

Corporate Highlights

Briefing Note

22 April 2011

C.I. Holdings

Uncertainty Lies Ahead

Share Price : RM2.94
Fair Value : RM3.30
Recom **Market Perform**
(Maintained)

Table 1 : Investment Statistics (CIHLDG; Code: 2828)

Bloomberg: CIH MK

FYE	Turnover (RMm)	Net					Net					
		profit (RMm)	EPS (sen)	Growth (%)	PER (x)	C.EPS* (sen)	P/NTA (x)	Gearing (x)	P/CF (x)	ROE (%)	GDY (%)	
June												
2010a	516.4	38.1	26.8	65.7	14.0	-	4.7	0.34	13.9	25.7	3.5	
2011f	616.3	39.2	27.6	2.8	10.7	30.0	4.1	17.4	0.3	22.2	2.8	
2012f	725.8	38.6	27.2	-1.6	10.8	34.0	4.0	9.9	net cash	19.0	2.8	
2013f	860.0	40.5	28.5	5.1	10.3	37.0	3.9	7.2	net cash	17.5	2.9	

Main Market Listing / Non-Trustee Stock / Syariah-Approved Stock By The SC

* Consensus Based On IBES Estimates

- ◆ **Weak festive revenues due to slightly earlier timing of CNY, amongst other reasons.** During the analyst's briefing yesterday, management explained the reason for the flattish revenue growth of 1.7% yoy and -4.5% qoq during the 3Q, i.e. the festive season. The timing of the CNY which was earlier this year played a part in the weak yoy and also the decline in qoq revenues. Given that CNY trade activities usually begin six to eight weeks ahead of CNY itself, the earlier timing of CNY this year (as compared to last year) of two weeks caused quite a sizeable CNY trade volume to be reflected in Dec 2010 (2QFY11).
- ◆ **Contracting gross margins.** The higher sugar cost could be seen from CIH's gross margins in the 3QFY06/11, which contracted by 3.9%-pts qoq to 37.3%. We understand that the sugar price impact could be mitigated by an average price increase of 3-5% across the board for CIH's beverage division, although given that CIH is not generally the price leader, it would wait for competitors such as F&N and Coca-Cola to raise prices before it will.
- ◆ **Tweaking trade discounts.** As mentioned, CIH at the end of the 3QFY06/11 (Mar) started "tweaking" its trade discounts to mitigate the impact of the sugar price increase. Note that trade discounts are discounts of about 7-8% generally given to wholesalers and other distributors. We understand that CIH is trying to mitigate the impact of the higher sugar prices by selectively reducing the discounts to protect its margins.
- ◆ **Impact uncertain.** As mentioned above, given our view on the uncertain outcome of CIH's tweaking of its trade discounts, we are taking a conservative stance on the matter by reducing slightly our revenue growth assumptions for CIH's beverage division for FY11-13 by 0.7-2.3% to account for potential volume drop as a result of the tweaking of trade discounts. Given the uncertain outlook pertaining to the impact on margins, we are keeping our cost assumptions unchanged. In the long run, we believe that the only way for CIH to protect its margins is by a selling price increase, although due to the competitive reasons mentioned, we believe that it will only happen once the other players raise prices.
- ◆ **Risks.** The risks include: 1) significant rise in sales volume; 2) significant decrease in raw material prices like crude oil and sugar; and 3) foreign exchange risk as CIH buys concentrate from PepsiCo in USD.
- ◆ **Forecasts.** After imputing our new revenue growth assumptions, our FY11-13 earnings were downgraded by 0.7-9%.
- ◆ **Maintain Market Perform.** Given the uncertain outlook of its revenue growth due to the trade discount-adjustments, we are reducing our CY11 target PER for CIH to 12x (from 13x previously), which is the high end of CIH's historical PE range of 8-12x over the last 5 years. Our fair value is thus reduced to RM3.30 (from RM3.88 previously). We maintain our **Market Perform** call on the stock. Re-rating catalysts would be a price increase across the board of 3-5%.

Issued Capital (m shares)	142.0
Market Cap (RMm)	412.5
Daily Trading Vol (m shs)	0.1
52wk Price Range (RM)	2.09-4.0

Major Shareholders:	(%)
Datuk Johari Abdul Ghani	30.0
Continental Theme	10.4
PNB	8.2

FYE June	FY11	FY12	FY13
EPS chg (%)	(7.3)	(9.3)	(0.7)
Var to Cons (%)	(8.0)	(20.0)	(27.0)

