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**VI. INDUSTRY OVERVIEW AND PROSPECTS**

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**1. INDUSTRY OVERVIEW****1.1 Overview of the Malaysian Economy**

The Malaysian economy entered 2002 on a stronger footing, after recovering from a downturn experienced in the last two quarters of 2001. Riding on the back of an earlier-than expected recovery of the U.S. economy and a stronger outturn in the later half of 2002, the Malaysian economy is expected to register a higher but moderate growth in GDP.

The year began with optimism as world economy recovered, led by the U.S. on account of better demand for housing, motor vehicles, increased public expenditure on defence and turnaround in demand for electronics. The high expectations of a strong recovery for the year were, however, marred by a series of uncertainties, particularly a weak second quarter performance, reflecting a slower U.S. GDP growth and lower corporate earnings. Billion dollar corporate scandals, involving gross mismanagement and fraudulent accounting practices in the U.S., coupled with rising Middle East tensions, had also adversely impacted equity prices and depressed investor and consumer confidence. Nonetheless, the continuation of an easy monetary policy and swift government regulatory measures to improve corporate governance and accountability, however, helped arrest further declines in sentiments. With global economic growth intact and supported by a strong domestic sector, Malaysia's economy is expected to further strengthen, particularly during the second half of 2002.

The economy is envisaged to register stronger growth in 2002, following better export performance and continued pick-up in domestic demand. Brighter external prospects due to the economic recovery of the U.S. and a rebound in global electronics demand, especially from the East Asian countries, have hastened Malaysia's export recovery, beginning early 2002. Export has somewhat broadened beyond the electronics sector, aided by the softening of the U.S. dollar against regional currencies to which the RM is pegged.

In the domestic sector, the multiplier effects of the fiscal stimulus measures have provided the impetus for continued economic expansion. Rising consumer confidence arising from improving employment prospects and higher commodity prices are expected to raise consumer spending further as the year progresses. The accommodative monetary policy and intensified efforts to speed up the implementation of public sector projects as well as increased activity in the construction sector are expected to result in a stronger domestic demand in 2002.

Economic growth thus far, has been accomplished within an environment of subdued inflation and full employment. Consumer price increases remained muted below 2% since 2000. Inflationary pressures were curtailed, due in part to excess capacity still prevalent in the economy as well as the benign global inflation. The subdued inflationary outlook provided flexibility in the conduct of fiscal and monetary policies to support the momentum of growth in domestic investment and consumption. With more employment created due to better all-round economic performance, unemployment will be contained with the economy continuing to operate under full employment. Real GDP is projected to grow at 4%-5% as targeted in Budget 2002, within an environment of low inflation and stronger economic fundamentals, supported by both prudent fiscal and accommodative monetary policies. The higher GDP growth of 4%-5%, driven by the domestic sector for the second year running, is expected to emanate from increasing contribution of the private sector.

*(Source: Economic Report 2002/2003)*

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## 1.2 Overview of the Paper Industry

The overall performance in the first nine months of 2002 compared to the same period in 2001 shows a growth of 2.6% which are due to the growth in the pulp paper and paperboard sector and other pulp, paper and paperboard articles sector. Nevertheless, the performance of this industry is expected to grow in the future years as it has established a strong performance since 1993.

The performance of industries in this sector, in terms of ex-factory sales value of establishments in the pulp, paper and related articles manufacturing industry from 1993 to 2002 are summarised below:

Year	Total Pulp and Paper Sector		Pulp, paper and paperboard		Containers and boxes of paper and paperboard		Other pulp, paper and paperboard articles*	
	RM 000	% change	RM 000	% change	RM 000	% change	RM 000	% change
1993	1,414,304	-	320,713	-	600,467	-	493,124	-
1994	1,684,981	19.1	426,060	32.8	740,224	23.3	518,697	5.2
1995	2,233,215	32.5	603,123	41.6	996,460	34.6	633,632	22.2
1996	2,391,660	7.1	649,494	7.7	1,137,029	14.1	605,137	(4.5)
1997	2,647,170	10.7	702,069	8.1	1,291,655	13.6	653,446	8.0
1998	2,598,772	(1.8)	729,337	3.9	1,175,154	(9.0)	694,281	6.2
1999	3,110,868	19.7	889,011	21.9	1,419,443	20.8	802,414	15.6
2000	3,694,286	18.8	1,007,357	13.3	1,880,519	32.5	806,410	0.5
2001	3,512,118	(4.9)	893,442	(11.3)	1,829,756	(2.7)	788,920	(2.2)
2002	3,704,358	5.5	964,834	8.0	1,869,154	2.1	870,370	10.3

(Source: Monthly Manufacturing Statistics, Department of Statistics, December 2002)

**Note:**

\* This is the sub-sector in which production of toilet paper, tissue paper, etc is included.

