

## V.S. Industry (VSI MK)

# No surprises in 3QFY22 results

### Results in-line; Maintain HOLD

VSI 9MFY22 results came in within our expectations but missed the street's estimates, making up 73%/67% of ours/consensus' full-year forecasts respectively. We maintain our earnings assumptions and TP of MYR1.07, derived by pegging its fully-diluted FY23E EPS of 6.4 sen to a PER multiple of 16.7x, in-line with the company's 5-year historical PER mean. The company's near-term outlook is weighed down by on-going labour issues, raw material shortages and increasing cost pressures. However, we believe the light at the end of the tunnel is near, with the arrival of foreign labour in 4QFY22. We prefer ATECH (BUY, TP: MYR2.03) for our EMS pick.

### Labour and component shortages dragged sales

VSI's 9MFY22 core net profit (CNP) came in at MYR134m (-35% YoY). The earnings contraction was mainly down to lower order deliveries due to labour/component shortages and higher depreciation costs. Meanwhile, its 3QFY22 CNP of MYR53m (+24% QoQ, -28% YoY) came in higher QoQ despite lower revenue (-9% QoQ, -14% YoY), thanks to improving margins attributable to a more favourable product sales mix.

### Diseconomies of scale hurting profitability

Zooming in on its geographical performance, Malaysia segment's 9MFY22 revenue shrank by 3% YoY as order deliveries reduced, hampered by shortages in labour and components. Likewise, PBT slumped by a larger 37% YoY due to diseconomies of scale and higher input costs (ie. labour costs, raw material costs and depreciation costs have all increased). The Indonesia and China segments remained lacklustre, as a result of lower sales orders and diseconomies of scale respectively.

### Rising costs and inflation headwinds ahead

While we believe VSI's labour shortage concerns will start to ease with the arrival of foreign workers in the coming quarter, its recovery process from the operational disruptions could be bumpy as rising costs and inflationary pressures are likely to affect its near-term margins and dampen consumer demand for the premium consumer electronic products it assembles, respectively. Hence, we maintain our HOLD recommendation for VSI.

FYE Jul (MYR m)	FY20A	FY21A	FY22E	FY23E	FY24E
Revenue	3,243	4,002	4,356	4,940	5,364
EBITDA	227	439	355	471	552
Core net profit	105	274	182	277	342
Core FDEPS (sen)	2.8	7.3	4.3	6.4	7.8
Core FDEPS growth(%)	(74.5)	161.1	(40.4)	48.0	22.5
Net DPS (sen)	2.6	3.7	2.1	3.1	3.9
Core FD P/E (x)	25.0	19.0	23.6	15.9	13.0
P/BV (x)	1.5	2.6	1.8	1.7	1.6
Net dividend yield (%)	3.7	2.7	2.0	3.1	3.8
ROAE (%)	5.4	13.1	8.7	12.4	14.3
ROAA (%)	3.6	8.5	5.0	7.4	8.7
EV/EBITDA (x)	11.4	12.2	10.2	7.5	6.0
Net gearing (%) (incl perps)	net cash	1.2	net cash	net cash	net cash
Consensus net profit	-	-	205	323	372
MKE vs. Consensus (%)	-	-	(11.3)	(14.3)	(7.8)

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# HOLD

Share Price	MYR 1.02
12m Price Target	MYR 1.07 (+8%)
Previous Price Target	MYR 1.07

### Company Description

VS Industry Bhd is the 26th largest EMS provider in the world by revenue, ranked according to Manufacturing Market Insider in 2020.

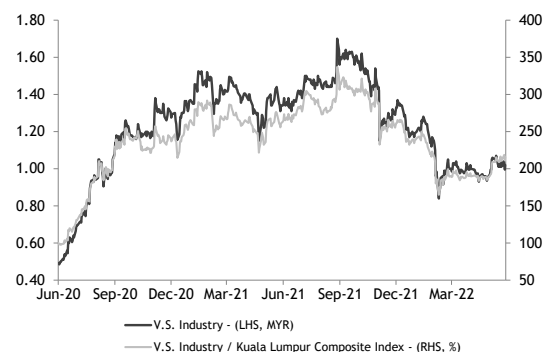
### Statistics

52w high/low (MYR)	1.70/0.84
3m avg turnover (USDm)	1.3
Free float (%)	65.5
Issued shares (m)	3,838
Market capitalisation	MYR3.9B
	USD889M

