



KCE Electronics

(KCE.BK/KCE TB) *

Neutral-Maintained

Price as of 9 May 2018	70.50
12M target price (Bt/share)	65.00
Unchanged/Revised up (down) (%)	Unchanged
Upside/downside (%)	(7.8)

Key messages

Performance improvement in both sales and gross margin would proceed gradually. However, we remain cautious as we do not see any earnings upside to our recent earnings forecast. We recommend investor to keep an eye on KCE's 2Q18 performance in order to look for the right time to take exposure again. We maintain a rating of Neutral with a 2018 target price of Bt65.00 based on multiple PER 16.0X (+0.5 S.D. sector average).

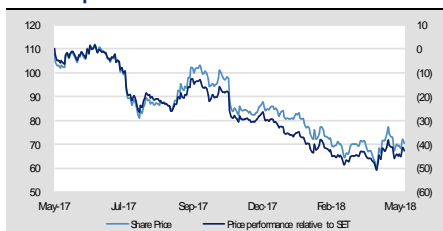
Trading data

Mkt cap (Btbn/US\$mn)	41.3/1,034
Outstanding share (mn)	586
Foreign ownership (mn)	167
3M avg. daily trading (mn)	3
52-week trading range (Bt)	60.3-112
Performance (%)	3M 6M 3M
Absolute	-5.70 -15.8 -36.5
Relative	-4.10 -19.0 -44.0

Quarterly EPS

EPS	Q1	Q2	Q3	Q4
2015	0.90	0.86	1.00	1.16
2016	1.30	1.39	1.34	1.18
2017	1.13	1.15	1.04	1.02
2018	0.88			

Share price chart



Source: SET

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Waiting for the right time

Event

Company update.

Impact

Positive signs for sales in US dollar terms

KCE maintained its 2018 sales growth target in US dollar terms at 12%-15% versus our assumption of 10%. The company expects sales to show some improvement going forward as new machinery has been set up that would relieve the bottleneck problem. To confirm the easing of the bottleneck problem and to achieve the company's sales growth target, we should see higher sales in US dollar terms from 2Q18 onward.

Development of gross margin would be seen

KCE should improve its gross margin step by step this year with i) better production efficiency after installing new machinery, and ii) cost pressure easing from 2017 (both copper and exchange rate). Since there should be less volatility in copper price and exchange rate than last year, KCE's operation should be more easily managed than in 2017. As a result, we believe gross margin through the rest of 2018 should be above the 25.8% recorded in 1Q18. However, we do not believe gross margin will surpass our assumption of 30.2%, and there may be some downside.

Waiting for a good time to enter again

Although sales and profitability are poised to signal some recovery, we expect the momentum to be gradual. Hence, we do not believe it is the right time to take a position in KCE as we do not see any upside to our forecast. Given upside risk from sales growth (our assumption of 10% vs. company target 12%-15%) and downside risk from gross margin (our assumption of 30.2% vs. 1Q18 of 25.8%), we expect this could be offset and allowing our 2018 earnings remain intact.

Valuation & Action

We maintain a rating of Neutral on KCE with a 2018 target price of Bt65.00 based on PER 16.0x (+0.5 S.D. sector average). We remain cautious toward the counter and recommend investors to keep an eye on the company's improvement in 2Q18 in both sales in US dollar terms and gross margin to confirm an upbeat outlook and the proper time to take exposure in KCE in the second half of 2018 and 2019.

Risks

Natural disasters, unplanned plant shutdowns, customers shifting to other suppliers, increasing raw material prices and Bt/US\$ appreciation (our assumption is Bt30.9/US\$ in 2018).

