4Q 2020 Outlook

4Q 2020 PART 3 – Our picks to sprint towards the finish line

KGI Singapore Research Team / 65 6202 1194 / sgp.kgi-research@kgi.com

Our part 3 follow-up goes more in-depth into our Tech and REITs "Outperform" call. In REITs, we see value in the retail space, while in Tech, we continue to prefer semi-related plays over contract manufacturing services. We also highlight Alibaba as a great software pick into 4Q20.

•**A volatile two weeks.** Since our Part 2 publication on 22nd September, markets have seesawed off a low on 24th September, mounted a rebound, only to see the rebound snuffed out on 2nd October upon news of US president Donald Trump's contraction of COVID-19. Friday's mood was risk-off as investors scrambled to understand the implications of Trump's current health condition on various events such as the elections, stimulus package, etc.

•**Volatility creates opportunity.** Early trading hours on Monday, 5th October, indicate optimism in Trump's recovery. While investors' focus will largely be on Trump's health in the next few days, we think any contraction should serve to benefit our recommended sectors, providing better entry points and greater alpha generation.

•**Retail REITs with good margin of safety.** Given the gloomy outlook for interest rates, in addition to a cap on banks' total dividends for FY20 (60% of FY19's distributions), we think that REITs will continue to be a favourable opportunity for many investors. Focusing solely on the last quarter of 2020, we think that retail REITs will see a boost given the quick recovery in consumer spending in 3Q20. Two of our picks are also pure-play China REITs, trading at cheap valuations despite their attractive dividends of >7%.

•**Tech's tailwinds persist, unchallenging valuations.** In lieu of September's risk-off, opportunities have emerged to accumulate on tech stocks that still ride on tailwinds into 2021. The tech sector exhibits K-shaped performance, and we expect the winners to continue extending their gains. We have a preference for the semi space, with one factory automation pick, opting to stay out of Electronic Manufacturing Services for the time being.

Company	Catalyst
REITs	
CapitaLand Mall Trust (CT SP) **CapitaLand Commercial Trust (CCT SP)**	Resulting merged entity slated to be the second largest in APAC – scale to offer larger headroom for domestic and international developments (unmatched by any S-REIT), positive re-rating for CapitaLand Integrated Commercial Trust (CICT) with higher trading liquidity and visibility
Mapletree Commercial Trust (MCT SP)	Leadership in the future Greater Southern Waterfront development to offer significant upsides to the REIT's strategically located and quality assets.
Sasseur REIT (SASSR SP)	Upside potential linked to China's growing outlet retail mall sales (the country's fastest growing retail segment), while offering downside protection with a fixed income component that increases 3% per annum until 2028. TP S$0.89, FY21F dividend yield c.8.0% based on last price of S$0.78.
EC World REIT (ECWREIT SP)	The only specialised and e-commerce logistics S-REIT that provides investment access into China's booming e-commerce industry. TP S$0.73, FY21F dividend yield c.8.5% based on last price of S$0.67.
TECHNOLOGY	
AEM Holdings (AEM SP)	Improved FY20 revenue guidance; debut of new tester could lead to another double-digit YoY increase in financial performance
UMS Holdings (UMSH SP)	US-China tensions unlikely to create big dent; current trading discounts are over-done
ISDN Holdings (ISDN SP)	Recovery in China's industrial activity, decent revenue visibility for 2H20

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Figure 1: Overall sector performance in Singapore as of 5th October

Sector Name	YTD Performance (%)	6 Months Performance (%)	Total Return 1 Year (%)	Comments	4Q20 Outlook
SG Commodities	1.44	35.61	15.88	One outperformer but sector is generally weaker off	Neutral
SG Consumer	-15.92	6.37	-12.17	Supermarket sales tapering down; generally poor outlook on retailers	Neutral
SG Energy	-15.47	9.93	-0.73	Oil still in oversupply position, recovery still a while away	Neutral
SG Financials	-15.39	13.04	-11.91	Low interest rates to stay, possible further dividend suspension	Neutral
SG Healthcare	438.20	266.61	86.57	Strong growth to continue but currently trading at challenging valuations	Neutral
SG Industrials	-23.62	-6.18	-21.37	Auto and construction outlook to remain weak, but weakness has been priced in	Neutral
SG Property	-18.74	7.90	-12.46	Residential subsector rebounds but construction delays and increased costs likely to weigh on 2021 performance	Neutral
SG REITs	-1.49	36.26	6.31	Attractive valuations coupled with spending incentives (retail) & tenant inflow (office)	Outperform
SG Technology	16.49	51.48	18.38	Strong tailwinds into 2021, unchallenging valuations	Outperform
SG Telecom	-29.09	-10.94	-22.43	Long-term competitor headwinds persist, 5G upside still murky	Underperform
SG Transport	-37.11	2.98	-34.21	Dependent on external demand, which will be muted for some time still	Neutral
SG Others	-18.81	5.03	-15.05		N/A

Source: Bloomberg, KGI Research

REITS

In the last quarter of the year, we opt to focus on the retail REIT sector as well as pure-play China retail and logistics REITs as we think that they remain undervalued considering the faster-than-expected recovery in retail spending. We believe that even if Singapore does experience a mild second wave, there is limited downside to the retail REITs whose prices still seem depressed.

While we see potential upsides for other sectors as well, all riding on Singapore's recovery out of Covid-19, we think that there are still limited catalysts for quick a recovery in the fourth quarter, and the bulk of the recovery will begin only next year, as more restrictions and measures are being relaxed over the next few months, provided community case numbers stay low and Singapore avoids a second wave of infections. The hospitality REITs' performance will also be largely dependent on the return of tourism, which we expect to be no earlier than the first quarter of 2021.

We are also positive on China's recovery as they have consistently outperformed expectations – and China is the only G20 country expected to see positive economic output this year. As such, we have highlighted two pure-play China REITs – both undervalued despite offering attractive growth potential and dividend yields.

