




Malaysia

HOLD (previously REDUCE)

Consensus ratings*: Buy 1 Hold 1 Sell 1

Current price: RM7.25
Target price:  RM7.80
Previous target: RM6.10
Up/downside: 7.6%
CGS-CIMB / Consensus: -10.3%

Reuters: KESM.KL
Bloomberg: KESM MK
Market cap: US\$74.41m
RM311.9m
Average daily turnover: US\$0.06m
RM0.24m
Current shares o/s: 43.68m
Free float: 51.6%

*Source: Bloomberg

Key changes in this note

- FY20F EPS decreased by 1.7%.
- FY21F EPS decreased by 2.4%.



Source: Bloomberg

Price performance	1M	3M	12M
Absolute (%)	3	3.1	-57.9
Relative (%)	3	7.3	-46.5

Major shareholders	% held
Sunright Limited	48.4

Analyst(s)



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KESM Industries

Back on a growth path in FY20F

- FY7/19 core net profit came in 18% above our estimates due to lower-than-expected depreciation, but was 9% below Bloomberg consensus estimates.
- Core EPS plunged 82% yoy in FY19 due to lower test and burn-in demand, and weakness in automotive market attributable to escalating trade tensions.
- But, we upgrade KESM to Hold with a higher RM7.80 TP in view of potential demand pick-up from newer products and inventory replenishment in FY20F.

Back in the black in 4QFY7/19

KESM's headline net profit grew from RM870k in 3QFY19 to RM2.3m in 4QFY19, mainly due to a decline in depreciation to RM16.9m vs. RM19m in 3QFY19. Stripping out the exceptional items such as the RM1.6m litigation settlement and RM516k gain from assets disposal, KESM returned to a core net profit in 4QFY19, at RM3.4m, against a core net loss of RM783k in 3QFY19. KESM declared 6 sen DPS for the quarter, bringing total dividend for FY19 to 9 sen, ahead of our expectation of 4 sen.

FY7/19 core net profit tumbled 82% yoy

FY19 revenue fell 12.1% yoy to RM307m due to lower demand for its burn-in and testing services; we estimate their utilisation fell below 50% in FY19 due to ongoing inventory adjustment by its customers amid escalating US-China trade tensions. Meanwhile, it also incurred higher raw material costs to support the growth of its electronics manufacturing services (EMS) segment. Raw material and consumable costs rose 30% yoy in FY19 to RM41.5m. Overall, FY19 core net profit plunged 82% yoy from RM39m to RM7m.

Optimistic for robust recovery in FY20F

We expect higher test and burn-in utilisation in FY20F driven by gradual industry demand recovery and inventory replenishment following tight inventory control in the past 12 months. KESM should benefit from better cost control as it expects the lower depreciation trend to continue in FY20F and will focus on staff training and development in automation to drive productivity. It is allocating RM40m capex for FY20F (FY19: RM26m).

Upgrade from Reduce to Hold with a higher RM7.80 TP

The stock has fallen 26% from its YTD high in Mar and by 65% since 2018 due to its poor earnings delivery and negative sentiment on the semiconductor industry amid escalating US-China trade tensions. In spite of the challenging operating environment in the past 24 months, KESM remains profitable. We think KESM is poised for an earnings recovery in FY20F, driven by improvement in utilisation and better cost control. The stock trades at 1x CY20F P/BV, supported by healthy net cash of RM143m or RM3.32/share.

Key upside and downside risks

We see a faster-than-expected demand recovery in the automotive segment and higher-than-expected dividend payout as potential upside risks to our call. Meanwhile, prolonged demand weakness due to the trade conflict is a key downside risk to our call.

