

Micro-Mechanics (Holdings) Ltd

A new growth driver emerges



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SINGAPORE | TECHNOLOGY | 4Q20 RESULTS

7 September 2020

- 4Q20 earnings met our expectations. PATMI jumped 48% YoY in 4Q20 to S\$3.9mn.
- Gross margins have recovered to their highest levels in seven quarters. We believe higher prices was a reason for the improvement.
- We are upgrading MMH to BUY. We are expecting record earnings for MMH. Firstly, the existing backend business is enjoying a recovery in sales and gross margins; Secondly, after several years of development, we believe the US operation has secured a significant breakthrough in new front-end projects and customers. It will be a new growth segment for MMH. Our target price is revised upward from S\$1.60 to S\$2.50, or 18x PE FY21e. FY21e earnings has been raised by 25%.

Results at a glance

S\$ mn	4Q20	4Q19	YoY	Comment
Revenue	16.1	14.0	15.2%	3rd consecutive quarter of appr. S\$16mn.
Gross profit	8.9	7.3	22.2%	Expansion in gross margins
Admin. Exp.	(2.3)	(2.3)	2.7%	Stable despite the rise in revenue.
PATMI	4.0	2.7	51.0%	
Gross margins	55.5%	52.3%	3.2%	Highest margins in seven quarters.
DPS - Final (cts)	5.0	5.0	0.0%	
- Special (cts)	2.0	1.0	100.0%	5th year of special dividends.

Source: Company, PSR

The Positives

+ Healthy revenue despite the disruptions. MMH managed to grow revenues despite production disruptions during the quarter. In Malaysia, staff levels were down to 25% of capacity in April and May, it recovered fully only in June. Meanwhile, the U.S. operations operated at 60% to 80% of staffing levels throughout the quarter.

+ Gross margins expanded. MMH enjoyed gross margins of 55.5% in 4Q20, the highest in seven quarters. Margins were surprisingly high despite the weaker utilization rate of 56% compared to 58% a year ago. We believe there was better pricing power in 4Q20 as customers needed to create buffers in their inventory levels with worries over possible disruption to the supply chain. A move in inventory levels from just-in-time (JIT) to just-in-case (JIC).

+ Dividends raised by 17%. The final MMH for FY20 was unchanged but special dividends doubled to 2 cents. Worth noting that MMH has been paying special dividends for the past five years. It seems to be normal rather than special. Therefore, the blended increase is 17% and total dividends for FY20 (including interim 5 cents) has increased by 20% to 12 cents. A dividend yield of 5.5%.

The Negative

- Nil.

BUY (Upgraded)

LAST TRADED PRICE	SGD 2.20
FORECAST DIV	SGD 0.13
TARGET PRICE	SGD 2.50
TOTAL RETURN	19.5%

COMPANY DATA

BLOOMBERG	MMH SP
O/S UNITS (MN)	139
MARKET CAP (USD mn / SGD mn)	224 / 306
52 - WK HI/LO (SGD)	2.23 / 1.32
3M Average Daily T/O (mn)	0.05

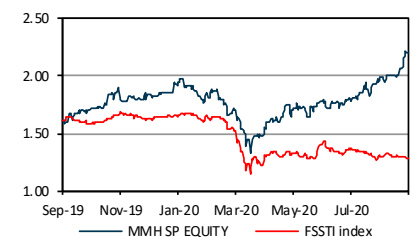
MAJOR SHAREHOLDERS

SARCADIA LLC	27.1%
CHRIS BORCH	24.8%
LOW MING WAH	5.1%

PRICE PERFORMANCE (%)

	1MTH	3MTH	1YR
COMPANY	11.7	24.3	46.0
STI RETURN	0.6	(5.5)	(16.4)

PRICE VS. STI



Source: Bloomberg, PSR

KEY FINANCIALS (MMH SP)

Y/E Jun SGDmn	FY19	FY20	FY21e	FY22e
Revenue	60.3	64.2	71.3	77.0
EBITDA	23.0	24.7	29.7	31.5
NPAT	13.0	14.7	19.2	20.8
EPS (SGD)	0.09	0.11	0.14	0.15
PER, (x)	23.6	20.9	15.9	14.7
P/BV, (x)	5.2	5.3	5.1	4.8
DPS (SGD)	0.10	0.12	0.13	0.14
DVD YIELD	4.5%	5.5%	5.9%	6.4%
ROE	21.8%	25.2%	32.4%	33.6%

Source: Bloomberg, PSR

VALUATION METHOD

18x PE FY21e

Paul Chew (+65 6212 1851)
Head Of Research
paulchewkl@phillip.com.sg

Outlook

We are upbeat on the outlook for MMH. The two major growth drivers are:

