



Company report

LEONG HUP INTERNATIONAL

(LHIB MK EQUITY, LEOG.KL)

20 Oct 2020

A better 2H as poultry prices, consumer demand improve

BUY

(Maintained)

AmInvestment Bank

www.amequities.com.my

03-2036 2290

Rationale for report: Company update

Price	RM0.70
Fair Value	RM0.96
52-week High/Low	RM1.00/RM0.43

Key Changes

Fair value	↑
EPS	↑

YE to Dec	FY19	FY20E	FY21F	FY22F
Revenue (RM mil)	6,054.8	5,398.4	6,348.5	7,382.6
Core net profit (RM mil)	150.6	109.3	172.2	205.9
FD Core EPS (sen)	4.1	3.0	4.7	5.6
FD Core EPS growth (%)	(19.1)	(27.4)	57.6	19.6
Consensus Net Profit (RM mil)	-	118.7	181.1	211.3
DPS (sen)	1.2	0.9	1.4	1.7
PE (x)	17.0	23.4	14.8	12.4
EV/EBITDA (x)	6.5	8.0	6.7	6.1
Div yield (%)	1.8	1.3	2.0	2.4
ROE (%)	10.2	6.5	9.7	10.8
Net Gearing (%)	98.5	105.7	111.0	120.8

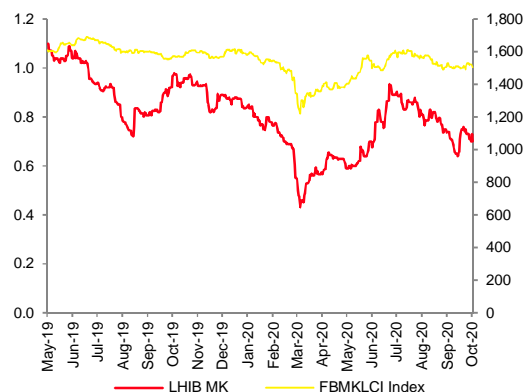
Stock and Financial Data

Shares Outstanding (million)	3,650.0
Market Cap (RM mil)	2,555.0
Book Value (RM/share)	0.45
P/BV (x)	1.6
ROE (%)	10.2
Net Gearing (%)	98.5

Major Shareholders	Clarinden Inv Pte. (9.0%)
	Lau Joo Han (2.1%)
	Lau Eng Guang (1.6%)

Free Float	87.3
Avg Daily Value (RM mil)	1.9

Price performance	3mth	6mth	12mth
Absolute (%)	(20.9)	19.7	(28.2)
Relative (%)	(16.0)	12.0	(25.0)

