

29 August 2019

## Southern Acids (M) Berhad Challenging Prospects

Southern Acids (M) Berhad (SAB)'s 1Q20 Core Net Profit (CNP) of RM5.2m came in below our expectation at 20% of forecast but in line with consensus' RM20.9m at 25%, dragged by lower average CPO prices and higher operating costs for its oleochemical segment. No dividend was declared as expected. Cut FY20-21E CNP by 14-22% to RM23.0-27.5m to reflect the thinner oleochemical margin. Maintain UNDERPERFORM with a higher TP of RM2.90 (from RM2.50), as we roll over to CY20.

**Below our, but within consensus, expectation.** 1Q20 CNP of RM5.2m came below our expectation but within consensus at 20%/25%. The negative deviation stemmed from higher-than-expected operating costs for its oleochemical segment. 1Q20 FFB output of 22.1k metric tons (MT) came in line with our full-year estimate of 88.6k MT, at 25%. No dividend was declared, as expected.

**Saved by healthcare.** YoY, 3M20 CNP declined (-30%) to RM3.8m (from a low base effect), due to: (i) lower average CPO prices (-18%) to RM1,978/MT, which was partially offset by a 17% increase in FFB output, and (ii) PBT margin compression (-3.0ppt) to -1.8% in its oleochemical segment due to higher operating costs. The decline in its plantation and oleochemical segments was partially mitigated by improvement (Revenue: +8%; PBT: +13%) in its healthcare segment, mainly due to slightly higher bed occupancy rate (+0.4ppt) and PBT margin expansion (+1.2ppt) from higher number of complex surgeries. QoQ, 1Q20 CNP increased 8x (from a low base effect) to RM5.2m, mainly attributed to: (i) normalisation of effective tax rate (-105.7ppt) to 22.4%, and (ii) 6% increase in FFB output.

**Headwinds ahead.** Moving forward, we believe its oleochemical segment outlook will continue to remain challenging amidst high operating cost and stiff competition in the market. Given its relatively smaller production size in the market, unit cost is likely to be higher due to lower economies of scale. Meanwhile, for its healthcare segment, we continue to expect growth to be driven by higher complex surgeries, leading to higher average revenue per patient (ARPP) as the company continues to recruit more specialists.

**Cut FY20-21E CNP by 14-22% to RM23.0-27.5m** as we update our assumptions for oleochemical segment to reflect thinner margins on higher operating costs.

**Maintain UNDERPERFORM with a higher TP of RM2.90** (from RM2.50) as we roll forward our valuation base year from CY19 to CY20 Sum-of-Parts (SoP). In our SoP valuation, we ascribed a higher Fwd. PER of 15x (from 13.5x), applying a 15% discount to upstream segment to reflect FFB production pick-up and higher CPO prices. Meanwhile, we maintain oleochemical segment at 11.0x Fwd. PER (average of small to mid-cap planters), ascribing 40% discount to the Fwd. PER to account for challenging business prospect. For healthcare segment, we ascribed a higher 22.0x PER on margin expansion from higher complex surgeries, while applying a conglomerate discount of 10% to arrive at our SoP TP of RM2.90.

**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:** RM3.61  
**Target Price:** RM2.90 ↑

**Expected Capital Gain:** -RM0.710 -19.7%  
**Expected Div. Yield:** RM0.050 +1.4%  
**Expected Total Return:** -RM0.660 -18.3%

**KLCI Index** 1,589.82

### Stock Information

Bloomberg Ticker	SA MK Equity
Bursa Code	5134
Listing Market	Main Market
Shariah Compliant	Yes
Shares Outstanding	136.9
Market Cap (RM m)	494.3
Par value per share (RM)	1.00
52-week range (H)	4.00
52-week range (L)	3.58
Free Float	47%
Beta	0.7
3-mth avg daily vol:	1,643

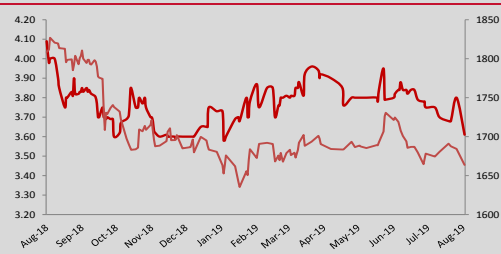
### Major Shareholders

Southern Palm Industry	31.3%
Lembaga Tabung Haji	13.0%
Southern Realty (Malaya)	8.4%

