

27 November 2015 | 3QFY15 Results Review

Ann Joo Resources

Negative margin gets wider

INVESTMENT HIGHLIGHTS

- **9MFY15 net loss widened to RM87.8m due to write down in inventory value, margin erosion and net FX losses**
- **Operating environment remains challenging with China's export of cheap steel products continued to be high affecting steel players' margin**
- **Raise our FY15 net loss forecast higher to -RM134.5m (previously -RM17.2m) as 9MFY15 losses came in wider than expected and were significantly below consensus estimate**
- **Downgrade to SELL from NEUTRAL with a lower TP of RM0.60 pegged to a lower PB multiple of 0.4x on FY16 BVPS.**

Higher loss of RM83.8m in 3QFY1 due to margin decline, net FX loss on USD borrowings and write down of inventory value.

Compared to 2QFY15, the higher loss in 3QFY15 was due to: i) steep decline in selling prices for steel which caused margins to drop and a write down in inventory value of RM51.5m as well as ii) net FX losses of RM6.8m on USD borrowings due to the strengthening of USD against MYR. Sale of steel in terms of tonnage in 3QFY15 was lower than that in the preceding quarter. Cumulatively for 9MFY15, net loss widened to RM87.8m (-383.3%yoy).

Revenue for its Manufacturing and Trading Division declined by -39.5%yoy and -28.5%yoy respectively in 3QFY15 due to steep decline in selling prices of steel. AJR's Manufacturing Division reported a loss of RM68.7m (-458.8%yoy) in 3QFY15. Meanwhile, its Trading Division recorded a loss of RM3.7m in 3QFY15 vs. a profit of RM8.5m in 3QFY14. Both its Manufacturing and Trading Divisions' profits were impacted by drop in steel prices resulting in a write own in inventory value, FX losses and further squeeze on margins.

The Group's inventories declined slightly by -0.2%qoq to RM1.078b. Borrowings was slightly reduced to RM1.37b with USD borrowings of USD27.7m (equivalent: RM121.7m). Net gearing increased to 1.41x as of end 3QFY15 from 1.32x in the preceding quarter due to depletion of shareholders' funds as a result of losses.

Downgrade to SELL (from NEUTRAL)

**Revised Target Price (TP): RM0.60
(Previously RM0.73)**

RETURN STATS	
Price (26 Nov 2015)	RM0.74
Target Price	RM0.60
Expected Share Price Return	-18.9%
Expected Dividend Yield	-
Expected Total Return	-18.9%

STOCK INFO	
KLCI	1,683.09
Bursa / Bloomberg	6556 / AJR MK
Board / Sector	Main / Industrial Products
Syariah Compliant	No
Issued shares (mil)	500.6
Par Value (RM)	1.00
Market cap. (RM'm)	370.4
Price over NA	0.4x
52-wk price Range	0.71 – 1.19
Beta (against KLCI)	0.72
3-mth Avg Daily Vol	0.06m
3-mth Avg Daily Value	RM0.05m
Major Shareholders	
Ann Joo Corp	36.6%
Lim Seng Chee & Sons S/B	13.9%

Steep decline in steel prices with steel bar and billet prices plummeting by 30% and 34% since Jan'15.

China's steel consumption declined by 5.7%yoy to 590.5m mt for 10CY15. The decline in the country's steel consumption was higher than the drop in steel production of -2.2%yoy to 675.1m mt for 10CY15. This continues to cause overcapacity in steel production resulting in the need to export high volumes of China's steel overseas consequently impacting margins of steel players.

Imports of China's steel bars and wire rods into Malaysia remain high. Totals import of steel bars and wire rods from China into Malaysia continued to be high with a growth of +147%yoy and +47%yoy respectively at of end 9MCY15. Malaysia has imposed a 5% import duty on carbon steel bar and wire rod since June 2015. Nevertheless, we understand that there has been a circumvention of the duty with China's mills now exporting more of their steel as alloy steel instead. This has caused to the industry locally to continue to face cheap influx of steel from China with a need by local players to match the prices of China's mills. We gather that some of the Chinese mills which have been suffering losses and facing tighter credits in China have been selling steel at prices below cost.

Challenging operating environment remains. The excess steel production capacity in China is not expected to be resolved quickly. With the devaluation of the Renminbi, exports of steel from China continued to be strong and this has caused steel prices to remain weak.

Downgrade to SELL from NEUTRAL. In view that the sector's earnings continue to be volatile with expected continued decline in the selling prices of steel causing margin deteriorations, we downgrade our call on Ann Joo to SELL from NEUTRAL as we raise our FY15 net loss forecast higher to -RM134.5m (previously -RM17.1m). Selling prices for steel are expected to remain under pressure with imminent further write downs in value of inventory. 

