EngTek (HOLD ←→, EPS ←→)

INDUSTRY: NEUTRAL
EARNINGS EVALUATION

23 August 2011
Price Target: RM2.50(↑)
Share Price: RM2.16

Weaker Than Expected Results

Results

- 1H11 normalised net profit of RM10.3m came in below expectations, at 23.6-24.1% of our and consensus full-year estimates of RM42.8-43.6m.

Deviations

- Lower volume shipments, ASP, higher costs, and weaker US$.

Risks

- Weaker than expected consumer demand for HDDs.
- Higher raw material costs.
- RM appreciation against the US dollar.

Forecasts

- Despite the weak results, we are keeping our earnings forecasts unchanged. Given the TYK Capital's offer to privatise Eng Tek at RM2.50/share (on 22 Jul 2011) is higher than our TP, earnings outlook is no longer material.

Rating

HOLD (TP: RM2.50↑)

- Negatives – USD depreciation, weak customer orders and high raw material prices will negatively impact the company's results.

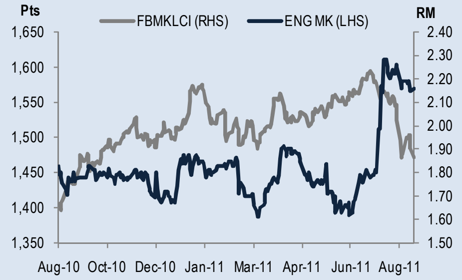
Valuation

- TP raised from RM1.86 to RM2.50 (in line with the GO price), and we continue to advocate investors to take up the proposed general offer (GO) given the offer price of RM2.50 is significantly higher than our original TP (which is derived based on a DCF of FCF until 2014 with a WACC of 13.1% and a terminal growth of 0%).
- We are also taking this opportunity to cease coverage on the stock, given the company's bleak outlook as well as the proposed GO made by the major shareholders of Eng Tek that is likely to succeed given the attractive offer price.

Low Yee Huap, CFA
yhlow@hlib.hongleong.com.my
(603) 2168 1078

KLCI	1,472.2
Expected share price return	15.7%
Expected dividend return	-
Expected total return	15.7%

Share Price



Information

Bloomberg Ticker	ENG MK
Bursa Code	8826
Issued Shares (m)	122
Market cap (RM m)	225
3-mth avg. volume ('000)	443

Price Performance	1M	3M	12M
Absolute	-5.3	21.3	18.2
Relative	0.3	25.1	13.2

Major Shareholders

PNB	14.4%
Yeow Siong Low	13.1%
Yong Khoon Teh	9.9%
Lembaga Tabung Haji	8.3%
Other related parties	10.8%
Free Float	43.4%

Summary Earnings Table

FYE 31 Dec (RMm)	2010A	2011E	2012E	2013E
Revenue	557.3	554.1	588.9	617.8
EBITDA	80.2	77.6	88	97.8
Pre-tax Profit	51.3	51	62.3	72.7
PATAMI	48.3	43.6	53.3	62.1
Adj. PATAMI	47.1	43.6	53.3	62.1
Rep. EPS sen	39.8	35.6	43.5	50.8
Adj. EPS sen	38.9	35.6	43.5	50.8
P/E (x)	5.6	6.1	5.0	4.3
Net DPS sen	16.0	-	-	-
Net DY (%)	7.4	-	-	-
P/BV (x)	0.97	0.86	0.75	0.66
EV/EBITDA (x)	2.8	2.6	1.9	1.3
Net D/E %	-15.0	-14.7	-24.8	-33.0
ROA %	11.8	9.7	10.8	11.4
ROE %	17.8	14.6	15.7	15.9

