Malaysia

MARKET DATELINE • PP 7767/09/2011(028730)

Corporate Highlights

RHB Research Institute Sdn Bhd
A member of the RHB Banking Group
Company No: 233327 -M

Company Update

19 October 2010

Integrated Logistics

Named Partner In Hong Leong Asia's New Warehouse Project In China

Share Price	:	RM0.93
Fair Value	:	RM1.47
Recom	:	**Outperform** (Maintained)

Table 1 : Investment Statistics (ILB; Code: 5614) — **Bloomberg: ILB MK**

FYE Dec	Turnover (RMm)	Net Profit# (RMm)	EPS# (sen)	Growth (%)	PER (x)	C.EPS* (sen)	P/NTA (x)	P/CF (x)	ROE (%)	Net Gearing (%)	GDY (%)
2009	187.0	(17.7)	(9.0)	nm	nm	-	0.5	3.0	(4.7)	0.3	3.2
2010f	173.2	11.4	5.8	nm	16.0	-	0.5	(2.6)	3.0	0.5	3.2
2011f	138.0	22.3	11.3	95.3	8.2	-	0.5	1.3	5.5	0.2	3.2
2012f	151.5	28.1	14.3	26.0	6.5	-	0.4	9.3	6.6	0.1	3.2

Main Market Listing/Trustee Stock/Syariah-Approved Stock By The SC *#Excluding EI* ** Consensus Based On IBES*

- **Revelation by Hong Leong Asia.** Hong Leong Asia revealed during a recent investors' conference that its refrigeration and cooling products division under Frestech/Xinfei based in Henan, China, has formed a "partnership with Integrated Logistics China to build and operate a central distribution centre".

- **A high-growth blue-chip client.** To ILB, we consider Frestech/Xinfei a high-growth blue-chip client of which ILB can piggy-back on to expand its presence and scale of operation in China. Frestech/Xinfei is the second largest refrigerator and freezer maker in China. Analysts project the market for refrigerators and freezers in China to grow by a CAGR of 9.9% between 2009 and 2013.

- **Frestech/Xinfei warehouse to boost FY12/12 earnings by 20%.** We understand that backed by a 5+5 year long-term lease agreement with Frestech/Xinfei, ILB's US$25m (RM77.5m) investment in the warehouse will have a pay-back period of 8-10 years. Based on our estimate, the first full-year contribution from the warehouse in FY12/12 will boost ILB's FY12/12 net profit by 20%.

- **Forecasts.** We are cutting FY12/10 net profit forecast by 42% largely to reflect: (1) A 3-month delay in the completion of the disposal of its Malaysian assets; and (2) A higher tax. FY12/12 net profit forecast is raised by 20% largely to reflect the first full-year contribution from the new Frestech/Xinfei warehouse.

- **Risks.** These include: (1) A double-dip in the global economy, and hence China's export sector; (2) Prolonged downturn in Dubai; and (3) Rising costs in China, particularly, labour.

- **A China play now, maintain Outperform.** With the disposal of its business in Malaysia, ILB has very much now become a high-growth China-based company listed in Malaysia. Indicative fair value is kept relatively unchanged at RM1.47 based on 13x FY12/11 EPS, at a 30% premium to our benchmark 1-year forward target PER for the transport and logistics sector of 10x to reflect ILB's superior earnings growth visibility with the good execution of its second wave of investment/expansion in China.

Issued Capital (m shares)	197.0
Market Cap(RMm)	183.2
Daily Trading Vol (m shs)	0.2
52wk Price Range (RM)	0.815-1.07
Major Shareholders:	**(%)**
Takahashi & Tee TS	>40
Lembaga Tabung Haji	9.7

FYE Dec	FY09	FY10	FY11
EPS Revision (%)	-42	-	+20
Var to Cons (%)	nm	nm	nm

Share Price Chart

Relative Performance To FBM KLCI

Joshua CY Ng
(603) 92802151
joshuang@rhb.com.my

Please read important disclosures at the end of this report.

