

08 March 2017 | Sector Update

Technology Sector

Upgrade to POSITIVE
(previously Neutral)

Higher sales growth in 2017

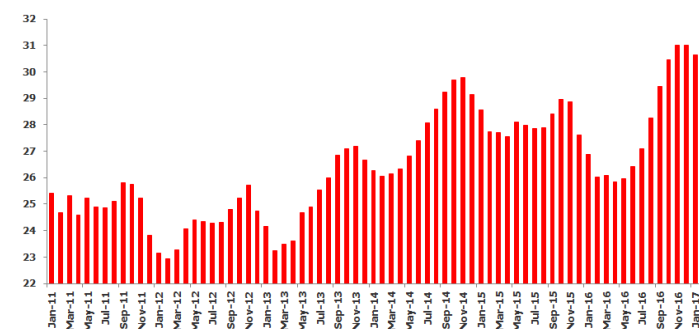
- January 2017 sales surged by +13.9%yoy, underpinned by strong demand from China
- Double digit sales growth was seen across all regions, with the exception of Europe
- WSTS revised upwards 2017 sales forecasts after factoring better-than-expected 4Q16 sales
- Upgrade to POSITIVE from Neutral previously

A. STATE OF GLOBAL SEMICONDUCTOR INDUSTRY

i. Global Semiconductor Sales (January 2017)

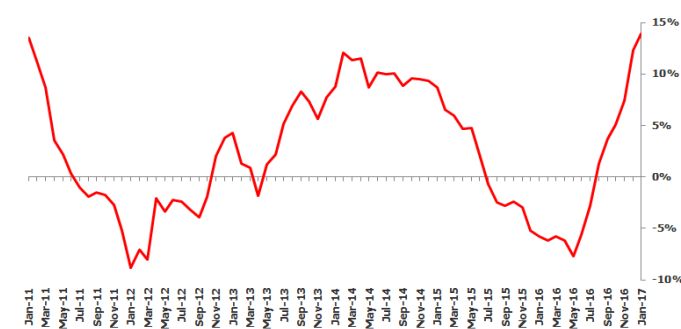
Double digit growth. January 2017 worldwide sales of semiconductors surged by +13.9%yoy to USD30.6b. This marks the highest-ever January sales and largest year-over-year growth in more than six years since November 2010. Inclusive of this, GSS has been growing on a year-over-year basis for the past six consecutive months since August 2016. The improvement in sales was mainly supported by the China market which grew by +20.5%yoy. Meanwhile, the other regions, with the exception of Europe, also posted double digit growth. To recall, January 2016 sales was also impacted by the elevated inventory level which further reduced the demand of semiconductor products. Nonetheless, the January 2017 sales represents a -1.2%mom decline as compared to December 2016 sales of USD31.0b, owing to normal seasonal trends.

Chart 1: Monthly global semiconductor sales (USD billion)



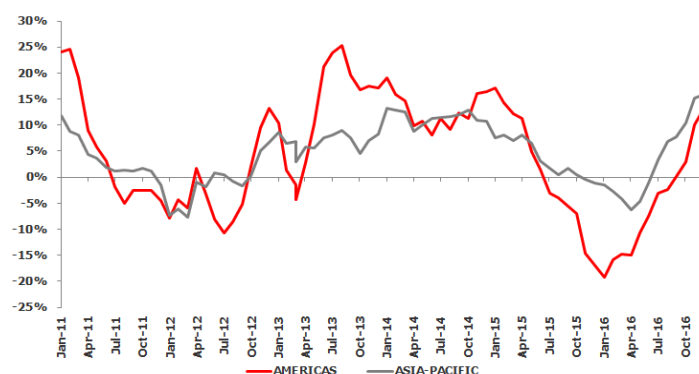
Sources: SIA, MIDFR

Chart 2: Monthly Global semiconductor sales (%yoy)



