FOOD EMPIRE HOLDINGS LIMITED

ACCUMULATE

Share Price:	S$0.515
Target Price:	S$0.63
Upside:	22.3%

COMPANY DESCRIPTION

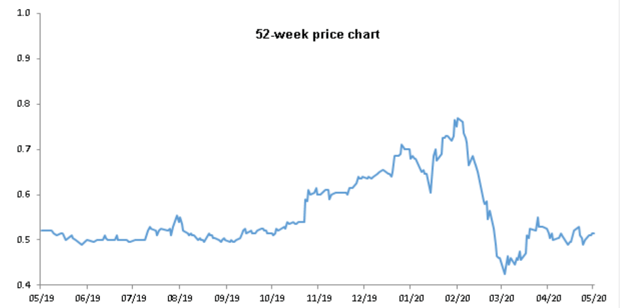
Food Empire Holdings is a global branding and manufacturing company specializing in the F&B industry. Today, Food Empire Holdings Ltd produces a wide variety of instant beverages such as regular and flavored coffee mixes and cappuccinos, chocolate drinks and flavored fruit teas. The company also markets instant cereal mixes and assorted frozen convenience foods, as well as produces and markets potato crisps.

Name	FOOD EMPIRE HOLDINGS
Bloomberg Code	FEH SP Equity
3M Avg Daily Trading Vol (k)	738.7
3M Avg Daily Trading Val ($'000)	419.3
Major Shareholder / Holdings	Anthoni Salim (24.6%) Tan Wang Cheow (22.5%)
Shares Outstanding (m)	536.5
Market Capitalisation (S$m)	276.4
52 week Share Price High/Low	S$0.765 / S$0.41

STOCK PRICE PERFORMANCE

	1M	3M	12M
Absolute Return (%)	-3.9	-30.5	2.9

PRICE CHART



Source : Bloomberg, Lim & Tan Research

Executive Summary

Despite the attractive valuations and favorable macros surrounding Food Empire Holdings, the heavy uncertainty and economic impact surrounding COVID-19 is still unable to be quantified. We believe that a second wave of infections may also be likely considering that a vaccine will need some time to be released. As such, we initiate coverage on Food Empire Holdings with a ACCUMULATE recommendation and a TP of $0.63, representing an upside potential of 22.3%. However, post COVID-19, a recovery of business conditions and confidence may plausibly warrant a future re-rating of the counter. With CEO Sudeep Nair at the helm, we like that Food Empire has successfully turned their Vietnam business around, with revenue growing at an astonishing CAGR of 59.8% within the past 6 years. The reduction of their dependence on Eastern Europe as a main source of revenue has resulted in geographical diversification as well as the discovery of a new driver of growth. With Vietnam's burgeoning middle class and soluble consumption growth being the highest at 455% amongst its ASEAN peers, we are positive on Food Empire's growth upon the return of consumer demand post COVID-19. Russia is also Food Empire's cash cow, as they command c.50% market share within Russia and the CIS markets. Both Russia and Vietnam are expected to contribute to cash flows steadily as Food Empire expands its production capacity. However, short-term volatility of the RUR/USD is to be expected due to demand and supply shocks in the oil markets as well as COVID-19's devastation of the global economy. As Food Empire turned net cash since 2017, we believe that their strong balance sheet and healthy cash flows will continue supporting them through the tumultuous COVID period. With a dividend yield of 3.9% at the current share price of S$0.515, Food Empire's current valuations of 7.4x P/E and 0.9x P/B is low with respect to that of its local and global peers. In comparison, Food Empire's peer Super Group was taken private at a P/E of c.30x in 2017. Initiate ACCUMULATE on Food Empire Holdings with a TP of $0.63.

KEY FINANCIALS

December YE	FY18	FY19	FY20F	FY21F	FY22F
Revenue (US$ mil)	284	289	245	305	322
EBITDA (US$ mil)	27.1	42.6	34.3	49.4	55.8
EBITDA Margin (%)	9.5%	14.8%	14.0%	16.2%	17.3%
Net Profit (US$ mil)	17.7	25.7	15.8	25.1	27.5
EPS (US¢)	3.4	4.9	2.9	4.7	5.1
EPS Growth (%)	36.0	44.2	-39.7	59.4	9.5
P/E (x)	10.7	7.4	12.3	7.7	7.0
P/B (x)	1.1	0.9	0.9	0.8	0.7
ROE (%)	10.1%	12.4%	7.0%	9.6%	9.6%
DPS (S¢)	0.68	2.00	0.63	1.00	1.50
Dividend Yield (%)	1.3%	3.9%	1.2%	1.9%	2.9%

Source: Food Empire, Bloomberg, Lim & Tan Research

ETHAN AW
Tel: 6533 0595
Email: ethanaw@limtan.com.sg

Vietnam as an emerging market. Between 2002 and 2018, GDP per capita grew by 270%, reaching c.USD$2,715 in 2019. The growth in foreign investments as well as education levels will help Vietnam grow its middle-class population through overall increased income per capita and hence, higher affordability. Along with the International Coffee Organisation's forecast, we believe that instant coffee will continue permeating through Vietnam's economy, supported by medium to long term macroeconomic growth factors which will benefit Food Empire as an instant coffee producer.

