

20 May 2021

Agriculture | Plantation

Kuala Lumpur Kepong (KLK MK)

Buy (Maintained)

Earnings Boost From Downstream Segment

- **Reiterate BUY, new MYR27.50 TP from MYR28.30, 25% upside with 2.5% FY22F (Sep) yield.** Kuala Lumpur Kepong's 1H21 results are in line with our but above consensus estimates, with core net profit rising 64% YoY. We continue to like KLK for its stellar earnings growth and inexpensive valuation of 19x FY21 vs other big-cap peers' 22-23x.
- **1H FY21 core net profit was at 54% of our and 62% of consensus FY21F forecasts.** Strong EBIT growth was seen from all segments, led by the upstream (+60% YoY) and the manufacturing divisions (+62% YoY). All in, 1H FY21's core net profit rose 64% YoY. The group declared a net interim DPS of 20 sen in 2QFY21
- **1H21 FFB production rose 0.3% YoY.** For FY21, KLK has now revised its FFB growth projection down to 5% YoY from 10% YoY (excluding contributions from recent land acquisitions), on the back of 12,000 ha of new area coming into maturity. As output growth in 7MFY21 has moderated further to flat YoY, we maintain our 3-4% growth projections for FY21-22, to be conservative.
- **1H FY21 CPO price of MYR2,846/tonne** was lower than the Malaysian spot CPO price, due to price discounts in Indonesia caused by the export tax levy and some forward sales that were entered into earlier. We understand that, for FY21, KLK has sold about 20-30% of its production 2-3 months ahead.
- **Estimated unit cost dropped by 15-20% YoY in 1H FY21,** likely due to the wet weather during the period, which could have prevented full fertilisation activities. Unit cost in FY20 was at MYR1,465/tonne, and management expects to be able to reduce this in FY21F on the back of higher FFB output.
- **Its oleochemicals EBIT margin rose in 2Q21 to 8.9%** (from 5.6% in 1Q21), bringing the 1H21 margin to 7.3% (from 5.7% in 1H20). This was achieved despite an increase in feedstock prices, as KLK managed to record higher sales volumes in Malaysia, China and Europe.
- **No change to earnings forecasts.** While we acknowledge the very strong 1H FY21 numbers, we make no changes to our estimates for now, as we believe earnings could moderate in 4Q21, in line with the CPO price movement.
- **BUY, with a slightly lower TP of MYR27.50,** after updating for KLK's latest listed investment values and net debt. Our SOP is based on an unchanged 25x 2022 target P/E for KLK's plantations, 15x for its manufacturing segment, and a 75% discount applied to the RNAV of its property landbank. KLK remains our top big-cap pick for its stellar earnings prospects and inexpensive valuations vs peers.

Target Price (Return): MYR27.50 (+25%)
 Price: MYR22.02
 Market Cap: USD5,758m
 Avg Daily Turnover (MYR/USD) 13.1m/3.19m

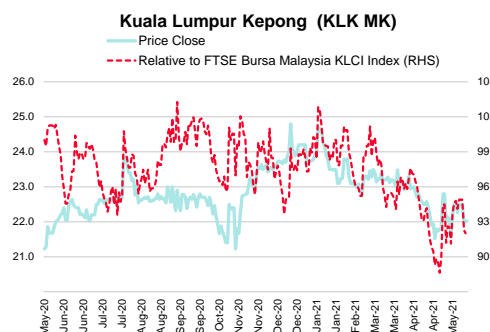
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Share Performance (%)

| | YTD | 1m | 3m | 6m | 12m |
|----------------------------|-------|-----|-------|-------------|-------|
| Absolute | (7.0) | 0.5 | (5.5) | (6.5) | 3.8 |
| Relative | (4.8) | 1.1 | (5.9) | (7.0) | (8.0) |
| 52-wk Price low/high (MYR) | | | | 21.2 – 24.8 | |



Source: Bloomberg

Overall ESG Score: 3.0 (out of 4)

E: Good

KLK has adopted a strict zero-burning policy since the mid-1990s that also extends to its plasma schemes. Additionally, the company reported a reduction in greenhouse gas (GHG) emissions intensity and recorded 67% GHG savings, compared to fossil fuel emissions in 2019 (exceeding its target of 65%). It has aimed to achieve 68% GHG savings by end-2020.