### Summary Earnings Table

FY Mar (RM m)	2019A	2020E	2021E
Turnover	598.6	656.8	699.9
EBIT	38.7	45.8	52.3
PBT	38.6	50.4	56.5
<b>Net Profit (NP)</b>	<b>21.5</b>	<b>23.0</b>	<b>27.5</b>
<b>Core NP</b>	<b>17.3</b>	<b>23.0</b>	<b>27.5</b>
Consensus (NP)	n.a.	20.9	20.3
Earnings Revision	n.a.	-14%	-22%
Core EPS (sen)	12.7	16.8	20.1
Core EPS growth (%)	-55%	32%	20%
NDPS (sen)	5.0	5.0	4.0
NTA per Share (RM)	4.39	4.51	4.67
Price to NTA (x)	0.8	0.8	0.8
PER (x)	28.5	21.5	18.0
Debt-to-Equity ratio(x)	N.Cash	N.Cash	N.Cash
Return on Asset (%)	2.4	3.1	3.9
Return on Equity (%)	2.9	3.7	4.3
Net Div. Yield (%)	1.4	1.4	1.1

### Share Price Performance



	1 mth	3 mths	12 mths
Absolute (%)	-3.7%	-5.0%	-11.7%
Relative (%)	-0.2%	-3.5%	1.2%

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## Results Highlights

FY Mar	1Q20	4Q19	QoQ %	1Q19	YoY%	3M20	3M19	YoY%
<b>Revenue</b>	<b>142.6</b>	<b>141.0</b>	<b>1%</b>	<b>158.0</b>	<b>-10%</b>	<b>142.6</b>	<b>158.0</b>	<b>-10%</b>
Op Profit	7.4	5.2	43%	10.4	-28%	7.4	10.4	-28%
Pretax Profit	7.5	4.7	59%	10.6	-29%	7.5	10.6	-29%
Tax	(1.7)	(6.1)	-72%	(2.1)	-21%	(1.7)	(2.1)	-21%
MI	(0.7)	1.8	nm	(1.1)	-42%	(0.7)	(1.1)	-42%
<b>Net Profit</b>	<b>5.2</b>	<b>0.5</b>	<b>904%</b>	<b>7.4</b>	<b>-30%</b>	<b>5.2</b>	<b>7.4</b>	<b>-30%</b>
<b>Core Net Profit</b>	<b>5.2</b>	<b>0.6</b>	<b>796%</b>	<b>7.4</b>	<b>-30%</b>	<b>5.2</b>	<b>7.4</b>	<b>-30%</b>
<b>EPS (sen)</b>	<b>3.8</b>	<b>0.4</b>	<b>895%</b>	<b>5.0</b>	<b>-24%</b>	<b>3.8</b>	<b>5.0</b>	<b>-24%</b>
Net DPS (sen)	0.0	5.0	nm	0.0	nm	0.0	0.0	nm
EBIT margin	5.2%	3.7%		6.6%		5.2%	6.6%	
PBT margin	5.3%	3.4%		6.7%		5.3%	6.7%	
Effective tax rate	22.4%	128.1%		19.9%		22.4%	19.9%	
<b>MPOB CPO Avg. (RM)</b>	<b>1,978</b>	<b>2,014</b>	<b>-2%</b>	<b>2,416</b>	<b>-18%</b>	<b>1,978</b>	<b>2,416</b>	<b>-18%</b>
<b>FFB Prod ('000 mt)</b>	<b>22,095</b>	<b>20,770</b>	<b>6%</b>	<b>18,959</b>	<b>17%</b>	<b>22,095</b>	<b>18,959</b>	<b>17%</b>

Source: Company, Kenanga Research

## Segmental Breakdown

FY Mar	1Q20	4Q19	QoQ %	1Q19	YoY%	3M20	3M19	YoY%
<b>Segmental Revenue</b>								
- Oleochemical	68.7	66.4	3.6%	76.2	-10%	68.7	76.2	-10%
- Upstream Plantation	47.8	50.5	-5%	57.1	-16%	47.8	57.1	-16%
- Healthcare	21.8	22.7	-4%	20.2	8%	21.8	20.2	8%
- Others	4.3	2.9	46%	4.4	-4%	4.3	4.4	-4%
<b>Total Group</b>	<b>142.6</b>	<b>142.5</b>	<b>0%</b>	<b>158.0</b>	<b>-10%</b>	<b>142.6</b>	<b>158.0</b>	<b>-10%</b>
<b>Segmental Profit</b>	<b>1Q20</b>	<b>4Q19</b>	<b>QoQ %</b>	<b>1Q19</b>	<b>YoY%</b>	<b>3M20</b>	<b>3M19</b>	<b>YoY%</b>
- Oleochemical	(1.2)	(0.1)	752%	0.9	nm	(1.2)	0.9	nm
- Upstream Plantation	2.2	(0.6)	nm	3.9	-44%	2.2	3.9	-44%
- Healthcare	6.1	6.2	-1%	5.4	13%	6.1	5.4	13%
- Others	0.4	(0.2)	nm	0.2	103%	0.4	0.2	103%
- Share of associate profit	0.1	(0.5)	nm	0.3	-63%	0.1	0.3	-63%
<b>Total PBT</b>	<b>7.5</b>	<b>4.7</b>	<b>59%</b>	<b>10.6</b>	<b>-29%</b>	<b>7.5</b>	<b>10.6</b>	<b>-29%</b>

