APEX SECURITIES BERHAD



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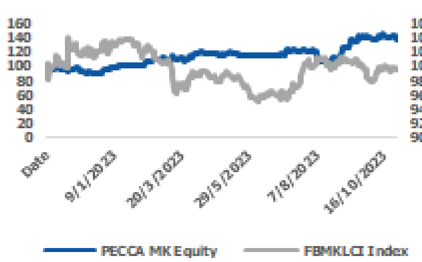
| | | |
|---|---|---|
| **Recommendation:** | | **Not Rated** |
| **Current Price:** | | **RM 1.20** |
| **Previous Target Price:** | | **-** |
| **Target Price:** | ↑ | **RM 1.37** |
| **Upside/Downside:** | | **14.2%** |

| **Stock information** | |
|---|---|
| Board | MAIN |
| Sector | Auto Parts |
| Bursa / Bloomberg Code | 5271 / PECCA MK |
| Syariah Compliant | Yes |
| FTSE4Good Index | Yes |
| FTSE ESG Rating | ☆☆☆★★ |
| Bloomberg ESG Rating | N/A |
| Shares issued (m) | 751.8 |
| Market Cap (RM' m) | 902.1 |
| 52-Week Price Range (RM) | 0.775-1.25 |
| Beta (x) | 0.6 |
| Free float (%) | 25.9 |
| 3M Average Volume (m) | 5.4 |
| 3M Average Value (RM' m) | 6.0 |

| **Top 3 Shareholders** | **(%)** |
|---|---|
| MRZ LEATHER HOLDINGS SDN BHD | 49.6 |
| Sam Yin Thing | 6.9 |
| HUAREN HOLDINGS | 4.6 |

**Share Price Performance**




| | 1M | 3M | 12M |
|---|---|---|---|
| Absolute (%) | -1.6 | 15.4 | 36.4 |
| Relative (%) | -2.4 | 16.7 | 37.4 |

# Pecca Group Berhad

## Promising Growth Opportunities on the Horizon

## Summary


- **Involved in styling, manufacturing, distribution and installation of upholstery seat covers as well as the supply of leather cut pieces for automotive upholstery industry.**
- **Core earnings expected to improve, buoy by strong demand from OEM customers and expansion in margins facilitated by the upskilling of newly recruited workers post-lockdown.**
- **Pecca Group is valued by pegging its FY24F core EPS of 5.6 sen to PE of 24.5x, leading to a FV of RM1.37 (14.2% potential upside from current price).**


## Company Background

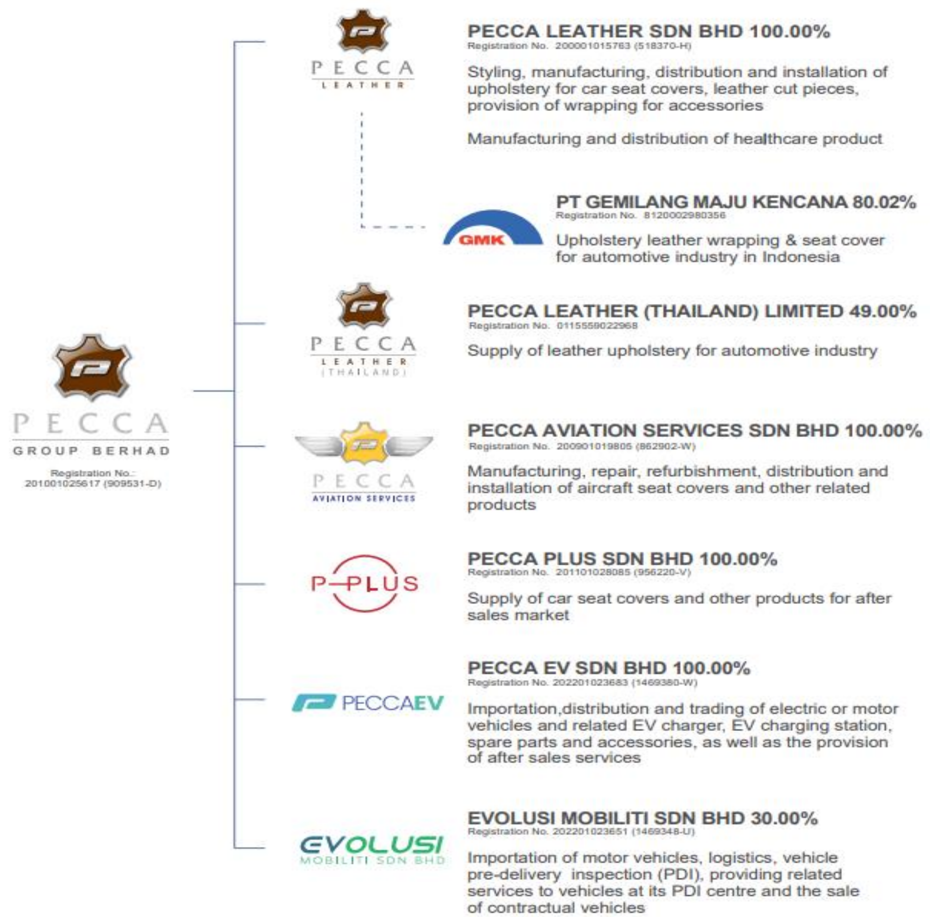
- Pecca Group Berhad was incorporated as a private limited company in Malaysia under the name of Pecca Malaysia Sdn Bhd on 27 July 2010 and subsequently changed its name to Pecca Group Sdn Bhd on 28 April 2014. The company eventually listed as Pecca Group Bhd on 19 April 2016.

