

# AEM Holdings (AEM SP)

## FY20 another record year

### 2H20 beat; maintain BUY

2H20 PATMI of SGD42.3m (+38.9% YoY) was 8%/5% ahead of our and consensus expectations, largely driven by requirements by key customer Intel. The beat vs. our expectation was due to lower-than-expected staff costs and other expenses. As AEM is unable to provide FY21 guidance currently, our forecasts are largely unchanged, and we maintain TP of SGD5.05 (14x FY21E P/E). BUY.

### Key customer drives strong revenue growth

2H20 revenue rose 42% YoY to SGD245.3m, on the back of increased requirements from the key customer. Gross material margin fell 4.5ppt YoY due to higher share of tools and machine sales (63% of revenue), which commands lower margins than consumables and services. Staff costs rose 42% YoY due to additional headcounts for R&D, other projects, as well as with the inclusion of Mu-TEST and DB-Design.

### Competition heating up

Management reiterated that as heterogeneous packaging becomes increasingly mainstream chipmakers' recognition of the need for system level test (SLT) has also increased. However, AEM expects competition to we increase from major test equipment players in SLT as well. To maintain its edge, AEM intends to continue strengthening its capabilities in-house, as well as via M&A.

### Risks and upside scenarios

The CEI acquisition is expected to close within 1H20. AEM also announced the acquisition of Lattice Innovation, which is expected to enhance AEM's capabilities in active thermal control. Our forecasts do not include contributions from CEI nor Lattice currently. We believe key risk to our FY21 earnings estimate is if there are high-base effects from strong HDMT performance in FY20. Contrastingly, we believe upside drivers are: i) accretive M&A; ii) better-than-expected cloud/ 5G spending momentum in 2H21; and/or iii) if customer Intel benefits from share gains as a result of tight foundry capacity faced by competitors.

FYE Dec (SGD m)	FY19A	FY20A	FY21E	FY22E	FY23E
Revenue	323	519	517	545	556
EBITDA	70	122	126	134	137
Core net profit	53	98	99	106	108
Core FDEPS (cts)	19.4	35.1	35.7	38.3	38.8
Core FDEPS growth(%)	58.3	80.9	1.8	7.0	1.4
Net DPS (cts)	5.1	9.0	9.0	9.6	9.8
Core FD P/E (x)	10.4	9.8	11.3	10.5	10.4
P/BV (x)	4.1	4.5	3.9	3.0	2.5
Net dividend yield (%)	2.5	2.6	2.2	2.4	2.4
ROAE (%)	47.3	56.4	39.9	32.6	26.6
ROAA (%)	29.1	34.6	27.3	24.2	20.7
EV/EBITDA (x)	6.3	6.7	7.2	6.1	5.5
Net gearing (%) (incl perps)	net cash	net cash	net cash	net cash	net cash
Consensus net profit	-	-	102	104	na
MKE vs. Consensus (%)	-	-	(2.2)	1.9	na

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# BUY

Share Price SGD 4.03  
 12m Price Target SGD 5.05 (+28%)  
 Previous Price Target SGD 5.05

### Company Description

AEM manufactures equipment used in the semiconductor back-end process

### Statistics

52w high/low (SGD)	4.62/1.37
3m avg turnover (USDm)	13.0
Free float (%)	76.9
Issued shares (m)	273
Market capitalisation	SGD1.1B USD828M

### Major shareholders:

Toh Ban Leng James	5.0%
Aberdeen Standard Investments (Asia) Ltd	5.0%
UBS Group AG	4.9%

### Price Performance



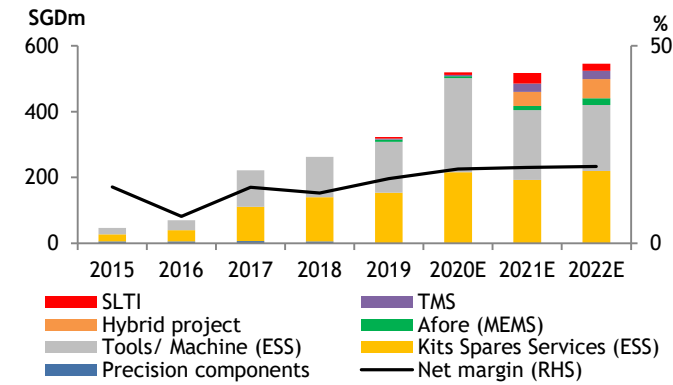
	-1M	-3M	-12M
Absolute (%)	(4)	15	86
Relative to index (%)	(4)	11	96

Source: FactSet

## Value Proposition

- Back-end test-equipment manufacturer that has co-developed the HDMT handler for a market-leading chipmaker with a market cap of USD210b.
- Leading-edge HDMT technology has helped its core customer achieve 2x savings in chip-testing costs.
- AEM provides strong synergies like field-service capabilities and manufacturing scale for the high-tech companies that it acquires.
- High single-customer and product risks.

