

Singapore Company Update

AEM Holdings Ltd

Bloomberg: AEM SP | Reuters: AEM.SI

Refer to important disclosures at the end of this report

DBS Group Research . Equity

13 Oct 2022

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HOLD (Downgrade from BUY)

Last Traded Price (12 Oct 2022): S\$3.67 (STI : 3,083.19)
Price Target 12-mth: S\$3.19 (13% downside) (Prev S\$5.88)

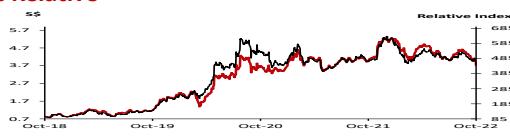
Analyst

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What's New

- Intel, AEM's key customer, plans to reduce headcount to cope with weakening demand in personal computers
- PC is one of the most affected device segments; expect shipments to drop c.15% y-o-y in 2022
- Weak PC market could lead to further capex cuts by Intel
- Downgrade to HOLD with lower TP of S\$3.19

Price Relative



Forecasts and Valuation

FY Dec (\$'m)	2021A	2022F	2023F	2024F
Revenue	565	798	702	764
EBITDA	125	157	147	160
Pre-tax Profit	111	143	132	144
Net Profit	92.1	119	109	119
Net Pft (Pre Ex.)	92.1	119	109	119
Net Pft Gth (Pre-ex) (%)	(5.6)	28.8	(8.0)	9.2
EPS (S cts)	29.9	38.6	35.5	38.7
EPS Pre Ex. (S cts)	29.9	38.6	35.5	38.7
EPS Gth Pre Ex (%)	(16)	29	(8)	9
Diluted EPS (S cts)	29.9	38.6	35.5	38.7
Net DPS (S cts)	7.60	9.79	9.01	9.84
BV Per Share (S cts)	131	160	186	215
PE (X)	12.3	9.5	10.3	9.5
PE Pre Ex. (X)	12.3	9.5	10.3	9.5
P/Cash Flow (X)	21.7	8.9	6.9	8.8
EV/EBITDA (X)	7.3	5.3	4.8	3.9
Net Div Yield (%)	2.1	2.7	2.5	2.7
P/Book Value (X)	2.8	2.3	2.0	1.7
Net Debt/Equity (X)	CASH	CASH	CASH	CASH
ROAE (%)	30.0	26.6	20.5	19.3
Earnings Rev (%):	(2)	(20)	N/A	
Consensus EPS (S cts):	39.0	44.5	51.6	
Other Broker Recs:	B: 5	S: 0	H: 1	

Source of all data on this page: Company, DBS Bank, Bloomberg Finance L.P.

Not spared from the downturn

Investment Thesis:

Earnings uncertainty in FY23F on potential of further capex cuts by Intel, AEM's key customer. To cut costs amid a slowing PC market, Intel is planning a major reduction in headcount. Earlier in July, Intel had slashed FY22F non-GAAP capex guidance by \$4bn to \$23bn and we think there is a risk that Intel may further reduce its capex spending given the PC market slowdown. While FY22 remains bright due to the ramp up of next generation handlers, the outlook for FY23 grows increasingly murky as the global economy slows.

Prolonged weakness for Intel could affect AEM. A prolonged weakness for Intel could ultimately affect AEM. AEM derives over 60% of revenue from its key customer, Intel. At the earnings level, contribution from Intel is higher as the other segments, including CEI Ltd, which AEM acquired in 2021, have generally lower margins. In terms of shipment, the consumer device markets such as PCs, mobiles and tablets are expected to see a recovery only in 2024.

Long term outlook still strong with structural trends intact. We believe AEM is well positioned to ride on the growing SLT (system level test) market that has benefitted from increased complexity of chips and increased test coverage requirements, alongside the need for advanced heterogeneous packaging.

Valuation:

Downgrade to HOLD with lower TP of S\$3.19, from S\$5.88 previously. We have reduced our revenue forecasts by 1.7% and 19.9% for FY22 and FY23 on weaker outlook for AEM's key customer, and thus our earnings forecasts by 1.6%/19.7% in FY22/FY23. We roll forward our valuation to FY23F and our TP is now pegged to 9x (vs 15x, +2SD previously), at the 5-year average PE given the overall weaker macroeconomic outlook and a slowing global PC market.

