

Aurelius Technologies (ATECH MK)

Further capacity expansion underway?

Maintain BUY and TP of MYR2.13

We maintain our BUY call and TP of MYR2.13 for ATECH, pegging its CY23's EPS of 13.8sen to a PER of 15.4x, following an investor briefing with the company recently. Our PER peg includes a 10% premium to ATECH's blended domestic and regional EMS peers' CY23 PER average of 14.0x. The PER premium reflects ATECH's robust earnings growth prospects vis-a-vis its peers, its growing exposure to higher value-added semiconductor components (MCICs), as well as its operational resilience, owing to its low dependence on foreign labour (unlike its other domestic listed EMS peers).

Strong demand driving further capacity expansion

Group capacity expansion is underway, having installed 4 SMT production lines for Customer F to-date. This will allow ATECH to raise its production capacity to c.1m MCICs pieces per month (pcs/mth) commencing 2QFY23E, which translates to MYR2-3m sales/mth based on our estimates. It is currently focusing on further ramping up its capacity for Customer F, with 3 additional SMT lines slated to be installed by end-FY23. Additionally, ATECH is currently in late-stage discussions with a new prospective customer which, if successful, could provide further earnings upside.

Higher margin MCICs to offset cost inflation

ATECH is anticipating rising staff, electricity and raw material costs - these could add c.24% to ATECH's FY23 total costs on our estimates, though expected to be passed through to its end customers. Nonetheless, we are projecting a 150-250bps gross profit margin expansion per annum over our forecast period, boosted by its growing exposure to higher-margin MCICs.

Striving for operational excellence amidst disruptions

In FY22, ATECH successfully increased its factory floor space by 69% to 132,821 sq. ft. It is now focusing on ramping up its production amidst the various operational disruptions such as labour shortages and component supply disruptions. However, the group has laid out plans to mitigate the impact of the disruptions, by increasing its inventory level as it deploys a "Just-In-Case" strategy. We prefer ATECH over its peers for its bright growth prospects, improving margins and its relatively resilient business operations vis-a-vis the various on-going disruptions in the EMS industry.

FYE Jan (MYR m)	FY21A	FY22A	FY23E	FY24E	FY25E
Revenue	362	367	470	533	593
EBITDA	27	37	54	69	81
Core net profit	16	24	39	51	57
Core EPS (sen)	4.4	6.7	10.9	14.1	16.0
Core EPS growth (%)	(33.3)	53.1	62.4	29.2	13.4
Net DPS (sen)	0.0	0.0	2.2	2.8	3.2
Core P/E (x)	na	31.8	17.5	13.5	11.9
P/BV (x)	na	3.8	2.8	2.4	2.1
Net dividend yield (%)	na	0.0	1.1	1.5	1.7
ROAA (%)	5.9	7.0	9.5	11.6	12.0
EV/EBITDA (x)	29.7	21.6	13.9	10.9	9.3
Net gearing (%) (incl perps)	141.1	18.9	26.7	25.4	20.7
Consensus net profit	-	-	36	47	57
MKE vs. Consensus (%)	-	-	7.7	7.0	0.1

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BUY

Share Price	MYR 1.91
12m Price Target	MYR 2.13 (+13%)
Previous Price Target	MYR 2.13

Company Description

Aurelius Technologies Bhd. provides manufacturing solutions for industrial electronic products.

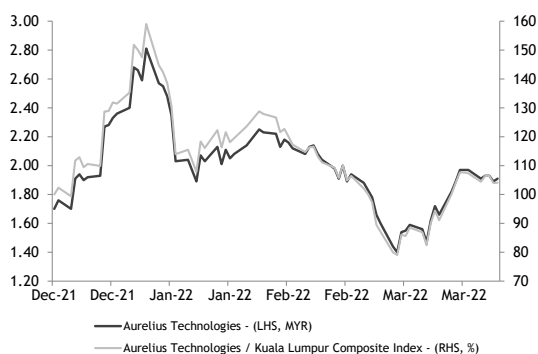
Statistics

52w high/low (MYR)	na/na
3m avg turnover (USDm)	3.3
Free float (%)	29.0
Issued shares (m)	358
Market capitalisation	MYR684.1M USD162M