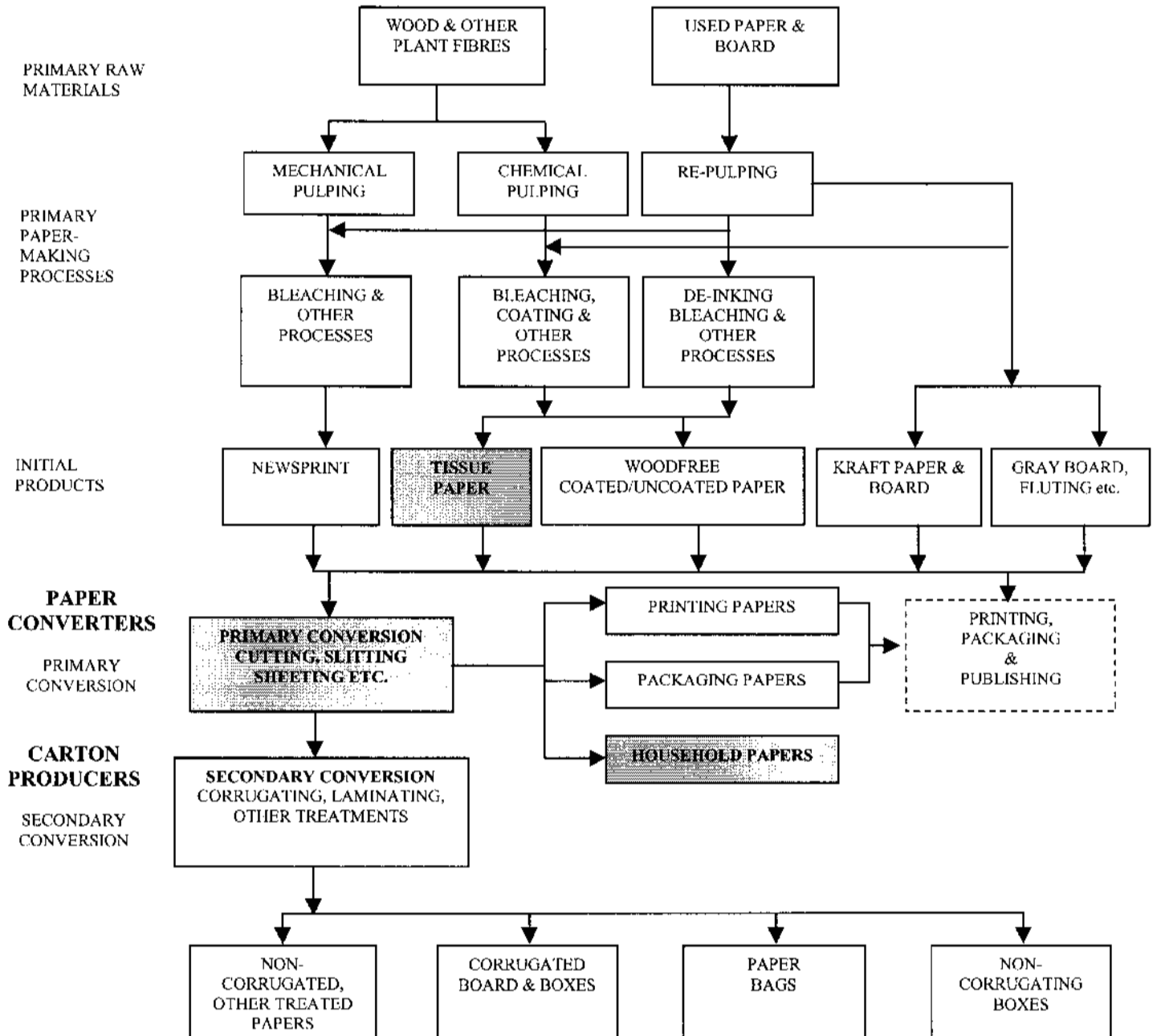
## 1.2.1 Industry Description

In overall, the paper industry is a complex industry as it involves a wide range of goods and has multiple connections to many of the parts of the economy. Its contribution to the GDP of the Malaysian economy is considerably large although its actual contribution is not easily quantifiable. The importance of the industry can be noted from the often usage of paper as the primary indicators by economists to keep track of economies output in developed countries.

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The paper industry can be classified under three (3) sub-categories namely paper, printing and packaging and publishing. The overall structure and processes involved in the paper industry can be summarised in the diagram below:

**PAPER MILLS**



(Source: Extracted from Dynaquest Sdn Bhd, 11 January 2000).

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The participants of the industry can be divided into pulp and paper manufacturers or better known as paper mills, paper converters and carton producers. As NTHB Group is involved in the pulp and paper manufacturers or paper mills and paper converters, the focus of this section will be only in these two (2) subcategories.

***Paper Mills***

The paper-making processes are undertaken at paper mills, which can be further classified into three (3) types namely, *integrated*, where paper is produced directly from wood, *pulp* where paper is produced from bought-in virgin pulp or recycled pulp and *wastepaper*, where wastepaper is converted into recycled pulp which is then turned into paper. The processed papers are then converted into end products such as tissue papers, household papers and other paper related products.

