



Don Agro International Ltd

(DAG SP/GRQ.SI)

Your source of bread and butter

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- Don Agro International (Don Agro) is one of the largest agricultural companies in Russia's Rostov region. It has a stable track record of profitability over the last five years, with net income reaching a record in 2020.
- We expect Don Agro to outperform again this year on the back of strong commodity prices for wheat and corn that are at their highest since 2014.
- We initiate with an Outperform recommendation and a DCF-backed target price of S\$0.64.

Financials & Key Operating Statistics					
YE Dec (S\$'000)	2019	2020	2021F	2022F	2023F
Revenue	35,431	30,996	40,914	42,824	47,295
PATMI	5,209	8,696	9,811	7,444	8,273
EPS (cents)	4.17	5.79	6.53	4.95	5.51
EPS growth (%)	(17.0)	38.9	12.8	(24.1)	11.1
Price P/E (x)	9.4	6.7	6.0	7.9	7.1
DPS (Sing cents)	0.7	1.2	1.3	1.0	1.1
Div Yield (Y%)	1.8%	3.0%	3.3%	2.5%	2.8%
Net Profit Margin (%)	14.7%	28.1%	24.0%	17.4%	17.5%
Net Gearing (%)	Net Cash	Net Cash	Net Cash	Net Cash	Net Cash
Price P/B (x)	1.30	1.35	1.14	1.03	0.92
ROE (%)	15.6%	21.5%	20.7%	13.7%	13.7%

Source: Company data, KGI Research

A Valentine's Day to remember. Listed on the Catalist board of SGX on 14 February 2020, Don Agro is one of the largest agricultural groups based in the Rostov Region of Russia. The group had its beginnings in 2009 when it was incorporated as a result of a reorganisation by merger of five agricultural companies, which were privatised collective farms. It initially owned approximately 3,500 hectares of land.

Executive Chairman and major shareholder Evgeny Tugolukov invested into Don Agro in 2012. Over the last ten years, the group has expanded through acquisitions of companies and land, and now has a total controlled land bank of 63,240 hectares, of which 51,200 hectares are arable land. The group produced a total of 87,852 tonnes of wheat, corn and sunflower, and 16,015 tonnes of raw milk in 2020. The breakdown between its different crops is shown in the table below.

Table 1: Production capacity summary

Crop/Livestock	Production in 2020 (tonnes)	Comments
Wheat	64,923	51,200 ha of arable land. 103,000 tonnes of grain storage capacity
Corn	5,291	
Sunflower	17,638	
Raw milk	16,015	2,188 milking cows

Source: Company, KGI Research

Where in the world... Don Agro operates within two main regions in Russia, both of which are among the most fertile regions in the country. The main operating division (53,240 hectares) is in the Millerovo District, Rostov Region, located close to terminals operated by international traders such as

Outperform - Initiation			
Price as of 22 Jul 21 (SGD)	0.39	Performance (Absolute)	
12M TP (\$)	0.64		1 Month (%) 2.6
Previous TP (\$)	-		3 Month (%) 5.8
Upside, incl div (%)	66.9		12 Month (%) 54.6
Trading data		Perf. vs STI Index (Red) 	
Mkt Cap (\$mn)	59		
Issued Shares (mn)	150		
Vol - 3M Daily avg (mn)	0.0		
Val - 3M Daily avg (\$mn)	0.0		
Free Float (%)	16.8%		
Major Shareholders		Previous Recommendations	
Evgeny Tugolukov	78.2%		

Cargill, Bunge and Glencore. The acquisition of Volgo-Agro LLC in 4Q2020 helped the group expand another 10,040 hectares into the Volgograd Region, located to the north of the Rostov Region. This new location would enable the group to reach new markets and customers.

Profitable farmer and a new milestone. Don Agro reported a record net profit of S\$8.7mn in 2020, representing a 66% YoY increase and more than double its 2016-2017 net profit.

Table 2: Financial summary

S\$'000	2016	2017	2018	2019	2020
Revenue	30,979	23,193	24,375	35,431	30,996
Gross Profit	5,913	6,747	9,062	8,589	14,626
Net Profit	4,203	4,096	6,388	5,223	8,696

Source: Company, KGI Research

A bowl full of opportunities. Favourably located and well-managed, Don Agro is in a sweet spot. Wheat demand, which is the key driver of the group, is forecasted to grow by almost 18% from 2019 to 2029, according to estimates by the US Department of Agriculture's Foreign Agricultural Service (USDA FAS). Furthermore, wheat, as a staple food source, provides a resilient revenue stream for the group despite changing economic trends.

Valuation & Action: We initiate with Outperform and a TP of S\$0.64 based on discounted cash flow, taking into account a WACC of 11.0% and terminal growth rate of 3.0%. Don Agro's current valuations are attractive as it only trades at 6.0x FY2021F EPS. With a good track record and healthy outlook, Don Agro is well-positioned to ride on long-term global trends.

Risks: Bad weather is the key short-term risk that will impact production volumes. Rising costs may impact profit margins if they rise faster than the group's selling price.

See the last page for important disclosures.

Contents

At a glance	3
Investment thesis.....	4
Sorting the wheat from the chaff: Market leadership in Rostov.....	4
Acquisition-led growth, supported by healthy balance sheet.....	4
Meeting the demand of a growing world.....	4
Valuations and peer comparison	5
Key valuation drivers	5
Base case valuation	5
Upside case valuation.....	6
Downside case valuation.....	6
Peer comparison	7
Agricultural related companies	7
Forecasts and financial review.....	8
Macro and Industry Outlook.....	10
Global economic growth boosted by fiscal and monetary policies	10
A focus on wheat and milk, Don Agro’s bread and butter	10
Company Background	15
A decade of experience	15
Big is better	15
Management team.....	16
Key Risks	17
Financial Summary.....	18
Appendix A: Type of crops and seasonality	19
Type of crops	19
Seasonality	19
Appendix B: Long-term Agricultural price trends	20

Rostov-on-Don and the
River Don, Russia

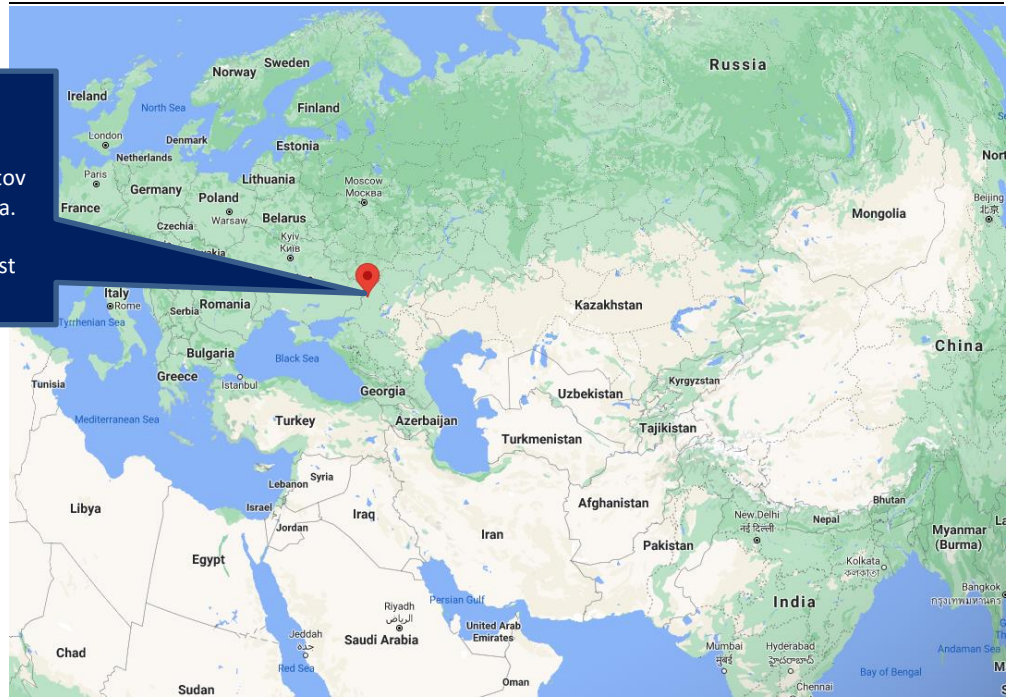


At a glance

Figure 1: Where in the world...Don Agro is located 800km south of Moscow, and around 8,000km from Singapore



Don Agro's farms are in the Rostov and Volgograd Regions in Russia. These areas are among the most fertile in the country.



Source: Google Maps, KGI Research

Did you know?

Bill Gates is the largest private owner of farmland in the US, having bought more than 100,000 hectares across 18 states.

In our upside case scenario, we expect Don Agro to have more than 100,000 hectares by 2023.

Millerovo District, Rostov Region

Main operating division with a controlled land bank of approximately **53,240 hectares**

Located close to the Azov Sea and Don River international ports

Allows for customers (mainly traders and exporters) to save on transportation costs

International traders such as Cargill, Bunge, Glencore, Louis Dreyfus have terminals located in this region

Kamyshinsky District, Volgograd Region

Second operating division with a controlled land bank of approximately **10,040 hectares**

Located north of the Caspian region and in basin of the Volga River, historically Russia's main waterway for trade with the Middle East and Asia

Also borders on Kazakhstan, a key gateway to markets such as China and the rest of Central Asia

Enables Group to reach new markets and customers

Crop production

Production of wheat, sunflower and corn

Total production in 2020:
64,923 tonnes of wheat
5,291 tonnes of corn
17,638 tonnes of sunflower

Revenue of S\$23.5mn in 2020
EBITDA of S\$10mn in 2020

Livestock

Production of raw milk and sale of livestock

Total production in 2020:
16,015 tonnes of raw milk

Revenue of S\$9.8mn in 2020
EBITDA of S\$0.4mn in 2020



Investment thesis

Sorting the wheat from the chaff: Market leadership in Rostov

Don Agro has been operating as a single entity for more than 10 years, a result of the privatisation of five collective farms. The group’s good financial track record can be attributed to the experienced gained and the structured and hands-on farm management practices, which continue to be overseen by a senior management team who has been with the group since at least 2015.

