

Kim Teck Cheong Consolidated Bhd

Initial Public Offering

STAG

IPO Price	RM 0.15
Fair Value	RM 0.20

IPO Summary

Public Issue of Ordinary Shares	142m
Issuance of RCPS (pre-IPO)	24m
Retail Offer	34m
Eligible Contributor	16.2m
Placement	91.7m
Market Cap	RM76m

Major Shareholders (%)

KTC Holdings	72.1%
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Indicative Timetable

Opening of application for IPO	28/10/15
Closing of application for IPO	12/11/15
Balloting of shares	16/11/15
Allotment of shares	23/11/15
Listing on the Ace Market	25/11/15

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Driving Growth in East Malaysia

We assign a PER of 13.0x pegged to KTC's FY17 fully diluted EPS of 1.52sen, a discount to its peers Yee Lee Corporation and DKSH Holdings while assigning a premium to Harrisons Holdings. Our recommendation is STAG with a target price RM0.20. Size-wise (market share), KTC is 90%, 80% and 62% smaller than Yee Lee, DKSH and Harrisons. Due to its earnings growth visibility, KTC deserves a valuation premium over Harrisons. Our target price implies an upside of 33%.

Quick View

Kim Teck Cheong Consolidated Bhd (KTC) is a Sabah-based consumer packaged goods (CPG) distributor. The group plans to expand its distribution business to Sarawak and Brunei. The group also distributes its CPG in Labuan. In 2013, the company ventured into CPG manufacturing and aims at boosting its own distribution of its own brands.

We forecast earnings growth at 14.9% and 25% and PAT at RM8.1m and RM10.2m in FY16 and FY17 respectively, underpinned by expansion of its warehousing and bakery capacity.

Table 1 :Investment Highlights & Earnings Forecasts

FYE June	FY12	FY13	FY14	FY15	FY16(F)	FY17(F)
Revenue (m)	200.3	222.7	229.5	299.9	338.1	356.9
PBT (m)	5.6	13.6	7.4	10.4	11.1	13.7
PAT (m)	4.0	11.7	5.6	7.1	8.1	10.2
Fully Diluted EPS (sen)	0.59	1.75	0.83	1.06	1.21	1.52
Earnings Growth (%)	NA	195.8	-52.7	27.5	14.9	25.0
GP Margin (%)	12.83	12.28	12.57	13.70	13.80	14.44
PBT Margin (%)	2.8	6.1	3.2	3.5	3.3	3.8
PAT Margin (%)	2.0	5.3	2.4	2.4	2.4	2.8
PER (x)	25.3	8.6	18.1	14.2	12.4	9.9
DPS (sen)	0.0	0.0	0.0	0.0	0.0	0.0
Dividend Yield (%)	0.0	0.0	0.0	0.0	0.0	0.0
ROE (%)	NA	NA	NA	7.5	7.9	9.0
ROA (%)	NA	NA	NA	3.1	3.5	4.1
Net Gearing Ratio (%)	NA	NA	NA	24.2	23.0	20.1
Price/Book Ratio (x)	NA	NA	NA	1.06	0.98	0.89

