
8. RISK FACTORS

NOTWITHSTANDING THE PROSPECTS OF OUR GROUP AS OUTLINED IN THIS PROSPECTUS, YOU SHOULD CAREFULLY CONSIDER THE FOLLOWING RISK FACTORS THAT MAY HAVE A SIGNIFICANT IMPACT ON OUR FUTURE PERFORMANCE, IN ADDITION TO ALL OTHER RELEVANT INFORMATION CONTAINED ELSEWHERE IN THIS PROSPECTUS, BEFORE MAKING AN APPLICATION FOR OUR IPO SHARES.

8.1 RISKS RELATING TO OUR BUSINESS AND OPERATIONS

8.1.1 Our business and operations are exposed to unanticipated disruptions caused by outbreak of pandemics

Our business and operations are subject to unanticipated disruptions caused by disease outbreaks in Malaysia and the countries to which we export our furniture products. Disease outbreaks may lead to governmental authorities implementing precautionary measures to curb the spread of the diseases, including temporarily halting business activities, border closures and travel restrictions.

In December 2019, there was an outbreak of COVID-19 which began in China, and subsequently spread to other nations including Malaysia. On 11 March 2020, COVID-19 has been classified as a global pandemic by the World Health Organisation. As a result of this pandemic, manufacturers globally faced disruptions in production arising from a shortage of workers and restrictions on human contact resulting from various forms of lockdown instituted by governmental authorities.

Due to the outbreak of COVID-19, the Government imposed the MCO throughout Malaysia which impacted most of the economic sectors and activities, especially those operating as non-essential services.

During the initial MCO period from 18 March 2020 to 30 April 2020, our Group's procurement and production operations were affected. The imposition of the MCO had also affected the operations of our subcontractors and suppliers, which resulted in delays in supplying materials and completion of our subcontracted production and assembly works. The disruption to our production activities, supply of materials and subcontractor services had led to production backlogs which resulted in delays in fulfilling selected orders during the said period. In respect of these delayed deliveries, there are no contractual terms for the customers to claim any delay charges. Nonetheless, we did not experience any cancellation in sales orders.

The pandemic also affected our foreign sales as we have a large export base of customers. Our operations, especially the delivery of products to foreign customers, were also impacted by precautionary measures taken by governments of these countries, such as closure of borders and logistics hubs, to curb the spread of COVID-19. Therefore, the delivery of products to customers who are located in selected countries where their borders or logistics hubs were closed or restricted due to the COVID-19 pandemic were delayed. We also did not experience any claims arising from delayed delivery during this period. Additionally, there have been certain container shortage problems we faced during FYE 2020 and FYE 2021 arising from the pandemic that has caused shipping costs to increase. This is not expected to affect our GP margins as it exports on a 'free on board' basis, where shipping costs are borne by customer. However, it has resulted in higher level of inventory holding as shipping arrangements became more uncertain.

Further, our sales and marketing activities were also affected by the COVID-19 pandemic as furniture fairs and exhibitions, being our key sales and marketing activities, have been postponed or cancelled entirely. This may affect our outreach to potential new customers in our efforts to grow our customer base in the near term and would temporary slowdown our expansion and growth rate.

8. RISK FACTORS (Cont'd)

The economic impact of the COVID-19 in our local and export markets due to mandatory social distancing/quarantines may result in loss of business and decrease in consumer spending, which may consequently impact the demand for furniture. If our customers suffer a loss in business due to the decreased demand for furniture, they may delay, reduce or halt further purchases from our Group, thereby adversely affecting our sales performance. Any such future pandemic outbreaks, as well as epidemic outbreaks affecting a significantly large population, may result in similar interruptions to our Group's business and operations, which may subsequently have a material adverse impact on our financial performance.

8.1.2 Absence of long term agreements with our customers may result in fluctuation of our financial performance

Our Group does not enter into any long term agreements with our customers. We manufacture our products based on confirmed orders. Our customers are mainly distributors, wholesalers and retailers of furniture products and they do not enter into long term agreements with us.

