BUY (Unchanged) | **TP: Bt 6.50** (From: Bt 6.40)

Change in Numbers | **Upside : 50.5%** | **19 MAY 2022**

Stark Corporation Pcl. (STARK TB)

Strong growth intact

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STARK proved in 1Q22 that its cost-plus revenue model worked amid a surge in raw material costs. We lift our earnings estimates by 20/7% in 2022-23F and see STARK as inexpensive at 18x 2022F PE versus a 19% EPS CAGR over 2022-24F. Reaffirm BUY with a Bt6.5 TP.

Cost-plus model works

We raise our 2022-23F earnings for STARK by 20% and 7% and lift our DCF-based 12-month TP (2022F base year) to Bt6.5 (from Bt6.4). We underestimated its gross margin since we did not include the 'realized FX gains' in our core earnings calculation. STARK operates a cost-plus model, in which it fixes selling prices and costs on the day it receives orders. As over 80% of COGS is dollar-based imported metals, mainly copper and aluminum, STARK hedges the currency to fully lock in margins. Therefore, realized FX gains and losses from those hedges should always be netted off from its COGS to properly reflect margins. After factoring that in, STARK's gross margin in 1Q22 was 21.7% vs. 20.6% in 4Q21 despite a rising copper price and the weakening Thai baht against the US dollar. This proves STARK's cost-plus model works even amid these unfavorable conditions.

Strong growth outlook

We now project a 19% EPS CAGR for STARK over 2022-24F via three major drivers. *First,* we expect strong growth in electricity cable demand in Thailand and Vietnam as we believe their new Power Development Plans (PDPs), likely to be released this year, will result in more developments of power plants and transmission lines. *Second,* the US cable market has become STARK's new export destination since 2H21 and we expect it to be another growth driver for STARK and lift exports to 20% of STARK's sales in 2025F (12% in 2021). *Third,* we expect STARK's gross margin to continue rising on better product mix and scale benefits.

Rising margin trend

We estimate STARK's gross margin to widen to 25% in 2024F, from 22% in 2021. A rising portion of high voltage and specialty (i.e., submarine and underground) cables vs. total sales is the key support factor. Growing revenue also yields scale benefits and higher plant utilization. STARK has proven over the past year that it can sustain margins despite the surge in metal prices which has pushed up raw material costs significantly for its buyers.

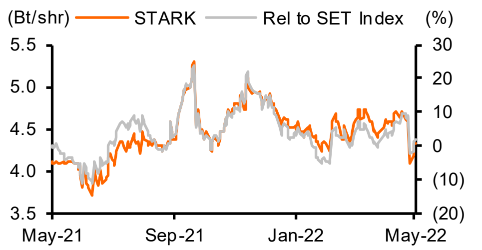
Attractive valuations in our view

We see STARK as an inexpensive growth stock, trading at only 18x PE vs. 22/17/18% EPS growth in 2022-24F. The multiple also looks mispriced to us given the company's long-term ROE at 35% from 2024F, which is impressive for a manufacturing company in our view. This is despite its gearing falling to 0.3x net D/E. We also expect STARK to offer a decent 4% dividend yield that year.

COMPANY VALUATION

Y/E Dec (Bt m)	2021A	2022F	2023F	2024F
Sales	27,094	30,861	34,395	37,750
Net profit	2,783	3,908	4,582	5,389
Consensus NP	—	3,264	4,304	5,348
Diff frm cons (%)	—	*19.7*	*6.5*	*0.8*
Norm profit	3,203	3,908	4,582	5,389
Prev. Norm profit	—	3,264	4,304	5,348
Chg frm prev (%)	—	*19.7*	*6.5*	*0.7*
Norm EPS (Bt)	0.2	0.2	0.3	0.3
Norm EPS grw (%)	170.7	22.0	17.2	17.6
Norm PE (x)	21.4	17.5	15.0	12.7
EV/EBITDA (x)	15.4	12.6	10.7	8.7
P/BV (x)	10.5	7.3	5.8	3.7
Div yield (%)	0.0	2.8	3.3	3.9
ROE (%)	63.3	49.0	43.0	35.2
Net D/E (%)	198.1	120.5	92.6	31.0