- Pecca's subsidiaries, Pecca Leather Sdn Bhd (PLeather) and Pecca Leather (Thailand) Limited involved in the styling, manufacturing, distribution and installation of upholstery seat covers as well as the supply of leather cut pieces for the automotive upholstery industry. Both subsidiaries boast an extensive client list locally as well as exporting their products to the overseas market such as the USA, Netherlands, Thailand, Australia, Japan, New Zealand, Singapore, Indonesia and United Kingdom. In 2023, PLeather acquired PT Gemilang Maju Kencana (GMK) to establish their foothold into the Indonesia market. GMK specialises in providing upholstery leather wrapping and seat covers to the Indonesian automotive industry through its extensive partnership with major brands such as Toyota, Daihatsu, Honda, Isuzu and etc.

- Besides that, Pecca also involve in manufacturing, repair, refurbishment, distribution and installation of aircraft seat covers, parts refurbishment and other aircraft interior related products through its subsidiary, Pecca Aviation Services Sdn Bhd (PAviation). The group has managed to obtained certification from the European Union Aviation Safety Agency (EASA) in April 2023, enabling it to extend its services to a broader market.

- During the early stage of the Covid-19 pandemic, Pecca started to venture into the Personal Protective Equipment (PPE) business which includes the development, manufacturing and supplying of face masks, face shields, and PPE garments (jumpsuit, gown, head & foot cover). The group has since invested in machineries and cleanroom facilities to produce high quality PPE products.

## Corporate Structure



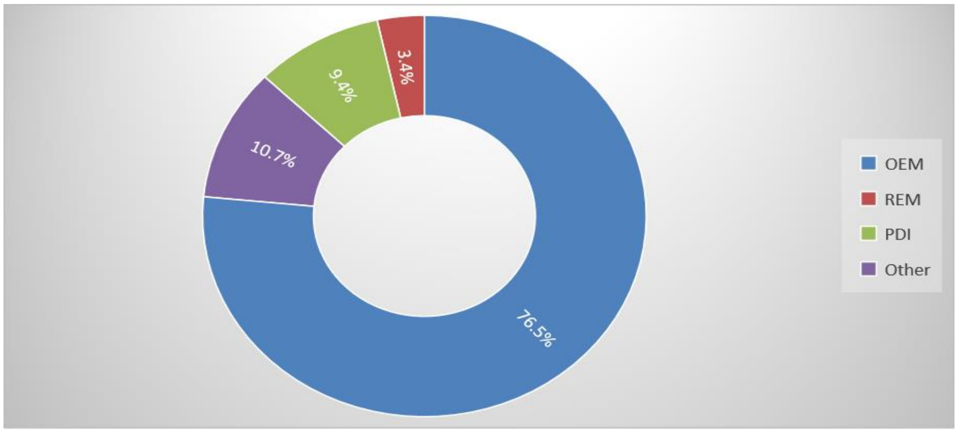

*Source: Company*

## Business Overview

- In FY23, the automotive segment remains as the dominant source of revenue, which amounted to 98.2% of the total revenue. Further breakdown of this segment reveals that the Original Equipment Manufacturer (OEM) category played a pivotal role, contributing 75.2% to total revenue. Meanwhile, both the Replacement Equipment Manufacturer (REM) and Pre-delivery Inspection (PDI) accounts for 3.4% and 9.2% of total revenue, respectively.

