Nationgate Holdings

A Hiccup in Its Growth Path

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OUTPERFORM ↔

Price : RM1.21

Target Price : RM1.40 ↓

NATGATE guided for flattish sequential 2QFY23 with only a meaningful pickup in orders seen in 2HFY23. Also, it will be on-boarding 2-3 new customers later this year which will contribute positively to FY23. We moderate our FY23-24F net profit forecasts by 9% and 6%, respectively, reduce TP by 7% to RM1.40 (from RM1.50) but maintain our OUTPERFORM call.

We came away from NATGATE's post-1QFY23 results briefing feeling encouraged of its prospects. The key takeaways are as follows:

1. Despite recognising that 1QFY23 is typically a seasonally weaker period, the group acknowledges that earnings could have been stronger if not for the slowdown in its networking and telco segment (-34% YoY), caused by an inventory realignment exercise by a key customer. The impact continued into April, with meaningful order replenishment only resuming in May. Fortunately, the group's remaining business segments (which makes up c.50% of group revenue) operates on a higher margin consignment arrangement which could cushion the slowdown in the networking and telco segment, which are on a turnkey basis. Consequently, 2QFY23 is expected to exhibit a flat QoQ performance.
2. NATGATE is in discussions with several prospective clients, with 2-3 of them currently in the final stage of negotiation. These clients, from China and Taiwan, are focused on products related to data computing and networking. The group plans to onboard these customers in 2HFY23, employing a consignment arrangement to minimize the risks associated with component shortages or inventory overrun.
3. To cater to the needs of prospective clients, the group is actively building additional capacity on the third floor of its Plant 5 (216k sq ft), adding c.80k sq ft which is set to be completed by July 2023. Moreover, the expansion of Plant 8 which offers another 248k sq ft, is progressing smoothly and anticipated to be finished by December 2023. Overall, these expansions will increase the group's total floor space by approximately 50%.

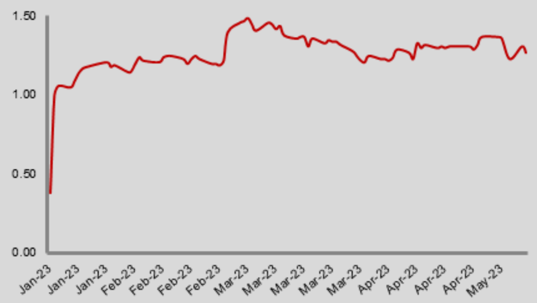
Forecasts. We moderate our FY23-24F net profit forecasts by 9% and 6%, respectively, to reflect the slight delay in order replenishment from its key customer in the optical transceiver space.

Consequently, we trim our TP by 7% to RM1.40 (from RM1.50) based on an unchanged 23x FY24F PER. This represents a 30% premium to peers' forward mean, justified by the group's favourable exposure to the fast-growing networking product segment and its advanced capabilities which yield better margins as well as enhancing customer stickiness. There is no adjustment to our TP based on ESG given a 3-star rating as appraised by us (see Page 4).

Investment thesis. We like NATGATE for its: (i) exposure to the fast-growing industrial and commercial products used in the networking and telecommunication sectors, (ii) 4IR-ready facilities that can take on higher complexity jobs, and (iii) added-value services such as chip-on-board (COB) that enhance customer stickiness and yield better margins. Maintain **OUTPERFORM.**

Risks to our call include: (i) heavy reliance on the networking segment which contributes c.70% of group revenue, (ii) competition from foreign EMS players that have presence in Malaysia, and (iii) adverse impact from component shortage which could delay delivery schedule.

Share Price Performance



KLCI	1,422.9
YTD KLCI chg	-4.9%
YTD stock price chg	226.3%

Stock Information

Shariah Compliant	Yes
Bloomberg Ticker	NATGATE MK Equity
Market Cap (RM m)	2,571.7
Shares Outstanding	2,073.9
52-week range (H)	1.50
52-week range (L)	0.81
3-mth avg daily vol:	7,015,784
Free Float	33.8%
Beta	2.0

Major Shareholders

Ooi Eng Leong	57.9%
Tan Ah Geok	7.2%
Lee Kim San	0.8%

Summary Earnings Table

FYE Dec (RM m)	2022A	2023F	2024F
Turnover	945.7	1,056.2	1,262.5
EBITDA	152.1	173.4	195.5
PBT	85.6	103.1	126.6
Core Net Profit	85.6	103.1	126.6
Consensus	-	110.3	135.5
Earnings Revision	-	-9%	-6%
EPS (sen)	4.1	5.0	6.1
EPS growth (%)	43.8	20.3	22.9
NDPS (sen)	1.0	0.3	0.3
BVPS (RM)	0.11	0.16	0.22
Price/BV (x)	10.7	7.5	5.5
PER (x)	28.6	23.7	19.3
Net Gearing (x)	1.4	0.6	0.5
ROA (%)	11.2	10.6	9.9
ROE (%)	37.4	31.5	28.2
Dividend Yield (%)	0.8	0.2	0.2