Key financials and valuations

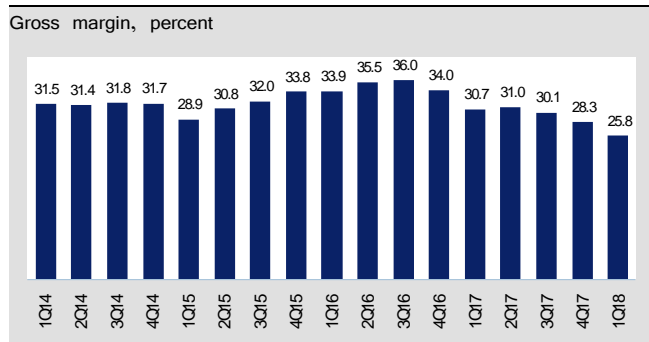
	Dec - 16A	Dec - 17A	Dec - 18F	Dec - 19F	Dec - 20F
Revenue (Btmn)	13,797	14,195	14,348	15,440	16,002
Gross Profit (Btmn)	4,813	4,262	4,330	4,730	4,925
SG&A (Btmn)	1,695	1,818	1,851	1,962	2,033
Net Profit (Btmn)	3,039	2,545	2,404	2,712	2,858
Normalized Profit (Btmn)	2,912	2,341	2,404	2,712	2,858
EPS(Bt)	5.18	4.34	4.10	4.63	4.87
Normalized EPS(Bt)	4.97	3.99	4.10	4.63	4.87
DPS(Bt)	2.10	1.74	1.64	1.85	1.95
EPS Growth (%)	33.0	(16.3)	(5.5)	12.8	5.4
Normalized EPS Growth	30.3	(19.6)	2.7	12.8	5.4
P/E (X)	23.5	16.2	17.2	15.2	14.5
P/B (X)	7.1	3.7	3.2	2.9	2.6
EV/EBITDA (X)	10.6	11.7	11.7	10.5	9.7
Net Debt to Equity (%)	36.3	21.1	8.3	(4.8)	(16.3)
Dividend Yield (%)	1.7	2.5	2.3	2.6	2.8
Return on Average Equity (%)	30.3	22.6	18.9	18.9	17.8

Source: Company data, KGI Research

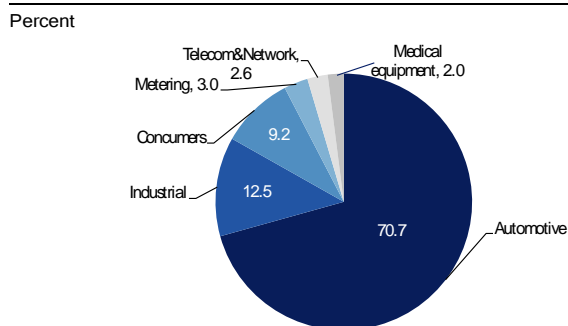
Figure 1: Company profile

KCE Electronics PCL (KCE), originally known as Kuang Charoen Electronics Company Limited, was established on November 5, 1982, with initial registered capital of Bt12.0mn. The company's core business is to produce and distribute custom printed circuit boards (PCBs), which are manufactured from copper clad laminate under the KCE trademark. KCE's PCB products are well-known and used in a variety of applications such as automotive, industrial, computer, and telecom systems. Its customers consist of the world's biggest names.

