

Equity Beat

25 February 2010

1QFY10 Results Review

KL Kepong Berhad

Rich valuation

Maintain NEUTRAL

Revised Target Price (TP): RM15.92 (from RM14.18)

- KLK's 1Q10 net earnings came in at RM242m, accounting for 29% of our full-year estimate. The figure is within our expectation as the Oct-Dec period is generally the highest yielding quarter for oil palm trees.
- KLK's 1Q10 earnings surged 267.3% over previous year largely due to the low-base effect.
- Plantation segment profit fell due to lower CPO selling price while manufacturing improved in the absence of write down. Retail (Crabtree) recovered post Chapter 11 restructuring.
- The historical mean PER of KLK is 17x, with a lower and an upper band of 11x and 24x. In view of the continuing economic recovery and prevailing accommodative liquidity situation, we expect the PER rating of KLK to hover within the top half of its PER bands. On FY10 earnings, the mid-way point between the mean and the upper band translates to a stock price of RM15.92. We thereby maintain our Neutral recommendation on the stock with a revised target price of RM15.92.

STOCK INFO

Price (24 Feb 10)	RM16.68	KLCI	1,270.78
Issued shares (mil)	1,067.50	Bursa / Bloomberg	2445/KLK MK
Par Value (RM)	1.00	Board / Sector	Main/ Plantation
Market cap. (RM'm)	17,806.0	Syariah Compliant	Yes
Price over NTA	3.35		
52-wk price Range	RM9.65–RM17.26	Major Shareholders	
Beta (against KLCI)	1.09	Batu Kawan Berhad	46.45%
3-mth Avg Daily Vol	1.9m	EPF	16.53%
3-mth Avg Daily Value	RM20.6m	Van Eck Associates	0.70%

Surge in earnings growth due to the low-base effect. KLK's 1Q10 earnings surged by 267.3% to RM241.8 million as compared to RM65.8 million recorded in the same quarter last year. The higher profit was partly contributed by improvements in the manufacturing and retail segments. However, the main reason for the apparent surge in 1Q10 earnings vis-à-vis 1Q09 was due to the write-back of a sum of RM19.3 million (on the allowance for diminution in value of investment) in the quarter under review as against the allowance of RM160.3 million in the corresponding quarter last year.

High FFB output failed to fully mitigate the effect of lower CPO selling price. Plantation segment profit fell 19.5% to RM233.1 million in 1Q10 from RM289.6 million in 1Q09 mainly due to lower average CPO selling price of RM2,120/MT as compared to RM2,417/MT in earlier year corresponding period. The shortfall was partly offset by improved output as FFB production jumped by 24.2% to 0.91 million tons during 1Q10 vis-à-vis the same period last year.

Manufacturing recorded higher profit in the absence of write down and impairment. The oleochemical division of the manufacturing segment recorded a higher profit of RM29.9 million in 1Q10 as compared to a mere RM2.7 million in the corresponding period last year. The much lower profit in 1Q09 was attributable to the write-down of


FYE 30 Sep	FY07	FY08	FY09	FY10F
Revenue (RM'm)	5,067.6	7,855.4	6,658.3	7,784.4
EBIT (RM'm)	922.6	1,509.7	956.1	1,117.9
Pretax Profit (RM'm)	886.5	1,445.5	887.4	1,121.0
Net Profit (RM'm)	694.2	1,040.7	612.5	829.6
EPS (sen)	65.2	97.7	57.4	77.7
EPS growth (%)	59.1%	49.8%	-41.3%	35.4%
PER(x)	25.6	17.1	29.1	21.5
Net Dividend (sen)	36.9	54.9	33.8	37.5
Net Dividend Yield (%)	2.2%	3.3%	2.0%	2.2%

Source: Company, Forecasts by MIDFR

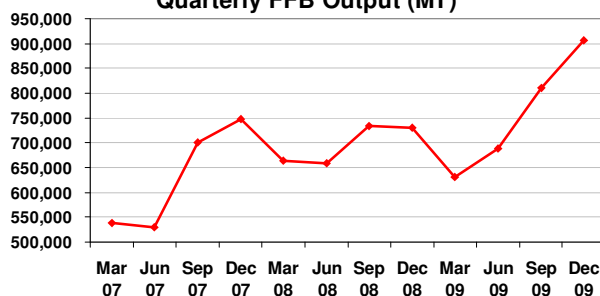
inventories by KLK's China plant.