Currently, the paper industry is characterised by a small number of participants due to the high capital intensity and operating cost of paper mills of an economical size. Based on an industrial sectoral analysis report prepared by Dynaquest Sdn Bhd on the paper industry dated 11 January 2000, there is only one integrated paper mill which produce paper directly from wood, namely Sabah Forest Industries Sdn Bhd ("SFI"), a subsidiary of Posim Bhd which has an annual capacity of 165,000 tonnes of woodfree and coated paper, making it the largest producer of printing and writing papers in Malaysia. Apart from SFI, another large manufacturer of paper and paper related products which uses both pulp and recycled papers is Muda Holdings Berhad ("Muda"). Other paper manufacturers which utilise both pulp and recycled paper include Genting Sanyen Industrial Paper Sdn Bhd with an annual operating capacity of 250,000 tonnes of brown grade paper, Pascorp Paper Industries Sdn Bhd with an annual production capacity of 50,000 tonnes and a joint venture company, Malaysian Newsprint Industries Sdn Bhd with 250,000 tonnes production capacity.

Apart from the above, other paper manufacturers are mainly wastepaper paper mills which use recycled papers to convert into papers and paper products. The largest paper recycler is Muda for both commercial and industrial grades. Other paper mills which produces household, toilet and tissue papers from recycled wastepaper are Kimberly, NTHB and Union Paper Industries Sdn Bhd.

Aside from these large paper mills, there are also other "backyard" plants of less than 10,000 tonnes production capacity each. The total average value of output of the 35 paper mills surveyed by the Statistics Department in 1996 was RM21 million with a total workforce of 113 people each.

*(Source: Dynaquest Sdn Bhd, 11 January 2000)*

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***Paper Converters***

In contrast, the paper converting industry is highly fragmented with 131 participants based on a survey conducted by the Statistics Department in 1996. These paper converters are mainly small-scaled operations serving paper merchants as well as local paper mills. This industry segment is getting increasingly more capital intensive and sophisticated.

There are also approximately a dozen of paper converters who cut tissue paper into final product forms such as hand tissues, toilet rolls etc. Amongst these paper converters include Kimberly, NTPM and other companies. Other paper converters which are more technologically advanced are involved in converting aluminium-on-paper laminators and carbonless paper.

*(Source: Dynaquest Sdn Bhd, 11 January 2000)*

**1.2.2 Demand**

Paper products have become part of the necessity of our daily life. For instance, tissue papers and toilet rolls have become a necessity to every households as well as individuals as the cultural attitudes begin to shift towards cleanliness. Therefore, the driving force of the growth in demand of the paper industry is highly influenced by the growth in population as well as the trends in the consumption expenditure of the country.

***Growth in population***

The growth in population of a country is expected to play a significant role in determining the consumption pattern. The total population of Malaysia, according to the 2000 Census was 23.27 million compared to 18.38 million in 1999, thus giving an average annual population growth rate of 2.6% over the 1991-2000 period. The population of Malaysia is expected to continue to grow annually by approximately 2.2% (2000: 23.27 million, 2001: 24.01 million, 2002: 24.53 million, 2003: 25.05 million). This will result in more consumers and new households in the domestic market which will increase the demand for necessary household products. In the Household Expenditure Survey conducted by the Department of Statistics 1998/1999, the findings showed an increasing trend on consumption expenditure by households in Malaysia. In 1973, the average monthly consumption expenditure was RM412, increased to RM1,161 in 1993/1994 and RM1,631 in 1998/1999. On average, households living in urban areas spent 1.5 times higher than households living in rural areas. The average monthly consumption expenditure was RM1,943 per month in the urban areas and RM1,270 per month in the rural areas. This presents an opportunity for growth in the consumer product industry.

*(Source: Malaysia Economic Statistics—Time Series (1999), Department of Statistics—Report on Households Expenditure 1998/99, Economic Report 2000/2001 and Press Statement for Population Distribution and Basic Demographic Characteristics Report Population and Housing Census 2000 dated 6 November 2001)*

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***Growth in private consumption***

Demand for consumer products is expected to improve in tandem with the growth in consumption spending. The strength of private consumption spending, amongst others, is due to the improvement in disposable income arising from the recovery in export earnings and the positive impact of an upward salary revision in the civil service sector and a reduction in individual tax rate. Other contributory factors include better employment opportunities, higher commodity prices and a positive wealth effect on the back of a modest recovery of the stock market. The fiscal policy will also remains mildly expansionary in 2002.

With the anticipation of improvements in consumer confidence arising from high disposable income partly due to large export earnings as well as the positive wealth effect from the improving stock market performance, private consumption is likely to increase strongly by 7.6% in 2003 (2002:5.9%).

*(Source: Economic Report 2002/2003)*

At the same time, the demand for such products is also driven by the changes in consumer preferences, lifestyle and trends. With the increase in awareness of personal hygiene and living standards, the demand for tissue and toilet paper is expected to increase accordingly.

***Seasonality***

The tissue papers, toilet rolls and paper related products industry has one of the biggest advantages of being a consumer product consumed for personal care and cleansing usage on a daily or regular basis as it is unlikely to be subjected to economic instability and is therefore not affected by economic cycles.

**1.2.3 Competition**

The tissue papers, toilet rolls and paper related products industry in Malaysia is highly competitive and operates on relatively fixed end price structures. Manufacturers feel that in order to remain competitive in the market, manufacturers have to expand their production capacity in order to enjoy economies of scale and reduce cost of production. Furthermore, brand awareness also plays a very significant role in the industry.

