

Malaysia

ADD (no change)

Consensus ratings*: Buy 11 Hold 0 Sell 1

Current price:	RM0.96
Target price:	RM1.41
Previous target:	RM1.94
Up/downside:	47.2%
CGS-CIMB / Consensus:	-16.5%

Reuters:	VSID.KL
Bloomberg:	VSI MK
Market cap:	US\$875.0m
	RM3,665m
Average daily turnover:	US\$3.01m
	RM12.65m
Current shares o/s:	3,812m
Free float:	60.3%

*Source: Bloomberg

Key changes in this note

- FY22-24F core EPS forecasts cut by 13.5-19.6% to reflect i) weaker revenue growth and EBITDA margins owing to inefficiencies from component and labour shortages and ii) a more gradual sales recovery post the supply chain issues going into FY23-24F.



Source: Bloomberg

Price performance	1M	3M	12M
Absolute (%)	-21.3	-16.5	-35.6
Relative (%)	-27.4	-24.3	-37.5

Major shareholders	% held
Beh/Gan Family	28.1
KWAP	11.4

Analyst(s)



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VS Industry Bhd

Worker welfare still a priority

- We remain positive on VSI post its investor update as we believe VS remains committed to resolving any potential issues/gaps in its labour practices.
- Our view on VSI's long-term earnings growth prospects remains intact notwithstanding further supply chain disruptions.

Migrant worker rights specialist ends engagement with VS

In its recent briefing, VS Industry (VSI) addressed a media article regarding actions taken by migrant worker rights specialist, Mr. Andy Hall on ending his engagement with VSI. To recap, Andy Hall and VSI had previously entered into an engagement pertaining to VSI's labour practices and the welfare of VSI's workers. Their engagement resulted in VSI agreeing to hire an independent third-party auditor (to be jointly decided by both parties) to run a social compliance audit (based on the 11 International Labour Organization (ILO) indicators), specifically on recalibrated workers (a government programme that allows companies to legally employ undocumented foreign workers from 6 Nov 2020 to 30 Jun 2022). We gather that the engagement ended as Andy Hall was dissatisfied with i) VSI appointing PwC Consulting to conduct the audit unilaterally, ii) VSI not sharing the full details of the audit methodology and findings with him, and iii) the length and the scope of the audit which included local workers instead of purely focusing on recalibrated workers.

An unfavourable development but...

In our view, the withdrawal of the engagement is an unfavourable development as it is likely to further aggravate the negative sentiment, specifically on ESG issues, plaguing the EMS sector's valuations. Nevertheless, we believe VSI's appointment of PwC Consulting to conduct a full-scale audit (on both local and foreign workers) into its labour practices serves as a testament to its commitment to uphold the welfare of its workers as well as identifying and addressing any gaps in terms of its labour practices. We believe any potential issues raised in the audit will allow VSI to address these gaps, which could serve as an unwritten certification that VSI's labour practices have zero elements of forced labour. This will not only reduce the risk of loss of key customers, but could also serve as a strong re-rating catalyst for the stock, in our view.

Reiterate Add on undemanding valuations

We cut our FY22-24F EPS forecasts ahead of its 2QFY22F results as we pencil in weaker revenue growth and EBITDA margins mainly to reflect sales disruptions and inefficiencies owing to component and labour shortages. We retain our Add call, but lower our TP to RM1.41 as we peg our valuation to a lower 15.7x CY23F P/E (vs. 19x), in line with its 5-year historical mean P/E, in view of the weaker sentiment following i) the elevated concerns over ESG, ii) weaker sentiment in the global tech sector in a rising interest rate environment and iii) concerns over supply chain disruptions in the EMS sector. We remain positive on VSI's earnings FY23-24F growth prospects, and continue to like VSI for its diversified customer base as well as undemanding valuations (FY23-24F P/E of 11.3x/9.0x, which is lower than 1.s.d below its 5-year mean).

