Technology

Singapore

February 28, 2020

Venture (VMS SP)

Positioned to benefit

BUY

Share Price	SGD 16.51
12m Price Target	SGD 18.23 (+15%)
Previous Price Target	*SGD 18.23*

FY19 slightly ahead; maintain BUY

4Q19 net profit fell 10.6% YoY to SGD96.2m amid a challenging operating environment, but was still a beat. VMS expects to largely fulfil 1Q20 backlog in 2Q20, and also expects a stronger 2H20, supported by new and existing customers. MKE D-Lab recently conducted a sentiment poll, which suggests that investors are broadly bullish on VMS' share price performance in 2020. Our forecasts, BUY rating, and ROE-g/COE-g TP of SGD18.23 (2x FY20E P/B) are maintained.

Maintains c.10% net margin in FY19E

4Q19 revenue rose 2.9% to SGD932.1m. Management attributed the relative stability despite a challenging environment to VMS' i) well diversified customer base, and ii) participation in domains such as life-science, instrumentation, healthcare & wellness. VMS achieved net margin of 10% in FY19 (FY18: 10.6%), reinforcing our confidence that the current level of elevated profitability (FY10-16 net margin range: 5-7%) is sustainable in light of VMS' continual pursuit for operational excellence, and value add it provides to customers.

NPIs in 2H20; beneficiary of S.E. Asian footprint

VMS anticipates a stronger 2H20 HoH as it supports new product introductions (NPI) across several domains. We believe this is consistent with our expectations for YoY earnings recovery in 2H20 (see Venturing into a 2H20 recovery). Further, VMS expects to gain growth momentum beyond 2020 with several new partners in life science & genomics and healthcare & wellness. Regarding Covid-19, production capacity outside China is intact, and that within China is largely restored. As VMS races to secure components, it anticipates to clear 1Q20 backlog in 2Q20, and is well positioned to see increased wallet share from customers whose production capacity are still affected.

D-Lab suggests investors are bullish on VMS

D-Lab conducted an investor sentiment poll in the first half of Feb-20. Of 21 respondents, 52.4% are bullish on VMS' share price performance in 2020. Among top 2 concerns that are likely to affect VMS' fundamentals in 2020 are i) supply chain disruptions from Covid-19 (86%) and ii) trade-related headwinds (52%). Final and full year DPS of SGD0.50/SGD0.70 maintained, translating to 4.2% yield.

FYE Dec (SGD m)	FY18A	FY19A	FY20E	FY21E	FY22E
Revenue	3,485	3,633	3,768	3,994	4,114
EBITDA	456	448	463	493	479
Core net profit	369	362	371	395	382
Core FDEPS (cts)	127.4	124.9	127.5	135.8	131.4
Core FDEPS growth(%)	1.4	(2.0)	2.1	6.5	(3.2)
Net DPS (cts)	70.0	70.0	70.0	70.0	70.0
Core FD P/E (x)	10.9	13.0	12.9	12.2	12.6
P/BV (x)	1.7	1.9	1.8	1.7	1.6
Net dividend yield (%)	5.0	4.3	4.2	4.2	4.2
ROAE (%)	16.3	14.9	14.4	14.3	13.0
ROAA (%)	11.6	11.2	11.1	11.2	10.2
EV/EBITDA (x)	7.2	8.8	8.6	7.7	7.7
Net gearing (%) (incl perps)	net cash	net cash	net cash	net cash	net cash
Consensus net profit	-	-	381	395	na
MKE vs. Consensus (%)	-	-	(2.7)	0.0	na

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Company Description

Venture is an EMS and ODM provider with manufacturing facilities in Singapore, Malaysia, and China.

