

17 September 2021

Industrials | Industrial Products

CEKD (CEKD MK)

Moulding Towards Greater Heights

- **MYR0.57 FV on 14x FY22F (Aug) P/E.** CEKD is expected to raise MYR24.3m from its IPO, and proceeds will mainly go towards buying a factory and machineries, upgrading computer software and servers, marketing activities, and repaying loans. Encouraging demand across its diverse customer base, higher production efficiency, and growth of customers should lift revenue growth. With a FY20-23F earnings CAGR of 13.7%, we believe it can trade up to 14x, on par with the Bursa Malaysia Industrial Products Index.
- **Encouraging demand across diverse customer base.** The rapid growth in the e-commerce space, further accelerated by the pandemic, has led to a boost in online purchases and higher demand for packaging materials. The rise in exports of electrical & electronics (E&E) products to major trading partners – China and the US – is expected to lead to higher demand for its products. Customer innovation has led to specification revisions, and this tends to drive demand for more die-cutting tool moulds to die-cut paper boxes, cartons and electrical components. We believe CEKD's ability to cater to customised die-cutting solutions, aside from its participation in the early development stages of its customers' product packaging solutions, should contribute to customer stickiness.
- **Consolidation of factory operations to lift efficiency.** The group has identified a factory (worth MYR8.8m) to consolidate two of Hotstar's operations under the same roof. This should help to streamline its productivity and lift production efficiency, with no immediate capacity expansion plans. As the new factory is unable to consolidate operations for all three rented properties, CEKD is sourcing for a second new factory.
- **Higher emphasis on export sales to expand customer base.** CEKD is exploring potential opportunities to widen its customer base in the South-East Asian (SEA) market (Vietnam and Thailand), through existing customers that have business operations in these areas. The group plans to participate in trade exhibitions and provide technical sharing sessions to raise product awareness. We believe being the sole certified die maker in SEA by Bobst (an established die-cutting machine manufacturer with a presence in over 20 countries in Europe and SEA), the recognition of its product quality will help CEKD to stand out among peers in terms of branding. We gather that margins could be higher for products that have higher complexity and requirements.
- **Earnings forecasts.** We estimate FY21F-23F PAT of MYR6.2-8.9m, assuming a pick-up in global economic activities across various industries and the launch of new products driving additional demand for moulds. This is assuming no significant delay or cancellation of orders caused by heightened movement restrictions or disruption in business operations.
- **Improving financials.** As at 7MFY21, net gearing stood at 0.1x. Post listing, we expect CEKD to turn to a net cash position from FY22F, with the IPO proceeds and operations cash flow. While there is no dividend policy, we assume FY22F-23F DPS to remain at 2 sen, implying a 4% yield.
- **Risks:** Ongoing pandemic and future outbreak causing business disruption, raw materials availability, general market downturn leading to lower demand.

Fair Value (Return)	MYR0.57 (+19%)
IPO Price:	MYR0.48
Closing Application Date:	17 Sep 2021
Indicative Listing Date	29 Sep 2021

Analyst

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Company Description

CEKD is principally involved in the manufacturing of die-cutting moulds and trading of related consumables, tools and accessories, mainly providing to the paper printing and packaging, E&E and other industries – such as automotive, plastic packaging, textile and leather.

IPO Details

Public Issue (%)	26.0
Shares outstanding (m)	194.6m
Implied market cap	MYR93.4m

Major Shareholders (%)

CEKD Holding	74.0
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Utilisation of IPO Proceeds

Acquisition of factory for Hotstar	8.8
Purchase of new machineries	3.0
Upgrade and development of computer software and server	1.3
Repayment of bank borrowings	4.0
Marketing activities	1.5
General working capital	2.7
Estimated listing expenses	3.0
TOTAL	MYR24.3

Additional Data

Listing Market	ACE
Bursa Code	0238

Forecasts and Key Data	Aug-19	Aug-20	Aug-21F	Aug-22F	Aug-23F
Total turnover (MYRm)	28.4	26.4	26.7	29.7	31.4
Recurring net profit (MYRm)	5.4	6.0	6.2	7.9	8.9
Recurring net profit growth (%)	(20.4)	11.5	2.6	27.9	11.9
Recurring P/E (x)	12.8	11.4	15.1	11.8	10.5
P/BV (x)	2.0	1.8	2.3	1.4	1.3
P/CF (x)	13.8	10.2	10.8	8.7	7.9
Dividend Yield (%)	0.0	5.0	3.6	4.2	4.2
EV/EBITDA (x)	7.3	8.9	9.5	5.5	4.7
Return on average equity (%)	18.0	16.7	14.7	14.8	12.7
Net debt to equity (%)	17.5	4.2	14.2	net cash	net cash