Currently, the tissue papers, toilet rolls and paper related products industry in Malaysia is made up of approximately seven (7) major companies having manufacturing facilities in Malaysia. However, the industry is mainly dominated by two (2) big manufacturers with well established distribution network and strong marketing arm as well as established brand names nationwide. These two (2) manufacturers enjoy economies of scale and have sufficient capital to invest in high technology machinery and focus on higher degree of automation.

Currently, NTHB is one of the two largest manufacturers in the Malaysian tissue papers, toilet rolls and paper related products industry, the other largest manufacturer being Kimberly. The remaining manufacturers are generally smaller in size and production capacity.

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**1.2.4 Barriers to Entry**

Potential new entrant of the tissue papers, toilet rolls and paper related products industry faces the following barriers to entry:

***Finance resources***

The industry is capital intensive as it requires substantial initial investment to set up the manufacturing facilities equipped with high technology machinery in order to commence operation. Although alternatives are available to smaller players to invest in low technology machinery and focus on highly labour intensive production, production capacity of these smaller players are unable to match that of the established manufacturers. Therefore, these smaller manufacturers will not have the economies of scale to undertake mass production and take advantage of production efficiency and cost saving.

At the same time, one would also need to have access to substantial funds for expansion in the business operation in terms of its distribution and marketing network, to maintain sufficient working capital to hold stocks to meet demands and operating expenditure for larger scale production.

***Production efficiency***

Although there are a large number of manufacturers involved in the industry, very few of them are able to enjoy the benefits of economies of scale as most of the production activities of these smaller companies are carried out on a small scale basis, hence not producing efficiently. As tissue papers, toilet rolls and paper related products are not considered high margin products, production efficiency and cost saving are important in this industry in order for manufacturers to enjoy a high profit margin while sustaining its position in the market.

Competitive pricing plays an important role in the success of the manufacturers. Therefore only those companies that are able to manufacture at low cost and efficiently will be able to sustain in the long term as this would allow them to offer their products at lower prices while still enjoying a high profit margin.

***Distribution network***

Apart from production efficiency, the strength of distribution network is also very important in determining the market coverage of manufacturers in the tissue papers, toilet rolls and paper related products industry which in turn will determine the ability of a company to sustain its position in the industry. Manufacturers with wide distribution network will have the opportunity to expand their market coverage and the ability to service different market segments throughout the country. Wide distribution network will also provide the benefit of better stock management and a more effective and efficient delivery system. These will not only help in providing wider market coverage but also at the same time help in reducing distribution costs, stockholding costs as well as ensuring timely delivery. Manufacturers with wide distribution network which enjoy these benefits will be able to differentiate itself from others as these manufacturers will be able to expand its market coverage to other parts of the country and even overseas markets at a lower cost compared to others.

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***Technical expertise***

This aspect covers the type of the machinery, production materials and experience of human resources. A reasonably high degree of technical know-how is required to constantly ensure high quality products and production efficiency. At the same time, there is also a need for good marketing skills in order to maintain a good and close relationship with suppliers and customers.

***Established brand name***

As tissue papers, toilet rolls and paper related products are consumer products, the recognition of brand names and the perception of customers on the brand names are very important. Therefore, new players may find it difficult to enter into the market to compete with other established brand names where there is existing customer loyalty and support.

**1.2.5 Supply Conditions**

The paper industry is subject to the influence of the supply conditions of raw material. A rise in the price of raw materials would be passed down the line to the secondary and tertiary processors. Thus a rise in the price of virgin pulp would push the price of wastepaper and recycled pulp upward. Therefore, all paper producers would be affected by a rise in raw material cost whether they start from virgin pulp or recycled pulp.

Furthermore, being industrial commodities, wastepaper and pulp are subject to fairly wide swings in prices. The length and amplitude of each price cycle are also is not consistent. It is hence very difficult to predict the future prices of paper. In fact, even large paper mills in the West, which have many decades of experience, do not seem to be able to fix paper prices in advance. Thus the local paper producers are subjected to the problems of wild swings in raw material prices.

In addition, paper price changes can be even sharper due to changes in the import duty on paper. If such changes are in the same direction as the changes in the international prices, the variations in local paper prices will be even fiercer. Thus users of paper and paper board whom are in an industry which is highly competitive such as carton manufacturers, they would find it difficult to pass on the cost increase directly to their customers.

*(Source: Dynaquest Sdn Bhd, 11 January 2000)*

During the economic crisis, the depreciation of RM had caused the prices of imported paper to increase accordingly due to the exchange rate loss. Nonetheless, the Common Effective Preferential Tariff Scheme ("CEPT") being the main implementing mechanism of AFTA in which member countries will gradually lower tariffs on each other's imports, is expected to reduce tariffs to a range of 0-5 per cent by the year 2003. *(Source: www.miti.gov.my)*. This will mean that paper manufacturers will be able to source for cheaper raw materials from other Asean countries and hence able to reduce their selling prices to remain competitive.



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Although the paper industry is exposed to the risk of fluctuation in raw material costs, the tissue papers, toilet rolls and paper related products industry, however, NTHB Group is unlikely to be greatly affected by world pulp prices since pulp constitutes only approximately 2% of the raw materials used for its production. In respect of wastepaper, the cost can be reduced through more effective wastepaper sorting methods and wider sourcing channels. Therefore, even if there is an increase in the raw material prices, the tissue papers, toilet rolls and paper related product manufacturers would not be severely affected as the increase will be marginal. Furthermore, the Group is not dependent on imports of pulp or wastepaper from overseas as pulp is a commodity product and there is currently adequate domestic supply of wastepaper.

