Fu Yu Corp

Bloomberg: FUYU SP | Reuters: FUYU.SI

Refer to important disclosures at the end of this report

DBS Group Research . Equity

15 Jan 2020

BUY

(Initiating Coverage)

Last Traded Price (14 Jan 2020): S$0.25 (**STI :** 3,270.54)
Price Target 12-mth: S$0.35 (40% upside)

Potential Catalyst: Higher manufacturing data print, further improvement in margins

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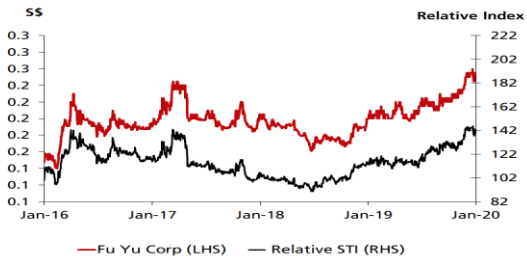
Price Relative



Forecasts and Valuation

FY Dec (S$m)	2018A	2019F	2020F	2021F
Revenue	198	197	201	208
EBITDA	21.3	29.8	29.5	31.1
Pre-tax Profit	15.9	13.8	28.5	23.2
Net Profit	11.9	10.5	21.9	17.9
Net Pft (Pre Ex.)	11.9	14.7	16.5	17.9
EPS (S cts)	1.58	1.39	2.91	2.38
EPS Pre Ex. (S cts)	1.58	1.95	2.19	2.38
EPS Gth (%)	165	(12)	109	(18)
EPS Gth Pre Ex (%)	165	24	12	8
Diluted EPS (S cts)	1.58	1.39	2.91	2.38
Net DPS (S cts)	1.60	1.60	1.60	1.60
BV Per Share (S cts)	21.8	21.6	22.9	23.7
PE (X)	15.8	18.0	8.6	10.5
PE Pre Ex. (X)	15.8	12.8	11.4	10.5
P/Cash Flow (X)	8.1	8.9	5.6	7.5
EV/EBITDA (X)	4.9	3.6	3.1	2.7
Net Div Yield (%)	6.4	6.4	6.4	6.4
P/Book Value (X)	1.1	1.2	1.1	1.1
Net Debt/Equity (X)	CASH	CASH	CASH	CASH
ROAE (%)	7.2	6.4	13.1	10.2
Consensus EPS (S cts):		1.80	1.80	1.80
Other Broker Recs:		B: 2	S: 0	H: 1

GIC Industry : Industrials
GIC Sector: Capital Goods
Principal Business: Fu Yu Corporation Limited is a one-stop high precision plastic parts and moulds manufacturer in Asia.

Source of all data on this page: Company, DBS Bank, Bloomberg Finance L.P.

Moulding for growth

- Turnaround in manufacturing across all regions
- Favourable shift in product mix towards higher profitability and growth potential
- Improving margins; high cash level (0.11 Scts/share) and attractive yield at 6.4%
- Initiate with BUY and TP of S$0.35

Turnaround in manufacturing across all regions. Manufacturing PMIs in China, Singapore, and Malaysia, where Fu Yu's manufacturing facilities are located, are indicating an expansion in the manufacturing sector. We believe that this will lead to an uptick in earnings for Fu Yu.

Emphasis on products with higher profitability and growth potential. Part of the Group's business strategy is to shift towards producing parts for products in the consumer, medical, and automotive space, which have higher profitability and growth potential, as compared to printing and imaging segment.

Cost efficiency to improve margins. Fu Yu is also expanding its margins through cost enhancement initiatives. The redevelopment of its Singapore factory and consolidation of its China operations in Shanghai and Suzhou will further lift normalised net profit margins to 8.2% in FY2020F, from 5.4% in FY2018.

Strong financial positioning. Fu Yu has a high cash level and no debt. Its cash level is equivalent to 44.1% of its market capitalisation and 37.7% of total assets. It has an attractive dividend yield of c.6.4% in FY2019F and TTM EV/EBITDA of 4.4x, vs peers of 6 to 7x.

Valuation:

Initiate with BUY and TP of S$0.35. Our TP is pegged to FY2020F forward PE of 16.0x, which is +1.0 SD its historical 5-year average. The current recovery of the manufacturing cycle across its operating regions, as well as its business strategies, presents an opportunity for a re-rating of the stock's forward PE. Ex-cash, Fu Yu is trading at an attractive FY2020F PE of 7.2x.

Key Risks to Our View:

Slowdown in manufacturing activity, increasing competition, escalation of the US-China Trade War, sharp decline in USDSGD.

At A Glance

Issued Capital (m shrs)	753
Mkt. Cap (Sm/USm)	188 / 140
Major Shareholders (%)	
Tam Wai	12.9
Ho Nee Kit	12.9
Ching Heng Yang	11.8
Free Float (%)	62.4
3m Avg. Daily Val (US$m)	0.25

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Investment Summary

We are initiating with a BUY and TP of S$0.35, representing an upside of 40.0% to its last traded price of S$0.25. Our TP is pegged to a FY2020F forward PE of 16.0x, which is +1.0 SD above its 5-year historical average forward PE. Based on similarities in late 2016, before the onset of the trade war, we believe that the uptrend in the manufacturing cycle justifies an upward re-rating of the stock's forward PE to +1.0 SD.

Fu Yu is a high precision plastic parts and mould manufacturer involved in the printing & imaging, networking & communications, consumer, medical, and automotive sectors. We like Fu Yu on the back of:

1. A recovery in manufacturing,
2. A focus on the faster growing manufacturing industries,
3. Cost efficiency initiatives to improve operating margins,
4. Its strong financial positioning.

1) Turnaround in manufacturing across all regions. The latest data prints of the manufacturing PMIs in Singapore, China, and Malaysia are showing positive signs of recovery heading into 2020 and we believe that Fu Yu's revenue and earnings will ride on the rising trend.

2) Emphasis on products with higher profitability and growth potential. Fu Yu is shifting its focus to products that are more sustainable and have higher growth potential. These industries – consumer, medical, and automotive industries – are poised to grow at high single digits, as compared to the general plastic injecting moulding industry growth of slightly below 5%. In addition, the products in these industries are able to command higher margins due to their demand and high design specifications. In 1H19, Fu Yu has demonstrated that their product mix has shifted towards these industries.

3) Cost efficiency initiatives to improve margins. Along with its focus on the higher growth industries, Fu Yu has also been focusing heavily on its cost management initiatives. The Group has in the past consolidated businesses and factories to reduce costs. In 2Q19, Fu Yu announced that it will be redeveloping its Singapore factory at 9 Tuas Drive 1. This will increase the building space of that factory by three times, while at the same time, it will be selling the leasehold of one other factory in Singapore. The upgraded factory will feature a more efficient layout as well as more advanced equipment to improve profitability.

In addition, Fu Yu will be terminating its Shanghai factory's lease and will be shifting the production to its Suzhou factory to improve the utilisation of its resources, which will further improve on its operational efficiencies.

4) Strong financial positioning. Fu Yu has high cash, equivalent to 44.1% of its market capitalisation and 37.7% of its total assets. It has a dividend policy of paying out at least 50% of its PATMI but has been consistently paying out dividends that is higher than its dividend policy. It recently increased its dividend per share from 1.5 Scts in FY2017 to 1.6 Scts in FY2018. Its current dividend payout represents a yield of c.6.4%. Given its high cash level and stable business performance, we believe that Fu Yu's dividend payout is likely to be maintained in the foreseeable future.

In addition, given Fu Yu's financial positioning and low TTM EV/EBITDA of 4.4x, it is a potential M&A target. Its peers in the region are currently trading at an average of c.6-7x EV/EBITDA.