S: Excellent

KLK is committed to ensuring the safety and well-being of its workers through the establishment of various task forces and grievance procedures. It aims to achieve zero fatal accidents and, for the fourth consecutive year (2019), its Malaysian operations recorded zero fatalities, with a 14% reduction in major accident incidents.

G: Excellent

63% of KLK's board members are independent, with full disclosure on director remuneration – which includes salaries and bonuses on a named basis. KLK has an in-house investor relations team and holds investor meetings regularly, embodying good transparency and disclosure practices.

| Forecasts and Valuation | Sep-19 | Sep-20 | Sep-21F | Sep-22F | Sep-23F |
|---------------------------------|--------|--------|---------|---------|---------|
| Total turnover (MYRm) | 15,534 | 15,596 | 21,662 | 19,889 | 19,952 |
| Recurring net profit (MYRm) | 649 | 692 | 1,274 | 1,047 | 1,070 |
| Recurring net profit growth (%) | (8.7) | 6.6 | 84.2 | (17.8) | 2.1 |
| Recurring P/E (x) | 36.13 | 34.17 | 18.64 | 22.68 | 22.20 |
| P/B (x) | 2.3 | 2.8 | 2.7 | 2.6 | 2.5 |
| P/CF (x) | 20.88 | 16.33 | 15.74 | 16.60 | 11.77 |
| Dividend Yield (%) | 2.3 | 1.8 | 2.5 | 2.5 | 2.5 |
| EV/EBITDA (x) | 17.34 | 12.65 | 9.81 | 11.43 | 11.26 |
| Return on average equity (%) | 5.4 | 8.4 | 11.5 | 9.1 | 9.1 |
| Net debt to equity (%) | 39.7 | 30.6 | 28.5 | 27.8 | 22.7 |

