27 October 2023

Technology | Semiconductors

Unisem (M) (UNI MK)

Neutral (Maintained)

Early Signs Of An Uneven Recovery In 4Q

Target Price (Return):	MYR2.98 (-4%)
Price (Market Cap):	MYR3.10 (USD1,045m)
ESG score:	2.9 (out of 4)
Avg Daily Turnover (MYR/USD)	1.98m/0.42m

- **Maintain NEUTRAL and MYR2.98 TP, 4% downside, c.2% yield.** Unisem (M)'s 9M23 results were a slight miss, as overall volume recovery was lower than expected. We trim our forecasts to reflect the prolonged weakness. A third interim dividend of 2 sen/share was declared. 4Q results are likely to be flattish-to-slightly better on more spot orders and an early recovery of China's smartphone segment. Management remains cautious on overall sector demand, citing uncertainties on end-consumer demand.
- **Slower-than-expected recovery.** 9M23 revenue of MYR1088.9m (-18.0% YoY) translated to core earnings of MYR55.0m (-69.3% YoY) – below expectations at only 61.2% and 55.9% of our and Street full-year estimates. Revenue was affected by soft demand from the overall semiconductor industry, which dragged EBITDA margin to 21.5% (9M22: 27.3%). Its bottomline, in turn, was further affected by higher staff and utility costs.
- **Prolonged weakness.** 3Q23 revenue of MYR356.2m was lower by 5.9% QoQ and 19% YoY as the loadings continued to be affected by lacklustre demand in the semiconductor sector. This led to a 60.9% dip YoY in core earnings to MYR22.2m, despite more favourable FX. However, earnings showed a mild 4.9% sequential improvement thanks to better margins from its product mix and lower staff costs. The headcount was further reduced by 71 QoQ to 5,675 from natural attrition, and is commensurate with the low utilisation rate.
- **Outlook.** Management guided for flattish-to-slightly better QoQ revenue, as sentiment in the semiconductor industry remains weak from prolonged lacklustre end-consumer demand and geopolitical tensions. Chengdu Phase 3 is undergoing qualification and will be ready to contribute in FY24. The Gopeng plant is progressing and is expected to be completed by 4Q23, followed by customer qualification and equipment installation in 1H24. Total capex incurred in 3Q23 was MYR77m (2Q23: MYR62.9m), for the Gopeng plant's construction and purchase of equipment for the Chengdu plant. Management also alluded to positive developments in customer acquisition and new programmes going into FY24, particularly for automotive, artificial intelligence (AI), server, and smartphone-related products, as well as growing exposure amid a recovery among Chinese smartphone players.
- **Forecasts and ratings.** Post results, we trim FY23F earnings by 8.6% after factoring in lower loadings and margin assumptions. Our MYR2.98 TP is unchanged, based on 27x FY24F P/E (+1.5SD above the 5-year mean), with a 2% ESG discount baked into our TP. We believe a more meaningful recovery will be seen in the latter part of FY24 due to the current uncertainties in market sentiment, and as it will take some time to achieve optimal utilisation rates (amid high input costs) for its various expansions.
- **Downside/upside risks** to our call are slower/higher-than-expected orders, and favourable/unfavourable FX movement.

Forecasts and Valuation	Dec-21	Dec-22	Dec-23F	Dec-24F	Dec-25F
Total turnover (MYRm)	1,569	1,782	1,468	1,712	1,954
Recurring net profit (MYRm)	202	247	82	182	269
Recurring net profit growth (%)	34.8	22.3	(66.8)	121.4	47.9
Recurring P/E (x)	24.73	20.22	60.92	27.52	18.61
P/B (x)	2.3	2.1	2.1	2.1	1.9
P/CF (x)	22.29	15.96	13.45	13.44	10.51
Dividend Yield (%)	1.9	1.9	2.3	2.6	2.6
EV/EBITDA (x)	16.68	9.22	14.93	10.76	8.33
Return on average equity (%)	2.4	11.0	3.4	7.5	10.7
Net debt to equity (%)	net cash	net cash	net cash	net cash	net cash