Vietnam to be Food Empire's next key engine of growth. Despite entering the market with premium pricing, Food Empire's Café PHO has been consistently gaining market share from incumbents such as Nescafe and Vinacafe. It has grown considerably from c.4.4% in FY15 to c.11.4% in FY19. After gradually paring losses within the first 2 years of operations in Vietnam, their profits had surged at a CAGR of 19.5% from FY15 to FY19. While we expect resilience from the instant coffee market during the global pandemic, management has indicated that footfall and general consumer purchases will invariably fall during this difficult time as unemployment rises. Post COVID-19, we expect Vietnam to continue being one of Food Empire's key revenue drivers as FEH grows its market presence within the country and takes greater market share from its competitors.

Expected stabilization of the Russian Ruble bodes well for FEH's largest market. The bulk of FEH's earnings is derived from Russia, where FEH remains a market leader with approximately 50% market share within Russia and the CIS countries. Looking ahead, we expect Russia to remain as one of FEH's largest revenue contributors at c.40% of sales. Of note, in Russian Ruble terms, FEH experienced significant 25% and 10% growth rates in 2015 and 2016 respectively. As consumer demand returns post COVID-19, we opine that the return for demand of oil will also lend stability to the Russian Ruble as its economy is highly dependent on oil. Any appreciation in the RUR/USD should result in higher margins and increased profitability.

Rewarding shareholders with dividends. With the unexpected onset of COVID-19, there is a need for companies to better conserve cash and divert resources to ensure business continuity in the midst of demand and supply chain constraints. While shareholders were rewarded with a dividend of 2 S cents per share for FY19 (representing a dividend yield of 3.9%), we believe dividend cuts will be necessary for the short term. We peg dividend payout ratios at a conservative 15% of earnings in the short term as we expect Food Empire to conserve cash, while remaining positive on the increment of dividend payouts upon the return of business confidence in the global economy.

Alignment of the goals of insiders to benefit shareholders. As of mid-March 2020, Group CEO Sudeep Nair holds a stake of 11.2% in Food Empire, while founder Tan Wang Cheow and his wife collectively own 22.52% of the company. As Sudeep has been instrumental in successfully penetrating Vietnam and accelerating the company's growth, he has shown a strong track record in delivering growth since taking over as the CEO of the company in 2012. He has also been increasing his stake via purchases of shares in the open market from 2016 to 2019. We like that this keeps the interest of management aligned with that of shareholders as this ensures their commitment towards Food Empire's continued growth.

FOOD EMPIRE HOLDINGS LIMITED

Company Background

Food Empire Holdings (FEH) is a pure-play instant coffee and tea mixes player with exposures mainly in the Russian and Vietnam markets. After successfully penetrating into the Russian market, the brand has grown from strength to strength and has built up strong brand equity and a wide distribution network.

Food Empire's products are sold to over 50 countries, in markets such as Russia, Ukraine, Kazakhstan, Central Asia, China, Indochina, the Middle East, Mongolia and the US. The Group has 23 offices worldwide and operates 7 manufacturing facilities in Malaysia, India, Vietnam, Russia and Ukraine.

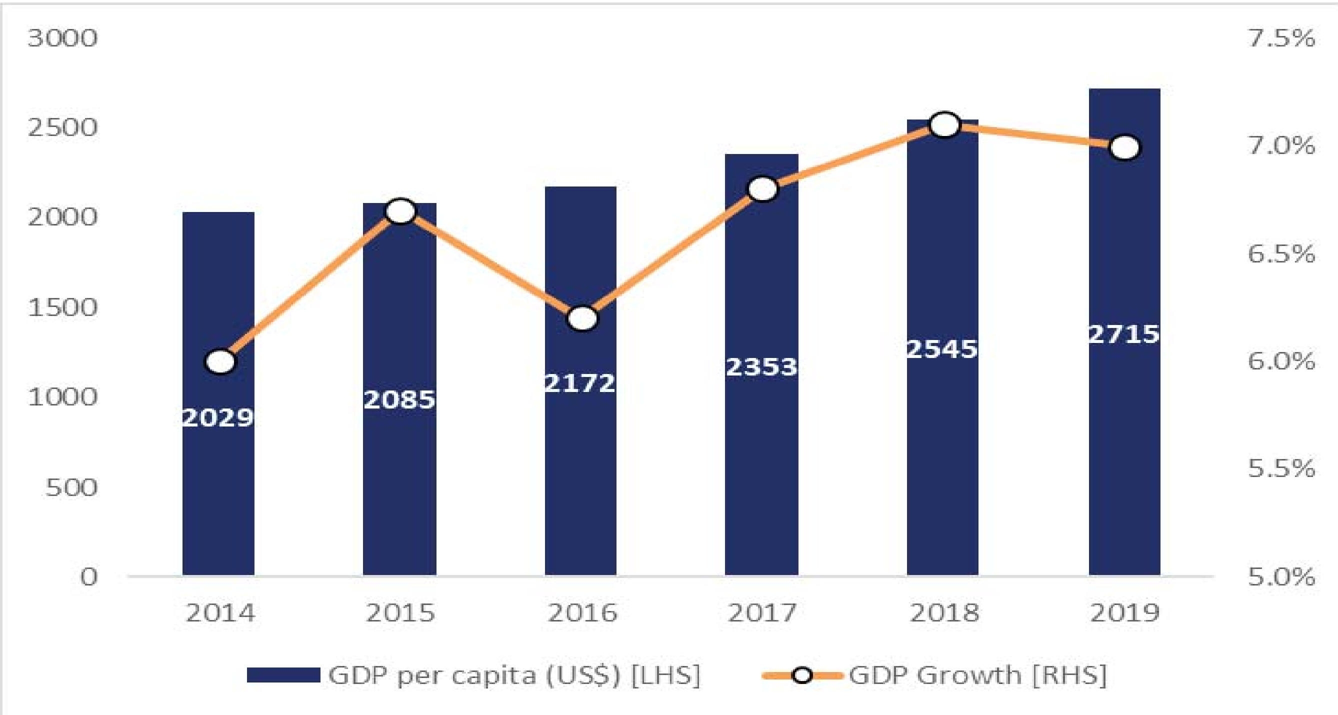
Food Empire's strength lies in its proprietary brands – including MacCoffee, Café PHO, Petrovskaya Sloboda, Klassno, Kracks and OrienBites. MacCoffee – the Group's flagship brand – has been consistently ranked as the leading 3-in-1 instant coffee brand in the Group's core market of Russia, Ukraine and Vietnam. The Group employs sophisticated brand building activities, localised to match the flavour of the local markets in which its products are sold.