Source: Company data, RHB

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Financial Exhibits

| | | | | | | |
|--|-------------------------------------|---------------|---------------|----------------|----------------|----------------|
| Asia | Financial summary (MYR) | Sep-19 | Sep-20 | Sep-21F | Sep-22F | Sep-23F |
| Malaysia | Recurring EPS | 0.61 | 0.64 | 1.18 | 0.97 | 0.99 |
| Agriculture | DPS | 0.50 | 0.40 | 0.55 | 0.55 | 0.55 |
| Kuala Lumpur Kepong | BVPS | 9.71 | 7.88 | 8.25 | 8.46 | 8.69 |
| KLK MK | Return on average equity (%) | 5.4 | 8.4 | 11.5 | 9.1 | 9.1 |
| Buy | | | | | | |
| Valuation basis | Valuation metrics | Sep-19 | Sep-20 | Sep-21F | Sep-22F | Sep-23F |
| Our SOP valuation comprises: | Recurring P/E (x) | 36.13 | 34.17 | 18.64 | 22.68 | 22.20 |
| i. Target P/E of 25x 22F for the plantations division; | P/B (x) | 2.3 | 2.8 | 2.7 | 2.6 | 2.5 |
| ii. 15x P/E for the downstream divisions; | FCF Yield (%) | 2.1 | 3.3 | 3.4 | 3.1 | 5.5 |
| iii. RNAV for the property division. | Dividend Yield (%) | 2.3 | 1.8 | 2.5 | 2.5 | 2.5 |
| | EV/EBITDA (x) | 17.34 | 12.65 | 9.81 | 11.43 | 11.26 |
| | EV/EBIT (x) | 27.31 | 18.20 | 13.07 | 16.12 | 15.91 |
| This is backed by an EV/ha of USD20,000-30,000/ha, which is in line with its Malaysian peer range. | Income statement (MYRm) | Sep-19 | Sep-20 | Sep-21F | Sep-22F | Sep-23F |
| Key drivers | Total turnover | 15,534 | 15,596 | 21,662 | 19,889 | 19,952 |
| i. CPO price movement; | Gross profit | 1,676 | 2,070 | 3,531 | 3,038 | 3,043 |
| ii. FFB production output; | EBITDA | 1,545 | 2,021 | 2,626 | 2,266 | 2,269 |
| iii. Competitiveness of its downstream processing division vs peers. | Depreciation and amortisation | (564) | (616) | (655) | (659) | (663) |
| | Operating profit | 981 | 1,405 | 1,971 | 1,606 | 1,606 |
| | Net interest | (166) | (243) | (230) | (213) | (206) |
| Key risks | Pre-tax profit | 792 | 1,303 | 1,873 | 1,540 | 1,573 |
| i. CPO price movement; | Taxation | (173) | (329) | (450) | (370) | (378) |
| ii. Weather risks; | Reported net profit | 586 | 890 | 1,274 | 1,047 | 1,070 |
| iii. Demand and supply dynamics of the global vegetable oil industry. | Recurring net profit | 649 | 692 | 1,274 | 1,047 | 1,070 |
| Company Profile | Cash flow (MYRm) | Sep-19 | Sep-20 | Sep-21F | Sep-22F | Sep-23F |
| Kuala Lumpur Kepong is an integrated plantations company with palm oil plantations landbank in Malaysia, Indonesia and Papua New Guinea. It also operates in the downstream manufacturing segment, through its edible oil refineries and oleochemical businesses. In addition, KLK is involved in the property development business. | Change in working capital | 69 | (50) | (570) | (399) | 159 |
| | Cash flow from operations | 1,123 | 1,447 | 1,509 | 1,431 | 2,017 |
| | Capex | (639) | (667) | (700) | (700) | (700) |
| | Cash flow from investing activities | (2,167) | 25 | (700) | (700) | (700) |
| | Cash flow from financing activities | 1,729 | (444) | (1,457) | (957) | (957) |
| | Cash at beginning of period | 1,278 | 2,041 | 2,953 | 2,305 | 2,079 |
| | Net change in cash | 685 | 1,028 | (648) | (226) | 361 |
| | Ending balance cash | 2,084 | 3,198 | 2,305 | 2,079 | 2,440 |
| | Balance sheet (MYRm) | Sep-19 | Sep-20 | Sep-21F | Sep-22F | Sep-23F |
| | Total cash and equivalents | 2,041 | 2,953 | 2,305 | 2,079 | 2,440 |
| | Tangible fixed assets | 9,198 | 8,753 | 8,798 | 8,838 | 8,876 |
| | Total investments | 2,058 | 2,107 | 2,107 | 2,107 | 2,107 |
| | Total assets | 20,399 | 20,946 | 21,152 | 21,533 | 21,706 |
| | Short-term debt | 1,349 | 1,311 | 1,111 | 911 | 711 |
| | Total long-term debt | 5,170 | 5,250 | 4,750 | 4,750 | 4,750 |
| | Total liabilities | 9,113 | 9,142 | 8,681 | 8,648 | 8,382 |
| | Total equity | 11,287 | 11,804 | 12,471 | 12,885 | 13,324 |
| | Total liabilities & equity | 20,399 | 20,946 | 21,152 | 21,533 | 21,706 |
| | Key metrics | Sep-19 | Sep-20 | Sep-21F | Sep-22F | Sep-23F |
| | Revenue growth (%) | (15.5) | 0.4 | 38.9 | (8.2) | 0.3 |
| | Recurrent EPS growth (%) | (8.7) | 5.8 | 83.3 | (17.8) | 2.1 |
| | Gross margin (%) | 10.8 | 13.3 | 16.3 | 15.3 | 15.2 |
| | Operating EBITDA margin (%) | 9.9 | 13.0 | 12.1 | 11.4 | 11.4 |
| | Net profit margin (%) | 3.8 | 5.7 | 5.9 | 5.3 | 5.4 |
| | Dividend payout ratio (%) | 91.1 | 61.7 | 59.4 | 72.2 | 70.7 |
| | Capex/sales (%) | 4.1 | 4.3 | 3.2 | 3.5 | 3.5 |
| | Interest cover (x) | 5.92 | 5.79 | 8.58 | 7.54 | 7.81 |