Retail performance improved pursuant to the Chapter 11 restructuring exercise. The retailing segment achieved a significant 71.8% rise in profit to RM52.5 million in 1Q10 vis-à-vis RM30.5 million recorded in 1Q09. The Chapter 11 restructuring exercise undertaken by its US operations had contributed to the much improved profit due to better retail performance, pursuant to the closure of non-performing stores, and lower operating expenses.

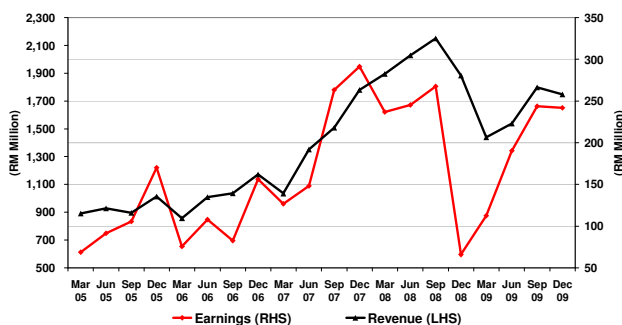
Fair outlook. KLK's performance is expected to remain firm in view of the following: (i) satisfactory performance from the plantation sector due to the prevailing higher CPO prices and the expected increase in FFB output; (ii) higher profits from the manufacturing sector on the expectation of increasing demand arising from the recovery of the global economy; and (iii) improving performance from the retailing sector pursuant to the completion of the Chapter 11 restructuring exercise.

We maintain our NEUTRAL recommendation. The historical mean PER of KLK is 17x, with a lower and an upper band of around 11x and 24x respectively (see PER chart below). Applying that empirical measures on FY10 earnings, we arrived at lower, mean and upper band prices of RM8.54, RM13.20 and RM18.64 respectively. In view of the continuing economic recovery and prevailing accomodative liquidity situation, we expect the PER rating of a key index stock such as KLK to hover within the top half of its PER bands. The mid-way mark between the mean (RM13.20) and the upper (RM18.64) band, i.e. the 75-percentile point, is RM15.92. We thereby maintain our **Neutral** recommendation on the stock with a revised target price of RM15.92. 

Quarterly FFB Output (MT)

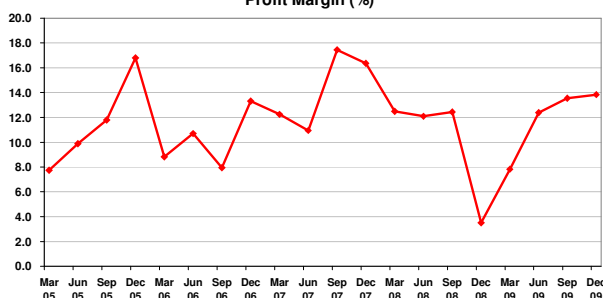


FFB output rose by 12%qoq in 1Q10. But expect output to decline in the subsequent quarters due to seasonal factor.

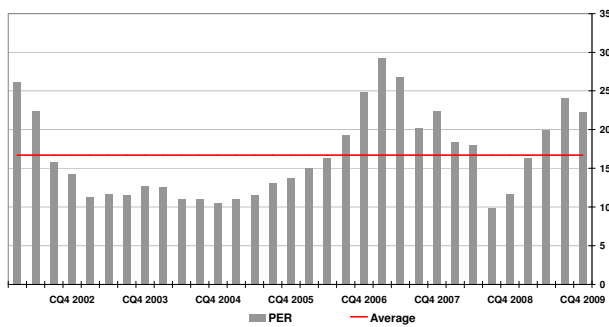


Slight reductions of q-o-q revenue and earnings in 1Q10 were largely owing to lower CPO selling price.

Profit Margin (%)



Profit margin in 1Q10 retained its normal levels of around 14%.



Historical average PER of 17x.