PRICE PERFORMANCE



COMPANY INFORMATION

Price *as of* 19-May-22 (Bt)	4.32
Market Cap (US$ m)	1,488.5
Listed Shares (m shares)	11,906.4
Free Float (%)	28.8
Avg Daily Turnover (US$ m)	4.9
12M Price H/L (Bt)	5.30/3.72
Sector	Industrial Materials & Machinery
Major Shareholder	K.Vonnarat Tangkaravakoon 48.7%

Sources: Bloomberg, Company data, Thanachart estimates

Strong growth looks intact

BUY for a robust long-term earnings growth outlook

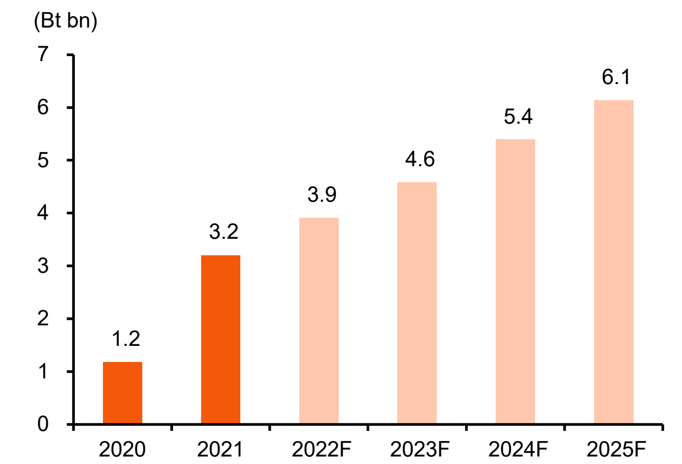
We reaffirm our BUY rating on shares of Stark Corporation Pcl (STARK), which we see as an inexpensive growth stock trading at 18x PE in 2022F vs. a 19% three-years EPS CAGR over 2022-24F. The strong earnings growth is supported by three major drivers in our view.

- **First,** we expect robust demand for electricity cables to continue in Thailand and Vietnam, which are STARK's production bases, especially after the release of their new Power Development Plan (PDPs), likely later this year. This is since we expect the PDPs to accelerate investment in electricity infrastructure projects, both transmission systems and power plants, in both countries.
- **Second,** having started in 2H21, we expect STARK's penetration into the US power cable market to become its next major revenue growth for 2022-23F and raise exports to 20% of its total sales in 2024F, up from 12% last year (2021).
- **Third,** we project STARK's improving margin trend to continue, rising to 25% in 2024F from 22% in 2021, driven by 1) a better product mix with growing portions of high-voltage and specialty cables, 2) stronger pricing power for raw material procurement from scale benefits, and 3) higher operating leverage from an improving utilization rate.

We lift our TP to Bt6.5/share after our earnings hikes

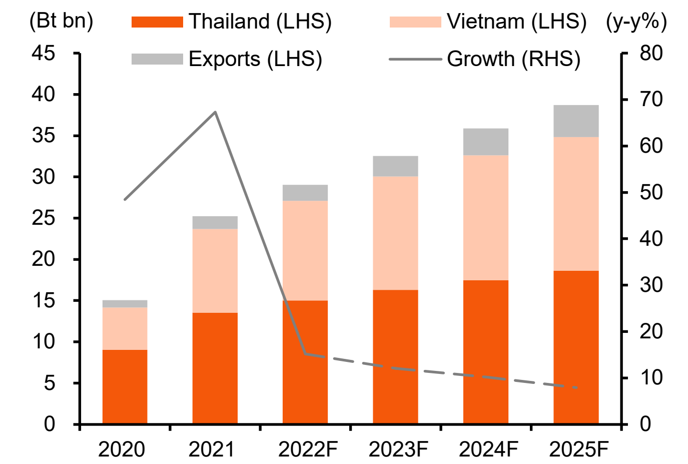
We boost our earnings estimates by 20% and 7% in 2022-23F after including STARK's realized FX gains from hedging in its core profit. We explain the reasons behind this change in our methodology in the last part of this report. After our earnings hikes, our DCF-based 12-month TP (2022F base year) for STARK is lifted to Bt6.5/share (from Bt6.4 previously).