Source: Company data, RHB

Results At a Glance

Figure 1: KLK's quarterly results review

| FYE Sep (MYRm) | 2QFY19 | 1QFY20 | 2QFY20 | QoQ (%) | YoY (%) | 1H19 | 1H20 | YoY (%) | Comments |
|--------------------------------|---------|---------|---------|---------|---------|---------|---------|---------|---|
| Revenue | 3,804.0 | 4,299.8 | 3,764.3 | (12.5) | (1.0) | 7881.4 | 8064.1 | 2.3 | See segmental breakdown. |
| EBIT | 334.0 | 503.3 | 538.7 | 7.0 | 61.3 | 651.9 | 1042.0 | 59.8 | See segmental breakdown. |
| EBIT margin (%) | 8.8 | 11.7 | 14.3 | | | 8.3 | 12.9 | | |
| Net interest income /(expense) | (62.0) | (58.3) | (57.5) | 1.3 | 7.3 | (125.4) | (115.7) | 7.7 | |
| Associates | 23.1 | 12.8 | 24.9 | 93.9 | 7.6 | 24.4 | 37.7 | 54.4 | |
| EI/Others | (192.5) | 36.1 | 143.2 | 297.0 | 174.4 | (188.5) | 179.3 | 195.1 | 2Q21 EI included, amongst others, a MYR154.6m surplus on the sale of land, MYR12.2m surplus on the fair value of an investment that was previously an associate, and a MYR24.8m unrealised loss on derivatives in the manufacturing division. |
| Pretax profit | 102.6 | 493.9 | 649.3 | 31.5 | 533.0 | 362.3 | 1143.2 | 215.5 | Filtered down from EBIT and EI gain. |
| Pretax margin (%) | 2.7 | 11.5 | 17.2 | | | 4.6 | 14.2 | | |
| Tax | (79.5) | (86.2) | (129.2) | (50.0) | (62.6) | (148.2) | (215.4) | (45.3) | |
| Effective tax rate (%) | 77.5 | 17.4 | 19.9 | | | 40.9 | 18.8 | | |
| Minority interest | 4.8 | (50.3) | (29.6) | 41.1 | (720.5) | (19.0) | (79.9) | (319.7) | |
| Net profit | 27.9 | 357.4 | 490.4 | 37.2 | 1658.4 | 195.1 | 847.8 | 334.6 | |
| Core profit | 256.8 | 321.3 | 368.0 | 14.5 | 43.3 | 420.0 | 689.3 | 64.1 | Added back MYR20.7m in deferred tax impact from a change in the Indonesia tax rate. In line with our but above Street estimates, comprising 54% of our FY20 forecasts and 62% of the consensus estimate. |
| Net margin (%) | 6.8 | 7.5 | 9.8 | | | 5.3 | 8.5 | | |
| EPS (sen) | 2.6 | 33.1 | 45.5 | 37.5 | 1650.0 | 18.3 | 78.6 | 329.5 | |
| Net DPS (sen) | 15.0 | 0.0 | 20.0 | - | 33.3 | 15.0 | 20.0 | 33.3 | Interim DPS of 20 sen declared. |

Source: Company data, RHB

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Figure 2: Segmental breakdown of results