At the same time, NTHB Group is able to reduce risk in terms of availability of raw materials as they have a large base of suppliers with whom they have good long term business relationships.

**1.2.6 Capital/Labour Intensive**

The tissue papers, toilet rolls and paper related products industry is a capital intensive industry with expenditure mainly incurred for production machinery and waste disposal management and equipment.

At the same time, it is also a labour intensive industry as the conventional production processes involve predominantly manual processing in terms of sorting and packaging.

The Group has continually invested in production equipment over the past five years and has also developed most of its manufacturing processes in-house over the years. Currently, NTHB Group is well equipped with a fully integrated manufacturing operation system.

Although the operations of NTHB Group is fully integrated, at this juncture, end-of-line processes are still labour intensive, but this is being gradually phased out through the introduction of automated process. The Group is currently moving towards automated production to reduce manual processing and to increase production efficiency.

**1.2.7 Relevant Laws and Regulations**

Currently, there are no relevant laws and regulations which governs the toilet and the tissue papers, toilet rolls and paper related products industry except for the regulations for manufacturing activities governed by the MITI such as the requirements of manufacturing licenses to operate and environment regulations in relation to the treatment and disposal of waste discharge from the manufacturing process.

However, to encourage investments, the Malaysian government provides several incentive schemes designed to grant relief from taxes in various forms. The major incentives for companies in the manufacturing sector are the Pioneer Status, Investment Tax Allowance and Reinvestment Allowance.

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**1.3 Outlook of the Malaysian Economy**

The Malaysian economy, with the stronger macroeconomic fundamentals already in place and complemented by more resilient corporate and financial sectors, is now poised to benefit from the much-improved global economic environment projected for 2003. Output expansion is anticipated in all sectors of the economy, with GDP envisaged to chalk 6%-6.5%, arising from a broader based economy with growth emanating from a more pronounced role of a revitalised and dynamic private sector.

Economic growth will be domestic-led and private sector-driven, particularly in new niche areas of services including tourism, transport, education, health and also agriculture. This is aimed at reducing over-dependence on manufacturing as well as the external sector. With Federal Government expenditure increasing at a moderate pace of 4.6%, the public sector financial position will be strengthened with a move towards consolidation and a balanced budget at the end of the Eighth Malaysia Plan. Federal Government is committed towards minimising and subsequently eliminating bureaucratic delays to further improve service delivery as well as ensure prompt and timely execution and completion of projects and programmes. With added measures directed towards further stimulating economic activity in 2003, both private sector investment and consumption are envisaged to rebound by 16.5% and 9.9%, respectively.

The anticipated growth in the global economy and world electronics demand will contribute to a more robust and broad-based growth in the manufacturing sector. The agriculture sector is expected to expand stronger with higher palm oil production. Economic expansion will also hasten the pace of growth in the services sector while underlying demand for affordable housing and on-going public projects such as the Bakun Hydroelectric Dam and the double-tracking rail projects will continue to fuel growth in the construction sector. The manufacturing sector is expected to continue its expansion to record 8.5% increase in output and contribute 2.6 percentage points to GDP growth while the services sector, with a projected increase of 5.9%, remains the major contributor to growth with 3.3 percentage points. The construction sector is forecast to expand 4.5% while the agriculture and mining sectors are envisaged to improve by 3.4% and 2.5%, respectively. Overall, real GDP growth is expected to accelerate to 6%-6.5% in 2003. With these encouraging economic prospects, GNP per capita is projected to rise further by 5.5% to RM14,098 or USD3,710 (2002: RM13,361, USD3,516), while income in terms of purchasing power parity will also increase by 5.4% to RM33,717 or USD8,873 (2002: 3.3%, RM31,988 or USD8,418).

*(Source: Economic Report 2002/2003)*

**1.4 Prospects of the Industry**

Based on the past performance, the prospect of the tissue papers, toilet rolls and paper related products industry is expected to remain good despite intense competition. Firstly, growth in institutional demand with the growth of Malaysia's hotel and restaurant sectors has a significant bearing on the potential use of tissue papers and toilet rolls including serviettes. The tourism industry is particularly seen to be vibrant and has expanded remarkably well over the years. The Government and related agencies are currently actively encouraging tourism and coupled with recovery in the economy, the demand from this sector is very likely to increase. Secondly, population growth and increasing income levels are expected to ensure a steady increase in demand for tissue papers, toilet rolls and paper related products.

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The growth of Malaysia's hotel and restaurant industries represents a potential growth for the tissue papers, toilet rolls and paper related products industry as concern with cleanliness in such facilities are high and disposable paper products play a crucial role in maintaining world standard expectations for both visitors and increasingly sophisticated domestic users. All major facilities in the area of tourism must now supply patrons with high-quality serviettes, tissue and toilet paper. Furthermore, with the change in cultural attitudes toward the products, more and more urban households are making purchases of such items such as paper kitchen towels and are using paper serviettes at meal times. As such, a significant expansion in this market is anticipated.

