

Response to Questions on Cheung Woh Technologies Ltd's Annual Report Posed by SIAS

1. The group reported a loss of \$(8.9) million for the financial year ended 28 February 2019. Although this was an improvement from a loss of \$(16.8) million in the previous financial year, shareholders' funds have decreased to just \$80.9 million. The following financial highlights are extracted from page 13 of the annual report for reference:



(Source: Adapted from company annual report)

Would the board/management provide shareholders with better clarity on the following operational/financial matters? Specifically:

(i) **Forged helium-filled hard-disk drive Baseplates:** In the chairman's statement, it was disclosed that the group's customer will switch to an alternative manufacturing method for their baseplates. The group will be supplying its baseplates until September 2019. With the completion of the current orders, the group expects its forged helium-filled hard-disk base Baseplates production to cease/substantially reduced. In the past two financial years, the group has recognised more than \$11.5 million in impairment of its property, plant and equipment (PPE) and a further \$1.4 million on capitalised expenses and patents related to the Baseplates.

(a) Can management help shareholders understand the total investments made to fund the group's venture into forged helium-filled hard-disk drive Baseplates?

Response:

The total investments made for forged helium-filled hard-disk drive Baseplates are:

	S\$ (million)
Plant and machineries	35.5
Buildings	5.5
Total	41.0

(b) Following the cessation of orders from the group's customer, what are the prospects of the group's forged helium-filled hard-disk drive Baseplates segment? Would there be further impairment of its PPE and/or retrenchment/restructuring costs in the future?

Response:

The Group will discontinue its manufacturing of Baseplates after completion of orders in September 2019. Currently the net book value of PPE related to production of Baseplates have been written down to fair value (based on the valuation reports). Any further impairment is dependent on the conditions and fair value at the time of assessment in the future. No major retrenchment will be

required as headcount will be reduced over time due to natural attrition. Upon cessation of Baseplates manufacturing, the remaining manpower will be transferred to other departments for existing and new products. We do not foresee there will be any major restructuring costs.

(c) Would management help shareholders understand the revenue derived from other HDD components (less revenue from helium-filled Baseplates)?

Response:

Revenue breakdown in HDD components segment:

FY2019	S\$ ('000)
Voice coil motor (VCM) plates	13,047
Air comb	27,538
Baseplates	24,119
High mix low volume (HMLV)	113
Total	64,817

(d) Would the board consider ceasing major investments into the HDD segment?

Response:

Yes. The Group has already ceased major CAPEX into the HDD components segment.

(e) What will be the utilisation rate of the group's manufacturing facilities after September 2019 when the orders are completed?

Response:

As customers do not give us order forecast beyond 6 months, we will not be able to accurately forecast the utilisation rate after September 2019.

(ii) **Precision metal stamping (PMS) segment:** Segment revenue decreased from \$15.7 million in FY2018 to \$12.0 million in FY2019, a drop of 24%. This despite the group trying to diversify away from the HDD business. The chairman has disclosed that the group has new projects in various stages of progress, from sample submission to mass production.

Can management elaborate further on the major opportunities in the next 12-24 months? What is the group's strategy to acquire new customers/projects? What is management's projected profit margin when bidding for these new projects?

Response:

In the next 12-24 months, the Group will continue with the existing business such as manufacture of PMS components, VCM plates, air-combs and HMLV products by utilising the existing manufacturing facilities. The Group will also diversify into various industries which have prospect of success and are profitable by leveraging on the Group's core competency.

For the HMLV products, the Group has ventured into the supply of seat actuation controller used in aerospace industry, industrial and commercial laser components and mechanical components used in autonomous vehicles. The progress of these new products ranges from sample submissions to mass productions.

For high volume products, the Group will continue to engage existing partners to leverage on our capabilities and actively explore new business opportunities with an open mind. The Group has secured samples orders to supply Continuous Variable Transmission (CVT) friction disk. The Group is in the enquiry stage for components used in 3C markets.

The Group will not be disclosing the profit margin included in new product bids.

(iii) Aerospace: Would management help shareholders understand the opportunities available to the group in the aerospace industry? Given that the aerospace segment is also highly competitive, how does the group ensure that it can be competitive/profitable as it ventures into this new segment?

Response:

The current opportunity to the aerospace industry is from an aerospace contract manufacturer with a strategic partnership agreement. The parts supplied by the Group are low volume in nature and therefore does not face much competition.

(iv) High mix low volume business: Given that the group's core competency was in high volume (low mix) production, what changes have been made to the group's operations and culture to carry out the new high mix low volume business successfully?

Response:

The Group makes use of the existing manufacturing system which also requires high standard of quality. However, we have reorganised work processes to adapt to the HMLV business segment. The Group is not new to this business as Penang plant has a mature operation in this segment.

Q2. As disclosed in Note 5 (page 69 - Investment properties), the group's investment properties have a fair value of \$7.06 million as at 28 February 2019. The two properties in Tuas are carried at a book value of \$2.46 million.

(i) Can the company let shareholders know if the two investment properties are fully leased out?

Response:

The two investment properties are leased out to their maximum allowable tenable area in accordance to regulations of JTC.

In addition, the group has 2 manufacturing sites in Penang, 2 manufacturing sites in Senai, Johor, Malaysia and a large manufacturing site in Zhuhai, China. The details of the major properties can be found on the inner back cover of the annual report.

(ii) Has the rising trade tension between USA and China affected the group's operation in Zhuhai, China?

Response:

There is no impact to our HDD business as we are not selling directly to USA customers. However, for HMLV products that are directly supplied to USA customers, we have been specifically instructed that manufacturing is to be done in our Malaysia plants.