Valuation & Peers Comparison

Valuation

FY2020F forward PE of 16.0x implies a target price of S$0.35, representing an upside of 40.0% to its last traded price of S$0.25. Fu Yu is currently trading at a 12-month rolling forward PE of 11.4x, which is slightly below its 5-year historical average forward PE of 12.9x. We believe the stock's forward PE will be **re-rated to 16.0x FY2020F earnings (+1.0 SD)** on the back of higher earnings growth driven mainly by:

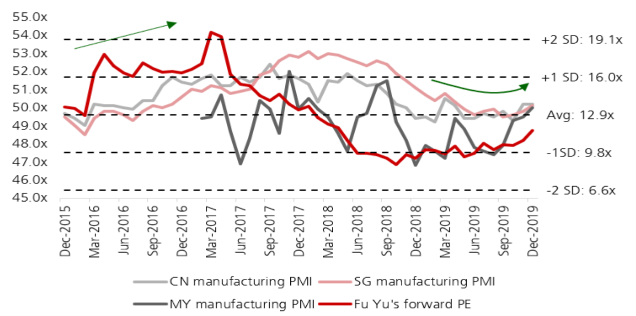
1. A recovery in the manufacturing sectors in Singapore, China, and Malaysia,
2. Strategic focus on industries with higher growth potentials (consumer, medical, and automotive), and
3. Cost efficiency initiatives.

Fu Yu's 5-year forward PE

Source: Bloomberg Finance L.P., Company, DBS Bank

FY2020F forward PE of +1.0 SD is a conservative estimate. The manufacturing PMIs in China and Singapore picked up in late 2016 along with the bottoming of the manufacturing cycle as well as a boost from the 2016 US presidential election when Trump was elected. As the manufacturing PMIs rose above 50, Fu Yu's forward PE also re-rated upwards from the average to above +2.0 SD. We believe that the current bottoming of the manufacturing cycle and progress of the US-China trade war represent a similar situation of an upward re-rating of its forward PE and a +1.0 SD valuation extends a fair margin of safety.

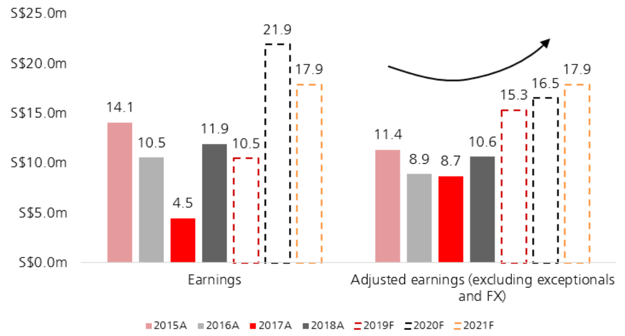
Manufacturing PMI in the region indicates a re-rating in forward PE



Source: Bloomberg Finance L.P., Company, DBS Bank

Stock price to trend up with earnings. In the last five years, Fu Yu's stock price began a decline following the last peak in its share price in early April 2017 and rebounded in July 2018, along with a bottoming in its earnings in FY2017. With higher earnings expected in FY2020F, we are positive on the continued uptrend in the stock price as well as a re-rating of its forward PE multiple.

Past the 2017 bottoming of earnings



Source: Bloomberg Finance L.P., Company, DBS Bank

Key Assumptions

Turnaround in revenue growth of 1.8%/3.4%/5.5% in FY2020F/21F/22F. We are optimistic on Fu Yu's revenue on signs of improving manufacturing PMI data prints in Singapore, China, and Malaysia. In addition, the focus on the faster growing industries (medical, consumer, and automotive) will further boost its revenue growth.

Improving gross profit margins of 19.5%/20.5%/21.0% in FY2020F/21F/22F. As the Group previously included the costs associated with the shutdown of its factory in China in its cost of sales, our gross profit margins projected exclude this one-off redevelopment of the building in FY2020F. With their continued exercising of cost control measures such as the reduction in overheads, we are expecting normalised gross profit margins of to decrease from FY2020F-22F.

The improvement in gross profit margins in FY2021F and FY2022F are due to its shift in product mix towards more profitable industries as well as its cost efficiency initiatives:

1. The consolidation of its Shanghai and Suzhou operations,
2. Redevelopment of its 9 Tuas Drive Singapore factory,
3. Leaner operations through automation and more efficient employees.

Normalised earnings growth of 12.3%/7.9%/9.0% in FY2020F/21F/22F. Fu Yu classifies its FX gains and losses under 'other operating income'. As the FX component is volatile and unpredictable, we have excluded this item in the calculation of the normalised net profit.

Earnings growth is driven by a rise in sales as well as improvements in profitability. Its net profit margin is projected to improve to 8.2%/8.6%/8.8% for FY2020F/21F/22F on the back of its cost enhancement initiatives.

Peer Comparison Table (As of 14 January 2020)

			Financial Data								Valuation				
Bloomberg Ticker	Company Name	Market Cap (S$m)	Sales (S$m)	Net Profit (S$m)	Net Profit Margin (%)	Cash (S$m)	Debt (S$m)	Net Cash as a % of Market Cap	Dividend Yield (%)	EV/EBITDA FY19F	EV/EBITDA FY20F	TTM PE	P/E FY19F	P/E FY20F
Singapore Peers														
FUYU SP Equity	Fu Yu Corp Ltd	188.2	197.7	11.9	6.0%	80.3	0.0	42.7%	6.4	4.7x	4.1x	15.8x	13.1x	11.6x
SUNN SP Equity	Sunningdale Tech Ltd	251.4	726.8	29.8	4.1%	88.7	109.7	-8.3%	6.1	6.8x	5.7x	15.9x	29.3x	15.3x
SPE SP Equity	Spindex Industries Ltd	121.1	155.8	15.3	9.8%	42.3	0.3	34.7%	3.3	N/A	N/A	7.9x	N/A	N/A
HIP SP Equity	Hi-P International Ltd	1,248.5	1,402.1	100.9	7.2%	286.7	169.1	9.4%	3.1	6.3x	5.7x	12.4x	15.0x	13.2x
SG peer average		**452.3**	**620.6**	**39.5**	**6.8%**	**124.5**	**69.8**	**19.6%**	**4.7**	**5.9x**	**5.2x**	**13.0x**	**19.1x**	**13.4x**
SG peer average (excluding Fu Yu)		**540.3**	**761.6**	**48.7**	**7.0%**	**139.2**	**93.0**	**11.9%**	**4.2**	**6.6x**	**5.7x**	**12.0x**	**22.2x**	**14.3x**
Regional Peers														
300151 CH Equity	Shenzhen Changhong Technology Co Ltd	837.8	141.5	11.6	8.2%	39.6	0.0	4.7%	0.7	N/A	N/A	66.5x	N/A	N/A
2283 HK Equity	TK Group Holdings Ltd	568.8	395.7	60.3	15.2%	124.8	59.6	11.5%	4.8	6.8x	5.6x	10.1x	9.9x	8.4x
BRB IN Equity	Bright Brothers Ltd	8.3	44.8	0.4	0.9%	0.5	2.0	-17.5%	2.6	N/A	N/A	21.8x	N/A	N/A
7958 JP Equity	Tenma Corp	656.5	1,038.3	27.2	2.6%	379.4	0.0	57.8%	4.0	N/A	N/A	15.0x	N/A	N/A
002855 CH Equity	Dongguan Chitwing Technology Co Ltd	684.0	449.3	6.0	1.3%	39.4	80.4	-6.0%	0.2	N/A	N/A	100.4x	44.8x	25.7x
Regional peer average		**517.9**	**405.1**	**24.9**	**6.7%**	**136.1**	**15.4**	**14.1%**	**3.0**	**6.8x**	**5.6x**	**28.4x**	**9.9x**	**8.4x**
Total average		**485.1**	**512.8**	**32.2**	**6.8%**	**130.3**	**42.6**	**16.9%**	**3.9**	**6.2x**	**5.3x**	**20.7x**	**16.8x**	**12.1x**
Total average (excluding Fu Yu)		**527.5**	**557.9**	**35.1**	**6.9%**	**137.4**	**48.7**	**13.2%**	**3.5**	**6.6x**	**5.7x**	**21.4x**	**18.1x**	**12.3x**

Source: Bloomberg Finance L.P., Company, DBS Bank

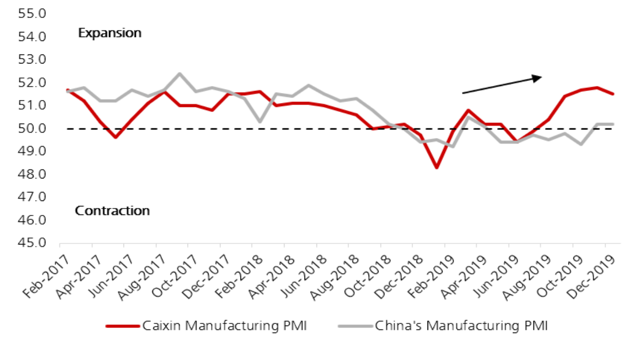
Investment Thesis

1) Turnaround in manufacturing across regions

Fu Yu's manufacturing plants are mainly in China, Singapore and Malaysia and its customers' locations are not significantly different from the location of Fu Yu's assets. As such, the health of the manufacturing activity is key in determining the sales level of the Group.

