

AEM Holdings (AEM SP)

2H24 hopes diminish

Still too early - Downgrade to HOLD

AEM 1Q24 revenue dropped 38.3% YoY to SGD94.2m while NPAT fell 85% YoY to SGD2.3m, below consensus estimates but in line with ours'. We were too optimistic of a much stronger 2H24E based on potential order recovery from its key customer as well as ramp up of recently unveiled new orders. However, management updated that the new orders will only start mass production at end-FY24 and the main surge will only come in FY25E. It also only expects an uptick in growth in 2025. Despite thinking the worst is over for AEM, we now believe earnings recovery is only likely in FY25E and it would be better to revisit it towards 4Q24. We lower our FY24E-25E PATMI estimates by 31.8% and 21.6%, respectively, to reflect the new reality and downgrade to HOLD with a new TP of SGD2.04, pegged to 11x FY24/25E blended PE.

Main recovery only likely in FY25E

AEM revenue fell 38.3% YoY to SGD94.2m, mainly due to drops in equipment sales of -69% YoY to SGD9.7m and services of -38% YoY to SGD94.2m, as a key customer already made large purchases in FY21-23. While we expected a weak 1H24, the muted outlook for 2H24E despite recent new order wins was way below our expectation for a much stronger 2H24E. As a result, we think that FY24E will likely remain weak and the main rebound will only come in FY25E.

Expect more orders from new customers

Management guided that it expects more orders from its other new customer in the next few months, similar to the ones announced in the past few weeks as it seeks to diversify its key customer base. Management expects program wins from this new customer to drive more than 5x revenue growth to triple-digit millions in FY25E.

Not time yet

Despite thinking the worst is over, and expecting more new order wins in the next few months, we think it's better to revisit AEM closer to 4Q24 as the bulk of the ramp-up orders will only likely come in FY25E. As a result, we downgrade AEM to HOLD from BUY.

FYE Dec (SGD m)	FY22A	FY23A	FY24E	FY25E	FY26E
Revenue	870	481	409	614	798
EBITDA	168	20	50	102	127
Core net profit	127	(1)	21	58	76
Core FDEPS (cts)	40.7	(0.4)	6.8	18.7	24.5
Core FDEPS growth(%)	37.9	nm	nm	176.1	31.1
Net DPS (cts)	10.2	0.0	1.7	4.7	6.2
Core FD P/E (x)	8.4	nm	34.2	12.4	9.5
P/BV (x)	2.2	2.3	1.5	1.4	1.2
Net dividend yield (%)	3.0	0.0	0.7	2.0	2.7
ROAE (%)	28.6	(0.2)	4.4	11.5	13.8
ROAA (%)	16.7	(0.2)	2.8	6.9	8.1
EV/EBITDA (x)	6.4	54.2	13.8	7.2	4.7
Net gearing (%) (incl perps)	3.1	5.2	net cash	0.7	net cash
Consensus net profit	-	-	40	79	95
MIBG vs. Consensus (%)	-	-	(47.1)	(25.8)	(19.3)

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HOLD

[Prior:BUY]

Share Price SGD 2.32
12m Price Target SGD 2.04 (-10%)
Previous Price Target SGD 2.78

Company Description

AEM manufactures equipment used in the semiconductor back-end process

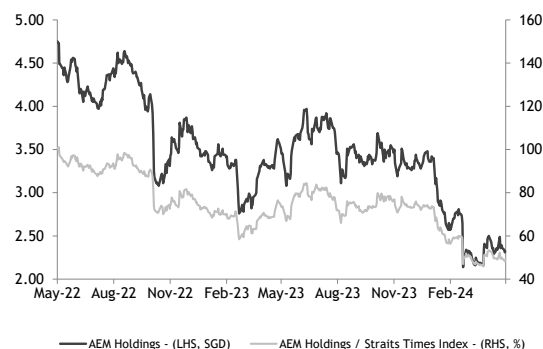
Statistics

52w high/low (SGD) 3.97/2.14
3m avg turnover (USDm) 3.8
Free float (%) 77.9
Issued shares (m) 312
Market capitalisation SGD723.6M
USD534M

Major shareholders:

Temasek Holdings Pte Ltd. (Investment Ma 12.4%
Employees Provident Fund 11.0%
Abrdn Asia Ltd. 9.8%

Price Performance



	-1M	-3M	-12M
Absolute (%)	(2)	(10)	(34)
Relative to index (%)	(4)	(14)	(35)