Figure 2: Overall S-REIT performance YTD

Bloomberg Ticker	Company Name	Sub-sector	YTD Price Performance (%)
MINT SP EQUITY	Mapletree Industrial Trust	Industrial	29
MLT SP EQUITY	Mapletree Logistics Trust	Industrial	22
FLT SP EQUITY	Frasers Logistics & Commercial Trust	Industrial	18
AREIT SP EQUITY	Ascendas Real Estate Investment Trust	Industrial	14
ECWREIT SP EQUITY	EC World Real Estate Investment Trust	Industrial	-4
ALLT SP EQUITY	ARA LOGOS Logistics Trust	Industrial	-7
AAREIT SP EQUITY	AIMS APAC REIT	Industrial	-12
SSREIT SP EQUITY	Sabana Shari'ah Compliant Industrial REIT	Industrial	-19
EREIT SP EQUITY	ESR-REIT	Industrial	-23
SBREIT SP EQUITY	Soilbuild Business Space REIT	Commercial	3
KORE SP EQUITY	Keppel Pacific Oak US REIT	Commercial	-4
CERT SP EQUITY	Cromwell European Real Estate Investment Trust	Commercial	-6
AIT SP EQUITY	Ascendas India Trust	Commercial	-9
PRIME SP EQUITY	Prime US REIT	Commercial	-9
KREIT SP EQUITY	Keppel REIT	Commercial	-10
ELITE SP EQUITY	Elite Commercial REIT	Commercial	-11
IREIT SP EQUITY	IREIT Global	Commercial	-12
CCT SP EQUITY	CapitaLand Commercial Trust	Commercial	-13
MCT SP EQUITY	Mapletree Commercial Trust	Commercial	-16
SUN SP EQUITY	Suntec Real Estate Investment Trust	Commercial	-17
MAGIC SP EQUITY	Mapletree North Asia Commercial Trust	Commercial	-18
MUST SP EQUITY	Manulife US Real Estate Investment Trust	Commercial	-21
OUECT SP EQUITY	OUE Commercial Real Estate Investment Trust	Commercial	-35
DASIN SP EQUITY	Dasin Retail Trust	Retail	0
SASSR SP EQUITY	Sasseur Real Estate Investment Trust	Retail	-6
FCT SP EQUITY	Frasers Centrepoint Trust	Retail	-12
BHGREIT SP EQUITY	BHG Retail REIT	Retail	-16
SPHREIT SP EQUITY	SPH REIT	Retail	-17
CT SP EQUITY	CapitaLand Mall Trust	Retail	-19
UHU SP EQUITY	United Hampshire US REIT	Retail	-19
LREIT SP EQUITY	Lendlease Global Commercial REIT	Retail	-22
CRCT SP EQUITY	CapitaLand Retail China Trust	Retail	-24
SGREIT SP EQUITY	Starhill Global REIT	Retail	-37
LMRT SP EQUITY	Lippo Malls Indonesia Retail Trust	Retail	-59
FEHT SP EQUITY	Far East Hospitality Trust	Hospitality	-24
ART SP EQUITY	Ascott Residence Trust	Hospitality	-30
CDREIT SP EQUITY	CDL Hospitality Trusts	Hospitality	-32
FHT SP EQUITY	Frasers Hospitality Trust	Hospitality	-39
ARAUS SP EQUITY	ARA US Hospitality Trust	Hospitality	-62
KDCREIT SP EQUITY	Keppel DC REIT	Data Centre	43
PREIT SP EQUITY	Parkway Life Real Estate Investment Trust	Healthcare	27
FIRT SP EQUITY	First Real Estate Investment Trust	Healthcare	-53

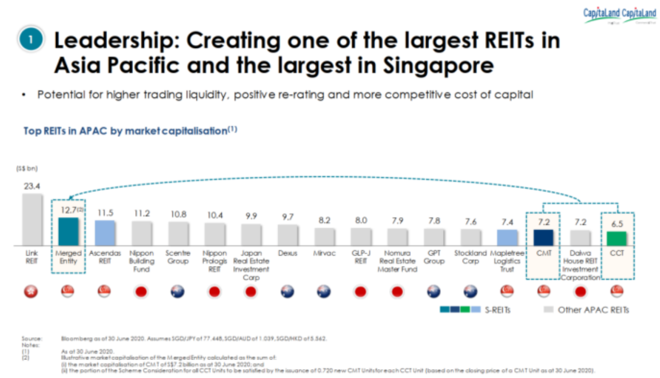
Source: Bloomberg, KGI Research

CapitaLand Mall Trust (CT SP)/ CapitaLand Commercial Trust (CCT SP)

Not rated

We continue to like the potential upsides from the merger of two CapitaLand REITs to form one of APAC's largest, just second to Link REIT listed in Hong Kong. Through Covid-19, the merger rationale has only been reinforced – to drive decentralisation, diversification and value creation. We believe that scale will inevitably attract greater visibility, paving the way for higher trading liquidity and an eventual positive re-rating of the combined entity.

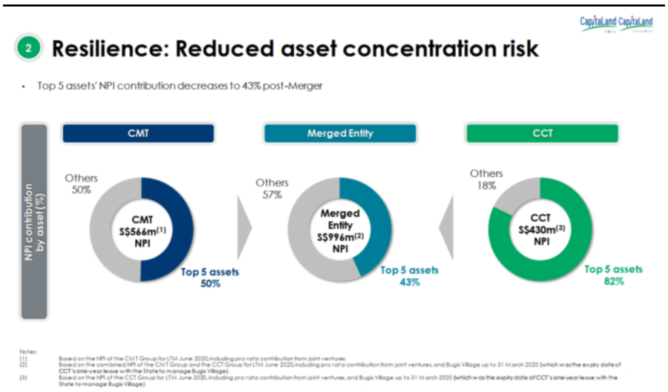
Figure 3: Merger to create one of the largest REITs in Asia Pacific and the largest in Singapore



Source: CapitaLand Mall Trust, KGI Research

The combined size, balance and diversification by value and NPI across its office, retail and integrated commercial assets will also result in a more stable and resilient portfolio that provides a robust hedge against inherent market cycles and volatility. The top five assets' NPI contribution decreases to 43% post-merger, from the current 50% and 82% for CT SP and CCT SP respectively, reducing earnings vulnerability.

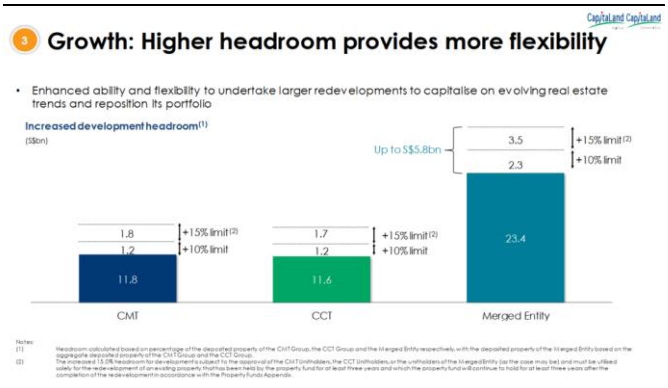
Figure 4: Diversification of assets reduces asset, tenant and trade sector concentration risks



Source: CapitaLand Mall Trust, KGI Research

The resulting REIT, CapitaLand Integrated Commercial Trust (CICT), will be in a stronger position to capitalise on accelerating trends such as the shift towards more flexible working arrangements and a greater emphasis on health and well-being. With S$5.8 billion in development headroom and proven track records in repositioning their respective portfolios to adapt to evolving real estate trends, CICT's growth potential is unmatched by any Singapore REIT. Management have expressed intentions to earmark up to 20%, from the current 4%, of the merged entity's portfolio value for overseas assets across developed markets, while still maintaining a strong 80% Singapore base. However, we note that gearing post-merger is expected to edge up to c.38%, although still significantly below MAS' adjusted 50% gearing limit.

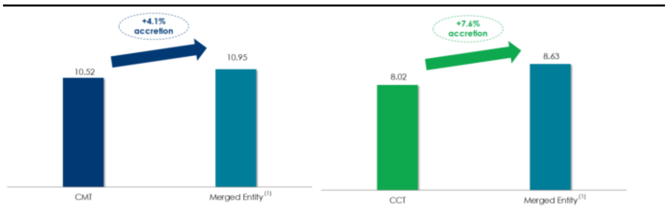
Figure 5: Significant development headroom of S$5.8 billion, unmatched by any other Singapore REIT



Source: CapitaLand Mall Trust, KGI Research

The transaction is also expected to be DPU accretive to both parties (based on *pro forma* DPU attributable to the Unitholders for LTM June 2020) – CMT unitholders will see a 4.1% accretion while CCT unitholders will see a 7.6% accretion post-merger.