- In addition, Pecca also offers services like leather cut pieces, sewing of fabric car seat covers, manufacturing of leather/PVC car seat covers, miscellaneous car interior accessories, as well as wrapping and stitching services. The aforementioned segment accounted for 10.7% of total revenue.

**Automotive segment revenue breakdown**




*Source: Company, Apex Securities*

- Pecca offers a diverse selection of products designed to meet the needs of different customer groups. Under OE Fit product line, Pecca manufactures leather seat covers according to customer specifications, including design, seat profile, and material combinations. Subsequently, the end product is supplied to Tier 1 car manufacturers whom then install the leather car seat covers onto the bare uncovered seats.

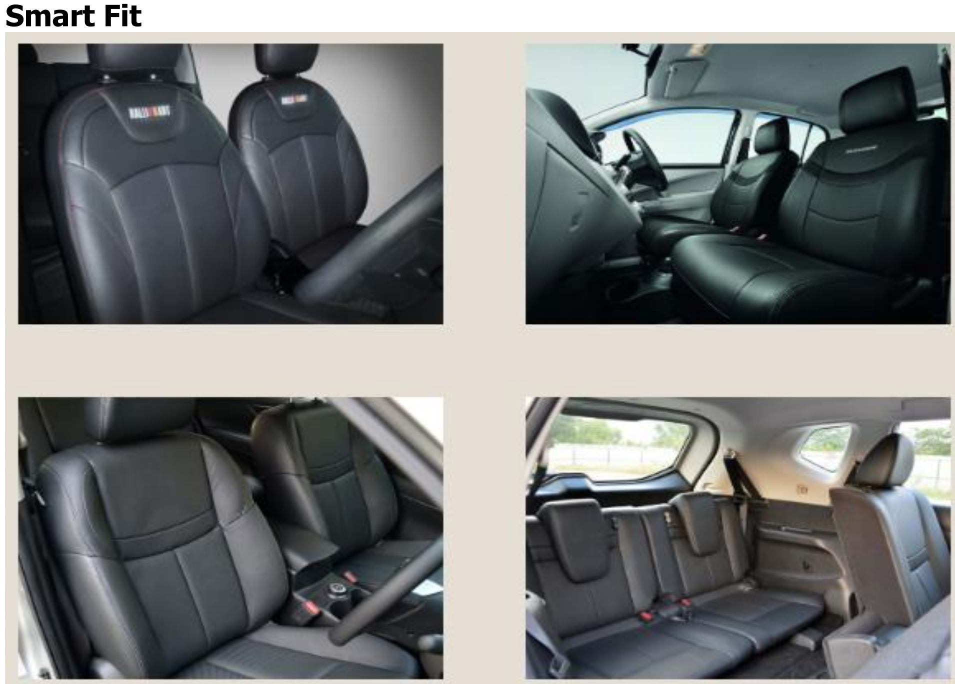
- Meanwhile, Smart Fit seat covers are created with a focus on the PDI market segment. These seat covers are retrofitted to offer flexibility and can be directly installed on car seat that is already equipped with the original fabric. The primary benefit of Smart Fit lies within the ability to provide precise fitting tailored to specific car models, while many leather seat covers in the market tend to be loosely fitted based on standardised sizes. Additionally, installing a Smart Fit leather car seat cover does not require the seat to be disassemble, in contrast to the traditional approach. Hence, installation process is deemed more efficient, requiring less manpower and time.

- Quick Fit seat covers share many similarities with Smart Fit seat covers, but the primary differentiation lies in its exclusive use of PVC material in their standard design. This allows Quick Fit car seat covers to meet the cost-conscious preferences of the broader consumer market as compared to leather car seat covers. Quick Fit car seat covers are accessible to end users through car accessory and retail stores.

