Mercury Securities Sdn Bhd

RESULTS – 2Q/FY11

30 Nov 2010

For period Jul-Sep 2010

Panasonic Manufacturing Malaysia		***Market Price:***	*RM18.62*
		Market Capitalisation:	*RM1131.1m*
		Board:	*Main Board*
Stock Code/Name:	*3719 / PANAMY*	***FBM Index:***	*EMAS Shariah/Small Cap*
Recommendation:	*BUY*	***Sector:***	*Consumer Products*

Analyst: *Edmund Tham*

Key Stock Statistics	**2011E**
EPS (sen)	136.8
P/E (x)	13.6
Dividend/Share (sen)	130.0
NTA/Share (RM)	10.59
Book Value/Share (RM)	10.59
Issued Capital (mil shares)	60.7
52- weeks share price (RM)	12.10 – 21.17
Major Shareholders:	%
Panasonic Management (M) SB	47.5
Aberdeen Assets Mgmt Plc	10.6
Employees' Provident Fund	6.0

Per Share Data	**2008**	**2009**	**2010**	**2011E**
Book Value (RM)	9.96	9.92	10.20	10.59
Earnings (sen)	86.6	81.9	106.8	136.8
Dividend (sen)	120.3	105.0	120.0	130.0
Payout Ratio (%)	103.9	96.1	84.3	71.3
PER (x)	21.5	22.7	17.4	13.6
P/Book Value (x)	1.9	1.9	1.8	1.8
Dividend Yield (%)	6.5	5.6	6.4	7.0
ROE (%)	8.7	8.3	10.5	12.9
Net Gearing (cash) (x)	(0.76)	(0.77)	(0.80)	(0.78)

P&L Analysis (RM mil)	**2008**	**2009**	**2010**	**2011E**
Year end: Mar 31				
Revenue	562.5	600.9	679.8	776.9
Operating Profit	58.4	51.9	72.5	97.6
Depreciation	(14.2)	(15.2)	(16.3)	(17.3)
Interest Expenses	0.0	0.0	0.0	0.0
Pre-tax Profit	64.9	60.8	79.3	103.4
Effective Tax Rate (%)	18.9	18.2	18.3	19.6
Net Profit	52.6	49.8	64.8	83.1
Operating Margin (%)	10.4	8.6	10.7	12.6
Pre-tax Margin (%)	11.5	10.1	11.7	13.3
Net Margin (%)	9.4	8.3	9.5	10.7

** RM1.00 par value*

2Q/ 30 Sep	**2Q11**	**2Q10**	**yoy %**	**1Q11**	**qoq%**
Rev (RMm)	202.2	172.8	17.0	205.5	(1.6)
EBIT (RMm)	22.2	13.9	59.6	17.1	29.6
NPAT (RMm)	22.0	15.6	41.1	19.3	14.0
EPS (sen)	36.2	25.7	41.1	31.8	14.0

1H/ 30 Sep	**1H11**	**1H10**	**yoy %**
Rev (RMm)	407.7	328.7	24.0
EBIT (RMm)	39.3	24.8	58.9
NPAT (RMm)	41.3	27.5	50.2
EPS (sen)	68.0	45.3	50.2

PERFORMANCE

Panasonic Manufacturing Malaysia's (PMMA) annualized 1H/FY11 **revenue and net profit after tax (NPAT) both came in on the upper-end of** our earlier estimates. Nevertheless, we note that PMMA usually performs better in its 1H of its financial year.

"Satisfactory 2Q performance"

PMMA's revenue of RM202.2 million for 2Q/FY11 ended 30th September 2010 was an increase of 17.0% as compared with the revenue of RM172.8 million registered in the corresponding 2Q/FY10. The company's combined profit before tax (PBT) of RM28.2 million for 2Q/FY11 had increased by 45.7% y-o-y. The company's combined 2Q/FY10 also included a derivative gain amounting to RM1.96 million.

PMMA registered revenue of RM407.7 million for its 1H/FY11 ended 30th September 2010, an increase of 24.0% y-o-y. This significant increase was mainly contributed by higher sales to the Middle East region and the transfer of manufacture and sales of some models of food processor and juicer from Japan to Malaysia (the full impact to be seen in FY11). PMMA had achieved a higher combined PBT of RM52.8 million for its 1H/FY11, an increase of 54.0% as compared to the PBT in 1H/FY10.

PMMA's 2Q/FY11 revenue of RM202.2 million had decreased slightly by 1.6% compared to the revenue recorded in the preceding 1Q/FY11. However, with a derivative gain of RM1.96 million in the quarter, the company achieved a combined PBT of RM28.2 million, an increase of 14.8% compared to the PBT reported in the preceding quarter.

