Investment Idea

Thong Guan Industries Bhd

The growth story continues

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★★★★☆ **BUY**

Price: **RM2.67**
Target price: **RM3.94**

We maintain our BUY recommendation on Thong Guan Industries Bhd (TGUAN) with a higher target price of RM3.94 from RM3.40 as we roll over to FY22. TGUAN's balance sheet remains strong at RM65m as at 1HFY21. Our TP is based on unchanged 14.5x PER (as per the 5-year average valuation of industry players) over FY22 EPS. Our BUY recommendation is premised on (i) strong earnings growth; (ii) improving demand; and (iii) higher production capacity.

To recap, TGUAN started in 1942 as a tea trading company under the 888 brand. Over the decades, the group has progressively moved up its value chain and is now the world's top 10 stretch film producer. TGUAN also one of the largest plastic packaging manufacturers in Asia Pacific with production capacity of more than 150,000MT/annum. Presently, over 90% of sales are underpin by plastics products (stretch films - 45%, industrial bags - 16%, garbage bag -16%, courier bag - 6%, PVC food wrap - 5%, compounding - 1%), while F&B segment contributed 8% of revenue anchored by its own "888" brand. Today, TGUAN has built a strong presence in the export market (over 80% of revenue) and is the top garbage bag supplier to Japan conquering 12% of market share, testament to its stringent product quality control.

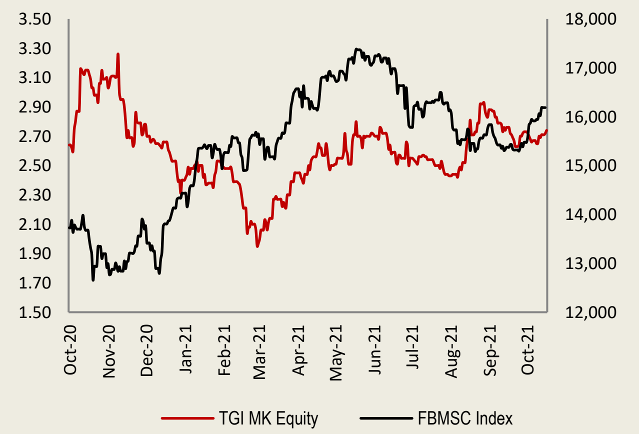
The packaging industry in Malaysia has over the years undergone consolidation, especially within the plastic packaging industry. In effect, the elimination of competition has enabled TGUAN access to new clients where previously was not possible. To this extent, TGUAN have been striving to move up the value chain coupled with the setting up of its own R&D centre. Its premium Nano stretch film which garners higher margin than the conventional film has been gaining good traction and the Group plan to add additional four lines progressively till year 2023, with potential additional revenue of RM80m-RM100m per line, representing approximately 10% of present revenue each line.

We gathered that TGUAN is running at full utilisation rate and orders are filled until end of the year. Meanwhile, expansion plan is in the pipeline for the next 5 years, with an estimated yearly CAPEX of RM30m to RM40m. The group's expansion plans include the construction of three new factory buildings on a 16-acre site in Sungai Petani to produce high-quality stretch and blown film products, courier and speciality bags.

Plastic film manufacturing is sensitive to price fluctuation of raw material (resin) by nature as resin made up majority of total cost. TGUAN operates based on cost-plus pricing strategy and is able to increase selling price in the case of rising resin prices, while the time lag effect in selling price adjustment could lead to near term margin expansion. With the recent reopening of economy in Malaysia, we reckon TGUAN will benefit as the plants will be able to run in full capacity without disruption. We maintain our FY21 and FY22 net earnings forecasts at RM88.6m and RM103.0m respectively. Meanwhile balance sheet is strong with net cash of RM65 as at 1HFY21.

Technically Speaking

Resistance level	RM2.74
Support level	RM2.65



KLCI	1,583.08
YTD KLCI change	-2.7%
YTD FBM SC change	10.3%
YTD stock price change	5.5%

Stock Information

Market Cap (RMmil)	1,022.93
Issued Shares (m)	383.1
52-week range (H)	3.35
52-week range (L)	1.95

Major Shareholders

Foremost Equals SB	38.8%

Summary Earnings Table

FY Dec (RM'm)	2019A	2020A	2021F	2022F
Revenue	939.2	960.6	1,101.70	1,272.0
EBIT	75.2	97.5	114.6	133
Pretax profit	75.5	100.2	113.3	131.2
Net profit	61.8	75.5	88.6	103.0
Core Net Profit	**61.1**	**75.4**	**88.6**	**103.0**
Consensus	-	-	89.75	101.5
EPS (sen)	16.2	19.9	23.4	27.2
EPS growth (%)	40%	23%	18%	16%
DPS (sen)	4.4	5.0	5.9	6.8
PER (x)	16.5	13.4	11.4	9.8
BV/Share (RM)	1.52	1.71	1.88	2.09
ROE (%)	10.6%	11.7%	13.0%	13.7%
Div. Yield (%)	1.65%	1.87%	2.21%	2.55%

Sources: Company, Rakuten Trade Research

COMPANY	Definition
Buy	The stock return is expected to exceed the KLCI benchmark by more than 10% over the next 6-12 months.
Trading Buy	Short-term positive development on the stock that could lead to a re-rating in the share price and translate into an absolute return of 10% over the next 3-6 months. Trading Buy is generally for investors who are willing to take on higher risks.
Take profit	The stock return previously recommended has gained by >10%
Hold	The stock return is expected to be in line with the KLCI benchmark (+/- 5%) over the next 6-12 months.
Sell	The stock return is expected to underperform the KLCI benchmark by more than 10% over the next 6-12 months.
SECTOR	
Overweight	Industry expected to outperform the KLCI benchmark, weighted by market capitalization, over the next 6-12 months.
Neutral	Industry expected to perform in-line with the KLCI benchmark, weighted by market capitalization, over the next 6-12 months.
Underweight	Industry expected to underperform the KLCI benchmark, weighted by market capitalization, over the next 6-12 months.

Scoring model:

The in-house scoring model is derived from Rakuten Trade Research valuation matrix based on earnings growth, earnings visibility, business model, valuation, balance sheet, technical analysis, and shareholder value creation. Each parameter is given a specific weighting.

Published:

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