Leong Hup International Berhad

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

A Bright Horizons Ahead

***Upgrade to* BUY**

(Previously Neutral)

***Revised* Target Price: RM0.80**

(Previously RM0.50)

KEY INVESTMENT HIGHLIGHTS

- **Improving Malaysian operations as government lifted price control on chicken**
- **Expect higher broiler chicken ASP in Vietnam in the near future**
- **Upbeat outlook for Indonesia segment in 2HFY23**
- **Raised earnings revision for FY23-25F and changed valuation**
- **Upgrade to BUY (from Neutral) with a higher TP of RM0.80 (from RM0.50)**

Improving Malaysian operations as government lifted price control on chicken. Price controls and subsidies on chicken were lifted on 1st November 2023. Meanwhile, price controls and subsidies on eggs remain. We believe that this is positive for operation of Leong Hup International ("LHI") in Malaysia from 4QFY23 onward as LHI has more flexibility to adjust prices in response to input costs as well as supply and demand in the market. Note that 26% of LHI total FY22 revenue was contributed by Malaysian operation. Despite the previous government subsidies supporting margin, we note that there was a delay for LHI to receive the government subsidies. With the lifting of price control of chicken, we believe LHI should have normalized margin going forward as LHI can adjust price of chicken swiftly in responding to the changes in input costs. Recall that the government subsidies for chicken was RM0.80 per kg (up to 1.8kg).

Expect higher broiler chicken ASP in Vietnam in the near future. Looking ahead, we anticipate improved dynamics for LHI's Vietnam operations from 2HFY23 onward. This is primarily attributed to the exit of smaller players as a result of rising operational costs. Additionally, we expect higher Average Selling Price (ASP) for broiler chicken ahead, due to tight supplies caused by the severe H5N1 avian flu outbreak in Vietnam. Based on our channel checks, the outbreak of H5N1 avian flu has forced affected poultry farms to cull which led to tight supplies. Besides, the growing demand for poultry products which fueled by return of tourists after the border reopening also provides further room to raise ASP. Hence, we are optimistic that positive Vietnam operations will improve revenue and earnings, given that it contributed to 24.5% of the total FY22 revenue

RETURN STATISTICS	
Price @ 23rd Nov 2023 (RM)	0.705
Expected share price return (%)	11.72
Expected dividend yield (%)	2.81
Expected total return (%)	**14.53**

SHARE PRICE CHART

Price performance (%)	Absolute	Relative
1 month	16.5	15.3
3 months	28.2	31.8
12 months	51.6	50.6

INVESTMENT STATISTICS

FYE Dec	2023F	2024F	2025F
Revenue	9,511.3	9,872.6	10,151.5
EBITDA	**767.3**	**838.6**	**929.4**
Profit before tax (PBT)	323.1	374.2	415.8
Core PATANCI	**201.8**	**239.6**	**270.3**
Core EPS (sen)	5.5	6.6	7.4
DPS (sen)	2.0	2.3	2.6
Dividend Yield (%)	2.8	3.3	3.6

KEY STATISTICS	
FBM KLCI	1,453.29
Issue shares (m)	3650.00
Estimated free float (%)	15.79
Market Capitalisation (RM'm)	2,573.25
52-wk price range	RM0.45-RM0.73
3-mth average daily volume (m)	3.53
3-mth average daily value (RM'm)	2.16
Top Shareholders (%)	
Emerging Glory Sdn Bhd	52.80
CLARINDEN INV PTE	8.14
Amanah Saham Nasional Bhd	7.07

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Upbeat outlook for Indonesia segment in 2HFY23. The feedmill business in Indonesia is expected to remain relatively stable in 2HFY23, given its cost-plus contract as well as the limited feedmill suppliers in Indonesia. We gather that 60% of the market share for feedmills in Indonesia is dominated by the three largest poultry players, which are Charoen Pokphand Indonesia, Japfa TBK, and PT Malindo (Leong Hup operates via PT Malindo in Indonesia). Meanwhile, we expect performance of the livestock segment to improve in 2HFY23 following the government's initiatives to manage the market demand and supply of DOC via facilitating supply adjustments in 1HFY23. Hence, we expect ASP prices to stabilize. Recall that the prolonged demand and supply imbalance in DOCs and broilers since 2022 has resulted in weak poultry prices. Overall, the growth in the Indonesia segment will benefit Leong Hup, given that it contributed 36.4% total revenue in FY22.

Expect further reductions in the cost of raw materials as global commodity prices soften. The average global corn and soybean meal prices for October 2023 decreased by -2.3%yoy and -26.1%yoy. The prices of the two raw materials also dropped significantly from their 2-year peak level in October 2023. Given that corn and soybean meal accounted for 70–80% of the total raw material costs for animal feed, the declining prices of these commodities globally may signal reduction in raw material costs in 2HFY23, which will improve the profit margin. This could more than offset the fluctuations in the USD/MYR exchange rate as most commodities are purchased in USD.