RESULTS SUMMARY

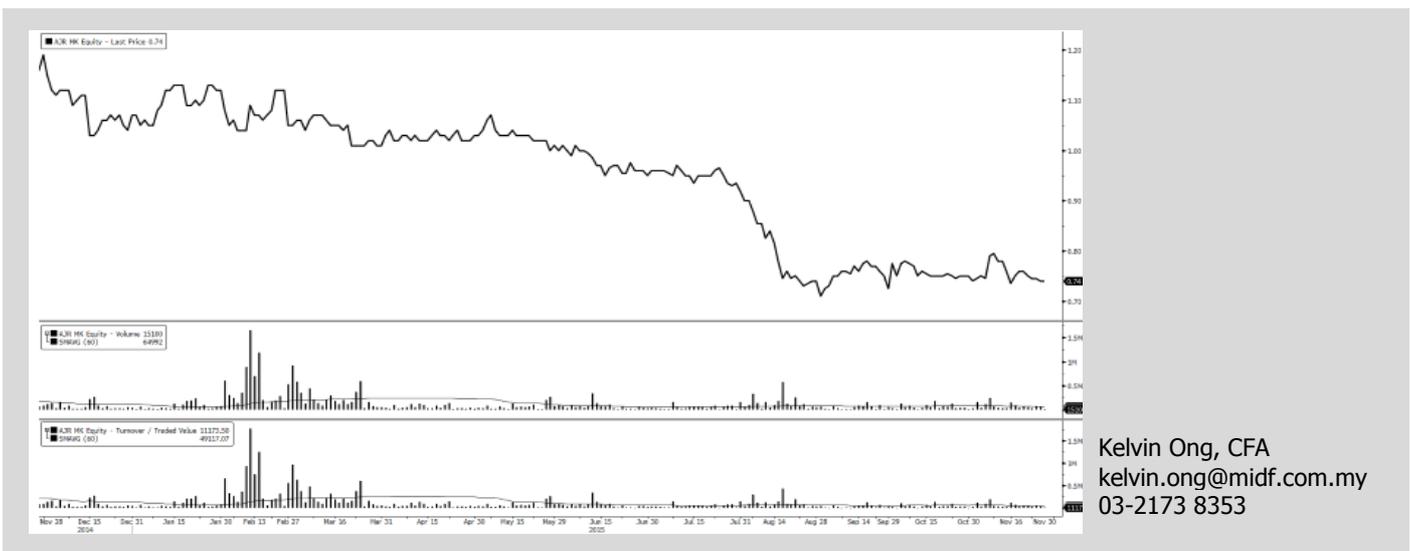
FYE Dec (RM m)	3Q15	2Q15	3Q14	%Qoq	%Yoy	9M15	9M14	%Yoy
Revenue	325.5	501.3	508.5	-35.1	-36.0	1,347.4	1,800.9	-25.2
EBIT	-68.9	-0.9	30.7	>100	-324.5	(47.1)	75.9	-162.1
Pre-tax profit	-83.8	-16.3	16.6	415.3	-604.8	(92.6)	34.4	-369.2
Net Profit	-82.3	-10.8	13.6	659.1	-705.0	(87.8)	31.0	-383.3
				+/- ppts	+/- ppts			
EBIT margin (%)	-21.2%	-0.2%	6.0%	-21.0	-27.2	-3.5%	4.2%	-7.7
Pre-tax margin (%)	-25.7%	-3.2%	3.3%	-22.0	-29.0	-6.9%	1.9%	-8.8
Net margin (%)	-25.3%	-2.2%	2.7%	-23.1	-28.0	-6.5%	1.7%	-8.2

INVESTMENT STATISTICS

FYE Dec	FY13	FY14	FY15F	FY16F
Revenue (RM 'm)	2,155.4	2,291.9	1,797.3	1,745.3
EBIT (RM'm)	62.7	81.3	-123.3	-181.7
Pre-tax Profit (RM'm)	4.48	25.0	-179.3	-237.7
Net Profit (RM'm)	12.3	23.4	-134.5	-178.3
EPS (sen)	2.5	4.7	-25.7	-34.1
EPS growth (%)	+164.1	+88.0	>-100	-32.6
PER(x)	29.6	15.7	n.m	n.m
Net Dividend (sen)	-	2.0	-	-
Net Dividend Yield (%)	-	2.0	-	-

Source: Company, MIDFR Forecast

DAILY PRICE CHART



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MIDF AMANAH INVESTMENT BANK : GUIDE TO RECOMMENDATIONS

STOCK RECOMMENDATIONS

BUY	Total return is expected to be >15% over the next 12 months.
TRADING BUY	Stock price is expected to <i>rise</i> by >15% within 3-months after a Trading Buy rating has been assigned due to positive news flow.
NEUTRAL	Total return is expected to be between -15% and +15% over the next 12 months.
SELL	Total return is expected to be <15% over the next 12 months.
TRADING SELL	Stock price is expected to <i>fall</i> by >15% within 3-months after a Trading Sell rating has been assigned due to negative news flow.

SECTOR RECOMMENDATIONS

POSITIVE	The sector is expected to outperform the overall market over the next 12 months.
NEUTRAL	The sector is to perform in line with the overall market over the next 12 months.
NEGATIVE	The sector is expected to underperform the overall market over the next 12 months.