

30 August 2019

Poultry | Food & Beverages Product

Leong Hup International (LHIB MK)

Buy (Maintained)

Look Forward To 3Q19 Turnaround; Stay BUY

Target Price (Return)	MYR1.36 (+79%)
Price:	MYR0.76
Market Cap:	USD657m
Avg Daily Turnover (MYR/USD)	4.59m/1.09m

- **Stay BUY and TP of MYR1.36 (WACC: 5.6%), 79% upside plus c.2% yield.**

1H19 results were broadly within expectations on anticipation of stronger quarters ahead. This is judging mainly from the sharp recovery in product prices in Malaysia. Over the longer run, sustainable growth would be underpinned by capacity expansion and robust consumption of poultry products. Selling could have been overdone with the stock now trading at 11x FY20F P/E, or a steep 35% discount to regional average.

- **1HFY19 results broadly within expectations.** Leong Hup International (LHI) reported 1H19 core net profit of MYR78.7m (-38.5% YoY), which accounted for 39%/37% of our/consensus forecasts. We deem the results as broadly within expectations on anticipation of stronger quarters ahead, judging from the sharp recovery in product prices in Malaysia. Note that average broiler and DOC prices in Malaysia surged 32% and 44% so far in 3Q19 vs 2Q19 average. Post results, we make no changes to our earnings forecasts and DCF-derived TP of MYR1.36.

- **Results review.** YoY, 1H19 revenue grew 7.7% to MYR3bn, mainly driven by robust growth in Indonesia and Vietnam, whilst Malaysia sales fell marginally due to weak product prices in 2Q19. By business segment, a jump in feedmill sales on the back of favourable pricing and capacity expansion has more than offset the weakness in livestock division on softer product prices. Meanwhile, 1H19 EBITDA inched up 1% to MYR330.4m, thanks to a higher contribution from Indonesia and Vietnam. Similarly, the feedmill division has also chipped in to the higher EBITDA in 1H19, underpinned by higher sales and margin expansion. The group declared a DPS of 1.6 sen.

- **Hatching the eggs patiently.** As we believe the market had priced in the moderate 2Q19 results, hence the depressed share price, it ignored the high possibility of a turnaround in 3Q19 that should stem from the recovery in product prices, particularly in Malaysia. In addition, the high base effect in Singapore should wear off from 3Q19 onwards. To recap, the group disposed a subsidiary in Singapore on 30 Jun 2018, which resulted in a loss of revenue.

Nonetheless, price fluctuations are inherent in the poultry industry, and investors should be focused on the longer term growth prospects of the company instead. This is likely to be underpinned by capacity expansion across operating markets, the robust consumption of poultry products as the cheapest source of protein, and its religious neutrality. A potential near-term catalyst would be a sharp earnings rebound in 3Q19.

- **Risks to our recommendation include** unfavourable changes in regulatory policy, and supply-demand dynamics.

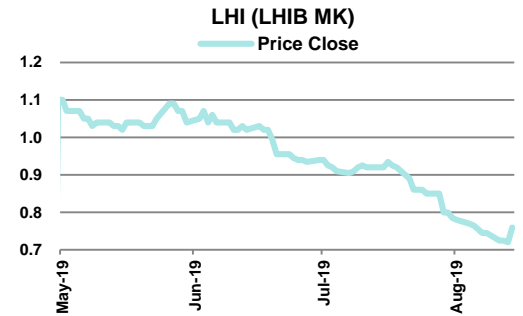
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Share Performance (%)

	YTD	1m	3m	6m	12m
Absolute	na	(17.4)	(26.2)	na	na
Relative	na	(14.5)	(24.5)	na	na
52-wk Price low/high (MYR)				0.72	1.19