Major shareholders:

Main Stream Ltd	21.3%
Loh Hock Chiang	19.7%
Lee Chong Yeow (Deceased)	19.7%

Price Performance



	-1M	-3M	-12M
Absolute (%)	4	(19)	na
Relative to index (%)	4	(21)	na

Source: FactSet

Ramping up capacity and production for Customer F

To date, ATECH has 4 SMT production lines together with 8 automated-backend lines installed and commissioned for Customer F (a company listed on Shanghai Stock Exchange; customer was acquired back in 2019). Based on our assumptions, this will allow the group to produce up to 1m MCICs pcs/mth (vs. c.800k pcs as of 4QFY22), which should translate into MYR2-3m sales for its semiconductor segment commencing 2QFY23E.

To recap, the group planned to install 7 SMT lines by early FY24 to cater for the rising demand from Customer F. Having said that, the group hopes to accelerate its installation of production lines ahead of the initial timeline (to have all 3 remaining SMT production lines installed by end-FY23), to catch up with the delays in Line 3 and Line 4's installation in 4QFY22 as the automated-backend equipment was held up in China due to lockdowns and port congestion during the quarter. The group has also guided that Customer F is able to fully absorb any and all volume manufactured by ATECH for now, implying that future capacity growth will translate directly to sales volume, until an optimal level is reached (to be agreed upon by both parties).

Figure 1: Revenue by segment and growth rates

Revenue (MYR'm) - FYE Jan	FY20	FY21	FY22	FY23E	FY24E	FY25E
Comm & IoT Products	300.2	324.1	317.4	372.7	412.2	458.2
Electronic Devices	89.1	34.1	38.9	59.7	63.8	68.2
Semiconductor Components	0.0	4.0	11.1	37.8	56.7	66.2
Total	389.3	362.2	367.4	470.2	532.6	592.5
Growth Rates (%)	FY20	FY21	FY22	FY23E	FY24E	FY25E
Comm & IoT Products	4.8%	7.9%	(2.1%)	17.4%	10.6%	11.2%
Electronic Devices	24.2%	(61.7%)	14.0%	53.4%	6.9%	6.9%
Semiconductor Components	nm	nm	178.4%	239.2%	50.0%	16.7%
Total	8.7%	(7.0%)	1.5%	28.0%	13.3%	11.3%

Source: Company, Maybank IBG Research

Gross profit margin expected to grow despite rising costs

ATECH is expecting costs to continue increasing in the near term, mainly due to (i) higher staff costs, driven by the increase in min. wage to MYR1,500 effective May 2022 (impacting c.800 employees by MYR200 per worker; recall that ATECH had increased its internal min. wage to MYR1,300 voluntarily since Oct. 2021), as well as higher headcount in the near-to-medium term from its capacity ramp-up exercise; (ii) higher input costs from the electricity tariff hike, which is expected to drive ATECH's electricity costs higher by 22% based on our assumptions; and (iii) higher raw material costs, which is expected to stay elevated over the next 12 months due to industry-wide component shortages. These additional costs are expected to increase ATECH's FY23 total costs by c.24%.

We are not overly perturbed by the increasing costs, as the group is able to pass on these costs to its end-customers (depending on negotiations, usually on a quarterly review basis), with the exception of raw material costs, which are able to be passed on immediately. In fact, we are projecting the group's gross profit margins to expand to 13.5% in FY23E (from 11.1% in FY22), and grow further to 15.2% in FY24, underpinned by its move up the value chain to the manufacturing of higher margins MCICs (our model assumes c.57% gross profit margin, vis-à-vis other segments' gross profit margin of c.9-20%).

