

Southern Cable Group Berhad

TP: RM0.385 (+13.2%)

Cables and Wires Manufacturer

Ace Market Listing

NOT RATED

Chan Mun Chun

Tel: +603-2167 9731

mcchan@ta.com.my

www.taonline.com.my

Background

Southern Cable Group Berhad (SCGB) is principally involved in manufacturing of cables and wires that are used for power distribution, communications as well as control and instrumentation applications. The group also derives revenue from related products and services such as sales of aluminium rods, plastic compounds, and wooden cable drums.

IPO Statistics

The IPO entails a public issue of 209,348,000 new ordinary shares, and an offer for sale of 20,000,000 shares at an IPO price of RM0.34/share.

Public Issue:

- 40,000,000 new shares for application by the Malaysian public;
- 22,000,000 new shares for application by eligible parties;
- 67,348,000 new shares by way of private placement to selected investors; and
- 80,000,000 new shares by way of private placement to identified Bumiputera investors approved by MITI.

Main Competitive Advantages

1. Established track record with technical capabilities;
2. Offer wide range of cable and wire products; and
3. Experienced management team.

Valuation

At IPO price of RM0.34/share, SCGB is priced at a trailing PER of 10.0x FY19 EPS. We value the company at 12x CY21 EPS, arriving at a fair value of **RM0.385/share**.

Earnings Summary

| FYE Dec (RMmn) | 2018 | 2019 | 2020F | 2021F | 2022F |
|----------------------|-------|-------|-------|-------|-------|
| Revenue | 683.2 | 656.7 | 540.7 | 623.3 | 681.2 |
| Gross profit | 65.2 | 67.2 | 53.5 | 62.3 | 70.8 |
| EBITDA | 48.7 | 53.0 | 41.8 | 48.5 | 56.0 |
| EBITDA margin (%) | 7.1 | 8.1 | 7.7 | 7.8 | 8.2 |
| EBIT | 41.9 | 46.7 | 35.7 | 42.0 | 48.0 |
| PBT | 33.1 | 39.3 | 27.7 | 33.8 | 39.7 |
| PAT | 26.2 | 28.5 | 21.1 | 25.7 | 30.2 |
| Core profit | 25.8 | 27.1 | 21.1 | 25.7 | 30.2 |
| Core EPS* (sen) | 3.2 | 3.4 | 2.6 | 3.2 | 3.8 |
| PER^ (x) | 10.5 | 10.0 | 12.9 | 10.6 | 9.0 |
| Gross dividend (sen) | n.a | n.a | 0.5 | 0.5 | 1.0 |
| Dividend yield^ (%) | n.a | n.a | 1.5 | 1.5 | 3.0 |

Note: *based on enlarged share base of 800.0mn, ^ based on IPO price of RM0.34/share

Share Information

| | |
|-----------------------------|------------|
| Listing | Ace Market |
| Enlarged Share Capital (mn) | 800.0 |
| Market Cap @ RM0.34 (RM mn) | 272.0 |
| Issue price (RM) | 0.34 |
| Oversubscription rate | N/A |
| Estimated free float (%) | 28.7 |
| Tentative listing date | 16-Oct-20 |

Tentative Listing Dates

| | |
|---------------------------|----------------|
| Event | Tentative Date |
| Opening of the IPO | 29-Sep-20 |
| Closing of the IPO | 6-Oct-20 |
| Balloting of Applications | 8-Oct-20 |
| Allotment of Shares | 15-Oct-20 |
| Listing | 16-Oct-20 |

Ratio & Analysis

| | |
|--------------------------------|------|
| NTA per share (post IPO) (sen) | 32.0 |
| Price to NTA (x) | 1.1 |
| Proforma Gearing (x) | 0.1 |