- Recovery in the semiconductor cycle: Using Taiwan back end semiconductor volumes as a barometer of the cycle, we believe another volume growth cycle is underway. As per Figure 1, a typical cycle of volume growth in units can last for an average of 33 months. The current cycle that started in September 2019 is only 10 months. The steepness in volume growth is not clear. But additional applications for semiconductors in automobile, telecommunications, IOT and gaming will be key catalysts. The usage of MMH consumables is dependent more on volumes than semiconductor prices.
- U.S. operations penetrating the front-end semi chain: US operations has been in losses for the past five of six years. The loss in FY20 was a minor S\$100k. With the announcement of the qualification of a new project with a family of ultra-critical parts in the wafer-fabrication (or front-end) process, we expect a major turnaround for the U.S. operations.

Figure 1: Growth in semiconductor volumes can linger for 33 months on average

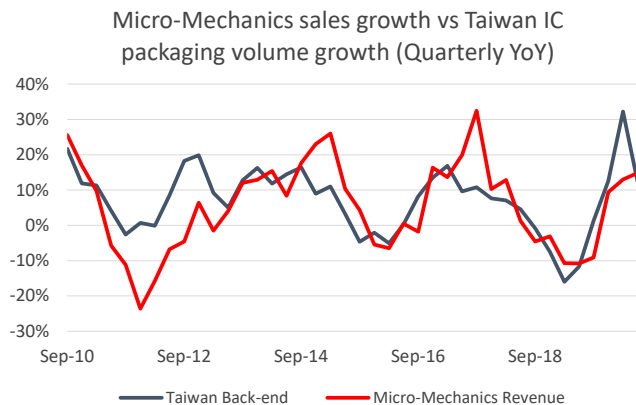
Growth Cycle	Months
Mar02 till Jan05	35
Jun05 till Sep08	40
Jul09 till Jul11	25
Apr12 till Jun15	39
Ju16 till Aug18	27
Average	33
Sep19 till present	10

Source: CEIC, PSR, The cycle is based on 3 month moving average of Taiwan semiconductor packaging volume growth.

Upgrade to BUY from NEUTRAL with a target price of S\$2.50.

We are raising our recommendation from NEUTRAL to BUY. MMH is entering a new upcycle in semiconductor volume and major penetration into a new business segment. MMH also pay an attractive dividend yield of 5.5% backed by a net cash balance sheet of S\$20mn and unlevered ROE of 25%. We benchmark our valuations to 18x PE of the back-end semiconductor equipment sector (Figure 3). Our FY21e earnings has been raised by 25%.

Figure 2: High correlation between Taiwan packaging volumes and MMH revenue



Source: CEIC, PSR

Figure 3: Back-end equipment makers trade at 18x forward PE

Company	1 Mth Perf.	3 Mth Perf.	YTD Perf.	Share Px Local Crcy	Mkt. Cap. (US\$m)	PE Yr 0	PE Yr + 1	PE Yr + 2	P/BV Yr 0	Dividend Yield	ROE Yr 0	EV/EBITDA	EBITDA Margin
OSAT													
ASE Technology	-15.7%	-10.9%	-28.5%	59.50	8,783	15.3	11.7	10.3	1.3	3.4%	8.3%	5.3	17.9%
Amkor Tech.	-15.2%	-2.0%	-11.5%	11.50	2,776	23.0	11.1	10.4	1.3	0.0%	14.0%	3.7	19.7%
Inari Amertron	-6.8%	40.8%	30.0%	2.21	1,742	46.3	32.3	26.0	6.0	2.0%	13.4%	18.7	25.1%
Unisem	4.4%	81.2%	65.3%	3.57	626	-272.0	28.4	22.5	1.9	2.0%	0.1%	9.3	14.5%
MPI	19.1%	66.4%	60.0%	18.30	878	23.8	20.8	18.9	2.6	1.5%	11.5%	7.2	24.6%
Globetronics	-3.0%	43.5%	23.2%	2.87	464	43.0	35.3	28.1	6.6	1.0%	16.9%	19.5	39.0%
	-11.4%	6.5%	-8.2%		15,268	19.6	13.5	11.9	2.1	2.4%	10.1%	7.3	19.9%
Equipment makers													
Teradyne	-12.2%	7.4%	15.3%	78.60	13,050	27.9	19.5	18.5	7.5	0.5%	38.8%	13.6	30.3%
ASM Pacific	-11.0%	11.2%	-23.9%	82.30	4,342	54.3	32.2	17.2	2.9	2.4%	7.1%	15.9	12.9%
BE Semiconductor	2.2%	2.0%	11.0%	38.26	3,626	37.7	26.7	19.3	9.7	2.6%	38.9%	18.8	31.4%
Tokyo Seimitsu	-6.4%	-12.7%	-24.4%	3220	1,264	18.8	14.7	11.8	1.2	2.4%	7.7%	6.4	17.9%
Kulicke & Soffa	0.3%	2.3%	-11.0%	24.22	1,498	128.5	26.8	18.9	2.0	2.0%	5.6%	12.5	7.8%
Micro-Mechanics	11.7%	24.3%	18.9%	2.20	224	20.9	15.9	14.7	5.3	4.5%	25.2%	10.5	40.3%
	-8.5%	6.1%	3.9%		24,003	32.7	21.9	17.8	6.3	1.4%	29.3%	14.3	25.4%

