JF APEX SECURITIES BERHAD
(47680-X)

Trading Idea

28 Jan 2010

# C.I. Holdings Bhd

## Not Rated

***New RM45m non-carbonated line***

**Target Price: RM2.04**

| Price (27 Jan 2010) | RM1.70 |
|---|---|
| KLCI | 1265.77 |

| Stock Data | |
|---|---|
| Bursa / Bloomberg code | 2828 / CIH MK |
| Board / Sector | MAIN / F&B |
| Syariah Compliant status | Yes |
| Issued shares (m) | 142.00 |
| Par Value (RM) | 1.00 |
| Market cap. (RM m) | 249.92 |
| Price over NTA | 2.52x |
| 52-week price Range | RM0.85 – 1.81 |
| Beta (against KLCI) | 0.63 |
| 3-m Avg Daily Volume | 28.90k |
| 3-m Avg Daily Value (RM) | 49.40k |

*^ based on closing price*

| Share Performance (as at 27 Jan 2010) | 1m | 3m | 12m |
|---|---|---|---|
| Absolute (%) | 4.8 | 2.9 | 85.3 |
| Relative (%-pts) | 5.4 | 19.0 | 28.8 |

| Historical PE | 2007 | 2008 | 2009 |
|---|---|---|---|
| Highest | 8.09 | 10.85 | 11.76 |
| Lowest | 7.77 | 7.08 | 6.56 |

| Important Balance Sheet Items (as at 31 Dec 09) | |
|---|---|
| NTA / share (sen) | 67.50 |
| Total Receivables (RM m) | 89.84 |
| Total Payables (RM m) | 71.95 |
| Total Assets (RM m) | 311.34 |
| Net Cash /(Debt) (RM m) | -40.01 |

| Major Shareholders | |
|---|---|
| 1. Datuk Johari bin Abdul Ghani | 25.4% |
| 2. SISMA Group | 20.0% |
| 3. PNB | 15.4% |

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***C.I. Holdings Berhad or "CIH" is mainly involved in the manufacturing and distribution of beverages, tap ware and ceramic sanitary ware. CIH's beverage division has an Exclusive Bottling Appointment ("EBA") with PepsiCo to bottle, market, sell and distribute the soft drinks. With the investment of RM45m in new non-carbonated line, we expect the Group to continue to deliver strong earnings. We value CIH at Target Price of RM2.04, implying potential upside of 20.0%.***

### Highlights

- **Beverages, tap ware and ceramic sanitary ware** – C.I. Holdings Berhad or "CIH" is mainly involved in the manufacturing and distribution of beverages, tap ware and ceramic sanitary ware. Permanis (CIH's beverage division) currently owns the exclusive rights under an Exclusive Bottling Appointment ("EBA") with PepsiCo and Seven-Up International to bottle, market, sell and distribute the soft drinks under the "Pepsi" and other peripheral brands such as "Mirinda", "7-Up","Gatorade", "Lipton", Tropicana" and "Evervess".
- **Focus on non-carbonated products -** CIH's strategy to focus on non-carbonated products such as tea and juice has been fruitful. Over the last few years, CIH has grown the non-carbonated segment from 20% revenue contribution to the current 40% contribution. Tropicana Twister is currently the market leader in the Ready To Drink Juice segment while Lipton is the market leader in the Ready To Drink Tea segment with 30% market share respectively each.
- **Investing RM45m in new non-carbonated line** - In order to accommodate the capacity constraints to allow future growth in Permanis' current range of non-carbonated products, the Company has decided to invest in new non-carbonated line which will cost RM45m. The new line has the capacity to produce 600 bottles per minute (double the speed of the existing PET line).
- **Strong 2Q2010 results -** CIH recorded revenue of RM114.5m (up 33.3% y-o-y but down 7.5% q-o-q) in 2Q2010. Besides that, profit before tax or "PBT" in 2Q2010 doubled to RM10.5m as compared to 2Q2009. The significantly higher PBT was attributed to the continued revenue growth and prudent cost management across the divisions under the Group.
- **Target price of RM2.04 -** By ascribing our discounted industry average PER of 8.9x (for F&B small cap) to our forecasted EPS of 22.93 sen, we value CIH at RM2.04. In our opinion, CIH is attractive for investors seeking dividend-paying stocks with plenty of opportunities for growth in resilient beverage industry.

