

29 August 2018

Southern Acids (M) Berhad 1Q19 Missed Expectations

1Q19 Core Net Profit (CNP) of RM1.2m fell far below expectations, making up only 5% of consensus and 4% of our forecast on lower-than expected margins from its core segment. No dividend was announced, as expected. We slash FY19-20E CNP by 16-17% to RM36.1-37.4m to reflect weaker Oleochemical and upstream performance. Downgrade to UNDERPERFORM with lower TP of RM3.20 (from RM3.95).

1Q19 missed forecasts. Excluding one-off unrealised forex gain (RM4.9m) and inventory write-down (RM0.02m), 1Q19 CNP came in at RM1.9m. This is far below expectations, making up only 5% of consensus' RM41.0m estimate and 4% of our RM42.9m full-year forecasts. The lower-than-expected CNP was dragged by weaker margins from its upstream plantation and likely higher operating cost on its healthcare division. FFB production at 18.0k metric tons (MT) was within our estimate, making up 24% of full-year forecast. No dividend was announced, as expected.

Oleochemical back to black but other segments weakened. YoY, 1Q19 CNP plunged (-81%) on sharp PBT decline by Oleochemical segment (-58%) to RM0.9m on lower ASPs of fatty acids (-12%) that led to margins erosion. Plantation Upstream PBT rose (+37%) to RM3.5m on higher FFB volumes (+24.6%) leading to lower production cost. Notably, healthcare PBT improved (+5%) attributed to higher inpatients average revenue per patient (ARPP) by (+9.3%) to RM5,482. **QoQ,** CNP plunged (-83%) on lower PBT contribution from upstream plantation (-29%) to RM3.5m likely caused by lower ASPs of CPO and PKs as well as higher raw materials costs. Meanwhile, healthcare division also registered weaker PBT of RM5.2m (-31%) due to seasonally lower bed occupancy rate during the festive period in June 2018. We note that SAB's Oleochemical division performance improved, which saw a reversal into PBT of RM0.9m (from RM0.3m losses previously), likely attributed by lower input costs.

Challenging prospects. We think SAB Oleochemical segment will continue to be under pressure amidst high operating cost and stiff competition in the market. Given relatively smaller production size in the market, unit cost will potentially be higher as a result of lower economies of scale. We think healthcare division will pick up for the rest of FY19 on the back of better average revenue per patient (ARPP) lifted by higher complex surgeries performed due to company's continuous effort in recruiting more specialists. We anticipate contribution from plantation upstream to be moderate given continuous easing in CPO prices.

Reduce FY19-20E CNP by 16%-17% to RM33.3-37.7m as we update our Oleochemical and plantation assumptions to reflect thinner margins on high operating costs.

Downgrade to UNDERPERFORM with lower TP of RM3.20 (from RM3.95) post earnings adjustment on Sum-of-Parts valuation based on average of FY19-20E EPS of 26.4 sen (lowered from 31.3 sen). In our Sum-of-Parts (SoP) valuation, we maintain our Fwd. PER of 13.0x for Oleochemical segment but cut EBIT to RM1.3m (from RM4.6m) to account for its challenging business prospect. We maintain 14.5x PER for upstream plantation division but also trimmed EBIT to RM12.6m (from RM19.1m). For healthcare division, we maintain our assumptions with unchanged 18.0x PER as well as our conglomerate discount of 15% to arrive at our SoP TP of RM3.20. Our TP implies a Fwd. PER of 12.1x, which is below -1.0SD of 3-year average. While we expect earnings to pick up on upcoming seasonally strong quarters, we downgrade our call to UNDERPERFORM (from MARKET PERFORM) in view of the challenging outlook in the Oleochemicals sector and softer upstream Plantation prospects.

Upside risks to our call include: (i) higher-than-expected CPO prices, (ii) lower-than-expected cost of production, and (iii) higher-than-expected CPO output.

UNDERPERFORM ↓

Price: **RM4.09**
Target Price: **RM3.20** ↓

Expected Capital Gain: **-RM0.890 -21.8%**
Expected Divd. Yield: **RM0.040 +1.0%**
Expected Total Return: **-RM0.850 -20.8%**

KLCI Index **1,826.90**

Stock Information

Bloomberg Ticker	SA MK Equity
Bursa Code	5134
Listing Market	Main Market
Shariah Compliant	Yes
Issued shares	136.9
Market Cap (RM m)	560.1
Par value per share (RM)	1.00
52-week range (H)	4.85
52-week range (L)	3.71
Free Float	47%
Beta	0.7
3-mth avg daily vol:	8,803

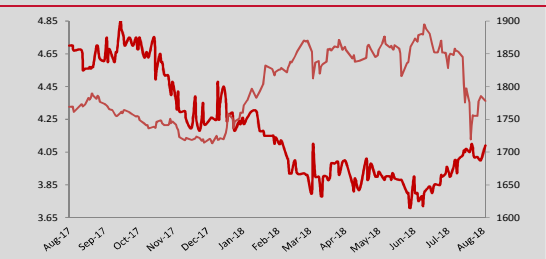
Major Shareholders

Southern Palm Industry	31.3%
Lembaga Tabung Haji	13.1%
Southern Realty (Malaya)	8.4%

