

# Stock Digest

## Results Note – Teo Seng Capital Bhd

Tuesday, 21 Aug, 2018



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## Below Expectation

### Results Highlights

- Teo Seng's 2Q2018 net loss narrowed to RM0.5 mln vs. a net loss of RM5.8 mln recorded in the previous corresponding quarter, due to the recovery in the average egg selling prices, coupled with the stabilising feed cost. Revenue for the quarter added 7.8% Y.o.Y to RM102.7 mln.
- The reported results came below our expectations, making up to only 28.8% of our previous estimated net profit estimate of RM20.2 mln. Meanwhile, the reported revenue came slightly below our expectations, amounting to 45.4% of our full-year forecast of RM479.7 mln. The variance in its bottom line was due to higher overhead cost arising from the group's expansion plans, coupled with the slower sales.
- Segment wise in 2Q2018, the poultry farming segment's pretax loss narrowed to RM3.0 mln vs. a pretax loss of RM4.9 mln, lifted by improved average egg selling prices, higher sales quantity and lower feed cost. The trading segment's pretax profit grew 6.7% Y.o.Y to RM2.3 mln on higher demand for animal health products.
- As of 2Q2018, Teo Seng's gearing is reduced to 68.0% (from 69.2% recorded in 1Q2018). Moving forward, we expect Teo Seng's gearing level to remain above the 50.0% level as the group continues to hinge on external funds to cater for its expansion plans, targeting production of 5.0 mln eggs per day in 2022.
- A single tier interim dividend of 0.5 sen per share was declared in conjunction with the release of its quarterly results.

Financial Highlights					
FYE Dec (RM mln)	2015A	2016A	2017A	2018F	2019F
Revenue	412.8	433.7	422.6	479.7	526.2
EBITDA	68.5	48.3	28.5	44.7	53.7
Net Profit	41.0	20.7	3.5	14.0	19.3
Revenue Growth (%)	8.4	5.1	-2.6	13.5	9.7
EBITDA Growth (%)	-15.9	-29.5	-40.9	56.9	20.2
Net Profit Growth (%)	-15.7	-49.5	-83.3	303.8	38.2
EPS (sen)	13.7	6.9	1.2	4.7	6.4
Diluted EPS (sen) *	N/A	N/A	N/A	4.1	5.6
P/E (x)	6.0	11.9	N/A	17.7	12.8
Diluted P/E (x) *	N/A	N/A	N/A	20.1	14.7
DPS (sen)	2.5	2.5	0.0	1.5	2.0
Dividend Yield (%)	3.0	3.0	0.0	1.8	2.4
P/BV (x)	1.3	1.0	1.0	0.9	0.9
ROE (%)	21.4	8.4	1.4	5.3	6.8

\* Based on enlarged share capital of 350.0 mln outstanding shares (After adjusting for full warrant conversion in 2018)

Source: Company Data & MSSB Research

**Recommendation: HOLD**

**Share Price: RM0.845**

**Target Price: RM0.90**

**Expected Return: +6.5%**

**Expected Dividend Return: +1.8%**

**Expected Total Return: +8.3%**

**FBM KLCI: 1,787.58**

### Key Statistics

**Bursa Code: 7252**

**Bloomberg Ticker: TSCB MK Equity**

**Stock Information:** Engaged in layer farming, manufacturing and marketing of animal feeds and paper egg trays, along with the distribution of animal health products.

**Listing Market:** Main Market

**Share Issued (mln):** 300.0

**Market Capital (RM mln):** 253.5

**Par Value (RM):** N/A

**52 week high/low:** RM1.05/RM0.82

**Estimated free float:** 28.0%

**Beta (x):** 1.1

**3-month average volume ('000):** 70.1

**Major Shareholders:**

Emerging Glory Sdn Bhd 54.5%

Koperasi Permodalan Felda 3.7%

Malaysia Bhd

Public Islamic Opportunities Fund 2.5%

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## Prospects

Teo Seng's egg production stood at 3.7 mln eggs per day in 1H2018 (relatively unchanged from end-2017). With the recent completion of a new feedmill plant, the group will now concentrate on ramping up its egg production, targeting daily production of 5.0 mln eggs by end-2022. Since peaking in January 2018, chicken egg prices have tumbled in 2Q2018, before staging a recovery in early 3Q2018 (see Appendix 1). Moving forward, we expect chicken prices to be fairly stable towards end-2018 as the demand-supply condition remains well balanced.

In the meantime, the group is targeting cost efficient measures by adopting automation processes in its daily operational activities. The investment in automated chicken manure belts in its farm houses is expected to be completed by 2019. This will reduce the reliance on foreign workers and could boost Teo Seng's bottomline margins.