Source: Bloomberg

Forecasts and Valuation	Dec-17	Dec-18	Dec-19F	Dec-20F	Dec-21F
Total turnover (MYRm)	5501	5747	6001	6502	7083
Net profit (MYRm)	185.0	219.0	201.2	252.2	295.5
Net profit growth (%)	(18.1)	18.4	(8.1)	25.3	17.2
Recurring EPS (MYR)	0.05	0.06	0.06	0.07	0.08
Recurring P/E (x)	15.0	12.7	13.8	11.0	9.4
P/B (x)	2.3	2.1	1.6	1.5	1.3
P/CF (x)	5.3	7.9	5.9	5.5	4.9
Dividend Yield (%)	1.4	2.1	2.2	2.7	3.2
EV/EBITDA (x)	8.3	7.9	7.4	6.6	6.0
Return on average equity (%)	15.4	17.6	13.3	14.0	14.8
Net debt to equity (%)	99.8	108.3	82.0	81.5	95.8

Source: Company data, RHB

Financial Exhibits

Asia		Financial summary	Dec-17	Dec-18	Dec-19F	Dec-20F	Dec-21F
Malaysia		Recurring EPS (MYR)	0.05	0.06	0.06	0.07	0.08
Consumer Poultry		DPS (MYR)	0.01	0.02	0.02	0.02	0.02
Leong Hup International		BVPS (MYR)	0.32	0.36	0.47	0.52	0.58
		ROE (%)	15.4	17.6	13.3	14.0	14.8
Major shareholders (%)		Valuation metrics	Dec-17	Dec-18	Dec-19F	Dec-20F	Dec-21F
Emerging Glory	52.80	Recurring P/E (x)	15.0	12.7	13.8	11.0	9.4
Lau Family	9.70	P/B (x)	2.3	2.1	1.6	1.5	1.3
Clarinden Investments	7.96	FCF Yield (%)	7.3	1.0	3.5	5.3	8.0
Valuation basis		Dividend yield (%)	1.4	2.1	2.2	2.7	3.2
Discounted Cash Flow (WACC: 5.6%, TG: 2.0%)		EV/EBITDA (x)	8.3	7.9	7.4	6.6	6.0
		EV/EBIT (x)	12.7	11.3	11.1	9.8	8.8
Key drivers		Income statement (MYRm)	Dec-17	Dec-18	Dec-19F	Dec-20F	Dec-21F
i. Regional expansion plan;		Total turnover	5,501	5,747	6,001	6,502	7,083
ii. Favourable product prices.		Gross profit	913	1,034	1,037	1,127	1,226
		EBITDA	583	655	681	783	882
Key risks		Depreciation and amortisation	(199)	(197)	(227)	(256)	(287)
i. Unfavourable change in regulatory policy;		Operating profit	384	457	455	527	596
ii. Unfavourable demand-supply dynamics.		Interest expenses	(103)	(92)	(109)	(113)	(113)
		Income from associates & JVs	0	1	1	1	1
Company Profile		Pre-tax profit	292	349	342	414	477
Leong Hup International is on one of the largest fully-integrated producers of poultry, eggs, and livestock feeds in South-East Asia.		Taxation	(45)	(102)	(75)	(91)	(105)
		Recurring net profit	185	219	201	252	296
		Cash flow (MYRm)	Dec-17	Dec-18	Dec-19F	Dec-20F	Dec-21F
		Change in working capital	11	(242)	(69)	(116)	(135)
		Cash flow from operations	524	349	471	505	566
		Capex	(368)	(423)	(450)	(450)	(450)
		Cash flow from investing activities	(367)	(379)	(450)	(450)	(450)
		Proceeds from issue of shares	-	-	275	-	-
		Dividend paid	(58)	(66)	(60)	(76)	(89)
		Cash flow from financing activities	(72)	(7)	(19)	(39)	(108)
		Cash at beginning of period	413	502	459	461	478
		Net change in cash	86	(36)	2	17	9
		Ending cash balance	502	459	461	478	486
		Balance sheet (MYRm)	Dec-17	Dec-18	Dec-19F	Dec-20F	Dec-21F
		Total cash and equivalents	502	459	461	478	486
		Tangible fixed assets	2,046	2,374	2,598	2,792	2,955
		Total investments	164	22	22	22	22
		Total assets	4,477	4,834	5,138	5,486	5,818
		Short-term debt	1,399	1,327	1,250	1,400	1,500
		Total long-term debt	742	1,044	1,000	1,000	1,000
		Total liabilities	2,835	3,069	2,957	3,129	3,254
		Total equity	1,186	1,302	1,718	1,894	2,101
		Net debt	1,638	1,912	1,789	1,922	2,014
		Total liabilities & equity	4477	4834	5138	5486	5818
		Key metrics	Dec-17	Dec-18	Dec-19F	Dec-20F	Dec-21F
		Revenue growth (%)	4.6	4.5	4.4	8.3	8.9
		Recurring EPS growth (%)	(18.1)	18.4	(8.1)	25.3	17.2
		Gross margin (%)	16.6	18.0	17.3	17.3	17.3
		Ebitda margin (%)	10.6	11.4	11.4	12.0	12.5
		Operating margin (%)	7.0	8.0	7.6	8.1	8.4
		Recurring net profit margin (%)	3.4	3.8	3.4	3.9	4.2
		Capex/sales (%)	6.7	7.4	7.5	6.9	6.4
		Interest cover (x)	4.2	4.2	4.0	4.7	5.0