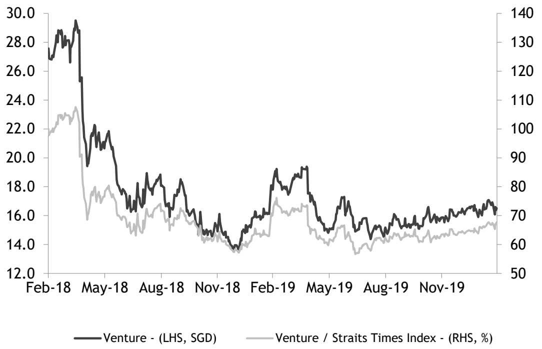
Statistics

52w high/low (SGD)	19.39/14.37
3m avg turnover (USDm)	12.3
Free float (%)	91.0
Issued shares (m)	290
Market capitalisation	SGD4.8B
	USD3.4B

Major shareholders:

WONG NGIT LIONG	7.0%
Schroder Investment Management (Singapor	4.9%
The Vanguard Group, Inc.	2.5%

Price Performance



	-1M	-3M	-12M
Absolute (%)	0	4	(7)
Relative to index (%)	4	8	(3)

Source: FactSet

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Additional takeaways:

- On Covid-19, management clarified China production accounts for less than 10% of capacity. VMS' China workforce has largely returned, and VMS also has the flexibility to route production to other non-China sites. As such, we view that a production bottleneck will likely be a result of global components shortage, and/ or other disruptions along the supply chain. Management is continually monitoring the situation on components.

- On NPIs in 2H20, selected domains highlighted by VMS are i) life science, ii) healthcare & wellness, iii) instrumentation, and iv) networking & communication.

- VMS is making plans to construct two buildings at its Batu Kawan land in Penang, Malaysia. This, while expected to introduce a decent amount of capacity, is only expected to come on stream in the coming years. Our capex forecasts have not factored in such plans owing to a lack of details currently.

- We see upside to our FY20E forecast if Covid-19 does not derail a recovery in most of VMS' end-markets, especially in 2H20. We believe a key risk is that deterioration in end-market outlook may result in delayed NPIs, and/ or lower volumes.

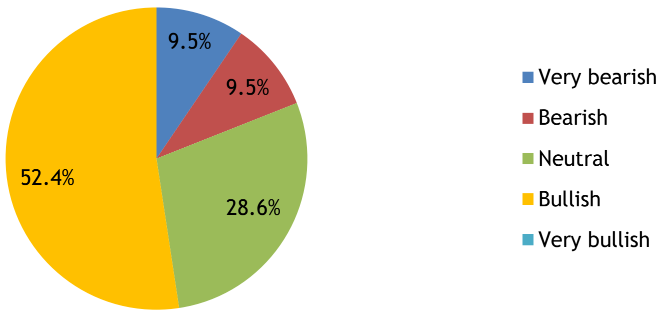
Our ROE-g/COE-g TP is based on FY20-22E average ROE of 13.9% and LTG of 2%. We continue to expect VMS to sustain full year DPS of SGD0.70 during our forecast horizon, which translates to a respectable 4.2% yield.

Fig 1: P&L summary

FYE Dec	4Q19	4Q18	3Q19	YoY Chg	QoQ Chg	FYE	FY19A vs MKE
	(SGD m)	(SGD m)	(SGD m)	(%)	(%)	SGDm	
Revenue	932.1	905.9	869.1	2.9	7.2	3,589.1	101.2
COGS	(694.4)	(661.7)	(652.5)	4.9	6.4	(2,699.0)	101.0
Gross profit	237.7	244.2	216.7	-2.7	9.7	890.1	101.9
Total SGA	(85.3)	(76.8)	(82.2)	11.2	3.8	(326.6)	102.0
R&D expenses	(11.9)	(14.7)	(8.5)	-19.2	40.1	(32.3)	113.2
Other op. income	0.2	0.4	0.1	-49.1	29.3	2.0	37.3
Other op. exp	(22.5)	(23.5)	(20.4)	-4.1	10.4	(93.0)	96.3
EBIT	107.3	121.9	95.6	-12.0	12.3	403.3	101.5
EBITDA	118.2	129.6	105.7	-8.8	11.8	440.2	101.8
Interest inc	2.7	2.9	3.2	-6.0	-14.1	10.0	110.1
Interest exp	(0.2)	(0.2)	(0.2)	-34.3	-2.5	(0.0)	1711.1
Associates	0.0	(0.1)	0.0	-100.0	nm	0.0	nm
Exceptionals	0.0	0.0	0.0	nm	nm	0.0	nm
Pretax profit	109.9	124.5	98.6	-11.8	11.4	413.3	101.6
Taxation	(13.6)	(16.8)	(13.2)	-19.2	2.9	(59.9)	94.5
Net profit	96.3	107.7	85.4	-10.6	12.8	353.3	102.8
Minority interest	0.0	(0.0)	0.2	nm	-92.8	0.2	125.5
PATMI	96.3	107.7	85.2	-10.6	13.0	353.1	102.8
Core PATMI	96.3	107.7	85.2	-10.6	13.0	353.1	102.8
EPS (SGD)	0.33	0.38	0.30	-10.9	13.2	1.2	102.8
					Change (ppt)		
Gross material margin	25.5%	27.0%	24.9%	-1.5	0.6		
EBIT margin	11.5%	13.5%	11.0%	-1.9	0.5		
Core net margin	10.3%	11.9%	9.8%	-1.6	0.5		

