November 3, 2020

Maybank IB Research

Frontken Corp. Bhd (FRCB MK)

A slight miss in 3Q20

HOLD

Share Price	MYR 3.53
12m Price Target	MYR 3.60 (+3%)
Previous Price Target	*MYR 3.60*

Maintain HOLD

3Q20 core net profit came in slightly below our estimates due to underperformance of the O&G segment, with 9M20 core earnings at 66%/67% of our/street's FY20 estimates. We tweak our FY20E earnings by -9% but maintain FY21-22E's. Our MYR3.60 TP is intact, pegged to unchanged 37x FY21E PER at approx. +2.0SD of mean due to their earnings resiliencies. Maintain HOLD. We believe current valuations have largely priced in upsides from the near-term semiconductor segment.

Semiconductor going strong, albeit some O&G easing

3Q20 core net profit was MYR19.8m (+4% YoY, -3% QoQ), taking 9M20 core earnings to MYR57.1m (+12% YoY). The higher 3Q20 earnings (YoY) were largely attributed to volume pick-up in the semiconductor segment - driven by higher demand and stronger order from its key Taiwanese customer, namely for the advanced nodes chips' equipment. Earnings, however, were partly eased by the weaker O&G segment which has affected revenue and margins (i.e. in Malaysia and Singapore), and marginally higher effective tax rate of 24% (+2ppt YoY). For 9M20 revenue split, semiconductor:O&G was 86%:14%.

Tweaking FY20E earnings

We lower our FY20E by 9% to mainly factor in softer O&G segment's earnings due to prolonged weakness from the O&G industry. Nonetheless, our FY21-22E earnings are intact – primarily underpinned by the continuation of favourable earnings growth of the semiconductor segment which would partly offset the softer O&G segment.

Outlook intact

We continue to favour near-term outlook of the broad semiconductor industry (i.e. higher demand for chips and higher wafer fab equipment spending), which in turn, could result in improved volume for Frontken. Elsewhere, we also note that Frontken is planning to expand its Taiwanese facilities (targeted completion in 2022) to take on more orders, namely the upcoming advanced nodes chips (i.e. 3nm and 2nm). However, details of the expansion have yet to be finalised at this point.

FYE Dec (MYR m)	FY18A	FY19A	FY20E	FY21E	FY22E
Revenue	327	340	415	507	574
EBITDA	92	114	130	165	172
Core net profit	54	72	79	102	106
Core EPS (sen)	5.2	6.9	7.5	9.7	10.1
Core EPS growth (%)	52.7	32.4	9.7	29.2	4.3
Net DPS (sen)	1.5	2.5	2.6	3.3	3.5
Core P/E (x)	13.6	33.4	46.9	36.3	34.8
P/BV (x)	2.3	6.4	8.8	7.6	6.6
Net dividend yield (%)	2.1	1.1	0.7	0.9	1.0
ROAE (%)	17.2	20.5	19.7	22.4	20.3
ROAA (%)	12.3	14.8	14.7	17.1	15.7
EV/EBITDA (x)	6.7	19.4	26.9	21.1	20.0
Net gearing (%) (incl perps)	net cash	net cash	net cash	net cash	net cash
Consensus net profit	-	-	86	104	109
MKE vs. Consensus (%)	-	-	(8.7)	(2.2)	(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.

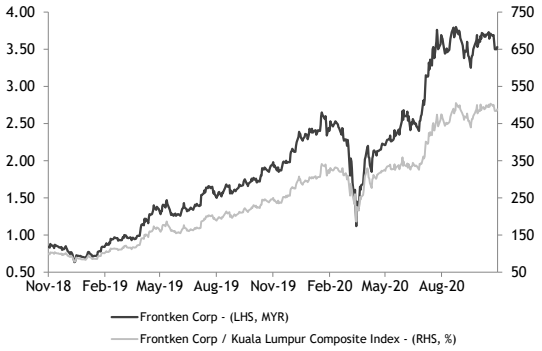
Statistics

52w high/low (MYR)	3.80/1.12
3m avg turnover (USDm)	3.4
Free float (%)	57.2
Issued shares (m)	1,053
Market capitalisation	MYR3.7B
	USD894M

Major shareholders:

