

21 December 2020

Consumer Non-cyclical | Packaging

VS Industry (VSI MK)

Neutral (from Buy)

Positives Largely In Share Price; D/G To NEUTRAL

Target Price (Return):	MYR2.76 (+8%)
Price:	MYR2.56
Market Cap:	USD1,192m
Avg Daily Turnover (MYR/USD)	39.1m/9.46m

- Downgrade to NEUTRAL from Buy with unchanged TP of MYR2.76, 8% upside and 3% FY22F (Jul) yield.** We keep our earnings unchanged post 1QFY21 results briefing as there is no significant change in management guidance on order volume. Whilst we believe the exciting earnings growth prospects remain intact, current valuation could have priced in most of the positives, following the YTD share price rally. In addition, we do not see fresh catalysts to support a further upgrade in valuation/earnings forecasts.
- VS Industry hosted a virtual post-results briefing.** The latest update and guidance from management have not deviated significantly from the one we obtained last quarter. Order flows from key existing customers remain largely intact, whereas two new production lines for a US-based customer are set to be commissioned by December. Meanwhile, management also guided on the seasonality pattern of its order flows whereby 2Q and 3Q would be relatively slower as compared to peak quarters in 1Q and 4Q. Having secured two major new customers in 2021, it is not resting on its laurels. Discussions are ongoing with several potential customers but realistically, a firm deal may only be struck earliest by end-2021.
- Reported positive COVID-19 case.** VS Industry announced that one of its local machinery technician from the tooling division has tested positive for COVID-19. Pursuant to this, the company has taken the necessary measures to disinfect the workspace and test all of the staffs that had close contact with the infected employee – we are relieved to learn that all of them have tested negative. That said, stock sentiment could turn cautious following this development.
- Exciting FY21F to look forward to.** Looking ahead, the robust earnings growth momentum should be sustained by heightened sales orders from key customers stemming from higher global demand for consumer electronics and US-China trade war diversion. Meanwhile, the two new customers secured earlier in 2020 are expected to contribute progressively once the production lines are set up in 2021. On top of that, the benign margin expansion trend in the past two quarters should continue thanks to a more favourable product mix with sales from customers with higher margin set to increase at a faster pace. We make no material changes to our earnings forecast and keep our TP of MYR2.76 unchanged based on 19x 2021F P/E, close to +2SD from its 5-year mean.
- Risks to our recommendation** include a widespread of COVID-19 pandemic amongst the workers and delay in new production lines start-up.

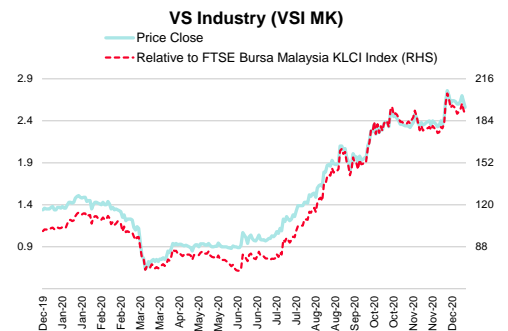
Analyst

Soong Wei Siang
 +603 9280 8865
soong.wei.siang@rhbgroup.com



Share Performance (%)

	YTD	1m	3m	6m	12m
Absolute	91.0	6.7	29.3	157.3	86.9
Relative	87.0	3.7	19.6	147.5	83.6
52-wk Price low/high (MYR)	0.64 – 2.76				



Source: Bloomberg

Forecasts and Valuation	Jul-19	Jul-20	Jul-21F	Jul-22F	Jul-23F
Total turnover (MYRm)	3,978	3,243	4,095	4,610	5,125
Recurring net profit (MYRm)	171	123	257	287	320
Recurring net profit growth (%)	7.1	(28.1)	109.7	11.6	11.3
Recurring P/E (x)	27.95	38.85	18.53	16.61	14.92
P/B (x)	3.0	2.8	2.6	2.4	2.2
P/CF (x)	21.25	14.78	23.46	15.53	14.04
Dividend Yield (%)	1.7	1.0	2.7	3.0	3.4
EV/EBITDA (x)	16.46	18.37	10.90	9.70	8.74
Return on average equity (%)	10.4	7.0	14.6	15.1	15.6
Net debt to equity (%)	2.8	net cash	net cash	net cash	net cash