### Major shareholders:

Kumpulan Wang Persaraan	8.6%
BEH KIM LING	7.7%
BEH HWEE SZE	7.3%

### Price Performance



	-1M	-3M	-12M
Absolute (%)	7	1	(22)
Relative to index (%)	14	12	(16)

Source: FactSet

Figure 1: V.S. Industry results summary

FY Jul (MYR m)	Quarterly results					Cumulative results		
	3Q22	2Q22	%QoQ	3Q21	%YoY	9M22	9M21	%YoY
Turnover	927.6	1,014.1	(8.5)	1,074.8	(13.7)	2,909.7	3,061.2	(4.9)
EBIT	65.6	56.3	16.6	103.7	(36.7)	174.7	280.4	(37.7)
Interest expense	(2.8)	(2.6)	7.6	(2.3)	23.5	(8.4)	(8.2)	2.3
Interest income	0.4	0.9	(56.7)	0.9	(59.4)	2.2	3.1	(28.8)
Associate	(0.4)	(0.3)	29.7	(2.7)	(84.6)	(1.3)	(2.0)	(33.7)
<b>Pre-tax profit</b>	<b>62.8</b>	<b>54.2</b>	<b>15.8</b>	<b>99.6</b>	<b>(37.0)</b>	<b>167.2</b>	<b>273.3</b>	<b>(38.8)</b>
Taxation	(14.8)	(11.8)	25.7	(27.2)	(45.6)	(39.1)	(73.4)	(46.7)
Minority interest	5.4	0.0	n.m.	1.0	>100	7.0	4.0	76.2
<b>Net profit</b>	<b>53.4</b>	<b>42.4</b>	<b>25.8</b>	<b>73.4</b>	<b>(27.3)</b>	<b>135.2</b>	<b>203.9</b>	<b>(33.7)</b>
E.I.	(0.8)	(0.0)	n.m.	(0.4)	74.2	(1.5)	1.3	n.m.
<b>Core net profit</b>	<b>52.6</b>	<b>42.4</b>	<b>24.0</b>	<b>72.9</b>	<b>(27.9)</b>	<b>133.6</b>	<b>205.2</b>	<b>(34.9)</b>
	3Q22	2Q22	+/- ppt	3Q21	+/- ppt	9M22	9M21	+/- ppt
Core net profit margin (%)	5.7	4.2	1.5	6.8	(1.1)	4.6	6.7	(2.1)
Tax rate (%)	23.6	21.7	1.9	27.3	(3.7)	23.4	26.9	(3.5)
	3Q22	2Q22	%QoQ	3Q21	%YoY	9M22	9M21	%YoY
<b>Revenue (MYR m)</b>	<b>927.6</b>	<b>1,014.1</b>	<b>(8.5)</b>	<b>1,074.8</b>	<b>(13.7)</b>	<b>2,909.7</b>	<b>3,061.2</b>	<b>(4.9)</b>
Malaysia	825.1	895.6	(7.9)	939.1	(12.1)	2,575.2	2,658.7	(3.1)
Indonesia	83.9	89.1	(5.8)	95.2	(11.9)	252.3	268.7	(6.1)
China	11.5	23.9	(52.0)	37.0	(69.1)	67.3	123.8	(45.7)
Others	7.2	5.6	29.5	3.4	109.0	14.9	9.9	50.2
	3Q22	2Q22	%QoQ	3Q21	%YoY	9M22	9M21	%YoY
<b>Pretax profit (MYR m)</b>	<b>62.8</b>	<b>54.2</b>	<b>15.8</b>	<b>99.6</b>	<b>(37.0)</b>	<b>167.2</b>	<b>273.3</b>	<b>(38.8)</b>
Malaysia	67.7	54.0	25.3	99.7	(32.1)	172.1	271.2	(36.6)
Indonesia	2.4	4.0	(41.3)	2.9	(19.5)	8.5	8.2	4.0
China	(6.5)	(5.5)	18.3	(1.8)	>100	(15.2)	(7.9)	92.9
Others	(0.8)	1.7	n.m.	(1.3)	(40.0)	1.9	1.7	6.4
	3Q22	2Q22	+/- ppt	3Q21	+/- ppt	9M22	9M21	+/- ppt
<b>Pretax profit margins (%)</b>	<b>6.8</b>	<b>5.3</b>	<b>1.4</b>	<b>9.3</b>	<b>(2.5)</b>	<b>5.7</b>	<b>8.9</b>	<b>(3.2)</b>
Malaysia	6.8	5.3	1.4	9.3	(2.5)	5.7	8.9	(3.2)
Indonesia	8.2	6.0	2.2	10.6	(2.4)	6.7	10.2	(3.5)
China	2.8	4.5	(1.7)	3.1	(0.3)	3.4	3.0	0.3

