STANDARD & POOR'S

Texchem Resources

Recommendation: **STRONG BUY**

Stock Code: **8702** Bloomberg: **TEX MK** Price: **MYR1.60** 12-Month Target Price: **MYR2.00** Date: **May 10, 2006**

Board: Main

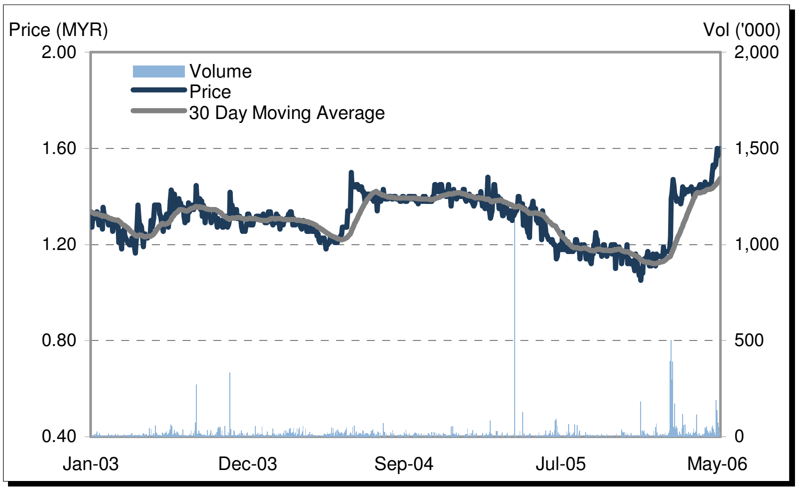
Sector: Trading / Services

GICS: Industrials / Industrial Conglomerates

Market Capitalization: MYR198.6 mln

Summary: Texchem Resources (TRB) is an investment holding company with subsidiaries engaged in four core businesses: industrial, packaging, family care and food.

Analyst: Christopher Lee



Results Review & Earnings Outlook

- Texchem's 1Q06 net profit of MYR4.4 mln, up 48.3% from 1Q05, was in line with our expectations. 1Q06 net profit accounted for about 23% of our full year forecast for 2006. Revenue increased by 3.4% YoY, as higher manufacturing and consumer revenue more than offset lower industrial trading revenue. EBIT margin rose to 3.5% from 3.2% due to improved profitability of the consumer division. Industrial and manufacturing margins were stable. The group did not declare any dividend for 1Q06, as it was the case the year before.

- Texchem continued to benefit from greater focus following the consolidation of its business activities in the past four years. The group's packaging division is riding on positive IT sector momentum particularly semiconductors. A separate listing of the packaging division in the Singapore Exchange (SGX) is expected in 3Q06. The group could reap exceptional gains from the spin-off, which we have not included in our forecast.

- We believe Texchem's other divisions should turn in stable performance in 2006 despite higher raw material prices. Industrial trading should benefit from the commencement of its operations in overseas markets. Its food processing business in Myanmar (i.e. surimi production) should continue to improve its revenue given rising demand from China and improving economies of scale. New boilers have been installed to control energy bills.

Recommendation & Investment Risks

- We maintain our Strong Buy recommendation on Texchem. We have increased our 12-month target price to MYR2.00 from MYR1.60 by raising our target valuation metrics to reflect the potential gains from the imminent spin off of the group's packaging business. We have used a target PER of 15x vs 14x and P/B of 1.0x vs 0.96x, respectively, on our 2006 EPS and BVPS estimates, plus our projected DPS. The revised target metrics are within the historical range for these multiples. As a check, we note that the projected dividend yield of 6.3% is compelling given the recovery in profits to a multi-year high and potential corporate development.

- We maintain our earnings forecast for 2006 and 2007 of MYR19.5 mln and MYR22.5 mln, respectively. The key driver is a turnaround of the surimi production business and the consumer trading business. Our net profit forecast for 2006 will exceed the group's last record profit in 1999. The group is expected to maintain a DPS of 10 sen for 2006 and 2007.

