

Frontken Corp. Bhd (FRCB MK)

1Q22: Record turnover for Taiwan operations

The good run continues; maintain BUY

FRCB posted another set of strong results in 1Q22, buttressed by record turnover and EBIT margins at its Taiwanese operations. Adopting a more conservative approach in an inflationary environment, we have lowered our valuation peg to 38x FY23E PER, at +0.5SD to the LT mean (from 44x FY23 PER, at +1SD). Our revised TP is now MYR3.55 (-13%), but our BUY call/forecasts are maintained, premised on FRCB's resilient demand and market-leading position as a niche SP to the largest wafer foundry globally.

Results within expectations

Excluding EIs of MYR0.9m, FRCB's 1Q22 core net profit came in at MYR25.6m (+14% YoY, -14% QoQ). Results were within expectations at 20% of our/the street's full-year estimates as 1Q is historically the weakest quarter. Group turnover was up 15% YoY, largely due to improved contributions (+21% YoY) from its 93%-owned Taiwanese subsidiary (AGTC), that continues to benefit from the robust demand for its key customer's industry-leading advanced node (<5nm) chips amidst the ongoing upcycle.

Taiwanese segmental margins hit an all-time high

Other key result takeaways: (i) EBIT margins remained elevated at 34%, underpinned by strong operational leverage at its Taiwanese ops (AGTC contributed c.86% to group EBIT with margins at a historical high of 41%); (ii) revenue for MY also grew 10% YoY from new workflow orders awarded as part of PG's umbrella contracts, in-line with higher oil prices; but (iii) segmental EBIT margins for MY/SG however dragged -8ppts/-5ppts YoY due to acute billing time lags, Covid-related worker shortages, and absence of wage relief subsidies in the previous year corresponding quarter; we opine that affected margins are likely to normalise in sequential quarters.

Rising-rate environment = moderated valuation peg

With Phase 1 of FRCB's new plant in Kaohsiung set to be operational in 2H22, coupled with its key customer's (TSMC) forward guidance of achieving record gross margins of 56%-58% in 2Q22, we continue to remain upbeat on FRCB's prospects as a direct proxy to the ongoing mega-foundry super cycle. While our previous valuation peg of 44x FY23 PER (+1SD to LT mean) reflected this robust outlook, we now adopt a more conservative approach towards sector valuation premiums given the suppressive effect of aggressive Fed tightening by moderating our valuation peg to 38x FY23 PER (+0.5SD to LT Mean). Earnings forecasts, BUY rating are maintained.

| FYE Dec (MYR m) | FY20A | FY21A | FY22E | FY23E | FY24E |
|------------------------------|----------|----------|----------|----------|----------|
| Revenue | 368 | 450 | 578 | 610 | 644 |
| EBITDA | 122 | 162 | 211 | 237 | 249 |
| Core net profit | 81 | 105 | 129 | 148 | 156 |
| Core EPS (sen) | 5.1 | 6.6 | 8.2 | 9.4 | 9.9 |
| Core EPS growth (%) | 17.3 | 29.1 | 23.5 | 14.3 | 5.7 |
| Net DPS (sen) | 2.7 | 4.0 | 4.1 | 4.7 | 5.0 |
| Core P/E (x) | 46.0 | 60.2 | 31.3 | 27.4 | 25.9 |
| P/BV (x) | 8.5 | 13.2 | 7.5 | 7.4 | 7.3 |
| Net dividend yield (%) | 1.1 | 1.0 | 1.6 | 1.8 | 1.9 |
| ROAE (%) | 20.1 | 22.8 | 25.4 | 27.1 | 28.3 |
| ROAA (%) | 14.3 | 16.5 | 18.8 | 20.2 | 21.1 |
| EV/EBITDA (x) | 28.2 | 37.7 | 18.3 | 16.4 | 15.8 |
| Net gearing (%) (incl perps) | net cash | net cash | net cash | net cash | net cash |
| Consensus net profit | - | - | 126 | 159 | 201 |
| MKE vs. Consensus (%) | - | - | 2.3 | (6.9) | (22.5) |

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BUY

| | |
|-----------------------|-----------------|
| Share Price | MYR 2.57 |
| 12m Price Target | MYR 3.55 (+40%) |
| Previous Price Target | MYR 4.10 |

Company Description

Frontken specialises in engineering and precision cleaning services, mostly for semiconductors and O&G markets in Taiwan, Singapore and Malaysia.

