

# Scientex Berhad

*Synergising with Daibochi to Become Giant Player*

**TP: RM9.87 (+13.8%)**
*Last Traded: RM8.67*
**Buy**

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Yesterday, Scientex Berhad entered into a Head of Agreement (HOA) with certain Daibochi Berhad's shareholders (vendors) for the proposed acquisition of 139.1mn ordinary shares representing 42.4% of total issued shares in Daibochi by Scientex for a total purchase consideration of RM222.5mn to be satisfied through the issuance of new Scientex shares on the basis of 1 Scientex share for 5.5 Daibochi shares. We are positive on this proposal as this would bring Scientex closer to its long-term annual sales target of RM10.0bn by 2028. Upgrade our call on Scientex to Buy with higher target price of RM9.87/share.

## Take-Over Proposal

Scientex proposed to enter into a Conditional Share Sale of Agreement (CSSA) through the HOA with the vendors to acquire 139.1mn ordinary shares i.e. 42.4% of total issued shares in Daibochi. The purchase consideration is RM222.5mn, which is equivalent to RM1.60 per Daibochi share. It will be satisfied through the issuance of new Scientex's ordinary shares via a share exchange of one new Scientex share for every 5.5 Daibochi shares held by the vendors. The CSSA is expected to be executed in the next two months and Scientex will then extend a mandatory take-over offer to acquire the remaining shares and warrants in Daibochi not already held by Scientex.

## Leveraging on Daibochi Strengths

Daibochi is involved in the flexible packaging manufacturing business and is currently leading the South East Asian market with several manufacturing plants in Malaysia and Myanmar. The group produces high-barrier laminated flexible packaging for reputable multinational clients in the Food and Beverages, Fast Moving Consumer Goods as well as specialty sectors.

According to management, the merger is expected to create synergistic benefits as both companies could join force to become a formidable giant in Malaysia with extensive resources to compete globally by offering an integrated range of flexible packaging solutions to a wider customer base. Further on capitalising from economies of scale, together they can bring strong technical market knowledge and talented workforce to tap in the growing segment of flexible plastic packaging. Note that Scientex intends to maintain Daibochi's listing status on the Main Market of Bursa Malaysia and retain all the staff and management of Daibochi.

## Fairly Valued Offer

Based on consensus forecast, the purchase price of RM1.60/share for Daibochi share represents 16.5x FY18 EPS and 12.3x FY19 EPS. This is 19.6% discount to last closing price of RM1.99/share. Meanwhile, based on the share exchange ratio of 1 Scientex share for 5.5 Daibochi shares, the new Scientex shares will be priced RM8.80/share or 13.2x CY18 EPS and 11.4x CY19 EPS. This is less than 3.0% premium to last closing price of RM8.67/share.

### Share Information

Bloomberg Code	SCI MK
Stock Code	4731
Listing	Main Market
Share Cap (mn)	488.9
Market Cap (RMmn)	4,239.0
Par value (RM)	0.5
52-wk Hi/Lo (RM)	9.30/6.51
12-mth Avg Daily Vol ('000 shrs)	229.1
Estimated Free Float (%)	31.5
Beta	0.88
<b>Major Shareholders (%)</b>	
Scientex Holdings Sdn Bhd	21.5
Scientex Leasing Sdn Bhd	9.7
Lim Teck Meng Sdn Bhd	8.4
TM Lim Sdn Bhd	7.9

### Forecast Revision

	FY19	FY20
Forecast Revision (%)	3.1	2.2
Net profit (RMmn)	356.1	394.1
Consensus	338.8	378.0
TA's / Consensus (%)	105.1	104.2
Previous Rating	Hold (Upgraded)	

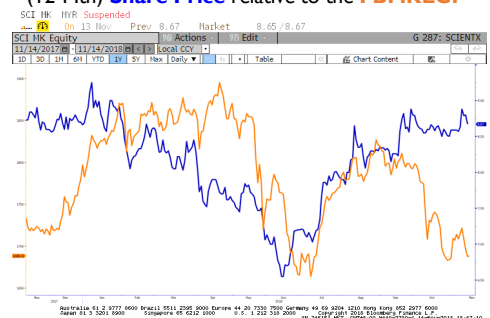
### Financial Indicators

	FY19	FY20
Net debt/equity (%)	51.4	39.6
ROE (%)	17.5	17.4
ROA (%)	9.5	10.1
NTA/Share (RM)	3.8	4.3
Price/NTA (x)	2.3	2.0