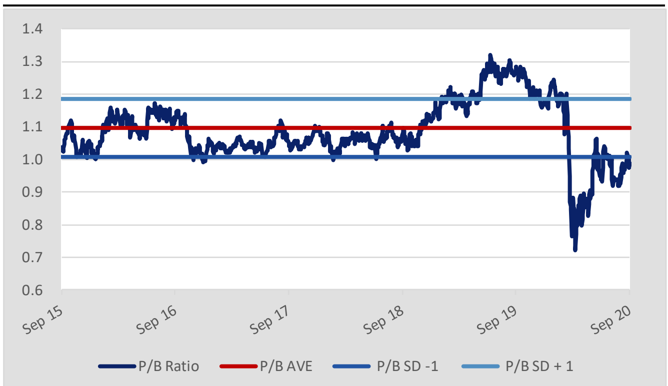
Figure 6: Transaction to be DPU accretive to both CMT and CCT unitholders



Source: CapitaLand Mall Trust, KGI Research

At less than S$2.00 and less than 1.0x P/B (about 1 s.d. below its five-year average of 1.1x P/B), and given the limited potential downside, we think it still presents an attractive opportunity for investors looking for resilient yields (FY21 dividend yield is estimated at 5.88%) as CICT's long term growth potential remains solid.

Figure 7: CT SP P/B Ratio, 2015-2020



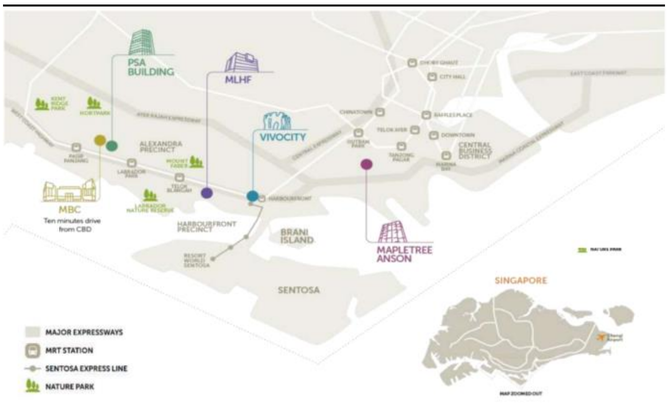
Source: Bloomberg, KGI Research

Mapletree Commercial Trust (MCT SP)

Not Rated

We believe that there still remains significant upsides for MCT given its assets that are proximate to the future Greater Southern Waterfront (GSW), which extends from Pasir Panjang to Marina East. URA has slated for the development will take place in phases, starting with the former Pasir Panjang Power District, Keppel Club and Mount Faber in the next 5 to 10 years.

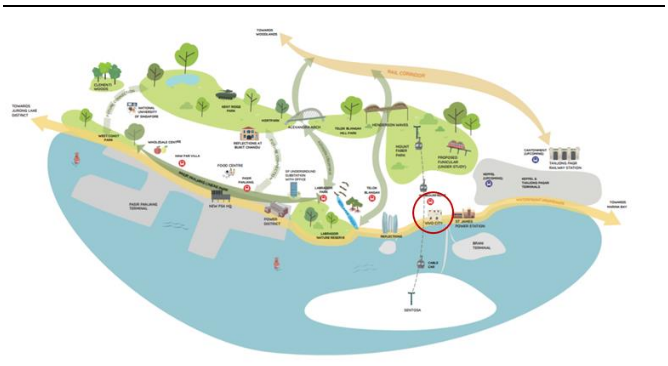
Figure 8: MCT's properties in the GSW area



Source: Mapletree Commercial Trust, KGI Research

Not only will Keppel Golf Club be redeveloped into 9,000 public and private homes with new MRT lines serving the GSW, but there are plans for Brani Terminal to be converted into a 'second Sentosa', with confirmed leisure attractions, nature parks and trails that will link multiple other parks, trails and reserves. The most noteworthy planned trail is Pasir Panjang Linear Park, a coastal trail linking Labrador Nature Reserve and West Coast Park – potentially mimicking the likes of East Coast Park.

Figure 9: MCT's Vivocity could be one of the only and largest retail malls along the GSW



Source: URA, KGI Research

With a strong fundamental foothold in the GSW area, all of MCT's assets - Mapletree Business City, PSA Building, Bank of America Merrill Lunch HarbourFront and Vivocity, are poised to benefit from the developments that could turn the bay area into an extension of the current central business district. Further, its recent MBC II acquisition completes its control over the entire Alexandra precinct, solidifying the REIT's leadership in the GSW development. We also like the asset diversification between retail and office as it has provided much needed support during the circuit breaker period. Its 1Q FY2021 NPI dipped just 10.7% YoY, despite COVID-19 rental rebates that were granted to eligible retail tenants during the quarter. This was due to the additional S$21.1mn contribution from MBC II, which was acquired in Nov 2019. Asset concentration has also improved following acquisition of MBC II, as retail contribution has fallen to 36.6% (from 45.5%).

Figure 10: MCT's Vivocity could be one of the only retail malls serving nearby neighbourhoods and residents in the bay area

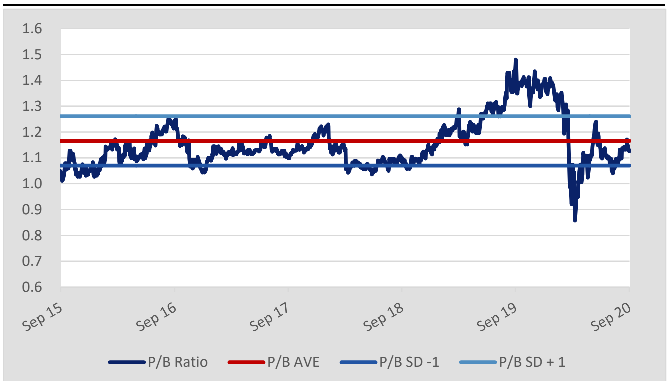
Source: URA, KGI Research

While e-commerce has affected brick-and-mortar retail spending to some extent, we believe that retail malls will remain an essential part of the Singaporean lifestyle, especially as 'pandemic fatigue' leaves many craving social interaction with friends and family. Despite also the downward pressure on valuations of retail malls due to lower expected market rent and growth assumptions in the near term, we believe that MCT's portfolio positioning will keep it buoyant and resilient.

Its balance sheet also remains strong with gearing of 33.7% (provides significant headroom to MAS's 50% limit, in support of further acquisitions of ROFR properties) and 4.1x interest coverage ratio. Debt maturity is well spread out with no more than 15% of debt due in any financial year, and weighted average cost of debt has dropped to 2.61% (from 3.00% in 1Q FY20). At current levels, dividend yields are estimated at c.4.2% and c4.8% for FY21/22 respectively.

MCT currently trades close to its 5-year average P/B and although its valuation may seem slightly expensive as compared to its peers, we believe that management's proven track record, on top of the REIT's stability and growth potential, justifies the premium.

Figure 11: MCT SP P/B Ratio, 2015-2020



Source: Bloomberg, KGI Research

Sasseur REIT (SASSR SP)
Outperform TP S$0.89

Although structured liked a REIT, Sasseur generates rents mainly through a sales-based system whereby tenants pay an agreed percentage of their sales revenue to the sponsor. Sasseur, therefore, allows investors to invest into a proxy of China's outlet retail spending, the country's fastest growing retail segment. Furthermore, its four outlet malls are located in fast growing Tier-2 cities of Chongqing, Hefei and Kunming. Demand is primarily driven by China's growing disposable income per capita.

