Maybank Kim Eng

Technology

Singapore

AEM Holdings (AEM SP)

Just a speedbump

BUY

Share Price	SGD 3.79
12m Price Target	SGD 5.56 (+49%)
Previous Price Target	*SGD 5.05*

Focus on FY22E recovery; BUY

1Q21 PATMI of SGD13.2 (-63.4% YoY) was weak as expected, due to an exceptionally high 1Q20, and cyclical softness ahead of volume ramp for new generation test handlers. We cut FY21E EPS by 23% to factor in margin dilution from CEI, but raise FY22E EPS by 4% to factor in our optimism of earnings recovery. Our TP is now higher at SGD5.56, as we roll forward to 14x FY22E P/E (prev: 14x FY21E) as we believe investors should focus on the recovery potential instead of transitory weakness. BUY.

Volume ramp for next gen test handlers in 2H21

1Q21 revenue fell 45.3% YoY, as Intel's demand for equipment and consumables drove an exceptionally strong 1Q20 and FY20. Our FY21E revenue of SGD518m is at the higher end of SGD460-520m guidance. 1H21 revenue YoY is expected to be lower, and AEM expects strong recovery in 2H21 into 2022 as next generation tools – catered for high-performance computing (HPC) – enter volume production.

Diversification efforts bearing fruits

AEM expects to derive meaningful revenue from 10 out of the top 20 semiconductor companies (spanning mobility, memory and high performance computing) in FY22. This is positive as it validates the proposition of AEM's SLT solutions as advanced packaging technologies become increasingly mainstream. This is important, in our view, as it should help investors transition their view of AEM from being just an "Intel-focused" play into a truly "system level test" play, properly leveraged to heterogeneous packaging – which in turn rides on significant trends in HPC, 5G/AI, mobility and so on.

We expect YoY growth to revert in 4Q21

As our concerns for cyclical softness have now materialised, and because we see this as transitory, we believe investors should focus at the realignment of cyclical recovery alongside structural growth momentum of AEM's growth story. Following this set of results, we believe street might cut TPs, which may introduce further short-term volatility. We would accumulate on any dips, as we believe AEM should revert to YoY growth in 4Q21.

FYE Dec (SGD m)	FY19A	FY20A	FY21E	FY22E	FY23E
Revenue	323	519	518	670	757
EBITDA	70	122	104	145	169
Core net profit	53	98	78	112	132
Core FDEPS (cts)	19.4	35.1	27.6	39.7	46.7
Core FDEPS growth(%)	58.3	80.9	(21.4)	43.9	17.5
Net DPS (cts)	5.1	9.0	7.0	10.0	11.8
Core FD P/E (x)	10.4	9.8	13.7	9.5	8.1
P/BV (x)	4.1	4.5	3.9	3.0	2.3
Net dividend yield (%)	2.5	2.6	1.8	2.6	3.1
ROAE (%)	47.3	56.4	32.5	36.0	32.7
ROAA (%)	29.1	34.6	21.7	25.4	23.9
EV/EBITDA (x)	6.3	6.7	9.3	6.0	4.6
Net gearing (%) (incl perps)	net cash	net cash	net cash	net cash	net cash
Consensus net profit	-	-	102	107	109
MKE vs. Consensus (%)	-	-	(23.5)	5.3	21.4

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Company Description

AEM manufactures equipment used in the semiconductor back-end process

Statistics

52w high/low (SGD)	4.62/2.53
3m avg turnover (USDm)	12.9
Free float (%)	83.5
Issued shares (m)	282
Market capitalisation	SGD1.1B
	USD803M

Major shareholders:

Toh Ban Leng James	5.0%
Aberdeen Standard Investments (Asia) Ltd	5.0%
UBS Group AG	4.9%

