

08 September 2023

# Thong Guan Industries

## Resilient Amidst Macro Headwinds

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TGUAN may see a spike in orders as its customers rush to stock up ahead of price hikes (prompted by the rising cost of input resin). However, we acknowledge that a more sustainable recovery in demand still hinges on a stronger global economy. We cut our FY23F earnings by 5% mainly to reflect higher electricity cost. We maintain our TP of RM3.05 and OUTPERFORM call.

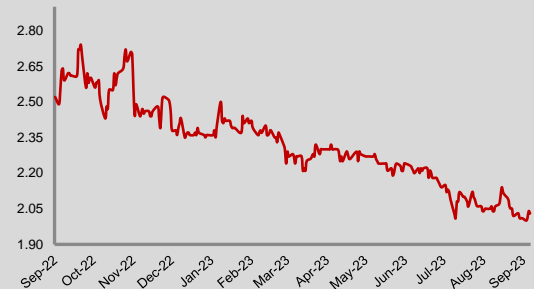
We came away from a post-results engagement with TGUAN feeling reassured of its FY24 and longer-term outlook despite current macro challenges. The key takeaways are as follows:

- Customers may rush to stock up ahead of price hikes.** Amidst the rising cost of input resin (see chart on next page) that will eventually prompt plastic packaging producers to raise products prices, stockists and users of plastic packaging users may rush to stock up. Already, TGUAN has recently seen a pick-up in orders for its courier bags and nano stretch film. However, we acknowledge that a more sustainable recovery in demand for plastic packaging products still hinges on a stronger global economy.
- Certain products are more resilient.** Amidst macro headwinds, we expect the demand for TGUAN's stretch film (especially nano stretch film) to stay resilient given: (i) its price competitiveness vs. those produced by European and US producers, stemming from TGUAN's lower energy and labour costs; (ii) TGUAN's proprietary technology in producing thinner but stronger film, making its product more economical, environmentally friendly (i.e. using less resin to produce the same square metres of film) and suitable for automated packaging (because of the added strength). In 2QFY23, stretch film made up half of TGUAN's total turnover.  
  
Similarly, we expect the demand for TGUAN's industrial bags (comprising lamination films, oil bags, sugar bags, shrink film, stretch hood) to stay robust given that they are mainly used in the F&B and FMCG sectors which are less affected by the economic downturn. In 2QFY23, industrial bags contributed to 17% of its total revenue.
- Expansion plans proceeding as planned.** Meanwhile, its 9th nano stretch film machine has been commissioned, and the installation of its 10th nano stretch film machine is on-going. These additions should boost its overall stretch film capacity by 25%-30% and help it to supply to countries like Spain, Mexico, Germany, UK and USA.
- Higher electricity cost.** Starting in Aug 2023, TGUAN will be facing a monthly increase of RM1m in electricity costs after opting out from the Green Electricity Tariff (GET) programme. The decision was made due to the higher GET rate of 21.8 sen/kWh (from 3.7 sen/kWh), compared to conventional ICPT surcharge of 17.0 sen/kWh. Note that this increase is higher than what we had expected as TGUAN clarified that 90% of its electricity consumption was under the GET programme which we had estimated at only 20%-30% previously. TGUAN plans to raise ASP in order to pass on the higher electricity cost to its customers. To further mitigate the impact, it is working to ramp up its solar PV system installation.

**OUTPERFORM** ↔

Price: **RM2.03**  
Target Price: **RM3.05** ↔

### Share Price Performance



KLCI 1,460.07  
YTD KLCI chg -2.4%  
YTD stock price chg -14.0%

### Stock Information

Shariah Compliant	Yes
Bloomberg Ticker	TGI MK EQUITY
Market Cap (RM m)	800.0
Shares Outstanding	394.1
52-week range (H)	2.76
52-week range (L)	2.00
3-mth avg daily vol:	201,501
Free Float	51%
Beta	0.6

### Major Shareholders

Foremost Equals Sdn Bhd	37.7%
Eastspring Inv Bhd	5.0%
Kenanga Funds Bhd	2.7%

### Summary Earnings Table

FY Dec (RMm)	2022A	2023F	2024F
Turnover	1386.5	1314.2	1479.9
EBIT	127.3	119.6	145.0
PBT	124.5	118.5	145.5
<b>Net Profit</b>	<b>100.0</b>	<b>90.8</b>	<b>109.2</b>
<b>Core PATAMI</b>	<b>110.6</b>	<b>90.8</b>	<b>109.2</b>
Consensus (NP)	-	95.1	109.0
Earnings Revision	-	-5%	-
Core EPS (sen)	28.1	23.0	27.7
EPS growth (%)	17.1	-17.9	20.3
NDPS (sen)	5.9	4.8	5.5
Core PER (x)	7.2	8.8	7.3
BVPS (RM)	2.2	2.3	2.6
PBV (x)	0.9	0.9	0.8
Net Gearing (x)	N.Cash	N.Cash	N.Cash
Net Div. Yield (%)	2.9	2.3	2.7