Source: Bloomberg, PSR, OSAT (outsourced assembly and test)

Financials

Income Statement

Y/E Jun, SGD mn	FY18	FY19	FY20	FY21e	FY22e
Revenue	65.1	60.3	64.2	71.3	77.0
EBITDA	27.1	23.0	24.7	29.7	31.5
Depreciation & Amortisation	(4.8)	(5.5)	(5.7)	(5.6)	(5.4)
EBIT	22.3	17.5	19.0	24.1	26.1
Net Finance Inc/(Exp)	0.0	0.0	0.0	0.0	0.0
Profit before tax	21.9	17.1	19.1	24.6	26.6
Taxation	(4.7)	(4.1)	(4.4)	(5.4)	(5.9)
Net profit before NCI	17.2	13.0	14.7	19.2	20.8
Non-controlling interest	0.0	0.0	0.0	0.0	0.0
Net profit, reported	17.2	13.0	14.7	19.2	20.8

Balance Sheet

Y/E Jun, SGD mn	FY18	FY19	FY20	FY21e	FY22e
ASSETS					
PPE	33.2	30.8	29.1	27.5	27.1
Others	2.5	2.3	3.1	3.1	3.1
Total non-current assets	35.7	33.1	32.2	30.6	30.2
Accounts receivables	11.9	10.4	12.7	12.5	14.9
Cash	21.1	21.9	20.8	29.4	26.7
Inventories	4.6	4.5	5.4	4.1	6.4
Others	0.0	0.0	0.0	0.0	0.0
Total current assets	37.6	36.8	38.9	45.9	47.9
Total Assets	73.3	69.9	71.1	76.6	78.2

LIABILITIES

Accounts payables	7.1	6.4	7.1	10.0	8.9
Short term loans	0.0	0.0	0.0	0.0	0.0
Others	2.5	2.0	2.8	2.8	2.8
Total current liabilities	9.6	8.5	10.0	12.9	11.8
Long term loans	0.0	0.0	0.0	0.0	0.0
Others	3.4	3.0	3.2	3.2	3.2
Total non-current liabilities	3.4	3.0	3.2	3.2	3.2
Total Liabilities	13.0	11.5	13.2	16.1	15.0

EQUITY

Non-controlling interests	0.0	0.0	0.0	0.0	0.0
Shareholder Equity	60.3	58.4	58.0	60.5	63.2

Valuation Ratios

Y/E Jun	FY18	FY19	FY20	FY21e	FY22e
P/E (X)	17.8	23.6	20.9	15.9	14.7
P/B (X)	5.1	5.2	5.3	5.1	4.8
EV/EBITDA (X)	10.5	12.4	11.6	9.3	8.9
Dividend Yield	4.5%	4.5%	5.5%	5.9%	6.4%

Growth & Margins

Growth					
Revenue	13.8%	-7.3%	6.4%	11.0%	8.0%
EBITDA	22.2%	-15.2%	7.4%	20.4%	6.1%
EBIT	24.7%	-21.3%	8.4%	27.0%	8.4%
Net profit, adj.	15.6%	-24.6%	13.1%	31.0%	8.2%
Margins					
EBITDA margin	41.6%	38.1%	38.4%	41.7%	41.0%
EBIT margin	34.2%	29.0%	29.6%	33.8%	34.0%
Net profit margin	26.4%	21.5%	22.8%	26.9%	27.0%

Key Ratios

ROE	29.9%	21.8%	25.2%	32.4%	33.6%
ROA	24.8%	18.1%	20.8%	26.0%	26.9%
Net Debt / (Cash)	(21)	(22)	(21)	(29)	(27)
Net Gearing (X)	Net Cash	Net Cash	Net Cash	Net Cash	Net Cash