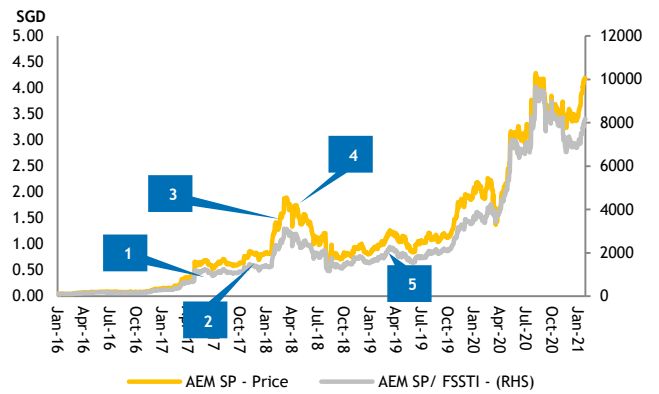
### Share of new revenue sources progressively growing



Source: Company, Maybank Kim Eng

## Price Drivers

### Historical share price trend



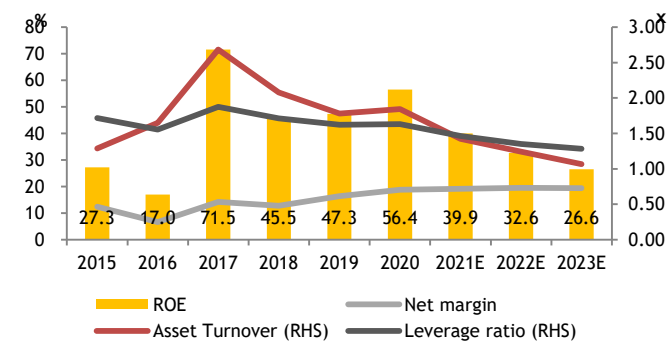
Source: Company, FactSet, Maybank Kim Eng

1. Announced favourable 1Q17 net profit as HDMT handlers delivery pick up momentum. There were also insider purchases.
2. Announced 2018 guidance for SGD255m in revenue and SGD42m PBT.
3. Announced accretive acquisition of Afore, Finnish-based MEMS test-solutions provider.
4. Novo Tellus distributes AEM shares in-specie to investors; Core customer announces 10nm delay.
5. AEM's core customer denies rumours from tech-blog SemiAccurate that its 10nm process was cancelled.

## Financial Metrics

- Over time, we expect increasing contributions from non-Intel revenue sources.
- AEM is not a capex-intensive company. Improved cash-flow from 2016 levels has allowed AEM to pursue highly synergistic acquisitions.
- Training a batch of engineers during pre-production ramp up could take 5-6 months. During such time, staff costs could be elevated and profitability could temporarily decline.
- Adopted 25% dividend payout ratio policy in 2017.

### DuPont ROE



Source: Company, Maybank Kim Eng

## Swing Factors

### Upside

- Revenue expansion from securing new customers or wallet expansion/increased orders from existing customers.
- Synergistic and accretive acquisitions.
- Positive customer-related news flow that could catalyse improved orders for AEM, such as capacity expansion or launch of new chips.

### Downside

- Order cancellation, delays and earnings misses.
- Emerging technology from rivals that could erode AEM's competitive position with customer(s).
- Erosion in the competitive advantages of the core customer as a result of company specific or industry related developments.



## Business Model & Industry Issues

- As an equipment maker, AEM is inherently exposed to environmental, workplace safety, and socio-economic risks. AEM has had zero incidences of environmental non-compliance, as well as zero substantiated cases of corruption and legal compliance issues in 2019.
- From an environmental and social perspective, AEM screens all of its suppliers. AEM constantly strives to be more efficient with electricity usage, and ensures employees are well trained and remunerated fairly.
- AEM is recognised for good transparency with shareholders, while still being able to balance business requirements (e.g. respecting non-disclosure agreements).  
AEM has several new products in the pipeline and it is engaging customers for more. In our view, this is the key for economic sustainability, as well as for development of its own employees.

