

27 September 2019

## SCGM Berhad

### Focused On Improving Margins

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We came away from SCGM's briefing comforted by management's determination on improving margins by reviewing product mix. Additionally, management does not expect any further cost impairments or write-downs from moving to the new factory, and can focus on improving efficiency through automation and economies of scale. We increase FY20-21E CNP to RM9.6-14.2m (from RM7.7-9.3m) on improved topline and margins. Maintain MP with a higher TP of RM1.20 (from RM1.05).

#### Results above and may continue to improve in coming quarters.

To recap, 1Q20 YoY topline was flattish, but EBIT margin saw marked improvement, increasing to 6.4% (vs. 4.9% in 1Q19, and -6.4% in 4Q19). However, given that SCGM has fully moved in to a new factory in April 2019 (4Q19), the Group can now focus on improving topline and margins by increasing utilization rates, targeting to achieve 70% by end FY20 (from c.60% currently)

**Improving margins on better efficiency and product mix.** Post briefing, we felt slightly more comforted on project EBIT margins going forward given that the company is taking active steps to review the product mix, amidst the backdrop of low resin prices. Apart from lower resin cost mentioned in 1Q20 results, the better EBIT margin was attributable to: (i) improved efficiency after moving into a new factory and (ii) review of product mix by aggressively marketing and increasing production of higher margin products. Additionally, management does not foresee any impairment, write-off or additional cost from moving to the new factory going forward.

**Outlook.** The group will focus on increasing its sales of F&B packaging in both the local and export markets and aims to introduce more degradable and biodegradable plastic packaging products. Meanwhile, the group has fully moved to the Kulai Plant, boosting production capacity to 67.6k MT/year (from c.41.0k MT/year). We expect SCGM to increase utilisation rates and improve efficiency through automation and economies of scale from the new factory and assume maintenance capex of RM15-15m for FY20-21.

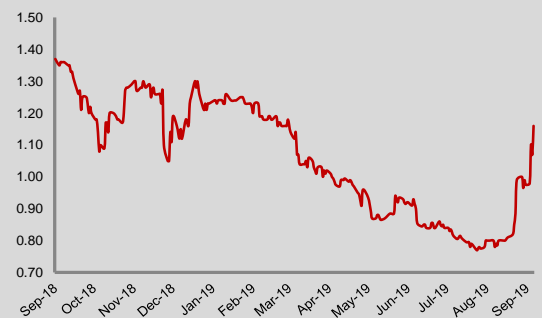
All in, we increase FY20-21E CNP by 24-53% to RM9.6-14.2m. This is on a higher utilization rate of 60-70% in FY20-21 (from 55-60%) as management targets to increase utilization to 70% by end FY20. We believe its margins would be able to improve from here on as management is taking active steps to review their product mix. As such, we increase FY20-21E EBIT margin by +0.3-0.9ppt to 6.6-8.0% and will continue to monitor margin trend in coming quarters. We also lower our FY20E effective tax rate to 15% (from our 20% estimate) in line with expectations of low tax rates from capital allowance. FY20-21E dividends are based on a 40% payout ratio of 2.0-2.9 sen, implying 1.7-2.5% yield.

**Maintain MARKET PERFORM with a higher Target Price of RM1.20 (from RM1.05).** We increase our TP post applying a higher PBV multiple of 1.35x based on -1.0SD to its 4-year historical average Fwd PBV (from 1.15x, -1.5SD). We increase our ascribed PBV post briefing as we favour management's commitment to tackle our previously mentioned concerns such as achieving a stable product mix which would foster consistent earnings deliveries going forward. That said, we maintain our PBV valuation method as we remain cautious given that this is the first quarter of positive earnings, and will look to switch our valuation method back to PER upon more consistent earnings deliveries going forward.

