ESG Grading Band ★

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Leong Hup International Berhad

Maintain **BUY**

(6633 | LHIB MK) Main | Consumer Products & Services| Agricultural Products

Resilient Demand

***Revised* Target Price: RM0.90**
(Previously RM1.05)

KEY INVESTMENT HIGHLIGHTS

- **Greater external sales of feedmill segment in 3QFY23**
- **Stronger sales volume for broiler chicken and eggs in 3QFY23**
- **Lower 3QFY23 COGS**
- **Margin outlook ahead**
- **Revised Earnings Projections for FY23-25F**
- **Maintain BUY with a revised TP of RM0.90(from RM1.05)**

We recently attended Leong Hup's analyst briefing for 3QFY23 and remain optimistic about its FY24F outlook. The key highlights are as follows:

Greater external sales of feedmill segment in 3QFY23. The group's utilization rate rose by +1.8ppt yoy to 65.9%, despite a higher total production capacity of +3.2%yoy to 1,085.8k mt. As such, the sales volume of feed for both internal and external sales increased by +3.9%yoy to 696.2k mt, with external sales contributed 64% of total sales in 3QFY23 (vs. 58% in 3QFY22). This suggests a stronger demand for feed during the quarter, driven by external players that expect increased demand for poultry products and higher production.

Stronger sales volume for broiler chicken and eggs in 3QFY23. The group reported a +13.4%yoy growth in the volume supplied of group broiler chicken to 43.1m birds. Similarly, the group's egg volume supplied rose by +13.4%yoy to 502.5m eggs, accompanied by a higher average selling prices (due to the sales mix favoring more premium eggs in Malaysia and higher selling prices in foreign operations) in 3QFY23. Meanwhile, the group's broiler DOC volume supplied decreased by -2.6%yoy to 141.1m chicks in 3QFY23, but this was offset by higher average selling prices of DOC in Malaysia and Indonesia.

Lower 3QFY23 COGS. The group's COGS decreased from RM1.8b in 3QFY22 to RM1.77b in 3QFY23, primarily due to lower feedstock input costs. This mirrors the global downward trend in corn and soybean meal prices from its all-time high in Feb/Mar 2023, though remained higher than FY19 levels. Overall, the global corn price continued on a decreasing trajectory, which could potentially offset the recent slight rebound in global soybean meal prices in mid-October 2023. Recall that corn is the biggest contributor to animal feed costs at 55-69%, followed by soybean meal at 19-32%. Looking forward, we cautiously anticipate a continued decrease in feed input costs, to below FY21 levels. However, we expect these costs to likely remain above FY19 levels in the near term.

Higher staff benefit in 3QFY23. In 3QFY23, LHI recruited more staff to support business expansion, leading to a +15.7%yoy increase in staff benefit costs to RM204.1m.

RETURN STATISTICS	
Price @ 28th Nov 2023 (RM)	0.68
Expected share price return (%)	+30.0
Expected dividend yield (%)	5.9
Expected total return (%)	**+35.9**

SHARE PRICE CHART

Price performance (%)	Absolute	Relative
1 month	7.1	6.8
3 months	23.6	29.0
12 months	40.2	43.2

INVESTMENT STATISTICS

FYE Dec	2023F	2024F	2025F
Revenue	9,685.0	9,967.6	10,241.2
EBITDA	**952.9**	**944.2**	**966.3**
Profit before tax (PBT)	516.7	519.7	559.0
Core PATANCI	**336.8**	**389.8**	**419.2**
Core EPS (sen)	9.2	10.7	11.5
DPS (sen)	4.0	4.1	4.4
Dividend Yield (%)	5.8	5.9	6.3

KEY STATISTICS	
FBM KLCI	1,446.07
Issue shares (m)	3650.00
Estimated free float (%)	15.84
Market Capitalisation (RM'm)	2,482.00
52-wk price range	RM0.4-RM0.73
3-mth average daily volume (m)	3.94
3-mth average daily value (RM'm)	2.47
Top Shareholders (%)	
Emerging Glory Sdn Bhd	52.80
CLARINDEN INV PTE	8.08
Amanah Saham Nasional Bhd	7.07

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Margin outlook ahead. The group reported an operating profit margin of 10.7% in 3QFY23 (+4.9ppt yoy; +4.1ppt qoq), primarily attributed to (1) greater sales of high-margin products at a higher selling price, (2) lower feedstock input costs, and (3) economies of scale. However, we consider the 3QFY23 margin extraordinary and may normalize in 4QFY23 and FY24, given the poultry industry's vulnerability to market-driven supply and demand dynamics.