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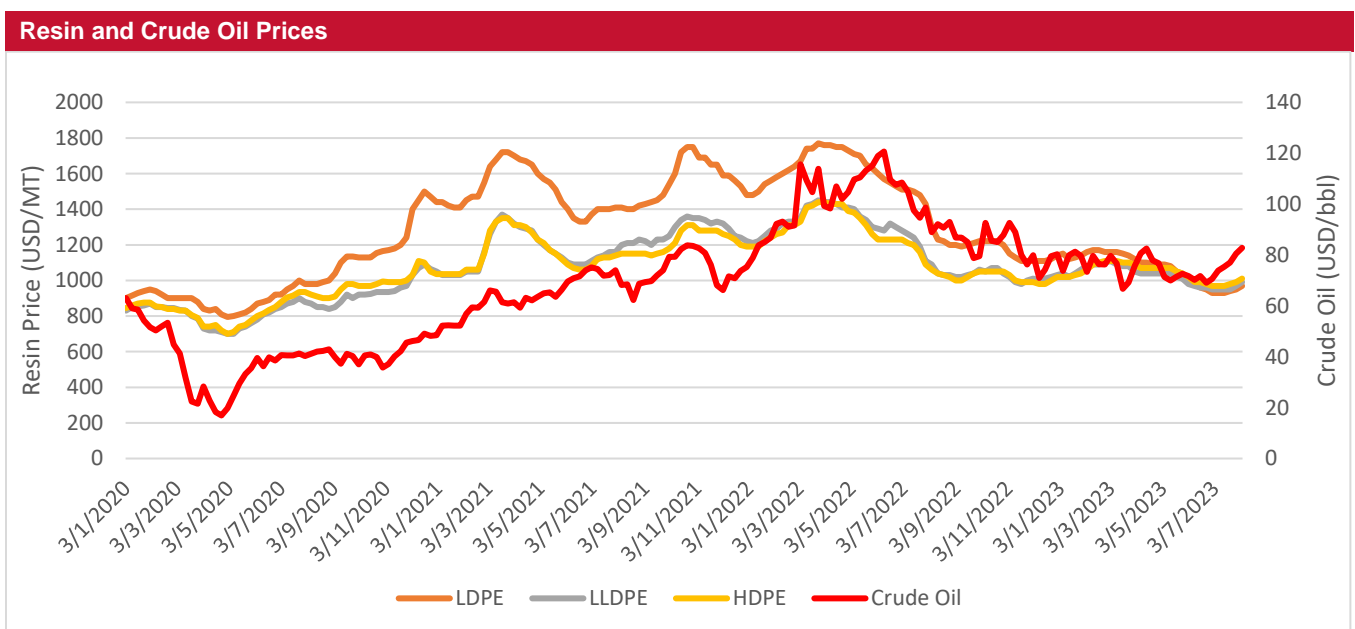
5. **Conserving cash.** TGUAN will not declare a dividend for 2QFY23 despite being in a net cash of RM63.3m. It is more inclined to channel the excess cash towards funding its on-going expansion plan as mentioned as well as to use it as a buffer in the event the global economy turns south. As such, we cut our FY23F dividend by 14% to 4.75 sen (from 5.50 sen).

**Forecasts.** We trim our FY23 earnings by 5% largely to reflect higher electricity cost.

However, we keep our TP of RM3.05 based on 11x FY24F PER, at a discount to the sector’s average historical forward PER of 13x to reflect TGUAN’s low share liquidity. There is no adjustment to our TP based on ESG given a 3-star rating as appraised by us (see Page 5).

We continue to like TGUAN due to: (i) the growth potential of the local plastic packaging sector as Malaysian players like TGUAN are gaining market shares from overseas producers that are losing competitiveness due to rising production costs, its aggressive push into the European and US markets with environmentally-friendly products. (ii) TGUAN’s earnings stability underpinned by a more diversified product portfolio and steadily growing clientele base, and (iii) its expansion plans for premium products, such as nano stretch films, courier bags, food wraps and some industrial bags (wicketed bags, oil/flour/sugar bags). Reiterate **OUTPERFORM**.

**Risks to our call include:** (i) a sudden surge in resin costs, (ii) weak demand for packaging materials due to prolonged global recession, and (iii) labour shortages and supply chain disruptions.