While 2Q20 rental income declined 4.0% YoY to S$28mn, we were encouraged by the healthy sequential improvement. On a QoQ basis, rental income rose 10.7% QoQ. As a result, 2Q20 DPU declined 6.0% YoY to 1.512 Scts but improved 13.3% QoQ. 1H20 DPU makes up 48% of our forecasts and is on track to meet full-year estimates.

Figure 12: 2Q20 performance showing positive momentum

RMB'million	2Q20 sales	QoQ	YoY	1Q20 sales YoY
Chongqing	396	+70%	-62%	-62%
Bishan	79	+52%	-16%	-58%
Hefei	218	+70%	-20%	-47%
Kunming	143	+18%	-20%	-47%
Portfolio	**836**	**+56%**	**-19%**	**-56%**

Source: Sasseur REIT, KGI Research

While we believe Sasseur's team has performed well to navigate the disruptions and economic slowdown, it is still not out of the woods yet. While August 2020 retail sales rose 0.5% YoY, it is only the first month in 2020 where retail sales have improved YoY. July 2020 retail sales in China fell 1.1% YoY, an improvement from -1.8% in June, -2.8% in May, -7.5% in April and -15.8% in March.

The concern now is that China's 2Q20 GDP growth could have been driven by pent-up demand, and performance may not repeat going forward. Specifically, the jobless rate for college graduates rose to 19% in June and may exert pressure on the consumer sector.

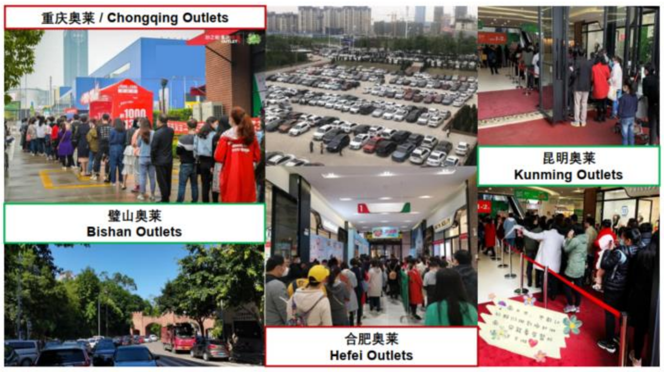
Figure 13: China's discretionary spending showed sequential improvement

Key discretionary sales	Aug YoY (%)	July YoY (%)	June YoY (%)	May YoY (%)	April YoY (%)	March YoY (%)	Jan-Feb YoY (%)
Home Appliances	+4 ▲	-2	+10 ▲	+4 ▲	-9 ▲	-30	-30
Home Furnishings	-4	-4	-1	+3 ▲	-5 ▲	-23 ▲	-34
Gold & Jewellery	+15 ▲	+8 ▲	-7	-4 ▲	-12 ▲	-30 ▲	-41
Apparel & Footwear	+4 ▲	-3	0 ▲	-1 ▲	-19 ▲	-35	-31
Cosmetics	+16 ▲	+9 ▲	+21 ▲	+13 ▲	+4 ▲	-12 ▲	-14

Source: Bloomberg, KGI Research ▲ *Sequential improvement in sales*

However, we expect the momentum to pick up further towards the last quarter of the year as local governments launch stimulus packages to spur consumption, and as spending is diverted from the restrictions on overseas travel, which is likely to last until the end of the year. Overall, there seems to be better demand visibility in China's post-COVID recovery compared to other countries, given its large domestic market and better control of the COVID-19 outbreak.

Figure 14: Long queues and significant shopper traffic improvements at Sasseur REIT's outlet malls

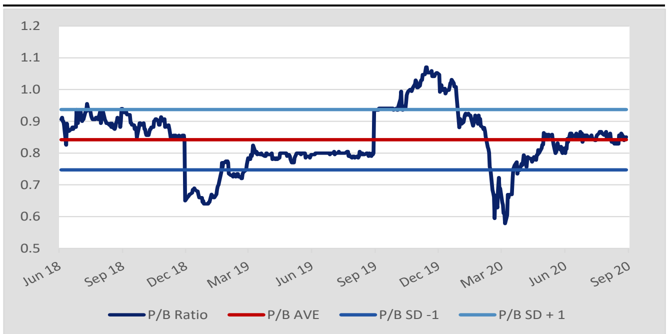


Source: Sasseur REIT, KGI Research

Stacked up against the three other China-focused retail REITs (CRCT, BHGREIT, DASIN), Sasseur has the lowest gearing (2Q20: 28.1% a comfortable level compared to peers who have gearings of between 35% and 40%). This stronger balance sheet places it in a better position to withstand property price declines, in addition to giving it more debt headroom to acquire DPU accretive assets or to implement asset enhancement initiatives, thereby driving higher operational yield.

Furthermore, Sasseur also offers the highest forward dividend yield of >7.0%, which is 100-300 bp higher than both Singapore and China-focused retail REITs. We think there could be additional DPU upside if management can continue to take advantage of lower interest rates. So far, it has done a good job of bringing down weighted average cost of debt to 4.17% in 2Q20 (4Q19: 4.41%). It is in the final stage of refinancing a S$125mn offshore loan due March 2021, which is based on a floating rate pegged to Singapore SOR.

Figure 15: SASSR SP P/B Ratio, 2018 (IPO) - 2020



Source: Bloomberg, KGI Research

We value SASSR at S$0.89 based on DDM. Our DDM-based valuation utilises a conservative set of assumptions, with a 9.0% cost of equity and 2.0% terminal growth rate. We also note that liquidity of Sasseur has improved since its IPO in 2018. The REIT was also included in the FTSE EPRA NAREIT Global Emerging Market Index in 2019, which is a well-followed index tracking global property-related companies.

EC World REIT (ECWREIT SP)
Outperform TP S$0.73

EC World REIT is the only specialized and e-commerce logistics S-REIT that provides investment access into China's booming e-commerce industry. c.40% of its investment assets (by AUM valuation) are also quality port logistics assets with prime and coveted access to the Beijing-Hangzhou Grand Canal due to recent UNESCO Heritage Site zonings. In total, the REIT has 8 quality assets located in Hangzhou and Wuhan, comprising specialized, ecommerce and port logistics assets, providing a good mix of stable income and growth potential.

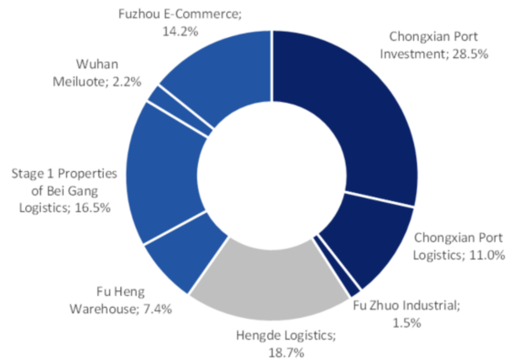
EC World REIT also has the established and capable Forchn Holdings Group co as its sponsor, who boasts ownerships of some of the leading brands in China in their respective categories – Ruyicang (Ecommerce Logistics Services), Zhang Xiao Quan (Consumer Goods), Est Mall (Real Estate) and Fuchun Resort (Health & Wellness). We believe that with the support and guidance of its sponsor, there is still a long runway for future growth and expansion.