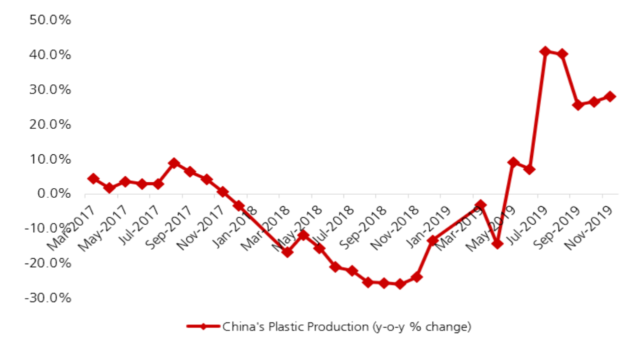
China's manufacturing indices indicate an expansion of the economy. The Caixin Manufacturing PMI bottomed in 1Q19 and China's Manufacturing PMI indicated an expansion in the economy (above 50.0) after six consecutive months of contraction. Both data points indicate an uptick in the manufacturing sector in China. In addition, y-o-y percentage change in the plastic production volume in China turned positive in May 2019 after 16 consecutive months of negative growth.

China's manufacturing PMIs enter expansion territory



Source: Bloomberg Finance L.P., DBS Bank

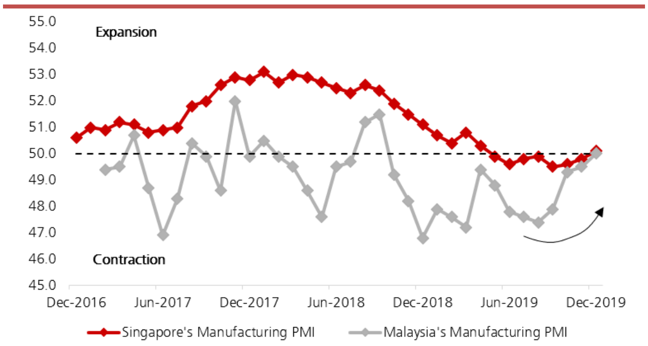
China's plastic product production volume reverses contraction



Source: CEIC, Company, DBS Bank

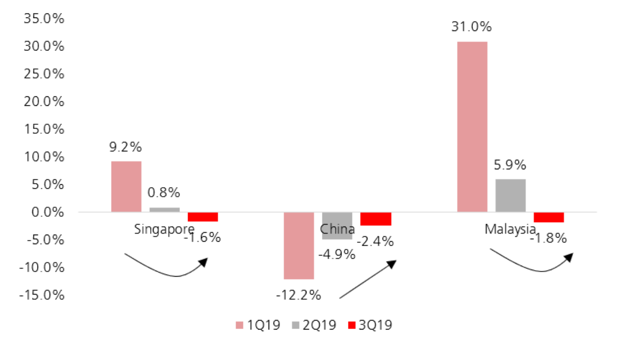
Singapore and Malaysia's manufacturing PMIs past their recent bottom. The negativity surrounding the trade war has impeded on global growth in 2018 and 2019. After news on the progress of the US-China trade war, both the Singapore and Malaysia manufacturing PMIs picked up, pointing to an expansion in their manufacturing sectors after six and 14 consecutive months of contraction respectively. With the bottoming out of the manufacturing PMIs, we are positive that the negative growth in these regions will reverse in FY2020.

Singapore and Malaysia's manufacturing PMIs past their recent bottom



Source: CEIC, Company, DBS Bank

Expect positive sales growth across all manufacturing regions



Source: Company, DBS Bank

2) Emphasis on products with higher profitability and growth potential

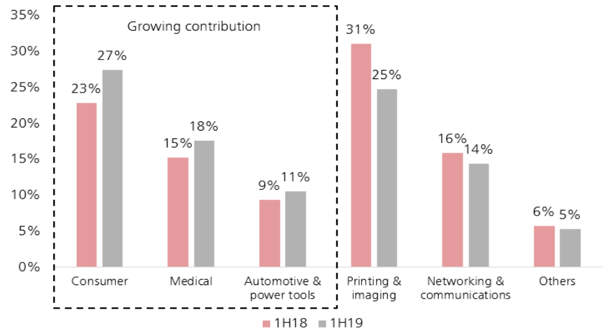
Focusing on the consumer, medical, and automotive products with higher margins. Compared with other plastic production methods, plastic injection moulding in which Fu Yu specialises, allows for high production rates, high precision, and the finished products are of good, consistent quality. As such, it is an indispensable method used for medical equipment, aerospace, automotive, and consumer goods. Fu Yu, which produces plastic parts via injection moulding, is focusing on products with longer life cycles and higher growth potential such as medical, automotive, eco-friendly and smart home consumer products in order to enhance its margins.

These products generally command higher margins due to the high-quality design specifications and higher demand, as compared to products in other segments like the printing &

imaging division. As such, Fu Yu's margins have improved as it shifts its product mix towards consumer, medical, and automotive products.

The consumer, medical, and automotive segments are also expected grow at a faster rate. Various industry sources have indicated that the consumer, medical, and automotive plastic parts industry will grow at high single digits. On the other hand, printing and imaging, and the overall plastic injection moulding industry are projected to grow below 5%. The shift in product mix towards the faster growing markets will drive higher revenue growth for Fu Yu.

Shift in product mix towards faster growing industries



Source: Company, DBS Bank

3) Cost efficiency initiatives to improve margins

Redevelopment of its factory in Singapore to improve productivity and efficiency. In 2Q19, Fu Yu announced that it had accepted a letter of offer from Jurong Town Corporation (JTC) to renew the lease of its premises at 7 Tuas Drive 1 and 9 Tuas Drive 1 that was due to expire on 15 November 2021 for a further term of 20 years. One of the agreements in the lease renewal was to sell its premises at 5 Tuas Drive 1 whose lease was due to expire on 15 November 2041, by 10 September 2020.

As such, Fu Yu will be redeveloping one of its Singapore premises at 9 Tuas Drive. The initiative entails the demolition of the existing building and a construction of a larger building to house a factory, warehouse, and office space. The new building will have an estimated gross floor area of 9,000 sqm, more than **three times the size of its existing building** (2,572sqm).

The layout of the new building will incorporate a seamless workflow across tooling, moulding, and assembly operations, to **enhance productivity and efficiencies**, and to ensure faster time-to-market for its customers. The Group expects the capex for the redevelopment to be c.S$15.4m, which will be financed via internal funds.

Selling of 5 Tuas Drive 1 to partially offset redevelopment costs. Based on the average rental rates and capitalisation rates of industrial properties in that region, we estimate that the property could be sold for S$8-10m, which will be used to partially offset the redevelopment costs in 9 Tuas Drive 1.

