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Kian Joo Can Factory Bhd ("Kian Joo") – The forgotten can manufacturer

Recommendation **Medium Term Buy**

Share Price **RM1.41**

FINANCIAL SUMMARY				
FYE 31 Dec (RM mil)	**2008A**	**2009A**	**2010F**	**2011F**
Revenue	875.50	875.60	1,006.9	1,107.6
EBIT	97.00	68.70	116.8	127.4
EBIT Margin (%)	11.1	7.8	11.6	11.5
Pretax Profit	90.20	68.70	112.8	123.4
Net Profit	69.50	48.90	84.6	92.5
EPS (sen)	15.6	11.0	19.0	20.8`
DPS (sen)	5.0	6.3	6.7	7.3
PER (x)	9.0	12.8	7.4	6.8
Dividend Yield (%)	3.6	3.6	4.7	5.2

OTHER KEY DATA	
Listing	Main Board
Issued Cap. (mil, RM0.25 par)	444.2
Market Cap. (RM bn)	626.3
52 Week Low/High (RM)	1.10/1.50
Net Gearing (%)	1.7
P/NAV (x)	0.7
NAV/share (RM)	1.92
Major Shareholders	**(%)**
Kian Joo Holdings	34.6
EPF	20.7

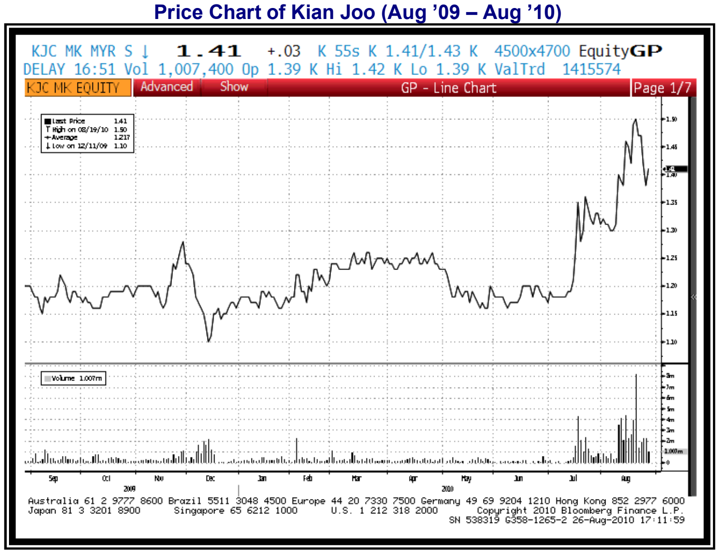
Source: Company, Bloomberg & PCM Estimates

Kian Joo is the largest can manufacturer in Malaysia and has strong presence in Vietnam.

Despite the See family tussle, Kian Joo has managed to grow its pretax earnings by CAGR of 7.6% and consistently pay out minimum 35% of the group earnings as dividends which we see as unusual strength.

Valuation wise, Kian Joo is trading at cheap 7x FY10 PER, 30% discount to its NAV and potential FY10 dividend yield of 4.7%. We recommend a medium term ***Buy*** on Kian Joo as an F&B related investment with considerable upside potential.

Price Chart of Kian Joo (Aug '09 – Aug '10)



Source: Bloomberg

Highlights:

Background – Kian Joo is the largest can manufacturer in Malaysia with > 60% and > 40% market share in Malaysia's aluminium cans and general cans segment respectively. It is also one of the oldest companies which was founded by Mr See Boon Tay in 1956 and was subsequently listed in Bursa Malaysia in 1984. Apart from can manufacturing, Kian Joo also does contract packing of milk powder and beverages for Dutch Lady and other notable fast moving consumer goods companies. Through its 51% controlled subsidiary, Box-Pak (Malaysia) Bhd, Kian Joo is also involved in corrugated fibreboard cartons manufacturing (See ***Table 1***).