## MARKET PERFORM ↔

Price : RM1.16  
Target Price : RM1.20 ↑

#### Share Price Performance



KLCI	1,593.00
YTD KLCI chg	-5.8%
YTD stock price chg	-1.7%

#### Stock Information

Shariah Compliant	Yes
Bloomberg Ticker	SCGM MK EQUITY
Market Cap (RM m)	222.2
Shares outstanding	191.5
52-week range (H)	1.37
52-week range (L)	0.76
3-mth avg daily vol:	397,315
Free Float	38%
Beta	0.9

#### Major Shareholders

SCGM Lee Sdn Bhd	16.0%
Lee Hock Seng	9.3%
Kumpulan Wang Persaraan Diperbadankan	7.6%

#### Summary Earnings Table

FY Apr (RM'm)	2019A	2020E	2021E
Turnover	219.6	257.8	313.7
EBIT	3.9	16.9	25.1
PBT	-1.7	11.3	18.6
<b>Net Profit (NP)</b>	<b>-5.1</b>	<b>9.6</b>	<b>14.2</b>
<b>Core NP</b>	<b>-4.4</b>	<b>9.6</b>	<b>14.2</b>
Consensus (NP)	N.A.	7.5	10.1
Earnings Revision	N.A.	+24%	+53%
Core EPS (sen)	-2.3	5.0	7.4
Core EPS growth (%)	-131.7	N.M.	47.7
NDPS (sen)	1.5	2.0	2.9
BV/Share (RM)	0.8	0.9	1.0
Core PER (x)	N.M.	23.3	15.8
Price/BV (x)	1.4	1.3	1.2
Net Gearing (x)	0.6	0.6	0.5
Net Dvd Yield (%)	1.3	1.7	2.5

\*FY19 share base is on a Fully Diluted basis for comparison purposes



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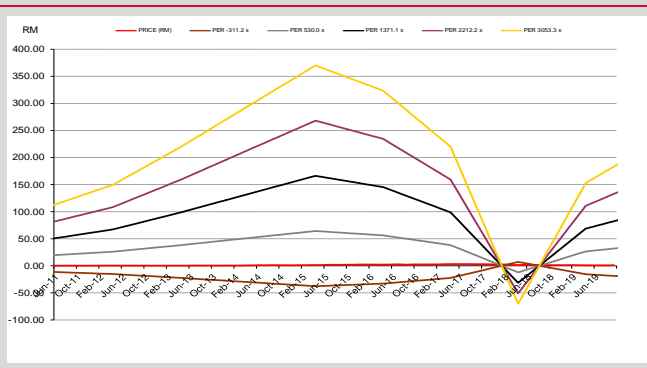
**OTHER POINTS**

**Risks to our call include;** (i) lower or higher-than-expected resin cost, (ii) higher product demand from overseas market, and (iii) stronger or weaker foreign currency rates.

