

OSK**MALAYSIA EQUITY**
Investment Research
Daily NewsVincent Lim Vi Ming
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viming.lim@my.oskgroup.com**Company Update****Evergreen Fibreboard****Stepping Up to Higher Demand**

We recently met the management of Evergreen Fibreboard (EFB) and came away with a positive outlook on its operations. We see earnings improving this year on the back of higher sales volume and wider operating margins due to the cost cutting measures initiated last year. We revise upwards our FY10 and FY11 net earnings by 35%-45% respectively on factoring in the developments mentioned earlier. We also arrive at a higher TP for the stock of RM2.08 from RM1.62 (derived by tagging a low end peers timber sector PE at 9.7 times) previously. **BUY recommended.**

Orders on the rise. EFB's sales have been on an uptrend since the start of last year. As at 1Q09, utilization at its domestic plant was at breakeven level of 50%. However as orders picked up in subsequent quarters, its plant utilization climbed to approximately 80% by end-2009. Riding on robust regional thirst for MDF products, demand is envisaged to be at healthy levels for the rest of FY10 and well into FY11.

More capacity. Compared to 2 years ago, EFB has expanded its production capacity from 700,000 m3 per annum to 1.3m m3 per annum. This applies to its operations in Malaysia, Thailand and Indonesia. We expect EFB to operate at a utilization rate of 80%-85% this year (excluding Indonesian plant) and subsequently rising 90% next year on in tandem with surging demand for MDF in the ASEAN region.

Costs under control. Amid rising raw material prices early this year, management believes that rubber wood cost is still manageable. The price surge, which was due to a shortage arising from heavy rain at logging sites, is expected to be only temporary. Glue costs should remain acceptable as well as EFB produces its own glue at 10% below the market spot price.

Earnings revision. The company's stronger earnings this year has prompted us to revise upwards our revenue projection by 1-6%. On the back of better economies of scale from higher sales and the cost cutting measures initiated in 2H last year, we are also assuming a higher gross profit margin of approximately 31% against 27% in FY09. Thus, we raise our bottom line net profit estimation by 35% for FY10 and 45.5% for FY11.

Higher TP. By ascribing a higher tier-end building material sector PE of 9 times to its FY10 EPS of 23.1 sen, we derive a target price of RM2.08 for EFB. Given the stock's upside of 22.4%, we also reiterate our BUY recommendation. We expect EFB to declare a gross DPS of 7.2 sen, or a gross yield of 4.3%. Our dividend assumption is based on a payout ratio of 23.5%, similar to that last year.

BUY ↔

Target

RM2.08

Previous

RM1.62

Price

RM1.70

BUILDING MATERIAL

Evergreen Fibreboard is involved in the manufacture of medium density fibreboards (MDF), particle boards, value-added fibreboards and furniture.

Stock Statistics

Bloomberg Ticker	EVF MK
Share Capital (m)	513.0
Market Cap (RMm)	872.1
52 week H L Price (RM)	1.80 0.50
3mth Avg Vol ('000)	1,071.0
YTD Returns	21.4
Beta (x)	1.64

Major Shareholders (%)

LTH	7.1
HIMB Trading Ltd	6.0
Hume Fibreboard	5.1

Share Performance (%)

Month	Absolute	Relative
1m	6.3	7.0
3m	15.9	13.6
6m	66.3	49.7
12m	236.0	125.0

6-month Share Price Performance

FYE Dec (RMm)	FY07	FY08	FY09	FY10f	FY11f
Revenue	731.6	730.5	771.5	874.5	967.7
Net Profit	118.5	76.7	87.4	118.7	135.2
% chg y-o-y	98.4	-35.3	13.9	35.8	13.9
Consensus	-	-	-	88.9	97.9
EPS (sen)	24.7	15.0	17.0	23.1	26.4
DPS (sen)	7.0	0.0	5.3	7.2	8.3
Dividend yield (%)	4.1	0.0	3.1	4.3	4.9
ROE (%)	24.7	13.4	13.3	15.8	15.9
ROA (%)	13.0	6.2	7.0	8.5	8.9
PER (x)	6.9	11.4	10.0	7.3	6.5
BV/share (RM)	1.04	1.19	1.38	1.55	1.75
P/BV (x)	1.7	1.5	1.3	1.1	1.0
EV/ EBITDA (x)	6.5	17.7	12.6	6.5	6.4

KEY HIGHLIGHTS

Orders on the uptrend. EFB's quarterly performance in 2009 had displayed trend of growing sales momentum. Starting with a plant utilization of 50% in 1Q09, utilization rates had strengthened to 80% by year-end, which is on par with pre-financial crisis levels. Based on our understanding, EFB's performance for the whole of FY2010 may well be reflected by its 4Q09 performance.

