

# Company Guide

# SKP Resources Bhd

Version 1 | Bloomberg: SKP MK | Reuters: SKPR.KL

Refer to important disclosures at the end of this report

Malaysia Equity Research

18 Apr 2016

## BUY

**Last Traded Price:** RM1.35 (KLCI : 1,727.99)

**Price Target :** RM1.78 (32% upside) (Prev RM1.78)

**Shariah Compliant:** Yes

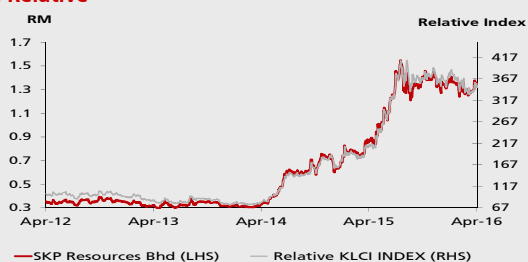
**Potential Catalyst:** New projects; higher utilisation at new Senai, Johor plant

**Where we differ:** Lower estimated earnings accretion from recent Dyson contracts

### Analyst

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### Price Relative



### Forecasts and Valuation

FY Mar (RMm)	2015A	2016F	2017F	2018F
Revenue	619	1,071	2,014	2,268
EBITDA	64.6	123	232	261
Pre-tax Profit	55.8	107	204	232
Net Profit	42.3	80.1	153	174
Net Pft (Pre Ex.)	42.3	80.1	153	174
Net Pft Gth (Pre-ex) (%)	44.3	89.3	90.5	14.0
EPS (sen)	4.70	6.95	12.2	13.9
EPS Pre Ex. (sen)	4.70	6.95	12.2	13.9
EPS Gth Pre Ex (%)	44	48	75	14
Diluted EPS (sen)	4.70	6.40	12.2	13.9
Net DPS (sen)	2.36	3.48	6.09	6.95
BV Per Share (sen)	16.9	25.1	29.2	36.1
PE (X)	28.7	19.4	11.1	9.7
PE Pre Ex. (X)	28.7	19.4	11.1	9.7
P/Cash Flow (X)	53.2	nm	14.2	7.3
EV/EBITDA (X)	17.5	12.6	7.2	6.0
Net Div Yield (%)	1.7	2.6	4.5	5.1
P/Book Value (X)	8.0	5.4	4.6	3.7
Net Debt/Equity (X)	CASH	0.0	CASH	CASH
ROAE (%)	22.7	36.3	46.6	42.5
<b>Earnings Rev (%):</b>		(7)	0	0
<b>Consensus EPS (sen):</b>		7.80	12.8	14.2
<b>Other Broker Recs:</b>		B: 4	S: 0	H: 2

Source of all data: Company, AllianceDBS Research, Bloomberg Finance L.P

## Full steam ahead

**Maintain BUY.** We trimmed our FY16F earnings by 7% to reflect a softer 4QFY16 due to slowing orders in January and February, as a result of the extended Christmas breaks and CNY celebrations. Moving forward, management assures that operations are on a "full-steam ahead" mode and is already seeing a pick-up in production volume. We maintain our FY17F/FY18F figures as the two Dyson contracts secured in 2015 are expected to be fully accretive in FY17F.

**Proxy to Dyson's aggressive expansion plans.** Dyson announced in 2014 that it was allocating GBP1.5bn (RM9bn) towards its R&D budget, and this will eventually culminate into 100 new products that will be launched worldwide in the next four years. We are positive of SKPRES' long term prospects as it is starting to see some spillover effect from Dyson's aggressive expansion plan. It secured two sizeable contracts from Dyson last year for the manufacturing of cordless vacuum cleaners totalling RM5bn - the first contract was announced in May 2015 (contract value of RM400m/p.a. over 5 years) and the second contract was announced in Sept 2015 (contract value of RM600m/p.a. over 5 years). We foresee more contract flows for SKPRES in the future as Dyson progresses along its expansion plan.

**Well positioned for further contract awards.** Taking into account the projects on hand, only c.25% of the capacity at SKPRES' new plant in Senai, Johor has been utilised. With ample spare capacity, we believe the group is well prepared to take on more contracts, which can come from both Dyson and non-Dyson related parties.

