WH Group Ltd

Bloomberg: 288 HK Equity | Reuters: 0288.HK

Refer to important disclosures at the end of this report

DBS Group Research . Equity

16 Aug 2023

BUY

Last Traded Price (15 Aug 2023): HK$4.01 (HSI: 18,581)
Price Target 12-mth: HK$5.49 (37% upside) (Prev HK$5.96)

Analyst

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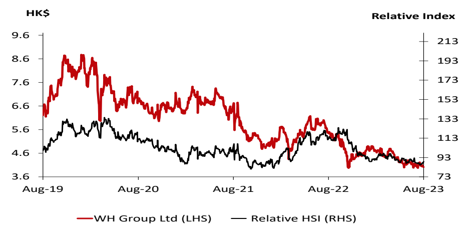
What's New

- 1H23/2Q23 attributable profit down 45%/32% y-o-y, below expectations
- Packaged meat businesses in China/US expected to sustain decent profitability of RMB4000/US$800 per tonne in FY23
- US pork segment to see sequential improvement; maintain BUY with lower TP of HK$5.49

Price Relative



Forecasts and Valuation

FY Dec (US$m)	2021A	2022A	2023F	2024F
Turnover	27,293	28,136	27,455	28,291
EBITDA	2,435	2,826	2,449	3,131
Pre-tax Profit	1,658	2,186	1,516	2,157
Net Profit	1,043	1,401	896	1,432
Net Pft (Pre Ex) (core profit)	1,043	1,118	896	1,432
Net Profit Gth (Pre-ex) (%)	7.2	34.3	(36.0)	59.7
EPS (US$)	0.07	0.11	0.07	0.11
EPS (HK$)	0.58	0.85	0.55	0.87
Core EPS (US$)	0.07	0.09	0.07	0.11
Core EPS (HK$)	0.58	0.68	0.55	0.87
EPS Gth (%)	12.1	48.1	(36.0)	59.7
Core EPS Gth (%)	12.1	18.2	(19.8)	59.7
Diluted EPS (HK$)	0.58	0.85	0.55	0.87
DPS (HK$)	0.20	0.30	0.19	0.31
BV Per Share (HK$)	4.84	5.85	6.87	8.07
PE (X)	7.0	4.7	7.3	4.6
CorePE (X)	7.0	5.9	7.3	4.6
P/Cash Flow (X)	3.7	3.7	4.2	3.2
P/Free CF (X)	7.0	7.9	6.8	4.6
EV/EBITDA (X)	4.4	3.3	3.6	2.5
Net Div Yield (%)	5.0	7.5	4.8	7.6
P/Book Value (X)	0.8	0.7	0.6	0.5
Net Debt/Equity (X)	0.2	0.2	0.1	0.0
ROAE(%)	11.1	15.3	8.6	11.7
Earnings Rev (%):			(34)	(6)
Consensus EPS (US$)			0.09	0.11
Other Broker Recs:		B:14	S:0	H:1

Source of all data on this page: Company, DBS Bank (Hong Kong) Limited ("DBS HK"), Thomson Reuters

Margin recovery ahead

Investment Thesis

Leading packaged meat play in China. As the market leader of packaged meats in both China and the US, WH Group should continue to ride on channel recovery (e.g., food services) and product mix premiumisation to generate better profit margins. We also believe its channel recovery should enable the Group to score low- to mid-single-digit volume growth for both FY23 and FY24 in China.

Sequential margin recovery. We expect WH Group's China packaged meat business to sustain a per tonne profit of RMB4,000 in 2H23, as the company has largely stockpiled frozen pork in 1H23 at low cost of c.RMB15/kg. Riding on the company's ongoing efforts towards cost control and product mix adjustment, per-tonne profit for US packaged meat is expected to reach US$800 in FY23. With the reduction of underperforming hog farms as well as the higher hog/pork prices by 3Q23, we expect the loss of pork segment in the US to narrow in 2H23, supporting a better h-o-h margin recovery.

Vertical integration in China. The company's poultry slaughtering capacity in China is targeting 220m/300m heads in FY23/FY24 (FY22: c.120m heads). This should support better margin growth in its packaged meat business in China given lower unit costs in the longer run. The company's hog farming is also expected to scale up in China, meeting 30%+ of WH Group's internal needs over time.

We cut FY23/24 earnings by 34%/6% given near-term margin pressure in the US pork segment. Our revised TP of HK$5.49 (previous TP: HK$5.96) is based on SOTP valuation – China/US operations are valued at 13x/6x rolling PE (previous TP based on FY23 PE), in line with peers.

Key Risks

Declining domestic demand; volatility in raw material prices; regulatory changes; food safety issues; disease outbreaks; etc.