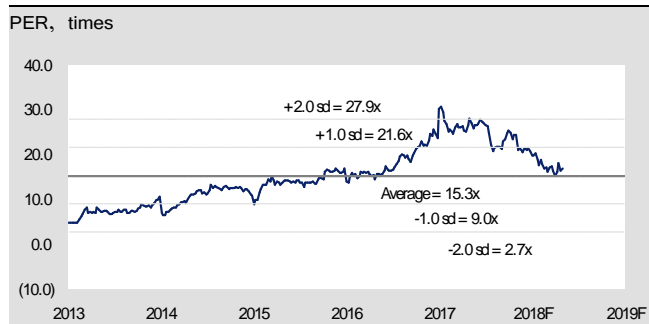
Source: Company data

Figure 3: Gross margin dropped


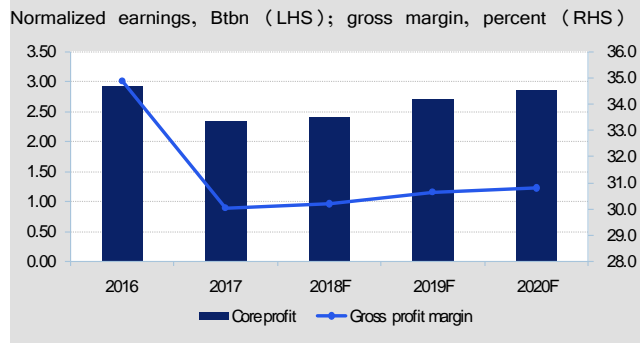
Source: Company data, KGI Research

Figure 5: KCE's main production segment is automotive


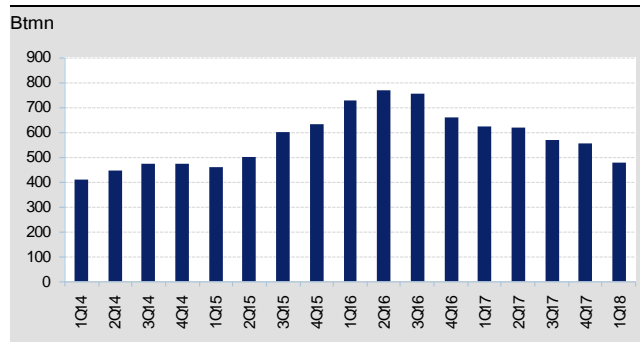
Source: Company data, KGI Research

Figure 7: Company's PER


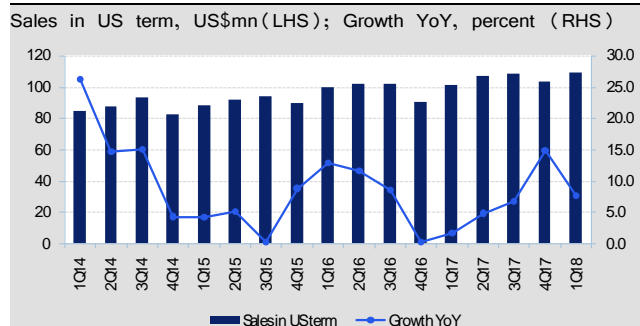
Source: KGI Research

Figure 2: Core profit flat in 2018


Source: Company data, KGI Research

Figure 4: Core profit quarterly


Source: Company data, KGI Research

Figure 6: Sales in US term


Source: Company data, KGI Research

Figure 8: Company's PBV


Source: KGI Research

Quarterly Income Statement

	Mar-14A	Jun-14A	Sep-14A	Dec-14A	Mar-15A	Jun-15A	Sep-15A	Dec-15A	Mar-16A	Jun-16A	Sep-16A	Dec-16A	Mar-17A	Jun-17A	Sep-17A	Dec-17A	Mar-18A
Income Statement (Bt mn)																	
Revenue	2,765	2,819	2,999	2,702	2,882	3,047	3,301	3,218	3,529	3,579	3,515	3,174	3,536	3,664	3,602	3,393	3,440
Cost of Goods Sold	(1,893)	(1,932)	(2,047)	(1,846)	(2,050)	(2,110)	(2,243)	(2,131)	(2,331)	(2,309)	(2,251)	(2,094)	(2,452)	(2,528)	(2,519)	(2,433)	(2,551)
Gross Profit	872	886	952	856	832	937	1,058	1,087	1,198	1,270	1,264	1,080	1,084	1,135	1,083	960	889
Operating Expense	(443)	(417)	(441)	(382)	(344)	(383)	(434)	(359)	(423)	(454)	(437)	(381)	(444)	(485)	(485)	(404)	(466)
Other incomes	13	19	15	12	9	20	37	(31)	9	17	12	17	23	18	22	54	93
Operating Profit	442	488	527	485	496	575	660	697	784	833	839	716	663	668	619	609	516
Depreciation of fixed asset	(133)	(137)	(141)	(143)	(136)	(153)	(195)	(199)	(203)	(211)	(216)	(219)	(217)	(220)	(222)	(224)	(230)
Operating EBITDA	575	626	668	628	632	728	855	896	987	1,044	1,056	935	881	889	842	834	746
Non-Operating Income	29	34	140	109	54	(12)	(28)	35	23	43	30	29	39	56	45	45	41
Interest Income	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0
Other Non-op Income	29	34	140	109	54	(12)	(28)	35	23	43	30	29	39	56	45	45	41