Ex 1: Steady But Strong Earnings Growth Trend



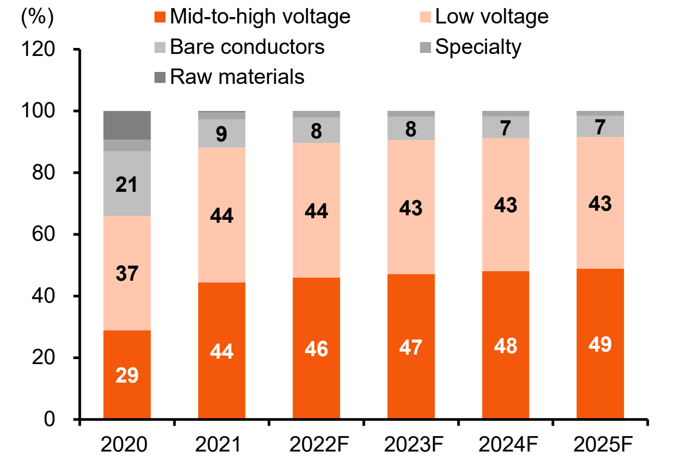
Sources: Company data, Thanachart estimates

Ex 2: Domestic Revenues Remain The Core Driver



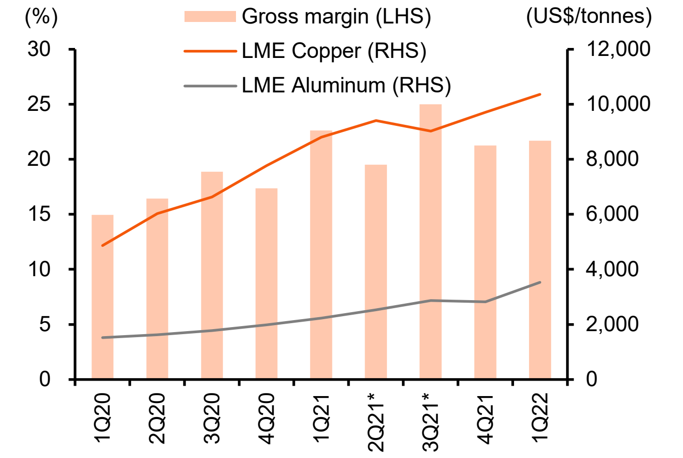
Source: Thanachart estimates

Ex 3: Rising High-Margin Product Portion In Sales Mix



Sources: Company data, Thanachart estimates

Ex 4: Proven Sustainable Margin Under Cost-Plus Model



Source: Company data

Note: * Adjusted for its shift of revenue recognition between the periods

Ex 5: Key Assumption Changes

	2020	2021	2022F	2023F	2024F
Normalized profit (Bt m)					
- New	1,183	3,203	3,908	4,582	5,389
- Old			3,264	4,304	5,348
- Change (%)			*19.7*	*6.5*	*0.7*
Total revenue (Bt bn)					
- New	16.9	27.1	30.9	34.4	37.7
- Old			31.2	35.5	39.7
- Change (%)			*(1.0)*	*(3.2)*	*(4.8)*
Gross margin (%)					
- New	18.1	22.0	23.2	24.2	25.0
- Old			21.3	23.1	24.1
- Change (pp)			*1.8*	*1.0*	*0.9*

Sources: Company data, Thanachart estimates

Appendix: Change in our core earnings calculation

We include 'realized FX gains' in its core profit

We had previously been underestimating STARK's earnings since we did not incorporate "realized FX gains/losses from hedging" into our core profit calculations. However, after our recent detailed discussion with the company, we now realize that the item is a part of its core business.