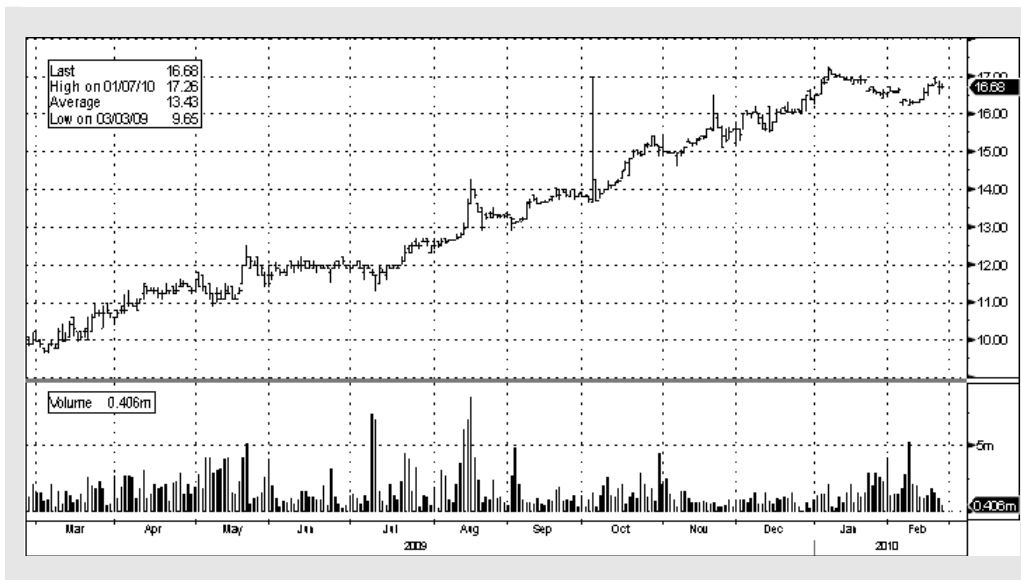
KL Kepong: 1QFY10 RESULTS SUMMARY

FYE Sep (RM m)	Quarterly Results			Comments
	1Q10	%YoY	%QoQ	
Revenue	1,747.7	-7.2%	-2.9%	Lower revenue due to decline in CPO selling prices despite higher FFB output
Operating profit	344.3	107.6%	-4.1%	Low-base effect and due to improved performance from manufacturing and retailing segments
Interest expense	-14.9	-20.9%	-8.4%	
Pre-tax profit	329.5	124.0%	-3.9%	As above
Tax	-73.9	-4.8%	-13.7%	
Net Profit	241.8	267.3%	-0.8%	As above
EPS (sen)	22.7	267.5%	-0.8%	
		+/- ppts	+/- ppts	
Op margin (%)	19.7%	10.9	-0.3	
Tax rate (%)	22.4%	-30.3	-2.6	
Segmental				
<u>Revenue:</u>				
Plantation	866.7	-13.7%	-11.8%	Weak CPO selling prices
Manufacturing	648.4	-0.6%	-9.0%	
Retailing	265.7	3.1%	117.3%	Recovering pursuant to Chapter 11 restructuring
Property	10.7	-41.7%	70.4%	
<u>Operating Profit:</u>				
Plantation	233.1	-19.5%	-20.1%	Weak CPO selling prices
Manufacturing	22.8	-488.7%	-56.5%	Absence of write down
Retailing	52.5	71.8%	-228.5%	Recovering pursuant to Chapter 11 restructuring
Property	2.5	-43.3%	-45.8%	
<u>Operating Margin:</u>				
Plantation	26.9%	-1.9	-2.8	Weak CPO selling prices
Manufacturing	3.5%	4.4	-3.9	
Retailing	19.7%	7.9	53.1	Recovering pursuant to Chapter 11 restructuring
Property	22.9%	-0.6	-49.1	
(Continued)				

Plantation Stats:				
CPO KLK (RM/MT)	2,120	-12.3%	-12.0%	
CPO Market (RM/MT)	2,318	44.5%	3.4%	
FFB production (MT)	906,147	24.2%	11.8%	Higher output as its plantations less affected by recent adverse weather

Source: Company, MIDFR

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

OVERWEIGHT	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.
UNDERWEIGHT	The sector is expected to underperform the overall market over the next 12 months.