Price Performance

	-1M	-3M	-12M
Absolute (%)	(10)	(14)	60
Relative to index (%)	(10)	(21)	29

Source: FactSet

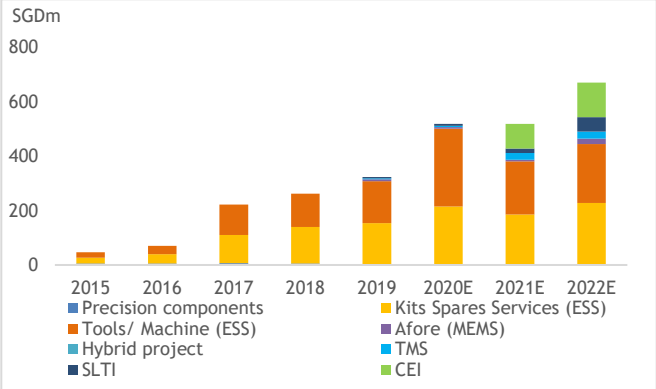
ESG@MKE
Tear Sheet Insert

Co. Reg No: 198700034E MICA (P) : 099/03/2012

Value Proposition

- Back-end test-equipment manufacturer that has co-developed the HDMT handler for a market-leading chipmaker with a market cap of USD210b.
- Leading-edge HDMT technology has helped its core customer achieve 2x savings in chip-testing costs.
- AEM provides strong synergies like field-service capabilities and manufacturing scale for the high-tech companies that it acquires.
- High single-customer and product risks.

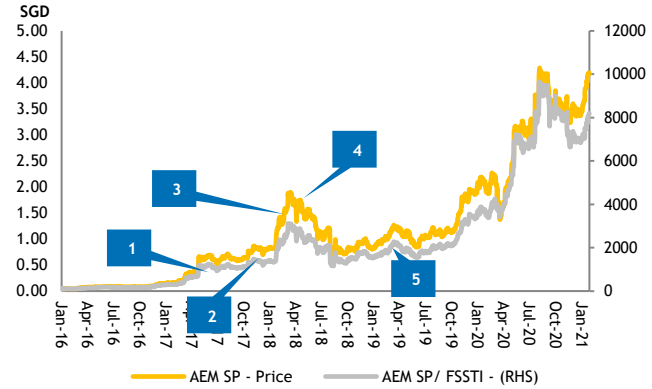
Share of new revenue sources progressively growing



Source: Company, Maybank Kim Eng

Price Drivers

Historical share price trend



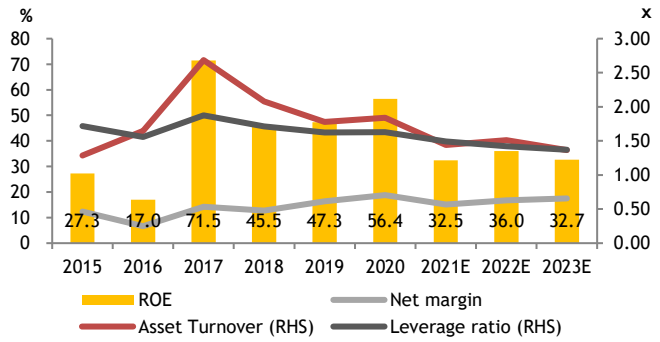
Source: Company, FactSet, Maybank Kim Eng

1. Announced favourable 1Q17 net profit as HDMT handlers delivery pick up momentum. There were also insider purchases.
2. Announced 2018 guidance for SGD255m in revenue and SGD42m PBT.
3. Announced accretive acquisition of Afore, Finnish-based MEMS test-solutions provider.
4. Novo Tellus distributes AEM shares in-specie to investors; Core customer announces 10nm delay.
5. AEM's core customer denies rumours from tech-blog SemiAccurate that its 10nm process was cancelled.

Financial Metrics

- Over time, we expect increasing contributions from non-Intel revenue sources.
- AEM is not a capex-intensive company. Improved cash-flow from 2016 levels has allowed AEM to pursue highly synergistic acquisitions.
- Training a batch of engineers during pre-production ramp up could take 5-6 months. During such time, staff costs could be elevated and profitability could temporarily decline.
- Adopted 25% dividend payout ratio policy in 2017.

DuPont ROE



Source: Company, Maybank Kim Eng

Swing Factors

Upside

- Revenue expansion from securing new customers or wallet expansion/increased orders from existing customers.
- Synergistic and accretive acquisitions.
- Positive customer-related news flow that could catalyse improved orders for AEM, such as capacity expansion or launch of new chips.

Downside

- Order cancellation, delays and earnings misses.
- Emerging technology from rivals that could erode AEM's competitive position with customer(s).
- Erosion in the competitive advantages of the core customer as a result of company specific or industry related developments.

