

SECTOR UPDATE

Technology – Singapore

Expect Earnings Weakness From Industry Headwinds

We expect earnings weakness for tech manufacturing stocks in 2Q23, due to weaker global demand for electronic goods and inventory destocking. Pure semiconductor names (AEM, UMS) should deliver weaker earnings due to a slowdown in the semiconductor cycle. On the other hand, stocks with a diverse customer base will not be spared from the general economic slowdown (Venture, Frencken). Aztech is the only BUY under our coverage. We have a SELL rating on AEM and Nanofilm.

WHAT'S NEW

- Tech-related companies scheduled to release their 2Q23 results between 21 July and 15 August.** Tech companies under our coverage will be releasing their 2Q22 results starting from next week with Aztech scheduled to report on 21 July, Venture on 4 August and Nanofilm on 10 August. We categorise the stocks into two groups: a) pure semiconductor names with large single customers (AEM Holdings (AEM), UMS Holdings (UMS)), and b) stocks with a diverse customer base (Venture Corp (Venture), Frencken Group (Frencken)). We believe both groups will be reporting a weaker yoy earnings for 2Q23 due to industry headwinds from weaker global demand for electronic goods.
- Pure semiconductor names are expected to record weaker yoy 1H23 earnings due to a slowdown in major segments of the semiconductor space.** We expect AEM and UMS to report 57% and 26% yoy earnings decline respectively in 2Q23. The small share (about 3%) of AI-related chips will not be able to lift global semiconductor sales out of decline for 2023. BCA Research's Jun 23 review of major semiconductor consuming sectors paints a subdued picture for global semiconductor demand: a) mobile phones, PCs and tablets, which account for about 40% of semiconductor sales, are seeing sluggish consumer demand due to overconsumption in previous years (global shipments of mobile phones and PCs plunged by around 14% and 30% in 1Q23); and b) automobiles, servers and industrial electronics, which account for around 30% of semiconductor sales, will experience <5% growth for 2023. Such small increase will not be enough to offset lower demand in the consumer electronic goods sector in the near term. China boosted its overseas purchases of processor and controller chips in 2H19 and 2020 to build up domestic inventory, but is now in a destocking process.
- Stocks with diverse customer base will not be spared from the general economic slowdown.** We believe Venture should continue to deliver a lacklustre set of results in 2Q23 after the earnings disappointment in 1Q23 as near-term demand weakness is expected based on Venture's latest customers' outlook. In its latest outlook statement, VMS has also highlighted that in the short term, the global macroeconomic and geopolitical environments remain uncertain. On the other hand, we expect Frencken to show a notable decline in its 2Q23 earnings as it expects the business environment to remain challenging in 2023 amid ongoing economic uncertainties and the cyclical downturn in the semiconductor industry. Frencken's outlook by segments for 1H23 vs 2H22 is as follows: a) semiconductor: softer revenue, b) medical: stable revenue, c) analytical & life sciences: increasing revenue, d) industrial automation: decreasing revenue, and e) automobile: stable revenue.

PEER COMPARISON

Company	Ticker	Rec	Price @ 20-Jul-23 (lcy)	Target Price (lcy)	Upside/ (Downside) to TP (%)	Market Cap (US\$m)	2022 (x)	PE 2023 (x)	2024 (x)	P/B 2023 (x)	2024 (x)	EV/EBITDA 2023 (x)	2024 (x)	ROE 2023 (%)	Yield 2023 (%)
BUY															
Aztech Global	AZTECH SP	BUY	0.695	1.00	43.9	406	8.0	6.0	5.5	1.5	1.3	2.4	2.3	27.8	7.6
Other Coverage															
Venture Corp	VMS SP	HOLD	14.62	16.99	16.2	3,216	11.5	13.3	12.8	1.5	1.4	8.5	8.2	11.1	5.5
UMS	UMSH SP	HOLD	1.10	0.97	(11.8)	558	7.5	10.7	9.8	2.0	1.8	7.9	7.3	19.2	4.5
Frencken	FRKN SP	HOLD	0.90	0.78	(13.3)	291	7.4	15.0	10.8	1.0	0.9	6.9	5.5	6.5	2.0
AEM	AEM SP	SELL	3.86	2.87	(25.6)	901	9.4	15.5	13.6	2.2	2.0	9.5	8.6	15.0	1.6
Nanofilm Tech	NANO SP	SELL	1.24	1.11	(10.5)	606	18.6	33.4	20.1	1.9	1.7	12.8	9.4	5.7	0.6

