

Hi-P International (HIP SP)

Lowers Guidance Again

2nd guidance cut this year; Slash TP 34%

HIP lowered its earnings guidance for the second time this year. It now expects lower sales and profit in 3Q18 on a YoY basis in contrast to its earlier guidance of higher revenue and similar profit. We are concerned industry headwinds are hitting HIP much harder than expected. Consequently, we slash our EPS by 25-32% for FY18-20E. Our ROE-g/COE-g TP is cut to SGD0.84, now based on 1.2x FY18E P/B (previous 1.8x), based on FY18-20E average ROE of 10.4% and COE of 9%. HOLD.

A double-whammy on margins

HIP blamed the guidance cut on: i) a delay in billing for certain production tools; ii) lower yields for products undergoing ramp-up; and iii) lower market demand for certain products. The latter two reasons may be a double-whammy that further accelerates a fall in HIP's profitability. HIP's margins are already under pressure given its large fixed cost base amid an environment of fierce pricing competition.

Demand outlook seems to have deteriorated fast

3Q is typically seasonally the strongest as HIP ramps up production to meet seasonal holiday demand. In Aug-18, management had indicated that the pace of the 3Q18 ramp-up was healthy. Since management has not quantified the impact of weaker demand we are worried the latest guidance cut is a sign the demand outlook has deteriorated much faster than we anticipated.

Volume disruption still the key risk

We believe HIP's performance in 4Q18 still largely hinges on the reception of the smartphones launched recently by its key wireless customer. A key downside risk to our forecasts is if actual volumes miss management's already tempered internal forecasts. On the flipside, strong demand of the customer's cheapest phone model in this year's launch may provide a positive surprise to our FY18 estimates.

FYE Dec (SGD m)	FY16A	FY17A	FY18E	FY19E	FY20E
Revenue	1,305	1,427	1,349	1,418	1,453
EBITDA	158	220	159	166	170
Core net profit	55	121	63	62	58
Core FDEPS (cts)	6.7	14.9	7.8	7.6	7.2
Core FDEPS growth(%)	nm	123.3	(47.9)	(2.6)	(5.4)
Net DPS (cts)	0.8	25.0	3.0	1.0	3.0
Core FD P/E (x)	7.6	12.5	11.7	12.1	12.7
P/BV (x)	0.7	2.9	1.3	1.2	1.1
Net dividend yield (%)	1.6	13.4	3.3	1.1	3.3
ROAE (%)	9.6	22.0	11.5	10.4	9.0
ROAA (%)	4.6	10.5	5.2	4.7	4.3
EV/EBITDA (x)	2.5	6.5	3.9	3.6	3.1
Net gearing (%) (incl perps)	net cash	net cash	net cash	net cash	net cash
Consensus net profit	-	-	85	89	87
MKE vs. Consensus (%)	-	-	(25.9)	(30.7)	(32.6)

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HOLD

Share Price	SGD 0.92
12m Price Target	SGD 0.84 (-8%)
Previous Price Target	SGD 1.27

Company Description

Hi-P is an EMS provider with 13 manufacturing sites across 4 countries

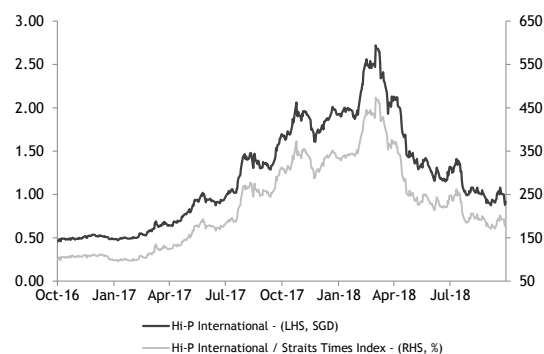
Statistics

52w high/low (SGD)	2.72/0.88
3m avg turnover (USDm)	3.1
Free float (%)	13.7
Issued shares (m)	887
Market capitalisation	SGD811.8M USD589M

Major shareholders:

Yao Hsiao Tung	83.0%
FMR LLC	2.3%
Edentree Investment Management	2.3%

Price Performance



	-1M	-3M	-12M
Absolute (%)	(3)	(29)	(45)
Relative to index (%)	(1)	(24)	(41)

