27 June 2024

Technology | Equipment

Pentamaster Corp (PENT MK)

Buy

Twin Growth Engines To Spur Growth; Initiate BUY

Target Price (Return):	MYR6.16 (+25%)
Price (Market Cap):	MYR4.93 (USD745m)
ESG score:	3.1 (out of 4)
Avg Daily Turnover (MYR/USD)	6.40m/1.36m

- **Initiate coverage with BUY and a TP of MYR6.16, 25% upside with 0.4% FY24F yield.** Our TP is pegged to 33x FY25F P/E (at +0.5SD from the 5-year mean) and includes a 2% premium, based on its ESG score of 3.1. We are optimistic about Pentamaster Corp's near-term earnings potential, driven by heightened demand in the factory automation solutions (FAS) segment and the recovery in the semiconductor space in the early upcycle, which should boost its automated test equipment (ATE) unit.
- **Automotive market revving back to life.** The automotive chip market is set to undergo exponential growth with power semiconductor devices like silicon carbide (SiC), gallium nitride (GaN) and insulated gate bipolar transistors (IGBT) being in high demand – given the advent of EVs. SEMI expects to see a 0.7% QoQ increase in capex spending in 2Q24 following declines of 17% YoY in 4Q23 and 11% in 1Q24. Several major semiconductor players are expected to continue investing in SiC manufacturing and fabrication facilities, due to the proliferation of such semiconductor material. Pentamaster's automated test and burn-in solutions for SiC- and GaN-related power modules should enable it to capitalise on this trend.
- **Further opportunity for FAS.** This segment is set to see structural demand growth, driven by the rising need for automation across various industries and the ongoing advancements of Industry 4.0. As businesses strive to enhance efficiency, reduce operational costs, and improve precision, the demand for automated solutions continues to rise. Currently, the medical industry is the main contributor to this division's growth – which Pentamaster intends to leverage on.
- **Semiconductor upcycle**. The semiconductor sector is poised for a robust recovery in 2H24 and into FY25, with the capex cycle showing signs of revitalisation. As per the latest World Semiconductor Trade Statistics (WSTS) forecast, the value of the global semiconductor market is projected to grow by 16% YoY in 2024 to USD611bn. This resurgence will be driven by increasing demand for advanced technologies such as 5G, artificial intelligence (AI) and EVs – as these require sophisticated semiconductor components. Additionally, it stands to benefit from US-China trade tensions, by becoming a strategic alternative supplier amid export restrictions, thereby enhancing its role in the industry's resurgence. Moreover, the National Semiconductor Strategy (NSS) will drive the long-term growth of Malaysia's semiconductor industry, benefiting companies like Pentamaster through enhanced investment and innovation.
- **We forecast a 3-year (FY24-26F) earnings CAGR of 18.2%,** mainly driven by the growth of the medical devices unit, coupled with the recovery of the automotive and semiconductor segments. The group has a healthy balance sheet and net cash of MYR490m (ie MYR0.69 per share) as of FY23. We ascribe 33x FY25F P/E (+0.5SD of its 5-year mean) and apply a 2% premium (based on its 3.1 ESG score) to its intrinsic value to derive our TP. Key downside risks include a slow replenishment of its orderbook and skilled labour shortages.

Forecasts and Valuation	Dec-22	Dec-23	Dec-24F	Dec-25F	Dec-26F
Total turnover (MYRm)	601	692	760	918	1,024
Recurring net profit (MYRm)	83	88	102	130	145
Recurring net profit growth (%)	13.5	6.2	15.9	28.3	11.0
Recurring P/E (x)	42.54	40.04	34.54	26.92	24.25
P/B (x)	5.6	5.0	4.5	3.9	3.4
P/CF (x)	92.90	16.34	20.44	19.35	15.66
Dividend Yield (%)	0.4	0.4	0.4	0.4	0.4
EV/EBITDA (x)	24.19	20.66	17.61	13.71	12.00
Return on average equity (%)	13.8	13.4	13.7	15.4	15.0
Net debt to equity (%)	net cash	net cash	net cash	net cash	net cash

Source: Company data, RHB

Analysts

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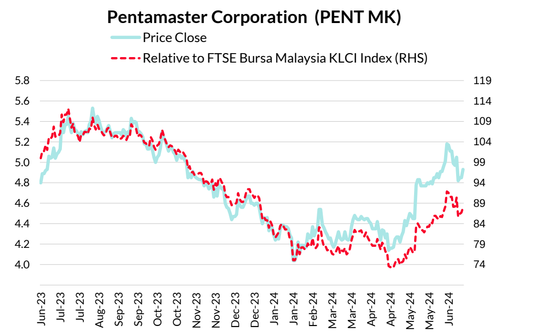
Share Performance (%)

	YTD	1m	3m	6m	12m
Absolute	7.2	3.4	10.8	7.2	4.0
Relative	(2.2)	5.2	7.4	(2.5)	(10.5)
52-wk Price low/high (MYR)					4.04 –5.53



Source: Bloomberg

Overall ESG Score: 3.1 (out of 4)

E: GOOD

The group is not involved in activities with a direct or significant impact on natural resources during its operations. To address potential climate change threats to communities, it has been steadily reducing its carbon footprint across its operations. The main source of greenhouse gas (GHG) emissions by the group is the consumption of electricity by its machinery.

S: GOOD

The company prioritises the well-being of employees who have significantly contributed to its growth. It has an open communication policy to maintain motivation, and encourages engagement across teams, levels, and departments.

G: EXCELLENT

Board characteristics are within the requirements stipulated by Bursa Malaysia, with half of it consisting of independent directors. There is 33% female representation on the Board. Pentamaster provides clear, timely and reliable information that is compliant with Malaysia's regulatory framework, and shareholder rights are well-protected.

Financial Exhibits

Asia
Malaysia
Equipment
Pentamaster Corp
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Buy

Valuation basis

33x FY25 P/E

Key drivers

i. Stronger orderbook growth;
ii. Recovery of the automotive sector;
iii. Semiconductor upcycle.

Key risks

i. Slow replenishment of orderbook;
ii. Skilled labour shortages.

Company Profile

Pentamaster provides integrated and customised solutions, serving customers across industries ranging from semiconductor, computer, automotive, electrical & electronics, pharmaceutical, medical devices, F&B, consumer electronics to general manufacturing.

Financial summary (MYR)	Dec-22	Dec-23	Dec-24F	Dec-25F	Dec-26F
Recurring EPS	0.12	0.12	0.14	0.18	0.20
DPS	0.02	0.02	0.02	0.02	0.02
BVPS	0.88	0.98	1.10	1.27	1.45
Return on average equity (%)	13.8	13.4	13.7	15.4	15.0

Valuation metrics	Dec-22	Dec-23	Dec-24F	Dec-25F	Dec-26F
Recurring P/E (x)	42.54	40.04	34.54	26.92	24.25
P/B (x)	5.6	5.0	4.5	3.9	3.4
FCF Yield (%)	(0.1)	3.2	2.0	2.9	5.0
Dividend Yield (%)	0.4	0.4	0.4	0.4	0.4
EV/EBITDA (x)	24.19	20.66	17.61	13.71	12.00
EV/EBIT (x)	26.24	23.25	20.37	15.82	13.90

Income statement (MYRm)	Dec-22	Dec-23	Dec-24F	Dec-25F	Dec-26F
Total turnover	601	692	760	918	1,024
Gross profit	183	207	232	294	328
EBITDA	137	159	187	239	266
Depreciation and amortisation	(11)	(18)	(25)	(32)	(36)
Operating profit	126	141	161	207	230
Net interest	7	0	0	0	0
Pre-tax profit	132	141	161	207	230
Taxation	(2)	(1)	(1)	(1)	(2)
Reported net profit	82	89	102	130	145
Recurring net profit	83	88	102	130	145