### Material E issues

- AEM's environmental exposure is through energy, water and inputs (fabricated parts and electronics).
- AEM adheres to all National Environment Agency laws and regulations and has not had incidences of environmental non-compliance over the past 10 years.
- Further, AEM's constant energy-saving initiatives have resulted in energy consumption rising by only 7.5% (in kWh) in 2019 despite a 23% increase in revenue.
- AEM screens suppliers for negative environmental and social impacts, including pollutions, biodiversity loss, global warming, incidences of child labour, breaches of customer privacy, and more. All eight key fabrication suppliers and 23 key standard part suppliers were found to have no negative environmental or social impacts.

### Material S issues

- AEM values talent retention. One approach is through wages. In Malaysia, where around a-third of production takes place, AEM's entry wage for production workers have been higher than the minimum wage at least since 2017, to retain employees. Entry wages are also higher than minimum wages in the US and China.
- Workforce diversity. AEM is an equal-opportunities employer. Management are hired from local communities and consists of various nationalities. 86% of management are local across AEM's footprint globally.
- Workplace safety. AEM trains its employees on health and safety work practices. In 2018, there was 1 minor injury.
- In 2019, average training per employee was 15.7 hours, or 7,590 hours in total, to equip staff with skills across technical, project management and software domains.
- Females comprise 22-23% of the total work force, and 19-23% of new hires since 2017.  
Turnover rate per month ranged from 1.1-2.1% in FY17-19. 2020 target is to maintain turnover rate at below 1.5% a month.

### Key G metrics and issues

- The board has seven directors, of which one is the executive chairman, four are independent directors (57%), and two are non-independent, non-executive. All the directors are male.
- The audit & risk management, remuneration, and nominating committees are chaired by independent directors. The strategy committee, which works with management on long-term strategic planning, is chaired by the executive chairman.
- Executive chairman Mr. Loke Wai San plans to return to a non-executive chairman role from 1 Jan-21.
- Key management compensation (comprising the Board and senior management) accounted for 27% of staff costs in 2019 (2018:17%). FY19 profit was 58% higher YoY.
- In 2019, AEM won "Most Transparent Company Award, Technology" and was runner up for the "Singapore Corporate Governance Award" by SIAS. AEM regularly updates on its sales guidance and orders received and it's active in engaging with the investment community.
- Zero substantiated cases of corruption or legal compliance issues in 2019, to be maintained in 2020.
- AEM was granted two patents in 2019, and the staff involved were rewarded. AEM views its considerable engineering development revenue as a positive sign of customer satisfaction and relationship.

Figure 1: 2H20 P&amp;L summary

FYE Dec	2H20	2H19	1H20	YoY Chg	HoH Chg	FYE	FY20 vs. FYE
	(SGD m)	(SGD m)	(SGD m)	(%)	(%)	SGDm	
Revenue	245.3	172.5	273.7	42.2	-10.4	512.3	101
COGS	(149.1)	(97.0)	(166.4)	53.6	-10.4	(309.5)	102
Gross profit	96.2	75.5	107.3	27.5	-10.3	202.9	100
Staff costs	(35.0)	(27.8)	(32.5)	25.9	7.9	(70.2)	96
Other op. inc	0.2	0.6	3.2	-69.1	-94.4	4.0	84
Other op. exp	(10.7)	(8.5)	(7.0)	26.7	54.0	(21.0)	84
EBIT	46.4	36.5	66.7	27.0	-30.5	107.3	105
EBITDA	49.2	39.7	71.0	23.8	-30.7	112.1	106
Interest inc	0.3	0.0	0.4	nm	-18.4	1.0	67
Interest exp	(0.1)	(0.1)	(0.1)	25.2	35.8	(0.2)	112
Associates	(0.1)	0.3	0.3	-119.0	-123.8	1.0	20
Exceptionals	0.0	0.0	0.0	nm	nm	0.0	nm
Pretax profit	46.5	36.8	67.3	26.5	-30.8	109.1	104
Taxation	(4.2)	(6.3)	(12.0)	-33.1	-64.8	(18.5)	87
Net profit	42.3	30.5	55.3	38.9	-23.5	90.6	108
Minority interest	0.0	0.0	0.0	nm	nm	0.0	nm
PATMI	42.3	30.5	55.3	38.9	-23.5	90.6	108
Core PATMI	42.3	30.5	55.3	38.9	-23.5	90.6	108
					<b>Change (ppt)</b>		
Gross material margin	39.2%	43.7%	39.2%	-4.5	0.0		
Core net margin	17.2%	17.7%	20.2%	-0.4	-3.0		

