13 August 2019

Consumer Non-cyclicals | Food & Beverage Products

Food Empire (FEH SP)

Buy (Maintained)

Better Margins Post Rationalisation; Still BUY

Target Price (Return)	SGD0.73 (+38%)
Price:	SGD0.53
Market Cap:	USD199m
Avg Daily Turnover (SGD/USD)	0.04m/0.03m

- **Stay BUY with a higher SGD0.73 TP from SGD0.69, 38% upside, 1.6% yield.** Food Empire's 2Q19 results beat our expectations. PATMI surged 140% to USD5.6m. Excluding FX impact, core PATMI grew 22% to USD5.2m. The tremendous improvement in results was largely attributed to the rationalisation of under-performing markets. We expect 2H19 to also show strong improvements following the rationalisation. As such, we raised our FY19F-21F earnings 6-8%, thereby increasing our TP.
- **2Q19's results were above our expectations.** This was largely attributed to the rationalisation of advertising & promotions (A&P) costs in under-performing new markets such as Myanmar and the Philippines. As a result, operating margins improved 2.1ppts YoY to 9.3%, leading to strong growth in earnings.
- **2Q19 revenue fell 2% YoY to USD68m.** Sales from Indochina fell 12% YoY, largely due to lower A&P expenditure in Myanmar. Food Empire's biggest market, Russia, saw increased sales in local currency terms, but showed a 6.4% YoY decline in revenue when translated into USD.

  Overall, sales were pulled up by Ukraine, Kazakhstan, and other Commonwealth of Independent States markets, which delivered strong revenue growth of 15% YoY during the quarter.
- **Positive outlook for near-term earnings.** Moving forward, Food Empire plans to focus its efforts on growing its core markets, given the slowing economy driven by US-China trade tensions. We expect to see a similar reduction in A&P expenditure over 2H19. However, the A&P savings are likely to be partially offset by higher depreciation from 4Q19. This is because the group's second instant coffee plant in India is expected to complete construction this year and commence operations in FY20.

  Barring any major depreciation of the RUB, we expect FY19 earnings to deliver strong growth of 22% this year. We have raised our FY19-21 earnings estimates 6-8%, which – in turn – increased our TP to SGD0.73, pegged to 13x FY19F P/E. We maintain our call on this counter.

Analyst

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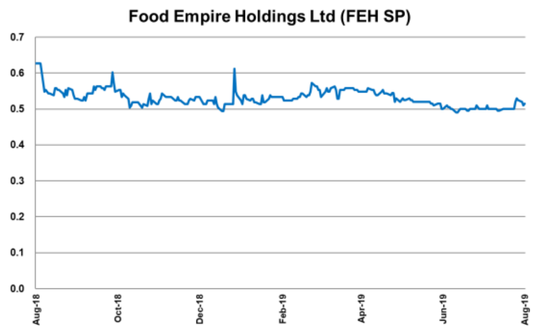
Share Performance (%)

	YTD	1m	3m	6m	12m
Absolute	(1.0)	3.0	(1.9)	(4.6)	(18.9)
Relative	(4.1)	9.0	2.5	(3.5)	(13.7)
52-week price low/high					0.49 - 0.64



Source: Bloomberg

Forecasts and Valuation	Dec-17	Dec 18	Dec 19F	Dec 20F	Dec 21F
Total turnover (USDm)	269.5	284.3	290.9	313.6	345.9
Recurring net profit (USDm)	20.7	18.1	22.2	24.2	27.3
Recurring net profit growth (%)	98.7	(12.6)	22.6	9.2	12.7
Recurring P/E (x)	10.0	11.5	9.3	8.6	7.6
P/BV (x)	1.2	1.2	1.1	1.0	0.9
P/CF (x)	9.7	18.8	11.7	10.1	9.6
Dividend Yield (%)	1.2	1.3	1.6	1.8	2.0
EV/EBITDA (x)	5.7	7.2	5.7	4.9	4.3
ROE (%)	12.3	10.3	11.3	11.2	11.4
Net debt to equity (%)	net cash	(4.9)	2.7	0.2	(6.5)
Interest coverage (x)	32.3	27.3	24.4	26.6	29.9

Source: Company data, RHB

Financial Exhibits

Asia
Singapore
Food & Beverage Products
Food Empire
FEH SP
BUY

Valuation basis

13x FY19F P/E.

Key drivers

i. M&A opportunities;
ii. Privatisation.

Key risks

Downside risks include:
i. RUB depreciation;
ii. Intensifying competition.

Company Profile

Food Empire is an instant coffee brand and manufacturing company. Its key markets are: Russia, Ukraine, Kazakhstan, CIS countries, and Vietnam.