Table 1: Kian Joo's composition of activity

Segment	1Q10 Operating profit (RM 'm)	%	Operating Profit Margin (%)
Cans	24.5	94.9	14.8
Cartons	0.7	2.7	1.7
Contract packing	0.6	2.4	4.2
Total	**25.8**	**100.0**	

Source: PCM and Bloomberg

The forgotten can manufacturer – The food and beverage (F&B) segment contribute approx. 90% to Kian Joo's business which means demands for its products and services are almost inelastic. According to the management, Kian Joo can pass on 100% of the raw material costs increases to their customers, but due to time lags between price renegotiation and fluctuations in raw material costs, Kian Joo has to absorb part of the costs hikes causing depletion in the operating margins. Raw materials like tin plates and aluminium coils command approx. 65% of its production costs. Amongst the listed F&B

related counters from packaging to fast food retailers, Kian Joo is still cheap and has lots of catching up to do in terms of price performance (see ***Table 2***). It seems that investors have forgotten Kian Joo which we would like to revive due to factors below:

Table 2: Kian Joo vs. other F&B related companies				
F&B Companies	**Price (RM)**	**FY10 PER**	**P/NAV**	**FY10 Dividend Yield (%)**
Cocoaland	2.87	16.8	2.9	3.4
CI Holdings	2.88	9.6	2.9	2.6
Mamee	3.37	10.5	1.9	4.7
Kian Joo	1.41	7.4	0.7	4.7
Tomypak	3.26	6.6	1.8	5.1
Source: PCM and Bloomberg				

Growing demand for canned food – As the emerging economies progress, food consumption trend tends to slowly migrate from freshly made food to readily packed food ranging from canned food to frozen food because of convenience as one's time gets more costly. This phenomenon buoys well for Kian Joo's earnings which has been growing steadily since 2000 by compounded annual growth return (CAGR) of 7.6%.

Strong presence in Vietnam and potential Indonesia expansion – As more food companies set up their operations in Vietnam and Indonesia, the demand for Kian Joo's products and services also grew which Kian Joo then expanded its operations to Vietnam. As of now, its Vietnam operations contribute approx. 20% of group earnings which it currently supplies to milk producers like Dutch Lady and Vinamilk. It now has plans to venture into Indonesia to take advantage of the huge consumer population.

Potential Can-One takeover – In May 2009, Can-One Bhd (Can-One) proposed to acquire 32.9% of Kian Joo at RM1.65 per share. However, due to some legal complications in the acquisition, the outcome of the acquisition is still pending. The fact that Can-One is willing to fork out at least RM1.65 to acquire a 32.9% stake in Kian Joo indicates that there is more to it than what Kian Joo is worth now. Should the acquisition be successful, the merger will bring synergistic benefits to Kian Joo and Can-One has the potential to become the largest can manufacturer in South East Asia, if not Asia.

Consistent dividend pay outs and low gearing – For the past 10 years, Kian Joo has consistently paid out minimum 35% of the group earnings and maintained its net gearing below 25% whilst expanding its operations to Vietnam. For the 1H10, Kian Joo witnessed a spectacular 90% jump in pretax profit vis-à-vis 1H09 attributed mainly to increased revenue as the economy recovers, better gross margins by 5.6% and overall production efficiency. The gross margins improved tremendously from 13.2% in 1H09 to 18.8% in 1H10 partly due to old inventories accumulated which Kian Joo normally keep around 3-4 months worth of inventories for its future production, and also due to better cost pass through of any increases in raw materials. This exceptional performance may not be sustainable going forward, but provided the raw material costs do not fluctuate excessively, Kian Joo is able to pass through whatever increases in raw material prices and maintain healthy low teen margins. Based on a historical payout rate of 35%, we expect Kian Joo to pay out 7.5 sen per share dividend, implying a dividend yield of 4.7% for FY10. Out of the 7.5 sen dividend per share estimated for FY10, 6.25 sen has been declared recently, of which 3.75 sen is special dividend and 2.5 sen is interim dividend.

Family squabble did not affect operations – Despite the ongoing squabble amongst the See family members for over 10 years, Kian Joo continued to perform with earnings growing by CAGR of 7.6%. We see Kian Joo's ability to perform amid various adversities as strength and believe its price will catch up once the family issues are settled like what we have seen in Tan Chong Motors Holdings Bhd (Tan Chong) case. Meanwhile, Kian Joo is trading at a low 7x FY10 PER and 30% discount to its NAV of RM1.92.

