



Recommendation:

**BUY and HOLD**

Rating at a Target Price\* of

**MNT 33,762**

Upside:

111.41%

*August 4, 2021*
**TCK.MSE Overview**

Ticker:	TCK
Industry:	Food manufacturing
Last close:	MNT 15,970
Target Price:	MNT 33,762
Market Cap:	MNT 14.0 billion
Shares Out:	1,023,703
52-week High:	18,000
52-week Low:	12,040

\*Target price has been estimated to be reached within 5 years from the time of current share price valuation.

Figure 1. Stock Price history


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**INTRODUCTION**

Talkh Chikher JSC (or the “Company”) is one of the largest flour product producers in Mongolia and has been operating for 37 years now. The Company is currently under Classification 1 on Mongolian Stock Exchange (MSE) and is a leading food manufacturing company that possess a dominant share of the bread and bakery market in Mongolia. The Company’s current operations include the production of bread, pastries, candies, biscuits and cake and distribution to retail and wholesale markets across Mongolia.

**INVESTMENT OVERVIEW**

**LEADING PLAYER IN THE DOMESTIC MARKET:** Talkh Chikher is a consumer staple product manufacturer and has maintained consistent sales during the pandemic despite the economic downfall, globally. In 2020, Mongolia's GDP fell by 5.3%, while the Company's revenue grew by 15%. Talkh Chikher is a key player in the industry that only has a few major competitors in the industry where there has a low risk of new entrants.

**TALKH CHIKHER IS ONE OF THE TOP 100 COMPANIES IN MONGOLIA:** On June 28, 2021, the Government of Mongolia (GoM) and the Mongolian National Chamber of Commerce and Industry (MNCCI) announced the top 100 companies in Mongolia, and Talkh Chikher has been selected as one of them for seven consecutive years. The list was based on five criteria: revenue, amount of tax paid, number of employees paying social security contributions, net profit, and total assets. This highlights that Talkh Chikher is one of the highest performing businesses in Mongolia.

Table 1. Key Historical Financials

MNT (Million)	2017A	2018A	2019A	2020A
<b>Income Statement</b>				
Revenue	36,427	46,604	54,856	63,054
COGS	27,286	35,550	40,886	47,695
Sales and marketing expense	313	538	438	348
General and admin expense	6,317	3,939	5,424	6,125
Net profit	1,128	1,976	2,456	3,036
<b>Balance Sheet</b>				
Current assets	11,931	9,937	17,497	18,363
Total assets	54,158	58,257	70,354	73,009
Current liabilities	5,046	9,236	10,361	13,169
Total liabilities	9,090	11,214	20,855	20,474
Shareholder’s equity	45,067	47,043	49,499	52,535
<b>Ratios</b>				
Revenue growth	12%	28%	18%	15%
Gross margin	25%	24%	25%	24%
ROE	3%	4%	5%	6%
Current ratio	2.36	1.08	1.69	1.39
Net profit margin	3%	4%	4%	5%
EPS	1'101	1'930	2'399	2'965
Dividend Payout ratio	15.4%	10.4%	9.4%	7.6%
P/E ratio	23.6	9.8	5.5	4.8

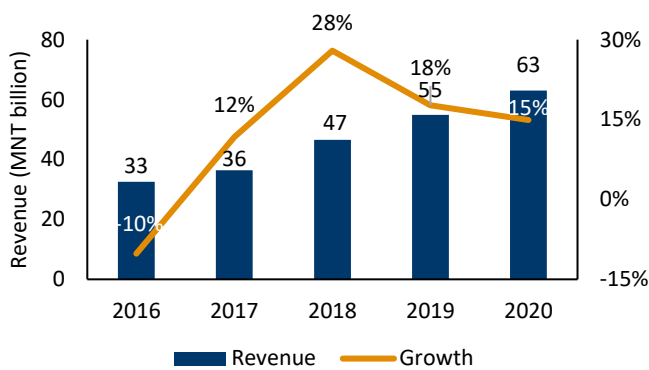
Source: Talkh Chikher Annual report, MICC estimates, MSE

## BUSINESS DESCRIPTION

**OVERVIEW:** Talkh Chikher JSC was established in 1984 and has been operating for over 3 decades now. The Company was one of the few that continued its businesses during the transition to the free market in the 1990s, where Mongolia’s major factories closed their doors. The Company operates through overall 21 Tachi bakery branches in Ulaanbaatar, Darkhan and Erdenet, and supply its products to over 3000 distribution channels in Ulaanbaatar. Distribution points include wholesale markets i.e., kiosks to large food markets such as hypermarkets. The Company first started its operation with one product line i.e., bread with a capacity of up to 90 tons per year, according to the Company report. As a result of the Company’s aim to produce products that align with customer preference and demand, Talkh Chikher increased its capacity and product options since its operation. Currently, the Company is capable of producing 131 types of products e.g., cake, candy, biscuit, bread, pastry, festive cake etc.