Since its public listing in 2000, Food Empire has won numerous accolades and awards including being recognised as one of the "Most Valuable Singapore Brands" by IE Singapore (now known as Enterprise Singapore), while MacCoffee has been ranked as one of "The Strongest Singapore Brands". Forbes Magazine has twice named Food Empire as one of the "Best under a Billion" companies in Asia and the company has been awarded one of Asia's "Top Brand" by Influential Brands. Food Empire was also presented with the Sustainability Award at the SIAS 20th Investors' Choice Award in Singapore.

Investment Merits

Vietnam as an emerging market. Since 1986, economic and political reforms enacted have changed Vietnam's economy drastically. From being one of the world's poorest nations, it has so far transformed into a lower-middle income country. Between 2002 and 2018, GDP per capita grew by 270%, reaching c.USD$2,715 in 2019. In that tim, Poverty rates have also sharply declined from 70% to 6%. From 2014 to 2019, Vietnam has also been experiencing strong GDP growth of above 6.0% per annum, achieving a 10 year high of 7.1% in 2018.

Exhibit 1: Vietnam GDP Per Capita vs GDP Growth



Source: FocusEconomics, General Statistics Office of Vietnam, CEIC, LTS Research

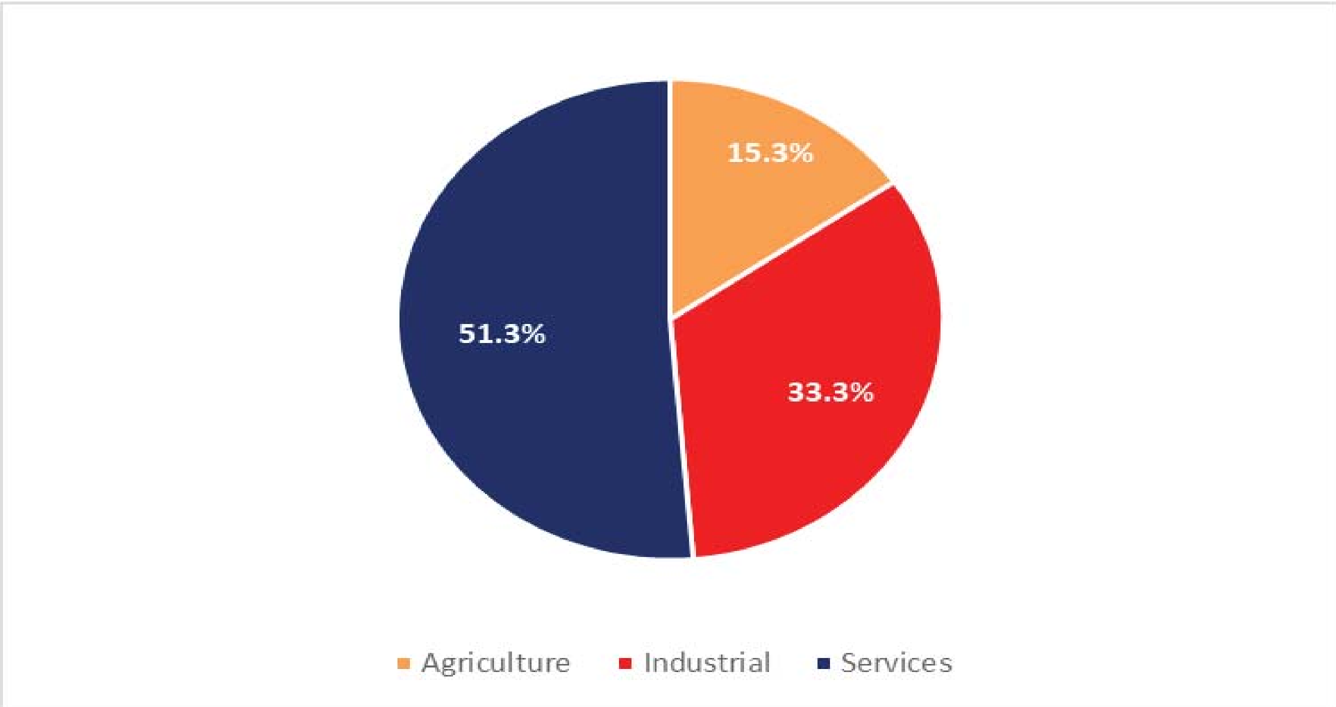
According to the World Bank, c.70% of Vietnam's population is under 35 years old, which means that a large proportion of its people will have the ability to upgrade their skills and drive the economy. Its people have a life expectancy of 76 years, the highest amongst countries in the region with comparable income levels. Vietnam's emerging middle class currently accounts for c.13% of the population, and this is expected to rise to 26% by 2026.

