

MNCs generate best return on equity



by
Doreen Leong

Investors often look at return on equity (ROE) as a measure of how well a company uses investments to generate earnings growth. ROE is used mostly when comparing the performance of companies in the same industry.

The financial ratio measures a company's profitability against the profit it has kept for the business including any capital injections. The "return" is the profit over the last 12 months. Generally, the higher the ROE, the more profit the company is making.

Essentially, the ability of the company's management in generating income from the equity available is often gauged using the ROE. As a general rule, an ROE of 15%-20% is considered good.

Our Focus List ranks the companies with the best ROE based on their latest financial year end. Not surprisingly, multinational companies (MNCs) dominate the list as they are seen as generating steady cash flow with little need to raise capital.

The top ROE companies

Topping our list is Digi.Com Bhd with an impressive ROE of 228.88% in its financial year ended Dec 31, 2018 (FY18). The telecommunications (telco) operator also offered a dividend yield of 4.4% in FY18.

Digi posted a net profit of RM1.54 bil in FY18 while its shareholders' equity was RM673.19 mil. However, the telco operator saw its service revenue decline 3% in its nine months ended Sept 30, 2019 mainly due to 25.8% fall in non-internet prepaid revenue (on the back of falling legacy revenue) but largely cushioned by an 8.5% growth in postpaid and non-internet prepaid revenue. This means Digi saw improved mix of internet and digital revenue further from 55% to 63% of service revenue.

According to TA Securities, Digi's strategic shift in revenue mix was supported by ongoing efforts to redefine its customer value proposition which has seen enhancements to network experience supplemented by value offerings like easy device ownership (PhoneFreedom 365), borderless and family plans, affordable internet passes, as well as personalised rewards and convenience via the MyDigi app to promote subscriber retention.

The research house points out that Digi has been taking a phased approach in expanding its fibre to the home (FTTH) services.

"They also see the expansion



Digi has an impressive ROE of 229% in its FY18



Eng says good ROEs on companies are a potential indicator on positive long-term returns

of FTTH services to help offload data and voice from the mobile network when customers are connected to WiFi, and this in turn would also help improve the network experience for all customers.

"And like peers, the group has been working on offering customers bundled propositions, namely with the bundling of postpaid and fixed broadband services."

However, TA Securities made no changes to its earnings forecasts.



Loke says MNCs are well liked because many have fixed dividend policy

"We reiterate our sell recommendation on Digi with an unchanged target price of RM4.25 per share based on a WACC (weighted average cost of capital) of 7.5% and long-term growth rate of 1%. We opine that the stock is fairly valued at current levels, trading at an EV/Ebitda of 13.8 times CY20 Ebitda which is in line with the stock's five-year mean.

In addition, the research house opines that Digi's FY19/FY20/FY21 forward dividend yields of 4%/4.2%/4.3% are not

attractive enough to warrant an entry considering the downside risk of continued challenges from its prepaid segment.

Carlsberg Brewery

Next on the list is Carlsberg Brewery Malaysia Bhd with an ROE of 158.43%. The brewer posted a net profit of RM286.76 mil in the financial year ended Dec 31, 2018 with shareholders' equity of RM181 mil. The counter has a dividend yield of 6.5% in FY18.

Carlsberg's nine months results ended Sept 30, 2019 core net profit grew by 6.4% yoy to RM222.6 mil due to higher organic sales across mainstream and premium brands from its operations in both Malaysia (+12.4% yoy) and Singapore (+6.7% yoy).

According to Affin Hwang Capital, this was partially offset by a dip in Ebit margins (-1.2 percentage points yoy) on the back of higher commercial-related spending as well as an increase in raw material costs. It points out that earnings contribution from its Lion Brewery associate remained robust (9M19: RM14.7 mil), despite higher beer duties (+12.5%) imposed in Sri Lanka from March, followed by bombing attacks which occurred

in April. A higher dividend per share of 17 sen was announced for the quarter.