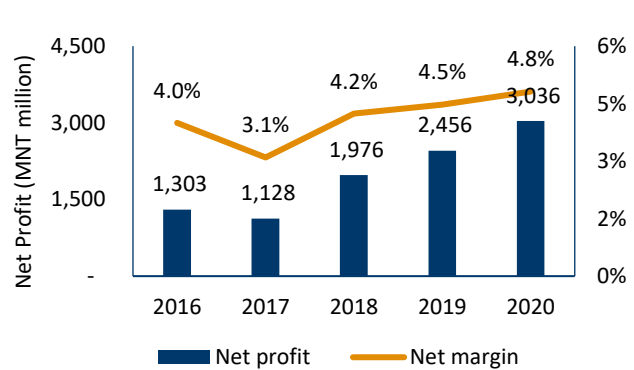
According to the financial statements of Talkh Chikher, the Company invested a total of MNT 24 billion on capital expenditure in the last 3 years, which may indicate Talkh Chikher is expanding its operation or replacing the obsolete equipment that had been in use for over a decade. In 2008, the Company’s market share price was MNT 920, and the value has been increasing gradually over the past decade, of which in 2021 the share price has risen to MNT 15,970. In 2019 and 2020, despite the restrictions put on businesses by the Government of Mongolia to fight against the Covid-19 spread, Talkh Chikher has managed to increase its revenue. Talkh Chikher’s revenue has reached MNT 63 billion with a net income of MNT 3 billion, showing an increase of 15% and 23%, respectively in 2020.

Figure 2. Talkh Chikher Sales Revenue (MNT billion)



Source: Talkh Chikher Annual report

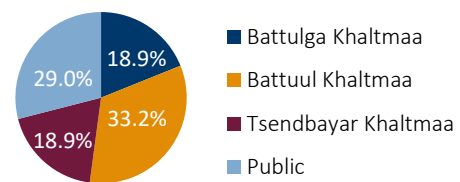
Figure 3. Talkh Chikher profitability (MNT million)



Source: Talkh Chikher Annual report

**Ownership Structure:** In 1991, under the decision of the Government of Mongolia, 30% of the Company was owned by the state which later became 100% private in 1999. Currently, the Company’s major shareholders include Battulga Khaltmaa /18.91%/, Battuul Khaltmaa /33.21%/ and Tsendbayar Khaltmaa /18.88%/, who own over 70% of the Company.

Figure 4. Talkh Chikher ownership structure



Source: MSE

**PRODUCTS AND SERVICES:** Talkh Chikher JSC employs highly qualified personnel who conduct regular inspections at each stage of production from receiving raw materials to delivering finished products to customers. Currently, the Company manufactures more than 27 types of bread, 28 types of pastries, 26 types of cakes, 9 types of biscuits, 4 types of festive cakes and 3 types of candies. Other products include 34 products under Tachi bakery brand including cupcake, muffin, pie, roll and layered cake etc. As consumer preference is leaning towards healthy, low sugar, whole-grain and gluten-free bread types, Talkh Chikher has introduced “Ontsgoi” brand which includes 4 types of bread and 1 pastry that contains healthy raw ingredients such as whole wheat, bran and coriander. In 2020, the Company started producing burger bread under the brand “Khaan” with Makh Impex, leading meat products producing company in Mongolia.

## ENVIRONMENTAL, SOCIAL & GOVERNANCE (ESG)

**ENVIRONMENTAL:** Talkh Chikher JSC has been operating in an environmentally friendly manner since its establishment. The Company has continuously supported the new laws and regulations that intend to protect the environment through its business activities. For example, the Company implemented the “Smart Consumer” program where customers were able to receive a cotton tote bag in exchange for 20 product packages in 2019. Through this program not only did the company provide tote bags to 10,000 customers and contribute their piece to protecting the environment, but they also showed themselves as strong supporters of the recent law concerning trash and waste which was passed on March 1st, 2019. We anticipate that the Company will continue to pursue environmentally friendly campaigns in line with its reputation and status.

**SOCIAL:** Talkh Chikher JSC puts great emphasis on community relations, human rights, and gender equality. The male-to-female ratio of the Company is 46-54, and about 70% of all employees are under 40 years old. The recruitment process has a holistic approach that takes into account diversity, experience, and an individual's skills and abilities. The Company strives to maintain a very high level of employee satisfaction and pays special attention to their families. Assuming that there are 5 people behind one employee, keeping more than 4,000 people with income, satisfaction and security is a sign that the Company has fulfilled its social responsibility very well.