Assumptions for 5 Tuas Drive 1

	Lower End	Higher End
Rental rates (S$/sqft/month)	1.20	1.50
Building area (sqm)	5,179	5,179
Net property income margin (%)	70.0	70.0
Capitalisation rate (%)	7.0	7.0
Selling price (S$'m)	8.0	10.0

Source: DBS Bank

Streamlining of operations in China. On 23 August 2019, Fu Yu announced that the landlord will be terminating its lease for the Shanghai factory on 31 January 2020, in advance of the original expiration date on 31 August 2021. This move was made amidst higher operating costs in Shanghai, contributed by the government initiatives in 2014 to shift the city's economy away from manufacturing:

- Lowered the terms of industrial land-use rights from 50 years to 20 years.
- Lowering of the proportion of industrial land from 27% to 17% by the end of 2020.

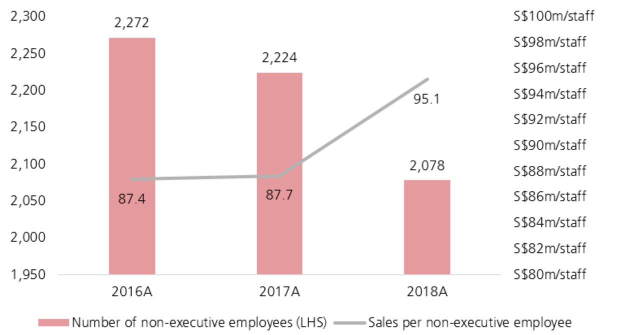
As such, the Group will be transferring its assets from its factory in Shanghai to Suzhou and will continue serving its customers located in Shanghai from its factory in Suzhou. This will further improve the utilisation of the resources and cost structure. Fu Yu expects a one-off expense of c.S$5.5m in relation to the closure of its Shanghai plant, of which it had booked in S$4.8m in 3Q19. We are expecting the closure of the operations in Shanghai to shave off c.S$2.4m from its depreciation expense, representing c.1.2% of its sales in FY2018.

Leaner operations through automation and more efficient employees. Fu Yu has ongoing initiatives to optimise its production processes through lean management and automation. The number of non-executive employees declined by 8.5% from 2016 to 2018 and the revenue generated per non-executive employee increased by 8.9% during the same period. A part of the employee overhead expenses related to the production of its goods are included in the cost of sales and this increase in efficiency has improved normalised gross profit margins by 4.4 percentage points, from 16.3% in 2016 to 20.7% in 9M19. The normalised gross profit margins exclude one-off expenses such as the costs related to the closure of the Shanghai plant.

We believe that the net impact from the cessation of operations in the Shanghai factory and expansion in the Singapore factory will be a c.10% reduction in the number of employees as:

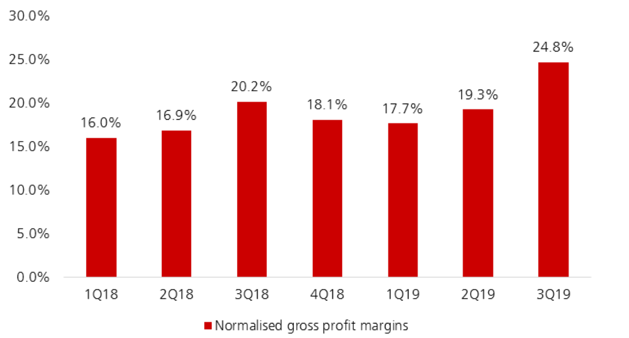
1. The Singapore expansion is smaller than the Shanghai factory.
2. The Singapore factory is likely to be more productive due to more efficient outlay and automation.

Decline in staff count and an increase in productivity



Source: Company, DBS Bank

Rising normalised gross profit margins



Source: Company, DBS Bank

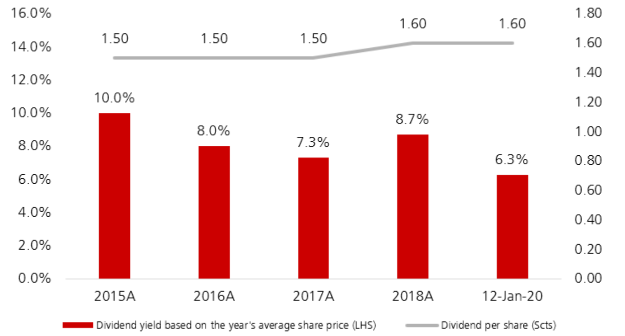
4) Strong financial positioning

High cash position with zero borrowings. As of 3Q19, Fu Yu had no borrowings and cash and cash equivalents of S$84.6m, which is equivalent to 44.1% of its market capitalisation on 12 January 2020 (share price of S$0.255) and forms 37.7% of its total assets.

Stable dividend payout; attractive dividend yield of c.6.4%. Although Fu Yu has a dividend policy of paying at least 50% of its PATMI, the Group has been paying out dividends of S1.5 Scts/share from FY2015 to FY2017, and 1.6 Scts in FY2018, all of which were above 80% of their PATMI. This translates to an average annual yield of 8.6% from 2015 to 2018.

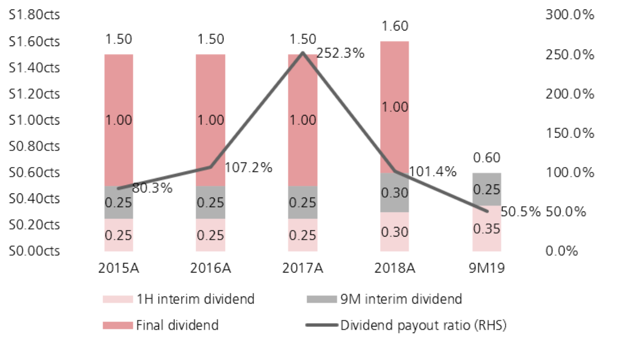
In FY2019F, Fu Yu has paid out interim dividends of 0.6 Scts, which is the same as FY2018. Based on its cash level, business performance, and funding needs, we expect Fu Yu to at least pay a final dividend of 1.0 Scts, translating to a total dividend payout of 1.6 Scts/share in FY2019F, similar to FY2018, which is equivalent to a dividend yield of 6.4% based on its current share price.

Stable dividend payout and attractive yield



Source: Company, DBS Bank

Dividend payout above its dividend policy



Source: Company, DBS Bank

Potential M&A with a 4.4x trailing-12-month EV/EBITDA. Fu Yu is currently trading at a trailing-12-month EV/EBITDA multiple of 4.4x. This is the lowest among its industry peers in this region, which are trading at an average of c.6-7x EV/EBITDA.

Key Risks

Slowdown in the manufacturing cycle. Fu Yu's forward PE trades closely to the manufacturing PMIs in China, Singapore, and Malaysia. A slowdown in manufacturing activity due to geopolitical risks or a weakening of end consumer demand could hinder the re-rating of its forward PE.

Intensifying competition in China. According to a research report by McKinsey, China is gaining market share through its enhanced competitiveness from automation. Chinese OEMs now have more than 50% market share in plastic moulding. An intensifying competition in plastic parts and mould manufacturing could eat into profitability margins for Fu Yu.

Escalation of the US-China trade war. The escalation of the US-China Trade War has weighed on global growth, with the International Monetary Fund indicating that global growth remains subdued, forecasting a 3.5% growth in 2020. In its October 2019 World Economic Outlook, it reported that momentum in manufacturing activity has weakened substantially to levels not seen since the financial crisis, citing a rise in trade and geopolitical tensions. A re-escalation of the US-China trade war would impede the recovery of manufacturing activity and thus Fu Yu's sales.

Foreign exchange translation losses. Fu Yu's key business operations are in Singapore, Malaysia, and China, with SGD as its reporting currency. A significant portion of its trade transactions are denominated in USD and while its foreign exchange risk is partially managed through a natural hedge between the revenue and the purchases in the same currency (USD), the remaining unhedged portion is usually a surplus of funds which will be converted to the required currencies when the need arises. As such, the Group has a net USD position on its assets and a depreciation of the USD against the SGD, MYR, or CNY will result in a foreign exchange loss recorded.

