

25 August 2022

Consumer Non-cyclical | Food Products

Farm Fresh (FFB MK)

Buy (Maintained)

GPM Pressure To Ease; Stay BUY

- **Maintain BUY, with new MYR1.85 TP from MYR1.88, 11% upside.** Farm Fresh's 1QFY23 (Mar) results missed expectations on higher-than-expected production costs. Despite the hiccup, we foresee margin recovery from 2QFY23F, given the implementation of price increases, contribution from products with better margins, and normalisation of raw material prices. In the longer run, its multi-pronged expansion plans, fresh dairy product proposition, and strong brand equity should underpin growth prospects.
- **FFB's 1QFY23 results were below expectations.** Core net profit of MYR17m (-15% YoY) met only 18% of our and consensus' forecasts on higher-than-expected input costs arising from the school milk project. Post results, we trim FY23F-25F earnings by 7%, 3% and 3%. Correspondingly, our DCF-derived TP (inclusive of a 6% ESG premium) drops to MYR1.85. The TP implies 32x 2023F P/E, which is at a premium over its mid-cap consumer staple peers.
- **Results review.** YoY, 1QFY23 revenue grew 7% to MYR144m thanks to the robust sales in Malaysia (+10%), but offset by lower sales in Australia (-16%) on the back of a planned downsizing of non-core business and the ceasing of external raw milk sales. Despite the flat GPM, 1QFY23 PBT fell 12% to MYR14m due to the higher sales and distribution (S&D) expenses that arose from the school milk project and ESOS expenses of MYR2m. QoQ, 1QFY23 sales was 13% higher following the broader reopening of the economy and contribution from new products. However, 1QFY23 gross profit only inched up by 3% on a 2.4ppts GPM slippage, dragged by higher input costs for the school milk project. Core net profit was 5% lower QoQ due to the abovementioned higher opex.
- **GPM should stage a quick rebound.** The group has raised the prices for its chilled ready-to-drink (RTD) products in Malaysia (effective mid-July) and Singapore (effective August) by an average of 5% and 10% in order to pass on the higher input costs. This should arrest GPM erosion going forward, further aided by the normalisation in skimmed milk powder prices. The new product launches in the UHT and growing up milk segments should also increasingly contribute in the quarters ahead, whilst FFB is also targeting to improve its market penetration in Singapore, followed by the planned entry into Indonesia, the Philippines and Hong Kong. These expansion plans will be supported by the new capacity coming on stream progressively over the next 1-2 years.
- **Risks to our recommendation** include a sharp rise in commodity prices and major delays in expansion plans.

Target Price (Return): MYR1.85 (+11%)
Price (Market Cap): MYR1.67 (USD692m)
ESG score: 3.30 (out of 4)
Avg Daily Turnover (MYR/USD) 5.56m/1.26m

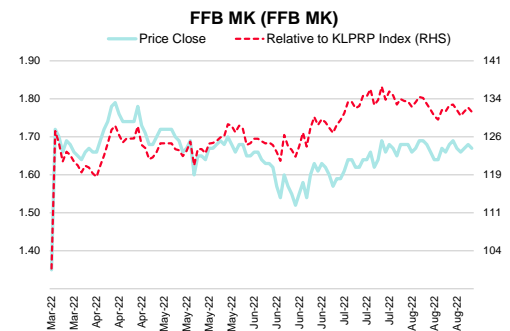
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Share Performance (%)

	YTD	1m	3m	6m	12m
Absolute	0.0	0.6	(0.6)	0.0	0.0
Relative	0.0	(2.9)	5.1	0.0	0.0
52-wk Price low/high (MYR)				1.35 – 1.79	



Source: Bloomberg

Overall ESG Score: 3.30 (out of 4)

E: GOOD

Completed a group-wide carbon footprint inventory exercise based on GHG Protocol Corporate Accounting and Reporting Standard, and aims to reduce 25% of their greenhouse emissions in five years. Makes use of sustainable packaging for its UHT products, and has regenerative agriculture processes and efficient water management in place.

S: EXCELLENT

Ensures that practices drafted by the Safety, Health and Environment Committee are reviewed and abided by. It also empowers local communities through the employment of rural demographics and internship programmes with local universities. Its farms have also attained the Certified Humane Raised and Handled Human certification

G: EXCELLENT

Adopted the recommendations under the Malaysian Code on Corporate Governance with independent directors comprising more than 50% of the board. Women make up about 40% of the board.