Cash flow (MYRm)	Dec-22	Dec-23	Dec-24F	Dec-25F	Dec-26F
Change in working capital	(108)	68	(13)	(54)	(39)
Cash flow from operations	38	215	172	181	224
Capex	(41)	(102)	(100)	(80)	(50)
Cash flow from investing activities	(47)	(117)	(100)	(80)	(50)
Dividends paid	(14)	(14)	(14)	(14)	(14)
Cash flow from financing activities	(53)	(32)	(14)	(14)	(14)
Cash at beginning of period	478	421	491	550	638
Net change in cash	(62)	66	58	87	160
Ending balance cash	418	488	548	637	798

Balance sheet (MYRm)	Dec-22	Dec-23	Dec-24F	Dec-25F	Dec-26F
Total cash and equivalents	421	491	550	638	800
Tangible fixed assets	170	282	357	405	419
Total investments	43	40	40	40	40
Total assets	1,158	1,318	1,474	1,701	1,940
Total liabilities	265	312	323	359	383
Total equity	893	1,006	1,152	1,343	1,557
Total liabilities & equity	1,158	1,318	1,474	1,701	1,940

Key metrics	Dec-22	Dec-23	Dec-24F	Dec-25F	Dec-26F
Revenue growth (%)	18.1	15.2	9.9	20.7	11.5
Recurrent EPS growth (%)	13.5	6.2	15.9	28.3	11.0
Gross margin (%)	30.5	30.0	30.5	32.0	32.0
Operating EBITDA margin (%)	22.8	23.0	24.5	26.0	26.0
Net profit margin (%)	13.7	12.9	13.4	14.2	14.1
Dividend payout ratio (%)	17.3	16.0	14.0	10.9	9.8
Capex/sales (%)	6.8	14.8	13.2	8.7	4.9
Interest cover (x)	1,449				

Source: Company data, RHB

Valuation & Recommendation

We initiate coverage on Pentamaster with a BUY call. Our TP of MYR6.16 is premised on 33x FY25F P/E, which is at +0.5SD from its 5-year mean, as we believe both its major contributing segments are set to supercharge its growth. Our TP also includes a 2% ESG premium applied to its intrinsic value, based on our ESG score of 3.1. Peers identified are within the ATE and FAS segments. Our valuation is broadly in line with that of local players in this space, which are trading at 16-38x FY25F P/Es. Given its larger market cap vs peers like QES Group, ECA Integrated Solution, and Genetec Technology, our valuation is above the sector-weighted average of 29x. Additionally, the group is forecasted to achieve comparable FY24 and higher FY25 earnings growth against the weighted average, mainly due to its expanding exposure in the growing medical technology (medtech) segment.

We are optimistic about Pentamaster's near-term earnings growth, driven by increased demand in the medical sector, which is strengthening the group's FAS segment. Pentamaster's strategic expansion into the medical sector is timely – this provides it with a significant new revenue stream and helps to mitigate effects of the cyclical nature of the semiconductor market. Additionally, the new semiconductor sector upcycle – fueled by the rise of high-performance semiconductor devices for generative AI, upticks seen in the consumer electronic market, along with the recovery of the automotive markets – should further enhance the group's earnings growth.

Figure 1: Pentamaster's 5-year P/E band

Source: Bloomberg, RHB

Figure 2: Peer comparison

Company Name	Country	Market Cap	P/E (x)		P/BV (x)		EPS Growth (%)		ROE (%)		EV/EBITDA		Div. Yield (%)
		(USDbn)	FY24	FY25	FY24	FY25	FY24	FY25	FY24	FY25	FY24	FY25	FY24
Pentamaster	MY	0.7	33.8	27.2	4.5	3.9	19.5	24.3	14.1	15.4	17.3	13.8	0.4
Local													
ViTrox Corp	MY	1.7	47.8	37.6	7.4	6.4	27.0	12.4	16.2	18.1	33.4	29.1	0.7
MI Technovation	MY	0.5	29.8	25.9	2.1	2.0	15.1	19.2	6.6	7.5	15.3	13.4	1.7
QES Group	MY	0.1	28.3	19.3	3.7	2.5	46.2	-5.3	10.3	16.1	na	na	na
Greatech Technology	MY	1.4	33.0	28.1	7.1	5.7	17.6	10.2	23.3	21.9	23.0	20.4	0.0
ECA Integrated Solution	MY	0.1	42.3	29.1	4.7	4.7	45.5	12.5	9.2	11.9	na	na	0.0
Genetec Technology	MY	0.4	18.2	16.3	3.6	3.0	11.5	24.1	22.6	20.2	12.6	10.7	na
Weighted Average			**35.1**	**28.6**	**5.8**	**4.9**	**20.6**	**12.2**	**16.7**	**17.2**	**23.0**	**20.1**	**0.4**
International													
Tokyo Electron	JP	104.6	35.1	27.0	8.3	7.2	30.1	21.0	25.2	29.2	18.7	16.5	1.9
Advantest Corp	JP	26.1	44.2	28.5	8.6	7.5	54.8	18.9	21.2	30.0	19.2	16.1	1.2
Koh Young Technology	KR	0.7	28.4	19.8	2.7	2.4	43.4	57.5	9.8	13.1	14.0	12.8	1.2
Chroma ATE	TW	3.8	24.7	20.6	5.1	4.6	19.6	11.3	20.7	23.6	15.3	13.6	3.2
Applied Materials	US	183.6	26.3	22.8	9.9	8.7	15.3	12.6	39.5	39.4	19.1	17.3	0.7
Lam Research Corp	US	125.9	32.4	26.5	15.4	13.4	22.2	26.5	47.3	51.4	21.8	17.9	0.9
KLA Corp	US	103.5	32.9	26.8	30.3	23.8	22.9	16.4	99.1	93.8	21.6	18.8	0.8
Emerson Electric Co	US	61.8	19.8	18.1	2.7	2.6	9.3	7.0	11.6	15.0	15.3	14.4	2.0
Teradyne	US	22.0	45.4	29.2	8.5	7.7	55.6	32.1	19.2	27.5	21.7	17.1	0.4
Veeco Instruments	US	2.4	24.8	21.1	3.6	3.1	17.6	-25.0	13.1	11.5	15.9	15.4	0.0
Cohu	US	1.5	161.1	21.6	1.6	1.6	647.4	na	-3.1	4.2	12.1	8.1	0.0
ASML Holding	NL	404.9	50.2	31.8	24.6	20.1	57.9	14.7	50.5	65.7	25.8	23.0	0.9
BE Semiconductor Industries	NL	12.9	54.0	32.8	24.6	19.7	64.8	36.1	48.0	66.4	25.5	19.5	2.7
Camtek	IL	4.9	42.6	36.4	9.2	7.7	17.3	23.0	25.4	25.2	30.7	na	na
Weighted Average			**38.7**	**27.6**	**17.7**	**14.6**	**37.6**	**16.7**	**46.3**	**53.3**	**22.1**	**19.3**	**1.0**

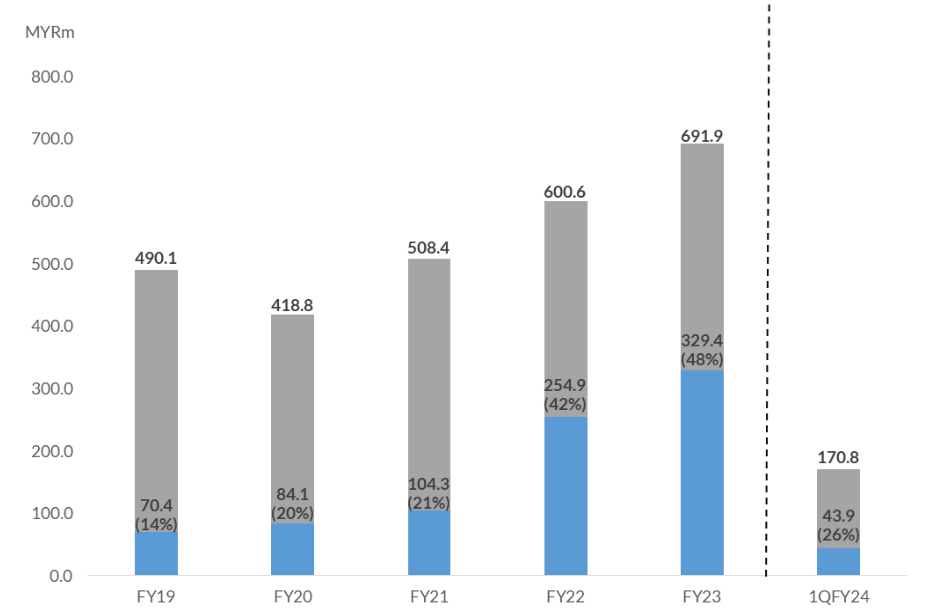
Source: Bloomberg, RHB

Investment Thesis

Automotive market revving back to life

Although there has been a recent deceleration in EV demand, the underlying trends supporting the automotive component market – including the shift towards more technologically advanced and electronically sophisticated vehicles – are indicative of a robust and eventual resurgence in semiconductor demand within the automotive industry. This bodes well for Pentamaster, as the automotive sector has been a main contributor to the group's revenue over the past two years (2020: 20%, 2021: 42%, 2023: 48%.)

