

Outthink. Outperform.

Resetting expectations

We expect Inari to report a weak set of 3QFY16 earnings on May 18 as inventory continues to be worn down and on concerns over a lacklustre new model later this year. In view of this we cut our FY16-18E EPS by 27-30%. We lower our TP to RM3.54 on the EPS cut but we roll forward our valuation horizon to 2017. Still a BUY despite an earnings blip as RF and fibre optic prospects remains exciting.

Weak smartphone sales will be a drag on Inari's 3QFY16

A leading smartphone manufacturer recently reported that its smartphone sales declined for the first time since its launch 9 years ago and has guided for weaker sales in the quarter ahead. This will likely have negative implications on Inari and we estimate that Inari's revenue could fall by up to 30% this quarter, taking into account the 2% appreciation of the RM. Recall that the RF business contributes nearly half of Inari's revenue. Concerns over weak demand ahead arising from a lacklustre new model by this same brand later this year are also valid.

FY16-18E EPS cut by 27-30%

If the 3Q16 revenue decline is close to our estimate, net profit for the quarter could be in the region of RM20-25m based on an estimated net margin of 10-12%. Although Inari reported a net margin of 14% in 2QFY16, margins are likely to be lower considering the adverse impact of operating leverage. Cumulative 9MFY16 net profit would thus be c. RM100m, or 50% of our FY16 estimate. While 4QFY16 is expected to be more robust in view of an anticipated order ramp up, matching our FY16E would be tough. We are thus lowering our revenue (cut by 17%) and net margin assumption (reduced from 16% to 14%) resulting in a 27% cut in FY16E EPS. We also cut FY17-18 EPS by 30% each year.

Maintain BUY, TP lowered to RM3.54 (18x fully-diluted CY17E EPS)

We cut our TP to RM3.54 (from RM4.12) based on an unchanged 18x PE after the earnings revision. However, we roll forward our valuation horizon to 2017. We maintain our BUY rating as we remain positive on Inari's long term prospects both in its RF operations as well as on the fibre optics front. We believe LTE adoption will continue to raise RF content per device driving growth despite an overall slowdown in smartphone sales. Key downside risks include a slowdown in global demand for smart devices, rapid ASP erosion and a loss of customer base.

Earnings & Valuation Summary

FYE June (RMm)	2014	2015	2016E	2017E	2018E
Revenue	793.7	933.1	1,054.6	1,193.9	1,341.4
EBITDA	129.0	166.8	192.1	224.8	268.3
Pretax profit	106.9	151.7	170.5	200.3	243.6
Net profit	99.2	152.5	155.5	180.9	220.2
EPS (sen)	10.4	16.0	16.3	19.0	23.1
PER (x)	26.3	17.1	16.8	14.4	11.9
Core net profit	94.0	132.7	152.3	180.9	220.2
Core EPS (sen)	9.9	13.9	16.0	19.0	23.1
Core EPS chg (%)	104.1	41.1	14.8	18.8	21.7
Core PER (x)	27.8	19.7	17.1	14.4	11.9
DPS (sen)	6.8	6.4	6.5	7.6	9.2
Dividend Yield (%)	2.5	2.3	2.4	2.8	3.4
EV/EBITDA (x)	20.2	14.3	12.1	10.0	8.1
% change			(26.7)	(30.2)	(30.0)
Affin/Consensus (x)	-	-	0.9	0.8	0.8

Source: Company, Affin Hwang forecasts, Bloomberg

Affin Hwang Investment Bank Bhd (14389-U)
(Formerly known as HwangDBS Investment Bank Bhd)

Company Update

Inari Amertron

INRI MK

Sector: Technology

RM2.74 @ 3 May 2016

BUY (maintain)

Upside 29%

Price Target: RM3.54

Previous Target: RM4.12



Price Performance

	1M	3M	12M
Absolute	-14.9%	-17.5%	+7.8%
Rel to KLCI	-11.9%	-17.4%	+18.7%

Stock Data

Issued shares (m)	956.1
Mkt cap (RMm)/(US\$m)	2619.7/666.2
Avg daily vol - 6mth (m)	5.1
52-wk range (RM)	2.24-3.96
Est free float	52.6%
BV per share (RM)	0.70
P/BV (x)	3.94
Net cash/ (debt) (RMm) (2Q16)	205.6
ROE (2016E)	35.1%
Derivatives	Nil
(Warr A 06/18, EP RM0.264)	
(Warr B 02/20, EP RM1.60)	
Shariah Compliant	Yes