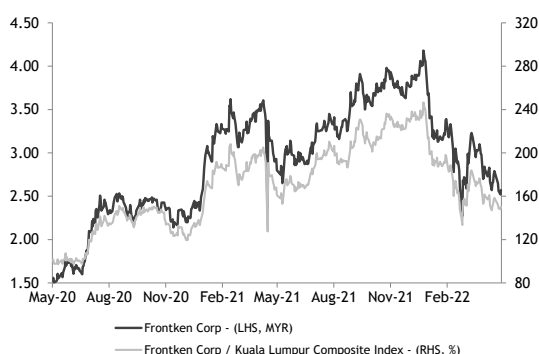
Statistics

| | |
|------------------------|-----------|
| 52w high/low (MYR) | 4.18/2.27 |
| 3m avg turnover (USDm) | 3.6 |
| Free float (%) | 61.0 |
| Issued shares (m) | 1,580 |
| Market capitalisation | MYR4.1B |
| | USD927M |

Major shareholders:

| | |
|---------------------------|-------|
| Dazzle Clean Ltd. | 16.7% |
| OOI KENG THYE / FRONTKEN/ | 14.8% |
| Public Mutual Bhd. | 4.6% |

Price Performance



| | -1M | -3M | -12M |
|-----------------------|------|------|------|
| Absolute (%) | (14) | (24) | (12) |
| Relative to index (%) | (11) | (23) | (10) |

Source: FactSet

Acronyms

AGTC - Ares Green Technology Corporation
 MY - Malaysia
 nm - nanometer
 PG - Petronas Group
 SG - Singapore
 SP - service provider
 TSMC - Taiwan Semiconductor Manufacturing Co.

EBIT - earnings before interest and tax
 EI - exceptional item
 LT - long-term
 PER - price-earnings ratio
 SD - standard deviation
 TP - target price

Fig 1: Frontken Corp's 1Q22 results summary

| FYE Dec (MYR'm) | Quarterly | | | | | Cumulative | | |
|----------------------------------|-------------|-------------|--------------------|-------------|--------------------|-------------|-------------|--------------------|
| | 1Q22 | 1Q21 | % YoY | 4Q21 | % QoQ | 3M22 | 3M21 | % YoY |
| Revenue | 119.1 | 103.5 | 15.1 | 121.5 | (1.9) | 119.1 | 103.5 | 15.1 |
| EBITDA | 43.1 | 37.4 | 15.4 | 45.0 | (4.2) | 43.1 | 37.4 | 15.4 |
| Depreciation | (4.1) | (4.4) | (7.4) | (4.3) | (4.5) | (4.1) | (4.4) | (7.4) |
| Other income | 1.9 | 2.0 | (7.6) | 1.0 | 80.6 | 1.9 | 2.0 | (7.6) |
| EBIT | 40.9 | 35.0 | 16.9 | 41.8 | (2.0) | 40.9 | 35.0 | 16.9 |
| Finance income | 0.1 | 0.2 | (38.2) | 0.2 | (32.7) | 0.1 | 0.2 | (38.2) |
| Finance costs | (0.2) | (0.2) | 21.6 | (0.2) | 1.1 | (0.2) | (0.2) | 21.6 |
| Pretax profit | 40.9 | 35.1 | 16.6 | 41.8 | (2.2) | 40.9 | 35.1 | 16.6 |
| Tax expense | (12.1) | (10.1) | 19.0 | (9.4) | 27.9 | (12.1) | (10.1) | 19.0 |