HLIB

Figure #1 Engtek's 2Q11 Results

RMm	2Q10	1Q11	2Q11	yoy%	qoq%	1H10	1H11	yoy%	Comments
Revenue	134.6	120.3	133.4	-1%	11%	288.1	253.7	-12%	YoY: Due to: (1) Weaker US$; (2) Lower ASP for hard disk products; and (3) Lower sales volume. QoQ: Due to lower ASPs.
EBITDA	17.7	12.5	14.6	-18%	16%	47.9	27.1	-43%	YoY: Hurt by: (1) Higher production costs; and (2) Margin squeeze arising from lower ASP and lower sales volume. QoQ: Helped by improved economies of scale that more than offset ASP erosion.
EBITDA Margin %	13.2%	10.4%	10.9%			16.6%	10.7%		
EBIT	10.8	5.3	7.3	-32%	38%	31.0	12.6	-59%	YoY: Hurt further by higher depreciation and amortization expenses.
PBT	12.8	5.6	6.5	-49%	16%	32.9	12.1	-63%	Filtered down from EBIT.
PAT	12.8	4.9	5.7	-55%	17%	31.2	10.6	-66%	Filtered down from PBT.
PATAMI	12.6	4.8	5.6	-56%	16%	30.8	10.4	-66%	
Normalised PATAMI	10.8	4.8	5.5	-49%	13%	29.9	10.3	-66%	
Reported EPS (sen)	8.9	3.9	4.5	-50%	13%	25.5	8.5	-67%	
Adjusted EPS (sen)	8.8	3.9	4.5	-49%	13%	24.8	8.4	-66%	

Company Data, HLIB

Figure #2 Engtek's HQ11 Results vs HLIB, Consensus

RMm	1H11	FY11 Consensus	Actual vs Consensus	FY11 HLIB Est.	Actual vs HLIB	Comments
Revenue	253.7	553.3	46%	554.1	45.8%	Below expectation
EBITDA	27.1	84.0	32%	77.6	35.0%	
EBITDA Margin %	10.7%	15.2%		14.0%		
EBIT	12.6	47.4	27%	48.6	25.9%	
PBT	12.1	52.1	23%	51.0	23.7%	
PAT	10.6	49.1	22%	44.4	23.9%	
PATAMI	10.4	49.0	21%	43.6	23.8%	Below expectation
Normalised PATAMI	10.3	49.0	21%	43.6	23.6%	
Reported EPS (sen)	8.5	41.5	20%	35.6	23.8%	
Adjusted EPS (sen)	8.4	41.8	20%	35.6	23.6%	

Company Data, HLIB, Bloomberg

Eng Teknologi Holdings Bhd (Hold, PT: RM2.50, CP: RM2.16)

Income statement

FYE 31 Dec (RMm)	2009A	2010A	2011E	2012E	2013E
Revenue	474.9	557.3	554.1	588.9	617.8
COGS	-385.1	-477.1	-476.5	-500.9	-520.1
EBITDA	**89.8**	**80.2**	**77.6**	**88.0**	**97.8**
D&A	-42.1	-31.5	-29.0	-28.9	-29.1
EBIT	47.7	48.7	48.6	59.1	68.6
Net Interest Income	2.5	1.4	2.3	3.2	4.0
Associates	0.0	0.0	0.1	0.0	0.0
Exceptionals	-1.0	1.2	0.0	0.0	0.0
PBT	**49.2**	**51.3**	**51.0**	**62.3**	**72.7**
Tax	-5.0	-2.1	-6.6	-8.1	-9.4
PAT	44.2	49.2	44.4	54.2	63.2
Minority Interests	0.8	0.9	0.8	0.9	1.1
PATAMI	**43.5**	**48.3**	**43.6**	**53.3**	**62.1**
Normalised PATAMI	**44.5**	**47.1**	**43.6**	**53.3**	**62.1**
Basic Shares (m)	119.3	122.0	122.4	122.4	122.4
Rep. EPS sen	36.5	39.8	35.6	43.5	50.8
Adj. EPS sen	37.3	38.9	35.6	43.5	50.8
Adj. FD EPS sen	37.3	38.4	35.6	43.5	50.7