### GOVERNANCE:

**Governance Assessment:** The board of directors are the fundamental of a robust corporate governance framework in a way that it ensure the effective monitoring of management and enhances accountability of performance. Following this statement, the Company meets the standards set by the Mongolian Corporate Governance Code, which requires financial institutions and joint-stock companies to have independent directors that are no less than 1/3 of the total 9 board members. Per this standard, Talkh Chikher’s board has three independent directors out of nine. The gender diversity at the board is also an important pillar for organisations as research shows that it drives innovation when woman make up more than 30% of the board. For Talkh Chikher, the percentage is 44%, which indicates balanced approach in composition of the diversity.

**Board of Directors:** Board diversity guarantees effective decision making, better utilisation of the knowledge and expertise, enhances corporates reputation and investor relations. Talkh Chikher’s Board of Directors committee is comprised of various individuals with diverse experiences from different industries, such as machinery and equipment, hospitality and most importantly food industry. This ensures better control for Talkh Chikher to allocate management power, to ensure safety protocol of day-to-day food operation and to formulate long-term strategy of the Company.

Figure 5. Corporate Governance



Source: SP&E Consultants

Table 2. Board members 2021

List of Board Members
<b>Battuul</b> Khaltmaa
<b>Tsendbayer</b> Khaltmaa
<b>Tsenddorj</b> Dashdonoi
<b>Munkhtsetseg</b> Narantsetseg
<b>Francis</b> Lee Bun Kim
<b>Giimaa</b> Khashbat
<b>Damdinsuren</b> Luvsansuren
<b>Oyunmaa</b> Banzragch
<b>Bayarsaikhan</b> Dorjpurev

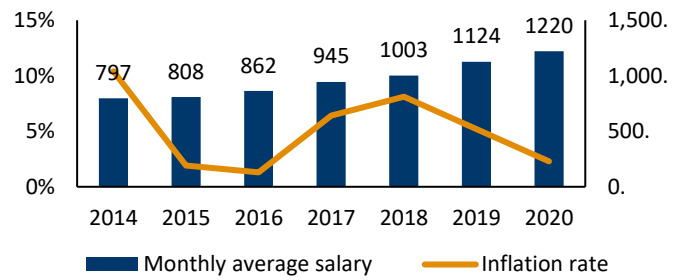
## INDUSTRY OVERVIEW & COMPETITIVE POSITIONING

**OVERVIEW:** Nationwide, a total of 8,500 food-producing entities are operating in Mongolia, of which 47% of them is in a rural area and 53% is in urban area. The food sector employs over 40,000 people<sup>1</sup>. According to the Ministry of Food and Agriculture in Mongolia /MOFA/, the sales of the food sector has increased by seven-fold during the last decade. Despite the gradual increase in food sales over the last 5 years, due to Covid-19 impacts in the first two half of 2020, the industry’s revenue has increased compared to the previous year. The consumer price index has risen by 2.3% from the last year mainly due to an increase in prices of food, alcoholic beverages, tobacco, medicine, and medical services. Average households with a monthly expenditure of less than MNT 500,000 has spent 32.4% of their cash on food items, 51.3% on items other than food and the remaining on other items including gifts and benefits<sup>2</sup>. Mongolian bread and pastry market is a oligopoly market, where a small number of suppliers make up majority of the sales.

**MACROECONOMIC ASPECT:** Mongolia’s GDP grew at CAGR of 10.9% throughout the past five years (2014-2019). However, the GDP growth rate has dropped to -5.3% in 2020 due to the global pandemic. According to the World Bank, the GDP growth rate will expect to rise back up to 5.9% in 2021E and 6.1% in 2022E. Economic growth will increase national household income, followed by a rise in household expenses on food purchases, which comprised 20% of total nationwide household expenses, influencing the raising flour market demands as well.

**DEMAND:** The production of baked products increased as the demand for them rose in recent years. The growing sales of baked products despite the pandemic ensued lockdowns, cut in income for workers, and business downfalls indicate the robustness of such products to economic instabilities. Therefore we predict that sales of baked products will continue growing consistently.