Key Shareholders

Insas Bhd	23.9%
KWAP	7.1%
EPF	6.5%

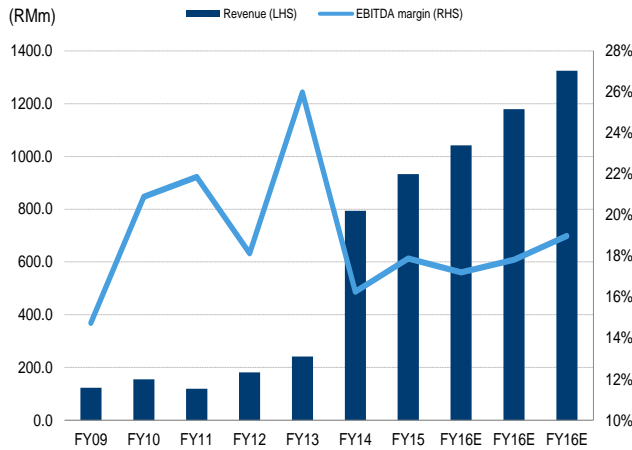
Source: Affin Hwang, Bloomberg

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Focus charts

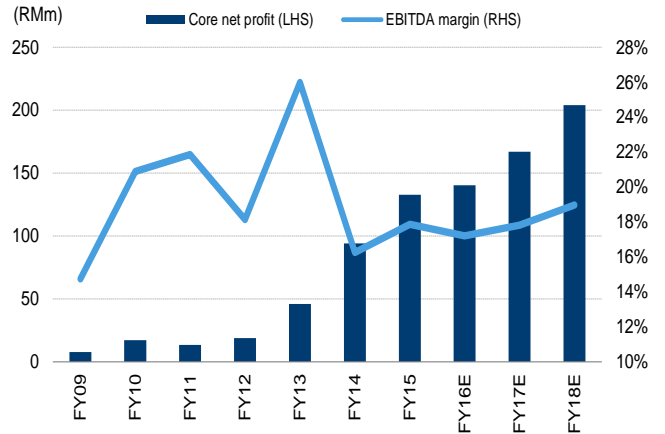
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Fig 1: Revenue and earnings projected to rise



