

Company Focus

Evergreen Fibreboard

Bloomberg: EVF MK | Reuters: EVGN.KL

Malaysia Equity Research PP 11272/04/2010(023521)

17 Aug 2009

BUY RM0.93 KLCI : 1,188.57

(Upgrade from Fully Valued)

Price Target : 12-Month RM 1.10 (Prev RM 0.45)

Reason for Report : Company update

Potential Catalyst: Stronger MDF prices and sales volume

Analyst

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Price Relative



Forecasts and Valuation

FY Dec (RM m)	2008A	2009F	2010F	2011F
Turnover	731	737	838	918
EBITDA	120	125	128	128
Pre-tax Profit	64	36	45	48
Net Profit	77	37	43	46
Net Pft (Pre Ex.)	85	40	43	46
EPS (sen)	15.0	7.3	8.4	9.0
EPS Pre Ex. (sen)	16.6	7.8	8.4	9.0
EPS Gth Pre Ex (%)	(33)	(53)	8	7
Diluted EPS (sen)	15.0	7.3	8.4	9.0
Net DPS (sen)	0.0	0.0	1.4	1.4
BV Per Share (sen)	119.0	126.3	134.7	142.4
PE (X)	6.2	12.8	11.1	10.3
PE Pre Ex. (X)	5.6	11.9	11.1	10.3
P/Cash Flow (X)	4.1	4.4	4.2	4.0
EV/EBITDA (X)	7.3	6.0	4.9	4.0
Net Div Yield (%)	0.0	0.0	1.5	1.5
P/Book Value (X)	0.8	0.7	0.7	0.7
Net Debt/Equity (X)	0.6	0.4	0.2	0.1
ROAE (%)	13.4	5.9	6.4	6.5

Earnings Rev (%)	24.1	16.2	15.6
Consensus EPS (sen)	7.9	10.4	11.9

ICB Industry : Industrials
 ICB Sector: Construction & Materials
 Principal Business: MDF Manufacturer

Source of all data: Company, DBS Vickers, Bloomberg

Better demand outlook

- EFB's forward bookings improved to 1-2 months from 1-2 weeks during the previous slump signalling demand has improved
- As one of the leading MDF players, EFB is well-positioned to ride the economic recovery
- Raised FY09-10F earnings by 16-24% on higher MDF sales volume
- Upgrade to Buy with RM1.10 (from RM0.45) TP based on 0.8x CY10F BV (from 0.4x), consistent with peers' average. The counter is trading at 0.7x CY10F BV.

MDF demand improves. MDF demand picked up again on expectation of gradual recovery of global economy. We understand that EFB's forward bookings had improved to 1-2 months from 1-2 weeks previously during the slump in mid-Oct 08 to Apr-09. EFB's capacity utilization also rose to 64% in 2Q09 from 55% in 1Q09. We believe there is more upside to it in 2H09 given that utilization rates were still below the pre-crisis level of more than 80%.

Demand coming from various new and old markets.

Though the bookings could be partly due to restocking activities, we understand that there is also demand from new markets. We are also not ruling out that MDF demand had picked up again on expectation of gradual recovery of global economy towards 2010. Furthermore, wide applications of MDF in different areas allowed it to benefit from recovery in various sectors.

Raised FY09-10F earnings by 16-24% on higher MDF sales volume. We expect MDF demand to slowly recover from 2H09 onwards. We now project MDF sales volume to grow by 23% in FY09F and 15% in FY10F (from -10% and +5% previously), implying capacity utilization of 66% and 76% respectively.

At A Glance

Issued Capital (m shrs)	513
Mkt. Cap (RMm/US\$m)	477 / 136
Major Shareholders	
Kuo Family (%)	42.3
Lembaga Tabung Haji (%)	2.9
EPF (%)	2.3
Free Float (%)	52.5
Avg. Daily Vol.('000)	680