Source: Company data, RHB

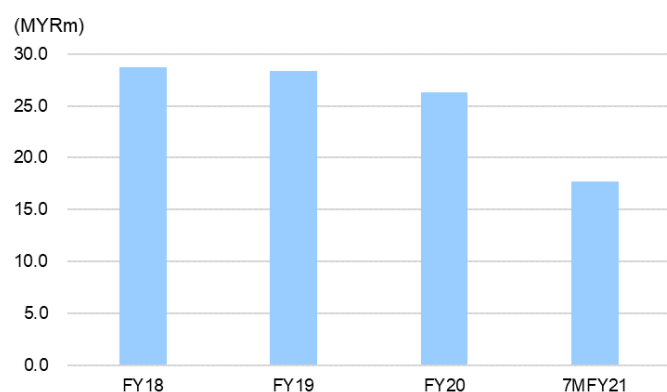
Financial Overview And Valuation

7MFY21 results review. CEKD's 7MFY21 revenue grew 10.5% YoY, attributable to a higher quantity of die-cutting moulds sold (+2,501 units to 65,624 units, or +4% YoY) and higher ASP (+3.9% to MYR215 per unit in 7MFY21). The higher orders were mainly from local customers across the packaging, E&E, and automotive industries. Meanwhile, the higher ASP was a result of more complex die-cutting moulds being manufactured, as a higher level of automation is required by its customers to reduce dependency on manual labour. Besides higher revenue from manufacturing activities, trading activities picked up as well (+29.2% YoY), from a higher quantity of base boards being sold overseas, mainly Australia (+110.8% YoY) and Thailand (+43.4% YoY) – the price of base boards is expected to increase further.

After stripping off listing expenses of MYR0.51m, 7MFY21 core PAT of MYR4.5m implied a stronger PAT margin of 25.6% (7MFY20: 22.1%), further aided by the reduction in the machinery upkeep expenses, carriage inwards expenses, and term loan interest.

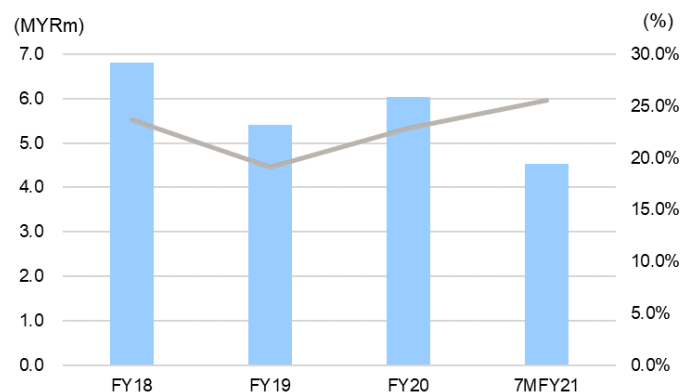
Impact of MCO. In the period of Mar-May 2020, the group saw a 30% and 34% decline YoY in local and overseas sales for its die-cutting moulds and tools business, as orders were reduced. However, it has not been largely impacted by the current movement restrictions so far, as it is considered as an essential service and its main manufacturing facilities are allowed to operate during this period.

Figure 1: Historical revenue trend



Source: Company data

Figure 2: Historical core PAT and margin trend



Source: Company data, RHB

Improving financials. As at 7MFY21, net gearing stood at 0.1x. Post listing, c.MYR4m of IPO proceeds will be used to pare down borrowings and lower interest expenses. We expect CEKD to turn to a net cash position from FY22F, with the IPO proceeds and operations cash flow. While there is no dividend policy, the group has declared dividends for FY20 and FPE21 (or 7MFY21). In view of acquisition and upgrading plans in place, we assume FY22F-23F DPS to remain at 2 sen, implying a 4% yield.

