

COMPANY UPDATE

Scientex (SCI MK)

Fulfilling Its 2028 Aspiration

Scientex has proposed to acquire 42% of Daibochi through the issuance of one new Scientex share for every 5.5 Daibochi shares. We are positive on the acquisition as Scientex embarks on a 10-year expansion plan to increase its manufacturing capacity to 1m MT p.a. (from 450,000 MT currently). The share swap would have minimal earnings dilution with potential synergies for the duo. Maintain BUY. Target price: RM10.41.

WHAT'S NEW

- Proposed acquisition of 42.4% of Daibochi via issuance of new shares.** Scientex has entered into a heads of agreement (HOA) with certain shareholders of Daibochi (vendors) for the proposed acquisition of 139.1m shares (or 42.4% of issued and paid up capital). This translates into a purchase consideration of RM222.5m, or RM1.60 per Daibochi share. The deal will be satisfied via the issuance of 25.3m new Scientex shares at an indicative price of RM8.80.
- Salient terms of the HOA.** The conditional share sale agreement will be satisfied via a share swap of 1 new Scientex share for 5.5 Daibochi shares held by the vendors. Once the share sale turns unconditional, Scientex is obliged to launch a mandatory takeover offer (MGO) to acquire the remaining shares and warrants in Daibochi. The proposed share sale is expected to be completed within six months from the date of execution of the conditional share sale agreement.
- Synergistic acquisition, minimal earnings dilution.** Clear synergies and Scientex's proven ability to enhance its acquired companies' growth overrides the slightly earnings-dilutive acquisition. While the acquisition cost is higher than in the past acquisitions (see table below), the earnings dilution is only 1.4% for the 42% stake.

SCIENTEX'S CURRENT AND PAST ACQUISITIONS

	PE (x)	P/B (x)	EV/EBITDA (x)
GW plastic & GW Packaging	14.4	1.5	8.5
Seacera Polyfilms	14.0	n.a.	n.a.
Mondi Ipoh	20.7	1.6	6.4
Klang Hock Plastic Industries	10.6	1.7	8.4
Daibochi	20.0	2.6	n.a.

Source: Scientex, UOB Kay Hian

KEY FINANCIALS

Year to 31 Jul (RMm)	2017	2018	2019F	2020F	2021F
Net turnover	2,043	2,627	3,647	4,180	4,630
EBITDA	388	436	568	619	686
Operating profit	325	364	494	546	614
Net profit (rep./act.)	256	290	378	419	474
Net profit (adj.)	267	287	378	419	474
EPS (sen)	55.2	59.5	78.2	86.7	98.0
PE (x)	15.7	14.6	11.1	10.0	8.8
P/B (x)	2.7	2.4	2.1	1.8	1.6
EV/EBITDA (x)	13.1	11.6	8.9	8.2	7.4
Dividend yield (%)	1.9	2.1	2.7	3.0	3.4
Net margin (%)	12.5	11.0	10.4	10.0	10.2
Net debt/(cash) to equity (%)	18.0	43.2	14.7	10.4	(3.6)
Interest cover (x)	27.7	40.6	20.1	21.7	24.1
ROE (%)	18.9	17.6	19.9	19.3	19.1
Consensus net profit	-	-	339	378	426
UOBKH/Consensus (x)	-	-	1.12	1.11	1.11

Source: Scientex, Bloomberg, UOB Kay Hian

BUY

(Maintained)

Share Price	RM8.67
Target Price	RM10.41
Upside	+20.0%

COMPANY DESCRIPTION

Scientex is one of the largest industrial packaging companies in the world and a niche property developer in Southern Malaysia.

STOCK DATA

GICS sector	Materials
Bloomberg ticker:	SCI MK
Shares issued (m):	488.9
Market cap (RMm):	4,239.0
Market cap (US\$m):	1,011.1
3-mth avg daily t'over (US\$m):	0.6

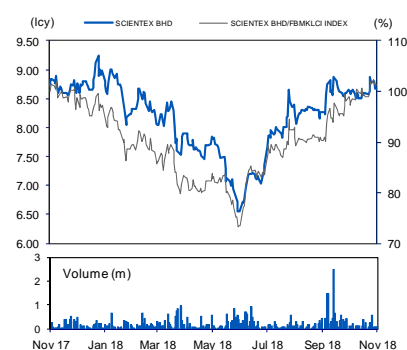
Price Performance (%)