Raised earnings revision for FY23-25F and changed valuation to the 3-year historical -0.5SD of 12x. We raised our earnings projections for FY23F-25F by 10.1%/9.8%/2.7%, respectively. This was after factoring in (1) higher revenue in the Malaysia, Indonesia and Vietnam operations, and (2) slightly lower raw material costs due to the falling global corn and soybean meal prices that more than offset the USD/MYR exchange rate. We also changed our valuation from the 3-year historical -1SD of 8.3x to the 3-year historical -0.5SD of 12x. This was after considering the positive outlook for the 3 segments mentioned above, which more than offset the ongoing price controls for eggs in Malaysia in the near term.

Upgrade to BUY (from NEUTRAL) with a higher TP of RM0.80 (from RM0.50). Our revised TP is based on an FY24F PER of 12x (-0.5SD 3-year historical PE) pegged to a revised FY24F EPS of 6.6sen (up from 6.0sen). We turned positive on the margin improvement for LHI Malaysia operation ahead, driven by the removal of price controls on chicken and the softening of global commodity prices for chicken feed. This allows the group flexibility to adjust market prices based on market supply and demand, as well as input costs. Besides, the improving operational outlook in Vietnam and Indonesia will also further improve revenue and earnings. We are also optimistic that the Singapore operation will continue to thrive in FY2024 following the removal of the export ban on broiler chicken from Malaysia to Singapore. Hence, we upgrade our call to **BUY** from NEUTRAL**. Downside risks** include (1) a substantial increase in raw material costs and (2) adverse regulatory changes, such as price controls or culling programs.

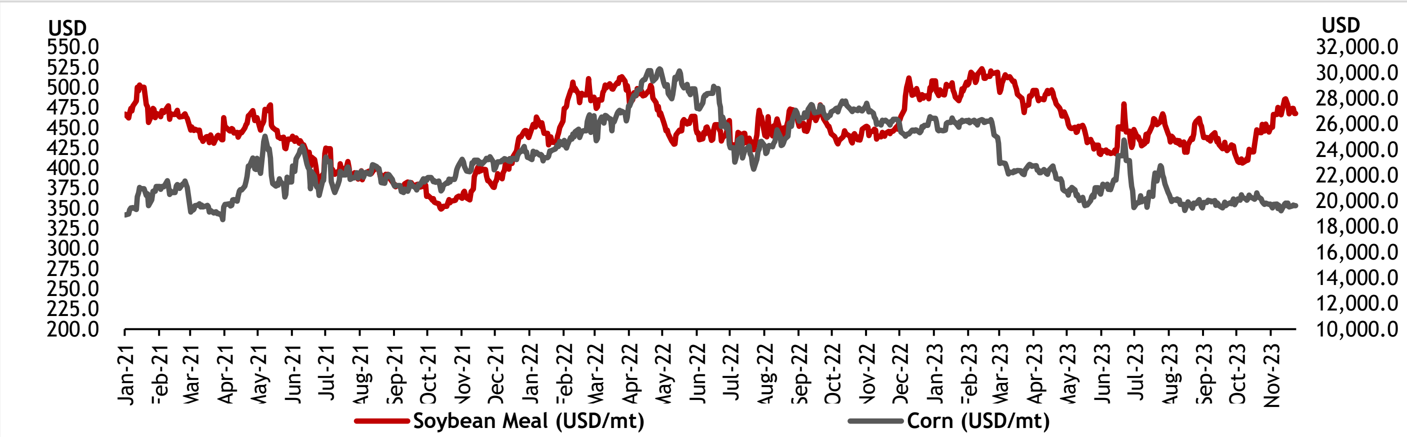
Table 1: Malaysia's Average Chicken Prices by State.

	Sept 2023	22 Nov 2023	chg (%)
Sabah	12.39	12.65	2.10
Sarawak	12.12	12.00	(0.99)
Labuan	11.30	12.00	6.19
Pahang	9.68	9.25	(4.44)
Selangor	9.51	9.20	(3.26)
Terengganu	9.39	8.85	(5.75)
Perak	9.32	8.89	(4.61)
Melaka	9.29	8.63	(7.10)
Negeri Sembilan	9.24	9.07	(1.84)
Perlis	9.19	8.82	(4.03)
Kedah	9.16	9.14	(0.22)
Kuala Lumpur	9.13	8.62	(5.59)
Pulau Pinang	9.11	8.87	(2.63)
Johor	9.05	8.80	(2.76)
Kelantan	8.98	8.76	(2.45)
Putrajaya	8.67	8.86	2.19

Sources: MIDFR, DOSM

***Note: Sabah, Sarawak, and Labuan are not subject to standard retail price ceilings, as price ceilings vary across cities.*