SWOT Analysis

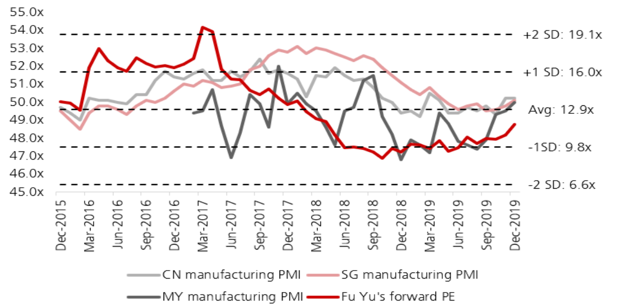
Strengths	Weakness
• **Broad and diversified customer base.** With 42 years of operating history, Fu Yu has built a broad and diversified customer base of blue-chip companies in various industries – the printing and imaging, networking and communications, consumer, medical, and automotive sectors. • **Strong financial position.** As of 3Q19, Fu Yu had no borrowings and cash and cash equivalents of S$84.6m. This amount represents c.44.1% of Fu Yu's market capitalisation on 12 January 2020. • **Experienced co-founders with substantial interest.** Three of Fu Yu's co-founders are on the Board of Directors as Executive Directors. They have a combined effective interest of 37.57% in the Group and oversee its operations. Being co-founders and long-standing shareholders of the company, they have the Group's long-term interests as their priority.	• **Foreign exchange exposure.** A significant portion of Fu Yu's trade transactions are denominated in USD and the surplus of funds are retained in USD. As of FY2018, the Group was in a net USD assets position and an appreciation of the USD against the SGD, MYR, and CNY will contribute to a foreign exchange gain and vice versa. • **High level of unutilised of cash.** As of 3Q19, 37.7% of Fu Yu's balance sheet comprised cash and cash equivalents of which are cash balances (12.9% of total assets) and bank deposits (24.8% of total assets) with maturities of three months or less from the date of acquisition. In FY2018, these deposits generated effective interest rates ranging from 1.08-3.95% per annum. The return on assets and return on equity for Fu Yu was 4.8% and 6.1% respectively in FY2018.
Opportunities	**Threats**
• **Recovering manufacturing sector in the region.** Manufacturing PMIs in China, Singapore, and Malaysia have entered expansionary territory after bottoming out in 2019. • **Consumer, medical, and automotive are positioned to grow faster than the industry.** According to various market research firms, the consumer, medical, and automotive plastic parts manufacturing industry are projected to grow at high single digits compared to the plastic manufacturing industry growth of less than 5%.	• **Slowdown in the manufacturing cycle.** Fu Yu's forward PE trades closely with the manufacturing PMIs in China, Singapore, and Malaysia. A slowdown in manufacturing activity would translate to a downward re-rating of its forward PE. • **Intensifying competition in China.** China OEMs are gaining market share through their automation, enhancing their competitiveness. An increase in competition in the industry would eat into Fu Yu's profitability. • **Escalation of the US-China trade situation.** The US-China trade war has disrupted global supply chains and stifled global growth. In 2019, the International Monetary Fund (IMF) downgraded its 2019 global economic growth forecast to 3.0% in its October meeting, from 3.3% in its April World Economic Outlook, citing rising trade barriers and increasing geopolitical tensions. A re-escalation of the US-China trade war could dampen trade volumes, economic growth, and end-user demand for its customers' products.

Source: DBS Bank

Critical Factors

Economic outlook of manufacturing regions. Fu Yu's business is dependent on manufacturing activity and its plants are located in Singapore, China, and Malaysia. Its customers' locations are not significantly different from the location of its assets. As such, the manufacturing PMIs of each country provides a good indication of the direction of its revenue and earnings derived from that country and its forward PE trades closely to the trend of the manufacturing PMIs.

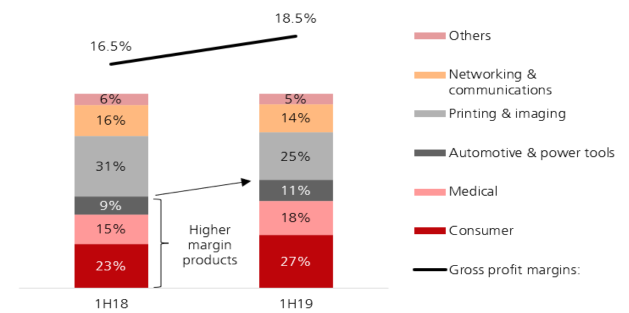
Forward PE trends with the manufacturing cycle



Source: Bloomberg Finance L.P., Company, DBS Bank

Product mix affects gross profit margins. Due to the difference in demand and growth of the finished products, and complexity of the design specifications of the plastic parts required in different industries, margins differ across the products from different industries. As such, a change in it is product mix will affect its gross profit margins.

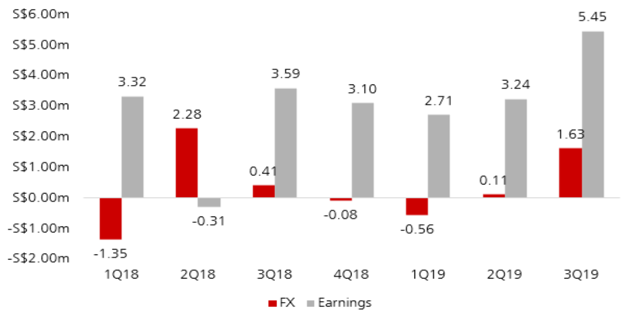
Shift in product mix towards more profitable industries



Source: Company, DBS Bank

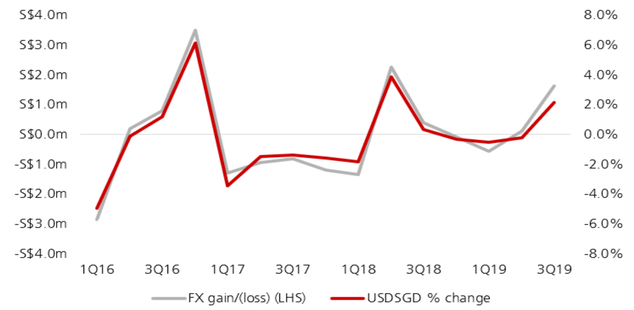
Movement of the USD currency against the SGD, CNY, and MYR impacts earnings. A significant portion of Fu Yu's trade transactions are denominated in USD and the Group retains its excess funds in USD. The cash is converted into the local currency where the funds are needed for operational purposes. As such, an appreciation of the USD against the SGD, MYR, and CNY will contribute to a foreign exchange gain and vice versa. Based on historical relationships, we estimate that a percentage point gain/(loss) in USDSGD translates to an FX gain/(loss) of S$0.5m.

FX gains or losses have an impact on earnings



Source: Company, DBS Bank

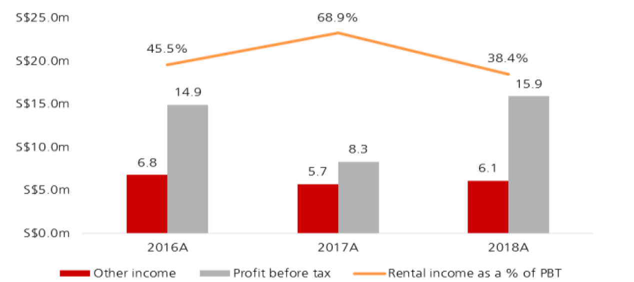
Close relationship between FX gains/(losses) and the USDSGD



Source: Company, DBS Bank

Other income accounts for a relatively substantial portion of its profit. The Group's other income mainly consists of rental income and the sale of scrap and raw materials. The rental income amounted to S$4.0m and S$3.8m in FY2017 and FY2018 respectively. One of the Group's leased properties is sublet to a third party, of which amounted to S$2.8m and S$2.9m in FY2017 and FY2018 respectively, is included in the rental income.