Sources: SIA, MIDFR

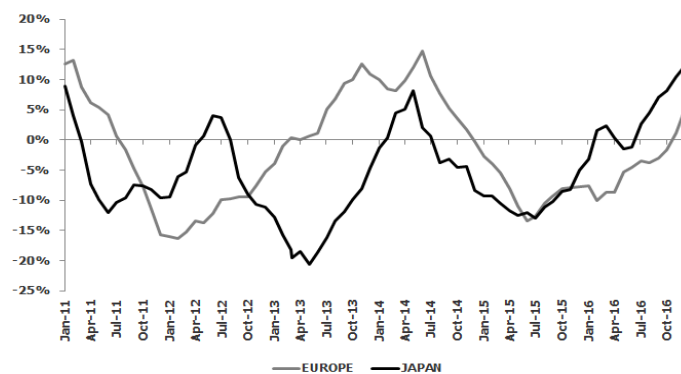
Chart 3: Americas and Asia Pacific* sales (%yoy)



Sources: SIA, MIDFR

*Includes China

Chart 4: Europe and Japan sales (%yoy)



Sources: SIA, MIDFR

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Kindly refer to the last page of this publication for important disclosures

China is the largest contributor. Higher semiconductor sales were seen across all regions. China spearheaded the sales growth at +20.5%yoy. As a result, the China market currently made up approximately one-third of global sales. Meanwhile, sales from the Americas, Japan and Asia Pacific regions also grew in the tune of +11%yoy to +14%yoy. Europe posted the slowest sales growth rate at +4.8%yoy.

ii. World Semiconductor Trade Statistics (WSTS) - Revised sales forecasts for 2017 and 2018

Upward revisions in WSTS' latest sales forecasts. To recall, 2016 annual sales increased by +1.1%yoy to USD338.9b which surpassed WSTS' expectation. Premised on the actual sales figures for 4Q16, WSTS has revised upwards 2017 sales forecasts by +USD14.8b to USD360.9b (+6.5%yoy) from USD346.1b previously. The largest sales growth is expected to stem from sensors, analog and memory, while all other products are expected to contribute positive growth. Nonetheless, 2018 sales growth projection has been maintained at +2.3%yoy.

Table 1: WSTS forecasts summary

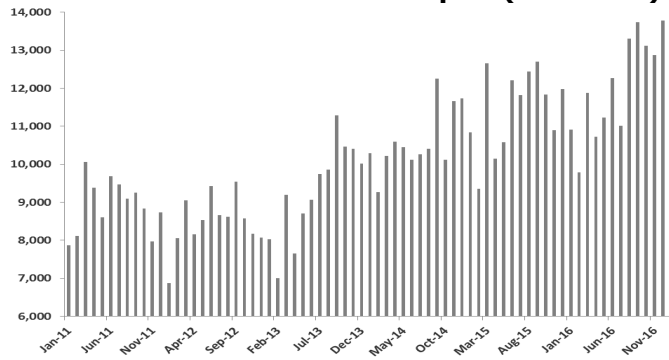
Fall 2016	Amounts (USD billion)				Year on year growth (%)			
	2015	2016	2017F	2018F	2015	2016F	2017F	2018F
By Region								
Americas	68.738	65.537	72.173	74.102	-0.8	-4.7	1.0	2.7
Europe	34.258	32.707	3.892	34.636	-8.6	-4.5	3.6	2.2
Japan	31.102	32.292	33.608	34.200	-10.7	3.8	4.1	1.8
Asia Pacific	201.070	208.395	221.230	226.113	3.5	3.6	6.2	2.2
Total World	335.168	338.931	360.903	369.050	-0.2	1.1	6.5	2.3
By Products								
Discrete Semiconductors	18.612	19.418	20.023	20.674	-7.7	4.3	3.1	3.2
Optoelectronics	33.256	31.994	32.679	32.241	11.3	-3.8	2.1	-1.3
Sensors	8.816	10.821	11.797	12.394	3.7	22.7	9.0	5.1
Integrated Circuits	274.484	276.698	296.404	303.741	-1.0	0.8	7.1	2.5
<i>Analog</i>	45.228	47.848	51.570	53.315	1.9	5.8	7.8	3.4
<i>Micro</i>	61.298	60.585	61.106	62.281	-1.2	-1.2	0.9	1.9
<i>Logic</i>	90.753	91.498	97.154	98.975	-1.0	0.8	6.2	1.9
<i>Memory</i>	77.205	76.767	86.574	89.170	-2.6	-0.6	12.8	3
Total Products	335.168	338.931	360.903	369.050	-0.2	1.1	6.5	2.3

