

HLIB Research

PP 9484/12/2012 (031413)

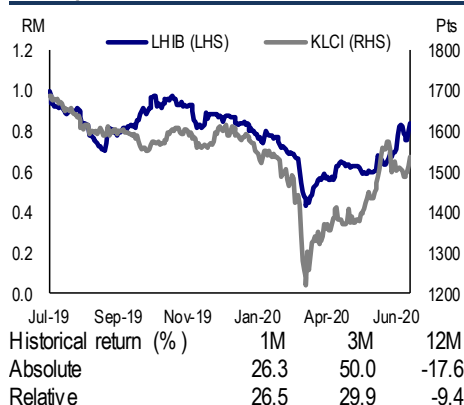
Chye Wen Fei
wfchye@hlib.hongleong.com.my
(603) 2083 1712
BUY (from Hold)

Target Price: RM0.90
Previously: RM0.56
Current Price: RM0.84

Capital upside	7.1%
Dividend yield	1.8%
Expected total return	8.9%

Sector coverage: Poultry

Company description: LHI offers breeding, egg production, broiler, and livestock feeding solutions, as well as manufactures chicken products in Malaysia, Singapore, Indonesia, Vietnam and Philippines.

Share price

Stock information

Bloomberg ticker	LHIB MK
Bursa code	6633
Issued shares (m)	3,650
Market capitalisation (RM m)	3,066
3-mth average volume ('000)	3,832
SC Shariah compliant	No

Major shareholders

Emerging Glory Sdn Bhd	52.8%
Clarinden	9.0%
Amanah Saham Nasional	5.7%

Earnings summary

FYE Dec (RMm)	FY19	FY20f	FY21f
PATMI - core	157.1	145.3	181.7
EPS - core (sen)	4.3	4.0	5.0
P/E (x)	19.5	21.1	16.9

Leong Hup International

Better long-term earnings stability

We are turning more positive on LHI's earnings prospects, on the back of recent recovery in poultry product prices in the SEA region and its aggressive downstream expansion plan (via the expansion of The Baker's Cottage (TBC) outlets). We raise our FY20-22 core net profit forecasts by 7.2%, 3.3% and 2.8%, respectively, mainly to account for slightly higher broiler price assumptions (following the sharper-than-expected demand recovery). We upgrade our rating on LHI to BUY with a higher TP of RM0.90 (based on revised 18x FY21 EPS of 5.0 sen).

We are turning more positive on LHI's earnings prospects, on the back of recent recovery in poultry product prices in the SEA region and its aggressive downstream expansion plan (via the expansion of The Baker's Cottage (TBC) outlets).

Downstream venture (via expansion of TBC outlets) to add stability to LHI's earnings stream. LHI's downstream venture, via the expansion of TBC outlets (from 53 outlets currently to 80 outlets by end-2020, and 300 outlets by end-2023) allows LHI to mitigate the volatile poultry product prices, and hence stabilising earnings at Malaysian operations over the longer term. Based on our estimates, LHI's downstream segment will consume at least 30% of its broiler supply by 2024, which at the same time, indicates that at least 30% of its broiler supply in Malaysia will no longer subject to price volatility.

Unfazed by intense competition among bakery businesses. Despite the intense competition among the bakery businesses, management is confident on its business model, as TBC has remodelled its business and repositioned itself to "hybrid concept" bakery, with roast chickens being its anchor product. LHI will embark on its outlet expansion in the suburban areas of Klang Valley and Southern region (where rental is cheaper and competition is less intense vis-à-vis the urban areas), and the prices of its products (in particularly, chicken products) are priced more affordably relative to most other (if not all) bakeries and/or quick service restaurants.

Capex of RM35-40m p.a. from downstream venture. The aggressive downstream expansion plan will incur an additional capex of RM35-40m p.a. over the next 4 years, and we believe LHI will not have issues in funding this, as LHI has already delayed part of its group expansion plans in FY20-21.

Poultry product prices recovered since mid-May. New venture aside, we note that poultry product prices have recovered swiftly in SEA region since mid-May, thanks to easing lockdown measures (which have resulted in a strong demand recovery for poultry products) and supply chain adjustment. While it remains questionable if current high poultry product prices could be sustained over the longer term, we believe it is unlikely for poultry product prices to revisit their previous lows, as economic activities have started showing signs of normalising (unless second wave of Covid-19 infection and lockdown happen).

Forecast. We raise our FY20-22 core net profit forecasts by 7.2%, 3.3% and 2.8%, respectively, mainly to account for slightly higher broiler price assumptions (following the sharper-than-expected demand recovery). We have yet to reflect earnings contribution from its downstream venture, as we await better clarity on its expansion plan progress.