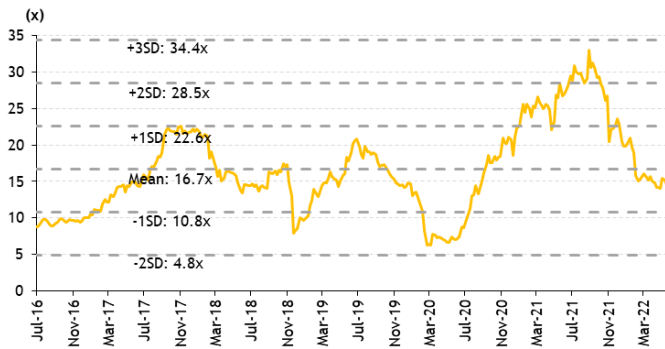
Source: Company, Maybank IBG Research

Figure 2: Revenue forecasts of selected key customers

Customer	Revenue forecasts (MYR'm)		
	FY22E	FY23E	FY24E
UK-based	1,407	1,414	1,415
US-based	987	1,050	1,092
Coffeemaker	748	806	868
Pool cleaner	344	468	558
Customer Y (Home appliances)	200	400	500

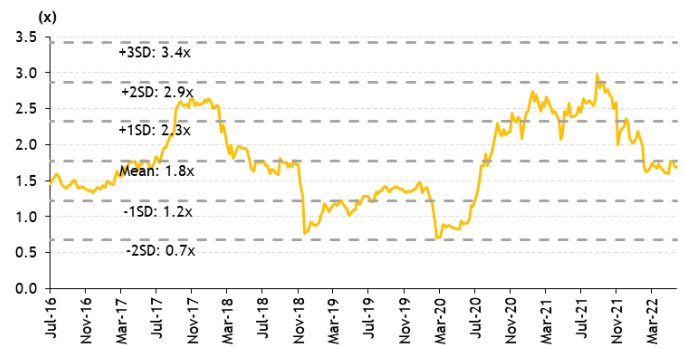
Source: Company, Maybank IBG Research

**Figure 3: VSI's 12M forward PER (currently trades at 14.4x)**



Source: Bloomberg, Maybank IBG Research

**Figure 4: VSI's 12M forward P/BV (currently trades at 1.7x)**



Source: Bloomberg, Maybank IBG Research

### Risk statement

There are several risk factors for our earnings estimates, target price and rating for VSI. Key risks are: (i) weaker-than-expected consumer demand for VSI assembled products (on weakening economics outlook); (ii) lower-than-expected costs pass through (as the mechanism depends on the company's negotiation with its clients); (iii) persistent operational disruptions from labour issues and components shortage; and (iv) USD/MYR forex volatility (we estimate for every +/-1% change in USD/MYR, bottom line impact is +/-0.5%). Potential upside includes (i) better-than-expected revenue from ramped up production (as labour and raw material shortage issue ease); (ii) new customer acquisitions; and (iii) improve margins from better efficiencies due to economics of scales.

FYE 31 Jul	FY20A	FY21A	FY22E	FY23E	FY24E
<b>Key Metrics</b>					
P/E (reported) (x)	24.3	19.1	21.4	14.0	11.3
Core P/E (x)	24.6	18.7	21.4	14.0	11.3
Core FD P/E (x)	25.0	19.0	23.6	15.9	13.0
P/BV (x)	1.5	2.6	1.8	1.7	1.6
P/NTA (x)	1.5	2.6	1.8	1.7	1.6
Net dividend yield (%)	3.7	2.7	2.0	3.1	3.8
FCF yield (%)	4.7	4.2	5.9	5.5	9.0
EV/EBITDA (x)	11.4	12.2	10.2	7.5	6.0
EV/EBIT (x)	19.2	15.8	15.5	10.0	7.7