Where we differ:

We are more cautious on revenue and earnings growth.

Key Risks to Our View:

Single-customer concentration risk, geopolitical events, protraction of the COVID-19 pandemic, and FX risk.

At A Glance

Issued Capital (m shrs)	309
Mkt. Cap (\$'m/US\$m)	1,134 / 790
Major Shareholders (%)	
Venezio Investments Pte Ltd	12.1
Employees Provident Fund Board	7.1
Aberdeen PLC	6.1
Free Float (%)	74.7
3M Avg. Daily Val (US\$m)	3.9
GIC Industry : Information Technology / Semiconductors & Semiconductor Equipment	



Watchlist the stock on Insights Direct to receive prompt updates

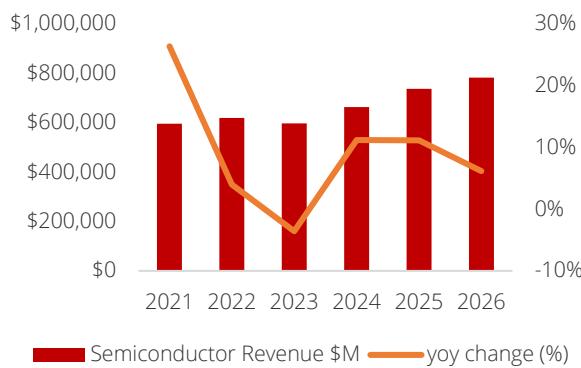


Live more. Bank less

WHAT'S NEW**Prolonged weakness for Intel could affect AEM**

Intel plans to reduce headcount to cope with weakening demand in personal computers. It was reported that Intel is planning a major reduction in headcount, likely numbering in the thousands, out of about 113,700 employees as of July, to cut costs and cope with weakening demand in the personal computer market. On the back of the rising inflation, risk of recession, and possibility of oversupply in chips due to the massive capex plans by the chip makers, tech companies are facing increasing headwinds.

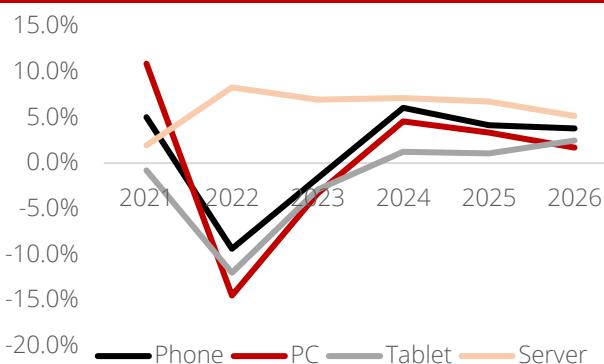
Hot semiconductor sales to turn cool. According to forecasts by Gartner, overall semiconductor revenue will grow 4.0% in 2022 followed by a 3.6% decline in 2023 (vs previous forecasts of 7.4% and -2.5%). Forecasts have been revised down to account for a deterioration in the macroeconomic environment and weakening consumer demand. Thus far, we have also seen decelerating growth rates in semiconductor shipments. As of August 2022, global semiconductor shipments came in at US\$47b, registering a meagre 0.1% y-o-y growth. The downtrend in growth rates have been observed since the start of the year and growth is likely to tip into negative territory as the global macroeconomic outlook weakens.

Semiconductor revenue

Charts/graphics created by DBS Bank based on Gartner® research.

Sources: Gartner, Inc., Semiconductor Forecast Database, Worldwide, 3Q22 Update, Ben Lee, et al., 29 Sept 2022
Semiconductors and Electronics Forecast Database, Worldwide, 3Q22 Update (gartner.com)
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PC one of the most affected segments. Demand for electronic devices has been relatively weak in recent months. Overall, we continue to expect a drop in shipment for the various consumer devices in 2022, after a stellar performance in 2021 due to the COVID pandemic, with PC segment being one of the weakest. PC shipment is expected to drop 14.5% y-o-y this year, and another 3.3% drop in 2023, according to Gartner.

