

21 November 2019

# Thong Guan Industries Bhd

## 9MFY19 Above Expectation

By Marie Vaz | [msvaz@kenanga.com.my](mailto:msvaz@kenanga.com.my);

**9MFY19 CNP of RM43.6m came in above our expectation at 89%, on margin improvement from better product mix with EBIT margin of 7.7% vs. our expectation of 6.6%. No dividend, as expected. The Group cautions that the challenging global outlook may weigh on demand but is actively seeking new customers and markets. Upgrade FY19-20E CNP by 26% on better margins. Maintain OP with a higher TP of RM4.10 (from RM3.00) on 12x FY20E EPS.**

**Above expectations on better margin.** 9MFY19 Core Net Profit (CNP) of RM43.6m came above our expectations at 89%. Top-line came in within our expectations at 79% while strong EBIT margin of 7.7% vs. our expectation of 6.6% came in at 92% of our EBIT expectations on better-than-expected product mix. No consensus was available as the stock is not widely tracked. No dividend, as expected with the bulk of dividends to be paid out in 4Q based on historical trends.

**Results' highlight.** YoY, 9MFY19 top-line increased by 9% on strong sales from increased exports of stretch film, garbage bags and courier bags. However, EBIT margin improved by 2.6ppt on better product margins and aided by lower resin cost environment this year which translated straight to bottom-line which was also up by 59%. QoQ, top-line was up by a strong 12% on higher demand for stretch film, garbage bags and courier bags. This coupled with a rise in EBIT margin (+2.2ppt) due to abovementioned reasons boosted CNP to increase by 45% despite slightly higher effective tax rate of 18% (vs 14.4%).

**Outlook.** The group cautioned that the global outlook which may weigh on demand for the sector in terms of sales growth from existing customers and the pace of market expansion. Moving forward, TGUAN will continue to seek new customers and markets for its products. The Group is also constantly investing in R&D to improve sales and margins for existing products (i.e. stretch film) and aims to target more MNCs. TGUAN is focusing on continued expansion into higher-margin production lines to sustain the plastic segment's margins going forward.

**Increase FY19-20E CNP by 26% each to RM61.6-63.3m** post increasing EBIT margin to 8.3% (from 6.6%) on expectations of improving product margins in coming quarters which is bolstered by the low resin cost environment. At current levels, FY19-20 dividends of 9.3-9.6 sen imply 3.0-3.1% yields based on an unchanged 24% payout ratio, in line with historical trends.

**Maintain OUTPERFORM with a higher Target Price to RM4.10 (from RM3.00).** Our TP is based on a higher FY20E FD EPS of 34.4 sen (from 27.2 sen) and a higher ascribed PER of 12.0x SD (4-year historical average valuations) from 11.0x (-0.5SD) as EBIT margin appear to be improving. Going forward, we may look to lift our valuations further should we see better earnings consistency and strong margin growth above historical high of 9.7%. We are comfortable with our OUTPERFORM call as we believe we have priced in most earnings risk and we are comfortable with the average valuations. Note that TGUAN was our preferred pick for 4QCY19 and the stock has done well, up 24% since our upgrade in our strategy report (*Seeking Convincing Margin Improvements dated 4<sup>th</sup> October 2019*) on the then compelling valuations of 9.0x PER while we believe TGUAN's better valuations is justified given improved earnings and margins.

**Risks to our call include:** (i) volatile plastic resin prices, (ii) foreign currencies fluctuations, and (ii) lower-than-expected margin.