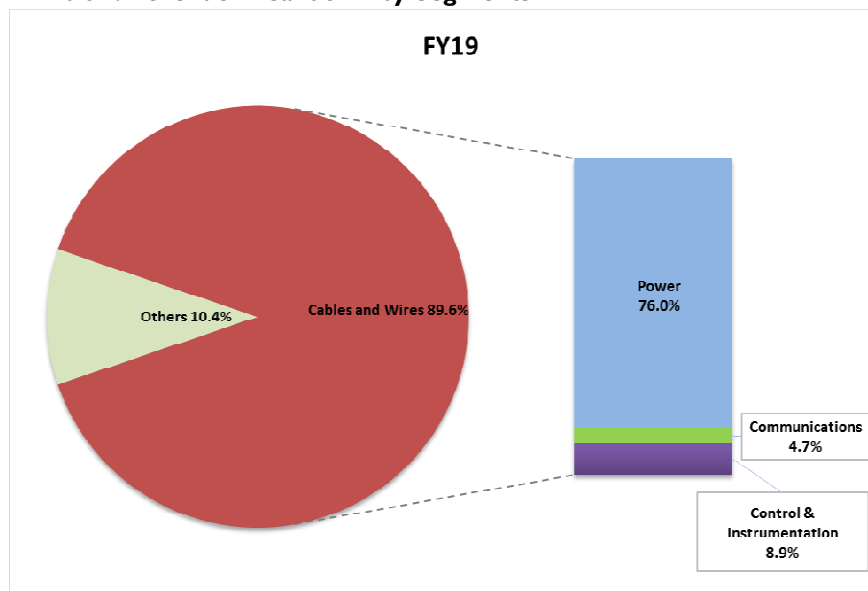
| Utilisation of Proceeds | RM(mn) | % |
|-----------------------------------|-------------|--------------|
| Capital expenditure and expansion | 30.0 | 42.2 |
| Repayment of bank borrowings | 9.2 | 12.9 |
| Working capital | 27.5 | 38.6 |
| Estimated listing expenses | 4.5 | 6.3 |
| TOTAL | 71.2 | 100.0 |

Business Overview

Southern Cable Sdn Bhd, the wholly-owned and core operating subsidiary of SCGB, was incorporated and commenced business operations in 1993. The principal business activity is manufacturing of cables and wires, and related products and services. The related products and services mainly include manufacturing of aluminium rods, trading of cables and wires, and copper strips, as well as supply and installation of rectifiers. The group's cables and wires are being used in many sectors such as power, telecommunication, oil & gas, manufacturing, building and construction.

Meanwhile, SCGB has another 2 subsidiaries, which are Nextol Polymer Sdn Bhd (Nextol) and Daya Forwarding Sdn Bhd (Daya). Nextol is principally involved in the manufacturing of plastic compounds while Daya is involved in the manufacturing and trading of wooden cable drums. At this juncture, Daya has temporarily ceased all the manufacturing activities due to reallocation of factory. Historically, the revenue was mainly derived from local market.

Exhibit 1: Revenue Breakdown by Segments



Source: Company, TA Securities

Exhibit 2: Manufacturing Plant Capacity with Utilisation Rate

| | Annual capacity | Annual actual production | Utilisation rate % |
|--|-----------------|--------------------------|-----------------------|
| FYE 2018 | | | |
| Cables and Wires (KM) | 31,080 | 25,920 | 83 |
| PVC Compounds (MT) | 7,800 | 4,800 | 62 |
| Wooden Cable Drums (pieces) | 60,000 | 26,400 | 44 |
| Aluminium Rod (MT) | 18,000 | 6,776 | 38 |
| Copper Rod (MT) | 12,000 | 8,100 | 68 |
| FYE 2019 | | | |
| Cables and Wires (KM) | 31,080 | 23,897 | 77 |
| PVC Compounds (MT) | 7,800 | 5,530 | 71 |
| Wooden Cable Drums [^] (pieces) | 60,000 | 25,530 | 43 |
| Aluminium Rod (MT) | 16,050 | 11,417 | 71 |
| Copper Rod (MT) | 12,000 | 7,952 | 66 |

Source: Company, TA Securities

Note: [^]Temporary ceased all the manufacturing activities of wooden cable drums since 29 February 2020.

