SJ SECURITIES SDN BHD

RESULTS UPDATE

Degem Bhd (DGEM)		***Price:***	*RM 0.73 @ Feb 06*
		Market capitalisation:	*RM97.82mn*
		Board:	*Main*
		Sector:	*Consumer Products*
Stock Code:	7119	***Recommendation:***	*SELL*

Key stock statistics	2004	2005
EPS (sen)	8.38	3.60
P/E (x)	16.11	18.34
Dividend/Share (RM)	0.02	0.02
NTA/Share (RM)	0.76	0.81
Book Value/Share (RM)	0.76	0.83
Issued capital (mn shares)	126.00	134
52-weeks Share Price Range (RM)	RM0.60-RM1.44	RM1.34-RM1.75
Government	-	
Qthers (spesify)	Legion Master Sdn Bhd (51.72%)	

Quarterly Results	4Q 2004 RMmn	3Q 2005 RMmn	4Q 2005 RMmn	Change QoQ %	Change YoY %
Revenue	41.2	30.0	26.2	(12.6)	(36.3)
EBIT	3.6	2.8	0.0	(98.7)	(99.0)
Interest Expenses	(0.4)	(0.4)	(0.3)	(25.3)	(21.1)
Pre –tax Profit	3.2	2.4	(0.3)	(110.8)	(108.0)
Net Profit	1.3	1.5	(0.1)	(108.2)	(109.9)
EBIT Margin (%)	13.7	9.2	0.1	(98.5)	(98.4)
Pre-tax Margin (%)	12.3	7.9	(1.0)	(112.4)	(112.6)
Net Margin (%)	4.9	5.1	(0.5)	(109.4)	(115.6)
Basic EPS (sen)	1.00	1.14	(0.09)	(107.9)	(109.0)

Per Share Data	**2003**	**2004**	**2005**	**2006E**
Book Value (RM)	0.70	0.76	0.83	0.85
Cash Flow (RM)	-	-	0.00	0.02
Earnings (RM)	0.10	0.08	0.04	0.04
Dividend (RM)	0.03	0.02	0.02	0.02
Payout Ratio(%)	23.99	23.86	60.34	50.43
PER (x)	14.01	16.11	18.34	13.00
P/Cash Flow (x)	-	-	567.74	25.78
P/Book Value (x)	2.09	1.77	0.80	0.61
Dividend Yield (%)	1.71	1.48	3.29	3.88
ROE (%)	14.88	11.00	4.36	4.71
Net Gearing (x)	0.14	0.24	0.26	0.07

Cumulative Quarterly Results	4Q04 RMmn	4Q05 RMmn	Change YTD %
Revenue	135.3	108.2	(20.1)
EBIT	17.8	8.2	(53.6)
Interest Expenses	(1.6)	(1.3)	(16.1)
Pre – tax Profit	16.2	6.9	(57.3)
Net Profit	10.6	4.8	(54.6)
EBIT Margin (%)	13.1	7.6	(42.0)
Pre-tax Margin (%)	12.0	6.4	(46.5)
Net Margin (%)	7.8	4.4	(43.2)
Basic EPS (sen)	8.38	3.60	(57.0)

P&L Analysis (RMmn)	**2003**	**2004**	**2005**	**2006E**
Year-end: 31st Dec				
Revenue	114.0	135.3	108.2	112.0
EBIT	20.6	17.8	8.2	9.0
Depreciation	(1.6)	(1.8)	(1.9)	(1.5)
Interest Expenses	(1.3)	(1.6)	(1.3)	(0.4)
Pre-tax Profit	19.4	16.2	11.3	7.5
Taxation	(4.6)	(4.0)	(2.1)	(2.1)
Net Profit	13.1	10.6	4.8	5.3
EBIT Margin (%)	18.1	13.1	7.6	8.0
Pre-tax Margin (%)	17.0	12.0	6.4	6.7
Net-Margin (%)	11.5	7.8	4.4	4.7
Revenue Growth (%)	11.5	18.7	(20.1)	3.5
EBIT Growth (%)	15.2	(13.9)	(53.6)	9.2
Pre-tax Growth (%)	14.6	(16.3)	(57.2)	8.5
Net Growth (%)	11.9	(19.6)	(54.6)	10.8

