

PP14767/09/2012(030761)

Thursday, May 21, 2015

Kuala Lumpur Kepong

“A Challenging Year”

Results Review

- Actual vs. expectations.** Kuala Lumpur Kepong Berhad (KLK) 1H15 earnings performance was slightly below our estimates although revenue actually increased by 14% y-o-y to RM6.18 billion from RM5.43 billion in 1H14. Y-o-y, earnings slipped by 28% to RM437 million dragged by weaker-than-expected EBIT contribution from both the plantation and manufacturing division which fell by 26% y-o-y and 53% y-o-y respectively, weighed by 1) lower CPO, PK and rubber selling prices; 2) drop in FFB and rubber production; 3) higher production cost of CPO; and 4) lower margins from the downstream business.
- Dividend.** The Board has proposed an interim single tier dividend of 15sen per share for the financial year ended September 2015 that will be paid on 11th August 2015, bringing total dividend to-date of 15sen per share (2013: 15sen).
- Plantation division.** Plantation division segment profit shrunk 27% y-o-y to RM400 million compared to RM545 million in 1H14, as margin decreased by 8pps to 12% (1H14: 20%), in line with the deceleration in CPO price. The unsatisfactory performance has been expected on account of lower average commodity selling price as its average CPO price realised decreased by 5% to RM2,170/MT (1H14: RM2,392/MT), while average rubber price realised declined by 20% to RM6.75/Kg (1H14: RM8.49/Kg). This was also aided by the decrease in FFB and rubber production as well as higher CPO production cost during the quarter. FFB and CPO production dropped by 4% and 1% y-o-y respectively to 1.78 million MT and 405,932 MT, made worse by the decline in rubber production by 10% y-o-y to 7.76 million kg (1H14: 8.61 million kg).

HOLD (TP: RM21.50)

Current Price (RM)	RM22.40
New Target Price (RM)	RM21.50
Previous Target Price (RM)	RM21.50
Previous Recommend.	HOLD
Upside To Target Price	-4.0%
Dividend Yield (FY15F)	2.7%

Stock Code

Bloomberg	KLK MK
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Stock & Market Data

Listing	MAIN MARKET	
Sector	Plantation	
Shariah Compliance	Yes	
Issued Shares (mn)	1,065.0	
Market Cap (RM mn)	23,855.2	
YTD Chg In Share Price	1.75%	
Beta (x)	1.13	
52-week Hi/Lo (RM)	RM25.14	RM19.60
3M Average Volume ('000shrs)	521.6mn	
Estimated Free Float	22%	

Major Shareholders

Batu Kawan	46.57%
EPF	13.63%
ASB	5.80%

- Manufacturing sector.** The manufacturing sector revenue improved 6% to RM2.93 billion in 1H15 from RM2.76 billion in 1H14. However, the segment profit slumped by 58% to RM91.8 million against RM217.7 million in 1H14 led by lower profit from oleo-chemicals and other manufacturing sub-segments that had tanked 59.5% and 5.79% y-o-y respectively to RM85.3 million and RM6.5 million respectively. Excluding the unrealised fair value loss on foreign currency forward exchange contract valued of RM14.1 million in 1H15 and unrealised gain of RM7.2 million in 1H14, the segment profit of RM105.9 million is 49.7% lower than the underlying profit of RM210.5 million made in 1H14. On top of that, the performance was also impacted by cheap petroleum prices which gave cost edge to synthetic products in fatty alcohol business.
- Property.** Property segment revenue increased by 49% to RM72.6 million in 1H15 from RM48.9 million in 1H14. In line with the increase in revenue, segments profit rose 2-fold or a growth of 98% y-o-y to RM42.8 million against RM21.6 million in 1H14, resultant from higher profit recognition from Bandar Seri Coalfields development and surpluses from the sale of industrial and commercial land during the period under review.
- Sector outlook.** We are maintaining our **NEUTRAL** call on the sector due to the absence of new fresh catalyst with prolong supply-demand miss-match coming on stream as production may build-up amid seasonal production growth cycle. In addition, demand is expected to be moderate in 2015 as import from major trading partner is likely to be slower. We are of the view that the only re-rating catalyst for CPO price in 2015 will be the widening premium of soybean oil against the palm oil and weather abnormalities, if any.
- Maintain forecast.** We maintain our FY15 and FY16 earnings forecast of RM1,060 million and RM1,181 million respectively, to impute our view on the uncertain of CPO price given no strong catalyst are seen to chart higher CPO price this year. We assume CPO prices to hover around RM2,100/MT - RM2,500/MT throughout the year and averaging at RM2,300/MT in 2015. The only concern is the stronger of USD currency that may impact the US Dollar denominated borrowings of KLK on the non-cash flow forex translation. However, we are of the view that, an increase in capacity from its downstream plants couple with higher FFB production and better CPO extraction rate may moderate the impact of lower palm oil product prices and hence, cushioning the KLK's earnings. We are still banking on the stock given its strong management, larger planted land bank and sizeable prime age profile which may provide visible revenue and earnings growth if CPO price starts to rebound.
- Valuation & recommendation.** We maintain our **HOLD** call on KLK with unchanged target price of RM21.50 based on 21x PER over CY15 EPS of RM1.024.