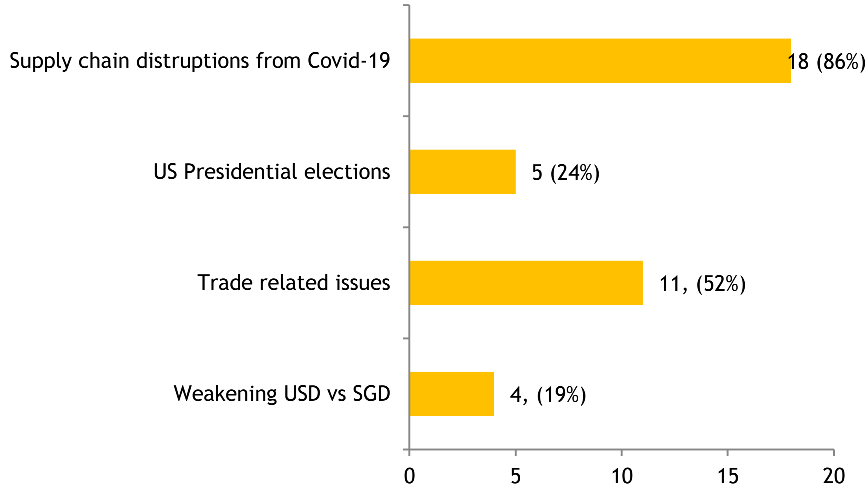
Source: Company, Maybank Kim Eng

Fig 2: "Are you bullish or bearish on Venture Corp's (VMS SP) stock performance in 2020?" (21 responses)



Source: Maybank Kim Eng

Fig 3: "What are your top 2 concerns that will affect Venture's fundamentals in 2020?" (21 responses)

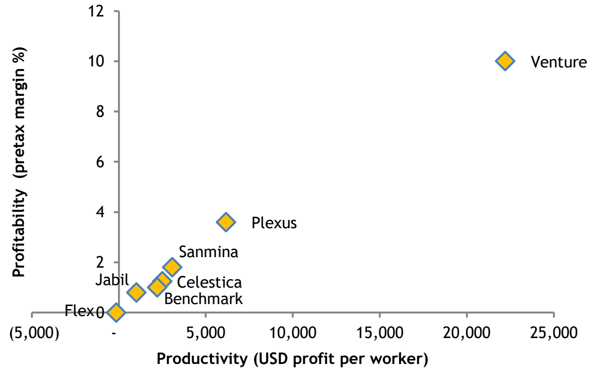


Source: Maybank Kim Eng

Value Proposition

- VMS is an EMS company that has been consistently creating value for its customers. Able to design complex industrial products and reduce time-to-market.
- Facing pricing pressure and increased competition. However, margins are still industry leading.
- Good diversification with >100 active customers, many of them blue chips.
- Good exposure to test & measurement, and life-science customers, still largely underpenetrated due to regulatory requirements and high specs.

