



# AEM Holdings Ltd

## (AEM SP/AWX.SI)

### No guidance, no worries

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- **AEM's 2H20 results in line.** In 2H20, AEM had S\$245.3mn sales (+42% YoY), S\$46.5mn PBT (+27% YoY) and S\$42.3mn PATMI (+39% YoY). Sales were below our expectations but PATMI exceeded expectations.
- **Change is constant.** AEM continued its acquisition spree with the acquisition of Lattice Innovation, incorporation of new subsidiary Wavem, and plans to acquire SGX-listed CEI Limited.
- **Maintain OUTPERFORM with lower TP of S\$5.05.** We expect AEM's blistering growth pace to decelerate this year, after 6 years of high double digit growth which saw revenue expand close to 16x from 2014's trough. AEM remains fairly undervalued relative to test equipment peers, as investors seek shelter from the lack of forward guidance.

**4Q20 left little to the imagination.** 4Q20 sales of S\$83.4mn is -5.9% YoY while 4Q20 PATMI is +7.3% YoY. FY20 core sales of S\$519mn are in the upper range of AEM's last estimate of S\$500-520mn, though missing our expectations of a guidance beat, as we were expecting a year-on-year sales beat. Production mix skewed back towards consumables in 4Q20. Overall FY20 mix is at 57% tools & machines and 43% consumables, a favourable mix for the longer term. While AEM has traditionally guided for machines to have lower margins than consumables, profit margin of 18.7% came in above our 18% estimate, supported by lower tax rates from a write back of tax provisions.

**Acquisition spree continues.** The past 2 months saw AEM announce an acquisition offer for CEI Limited (SGX: AVV), a listed contract manufacturer with focus on printed circuit boards and various semiconductor capital equipment involved in wafer sort and optical inspection. AEM cites vertical integration, improved regional presence and enhanced service and product offerings for its customers with CEI's assembly and box build capabilities. Though CEI's acquisition is EPS accretive for AEM regardless of which option CEI shareholders choose, we expect minimal positive sales impact with the acquisition, and for synergies to come from the cost end or from the strategic standpoint of supply chain diversification.

**Key customer dynamics remain the same.** Intel has hired a new CEO, Pat Gelsinger, who was an ex-CTO at Intel. In Intel's 4Q20 earnings call, Intel announced that 7nm products are on track for a 2023 launch, and most products are to be produced internally. While Intel's usage of external foundries have been headline news in recent months, we see core dynamics to be unchanged for AEM and Intel as the key products of compute and server processors are to remain in-house, a boon for AEM's HDMT and new test handler iterations.

Outperform (Maintain)		Performance (Absolute)	
Price as of 11 Mar 21 (SGD)	3.88	1 Month (%)	-9.8
12M TP (S\$)	5.05	3 Month (%)	10.6
Previous TP (S\$)	5.26	12 Month (%)	113.3
Upside (%)	30.3	<b>Perf. vs STI Index (Red)</b>	
<b>Trading data</b>			
Mkt Cap (S\$m)	1,068		
Issued Shares (mn)	275		
Vol - 3M Daily avg (mn)	4.6		
Val - 3M Daily avg (\$mn)	18.5		
Free Float (%)	87.1%		
<b>Major Shareholders</b>		<b>Previous Recommendations</b>	
James Toh Ban Leng	5.2%	5-Nov-20	OP S\$5.26
UBS	5.0%	5-Oct-20	OP S\$4.78
Morgan Stanley	5.0%	4-Aug-20	OP S\$4.60

Financials & Key Operating Statistics					
YE Dec (S\$m)	2019A	2020A	2021F	2022F	2023F
Revenue	323.3	522.3	550.4	599.1	611.3
PATMI	52.8	97.6	98.5	107.9	110.5
Core PATMI	52.6	89.2	98.0	107.4	110.0
Core EPS	0.195	0.330	0.363	0.398	0.407
Core EPS grth (%)	59.7	69.4	9.9	9.6	2.5
Core P/E (x)	19.9	11.3	10.6	9.7	9.5
DPS (SGCents)	5.1	8.6	9.1	10.0	10.2
Div Yield (%)	1.3	2.2	2.3	2.6	2.6
Net Margin (%)	16.3	18.7	17.9	18.0	18.1
Gearing (%)	net cash	net cash	net cash	net cash	net cash
Price / Book (x)	7.8	5.0	3.6	2.8	2.3
ROE (%)	47.1	56.4	34.2	32.7	26.6

