

22 August 2019

D&O Green Technologies Flashing Recovery Signs

2Q19 core PATAMI came in below expectations at RM6.0m (+79% YoY; -1.6% QoQ), bringing 1H19 core PATAMI to RM12.1m (+23% YoY), forming only 29% of both consensus and our full-year estimates due to lower-than-expected gross profit margin. No dividend was announced, as expected. Trim FY19-20E core PATAMIs by 9-8% to RM38.0-46.2m. Maintain OUTPERFORM with lower TP of RM0.625.

Below expectations. 2Q19 core PATAMI came in below expectations at RM6.0m (+79% YoY; -1.6% QoQ). This brought 1H19 core PATAMI to RM12.1m (+23% YoY), accounting for only 29% of both consensus and our full-year estimates. The earnings disappointment mainly stemmed from lower-than-expected gross profit margin (27.1% in 1H19 vs. our FY19 assumption of 28.5%) amid tough operating environment. No dividend was announced during the quarter, as expected.

YoY, commendably, 1H19 revenue inched up 1% despite falling passenger vehicle sales in key markets like China and the Europe. We believe this signifies that the group has been gaining market share in the automotive LED space. The stronger core PATAMI growth of 23% is explained by a lower effective tax rate of 17.7% (vs. 22.6% in 1H18), thanks to capital and investment allowances. **QoQ**, despite a slight 2% growth in 2Q19 revenue, core PATAMI edged down by 2% owing to lower foreign exchange gain (-85% or -RM0.4m) and higher inventory impairment (66% or +RM0.9m).

Flashing recovery signs. Moving into 2H19, we believe earnings would pick up on a combination of seasonality and automotive market recovery. Traditionally, 4Q is the strongest quarter as D&O's customers ramp up orders to prepare for stronger festive and year-end promotional period demands. The monthly decline in China's passenger vehicle sales has been narrowing from mostly double-digit growth over the past one year to low single-digit (3.9% in July). Additionally, CEIC data show that China's passenger car inventory has been declining from close to 900k units in the beginning of this year to c.753k units in June 2019. With VI emission standards concluded in July 2019, alongside a series of friendly policies in 2H19 (e.g. tax-cut for rural consumers, fees reduction and lifting of licence plates quota in Guangzhou and Shenzhen), passenger vehicle sales are likely to return to the growth trajectory. In the Europe, we are also seeing possible signs of recovery as the adverse effect of the Worldwide Light Vehicles Test Procedure (WLTP; introduced in September 2018) subsides.

Trim FY19-20E core PATAMIs by 9-8% to RM38.0-46.2m as we lower our gross profit margin assumptions from 28.5-29.5% to 27.5-28.5%.

Maintain OUTPERFORM with lower Target Price of RM0.625 (previously RM0.675) based on an unchanged FY20E PER of 18.0x, in line with the valuation of its German competitor. D&O is a prime proxy for the potential recovery in the automotive market, amplified by its rising LED content in passenger vehicles and its augmenting market share. The introduction of smart LED (boosting ASP substantially) and growing focus on higher-margin exterior lightings also offer bright prospects and ensure sustainable long-term growth. These prospects are backed by its ongoing factory expansion plan, which could increase production capacity by as much as 3x. Having corrected 40-50% from the 52-week high of RM1.00 (on 4 October 2018), D&O appears highly attractive at the current level.

Risks to our call include: (i) disruption of components supply, (ii) replacement/obsolescence of LED technology, (iii) adverse currency fluctuations, and (iv) adverse foreign labour policy.

OUTPERFORM ↔

Price: RM0.550
Target Price: RM0.625 ↓

Expected Capital Gain: RM0.075 +13.6%
Expected Div. Yield: RM0.011 +2.0%
Expected Total Return: RM0.086 +15.6%

KLCI Index 1,594.59

Stock Information

Bloomberg Ticker	DOGT MK Equity
Bursa Code	7204
Listing Market	Main Market
Shariah Compliant	Yes
Shares Outstanding	1,110.1
Market Cap (RM m)	610.5
Par value per share (RM)	0.10
52-week range (H)	1.00
52-week range (L)	0.51
Free Float	61%
Beta	1.0
3-mth avg daily vol	2,730,944

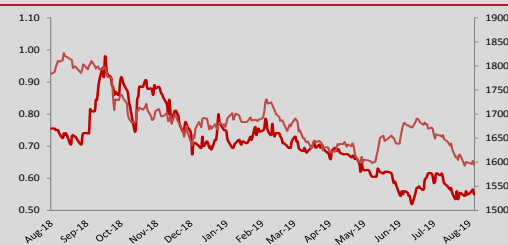
Major Shareholders

Prt Capital Pte Ltd	14.6%
Keen Capital Investments	13.8%
Omega Riang Sdn Bhd	10.2%

Summary Earnings Table

FY Dec (RM m)	2018A	2019E	2020E
Turnover	490.8	509.0	562.6
EBIT	85.1	87.2	100.7
PBT	52.1	52.2	63.5
Net Profit	36.0	38.0	46.2
Core PATAMI	31.1	38.0	46.2
Consensus (NP)	N.A.	42.4	50.3
Earnings Revision	N.A.	-9%	-8%
Core EPS (sen)	2.7	3.0	3.4
Core EPS growth (%)	42.3	14.0	14.1
NDPS (sen)	0.5	1.1	1.3
NTA per Share (RM)	0.28	0.28	0.28
Price to NTA (x)	2.0	2.0	1.9
PER (x)	20.7	18.2	15.9
Debt-to-Equity ratio (x)	0.1	0.1	0.1
Return on Asset (%)	6%	7%	8%
Return on Equity (%)	10%	11%	12%
Net Div. Yield (%)	0.9%	2.0%	2.4%