USD/MYR earnings sensitivity. Based on 7MFY21, c.14.1% of sales (c.MYR2.5m) and 78.2% of purchases (c.MYR2.1m) are denominated in foreign currencies. Although the majority of material purchases are in foreign currencies, it only contributes to c.25% of cost of sales. After netting off sales and purchases, based on our estimates, every 5% appreciation of the USD would only lead to an increase in CEKD's PAT by c.1%. We believe this could be also contributed by the group's practice of keeping at least four months' worth of inventory. As the group purchases premium wood and processed steel rules instead of raw wood or raw steel, prices do not fluctuate materially according to the commodity prices.

Earnings forecasts. We estimate FY21F-23F PAT at MYR6.2-8.9m, assuming a pick-up in global economic activities across various industries and the launch of new products that will drive demand for new and additional moulds. This is assuming no significant delays or cancellation of orders caused by heightened movement restrictions, or disruptions in business operations across countries.

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Valuation. Our fair value of MYR0.57 is based on 14x FY22F P/E. CEKD will be the only listed die-cutting mould manufacturer, and its closest peers that we could compare with are in the business of precision moulds and high precision metals (Figure 3). Having said that, we are unable to do a close comparison, as there is no coverage for these counters and their historical P/E's were relatively high. Moreover, we think that CEKD, being the sole certified die-maker by Bobst in SEA, gives it the competitive advantage in the die-cutting mould industry, as this is a form of recognition for its product quality. Note that Bobst is an established die-cutting machine manufacturer with a presence in over 20 countries in Europe and SEA.

As such, we deem our valuation, which is in line with the Bursa Malaysia Industrial Production Index, as a better comparison yardstick. While its market cap upon listing is relatively small, our FY22F PAT of +27.9% YoY is higher than the index's flattish FY22F growth. Overall, we expect FY20-23F earnings CAGR of 13.7%. Hence, we believe our valuation is justifiable. This is on top of the encouraging demand across a diverse customer base, higher production efficiency from the consolidation of factory operations and new machineries, and the expansion of its customer base through export sales, while being backed by stronger financials under the helm of an experienced management team.

Figure 3: Peer comparison

Company	FYE	Price	Mkt Cap (MYRm)	P/E (x)				Div. Yld (%)	ROE (%)	P/BV (x)	NP Growth (%)	
		15 Sep 21 (MYR)		FY19/ 20	FY20/ 21	1 Yr Fwd	2 Yr Fwd	1 Yr Fwd	1 Yr Fwd	1 Yr Fwd	1 Yr Fwd	2 Yr Fwd
Kumpulan H&L High-Tech	Oct	2.26	248	24.6	34.0	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Wong Engineering Corp	Oct	2.02	222	39.5	71.4	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
YBS International	Mar	0.39	96	156.0	42.9	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Weighted Average				52.8	50.1							
CEKD	Aug	0.48	93	12.8	11.4	15.1	11.8	3.6	14.7	2.3	2.6	27.9

Source: Bloomberg, RHB

Outlook

Encouraging demand across its diverse customer base. CEKD's products can be used in various industries and the group mainly serves the paper printing and packaging, and E&E industries. The rapid growth in the e-commerce space, further accelerated by the pandemic, has led to a boost in online purchasing and higher demand for packaging materials. Meanwhile, the growing emphasis on environmentally friendly packaging worldwide has also contributed to higher demand for paper and paperboard products that are recyclable and biodegradable. The increasing demand from the end-user industry, in turn, flows back to higher demand for moulds to produce relevant sustainable packaging materials, as the moulds and tools are used to die-cut paper boxes and cartons.

As for the E&E industry, the die-cutting tools are used to die-cut electrical components which are then used in electrical products such as television panels, laptops, hard disks, audio speakers, remote controllers and washing machine panels. With the increase in exports of E&E products to major trading partners – China and the US – we believe more R&D activities are vital for companies to launch more products, improve technical capabilities in order to be more competitive. Since the group produces customised die-cutting moulds based on customer specifications, we believe the increase in new products by customers will drive demand for more die-cutting tool moulds.

CEKD has long-established relationships (of more than 10 years) with its Top 5 customers (total: 24.6% of 7MFY21 revenue), indicating customer stickiness as well as a form of quality recognition by customers. As there is no single customer that contributes more than 10% of revenue and as CEKD has a large and diverse customer base across the paper printing and packaging, E&E, automotive, plastic packaging, textile and leather industries, this shows that the group is not heavily reliant on any one customer or industry.