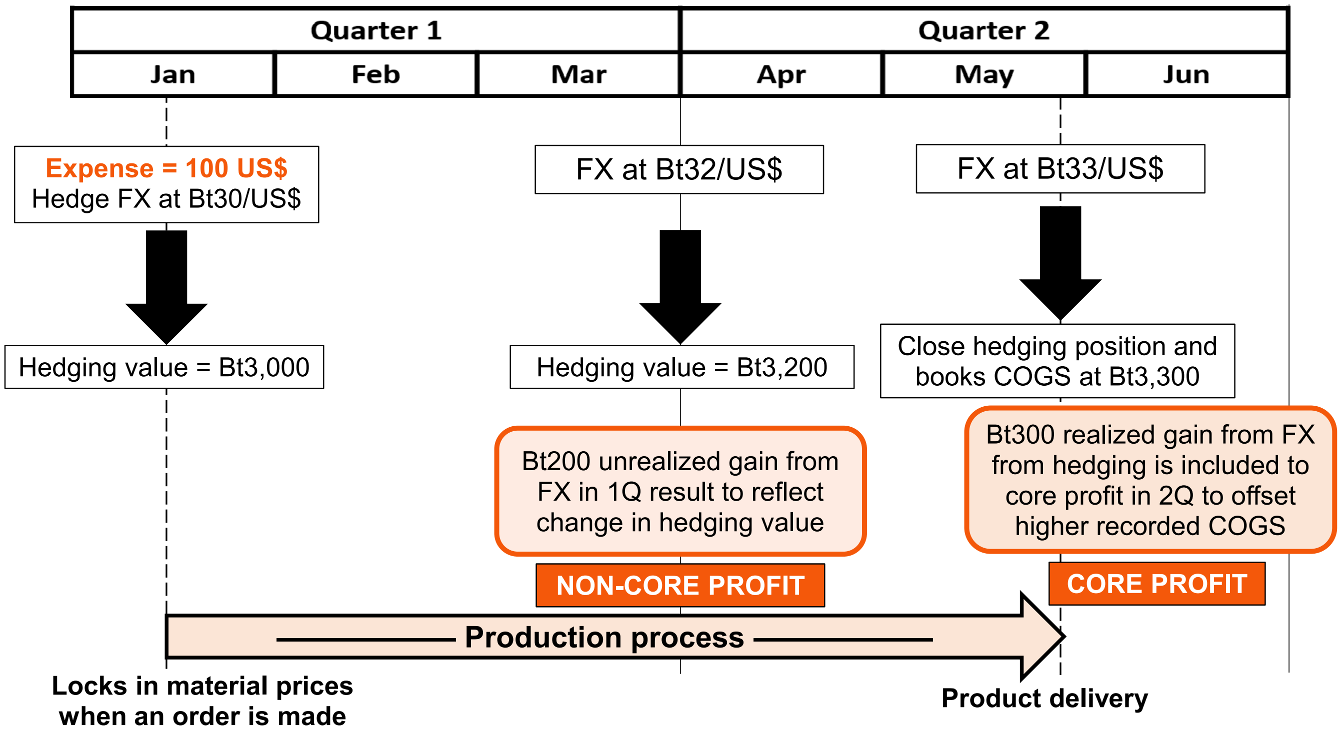
STARK has a policy to fully hedge US-dollar COGS

Due to the customizable and made-to-order nature of electricity cable products, STARK is able to set selling prices in a cost-plus manner. Its products have no standard market prices so customers need to request a price quote for every order they make. STARK is thus able to quote product prices based on current raw material costs plus some margin, depending on the complexity of the manufacturing. Given that over 80% of those materials are US dollar based, mainly copper and aluminum, STARK has a policy to fully hedge those dollar costs to ensure its margin. Therefore, we believe the gains/losses from those currency hedging instruments (shown as realized FX gains/losses in its financial statements) must be included in its core profit calculation, by netting off against its reported COGS to better reflect operating margin from product sales.

