

B | Stock Selections

Stocks selected under this section are meant for medium and/or long-term investments. When stocks are recommended under this section, it does not mean that its price will take 1 or 2 years to move. If the price moves too fast, *iCapital*® may recommend a sell. Or if it is still attractive after holding for a while and its price has gone up, we may still recommend holding or even buying more. Or if it declines, *iCapital*® quotes Warren Buffett who was supposed to have said this: "If you aren't prepared to see your stocks go down 50%, you shouldn't own them. Be prepared for declines – and arrange your financial affairs such that you won't have to sell out".

B.1. Thong Guan Industries Berhad (TGUAN, 7034)**Principal activities**

Flexible packaging manufacturer.

Major shareholder/s

Foremost Equals S/B.

Latest paid-up

105.27 mln shares of RM1.00 each

Market capitalisation

RM530.8 mln @ RM3.10

2016 PE Ratio (fully diluted)

Around 16.3 times @ RM3.10

*Figures are unaudited

Sources: Thong Guan, Bursa Malaysia, Capital Dynamics

Financial highlights (RM mln) – 31 December										
	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015*
Sales	469.3	518.2	564.6	408.8	488.6	540.0	631.2	720.3	740.2	712.1
Pre-tax profit	26.71	16.01	3.815	18.54	22.66	28.06	29.30	31.84	18.82	43.17
Net profit	21.07	12.01	4.646	15.16	19.79	27.04	27.22	28.18	17.48	38.50
Adjusted net profit	20.99	11.08	4.476	15.15	19.69	26.72	27.13	27.89	17.30	38.49
Depreciation	12.76	14.36	14.56	14.57	14.47	16.28	16.71	17.13	18.10	20.45
Finance cost	3.132	3.012	2.266	0.794	0.643	0.677	0.832	0.906	1.146	1.331
Current assets	183.1	210.8	182.0	182.5	211.6	237.7	272.1	323.6	407.9	382.6
Current liabilities	117.8	137.9	98.73	75.87	94.38	115.0	112.9	140.6	174.6	113.7
Fixed assets	127.6	122.8	113.7	104.5	109.6	129.0	120.3	122.9	135.5	146.0
Total assets	312.0	336.4	297.8	289.0	323.2	368.5	394.0	447.5	547.7	533.0
Total debts	70.74	59.68	55.48	22.54	29.39	38.76	42.63	49.65	96.88	51.59
Return on equity (%)	13.13	6.873	2.529	7.908	9.682	12.48	11.24	10.77	6.038	11.26



4th quarter RM mln		
	31/12/15*	31/12/14
Sales	195.7	167.0
Pretax profit	18.13	-4.51
Net profit	15.52	-4.17
Finance cost	0.349	0.511
Depreciation	4.499	4.803
Cash & cash equivalents	103.9	91.56

This week, *iCapital* features Thong Guan Industries Berhad (TGUAN), a manufacturer of flexible packaging. Headquartered in Kedah, the company was incorporated in 1942 and became a public listed company in 1997. It specialises in the manufacturing of cast LLDPE stretch film but also produces other products such as garbage bags, industrial films, PVC foodwrap, and compound masterbatch, with a total production capacity of about 100,000 tonnes per annum.

Business Operations

Currently, it has eight plants in Kedah, two plants in China, two plants in Kota Kinabalu, and one plant (joint venture) in Thailand. Its main products are stretch film and garbage bags which contribute 50-55% and about 20% of sales respectively, followed by industrial films (about 10%), PVC foodwrap (about 8%), and masterbatch compound business (about 5%). The split of revenue between local sales and export sales is about 15% versus 85%. The company is exporting to more than 50 countries, some of which are Japan, Australia, China, New Zealand, and Taiwan. Japan itself contributes 30% of sales, whereas Australia and New Zealand contribute a total of 20% of sales. Its largest customer generates less than 2% of revenue, whereas its top 10 customers generate less than 8% of revenue. Besides that, it has about 300 active customers. It does not have long-term contracts with customers but deals with them based on monthly orders. The company has been doing business with its top 10 customers for a long period of time, some for over 10 years, some for over 15-20



Thong Guan's production facilities

Source: thongguan.com

While chopping off its distributors and selling directly to customers to enhance its profit margin, **it may also result in more loyal customers in addition to its existing pool of 300 active customers.**

years. The raw material cost makes up 80% of total costs, whereas staff cost is less than 3%; utility is approximately 2%; depreciation about 3%. Less than 10% of the raw materials are sourced locally.