Source: FactSet

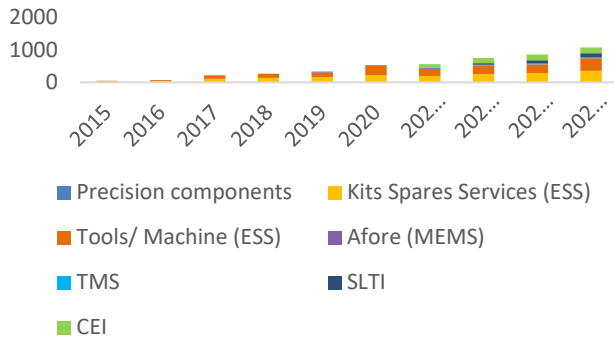
ESG@MAYBANK IBG

Tear Sheet Insert

Value Proposition

- Back-end test-equipment manufacturer that has co-developed the HDMT handler for Intel.
- 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 risk.

Share of new revenue sources progressively growing



Note: FY21E split is our estimation.
Source: Company, Maybank IBG Research

Price Drivers

Historical share price trend



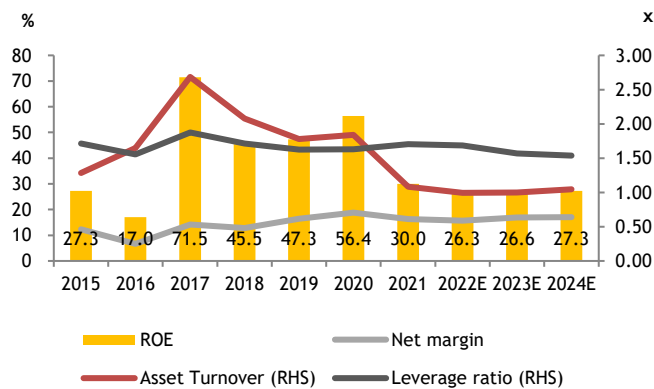
Source: Company, Maybank IBG Research

1. Novo Tellus distributes AEM shares in-specie to investors; Core customer announces 10nm delay.
2. AEM's core customer denies rumours from tech-blog SemiAccurate that its 10nm process was cancelled.
3. Through 2020, AEM announced several positive guidance revisions, catalysing rallies
4. Announced FY21 revenue guidance of SGD460-520m, which the market perceived as a disappointment.
5. Announced placement to Temasek.

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 pay-out ratio policy in 2017.

DuPont ROE



Source: Company, Maybank IBG Research

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 competitive advantages of core customer as a result of company specific or industry related developments.

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Risk Rating & Score ¹	23.1 (Medium)
Score Momentum ²	na
Last Updated	11 November 2020
Controversy Score ³	0 - No Reported Incident

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 2021.
- 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.
- Emissions intensity ratio rose to 0.0014318MT/SGD’000 in 2021 (FY19: 0.007588), due to the consolidation of CEI.
- AEM screens suppliers for negative environmental and social impacts, including pollution, biodiversity loss, global warming, incidences of child labour, breaches of customer privacy, and more. All suppliers were found to have no negative environmental or social impacts.

Material S issues

- AEM adheres to minimum wage laws of the countries it operates in. There is no difference in pay between male and female employees at the entry-level across all countries with minimum wage laws.
- Workforce diversity. AEM is an equal-opportunities employer. Management are hired from local communities and consists of various nationalities. >90% 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 2021, average training per employee was 18.4 hours, to equip staff with skills across technical, project management and software domains (FY20: 7.8 hours).
- Females comprise 34% of the total work force in FY21, higher than 24% in FY20, due to the inclusion of CEI.
- Turnover rate rose to 23% vs. 10% in FY20.

Key G metrics and issues

- The board has seven directors, of which one is the executive chairman, four are independent directors (57%), and three are non-independent, non-executive.
- 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.
- Key management compensation (comprising the Board and senior management) accounted for 7.1% of staff costs in 2021 (2020: 13.6%).
- 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 2021. There was one case of whistleblowing in 2020, but upon investigation, it was concluded to be unsubstantiated.
- 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.

¹**Risk Rating & Score** - derived by Sustainalytics and assesses the company’s exposure to unmanaged ESG risks. Scores range between 0 - 50 in order of increasing severity with low/high scores & ratings representing negligible/significant risk to the company’s enterprise value, respectively, from ESG-driven financial impacts. ²**Score Momentum** - indicates changes to the company’s score since the last update - a **negative** integer indicates a company’s improving risk score; a **positive** integer indicates a deterioration. ³**Controversy Score** - reported periodically by Sustainalytics in the event of material ESG-related incident(s), with the impact severity scores of these events ranging from Category 0-5 (0 - no reports; 1 - negligible risks; ...; 5 - poses serious risks & indicative of potential structural deficiencies at the company).

