

21 August 2014 | 3QFY14 Results Review

Kuala Lumpur Kepong

Higher CPO price squeezed manufacturing margin

Maintain NEUTRAL

Revised Target Price (TP): RM25.00
(from RM26.55)

INVESTMENT HIGHLIGHTS

- 3QFY14 earnings improved +13.0%yoy to RM213.7m while 9MFY14 earnings increased +24.4%yoy to RM821m.
- Nonetheless, the cumulative 9MFY14 earnings is lower than ours and consensus expectations, accounting for 61.3% and 67.3% of full year forecasts respectively.
- Plantation segment continued to record a commendable growth. However, the performance of property segment slid significantly.
- We are maintaining our NEUTRAL recommendation with a lower TP of RM25.00.

Decent performance. KLK's 3QFY14 revenue and earnings grew +34.4%yoy and +13.0%yoy to RM2.9b and RM213.7m respectively. This consequently brought the cumulative 9MFY14 revenue and earnings higher at RM8.4b and RM821.0m respectively. Nonetheless, the cumulative 9-month earnings is lower than ours and consensus expectations, accounting for 61.3% and 67.3% of full year forecasts respectively.

Upstream plantation business improved two folds. The increase in the Group's earnings was mainly attributable to significant improvement in its plantation segment, the upstream business in particular. The plantation profit increased +105%yoy to RM229.6m on the back of higher FFB production, favorable selling prices of palm products and also due to the reduction in production cost of CPO.

Weaker manufacturing segment in 3QFY14. Profit from manufacturing segment declined by a slight -0.1%yoy during 3QFY14 due to higher material prices. Additionally, higher processing cost resulted in lower profit margin. However, the cumulative 9-month segmental earnings of RM293.3m is still higher at +32.6%yoy as compared to that in the same period last year.

Unexciting property contribution. Unlike its plantation segment, earnings from KLK's property segment fell -54.8%yoy to RM10.4m in 3QFY14. This was mainly due to the decline in progressive recognition from the development of Bandar Seri Coalfields. Without any new property launches, we are expecting the property segment to continue to show decline in the coming quarter.

RETURN STATS

Price (20 August 2014)	RM23.86
Target Price	RM25.00
Expected Share Price Return	+4.78%
Expected Dividend Yield	+3.98%
Expected Total Return	+8.76%


STOCK INFO

KLCI	1878.99
Bursa / Bloomberg	2445/ KLK MK
Board / Sector	Main/ Plantation
Syariah Compliant	Yes
Issued shares (mil)	1,065.0m
Par Value (RM)	1.00
Market cap. (RM'm)	25,410.1
Price over NA	3.30x
52-wk price Range	RM20.60- RM25.28
Beta (against KLCI)	0.83
3-mth Avg Daily Vol	0.72m
3-mth Avg Daily Value	RM17.26m
Major Shareholders	
Batu Kawan	46.6%
EPF	14.02%
Blackrock	2.33%

Key terms:

FFB – Fresh fruit bunches
CPO – Crude palm oil
PK – Palm Kernel

Earnings forecasts adjusted due to weaker price outlook. We are revising KLK's earnings forecasts for FY14 and FY15 downwards by -7.3% and -5.6% respectively pursuant to (i) the reduction in our average CPO price assumptions for 2014 and 2015 in our report dated 6 August 2014, and (ii) after taking into consideration of lower manufacturing margin due to the increase in processing cost which is higher than our earlier expectation.

Maintain NEUTRAL. Against this backdrop, we do not foresee a significant upside price potential in the next 12 months. Hence, we reiterate our NEUTRAL recommendation on KLK with revised TP of RM25.00, derived from sum-of-parts valuation. 