Financial Summary	Jul-20A	Jul-21A	Jul-22F	Jul-23F	Jul-24F
Revenue (RMm)	3,243	4,002	4,518	5,373	6,252
Net Profit (RMm)	116.5	245.5	245.1	325.2	405.2
Normalised EPS (RM)	0.04	0.07	0.06	0.09	0.11
Normalised EPS Growth	(31%)	100%	(9%)	33%	25%
FD Normalised P/E (x)	27.17	13.56	14.93	11.25	9.03
Price To Sales (x)	1.12	0.91	0.81	0.68	0.59
DPS (RM)	0.026	0.042	0.022	0.029	0.036
Dividend Yield	2.71%	4.38%	2.24%	2.97%	3.71%
EV/EBITDA (x)	13.27	8.20	8.18	6.35	5.08
P/FCFE (x)	34.8	119.9	16.5	14.6	11.1
Net Gearing	(8.1%)	0.1%	(3.6%)	(7.5%)	(12.5%)
P/BV (x)	2.14	1.79	1.67	1.54	1.39
ROE	8.1%	14.4%	11.6%	14.2%	16.2%
% Change In Normalised EPS Estimates			(18.5%)	(19.6%)	(13.5%)
Normalised EPS/consensus EPS (x)			0.89	0.93	1.07

SOURCES: CGS-CIMB RESEARCH, COMPANY REPORTS

Worker welfare still a priority

Upside and downside risks ►

We believe the findings of the audit report will be a key focus area among investors, and a positive outcome from the report should serve as a re-rating catalyst for the stock. Other potential re-rating catalysts include securing of new clients, especially for its China operations, and stronger revenue growth. Downside risks include lower-than-expected end-demand for its products and higher learning curve costs for production works for its new customers

Figure 1: VSI's 12M rolling forward P/E (x) chart : Trades at an attractive 12M forward P/E of 11.7x, close to 1 s.d. below mean



SOURCES: CGS-CIMB RESEARCH, COMPANY REPORTS

Figure 2: Earnings revision table

FYE Jul (RM m)	2021A	2022F			2023F			2024F		
		Old	New	chg	Old	New	chg	Old	New	chg
Revenue	4,002	4,912	4,518	(8%)	5,677	5,373	(5%)	6,555	6,252	(5%)
EBITDA	463	530	454	(14%)	677	567	(16%)	765	679	(11%)
Core pretax profit	354	408	332	(19%)	550	441	(20%)	637	551	(14%)
Core net profit	263	301	245	(18%)	405	325	(20%)	468	405	(13%)

SOURCES: CGS-CIMB RESEARCH, COMPANY REPORTS

ESG in a nutshell

DBL-Click to DEL Table



VSI is one of the largest electronic manufacturing services (EMS) players in South East Asia and is involved in the manufacturing, assembly and sale of plastic mould components and parts. It also has an electronic product business division. VSI aims to deliver sustainable shared values via five pillars: Environment, Welfare of Employees, Community, Marketplace and Suppliers. VSI has been included in the FTSE4Good Bursa Malaysia Index since Jun 2018.

Keep your eye on

VSI was recently working with migrant worker rights specialist Andy Hall to address any potential gaps it faces in its labour practices. They had both identified potential labour issues that could be present among VSI's workers hired through the Recalibrated Worker programme. Pursuant to that, VSI hired PwC to conduct an independent social compliance audit (based on the 11 International Labour Organization (ILO) indicators of forced labour), which will encompass all of VSI's workers, both local and foreign.

Implications

We believe the audit findings will remain as a key focus area among investors. We believe any potential issues raised in the audit will allow VSI to address these gaps, which could potentially serve as an unwritten certification that VSI's labour practices have zero elements of forced labour. This will not only reduce the risk of loss of key customers, but could also serve as a strong re-rating catalyst for the stock, in our view. We have lowered our P/E valuations to partially reflect the ESG risks present in this development.

ESG highlights

On the environmental front, VSI allocates resources to waste management, particularly the handling of non-scheduled waste. The volume of recycled waste at VSI increased by 26.7% in FY20 (vs. FY19). Noise pollution and air emissions are less of an issue for VSI compared with other manufacturing companies.

Implications

We believe that VSI's focus on maintaining its competitiveness as a manufacturing partner requires it to continuously improve its manufacturing practices. This includes its implementation of a lean manufacturing programme, which targets to reduce wasteful processes, materials and defects in its production.

Trends

Given the increasing attention on forced labour practices in Malaysia and South East Asia, VSI's treatment and sourcing of labour will be a key trend to watch. Changes in government policies regarding labour, including sourcing requirements and minimum wages, will impact VSI.