Summary Earnings Table

FY Mar (RM m)	2018A	2019E	2020E
Turnover	763.2	709.3	732.2
EBIT	51.1	48.5	49.0
PBT	51.4	53.1	53.9
Net Profit (NP)	32.7	36.1	37.4
Core NP	38.8	36.1	37.4
Consensus (NP)	N.A.	41.0	43.6
Earnings Revision	N.A.	-16%	-17%
Core EPS (sen)	28.4	26.4	27.3
Core EPS growth (%)	-11%	-7%	4%
NDPS (sen)	5.0	4.0	4.0
NTA per Share (RM)	4.28	4.50	4.74
Price to NTA (x)	0.9	0.9	0.9
PER (x)	14.3	15.3	14.8
Debt-to-Equity ratio(x)	N. Cash	N. Cash	N. Cash
Return on Asset (%)	5.4	4.8	4.8
Return on Equity (%)	6.6	5.9	5.8
Net Div. Yield (%)	1.2	1.0	1.0

Share Price Performance



	1 mth	3 mths	12 mths
Absolute (%)	4.9%	4.9%	-13.0%
Relative (%)	1.6%	2.0%	-16.2%

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29 August 2018

Results Highlights								
FY Mar	1Q19	4Q18	QoQ %	4Q17	YoY%	3M19	3M18	YoY%
Revenue	158.0	196.7	-20%	220.1	-28%	158.0	178.7	-12%
Op Profit	9.7	13.4	-28%	25.7	-62%	9.7	10.6	-8%
Pretax Profit	10.0	13.5	-26%	25.6	-61%	10.0	10.7	-6%
Tax	(2.1)	(5.9)	-64%	(4.8)	-56%	(2.1)	(2.0)	5%
MI	(1.1)	0.8	-245%	(3.9)	-71%	(1.1)	(0.9)	25%
Net Profit	6.8	8.4	-19%	16.8	-60%	6.8	7.7	-13%
Core Net Profit	1.9	11.3	-83%	18.4	-90%	1.9	10.2	-81%
EPS (sen)	5.0	6.1	-19%	12.3	-60%	5.0	5.7	-13%
Net DPS (sen)	0.0	5.0	N.M.	0.0	N.M.	0.0	5.0	-100%
EBIT %	6.2%	6.8%		11.7%		6.2%	5.9%	
PBT%	6.4%	6.9%		11.6%		6.4%	6.0%	
Tax %	21.1%	43.7%		18.9%		21.1%	18.9%	
CPO Avg	2,416	2,467	-2%	3,201	-25%	2,416	2,681	-10%
FFB Prod ('000 mt)	18,959	18,915	0%	19,112	-1%	18,959	15,527	22%

Source: Company, Kenanga Research

Segmental Breakdown								
FY Mar	1Q19	4Q18	QoQ %	4Q17	YoY%	3M19	3M18	YoY%
Segmental Revenue								
- Oleochemical	76.2	95.6	-20.3%	112.4	-32%	76.2	97.2	-22%
- Upstream Plantation	57.1	72.6	-21%	83.7	-32%	57.1	55.9	2%
- Healthcare	20.2	22.7	-11%	21.9	-8%	20.2	21.2	-5%
- Others	4.4	5.8	-24%	2.2	104%	4.4	4.4	1%
Total Group	158.0	196.7	-20%	220.1	-28%	158.0	178.7	-12%
Segmental Profit	1Q19	4Q18	QoQ %	4Q17	YoY%	3M19	3M18	YoY%
- Oleochemical	0.9	(0.3)	n.m	5.6	-85%	0.9	2.0	-58%
- Upstream Plantation	3.5	4.9	-29%	13.7	-74%	3.5	2.5	37%
- Healthcare	5.2	7.6	-31%	6.4	-19%	5.2	4.9	5%
- Others	0.2	1.2	-85%	(0.0)	-848%	0.2	1.0	-82%
- Share of associate profit	0.3	0.1	417%	(0.1)	-399%	0.3	0.1	144%
Total PBT	10.0	13.5	-26%	25.6	-61%	10.0	10.7	-6%
Segmental PBT Margins	1Q19	4Q18		4Q17		3M19	3M18	
- Oleochemical	1%	n.m		5%		1%	2%	
- Upstream Plantation	6%	7%		16%		6%	5%	
- Healthcare	26%	33%		29%		26%	23%	

Source: Company, Kenanga Research

Sum-of-Parts Valuation					
Segment	Valuation	Note	Fair Value (RM'm)	PE/RNAV discount	Net Income (RM'm)
Oleochemicals	13x PER on CY18E earnings	20% discount to Plantation small caps valuation	17	13.0	1.3
Hospital	18x PER on CY18E earnings	Small cap healthcare average valuation	317	18.0	17.6
Plantation	14.5x PER on CY18E earnings	10% discount to Plantation small caps valuation	182	14.5	12.6
Sum-Of-Parts (RM m)			516		
Conglomerate discount			15%		
Adj. Sum-Of-Parts (RM m)			439		
No of shares (m)			137		
TP (RM)			3.20		