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

Price Performance



	-1M	-3M	-12M
Absolute (%)	0	(1)	83
Relative to index (%)	2	6	99

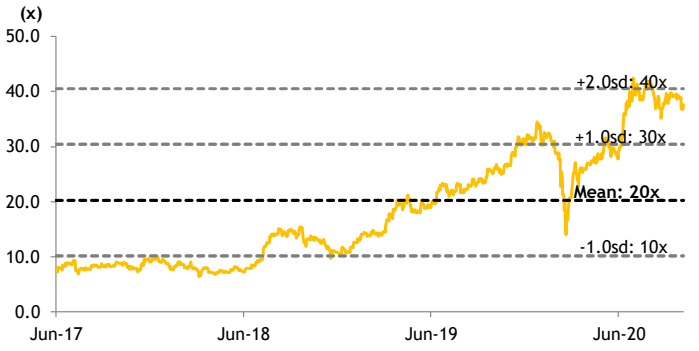
Source: FactSet

Fig 1: Results summary

FYE Dec (MYR'm)	Quarterly					Cumulative		
	3Q20	3Q19	%YoY	2Q20	%QoQ	9MFY20	9MFY19	%YoY
Revenue	94.8	87.0	*8.9*	87.6	*8.2*	267.3	251.0	*6.5*
EBITDA	**32.4**	**29.4**	***10.1***	**30.7**	***5.5***	**89.8**	**83.2**	***8.0***
Depreciation	(4.6)	(4.6)	*(0.5)*	(4.6)	*(0.4)*	(13.9)	(14.1)	*(1.2)*
Other income	2.5	1.2	*101.7*	1.7	*44.6*	6.5	2.5	*163.2*
EBIT	**30.3**	**26.0**	***16.3***	**27.8**	***8.9***	**82.4**	**71.6**	***15.2***
Finance income	0.2	0.3	*(18.5)*	0.3	*(24.1)*	1.0	0.8	*30.1*
Finance costs	(0.2)	(0.2)	*(14.1)*	(0.2)	*(10.7)*	(0.5)	(0.6)	*(15.9)*
Pretax profit	**30.3**	**26.1**	***16.1***	**27.9**	***8.6***	**83.0**	**71.8**	***15.6***
Tax expense	(7.3)	(5.6)	*30.0*	(6.1)	*20.5*	(19.9)	(17.1)	*16.2*
Minority interest	(1.7)	(1.4)	*15.8*	(1.5)	*10.3*	(1.7)	(1.4)	*15.8*
Net profit	**21.3**	**19.0**	***12.0***	**20.3**	***5.0***	**58.7**	**51.0**	***15.1***
Net profit ex-EI	**19.8**	**19.0**	***3.9***	**20.3**	***(2.6)***	**57.1**	**51.0**	***12.1***
Basic EPS (sen)	2.0	1.8	*12.1*	1.9	*5.2*	5.6	4.9	*15.0*
Margin (%)	**3Q20**	**3Q19**	**+/- ppt**	**2Q20**	**+/- ppt**	**9MFY20**	**9MFY19**	**+/- ppt**
EBIT	31.9	29.9	*2.0*	31.7	*0.2*	30.8	28.5	*2.3*
Pretax profit	32.0	30.0	*2.0*	31.9	*0.1*	31.0	28.6	*2.5*
Net profit ex-EI	20.9	21.9	*(1.0)*	23.2	*(2.3)*	21.4	20.3	*1.1*
Segmental revenue (MYR'm)	**3Q20**	**3Q19**	**%YoY**	**2Q20**	**%QoQ**	**9MFY20**	**9MFY19**	**%YoY**
Taiwan	64.2	48.7	*31.9*	58.9	*9.1*	175.3	137.6	*27.4*
Singapore	14.7	19.0	*(22.6)*	14.4	*1.7*	44.7	52.2	*(14.3)*
Malaysia	11.6	15.3	*(24.3)*	10.9	*6.4*	11.2	12.3	*(8.4)*
Philippines	4.2	3.9	*6.4*	3.2	*30.0*	35.5	48.4	*(26.8)*
Indonesia	0.1	0.1	*(20.0)*	0.2	*(47.0)*	0.6	0.6	*(1.2)*
Segmental EBIT (MYR'm)	**3Q20**	**3Q19**	**%YoY**	**2Q20**	**%QoQ**	**9MFY20**	**9MFY19**	**%YoY**
Taiwan	22.9	15.0	*52.9*	20.1	*14.0*	60.2	40.3	*49.1*
Singapore	4.5	7.4	*(38.7)*	5.5	*(17.4)*	15.4	18.3	*(15.7)*
Malaysia	2.6	3.2	*(19.7)*	1.1	*123.9*	5.8	11.1	*(47.7)*
Philippines	0.8	0.6	*46.8*	0.4	*119.5*	1.7	2.0	*(17.5)*
Indonesia	(0.5)	(0.1)	*647.1*	0.7	*(172.8)*	(0.6)	(0.2)	*217.6*
Segmental EBIT margin (%)	**3Q20**	**3Q19**	**+/- ppt**	**2Q20**	**+/- ppt**	**9MFY20**	**9MFY19**	**+/- ppt**
Taiwan	35.6	30.7	*4.9*	34.1	*1.5*	34.3	29.3	*5.0*
Singapore	30.8	39.0	*(8.1)*	38.0	*(7.1)*	34.5	35.0	*(0.6)*
Malaysia	61.1	80.9	*(19.8)*	35.5	*25.6*	16.4	23.0	*(6.6)*
Philippines	7.0	3.6	*3.4*	3.4	*3.6*	4.7	4.2	*0.5*
Indonesia	(450.9)	(48.3)	*(402.6)*	327.9	*(778.7)*	(108.0)	(33.6)	*(74.4)*