Source: Bloomberg, UOB Kay Hian

MARKET WEIGHT

(Downgraded)

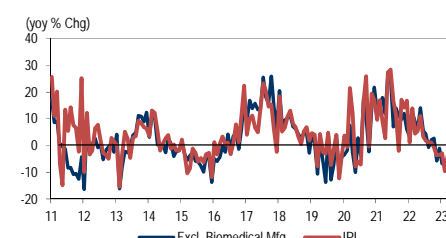
STOCKS UNDER COVERAGE

Company	Rec	Target Price (\$)	Share Price (\$)	UOBKH 2023 Estimated Earnings (\$m)
BUYS				
Aztech Global	BUY	1.00	0.695	20 (-31% yoy)
Other coverage				
Venture	HOLD	16.99	14.62	73 (-19% yoy)
Frencken Group	HOLD	0.78	0.90	6 (-55% yoy)
UMS Holdings	HOLD	0.97	1.10	15 (-26% yoy)
AEM	SELL	2.87	3.86	18 (-57% yoy)
Nanofilm	SELL	1.11	1.24	-8* (vs 19 in 1H22)

Source: UOB Kay Hian

* 1H23 earnings due to absence of 1Q23 earnings reporting

SINGAPORE INDUSTRIAL PRODUCTION



Source: CEIC

PURCHASING MANAGER INDEX



Source: CEIC

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ESSENTIALS

- **Weak results from global chipmakers indicate room for earnings disappointment, which could lead to further earnings downgrade.** We believe there is a good chance for earnings disappointment moving into 2Q23 as the street has not fully factored in the demand slowdown and margin contraction as volume declines. Based on the latest results of the major chipmakers including Taiwan Semiconductor Manufacturing Company (TSMC), Samsung and Intel, they have all indicated demand weakness for 2023: a) TSMC's 2Q23 revenue and earnings fell 14% and 23% yoy. It has cut its guidance in projecting a 10% fall in sales this year, vs a previous guidance for a single-digit decline, b) Samsung reported an 18% yoy revenue decline in 1Q23 due to demand weakness for memory chips, and c) Intel reported a 36% yoy decline in its 1Q23 revenue.

ACTION

- **Downgrade to MARKET WEIGHT.** We recommend investors to be cautious in the tech manufacturing sector as 2Q23 results could surprise on the downside. For those who seek to increase exposure in the sector should wait for better clarity after the 2Q23 results announcement.

AEM Holdings (AEM SP/SELL/Target: S\$2.87)

- **Expect 2Q23 earnings to decline significantly yoy due to high base effect and inventory destocking.** We are expecting AEM to report 2Q23 earnings of S\$18m (-57% yoy, +16% qoq), with the decline from an exceptionally strong 2Q22. This was mainly driven by the exceptionally high revenue in 2Q22 due to the volume ramp up in its customer's new platforms which started to taper in 3Q22. Major customer Intel generated around 30% of total revenue from the data centre & AI segment in 1Q23 but this has been declining due to a decrease in server volume as the customers are tempering purchases to reduce existing inventories in a softening data centre market. In its latest guidance in 1Q23 results release, Intel also highlighted that it expects the macroeconomic uncertainty and the challenging market condition will continue during 2023.
- **Maintain SELL and target price of S\$2.87.** This is based on 11.5x 2023F PE, pegged to 0.5SD above AEM's long-term forward mean PE.

UMS Holdings (UMSH SP/HOLD/Target: S\$0.97)

- **Expect yoy and qoq earnings decline for 2Q23.** We are expecting UMS to report 2Q23 earnings of S\$15m (-26% yoy/-14% qoq), as the company should see weaker demand for its semiconductor integrated system sales due to lower wafer fabrication equipment spending. Semiconductor Equipment and Materials International (SEMI) predicts global fab equipment spending for front-end facilities to decrease 22% yoy to US\$76b in 2023 from a record high of US\$98b in 2022 before rising 21% yoy to US\$92b in 2024. Specifically for UMS, Applied Material (AMAT) has guided for its semiconductor system sales to grow 2% yoy but decline 6% qoq in 2Q23 as it expects 2023 wafer fabrication equipment spending to decline yoy.
- **Maintain HOLD with a target price of S\$0.97,** based on a PE-based valuation of 9.5x 2023F EPS. This is pegged to 0.5SD below UMS's long-term forward mean PE to reflect the more challenging near-term outlook in the semiconductor industry.