(iii) Given the scaling down of the forged helium-filled hard-disk drive Baseplates segment, are there opportunities for the group to further streamline its operations?

Response:

We have already streamlined our operations.

(iv) Given the trends of the group's HDD business, has the board considered if it would be opportune to scale back its manufacturing operations and to right-size the manufacturing capacity?

Response:

Yes, we have scaled-back and reallocated manufacturing capacity to other products and have right-size the operation to meet the current demand.

At the group level, the carrying value of leasehold land and buildings is \$21.45 million as at 28 February 2019. This is based on the group's accounting policy of measuring property, plant and equipment at cost less accumulated depreciation (and any accumulated impairment losses).

(v) Has the board carried out a valuation of the leasehold properties in the group? What is the fair value of the properties recognised as leasehold land and buildings (under property, plant and equipment)?

Response:

The Group has carried out valuation for the leasehold properties located in Singapore for the purpose of determining disposal price.

Based on the valuation report dated 28 February 2019, the market value for the two leasehold properties are as follow:

Property	Market value
23 Tuas South Street 1, Singapore 638033	S\$8 million
17 Tuas South Street 1, Singapore 638065	S\$3.3 million

(vi) Given the group's long term growth prospects, are there opportunities to monetise some of these properties recognised as PPE?

Response:

The Group will consider to dispose its property at Tuas when the price is right.

Q3. At the annual general meeting scheduled to be held on 24 June 2019, the company is proposing to re-elect Dr. Chen Yuk Fu who is retiring in accordance with Article 107 of the Company's Constitution.

Dr. Chen was first appointed to the board on 15 September 2000. As such, Dr. Chen has served as a director on the board for more than 18 years.

In addition, Mr Lim Kian Wee, an independent director on the board, was first appointed on 30 September 2005 and has served for more than 13 years.

In the Corporate Governance report, the company has disclosed that, following a rigorous review of the independence of the long tenured directors, the board has confirmed that the two long tenured independent directors are independent. It further stated that "*the board agreed there is **no need for progressive refreshing***" (page 17) [emphasis added].

In August 2018, the Monetary Authority of Singapore issued a revised Code of Corporate Governance ("2018 CG Code"). As a consequence of the revised 2018 CG Code, the Singapore Exchange has made amendments to its Listing Rules which came into effect on 1 January 2019, except for the rules on the 9-year tenure for independent directors and the requirement for independent directors to comprise one-third of the board which come into effect on 1 January 2022. Under the revised Listing Rules, the term of an independent director will be limited to nine years after which the long tenured directors will be subject to a two-tier vote by shareholders.

(i) Has the company evaluated the impact of the 2018 CG Code and the amendments to the Listing Rules on the board?

Response:

The Board is aware of the 2018 CG Code and amendment to the Listing Rules and has evaluated its impact.

(ii) Can the nominating committee (NC) elaborate further on the succession plans for the board and other key management positions?

Response:

The NC has considered succession plans for the Board and key management positions and was updated on the progress of succession planning. Succession planning involves a process for identifying, nurturing and developing management staffs and external talents to fill each key role within the Company. This is to ensure that the best mix of executive officers are lined up to meet the Company's strategic goals and challenges for building long-term shareholder value.

The NC has regular discussions on succession planning and review the structure, size and composition of the Board. Where new appointments are required, the NC will consider recommendations for new directors, review their qualifications and meet with such candidates before a decision is made.

(iii) Has the nominating committee reviewed the overall desired competency matrix of the board and identified any gaps in skills or competencies that could be addressed in future director appointments? This is especially important as the group diversifies itself away from the HDD industry.

Response:

The NC reviews the structure, size and composition of the Board annually and identifies any gap in the skills and competencies of the Directors. The NC, taking into account the scope and nature of the operations of the Company, is satisfied that the current size of the Board, the standing of the members of the Board in the business community, and their combined experience, knowledge and expertise in areas such as legal, business and finance provide for effective decision making and direction to the Company. There is an appropriate balance and diversity of skills, experience, gender and knowledge of the Company. The core competencies in areas such as legal business and management experience, industry knowledge and strategic planning experience is beneficial to the Company and Management as decision by the Board will be enriched by a broad range of views and perspective and experience of Directors.

With the review of the Company's current and future strategic and operational plans, the NC has considered the current core competencies of the Board in areas such as legal, business and finance remains relevant for future Board appointments.

(iv) In view of the impending cessation of the forged helium-filled hard-disk drive baseplates business and with the group's effort to go into high mix low volume machining business, would the board be evaluating the benefits of progressive refreshing of the board? As noted above, the board has stated that it "*agreed there is no need for progressive refreshing*" (page 17) [emphasis added].

Response:

For FY2019, the Board has considered familiarity of Directors with the business will continue to contribute positively to the deliberation at the Board and Board Committees and brings valuable insight, knowledge and expertise to the Board. Hence, the Board agreed there is no need for progressive refreshing.

Annually, the NC considers the need for progressive refreshing to ensure the best mix of skills to meet the Company's strategic goals and challenges for building long-term shareholder value.

(v) What are the company's near term plans to refresh the membership of the board to comply with the new 2018 Code in good time? Reconstituting the board early to comply with the new 2018 Code would avoid undue disruption and help to maintain institutional knowledge and continuity in the board.

Response:

The NC reviews the structure, size and composition of the Board annually and identifies any gap in the skills and competencies of the Directors. The NC will consider recommendations for new directors, review their qualifications such as track record, age, experience, and capabilities and meet with such candidates before a decision is made.