Figure 2: Gross profit by segment and gross profit margins

Gross Profit (MYR'm) - FYE Jan	FY20	FY21	FY22	FY23E	FY24E	FY25E
Comm & IoT Products	20.9	24.2	28.9	32.1	37.4	43.9
Electronic Devices	27.8	7.2	5.8	11.9	12.8	13.6
Semiconductor Components	(1.0)	(0.2)	6.0	21.5	32.3	37.7
Total	46.2	30.1	40.7	63.6	80.8	93.9

Gross Profit Margin (%)	FY20	FY21	FY22	FY23E	FY24E	FY25E
Comm & IoT Products	7.0%	7.5%	9.1%	8.6%	9.1%	9.6%
Electronic Devices	31.2%	21.1%	14.9%	20.0%	20.0%	20.0%
Semiconductor Components	0.0%	(5.1%)	53.8%	57.0%	57.0%	57.0%
Total	11.9%	8.3%	11.1%	13.5%	15.2%	15.9%

Source: Company, Maybank IBG Research

Demand from customers remain strong

A TECH orderbook remains healthy and increased to MYR523m as of end-FY22, from over MYR400m a year ago - more than three quarters of the orderbook are contributed by the IoT and communications segment, with the remainder primarily from the electronic device segment. The current orderbook excludes orders from Customer F, which remains the key growth driver to the group's earnings in the near-to-medium term, providing further upside to the group's earnings outlook.

Apart from that, the group is also in advanced discussions with another new customer, an established global player focusing on the automotive sensor industry. For a start, ATECH has allocated 1 SMT production line for the new customer's pilot production exercise. Negotiations between both parties have been somewhat hindered by the border lockdowns, as the new customer has yet to visit ATECH's factory sites for quality checks and supply chain auditing. Nonetheless, the group is ready to progress negotiations with the new customer once borders reopen. Assuming the deal goes through, the group will have to ramp up its capacity further via the acquisition of a new factory (to be funded internally/via bank borrowings), that is expected to take 9-12 months to set up. We have yet to include this development in our current forecasts, pending the official signing of the master purchase agreement.

Positive on ATECH's latest developments

All in, we are positive on ATECH's latest developments. The current strong demand is exceeding its existing capacity, translating into promising high utilisation rates (notwithstanding its aggressive capacity expansion). We also believe there is more room for growth from wallet share increases of its existing customers.

ATECH's near term outlook will continue be driven by its capacity expansion as it brings in new machinery and equipment to its newly-built factory floor space (total floor space increased by 69% to 132,821 sq. ft.). Its move up the value chain towards the manufacturing of the higher-margin MCICs will also help improve the group's margins over time. Over a longer-term horizon, ATECH is riding on the tailwinds of the rapidly expanding local EMS industry, in-part due to the US-China trade war that has seen many MNCs relocate their supply chain out of China and thus, benefiting local contract manufacturers like ATECH.

Risk statement

There are several risk factors for our earnings estimates, target price and rating for ATECH. Key risks are: (i) weaker-than-expected demand from customers in view of rising inflation and geopolitical risks; (ii) lower-than-expected costs pass through (as the mechanism depends on the group's negotiation with its clients); and (iii) operational disruptions from persistent labour issues and component shortages.