At A Glance

Issued Capital (m shrs)	12,830
Mkt Cap (HKm/US$m)	51,448 / 6,576
Major Shareholders (%)	
Rise Grand Group Ltd.	27.1
Mondrian Investment Partners Ltd.	6.0
Free Float (%)	66.9
3m Avg. Daily Val. (US$m)	8.9
GICS Industry: Consumer Staples / Food, Beverage & Tobacco	

ed- PJ / sa- CS /JY

WHAT'S NEW

1H23 results below expectations. Revenue dropped 2% to US$13.1bn, mainly due to the decrease in the packaged meat segment. Operating profit dropped by 47% to US$639m, mainly attributable to the loss of US$495m in the US pork segment (1H22: profit of US$102m) given the lower hog/pork prices and higher raising costs, squeezing hog farming profit. Attributable profit (before biological fair value adjustments) contracted by 45% to US$383m. In China, operating profit dropped by 3.2% (or up 3.5% in RMB) with higher y-o-y raw material cost as well as foreign currency impacts. In North America, operating profit contracted by 94%, mainly due to the loss in the hog raising business. In Europe, company operations benefited from higher hog prices and saw a 51% rebound in operating profit.

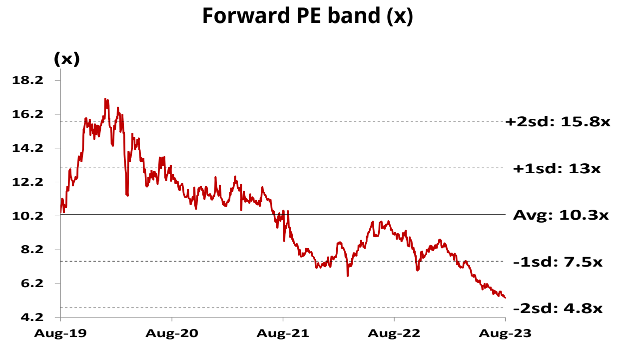
Packaged meat to sustain decent profit in China. In 1H23, hog price remained low, supporting a decent operating profit margin of 23% in China's packaged meat business. While hog price has seen a rebound in Jul-Aug so far, management expects average hog price to increase by 10-20% h-o-h in 2H23 to c.RMB17/kg. Per tonne profit of packaged meat is expected to sustain at c.RMB4,000 in 2H23 given that the company has largely stockpiled frozen pork inventory at c.RMB15/kg during 1H23. The pork sector should continue to sustain unit profit of RMB50-70/head with better profitability in the frozen pork sales in 2H23 amid the hog price uptrend.

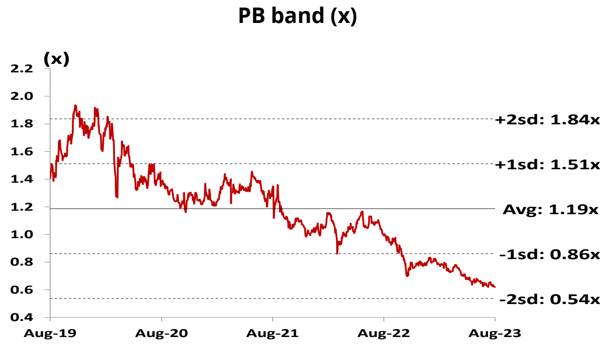
Continues to streamline hog farming in the US. The per-tonne profit of packaged meat reached a historical high of US$900 in 1H23, thanks to lower average pork prices in the US (down c.20% y-o-y). WH Group should be able to score a per-tonne profit of c.US$800 in FY23 for its packaged meat segment. In the meantime, hog raising costs remained high in 1H23, resulting in a loss in the US pork segment. WH Group has thus closed c.100 farms YTD in order to streamline the currently loss-making hog farming business. For the rest of FY23 and FY24, the company should continue to close certain underperforming and less efficient farms. Total production capacity should go below 15m heads by end of this year. We expect US operations to see sequential margin improvements in 2H23 as hog price rises in 3Q23, along with ongoing efficiency gains.

Company Background

WH Group is the largest pork company in the world, with leading positions in China, the US, and key markets in Europe. The group operates an integrated pork business chain including hog production, fresh pork, and packaged meat. WH Group is a controlling shareholder of Shuanghui Development (000895:CH), with a 70.33% stake; Asia's largest meat processing business; and controls 100% of Smithfield. As at end-2022, the group had a total of 4.09m tonnes of packaged meat production capacity (US: 2.14m tonnes; China: 1.62m tonnes; Europe: 0.33m tonnes), and 62.99m heads of fresh pork production capacity (China: 25.06m heads; US: 32.21m heads; Europe: 5.72m heads).

