

# Company Focus

Malaysia Equity Research PP 11272/7/2008

12 Feb 2008

**BUY RM1.36** KLCI: 1,407.38

Price Target : 12-Month RM2.50 (Prev RM3.20)

Reason for Report : Update

Potential Catalyst : Higher MDF consumption and selling prices, capacity expansion and vertical integration.

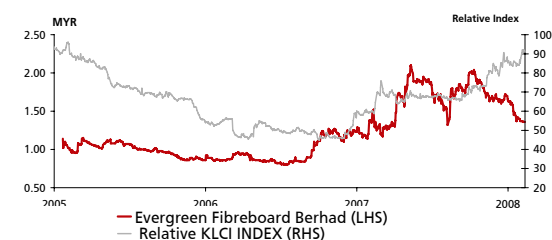
## ANALYST

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## FORECASTS AND VALUATION

FY Dec (RM m)	2006A	2007F	2008F	2009F
Turnover	528	695	757	834
EBITDA	90	174	189	218
Pre-tax Profit	68	139	144	171
Net Profit	60	112	124	146
Net Pft (Pre Ex.)	60	112	124	146
EPS (sen)	12.4	23.4	25.9	30.4
EPS Pre Ex. (sen)	12.4	23.4	25.9	30.4
EPS Gth Pre Ex (%)	10	88	11	17
Diluted EPS (sen)	12.4	23.4	25.9	30.4
Net DPS (sen)	5	6.5	7.5	9
BV Per Share (sen)	72.5	90.9	110.3	133.2
PE (X)	10.9	5.8	5.3	4.5
PE Pre Ex. (X)	10.9	5.8	5.3	4.5
P/Cash Flow (X)	8.2	4.7	4.1	3.5
EV/EBITDA (X)	8.3	4.5	4.3	3.3
Net Div Yield (%)	3.7	4.8	5.5	6.6
P/Book Value (X)	1.9	1.5	1.2	1
Net Debt/Equity (X)	CASH	0	0	CASH
ROAE (%)	18.4	28.7	25.7	25

## PRICE RELATIVE



## AT A GLANCE

Issued Capital (m shrs)		480.0
Mkt Cap (RMm/US\$m)	653.0 /	202.0
Major Shareholders (%)		
Kuo Family		42.3
Lembaga Tabung Haji		7.0
Free Float (est.)		48.8
Average daily volume (m'sh/rs)		566.00

Earnings Rev : 2008: -1%      2009: 2%  
 Concensus EPS (sen) : 2008: 27.2      2009: 32.7  
 Variance vs Cons : 2008: -4.8%      2009: -7.0%

Sector: Industrials

Bloomberg/Reuters Code: 522.MK / 0522.KL

Principal Business : MDF manufacturer

# Evergreen Fibreboard

## Expanding at the right time

➤ **Story:** FY07 growth in MDF volume could be higher than expected. Though 4Q07 net profit may be weaker q-o-q, Evergreen Fibreboard (EFB) would likely still record a strong c. 20% y-o-y growth in MDF volume for the full year of FY07, largely driven by the Middle East market.

➤ **Point:** We have upgraded our FY07 earnings forecast by 13% to RM112.4m (+88% y-o-y) to factor in higher MDF volume growth. We understand that though 4Q07 would be weaker q-o-q, it would likely be stronger y-o-y due to strong MDF demand. For FY08 and FY09, we have finetuned our earnings forecast downwards by 1% to RM124.3m (+11% y-o-y) and 2% to RM145.8m (+17% y-o-y), respectively.

➤ **Relevance:** We maintain our Buy call with a RM2.50 price target, based on 8x CY09 EPS (from RM3.20, based on 12x CY08 EPS). This is consistent with its peer average, which has corrected likely due to weaker equity market sentiment, and EFB's 3-year historical forward PE range. We continue to like EFB for its attractive valuation at 4.5x CY09 EPS with attractive dividend yield of 6.6%, bright prospects in the global MDF market, and it being the second largest MDF manufacturer in Malaysia.