Figure 1: FY 2009 utilization rates and revenue by quarter

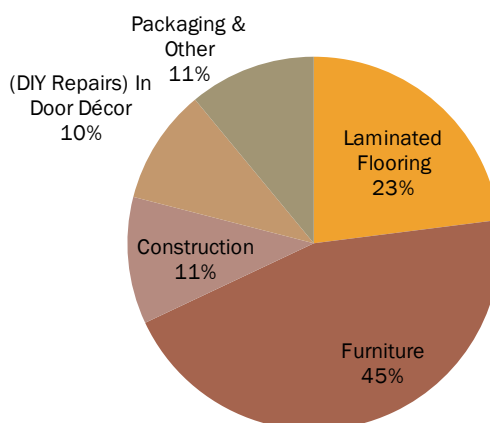
FY 2009	Quarter 1	Quarter 2	Quarter 3	Quarter 4
Revenue (RMm)	154.9	180.6	211.9	224.1
Pretax profits	2.7	12.1	31.4	34.2

Source: OSK, Company

Capacity to meet demand. Compared to two years ago, EFB has expanded its production capacity from 700,000 m3 per annum to 1.3m m3 per annum. This applies to all its production plants in Malaysia (620,000 m3/annum), Thailand (570,000 m3/annum) and Indonesia (120,000 m3/annum). Thus we think its future earnings may well be reflected in its increased capacity in tandem with increasing regional demand for MDF products. Despite public perception that EFB's sales and selling prices are tied to global demand for wood based products and also linked to Japan, United States and Europe, we point out that EFB as a downstream wood product manufacturer is in fact more exposed to the ASEAN region in terms of sales.

Diverse market. EFB's sales are spread across 45 countries with no one country accounting for more than 20% of its distributed volume. Should we segregate its sales regionally, 50% of EFB's distribution is to ASEAN while 25% of exports is to Middle East markets. The remaining 25% goes to markets such as Far East Asia, United States and Europe. Most of EFB's MDF sales are mainly for a country's in-house consumption and often used for applications in the furniture and laminated flooring industry. Hence, suffice to say, EFB's sales are riding on growing consumption for MDF, which are for consumer related goods in ASEAN instead of being used in mass housing construction projects such as those practised in Japan, United States and Europe.

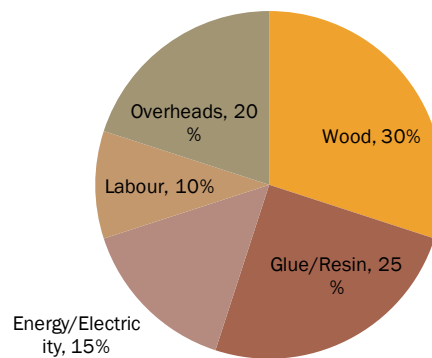
Figure 2: MDF applications



Source: Company

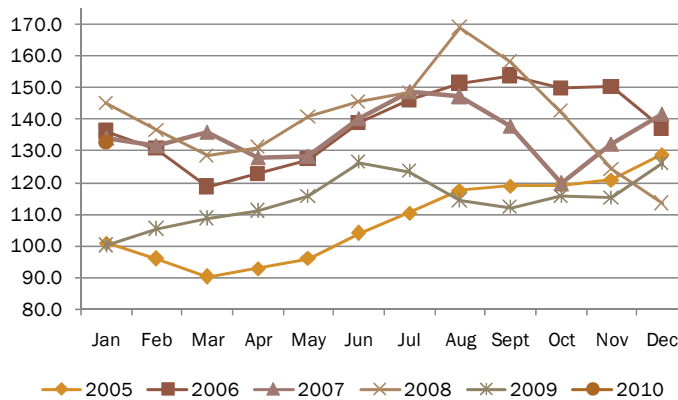
Cost not a concern. Rain in the rainforest during the months of January and February force loggers to cut back on log harvesting, causing a shortage which in turn leads to wood prices surging. However, management opines that its main raw material – rubber wood – was only slightly affected in terms of pricing. This is because the prices that have surged are mainly for hard wood, which has its habitat at hilly areas that are inaccessible during rainy seasons. However, since rubber trees are planted on flat ground, supply constraints are usually minimal. Geographically, EFB sources its rubber wood from the district of Jempol in Negeri Sembilan state. It sources its wood particularly from the towns of and around Bahau, Serting and Tampin. Our geographical checks confirm the flat contour of the land in the area. Supply wise, assuming there is no replanting of rubber trees, Malaysia’s current rubber wood supply at 1.2bn hectares of rubber trees is enough to provide a steady stream of supply for as long as 20 years. Now that EFB also produces its own glue/resin for internal consumption, it is able to source its glue at prices 10% below the spot price. Furthermore, wood and glue price fluctuations are often the cost components which EFB can pass on to its customers, as opposed to fixed costs such as overheads, labour and electricity.