Business strategies

While adding new machinery and equipment to its production lines, such as the five-layered blown film stretch hood line from Germany, the company has been disposing of old machines which cannot produce films that are less than 15 microns

in thickness. Additionally, it has recently set up a new R&D centre in Kedah which will demonstrate to its customers how nano-layered stretch films, which meet the European standards for pallet stability and safety, can better protect goods while they are being transported. Also, it launched new packaging products last year, such as nano-layered stretch film materials and stretch hood materials, which are expected to be key contributors to group revenue next year. Meanwhile, for its high-margin

product, PVC foodwrap, it plans on tapping into new markets such as Latin America and Africa, while growing in existing markets such as Pakistan and India.

Financial Performance

The company has generated an increasing stream of revenue over the last 10 years except in 2009, which occurred due to the decrease of export sales and price falls arising from the decline in raw material costs and other input costs. The adjusted profit margin was squeezed in 2008 because of inventory write down and discounts given to customers following the sharp drop in raw material prices in the first quarter of the year. In 2014, revenue grew because of higher exports of mainly stretch film products and higher raw material prices; however, the adjusted net profit margin plunged to

2.34% because of the losses it suffered from its China-based operations, weak demand from its main market, Japan, higher operating costs due to minimum wage regulation, electricity tariff hikes, and increases in transportation and packaging material costs. The margin significantly improved in 2015 due to a higher margin contributed by export sales - see **figure 1**.

The company has a healthy and improving liquidity. The company's current ratio rose from 2.07 in 2011 to 3.36 in 2015; the quick ratio rose from 1.02 in 2011 to 1.97 in 2015; whereas the cash ratio also increased from 0.35 in 2011 to 0.94 in 2015 - see **table 1**.

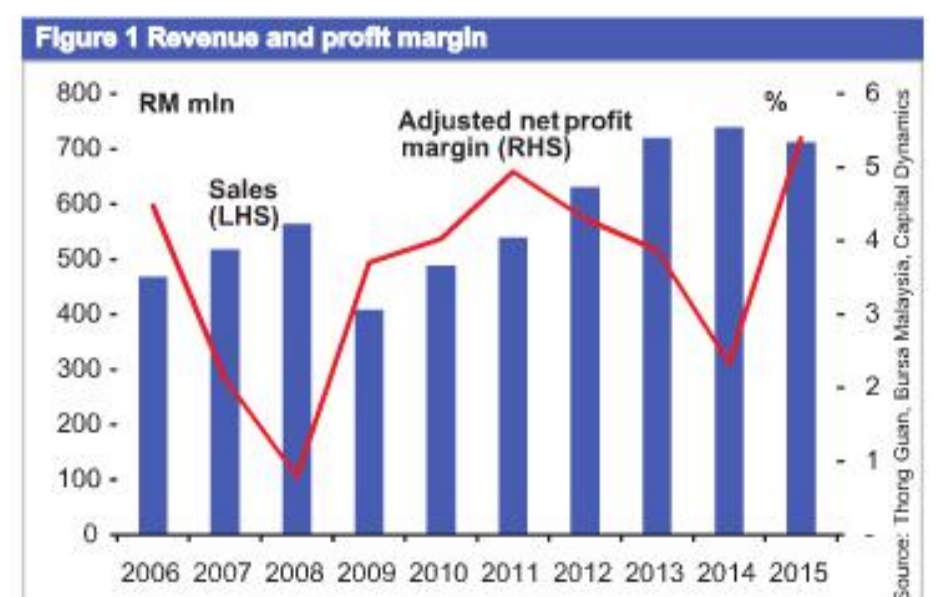
Table 2 & 3 below show the current asset breakdown. For the past five years, on average, 44% of its total current assets were made up of inventory, 31% trade receivables, 23% cash and cash equivalents, and 2% others.