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Business Model & Industry Issues

- As an equipment maker, AEM is inherently exposed to environmental, workplace safety, and socio-economic risks. AEM has had zero incidences of environmental non-compliance, as well as zero substantiated cases of corruption and legal compliance issues in 2019.
- From an environmental and social perspective, AEM screens all of its suppliers. AEM constantly strives to be more efficient with electricity usage, and ensures employees are well trained and remunerated fairly.
- AEM is recognised for good transparency with shareholders, while still being able to balance business requirements (e.g. respecting non-disclosure agreements).
- AEM has several new products in the pipeline and it is engaging customers for more. In our view, this is the key for economic sustainability, as well as for development of its own employees.

Material E issues

- AEM's environmental exposure is through energy, water and inputs (fabricated parts and electronics).
- AEM adheres to all National Environment Agency laws and regulations and has not had incidences of environmental non-compliance over the past 10 years.
- Further, AEM's constant energy-saving initiatives have resulted in energy consumption rising by only 7.5% (in kWh) in 2019 despite a 23% increase in revenue.
- AEM screens suppliers for negative environmental and social impacts, including pollutions, biodiversity loss, global warming, incidences of child labour, breaches of customer privacy, and more. All eight key fabrication suppliers and 23 key standard part suppliers were found to have no negative environmental or social impacts.

Material S issues

- AEM values talent retention. One approach is through wages. In Malaysia, where around a-third of production takes place, AEM's entry wage for production workers have been higher than the minimum wage at least since 2017, to retain employees. Entry wages are also higher than minimum wages in the US and China.
- Workforce diversity. AEM is an equal-opportunities employer. Management are hired from local communities and consists of various nationalities. 86% of management are local across AEM's footprint globally.
- Workplace safety. AEM trains its employees on health and safety work practices. In 2018, there was 1 minor injury.
- In 2019, average training per employee was 15.7 hours, or 7,590 hours in total, to equip staff with skills across technical, project management and software domains.
- Females comprise 22-23% of the total work force, and 19-23% of new hires since 2017.
- Turnover rate per month ranged from 1.1-2.1% in FY17-19. 2020 target is to maintain turnover rate at below 1.5% a month.

Key G metrics and issues

- The board has seven directors, of which one is the executive chairman, four are independent directors (57%), and two are non-independent, non-executive. All the directors are male.
- The audit & risk management, remuneration, and nominating committees are chaired by independent directors. The strategy committee, which works with management on long-term strategic planning, is chaired by the executive chairman.
- Executive chairman Mr. Loke Wai San plans to return to a non-executive chairman role from 1 Jan-21.
- Key management compensation (comprising the Board and senior management) accounted for 27% of staff costs in 2019 (2018:17%). FY19 profit was 58% higher YoY.
- In 2019, AEM won "Most Transparent Company Award, Technology" and was runner up for the "Singapore Corporate Governance Award" by SIAS. AEM regularly updates on its sales guidance and orders received and it's active in engaging with the investment community.
- Zero substantiated cases of corruption or legal compliance issues in 2019, to be maintained in 2020.
- AEM was granted two patents in 2019, and the staff involved were rewarded. AEM views its considerable engineering development revenue as a positive sign of customer satisfaction and relationship.

Fig 1: Forecast revisions

	FY21E			FY22E		
	New	Old	Chg (%)	New	Old	Chg (%)
Revenue (SGDm)	518.0	517.3	0.1	669.8	545.4	22.8
Gross profit (SGDm)	196.8	210.5	-6.5	261.2	224.7	16.2
EBIT (SGDm)	91.9	117.4	-21.8	133.3	125.9	5.9
EBITDA (SGDm)	100.5	122.6	-18.0	141.2	130.8	7.9
Core net profit (SGDm)	78.1	99.3	-21.3	112.5	106.3	5.8
EPS (SGD)	0.28	0.36	-22.9	0.40	0.39	3.7
			Chg (ppt)			Chg (ppt)
Gross margin	38.0%	40.7%	-2.7	39.0%	41.2%	-2.2
Staff cost as % of sales	15.0%	13.6%	1.4	15.0%	14.0%	1.0

Source: Maybank Kim Eng

Fig 2: 1Q21 performance summary

	1Q21	1Q20	4Q20	YoY Chg	QoQ Chg	FYE	as a % of FY21E
	SGDm	SGDm	SGDm	(%)	(%)	SGDm	(%)
Revenue	80.2	146.8	83.4	-45.3	-3.8	517.3	16%
PBT	15.9	43.8	16.6	-63.7	-4.2	119.7	13%
Net profit	13.2	36.1	18.0	-63.5	-26.5	99.3	13%
PBT margin	19.8%	29.9%	19.9%	-10.0	-0.1		
Net margin	16.5%	24.6%	21.5%	-8.2	-5.1		