Source: Company data, RHB

Results At a Glance

Figure 1: LHI's results review

FYE Dec (MYRm)	2Q18	1Q19	2Q19	QoQ (%)	YoY (%)	1H18	1H19	YoY (%)	Comments
Revenue	1,423.1	1,506.4	1,477.2	(1.9)	3.8	2,769.5	2,983.6	7.7	Driven mainly by robust sales in Indonesia and Vietnam
EBITDA	176.4	200.6	129.8	(35.3)	(26.4)	327.2	330.4	1.0	
<i>EBITDA margin (%)</i>	<i>12.4</i>	<i>13.3</i>	<i>8.8</i>	<i>(4.5)</i>	<i>(3.6)</i>	<i>11.8</i>	<i>11.1</i>	<i>(0.7)</i>	
EBIT	127.5	147.7	74.7	(49.4)	(41.4)	229.3	222.4	(3.0)	
<i>EBIT Margin (%)</i>	<i>9.0</i>	<i>9.8</i>	<i>5.1</i>	<i>(4.7)</i>	<i>(3.9)</i>	<i>8.3</i>	<i>7.5</i>	<i>(0.8)</i>	
Finance costs	(24.9)	(32.9)	(35.0)	6.5	40.6	(49.4)	(67.9)	37.4	
EI	9.7	0.0	2.1	nm	nm	9.7	2.1	nm	2Q18: write-off in value added tax receivables, 2Q19: share option expenses
Profit before tax	102.7	114.9	39.9	(65.3)	(61.2)	180.1	154.8	(14.1)	
<i>PBT Margin (%)</i>	<i>7.2</i>	<i>7.6</i>	<i>2.7</i>	<i>(4.9)</i>	<i>(4.5)</i>	<i>6.5</i>	<i>5.2</i>	<i>(1.3)</i>	
Tax expense	(27.9)	(24.6)	(13.3)	(46.0)	(52.4)	(44.3)	(37.9)	(14.5)	
<i>Effective tax rate (%)</i>	<i>(27.2)</i>	<i>(21.4)</i>	<i>(33.4)</i>	<i>(11.9)</i>	<i>(6.2)</i>	<i>(24.6)</i>	<i>(24.5)</i>	<i>0.1</i>	
Minority interests	(9.1)	(29.7)	(10.5)	nm	nm	(17.5)	(40.2)	nm	
PATAMI	65.7	60.6	16.1	(73.4)	(75.5)	118.3	76.7	(35.2)	
Core PATAMI	75.4	60.6	18.2	(70.0)	(75.9)	128.1	78.7	(38.5)	Broadly within expectations at 37-39% of forecasts.
<i>Net Margin (%)</i>	<i>5.3</i>	<i>4.0</i>	<i>1.2</i>	<i>(2.8)</i>	<i>(4.1)</i>	<i>4.6</i>	<i>2.6</i>	<i>(2.0)</i>	DPS of MYR0.016 was declared.