Source: Bloomberg, Kenanga Research

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Income Statement						Financial Data & Ratios					
FY Dec (RM m)	2020A	2021A	2022A	2023F	2024F	FY Dec	2020A	2021A	2022A	2023F	2024F
Revenue	960.6	1214.9	1386.5	1314.2	1479.9	<b>Growth (%)</b>					
EBITDA	124.7	153.6	159.1	156.4	189.8	Revenue	2.3	26.5	14.1	-5.2	12.6
Depreciation	-27.5	-30.2	-31.7	-36.8	-44.8	EBITDA	25.2	23.2	3.6	-1.7	21.4
EBIT	97.2	123.4	127.3	119.6	145.0	EBIT	29.2	26.9	3.2	-6.1	21.3
Int Exp/(Income)	1.6	1.3	-3.7	-1.1	0.4	Pre-tax Income	32.4	25.3	-0.6	-4.8	22.8
Associates P/L	1.1	0.5	0.8	0.0	0.0	Net Income	21.8	23.3	7.6	-9.2	20.3
PBT	99.9	125.2	124.5	118.5	145.5	Core Net Income	17.2	23.7	17.1	-17.9	20.3
Taxation	-19.7	-27.2	-22.8	-24.9	-30.5	<b>Profitability (%)</b>					
Minority Interest	5.0	5.1	1.7	2.8	5.7	EBITDA Margin	13.0	12.6	11.5	11.9	12.8
PATAMI	75.3	92.9	100.0	90.8	109.2	EBIT Margin	10.1	10.2	9.2	9.1	9.8
Core PATAMI	76.3	94.4	110.6	90.8	109.2	PBT Margin	10.4	10.3	9.0	9.0	9.8
						Net Margin	7.9	7.8	8.0	6.9	7.4
<b>Balance Sheet</b>						Effective Tax Rate	19.7	21.7	18.3	21.0	21.0
<b>FY Dec (RM m)</b>	<b>2020A</b>	<b>2021A</b>	<b>2022A</b>	<b>2023F</b>	<b>2024F</b>	ROE	11.8	12.9	13.5	10.2	11.1
Fixed Assets	294.8	328.6	400.2	487.0	581.8	ROA	7.5	7.7	8.4	6.5	7.2
Intangibles	2.0	3.0	4.0	5.0	6.0	<b>DuPont Analysis</b>					
Other FA	29.0	71.5	50.8	5.0	5.0	Net margin (%)	7.9	7.8	8.0	6.9	7.4
Inventories	210.2	257.5	284.8	283.7	313.3	Assets Turnover (x)	0.9	1.0	1.1	0.9	1.0
Receivables	180.1	262.7	290.6	263.8	303.6	Leverage Factor (x)	1.6	1.7	1.6	1.6	1.5
Other CA	2.8	4.5	4.0	0.0	0.0	ROE (%)	11.8	12.9	13.5	10.2	11.1
Cash	293.7	292.9	274.0	347.3	303.7	<b>Leverage</b>					
Total Assets	1012.6	1220.8	1308.4	1391.8	1513.3	Debt/Asset (x)	0.14	0.15	0.17	0.16	0.15
Payables	169.1	229.0	183.2	234.1	260.7	Debt/Equity (x)	0.23	0.25	0.27	0.26	0.23
ST Borrowings	89.8	121.0	164.8	169.8	164.8	N.Debt/(Cash)	-147.2	-106.6	-50.5	-119.3	-79.6
Other ST liability	7.6	6.4	7.0	0.0	0.0	N.Debt/Equity (x)	-0.23	-0.15	-0.06	-0.13	-0.08
LT Borrowings	56.7	65.3	58.7	58.3	59.3	<b>Valuations</b>					
Other LT liability	19.1	34.4	40.5	8.6	20.5	Core EPS (sen)	19.4	24.0	28.1	23.0	27.7
<b>Net Assets</b>	<b>645.3</b>	<b>733.8</b>	<b>821.1</b>	<b>889.6</b>	<b>981.3</b>	NDPS (sen)	2.39	5.36	5.95	4.75	5.50
Share Capital	237.1	246.5	255.5	255.5	255.5	BV/share (RM)	1.7	1.9	2.2	2.3	2.6
Reserves	408.3	487.3	565.5	640.4	733.6	Core PER (x)	10.5	8.5	7.2	8.8	7.3
<b>S. Equity</b>	<b>645.3</b>	<b>733.8</b>	<b>821.1</b>	<b>889.6</b>	<b>981.3</b>	Net Div. Yield	1.4	1.8	1.2	2.7	2.9
						PBV (x)	1.2	1.1	0.9	0.9	0.8
<b>Cashflow Statement</b>											
<b>FY Dec (RM m)</b>	<b>2020A</b>	<b>2021A</b>	<b>2022A</b>	<b>2023F</b>	<b>2024F</b>						
Operating CF	125.8	51.1	64.9	137.7	33.0						
Investing CF	-51.5	-76.6	-100.5	-50.0	-50.0						
Financing CF	-9.5	22.6	10.5	-13.7	-26.7						

