

British American Tobacco

Hold

(RM43.98 ROTH MK)

Target Price: RM43.00

2QFY10 : Illicit levels marginally lower

CONSUMER

- 6MFY10 revenue +1.5% y-o-y, net profit -7.2% y-o-y**

BAT's 6MFY10 results were within our and consensus estimates. Revenue and net profit represented about 51% and 52% of house FY10 estimates respectively. Against FY10 consensus estimates, revenue and net profit were at 51% and 49% respectively.

Growth in revenue came from higher excise led pricing partially offset by unfavourable pack size mix due to ban on packs less than 20 sticks and lower sales volume. Profitability however fell due to higher costs of Dunhill Reloc packs and timing of A&P expenses. More positively, illicit trade is understood to have fallen from a peak of 38.7% to 37% and is likely to trend marginally downwards or stay flat, though latest official figures were not available yet.

- 6MFY10 sales volume -1.6% y-o-y, TIV -0.9% y-o-y**

BAT's 6MFY10 sales volume dropped 1.6% to 4.47bn sticks, in contrast to a smaller drop in total industry volume (TIV) of 0.9% to 6.85bn sticks. BAT's sales volume was somewhat affected by the gradual phase out of 14-stick packs in preparation for the withdrawal of less than 20 stick packs implemented in Jun. On the other hand, strong economic growth in 1HCY10 had helped to stem the decline in overall TIV. As for YTD market share in May, Dunhill was resilient in the premium segment at 43.9% (-0.1ppt y-o-y), while Kent's rose 0.1 ppt y-o-y to 2.8%. In the value-for-money segment, Pall Mall gained 0.4 ppt to record 7.9% market share.

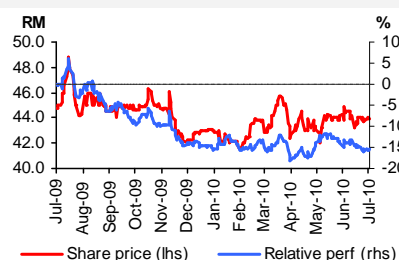
- 113 sen 1st interim dividend declared**

The 1st interim tax exempt dividend is within expectations. Hence, we maintain our net DPS forecast of RM2.42 for FY10 based on 90% payout ratio. This implies a decent dividend yield of 5.5%.

- Reiterate HOLD, target price maintained at RM43.00**

We reiterate our HOLD rating for BAT and DCF-derived target price at RM43.00 (WACC: 7.3%, g: 0.5%). While the operating environment has improved for BAT as illicit levels start to subside, the withdrawal of less than 20 stick packs will put pressure on margins in 2HFY10. Nonetheless, BAT has seen a positive migration trend in pack size mix during Apr and May, which has actually helped Dunhill record its highest ever market share of 44.8% in May. It is still early days though and we will likely see a clearer picture in 3QCY10. Key risks to our recommendation are (1) more than expected consumers down-trading, and (2) a steeper than anticipated decline in TIV.

Share Price Chart



Source: Bloomberg

Price Performance

Price (RM)	43.98		
52-week Range (RM)	41.60 – 48.76		
Avg Daily Volume ('000)	90		
	1M	3M	6M
Absolute (%)	0.4	2.3	2.8
Relative (%)	0.6	3.6	0.0

Key Data

Market Cap (RM m)	12,558
Issued Shares (m)	285

Major Shareholders

	%
BAT Holdings B.V. Bhd	50
Permodalan Nasional Bhd	6

Balance Sheet Highlights (RM m)

(@ 31.12.2010) (performance indicator's annualised)

Total Assets	1,634
Total Liabilities	1,074
Total Debt (Gross)	650
Shareholders' Equity	560

Return on Assets (%)	46.9
Return on Equity (%)	136.9
Net Cash / Share (RM)	-

Debt / Equity (x)	1.2
Interest Cover (x)	38.1

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Financial summary

FYE 31 Dec	2008	2009	2010F	2011F	2012F
Revenue (RM m)	4,135.2	3,923.4	3,928.5	4,043.8	4,261.3
EBITDA (RM m)	1,182.2	1,108.9	1,123.2	1,156.1	1,218.3
Net profit (RM m)	811.7	746.8	767.1	797.9	845.9
EPS (sen)	284.3	261.5	268.7	279.5	296.2
ECM / Consensus (%)			104.9	107.6	110.7
EPS growth (%)	10.9	(8.0)	2.7	4.0	6.0
P/E (x)	15.5	16.8	16.4	15.7	14.8
Net DPS (sen)	265.0	236.0	242.4	252.2	267.3
Dividend yield (%)	6.0	5.4	5.5	5.7	6.1
BVPS (RM)	2.85	3.08	3.60	4.15	4.73
P/BV (x)	15.4	14.3	12.2	10.6	9.3

Figure 1 : Results analysis

RM m	2Q10	2Q09	1Q10	% y-o-y chg	% q-o-q chg	6M10	6M09	% y-o-y chg	Comments
Revenue	994	978	1,019	1.7	(2.4)	2,013	1,983	1.5	Higher pricing offset by lower sales volume
Gross profit	381	377	395	1.2	(3.4)	776	782	(0.7)	
PBT	250	270	258	(7.4)	(3.1)	508	543	(6.4)	
Net profit	186	201	192	(7.7)	(3.2)	378	407	(7.2)	
Margin (%)									
Gross profit	38.4	38.6	38.7	(0.2)	(0.4)	38.6	39.4	(0.9)	Lower due to higher costs of Reloc packs
Net profit	18.7	20.6	18.8	(1.9)	(0.1)	18.8	20.5	(1.8)	
EPS (sen)	65.1	70.5	67.2	(7.7)	(3.1)	132.3	142.6	(7.2)	
Net DPS (sen)	113.0	113.0	-			113.0	113.0		
BVPS (RM)	2.23	2.09	2.20			2.23	2.09		

Source: Company, ECM Libra

Key to stock recommendations:

Buy = Share price is expected to appreciate by >10% over the next 12 months
Hold = Share price is expected to move by less than +/-10% over the next 12 months
Sell = Share price is expected to decline by >10% over the next 12 months

Key to sector recommendations:

Overweight = Industry expected to outperform the market over the next 12 months
Neutral = Industry expected to perform in-line with the market over the next 12 months
Underweight = Industry expected to underperform the market over the next 12 months

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