## Company Background

***Beverages, tap ware and ceramic sanitary ware.***

C.I. Holdings Berhad or "CIH" is mainly involved in the manufacturing and distribution of beverages, tap ware and ceramic sanitary ware. Under the Group, there are three subsidiaries namely Permanis Sdn. Bhd. or "Permanis", Doe Industries Sdn. Bhd. or "Doe" and Potex Sdn. Bhd. or "Potex".

***Exclusive Bottling Agreement with PepsiCo and Seven-Up International.***

Permanis currently owns the exclusive rights under an Exclusive Bottling Appointment ("EBA") with PepsiCo and Seven-Up International to bottle, market, sell and distribute the soft drinks under the "Pepsi" and other peripheral brands such as "Mirinda", "7-Up","Gatorade", "Lipton", Tropicana" and "Evervess".

***Own brand: Chill, Excel, Frost, Bleu and Shot.***

Besides that, Permanis products has penetrated majority of the segments in the beverage industry namely Carbonated Soft Drinks, Isotonic Drinks, Ready to Drink Coffee and Tea, Juice, Energy Drinks, Asian Drinks and Mineral Water. Lastly, Permanis also manufactures its own brand of drinks and its products include "Chill", "Excel", "Frost", "Bleu" and "Shot".

***Doe: manufacturer of chrome-plated brass tapwares and sanitary fitting***

With industry experience surpassing 25 years, Doe has the expertise as manufacturer of chrome-plated brass tapwares and sanitary fitting. The Company operates gravity die-casting foundry producing brass die-castings which are then surfaced-finished in chrome by its automatic electroplating line. Besides being the market leader in the Tap Ware segment, the Company also has its factory in Senawang, Negeri Sembilan. Currently, some of the brands produced by Doe are "Ignite", "Huber" and "Prima".

***Potex: manufacturing, distribution and marketing of ceramic sanitary ware***

Meanwhile, Potex is primarily focused on the manufacturing, distribution and marketing of ceramic sanitary ware. Owning a production plant located at Masjid Tanah Melaka, some of the Company's brand are "Potex", "Ascot" and "Carravagio". Overall, Potex's ceramic sanitary ware range and Doe's range of tapware and sanitary fittings compliments each other.

## Business Outlook

***Positive prospect for continuous cooperation with PepsiCo***

Since its incorporation on 3 October 1973, Permanis has started to establish strong business relationship with PepsiCo by undertaking manufacturing, distribution and marketing activities of beverages under the latter's franchise. As a result, we believe that Permanis prospect for continuous cooperation with PepsiCo is very positive on the back of the 37 years relationship. Besides that, finding a new franchise may not be cost efficient to PepsiCo.

***Focus on non-carbonated products***

In the financial year ended June-2009, CIH's strategy to focus on non-carbonated products such as tea and juice has been fruitful. With the new non-carbonated production plant commissioned in Feb-2008, most of the Company's non-carbonated products are now manufactured in-house. In Ready To Drink Tea segment, Lipton Tea continued its market leader status with 30% market share.

***Boost from Tropicana Twister***

Meanwhile, Tropicana Twister launch in Mar-2008 has allowed CIH to capture significant market share in the juice segment. Despite being launched only for 10 months, Tropicana Twister has gained its status as the market leader as of end-2009 with 30% market share. Based on the reputation of Tropicana Twister as World's No. 1 100% juice brand, we expect the brand to continue to be the market leader in FY2010.

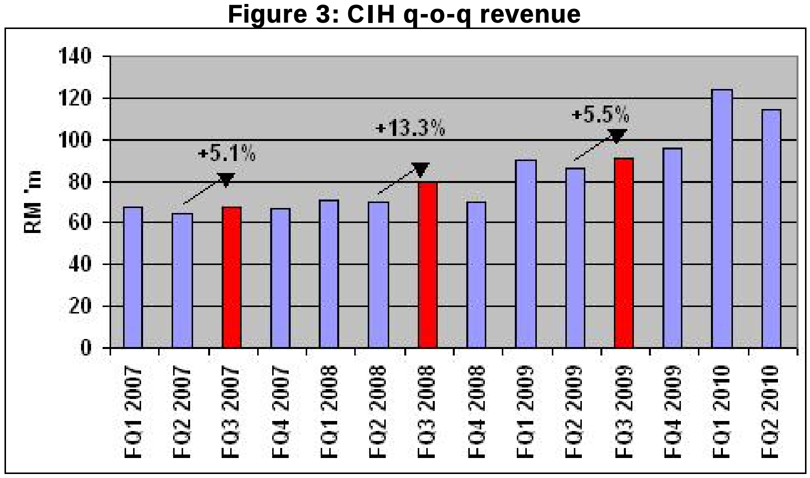
**Figure 1: Beverages brand manufactured by Permanis**

*Source: Company website*

**Figure 2: Some of the products manufactured by Potex**


*Source: Potex website*

**Figure 3: CIH q-o-q revenue**




*Source: Bloomberg, JF Apex compilation*

***New investment in new non-carbonated line***

Currently, CIH's existing RM35m non-carbonated lines (which were commissioned in Mar-2008) include a PET line (bottle line) and can line. Due to the higher than expected demand for Tropicana Twister, the PET non-carbonated capacity has been under pressure and caused Permanis to move some Lipton production to back co-packers.