Executive Chairman and major shareholder, Evgeny Tugolukov, invested into Don Agro in 2012, and was previously a Member of Parliament of the State Duma of the Russian Federation, as well as the Chairman of the State Duma Committee on Natural Resources. He promoted bilateral trade and business relations between Russia and Singapore from 2014 to 2018, when he was an honorary business representative with [Enterprise Singapore](#).

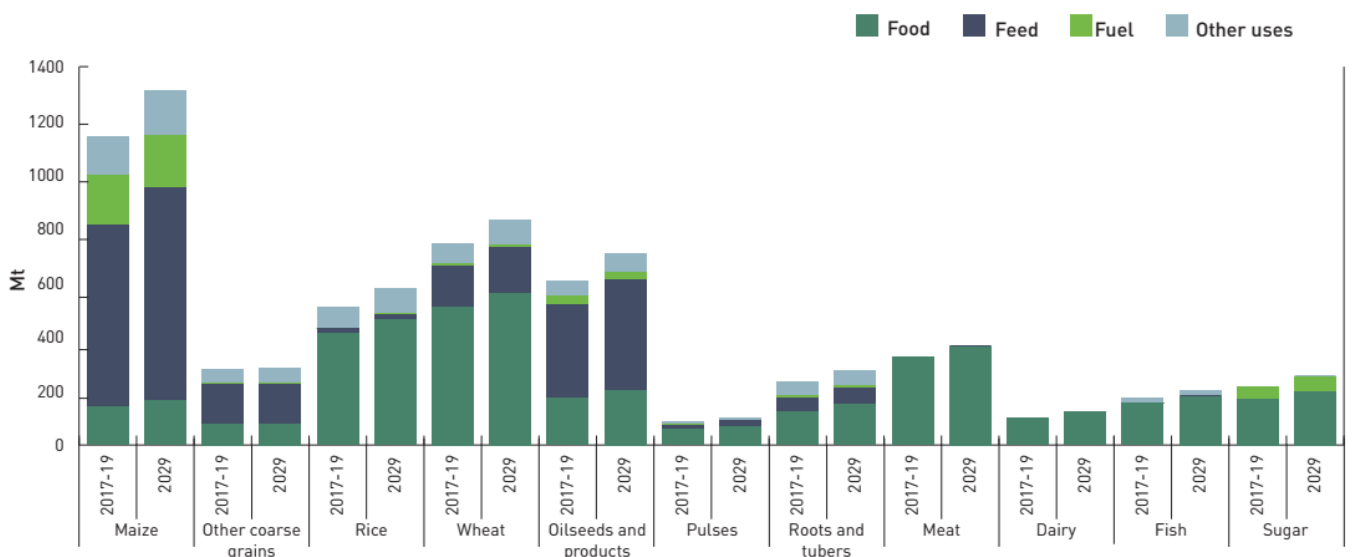
Acquisition-led growth, supported by healthy balance sheet

We expect growth to be primarily driven by acquisitions. With the purchase of Volgo-Agro LLC (Volgo-Agro) in 4Q2020, Don Agro added around 10,040 hectares to its land bank, increasing it by 19% to 63,240 hectares as at end-2020. In the future, the group is in a robust financial position to embark on more acquisition-led growth and to continue to invest in new machinery, thereby increasing production yield. The group has generated positive free cash flows since 2018 and was in a net cash position of S\$7mn as at end-2020.

Meeting the demand of a growing world

Don Agro’s key products are wheat, sunflower, corn, and raw milk. All these agricultural and dairy products are witnessing global demand growth, albeit at varying growth rates. The OECD-FAO forecasts that the expanding global population remains the key growth factor for agricultural demand. Historically, China’s growth has been the main driver of demand and international trade of agricultural products. However, this may shift to other regions which are displaying faster population growths, such as Africa and South Asia.

Figure 2: OECD-FAO forecasts of major commodities, and the breakdown of their usage in food, feed, and fuel.



Source: OECD-FAO Agricultural Outlook 2020

Valuations and peer comparison

We initiate Don Agro with an Outperform recommendation and a S\$0.64 price target under our base case scenario. Don Agro is well-positioned as a market leader in Russia's Rostov region to expand and diversify its product range. The group's extensive land bank, continuous investments to improve crop yields and experienced management team, bode well for delivering shareholder returns.

While investors should not overlook country-specific risks, these are offset by positive long-term structural demand trends and the group's diversification strategy.

We expect Don Agro's valuations to be driven primarily by land bank size and EBIT margins.

Key valuation drivers

The two key drivers of Don Agro's valuation are total controlled land bank and EBIT margins. While commodity prices impact revenue, we have assumed normalised prices that consider the complete commodity cycle. Taxes are minimal as there is zero corporate income tax for agricultural enterprises in Russia. There is a 5% withholding tax for dividends to Singapore.

Valuation	Assumptions for 2021-2025	Valuation per share (S\$)
Base	Increase arable land bank by 7,000 hectares per annum and 19.5% EBIT margin. Capex increases accordingly for acquisition and improvement works.	S\$0.64
Upside	Increase arable land bank to 115,000 hectares by 2023, from current 51,200 hectares. Capex increases accordingly for acquisition and improvement works. EBIT margin of 22.5%	S\$0.82
Downside	No new acquisitions, 17.5% EBIT margin, higher WACC and lower terminal growth rate	S\$0.45

Base case valuation

Our base case valuation scenario utilises a fairly conservative set of assumptions to derive a discount cash flow (DCF) based fair value for Don Agro. Arable land bank increases at a rate of 7,000 hectares per year. We applied an 11.0% discount rate and a 3.0% terminal growth rate. The cost of debt is at 5.0%, and the cost of equity equals 12.2%. We assume an EBIT margin of 19.5% vs its 5-year average of 23.2%.

Discounted Cash Flow (S\$'000)	2020	2021F	2022F	2023F	2024F	2025F	Terminal
EBIT	9,702	10,842	8,351	9,223	10,095	10,967	
TAX	(315)	(516)	(392)	(435)	(479)	(523)	
D&A	2,139	2,782	2,912	3,216	3,520	3,824	
Change in NWC	(4,086)	(5,045)	(1,577)	(1,480)	(1,480)	(1,480)	
Capex	(4,072)	(3,500)	(3,500)	(3,500)	(3,500)	(3,500)	
Unlevered Free Cash flow	3,368	4,563	5,793	7,023	8,156	9,288	119,583
Valuation							
Enterprise Value (S\$'000)	\$88,766						
Less Net Debt / Add Net Cash (S\$'000)	7,092						
Equity Value (S\$'000)	\$95,858						
Shares outstanding ('000)	150,273						
Equity value/share (S\$)	\$0.64						
Implied historical P/E (x)	11.0x						
Implied forward P/E (x)	9.8x						
Assumptions							
Discount Rate	11.0%						
Perpetual Growth Rate	3.0%						

Upside case valuation

Our upside case assumes that Don Agro can optimise its asset portfolio to yield a higher EBIT margin of 22.5%. We also forecast a larger arable land bank size that more than doubles to 115,200 hectares by 2023. Our capex assumption rises accordingly to account for acquisitions and improvement works. As a result, upside case scenario is S\$0.82.

Our upside valuation assumes a doubling of land size by 2023.

Don Agro started off with only 3,500 hectares in 2009, and now has 63,240 hectares.

Discounted Cash Flow (S\$'000)	2020	2021F	2022F	2023F	2024F	2025F	Terminal
EBIT	9,702	10,842	11,813	16,581	16,598	16,614	
TAX	(315)	(516)	(565)	(803)	(804)	(805)	
D&A	2,139	2,782	3,570	5,011	5,016	5,021	
Change in NWC	(4,086)	(5,045)	(4,262)	(6,804)	(23)	(23)	
Capex	(4,072)	(5,000)	(8,000)	(10,000)	(7,500)	(7,500)	
Unlevered Free Cash flow	3,368	3,063	2,557	3,985	13,286	13,307	171,324

Valuation

Enterprise Value (S\$'000)	\$115,994
Less Net Debt / Add Net Cash (S\$'000)	7,092
Equity Value (S\$'000)	\$123,086
Shares outstanding ('000)	150,273
Equity value/share (S\$)	\$0.82
Implied historical P/E (x)	14.2x
Implied forward P/E (x)	12.5x

Assumptions

Discount Rate	11.0%
Perpetual Growth Rate	3.0%



More upside to our upside scenario by going organic. In line with Don Agro's diversification strategy, it has allocated an initial 11.0 hectares of land to grow organic food. It plans to harvest 25-40 tonnes on a trial basis, and once proven, will scale up acreage and production across its land bank. We believe this is an excellent opportunity to increase margins as organic wheat can be 2-5 times more expensive than regular wheat. While we have not factored this into our forecasts, this segment provides significant upside potential for Don Agro if it can successfully scale up.

Downside case valuation

We derive a bear case valuation of S\$0.45 when we assume lower EBIT margins near its 5-year historical low of 17.5%. We also increased the discount rate to 12.0% while lowering the terminal growth rate to 2.0%.

