

WH Group (288 HK)

US ham price up after Mexico dropped tariff

SUMMARY. After an update with management, we reduced FY19-21E EPS by 2-4% as we lowered China fresh pork volume growth and OP margin assumptions. Our TP is changed from HK\$11.10 to HK\$10.70. Maintain BUY.

- Ham price has jumped 7% since Mexico dropped pork tariff.** In FY18, WH exported ~210k metric tons of pork products (mainly ham) to Mexico, representing 29%/8% of export volume/fresh pork volume. Ham price has gained greater than hog price's 0.2% increase since 19 May, which should be positive to US fresh pork margin. To recap, WH's share price fell 12% in a week after Mexico announced to impose US pork tariffs on 5 Jun 2018, suggesting that US-Mexico trade issues have big impact on share price.
- Limited impact from Chinese retaliatory tariffs.** The PRC government announced to impose 25% tariffs on salted pig casings and processed pig hind legs on 13 May. We think the impact is limited on WH because currently most of its exports to China are offal, head, ear and tail, etc.
- China fresh pork segment growth to moderate.** The 21% growth of hog processed and RMB114 OP/head in 1Q19 is not sustainable. As ASF continues to spread, the YoY decline of hogs balance was widened to 21% in Apr 2019. The escalating hog shortage would limit volume growth of hog processed. Also, hog prices disparities across provinces due to ASF almost disappeared beginning late Mar 2019. We expect OP/head would normalize to RMB40-50/head beginning 2Q19.
- Investment thesis.** USDA forecasts China's pork production volume would fall by 10% YoY in 2019E and its import volume would increase by 41% YoY to 2.2mn metric tons. Its import volume as a percentage of global import volume would increase from 20% in 2018 to 25% in 2019E. Given that number of sows was falling 23% YoY in China in Apr 2019 and it takes around 18 months to increase hog supply, we think this will trigger global hog prices increases in 2019 and 2020.
- Valuation.** We fine tuned our SOTP-based TP from HK\$11.10 to HK\$10.70, representing 15.4x FY19E P/E. **Catalysts:** (1) China reduces import tariffs or increases pork imports on US pork; (2) stronger-than-expected US hog price. **Risks:** (1) Packaged meat and fresh pork margins hurt by rising pork prices; (2) lower-than-expected sales of packaged meat and pork.

Earnings Summary

(YE 31 Dec)	FY17A	FY18A	FY19E	FY20E	FY21E
Revenue (US\$ mn)	22,379	22,605	24,775	26,542	26,427
Net profit (US\$ mn)	1,127	1,047	1,315	1,432	1,477
Adj. net profit (US\$ mn)	1,090	1,046	1,315	1,432	1,477
Adj. EPS (US\$)	0.075	0.071	0.090	0.098	0.101
YoY growth (%)	1.0	(4.9)	25.7	8.9	3.1
Adj. P/E (x)	12.5	13.1	10.5	9.6	9.3
P/B (x)	1.8	1.8	1.6	1.4	1.3
Yield (%)	3.7	2.7	4.3	4.7	4.8
Adj. ROAE (%)	15.8	13.8	16.0	15.7	14.9
Net gearing (%)	22	30	21	15	9

Source: Company data, CMBIS estimates

BUY (Maintain)

Target Price HK\$10.70
 (Previous TP) HK\$11.10
Up/Downside +47%
Current Price HK\$7.30

China Staples Sector

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Stock Data

Mkt Cap (HK\$ mn)	107,378
Avg 3 mths t/o (HK\$ mn)	689.2
52w High/Low (HK\$)	9.95/5.51
Total Issued Shares (mn)	14,664.2

Source: Bloomberg

Shareholding Structure

Rise Grand	35.94%
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Source: HKEx