## Leather Car Seat Cover

### OE Fit

### Smart Fit



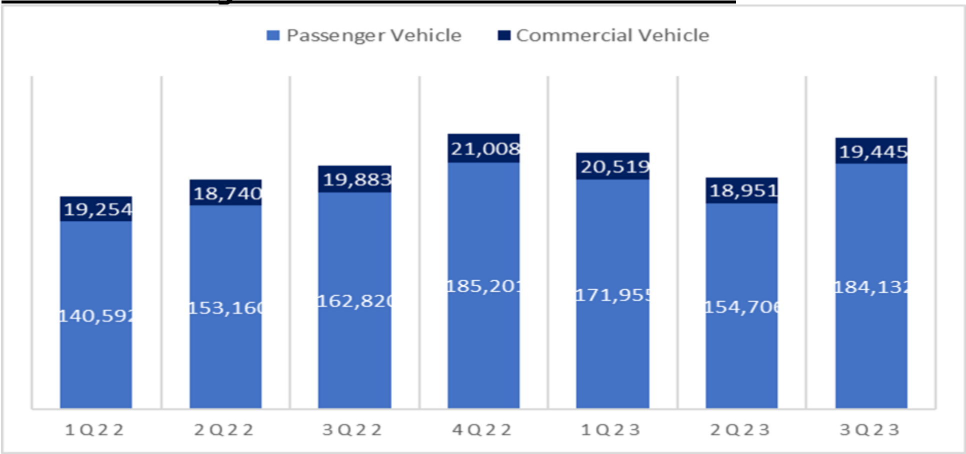
*Source: Company*

## Industry Overview

- We gather that total Industry Volume (TIV) in 3Q23 rose +17.2% QoQ primarily fuelled by robust sales in the passenger vehicles segment, which witnessed a growth of +19.0% for the quarter. This surge in passenger vehicle sales can be attributed to a strong demand observed in August 2023 (+12.7% MoM), driven by improvements in supply chain and national day promotion offered by popular brands. Nonetheless, we noticed signs of slowdown in September 2023 (-5.0% MoM), as consumers exhibited caution in spending ahead of the tabling of Budget 2024.

- Looking forward, we maintain our view that the Total Industry Volume (TIV) will remain robust for 2023, driven by the continuous fulfilment of backlog orders and new model releases. The Malaysian Automotive Association (MAA) has also expressed optimism regarding the automotive sector by revising its full-year 2023 TIV projection from 650,000 units to 725,000 units, which reflects a potential increase of +11.5% YoY. However, we anticipate a slight deceleration in TIV growth for 2024 after a bumper year in 2023, taking into account onto withdrawal of sales tax exemption as well as slower replenishment rate.

**TIV for Passenger vehicle and Commercial vehicle**



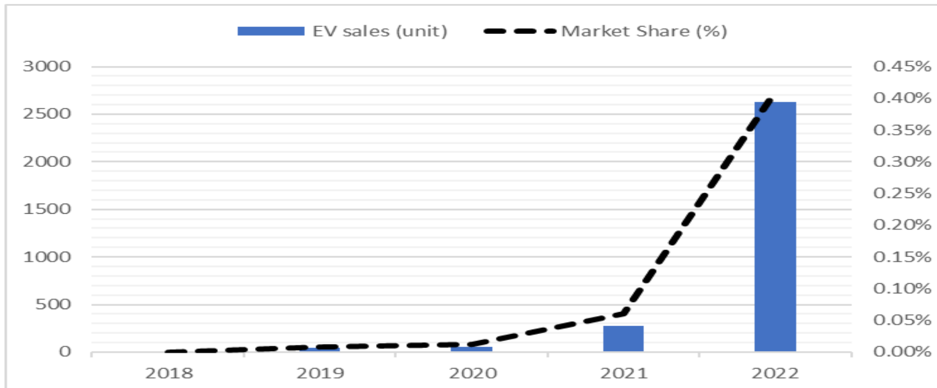

*Source: MAA, Apex Securities*

- Nevertheless, our long-term outlook for the automotive sector remains optimistic, primarily due to government's emphasis and dedication in transitioning to clean energy, as highlighted under Budget 2024. This commitment is evident through several initiatives, such as individual income tax relief for EV charging facilities and incorporating EVs as official vehicles for the federal administration.

- Although no groundbreaking incentives were introduced for the EV sector from the Budget announcement, we do hold the view that the government is moving in the right direction by progressively enhancing the ecosystem. This approach is essential, considering Malaysia's EV charging infrastructures at present are not be prepared to accommodate a sudden surge in EVs on the roads.