Other income accounts for a relatively substantial portion of profit before tax

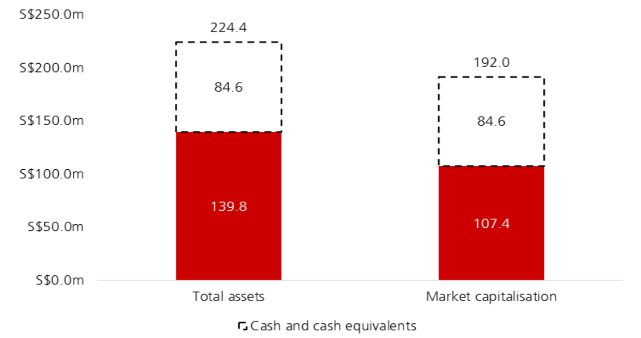


Source: Company, DBS Bank

Financials

High cash levels with zero borrowings. Fu Yu has a high cash level of S$84.6m and no debt. Its cash level is equivalent to 37.7% of its total assets and 44.1% of its current market capitalisation.

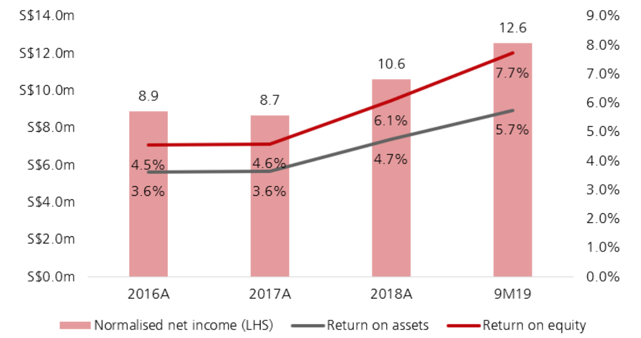
Cash is a high percentage of total assets and market capitalisation



Source: Company, DBS Bank

More efficient use of resources – Higher ROA and ROE, operating margins, and quicker cash conversion cycle. In the last few years, Fu Yu has been focused on increasing its profitability through a focus on more profitable industries as well as improving its cost efficiencies. As such, its utilisation of assets (return on assets and return on equity) improved from 3.6% and 4.6% in FY2016A to 5.7% and 7.7%, respectively in 9M19.

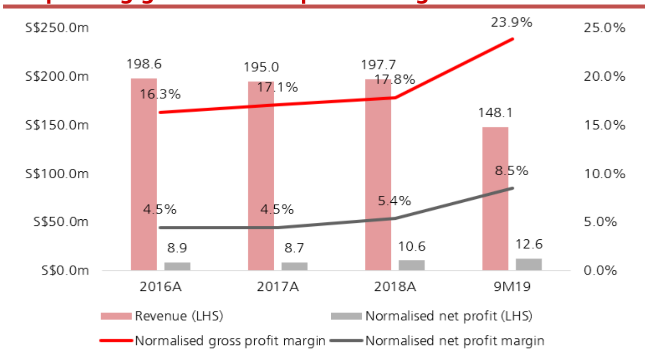
Higher returns on assets and equity



Source: Company, DBS Bank

Through its operational efficiencies, the Group managed to increase its gross profit margins and net profit margins through a shift in product mix, leaner operations, automation, and increase in employee efficiency.

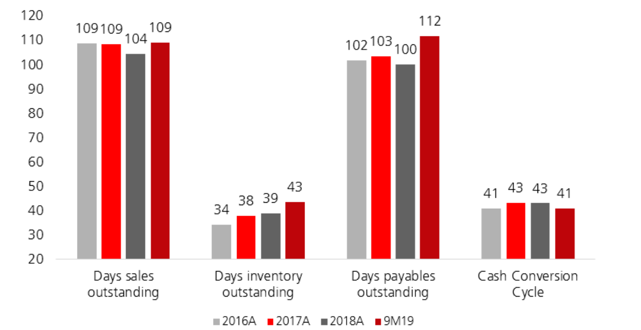
Improving gross and net profit margins



Source: Company, DBS Bank

In addition, the Group managed to lower its cash conversion cycle from 43.0 days in FY2018 to 40.9 days in 9M19, which indicates a faster conversion of its cash from inventories and a more efficient use of its resources.

Faster cash conversion cycle



Source: Company, DBS Bank

Key Assumptions

FY Dec	2016A	2017A	2018A	2019F	2020F	2021F
Gross Profit Margins	16.3%	17.1%	17.8%	19.5%	20.5%	21.0%
Administrative Costs as a % of Revenue	14.0%	13.9%	13.9%	13.5%	13.5%	13.5%

Cost savings from the reduction in overheads and increase in efficiency

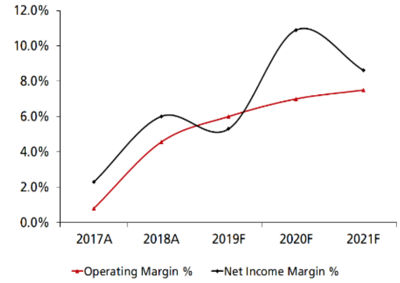
Source: Company, DBS Bank

Income Statement (S$m)

FY Dec	2016A	2017A	2018A	2019F	2020F	2021F
Revenue	199	195	198	197	201	208
Cost of Goods Sold	(166)	(162)	(162)	(159)	(160)	(164)
Gross Profit	**32.4**	**33.3**	**35.3**	**38.5**	**41.2**	**43.6**
Other Opng (Exp)/Inc	(26.3)	(31.8)	(26.3)	(26.6)	(27.1)	(28.0)
Operating Profit	**6.15**	**1.53**	**9.00**	**11.8**	**14.1**	**15.6**
Other Non Opg (Exp)/Inc	6.78	5.73	6.12	6.00	6.00	6.00
Associates & JV Inc	0.09	(0.7)	(0.8)	0.0	0.0	0.0
Net Interest (Exp)/Inc	1.88	1.76	1.60	1.45	1.38	1.67
Exceptional Gain/(Loss)	0.0	0.0	0.0	(5.5)	7.00	0.0
Pre-tax Profit	**14.9**	**8.32**	**15.9**	**13.8**	**28.5**	**23.2**
Tax	(3.0)	(2.9)	(3.7)	(3.3)	(6.5)	(5.3)
Minority Interest	(1.3)	(1.0)	(0.3)	0.0	0.0	0.0
Preference Dividend	0.0	0.0	0.0	0.0	0.0	0.0
Net Profit	**10.5**	**4.48**	**11.9**	**10.5**	**21.9**	**17.9**
Net Profit before Except.	10.5	4.48	11.9	14.7	16.5	17.9
EBITDA	22.8	14.3	21.3	29.8	29.5	31.1
Growth						
Revenue Gth (%)	(10.7)	(1.8)	1.4	(0.2)	1.8	3.4
EBITDA Gth (%)	(25.0)	(37.5)	49.5	39.7	(0.8)	5.4
Opg Profit Gth (%)	(26.7)	(75.1)	488.7	31.5	18.8	10.8
Net Profit Gth (Pre-ex)	(25.1)	(57.5)	165.5	23.7	12.3	8.4
Margins & Ratio						
Gross Margins (%)	16.3	17.1	17.8	19.5	20.5	21.0
Opg Profit Margin (%)	3.1	0.8	4.6	6.0	7.0	7.5
Net Profit Margin (%)	5.3	2.3	6.0	5.3	10.9	8.6
ROAE (%)	6.0	2.6	7.2	6.4	13.1	10.2
ROA (%)	4.3	1.9	5.3	5.0	10.1	7.9
ROCE (%)	6.3	3.3	7.7	9.8	10.6	11.1
Div Payout Ratio (%)	107.2	252.3	101.4	115.1	55.0	67.3
Net Interest Cover (x)	NM	NM	NM	NM	NM	NM

Source: Company, DBS Bank

Margins Trend



Cost of sales excludes the one-off expense of S$5.5m that is related to the closure of the Shanghai plant

Cost of sales of S$5.5m that is related to the closure of the Shanghai plant is re-categorised under exceptional

