	93.4	100.4	105.4
ST borrowings	3.9	0.8	0.8	0.8	0.8
LT borrowings	7.5	0.0	0.0	0.0	0.0
Other Liabilities	16.5	32.1	32.1	32.1	32.1
Total liabilities	110.4	117.0	126.3	133.3	138.3
Shareholders' Funds	325.0	377.0	428.0	483.9	543.9
MI	19.6	21.8	26.9	32.2	37.2
Total S/H Equity	344.6	398.7	454.9	516.2	581.1
Ttl Liab&S/H Funds	455.1	515.7	581.3	649.5	719.4

Cashflow Analysis

FYE Dec	FY18	FY19	FY20f	FY21f	FY22f
EBITDA	92.6	113.7	125.4	134.5	141.2
Tax Paid	(14.2)	(19.8)	(23.3)	(25.4)	(27.0)
WC Changes	(14.6)	21.3	(1.7)	(1.3)	(1.0)
Other	(0.4)	(0.3)	1.3	1.8	2.2
CFO	63.3	114.9	101.8	109.5	115.4
FCF	55.8	107.9	91.8	99.5	105.4
CAPEX(CF)	(7.5)	(7.0)	(10.0)	(10.0)	(10.0)
Acquisitions	(7.1)	(2.6)	0.0	0.0	0.0
Other	7.5	(2.4)	0.0	0.0	0.0
CFI	(7.1)	(12.1)	(10.0)	(10.0)	(10.0)
Dividend	(10.0)	(18.9)	(31.3)	(34.3)	(36.8)
Debt changes	(16.7)	(10.7)	0.0	0.0	0.0
Other	(1.1)	(4.2)	0.0	0.0	0.0
CFF	(27.8)	(33.7)	(31.3)	(34.3)	(36.8)
Net Cashflow	28.4	69.1	60.5	65.2	68.6

Quarterly financial summary

FYE Dec	1Q19	2Q19	3Q19	4Q19	1Q20
Revenue	83.8	80.1	87.0	88.9	84.9
COGS	(56.5)	(52.5)	(56.4)	(60.9)	(55.8)
EBITDA	27.4	27.7	30.6	28.0	29.1
D&A	(4.8)	(4.6)	(4.6)	(3.8)	(4.7)
EBIT	22.6	23.0	26.0	24.3	24.4
Net Interest Income	(0.0)	0.1	0.1	0.2	0.3
Associates	0.0	0.0	0.0	0.0	0.0
PBT	22.5	23.1	26.1	24.5	24.7
Tax	(6.2)	(5.3)	(5.6)	(4.9)	(6.5)
Net Profit	16.3	17.8	20.5	19.6	18.2
MI	(0.9)	(1.3)	(1.4)	(1.4)	(1.2)
PATAMI	15.4	16.5	19.0	18.2	17.0
Exceptionals	(0.0)	0.8	(1.0)	0.7	(0.7)
Adj PATAMI	15.4	17.3	18.0	18.9	16.3
Basic Shares (m)	1,053.0	1,053.0	1,053.0	1,053.0	1,053.0
Rep EPS (sen)	1.5	1.6	1.8	1.7	1.6
Adj EPS (sen)	1.5	1.6	1.7	1.8	1.6
Adj FD EPS (sen)	1.5	1.6	1.7	1.8	1.6

Valuation Ratios

FYE Dec	FY18	FY19	FY20f	FY21f	FY22f
PER (x)	46.1	34.9	29.3	26.7	24.9
Core PER (x)	44.3	34.6	29.3	26.7	24.9
FD PER (x)	44.3	34.6	29.3	26.7	24.9
DPS (sen)	1.5	2.5	3.0	3.3	3.5
Net DY (%)	0.7	1.1	1.3	1.4	1.5
Book/share (sen)	30.9	35.8	40.6	46.0	51.7
P/Book (x)	7.4	6.4	5.6	5.0	4.4
FCF/share (sen)	5.3	10.2	8.7	9.4	10.0
FCF yield (%)	2.3	4.5	3.8	4.1	4.4
Mkt Cap	2,411.4	2,411.4	2,411.4	2,411.4	2,411.4
Net Cash/Debt	121.5	196.3	256.8	322.0	390.5
EV	2,289.8	2,215.1	2,154.6	2,089.4	2,020.8
EV/EBITDA (x)	24.7	19.5	17.2	15.5	14.3
ROE (%)	16.7	18.5	19.3	18.6	17.8
Current Ratio (x)	2.9	3.5	3.9	4.4	4.9
Quick Ratio (x)	2.8	3.3	3.7	4.2	4.7
Interest Cover (x)	132.5	126.8	4,321.0	4,709.3	4,996.0

Other Ratios

FYE Dec	FY18	FY19	FY20f	FY21f	FY22f
Sales Growth (%)		3.9	10.9	7.4	5.0
EBITDA Growth (%)		22.8	10.3	7.2	5.0
EBIT Growth (%)		27.4	14.1	9.0	6.1
PBT Growth (%)		27.3	15.1	9.3	6.4
Net Profit Growth (%)		30.2	17.9	9.3	6.4
EBITDA Margin (%)	28.3	33.4	33.3	33.2	33.2
EBIT Margin (%)	23.0	28.2	29.0	29.5	29.8
PBT Margin (%)	23.1	28.3	29.4	29.9	30.3
Net Profit Margin (%)	17.4	21.8	23.2	23.6	23.9
Net Debt/Equity (%)	Cash	Cash	Cash	Cash	Cash
CAPEX/Sales (%)	2.3	2.1	2.7	2.5	2.4

Figure #1 **Quarterly results comparison**

FYE Dec (RM m)	1Q19	4Q19	1Q20	QoQ	YoY
Revenue	83.8	88.9	84.9	(4.5)	1.2
EBITDA	27.4	28.0	29.1	3.8	6.3
EBITDA Margin	32.6	31.5	34.3		
EBIT	22.6	24.3	24.4	0.4	8.1
PBT	22.5	24.5	24.7	1.0	9.6
PAT	16.3	19.6	18.2	(6.8)	11.6
Reported PATMI	15.4	18.2	17.0	(6.5)	10.4
Core PATMI	15.4	18.9	16.3	(13.7)	6.1
Reported EPS (sen)	1.5	1.7	1.6	(6.5)	10.4
Core EPS (sen)	1.5	1.8	1.6	(13.7)	6.1

Bursa, HLIB Research

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

Sector rating guidelines

OVERWEIGHT	Sector expected to outperform the market over the next 12 months.
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UNDERWEIGHT	Sector expected to underperform the market over the next 12 months.

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