Financial Summary	Jul-18A	Jul-19A	Jul-20F	Jul-21F	Jul-22F
Revenue (RMm)	349.8	307.4	329.1	345.5	361.5
Net Profit (RMm)	39.01	6.99	17.16	24.35	28.72
Core EPS (RM)	0.89	0.16	0.39	0.56	0.66
Core EPS Growth	(11%)	(82%)	146%	42%	18%
FD Core P/E (x)	8.12	45.30	18.45	13.01	11.03
Price To Sales (x)	0.91	1.03	0.96	0.92	0.88
DPS (RM)	0.19	0.09	0.12	0.17	0.20
Dividend Yield	2.55%	1.24%	1.66%	2.34%	2.76%
EV/EBITDA (x)	1.86	2.09	1.42	0.98	0.58
P/FCFE (x)	527.8	32.7	7.3	8.0	7.4
Net Gearing	(25.0%)	(39.7%)	(49.5%)	(56.6%)	(63.0%)
P/BV (x)	0.89	0.88	0.85	0.82	0.78
ROE	11.4%	2.0%	4.7%	6.4%	7.2%
% Change In Core EPS Estimates			(1.65%)	(2.44%)	
CGS-CIMB/Consensus EPS (x)			0.89	0.86	

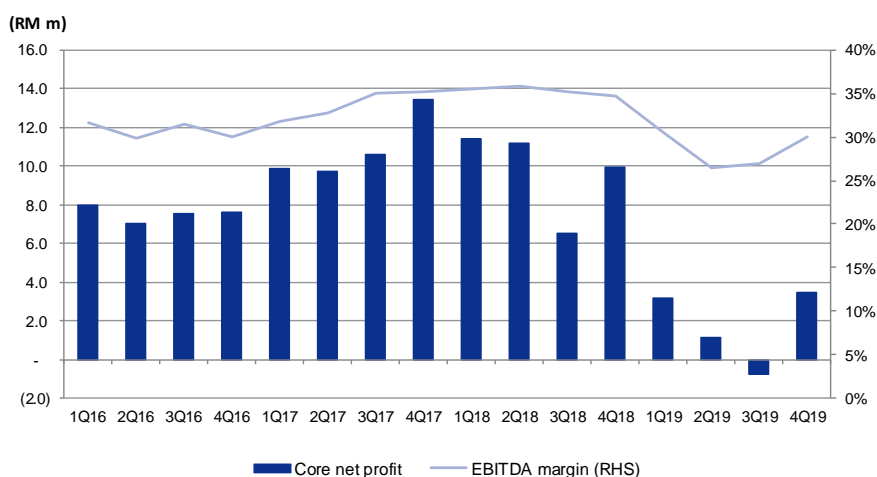
SOURCES: CGS-CIMB RESEARCH, COMPANY REPORTS

Figure 1: Results comparison

FYE July (RM m)	4QFY19	4QFY18	yoy % chg	3QFY19	qoq % chg	4QFY19	4QFY18	yoy % chg	Prev. FY19F	Comments
Revenue	70.9	85.3	(16.8)	73.8	(3.9)	307.4	349.8	(12.1)	308.9	Lower demand for burn-in and testing services
Operating costs	(51.2)	(56.9)	(10.0)	(55.2)	(7.3)	(222.8)	(228.4)	(2.5)	(222.2)	
EBITDA	19.7	28.3	(30.5)	18.6	6.0	84.6	121.4	(30.3)	86.7	In line
EBITDA margin (%)	27.8	33.2		25.2		27.5	34.7		28.1	
Depn & amort.	(16.9)	(19.8)	(14.7)	(19.0)	(11.0)	(74.9)	(78.4)	(4.4)	(76.9)	
EBIT	2.8	8.5	(67.3)	(0.4)	> 100	9.7	43.0	(77.5)	9.8	
Interest expense	(0.8)	(1.3)	(34.8)	(1.0)	(19.3)	(4.1)	(4.1)	(0.2)	(4.4)	Net cash of RM143m as at end July 2019
Interest & invt inc	1.6	1.3	24.8	1.4	20.3	4.6	4.4	4.0	4.5	Cash balances of RM200m as at end July 2019
Exceptionals	(1.1)	1.4	> 100	1.7	> 100	(0.7)	0.3	> 100	-	Gain on asset disposal and litigation fee
Pretax profit	2.5	10.0	(75.2)	1.6	55.2	9.5	43.7	(78.2)	9.8	In line
Tax	(0.2)	1.3	> 100	(0.7)	(74.7)	(3.2)	(4.3)	(25.7)	(3.9)	Below expectation
Tax rate (%)	7.4	-13.4		45.4		34.0	10.0		40.0	
Net profit	2.3	11.3	(79.8)	0.9	> 100	6.3	39.3	(84.0)	5.9	
Core net profit	3.4	9.9	(65.4)	(0.8)	> 100	7.0	39.0	(82.1)	5.9	Above expectation
EPS (sen)	5.3	26.3	(79.8)	2.0	> 100	14.6	91.5	(84.0)	13.7	FY7/19 core net profit came in 18% above our estimated,
Core EPS (sen)	8.0	23.1	(65.4)	(1.8)	> 100	16.3	90.7	(82.1)	13.7	but 9% below Bloomberg consensus forecast
Net DPS (sen)	6.0	6.0	-	-	n.m.	9.0	18.5	(51.4)	3.5	