Exhibit 3: IPO Structure

| Public Issue | No. of Shares | % of Enlarged Share Capital |
|---|---------------|-----------------------------|
| Malaysian public | 40,000,000 | 5.00 |
| Eligible parties | 22,000,000 | 2.75 |
| Placement to selected investors | 67,348,000 | 8.42 |
| MITI-approved Bumiputera investors | 80,000,000 | 10.00 |
| Offer for Sale | | |
| Private placement to selected investors | 20,000,000 | 2.50 |

Source: Company, TA Securities

Utilisation of Proceeds

The estimated gross proceeds of RM71.2mn raised are expected to be utilised for the followings:

Exhibit 4: Utilisation of Proceeds

| Utilisation of proceeds | Estimated timeframe for utilisation | RM'000 | % |
|--|-------------------------------------|---------------|---------------|
| Capital expenditure and expansion | 36 months | | |
| • Purchase and upgrade of machinery and equipment | | 18,500 | 26.0 |
| • Construction of new factories | | 7,500 | 10.6 |
| • Purchase and installation of ERP information technology system | | 4,000 | 5.6 |
| Repayment of bank borrowings | 6 months | 9,188 | 12.9 |
| Working capital | 6 months | 27,490 | 38.6 |
| Estimated listing expenses | 3 months | 4,500 | 6.3 |
| | Total | 71,178 | 100.00 |

Source: Company, TA Securities

Competitive Advantages

1) Established track record with technical capabilities

SCGB has a solid track record of 27 years of experience in manufacturing of wires and cables. The manufacturing operations are supported by key activities which are furnace and continuous casting as well as plastic compounds manufacturing that enable the group to control the quality and timely availability of the input materials. The group is currently a registered supplier of cables and wires with Tenaga Nasional Berhad, Sabah Electricity Sdn Bhd, Telekom Malaysia Berhad, and Petronas.

2) Offer wide range of cable and wire products

The group is able to manufacture cables and wires that are being used for power distribution and transmission, communications, as well as control and instrumentation applications. Hence, the group is able to supply a wide range of cable and wire products to fulfil the diverse needs from the pool of customers. Meanwhile, the group has also obtained various local and international certifications for its cable and wire products.

3) *Established management team*

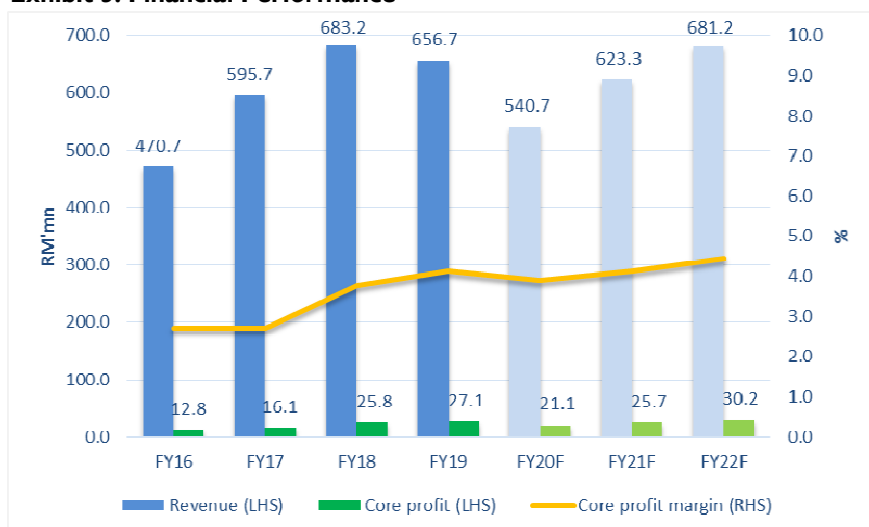
The management team is led by Managing Director, Mr. Tung Eng Hai, who has about 41 years of experience in the cable and wire industry. He is supported by the Executive Director, Mr. Wong Meng Kee, who has about 33 years of experience in the business management, and is responsible for the overall business operations.

Key Risks Relating to Business and Industry

- 1) Foreign exchange risk;
- 2) Price fluctuation of raw materials cost; and
- 3) Outbreak of Covid-19 pandemic.

Financial Highlights

Exhibit 5: Financial Performance



Source: Company, TA Securities

The revenue for FY17 increased 26.6% YoY to RM595.7mn from RM470.7mn mainly attributed to higher sales from cables and wires that were being used for power, as well as control and instrumentation applications. As a result, core profit increased 25.5% YoY to RM16.1mn from RM12.8mn a year ago. In the subsequent year, FY18 revenue surged 14.7% YoY to RM683.2mn due to higher revenue contribution from the sales of power and communications cables and wires. In addition, the stronger topline was also partly driven by higher revenue contribution from the related products and services such as sales of aluminium rods and trading of cables, wires, and copper strips. The group's core profit surged 60.4% YoY to RM25.8mn thanks to improvement in gross profit and higher gross profit margin from the cable and wire manufacturing operations.