Discounted Cash Flow (S\$'000)	2020	2021F	2022F	2023F	2024F	2025F	Terminal
EBIT	9,702	10,842	6,724	6,737	6,749	6,762	
TAX	(315)	(516)	(310)	(311)	(312)	(312)	
D&A	2,139	2,782	2,613	2,618	2,623	2,627	
Change in NWC	(4,086)	(5,045)	(375)	(24)	(24)	(24)	
Capex	(4,072)	(2,000)	(2,000)	(2,000)	(2,000)	(2,000)	
Unlevered Free Cash flow	3,368	6,063	6,652	7,019	7,036	7,053	71,936

Valuation

Enterprise Value (S\$'000)	\$60,630
Less Net Debt / Add Net Cash (S\$'000)	7,092
Equity Value (S\$'000)	\$67,722
Shares outstanding ('000)	150,273
Equity value/share (S\$)	\$0.45
Implied historical P/E (x)	7.8x
Implied forward P/E (x)	6.9x

Assumptions

Discount Rate	12.0%
Perpetual Growth Rate	2.0%

Peer comparison

Agricultural related companies

Don Agro does not have a directly comparable local peer when we look at wheat and corn production. Nevertheless, we have included agricultural-related companies, both local and foreign listed, in the comparison table below. This is to provide a reference for investors to gauge the valuation profile of agricultural-related companies.

Closest, but still not comparable. SGX-listed Olam International (OLAM SP) may be considered the closest peer as it has overlapping businesses in wheat and dairy production. However, we note that Olam's focus is primarily in cocoa, coffee, rice, nuts and spices. In addition, Olam's business spans from animal feed to processing. Other related agricultural SGX-listed companies are in the palm oil business and include Wilmar International (WIL SP), Golden Agri-Resources (GGR SP) and First Resources (FR SP).

Meanwhile, many US-listed companies, including Archer-Daniels-Midland Company and Bunge, are focused on trading and processing, with some of them being buyers of Don Agro's products.

In the dairy business, the closest comparable peer is Japfa (JAP SP). However, Japfa is also not directly comparable given its presence in both the upstream and downstream business segments of the dairy supply chain. In addition, Japfa is involved in other businesses such as animal protein (poultry, swine, beef, and aquaculture) and the distribution of branded consumer goods.

Peer valuation multiples are in line with our DCF-derived valuation. Our DCF-derived valuations for Don Agro are in line with the forward P/E multiples of that of its locally-listed peers. Overall, SGX-listed agricultural companies' P/E are trading within the range of 6x and 12x. In our upside case scenario, our target price implies a historical 11x P/E and forward 10x P/E, while our base case implies an 8-11x P/E.

Our DCF-derived target price's implied P/E multiple is in line with locally listed peers.

Figure 3: Peer comparison

Bloomberg Code	Company Name	Market Cap (local currency mn)	1M Return	3M Return	1Y Return	Price to Sales (Forward)	Price to Earnings (Forward)	EV/EBITDA	Gross Margin (%)	Operating Margin (%)	Net Margin (%)	ROE	ROA
DAG SP	DON AGRO INTERNATIONAL LTD	58.6	2.6%	1.3%	50.0%	1.4	6.0	4.3	47.2	31.3	28.1	21.5	15.5
Singapore													
WIL SP	WILMAR INTERNATIONAL LTD	28,815	1.3%	-14.0%	7.6%	0.4	13.4	12.4	11.1	4.4	3.0	8.6	3.1
OLAM SP	OLAM INTERNATIONAL LTD	4,717	-8.1%	-14.4%	11.1%	NA	NA	10.3	8.8	1.5	0.7	3.7	0.9
GGR SP	GOLDEN AGRI-RESOURCES LTD	2,729	-4.4%	0.0%	38.7%	0.3	7.2	5.9	16.2	4.3	0.4	0.7	0.4
FR SP	FIRST RESOURCES LTD	2,051	-0.8%	-12.8%	-7.1%	2.0	9.5	7.0	44.3	28.8	15.1	9.5	5.7
JAP SP	JAPFA LTD	1,668	-1.8%	-10.4%	42.5%	0.3	5.7	5.5	22.2	9.4	8.3	34.4	10.8
BAL SP	BUMITAMA AGRI LTD	780	-3.2%	-3.2%	-9.1%	0.8	8.8	6.2	27.8	21.6	12.4	13.2	6.3
IFAR SP	INDOFOOD AGRI RESOURCES LTD	447	-5.9%	4.9%	10.3%	NA	NA	7.2	20.2	11.4	0.1	0.2	0.1
US													
ADM US	ARCHER-DANIELS-MIDLAND CO	32,461	-5.7%	-1.3%	41.2%	0.4	12.8	13.6	6.9	2.6	2.8	10.4	4.1
MOS US	MOSAIC CO/THE	11,564	-2.0%	-7.9%	127.1%	1.0	9.0	8.4	12.3	4.8	7.7	11.4	5.3
BG US	BUNGE LTD	10,735	-4.9%	-8.9%	75.0%	0.2	9.6	8.3	6.7	3.4	2.8	42.5	10.0
China													
600598 CH	HEILONGJIANG AGRICULTURE-A	25,990	-5.6%	-4.9%	-22.8%	7.8	25.2	25.7	46.2	30.8	30.5	13.8	8.8
000998 CH	YUAN LONGPING HIGH-TECH AG-A	23,679	13.4%	4.2%	5.0%	6.2	66.3	48.8	38.6	6.8	3.5	2.3	0.9
601952 CH	JIANGSU PROVINCIAL AGRICULTU	14,524	-3.7%	3.0%	-12.2%	1.5	15.7	18.5	15.0	8.1	7.8	12.0	6.4
002041 CH	SHANDONG DENGHAI SEEDS CO-A	15,409	14.4%	12.3%	18.9%	NA	79.6	209.9	28.8	2.0	11.3	4.4	3.5
300087 CH	WINALL HI-TECH SEED CO LTD-A	13,108	28.6%	39.8%	96.5%	6.9	76.2	62.0	30.7	9.9	8.3	20.8	5.7
000713 CH	HEFEI FENGLE SEED CO LTD-A	5,772	4.6%	-0.9%	19.1%	NA	NA	58.2	14.5	3.1	2.1	2.5	1.6
Russia													
AGRO LI	ROS AGRO PLC- GDR REG S	1,956	6.4%	23.4%	51.5%	0.8	6.9	6.4	26.5	14.4	14.8	20.9	9.4
Ukraine													
KER PW	KERNEL HOLDING SA	4,370	-8.6%	-0.4%	28.4%	0.2	3.4	3.9	11.8	8.2	2.9	24.8	10.7

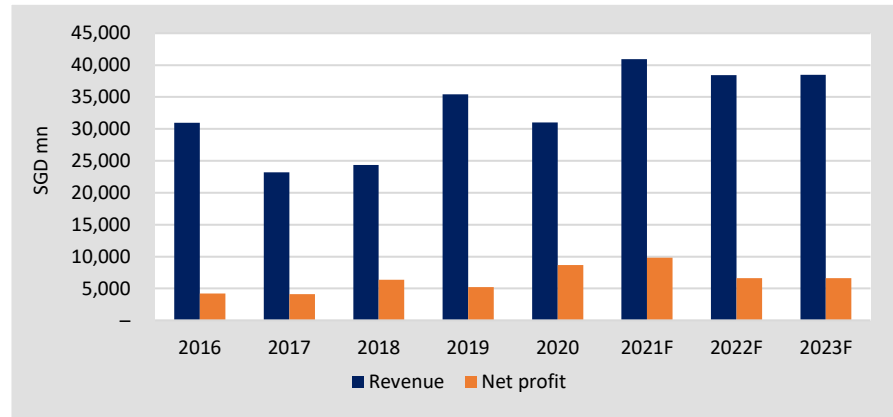
Source: Bloomberg, KGI Research

Forecasts and financial review

We forecast a bumper year in 2021 due to the contribution from Volgo-Agro (which helped increased total landbank by 19% to 63,240 hectares) and higher wheat prices. Wheat prices are the highest since 2014 (see our Industry Outlook section), and we expect prices to remain resilient given the favourable supply-demand dynamics.

We forecast 2021 to be a bumper year due to strong commodity demand.

Figure 4: Revenue and net profit forecasts

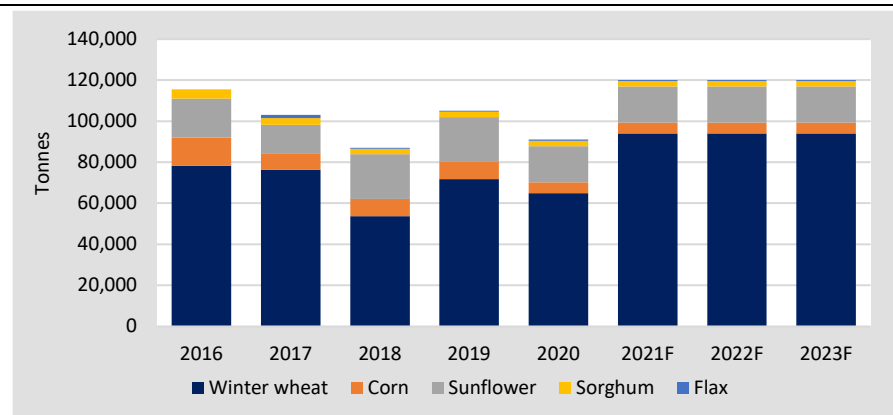


Source: Company data, KGI Research

Segment	Description	KGI Estimates for 2021-2023
Crops	Production and sale of agricultural produce in the Russian Federation, mainly winter wheat, sunflower and corn	S\$30-37mn in annual revenue, based on an increase of 7,000 hectares of arable land per annum
Livestock	Breeding of dairy cows for milk production and sale of livestock	S\$10mn in annual revenue based on its current herd size of 4,245 cows

Product mix is expected to remain similar to 2020's production volumes. In 2020, it produced 64,923 tonnes of wheat, 5,291 tonnes of corn and 17,638 tonnes of sunflower. The acquisition of Volgo-Agro will contribute mainly to wheat production. While Don Agro produces other crops like sorghum and flax, these are in minimal volumes and will not impact our valuation of the group.

