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*Edge Weekly*

# High feed costs and lower prices have poultry players walking on eggshells

Lee Weng Khuen / The Edge Malaysia

September 07, 2021 15:00 pm +08

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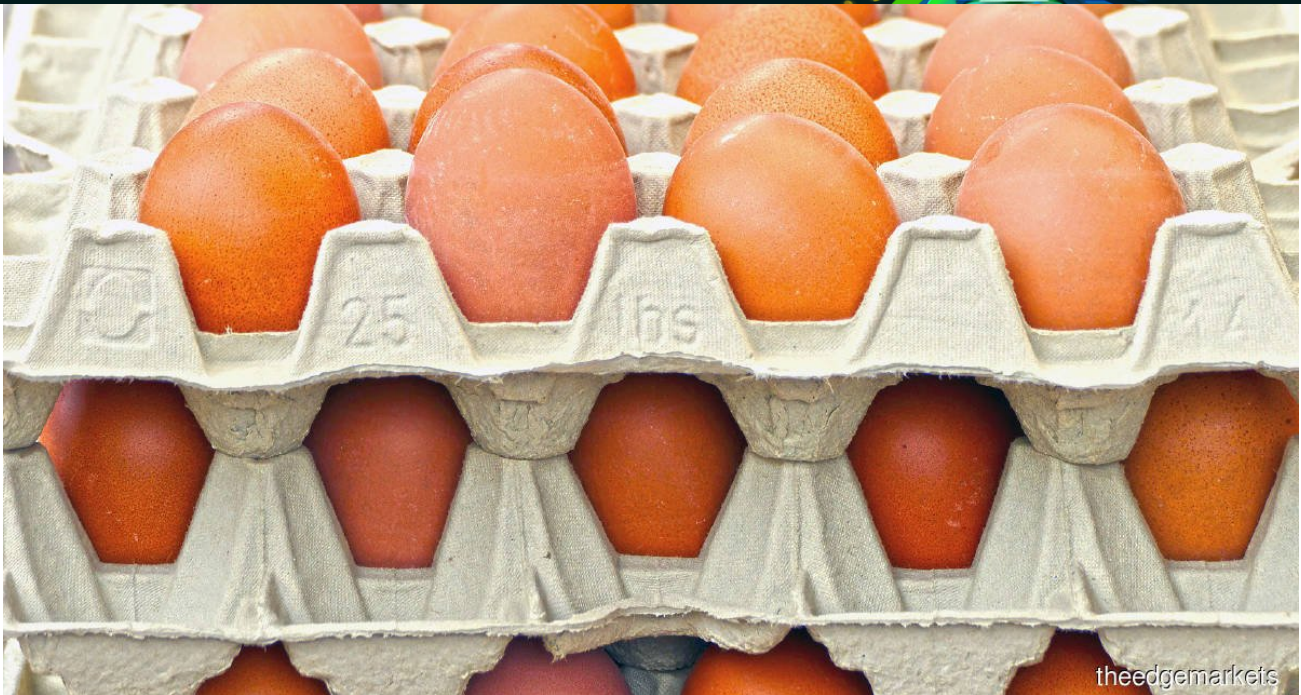
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MALAYSIAN egg producers are walking on eggshells. Hit by low consumption and average selling prices (ASPs) on the back of persistent movement restrictions imposed by the government to curb the spread of Covid-19, rising feed production costs have added to their misery.

Indeed, the higher costs of soybean and maize appear to be inflicting a more significant impact on their business operations.

Malacca Securities Sdn Bhd head of research Loui Low thinks that the current situation may drag on for another six months before a normalisation in raw material prices can be seen.

“The high feed price costs stem from the weakening of the ringgit and elevated demand for these raw materials. They will definitely stabilise and normalise, probably by another two quarters,” he tells The Edge.

HLIB Research analyst Syifaa’ Mahsuri Ismail says climate change, which has affected harvesting, has contributed to the incremental increase in livestock feed costs as well.

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Hence, I would say it's a double whammy for egg producers with selling prices falling and cost to produce increasing, which has resulted in shrinking margins," she notes.

Compared with other poultry players, Low says the overall impact on Teo Seng Capital Bhd — a subsidiary of Leong Hup International Bhd — will be more significant as it is highly dependent on the egg production segment. However, he has upgraded Teo Seng to a "hold" from "sell" with a target price of 69 sen.