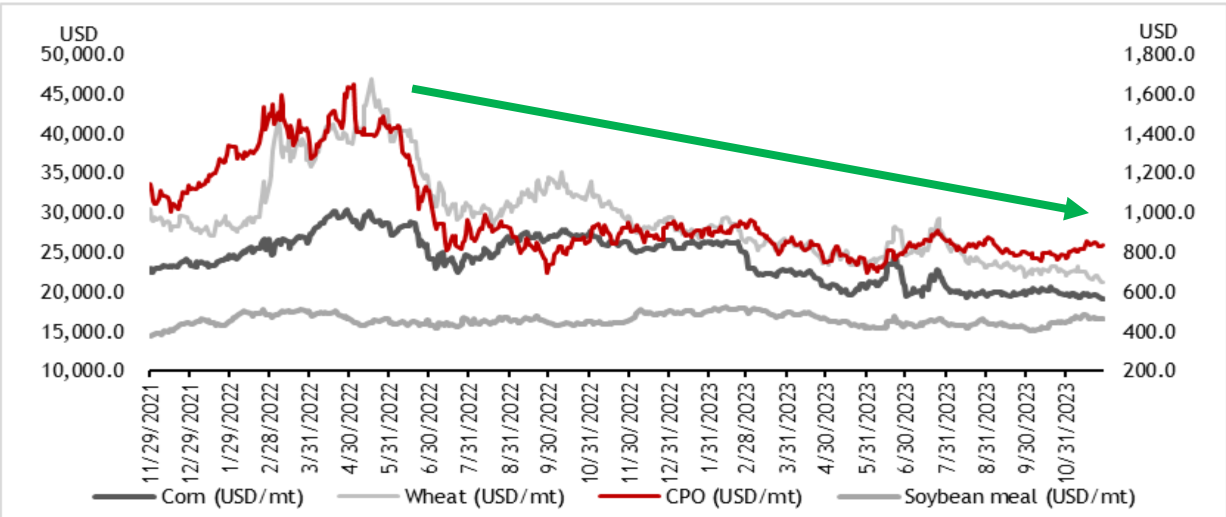
In particular, we gather that the recession fears in European countries have led to permanent or temporary shutdowns of factories in Vietnam, resulting in job losses and decreased demand for poultry products. In Malaysia, the removal of chicken subsidies has not fully translated to higher selling prices for live birds, primarily due to reduced local demand.

On a positive note, we expect a better margin in 4QFY23 as compared to 2QFY23 (rather than to the extraordinary 3QFY23 margin). This is primarily attributed to the anticipation of a greater ability to offer higher selling prices for DOC in Malaysia and Indonesia, driven by shortages of great-grandparent DOCs that are not expected to normalize for at least the next two years. Additionally, the decline in feed input prices for corn and soybean from the peak levels in Feb/Mar is expected to persist, keeping costs relatively lower for 4QFY23 onward compared to 2Q and 1QFY23

Revised Earnings Projections for FY23-25F. Post analyst briefing, we revised our earnings projections for FY23-25F down by -13.6%/-17.2%/-23.2% respectively. This adjustment was made after considering (1) a slight decrease in demand from Vietnam, influenced by multiple headwinds that more than offset tighter supplies, (2) normalization of the gross profit margin to FY21 levels, attributed to the decline in global commodities from their two-year peak, 3) anticipated higher labor costs due to the expectation of an increased workforce following business expansion, and (4) higher capital expenditures aligning with the group's guidance of RM250-300m for FY23-24.

Maintain BUY with a revised TP of RM0.90 (from RM1.05). Our revised **TP** is based on a PER of 8.4x (5-year historical -1SD PER) pegged to a revised FY24F EPS of 10.68sen (from 12.90sen). Despite facing multiple headwinds, we are positive about Leong Hup's FY24F outlook, underpinned by (1) the staple food nature of its product, indicating resilient demand, (2) the normalization of margins in its Malaysian operations due to the removal of price controls for chicken, and (3) the global softening of commodity prices for chicken feed, thereby improving the margin for the livestock segment. We are also optimistic about a more favorable operating environment in Indonesia, where supplies have normalized following government initiatives to manage market demand and supply, allowing the company to increase selling prices with better margins. Also, given the persistent shortage of day-old chicks (DOC) and eggs worldwide, we believe that LHI is well-positioned to meet unmet demand, thanks to its strong regional production capacity. Hence, we maintain our **BUY** call on Leong Hup. **Downside risks** include (1) significant raw material cost increases, (2) adverse regulatory changes like price controls or culling programs, (3) shortages of great-grandparent DOC, and (4) disease outbreaks.