For FY19, the group's revenue fell 3.9% YoY to RM656.7mn from RM683.2mn which was mainly attributed to the decrease in the sales of communications cables and wires. However, the group saw its core profit increased 4.9% YoY to RM27.1mn due to continuous improvement in gross profit margin in the cable and wire operations. Going forward, we forecast revenue and net profit for FY20 to be lower as the business operations especially in the IHFY20 were negatively impacted by the Movement Order Control (MCO) as a result of Covid-19 outbreak. Nevertheless, we expect the group to recover gradually following the relaxation of MCO.

Future Plans and Business Strategies

The group's future plans and business strategies are as follows:

1) Expansion of Production Facilities

The group intends to construct new factories and purchase new machinery and equipment in order to expand its manufacturing capacity for wires, cables, and plastic compounds. For wires and cables, the group targets to increase additional annual production capacity of 6,350KM by 1H2022. Meanwhile, the group plans to purchase a new ERP information technology system to replace the existing system. Besides, the group also plans to build a new factory to increase additional 4,200MT of production capacity for plastic compounds by 1H2022.

2) Expansion in Product Range

The group aims to expand its product range for cables, wires and plastic compounds in order to cater for the demand from existing and potential customers.

Outlook

According to an independent market research report prepared by Vital Factor Consulting, which was enclosed in the IPO prospectus, the sales volume of the manufacture of electric and electronic cables and wires in Malaysia increased at a CAGR of 6.2% between 2015 and 2019. Nevertheless, the sales value of the manufacture of electric and electronic cables and wires declined at an average annual rate of 0.7% during the same period.

Moving forward, we expect the demand for cables and wires especially for power and distribution to remain healthy as Malaysian government is actively pushing for rural electrification program in order to achieve 99% electricity coverage for rural areas. Meanwhile, given that SCGB's revenue is mainly derived from local market, going forward, we expect the group to look for more international presence to grow its business.

Balance Sheet

On a pro forma basis, post-listing, the balance sheet is expected to improve from a net debt position of RM97.2mn (net gearing level of 0.53x) to a net debt position of RM28.1mn (net gearing level of 0.11x).

Dividend Policy

The Board intends to adopt a policy of recommending at least 15% of the net profit in each financial year to be distributed as dividends.

Earnings Forecast

We estimate the group to register 22.1% YoY drop in core profit to RM21.1mn for FY20 due to Covid-19 outbreak. We believe the group shall be able to recover in the subsequent years by posting earnings growths of 21.9% and 17.5% to RM25.7mn and RM30.2mn for FY21 and FY22 respectively, supported by top-line growth with higher production volumes. The domestic market will remain as the main revenue generator while the export market is expected to contribute further once the group expands its production capacity with increasing international marketing activities.

All in, our FY20-22 earnings projections are premised on the key assumptions below:

- Annual production capacity for cables and wires manufacturing of 31,080KM for FY20, 33,780KM for FY21, and 40,130KM for FY22 with utilisation rate of 68%, 73%, and 66% respectively; and
- Annual production capacity for plastic compounds manufacturing of 7,800MT each for FY20 and FY21, and 12,000MT for FY22 with utilisation rate of 70%, 72%, and 60% respectively.

Valuation

We assign a target PE multiple of 12x to SCGB and arrive at a fair value of RM0.385/share. This is after considering the group has:

- Proven track record in cable and wire manufacturing industry;
- Potential growth from capacity expansion; and
- Experienced management team.

