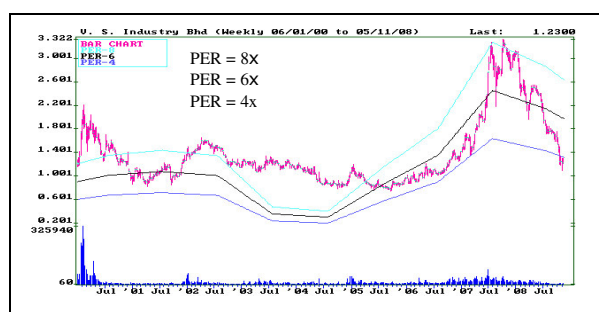


Date: 6 November 2008

Texchem Resources <i>Expect Stronger 4Q</i>	Price:	RM0.965
	Market Capitalisation:	RM119.8m
	Board:	Main Board
	Sector:	Trading Services
	Stock Code:	8702
	Recommendation:	SELL

<u>Key Stock Statistics</u>	<u>2007</u>	<u>2008F</u>
EPS (est.)	14.4	4.6
P/E (est.)	6.7	20.9
Dividend/Share	12.0	12.0
NTA/Share (RM)	1.02	0.98
Book Value/Share	1.43	1.39
Issued Capital (mil shares)	124.1	
52-weeks Share Price Range	0.90-1.34	
<u>Major Shareholders:</u>	<u>%</u>	
Texchem Holdings	31.4	
Texchem Corporation	20.6	
Tan Sri Dato' Seri Fumihiko Konishi	5.6	

PE Band Chart



1. Highlights:

Expect stronger 4Q. Although Texchem's 9M net profit of RM2.5m accounted for just 44.4% of our full-year estimate, we consider the results to be in line as 4Q is a seasonally stronger quarter. Moreover, the sharp fall in crude oil prices since Jul should help ease margin pressures. As expected, Texchem did not declare any interim dividend for the quarter

Qoq, net profit increased by 118% ... largely on the back of a lower effective tax rate (3Q: 57.8% vs. 2Q: 84.3%). Pretax profit was flat qoq as the drop in operating profit (-18.9% qoq due to cost pressures) was largely offset by lower associate losses. We note that except for the family care division, all three other divisions saw their EBIT margins contract by 0.5-1.4%-pts qoq due to, we believe, higher material and operating costs.

... but 9M core pre-tax profit falls 13.1%. 9M revenue was up 22.4% yoy led by the industrial segment (+44.3% yoy due to contribution from subsidiary acquired in Oct 2007) and food division (+7.1% yoy), partly offset by lower contribution from the family care division (-19.6% yoy) following the sale of the FMCG business. 9M core pre-tax profit, however, fell 13.1% yoy due to margin squeeze (operating profit margin dropped 0.4%-pts yoy) and higher associate losses (in 2Q).

Net gearing level continues to rise. As at end-3Q, Texchem's net gearing stood at 1.51x, up from 1.38x as at end-Jun 2008 and 1.12x at end-3Q07. The high financial leverage puts Texchem at risk should the economic situation turn out to be worse than expected while increasing earnings volatility, in our view.

<u>Per Share Data</u>	<u>2007</u>	<u>2008F</u>	<u>2009F</u>	<u>2010F</u>
Book Value (RM)	1.43	1.39	1.40	1.43
Cash Flow (sen)	44.5	33.8	39.9	43.0
Earnings (sen)	14.4	4.6	9.7	11.8
Dividend (sen)	12.0	12.0	12.0	12.0
Payout Ratio	93.5	192.0	93.2	76.0
PER (x)	6.7	20.9	10.0	8.1
P/Cash Flow (x)	2.2	2.9	2.4	2.2
P/Book Value (x)	0.7	0.7	0.7	0.7
Dividend Yield (%)	12.4	12.4	12.4	12.4
ROE (%)	6.7	3.3	6.9	8.4
Net Gearing (%)	113.5	145.4	142.0	135.3

<u>P&L Analysis (RM mil)</u>	<u>2007</u>	<u>2008F</u>	<u>2009F</u>	<u>2010F</u>
Year-end: Dec				
Revenue	1,258.6	1,348.3	1,383.1	1,415.7
Operating Profit	41.6	39.2	41.6	43.3
Depreciation	(37.3)	(36.2)	(37.6)	(38.7)
Interest Expenses	(17.1)	(16.3)	(16.3)	(16.3)
Pre-tax Profit	29.7	13.9	20.7	25.4
Effective Tax Rate	26.7	50.0	30.0	30.0
Net Profit	17.9	5.7	12.0	14.7
Operating Margin	3.3	2.9	3.0	3.1
Pre-tax Margin	2.4	1.0	1.5	1.8
Net-Margin	1.4	0.4	0.9	1.0

Risks. The risks include: 1) stronger-than expected margins, which could be due to falling raw material prices; and 2) quicker-than-expected recovery in the global economy, which would aid in the recovery of the semiconductor and consumer electronic sectors.

Forecasts. No change to our forecasts for now.