| Minority interest | (2.3) | (2.0) | 14.0 | (2.8) | (18.8) | (2.3) | (2.0) | 14.0 |
| Net profit | 26.5 | 22.9 | 15.7 | 29.5 | (10.3) | 26.5 | 22.9 | 15.7 |
| Net profit ex-EI | 25.6 | 22.4 | 14.4 | 29.7 | (13.9) | 25.6 | 22.4 | 14.4 |
| Basic EPS (sen) | 1.7 | 2.2 | (22.8) | 1.9 | (10.1) | 1.7 | 2.2 | (22.8) |
| Margin (%) | 1Q22 | 1Q21 | +/- ppt YoY | 4Q21 | +/- ppt QoQ | 3M22 | 3M21 | +/- ppt YoY |
| EBIT | 34.3 | 33.8 | 0.5 | 34.4 | (0.0) | 34.3 | 33.8 | 0.5 |
| Pretax profit | 34.3 | 33.9 | 0.4 | 34.4 | (0.1) | 34.3 | 33.9 | 0.4 |
| Net profit ex-EI | 21.5 | 21.6 | (0.1) | 24.4 | (3.0) | 21.5 | 21.6 | (0.1) |
| Segmental revenue (MYR'm) | 1Q22 | 1Q21 | +/- ppt YoY | 4Q21 | +/- ppt QoQ | 3M22 | 3M21 | +/- ppt YoY |
| Taiwan | 84.9 | 70.2 | 21.0 | 84.1 | 1.0 | 84.9 | 70.2 | 21.0 |
| Singapore | 14.4 | 14.5 | (0.6) | 15.4 | (6.3) | 14.4 | 14.5 | (0.6) |
| Malaysia | 16.3 | 14.9 | 9.5 | 17.7 | (7.9) | 3.3 | 3.7 | (10.5) |
| Philippines | 3.3 | 3.7 | (10.5) | 4.1 | (19.6) | 16.3 | 14.9 | 9.5 |
| Indonesia | 0.2 | 0.2 | (15.4) | 0.1 | 25.0 | 0.2 | 0.2 | (15.4) |
| Segmental EBIT (MYR'm) | 1Q22 | 1Q21 | +/- ppt YoY | 4Q21 | +/- ppt QoQ | 3M22 | 3M21 | +/- ppt YoY |
| Taiwan | 35.2 | 27.5 | 28.2 | 32.8 | 7.5 | 35.2 | 27.5 | 28.2 |
| Singapore | 3.5 | 4.2 | (15.9) | 5.6 | (36.7) | 3.5 | 4.2 | (15.9) |
| Malaysia | 1.8 | 2.9 | (37.7) | 3.0 | (40.1) | 1.8 | 2.9 | (37.7) |
| Philippines | 0.4 | 0.6 | (29.6) | 0.5 | (18.1) | 0.4 | 0.6 | (29.6) |
| Indonesia | (0.1) | (0.2) | (53.5) | (0.1) | (18.9) | (0.1) | (0.2) | (53.5) |
| Segmental EBIT margin (%) | 1Q22 | 1Q21 | +/- ppt YoY | 4Q21 | +/- ppt QoQ | 3M22 | 3M21 | +/- ppt YoY |
| Taiwan | 41.5 | 39.2 | 2.3 | 39.0 | 2.5 | 41.5 | 39.2 | 2.3 |
| Singapore | 24.5 | 29.0 | (4.5) | 36.3 | (11.8) | 24.5 | 29.0 | (4.5) |
| Malaysia | 10.9 | 19.2 | (8.3) | 16.8 | (5.9) | 53.6 | 77.1 | (23.5) |
| Philippines | 13.4 | 17.1 | (3.6) | 13.2 | 0.2 | 2.7 | 4.3 | (1.5) |
| Indonesia | (58.2) | (106.0) | 47.7 | (89.7) | 31.5 | (58.2) | (106.0) | 47.7 |