Source: Company Data, KGI Research

**No guidance, no worries.** While AEM has perhaps inadvertently delayed guidance for FY21, our checks on the key customer and fellow key customer suppliers indicate that we may still be at the early-mid stages of capital equipment investment.

**Forecasts:** We continue to forecast for about 6% YoY core revenue growth, after adjusting our product mix forecast to skew towards machine production over consumables. Our profit margin forecast remains around 18% for FY21/22/23. Our forecast currently excludes the impact from CEI's acquisition.

**Valuation & Action: Maintain OUTPERFORM, with reduced 12M Target Price of S\$5.05.** We maintain 14x P/E peg, above AEM's usual PE band as we expect continued tailwinds for the semiconductor capital equipment industry. Given AEM's recent increase in production capacity, we may see further upside to our TP.

**Risks:** Weak order book, long-term competitiveness of key customer, US-China trade tensions.

## Test equipment in 2021

Test equipment outlook remains strong in 2021, after growing 14% YoY in 2020, according to VLSI Research. VLSI expects test demand to grow 10% to US\$6.9bn in 2021 on the back of strong business fundamentals in the semiconductor industry. Consensus forecasts for Advantest are at 12% growth for its next fiscal year, led by System-on-Chip tester demand. Meanwhile, Teradyne provided an FY24 guidance outlook of US\$3.875bn sales, implying a 5.6% CAGR for the next 4 years.

	FY20 sales	FY21 consensus sales forecast	2021 test market forecast
Advantest (1 USD = 106 JPY)	JP\$ 305bn* (US\$2.877bn)	JP\$ 332.69bn (US\$3.139bn)	US\$3.9 – 4.3bn
Teradyne	US\$ 3.121bn	US\$ 3.307bn	US\$4.45bn

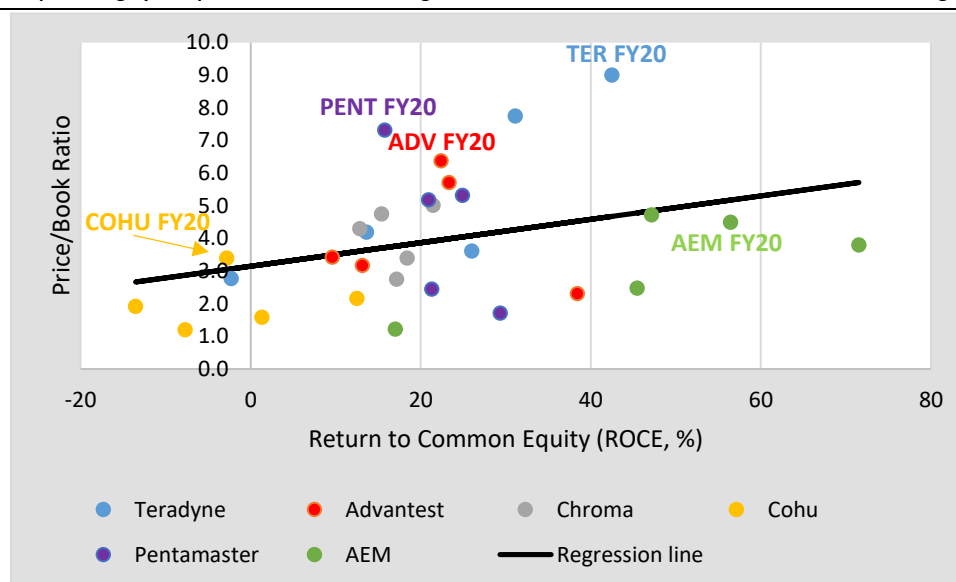
Source: Company reports. Advantest FY20 sales are from the company's own forecast.

