

7 April 2021

Consumer Cyclical | Consumer Products

Malayan Flour Mills (MFL MK)

Not Rated

Hatching Into An ASEAN Consumer Play

Fair Value (Return): MYR1.20 (+30%)
 Price: MYR0.92
 Market Cap: USD226m
 Avg Daily Turnover (MYR/USD) 10.6m/2.64m

- SOP-based FV of MYR1.20.** Malayan Flour Mills is on the cusp of a rerating, as it transforms itself into an ASEAN consumer play. It should benefit from the recovery in consumption due to its dominant position in the flour market, while the recent proposed disposal of its 49% stake in its poultry unit to US-based Tyson Foods is a boon for earnings. Our fair value implies a target P/E of between 18.5x for 2021F and 10.5x for 2022F, vs peers that trade at historical P/Es of 12-22x and forward P/Es of 11-21x.
- Flour division provides a steady anchor.** MFM's flour division is capitalising on a recovery in consumption which – together with the rising consumption of flour per capita in Vietnam and Indonesia, where MFM's expansions have taken place over the last few years – will ensure continued earnings growth from this division. In Vietnam, consumption of flour per capita is 16kg, while in Indonesia, it is 21kg and Malaysia, 35kg. This indicates that the growth potential in Vietnam is huge, and MFM's dominant positioning will enable it to benefit. In Indonesia, MFM's 30%-owned JV company has also been expanding rapidly, doubling its capacity over the last two years, in order to expand its geographical reach to other provinces.
- Turnaround of poultry division is the biggest catalyst.** MFM's poultry division has been in the red over the last three years, with the largest loss recorded in FY20, on the back of falling live chicken prices (-25% in 2H20). While live chicken prices have recovered slightly, this should no longer have a significant impact on profits, given the recent tripling in capacity of its processed poultry products plant. Unlike live chicken prices, selling prices of processed poultry products are less volatile. In 2019, live bird sales comprised 50% of poultry revenue, vs 10% currently. The new plant was running at a capacity utilisation of 40-50% at end-2020. This is targeted to rise to 70-80% in the next 18 months.
- Disposal of 49% stake to Tyson Foods.** This turnaround is likely to come on the back of the recent proposed disposal of a 49% stake in its poultry business to US-based Tyson Foods for MYR420m. While MFM will no longer be able to consolidate this division's earnings, the benefits in the form of producing more value-added Tyson-brand products, offtake agreements with Tyson's entities like Mac Food (supplier of McDonald's Malaysia) and opportunities for new export markets, given its plant's *halal* status, far outweighs the costs. There are EBIDTA profit guarantees that come with the disposal, of MYR58m for FY21, MYR141m in FY22 and MYR173m in FY23. With the profit guarantees and penalties in place, we believe MFM has every incentive to achieve these EBITDA targets.
- 5-year earnings CAGR of 32.3%.** Our fair value of MYR1.20 is based on a 14x 2021F P/E for the flour division and a book value based on the disposal price for the poultry division. Dividend yields, based on a 50% payout, are also likely to rise to 3.8-7.6% in 2021-2023F.

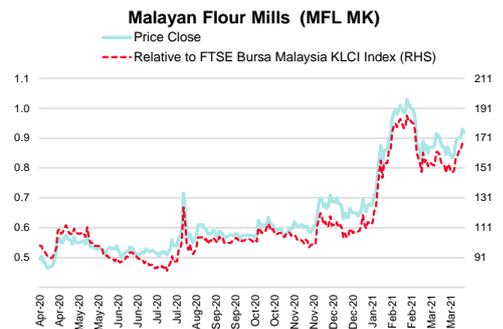
Analyst

Hoe Lee Leng
 +603 9280 8860
hoe.lee.leng@rhbgroup.com



Share Performance (%)

	YTD	1m	3m	6m	12m
Absolute	41.5	5.7	42.6	60.0	104.4
Relative	44.1	6.6	44.0	55.2	85.3
52-wk Price low/high (MYR)				0.47	1.03