Source: FactSet

Forecast changes

Fig 1: MKE forecast changes for HIP

	FY18E			FY19E			FY20E		
	New	Old	Chg (%)	New	Old	Chg (%)	New	Old	Chg (%)
Revenue (SGDm)	1,349.0	1,432.4	-5.8	1,418.0	1,516.8	-6.5	1,452.6	1,568.2	-7.4
Gross profit (SGDm)	167.9	190.5	-11.9	175.5	203.7	-13.8	175.9	208.3	-15.6
EBIT (SGDm)	77.0	102.4	-24.9	79.0	113.7	-30.5	77.3	110.3	-30.0
EBITDA (SGDm)	158.6	184.1	-13.8	165.8	199.7	-17.0	170.1	201.6	-15.6
Core net profit (SGDm)	63.3	84.4	-25.0	61.6	90.4	-31.8	58.3	85.8	-32.0
EPS (cts)	7.8	10.4	-25.0	7.6	11.1	-31.8	7.2	10.6	-32.0
			Chg (ppt)			Chg (ppt)			Chg (ppt)
Gross margin	12.4%	13.3%	-0.9	12.4%	13.4%	-1.1	12.1%	13.3%	-1.2
SGA as % of sales	6.0%	5.8%	0.2	6.1%	5.8%	0.3	6.1%	5.8%	0.3

Source: Maybank Kim Eng

We slash our FY18-20E EPS by 25-32% reflecting expectations of a weaker demand outlook. Gross margins have been cut 0.9-1.2ppt to reflect lower manufacturing yields and a possible worsening of pricing pressure as the demand outlook weakens. We believe downside risks to our FY18E could materialise if actual volumes miss management's internal forecasts for 4Q18. On the flipside, strong reception of the cheapest smartphone model launched by its key wireless customer this year may contribute to a positive earnings surprise.

Fig 2: Peer comps

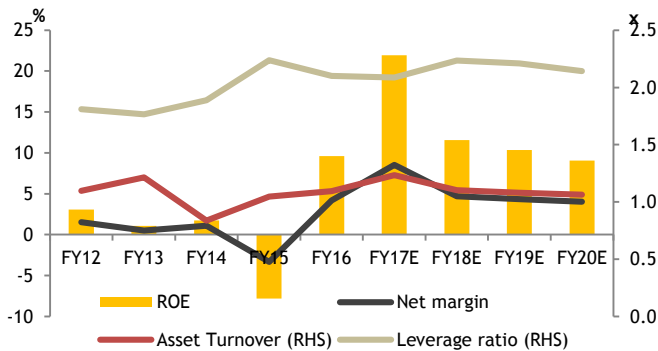
Company	BBG Code	MKE Rec	MKE TP (LC)	Price (LC)	FYE mm	Mcap USDm	P/E (x)				EV /EBITDA (x)	PBR (x)
							Act	FY1	FY2	FY3	FY1	FY1
HI-P Int'l	HIP SP	Hold	0.84	0.92	12	589	6.1	11.7	12.0	12.7	3.2	1.4
Singapore listed EMS and precision engineering peers												
Valuetronics	VALUE SP	Buy	1.05	0.65	03	205	7.9	7.9	7.0	6.3	3.7	-
Sunningdale Tech	SUNN SP	NR	-	1.38	12	189	8.5	9.5	8.2	7.5	-	0.7
Memtech Int'l	MTEC SP	NR	-	0.88	12	91	7.5	7.8	6.6	5.9	2.7	0.8
Venture Corp	VMS SP	Buy	25.77	16.39	12	3,437	12.4	12.1	10.9	9.3	7.9	-
Average							11.1	11.7	10.6	9.4	6.9	1.2
High mix low volume EMS peers												
Benchmark Elec	BHE US	NR	-	23.25	12	1,083	17.8	16.4	13.7	12.0	-	-
Plexus	PLXS US	NR	-	53.72	09	1,732	16.6	17.1	13.9	12.6	9.0	2.0
Average							17.1	16.8	13.8	12.4	9.0	2.0
Global EMS peers												
Hon Hai	2317 TT	NR	-	71.90	12	40,380	9.0	9.9	9.2	8.3	5.8	1.0
Flex	FLEX US	NR	-	11.98	03	6,382	11.0	9.7	7.9	6.6	5.8	1.8
Jabil	JBL US	NR	-	23.73	08	3,997	9.1	8.0	7.1	6.7	3.4	1.9
Pegatron	2938 TT	NR	-	53.90	12	4,564	9.5	9.0	7.6	7.1	3.1	0.9
V.S. Industry	VSI MK	Buy	1.95	1.64	07	687	15.5	19.8	14.5	12.1	9.8	-
Sanmina	SANM	NR	-	24.16	09	1,642	8.4	11.0	8.8	8.1	-	-
FIH Mobile	2038 HK	NR	-	0.72	12	744	-	-	nm	30.6	-	0.3
Celestica	CLS CN	NR	-	14.03	12	1,300	9.6	9.5	8.0	7.0	4.7	1.1
UMC Electronics	6615 JP	NR	-	2,129	03	364	22.6	22.6	15.7	12.4	-	1.4
Fabrinet	FN US	NR	-	44.31	06	1,615	14.9	13.3	11.6	9.8	-	-
Average							9.5	10.0	8.9	8.3	5.4	1.2