TURN TO PAGE 17 >>

Table 1 Liquidity ratio					
	2011	2012	2013	2014	2015*
Current ratio	2.07	2.41	2.30	2.34	3.36
Quick ratio	1.02	1.42	1.37	1.23	1.97
Cash ratio	0.35	0.70	0.60	0.57	0.94

* Based on unaudited figures

Sources: Annual Reports, Bursa Malaysia, Capital Dynamics



B | Stock Selections

► FROM PAGE 16



The company has a lower profit margin than its peers but **better operating efficiency level along with constantly growing revenue.**



The fixed asset turnover of Thong Guan is higher than its peers. In the last five years, its average fixed asset turnover was 5.13 times compared with the approximate 3.2 times of its peers'. The slight drop in 2014 and 2015 was due to slower sales as experienced by its major competitors as well – see **table 4**.

On 15 Oct 2014, the company issued RM52,602,250 nominal value of 5-year 5% ICULS at 100% of its nominal value for capital expansion and working capital purposes. The ICULS conversion rate is one ordinary share for one ICULS. The last closing price for the ICULS is RM2.92 and there are currently 52,602,250 ICULS units outstanding. During the financial year 2014, the company issued 26,301,106 free warrants on the basis of one warrant for every two ICULS subscribed for. The conversion period is five years with an exercise price of RM1.50. The conversion ratio is one ordinary share for one warrant. The last closing price for the warrants is RM1.93 and there are currently 26,234,606

warrant units outstanding.

Conclusion

At RM3.10 and with ICULS and warrants outstanding, Thong Guan is capitalised at RM530.8 mln. For this, what do investors get in return ?

The company has a lower profit margin than its peers but better operating efficiency levels along with constantly growing revenue. Given its moderate investment in property, plants and equipment, the company is further increasing its production capacity while launching new products. Chopping off distributors and selling directly to customers could enhance its profit margin and also result in more loyal customers in addition to its existing pool of 300 active ones.

With a regular investment in machinery and equipment alongside efforts to enhance the profit margin and expand market share, the company is believed to be heading for further growth. *i* Capital revises its rating for Thong Guan Industries Berhad to a Buy below RM2.50/Hold for the longer-term. •

Table 2 Current asset breakdown (RM min)

	2011	2012	2013	2014	2015*
Inventory	120.3	111.6	130.3	192.8	158.6
Trade receivables	77.52	80.90	108.3	114.9	116.7
Cash and cash equivalent	38.57	79.01	70.25	91.56	103.9
Others	1.295	0.573	14.82	8.554	3.369
Total	237.7	272.1	323.6	407.9	382.6

*Figures are unaudited

Sources: Annual reports, Bursa Malaysia, Capital Dynamics

Table 3 Current asset breakdown (%)

	2011	2012	2013	2014	2015*
Inventory	50.61	41.01	40.26	47.28	41.46
Trade receivables	32.62	29.74	33.45	28.18	30.50
Cash and cash equivalent	16.23	29.04	21.71	22.45	27.16
Others	0.545	0.211	4.580	2.097	0.881
	50.61	41.01	40.26	47.28	41.46