Source: Bloomberg

Forecasts and Valuation	Dec-19	Dec-20	Dec-21F	Dec-22F	Dec-23F
Total turnover (MYRm)	2,682	2,681	2,791	2,929	3,175
Recurring net profit (MYRm)	36	(2)	66	117	141
Recurring net profit growth (%)	2.4	(105.5)	-	77.0	20.9
Recurring P/E (x)	24.75	na	14.09	7.96	6.58
P/B (x)	0.8	0.9	0.8	0.8	0.8
P/CF (x)	6.33	4.51	11.81	4.64	4.64
Dividend Yield (%)	3.3	1.1	3.8	6.5	7.6
EV/EBITDA (x)	11.67	13.91	8.30	5.78	5.12
Return on average equity (%)	4.5	0.5	6.1	10.3	11.8
Net debt to equity (%)	73.6	66.9	70.6	62.9	56.0

Source: Company data, RHB

Note:

Small cap stocks are defined as companies with a market capitalization of less than USD1bn.

Financial Exhibits

Asia	Financial summary (MYR)	Dec-19	Dec-20	Dec-21F	Dec-22F	Dec-23F
Malaysia	Recurring EPS	0.04	(0.00)	0.07	0.12	0.14
Consumer Cyclical	DPS	0.03	0.01	0.04	0.06	0.07
Malayan Flour Mills	BVPS	1.09	1.06	1.09	1.15	1.22
MFL MK	Return on average equity (%)	4.5	0.5	6.1	10.3	11.8
Not Rated						
	Valuation metrics	Dec-19	Dec-20	Dec-21F	Dec-22F	Dec-23F
	Recurring P/E (x)	24.75	na	14.09	7.96	6.58
	P/B (x)	0.8	0.9	0.8	0.8	0.8
	FCF Yield (%)	(8.4)	14.2	(4.4)	10.8	10.8
	Dividend Yield (%)	3.3	1.1	3.8	6.5	7.6
	EV/EBITDA (x)	11.67	13.91	8.30	5.78	5.12
	EV/EBIT (x)	22.26	35.74	13.01	7.82	6.70
	Income statement (MYRm)	Dec-19	Dec-20	Dec-21F	Dec-22F	Dec-23F
	Total turnover	2,682	2,681	2,791	2,929	3,175
	Gross profit	260	224	318	414	469
	EBITDA	143	117	209	298	337
	Depreciation and amortisation	(68)	(72)	(76)	(78)	(79)
	Operating profit	75	46	133	220	258
	Net interest	(18)	(17)	(21)	(22)	(21)
	Pre-tax profit	78	37	114	201	243
	Taxation	(18)	(16)	(31)	(54)	(66)
	Reported net profit	43	5	66	117	141
	Recurring net profit	36	(2)	66	117	141
	Cash flow (MYRm)	Dec-19	Dec-20	Dec-21F	Dec-22F	Dec-23F
	Change in working capital	21	129	(80)	(24)	(56)
	Cash flow from operations	139	205	79	201	200
	Capex	(213)	(74)	(120)	(100)	(100)
	Cash flow from investing activities	(267)	(89)	(120)	(100)	(100)
	Dividends paid	(26)	(25)	(35)	(61)	(71)
	Cash flow from financing activities	291	(37)	(55)	(81)	(121)
	Cash at beginning of period	169	331	405	308	328
	Net change in cash	164	79	(97)	20	(20)
	Ending balance cash	331	405	308	328	308
	Balance sheet (MYRm)	Dec-19	Dec-20	Dec-21F	Dec-22F	Dec-23F
	Total cash and equivalents	331	405	308	328	308
	Tangible fixed assets	1,126	1,126	1,170	1,192	1,213
	Total investments	132	166	166	166	166
	Total assets	2,582	2,582	2,597	2,667	2,740
	Short-term debt	955	939	939	939	939
	Total long-term debt	226	231	211	191	141
	Total liabilities	1,401	1,417	1,384	1,368	1,335
	Total equity	1,181	1,165	1,213	1,299	1,406
	Total liabilities & equity	2,582	2,582	2,597	2,667	2,740
	Key metrics	Dec-19	Dec-20	Dec-21F	Dec-22F	Dec-23F
	Revenue growth (%)	10.6	(0.0)	4.1	4.9	8.4
	Recurrent EPS growth (%)	(41.2)	(105.2)	0.0	77.0	20.9
	Gross margin (%)	9.7	8.3	11.4	14.2	14.8
	Operating EBITDA margin (%)	5.3	4.4	7.5	10.2	10.6
	Net profit margin (%)	1.6	0.2	2.4	4.0	4.4
	Dividend payout ratio (%)	69.8	186.6	53.6	51.9	50.1
	Capex/sales (%)	7.9	2.7	4.3	3.4	3.1
	Interest cover (x)	2.53	1.23	3.79	6.38	7.72