OUTLOOK/CORP. UPDATES

We are still optimistic on PMMA's earnings outlook for its FY11, despite of economic and debt difficulties in some economies around the word. PMMA's business model, cost structure and profitability have remained resilient.

"Still optimistic on outlook"

In its World Economic Outlook (WEO) report, the International Monetary Fund (IMF) viewed that the global recovery remains fragile, due to imbalances in a number of economies. Global economic activity is forecast to expand by 4.8% in 2010 and 4.2% in 2011. IMF projects that the output of "emerging and developing" economies will expand at rates of 7.1% and 6.4%, respectively in 2010 and 2011. In advanced economies, however, growth is projected at only 2.7% and 2.2%, respectively, with some economies slowing noticeably during the second half of 2010 and the first half of 2011, followed thereafter by a reacceleration of economic activity.

"Economic factors to affect consumer sentiment"

Malaysia had reported a reasonable 3Q/2010 GDP growth of +5.3% while Bank Negara Malaysia (BNM) had continued to maintained its overnight policy rate (OPR) at 2.75%. Malaysia's 3Q/2010 unemployment rate has dropped to 3.2% while its CPI for October 2010 has risen slightly to a still comfortable 2.0%. The continued economic recovery would lead to sustained consumer optimism and hence assist to raise domestic consumption, including spending on retail products such as household electrical and electronic products. This augurs well for PMMA's prospects and outlook.

PMMA will continue to strengthen its collaboration activities with its associated sales companies to boost sales of its products in both the domestic and export markets amidst an increasingly competitive market. Besides this, PMMA also routinely organizes various sales, marketing and A&P (advertising and promotion) activities including sales conventions, road shows and dealers' workshops. PMMA had doubled up its efforts in strengthening frontline capabilities, product competitiveness and customer service infrastructure. PMMA's management also plans to strengthen its competitive edge through continuous productivity and quality improvement initiatives, prudent cash management and cost control measures.

PMMA is committed to improve its earnings growth and manufacturing capabilities under its mid-term plan that focuses on sales expansion of its existing products to the equatorial zone countries and the continued increase of sales derived from the **transfer of some product models to PMMA**, which are currently produced by other manufacturing companies in Japan and China (e.g. food processor and juicer).

"Regional collaborations"

In March 2010, the **Equator Volume Zone project** was launched. This was a collaboration project between Panasonic companies in Asia and Oceania region, the Middle East, Africa and Latin America to spread the horizontal expansion of volume zone products in the equatorial belt zone. PMMA plans to develop and produce regional-based products with emphasis on sales to the Asian/Middle East region.

"Various innovative changes implemented"

PMMA's management has implemented many new innovative changes, including in manufacturing processes, information technology innovations and human resources system. With the application of a flexible manufacturing concept to meet market demand, the company had increased the number of **assembly block cells,** which enable simultaneous production of different product models. This has improved daily production capacity, helped to reduce product model changing time and minimized manpower.

PMMA had implemented a drive to increase the number of suppliers under the **Vendor Managed Inventory programme** whereby the suppliers consigned their goods to PMMA's factory location and shipment consolidation was arranged to designated hubs (across Southeast Asia and East Asia) in order to maximise delivery load per container. This reduced logistic costs and at the same time led to lower inventory levels.

PMMA is currently in the process of implementing a new **Enterprise Resource Planning** (ERP) system by Oracle, which will fully integrate its financial, distribution and manufacturing systems under one single platform. This is a major transformational phase for the company, and when the system is fully implemented, it will improve the overall operational efficiency of the company.

Meanwhile, PMMA's associate company, Panasonic Malaysia SB (PMSB) expects to handle more than 80,000 cubic meters of logistics transactions per month with its new "**Eco-Friendly Integrated Logistics Complex**" that will start operating in December 2010. PMSB's Managing Director, Jeff Lee, said the company currently processed about 60,000 cubic metres of transactions per month. The Integrated Logistics Complex, built on an 8-hectare site, comprises a 300,000-square foot warehouse and a 14,000-square foot administrative and operations office.

"Number 1 in Malaysia for 11 products"

Panasonic brand is ranked as the No.1 brand in Malaysia for 11 products by GfK Group (one of the largest global market research companies). These 11 products are namely rice cooker, blender, vacuum cleaner, flat panel TV, fridge, washing machine, air conditioners, microwave oven, iron, men's shaver and hair dryer). This was based on GfK's retail audit data of Malaysia unit sales from January to December 2009. In June 2010, PMMA also received the GfK Award for No. 1 Market Share in Thailand for its home shower products. During the past year, PMMA had launched 2 new products, namely bidet and dish dryer into the domestic market as well as introduced several new vacuum cleaner, home shower, blender and ceiling fan models with new or enhanced features to the domestic and export markets.