*Figures are unaudited

Sources: Annual reports, Bursa Malaysia, Capital Dynamics

Table 4 Fixed asset turnover

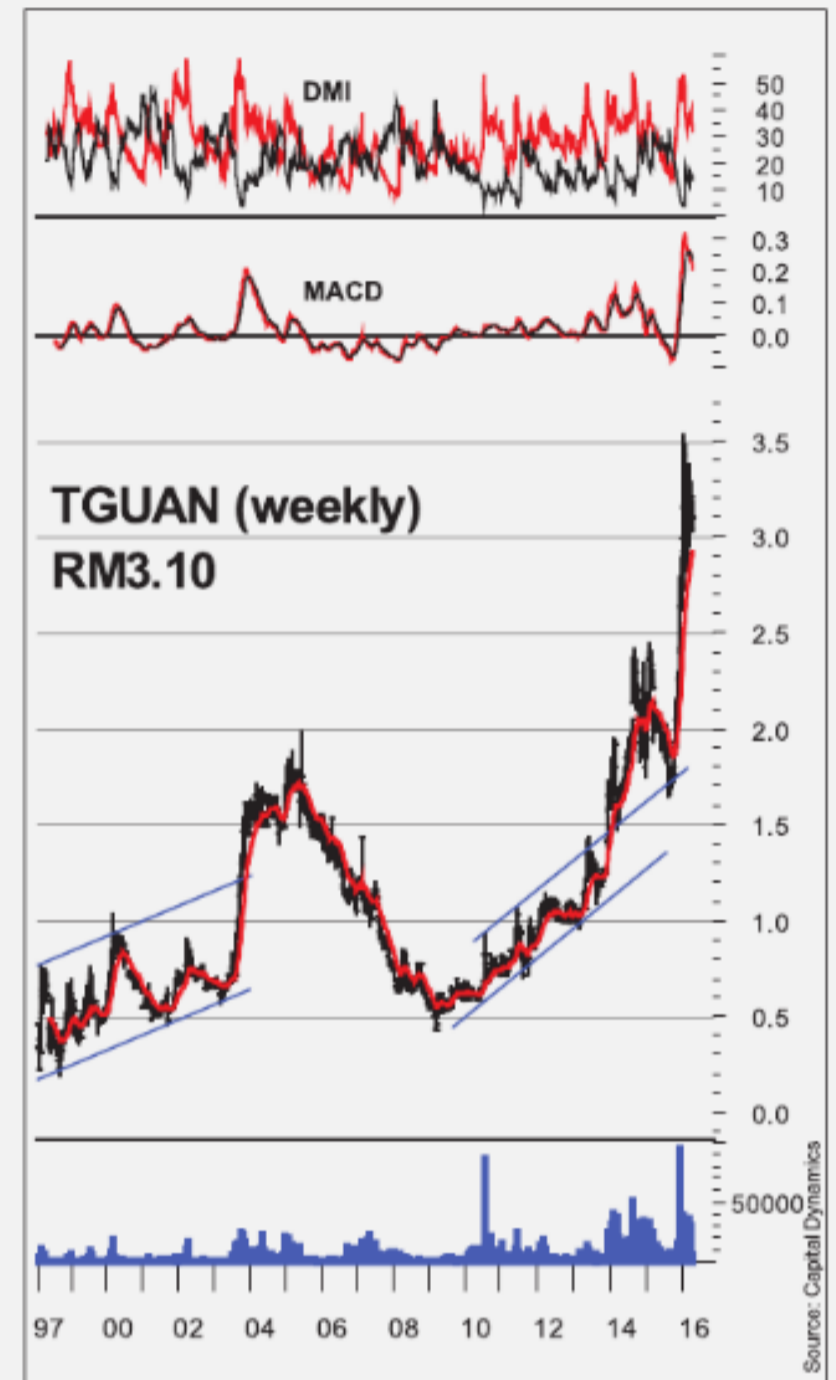
	2011	2012	2013	2014	2015*
PPE (RM mln)	129.00	120.34	122.90	135.53	146.01
Growth rate (%)	17.70	-6.71	2.13	10.28	7.73
Sales (RM mln)	540.01	631.19	720.28	740.23	712.09
Growth rate (%)	10.52	16.88	14.11	2.77	-3.80
Fixed asset turnover (times)	4.19	5.25	5.86	5.46	4.88