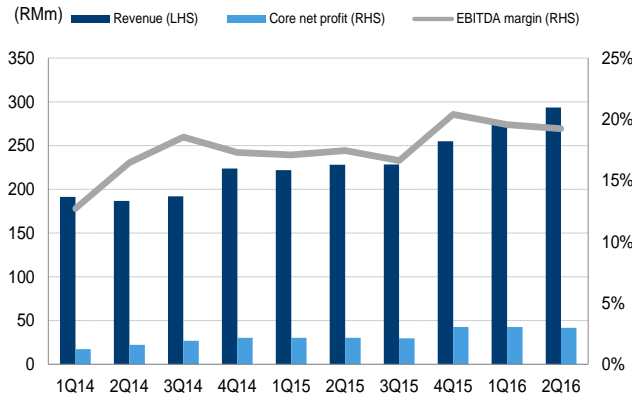
Source: Company, Affin forecasts

Fig 2: 3-year forward net profit CAGR of 18%



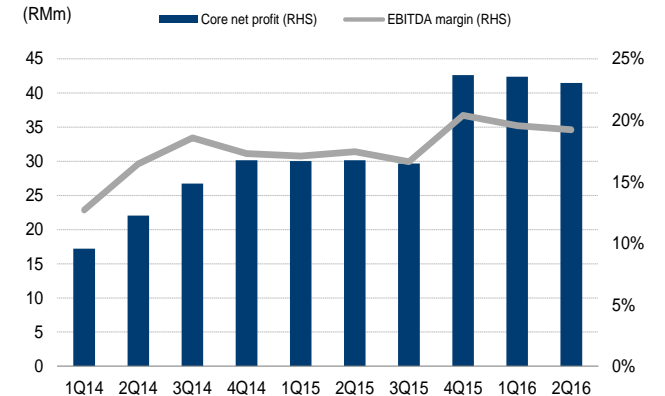
Source: Company, Affin forecasts

Fig 3: RM depreciation has aided recent quarters growth



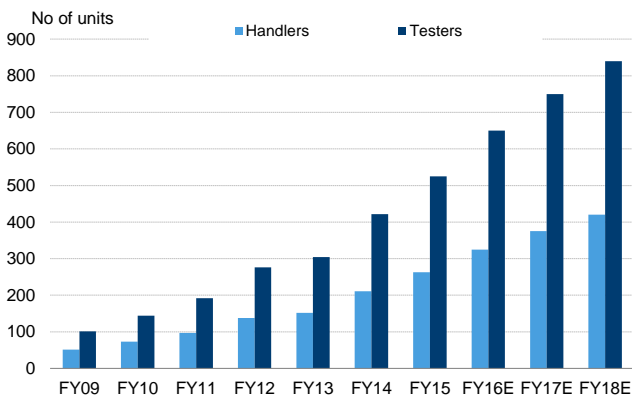
Source: Company, Affin

Fig 4: ..and likewise profitability



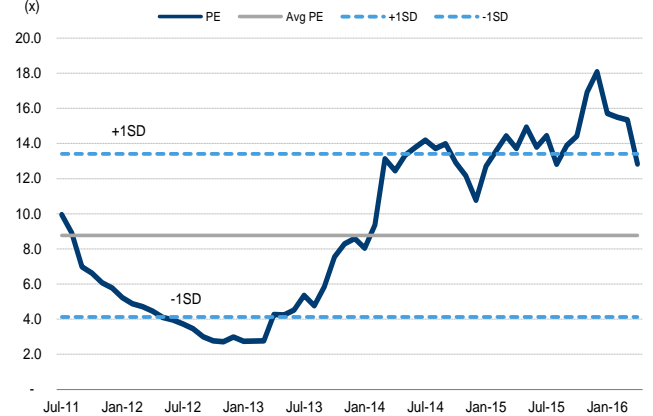
Source: Company, Affin

Fig 5: Capacity has been progressively increased



Source: Company, Affin

Fig 6: PE band



Source: Bloomberg

INARI – FINANCIAL SUMMARY

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Profit & Loss Statement

FYE June (RMm)	2014	2015	2016E	2017E	2018E
Total revenue	794	933	1055	1194	1341
Operating expenses	(665)	(766)	(862)	(969)	(1073)
EBITDA	129	167	192	225	268
Depreciation	(23)	(33)	(23)	(26)	(28)
Amortisation	0	0	0	0	0
EBIT	106	133	169	199	241
Net interest income/(expense)	(5)	(2)	(1)	1	3
Associates' contribution	0	0	0	0	0
Others	0	0	0	0	0
Pretax profit	102	132	167	200	244
Tax	(7)	(1)	(12)	(12)	(15)
Minority interest	(1)	2	(3)	(7)	(9)
Net profit	99	153	155	181	220
Core net profit	94	133	152	181	220

Balance Sheet Statement

FYE June (RMm)	2014	2015	2016E	2017E	2018E
Fixed assets	130	190	211	231	248
Other long term assets	16	14	14	14	14
Total non-current assets	145	204	226	245	263
Cash and equivalents	57	144	195	267	364
Stocks	138	145	173	196	221
Debtors	137	187	173	196	221
Other current assets	20	154	154	154	154
Total current assets	352	631	696	813	959
Creditors	120	171	159	180	202
Short term borrowings	36	45	45	45	45
Other current liabilities	13	16	16	16	16
Total current liabilities	170	232	220	241	263
Long term borrowings	66	65	65	65	65
Other long term liabilities	3	3	3	3	3
Total long term liabilities	69	68	68	68	68
Shareholders' Funds	259	535	634	750	891