Forecasts and Valuation	Mar-21	Mar-22	Mar-23F	Mar-24F	Mar-25F
Total turnover (MYRm)	490	502	615	718	868
Recurring net profit (MYRm)	80	82	87	115	142
Recurring net profit growth (%)	172.9	2.1	6.6	31.5	24.1
Recurring P/E (x)	38.78	37.96	35.61	27.08	21.83
P/B (x)	13.2	5.1	4.6	4.1	3.6
P/CF (x)	52.00	63.25	29.95	21.18	18.27
Dividend Yield (%)	na	na	0.7	0.9	1.1
EV/EBITDA (x)	32.95	28.65	21.91	16.89	13.81
Return on average equity (%)	17.1	19.0	13.6	16.0	17.5
Net debt to equity (%)	95.5	net cash	12.2	16.4	8.1

Source: Company data, RHB

See important disclosures at the end of this report

Market Dateline / PP 19489/05/2019 (035080)

Financial Exhibits

Asia	Financial summary (MYR)	Mar-21	Mar-22	Mar-23F	Mar-24F	Mar-25F
Malaysia	Recurring EPS	0.04	0.04	0.05	0.06	0.08
Consumer Non-cyclical	DPS	-	-	0.01	0.02	0.02
Farm Fresh	BVPS	0.13	0.33	0.36	0.41	0.46
FFB MK	Return on average equity (%)	17.1	19.0	13.6	16.0	17.5
Buy						
	Valuation metrics	Mar-21	Mar-22	Mar-23F	Mar-24F	Mar-25F
	Recurring P/E (x)	38.78	37.96	35.61	27.08	21.83
	P/B (x)	13.2	5.1	4.6	4.1	3.6
	FCF Yield (%)	(1.1)	(0.4)	(2.5)	(0.1)	3.2
	Dividend Yield (%)	-	-	0.7	0.9	1.1
	EV/EBITDA (x)	32.95	28.65	21.91	16.89	13.81
	EV/EBIT (x)	42.07	39.58	29.38	22.71	18.35
Valuation basis						
Discounted Cash Flow						
Key drivers						
i. Market share gains;						
ii. Expansion into new overseas markets;						
iii. Growing health consciousness amongst the consumers.						
Key risks						
i. Sharp hike in raw material costs;						
ii. Intense competition;						
iii. Major delay in expansion plans.						
Company Profile						
Farm Fresh operates a fast-growing vertically integrated dairy group engaged in the business of farming, manufacturing and distribution of various dairy products and plant-based products.						
	Income statement (MYRm)	Mar-21	Mar-22	Mar-23F	Mar-24F	Mar-25F
	Total turnover	490	502	615	718	868
	Gross profit	141	136	174	213	258
	EBITDA	99	103	140	184	221
	Depreciation and amortisation	(21)	(29)	(36)	(47)	(55)
	Operating profit	77	75	104	137	167
	Net interest	(10)	(9)	(8)	(10)	(9)
	Pre-tax profit	68	66	96	127	157
	Taxation	(35)	13	(8)	(10)	(13)
	Reported net profit	36	80	87	115	142
	Recurring net profit	80	82	87	115	142
	Cash flow (MYRm)	Mar-21	Mar-22	Mar-23F	Mar-24F	Mar-25F
	Change in working capital	(2.8)	(53.4)	(27.3)	(25.6)	(37.5)
	Cash flow from operations	59.7	49.1	103.6	146.5	169.9
	Capex	(93.6)	(60.8)	(180.0)	(150.0)	(70.0)
	Cash flow from investing activities	(85.7)	(51.7)	(180.0)	(150.0)	(70.0)
	Dividends paid		0.0	(21.8)	(28.6)	(35.5)
	Cash flow from financing activities	24.5	339.0	(32.2)	(71.3)	(94.9)
	Cash at beginning of period	7.5	11.7	28.1	50.1	25.3
	Net change in cash	(1.5)	336.4	(108.6)	(74.8)	5.0
	Ending balance cash	6.0	348.1	(80.5)	(24.7)	30.2
	Balance sheet (MYRm)	Mar-21	Mar-22	Mar-23F	Mar-24F	Mar-25F
	Total cash and equivalents	12	309	200	125	129
	Tangible fixed assets	312	340	484	587	602
	Total investments	85	121	121	121	121
	Total assets	622	1,010	1,095	1,167	1,252
	Short-term debt	141	52	50	50	50
	Total long-term debt	101	232	232	200	150
	Total liabilities	381	399	418	405	383
	Total equity	241	611	676	762	869
	Total liabilities & equity	622	1,010	1,095	1,167	1,252
	Key metrics	Mar-21	Mar-22	Mar-23F	Mar-24F	Mar-25F
	Revenue growth (%)	61.8	2.3	22.5	16.7	21.0
	Recurrent EPS growth (%)	172.9	2.1	6.6	31.5	24.1
	Gross margin (%)	28.7	27.2	28.3	29.6	29.8
	Operating EBITDA margin (%)	20.1	20.6	22.8	25.7	25.5
	Net profit margin (%)	7.4	15.9	14.2	16.0	16.4
	Dividend payout ratio (%)	0.0	0.0	25.0	25.0	25.0
	Capex/sales (%)	19.1	12.1	29.3	20.9	8.1
	Interest cover (x)	7.75	6.75	8.19	10.30	14.81