Source: FactSet, Bloomberg, Maybank Kim Eng

Value Proposition

- Strong execution with key customers like Apple has helped Hi-P win increased volume in recent years.
- ODM capabilities created some form of customer stickiness in the consumer electronics segment.
- Demonstrated ability to move away from assembly projects that have razor-thin margins to prioritise ones with better profitability.
- Operates in a highly competitive industry. As such, Hi-P must continually invest in value-added capabilities.

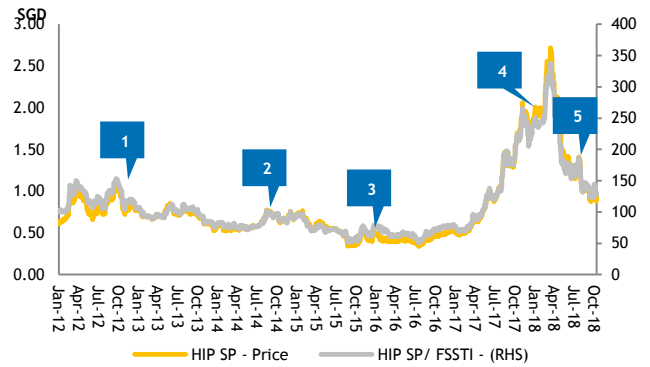
DuPont ROE



Source: Company, Maybank Kim Eng

Price Drivers

Historical share price trend



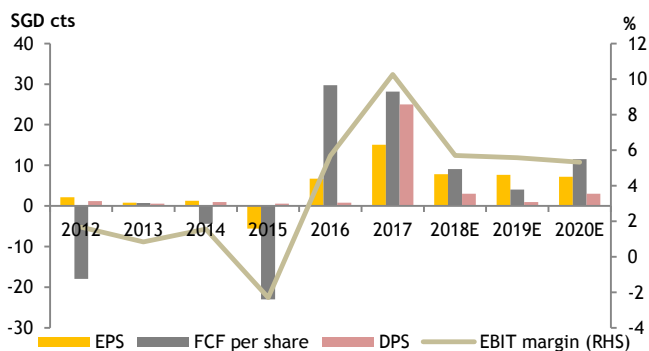
Source: Company, FactSet, Maybank Kim Eng

1. Between FY11-14, lacklustre share price performance was due to customers Nokia and Blackberry losing market share.
2. YotaPhone 2 official launch. Russia was expected to be a key market. However, Russian economic crisis and sanctions destroyed local and European demand.
3. Hi-P commenced arbitration proceedings against Yota, claiming USD126m.
4. Upgraded 3Q17 earnings guidance. Subsequently, Hi-P announced record quarterly profit of SGD34m, with sanguine 4Q17 outlook.
5. Downgraded FY18 revenue and net profit guidance.

Financial Metrics

- Earnings delivery has largest effect on Hi-P’s share price.
- We forecast FY17-20 EPS CAGR of -21.7% following two negative revisions in management guidance, citing a cautious outlook by customers.
- Clean balance sheet and treasury shares provide ammo for inorganic growth.

EPS, FCF per share and DPS



Source: Company

Swing Factors

Upside

- Better-than-expected orders and execution from existing projects.
- New customer wins and new projects.
- Improved communication regarding strategy, as well as cost-control efforts.

Downside

- Micro- and macro-driven risks that negatively affect end-demand of products Hi-P participates in.
- Market share losses and/or payment defaults from customers.
- Sudden and steep declines in the USD (revenue exposure), against the CNY (operating exposure) and SGD (reported currency).