While AEM has not provided FY21 guidance due to the CEI acquisition, we remain optimistic for AEM's order book. Positive indicators we have gathered include:

- 1) A recent refurbishment of Intel's test facility in Malaysia, which "houses the most advanced test technology in the company today", according to Intel Malaysia's managing director Robin Martin. We think that this could mean AEM's S\$143mn of sales to Malaysia are less likely to be a one-off boost.
- 2) Intel's announcement of an additional US\$475mn investment into Intel Products Vietnam, to support Intel's largest assembly and test manufacturing facility. We note that CEI's Vietnam factory is less than a 40 minute drive away from Intel's Vietnam factory, thus allowing AEM to better support Intel.
- 3) Intel supplier peers increasing production capacity, such as:
  - a. FormFactor (NASDAQ: FORM), specialising in probe cards for wafer test, who bought a new 90,000 sqft factory in 2Q20; had US\$694mn sales in 2020 and are aiming for US\$850mn sales by 2023, a 7% CAGR.
  - b. iBiden (TYO: 4062), who produce flip chip package substrates for Intel, investing JP\$ 60bn (US\$ 550mn) last year to expand production capacity.

Additionally, our updated PB-ROE chart indicates price multiple expansion for most semiconductor test peers, while AEM remains on the undervalued end. We think AEM's recent 20% share price correction was in line with other semiconductor names, which fell in similar magnitudes due to a broad rotation from tech to value stocks.

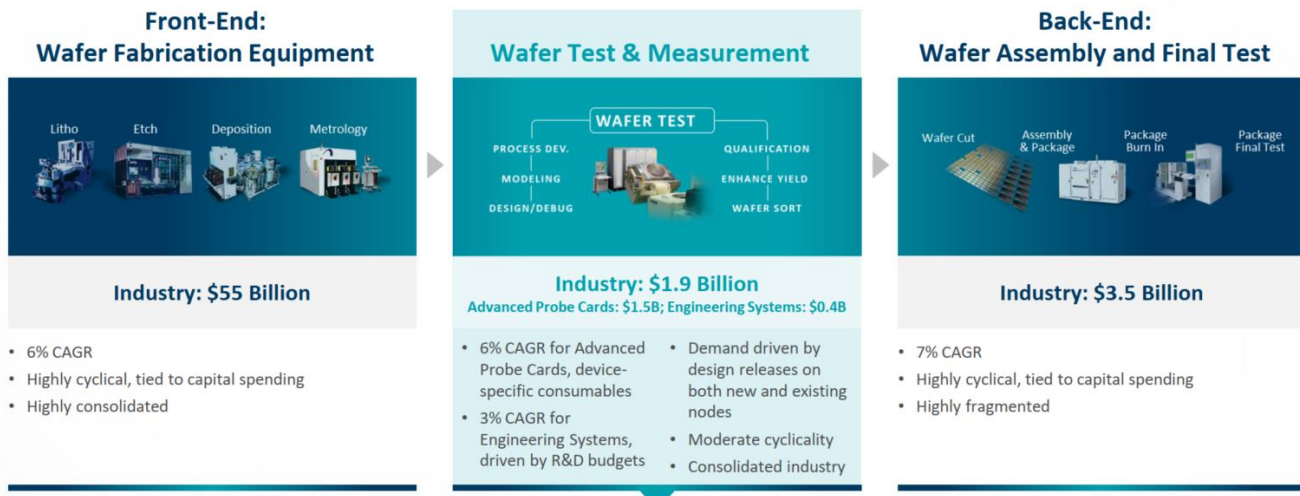
Figure 1: Test equipment peers largely saw positive valuation re-rating while AEM remained on the lower end of Price/Book range



Source: Bloomberg, KGI Research.

Figure 2: FormFactor operates between fabs and back end test, and expects to grow at 7-8% CAGR

## FormFactor Occupies a Unique Place in Semiconductor Industry



Customers' shorter product cycles and faster times-to-market amplify secular growth in silicon devices

Sources: All market size and growth rates are VLSIresearch estimates, except for Engineering Systems which are company estimates.

