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## FY1Q11 earnings review: Earnings turnaround

### What's new

KSL reported a FY1Q11 net profit of Bt144.4mn, improving from a net loss of Bt63mn in FY1Q10 (restatement) and net profit of Bt51.2mn in FY4Q10 (restatement). Gross margin improved to 26.7%, from 24.4% in 1Q10 and 17.1% in 4Q10. Additionally, there was no loss from derivatives in the quarter. The company reported loss from derivatives of Bt236.6mn in FY1Q10 and Bt600K in 4Q10.

### Implications

FY1Q11 earnings turned around as we expected. The gross margin improved YoY and QoQ due to easing competition between sugar millers to buy sugar cane compared to last fiscal year as there is no oversell problem. The key factor behind the earnings turnaround was the absence of loss from derivatives.

Sugar prices are currently down to around US\$0.26/lbs, which is lower than our forward contracts assumption of US\$0.28/lbs. This may imply KSL would not book loss from derivatives in FY2Q11, so we anticipate FY2Q11 to be the company's peak quarter for the year as the second quarter is typically the high season for the sugar mill.

Though KSL reported improved operations in the quarter and FY2Q11 earnings should grow QoQ and are expected to be the peak quarter, we believe that the upside in the share price is limited. Sugar prices should have already passed their peak in early 2011 and world supply of sugar next season is expected to increase. Thus a decline in sugar prices would depress investment sentiment on KSL's shares. Furthermore, all sugar mills in Thailand currently have to reserve an additional 300K tons of sugar for sell domestically (Quota A.), if there is supply shortage in 2011. This implies that there is a risk that Quota A would be raised to 2.8mn tons from 2.5mn tons for 2011. If the quota were lifted, KSL's full-year earnings are expected to be 6.6% below our current projection of Bt930mn, as the domestic price is lower than the current export price.

### Valuation & action

Given the two risk factors, KSL should not trade at its historical high PE of 30x as we previously expected. Currently, the counter trades at 23x 11PE. We will review our target price and rating on KSL after its analyst meeting on 23 March, but for now maintain a rating of Outperform with a target price of Bt17.00.

Figure 1: FY1Q11 earnings summary

Bt mn	FY1Q11	FY1Q10	YoY(%)	FY4Q10	QoQ (%)	Comment
Sales	2,610.0	2,555.6	2.1	2,316.7	12.7	
COGS	(1,914.3)	(1,931.9)	(0.9)	(1,920.8)	(0.3)	
Gross profit	695.7	623.7	11.5	395.9	75.7	
SG&A	(489.1)	(478.4)	2.2	(329.3)	48.5	
EBIT	303.3	211.9	43.1	162.2	87.0	
Interest expense	(89.0)	(63.9)	39.2	(95.4)	(6.7)	
Normalized profit	144.4	173.5	(16.8)	51.8	178.9	
Extra Items	N.A.	(236.6)	N.A.	(0.6)	N.A.	No loss from derivatives in the quarter
Net profit	144.4	(63.0)	N.A.	51.2	182.2	
EPS (Bt)	0.09	(0.04)	N.A.	0.03	182.2	
Percent	FY1Q11	FY1Q10	YoY (ppts)	FY4Q10	QoQ (ppts)	
Gross margin	26.7	24.4	2.2	17.1	9.6	Gross margin improved YoY and QoQ
SG&A to sales	18.7	18.7	0.0	14.2	4.5	
EBIT margin	11.6	8.3	3.3	7.0	4.6	
Net profit margin	5.5	(2.5)	8.0	2.2	3.3	

Source: Company data; KGI Securities (Thailand)

\*The Company may be issuer of Derivative Warrants on these securities.

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		<i>* Excess return = 12M target price/current price-1</i>
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