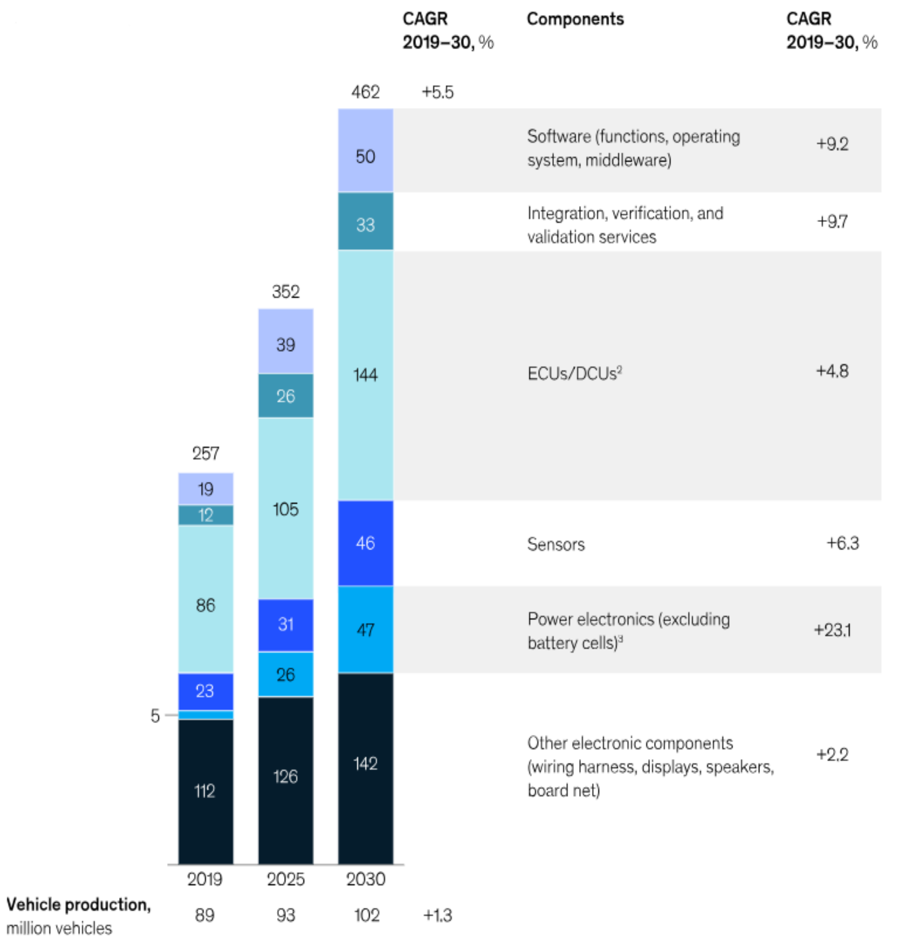
Figure 3: Pentamaster's FY19-1QFY24 automotive revenue vs total revenue



Source: Company data, RHB

As reported by McKinsey, passenger car and light commercial vehicle (LCV) unit sales are forecasted to increase modestly from 89m vehicles in 2019 to 102m in 2030, translating to a CAGR of just over 1%. However, the market for automotive software and electronics is expected to quadruple that pace during the same timeframe. The electronic control unit (ECU) and domain control unit (DCU) segment, which will account for the largest market share, is anticipated to hit USD144bn by 2030. Software development – encompassing integration, verification, and validation – will comprise the second-largest market share, with projected revenues reaching USD83bn by 2030. Power electronics will see the most rapid growth, driven by EV adoption, with an expected CAGR of 23% through 2030. Additionally, the sensor market, propelled by advancements in Autonomous Driving (AD) and Advanced Driver Assistance Systems (ADAS), is estimated to expand at a 6% CAGR.

Figure 4: Automotive software and E&E market (USDbn)

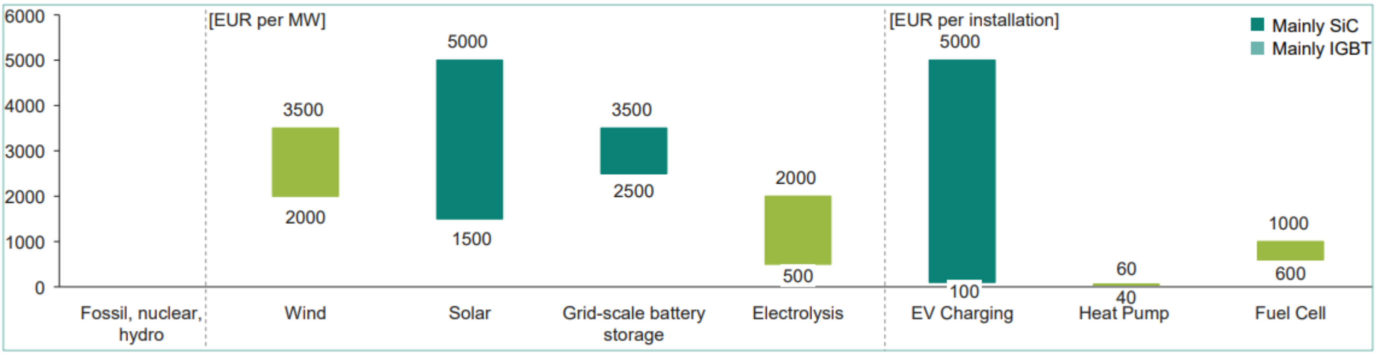


Source: McKinsey & Co

The demand for advanced power semiconductor devices such as IGBT, SiC, and GaN is surging, driven primarily by the rapid growth of the EV market. IGBTs are valued for their high efficiency and fast switching capabilities, making them essential for power conversion in EV inverters and other automotive applications. SiC devices, which offer superior electric field strength, higher thermal conductivity, and greater efficiency compared to traditional silicon-based semiconductors, are increasingly being adopted for their ability to handle higher voltages and temperatures – which is crucial for EV powertrains and charging infrastructure. Similarly, GaN technology, known for its high electron mobility and efficiency at high frequencies, is gaining traction in EV applications, particularly in fast-charging systems and power management.

As the EV industry continues to expand, the need for these advanced materials to improve performance, reduce energy loss, and enhance the overall efficiency of EVs is driving significant growth in the demand for IGBT, SiC and GaN-based components. Beyond EVs, SiC and IGBT are finding increasing applications across various industries. SiC is becoming crucial in RE systems such as solar inverters and wind turbines, enhancing energy conversion and reducing losses. IGBTs are widely used in industrial motor drives, home appliances, and power supply units, where they contribute to energy savings and improved performance. As technology advances and the demand for energy-efficient solutions grows, the adoption of SiC and IGBT in these diverse applications continues to expand.