The research house maintains its earnings estimates and a hold call on the stock, with an unchanged target price of RM28.50.

Dutch Lady

Taking the third spot is Dutch Lady Milk Industries Bhd with an ROE of 122.75%. It registered a net profit of RM129.45 mil in the financial year ended Dec 31, 2018 while its shareholders' equity was RM105.46 mil. For the third quarter ended Sept 30, 2019, it saw a decline in net profit to RM25.2 mil from RM34.21 mil a year ago despite posting higher revenue of RM278.31 mil versus RM257.05 mil previously.

Despite the lower net profit, the company declared an interim dividend of 50 sen per share amounting to RM32 mil in respect of the financial year ended Dec 31, 2019.

The company says the market remains volatile and is subject to various domestic and global uncertainties, foreign exchange rate and potential regulatory changes.

"However, the company continues to focus on growth increasing the consumption of milk among

continues on page 48

Top 50 Best ROE for FY18

#	COMPANY	REVENUE FY18 (RM'000)	NET PROFIT FY18 (RM'000)	TOTAL ASSETS FY18 (RM'000)	SHAREHOLDERS' EQUITY FY18 (RM'000)	ROE FY18 (%)	ROA FY18 (%)	EPS (SEN)	P/E FY18	ENTERPRISE VALUE FY18 (RM'000)	DIVIDEND YIELD FY18 (%)	PRICE NOV19 (SEN)	MARKET CAP NOV19 (RM'000)
1	Digi.Com	6,527,111	1,540,788	6,206,056	673,188	228.88	24.83	19.80	22.73	37,250,000	4.40	4.63	36,000,000
2	Carlsberg Brewery Malaysia	1,982,342	286,757	682,523	180,997	158.43	42.01	90.65	21.71	6,040,000	6.50	28.10	8,640,000
3	Dutch Lady Milk Industries	1,048,568	129,449	404,802	105,459	122.75	31.98	202.30	30.65	3,950,000	1.61	57.72	3,690,000
4	Astro Malaysia Holdings	5,530,753	763,976	6,847,947	653,329	116.94	11.16	15.00	17.33	16,560,000	4.60	1.41	7,350,000
5	British American Tobacco (Malaysia)	2,822,946	468,531	1,101,106	421,667	111.11	42.55	164.10	21.99	10,630,000	4.19	16.40	4,680,000
6	Nestlé (Malaysia)	5,519,045	658,882	2,847,282	654,333	100.70	23.14	281.00	52.46	39,810,000	1.90	144.20	33,810,000
7	Heineken Malaysia	2,029,672	282,520	940,323	371,147	76.12	30.04	93.50	21.88	6,270,000	4.60	26.12	7,890,000
8	Malaysian Bulk Carriers	238,974	263,952	1,022,740	394,177	66.96	25.81	26.38	2.12	681,120	0.00	0.62	620,000
9	7-Eleven Malaysia	2,217,049	51,330	749,367	92,478	55.51	6.85	4.57	32.82	1,790,000	1.60	1.42	1,630,000
10	Ucrest	48,263	14,846	41,977	32,027	46.35	35.37	4.02	5.48	91,240	0.00	0.16	74,250
11	Uchi Technologies	139,967	69,009	219,000	150,825	45.75	31.51	15.41	16.48	1,030,000	2.76	2.81	1,260,000
12	Elsoft Research	78,150	39,766	129,547	112,930	35.21	30.70	6.00	18.17	652,270	8.53	0.92	613,990
13	E.A. Technique (M)	419,000	74,233	883,664	237,666	31.23	8.40	14.73	2.65	582,500	0.00	0.39	196,560
14	Ideal United Bintang International	677,694	109,851	647,103	359,595	30.55	16.98	47.55	2.37	232,350	0.00	1.38	639,940
15	Scicom (MSC)	165,289	31,916	117,018	104,638	30.50	27.27	9.06	21.96	653,660	4.70	1.03	366,120
16	Berjaya Sports Toto	5,660,587	237,944	2,631,057	786,397	30.26	9.04	17.05	12.32	3,620,000	7.62	2.56	3,450,000
17	Dufu Technology Corp	241,451	51,826	220,193	174,481	29.70	23.54	20.64	9.98	472,870	3.40	2.86	733,040
18	Wellcall Holdings	171,124	31,649	130,581	107,485	29.45	24.24	6.36	20.28	605,090	3.14	1.17	582,070
19	Syarikat Takaful Malaysia Keluarga	2,639,065	292,617	8,931,576	1,012,158	28.91	3.28	35.79	10.62	2,150,000	4.00	6.05	5,000,000