Figure 5: Crop production mix forecasts



Source: Company data, KGI Research

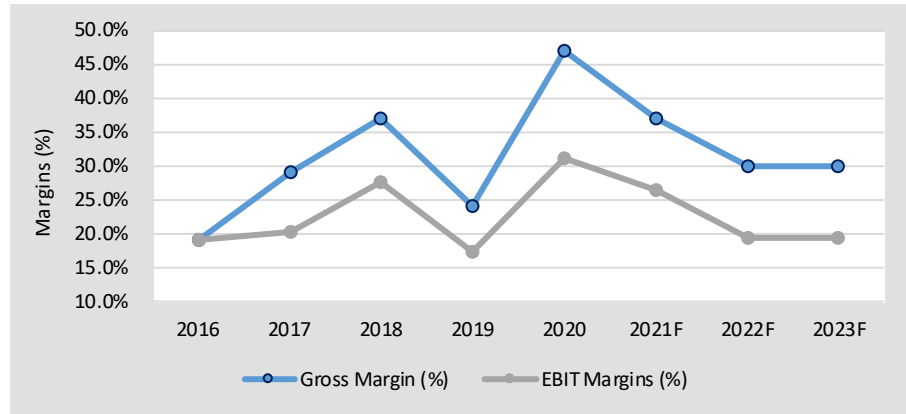
Dairy production is expected to remain at around 16,000 tonnes per year, based on a dairy herd size of 4,254 heads, which includes 2,188 milking cows. In 2020, milk yield per cow improved from 19.5 litres/day to 20.1 litres/day. While the Russian government provides incentives to improve milk yield, the room for improvement is minimal and we expect stable revenue of approximately S\$10mn per year from this business segment.

Margins are expected to normalise going into 2022 due to rising feed costs.

We forecast normalised gross margin of 30% and EBIT margin of 20%.

We expect a moderation of margins going forward following a strong 2020 performance, given that costs are expected to increase. Fertilisers, pesticides, and other chemicals typically account for 8-19% of the group’s cost of sales. Our normalised gross profit and EBIT margin assumptions are 30% and 20%, respectively.

Figure 6: Gross profit and EBIT Margins



Source: Company data, KGI Research

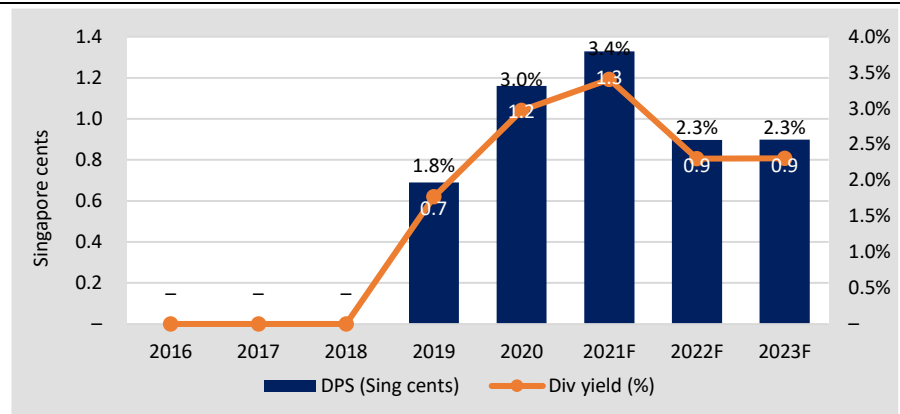
Don Agro paid out a 1.16 Sing cents dividend for 2020, an increase from 0.69 Sing cents in 2019. While the group does not have a fixed dividend policy, the board has stated its intentions to distribute dividends of up to 20% of net profit after tax attributable to shareholders. This is a prudent strategy, in our view, as the group is currently in the growth phase and will need cash to grow via acquisitions.

We expect a dividend yield of 2-3% based on a 20% payout ratio.

As the company is still in the growth stage, we are of the view that it should allocate more capital for expansion.

We forecast a 1.30 Sing cent dividend for 2021 based on a 20% payout ratio. Thereafter, we expect dividends to normalise at around 0.9 Sing cents for 2022-2023. The decline from 2021 should not be taken negatively, mainly because this year is expected to be an exceptional year due to the strong commodity boom driven primarily by pent-up demand and the disruption to global supply chains.

Figure 7: Dividend forecasts



Source: Company data, KGI Research



Macro and Industry Outlook

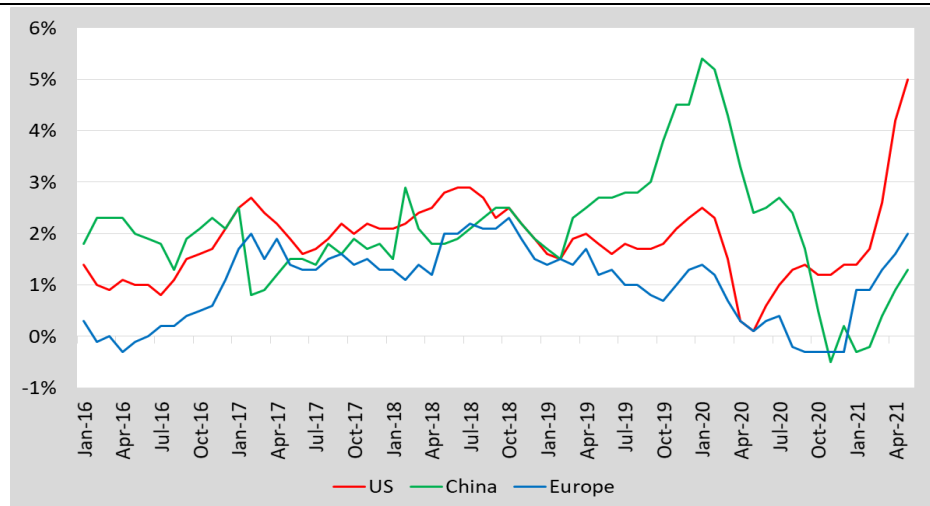
Global economic growth boosted by fiscal and monetary policies

The COVID-19 pandemic drastically disrupted economic and production orders in 2020. Lockdown and quarantine measures slowed down or even suspended economic activities to various extent across countries. Global central banks had to release unprecedented liquidity to bail out frozen or semi-frozen economies during the height of the COVID-19 outbreak: US M2 supply up 32% to US\$20.3tn, EU M2 supply up 12.9% to EUR14tn, China M2 supply up 12.9% to RMB227tn. However, the recovery of economic activities, including traffic, production, and global or regional trade has been outpaced by loose monetary supply as normalisation of businesses have not fully recovered given the uneven rate of global vaccination efforts.

The confluence of accommodative monetary and fiscal policy, as well as the stronger-than-expected global economic recovery, is driving commodity prices to multi-year highs.

Inflation has surfaced since 4Q20. The US recently reported a significant jump in inflation with May's CPI of 5%, the highest since the 2008 global financial crisis. Europe and China's inflation numbers remained moderate but have started to trend upward. Rising inflation is a commingled reflection of rising prices in energy, materials, food, drinks, and other components. However, we must note that the main drivers are the synergies between accommodative monetary policies and supply-demand imbalance.

Figure 8: CPI in major economies has surged



Source: Bloomberg, KGI Research

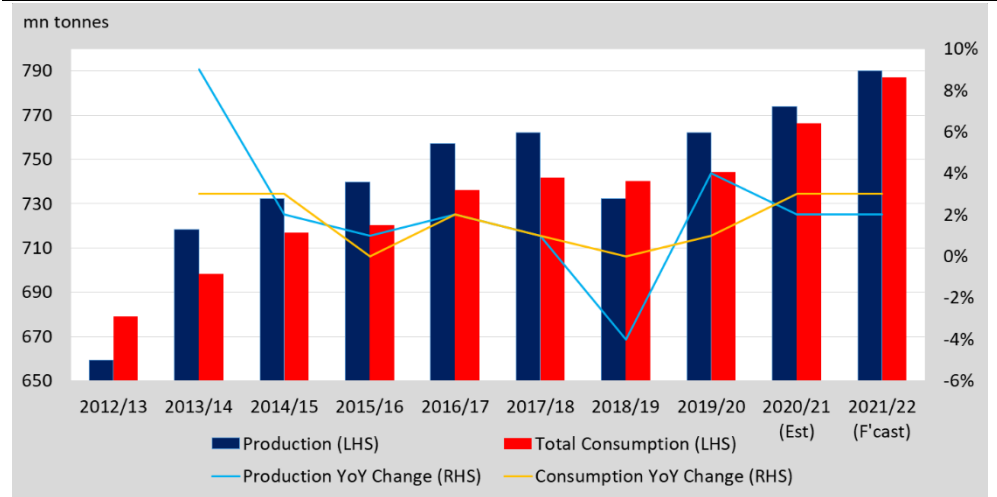
A focus on wheat and milk, Don Agro's bread and butter

The inflation-driven commodity upward cycle is being displayed in hard commodities such as basic metals, precious metals, and energy products and soft commodities such as various raw agricultural products. Here we mainly focus on wheat and milk as these are the main products of Don Agro.

The International Grains Council is upbeat on the global wheat outlook this year and next.