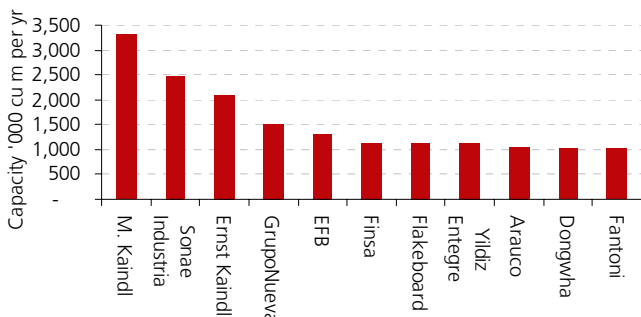
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Highlights

Demand coming from various new and old markets. We understand that demand for EFB’s MDF products came from various international markets including China, U.S., Vietnam, and the Middle East. Though the bookings could be partly due to restocking activities, we understand that there is also demand from new markets. We do not rule out that MDF demand had picked up again on expectation that global economy will slowly recover towards 2010. Furthermore, wide applications of MDF in different areas (such as automotives, building interiors, household products, and other building materials) allowed it to benefit from recovery in various sectors.

Well-positioned to benefit from economic recovery given that EFB is one of the biggest MDF players in the world. EFB is known to be the 5th largest MDF producer (by production capacity) in the world and they are likely to be the biggest in the region.

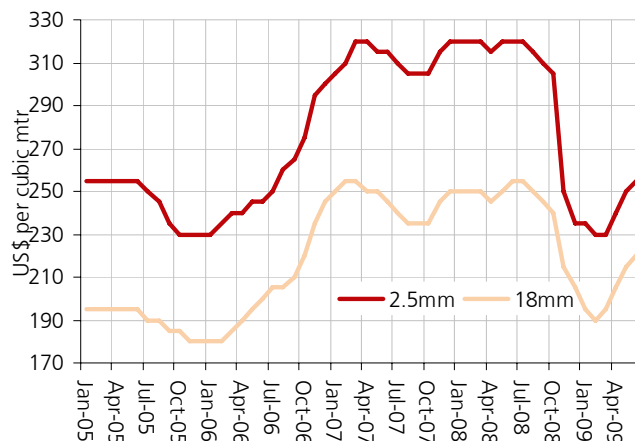
Leading global MDF players



Source: Company, DBS Vickers

Raised FY09F and 10F earnings by 24% and 16% respectively after imputing higher MDF sales volume as we expect MDF demand to slowly recover from 2H09 onwards. We now project MDF sales volume to grow by 23% in FY09F and 15% in FY10F (from -10% and +5% previously), implying capacity utilization of 66% and 76% respectively. EFB’s present MDF production capacity stood at 1.19mil m³ p.a. (excluding Indonesian plant). We have also included stronger USD against MYR in FY09F-10F by 4-6% based on our latest house forecasts leading to higher average MDF prices in MYR terms i.e. 5-7%.

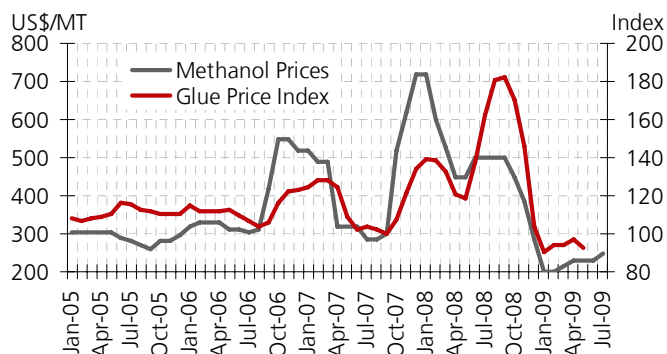
MDF prices trending upwards



Source: Company, DBS Vickers

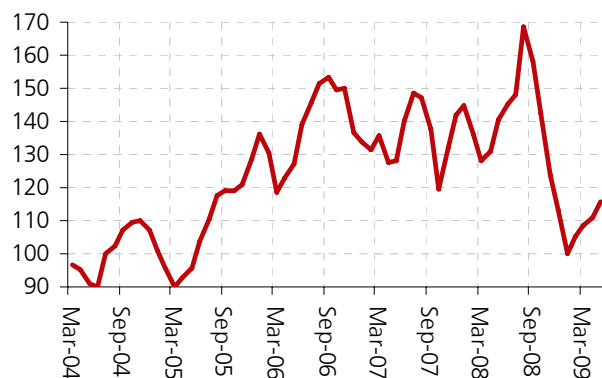
A volume game. EFB’s earnings are expected to be driven by higher sales volume rather than benefiting from higher MDF prices. We expect gross margin to remain soft, if not stable, going forward, on higher glue cost assumptions (on expectation that crude oil price will recover) as well as increase in rubberwood prices (due to limited supply). Note that glue and rubberwood costs account for 25-28% and 30-35% of total MDF manufacturing cost respectively.