Over at the group's major production cost, soybean prices have slumped in June 2018, averaging at RM38.61 per bushel in 2Q2018 (-3.7% Q.o.Q) after China retaliated by imposing a 25.0% import duty on U.S. soybeans after the U.S. imposed a similar tariff on US\$34.0 bln worth of China products. In 2017, the U.S. exported approximately US\$14.0 bln worth of soybeans to China.

Meanwhile, Maize prices remained stable, averaging at RM803.93 per tonne (+0.3% Q.o.Q) (see Appendix 2). Moving forward, we expect soybean prices to remain weak, trading below RM40.00 per bushel, whilst Maize prices are expected to remain above RM750.00 per metric tonne for the remainder of 2018 on improved demand for livestock feed and industrial processing.

## Valuation And Recommendation

With the reported earnings coming below our expectations, we trimmed our earnings forecast by 30.8% and 20.2% for 2018 and 2019 respectively, accounting for the higher overhead cost, coupled with the lower average selling prices of eggs. Consequently, we downgrade Teo Seng to **HOLD** (from BUY) with a lower target price of RM0.90 (from RM1.15).

We rolled over our valuation metrics to 2019 and derive our target price by ascribing an unchanged target PER of 14.0x to its 2019 EPS of 6.4 sen. The ascribed target PER is at a 25% discount to its peers average of 18.7x due to its smaller market capitalisation. At current price of RM0.845, TSCB is trading at prospective PERs of 18.1x and 13.1x for 2018 and 2019 respectively and are already close to fair, in our view.

Risks to our recommendation include avian influenza – a viral infection that can infect not only birds, but also humans and other animals. Chicken feed (mainly soybean and maize) makes up 70% of production cost. The stronger commodity prices (soybean and maize) will negatively impact its margins and vice versa. A firmer Ringgit against the U.S. Dollar could also affect the group's bottom line. A recovery in the local currency

against the Greenback will have a positive impact on the group's earnings and vice versa, as the commodity purchases are denominated in U.S. Dollars.

Quarterly Performance					
FYE Dec (RM mln)	2Q2018	2Q2017	% Change		
			Y.o.Y	1Q2018	Q.o.Q
Revenue	102.7	95.3	7.8%	115.1	-10.7%
EBITDA	6.2	-2.9	-315.8%	15.3	-59.7%
Depreciation & Amotization	-4.9	-4.2	15.9%	-4.8	1.5%
Net Interest Income/ (Expense)	-2.0	-1.7	20.0%	-2.0	3.1%
Profit before Tax	-0.7	-8.7	91.9%	8.6	-108.2%
Net Profit	-0.5	-9.2	94.3%	6.6	-108.0%
Basic EPS (Sen)	-0.2	-3.1	94.3%	2.2	-108.0%

Source: Company Data & MSSB Research

Income Statement					
FYE Dec (RM mln)	2015A	2016A	2017A	2018F	2019F
Revenue	412.8	433.7	422.6	479.7	526.2
EBITDA	68.5	48.3	28.5	44.7	53.7
Depreciation & Amortisation	-11.4	-13.2	-15.8	-17.3	-18.5
Net Interest Expense	-13.2	-15.8	-17.3	-18.5	-20.0
Pre-tax Profit	50.7	26.0	4.1	18.1	25.1
Effective Tax Rate	19.0%	20.2%	15.3%	23.0%	23.0%
Net Profit	41.0	20.7	3.5	14.0	19.3
EBITDA Margin	16.6%	11.1%	6.7%	9.3%	10.2%
PreTax Margin	12.3%	6.0%	1.0%	3.8%	4.8%
Net Margin	9.9%	4.8%	0.8%	2.9%	3.7%

Source: Company Data & MSSB Research

Balance Sheet					
FYE Dec (RM mln)	2015A	2016A	2017A	2018F	2019F
Total Assets	366.0	468.2	495.0	531.5	576.1
Fixed Assets	222.6	294.4	316.1	345.5	364.9
Current Assets	143.4	173.8	178.9	185.9	211.2
Other LT Assets	0.0	0.0	0.0	0.0	0.0
Current Liabilities	134.5	149.9	177.4	199.2	223.1
LT Liabilities	39.8	72.5	68.8	69.4	70.9
Share Capital	60.0	60.0	60.0	60.0	60.0
Shareholder's Funds	191.7	245.8	248.8	262.8	282.1
Minority Interests	0.1	0.0	0.0	0.0	0.0

Source: Company Data & MSSB Research

Per Share Data					
FYE Dec	2015A	2016A	2017A	2018F	2019F
Book Value (Sen)	63.9	81.9	82.9	87.6	94.0
Cash Flow (Sen)	14.9	11.4	10.9	2.1	15.3
Net Earnings (sen)	13.7	6.9	1.2	4.7	6.4
Dividend (sen)	2.5	2.5	0.0	1.5	2.0
Payout Ratio (%)	18.3	36.2	0.0	32.2	31.1
Dividend Yield (%)	3.0	3.0	0.0	1.8	2.4
PER (x)	6.2	12.2	N/A	18.1	13.1
P/Cash Flow (x)	5.7	7.4	7.8	40.0	5.5
P/Book Value (x)	1.3	1.0	1.0	1.0	0.9
ROE (%)	21.4	8.4	1.4	5.3	6.8
Net Gearing (%)	44.6	47.3	63.7	68.5	65.6