The Directors of NTHB believe that the world tissue paper demand is expected to increase in the future and the best growth prospects are in China and other Asian countries, where economic growth, rising standards of living, rapid growth of travel, hotel businesses and fast food chains, all contribute to demand growth.

At the same time, the Eighth Malaysian Plan ("Plan") has also strategically emphasised the diversification, modernisation and strengthening of the industrial base, encouraging increased investment in downstream, resource-based industries such as the pulp and paper industry.

The Plan which covers the period 2001 to 2005 represents the first phase in the implementation of the Third Outline Perspective Plan ("OPP3") 2001-2010 which contains the National Vision Policy to provide the direction for the development of the nation and the policy agenda for the next ten (10) years. The confidence is based upon the ability to implement the Seventh Malaysian Plan despite the attacks by currency speculators that caused the country to experience slowdown in the economy.

The theme of the Plan is achieving sustainable growth with resilience. The three (3) key thrusts of the Eighth Malaysian Plan are to shift the growth strategy from input-driven towards knowledge-driven in order to enhance potential output growth, accelerate structural transformation within the agriculture, manufacturing and services sector and strengthen socio-economic stability through equitable distribution of the nation's income and wealth.

The strengthening of macroeconomic fundamentals and the financial sector together with the strong performance of the economy in 2000 will provide the base to sustain the high growth during the Plan period. With the expected maturity of the economy, there will be less reliance on labour and capital input, while the contribution of Total Factor Productivity as a source for growth will be further enhanced during the Plan period.

The sectoral thrusts of the Plan will see the manufacturing, agriculture and services sector continue to be the major contributors to growth. The manufacturing sector is expected to grow at an average growth rate of 8.9% per annum with its share to GDP increasing to 35.8% by 2005. The downstream development of higher value-added products of the resource-based industries, particularly wood products, rubber products and food product industries are expected to further contribute to the building up of the domestic capabilities as well as the competitiveness of the manufacturing sector.

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At the same time, the Plan also focus on the services sector with higher growth expected from three (3) major subsectors namely, transport, storage and communications; finance, insurance, real estate and business services; and the wholesale and retail trade, hotels and restaurant subsectors. The wholesale and retail trade, hotels and restaurants subsector will be propelled by higher disposable income and also the concerted efforts to make Malaysia a major tourist and shopping destination by hosting major sporting events, making Malaysia a major centre for meetings, conventions and exhibitions as well as organising year long event-based activities. At the same time, efforts will be undertaken to promote domestic tourism, especially to take advantage of the two (2) non-working Saturdays every month.

Through the implementation of the Plan, the tissue papers, toilet rolls and paper related products industry will indirectly benefit and realise potential future growth.

*(Source: Eighth Malaysian Plan 2001 – 2005)*

Furthermore, Asean as a whole is also expected to experience a higher growth rate over the next five (5) years with the opening of new economic frontiers in Myanmar, Vietnam, Cambodia and Laos, particularly with the implementation of AFTA in 2003. Although the consumption rate for these areas are still relatively small, there remains a huge potential in these markets following the growth in the respective economies and the increase in foreign investments.

In terms of long term growth, with increasing awareness of hygiene among the Malaysian population, it is envisaged that consumption in this country will grow and this augurs well for the tissue papers, toilet rolls and paper related products industry.

NTHB Group believes that by having the advantage of efficient and effective distribution network and production capabilities, they will be able to capitalise on the potential growth in the sector. With the increase in population and the increasing awareness of hygiene, the demand for the Group's products is expected to continue to be strong. Furthermore, with its future plans formulated in line with the nation's interests and the Plan, NTHB Group believes that the continuous efforts and commitment by the Group towards process development efforts to further improve production capacities and expand its product range will result in good future prospects for the Group in years to come.

## **2. PROSPECTS AND FUTURE PLANS OF NTHB GROUP**

The Group's main strategy for future growth is to consolidate its local base and strengthen its position in the domestic market while expanding into the overseas markets and diversifying its current product base over the next five (5) years. The Group expects to achieve this through expanding its market base to regional and global markets, expanding its product range to meet the changing needs of consumers and increasing its current production capacity.

- **Market Expansion**

As part of NTHB Group's strategy to fully realise the benefits from the implementation of AFTA in 2003, the Group is planning to establish a stronger foothold its current market coverage in its overseas market including Brunei, Philippines, Thailand, Myanmar and Cambodia. The NTHB Group also plans to export its products to Vietnam by mid 2006 and Southern China by mid 2007. These overseas markets with high population offer a vast opportunity for consumption of tissue papers and toilet rolls and thus enable NTHB Group to expand its existing customer base.

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Currently, the Group has established agency relationships with the local distributors in several of these Asean countries such as Brunei, Philippines, Thailand, Myanmar and Cambodia to market its products. With the implementation of AFTA in 2003, NTHB Group intends to strengthen its distribution channels as well as establishing new production facilities in these Asean countries beginning from the third quarter of 2003 in order to not only serve as agents for the local distributors but as a market player in the local market under its own brand names.