Source: Company

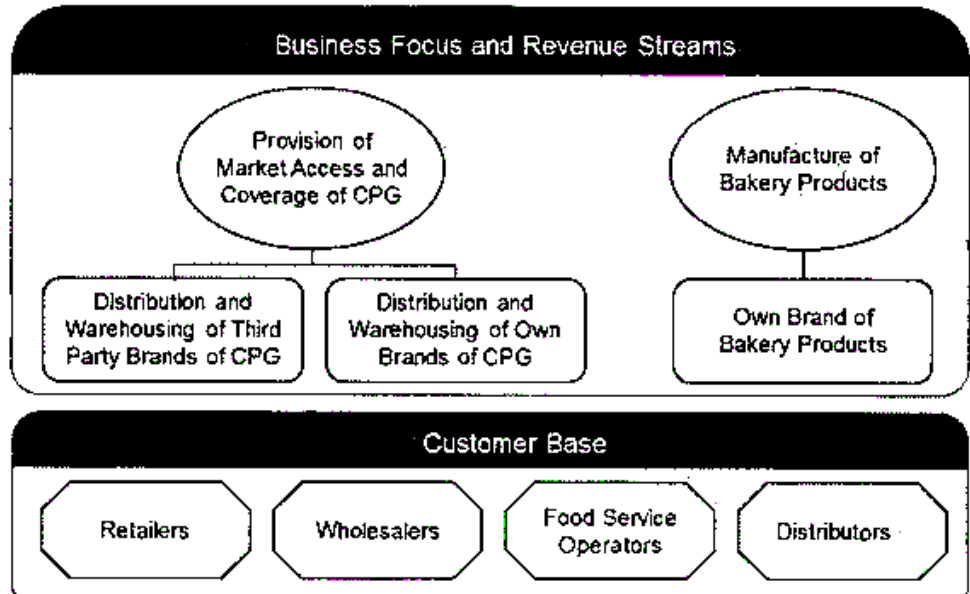
Corporate Background and Structure

Exhibit 2:- Corporate Structure

	Ownership	Principal Activities
AMDA Marketing (Sabah) Sdn Bhd	100%	Distribution of CPG
Creamos (Malaysia) Sdn bhdK	100%	Manufacture bakery products
Kim Teck Cheong Brands Sdn Bhd	100%	Brand owner (Orie and Bamble) and procurement arm for own brand products
Kim Teck Cheong Distribtuion Sdn Bhd	100%	Distribution of CPG
Kim Teck Cheong (Sarawak) Sdn Bhd	80%	Distribution of CPG InSarawak
Kim Teck Cheong Sdn Bhd	100%	Distribution of CPG
Kim Teck Cheong (Tawau) Sdn Bhd	100%	Distribution of CPG in Tawau

Source: Company

Exhibit 2:- Operation Segment



Source: Company

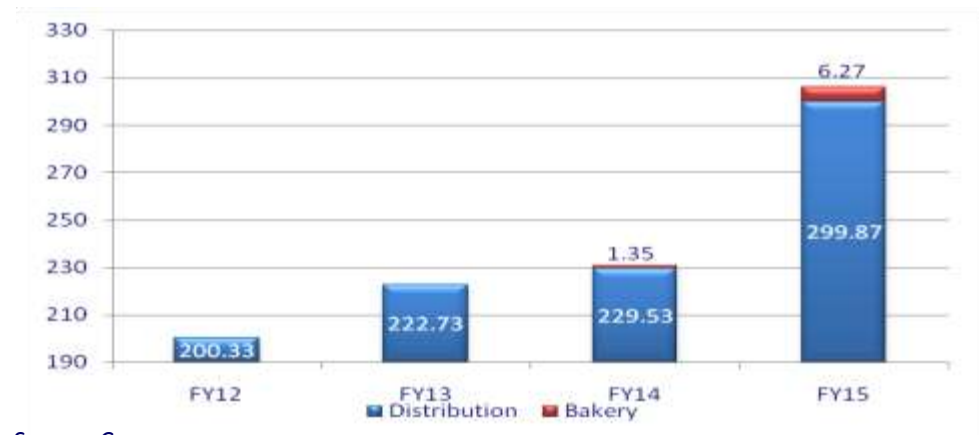
Management team

- **Y. Bhg. Datuk Lau Koh Shing @ Lau Kok Sing** (Managing Director/Chairman): Took over the operation of his business from his late father, Datuk Lau Yeong Ching. Responsible for developing overall strategic direction and was involve in the business for more than 50 years. Currently the National Vice President of the Malaysia-China Chamber of Commerce and President of the Sabah chapter of the Malaysia-China Chamber of Commerce
- **Lim Hui Kiong** (Executive Director): He worked with DKSH Malaysia as sales representative before co founding KTC with Datuk Lau Koh Shing. Played a key role in growing the company by focusing on providing market access and coverage of CPG products in Sabah. Subsequently appointed as director in KTC Sarawak in 2013.
- **Lau Wei Dick @ Dexter Dick Lau** (Executive Director): Appointed in 2013, responsible for the group day to day management and established the group's bakery operation.

