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13 May 2010

CI Holdings

Getting its juices flowing

RECOM	Buy
PRICE	RM2.31
MKT CAPITALISATION	RM328.0m
BOARD	Main (Syariah stock)
SECTOR	Food & Beverage
INDEX COMPONENT	Nil

CIH MK / CIHB.KL

Norziana Mohd Inon + 60 (3) 2084-9645 – norziana.inon@cimb.com

Investment highlights

- Maintain BUY.** We recently spoke to CI Holdings' (CIH) management who confirmed that the construction of the RM45m new production line for non-carbonated beverages at the Bangi facility is on schedule. The timely completion of the new line by Sep is vital to CIH's operations because 1) the company is bumping against capacity constraints in its production of non-carbonated drinks, 2) F&N Holdings (FNH MK, Underperform), which currently trails behind CIH, will launch a new range of fruit juices this month, and 3) the new line will allow for the in-house manufacture of non-carbonated products which are currently contract-packed. We maintain our earnings forecasts and target price of RM3.28, pegged to an unchanged 20% discount to our 15x target market P/E to account for the stock's relatively low liquidity. CIH remains firmly a BUY, with the potential re-rating catalysts being 1) capacity expansion, and 2) an increasingly marketable product line.
- Undemanding valuations.** CIH has made a smooth transition from a loss-making entity to a successfully executed turnaround story, having racked up 15 consecutive quarters of not just profits but continually improving results. The company's performance has exceeded our forecasts for four straight quarters. It also offers a breath of fresh air in a sector where limited growth and pricey valuations cap investor interest even though the sector is lauded for being less susceptible to boom and bust. Despite the improvement in its share price, CIH's P/E valuations remain undemanding at less than 10x against a 3-year EPS CAGR of 20.3%, which is the highest in our F&B portfolio and superior to the sector average of 12.1%. Its dividend yield of 4-6% is an added attraction. Also, CIH may be an effective indirect exposure to PepsiCo given that PepsiCo brands make up 85% of CIH's product portfolio and 80% of the company's revenue.

Key stock statistics

	2009	2010F
FYE 30 Jun		
EPS (sen)	14.8	24.6
P/E (x)	15.6	9.4
Dividend/Share (sen)	7.0	10.0
NTA/Share (RM)	0.7	0.8
Book Value/Share (x)	0.7	0.8
Issued Capital (m shares)	129.6	142.0
52-weeks Share Price Range (RM)	RM0.90/RM2.54	
Major Shareholders:	%	
Datuk Johari Abdul Ghani	27.0	
Continental Theme Sdn Bhd	11.1	
ASB	7.0	

Per share data

	2007	2008	2009	2010F
FYE 30 Jun				
Book Value (RM)	0.7	0.7	0.7	0.8
Cash Flow (sen)	16.1	22.0	27.8	35.9
Earnings (sen)	6.0	10.2	14.8	24.6
Dividend (sen)	0.0	4.0	7.0	10.0
Payout Ratio (%)	0.0	28.1	34.1	29.2
P/E (x)	38.3	22.5	15.6	9.4
P/Cash Flow (x)	14.4	10.5	8.3	6.4
P/Book Value (x)	3.5	3.3	3.1	2.9
Dividend Yield (%)	0.0	1.7	3.0	4.3
ROE (%)	9.0	15.9	21.8	30.7
Net Gearing (%)	83.4	83.2	83.0	73.6

Source: Company, CIMB estimates, Bloomberg

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Recent developments

We recently spoke to management who confirmed that the construction of the RM45m new production line for non-carbonated drinks at the Bangi facility is on schedule. The market's response to Tropicana fruit juices has surpassed management's expectations, forcing CI Holdings (CIH) to expand its current facility much earlier than expected.

Earnings outlook

Four consecutive quarters of outperformance. To recap, CIH blew us away with 3QFY6/10 net profit of RM10.9m, which was more than double 3Q09's RM5.2m despite the absence of new products. It was the fourth straight quarter of results outperformance. Much of the earnings growth came from Tropicana fruit juices and Lipton Tea variants. About 92% of CIH's revenue came from the beverage business while the remainder came from the sanitary and tapware business. The market's response to Tropicana has surpassed management's expectations, forcing the company to expand its current facility much earlier than expected. Tropicana and Lipton are PepsiCo brands. Other PepsiCo brands that are in CIH's product portfolio are Mirinda, 7-Up, Gatorade, Mountain Dew, Sting and Everness. The beverage business is housed under wholly-owned unit Permanis.