Source: WSTS, MIDF

B. MALAYSIA SEMICONDUCTOR EXPORT (January 2017)

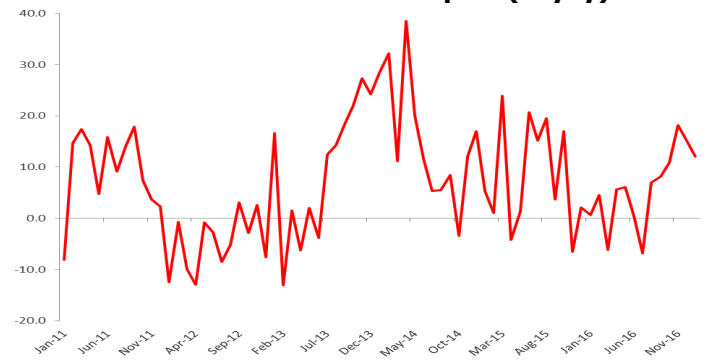
In-tandem with global demand. Malaysia's export of semiconductor products for the month of January 2017 improved by +12.0%yoy to RM12.2b. Inclusive of this, the demand for local semiconductor products has been growing on a year-over-year basis for the sixth consecutive months since August 2016. This is in-line with the global market demand. Moving forward, we expect the demand of local semiconductor products to remain in the positive territory. This would be mainly supported by stronger demand from China.

Chart 6: Local semiconductor export (RM billion)



Sources: DoS, MIDFR

Chart 7: Local semiconductor export (%yoy)

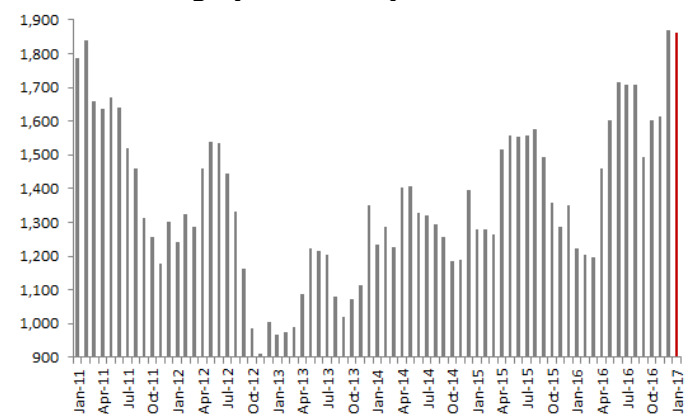


Sources: DoS, MIDFR

C. INDUSTRY UPDATE

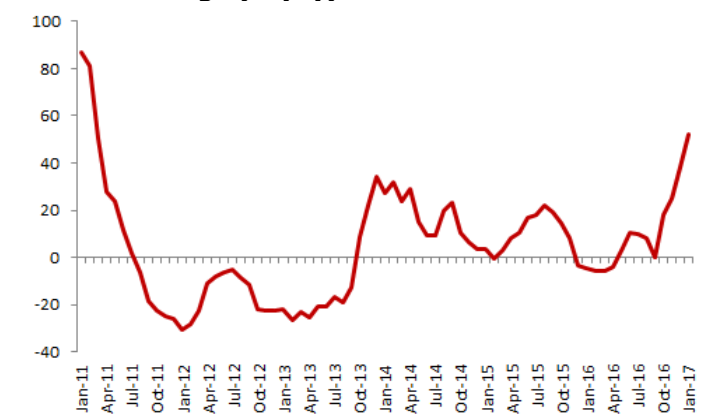
Capital spending. The North America-based manufacturers of semiconductor equipment posted January 2017 billings of USD1.86b. This represents an increase of +52.3%yoy as compared to January 2016 billings of USD1.22b. On a sequential basis, the billings dropped marginally by -0.5%yoy from USD1.87b. The Semiconductor Equipment and Materials International (SEMI) expect "strong spending growth in 2017 based on investments in leading-edge memory and foundry fabs."