Quarterly financial summary

FYE 31 Dec (RMm)	2Q10	3Q10	4Q10	1Q11	2Q11
Revenue	134.60	132.59	136.55	120.30	133.44
COGS	-116.89	-116.96	-119.95	-107.76	-118.85
EBITDA	**17.71**	**15.63**	**16.60**	**12.54**	**14.59**
D&A	-6.95	-7.07	-7.47	-7.24	-7.31
EBIT	10.76	8.56	9.13	5.29	7.28
Net Interest Income	0.26	0.71	-0.29	0.26	-0.82
Associates	0.01	-0.07	0.03	0.06	-0.07
Exceptionals	1.80	-0.41	0.68	-0.02	0.10
PBT	**12.83**	**8.80**	**9.56**	**5.59**	**6.49**
Tax	0.01	-0.31	-0.05	-0.69	-0.77
PAT	12.84	8.49	9.51	4.90	5.72
Minority Interests	0.22	0.28	0.19	0.10	0.16
PATAMI	**12.63**	**8.20**	**9.31**	**4.80**	**5.57**
Normalised PATAMI	**10.83**	**8.62**	**8.63**	**4.82**	**5.47**
Basic Shares (m)	121.9	122.0	122.0	122.4	122.5
Rep. EPS sen	10.35	6.72	7.63	3.92	4.54
Adj. EPS sen	8.88	7.06	7.07	3.94	4.46
Adj. FD EPS sen	8.77	6.99	7.01	3.93	4.45

Balance sheet

FYE 31 Dec (RMm)	2009A	2010A	2011E	2012E	2013E
Cash	60.1	89.3	93.9	128.2	170.9
Receivables	114.3	107.0	125.7	132.9	139.5
Inventories	43.7	45.0	63.9	66.6	69.2
Investments	0.0	0.9	1.3	1.3	1.3
Fixed Assets	120.8	116.8	111.7	113.0	114.0
Intangibles	27.1	28.6	28.4	28.3	28.1
Other Assets	26.6	20.7	23.7	23.7	23.7
Ttl Assets	**392.5**	**408.4**	**448.7**	**493.9**	**546.7**
Payables	50.0	46.1	59.5	62.9	66.0
Short Term Debt	45.0	39.1	39.4	39.4	39.4
Long Term Debt	23.4	9.3	9.9	9.9	9.9
Other Liabilities	34.4	42.4	41.9	41.9	41.9
Ttl Liab	**152.8**	**136.9**	**150.6**	**154.0**	**157.1**
Shareholders' Funds	239.8	271.5	298.1	339.9	389.6
Minority Interests	2.2	2.1	2.8	3.7	4.8
Total S/H Equity	237.6	269.4	295.3	336.2	384.8
Ttl Liab&S/H Funds	**392.5**	**408.4**	**448.7**	**493.9**	**546.7**

Valuation Ratios

FYE 31 Dec (RMm)	2009A	2010A	2011E	2012E	2013E
PER (x)	5.9	5.4	6.1	5.0	4.3
Adj. PER (x)	5.8	5.6	6.1	5.0	4.3
FD PER (x)	5.8	5.6	6.1	5.0	4.3
Net DPS sen	6.0	16.0	-	-	-
Net DY (%)	2.8	7.4	-	-	-
Book/share sen	2.01	2.22	2.51	2.87	3.29
P/Book (x)	1.07	0.97	0.86	0.75	0.66
FCF/share sen	59.3	51.0	12.1	38.1	46.0
FCF yield (%)	27.4	23.6	5.6	17.6	21.3
Mkt Cap	258	264	264	264	264
Net Cash(Debt)	-8	41	45	87	133
EV	266	223	219	177	132
EV/EBITDA (x)	3.0	2.8	2.8	2.0	1.3
ROE (%)	18.5	17.8	14.6	15.7	15.9
Current Ratio (x)	1.8	2.0	2.4	2.7	3.0
Quick Ratio (x)	1.5	1.7	1.8	2.2	2.5
Interest Cover (x)	-11.4	-21.0	-23.3	-22.3	-24.3