Venture Corp (VMS SP/HOLD/Target: S\$16.99)

- **Expect earnings to decline 14% yoy but expand 6% qoq; demand from customers remain weak.** We expect Venture to report 2Q23 earnings of S\$73m (-19% yoy, -1% qoq). Based on Venture's customers' outlook, near-term demand weakness is expected. Venture also highlighted in its latest outlook statement that in the short term, the global macroeconomic and geopolitical environments remain uncertain. While prevailing market conditions affecting demand are beyond Venture's control, it is proactively pursuing multiple pathways to drive revenue and profitability. Leveraging on its diverse service offerings and differentiating capabilities, Venture will work on increasing market share.

- **Maintain HOLD and target price of S\$16.99**, pegged to its long-term forward mean PE of 15.5x 2023F earnings. Currently, VMS offers a decent dividend yield of around 5.5%.

Frencken Group (FRKN SP/HOLD/Target: S\$0.78)

- **Expect continued weakness in 2Q23 results as business environment remains challenging for 2023.** We expect 2Q23 earnings of S\$6m (-55% yoy/+15% qoq) as the business environment remain challenging in 2023 amid ongoing economic uncertainties and the cyclical downturn in the semiconductor industry. Frencken's outlook for its various segments for 1H23 vs 2H22 is as follows: a) semiconductor: softer revenue, b) medical: stable revenue, c) analytical & life sciences: increasing revenue, d) industrial automation: decreasing revenue, and e) automobile: stable revenue. Backed by its diverse exposure to multiple market segments, Frencken is confident of weathering the current headwinds.
- **Maintain HOLD with target price of S\$0.78, pegged to 13x 2023F PE**, based on 1SD above mean PE.

NanoFilm Technologies (NANO SP/SELL/Target: S\$1.11)

- **Issued a profit warning, guiding for weak 1H23 earnings due to market-related issues.** Nanofilm expects that it will report 1H23 net loss of S\$8m (vs S\$19m net profit in 1H22/S\$25m in 2H22). The weaker-than-expected performance is attributable to: a) slower-than-expected recovery in end-consumer sentiment linked to macro challenges, b) softer-than-anticipated post-reopening recovery in China during 1H23, c) weaker demand across the broader consumer electronics sector that has significantly impacted Nanofilm's Advanced Material Business Unit (AMBU), and d) increased operating expenses due to investments in long-term business initiatives. Nanofilm expects revenue for 2H23 to be better than and remain profitable for full-year 2023. However, given that the consumer market contributes a large portion of Nanofilm's revenue, its outlook depends on the various key factors not worsening
- **Maintain SELL with a target price of S\$1.11.** We value Nanofilm based on 18x 2024F EPS, pegged to -1SD of its historical mean to reflect the challenging environment it is facing.

Aztech Group (AZTECH SP/BUY/Target: S\$1.00)

- **Expect yoy earnings decline for 2Q23 but improvement qoq due to seasonality and strengthening of USD vs CNY.** We expect Aztech to report 2Q23 earnings of S\$20m (-31% yoy, +49% qoq). We believe coming off of low 1Q seasonality and notable strengthening of USD vs CNY in 1Q23 will help lift Aztech's 2Q23 earnings. Aztech's orderbook remained strong at S\$662m as at 4 May 23 and the majority of these are scheduled for completion in 2023. In its latest outlook statement, Aztech is cautiously optimistic on its 2023 business outlook, as it expects a double-digit growth in its major customer's revenue. While Aztech works on ramping up its new Malaysia operations, it will continue to manage its orderbook by balancing and co-ordinating customer orders across its manufacturing plants to ensure timely and efficient delivery.
- **Maintain BUY and target price of S\$1.00**, pegged to 8.6x 2023F EPS. This is based on Aztech's long-term mean PE. We continue to like Aztech as it is a proxy to high-growth IoT products, for which we believe orders will continue to grow in 2023.

SECTOR CATALYSTS

- Increasing capex spending by upstream global tech manufacturers.
- Better-than-expected 2Q23 sales and earnings. Improved guidance for 2H23.