Table 1: Peers Comparison - Stocks under Coverage

Company	Mkt. Cap (RM m)	Price (RM)	EPS (sen)		P/E (X)		P/B (X)		ROE	Div. Yield	TP	Call
			FY1	FY2	FY1	FY2	FY1	FY2				
IOI CORP	26,395.2	4.16	15.6	22.9	26.7	18.2	3.2	3.0	7.8	0.6	4.04	HOLD
KLK	23,855.2	22.40	99.5	110.9	22.5	20.2	2.8	2.6	11.3	2.7	21.50	HOLD
GENPLANTS	7,737.5	10.00	52.3	58.9	19.1	17.0	1.9	1.7	10.3	1.4	10.63	HOLD
IJM PLANTS	3,064.4	3.48	12.5	17.1	27.8	20.4	2.0	1.9	9.2	1.4	3.20	HOLD
TH PLANTS	1,370.0	1.55	2.9	7.4	7.4	20.9	1.1	1.1	4.0	1.3	1.47	HOLD
TSH RESOURCES	3,050.4	2.25	10.1	11.9	22.3	18.9	2.3	2.1	11.1	1.1	2.38	HOLD
Average					21.0	19.3	2.2	2.1	8.9	1.4		

Notes: FY1 is the current FY estimate

Source: Bloomberg, M&A Securities

Table 2: Results Review - Quarterly figures

FYE 30 Sept (RM'm)	2Q14	1Q15	2Q15	q-o-q	y-o-y	1H14	1H15	y-o-y
Revenue	2,934	3,114	3,065	-1.6%	4.5%	5,428	6,180	13.8%
EBIT	435	311	325	4.6%	-25.3%	825	636	-23.0%
Pretax profit	424	294	297	0.7%	-30.1%	802	591	-26.3%
Taxation	-87	-67	-69	3.6%	-20.5%	-163	-136	-16.1%
Minority interest	-23	-13	-5	-65.0%	-79.5%	-32	-18	-45.0%
Net Profit	315	214	223	3.9%	-29.3%	607	437	-28.1%
EPS (sen)	29.5	20.1	20.9	4.0%	-29.2%	57.0	41.0	-28.1%
Net gearing (x)	0.16	0.19	0.21	13.2%	33.9%	0.16	0.21	33.9%
EBIT margin (%)	14.8	10.0	10.6			15.2	10.3	
PBT margin (%)	14.5	9.5	9.7			14.8	9.6	
Net margin (%)	10.7	6.9	7.3			11.2	7.1	

Source: Bursa Malaysia, M&A Securities

Table 3: Financial Summary

YE: Sept (RM million)	2012	2013	2014	2015F	2016F
Revenue	10,570	9,147	11,130	11,187	11,923
EBIT	1597	1251	1369	1562	1722
PBT	1560	1200	1318	1472	1641
Net profit	1211	918	992	1060	1181
EPS (sen)	113.7	86.2	93.1	99.5	110.9
Pre-tax margin	15%	13%	12%	13%	14%
Net profit margin	11%	10%	9%	9%	10%
PER (x)	19.7	26.0	24.1	22.5	20.2
P/BV (x)	3.4	3.2	3.1	2.8	2.6
ROE	17.1%	12.5%	13.5%	13.9%	14.0%
ROA	10.8%	7.9%	8.1%	8.1%	8.8%
Dividend (RM)	0.65	0.50	0.55	0.60	0.67
Dividend Yield	2.9	2.2	2.5	2.7	3.0