Figure 5: Power semiconductor content by application



Additions in 2022[1)]	74 [GW]	220 [GW]	12 [GW]	<1 [GW]	~6m [inst.]	22m [inst.]	5k [inst.]
CAGR 2023 – 30	16%	23%	56%	92%[2)]	31%	16%	42%

Note: 1) IEA: World Energy Outlook, Oct 2023; sector-tracking reports as of Oct 2023; internal analysis
2) Based on 270 GW pipeline (midpoint), >100% based on NZE requirements of 560GW
Source: Infineon Technologies

Wolfspeed, a global SiC manufacturer, has committed to a capital expenditure of USD6.5bn up to 2027. This investment will be used to expand the world's first 200mm SiC fabrication facility in Mohawk Valley and to set up a second 200mm fabrication facility in Saarland, Germany. Similarly, Infineon is ramping up its SiC 200mm volume production in Villach and Kulim. Infineon's capex forecast of EUR2.9bn for FY24 will primarily focus on completing Phase 1 of the third manufacturing module at the Kulim site in Malaysia, which is intended for compound semiconductor production, as well as commencing Phase 2. Meanwhile, significant funds are also allocated to machinery for manufacturing SiC and GaN-based products.

To expand its semiconductor business into SiC chip manufacturing, Bosch acquired TSI Semiconductors which currently focuses on developing and producing high volumes of chips on 200mm silicon wafers for sectors such as mobility, telecommunications, energy, and life sciences. Over the next few years, Bosch plans to invest over USD1.5bn to transform TSI's Roseville site into a facility for SiC processes, with the aim to start producing chips on 200mm wafers by 2026. By the end of 2030, Bosch intends to significantly expand its global SiC chip portfolio to meet the soaring demand driven by the growth of electro-mobility. Given that Pentamaster's main proprietary product is the burn-in wafer for SiC and as it is one of the top four manufacturers, it is strategically placed to capitalise on this demand.

Although there has been a recent deceleration in EV demand, the underlying trends supporting the automotive component market, including the shift towards more technologically advanced and electronically sophisticated vehicles, indicate a robust and eventual resurgence in semiconductor demand within the automotive industry.

Into the new semiconductor upcycle

The semiconductor industry is undergoing a rebound following a slowdown in 2023, driven by increased demand for chips across various sectors. The WSTS projects a 16% YoY growth in the global semiconductor market for 2024, with the market valued at USD611bn. WSTS is expecting a stronger performance in 2H24, especially in the computing end-markets. The increase will be primarily driven by the memory sector, which is anticipated to surge by 76.8%, followed by a 10.7% increase in the logic component. These gains will offset the single-digit declines projected in other categories such as discrete, optoelectronics, sensors, and analogue semiconductors. For 2025, WSTS forecasts a 12.5% growth, bringing the market to an estimated valuation of USD687bn. Similarly, this growth is expected to be primarily fueled by the memory and logic sectors, while all other segments are anticipated to record single-digit growth rates. Pentamaster, with its expertise in automation and robotics, is poised to capitalise on this trend by offering advanced solutions to semiconductor manufacturers.

Increased demand for automation solutions. As semiconductor companies scale up production, there is a growing need for automation solutions to improve efficiency, throughput, and quality control. Pentamaster, with its expertise in automation and robotics, can offer cutting-edge solutions to facilitate these technology upgrades, establishing the company as a crucial partner for semiconductor manufacturers.

Beneficiary of the US-China chip war. Pentamaster is strategically positioned to benefit from the ramp-up in US-China tensions in the semiconductor sector. As the US faces export restrictions to China, Pentamaster has emerged as a strategic alternative supplier in this high-stakes chip warfare, potentially capitalising on the growing technological investment needs of these economic giants. The semiconductor industry's rebound presents significant opportunities for Pentamaster, a leading provider of automation solutions. This report outlines the ways in which Pentamaster stands to benefit from the resurgence in the semiconductor market.

National Semiconductor Strategy (NSS) a long-term positive. Malaysia's NSS is a comprehensive plan designed to enhance the country's semiconductor industry, which is crucial for its economic growth and technological advancement. The strategy aims to strengthen the semiconductor ecosystem, attracting significant domestic and foreign investments to boost R&D and production. For instance, Malaysia aims to increase its semiconductor market share from 7% to 13% by 2030.

The NSS is structured in three progressive phases to transform Malaysia into a major global player in semiconductor technology. Phase 1 focuses on leveraging existing industry capacity to modernise OSATs with advanced packaging, expanding current fabrications, attracting FDI to boost capacity in trailing-edge chips, particularly power chips, and developing local chip design champions. Phase 2 aims to pursue cutting-edge logic and memory chip design, fabrication, and testing, integrating chip purchasers into the ecosystem, thereby attracting leading advanced chip manufacturers. Phase 3 continues to support the development of world-class Malaysian firms in semiconductor design, advanced packaging, and manufacturing equipment while attracting top global companies like Apple, Huawei, and Lenovo for advanced manufacturing in Malaysia. The NSS will remain a flexible, evolving document, with a steadfast goal of positioning Malaysia as a leader in accessible technology. Key targets include securing at least MYR500bn in investments during Phase 1, establishing at least 10 Malaysian companies with revenues of MYR1-4.7bn by Phase 2, developing Malaysia as a global R&D hub, training and upskilling 60,000 high-skilled engineers, and allocating at least MYR25bn in fiscal support, with detailed incentives to be announced by the Ministry of Investment, Trade and Industry.

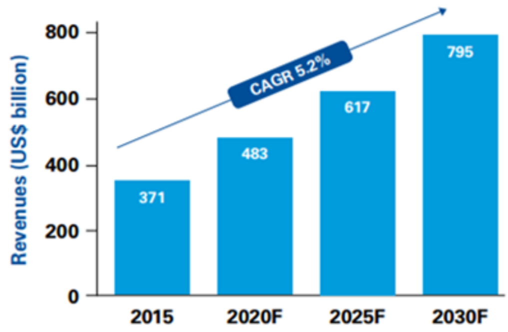
By fostering international partnerships and establishing favourable policies, Malaysia seeks to integrate itself into the global semiconductor value chain. Pentamaster, a key player in semiconductor testing and automation solutions, stands to benefit significantly from this strategy. With the increased focus on semiconductor production and innovation, Pentamaster can expand its market presence, drive growth, and capitalise on the rising demand for advanced semiconductor testing technologies.

Medical expansion: Focused growth and market potential

In 2019, as a strategic move to diversify its offerings, Pentamaster acquired TP Concept. While TP Concept focused on insulation displacement connection (IDC) machines, acquiring the company gives Pentamaster a foothold in the medical device industry. To solidify this commitment, Pentamaster MediQ was established as a subsidiary specifically dedicated to medical product manufacturing in 2020. Anticipating significant growth in this segment, Pentamaster is undertaking a major infrastructure expansion – a third plant (c.720k sq ft, which is about three times the size of its current facilities), currently under construction in Batu Kawan, is expected to be completed in 1Q25. The production lines and cleanroom facilities focusing on medical devices under the FAS segment will utilise c.80% of the space. In the meantime, the remaining c.20% will be used for R&D, administration, and warehousing. Capex of MYR300m has been designated for the construction of the facility, with MYR150m to be distributed across FY24 and FY25.

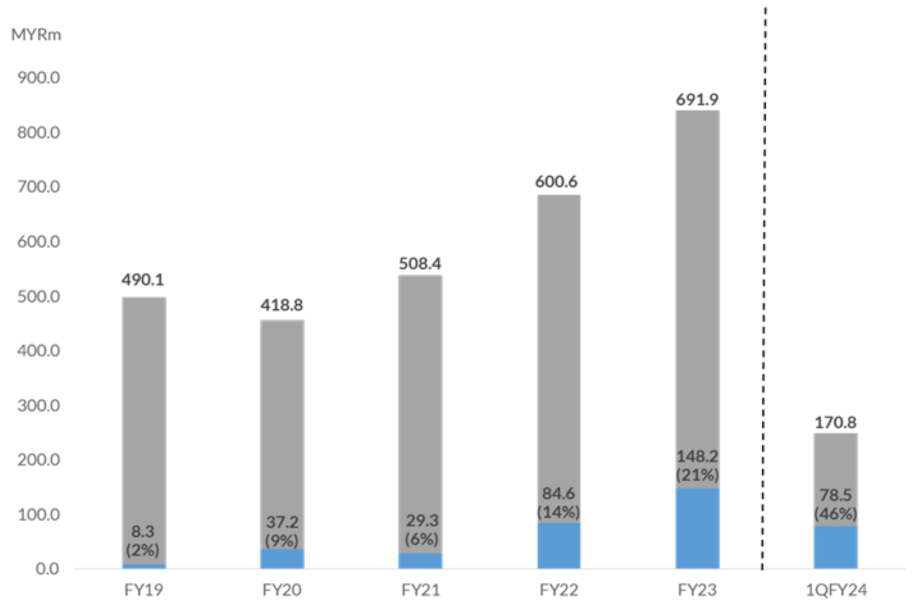
Against the backdrop of a growing need for inventive new devices and services as lifestyle-related illnesses become more widespread, KPMG forecasted the medical devices market to record a CAGR of 5.2% over 2015-2030, valuing the market at MYR795bn by 2030. As such, this provides tremendous market opportunities for Pentamaster's FAS segment to further position itself for a market size that could be worth billions of dollars (in USD terms) – which the group is well-prepared for with its ongoing infrastructure expansion. As a testament of the expanding market, the company saw an increase in revenue contributions from medical devices, surging to MYR148.2m in FY23 from MYR8.3m in FY19, indicating a 5-year revenue CAGR of 78%.

