

Valuetronics Holding Ltd

3Q results to expectation. Steady performance and good transition justifies it's undervalued. Maintain Buy.

11 February 2015

SINGAPORE | Electronics | 3Q14 results update

3QFY15 hit our expectations, Industrial & Commercial Electronics (ICE) growth pacing with Consumer Electronics (CE) decline. Being cash-rich, and having a successful transition to higher margin company with earning support due to US macro make this a BUY.

- **Not only is it cheap, but with a satisfactory 3Q performance, there is a high probability for Valuetronics to beat our defensive forecast.** With our very conservative FY15 net earnings forecast from last quarter, Valuetronics has already attained 85% based on 9M15 results. Using our conservative FY15 forecast and with recent share price of 40.5 SG cents, that corresponds to 6.5x adj. FY15 PE and 3.2x FY15 PE ex net cash.
- **Market fears overblown: Last 2 quarters have shown that the market fear on CE disruption has been excessive.** The growth of ICE revenue (+4.4%) has kept pace with the decline of CE revenue (-10%) qoq, leading to a flat growth 9M15 vs 9M14 net income. For 2 quarters already, the major MNC restructuring had no obvious disruption to their client-supplier relationship. Hence, any declines in CE should not be due to client restructuring shocks, but due to the natural increase in competition due to the product phase in the innovation cycle. We are already discounted the gradual decline in CE while ...
- **Growth drivers in place: ICE segment in the right place and right time. US manufacturing and spending looks good.** Market should note that not only does the ICE segment operate at higher gross margins of ~19% (vs ~9% CE), its revenues are growing at a constant pace, on the tailwinds of improving US PMIs and a stronger US dollar. Recall that ICE customers are diversified niche leaders in industrial products that has a US market concentration, and Valuetronics is reaping the fruits of concentrating efforts in that segment.
- **Perception of Valuetronic's business quality should improve because ICE has already surpassed the CE segment in gross income distribution accounting for about 60% of gross income.** In addition, Valuetronics has been holding net income levels steady during this transition of declining LED retrofit bulbs. At some point in next few quarters, not only will market fears on the CE segment dissipate due to clarity of resolution of the major MNC restructuring (even now, there has been no obvious disruption of the client-supplier partnership), but Valuetronics will increase in gross margins based on product mix alone.
- **Buy:** With a forecasted dividend yield of 7.5%, we think this cash-rich, transitioning to higher margins company is easily undervalued. Using our conservative FY15 net income forecast we maintain our conservative target share price of 0.495 SGD based on conservative 7x FW15 PE of 6.1 SG cents EPS with only 60% idle net cash added in.

Key Financial Summary

Y/E Mar	FY11	FY12	FY13	FY14	FY15E
Revenue (HKD '000)	1,970,421	2,378,625	2,242,888	2,433,272	2,422,988
NPAT, cont. (HKD '000)	141,100	160,281	118,435	147,905	129,168
EPS. (HK cents)	34.20	36.50	21.90	39.47	35.04
P/E (X),adj.	3.8	3.4	5.8	7.7	6.5
P/B (X)	0.84	0.77	0.77	1.58	1.06
DPS (HK cents)	14.0	14.0	16.9	7.9	17.2
Div. Yield (%)	12.5%	14.6%	6.8%	6.0%	7.5%

Source: Bloomberg, PSR est.

*Forward multiples and yields are based on current price; historical multiples and yields are based on historical prices

BUY (Maintain)

CLOSING PRICE	SGD 0.405
FORECAST DIV	SGD 0.032
TARGET PRICE	SGD 0.495
TOTAL RETURN	30.1%

COMPANY DATA

O/S SHARES (MN):	375
MARKET CAP (USD mn / SGD mn):	112 / 150
52 - WK HI/LO (SGD):	0.58 / 0.27
3M Average Daily T/O (mn):	159