Segment Information

Business segments

Exhibit 3:- Operation Segment Breakdown



Source: Company

The group distributes 194 third party brands of CPG and 36 brand owners. The group covers food products including dry frozen, and chilled food, as well as beverages while non-food products includes personal care, household, baby care, OTC drugs and health supplements. Prominent brands under that portfolio are Coca-cola, P&G, Danone Dumex and Winpro Unza. The group also distributes their own brand of CPG which includes bakery products and frozen food. The group runs 18 distribution centers in East Malaysia with a prominent pivot in Sabah.

Exhibit 4: CPG brands portfolio



Source: Company

The group commenced manufacturing of bakery products in 2014 and holds a Halal certification sold under the 'Cremos' brand. The 'Cremos' brand is sold in Kota Kinabalu and Sandakan and products are available at various outlets including hypermarkets, supermarkets, sundry shops, convenience store, petrol kiosk, Chinese medical halls and school canteen.

IPO Utilization

Increased exposure in Sarawak

Exhibit 5: IPO Utilization

	RM(m)	Time Frame	%
Acquisition of warehousing (Sarawak)	11.0	Within 24 months	36%
Construction of new warehouse (Sabah)	9.0	Within 18 months	30%
Bakery production line	3.0	Within 12 months	10%
Working Capital	4.7	Within 12 months	16%
Estimated Listing Expenses	2.6	Upon Listing	9%
Total	30.3		

Source: Company

The group plans to add an additional 75k sq ft of warehousing space, up from its current 283k sq ft. The group intends to relocate its existing distribution centers in Sibul, Miri and Kuching from rented premises by acquisition of warehouses of 15k sq ft each respectively. Furthermore, the group intends to construct an additional warehouse facility of 35,914 sq ft in Sabah. For its bakery segment, the group will increase output to 104k from 38k per shift with the installation of 4 production lines (3 in Sabah and 1 in Sarawak).

Future plans

- Establish a new distribution centre in Burnei
- Acquisition of warehouse facilities in Sibul, Miri and Kuching, Sarawak
- Construction of new warehousing facilities in Kota Kinabalu, Sabah
- Expansion of own brands of CPG
- Expansion of manufacturing operations
- Expansion of bakery products

Exhibit 5: Capacity forecast

Capacity	2015	2017(F)
Warehousing Space (sq ft)	202,000	232,000
Pallets	9,817	11817
Utilization rate	86%	82%
Pastry Output	51,200	104,200
Utilization rate	74%	74%

Source: Company, Inter-Pacific

Merits and Threats

Merits and Strengths

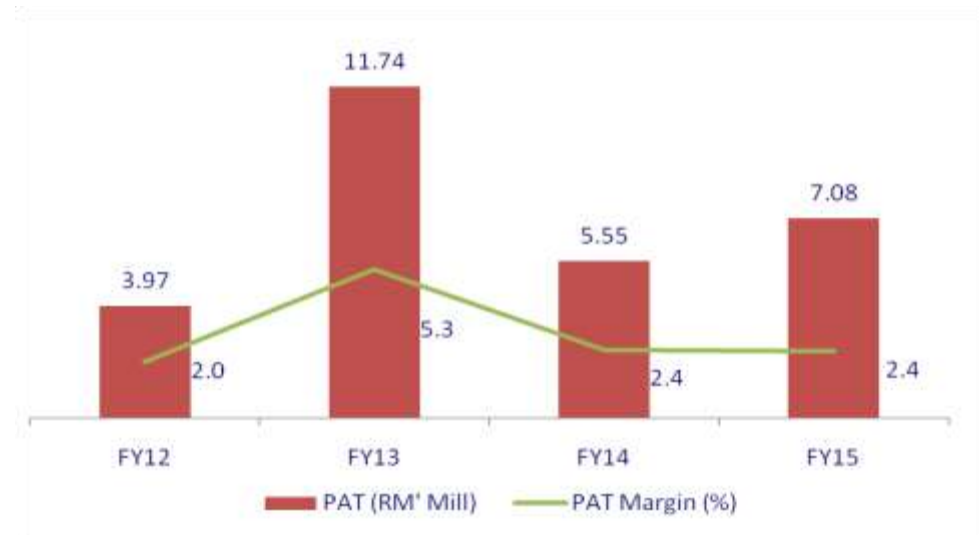
- **Extensive network:** The group is one of the top 3 in players in the tier one category. It boasts a history and long experience in CPG distribution for 76 years and has established 6,419 sales and distribution points covering over 80 districts. The group's extensive network can help it secure new agency distributorships.
- **Own brand growth:** In the pipeline is the group's expansion of distribution for its own brands such as Creamos, Orie and Bamble (bakery, and personal health care products). KTC can ride on its distribution arm for strategic sales channel and cost savings from distribution. Own brand products fetch higher margins than third party brands and will drive future margin expansion.