52-week high/low	RM9.25/RM6.55			
1mth	3mth	6mth	1yr	YTD
0.8	3.8	12.6	(2.6)	0.1

Major Shareholders

	%
Scientex Holdings Sdn Bhd	21.37
Scientex Leasing Sdn Bhd	9.65
Scientex Infinity Sdn Bhd	8.39
FY19 NAV/Share (RM)	4.19
FY19 Net Debt/Share (RM)	0.62

PRICE CHART



Source: Bloomberg

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STOCK IMPACT

- Potential outcome of MGO.** Assuming the share sale agreement turns unconditional, the proposed MGO is expected to be completed within two months. There are two possible ways of undertaking the MGO, namely cash or share issuance. Should Scientex opt to fund the MGO via cash, it has to pay additional RM308m for the remaining 58% stake and incur RM15.3m in interest cost; while a share swap deal would essentially further dilute its earnings marginally by around 1.6%. Note that we assume the cost of Daibochi's warrants is close to zero at this juncture, given that the exercise price is well above the current share price. Nevertheless, we are not ruling out the possibility that the MGO will not be successful, given the RM1.60 price tag for Daibochi's shares, which is 20% below its last trading price.
- A synergistic acquisition...** The acquisition of Daibochi allows Scientex to tap on the former's strong MNC clientele in the F&B and FMCG sectors, ie Nestle, Mondelez International and PepsiCo. Presently, Scientex is a supplier of BOPP plastic packaging to Daibochi and does not have direct access to Daibochi's MNC clients. Note that Daibochi's manufacturing facilities are located in Melaka (Malaysia) and Yangon (Myanmar) and we believe there are vast opportunities for the enlarged entity to enjoy synergies from operational efficiency and product innovations. We believe the group would also benefit from the growing flexible plastic packaging (FPP) industry. Note that the global FPP market is projected to grow from US\$151.1b in 2014 to US\$192.2b by 2019 with a CAGR of 4.9%.
- ...made more possible with Scientex's successful acquisition record.** Scientex's past acquisitions had benefitted both the acquirer and acquiree. Among the acquisitions were: a) GW Plastic & GW Packaging which led to Scientex's first foray into the consumer packaging space; b) Seacera Polyfilms which enabled Scientex to venture into BOPP; and c) Mondi Ipoh and KHPI which added new customers to the group. Over time, Scientex rapidly expanded its acquirees' manufacturing capacities. Currently, Scientex's custom film capacity has increased to 230,000MT p.a. with stretch film reaching capacity of 170,000MT p.a.
- Daibochi registered record quarterly earnings.** Daibochi announced its 3Q18 results yesterday with revenue and core net profit rising 7% and 11% yoy respectively (see RHS table). This was mainly attributed to: a) higher sales from Malaysia, driven by demand from the ANZ region; and b) marginal improvement from the Myanmar division. That said, raw material costs increased significantly, which led to EBITDA falling 26% yoy. Going forward, Daibochi aspires to: a) increase Daibochi Myanmar sales by more than double, amid increasing its exports to cost-sensitive customers and major domestic consumer brands; and b) higher contribution from a MNC in the ANZ region since the commencement of a contract on Apr 18.

EARNINGS REVISION/RISK

- None.

VALUATION/RECOMMENDATION

- Maintain BUY and target price of RM10.41**, implying 12x FY20F PE. Although our target PE multiple is above mean valuation, the stock is still trading at a big discount to companies that have good earnings growth visibility and strong track records, and are trading at well above +1SD their respective mean PEs. The acquisition of Daibochi is in line with Scientex's intention to increase its manufacturing capacity to 1m MT p.a. (currently 450,000MT) and build 50,000 homes (currently 17,000) by FY28.

DAIBOCHI'S 3Q18 RESULTS

Year to 31 Dec (RMm)	3Q18	qoq % chg	yoy % chg	9M18	roy % chg
Turnover	109.2	2.6	7.0	320.3	13.2
EBITDA	10.9	3.2	(26.0)	34.2	(6.6)
Operating Profit	7.4	4.1	(34.3)	23.8	(9.6)
Core Net Profit	7.8	17.4	11.5	22.6	16.4
Margins (%)					
EBIT	6.7	0.1	(4.2)	7.4	(1.9)
Effective tax rate (%)	8.4	(11.7)	(17.4)	15.4	(9.0)
Core Net Profit	7.2	0.9	0.3	7.1	0.2