Source: Company data, RHB

Financial Exhibits

Asia	Financial summary (MYR)	Jul-19	Jul-20	Jul-21F	Jul-22F	Jul-23F
Malaysia	Recurring EPS	0.09	0.07	0.14	0.15	0.17
Consumer Non-cyclical	DPS	0.04	0.03	0.07	0.08	0.09
VS Industry	BVPS	0.86	0.91	0.98	1.06	1.15
VSI MK	Return on average equity (%)	10.4	7.0	14.6	15.1	15.6
Neutral						
	Valuation metrics	Jul-19	Jul-20	Jul-21F	Jul-22F	Jul-23F
Valuation basis	Recurring P/E (x)	27.95	38.85	18.53	16.61	14.92
P/E	P/B (x)	3.0	2.8	2.6	2.4	2.2
	FCF Yield (%)	2.3	4.2	0.1	4.8	5.4
Key drivers	Dividend Yield (%)	1.7	1.0	2.7	3.0	3.4
i. New work orders from trade war diversion;	EV/EBITDA (x)	16.46	18.37	10.90	9.70	8.74
ii. Strong demand for key customers' products.	EV/EBIT (x)	24.82	28.93	14.51	12.77	11.33
	Income statement (MYRm)	Jul-19	Jul-20	Jul-21F	Jul-22F	Jul-23F
Key risks	Total turnover	3,978	3,243	4,095	4,610	5,125
i. Loss of key customers;	Gross profit	370	321	480	546	609
ii. Unable to pass on higher costs.	EBITDA	294	251	436	482	524
	Depreciation and amortisation	(99)	(92)	(108)	(116)	(120)
Company Profile	Operating profit	195	160	327	366	404
VS Industry is an integrated electronics manufacturing services (EMS) provider for world-renowned manufacturers of office and household appliances.	Net interest	(19)	(10)	(3)	(4)	(1)
	Pre-tax profit	174	152	324	362	403
	Taxation	(62)	(49)	(70)	(78)	(87)
	Reported net profit	158	116	257	287	320
	Recurring net profit	171	123	257	287	320
	Cash flow (MYRm)	Jul-19	Jul-20	Jul-21F	Jul-22F	Jul-23F
	Change in working capital	(110)	30	(168)	(102)	(102)
	Cash flow from operations	224	323	203	307	340
	Capex	(117)	(121)	(200)	(80)	(80)
	Cash flow from investing activities	(102)	(109)	(200)	(80)	(80)
	Dividends paid	(79)	(48)	(129)	(144)	(160)
	Cash flow from financing activities	(171)	(204)	(161)	(208)	(211)
	Cash at beginning of period	416	379	405	241	255
	Net change in cash	(48)	10	(157)	19	49
	Ending balance cash	367	389	247	261	304
	Balance sheet (MYRm)	Jul-19	Jul-20	Jul-21F	Jul-22F	Jul-23F
	Total cash and equivalents	379	405	241	255	299
	Tangible fixed assets	889	847	939	903	863
	Total investments	152	151	151	151	151
	Total assets	3,033	2,825	3,043	3,197	3,376
	Short-term debt	362	215	200	150	100
	Total long-term debt	67	23	10	0	0
	Total liabilities	1,256	957	1,049	1,062	1,086
	Total equity	1,777	1,869	1,994	2,134	2,290
	Total liabilities & equity	3,033	2,825	3,043	3,197	3,376
	Key metrics	Jul-19	Jul-20	Jul-21F	Jul-22F	Jul-23F
	Revenue growth (%)	(2.7)	(18.5)	26.3	12.6	11.2
	Recurrent EPS growth (%)	(2.8)	(28.1)	109.7	11.6	11.3
	Gross margin (%)	9.3	9.9	11.7	11.9	11.9
	Operating EBITDA margin (%)	7.4	7.8	10.6	10.4	10.2
	Net profit margin (%)	4.0	3.6	6.3	6.2	6.2
	Dividend payout ratio (%)	50.0	41.8	50.0	50.0	50.0
	Capex/sales (%)	2.9	3.7	4.9	1.7	1.6
	Interest cover (x)	7.22	9.24	28.97	40.37	64.13

Source: Company data, RHB

Recommendation Chart



Source: RHB, Bloomberg

Date	Recommendation	Target Price	Price
2020-10-01	Buy	2.76	2.36
2020-09-28	Buy	2.58	2.16
2020-08-20	Buy	2.28	1.79
2020-08-07	Buy	1.90	1.50
2020-07-17	Buy	1.47	1.26
2020-06-25	Buy	1.25	0.99
2020-06-24	Buy	1.35	1.04
2020-03-26	Buy	1.18	0.73
2019-09-27	Buy	1.62	1.36
2019-03-07	Buy	1.28	1.04

Source: RHB, Bloomberg

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KUALA LUMPUR

RHB Investment Bank Bhd

Level 3A, Tower One, RHB Centre
Jalan Tun Razak
Kuala Lumpur 50400
Malaysia
Tel : +603 9280 8888
Fax : +603 9200 2216

JAKARTA

PT RHB Sekuritas Indonesia

Revenue Tower, 11th Floor, District 8 - SCBD
Jl. Jendral Sudirman Kav 52-53
Jakarta 12190
Indonesia
Tel : +6221 509 39 888
Fax : +6221 509 39 777

BANGKOK

RHB Securities (Thailand) PCL

10th Floor, Sathorn Square Office Tower
98, North Sathorn Road, Silom
Bangrak, Bangkok 10500
Thailand
Tel: +66 2088 9999
Fax :+66 2088 9799

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RHB Bank Berhad (Singapore branch)

90 Cecil Street
#04-00 RHB Bank Building
Singapore 069531