INVESTMENTS STATISTICS

FYE 31 SEPT	FY11	FY12	FY13	FY14F	FY15F
Revenue (RM'm)	10,743.25	10,570.19	9,147.33	10,400.26	11,132.87
EBIT (RM'm)	2,112.67	1,882.10	1,267.20	1,768.13	2,009.15
Pre-tax Profit (RM'm)	2,066.21	1,560.44	1,199.77	1,679.72	1,908.70
Net Profit (RM'm)	1,571.41	1,211.24	917.74	1,241.65	1,410.91
EPS (sen)	147.56	113.74	86.20	116.59	132.48
EPS growth	55.23%	-22.92%	-24.21%	35.26%	13.63%
PER(x)	16.17	20.98	27.68	20.46	18.01
Dividend (sen)	85.00	65.00	35.00	85.00	95.00
Net Dividend Yield (%)	3.56	2.72	1.47	3.56	3.98

Source: Company, Forecast by MIDFR

SUM-OF-PART VALUATION

Division	FY15F Earnings	PE multiple (x)	Fair Value (RM)
Plantation	1,368.6	20.0	27,385.31
Property	42.3	9.0	380.95
Less Net Debt			-1,139.03
Total Fair Value			26,627.23
No of Shares			1,065.00
Fair Value/ Share			25.00

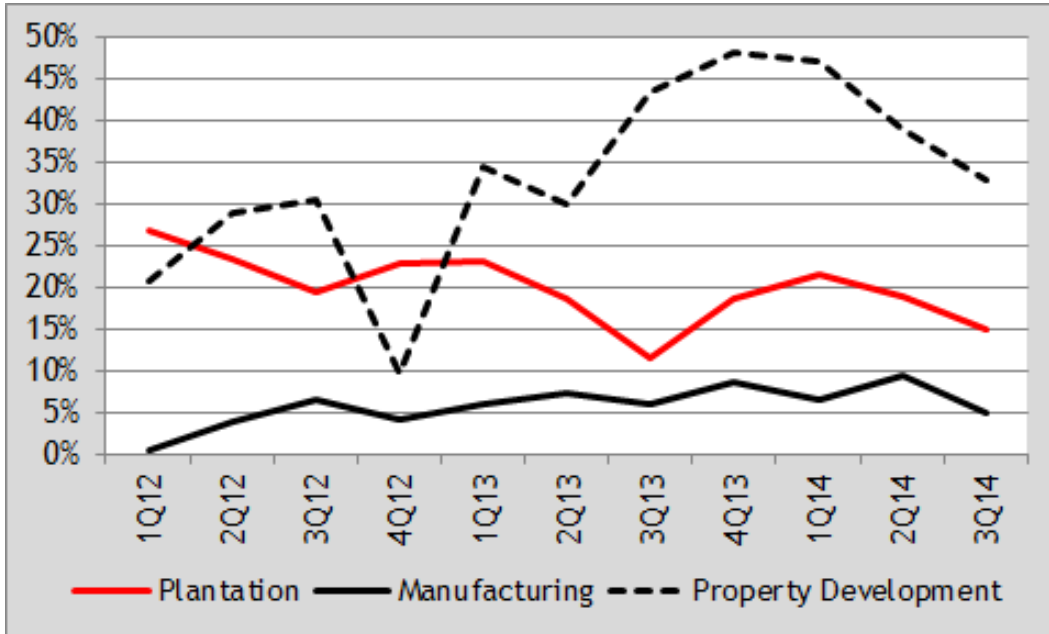
Source: MIDFR

KLK 3QFY14 RESULT SUMMARY

FYE Sep (RM m)	Quarterly Results			Cumulative		Comments
	3Q14	YoY	QoQ	9MFY14	YoY	
Revenue	2,923.64	34.4%	-0.4%	8,351.83	24.1%	Favorable selling prices of palm products
Gross Profit	285.67	35.8%	-34.4%	1,075.3	26.4%	
Finance Costs	(22.64)	-64.2%	15.4%	(63.3)	1.5%	
Pre-tax profit	276.93	21.0%	-34.8%	1,079.1	24.5%	
Tax	(58.62)	94.5%	-32.8%	(221.2)	29.7%	
Net Profit	213.66	13.0%	-32.1%	821.0	24.4%	Improved due to lower production cost
EPS (sen)	20.10	12.9%	-31.9%	77.1	24.6%	
		+/- pts	+/- pts		+/- pts	
Operating margin	7.31%	-1.38	-3.41	9.83%	0.03	
Tax rate	21.17%	8.00	0.60	20.50%	0.83	
Segmental						
<u>Revenue:</u>						
Plantation	1,532.02	58.3%	0.4%	4,253.92	34.4%	FFB production had increased slightly
Manufacturing	1,456.82	24.5%	-2.5%	4,219.89	22.2%	Higher sales volume as well as selling prices
Property Development	31.75	-40.3%	48.2%	80.61	-49.5%	Lower profit recognition from Bandar Seri Coalfield's project
Investment Holdings	52.58	56.1%	76.1%	155.33	49.2%	
<u>Operating Profit:</u>						
Plantation	229.6	105.0%	-20.5%	774.5	35.1%	
Manufacturing	70.8	-0.1%	-49.6%	293.3	32.6%	
Property Development	10.4	-54.8%	25.0%	31.6	-44.8%	
Investment Holdings	9.3	-31.7%	115.6%	36.8	-12.3%	
<u>Operating margin:</u>		+/- pts	+/- pts		+/- pts	
Plantation	14.99%	3.41	-3.94	18.21%	0.10	
Manufacturing	4.86%	-1.20	-4.54	6.95%	0.54	
Property Development	32.81%	-10.50	-6.08	39.26%	3.37	
Investment Holdings	17.68%	-22.70	3.24	23.69%	-16.60	

