



Scientex Berhad

Setting Foot in America

TP: RM8.50 (+26.1%)

Last Traded: RM6.74

BUY

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TA Research Team Coverage

Tel: +603-2072 1277 (ext: 9602)

damia@ta.com.my

www.taonline.com.my

Last week, we met with the Investor Relations (IR) team of Scientex Berhad and gained further insights into Scientex's new venture in the US. We see this as good opportunity to expand its footing into the country. Key benefit to Scientex is to diversify export sales away from the saturating Japanese market. Maintain Scientex as Buy with unchanged target price of RM8.50/share.

Venturing into America

In November, Scientex announced that the company has established a new wholly-owned subsidiary called Scientex Phoenix, LLC to set up a new stretch film manufacturing plant in Arizona, USA. According to management, the plant will have a manufacturing capacity of 30k tonnes/annum, boosting the group total capacity to 180k tonnes/annum.

Figure 1: Arizona Plant Progress Timeline

Timeline		Progress
CY	FY	
2017	1H18	Completion of plant in Arizona
1H18	2019	Trial run
2019	1H20	Running at full capacity

Source: TA Research, Company

The plant is expected to be completed by end-2017. Assuming a production trial run of 6 months, the plant should commence operations from 2Q18 (or beginning of FY19) onwards. As far as cost is concerned, it is estimated to cost US\$25mn (RM106.3mn excluding land cost) for the purchase of land and setting up the plant with 2 production lines. To finance this expansion, the company will use both internally-generated funds and borrowings.

Expanding Within the USA Market

Currently, Scientex is already exporting small volumes of stretch films to the US. Of the total capacity of 150k tonnes/annum, exports to the US account for only 1% while the majority is exported to Japan (90%) or sold in Malaysia (9%). However, exports to the US is expected to grow substantially to 17.5% of the group's sales mix when the US plant is ready for production.

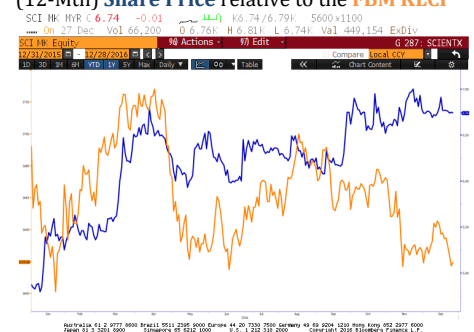
Share Information	
Bloomberg Code	SCI MK
Stock Code	4,731
Listing	Main Market
Share Cap (mn)	463.6
Market Cap (RMmn)	3,124.4
Par Value	0.5
52-wk Hi/Lo (RM)	7.08/4.72
12-mth Avg Daily Vol ('000 shrs)	407.9
Estimated Free Float (%)	32.8
Beta	0.5
Major Shareholders (%)	
Scientex Holdings Sdn Bhd	21.4
Scientex Leasing Sdn Bhd	10.0
Lim Teck Meng Sdn Bhd	8.1
Sim Swee Tin Sdn Bhd	5.3

Forecast Revision		
	FY17	FY18
Forecast Revision (%)	0.0	0.0
Core Net Profit (RMm)	314.7	361.6
Consensus	311.8	359.2
TA's / Consensus (%)	100.9	100.7
Previous Rating	Buy (Maintained)	

Financial Indicators		
	FY17	FY18
Net debt/ equity (%)	40.9	42.1
ROE (%)	21.4	20.8
ROA (%)	11.7	11.4
NTA/Share (RM)	2.2	2.7
Price/NTA (x)	3.1	2.5

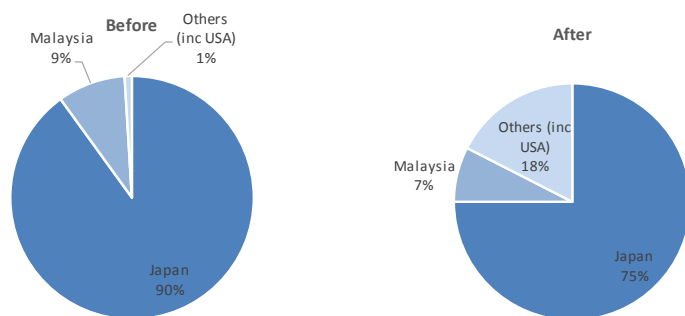
Share Performance (%)		
Price Change	SCIENTEX	FBM KLCI
1 mth	(2.7)	(0.6)
3 mth	(0.1)	(2.7)
6 mth	12.3	(0.9)
12 mth	38.1	(3.1)

