

Outthink. Outperform.

Trough has likely passed

Inari's near-term outlook remains encouraging with a likely earnings rebound set for 4QFY16 following key customer Broadcom's upbeat guidance for its wireless segment. Moreover, long-term drivers are in place as Inari further entrenches itself in the data-network segment. Reaffirm BUY and 12-month TP of RM3.54, based on 18x CY17E PER.

Likely strong 4QFY16 given upbeat guidance from Broadcom

Inari appears to be on track to register revenue growth of 20% over the previous quarter. This is underpinned by a combination of reasons: 1) a low base in 3QFY16 where revenue fell 26% qoq; and 2) strong shipments by a Korean customer. Recent management outlook and guidance on the 2Q16 analysts' result call from Broadcom, a key customer, further confirms our view of Inari's improved outlook in the coming quarters.

Broadcom's wireless division to see mid 20% growth

According to Broadcom's President, Hock Tan, the wireless division is expected to see mid-20% sequential revenue growth in the upcoming quarter. He further elaborated that strong revenue growth should further sustain in the following quarter as it would capture the full ramp of its North American customer. However, apart from the usual strong seasonal ramp, the next generation phones are also expected to see higher RF content per device. This is consistent with the growth that we are projecting for Inari's RF segment.

New RF testers to meet demand

We expect the number of Inari's RF testers to hit 680 units by September (from the present 609 units). This represents a 61% increase from the 422 units as at end-June 2014. Thus far, capacity has mirrored Broadcom's own expansion, although we understand that the capacity still lags behind Broadcom's own wafer-fab expansion, which has effectively doubled over the same period. Hence, while Inari is ready to capture the growth that Broadcom is expected to experience, we believe that Broadcom will still need to rely on its other contractors to fulfil capacity in the coming quarters. We also understand that Broadcom has qualified a number of new contractors to fulfil this requirement. While this may appear to be a risk, we nevertheless believe that there is sufficient growth opportunities for Inari.

Earnings & Valuation Summary

FYE 30 June	2014	2015	2016E	2017E	2018E
Revenue (RMm)	793.7	933.1	1,054.6	1,193.9	1,341.4
EBITDA (RMm)	129.0	166.8	192.1	224.8	268.3
Pretax profit (RMm)	106.9	151.7	170.5	200.3	243.6
Net profit (RMm)	99.2	152.5	155.5	180.9	220.2
EPS (sen)	10.4	16.0	16.3	19.0	23.1
PER (x)	28.5	18.5	18.2	15.6	12.8
Core net profit (RMm)	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 growth (%)	104.1	41.1	14.8	18.8	21.7
Core PER (x)	30.1	21.3	18.6	15.6	12.8
Net DPS (sen)	6.8	6.4	6.5	7.6	9.2
Dividend Yield (%)	2.3	2.2	2.2	2.6	3.1
EV/EBITDA (x)	21.9	15.6	13.3	11.0	8.9

Chg in EPS (%)	-	-	-
Affin/Consensus (x)	1.0	0.9	1.0

Source: Company, Affin Hwang forecasts, Bloomberg

Company Update

Inari Amertron

INRI MK

Sector: Technology

RM2.97 @ 13 June 2016

BUY (maintain)

Upside 19%

Price Target: RM3.54

Previous Target: RM3.54



Price Performance

	1M	3M	12M
Absolute	+8.8	-9.7	+7.7
Rel to KLCI	+8.5	-6.2	+14.4

Stock Data

Issued shares (m)	956.5
Mkt cap (RMm)/(US\$m)	2840.9/694.6
Avg daily vol - 6mth (m)	4.46
52-wk range (RM)	2.24-3.96
Est free float	52.4%
BV per share (RM)	0.68
P/BV (x)	4.37
Net cash/ (debt) (RMm) (3Q16)	210.6
ROE (2016E)	26.1%
Derivatives	Nil
(Warr A 06/18, EP RM0.264)	
(Warr B 02/20, EP RM1.60)	
Shariah Compliant	Yes

Key Shareholders

Insas Bhd	23.7%
EPF	8.2%
KWAP	7.6%

Source: Affin Hwang, Bloomberg

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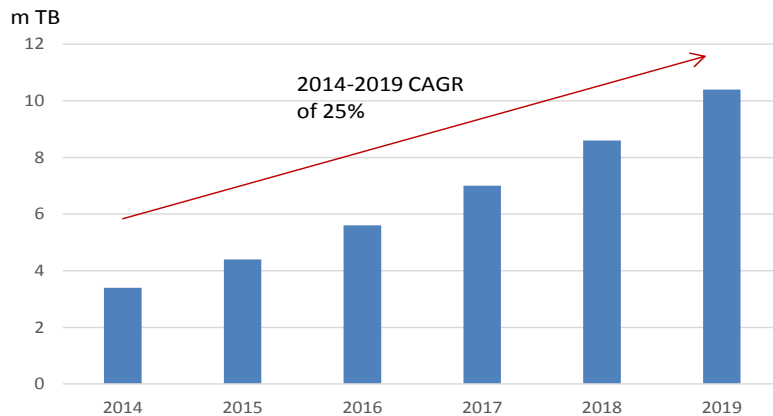
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Plant 21 should be a new journey

Moreover, the completed renovation of Plant 21 by end-June 2016 should pave the way for further expansion ahead. Approximately 50 new testers are expected to be installed as part of Phase 1 to cater to Broadcom's wired division. These new products would likely encompass network switches used in the cloud and data-storage space.

Market for network switches will likely remain exciting...

Broadcom has a leading market share in network switches and this market segment is expected to continue to remain exciting in the years to come as the technology-upgrade cycle plays out. The key drivers behind the upgrade cycle lie in the necessity to cater for improved performance as servers and storage become faster while 4K resolution becomes more mainstream. From a cost perspective, with a rapidly-declining ASP for switches, there should also be impetus for a transition from 10GbE to 25GbE. Finally, a large-scale rollout of cloud servers would further accelerate the adoption of this technology upgrade.

Global Data Centre IP traffic growth

Source: Cisco

...which should be positive longer term

Again, we are positive long term as the transfer of new products and technology should further entrench Inari's position as a major contractor for Broadcom, apart from diversifying its exposure away from the latter's wireless division. And, although this new business is a deviation away from Avago's business model where equipment was predominantly consigned, we believe that any capex outlay should be allayed by the RM100m grant procured from MIDA for this new product transfer.

Reaffirm BUY and target price of RM3.54

We reaffirm our BUY rating and 12-month target price of RM3.54 (based on an unchanged 18x CY17E PER). Key risks to our call would be a slowdown in global demand for smart devices, rapid ASP erosion, loss of customer base and the introduction of new technologies that may render Inari's products obsolete. Inari is also a country top pick for 2016.

INARI – FINANCIAL SUMMARY

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 inc 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

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

Source: AffinHwang forecasts, Company data

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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