2. Recommendation:

We have maintained our indicative fair value of RM1.00, which is based on unchanged CY09 PER of 10x. Maintain **Sell** call on the stock.

Table 1 : Earnings Review

FYE Dec (RMm)	3Q07	2Q08	3Q08	QoQ (%)	YoY (%)	9M07	9M08	YoY (%)	Comments
Revenue	320.2	386.4	406.3	5.1	26.9	931.4	1,139.7	22.4	Yoy growth due to stronger contribution from the industrial division, partially offset by the sale of the FMCG business (in May 2007).
Operating profit	10.3	10.5	8.5	(18.9)	(17.4)	26.0	27.0	3.8	Slower yoy growth (as compared to revenue) as margins were squeezed due to higher material and operating costs.
Interest expense	(4.1)	(4.4)	(4.7)	7.0	16.5	(13.2)	(13.1)	(0.5)	
Associates	0.5	(3.0)	(0.7)	(76.4)	>100	(1.2)	(3.8)	>100	2Q mainly hit by, we believe, suspension of seafood exports to EU.
Exceptionals	0.0	0.0	0.0	nm	nm	6.2	0.0	(100.0)	Relates to gain on disposal of the FMCG business.
Pre-tax profit	6.7	3.1	3.1	(0.4)	(54.4)	17.8	10.1	(43.3)	
Tax	(1.9)	(2.6)	(1.8)	(31.7)	(8.6)	(6.5)	(6.5)	0.3	
Minority interest	(1.1)	(0.0)	(0.3)	>100	(76.3)	(2.0)	(1.0)	(48.9)	
Net profit	3.6	0.5	1.0	>100	(72.0)	9.3	2.5	(72.7)	
Margins (%)									
Op profit	3.2	2.7	2.1			2.8	2.4		
Pre-tax	2.1	0.8	0.8			1.9	0.9		
Effective tax rate	28.8	84.3	57.8			36.5	64.7		Above statutory rate as losses by certain subsidiaries could not be offset against the taxable profits made by other subsidiaries as well as non-deductibility of certain expenses.
Net profit	1.1	0.1	0.3			1.0	0.2		
Segmental revenue									
Industrial	155.6	210.3	224.9	6.9	44.5	429.9	620.3	44.3	Higher yoy due to consolidation of subsidiary acquired in Oct 2007.
Packaging	58.5	57.7	61.0	5.6	4.3	165.8	176.6	6.5	
Family care	29.5	38.8	36.5	(6.0)	23.9	128.3	103.2	(19.6)	Lower yoy due to sale of the FMCG business.
Food	85.3	80.5	85.0	5.6	(0.3)	226.5	242.7	7.1	
Eliminations	(8.6)	(1.0)	(1.1)	14.7	(87.1)	(19.2)	(3.1)	(84.1)	
Total	320.2	386.4	406.3	5.1	26.9	931.4	1,139.7	22.4	
Segmental results									
Industrial	3.9	6.3	5.7	(9.4)	46.2	10.4	14.6	39.8	Yoy growth lifted by higher revenue.
Packaging	3.7	2.8	2.7	(6.1)	(28.2)	9.0	8.3	(7.4)	
Family care	3.0	1.4	1.4	(4.1)	(53.0)	8.7	5.0	(42.7)	
Food	1.3	1.5	0.4	(74.6)	(70.7)	1.7	3.7	>100	9M improvement due to, we believe, better all-round performance from the seafood processing business and Sushi King chain of restaurants
Eliminations	(1.6)	(1.6)	(1.6)	3.8	5.3	(3.8)	(4.6)	20.2	
Total	10.3	10.5	8.5	(18.9)	(17.4)	26.0	27.0	3.8	
Segmental margins (%)									
Industrial	2.5	3.0	2.5			2.4	2.4		
Packaging	6.3	4.9	4.4			5.4	4.7		Affected by higher material and operating costs, in tandem with the increase in crude oil price.
Family care	10.0	3.7	3.8			6.8	4.8		Weak margins due to cost pressures.
Food	1.5	1.8	0.4			0.8	1.5		Weak margins due to cost pressures.

Source: Company, RHBRI

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Outperform = The stock return is expected to exceed the KLCI benchmark by greater than five percentage points over the next 6-12 months.

Trading Buy = Short-term positive development on the stock that could lead to a re-rating in the share price and translate into an absolute return of 15% or more over a period of three months, but fundamentals are not strong enough to warrant an Outperform call. It is generally for investors who are willing to take on higher risks.

Market Perform = The stock return is expected to be in line with the KLCI benchmark (+/- five percentage points) over the next 6-12 months.

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Industry/Sector Ratings

Overweight = Industry expected to outperform the KLCI benchmark, weighted by market capitalisation, over the next 6-12 months.

Neutral = Industry expected to perform in line with the KLCI benchmark, weighted by market capitalisation, over the next 6-12 months.

Underweight = Industry expected to underperform the KLCI benchmark, weighted by market capitalisation, over the next 6-12 months.

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