| FYE Sep (MYRm) | 2QFY20 | 1QFY21 | 2QFY21 | QoQ (%) | YoY (%) | 1H20 | 1H21 | YoY (%) | Comments |
|----------------------------|----------------|----------------|----------------|---------------|--------------|---------------|---------------|-------------|---|
| Plantation | 1,987.9 | 2,098.2 | 1,481.0 | (29.4) | (25.5) | 4204.9 | 3579.2 | (14.9) | Higher PK (+42% YoY) and CPO (+20%) prices, offset slightly by flattish (+0.3% YoY) FFB production. |
| Manufacturing | 1,977.1 | 2,340.5 | 2,620.0 | 11.9 | 32.5 | 3903.2 | 4960.5 | 27.1 | Increase from oleochemical contributions in Malaysia, China and Europe. |
| Property development | 17.0 | 53.4 | 41.6 | (22.1) | 145.0 | 69.2 | 95.1 | 37.4 | Higher revenue recognition from Bandar Seri Coalfields. |
| Others | 148.0 | 207.8 | 154.1 | (25.8) | 4.1 | 338.2 | 361.9 | 7.0 | Includes contributions from its wheat farming operations in Australia, which are seasonal in nature. |
| Inter-segment | (326.1) | (400.1) | (532.4) | (33.1) | (63.3) | (634.2) | (932.6) | (47.1) | |
| Revenue | 3,804.0 | 4,299.8 | 3,764.3 | (12.5) | (1.0) | 7881.4 | 8064.1 | 2.3 | |
| Plantation | 191.7 | 304.2 | 285.7 | (6.1) | 49.0 | 368.4 | 589.9 | 60.1 | Higher margins of 16.5% (vs 8.8% in 1H20) due to higher CPO and PK prices. |
| Manufacturing | 126.2 | 130.2 | 232.0 | 78.2 | 83.8 | 224.1 | 362.2 | 61.6 | Higher margins of 7.3% (from 5.7% in 1H20). |
| Property development | 3.3 | 19.7 | 14.2 | (27.7) | 332.5 | 16.2 | 33.9 | 109.4 | Higher margins from higher progress billings. |
| Others | 12.8 | 49.2 | 6.8 | (86.2) | (47.1) | 43.2 | 56.0 | 29.5 | Better profit from Australian farming sector of MYR44.1m (vs MYR1.2m in 1H20) due to a rise in crop output. |
| EBIT (excluding EI) | 334.0 | 503.3 | 538.7 | 7.0 | 61.3 | 651.9 | 1042.0 | 59.8 | Contributions from all segments improved significantly. |

Source: Company data, RHB

Figure 3: KLK's operational statistics

| FYE Sep (MYRm) | 2QFY20 | 1QFY21 | 2QFY21 | QoQ (%) | YoY (%) | 1H20 | 1H21 | YoY (%) | Comments |
|---------------------|-----------|-----------|-----------|---------|---------|-----------|-----------|---------|---|
| FFB volume (tonnes) | 890,733 | 973,744 | 900,153 | (7.6) | 1.1 | 1,868,594 | 1,873,897 | 0.3 | Below our 4% growth projection and management's original guidance of 10%. |
| CPO volume (tonnes) | 199,416 | 210,715 | 216,173 | 2.6 | 8.4 | 414,627 | 426,888 | 3.0 | |
| CPO price (MYR/t) | 2,572 | 2,703 | 2,997 | 10.9 | 16.5 | 2,373 | 2,846 | 19.9 | Marginally below our blended CPO price projection of MYR2,960/tonne. |
| Rubber prod (kg) | 2,451,377 | 2,543,743 | 1,760,296 | (30.8) | (28.2) | 5,363,054 | 4,304,039 | (19.7) | |

Source: Company data, RHB

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Figure 4: KLK's forecast assumptions

| | 2019 | 2020 | 2021F | 2022F | 2023F |
|-------------------------------|-------|-------|-------|-------|-------|
| FFB Produced ('000 tonnes) | 4,104 | 3,929 | 4,086 | 4,208 | 4,360 |
| CPO Production ('000 tonnes) | 1,023 | 863 | 1,037 | 1,064 | 1,097 |
| PK Production ('000 tonnes) | 205 | 162 | 190 | 195 | 201 |
| Average CPO price (MYR/tonne) | 1,924 | 2,344 | 3,200 | 2,800 | 2,700 |
| Average PK price (MYR/tonne) | 1,210 | 1,374 | 2,100 | 1,800 | 1,700 |

