

September 23, 2003

Thai Gypsum Products Plc. (TGP)

NEW : HOLD
PREVIOUS : L-T BUY

BUILDING
Fully valued even after factoring in doubling of production capacity
Price Target
Bt6.35
Bt6.00

We came away from a meeting with the management of Thai Gypsum Products yesterday feeling quite optimistic on the company's growth prospects. The key point is that the management is so confident of the potential growth in demand that they will be making a decision on nearly doubling production capacity within the next several months.

With the recent recovery in demand in both the domestic and regional export markets, TGP's plant is currently operating at full capacity – 24 hours a day, seven days a week. The new line, which will expand capacity at its Laem Chabang plant from the current 35mn sqm to 65-70mn sqm, will come on line in mid-2005. Until then, TGP will need to turn to third party manufacturers to maintain its share in both the local and export markets and ramp up sales for the new plant.

While TGP's prospects look very positive, we believe that the good news is already fully reflected in the company's share price. TGP's shares have gained 50.5% since our last report on August 14. At the current price, TGP is trading on a prospective 03/04 (year-end March) PER of 14.85x and 04/05 PER of 12.62x.

Factoring in the growth potential and the new plant expansion, we believe the fair value for TGP shares should be a 04/05 PER of around 12x, or a share price of Bt6. We want to be clear that TGP shares are still very good for long-term investors. However, since we don't see much further near-term upside potential, we are downgrading our recommendation from LONG-TERM BUY to **HOLD**.

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TGP's income statement (Mn Bt)

	00/01	01/02	02/03	03/04F	04/05F	05/06F
Sales	1,251	1,394	1,738	2,085	2,461	2,830
Cost of goods sold	658	701	954	1,074	1,267	1,457
Depreciation and amortisation	155	129	102	131	146	150
SG&A and others expenses	385	357	419	487	573	657
EBIT	103	220	283	421	495	588
Interest expenses	34	24	17	-	-	-
Net profit before extra items	73	191	262	421	495	588
Extra items	(25)	-	252	-	-	-
Net profit	48	191	514	421	495	588
EPS	0.05	0.19	0.51	0.42	0.50	0.59
EPS Growth	(98%)	298%	169%	(18%)	18%	19%
PER	130.27	32.77	12.16	14.85	12.62	10.62
EV/EBITDA	24.48	17.28	14.38	9.80	8.08	6.12
P/BV	3.46	3.13	2.49	2.13	1.82	1.56
Gearing	0.05	net cash	net cash	net cash	net cash	net cash

Note: COGS does not include Depreciation and Amortisation

TGP's performance this year is being driven by a recovery in the construction markets throughout the region. Currently, approximately 55% of the company's sales are local and 45% exports. We are projecting sales growth this year of 20% to Bt2,085mn, which may be a little ahead of the company's own target but still achievable given its first quarter performance up to June. With the capacity constraints, we are assuming that TGP turns to third party manufacturers later this year. Based on our new assumptions, we have revised up our normalised earnings projections for this year and next year by 22% and 20% to Bt421mn and Bt495mn, respectively.

Revised profit forecasts

	Original		Revision		%Change	
	03/04E	04/05E	03/04E	04/05E	03/04E	04/05E
Sales	2,085	2,398	2,085	2,461	0%	3%
Net profit	346	412	421	495	22%	20%
EPS	0.35	0.41	0.42	0.50	22%	20%

TGP's management said that the growth in the domestic market is largely from ceiling construction for residential units. Even though TGP and its chief rival Lafarge continue to spend money trying to educate local architects and contractors to switch from wet wall construction to gypsum board walls, progress remains quite slow. Gypsum board construction is significantly more expensive than wet wall construction due to higher labour costs. This is the main reason that consumption of gypsum board in Thailand is less than 1 sqm per head, compared to 10 sqm per head in the US.

TGP does not expect to see much benefit from the government's low-income housing project since the major contractors bidding for the project are pushing for modular-type of construction, which can be mass-produced.

AS TGP's first quarter gross margin widened to 43.2% from 32% in previous quarter and 39.4% in previous year. Since British Plaster Board (BPB) took over the company at the end of 1999, the new management has dramatically improved TGP's manufacturing efficiency that made the gross margin up from 15.7% in 1Q00 to 43.2% currently. TGP's gypsum board plant at Laem Chabang is one of the lowest cost plants in the world.

We could see some margin erosion in the near-term, however. Firstly, the strengthening baht against the dollar should erode margins on the company's exports. Secondly, TGP's margins will be very thin on new sales as the company has to turn to outsourcing from third parties. Thirdly, TGP's management is concerned that the German construction material conglomerate, Knauf, may use its Indonesian plant to sell gypsum board cheaply into the Thai market.

Currently, Lafarge (previously Siam Gypsum of the Siam Cement Group) has the biggest share of the local market at an estimated 45-50% with TGP holding 40-45% and 5% imports. Lafarge doesn't face the capacity constraints of TGP with one of its three plants having been temporary mothballed after the Asian economic crisis. Lafarge's capacity estimated at around 90mn sqm is more than double TGP's current capacity.

TGP is determined to maintain its market share and must, therefore, accelerate plans to increase capacity from the current 35mn sqm. The company plans to add an additional 30-35mn sqm capacity by adding an additional line to its current Laem Chabang plant. The expansion will cost around \$45-60mn and take about two years to complete. We assume that the new plant will come on line around mid-2005. TGP can completely finance the expansion through its cash reserves and internally generated cash flow. At the end of June, TGP had a net cash position of Bt833mn and should generate positive cash flow of about Bt521mn this fiscal year and Bt581mn next fiscal year.

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