Share Performance

	Absolute	Relative
1-mth	-20.2%	-13.7%
3-mth	-6.8%	-3.1%
6-mth	20.1%	12.8%

Source: Bloomberg

12-mth Price Performance



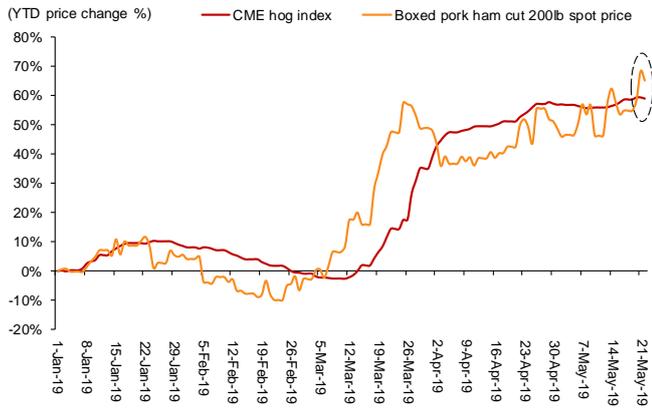
Source: Bloomberg

Auditor: EY

Related Reports

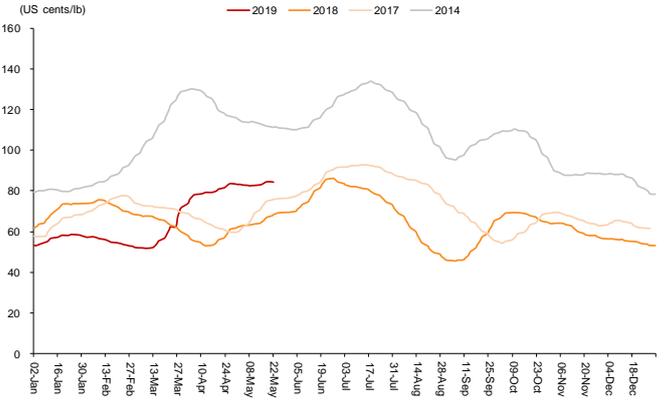
- "WH Group – 1Q19 net profit fell but earnings outlook still positive" – 30 Apr 2019
- "WH Group – US hog price is recovering; lift TP to HK\$9.00" – 18 Mar 2019

Figure 1: US ham price has risen 7% since Mexico dropped pork tariff on 19 May



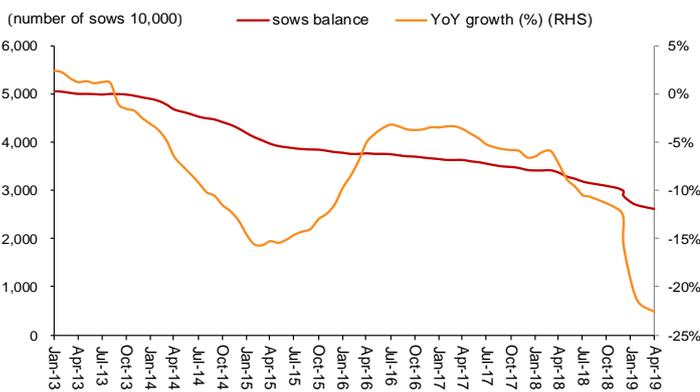
Source: Bloomberg, CMBIS

Figure 2: CME lean hog price began to rally in Mar due to China's continuing spread of ASF