Source: Company data, Maybank Kim Eng

FYE 31 Dec	FY19A	FY20A	FY21E	FY22E	FY23E
<b>Key Metrics</b>					
P/E (reported) (x)	6.2	8.4	11.2	10.4	10.3
Core P/E (x)	10.3	9.7	11.2	10.4	10.3
Core FD P/E (x)	10.4	9.8	11.3	10.5	10.4
P/BV (x)	4.1	4.5	3.9	3.0	2.5
P/NTA (x)	4.1	4.5	3.9	3.0	2.5
Net dividend yield (%)	2.5	2.6	2.2	2.4	2.4
FCF yield (%)	11.1	8.2	8.3	10.8	9.0
EV/EBITDA (x)	6.3	6.7	7.2	6.1	5.5
EV/EBIT (x)	6.9	7.2	7.8	6.5	5.9

**INCOME STATEMENT (SGD m)**

Revenue	323.1	519.0	517.3	545.4	555.5
Gross profit	130.8	203.5	210.5	224.7	228.9
EBITDA	69.5	121.6	126.2	134.4	137.1
Depreciation	(4.4)	(6.1)	(5.2)	(4.9)	(5.4)
Amortisation	(1.5)	(2.3)	(3.6)	(3.6)	(3.6)
EBIT	63.6	113.2	117.4	125.9	128.1
Net interest income / (exp)	(0.2)	0.4	0.8	0.8	0.8
Associates & JV	0.5	0.2	1.5	1.5	1.0
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	63.9	113.8	119.7	128.1	129.9
Income tax	(11.0)	(16.2)	(20.3)	(21.8)	(22.1)
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	52.9	97.6	99.3	106.3	107.8
Core net profit	52.9	97.6	99.3	106.3	107.8

**BALANCE SHEET (SGD m)**

Cash & Short Term Investments	107.7	134.8	198.1	288.0	357.1
Accounts receivable	28.0	47.6	48.8	46.8	50.6
Inventory	57.5	79.7	71.6	77.8	74.4
Property, Plant & Equip (net)	6.4	8.1	7.0	6.1	4.7
Intangible assets	19.0	56.2	56.2	56.2	56.2
Investment in Associates & JVs	4.6	4.7	6.1	7.6	8.6
Other assets	4.9	4.5	4.5	4.5	4.5
<b>Total assets</b>	<b>228.0</b>	<b>335.5</b>	<b>392.2</b>	<b>486.9</b>	<b>556.0</b>
ST interest bearing debt	0.0	0.0	0.0	0.0	0.0
Accounts payable	73.1	83.7	76.0	90.9	79.1
LT interest bearing debt	0.0	0.0	0.0	0.0	0.0
Other liabilities	20.0	40.0	30.0	30.0	30.0
<b>Total Liabilities</b>	<b>93.6</b>	<b>124.1</b>	<b>106.3</b>	<b>121.2</b>	<b>109.4</b>
Shareholders Equity	134.3	211.4	285.9	365.7	446.6
Minority Interest	0.0	0.0	0.0	0.0	0.0
<b>Total shareholder equity</b>	<b>134.3</b>	<b>211.4</b>	<b>285.9</b>	<b>365.7</b>	<b>446.6</b>
<b>Total liabilities and equity</b>	<b>228.0</b>	<b>335.5</b>	<b>392.2</b>	<b>486.9</b>	<b>556.0</b>

**CASH FLOW (SGD m)**

Pretax profit	63.9	113.8	119.7	128.1	129.9
Depreciation & amortisation	5.9	8.4	8.8	8.5	9.0
Adj net interest (income)/exp	0.0	0.0	0.0	0.0	0.0
Change in working capital	2.3	(27.2)	(10.9)	10.7	(12.1)
Cash taxes paid	(5.8)	(8.8)	(20.3)	(21.8)	(22.1)
Other operating cash flow	0.0	0.0	0.0	0.0	0.0
Cash flow from operations	65.8	86.0	95.7	124.1	103.7
Capex	(5.1)	(7.9)	(4.0)	(4.0)	(4.0)
Free cash flow	60.7	78.1	91.7	120.1	99.7
Dividends paid	(10.5)	(22.2)	(24.8)	(26.6)	(27.0)
Equity raised / (purchased)	0.0	4.9	0.0	0.0	0.0
Change in Debt	(0.3)	0.0	0.0	0.0	0.0
Other invest/financing cash flow	(1.3)	(34.7)	(3.6)	(3.6)	(3.6)
Effect of exch rate changes	0.2	0.0	0.0	0.0	0.0
Net cash flow	48.9	26.1	63.3	89.9	69.1