**Upgrade FY07 earnings forecast, finetuned downwards for FY08-09 due to expected stronger RM.** We have upgraded our net profit forecast for FY07 by 13% as we project higher MDF volume growth of c.20% from 10% previously. We understand that though 4Q07 net profit would be weaker (due to a recent fire incident that affected one of their production lines in Johor), it would likely be stronger than 4Q06 given the continued strong MDF demand. For FY08 and FY09, we have finetuned our earnings forecast downwards by 1% and 2% respectively, largely due to the expected stronger Ringgit against the US dollar. We have imputed MYR/USD exchange rate of 3.25 each year, 1.8% lower than the previous 3.31.

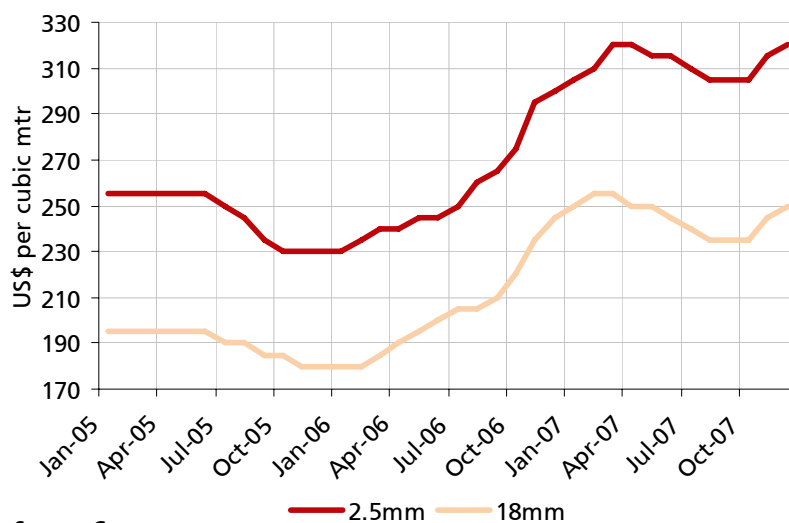
**Expansion is on track.** We understand that EFB's Indonesian plant could come onstream in Feb 08, while its new MDF line in Thailand is on track to be operational by end-08. The capacity expansion is timely as EFB has been operating at 86-88% utilisation over FY03-06.

**Catalysts for the stock** include growth in MDF volume, higher selling prices, additional contribution from its new Indonesian subsidiary, and cost savings from Indonesian subsidiary, and cost savings from producing its own glue and energy.

Highlights

- **FY07 growth in MDF volume could be higher than expected.** Though 4Q07 net profit may be weaker q-o-q, EFB would likely record a strong c. 20% y-o-y growth in MDF volume for FY07, largely driven by the Middle East market e.g. U.A.E, Saudi Arabia, and Jordan. Given the strong growth, EFB could be operating near its full capacity i.e. c. 90%.
- **FY07 average MDF prices rose 20-21% y-o-y.** This could be attributed to rising demand for MDF as it is increasingly used as a substitute for plywood and solid wood. Sustained high oil prices may help support higher MDF prices.

Figure 1: MDF Price Trend



Source: Company

- **Acquisition of the remaining 25% of its Thai MDF plant completed in 4Q07.** This results in Siam Fibreboard Company Limited being a wholly-owned subsidiary of the Group. The Group owns a MDF manufacturing plant through Siam Fibreboard in Thailand that has a total capacity of 320,000 m<sup>3</sup> p.a.
- **MDF volume is projected to grow** by 15% in FY08 and another 11% in FY09 as we expect substitution for plywood to continue and demand from emerging markets e.g. Middle East to continue to increase. FY09 would record full year contribution from the newly acquired Indonesian plant.
- **Cost savings could partially offset the expected stronger RM against the USD in FY08-09.** We project margins to soften marginally by 1ppt to 35.6% in FY08, but expand by 1.1ppts to 37.9% in FY09, aided by lower raw material costs as EFB begins to consume its own-produced glue and electricity for its plants in Malaysia and Thailand respectively in FY08. The glue plant in Johor, Malaysia, is currently under construction and on track to be operational by Mar 08, while the biomass power plant in Thailand is also on track to come onstream in 1Q08. Full year impact of the cost savings would be reflected in FY09. Note that glue and electricity are the main cost components of MDF manufacturing, accounting for 25-28% and 10-15% of the Group's total operating costs, respectively.
- **Indonesian plant to come onstream in Feb 08.** The new plant would boost the Group's MDF manufacturing capacity by 15.5% to 820,000 m<sup>3</sup> p.a. The capacity expansion is timely as EFB has been operating at 86-88% utilisation over FY03-06. In addition, the expansion to Indonesia would allow the Group to gain access to new markets and also benefiting from the low-cost environment.
- **New MDF line in Thailand is on track to be operational in end-08.** The plant is expected to boost capacity by another 33% to 1,088,000 m<sup>3</sup> p.a.