Source: Company, Kenanga Research

## Sum-of-Parts Valuation

Segment	Valuation	Note	Fair Value (RM'm)	PE/RNAV discount	Net Income (RM'm)
Oleochemicals	11x PER on CY20E earnings	40% discount to Plantation small mid-caps valuation	12	11.0	1.1
Hospital	22x PER on CY20E earnings	Small cap healthcare average valuation	271	22.0	12.3
Plantation	15x PER on CY20E earnings	15% discount to Plantation small caps valuation	160	15.0	10.7
<b>Sum-Of-Parts (RM m)</b>			<b>444</b>		
Conglomerate discount			10%		
<b>Adj. Sum-Of-Parts (RM m)</b>			<b>400</b>		
No of shares (m)			137		
<b>TP (RM)</b>			<b>2.90</b>		

Source: Company, Kenanga Research

29 August 2019

## 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.		
<b>STOCKS UNDER COVERAGE</b>																	
CB INDUSTRIAL PRODUCT HLDG	0.840	425.4	Y	12/2019	-23.6%	31.9%	-36.5%	45.9%	8.4	13.2	9.1	0.6	0.6	4.4%	4.8%	0.850	MP
FGV HOLDINGS BHD	0.950	3,465.7	Y	12/2019	3.1%	3.5%	-162.9%	-768.3%	N.A.	N.A.	N.A.	0.9	0.9	-2.4%	0.0%	1.00	MP
GENTING PLANTATIONS BHD	10.00	8,972.0	Y	12/2019	1.3%	6.3%	14.0%	46.9%	56.4	53.9	39.8	2.0	2.1	3.9%	1.0%	8.80	UP
HAP SENG PLANTATIONS HLDGS	1.48	1,183.5	Y	12/2019	-0.2%	10.2%	-76.7%	310.3%	40.7	174.5	42.5	0.7	0.7	0.4%	0.7%	1.50	MP
IJM PLANTATIONS BHD	1.43	1,259.2	Y	03/2020	-5.1%	11.5%	119.1%	177.8%	N.A.	142.0	51.1	0.7	0.7	0.5%	0.4%	1.40	MP
IOI CORPORATION BHD	4.22	26,521.2	Y	06/2020	-7.7%	0.1%	24.1%	2.2%	34.9	28.1	27.5	2.9	2.7	9.9%	2.1%	4.10	MP
KUALA LUMPUR KEPONG BHD	23.48	25,005.4	Y	09/2019	-1.9%	6.5%	-25.5%	26.4%	28.0	37.6	29.8	2.4	2.4	5.8%	1.7%	21.50	UP
PPB GROUP BERHAD	18.80	26,744.9	Y	12/2019	7.5%	4.9%	23.4%	4.1%	28.3	23.0	22.1	1.3	1.2	5.6%	1.8%	16.00	UP
SIME DARBY PLANTATION BHD	4.86	33,459.0	Y	12/2019	71.7%	11.1%	88.6%	154.0%	285.9	121.5	48.6	2.5	2.5	3.2%	0.8%	4.00	UP
SOUTHERN ACIDS MALAYSIA BHD	3.61	494.3	Y	03/2020	9.7%	6.6%	32.5%	20.0%	28.5	21.5	18.0	0.8	0.8	3.8%	1.4%	2.90	UP
TA ANN HOLDINGS BERHAD	2.16	951.4	Y	12/2019	-7.8%	16.5%	-60.6%	117.0%	11.6	29.5	13.6	0.7	0.7	2.4%	1.9%	2.20	MP
TSH RESOURCES BHD	0.890	1,228.4	Y	12/2019	18.9%	12.0%	-8.2%	45.1%	24.8	26.9	18.5	0.9	0.8	3.2%	0.9%	0.900	MP
UNITED MALACCA BHD	5.15	1,079.9	Y	04/2020	15.3%	10.4%	-449.2%	78.8%	N.A.	N.A.	112.9	0.6	0.6	-0.4%	1.2%	5.00	MP
<b>Simple Average</b>					<b>6.2%</b>	<b>10.1%</b>	<b>-39.8%</b>	<b>20.0%</b>	<b>54.8</b>	<b>61.1</b>	<b>36.1</b>	<b>1.3</b>	<b>1.3</b>	<b>3.1%</b>	<b>1.4%</b>		

Source: Bloomberg, Kenanga Research

29 August 2019

**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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