Source: Company data. Maybank IBG Research

Fig. 2: Frontken Corp’s 12M forward PER band (currently trading at 29.7x)



Source: Bloomberg, Maybank IBG Research

Fig. 3: Frontken Corp’s 12M forward PBV band (currently trading at 7.4x)



Source: Bloomberg, Maybank IBG Research

Risk statement

There are several risk factors for our earnings estimates, target price and rating for Frontken Corp. A sharp downturn in the global markets for electronics and/or oil & gas will affect the demand for Frontken Corp’s services. Additionally, forex volatility, especially USD/MYR, will also affect Frontken Corp’s earnings, as about 1/5 of the Group’s revenue is denominated in USD.

| FYE 31 Dec | FY20A | FY21A | FY22E | FY23E | FY24E |
|-------------------------------------|--------------|--------------|--------------|--------------|--------------|
| Key Metrics | | | | | |
| P/E (reported) (x) | 36.8 | 50.5 | 31.3 | 27.4 | 25.9 |
| Core P/E (x) | 46.0 | 60.2 | 31.3 | 27.4 | 25.9 |
| P/BV (x) | 8.5 | 13.2 | 7.5 | 7.4 | 7.3 |
| P/NTA (x) | 9.2 | 14.3 | 8.0 | 7.8 | 7.8 |
| Net dividend yield (%) | 1.1 | 1.0 | 1.6 | 1.8 | 1.9 |
| FCF yield (%) | 3.3 | 0.3 | 2.1 | 3.6 | 3.8 |
| EV/EBITDA (x) | 28.2 | 37.7 | 18.3 | 16.4 | 15.8 |
| EV/EBIT (x) | 30.4 | 40.9 | 20.8 | 18.3 | 17.5 |
| INCOME STATEMENT (MYR m) | | | | | |
| Revenue | 368.3 | 450.2 | 577.9 | 609.9 | 644.2 |
| EBITDA | 122.3 | 161.9 | 211.5 | 237.1 | 249.2 |
| Depreciation | (18.4) | (17.7) | (25.6) | (24.5) | (24.5) |
| Amortisation | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 |
| EBIT | 113.7 | 149.3 | 185.9 | 212.6 | 224.7 |
| Net interest income / (exp) | 0.6 | 0.2 | 0.9 | 0.9 | 0.9 |
| Associates & JV | 0.0 | 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 | 114.3 | 149.5 | 186.8 | 213.5 | 225.6 |
| Income tax | (25.9) | (35.3) | (44.1) | (50.4) | (53.2) |
| Minorities | (6.4) | (9.7) | (13.6) | (15.5) | (16.4) |
| Discontinued operations | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 |
| Reported net profit | 82.0 | 104.5 | 129.2 | 147.6 | 156.0 |
| Core net profit | 81.0 | 104.6 | 129.2 | 147.6 | 156.0 |
| BALANCE SHEET (MYR m) | | | | | |
| Cash & Short Term Investments | 312.2 | 228.3 | 218.4 | 188.0 | 151.8 |
| Accounts receivable | 110.7 | 123.3 | 156.1 | 164.4 | 173.2 |
| Inventory | 20.0 | 21.2 | 23.4 | 23.6 | 25.1 |
| Reinsurance assets | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 |
| Property, Plant & Equip (net) | 121.7 | 224.1 | 276.6 | 309.1 | 341.6 |
| 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 | 19.8 | 19.5 | 19.0 | 19.0 | 19.0 |
| Total assets | 618.1 | 650.1 | 727.3 | 737.8 | 744.4 |
| ST interest bearing debt | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 |
| Accounts payable | 118.0 | 124.3 | 130.1 | 130.5 | 132.4 |
| Insurance contract liabilities | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 |
| LT interest bearing debt | 9.5 | 1.3 | 1.3 | 1.3 | 1.3 |
| Other liabilities | 24.0 | 18.0 | 18.0 | 18.0 | 18.0 |
| Total Liabilities | 151.1 | 143.7 | 149.5 | 149.8 | 151.8 |
| Shareholders Equity | 440.0 | 475.5 | 540.1 | 549.3 | 553.5 |
| Minority Interest | 27.0 | 30.9 | 37.7 | 38.6 | 39.1 |
| Total shareholder equity | 467.0 | 506.4 | 577.8 | 588.0 | 592.6 |
| Total liabilities and equity | 618.1 | 650.1 | 727.3 | 737.8 | 744.4 |
| CASH FLOW (MYR m) | | | | | |
| Pretax profit | 114.3 | 149.5 | 186.8 | 213.5 | 225.6 |
| Depreciation & amortisation | 18.4 | 17.7 | 25.6 | 24.5 | 24.5 |
| Adj net interest (income)/exp | (0.6) | (0.2) | (0.9) | (0.9) | (0.9) |
| Change in working capital | 12.1 | (7.5) | (29.2) | (8.1) | (8.3) |
| Cash taxes paid | (22.9) | (35.3) | (44.1) | (50.4) | (53.2) |
| Other operating cash flow | (0.6) | 0.0 | 0.0 | 0.0 | 0.0 |
| Cash flow from operations | 131.8 | 124.1 | 138.2 | 178.5 | 187.7 |
| Capex | (7.7) | (102.4) | (52.5) | (32.5) | (32.5) |
| Free cash flow | 124.1 | 21.7 | 85.7 | 146.0 | 155.2 |
| Dividends paid | (29.1) | (68.8) | (71.4) | (81.6) | (86.2) |
| Equity raised / (purchased) | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 |
| Change in Debt | (5.7) | 0.0 | 0.0 | 0.0 | 0.0 |
| Other invest/financing cash flow | (4.8) | 0.2 | 0.9 | 0.9 | 0.9 |
| Effect of exch rate changes | 6.2 | 0.0 | 0.0 | 2.0 | 4.0 |
| Net cash flow | 90.8 | (46.9) | 15.2 | 67.4 | 73.9 |