Construction of new line progresses on schedule. The construction of the RM45m new production line for non-carbonated drinks at the Bangi facility is on schedule and it is expected to be ready by Sep, just in time for Hari Raya. The Bangi facility, which has the capability to produce non-carbonated beverages such as fruit juices, teas and Asian drinks, was commissioned in Mar 08. Two years into operations, the facility is already running at full capacity (three shifts a day and seven days a week). Based on the initial plan, the facility was expected to hit maximum production in five years at the earliest but the success of Tropicana fruit juices has shortened it to two years. From 20% two years ago, non-carbonated drinks, led by Tropicana, now account for 40% of group sales, with the remaining 60% represented by carbonated drinks. The revenue split between non-carbonated drinks and carbonated drinks is expected to hit 50:50 in two years' time given the additional capacity.

Crucial on-time completion. The new production line will have the capacity to produce 600 bottles per minute, which is twice the speed of the existing line. At full capacity, the new line will have the ability to manufacture products worth RM300m. The expected payback period is five years and the breakeven capacity utilisation is 20%. Timely completion of the new line is vital to CIH's operations due to three reasons:

- **No capacity left.** The success of Tropicana has overshot management's expectations. CIH has run out of capacity for non-carbonated beverages and will not be able to introduce new non-carbonated products in 2H10. Tropicana Twister is often out of stock as the existing production capacity cannot keep up with the unprecedented demand growth. The non-carbonated drinks are enjoying double-digit growth compared with single-digit growth for the carbonated drinks.
- **Competition heats up.** At the 7 May analyst briefing, F&N's management acknowledged that CIH has had a "free run" in the fruit juice segment. CIH was the late entrant in the local fruit juice market but has, in just two years, catapulted itself to the No. 1 spot in the local fruit juice market with a 35% share, followed by Malaysia Milk's Marigold (30%) and F&N's Fruit Tree and Sunkist (13%). F&N plans to launch a new range of fruit juices (Figure 1) this month, which should be helped by the fact that Tropicana is out of stock in the marketplace. F&N did not disclose its sales target for the new juices. Currently, F&N services some 40,000 retail outlets nationwide while CIH distributes to 35,000 outlets.
- **One-stop manufacture.** The new production line will also allow contract-packed non-carbonated products (Lipton Tea) to be manufactured in-house, thereby eliminating a leakage in margins.

Figure 1: P&L analysis (RM m)

FYE 30 Jun	2007	2008	2009	2010F
Revenue	267.0	290.2	363.0	508.2
Operating Profit (EBIT)	38.1	52.3	67.2	82.4
Depreciation	(13.0)	(14.0)	(15.0)	(16.0)
Interest Expenses	(4.9)	(8.7)	(9.2)	(9.7)
Pretax Profit	7.3	15.6	28.0	40.7
Effective Tax Rate (%)	(7.5)	7.1	25.2	14.0
Net Profit	7.8	14.5	21.0	35.0
Operating Margin (%)	14.3	18.0	18.5	16.2
Pretax Margin (%)	2.7	5.4	7.7	8.0
Net Margin (%)	2.9	5.0	5.8	6.9

Source: Company, CIMB estimates

Figure 2: F&N's Fruit Tree ambient juices



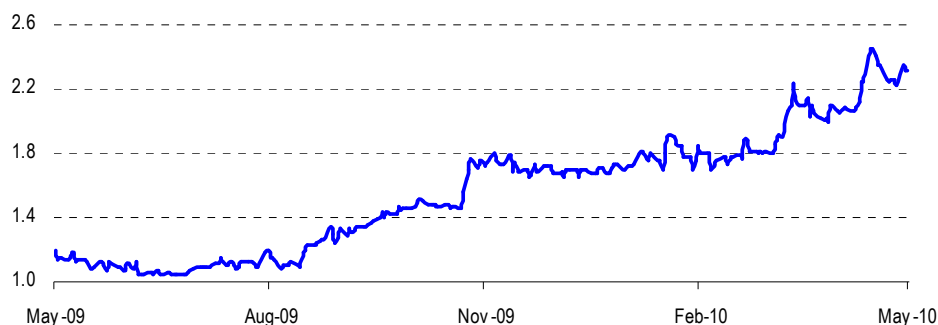
Source: Company

Recommendation

Undemanding valuations. CIH has made a smooth transition from a loss-making entity to a successfully executed turnaround story, having racked up 15 consecutive quarters of not just profits but continually improving results. The company's performance has exceeded our forecasts for four straight quarters. It also offers a breath of fresh air in a sector where limited growth and pricey valuations cap investor interest even though it is lauded for being less susceptible to boom and bust. Despite the improvement in its share price (Figure 3), CIH's P/E valuations remain undemanding at less than 10x against a 3-year EPS CAGR of 20.3%, which is the highest in our F&B portfolio and superior to the sector average of 12.1% (see Sector comparisons table). Its dividend yield of 4-6% is an added attraction. Also, CIH may be an effective indirect exposure to PepsiCo (Figure 4) given that PepsiCo brands make up 85% of CIH's product portfolio and 80% of the company's revenue.