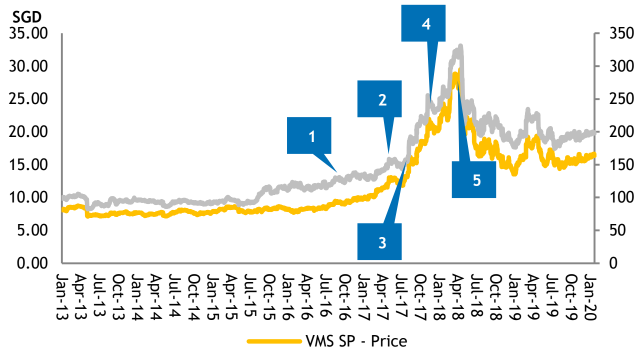
Industry-leading profitability and productivity



Source: Bloomberg, Companies

Price Drivers

Historical share price trend



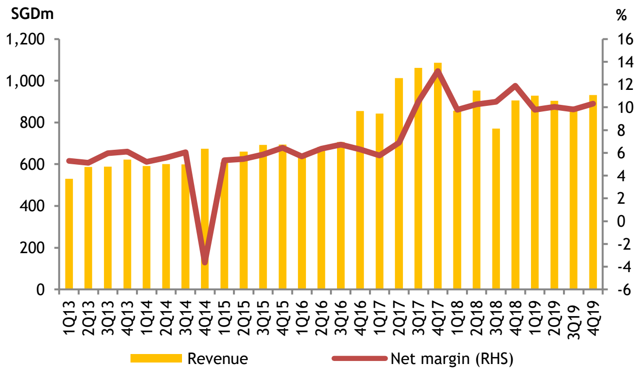
Source: Company, FactSet, Maybank Kim Eng

1. Street raised TPs for the first time in two years following strong 3Q/4Q16 earnings.
2. Strong 2Q17. Increasing market familiarity with the potential of VMS emanating from Illumina and cloud / 5G network spending.
3. CEO Wong Ngit Liong bought 400,000 shares at SGD15.26.
4. Strong 3Q17; management raised net-margin guidance.
5. Short-seller report alleging weaker-than-expected Philip Morris IQOS device growth would have knock-on effects on VMS.

Financial Metrics

- We expect VMS' to resume YoY earnings growth in 2H20 as it ramps up production of new products for customers.
- Operating margins should be steady from more products with higher R&D content & cost control.
- Net cash since 2008. Healthy FCF levels in FY19-21E could provide upside for dividends.

New level of profitability



Source: Company

Swing Factors

Upside

- Better-than-expected reception for high-growth products.
- Stronger US / global economy.
- Moderate USD strength as the revenue of VMS is entirely in USD.

Downside

- M&A among customers, and acquisitions of customers by competitors could disrupt orders.
- Excessive USD strength may erode customers' competitiveness. Excessive USD weakness may weaken its SGD earnings.
- Holding more inventories at its major hubs due to higher customer demand. This would tie up working capital.