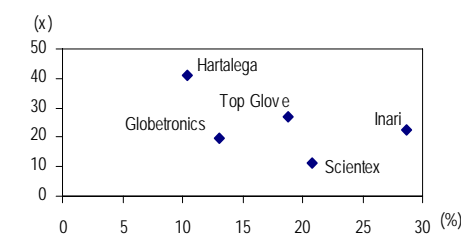
Source: UOB Kay Hian

SCENARIO ANALYSIS ON THE ACQUISITION

	Current at 42%	Full MI Acceptance All Cash	All Shares
EPS (sen)	0.76	0.77	0.75
PE (x)	11.4	11.3	11.6
Net Gearing (%)	0.41	0.56	0.40
Net Debt/EBITDA (X)	1.6	2.3	1.6

Source: UOB Kay Hian

PE VS 2-YEAR CAGR OF EXPORT ORIENTED GROWTH COMPANIES



Source: Bloomberg, UOB Kay Hian

PROFIT & LOSS

Year to 31 Jul (RMm)	2018	2019F	2020F	2021F
Net turnover	2,627	3,647	4,180	4,630
EBITDA	436	568	619	686
Deprec. & amort.	72	73	73	72
EBIT	364	494	546	614
Associate contributions	8	8	8	8
Net interest income/(expense)	(11)	(28)	(29)	(29)
Pre-tax profit	362	474	526	594
Tax	(68)	(90)	(100)	(113)
Minorities	(4)	(6)	(6)	(7)
Net profit	290	378	419	474
Net profit (adj.)	287	378	419	474

CASH FLOW

Year to 31 Jul (RMm)	2018	2019F	2020F	2021F
Operating	392	578	243	542
Pre-tax profit	362	474	526	594
Tax	(80)	(90)	(100)	(113)
Deprec. & amort.	72	73	73	72
Working capital changes	31	121	(255)	(12)
Other operating cashflows	8	0	0	1
Investing	(703)	(80)	(60)	(60)
Capex (growth)	(65)	(80)	(60)	(60)
Investments	(147)	0	0	0
Proceeds from sale of assets	0	0	0	0
Others	(491)	0	0	0
Financing	291	(18)	(127)	(145)
Dividend payments	(58)	(113)	(126)	(142)
Issue of shares	0	0	0	1
Proceeds from borrowings	365	0	0	1
Loan repayment	0	16	0	0
Others/interest paid	(16)	79	(1)	(5)
Net cash inflow (outflow)	(20)	480	56	337
Beginning cash & cash equivalent	192	172	652	709
Changes due to forex impact	0	0	0	0
Ending cash & cash equivalent	172	652	709	1,046

BALANCE SHEET

Year to 31 Jul (RMm)	2018	2019F	2020F	2021F
Fixed assets	1,151	1,150	1,137	1,126
Other LT assets	1,018	1,015	1,016	1,017
Cash/ST investment	172	652	709	1,046
Other current assets	1,023	1,002	1,237	1,318
Total assets	3,364	3,819	4,099	4,506
ST debt	610	650	650	650
Other current liabilities	514	683	663	732
LT debt	324	300	300	300
Other LT liabilities	82	82	82	82
Shareholders' equity	1,764	2,028	2,322	2,654
Minority interest	70	76	82	89
Total liabilities & equity	3,364	3,819	4,099	4,507

KEY METRICS

Year to 31 Jul (%)	2018	2019F	2020F	2021F
Profitability				
EBITDA margin	16.6	15.6	14.8	14.8
Pre-tax margin	13.8	13.0	12.6	12.8
Net margin	11.0	10.4	10.0	10.2
ROA	9.8	10.5	10.6	11.0
ROE	17.6	19.9	19.3	19.1
Growth				
Turnover	28.6	38.8	14.6	10.8
EBITDA	12.3	30.2	9.0	10.9
Pre-tax profit	13.7	31.1	10.9	13.0
Net profit	13.3	30.5	10.9	13.0
Net profit (adj.)	7.7	31.5	10.9	13.0
EPS	7.7	31.5	10.9	13.0
Leverage				
Debt to total capital	33.8	31.1	28.3	25.7
Debt to equity	53.0	46.8	40.9	35.8
Net debt/(cash) to equity	43.2	14.7	10.4	(3.6)
Interest cover (x)	40.6	20.1	21.7	24.1

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