

9 June 2020

Consumer Non-cyclical | Food & Beverage Products

Food Empire (FEH SP)

Buy (Maintained)

RUB Appreciation Helps; Keep BUY

Target Price (Return): SGD0.75 (41.5%)
 Price: SGD0.53
 Market Cap: USD204m
 Avg Daily Turnover (SGD/USD) 0.29m/0.20m

- **Keep BUY and SGD0.75 TP, 42% upside and c.3% yield.** The RUB has appreciated 15% against the USD over the last two months amidst oil price improvements. This is positive for Food Empire, as it should help support gross margins and minimise FX losses. We still expect 2Q20 results to be soft due to the introduction of the non-working period in Russia from end March to mid-May. We expect business to start picking up in June with the relaxing of the lockdown measures.
- **Strengthening of the RUB reduces FEH's downside risks.** The Russia market contributes c.40% to the group's revenue. We note that the RUB has appreciated from its low in March along with the reversal of oil price movements. Yesterday, the currency stood at RUB68 against USD1.00 – almost comparable to pre-oil crisis levels (2019 average: RUB65) vs the low of RUB78 against USD1.00 as at 31 Mar when oil prices plunged. The UAH and KZT have also appreciated in tandem with the RUB.
- **Given that FEH's sales of goods are denominated in local currencies,** while the bulk of raw materials are priced in USD, the strengthening of the Commonwealth of Independent States (CIS) currencies should help reduce gross margin erosion in 2Q20. It could lead to some FX gains in 2Q20 and erase some of the FX losses recognised in 1Q20.
- **Expect 2Q20 to remain weak, with a recovery in 2H20.** Russia imposed a non-working period from end March to 11 May, with only essential services opened. The Moscow and Saint Petersburg regions extended their lockdowns to 31 May. Unemployment rose 26% MoM in April, with the unemployment rate reaching a high of 5.8%. Management earlier said Russia's sales were negatively impacted in April due to lower footfalls at retail stores. We believe sales for May will also remain soft before picking up in June – in line with the gradual resumption of economic activities. We expect the same for Ukraine and Kazakhstan, as these two countries also began to gradually ease their restriction measures.
- **As 3-in-1 instant coffee mix is a relatively staple product,** and FEH has a strong market share in this segment in its key CIS markets, we expect sales to improve in 2H20 as COVID-19 fears dampen. The group also implemented a c.10% price hike for some of its key markets. The impact of the price increase should be fully reflected from 3Q20 onwards.
- **Outlook improves as the RUB stabilises.** With the recent strengthening of the RUB, we reduce our assumptions for FX losses for FY20. This raised our FY20F reported PATMI by 6%, while our core PATMI forecast – excluding FX – remains largely unchanged. We maintain our call and SGD0.75 TP, which is pegged to 12x P/E.

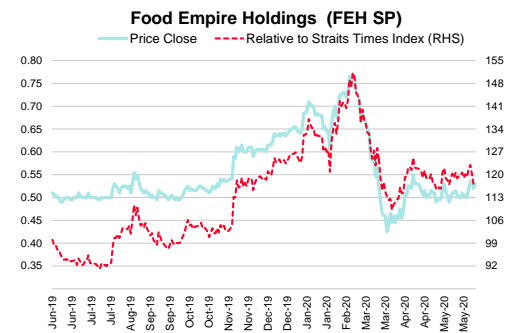
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Share Performance (%)

	YTD	1m	3m	6m	12m
Absolute	(18.5)	7.1	(18.5)	(12.4)	2.9
Relative	(3.9)	0.1	(9.7)	0.9	15.3
52-wk Price low/high (SGD)					0.43 – 0.77



Source: Bloomberg

Forecasts and Valuation	Dec-18	Dec-19	Dec-20F	Dec-21F	Dec-22F
Total turnover (m)	284	289	286	315	339
Recurring net profit (m)	22	26	24	28	31
Recurring net profit growth (%)	4.5	17.9	(7.6)	19.0	11.7
Recurring P/E (x)	9.38	8.03	8.68	7.30	6.53
P/B (x)	1.2	1.0	0.9	0.8	0.8
P/CF (x)	13.64	5.56	7.94	8.25	5.81
Dividend Yield (%)	1.3	1.9	2.9	3.7	3.8
EV/EBITDA (x)	7.05	5.44	5.47	4.48	3.68
Return on average equity (%)	10.5	13.6	9.1	12.0	12.2
Net debt to equity (%)	net cash	net cash	0.6	0.7	net cash