Quantitative Parameters (Score: 44)						
	Particulars	Unit	2019	2020	2021	UMSH SP (2021)
E	Scope 1 GHG emissions	tCO2e	NA	NA	15	NA
	Scope 2 GHG emissions	tCO2e	3344	3938	8082	NA
	Total	tCO2e	3344	3938	8097	NA
	Scope 3 GHG emissions	tCO2e	NA	NA	NA	NA
	Total	tCO2e	3344	3938	8097	NA
	GHG intensity (Scope 1 and 2)	KgCO2e/emp	0.010	0.008	0.014	NA
	Energy consumption	kWh/unit of sales	0.02	0.01	0.02	0.13
	Water consumption	M2/unit of sales	0.04	0.03	0.09	0.0011
	Recycled waste generated	Metric tonnes	NA	NA	50	50
S	% of women in workforce	%	21	22	35	NA
	Economic value generated and distributed	SGD'000	54778	86207	89181	53100
	Proportion of training hours by gender (women)	%	20	20	48	NA
	New employees hired by gender (women)	%	23	24	34	NA
	Direct training hours	%	22	31	71	NA
	Key operations assessed for risks related to corruption	%	100	100	100	100
G	MD/CEO salary as % of reported net profit	%	3.87	3.23	1.34	0.04
	Board salary as % of reported net profit	%	1.09	0.60	1.06	0.05
	Independent directors on the Board	%	67	57	57	60
	Female directors on the Board	%	0	0	14	20

Qualitative Parameters (Score: 50)	
a)	is there an ESG policy in place and whether there is a standalone ESG committee or is it part of a risk committee? <i>Yes, the group has established a Sustainability Steering Committee comprising a senior management team to support the board, which determines the overall direction of sustainability strategies. It is aided by the audit and risk management committee which evaluates and incorporates sustainability issues as part of the group's strategic formulation. It also approves, manages and monitors ESG factors material to the business.</i>
b)	Is the senior management salary linked to fulfilling ESG targets? <i>No</i>
c)	Does the company follow the task force of climate related disclosures (TCFD) framework for ESG reporting? <i>Yes</i>
d)	Does the company have a mechanism to capture Scope 3 emissions - which parameters are captured? <i>No</i>
e)	What are the 2-3 key carbon mitigation/water/waste management strategies adopted by the company? <i>The Group is replacing its air-conditioning ducting from cassette to inverter type and has programmed its air-conditioners and lights to switch off automatically after office hours. It has also engaged a third-party recycler to recycle waste generated from manufacturing and operations.</i>
f)	Does carbon offset form part of the net zero/carbon neutrality target of the company? <i>No</i>

Target (Score: 66.7)			
Particulars		Target	Achieved
Maintain economic value generation of at least 5%		5%	3%
Low turnover rate		2%	0.9%
Maintain 100% of employees receiving regular performance reviews		100	100
Carbon neutrality/net zero		NA	NA
Impact			
NA			
Overall Score: 51			
As per our ESG matrix, AEM (AEM SP) has an overall score of 51.			

ESG score	Weights	Scores	Final Score
Quantitative	50%	44	22
Qualitative	25%	50	13
Target	25%	67	17
Total			51

As per our ESG assessment, AEM has an established framework, internal policies, and tangible mid/long-term targets but needs to make headway in improving its quantitative "E" metrics. AEM's overall ESG score is 51, which makes its ESG rating above average in our view (average ESG rating = 50; refer to Appendix I for our ESG Assessment Scoring).

Fig 1: Changes in our forecasts

	FY24E			FY25E			FY26E		
	New	Old	Chg (%)	New	Old	Chg (%)	New	Old	Chg (%)
Revenue (SGDm)	409.1	505.3	-19.0	613.6	657.0	-6.6	797.7	854.0	-6.6
Gross profit (SGDm)	81.8	126.3	-35.2	153.4	177.4	-13.5	199.4	230.6	-13.5
EBIT (SGDm)	30.6	62.6	-51.1	75.6	94.0	-19.5	97.7	121.6	-19.6
EBITDA (SGDm)	50.2	82.2	-38.9	101.9	120.2	-15.3	126.7	150.6	-15.8
Core net profit (SGDm)	21.1	47.7	-55.7	58.3	73.5	-20.7	76.4	96.2	-20.6
EPS (SGD)	0.07	0.10	-31.8	0.19	0.24	-21.6	0.25	0.34	-27.4
			Chg (ppt)			Chg (ppt)			Chg (ppt)
EBIT margin	7.5%	18.5%	-11.0	12.3%	14.3%	-2.0	12.3%	14.2%	-2.0
Net margin	5.2%	15.3%	-10.1	9.5%	11.2%	-1.7	9.6%	11.3%	-1.7