1.0 Results Commentary

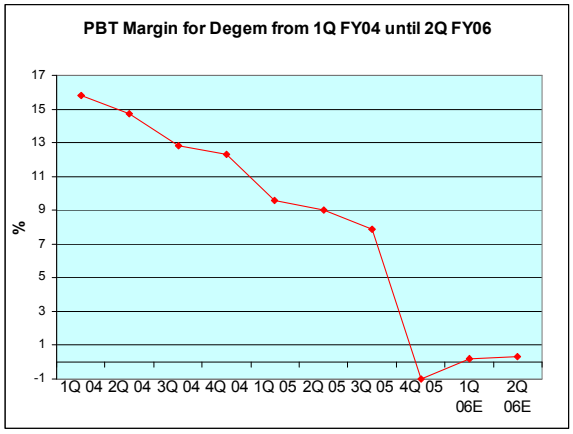
Degem reported disappointing results for FY05. The Group registered a sharp fall of 109.9% in net profit to a loss of RM125,000 in 4QFY05 from RM817,000 a year ago. Its revenue declined 36.3% to RM26.2mn from RM41.2mn during the same period. The lower sales and net profit were mainly due to stiff competition and lower margin.

Compared to its preceding quarter, both the revenue and net profit decline of 12.6% and 108.2% respectively to RM26.2mn and a loss of RM125,000. Sales for 4Q were lower, and the traditionally high festive season sales did not meet the Group's expectation.

For FY05, the Group's revenue declined 20.1% from RM135.3mn to RM108.2mn as compared to last FY. The net profit declined 54.6% from RM10.6mn to RM4.8mn. According to the management, lower sales and net profit for the year were mainly due to stiff competition and lower margin.

2.0 Outlook

The Group had been experiencing a decline in PBT margin since 1Q FY04. We had earlier anticipated the trend to continue in FY05 due to stiff competition and a weaker consumer purchasing power. However, we did not expect the margin to dip to negative 1% in 4Q FY05.



The Group has proposed to dispose two showrooms and some properties. The gross proceed of RM20.4mn arising from the disposal will be utilised as working capital, resulting in gross interest saving of approximately RM854,700 per annum. In addition, we believe the operating cost will be reduced significantly upon completion of disposal. Earlier on, the Group had shut down a Diamond & Platinum outlet.

Going forward, we expect the margin to improve in FY06, at least to breakeven. Nonetheless, we are pessimistic in Degem due to following reasons:-

- Growth and profitability in Degem have been declining significantly since 2004 whilst other players are maintaining or expanding their growth and profitability margin.
- Compare to its competitors, the Group does not have a good distribution network and geographical coverage throughout Malaysia. There are limited outlets available in strategic locations.

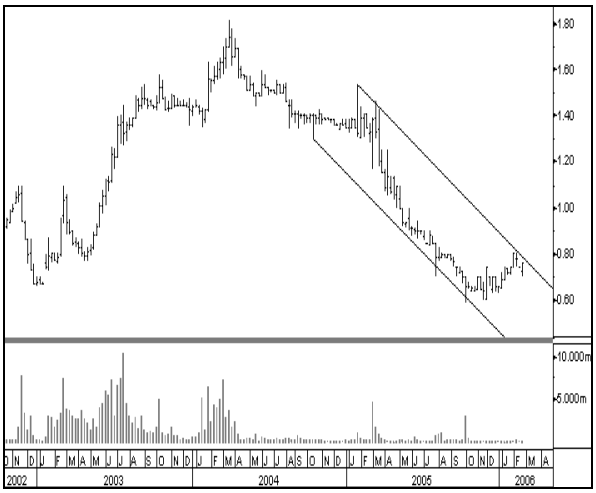
We foresee a continual down trend in net profit for FY06 as number of show rooms had reduced, hence reduce future earnings contribution.

3.0 Recommendation

EPS FY05 of 3.60sen is 36.8% lower than our expectation of 5.7sen. The unexpected disappointing result was due to unexpected lower sales in 4Q.

We reiterate our **SELL** recommendation at target price of RM0.52, pegging to a PY06 PE of 13x, based on weighted average PE in jewellery industry.

4.0 Share Price Chart



DEGEM (Stock code: 7119) – Overbought

Resistance: 0.81
Support: 0.50, 0.64

Share price is at 0.73 on 2/3/06. The recent technical rebound from the July 2005 low at 0.59 appears to be capped at the downtrend line of 0.81 in February 2006. A consolidation is expected for the near term. However, a dip below 0.64 will lead to a test on the 0.50 support level.

The accuracy or completeness of the information provided herein is not guaranteed and opinions are subject to change without notice. This report is for information of clients only and should not be construed as a solicitation for contracts. We accept no liability for any direct or indirect loss arising from the use of this document. We, our associates, directors or employees may have an interest in the securities and/or companies mentioned herein.