Figure 6. Salary and inflation rate (MNT thousand)



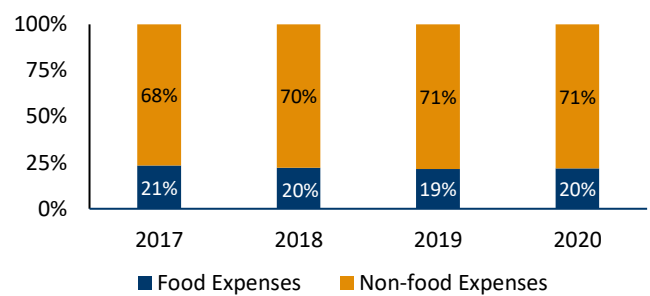
Source: NSO

Table 3. N concentration ratio (National Amount)

	Bread	Pastry
N=2	97%	50%
N=4	97%+	80%

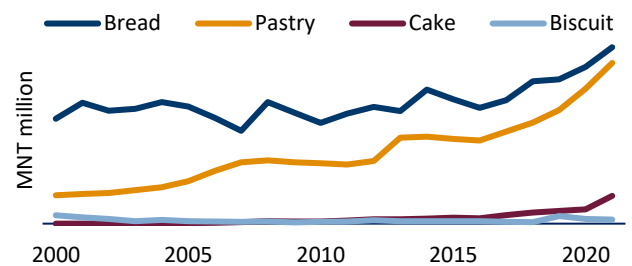
Source: Talkh Chikher Annual Report, MICC estimates

Figure 7. Monthly household expenses (National average)



Source: NSO

Figure 8. Production of bread and bakery products in Mongolia



Source: NSO

<sup>1</sup> Mongolian Ministry of Food and Agriculture

<sup>2</sup> NSO

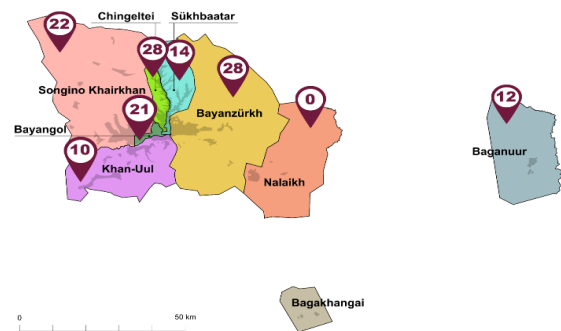
## BREAD AND BAKERY INDUSTRY

**OVERVIEW:** The term “bakery” has changed and evolved in the last 25 years, not just in Mongolia but throughout the world. Back in the 1990s, a bakery was seen as a traditional pastry-making business through shops or a wholesalers. However, now it can mean someone baking for markets from their home or a general food factory that supplies bread, pastry, and other baked goods to different sales points<sup>3</sup>. According to NSO, the bread and bakery industry in Mongolia produces around 55 tons of wheat products each year. Since the bakery industry is a very broad term, it can be divided into two categories, retail and wholesale, depending on the function of the business. While the market of wholesale bakeries is highly fragmented four producers Talkh-Chikher, Uguuj, Stimo, and Atar-Urguu account for around 80% of total commercial bakery revenue, according to Talkh Chikher operation report.

Bread and bakery products play an important role in Mongolia due to its nutritional value and affordable price. The bread revenue has reached **USD 61 million**<sup>4</sup> in 2020, which is an increase of 9% from the previous year. Flour and bakery products are the most widely consumed and prominent products in Mongolia after meat and meat products. The average expenditure of cereals, flour and bakery products per month was MNT 71,613, or 24.7% of total food expenses after meat and meat products which is MNT 91,437<sup>5</sup> for an average household.

Wheat is the main raw material for bread and different types of pastry such as cake, pastry, bread, and traditional sole cake etc. and is considered a strategic food in Mongolia. According to the statistics prepared by the National Statistics Office, an average consumption per capita reaches 10.2kg, which is almost two times higher than the world average of 5.6 kg per month<sup>6</sup>. This implies Mongolia is one of the highest flour-consuming countries in the world. The average monthly consumption of wheat per capita is 11.6kg for rural areas and 8.9kg for the urban area. This is about 1 kg less than the consumption of two main strategic foods in Mongolia, which are milk and dairy products and 1.5 kg more than the consumption of meat and meat products. In 2019, Mongolia produced 47

Figure 9. Flour and flour products processing factories 2018



Source: NSO

Table 4. Wheat products produced 2015 – 2019 /in thousand tons/

Product	2015	2016	2017	2018	2019
Pastry	16.3	16.0	17.7	19.5	21.9
Biscuit	0.5	0.5	0.4	0.3	1.5
Cake	1.2	1.0	1.6	2.1	2.5
Bread	24.0	22.3	23.8	27.4	27.8
Traditional sole cake	0.5	0.5	0.5	0.5	0.6
Sweets	0.04	0.03	0.05	0.05	0.05

Source: NSO

Table 5. Wheat products per capita 2015 – 2019

Product	2015	2016	2017	2018	2019
Flour	69.7	69.3	67.3	66.8	66.3
Pastry	5.4	5.1	5.6	6.0	6.7
Biscuit	0.2	0.2	0.1	0.1	0.5
Cake	0.4	0.3	0.5	0.7	0.8
Bread	8.1	7.4	7.7	8.7	8.7
Traditional sole cake	0.2	0.2	0.2	0.2	0.2

Source: NSO

<sup>3</sup> Bakeinfo

<sup>4</sup> Statista

<sup>5</sup> National Statistics office of Mongolia

<sup>6</sup> Statista

thousand tons of wheat products domestically. There are about 2,000 food factories operating in Mongolia, of which 920 are wheat-products producing companies and approximately 30 are cake producers. In 2019, 27.8 thousand tons of bread and 21.2 thousand tons of pastries were produced.