Figure 6: Global medical device sales – forecasted to 2030



Source: KPMG Medical Devices 2030 report

Figure 7: Pentamaster's FY19-1QFY24 medical devices revenue against total revenue



Source: Company data, RHB

This is also in line with Malaysia increasing its focus on the medtech sector as a key driver of economic growth and innovation. Recognising the potential of medtech to improve healthcare outcomes and create high-value jobs, the Government has implemented various initiatives to bolster this industry. These efforts include the establishment of specialised medical device parks, incentives for R&D, and collaborating with global medtech companies to foster technology transfer and skill development. The emphasis on medtech supports Malaysia's broader economic goals of diversifying its industrial base and advancing its position in the global value chain.

FAS division to grow from strength to strength

The group saw significant growth for its FAS segment, mainly driven by substantial contributions from the medical devices industry. FAS accounted for 66.3% of revenue in 4Q23, vs 62.7% in 4Q22. Moving ahead, Pentamaster expects the demand for its Automated Robotic Manufacturing System (i-ARMS) factory automation solutions from the medical device segment to continue expanding in 2024. This anticipation stems from customers' plans to expand production capacity, necessitating additional manufacturing automation lines. Beyond medical devices, the group’s i-ARMS for FAS is beginning to penetrate the food and beverage and automotive sectors. This expansion across segments is expected to aid growth in the FAS division, with Pentamaster projecting the segment's contribution to reach 40% of group revenue in the near term.

Financial Overview

Results review

Pentamaster's 1Q24 revenue increased marginally by 3.3% YoY on stronger sales from the FAS division. However, core net profit fell by 41% YoY as a result of higher depreciation expenses and higher administrative cost on bonus payouts.

The ATE division's 1Q24 revenue plunged by 34% YoY, however. This decline was due to a 51% YoY decrease in revenue from the automotive segment, reflecting the overall weak demand of the market – driven by shifting consumer demands and the lack of transparency surrounding subsidies for the EV markets globally. However, the decline was partially offset by segmental sales growth in electro-optical operations (+48% YoY). As the automotive segment accounts for 60.3% of ATE division's revenue, the unit booked a 34.3% decrease for the same metric.

The FAS division's 1Q24 revenue rose 69% YoY following stronger demand from the medical devices segment and higher orders for i-ARMS. QoQ, 1Q24 core net profit declined by 27% to MYR17mil due to the aforementioned higher administrative cost as well as R&D cost for the single-use medical device segment.

Figure 8: 1Q24 results

FYE (MYRm)	1Q23	4Q23	1Q24	QoQ (%)	YoY (%)
Revenue	**165.3**	**169.0**	**170.8**	**1.1**	**3.3**
Gross Profit	**46.7**	**53.4**	**49.5**	**(7.3)**	**6.0**
GP margin (%)	*28.3*	*31.6*	*29.0*		
Adjusted EBITDA	**36.8**	**35.8**	**31.0**	**(13.4)**	**(15.7)**
Adjusted EBITDA margin (%)	*22.2*	*21.1*	*18.2*		
Depreciation	(3.5)	(4.5)	(5.1)	13.3	45.7
Adjusted EBIT	**33.3**	**31.3**	**31.0**	**(1.0)**	**(6.7)**
EI/Others	(7.6)	(2.6)	2.3	nm	nm
Reported PBT	**34.3**	**31.3**	**30.8**	**(1.6)**	**(10.2)**
Tax	(0.6)	1.6	(0.5)	nm	21.2
Effective tax rate (%)	*1.9*	*(5.2)*	*1.6*		
Minority Interest	(12.4)	(12.2)	(10.9)	(10.7)	(11.9)
Net Profit	**21.3**	**20.7**	**19.4**	**(6.4)**	**(8.9)**
Core Profit	**28.9**	**23.3**	**17.1**	**(26.7)**	**(40.8)**
Core net margin (%)	*17.5*	*13.8*	*10.0*		

Source: Company data, RHB

Figure 9: 1Q24 breakdown by segment

FYE (MYRm)	1Q23	4Q23	1Q24	QoQ (%)	YoY (%)
Revenue					
ATE	111.4	94.0	73.2	(22.2)	(34.3)
FAS	58.3	78.7	98.8	*25.5*	69.4
PBT profit					
ATE	*27.8*	*19.0*	*11.6*	*(38.7)*	(58.1)
FAS	8.8	18.3	23.6	28.7	>100
PBT margin					
ATE	*25.0*	*20.2*	*16.0*		
FAS	*16.3*	*23.3*	*24.1*		

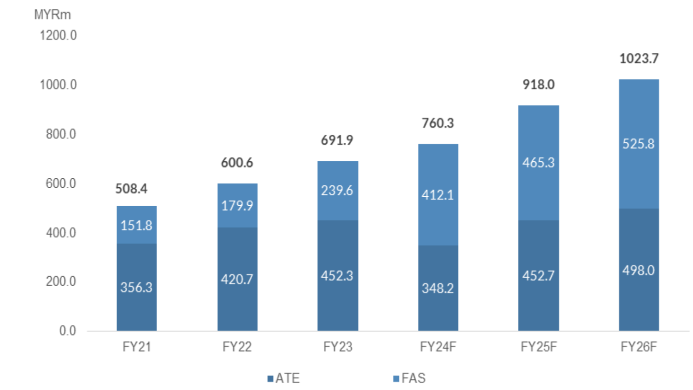
Source: Company data, RHB

Stronger earnings growth in FY24-26

We expect a stronger FY24, driven by the demand for medical automation solutions – this segment is expected to contribute 30-35% of revenue. Hence, we project the FAS segment to surpass ATE for the year. This balances the softer automotive outlook as customers scale back on capex spending, leading to a 12.5% QoQ decline in its orderbook. Consequently, we expect the automotive segment's revenue contribution to fall to around 30% for FY24. While the electro-optical segment had a higher contribution in 1Q24, this was primarily due to the delivery of its flagship test equipment. Therefore, we still anticipate a 10% contribution from this segment. For the semiconductor unit, we expect a recovery in 2H and its contribution to remain at 15% of total revenue, while the consumer products segment is expected to continue its soft trend, with a single-digit to 10% contribution to FY24's revenue.