Exhibit 6: Peer Comparison

| Stock | Share price (RM) | Market Cap (RMmn) | EPS^ (sen) | P/E ratio (x) | DPS (sen) | Div Yield^ (%) | Net gearing (x) | P/B ratio (x) |
|--------|---------------------|----------------------|---------------|------------------|--------------|-------------------|--------------------|------------------|
| SCABLE | 0.21 | 66.6 | -26.6 | n.a | n.a | n.a | 3.4 | 0.5 |
| SCGB* | 0.34 | 272.0 | 3.4 | 10.0 | n.a | n.a | 0.53 | 1.1 |

Note: *based on pro-forma balance sheet

^based on previous financial year










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Appendix

Exhibit 7: Cables and Wires

| | | |
|--|--|---|
| <p>Design For Power Distribution</p>  <p>HIGH VOLTAGE CABLES</p> <div>  Aluminium Conductor Steel Reinforce (ACSR) </div> <div>  All Aluminium Alloy Conductor (AAAC) </div> <div>  High Voltage Cable (132kV) </div> | <p>Design For Manufacturing & Processing Industries</p>  <p>CONTROL AND INSTRUMENTATION CABLES AND WIRES</p> <div>  Armoured Medium Voltage Power Cable </div> <div>  Multi-core Medium Voltage Power Cable </div> <div>  Control Cable </div> | <p>Design For Oil & Gas Processing and Petrochemical Plants</p>  <p>CONTROL AND INSTRUMENTATION CABLES AND WIRES</p> <div>  Armoured Instrument Cable </div> <div>  Screen Signal Cable </div> <div>  Control Cable </div> |
| <p>Design For Fire Protection</p>  <p>FIRE RESISTANCE, FLAME RETARDANT AND LOW SMOKE ZERO HALOGEN CABLES AND WIRES</p> <div>  Non-Armoured FR Cable </div> <div>  Steel Wire Armoured FR Cable </div> <div>  Low Smoke Zero Halogen FR Cable </div> <div>  Flame Retardant FR Cable </div> <div>  FRMI & LPCB FR Cable </div> | <p>Design For Building & Construction</p>  <p>LOW VOLTAGE CABLES AND WIRES</p> <div>  XLPE Insulated PVC Sheathed Armoured Cable </div> <div>  XLPE Insulated PVC Sheathed Cable </div> <div>  PVC Insulated Non-Sheathed Cable </div> <div>  PVC Insulated PVC Sheathed Armoured Cable </div> | <p>Design For Rail & Train System</p>  <p>CONTROL AND INSTRUMENTATION CABLES AND WIRES</p> <div>  DC Track Feeder Cable </div> <div>  LAN Cable (Cat 5E-UTP) </div> <div>  Audio Cable (Halogen Free) </div> <div>  Medium Voltage Power Cable (33kV) </div> <div>  Low Voltage Power Cable (Multicore FR Armoured) </div> |

Source: Company website

| | |
|--|--|
| <p>Design For Communications</p>  <p>COMMUNICATIONS CABLES AND WIRES</p> <div>  Fully Filled Telephone Cable </div> <div>  Alarm Cable </div> <div>  Coaxial Cable </div> | <p>Design For General Usage</p>  <p>COPPER & ALUMINIUM RODS</p> <div>  Bare Copper Rod </div> <div>  Bare Copper Wire </div> <div>  Bare Aluminium Rod </div> <div>  Bare Aluminium Wire </div> |
|--|--|

Source: Company website

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Stock Recommendation Guideline

- BUY** : Total return within the next 12 months exceeds required rate of return by 5%-point.
HOLD : Total return within the next 12 months exceeds required rate of return by between 0-5%-point.
SELL : Total return is lower than the required rate of return.
Not Rated: The company is not under coverage. The report is for information only.

Total Return is defined as expected share price appreciation plus gross dividend over the next 12 months. Gross dividend is excluded from total return if dividend discount model valuation is used to avoid double counting.

Required Rate of Return of 7% is defined as the yield for one-year Malaysian government treasury plus assumed equity risk premium.

Disclaimer

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As of Monday, October 05, 2020, the analyst, Chan Mun Chun, who prepared this report, has interest in the following securities covered in this report:
(a) nil

Kaladher Govindan – Head of Research

TA SECURITIES HOLDINGS BERHAD (14948-M)

A Participating Organisation of Bursa Malaysia Securities Berhad

Menara TA One | 22 Jalan P. Ramlee | 50250 Kuala Lumpur | Malaysia | Tel: 603 – 2072 1277 | Fax: 603 – 2032 5048
www.ta.com.my