The absence of long term agreements may result in the fluctuation of our Group's revenue and overall financial performance as the orders from our customers are generally on a purchase order basis. While our Group continuously seeks to maintain and strengthen our existing business relationships and establish relationships with new customers to expand our customer base, there can be no assurance that there will be no termination of business relationship or reduced orders from any of our customers which could potentially result in a decline in our financial performance.

8.1.3 We experience concentration of customer base

Our major customers who have contributed significantly to our revenue from FYE 2018 to 2020 and FPE 2021 are as follows:

	FYE 2018	FYE 2019	FYE 2020	FPE 2021	Length of business relationship as at LPD
	%	%	%	%	Years
Birlea Furniture Ltd	8.9	20.7	9.3	5.2	3.3
Noble House Home Furnishings LLC	6.2	6.9	10.4	16.9	3.8
Line Furniture Trd. Est	-	6.8	21.2	26.5	2.8
	15.1	34.4	40.9	48.6	

Note:

* Further details of our major customers and their respective revenue contribution are set out in Section 6.21.

Collectively, the abovementioned major customers contributed approximately 15.1%, 34.4%, 40.9%, 48.6% to our Group's revenue in FYE 2018, FYE 2019, FYE 2020 and FPE 2021 respectively. We expect that these major customers will continue to contribute to our Group's revenue in the future.

8. RISK FACTORS (Cont'd)

Our Group has not historically entered into and presently does not have any long term agreements with these major customers or any of our other major customers. Although the Group is not dependent on its major customers individually, we may be materially and adversely affected if we were to lose one or more of our major customers without securing new customers in a timely manner to replace the loss of business, or if we were to encounter difficulties in collecting payment from these major customers.

8.1.4 We may be affected by price fluctuations of our raw materials

We purchase our raw materials from a pool of local suppliers who have established track record and are able to provide a constant supply at competitive prices. The main raw materials we use in furniture production is particle boards and MDF, which accounted for approximately 61.1%, 51.4%, 50.4% and 50.1% of our total cost of sales for FYE 2018, FYE 2019, FYE 2020 and FPE 2021, respectively.

The price of our raw materials may fluctuate due to changes in supply and demand. Any shortage or disruption in the supply of raw materials which results in price fluctuation may adversely affect our operations and financial performance. In particular, raw material prices have been increasing by between 5% to 20% during the second half of FYE 2021. Overall, this has caused cost of sales to increase by approximately 2.5% increase in general. However, the impact of higher material costs on our GP margins is temporary, as we can gradually increase the selling price of our furniture to maintain our profit margins and mitigate these cost increases. As at LPD, we have not encountered any material fluctuations in the cost of our raw materials that would adversely affect our financial performance.

8.1.5 We are exposed to fluctuations in foreign exchange rates

Our furniture products are primarily exported, with 47.9%, 76.7%, 84.9% and 82.9% of our revenue in FYE 2018, FYE 2019, FYE 2020 and FPE 2021 being derived from export sales. Our export sales are primarily denominated in USD. Our export market primarily comprises customers from the Middle East, Europe and North America. This inherently subjects us to foreign exchange rates risks which are affected by various factors that are beyond our control, including but not limited to political and economic climates of Malaysia and the world. Therefore, any significant change in foreign exchange rates may affect our Group's financial results. For FYE 2018 to 2020, and FPE 2021, the currency breakdown of our revenue is as follows:

	Audited							
	FYE 2018		FYE 2019		FYE 2020		FPE 2021	
	RM'000	%	RM'000	%	RM'000	%	RM'000	%
Revenue								
• in RM	5,306	54.9	5,790	24.0	6,510	15.4	3,407	17.1
• in USD	4,364	45.1	18,351	76.0	35,888	84.6	16,512	82.9

The weighted average exchange rate ("WAFEX") for USD:RM over FYE 2018 to 2019, FPE 2020 and FPE 2021, is as follows:

	FYE 2018	FYE 2019	FYE 2020	FPE 2020	FPE 2021
WAFEX (USD:RM)	4.13	4.01	4.10	4.09	4.23

For illustration, if the USD weakened against RM by 5% in FYE 2020 and in FPE 2021, this would result in our sales transacted in USD decreasing by approximately RM1.7 million and RM0.8 million respectively.