FYE 31 Dec	FY19A	FY20A	FY21E	FY22E	FY23E
<b>Key Ratios</b>					
<b>Growth ratios (%)</b>					
Revenue growth	23.2	60.6	(0.3)	5.4	1.9
EBITDA growth	65.8	74.9	3.8	6.5	2.0
EBIT growth	58.8	77.9	3.8	7.2	1.8
Pretax growth	59.9	78.1	5.2	7.0	1.4
Reported net profit growth	58.1	84.3	1.8	7.0	1.4
Core net profit growth	58.1	84.3	1.8	7.0	1.4
<b>Profitability ratios (%)</b>					
EBITDA margin	21.5	23.4	24.4	24.6	24.7
EBIT margin	19.7	21.8	22.7	23.1	23.1
Pretax profit margin	19.8	21.9	23.1	23.5	23.4
Payout ratio	26.0	25.4	25.0	25.0	25.0
<b>DuPont analysis</b>					
Net profit margin (%)	16.4	18.8	19.2	19.5	19.4
Revenue/Assets (x)	1.4	1.5	1.3	1.1	1.0
Assets/Equity (x)	1.7	1.6	1.4	1.3	1.2
ROAE (%)	47.3	56.4	39.9	32.6	26.6
ROAA (%)	29.1	34.6	27.3	24.2	20.7
<b>Liquidity &amp; Efficiency</b>					
Cash conversion cycle	5.2	15.0	28.6	21.7	21.7
Days receivable outstanding	27.7	26.2	33.5	31.6	31.6
Days inventory outstanding	80.2	78.3	88.8	83.8	83.8
Days payables outstanding	102.7	89.5	93.7	93.7	93.7
Dividend cover (x)	3.8	3.9	4.0	4.0	4.0
Current ratio (x)	2.2	2.4	3.4	3.8	5.0
<b>Leverage &amp; Expense Analysis</b>					
Asset/Liability (x)	2.4	2.7	3.7	4.0	5.1
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)	nm	na	na	na	na
Debt/EBITDA (x)	0.0	0.0	0.0	0.0	0.0
Capex/revenue (%)	1.6	1.5	0.8	0.7	0.7
Net debt/ (net cash)	(107.7)	(134.8)	(198.1)	(288.0)	(357.1)

Source: Company; Maybank

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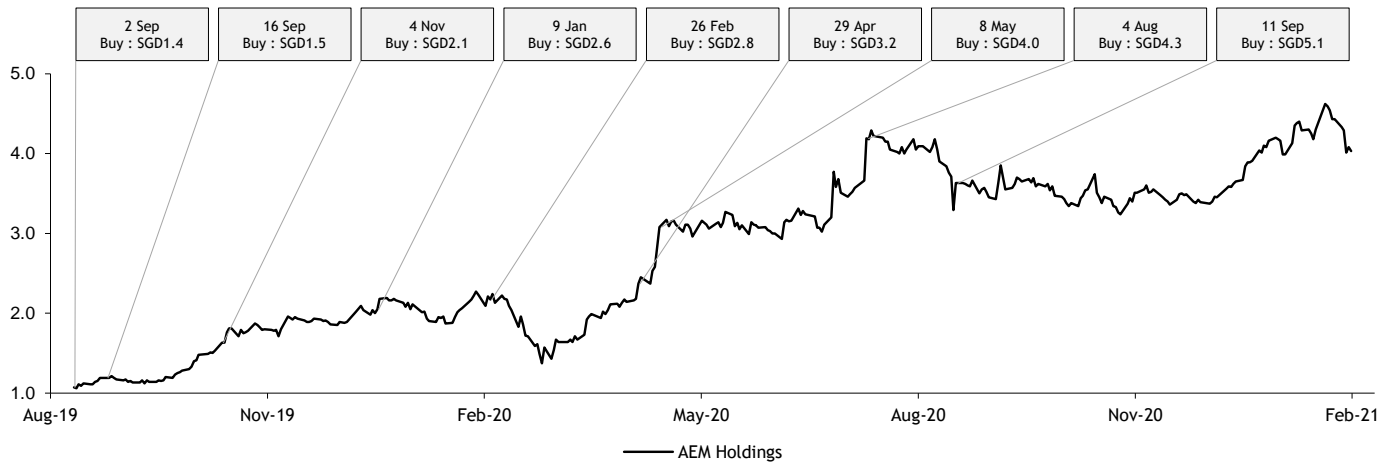
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