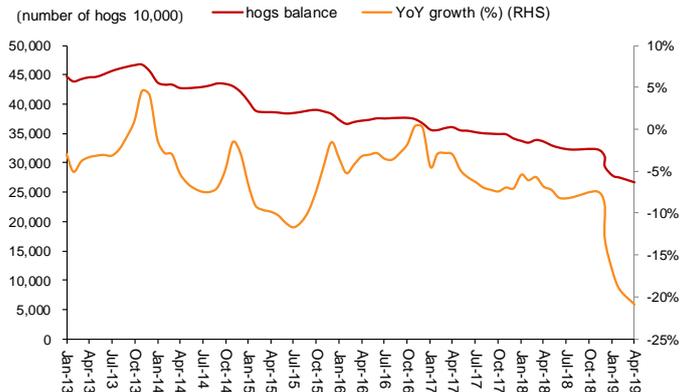
Source: Bloomberg, CMBIS

Figure 3: Sows balance in China fell 23% YoY in Apr 2019



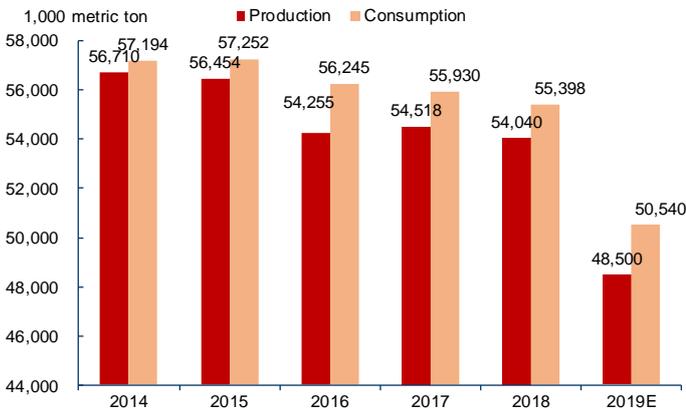
Source: WIND, CMBIS

Figure 4: Hogs balance in China fell 21% YoY in Apr 2019



Source: WIND, CMBIS

Figure 5: China's pork import is estimated to grow by 41% in 2019E

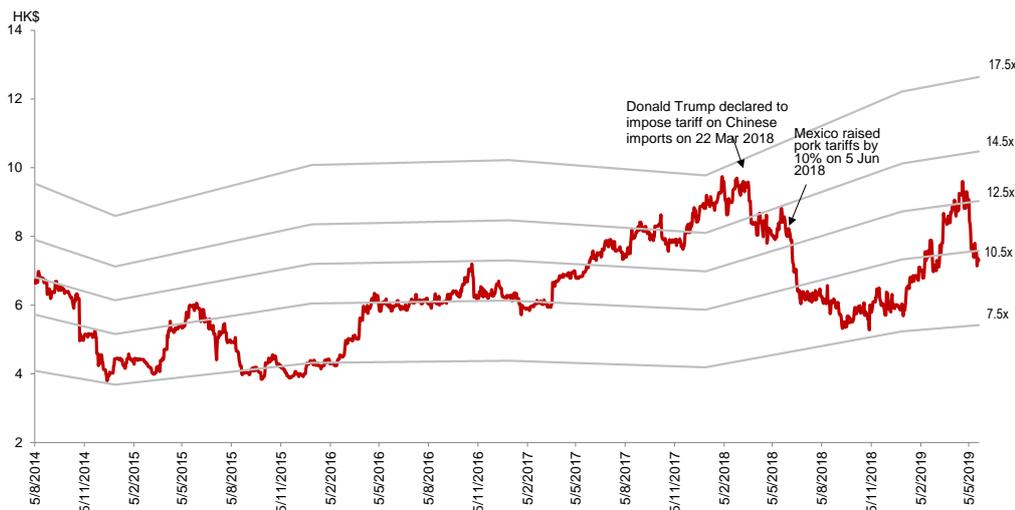


Source: USDA

Figure 6: SOTP-based valuation

Segment	FY19 P/E	FY19 net profit (US\$m)	Valuation (US\$m)	Remarks
US & Europe businesses	14.0	819.5	11,473	Tyson Foods historical average forward P/E plus 1sd 30% discount on HK listed peers' average 25.1x FY19 P/E
China business	17.6	495.8	8,726	
Total			20,199	
Value per share (HK\$)			10.7	
Implied FY19 P/E			15.4	

Source: Company data, Bloomberg, CMBIS estimates

Figure 7: P/E band

Source: Bloomberg, Company data, CMBIS estimates

Figure 8: Earnings revision

US\$ mn	New			Old			Diff (%)		
	FY19E	FY20E	FY21E	FY19E	FY20E	FY21E	FY19E	FY20E	FY21E
Revenue	24,775	26,542	26,427	24,857	26,899	27,100	-0.3%	-1.3%	-2.5%
Gross Profit	4,973	5,379	5,427	4,987	5,447	5,564	-0.3%	-1.3%	-2.5%
Operating Profit	2,029	2,157	2,250	2,101	2,209	2,299	-3.4%	-2.4%	-2.2%
Adj. net profit	1,315	1,432	1,477	1,368	1,467	1,510	-3.9%	-2.4%	-2.2%
Gross Margin	20.1%	20.3%	20.5%	20.1%	20.3%	20.5%	flat	flat	flat
Operating Margin	8.2%	8.1%	8.5%	8.5%	8.2%	8.5%	-0.3ppt	-0.1ppt	flat
Net Margin	5.3%	5.4%	5.6%	5.5%	5.5%	5.6%	-0.2ppt	-0.1ppt	-0.1ppt