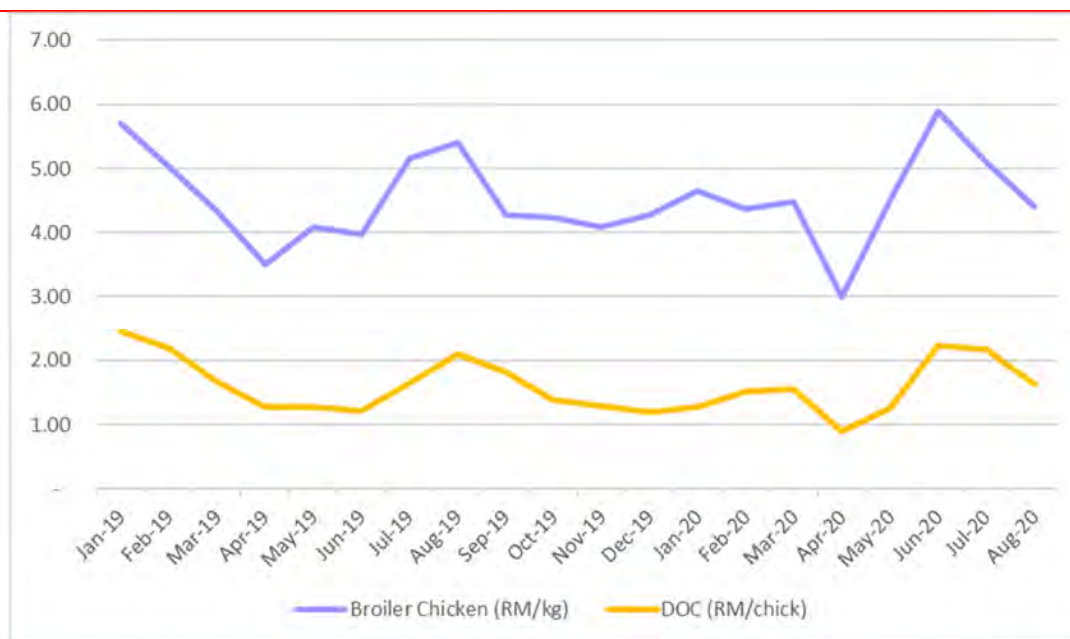


Investment Highlights

- We maintain our BUY call on Leong Hup International (LHI) with a slightly higher fair value (FV) of RM0.96/share (vs. RM0.94/share previously). Our FV is based on an unchanged PE of 17x FY22F EPS.
- We increase our earnings forecast by 3% for FY20E and 2% each for FY21F and FY22F. These are to account for stronger-than-anticipated poultry prices and solid showings by The Baker's Cottage (TBC).
- That said, we expect volatility in poultry prices resulting from the ongoing conditional movement control order (CMCO). LHI's decision to forego previous expansion plans in favour of projects geared towards processed food may also limit earnings in the short term.
- Key takeaways from LHI's teleconference include:
 1. Poultry product prices continue to be volatile as the CMCO weakens demand from the HORECA industry.
 2. The lower demand for poultry is also expected to affect animal feed sales volume. Furthermore, raw material prices have been steadily rising.
 3. LHI's expansion plans are recalibrated due to poorer demand: overall capex is lower and it could be looking towards processed food production.
 4. Following better poultry prices after the MCO, TBC sales have normalized. Store expansion is ahead of schedule.
- With ongoing pandemic disruptions, the group anticipates poultry ASP to be volatile. Nonetheless, poultry prices have experienced a gradual recovery after the first MCO and we have adjusted our forecasts upwards, most notably for Malaysian products — by +27% to RM3.90 per kg for broiler chicken and +15% to RM1.36 for day-old-chicks (DOC) for FY20E.
- We believe that our average price assumption of RM3.90/kg for broiler chicken for FY20E is conservative enough to account for any price decline following the second MCO in October 2020.
- Currently, Malaysian broiler and DOC ASP are priced at RM4.30 and RM1.50 respectively (FY19 average: RM4.17, RM1.50), with Indonesia at similar figures.