Source: Company data, RHB

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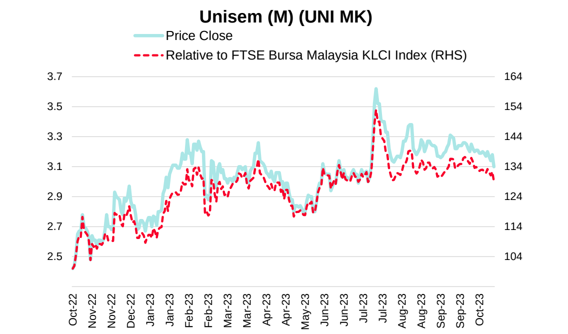
Share Performance (%)

	YTD	1m	3m	6m	12m
Absolute	12.3	(4.3)	(6.9)	3.3	28.1
Relative	16.0	(3.9)	(6.3)	1.4	29.1
52-wk Price low/high (MYR)					2.44 – 3.62



Source: Bloomberg

Overall ESG Score: 2.9 (out of 4)

E: GOOD
The group monitors and manage its greenhouse gas emission. Various key energy consumption reduction initiatives are performed at their sites. In terms of waste management, Unisem has a target of achieving 50% recycling rate of total scheduled waste generated. All of its sites comply to local environmental laws on e-waste handling and practices

S: GOOD
Unisem has a Safety and Health Policy in place to create a safe and conducive work environment for its employees. Health and safety training are provided to enhance employee safety awareness

G: GOOD
Unisem has applied and adopted majority of the best practices of the Malaysian Code on Corporate Governance. Nevertheless, we highlight that the CEO and Chairman position are held by the same person. Independent board members represents less than half of the board while women directors represents only 18% of women participation on the board (less than the 30% target)

Financial Exhibits

Asia
Malaysia
Technology
Unisem (M)
UNI MK
Neutral

Valuation basis

27x FY24F P/E

Key drivers

i. New contract wins;
ii. Higher loadings;
iii. Weaker MYR vs USD.

Key risks

i. Fluctuation in orders;
ii. Slower-than-expected smartphone sales;
iii. Stronger MYR vs USD.

Company Profile

Unisem is an OSAT player with plants in Ipoh, Perak, Malaysia and Chengdu, China. The company offers a suite of assembly and test services, such as wafer bumping, wafer probing, wafer grinding, a range of leadframe and substrate integrated circuits packaging, wafer level chipscale packaging (CSP), flipchip and radio frequency, analog, digital and mixed-signal testing services.

Financial summary (MYR)	Dec-21	Dec-22	Dec-23F	Dec-24F	Dec-25F
Recurring EPS	0.13	0.15	0.05	0.11	0.17
DPS	0.06	0.06	0.07	0.08	0.08
BVPS	1.34	1.50	1.48	1.51	1.60
Return on average equity (%)	2.4	11.0	3.4	7.5	10.7

Valuation metrics	Dec-21	Dec-22	Dec-23F	Dec-24F	Dec-25F
Recurring P/E (x)	24.73	20.22	60.92	27.52	18.61
P/B (x)	2.3	2.1	2.1	2.1	1.9
FCF Yield (%)	(5.2)	(5.6)	(0.6)	(0.6)	5.5
Dividend Yield (%)	1.9	1.9	2.3	2.6	2.6
EV/EBITDA (x)	16.68	9.22	14.93	10.76	8.33
EV/EBIT (x)	58.36	15.56	44.51	22.56	14.85

Income statement (MYRm)	Dec-21	Dec-22	Dec-23F	Dec-24F	Dec-25F
Total turnover	1,569	1,782	1,468	1,712	1,954
Gross profit	830	964	713	857	1,014
EBITDA	271	503	320	459	575
Depreciation and amortisation	(194)	(205)	(213)	(240)	(252)
Operating profit	77	298	107	219	323
Net interest	(2)	(5)	(9)	(10)	(10)
Pre-tax profit	71	289	99	209	312
Taxation	(24)	(36)	(17)	(27)	(44)
Reported net profit	47	253	82	182	269
Recurring net profit	202	247	82	182	269