8. RISK FACTORS (Cont'd)

We maintain foreign currency accounts to receive our USD sales proceeds. Additionally, we also enter into foreign currency forward exchange contracts with banking institutions to sell our USD sales proceeds at agreed exchange rates for fixed periods of time to reduce the exposure of our receivables. Our Group mitigates foreign exchange risk through natural hedging by using our USD sales proceeds to pay for our USD purchases of raw materials. There are some purchases amounting to RM0.4 million for FPE 2021 from a new supplier in Thailand which are quoted in USD.

With the use of foreign currency forward exchange contracts, the foreign exchange gain/(loss) recorded is as follows:

	<u>FYE 2018</u> <u>RM'000</u>	<u>FYE 2019</u> <u>RM'000</u>	<u>FYE 2020</u> <u>RM'000</u>	<u>FPE 2021</u> <u>RM'000</u>
Foreign exchange gain/(loss)	(23)	147	302	(91)

For illustration, the foreign exchange gain/(loss) recorded without the use of foreign currency forward exchange contracts is as follows:

	<u>FYE 2018</u> <u>RM'000</u>	<u>FYE 2019</u> <u>RM'000</u>	<u>FYE 2020</u> <u>RM'000</u>	<u>FPE 2021</u> <u>RM'000</u>
Foreign exchange gain/(loss)	-	(15)	12	211

Any adverse fluctuation in foreign exchange rates will have a negative impact on our financial performance.

Kindly refer to Section 11.10.1 for further details relating to the impact of foreign exchange rates.

8.1.6 We are dependent on our key senior management

The continued success and growth of our business is dependent on our ability to retain our key management personnel, in particular our Managing Director, Jason Koh Jian Hui and our Executive Director, Koh Cheng Huat. Since our incorporation in 2016, they have been instrumental in the development of our corporate strategy and the growth of our business. Their ability to understand the furniture industry and anticipate consumer trends equips them with the necessary skillsets to establish business relationships with our customers and suppliers.

They are supported by a team of qualified and experienced key senior management personnel. Collectively, they have extensive industry knowledge which enable us to remain competitive in the furniture industry. As such, a loss of such experienced management personnel without suitable and timely replacements could have a material impact on our competitiveness, business and operations.

8.1.7 We are subject to subcontracting risks

We leverage on our subcontractors for parts of our production process, and are therefore dependent on them to a certain extent whereby the total subcontractor charges make up 14.2%, 7.8%, 10.5% and 10.4% of total cost of sales for FYE 2018, FYE 2019, FYE 2020 and FPE 2021. The subcontractors Jacksing Deco-Brand Sdn Bhd and Chilly Deco Sdn Bhd are listed among our major suppliers. We select our subcontractors based on, among other factors, their competitiveness in terms of the quality of their processes, delivery time, our past working experience with them and their past track record. However, there can be no assurance that the processes performed by our subcontractors will always be satisfactory or will always meet our requirements and specifications.

8. RISK FACTORS (*Cont'd*)

In addition, we may be liable for any losses or damages which arise from the delays of fulfilment of orders and delivery by our subcontractors. These risks may have a material impact on our business, results of operations and financial performance.

As at LPD, we have not faced such circumstances that have had a material adverse impact on our business and operations. There have been no issues with our subcontractors performances in the past. Nonetheless, if we are not able to engage any subcontractors, it will adversely affect our production, revenue and profitability.

8.1.8 Inability to keep abreast with developments in the furniture industry

The marketability of our furniture products depends significantly on consumer preferences and spending trends. The changes in these trends are influenced by factors including, amongst others, the state of the economy and market demographic profiles, which are all beyond our control. The lower consumer spending due to economic downturn would create a material impact on our business and financial performance, as consumers are more cost conscious and selective in spending.

