

# Thong Guan (TGI MK)

Consumer Non-cyclical – Packaging

Market Cap: USD68.5m

**Neutral** (from Buy)

Target Price: MYR2.57

Price: MYR2.78

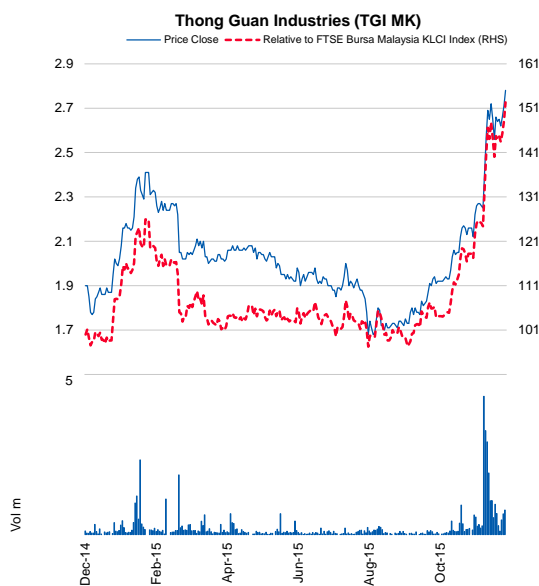
## All In The Price For Now

Macro

Risks

Growth

Value



Source: Bloomberg

Avg Turnover (MYR/USD)	0.90m/0.21m
Cons. Upside (%)	-9.7
Upside (%)	-7.6
52-wk Price low/high (MYR)	1.68 - 2.78
Free float (%)	39
Share outstanding (m)	105
<b>Shareholders (%)</b>	
Foremost Equals SB	39.8

### Share Performance (%)

	YTD	1m	3m	6m	12m
Absolute	48.7	28.7	59.8	44.8	44.8
Relative	54.5	30.3	56.3	48.8	49.3

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We downgrade Thong Guan to **NEUTRAL** as there is now an **8% downside** to our MYR2.57 TP. We recently met with management to find out more about its venture into the noodle manufacturing business and the ongoing expansion of its stretch film division, but make no changes to our forecasts, as we had previously factored these in.

- ◆ **Focuses on higher value-added stretch films.** Thong Guan Industries' (Thong Guan) anticipated 33-layer nano-technology stretch film line is to be commissioned in mid-December. It is slated for commercialisation in 1Q16. The multi-layer film is a new formulation arising from its research & development (R&D) efforts and should enable the company to command higher margins going forward. The extra line would increase monthly stretch film production by an estimated 15-20%.
- ◆ **A step further into food & beverage (F&B).** Thong Guan recently diversified into the noodle manufacturing business through the acquisition of a 60% stake in Everprosper Food Industries SB (EFI) in August via a wholly-owned subsidiary. EFI has a manufacturing plant at the Sepang Industrial Park that manufactures steamed noodles. The company is in the midst of setting up another manufacturing plant in Sungai Petani, Kedah, which is expected to be operational in 1Q16. It is to focus on manufacturing stick noodles. Management guided that an estimated 80% of the manufactured noodles are to be exported to various markets, including Australia, Singapore and Thailand. Thong Guan also recently tied up with a multinational food company and would serve as its sole noodle supplier in South-East Asia. In addition, the company is to start supplying noodles to a chain retailer in Australia in 2Q16. While Thong Guan expects revenue contribution from the noodles business to be <10% in FY16, it anticipates this division to grow further going forward. This is as it looks to penetrate into new markets such as Indonesia, Vietnam and China.
- ◆ **Downgrade to NEUTRAL with an unchanged MYR2.57 TP.** We make no changes to our earnings forecast and MYR2.57 TP, as we have previously factored in the capacity expansion and earnings contribution from its noodle business. However, we downgrade our call to NEUTRAL (from Buy) as there is now a potential 8% downside to our TP. Our corroborative DDM-valuation is also supportive of our TP. Risks to our forecast include: i) delays in its capacity expansion, ii) a spike in raw material costs, and iii) further weakness of the MYR against the USD.