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FYE 31 Dec	FY18A	FY19A	FY20E	FY21E	FY22E
Key Metrics					
P/E (reported) (x)	15.5	12.8	12.8	12.0	12.5
Core P/E (x)	10.8	12.9	12.8	12.0	12.5
Core FD P/E (x)	10.9	13.0	12.9	12.2	12.6
P/BV (x)	1.7	1.9	1.8	1.7	1.6
P/NTA (x)	1.7	1.9	1.8	1.7	1.6
Net dividend yield (%)	5.0	4.3	4.2	4.2	4.2
FCF yield (%)	4.3	5.0	6.1	8.5	6.5
EV/EBITDA (x)	7.2	8.8	8.6	7.7	7.7
EV/EBIT (x)	7.8	9.7	9.3	8.3	8.3
INCOME STATEMENT (SGD m)					
Revenue	3,484.6	3,633.4	3,767.9	3,993.9	4,113.8
Gross profit	953.8	906.8	934.4	998.5	1,020.2
EBITDA	455.5	448.2	463.3	492.8	479.3
Depreciation	(30.7)	(38.7)	(34.6)	(35.6)	(36.6)
Amortisation	(1.1)	(1.0)	(1.0)	(1.0)	(1.0)
EBIT	423.7	408.5	427.7	456.2	441.7
Net interest income /(exp)	8.2	10.5	9.0	9.0	8.5
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	431.9	419.0	436.7	465.2	450.2
Income tax	(62.9)	(56.6)	(65.5)	(69.8)	(67.5)
Minorities	(0.2)	(0.3)	(0.2)	(0.2)	(0.2)
Discontinued operations	0.0	0.0	0.0	0.0	0.0
Reported net profit	368.8	362.1	371.0	395.2	382.5
Core net profit	368.8	362.1	371.0	395.2	382.5
BALANCE SHEET (SGD m)					
Cash & Short Term Investments	712.8	714.5	784.3	986.5	1,093.9
Accounts receivable	735.9	898.9	856.0	938.6	932.4
Inventory	808.2	706.2	815.4	826.0	886.1
Property, Plant & Equip (net)	230.7	231.7	224.6	218.5	213.1
Intangible assets	639.9	667.5	667.5	667.5	667.5
Investment in Associates & JVs	0.7	0.8	0.8	0.8	0.8
Other assets	76.4	54.7	46.2	46.2	46.2
Total assets	**3,204.6**	**3,274.2**	**3,394.7**	**3,684.1**	**3,840.0**
ST interest bearing debt	1.8	1.1	1.1	1.1	1.1
Accounts payable	529.0	490.3	518.8	613.7	589.8
LT interest bearing debt	0.0	0.0	0.0	0.0	0.0
Other liabilities	322.0	284.0	207.0	208.0	207.0
Total Liabilities	**852.5**	**775.7**	**726.9**	**822.7**	**797.9**
Shareholders Equity	2,349.9	2,496.2	2,665.3	2,858.6	3,039.1
Minority Interest	2.2	2.4	2.6	2.8	3.0
Total shareholder equity	**2,352.1**	**2,498.6**	**2,667.9**	**2,861.4**	**3,042.1**
Total liabilities and equity	**3,204.6**	**3,274.2**	**3,394.7**	**3,684.1**	**3,840.0**
CASH FLOW (SGD m)					
Pretax profit	431.9	419.0	436.7	465.2	450.2
Depreciation & amortisation	31.8	39.7	35.6	36.6	37.6
Adj net interest (income)/exp	0.0	0.0	0.0	0.0	0.0
Change in working capital	(170.9)	(125.8)	(89.3)	2.7	(78.8)
Cash taxes paid	(56.3)	(61.7)	(65.5)	(69.8)	(67.5)
Other operating cash flow	0.0	0.0	0.0	0.0	0.0
Cash flow from operations	236.6	271.1	317.5	434.7	341.5
Capex	(63.6)	(39.7)	(27.5)	(29.6)	(31.2)
Free cash flow	173.0	231.4	290.1	405.1	310.3
Dividends paid	(230.0)	(201.9)	(201.9)	(201.9)	(201.9)
Equity raised / (purchased)	41.5	7.9	0.0	0.0	0.0
Change in Debt	(29.0)	(0.7)	0.0	0.0	0.0
Other invest/financing cash flow	3.8	(35.9)	(18.3)	(1.0)	(1.0)
Effect of exch rate changes	0.0	0.0	0.0	0.0	0.0
Net cash flow	(40.7)	0.6	69.8	202.2	107.4

