

4Q FYE DEC 2016 RESULTS REPORT

23 February 2017

Name of PLC: Muda Holdings Berhad (Muda)		Target Price:	RM 2.80
Business Summary : Manufacturing of paper, corrugated carton and paper related products			
Major Shareholders :			
(as at 22-Mar-2016)		Hartaban Holdings Sdn Bhd	37.4%
		Asia File Corporation Bhd	20.0%
PLC Website : www.muda.com.my		Recommendation:	BUY
		Market Capitalisation:	RM 451.5m
		Current Price:	RM 1.48
		Market / Sector:	Industrial Products
		Stock Code:	3883
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Key Stock Statistics	2014	2015	2016	2017F
EPS (sen)	7.1	8.6	6.2	12.6
EPS ex-EI (sen)	7.1	12.2	10.0	12.6
P/E (x)	20.7	17.2	24.0	11.7
P/E ex-EI (x)	20.7	12.1	14.8	11.7
Net Dividend/Share (sen)	3.0	3.0	3.0	3.0
NTA/Share (RM)	2.64	2.72	2.76	2.85
Book Value/Share (RM)	2.67	2.76	2.79	2.89
Issued Capital (m shares)	305.1	305.1	305.1	305.1
52-weeks Share Price Range (RM)			1.40 - 2.50	

Per Share Data	2014	2015	2016	2017F
Year-end 31 Dec				
Book Value (RM)	2.67	2.76	2.79	2.89
Operating Cash Flow (sen)	23.9	26.4	25.2	30.6
EPS (sen)	7.1	8.6	6.2	12.6
Net Dividend/Share (sen)	3.0	3.0	3.0	3.0
Payout Ratio (%)	42.1	34.9	48.7	23.8
P/E (x)	20.7	17.2	24.0	11.7
P/Cash Flow (x)	6.2	5.6	5.9	4.8
P/Book Value (x)	0.6	0.5	0.5	0.5
Dividend Yield (%)	2.0	2.0	2.0	2.0
ROE (%)	2.7	3.2	2.2	4.4
Net Gearing (%)	55.7	50.4	51.8	46.3

P&L Analysis (RM mil)	2014	2015	2016	2017F
Revenue	1,051.57	1,124.85	1,217.75	1,284.02
EBITDA	114.52	130.64	125.99	139.02
Depreciation & amort	(57.25)	(54.05)	(58.09)	(58.93)
Net interest income	(25.28)	(25.03)	(24.35)	(23.55)
Associate	2.71	0.53	(0.29)	0.50
EI	-	(10.96)	(11.77)	-
Pre-tax Profit	34.70	41.14	31.49	57.04
Tax	(10.15)	(12.91)	(10.65)	(16.54)
Minority interest	(2.80)	(1.98)	(2.03)	(2.00)
Net Profit	21.76	26.26	18.81	38.50
EBITDA Margin (%)	10.9	11.6	10.3	10.8
Pre-tax Margin (%)	3.3	3.7	2.6	4.4
Net-Margin (%)	2.1	2.3	1.5	3.0

1. 4QFY16 Results Highlight

	4Q FY16	4Q FY15	Chg
	RMm	RMm	%
Revenue	360.89	347.42	3.9
Operating Profit	21.09	25.31	(16.7)
Finance	(6.08)	(6.32)	(3.8)
Associate	(0.49)	(0.22)	117.4
Exceptional items	9.40	-	n.m.
Pre-tax Profit	23.92	18.76	27.5
Net Profit	17.91	9.86	81.7
Operating Margin (%)	5.8	7.3	
Pre-tax Margin (%)	6.6	5.4	
Net-Margin (%)	5.0	2.8	

- Turnover in 4QFY16 improved marginally by 3.9% to RM360.89m. Both PBT and net profit jumped by 27.5% and 81.7% to RM23.92m and RM17.91m respectively.
- However, stripping out progressive compensation payment by insurer amounting to RM9.40m, operating profit actually declined by 16.7% to RM21.09m in 4QFY16.

