

13 August 2019 | 2QFY19 Results Preview

Leong Hup International Berhad

2QFY19 earnings to be impacted by lower selling prices

INVESTMENT HIGHLIGHTS

- Expect 2QFY19 normalised earnings to be below RM45.0m
- The subdued quarterly earnings was mainly due to the lower selling prices of products sold particularly in Malaysia
- Given ASP has recovered from June 2019 onwards, we expect improve profitability in the subsequent quarters
- Initial valuation premium does not match the earnings quality of the group
- Downgrade to NEUTRAL with a revised target price of RM0.88

Expect 2QFY19 normalised earnings to be below RM45.0m. To recall, Leong Hup International Berhad (LHI) recorded a strong 1QFY19 normalised earnings which came in at RM60.5m, accounting for 31.2% of our full year FY19. However, moving forward, we are expecting 2QFY19 normalised earnings to come not more than RM45.0m, which translate into a decline of about -25.0%qoq. This is largely due to the significant reduction in average selling price (ASP) of the products sold by the group, particularly in Malaysia.

Reduction in selling prices of products sold. Based on management latest guidance, the subdued earnings in the 2QFY19 is attributable to the significant reduction in 2QFY19 selling price of broiler's day-old-chicks (DOC) in Malaysia to RM1.21 per DOC and broiler chicken to RM3.99 per kg. These represent a decline of -38.6%yoy and -14.7%yoy respectively. We suspect the decline in ASP was mainly due stricter enforcement of price control mechanism on poultry products, especially during the Hari Raya festive period. However, this is partly mitigated by the higher sales volume achieved by both products during the quarter with a growth of +8.1%yoy and +10.7%yoy respectively. Note that Malaysia's livestock business historically contributed between 10.0% to 12.0% of the group's total revenue. Hence, we expect a considerable drag in the 2QFY19 earnings.

ASP is now on a recovery trend. From June 2019 onward, we observed that selling prices of both products are on an uptrend in Malaysia. The latest ASP for broiler DOC and broiler chicken have recovered to RM2.00 per DOC and RM5.00 per kg respectively. Furthermore, the group has ongoing initiatives to lower cost per unit of production such as reducing dependency on third-party contract farms. Coupled with the stronger ASP moving forwards, we expect the margins and profitability will gradual improve in the subsequent quarters.

Downgrade to NEUTRAL

(Previously BUY)

Revised Target Price (TP): RM0.88

(Previously RM1.34)

RETURN STATS

Price (9 th August 2019)	RM0.85
Target Price	RM0.88
Expected Share Price Return	+3.5%
Expected Dividend Yield	+2.1%
Expected Total Return	+5.6%

STOCK INFO

KLCI	1,615.05
Bursa / Bloomberg	6633 / LHIB MK
Syariah Compliant	No
Issued shares (mil)	3,650.0
Market cap. (RM'm)	3,102.5
Price over NA	2.13
52-wk price Range	RM0.84 – RM1.19
Beta (against KLCI)	NA
3-mth Avg Daily Vol	NA
3-mth Avg Daily Value	NA
Major Shareholders (%)	
Clariden Inv	9.01%
Lau Joo Han	2.11%
Lau Eng Guang	1.61%
Joo Hong Lau	0.76%

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Impact to earnings. We are maintaining our FY19F and FY20 earnings forecasts as our earnings projections are still within expectations as we have already imputed lower ASP. Note that the reduction in ASP was partially mitigated by a higher sales volume, in our view.

Target price. We value LHI at **RM0.88** (previously RM1.34) per share based on pegging FY20F EPS of 5.6sen to target PER of 15.8x (previously 24.0x). We revised our target PER downward to 15.8x which is the FY20 market cap weighted average PER of LHI's regional peers to take into account the abrupt selling price fluctuation of the group's products. We do not expect the selling price to be significant lower than previous year.

Table 1: Peer Comparison Table

Company	Country	Market Cap (RM)	FY20 PE
Charoen Pokphand Indonesia	Indonesia	1,236.0	18.8
Japfa Comfeed Indonesia	Indonesia	587.8	9.2
Thaifoods Group	Thailand	217.8	16.3
		Market Cap Weighted Average	15.8