## OUTPERFORM ↔

Price: **RM3.15**  
Target Price: **RM4.10** ↑

### Share Price Performance



KLCI 1,601.14  
YTD KLCI chg -5.3%  
YTD stock price chg 43.2%

### Stock Information

Shariah Compliant	Yes
Bloomberg Ticker	TGI MK EQUITY
Market Cap (RM m)	578.4
Shares Outstanding	183.6
52-week range (H)	3.15
52-week range (L)	2.18
3-mth avg daily vol:	299,316
Free Float	47%
Beta	1.0

### Major Shareholders

Foremost Equals Sdn Bhd	40.5%
Employees Provident Fund Board	2.4%
Neoh Choo Ee & Company Sdn Bhd	1.9%

### Summary Earnings Table

FY Dec (RM'm)	2018A	2019E	2020E
Turnover	861.6	891.3	916.8
EBIT	56.7	73.7	75.4
PBT	52.0	73.2	75.3
<b>Net Profit (NP)</b>	43.7	61.6	63.3
<b>Core NP*</b>	48.0	61.6	63.3
Consensus (NP)	N.A.	54.0	52.1
Earnings Revision	N.A.	26%	26%
Core EPS (sen)	30.4	39.0	40.0
FD Core EPS (sen)	26.1	33.4	34.4
FD EPS growth	12.9%	28.2%	2.8%
NDPS (sen)	8.0	9.3	9.6
FD BVPS (RM)	2.7	3.0	3.3
FD Core PER (x)	11.9	9.3	9.0
FD Price/BV (x)	1.1	1.0	1.0
Net Gearing (x)	N.Cash	N.Cash	N.Cash
Net Div. Yield	2.2%	3.0%	3.1%

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**OTHER POINTS**

<b>Results Highlights</b>								
<b>FYE Dec (RM'm)</b>	<b>3Q19</b>	<b>2Q19</b>	<b>QoQ Change</b>	<b>3Q18</b>	<b>YoY- Change</b>	<b>9M19</b>	<b>9M18</b>	<b>YoY-Ytd Change</b>
Turnover	256.5	229.7	12%	221.6	16%	703.4	642.5	9%
Operating Income	23.1	15.6	48%	12.6	83%	54.3	32.7	66%
Interest income	1.1	1.1	-6%	0.9	25%	3.2	2.2	44%
Finance costs	(1.1)	(1.2)	-6%	(1.0)	12%	(3.4)	(2.3)	46%
Associates	0.1	0.0	n.a.	0.0	n.a.	0.1	0.0	n.a.
<b>Pretax profit</b>	<b>23.2</b>	<b>15.6</b>	<b>49%</b>	<b>12.5</b>	<b>86%</b>	<b>54.2</b>	<b>32.5</b>	<b>66%</b>
Taxation	(4.2)	(2.3)	86%	(2.2)	94%	(9.0)	(4.9)	82%
Profit after tax	19.0	13.3	43%	10.3	84%	45.2	27.6	64%
Minority interest	(1.7)	0.4	-475%	(0.3)	534%	(1.3)	(0.4)	187%
<b>Net profit</b>	<b>17.3</b>	<b>13.8</b>	<b>26%</b>	<b>10.0</b>	<b>73%</b>	<b>43.9</b>	<b>27.2</b>	<b>62%</b>
<b>Core net profit</b>	<b>17.5</b>	<b>12.0</b>	<b>45%</b>	<b>9.2</b>	<b>90%</b>	<b>43.6</b>	<b>27.4</b>	<b>59%</b>
Core EPS (sen)	11.1	8.0		6.7		27.6	20.0	
NDPS (sen)	0.0	0.0		0.0		0.0	0.0	
NTA/share (RM)	3.50	3.38		3.51		3.50	3.51	
Operating margin	9.0%	6.8%		5.7%		7.7%	5.1%	
Pretax margin	9.0%	6.8%		5.6%		7.7%	5.1%	
Core net profit margin	6.8%	5.2%		4.1%		6.2%	4.3%	
Effective tax rate	18.0%	14.4%		17.3%		16.6%	15.2%	