***Cost of RM45m***

In order to accommodate the capacity constraints to allow future growth in Permanis' current range of non-carbonated products, the Company has decided to invest in new non-carbonated line which will cost RM45m. The new line has the capacity to produce 600 bottles per minute (double the speed of the existing PET line). Effectively, this means that Permanis has the capacity to triple its production rate once the new line is setup. The new non-carbonated line is expected to be completed by 1QFY2011 (i.e. between Jul-2010 to Sep-2010).

***Minimal impact to balance sheet strength***

The management has expected the gearing to increase upon the full payment of the new line. However, the peak gearing shall not exceed 0.7 and will be managed down to 0.5 in the short term. Lastly, the new line is expected to have payback period of 5 years and breakeven capacity utilization of 20%.

***Expect demand growth during Chinese New Year***

Lastly, we anticipate CIH's revenue to grow in 3Q2010 due to the seasonal effect caused by Chinese New Year or "CNY". Based on the previous three financial years trend, q-o-q revenue growth has been recorded consecutively in FY2007 (5.1%), FY2008 (+13.3%) and FY2009 (+5.5%). We believe that this is caused by higher demand for Ready To Drink beverages during the CNY.

## Financial Review

***3-year CAGR of 17.8%***

Overall, we like CIH due to its defensive business in the food and beverage industry, with the opportunity of growth from the expected increasing demand for Tropicana Twister. Historically, CIH managed to record a positive growth y-o-y consecutively in the last three years with a 3-year Compounded Average Growth Rate or "CAGR" of 17.8% from RM222.16m in FY2006 to RM363.0m in FY2009.

***Expect revenue growth of 31.3% in FY2010***

Furthermore, CIH has recorded revenue of RM238.3m in 1H2010. Assuming that CIH's 2H2010 revenue will be at least similar to 1H2010, we have forecasted CIH to achieve revenue of RM476.6m for FY2010, implying a 31.3% possible growth y-o-y in FY2010.

***Gross profit margin jumped to 40.4% in 1H2010***

Besides that, gross profit margin has jumped to 40.4% in 1H2010 (vs. 38.1% in FY2009). Since FY2006 (gross profit margin: 29.6%), CIH has successfully registered higher gross profit margin y-o-y. Meanwhile, gross profit for 1H2010 has also grown 51.0% to RM96.4m (as compared to 1H2009) due to mix shift to more profitable brands and packages.

***Investing heavily in S&D to cover 42,000 outlets***

The Group is currently investing heavily to enhance its selling and distribution in anticipation of future growth by increasing its nationwide coverage from 35,000 outlets to 42,000 outlets by end-Jun 2010. Currently, the Group has managed to cover more than 40,000 outlets and thus is positive towards achieving the target of 42,000 outlets.

## 2Q2010 Results Review

***2Q2010 revenue up 33.3% y-o-y***

CIH recorded revenue of RM114.5m (up 33.3% y-o-y but down 7.5% q-o-q) in 2Q2010. The higher revenue y-o-y is mainly caused by the improvement in the beverages division while the weaker revenue q-o-q is due to the stronger sales experienced in the last quarter during Hari Raya festive period. As mentioned previously, revenue should bounce back to positive growth in 3Q2010 due to expected higher sales during Chinese New Year.

***Profit before tax doubled to RM10.5m***

Besides that, profit before tax or "PBT" in 2Q2010 doubled to RM10.5m as compared to 2Q2009. The significantly higher PBT was attributed to the continued revenue growth and prudent cost management across the divisions under the Group. However, PBT for 2Q2010 is lower by 3.8% q-o-q on the back of lower revenue experienced this quarter.

***Beverage division revenue improved 35%***

Meanwhile, the beverage division continues its success path as revenue improved 35% while net profit was 83%. This is mainly due to higher sales and resultant economies of scale. Besides that, the beverage division has launched a refreshed packaging design and campaign for Pepsi called "Breathtaking". As for 7 Up Revive, the division has leveraged on the digital media by embarking on aggressive online and offline "Revive" 'Rev Up' Facebook campaign.