PE Band Chart



Relative Performance To FBM KLCI



Hoe Lee Leng
(603) 92802641
hoe.lee.leng@rhb.com.my

Key takeaways from analysts briefing

- ◆ **Weak festive revenues due to slightly earlier timing of CNY, amongst other reasons.** During the analyst's briefing yesterday, management explained the reason for the flattish revenue growth of 1.7% yoy and -4.5% qoq during the 3Q, i.e. the festive season. The timing of the CNY which was earlier this year played a part in the weak yoy and also the decline in qoq revenues. Given that CNY trade activities usually begin six to eight weeks ahead of CNY itself, the earlier timing of CNY this year (as compared to last year) of two weeks caused quite a sizeable CNY trade volume to be reflected in Dec 2010 (2QFY11). Furthermore, we understand that due to the higher sugar costs, CIH "tweaked" some of its trade discounts in an effort to mitigate the higher sugar costs in March after the festive season. We believe that this caused some volume weakness in March, although it can also be argued that the weaker sales in March was due to the after effects of heavy trade loading by wholesalers taking advantage of the festive season's trade discounts. Another reason for the weak revenues, albeit on a less significant level, was the unusually high level of rainfall during March. The high level of rainfall, which resulted in floods for a few areas in the country caused some logistics issues for distribution, although we believe the impact was minimal.
- ◆ **Contracting gross margins.** Another key issue that was raised during the analyst briefing was the higher sugar cost structure that affected CIH and 13 other beverage manufacturers, which was implemented beginning Jan 1. In brief, the beverage manufacturers which include CIH, F&N, Coca-cola, among others, were no longer allowed to purchase subsidised sugar. Subsidised sugar price is currently RM2.10/kg while unsubsidised sugar is RM2.62/kg. Note that we have an extensive explanation pertaining to the sugar issue in our CIH report dated 28 Jan. The higher sugar cost could be seen from CIH's gross margins in the 3QFY06/11, which contracted by 3.9%-pts qoq to 37.3%. We understand that the sugar price impact could be mitigated by an average price increase of 3-5% across the board for CIH's beverage division, although given that CIH is not generally the price leader, it would wait for competitors such as F&N and Coca-Cola to raise prices before it follows suit. We don't expect a price increase in the short term, as competitors such as F&N have other products to fall back on to boost the overall group margins such as their dairy products, while for Coca-Cola, given that it is still being bottled by F&N, we believe that any price increase would be done after their separation from F&N in October 2011.
- ◆ **Tweaking trade discounts.** As mentioned, CIH at the end of the 3QFY06/11 (Mar) started "tweaking" its trade discounts to mitigate the impact of the sugar price increase. Note that trade discounts are discounts of about 7-8% generally given to wholesalers and other distributors. We understand that CIH is trying to mitigate the impact of the higher sugar prices by selectively reducing the discounts to protect its margins. Given that it only started tweaking after the festive season, we understand that it is still too early to gauge the impact on both revenues and margins. Assuming the method does work on margins, we believe it could put downward pressure on CIH's revenues, especially if some wholesalers/retailers refuse to take the lesser discount and not carry CIH's products.
- ◆ **Impact uncertain.** As mentioned above, given our view on the uncertain outcome of CIH's tweaking of its trade discounts, we are taking a conservative stance on the matter by reducing slightly our revenue growth assumptions for CIH's beverage division for FY11-13 by 0.7-2.3% to account for potential volume drop as a result of the tweaking of trade discounts. Given the uncertain outlook pertaining to the impact on margins, we are keeping our cost assumptions unchanged. In the long run, we believe that the only way for CIH to protect its margins is by a selling price increase, although due to the competitive reasons mentioned, we believe that it will only happen once the other players raise prices.
- ◆ **New PET line by mid-2012.** Besides the issue of the higher cost, management also indicated that they are going to add a new carbonated PET line which will come in by mid-2012. The new carbonated PET line would incur approximately RM20-25m in capex and is expected to increase CIH's carbonated PET capacity by ~30-40%. We are thus increasing our capex assumptions for FY06/12 to RM35m (from RM12m previously) to include the cost of the new line, while we have also imputed the new capacity into our forecast for FY06/13. Note that this would be the last major capex for CIH in the coming years.

Forecasts

- ◆ **Forecasts.** After imputing our new revenue growth and capex assumptions, our FY11-13 earnings were downgraded by 0.7-9%.

Risks

- ◆ **Risks to our view.** The risks include: 1) significant rise in sales volume; 2) significant decrease in raw material prices like crude oil and sugar; and 3) foreign exchange risk as CIH buys concentrate from PepsiCo in USD.

Valuations and recommendations

- ◆ **Maintain Market Perform.** Given the uncertain outlook of its revenue growth due to the trade discount adjustments, we are reducing our CY11 target PER for CIH to 12x (from 13x previously), which is the high end of CIH's historical PE range of 8-12x over the last 5 years. Our fair value is thus reduced to RM3.30 (from RM3.88 previously). We maintain our **Market Perform** call on the stock. Rerating catalysts would be a price increase across the board of 3-5%.