### Share Performance (%)

Price Change	SCIENTEX	FBM KLCI
1 mth	0.1	(2.3)
3 mth	3.2	(5.5)
6 mth	10.6	(8.6)
12 mth	(0.7)	(2.0)

### (12-Mth) Share Price relative to the FBMKLCI



Source: Bloomberg

Before the acquisition, the consensus is expecting Daibochi's EPS to grow 10.1% and 11.5% for FY18 and FY19 respectively. Daibochi has a net debt/equity ratio of 30.2% as of Sep-18, which we believe is healthy, allowing the group to finance for future expansion plans if any. In our opinion, the Daibochi's earnings growth could potentially be higher after the conclusion of take-over exercise. As such, considering the earnings growth potential and the synergies from the acquisition, we deem the purchase price of RM1.60/share fair.

### Impact

No change to our Scientex's share capital at this juncture, pending the completion of CSSA and MGO. However, based on our rough estimates, the acquisition would result up to 3.0% EPS growth after new issuance assuming Scientex to control 75% stake in Daibochi.

We raise our earnings forecast by 2.2% to 4.7% for FY19 to FY21 after adjusting our Ringgit assumption from MYR4.00/USD to MYR4.15/USD and also incorporating the FY18 audited financial results into our model.

### Recommendation

We like the acquisition due to synergistic benefits from economies of scale to support earnings growth. We believe this would increase Scientex's EPS by up to 3.0% YoY. Also note that Daibochi has a net debt/equity of 30.2% as of 9M18, which is lower than Scientex 51.0% net debt/equity level for FY18. We upgrade Scientex to Buy from Hold with a higher target price of RM9.87/share (previously RM9.16/share) based on CY19 EPS of SOP 20.0x PER for Manufacturing segment and 6.0x PER for Property segment.

**Table 1 : Valuation Method**

Sum-of-Parts	PAT (RMmn)			Target PER (x)	Segment Value (RMmn)
	FY19	FY20	CY19		
Manufacturing	178.0	197.0	185.9	20	3,635.3
Property	178.0	197.0	185.9	6	1,190.1
					Equity value (RMmn)
					4,825.3
					Share cap (mn)
					488.9
					<b>Target Price (RM)</b>
					<b>9.87</b>

**Earnings Summary**
**PROFIT & LOSS**

FYE July (RMmn)	FY17	FY18	FY19E	FY20F	FY21F
Revenue	2,403.2	2,626.8	3,071.4	3,459.9	3,621.3
Gross Profit	493.2	518.3	622.4	678.3	700.6
EBITDA	388.3	436.1	549.2	597.4	618.7
EBIT	325.1	364.4	457.1	500.7	509.7
Reported PBT	318.0	361.7	445.1	492.6	501.6
Reported net profit	255.9	289.8	356.1	394.1	401.3
Adj. net profit	255.9	289.8	356.1	394.1	401.3
Basic EPS (sen)	55.0	60.0	72.8	80.6	82.1
Adj. EPS (sen)	52.3	59.3	72.8	80.6	82.1
GDPS (sen)	17.0	20.0	21.0	22.0	23.0

**CASH FLOW**

FYE July (RMmn)	FY17	FY18	FY19E	FY20F	FY21F
PBT	318.0	361.7	445.1	492.6	501.6
Adjustments for:					
Depreciation of PPE	63.2	71.7	92.0	96.7	108.9
Finance costs	14.0	10.8	20.9	17.9	18.9
Others	2.2	(2.5)	-	-	-
Op profit before WC	397.4	441.6	558.0	607.1	629.4
(+/-) in inventories	(31.5)	(41.0)	(44.6)	(39.0)	(16.2)
(+/-) in receivables	(68.9)	(25.2)	(89.1)	(77.9)	(32.4)
+ /(-) in payables	16.5	(4.5)	83.1	72.6	30.1
Income Tax Paid	(69.6)	(80.2)	(89.0)	(98.5)	(100.3)
<b>CFO</b>	<b>322.8</b>	<b>392.4</b>	<b>418.3</b>	<b>464.3</b>	<b>510.7</b>
Purchase of PPE	(127.2)	(64.6)	(50.0)	(50.0)	(50.0)
Others	(126.2)	(638.3)	(200.0)	(200.0)	(200.0)
<b>CFI</b>	<b>(253.4)</b>	<b>(702.8)</b>	<b>(250.0)</b>	<b>(250.0)</b>	<b>(250.0)</b>
Net term loans	(7.8)	364.9	110.0	(150.0)	50.0
Dividend paid	(103.0)	(56.5)	(159.4)	(164.5)	(169.7)
Finance costs paid	(18.6)	(15.4)	(20.9)	(17.9)	(18.9)
Others	151.2	(2.2)	-	-	-
<b>CFF</b>	<b>21.8</b>	<b>290.8</b>	<b>(70.3)</b>	<b>(332.4)</b>	<b>(138.6)</b>
Net Cash Flow	91.3	(19.6)	98.0	(118.1)	122.1