Named Partner In Hong Leong Asia's New Warehouse Project In China

- **Revelation by Hong Leong Asia.** We caught the wind of potentially a positive development on ILB, i.e. securing a new warehouse project in the eastern central part of China, backed by a long-term tenancy signed with a multinational, as early as during the early part of this year (see our *Visit Note* on ILB dated 13 Jan 2010). Todate, ILB has yet to make any formal announcement on the subject matter (we suspect due to certain technical issues that are still pending, such as land rights, etc), apart from dropping a small hint in its 2QFY12/10 results announcement by stating that "the lower profitability (in 2QFY12/10 vis-à-vis 1QFY12/10) was mainly attributable to preliminary expenditures incurred pursuant to a new project in Henan, China". On the other hand, the "multinational", i.e. Hong Leong Asia, "stole the thunder" during a recent investors' conference by revealing in its presentation slides *(http://www.hlasia.com.sg/news/HLA_20100708_1.pdf)* that its refrigeration and cooling products division under Frestech/Xinfei based in Henan, China, has formed a "partnership with Integrated Logistics China to build and operate a central distribution centre".

- **A high-growth blue-chip client.** To ILB, we consider Frestech/Xinfei a high-growth blue-chip client of which ILB can piggy-back on to expand its presence and scale of operation in China. Frestech/Xinfei is one of the biggest success stories of ASEAN-based companies in China in recent years. Since the takeover by Hong Leong Group in 1994, Frestech/Xinfei has steadily grown from a virtual unknown player with a production capacity of 300,000 units per annum, to the second largest refrigerator and freezer maker in China (after Haier) with an annual production capacity of 7m units at present (see Charts 1 & 2 for Frestech/Xinfei's market shares for refrigerators and freezers in China in 2009). Analysts project the market for refrigerators and freezers in China to grow by a CAGR of 9.9% between 2009 and 2013, underpinned by the rising disposal income and hence consumerism in China, as well as the narrowing gap between the rural and urban refrigerator ownership in China, estimated at 94 per 100 urban households vis-à-vis 30 per 100 rural households in 2008.

Chart 1: Refrigerator Market Share By Volume In China In 2009*

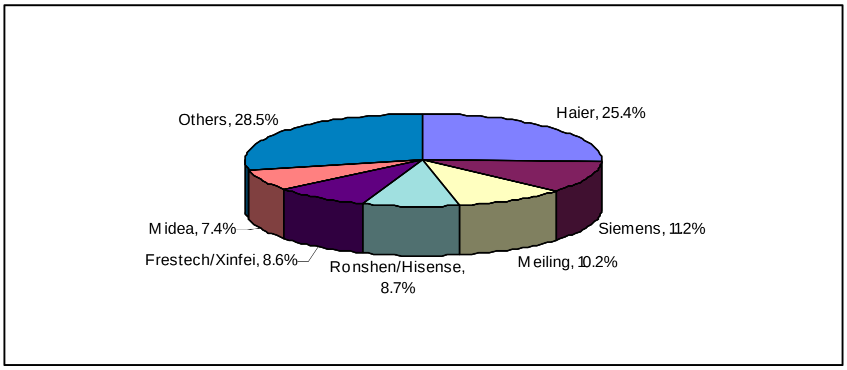
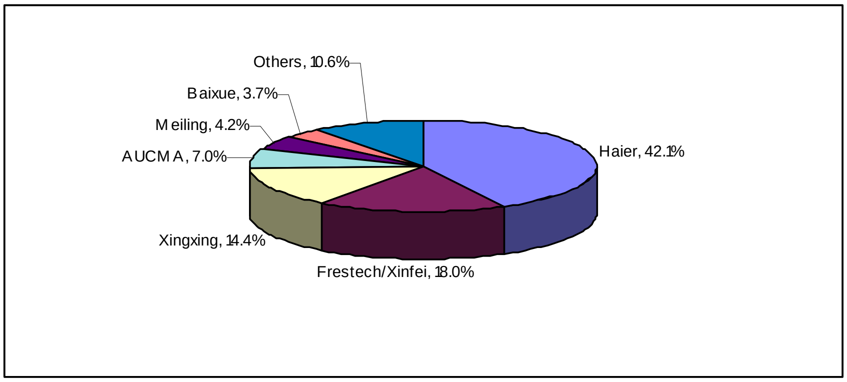