The Panasonic group in Malaysia collectively fulfils its **corporate social responsibility** (CSR) aligned with its late founder's management philosophy of "contributing to society through its business activities". Its CSR efforts include those for the environment (controlling emission levels, exhibition, town clean-up, waste management, marine conservation), human capital (OSH efforts, internships, skills training) and the community (the needy, sports, scholarships, donations for Indonesian earthquake victims). PMMA had won the StarBiz-ICR Malaysia Corporate Responsibility Awards 2009 among the 20 finalists of public listed companies.

VALUATION

After PMMA's strong 1H/FY11 performance, we have tweaked upwards our estimates for PMMA's full-year FY11. We believe this performance would be supported by strong sales both domestically and in export markets. Nevertheless, PMMA will face challenges from the escalating price of some raw materials (such as aluminium sheet, resin, steel roll and copper wire) and also the strengthening of the Ringgit against other major currencies (US Dollar and Yen) of which export sales are denominated in.

"FY11 forecast revised upwards"

For FY10 ended 31st March 2010, a final dividend of 35 sen per share (DPS) and a special dividend of 70 sen per share (both less tax), were paid by PMMA on 13th October 2010. These dividend payouts amounted to a total of RM47.8 million. Meanwhile, PMMA has announced an interim FY11 gross dividend per share of 15 (less tax) to be payable on 25th January 2011. This dividend would be paid out to shareholders with securities transferred into the depositor's securities account before 4pm on 31st December 2010 in respect of transfers and also securities deposited before 12:30pm on 29th December 2010 in respect of securities exempted from mandatory deposit.

"We anticipate higher FY11 DPS"

On a dividend payout ratio basis, PMMA appears to be allowing the payout ratio to drop gradually y-o-y. Nevertheless, we still expect that the amount paid out in Ringgit would be higher y-o-y. We anticipate that PMMA would pay out an even higher gross DPS for its FY11, given its strong cash position and earnings prospects.

"Valuation still attractive"

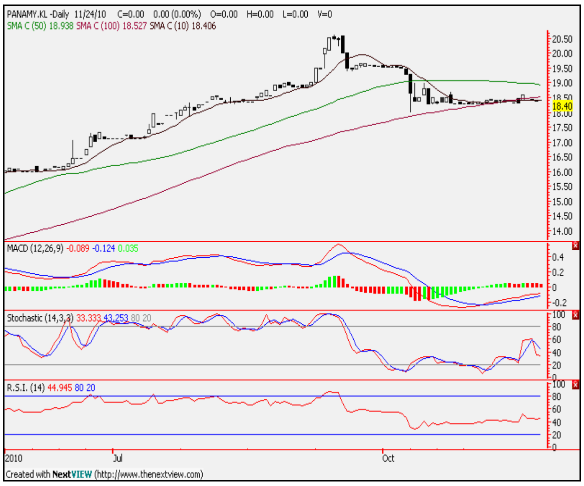
Despite retreating from its year high achieved during September 2010, PMMA still substantially outperformed the KLCI this year (+52.4% vs. +17.2% YTD). This was despite of its relatively weak adjusted beta of 0.42 to the KLCI. Based on our revised forecast of PMMA's FY11 EPS and an estimated P/E of 16 times, we derive a FY11-end (March 2011) **target price (TP) of RM21.89**, which is an upside of 17.6% from its current market price. Despite of its market leadership position, PMMA's P/E is still substantially lower than the domestic durable household product sector's average P/E of 43.0 times.

"Upgrade to Buy Call"

We opine that the fall in PMMA's stock price during the past 1-2 months was not justified. This is given that PMMA's earnings performance remains very strong and it has a very strong balance sheet with zero borrowings and ample cash reserves. We note that Panasonic Corporation's (Panasonic group's global HQ in Japan) latest results announced in October 2010 reflected a positive performance as well. Furthermore, with the fall of PMMA's stock price, we view that there is now substantial stock price upside.

PMMA is a suitable stock for fundamental, long-term investors seeking a reputable, resilient, solid dividend yielding, sizeable market-cap stock with relatively steady earnings growth. As PMMA is a dominant market leader in the domestic household electrical durable goods sector, we continue to view its earnings prospects and outlook very favourably. In the future, the strength of the region's economic and consumer demand growth would continue to guide our view on PMMA's prospects.

Panasonic: 6-month Share Price



Source: NextView