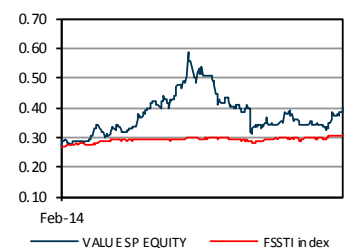
TOP FIVE SHAREHOLDERS (%)

CHONG HING TSE	18.4%
KOK KIT CHOW	7.7%
PYN RAHASTOYHTIO	4.7%
KAI WING HUNG	3.79%
KOK KEE CHOW	0.09%

PRICE PERFORMANCE (%)

	1M TH	3M TH	1Y R
COMPANY	116	13.2	511
STI RETURN	2.42	4.31	16.98

PRICE VS. STI



Source: Bloomberg, PSR

PRICE PERFORMANCE (%)

HKD MN	FY 12	FY 13	FY 14 F	FY 15 F
Revenue	2,379	2,243	2,433	2,423
EBITDA	221	175	205	181
NPAT (adj.)	160	118	148	129
EPS (hk cents)	36	22	40	34
PER, x (adj.)	3.4	5.8	7.7	6.5
P/BV, x	0.8	0.8	16	11
DPS (hk cents)	14.0	16.9	7.9	17.2
Div Yield, %	14.6%	6.8%	6.0%	7.5%
ROE, %				

Source: Bloomberg, PSR est.

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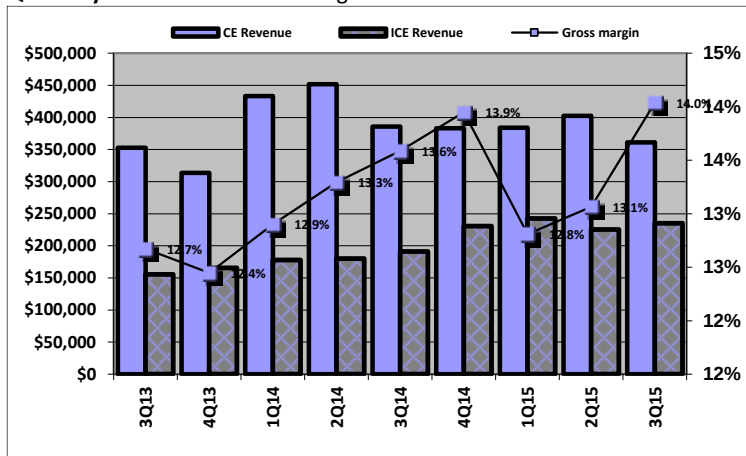
Results at a glance

(HK\$'000)	3Q14	3Q15	y-y(%)	2Q15	q-q(%)	Comments
CE Revenue	\$ 385,700	\$ 361,200	-6.4%	\$ 402,400	-10.2%	To expectations vs our -10% 3Q forecast
ICE Revenue	\$ 191,100	\$ 235,000	23.0%	\$ 225,200	+4.4%	To expectations vs our +5% 3Q forecast
Total Sales	\$ 576,800	\$ 596,200	3.4%	\$ 627,600	-5.0%	To expectations
Gross Profit	\$ 78,378	\$ 83,702	6.8%	\$ 81,996	+2.1%	To expectations
PBT	\$ 40,125	\$ 44,759	11.5%	\$ 41,159	+8.7%	Boosted by interest and FX gains
Net Profit	35,531	\$ 39,206	10.3%	36,316	+8.0%	Boosted by interest and FX gains
Adj. Net Profit	35,471	\$ 37,600	6.0%	33,388	+12.6%	Slightly better than expected