Chart 5: Raw Material Futures Price Trend for Poultry Producer (USD/mt)



Sources: MIDFR

FINANCIAL SUMMARY

Income Statement (RM'm)	2021A	2022A	2023F	2024F	2025F
Revenue	**7,153.5**	**9,042.7**	**9,511.3**	**9,872.6**	**10,151.5**
Change in biological assets	42.8	7.9	8.6	9.2	9.9
Change in closing inventories	228.6	29.6	32.1	34.3	37.0
Purchase of inventories and livestock	(5,514.4)	(6,865.4)	(7,084.0)	(7,253.8)	(7,324.4)
Gross Profit	**1,910.5**	**2,214.8**	**2,468.0**	**2,662.3**	**2,874.0**
Other Income	39.1	188.8	88.5	91.8	94.4
Employee benefit costs including Directors' remuneration	(645.8)	(677.4)	(729.1)	(769.7)	(820.6)
Utilities costs	(185.6)	(221.4)	(260.8)	(284.2)	(306.9)
Repair and maintenance	(80.0)	(91.2)	(103.7)	(113.0)	(119.6)
Transportation expenses	(149.9)	(181.4)	(194.6)	(218.2)	(235.5)
Other operating expenses	(366.7)	(467.0)	(501.0)	(530.5)	(556.3)
EBIT	**237.9**	**464.0**	**491.5**	**546.0**	**596.3**
Profit before tax (PBT)	**140.3**	**326.6**	**323.1**	**374.2**	**415.8**
Profit After tax (PAT)	95.9	243.9	241.3	279.5	310.5
Core PATANCI	**88.2**	**218.9**	**201.8**	**239.6**	**270.3**
Core EPS (sen)	2.4	6.0	5.5	6.6	7.4
DPS (sen)	0.7	1.8	2.0	2.3	2.6

Balance Sheet (RM'm)	2021A	2022A	2023F	2024F	2025F
Property, plant and equipment	2,770.3	2,784.5	2,671.1	2,578.8	2,496.0
Total Non-current assets	**3,411.2**	**3,431.8**	**3,332.4**	**3,254.2**	**3,168.6**
Inventories	973.5	1,025.9	1,169.8	1,188.4	1,169.0
ST - Trade and other receivables	740.1	823.2	932.6	963.5	970.9
Cash and cash equivalents	764.6	840.3	839.6	862.8	878.3
Total current assets	**2,918.6**	**3,160.4**	**3,516.5**	**3,574.9**	**3,574.6**
Total Assets	**6,329.8**	**6,592.2**	**6,848.9**	**6,829.1**	**6,743.2**
Total Equity	**2,359.8**	**2,589.6**	**2,833.9**	**2,758.0**	**2,506.0**
LT Loans and borrowings	1,054.6	1,046.4	1,015.0	1,035.3	1,087.1
Total Non-current liabilities	**1,321.4**	**1,339.5**	**1,321.9**	**1,352.9**	**1,413.1**
ST Trade and other payables	534.7	629.8	717.0	701.6	707.8
ST Loans and borrowings	2,070.1	1,986.3	1,926.7	1,965.2	2,063.5
Total Current Liabilities	**2,648.5**	**2,663.1**	**2,693.2**	**2,718.1**	**2,824.1**
Total Liabilities	**3,970.0**	**4,002.6**	**4,015.1**	**4,071.1**	**4,237.2**

Cash Flow (RM'm)	2021A	2022A	2023F	2024F	2025F
Pretax profit	140.3	326.6	323.1	374.2	415.8
Cash flow from operations	44.2	620.9	822.7	466.6	434.4
Cash flow from investing	(392.6)	(277.6)	(195.9)	(237.3)	(287.6)
Cash flow from financing	264.3	(362.1)	(343.1)	(206.1)	(131.3)
Net cash flow	**(84.1)**	**(18.8)**	**283.6**	**23.2**	**15.5**
(+/-) Adjustments	13.4	(0.3)	0.0	0.0	0.0
Net cash/(debt) b/f	**645.8**	**575.1**	**556.1**	**839.6**	**862.8**
Net cash/(debt) c/f	**575.1**	**556.1**	**839.6**	**862.8**	**878.3**

Key Metrics	2021A	2022A	2023F	2024F	2025F
Effective tax rate (%)	31.7	25.3	25.3	25.3	25.3
PER (x)	30.1	11.8	10.7	9.2	8.3
Net debt/total equity (%)	1.0	0.8	0.7	0.8	0.9

Profitability Margins	2021A	2022A	2023F	2024F	2025F
Gross Profit Margin (%)	26.7	24.5	25.9	27.0	28.3
EBIT Margin (%)	3.3	5.1	5.2	5.5	5.9
Core PATANCI Margin (%)	1.2	2.4	2.1	2.4	2.7

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