

COMPANY UPDATE

Scientex (SCI MK)

A Temporary Blip

Scientex has not been spared from the impact of COVID-19 as the MCO has reduced its manufacturing workforce by half and temporarily paused property development activities. Nevertheless, we foresee utilisation rate resuming post MCO and the affordability of its properties is expected to alleviate demand pressure from a broad-based slowdown in the economy. We reduce FY20 and FY21 earnings forecasts by 10% and 3% respectively while maintaining BUY with a lower target price of RM9.90.

WHAT'S NEW

- Manufacturing segment in compliance with minimum 50% workforce cut during MCO.** While Scientex falls under the list of manufacturers (of selected essential products) exempted from the movement control order (MCO), the government has imposed certain compulsory conditions to be fulfilled. Among others is the reduction of number of employees to a minimum level or by at least 50% of current registered employees. We gather that the group has cut its workforce by 50% across its manufacturing plants, in compliance with Ministry of International Trade and Industry's (MITI) direction.
- Drop in utilisation rate does not mirror workforce cut.** We do not expect Scientex's manufacturing utilisation rate to fall by half, buoyed by robust custom film and converting businesses amid relatively inelastic demand from consumer products-related packaging. Nevertheless, stretch film demand is expected to soften owing to the slow-down in global economic activities as the impact of COVID-19 unravels. Notably, Scientex stretch film, custom film and specialty products account for approximately 40%, 50% and 10% of the group's total capacity respectively.
- Property activities taking a pause during MCO.** Our channel checks suggest all property related activities have been temporarily halted during the MCO period, including property developments and showrooms. While Scientex's property offerings are mainly on affordable housing with approximately 60% of properties priced below RM200,000, we remain cautious that buyers would take a wait-and-see approach for big-ticket items. This would consequently impact its unbilled sales and progress billings recognition in the coming quarters. However, the group's high unbilled sales of RM740m as of 2QFY20 would provide a good buffer for its property segment in the coming quarters. The group is still maintaining its RM1.1b worth of properties launches for FY20.

KEY FINANCIALS

Year to 31 Jul (RMm)	2018	2019	2020F	2021F	2022F
Net turnover	2,603	3,247	3,694	4,347	5,324
EBITDA	429	554	626	710	827
Operating profit	357	462	532	603	708
Net profit (rep./act.)	285	334	367	448	543
Net profit (adj.)	284	353	367	448	543
EPS (sen)	58.8	72.9	84.1	95.7	112.6
PE (x)	13.2	10.6	9.2	8.1	6.9
P/B (x)	2.1	1.7	1.5	1.3	1.2
EV/EBITDA (x)	10.9	8.4	7.5	6.6	5.7
Dividend yield (%)	2.2	2.6	3.3	3.7	4.4
Net margin (%)	10.9	10.3	11.0	10.6	10.2
Net debt/(cash) to equity (%)	43.6	32.2	19.5	15.3	10.8
Interest cover (x)	39.9	35.7	40.0	45.9	53.4
ROE (%)	17.4	16.8	17.2	17.3	18.0
Consensus net profit	-	-	387	448	486
UOBKH/Consensus (x)	-	-	1.05	1.03	1.12

Source: Scientex, Bloomberg, UOB Kay Hian

BUY

(Maintained)

Share Price	RM7.75
Target Price	RM9.90
Upside	+37.7%
(Previous TP)	RM10.67

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):	515.9
Market cap (RMm):	3,998.0
Market cap (US\$m):	921.4
3-mth avg daily t'over (US\$m):	0.8

Price Performance (%)

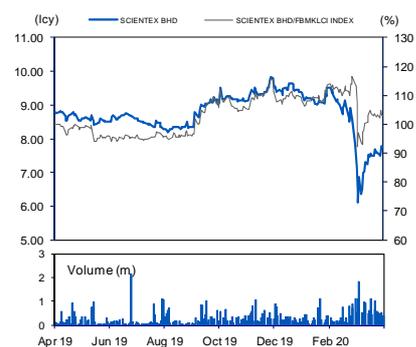
52-week high/low	RM9.84/RM6.09			
1mth	3mth	6mth	1yr	YTD
(8.7)	(17.6)	(15.5)	(9.6)	(18.0)