Figure 3: EFB’s cost breakdown

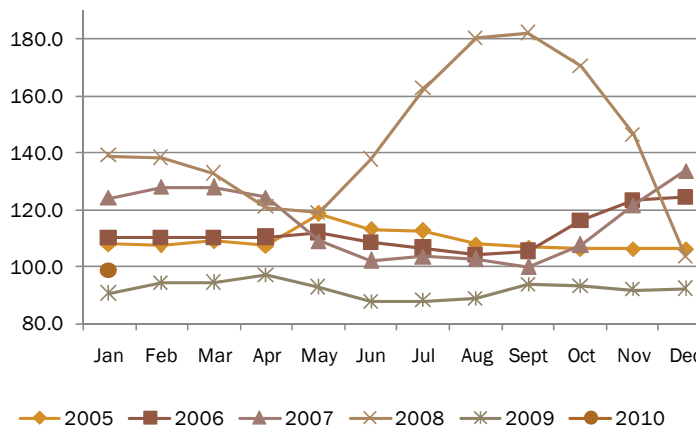


Source: Company

Figure 4: Rubber wood price index (2005-2010)



Source: Company

Figure 5: Glue/Resin price index (2005-2010)

Source: Company

Better earnings. We marginally revise higher our revenue estimates for FY10 and FY11 by around 1-6% on the back of higher plant utilization rates. We see EFB's production plants in Malaysia and Thailand operating at 80%-82% utilization this year, similar to that in 4Q09. For FY11, we see plant utilization rising to 85-90%. EFB's Indonesian plant is expected to commence in 2H this year but at a utilization rate of only ~60% although we see it improving to 65% next year. On the back of better economies of scale and EFB's cost cutting measures in 2H09, we are also assuming a higher gross profit margin of approximately 31% against 27% in FY09. Thus, we raise our bottom line net profit estimates by 35% for FY10 and 45.5% for FY11.

Higher TP of RM2.08. We envisage higher earnings for EFB this year to translate into a FY10 EPS of 23.1 sen. Hence, by ascribing a higher tier-end building material sector PE of 9 times to its EPS, we derive a target price of RM2.08. Given the stock's upside of 22.4%, we also reiterate our BUY recommendation. We see EFB declaring a gross DPS of 7.2 sen, or a gross yield of 4.3%. Our dividend assumption is based on a pay-out ratio of 23.5%, similar to last year's.

EARNINGS FORECAST

FYE Dec (RMm)	FY07	FY08	FY09	FY10f	FY11f
Turnover	731.6	730.5	771.5	874.5	967.7
EBITDA	117.8	60.9	88.9	190.1	210.9
PBT	140.4	63.9	80.4	120.6	137.4
Net Profit	118.5	76.7	87.4	118.7	135.2
EPS (sen)	24.7	15.0	17.0	23.1	26.4
DPS (sen)	7.0	0.0	5.3	7.2	8.3
Margin					
EBITDA (%)	16.1	8.3	11.5	21.7	21.8
PBT (%)	19.2	8.7	10.4	13.8	14.2
Net Profit (%)	16.2	10.5	11.3	13.6	14.0
ROE (%)	24.7	13.4	13.3	15.8	15.9
ROA (%)	13.0	6.2	7.0	8.5	8.9
Balance Sheet					
Fixed Assets	517.7	902.9	885.0	860.1	821.2
Current Assets	347.8	289.4	308.8	477.2	635.3
Total Assets	912.6	1246.2	1249.4	1392.6	1511.5
Current Liabilities	138.4	407.3	227.9	276.6	287.5
Net Current Assets	209.3	-117.9	80.9	200.6	347.9
LT Liabilities	235.1	222.6	313.6	313.3	313.3
Shareholders Funds	532.5	610.7	706.2	796.9	900.3
Net Gearing (%)	19.7	64.5	42.8	27.1	12.6
Cash Flow					
PBT	140.4	63.9	80.4	120.6	137.4
Other Operating Cash	-265.8	-138.0	382.7	18.3	18.8
Chg in Working Capital	-17.1	155.8	-397.3	-40.5	6.2
Operating Cashflow	1.7	121.5	121.2	155.5	221.3
CAPEX	179.5	457.6	19.8	50.0	20.0
FCF	181.2	579.1	141.0	205.5	241.3

OSK Research Guide to Investment Ratings

Buy: Share price may exceed 10% over the next 12 months

Trading Buy: Share price may exceed 15% over the next 3 months, however longer-term outlook remains uncertain

Neutral: Share price may fall within the range of +/- 10% over the next 12 months

Take Profit: Target price has been attained. Look to accumulate at lower levels

Sell: Share price may fall by more than 10% over the next 12 months

Not Rated (NR): Stock is not within regular research coverage

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