SOURCE: CIMB, COMPANY

Figure 2: Quarterly core net profit and EBITDA margin trend



SOURCE: CIMB, COMPANY

Figure 3: Earnings revision

(RM m)	Previous			Revised			Changes (%)		
	FY20F	FY21F	FY22F	FY20F	FY21F	FY22F	FY20F	FY21F	FY22F
Revenue	329.1	348.3	na	329.1	345.5	361.5	-	(0.8)	na
EBIT	22.8	31.0	na	20.9	28.2	32.9	(8.3)	(9.2)	na
PBT	21.3	29.7	na	20.9	28.6	33.8	(1.7)	(3.6)	na
Net profit	17.4	25.0	na	17.2	24.3	28.7	(1.7)	(2.4)	na
EPS (sen)	40.6	58.0	na	39.9	56.6	66.8	(1.7)	(2.4)	na

SOURCE: CIMB, COMPANY

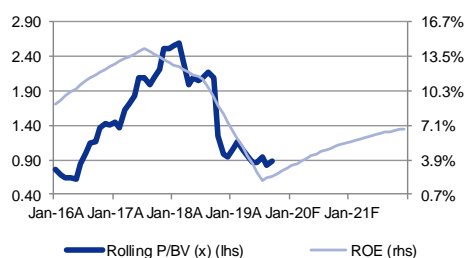
Figure 4: Sector comparison

Company	Recom.	Price (local currency)	Target Price (local currency)	Mkt Cap (US\$ m)	P/E (x)		P/BV (x)		Recurring ROE (%)		EV/EBITDA (x)		Dividend Yield (%)	
					CY19F	CY20F	CY19F	CY20F	CY19F	CY20F	CY19F	CY20F	CY19F	CY20F
KESM Industries	Hold	7.25	7.80	74	28.2	15.7	0.9	0.8	3.1	5.5	1.8	1.2	1.4	1.9
Inari-Amertron Bhd	Hold	1.76	1.52	1,335	25.1	20.3	4.7	4.6	19.2	23.0	14.7	12.7	3.4	4.2
MPI	Add	9.10	11.20	432	13.2	11.7	1.5	1.4	11.4	12.1	3.7	3.3	3.3	3.8
Unisem	Reduce	2.06	1.80	357	24.7	16.4	1.0	1.0	4.3	6.3	4.7	3.8	3.4	4.9
Sector average					21.1	16.8	2.1	2.1	10.3	12.5	7.3	6.4	3.3	4.2

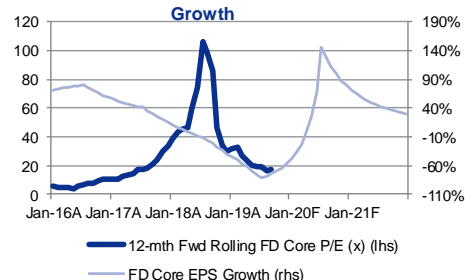
SOURCES: CGS-CIMB RESEARCH, COMPANY REPORTS