Figure 2: Expansion Summary

	2003	2004	2005	2006	2007F	2008F	2009F
<b>MDF (m<sup>3</sup> p.a.)</b>	<b>280,000</b>	<b>442,000</b>	<b>600,000</b>	<b>600,000</b>	<b>820,000</b>	<b>1,088,000</b>	<b>1,088,000</b>
Malaysia	280,000	280,000	280,000	280,000	390,000	390,000	390,000
Thailand	-	162,000	320,000	320,000	320,000	588,000	588,000
Indonesia	-	-	-	-	110,000	110,000	110,000
<b>Knock-down wooden furniture (sets p.a.)</b>	<b>1,200,000</b>	<b>1,800,000</b>	<b>1,800,000</b>	<b>1,800,000</b>	<b>1,800,000</b>	<b>1,800,000</b>	<b>1,800,000</b>
<b>Particleboard (m<sup>3</sup> p.a.)</b>	<b>120,000</b>	<b>120,000</b>	<b>120,000</b>	<b>120,000</b>	<b>120,000</b>	<b>120,000</b>	<b>120,000</b>
<b>Glue (MT p.a.)</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>150,000</b>	<b>284,000</b>	<b>284,000</b>	<b>284,000</b>
Malaysia	-	-	-	-	84,000	84,000	84,000
Thailand	-	-	-	150,000	150,000	150,000	150,000
Indonesia	-	-	-	-	50,000	50,000	50,000
<b>Electricity – biomass power plant, Thailand</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>9.6MW &amp; 20 tons of steam</b>	<b>9.6MW &amp; 20 tons of steam</b>

Source: Company, HwangDBS Vickers Research

### Key Assumptions

	2007F	2008F	2009F
<b>MDF prices (in USD)</b>			
2.5mm	312.1	312.1	312.1
18mm	245.4	245.4	245.4
<b>Y-o-y price change</b>			
2.5mm	22%	0%	0%
18mm	20%	0%	0%
<b>MYR/ USD rate</b>	<b>3.55</b>	<b>3.25</b>	<b>3.25</b>
<b>MDF Volume Growth</b>	<b>21%</b>	<b>15%</b>	<b>11%</b>
<b>Potential cost savings</b>	<b>-</b>	<b>RM16m</b>	<b>RM26m</b>

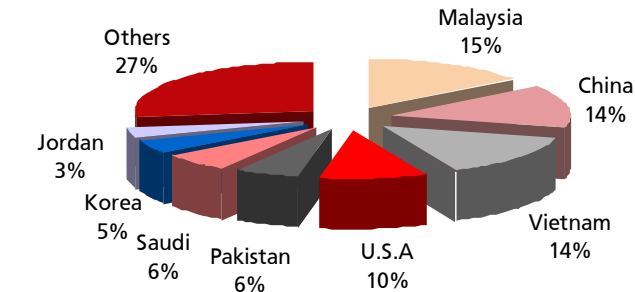
Source: HwangDBS Vickers Research

### Key Risks

- **Weakening USD against RM could adversely impact earnings** given that overseas revenue accounts for 85% of the Group's total revenue (FY06). However, EFB partly mitigates this risk by hedging half of its total overseas revenue. Our sensitivity analysis shows a 1% increase in USD against RM could drag earnings by 3.5% to RM119.9m in FY08 and 3.2% to RM141.1m in FY09.