In RMB terms, gross revenue and NPI for 1H20 were 9.5% and 11.8% higher respectively compared to 1H19, mainly due to contribution from Fuzhou E-commerce which was acquired in August 2019 and organic rental escalations, offset by one-off rental rebates (approx. RMB23.7mn or S$4.76mn) given to tenants to mitigate the adverse effects of the current COVID-19 situation on tenants' operations. We also note that management have prudently retained some cash for FY20 in view of the pandemic and increasingly volatile environment, which should be redistributed should China's recovery continue to outperform.

The lease renewal for Hengde Logistics, expiring in October 2020, is also on track and still in progress, although rental reversions are likely to be flat. Our valuations have factored in a slower reversion rate across all assets and a slightly higher cost of capital due to the uncertainties relating to China's economy especially relating to US-China trade tensions, and the impending US Presidential Elections. EC World REIT is also slightly more leveraged at 39.1% however after the acquisition of Fuzhou E-Commerce (MAS gearing limit increased to 50%), with a relatively low interest coverage ratio of 2.45x.

Nonetheless, ECW's portfolio is well-diversified into the three main logistics segments: Port, Specialised, and E-Commerce logistics, lending stability to its income. Weighted average lease expiry also stands at a healthy 3.6 years (by gross rental income). Most notably, we see the e-commerce space to be a key driver for ECW, particularly since China has quickly emerged as a global leader in e-commerce with the rise of technology (which has been further catalyzed in recent months with the outbreak of the global pandemic). This inevitably translates into demand for e-commerce logistics assets, which represent 40% of ECW's portfolio.

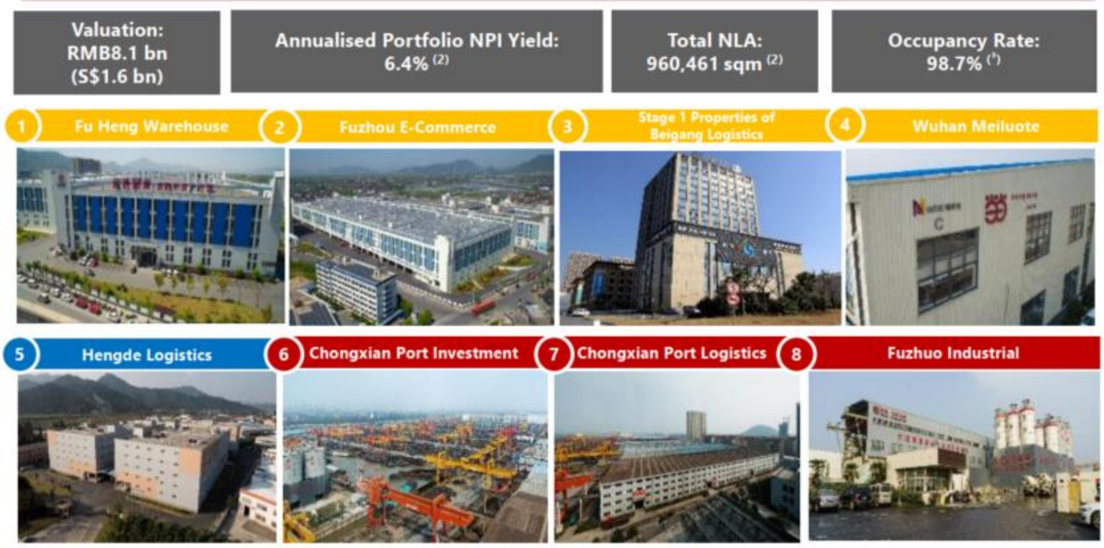
Figure 16: ECW AUM valuation breakdown by asset and logistic segment



BY AUM VALUATION	
Port Logistics	40.9%
Specialised Logistics	18.7%
E-Commerce Logistics	40.3%

Source: ECW, KGI Research

Figure 17: ECW AUM valuation breakdown by asset and logistic segment



Source: EC World REIT, KGI Research

TECH

Tan Jiunn Chyuan (Kenny) / 6202 1196 / kenny.tan@kgi.com

Figure 18: Overall Tech sector performance YTD

Bloomberg Ticker	Company Name	Sub-sector	YTD Price Performance (%)
Semi			
AEM SP EQUITY	AEM Holdings Ltd	Circuit Boards	82
MMH SP EQUITY	Micro-Mechanics Holdings Ltd	Mach Tools&Rel Products	27
AVIT SP EQUITY	Avi-Tech Electronics Ltd	Semicon Compo-Intg Circu	4
GVTL SP EQUITY	Grand Venture Technology Ltd	Electronic Compo-Semicon	4
UMSH SP EQUITY	UMS Holdings Ltd	Semiconductor Equipment	-2
ASA SP EQUITY	Advanced Systems Automation Ltd	Semiconductor Equipment	NA
Tech Manufacturing			
ISDN SP EQUITY	ISDN Holdings Ltd	Industrial Automat/Robot	66
MC SP EQUITY	Multi-Chem Ltd	Circuit Boards	53
VMS SP EQUITY	Venture Corp Ltd	Electronic Compo-Misc	27
SUNN SP EQUITY	Sunningdale Tech Ltd	Rubber/Plastic Products	15
FRKN SP EQUITY	Frencken Group Ltd	Electric Products-Misc	8
TREK SP EQUITY	Trek 2000 International Ltd	Engineering/R&D Services	6
CEI SP EQUITY	CEI Ltd	Circuit Boards	3
INNOT SP EQUITY	InnoTek Ltd	Electronic Compo-Misc	-1
PDS SP EQUITY	Powermatic Data Systems Ltd	Networking Products	-5
DTECH SP EQUITY	Dutech Holdings Ltd	Electronic Compo-Semicon	-6
BWAY SP EQUITY	Broadway Industrial Group Ltd	Computers-Memory Devices	-21
HIP SP EQUITY	Hi-P International Ltd	Electronic Compo-Misc	-23
CREAF SP EQUITY	Creative Technology Ltd/Singapore	Electronic Compo-Semicon	-24
VALUE SP EQUITY	Valuetronics Holdings Ltd	Electronic Compo-Misc	-29
PROC SP EQUITY	Procurri Corp Ltd	Telecommunication Equip	-35
Others			
REVEZ SP EQUITY	Revez Corp Ltd	Computer Services	89
SCL SP EQUITY	Synagie Corp Ltd	E-Commerce/Products	54
KTH SP EQUITY	Karin Technology Holdings Ltd	Computer Services	1
SERL SP EQUITY	Serial System Ltd	Electronic Parts Distrib	-8
CSE SP EQUITY	CSE Global Ltd	Computers-Integrated Sys	-11
ASMH SP EQUITY	A-Smart Holdings Ltd	Printing-Commercial	-15
CDW SP EQUITY	CDW Holding Ltd	Audio/Video Products	-18
ELL SP EQUITY	Ellipsiz Ltd	Electronic Compo-Semicon	-27
ADDV SP EQUITY	Addvalue Technologies Ltd	Telecommunication Equip	-29
SILV SP EQUITY	Silverlake Axis Ltd	Enterprise Software/Serv	-29
EXLP SP EQUITY	Excelpoint Technology Ltd	Electronic Compo-Misc	-33
SUNR SP EQUITY	Sunright Ltd	Electronic Compo-Semicon	-35
AZEUS SP EQUITY	Azeus Systems Holdings Ltd	Computer Services	NA
CWM SP EQUITY	Cheung Woh Technologies Ltd	Computers-Memory Devices	NA

Source: Bloomberg, KGI Research

Semi

The semiconductor sector remains healthy as recent data publications indicate that the stable, positive YoY sales trend will continue. However, the market has experienced a pullback in September; SOX's peak-to-trough performance is roughly -11%, S&P500 around -10% and NASDAQ about -13%. SGX listed prominent semiconductor and tech manufacturing names AEM, UMS and Hi-P have had peak-to-trough share price movements exceeding 20%, roughly double the fall of US benchmarks and more than triple of STI's pull-back in the same time period. The three tech manufacturing plays have traded in greater alignment with US's major indices rather than alongside STI, with AEM having the highest beta and share price volatility. As of late September/early October, we observe a nascent market recovery, which we expect to be sustained going into the last quarter.