BY THE NUMBERS

P/BV vs ROE



12-mth Fwd FD Core P/E vs FD Core EPS Growth



Profit & Loss

(RMm)	Jul-18A	Jul-19A	Jul-20F	Jul-21F	Jul-22F
Total Net Revenues	352.9	310.0	331.7	348.1	364.1
Gross Profit	122.1	83.3	93.6	99.5	103.0
Operating EBITDA	122.1	83.3	93.6	99.5	103.0
Depreciation And Amortisation	(78.4)	(74.9)	(72.6)	(71.3)	(70.2)
Operating EBIT	43.7	8.4	20.9	28.2	32.9
Financial Income/(Expense)	(0.4)	1.8	0.0	0.5	0.9
Pretax Income/(Loss) from Assoc.	0.0	0.0	0.0	0.0	0.0
Non-Operating Income/(Expense)	0.0	0.0	0.0	0.0	0.0
Profit Before Tax (pre-EI)	43.4	10.2	20.9	28.6	33.8
Exceptional Items					
Pre-tax Profit	43.4	10.2	20.9	28.6	33.8
Taxation	(4.3)	(3.2)	(3.8)	(4.3)	(5.1)
Exceptional Income - post-tax					
Profit After Tax	39.0	7.0	17.2	24.3	28.7
Minority Interests	0.0	0.0	0.0	0.0	0.0
Preferred Dividends					
FX Gain/(Loss) - post tax					
Other Adjustments - post-tax					
Net Profit	39.0	7.0	17.2	24.3	28.7
Recurring Net Profit	39.0	7.0	17.2	24.3	28.7
Fully Diluted Recurring Net Profit	39.0	7.0	17.2	24.3	28.7

Cash Flow

(RMm)	Jul-18A	Jul-19A	Jul-20F	Jul-21F	Jul-22F
EBITDA	122.1	83.3	93.6	99.5	103.0
Cash Flow from Inv. & Assoc.					
Change In Working Capital	(37.9)	1.1	(3.4)	(2.6)	(2.5)
(Incr)/Decr in Total Provisions					
Other Non-Cash (Income)/Expense					
Other Operating Cashflow	(1.6)	6.1	0.0	0.0	0.0
Net Interest (Paid)/Received	(4.1)	(4.1)	(2.9)	(2.9)	(2.9)
Tax Paid	(4.6)	(3.5)	(3.8)	(4.3)	(5.1)
Cashflow From Operations	73.9	82.9	83.5	89.7	92.6
Capex	(41.5)	(25.8)	(40.0)	(50.0)	(50.0)
Disposals Of FAs/subsidiaries	(0.1)	0.0	0.0	0.0	0.0
Acq. Of Subsidiaries/investments	(56.7)	(20.8)	0.0	0.0	0.0
Other Investing Cashflow	(0.2)	4.5	0.0	0.0	0.0
Cash Flow From Investing	(98.6)	(42.1)	(40.0)	(50.0)	(50.0)
Debt Raised/(repaid)	25.3	(31.1)	0.0	0.0	0.0
Proceeds From Issue Of Shares					
Shares Repurchased					
Dividends Paid	(8.0)	(3.9)	(5.2)	(7.3)	(8.6)
Preferred Dividends					
Other Financing Cashflow	(2.0)	(9.5)	0.0	0.0	0.0
Cash Flow From Financing	15.3	(44.4)	(5.2)	(7.3)	(8.6)
Total Cash Generated	(9.4)	(3.6)	38.3	32.4	34.0
Free Cashflow To Equity	0.6	9.7	43.5	39.7	42.6
Free Cashflow To Firm	(20.6)	44.9	46.4	42.6	45.5