FYE 31 Dec	FY16A	FY17A	FY18E	FY19E	FY20E
Key Metrics					
P/E (reported) (x)	6.5	7.2	11.7	12.0	12.7
Core P/E (x)	7.6	12.4	11.7	12.0	12.7
Core FD P/E (x)	7.6	12.5	11.7	12.1	12.7
P/BV (x)	0.7	2.9	1.3	1.2	1.1
P/NTA (x)	0.7	2.9	1.3	1.2	1.1
Net dividend yield (%)	1.6	13.4	3.3	1.1	3.3
FCF yield (%)	54.8	15.0	9.9	4.4	12.9
EV/EBITDA (x)	2.5	6.5	3.9	3.6	3.1
EV/EBIT (x)	5.4	9.8	8.1	7.6	6.9

INCOME STATEMENT (SGD m)

Revenue	1,305.1	1,426.9	1,349.0	1,418.0	1,452.6
Gross profit	155.8	232.9	167.9	175.5	175.9
EBITDA	158.2	219.7	158.6	165.8	170.1
Depreciation	(84.1)	(73.4)	(81.6)	(86.8)	(92.8)
Amortisation	0.0	0.0	0.0	0.0	0.0
EBIT	74.1	146.4	77.0	79.0	77.3
Net interest income / (exp)	(3.2)	(0.1)	(1.0)	(4.8)	(7.1)
Associates & JV	0.3	0.0	0.3	0.3	0.3
Exceptionals	0.0	0.0	0.0	0.0	0.0
Other pretax income	0.0	0.0	0.0	0.0	0.0
Pretax profit	71.2	146.3	76.2	74.5	70.5
Income tax	(16.7)	(24.8)	(13.0)	(12.7)	(12.0)
Minorities	0.0	(0.0)	0.0	(0.2)	(0.2)
Discontinued operations	0.0	0.0	0.0	0.0	0.0
Reported net profit	54.5	121.5	63.3	61.6	58.3
Core net profit	54.5	121.5	63.3	61.6	58.3
Preferred Dividends	0.0	0.0	0.0	0.0	1.0

BALANCE SHEET (SGD m)

Cash & Short Term Investments	110.9	277.9	376.1	400.5	469.3
Accounts receivable	361.8	452.8	286.3	475.2	320.8
Inventory	142.9	178.5	132.1	194.7	141.1
Property, Plant & Equip (net)	359.6	315.1	313.5	326.7	283.8
Intangible assets	11.8	11.4	11.4	11.4	11.4
Investment in Associates & JVs	2.5	7.0	7.3	7.6	7.9
Other assets	40.4	37.1	42.0	42.0	42.0
Total assets	1,030.1	1,279.9	1,168.7	1,458.0	1,276.2
ST interest bearing debt	95.5	205.2	260.0	260.0	260.0
Accounts payable	247.7	421.4	219.2	454.8	237.8
LT interest bearing debt	0.1	0.0	0.0	0.0	0.0
Other liabilities	108.0	124.0	121.0	121.0	122.0
Total Liabilities	450.8	750.4	600.1	835.7	619.6
Shareholders Equity	578.2	528.5	567.6	621.1	655.2
Minority Interest	1.0	1.0	1.0	1.2	1.4
Total shareholder equity	579.2	529.5	568.5	622.3	656.6
Total liabilities and equity	1,030.1	1,279.9	1,168.7	1,458.0	1,276.2

CASH FLOW (SGD m)

Pretax profit	71.2	146.3	76.2	74.5	70.5
Depreciation & amortisation	84.1	73.4	81.6	86.8	92.8
Adj net interest (income)/exp	0.0	0.0	0.0	0.0	1.0
Change in working capital	92.0	54.9	8.6	(15.9)	(8.0)
Cash taxes paid	(12.6)	(18.6)	(13.0)	(12.7)	(12.0)
Other operating cash flow	0.0	0.0	0.0	0.0	1.0
Cash flow from operations	234.4	256.0	153.2	132.5	145.0
Capex	(6.9)	(28.9)	(80.0)	(100.0)	(50.0)
Free cash flow	227.5	227.1	73.2	32.5	95.0
Dividends paid	(5.7)	(172.7)	(24.2)	(8.1)	(24.2)
Equity raised / (purchased)	0.0	0.0	0.0	0.0	0.0
Perpetual securities	0.0	0.0	0.0	0.0	1.0
Change in Debt	(220.7)	109.7	54.8	0.0	0.0
Other invest/financing cash flow	(31.1)	(2.2)	(5.6)	0.2	0.4
Effect of exch rate changes	(0.1)	5.2	0.0	(0.2)	(0.4)
Net cash flow	(30.1)	167.0	98.2	24.4	71.8