Source: Company data, RHB

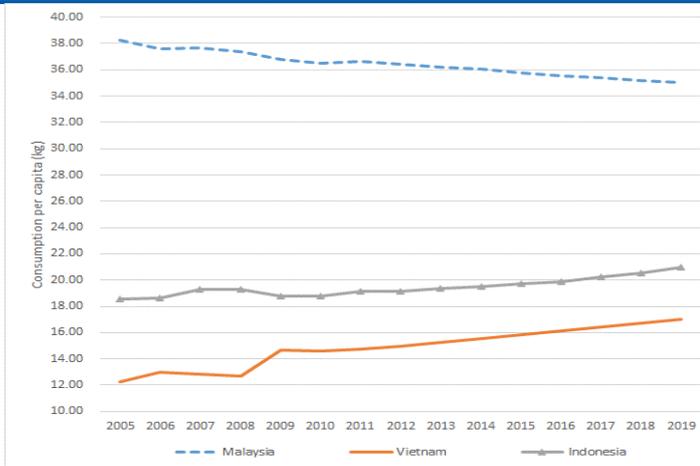
Prime beneficiary of consumer demand recovery

We believe MFM is evolving to become a full-fledged ASEAN consumer play, with its recent strategic disposal of a 49% stake in its poultry division to Tyson Foods. This should enable it to bounce back to profitability after three consecutive years of losses at this division, as MFM will be able to capitalise on Tyson Foods' range of value-added products, as well as benefit from offtake agreements to supply to the latter's customers. The flour division will remain a steady anchor, providing consistent growth via its exposure in Vietnam, Indonesia and Malaysia.

MFM's flour division is capitalising on a recovery in consumption, with the advent of the vaccine and the hotel, restaurant and café (HoReCa) sector being reopened. This, together with rising consumption of flour per capita in Vietnam and Indonesia – where MFM's expansions have taken place over the last few years – will ensure continued earnings growth from this division. In Vietnam, consumption of flour per capita is at 16kg. In Indonesia, it is at 21kg and Malaysia, 35kg. The gap widens further when compared to China and India, where consumption per capita is at 60kg. This indicates that the growth potential in Vietnam is huge, and MFM's dominant positioning will enable it to benefit. MFM expanded its capacity in Vietnam by 50% in 2016 to 1,500 tonnes per day, further cementing its market share reach.

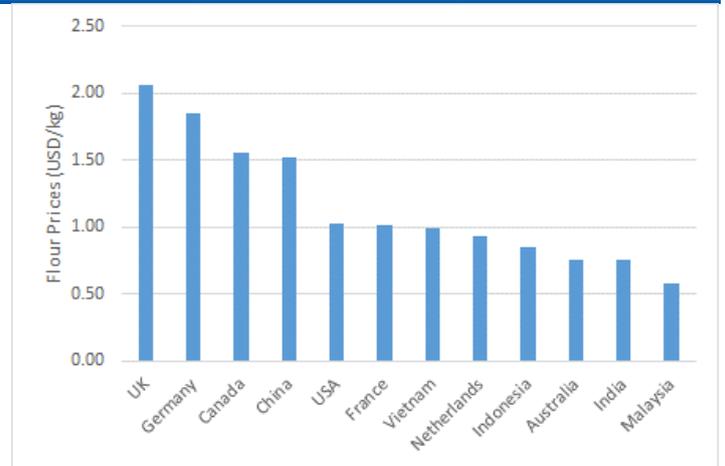
In Indonesia, MFM's 30%-owned JV company has also been expanding rapidly, doubling its capacity over the last two years, in order to expand its geographical reach to other provinces. Its two newest plants in Medan and Makassar were completed in end-2020, and will propel PT Bungasari's growth, adding capacity of 1,400 tonnes per day to bring total capacity to 3,400 tonnes per day. This will enable MFM to also benefit from the growing urbanisation trend in Indonesia in North Sumatra and South Sulawesi. In 2019, this JV contributed as much as MYR14m in profit to MFM's bottomline, although the amount shrank to MYR1m in 2020 due to higher wheat prices and the weaker IDR. Capacity utilisation in Indonesia fell to 60-70% in 2020, from 80% in 2018-2019. Looking ahead, with the doubling of capacity in Indonesia and the anticipated recovery in consumption post-COVID-19, a recovery in contributions from this JV should also strengthen MFM's bottomline.