We provide a scenario in Exhibit 6

We show a scenario of the process in Exhibit 6. When its customer makes an order during 1Q, STARK immediately purchases the required raw materials (assumed to cost US$100 under this scenario) and fully hedges the amount. At the end of 1Q, assuming the baht weakens to Bt32/US$1 (from Bt30 when it made the hedge) the order has yet to be delivered so neither revenue nor COGS are booked in the quarter, while the hedging value is marked to market, incurring a Bt200 unrealized FX gain. We do not include this accounting gain in our core profit calculation. During 2Q, STARK delivers the order and books revenue and COGS in its quarterly results. As it then closes its hedging position immediately, it also records a Bt300 FX gain (assuming the baht weakens further to Bt33/US$ at the time of recognition). We include this "realized FX gain" in STARK's core profit by deducting it from COGS, so we can then calculate the actual margin that STARK marks up to the order.

Ex 6: We Add 'Realized FX Gain/Loss From Hedging' To STARK's Core Profit



Sources: Company data, Thanachart compilation

Ex 7: 12-month DCF-based TP Calculation Using A Base Year Of 2022F

(Bt m)	2022F	2023F	2024F	2025F	2026F	2027F	2028F	2029F	2030F	2031F	2032F	2033F	Terminal Value
EBITDA (excl. depre from right of use)	6,311	7,391	8,459	9,352	10,157	10,890	11,549	12,173	12,728	13,308	13,914	14,549	—
Free cash flow	1,056	2,744	23,641	4,898	5,850	6,716	7,616	8,071	8,482	8,888	9,312	9,755	153,020
PV of free cash flow	1,053	2,371	18,979	3,655	4,056	4,223	4,432	4,347	4,228	4,101	3,976	3,662	57,448

Risk-free rate (%)	2.5
Market risk premium (%)	8.0
Beta	0.9
WACC (%)	7.6
Terminal growth (%)	2.0
Enterprise value - add investments	116,530
Net debt (2021)	13,060
Minority interest	87
Equity value	103,384
# of shares *	15,875
Equity value/share (Bt)	**6.50**

Sources: Company data, Thanachart estimates

Note: * We use the number of fully diluted shares in our DCF calculation, assuming all of its STARK-W1 warrants are exercised in 2024F.

Valuation Comparison

Ex 8: Comparison With Regional Peers

Name	BBG code	Country	EPS growth 22F (%)	EPS growth 23F (%)	PE 22F (x)	PE 23F (x)	P/BV 22F (x)	P/BV 23F (x)	EV/EBITDA 22F (x)	EV/EBITDA 23F (x)	Div yield 22F (%)	Div yield 23F (%)
Nexans SA	NEX FP	France	28.7	20.4	16.7	13.9	2.3	2.1	6.9	6.2	1.6	1.8
nVent Electric PLC	NVT US	Britain	35.3	7.8	15.5	14.4	2.2	2.1	12.8	11.8	2.2	2.3
TE Connectivity Ltd	TEL US	Switzerland	4.3	9.9	17.1	15.6	3.6	3.2	11.5	10.8	1.7	1.7
Huber + Suhner AG	HUBN SW	Switzerland	(6.6)	5.7	19.1	18.1	2.3	2.2	10.4	9.8	2.5	2.6
Topsec Technologies Group	002212 CH	China	211.2	33.5	14.5	10.8	1.0	0.9	12.4	9.2	0.7	1.0
Yangtze Optical Fibre & Cabl	601869 CH	China	35.5	16.4	21.0	18.0	1.9	1.8	11.7	10.2	1.4	1.6
Interlink Telecom PCL	ITEL TB	Thailand	(5.7)	16.6	23.7	20.4	2.1	2.1	12.6	10.8	2.0	2.4
Stark Corporation *	STARK TB	Thailand	22.0	17.2	17.5	15.0	7.3	5.8	12.6	10.7	2.8	3.3
Average			**40.6**	**16.0**	**18.2**	**15.8**	**2.8**	**2.5**	**11.4**	**9.9**	**1.9**	**2.1**

Sources: Bloomberg, * Thanachart estimates

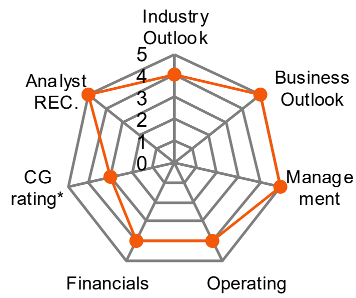
Based on 19 May 2022 closing prices

COMPANY DESCRIPTION

Stark Corporation Pcl (STARK) is a holding company with subsidiaries that are major wire and cable manufacturers with more than 50 years of industry experience in Thailand and Vietnam. Its total production capacity is the largest in ASEAN and it is ranked 14th globally. STARK also runs service businesses of providing manpower, logistics, and warehouse rentals to clients in the oil and gas industry.