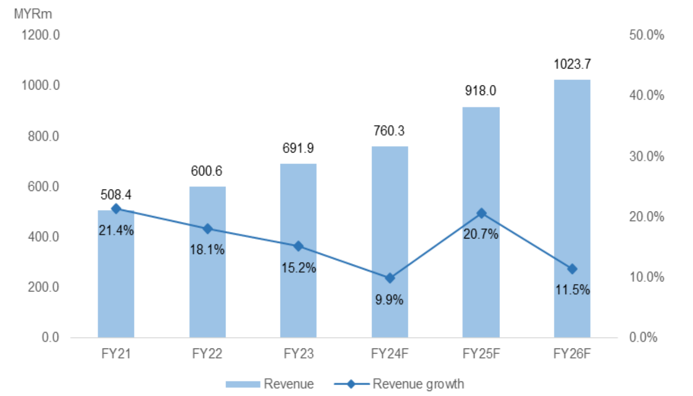
We anticipate better contributions from the ATE segment in FY25-26 as the automotive industry is expected to gain momentum in 2H24, driven by the ongoing global shift towards EVs. Additionally, the group's recent expansion into Germany in 2023 will enhance its presence in the European automotive market alongside the medtech segment. We also expect better semiconductor contributions from the emergence of high semiconductor devices for generative AI and data centres. Furthermore, we foresee a continuously growing contribution as the group aims to capitalise on the rising opportunities in the widespread adoption of automation in medical manufacturing and single-use medical devices. With a projected GP margin of 30-32%, largely driven by higher-margin products in the medical devices segment, we arrive at 3-year earnings CAGR of 18.2%.

Figure 10: Revenue breakdown by segment



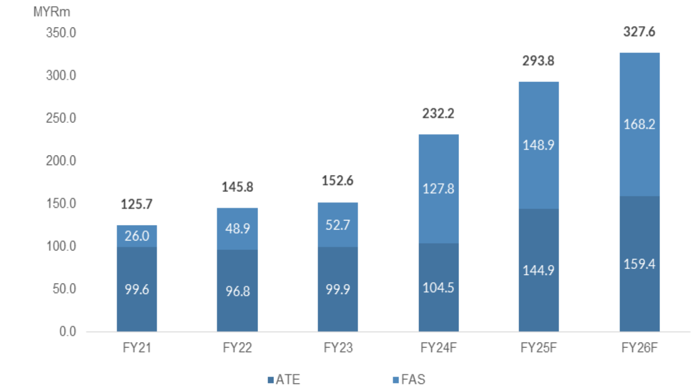
Source: Company data, RHB

Figure 11: Revenue trend



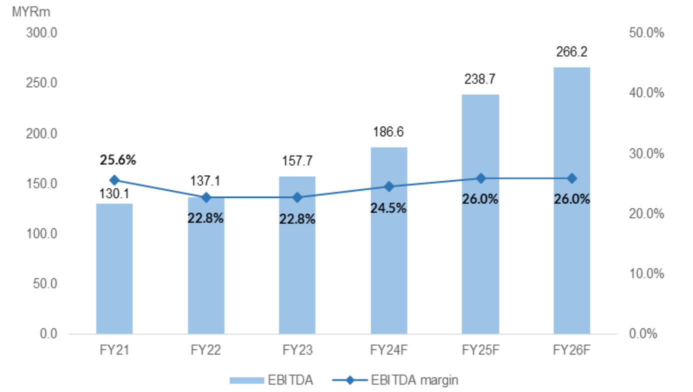
Source: Company data, RHB

Figure 12: EBIT breakdown by segment



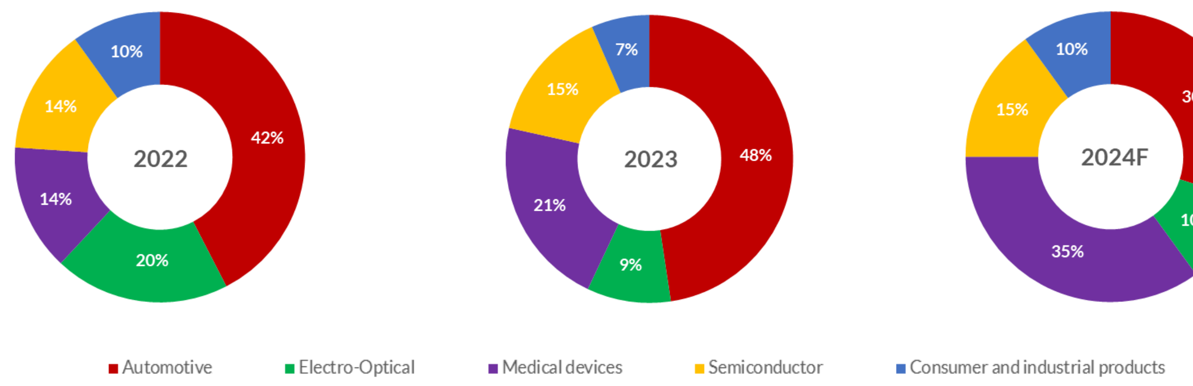
Source: Company data, RHB

Figure 13: EBITDA trend



Source: Company data, RHB

Figure 14: 2022-2024F revenue breakdown by industry

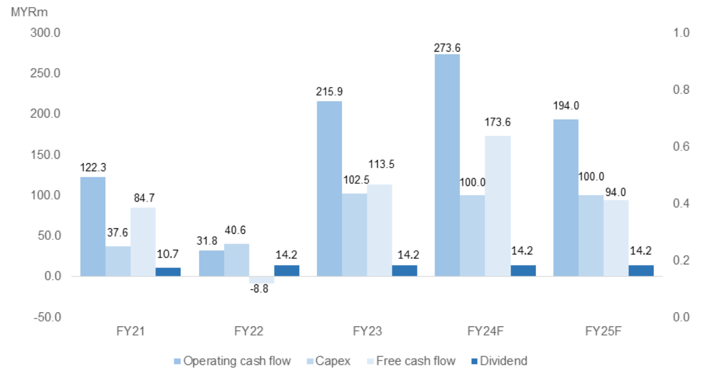


Source: *Company data, RHB*

Healthy balance sheet

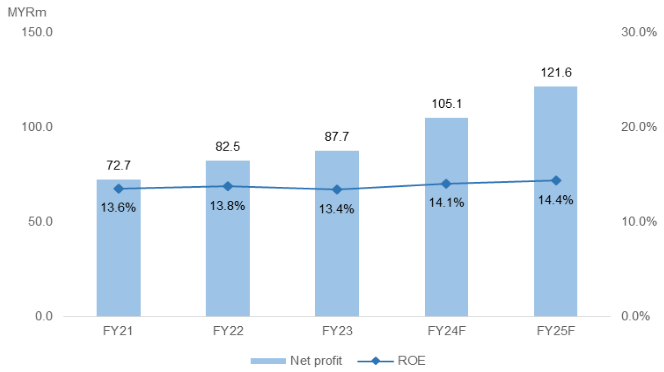
As of FY23, Pentamaster maintains a robust financial position, boasting a net cash balance of MYR490.9m. During the previous year, the group cleared its term loan outstanding balance, which was utilised to partially fund the acquisition of leasehold land for its second production facility in Batu Kawan, Penang. This repayment resulted in the group being debt-free. Despite the slight decline in ROAE to 13.4% in FY23 from 13.8% in FY22, primarily due to a decrease in net margin, it is anticipated that ROAE will rebound in subsequent quarters – driven by heightened orders from the FAS segment.