Source: Company data, CMBIS estimates

Figure 9: CMBI estimates vs consensus

US\$ mn	CMBI			Consensus			Diff (%)		
	FY19E	FY20E	FY21E	FY19E	FY20E	FY21E	FY19E	FY20E	FY21E
Revenue	24,775	26,542	26,427	24,011	25,476	26,591	3.2%	4.2%	-0.6%
Gross Profit	4,973	5,379	5,427	4,948	5,268	5,564	0.5%	2.1%	-2.5%
Operating Profit	2,029	2,157	2,250	1,936	2,078	2,205	4.8%	3.8%	2.0%
Net profit	1,315	1,432	1,477	1,256	1,392	1,455	4.7%	2.9%	1.5%
Gross Margin	20.1%	20.3%	20.5%	20.6%	20.7%	20.9%	-0.5ppt	-0.4ppt	-0.4ppt
Operating Margin	8.2%	8.1%	8.5%	8.1%	8.2%	8.3%	+0.1ppt	-0.1ppt	+0.2ppt
Net Margin	5.3%	5.4%	5.6%	5.2%	5.5%	5.5%	+0.1ppt	-0.1ppt	flat

Source: Bloomberg, CMBIS estimates

Figure 10: Major assumptions for US market

(US\$mn)	FY17	FY18	FY19E	FY20E	FY21E
Packaged meat segment					
External revenue	7,807	7,773	8,003	8,366	8,660
<i>growth %</i>	9.6%	-0.4%	3.0%	4.5%	3.5%
Sales volume (mn metric tons)	1.45	1.46	1.47	1.51	1.55
<i>growth %</i>	3.3%	0.9%	1.0%	2.5%	2.5%
ASP (US\$/ton)	5,395	5,324	5,430	5,539	5,594
<i>growth %</i>	6.1%	-1.3%	2.0%	2.0%	1.0%
<i>OP margin</i>	9.3%	10.1%	10.0%	9.5%	11.0%
Fresh pork segment					
External revenue	4,961	4,790	5,333	5,656	5,074
<i>growth %</i>	11.7%	-3.4%	11.3%	6.1%	-10.3%
Hog processed (mn heads)	34.43	33.95	34.96	35.31	34.61
<i>growth %</i>	8.0%	-1.4%	3.0%	1.0%	-2.0%
OP/head (US\$)	12.6	1.4	5.5	5.0	5.0
Hog production segment					
External revenue	510	619	656	690	642
<i>growth %</i>	-35.8%	21.4%	6.0%	5.1%	-6.9%
Hog produced (mn heads)	16.38	16.47	16.63	16.97	16.63
<i>growth %</i>	4.8%	0.5%	1.0%	2.0%	-2.0%
OP/head (US\$)	(4.2)	(8.9)	12.5	20.0	5.0
Total external revenue	13,278	13,182	13,993	14,712	14,376
Packaged meat	7,807	7,773	8,003	8,366	8,660
Fresh pork	4,961	4,790	5,333	5,656	5,074
Hog production	510	619	656	690	642
Segment profit	923	615	1,116	1,218	1,112
<i>growth %</i>	3.9%	-33.4%	81.4%	9.1%	-8.7%
Packaged meat	726	785	801	795	953
Fresh pork	433	48	192	177	173
Hog production	(68)	(147)	208	339	83
Others	(168)	(71)	(85)	(94)	(97)
Segment profit margin	7.0%	4.7%	8.0%	8.3%	7.7%