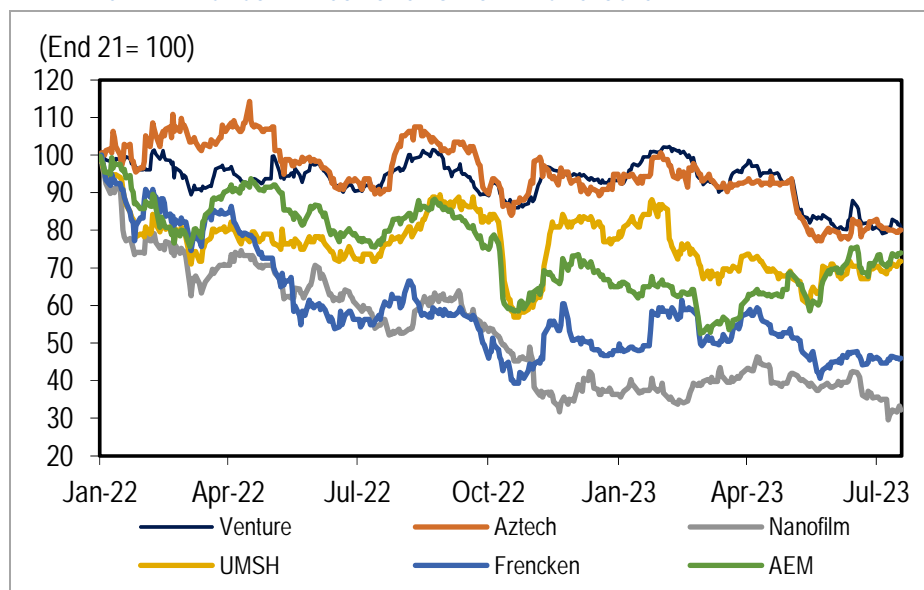
ASSUMPTION CHANGES

- No changes to our forecasts.

RISKS

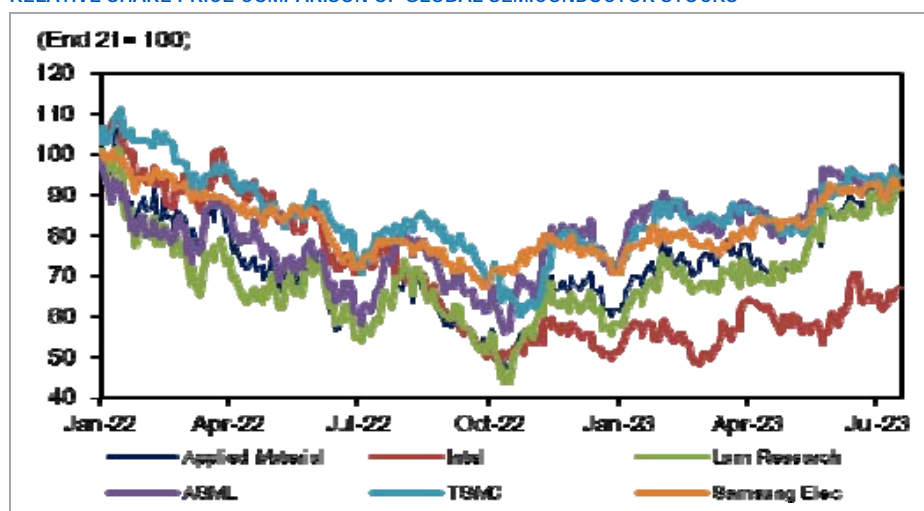
- Reduced demand for electronic goods as a result of global recession.
- Escalation of geopolitical tension and trade conflict between the US and China.