Glue index vs methanol prices



Source: Company, DBS Vickers

Rubberwood log price index



Source: Company, DBS Vickers

Thailand's 3rd MDF line is up and running but Indonesian plant is temporarily shut down. We understand that the new third MDF line in Thailand began full operations in Mar 09. However, the Indonesian plant (under EFB's 51% owned joint venture with Indonesian-based P.T. Hutrindo Jaya Fibreboard Mfg. Co. and P.T. Uforin Prajen Adhesive Industry) had been shut down since early this year due to financial difficulties faced by the Indonesian partners. We understand that the partners are presently seeking to sell their stake and target to conclude by end-09. In the worst case scenario, we foresee EFB exiting the business or taking over the assets although it is very unlikely to happen as the Group prefers to operate with a local partner in Indonesia. We understand that the cost to maintain the project is minimal i.e. c. RM2.4m per year. EFB had invested RM35m in the project thus far.

2Q09 could be stronger q-o-q on expected higher sales volume as capacity utilization improved from 54.5% in 1Q09 to 66.7% in 2Q09. However, EFB may have not able to catch up with the higher MDF prices in the 2Q09 as it carried out previous orders which had prices quoted in 1Q09. Note that, average MDF prices rose 6% q-o-q to RM820/m³. Meanwhile,

gross margin is expected to remain relatively stable q-o-q although average rubberwood prices rose 8%. Apart from higher production volume, this could be partly mitigated by c.10-20% reduction in salaries and overtime. Glue prices were relatively flat q-o-q.

Key business risks

Weakening USD against MYR could adversely impact earnings given that overseas revenue presently accounts for c.75% the Group's total revenue. We understand that EFB have not hedged its sales from 3Q09 onwards. Our sensitivity analysis shows a 1% increase in USD against MYR could drag down FY09-11F earnings by 11-12%.

Higher crude oil prices could result in higher methanol prices. Methanol is used as the feedstock for the production of glue, the main cost component in MDF manufacturing. We have projected higher glue cost in FY10F and FY11F on the back of higher forecast crude oil prices. Our house projects crude oil prices to average US\$75/barrel and US\$80/barrel in FY10F and FY11F respectively (from US\$57/barrel this year).

Higher electricity tariff could suppress margins as electricity cost accounts for 10-15% of total MDF manufacturing costs. After 26% rise in June 08 and 5% reduction in Mar 09, next review of electricity tariff is due in Jan 10. Our sensitivity analysis shows a 5% increase in electricity tariff could drag down FY10F-11F earnings by 2%, assuming all else equal.

Valuation

Upgrade to Buy (from Fully Valued) with a higher TP of RM1.10 (from RM0.45) based on 0.8x CY10F BV (from 0.4x), consistent with the valuation for its peers. We believe EFB's valuation is still relatively low at 0.7x BV, lower than its historical average of 1.0x.

Peers Comparison

	Local Currency	Price (local currency)	Mkt Cap (US\$ mil)	CY09 PE	CY10 PE	CY10 P/BV
Vanachai Group PCL	THB	1.62	62	6.1	3.7	0.4
Sumalindo Lestari Jaya Tbk PT	IDR	560.00	70	n.a.	n.a.	n.a.
Pfleiderer Grajewo SA	PLN	10.34	177	(114.9)	21.3	0.9
Sonae Industria SGPS SA	EUR	2.27	453	(3.2)	(5.9)	1.1
Masisa SA	CLP	77.00	924	23.4	12.8	n.a.
Evergreen Fibreboard	MYR	0.93	136	11.9	11.1	0.7
Average (exc. EFB)				14.7	12.6	0.8

Source: Bloomberg, DBS Vickers

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EFB's historical 1-year forward P/BV



