

Singapore Technology

POSITIVE

[Unchanged]

2Q21 earnings preview

UMS and Frencken might beat in 2Q21

Entering into the 2Q21 earnings season, we remain Positive on the Singapore tech sector. On the back of strong WFE spending momentum, we believe UMS and Frencken have room to beat on results. While we are cautious towards risks of earnings disappointment for AEM and VMS, we are positive on their prospects over the next 12 months and beyond, based on currently visible drivers. We continue to see supply-side risks as key ones that could curb earnings performance as we move throughout 2021.

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Strong WFE momentum boon for UMS and Frencken

SEMI now expects WFE spending to surge 34% YoY to USD81.7b in 2021, revised up from the low USD70b range in March. We believe the stronger than expected WFE momentum bodes well for UMS (customer: Applied Materials), and Frencken (customers: ASML and AMAT). Given robust demand momentum, we also see potential for Aztech to beat expectations in 2Q21. Detailed estimates, thesis and discussion of risks for our universe are in Fig 1.

Focus beyond 2Q21 for VMS and AEM

For VMS, we see risks that components shortages may not have been fully resolved in 2Q21, and if this pans out, could result in a seasonally softer 1H21 than in previous years. However, insofar as demand outlook remains strong and components shortages are gradually resolved, we continue to like VMS as a “late cycle” play. Meanwhile, we like AEM for its earnings recovery potential as it ramps up new generations of HDMT in late 3Q21 through 2022, as well as new customers’ contributions in 2022. Hence, while transitory weakness may result in softer than expected 2Q21 earnings, we do not fundamentally see this impacting our positive thesis.

Where we might be wrong

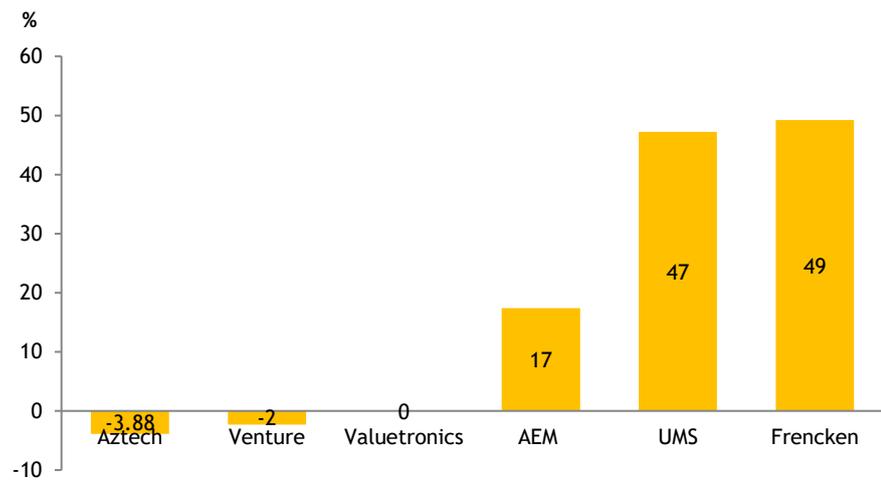
We believe key risks to our view largely surround supply-side problems, e.g. components shortages, logistical challenges, and or cumulative inefficiencies as a result of lockdowns in the geographies companies operate in. We think these are practical risks to consider in 2H21 as well, especially because barring material hindrances, we expect most of the companies that we cover to be seasonally stronger in 2H21.

Stock	Bloomberg code	Mkt cap (USD'm)	Rating	Price (LC)	TP (LC)	Upside (%)	P/E (x)		P/B (x)		Div yld (%)	
							21E	22E	21E	22E	21E	22E
Venture	VMS SP	4,029	Buy	18.81	22.00	21	15.8	13.8	2.0	1.9	4.0	4.0
AEM Holdings	AEM SP	824	Buy	3.98	5.56	42	14.3	9.9	4.1	3.2	1.7	2.5
Aztech Global	AZTECH SP	700	Buy	1.23	1.86	53	11.5	8.7	3.3	2.6	2.5	3.4
UMS Holdings	UMSH SP	612	Buy	1.55	1.80	19	13.0	11.6	2.8	2.4	2.6	2.6
Frencken Group	FRKN SP	592	Buy	1.89	2.00	8	13.7	11.9	2.1	1.9	2.2	2.5
Valuetronics	VALUE SP	187	Hold	0.59	0.60	6	8.1	10.1	1.1	1.0	5.7	3.9