**Financial Forecasts**

YE 31 Dec

<b>INCOME STATEMENT (\$\$mn)</b>	<b>2019A</b>	<b>2020A</b>	<b>2021F</b>	<b>2022F</b>	<b>2023F</b>
<b>Core Revenue</b>	<b>323.1</b>	<b>519.0</b>	<b>549.8</b>	<b>598.5</b>	<b>610.7</b>
Cost of sales	(210.9)	(325.9)	(335.4)	(365.7)	(373.7)
<b>Gross Profit</b>	<b>130.8</b>	<b>203.5</b>	<b>214.4</b>	<b>232.8</b>	<b>237.0</b>
D&A expense	(6.1)	(8.4)	(9.7)	(9.3)	(8.9)
Staff expenses	(47.4)	(67.5)	(71.5)	(77.8)	(79.4)
Selling, general, admin expenses	(14.5)	(17.7)	(16.9)	(18.4)	(18.7)
Other operating income/(expenses)	0.2	3.4	0.5	0.6	0.6
<b>Profit from Operations</b>	<b>62.7</b>	<b>109.8</b>	<b>116.4</b>	<b>127.3</b>	<b>129.9</b>
Finance income/(expenses)	0.4	0.4	1.2	1.5	2.0
Share of JV results	0.5	0.2	0.5	0.6	0.6
Exceptionals/Investment income	0.0	0.0	0.0	0.0	0.0
<b>Profit before Tax</b>	<b>63.6</b>	<b>110.4</b>	<b>118.1</b>	<b>129.4</b>	<b>132.6</b>
Income tax	(11.0)	(16.2)	(20.2)	(22.1)	(22.6)
Non-controlling interests	0.0	0.0	0.0	0.0	0.0
<b>PATMI</b>	<b>52.6</b>	<b>94.2</b>	<b>97.9</b>	<b>107.3</b>	<b>109.9</b>
<b>BALANCE SHEET (\$\$mn)</b>	<b>2019A</b>	<b>2020A</b>	<b>2021F</b>	<b>2022F</b>	<b>2023F</b>
Cash and cash equivalents	107.7	134.8	209.5	290.1	374.4
Trade and other receivables	32.8	51.9	56.7	61.7	63.0
Inventory	57.5	79.7	67.1	73.1	74.7
Other current assets	0.0	0.0	0.0	0.0	0.0
<b>Current Assets</b>	<b>198.0</b>	<b>266.4</b>	<b>333.3</b>	<b>425.0</b>	<b>512.1</b>
Property, plant and equipment	6.3	8.1	8.9	10.9	12.8
Intangibles	16.9	46.6	43.8	41.5	39.8
Other non-current assets	6.8	14.4	24.2	35.2	35.1
<b>Non-current Assets</b>	<b>30.0</b>	<b>69.1</b>	<b>76.9</b>	<b>87.7</b>	<b>87.7</b>
<b>Total assets</b>	<b>228.0</b>	<b>335.5</b>	<b>410.3</b>	<b>512.7</b>	<b>599.8</b>
Trade and other payables	73.1	83.7	86.0	93.8	95.9
Borrowings (current)	0.0	5.0	0.0	0.0	0.0
Other current liabilities	18.1	23.0	22.4	22.8	22.9
<b>Current Liabilities</b>	<b>91.3</b>	<b>111.7</b>	<b>108.4</b>	<b>116.6</b>	<b>118.8</b>
Borrowings (non-current)	0.0	6.3	0.0	0.0	0.0
Other non-current liabilities	2.4	6.1	13.7	24.0	22.8
<b>Non-current liabilities</b>	<b>2.4</b>	<b>12.4</b>	<b>13.7</b>	<b>24.0</b>	<b>22.8</b>
Shareholders equity	134.3	211.4	288.1	372.2	458.2
Non-controlling interests	0.0	0.0	0.0	0.0	0.0