Source: Kenanga Research

29 August 2018

Peer Comparison

Name	Last Price	Market Cap	Shariah Compliant	Current FYE	Revenue Growth		Core Earnings Growth		PER (x) - Core Earnings			PBV (x)		ROE (%)	Net Div. Yld. (%)	Target Price (RM)	Rating
	(RM)	(RM'm)			1-Yr. Fwd.	2-Yr. Fwd.	1-Yr. Fwd.	2-Yr. Fwd.	Hist.	1-Yr. Fwd.	2-Yr. Fwd.	Hist.	1-Yr. Fwd.	1-Yr. Fwd.	1-Yr. Fwd.		
STOCKS UNDER COVERAGE																	
CB INDUSTRIAL PRODUCT HLDG	1.26	658.4	Y	12/2018	-26.1%	3.6%	-3.9%	-3.3%	7.8	8.1	8.4	0.9	0.8	10.6%	4.0%	1.30	MP
FGV HOLDINGS BHD	1.65	6,019.5	Y	12/2018	-0.2%	4.0%	-67.6%	127.3%	56.2	173.4	76.3	1.0	1.0	0.6%	0.6%	1.60	MP
GENTING PLANTATIONS BHD	9.44	7,597.9	Y	12/2018	13.6%	12.8%	6.4%	21.3%	22.5	21.6	18.2	1.6	1.6	7.3%	2.5%	10.75	OP
HAP SENG PLANTATIONS HLDGS	2.25	1,799.3	Y	12/2018	-9.5%	2.9%	-34.0%	13.4%	13.5	20.2	17.8	0.9	0.9	4.3%	3.1%	2.10	MP
IJM PLANTATIONS BHD	2.41	2,122.2	Y	03/2019	-8.7%	9.6%	-7.5%	43.2%	30.2	32.6	22.8	1.2	1.2	3.7%	1.7%	1.60	UP
IOI CORP BHD	4.55	27,784.3	Y	06/2019	0.1%	3.5%	18.2%	6.3%	30.6	25.9	24.4	3.1	3.0	11.7%	2.1%	4.40	MP
KUALA LUMPUR KEPONG BHD	24.78	26,389.8	Y	09/2018	-10.9%	2.5%	-11.8%	29.1%	24.7	28.0	21.7	2.3	2.2	8.0%	2.0%	24.20	MP
PPB GROUP BERHAD	16.74	23,814.3	Y	12/2018	12.6%	6.3%	-7.2%	5.5%	19.6	21.1	20.0	1.1	1.1	5.3%	1.4%	18.60	OP
SIME DARBY PLANTATION BHD	5.30	36,044.4	Y	12/2018	-6.0%	-52.9%	4.1%	-43.0%	29.5	28.4	49.8	2.8	2.7	10.0%	0.4%	5.60	MP
SOUTHERN ACIDS MALAYSIA BHD	4.09	560.1	Y	03/2019	-7.1%	3.2%	-7.0%	3.5%	14.3	15.3	14.8	1.0	0.9	6.0%	1.0%	3.20	UP
TA ANN HOLDINGS BERHAD	2.63	1,169.4	Y	12/2018	-19.3%	3.0%	-19.1%	2.4%	9.3	11.5	11.2	0.9	0.8	7.4%	2.7%	2.85	OP
TSH RESOURCES BHD	1.19	1,643.1	Y	12/2018	6.9%	6.3%	-35.4%	26.3%	16.1	25.3	20.1	1.0	1.0	4.4%	1.0%	1.10	UP
UNITED MALACCA BHD	6.16	1,291.6	Y	04/2019	-4.2%	1.9%	37.9%	30.7%	33.6	24.3	18.6	0.8	0.7	3.0%	2.4%	6.20	MP
Simple Average					-4.5%	0.5%	-9.7%	20.2%	23.7	33.5	24.9	1.4	1.4	6.3%	1.9%		

Source: Bloomberg, Kenanga Research

29 August 2018

Stock Ratings are defined as follows:**Stock Recommendations**

OUTPERFORM : A particular stock's Expected Total Return is MORE than 10%
MARKET PERFORM : A particular stock's Expected Total Return is WITHIN the range of -5% to 10%
UNDERPERFORM : A particular stock's Expected Total Return is LESS than -5%

Sector Recommendations***

OVERWEIGHT : A particular sector's Expected Total Return is MORE than 10%
NEUTRAL : A particular sector's Expected Total Return is WITHIN the range of -5% to 10%
UNDERWEIGHT : A particular sector's Expected Total Return is LESS than -5%

*****Sector recommendations are defined based on market capitalisation weighted average expected total return for stocks under our coverage.**

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