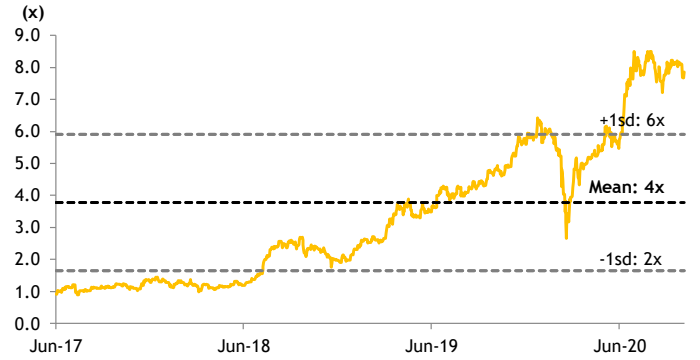
Source: Company data. Maybank Kim Eng

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	21.1	46.9	36.3	34.8
Core P/E (x)	13.6	33.4	46.9	36.3	34.8
P/BV (x)	2.3	6.4	8.8	7.6	6.6
P/NTA (x)	2.3	6.4	9.8	8.8	7.6
Net dividend yield (%)	2.1	1.1	0.7	0.9	1.0
FCF yield (%)	7.6	5.5	1.7	2.6	2.8
EV/EBITDA (x)	6.7	19.4	26.9	21.1	20.0
EV/EBIT (x)	8.3	22.4	31.0	23.6	22.3
INCOME STATEMENT (MYR m)					
Revenue	327.2	339.9	415.2	507.4	574.5
Gross profit	126.6	148.1	177.4	216.6	226.2
EBITDA	92.5	113.7	130.1	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	98.6	113.1	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	99.0	113.9	148.2	154.6
Income tax	(18.6)	(22.0)	(27.3)	(35.6)	(37.1)
Minorities	(4.7)	(5.1)	(7.6)	(10.7)	(11.2)
Discontinued operations	0.0	0.0	0.0	0.0	0.0
Reported net profit	52.3	71.9	78.9	102.0	106.4
Core net profit	54.3	71.9	78.9	102.0	106.4
BALANCE SHEET (MYR m)					
Cash & Short Term Investments	149.9	225.4	222.8	264.2	311.3
Accounts receivable	113.6	93.7	126.9	155.1	175.6
Inventory	13.7	15.1	14.8	18.1	21.6
Reinsurance assets	0.0	0.0	0.0	0.0	0.0
Property, Plant & Equip (net)	140.4	125.7	133.7	141.7	149.7
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	22.0	23.4	23.4	23.0
Total assets	**455.1**	**515.7**	**555.5**	**636.3**	**715.1**
ST interest bearing debt	4.8	0.8	2.7	2.7	2.7
Accounts payable	81.6	84.0	86.8	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	20.0	15.0	15.0	15.0
Total Liabilities	**110.4**	**117.0**	**106.3**	**112.8**	**114.0**
Shareholders Equity	324.4	377.0	422.4	489.7	559.9
Minority Interest	19.6	21.8	26.8	33.9	41.2
Total shareholder equity	**344.0**	**398.7**	**449.2**	**523.5**	**601.1**
Total liabilities and equity	**454.4**	**515.7**	**555.5**	**636.3**	**715.1**
CASH FLOW (MYR m)					
Pretax profit	75.6	99.0	113.9	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	(30.1)	(25.0)	(22.9)
Cash taxes paid	(14.2)	(19.8)	(27.3)	(35.6)	(37.1)
Other operating cash flow	(0.4)	1.2	0.0	0.0	0.0
Cash flow from operations	63.3	138.6	72.7	104.3	111.8
Capex	(7.5)	(7.0)	(8.0)	(8.0)	(8.0)
Free cash flow	55.8	131.5	64.7	96.3	103.8
Dividends paid	(10.0)	(19.9)	(29.4)	(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	94.4	36.0	58.9	64.6