***Tap and sanitary ware division is still facing a challenging building sector***

On the other hand, tap and sanitary ware division is still facing a challenging building sector. However, the management has seen some signs of the start of recovery in the private sector as the progress of on-going projects for private sector developers seem to be picking up momentum. Lastly, the division managed to double the net profit despite slow revenue growth due to improved margin driven by product mix.

***Positive outlook from CIH Directors***

In its filing to Bursa Malaysia, CIH has maintained its positive outlook on FY2010 by mentioning that *"Barring any unforeseen circumstances, the Directors are of the opinion that the Group's financial performance for the financial year ending 30th June 2010 will continue to improve."* We believe that this is achievable based on the reasons highlighted in our Business Outlook segment above.

***Expect minimum dividend yield of 5.3%***

Lastly, CIH has declared an interim dividend of 4 sen per share less income tax at 25%. As compared to 2 sen dividend announced last year, the dividend has doubled in the absolute value. Assuming the Group maintained the same amount of 5 sen for its Final Dividend, this will translate into total dividend of 9 sen or dividend yield of 5.3% at the price of RM1.70. As we have not include the possibility of higher Final Dividend, we believe that 5.3% dividend yield should be the minimum yield expected.

## Investment Risks

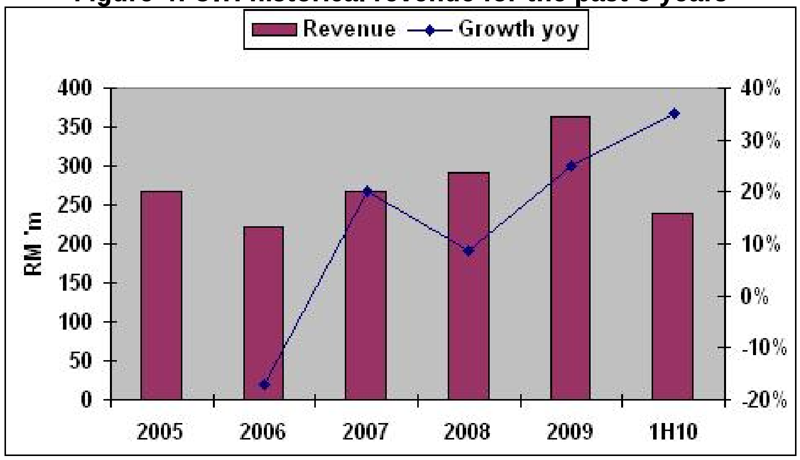
***Risk 1: May lose some market share***

We expect the beverage sector to remain competitive as some smaller players is planning to capture higher market shares in 2010. Thus, CIH may lose some market shares. However, the risk is minimal on the back of strong market leadership from Lipton Tea and Tropicana Twister.

***Risk 2: Higher-than-expected sugar price increase***

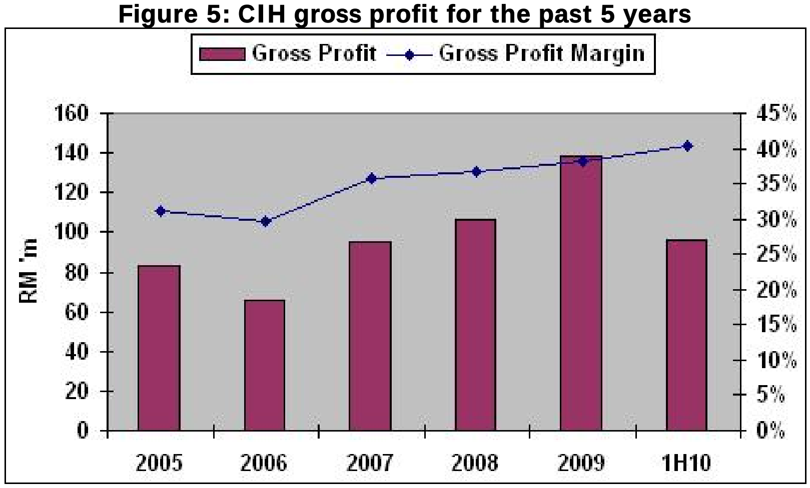
Besides that, the rising raw material price might erode CIH's profit. Higher-than-expected increment in the sugar price may erode CIH's profitability. However, the negative impact should be in the short run, as we believe CIH should be able to pass on the impact to consumers.