| FYE 31 Dec | FY20A | FY21A | FY22E | FY23E | FY24E |
|--|----------|----------|----------|----------|----------|
| Key Ratios | | | | | |
| Growth ratios (%) | | | | | |
| Revenue growth | 8.4 | 22.2 | 28.4 | 5.5 | 5.6 |
| EBITDA growth | 7.6 | 32.4 | 30.6 | 12.1 | 5.1 |
| EBIT growth | 18.6 | 31.3 | 24.6 | 14.4 | 5.7 |
| Pretax growth | 18.7 | 30.8 | 25.0 | 14.3 | 5.7 |
| Reported net profit growth | 18.5 | 27.5 | 23.6 | 14.3 | 5.7 |
| Core net profit growth | 17.3 | 29.1 | 23.5 | 14.3 | 5.7 |
| Profitability ratios (%) | | | | | |
| EBITDA margin | 33.2 | 36.0 | 36.6 | 38.9 | 38.7 |
| EBIT margin | 30.9 | 33.2 | 32.2 | 34.9 | 34.9 |
| Pretax profit margin | 31.0 | 33.2 | 32.3 | 35.0 | 35.0 |
| Payout ratio | 51.1 | 60.3 | 50.0 | 50.0 | 50.0 |
| DuPont analysis | | | | | |
| Net profit margin (%) | 22.3 | 23.2 | 22.4 | 24.2 | 24.2 |
| Revenue/Assets (x) | 0.6 | 0.7 | 0.8 | 0.8 | 0.9 |
| Assets/Equity (x) | 1.4 | 1.4 | 1.3 | 1.3 | 1.3 |
| ROAE (%) | 20.1 | 22.8 | 25.4 | 27.1 | 28.3 |
| ROAA (%) | 14.3 | 16.5 | 18.8 | 20.2 | 21.1 |
| Liquidity & Efficiency | | | | | |
| Cash conversion cycle | (22.9) | (28.9) | (28.7) | (22.0) | (16.0) |
| Days receivable outstanding | 99.9 | 93.5 | 87.0 | 94.6 | 94.3 |
| Days inventory outstanding | 25.8 | 25.1 | 24.6 | 25.7 | 25.1 |
| Days payables outstanding | 148.5 | 147.6 | 140.3 | 142.3 | 135.3 |
| Dividend cover (x) | 2.0 | 1.7 | 2.0 | 2.0 | 2.0 |
| Current ratio (x) | 3.2 | 2.7 | 2.8 | 2.6 | 2.4 |
| Leverage & Expense Analysis | | | | | |
| Asset/Liability (x) | 4.1 | 4.5 | 4.9 | 4.9 | 4.9 |
| 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 | 0.0 | 0.0 | 0.0 | 0.0 |
| Capex/revenue (%) | 2.1 | 22.7 | 9.1 | 5.3 | 5.0 |
| Net debt/ (net cash) | (302.7) | (226.9) | (217.1) | (186.6) | (150.5) |

Source: Company; Maybank IBG Research

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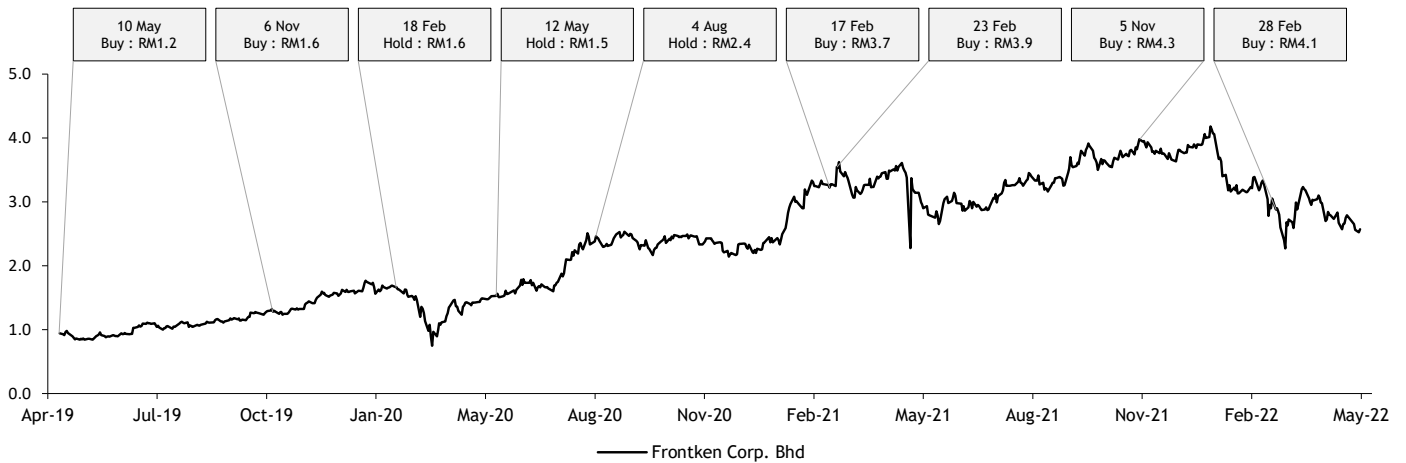
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