Source: Thanachart

COMPANY RATING



Rating Scale	
Excellent	**5**
Good	**4**
Fair	**3**
Weak	**2**
Very Weak	**1**
None	**0**

Source: Thanachart; * CG Rating

THANACHART'S SWOT ANALYSIS

S — Strength

- Good reputation and track record in home-based markets
- Strong purchasing power with its suppliers and scale benefits over peers as it is now the largest cable producer in ASEAN

W — Weakness

- Relies on importing key raw materials, copper and aluminum, from abroad
- Relies on government spending on national infrastructure projects to grow sales

O — Opportunity

- Opportunities to export more products, and leverage on scale advantages, low labor wages, and tax privileges with various developing countries
- Potential to acquire more related businesses to strengthen its competitiveness and increase market share

T — Threat

- Cable manufacturing is a mature technology, so it is not difficult for new players with substantial capital to penetrate the market
- Changes to tax incentives and regulations to take part in biddings for infrastructure projects in each country

CONSENSUS COMPARISON

	Consensus	Thanachart	Diff
Target price (Bt)	6.45	6.50	1%
Net profit 22F (Bt m)	3,264	3,908	20%
Net profit 23F (Bt m)	4,304	4,582	6%
Consensus REC	**BUY: 2**	**HOLD: 0**	**SELL: 0**

HOW ARE WE DIFFERENT FROM THE STREET?

- Our 2022F earnings estimate is 20% higher than the Bloomberg consensus' number, likely since we are more bullish on STARK's margin improvement this year.
- Having said that, our TP is in line with the Street's.

Sources: Bloomberg consensus, Thanachart estimates

RISKS TO OUR INVESTMENT CASE

- Slower-than-expected pace of infrastructure progress in Thailand and Vietnam, either from changes in government policy or delays to construction, would represent the key downside risk to our earnings forecasts.
- A slower-than-expected pace of its capacity expansion plan and ability to build new power plants in those countries represents a secondary downside risk to our numbers.
- Lower-than-expected demand for high-end products would represent another downside risk to its margins, and therefore our earnings projections.

Source: Thanachart

Strong sales growth driven by power cable demand in TH and VN

INCOME STATEMENT

FY ending Dec (Bt m)	2020A	2021A	2022F	2023F	2024F
Sales	16,858	27,094	30,861	34,395	37,750
Cost of sales	13,809	21,134	23,716	26,084	28,302
Gross profit	**3,049**	**5,959**	**7,145**	**8,311**	**9,448**
% gross margin	18.1%	22.0%	23.2%	24.2%	25.0%
Selling & administration expenses	854	1,097	1,279	1,440	1,575
Operating profit	**2,195**	**4,862**	**5,867**	**6,871**	**7,873**
% operating margin	13.0%	17.9%	19.0%	20.0%	20.9%
Depreciation & amortization	363	430	489	567	636
EBITDA	**2,558**	**5,293**	**6,355**	**7,438**	**8,508**
% EBITDA margin	15.2%	19.5%	20.6%	21.6%	22.5%
Non-operating income	60	36	34	33	35
Non-operating expenses	0	0	0	0	0
Interest expense	(660)	(943)	(999)	(1,010)	(795)
Pre-tax profit	**1,595**	**3,955**	**4,902**	**5,894**	**7,112**
Income tax	403	741	980	1,297	1,707
After-tax profit	**1,192**	**3,215**	**3,922**	**4,597**	**5,405**
% net margin	7.1%	11.9%	12.7%	13.4%	14.3%
Shares in affiliates' Earnings	1	(0)	0	0	0
Minority interests	(10)	(12)	(14)	(15)	(17)
Extraordinary items	338	(420)	0	0	0
NET PROFIT	**1,521**	**2,783**	**3,908**	**4,582**	**5,389**
Normalized profit	**1,183**	**3,203**	**3,908**	**4,582**	**5,389**
EPS (Bt)	0.1	0.2	0.2	0.3	0.3
Normalized EPS (Bt)	0.1	0.2	0.2	0.3	0.3

