

Samling Global: Forestry conglomerate

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Recommendation: Not Rated

Forestry

Price	HK\$2.57	Yield (6/06A)	0.03%
12 mth range	HK\$2.08-2.71	ROE (6/06A)	2.5%
Market cap.	US\$30.4m	Net gearing (6/06A)	94.2%
No. shares o/s	4,144.2m	Net debt/sh. (6/06A)	HK\$0.88
Daily t/o, 3 mth	US\$35.4m	BV/sh. (6/06A)	HK\$0.42
Free float %	25.3%	Consensus EPS	
Major shareholder	Samling Strategic – 56%	- 6/07F	na
Ticker	3938.HK/ 3938 HK	- 6/08F	na

Key points:

- Malaysia-based Samling Global is an only sizeable integrated forest resource and wood products company listed on the HKEX.
- Sustainable forest resources support downstream operation.
- Broad and geographically diversified customer base.
- Set to benefit from diminishing tropical hardwood resources globally.

Corporate profile. Based in Malaysia, Samling Global is an integrated forest resource and wood products maker with about 4.0m hectares of forest in Guyana, Malaysia and New Zealand. The company's upstream operations comprise timber harvesting, management of natural forest concessions in Malaysia and Guyana, and tree plantations in New Zealand and Malaysia. Its downstream operations involve the manufacturing and sales of wood products, including logs, plywood, veneer, sawn timber, and value-added products such as fiberboard, door facings and housing products.

History. The group's founder, Datuk Yaw Teck Seng, started his logging business in Sarawak, Malaysia in 1963. In 1976, he established SST, the first company in Samling Global, for log contracting. Between 1976 and 1993, the group expanded its forest concession areas in Sarawak. In 1991, it ventured into Guyana (got a forest concession licence for about 1.6m of hectares in the country's northwest region) and South America. In 1993 and 1996, the company established a plywood and sawmill operation in Guyana. In 1997, it expanded into New Zealand via the acquisition of HHH which operates radiata pine plantations in New Zealand.

Upstream timber operations. Its upstream timber operations comprise the management and operation of natural forest concessions and tree plantations and the extraction of logs for sale to third parties or conversion into downstream wood products. With concessions, the company has the right to harvest logs in natural government-owned forestland.

Production base. As of September 2006, the company had 15 concession areas covering about 1.4m hectares of natural tropical hardwood forest in Malaysia and about 1.6m hectares in Guyana. In Guyana, it also has harvesting rights for another 445,000 gross hectares. The total net operable area within these concession areas is about 908,000 hectares in Malaysia and 1.7m hectares in Guyana, including areas subject to harvesting rights. The group also has maturing tree plantations in New Zealand and is developing tree plantations in Malaysia. As of December 2006, the total gross area of its tree plantations was about 35,000 hectares in New Zealand and 438,000 hectares in Malaysia, of which about 26,000 hectares and 11,000 hectares, respectively, have been planted.

Log sources. The group derived 81.0% of its total annual volume of logs from its natural forest concessions and harvesting rights in Malaysia and Guyana in FY6/06A. The rest came from its tree plantations in New Zealand, helicopter logging in Malaysia and the salvage logs from the clearing of about 11,000 hectares of its tree plantation

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areas.

Annual quota system in Sarawak, Malaysia. The Sarawak Forest Department grants annual harvesting quotas for each of the company's concession license, which represent the maximum volume of logs harvested using ground-based methods with tractors permitted for royalty assessment in any 12-month period beginning 1 July of each year.

Downstream timber operation. The company turns logs into plywood, veneer and sawn timber and processes them into downstream products such as housing products including flooring, doors and furniture. It also converts wood residue from its plywood and sawn timber operations into panel products such as fiberboard and door facings. In addition, it uses some of the wood residue as fuel for electricity production. The supply of logs in its manufacturing plants comes mainly from its own forest concessions.

Other business. The company is also engaged in the manufacturing of rubber retread, property investment and quarrying in Malaysia. Its subsidiary Lingui holds a 36.4% interest in oil palm plantation operator Glenealy, which is listed on the Malaysia Stock Exchange.

Customer base and markets. The company has a broad customer base covering different segments of the distribution chain from general traders to distributors and end-user customers. In FY6/06A, it sold 49.2% of its logs to third parties and 50.8% to its downstream processing facilities. All downstream products are sold to third party customers. Greater China (China, Hong Kong and Taiwan) are its largest log market, accounting for 30.0% of the total logs sales in FY6/06A, while Malaysia accounted for 23.0%, Japan 14.0%, India and Pakistan 18.0% of the total logs sales. In terms of plywood and veneer sales, Japan represented 36.0%, North America 19.0% and Greater China 11.0%.

Strength 1 - sustainable forests resources. The company has a large sustainable forest resource base and holds concessions and harvesting rights covering about 3.5m gross hectares of mainly mixed tropical hardwood forests in Malaysia and Guyana. In addition, it has a license covering about 438,000 hectares to develop hardwood plantations in Malaysia. It also has a maturing radiata pine softwood plantation with a gross area of about 35,000 hectares in New Zealand.