(12-Mth) Share Price relative to the FBM KLCI



Source: Bloomberg

Figure 2: Before and After Comparison of Capacity Breakdown to Markets



Source: TA Research, Company

Our view

Overall, we are neutral on this venture despite our expectation that near-term contribution from the plant could be minimal. We see the establishment of the plant as a testament to long-term commitment to customers in the US and to maintain existing business relationship with existing customers.

Even though the expansion would allow Scientex to be closer to its US customers, we opine that the operating environment could be challenging due to: i) high level of competition among local stretch film players, ii) protectionist measures from the USA government in protecting local players, and iii) gestation period for local US market to buy from Scientex.

Forecast

No change to our FY17-18 earnings projections as the plant is expected to start contributing from FY19 onwards. Assuming that Scientex would fund 80% of the establishment cost via borrowings, the group's net gearing will be little changed at 0.1x for FY17.

Recommendation

We maintain our SOP-valuation of **RM8.50**/share for Scientex. We continue to like Scientex as the current market environment, where demand is far exceeding the supply, bodes well for the group's future profit. Maintain **Buy**

Earnings Summary

FYE July 31 (RM'mn)	2014	2015	2016	2017F	2018F
Revenue	1,589.7	1,801.7	2,201.0	3,095.3	3,670.5
Core EBIT	187.5	220.7	312.6	414.3	490.2
EI	(2.8)	(0.6)	1.9	0.0	0.0
D&A	(39.5)	(43.8)	(54.5)	(77.2)	(87.8)
Reported PBT	186.3	221.0	306.3	403.0	463.0
Core PBT	183.5	220.4	308.2	403.0	463.0
Taxation	(34.8)	(58.9)	(59.8)	(78.6)	(90.3)
Minority Interest	(3.1)	(3.9)	(5.7)	(9.7)	(11.2)
Reported Net Profit	148.5	158.2	240.9	314.7	361.6
Core Net Profit	145.7	157.6	242.7	314.7	361.6
Core EPS * (sen)	31.7	34.3	52.8	68.4	78.6
Dividend / Share * (sen)	10.0	11.0	16.0	20.0	23.0
Div Yield (%)	1.5	1.6	2.4	2.4	3.0

Cash Flow

FYE July 31 (RM'mn)	2014	2015	2016	2017F	2018F
PBT	186.3	221.0	306.3	403.0	463.0
D&A	39.5	43.8	54.5	77.2	87.8
Interest expense	7.1	8.3	17.4	17.2	20.3
Interest income	(2.1)	(4.2)	(7.4)	(6.2)	(15.2)
Others	(4.6)	0.5	4.5	0.0	0.0
Cash flow before WC	226.1	269.3	375.3	489.6	553.1
Changes in WC					
Inventories	(23.1)	(2.6)	(7.0)	(38.1)	(40.3)
Receivables	(19.8)	(45.8)	(34.8)	(122.1)	(87.9)
Payable	29.2	20.6	56.4	84.2	88.7
Others	(13.2)	(40.1)	28.0	0.0	0.0
Total working capital	(35.4)	(32.1)	70.4	(71.4)	(8.4)
Income tax paid	(37.3)	(45.4)	(65.0)	(78.6)	(90.3)
Others	191.1	237.1	445.4	419.8	554.5
CFO	153.8	191.8	380.4	341.2	464.2
Investing Cash Flow					
Capex	(65.7)	(100.0)	(281.4)	(300.0)	(200.0)
Others	(83.8)	60.9	(279.2)	6.2	15.2
CFI	(149.5)	(39.1)	(560.7)	(293.8)	(184.8)
Financing Cash Flow					
Net change in debts	(8.0)	(120.7)	217.6	236.3	130.0
Dividends paid	(47.1)	(47.1)	(49.8)	(94.4)	(108.5)
Finance costs paid	(7.2)	(8.3)	(17.4)	(17.2)	(20.3)
Others	(10.4)	30.2	39.7	0.0	0.0
CFF	(72.7)	(145.8)	190.2	20.0	4.0
Net change	(68.4)	6.9	10.0	67.4	283.5
Beginning cash	152.2	83.8	90.6	100.6	168.0
Ending cash	83.8	90.6	100.6	168.0	451.4