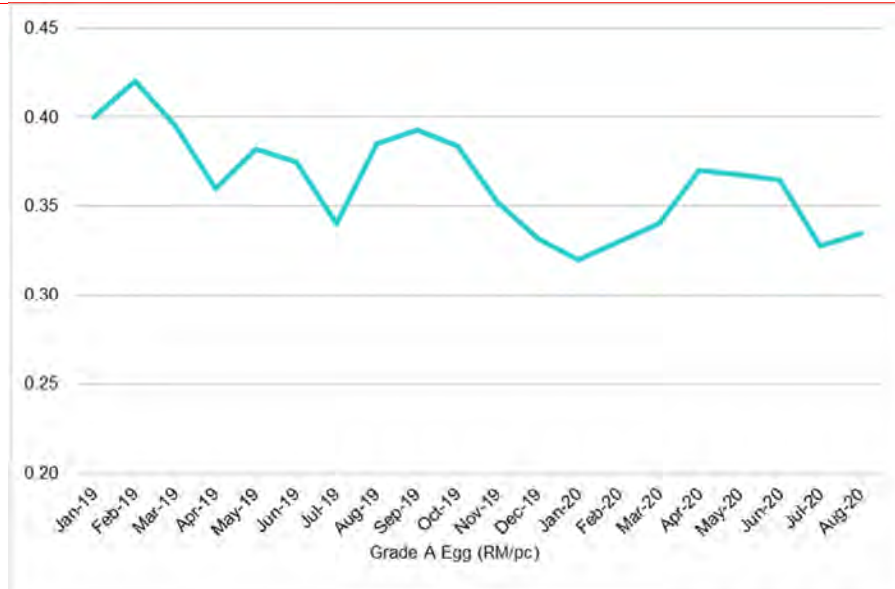
- We believe that this pattern of poor demand will persist well into FY21F. Nevertheless, the mitigation factors are: (1) TBC provides an alternative means of inventory rundown; (2) Indonesia has executed market price stabilizing measures, including mass culling and limited egg hatching.
- LHI expects lower sales from its feedmills as result of lower meat demand. Raw material prices have risen steadily since 1H20 — Corn: 15% QoQ; Soybean 16% QoQ — leading to a forecasted 15% QoQ increase of feed prices. Fortunately, gross margin contraction arising from lower feedmeal pricing is only temporary and not expected to affect profit margins significantly as the extra cost will eventually be passed on to customers.
- Overall capex for FY20F is expected to fall to RM300mil from the previous estimation of RM500mil.
- A number of LHI's expansions plans in Indonesia and the Philippines have been put on hold. LHI has made small forays into Myanmar and Cambodia but subsequently postponed all plans until the situation improves.
- In Malaysia, capex is mainly used for its processed food plant and TBC expansion. From 28 outlets at time of takeover, LHI is slated to open 100 outlets by the end of the year, higher than its initial target of 85 outlets (which is the number of currently functional stores). The processed food plant is intended to widen TBC's product range.
- Following the relaxation of the first MCO, higher poultry prices have led to lower sales for TBC. Sales have declined to 100 birds per store daily (8.5K birds sold/day) from 300 birds sold/day during the height of the first MCO. However, this is still well within the group's expectation of 8–9K birds daily. The group forecasts a slight boost in sales during the CMCO as the population refrains from eating out.
- We believe that over a longer period, the current poor industry conditions will actually benefit LHI. The group has been steadily increasing market share in Malaysia — 25% DOC, 10% broilers — as smaller farms die out and provide it with further room for economies of scale. The group's efforts to boost its processed food segment will provide a more diverse, stable earnings base.
- However, in the short term, volatile prices, scrapped expansionary plans and weaker poultry and feed demand could exert downward pressures to the group's profitability. Nonetheless, the group's control of the whole supply chain through its TBC business, economy of scale benefits and product status as a consumer staple will maintain its decent performance for now.
- We believe LHI's performance will improve in 2HFY20 on the back of improving poultry prices and consumer demand. We forecast a 58% improvement in net profit in FY21F as better pandemic management continues to strengthen ASP and demand.

EXHIBIT 1: PRICE OF POULTRY



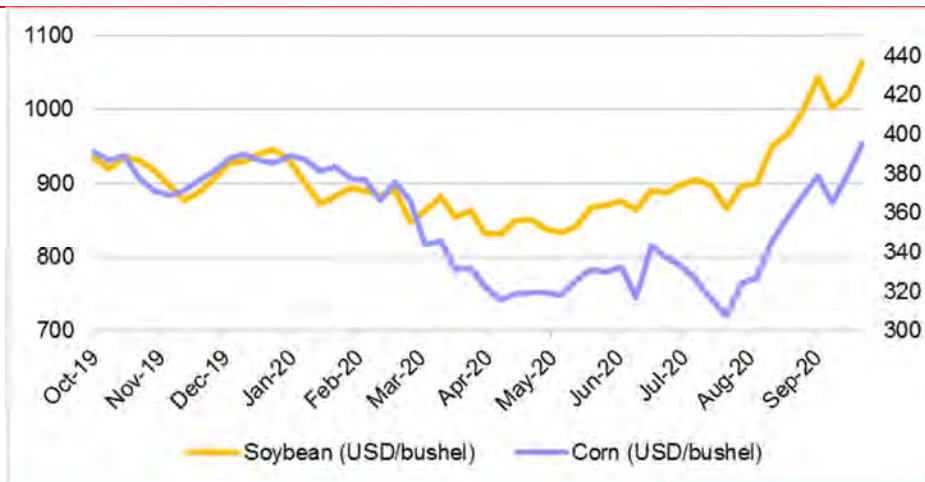
Source: Bloomberg, AmInvestment Bank Bhd