- **Economic slowdown in US and Japan may adversely impact global MDF demand.** We understand that EFB's share of FY07 revenue from the US has shrunk to 7% from 10% in FY06, as American buyers are becoming more cautious due to the expected economic slowdown there. We believe the Group's diversified customer base, i.e. c.45 countries, will help to spread the risks rather than being largely exposed to market downturn in these countries. Revenue from the US accounted for 10% of EFB's total FY06 revenue, while Japan accounted for less than 3%.

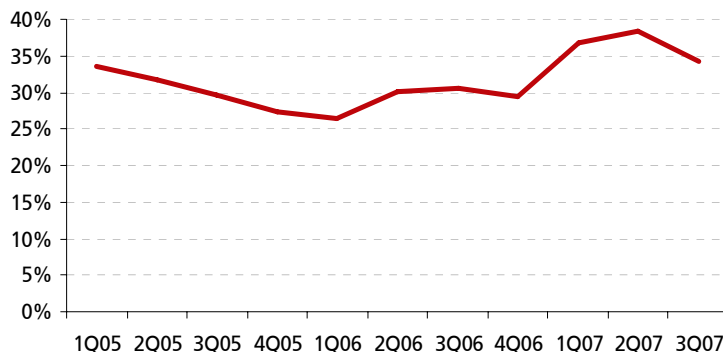
**Figure 3: EFB has a diversified customer base**



Source: Company

- **Higher manufacturing costs with rising methanol and oil prices.** Methanol is used as the feedstock for the production of glue. Glue cost is one of the main cost components in MDF manufacturing, i.e. 25-28% of total operating costs for EFB.
- **For freight costs, rising bunker fuel prices due to high oil prices could drive up freight rates.** The freight costs vary depending on the markets e.g. of total operating costs, South East Asia and Far East account for c.5%, while Middle East accounts for c.20%. To mitigate the rising costs, EFB could raise its selling prices and pass on the cost increase (with 1-2 months lag). We understand that at least 70% of the common manufacturing costs that are affected by global changes e.g. methanol and oil prices, can be passed on to customers.

**Figure 4: Historical gross margins**

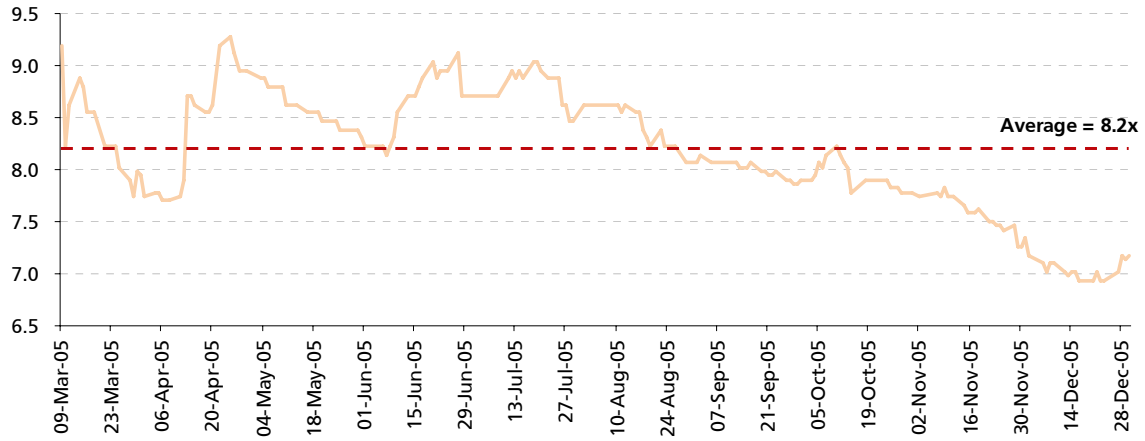


Source: Company

**Valuation**

- **Compelling valuation at 4.5x CY09 EPS and attractive dividend yield of 6.6%.** We expect dividend payout of 30% each year for FY07-09F. Hence, we project the Group to pay out net dividend of 6.5 sen per share in FY07, 7.5 sen per share in FY08, and 9.0 sen per share in FY09, which translates into 4.8%, 5.5%, and 6.6% net dividend yield, respectively. Thus far, EFB has declared an interim dividend (tax-exempted) of 2.5 sen per share for FY07.
- **We maintain our Buy call with a RM2.50 price target,** based on 8x CY09 EPS (from RM3.20, based on 12x CY08 EPS). This is consistent with its peer average, which has corrected likely due to weaker equity market sentiment, and EFB's 3-year historical forward PE range.