### Valuation:

Our BUY rating with TP RM1.78 is based on 14.6x fully-diluted FY17F EPS, which is the sector's weighted average PE valuation excluding SKPRES. The stock is currently trading at an undemanding 11x FY17F PE. Moreover, given its strong earnings growth potential at 3-year EPS CAGR of c.44%, it is trading at an attractive PEG of c.0.25x.

### At A Glance

Issued Capital (m shrs)	1,120
Mkt. Cap (RMm/US\$m)	1,512 / 387
Major Shareholders (%)	
Dato' Gan Kim Huat	53.4
Free Float (%)	46.6
3m Avg. Daily Val (US\$m)	0.80

**ICB Industry :** Industrials / Electronic & Electrical Equipment

**CRITICAL DATA POINTS TO WATCH**

**Earnings Drivers:**

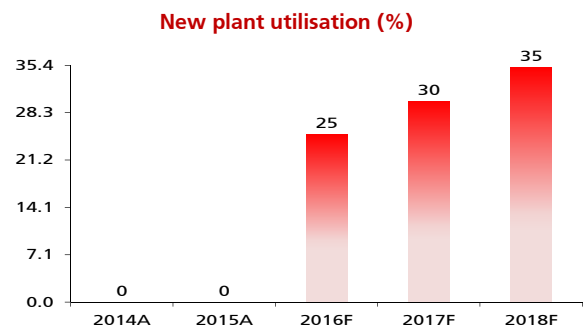
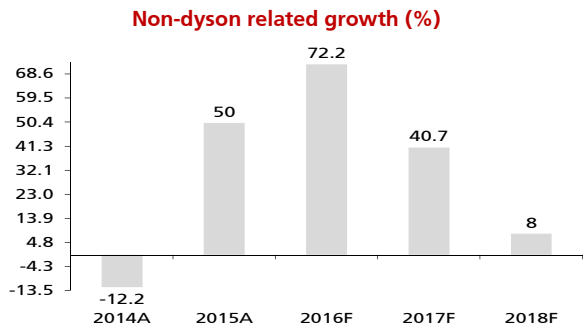
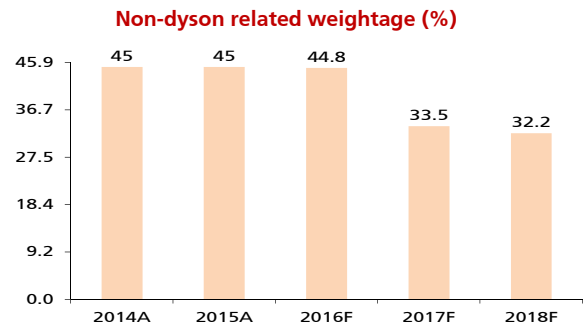
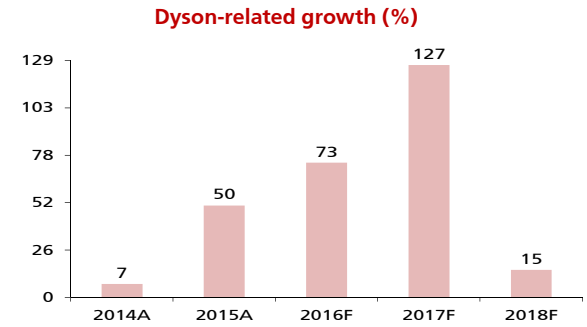
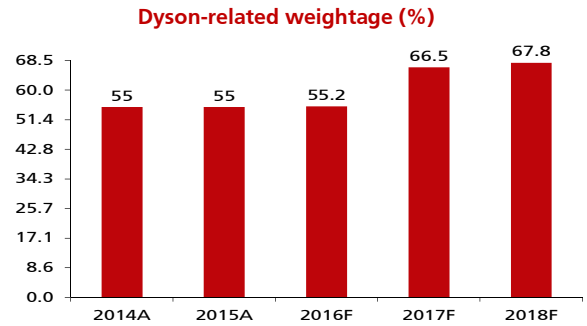
**Longstanding relationship with Dyson.** SKPRES has proven to be a capable and reliable world-class manufacturer for Dyson. SKPRES is one of Dyson’s four key contract manufacturers. The other three contract manufacturers are Flextronics (US), Meiban Group (Singapore) and ATA Industrial (Singapore). Dyson is also the group’s main client. The bulk of SKPRES’ business (c.55% in FY15), is from Dyson-related contracts. SKPRES currently has three existing Dyson contracts worth c.RM300m-RM400m p.a. which will run for another 3-4 years; two contracts to manufacture the upright vacuum cleaner and one contract to manufacture bladeless fan.