STARK is repaying debts used for business acquisition in 2020

BALANCE SHEET

FY ending Dec (Bt m)	2020A	2021A	2022F	2023F	2024F
ASSETS:					
Current assets:	16,331	27,962	30,194	33,366	36,362
Cash & cash equivalent	1,214	1,029	1,000	1,000	1,000
Account receivables	6,042	15,571	16,910	18,847	20,685
Inventories	8,618	10,487	11,695	12,864	13,957
Others	457	875	589	656	720
Investments & loans	344	329	329	329	329
Net fixed assets	4,417	4,413	5,969	7,249	8,163
Other assets	6,266	6,438	5,411	4,941	4,468
Total assets	**27,358**	**39,142**	**41,903**	**45,886**	**49,322**
LIABILITIES:					
Current liabilities:	19,649	23,548	24,962	26,135	25,373
Account payables	10,248	17,093	17,543	19,295	20,936
Bank overdraft & ST loans	7,761	4,030	3,747	3,031	1,712
Current LT debt	1,057	1,711	2,623	2,728	1,541
Others current liabilities	583	714	1,049	1,081	1,184
Total LT debt	**3,310**	**8,347**	**6,120**	**6,365**	**3,596**
Others LT liabilities	723	655	1,285	1,376	1,461
Total liabilities	**23,682**	**32,551**	**32,367**	**33,875**	**30,430**
Minority interest	55	87	100	116	133
Preferreds shares	0	0	0	0	0
Paid-up capital	11,906	11,906	11,906	11,906	15,875
Share premium	(10,542)	(10,542)	(10,542)	(10,542)	(10,542)
Warrants	0	0	0	0	0
Surplus	(591)	(493)	(493)	(493)	(493)
Retained earnings	**2,847**	**5,633**	**8,564**	**11,024**	**13,920**
Shareholders' equity	3,621	6,505	9,436	11,895	18,760
Liabilities & equity	**27,358**	**39,142**	**41,903**	**45,886**	**49,322**

Sources: Company data, Thanachart estimates

CASH FLOW STATEMENT

Strong cash flow generation with low capex requirements

FY ending Dec (Bt m)	2020A	2021A	2022F	2023F	2024F
Earnings before tax	1,595	3,955	4,902	5,894	7,112
Tax paid	(190)	(1,020)	(725)	(1,410)	(1,615)
Depreciation & amortization	363	430	489	567	636
Chg In working capital	(2,064)	(4,553)	(2,097)	(1,353)	(1,291)
Chg In other CA & CL / minorities	74	168	8	78	(52)
Cash flow from operations	**(222)**	**(1,020)**	**2,576**	**3,776**	**4,790**
Capex	(2,126)	(381)	(2,000)	(1,800)	(1,500)
Right of use	(789)	(31)	(50)	(50)	(50)
ST loans & investments	(179)	(149)	358	0	0
LT loans & investments	(44)	15	0	0	0
Adj for asset revaluation	0	0	0	0	0
Chg In other assets & liabilities	(4,202)	(114)	1,662	563	559
Cash flow from investments	**(7,339)**	**(659)**	**(30)**	**(1,287)**	**(991)**
Debt financing	7,512	1,393	(1,599)	(367)	(5,274)
Capital increase	(432)	0	(0)	0	3,969
Dividends paid	0	0	(977)	(2,122)	(2,493)
Warrants & other surplus	264	101	0	0	0
Cash flow from financing	**7,344**	**1,494**	**(2,576)**	**(2,490)**	**(3,798)**
Free cash flow	**(2,348)**	**(1,400)**	**576**	**1,976**	**3,290**

