

3Q FYE DEC 2016 RESULTS REPORT

15 November 2016

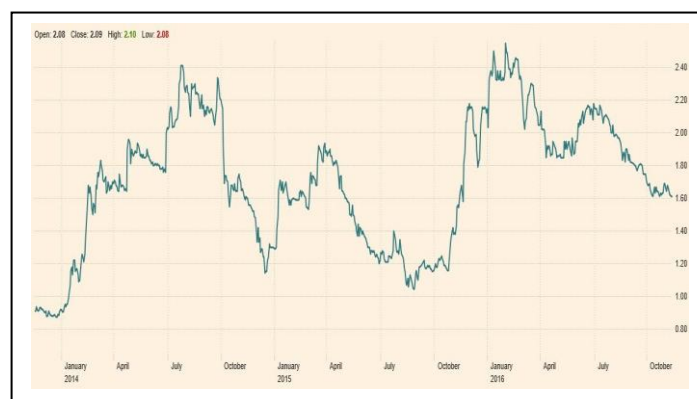
Name of PLC: Muda Holdings Berhad (Muda)	Target Price:	RM 2.80
Business Summary : Manufacturing of paper, corrugated carton and paper related products		
Major Shareholders : (as at 22-Mar-2016)	Hartaban Holdings Sdn Bhd Asia File Corporation Bhd	37.4% 20.0%
PLC Website : www.muda.com.my	Recommendation:	BUY
	Market Capitalisation:	RM 491.1m
	Current Price:	RM 1.61
	Market / Sector:	Industrial Products
	Stock Code:	3883
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Key Stock Statistics	2014	2015	2016F	2017F
EPS (sen)	7.1	8.6	12.4	12.7
EPS ex-EI (sen)	7.1	12.2	12.4	12.7
P/E (x)	22.6	18.7	13.0	12.7
P/E ex-EI (x)	22.6	13.2	13.0	12.7
Net Dividend/Share (sen)	3.0	3.0	3.0	3.0
NTA/Share (RM)	2.64	2.72	2.82	2.92
Book Value/Share (RM)	2.67	2.76	2.85	2.95
Issued Capital (m shares)	305.1	305.1	305.1	305.1
52-weeks Share Price Range (RM)			1.58 - 2.60	

Per Share Data	2014	2015	2016F	2017F
Year-end 31 Dec				
Book Value (RM)	2.67	2.76	2.85	2.95
Operating Cash Flow (sen)	23.9	26.4	28.1	28.9
EPS (sen)	7.1	8.6	12.4	12.7
Net Dividend/Share (sen)	3.0	3.0	3.0	3.0
Payout Ratio (%)	42.1	34.9	24.2	23.6
P/E (x)	22.6	18.7	13.0	12.7
P/Cash Flow (x)	6.7	6.1	5.7	5.6
P/Book Value (x)	0.6	0.6	0.6	0.5
Dividend Yield (%)	1.9	1.9	1.9	1.9
ROE (%)	2.7	3.2	4.4	4.4
Net Gearing (%)	55.7	50.4	47.0	43.3

P&L Analysis (RM mil)	2014	2015	2016F	2017F
Revenue	1,051.57	1,124.85	1,189.72	1,255.00
EBITDA	114.52	130.64	134.33	135.62
Depreciation & amort	(57.25)	(54.05)	(54.81)	(55.07)
Net interest income	(25.28)	(25.03)	(23.94)	(23.55)
Associate	2.71	0.53	0.50	0.50
EI	-	(10.96)	-	-
Pre-tax Profit	34.70	41.14	56.09	57.49
Tax	(10.15)	(12.91)	(16.27)	(16.67)
Minority interest	(2.80)	(1.98)	(2.00)	(2.00)
Net Profit	21.76	26.26	37.82	38.82
EBITDA Margin (%)	10.9	11.6	11.3	10.8
Pre-tax Margin (%)	3.3	3.7	4.7	4.6
Net-Margin (%)	2.1	2.3	3.2	3.1

Share Price Chart



1. 3QFY16 Results Highlight

	3Q FY16 RMm	3Q FY15 RMm	Chg %
Revenue	281.58	261.04	7.9
Operating Profit	12.72	14.67	(13.3)
Finance	(6.52)	(6.37)	2.5
Associate	0.33	0.25	29.0
Exceptional items	(21.38)	-	n.m.
Pre-tax Profit	(14.86)	8.56	n.m.
Net Profit	(15.76)	7.45	n.m.
Operating Margin (%)	4.5	5.6	
Pre-tax Margin (%)	(5.3)	3.3	
Net-Margin (%)	(5.6)	2.9	

- In 3QFY16, although turnover increased by 7.9% to RM281.58m, Muda turned into a pretax loss of RM14.86m due mainly to write-off relating to a fire incident.