Non-Operating Expense	(32)	(34)	(29)	(23)	(21)	(35)	(49)	(48)	(46)	(46)	(42)	(37)	(30)	(33)	(32)	(32)	(29)
Interest Expense	(32)	(34)	(29)	(23)	(21)	(35)	(49)	(48)	(46)	(46)	(42)	(37)	(30)	(33)	(32)	(32)	(29)
Other Non-op Expense	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0
Equity Income/(Loss)	11	9	7	7	3	6	10	2	6	7	10	6	4	6	5	6	4
Pre-tax profit	450	497	645	578	531	534	593	686	767	837	837	714	676	698	638	629	532
Current Taxation	(7)	(14)	(30)	5	(17)	(40)	(17)	(18)	(10)	(20)	(47)	(21)	(10)	(21)	(21)	(27)	(10)
Minorities	3	4	3	3	3	4	3	3	6	5	4	3	4	5	5	5	5
Extraordinary items																	
Net Profit	439	479	611	580	511	490	573	665	751	812	786	690	662	672	612	598	517
Normalized Profit	411	445	471	472	457	502	602	631	728	768	756	661	623	616	567	552	476
EPS(Bt)	0.80	0.86	1.08	1.03	0.90	0.86	1.00	1.16	1.30	1.39	1.34	1.18	1.13	1.15	1.04	1.02	0.88
Normalized EPS(Bt)	0.75	0.80	0.83	0.83	0.80	0.88	1.05	1.10	1.26	1.31	1.29	1.13	1.06	1.05	0.97	0.94	0.81
Margins																	
Gross profit margin	31.5	31.4	31.8	31.7	28.9	30.8	32.0	33.8	33.9	35.5	36.0	34.0	30.7	31.0	30.1	28.3	25.8
Operating EBIT margin	16.0	17.3	17.6	18.0	17.2	18.9	20.0	21.7	22.2	23.3	23.9	22.6	18.8	18.2	17.2	18.0	15.0
Operating EBITDA margin	20.8	22.2	22.3	23.3	21.9	23.9	25.9	27.8	28.0	29.2	30.0	29.5	24.9	24.3	23.4	24.6	21.7
Net profit margin	15.9	17.0	20.4	21.5	17.7	16.1	17.4	20.7	21.3	22.7	22.4	21.7	18.7	18.4	17.0	17.6	15.0
Growth																	
Revenue growth	10.9	1.9	6.4	(9.9)	6.7	5.7	8.3	(2.5)	9.7	1.4	(1.8)	(9.7)	11.4	3.6	(1.7)	(5.8)	1.4
Operating EBIT growth	13.1	10.5	8.0	(7.9)	2.2	15.8	14.9	5.6	12.5	6.2	0.8	(14.7)	(7.4)	0.8	(7.3)	(1.6)	(15.3)
Operating EBITDA growth	12.8	8.8	6.8	(5.9)	0.7	15.0	17.6	4.7	10.1	5.8	1.2	(11.4)	(5.9)	0.9	(5.3)	(1.0)	(10.5)
Net profit growth	16.8	9.0	27.6	(5.0)	(11.9)	(4.1)	17.0	16.0	12.9	8.1	(3.2)	(12.2)	(4.0)	1.5	(8.9)	(2.4)	(13.5)
Normalized profit growth	19.6	8.3	5.8	0.2	(3.0)	9.8	19.8	4.8	15.4	5.6	(1.7)	(12.5)	(5.8)	(1.1)	(7.9)	(2.6)	(13.9)