The expansion of business operations will be implemented through either setting up regional marketing offices in the respective countries or by acquiring existing distributors in the local market. This strategy will not only consolidate the positions of smaller existing market players but at the same time eliminates competition. These regional marketing offices will serve as a new distribution channel for NTHB Group in servicing the local markets. Furthermore, with the head office of NTHB Group strategically located in Penang, the Group will become the centre point of the operations in the Asean region.

Besides establishing new distribution channels and marketing network, NTHB Group also intends to build manufacturing plants on a joint venture basis with the local manufacturers in the longer term in several countries including Thailand, Myanmar and China from 2nd quarter of 2004 onwards. This is expected to benefit the Group in terms of cost savings as the production costs in these countries are comparatively lower due to the lower labour costs. At the same time, production activities undertaken in these countries will allow NTHB Group to meet prompt delivery and minimise distribution costs incurred for exporting their products to overseas markets.

Apart from expanding into the Asean region, NTHB Group is also expanding its market share in the local scene in Malaysia particularly in the commercial sector. This includes supplying to more corporate customers such as hotels, large corporations, industrial and commercial properties, shopping complexes and many more. This will help the Group in further strengthening its market position from other market players. Recently, NTPM was awarded by Marko Cash and Carry Distribution (M) Sdn Bhd to manufacture tissue papers, toilet rolls, kitchen towels and serviettes under its in-house brand name of "Aro".

Besides the Asean region, the Group also plans to expand its global market in the long term in order to gain worldwide recognition. Currently, as an initial step towards achieving global recognition, the Group is exporting its products such as tissue and toilet papers as well as jumbo rolls to Taiwan, Australia, South Africa, Bangladesh, Nepal, India, China, Zimbabwe, Turkey, Kuwait and Netherlands. The products exported to these countries are the excess production of the Group after servicing the demands of the domestic as well as Asean region market. This is to ensure that excess production will not affect the pricing in the major markets of the Group. As part of the future plans, the Group is eyeing towards exporting more of its products to other countries in Europe. Currently, the products exported to Europe are under the brand names of Premier, Cutie and Clove.

As part of the strategies to undertake its market expansion programme, H-Link, the dormant company which is intended for e-commerce purposes will be used as the marketing arm of the Group via the internet in order to service the markets in other Asean countries as well as the global market in the longer term by 2004. Through the implementation of AFTA in 2003, the Group will be able to realise potential benefits in terms of cost savings as marketing activities, promotions and advertising activities can be done for the Group as a whole to provide coverage for all the Asean region.

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- **Product Improvement and Diversity**

The Group has, in its current production, a significant range of tissue papers and toilet rolls and paper related products marketed under its own established brand names which are widely accepted by consumers throughout Malaysia. In order to maintain or increase its current market share in the domestic market, the Group will continue to improve and aggressively promote its current three (3) major brands, "Premier", "Cutie" and "Royal Gold Interleaf" and its new brand "ConviRoll".

The strategies to improve and promote its brand names include continuously improving the quality of its products through the use of high quality wastepaper. In order to achieve this, the Group has undertaken various analyses to study the compatibility and suitability of other paper materials as cheaper pulp substitutes in the production of tissue papers and toilet rolls to produce papers with softer texture similar to those produced by virgin pulp. Such developments which were proven to be effective and has been put into commercial production in February 2001. Since then, the usage of the said substitutes has been increasing each month. NTHB Group has and will continue its research and development activities to develop new alternatives to improve the products as well as its production processes.

Apart from strengthening its existing products, the Group has plans to further diversify its product range to have a wider range of products to cater for all segments of the market. Among the various strategies which the Group intends or will continue to employ in order to diversify are as follows:

- (a) Production of wider range of products for industrial use, in particular for cleaning and packaging purposes such as industrial wipes under the brand names of CONVroll and CONVwipes and a wider range of products for commercial use, which includes tissue products for hotels, restaurants and other tourism related entities; and
- (b) Marketing of other paper related products such as facial cotton, sanitary napkins and disposable towels for hospitals.

NTHB Group has launched its facial cotton, cotton buds, cotton balls and cotton wool manufactured under Original Equipment Manufacturer ("OEM") arrangement in March 2002 and is expected to launch its sanitary napkins in 2003.

- **Production Capacity**

The Group has over the past five (5) years implemented a capital investment program to constantly upgrade its production lines and improve production efficiency and productivity. In line with the above objectives, the Group had completed the installation of the Black Clawson de-inking machine and the machine was commissioned in January 2002. With this machine, the Group is able to increase the quality of lower grade raw material and thus maintain the quality of its products at a lower cost. The Group had also completed the upgrading of its existing production line to increase its production capacity to 150 metric tonnes per day. The Group is also planning to invest in acquiring plant and machineries in 2003 costing approximately RM30.0 million to further increase its production capacity by 100 metric tonnes per day bringing its total production capacity to 250 metric tonnes per day by 2004.

NTHB Group has launched its own integrated production software system and it is being implemented in stages as a mean to advance its existing production processes towards a fully automated production process controlled by a central unit in order to increase its production efficiency and reduce manual labour.

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**VI. INDUSTRY OVERVIEW AND PROSPECTS *(Cont'd)***

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NTHB Group believes that with the increase in advertising to promote market awareness of the Group's products and the introduction of several new products, the Group will be able to increase its domestic market share as well as to penetrate into new overseas markets. The future plans of NTHB Group will enable it to achieve its main objective of becoming one of the major players in the industry in the Asean region as well as the global market.