SOURCES: CGS-CIMB RESEARCH, COMPANY REPORTS

BY THE NUMBERS... cont'd

Balance Sheet

(RMm)	Jul-18A	Jul-19A	Jul-20F	Jul-21F	Jul-22F
Total Cash And Equivalents	177.6	200.0	241.2	277.0	314.7
Total Debtors	77.3	65.9	70.6	74.1	77.5
Inventories	9.3	7.4	7.9	8.3	8.7
Total Other Current Assets	16.4	10.7	10.7	10.7	10.7
Total Current Assets	280.6	284.0	330.4	370.1	411.6
Fixed Assets	211.0	164.8	132.2	110.9	90.7
Total Investments	0.0	0.0	0.0	0.0	0.0
Intangible Assets	0.0	0.0	0.0	0.0	0.0
Total Other Non-Current Assets	3.2	3.7	3.7	3.7	3.7
Total Non-current Assets	214.3	168.5	135.9	114.6	94.4
Short-term Debt	43.4	42.4	42.4	42.4	42.4
Current Portion of Long-Term Debt					
Total Creditors	37.0	24.8	26.6	27.9	29.2
Other Current Liabilities	4.6	3.4	3.4	3.4	3.4
Total Current Liabilities	85.0	70.7	72.4	73.8	75.1
Total Long-term Debt	45.0	14.9	14.9	14.9	14.9
Hybrid Debt - Debt Component					
Total Other Non-Current Liabilities	5.4	4.5	4.5	4.5	4.5
Total Non-current Liabilities	50.4	19.4	19.4	19.4	19.4
Total Provisions	3.0	3.3	3.3	3.3	3.3
Total Liabilities	138.4	93.4	95.2	96.5	97.8
Shareholders' Equity	356.5	359.1	371.1	388.2	408.3
Minority Interests	0.0	0.0	0.0	0.0	0.0
Total Equity	356.5	359.1	371.1	388.2	408.3

Key Ratios

	Jul-18A	Jul-19A	Jul-20F	Jul-21F	Jul-22F
Revenue Growth	3.5%	(12.1%)	7.1%	5.0%	4.6%
Operating EBITDA Growth	7.0%	(31.8%)	12.3%	6.3%	3.6%
Operating EBITDA Margin	34.9%	27.1%	28.4%	28.8%	28.5%
Net Cash Per Share (RM)	2.04	3.27	4.21	5.03	5.89
BVPS (RM)	8.16	8.22	8.50	8.89	9.35
Gross Interest Cover	10.66	2.05	7.29	9.83	11.46
Effective Tax Rate	10.0%	31.6%	18.0%	15.0%	15.0%
Net Dividend Payout Ratio	20.4%	55.4%	30.1%	30.0%	30.0%
Accounts Receivables Days	83.49	85.06	75.91	76.42	76.55
Inventory Days	12.98	13.42	11.79	11.93	11.91
Accounts Payables Days	88.25	49.80	39.53	40.02	39.95
ROIC (%)	14.6%	2.0%	7.6%	12.3%	15.8%
ROCE (%)	11.3%	3.3%	5.6%	7.2%	8.0%
Return On Average Assets	8.10%	1.22%	3.73%	5.04%	5.64%

Key Drivers

	Jul-18A	Jul-19A	Jul-20F	Jul-21F	Jul-22F
ASP Change (% , Main Product)	N/A	N/A	N/A	N/A	N/A
Unit sales growth (% , main prod)	3.0%	-15.0%	10.0%	5.0%	5.0%
No. Of Lines (main Product)	N/A	N/A	N/A	N/A	N/A
Rev per line (US\$, main prod)	N/A	N/A	N/A	N/A	N/A
ASP chg (% , 2ndary prod)	N/A	N/A	N/A	N/A	N/A
Unit sales grth (% , 2ndary prod)	4.0%	-15.0%	10.0%	7.0%	5.0%
No. Of Lines (secondary Product)	N/A	N/A	N/A	N/A	N/A
Rev per line (US\$, 2ndary prod)	N/A	N/A	N/A	N/A	N/A