Teo Seng and Lay Hong Bhd are the underperformers in the sector, with their share prices falling 19.2% and 20% respectively year to date. QL Resources Bhd and Leong Hup have slipped by a more marginal 3.3% and 0.7% respectively.

Egg prices tumbled by a considerable 26% year on year in 2Q2021 to average 25 sen each. Low expects prices to hold at around 35 sen each for Grade C chicken eggs amid a gradual resumption of economic activities, along with improved vaccination rates in Malaysia. Average Grade C chicken egg prices saw an improvement in July to 35 sen.

Meanwhile, soybean prices rose 7.6% quarter on quarter in 2Q2021 on concerns of tighter market conditions amid renewed foreign demand. Likewise, maize prices spiked 10.3% q-o-q on the back of supply concerns due to unfavourable weather as well as heightened export demand.

Would expanding export markets help mitigate the egg price pressure?

Low opines that margins ought to be the same for both domestic and export markets. "I don't think it will be a very huge difference because the cost is higher compared with the demand. So, the cost impact outweighs that of demand. Furthermore, everywhere is under lockdown, so it won't help much."

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“I reckon it’ll be a challenging year for poultry players with the still heightened livestock feed costs,” she says, adding that she has not made any rating or target price changes pending the release of financial results.

QL Resources recently flagged a negative outlook for its integrated livestock farming (ILF) division as egg prices in Peninsular Malaysia are expected to continue falling given the industry glut. It also warned that raw material prices are likely to remain at “extremely high” levels, putting pressure on its farming operations.

The company’s net profit tumbled 63% to RM42.19 million for the quarter ended June 30, against RM114.06 million in the preceding quarter. Its ILF division saw severe margin erosion on the back of high feed raw material prices and a drastic surge in Covid-19 cases.

Lay Hong executive director Datuk Yap Chor How believes that egg prices will remain volatile in the near term, but they are not expected to remain weak in the long term as eggs remain among the main sources of protein for most Malaysians.

“We hope that the gradual reopening of the economy and easing of restrictions that allow fully vaccinated individuals to eat out will drive the demand for eggs going forward,” he tells The Edge.

Yap says Lay Hong has mostly priced in the impact of lower egg prices in the group’s long-term growth strategies. In the interim, it is focusing on ensuring a more agile management and workforce for better cost management efficiency.

“The group has also embarked on digital transformation initiatives to improve the operation process and engagement with our customers via various platforms.”

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value adjustments on biological assets recognised and one-off revaluation loss on certain property, plant and equipment.

Leong Hup, which undertakes the egg production business through Teo Seng, notes that the ASPs of table eggs appear to have stabilised since mid-July, owing to a relative improvement in demand-supply dynamics.

“Apart from weighing on business activities and consumer spending, the prolonged transitions between shut and open containment measures have meant that it is harder to plan ahead [for] the production cycle of layering hens,” a spokesperson tells The Edge.

He says that since the onset of Covid-19 and the enforcement of lockdowns, commercial egg producers have been proactively managing their flocks, including retiring layering hens earlier, in a bid to restore demand-supply equilibrium during this uncertain period.

“Barring unforeseen circumstances, smooth progress in the National Recovery Plan is expected to help restore and stimulate demand for poultry and eggs, as well as ensure a sustained recovery of ASPs,” the spokesperson adds.

## Going further downstream

Because of the protracted impact from Covid-19, the spokesperson reveals that Teo Seng’s strategy is to go further downstream for stronger pricing ability and better margins. For instance, it started selling hard-boiled eggs in 2Q2021, although the sales volume is still small.

Nonetheless, challenges abound, he acknowledges, as the pandemic has accelerated the process of consolidation in the industry. “Commercial integrated producers that have the strength in balance sheet and ability to withstand short-term losses (due to the higher than usual fluctuation in selling prices since last year) have been gradually picking up market share.

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managed to maintain operations with increased y-o-y sales volume, despite total industry volume declining since last year due to the pandemic,” he adds.

Teo Seng’s net loss widened to RM10.53 million in its second quarter ended June from RM798,000 in 1QFY2021, mainly due to the increase in feed production costs, despite a slight rise in revenue of 2.2% q-o-q to RM118.02 million, driven by higher sales of eggs.

Similarly, Leong Hup was also hit by an increase in raw material costs for livestock feed production, which led to a 56.6% q-o-q slump in net profit to RM30.5 million against RM70.33 million in 1QFY2021.

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