*Figures are unaudited

Sources: Annual reports, Bursa Malaysia, Capital Dynamics

Technical Analysis of Thong Guan Industries Berhad

After listing on the Mainboard in Dec 1997, Thong Guan Industries (TGUAN) fluctuated in an upward sloping price channel for almost 6 years. It broke the resistance of its upper boundary in Oct 2003, contributed by growth in revenue from exports, its China based operation and weakening of the US\$. It peaked out at RM2.00 followed by a downtrend which lasted for 4 years. In tandem with economic recovery, it embarked on a rally within a rising price channel. Breaking out from its channel, the resistance line provided TGUAN with strong support. The second rebound pushed TGUAN to surge in a parabolic manner, supported by a substantial increase in trading volume, and hit a high of RM3.50 in Jan 2016. However, it has lost its upward momentum; its weekly MACD has turned bearish. Breaking its 20-week exponential moving average would see Thong Guan Industries falling all the way to its major support at RM2.00.



icapital.biz Berhad (ICAP,5108)

Introduction

icapital.biz Berhad is a RM140 million Closed-end Fund, listed on the Main Board of Bursa Malaysia in 2005. The fund is managed by Capital Dynamics Asset Management Sdn Bhd and advised by Capital Dynamics Sdn Bhd. It is currently the only listed closed-end fund in Malaysia.

Fund Facts

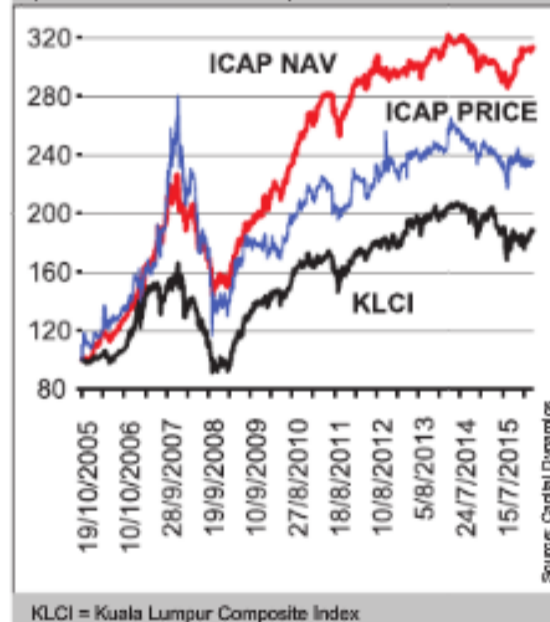
NAV (as at 6 Apr 2016)	RM3.02
Share Price	RM2.28
Premium(+)/Discount(-)	-24.50%
KLCI	1,717.01
Fund Manager	Capital Dynamics Asset Management Sdn Bhd
Paid-up Capital	140 million shares
Listed on	Bursa Malaysia's Main Market
Structure	Closed-end

INCEPTION DATE – 19 OCTOBER 2015

Recent Performance

	6 Mar 2016	6 Apr 2016	% Change
ICAP NAV (RM)	3.02	3.02	0.00
ICAP PRICE (RM)	2.27	2.28	0.44
KLCI (RM)	1,692.49	1,717.01	1.45

ICAP CUMULATIVE PERFORMANCE IN MYR (19 OCT 2005 TO 6 APR 2016)



Total Return, From Inception

	Since Inception (%)	Annual compound return (%)
ICAP NAV (RM)	212.52	11.50
ICAP PRICE (RM)	135.00	8.50
KLCI (RM)	87.82	6.20

*Special Dividend of 9.5 sen per share less Income Tax of 25% for the financial year ended 31 May 2013 is deducted from NAV and share price as at 17th September 2013.

NOTE: % change and Total Returns are calculated based on the announced figures plus the dividend paid.

The performance of icapital.biz Berhad for the period 19 October 2005 to 31 Dec 2014 has been independently verified. The performance for the period 1 January 2015 to 6 April 2016 is believed to be reliable, but has not been independently verified. Past performance and any forecast are not necessarily indicative of future or likely performance.