Income Statement

FY Dec (RM m)	2020A	2021A	2022F	2023F	2024F
Revenue	566.2	760.9	945.7	1,056.2	1,262.5
EBITDA	57.3	95.7	152.1	173.4	195.5
Depre & Amor	-19.7	-25.9	-35.1	-37.1	-32.6
Operating Profit	37.5	69.9	117.0	136.3	162.9
Other Income	1.4	1.7	6.0	2.1	2.5
Interest Exp	-4.6	-7.2	-12.4	-10.6	-8.5
Associate	0.0	0.0	0.0	0.0	0.0
PBT	32.9	62.7	104.6	125.7	154.4
Taxation	-2.2	-3.1	-19.0	-22.6	-27.8
Minority Interest	0.0	0.0	0.0	0.0	0.0
Net Profit	30.7	59.5	85.6	103.1	126.6
Core Net Profit	30.7	59.5	85.6	103.1	126.6

Balance Sheet

FY Dec (RM m)	2020A	2021A	2022F	2023F	2024F
Fixed Assets	182.5	209.7	235.5	206.6	183.8
Intangible Assets	0.0	0.0	0.0	0.0	0.0
Other FA	0.8	0.4	25.5	25.5	25.5
Inventories	100.1	152.8	187.2	208.2	245.2
Receivables	147.7	166.6	220.7	246.5	294.6
Other CA	22.6	31.0	40.1	40.1	40.1
Cash	18.2	45.6	53.4	244.6	484.9
Total Assets	**472.1**	**606.2**	**762.4**	**971.4**	**1,274.0**
Payables	203.0	216.3	179.8	200.0	347.0
ST Borrowings	76.4	143.0	250.3	144.8	144.8
Other ST Liability	1.8	1.1	19.1	215.6	249.7
LT Borrowings	78.0	87.1	67.5	67.5	67.5
Other LT Liability	0.5	0.3	16.6	16.6	16.6
Net Assets	**112.4**	**158.4**	**229.1**	**326.9**	**448.4**
Shr. Equity	112.0	155.9	229.1	326.9	448.4
Mnrt. Interest	0.3	2.6	0.0	0.0	0.0
Total Equity	**112.4**	**158.4**	**229.1**	**326.9**	**448.4**

Cashflow Statement

FY Dec (RM m)	2020A	2021A	2022A	2023F	2024F
Operating CF	45.8	28.9	20.6	108.2	191.3
Investing CF	-39.6	-27.2	-56.0	-8.2	-9.8
Financing CF	6.1	26.1	36.7	97.6	58.8

Financial Data & Ratios

FY Dec	2020A	2021A	2022A	2023F	2024F
Growth (%)					
Turnover	73.7	34.4	24.3	11.7	19.5
EBITDA	126.5	67.1	58.9	14.0	12.7
Operating Profit	286.8	86.1	67.5	16.5	19.5
PBT	420.5	90.4	67.0	20.1	22.9
Adj Net Profit	482.6	94.2	43.8	20.3	22.9
Profitability (%)					
EBITDA Margin	10.1	12.6	16.1	16.4	15.5
Operating Margin	6.6	9.2	12.4	12.9	12.9
PBT Margin	5.8	8.2	11.1	11.9	12.2
Core Net Margin	5.4	7.8	9.1	9.8	10.0
Effective Tax Rate	6.8	5.0	18.2	18.0	18.0
ROA	6.1	6.5	9.8	11.2	10.6
ROE	27.4	38.2	37.4	31.5	28.2
DuPont Analysis					
Assets Turnover (x)	1.2	1.3	1.2	1.1	1.0
Leverage Factor (x)	4.2	3.8	3.3	3.0	2.8
ROE (%)	27.4	38.2	37.4	31.5	28.2
Leverage					
Debt/Asset (x)	0.3	0.4	0.4	0.2	0.2
Debt/Equity (x)	1.4	1.5	1.4	0.6	0.5
Net (Cash)/Debt	136.1	184.5	264.4	-32.3	-272.6
Net Debt/Equity (x)	1.2	1.2	1.2	-0.1	-0.6
Valuations					
Core EPS (sen)	1.5	2.9	4.1	5.0	6.1
DPS (sen)	0.2	0.6	1.0	0.3	0.3
BVPS (RM)	0.1	0.1	0.1	0.2	0.2
PER (x)	79.8	41.1	28.6	23.7	19.3
Div. Yield (%)	0.2	0.5	0.8	0.2	0.2
P/BV (x)	21.8	15.7	10.7	7.5	5.5
EV/EBITDA (x)	47.3	45.1	27.5	17.8	13.9