EXHIBIT 2: PRICE OF EGGS



Source: Bloomberg , AmInvestment Bank Bhd

EXHIBIT 3: CORN AND SOYBEAN PRICES



Source: Bloomberg , AmInvestment Bank Bhd

EXHIBIT 4: AVERAGE SELLING PRICE ASSUMPTIONS BY COUNTRY

	FY19	FY20F	FY21F
Malaysia			
DOCs per chick	1.58	1.36	1.53
Broiler chickens per kg	4.17	3.90	4.13
Per Egg	0.31	0.26	0.27
Indonesia			
DOCs per chick	1.69	1.12	1.28
Broiler chickens per kg	4.89	3.29	4.12
Eggs	0.35	0.31	0.35
Vietnam			
DOCs per chick	1.67	1.45	1.55
Broiler chickens per kg	4.58	3.49	3.95
Per Egg	0.24	0.29	0.29

Source: Company, AmInvestment Bank Bhd

EXHIBIT 5: PB BAND CHART

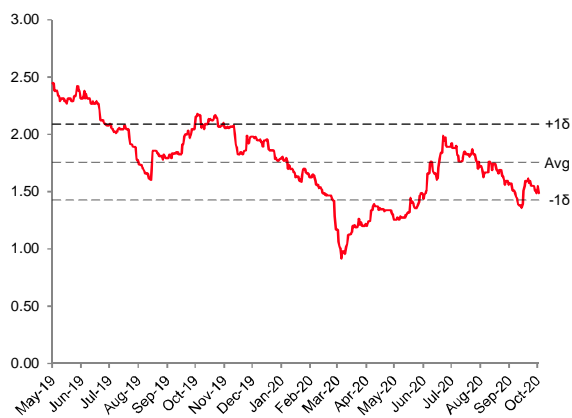


EXHIBIT 6: PE BAND CHART

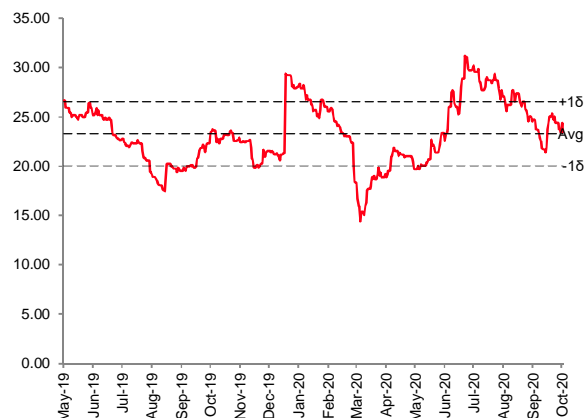


EXHIBIT 7: FINANCIAL DATA

Income Statement (RMmil, YE 31 Dec)	FY18	FY19	FY20E	FY21F	FY22F
Revenue	5,746.6	6,054.8	5,398.4	6,348.5	7,382.6
EBITDA	646.8	637.7	546.4	689.8	812.8
Depreciation/Amortisation	(189.9)	(225.5)	(201.1)	(236.5)	(275.0)
Operating income (EBIT)	456.9	412.1	345.3	453.3	537.8
Other income & associates	0.6	0.4	0.5	0.7	1.0
Net interest	(108.9)	(123.8)	(145.0)	(157.1)	(179.3)
Exceptional items	-	-	-	-	-
Pretax profit	348.6	288.8	200.8	296.9	359.6
Taxation	(101.8)	(75.8)	(46.2)	(68.3)	(82.7)
Minorities/pref dividends	(60.7)	(62.4)	(45.3)	(56.4)	(70.9)
Net profit	186.1	150.6	109.3	172.2	205.9
Core net profit	186.1	150.6	109.3	172.2	205.9
Balance Sheet (RMmil, YE 31 Dec)	FY18	FY19	FY20E	FY21F	FY22F
Fixed assets	2,216.8	2,396.5	2,696.5	3,096.5	3,496.5
Intangible assets	97.3	97.5	97.5	97.5	97.5
Other long-term assets	261.2	85.9	86.1	86.1	86.1
Total non-current assets	2,575.3	2,579.8	2,880.1	3,280.1	3,680.1
Cash & equivalent	458.9	764.8	481.0	514.7	555.1
Stock	575.6	679.6	529.6	633.3	733.1
Trade debtors	649.2	499.3	577.1	687.9	788.6
Other current assets	574.2	561.1	500.8	560.9	619.4
Total current assets	2,257.9	2,504.8	2,088.4	2,396.8	2,696.2
Trade creditors	248.9	273.1	239.6	283.3	331.6
