

**HLIB Research**

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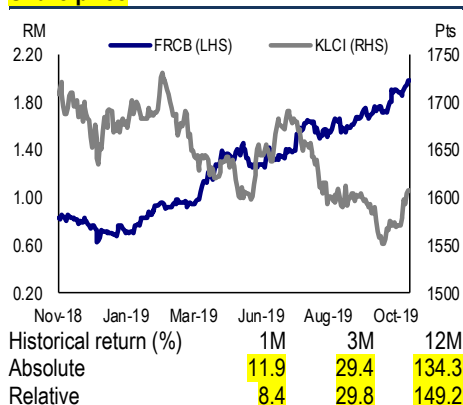
**HOLD** (Maintain)

**Target Price:** **RM2.40**
**Previously:** **RM2.14**
**Current Price:** **RM2.49**

Capital upside	-3.6%
Dividend yield	0.9%
Expected total return	-2.7%

**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)	2,075
3-mth average volume ('000)	6,105
SC Shariah compliant	Yes

**Major shareholders**

Dazzle Clean	27.8%
Ooi Keng Thye	14.5%
CIMB Group Holdings Bhd	5.7%

**Earnings summary**

	FY19	FY20f	FY21f
FYE (Dec)			
PATMI – core (RM m)	69.6	82.4	90.2
EPS – core (sen)	6.6	7.8	8.6
P/E (x)	37.7	31.8	29.1

# Frontken Corporation

## Concluded FY19 with flying colours

Frontken's FY19 core net profit of RM70m (+28% YoY) matched expectations. Relentless focus on operational excellence has yielded strong bottom line growth outpacing top line expansion. Outlook for both business segments remain positive, yet to see any Covid-19 impact: gaining new customers in semiconductor while O&G to leverage on Petronas appointment. Forecasts were unchanged but we lifted our TP to RM2.40, pegged to 28x of FY21 EPS. Maintain HOLD.

**Within expectations.** 4Q19 core net profit of RM19m (+5% QoQ, -3% YoY) brings FY19's total to RM70m (+28% YoY), which match expectations accounting for 97% of HLIB and consensus full year forecasts, respectively. 4Q19 one-off adjustment includes PPE disposal gain and forex loss (RM1m).

**Dividend.** The board declared a second single tier dividend of 1.5 sen (4Q18: 0.8 en) per share. FY19 total dividend amounted to 2.5 sen (FY18: 1.5 sen) per share (38% payout ratio), higher than our previous projection of 2.1 sen per share.

**QoQ.** Turnover gained 2% attributable to higher contributions from Taiwan (+6%), and Malaysia (+2%), offsetting the declines in Singapore (-7%), Philippines and Indonesia (-1%). In turn, core net profit grew 5% boosted by lower D&A (-17%) and effective corporate tax rate (4Q19: 20% vs 3Q19: 22%).

**YoY.** Top line was flattish driven by Taiwan's semiconductor (+8%) and Malaysia's O&G (+4%) businesses, but largely neutralized by Singapore and Philippines due to operational issues experienced by respective customers resulting in some works being requested to be put on hold. However, core earnings dipped 3% to RM19m due to lower EBITDA margin, higher effective corporate tax rate (4Q19: 20% vs 4Q18: 18%) and MI charge.

**FY19.** Revenue increased 4% to RM251m stimulated by Malaysia (+11%), Singapore (+7%) and Taiwan (+2%) offsetting the decline Philippines and Indonesia (-7%). However, core earnings strengthened 28% thanks to leaner operations where EBITDA margin gained 5ppt.

**Semiconductor.** Generated 78% (FY18: 80%) of group revenue in FY19. Frontken believes that the developments in the electronic and technology space will be positive for years to come. Despite the Covid-19 outbreak, it has yet to experience any impact and utilization was surprisingly high even during CNY. Getting orders from new clients in HDD (high volume with simple cleaning process) and solar players. It is in talks with an equipment maker who is setting up shop in Penang for new machine cleaning.

**O&G.** Accounted for the remaining 22% of group turnover in FY19 with sustainable profitability. The appointment as one of Petronas' panel contractors for the provision of manpower supply and mechanical rotating equipment services and parts augur well for the group in the next few years.

**FY20 capex.** Likely to be at the same level as FY19 (RM7-8m).

**Forecast.** Unchanged as results are in line.

Maintain **HOLD** while our TP is higher at **RM2.40**, pegged to 28x (previously 25x) of FY21 EPS. We 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); (4) favourable O&G market; and (5) strong balance sheet (net cash of RM223m or 21.2 sen per share).