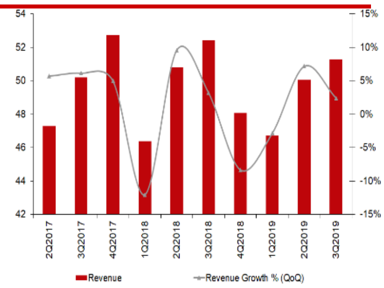
Estimated sale of 5 Tuas Drive 1 and administrative costs involved in the redevelopment of 9 Tuas Drive 1

Quarterly / Interim Income Statement (S$m)

FY Dec	2Q2018	3Q2018	4Q2018	1Q2019	2Q2019	3Q2019
Revenue	50.8	52.4	48.1	46.7	50.1	51.3
Cost of Goods Sold	(42.2)	(41.9)	(39.4)	(38.4)	(40.4)	(38.6)
Gross Profit	**8.57**	**10.6**	**8.69**	**8.26**	**9.66**	**12.7**
Other Oper. (Exp)/Inc	(5.0)	(4.8)	(6.4)	(7.5)	(6.5)	(4.9)
Operating Profit	**3.62**	**5.77**	**2.24**	**0.80**	**3.15**	**7.75**
Other Non Opg (Exp)/Inc	1.33	0.09	1.44	1.35	1.31	1.26
Associates & JV Inc	(0.1)	(0.3)	(0.2)	(0.1)	(0.1)	0.0
Net Interest (Exp)/Inc	0.43	0.31	0.39	0.40	0.41	0.45
Exceptional Gain/(Loss)	0.0	0.0	0.0	0.0	0.0	(4.8)
Pre-tax Profit	**5.24**	**5.90**	**3.82**	**2.48**	**4.76**	**4.65**
Tax	(1.0)	(1.5)	(0.9)	(0.9)	(1.3)	(0.7)
Minority Interest	0.0	0.0	0.0	0.0	0.0	0.0
Net Profit	**4.24**	**4.40**	**2.94**	**1.59**	**3.46**	**3.91**
Net profit bef Except.	4.24	4.40	2.94	1.59	3.46	8.71
EBITDA	6.59	7.31	5.13	5.10	7.35	12.0
Growth						
Revenue Gth (%)	9.6	3.2	(8.3)	(2.8)	7.2	2.4
EBITDA Gth (%)	189.6	11.0	(29.8)	(0.6)	44.2	62.7
Opg Profit Gth (%)	(577.6)	59.4	(61.2)	(64.2)	292.1	146.3
Net Profit Gth (Pre-ex)	580.0	3.6	(33.2)	(45.9)	117.6	152.0
Margins						
Gross Margins (%)	16.9	20.2	18.1	17.7	19.3	24.8
Opg Profit Margins (%)	7.1	11.0	4.7	1.7	6.3	15.1
Net Profit Margins (%)	8.4	8.4	6.1	3.4	6.9	7.6

Source: Company, DBS Bank

Revenue Trend



One-off expense of S$4.0m related to the closure of the Shanghai plant is excluded from cost of sales

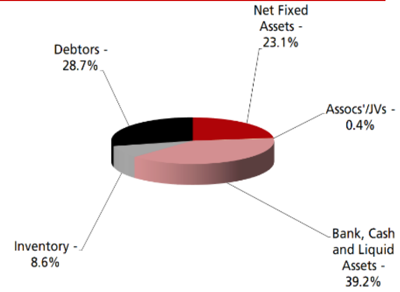
One-off expense from the closure of the Shanghai plant

Balance Sheet (S$m)

FY Dec	2016A	2017A	2018A	2019F	2020F	2021F
Net Fixed Assets	47.7	46.0	44.8	45.5	42.2	38.8
Invts in Associates & JVs	2.16	1.49	0.71	0.71	0.71	0.71
Other LT Assets	10.3	9.93	8.82	8.64	8.46	8.28
Cash & ST Invts	108	98.8	83.9	80.5	96.1	103
Inventory	16.0	17.6	16.9	16.9	17.0	17.5
Debtors	57.0	59.0	54.0	56.4	57.4	59.4
Other Current Assets	0.08	3.44	2.38	2.38	2.38	2.38
Total Assets	242	236	212	211	224	230
ST Debt	0.0	0.0	0.0	0.0	0.0	0.0
Creditor	45.4	46.2	43.0	43.6	43.9	45.1
Other Current Liab	2.38	3.94	3.48	3.90	7.12	5.93
LT Debt	0.0	0.0	0.0	0.0	0.0	0.0
Other LT Liabilities	0.61	0.62	0.95	0.95	0.95	0.95
Shareholder's Equity	174	165	164	163	172	178
Minority Interests	19.6	20.2	0.0	0.0	0.0	0.0
Total Cap. & Liab.	242	236	212	211	224	230
Non-Cash Wkg. Capital	25.3	30.0	26.8	28.2	25.8	28.2
Net Cash/(Debt)	108	98.8	83.9	80.5	96.1	103
Debtors Turn (avg days)	108.7	108.6	104.3	102.1	103.4	102.6
Creditors Turn (avg days)	108.2	108.5	104.7	107.6	106.2	105.0
Inventory Turn (avg days)	36.2	39.8	40.6	42.1	41.2	40.7
Asset Turnover (x)	0.8	0.8	0.9	0.9	0.9	0.9
Current Ratio (x)	3.8	3.6	3.4	3.3	3.4	3.6
Quick Ratio (x)	3.5	3.1	3.0	2.9	3.0	3.2
Net Debt/Equity (X)	CASH	CASH	CASH	CASH	CASH	CASH
Net Debt/Equity ex MI (X)	CASH	CASH	CASH	CASH	CASH	CASH
Capex to Debt (%)	N/A	N/A	N/A	N/A	N/A	N/A

Source: Company, DBS Bank

Asset Breakdown

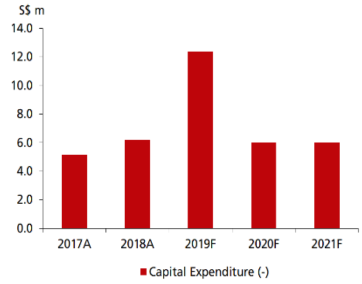


Cash Flow Statement (S$m)

FY Dec	2016A	2017A	2018A	2019F	2020F	2021F
Pre-Tax Profit	14.9	8.32	15.9	13.8	28.5	23.2
Dep. & Amort.	9.79	7.70	6.99	11.9	9.44	9.53
Tax Paid	(3.4)	(2.1)	(2.1)	(2.9)	(3.3)	(6.5)
Assoc. & JV Inc/(loss)	(0.1)	0.70	0.80	0.0	0.0	0.0
Chg in Wkg.Cap.	0.68	(6.1)	3.09	(1.8)	(0.9)	(1.2)
Other Operating CF	(0.9)	(2.6)	(1.4)	0.0	0.0	0.0
Net Operating CF	**21.0**	**5.93**	**23.3**	**21.0**	**33.7**	**25.0**
Capital Exp.(net)	(6.4)	(5.1)	(6.2)	(12.4)	(6.0)	(6.0)
Other Invts.(net)	0.92	(0.6)	(0.3)	0.0	0.0	0.0
Invts in Assoc. & JV	0.0	0.0	0.0	0.0	0.0	0.0
Div from Assoc & JV	0.37	0.0	0.0	0.0	0.0	0.0
Other Investing CF	1.88	1.76	1.60	0.0	0.0	0.0
Net Investing CF	**(3.2)**	**(3.9)**	**(4.9)**	**(12.4)**	**(6.0)**	**(6.0)**
Div Paid	(12.7)	(12.2)	(12.0)	(12.0)	(12.0)	(12.0)
Chg in Gross Debt	0.0	0.0	0.0	0.0	0.0	0.0
Capital Issues	0.0	0.0	0.0	0.0	0.0	0.0
Other Financing CF	(0.1)	0.06	(21.3)	0.0	0.0	0.0
Net Financing CF	**(12.7)**	**(12.1)**	**(33.3)**	**(12.0)**	**(12.0)**	**(12.0)**
Currency Adjustments	(2.3)	(0.1)	(0.2)	0.0	0.0	0.0
Chg in Cash	2.69	(10.2)	(15.1)	(3.4)	15.6	6.98
Opg CFPS (S cts)	2.70	1.59	2.68	3.03	4.59	3.48
Free CFPS (S cts)	1.94	0.11	2.27	1.15	3.68	2.53

Source: Company, DBS Bank

Capital Expenditure



Redevelopment cost of 9 Tuas Drive 1

Company Background

Company Background

Over 40 years of history. Fu Yu Corporation Limited (Fu Yu) was founded in 1978 and was listed on the Main Board of the Singapore Exchange on 14 June 1995. It began as a small moulding and tooling fabrication factory and extended its operations in 1985 to include various sub-assembly processes. It is now one of the largest manufacturers of high precision plastic parts and moulds in Asia.