Recommendation:-

We favour Kian Joo because amongst all the F&B related companies, Kian Joo's valuation is still cheap at 7x FY10 PER and 30% discount to its NAV despite the fact that Kian Joo is the largest can manufacturer in Malaysia. In addition, given its long operating history that recorded steady growth in pretax earnings and consistent dividend payouts, we believe more is in store for Kian Joo's future especially since it has strong presence in Vietnam and plans to expand to Indonesia. We view their continuous growth in its operations in the face of the See family squabble as unusual strength signalling better things to come should the squabble come to an end. We recommend medium term ***Buy*** on Kian Joo.

For Phillip Capital Management Sdn Bhd

Nona Salleh
Executive Chairperson

APPENDIX

LIST OF STOCKS RECOMMENDED SINCE 2009

Our Picks – 2009/10						
No	**Stock**	**Date**	**Price***	**Price @ 26/08/10**	**% Change**	**Comments**
1	Axis REIT	9 Jan 09	RM0.96	RM2.10	+118.8%	Hold. Has performed well recently despite weaker earnings.
2	Tanjong Plc	26 Feb 09	RM13.27	RM21.34	+60.8%	Hold. GO at RM22.80.
3	Sino Hua-An	30 Mar 09	RM0.20	RM0.36	+80.0%	Hold. 2Q results be below expectation.
4	Axiata	20 Apr 09	RM1.74	RM4.47	+156.9%	Hold. Indo subsidiary did well in 2Q
5	QL Resources	29 May 09	RM2.18	RM4.57	+109.6%	Hold. Valuation is coming to fair value
6	Mudajaya	24 Jun 09	RM1.44	RM4.17	+189.6%	Buy on Weakness. Trade on ST. Buy on LT.
7	Kulim	25 Jun 09	RM6.05	RM8.43	+39.3%	Hold. Stronger CPO price support the price
8	AEON	28 July 09	RM4.44	RM5.06	+14.0%	Buy. One of the few blue chips that has not move yet.
9	RCE Cap	28 July 09	RM0.615	RM0.63	+2.4%	Hold. Did quite well in 2Q in terms of loan growth
10	TRC Synergy	28 Aug 09	RM1.45	RM1.03	-29.0%	Hold. Only managed to get small contracts recently
11	Fajarbaru	3 Sep 09	RM1.14	RM1.03	-9.6%	Hold. Went above RM0.99 resistance.
12	Sino Hua-An	30 Sep 09	RM0.505	RM0.36	-28.7%	*See above*
13	Hock Seng Lee	12 Oct 09	RM1.07	RM1.59	+48.6%	Buy/Hold. Price started to firm up again
14	Tomypak	26 Nov 09	RM1.64	RM3.27	+99.4%	Buy/Hold. Split issue and 1:4 bonus will ex on 1 Sept.
15	MBSB	30 Nov 09	RM0.95	RM1.40	+47.4%	Buy. We like the strong government servant loan.
16	Parkson	22 Dec 09	RM5.17	RM5.50	+6.4%	Buy. Stronger yuan augurs well for Parkson.
17	QSR	15 Jan 10	RM3.32	RM4.47	+34.6%	Hold. Bonus issue of KFC lifted price of QSR.
18	Salcon	22 Feb 10	RM0.65	RM0.70	+7.7%	Buy. Has acquired another waste water concession in China
19	UliCorp	30 Mar 10	RM0.635	RM0.66	+3.9%	Buy/Hold. Price drifting due to little interest
20	Tomypak	13 April 10	RM3.07	RM3.27	+6.5%	*See above.*
21	Dayang	29 April 10	RM1.92	RM2.02	+5.2%	Buy. Good entry level
22	Suria	14 May 10	RM1.51	RM1.58	+4.6%	Medium Term Buy. Share price has also strengthen in line with market
23	JTI	31 May 10	RM5.29	RM6.04	+14.2%	Buy. Strong earnings from increasing market share
24	Tenaga	18 June 10	RM8.35	RM8.75	+4.8%	Buy. Given the green light to start 1,000 MW coal power plant
25	KSL	30 June 10	RM1.35	RM1.54	+14.1%	Buy. High margin is KSL strength.
26	CIMB X25	22 July 10	RM1.01	RM0.97	-4.0%	Buy. Exposure to China market

**Price adjusted for dividend, bonus and rights*