Going forward, we expect similar demand drivers in the semi space, namely:

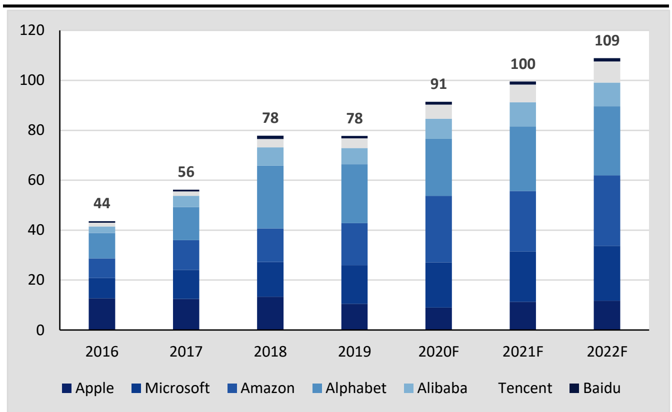
- Sustained demand and spending in the data centre space, supported by increasing Capex spend of Big Tech players whom are also hyperscalers.

- Short/medium term demand for the newest gaming consoles that will be sold late 2020. Since major console refresh cycles are usually much longer (~6 years) than other comparable entertainment devices, there will be a noticeable demand spurt.

- A GPU refresh cycle that is shaping up to offer better price-to-performance ratios than the prior year's, thus likely leading to improved demand. NVIDIA seems to have acknowledged that FY20's (ending Jan 2020) financial results in the Graphics business segment was weaker than FY19's – both sales and operating income margin were down YoY – as 2019's GPU launches did not impress consumers.

- Second, third, and possibly more waves of coronavirus that will continue to favour Work-From-Home trends, thus fuelling additional demand for home-based devices such as desktops, laptops, in-home entertainment devices such as the consoles mentioned earlier, etc. This could also stem the downtrend of desktop sales, and also supports the demand trend of data centres and data centre equipment.

Figure 19: Big Tech Capex to continue climbing (in USD bn)



Source: Bloomberg, KGI Research

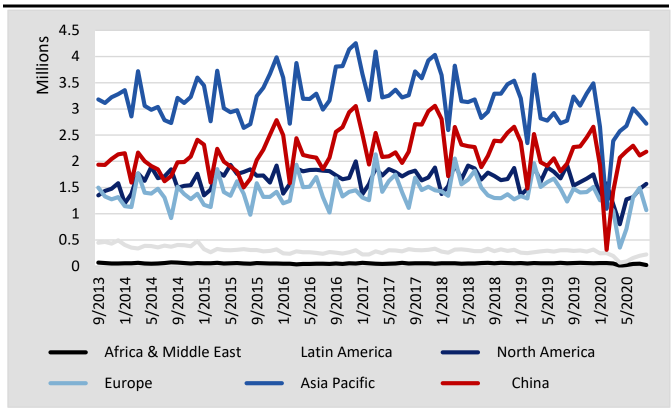
However, certain key risks continue to hold back the sector, and may have had significant contributions in causing the September sell-off. The escalation of US-China trade tensions continued to take centre stage in the tech sector, with negative developments accorded to more companies. The initial Huawei saga is still ongoing and discussions have moved beyond US, whom have cut business ties with Huawei's smartphone and networking equipment segments. Other countries such as Australia, New Zealand, Japan, Taiwan and UK have made decisions to ban or phase out Huawei's 5G equipment, with a few other European countries mulling the decision. The saga has spiralled to include a tit-for-tat reaction by the Chinese government, whom created an "unreliable entity list" that will discourage Chinese firms from working with companies in the list. While there are currently no known major tech firms on this list, the formalisation of the list creates greater uncertainty for foreign firms dealing with China, given its current ambiguity on defining "unreliable". For instance, the threat of HSBC Holdings being added to the list sent its shares down 5.3% on 21 September.

Additionally, US has increased its focus on the semiconductor space, targeting suppliers to Semiconductor Manufacturing International Corporation (SMIC), which is China's biggest semiconductor foundry, with additional export restrictions. This comes on top of prior soft restrictions, such as China's inability to get the latest photolithography machines from ASML, whom hold a monopoly on cutting edge lithography technology.

Going forward, we expect trade tensions to continue, regardless of which US political party wins in November. Both parties have stated an interest in monitoring trade activity with China, and the motion has support across both parties, albeit with differences in approach.

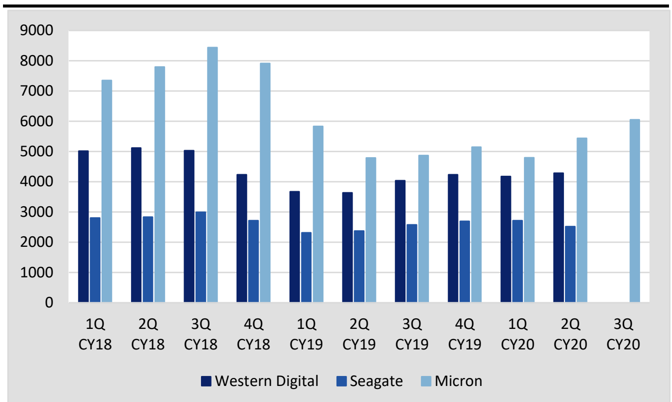
Industry-specific weakness has also persisted, with automotive sector remaining one of the worst hit. Apart from China where auto sales are currently comparable with prior year data, most other countries exhibit weaker YoY performance, which looks to continue to 2021. The memory and HDD space has also stayed in a downcycle despite supplementary demand from WFH practices, as both Seagate and Western Digital produced fairly disappointing profit figures, with a lower QoQ sales forecast for CY 3Q20. Micron's recently released results on 30 Sep also did not impress despite increased sales and income as Huawei's woes have dented Micron's outlook.