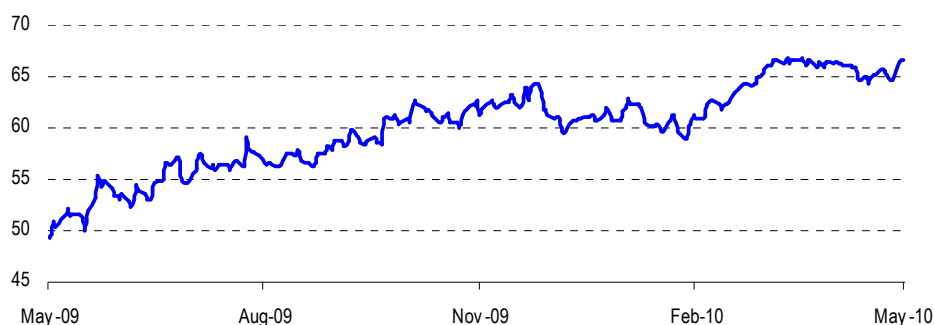
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Figure 3: CI Holdings' share price chart (RM)



Source: Bloomberg

Figure 4: PepsiCo's share price chart (US\$)



Source: Bloomberg

Financial summary

FYE Jun	2008	2009	2010F	2011F	2012F
Revenue (RM m)	290.2	363.0	508.2	609.8	731.8
EBITDA (RM m)	38.3	52.2	66.4	69.6	60.6
EBITDA margins (%)	13.2	14.4	13.1	11.4	8.3
Pretax profit (RM m)	15.6	28.0	40.7	43.7	46.6
Net profit (RM m)	14.5	21.0	35.0	37.6	40.1
EPS (sen)	11.2	16.2	24.6	26.5	28.2
EPS growth (%)	+86%	+44%	+52%	+7%	+7%
P/E (x)	20.6	14.3	9.4	8.7	8.2
Core EPS (sen)	11.2	16.2	24.6	26.5	28.2
Core EPS growth (%)	+86%	+44%	+52%	+7%	+7%
Core P/E (x)	20.6	14.3	9.4	8.7	8.2
FD EPS (sen)	10.2	14.8	24.6	26.5	28.2
FD P/E (x)	22.5	15.6	9.4	8.7	8.2
Gross DPS (sen)	4.0	7.0	10.0	11.0	12.0
Dividend yield (%)	1.7	3.0	4.3	4.8	5.2
P/NTA (x)	3.3	3.1	2.9	2.8	2.7
ROE (%)	15.9	21.8	30.7	31.9	32.9
Net gearing (%)	83.2	83.0	73.6	71.7	69.8
P/CF (x)	10.5	8.3	6.4	6.0	5.8
EV/EBITDA (x)	8.0	5.8	4.6	4.4	5.0
% change in EPS estimates			-	-	-
CIMB/Consensus (x)			1.02	1.01	1.05

Source: Company, CIMB/CIMB-GK Research, Reuters Estimates

Sector comparisons

	Bloomberg ticker	Recom.	Price (Local)	Target price (Local)	Mkt cap (US\$ m)	Core P/E (x) CY2010	Core P/E (x) CY2011	3-yr EPS CAGR (%)	P/BV (x) CY2010	ROE (%) CY2010	Div yield (%) CY2010
CI Hldgs	CIH MK	B	2.31	3.28	103	9.0	8.5	20.3	2.8	31.3	4.8
CocoaLand	COLA MK	O	1.41	1.78	58	9.3	7.1	16.0	1.5	17.5	7.1
F&N Hldgs	FNH MK	U	11.08	8.65	1,233	14.1	13.9	8.9	3.7	26.9	4.8
Nestle (M)	NESZ MK	U	34.40	28.00	2,517	21.6	20.6	5.2	13.4	68.3	5.9
QSR	QSR MK	O	3.51	5.60	314	9.7	8.8	9.9	2.2	22.7	3.7
Simple average						12.7	11.8	12.1	4.7	33.3	5.3

O = Outperform, N = Neutral, U = Underperform, TB = Trading Buy, B = Buy and TS = Trading Sell
Source: Company, CIMB Research

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