Source: Maybank IBG Research

FYE 31 Dec	FY22A	FY23A	FY24E	FY25E	FY26E
Key Metrics					
P/E (reported) (x)	10.3	nm	34.0	12.3	9.4
Core P/E (x)	8.4	nm	34.0	12.3	9.4
Core FD P/E (x)	8.4	nm	34.2	12.4	9.5
P/BV (x)	2.2	2.3	1.5	1.4	1.2
P/NTA (x)	2.2	2.3	1.5	1.4	1.2
Net dividend yield (%)	3.0	0.0	0.7	2.0	2.7
FCF yield (%)	nm	3.9	8.7	nm	21.0
EV/EBITDA (x)	6.4	54.2	13.8	7.2	4.7
EV/EBIT (x)	6.8	80.2	22.6	9.6	6.1

INCOME STATEMENT (SGD m)

Revenue	870.5	481.3	409.1	613.6	797.7
EBITDA	168.0	20.3	50.2	101.9	126.7
Depreciation	(7.8)	(6.6)	(19.5)	(26.2)	(29.0)
Amortisation	0.0	0.0	0.0	0.0	0.0
EBIT	160.3	13.8	30.6	75.6	97.7
Net interest income / (exp)	(1.3)	(5.5)	(6.2)	(6.4)	(6.6)
Associates & JV	(0.3)	(0.6)	1.0	1.0	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	158.7	7.6	25.4	70.2	92.1
Income tax	(31.4)	(8.8)	(4.3)	(11.9)	(15.7)
Minorities	(0.5)	0.0	0.0	0.0	0.0
Discontinued operations	0.0	0.0	0.0	0.0	0.0
Reported net profit	126.8	(1.2)	21.1	58.3	76.4
Core net profit	126.8	(1.2)	21.1	58.3	76.4

BALANCE SHEET (SGD m)

Cash & Short Term Investments	127.8	101.8	177.9	142.8	275.6
Accounts receivable	92.9	60.1	63.2	121.8	118.7
Inventory	367.7	328.6	345.0	362.3	380.4
Property, Plant & Equip (net)	41.9	40.3	54.9	73.4	62.8
Intangible assets	150.9	158.7	158.7	158.7	158.7
Investment in Associates & JVs	15.2	8.8	9.8	10.8	11.8
Other assets	9.3	10.5	10.5	10.5	10.5
Total assets	805.6	708.9	820.1	880.2	1,018.4
ST interest bearing debt	13.7	83.9	83.9	83.9	83.9
Accounts payable	118.9	74.8	151.2	166.6	246.5
LT interest bearing debt	129.7	42.5	61.5	62.5	63.5
Other liabilities	50.0	33.0	33.0	33.0	33.0
Total Liabilities	312.1	234.5	329.9	346.3	427.2
Shareholders Equity	485.0	467.5	483.3	527.0	584.3
Minority Interest	8.4	6.9	6.9	6.9	6.9
Total shareholder equity	493.5	474.4	490.2	533.9	591.3
Total liabilities and equity	805.6	708.9	820.1	880.2	1,018.4

CASH FLOW (SGD m)

Pretax profit	158.7	7.6	25.4	70.2	92.1
Depreciation & amortisation	7.8	6.6	19.5	26.2	29.0
Adj net interest (income)/exp	0.0	0.0	0.0	0.0	0.0
Change in working capital	(145.9)	63.6	56.9	(60.4)	64.9
Cash taxes paid	(21.6)	(28.9)	(4.3)	(11.9)	(15.7)
Other operating cash flow	0.0	0.0	0.0	0.0	0.0
Cash flow from operations	(0.7)	49.6	96.5	23.1	169.3
Capex	(25.1)	(7.3)	(34.2)	(44.7)	(18.4)
Free cash flow	(25.9)	42.3	62.3	(21.5)	150.9
Dividends paid	(36.2)	11.1	(5.3)	(14.6)	(19.1)
Equity raised / (purchased)	0.0	0.0	0.0	0.0	0.0
Change in Debt	24.5	(26.0)	19.0	1.0	1.0
Other invest/financing cash flow	(20.2)	(45.5)	0.0	0.0	0.0
Effect of exch rate changes	0.7	0.9	0.0	0.0	0.0
Net cash flow	(57.0)	(17.2)	76.1	(35.1)	132.8