**Benefitting from Dyson’s expansion plans.** Given the group’s enduring partnership with Dyson, we are positive of SKPRES long term prospects as we expect it to gain further contracts from Dyson’s aggressive expansion plan. SKPRES secured two substantial contracts from Dyson last year for the manufacturing of cordless vacuum cleaners totalling RM5bn; the first contract was announced in May 2015 (contract value of RM400m/p.a. over 5 years) and the second contract was announced in Sept 2015 (contract value of RM600m/p.a. over 5 years). The first contract has started contributing from 2HFY16 while the second contract is expected to contribute from 1QFY17 onwards. After imputing the new contract wins into our model, revenue from Dyson-related contracts is forecasted at c.68% in FY18F. We foresee more contract flows for SKPRES in the future as Dyson progresses along its expansion plan.

**Tecnic’s contribution.** In 2015, SKPRES acquired the entire issued and paid-up share capital of all the wholly-owned subsidiaries of Tecnic. The acquisition has mitigated Dyson’s high contribution to revenue by the sizeable inclusion of Tecnic-related contracts worth RM350m (weightage c.30%) in FY16F. Without the inclusion of Tecnic, Dyson’s revenue contribution would have risen to c.77% in FY16F and c.83% in FY18F. This would have exposed SKPRES to a higher single customer dependency risk.

**Expanding clientele base.** Growth is also supported by SKPRES’ initiative to expand its clientele base and management has targeted 8% annual growth for non-Dyson contracts. Among the areas management is looking into is the F&B packaging segment, with plans to supply more plastic packaging to existing customers such as Unilever, Nestle, Suntory, and Shell. The recent acquisition of Tecnic has not only increased SKPRES’ production capacity but also enabled the group to leverage on Tecnic’s existing clientele to grow its customer base.

**Well positioned for more contract awards.** Taking into account the projects at hand, only c.25% of the floor capacity in SKPRES’ new plant in Senai, Johor has been utilised. Furthermore, the new plant has a potential capacity for 20 assembly lines, and only 5 assembly lines are used to produce cordless vacuum cleaners. The remaining c.75% of floor capacity is currently unutilised. With ample spare capacity, we believe the group can take on further contracts, both from Dyson and non-Dyson related parties.



Source: Company, AllianceDBS Research

**Balance Sheet:**

**Strong balance sheet in net cash position.** Despite rapid expansion in the past few years, SKPRES has been able to maintain a net cash position due to its strong earnings and healthy cash-flows. In addition, SKPRES has minimal debt and prior to FY15, the group had no debt. The group took up a long term debt of c.RM24m to partly finance the construction of the new plant in Senai, Johor with estimated capex of RM40m and additional short term debt of c.RM25m to finance the capex of RM20m for equipment and machineries for the new plant and other working capital purposes. However, we expect total capex to normalise to RM25m p.a. from FY17F onwards mainly for maintenance works. We estimate gross gearing to remain at c.13% in FY16F-FY18F.

**Share Price Drivers:**

**New contract awards.** SKPRES's price movement is highly sensitive to new contract announcements, as seen in the past when the share price rose by c.40% from the date of the announcement of the first Dyson contract in May 2015.

**Margin expansion.** Margins fell in FY14-FY15 mainly due to the shift in customer mix as SKPRES undertook more Dyson related projects which incurred high costs for purchasing specific components to support Dyson's orders. Nevertheless, the shortfall in margins has been compensated by the increase in contract values. We note that any slight improvement in margins will considerably improve SKPRES's earnings as the contract values are significant.