Cash flow (MYRm)	Dec-21	Dec-22	Dec-23F	Dec-24F	Dec-25F
Change in working capital	(74)	(77)	77	(50)	(46)
Cash flow from operations	224	313	372	372	476
Capex	(483)	(595)	(400)	(400)	(200)
Cash flow from investing activities	(473)	(440)	(400)	(400)	(200)
Dividends paid	(64)	(97)	(113)	(129)	(129)
Cash flow from financing activities	121	(63)	(83)	(99)	(129)
Cash at beginning of period	664	656	556	445	318
Net change in cash	(127)	(189)	(111)	(127)	147
Ending balance cash	543	465	445	318	464

Balance sheet (MYRm)	Dec-21	Dec-22	Dec-23F	Dec-24F	Dec-25F
Total cash and equivalents	656	556	445	318	464
Tangible fixed assets	1,637	1,950	2,137	2,297	2,244
Total assets	2,783	3,019	3,026	3,135	3,306
Short-term debt	119	163	178	193	193
Total long-term debt	56	33	48	63	63
Total liabilities	617	602	640	696	728
Total equity	2,166	2,416	2,386	2,438	2,578
Total liabilities & equity	2,783	3,019	3,026	3,135	3,306

Key metrics	Dec-21	Dec-22	Dec-23F	Dec-24F	Dec-25F
Revenue growth (%)	21.7	13.6	(17.6)	16.6	14.1
Recurrent EPS growth (%)	34.8	22.3	(66.8)	121.4	47.9
Gross margin (%)	52.9	54.1	48.6	50.1	51.9
Operating EBITDA margin (%)	17.3	28.2	21.8	26.8	29.4
Net profit margin (%)	3.0	14.2	5.6	10.6	13.7
Dividend payout ratio (%)	207.4	38.3	137.6	71.0	48.0
Capex/sales (%)	30.8	33.4	27.2	23.4	10.2
Interest cover (x)	32.5	56.8	12.6	21.8	31.1

Source: Company data, RHB

Emissions And ESG

Trend analysis

Overall greenhouse gas (GHG) emissions increased 7% compared to the previous year due to higher utilisation and production activities. Nonetheless, GHG emissions intensity recorded a slight increase as production during the year involved more products requiring more sophisticated production methods and a higher amount of electricity.

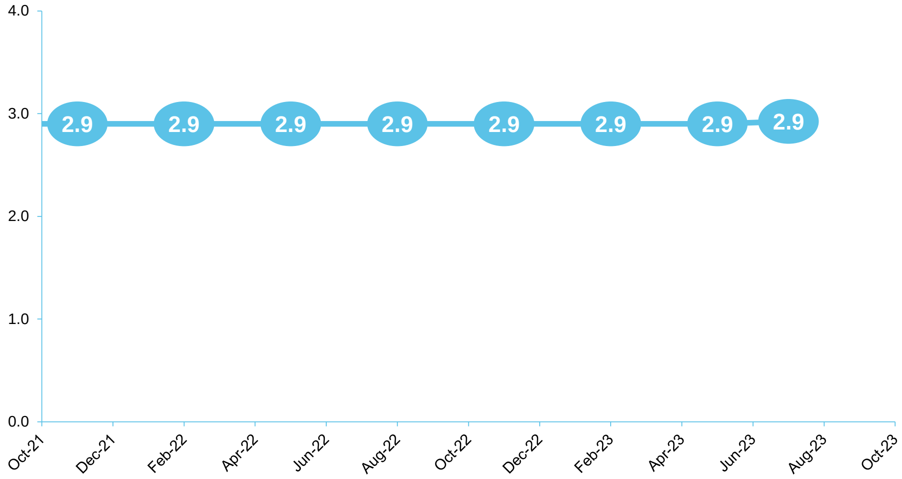
Emissions (tCO2e)	Dec-20	Dec-21	Dec-22
Scope 1	2	1	2
Scope 2	125	136	145
Scope 3	-	-	-
Total emissions	127	137	147

Source: Company data, RHB

Latest ESG-Related Developments

- Unisem re-entered the FTSE4Good Bursa Malaysia Index in Jun 2021, putting it among companies with leading ESG practices and which are in compliance with the best practice disclosures
- Its new Environmental Roadmap will chart the direction and environmental initiatives for the next few years up to 2025, which includes stepped-up targets to reduce energy intensity, GHG intensity, and water consumption intensity; targeting Green Building Certification for its new plants; and stepped-up target for non-hazardous waste recycling rates
- The group is exploring options to reduce reliance on fossil-based power and also looking into areas where it can take advantage of solar power generation at operating sites