Source: Bloomberg, HwangDBS Vickers Research

EFB's historical 1-year forward PE



Source: Bloomberg, HwangDBS Vickers Research

Cash flow summary and comments

FYE Dec (RMm)	3Q08	4Q08	1Q09	FY09F	FY10F	FY11F	Comment
Profit before taxation	13.4	(0.9)	2.7	36.2	44.7	48.2	
Changes in working capital	31.2	(33.5)	(8.0)	(0.2)	(19.6)	(15.6)	Inventory days improved to 70 days in 1Q09 from 75 days in 3Q08 and 4Q08.
Others inc. non-cash items	32.3	23.4	15.8	74.9	75.8	76.8	
Net cash flow generated from/(used in) operating activities	76.9	(11.0)	10.5	110.8	101.0	109.4	
Capex	(327.2)	(49.6)	(7.5)	(15.0)	(15.0)	(15.0)	
Others inc. non-cash items	0.9	0.7	0.5	-	-	-	
Net cash flow generated from/(used in) investing activities	(326.3)	(48.9)	(6.9)	13.9	13.9	13.9	
Increase in share capital	43.2	-	-	-	-	-	Issued 33m new shares at RM1.31 each for the acquisition of Hume Fibreboard in 3Q08.
Dividend Paid	(21.6)	-	-	-	-	(7.2)	
Drawdown / (Repayment) of loan	215.9	24.4	33.9	(30.0)	(60.0)	(60.0)	Total borrowings increased by RM40.7m to RM510.5m. However, net gearing remained stable at 0.6x in 1Q09 due to EFB's higher cash balance.
Net cash flow generated from/(used in) financing activities	237.5	24.4	33.9	(30.0)	(60.0)	(67.2)	
Net Change in Cash & Cash Equivalents	(11.9)	(35.5)	37.5	94.7	54.8	56.1	

Source: Company, DBS Vickers

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Income Statement (RM m)

FY Dec	2008A	2009F	2010F	2011F
Turnover	731	737	838	918
Cost of Goods Sold	(533)	(562)	(653)	(726)
Gross Profit	198	175	184	191
Other Opng (Exp)/Inc	(118)	(120)	(128)	(136)
Operating Profit	80	55	56	55
Other Non Opng (Exp)/Inc	0	0	0	0
Associates & JV Inc	2	0	0	0
Net Interest (Exp)/Inc	(10)	(16)	(12)	(8)
Exceptional Gain/(Loss)	(8)	(3)	0	0
Pre-tax Profit	64	36	45	48
Tax	5	(4)	(3)	(4)
Minority Interest	8	5	2	2
Preference Dividend	0	0	0	0
Net Profit	77	37	43	46
Net Profit before Except.	85	40	43	46
EBITDA	120	125	128	128
Sales Gth (%)	(0.1)	0.9	13.7	9.6
EBITDA Gth (%)	(31.4)	4.1	1.9	0.1
Opg Profit Gth (%)	(44.7)	(31.8)	2.6	(1.4)
Net Profit Gth (%)	(35.4)	(51.4)	15.8	7.4
Effective Tax Rate (%)	N/A	10.1	7.8	7.8

Cash Flow Statement (RM m)

FY Dec	2008A	2009F	2010F	2011F
Pre-Tax Profit	64	36	45	48
Dep. & Amort.	40	70	71	72
Tax Paid	(7)	(1)	(1)	(1)
Assoc. & JV Inc/(loss)	(2)	0	0	0
Chg in Wkg.Cap.	19	0	(20)	(16)
Other Operating CF	6	6	6	6
Net Operating CF	120	111	101	109
Capital Exp.(net)	(409)	(15)	(15)	(15)
Other Invt.(net)	0	0	0	0
Invt in Assoc. & JV	0	0	0	0
Div from Assoc & JV	0	0	0	0
Other Investing CF	29	29	29	29
Net Investing CF	(380)	14	14	14
Div Paid	(22)	0	0	(7)
Chg in Gross Debt	234	(30)	(60)	(60)
Capital Issues	0	0	0	0
Other Financing CF	1	0	0	0
Net Financing CF	213	(30)	(60)	(67)
Net Cashflow	(47)	95	55	56