Results at a glance

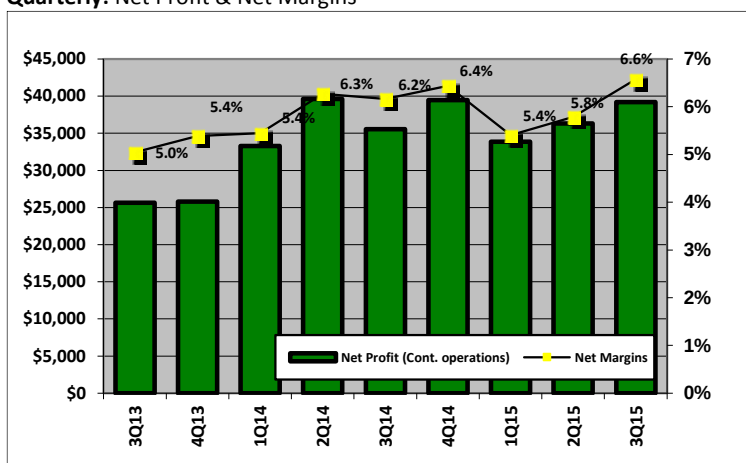
(HK\$'000)	9M14	9M15	y-y(%)	FY15 forecast	9M/FY15	Comments
CE Revenue	\$ 1,270,400	\$ 1,147,500	-9.7%	\$ 1,471,000	78.0%	Cost pressures
ICE Revenue	\$ 549,300	\$ 702,900	28.0%	\$ 952,000	73.8%	Good transitioning to ICE
Total Sales	\$ 1,819,700	\$ 1,850,400	1.7%	\$ 2,423,000	76.4%	
Gross Profit	\$ 241,249	\$ 245,959	2.0%	\$ 325,000	75.7%	Within expectations
PBT	\$ 125,988	\$ 124,382	-1.3%	\$ 146,800	84.7%	On the higher side of expectations
Net Profit	108,432	\$ 109,381	0.9%	129,200	84.7%	On the higher side of expectations