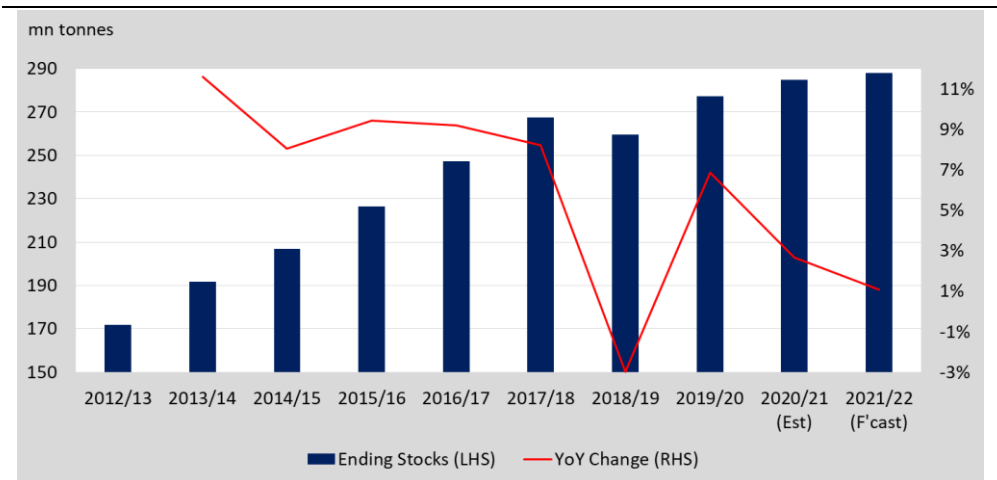
Over the last decade, the global wheat market has been growing healthily as both production and consumption grew moderately at an average of 2%. In 2018/19, the exceptional drop in supply and demand was due mainly to adverse weather conditions. Accordingly, wheat inventory was built back but then decreased as that was the only year when demand outnumbered supply. Moving forward, the International Grains Council (IGC) is upbeat on the global wheat outlook for 2021 and 2022. The respective growth of global production and consumption are expected to be 2% and 3%, and there is no shortage of supply expected in the next 18 months.

Figure 9: Growing global wheat production and consumption



Source: IGC, KGI Research

Figure 10: Growing global wheat ending stocks



Source: IGC, KGI Research

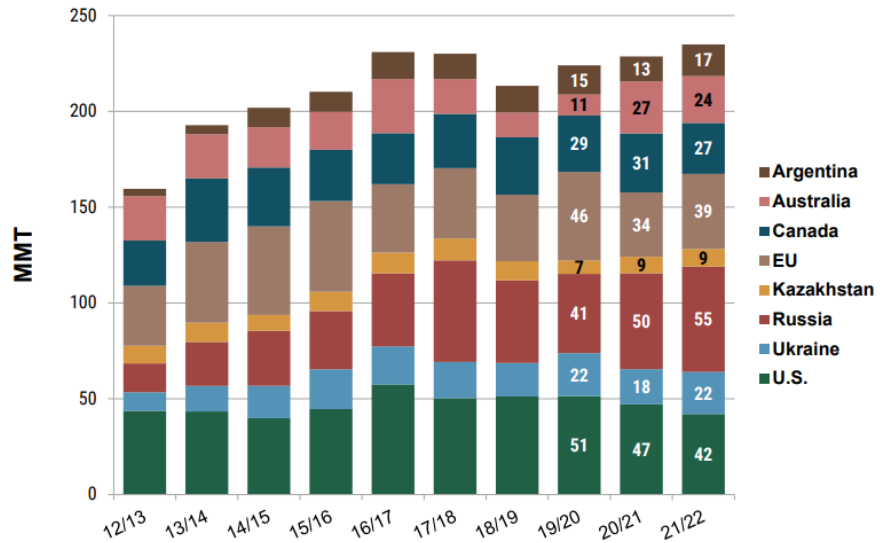
Russia plays an essential role in the global wheat market. According to the US Wheat Associates, Russia will resume being the largest global wheat exporter this year and next. The exportable wheat supplies in Russia is estimated to grow by 22.0% YoY to 50mn MT in 2020/21 and by 10% YoY to 55mn MT in 2021/22, which will help the country gain market share from the EU and the US.

In February 2021, the Russian government enacted several policies on agricultural products trades, including a new export quota of 17.5mn tonnes for wheat, barley, corn, and rye for the period February 15 to June 30. Meanwhile, an export tax of EUR50/tonne was imposed on March 1, which accelerated foreign procurement in February.

Recently, a floating export tax based on benchmark factors (70% of the difference between the export price and US\$200 per tonne) replaced the fixed export tax of EUR50/tonne. The floating tax rate was EUR23.5/tonne and EUR24.3/tonne on the first and second week in June.

While the Russian government has raised export duties in early 2021, we expect this to be a temporary measure to help bring down local prices for agricultural products.

Figure 11: Exportable wheat supplies by exporting countries (MMT: mn metric tonnes)



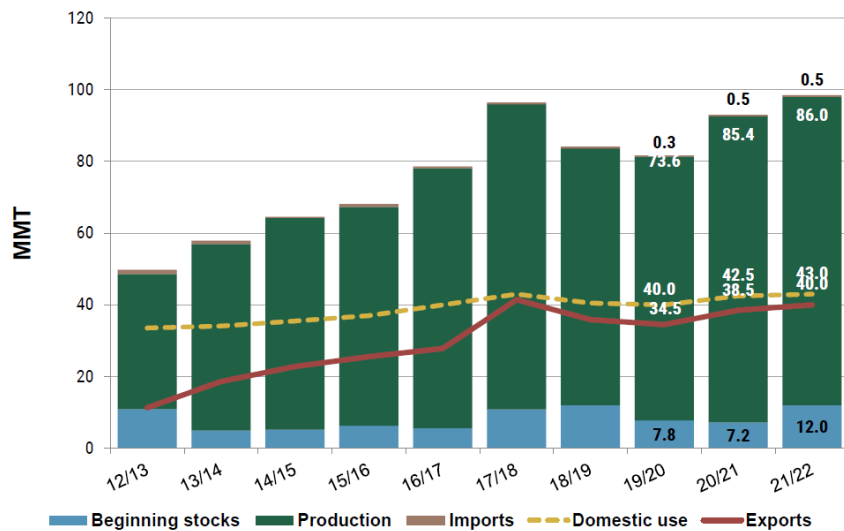
MMT: million metric tonnes

*Exportable Supplies = (Beginning Stocks + Production) – Domestic Consumption

Source: US Wheat Associates

Overall, Russian production is estimated to grow by 16% YoY in 2020/21 and by 0.7% YoY in 2021/22, and the total forecasted 86mn MT of volume next year will make a new wheat production record. As domestic consumption and export growths are expected to be 1.1% YoY and 3.9% YoY respectively in 2021/22, incremental wheat production is mainly for exports.

Figure 12: Russia wheat market situation



MMT: million metric tonnes

Source: US Wheat Associates

Wheat prices are the highest since 3Q 2014. A softer dollar will provide some support to wheat prices next year.

Wheat, as one of the major soft commodities, also rode on the upward cycle. The IGC wheat index shows that the upcycle of wheat started in 3Q20. The current price is back to the level in 3Q14. The restoration of supply and demand balance in 2021/22 will ease the upward price pressure. However, accommodative monetary supply is expected to remain, weakening the purchasing power of fiat money. To be more specific, the soft outlook for the US dollar is expected to provide some support to wheat prices next year. In a nutshell, we expect wheat prices to hover around the current levels in the next couple of quarters.

Figure 13: IGC Grain and Oilseeds Sub Index - Wheat

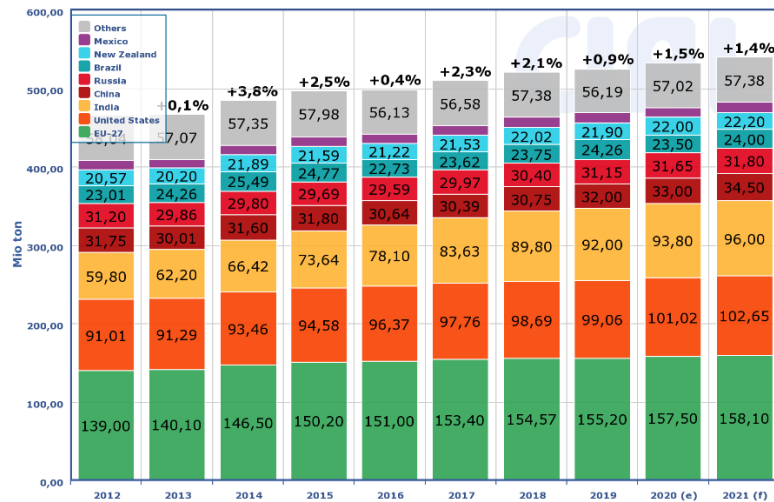


Source: IGC, KGI Research

The global dairy market is expected to grow steadily alongside world population growth.

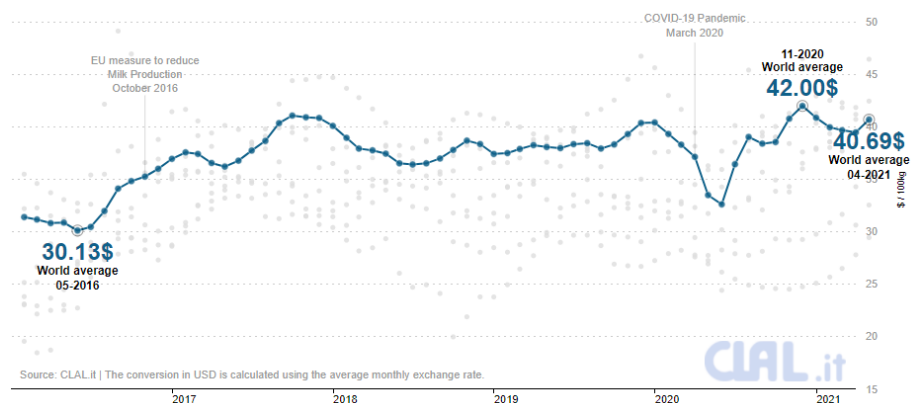
The dairy market is a steadily growing market in line with the world population growth, which is around 1% p.a.. According to the US Department of Agriculture, the global cow milk production is forecasted to be 540mn tonnes with a YoY growth of 1.4%. The supply and demand dynamics are stable in the past. However, driven by more costly feed to cattle, milk prices went up during the pandemic period. At the moment, the world average milk prices have remained elevated but are within a flattish range.