## Financial Forecast

All items in (RM m) unless otherwise stated

### Income statement

FYE Dec	FY17	FY18	FY19	FY20f	FY21f
Revenue	296.6	327.2	339.9	376.8	404.7
COGS	(231.9)	(234.7)	(226.2)	(251.4)	(270.2)
EBITDA	64.7	92.6	113.7	125.4	134.5
D&A	(18.5)	(17.3)	(17.8)	(15.8)	(15.2)
EBIT	46.2	75.3	95.9	109.6	119.3
Net Interest Income	(0.1)	0.3	0.4	1.3	1.8
Associates	0.0	0.0	0.0	0.0	0.0
PBT	46.1	75.6	96.3	110.9	121.1
Tax	(9.7)	(18.6)	(22.0)	(23.4)	(25.6)
Net Profit	36.4	57.0	74.2	87.5	95.6
MI	(6.6)	(4.7)	(5.1)	(5.1)	(5.3)
PATAMI	29.9	52.3	69.2	82.4	90.2
Exceptionals	4.4	2.2	0.5	0.0	0.0
<b>Adj PATAMI</b>	<b>34.3</b>	<b>54.4</b>	<b>69.6</b>	<b>82.4</b>	<b>90.2</b>
Basic Shares (m)	1,053.0	1,053.0	1,053.0	1,053.0	1,053.0
Rep EPS (sen)	2.8	5.0	6.6	7.8	8.6
Adj EPS (sen)	3.3	5.2	6.6	7.8	8.6
Adj FD EPS (sen)	3.3	5.2	6.6	7.8	8.6

### Balance sheet

FYE Dec	FY17	FY18	FY19	FY20f	FY21f
Cash	119.3	133.0	197.2	253.3	323.3
Receivables	91.7	106.8	86.3	123.9	133.0
Inventories	13.5	13.7	15.1	13.8	14.8
Investment	2.0	0.0	0.0	0.0	0.0
PPE	150.0	140.4	145.5	128.1	122.9
Intangibles	33.8	33.8	33.8	33.8	33.8
Other Assets	20.8	27.4	37.9	27.4	27.4
<b>Total Assets</b>	<b>431.1</b>	<b>455.1</b>	<b>515.7</b>	<b>580.1</b>	<b>655.2</b>
Payables	79.8	82.4	84.0	89.5	96.2
ST borrowings	21.9	3.9	0.8	3.9	3.9
LT borrowings	11.5	7.5	0.0	7.5	7.5
Other Liabilities	11.8	16.5	32.1	16.5	16.5
<b>Total liabilities</b>	<b>125.1</b>	<b>110.4</b>	<b>117.0</b>	<b>117.5</b>	<b>124.2</b>
Shareholders' Funds	281.6	325.0	377.0	432.7	495.7
MI	24.4	19.6	21.8	29.9	35.3
Total S/H Equity	306.0	344.6	398.7	462.6	531.0
<b>Ttl Liab&amp;S/H Funds</b>	<b>431.1</b>	<b>455.1</b>	<b>515.7</b>	<b>580.1</b>	<b>655.2</b>

### Cashflow Analysis

FYE Dec	FY17	FY18	FY19	FY20f	FY21f
EBITDA	64.7	92.6	113.7	125.4	134.5
Tax Paid	(7.9)	(14.2)	(19.8)	(23.4)	(25.6)
WC Changes	6.9	(14.6)	21.3	(4.7)	(3.5)
Other	5.3	(0.4)	(0.3)	1.3	1.8
<b>CFO</b>	<b>69.0</b>	<b>63.3</b>	<b>114.9</b>	<b>98.6</b>	<b>107.2</b>
<b>FCF</b>	<b>48.9</b>	<b>55.8</b>	<b>107.9</b>	<b>88.6</b>	<b>97.2</b>
CAPEX (CF)	(20.2)	(7.5)	(7.0)	(10.0)	(10.0)
Acquisitions	(13.3)	(7.1)	(2.6)	0.0	0.0
Other	1.3	7.5	(2.4)	0.0	0.0
<b>CFI</b>	<b>(32.1)</b>	<b>(7.1)</b>	<b>(12.1)</b>	<b>(10.0)</b>	<b>(10.0)</b>
Dividend	(5.2)	(10.0)	(18.9)	(24.8)	(27.2)
Debt changes	0.0	(16.7)	(10.7)	0.0	0.0
Other	(3.2)	(1.1)	(4.2)	0.0	0.0
<b>CFF</b>	<b>(8.4)</b>	<b>(27.8)</b>	<b>(33.7)</b>	<b>(24.8)</b>	<b>(27.2)</b>
<b>Net Cashflow</b>	<b>28.6</b>	<b>28.4</b>	<b>69.1</b>	<b>63.8</b>	<b>70.0</b>