20	Bermaz Auto	1,992,868	150,963	851,739	524,504	28.78	17.72	12.12	18.32	2,350,000	3.83	2.21	2,570,000
21	Dutaland	16,352	384,799	1,405,241	1,349,994	28.50	27.38	45.60	--	-175,500	10.20	0.41	351,140
22	Guan Chong	2,273,424	190,115	1,784,150	667,140	28.50	10.66	39.78	6.91	1,870,000	0.73	2.59	2,610,000
23	Lingkar Trans Kota Holdings	523,897	228,554	2,260,183	822,917	27.77	10.11	43.34	13.13	3,530,000	4.39	4.50	2,390,000
24	AirAsia Group	10,638,296	1,695,394	18,549,771	6,185,265	27.41	9.14	58.90	5.04	6,200,000	4.04	1.86	6,220,000
25	Padini Holdings	1,678,790	178,174	924,000	653,200	27.28	19.28	27.08	22.05	3,510,000	1.68	3.50	2,300,000
26	Hup Seng Industries	307,373	42,959	236,464	158,270	27.14	18.17	5.37	17.69	663,680	6.32	0.90	724,000
27	GDB Holdings	274,559	27,890	212,751	104,121	26.79	13.11	4.68	4.91	60,420	8.70	0.50	312,500
28	George Kent (Malaysia)	616,994	124,402	951,503	475,783	26.15	13.07	22.09	17.29	1,690,000	2.50	1.03	554,310
29	ViTrox Corporation	394,684	105,484	576,105	413,505	25.51	18.31	22.43	28.04	2,870,000	0.48	7.84	3,690,000
30	Hong Leong Industries	2,488,246	402,362	2,013,504	1,584,772	25.39	19.98	107.77	10.54	2,990,000	3.26	10.02	3,200,000
31	Datasonic Group	258,601	67,121	445,436	266,677	25.17	15.07	4.98	17.67	1,310,000	2.27	1.04	1,400,000
32	Amway (Malaysia) Holdings	972,272	54,510	403,141	216,604	25.17	13.52	33.16	18.09	809,600	3.33	5.95	978,090
33	Maxis	9,192,436	1,779,719	19,806,561	7,149,731	24.89	8.99	22.80	23.46	48,900,000	3.70	5.34	41,760,000
34	Sunway Construction Group	2,256,835	145,020	1,754,468	592,518	24.48	8.27	11.20	11.88	1,350,000	2.63	1.98	2,550,000
35	Inari Amertron	1,376,042	260,130	1,331,775	1,070,817	24.29	19.53	8.08	27.97	6,600,000	2.83	1.95	6,210,000
36	Fintec Global	30,888	43,365	202,314	183,733	23.60	21.43	9.83	1.07	-81,010	0.00	0.08	50,890
37	Econpile Holdings	728,399	87,101	651,548	369,652	23.56	13.37	6.50	11.38	1,030,000	1.35	0.81	1,080,000
38	Globetronics Technology	327,956	70,117	376,069	301,145	23.28	18.64	10.50	16.67	1,070,000	4.91	2.10	1,410,000
39	Edaran	150,285	6,936	83,658	30,283	22.90	8.29	12.44	16.97	-1,450	0.00	0.43	24,610
40	Hap Seng Consolidated	6,246,519	1,186,862	5,510,052	5,199,193	22.83	21.54	46.01	21.41	29,480,000	3.55	9.95	24,770,000
41	SKP Resources	2,094,997	126,670	905,834	556,971	22.74	13.98	10.32	15.31	1,800,000	3.21	1.23	1,540,000
42	Hai-O Enterprise	461,696	72,521	395,999	318,923	22.74	18.31	24.88	19.94	1,380,000	2.22	2.20	638,720
43	ATA IMS	2,308,458	92,527	1,089,660	418,653	22.10	8.49	8.82	18.14	1,840,000	0.00	1.74	2,100,000
44	Westports Holdings	1,614,694	533,474	5,087,420	2,415,086	22.09	10.49	15.64	23.15	13,700,000	3.24	4.30	14,660,000
45	Hartalega Holdings	2,405,638	439,632	2,631,979	1,997,391	22.01	16.70	13.28	45.56	20,200,000	1.93	5.37	18,110,000
46	Rexit	21,835	7,857	39,053	36,053	21.79	20.12	4.00	16.13	84,480	4.65	0.70	123,200
47	Southern Steel	3,698,191	211,245	2,489,084	972,087	21.73	8.49	48.78	3.20	1,830,000	2.24	0.73	314,390
48	MB World Group	287,006	51,057	655,939	235,161	21.71	7.78	32.44	5.54	349,310	5.81	1.54	242,360
49	Hibiscus Petroleum	394,344	203,712	1,973,965	995,790	20.46	10.32	13.19	6.71	1,280,000	0.00	0.93	1,470,000
50	VisDynamics Holdings	41,394	8,169	54,095	40,708	20.07	15.10	4.91	10.59	79,120	0.00	0.41	69,360