Figure 14: World cow milk production



Source: CLAL

Figure 15: World average milk price



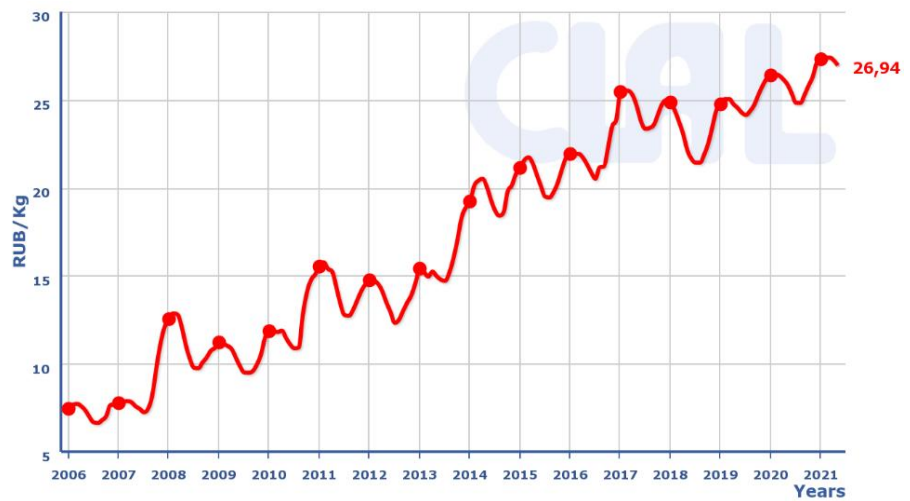
Source: CLAL

Russia's dairy outlook may look challenging in the short-term but will eventually stabilise given a longer time horizon.

Russia accounts for less than 6% of the world's cow milk production. Its estimated milk production in 2021 is 31.8mn tonnes, and domestic consumption is 7.1mn tonnes. The extra supply is for the manufacture of dairy products and exports.

The dairy sector outlook in Russia is less promising compared to other agricultural products as it has signs of oversupply and lower profit margins. The increasing production costs due to the growth of feed prices and depreciation of the Russian ruble (RUB) has led to a deterioration of the financial conditions in the sector. According to the draft Federal Budget, RUB257.5bn (US\$3.4bn) have been allocated for the state program of Agricultural Development in 2021, and the amount is RUB33.7bn (US\$455mn) less than the previous version of the budget. It is possible some subsidies to the dairy sector will be cut and allocated to other agricultural subsectors which have higher growth potential.

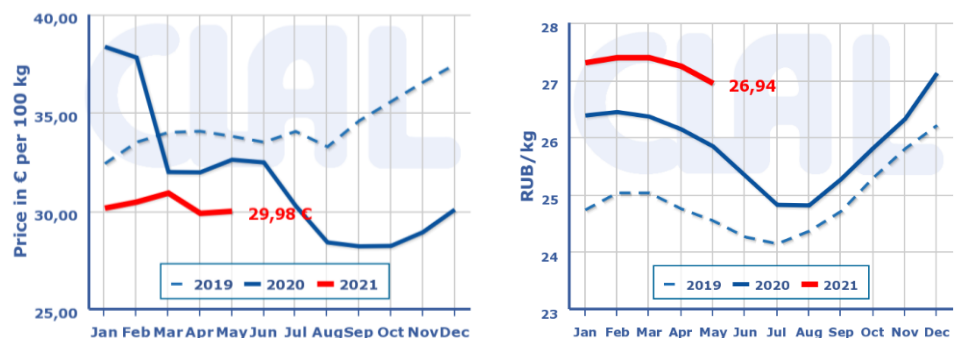
Figure 16: Domestic cow milk price in Russia



Source: CLAL

While the farm gate milk price in Russia has increased in 2021, it has declined in terms of euro, as shown in the graph below.

Figure 17: Impact on milk price from a devaluation of the RUB. Left graph shows milk prices in euro, while right graph shows milk prices in RUB.

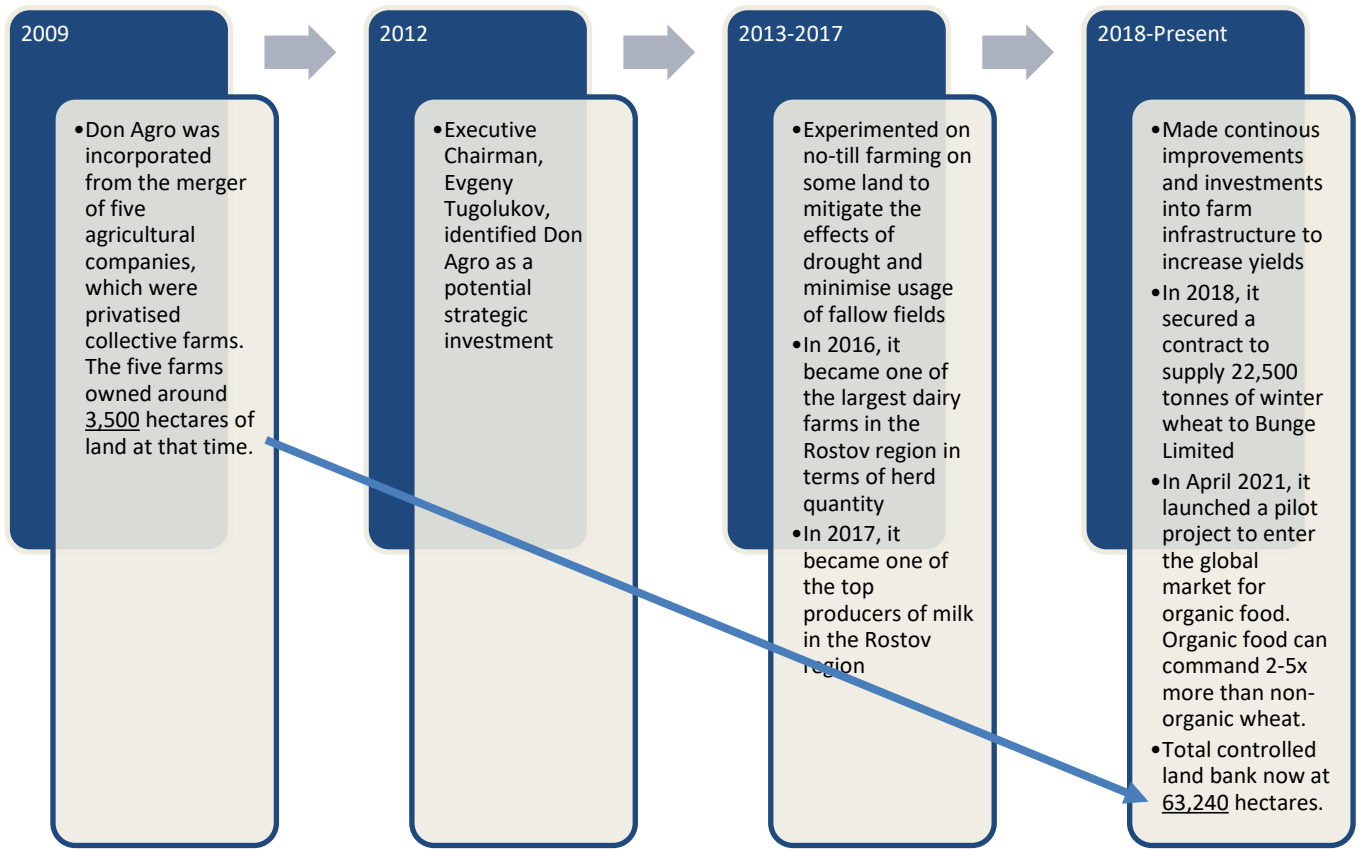


Source: CLAL

Company Background

A decade of experience

Figure 18: Growth of Don Agro



Source: Company, KGI Research

Big is better

Don Agro is one of the largest agricultural companies in the Rostov region in Russia. The region is one of the most fertile regions in Russia, located around 220km away from the Azov Sea and Don River international ports. Its customers are mainly traders and exporters and are thus able to save on transportation costs due to the proximity to these key transport facilities. The group's strategy to achieve economies of scale is twofold:

- Expand its arable land bank through acquisitions
- Invest in new equipment and machinery to improve yield

Minimal risk from customers who are international and local grain traders

Don Agro sells its agricultural produce primarily to international (Bunge, Glencore, Cargill) and local grain traders (Aston, Efcu, Yug Rusi) and exporters on an invited tender basis. There is minimal risk of clients defaulting as after tender, most of Don Agro's customers typically pay a deposit of no less than 50% of the contract sum depending on the customer's risk profile. Following the payment of the deposit, the customer will take delivery of half of the purchased amount, and the remaining half will be delivered after the receipt of the remaining purchase price from the customer.