In terms of FY20 industry revenue, CEKD is estimated to have a 13.4% market share in the die-cutting tool manufacturing industry. Based on the independent market research report by Protégé, the die-cutting tools manufacturing industry underwent a contraction of 8.7% in FY20 revenue, mainly due to the global economic slowdown as caused by COVID-19. It has projected the industry to expand by a CAGR of 3.2% from 2019 to 2025. With progressive improvements in global economic activities, we estimate FY20-23F revenue and PAT CAGR of 6.0% and 13.7%, as we expect a pick-up in demand.

Consolidation of factory operations and investment in machineries to lift production efficiency. CEKD is currently operating from six factories (four in Kuala Lumpur, two in Penang). Within 24 months from the listing date, it is looking to purchase two new factories in Kepong. As of now, it has found a factory (worth MYR8.8m) to consolidate two of Hotstar's operations under the same roof. Note that Hotstar's operations are currently being carried out in three separate locations. As such, the new factory is expected to help to streamline its productivity and lift production efficiency, with no immediate capacity expansion plans.

Given the new factory is unable to consolidate operations for all three rented properties, the group is sourcing for the second new factory in the same area. It is expected to be financed through bank borrowings and/or internally generated funds.

Figure 4: Production capacity and utilisation rates

Annual production capacity (units)	FY20	7MFY21
Flatbed die-cutting moulds & rotary die-cutting mould	133,851 ¹	80,000 ³
Other die-cutting moulds and tools	13,292 ²	7,754 ⁴
Actual production (units)	FY20	7MFY21
Flatbed die-cutting moulds & rotary die-cutting mould	104,542	65,264
Other die-cutting moulds and tools	6,094	3,225
Utilisation rate (%)	FY20	7MFY21
Flatbed die-cutting moulds & rotary die-cutting mould	78.1%	81.6%
Other die-cutting moulds and tools	45.8%	41.6%

¹: Based on 8-hour shift, 2 shifts per day, and 20 working days per month for 12 months

²: Based on 8-hour shift, 1 shift per day, and 20 working days per month for 12 months

³: Based on 8-hour shift, 2 shifts per day, and 20 working days per month for 7 months

⁴: Based on 8-hour shift, 1 shift per day, and 20 working days per month for 7 months

Source: Company data

Besides the new factory, c.MYR4.3m of IPO proceeds is allocated to be used within 24 months from the listing date for the purchase of machineries and upgrade of computer software and server. This is expected to help lift production capability and automate certain production process, thereby reduce dependency on labour as well as improve precision and consistency of die-cutting moulds.

Figure 5: Purchase of machinery and upgrade of computer software

Machineries and software	Units	Estimated cost (MYRm)
Automatic steel rule processor	3	1.2
Laser cutting machine	1	1.8
CAD software	1	0.3
Upgrade Focuswin and Hotstar's computer server	1	0.5
Upgrade ERP system and integrate with CAD software	1	0.5
Total		4.3

Source: Company data

Meanwhile, the new machines are anticipated to enhance CEKD's capability in expanding its product portfolio for the paper printing and packaging industries. We believe this is essential to remain up to date to customer needs as well as tap into potential new customer base.

With the purchase of a new laser-cutting machine, the group is able to have in-house resources to cut metal sheet base materials, as compared to relying on outsourcing the cutting process currently. This should help it to have a better response time, flexibility, and potentially reduce production cost in the long run.

Additionally, the integration of existing ERP system with CAD software, and the setting up of a barcode inventory system should help to lift operational efficiency, as it aligns the tracking of inventory and accelerate ordering and procurement of raw materials.

Higher emphasis on export sales to expand customer base. The group is exploring potential opportunities to widen customer base in the South-East Asian market – Vietnam and Thailand – through its existing customers that have business operations in the said countries.

In order to reach out to more global customers, CEKD has allocated c.MYR1.5m of IPO proceeds for marketing activities. This includes participating in trade exhibitions such as Pack Print International (which it participated in Thailand back in 2017) and provide technical sharing sessions through conferences and seminars in order to demonstrate its products existing and prospective customers, as well as advertise in international trade magazines (ie Folding Carton and International Paperboard). Besides raising product awareness, these activities could serve as a direct platform of data collection based on customer feedback.

