

22 July 2022

Technology | Technology

Technology

Overweight (Maintained)

Potential Headwinds On The Horizon; Still O/W

- **Maintain sector OVERWEIGHT on undemanding valuations; Top Picks: Frecken Group and Venture Corp.** With the technology (tech) sector's share price performance still being soft, especially in Singapore, valuations remain cheap. We believe the risk-reward profile at these levels still remain attractive, but take note of a potential slowdown in the semiconductor industry. This sector has enjoyed robust growth for the last few years, but we expect margin erosion due to higher operational costs in the near future.
- **Despite headwinds, valuations are still attractive.** Tech stocks have undergone a correction of 50-70% – which has made valuations attractive, especially in Singapore. However, we do expect certain headwinds, like rising operational costs, that will likely erode margins for the sector. We believe a company's ability to pass on costs to its customers will likely determine its earnings resiliency against that of peers.
- **Manufacturers with strong demand will do much better this year.** We are of the view that manufacturers like Venture – which reported strong 1Q22 numbers and also guided for a positive outlook, with a sturdy orderbook – will do much better in 2022. Manufacturing stocks have been largely impacted by the global component shortages of the last two years. However, we think that this will likely ease in 2H22, which will lead to a much better performance for this year and – possibly – lead to a positive sector re-rating. While semiconductor stocks rallied in 2020 and 2021, electronics manufacturing services players' stock prices have typically remain muted. This could change in 2H22.
- **Chip sector may be facing a slowdown.** TSMC recently announced that it will trim spending on expansions by as much as 9% vs initial projections. The company also said it will delay some capex spending to 2023, despite surging revenues. We believe this is a huge indicator on concerns about elevating inventory in the USD550bn semiconductor industry, as well as the longer-term impact of a potential global recession due to rising interest rates and the ongoing Russia-Ukraine War. Micron Technology's recent weak outlook forecast also served as a red flag, or a signal of a potential incoming slowdown. The memory chip firm is now shifting to a more conservative posture on adding capacity, and expects capex on wafer fabrication equipment in the Aug 2023 fiscal year to be down from the roughly USD12bn it expected to spend in 2022. In the next few months, we expect broad capex cuts announcements from memory chip companies and second-tier foundries, as well as potential delays at top-tier foundries.

Stocks Covered 5
Rating (Buy/Neutral/Sell): 3 / 2 / 0
Last 12m Earnings Revision Trend: Positive

Top Picks

Frecken Group (FRKN SP) – BUY
Venture Corp (VMS SP) – BUY

Target Price

SGD1.24
SGD22.75

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Company Name	Rating	Target (SGD)	% Upside (Downside)	P/E (x) Dec-22F	P/B (x) Dec-22F	ROAE (%) Dec-22F	Yield (%) Dec-22F
Avi-Tech Holdings	Buy	0.42	44.8	9.0	0.9	10.4	7.8
Frecken Group	Buy	1.24	6.9	9.4	1.2	13.2	3.2
Fu Yu Corp	Neutral	0.28	5.7	10.8	1.3	11.8	6.4
Valuetronics	Neutral	0.53	(1.9)	11.3	0.9	8.5	5.7
Venture Corp	Buy	22.75	34.1	14.2	1.7	12.4	4.4

Source: Company data, RHB

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