Management team

Evgeny Tugolukov - Executive Chairman

- Evgeny Tugolukov was appointed to Don Agro's Board on 28 November 2018 and is responsible for setting and executing the strategic directions and expansion plans for the growth and development of the Group. He has over 20 years of experience holding top management positions in various financial and industrial groups.
- Evgeny Tugolukov began his career in 1993 when he joined MDM Bank, one of the largest private banks in Russia, before going on to build up and manage several sizeable holdings.
- In 2005, he formed EMAlliance Public JSC ("EMAlliance") where he served as chairman of the board of directors until 2007, developing it into one of Russia's largest power machine-building companies. In 2008, he founded Strongbow Investments Pte Ltd (Strongbow), a Singapore-incorporated international holding company with a diverse range of investments in the areas of high-tech start-ups, entertainment, healthcare, real estate development and agriculture, and a strong geographical focus on Southeast Asia, Russia and Eastern Europe. He has been the managing director of Strongbow since 2012.
- From 2007 to 2011, Evgeny Tugolukov was a Member of Parliament of the State Duma of the Russian Federation, as well as the Chairman of the State Duma Committee on Natural Resources. He has also been an honorary business representative with Enterprise Singapore, promoting bilateral trade and business relations between Singapore and Russia from 2014 to 2018.
- Evgeny Tugolukov graduated with a Diploma in Economics and Management from the Ural Federal University in 2000.

Marat Devlet-Kildeev - Chief Executive Officer

- Marat Devlet-Kildeev is responsible for directing and controlling the operations of the Group and its key operational subsidiaries.
- Marat Devlet-Kildeev has been with the Group since 2012, when he was the chairman of the board of Don Agro JSC and Don Agro LLC. He became the general director of Don Agro LLC in 2014. He became the President of Don Agro LLC in 2017 where he was responsible for developing relationships with potential investors and foreign partners as well as evaluating foreign capital markets. He took on the same role in Tetra JSC in 2018 and was appointed to Don Agro's Board on 28 November 2018.
- Marat Devlet-Kildeev joined Barclays Bank of Canada in 1993 (which was subsequently acquired by Hong Kong Bank of Canada in 1995) where he was deputy treasury manager and head of leasing. He then joined Renaissance Capital Limited in 1998 as head of risk management and then became chief financial officer for the company, before becoming the first deputy general director of the Renaissance Insurance Group LLC in 1999. He then joined a media company, Afisha Industries CJSC, as general director in 2001 before joining an investment holding company, Rinaco JSC, as managing director in 2003.
- He subsequently joined a Rinaco JSC-managed engineering company, TKZ-Management LLC, as general director in 2005, and EMAlliance as first deputy general director in 2005. In 2006, he became the chief operating officer of power and energy-focussed, ESN JSC. He then worked for an Aegis Media Russia-related media company, O.K. Solutions LLC, as general director in 2007 to 2008, before joining the Moscow representative office of CTC-Media. Inc. as deputy general director and head of international broadcasting in 2009 until 2012. In 2012, he joined ProdAlliance Limited, which was managing the business of our Group, as head of representative office until 2018.
- Marat Devlet-Kildeev graduated with a Diploma in Russian Linguistics and Teaching Russian for Foreigners from the Leningrad State University in 1987 and received his Master of Business Administration degree from the University of Toronto Faculty of Management in 1993.

Artur Nazaryan - Chief Financial Officer

- Artur Nazaryan is responsible for the finance, accounting and taxation matters and has also been the Financial Advisor to Don Agro LLC since 2014.
- Artur Nazaryan began his career in 2004 as an accountant in the receivables department of Zaslon LLC, where his responsibilities included controlling accounts receivables ledgers and preparing presentations for potential customers. He moved to CJSC KPMG's audit department in 2007 as auditor and audit supervisor, where he supervised audit and financial consulting engagements and prepared financial models and financial statements. In 2013, he joined Guardian Glass Rostov LLC, a float glass production company, as head of finance and was in charge of all manner of finance, including taxation, reporting, cash flow and working capital management and the development of management accounting systems. In 2014, he became the chief financial officer of ProdAlliance Limited until 2018.
- Artur Nazaryan graduated with Specialist Diploma in Organisation Management from the Southern Federal University in 2008. He has also been a member of the Association of Chartered Certified Accountants (ACCA) since 2015.

Vadim Novikov - Chief Operating Officer

- Vadim Novikov is responsible for overseeing the entire operations of the Group and has been the General Director of Tetra JSC and Don Agro LLC since 2012 and 2014, respectively.
- Vadim Novikov started his career in 2001 as a legal counsel at Law Firm JSC JurCon, a local Russian law firm specialising in advising corporate clients in the power and energy sectors. He moved to an investment company, JSC Rinaco, as a legal counsel in 2003, and provided legal support in corporate and share capital transactions. In 2005, he joined EMAlliance where he was legal counsel, head of corporate and deputy head of tax and legal. Thereafter, Vadim Novikov joined ProdAlliance Limited in 2013 as legal counsel providing legal support for its investment activities until 2018.
- Vadim Novikov obtained his Diploma with Honours in Law from the Ural State Law University (formerly known as Ural State Law Academy) in 2001.

Key Risks

Unfavourable weather conditions can reduce both crop yield and quality

Production of crops is vulnerable to extreme weather conditions such as windstorms, hailstorms, droughts, and temperature extremes, as well as natural disasters. Natural disasters or adverse conditions may occur in Russia, including severe weather, such as excessive rainfall and drought as well as power outages or other events.

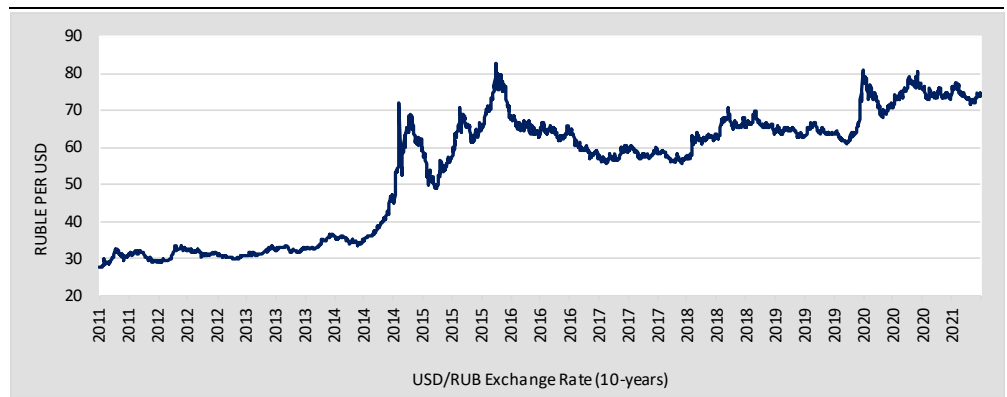
In the longer term, the impact of climate change could lead to a shift in global weather patterns, and cause droughts in Russia's southern agricultural regions which includes Stavropol and Rostov. In 2020, many areas of Russia experienced the hottest temperatures on record, contributing to forest fires.

Forex volatility

Don Agro's functional currency is in RUB, as well as the majority of its revenue and costs. The sales of agricultural products to customers are in USD while costs are in RUB, which will likely help offset depreciation of the RUB against SGD when it pays out dividend distribution to investors in Singapore.

However, we note that the volatility in the RUB can impact the company's assets and liabilities, which are reported in SGD. The RUB has depreciated around 11% against the USD over the past 5 years, with a trading range of more than 40% within the 5-year peak to trough levels. The last significant devaluation of the RUB was in 2014 when it declined more than 100% vs the USD due to the fall in oil prices and economic sanctions imposed by the US and the EU.

Figure 19: USD/RUB



Source: Bloomberg, KGI Research

International sanctions

No individual entity or individual within Don Agro has been designated by the US, the EU or any other country as a specific target of any sanctions. However, as the group operates entirely in Russia, its customer and suppliers may be subjected to various trade and economic sanctions as part of international sanctions against Russia.

The group's principal bankers, RSHB and Sberbank, are state-owned banks and are included in certain economic and diplomatic sanctions imposed by the US, the EU, Australia and Ukraine. However, the existing sanctions on the group's customers, suppliers and banks have not affected Don Agro's business, results of operations and financial condition.