Chart 1: Raw Material Futures Price Trend for Chicken Feed (USD/mt)



Sources: MIDFR

FINANCIAL SUMMARY

Income Statement (RM'm)	2021A	2022A	2023F	2024F	2025F
Revenue	**7,153.5**	**9,042.7**	**9,685.0**	**9,967.6**	**10,241.2**
Change in biological assets	42.8	7.9	73.9	(0.8)	11.0
Change in closing inventories	228.6	29.6	60.0	(1.8)	24.2
Purchase of inventories and livestock	(5,514.4)	(6,865.4)	(7,205.9)	(7,193.8)	(7,354.2)
Gross Profit	**1,910.5**	**2,214.8**	**2,613.0**	**2,771.2**	**2,922.1**
Other Income	39.1	188.8	151.7	36.2	37.2
Employee benefit costs including Directors' remuneration	(645.8)	(677.4)	(715.1)	(740.3)	(792.9)
Utilities costs	(185.6)	(221.4)	(284.5)	(291.4)	(309.8)
Repair and maintenance	(80.0)	(91.2)	(118.1)	(121.6)	(124.9)
Transportation expenses	(149.9)	(181.4)	(196.2)	(208.0)	(252.2)
Other operating expenses	(366.7)	(467.0)	(497.7)	(501.9)	(513.1)
EBIT	**237.9**	**464.0**	**675.5**	**663.9**	**683.3**
Profit before tax (PBT)	**140.3**	**326.6**	**516.7**	**519.7**	**559.0**
Profit After tax (PAT)	95.9	243.9	387.5	389.8	419.2
Core PATANCI	**88.2**	**240.6**	**336.8**	**389.8**	**419.2**
Core EPS (sen)	2.4	6.6	9.2	10.7	11.5
DPS (sen)	0.7	1.8	4.0	4.1	4.4

Balance Sheet (RM'm)	2021A	2022A	2023F	2024F	2025F
Property, plant and equipment	2,770.3	2,784.5	2,759.6	2,699.6	2,636.9
Total Non-current assets	**3,411.2**	**3,431.8**	**3,404.5**	**3,349.3**	**3,291.1**
Inventories	973.5	1,025.9	1,085.8	1,084.0	1,108.2
ST - Trade and other receivables	740.1	823.2	928.7	955.8	982.0
Cash and cash equivalents	764.6	840.3	810.0	825.3	839.4
Total current assets	**2,918.6**	**3,160.4**	**3,373.2**	**3,414.5**	**3,491.7**
Total Assets	**6,329.8**	**6,592.2**	**6,777.7**	**6,763.9**	**6,782.7**
Total Equity	**2,359.8**	**2,589.6**	**3,009.0**	**3,125.2**	**3,252.4**
LT Loans and borrowings	1,054.6	1,046.4	943.5	896.3	851.5
Total Non-current liabilities	**1,321.4**	**1,339.5**	**1,255.1**	**1,216.3**	**1,179.5**
ST Trade and other payables	534.7	629.8	631.8	630.7	644.8
ST Loans and borrowings	2,070.1	1,986.3	1,831.5	1,739.9	1,652.9
Total Current Liabilities	**2,648.5**	**2,663.1**	**2,513.6**	**2,422.4**	**2,350.8**
Total Liabilities	**3,970.0**	**4,002.6**	**3,768.7**	**3,638.6**	**3,530.3**

Cash Flow (RM'm)	2021A	2022A	2023F	2024F	2025F
Pretax profit	140.3	326.6	516.7	519.7	559.0
Cash flow from operations	44.2	620.9	1,119.0	711.6	694.9
Cash flow from investing	(392.6)	(277.6)	(286.7)	(257.8)	(258.0)
Cash flow from financing	264.3	(362.1)	(578.4)	(438.5)	(422.7)
Net cash flow	**(84.1)**	**(18.8)**	**253.9**	**15.3**	**14.2**
(+/-) Adjustments	13.4	(0.3)	0.0	0.0	0.0
Net cash/(debt) b/f	**645.8**	**575.1**	**556.1**	**810.0**	**825.3**
Net cash/(debt) c/f	**575.1**	**556.1**	**810.0**	**825.3**	**839.4**

Key Metrics	2021A	2022A	2023F	2024F	2025F
Effective tax rate (%)	31.7	25.3	25.0	25.0	25.0
PER (x)	29.5	11.5	6.5	6.5	6.0
Net debt/total equity (%)	1.0	0.8	0.7	0.6	0.5

Profitability Margins	2021A	2022A	2023F	2024F	2025F
Gross Profit Margin (%)	26.7	24.5	27.0	27.8	28.5
EBIT Margin (%)	3.3	5.1	7.0	6.7	6.7
Core PATANCI Margin (%)	1.2	2.7	3.5	3.9	4.1

Source: Bloomberg, MIDFR

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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 *rise* 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 *fall* 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.
ESG RECOMMENDATIONS* - source Bursa Malaysia and FTSE Russell	
☆☆☆☆	Top 25% by ESG Ratings amongst PLCs in FBM EMAS that have been assessed by FTSE Russell
☆☆☆	Top 26-50% by ESG Ratings amongst PLCs in FBM EMAS that have been assessed by FTSE Russell
☆☆	Top 51%- 75% by ESG Ratings amongst PLCs in FBM EMAS that have been assessed by FTSE Russell
☆	Bottom 25% by ESG Ratings amongst PLCs in FBM EMAS that have been assessed by FTSE Russell

* ESG Ratings of PLCs in FBM EMAS that have been assessed by FTSE Russell in accordance with FTSE Russell ESG Ratings Methodology