

22 March 2017

Consumer Non-cyclical | Packaging

Scientex

Buy (Maintained)

Target Price: MYR8.40
 Price: MYR7.25
 Market Cap: USD759m
 Bloomberg Ticker: SCI MK

Anticipating a Stronger 2HFY17

We maintain BUY on Scientex with a higher TP of MYR8.40 (from MYR7.83, 16% upside). We continue to like the company for its aggressive capacity expansion plan in both industrial and consumer packaging as well as defensive positioning in the property market to focus on affordable homes. Near-term growth could come from the production ramp-up of its BOPP plant, currently 35% utilised. The longer-term excitement is supported by its US expansion, thereby diversifying from its huge dependence on the Japanese market.

Expansion to drive growth. Moving forward, the near-term growth could come from the production ramp-up of its bi-axially oriented polypropylene film (BOPP) plant. Scientex targets to fill up its annual capacity of 60,000 tonnes in two years having commenced operations in Sep 2016. Its longer-term prospect is underpinned by an expansion into US. This would allow the company to diversify from its key Japanese market (90% of industrial revenue) besides benefiting from the ample supply of shale gas-based resin and savings in logistics costs. Meanwhile, for its property business, the focus would still be on the affordable homes with MYR700m worth of new launches targeted for FY17. Unbilled sales of MYR600m as at 1HFY17 (Jul) should provide earnings visibility for the next two to three years.

Maintain BUY. We trim FY17F-19F earnings by 4-5% as our previous expectations of the production ramp-up were too optimistic. Our SOP-derived TP is raised to MYR8.40 after adjusting to the revised risk assumptions to reflect improved global growth outlook and higher investor risk appetite. Maintain BUY as we continue to like Scientex for its aggressive capacity expansion in the manufacturing division and resilient market positioning in the property division. It appears to be cheaper in terms of P/E valuation vs industry peers due to its significant earnings contribution from its property business (64% as of 1HFY17).

2QFY17 (Jul) earnings announced on 22 Mar 2017 are slightly below expectations.

| FYE (Jul) (MYRm) | 2QFY17 | 1QFY17 | QoQ (%) | 2QFY16 | YoY (%) | Comments |
|------------------|--------|--------|---------|--------|---------|---|
| Revenue | 586.2 | 534.7 | 9.6 | 545.4 | 7.5 | Driven by two operating divisions. Manufacturing division rebounded from a weak 1QFY17. |
| EBITDA | 98 | 85 | 15.3 | 92 | 6.5 | Margin recovery from 1QFY17 |
| EBITDA Mar (%) | 16.7 | 15.9 | | 16.9 | | Slightly below expectation (36-38% of forecasts) |
| Net Profit | 65.2 | 53 | 23 | 64.6 | 0.9 | |
| Net Mar (%) | 11.1 | 9.9 | | 11.8 | | |

Source: Company data, RHB

Slightly below expectations. Scientex's 1HFY17 net profit of MYR118.2m (-5.8% YoY) was slightly below expectations, meeting 36-38% of our previous forecasts. 1H17's revenue was flattish (-0.3%) dragged down by industrial packaging (-3.2%) on lower exports while consumer packaging grew 3% thanks to the contribution from new lines. Stronger QoQ growth was observed in 2QFY17, with net profit jumping 23% to MYR64.6m in line with the sales recovery (+9.6%) driven by a ramp-up in production from both industrial and consumer packaging.