Source: Company, Maybank Kim Eng

FYE 31 Dec	FY19A	FY20A	FY21E	FY22E	FY23E
Key Metrics					
P/E (reported) (x)	6.2	8.4	13.6	9.5	8.1
Core P/E (x)	10.3	9.7	13.6	9.5	8.1
Core FD P/E (x)	10.4	9.8	13.7	9.5	8.1
P/BV (x)	4.1	4.5	3.9	3.0	2.3
P/NTA (x)	4.1	4.5	3.9	3.0	2.3
Net dividend yield (%)	2.5	2.6	1.8	2.6	3.1
FCF yield (%)	11.1	8.2	nm	11.8	12.3
EV/EBITDA (x)	6.3	6.7	9.3	6.0	4.6
EV/EBIT (x)	6.9	7.2	10.5	6.5	4.9
INCOME STATEMENT (SGD m)					
Revenue	323.1	519.0	518.0	669.8	756.6
EBITDA	69.5	121.6	104.1	144.8	169.4
Depreciation	(4.4)	(6.1)	(8.7)	(7.9)	(8.4)
Amortisation	(1.5)	(2.3)	(3.6)	(3.6)	(3.6)
EBIT	63.6	113.2	91.9	133.3	157.4
Net interest income /(exp)	(0.2)	0.4	0.8	0.8	0.8
Associates & JV	0.5	0.2	1.5	1.5	1.0
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	63.9	113.8	94.1	135.5	159.2
Income tax	(11.0)	(16.2)	(16.0)	(23.0)	(27.1)
Minorities	0.0	0.0	0.0	0.0	0.0
Discontinued operations	0.0	0.0	0.0	0.0	0.0
Reported net profit	52.9	97.6	78.1	112.5	132.1
Core net profit	52.9	97.6	78.1	112.5	132.1
BALANCE SHEET (SGD m)					
Cash & Short Term Investments	107.7	134.8	99.9	194.2	288.5
Accounts receivable	28.0	47.6	66.0	80.8	85.0
Inventory	57.5	79.7	122.7	134.8	141.2
Property, Plant & Equip (net)	6.4	8.1	28.5	24.6	20.2
Intangible assets	19.0	56.2	56.2	56.2	56.2
Investment in Associates & JVs	4.6	4.7	6.1	7.6	8.6
Other assets	4.9	4.5	4.5	4.5	4.5
Total assets	**228.0**	**335.5**	**383.8**	**502.6**	**604.1**
ST interest bearing debt	0.0	0.0	0.0	0.0	0.0
Accounts payable	73.1	83.7	83.5	118.0	120.3
LT interest bearing debt	0.0	0.0	0.0	0.0	0.0
Other liabilities	20.0	40.0	30.0	30.0	30.0
Total Liabilities	**93.6**	**124.1**	**113.8**	**148.2**	**150.6**
Shareholders Equity	134.3	211.4	270.0	354.4	453.5
Minority Interest	0.0	0.0	0.0	0.0	0.0
Total shareholder equity	**134.3**	**211.4**	**270.0**	**354.4**	**453.5**
Total liabilities and equity	**228.0**	**335.5**	**383.8**	**502.6**	**604.1**
CASH FLOW (SGD m)					
Pretax profit	63.9	113.8	94.1	135.5	159.2
Depreciation & amortisation	5.9	8.4	12.3	11.5	12.0
Adj net interest (income)/exp	0.0	0.0	0.0	0.0	0.0
Change in working capital	2.3	(27.2)	(71.7)	7.5	(8.2)
Cash taxes paid	(5.8)	(8.8)	(16.0)	(23.0)	(27.1)
Other operating cash flow	0.0	0.0	0.0	0.0	0.0
Cash flow from operations	65.8	86.0	17.2	130.0	134.9
Capex	(5.1)	(7.9)	(29.0)	(4.0)	(4.0)
Free cash flow	60.7	78.1	(11.8)	126.0	130.9
Dividends paid	(10.5)	(22.2)	(19.5)	(28.1)	(33.0)
Equity raised / (purchased)	0.0	4.9	0.0	0.0	0.0
Change in Debt	(0.3)	0.0	0.0	0.0	0.0
Other invest/financing cash flow	(1.3)	(34.7)	(3.6)	(3.6)	(3.6)
Effect of exch rate changes	0.2	0.0	0.0	0.0	0.0
Net cash flow	48.9	26.1	(34.9)	94.3	94.3