FOOD EMPIRE HOLDINGS LIMITED

In terms of general education, Vietnam spent approximately 6% of its GDP on education, which is high by global standards. Educational reforms have also better enabled students by placing greater emphasis on English. We believe that as its workforce becomes increasingly educated, income per capita will grow accordingly, bringing about higher spending power.

As companies seek to diversify their sources of production, many have been setting up their manufacturing facilities in Vietnam as a means of reducing reliance on China. One prominent example is Samsung, which shifted a large part of its supply chain due to the US-China trade war. This has led to an increase in the number of jobs and transference of technological know-hows, which will also fuel the advancement of Vietnam's income per capita. As of 2017, industrial manufacturing and service-based businesses contributed to c.84.6% of Vietnam's GDP, as opposed to agriculture's 15.3% contribution. In our opinion, it is highly reminiscent of China's growth as an emerging market when they opened up their economy to foreign investments, resulting in the shift from an agrarian-based economy since the 1970s to one centered around manufacturing and services today.

Exhibit 2: Vietnam 2017 GDP Composition



Source: US CIA, LTS Research

Despite the ill-effects of COVID-19, we expect FEH to continue benefiting from Vietnam's growth in the medium to long term. As of 2019, consumption constitutes c.70% of Vietnam's GDP, one of the highest by global standards. A burgeoning middle and upper class would result in increased affordability, and the resulting busy lifestyles are likely to boost instant coffee spending as a means of having quick access to coffee. Instant coffee producers have also been improving aroma recovery processes over time, closing the gap between flavors of instant coffee versus that of brewed coffee. Over time, we believe that instant coffee will continue penetrating Vietnam's market, supported by aforementioned medium to long term macroeconomic growth factors which we opine will benefit FEH's standing as an instant coffee producer.

Vietnam to be Food Empire's next key engine of growth. Since economic liberalization, Vietnam gradually became the world's second largest producer (after Brazil) and exporter of coffee (US$3.3bln in FY18, 10.5% of total coffee exports). The industry has grown tremendously, alongside population growth. The overall uplift in the coffee market has invariably led to the growth of the instant coffee market as well.

Unbeknownst to most, Vietnam has a strong coffee culture. This began since the French (who were rulers of Vietnam previously) were very inclined towards coffee, and the culture has remained ever since. Vietnam is famous for their Robusta coffee beans, as their weather conditions are highly favorable for them, resulting in c.97% of coffee plantations being of the Robusta variety. We believe that the strong coffee culture will fuel FEH's growth as they continue appealing to the taste buds of the local populace.

According to the International Coffee Organisation, in 2017, 44% of the coffee consumed in the region was in soluble form. They've also mentioned that soluble coffee is still gaining market share in Vietnam, alongside fresh coffee. Amongst its peers, Vietnam has had the largest percentage change in soluble coffee consumption per capita between 2003 and 2017 at 344%, compared to the average of 156%. This lends support to Vietnam's strong coffee culture as well as why we are bullish on Vietnam being FEH's next engine of growth.

Exhibit 3: SEA % Change In Soluble Coffee Consumption 2003 – 2017

Country	% change in soluble coffee consumption 2003 - 2017	% change in soluble coffee consumption per capita 2013 - 2017
Taiwan	-31	-40
Indonesia	279	204
Vietnam	455	344
India	220	143
South Korea	2	-12
China	372	317
Philippines	229	137
Average	**218**	**156**

Source: International Coffee Organisation, Euromonitor International, LTS Research

FEH first entered the Vietnam market around 2012, with their key product MacCoffee - Café PHO. With confidence in its quality, and to make known their standing within the instant coffee marketplace, FEH priced it at a premium to ensure it would be profitable as soon as possible.