| Forecasts and Valuations | Jul-15 | Jul-16 | Jul-17F | Jul-18F | Jul-19F |
|-------------------------------------|--------|--------|---------|---------|----------|
| Total turnover (MYRm) | 1,802 | 2,201 | 3,293 | 3,873 | 4,284 |
| Reported net profit (MYRm) | 155 | 241 | 315 | 380 | 420 |
| Recurring net profit (MYRm) | 155 | 241 | 315 | 380 | 420 |
| Recurring net profit growth (%) | (8.1) | 55.4 | 30.7 | 20.6 | 10.6 |
| Recurring EPS (MYR) | 0.34 | 0.52 | 0.68 | 0.83 | 0.91 |
| DPS (MYR) | 0.11 | 0.16 | 0.21 | 0.25 | 0.27 |
| Recurring P/E (x) | 21.4 | 13.8 | 10.6 | 8.8 | 7.9 |
| P/B (x) | 3.53 | 2.84 | 2.39 | 2.01 | 1.71 |
| P/CF (x) | 17.7 | 9.0 | 13.8 | 7.5 | 7.8 |
| Dividend Yield (%) | 1.5 | 2.3 | 2.8 | 3.4 | 3.8 |
| EV/EBITDA (x) | 13.0 | 10.0 | 7.5 | 5.9 | 5.1 |
| Return on average equity (%) | 18.7 | 22.8 | 24.5 | 24.8 | 23.2 |
| Net debt to equity (%) | 13.4 | 29.9 | 29.7 | 11.3 | net cash |
| Our vs consensus EPS (adjusted) (%) | | | 2.4 | 8.6 | 12.0 |

Source: Company data, RHB

Share Data

| | |
|------------------------------|-------------|
| Avg Daily Turnover (MYR/USD) | 1.74m/0.39m |
| 52-wk Price low/high (MYR) | 5.93 - 7.54 |
| Free Float (%) | 29 |
| Shares outstanding (m) | 458 |
| Estimated Return | 16% |

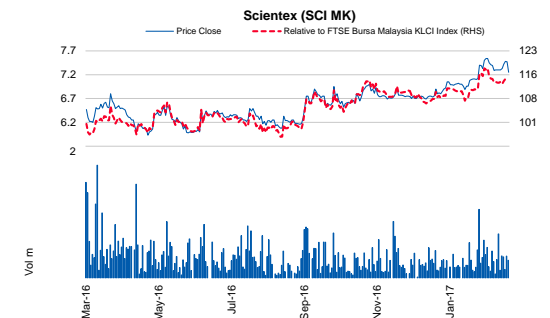
Shareholders (%)

| | |
|----------------------|------|
| Scientex Holdings SB | 21.4 |
| Scientex Leasing SB | 10.0 |
| Lim Teck Meng | 8.1 |

Share Performance (%)

| | YTD | 1m | 3m | 6m | 12m |
|----------|-----|-------|-------|------|------|
| Absolute | 8.2 | 2.1 | 7.6 | 17.7 | 12.1 |
| Relative | 1.3 | (0.6) | (0.5) | 12.6 | 10.4 |