Major Shareholders

-	-
-	-
-	-

FY20 NAV/Share (RM)	5.19
FY20 Net Debt/Share (RM)	1.01

PRICE CHART



Source: Bloomberg

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- Low resin costs to sustain.** Resin prices have continued to come off gradually mainly due to: a) COVID-19, as global growth tapers; and b) a low oil price environment. Note that Scientex would partially benefit from lower resin prices, particular on custom films which have a longer lead time of about 3 months vs stretch film's 4-6 weeks. Based on our back-of-the-envelope calculations, a 1% drop in resin cost will translate into savings of 0.4%.
- Resilient supply chain amid COVID-19.** We gather that Scientex's supply chain is not impacted by COVID-19 so far, as resin, which accounts for approximately 80% of its manufacturing raw material, is considered an essential item to be produced.

STOCK IMPACT

- Manufacturing faced temporary pressure from MCO but to recover eventually.** We opine that demand for Scientex's manufacturing would recover gradually beyond 3QFY20 when its operations/workforce are fully back on track. Management alluded that the group intends to achieve utilisation rate of 70% in FY20 (FY19: 60%), driven by: a) full-year contribution from Daibochoi and MPP; and b) ramp-up at the biaxially-oriented polypropylene (BOPP) and new stretch film plant in Arizona. Meanwhile, the group is looking to diffuse production bottlenecks at some of its factories, primarily the stretch film (+10% of existing capacity), printing and laminating plants.
- A first mover on the sustainability bandwagon.** A beneficiary of the rising environmental, social and governance (ESG) trend, Scientex (via subsidiary Diabochi) is expanding its monolamination packaging production (first launched in 4Q19) which fits into the F&B manufacturing MNCs' overarching packaging policy. The group is expected to reap first-mover advantages, such as higher ASP and order volume. Note that its stretch film is already in compliance with the sustainable packaging standards, and management is in the final stage of developing sustainable custom films and targeting for product commercialisation as soon as 2020.

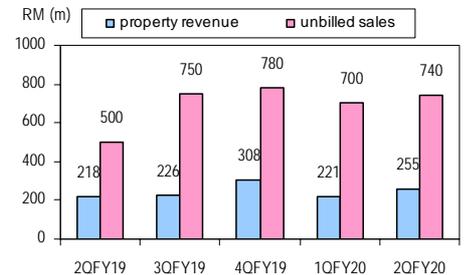
EARNINGS REVISION/RISK

- We cut Scientex's FY20 and FY21 earnings forecasts by 10% and 3% respectively** as we adjust for billings recognition of the property segment's forecasted unbilled sales and lower the manufacturing division's utilisation rate to 55% (from currently 65%) during the period of the MCO. Beyond the MCO, we foresee utilisation rate at its manufacturing plants resuming smoothly and the affordability of its range of property offerings is expected to alleviate demand pressure from a broad-based slowdown in the economy.
- We still expect earnings to grow 4% yoy in FY20 supported by: a) stronger utilisation rate across manufacturing plants, b) consolidation of newly-acquired companies, and c) high unbilled sales at its property segment.

VALUATION/RECOMMENDATION

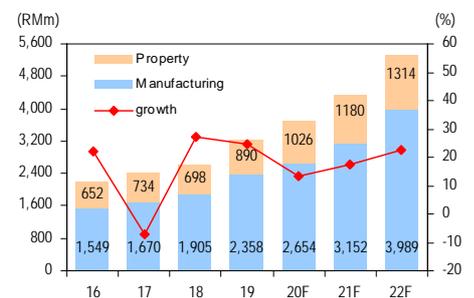
- Maintain BUY with a lower target price of RM9.90** (previously RM10.67), based on 12x 2020F PE. Share price has dropped approximately 20% ytd. We still like the stock for its strong management team and track record, which enables the group to deliver record annual results year after year.