**EFB's Historical 3-Year Forward PE**



Source: Bloomberg

**Peers Valuation**

	Market Cap (USDm)	CY07F PE (x)	CY08F PE (x)	CY09F PE (x)	CY09 Dividend Yield (%)
Vanachai Group PCL	151.1	6.9	6.4	5.1	9.1
Sumalindo Lestari Jaya Tbk PT	376.3	24.1	11.8	9.3	0.0
Pfleiderer Grajewo SA	829.5	14.3	12.6	11.2	3.9
Evergreen Fibreboard	202.0	5.8	5.3	4.5	6.6
<b>Average (ex EFB)</b>		<b>15.1</b>	<b>10.2</b>	<b>8.5</b>	

Source: Bloomberg, HwangDBS Vickers Research

## Company Focus

## Evergreen Fibreboard

### Income Statement (RM m)

FY Dec	2006A	2007F	2008F	2009F
Turnover	528	695	757	834
Cost of Goods Sold	(375)	(441)	(488)	(528)
<b>Gross Profit</b>	<b>153</b>	<b>254</b>	<b>269</b>	<b>306</b>
Other Opng (Exp)/Inc	(85)	(110)	(120)	(129)
<b>Operating Profit</b>	<b>68</b>	<b>144</b>	<b>150</b>	<b>176</b>
Other Non Opng (Exp)/Inc	0	0	0	0
Associates & JV Inc	2	2	3	3
Net Interest (Exp)/Inc	(3)	(7)	(8)	(8)
Exceptional Gain/(Loss)	0	0	0	0
<b>Pre-tax Profit</b>	<b>68</b>	<b>139</b>	<b>144</b>	<b>171</b>
Tax	(3)	(12)	(12)	(14)
Minority Interest	(5)	(15)	(8)	(12)
Preference Dividend	0	0	0	0
<b>Net Profit</b>	<b>60</b>	<b>112</b>	<b>124</b>	<b>146</b>
Net Profit before Except.	60	112	124	146
EBITDA	90	174	189	218
Sales Gth (%)	15.4	31.6	8.9	10.2
Opg Profit Gth (%)	21.1	111.4	3.7	17.9
Net Profit Gth (%)	9.6	88.2	10.5	17.3
Effective Tax Rate (%)	3.8	8.4	8.1	8.1

### Cash Flow Statement (RM m)

FY Dec	2006A	2007F	2008F	2009F
Pre-Tax Profit	68	139	144	171
Dep. & Amort.	22	30	39	42
Tax Paid	(2)	(1)	(12)	(12)
Assoc. & JV Inc/(loss)	(2)	(2)	(3)	(3)
Chg in W/kg.Cap.	1	(45)	(9)	(10)
Other Operating CF	(4)	(4)	(4)	(4)
<b>Net Operating CF</b>	<b>83</b>	<b>117</b>	<b>156</b>	<b>184</b>
Capital Exp.(net)	(123)	(113)	(133)	(36)
Other Invts.(net)	5	5	5	5
Invts in Assoc. & JV	0	0	0	0
Div from Assoc & JV	0	0	0	0
Other Investing CF	(8)	(8)	(8)	(8)
<b>Net Investing CF</b>	<b>(126)</b>	<b>(116)</b>	<b>(136)</b>	<b>(39)</b>
Div Paid	(19)	(24)	(31)	(36)
Chg in Gross Debt	88	17	0	0
Capital Issues	0	0	0	0
Other Financing CF	0	0	0	0
<b>Net Financing CF</b>	<b>69</b>	<b>(7)</b>	<b>(31)</b>	<b>(36)</b>
Net Cashflow	26	(6)	(10)	109