Source: Bloomberg



Source: Bloomberg

Analyst

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Financial Exhibits

Financial model updated on : 2017-03-22

| | | | | | | |
|--|-------------------------------------|---------------|---------------|----------------|----------------|----------------|
| Asia | Financial summary | Jul-15 | Jul-16 | Jul-17F | Jul-18F | Jul-19F |
| Malaysia | Recurring EPS (MYR) | 0.34 | 0.52 | 0.68 | 0.83 | 0.91 |
| Consumer Non-cyclical | EPS (MYR) | 0.34 | 0.52 | 0.68 | 0.83 | 0.91 |
| Scientex | DPS (MYR) | 0.11 | 0.16 | 0.21 | 0.25 | 0.27 |
| Bloomberg SCI MK | BVPS (MYR) | 2.06 | 2.55 | 3.03 | 3.61 | 4.25 |
| Buy | Weighted avg adjusted shares (m) | 458 | 460 | 460 | 460 | 460 |
| Valuation basis | Valuation metrics | Jul-15 | Jul-16 | Jul-17F | Jul-18F | Jul-19F |
| SOP – DCF valuation for its manufacturing segment, and 40% discount to RNAV for its property division | Recurring P/E (x) | 21.4 | 13.8 | 10.6 | 8.8 | 7.9 |
| | P/E (x) | 21.4 | 13.8 | 10.6 | 8.8 | 7.9 |
| | P/B (x) | 3.53 | 2.84 | 2.39 | 2.01 | 1.71 |
| Key drivers | FCF Yield (%) | 2.6 | 2.7 | 4.2 | 11.2 | 10.7 |
| i. Ongoing capacity expansion of its plastic segment; | Dividend Yield (%) | 1.5 | 2.3 | 2.8 | 3.4 | 3.8 |
| ii. Venture into new film products that bear exciting market opportunities locally. | EV/EBITDA (x) | 13.0 | 10.0 | 7.5 | 5.9 | 5.1 |
| | EV/EBIT (x) | 15.6 | 11.8 | 8.8 | 6.8 | 5.9 |
| Key risks | Income statement (MYRm) | Jul-15 | Jul-16 | Jul-17F | Jul-18F | Jul-19F |
| i. Weak consumer spending; | Total turnover | 1,802 | 2,201 | 3,293 | 3,873 | 4,284 |
| ii. Soft property market. | Gross profit | 388 | 477 | 722 | 838 | 915 |
| | EBITDA | 266 | 367 | 503 | 595 | 643 |
| | Depreciation and amortisation | (44) | (55) | (75) | (80) | (84) |
| | Operating profit | 222 | 313 | 427 | 514 | 559 |
| | Net interest | (8) | (14) | (21) | (20) | (13) |
| | Income from associates & JVs | 4 | 7 | 4 | 4 | 5 |
| | Pre-tax profit | 218 | 306 | 411 | 498 | 551 |
| | Taxation | (59) | (60) | (88) | (110) | (121) |
| | Minority interests | (4) | (6) | (7) | (9) | (10) |
| | Recurring net profit | 155 | 241 | 315 | 380 | 420 |
| Company Profile | Cash flow (MYRm) | Jul-15 | Jul-16 | Jul-17F | Jul-18F | Jul-19F |
| Scientex is a manufacturer of industrial packaging with manufacturing facilities in Malaysia and Vietnam. It also has a property development arm with projects concentrated in Malaysia's southern region. | Change in working capital | (34) | 70 | (174) | (41) | (95) |
| | Cash flow from operations | 188 | 372 | 241 | 444 | 427 |
| | Capex | (100) | (281) | (100) | (70) | (70) |
| | Cash flow from investing activities | (37) | (561) | (100) | (70) | (70) |
| | Dividends paid | (48) | (53) | (94) | (114) | (126) |
| | Cash flow from financing activities | (146) | 190 | (95) | (94) | (89) |
| | Cash at beginning of period | 84 | 91 | 101 | 123 | 153 |
| | Net change in cash | 4 | 2 | 46 | 280 | 268 |
| | Ending balance cash | 88 | 92 | 147 | 403 | 421 |
| | Balance sheet (MYRm) | Jul-15 | Jul-16 | Jul-17F | Jul-18F | Jul-19F |
| | Total cash and equivalents | 91 | 101 | 123 | 153 | 176 |
| | Tangible fixed assets | 911 | 1,400 | 1,516 | 1,506 | 1,492 |
| | Total investments | 66 | 88 | 92 | 96 | 96 |
| | Total assets | 1,638 | 2,251 | 2,686 | 2,848 | 3,021 |
| | Short-term debt | 150 | 233 | 280 | 150 | 50 |
| | Total long-term debt | 76 | 239 | 280 | 200 | 100 |
| | Other liabilities | 19 | 24 | 24 | 24 | 24 |
| | Total liabilities | 633 | 1,009 | 1,217 | 1,104 | 972 |
| | Shareholders' equity | 942 | 1,175 | 1,396 | 1,661 | 1,955 |
| | Minority interests | 63 | 66 | 74 | 83 | 93 |
| | Total equity | 1,005 | 1,242 | 1,469 | 1,744 | 2,048 |
| | Net debt | 135 | 371 | 437 | 197 | (26) |
| | Total liabilities & equity | 1,638 | 2,251 | 2,686 | 2,848 | 3,021 |
| | Key metrics | Jul-15 | Jul-16 | Jul-17F | Jul-18F | Jul-19F |
| | Revenue growth (%) | 13.3 | 22.2 | 49.6 | 17.6 | 10.6 |
| | Recurrent EPS growth (%) | (55.6) | 54.7 | 30.7 | 20.6 | 10.6 |
| | Gross margin (%) | 21.5 | 21.7 | 21.9 | 21.6 | 21.3 |
| | Operating EBITDA margin (%) | 14.7 | 16.7 | 15.3 | 15.4 | 15.0 |
| | Net profit margin (%) | 8.6 | 10.9 | 9.6 | 9.8 | 9.8 |
| | Dividend payout ratio (%) | 31.9 | 31.3 | 30.0 | 30.0 | 30.0 |
| | Capex/sales (%) | 5.6 | 12.8 | 3.0 | 1.8 | 1.6 |
| | Interest cover (x) | 26.9 | 22.9 | 20.8 | 25.2 | 44.6 |