**Figure 4: CIH historical revenue for the past 5 years**




***Source: Company, JF Apex compilation***

**Figure 5: CIH gross profit for the past 5 years**




***Source: Company, JF Apex compilation***

**Figure 6: "Revive" 'Rev Up' Facebook campaign**


***Source: Facebook***

## Valuation and Recommendation

***Target price of RM2.04***

By ascribing our discounted industry average PER of 8.9x (for F&B small cap) to our forecasted EPS of 22.93 sen, we value CIH at RM2.04. In our opinion, CIH is attractive for investors seeking dividend-paying stocks with plenty of opportunities for growth in a resilient beverage industry.

Besides that, we noticed that F&N is trading at 17.1x forward PER 2010 (based on Bloomberg consensus mean EPS2010F of 65 sen) while CIH is only trading at 9.4x forward PER 2010 (based on Bloomberg consensus mean EPS2010F of 18 sen). Thus, there may still be plenty of potential upside for CIH should its PER converge to industry PER.

**Figure 7: CIH historical price movement**

**Figure 8: CIH Income Statement Forecast**

| FYE Jun (RM m) | FY08 | FY09 | FY10F | FY11F | FY12F |
|---|---|---|---|---|---|
| Revenue | 290.45 | 362.98 | 476.60 | 524.26 | 566.20 |
| COGS | -183.67 | -224.59 | -290.73 | -319.80 | -345.38 |
| Gross Profit | 106.79 | 138.40 | 185.87 | 204.46 | 220.82 |
| | | | | | |
| *Other Income* | 2.53 | 5.38 | 3.95 | 3.95 | 3.95 |
| *S&D Cost* | -56.14 | -74.57 | -110.51 | -123.77 | -136.14 |
| *Admin Expense* | -32.48 | -34.52 | -37.88 | -39.78 | -41.76 |
| *Other Expense* | -0.30 | -1.84 | -1.84 | -1.84 | -1.84 |
| EBIT | 20.39 | 32.84 | 39.60 | 43.03 | 45.02 |
| *Finance Cost* | -4.84 | -4.88 | 3.68 | 3.50 | 3.32 |
| PBT | 15.55 | 27.97 | 43.28 | 46.53 | 48.35 |
| Depr & Amort | 11.38 | 12.91 | 12.46 | 13.08 | 13.73 |
| EBITDA | 31.77 | 45.75 | 52.05 | 56.11 | 58.75 |
| Tax | -1.10 | -7.09 | -10.82 | -11.63 | -12.09 |
| Net Profit | 14.45 | 20.88 | 32.46 | 34.90 | 36.26 |
| Minority Int | 0.10 | 0.09 | 0.09 | 0.09 | 0.09 |
| Net Profit (Equity) | 14.54 | 20.98 | 32.55 | 34.99 | 36.35 |
| EPS (sen) | 11.22 | 16.15 | 22.93 | 24.64 | 25.60 |
| PER | 15.15 | 10.53 | 7.42 | 6.90 | 6.64 |
| DPS (sen) | 4.00 | 7.00 | 9.00 | 10.00 | 10.00 |
| Div Yield (%) | 2.35 | 4.12 | 5.29 | 5.88 | 5.88 |
| | | | | | |
| **Margin** | | | | | |
| EBITDA | 10.94% | 12.60% | 10.92% | 10.70% | 10.38% |
| PBT | 5.35% | 7.70% | 9.08% | 8.88% | 8.54% |
| Net Profit | 5.01% | 5.78% | 6.83% | 6.67% | 6.42% |

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## JF APEX SECURITIES - RESEARCH RECOMMENDATION FRAMEWORK

**STOCK RECOMMENDATIONS**

**BUY** : The stock's total returns* are expected to exceed 10% within the next 12 months.

**HOLD** : The stock's total returns* are expected to be within +10% to – 10% within the next 12 months.

**SELL** : The stock's total returns* are expected to be below -10% within the next 12 months.

**TRADING BUY** : The stock's total returns* are expected to exceed 10% within the next 3 months.

**TRADING SELL** : The stock's total returns* are expected to be below -10% within the next 3 months.

**SECTOR RECOMMENDATIONS**

**OVERWEIGHT** : The industry as defined by the analyst is expected to exceed 10% within the next 12 months.

**MARKETWEIGHT** : The industry as defined by the analyst is expected to be within +10% to – 10% within the next 12 months.

**UNDERWEIGHT** : The industry as defined by the analyst, is expected to be below -10% within the next 12 months.

*capital gain + dividend yield

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