Figure 1: Wheat per capita consumption trends



Source: Organisation for Economic Co-operation and Development (OECD)

Figure 2: A comparison of global flour prices



Source: Global Product Prices.com

Vietnam and Indonesia, unlike Malaysia are deregulated markets when it comes to flour prices. This would imply that MFM is able to pass on rising costs to customers via selling price hikes, if the need arises. We understand selling price increases are able to be passed on more easily in Vietnam, given its dominant market share there. In Malaysia, the ceiling price of flour is applicable only to general purpose flour, which only makes up 5% of MFM's sales volumes. However, MFM may not be able to raise selling prices easily in Malaysia, as it is not the dominant market player here.

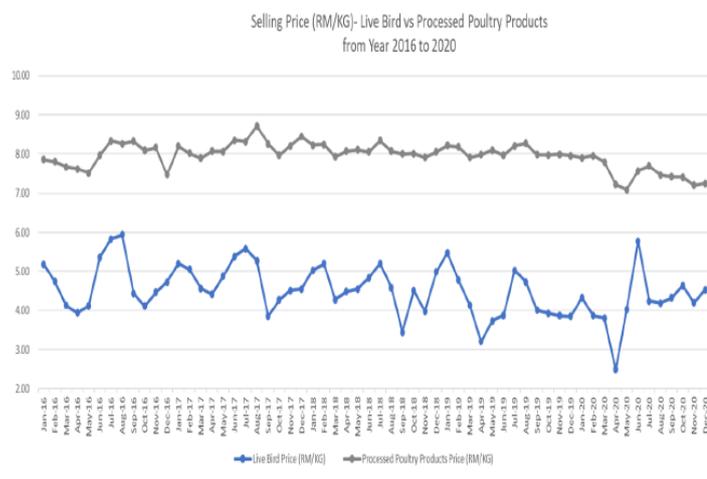
Nevertheless, we estimate that, even though revenue contributions for the flour division from Malaysia make up 55% of the total (the remaining 45% comes from Vietnam), profit contributions are likely the other way around – as profit margins in Vietnam are generally higher. Wheat prices have been on the rise of late, up 40% over the last six months. Given that raw materials like wheat account for 90% of costs, this is likely to crimp margins, especially as it is unlikely that MFM would be able to pass on all its costs to customers immediately. MFM does, however, practice hedging on a 6-month average rolling basis, to mitigate the risk of price volatility.

We highlight that, in 2020, MFM managed to post higher YoY EBIT margins of 6.1% (from 5.8%) for the flour division despite wheat prices rising 13% YoY. In our forecasts, we have assumed EBIT margins for this division will decline slightly to 5-5.5% in FY21-23F (from 5.5-6% in the last two years).

Turnaround of its poultry division is the biggest catalyst. MFM's poultry division has been recording losses over the last three years, with the largest one booked in FY20. This was on the back of live chicken prices, which fell 25% from June to Dec 2020. While live chicken prices have since recovered by 8% at end-February, this volatility should no longer have a significant impact on MFM's profits, given the recent expansion of its processed poultry products plant.

