

BP Plastics Holding Bhd

Company Update

Stock Code: 5100

Price: RM 1.20

Market Capitalisation: RM 144m

Board: Main Board

Sector: Industrial

Recommendation: Maintain BUY

Key Stock Statistics

<u>FYE Dec (RMm)</u>	<u>2005</u>	<u>2006F</u>
EPS (sen)	17.1	21.8
P/E (x)	7.0	5.5
Dividend/Share (sen)	7.0	7.0
NTA/Share (RM)	0.72	0.84
Book Value/Share	0.70	0.82
Issued Capital (mil shares)	120.0	120.0
52-weeks Share Price Range	RM0.90-RM1.49	

Major Shareholders:

	<u>%</u>
LG Capital	45

Per Share Data

<u>FYE Dec (RMm)</u>	<u>2003</u>	<u>2004</u>	<u>2005</u>	<u>2006F</u>	<u>2007F</u>
Book Value (RM)	-	0.5	0.7	0.8	1.0
Cash Flow (sen)	-	1.1	24.8	28.6	29.3
Earnings (sen)	8.9	12.3	17.1	21.8	24.0
Dividend (sen)	-	-	7.0	7.0	7.0
Payout Ratio	-	-	41.0	32.0	29.2
PER (x)	13.5	9.8	7.0	5.5	5.0
P/Cash Flow (x)	-	-	4.8	4.2	4.1
P/Book Value (x)	-	-	1.7	1.5	1.2
Dividend Yield (%)	-	-	5.8	5.8	5.8
ROE (%)	-	-	28.1	28.8	26.6
Net Gearing (%)	-	-	(8.5)	Net Cash	Net Cash

P&L Analysis (RM mil)

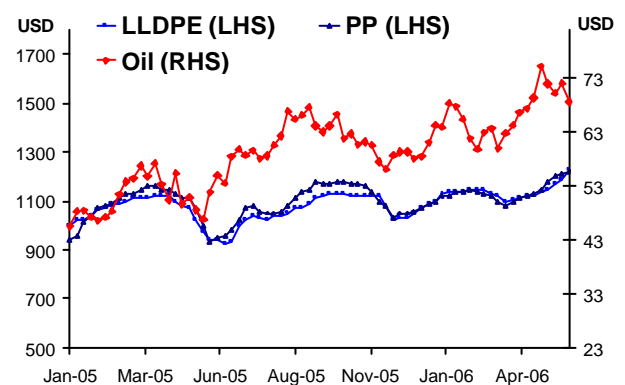
<u>FYE Dec (RMm)</u>	<u>2003</u>	<u>2004</u>	<u>2005</u>	<u>2006F</u>	<u>2007F</u>
Revenue	64.9	122.1	160.5	228.5	254.8
Operating Profit	12.6	17.3	22.4	31.0	33.3
Depreciation	-2.2	-3.2	-3.7	-4.7	-5.1
Interest Expenses	-0.2	-0.3	-0.4	-0.4	-0.4
Pre-tax Profit	12.9	17.9	23.4	31.6	34.7
Effective Tax Rate	17.5	17.7	12.5	17.0	17.0
Net Profit	10.7	14.7	20.5	26.2	28.8
Operating Margin	19.5	14.2	14.0	13.6	13.1
Pre-tax Margin	19.9	14.6	14.6	13.8	13.6
Net-Margin	16.4	12.1	12.8	11.5	11.3

Recent Developments

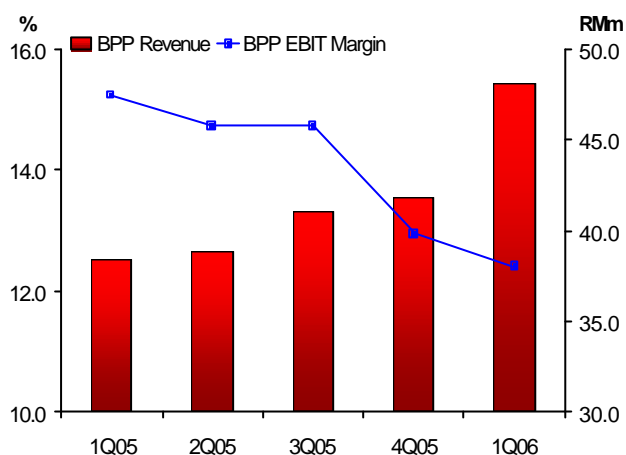
- We recently visited BPP's new 5 acre manufacturing facility, which is just minutes away from its existing factory in Batu Pahat, Johor. To recap, BPP had, in Dec 05, invested in an additional 21,600MT p.a. capacity, thus increasing its annual capacity to 60,000MT. The 2 newly-installed lines were the 16,800MT p.a. cast stretch film machine (Line 1) and the 4,800MT p.a. blown film machine (Line 2), of which only Line 1 has been operational. Management said that they were waiting for some parts for Line 2, which have yet to arrive from Germany, but it is expected to commence operations in June 06.
- BPP has also invested in a new recycling unit at the new factory. This replaces an older recycling unit at the main factory, which was less efficient. Recycling its waste allows BPP to reduce slightly the amount of resin purchased. The recycled resin, albeit of poorer quality, are cheaper and can be used in lower quality films and bags as per the requirements of the customer.