Source: Company data, RHB

Figure 1 : Scientex's 2QFY17 results review

| FYE Jul (MYRm) | 2QFY16 | 1QFY17 | 2QFY17 | QoQ (%) | YoY (%) | 1HFY16 | 1HFY17 | YoY (%) | Comments |
|------------------------|-------------|-------------|-------------|-------------|------------|--------------|--------------|--------------|---|
| Revenue | 545.4 | 534.7 | 586.2 | 9.6 | 7.5 | 1,096 | 1,120.9 | 2.3 | Marginal growth dragged down by manufacturing division |
| EBITDA | 92 | 85 | 98 | 15.3 | 6.5 | 187.5 | 182.9 | (2.5) | |
| Depreciation | (13.4) | (15.2) | (15.4) | 1.4 | 14.5 | (26.9) | (30.6) | 13.6 | |
| EBIT | 78.6 | 69.8 | 82.6 | 18.3 | 5.1 | 160.6 | 152.3 | (5.2) | |
| EBIT Margin (%) | 14.4 | 13 | 14.1 | | | 14.7 | 13.6 | | Margin erosion due to the lower product margin and penetrative pricing strategy in manufacturing division |
| Interest expense | (2.6) | (3.5) | (3.6) | 4.9 | 39.5 | (5.7) | (7.1) | 24.7 | |
| Interest income | 3.9 | 1 | 2.9 | nm | (25.5) | 5.7 | 3.956 | nm | |
| Associates | 0.0 | 0.0 | 0.0 | nm | nm | 0.0 | 0.0 | nm | |
| Pretax profit | 79.9 | 67.3 | 81.8 | 21.5 | 2.5 | 160.6 | 149.2 | (7.1) | |
| Pretax Margin (%) | 14.6 | 12.6 | 14 | | | 14.7 | 13.3 | | |
| Tax | (13.2) | (13.4) | (15.5) | 15.5 | 17.5 | (31.2) | (28.9) | (7.3) | |
| Effective tax rate (%) | 16.5 | 19.9 | 19 | | | 19.4 | 19.4 | | |
| Minority Interest | 2 | 0.9 | 1.1 | 21.2 | (44.5) | 3.9 | 2.1 | (47.7) | |
| Net Profit | 64.6 | 53 | 65.2 | 23 | 0.9 | 125.5 | 118.2 | (5.8) | Slightly below expectation at 36-38% of the forecasts |
| Net Margin (%) | 11.8 | 9.9 | 11.1 | | | 11.4 | 10.5 | | |

Source: Company, RHB

Figure 2: Segmental breakdown

| FYE Jul (MYRm) | 2QFY16 | 1QFY17 | 2QFY17 | QoQ (%) | YoY (%) | 1HFY16 | 1HFY17 | YoY (%) | Comments |
|------------------------|--------------|--------------|--------------|------------|------------|--------------|---------------|------------|--|
| Revenue | | | | | | | | | |
| Manufacturing | 402.0 | 379.7 | 411.9 | 8.5 | 2.5 | 794 | 791.6 | -0.3 | QoQ growth driven by growth in both industrial (+10%) and consumer segment (+7.1%) |
| Property | 143.4 | 155 | 174.3 | 12.5 | 21.5 | 302 | 329.4 | 9 | Driven by stable sales and construction progress |
| Total | 545.4 | 534.7 | 586.2 | 9.6 | 7.5 | 1096 | 1120.9 | 2.3 | |
| EBIT | | | | | | | | | |
| Manufacturing | 38.7 | 23.8 | 30.2 | 27.2 | - | 76.7 | 54 | -29.6 | QoQ improvement on better sales and margin |
| Property | 36.4 | 45.1 | 52.3 | 16.1 | 43.8 | 83.9 | 97.4 | 16.1 | In line with the higher billing of sales |
| Total | 75.1 | 68.8 | 82.6 | | | 160.6 | 151.4 | | |
| EBIT Margin (%) | | | | | | | | | |
| Manufacturing | 9.6 | 6.3 | 7.3 | | | 9.7 | 6.8 | | Margin expanded QoQ from low base as sales picked up. |
| Property | 25.4 | 29.1 | 30 | | | 27.8 | 29.6 | | |