In 2019, live bird sales comprised 50% of its poultry revenue, compared to 10% currently. This change happened as a result of the commissioning of MFM's newly expanded poultry processing plant in Feb 2020 – where processing capacity rose to 280,000 birds/day (from 90,000). The plant was running at a capacity utilisation rate of 40-50% at end-2020, and this is targeted to increase to 70-80% within the next 18 months. As selling prices of processed poultry products are not controlled, and are market-dependant, MFM would not be subject to the price volatilities seen in the live bird market. We understand selling prices of live birds generally range between MYR4.00 and MYR6.00 per kg, while processed products are priced between MYR7.00 and MYR9.00 per kg. We believe the turnaround of this business is the biggest catalyst to MFM's earnings.

Figure 3: ASPs of live birds vs processed products



Source: Company data

Figure 4: Tyson's processed poultry products



Source: Company

Disposal of 49% stake to Tyson Foods. This turnaround is likely to come on the back of the recent proposed disposal of a 49% stake in its poultry business (under the company Dindings Supreme (DSSB)) to Tyson Foods. While MFM will no longer be able to consolidate its poultry earnings, the benefits from collaboration in the form of producing more value-added Tyson-branded products, offtake agreements with Tyson Foods' entities like Mac Food (supplier of McDonald's Malaysia) and opportunities for new export markets given its plant's *halal* status, far outweighs the costs.

The MYR420m consideration is to be paid in stages – with MYR140m initially, followed by the next MYR140m if EBITDA is MYR141m in FY22, and the last MYR140m if EBITDA is at MYR173m in FY23. FY21's profit guarantee is MYR58m. After five years, Tyson has a call option to acquire another 11% stake. With the profit guarantees and penalties in place, MFM has every incentive to achieve these EBITDA targets. If MFM does not hit the EBITDA target in 2021, a penalty of MYR12-15m is to be paid to Tyson, while for 2022 and 2023, the penalty would be 1.5x the shortfall amount.

Long-term offtake agreement with Mac Food will double output. Within the agreement with Tyson, there are also several others – including a 5-year supply agreement between MFM and Mac Food (the supplier of McDonald's Malaysia) to support the domestic requirement of Mac Food in Malaysia. MFM is targeting to supply up to 75% of Mac Food's raw chicken requirements in Malaysia, which is estimated to amount to an additional volume of 12,000 tonnes per year. We understand this is a conservative estimate for the initial period. This would translate to 80,000-90,000 birds a day, or double its previous processing output in 2019.

Grain supply agreement will boost flour division earnings. Besides this agreement, there is also a 10-year grain supply agreement between MFM's 51% grain-trading subsidiary and DSSB to supply all its corn and soybean meal requirements. The grain trading subsidiary sits within MFM's flour division. This agreement would also help to boost earnings in the flour division going forward, as the volume of chicken rises.

Synergies abound. We believe there is more potential for further offtake agreements, as Tyson Foods intends to leverage of MFM's *halal* certified status to add *halal* products to its line-up of products. MFM will also be able to introduce more Tyson Foods products to the Malaysian market, including the pet food variety, ready meals etc. Besides this, MFM intends to expand its geographical reach via Tyson Foods' global distribution capabilities, particularly targeting the market for *halal*-certified products in Middle East and Singapore. With the potential for more variations of processed food and a wider geographical reach, MFM is also building a new further processing plant at its old plant site to cater for this new market. The plant will triple its existing further processed products capacity at a cost of MYR180m, and is expected to be completed by end-2022.

If all targets are met, the poultry division will see a significant spike in earnings to profitability. In our forecasts, we have not stripped out the disposal of DSSB to Tyson Foods, which is due to be completed by 1H21. We have also assumed that MFM achieves the EBITDA targets set by Tyson Foods, which will enable it to post a significant turnaround at its poultry division in FY21 and beyond.

Financials

Strong earnings CAGR. We project MFM to post a 5-year earnings CAGR of 32.3% to 2023. For FY21, we project earnings to post a strong recovery to a profit of MYR66m, from a core net loss of MYR2m in FY20. This will come on the back of an assumed turnaround in the poultry division earnings.