- In 4QFY16, its topline turnover growth was driven by better selling prices of industrial grade paper and paper packaging products. However, operating profit was lower due to higher operating expenses and prices of raw material which was cushioned by increase in average selling price (ASP) and improved productivity.
- Although its gross margin fell to 18.3% in 4QFY16 as compared with 21.4% in 4QFY15, this level of profitability was within historical range of 17-20%.
- In addition, there was a fire incident occurred at one of its paper mills in Tasek, Penang on 17-Aug-16. The fire destroyed three warehouses with finished goods and other assets such as forklifts, machinery and parts. Paper production lines at the plant were not affected in the fire and the plant resumed production on 19-Aug-2016. The total material damage caused by the fire has been ascertained at RM21.38m for write-off of inventories, warehouse and machinery. The first progressive payment from insurer amounting to RM10m was received on 30-Nov-16. After accounting for some write-off and expenses pertaining to the fire incident, Muda booked in an exceptional gain of RM9.40m in 4QFY16. For full year FY16, the total net loss relating to the fire incident amounted to RM11.77m. The second progressive payment amounting to RM13m was received on 17-Feb-17. The final claim for compensation is still pending.
- Excluding the exceptional gain due to the fire incident, Muda would have recorded a PBT ex-EI of RM14.52m (4QFY16) as compared with RM18.76m (4QFY15). The lower PBT was attributed to the unusual high profitability experienced in 4QFY15. On a sequential basis, PBT in 4QFY16 of RM14.52m was a marked improvement as compared with RM6-7m recorded in 2QFY16 and 3QFY16.

FY16 Results Highlight

	FY16	FY15	Chg
	RMm	RMm	%
Revenue	1,217.75	1,124.85	8.3
Operating Profit	68.49	77.29	(11.4)
Finance	(24.94)	(25.73)	(3.0)
Associate	(0.29)	0.53	(154.5)
Exceptional items	(11.77)	(10.96)	7.4
Pre-tax Profit	31.49	41.14	(23.5)
Net Profit	18.81	26.26	(28.4)
Operating Margin (%)	19.0	22.2	
Pre-tax Margin (%)	8.7	11.8	
Net-Margin (%)	5.2	7.6	

- For full year FY16, Muda recorded an impressive turnover growth of 8.3% to RM1.2b due to ASP hike and higher sales volume. Operating profit declined by 11.4% to RM68.49m in FY16.
- The demand for industrial grade paper at its paper milling operations was steady in FY16. Its turnover growth was mainly driven by ASP hike (+8.2%) due to weak ringgit and tight supply of industrial grade paper in China. The tight supply situation in China was attributed to weak RMB and shortage of supply due to closure of mills in China. This put pressure on downstream paper packaging customers to increase local sourcing of industrial paper from manufacturers such as Muda.
- Muda’s inhouse downstream paper packaging manufacturing was not spared from higher paper costs and more intense market competition.
- Profitability at group manufacturing was reduced in FY16 due to the impact of higher energy cost arising from a gas tariff hike of 17% and 5.95% each effective from 1-Jan-16 and 15-Jul-16, as well as higher raw material cost due to tight supply of recovered paper. The impact was partially mitigated by ASP hike and improved productivity.
- Gross margin declined to 17.6% (FY16) from 18.5% (FY15). Consequently, operating profit also declined by 11.4% to RM68.49m in FY16.

- In FY16, Muda incurred a net exceptional expense of RM11.77m relating to the fire incident, while expenses related to forex and impairment came in at RM10.96m in FY15. The second progressive payment amounting to RM13m was received on 17-Feb-17. The final claim for compensation is still pending.