Quarterly / Interim Income Statement (RM m)

FY Dec	2Q2008	3Q2008	4Q2008	1Q2009
Turnover	186	193	172	155
Cost of Goods Sold	(129)	(148)	(131)	(121)
Gross Profit	58	46	41	34
Other Oper. (Exp)/Inc	(31)	(30)	(31)	(24)
Operating Profit	27	16	9	10
Other Non Opng (Exp)/Inc	0	0	0	0
Associates & JV Inc	0	1	0	0
Net Interest (Exp)/Inc	(3)	(3)	(5)	(5)
Exceptional Gain/(Loss)	0	0	(5)	(3)
Pre-tax Profit	24	13	(1)	3
Tax	1	1	4	(1)
Minority Interest	1	2	4	3
Net Profit	26	16	8	5
Net profit bef Except.	26	16	13	7
Sales Gth (%)	4.0	3.7	(11.1)	(9.9)
Opg Profit Gth (%)	(14.7)	(42.5)	(39.0)	6.6
Net Profit Gth (%)	(15.0)	(37.1)	(50.9)	(41.8)
Gross Margins (%)	30.9	23.6	23.8	22.1
Opg Profit Margins (%)	14.5	8.0	5.5	6.5
Net Profit Margins (%)	13.8	8.4	4.6	3.0

Source: Company, DBS Vickers

Balance Sheet (RM m)

FY Dec	2008A	2009F	2010F	2011F
Net Fixed Assets	903	847	791	734
Invt in Associates & JVs	21	21	21	22
Other LT Assets	33	33	33	33
Cash & ST Invt	76	171	226	282
Inventory	137	136	162	182
Debtors	43	43	49	54
Other Current Assets	33	33	33	33
Total Assets	1,246	1,286	1,315	1,339
ST Debt	255	191	191	191
Other Current Liab	152	152	164	173
LT Debt	215	249	189	129
Other LT Liabilities	8	45	82	119
Shareholder's Equity	611	648	691	730
Minority Interests	6	1	(1)	(3)
Total Cap. & Liab.	1,246	1,286	1,315	1,339
Non-Cash Wkg. Capital	61	61	81	96
Net Cash/(Debt)	(393)	(269)	(154)	(38)

Rates & Ratio

FY Dec	2008A	2009F	2010F	2011F
Gross Margins (%)	27.1	23.7	22.0	20.9
Opg Profit Margin (%)	11.0	7.4	6.7	6.0
Net Profit Margin (%)	10.5	5.1	5.2	5.0
ROAE (%)	13.4	5.9	6.4	6.5
ROA (%)	7.1	2.9	3.3	3.5
ROCE (%)	8.5	4.4	4.5	4.4
Div Payout Ratio (%)	0.0	0.0	16.7	15.5
Net Interest Cover (x)	8.3	3.4	4.8	7.3
Asset Turnover (x)	0.7	0.6	0.6	0.7
Debtors Turn (avg days)	23.8	21.4	20.2	20.6
Creditors Turn (avg days)	38.8	46.1	42.5	43.6
Inventory Turn (avg days)	80.9	101.4	93.5	95.7
Current Ratio (x)	0.7	1.1	1.3	1.5
Quick Ratio (x)	0.3	0.6	0.8	0.9
Net Debt/Equity (X)	0.6	0.4	0.2	0.1
Net Debt/Equity ex MI (X)	0.6	0.4	0.2	0.1
Capex to Debt (%)	87.1	3.4	3.9	4.7
Z-Score (X)	1.4	1.4	1.7	1.8
N. Cash/(Debt)PS (sen)	(76.7)	(52.4)	(30.0)	(7.4)
Opg CFPS (sen)	19.7	21.6	23.5	24.4
Free CFPS (sen)	(56.4)	18.7	16.8	18.4

Segmental Breakdown / Key Assumptions

FY Dec	2008A	2009F	2010F	2011F
Key Assumptions				
Average MDF price (2.5mm)	304.2	268.2	271.1	272.3
Average MDF price (18mm)	242.5	229.4	231.8	232.9
Volume growth	1.8	22.7	15.0	10.0
MYR/USD	3.3	3.6	3.5	3.3

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