Figure 20: Regional auto sales are largely down YoY except China



Source: Bloomberg, KGI Research

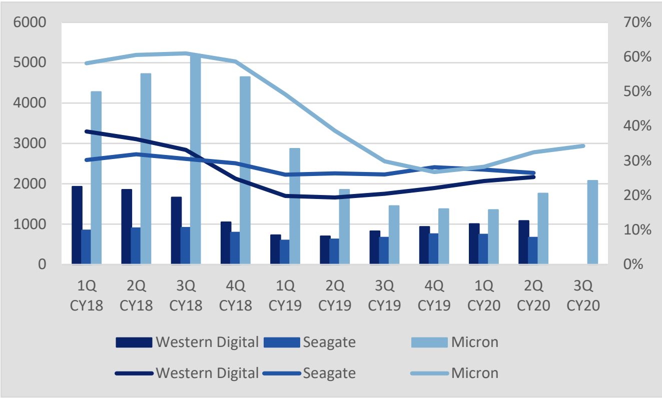
Figure 21: While memory players' sales (in USD mn) have held up…



Source: Bloomberg, KGI Research

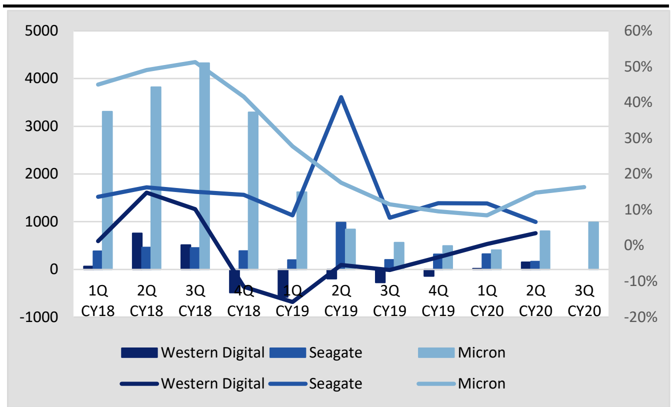
Note: Micron's Fiscal Quarter 4 ending late Aug/early Sep is treated as Calendar Quarter 3

Figure 22: Gross margins (RHS, line graph) haven fallen…



Source: Bloomberg, KGI Research

Figure 23: Net margins have also stayed low, disappointing investors

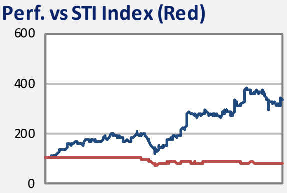


Source: Bloomberg, KGI Research

AEM Holdings (AEM SP)

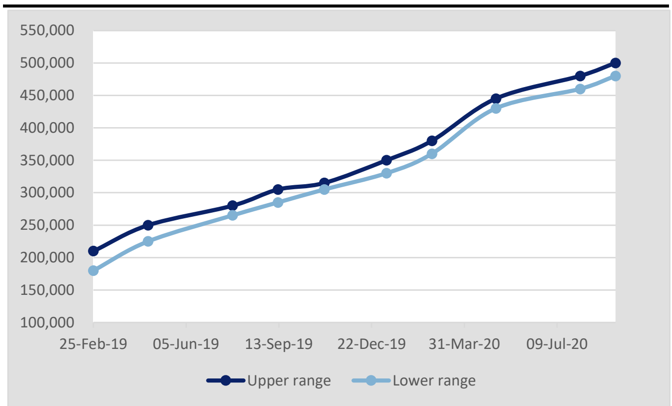
Maintain OUTPERFORM, TP S$4.78

Outperform (Maintain)			
Price as of 1 Oct 20 (SGD)	3.71	**Performance (Absolute)**	
12M TP (S$)	4.78	1 Month (%)	-9.1
Previous TP (S$)	4.60	3 Month (%)	24.1
Upside (%)	28.9	12 Month (%)	227.0
Trading data		**Perf. vs STI Index (Red)**	
Mkt Cap (S$mn)	1,019		
Issued Shares (mn)	275		
Vol - 3M Daily avg (mn)	6.5		
Val - 3M Daily avg ($mn)	23.6		
Free Float (%)	89.5%		
Major Shareholders		**Previous Recommendations**	
James Toh Ban Leng	6.8%	4-Aug-20	OP S$4.60
Standard Life Aberdeen	5.0%	23-Jul-20	OP S$4.24
Morgan Stanley	5.0%	14-May-20	OP S$3.61



We view 10 September's revised financial guidance of S$480mn – 500mn (up from 460 – 480mn) as a largely reactionary move to the day's share price performance. Beyond the update, there was little fundamental change over the month. We find that AEM's high beta seems to serve a self-fulfilling feedback loop in which a broad market contraction affects AEM more than other tech manufacturing companies, despite the company being less exposed to key sector risks such as US-China trade tensions. We adjust our sales estimate to match the new guidance, and arrive at a TP of S$4.78. Maintain OUTPERFORM.

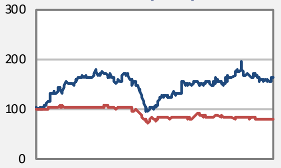
Figure 24: AEM's guided sales over FY19 and FY20



Source: Company data, KGI Research

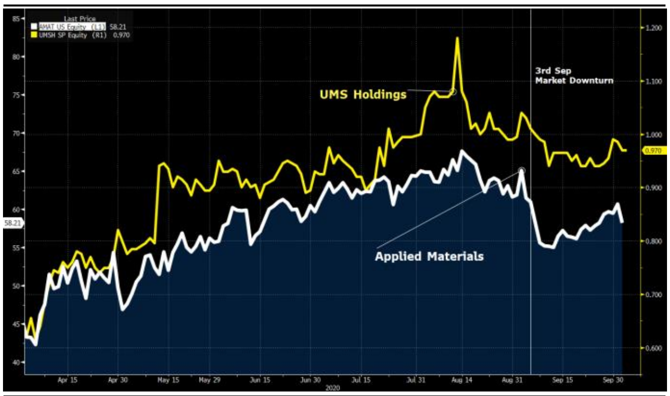
UMS Holdings (UMSH SP)

Upgrade to OUTPERFORM, TP S$1.17

Outperform (Upgrade)			
Price as of 1 Oct 20 (SGD)	0.99	**Performance (Absolute)**	
12M TP ($)	1.17	1 Month (%)	-1.0
Previous TP ($)	0.89	3 Month (%)	11.8
Upside (%)	18.4	12 Month (%)	68.6
Trading data		**Perf. vs STI Index (Red)**	
Mkt Cap ($mn)	525		
Issued Shares (mn)	533		
Vol - 3M Daily avg (mn)	8.1		
Val - 3M Daily avg ($mn)	8.2		
Free Float (%)	79.5%		
Major Shareholders		**Previous Recommendations**	
Luong Andy	20.8%	17-Aug-20	N S$1.17
Dimensional Fund Advis	1.6%	22-Jul-20	N S$0.89
eQ Rahastoyhtio Oy	0.6%	14-May-20	UP S$0.74

The earliest news on SMIC's potential blacklist came about around 6th September, yet the share price hit to key suppliers ASML, Lam Research and Applied Materials seemed to have largely came in a few days earlier on the 3rd and 4th of September, alongside retracements of major stock indices. However, AMAT's revenue dependency on SMIC is fairly small, at an estimated < 3% of sales. Hence, unlike the Huawei-Micron relationship (where Huawei is consistently ~10% of Micron's sales), we expect minimal sales fall-off, with the potential demand upswing from other customers to be sufficient to cover the gap.