FYE 31 Dec	FY19A	FY20A	FY21E	FY22E	FY23E
Key Ratios					
Growth ratios (%)					
Revenue growth	23.2	60.6	(0.2)	29.3	13.0
EBITDA growth	65.8	74.9	(14.3)	39.0	17.0
EBIT growth	58.8	77.9	(18.8)	45.0	18.1
Pretax growth	59.9	78.1	(17.3)	43.9	17.5
Reported net profit growth	58.1	84.3	(19.9)	43.9	17.5
Core net profit growth	58.1	84.3	(19.9)	43.9	17.5
Profitability ratios (%)					
EBITDA margin	21.5	23.4	20.1	21.6	22.4
EBIT margin	19.7	21.8	17.7	19.9	20.8
Pretax profit margin	19.8	21.9	18.2	20.2	21.0
Payout ratio	26.0	25.4	25.0	25.0	25.0
DuPont analysis					
Net profit margin (%)	16.4	18.8	15.1	16.8	17.5
Revenue/Assets (x)	1.4	1.5	1.3	1.3	1.3
Assets/Equity (x)	1.7	1.6	1.4	1.4	1.3
ROAE (%)	47.3	56.4	32.5	36.0	32.7
ROAA (%)	29.1	34.6	21.7	25.4	23.9
Liquidity & Efficiency					
Cash conversion cycle	5.2	15.0	59.2	64.1	54.2
Days receivable outstanding	27.7	26.2	39.5	39.5	39.5
Days inventory outstanding	80.2	78.3	113.4	113.4	108.5
Days payables outstanding	102.7	89.5	93.7	88.8	93.7
Dividend cover (x)	3.8	3.9	4.0	4.0	4.0
Current ratio (x)	2.2	2.4	2.9	3.0	3.8
Leverage & Expense Analysis					
Asset/Liability (x)	2.4	2.7	3.4	3.4	4.0
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)	nm	na	na	na	na
Debt/EBITDA (x)	0.0	0.0	0.0	0.0	0.0
Capex/revenue (%)	1.6	1.5	5.6	0.6	0.5
Net debt/ (net cash)	(107.7)	(134.8)	(99.9)	(194.2)	(288.5)

Source: Company; Maybank

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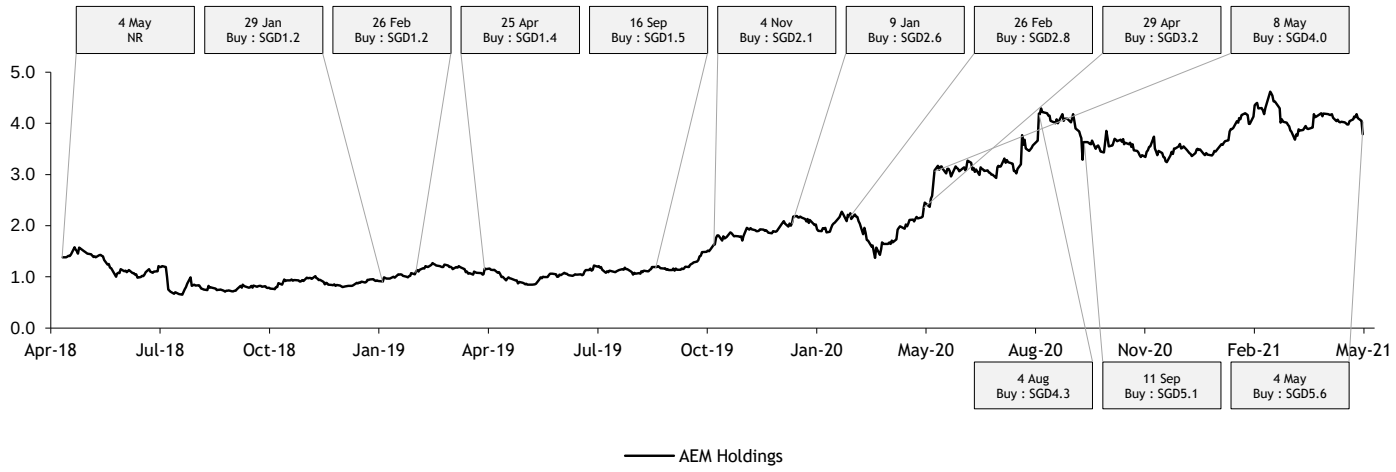

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