Cash Flow Statement

FYE June (RMm)	2014	2015	2016E	2017E	2018E
EBIT	106	133	169	199	241
Depreciation & amortisation	23	33	23	26	28
Working capital changes	-91	-6	-26	-25	-26
Cash tax paid	-1	-1	-12	-12	-15
Others	4	17	2	1	3
Cashflow from operations	41	176	156	189	230
Capex	-41	-62	-45	-45	-45
Disposal/(purchases)	-3	-27	0	0	0
Others	0	0	0	0	0
Cash flow from investing	-44	-89	-45	-45	-45
Debt raised/(repaid)	54	161	0	0	0
Equity raised/(repaid)	0	21	2	0	0
Net inct income/(expense)	-5	-2	-1	1	3
Dividends paid	-22	-52	-62	-72	-88
Others	7	2	1	-1	-3
Cash flow from financing	35	131	-60	-72	-88
Net change in CF	31	218	51	72	97
Free Cash Flow	-1	87	111	144	185

Source: AffinHwang, Company data

Key Financial Ratios and Margins

FYE June (RMm)	2014	2015	2016E	2017E	2018E
Growth					
Revenue (%)	229.1	17.6	13.0	13.2	12.4
EBITDA (%)	105.9	29.3	15.2	17.0	19.3
Core net profit (%)	104.1	41.1	14.8	18.8	21.7
Profitability					
EBITDA margin (%)	16.3	17.9	18.2	18.8	20.0
PBT margin (%)	13.5	16.3	16.2	16.8	18.2
Net profit margin (%)	12.5	16.3	14.7	15.2	16.4
Effective tax rate (%)	6.1	0.9	7.0	6.0	6.0
ROA (%)	20.0	18.3	16.9	17.1	18.0
Core ROE (%)	45.2	33.4	26.1	26.2	26.8
ROCE (%)	42.5	29.1	25.9	26.2	27.1
Dividend payout ratio (%)	35.4	40.0	40.0	40.0	40.0
Liquidity					
Current ratio (x)	2.1	2.7	3.2	3.4	3.6
Op. cash flow (RMm)	40.6	176.2	155.6	189.1	230.3
Free cashflow (RMm)	(0.6)	113.8	110.6	144.1	185.3
FCF/share (sen)	(0.1)	11.9	11.6	15.1	19.5
Asset management					
Debtors turnover (days)	63.2	73.3	60.0	60.0	60.0
Stock turnover (days)	63.4	56.8	60.0	60.0	60.0
Creditors turnover (days)	55.2	67.0	55.0	55.0	55.0
Capital structure					
Net Gearing (%)	(0.8)	(43.2)	(44.4)	(47.1)	(50.6)
Interest Cover (x)	23.8	29.2	43.9	51.4	56.9

Quarterly Profit & Loss

FYE June (RMm)	2Q15	3Q15	4Q15	1Q16	2Q16
Revenue	228	228	255	275	294
Operating expenses	-188	-190	-203	-221	-237
EBITDA	40	38	52	54	56
Depreciation	-8	-8	-10	-12	-12
EBIT	32	30	42	42	45
Net int income/(expense)	-2	0	0	-1	0
Associates' contribution	1	2	3	4	5
Exceptional Items	10	8	-2	3	0
Pretax profit	41	40	43	48	50
Tax	-1	-1	0	-1	-2
Minority interest	1	1	0	3	-1
Net profit	41	40	43	50	46
Core net profit	31	32	46	46	46
Margins (%)					
EBITDA	17.4	16.6	20.4	19.6	19.2
PBT	18.0	17.5	16.8	17.4	17.0
Net profit	18.1	17.6	17.0	18.0	15.8

Equity Rating Structure and Definitions

BUY	Total return is expected to exceed +10% over a 12-month period
HOLD	Total return is expected to be between -5% and +10% over a 12-month period
SELL	Total return is expected to be below -5% over a 12-month period
NOT RATED	Affin Hwang Investment Bank Berhad does not provide research coverage or rating for this company. Report is intended as information only and not as a recommendation

The total expected return is defined as the percentage upside/downside to our target price plus the net dividend yield over the next 12 months.

OVERWEIGHT	Industry, as defined by the analyst's coverage universe, is expected to outperform the KLCI benchmark over the next 12 months
NEUTRAL	Industry, as defined by the analyst's coverage universe, is expected to perform inline with the KLCI benchmark over the next 12 months
UNDERWEIGHT	Industry, as defined by the analyst's coverage universe is expected to under-perform the KLCI benchmark over the next 12 months

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