Quarterly: Revenues & Gross Margin



Source: Company, PSR

Quarterly: Net Profit & Net Margins

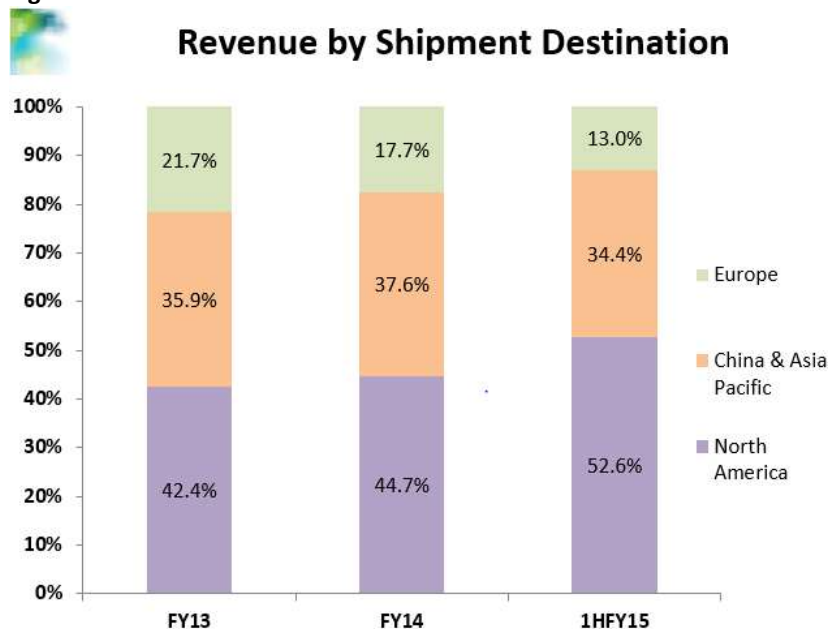


Source: Company, PSR

Economic drivers for ICE

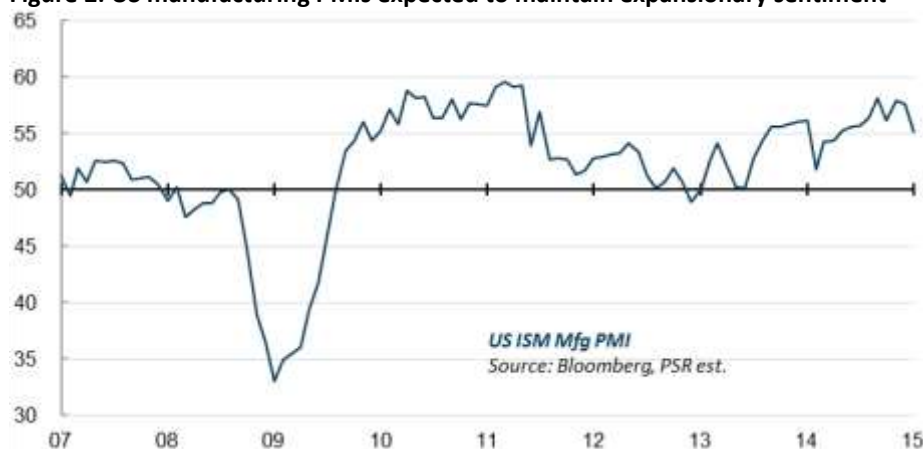
Recall that the portfolio of ICE client not only are concentrated in the US, but even their product mix is diversified from high precision GPS, refrigeration solutions equipment, to access card readers and medical equipment for testing human tissues. The 3 main shipment destinations of US, China & Asia Pacific, and Europe have improving fundamentals going for them. The US is in a sweet spot with PMIs expected to stay expansionary, and US consumers not only earning more, but saving more as well (Figure 2-4). The Bloomberg consensus real GDP growth for US is expected to be 2.8% for 2015. This bodes well for the ICE segment, whose revenues are concentrated in the US. For the other regions, China is targeting a 2015 GDP growth of 7%, and Europe has recently declared a 1.08 trillion Euro QE program till Sep 2016, which is expected to lower borrowing costs, increase the money supply, and increase wealth effects that will likely boast consumer and industrial CAPEX/OPEX spending.

Figure 1: Total Revenue distribution. ICE revenue concentrated in the US.



Source: Company

Figure 2: US manufacturing PMIs expected to maintain expansionary sentiment



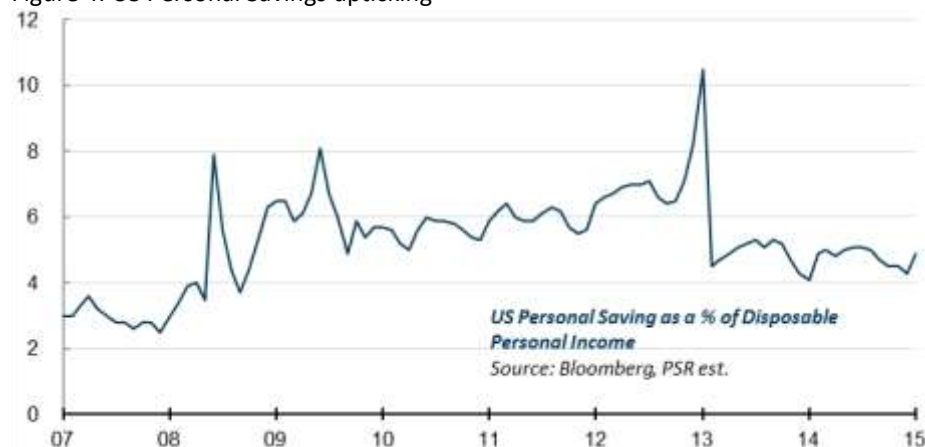
Source: Bloomberg, PSR

Figure 3: US Personal Income increasing to boost consumer spending



Source: Bloomberg, PSR

Figure 4: US Personal Savings upticking



Source: Bloomberg, PSR

Quarterly results Notes:

Revenues and Gross Profits were in-line with expectations, qoq, where CE revenue decreased by 10% and ICE revenue increased by 4.4%, this caused a slight growth of 2% for gross profit.

Net profits grew even more to +8% qoq, but this was partially due to increase of interest as well as FX translation gains due to a strengthening US dollar.