Source: Kenanga Research

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## Peer Table Comparison

Name	Rating	Last Price (RM)	Target Price (RM)	Upside (%)	Market Cap (RM m)	Shariah Compliant	Current FYE	Core EPS (sen)		Core EPS Growth		PER (x) - Core Earnings		PBV (x)	ROE (%)	Net Div. (sen)	Net Div. Yld. (%)
								1-Yr. Fwd.	2-Yr. Fwd.	1-Yr. Fwd.	2-Yr. Fwd.	1-Yr. Fwd.	2-Yr. Fwd.	1-Yr. Fwd.	1-Yr. Fwd.	1-Yr. Fwd.	1-Yr. Fwd.
<b>Stocks Under Coverage</b>																	
ANCOM NYLEX BHD	OP	1.07	1.80	68.2%	1,017.4	Y	05/2024	11.8	13.9	47.1%	23.7%	9.0	7.7	1.6	19.8%	1.0	0.9%
BOILERMECH HOLDINGS BHD	MP	0.985	0.720	-26.9%	508.3	Y	03/2024	4.5	4.4	65.2%	-2.6%	21.8	22.4	1.9	9.0%	1.8	1.8%
BP PLASTICS HOLDINGS BHD	MP	1.27	1.23	-3.1%	357.5	Y	12/2023	11.8	13.7	7.1%	16.3%	10.8	9.3	1.4	13.6%	5.5	4.3%
HPP HOLDINGS BHD	OP	0.395	0.720	82.3%	153.4	Y	05/2024	4.4	5.5	81.7%	27.2%	9.1	7.1	1.1	12.9%	1.5	3.8%
KUMPULAN PERANGSANG SELANGOR	UP	0.710	0.510	-28.2%	381.5	Y	12/2023	1.3	5.1	-73.6%	279.2%	53.0	14.0	0.4	0.7%	0.0	0.0%
SCIENTEX BHD	UP	3.73	2.99	-19.8%	5,785.5	Y	07/2023	30.6	35.5	15.0%	16.0%	12.2	10.5	1.8	15.5%	7.4	2.0%
SLP RESOURCES BHD	MP	0.835	0.900	7.8%	264.7	Y	12/2023	4.8	5.9	-6.8%	23.8%	17.5	14.2	1.4	7.9%	5.5	6.6%
TECHBOND GROUP BHD	OP	0.405	0.450	11.1%	214.4	Y	06/2024	3.8	4.1	112.8%	9.5%	10.7	9.8	1.2	11.5%	1.5	3.7%
THONG GUAN INDUSTRIES BHD	OP	2.03	3.05	50.2%	800.0	Y	12/2023	23.0	27.7	-17.9%	20.3%	8.8	7.3	0.9	10.2%	4.8	2.3%
<b>Sector Aggregate</b>					<b>9,482.7</b>					<b>25.5%</b>	<b>19.7%</b>	<b>12.0</b>	<b>10.0</b>	<b>1.4</b>	<b>11.6%</b>		<b>2.8%</b>

Source: Kenanga Research

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**Stock ESG Ratings:**

	Criterion	Rating			
<b>GENERAL</b>	Earnings Sustainability & Quality	★	★	★	★
	Corporate Social Responsibility	★	★	★	★
	Management/Workforce Diversity	★	★	☆	
	Accessibility & Transparency	★	★	★	★
	Corruption-Free Pledge	★	★	★	
	Carbon-Neutral Initiatives	★	★	★	☆
	<b>OVERALL</b>	★	★	★	
<b>SPECIFIC</b>	Migrant Worker Welfare	★	★	★	
	Waste Disposal/Pollution Control	★	★	★	
	Work Site Safety	★	★	★	
	Usage of Biodegradable Materials	★	★	★	
	Supply Chain Auditing	★	★	★	
	Energy Efficiency	★	★	★	★
	<b>OVERALL</b>	★	★	★	

☆ denotes half-star  
 ★ -10% discount to TP  
 ★★ -5% discount to TP  
 ★★★ TP unchanged  
 ★★★★ +5% premium to TP  
 ★★★★★ +10% premium to TP

**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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