Manufacturer of high precision plastic parts and moulds. It offers a one-stop solution by providing vertically integrated services for the manufacturing of precision plastic components and the fabrication of precision moulds and dies. Its capabilities range from precision tool design and fabrication, precision injection moulding to secondary processes such as silk screen printing, ultrasonic welding, heat staking and spray painting, as well as sub-assembly.

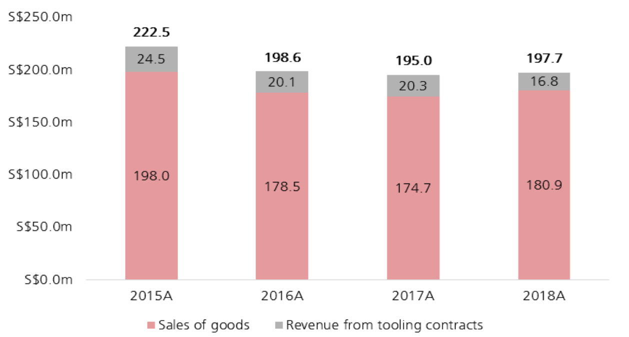
Business Operations

Fu Yu segments its revenue into i) Sales of goods and ii) Revenue from tooling contracts.

- **Sales of goods:** Manufacturing and sub-assembly of precision plastic parts and components
- **Revenue from tooling contracts:** Fabrication of precision moulds and dies

Main business is in manufacturing and sub-assembly. Sales of goods is its main operating segment, contributing c.90% of the Group's total revenue.

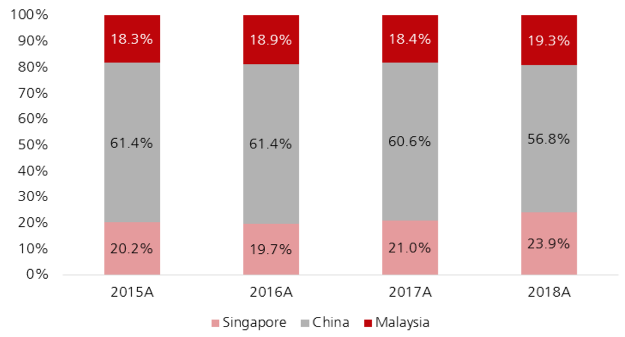
Revenue by Operating Segments



Source: Company, DBS Bank

Operations in Singapore, China, and Malaysia. Fu Yu conducts its business operations in Singapore, China, and Malaysia. China has been its main contributing region, accounting for c.57-60% of its revenue. Singapore and Malaysia account for c.20-25% and c.18-20% of its revenue respectively.

Revenue by Geographical Segments



Source: Company, DBS Bank

Fu Yu operates within the printing and imaging, networking and communications, consumer, medical, and automotive sectors.

Supply Chain

Assets in Singapore, China, and Malaysia. The Group has a total of seven manufacturing facilities in Singapore (one), China (four), and Malaysia (two) to support its operations locally. Its customers' locations are not significantly different from the location of Fu Yu's assets.

The manufacturing plants are located in:

- **Singapore:** Singapore
- **Malaysia:** Johor, Penang
- **China:** Dongguan, Suzhou, Zhuhai, and Chongqing

Blue chip customers. Its customers are blue chip companies in the printing and imaging, networking and communications, consumer, medical, and automotive industries.

Two major customers account for c.20-25% of its revenue. Fu Yu has two major customers which account for c.20-25% of its revenue. The revenue from these two customers are derived from all three of its operating regions.

Management & Strategy

Key Management Team

Name	Background & Experiences
Dr John Chen Seow Phun Non-Executive Chairman, Independent Director *(0.13% effective interest)*	Dr Chen holds a PhD in Electrical Engineering from the University of Waterloo, Canada. He was appointed as the Non-Executive Chairman and Independent Director of Fu Yu in November 2007. **Other responsibilities:** Dr Chen is also presently the Executive Chairman of Pavillon Holdings Ltd and the Chairman of SAC Capital Pte Ltd. He also sits on the board of several publicly listed companies.
Ching Heng Yang *(Co-Founder)* Vice Chairman, Executive Director *(11.81% effective interest)*	Mr Ching, one of the co-founders of Fu Yu, was appointed as the Executive Director in December 1980. He has over 44 years of experience in the mould fabrication and plastic injection moulding industry. **Group responsibilities:** Oversees the plastic injection moulding, finishing, and sub-assembly operations of the Group. He is also responsible for the investment in factory buildings and machinery.
Tam Wai *(Co-Founder)* Executive Director *(12.88% effective interest)*	Mr Tam, one of the co-founders of Fu Yu, was appointed as the Executive Director in December 1980. He has over 49 years of experience in the mould fabrication and plastic injection moulding industry. **Group responsibilities:** Oversees the mould design and fabrication operations of the Group.
Ho Nee Kit *(Co-Founder)* Executive Director *(12.88% effective interest)*	Mr Ho, one of the co-founders of Fu Yu, was appointed as the Executive Director in December 1980. **Group responsibilities:** Oversees the mould fabrication, plastic injection moulding, finishing, and sub-assembly operations of the Group.
Hew Lien Lee Executive Director, Chief Executive Officer, and Chief Operating Officer *(1.08% effective interest)*	Mr Hew holds a Diploma in Electrical Engineering. He first joined Fu Yu in 1984 and was appointed as Executive Director and Chief Operating Officer in March 2007. In February 2016, Mr Hew was promoted to Chief Executive Officer of the Group. He has 39 years of experience in the plastic injection moulding industry. **Group responsibilities:** Responsible for the overall strategic direction and management of the Group.

Source: Company, DBS Bank

Business Strategy

Maintain a diversified customer base. Fu Yu's long-term strategy is to maintain a diversified customer base across its target market segments, which includes printing and imaging, consumer, medical, networking and communications, and automotive.

Focus on growth products. Its focus will be to secure products with greater stability, longer life cycles, and higher growth potential. These products include those that are in the medical, automotive, eco-friendly and smart consumer products, as well as 3D printers.

Improve operational efficiencies. Fu Yu has been undertaking cost-reduction initiatives such as lean management and automation. Over the last few years, it has consolidated operations, liquidated unprofitable businesses, as well as reduced employee overheads through automation.

^ Bloomberg ESG Disclosure Scores rate companies annually based on their disclosure of quantitative and policy-related ESG data. It is based on a scoring scale of 0-100, and calculated using a subset of more than 100 raw data points it collects on ESG. It is designed to measure the robustness of companies' disclosure of ESG information in their reporting/the public domain. Based on Bloomberg disclosures, as of 25 Jan 2019, the global ESG disclosure average score is 24.92 and 22.14, 28.26, 49.97 for Environmental, Social and Governance, respectively.

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BUY (>15% total return over the next 12 months for small caps, >10% for large caps)
HOLD (-10% to +15% total return over the next 12 months for small caps, -10% to +10% for large caps)
FULLY VALUED (negative total return, i.e., > -10% over the next 12 months)
SELL (negative total return of > -20% over the next 3 months, with identifiable share price catalysts within this time frame)

**Share price appreciation + dividends*

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