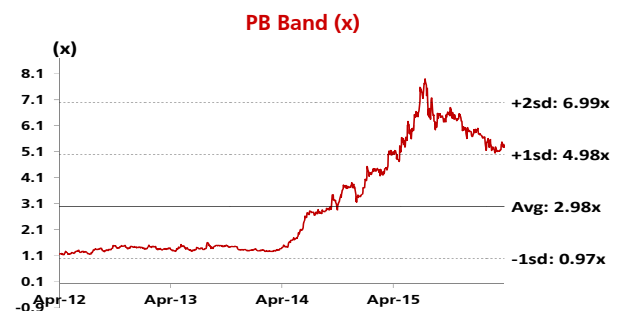
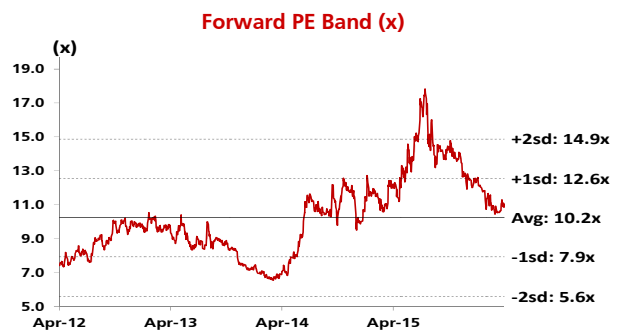
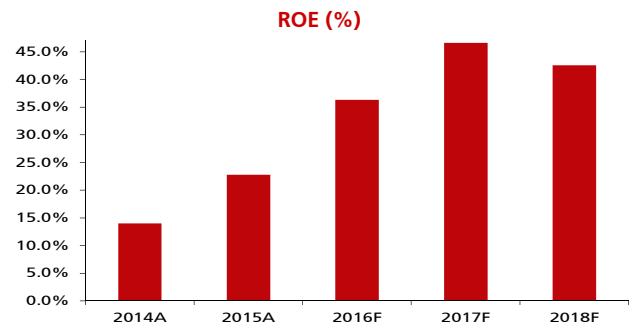
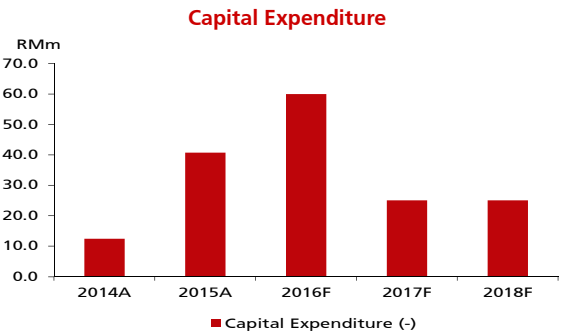
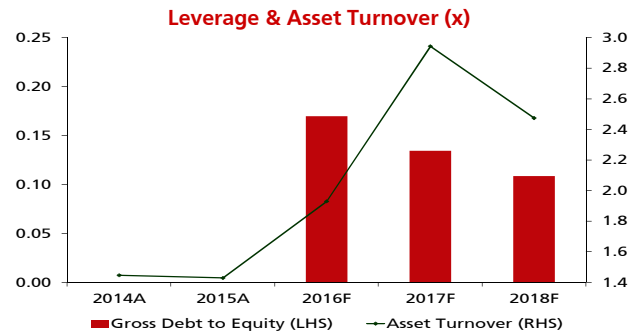
**Key Risks:**

**Relatively high customer concentration risk.** Note that c.55% of SKPRES' FY15 revenue is derived from Dyson, resulting in relatively high dependency on a single customer. Looking forward, including the recent two major contracts worth RM1.0bn per annum that SKPRES secured in 2015, our estimates suggest that Dyson will contribute an even higher portion, c.68% in FY18. In the event that Dyson reduces or terminates contracts with SKPRES, SKPRES' operating result could be materially and adversely affected. Although we have concerns with SKPRES' reliance on a single customer, we are not overtly alarmed by this risk, at least in the mid-term, as SKPRES has established a good relationship with Dyson throughout the years. SKPRES has continuously been awarded contracts by Dyson with contracts on mid-to-long term basis. The two recent contract wins are expected to provide some protection for any mid-term downside as both contracts are for an interval of 5 years.

**Downturn of the E&E industry.** SKPRES, as an EMS provider, is primarily dependent on the global demand for E&E products. In FY15, almost 100% of its revenue was generated from the E&E industry. Hence, any unfavourable macro factors such as a global economic slowdown or another financial crisis will negatively impact demand for SKPRES' products.