Shipment by device markets

Source: Gartner, Inc., Forecast: PCs, Tablets and Mobile Phones, Worldwide, 2020-2026, 3Q22 Update, Ranjit Atwal, et al., 23 September 2022

Our Thoughts

Prolonged weakness for Intel could affect AEM. A prolonged weakness for Intel could ultimately affect AEM. AEM derives about over 60% of the group revenue from its key customer, Intel. At the earnings level, contribution from Intel is higher as the other segments, including CEI Ltd, which AEM acquired in 2021, have generally lower margins. In terms of shipment, the consumer device markets such as PCs, mobiles and tablets are expected to see a recovery only in 2024. We do not expect the new customer wins in 1H22 to wholly cushion the weakness from Intel as their contributions are relatively small compared to Intel and contributions are only likely to come in the end of FY23 or early FY24.

Potential for further capex cuts by Intel, AEM's key customer. In a bid to cut costs amid a slowing PC market, Intel is planning for a major reduction in headcount. Earlier this year in July, Intel had already slashed FY22 non-GAAP capex guidance by \$4bn to \$23bn and we think that there is a risk that Intel may further reduce its capex

spending given the PC market slowdown. Higher capital expenditure by Intel is a key revenue driver for AEM and has historically led to a greater demand for AEM's test handlers. The converse is true which dampens the outlook for FY23. On the brighter side, we are still estimating 29% earnings growth in FY22 due to the ramp up of next generation handlers.

Expect weaker 2H22 vs 1H22. We expect AEM to report revenue of S\$798m for FY22F, vs AEM's guidance of S\$750m – S\$800m. This implies a weaker 2H22 as 1H22 revenue was already S\$540m. The stellar 1H22 performance was mainly due to the strong demand of the new generation equipment and tools that were launched in 2H21. For the full year FY22F, we expect earnings to grow 29% y-o-y, after a weak FY21A where earnings dropped 6%.

Long term outlook still strong with structural trends intact. We believe that AEM is well positioned to ride on the growing SLT (system level test) market that has benefited from increased complexity of chips and increased test coverage requirements, alongside the need for advanced heterogeneous packaging.

Earnings and recommendation

Dowgrade to HOLD with lower TP of S\$3.19, from S\$5.88 previously. We have reduced our revenue forecasts by 1.7% and 19.9% for FY22 and FY23 on the weaker outlook for AEM's key customer. Accordingly, we have also reduced our earnings forecasts by 1.6% and 19.7% in FY22/FY23 in line with lower toplines. We roll forward our valuation to FY23F and our TP is pegged to 9x (vs 15x, +2SD previously), at the 5-year average PE given the overall weaker macroeconomic outlook and a slowing global PC market.

Company Background

AEM is a solutions provider for the back-end testing of the semiconductor manufacturing process. It works closely with its key customer, Intel, to design, engineer, and manufacture the test handlers. AEM then provides field support and post-sales replacements.

Historical PE and PB band**Forward PE band (x)****PB band (x)**

Source: Bloomberg Finance L.P., DBS Bank estimates

Source: Bloomberg Finance L.P., DBS Bank estimates

Income Statement (S\$M)