Others: The expected wage inflation was offset by savings in marketing expense.

Financials

Income Statement

Y/E Mar, HKD '000	FY12	FY13	FY14	FY15F
Revenue	2,378,625	2,242,888	2,433,272	2,422,988
EBITDA	220,946	175,425	205,449	181,474
Depreciation & Amortisation	41,265	43,768	39,674	36,839
EBIT	179,681	131,657	165,775	144,635
Net Finance (Expense)/Inc	(1,198)	(356)	1,144	2,148
Profit Before Tax	178,483	131,301	166,919	146,782
Taxation	(18,202)	(12,866)	(19,014)	(17,614)
Profit After Tax	160,281	118,435	147,905	129,168
Non-controlling Interest	-	-	-	-
Net Income, continuing	160,281	118,435	147,905	129,168
Net Income, with discontinuing	130,326	78,683	147,905	129,168

Per share data

Y/E Mar, HK cents	FY12	FY13	FY14	FY15F
EPS, basic	36.5	21.9	40.6	35.0
EPS, adj.	36.1	21.8	40.4	34.4
DPS	14.0	16.9	7.9	17.2
BVPS	158.5	164.5	197.2	211.1

Cash Flow

Y/E Mar, HKD '000	FY12	FY13	FY14	FY15F
CFO				
PBT	178,483	131,301	166,919	146,782
Adjustments	43,834	48,875	44,018	31,101
WC changes	42,108	(88,213)	100,827	(449)
Cash generated from ops	264,425	91,963	311,764	177,435
Others (Income tax, interest)	(18,004)	(19,095)	(8,807)	(17,614)
Cashflow from ops	246,421	72,868	302,957	159,821
CFI				
CAPEX, net	(44,218)	(17,926)	(20,438)	(50,000)
Others	406	(2,967)	(5,900)	2,868
Cashflow from investments	(43,812)	(20,893)	(26,338)	(47,132)
CFF				
Share issuance	2,505	268	7,314	-
Loans, net of repayments	(18,015)	(20,000)	-	-
Dividends	(49,998)	(61,022)	(29,215)	(64,584)
Others	-	-	-	-
Cashflow from financing	(65,508)	(80,754)	(21,901)	(64,584)
Net change in cash	137,101	(28,779)	254,718	48,104
Effects of exchange rates	1,294	548	1,637	-
CCE, end	263,730	221,579	477,934	526,038

Source: Company Data, PSR est

*Forward multiples & yields based on current market price; historical multiples& yields based on historical market price

Balance Sheet

Y/E Mar, HKD '000	FY12	FY13	FY14	FY15F
ASSETS				
PPE	222,689	196,454	181,681	195,345
Intangibles	10	-	-	-
Investments	-	-	-	-
Others	21,509	22,740	32,986	32,483
Total non-current assets	244,208	219,194	214,667	227,828
Inventories	204,090	178,358	198,874	198,685
Accounts Receivables	508,120	481,509	517,213	515,027
Investments	-	2,476	-	-
Cash	263,730	221,579	477,934	526,038
Others	13,238	9,327	12,843	12,843
Total current assets	989,178	893,249	1,206,864	1,252,593
Total Assets	1,233,386	1,112,443	1,421,531	1,480,421