Moreover, as of 6 Aug, CEKD's subsidiary, Sharp Die Cutting Mould (Sharp DCM), is the sole certified die-maker by Bobst in SEA, providing die-cutting moulds and tools to its customers – indicating that Sharp DCM's products are up to standard for Bobst's die-cutting machines. Note that Bobst is an established die-cutting machine manufacturer with a presence in over 20 countries in Europe and SEA. In our view, besides being in compliance with ISO9001:2015 standards, this serves as an additional recognition for its product quality.

On top of that, as Bobst's certified die maker, Sharp DCM has access to Bobst's latest die-cutting technology that allows it to respond quickly to Bobst's technological advancements in the die-cutting tools manufacturing industry. While the group is not dependent on Bobst's certification for sales, we believe this helps it to stand out among peers in terms of operations and branding.

Qualified to be a *shariah*-compliant counter. To be listed as a *shariah*-compliant counter, the financial ratio for cash over total assets and debt over total assets must be below 33%. Based on the 7MFY21 audited numbers, CEKD has met both of the criteria. As such, we believe the group will be listed as a *shariah*-compliant counter in the next Securities Commission review.

Key Risks

Ongoing pandemic and future outbreak cause business disruption. The ongoing pandemic and any future outbreak may have a significant adverse impact on the group, as it could disrupt the supply chain, thereby affecting CEKD's operations, customer demand, as well as shortage or delay in supply of raw materials.

In view of this, the group has implemented new COVID-19 standard operating procedures, ie requiring workers to declare their condition of health and travel history prior to returning to the office and factories, movement control routing, mandating the use of face masks at all times, social distancing, daily temperature checks, and daily sanitisation of the office and factories. For employees that appear to develop any COVID-19 symptoms and not recover after being quarantined for three days, a diagnosis is required, as well as treatment from a nearby hospital, if necessary.

Also, the group has been conducting weekly mass testing (costing c.MYR20,000 per month) for all employees since the end of July for detection purposes. From September onwards, it is looking to conduct bi-weekly mass testing (at a cost of about MYR10,000 per month).

Dependent on availability and quality of raw materials. Any prolonged shortage or interruption in the supply of raw materials may disrupt business operations. While its top five major suppliers accounted for c.54% of its 7MFY21 purchases, it is not dependent on the major suppliers. Having said that, the group has been maintaining a good working relationship with its major suppliers for the past three financial years without facing any disruption, thus far.

Major raw materials such as wood and processed steel rules accounted for c.23.4% of 7MFY21 cost of sales. As part of its raw materials and cost management, the group makes the effort to keep at least four months' worth of inventory as its minimum reorder level for major raw materials. As such, the COVID-19 pandemic did not have a material impact on its supply chain, since the company already bought raw materials in 1Q20 prior to MCO 1.0.

General market downturn could lead to lower demand in the end-user markets. The group is dependent on the quantum of demand from the end-user markets, especially for consumer products. As such, in the event of an economic downturn, lower consumer spending will have a domino effect – whereby it reduces demand for consumer products and related packaging. This, in turn, would lower the demand for die-cutting moulds, as lesser moulds would be required by the paper printing and packaging industry.

No long term contracts with customers. Generally, customers tend to purchase on a weekly or monthly basis. It could even be on a daily basis, depending on the customer. Given that it has a large and diverse customer base across various industries, while maintaining over 10 years of working relationship with its major customers, we believe customer stickiness could be a sign of confidence on its product quality.