Source: RHB

Figure 5: RNAV of KLK's property landbank

| | Acres | BV (MYRm) | MV (MYRm) | Effective stake | Net surplus (MYRm) |
|---------------------------|-------|-----------|-----------|-----------------|--------------------|
| Ijok, Selangor | 1,947 | 32 | 1,103 | 100% | 572 |
| Colville, Ng Sembilan | 1,040 | 10 | 453 | 100% | 310 |
| Gombak, Selangor | 996 | 142 | 4,338 | 100% | 2,937 |
| Bagan Samak, Kedah | 867 | 13 | 189 | 100% | 123 |
| Tanjung Kupang, Johor | 502 | 884 | 884 | 60% | - |
| Tj Malim, Selangor | 425 | 8 | 56 | 100% | 34 |
| Paloh, Johor | 64 | 0 | 7 | 100% | 5 |
| KLK Complex, Sg Buloh | 20 | 3 | 34 | 100% | 22 |
| Ladang Tuan Mee, Sg Buloh | 3,677 | 17 | 8,008 | 100% | 5,593 |
| Ladang Fraser, Kulai | 2,500 | 12 | 871 | 40% | 241 |
| Subtotal | | | | | 9,836 |
| Shareholders' funds | | | | | 1,389 |
| Total RNAV | | | | | 11,225 |
| Discount to RNAV | | | | | 75% |
| Discounted RNAV | | | | | 2,806 |

Source: RHB, Company data

Figure 6: KLK's SOP valuation

| | Valuation basis | MYR'm |
|--------------------------|----------------------|------------------|
| Plantation earnings | 25x Sep 22F earnings | 20,817.93 |
| Manufacturing earnings | 15x Sep 22F earnings | 6,119.07 |
| Property RNAV | 75% discount to RNAV | 2,806.18 |
| Synthomer Plc Investment | Mkt value | 2,072.43 |
| MP Evans Investment | Mkt value | 522.23 |
| Net cash/(debt) | As at 2QFY21 | (2,683.25) |
| TOTAL SOP | | 29,654.59 |
| No Shares* (m) | | 1,078.53 |
| SOP/share (MYR) | | 27.48 |

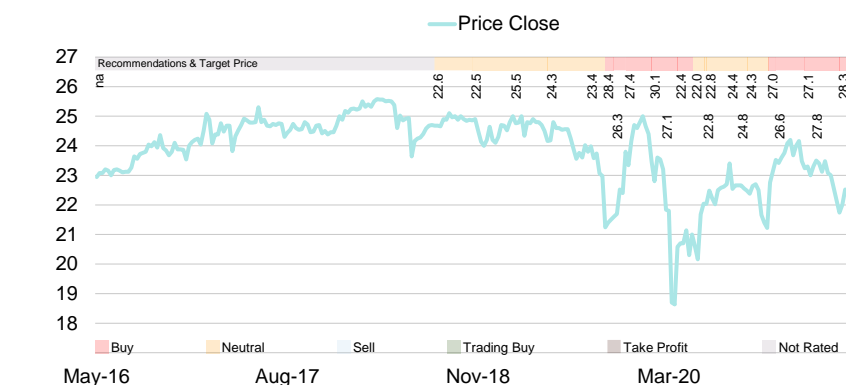
Note: * Weighted average

Source: RHB

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Recommendation Chart



Source: RHB, Bloomberg

| Date | Recommendation | Target Price | Price |
|------------|----------------|--------------|-------|
| 2021-04-21 | Buy | 28.3 | 21.5 |
| 2021-02-17 | Buy | 27.8 | 22.8 |
| 2021-01-27 | Buy | 27.1 | 23.1 |
| 2020-11-18 | Buy | 26.6 | 23.3 |
| 2020-11-01 | Buy | 27.0 | 21.2 |
| 2020-09-10 | Neutral | 24.3 | 22.9 |
| 2020-08-20 | Neutral | 24.8 | 22.6 |
| 2020-07-26 | Neutral | 24.4 | 22.7 |
| 2020-05-28 | Neutral | 22.8 | 22.0 |
| 2020-04-29 | Neutral | 22.0 | 20.6 |
| 2020-03-23 | Buy | 22.4 | 18.1 |
| 2020-02-17 | Buy | 27.1 | 23.7 |
| 2020-01-20 | Buy | 30.1 | 24.3 |

Source: RHB, Bloomberg

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| | |
|---------------------|--|
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