Despite entering the market with premium pricing, Café PHO has consistently been gaining market share over the last 5 years from c.4.4% in FY15 to c.11.4% in FY19. This shows that Café PHO had successfully appealed to the tastes of its local consumers, and had been performing well even though the marketplace was saturated with incumbents. This success came in spite of FEH raising the price of Café PHO 3 times in 6 years, and that incumbents have released similar products at lower price points, but failed to suppress Café PHO's growth.

Exhibit 4: Market Shares Of VN's Instant Coffee Producers

Vietnam's 3-in-1 Market Share	FY15	FY16	FY17	FY18	FY19
MacCoffee (Café PHO)	4.4%	6.6%	8.6%	9.1%	11.4%
Nescafe	20.0%	20.3%	20.5%	19.8%	17.9%
Vinacafe	19.2%	19.3%	17.7%	15.0%	14.6%
G7	14.3%	13.2%	13.9%	13.8%	13.8%
Wakeup	18.9%	18.0%	15.9%	14.1%	13.7%
Tran Quang	11.6%	11.9%	13.2%	17.6%	15.7%
Total	**88.9%**	**89.9%**	**90.5%**	**91.1%**	**91.2%**

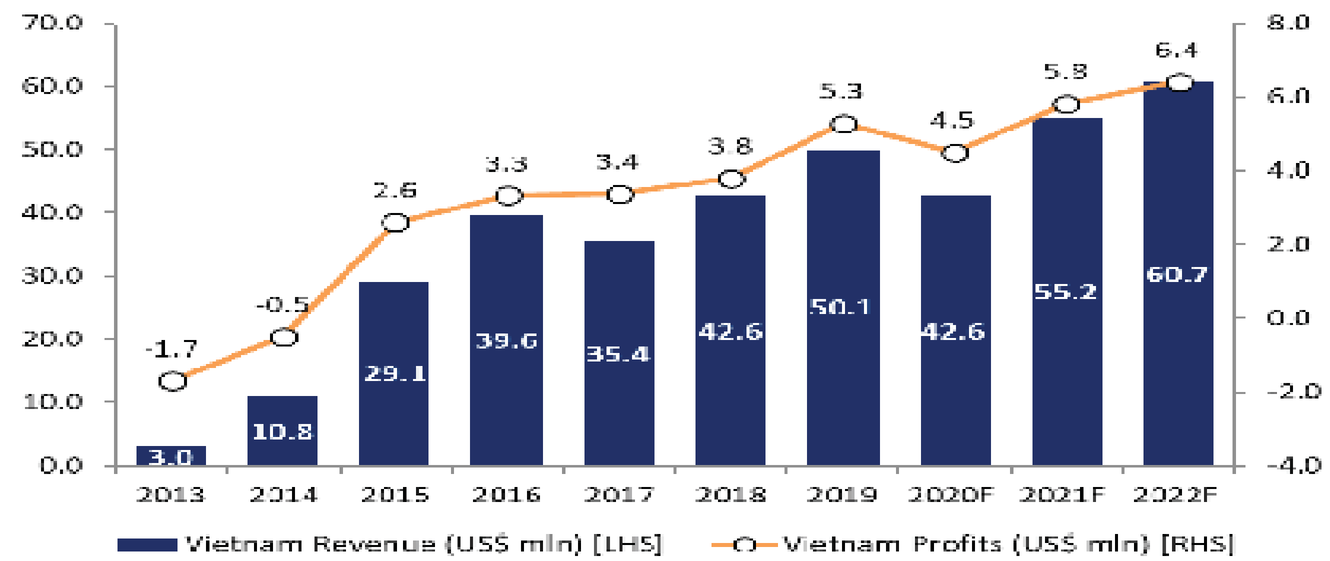
Source: Food Empire, LTS Research

Exhibit 5: Estimations Of Vietnam's Instant Coffee Prices

Source: Food Empire, LTS Research

From a low revenue base of USD 3mil in 2013, FEH's Vietnam sales had surged to USD 50.1mil in 2019, representing a CAGR of 59.8%. After quickly reducing losses within its first 2 years of penetrating Vietnam's instant coffee market, its profits had grown at a CAGR of 19.5% from 2015 to 2019. Post COVID-19, we expect profit to be in the range of US$4.5 mln and US$5.8 mln for 2020F and 2021F respectively. We also expect resilience during these challenging times as consumers are made to stay home. Instant coffee can be purchased and stored at home for long periods, unlike that of fresh coffee. However, FEH's management has indicated that most of its factories have been affected by lockdown measures which brought about supply chain constraints. Footfall at shops will also decline as people remain at home. Hence, we ascribe a conservative 15% fall in Vietnam's sales for FY20.

Exhibit 6: Food Empire VN Revenue vs Profits 2013 – 2022F



Source: Food Empire, LTS Research

Aside from the name "PHO" which resonates within locals, FEH has also done well in marketing by promoting the visibilities of their products. Instead of targeting modern trade channels (i.e. supermarkets), FEH recognized that value came from traditional markets. Hence, salesmen were hired to push for product placements in sundry shops, and strings of Café PHO sachets were given out to be prominently hung outside the store front. As inner retail space in sundry shops were small, motorists would often stop outside storefronts and 'order' products from store owners, and the "free" visibility of Café PHO helped largely with sales. We've noted that customers usually buy 3-5 chains of sachets per store visit and that usually 30 chains (1/2 box) are restocked on a weekly basis.