Source: Company data, RHB

Figure 2: LHI's geographical breakdown

FYE Dec (MYRm)	2Q18	1Q19	2Q19	QoQ (%)	YoY (%)	1H18	1H19	YoY (%)	Comments
Malaysia	426.5	442.2	368.0	(16.8)	(13.7)	820.8	810.3	(1.3)	Due to weak product prices
Singapore	256.1	193.3	191.1	(1.1)	(25.4)	527.5	384.5	(27.1)	Due to loss of revenue arising from disposal of subsidiary on 30 June 2018
Vietnam	269.1	293.2	335.2	14.3	24.6	518.5	628.4	21.2	Boosted by feedmill capacity expansion
Indonesia	453.1	563.4	563.9	0.1	24.5	873.5	1,127.3	29.1	Higher DOC and feedmill sales
Philippines	12.3	14.1	16.7	18.0	35.2	23.2	30.8	32.8	
Group revenue	1,423.1	1,506.4	1,477.2	(1.9)	3.8	2,769.5	2,983.6	7.7	
Malaysia	57.9	78.9	24.0	(69.6)	(58.6)	117.2	102.9	(12.2)	
Singapore	32.7	27.8	29.3	5.3	(10.6)	67.5	57.1	(15.4)	Base effect will wear off in 1H19
Vietnam	31.4	29.1	29.1	(0.2)	(7.4)	50.0	58.2	16.4	
Indonesia	53.5	63.1	45.8	(27.4)	(14.4)	89.5	108.9	21.6	
Philippines	0.9	1.7	1.7	0.2	92.7	3.1	3.5	13.4	
Group EBITDA	176.4	200.6	129.8	(35.3)	(26.4)	327.2	330.4	1.0	
Malaysia	13.6	17.8	6.5	(11.3)	(7.1)	14.3	12.7	(1.6)	
Singapore	12.8	14.4	15.3	0.9	2.5	12.8	14.8	2.1	
Vietnam	11.7	9.9	8.7	(1.3)	(3.0)	9.6	9.3	(0.4)	
Indonesia	11.8	11.2	8.1	(3.1)	(3.7)	10.2	9.7	(0.6)	
Philippines	7.3	12.2	10.4	(1.8)	3.1	13.2	11.2	(1.9)	
Group margin (%)	12.4	13.3	8.8	(4.5)	(3.6)	11.8	11.1	(0.8)	

Source: Company data, RHB

Figure 3: LHI's segmental breakdown

FYE Dec (MYRm)	2Q18	1Q19	2Q19	QoQ (%)	YoY (%)	1H18	1H19	YoY (%)	Comments
Livestock	910.7	859.7	803.7	-6.5	-11.8	1747.9	1663.3	-4.8	Mainly dragged down by loss of revenue arising from disposal of Singapore subsidiary Boosted by capacity expansion in Vietnam and higher volume in Indonesia
Feedmill	506.4	643.6	671.3	4.3	32.6	1013.1	1314.9	29.8	
Others	6.0	3.1	2.3	-26.2	-61.7	8.5	5.4	-36.6	
Group revenue	1423.1	1506.4	1477.2	-1.9	3.8	2769.5	2983.6	7.7	
Livestock	129.6	118.9	45.7	-61.6	-64.7	224.1	164.6	-26.5	Margin erosion due to drop in product prices in Malaysia
Feedmill	48.3	85.2	87.6	2.8	81.4	110.8	172.7	55.9	Capacity expansion continue to bear fruits
Others	-1.5	-3.5	-3.5	-1.1	129.8	-7.6	-6.9	-9.1	
Group EBITDA	176.4	200.6	129.8	-35.3	-26.4	327.2	330.4	1.0	
Livestock	14.2	13.8	5.7	-8.1	-8.5	12.8	9.9	-2.9	
Feedmill	9.5	13.2	13.0	-0.2	3.5	10.9	13.1	2.2	
Group margin (%)	12.4	13.3	8.8	-4.5	-3.6	11.8	11.1	-0.7	

Source: Company data, RHB

Buy:	Share price may exceed 10% over the next 12 months
Trading Buy:	Share price may exceed 15% over the next 3 months, however longer-term outlook remains uncertain
Neutral:	Share price may fall within the range of +/- 10% over the next 12 months
Take Profit:	Target price has been attained. Look to accumulate at lower levels
Sell:	Share price may fall by more than 10% over the next 12 months
Not Rated:	Stock is not within regular research coverage

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