FYE 31 Jan	FY21A	FY22A	FY23E	FY24E	FY25E
Key Metrics					
P/E (reported) (x)	na	35.4	17.5	13.5	11.9
Core P/E (x)	na	31.8	17.5	13.5	11.9
P/BV (x)	na	3.8	2.8	2.4	2.1
P/NTA (x)	na	nm	nm	nm	nm
Net dividend yield (%)	na	0.0	1.1	1.5	1.7
FCF yield (%)	na	nm	nm	nm	2.0
EV/EBITDA (x)	29.7	21.6	13.9	10.9	9.3
EV/EBIT (x)	35.6	25.4	15.1	11.7	10.0
INCOME STATEMENT (MYR m)					
Revenue	362.2	367.4	470.2	532.6	592.5
EBITDA	26.9	37.3	53.9	69.5	80.7
Depreciation	(4.5)	(5.6)	(4.5)	(4.7)	(5.6)
Amortisation	0.0	0.0	0.0	0.0	0.0
EBIT	22.4	31.7	49.5	64.7	75.1
Net interest income / (exp)	(3.9)	(3.8)	(3.4)	(3.5)	(3.4)
Associates & JV	0.0	0.0	0.0	0.0	0.0
Exceptionals	(0.6)	(2.1)	0.0	0.0	0.0
Other pretax income	0.0	0.0	0.0	0.0	0.0
Pretax profit	17.8	25.9	46.0	61.3	71.7
Income tax	(2.7)	(3.9)	(6.9)	(10.7)	(14.3)
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	15.1	22.0	39.1	50.6	57.3
Core net profit	15.7	24.1	39.1	50.6	57.3
BALANCE SHEET (MYR m)					
Cash & Short Term Investments	22.3	76.3	40.1	26.8	22.1
Accounts receivable	100.2	90.6	128.8	145.9	162.3
Inventory	72.5	133.5	100.2	111.4	122.9
Property, Plant & Equip (net)	56.2	84.0	109.3	133.4	151.5
Intangible assets	0.0	0.0	0.0	0.0	0.0
Investment in Associates & JVs	0.0	0.0	0.0	0.0	0.0
Other assets	30.4	27.0	34.7	39.0	43.1
Total assets	281.6	411.3	413.1	456.5	501.9
ST interest bearing debt	110.2	96.9	78.1	72.5	64.4
Accounts payable	46.3	82.3	55.7	61.9	68.3
LT interest bearing debt	26.1	17.5	26.1	26.1	26.1
Other liabilities	18.0	13.0	13.0	13.0	13.0
Total Liabilities	200.8	209.9	172.5	173.2	171.4
Shareholders Equity	80.8	201.4	240.6	283.3	330.5
Minority Interest	0.0	0.0	0.0	0.0	0.0
Total shareholder equity	80.8	201.4	240.6	283.3	330.5
Total liabilities and equity	281.6	411.3	413.1	456.5	501.9
CASH FLOW (MYR m)					
Pretax profit	17.8	25.9	46.0	61.3	71.7
Depreciation & amortisation	4.5	5.6	4.5	4.7	5.6
Adj net interest (income)/exp	3.9	3.8	3.4	3.5	3.4
Change in working capital	(18.4)	(18.6)	(40.3)	(26.3)	(25.6)
Cash taxes paid	0.0	0.0	0.0	0.0	0.0
Other operating cash flow	0.5	0.5	0.0	0.0	0.0
Cash flow from operations	0.1	11.1	3.1	28.7	37.1
Capex	(11.4)	(35.7)	(25.8)	(28.9)	(23.7)
Free cash flow	(11.3)	(24.6)	(22.7)	(0.1)	13.4
Dividends paid	(4.9)	(3.3)	0.0	(7.8)	(10.1)
Equity raised / (purchased)	0.0	104.5	0.0	0.0	0.0
Change in Debt	9.8	(25.0)	(7.1)	(5.6)	(8.2)
Other invest/financing cash flow	(3.9)	0.9	0.2	0.2	0.2
Effect of exch rate changes	0.1	(0.0)	0.0	0.0	0.0
Net cash flow	(10.3)	52.5	(29.6)	(13.3)	(4.7)