Latest results. MFM recorded a core net loss in FY20 of MYR2m, coming from losses incurred at its poultry division (EBIT loss of MYR70m). This was offset by higher EBIT contributions from the flour division (+7%), which was achieved despite the increase of raw material prices.

Figure 5: Quarterly EBIT margin trends by segment



Figure 6: Global wheat prices (USD/bushel)



Source: Company data, RHB

Source: Macrotrends.net

Net gearing to improve. As at end-FY20, MFM's net gearing was at 71%, down from 77% in FY19. This should improve further from FY21F onwards, as MYR126m of the initial proceeds of the disposal will be used to repay debt. Operating cash flow is decent, at MYR100-200m per year. In terms of capex plans, besides the new further processed product plant, MFM intends to expand its broiler capacity by either buying more land to build more farms or increasing the number of its contract farmers. This would enable MFM to service its poultry processing plant's needs as its customer base grows. We have projected a capex of MYR100-120m per year for FY21-23F.

MFM has no official dividend policy but has been paying 50-120% of earnings as dividends over the last few years. Assuming that the payout ratio remains at 50-55% for the next few years, this would translate to an admirable net yield of 3.8-7.6% for FY21-23F.

Valuation

Fair value of MYR1.20. We believe MFM is on the cusp of a rerating, especially once it proves it is able to achieve the EBITDA targets for the poultry business. Our fair value of MYR1.20 is based on a SOP calculation, which includes a target P/E of 14x 2021F for the flour division and a book value based on disposal price for the poultry division. This implies a target P/E of between 18.5x 2021F and 10.5x 2022F. Its peers trade at historical P/Es of 12-22x. Its dividend yields, based on a 50% payout ratio, are also likely to rise to 3.8-7.6% in 2021-2023F.

Risks include:

- i. Continued losses at the poultry division, should MFM not be able to improve sales volumes and margins;
- ii. Inability to pass on higher raw material prices like wheat and grains; and
- iii. Diseases that affect livestock.

Figure 7: Peer comparison

	FYE	Price (local ccy)	Market cap (USDm)	P/E FY19	P/E FY20	P/E FY21F	Div yield FY20	ROE FY20	P/BV FY20	Net Profit Growth (%)		
										FY20	FY21F	FY22F
PPB Group	Dec/21	18.50	6,358	22.8	20.3	20.7	1.6	6.0	1.2	12.7	8.4	8.3
QL Resources	Mar/21	6.07	3,569	67.1	62.1	55.2	0.5	11.3	6.7	8.1	12.6	13.2
Leong Hup International	Mar/21	0.70	617	17.0	22.9	14.8	0.8	6.7	1.5	(25.9)	55.2	17.8
CCK Consolidated	Dec/21	0.69	104	12.9	12.1	11.6	0.7	12.3	1.5	6.9	4.3	7.5
CAB Cakaran	Sep/21	0.42	70	23.9	107.0	na	na	1.6	0.6	(77.7)	na	na
Teo Seng Capital	Dec/21	0.79	56	3.9	55.8	na	na	1.4	0.7	(93.0)	na	na
Lay Hong	Mar/21	0.34	54	30.4	66.5	na	2.2	2.0	0.7	(54.2)	na	na
WEIGHTED AVE				37.0	35.1	30.7	1.2	7.8	3.0			
Malayan Flour Mill	Dec/21	0.92	929	24.8	n.m.	14.1	1.1	0.4	0.9	(105.5)	>1000	77.0

Note: Prices are as at 2 Apr 2021

Source: RHB, Bloomberg, Company data

Figure 8: SOP valuation

	Valuation basis	MYRm
Flour and grains trading	14x 2021F P/E	783.87
Integrated poultry	Based on 100% stake of Tyson's disposal price	437.14
TOTAL SOP		1,221.01
No of shares		1,010.28
SOP/share (MYR)		1.21

Source: RHB

Background

MFM is involved in two main businesses – flour milling and grain trading and poultry farming and processing.