Today, FEH sells wholesale to 135 distributors spread across entire Vietnam and employs 540 salesmen who perform weekly stock and visibility checks to ensure products are prominently placed. We like that FEH had successfully recognized the value in unconventional marketing within Vietnam and we believe that while existing customers will remain loyal to Café PHO, new customers will also be enticed to try them. This will likely, in our opinion, continue cementing FEH's standing in Vietnam's instant coffee market.

Exhibit 7: Visibility Of FEH's Products In Vietnam's Store Fronts

Source: LTS Research

Since the outbreak of COVID-19, Vietnam was one of the earliest countries to implement border controls in January, especially due to their close proximity to China. Large-scale quarantine measures have also resulted in a reduction in reported daily new cases since early April. With only 320 confirmed COVID-19 infections, the Vietnamese government began easing measures, allowing domestic travel to take place. Based on management's guidance, sales for April and May have remained resilient, and are still expecting Vietnam to be their next engine of growth post COVID. We believe that this will lend support to consumerism, and therefore FEH's Vietnam sales in this period.

Potential stabilization of the Russian Ruble bodes well for Food Empire. The bulk of FEH's earnings is derived from Russia, where FEH remains a market leader with approximately 50% market share within Russia and the CIS countries. Before the Ruble's depreciation in 2014-2015, c.60% of FEH's sales were derived from Russia. In recent years, Russia has only contributed to c.40% of its revenue, but still remains FEH's biggest market.

In mid-2014, the Russian Ruble took a nosedive as investors lost confidence in the currency due to 2 key factors. Firstly, there was a huge dip in the oil prices due to the advent of shale oil production in the US. From 0.4 million barrels per day (bpd) in 2007, production levels had starkly increased to 8.8 million bpd in 2014. Coupled with the US' reduced reliance on foreign oil imports and Europe's lower demand, this resulted in an overall fall in demand with increased global supply levels. As exports of crude oil and related products made up more than 60% of Russia's total exports as well as more than half of their governmental revenue, demand for Russia's currency is highly sensitive to oil prices. It brought about a lack of investor confidence in the Russian economy, and therefore the subsequent sell-off in Russian assets.

Secondly, economic sanctions were placed on Russia as a result of their invasion of Ukraine. This made it difficult for Russian companies to refinance their debt as many of them were borrowing from foreign capital markets. Foreign banks were also unwilling to lend to these companies due to the instability of the Russian economy at the time. Those that were willing to lend demanded exorbitant interest rates as a means of mitigating risk. In spite of the government's decision to hike interest rates by 6.5% to 17%, it was not enough to cushion the falling Ruble.

Exhibit 8: Russian Ruble vs US Dollar 10Y Price Chart

Source: Bloomberg, LTS Research

With the collapse of the RUR/USD, it resulted in a distortion since FEH reports its results in USD. Of note, in Russian Ruble terms, FEH experienced significant 25% and 10% growth rates in 2015 and 2016 respectively. Barring the fluctuations of the RUR/USD, we would have seen FEH's Russia segment grow steadily at an average of 6% per annum instead of -3% in USD terms between 2015-2019.

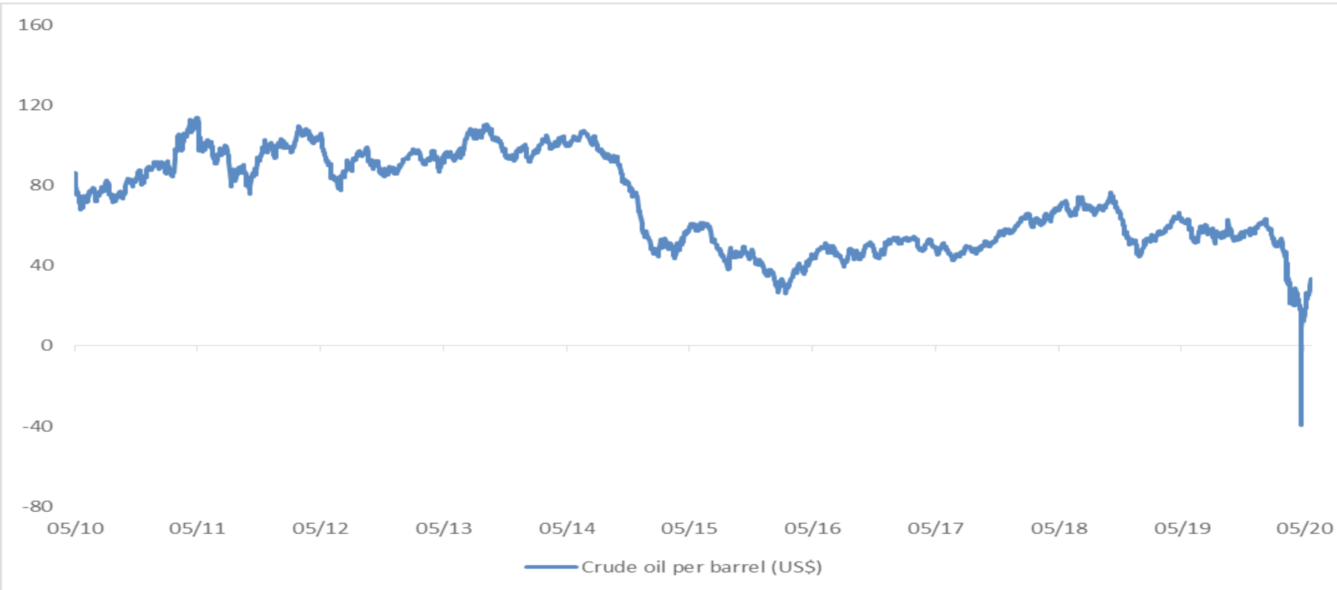
Exhibit 9: FEH Russia Revenue Comparisons In RUR vs USD