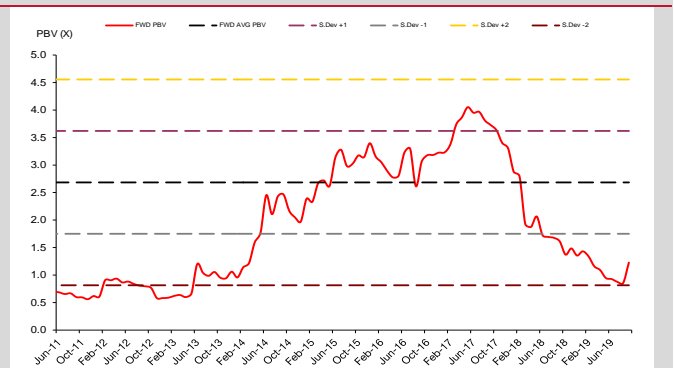
Income Statement						Financial Data & Ratios					
FY Apr (RM m)	2017A	2018A	2019A	2020E	2021E	FY Apr (RM m)	2017A	2018A	2019A	2020E	2021E
Revenue	178.8	207.4	219.6	257.8	313.7	<b>Growth (%)</b>					
EBITDA	35.7	31.9	18.6	34.4	43.2	Revenue	33.9	16.0	5.9	17.4	21.7
Depreciation	-8.4	-11.2	-14.7	-17.4	-18.1	EBITDA	10.4	-10.7	-41.7	84.7	25.7
Operating Profit	27.3	20.7	3.9	16.9	25.1	Op. Profit	4.2	-24.1	-81.2	334.3	48.2
Financial Costs	-0.7	-1.6	-5.6	-5.6	-6.4	Pre-tax Income	3.3	-28.1	n.m.	n.m.	65.2
PBT	26.6	19.1	-1.7	11.3	18.6	Core Net Income	11.9	-33.6	n.m.	n.m.	47.7
Taxation	-3.6	-2.7	-3.4	-1.7	-4.5	<b>Profitability (%)</b>					
Minority Interest	0.0	0.0	0.0	0.0	0.0	EBITDA Margin	20.0	15.4	8.5	13.3	13.8
Net Profit	23.0	16.4	-5.1	9.6	14.2	Operating Margin	15.3	10.0	1.8	6.6	8.0
Core Net Profit	22.6	15.0	-4.4	9.6	14.2	PBT Margin	14.9	9.2	-0.8	4.4	5.9
<b>Balance Sheet</b>						CNP Margin	12.6	7.2	-2.0	3.7	4.5
FY Apr (RM m)	2017A	2018A	2019A	2020E	2021E	ETR	13.0	14.3	-203.6	15.0	24.0
Fixed Assets	97.8	214.4	213.4	223.4	233.4	ROE	13.7	9.0	-2.7	5.8	7.9
Prepaid Leases	0.2	0.2	0.2	0.2	0.2	ROA	9.9	5.6	-1.4	3.0	4.1
Other FA	0.0	0.0	1.3	1.3	1.3	<b>DuPont Analysis</b>					
Inventories	25.2	30.5	33.2	39.0	42.3	CNP Margin (%)	12.6	7.2	-2.0	3.7	4.5
Receivables	41.2	49.9	46.9	55.0	66.9	Assets T/o (x)	0.8	0.7	0.7	0.8	0.9
Other CA	51.1	5.4	6.3	6.3	6.3	Lev Factor (x)	1.4	1.8	2.0	1.9	2.0
Cash	12.8	4.4	8.3	6.5	9.0	ROE (%)	13.7	9.0	-2.7	5.8	7.9
Total Assets	228.1	304.8	309.5	331.7	359.5	<b>Leverage</b>					
Payables	9.9	10.0	25.0	29.3	35.7	Debt/Asset (x)	12.4	26.3	35.0	31.6	29.2
ST Borrowings	20.8	37.1	53.5	50.0	45.0	Debt/Equity (x)	17.1	47.9	69.1	60.0	57.2
Other ST Liability	18.1	37.5	2.9	6.4	19.3	Net Cash/(Debt)	-15.4	-75.8	-100.1	-98.4	-95.9
LT Borrowings	7.4	43.0	54.9	54.9	59.9	Net Debt/Eq (x)	0.1	0.5	0.6	0.6	0.5
Other LT Liability	7.1	9.9	16.4	16.4	16.4	<b>Valuations</b>					
Minorities Int.	0.0	0.0	0.0	0.0	0.0	Core EPS (sen)	11.7	7.2	(2.3)	5.0	7.4
<b>Net Assets</b>	<b>164.8</b>	<b>167.3</b>	<b>156.9</b>	<b>174.7</b>	<b>183.2</b>	NDPS (sen)	4.7	5.6	1.5	2.0	2.9
Share Capital	134.9	134.9	134.7	134.7	134.7	BVPS (RM)	0.6	0.7	0.8	0.9	1.0
Reserves	29.9	38.8	22.2	40.0	48.5	Core PER (x)	9.9	16.1	(50.8)	23.3	15.8
<b>Equity</b>	<b>164.8</b>	<b>167.3</b>	<b>156.9</b>	<b>174.7</b>	<b>183.2</b>	Net Div. Yield (%)	4.0	4.8	1.3	1.7	2.5
<b>Cashflow Statement</b>						P/BV (x)	1.8	1.8	1.4	1.3	1.2
FY Apr (RM m)	2017A	2018A	2019A	2020E	2021E	EV/EBITDA (x)	6.7	9.4	17.4	9.4	7.4
Operating CF	11.3	-8.4	-2.9	15.6	8.1						
Investing CF	-56.1	-0.7	-13.9	-15.0	-15.0						
Financing CF	36.1	21.7	20.6	-9.5	-12.2						
Change In Cash	-8.7	12.7	3.8	-8.9	-19.1						