Upgrade to BUY, with higher TP of RM0.90. Higher core net profit forecasts aside, we took the opportunity to (i) roll forward our valuation base year (from FY20 to FY21), and (ii) raise our target P/E to 18x (from 15x earlier), as we believe LHI deserves a higher valuation multiple following its downstream venture (which will in turn stabilise its earnings base over the longer term). Correspondingly, we upgrade

our rating on LHI to **BUY** (from Hold), with a higher TP of RM0.90 (from RM0.56 earlier) based on revised 18x FY21 core EPS of 5.0 sen.

Financial Forecast

All items in (RM m) unless otherwise stated

Balance Sheet

FYE Dec	FY18A	FY19A	FY20F	FY21F	FY22F
Cash	458.9	764.8	749.0	716.8	820.9
Receivables	825.5	670.0	673.5	706.8	741.5
Inventories	575.6	679.6	667.1	700.1	734.6
PPE	2,216.8	2,396.5	2,572.8	2,734.9	2,792.1
Others	757.2	898.2	895.3	914.1	933.8
Assets	4,834.0	5,409.1	5,557.6	5,772.8	6,022.9
Payables	519.9	560.2	558.8	586.4	615.3
Debt	2,370.9	2,381.8	2,381.8	2,381.8	2,381.8
Others	177.8	282.9	282.9	282.9	282.9
Liabilities	3,068.6	3,228.6	3,227.2	3,254.9	3,283.8
Shareholders' equity	1,301.8	1,641.2	1,742.7	1,869.6	2,017.3
Non-controlling interests	463.6	539.3	587.7	648.3	721.9
Equity	1,765.4	2,180.5	2,330.4	2,517.9	2,739.2

Income Statement

FYE Dec	FY18A	FY19A	FY20F	FY21F	FY22F
Revenue	5,746.6	6,054.8	6,003.6	6,300.9	6,611.3
EBITDA	654.6	650.5	610.2	681.7	743.5
EBIT	457.5	425.0	386.3	443.7	500.4
Finance cost	-109.5	-136.6	-125.0	-116.8	-103.2
Associates	0.6	0.4	0.5	0.5	0.5
Profit before tax	348.6	288.8	261.7	327.3	397.7
Tax	-101.8	-75.8	-68.1	-85.1	-103.4
PAT	246.8	213.0	193.7	242.2	294.3
Non-controlling interests	-60.6	-62.4	-48.4	-60.6	-73.6
Reported PATMI	186.2	150.6	145.3	181.7	220.7
Exceptionals	33.4	6.5	0.0	0.0	0.0
Core PATMI	219.6	157.1	145.3	181.7	220.7
Consensus core PATMI			167.9	200.8	224.7
HLIB/ Consensus			86.5%	90.5%	98.2%

Cash Flow Statement

FYE Dec	FY18A	FY19A	FY20F	FY21F	FY22F
Profit before tax	348.6	288.8	261.7	327.3	397.7
D&A	199.4	197.4	224.0	238.1	243.0
Working capital	-241.8	38.7	10.8	-57.3	-59.7
Tax paid	-75.7	-57.0	-68.1	-85.1	-103.4
Others	118.8	189.1	124.5	116.3	102.7
CFO	-378.6	-373.0	-400.0	-400.0	-300.0
Capex	-423.0	-403.6	-400.0	-400.0	-300.0
Others	44.4	30.7	0.0	0.0	0.0
CFI	-378.6	-373.0	-400.0	-400.0	-300.0
Changes in debt	178.9	-43.5	0.0	0.0	0.0
Shares issued	0.0	269.6	0.0	0.0	0.0
Dividends	-66.3	-84.5	-43.8	-54.8	-73.0
Others	-119.5	-144.3	-125.0	-116.8	-103.2
CFF	-6.9	-2.7	-168.8	-171.6	-176.2
Net cash flow	-36.2	281.1	-15.8	-32.2	104.1
Beginning cash	427.4	390.4	670.8	655.0	622.8
Forex	-0.8	-0.7	0.0	0.0	0.0
Ending cash	390.4	670.8	655.0	622.8	726.9

Ratios

FYE Dec	FY18A	FY19A	FY20F	FY21F	FY22F
Core EPS (sen)	6.0	4.3	4.0	5.0	6.0
P/E (x)	14.0	19.5	21.1	16.9	13.9
EV/EBITDA (x)	7.2	7.2	7.7	6.9	6.3
DPS (sen)	1.6	1.2	1.5	2.0	2.0
Dividend yield	1.9%	1.4%	1.8%	2.4%	2.4%
BVPS (RM)	0.4	0.4	0.5	0.5	0.6
P/B (x)					
EBITDA margin	18.9%	19.2%	18.1%	19.4%	20.5%
EBIT margin	6.6%	5.7%	5.0%	5.5%	6.0%
PBT margin	5.0%	3.9%	3.4%	4.1%	4.7%
Net margin	3.2%	2.1%	1.9%	2.3%	2.6%
ROE	17.7%	10.7%	8.6%	10.1%	11.4%
ROA	4.7%	3.1%	2.6%	3.2%	3.7%
Net gearing	108.3%	74.2%	70.1%	66.1%	57.0%