SOURCES: CGS-CIMB RESEARCH, COMPANY REPORTS

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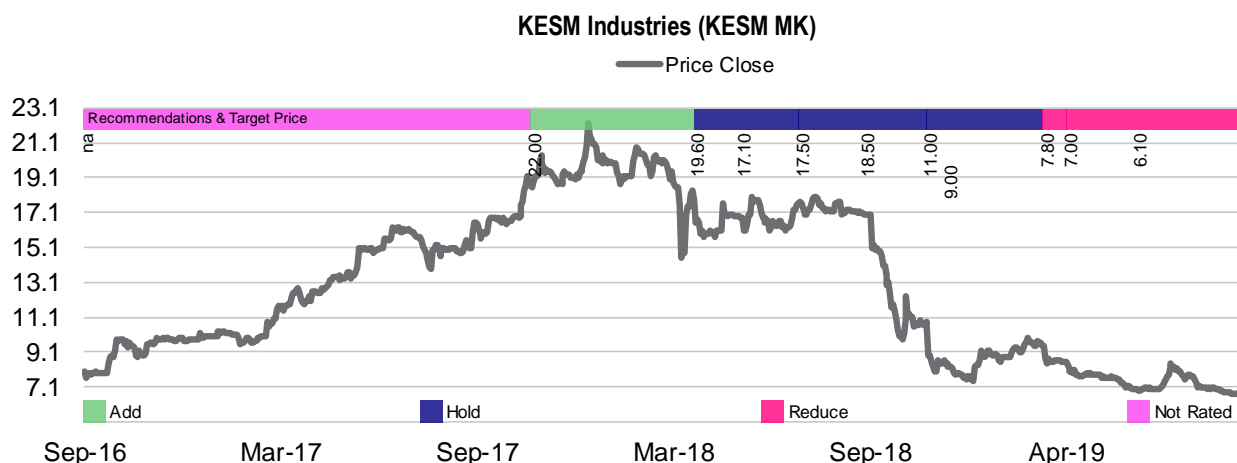
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791 companies under coverage for quarter ended on 30 June 2019		
	Rating Distribution (%)	Investment Banking clients (%)
Add	57.9%	4.2%
Hold	26.5%	1.8%
Reduce	15.5%	0.4%

Spitzer Chart for stock being researched (2 year data)



Corporate Governance Report of Thai Listed Companies (CGR). CG Rating by the Thai Institute of Directors Association (Thai IOD) in 2018, Anti-Corruption 2018