Source: Kenanga Research

**Fwd PER Band**



**Fwd PBV Band**



Source: Bloomberg, Kenanga Research

Peer Comparison

Name	Last Price	Market Cap (RM'm)	Shariah Compliant	Current FYE	Revenue Growth		Core Earnings Growth		PER (x) - Core Earnings			PBV (x)		ROE (%)	Net Div.Yld. (%)	Target Price (RM)	Rating
	(RM)				1-Yr. Fwd.	2-Yr. Fwd.	1-Yr. Fwd.	2-Yr. Fwd.	Hist.	1-Yr. Fwd.	2-Yr. Fwd.	Hist.	1-Yr. Fwd.	1-Yr. Fwd.	1-Yr. Fwd.		
<b>STOCKS UNDER COVERAGE</b>																	
SCGM BHD	1.16	222.2	Y	04/2020	17.4%	21.7%	45.8%	47.9%	N.M.	23.3	15.8	1.4	1.3	5.8%	1.7%	1.20	MP
SCIENTEX BHD	8.89	4,580.7	Y	07/2020	16.9%	8.6%	16.5%	22.9%	14.4	12.3	10.0	2.4	1.8	20.0%	2.4%	9.45	MP
SLP RESOURCES BHD	1.39	440.6	Y	12/2019	12.5%	5.4%	-6.7%	5.5%	17.4	18.5	17.6	2.4	2.2	12.6%	3.2%	1.45	OP
THONG GUAN INDUSTRIES BHD	2.68	474.7	Y	12/2019	3.4%	2.9%	0.8%	2.7%	10.2	10.1	9.8	1.0	0.9	9.5%	3.4%	2.45	MP
TOMYPAK HOLDINGS	0.480	201.1	Y	12/2019	-2.5%	5.6%	-3.3%	N.A.	N.A.	N.A.	N.A.	1.4	1.0	-6.1%	0.0%	0.270	UP
<b>Simple Average</b>					<b>9.6%</b>	<b>8.8%</b>	<b>10.6%</b>	<b>-8.9%</b>	<b>14.0</b>	<b>16.0</b>	<b>13.3</b>	<b>1.8</b>	<b>1.5</b>	<b>8.3%</b>	<b>2.1%</b>		

Source: Bloomberg, Kenanga Research

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**Stock Ratings are defined as follows:****Stock Recommendations**

OUTPERFORM	: A particular stock's Expected Total Return is MORE than 10%
MARKET PERFORM	: A particular stock's Expected Total Return is WITHIN the range of -5% to 10%
UNDERPERFORM	: A particular stock's Expected Total Return is LESS than -5%

**Sector Recommendations\*\*\***

OVERWEIGHT	: A particular sector's Expected Total Return is MORE than 10%
NEUTRAL	: A particular sector's Expected Total Return is WITHIN the range of -5% to 10%
UNDERWEIGHT	: A particular sector's Expected Total Return is LESS than -5%

**\*\*\*Sector recommendations are defined based on market capitalisation weighted average expected total return for stocks under our coverage.**

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