Historical PE and PB band





Source: Thomson Reuters, DBS HK

Segmental Breakdown (US$ m)

FY Dec	2020A	2021A	2022A	2023F	2024F
Revenues (US$ m)					
China	10,828	10,516	9,536	9,843	10,093
US	12,363	14,184	15,765	14,383	14,941
Others	2,398	2,593	2,835	3,229	3,257
Total	25,589	27,293	28,136	27,455	28,291
Segment result (US$ m)					
China	1,140	930	1,040	1,101	1,139
US	415	919	940	274	867
Others	174	117	113	166	174
Total	1,729	1,966	2,093	1,541	2,181
Segment result Margins (%)					
China	10.5	8.8	10.9	11.2	11.3
US	3.4	6.5	6.0	1.9	5.8
Others	7.3	4.5	4.0	5.1	5.3
Total	6.8	7.2	7.4	5.6	7.7

Source: Company, DBS HK

Income Statement (US$ m)

FY Dec	2020A	2021A	2022A	2023F	2024F
Revenue	25,589	27,293	28,136	27,455	28,291
Cost of Goods Sold	(21,096)	(22,587)	(23,202)	(23,061)	(23,170)
Gross Profit	4,493	4,706	4,934	4,394	5,121
Other Opng (Exp)/Inc	(2,788)	(2,841)	(2,924)	(2,853)	(2,940)
Operating Profit	1,705	1,865	2,010	1,541	2,181
Other Non Opg (Exp)/Inc	0	0	0	0	0
Associates & JV Inc	(87)	(98)	25	77	78
Net Interest (Exp)/Inc	(118)	(109)	(132)	(102)	(102)
Dividend Income	0	0	0	0	0
Exceptional Gain/(Loss)	0	0	283	0	0
Pre-tax Profit	1,500	1,658	2,186	1,516	2,157
Tax	(263)	(381)	(503)	(334)	(474)
Minority Interest	(264)	(234)	(282)	(286)	(251)
Preference Dividend	0	0	0	0	0
Net Profit	973	1,043	1,401	896	1,432
Net Profit before Except.	973	1,043	1,118	896	1,432
EBITDA	2,252	2,435	2,826	2,449	3,131
Growth					
Revenue Gth (%)	6.2	6.7	3.1	(2.4)	3.0
EBITDA Gth (%)	(10.6)	8.1	16.1	(13.4)	27.9
Opg Profit Gth (%)	(15.8)	9.4	7.8	(23.3)	41.5
Net Profit Gth (%)	(29.5)	7.2	34.3	(36.0)	59.7
Margins & Ratio					
Gross Margins (%)	17.6	17.2	17.5	16.0	18.1
Opg Profit Margin (%)	6.7	6.8	7.1	5.6	7.7
Net Profit Margin (%)	3.8	3.8	5.0	3.3	5.1
ROAE (%)	10.4	11.1	15.3	8.6	11.7
ROA (%)	5.4	5.5	7.1	4.3	6.3
ROCE (%)	9.4	9.2	9.8	7.2	9.2
Div Payout Ratio (%)	34.2	34.6	35.1	35.1	35.1
Net Interest Cover (x)	14.4	17.1	15.2	15.1	21.4

Source: Company, DBS HK

Balance Sheet (US$ m)

FY Dec	2020A	2021A	2022A	2023F	2024F
Net Fixed Assets	5,531	6,367	6,536	7,587	8,163
Invts in Associates & JVs	354	253	252	252	252
Other LT Assets	4,996	5,169	5,058	5,058	5,058
Cash & ST Invts	1,650	1,600	1,471	2,027	3,107
Inventory	2,641	2,625	2,855	2,838	2,851
Debtors	1,427	1,732	2,068	2,140	2,280
Other Current Assets	2,116	1,665	1,615	1,790	1,987
Total Assets	18,715	19,411	19,855	21,691	23,698
ST Debt	796	874	862	1,000	1,000
Creditors	1,223	1,222	1,118	1,202	1,273
Other Current Liab	2,048	2,479	3,005	2,988	3,001
LT Debt	1,840	3,140	2,504	2,504	2,504
Other LT Liabilities	1,823	2,009	1,954	1,909	1,867
Shareholder's Equity	10,005	8,748	9,600	11,276	13,241
Minority Interests	980	939	812	812	812
Total Cap. & Liab.	18,715	19,411	19,855	21,691	23,698
Non-Cash Wkg. Capital	2,913	2,321	2,415	2,577	2,844
Net Cash/(Debt)	(986)	(2,414)	(1,895)	(1,477)	(397)
Debtors Turn (avg days)	45.7	42.4	44.9	44.9	44.9
Creditors Turn (avg days)	15.8	18.6	21.9	21.9	21.9
Inventory Turn (avg days)	45.7	42.4	44.9	44.9	44.9
Asset Turnover (x)	1.4	1.4	1.4	1.3	1.2
Current Ratio (x)	1.9	1.7	1.6	1.7	1.9
Quick Ratio (x)	0.8	0.7	0.7	0.8	1.0
Net Debt/Equity (X)	0.1	0.2	0.2	0.1	0.0
Net Debt/Equity ex MI (X)	0.1	0.3	0.2	0.1	0.0
Capex to Debt (%)	20.9	23.0	28.2	17.1	17.1
Z-Score (X)	NA	NA	NA	NA	NA