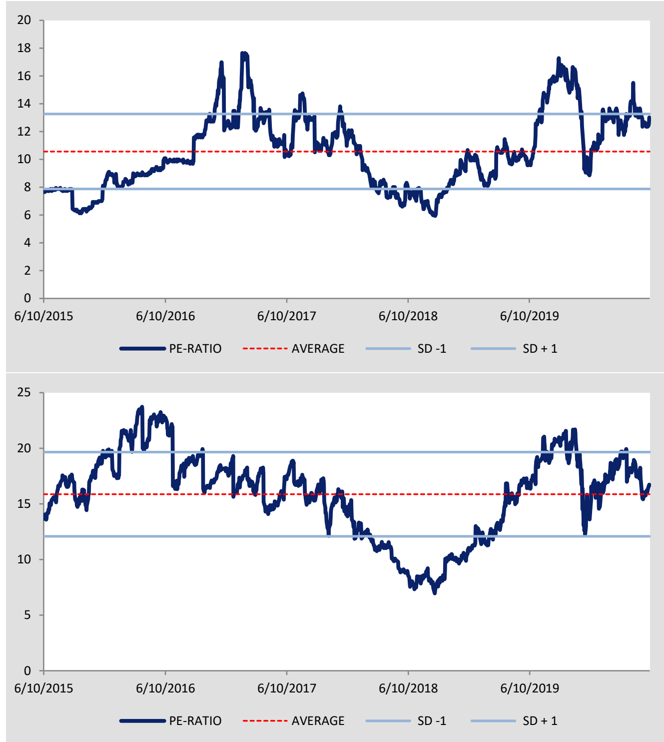
Figure 25: AMAT (White) and UMS (Yellow) market contraction prior to SMIC blacklisting news



Source: Bloomberg, KGI Research

We thus see the recent retracement in UMS's share price as an opportunity to accumulate. The SemiCap sector is expected to continue growing into 2021, and while there remains a possibility of losing the business opportunity of the entire Chinese market, we think the scope of damage to AMAT (and by proxy UMS) is likely to be much less than we initially expected, as 1) We do not expect US to extend restrictions to non-Chinese companies operating in China, such as Micron or Samsung, thus still enabling geographical sales to China, albeit to non-Chinese entities, 2) as an extension of the first point, we doubt US will have reasonable basis to extend the ban to non-US companies operating in China, given that the bans were formed from US-specific security concerns, and 3) should there be such an escalation, we think major semi players would relocate fabs, rather than wait an unknown number of years for China's design capabilities to catch up. Upgrade UMS to OUTPERFORM.

Figure 26: UMS (top) continues trading at +1 S.D. while AMAT (btm) retraces back to average P/E levels



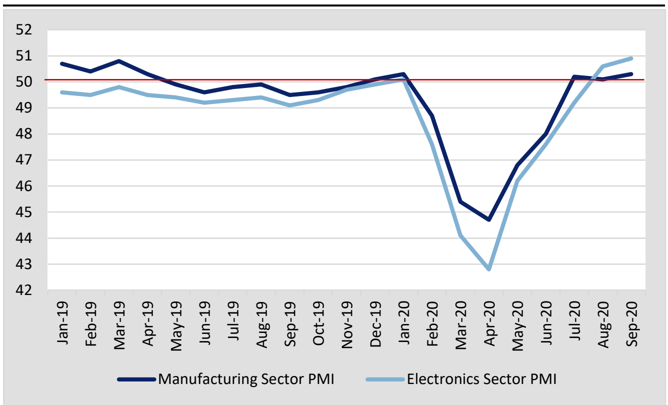
Source: Company data, KGI Research

Tech manufacturing

The electronics manufacturing sector saw a turn-around in August after 6 months of contraction. Prior to the 50.1 PMI reading (Singapore PMI Electronics Industry) on January 2020, the sector underwent a full 14 months of contraction, caused by a brewing US-China trade war and a slowdown of the Chinese economy. September's results were also recently released and indicated a continuation of sector expansion.

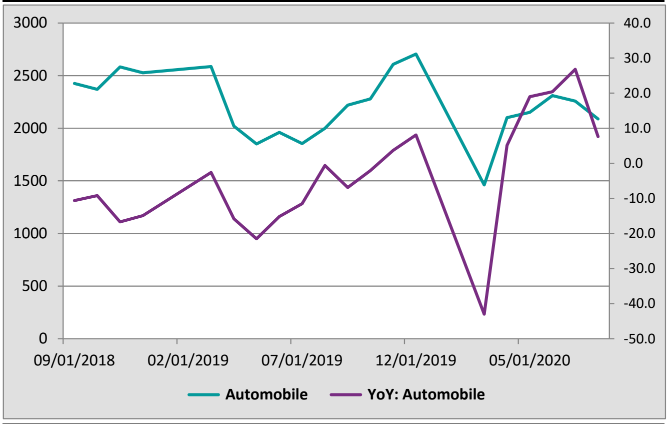
Amongst listed tech manufacturing plays, large caps generally performed worse than small caps – Venture and Hi-P having reported -25% YoY sales and weaker earnings performance. Venture has however had decent share price performance due to their key clients' outlook and prospects, while Hi-P's has been lacklustre due to potential pricing pressures and perceived weakness in clients' end-product demand. Small/mid caps such as Sunningdale Tech and Innotek largely recovered, while Valuetronics is still down 30+% year-to-date.

Figure 27: Electronics sector PMI continues expansion in September after substantial contraction during COVID-19 months



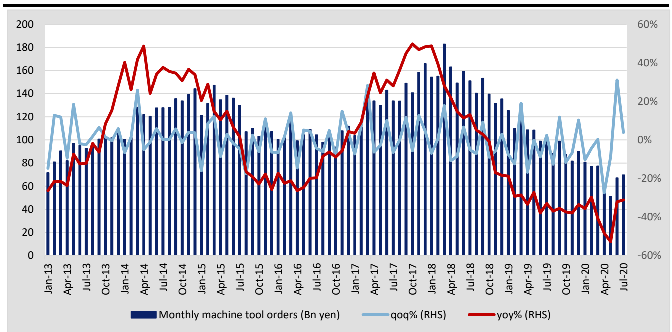
Source: SIPMM, KGI Research

Figure 28: Auto production in China back to growth since April. LHS = monthly automobile production, RHS = YoY% growth



Source: CEIC, KGI Research

Figure 29: 26-month tool orders contraction ended in May, inflection in June and growth continued in July



Source: JMTBA, KGI Research

ISDN Holdings (ISDN SP)

Maintain OUTPERFORM, TP S$0.47

As monthly macro data continues to illustrate a situation of recovery, we think ISDN remains a top pick amongst the group, as they have decent revenue visibility despite the unstable business environment. We favour the automation sector to rebound together with cyclicals, as industrial activity in China picks up again post-COVID.

In August, ISDN management have mentioned that July was the best performing month in the history of the company. Given that China's auto industry is recovering at a steady pace, we think ISDN's automotive business will also see a similar pick up in 2H20. Should ISDN be able to replicate 1H20's profitability margins, we expect further upside to our current TP of S$0.47.

SPECIAL MENTIONS

Alibaba (9988 HK)

Unrated

We have mentioned Alibaba as a software play in Part 2, and recent updates indicate that Alibaba continues to be a safe Big Tech pick.

Alibaba is the second largest cloud computing player in the Asia-Pacific region, behind Amazon, and the largest cloud computing company in China. Cloud revenue rose 58.5% YoY in 1Q FY21, compromising of 8% of Alibaba's total revenue.

Alibaba held their annual investor conference recently, and mentioned that the cloud unit will be turning profitable for the first time in the current Fiscal Year ending March 2021. Additionally, the logistics business, Cainiao Network, will generate positive operating cash flow in this period.

Despite competition from other e-commerce players, Alibaba's e-commerce business is likely to maintain 20% steady growth, providing recurrent income to the group. Together with other businesses that contribute positive profit, as well as the upcoming Ant Group IPO on 28th October, we expect Alibaba to outperform the tech sector. Our Hong Kong team associates a HKD 310 price target to Alibaba's share price.

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Neutral (N)	We take a neutral view on the stock. The stock is expected to perform in line with the expected total return of the KGI coverage universe in the related market over a 12-month investment horizon.
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