**Company Background**

SKPRES is principally involved in manufacturing plastic components, precision mould making, advance secondary processes, sub-assembly of electronics equipment and full turn-key contract manufacturing.



Source: Company, AllianceDBS Research

## Key Assumptions

FY Mar	2014A	2015A	2016F	2017F	2018F
Dyson-related weightage (%)	55.0	55.0	55.2	66.5	67.8
Dyson-related growth (%)	7.27	50.0	73.4	127	15.0
Non-dyson related weightage	45.0	45.0	44.8	33.5	32.2
Non-dyson related growth (%)	(12.2)	50.0	72.3	40.7	8.0
New plant utilisation (%)	0.0	0.0	25.0	30.0	35.0

## Sensitivity Analysis

Dyson +/- 1%	Net Profit +/- 1%
Non-Dyson +/- 1%	Net Profit +/- 0.4%

Growth will normalise to c.15% for Dyson related and c.8% for non-Dyson related

## Income Statement (RMm)

FY Mar	2014A	2015A	2016F	2017F	2018F
Revenue	413	619	1,071	2,014	2,268
Cost of Goods Sold	(350)	(532)	(921)	(1,732)	(1,950)
<b>Gross Profit</b>	<b>62.6</b>	<b>87.1</b>	<b>150</b>	<b>282</b>	<b>318</b>
Other Opng (Exp)/Inc	(24.2)	(32.1)	(41.8)	(76.5)	(83.9)
<b>Operating Profit</b>	<b>38.5</b>	<b>55.0</b>	<b>108</b>	<b>205</b>	<b>234</b>
Other Non Opng (Exp)/Inc	0.0	0.0	0.0	0.0	0.0
Associates & JV Inc	0.0	0.0	0.0	0.0	0.0
Net Interest (Exp)/Inc	1.30	0.83	(1.3)	(1.9)	(1.6)
Exceptional Gain/(Loss)	0.0	0.0	0.0	0.0	0.0
<b>Pre-tax Profit</b>	<b>39.8</b>	<b>55.8</b>	<b>107</b>	<b>204</b>	<b>232</b>
Tax	(10.4)	(13.5)	(26.7)	(50.9)	(58.0)
Minority Interest	0.0	0.0	0.0	0.0	0.0
Preference Dividend	0.0	0.0	0.0	0.0	0.0
<b>Net Profit</b>	<b>29.3</b>	<b>42.3</b>	<b>80.1</b>	<b>153</b>	<b>174</b>
Net Profit before Except.	29.3	42.3	80.1	153	174
EBITDA	46.9	64.6	123	232	261
<b>Growth</b>					
Revenue Gth (%)	(2.5)	50.0	72.9	88.1	12.6
EBITDA Gth (%)	(22.3)	37.8	90.6	88.1	12.6
Opg Profit Gth (%)	(25.4)	42.9	96.7	90.0	13.7
Net Profit Gth (Pre-ex) (%)	(25.9)	44.3	89.3	90.5	14.0
<b>Margins &amp; Ratio</b>					
Gross Margins (%)	15.2	14.1	14.0	14.0	14.0
Opg Profit Margin (%)	9.3	8.9	10.1	10.2	10.3
Net Profit Margin (%)	7.1	6.8	7.5	7.6	7.7
ROAE (%)	14.0	22.7	36.3	46.6	42.5
ROA (%)	10.3	9.8	14.4	22.3	19.0
ROCE (%)	14.1	21.9	29.7	37.4	35.6
Div Payout Ratio (%)	52.2	50.2	50.0	50.0	50.0
Net Interest Cover (x)	NM	NM	83.8	108.8	146.4