<b>Total Equity</b>	<b>134.3</b>	<b>211.4</b>	<b>288.1</b>	<b>372.2</b>	<b>458.2</b>
<b>Total Liabilities and Equity</b>	<b>228.0</b>	<b>335.5</b>	<b>410.3</b>	<b>512.7</b>	<b>599.8</b>
<b>CASH FLOW STATEMENT (\$\$mn)</b>	<b>2019A</b>	<b>2020A</b>	<b>2021F</b>	<b>2022F</b>	<b>2023F</b>
Net income before tax	63.7	113.8	118.6	130.0	133.2
Depreciation & Amortisation	3.3	4.4	9.7	9.3	8.9
Other non-cash adjustments	8.7	(47.2)	7.2	(4.4)	(0.8)
Change in Working Capital	(4.4)	21.2	(8.2)	2.7	0.7
Income Tax Paid	(6.6)	(9.8)	(20.2)	(22.1)	(22.6)
Interest Paid	0.2	0.0	0.0	0.0	0.0
<b>CF from operating activities</b>	<b>64.9</b>	<b>82.2</b>	<b>107.2</b>	<b>115.5</b>	<b>119.3</b>
Purchase/Disposal of PPE	(2.4)	(3.2)	(4.4)	(4.8)	(4.9)
Other CFI	(0.4)	(26.5)	1.2	1.5	2.0
<b>CF from investing activities</b>	<b>(2.8)</b>	<b>(29.8)</b>	<b>(3.2)</b>	<b>(3.3)</b>	<b>(2.9)</b>
Dividends Paid	(10.5)	(22.2)	(24.6)	(27.0)	(27.6)
Debt Raised / (Repaid)	(0.2)	0.4	0.0	0.0	0.0
Equity Raised / (Bought Back)	(1.7)	(2.9)	0.0	0.0	0.0
Other Cash from Financing	(2.8)	(1.2)	(4.6)	(4.6)	(4.6)
<b>CF from financing activities</b>	<b>(15.2)</b>	<b>(25.9)</b>	<b>(29.2)</b>	<b>(31.6)</b>	<b>(32.2)</b>
Net increase in cash & cash equiv.	49.7	30.6	74.7	80.6	84.2
FX effects	(0.9)	(3.5)	0.0	0.0	0.0
Beginning Cash	58.9	107.7	134.8	209.5	290.1
<b>Ending Cash</b>	<b>107.7</b>	<b>134.8</b>	<b>209.5</b>	<b>290.1</b>	<b>374.4</b>
<b>KEY RATIOS</b>	<b>2019A</b>	<b>2020A</b>	<b>2021F</b>	<b>2022F</b>	<b>2023F</b>
<b>Profitability</b>					
Core EPS	0.1949	0.3302	0.3629	0.3977	0.4075
Core EPS Growth (%)	59.7%	69.4%	9.9%	9.6%	2.5%
DPS (SGD Cents)	5.1	—	9.1	10.0	10.2
Dividend Yield (%)	1.3	2.2	2.3	2.6	2.6
<b>Profitability (%)</b>					
Gross margin	40.5%	39.6%	39.1%	39.0%	38.9%
EBITDA margin	21.3%	23.3%	23.0%	22.9%	22.8%
Net margin	16.3%	18.7%	17.9%	18.0%	18.1%
ROE	47.1%	56.4%	34.2%	32.7%	26.6%
ROA	29.0%	34.6%	24.0%	23.4%	19.9%
<b>Financial Structure</b>					
Interest coverage (x)	393.2	505.2	nm	nm	nm
Total Debt/Equity (%)	0.0	5.3	0.0	0.0	0.0
Net Gearing (%)	net cash	net cash	net cash	net cash	net cash
<b>Market Valuation (x)</b>					
Price / Earnings	19.9	11.3	10.6	9.7	9.5
Price / Book	7.8	5.0	3.6	2.8	2.3
Price / Sales	3.2	2.0	1.9	1.8	1.7
EV / EBITDA	13.6	7.4	6.6	5.5	4.8

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