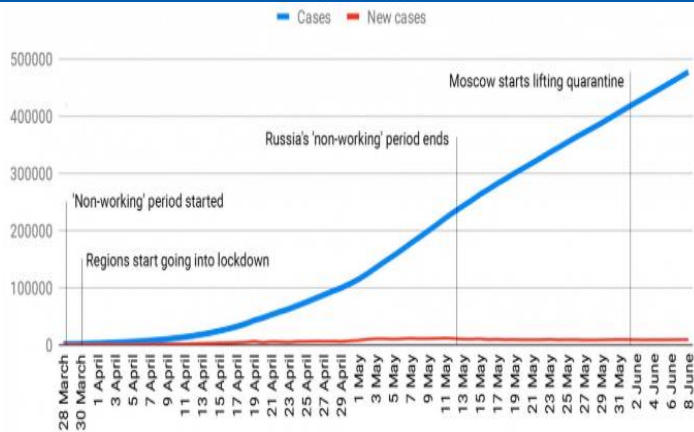
Source: Company data, RHB

Financial Exhibits

Asia	Financial summary	Dec-18	Dec-19	Dec-20F	Dec-21F	Dec-22F
Singapore	Recurring EPS	0.04	0.05	0.04	0.05	0.06
Consumer Non-cyclical	DPS	0.00	0.01	0.01	0.01	0.01
Food Empire	BVPS	0.33	0.38	0.41	0.46	0.50
FEH SP	Return on average equity (%)	10.5	13.6	9.1	12.0	12.2
Buy						
	Valuation metrics	Dec-18	Dec-19	Dec-20F	Dec-21F	Dec-22F
Valuation basis	Recurring P/E (x)	9.38	8.03	8.68	7.30	6.53
12x FY20F P/E.	P/B (x)	1.2	1.0	0.9	0.8	0.8
	FCF Yield (%)	2.0	(0.6)	0.4	2.3	12.3
Key drivers	Dividend Yield (%)	1.3	1.9	2.9	3.7	3.8
i. Margins expansion on a strengthening RUB;	EV/EBITDA (x)	7.05	5.44	5.47	4.48	3.68
ii. Expansion into Indochina and China.	EV/EBIT (x)	8.96	6.54	7.11	5.83	4.82
	Income statement (m)	Dec-18	Dec-19	Dec-20F	Dec-21F	Dec-22F
Key risks	Total turnover	284	289	286	315	339
i. Negative movement in the RUB and other CIS currencies;	Gross profit	111	112	111	123	132
ii. Rising coffee bean prices.	EBITDA	27	37	37	46	51
	Depreciation and amortisation	(6)	(6)	(9)	(11)	(12)
	Operating profit	22	30	29	35	39
	Net interest	(1)	(1)	(1)	(1)	(1)
	Pre-tax profit	20	32	24	34	38
	Taxation	(2)	(6)	(4)	(6)	(7)
	Reported net profit	18	26	20	28	31
	Recurring net profit	22	26	24	28	31
	Cash flow (m)	Dec-18	Dec-19	Dec-20F	Dec-21F	Dec-22F
	Change in working capital	(11.9)	(14.9)	(2.0)	(13.4)	(7.8)
	Cash flow from operations	14.9	36.8	25.8	24.8	35.2
	Capex	(10.8)	(38.1)	(25.0)	(20.0)	(10.0)
	Cash flow from investing activities	(9.6)	(37.4)	(25.0)	(20.0)	(10.0)
	Dividends paid	(2.4)	(2.6)	(3.9)	(5.9)	(7.6)
	Cash flow from financing activities	(5.0)	12.7	(5.8)	(15.4)	(23.1)
	Cash at beginning of period	42.8	42.2	54.7	49.7	39.2
	Net change in cash	0.3	12.1	(5.0)	(10.6)	2.2
	Ending balance cash	42.2	54.0	49.7	39.2	41.3
	Balance sheet (m)	Dec-18	Dec-19	Dec-20F	Dec-21F	Dec-22F
	Total cash and equivalents	42	55	50	39	41
	Tangible fixed assets	69	99	116	125	124
	Total investments	30	41	41	41	41
	Total assets	245	308	322	342	352
	Short-term debt	20	15	10	10	15
	Total long-term debt	13	35	41	31	10
	Total liabilities	69	102	101	98	84
	Total equity	175	206	221	244	268
	Total liabilities & equity	245	308	322	342	352
	Key metrics	Dec-18	Dec-19	Dec-20F	Dec-21F	Dec-22F
	Revenue growth (%)	5.5	1.5	(0.9)	10.2	7.7
	Recurrent EPS growth (%)	4.5	16.9	(7.6)	19.0	11.7
	Gross margin (%)	39.0	38.7	39.0	39.0	38.8
	Operating EBITDA margin (%)	9.6	12.7	13.1	14.5	15.0
	Net profit margin (%)	6.4	9.0	6.8	8.9	9.2
	Dividend payout ratio (%)	14.7	29.8	30.0	27.0	25.0
	Capex/sales (%)	3.8	13.2	8.7	6.3	2.9
	Interest cover (x)	27.3	21.6	22.2	31.8	57.6

