Company Report
Micro-Mechanics (Holdings) Ltd - Initiation

Singapore Strategy Update
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Micro-Mechanics (Holdings) Ltd

High margin, High ROE consumables business

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Paul Chew
Phillip Securities Research Pte Ltd
25 Sept 2017
Micro-Mechanics Holdings Ltd (BUY, TP:S$2.00, Last: S$1.545)

• Background
  ➢ Founded 34 years ago with now five plants across SG, MY, PH, CH, USA
  ➢ Manufactures precision tools and consumable products for the semiconductor industry
  ➢ Building up capabilities to serve the front-end of the semiconductor industry through its US operations.

• Investment merits
  ➢ A 60%-margin, 30%-ROE consumables business
  ➢ 15-year earnings CAGR of 20%, unlevered returns and pays 5% yield
  ➢ MMH Jun 17 quarter earnings jumped by 60% YoY, expect the momentum to sustain

• Valuations
  ➢ Our target price pegs MMH at 15x PE FY/18e, in-line with peers in the back-end semiconductor supply chain
  ➢ We believe this is conservative given its superior margins, ROE and dividend yield.
MMH is focused on 2 steps of the back-end semiconductor process

1. Die attach: Pick up die from wafer and place onto the leadframe. MMH produces the rubber/plastic tips and metal tool.

Source: Company, PSR

Source: Kulicke & Soffa

Source: Company
2. Wire bonding: Connect wires of the die onto the leadframe. MMH produces the clamp to hold the leadframe while the wire-bonding process occurs.
3. Front-end semiconductor parts: Parts used in the vapour deposition and etch machine. Small losses at present but strategy to penetrate front-end market.

Source: Company
Micro-Mechanics Holdings Ltd – Competitive Advantages

- Increased miniaturization - dies sizes are now as small as 1mm² to 10mm²

- Complex material engineering - materials must avoid electrostatic discharge (ESG) that can burn the semiconductor chip

- Need for customization - every customer will require some level of customization for their tools despite some using the same die attach or wire bonding machine

- High quality and reliability - accuracy in placing the die now encroaching the 3 micrometres - high volume and automated process in die attach - size and fragility of the die,
Micro-Mechanics Holdings Ltd – What we like about MMH?

• Huge margins - gross margins averaged 55% over the past 5 years; recent quarter margin almost 60%; easily double of the industry average

• Great track record – past 15 years earnings CAGR 20%; 5-year track record for earnings is now 28% CAGR

• Health balance sheet - no leverage on its balance sheet for past 15 years; S$22m net cash

• Consumable nature of the product - to be replaced every 8-hour shift by the customer

• Huge growth opportunity ahead - grow 9% per year on a per unit basis from 2016 till 2021, according to Gartner; from lighting, vehicles, IOT, solid state memory, wearable.

• Advanced packaging - requirement for the pick and placing of dies becomes ever more critical; for instance, flip chip and wafer level packaging
Micro-Mechanics Holdings Ltd – Outlook

- Robust revenue and earnings growth expected
  - Revenue has a close correlation with semiconductor industry revenues.
  - Jun 17 quarter earnings jumped by 60% YoY
  - Latest July 2017 semiconductor sales growth was 24%, fastest pace of growth in almost 7 years. Late 2016 only saw the pick-up in industry semiconductor sales.
Micro-Mechanics Holdings Ltd – Valuation

- Target price of 15x in line with industry
  - Conservative valuation considering superior margins, ROE and dividend yield.

<table>
<thead>
<tr>
<th>Company</th>
<th>1 Mth Perf.</th>
<th>3 Mth Perf.</th>
<th>YTD Perf.</th>
<th>Share Price</th>
<th>Mkt. Cap. (US$ m)</th>
<th>PE</th>
<th>Yr 0</th>
<th>Yr + 1</th>
<th>Yr + 2</th>
<th>Dividend Yield</th>
<th>ROE Yr 0</th>
<th>EV/EBITDA</th>
<th>EBITDA Margin</th>
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<td>14.2</td>
<td>13.5</td>
<td>12.2</td>
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<td>3.7%</td>
<td>14.8%</td>
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<td>15.9</td>
<td>14.0</td>
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<td>3.7%</td>
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<td>15.1</td>
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Source: Bloomberg, PSR, Prices as at 20Sep17

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Singapore Strategy update

Paul Chew
Phillip Securities Research Pte Ltd
25 Sept 2017
Singapore strategy update – September

• Maintain Neutral: STI Target 3270 unchanged

• Macro
  ➢ Fed meeting: December rate hike expected; limited impact on USD and yields unless tax cuts happen
  ➢ Near term data distortion from US due to hurricane and China due to production cuts in winter
  ➢ Singapore macro: robust exports (YTD17 fastest in six years); PMI new order suggest trend to sustain

• BUY sustainable yield, property, coal and economic momentum
  ➢ Yield: AsianPayTV, CCT, MINT, Ascendas REIT / Property: CapitaLand, Wheelock, Chip Eng Seng
  ➢ Banyan Tree: large pipeline of hotel-management contracts for the next several years
  ➢ Coal: strong production and beneficiary of SOE reform
  ➢ DBS: 3 tailwinds of rising SIBOR + healthy capital markets + improving domestic economy
  ➢ Micro-mechanics: proxy to surge in semiconductor sales

• Sector updates
  ➢ Domestic retail sector still soft: retail but construction and materials recovering
  ➢ Hopes of strong hospitality fizzled out in Jul17 data
  ➢ Property sales up 60% YoY in August17, 2017 on track for best sales in five years
Singapore Coal Sector Video

Available on PhillipCapital YouTube channel
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