Table 2. Earnings Forecasts				
FYE Jun (RMm)	FY10a	FY11F	FY12F	FY13F
Turnover	516.4	616.3	725.8	860.0
Turnover growth (%)	42.3	19.3	17.8	18.5
Cost of Sales	(304.6)	(373.3)	(449.9)	(541.7)
Gross Profit	211.8	243.0	275.9	318.4
EBITDA	64.8	72.0	75.3	75.7
EBITDA margin (%)	12.6	11.7	10.4	8.8
Depr&Amor	13.6	18.8	23.3	21.6
Net Interest	(3.2)	(3.1)	(2.7)	(2.2)
Pretax Profit	48.0	50.1	49.3	51.9
Tax	(10.0)	(11.0)	(10.9)	(11.4)
Net Profit	38.1	39.2	38.6	40.5

Source: Company, RHBRI Estimates

Table 3. Forecast Assumptions			
FYE Jun	FY11F	FY12F	FY13F
Carb-lines	4.00	4.00	4.00
Utilisation	75%	85%	75%
Non-carb lines	3	3	3
Utilisation	45%	56%	69%

Source: Company, RHBRI

IMPORTANT DISCLOSURES

This report has been prepared by RHB Research Institute Sdn Bhd (RHBRI) and is for private circulation only to clients of RHBRI and RHB Investment Bank Berhad (previously known as RHB Sakura Merchant Bankers Berhad). It is for distribution only under such circumstances as may be permitted by applicable law. The opinions and information contained herein are based on generally available data believed to be reliable and are subject to change without notice, and may differ or be contrary to opinions expressed by other business units within the RHB Group as a result of using different assumptions and criteria. This report is not to be construed as an offer, invitation or solicitation to buy or sell the securities covered herein. RHBRI does not warrant the accuracy of anything stated herein in any manner whatsoever and no reliance upon such statement by anyone shall give rise to any claim whatsoever against RHBRI. RHBRI and/or its associated persons may from time to time have an interest in the securities mentioned by this report.

This report does not provide individually tailored investment advice. It has been prepared without regard to the individual financial circumstances and objectives of persons who receive it. The securities discussed in this report may not be suitable for all investors. RHBRI recommends that investors independently evaluate particular investments and strategies, and encourages investors to seek the advice of a financial adviser. The appropriateness of a particular investment or strategy will depend on an investor's individual circumstances and objectives. Neither RHBRI, RHB Group nor any of its affiliates, employees or agents accepts any liability for any loss or damage arising out of the use of all or any part of this report.

RHBRI and the Connected Persons (the "RHB Group") are engaged in securities trading, securities brokerage, banking and financing activities as well as providing investment banking and financial advisory services. In the ordinary course of its trading, brokerage, banking and financing activities, any member of the RHB Group may at any time hold positions, and may trade or otherwise effect transactions, for its own account or the accounts of customers, in debt or equity securities or loans of any company that may be involved in this transaction.

"Connected Persons" means any holding company of RHBRI, the subsidiaries and subsidiary undertaking of such a holding company and the respective directors, officers, employees and agents of each of them. Investors should assume that the "Connected Persons" are seeking or will seek investment banking or other services from the companies in which the securities have been discussed/covered by RHBRI in this report or in RHBRI's previous reports.

This report has been prepared by the research personnel of RHBRI. Facts and views presented in this report have not been reviewed by, and may not reflect information known to, professionals in other business areas of the "Connected Persons," including investment banking personnel.

The research analysts, economists or research associates principally responsible for the preparation of this research report have received compensation based upon various factors, including quality of research, investor client feedback, stock picking, competitive factors and firm revenues.

The recommendation framework for stocks and sectors are as follows : -

Stock Ratings

Outperform = The stock return is expected to exceed the FBM KLCI benchmark by greater than five percentage points over the next 6-12 months.

Trading Buy = Short-term positive development on the stock that could lead to a re-rating in the share price and translate into an absolute return of 15% or more over a period of three months, but fundamentals are not strong enough to warrant an Outperform call. It is generally for investors who are willing to take on higher risks.

Market Perform = The stock return is expected to be in line with the FBM KLCI benchmark (+/- five percentage points) over the next 6-12 months.

Underperform = The stock return is expected to underperform the FBM KLCI benchmark by more than five percentage points over the next 6-12 months.

Industry/Sector Ratings

Overweight = Industry expected to outperform the FBM KLCI benchmark, weighted by market capitalisation, over the next 6-12 months.

Neutral = Industry expected to perform in line with the FBM KLCI benchmark, weighted by market capitalisation, over the next 6-12 months.

Underweight = Industry expected to underperform the FBM KLCI benchmark, weighted by market capitalisation, over the next 6-12 months.

RHBRI is a participant of the CMDP-Bursa Research Scheme and will receive compensation for the participation. Additional information on recommended securities, subject to the duties of confidentiality, will be made available upon request.

This report may not be reproduced or redistributed, in whole or in part, without the written permission of RHBRI and RHBRI accepts no liability whatsoever for the actions of third parties in this respect.