* Based on enlarged share base

FYE July 31 (RM'mn)	2014	2015	2016	2017F	2018F
PPE	552.1	642.8	952.5	1,175.3	1,287.5
Investment prop. + other inv.	9.6	24.1	25.0	25.0	25.0
Land held for prop. dev.	260.4	268.6	447.0	447.0	447.0
Associates & JV	37.5	41.5	48.7	48.7	48.7
Total Non-Current Assets	859.5	979.1	1,489.8	1,712.6	1,824.8
Prop. Dev. costs	104.6	136.5	174.7	174.7	174.7
Inventories	109.0	112.0	137.0	175.1	215.4
Receivables	243.5	321.7	350.7	472.8	560.7
Cash	83.8	90.6	100.6	168.0	451.4
Tax recoverable	0.0	0.0	0.0	0.0	0.0
Total Current Assets	540.8	660.8	763.0	982.8	1,337.5

FYE July 31 (RM'mn)	2014	2015	2016	2017F	2018F
Total Assets	1,400.4	1,639.9	2,252.8	2,695.4	3,162.3
Share Capital	115.0	115.0	115.0	115.0	115.0
Reserves	64.3	137.8	0.0	0.0	0.0
Retained profits	533.4	689.2	1,060.2	1,280.4	1,533.5
Shareholders' funds	712.7	942.0	1,175.2	1,395.4	1,648.5
MI	22.7	62.8	66.5	76.2	87.4
Total Equity	735.4	1,004.8	1,241.7	1,471.7	1,735.9
Non-Current Liabilities					
Loans & Borrowings	77.5	75.5	238.9	445.2	545.2
Others	40.9	59.5	60.7	60.7	60.7
Total Non-Current Liabilities	118.5	135.0	299.5	505.8	605.8
Current Liabilities					
Loans & Borrowings	262.9	149.9	232.7	262.7	292.7
Trade and other payables	254.4	308.3	431.2	520.0	639.8
Others	29.2	42.0	47.6	47.6	47.6
Total Current Liabilities	546.5	500.1	711.6	830.4	980.1
Total Equity and Liabilities	1,400.4	1,639.9	2,252.8	2,695.4	3,162.3

Ratios

FYE July 31 (RM'mn)	2014	2015	2016	2017F	2018F
Profitability ratios					
Gross Margin (%)	18.3	19.9	20.0	20.0	17.0
Core EBITDA Margin (%)	14.3	14.7	16.7	15.9	16.4
Core EBIT Margin (%)	11.8	12.3	14.2	13.4	13.4
PBT Margin (%)	11.7	12.3	13.9	13.2	13.8
Net Profit Margin (%)	9.3	8.8	10.9	10.3	10.7
Core Net Profit Margin (%)	9.2	8.7	11.0	10.3	10.7
Valuations					
PER (x)	20.9	19.6	12.9	9.8	8.0
NTA/share (x)	1.2	1.4	1.6	2.2	2.7
P/NTA (RM)	RM 5.6	4.8	4.2	3.1	2.5

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Stock Recommendation Guideline

- BUY** : Total return within the next 12 months exceeds required rate of return by 5%-point.
HOLD : Total return within the next 12 months exceeds required rate of return by between 0-5%-point.
SELL : Total return is lower than the required rate of return.
Not Rated: The company is not under coverage. The report is for information only.

Total Return is defined as expected share price appreciation plus gross dividend over the next 12 months.

Required Rate of Return of 7% is defined as the yield for one-year Malaysian government treasury plus assumed equity risk premium.

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for TA SECURITIES HOLDINGS BERHAD^(14948-M)
(A Participating Organisation of Bursa Malaysia Securities Berhad)
Kaladher Govindan – Head of Research