Forecasts and Valuations	Dec-13	Dec-14	Dec-15F	Dec-16F	Dec-17F
Total turnover (MYRm)	720	733	960	1,128	1,271
Reported net profit (MYRm)	28.2	17.5	34.8	44.8	49.6
Recurring net profit (MYRm)	28.2	17.5	35.8	44.8	49.6
Recurring net profit growth (%)	3.5	(38.0)	104.8	25.1	10.7
Recurring EPS (MYR)	0.27	0.17	0.34	0.28	0.31
DPS (MYR)	0.08	0.07	0.12	0.12	0.10
Recurring P/E (x)	10.4	16.7	8.2	9.8	8.9
P/B (x)	1.01	0.86	0.80	0.99	0.92
P/CF (x)	14.9	na	3.8	12.7	9.9
Dividend Yield (%)	2.9	2.5	4.2	4.5	3.6
EV/EBITDA (x)	5.32	7.41	3.69	4.35	3.82
Return on average equity (%)	10.2	5.5	9.8	11.1	10.8
Net debt to equity (%)	net cash	net cash	net cash	net cash	net cash
Our vs consensus EPS (adjusted) (%)			9.8	1.3	3.0

Source: Company data, RHB

**Figure 1: Thong Guan's DDM valuation**

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Risk-free rate (%)	4.3
Beta	0.6
Equity Risk Premium (%)	6.7
CoE (%)	<b>8.0</b>
DPS (MYR)	0.11
g (%)	3.5
<b>TP (MYR)</b>	<b>2.58</b>

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Source: RHB

## Financial Exhibits

<b>Profit &amp; Loss (MYRm)</b>	<b>Dec-13</b>	<b>Dec-14</b>	<b>Dec-15F</b>	<b>Dec-16F</b>	<b>Dec-17F</b>
Total turnover	720	733	960	1,128	1,271
Cost of sales	(645)	(656)	(851)	(1,001)	(1,129)
<b>Gross profit</b>	<b>76</b>	<b>76</b>	<b>110</b>	<b>127</b>	<b>141</b>
Gen & admin expenses	(21)	(23)	(30)	(35)	(39)
Selling expenses	(23)	(25)	(30)	(36)	(40)
Other operating costs	1	(9)	(4)	1	2
<b>Operating profit</b>	<b>32</b>	<b>19</b>	<b>45</b>	<b>58</b>	<b>63</b>
Operating EBITDA	49	38	66	80	86
Depreciation of fixed assets	(17)	(18)	(21)	(23)	(23)
Amortisation of intangible assets	(0)	(0)	-	-	-
<b>Operating EBIT</b>	<b>32</b>	<b>19</b>	<b>45</b>	<b>58</b>	<b>63</b>
Interest income	1	1	1	1	2
Interest expense	(1)	(1)	(1)	(1)	(1)
<b>Pre-tax profit</b>	<b>32</b>	<b>19</b>	<b>45</b>	<b>58</b>	<b>64</b>
Taxation	(3)	(0)	(8)	(10)	(12)
Minority interests	(1)	(1)	(2)	(3)	(3)
<b>Profit after tax &amp; minorities</b>	<b>28</b>	<b>17</b>	<b>35</b>	<b>45</b>	<b>50</b>
<b>Reported net profit</b>	<b>28</b>	<b>17</b>	<b>35</b>	<b>45</b>	<b>50</b>
<b>Recurring net profit</b>	<b>28</b>	<b>17</b>	<b>36</b>	<b>45</b>	<b>50</b>

Source: Company data, RHB

<b>Cash flow (MYRm)</b>	<b>Dec-13</b>	<b>Dec-14</b>	<b>Dec-15F</b>	<b>Dec-16F</b>	<b>Dec-17F</b>
<b>Operating profit</b>	<b>32</b>	<b>19</b>	<b>45</b>	<b>58</b>	<b>63</b>
<b>Depreciation &amp; amortisation</b>	<b>17</b>	<b>19</b>	<b>21</b>	<b>23</b>	<b>23</b>
<b>Change in working capital</b>	<b>(26)</b>	<b>(68)</b>	<b>16</b>	<b>(34)</b>	<b>(29)</b>
Other operating cash flow	0	(0)	5	0	1
<b>Operating cash flow</b>	<b>24</b>	<b>(30)</b>	<b>87</b>	<b>47</b>	<b>58</b>
Interest received	(1)	(1)	(1)	(1)	(2)
Interest paid	1	1	(0)	(0)	(1)
Tax paid	(5)	(3)	(8)	(10)	(12)
<b>Cash flow from operations</b>	<b>20</b>	<b>(32)</b>	<b>77</b>	<b>35</b>	<b>44</b>
Capex	(15)	(29)	(30)	(30)	(10)
Other new investments	(13)	-	-	-	-
Other investing cash flow	1	60	3	4	4
<b>Cash flow from investing activities</b>	<b>(27)</b>	<b>31</b>	<b>(27)</b>	<b>(26)</b>	<b>(6)</b>
Dividends paid	(7)	(12)	(12)	(20)	(16)
Proceeds from issue of shares	-	-	-	53	-
Increase in debt	6	37	(40)	-	-
Other financing cash flow	(1)	(3)	0	0	1
<b>Cash flow from financing activities</b>	<b>(3)</b>	<b>22</b>	<b>(52)</b>	<b>33</b>	<b>(15)</b>
Cash at beginning of period	79	70	92	91	133
<b>Total cash generated</b>	<b>(10)</b>	<b>21</b>	<b>(2)</b>	<b>42</b>	<b>23</b>
Forex effects	2	1	-	-	-
<b>Implied cash at end of period</b>	<b>70</b>	<b>92</b>	<b>90</b>	<b>133</b>	<b>156</b>