Chart 2: Freezer Market Share By Volume In China In 2009*



**Only Tier-1 and Tier-2 cities*

Source: www.hlasia.com.sg

- **Frestech/Xinfei warehouse to boost FY12/12 earnings by 20%.** The scale of the Frestech/Xinfei warehouse is significant. We understand from independent sources that the warehouse will have a total area of 900k sq ft, that is equivalent to almost two-thirds the size of ILB's flagship warehouse complex in Shenzhen with a total area of 1.4m sq ft (Note that the Shenzhen warehouse complex comprising three warehouses were built over a span of 11 years between 1995 and 2005). According to Hong Leong Asia, the new warehouse (dubbed "central distribution centre") will "streamline distribution and reduce delivery lead time from 60 hours to 24 hours). We also understand from independent sources that backed by a 5+5 year long-term lease agreement with Frestech/Xinfei, ILB's US$25m (RM77.5m) investment in the warehouse will have a pay-back period of 8-10 years. Based on our estimate, the first full-year contribution from the warehouse in FY12/12 will boost ILB's FY12/12 net profit by 20%.

- **Forecasts.** We are cutting FY12/10 net profit forecast by 42% largely to reflect: (1) A 3-month delay (from end-Jun to end-Sep 2010) in the completion of the disposal of its Malaysian assets (the disposal is earnings accretive due to massive interest savings); and (2) A higher tax. FY12/12 net profit forecast is raised by 20% largely to reflect the first full-year contribution from the new Frestech/Xinfei warehouse.

- **Risks.** These include: (1) A double-dip in the global economy, and hence China's export sector; (2) Prolonged downturn in Dubai; and (3) Rising costs in China, particularly, labour.

- **A China play now, maintain Outperform.** With the disposal of its business in Malaysia, ILB has very much now become a high-growth China-based company listed in Malaysia, operating six key warehouses in China of which half are owned (i.e. Shenzhen 2 & 3 and Wujiang 1) and the other half on a sale-and-lease-back basis (i.e. Shenzhen 1 and Shanghai 1 & 2). ILB is also building a new warehouse each in Henan, China (for Frestech/Xinfei of Hong Leong Asia) and Dubai (that is substantially equipped with cold room facilities, i.e. 42,000 out of 67,400 pallet positions, or 62% of total). It is also planning a Phase 2 in Wujiang (Wujiang 2) (see Table 2). ILB also holds a 20.3% stake in Hengyang Petrochemical Logistics Ltd (Bloomberg: HYNG SP) (Hengyang), a tank farm owner/operator in the Yangtze Delta region, listed on the Catalist Board of SGX. At the last traded price of S$0.53, ILB's stake is worth RM37.8m or 19.2sen per ILB share. Indicative fair value is kept relatively unchanged at RM1.47 based on 13x FY12/11 EPS, at a 30% premium to our benchmark 1-year forward target PER for the transport and logistics sector of 10x to reflect ILB's superior earnings growth visibility with the good execution of its second wave of investment/expansion in China.

Table 2: Warehouses Under ILB's Stable

Warehouse	Floor Area ('000 sq ft)	Status	Ownership	Remarks
Shenzhen 1	320	In operation	No^	-
Shenzhen 2	450	In operation	Yes	-
Shenzhen 3	640	In operation	Yes	-
Shanghai 1	180	In operation	No^^	-
Shanghai 2	210	In operation	No^^	-
Wujiang 1	280	In operation	Yes	-
Dubai (Jebel Ali FTZ)	1,300-1,500*	Under construction	50%-owned	Total project cost of RM240m.
Henan (Frestech/Xinfei)#	900#	Under construction	Yes#	Total project cost of US$25m (RM77.5m)#.
Wujiang 2	240	Under planning	Yes	Total project cost of only RMB30-40m (RM15-20m), vis-à-vis RMB110-120m (RM54-59m) of Wujiang 1 as bulk of the basic infrastructure cost has already been put in.