ADVANC – Excellent, Certified, **AEONTS** – Good, n/a, **AH** – Very Good, n/a, **AMATA** – Excellent, Declared, **ANAN** – Excellent, Declared, **AOT** – Excellent, Declared, **AP** – Excellent, Certified, **ASP** – Very Good, Certified, **BANPU** – Excellent, Certified, **BAY** – Excellent, Certified, **BBL** – Very Good, Certified, **BCH** – Good, Certified, **BCP** – Excellent, Certified, **BCPG** – Excellent, Certified, **BEM** – Very Good, n/a, **BDMS** – Very Good, n/a, **BEAUTY** – Good, n/a, **BEC** – Very Good, n/a, **BGRIM** – Very Good, Declared, **BH** – Good, n/a, **BJC** – Very Good, Declared, **BJCHI** – Very Good, Certified, **BLA** – Very Good, Certified, **BPP** – Very Good, Declared, **BR** – Good, Declared, **BTS** – Excellent, Certified, **CBG** – Very Good, n/a, **CCET** – Good, n/a, **CENTEL** – Very Good, Certified, **CHG** – Very Good, Declared, **CK** – Excellent, n/a, **COL** – Excellent, Declared, **CPALL** – Very Good, Certified, **CPF** – Excellent, Certified, **CPN** – Excellent, Certified, **DELTA** – Excellent, n/a, **DEMCO** – Excellent, Certified, **DDD** – Very Good, Declared, **DIF** – not available, n/a, **DREIT** – not available, n/a, **DTAC** – Excellent, Certified, **EA** – Excellent, n/a, **ECL** – Very Good, Certified, **EGCO** – Excellent, Certified, **EPG** – Very Good, n/a, **ERW** – Very Good, n/a, **GFPT** – Excellent, Certified, **GGC** – Excellent, Certified, **GLOBAL** – Very Good, n/a, **GLOW** – Very Good, Certified, **GPSC** – Excellent, Certified, **GULF** – Very Good, n/a, **GUNKUL** – Excellent, Certified, **HANA** – Excellent, Certified, **HMPRO** – Excellent, Certified, **HREIT** – Excellent, Certified, **ICHI** – Excellent, Declared, **HUMAN** – not available, n/a, **III** – Good, n/a, **INTUCH** – Excellent, Certified, **IRPC** – Excellent, Certified, **ITD*** – Very Good, n/a, **IVL** – Excellent, Certified, **JASIF** – not available, n/a, **JWD** – Very Good, n/a, **KBANK** – Excellent, Certified, **KCE** – Excellent, Certified, **KKP** – Excellent, Certified, **KSL** – Excellent, Certified, **KTB** – Excellent, Certified, **KTC** – Excellent, Certified, **LH** – Very Good, n/a, **LPN** – Excellent, Certified, **M** – Very Good, Certified, **MACO** – Very Good, n/a, **MAJOR** – Very Good, n/a, **MAKRO** – Excellent, Declared, **MALEE** – Very Good, Certified, **MC** – Very Good, Certified, **MCOT** – Excellent, Certified, **MEGA** – Very Good, n/a, **MINT** – Excellent, Certified, **MTC** – Excellent, Declared, **NETBAY** – Good, n/a, **OSP** – not available, n/a, **PLANB** – Excellent, Declared, **PLAT** – Very Good, Certified, **PR9** – not available, n/a, **PSH** – Excellent, Certified, **PSTC** – Good, Certified, **PTT** – Excellent, Certified, **PTTEP** – Excellent, Certified, **PTTGC** – Excellent, Certified, **QH** – Excellent, Certified, **RATCH** – Excellent, Certified, **ROBINS** – Excellent, Certified, **RS** – Very Good, n/a, **RSP** – not available, n/a, **S** – Very Good, n/a, **SAMART** – Excellent, n/a, **SAPPE** – Very Good, Declared, **SAT** – Excellent, Certified, **SAWAD** – Very Good, n/a, **SC** – Excellent, Declared, **SCB** – Excellent, Certified, **SCC** – Excellent, Certified, **SCN** – Very Good, Certified, **SF** – Good, n/a, **SIRI** – Very Good, Certified, **SPA** – Good, n/a, **SPALI** – Excellent, n/a, **SPRC** – Excellent, Certified, **STA** – Very Good, Certified, **STEC** – Excellent, n/a, **SVI** – Excellent, Certified, **SYNEX** – Very Good, Declared, **TASCO** – Excellent, Certified, **TCAP** – Excellent, Certified, **THANI** – Excellent, Certified, **TIPCO** – Very Good, Certified, **TISCO** – Excellent, Certified, **TKN** – Very Good, Declared, **TMB** – Excellent, Certified, **TNR** – Very Good, Declared, **TOP** – Excellent, Certified, **TPCH** – Good, n/a, **TPIPP** – Good, n/a, **TRUE** – Excellent, Certified, **TU** – Excellent, Certified, **TVO** – Very Good, Declared, **UNIQ** – Good, n/a, **VGI** – Excellent, Certified, **WHA** – Excellent, Certified, **WHART** – not available, n/a, **WICE** – Very Good, Certified, **WORK** – Good, n/a.

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- Hold** The stock's total return is expected to be between 0% and positive 10% over the next 12 months.
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The total expected return of a stock is defined as the sum of the: (i) percentage difference between the target price and the current price and (ii) the forward net dividend yields of the stock. Stock price targets have an investment horizon of 12 months.

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- Neutral** A Neutral rating means stocks in the sector have, on a market cap-weighted basis, a neutral absolute recommendation.
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