### Quarterly financial summary

FYE Dec	4Q18	1Q19	2Q19	3Q19	4Q19
Revenue	88.7	83.8	80.1	87.0	88.9
COGS	(60.2)	(56.5)	(52.5)	(56.4)	(60.9)
EBITDA	28.5	27.4	27.7	30.6	28.0
D&A	(4.3)	(4.8)	(4.6)	(4.6)	(3.8)
EBIT	24.2	22.6	23.0	26.0	24.3
Net Interest Income	0.2	(0.0)	0.1	0.1	0.2
Associates	0.0	0.0	0.0	0.0	0.0
PBT	24.4	22.5	23.1	26.1	24.5
Tax	(4.4)	(6.2)	(5.3)	(5.6)	(4.9)
Net Profit	20.0	16.3	17.8	20.5	19.6
MI	(1.3)	(0.9)	(1.3)	(1.4)	(1.4)
PATAMI	18.7	15.4	16.5	19.0	18.2
Exceptionals	0.9	(0.0)	0.8	(1.0)	0.7
<b>Adj PATAMI</b>	<b>19.6</b>	<b>15.4</b>	<b>17.3</b>	<b>18.0</b>	<b>18.9</b>
Basic Shares (m)	1,053.0	1,053.0	1,053.0	1,053.0	1,053.0
Rep EPS (sen)	1.8	1.5	1.6	1.8	1.7
Adj EPS (sen)	1.9	1.5	1.6	1.7	1.8
Adj FD EPS (sen)	1.9	1.5	1.6	1.7	1.8

### Valuation Ratios

FYE Dec	FY17	FY18	FY19	FY20f	FY21f
PER (x)	87.8	50.2	37.9	31.8	29.1
Core PER (x)	76.5	48.2	37.7	31.8	29.1
FD PER (x)	76.5	48.2	37.7	31.8	29.1
DPS (sen)	0.5	1.5	2.5	2.4	2.6
Net DY (%)	0.2	0.6	1.0	0.9	1.0
Book/share (sen)	26.7	30.9	35.8	41.1	47.1
P/Book (x)	9.3	8.1	7.0	6.1	5.3
FCF/share (sen)	4.6	5.3	10.2	8.4	9.2
FCF yield (%)	1.9	2.1	4.1	3.4	3.7
Mkt Cap	2,622.0	2,622.0	2,622.0	2,622.0	2,622.0
Net Cash(Debt)	85.8	121.5	196.3	241.8	311.9
EV	2,536.1	2,500.4	2,425.7	2,380.1	2,310.1
EV/EBITDA (x)	39.2	27.0	21.3	19.0	17.2
ROE (%)	12.2	16.7	18.5	19.0	18.2
Current Ratio (x)	2.2	2.9	3.5	4.2	4.7
Quick Ratio (x)	2.1	2.8	3.3	4.0	4.6
Interest Cover (x)	49.7	132.5	279.1	319.2	347.4

### Other Ratios

FYE Dec	FY17	FY18	FY19	FY20f	FY21f
Sales Growth (%)		10.3	3.9	10.9	7.4
EBITDA Growth (%)		43.1	22.8	10.3	7.2
EBIT Growth (%)		62.8	27.4	14.3	8.8
PBT Growth (%)		63.9	27.3	15.2	9.2
Net Profit Growth (%)		56.6	30.2	17.9	9.2
EBITDA Margin (%)	21.8	28.3	33.4	33.3	33.2
EBIT Margin (%)	15.6	23.0	28.2	29.1	29.5
PBT Margin (%)	15.6	23.1	28.3	29.4	29.9
Net Profit Margin (%)	12.3	17.4	21.8	23.2	23.6
Net Debt/Equity (%)	N Cash	N Cash	N Cash	N Cash	N Cash
CAPEX/Sales (%)	6.8	2.3	2.1	2.7	2.5

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

FYE Dec (RM m)	4Q18	3Q19	4Q19	QoQ	YoY	FY18	FY19	YoY
Revenue	88.7	87.0	88.9	2.1	0.3	327.2	339.9	3.9
EBITDA	28.5	30.6	28.0	(8.5)	(1.5)	92.6	113.7	22.8
EBITDA Margin	32.1	35.2	31.5			28.3	33.4	
EBIT	24.2	26.0	24.3	(6.7)	0.3	75.3	95.9	27.4
PBT	24.4	26.1	24.5	(6.2)	0.3	75.6	96.3	27.3
PAT	20.0	20.5	19.6	(4.4)	(2.1)	57.0	74.2	30.2
Reported PATMI	18.7	19.0	18.2	(4.5)	(2.6)	52.3	69.2	32.4
Core PATMI	19.6	18.0	18.9	5.1	(3.3)	54.4	69.6	27.9
Reported EPS (sen)	1.8	1.8	1.7	(4.5)	(2.6)	5.0	6.6	32.4
Core EPS (sen)	1.9	1.7	1.8	5.1	(3.3)	5.2	6.6	27.9

*Bursa, HLIB Research*

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<b>BUY</b>	Expected absolute return of +10% or more over the next 12 months.
<b>HOLD</b>	Expected absolute return of -10% to +10% 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.
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