VALUATION

Multiples look attractive to us given its robust growth outlook

FY ending Dec	2020A	2021A	2022F	2023F	2024F
Normalized PE (x)	58.0	21.4	17.5	15.0	12.7
Normalized PE - at target price (x)	87.2	32.2	26.4	22.5	19.1
PE (x)	45.1	24.6	17.5	15.0	12.7
PE - at target price (x)	67.9	37.1	26.4	22.5	19.1
EV/EBITDA (x)	31.1	15.4	12.6	10.7	8.7
EV/EBITDA - at target price (x)	44.6	22.0	18.0	15.4	12.8
P/BV (x)	18.9	10.5	7.3	5.8	3.7
P/BV - at target price (x)	28.5	15.9	10.9	8.7	5.5
P/CFO (x)	(308.9)	(67.3)	26.6	18.2	14.3
Price/sales (x)	3.1	1.9	1.7	1.5	1.4
Dividend yield (%)	0.0	0.0	2.8	3.3	3.9
FCF Yield (%)	(3.4)	(2.0)	0.8	2.9	4.8
(Bt)					
Normalized EPS	0.1	0.2	0.2	0.3	0.3
EPS	0.1	0.2	0.2	0.3	0.3
DPS	0.0	0.0	0.1	0.1	0.2
BV/share	0.2	0.4	0.6	0.7	1.2
CFO/share	(0.0)	(0.1)	0.2	0.2	0.3
FCF/share	(0.1)	(0.1)	0.0	0.1	0.2

Sources: Company data, Thanachart estimates

Sustainable 35% ROE from 2024F is impressive for a manufacturing firm

FINANCIAL RATIOS

FY ending Dec	2020A	2021A	2022F	2023F	2024F
Growth Rate					
Sales (%)	46.2	60.7	13.9	11.5	9.8
Net profit (%)	1,127.2	83.0	40.4	17.2	17.6
EPS (%)	1,127.2	83.0	40.4	17.2	17.6
Normalized profit (%)	687.6	170.7	22.0	17.2	17.6
Normalized EPS (%)	687.6	170.7	22.0	17.2	17.6
Dividend payout ratio (%)	0.0	0.0	50.0	50.0	50.0
Operating performance					
Gross margin (%)	18.1	22.0	23.2	24.2	25.0
Operating margin (%)	13.0	17.9	19.0	20.0	20.9
EBITDA margin (%)	15.2	19.5	20.6	21.6	22.5
Net margin (%)	7.1	11.9	12.7	13.4	14.3
D/E (incl. minor) (x)	3.3	2.1	1.3	1.0	0.4
Net D/E (incl. minor) (x)	3.0	2.0	1.2	0.9	0.3
Interest coverage - EBIT (x)	3.3	5.2	5.9	6.8	9.9
Interest coverage - EBITDA (x)	3.9	5.6	6.4	7.4	10.7
ROA - using norm profit (%)	5.9	9.6	9.6	10.4	11.3
ROE - using norm profit (%)	40.2	63.3	49.0	43.0	35.2
DuPont					
ROE - using after tax profit (%)	40.5	63.5	49.2	43.1	35.3
- asset turnover (x)	0.8	0.8	0.8	0.8	0.8
- operating margin (%)	13.4	18.1	19.1	20.1	20.9
- leverage (x)	6.8	6.6	5.1	4.1	3.1
- interest burden (%)	70.7	80.7	83.1	85.4	89.9
- tax burden (%)	74.7	81.3	80.0	78.0	76.0
WACC (%)	7.6	7.6	7.6	7.6	7.6
ROIC (%)	28.3	27.2	24.0	25.6	26.0
NOPAT (Bt m)	1,640	3,952	4,693	5,359	5,983
invested capital (Bt m)	14,534	19,564	20,926	23,018	24,608

Sources: Company data, Thanachart estimates

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For sectors, an “Overweight” sector weighting is used when we have BUYs on majority of the stocks under our coverage by market cap. “Underweight” is used when we have SELLs on majority of the stocks we cover by market cap. “Neutral” is used when there are relatively equal weightings of BUYs and SELLs.

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