Margins to gradually improve

Source: Company, AllianceDBS Research

**Quarterly / Interim Income Statement (RMm)**

FY Mar	3Q2015	4Q2015	1Q2016	2Q2016	3Q2016
Revenue	150	194	243	261	315
Cost of Goods Sold	(130)	(174)	(209)	(225)	(271)
<b>Gross Profit</b>	<b>20.5</b>	<b>20.4</b>	<b>33.9</b>	<b>36.3</b>	<b>43.8</b>
Other Oper. (Exp)/Inc	(6.6)	(4.6)	(9.9)	(11.7)	(11.5)
<b>Operating Profit</b>	<b>14.0</b>	<b>15.8</b>	<b>24.1</b>	<b>24.6</b>	<b>32.3</b>
Other Non Opg (Exp)/Inc	0.0	0.0	0.0	0.0	0.0
Associates & JV Inc	0.0	0.0	0.0	0.0	0.0
Net Interest (Exp)/Inc	0.33	0.21	(0.5)	(0.4)	(0.5)
Exceptional Gain/(Loss)	0.0	0.0	0.0	0.0	0.0
<b>Pre-tax Profit</b>	<b>14.3</b>	<b>16.0</b>	<b>23.5</b>	<b>24.2</b>	<b>31.8</b>
Tax	(3.8)	(4.7)	(5.6)	(5.8)	(7.6)
Minority Interest	0.0	0.0	0.0	0.0	0.0
<b>Net Profit</b>	<b>10.5</b>	<b>11.3</b>	<b>17.9</b>	<b>18.4</b>	<b>24.2</b>
Net profit bef Except.	10.5	11.3	17.9	18.4	24.2
EBITDA	16.4	18.3	28.7	29.3	37.1

**Growth**

Revenue Gth (%)	7.1	29.4	25.0	7.5	20.5
EBITDA Gth (%)	2.5	11.5	56.6	2.0	26.6
Opg Profit Gth (%)	1.2	13.1	52.2	2.3	31.1
Net Profit Gth (Pre-ex) (%)	0.1	7.3	58.3	3.0	31.0

**Margins**

Gross Margins (%)	13.7	10.5	14.0	13.9	13.9
Opg Profit Margins (%)	9.3	8.1	9.9	9.4	10.2
Net Profit Margins (%)	7.0	5.8	7.4	7.1	7.7

**Balance Sheet (RMm)**

FY Mar	2014A	2015A	2016F	2017F	2018F
Net Fixed Assets	79.0	179	194	193	191
Invt in Associates & JVs	0.0	0.0	0.0	0.0	0.0
Other LT Assets	3.36	3.23	2.98	2.74	2.49
Cash & ST Invt	94.8	83.4	47.6	65.1	186
Inventory	25.5	74.9	75.7	142	160
Debtors	96.5	219	220	414	466
Other Current Assets	3.79	6.00	6.00	6.00	6.00
<b>Total Assets</b>	<b>303</b>	<b>565</b>	<b>546</b>	<b>823</b>	<b>1,011</b>
ST Debt	0.0	0.0	25.4	25.4	25.4
Creditor	74.9	398	179	380	481
Other Current Liab	0.0	0.45	2.08	2.08	2.08
LT Debt	0.0	0.0	23.6	23.6	23.6
Other LT Liabilities	7.98	14.6	26.6	26.6	26.6
Shareholder's Equity	220	152	289	366	453
Minority Interests	0.0	0.0	0.0	0.0	0.0
<b>Total Cap. &amp; Liab.</b>	<b>303</b>	<b>565</b>	<b>546</b>	<b>823</b>	<b>1,011</b>
Non-Cash Wkg. Capital	50.9	(98.6)	120	180	149
Net Cash/(Debt)	94.8	83.4	(1.4)	16.1	137
Debtors Turn (avg days)	74.9	92.9	74.8	57.4	70.8
Creditors Turn (avg days)	73.2	165.0	116.2	59.8	81.7
Inventory Turn (avg days)	26.6	35.1	30.3	23.3	28.7
Asset Turnover (x)	1.4	1.4	1.9	2.9	2.5
Current Ratio (x)	2.9	1.0	1.7	1.5	1.6
Quick Ratio (x)	2.6	0.8	1.3	1.2	1.3
Net Debt/Equity (X)	CASH	CASH	0.0	CASH	CASH
Net Debt/Equity ex MI (X)	CASH	CASH	0.0	CASH	CASH
Capex to Debt (%)	N/A	N/A	122.4	51.0	51.0
Z-Score (X)	11.5	3.5	6.8	6.1	5.6