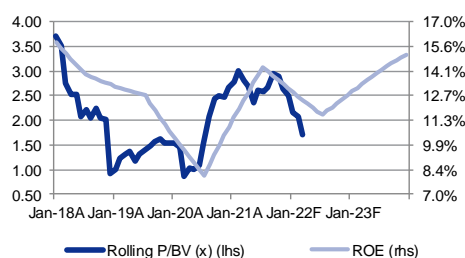
Implications

In addition to adhering to stringent labour standards, VSI invested in new machines and equipment to increase automation and boost the productivity of its workforce. A portion of the RM64m capital expenditure it spent in FY20 was utilised for investments in new technology and initiatives to boost productivity. Additionally VSI is investing in the construction of new hostels, which cost approximately RM30m for FY23F. The hostels comply with the Workers' Minimum Standards of Housing and Amenities Act, 1990 (No. 446)

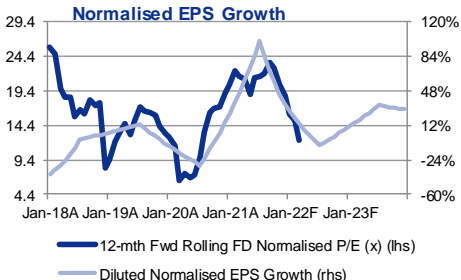
SOURCES: CGS-CIMB RESEARCH, REFINITIV

BY THE NUMBERS

P/BV vs ROE



12-mth Fwd FD Normalised P/E vs FD Normalised EPS Growth



Profit & Loss

(RMm)	Jul-20A	Jul-21A	Jul-22F	Jul-23F	Jul-24F
Total Net Revenues	3,243	4,002	4,518	5,373	6,252
Gross Profit	321	527	452	537	625
Operating EBITDA	271	463	454	567	679
Depreciation And Amortisation	-92	-101	-119	-126	-130
Operating EBIT	179	362	335	441	549
Financial Income/(Expense)	-10	-7	-6	-2	0
Pretax Income/(Loss) from Assoc.	2	-1	2	2	2
Non-Operating Income/(Expense)	0	0	0	0	0
Profit Before Tax (pre-EI)	171	354	332	441	551
Exceptional Items	-18	-24	0	0	0
Pre-tax Profit	153	329	332	441	551
Taxation	-49	-88	-90	-119	-149
Exceptional Income - post-tax					
Profit After Tax	104	242	242	322	402
Minority Interests	12	4	3	3	3
Preferred Dividends					
FX Gain/(Loss) - post tax					
Other Adjustments - post-tax					
Preference Dividends (Australia)					
Net Profit	116	246	245	325	405
Normalised Net Profit	122	266	242	322	402
Fully Diluted Normalised Profit	134	270	245	325	405

Cash Flow

(RMm)	Jul-20A	Jul-21A	Jul-22F	Jul-23F	Jul-24F
EBITDA	270.9	463.1	453.9	567.3	678.9
Cash Flow from Inv. & Assoc.					
Change In Working Capital	71.2	(270.8)	2.0	(147.7)	(151.7)
(Incr)/Decr in Total Provisions					
Other Non-Cash (Income)/Expense	57.8	11.3	11.3	11.3	11.3
Other Operating Cashflow					
Net Interest (Paid)/Received	(10.2)	(7.3)	(5.7)	(2.0)	0.1
Tax Paid	(49.2)	(100.7)	(89.5)	(119.2)	(148.8)
Cashflow From Operations	340.4	95.6	372.0	309.8	389.8
Capex	(115.6)	(233.6)	(150.0)	(60.0)	(60.0)
Disposals Of FAs/subsidiaries	13.4	10.5	0.0	0.0	0.0
Acq. Of Subsidiaries/investments	(9.5)	3.8	0.0	0.0	0.0
Other Investing Cashflow	2.9	6.1	0.0	0.0	0.0
Cash Flow From Investing	(108.9)	(213.2)	(150.0)	(60.0)	(60.0)
Debt Raised/(repaid)	(126.8)	148.1	0.0	0.0	0.0
Proceeds From Issue Of Shares	20.5	49.2	0.0	0.0	0.0
Shares Repurchased	0.0	0.0	0.0	0.0	0.0
Dividends Paid	(48.1)	(105.7)	(98.0)	(130.1)	(162.1)
Preferred Dividends					
Other Financing Cashflow	(15.2)	(0.1)	(11.3)	(11.3)	(11.3)
Cash Flow From Financing	(169.5)	91.6	(109.3)	(141.4)	(173.4)
Total Cash Generated	62.0	(26.1)	112.6	108.5	156.4
Free Cashflow To Equity	104.8	30.5	222.0	249.8	329.8
Free Cashflow To Firm	248.8	(106.3)	233.2	261.1	341.1