Strength 2 - value enhancement of wood resources. The company's high-grade logs are mainly for export and it maximizes the value of the residue by converting it into plywood, veneer and sawn timber in its own processing facilities. Its capability to produce and sell a wide range of products allows it to maximize the recovery of its wood resources, optimize margins, diversify its revenue base and respond to changes in its customers' needs.

Strength 3 - vertical integration. The company's operations are highly integrated, covering the entire wood product supply chain from harvesting and processing to sales and distribution. As its natural forest concessions in Malaysia and Guyana are contiguous in regions and plywood and veneer operations are located close to its forests, it can manage the infrastructure and logistics efficiently.

Strength 4 – environmentally certificated products. Its certificated wood products allow it to meet the requirements of the growing number of customers who require FSC and MTCC forest management and chain of custody certifications.

Opportunities. The group is set to benefit from diminishing tropical hardwood resources globally and the increase in demand for wood products in the Asia-Pacific region. The declining availability of hardwood logs will continue to drive up log prices. Since 2002, prices of certain log grades have increased by as much as 65.0%.

Risk factors. 1) Malaysian policy requirements related to minimum ownership levels by Samling Strategic, its controlling shareholder, and by Bumiputera in its Malaysian operations, which may limit its ability to raise equity capital; 2) Inability to renew or secure new forest concessions, harvesting rights, plantation licenses and forestry rights upon their expiration or termination; 3) Inability to maintain or renew forest management and chain of custody certifications or to obtain new certifications; 4) Result fluctuations due to revaluation gains or losses on plantation assets; 5) Constrains on its wood flow in Sarawak by royalties and annual quotas established by and annual harvesting plans approved by the Sarawak Forestry Corporation; 6) Weather; 7) Substantial initial capital expenditure not recoverable in the short term because of the 10-30 year plantation development cycle; 8) Illegal logging and resultant price pressure; 9) Competition from non-wood product substitutes.

Track record. Earnings plunged 96.5% YoY to US\$1.5m for FY6/06A, due to a 5.0% YoY decrease in sales as a result of bad weather, 5.1 pcp drop in the gross profit margin and losses from a change in the fair value of plantation assets. Net profit surged more than twelve-fold to US\$46.1m for 1H FY6/07A, thanks to a 58.8% YoY increase in turnover to US\$298.3m and a 17.5 pcp expansion in the gross profit margin. Selected forestry companies are trading at average one year forward P/E of 22.6x and two-year forward P/E of 17.8x.

Table 1: Peer group comparison

Company name	Ticker	Year end	Currency	Market cap (US\$m)	P/E (x) 1-yr forward	P/E (x) 2-yr forward
Ta Ann	TAH MK	Dec	MYR	637.7	13.0	11.4
Jaya Tiasa	JT MK	Apr	MYR	363.5	16.8	21.8
WTK Holdings	WTKH MK	Dec	MYR	397.1	9.7	8.8
West Fraser Timber	WFT CN	Dec	CAD	1,578.9	61.7	19.7
Norbord Inc	NBD CN	Dec	CAD	1,013.7	37.5	26.9
Timberwest Forest	TWF-U CN	Dec	CAD	1,234.0	29.2	26.3
Weyerhaeuser	WY US	Dec	USD	16,313.4	25.7	19.8
International Paper	IP US	Dec	USD	16,302.9	17.3	14.8
Rayonier	RYN US	Dec	USD	3,271.1	21.0	22.4
Potlatch	PCH US	Dec	USD	1,778.0	29.6	22.6
Fletcher Building	FBU NZ	Jun	NZD	3,688.4	13.4	12.9
Gunns	GNS AU	Jun	AUD	864.1	13.1	12.1
Average					22.6	17.8

