Shariah Compliant

Industrials

Malaysia

August 4, 2020

Maybank IB Research

Frontken Corp. Bhd (FRCB MK)

2Q20 earnings on track

HOLD

Share Price	MYR 3.69
12m Price Target	MYR 3.60 (-1%)
Previous Price Target	*MYR 2.30*

Maintain HOLD

2Q20 results were in-line – 1H20 earnings were at 43%/44% of our/consensus' full-year estimates. We maintain our earnings forecasts but increase our TP by MYR1.30 to MYR3.60. Our TP is pegged to a rolled-forward, re-rated 37x FY21E PER at +2.5SD of mean due to its earnings resiliencies. Maintain HOLD, pending next major growth catalyst(s). We believe current valuation has largely priced in growth upsides from the semiconductor segment at this juncture.

Driven by semiconductor segment

2Q20 net profit grew 23% YoY and 20% QoQ to MYR20.3m – taking 1H20 earnings to MYR37.3m (+17% YoY). This was within our expectations as we are anticipating a seasonally stronger 2H20. 2Q20 bottomline growth (YoY) was largely driven by the semiconductor segment, namely from its key Taiwanese customer (i.e. work orders related to 5nm and 7nm nodes), as well as improved operational efficiencies across the group. 2Q20 earnings, however, was partly mitigated by the slowdown of the global O&G sector which has led to lower earnings of its Malaysian, Singaporean and Philippines entities. 1H20's revenue split was 87%/13% for the semiconductor/O&G segments.

Estimates unchanged

We maintain our FY20-22 net profit forecasts at this juncture. For our near-term earnings growth, we have mainly pencilled in sustained favourable growth at its semiconductor segment and gradual recovery of the O&G segment (post FY20).

Increasing TP and valuation peg

We raise our TP by MYR1.30 to MYR3.60, pegged to a rolled-forward, re-rated 36x FY21E PER (+2.5SD of mean) from 28x FY20E PER (+2SD of mean). This is primarily based on its resilient earnings and work orders from its key semiconductor customers (i.e Taiwan) while its mid to long-term outlook is underpinned by increasing high value work orders for equipment which produces newer chips with smaller nodes (i.e. 2nm).

FYE Dec (MYR m)	FY18A	FY19A	FY20E	FY21E	FY22E
Revenue	327	340	450	507	574
EBITDA	92	111	141	165	172
Core net profit	54	69	87	102	106
Core EPS (sen)	5.2	6.6	8.3	9.7	10.1
Core EPS growth (%)	52.7	27.4	25.4	17.6	4.3
Net DPS (sen)	1.5	2.5	2.8	3.3	3.5
Core P/E (x)	13.6	34.7	44.6	37.9	36.4
P/BV (x)	2.3	6.4	9.0	7.8	6.8
Net dividend yield (%)	2.1	1.1	0.8	0.9	0.9
ROAE (%)	17.2	19.7	21.5	22.1	20.0
ROAA (%)	12.3	14.3	16.1	17.0	15.7
EV/EBITDA (x)	6.7	19.9	26.0	22.1	20.9
Net gearing (%) (incl perps)	net cash	net cash	net cash	net cash	net cash
Consensus net profit	-	-	85	103	109
MKE vs. Consensus (%)	-	-	2.6	(1.2)	(2.4)

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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.

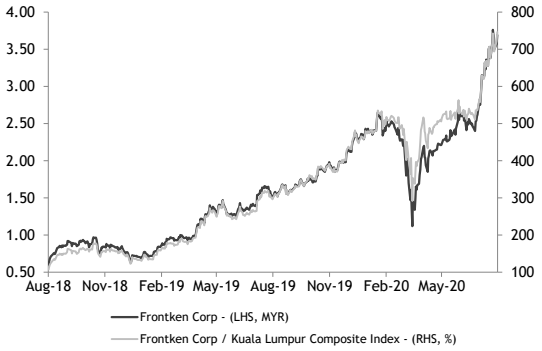
Statistics

52w high/low (MYR)	3.76/1.12
3m avg turnover (USDm)	4.1
Free float (%)	57.2
Issued shares (m)	1,053
Market capitalisation	MYR3.9B
	USD921M

Major shareholders:

Dazzle Clean Ltd.	21.5%
OOI KENG THYE /FRONTKEN/	15.1%
Public Mutual Bhd.	3.5%

Price Performance



	-1M	-3M	-12M
Absolute (%)	41	67	138
Relative to index (%)	39	46	146

Source: FactSet

Fig 1: Results summary

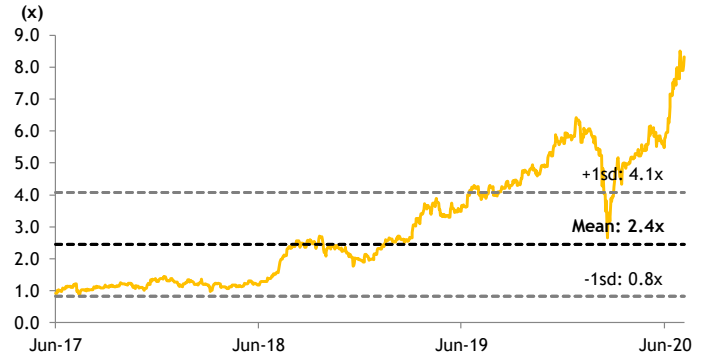
FYE Dec (MYR'm)	Quarterly					Cumulative		
	2Q20	2Q19	%YoY	1Q20	%QoQ	1HFY20	1HFY19	%YoY
Revenue	87.6	80.1	*9.3*	84.9	*3.2*	172.5	164.0	*5.2*
EBITDA	**30.7**	**27.4**	***12.1***	**26.8**	***14.6***	**57.4**	**53.8**	***6.8***
Depreciation	(4.6)	(4.6)	*(1.1)*	(4.7)	*(2.8)*	(9.3)	(9.5)	*(1.5)*
Other income	1.7	0.3	*510.0*	2.3	*(26.8)*	4.1	1.3	*223.5*
EBIT	**27.8**	**23.0**	***20.8***	**24.4**	***14.0***	**52.2**	**45.6**	***14.5***
Finance income	0.3	0.3	*2.1*	0.5	*(43.5)*	0.8	0.5	*55.6*
Finance costs	(0.2)	(0.2)	*(7.8)*	(0.2)	*(1.7)*	(0.4)	(0.4)	*(16.7)*
Associate profit/loss	-	-	*NM*	-	*NM*	-	-	*NM*
Pretax profit	**27.9**	**23.1**	***20.8***	**24.7**	***12.9***	**52.6**	**45.7**	***15.3***
Tax expense	(6.1)	(5.3)	*15.3*	(6.5)	*(6.0)*	(12.6)	(11.5)	*9.4*
Minority interest	(1.5)	(1.3)	*14.9*	(1.2)	*21.2*	(1.5)	(1.3)	*14.9*
Net profit	**20.3**	**16.5**	***23.1***	**17.0**	***19.5***	**37.3**	**31.9**	***17.0***
Net profit ex-EI	**20.3**	**16.5**	***23.1***	**17.0**	***19.5***	**37.3**	**31.9**	***17.0***
Basic EPS (sen)	1.94	1.58	*22.8*	1.62	*19.8*	6.6	3.1	*16.7*
Margin (%)	**2Q20**	**2Q19**	**+/- ppt**	**1Q20**	**+/- ppt**	**1HFY20**	**1HFY19**	**+/- ppt**
EBIT	31.7	28.7	*3.0*	28.7	*3.0*	30.3	27.8	*2.5*
Pretax profit	31.9	28.8	*3.0*	29.1	*2.7*	30.5	27.8	*2.7*
Net profit ex-EI	23.2	20.6	*2.6*	20.0	*3.2*	21.6	19.5	*2.2*
Segmental revenue (MYR'm)	**2Q20**	**2Q19**	**%YoY**	**1Q20**	**%QoQ**	**1HFY20**	**1HFY19**	**%YoY**
Taiwan	58.9	43.7	*34.8*	52.2	*12.7*	111.1	88.9	*24.9*
Singapore	14.4	16.9	*(14.7)*	15.6	*(7.2)*	30.0	33.2	*(9.6)*
Malaysia	10.9	15.1	*(28.2)*	13.0	*(16.5)*	23.9	33.2	*(27.9)*
Philippines	3.2	4.1	*(21.9)*	3.8	*(15.4)*	7.0	8.3	*(15.4)*
Indonesia	0.2	0.3	*(30.9)*	0.3	*(12.4)*	0.5	0.4	*4.9*
Segmental EBIT (MYR'm)	**2Q20**	**2Q19**	**%YoY**	**1Q20**	**%QoQ**	**1HFY20**	**1HFY19**	**%YoY**
Taiwan	20.1	13.0	*54.1*	17.2	*16.7*	37.3	25.4	*46.9*
Singapore	5.5	5.9	*(7.0)*	5.4	*1.9*	10.9	10.9	*(0.1)*
Malaysia	1.1	3.4	*(66.0)*	2.1	*(46.0)*	3.3	7.9	*(59.0)*
Philippines	0.4	0.7	*(49.3)*	0.5	*(24.0)*	0.9	1.5	*(41.7)*
Indonesia	0.7	(0.0)	*NM*	(0.8)	*NM*	(0.1)	(0.1)	*(15.5)*
Segmental EBIT margin (%)	**2Q20**	**2Q19**	**+/- ppt**	**1Q20**	**+/- ppt**	**1HFY20**	**1HFY19**	**+/- ppt**
Taiwan	34.1	29.9	*4.3*	33.0	*1.2*	33.6	28.6	*5.0*
Singapore	38.0	34.8	*3.2*	34.6	*3.4*	36.2	32.8	*3.5*
Malaysia	10.5	22.2	*(11.7)*	16.3	*(5.7)*	13.6	24.0	*(10.3)*
Philippines	11.5	17.7	*(6.2)*	12.8	*(1.3)*	12.2	17.7	*(5.5)*
Indonesia	327.9	(5.4)	*333.2*	(330.8)	*658.7*	(23.2)	(28.9)	*5.6*