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**VII. RELATED PARTY TRANSACTIONS/CONFLICT OF INTERESTS**

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**1. RELATED PARTY TRANSACTIONS**

**1.1 Interest in Similar Business**

Save as disclosed below, none of the other Directors or Substantial Shareholders of NTHB and/or its subsidiaries have interest, directly or indirectly, in any business carrying on a similar trade as the Company and/or its subsidiaries:

Mr Lee Eng Sia is an existing substantial shareholder of NTHB and brother of Mr Lee See Jin, the Managing Director and substantial shareholder of NTHB. He is also a director and substantial shareholder of Kooka Marketing (M) Sdn Bhd and Kooka Paper Manufacturing Sdn Bhd (collectively referred to as "Kooka"), companies engaged in similar business activities as NTHB Group.

NTHB Group is a supplier of Kooka. The supplies to Kooka amounts to RM10,825 for the financial year ended 30 April 2002. No supplies were made to Kooka for the five (5) month financial period ended 30 September 2002. However, Mr Lee Eng Sia will cease to be a substantial shareholder of NTHB pursuant to the Offer for Sale. In addition, he is not involved in the day-to-day operations of NTHB Group and does not influence the management of NTHB Group. The value of the transaction between NTHB Group and Kooka is immaterial and is at arm's length. As such, the Directors of NTHB Group are of the opinion that Mr Lee Eng Sia's directorship and shareholdings in Kooka will not result in a material conflict of interest and all transactions between NTHB Group and Kooka have been/will be at arm's length.

**1.2 Transactions between NTHB Group and the Promoters, Directors of NTHB Group and/or its Related Parties**

Save as disclosed below, there are no other existing or recurrent transactions between NTHB Group and its Promoters, Directors and/or its related parties:

- (i) Lee Eng Sia, an existing substantial shareholder of NTHB and the brother of Lee See Jin is also a director and substantial shareholder of Priority Plus Sdn Bhd ("Priority"), a company engaged in electronic contract manufacturing. NTHB Group has a rental arrangement with Priority for one of its properties with a monthly rental payment amounting to RM14,000 per month pursuant to the tenancy agreement dated 1 December 2002 between NTPM and Priority for the factory building bearing the address Lot 139, Kawasan Perindustrian Simpang Lima, 34200 Parit Buntar, Perak. The tenancy agreement is for a period of three (3) years from 1 December 2002 to 30 November 2005.

In addition, Lee Eng Sia is also a director and substantial shareholder of Kooka Services Sdn Bhd ("KSSB"), a private limited company engaged in water trading through its shareholding in Kooka Paper Marketing Sdn Bhd. For the five (5) month financial period ended 30 September 2002, NTHB purchased drinking water from KSSB amounting to a total of RM1,070.

Nevertheless, Lee Eng Sia will cease to be a substantial shareholder of NTHB pursuant to the Offer for Sale and he is not involved in the day-to-day operations of NTHB Group and does not influence the management of NTHB Group. The value of the transaction with Priority and KSSB is immaterial and is at arm's length. Therefore, the Directors of NTHB Group are of the opinion that Lee Eng Sia's directorship and shareholding in Priority and KSSB will not result in a material conflict of interest and all transactions between NTHB Group and Priority and KSSB have been/will be at arm's length.



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**VII. RELATED PARTY TRANSACTIONS/CONFLICT OF INTERESTS (Cont'd)**

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- (ii) Teoh Teik Jin, a director and shareholder of NTHB is also a director and substantial shareholder of T.J. Computer Sdn Bhd ("TJC"), a private limited company engaged in supplies of computer hardware. Currently, TJC supplies computer hardware to NTHB Group. For the financial year ended 30 April 2002, the transaction between the Group and TJC amounts to RM32,602. No transactions were recorded between NTHB Group and TJC for the five (5) month financial period ended 30 September 2002.

However, the value of the transaction between TJC and NTHB Group is immaterial and is at arm's length. Therefore, the Directors of NTHB Group (excluding Teoh Teik Jin) are of the opinion that Teoh Teik Jin's directorship and shareholding in NTHB and TJC will not result in a material conflict of interest and all transactions between NTHB Group and TJC have been/will be at arm's length.

**2. DECLARATION OF THE ADVISERS**

CIMB hereby confirms that, as at the date of this Prospectus, there are no existing or potential conflicts of interest in its capacity as the Adviser for the Listing.

Messrs. Ong and Manecksha hereby confirms that, as at the date of this Prospectus, there are no existing or potential conflicts of interest in its capacity as the Solicitor for the Listing.

Messrs. Ernst & Young hereby confirms that, as at the date of this Prospectus, there are no existing or potential conflicts of interest in its capacity as the Reporting Accountants for the Listing.

Messrs. Henry Butcher, Lim & Long (N) Sdn Bhd and Messrs. Henry Butcher, Lim & Long (Malacca) Sdn Bhd hereby confirm that as at the date of this Prospectus, there are no existing or potential conflicts of interest in their capacity as the Valuers for the Listing.