Source: Company data, CMBIS estimates

Figure 11: Major assumptions for China market

(US\$mn)	FY17	FY18	FY19E	FY20E	FY21E
Packaged meat segment					
External revenue	3,312	3,458	3,590	3,753	3,943
<i>growth %</i>	-1.0%	4.4%	3.8%	4.5%	5.1%
Sales volume (mn metric tons)	1.58	1.60	1.62	1.64	1.69
<i>growth %</i>	-1.4%	1.1%	1.0%	1.5%	3.0%
ASP (Rmb/ton)	14,126	14,303	14,875	15,321	15,627
<i>growth %</i>	2.2%	1.3%	4.0%	3.0%	2.0%
OP margin %	20.9%	20.6%	15.0%	14.5%	18.0%
Fresh pork segment					
External revenue	3,888	3,584	4,202	4,749	4,338
<i>growth %</i>	-7.3%	-7.8%	17.3%	13.0%	-8.6%
Hog processed (mn heads)	14.27	16.31	17.12	17.12	17.98
<i>growth %</i>	15.5%	14.3%	5.0%	0.0%	5.0%
OP/head (Rmb)	48.8	72.7	65.0	45.0	50.0
Hog production segment					
External revenue	11	8	11	15	14
<i>growth %</i>	-21.4%	-27.3%	42.4%	29.3%	-3.2%
Hog produced (mn heads)	0.31	0.29	0.30	0.31	0.31
<i>growth %</i>	0.0%	-6.1%	3.0%	3.0%	3.0%
OP/head (Rmb)	498.0	113.0	250.0	450.0	150.0
Total external revenue	7,446	7,328	8,105	8,848	8,660
Packaged meat	3,312	3,458	3,590	3,753	3,943
Fresh pork	3,888	3,584	4,202	4,749	4,338
Hog production	11	8	11	15	14
Others	235	278	302	332	366
Segment profit	525	922	744	711	885
<i>growth %</i>	-36.2%	75.6%	-19.3%	-4.5%	24.5%
Packaged meat	692	712	538	544	710
Fresh pork	103	179	166	115	134
Hog production	23	5	11	21	7
Others	(293)	26	28	31	34
Segment profit margin	7.1%	12.6%	9.2%	8.0%	10.2%

Source: Company data, CMBIS estimates

Figure 12: Major assumptions for Europe market

(US\$m)	FY17	FY18	FY19E	FY20E	FY21E
Packaged meat segment					
External revenue	658	916	1,109	1,280	1,478
growth %	8.4%	39.2%	21.1%	15.4%	15.5%
Sales volume (mn metric tons)	0.24	0.29	0.32	0.36	0.40
growth %	11.6%	18.0%	13.0%	12.0%	10.0%
ASP (EUR/ton)	3,105	3,818	4,009	4,289	4,504
growth %	-0.5%	23.0%	5.0%	7.0%	5.0%
OP margin	2.6%	5.5%	5.2%	6.2%	7.5%
Fresh pork segment					
External revenue	677	762	1,086	1,173	1,316
growth %	24.7%	12.6%	42.5%	8.0%	12.2%
Hog processed (mn heads)	5.09	5.83	7.28	8.01	8.81
growth %	0.6%	14.6%	25.0%	10.0%	10.0%
OP/head (EUR)	2.5	3.9	0.0	3.5	4.0
Hog production segment					
External revenue	51	61	67	70	68
growth %	41.7%	19.6%	9.6%	4.1%	-2.1%
Hog produced (mn heads)	3.53	4.17	4.30	4.42	4.56
growth %	8.9%	18.0%	3.0%	3.0%	3.0%
OP/head (EUR)	32.4	8.2	10.0	13.0	10.0
Total external revenue	1,655	2,095	2,677	2,982	3,391
Packaged meat	658	916	1,109	1,280	1,478
Fresh pork	677	762	1,086	1,173	1,316
Hog production	51	61	67	70	68
Others	269	356	415	459	528
Segment profit	135	113	114	174	198
growth %	75.3%	-16.3%	1.2%	52.4%	13.5%
Packaged meat	17	50	58	80	110
Fresh pork	11	19	0	23	29
Hog production	101	29	37	48	38
Others	6	15	20	24	21
Segment profit margin	8.2%	5.4%	4.3%	5.8%	5.8%

Source: Company data, CMBIS estimates

Financial Summary

Income statement

YE 31 Dec (US\$ mn)	FY17A	FY18A	FY19E	FY20E	FY21E
Revenue	22,379	22,605	24,775	26,542	26,427
China	7,446	7,328	8,105	8,848	8,660
US	13,278	13,182	13,993	14,712	14,376
EUR	1,655	2,095	2,677	2,982	3,391
Cost of sales	(17,766)	(18,103)	(19,803)	(21,163)	(21,001)
Gross profit	4,613	4,502	4,973	5,379	5,427
Other income and gains	113	98	89	89	93
SG&A expenses	(2,753)	(2,871)	(3,033)	(3,311)	(3,270)
Operating profit	1,973	1,729	2,029	2,157	2,250
Finance cost	(198)	(115)	(117)	(103)	(102)
Other expenses	(326)	(74)	(50)	(50)	(50)
Other gains/(losses)	7	(21)	0	0	0
Share of profit of associate	8	8	8	9	9
Share of profit of JV	14	23	30	33	36
Profit before tax	1,478	1,550	1,900	2,046	2,143
Income tax	(165)	(293)	(407)	(441)	(457)
Non-controlling interests	(186)	(210)	(178)	(173)	(209)
Net profit	1,127	1,047	1,315	1,432	1,477
Adj. net profit	1,090	1,046	1,315	1,432	1,477