### Quarterly / Interim Income Statement (RM m)

FY Dec	4Q2006	1Q2007	2Q2007	3Q2007
Turnover	137	167	193	202
Cost of Goods Sold	(97)	(105)	(119)	(133)
<b>Gross Profit</b>	<b>40</b>	<b>61</b>	<b>74</b>	<b>69</b>
Other Oper. (Exp)/Inc	(20)	(25)	(29)	(32)
<b>Operating Profit</b>	<b>20</b>	<b>36</b>	<b>45</b>	<b>38</b>
Other Non Opng (Exp)/Inc	0	0	0	0
Associates & JV Inc	1	1	1	1
Net Interest (Exp)/Inc	(1)	(2)	(2)	(2)
Exceptional Gain/(Loss)	0	0	0	0
<b>Pre-tax Profit</b>	<b>20</b>	<b>35</b>	<b>44</b>	<b>37</b>
Tax	(1)	(2)	(7)	(2)
Minority Interest	(1)	(5)	(5)	(3)
<b>Net Profit</b>	<b>19</b>	<b>28</b>	<b>32</b>	<b>32</b>
Net profit bef Except.	19	28	32	32
EBITDA	21	37	45	39
Sales Gth (%)	(0.7)	21.7	15.5	5.1
Opg Profit Gth (%)	(4.1)	81.2	22.6	(15.4)
Net Profit Gth (%)	27.2	161.1	127.6	72.6
Gross Margins (%)	29.4	36.8	38.4	34.2
Opg Profit Margins (%)	14.6	21.8	23.1	18.6

Source: Company, DBS Vickers

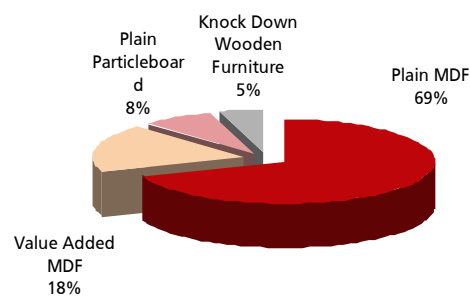
### Balance Sheet (RM m)

FY Dec	2006A	2007F	2008F	2009F
Net Fixed Assets	361	444	538	532
Invts in Associates & JVs	16	18	21	24
Other LT Assets	23	23	22	30
Cash & ST Invts	147	141	131	240
Other Current Assets	120	176	188	202
<b>Total Assets</b>	<b>667</b>	<b>802</b>	<b>900</b>	<b>1,027</b>
ST Debt	14	11	11	11
Other Current Liab	56	78	81	87
LT Debt	130	151	151	151
Other LT Liabilities	16	8	0	0
Shareholder's Equity	426	514	607	717
Minority Interests	26	41	49	61
<b>Total Cap. &amp; Liab.</b>	<b>667</b>	<b>802</b>	<b>900</b>	<b>1,027</b>
Non-Cash W/kg. Capital	65	110	119	129
Net Cash/(Debt)	3	(21)	(31)	78

### Rates & Ratio

FY Dec	2006A	2007F	2008F	2009F
Gross Margins (%)	29.1	36.6	35.6	36.7
Opg Profit Margin (%)	12.9	20.8	19.8	21.2
Net Profit Margin (%)	11.3	16.2	16.4	17.5
ROAE (%)	18.4	28.7	25.7	25.0
ROA (%)	10.1	15.3	14.6	15.1
ROCE (%)	15.5	25.7	21.8	22.1
Div Payout Ratio (%)	40.2	27.8	29.0	29.6
Net Interest Cover (x)	25.4	20.0	18.5	21.8
Asset Turnover (x)	0.9	0.9	0.9	0.9
Debtors Turn (avg days)	33.2	28.6	31.2	31.1
Creditors Turn (avg days)	26.4	26.8	27.7	27.8
Inventory Turn (avg days)	56.0	57.9	58.9	59.1
Current Ratio (x)	3.8	3.6	3.5	4.5
Quick Ratio (x)	2.9	2.7	2.6	3.6
Net Debt/Equity (X)	CASH	0.0	0.0	CASH
Capex to Debt (%)	84.9	70.0	81.9	22.3
N. Cash/(Debt)PS (sen)	0.6	(4.3)	(6.4)	16.3
Opg CFPS (sen)	17.0	33.6	34.4	40.5
Free CFPS (sen)	(8.4)	0.8	5.0	30.9


### Revenue Breakdown in 2006



Source: Company

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