Source: Kenanga Research

Malaysian Technology Peers Comparison

Name	Rating	Last Price (RM)	Target Price (RM)	Upside (%)	Mkt Cap (RM'm)	Shariah Compliant	Current FYE	Core EPS (sen)		Core EPS Growth		PER (x) – Core Earnings		PBV (x)	ROE (%)	Net. Div. (sen)	Net. Div. Yld (%)
								1-Yr. Fwd.	2-Yr. Fwd.	1-Yr. Fwd.	2-Yr. Fwd.	1-Yr. Fwd.	2-Yr. Fwd.	1-Yr. Fwd.	1-Yr. Fwd.	1-Yr. Fwd.	1-Yr. Fwd.
D&O GREEN TECHNOLOGIES BHD	UP	3.85	3.51	-8.83%	4,765.5	Y	12/2023	10.3	14.0	31.6%	35.5%	37.2	27.5	5.0	14.0%	1.7	0.4%
GHL SYSTEMS BHD	OP	0.790	1.05	32.91%	896.1	Y	12/2023	3.0	3.4	21.3%	12.9%	26.3	23.4	1.7	6.5%	0.0	0.0%
INARI AMERTRON BHD	MP	2.26	2.46	8.85%	8,436.4	Y	06/2023	9.0	10.2	-14.1%	13.1%	25.1	22.2	3.3	13.3%	8.6	3.8%
JHM CONSOLIDATION BHD	MP	0.730	0.800	9.59%	439.4	Y	12/2023	5.3	5.9	40.0%	10.6%	13.7	12.4	1.3	9.8%	0.5	0.7%
KELINGTON GROUP BHD	OP	1.36	1.92	41.18%	874.5	Y	12/2023	8.7	9.0	1.1%	3.2%	15.6	15.1	3.1	21.3%	2.4	1.8%
KESM INDUSTRIES BHD	MP	6.81	6.91	1.47%	292.9	Y	07/2023	(15.8)	1.2	-3500.0%	-92.6%	N.A.	549.6	0.8	-1.9%	7.5	1.1%
LGMS BHD	OP	1.09	1.50	37.61%	497.0	Y	12/2023	3.5	5.9	26.2%	69.8%	31.3	18.4	5.0	17.4%	0.0	0.0%
M'SIAN PACIFIC INDUSTRIES BHD	UP	25.72	15.26	-40.67%	5,115.6	Y	06/2023	41.8	105.8	-74.7%	153.3%	61.2	24.3	2.5	4.1%	35.0	1.4%
NATGATE HOLDINGS BHD	OP	1.21	1.40	15.70%	2,509.5	Y	12/2023	5.0	6.1	20.4%	22.8%	24.3	19.8	7.7	37.1%	0.3	0.2%
OPPSTAR BHD	UP	1.89	1.30	-31.22%	1,202.4	N	12/2023	3.1	4.0	18.1%	29.6%	61.4	47.4	41.8	90.7%	0.8	0.4%
P.I.E. INDUSTRIAL BHD	OP	3.35	4.05	20.90%	1,286.5	Y	12/2023	22.5	25.3	22.0%	12.5%	14.9	13.2	2.1	14.6%	7.0	2.1%
SKP RESOURCES BHD	UP	0.990	1.20	21.21%	1,546.7	Y	03/2023	9.7	7.9	-11.1%	-17.9%	10.2	12.5	1.7	17.8%	4.8	4.8%
UNISEM (M) BHD	MP	2.86	2.75	-3.85%	4,613.4	Y	12/2023	8.9	13.8	-41.2%	55.7%	18.6	16.7	1.9	5.9%	6.0	2.1%
Simple Average										-22.4%	28.6%	27.5	21.4	6.0	19.3%		1.5%

Source: Kenanga Research

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Stock ESG Ratings:

	Criterion	Rating				
GENERAL	Earnings Sustainability & Quality	★	★	★	☆	
	Community Investment	★	★	☆		
	Workers Safety & Wellbeing	★	★	★		
	Corporate Governance	★	★	★		
	Anti-Corruption Policy	★	★	★		
	Emissions Management	★	★	★		
SPECIFIC	Technology & Innovation	★	★	★	☆	
	Supply Chain Management	★	★	★		
	Energy Efficiency	★	★	★		
	Effluent/Water Management	★	★	★		
	Waste Management	★	★	★		
	Ethical Practices	★	★	★	☆	
	OVERALL	★	★	★		

☆ denotes half-star
★ -10% discount to TP
★★ -5% discount to TP
★★★ TP unchanged
★★★★ +5% premium to TP
★★★★★ +10% premium to TP

Stock Ratings are defined as follows:

Stock Recommendations

OUTPERFORM : A particular stock's Expected Total Return is MORE than 10%
MARKET PERFORM : A particular stock's Expected Total Return is WITHIN the range of -5% to 10%
UNDERPERFORM : A particular stock's Expected Total Return is LESS than -5%

Sector Recommendations***

OVERWEIGHT : A particular sector's Expected Total Return is MORE than 10%
NEUTRAL : A particular sector's Expected Total Return is WITHIN the range of -5% to 10%
UNDERWEIGHT : A particular sector's Expected Total Return is LESS than -5%

******Sector recommendations are defined based on market capitalisation weighted average expected total return for stocks under our coverage.***

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