Source: Company Data & MSSB Research

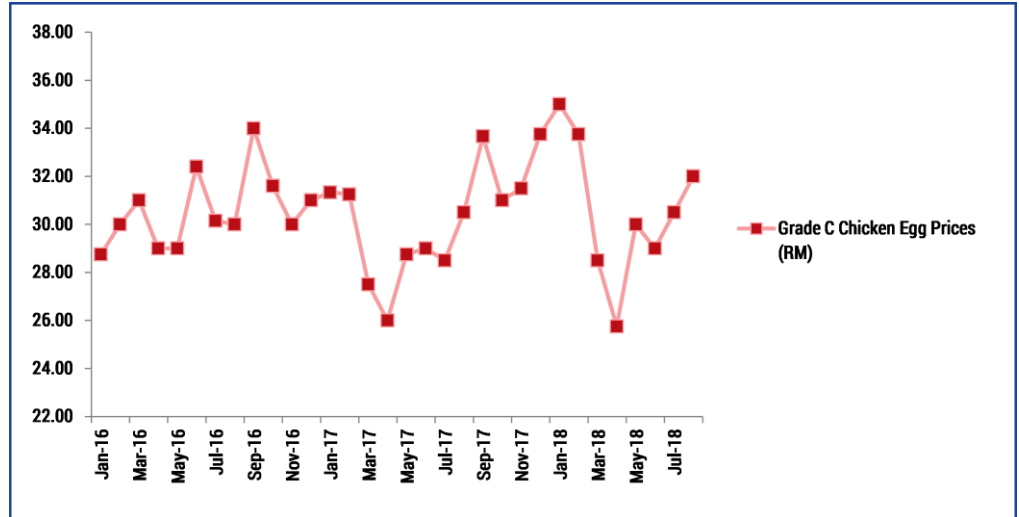
## Stock Price Performance vs KLCI



Price Performance	1 month	3 months	12 months
Absolute (%)	-0.59%	-10.11%	-1.74%
Relative (%)	-2.46%	-6.50%	-2.65%

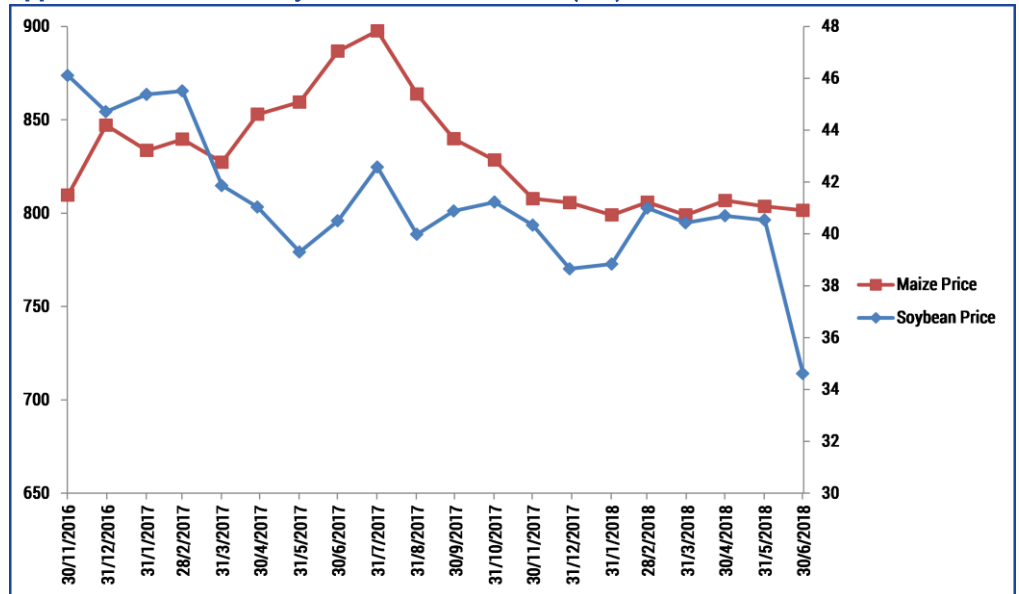
Source: Company Data, Bloomberg

### Appendix 1: Historical Grade C Chicken Egg Prices (RM)



Source: Department of Veterinary, MSSB Research

### Appendix 2: Historical Soybean and Maize Prices (RM)



Source: Bloomberg, MSSB Research

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