It is therefore important for us to produce designs with sufficient market appeal to a wider consumer base in order to remain competitive in the furniture industry, such as introducing affordable furniture range with enhanced functionality. In the event that our furniture designs are unable to keep up with the changing consumer preferences, our prospects and financial performance may be materially affected as we experience loss in consumer demand and market share.

8.1.9 We may be exposed to major or sustained disruptions in our operations

Major or sustained disruptions to our operations will result in a longer lead time for the production of our furniture products. Such risks include, amongst others, fire hazards, power shortage, mechanical failure or operational difficulties. Failure to meet delivery deadlines as a consequence of such disruptions may in turn result in the loss of business or claims against us and such incidents may affect our business relationships with our customers thereby affecting our profitability. As such, we need to ensure that our production process operates efficiently such that we can fulfil our orders in a timely manner.

In addition, as most of our furniture products for the export market are transported by ships, we are subjected to shipping disruptions for various reasons such as adverse weather conditions and port strikes which may lead to delayed or lost shipments and may have impact on our financial performance. There were no product liability claims against the Group in the past.

8.1.10 We may be exposed to potential product liability claims

The nature of our business exposes us to the risk of product liability claims that is inherent in the production of our furniture products. We are exposed to potential product liability if our products are found to be unfit for use or prove to be defective.

If our customers suffer losses or damages, we may be liable to product liability claims under Malaysian law or the laws of other jurisdictions which we may be subject to. Additionally, we are not have product liability insurance. Nonetheless, there is no known circumstance where our products have resulted in monetary claims from any suppliers, retailers or end consumers. In the event that there is any defect to a sold product, we would normally replace such products in line with our regular practice.

8. RISK FACTORS (Cont'd)

As a result, we may have to incur significant legal costs and divert our administrative resources regardless of the outcome of the claims. Any successful product liability claim against us will adversely affect our business and reputation. Even if we are able to successfully defend such claim, there can be no assurance that customers will not lose confidence in our products. There were no product liability claims against the Group in the past.

8.1.11 We are subject to regulatory requirements for our business operations

Our business is subject to various laws, rules and regulations. Save for the Certificate for Accommodation (as set out below), we have obtained the necessary licences and approvals from various governmental authorities for our business, as set out in Section 6.18.

The licences and approvals are subject to compliance with relevant conditions, laws and regulations under which they were issued. In the event of non-compliance, these licences and approvals may be revoked or may not be renewed upon expiry. Similarly, any breach of these conditions, laws and regulations can result in penalties, fines, potential prosecution against us and/or our directors, restrictions on operations and/or remedial liabilities.

Pursuant to Section 24D(1) of the Workers Minimum Standards of Housing and Amenities (Amendment) Act 2019 ("**WMSHA 2019**"), no accommodation shall be provided to an employee unless certified with a Certificate for Accommodation ("**CFA**"). Ecomate provides such accommodation to our foreign workers at rented apartments located within the vicinities of our factories. As such, the CFA is required to be obtained by Ecomate. Section 24D(3) of the WMSHA 2019 provides that an employer who contravenes Section 24D(1) of the WMSHA 2019 commits an offence and shall, on conviction, be liable to a fine not exceeding RM50,000.

As at LPD, the issuance of CFA for the aforementioned premises is still pending. Nonetheless, the premises rented for workers' quarters is in compliance with the relevant land and building regulations. These details are set out in Section 6.17.2

If we fail to obtain the Certificate for Accommodation, on conviction, we shall be liable to a fine not exceeding RM50,000 for each location. In addition, our operations may be temporarily disrupted as we will be required to relocate our foreign workers to new accommodation locations with ready CFA.

8.1.12 Political, economic, legal or social conditions of the countries where we transact our business

We derive a significant portion of our revenue from our export markets. For FYE 2018, FYE 2019, FYE 2020 and FPE 2021, our export sales accounted for approximately 47.9%, 76.7%, 84.9% and 82.9% of our revenue respectively.

Factors such as changes in political leadership, economic conditions, interest rates, business and credit conditions as well as government policies includes currency exchange rules and introduction of new regulations or changes in import quotas would affect our financial condition and results of operations. As such, we are susceptible to political, social, economic, legal and regulatory developments in these countries where we have direct business relationships with our customers.

