

1QFY15 RESULTS UPDATE

8 June 2015

# Leon Fuat Berhad

Price : RM0.585

Market Capitalization : RM181.4 mln

Market : Main Market

Sector : Industrial Products

Recommendation : Buy

Bursa / Bloomberg Code: 5232 / LEFU MK

**LFB: 1QFY15 results**

| FYE Dec<br>(RM mln)   | Quarter-on-Quarter |        |       | Year-on-Year |       |
|-----------------------|--------------------|--------|-------|--------------|-------|
|                       | 1QFY15             | 4QFY14 | % chg | 1QFY14       | % chg |
| Turnover              | 140.3              | 124.4  | 12.8% | 111.4        | 26.0% |
| Operating profit      | 11.2               | 11.1   | 0.9%  | 7.5          | 50.7% |
| Finance costs         | (2.1)              | (2.0)  |       | (1.5)        |       |
| Pre-tax profit        | 9.2                | 9.1    | 0.9%  | 5.9          | 55.4% |
| Tax                   | (2.6)              | (2.4)  |       | (1.6)        |       |
| Net profit            | 6.6                | 6.7    | -1.1% | 4.3          | 55.3% |
| EPS (sen) - basic     | 2.1                | 2.2    | -0.9% | 1.4          | 55.1% |
| Op. profit margin     | 8.0%               | 9.0%   |       | 6.7%         |       |
| Pre-tax margin        | 6.5%               | 7.3%   |       | 5.3%         |       |
| Net profit margin     | 4.7%               | 5.4%   |       | 3.8%         |       |
| Net Assets/share (RM) | 0.74               |        |       |              |       |

## 1QFY15 Results Review

- LFB turned in a record turnover of RM140.3 mln in 1QFY15 (+26% y-o-y), its highest since the Group got listed in June 2013. This is commendable as the sales were achieved despite concerns on the overall economic slowdown and weakening consumer spending.
- 1QFY15 net profit too, rose by a substantial 55.3% y-o-y to RM4.3 mln. We consider the results in line with our expectations despite reaching only 23% of our estimate as we anticipate stronger net profit contribution in the coming quarters. Historically, 1Q appears to be the slowest quarter.

|                     | Y-o-Y        |              |              |
|---------------------|--------------|--------------|--------------|
|                     | 1QFY15       | 1QFY14       | % Chg        |
| <b>Revenue</b>      |              |              |              |
| Trading             | 50.1         | 41.3         | 21.3%        |
| Processing          | 90.2         | 70.0         | 28.8%        |
| Others*             | 0.1          | 0.1          | 35.2%        |
| <b>Group</b>        | <b>140.3</b> | <b>111.4</b> | <b>26.0%</b> |
| <b>Gross profit</b> |              |              |              |
| Trading             | 6.4          | 5.2          | 22.0%        |
| Processing          | 13.5         | 10.1         | 33.6%        |
| Others              | 0.0          | 0.0          | 82.4%        |
| <b>Group</b>        | <b>19.8</b>  | <b>15.3</b>  | <b>29.7%</b> |
| <b>GP margin</b>    |              |              |              |
| Trading             | 12.7%        | 12.6%        |              |
| Processing          | 14.9%        | 14.4%        |              |
| Others              | 26.1%        | 19.3%        |              |
| <b>Group</b>        | <b>14.1%</b> | <b>13.7%</b> |              |