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	FY18A	FY19A	FY20E	FY21E	FY22E
Key Metrics					
P/E (reported) (x)	12.0	22.0	44.6	37.9	36.4
Core P/E (x)	13.6	34.7	44.6	37.9	36.4
P/BV (x)	2.3	6.4	9.0	7.8	6.8
P/NTA (x)	2.3	6.4	10.3	9.0	7.8
Net dividend yield (%)	2.1	1.1	0.8	0.9	0.9
FCF yield (%)	7.6	5.4	1.6	2.8	2.7
EV/EBITDA (x)	6.7	19.9	26.0	22.1	20.9
EV/EBIT (x)	8.3	23.1	29.6	24.7	23.4
INCOME STATEMENT (MYR m)					
Revenue	327.2	339.9	450.1	507.4	574.5
Gross profit	126.6	108.4	189.7	216.6	226.2
EBITDA	92.5	110.9	141.4	164.9	171.8
Depreciation	(17.3)	(17.8)	(17.0)	(17.5)	(17.9)
Amortisation	0.0	0.0	0.0	0.0	0.0
EBIT	75.2	95.9	124.4	147.4	153.8
Net interest income /(exp)	0.3	0.4	0.7	0.8	0.8
Associates & JV	0.1	0.0	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	75.6	96.3	125.1	148.2	154.6
Income tax	(18.6)	(22.0)	(30.0)	(35.6)	(37.1)
Minorities	(4.7)	(5.1)	(8.4)	(10.7)	(11.2)
Discontinued operations	0.0	0.0	0.0	0.0	0.0
Reported net profit	52.3	69.2	86.7	102.0	106.4
Core net profit	54.3	69.2	86.7	102.0	106.4
BALANCE SHEET (MYR m)					
Cash & Short Term Investments	149.9	224.2	216.1	267.5	314.6
Accounts receivable	113.6	93.7	137.6	155.1	175.6
Inventory	13.7	15.1	16.2	18.1	21.6
Reinsurance assets	0.0	0.0	0.0	0.0	0.0
Property, Plant & Equip (net)	140.4	145.5	153.5	161.5	169.5
Intangible assets	33.8	33.8	33.8	33.8	33.8
Investment in Associates & JVs	0.0	0.0	0.0	0.0	0.0
Other assets	3.7	3.6	3.7	3.7	3.3
Total assets	**455.1**	**515.7**	**560.8**	**639.6**	**718.4**
ST interest bearing debt	4.8	3.9	2.7	2.7	2.7
Accounts payable	81.6	84.0	88.8	93.3	94.5
Insurance contract liabilities	0.0	0.0	0.0	0.0	0.0
LT interest bearing debt	8.9	11.9	1.3	1.3	1.3
Other liabilities	15.0	17.0	12.0	12.0	12.0
Total Liabilities	**110.4**	**117.0**	**105.3**	**109.7**	**111.0**
Shareholders Equity	325.0	377.0	428.2	495.5	565.7
Minority Interest	19.6	21.8	27.3	34.4	41.7
Total shareholder equity	**344.6**	**398.7**	**455.5**	**529.9**	**607.4**
Total liabilities and equity	**455.1**	**515.7**	**560.8**	**639.6**	**718.4**
CASH FLOW (MYR m)					
Pretax profit	75.6	96.3	125.1	148.2	154.6
Depreciation & amortisation	17.3	17.8	17.0	17.5	17.9
Adj net interest (income)/exp	(0.3)	(0.4)	(0.7)	(0.8)	(0.8)
Change in working capital	(15.9)	20.9	(40.2)	(14.9)	(22.9)
Cash taxes paid	(14.2)	(19.8)	(30.0)	(35.6)	(37.1)
Other operating cash flow	(0.4)	(0.3)	0.0	0.0	0.0
Cash flow from operations	63.3	135.8	71.2	114.4	111.8
Capex	(7.5)	(7.0)	(8.0)	(8.0)	(8.0)
Free cash flow	55.8	128.8	63.2	106.4	103.8
Dividends paid	(10.0)	(19.9)	(32.3)	(38.3)	(40.0)
Equity raised / (purchased)	0.0	0.0	0.0	0.0	0.0
Change in Debt	(17.3)	(13.0)	0.0	0.0	0.0
Other invest/financing cash flow	(0.2)	(5.8)	0.7	0.8	0.8
Effect of exch rate changes	0.3	1.7	0.0	0.0	0.0
Net cash flow	28.7	91.7	31.6	68.9	64.6