SOURCES: CGS-CIMB RESEARCH, COMPANY REPORTS

BY THE NUMBERS... cont'd

Balance Sheet

(RMm)	Jul-20A	Jul-21A	Jul-22F	Jul-23F	Jul-24F
Total Cash And Equivalents	405	402	489	598	754
Total Debtors	884	992	1,114	1,325	1,542
Inventories	332	637	668	795	925
Total Other Current Assets	106	201	201	201	201
Total Current Assets	1,727	2,232	2,473	2,919	3,422
Fixed Assets	847	990	1,052	991	926
Total Investments	152	267	267	267	267
Intangible Assets	0	0	0	0	0
Total Other Non-Current Assets	107	109	109	109	109
Total Non-current Assets	1,107	1,366	1,428	1,367	1,302
Short-term Debt	224	316	316	316	316
Current Portion of Long-Term Debt					
Total Creditors	576	847	1,003	1,192	1,387
Other Current Liabilities	39	37	37	37	37
Total Current Liabilities	839	1,200	1,356	1,546	1,741
Total Long-term Debt	28	89	89	89	89
Hybrid Debt - Debt Component					
Total Other Non-Current Liabilities	24	24	24	24	24
Total Non-current Liabilities	52	112	112	112	112
Total Provisions	66	68	68	68	68
Total Liabilities	957	1,381	1,536	1,726	1,921
Shareholders' Equity	1,709	2,041	2,188	2,383	2,626
Minority Interests	168	177	177	177	177
Total Equity	1,877	2,218	2,365	2,560	2,803

Key Ratios

[Call-Outs Type/Pasteover]

	Jul-20A	Jul-21A	Jul-22F	Jul-23F	Jul-24F
Revenue Growth	(18.5%)	23.4%	12.9%	18.9%	16.4%
Operating EBITDA Growth	(18.1%)	70.9%	(2.0%)	25.0%	19.7%
Operating EBITDA Margin	8.4%	11.6%	10.0%	10.6%	10.9%
Net Cash Per Share (RM)	0.040	(0.001)	0.022	0.051	0.092
BVPS (RM)	0.45	0.54	0.57	0.63	0.69
Gross Interest Cover	10.37	32.04	29.70	39.10	48.64
Effective Tax Rate	31.9%	26.6%	27.0%	27.0%	27.0%
Net Dividend Payout Ratio	35.8%	39.2%	40.0%	40.0%	40.0%
Accounts Receivables Days	106.0	85.6	85.1	82.8	83.9
Inventory Days	44.05	50.85	58.57	55.22	55.94
Accounts Payables Days	80.41	74.73	83.02	82.83	83.90
ROIC (%)	7.7%	16.5%	12.5%	15.9%	19.0%
ROCE (%)	8.3%	15.0%	12.3%	15.4%	17.8%
Return On Average Assets	4.43%	8.45%	6.57%	7.91%	8.93%

Key Drivers

	Jul-20A	Jul-21A	Jul-22F	Jul-23F	Jul-24F
Customer X (RM m)	1,300.0	1,275.6	1,403.2	1,613.7	1,855.7
Coffee Brewer Customer (RM m)	715.0	717.5	717.5	753.4	791.1
Pool Cleaner Customer (RM m)	227.0	358.8	394.6	453.8	521.9
US-Based customer (RM m)	162.0	797.3	956.7	1,052.4	1,157.6
Customer Y (US-Based) (RM m)	-	-	150.0	550.0	900.0
Others (RM m)	164.3	318.9	334.8	351.6	386.7
Blended EBITDA margin (%)	8.4%	11.6%	10.0%	10.6%	10.9%