Earnings Outlook

- In line with increases in crude oil prices, the cost of resin has also been on the rise, albeit at a less volatile rate. **Figure 1** shows the fluctuations seen in crude oil prices since 2005 and the impact this has had on global prices for linear low density polyethylene (LLDPE) and polypropylene (PP). Since resin constitutes about 90% of BPP's raw material costs, such increases result in higher costs for BPP. Even so, BPP has managed to pass on most of the cost to its customers. However, margins are still affected due to the timing differences between receiving an order and the purchase of resin. We are therefore ascribing a slight dip in margins for FY06, with ASP and cost price assumptions for FY06 to increase by 9% and 10% respectively (0% growth for both previously).

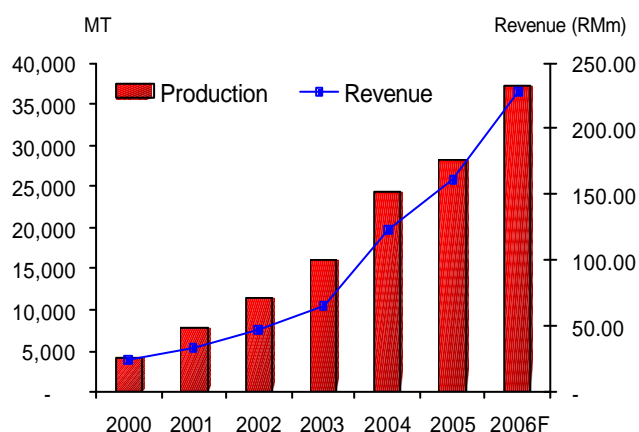
Figure 1: LLDPE and PP prices relative to crude oil


Source: Bloomberg

Figure 2: BPP's revenue and EBIT margin comparison


Source: Company Data

- Figure 2** highlights the falling quarterly EBIT margins in line with rising oil and resin prices despite the increase in revenue. The sharper fall in 4Q05 and 1Q06 margins are also attributed to teething problems incurred with the new plant. Furthermore, the commencement of the new plant's Line 1, which produces stretch film, has altered BPP's stretch to blown mix from 70:30 previously to 75:25.
- Similarly, the increase in stretch film production, which traditionally has lower margins compared to blown film, contributed to the fall in 1Q06 margins but also boosted 1Q06 revenue. Thus, we have imputed a higher yoy increase in total FY06 production of 32%, compared with 20% previously. This is illustrated in **Figure 3** below. We believe margins will improve in the subsequent quarters and have factored in contribution from the new plant's Line 2, which produces the higher-margin blown products.

Figure 3: BPP's revenue and production comparison


Source: Company Data, HLGS estimates

- These revisions translate to an increase of 22.2% and 16.8% for FY06-07 revenue forecasts. FY06-07 net profit forecast is also 9.6% and 17.4% higher respectively. On the other hand, FY06 net profit margins have been reduced to 11.5% from 12.8% previously. No changes were made to FY07 margins

because the higher interest income offsets the fall in operating margins. BPP is in a net cash position with minimal borrowings.

- Going forward, Chemical Markets Associates, Inc. (CMAI), an independent research company, has forecasted that resin prices will continue to rise for the coming years with rising demand. As Malaysia is a leading film and bags producer (19% of the EU's imports for films and bags are from Malaysia), the higher global demand implies there is ample room for growth for BPP and its peers. BPP is also at an advantage as it is one of the Top 10 stretch film producers in the world.
- With higher production resulting from higher demand, BPP will also be in a position to achieve economies of scale, enabling BPP to improve or at least maintain its margins. The capacity expansion in FY05, funded by the listing receipts, was in expectation of growing demand.

Valuation & Recommendation

- We are maintaining our **BUY** recommendation on BPP with a revised target price of **RM1.68** (from RM1.59) based on its peers average PER of 7.7x. We like the stock due to its decent earnings growth, constant delivery of earnings, cheap valuations (5.5x FY06 EPS) and a decent net dividend yield of 5.8%.

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BUY	Total return is expected to exceed +10% over a 12-month period
TRADING BUY (TR BUY)	Total return is expected to exceed +10% over a 3-month period due to short-term positive development, but fundamentals are not strong enough to warrant a Buy call. This is to cater to investors who are willing to take on higher risks
HOLD	Total return is expected to be between -10% to +10% over a 12-month period
SELL	Total return is expected to be below -10% over a 12-month period
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