Figure 15: Cash flow



Source: *Company data, RHB*

Figure 16: ROE improvement from margin recovery



Source: *Company data, RHB*

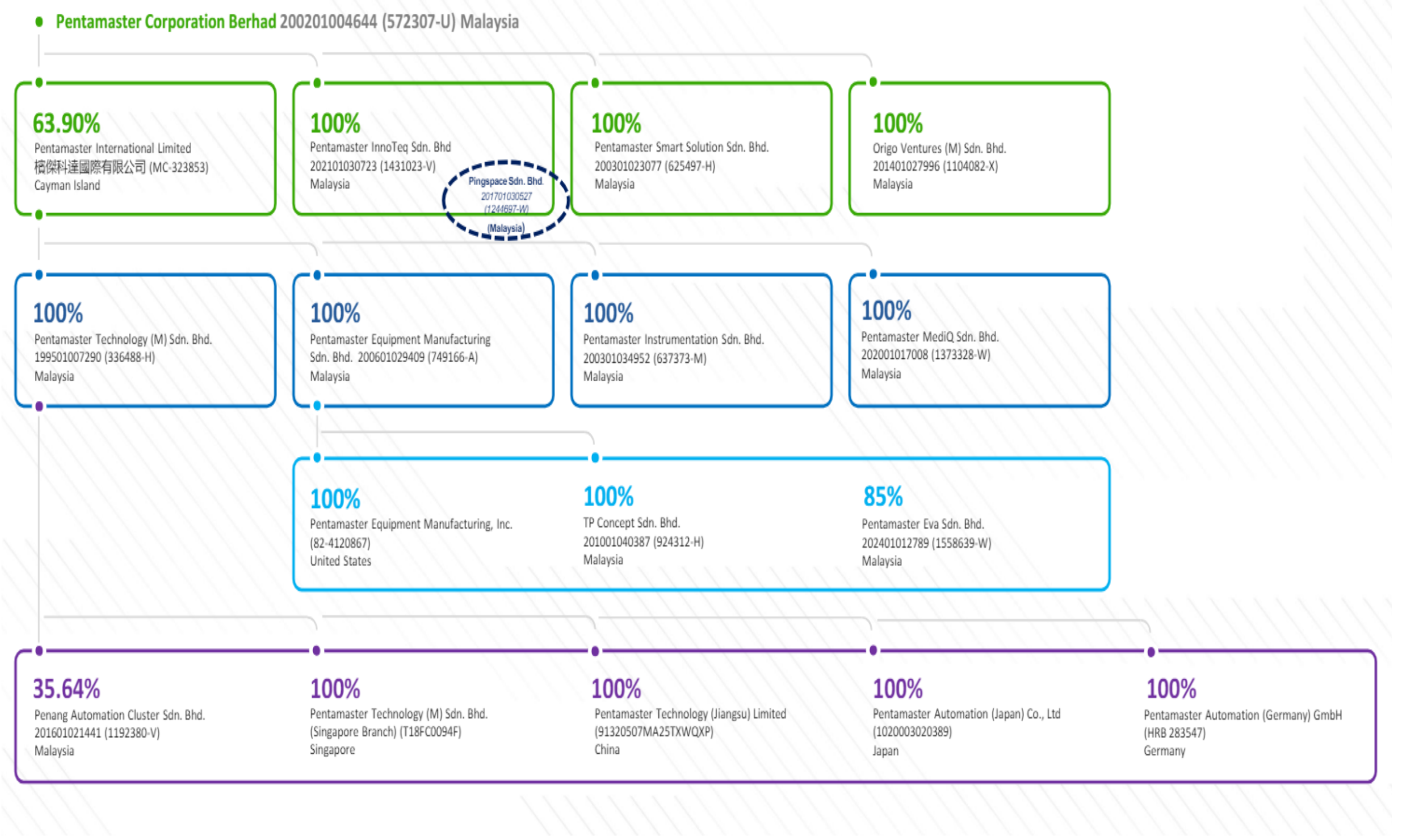
Company Overview

Background

Pentamaster, based in Penang, Malaysia, is a prominent player in automation and technology solutions. With over 30 years of expertise in delivering integrated and customised solutions, the group serves a diverse range of global industry sectors. These sectors encompass semiconductors, consumer electronics, automotive, E&E, medical devices, F&B, consumer electronics, and general manufacturing.

Founded in 1991 with a focus on vision inspection solutions, Pentamaster has grown, establishing itself as a global provider of advanced automation systems and. In 2018, its subsidiary, Pentamaster International (PIL), was listed on the HKEX. This strategic move allows Pentamaster to expand its presence in the Greater China market and leverage its international listing status.

Figure 17: Pentamaster's corporate structure



Source: Company data

Geographical diversification. Pentamaster has strategically broadened its geographical presence with the aim of fostering greater self-reliance in the semiconductor and electronics supply chain. In 2023, the group expanded its footprint to Germany. This positions it to enhance its presence in Europe to further build its automotive and medtech segments in this region. Other countries where the group has a presence in include China, Japan, Indonesia, and the US, amongst others. This move aims to diversify its customer base and sustain growth across its different business segments, enabling the company to effectively navigate and capitalise on the evolving dynamics of the global economy.

Business overview

Pentamaster's operations are broadly categorised into two key business segments.

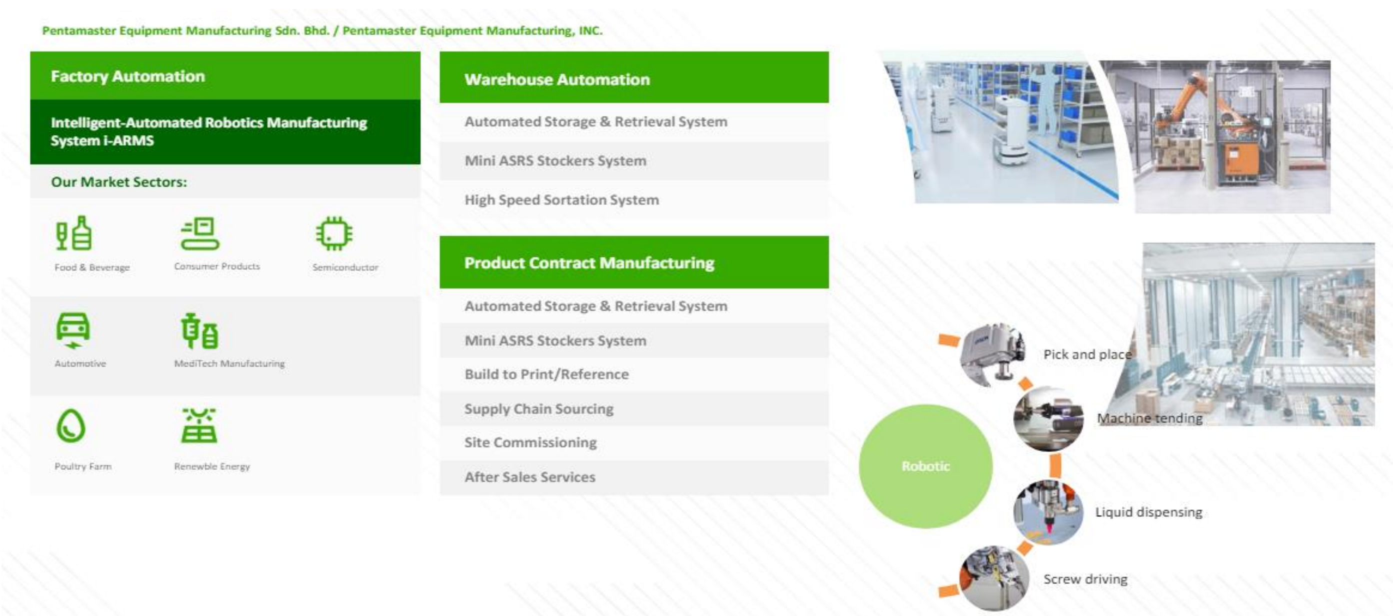
i. Automated test equipment (ATE): Designing, development and manufacturing of standard and non-standard automated equipment. The ATE segment primarily serves the automotive industry and has done so for the past two financial years.

Figure 18: Pentamaster's ATE segment business model

Source: Company data

ii. Factory automation solutions (FAS): Designing, development and installation of integrated factory automation solutions. The medical devices business is the major contributor of the segment, and also its main growth driver.

Figure 19: Pentamaster's FAS segment business model



Source: Company data

Board of Directors

Chuah Choon Bin, Executive Chairman. He is a co-founder of Pentamaster and has been with the company since 2002. He currently sits on the Board of PIL as the Executive Director and Chairman. PIL is a subsidiary of the company and was listed on the Main Board of HKEX on 19 Jan 2018. Chuah also holds directorships in subsidiary companies of the group. He has extensive experience in automation engineering, having previously worked for major technology firms, and has been instrumental in growing Pentamaster from a simple automation provider to a high-technology group offering factory automation equipment and systems and ICT solutions to industrial and commercial customers.

Gan Pei Joo, Executive Director. She is also the CFO and oversees the overall management, corporate affairs, finance, treasury, control functions and budgeting of the group, She also holds directorships in all the subsidiaries of the group.

Lee Kean Cheong, Independent Non-Executive Director. Lee began his career at Ernst & Young before transitioning to senior managerial roles in the commercial sector, gaining over 20 years of experience in finance and commerce. Presently, he is a partner in an accounting firm and a director of a management consultancy firm. He also serves as an independent non-executive director for SLP Resources and MSM International, both listed companies.