PROPERTY SEGMENT



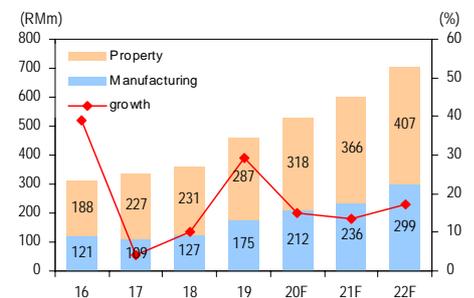
Source: Scientex, UOB Kay Hian

SALES BY SEGMENT



Source: Scientex, UOB Kay Hian

EBIT BY SEGMENT



Source: Scientex, UOB Kay Hian

PROFIT & LOSS

Year to 31 Jul (RMm)	2019	2020F	2021F	2022F
Net turnover	3,247	3,694	4,347	5,324
EBITDA	554	626	710	827
Deprec. & amort.	92	95	107	119
EBIT	462	481	584	707
Associate contributions	4	4	4	4
Net interest income/(expense)	(16)	(16)	(15)	(15)
Pre-tax profit	451	470	573	695
Tax	(105)	(99)	(113)	(132)
Minorities	(12)	(15)	(17)	(20)
Net profit	334	367	448	543
Net profit (adj.)	353	367	448	543

BALANCE SHEET

Year to 31 Jul (RMm)	2019	2020F	2021F	2022F
Fixed assets	1,248	1,483	1,676	1,858
Other LT assets	1,161	1,161	1,161	1,161
Cash/ST investment	258	461	518	604
Other current assets	1,441	1,309	1,513	1,816
Total assets	4,107	4,414	4,868	5,439
ST debt	704	650	650	650
Other current liabilities	626	657	770	938
LT debt	270	300	300	300
Other LT liabilities	109	109	109	110
Shareholders' equity	2,225	2,510	2,833	3,216
Minority interest	174	189	206	226
Total liabilities & equity	4,107	4,414	4,868	5,439

CASH FLOW

Year to 31 Jul (RMm)	2019	2020F	2021F	2022F
Operating	557	463	496	549
Pre-tax profit	451	520	592	697
Tax	(88)	(99)	(113)	(132)
Deprec. & amort.	82	95	107	119
Working capital changes	86	(54)	(91)	(135)
Other operating cashflows	26	0	0	1
Investing	(299)	(330)	(300)	(300)
Capex (growth)	(217)	(330)	(300)	(300)
Investments	(80)	0	0	0
Proceeds from sale of assets	3	0	0	0
Others	(5)	0	0	0
Financing	(173)	70	(139)	(162)
Dividend payments	(107)	(122)	(139)	(163)
Issue of shares	0	0	0	1
Proceeds from borrowings	31	0	0	1
Loan repayment	(65)	(24)	0	0
Others/interest paid	(32)	216	0	(1)
Net cash inflow (outflow)	85	203	57	86
Beginning cash & cash equivalent	172	258	461	518
Changes due to forex impact	0	0	0	0
Ending cash & cash equivalent	258	461	518	604

KEY METRICS

Year to 31 Jul (%)	2019	2020F	2021F	2022F
Profitability				
EBITDA margin	17.1	17.0	16.3	15.5
Pre-tax margin	13.9	14.1	13.6	13.1
Net margin	10.3	11.0	10.6	10.2
ROA	8.9	9.5	10.0	10.6
ROE	16.8	17.2	17.3	18.0
Growth				
Turnover	24.8	3.4	17.7	22.5
EBITDA	29.1	3.9	20.0	19.4
Pre-tax profit	27.0	4.2	21.9	21.4
Net profit	17.3	4.0	21.9	21.4
Net profit (adj.)	24.0	4.0	21.9	21.4
EPS	24.0	4.0	21.9	21.4
Leverage				
Debt to total capital	28.9	26.0	23.8	21.6
Debt to equity	43.8	37.9	33.5	29.5
Net debt/(cash) to equity	32.2	19.5	15.3	10.8
Interest cover (x)	35.7	40.0	45.9	53.4

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