Revenue comparison	2014	2015	2016	2017	2018	2019
Russia Revenue in RUR mln	5278.2	6571.8	7228.2	6808.4	7115.4	7035.6
% increase / (decrease)		*25%*	*10%*	*-6%*	*5%*	*-1%*
Russia Revenue in USD mln	136.7	107.3	107.9	116.7	113.3	112.6
% increase / (decrease)		*-22%*	*1%*	*8%*	*-3%*	*-1%*

Source: Food Empire, LTS Research, Bloomberg

As an incumbent in Russia, the business is now a cash-cow for FEH and we expect its Russian business to grow at c.5% per annum, with gross margins remaining steady at c.38% moving forward. Marketing expenses are also tied to revenue at c.15% as of FY19, with marketing expenses to be reduced in the absence of further growth. We like that the Russian instant coffee market has a medium-high barrier to entry due to its fair split between modern (e.g. supermarkets) and traditional distribution channels (e.g. small retailers). New entrants will need to focus on both modern and traditional trades, which will require huge financial prowess. Time will also be required to build up brand equity. As the instant coffee market remains their consumers' first choice compared to ground coffee, we believe that FEH will continue benefiting from Russia with a stronghold in the instant coffee market in the long run.

Exhibit 10: Crude Oil 10Y Price Chart



Source: Bloomberg, LTS Research

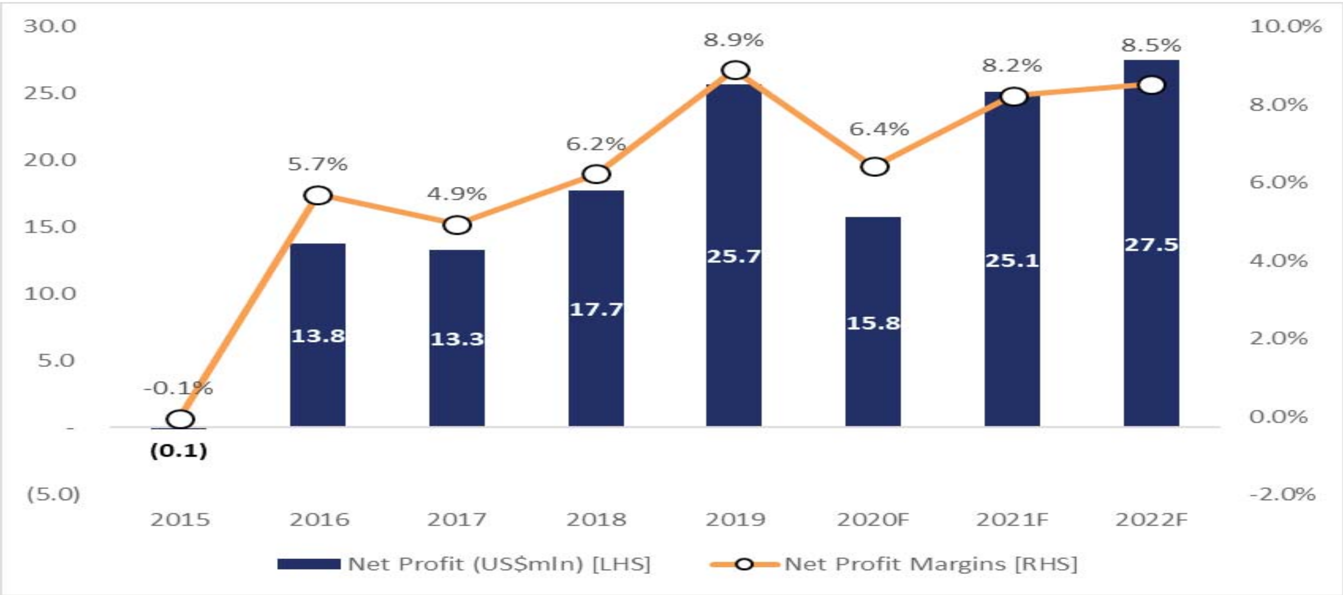
Even though the COVID-19 pandemic had led to both a demand and supply shock in the oil markets, the RUR/USD remained range-bound, still above its 10Y low of 0.0117. Looking ahead, as the OPEC+ alliance had agreed to a 2-year production cut with reductions to taper over time, we expect oil prices to maintain range-bound as well in the near term. However, plausible volatility of oil prices must also be taken into consideration, along with the effects it will have on the RUR/USD. Cities such as Moscow and Saratov have placed bans on simple outdoor activities such as taking walks or exercising. Along with the rising number of COVID-19 cases by the thousands on a daily basis, we expect the restrictive measures to place strain on consumption in the short-term.