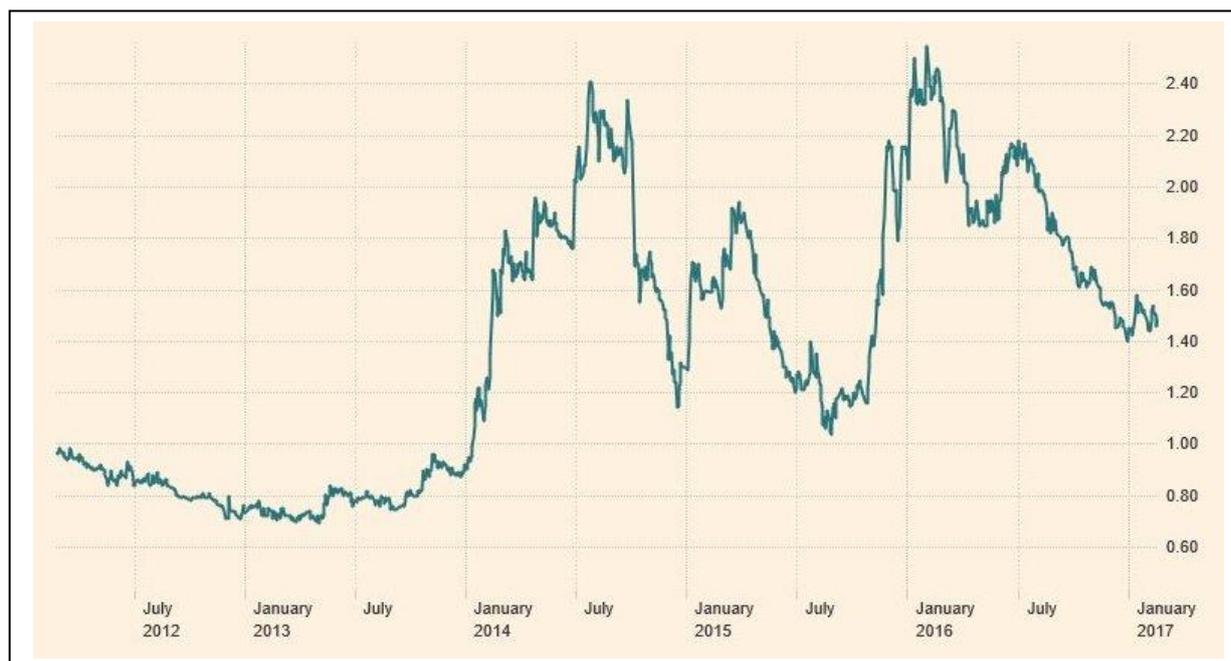
2. Earnings Outlook

- Muda is one of the largest integrated paper mill and corrugated plants in Malaysia. Its principal activities comprise manufacturing of industrial paper, corrugated carton, paper-related products such as paper-based stationery and food packaging, as well as trading of imported paper for the domestic market.
- Its paper milling plants have a combined production capacity of 475,000 tonnes per annum, which is the largest in Malaysia in terms of capacity of industrial paper.
- Demand for paper products will be steadily growing underpinned by domestic consumption, manufacturing activities and external export growth. Historically, the demand growth is tied to Malaysia's GDP growth. Additional growth is underpinned by import substitution as Malaysia is still a net importer of paper products. The weakening ringgit and supply shortage in China will benefit locally-based Muda.
- Due to the high cost of start-up and shut-down and to ensure consistency in paper quality, paper milling plant is always running at 100%. Its profitability can be sustainable as production output is maintained at high level of 80-90%. In the short-term, its profitability at milling operations can be sustained due to tight supply situation despite the higher energy costs. The benefits from higher production utilisation and productivity improvement through upgrading of machinery and processes would mitigate the impact of higher production cost.
- While the manufacturing of industrial grade paper commands some competitive advantages, its downstream carton manufacturing is faced with higher price of raw material, higher energy costs and intense competition in the carton industry.
- As part of its product diversification plan into higher-value products, Muda has expanded into the manufacturing of machine-glazed paper for food packaging. First phase, which involves the installation of 1 new line, has commenced commercial production in 3QFY16. It has an annual production capacity of 18,000 tonnes.
- In addition, Muda has incurred a capex of RM50m for new machinery from Germany and plant extension to double the carton capacity in its Kajang factory to 6,000 mt/month. As it gradually ramps up production, a more meaningful contribution can only be expected towards the later part of 2017.

3. Valuation and Recommendation

- We like Muda for its unique value proposition in terms of a sizeable integrated operation ranging from wastepaper collection, upstream milling and downstream paper packaging operations, which cannot be easily replicated. The integrated synergies and economies of scale position the group in a competitive position in terms of inventory control, better cost control, reliable packaging solution and on-time deliveries to its customers
- Muda also has a market leading position in the production of industrial paper in Malaysia. Against the backdrop of steady consumption growth and import substitution, the demand for industrial paper will always be growing at a steady growth rate.
- We are keeping our Buy recommendation on the stock. At the current share price of RM1.48, it's trading at about half of its book value of RM2.79. The stock is currently trading at P/E of 14.8x and 11.7x for FY16 and FY17.

Share Price Chart



Disclosures/Disclaimer

Investment ratings:

Buy (generally >10% upside over the next 12 months)

Hold (generally negative 10% downside to positive 10% upside over the next 12 months)

Sell (generally >10% downside over the next 12 months)

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