**INCOME STATEMENT (MYR m)**

Revenue	3,243.2	4,002.3	4,356.2	4,940.4	5,364.1
EBITDA	226.7	438.6	354.9	470.8	552.0
Depreciation	(89.5)	(99.1)	(118.7)	(116.5)	(114.5)
Amortisation	(2.3)	(2.3)	(2.3)	(2.3)	(2.3)
EBIT	134.9	337.1	233.8	352.0	435.2
Net interest income / (exp)	(10.2)	(7.3)	(14.0)	(11.5)	(8.3)
Associates & JV	2.3	(0.7)	(0.7)	(0.7)	(0.7)
Other pretax income	0.0	0.0	0.0	0.0	0.0
Pretax profit	126.9	329.1	219.2	339.8	426.2
Income tax	(48.9)	(87.5)	(48.2)	(81.5)	(102.3)
Minorities	12.0	3.7	10.9	18.5	18.6
Discontinued operations	0.0	0.0	0.0	0.0	0.0
Reported net profit	90.0	245.3	181.8	276.7	342.5
Core net profit	104.6	274.3	181.8	276.7	342.5

**BALANCE SHEET (MYR m)**

Cash & Short Term Investments	404.5	402.4	863.0	930.4	1,078.4
Accounts receivable	877.6	992.1	895.1	1,015.2	1,053.2
Inventory	331.8	633.8	409.1	453.9	477.0
Reinsurance assets	0.0	0.0	0.0	0.0	0.0
Property, Plant & Equip (net)	846.9	989.5	970.8	954.3	939.8
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	364.7	577.8	473.5	467.5	461.5
<b>Total assets</b>	<b>2,825.5</b>	<b>3,595.6</b>	<b>3,611.4</b>	<b>3,821.2</b>	<b>4,010.0</b>
ST interest bearing debt	215.4	318.8	318.8	318.8	318.8
Accounts payable	576.0	844.2	767.3	838.2	879.6
Insurance contract liabilities	0.0	0.0	0.0	0.0	0.0
LT interest bearing debt	47.0	109.4	109.4	109.4	80.4
Other liabilities	118.0	106.0	106.0	106.0	106.0
<b>Total Liabilities</b>	<b>956.7</b>	<b>1,378.1</b>	<b>1,301.3</b>	<b>1,372.2</b>	<b>1,384.6</b>
Shareholders Equity	1,702.4	2,040.5	2,144.0	2,301.4	2,496.3
Minority Interest	166.4	177.0	166.1	147.7	129.1
<b>Total shareholder equity</b>	<b>1,868.8</b>	<b>2,217.5</b>	<b>2,310.1</b>	<b>2,449.1</b>	<b>2,625.4</b>
<b>Total liabilities and equity</b>	<b>2,825.5</b>	<b>3,595.6</b>	<b>3,611.4</b>	<b>3,821.2</b>	<b>4,010.0</b>

**CASH FLOW (MYR m)**

Pretax profit	126.9	329.1	219.2	339.8	426.2
Depreciation & amortisation	91.8	101.5	121.1	118.8	116.8
Adj net interest (income)/exp	10.2	7.3	14.0	11.5	8.3
Change in working capital	79.0	(266.9)	23.7	(77.4)	(1.8)
Cash taxes paid	(48.9)	(87.5)	(48.2)	(81.5)	(102.3)
Other operating cash flow	(31.2)	358.5	0.7	0.7	0.7
Cash flow from operations	227.9	442.1	330.4	311.8	447.9
Capex	(107.2)	(227.3)	(100.0)	(100.0)	(100.0)
Free cash flow	120.7	214.8	230.4	211.8	347.9
Dividends paid	(48.1)	(105.7)	(78.4)	(119.3)	(147.6)
Equity raised / (purchased)	0.0	0.0	0.0	0.0	0.0
Change in Debt	5.1	19.2	0.0	0.0	(29.0)
Other invest/financing cash flow	(19.0)	(18.1)	(25.2)	(25.2)	(23.3)
Effect of exch rate changes	21.9	19.1	0.0	0.0	0.0
Net cash flow	80.7	129.2	126.8	67.4	148.1