Weakness

- **Changing of partners:** As strong as KTC's network may be, it is still vulnerable to loss of distribution rights to any of its CPG products.

Financials

Exhibit 6: PAT vs PAT Margin



Source: Company

In FY2013, PAT and PAT margin expanded to RM11.74m and 5.27% from RM3.97m and 2% respectively, mainly due to net asset revaluation. In the subsequent year, PAT fell to RM5.55m and margin dropped to 2.4% respectively, after the low base effect faded. FY2013 PAT and PAT margin performance was stronger compared to FY2012 due to higher sales from milk products (Danone Dumex), frozen food and personal care

products (Wirpo Unza). Lastly in FY15, PAT jump to RM7.08m while margins held, with the rise in earnings underpinned by higher beverage sales (new Coca-Cola dealership).

Valuation and Recommendation

We assign a PER of 13.0x pegged to KTC's FY17 EPS of 1.52sen, fully diluted for the Redeemable Convertible Preference Shares (RCPS) issued to shareholders prior to the IPO. This is a discount to valuations for its peers Yee Lee Corporation and DKSH Holdings but a premium to that for Harrison Holdings. We recommend subscribing with a STAG view and a target price of RM0.20. Capitalisation-wise (market share), KTC is 90%, 80% and 62% smaller than Yee Lee, DKSH and Harrison's respectively. Due to foreseeable earnings growth, KTC deserves a premium over valuations for Harrison's. The target price implies an upside of 33%. The group does not have a fixed dividend policy but we do anticipate it will announce dividend payouts.

Table 6 : Peer Comparison as at 11/11/15

Company	Price (RM)	Market Cap(RM m)	Trailing PER (x)	Forward PER (x)	P/B (x)	Gearing (%)	ROE (%)	Dividend Yield (%)
KTC	0.15	76	14.2	9.9	1.0	24	7.5	NA
Harrison	3.36	232	10.8	NA	0.8	18	3.5	4.4
Yee Lee	1.92	351	15.0	13.2	0.9	15	6.5	1.5
DKSH	4.61	733	13.5	NA	1.5	0	11.7	2.0

Source: Inter-Pacific and Bloomberg

Appendix: Key Details of RCPS

Issue Size	24m
Issue Price	RM1.00 for each RCPS
Par Value	RM1.00 for each RCPS
Dividend Rate	0%
Tenure	5 years
Issue Date	1-Jul-15
Maturity Date	30-Jun-20
Conversion Price	RM0.15
Conversion Ratio	1 RCPS is convertible into 6.66 shares approximately
Conversion Period	Any time from issue date until maturity date

Ratings System

Ratings:	Description:
BUY	Total return is expected to exceed 15% in the next 12 months
NEUTRAL	Total return is expected to be between above -15% to 15% in the next 12 months
SELL	Total return is expected to be below -15% in the next 12 months

Abbreviation

Abbreviation	Definition	Abbreviation	Definition
PER	Price Earnings Ratio	CAGR	Compounded Annual Growth Rate
PEG	PER to Growth	CAPEX	Capital Expenditure
EPS	Earnings per Share	DPS	Dividend per Share
FYE	Financial Year End	ROA	Return on Asset
FY	Financial Year	ROE	Return on Equity
CY	Calendar Year	PBT	Profit Before Tax
MoM	Month-on-Month	PAT	Profit After Tax
QoQ	Quarter-on-Quarter	EV	Enterprise Value
YoY	Year-on-Year	EBIT	Earnings Before Interest And Tax
YTD	Year-to-Date	EBITDA	EBIT Depreciation & Amortisation
p.a.	Per Annum	WACC	Weighted Average Cost of Capital
DCF	Discounted Cash Flow	NTA	Net Tangible Asset
FCF	Free Cash Flow	BV	Book Value
NAV	Net Asset Value		

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