Source: Bloomberg

P & L (HK\$m)	04A	05A	06A	Cash Flow (HK\$m)	04A	05A	06A
Year to Jun				Year to Jun			
Turnover	364.3	409.1	388.7	EBIT	47.5	62.2	26.5
% chg	-	12.3	(5.0)	Depre./amort.	44.8	44.7	52.9
Gross profit	60.3	69.3	46.9	Net int. paid	9.3	7.6	15.5
				Tax paid	2.0	(8.7)	(7.9)
EBITDA	92.3	106.8	79.4	Dividends received	0.4	0.8	0.7
Depre./amort.	(44.8)	(44.7)	(52.9)	Gross cashflow	104.0	106.4	87.6
EBIT	47.5	62.2	26.5	Chgs. in working cap.	4.9	6.0	12.8
Net int. income/(exp.)	(9.3)	(7.6)	(15.5)	Operating cashflow	109.0	112.4	100.4
Exceptionals	10.4	(14.8)	(15.3)	Capex	(35.3)	(61.7)	(101.5)
Associates	5.5	2.3	1.3	Free cashflow	73.6	50.7	(1.1)
Jointly-controlled entit.	-	2.4	2.8	Dividends paid	(2.5)	(1.3)	(5.0)
Pre-tax profit	54.1	44.6	(0.2)	Net distribution to MI	-	-	-
Tax	(8.8)	(1.3)	1.7	Investments	-	-	-
Minority interests	(21.7)	(20.1)	3.6	Disposals	5.1	59.3	8.3
Net profit	23.5	23.1	5.1	New shares	-	-	-
% chg	-	(1.7)	(77.8)	Others	(364.5)	(102.5)	(69.1)
Dividends	(2.5)	(2.5)	(2.4)	Net cashflow	(288.4)	6.3	(66.9)
Retained earnings	21.0	20.6	2.7	Net (debt)/cash - Beg.	-	(288.4)	(282.1)
EPS (HK\$) - Basic	0.008	0.007	0.002	Net (debt)/cash - End.	(288.4)	(282.1)	(349.0)
EPS (HK\$) - F.D.	0.008	0.007	0.002				
DPS (HK\$)	0.001	0.001	0.001	Interim Results (HK\$m)	05A	06A	
No. sh.s o/s (m) - W.A.	3,094.2	3,094.2	3,094.2	Six months to Dec			
No. sh.s o/s (m) - Y.E.	3,094.2	3,094.2	3,094.2	Turnover	187.8	298.3	
No. sh.s o/s (m) - F.D.	3,094.2	3,094.2	3,094.2	% chg	-	58.8	
				Profit from operations	11.0	80.1	
Margins (%)				Interest expenses	(4.8)	(2.9)	
Gross	16.6	17.0	12.1	Associates	(0.3)	2.1	
EBITDA	25.3	26.1	20.4	Jointly-controlled entit.	1.3	1.1	
EBIT	13.0	15.2	6.8	Pre-tax profit	7.2	80.4	
Pre-tax	14.8	10.9	(0.1)	Tax	(2.2)	(14.7)	
Net	6.5	5.7	1.3	Minority interests	(1.2)	(19.6)	
				Net profit	3.7	46.1	
				% chg	-	1,132.9	
				EPS (HK\$) - Basic	0.001	0.015	
				DPS (HK\$)	-	-	
				Shareholding Structure			
Balance Sheet (HK\$m)	04A	05A	06A		Shares o/s (m)	%	
Year to Jun				Samling Strategic	2,320.4	56.0	
Fixed assets	594.4	630.3	676.9	SIL	203.5	4.9	
Intangible assets	0.6	0.6	0.6	Datuk Yaw Teck Seng	68.4	1.7	
Other LT assets	4.5	3.4	3.7	Wong Lee Ung	1.7	0.0	
Cash	19.7	26.5	21.1	Yong Nyan Siong	2.9	0.1	
Accounts receivable	206.7	218.8	97.3	PDT	207.2	5.0	
Other receivables	-	-	-	Tapah	225.4	5.4	
Inventories	73.4	69.0	83.5	Glory Winner Trading Limited	64.7	1.6	
Due from related co.s	-	-	-	Public	1,050.1	25.3	
Other current assets	8.6	8.5	9.4	Total	4,144.2	100.0	
Total assets	907.9	957.1	892.5	Background			
Accounts payable	(194.8)	(137.6)	(186.3)	Based in Malaysia, Samling Global is an integrated forest resource and wood products maker with about 4.0m hectares of forest in Guyana, Malaysia and New Zealand. The company's upstream operations comprise timber harvesting, management of natural forest concessions in Malaysia and Guyana, and tree plantations in New Zealand and Malaysia. Its downstream operations involve the manufacturing and sales of wood products, including logs, plywood, veneer, sawn timber, and value-added products such as fiberboard, door facings and housing products.			
Other payable	-	-	-				
Tax payable	(9.9)	(2.5)	(1.8)				
Due to related co.s	-	-	-				
ST debts	(122.2)	(146.5)	(144.6)				
Other current liab.	(2.2)	-	-				
LT debts	(185.9)	(162.2)	(225.6)				
Other LT liabilities	(87.1)	(53.4)	(47.9)				
Total liabilities	(602.2)	(502.2)	(606.1)	Key Ratios	04A	05A	06A
Share capital	49.0	50.4	1.0	Net gearing (%)	(94.3)	(74.2)	(94.2)
Reserves	75.5	197.3	166.4	Net ROE (%)	18.9	12.4	2.5
Shareholders' funds	124.5	247.8	167.4	EBIT ROCE (%)	7.7	9.0	3.7
Minority interest	181.3	207.2	118.9	Dividend payout (%)	10.8	10.8	47.8
Total	305.7	455.0	286.3	Effective tax rate (%)	16.3	2.9	876.9
Capital employed	613.8	763.6	656.5	Net interest coverage (x)	5.1	8.2	1.7
Net (debt)/cash	(288.4)	(282.1)	(349.0)	A/R turnover (days)	207.1	189.8	148.4
				A/P turnover (days)	195.2	148.3	152.1
				Stock turnover (days)	88.1	76.5	81.4