

COMPANY UPDATE

Frencken Group (FRKN SP)

Positive Outlook For Key Customer And Improving Cost Pressure

ASML reported a strong 4Q22 earnings growth of 28% yoy on 25 Jan 23 and guided for sales growth of more than 25% yoy in 2023 as demand remains high. We expect Frencken to benefit from this guidance as ASML contributed around 30% of its total revenue as of 1H22. Also, Frencken's gross margin should improve qoq as electricity costs in Europe are falling and Frencken had passed on cost increases to customers in 4Q22. Upgrade to BUY with a 27% higher target price of S\$1.36.

WHAT'S NEW

- Positive guidance from major customer ASML.** On 25 Jan 23, Frencken Group's (Frencken) major customer ASML reported a strong 4Q22 earnings growth of 28% yoy which beat earnings forecast as it is still struggling to meet demand from top customers: TSMC, Samsung and Intel which are engaged in major expansion. ASML highlighted that its order backlog has increased to a record €40b as of 2022 and guided for a rise of more than 25% in 2023 sales despite possible new curbs on its exports to China. ASML's CEO highlighted that although the economic outlook for 2023 is clouded by worries over the economy and growing semiconductor inventories, customers also see conditions improving toward the end of the year and China's economy recovering after the end of COVID-19 curbs. As a result, the demand is still higher than what ASML can make.
- Falling natural gas prices in Europe should reduce Frencken's energy expenses.** The Dutch TTF Natural Gas Future has fallen by close to 50% mom and by around 15% ytd as Europe has managed to make it through winter so far without severe energy shortages, thanks to above-normal temperatures, ample supplies and reduced consumption. This bodes well for Frencken as close to 40% of its revenue was derived from Europe in 1H22, with majority from The Netherlands. To recap, Frencken's gross profit margin fell to 13.7% in 3Q22 from 17.1% in 3Q21 as the inflationary cost pressures were prevalent in Europe due to soaring energy expenses and manpower costs.
- Frencken's latest guidance indicates positive cost-sharing efforts; 2H22 to be stable hoh.** Based on the latest outlook statement from the 3Q22 business update, Frencken expects its cost-sharing efforts with customers in Europe to yield positive effects from 4Q22 and expects group revenue in 2H22 to be stable hoh. Breakdown of outlook by segments: a) semiconductor: stable, b) medical: increase, c) automobile: increase, d) analytical & life science: slightly lower, and e) industrial automation: decrease.

KEY FINANCIALS

Year to 31 Dec (\$m)	2020	2021	2022F	2023F	2024F
Net turnover	621	767	781	831	889
EBITDA	80	95	84	96	102
Operating profit	59	72	60	71	76
Net profit (rep./act.)	43	59	47	57	61
Net profit (adj.)	43	59	47	57	61
EPS (S\$ cents)	10.0	13.8	11.1	13.3	14.2
PE (x)	11.5	8.4	10.4	8.6	8.1
P/B (x)	1.5	1.3	1.2	1.1	1.0
EV/EBITDA (x)	4.1	3.4	3.9	3.4	3.2
Dividend yield (%)	2.6	3.6	2.9	3.5	3.7
Net margin (%)	6.9	7.7	6.1	6.8	6.8
Net debt/(cash) to equity (%)	(32.1)	(25.4)	(32.8)	(37.2)	(41.4)
Interest cover (x)	95.6	67.6	58.7	63.2	62.8
ROE (%)	13.5	16.5	12.1	13.3	12.9
Consensus net profit	-	-	49	56	60
UOBKH/Consensus (x)	-	-	0.97	1.01	1.02

Source: Frencken, Bloomberg, UOB Kay Hian

BUY

(Upgraded)

Share Price	S\$1.15
Target Price	S\$1.36
Upside	18.3%
(Previous TP)	S\$1.07)

COMPANY DESCRIPTION

Frencken is a global integrated technology solutions company. The group provides ODM and OEM services for the automotive, healthcare, industrial, analytical & life sciences and semiconductor industries.

STOCK DATA

GICS sector	Information Technology
Bloomberg ticker:	FRKN SP
Shares issued (m):	427.0
Market cap (S\$m):	491.1
Market cap (US\$m):	374.5
3-mth avg daily t'over (US\$m):	3.2

Price Performance (%)

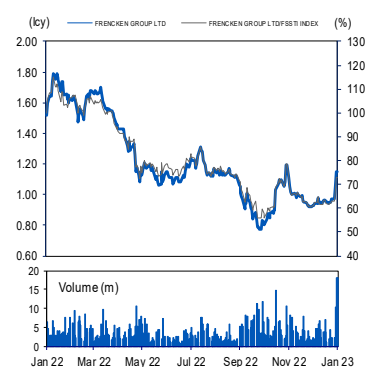
52-week high/low S\$ 1.79/S\$ 0.775

1mth	3mth	6mth	1yr	YTD
25.0	39.4	(4.2)	(29.0)	21.7

Major Shareholders

	%
Dato' Gooi Soon Chai	23.5
-	-
-	-
FY23 NAV/Share (S\$)	1.05
FY23 Net Cash/Share (S\$)	0.39

PRICE CHART



Source: Bloomberg

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STOCK IMPACT

- **Frencken should benefit from improved orders from key customer and recovery in gross margin.** Based on the huge order backlog and positive sales growth guidance of ASML, Frencken should benefit from improved order flows from ASML as it contributed around 30% of Frencken's revenue in 1H22. In addition, Frencken should enjoy a recovery in gross margin due to falling energy costs in Europe coupled with its cost-sharing efforts with customers that is expected to yield positive impact in 4Q22.