Figure 9: Segmental revenue breakdown

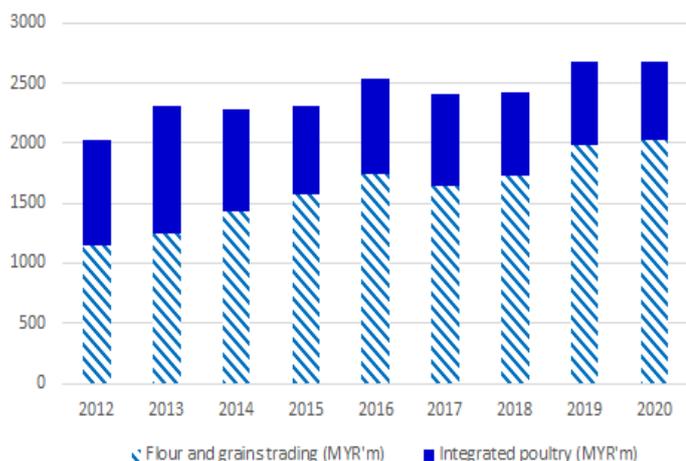


Figure 10: Segmental EBIT breakdown



Source: Company, RHB

Source: Company, RHB

Its flour milling division has operations in Malaysia, Vietnam and Indonesia (through its 30% stake in the JV, PT Bungasari Flour Mills). The flour and grains trading division contributed the largest chunk of revenue in FY20 of 75%, up from 56% eight years ago. MFM is one of the top three largest flour millers in Malaysia with an estimated market share of 20-25%, with its 2,000 tonnes a day milling capacity. In Vietnam, it is the largest flour miller in the country with an estimated 50% market share in the north and a 18-20% market share in the south, with its 2,600 tonnes per day capacity. In Indonesia, it is one of the five largest flour millers, with a 7-8% market share and a production capacity of 3,400 tonnes per day. MFM sells mostly non-general purpose flour products, with general purpose flour only making up less than 5% of volumes.

Its integrated poultry division consists of feed milling, breeder and broiler farming and poultry processing, operating via its 100% owned-subsiidiary Dindings Supreme. MFM produces 60m chicks a year, of which only 10% are sold in the live market, while the remaining 90% are processed into dressed chicken, marinated products and further processed products. MFM’s new state-of-the-art poultry processing plant which commenced operations in Feb-2020, has a capacity of 280,000 birds a day (100m a year) and currently services customers like McDonald’s, Texas Chicken and KFC, amongst others.

Management. MFM is helmed by Teh Wee Chye, its major shareholder and managing director. The other major shareholder is non-Independent Non-Executive Chairman Tan Sri Dato’ Seri Utama Arshad Ayub, whose son, Azhari Arshad, is an executive director of the firm. Azhari is also in charge of business development and corporate affairs. Together, with related parties, they hold around 30.2% of the company.

Recommendation Chart



Source: RHB, Bloomberg

Date	Recommendation	Target Price	Price
2021-04-05			

Source: RHB, Bloomberg

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Buy:	Share price may exceed 10% over the next 12 months
Trading Buy:	Share price may exceed 15% over the next 3 months, however longer-term outlook remains uncertain
Neutral:	Share price may fall within the range of +/- 10% over the next 12 months
Take Profit:	Target price has been attained. Look to accumulate at lower levels
Sell:	Share price may fall by more than 10% over the next 12 months
Not Rated:	Stock is not within regular research coverage

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KUALA LUMPUR

RHB Investment Bank Bhd
Level 3A, Tower One, RHB Centre
Jalan Tun Razak
Kuala Lumpur 50400
Malaysia
Tel : +603 9280 8888
Fax : +603 9200 2216

JAKARTA

PT RHB Sekuritas Indonesia
Revenue Tower, 11th Floor, District 8 - SCBD
Jl. Jendral Sudirman Kav 52-53
Jakarta 12190
Indonesia
Tel : +6221 509 39 888
Fax : +6221 509 39 777

BANGKOK

RHB Securities (Thailand) PCL
10th Floor, Sathorn Square Office Tower
98, North Sathorn Road, Silom
Bangrak, Bangkok 10500
Thailand
Tel: +66 2088 9999
Fax :+66 2088 9799

SINGAPORE

RHB Bank Berhad (Singapore branch)
90 Cecil Street
#04-00 RHB Bank Building
Singapore 069531