FYE 31 Dec	FY16A	FY17A	FY18E	FY19E	FY20E
Key Ratios					
Growth ratios (%)					
Revenue growth	(4.2)	9.3	(5.5)	5.1	2.4
EBITDA growth	124.7	38.9	(27.8)	4.5	2.6
EBIT growth	nm	97.4	(47.4)	2.6	(2.2)
Pretax growth	nm	105.5	(47.9)	(2.3)	(5.3)
Reported net profit growth	nm	122.8	(47.9)	(2.6)	(5.4)
Core net profit growth	nm	122.8	(47.9)	(2.6)	(5.4)
Profitability ratios (%)					
EBITDA margin	12.1	15.4	11.8	11.7	11.7
EBIT margin	5.7	10.3	5.7	5.6	5.3
Pretax profit margin	5.5	10.3	5.7	5.3	4.9
Payout ratio	12.0	166.2	38.3	13.1	41.5
DuPont analysis					
Net profit margin (%)	4.2	8.5	4.7	4.3	4.0
Revenue/Assets (x)	1.3	1.1	1.2	1.0	1.1
Assets/Equity (x)	1.8	2.4	2.1	2.3	1.9
ROAE (%)	9.6	22.0	11.5	10.4	9.0
ROAA (%)	4.6	10.5	5.2	4.7	4.3
Liquidity & Efficiency					
Cash conversion cycle	78.6	50.4	48.3	46.4	48.3
Days receivable outstanding	116.1	102.8	98.6	96.7	98.6
Days inventory outstanding	60.4	48.5	47.3	47.3	47.3
Days payables outstanding	97.9	100.9	97.6	97.6	97.6
Dividend cover (x)	8.4	0.6	2.6	7.6	2.4
Current ratio (x)	1.4	1.2	1.4	1.3	1.6
Leverage & Expense Analysis					
Asset/Liability (x)	2.3	1.7	1.9	1.7	2.1
Net gearing (%) (incl perps)	net cash	net cash	net cash	net cash	net cash
Net gearing (%) (excl. perps)	net cash	net cash	net cash	net cash	net cash
Net interest cover (x)	22.9	nm	73.4	16.5	10.9
Debt/EBITDA (x)	0.6	0.9	1.6	1.6	1.5
Capex/revenue (%)	0.5	2.0	5.9	7.1	3.4
Net debt/ (net cash)	(15.3)	(72.7)	(116.1)	(140.5)	(209.3)

Source: Company; Maybank

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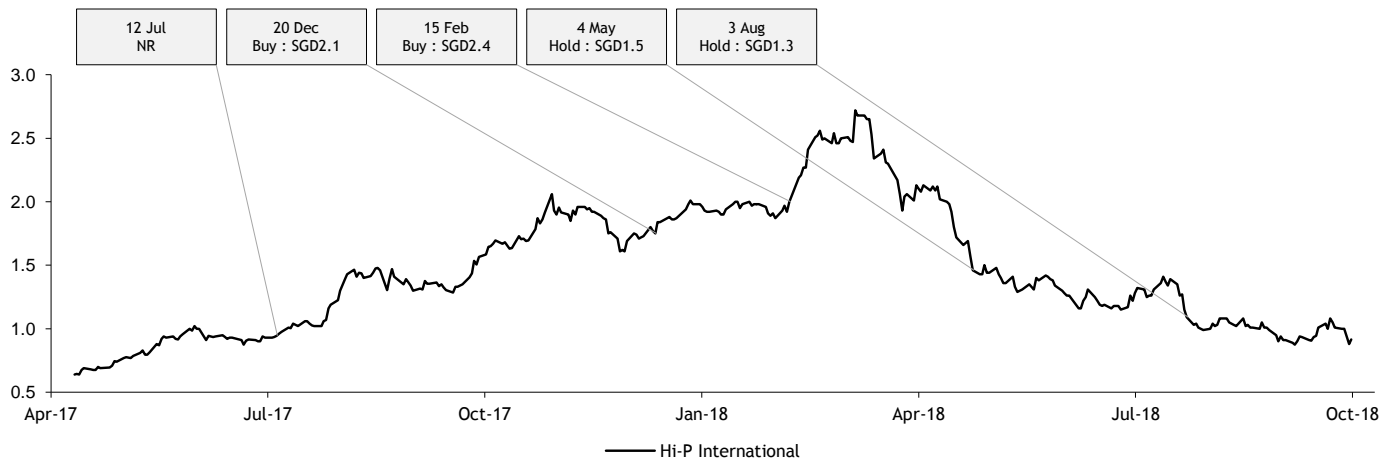
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