While we take measures to mitigate such risks by keeping abreast with economic and regulatory changes in the relevant countries, there can be no assurance that any adverse changes in political, economic and regulatory conditions of the countries will not materially affect our financial performance. However, with our continuous effort to diversify our customer base, we could reduce the susceptibility of our financial performance to any political, economic and regulatory changes in a particular country.

8. RISK FACTORS (*Cont'd*)

8.2 RISKS RELATING TO OUR INDUSTRY

8.2.1 We are subject to regulatory requirements for our business operations

Our business is subject to various laws, rules and regulations. We have obtained the necessary major licences, permits and approvals from various governmental authorities and issuers for our business, as set out in Section 6.18 save for the Wood-based Furniture Factory Licence.

Under the Johor Wood-based Industries Enactment 1986, a Wood-based Furniture Factory Licence is required from the state forestry authority to operate a furniture factory. Our Group had, on 4 May 2020, submitted an application for the Wood-based Furniture Factory Licence to the Johor Utara District Forestry Office ("**JFD**"). JFD had via its letter dated 20 September 2020 to the Director of Forestry, Johor stated that they had no objections to Ecomate's application for the Wood-based Furniture Factory Licence. A site visit was conducted by the JFD on 2 November 2020. In addition, the Company had a meeting with the relevant officers from the JFD on 5 January 2021 to expedite the application and was informed that the application is only pending the approval at the Johor State Council Meeting.

We recognise the importance of obtaining such licence and we shall endeavour to procure such licence as well as fulfil and comply with the conditions imposed on the aforesaid licence, if any, when the same is issued. Thus far, we have not encountered any difficulty in obtaining business licence and other operational licences in the past for the operation of our business. However, there can be no assurance that the regulatory authorities will issue the Wood-based Furniture Factory Licence without delay or will not vary, modify or impose further conditions on our Group for such licence in the future. Our management is monitoring and liaising closely with the relevant authorities to obtain this Wood-based Furniture Factory Licence.

The major licences, permits and approvals as aforementioned are subject to compliance with relevant conditions (if any), laws and regulations under which they were issued. In the event of non-compliance, these licences, permits and approvals may be revoked or may not be renewed upon expiry.

Further, the relevant governmental authorities or issuer may take action by issuing warnings, imposing penalties, suspending the licences, permits or approvals, reducing the term, imposing additional conditions or restrictions and/or revoking the licences, permits or approvals, against us for any breach or non-compliance. Any revocation or failure to obtain, maintain or renew any of the licences or permits may materially and adversely affect our business operations and financial performance.

In addition, we may be required to comply with further and/or stricter requirements if there are changes to applicable laws, regulations or policies in Malaysia. This may affect our business operations and financial performance if we are unable to comply with the new laws, regulations or policies.

8.2.2 We are dependent on foreign production workers

As a result of the shortage of local workers in Malaysia, we are dependent on foreign workers from Bangladesh and Myanmar. As at LPD, we have 68 foreign workers, representing approximately 50.7% of our employees. We are therefore vulnerable to changes in the availability and costs of employing foreign workers.

8. RISK FACTORS (Cont'd)

Any unfavourable changes of labour policies and visa restrictions of these countries will cause disruptions to our production activities and business operations. The supply of foreign workers in Malaysia is subject to the policies and regulations imposed by the Government from time to time. Malaysia's strict immigration policies and rules limit the inflow of foreign labour into the country. For instance, the availability of foreign workers in Malaysia is regulated through policies such as imposition of levies and quotas. As a result, we may face shortage in employing workers to meet the needs of our production activities and operations.

In addition, with increasing demand of foreign labour, especially skilled labour, we cannot assure that we can continue to attract foreign workers at the current level of wages or our current foreign workers will continue to be employed by us. Any increase in competition for foreign workers, especially skilled workers, may result in higher labour wages. Consequently, if we are unable to pass on the increase in labour costs to our customers, our financial performance will be affected.