EARNINGS REVISION/RISK

- We maintain our earnings forecasts.

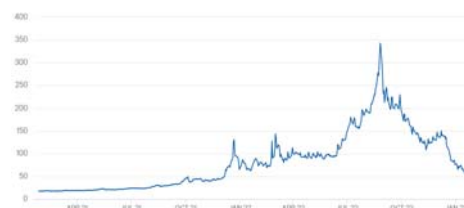
VALUATION/RECOMMENDATION

- **Upgrade to BUY with a 27% higher target price of S\$1.36**, pegged to 10.2x 2023F PE, based on mean PE (raised from 8x 2023F PE, based on -1SD of mean PE previously) to reflect the improved outlook from its key customer and reducing energy costs of its key market. We note that Frencken has a diverse stream of revenue sources, which could help the company stand firm amid a volatile macro environment.

SHARE PRICE CATALYST

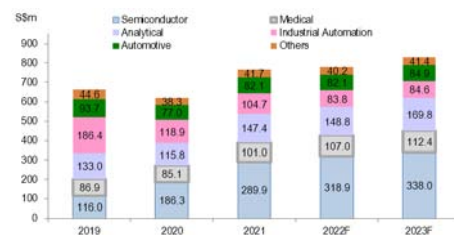
- Higher-than-expected factory utilisation rates.
- Better-than-expected cost management.

DUTCH TTF NATURAL GAS FUTURES



Source: ICE

2019-23 REVENUE BY SEGMENT



Source: Frencken, UOB Kay Hian

FRENCKEN'S FORWARD PE BAND



Source: Bloomberg, UOB Kay Hian

PEER COMPARISON

Company	Ticker	Trading Curr (TC)	Price @ 26-Jan-23 (TC)	Market Cap (USD)	PE		PB		EV/EBITDA		Yield 2022F (%)	Net Gearing (%)
					2022F (x)	2023F (x)	2022F (x)	2023F (x)	2022F (x)	2023F (x)		
Frencken	FRKN SP	SGD	1.15	374	10.4	8.6	1.2	1.1	3.9	3.4	2.9	(18.0)
SGX-listed peers												
Venture	VMS SP	SGD	18.46	4,094	14.7	14.1	1.9	1.8	10.3	9.9	4.3	(25.1)
AEM	AEM SP	SGD	3.56	838	8.3	9.5	2.3	1.9	5.9	6.7	3.0	(17.6)
UMS	UMSH SP	SGD	1.34	685	8.8	8.2	2.6	2.1	7.7	6.5	3.7	(8.9)
Average					10.6	10.6	2.2	1.9	8.0	7.7	3.7	
Semiconductor (39% of Frencken's 2022F sales)												
Asmi Hol	ASML NA	EUR	617.1	271,564	43.6	33.5	28.2	23.9	34.6	26.6	0.9	(43.8)
Intel Corp	INTC US	USD	29.7	122,572	15.2	17.2	1.2	1.2	7.0	6.6	5.0	11.2
Kulicke & Soffa	KLIC US	USD	52.59	2,992	7.3	23.2	2.5	n.a.	4.5	16.9	1.3	(61.4)
Benchmark Elec	BHE US	USD	29.08	1,023	13.7	12.2	n.a.	n.a.	n.a.	n.a.	n.a.	15.3
Average					20.0	21.5	10.7	12.6	15.4	16.7	2.4	
Industrial automation (16% of 2022F sales)												
Seagate Tech	STX US	USD	62.25	12,854	8.3	37.1	119.8	n.a.	7.6	15.6	4.4	4,661.5
Western Digital	WDC US	USD	41.31	13,122	8.6	n.a.	1.1	1.1	5.5	13.9	0.0	44.0
Average					8.4	37.1	60.5	1.1	6.5	14.8	2.2	
Analytical & Medical (31% of 2022F sales)												
Thermo Fisher	TMO US	USD	575.32	225,638	25.0	24.9	5.1	4.7	21.2	21.2	0.2	60.0
Oxford Instruments	OXIG LN	GBP	2340	1,674	24.1	23.1	396.6	354.5	n.a.	n.a.	0.8	(20.8)
Koninklijke Philips	PHIA NA	EUR	15.448	14,997	18.4	14.1	1.1	1.1	10.5	8.4	5.5	45.6
Siemens Healthineers	SHL GR	EUR	48.86	60,163	27.0	23.7	2.8	2.7	16.4	16.8	1.9	74.8
Average					23.6	21.4	101.4	90.8	16.1	15.5	2.1	
Automotive peers (15% of 2022F sales)												
Valeo	FR FP	EUR	18.95	5,037	21.8	10.6	1.2	1.1	3.9	3.4	2.1	80.2
Visteon	VC US	USD	143.21	4,030	26.0	19.4	6.5	5.8	12.6	10.1	0.0	17.1
Thyssenkrupp	TKA GR	EUR	7.118	4,837	3.9	13.5	0.3	0.3	0.6	0.9	2.1	(23.4)
Bosch	BOS IN	INR	16720.35	6,052	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	0.8	(30.1)
Denso	6902 JP	JPY	6923	42,169	14.4	11.3	1.2	1.1	7.1	6.1	2.6	3.7
Johnson Contr	JCI US	USD	68.1	46,799	31.0	19.4	2.9	2.7	19.6	13.4	2.0	47.1
Average					19.4	14.8	2.4	2.2	8.8	6.8	1.6	