Source: Company data, RHB

## Financial Exhibits

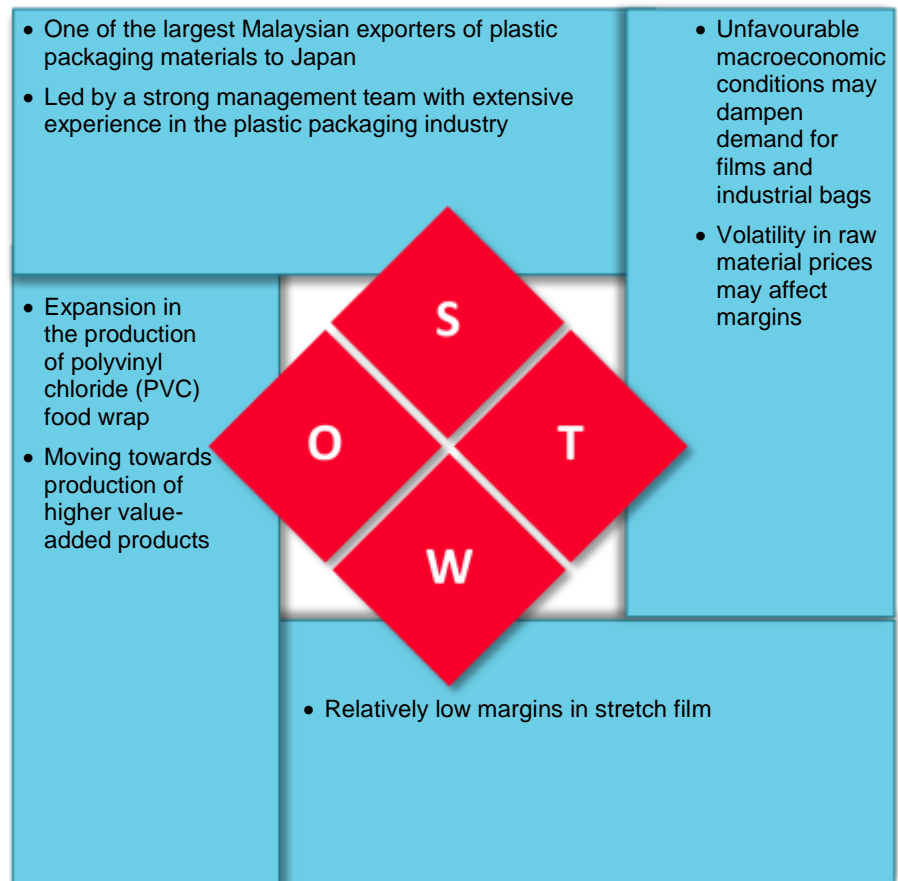
<b>Balance Sheet (MYRm)</b>	<b>Dec-13</b>	<b>Dec-14</b>	<b>Dec-15F</b>	<b>Dec-16F</b>	<b>Dec-17F</b>
Total cash and equivalents	70	92	91	133	156
Inventories	130	192	181	213	240
Accounts receivable	108	113	147	173	195
Other current assets	15	9	9	9	9
<b>Total current assets</b>	<b>324</b>	<b>406</b>	<b>429</b>	<b>528</b>	<b>601</b>
Total investments	12	12	12	12	12
Tangible fixed assets	112	124	130	135	120
Total non-current assets	124	136	143	148	132
<b>Total assets</b>	<b>448</b>	<b>542</b>	<b>571</b>	<b>676</b>	<b>733</b>
Short-term debt	42	74	40	40	40
Accounts payable	98	96	135	158	179
Other current liabilities	1	12	12	12	12
<b>Total current liabilities</b>	<b>141</b>	<b>182</b>	<b>186</b>	<b>210</b>	<b>230</b>
Total long-term debt	7	11	5	5	5
Other liabilities	6	1	7	7	7
<b>Total non-current liabilities</b>	<b>14</b>	<b>13</b>	<b>12</b>	<b>12</b>	<b>12</b>
<b>Total liabilities</b>	<b>154</b>	<b>194</b>	<b>198</b>	<b>222</b>	<b>242</b>
Share capital	105	105	105	158	158
Retained earnings reserve	167	173	197	222	255
Other reserves	17	64	64	64	64
<b>Shareholders' equity</b>	<b>290</b>	<b>342</b>	<b>366</b>	<b>443</b>	<b>477</b>
Minority interests	4	5	8	11	14
Other equity	0	(0)	(0)	0	-
<b>Total equity</b>	<b>293</b>	<b>347</b>	<b>374</b>	<b>454</b>	<b>491</b>
<b>Total liabilities &amp; equity</b>	<b>448</b>	<b>542</b>	<b>571</b>	<b>676</b>	<b>733</b>