**Effective, with auto-racking system*

^Sale-and-lease-back with Mitsui & Co Ltd, Japan *^^ Sale-and-lease-back with Mapletree, Singapore*

#According to RHBRI's independent sources

Source: RHBRI, company

Table 3: Earnings Forecasts

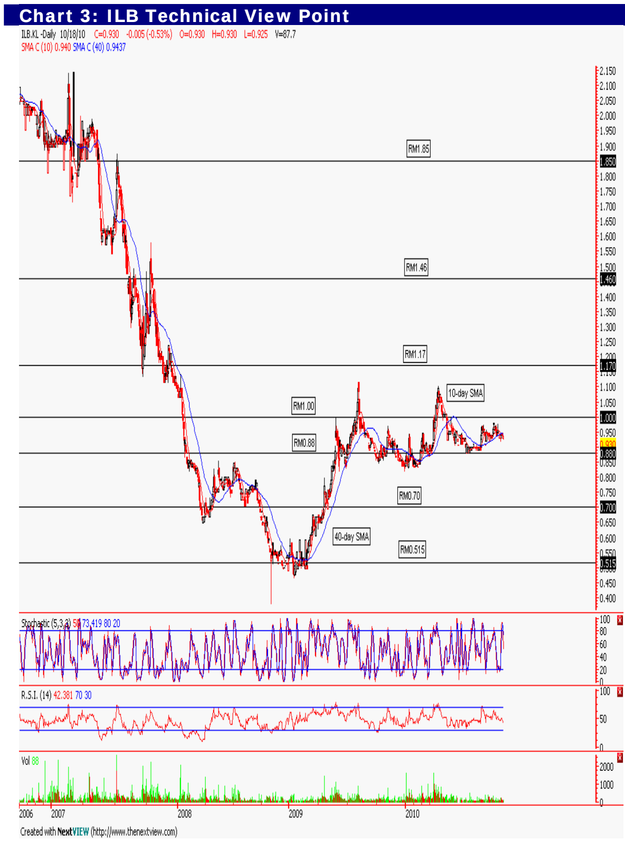
FYE Dec (RMm)	FY09a	FY10F	FY11F	FY12F
Turnover	187.0	173.2	138.0	151.5
Turnover growth (%)	-12.7	-7.4	-20.3	9.8
EBITDA	29.6	34.1	34.2	39.7
EBITDA margin (%)	15.8	19.7	24.8	26.2
Depreciation	-28.4	-13.6	-10.2	-10.2
Net Interest	-6.4	-4.6	0.0	-1.3
Associates	1.9	5.4	6.0	8.0
EI	13.6	0.0	0.0	0.0
Pretax Profit	10.4	21.4	30.0	36.3
Tax	-8.0	-4.0	-0.6	-0.6
PAT	2.5	17.3	29.4	35.7
Minorities	-6.6	-5.9	-7.1	-7.6
Net Profit	-4.1	11.4	22.3	28.1

Source: Company data, RHBRI estimates

Table 4: Forecast Assumptions

FYE Dec	FY10F	FY11F	FY12F
Floor space ('000 sq ft)			
Shenzhen	1,410	1,410	1,410
Shanghai	390	390	390
Wujiang	280	280	280
Henan	-	450	900
Dubai	-	500	1,000

Chart 3: ILB Technical View Point



- ILB plunged to a low of RM0.38 in Oct 2008, before kicking off a sharp technical rebound and stormed towards the RM1.00 resistance level to hit a high of RM1.11 in Aug 2009.
- Though it was dragged lower again from Aug to Oct 2009, it managed to launch a powerful upswing in late Mar 2010, to a high of RM1.10, by forming a base near the RM0.88 support region.
- However, as it failed to overcome the previous high near RM1.11, and registered a fresh high of RM1.10 in Apr 2010, investors rushed in to take profit on fears of a potential bearish "double top" formation.
- As a result, it was pulled back towards the RM0.88 support region, before the recent bounce to close at RM0.93 yesterday.
- Technically, closed with the recent poor readings, the stock is expected to stick within the range of RM0.88 to RM1.00 in the near term.
- Without breaching either of these levels, the technical outlook will stay rangebound in a sideways trend, in our view.
- Further support is at RM0.70, while higher resistance is seen at RM1.17.

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Stock Ratings

Outperform = The stock return is expected to exceed the FBM 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 FBM KLCI benchmark (+/- five percentage points) over the next 6-12 months.

Underperform = The stock return is expected to underperform the FBM KLCI benchmark by more than five percentage points over the next 6-12 months.

Industry/Sector Ratings

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

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

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

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