FYE 31 Dec	FY18A	FY19A	FY20E	FY21E	FY22E
Key Ratios					
Growth ratios (%)					
Revenue growth	10.3	3.9	22.1	22.2	13.2
EBITDA growth	42.8	22.9	14.5	26.7	4.2
EBIT growth	62.4	31.1	14.7	30.3	4.3
Pretax growth	63.9	30.9	15.0	30.2	4.3
Reported net profit growth	75.0	37.6	9.8	29.2	4.3
Core net profit growth	52.7	32.4	9.7	29.2	4.3
Profitability ratios (%)					
EBITDA margin	28.3	33.4	31.3	32.5	29.9
EBIT margin	23.0	29.0	27.2	29.1	26.8
Pretax profit margin	23.1	29.1	27.4	29.2	26.9
Payout ratio	30.1	36.4	34.0	34.0	34.0
DuPont analysis					
Net profit margin (%)	16.0	21.2	19.0	20.1	18.5
Revenue/Assets (x)	0.7	0.7	0.7	0.8	0.8
Assets/Equity (x)	1.4	1.4	1.3	1.3	1.3
ROAE (%)	17.2	20.5	19.7	22.4	20.3
ROAA (%)	12.3	14.8	14.7	17.1	15.7
Liquidity & Efficiency					
Cash conversion cycle	(4.4)	(18.6)	(11.1)	8.9	27.1
Days receivable outstanding	115.8	109.8	95.6	100.1	103.6
Days inventory outstanding	24.4	27.0	22.6	20.3	20.5
Days payables outstanding	144.6	155.4	129.3	111.5	97.1
Dividend cover (x)	3.3	2.7	2.9	2.9	2.9
Current ratio (x)	2.8	3.3	3.5	4.0	4.5
Leverage & Expense Analysis					
Asset/Liability (x)	4.1	4.4	5.2	5.6	6.3
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)	na	na	na	na	na
Debt/EBITDA (x)	0.1	0.1	0.0	0.0	0.0
Capex/revenue (%)	2.3	2.1	1.9	1.6	1.4
Net debt/ (net cash)	(136.3)	(212.6)	(218.8)	(260.1)	(307.3)

Source: Company; Maybank

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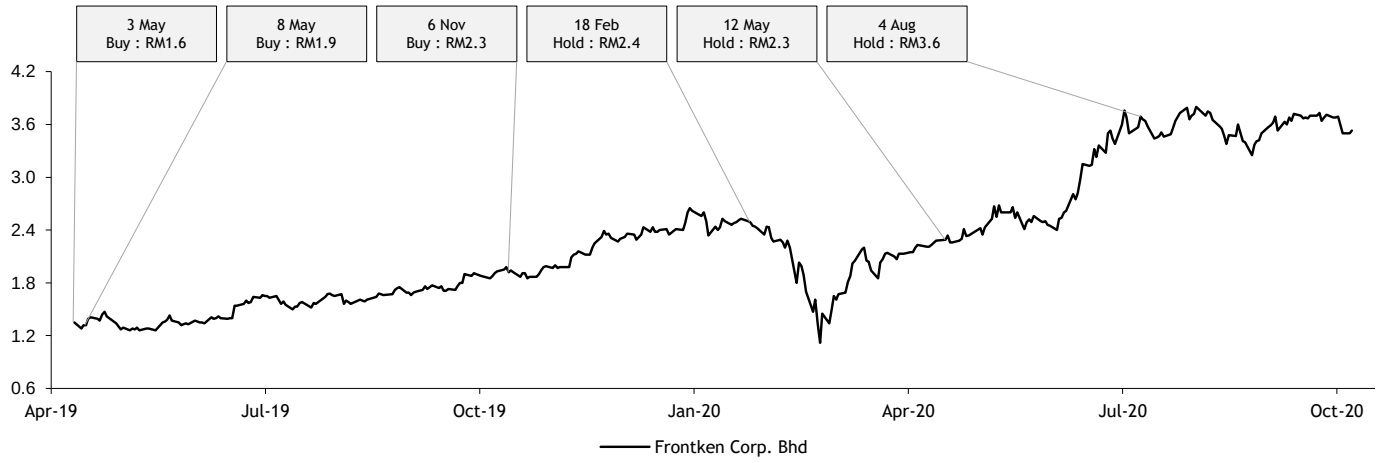

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