\*refers to trading of specialized steel materials

- Both its trading and steel processing divisions registered healthy sales tonnage growth, with segmental turnover expanding 21.3% and 28.8% y-o-y respectively, which in turn contributed to the record topline number. Gross profit margin at Group level too, inched up to 14.1% in 1QFY15 vs. 13.7% a year ago.
- Sequentially, we note that despite the 12.8% growth in turnover, net profit actually declined 1.1% and this was largely caused by increase in opex and financing cost. Higher director remuneration and staff cost, depreciation charges and rental expenses were some of the reasons behind the rise in opex.
- Net gearing increased from 0.6x in December 2014 to 0.7x in March 2015. More than 90% of the borrowings are trade financing in nature and as such, we opine the rise in net gearing would not be a concern yet for now. We noted that the Group had utilized its trade lines to purchase more raw materials during the quarter under review. LFB's balance sheet remains supported by a BV/share of 74 sen.
- We leave our FY15 earnings estimate of RM29.0 mln unchanged at this juncture. We expect better net earnings performance from the remaining quarters. The Group has thus far demonstrated resilience in chalking up growth despite the challenging business environment. We understand from management there has not been any material change in business volume since the implementation of GST effective 1 April 2015, which is good news. We believe the management is proactively managing its cost structure to remain competitive. Overall, management has consistently expanded its earnings base on a gradual and steady basis, unlike its other peers in the industry which experienced more volatile swings in the earnings along with the changes in the commodity prices. In the medium term, the Group may also stand benefit from the Government's spending on infrastructure projects under the 11MP.
- No dividend was declared for the quarter under review.

## Recommendation

We maintain our **Buy** recommendation on LFB with an unchanged fair value of **75 sen**, which is derived from using a blended approach of 0.8x BV and 10x PER on FY15 earnings. We like LFB for its consistent earnings delivery track record, steady earnings growth and hands-on management. LFB's prospective valuation, at 6.3x FY15 PER remains undemanding in our opinion, and is supported by an attractive projected 5.1% net dividend yield. We believe the stock is under-appreciated by investors due to the neutral and at times, negative outlook on the steel industry, and hence, is not in favour with investors. Moreover, LFB's small market capitalization and illiquid trading volume could also be the deterring factors for larger institutional investors.

| Per Share Data     |       |       |       | P&L Summary           |       |       |       |       |
|--------------------|-------|-------|-------|-----------------------|-------|-------|-------|-------|
| FYE Dec            | FY13  | FY14  | FY15  | FYE Dec (RM mln)      | FY12  | FY13  | FY14  | FY15f |
| Book Value (RM)    | 0.65  | 0.72  | 0.78  | Revenue               | 437.2 | 455.3 | 489.2 | 511.5 |
| Cash Flow (sen)    | 11.1  | 10.8  | 11.4  | Operating profit      | 38.9  | 42.2  | 44.1  | 46.3  |
| Earnings (sen)     | 9.0   | 8.9   | 9.3   | Net Int Exp           | (5.5) | (6.8) | (6.7) | (6.6) |
| Net Dividend (sen) | 3.0   | 3.0   | 3.0   | Pre-tax Profit        | 33.4  | 35.4  | 37.4  | 39.7  |
| Payout Ratio (%)   | 36.1% | 33.8% | 32.1% | Eff. Tax Rate         | 27.9% | 27.1% | 26.3% | 27.0% |
| PER (x)            | 6.5   | 6.6   | 6.3   | Net Profit            | 24.1  | 25.8  | 27.5  | 29.0  |
| P/Cash Flow (x)    | 5.3   | 5.4   | 5.1   | Op. Profit Margin (%) | 8.9%  | 9.3%  | 9.0%  | 9.1%  |
| P/Book Value (x)   | 0.9   | 0.8   | 0.7   | Pre-tax Margin (%)    | 7.6%  | 7.8%  | 7.6%  | 7.8%  |
| Dividend Yield (%) | 5.1%  | 5.1%  | 5.1%  | Net Margin (%)        | 5.5%  | 5.7%  | 5.6%  | 5.7%  |
| ROE (%)            | 13.9% | 12.3% | 11.9% |                       |       |       |       |       |
| Net gearing (x)    | 0.6   | 0.6   | 0.7   |                       |       |       |       |       |

**LFB's last 12-month share price chart**



Source: Bloomberg

**RATING GUIDE**

|      |  |
|------|--|
| BUY  | Price appreciation expected to exceed 10% within the next 12 months                            |
| SELL | Price depreciation expected to exceed 10% within the next 12 months                            |
| HOLD | Price movement expected to be between -10% and +10% over the next 12 months from current level |

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