Company Overview

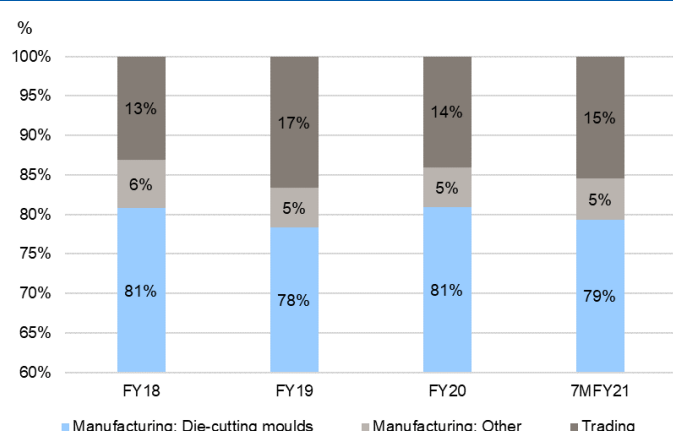
A die-cutting solutions provider

CEKD is principally involved in the manufacturing of die-cutting moulds and trading of related consumables, tools and accessories. It has an extensive customer base (1,309 customers as of early August), mainly providing to the paper printing and packaging, E&E, and other industries such as automotive (to die-cut parts such as engine gaskets, emblems, fabric and leather materials to wrap interior components such as steering wheels, car seats and sun visors), plastic packaging, textile and leather.

CEKD also helps its customers to convert raw materials provided by customers into semi-finished die-cutting moulds.

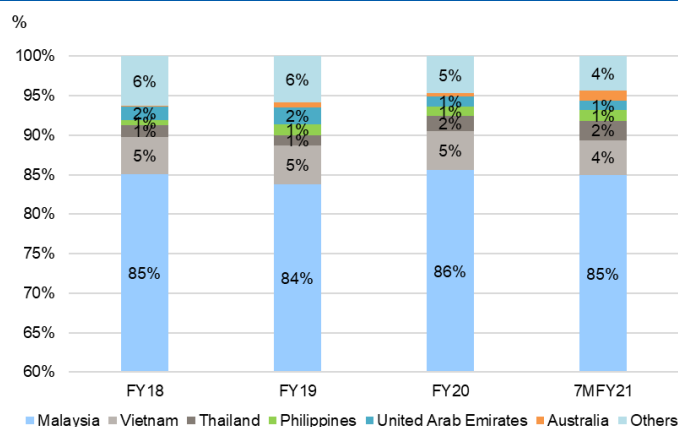
As of 7MFY21, export sales made up to c.15% of total revenue, within its historical range of 14-16% for FY18-FY20. This includes Vietnam, Thailand, the Philippines, Australia, the United Arab Emirates, and others.

Figure 6: Revenue by business segment



Source: Company data

Figure 7: Revenue by geographical market



Source: Company data

Key senior management

In 1994, Deputy Executive Chairman Yap Tian Tion joined Sharp DCM via an acquisition of a 49.2% stake from Wong Kin Loi. With his industry experience in manufacturing die-cutting moulds and trading in related consumables, tools and accessories, Sharp DCM's business grew along the way and the product offering was diversified to the converting, paper printing and packaging, as well as E&E industries. Over the years, the company underwent a series of shareholding restructuring, and CEKD Holding became the sole shareholder of Sharp DCM in 2018.

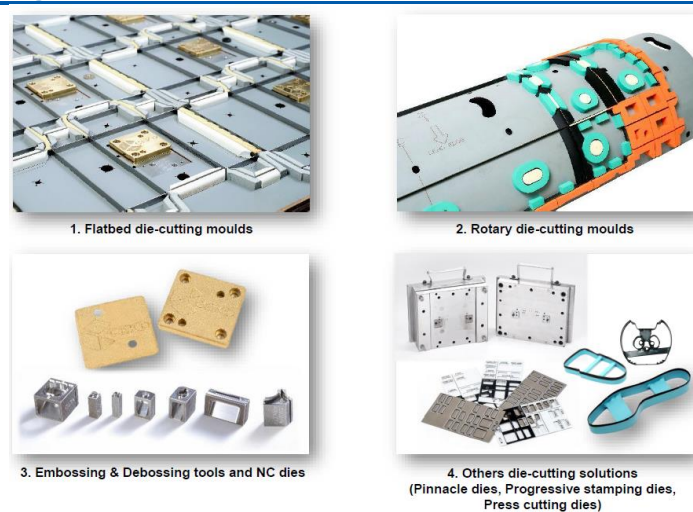
CEKD has a succession plan in place, whereby Yap Kai Ning – the daughter of Yap Tian Tion – has been identified as the successor. She joined Sharp DCM in 2008, and has exposure in the entire group's operations before being appointed as Managing Director in 2015. Meanwhile, Yap Kai Min accumulated experience in group sales and marketing, as well as in the supply chain department before being appointed as COO in 2020, assisting the managing director in overseeing day-to-day operations. She is also responsible for the continuous integration and implementation of the ISO-compliant quality management system. In view of the key management team's extensive experience in the industry and its succession plan in place, we believe the group should be able to weather through challenges.