**BALANCE SHEET**

FYE July (RMmn)	FY17	FY18	FY19E	FY20F	FY21F
PPE	1,012.6	1,150.6	1,208.6	1,361.9	1,502.9
Deferred tax assets	18.9	28.9	28.9	28.9	28.9
Goodwill	12.1	59.0	59.0	59.0	59.0
Others	581.1	930.1	1,030.1	1,030.1	1,030.1
<b>Non-current assets</b>	<b>1,624.7</b>	<b>2,168.6</b>	<b>2,326.6</b>	<b>2,479.9</b>	<b>2,621.0</b>
Property dev. costs	165.1	233.0	233.0	233.0	233.0
Inventories	168.8	263.6	308.2	347.2	363.3
Trade & Other receivables	426.4	526.6	615.7	693.6	726.0
Tax recoverable	0.9	-	-	-	-
Cash and equivalents	191.9	172.3	270.3	152.2	274.3
<b>Current Assets</b>	<b>953.1</b>	<b>1,195.4</b>	<b>1,427.2</b>	<b>1,426.0</b>	<b>1,596.6</b>
<b>Assets</b>	<b>2,577.8</b>	<b>3,364.1</b>	<b>3,753.8</b>	<b>3,905.9</b>	<b>4,217.6</b>
Borrowings	166.5	323.9	433.9	283.9	333.9
Retirement benefits	27.8	31.1	31.1	31.1	31.1
Deffered tax liabilities	35.9	50.6	50.6	50.6	50.6
<b>Non Current Liabilities</b>	<b>230.2</b>	<b>405.7</b>	<b>515.7</b>	<b>365.7</b>	<b>415.7</b>
Borrowings	301.2	610.4	610.4	610.4	610.4
Trade & other payables	419.4	490.7	573.7	646.3	676.4
Others	23.0	23.8	23.8	23.8	23.8
<b>Current liabilities</b>	<b>743.7</b>	<b>1,124.8</b>	<b>1,207.9</b>	<b>1,280.4</b>	<b>1,310.6</b>
Share capital	411.8	453.9	453.9	453.9	453.9
Reserves	1,123.6	1,309.7	1,506.4	1,735.9	1,967.5
Shareholders' Funds	1,535.5	1,763.6	1,960.2	2,189.8	2,421.3
MI	68.4	70.0	70.0	70.0	70.0
<b>Equity</b>	<b>1,603.9</b>	<b>1,833.6</b>	<b>2,030.2</b>	<b>2,259.7</b>	<b>2,491.3</b>
<b>Equity &amp; Liabilities</b>	<b>2,577.8</b>	<b>3,364.1</b>	<b>3,753.8</b>	<b>3,905.9</b>	<b>4,217.6</b>

**FINANCIAL RATIOS**

FYE July (RMmn)	FY17	FY18	FY19E	FY20F	FY21F
P/E (x)	16.6	14.6	11.9	10.8	10.6
P/BV (x)	2.7	2.4	2.3	2.0	1.8
Dividend yield (%)	2.0	2.3	2.4	2.5	2.7
ROE (%)	16.0	15.8	17.5	17.4	16.1
ROA (%)	9.9	8.6	9.5	10.1	9.5
EBIT margin (%)	13.5	13.9	14.9	14.5	14.1
Net margin (%)	10.6	11.0	11.6	11.4	11.1
Gearing (x)	0.3	0.5	0.5	0.4	0.4

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### Stock Recommendation Guideline

- BUY** : Total return within the next 12 months exceeds required rate of return by 5%-point.  
**HOLD** : Total return within the next 12 months exceeds required rate of return by between 0-5%-point.  
**SELL** : Total return is lower than the required rate of return.  
**Not Rated:** The company is not under coverage. The report is for information only.

**Total Return** is defined as expected share price appreciation plus gross dividend over the next 12 months. Gross dividend is excluded from total return if dividend discount model valuation is used to avoid double counting.

**Required Rate of Return** of 7% is defined as the yield for one-year Malaysian government treasury plus assumed equity risk premium.

### Disclaimer

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As of Thursday, November 15, 2018, the analyst, Damia Othman, who prepared this report, has interest in the following securities covered in this report:

(a) nil

**Kaladher Govindan – Head of Research**

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