Source: Company data, RHB

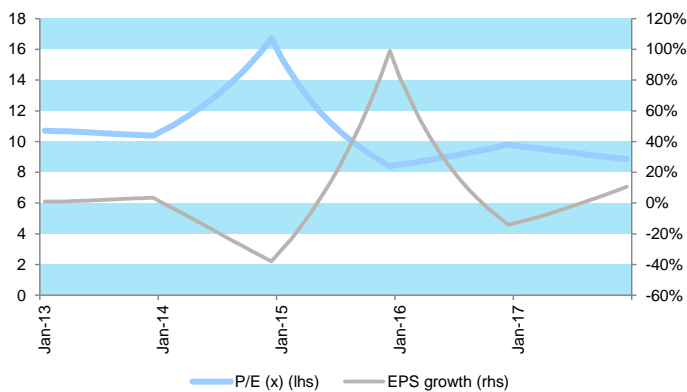
<b>Key Ratios (MYR)</b>	<b>Dec-13</b>	<b>Dec-14</b>	<b>Dec-15F</b>	<b>Dec-16F</b>	<b>Dec-17F</b>
Revenue growth (%)	14.1	1.7	31.1	17.5	12.6
Operating profit growth (%)	8.5	(39.6)	133.6	27.7	9.5
Net profit growth (%)	3.5	(38.0)	99.1	28.7	10.7
EPS growth (%)	3.5	(38.0)	99.1	(14.2)	10.7
BVPS growth (%)	10.6	18.1	6.9	(19.2)	7.6
Operating margin (%)	4.4	2.6	4.7	5.1	5.0
Net profit margin (%)	3.9	2.4	3.6	4.0	3.9
Return on average assets (%)	6.7	3.5	6.3	7.2	7.0
Return on average equity (%)	10.2	5.5	9.8	11.1	10.8
Net debt to equity (%)	(7.0)	(1.8)	(12.3)	(19.3)	(22.6)
DPS	0.08	0.07	0.12	0.12	0.10
Recurrent cash flow per share	0.19	(0.31)	0.73	0.22	0.28

Source: Company data, RHB

## SWOT Analysis

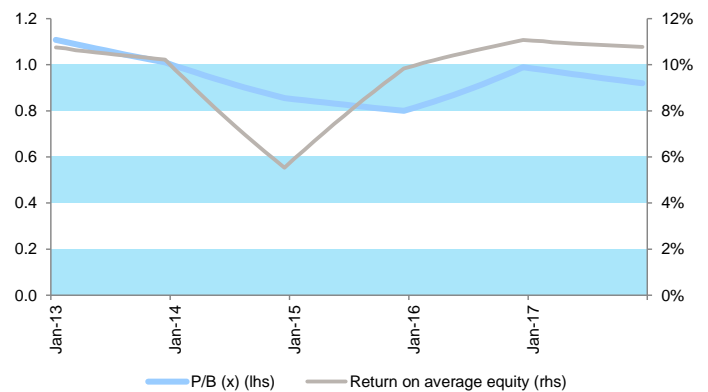


P/E (x) vs EPS growth



Source: Company data, RHB

P/BV (x) vs ROAE



Source: Company data, RHB

## Company Profile

Thong Guan Industries (Thong Guan) is principally involved in the manufacture of industrial packaging products, with manufacturing operations in Malaysia, China and Thailand. The group also involves in the manufacturing of food, beverages and other consumer products.

## Recommendation Chart



Source: RHB, Bloomberg

Date	Recommendation	Target Price	Price
2015-11-20	Buy	2.57	2.41
2015-08-20	Neutral	1.77	1.80
2015-05-28	Neutral	2.05	1.95
2015-03-02	Neutral	2.03	2.05
2014-11-21	Buy	2.60	2.09
2014-09-15	Buy	2.60	2.25
2014-08-28	Buy	3.60	2.86
2014-08-27	Buy	3.60	2.86

Source: RHB, Bloomberg

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**Trading Buy:** Share price may exceed 15% over the next 3 months, however longer-term outlook remains uncertain

**Neutral:** Share price may fall within the range of +/- 10% over the next 12 months

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- (a) -

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