In the event of a shortage of foreign workers to meet our operational requirements, we may not be able to fulfil orders placed by our customers in a timely manner or our costs of labour may increase.

We have obtained 1-year working permits for our foreign workers, which are renewable annually. Notwithstanding the above, as at LPD, we have not experienced any shortage in foreign workers which has resulted in major disruption to our production.

8.2.3 We are subject to competition from local and foreign manufacturers

The furniture industry is highly competitive and we face competition from local and foreign manufacturers. Typically, we compete with our competitors on a variety of factors, such as product quality, product designs, pricing, delivery times, reputation and customer service. There can be no assurance that we will be able to compete with our competitors effectively and the competition will become more intense with the entry of new market players.

Our competitors or potential competitors may possess longer operating histories, more extensive experience, wider network of suppliers and customers, greater financial capability, better marketing efforts and other resources which enable them to capture a larger market share than us. Some of our competitors may also be more aggressive in their pricing to capture or retain their market share or may have lower cost of production, which would enable them to pass the cost savings to their customers. This may lead to an increased pressure on us to maintain competitiveness by lowering the prices of our products. Consequently, the intense pricing competition will lower our profit margins due to the loss of market share.

As such, we have to promptly adapt to market conditions and trends to maintain and grow our market share and there can be no assurance that we are able to compete effectively with our competitors.

8.3 RISKS RELATING TO THE INVESTMENT IN OUR SHARES

8.3.1 There is no prior market for our Shares

Prior to our Listing, there was no public trading for our Shares. The listing of our Shares on the ACE Market does not guarantee that an active market for our Shares will develop.

There is also no assurance that our IPO Price will correspond to the price at which our Shares will be traded on the ACE Market.

8. RISK FACTORS (*Cont'd*)

8.3.2 Our Listing is exposed to the risk that it may be aborted or delayed

Our Listing may be aborted or delayed should any of the following occurs:

- (a) The selected investors fail to subscribe for their portion of our IPO Shares;
- (b) Our Underwriter exercising its rights under the Underwriting Agreement to discharge itself from its obligations therein; and
- (c) We are unable to meet the public shareholding spread requirement set by Bursa Securities, whereby at least 25.0% of our total number of Shares for which listing is sought must be held by a minimum number of 200 public shareholders each holding not less than 100 Shares upon the completion of our IPO and at the point of our Listing.

If any of these events occur, investors will not receive any Shares and we will return in full without interest, all monies paid in respect of the Application within 14 days, failing which the provisions of Section 243(2) of the CMSA will apply.

If our Listing is aborted and/or terminated, and our Shares have been allotted to the investors, a return of monies to the investors could only be achieved by way of cancellation of share capital as provided under Sections 116 or 117 of the Act and its related rules.

Such cancellation requires the approval of shareholders by special resolution in a general meeting, with sanction of High Court of Malaya or with notice to be sent to the Director General of the Inland Revenue Board and ROC within 7 days of the date of the special resolution and us meeting the solvency requirements under Section 117(3) of the Act.

There can be no assurance that such monies can be recovered within a short period of time in such circumstances.

8.3.3 The trading price and trading volume of our Shares following our Listing may be volatile

The trading price and volume of our Shares may fluctuate due to various factors, some of which are not within our control and may be unrelated or disproportionate to our financial results. These factors may include variations in the results of our operations, changes in analysts' recommendations or projections, changes in general market conditions and broad market fluctuations.

The performance of Bursa Securities is also affected by external factors such as the performance of the regional and world bourses, inflow or outflow of foreign funds, economic and political conditions of the country as well as the growth potential of the various sectors of the economy. These factors invariably contribute to the volatility of trading volumes witnessed on Bursa Securities, thus adding risks to the market price of our Shares.

8.4 OTHER RISKS

8.4.1 Our Promoters will be able to exert significant influence over our Company

Our Promoters will collectively hold approximately 66.2% of our enlarged share capital upon Listing. Because of the size of their shareholdings, our Promoters will have significant influence on the outcome of certain matters requiring the vote of shareholders unless they are required to abstain from voting by law and/or as required by the relevant authorities.