Assumptions

FYE Dec	FY20F	FY21F	FY22F
Feedmill			
- Production volume ('000 mt)	2,453.6	2,588.2	2,731.2
- Utilisation rate	72%	73%	77%
Livestock			
- Broiler DOC supplied (m chicks)	179.6	185.0	190.5
- Broiler supplied (m birds)	119.6	122.6	125.2
- Eggs supplied (m eggs)	1,804.7	1,851.8	1,900.4

Disclaimer

The information contained in this report is based on data obtained from sources believed to be reliable. However, the data and/or sources have not been independently verified and as such, no representation, express or implied, are made as to the accuracy, adequacy, completeness or reliability of the info or opinions in the report.

Accordingly, neither Hong Leong Investment Bank Berhad nor any of its related companies and associates nor person connected to it accept any liability whatsoever for any direct, indirect or consequential losses (including loss of profits) or damages that may arise from the use or reliance on the info or opinions in this publication.

Any information, opinions or recommendations contained herein are subject to change at any time without prior notice. Hong Leong Investment Bank Berhad has no obligation to update its opinion or the information in this report.

Investors are advised to make their own independent evaluation of the info contained in this report and seek independent financial, legal or other advice regarding the appropriateness of investing in any securities or the investment strategies discussed or recommended in this report. Nothing in this report constitutes investment, legal, accounting or tax advice or a representation that any investment or strategy is suitable or appropriate to your individual circumstances or otherwise represents a personal recommendation to you.

Under no circumstances should this report be considered as an offer to sell or a solicitation of any offer to buy any securities referred to herein.

Hong Leong Investment Bank Berhad and its related companies, their associates, directors, connected parties and/or employees may, from time to time, own, have positions or be materially interested in any securities mentioned herein or any securities related thereto, and may further act as market maker or have assumed underwriting commitment or deal with such securities and provide advisory, investment or other services for or do business with any companies or entities mentioned in this report. In reviewing the report, investors should be aware that any or all of the foregoing among other things, may give rise to real or potential conflict of interests.

This research report is being supplied to you on a strictly confidential basis solely for your information and is made strictly on the basis that it will remain confidential. All materials presented in this report, unless specifically indicated otherwise, are under copyright to Hong Leong Investment Bank Berhad. This research report and its contents may not be reproduced, stored in a retrieval system, redistributed, transmitted or passed on, directly or indirectly, to any person or published in whole or in part, or altered in any way, for any purpose.

This report may provide the addresses of, or contain hyperlinks to websites. Hong Leong Investment Bank Berhad takes no responsibility for the content contained therein. Such addresses or hyperlinks (including addresses or hyperlinks to Hong Leong Investment Bank Berhad own website material) are provided solely for your convenience. The information and the content of the linked site do not in any way form part of this report. Accessing such website or following such link through the report or Hong Leong Investment Bank Berhad website shall be at your own risk.

1. As of 03 July 2020, Hong Leong Investment Bank Berhad has proprietary interest in the following securities covered in this report:

(a) -

2. As of 03 July 2020, the analyst(s) whose name(s) appears on the front page, who prepared this report, has interest in the following securities covered in this report:

(a) -

Published & printed by:

Hong Leong Investment Bank Berhad (10209-W)

Level 28, Menara Hong Leong,

No. 6, Jalan Damanlela,

Bukit Damansara,

50490 Kuala Lumpur

Tel: (603) 2083 1800

Fax: (603) 2083 1766

Stock rating guide

BUY	Expected absolute return of +10% or more over the next 12 months.
HOLD	Expected absolute return of -10% to +10% over the next 12 months.
SELL	Expected absolute return of -10% or less over the next 12 months.
UNDER REVIEW	Rating on the stock is temporarily under review which may or may not result in a change from the previous rating.
NOT RATED	Stock is not or no longer within regular coverage.

Sector rating guide

OVERWEIGHT	Sector expected to outperform the market over the next 12 months.
NEUTRAL	Sector expected to perform in-line with the market over the next 12 months.
UNDERWEIGHT	Sector expected to underperform the market over the next 12 months.

The stock rating guide as stipulated above serves as a guiding principle to stock ratings. However, apart from the abovementioned quantitative definitions, other qualitative measures and situational aspects will also be considered when arriving at the final stock rating. Stock rating may also be affected by the market capitalisation of the individual stock under review.