- The topline growth in 3QFY16 was underpinned by higher selling price and higher demand for industrial grade paper. The rising demand was driven by increased local sourcing of industrial paper by Malaysia-based customers to curtail the forex risk arising from depreciating ringgit and over-stocking.
- Operationally, its profitability was slightly lower in 3QFY16 as shown in the lower gross margin of 15.5% (3QFY16) as compared with 17.8% (3QFY15) 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 higher selling price and higher efficiency.
- 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. Filing of claims for compensation with insurer is currently in progress.
- Operationally, operating profit only declined by 13.3% to RM12.72m in 3QFY16 due to higher manufacturing cost. Excluding the write-off due to fire incident, Muda would have recorded a PBT ex-EI of RM6.52m (3QFY16) as compared with RM8.56m (3QFY15).
- In 3QFY16, its manufacturing division saw 6.7% growth in turnover to RM250.40m. This was driven by increased local sourcing of industrial grade paper by Malaysia-based customers due to competitive pricing against imported paper arising from cheaper ringgit. It also benefited from higher selling price. However, its downstream paper packaging segment, the carton manufacturing in particular was faced with softened market and intense competition.
- EBIT (ex-EI) of manufacturing division was 12.2% lower at RM14.89m due to higher energy and raw material costs.
- Its trading division, which is involved in trading of imported papers and stationery products, grew the turnover by 18.3% to RM31.14m in 3QFY16 due to increase in the purchase price of recovered paper. It reported a small EBIT of RM0.07m (3QFY16) as compared with RM0.68m (3QFY15).
- Muda reported a pretax and net loss of RM14.86m and RM15.76m in 3QFY16 due mainly to write-off associated with the fire incident.

9MFY16 Results Highlight

	9M FY16	9M FY15	Chg
	RMm	RMm	%
Revenue	856.87	777.43	10.2
Operating Profit	47.62	41.03	16.1
Finance	(18.86)	(19.41)	(2.8)
Associate	0.20	0.76	(73.9)
Exceptional items	(21.38)	-	n.m.
Pre-tax Profit	7.57	22.38	(66.2)
Net Profit	0.89	16.40	(94.5)
Operating Margin (%)	16.9	15.7	
Pre-tax Margin (%)	2.7	8.6	
Net-Margin (%)	0.3	6.3	

- In 9MFY16, turnover grew by 10.2% to RM856.87m due to increased local sourcing by customers and better selling price.
- However, it reported a substantially lower PBT of RM7.57m in 9MFY16 due mainly to write-off related to fire incident. Excluding this, PBT would have been RM28.95m for 9MFY16 as compared with RM22.38m for 9MFY15.

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 which is around 5-6%. In addition, additional growth is underpinned by import substitution as Malaysia is still a net importer of paper products. Against the backdrop of a weakening ringgit, locally-based Muda is poised to benefit from more competitive pricing against imported papers.
- 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 has come under some pressure due to tight supply of recovered paper, resulting in higher cost of raw materials as well as 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 softened market 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. The capacity expansion is expected to complete towards end of 2016. As it gradually ramps up production, a more meaningful contribution can only be expected towards the later part of 2017.

3. Valuation and Recommendation

- 9MFY16's reported earning is below our forecast due mainly to write-off and seasonally slower 3Q. Due to seasonal variation in the sales of stationery products in Singapore, its trading division usually records the highest turnover and profits in 4Q. As such, we are maintaining our earnings forecast.
- 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 RM1.61, it's trading at a discount to its book value of RM2.73. The stock is currently trading at P/E of 13.0x and 12.7x for FY16 and FY17.

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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