FY Dec	2020A	2021A	2022F	2023F	2024F
Revenue	519	565	798	702	764
Cost of Goods Sold	(352)	(379)	(547)	(470)	(512)
Gross Profit	167	187	251	232	252
Other Opg (Exp)/Inc	(54.3)	(74.8)	(110)	(102)	(111)
Operating Profit	113	112	141	129	141
Other Non Opg (Exp)/Inc	0.0	0.0	0.0	0.0	0.0
Associates & JV Inc	0.20	0.64	0.0	0.0	0.0
Net Interest (Exp)/Inc	0.45	(1.3)	1.64	2.17	2.76
Exceptional Gain/(Loss)	0.0	0.0	0.0	0.0	0.0
Pre-tax Profit	114	111	143	132	144
Tax	(16.2)	(19.1)	(24.3)	(22.4)	(24.4)
Minority Interest	0.0	0.0	0.0	0.0	0.0
Preference Dividend	0.0	0.0	0.0	0.0	0.0
Net Profit	97.6	92.1	119	109	119
Net Profit before Except.	97.6	92.1	119	109	119
EBITDA	122	125	157	147	160
Growth					
Revenue Gth (%)	60.6	9.0	41.1	(12.0)	8.9
EBITDA Gth (%)	75.3	3.0	25.5	(6.8)	8.8
Opg Profit Gth (%)	79.8	(1.2)	26.4	(8.5)	8.9
Net Profit Gth (Pre-ex) (%)	85.0	(5.6)	28.8	(8.0)	9.2
Margins & Ratio					
Gross Margins (%)	32.3	33.0	31.5	33.0	33.0
Opg Profit Margin (%)	21.8	19.8	17.7	18.4	18.4
Net Profit Margin (%)	18.8	16.3	14.9	15.6	15.6
ROAE (%)	56.4	30.0	26.6	20.5	19.3
ROA (%)	34.6	17.6	15.5	12.9	12.9
ROCE (%)	54.4	26.0	23.2	18.5	17.7
Div Payout Ratio (%)	25.4	25.4	25.4	25.4	25.4
Net Interest Cover (x)	NM	84.4	NM	NM	NM

Source: Company, DBS Bank

Interim Income Statement (S\$M)

FY Dec	1H2020	2H2020	1H2021	2H2021	1H2022
Revenue	274	245	192	373	540
Cost of Goods Sold	(166)	(149)	(127)	(252)	(374)
Gross Profit	107	96.2	65.4	121	166
Other Oper. (Exp)/Inc	(40.5)	(49.8)	(29.0)	(45.9)	(63.2)
Operating Profit	66.7	46.4	36.5	75.4	103
Other Non Opg (Exp)/Inc	0.0	0.0	0.0	0.0	0.0
Associates & JV Inc	0.26	(0.1)	(0.2)	0.85	(0.5)
Net Interest (Exp)/Inc	0.28	0.17	(0.8)	(0.6)	(0.6)
Exceptional Gain/(Loss)	0.0	0.0	0.0	0.0	0.0
Pre-tax Profit	67.3	46.5	35.5	75.6	102
Tax	(12.0)	(4.2)	(5.8)	(13.2)	(19.0)
Minority Interest	0.0	0.0	0.0	0.0	0.0
Net Profit	55.3	42.3	29.7	62.4	83.1
Net profit bef Except.	55.3	42.3	29.7	62.4	83.1
EBITDA	71.3	50.5	40.5	84.9	113
Growth					
Revenue Gth (%)	58.7	(10.4)	(21.6)	94.1	44.8
EBITDA Gth (%)	79.3	(29.1)	(19.8)	109.6	33.5
Opg Profit Gth (%)	84.2	(30.5)	(21.4)	106.6	36.8
Net Profit Gth (%)	81.5	(23.5)	(29.8)	110.1	33.1
Margins					
Gross Margins (%)	39.2	39.2	34.0	32.5	30.8
Opg Profit Margins (%)	24.4	18.9	19.0	20.2	19.1
Net Profit Margins (%)	20.2	17.2	15.4	16.7	15.4

Source: Company, DBS Bank

Balance Sheet (\$\$m)