Figure 8: Utilisation of IPO proceeds

Utilisation of proceeds	Amount (MYRm)	Percentage (%)	Estimated timeframe for utilisation
Acquisition of factory for Hotstar	8.8	36.2	24 months
Capital expenditure comprising:			
Purchase of new machineries	3.0	12.4	24 months
Upgrade and development of computer software and server	1.3	5.4	24 months
Repayment of bank borrowings	4.0	16.5	6 months
Marketing activities	1.5	6.2	24 months
General working capital	2.7	11.0	24 months
Estimated listing expenses	3.0	12.3	Immediately
Total	24.3	100.0	

Source: Company data

Figure 9: CEKD's products



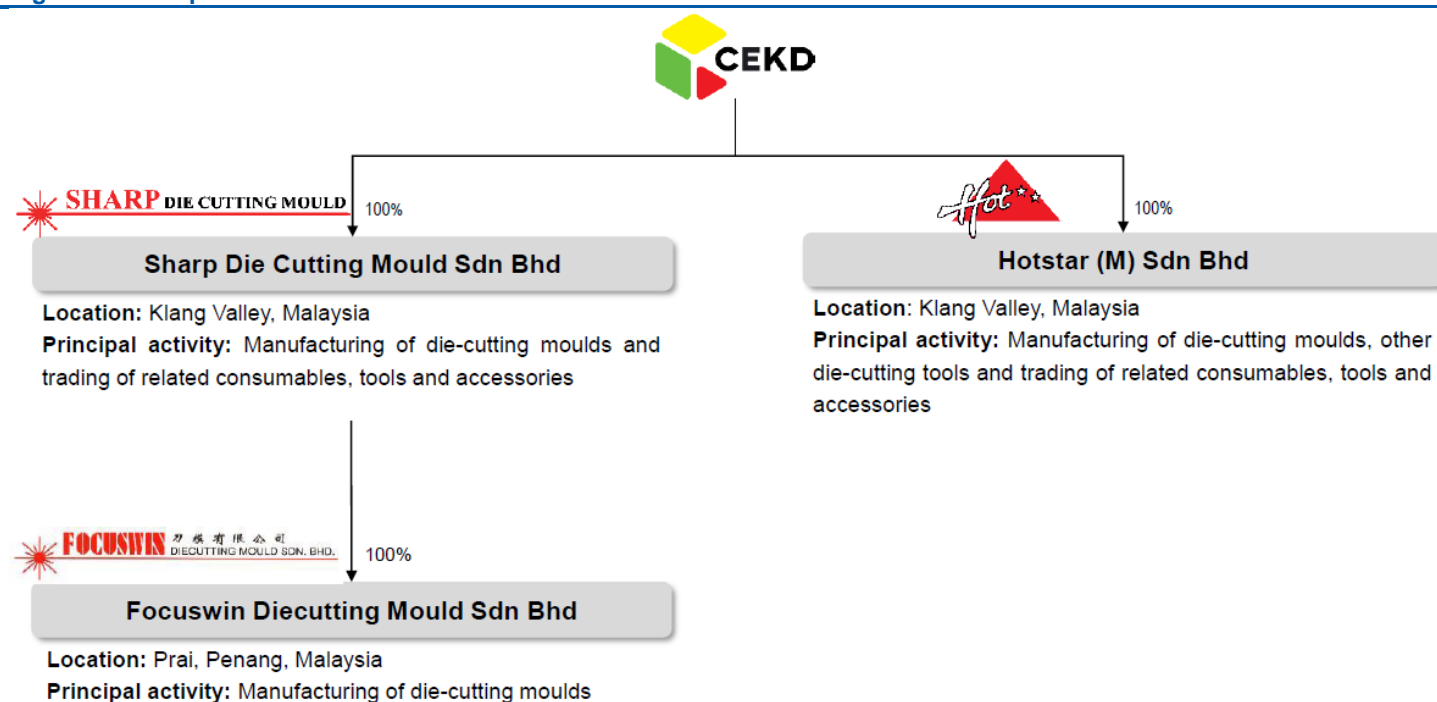
Source: Company

Figure 10: CEKD's trading products



Source: Company

Figure 11: Group structure



Source: Company

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