**CUSTOMER PREFERENCE:** The main criterion for choosing a place to buy pastry products is how close the food selling place is to the residence or workplace. Therefore three-quarters of the purchase of bakery products are sold through stores and supermarkets. Currently, there are 14,078 supermarkets or similar operating food distribution points in Mongolia, mostly concentrated in urban areas. Consumers tend to make the buying decision based on the possibility to buy other kinds of products at once and are mostly concerned with the taste, freshness, and price of the pastry. Although new innovative pastry producing places are opening such as Tous Les Jours, the price is at least 3 times expensive than the traditional pastry producers. Consumers' tastes do not differ by certain types: the leader of the advantages are the long-standing popular varieties of pastries such as Jimst, Muukhii, Suut and Boortsog or bread such as Atar.

Table 6. Food distribution points across Mongolia





Size	Category	Area		Total
		Urban	Rural	
Large	Hypermarket	33	10	43
Medium	Supermarket	142	175	317
Semi-medium	Minimarket	570	574	1244
	Convenience store	84	70	154
Small	Grocery store	3638	6332	9970
	Next to fuel distribution points	30	69	99
	Kiosk	1669	582	2251

Source: Ministry of Food and Agriculture in Mongolia

Sales of these varieties account for a huge share of market sales. In recent years, consumers change their preferences and choose healthier consumption. As a result, the Company adopts and produces high-quality keto products such as keto bread, flax flour bread, vegan hard bread, and almond coconut bread to suit their tastes. This adaptation exemplifies that the Company is capable of producing an array of high-quality and standard products that match any changes in customer preferences.

**COMPETITIVE POSITIONING:**

Table 7. Key Players in Bread and Pastry Industry

				
Founded	1984	1936	1993	1941
Private or public	Public	Private	Private	Public
Products and Services	Around 131 kinds of products	Around 130 kinds of products	Bakery, tea, cookies, normal pastry	Bakery, cookies, candies
Employees	886	Around 400	N/A	Around 400
Market cap	MNT 15.2 billion	N/A	N/A	MNT 10.3 billion

**SWOT ANALYSIS:**

Source: Company websites



Table 8. SWOT analysis

Strengths	Weaknesses
<ul style="list-style-type: none"> <li>• Strong brand image and market presence among consumers for its quality and key brands such as “Atar Talkh” and “Misheel Talkh.”</li> <li>• Highly diversified portfolio of products with more than 35 types of bread, 34 types of pastries, 10 types of festive cake, marmalade, soft candy collection and biscuits.</li> <li>• A robust network of supply chain and distribution network of over 3000 distribution channels in just Ulaanbaatar.</li> <li>• Owns a number of intellectual property rights, including 50 patents and 38 quality marks that allow exclusivity over the products.</li> <li>• Promotes workplace diversity and inclusion, with people of many educational, age, socio-economic backgrounds as well as maintaining gender diversity.</li> </ul>	<ul style="list-style-type: none"> <li>• Sales and marketing costs have declined over the past three years, which could weaken the Company’s ability to expand its’ customer base and market its new products.</li> <li>• Vulnerability to the changing prices of raw materials from Russia as there is lack of stable sources domestically.</li> <li>• The Company operates in industry where prices are inelastic as the brand-switching is easy for customers.</li> <li>• The inability to adapt to changing customer needs such as continuing to produce traditional products allow for little room for innovations concerning the product type and packaging design.</li> </ul>
Opportunities	Threats
<ul style="list-style-type: none"> <li>• Introduce new products which contain healthy ingredients such as flax flour and almond flour for the increasing number of health-conscious consumers.</li> <li>• Expand operations and distribution network by selling to new restaurants and supermarket franchises like CU and GS25.</li> <li>• Deploy digital tools and leverage technology across the supply chain to meet the demand of online consumers and attract new customers.</li> <li>• A frozen food market is a new opportunity amidst the times like Covid-19.</li> </ul>	<ul style="list-style-type: none"> <li>• Threats of new entrants of small and medium-sized enterprises producing healthy pastries which can result in a highly fragmented industry.</li> <li>• Change of consumer food preference results in increased demand for more gluten-free or trans-fat-free foods.</li> <li>• Risk effects of the agricultural sector like poor wheat yield or inadequate harvest amount.</li> <li>• Covid-19 pandemic highlighted Mongolia’s dependence on flour imports from Russia and inadequate domestic supply of eggs. Thus, rising prices of raw materials such as eggs and flour can increase costs and negatively affect the Company’s production.</li> </ul>