FY Dec	2020A	2021A	2022F	2023F	2024F
Net Fixed Assets	17.6	26.1	28.7	25.0	20.1
Invts in Associates & JVs	4.68	15.9	15.9	15.9	15.9
Other LT Assets	46.8	118	116	113	110
Cash & ST Invts	135	216	297	423	510
Inventory	79.7	205	240	187	203
Debtors	47.6	128	120	106	115
Other Current Assets	4.36	1.06	1.06	1.06	1.06
Total Assets	336	711	818	870	976
ST Debt	0.0	0.0	0.0	0.0	0.0
Creditor	83.7	181	195	167	182
Other Current Liab	28.0	55.6	61.1	59.1	61.2
LT Debt	0.0	0.0	0.0	0.0	0.0
Other LT Liabilities	12.4	71.3	71.3	71.3	71.3
Shareholder's Equity	211	403	491	572	661
Minority Interests	0.0	0.0	0.0	0.0	0.0
Total Cap. & Liab.	336	711	818	870	976
Non-Cash Wkg. Capital	20.0	97.3	105	67.0	76.1
Net Cash/(Debt)	135	216	297	423	510
Debtors Turn (avg days)	26.6	56.6	56.8	58.8	52.8
Creditors Turn (avg days)	82.6	132.0	129.2	145.9	129.4
Inventory Turn (avg days)	73.0	142.0	152.9	171.8	144.4
Asset Turnover (x)	1.8	1.1	1.0	0.8	0.8
Current Ratio (x)	2.4	2.3	2.6	3.2	3.4
Quick Ratio (x)	1.6	1.5	1.6	2.3	2.6
Net Debt/Equity (X)	CASH	CASH	CASH	CASH	CASH
Net Debt/Equity ex MI (X)	CASH	CASH	CASH	CASH	CASH
Capex to Debt (%)	N/A	N/A	N/A	N/A	N/A

Source: Company, DBS Bank

Cash Flow Statement (\$\$m)

FY Dec	2020A	2021A	2022F	2023F	2024F
Pre-Tax Profit	114	111	143	132	144
Dep. & Amort.	8.42	13.0	16.0	17.4	18.7
Tax Paid	(9.8)	(20.2)	(18.8)	(24.3)	(22.4)
Assoc. & JV Inc/(loss)	(0.2)	(0.6)	0.0	0.0	0.0
Chg in Wkg.Cap.	(29.2)	(55.1)	(13.4)	40.1	(11.1)
Other Operating CF	3.33	3.96	0.0	0.0	0.0
Net Operating CF	86.3	52.1	127	165	129
Capital Exp.(net)	(30.4)	(72.9)	(16.0)	(11.0)	(11.0)
Other Invts.(net)	0.0	(2.6)	0.0	0.0	0.0
Invts in Assoc. & JV	0.0	(8.5)	0.0	0.0	0.0
Div from Assoc & JV	0.0	0.0	0.0	0.0	0.0
Other Investing CF	0.67	(1.2)	0.0	0.0	0.0
Net Investing CF	(29.8)	(85.2)	(16.0)	(11.0)	(11.0)
Div Paid	(22.2)	(18.6)	(30.1)	(27.7)	(30.3)
Chg in Gross Debt	(0.6)	56.7	0.0	0.0	0.0
Capital Issues	0.0	103	0.0	0.0	0.0
Other Financing CF	(3.1)	(27.8)	0.0	0.0	0.0
Net Financing CF	(25.9)	113	(30.1)	(27.7)	(30.3)
Currency Adjustments	(3.5)	1.11	0.0	0.0	0.0
Chg in Cash	27.1	81.4	80.7	126	87.6
Opg CFPS (S cts)	41.9	34.8	45.5	40.5	45.5
Free CFPS (S cts)	20.3	(6.8)	36.0	49.9	38.3

Source: Company, DBS Bank

Target Price & Ratings History

S.No.	Date of Report	Closing Price	12-mth Target Price	Rating
1:	25 Nov 21	5.08	6.04	BUY
2:	25 Feb 22	4.21	6.04	BUY
3:	16 Aug 22	4.50	5.88	BUY
4:	17 Aug 22	4.54	5.88	BUY

Note : Share price and Target price are adjusted for corporate actions.

Source: DBS Bank

Analyst: Lee Keng LING

Singapore Research Team

DBS Bank recommendations are based on an Absolute Total Return* Rating system, defined as follows:

STRONG BUY (>20% total return over the next 3 months, with identifiable share price catalysts within this time frame)

BUY (>15% total return over the next 12 months for small caps, >10% for large caps)

HOLD (-10% to +15% total return over the next 12 months for small caps, -10% to +10% for large caps)

FULLY VALUED (negative total return, i.e., > -10% over the next 12 months)

SELL (negative total return of > -20% over the next 3 months, with identifiable share price catalysts within this time frame)

*Share price appreciation + dividends

Completed Date: 13 Oct 2022 07:28:01 (SGT)

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