Chart 8: Billings (USD billion)



Sources: SEMI, MIDFR

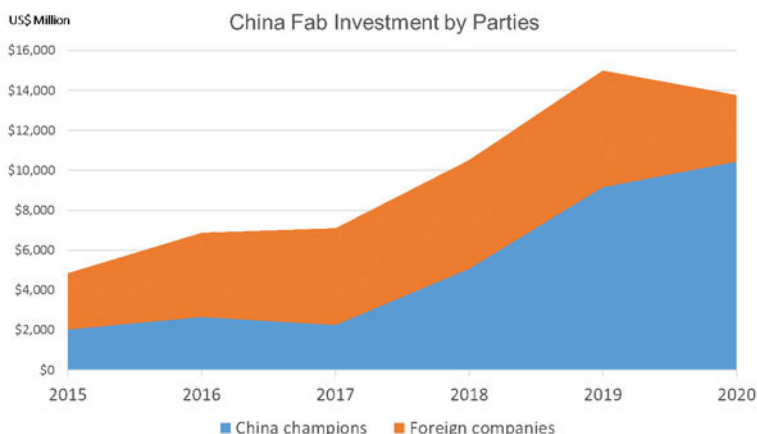
Chart 9: Billings (%yoy)



Sources: SEMI, MIDFR

Fab equipment. China will remain as one of the main spending region for fab equipment with more than 20 upcoming new fab projects. This will raise its fab equipment spending to more than USD10b annually by 2018. Given this trend, SEMI projected China to be the top spending region for fab equipment by 2019. Such quantum of investment will lift China to become a first-tier player in the semiconductors industry.

Chart 10: Fab investment




Source: SEMI

Note that SEMI has ceased publishing the monthly North America Book-to-Bill (BTB) report this year. This is mainly due to changes in reporting by some participants where the reporting of orders/bookings into the data collection program is no longer a necessary component of their industry analysis. As such, we will no longer feature the BTB ratio from our monthly sector update report.

Nokia launches three new smartphones. The three new budget models include Nokia 3, Nokia 6 and Nokia 5. In addition, the phone maker also re-introduced an upgraded version of Nokia 3310. The latter will focus primarily on emerging markets such as India and Africa. Nokia's re-entry is expected to further excite the smartphone market which could lead to potentially higher shipping volumes. This, in turn, will bode well for semiconductor companies who manage to position themselves within Nokia's product value chain.

Upgrade to POSITIVE. In recent years, the China government has been supporting the Chinese domestic semiconductor industry with tremendous capital budgets. This has led to China gradually playing a pivotal role in upholding the demand of semiconductor products. At present, sales from China has accounted for one-third of global sales. It is also the main export destination of local semiconductor products. Moving forward, we expect the sales growth momentum emanating from China to remain robust in the foreseeable term. This is in-tandem with the anticipated heavy investment in fab equipment in the upcoming years. In the immediate term, we expect the global semiconductor sales to continue to record positive sales growth on a year-over-year basis. This was partly due to lower demand seen in early 2016 as a results of inventory burn-off.

Apart from the smart devices segment, we also expect healthier demand from the automotive and storage markets. The automotive market will driven by the continuous effort to increase the average semiconductor content per vehicle. Demand from this market is also less susceptible to seasonality factors, thus providing a steadier stream of revenue. Meanwhile, higher demand for the storage market would be supported by the cloud computing and data centre industries.

All factors considered, we upgrade our Technology sector call to **POSITIVE** from Neutral stance previously. Our top pick for the sector is Inari Amertron Bhd (TP: RM2.23) due to its strategic positioning within the semiconductor product value chain. 

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STOCK RECOMMENDATIONS

BUY	Total return is expected to be >15% over the next 12 months.
TRADING BUY	Stock price is expected to <i>rise</i> by >15% within 3-months after a Trading Buy rating has been assigned due to positive newsflow.
NEUTRAL	Total return is expected to be between -15% and +15% over the next 12 months.
SELL	Total return is expected to be <-15% over the next 12 months.
TRADING SELL	Stock price is expected to <i>fall</i> by >15% within 3-months after a Trading Sell rating has been assigned due to negative newsflow.

SECTOR RECOMMENDATIONS

POSITIVE	The sector is expected to outperform the overall market over the next 12 months.
NEUTRAL	The sector is to perform in line with the overall market over the next 12 months.
NEGATIVE	The sector is expected to underperform the overall market over the next 12 months.