## Valuation

We issue a BUY and HOLD recommendation on Talkh Chikher (TCK) with a target price of **MNT 33,762**, representing a 111.41% upside from the closing price of MNT 15,970 per share of July 21<sup>st</sup>, 2021. The target price is based on a mix of the Discounted Cash Flow to Firm Model and EV/EBITDA multiples, attributing 70% and 30% weighting respectively to each methodology. Even though the analysis shows that the Company share has an upside of 111% potential, we issued the BUY and HOLD recommendation due to capital market in Mongolia is relatively slow compared to other markets such as NYSE and LSE. This means the upside potential could not be achieved in the next 12 months but in the long term.

**DCF VALUATION:** Since Talkh Chikher's cash flow is rather stable especially during the pandemic, with a gradual increase in sales, hence Free cash flow to firm ("FCFF") methodology was chosen to arrive at the intrinsic value of the Company. We expect the terminal growth rate to stabilize at 2.0% after 2025 contingent on the increased demand for bakery products and growing population. Based on the FCFF method of our DCF model, the estimated price is MNT 33,055.

Table 12. Discounted Cash Flow method

(MNT million)	2017A	2018A	2019A	2020A	2021E	2022E	2023E	2024E	2025E
<b>Revenue</b>	<b>36,427</b>	<b>46,604</b>	<b>54,856</b>	<b>63,054</b>	<b>70,305</b>	<b>76,492</b>	<b>82,688</b>	<b>88,476</b>	<b>93,785</b>
<i>growth</i>	12%	28%	18%	15%	12%	9%	8%	7%	6%
COGS	27,287	35,520	40,886	47,695	52,810	57,585	62,312	66,522	70,636
<b>Gross profit</b>	<b>9,141</b>	<b>11,084</b>	<b>13,970</b>	<b>15,359</b>	<b>17,496</b>	<b>18,907</b>	<b>20,376</b>	<b>21,955</b>	<b>23,149</b>
<i>margin, %</i>	25%	24%	25%	24%	25%	25%	25%	25%	25%
Sales and marketing expenses	313	538	438	348	527	543	653	610	675
G&A expenses	6,317	3,939	5,424	6,125	6,574	7,190	7,740	8,443	8,885
Other expense	797	496	739	490	903	1,019	960	1,044	1,075
Forex gain/(loss)	-	-	-	-	-	-	-	-	-
Other income (losses)	(415)	(506)	(525)	(495)	(558)	(728)	(756)	(779)	(811)
<b>EBITDA</b>	<b>1,299</b>	<b>5,606</b>	<b>6,844</b>	<b>7,902</b>	<b>8,934</b>	<b>9,427</b>	<b>10,267</b>	<b>11,078</b>	<b>11,703</b>
Depreciation & Amortization	N/A	3,354	4,000	4,418	4,886	5,160	5,589	6,006	6,482
<b>EBIT</b>	<b>1,299</b>	<b>2,252</b>	<b>2,843</b>	<b>3,483</b>	<b>4,048</b>	<b>4,266</b>	<b>4,678</b>	<b>5,072</b>	<b>5,221</b>
Tax	171	276	387	447	405	427	468	507	522
CAPEX	-	9,448	8,537	6,207	7,729	7,994	7,906	8,112	9,188
Net Working Capital	974	(2,387)	(1,943)	(3,514)	(4,087)	(4,732)	(4,785)	(4,662)	(5,480)
Increase/Decrease in NWC	(1,112)	(3,360)	443	(1,571)	(573)	(644)	(53)	123	(818)
<b>Unlevered Free Cash Flow</b>	<b>1,303</b>	<b>2,240</b>	<b>(758)</b>	<b>(2,524)</b>	<b>1,373</b>	<b>1,651</b>	<b>1,946</b>	<b>2,336</b>	<b>2,811</b>
WACC					15.00%	15.00%	15.00%	15.00%	15.00%
Discount Period					0.00	1.00	2.00	3.00	4.00
Discount Factor					1.00	0.87	0.76	0.66	0.57
<b>PV of Free Cash Flow</b>					<b>1,373</b>	<b>1,436</b>	<b>1,471</b>	<b>1,536</b>	<b>1,607</b>

Table 9. Valuation Matrix

Valuation matrix		
Method	Weight	Share price
DCF	60%	33,055
Comparable companies	40%	34,822
<b>Target price</b>		<b>MNT 33,762</b>