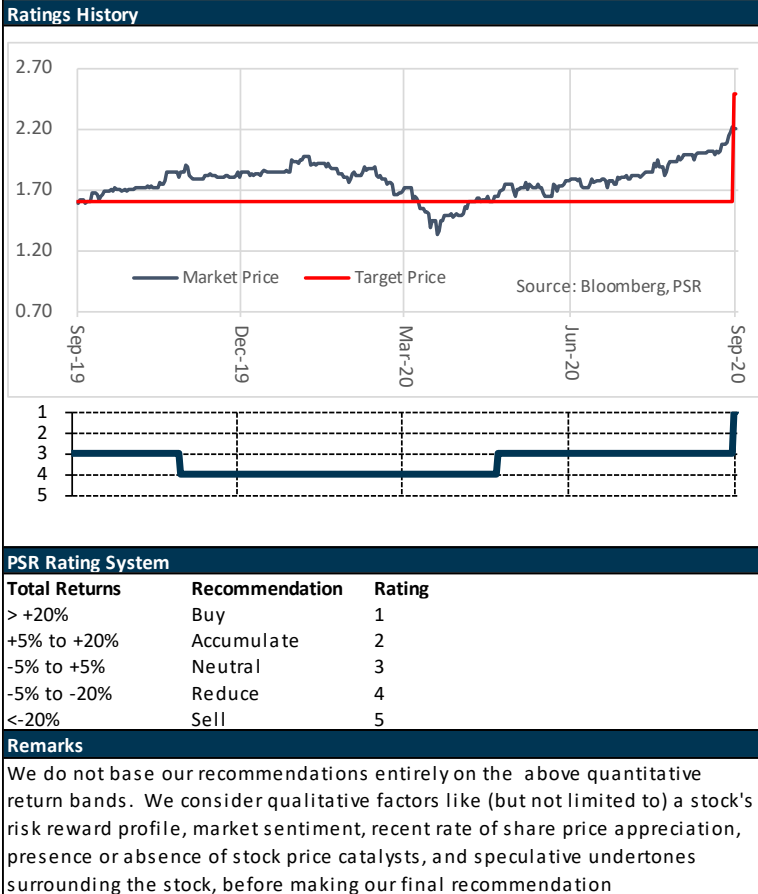
Per share data (SGD)

Y/E Jun	FY18	FY19	FY20	FY21e	FY22e
EPS, reported	0.124	0.093	0.105	0.138	0.149
DPS	0.10	0.10	0.12	0.13	0.14
BVPS	0.43	0.42	0.42	0.44	0.45

Cash Flow

Y/E Jun, SGD mn	FY18	FY19	FY20	FY21e	FY22e
CFO					
Profit before tax	21.9	17.1	19.1	24.6	26.6
Depreciation & Amortisation	4.8	6.5	6.8	5.6	5.4
WC changes	(1.3)	0.3	(3.1)	4.5	(5.8)
Net finance inc/(exp)	(0.1)	(0.1)	(0.1)	0.0	0.0
Tax paid	(3.8)	(4.6)	(3.8)	(5.4)	(5.9)
Others	(0.3)	(0.1)	(0.1)	0.0	0.0
Cashflow from ops	21.3	19.3	18.8	29.3	20.4
CFI					
CAPEX, net	(12.1)	(3.4)	(3.7)	(4.0)	(5.0)
Others	0.7	0.2	0.3	0.0	0.0
Cashflow from investments	(11.4)	(3.2)	(3.4)	(4.0)	(5.0)
CFE					
Share issuance, net	0.0	0.0	0.0	0.0	0.0
Loans, net of repayments	0.0	0.0	0.0	0.0	0.0
Dividends	(12.5)	(13.9)	(15.3)	(16.7)	(18.1)
Others	(1.1)	(1.1)	(1.1)	0.0	0.0
Cashflow from financing	(13.6)	(15.0)	(16.4)	(16.7)	(18.1)
Net change in cash	(3.7)	1.1	(1.0)	8.6	(2.7)
CCE, end	19.7	22.2	20.8	29.4	26.7

Source: Company, Phillip Securities Research (Singapore) Estimates



Contact Information (Singapore Research Team)

Head of Research

Paul Chew – paulchewkl@phillip.com.sg

Research Admin

Siti Nursyazwina – syazwina@phillip.com.sg

Property | REITs

Natalie Ong – natalieongpf@phillip.com.sg

Small-Mid Cap

Tan Jie Hui – jhtan@phillip.com.sg

Consumer | Industrial

Terence Chua – terencechuat@phillip.com.sg

Banking & Finance | Healthcare

Tay Wee Kuang – Taywk@phillip.com.sg

Credit Analyst (Bonds)

Timothy Ang – timothyang@phillip.com.sg

Technical Analyst

Chua Wei Ren – chuawr@phillip.com.sg

Contact Information (Regional Member Companies)

SINGAPORE

Phillip Securities Pte Ltd

Raffles City Tower
250, North Bridge Road #06-00
Singapore 179101
Tel +65 6533 6001
Fax +65 6535 6631
Website: www.poems.com.sg

JAPAN

Phillip Securities Japan, Ltd.