Financial Summary

FYE 31 December					
	2019	2020	2021F	2022F	2023F
INCOME STATEMENT (SGD'000)					
Revenues	35,431	30,996	40,914	42,824	47,295
Cost of sales	(33,354)	(25,587)	(31,776)	(35,977)	(39,107)
Gain from change in fair value of biological asse	6,512	9,217	6,000	6,000	6,000
Gross profit	8,589	14,626	15,138	12,847	14,189
Administrative expenses	(2,122)	(3,117)	(2,659)	(2,784)	(3,074)
Other operating expenses, net	(282)	(1,807)	(1,637)	(1,713)	(1,892)
Net finance costs	(659)	(691)	(515)	(515)	(515)
Profit before tax	(303)	(315)	(516)	(392)	(435)
Tax expense	(303)	(315)	(516)	(392)	(435)
Profit for the year	5,223	8,696	9,811	7,444	8,273
Non-controlling interests	14	–	–	–	–
PATMI	5,209	8,696	9,811	7,444	8,273
Earnings per share (Sing cents)	4.2	5.8	6.5	5.0	5.5
DPS (Sing cents)	0.7	1.2	1.3	1.0	1.1
BALANCE SHEET (SGD'000)					
Cash and cash equivalents	4,646	9,992	12,078	15,868	20,722
Inventories	6,555	9,879	12,075	13,671	14,860
Other current assets	13,677	14,876	15,794	15,985	16,433
Total current assets	24,878	34,747	39,947	45,524	52,015
Property, plant and equipment	11,890	12,770	13,488	14,076	14,360
Biological assets	9,989	7,807	7,807	7,807	7,807
Other non-current assets	4,610	5,306	5,306	5,306	5,306
Total non-current assets	26,489	25,883	26,601	27,189	27,473
Total assets	51,367	60,630	66,548	72,713	79,488
Trade and other payables	1,728	3,520	1,589	1,799	1,955
Loans and contract liabilities	4,679	6,085	6,085	6,085	6,085
Other current liabilities	1,700	1,699	1,699	1,699	1,699
Total current liabilities	8,107	11,304	9,373	9,583	9,739
Lease liabilities	4,425	4,530	4,530	4,530	4,530
Other non-current liabilities	1,346	1,397	1,397	1,397	1,397
Total non-current liabilities	5,771	5,927	5,927	5,927	5,927
Total liabilities	13,878	17,231	15,300	15,510	15,666
Unitholders' funds and reserves	37,489	43,399	51,248	57,203	63,821
Total liabilities and equity	51,367	60,630	66,548	72,713	79,488
CASH FLOW STATEMENT (SGD'000)					
Profit before tax	5,223	8,696	9,811	7,444	8,273
Adjustments	4,741	1,644	2,782	2,912	3,216
Operating cash flows before WC changes	9,964	10,340	12,593	10,356	11,489
Change in working capital	302	(4,086)	(5,045)	(1,577)	(1,480)
Income tax paid	(200)	(144)	(516)	(392)	(435)
Cash flows from operations	10,066	6,110	7,032	8,387	9,573
Capital expenditure	204	223	200	200	200
Acquisition of subsidiaries	(1,742)	(4,072)	(3,500)	(3,500)	(3,500)
Others	(2,317)	(2,190)	316	192	235
Cash flows from investing	(3,855)	(6,039)	(2,984)	(3,108)	(3,065)
Lease payments	(429)	(313)	–	–	–
Dividends paid	–	5,060	–	–	–
Interest paid	(601)	(990)	(1,962)	(1,489)	(1,655)
Other financing cashflow	(2,015)	2,469	–	–	–
Cash flows from financing	(3,045)	6,226	(1,962)	(1,489)	(1,655)
FX Effects, Others	–	–	–	–	–
Net increase in cash	3,166	6,297	2,086	3,790	4,854
Beginning Cash	1,263	4,646	9,992	12,078	15,868
Ending cash	4,646	9,992	12,078	15,868	20,722
KEY RATIOS					
DPS (SGD cents)	0.69	1.16	1.31	0.99	1.10
Dividend yield (%)	1.8	3.0	3.3	2.5	2.8
NAV per share (SGD cents)	30.0	28.9	34.1	38.0	42.4
Price/NAV (x)	1.3	1.4	1.1	1.0	0.9
Profitability					
EBITDA Margin (%)	23.9	38.2	33.3	26.3	26.3
Net Margin (%)	14.7	28.1	24.0	17.4	17.5
ROE (ex. Property FV gain) (%)	11.6	15.5	15.4	10.7	10.9
ROA (ex. Property FV gain) (%)	15.6	21.5	20.7	13.7	13.7
Financial Structure					
Interest Coverage Ratio (x)	6.8	12.4	15.2	11.7	12.9
Net Gearing Ratio (%)	(5.7)	(16.4)	(17.9)	(22.7)	(27.9)

Appendix A: Type of crops and seasonality

Type of crops

Type of crops	Description
Winter wheat	Winter wheat is a strain of wheat that is planted in the autumn to germinate and develop into young plants that remain in the vegetative phase during the winter and resume growth in early spring. Winter wheat is mainly used in food and animal fodder production and has a high yield potential.
Sunflower	Sunflower is generally used as a raw material in the production of sunflower oil, which sees a high demand in the food industry.
Corn	Corn is an annual cereal grass plant that has several uses. It is used as livestock feed, biofuel, staple food and raw materials. Corn is a major food globally that is widely used. There are various commercial classifications for corn based mainly on the texture of the kernel. Some classifications are dent corn, flour corn, sweet corn, flint corn and popcorn. Corn is also harvested as fodder for our dairy operations.
Sorghum	Sorghum is a cereal grain plant that is also known as milo. There are several varieties of sorghum and different variety has their own use. For example, grain sorghums are used for food, grass sorghums are used for hay and fodder and broomcorn are used to make brooms and brushes. The sorghum grain is gluten-free and can be used as a substitute of wheat.
Flax	Flax is an annual herbaceous plant that is adaptable to a variety of soil. It is cultivated for its fibre and seeds. The fibre of the plant can be made into linen yarn and fabric. The seed is regarded as a health food globally due to its high dietary fibre and omega-3 fatty acid content. The seed can be used directly for human consumption or be processed into cooking oil.

Seasonality

Don Agro's business is highly seasonal as a substantial portion of revenue is generated by crop production and the crop production cycle varies between the type of crops.

The group currently focuses on the production of winter wheat and sunflower, which are generally harvested in July and from September to October, respectively. Due to the seasonal nature of agricultural activity, Don Agro typically generates significantly higher revenue in the second half of its financial year when harvested crops are typically sold.

The group aims to sell crops when prices are at their peak. If prices are not favourable following a harvest, it may store a particular crop and sell it when prices are more favourable, which may be as late as the following year. Accordingly, this may result in variations to financial results on a quarterly basis from year to year.

The dairy business is generally not subject to any seasonal factors as the group is able to produce raw milk throughout the year. However, milk production tends to be higher during the winter season, which is from November to February, as (1) milking cows tend to produce less milk when temperatures are higher especially during the summer months; and (2) the current production cycles of most of the group's dairy herd is in the second half of the calendar year.

	Tillage / Spraying	Sowing	Plant cultivation	Harvesting
Winter wheat	August	September	September to June	July
Sunflower	October / May to June	April to May	April to May	September to October
Sorghum	October / May to June	April to May	April to May	September to October
Corn	October / May to June	May	May	September to October
Flax	October	April to May	April to May	August

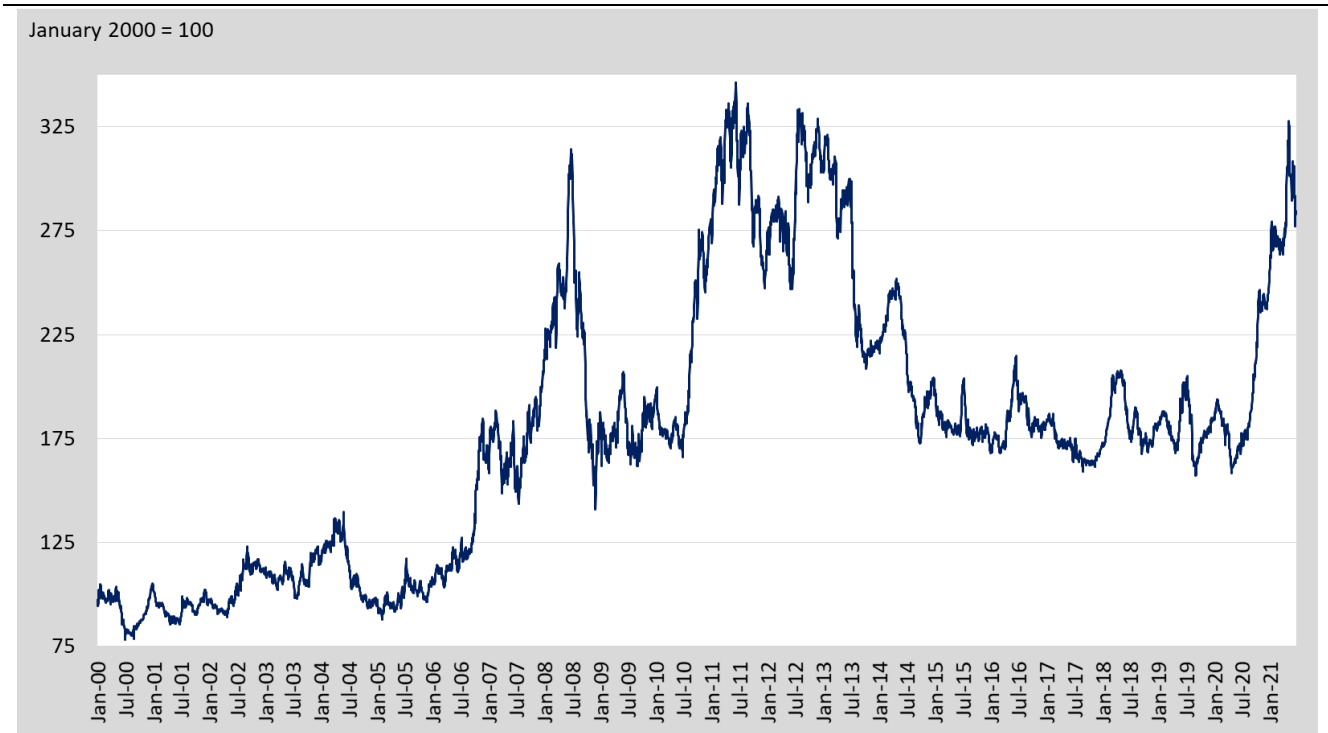
Appendix B: Long-term Agricultural price trends

Figure 20: IGC Wheat Index



Source: IGC, KGI Research

Figure 21: IGC Maize Index



Source: IGC, KGI Research

KGI's Ratings

Rating	Definition
Outperform (OP)	We take a positive view on the stock. The stock is expected to outperform the expected total return of the KGI coverage universe in the related market over a 12-month investment horizon.
Neutral (N)	We take a neutral view on the stock. The stock is expected to perform in line with the expected total return of the KGI coverage universe in the related market over a 12-month investment horizon.
Underperform (U)	We take a negative view on the stock. The stock is expected to underperform the expected total return of the KGI coverage universe in the related market over a 12-month investment horizon.
Not Rated (NR)	The stock is not rated by KGI Securities.
Restricted (R)	KGI policy and/or applicable law regulations preclude certain types of communications, including an investment recommendation, during the course of KGI's engagement in an investment banking transaction and in certain other circumstances.

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