Roslinda Binti Ahmad, Independent Non-Executive Director. She is recognised for her expertise in Islamic investment banking and currently holds the position of Head of Islamic Products & Services at Crowd Sense. She also works as a strategic consultant for an Islamic financial training provider.

Leng Kean Yong, Non-Independent Non-Executive Director. He is also a Non-Executive Director at PIL. With over 20 years of experience in finance and marketing, Leng specialises in business strategy, including financial matters, business planning, and marketing. He has successfully executed projects for various companies, from SMEs to multinational corporations, across different stock exchanges. Leng is also a Director at Crowd Sense.

Dato' Loh Nam Hooi, Non-Independent Non-Executive Director. He previously served as a board member of the Penang Water Authority from 1997 to 1999, and as a Director of Kwong Wah Yit Poh Press in 1996. Additionally, Loh sits on the boards of several private companies.

Key senior management team

Hon Tuck Weng, Operations Director. He has served as the operations director since May 2007, and is currently overseeing daily operations including management information systems, quality assurance and control, facilities, and internal control functions.

Teoh Siow Khiang, Senior General Manager. Teoh has served as the senior general manager of Pentamaster Instrumentation since Jan 2017, overseeing the daily operations of this subsidiary.

Teh Eng Chuan, COO of the ATE division. He has been the COO of Pentamaster Technology since Jan 2015. With over 20 years of experience in the machine vision, design and control, Teh is primarily responsible for overseeing the daily operations of Pentamaster Technology.

Ng Chin Keng, COO of the FAS division. He has been the COO of Pentamaster Equipment since Jan 2015, and is primarily responsible for overseeing the daily operations of this company.

Ong Thean Lye, COO of the medical devices division. He has been the COO of Pentamaster MediQ since its inception in 2020. He is responsible for overseeing the daily operation of Pentamaster MediQ in the development of the medical devices business. Currently, Ong is the director of Walta Centre of Excellence (WCOE) and a member of the Industrial Advisory Panel (IAP) of the Electrical Engineering Technology Faculty of University Malaysia Perlis (UniMAP).

You Chin Teik, Vice President of New Business Development. He is the vice president of new business development and is primarily responsible for overseeing the R&D activities of the group.

ESG Efforts

Environment. The group does not partake in activities with a direct or significant impact on natural resources during its operations. To address potential climate change threats to communities, it has been steadily reducing its carbon footprint across its operations. The main source of greenhouse gas (GHG) emissions by the group is the consumption of electricity of machineries. Hence, routine inspection on the power supply is carried out to minimise the breakdown of machinery which, in turn, reduces production wastage and the consumption of electricity. Pentamaster also aims to encourage employees to choose environmentally friendly vehicles to lower emissions. Additionally, plans are in place to install more smart sensors to mitigate power wastage. The group intends to reduce both the direct and indirect intensity of GHG as a whole by 20% by 2030, with 2020 as the base year.

Social. The group prioritises the well-being of employees who have significantly contributed to its growth. It promotes an open communication policy to maintain motivation and encourages engagement across teams, levels, and departments. Furthermore, it is dedicated to ensuring a safe and healthy work environment for employees. Occupational safety and health committees (OSHA) conduct quarterly safety audits and ensure continuous health and safety improvements in all of the group’s business operations. Regular training sessions, including emergency first aid training, are provided to the emergency response team and employee safety and health committee.

Governance. Board characteristics are within the requirements stipulated by Bursa Malaysia, with half of the members consisting of independent directors. There is 33% female representation in the Board. Pentamaster provides clear, timely and reliable information that is compliant with Malaysia’s regulatory framework. Shareholder rights are well-protected.

Key Risks

Prolonged recovery of the semiconductor and EV market. A delayed recovery in the semiconductor and EV markets could significantly impact Pentamaster's revenue and growth prospects. As these sectors are pivotal to the company's operations, any prolonged downturn or slower-than-expected rebound could hinder its financial performance and disrupt strategic plans.

Failure to grow new ventures and adapt to industry trends. Pentamaster's ability to sustain its competitive edge hinges on successfully expanding into new ventures and adapting to evolving industry trends. If the company fails to innovate or effectively tap into emerging markets, it risks losing market share to more agile competitors, and may struggle to maintain its growth trajectory.

Strengthening of MYR against USD. A stronger MYR compared to the USD could adversely affect Pentamaster's profitability, as prices might be less competitive. Given that a substantial portion of the company's earnings comes from international markets, currency fluctuations could lead to unfavourable exchange rates, impacting financial results.

Ability to recruit or maintain talent. Securing and retaining skilled talent is crucial for Pentamaster’s continued success. The company's ability to innovate and deliver high-quality products depends on a workforce equipped with the necessary expertise and experience. Challenges in attracting or maintaining top talent could hinder operational efficiency, delay product development, and limit the company's capacity to capitalise on growth opportunities.

Emissions And ESG

Trend analysis

Pentamaster's total GHG emissions were indirectly reduced by 5% FY23 primarily due the decrease in its purchased electricity consumption.

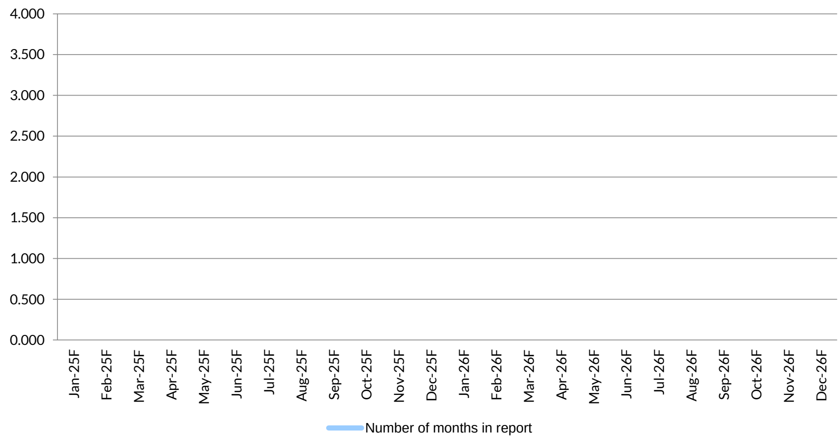
Emissions (tCO2e)	Dec-21	Dec-22	Dec-23
Scope 1	na	na	na
Scope 2	4,227	4,900	4,579
Scope 3	82	139	206
Total emissions	4,309	5,038	4,785

Source: Company data, RHB

Latest ESG-Related Developments

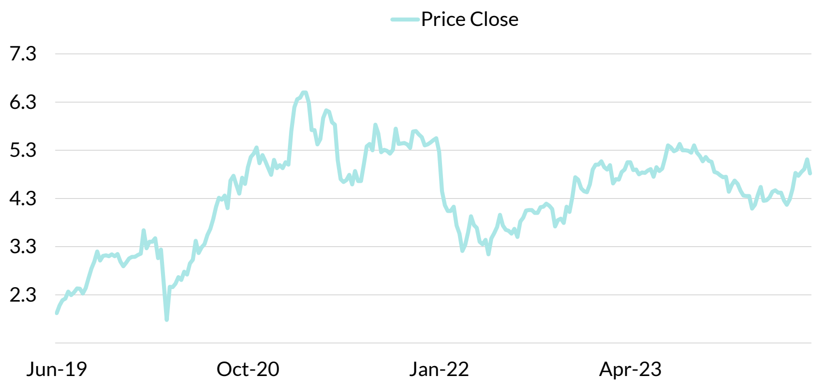
- Pentamaster aims to reduce its overall GHG emissions intensity by 20% by 2030, with 2020 as the base year.
- The group's new Campus 3 will feature energy-efficient systems, including solar panel fittings, rainwater harvesting, LED lighting, zoning, and smart sensors to optimise energy.

ESG Rating History



Source: RHB

Recommendation Chart



Source: RHB, Bloomberg

Date	Recommendation	Target Price	Price
2024-06-26			

Source: RHB, Bloomberg

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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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