ESG Rating History



Source: RHB

Results At a Glance

Figure 1: Results review

FYE Dec (MYRm)	3Q22	2Q23	3Q23	QoQ (%)	YoY (%)	9M22	9M23	YoY (%)	Comments
Revenue	**439.7**	**378.7**	**356.2**	**(5.9)**	**(19.0)**	**1,328.2**	**1,088.9**	**(18.0)**	Lower orders for all products amid prolonged softer market conditions
EBITDA	**118.6**	**81.2**	**83.2**	**2.5**	**(29.8)**	**362.7**	**234.6**	**(35.3)**	
EBITDA margin (%)	*27.0*	*21.4*	*23.4*			*27.3*	*21.5*		YoY: Loss of economies of scale, higher electricity and labour costs, cushioned by favourable FX
Depreciation & amortisation	(52.3)	(53.3)	(53.1)	0.3	(1.6)	(153.8)	(158.9)	(3.3)	
EBIT	**66.2**	**27.9**	**30.1**	**8.0**	**(54.6)**	**208.9**	**75.7**	**(63.8)**	
EBIT margin (%)	*15.1*	*7.4*	*8.5*			*15.7*	*7.0*		
Interest expense	(1.5)	(2.5)	(2.5)	(0.7)	(63.5)	(3.0)	(7.6)	(152.4)	
Interest income	-	-	-	Nm	Nm	-	-	Nm	
Associates	-	-	-	Nm	Nm	-	-	Nm	
EI/Others	(0.4)	3.9	(3.2)	(184.2)	651.4	(1.2)	(1.1)	(7.7)	FX gains/losses
Pretax profit	**64.3**	**29.2**	**24.3**	**(16.8)**	**(62.1)**	**204.7**	**67.0**	**(67.3)**	
Pretax Margin (%)	*14.6*	*7.7*	*6.8*			*15.4*	*6.2*		
Tax	(8.0)	(4.2)	(5.4)	(27.5)	32.5	(26.8)	(13.1)	51.1	
Effective tax rate (%)	*(12.4)*	*(14.4)*	*(22.1)*			*(13.1)*	*(19.6)*		
Minority Interest	-	-	-	Nm	Nm	-	-	Nm	
Net profit	**56.3**	**25.0**	**19.0**	**(24.2)**	**(66.3)**	**177.9**	**53.9**	**(69.7)**	
Core profit	**56.7**	**21.2**	**22.2**	**4.9**	**(60.9)**	**179.1**	**55.0**	**(69.3)**	Below expectations
Net Margin (%)	*12.9*	*5.6*	*6.2*			*13.5*	*5.1*		

Source: Company data, RHB

Recommendation Chart

Source: RHB, Bloomberg

Date	Recommendation	Target Price	Price
2023-07-28	Neutral	3.0	3.2
2023-04-28	Neutral	2.9	3.0
2023-02-24	Buy	3.8	3.1
2022-10-12	Buy	3.4	2.4
2022-07-29	Buy	4.2	3.0
2022-03-21	Buy	3.8	3.1
2022-02-28	Buy	4.6	2.9
2021-10-27	Buy	4.6	4.1
2021-08-01	Buy	10.0	4.2
2021-04-28	Buy	9.2	3.9
2021-02-26	Neutral	9.2	4.5
2020-10-25	Buy	5.5	2.2
2020-08-04	Buy	3.7	1.7
2020-04-30	Neutral	2.0	1.0
2020-04-03	Neutral	1.7	0.8

Source: RHB, Bloomberg

RHB Guide to Investment Ratings

Buy:	Share price may exceed 10% over the next 12 months
Trading Buy:	Share price may exceed 15% over the next 3 months, however longer-term outlook remains uncertain
Neutral:	Share price may fall within the range of +/- 10% over the next 12 months
Take Profit:	Target price has been attained. Look to accumulate at lower levels
Sell:	Share price may fall by more than 10% over the next 12 months
Not Rated:	Stock is not within regular research coverage

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