Short-term borrowings	1,326.6	1,508.7	1,545.9	1,654.4	1,784.1
Other current liabilities	309.3	307.6	305.6	308.6	311.8
Total current liabilities	1,884.8	2,089.5	2,091.1	2,246.3	2,427.6
Long-term borrowings	1,044.3	873.1	751.0	900.0	1,166.0
Other long-term liabilities	139.4	144.4	144.4	144.4	144.4
Total long-term liabilities	1,183.8	1,017.5	895.4	1,044.4	1,310.4
Shareholders' funds	1,301.8	1,641.2	1,717.7	1,838.2	1,982.4
Minority interests	463.6	539.3	480.8	565.5	657.6
BV/share (RM)	0.36	0.45	0.47	0.50	0.54
Cash Flow (RMmil, YE 31 Dec)	FY18	FY19	FY20E	FY21F	FY22F
Pretax profit	348.6	288.8	200.8	296.9	359.6
Depreciation/Amortisation	189.9	225.5	201.1	236.5	275.0
Net change in working capital	(241.8)	38.7	(132.6)	274.7	259.0
Others	52.5	103.9	(41.2)	(580.2)	(787.1)
Cash flow from operations	349.2	656.9	228.1	227.9	106.4
Capital expenditure	(423.0)	(403.6)	(300.0)	(400.0)	(400.0)
Net investments & sale of fixed assets	6.5	(5.0)	(0.3)	-	-
Others	37.9	35.7	-	-	-
Cash flow from investing	(378.6)	(373.0)	(300.3)	(400.0)	(400.0)
Debt raised/(repaid)	178.9	(43.5)	(84.9)	257.5	395.7
Equity raised/(repaid)	-	-	-	-	-
Dividends paid	(58.0)	(84.5)	(32.8)	(51.7)	(61.8)
Others	(127.8)	125.2	-	-	-
Cash flow from financing	(6.9)	(2.7)	(117.7)	205.8	333.9
Net cash flow	(36.2)	281.1	(189.8)	33.7	40.4
Net cash/(debt) b/f	427.4	390.4	670.8	481.0	514.7
Net cash/(debt) c/f	390.4	670.8	481.0	514.7	555.1
Key Ratios (YE 31 Dec)	FY18	FY19	FY20E	FY21F	FY22F
Revenue growth (%)	4.5	5.4	(10.8)	17.6	16.3
EBITDA growth (%)	10.9	(1.4)	(14.3)	26.2	17.8
Pretax margin (%)	6.1	4.8	3.7	4.7	4.9
Net profit margin (%)	3.2	2.5	2.0	2.7	2.8
Interest cover (x)	4.2	3.3	2.4	2.9	3.0
Effective tax rate (%)	29.2	26.2	23.0	23.0	23.0
Dividend payout (%)	-	30.0	30.0	30.0	30.0
Debtors turnover (days)	41	30	39	40	39
Stock turnover (days)	35	38	41	33	34
Creditors turnover (days)	16	16	17	15	15

Source: Company, AmInvestment Bank Bhd estimates

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