Source: KGI Research

Balance Sheet

As of 31 Dec (Bt mn)	2016	2017	2018F	2019F	2020F
Total Assets	17,328	17,850	18,365	19,403	20,428
Current Assets	7,296	7,505	8,207	9,643	11,030
Cash & ST Investment	892	1,140	1,567	2,514	3,647
Inventories	2,265	2,428	2,470	2,641	2,731
Account Receivable	4,080	3,876	4,127	4,442	4,603
Others	59	61	43	46	48
Non-current Assets	10,032	10,346	10,158	9,759	9,398
LT Investment	318	276	318	318	318
Net fixed Assets	9,137	9,510	9,259	8,833	8,450
Others	576	560	581	608	630
Total Liabilities	7,300	6,576	5,639	5,049	4,360
Current Liabilities	4,944	4,595	4,152	4,046	3,849
Account Payable	2,520	2,802	2,745	2,934	3,035
ST Borrowing	1,808	1,156	856	556	256
Others	616	636	552	556	558
Long-term Liabilities	2,356	1,981	1,487	1,003	511
Long-term Debts	2,155	1,771	1,271	771	271
Others	201	210	215	232	240
Shareholders' Equity	10,028	11,274	12,726	14,354	16,068
Common Stock	586	586	586	586	586
Capital Surplus	1,895	1,907	1,907	1,907	1,907
Retained Earnings	7,478	8,732	10,175	11,802	13,517
Preferred Stock	0	0	0	0	0

Source: KGI Research

Key Ratios

Year to 31 Dec	2016	2017	2018F	2019F	2020F
Growth (%YoY)					
Sales	10.8	2.9	1.1	7.6	3.6
OP	30.6	(19.8)	0.9	11.5	4.4
EBITDA	31.3	(12.5)	(3.0)	7.6	2.2
NP	35.7	(16.3)	(5.5)	12.8	5.4
Normalized Profit	32.8	(19.6)	2.7	12.8	5.4
EPS	33.0	(16.3)	(5.5)	12.8	5.4
Normalized EPS	30.3	(19.6)	2.7	12.8	5.4
Profitability (%)					
Gross Margin	34.9	30.0	30.2	30.6	30.8
Operating Margin	23.0	17.9	17.9	18.5	18.7
EBITDA Margin	30.3	25.7	24.7	24.7	24.3
Net Margin	22.0	17.9	16.8	17.6	17.9
ROAA	17.5	14.3	13.1	14.0	14.0
ROAE	30.3	22.6	18.9	18.9	17.8
Stability					
Gross Debt/Equity (%)	0.7	0.6	0.4	0.4	0.3
Net Debt/Equity (%)	0.4	0.2	0.1	(0.0)	(0.2)
Interest Coverage (x)	19.4	21.8	28.2	43.3	70.6
Interest & ST Debt Coverage (x)	1.7	2.2	2.7	4.6	10.1
Cash Flow Interest Coverage (x)	23.7	29.6	32.9	50.2	84.2
Cash Flow/Interest & ST Debt (x)	2.1	2.9	3.2	5.4	12.0
Current Ratio (x)	1.5	1.6	2.0	2.4	2.9
Quick Ratio (x)	1.0	1.1	1.4	1.7	2.2
Net Debt (Bt mn)	3,637	2,380	1,061	(687)	(2,620)
Per Share Data (Bt)					
EPS	5.2	4.3	4.1	4.6	4.9
Normalized EPS	5.0	4.0	4.1	4.6	4.9
CFPS	6.9	6.4	5.2	5.7	6.1
BVPS	17.1	19.2	21.7	24.5	27.4
SPS	23.5	24.2	24.5	26.3	27.3
EBITDA/Share	7.1	6.2	6.0	6.5	6.6
DPS	2.1	1.7	1.6	1.9	1.9
Activity					
Asset Turnover (x)	0.8	0.8	0.8	0.8	0.8
Days Receivables	108	100	105	105	105
Days Inventory	92	89	90	90	90
Days Payable	102	103	100	100	100
Cash Cycle	98	86	95	95	95