FYE 31 Jul	FY20A	FY21A	FY22E	FY23E	FY24E
<b>Key Ratios</b>					
<b>Growth ratios (%)</b>					
Revenue growth	(18.5)	23.4	8.8	13.4	8.6
EBITDA growth	(25.0)	93.5	(19.1)	32.7	17.3
EBIT growth	(33.6)	149.9	(30.6)	50.5	23.6
Pretax growth	(30.2)	159.3	(33.4)	55.0	25.4
Reported net profit growth	(45.6)	172.5	(25.9)	52.2	23.8
Core net profit growth	(46.6)	162.2	(33.7)	52.2	23.8
<b>Profitability ratios (%)</b>					
EBITDA margin	7.0	11.0	8.1	9.5	10.3
EBIT margin	4.2	8.4	5.4	7.1	8.1
Pretax profit margin	3.9	8.2	5.0	6.9	7.9
Payout ratio	106.8	56.2	43.1	43.1	43.1
<b>DuPont analysis</b>					
Net profit margin (%)	2.8	6.1	4.2	5.6	6.4
Revenue/Assets (x)	1.1	1.1	1.2	1.3	1.3
Assets/Equity (x)	1.7	1.8	1.7	1.7	1.6
ROAE (%)	5.4	13.1	8.7	12.4	14.3
ROAA (%)	3.6	8.5	5.0	7.4	8.7
<b>Liquidity &amp; Efficiency</b>					
Cash conversion cycle	68.2	60.5	51.9	38.9	39.0
Days receivable outstanding	103.9	84.1	78.0	69.6	69.4
Days inventory outstanding	43.3	50.0	47.8	35.6	35.9
Days payables outstanding	79.1	73.6	73.8	66.3	66.3
Dividend cover (x)	0.9	1.8	2.3	2.3	2.3
Current ratio (x)	2.0	1.9	2.0	2.1	2.2
<b>Leverage &amp; Expense Analysis</b>					
Asset/Liability (x)	3.0	2.6	2.8	2.8	2.9
Net gearing (%) (incl perps)	net cash	1.2	net cash	net cash	net cash
Net gearing (%) (excl. perps)	net cash	1.2	net cash	net cash	net cash
Net interest cover (x)	13.2	46.0	16.7	30.5	52.2
Debt/EBITDA (x)	1.2	1.0	1.2	0.9	0.7
Capex/revenue (%)	3.3	5.7	2.3	2.0	1.9
Net debt/ (net cash)	(142.1)	25.8	(434.8)	(502.2)	(679.3)

Source: Company; Maybank IBG Research

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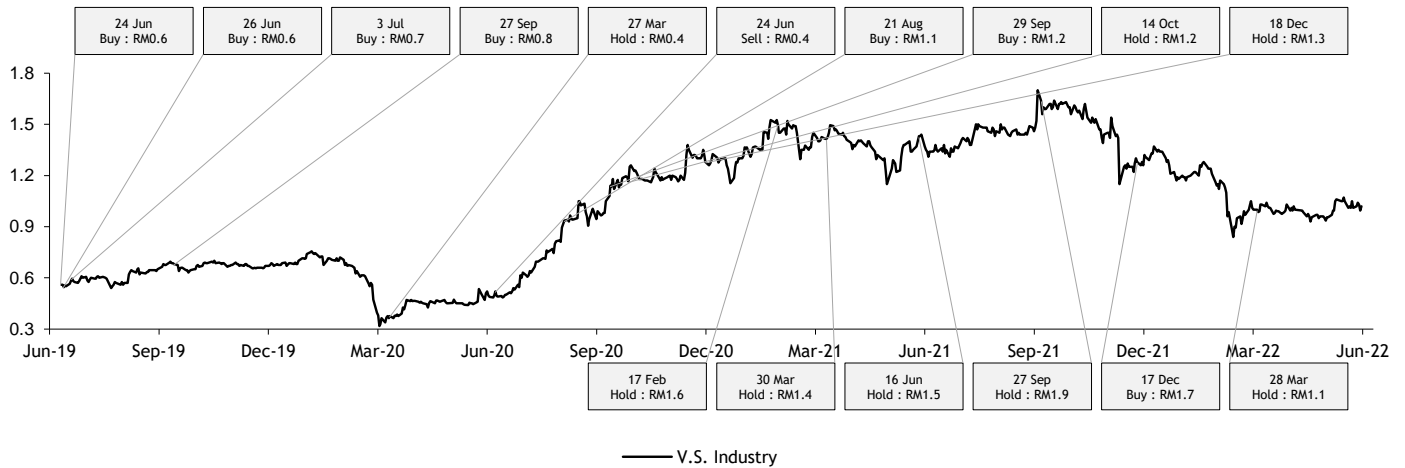
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