FYE 31 Dec	FY18A	FY19A	FY20E	FY21E	FY22E
Key Ratios					
Growth ratios (%)					
Revenue growth	(13.0)	4.3	3.7	6.0	3.0
EBITDA growth	(0.8)	(1.6)	3.4	6.4	(2.7)
EBIT growth	(0.7)	(3.6)	4.7	6.7	(3.2)
Pretax growth	(2.4)	(3.0)	4.2	6.5	(3.2)
Reported net profit growth	(0.8)	(1.8)	2.5	6.5	(3.2)
Core net profit growth	2.3	(1.8)	2.5	6.5	(3.2)
Profitability ratios (%)					
EBITDA margin	13.1	12.3	12.3	12.3	11.7
EBIT margin	12.2	11.2	11.4	11.4	10.7
Pretax profit margin	12.4	11.5	11.6	11.6	10.9
Payout ratio	54.4	55.7	54.4	51.1	52.8
DuPont analysis					
Net profit margin (%)	10.6	10.0	9.8	9.9	9.3
Revenue/Assets (x)	1.1	1.1	1.1	1.1	1.1
Assets/Equity (x)	1.4	1.3	1.3	1.3	1.3
ROAE (%)	16.3	14.9	14.4	14.3	13.0
ROAA (%)	11.6	11.2	11.1	11.2	10.2
Liquidity & Efficiency					
Cash conversion cycle	105.1	113.7	116.4	111.5	111.5
Days receivable outstanding	77.6	81.0	83.8	80.9	81.9
Days inventory outstanding	107.2	100.0	96.7	98.6	99.6
Days payables outstanding	79.7	67.3	64.1	68.1	70.0
Dividend cover (x)	1.8	1.8	1.8	2.0	1.9
Current ratio (x)	2.7	3.1	3.4	3.4	3.7
Leverage & Expense Analysis					
Asset/Liability (x)	3.8	4.2	4.7	4.5	4.8
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)	0.0	0.0	0.0	0.0	0.0
Capex/revenue (%)	1.8	1.1	0.7	0.7	0.8
Net debt/ (net cash)	(711.0)	(713.4)	(783.3)	(985.5)	(1,092.9)

Source: Company; Maybank

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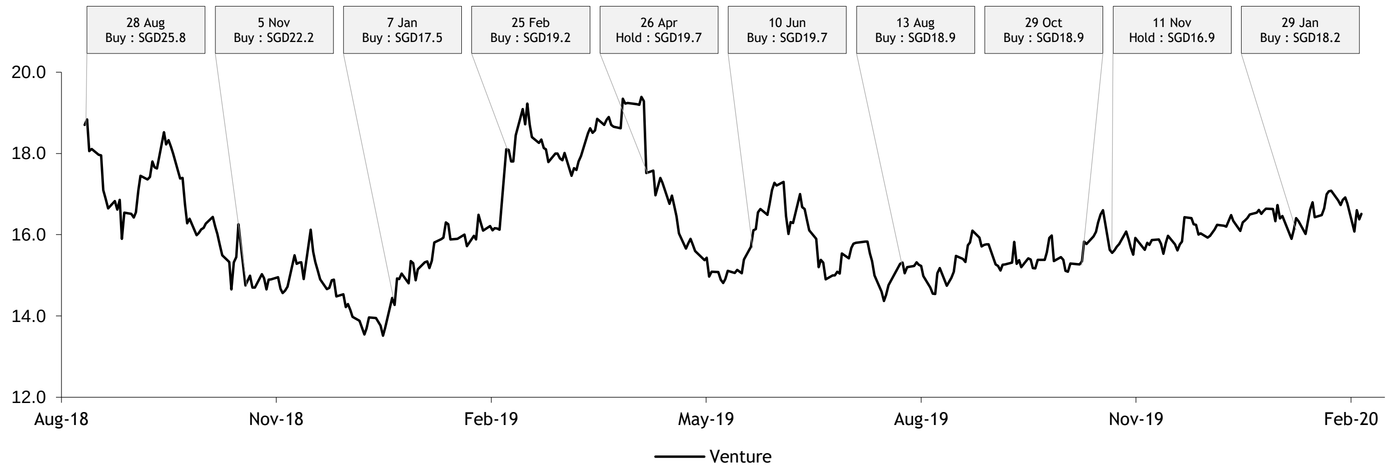
Historical recommendations and target price: Venture (VMS SP)



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