Fig 1: Overview of SG Tech coverage ahead of 2Q21 reporting season

Company	2Q21E PATMI range	Basis for 2Q21 estimate/ Thesis/ Risks
AEM	SGD14-16m (-22% YoY at midpoint)	<p>Thesis: We believe investors should look past 1H21 transitory softness, and focus on structural growth drivers. AEM is a beneficiary of Intel's increasing focus on various packaging and testing technologies as mission-critical chips become more complex, leading to lengthening test times to ensure product reliability. Separately, AEM is now working with 10 out of top 20 semiconductor companies and expects to derive meaningful revenue from these in 2022.</p> <p>Basis: We expect 2Q21 to be sequentially stronger than 1Q21 (PATMI: SGD13.2m).</p> <p>Upside drivers: We believe stronger than expected cloud spending recovery, and/ or materially accretive M&As are upside drivers in 2H21 and beyond.</p> <p>Risks: As AEM has reiterated that new generation of HDMT equipment will undergo production ramp-up in late 3Q21 through 2022, we do not see demand as the key risk as we enter a new earnings cycle. Rather, we see any unforeseen supply side bottlenecks as the key risk. From a stock trading perspective, AEM has gained 20% since it bottomed out in mid-May. We do not rule out profit taking in the near term, especially if the market perceives 2Q21 results to be a non-event, or if 2Q21 results disappoint. We would recommend buying on dips if our thesis remains intact.</p>
Aztech Global	SGD18-20m (Period YoY not available)	<p>Thesis: We see Aztech as a proxy to IoT adoption, in turn propelled by growth via key customer A (c.60% of revenue), as well as contribution from new IoT customers. IoT is also early in its technology lifecycle.</p> <p>Basis: Estimating 1H:2H seasonality of around 40:60, and for 2Q21 profit to be sequentially stronger than 1Q21.</p> <p>Upside drivers: Stronger than expected demand of smart security cams and other IoT products, especially in 2H21 - contingent on no/minimal supply side bottlenecks.</p> <p>Risks: Components shortages later in the year. Material delays in introducing new production capacity outside China in 1H22 due to the current Covid-19 situation in Malaysia.</p>
Frencken	SGD15-17m (+73% YoY at midpoint)	<p>Thesis: We like Frencken from both a cyclical and structural perspective. Frencken is usually the sole source for critical but non-core products in Mechatronics (80% of revenue), boosting stickiness. We expect margins to expand as management continue to execute on improved mix and cost control. Cyclically, c.70% of revenues (semiconductor/ analytical/ automotive) are in varying degrees of recovery/ upswing.</p> <p>Basis: Our estimates assume that 2Q21 should be slightly seasonally stronger than 1Q21, as this is usually the case with the end-markets Frencken is exposed to.</p> <p>Upside drivers: We believe that the stronger than expected semicon equipment cycle may provide upside in 2021. In FY22 and beyond, we believe upside may stem from i) resilience of semi revenues, ii) easing of auto components shortages, iii) growth from industrial automation, and iv) our underestimation of strength from new product launches in other verticals.</p> <p>Risks: In the semi equipment subsegment (c.30% of revenue), Frencken is a beneficiary of chip shortages. Thus far, shortages in auto supply chains have not derailed Frencken's growth trajectory in 2021. We believe the key risk is if components shortages worsen to the point where Frencken's overall growth is curbed across the rest of its end-markets, therefore eclipsing the potential from semicon.</p>
UMS	SGD16-18m (+47% YoY at midpoint)	<p>Thesis: Beneficiary of global semiconductor capex spending growth through key customer Applied Materials. In turn, semi equipment spending is powered by structural technology inflections like 5G/AI, accelerated digitisation, and chip shortages.</p> <p>Basis: We are expecting 2Q21 to be sequentially stronger than 1Q21 PATMI of SGD15.4m as the WFE upcycle gains momentum.</p> <p>Upside drivers: potential share gains as suppliers struggle to meet demand from the current momentum of the cycle and/or from suppliers that are switching over to Lam Research (which is building out supply chain in Penang). If UMS can win a new customer, this would be longer-term positive.</p> <p>Risks: As current demand momentum is robust, we believe key risks would be supply-side bottlenecks. While we believe effects of tightened restrictions may have had an immaterial impact to UMS in 1H21, we cannot rule out such risks from surfacing in 2H21.</p>
Venture	SGD70-73m (+2% YoY at the midpoint)	<p>Thesis: We see VMS as a "late cycle" play, as while demand for products are robust, risks of components shortages may cap growth in 2021. VMS expects breadth of products from its R&D labs to enter manufacturing in 2021. Customers, especially in life-science, medical technology and networking are also optimistic about end-markets and new products.</p> <p>Basis and risks: We are assuming 1H21:2H21 seasonality of 40:60 than the traditional seasonality of 45:55, but expect 2Q21 to be seasonally stronger than 1Q21 (PATMI: SGD65.3m). We see risks that because of components shortages and potential build-up of inefficiencies from worker capacity restrictions in Malaysia may have prevented VMS to entirely fulfill delivery requirements in 1H21.</p> <p>Upside drivers: We seek to get a better understanding of VMS' ability and the state of components availability during 2Q21 briefing. If these are largely resolved, we believe stronger than expected business momentum across a breadth of customers may be the key upside driver as we progress through the cycle, as VMS' earnings upgrade cycles have typically been enabled by i) broad-based new launches, and ii) strong end-markets.</p>

Source: Maybank Kim Eng

Fig 2: YTD performance of Singapore tech coverage

Source: FactSet

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