RELATIVE SHARE PRICE COMPARISON OF SINGAPORE TECH STOCKS



Source: Bloomberg, UOB Kay Hian

RELATIVE SHARE PRICE COMPARISON OF GLOBAL SEMICONDUCTOR STOCKS



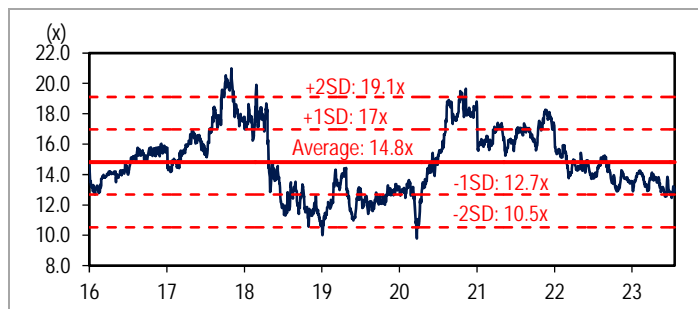
Source: Bloomberg, UOB Kay Hian

PEER COMPARISON TABLE OF GLOBAL SEMICONDUCTOR PLAYERS

Company	Ticker	Trading Curr (lcy)	Price @ 20-Jul-23 (lcy)	Market Cap (US\$m)	2022 (x)	PE 2023 (x)	2024 (x)	P/B 2023 (x)	2024 (x)	EV/EBITDA 2023 (x)	2024 (x)	ROE 2023 (%)	Yield 2023 (%)
Applied Material	AMAT US	USD	141.78	119,059	18.9	19.2	19.9	8.1	8.0	15.7	16.7	45.5	0.8
Intel	INTC US	USD	34.46	143,733	17.7	102.6	20.7	1.5	1.4	16.1	9.9	0.3	2.1
Lam Research	LRCX US	USD	640.11	85,993	19.4	19.3	24.9	10.5	10.2	15.5	19.5	60.2	1.1
ASML	ASML NA	EUR	633.30	286,174	44.8	32.9	28.1	22.6	18.6	26.8	22.7	74.5	1.0
TSMC	2330 TT	TWD	579.00	482,787	14.8	18.6	15.0	4.4	3.6	10.0	7.9	25.2	2.1
Samsung Elec	005930 KS	KRW	71000.00	333,083	8.8	46.0	14.9	1.4	1.3	6.7	4.2	3.0	2.0
Average					20.7	39.8	20.6	8.1	7.2	15.1	13.5	34.8	1.5

Source: Bloomberg, UOB Kay Hian

VENTURE CORP 12-MONTH FORWARD PE BAND



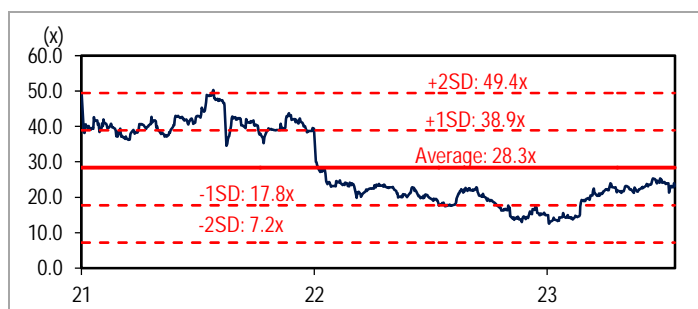
Source: Bloomberg, UOB Kay Hian

AZTECH GLOBAL 12-MONTH FORWARD PE BAND



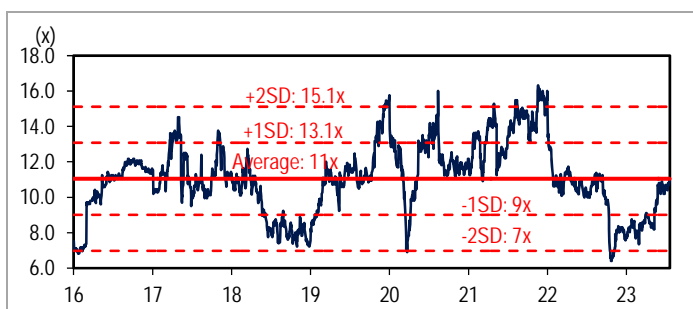
Source: Bloomberg, UOB Kay Hian

NANOFILM TECHNOLOGIES 12-MONTH FORWARD PE BAND



Source: Bloomberg, UOB Kay Hian

UMS HOLDINGS 12-MONTH FORWARD PE BAND



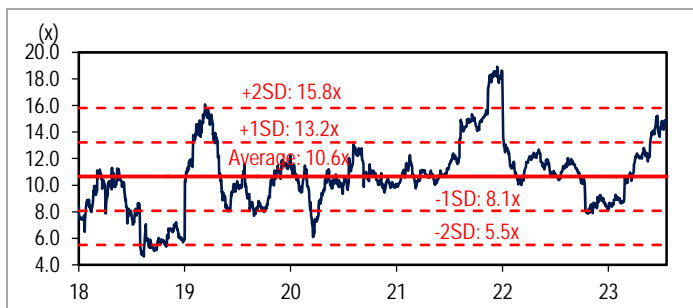
Source: Bloomberg, UOB Kay Hian

FRENCKEN GROUP 12-MONTH FORWARD PE BAND



Source: Bloomberg, UOB Kay Hian

AEM 12-MONTH FORWARD PE BAND



Source: Bloomberg, UOB Kay Hian

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