SOURCES: CGS-CIMB RESEARCH, COMPANY REPORTS

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Score Range:	90 - 100	80 – 89	70 - 79	Below 70	No Survey Result
Description:	Excellent	Very Good	Good	N/A	N/A

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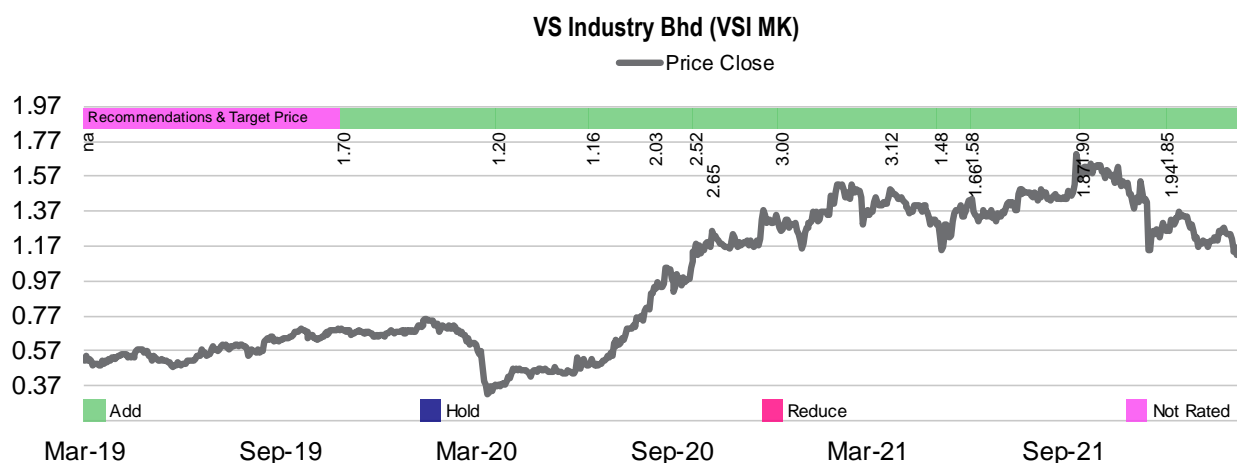
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Distribution of stock ratings and investment banking clients for quarter ended on 31 December 2021		
619 companies under coverage for quarter ended on 31 December 2021		
	Rating Distribution (%)	Investment Banking clients (%)
Add	71.1%	1.5%
Hold	21.8%	0.0%
Reduce	7.1%	0.0%

Spitzer Chart for stock being researched (2 year data)



Corporate Governance Report of Thai Listed Companies (CGR). CG Rating by the Thai Institute of Directors Association (Thai IOD) in 2021, Anti-Corruption 2021