FYE 31 Dec	FY22A	FY23A	FY24E	FY25E	FY26E
Key Ratios					
Growth ratios (%)					
Revenue growth	53.9	(44.7)	(15.0)	50.0	30.0
EBITDA growth	33.0	(87.9)	146.7	103.0	24.4
EBIT growth	43.3	(91.4)	122.8	146.9	29.2
Pretax growth	42.8	(95.2)	235.3	176.1	31.1
Reported net profit growth	37.9	nm	nm	176.1	31.1
Core net profit growth	37.9	nm	nm	176.1	31.1
Profitability ratios (%)					
EBITDA margin	19.3	4.2	12.3	16.6	15.9
EBIT margin	18.4	2.9	7.5	12.3	12.3
Pretax profit margin	18.2	1.6	6.2	11.4	11.5
Payout ratio	25.0	0.0	25.0	25.0	25.0
DuPont analysis					
Net profit margin (%)	14.6	nm	5.2	9.5	9.6
Revenue/Assets (x)	1.1	0.7	0.5	0.7	0.8
Assets/Equity (x)	1.7	1.5	1.7	1.7	1.7
ROAE (%)	28.6	(0.2)	4.4	11.5	13.8
ROAA (%)	16.7	(0.2)	2.8	6.9	8.1
Liquidity & Efficiency					
Cash conversion cycle	127.9	314.3	300.5	206.6	153.4
Days receivable outstanding	45.7	57.2	54.2	54.2	54.2
Days inventory outstanding	172.7	356.1	370.5	276.7	223.4
Days payables outstanding	90.5	99.1	124.3	124.3	124.3
Dividend cover (x)	4.0	nm	4.0	4.0	4.0
Current ratio (x)	3.5	2.8	2.3	2.3	2.2
Leverage & Expense Analysis					
Asset/Liability (x)	2.6	3.0	2.5	2.5	2.4
Net gearing (%) (incl perps)	3.1	5.2	net cash	0.7	net cash
Net gearing (%) (excl. perps)	3.1	5.2	net cash	0.7	net cash
Net interest cover (x)	122.2	2.5	4.9	11.8	14.7
Debt/EBITDA (x)	0.9	6.2	2.9	1.4	1.2
Capex/revenue (%)	2.9	1.5	8.4	7.3	2.3
Net debt/ (net cash)	15.5	24.5	(32.5)	3.6	(128.2)

Source: Company; Maybank IBG Research

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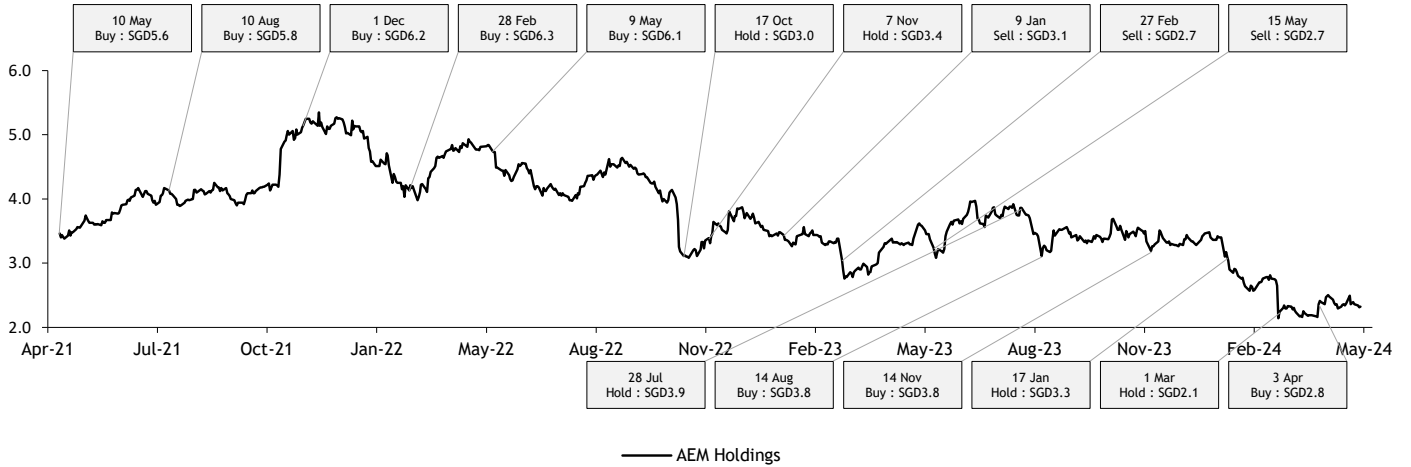
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