Financial summary	Dec-17	Dec-18	Dec-19F	Dec-20F	Dec-21F
Recurring EPS (USD)	0.04	0.03	0.04	0.05	0.05
DPS (SGD)	0.00	0.00	0.01	0.01	0.01
BVPS (USD)	0.31	0.33	0.37	0.41	0.45
ROE (%)	12.33	10.26	11.33	11.17	11.35

Valuation metrics	Dec-17	Dec-18	Dec-19F	Dec-20F	Dec-21F
Recurring P/E (x)	10.0	11.5	9.3	8.6	7.6
P/B (x)	1.2	1.2	1.1	1.0	0.9
FCF Yield (%)	0.2	0.1	0.3	0.2	0.2
Dividend yield (%)	1.2	1.3	1.6	1.8	2.0
EV/EBITDA (x)	5.7	7.2	5.7	4.9	4.3
EV/EBIT (x)	6.6	8.7	6.9	6.2	5.1

Income statement (USDm)	Dec-17	Dec-18	Dec-19F	Dec-20F	Dec-21F
Total turnover	269	284	291	314	346
Gross profit	103	111	114	122	131
EBITDA (adj.)	35	27	35	40	46
Depreciation & amortisation	5	6	6	8	10
Operating profit	29	22	29	32	36
Net interest	-1	-1	-1	-1	-1
Pre-tax profit	18	20	28	31	35
Taxation	-5	-2	-6	-7	-8
Net profit	13	18	22	24	27
Recurring net profit	21	18	22	24	27

Cash flow (USDm)	Dec-17	Dec-18	Dec-19F	Dec-20F	Dec-21F
Change in working capital	-4	-12	-5	-4	-7
Cash flow from operations	29	15	24	28	29
Capex	-6	-11	-30	-20	-10
Cash flow from investing activities	-10	-10	-36	-20	-10
Dividends paid	-6	-11	-30	-20	-10
Cash flow from financing activities	-5	-5	15	-3	-3
Cash at beginning of period	29	43	42	45	50
Net change in cash	14	-1	3	5	16
Ending balance cash	43	42	45	50	66

Balance sheet (USDm)	Dec-17	Dec-18	Dec-19F	Dec-20F	Dec-21F
Total cash and equivalents	43	42	45	50	66
Tangible fixed assets	65	69	93	105	106
Total investments	13	11	11	11	11
Total assets	247	245	286	311	340
Short-term debt	20	20	10	10	10
Total long-term debt	16	13	40	40	40
Total liabilities	80	69	91	95	100
Total equity	167	175	195	216	240
Total liabilities & equity	247	245	286	311	340

Key metrics	Dec-17	Dec-18	Dec-19F	Dec-20F	Dec-21F
Revenue growth (%)	11.2	5.5	2.3	7.8	10.3
Recurrent EPS growth (%)	98.5	(12.6)	22.6	9.2	12.7
Gross margin (%)	38.3	39.0	39.3	39.0	38.0
Operating EBITDA margin (%)	12.8	9.6	12.0	12.8	13.2
Net profit margin (%)	7.7	6.4	7.6	7.7	7.9
Capex/sales (%)	2.2	3.8	10.3	6.4	2.9
Interest cover (x)	32.3	27.3	24.4	26.6	29.9

Figure 1: 2Q19 results summary

(USDm)	2Q19	1Q19	2Q18	QoQ	YoY	Comment
Revenue	67.8	70.7	69.3	(4.1)	(2.2)	Decline in revenue was due to rationalisation of under-performing new markets.
Gross profit	25.6	28.4	26.9	(9.9)	(4.6)	
Gross margin	*37.8*	*40.2*	*38.7*			
EBIT	6.3	9.1	5.0	(30.6)	27.1	
Op margin	*9.3*	*12.9*	*7.2*			Operating margin improved YoY as a result of reduced A&P.
Recurring PATMI	5.2	7.2	4.3	(27.6)	21.9	Excluding FX impact, core PATMI grew 22% YoY.
Net margin	*7.6*	*10.1*	*6.1*			

Source: Company data, RHB

Figure 2: Revenue breakdown by segments

('000 USD)	2Q19	1Q19	2Q18	QoQ	YoY
Russia	25,152	29,240	26,877	(14.0)	(6.4)
Ukraine	6,954	6,665	6,063	4.3	14.7
Kazakhstan and CIS Markets	9,985	9,072	8,706	10.1	14.7
Indochina	12,270	14,450	13,942	(15.1)	(12.0)
Others	13,445	11,257	13,728	19.4	(2.1)

Source: Company data, RHB

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