Growth attributed to inclusion of the new Dyson contract

Net cash position

Source: Company, AllianceDBS Research

**Cash Flow Statement (RMm)**

<b>FY Mar</b>	<b>2014A</b>	<b>2015A</b>	<b>2016F</b>	<b>2017F</b>	<b>2018F</b>
Pre-Tax Profit	39.8	55.8	107	204	232
Dep. & Amort.	8.39	9.61	15.0	26.2	27.2
Tax Paid	(10.4)	(13.5)	(26.7)	(50.9)	(58.0)
Assoc. & JV Inc/(loss)	0.0	0.0	0.0	0.0	0.0
Chg in Wkg.Cap.	(13.9)	(29.2)	(98.2)	(60.0)	31.2
Other Operating CF	(3.2)	0.15	0.0	0.0	0.0
<b>Net Operating CF</b>	<b>20.6</b>	<b>22.8</b>	<b>(3.1)</b>	<b>119</b>	<b>232</b>
Capital Exp.(net)	(12.4)	(40.7)	(60.0)	(25.0)	(25.0)
Other Invt.(net)	(71.1)	71.4	0.0	0.0	0.0
Invt in Assoc. & JV	0.0	0.0	0.0	0.0	0.0
Div from Assoc & JV	0.0	0.0	0.0	0.0	0.0
Other Investing CF	1.38	16.2	0.0	0.0	0.0
<b>Net Investing CF</b>	<b>(82.1)</b>	<b>47.0</b>	<b>(60.0)</b>	<b>(25.0)</b>	<b>(25.0)</b>
Div Paid	(15.3)	(21.2)	(40.1)	(76.3)	(87.0)
Chg in Gross Debt	0.0	0.0	49.0	0.0	0.0
Capital Issues	0.0	0.0	18.3	0.0	0.0
Other Financing CF	7.20	5.93	0.0	0.0	0.0
<b>Net Financing CF</b>	<b>(8.1)</b>	<b>(15.3)</b>	<b>27.3</b>	<b>(76.3)</b>	<b>(87.0)</b>
Currency Adjustments	(0.1)	0.26	0.0	0.0	0.0
Chg in Cash	(69.6)	54.8	(35.8)	17.5	120
Opg CFPS (sen)	3.84	5.79	8.25	14.3	16.1
Free CFPS (sen)	0.92	(2.0)	(5.5)	7.49	16.6

Maintenance capex

Source: Company, AllianceDBS Research

**Target Price & Ratings History**



S.No.	Date	Closing Price	Target Price	Rating
1:	15 Feb 16	1.24	1.78	BUY
2:	22 Feb 16	1.36	1.78	BUY
3:	02 Mar 16	1.31	1.78	BUY

Note: Share price and Target price are adjusted for corporate actions.

Source: AllianceDBS Research

## DISCLOSURE

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### Stock rating definitions

STRONG BUY	-	> 20% total return over the next 3 months, with identifiable share price catalysts within this time frame
BUY	-	> 15% total return over the next 12 months for small caps, >10% for large caps
HOLD	-	-10% to +15% total return over the next 12 months for small caps, -10% to +10% for large caps
FULLY VALUED	-	negative total return > -10% over the next 12 months
SELL	-	negative total return of > -20% over the next 3 months, with identifiable catalysts within this time frame

### Commonly used abbreviations

Adex = advertising expenditure	EPS = earnings per share	PBT = profit before tax
bn = billion	EV = enterprise value	P/B = price / book ratio
BV = book value	FCF = free cash flow	P/E = price / earnings ratio
CF = cash flow	FV = fair value	PEG = P/E ratio to growth ratio
CAGR = compounded annual growth rate	FY = financial year	q-o-q = quarter-on-quarter
Capex = capital expenditure	m = million	RM = Ringgit
CY = calendar year	M-o-m = month-on-month	ROA = return on assets
Div yld = dividend yield	NAV = net assets value	ROE = return on equity
DCF = discounted cash flow	NM = not meaningful	TP = target price
DDM = dividend discount model	NTA = net tangible assets	trn = trillion
DPS = dividend per share	NR = not rated	WACC = weighted average cost of capital
EBIT = earnings before interest & tax	p.a. = per annum	y-o-y = year-on-year
EBITDA = EBIT before depreciation and amortisation	PAT = profit after tax	YTD = year-to-date

**DISCLAIMER**

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