Cash flow summary

YE 31 Dec (US\$ mn)	FY17A	FY18A	FY19E	FY20E	FY21E
Profit before tax	1,501	1,411	1,900	2,046	2,143
Depreciation and amortization	394	441	469	501	531
Change in working capital	(321)	(570)	(151)	(91)	5
Others	(62)	(27)	(362)	(382)	(459)
Net cash from operating	1,512	1,255	1,856	2,075	2,219
Capex & investments	(530)	(811)	(800)	(800)	(800)
Interest received	12	6	17	15	18
Others	(266)	(412)	(58)	(57)	(56)
Net cash from investing	(784)	(1,217)	(841)	(842)	(838)
Change of borrowings	64	4	(200)	(200)	(300)
Dividend paid	(668)	(795)	(447)	(780)	(851)
Others	13	1	0	0	0
Net cash from financing	(591)	(790)	(647)	(980)	(1,151)
Net change in cash	137	(752)	368	252	230
Cash at the beginning	1,121	1,250	498	866	1,117
Exchange difference	(9)	0	0	0	0
Cash at the end	1,250	498	866	1,117	1,348

Balance sheet

YE 31 Dec (US\$ mn)	FY17A	FY18A	FY19E	FY20E	FY21E
Non-current assets	9,592	9,838	10,208	10,548	10,862
PPE	5,037	5,300	5,644	5,956	6,238
Goodwill	3,580	3,581	3,572	3,563	3,554
JV/associates	295	352	390	432	477
Others	680	605	601	597	593
Current assets	5,666	5,460	6,206	6,729	6,933
Cash and pledged deposits	1,440	579	947	1,199	1,429
Inventory	1,905	2,022	2,256	2,411	2,393
Trade receivables	989	1,135	1,244	1,333	1,327
Others	1,332	1,724	1,758	1,786	1,785
Current liabilities	3,499	3,328	3,534	3,718	3,698
Borrowings	901	860	860	860	860
Trade payables	1,076	977	1,069	1,142	1,133
Other payables	1,472	1,430	1,564	1,672	1,659
Others	50	61	41	44	46
Non-current liabilities	3,537	3,552	3,416	3,267	2,964
Borrowings	2,297	2,259	2,059	1,859	1,559
Deferred revenue	601	695	759	810	807
Others	639	598	598	598	598
Minority Interest	777	672	778	763	766
Total net assets	8,222	8,418	9,464	10,292	11,134
Shareholders' equity	7,445	7,746	8,686	9,527	10,359

Key ratios

YE 31 Dec	FY17A	FY18A	FY19E	FY20E	FY21E
Sales mix (%)					
China	33.3	32.4	32.7	33.3	32.8
US	59.3	58.3	56.5	55.4	54.4
EUR	7.4	9.3	10.8	11.2	12.8
P&L ratios (%)					
Gross profit margin	20.6	19.9	20.1	20.3	20.5
Operating profit margin	8.8	7.6	8.2	8.1	8.5
Net profit margin	5.0	4.6	5.3	5.4	5.6
Adj. net profit margin	4.9	4.6	5.3	5.4	5.6
Payout ratio	44.7	40.0	45.0	45.0	45.0
Balance sheet ratios					
Current ratio (x)	1.6	1.4	1.8	1.8	1.9
Receivables turnover days	15	17	18	18	18
Payables turnover days	20	21	19	19	20
Inventory turnover days	37	40	39	40	42
Asset turnover (x)	1.5	1.5	1.5	1.5	1.5
Net gearing ratio (%)	22	30	21	15	9
Returns (%)					
Adj. ROAE	15.8	13.8	16.0	15.7	14.9
Adj. ROAA	8.8	8.2	9.4	9.5	9.6
Per share data					
Adj. EPS (US\$)	0.075	0.071	0.090	0.098	0.101
DPS (HK\$)	0.27	0.20	0.31	0.34	0.35
BVPS (US\$)	0.51	0.53	0.59	0.65	0.71

Source: Company data, CMBIS estimates

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