Source: Bloomberg, UOB Kay Hian

PROFIT & LOSS

Year to 31 Dec (\$m)	2021	2022F	2023F	2024F
Net turnover	767.1	780.9	831.1	888.5
EBITDA	94.9	83.8	96.0	102.0
Deprec. & amort.	23.0	24.1	25.3	26.5
EBIT	71.9	59.8	70.7	75.6
Associate contributions	0.0	0.0	0.0	0.0
Net interest income/(expense)	(1.4)	(1.4)	(1.5)	(1.6)
Pre-tax profit	70.5	58.3	69.2	73.9
Tax	(11.4)	(10.5)	(11.8)	(12.6)
Minorities	(0.4)	(0.4)	(0.5)	(0.5)
Net profit	58.7	47.4	56.9	60.8
Net profit (adj.)	58.7	47.4	56.9	60.8

BALANCE SHEET

Year to 31 Dec (\$m)	2021	2022F	2023F	2024F
Fixed assets	127.9	126.9	124.6	121.1
Other LT assets	24.4	24.1	23.7	23.4
Cash/ST investment	192.6	216.5	259.0	304.6
Other current assets	343.2	322.8	352.1	380.4
Total assets	688.1	690.2	759.4	829.4
ST debt	95.6	81.9	90.5	99.3
Other current liabilities	192.7	177.8	194.5	210.2
LT debt	1.6	1.6	1.6	1.6
Other LT liabilities	19.2	20.1	21.1	22.5
Shareholders' equity	376.2	405.9	448.6	492.3
Minority interest	2.9	2.9	2.9	2.9
Total liabilities & equity	688.1	690.1	759.1	828.8

CASH FLOW

Year to 31 Dec (\$m)	2021	2022F	2023F	2024F
Operating	40.4	78.3	71.0	76.6
Pre-tax profit	70.5	58.3	69.2	73.9
Tax	(16.2)	(10.4)	(11.2)	(12.0)
Deprec. & amort.	23.0	24.1	25.3	26.5
Working capital changes	(32.1)	6.3	(12.3)	(11.8)
Non-cash items	(4.8)	0.0	0.0	0.0
Investing	(15.8)	(21.7)	(21.6)	(21.5)
Capex (growth)	(17.5)	(23.0)	(23.0)	(23.0)
Proceeds from sale of assets	0.3	0.0	0.0	0.0
Others	1.4	1.3	1.4	1.5
Financing	(9.2)	(33.8)	(8.2)	(11.0)
Dividend payments	(12.7)	(17.6)	(14.2)	(17.1)
Issue of shares	0.1	0.0	0.0	0.0
Loan repayment	29.9	(13.8)	8.6	8.8
Others/interest paid	(26.5)	(2.4)	(2.6)	(2.7)
Net cash inflow (outflow)	15.4	22.8	41.3	44.1
Beginning cash & cash equivalent	174.5	192.6	216.5	259.0
Changes due to forex impact	2.8	1.1	1.2	1.5
Ending cash & cash equivalent	192.6	216.5	259.0	304.6

KEY METRICS

Year to 31 Dec (%)	2021	2022F	2023F	2024F
Profitability				
EBITDA margin	12.4	10.7	11.6	11.5
Pre-tax margin	9.2	7.5	8.3	8.3
Net margin	7.7	6.1	6.8	6.8
ROA	9.4	6.9	7.8	7.7
ROE	16.5	12.1	13.3	12.9
Growth				
Turnover	23.6	1.8	6.4	6.9
EBITDA	18.5	(11.7)	14.5	6.3
Pre-tax profit	36.0	(17.3)	18.6	6.8
Net profit	38.0	(19.3)	20.1	6.9
Net profit (adj.)	38.0	(19.3)	20.1	6.9
EPS	37.8	(19.3)	20.1	6.9
Leverage				
Debt to total capital	20.4	17.0	16.9	16.9
Debt to equity	25.8	20.6	20.5	20.5
Net debt/(cash) to equity	(25.4)	(32.8)	(37.2)	(41.4)
Interest cover (x)	67.6	58.7	63.2	62.8

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