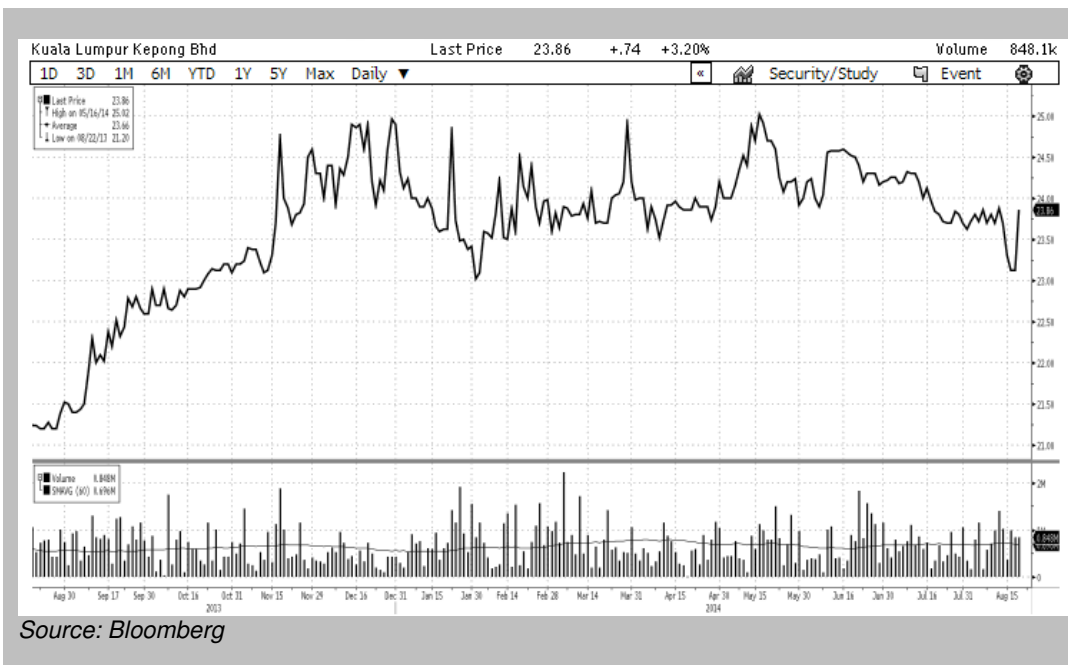
Source: Company, MIDFR

Figure 1: The operating profit margin of KLK's business segments



Margin from property segment declining as lower profit recognized from its development projects

DAILY PRICE CHART



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MIDF AMANAH INVESTMENT BANK : GUIDE TO RECOMMENDATIONS

STOCK RECOMMENDATIONS

BUY	Total return is expected to be >15% over the next 12 months.
TRADING BUY	Stock price is expected to <i>rise</i> by >15% within 3-months after a Trading Buy rating has been assigned due to positive newsflow.
NEUTRAL	Total return is expected to be between -15% and +15% over the next 12 months.
SELL	Total return is expected to be <15% over the next 12 months.
TRADING SELL	Stock price is expected to <i>fall</i> by >15% 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.