Source: KGI Research

Profit & Loss

Year to Dec 31 (Bt mn)	2016	2017	2018F	2019F	2020F
Revenue	13,797	14,195	14,348	15,440	16,002
Cost of Goods Sold	(8,985)	(9,933)	(10,018)	(10,711)	(11,077)
Gross Profit	4,813	4,262	4,330	4,730	4,925
Operating Expenses	(1,695)	(1,818)	(1,851)	(1,962)	(2,033)
Other Incomes	54	98	86	93	96
Operating Profit	3,171	2,543	2,566	2,860	2,988
Depreciation of fixed assets	(849)	(884)	(951)	(926)	(883)
Operating EBITDA	4,176	3,653	3,542	3,811	3,896
Non-Operating Income	127	203	0	0	0
Interest Income					
Other Non-op Income	127	203	0	0	0
Non-Operating Expense	(171)	(127)	(92)	(67)	(43)
Interest Expense	(171)	(127)	(92)	(67)	(43)
Other Non-op Expense	0	0	0	0	0
Equity Income/(Loss)	28	22	25	25	25
Pretax Profit	3,155	2,641	2,499	2,819	2,970
Current Taxation	(98)	(78)	(77)	(87)	(92)
Minorities	18	18	17	19	20
Extraordinaries items	0	0	0	0	0
Net Profit	3,039	2,545	2,404	2,712	2,858
Normalized Profit	2,912	2,341	2,404	2,712	2,858
EPS(Bt)	5.18	4.34	4.10	4.63	4.87
Normalized EPS(Bt)	4.97	3.99	4.10	4.63	4.87

Source: KGI Research

Cash Flow

Year to 31 Dec (Bt mn)	2016	2017	2018F	2019F	2020F
Operating Cash Flow	4,069	3,758	3,031	3,350	3,593
Net Profit	3,039	2,545	2,404	2,712	2,858
Depreciation & Amortization	849	884	951	926	883
Change in Working Capital	181	329	(325)	(288)	(148)
Others					
Investment Cash Flow	(956)	(1,203)	(759)	(517)	(517)
Net CAPEX	(770)	(1,257)	(700)	(500)	(500)
Change in LT Investment	(211)	42	(42)	0	0
Change in Other Assets	25	12	(17)	(17)	(17)
Free Cash Flow	3,114	2,555	2,271	2,833	3,076
Financing Cash Flow	(2,895)	(2,307)	(1,844)	(1,885)	(1,943)
Change in Share Capital	11	0	0	0	0
Net Change in Debt	(1,784)	(1,009)	(892)	(800)	(800)
Change in Other LT Liab.	(1,123)	(1,298)	(952)	(1,085)	(1,143)
Net Cash Flow	218	248	427	948	1,133