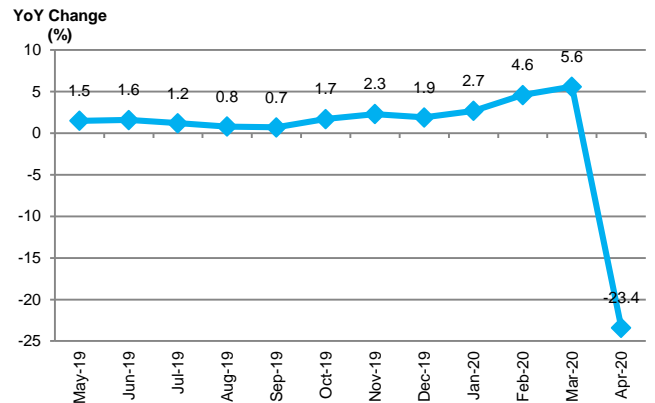
Source: Company data, RHB

Figure 1: Russia's COVID-19 cases and timeline



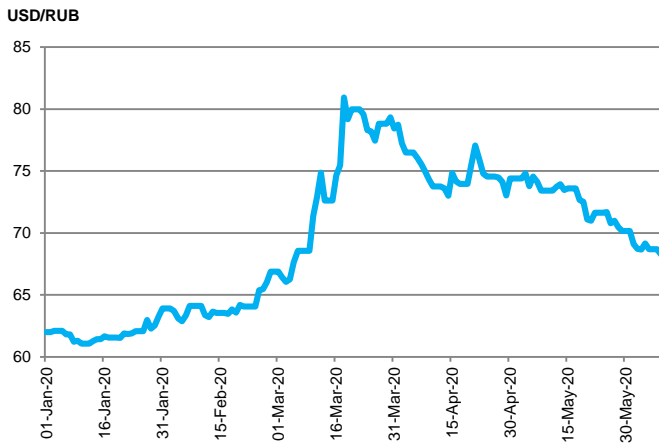
Source: The Moscow Times

Figure 2: Russian retail sales plunged in April due to the negative impact of COVID-19 and lockdowns



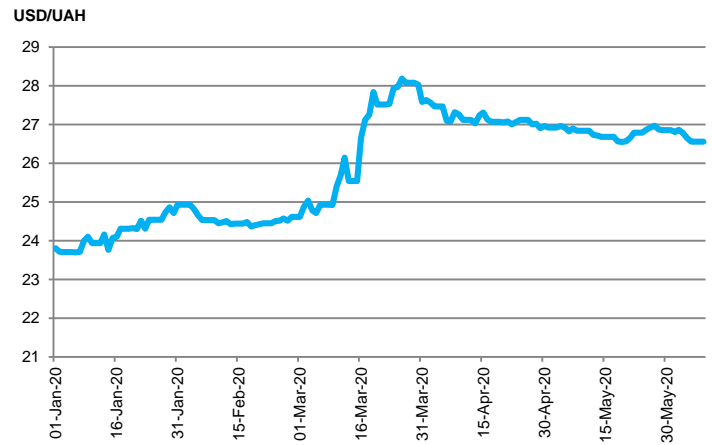
Source: Russia Federal State Statistic Service

Figure 3: The RUB reversed most of the losses in March



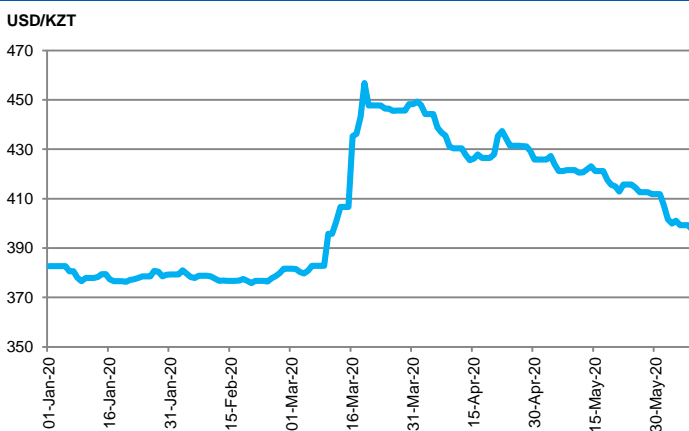
Source: Bloomberg

Figure 4: The UAH/USD has also stabilised



Source: Bloomberg

Figure 5: A similar trend was also seen in the USD/KZT



Source: Bloomberg

Recommendation Chart



Source: RHB, Bloomberg

Date	Recommendation	Target Price	Price
2020-05-13	Buy	0.75	0.51
2020-02-26	Buy	0.88	0.73
2020-01-17	Buy	0.83	0.70
2019-11-12	Buy	0.73	0.59
2019-03-04	Buy	0.69	0.57
2018-11-19	Buy	0.66	0.53
2018-08-15	Neutral	0.60	0.56

Source: RHB, Bloomberg

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