- Risks to our recommendation and target price include lower-than-expected contributions from the food business, higher-than-expected fuel cost, decreasing demand for packaging materials due to more intense competition, and higher than expected interest rates given the group's relatively high borrowings. Also, a delay in the spin off of its packaging business could affect investors' sentiment.

Key Stock Statistics

FY Dec.	2005	2006F
EPS (sen)	15.0	15.7
PER (x)	10.6	10.2
Dividend/Share (sen)	10.0	10.0
NTA/Share (MYR)	0.95	1.00
Book Value/Share (MYR)	1.33	1.39
Issued Capital (mln shares)	124.1	
52-weeks Share Price Range (MYR)	1.04-1.61	
Major Shareholders:	%	
Texchem Holdings	33.0	
Texchem Corporation	17.5	

Per Share Data

FY Dec.	2003	2004	2005	2006F
Book Value (MYR)	1.33	1.28	1.33	1.39
Cash Flow (sen)	17.1	24.0	40.5	39.0
Earnings (sen)	3.7	3.2	15.0	15.7
Dividend (sen)	8.0	8.0	10.0	10.0
Payout Ratio	217.1	247.1	66.5	63.7
PER (x)	43.4	49.4	10.6	10.2
P/Cash Flow (x)	9.3	6.7	4.0	4.1
P/Book Value (x)	1.2	1.2	1.2	1.2
Dividend Yield (%)	5.0	5.0	6.3	6.3
ROE (%)	2.8	2.5	11.5	11.5
Net Gearing (%)	128.3	152.5	139.6	135.4

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Quarterly Performance

FY Dec. / MYR mln	1Q06	1Q05	% Change
Revenue	304.2	294.1	+3.4
Operating Profit (EBIT)	10.6	9.6	+11.1
Depreciation	NA	NA	NM
Net Interest Income / (Expense)	-3.9	-3.7	+5.4
Pre-tax Profit	6.8	4.9	+39.4
Net Profit	4.4	3.0	+48.3
Operating Margin (%)	3.5	3.2	-
Pre-tax Margin (%)	2.3	1.7	-
Net Margin (%)	1.5	1.0	-

Source: Company data

Profit & Loss

FY Dec. / MYR mln	2004	2005	2006F	2007F
Revenue	1,056.8	1,187.8	1,281.0	1,335.3
Operating Profit	23.5	33.8	42.1	45.6
Depreciation	-25.2	-31.5	-28.9	-31.5
Interest Expense	-11.9	-13.5	-13.5	-12.6
Pre-tax Profit	11.0	25.5	29.1	33.6
Effective Tax Rate (%)	66.4	25.4	33.0	33.0
Net Profit	3.9	18.7	19.5	22.5
Operating Margin (%)	2.2	2.8	3.3	3.4
Pre-tax Margin (%)	1.0	2.1	2.3	2.5
Net Margin (%)	0.4	1.6	1.5	1.7

Source: Company data, S&P Equity Research

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Glossary

Strong Buy: Total return is expected to outperform the total return of the KLCI or KL Emas Index respectively, by a wide margin over the coming 12 months, with shares rising in price on an absolute basis.
Buy: Total return is expected to outperform the total return of the KLCI or KL Emas Index respectively, over the coming 12 months, with shares rising in price on an absolute basis.
Hold: Total return is expected to closely approximate the total return of the KLCI or KL Emas Index respectively, over the coming 12 months with shares generally rising in price on an absolute basis.
Sell: Total return is expected to underperform the total return of the KLCI or KL Emas Index respectively, over the coming 12 months and share price is not anticipated to show a gain.
Strong Sell: Total return is expected to underperform the total return of the KLCI or KL Emas Index respectively, over the coming 12 months by a wide margin, with shares falling in price on an absolute basis.

S&P 12 Month Target Price – The S&P equity analyst's projection of the market price a given security will command 12 months hence, based on a combination of intrinsic, relative, and private market valuation metrics.

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