ADVANC – Excellent, Certified, **AMATA** – Excellent, Certified, **ANAN** – Excellent, n/a, **AOT** – Excellent, n/a, **AP** – Excellent, Certified, **ASP** – Excellent, n/a, **AWC** – Excellent, Declared, **AU** – Good, n/a, **BAM** – Very Good, Certified, **BAY** – Excellent, Certified, **BBL** – Excellent, Certified, **BCH** – Very Good, Certified, **BCP** – Excellent, Certified, **BCPG** – Excellent, Certified, **BDMS** – Excellent, n/a, **BEAUTY** – Good, n/a, **BEM** – Excellent, n/a, **BH** – Good, n/a, **BJC** – Very Good, n/a, **BLA** – Very Good, Certified, **BTS** – Excellent, Certified, **CBG** – Very Good, n/a, **CCET** – n/a, n/a, **CENTEL** – Excellent, Certified, **CHAYO** – Very Good, n/a, **CHG** – Very Good, n/a, **CK** – Excellent, n/a, **COM7** – Excellent, Certified, **CPALL** – Excellent, Certified, **CPF** – Excellent, Certified, **CPN** – Excellent, Certified, **CPNREIT** – n/a, n/a, **CRC** – Excellent, Declared, **DELTA** – Excellent, Certified, **DDD** – Excellent, n/a, **DIF** – n/a, n/a, **DOHOME** – Very Good, Declared, **DREIT** – n/a, n/a, **DTAC** – Excellent, Certified, **ECL** – Excellent, Certified, **EGCO** – Excellent, Certified, **EPG** – Excellent, Certified, **ERW** – Very Good, Certified, **GFPT** – Excellent, Certified, **GGC** – Excellent, Certified, **GLOBAL** – Excellent, n/a, **HANA** – Excellent, Certified, **HMPRO** – Excellent, Certified, **HUMAN** – Good, n/a, **ICHI** – Excellent, Certified, **III** – Excellent, Declared, **INTUCH** – Excellent, Certified, **IRPC** – Excellent, Certified, **ITD** – Very Good, n/a, **IVL** – Excellent, Certified, **JASIF** – n/a, n/a, **JKN** – n/a, Certified, **JMT** – Very Good, n/a, **KBANK** – Excellent, Certified, **KCE** – Excellent, Certified, **KEX** – Very Good, Declared, **KKP** – Excellent, Certified, **KSL** – Excellent, Certified, **KTB** – Excellent, Certified, **KTC** – Excellent, Certified, **LH** – Excellent, n/a, **LPN** – Excellent, Certified, **M** – Very Good, Certified, **MAKRO** – Excellent, Certified, **MC** – Excellent, Certified, **MEGA** – Very Good, n/a, **MINT** – Excellent, Certified, **MTC** – Excellent, Certified, **NETBAY** – Very Good, n/a, **NRF** – Very Good, Declared, **OR** – Excellent, n/a, **ORI** – Excellent, Certified, **OSP** – Excellent, n/a, **PLANB** – Excellent, Certified, **PRINC** – Very Good, Certified, **PR9** – Excellent, Declared, **PSH** – Excellent, Certified, **PTT** – Excellent, Certified, **PTTEP** – Excellent, n/a, **PTTGC** – Excellent, Certified, **QH** – Excellent, Certified, **RAM** – n/a, n/a, **RBF** – Very Good, n/a, **RS** – Excellent, Declared, **RSP** – Good, n/a, **S** – Excellent, n/a, **SAK** – Very Good, Declared, **SAPPE** – Very Good, Certified, **SAWAD** – Very Good, n/a, **SCB** – Excellent, Certified, **SCC** – Excellent, Certified, **SCGP** – Excellent, Declared, **SECURE** – n/a, n/a, **SHR** – Excellent, n/a, **SIRI** – Excellent, Certified, **SPA** – Very Good, n/a, **SPALI** – Excellent, Certified, **SPRC** – Excellent, Certified, **SSP** – Good, Certified, **STEC** – Excellent, n/a, **SVI** – Excellent, Certified, **SYNEX** – Very Good, Certified, **TCAP** – Excellent, Certified, **THANI** – Excellent, Certified, **TIDLOR** – n/a, Certified, **TISCO** – Excellent, Certified, **TKN** – Very Good, n/a, **TOP** – Excellent, Certified, **TRUE** – Excellent, Certified, **TTB** – Excellent, Certified, **TU** – Excellent, Certified, **TVO** – Excellent, Certified, **VGI** – Excellent, Certified, **WHA** – Excellent, Certified, **WHART** – n/a, n/a, **WICE** – Excellent, Certified, **WORK** – Good, n/a.

- CG Score 2021 from Thai Institute of Directors Association (IOD)

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Definition:

- Add** The stock's total return is expected to exceed 10% over the next 12 months.
- Hold** The stock's total return is expected to be between 0% and positive 10% over the next 12 months.
- Reduce** The stock's total return is expected to fall below 0% or more over the next 12 months.

The total expected return of a stock is defined as the sum of the: (i) percentage difference between the target price and the current price and (ii) the forward net dividend yields of the stock. Stock price targets have an investment horizon of 12 months.

Sector Ratings

Definition:

- Overweight** An Overweight rating means stocks in the sector have, on a market cap-weighted basis, a positive absolute recommendation.
- Neutral** A Neutral rating means stocks in the sector have, on a market cap-weighted basis, a neutral absolute recommendation.
- Underweight** An Underweight rating means stocks in the sector have, on a market cap-weighted basis, a negative absolute recommendation.

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Definition:

- Overweight** An Overweight rating means investors should be positioned with an above-market weight in this country relative to benchmark.
- Neutral** A Neutral rating means investors should be positioned with a neutral weight in this country relative to benchmark.
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