Source: Company data, RHB

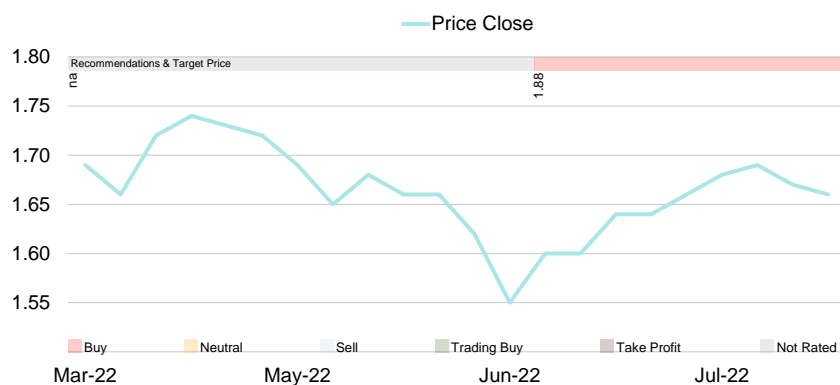
Results At A Glance

Figure 1: FFB's results review

FYE Mar (MYRm)	1QFY22	4QFY22	1QFY23	QoQ (%)	YoY (%)	Comments
Revenue	134.8	128.1	144.0	12.5	6.9	Thanks to robust chilled milk sales growth and new product launches
Gross profit	35.3	36.7	37.7	2.8	6.8	
Gross margin	26.2	28.6	26.2	(2.4)	(0.0)	QoQ weakness on higher raw material costs
EBIT	19.4	17.6	16.5	(6.1)	(14.8)	
EBIT Margin (%)	14.4	13.8	11.5	(2.3)	(2.9)	
Net finance costs	(3.2)	(1.5)	(2.4)	55.8	(27.1)	
EI	(0.4)	0.0	(1.5)	n.a.	n.a.	
Pretax profit	16.2	16.1	14.2	(11.9)	(12.3)	Higher S&D expenses related to school milk project
Pretax Margin (%)	12.0	12.6	9.8	(2.7)	(2.2)	
Tax	2.9	1.2	1.1	(6.5)	(60.8)	
Effective tax rate (%)	17.8	7.5	8.0	0.5	(9.8)	
Net Profit	19.2	17.7	15.2	(13.8)	(20.7)	
Core Profit	19.6	17.7	16.7	(5.4)	(14.7)	At 18% of our and consensus' forecasts
Net Margin (%)	14.6	13.8	11.6	(2.2)	(2.9)	

Source: Company data, RHB

Recommendation Chart

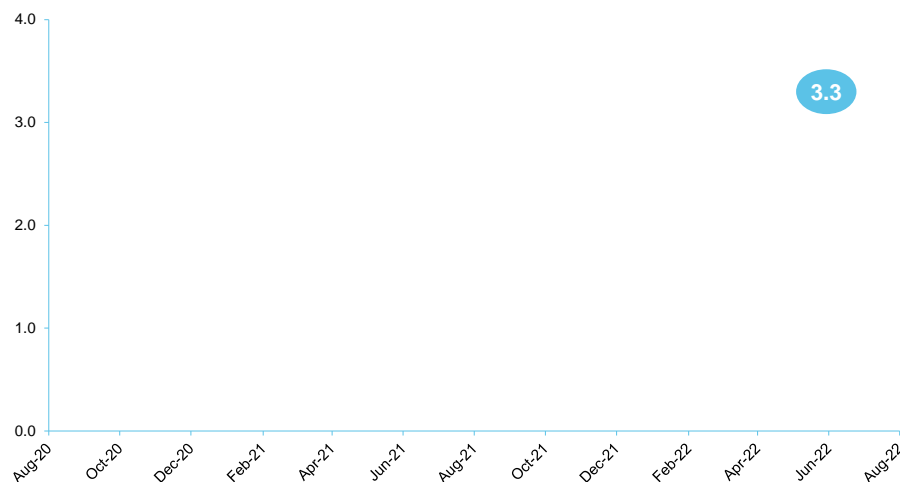


Date	Recommendation	Target Price	Price
2022-06-21	Buy	1.88	1.55

Source: RHB, Bloomberg

Source: RHB, Bloomberg

ESG Rating History



Source: RHB

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Trading Buy:	Share price may exceed 15% over the next 3 months, however longer-term outlook remains uncertain
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