FYE 31 Dec	FY18A	FY19A	FY20E	FY21E	FY22E
Key Ratios					
Growth ratios (%)					
Revenue growth	10.3	3.9	32.4	12.7	13.2
EBITDA growth	42.8	20.0	27.5	16.6	4.2
EBIT growth	62.4	27.5	29.7	18.5	4.3
Pretax growth	63.9	27.3	30.0	18.5	4.3
Reported net profit growth	75.0	32.4	25.4	17.6	4.3
Core net profit growth	52.7	27.4	25.4	17.6	4.3
Profitability ratios (%)					
EBITDA margin	28.3	32.6	31.4	32.5	29.9
EBIT margin	23.0	28.2	27.6	29.1	26.8
Pretax profit margin	23.1	28.3	27.8	29.2	26.9
Payout ratio	30.1	37.9	34.0	34.0	34.0
DuPont analysis					
Net profit margin (%)	16.0	20.3	19.3	20.1	18.5
Revenue/Assets (x)	0.7	0.7	0.8	0.8	0.8
Assets/Equity (x)	1.4	1.4	1.3	1.3	1.3
ROAE (%)	17.2	19.7	21.5	22.1	20.0
ROAA (%)	12.3	14.3	16.1	17.0	15.7
Liquidity & Efficiency					
Cash conversion cycle	(4.4)	3.4	(5.3)	12.3	27.1
Days receivable outstanding	115.8	109.8	92.5	103.8	103.6
Days inventory outstanding	24.4	22.4	21.6	21.2	20.5
Days payables outstanding	144.6	128.7	119.5	112.7	97.1
Dividend cover (x)	3.3	2.6	2.9	2.9	2.9
Current ratio (x)	2.8	3.3	3.6	4.1	4.7
Leverage & Expense Analysis					
Asset/Liability (x)	4.1	4.4	5.3	5.8	6.5
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)	na	na	na	na	na
Debt/EBITDA (x)	0.1	0.1	0.0	0.0	0.0
Capex/revenue (%)	2.3	2.1	1.8	1.6	1.4
Net debt/ (net cash)	(136.3)	(208.3)	(212.0)	(263.4)	(310.5)

Source: Company; Maybank

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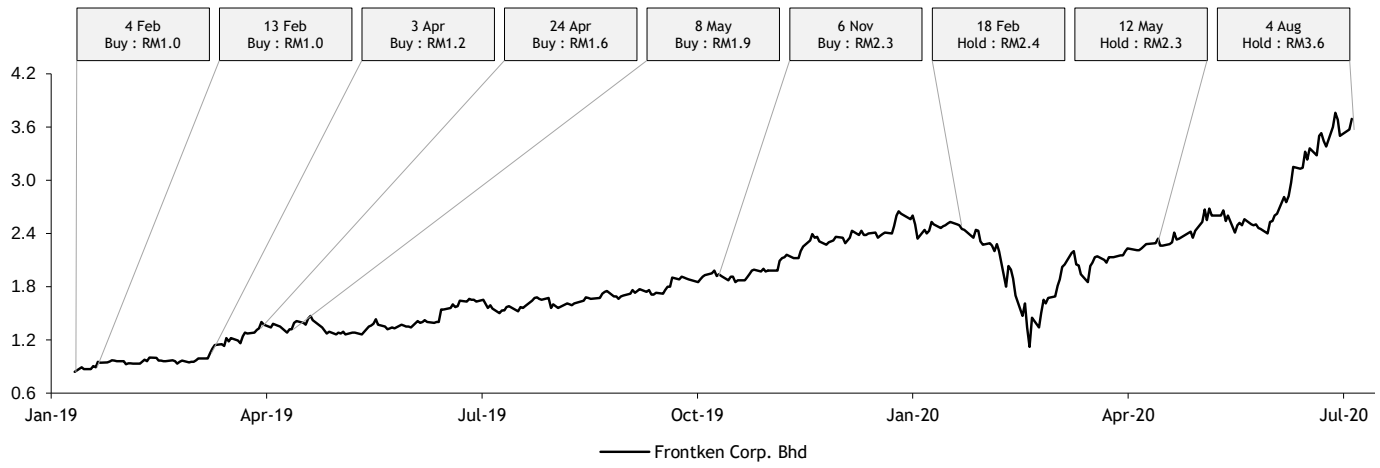

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