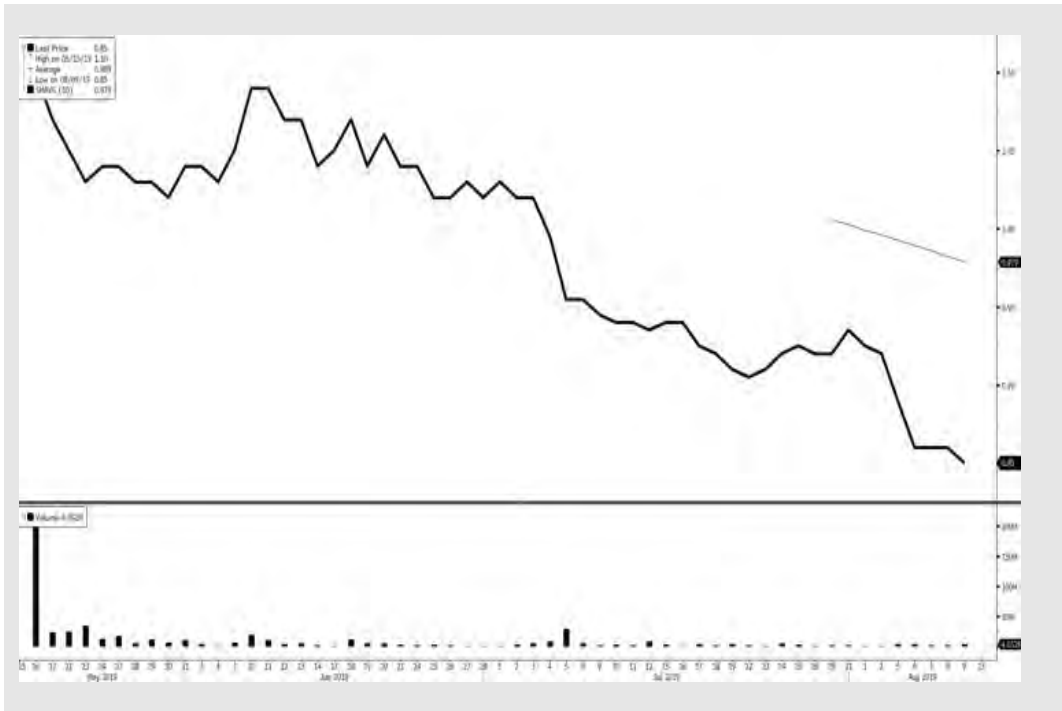
Downgrade to NEUTRAL. The livestock business is a high- volume, low-margin business as the products can be regarded as a commodity and consumers are mostly price sensitive. As such, it is important for poultry players to emphasis on volume and to manage their cost effectively in order to protect their profit margins. Moving forward, we do not expect a wild fluctuation in LHI's product prices as seen in 2Q19. Premised on this, we still expect that LHI's earnings growth will be sustained driven by its strategy to focus on: (i) economies of scale; (ii) vertically integration and; (iii) geographically diversifying its operation. All things considered, we are downgrading our call recommendation to **NEUTRAL** from BUY previously. 

INVESTMENT STATISTICS

FYE Dec (RMm)	FY2016	FY2017	FY2018	FY2019F	FY2020F
Revenue	5,257.4	5,501.4	5,746.6	5,976.4	6,245.4
Core EBITDA	646.8	583.1	654.6	681.1	709.9
Depreciation & amortisation	(196.9)	(199.1)	(197.1)	(210.9)	(220.4)
Core EBIT	449.9	384.0	457.5	470.2	489.5
Finance costs	(103.0)	(92.2)	(109.5)	(107.6)	(112.4)
Share of profits of associates	0.4	0.5	0.6	0.6	0.6
PBT	347.3	292.3	348.6	363.2	377.7
PAT	270.0	247.4	246.8	257.1	271.9
PATANCI	182.5	192.6	186.2	194.1	206.1
EPS (sen)	5.0	5.3	5.1	5.3	5.6
EPS growth (%)	66.2	5.5	(3.3)	4.3	6.2
Net Dividend (sen)	-	-	-	1.9	2.0
EBITDA margin (%)	12.3	10.6	11.4	11.4	11.4
PATANCI margin (%)	3.5	3.5	3.2	3.2	3.3
Dividend yield (%)	-	-	-	2.1	2.1

Source: Company, MIDFR

DAILY PRICE CHART



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MIDF AMANAH INVESTMENT BANK : GUIDE TO RECOMMENDATIONS

STOCK RECOMMENDATIONS

BUY	Total return is expected to be >10% over the next 12 months.
TRADING BUY	Stock price is expected to <i>rise</i> by >10% within 3-months after a Trading Buy rating has been assigned due to positive newsflow.
NEUTRAL	Total return is expected to be between -10% and +10% over the next 12 months.
SELL	Total return is expected to be <10% over the next 12 months.
TRADING SELL	Stock price is expected to <i>fall</i> by >10% within 3-months after a Trading Sell rating has been assigned due to negative newsflow.

SECTOR RECOMMENDATIONS

POSITIVE	The sector is expected to outperform the overall market over the next 12 months.
NEUTRAL	The sector is to perform in line with the overall market over the next 12 months.
NEGATIVE	The sector is expected to underperform the overall market over the next 12 months.