SOURCES: BURSA, BLOOMBERG | RESEARCHED BY MATHENNY K

from page 48

consumers," Dutch Lady says.

Meanwhile, Astro Malaysia Holdings Bhd and British American Tobacco (Malaysia) Bhd took the fourth and fifth position respectively. Astro generated an ROE of 116.94% while BAT 111.11%.

Not the best benchmark

In reality, assessing the value of a company based on its ROE may not be the best method.

"ROE is looking at the specific historical base of a company, hence may not be the best benchmark across companies,

especially public companies where the shares are publicly traded with market price that can be better measured with dividend yield, which is the 'real return' into the hands of investors," says Baker Tilly Malaysia managing partner, audit & assurance Datuk Lock Peng Kuan.

"ROE differs from company to company as some companies, especially MNCs with steady cash flows, hardly see any capital call or transactions, as their international holding company is usually not pumping in more capital after the initial outlays - more

so they are calling for dividends from these investments. Hence, the equity based of these companies might not differ much from year on year, and ROE could be deemed as a historical comparison based on their initial equity base," he tells **FocusM**.

Lock adds that MNCs are well liked because many have fixed dividend policy where a big chunk of their profits is allocated for dividends.

"The MNCs don't need to preserve capital for expansion and usually dividend yields are also high. At least the dividend

yield is more reflective as it takes into account the current share price," Lock adds.

Meanwhile, Etiqa Insurance and Takaful chief strategy officer Chris Eng says good ROEs on companies such as Dutch Lady and Digi are a potential indicator on positive long-term returns.

However, he adds that ROE should not be used as the sole indicator of the potential returns on companies.

"In cases where the regulatory environment mandates a higher level of capital, ROEs may be dampened not because

the return is low but because the equity is high.

"In some cases, a high ROE may indicate a mature operating environment where growth opportunities are limited and thus companies have returned significant profits to shareholders in the form of dividends.

"So high ROEs are a good sign but should not be the sole characteristic when evaluating companies. ROE combined with CAGR (compound annual growth rate) and PER (price to earnings ratio) make for better combination," he explains. **FocusM**