LIABILITIES

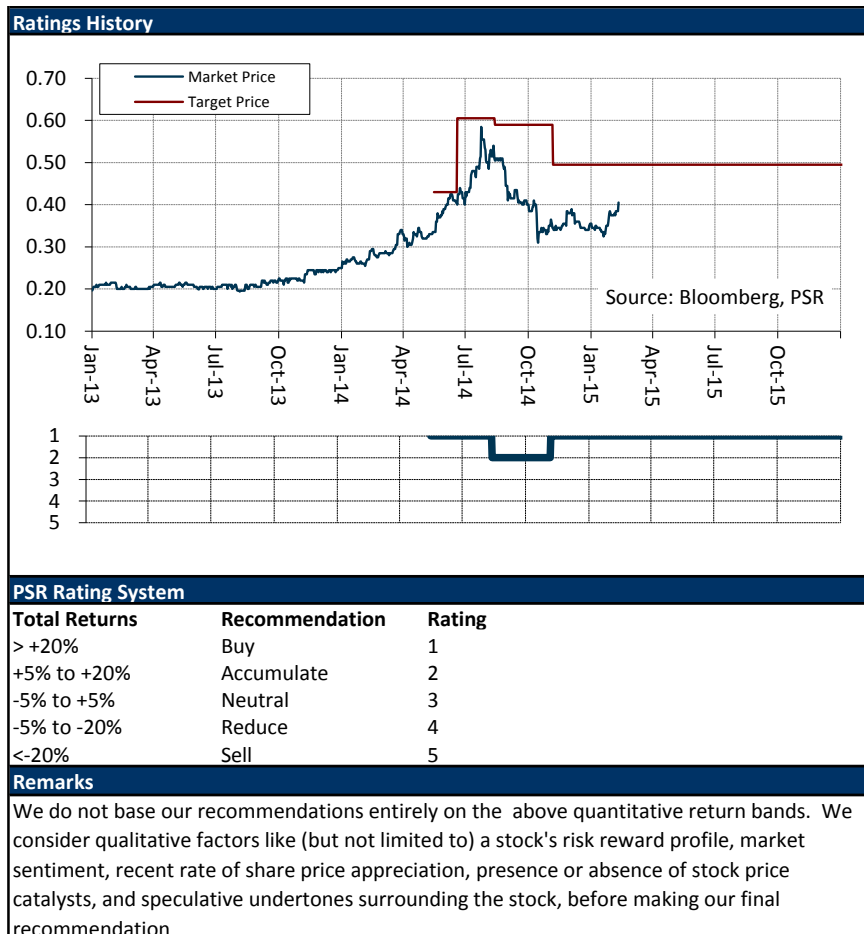
Short term loans	9,000	-	-	-
Accounts Payables	625,937	506,337	668,082	665,259
Others	15,130	10,491	24,255	21,384
Total current liabilities	650,067	516,828	692,337	686,642
Long term loans	11,000	-	-	-
Others (Deferred tax)	3,944	3,388	2,627	2,627
Total non-current liabilities	14,944	3,388	2,627	2,627
Total Liabilities	665,011	520,216	694,964	689,269

EQUITY

Non-controlling interest	-	-	-	-
Shareholder Equity	568,375	592,227	726,567	791,151

Valuation Ratios

Y/E Mar	FY12	FY13	FY14	FY15F
P/E (X) (Total)	3.4	5.8	7.7	6.5
P/B (X)	0.77	0.77	1.58	1.06
EV/EBITDA (X)	1.0	1.4	3.4	1.8
Dividend Yield (%)	14.6%	6.8%	6.0%	7.5%
Growth & Margins (%)				
Growth				
Revenue	20.7%	-5.7%	8.5%	-0.4%
EBITDA	17.0%	-20.6%	17.1%	-11.7%
EBIT	15.4%	-26.7%	25.9%	-12.8%
Net Income, adj.	7.5%	-39.6%	88.0%	-12.7%
Margins				
EBITDA margin	9.3%	7.8%	8.4%	7.5%
EBIT margin	7.6%	5.9%	6.8%	6.0%
Net Profit Margin	6.7%	5.3%	6.1%	5.3%
Key Ratios				
ROE (%)	30.7%	20.4%	22.4%	17.0%
ROA (%)	14.2%	10.1%	11.7%	8.9%
Net Debt/(Cash)	(243,730)	(221,579)	(477,934)	(526,038)
Net Gearing (X)	Net Cash	Net Cash	Net Cash	Net Cash
Net Cash/Market Cap	56%	49%	42%	63%



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