Source: Company, RHB

Figure 3: SOP-derived TP

| Divisions | Method | Valuation (MYRm) |
|---------------------------|--------------------------|------------------|
| Manufacturing | DCF (WACC:6.7%, TG:1.0%) | 3,103 |
| Property | RNAV (Discount of 40%) | 764.3 |
| Total Equity Value | | 3,867.3 |
| No. of shares (m) | | 460 |
| TP per share (MYR) | | 8.40 |
| Implied FY17F P/E | | 12.3 |

Source: RHB

Figure 4: Scientex's DCF valuation

| FYE Jul | FY17F | FY18F | FY19F | FY20F | FY21F | FY22F | FY23F | FY24F | FY25F | FY26F |
|-----------------------------------|-------------|------------|------------|------------|------------|------------|------------|------------|------------|------------|
| EBIT | 205 | 266 | 293 | 293 | 307 | 307 | 315 | 308 | 313 | 311 |
| EBIT x (1-Tax) | 156 | 202 | 223 | 223 | 233 | 234 | 239 | 234 | 238 | 236 |
| Add: D&A | 46 | 49 | 56 | 66 | 71 | 76 | 81 | 69 | 68 | 66 |
| Less: Capex | -50 | -60 | -65 | -80 | -80 | -75 | -75 | -70 | -70 | -70 |
| Less: WC requirements | -56 | -45 | -27 | 4 | -9 | -6 | -9 | -13 | -12 | -2 |
| Unlevered FCF | 96 | 147 | 187 | 213 | 214 | 229 | 236 | 221 | 224 | 230 |
| PV of unlevered FCF | 90 | 129 | 154 | 164 | 155 | 155 | 150 | 132 | 126 | 121 |
| Sum of PV of unlevered FCF | 1377 | | | | | | | | | |

| | |
|-----------------------------|--------------|
| Terminal value | 4,119 |
| PV of Terminal value | 2,164 |
| Enterprise value | 3,540 |
| Less: net debt | 437 |
| Equity value | 3,103 |

| | |
|--------------------------|-------|
| Risk-free | 4.2% |
| Beta | 0.6 |
| Equity Risk Premium | 5.1% |
| Cost of Equity | 7.4% |
| Cost of Debt (after tax) | 3.8% |
| WACC | 6.7% |
| Tax rate | 24.0% |
| Terminal growth | 1.0% |

| | |
|-------------------------------|-------------|
| Equity value per share | 6.75 |
|-------------------------------|-------------|

| | |
|--------------------------------|------|
| Implied Manufacturing PE FY17F | 21.9 |
|--------------------------------|------|