- While EV market share in Malaysia stood at a modest 0.4% of total passenger vehicle sales in 2022, we, however anticipated growth prospects is largely on the horizon. The government's aim to achieve 125,000 EVs on the road by 2030 is poised to drive expansion in the market in the years to come. Evidently, we have observed rising number of domestic and foreign companies are taking a slice of the EV supply chain over the past few years, contributing to various elements including battery manufacturing, charging station infrastructure, and other EV components.

**EV sales and market share**




*Source: MAA, Apex Securities*

## Investment Highlights

- **Production capacity to expand twofold.** Pecca intends to double their plant capacity from 240,000 units to 480,000 units to keep pace with the growing demand. Upon completion of the expansion, the group aims to achieve a combined utilisation rate of 80% (current utilisation rate at 85%). That said, the incremental earnings are anticipated to materialise only in FY26, given that the new capacity is scheduled to commence operations in mid-2025. Still, we are optimistic on this expansion, forecasting a substantial contribution (circa RM6.1m) to the bottom line.

- **Penetrating into the Indonesia market.** Pecca has finalised the purchase of GMK at a cost of RM1.9m, fully funded internally through the internal cash reserves. The acquisition aligns with Pecca's expansion strategy to establish a foothold in the massive and growing market, while at the same time expands GMK product offering by extracting Pecca's expertise in upholstery seat covers for common vehicle model. Following the completion of the acquisition, GMK has contributed RM1.7m in sales to Pecca's 4Q23 results. We were guided that GMK may contribute 5%-6% of Pecca's revenue in FY24. Besides that, Pecca will continue to infuse an additional funds of Rp2.4bn (circa. RM720,000) into GMK within the next three years.

- **Stable customer base.** Pecca's primary OEM customers presently comprises of Perodua, Proton, Toyota, Nissan, Mitsubishi and etc, which holds a significant market share in Malaysia's automotive market. Concurrently, Pecca commands approximately 50% market share in the leather upholstery sector in the country. Looking ahead, the group's main focus for future growth involves sustaining relationships with existing OEM customers while strategically targeting luxury brands. This strategy hinges on Pecca's capability in maintaining stringent quality control standards which already proven with its recently awarded EASA license.

- **Aviation segment growth prospect still intact.** Pecca's wholly-owned subsidiary, PAviation, has secured certification from EASA for its POA (Production

Organization Approval) in April 2023. This significant milestone places Pecca as the first company in the region to obtain such license and position the group as an exclusive supplier of aircraft upholstery for international aircraft manufacturers. Formerly restricted to serving Malaysian-registered aircraft, Pecca can now extend its services to a broader market and command more favourable pricing as well as profit margins for its aircraft upholstery services. Shortly after obtaining the EASA license, Pecca has established a memorandum of understanding (MoU) with Aero Cabin Solutions SAS (ACS) in France and has secured its first purchase order.

- **Riding on the EV wave.** Leveraging onto the government's strong focus on the EV industry, Pecca has been actively engaging in various initiatives related to EVs. To date, the Group has entered a MoU with the Malaysia Automotive Robotics and IoT Institute (MARii) to collaborate on electric vehicle parts and components technology as well as localisation of luxury brands such as Porsche, Mercedes, Ferrari, Lamborghini, and among others.

## Financial Highlights

- We noticed Pecca's revenue and net profit experienced a three-year CAGR of 28.4% and 61.6% to RM221.3m and RM35.4m respectively in FY23. The remarkable growth can be largely attributed to the robust contribution in the automotive segment, driven by pent-up demand during the Covid-19 pandemic coupled with sales tax exemption. During the period, operating margins also improved from 18.7% to 23.0% due to better operational efficiency as a result from lower labour costs and improving material yield.