Source: Bursa Malaysia, M&A Securities

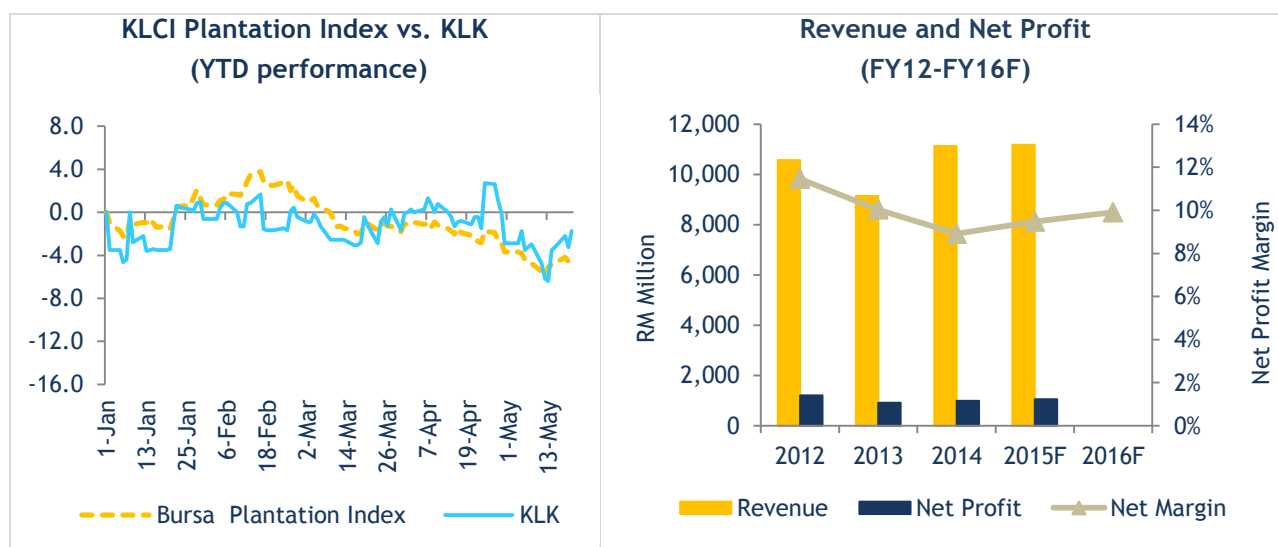
Table 4: Results Analysis - Segmental Breakdown

FYE: September (RM' Mil)	1H14	1H15	y-o-y
Plantation	2,721.9	3,465.0	27%
Manufacturing	2,763.1	2,925.2	6%
Property Development	48.9	72.6	49%
Investment Holding/Others	102.8	127.9	24%
Elimination	-208.4	-411.1	97%
Segment Results:			
Plantation	545.2	399.9	-27%
Manufacturing	217.7	91.8	-58%
Property Development	21.6	42.8	98%
Investment Holding/Others	10.0	7.6	-24%

Table 5: Plantation Statistics

FYE: September	1H15	1H14	y-o-y	2QFY15	1QFY15	2QFY14	q-o-q	y-o-y
FFB production (MT)	1,780,258	1,846,781	-4%	825,549	954,709	842,337	-14%	-2%
CPO Production (MT)	405,932	409,120	-1%	188,778	217,154	188,406	-13%	0%
Rubber ('000 kg)	7759.9	8613.4	-10%	4220.734	3539.182	4182.644	19%	1%
Crude Palm Oil (RM/MT ex-mill)	2,170	2,392	-9%	2,212	2,138	2,499	3%	-11%
Palm Kernel (RM/MT ex-mill)	1,472	1,542	-5%	1,607	1,362	1,742	18%	-8%
Rubber (RM/KG net of cess)	6.75	8.49	-20%	6.89	6.63	8.21	4%	-16%

Source: Bursa Malaysia, M&A Securities



Source: Bloomberg, M&A Securities

M&A Securities

STOCK RECOMMENDATIONS

BUY	Share price is expected to be $\geq +10\%$ over the next 12 months.
TRADING BUY	Share price is expected to be $\geq +10\%$ within 3-months due to positive newsflow.
HOLD	Share price is expected to be between -10% and $+10\%$ over the next 12 months.
SELL	Share price is expected to be $\geq -10\%$ over the next 12 months.

SECTOR RECOMMENDATIONS

OVERWEIGHT	The sector is expected to outperform the FBM KLCI over the next 12 months.
NEUTRAL	The sector is expected to perform in line with the FBM KLCI over the next 12 months.
UNDERWEIGHT	The sector is expected to underperform the FBM KLCI over the next 12 months.

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