Cashflow Analysis

FYE 31 Dec (RMm)	2009A	2010A	2011E	2012E	2013E
EBITDA	89.8	80.2	77.6	88.0	97.8
Net Interest	2.5	1.4	2.3	3.2	4.0
Tax Paid	-5.0	-2.1	-6.6	-8.1	-9.4
Working Capital Chgs	13.4	2.1	-24.2	-6.5	-6.1
Other	-1.1	-1.3	-4.3	0.0	0.0
Operating CF	**99.6**	**80.2**	**44.7**	**76.6**	**86.3**
FCF	**70.7**	**62.2**	**14.8**	**46.6**	**56.3**
CAPEX	-10.8	-18.0	-29.9	-30.0	-30.0
Asset Sales	0.8	0.8	0.1	0.0	0.0
Acquisitions	-18.2	0.0	0.0	0.0	0.0
Other	0.3	-1.6	0.2	0.0	0.0
Investing CF	**-27.7**	**-18.8**	**-29.7**	**-30.0**	**-30.0**
Dividends	-7.1	-14.6	-10.6	-12.4	-13.6
Debt Chgs	-49.7	-20.0	0.9	0.0	0.0
Other	-0.1	3.8	0.3	0.0	0.0
Financing CF	**-57.0**	**-30.8**	**-9.4**	**-12.4**	**-13.6**
Net Cashflow	**14.9**	**30.6**	**5.7**	**34.2**	**42.7**

Other Ratios

FYE 31 Dec (RMm)	2009A	2010A	2011E	2012E	2013E
Sales Growth (%)	-14.4	17.3	-0.6	6.3	4.9
EBITDA Growth (%)	-12.2	-10.7	-3.2	13.4	11.2
EBIT Growth (%)	-19.1	2.1	-0.1	21.6	16.1
PBT Growth (%)	18.0	4.2	-0.5	22.3	16.6
Net Profit Growth (%)	77.6	11.1	-9.7	22.3	16.6
EBITDA Margin (%)	18.9	14.4	14.0	14.9	15.8
EBIT Margin (%)	10.0	8.7	8.8	10.0	11.1
PBT Margin (%)	10.4	9.2	9.2	10.6	11.8
Net Profit Margin (%)	9.3	8.8	8.0	9.2	10.2
Net Debt/Equity (%)	3.5	-15.0	-15.0	-23.2	-31.2
CAPEX/Sales (%)	2.3	3.2	5.4	5.1	4.9

Disclaimer

1. As of 23 August 2011, Hong Leong Investment Bank Berhad has proprietary interest in the following securities covered in this report:
(a) -.

2. As of 23 August 2011, the analyst, Low Yee Huap who prepared this report, has interest in the following securities covered in this report:
(a) -.

Published & Printed by
Hong Leong Investment Bank Berhad (43526-P)
Level 8, Menara HLA
No. 3, Jalan Kia Peng
50450 Kuala Lumpur
Tel 603 2168 1168 / 603 2710 1168
Fax 603 2161 3880

Equity rating definitions

BUY	Positive recommendation of stock under coverage. Expected absolute return of more than +10% over 12-months, with low risk of sustained downside.
TRADING BUY	Positive recommendation of stock not under coverage. Expected absolute return of more than +10% over 6-months. Situational or arbitrage trading opportunity.
HOLD	Neutral recommendation of stock under coverage. Expected absolute return between -10% and +10% over 12-months, with low risk of sustained downside.
TRADING SELL	Negative recommendation of stock not under coverage. Expected absolute return of less than -10% over 6-months. Situational or arbitrage trading opportunity.
SELL	Negative recommendation of stock under coverage. High risk of negative absolute return of more than -10% over 12-months.
NOT RATED	No research coverage, and report is intended purely for informational purposes.

Industry rating definitions

OVERWEIGHT	The sector, based on weighted market capitalization, is expected to have absolute return of more than +5% over 12-months.
NEUTRAL	The sector, based on weighted market capitalization, is expected to have absolute return between –5% and +5% over 12-months.
UNDERWEIGHT	The sector, based on weighted market capitalization, is expected to have absolute return of less than –5% over 12-months.