- Moving forward, we anticipate that both revenue and core net profit will continue to exhibit improvement, to RM244.5m (+10.5% YoY) and RM41.9m (+18.3% YoY) respectively in FY24F. The projected growth will be underpinned by two key factors: i) strong demand from OEM customers from delivery of backlog orders and ii) expansion in margins facilitated by the upskilling of newly recruited workers post-lockdown, leading to reduced wastage.

| FYE Jun (RM m) | FY21 | FY22 | FY23 | FY24F | FY25F |
|---|---|---|---|---|---|
| Revenue | 144.8 | 164.4 | 221.3 | 244.5 | 257.1 |
| EBITDA | 29.5 | 33.4 | 49.8 | 59.7 | 62.7 |
| Pre-tax Profit | 25.8 | 29.3 | 46.9 | 55.1 | 58.0 |
| Profit After Tax | 19.2 | 22.8 | 35.4 | 41.9 | 44.1 |
| Net Profit | 19.2 | 22.9 | 35.4 | 41.9 | 44.1 |
| Core Net Profit | 19.2 | 22.9 | 35.4 | 41.9 | 44.1 |
| | | | | | |
| Core EPS (sen) | 10.7 | 5.0 | 4.7 | 5.6 | 5.9 |
| Core P/E (x) | 11.2 | 24.2 | 25.4 | 21.5 | 20.5 |
| Dividend Yield (%) | 0.0 | 1.2 | 2.0 | 1.9 | 2.0 |
| P/B (x) | 1.3 | 2.9 | 4.2 | 3.8 | 3.4 |
| ROE (%) | 11.9 | 12.8 | 17.6 | 18.6 | 17.5 |
| Gearing (%) | 0.0 | 4.5 | 5.3 | 5.0 | 4.5 |

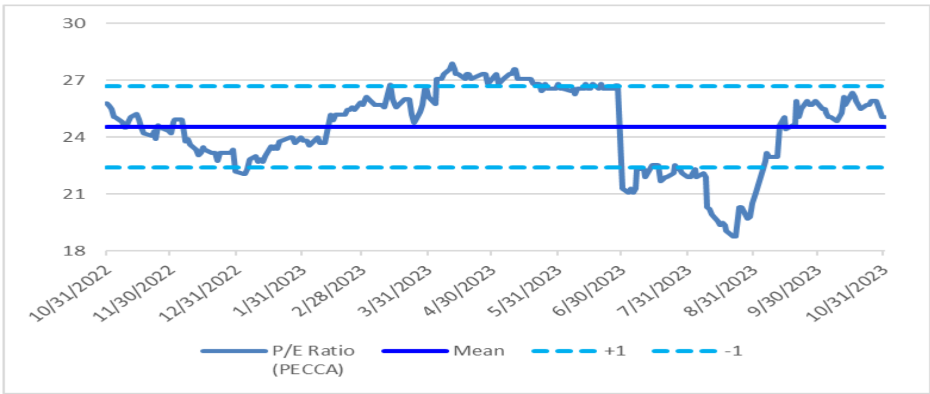
*Source: Company, Apex Securities*

## Valuation & Recommendation

- We are positive on Pecca's earnings growth prospects, supported by increasing EV adoption, future growth potential from its new capacity expansion as well as greater exposure of aviation segment into the foreign markets.

- We derive our target price at RM1.37/, by pegging 1-year historical P/E of 24.5x to FY24 EPS of 5.6 sen.

- We favour Pecca for its double-digit earnings growth potential and backed by a sizeable war chest with net cash position of over RM99.3m. Furthermore, Pecca is expected to remain in a positive operating cash flow with minimal capex spending of RM6.0m for the next 2 years. At present, Pecca has a conservative dividend payout policy of minimum 40% of net profit, translating into a potential 1.9% net dividend yield for FY24.




*Source: Bloomberg, Apex Securities*

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## RESEARCH RECOMMENDATION FRAMEWORK

**STOCK RECOMMENDATIONS**
**BUY**: Total returns* are expected to exceed 10% within the next 12 months.
**HOLD**: Total returns* are expected to be within +10% to – 10% within the next 12 months.
**SELL**: Total returns* are expected to be below -10% within the next 12 months.
**TRADING BUY**: Total returns* are expected to exceed 10% within the next 3 months.
**TRADING SELL**: Total returns* are expected to be below -10% within the next 3 months.
*Capital gain + dividend yield

**SECTOR RECOMMENDATIONS**
**OVERWEIGHT**: The industry defined by the analyst is expected to exceed 10% within the next 12 months.
**NEUTRAL**: The industry defined by the analyst is expected to be within +10% to – 10% within the next 12 months.
**UNDERWEIGHT**: The industry defined by the analyst, is expected to be below -10% within the next 12 months.

## DISCLAIMER