Source: Company, Kenanga Research

<b>Segmental Breakdown</b>								
<b>FYE Dec (RM'm)</b>	<b>3Q19</b>	<b>2Q19</b>	<b>QoQ Change</b>	<b>3Q18</b>	<b>YoY- Change</b>	<b>9M19</b>	<b>9M18</b>	<b>YoY-Ytd Change</b>
<b>Turnover</b>								
Plastic products	241.7	214.3	13%	206.7	17%	657.6	598.6	10%
F&B, other consumable products	14.9	15.4	-3%	14.9	0%	45.9	43.9	4%
<b>Group Turnover</b>	<b>256.5</b>	<b>229.7</b>	<b>12%</b>	<b>221.6</b>	<b>16%</b>	<b>703.4</b>	<b>642.5</b>	<b>9%</b>
<b>Segment Results</b>								
Plastic products	22.2	14.7	51%	12.5	78%	51.8	34.6	50%
F&B, other consumable products	0.9	0.8	11%	(0.0)	n.m.	2.4	(2.1)	n.m.
<b>Group PBT</b>	<b>23.2</b>	<b>15.6</b>	<b>49%</b>	<b>12.5</b>	<b>86%</b>	<b>54.2</b>	<b>32.5</b>	<b>66%</b>
<b>PBT Margin</b>								
Plastic products	9.2%	6.9%		6.1%		7.9%	5.8%	
F&B, other consumable products	6.3%	5.5%		-0.3%		5.2%	-4.8%	
<b>Group PBT Margin</b>	<b>9.0%</b>	<b>6.8%</b>		<b>5.6%</b>		<b>7.7%</b>	<b>5.1%</b>	

Source: Company, Kenanga Research

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### Peer Comparison

Name	Last Price	Market	Shariah	Current	Revenue Growth		Core Earnings Growth		PER (x) - Core Earnings			PBV (x)		ROE (%)	Net Div. Yld. (%)	Target Price	Rating	
	(RM)	Cap (RM'm)	Compliant	FYE	1-Yr. Fwd.	2-Yr. Fwd.	1-Yr. Fwd.	2-Yr. Fwd.	Hist.	1-Yr. Fwd.	2-Yr. Fwd.	Hist.	1-Yr. Fwd.	1-Yr. Fwd.	1-Yr. Fwd.	(RM)		
<b>STOCKS UNDER COVERAGE</b>																		
SCGM BHD	1.37	262.4	Y	04/2020	17.4%	21.7%	45.8%	47.9%	N.A.	27.4	18.5	1.7	1.5	5.8%	1.5%	1.200	MP	
SCIENTEX BHD	9.25	4,766.2	Y	07/2020	16.9%	8.6%	16.5%	22.9%	14.9	12.8	10.4	2.7	2.2	20.0%	2.3%	9.45	MP	
SLP RESOURCES BHD	1.30	412.0	Y	12/2019	12.5%	5.4%	-6.7%	5.5%	16.3	17.3	16.5	2.3	2.1	12.6%	4.1%	1.45	OP	
THONG GUAN INDUSTRIES BHD	3.15	578.4	Y	12/2019	3.4%	2.9%	28.3%	2.8%	11.9	9.3	9.0	1.1	1.0	12.0%	3.0%	4.10	OP	
TOMYPAK HOLDINGS	0.500	209.5	Y	12/2019	-2.5%	5.6%	-3.3%	-123.3%	N.A.	N.A.	N.A.	1.4	1.0	-6.1%	0.0%	0.270	UP	
<b>Simple Average</b>					<b>9.6%</b>	<b>8.8%</b>	<b>16.1%</b>	<b>-8.9%</b>	<b>14.4</b>	<b>16.7</b>	<b>13.6</b>	<b>1.8</b>	<b>1.6</b>	<b>8.8%</b>	<b>2.2%</b>			

Source: Bloomberg, Kenanga Research

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**Stock Ratings are defined as follows:****Stock Recommendations**

OUTPERFORM	: A particular stock's Expected Total Return is MORE than 10%
MARKET PERFORM	: A particular stock's Expected Total Return is WITHIN the range of -5% to 10%
UNDERPERFORM	: A particular stock's Expected Total Return is LESS than -5%

**Sector Recommendations\*\*\***

OVERWEIGHT	: A particular sector's Expected Total Return is MORE than 10%
NEUTRAL	: A particular sector's Expected Total Return is WITHIN the range of -5% to 10%
UNDERWEIGHT	: A particular sector's Expected Total Return is LESS than -5%

**\*\*\*Sector recommendations are defined based on market capitalisation weighted average expected total return for stocks under our coverage.**

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