FYE 31 Jan	FY21A	FY22A	FY23E	FY24E	FY25E
Key Ratios					
Growth ratios (%)					
Revenue growth	(7.0)	1.5	28.0	13.3	11.3
EBITDA growth	(31.5)	38.8	44.5	28.8	16.2
EBIT growth	(38.2)	41.7	55.9	30.9	16.0
Pretax growth	(45.0)	45.4	77.7	33.1	17.0
Reported net profit growth	(36.0)	46.0	77.6	29.2	13.4
Core net profit growth	(33.3)	53.1	62.5	29.2	13.4
Profitability ratios (%)					
EBITDA margin	7.4	10.2	11.5	13.0	13.6
EBIT margin	6.2	8.6	10.5	12.2	12.7
Pretax profit margin	4.9	7.1	9.8	11.5	12.1
Payout ratio	0.0	0.0	20.0	20.0	20.0
DuPont analysis					
Net profit margin (%)	4.2	6.0	8.3	9.5	9.7
Revenue/Assets (x)	1.3	0.9	1.1	1.2	1.2
Assets/Equity (x)	3.5	2.0	1.7	1.6	1.5
ROAE (%)	na	na	na	na	na
ROAA (%)	5.9	7.0	9.5	11.6	12.0
Liquidity & Efficiency					
Cash conversion cycle	125.8	136.1	126.4	130.3	131.2
Days receivable outstanding	96.0	93.4	84.0	92.9	93.6
Days inventory outstanding	74.2	113.5	103.5	84.3	84.6
Days payables outstanding	44.4	70.8	61.1	46.8	47.0
Dividend cover (x)	nm	nm	5.0	5.0	5.0
Current ratio (x)	1.3	1.8	2.0	2.2	2.3
Leverage & Expense Analysis					
Asset/Liability (x)	1.4	2.0	2.4	2.6	2.9
Net gearing (%) (incl perps)	141.1	18.9	26.7	25.4	20.7
Net gearing (%) (excl. perps)	141.1	18.9	26.7	25.4	20.7
Net interest cover (x)	5.7	8.4	14.5	18.8	21.8
Debt/EBITDA (x)	5.1	3.1	1.9	1.4	1.1
Capex/revenue (%)	3.2	9.7	5.5	5.4	4.0
Net debt/ (net cash)	114.0	38.0	64.2	71.9	68.4

Source: Company; Maybank IBG Research

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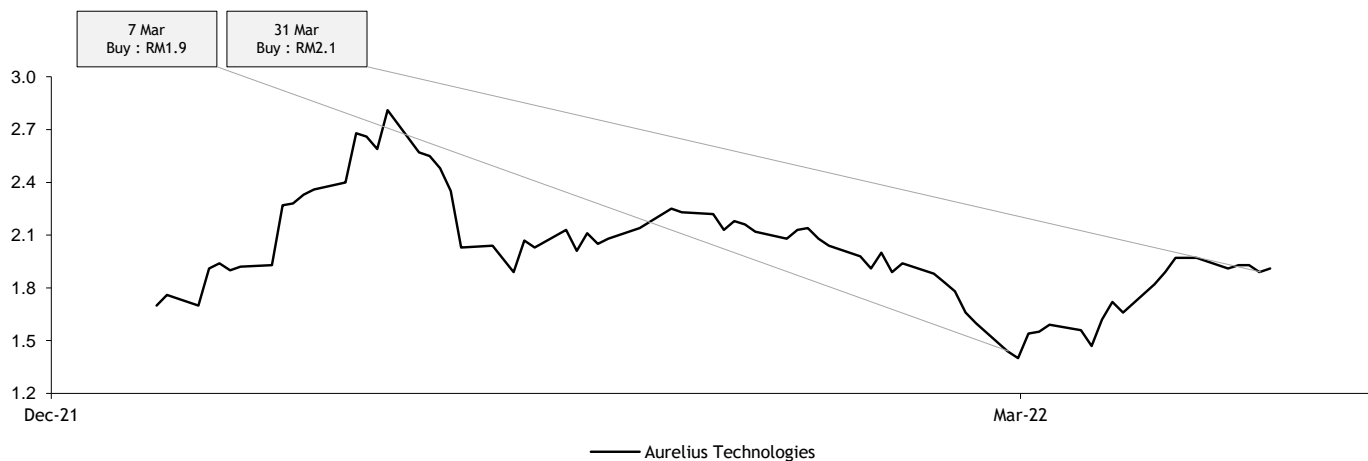
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