4-2 Nihonbashi Kabuto-cho Chuo-ku,
Tokyo 103-0026
Tel +81-3 3666 2101
Fax +81-3 3666 6090
Website: www.phillip.co.jp

THAILAND

Phillip Securities (Thailand) Public Co. Ltd

15th Floor, Vorawat Building,
849 Silom Road, Silom, Bangkok,
Bangkok 10500 Thailand
Tel +66-2 6351700 / 22680999
Fax +66-2 22680921
Website www.phillip.co.th

UNITED STATES

Phillip Capital Inc

141 W Jackson Blvd Ste 3050
The Chicago Board of Trade Building
Chicago, IL 60604 USA
Tel +1-312 356 9000
Fax +1-312 356 9005
Website: www.phillipusa.com

INDIA

PhillipCapital (India) Private Limited

No.1, 18th Floor, Urmi Estate
95, Ganpatrao Kadam Marg
Lower Parel West, Mumbai 400-013
Maharashtra, India
Tel: +91-22-2300 2999 / Fax: +91-22-2300 2969
Website: www.phillipcapital.in

MALAYSIA

Phillip Capital Management Sdn Bhd

B-3-6 Block B Level 3 Megan Avenue II,
No. 12, Jalan Yap Kwan Seng, 50450
Kuala Lumpur
Tel +603 2162 8841
Fax +603 2166 5099
Website: www.poems.com.my

INDONESIA

PT Phillip Securities Indonesia

ANZ Tower Level 23B,
Jl Jend Sudirman Kav 33A
Jakarta 10220 – Indonesia
Tel +62-21 5790 0800
Fax +62-21 5790 0809
Website: www.phillip.co.id

FRANCE

King & Shaxson Capital Limited

3rd Floor, 35 Rue de la Bienfaisance 75008
Paris France
Tel +33-1 45633100
Fax +33-1 45636017
Website: www.kingandshaxson.com

AUSTRALIA

Phillip Capital Limited

Level 10, 330 Collins Street
Melbourne, Victoria 3000, Australia
Tel +61-03 8633 9803
Fax +61-03 8633 9899
Website: www.phillipcapital.com.au

TURKEY

PhillipCapital Menkul Degerler

Dr. Cemil Bengü Cad. Hak Is Merkezi
No. 2 Kat. 6A Caglayan
34403 Istanbul, Turkey
Tel: 0212 296 84 84
Fax: 0212 233 69 29
Website: www.phillipcapital.com.tr

HONG KONG

Phillip Securities (HK) Ltd

11/F United Centre 95 Queensway
Hong Kong
Tel +852 2277 6600
Fax +852 2868 5307
Websites: www.phillip.com.hk

CHINA

Phillip Financial Advisory (Shanghai) Co Ltd

No 550 Yan An East Road,
Ocean Tower Unit 2318,
Postal code 200001
Tel +86-21 5169 9200
Fax +86-21 6351 2940
Website: www.phillip.com.cn

UNITED KINGDOM

King & Shaxson Capital Limited

6th Floor, Candlewick House,
120 Cannon Street,
London, EC4N 6AS
Tel +44-20 7426 5950
Fax +44-20 7626 1757
Website: www.kingandshaxson.com

CAMBODIA

Phillip Bank Plc

Ground Floor of B-Office Centre, #61-64,
Norodom Blvd Corner Street 306, Sangkat
Boeung Keng Kang 1, Khan Chamkamorn,
Phnom Penh, Cambodia
Tel: 855 (0) 7796 6151/855 (0) 1620 0769
Website: www.phillipbank.com.kh

DUBAI

Phillip Futures DMCC

Member of the Dubai Gold and
Commodities Exchange (DGCX)
Unit No 601, Plot No 58, White Crown Bldg,
Sheikh Zayed Road, P.O.Box 212291
Dubai-UAE
Tel: +971-4-3325052 / Fax: + 971-4-3328895

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