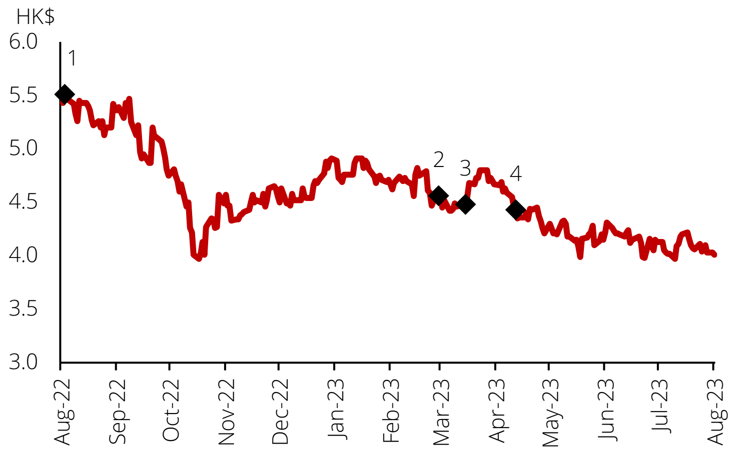
Source: Company, DBS HK

Cash Flow Statement (US$ m)

FY Dec	2020A	2021A	2022A	2023F	2024F
Pre-Tax Profit	1,315	1,700	2,132	1,516	2,157
Dep. & Amort.	644	679	802	831	872
Tax Paid	(418)	(288)	(449)	(334)	(474)
Assoc. & JV Inc/(loss)	0	0	0	0	0
(Pft)/ Loss on disposal of FAs	585	298	(18)	(286)	(251)
Chg in Wkg.Cap.	382	(410)	(665)	(162)	(267)
Other Operating CF	(12)	(27)	(19)	0	0
Net Operating CF	2,496	1,952	1,783	1,565	2,037
Capital Exp.(net)	(551)	(922)	(948)	(600)	(600)
Other Invts.(net)	0	0	0	0	0
Invts in Assoc. & JV	0	0	0	0	0
Div from Assoc & JV	0	0	0	0	0
Other Investing CF	(412)	513	598	(45)	(43)
Net Investing CF	(963)	(409)	(350)	(645)	(643)
Div Paid	(599)	(332)	(311)	(502)	(315)
Chg in Gross Debt	3,279	5,220	3,730	138	0
Capital Issues	880	(1,931)	0	0	0
Other Financing CF	(4,039)	(4,390)	(4,810)	0	0
Net Financing CF	(479)	(1,433)	(1,391)	(364)	(315)
Currency Adjustments	0	0	0	0	0
Chg in Cash	1,054	110	42	556	1,080
Opg CFPS (US$)	0.14	0.17	0.19	0.13	0.18
Free CFPS (US$)	0.13	0.07	0.07	0.08	0.11

Source: Company, DBS HK

Target Price & Ratings 12-mth History



S.No.	Date	Closing Price	Target Price	Rating
1	17-Aug-22	HK$5.43	HK$6.79	BUY
2	14-Mar-23	HK$4.59	HK$6.32	BUY
3	29-Mar-23	HK$4.47	HK$6.29	BUY
4	26-Apr-23	HK$4.45	HK$5.96	BUY

Source: DBS HK

Analyst: Clement Xu

Mavis Hui

DBS HK recommendations are based on an Absolute Total Return* Rating system, defined as follows:
STRONG BUY (>20% total return over the next 3 months, with identifiable share price catalysts within this time frame)
BUY (>15% total return over the next 12 months for small caps, >10% for large caps)
HOLD (-10% to +15% total return over the next 12 months for small caps, -10% to +10% for large caps)
FULLY VALUED (negative total return, i.e., > -10% over the next 12 months)
SELL (negative total return of > -20% over the next 3 months, with identifiable share price catalysts within this time frame)

**Share price appreciation + dividends*

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Sources for all charts and tables are DBS HK unless otherwise specified.

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