Table 10. Company information

Assumptions	Value
Outstanding shares	1,023,703
Projection period	5 years
Discount rate	15%
Perpetual growth rate	2%
Closing share price (as of 21 <sup>st</sup> of July 2021)	15,970

Table 11. DCF valuation

DCF valuation /MNT million/	
Enterprise value	30,457
Less: Total debt	-
Plus: Cash and cash equivalents	3,382
Equity value ("Market Cap")	33,839
<b>Price per share (MNT)</b>	<b>33,055</b>



## Sensitivity analysis

We evaluate the DCF model's robustness to changes in the key inputs, which are WACC and growth rate. To check whether the growth rate and WACC could affect the share price, we used sensitivity analysis. As can be seen in Table 14, despite the growth rate being at 0% and 17% of WACC, the share price is still 87.0% higher than its closing price of MNT 15,970.

**RELATIVE VALUATION: PEER ANALYSIS:** We identified Enterprise Value ("EV") to Earnings before Interest, Tax, Depreciation and Amortization ("EBITDA") as the most appropriate multiple to compare Talkh Chikher JSC to its peers due to the nature of its business model. The peer group consists of major players in the food industry including meat and milk that are public on the Mongolian Stock Exchange. As the Mongolian stock market is rather small and equity trading volume is quite low compared to other markets<sup>7</sup>, the trade volume has been stagnant for the Company. The share trade volume is relatively low with an average of 52 shares volume a day, which indicates low liquidity compared to shares of other companies such as Tumen Shuvuut JSC /an average of 66,000 shares per day/ and Suu JSC / an average of 8,600 shares per day/. Therefore, the relative valuation, using EV/EBITDA multiple has led to a 5-year horizon target price of MNT 34,822, which weighs 40% of the total valuation analysis.

Table 15. Relative valuation: Peer analysis

Companies	Ticker	Country	Market Cap	Share price	ROE	EV/EBITDA	P/E
			MNT million	MNT			
Atar-Urguu	ATR	Mongolia	10,298	60,000	2%	5.00	53.1
Makhimpex	MMX	Mongolia	10,604	2,790	15%	5.87	17.4
Suu	Suu	Mongolia	77,107	225	20%	1.57	12.4
<b>Mean</b>					<b>12%</b>	<b>4.15</b>	<b>27.6</b>

Source: MSE, MICC estimates

Relative valuation	MNT million
Enterprise value ("EV")	<b>37,057</b>
EV/EBITDA	4.15
Less: Total debt	2,179
Plus: Cash and cash equivalent	769
Equity value ("Market Cap")	35,647
Outstanding shares	1,023,703
<b>Price per share (MNT)</b>	<b>34,822</b>

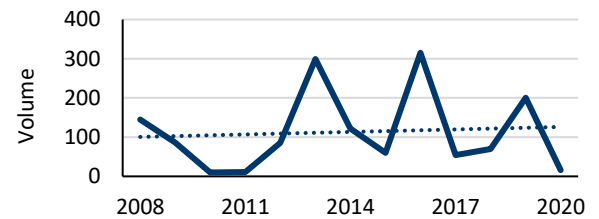
Source: MICC estimates

Table 13. Sensitivity analysis

Growth rate	WACC				
	13%	14%	15%	16%	17%
0%	34,833	33,417	32,129	30,950	29,864
1%	35,443	33,926	32,559	31,317	30,179
2%	36,164	34,520	33,055	31,736	30,536
3%	37,029	35,222	33,634	32,219	30,945
4%	38,086	36,065	34,318	32,783	31,416

Source: MICC estimates

Figure 10. Trade volume of Talkh Chikher stock on MSE



Source: MSE

Table 14. Public floats of classification 1 listed companies

Ticker	Public float
TCK	29.00%
TUM	25.00%
MNDL	22.90%
BODI	19.90%
GOV	15.77%
SUU	7.20%
APU	5.53%

Source: MSE

<sup>7</sup> CFA institute

## INVESTMENT RISKS

**MACROECONOMIC RISK:** The delta variant, a mutated version of the coronavirus, was first identified in India and is spreading rapidly in some parts of the world, and on track to become the dominant virus strain globally. If the virus spreads in Mongolia, it could lead to another lockdown. This can create a severe situation for the economy and businesses, causing businesses to go bankrupt. The inflation rate has risen from 3.3% to 6.2% over the past year, boosting raw material prices. This will increase the price of the main products and may lead to a decrease in demand.

**LIQUIDITY RISK:** Liquidity indicators are a crucial part of a company's operations. Over the past five years, Talkh Chikher's liquidity has been declining. Since 2016, the current and quick ratio has been declining compared to the industry average. However, the Company has low financial leverage and that does not pose a serious problem.