Source: RHB estimates

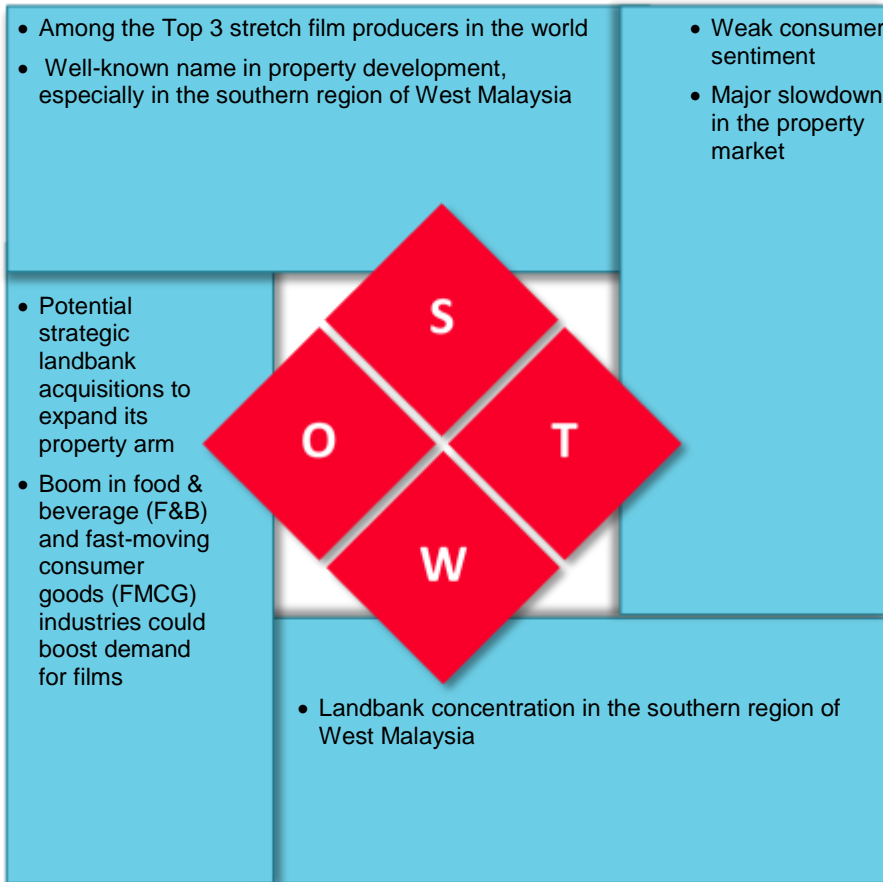
Figure 5: Peer comparison

| NAME | Bloomberg Ticker | Price (MYR) | Mkt Cap (MYRm) | | P/E | DY | ROE | P/BV | 1-yr fwd NP growth | 2-yr fwd NP growth | TP (MYR) | Rating | |
|---------------------------|------------------|-------------|----------------|-------------|-------------|-----------|-----------|------------|--------------------|--------------------|------------|--------|-----|
| | | | | Hist. | 1-yr fwd | 2-yr fwd | (%) | (%) | (x) | (%) | (%) | | |
| Plastics packaging | | | | | | | | | | | | | |
| SCGM | SCGM MK | 3.73 | 541.6 | 26.8 | 23 | 18.9 | 2% | 18% | 4.88 | 16% | 22% | NR | NR |
| Daibochi | DPP MK | 2.46 | 671.6 | 27.4 | 21.3 | 18.7 | 2% | 13% | 3.55 | 29% | 14% | NR | NR |
| SLP Resources | SLPR MK | 2.60 | 643 | 22.5 | 17.6 | 13.3 | 2% | 22% | 4.90 | 28% | 33% | NR | NR |
| Simple average | | | | 25.6 | 20.6 | 17 | 2% | 18% | 4.44 | 24% | 23% | | |
| Scientex | SCI MK | 7.25 | 3,335 | 13.8 | 10.6 | 8.8 | 3% | 19% | 2.69 | 31% | 21% | 8.40 | BUY |

Note: Data as of 22 Mar 2017

Source: RHB

SWOT Analysis



Recommendation Chart



Source: RHB, Bloomberg

| Date | Recommendation | Target Price | Price |
|------------|----------------|--------------|-------|
| 2016-09-27 | Buy | 7.8 | 6.5 |
| 2016-03-23 | Buy | 14.5 | 6.3 |
| 2016-03-18 | Buy | 13.1 | 6.0 |
| 2015-12-18 | Buy | 10.7 | 4.8 |
| 2015-09-30 | Buy | 8.3 | 3.6 |
| 2015-08-06 | Buy | 8.8 | 3.8 |
| 2015-06-30 | Buy | 7.9 | 3.4 |
| 2015-03-24 | Buy | 8.2 | 3.3 |
| 2014-12-18 | Buy | 8.6 | 3.5 |
| 2014-09-25 | Buy | 8.6 | 3.5 |

Source: RHB, Bloomberg

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