Share Price Performance



	1 mth	3 mths	12 mths
Absolute (%)	-10.6%	-12.0%	-26.7%
Relative (%)	-6.7%	-11.4%	-15.3%

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Results Highlights

	2Q	1Q	QoQ	2Q	YoY	1H	1H	YoY
FYE Dec (RM'm)	FY19	FY19	Chg	FY18	Chg	FY19	FY18	Chg
Turnover	115.0	113.1	1.8%	113.3	1.6%	228.1	226.3	0.8%
GP	31.3	30.5	2.3%	31.2	0.3%	61.8	62.0	-0.3%
EBIT	8.9	9.0	-0.7%	12.3	-27.2%	17.9	22.6	-20.8%
Adjusted EBIT	9.0	9.1	-1.0%	6.9	29.9%	18.0	17.8	1.1%
PBT/(LBT)	8.2	8.3	-1.2%	11.8	-30.9%	16.4	21.7	-24.3%
Taxation	-1.4	-1.5	2.1%	-2.7	46.1%	-2.9	-4.9	40.5%
PAT	6.7	6.8	-1.0%	9.1	-26.5%	13.5	16.8	-19.6%
Core PAT	6.8	6.9	-1.5%	3.8	78.9%	13.6	13.4	1.6%
Net Profit / (Loss)	6.0	6.0	-1.2%	8.1	-26.6%	12.0	13.3	-9.5%
Core NP	6.0	6.1	-1.6%	3.4	78.6%	12.1	9.8	23.4%
FD EPS (sen)	0.4	0.4	-1.2%	0.5	-27.2%	0.8	0.9	-10.2%
DPS (sen)	0.0	0.5		0.0		0.5	0.0	
GP margin	27.2%	27.0%		27.5%		27.1%	27.4%	
EBIT margin	7.8%	7.9%		10.8%		7.8%	10.0%	
Adjusted EBIT margin	7.8%	8.0%		6.1%		7.9%	7.9%	
Pretax margin	7.1%	7.3%		10.4%		7.2%	9.6%	
NP margin	5.2%	5.3%		7.2%		5.3%	5.9%	
CNP margin	5.2%	5.4%		3.0%		5.3%	4.3%	
Effective tax rate	-17.6%	-17.8%		-22.6%		-17.7%	-22.6%	

Source: Company, Kenanga Research

Segmental Breakdown

	2Q	1Q	QoQ	2Q	YoY	1H	1H	YoY
Total Revenue (RM'm)	FY19	FY19	Chg	FY18	Chg	FY19	FY18	Chg
Total Revenue (RM'm)	115.0	113.1	1.8%	113.3	1.6%	228.1	226.3	0.8%
Automotive	113.1	109.7	3.1%	106.9	5.8%	222.8	213.6	4.3%
Non-automotive	1.9	3.4	-43.2%	6.4	-69.7%	5.3	12.7	-58.0%

Source: Company, Kenanga Research

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Malaysian Technology Peers Comparison

Name	Last Price (RM)	Market Cap (RM'm)	Shariah Compliant	Current FYE	Revenue Growth		Core Earnings Growth		PER (x) - Core Earnings			PBV (x)		ROE (%)	Net Div Yld (%)	Target Price (RM)	Rating
					1-Yr. Fwd.	2-Yr. Fwd.	1-Yr. Fwd.	2-Yr. Fwd.	Hist.	1-Yr. Fwd.	2-Yr. Fwd.	Hist.	1-Yr. Fwd.	1-Yr. Fwd.			
D&O GREEN TECHNOLOGIES BERHAD	0.550	610.5	Y	12/2019	3.7%	10.5%	22.2%	21.8%	20.7	18.2	15.9	2.0	2.0	10.6%	2.0%	0.625	OP
KESM INDUSTRIES BERHAD	6.99	300.7	N	07/2019	-9.8%	15.1%	-70.7%	74.3%	7.6	26.1	15.0	0.8	0.8	3.2%	2.6%	8.70	OP
MALAYSIAN PACIFIC INDUSTRIES BERHAD	8.44	1,678.7	N	06/2019	8.1%	5.3%	16.0%	5.8%	9.8	8.5	8.0	1.5	1.4	13.6%	3.7%	12.10	OP
P.I.E. INDUSTRIAL BERHAD	1.16	445.5	Y	12/2019	5.5%	7.3%	-7.5%	16.2%	10.5	11.4	9.8	1.1	1.0	9.1%	4.3%	1.20	MP
SKP RESOURCES BHD	1.16	1,450.2	Y	03/2020	24.9%	13.3%	21.5%	17.0%	15.0	12.3	10.5	2.5	2.2	19.0%	4.1%	1.20	MP
UNISEM (M) BERHAD	2.09	1,519.6	Y	12/2019	-6.8%	2.7%	-25.5%	31.4%	15.9	21.5	16.4	1.1	1.0	4.9%	2.9%	2.05	MP

Source: Bloomberg, Kenanga Research

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Stock Ratings are defined as follows:**Stock Recommendations**

OUTPERFORM	: A particular stock's Expected Total Return is MORE than 10%
MARKET PERFORM	: A particular stock's Expected Total Return is WITHIN the range of -5% to 10%
UNDERPERFORM	: A particular stock's Expected Total Return is LESS than -5%

Sector Recommendations***

OVERWEIGHT	: A particular sector's Expected Total Return is MORE than 10%
NEUTRAL	: A particular sector's Expected Total Return is WITHIN the range of -5% to 10%
UNDERWEIGHT	: A particular sector's Expected Total Return is LESS than -5%

*****Sector recommendations are defined based on market capitalisation weighted average expected total return for stocks under our coverage.**

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