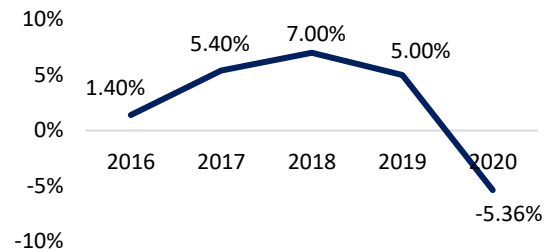
**MARKET RISK:** Consumers are increasingly opting for healthier and more nutritious foods. This is one of the reasons why they may refuse white flour bread and pastries in the future. However, Talkh Chikher produces products that meet the needs of its customers in a timely manner. Since the Company has satisfied its market position, the market risk would not have significant impact to the Company's operation.

Table 16 Risk Matrix

		Impact				
		Negligible	Minor	Moderate	Significant	Severe
Probability	Certain					
	Likely					
	Possible				1	
	Unlikely			3		2
	Rare					

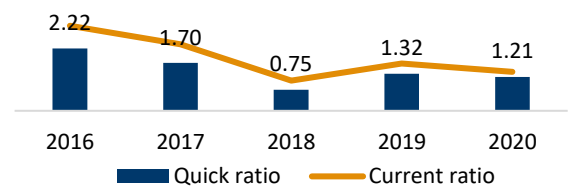
Source: MICC estimates

Figure 11. GDP growth rate



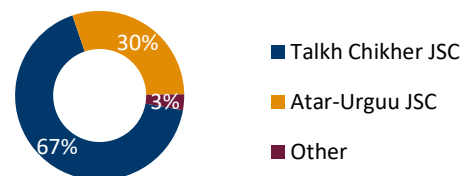
Source: NSO

Figure 12. Liquidity ratios



Source: Talkh Chikher financial report

Figure 13. Bread Market Shares by Companies



Source: Talkh Chikher operation report

## CONCLUSION

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Talkh Chikher JSC is one of the leaders in the bread and bakery industry in Mongolia as well as one of the only two public companies within the industry. Based on Talkh Chikher's historical track record and our analysis of the Company's current market position, we expect Talkh Chikher to remain the dominant player in the Mongolian baked goods industry for years to come. This is because the Company has a competitive advantage by producing healthy products with high-quality standards that meet the changing needs of consumers, and there is a low threat of new entrants to the market. Also, Talkh Chikher JSC continues to be unaffected by Covid-19 restrictions and its effect on the global economy as the Company produces widely used consumer staples goods. As the Delta Variant fears spread throughout the world, there is a risk of the economic and business downturn as Mongolia might commence strict quarantine measures. However, as the Company has already successfully weathered through previous lockdowns, we believe the Company will still be able to grow in case there is another lockdown.

Talkh Chikher JSC's target price was derived by a mix of DCF model and relative valuation, accounting for 70% and 30% respectively. As per our estimation, we believe the Company is currently undervalued and we have a BUY and HOLD rating at a target share price of **MNT 33,762** with an upside potential of **111.41%** in the long term (in 5 years). The Company was able to increase its revenue by 15% in 2020 during the Covid-19 pandemic which proves Talkh Chikher's profitability is not too much dependent on the global pandemic because bakery products are a basic everyday necessity for low to mid-income households as a food source. The competitive positioning of Talkh Chikher JSC in the market and the growth prospective of the bakery industry with regards to the growing population have contributed to derive the target price. We believe that the difference between the current share price and the target price is mostly due to the current inefficient capital market whose security price does not fully reflect the value of its assets and also the shares of Talkh Chikher are illiquid. For companies whose stock price is quite high and illiquid, a stock split is recommended to facilitate trading, attract new investors, and make it easier for buyers and sellers to participate in the stock market. Therefore, in order for the Company to reach its full potential, Talkh Chikher needs to split the stock. Moreover, the Company should increase the dividend payout ratio in the future.

## ABOUT MICC

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Mongolia International Capital Corporation (MICC) was established in 2005 as the first investment banking firm in Mongolia. Mongolia's rapid economic development and favorable financial environment present unique prospects for investment opportunities and growth potential for companies. In order to enable our clients and investors to take full advantage of these opportunities, MICC offers investment banking, asset management, securities underwriting, and brokerage services. In addition, we conduct periodic macroeconomic research, develop analyses of domestic industries and review equities listed on the Mongolian Stock Exchange.

MICC continues to make history in the Mongolian financial sector. We serve leading companies in the mining, manufacturing, financial, retail trade, airline, and construction sectors, and prize our close and long-standing working relationships with our clients. Our goal is to assist both local and international companies to realize their strategic goals by offering innovative and efficient financing solutions.

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### Disclosure

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