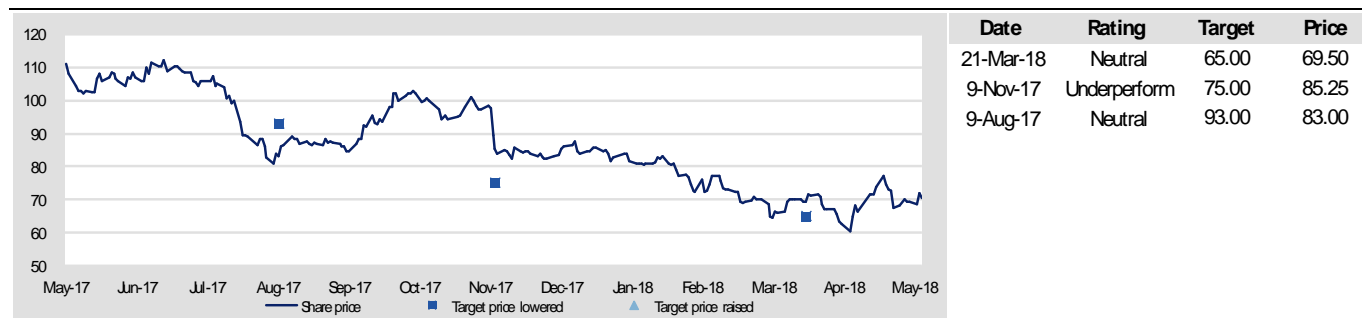
Source: KGI Research

Rates of Return on Invested Capital

Year	1- $\frac{\text{COGS}}{\text{Revenue}}$	+ $\frac{\text{Depreciation}}{\text{Revenue}}$	+ $\frac{\text{Operating Exp.}}{\text{Revenue}}$	= $\frac{\text{Operating Margin}}{\text{Revenue}}$
2016	65.1%	6.2%	12.7%	16.1%
2017	70.0%	6.2%	13.5%	10.3%
2018F	69.8%	6.6%	13.5%	10.1%
2019F	69.4%	6.0%	13.3%	11.3%
2020F	69.2%	5.5%	13.3%	11.9%
Year	1/ $\frac{\text{Working Capital}}{\text{Revenue}}$	+ $\frac{\text{Net PPE}}{\text{Revenue}}$	+ $\frac{\text{Other Assets}}{\text{Revenue}}$	= $\frac{\text{Capital Turnover}}{\text{Revenue}}$
2016	0.0	0.7	0.6	0.8
2017	0.0	0.7	0.6	0.8
2018F	(0.0)	0.6	0.6	0.8
2019F	(0.0)	0.6	0.7	0.8
2020F	(0.0)	0.5	0.7	0.8
Year	Operating Margin	x $\frac{\text{Capital Turnover}}{\text{Revenue}}$	x $\frac{\text{Cash Tax Rate}}{\text{Revenue}}$	= $\frac{\text{After-tax Return on Inv. Capital}}{\text{Revenue}}$
2016	16.1%	0.8	3.1%	0.4%
2017	10.3%	0.8	3.0%	0.2%
2018F	10.1%	0.8	3.1%	0.2%
2019F	11.3%	0.8	3.1%	0.3%
2020F	11.9%	0.8	3.1%	0.3%

Source: KGI Research

KCE Electronics - Recommendation & target price history



Source: KGI Research

KGI Locations

China	Shanghai	Room 1507, Park Place, 1601 Nanjing West Road, Jingan District, Shanghai, PRC 200040
	Shenzhen	Room 24D1, 24/F, A Unit, Zhen Ye Building, 2014 Bao'annan Road, Shenzhen, PRC 518008
Taiwan	Taipei	700 Mingshui Road, Taipei, Taiwan Telephone 886.2.2181.8888 · Facsimile 886.2.8501.1691
Hong Kong		41/F Central Plaza, 18 Harbour Road, Wanchai, Hong Kong Telephone 852.2878.6888 Facsimile 852.2878.6800
Thailand	Bangkok	8th - 11th floors, Asia Centre Building 173 South Sathorn Road, Bangkok 10120, Thailand Telephone 66.2658.8888 Facsimile 66.2658.8014
Singapore		4 Shenton Way #13-01 SGX Centre 2 Singapore 068807 Telephone 65.6202.1188 Facsimile 65.6534.4826

KGI's Ratings

Rating	Definition
Outperform (OP)	The stock's excess return over the next twelve months is ranked in the top 40% of KGI's coverage universe in the related market (e.g. Taiwan)..
Neutral (N)	The stock's excess return over the next twelve months is ranked in the range between the top 40% and the bottom 40% of KGI's coverage universe in the related market (e.g. Taiwan)
Under perform (U)	The stock's excess return over the next twelve months is ranked in the bottom 40% of KGI's coverage universe in the related market (e.g. Taiwan).
Not Rated (NR)	The stock is not rated by KGI.
Restricted (R)	KGI policy and/or applicable law regulations preclude certain types of communications, including an investment recommendation, during the course of KGI's engagement in an investment banking transaction and in certain other circumstances. <i>Excess return = 12M target price/current price-</i>
Note	When an analyst publishes a new report on a covered stock, we rank the stock's excess return with those of other stocks in KGI's coverage universe in the related market. We will assign a rating based on its ranking. If an analyst does not publish a new report on a covered stock, its rating will not be changed automatically.

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