As consumer demand returns post COVID-19, we opine that oil prices should gradually increase albeit at a slow pace, barring any unforeseen circumstances. This should lend stability to the RUR/USD, and any appreciation of the Ruble would lead to higher margins and therefore increased profitability. We also expect Russia to remain as one of FEH's largest revenue contributors at c.40% of sales.

Prudence in cost rationalization allows Food Empire to better control operating costs. In 2012, after Sudeep Nair had been promoted to the role of CEO, he initiated FEH's foray into three key ASEAN markets as a means of diversifying their revenue streams – Myanmar, Vietnam and Philippines. While Vietnam has become a successful turnaround story, and Philippines is still a work-in-progress, FEH had decided to exit the Myanmar market due to unfavorable business conditions. According to management, they were greatly affected by the devaluation of the MMK/USD as well as the inability to raise prices to maintain margins. Several companies had continued to operate at low or negative margins in a bid to wait for prices to readjust.

Their stemming of losses had resulted in a growth in net profit margin from 6.2% in FY18 to 8.9% in FY19. We remain confident in FEH's ability to prudently control operating costs where necessary. Along with management's guidance, we expect COVID-19 to present headwinds as long as the global economy remains unstable. They have also indicated in their latest 1Q20 business update that their financial results for Russia, Ukraine and CIS markets to be negatively impacted in 2Q20 due to lower sales volumes linked to pandemic containment efforts and currency depreciation. As such, we have ascribed a 15% fall in sales to these markets. We also conservatively peg our profit margin forecasts to 6.4% for FY20F, with expectations of an uptrend upon return of stable consumer demand.

Exhibit 11: Group NPAT vs NPAT Margins 2015 – 2022F



Source: Food Empire, LTS Research

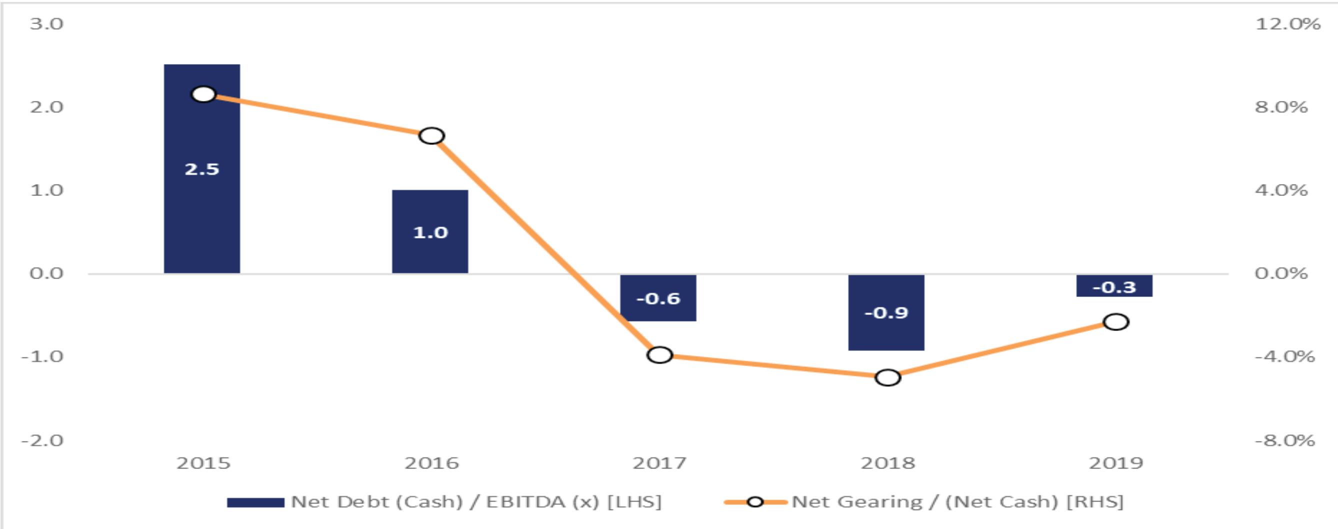
Expanding factory capabilities to cater to demand. In spite of FEH's Vietnam factory running for 24hours / day for 6 days with 3 different shifts, utilization rate has inched higher with the consistently growing demand for Café PHO pre COVID-19. They are being shipped out in under 48 hours. To cater to this growth, FEH plans to ramp up production capacity with new automated machines. Based on management's guidance, these machines were supposed to be ready within 6-9 months, and will be able to increase production volume by c.300-400%. It will help to further save costs through operating efficiency. Further, labor costs currently remain low and do not serve as a threat to FEH's cost structure. Post COVID-19, we opine that as business confidence returns, FEH will continue with the construction of the automated machines to meet demand.

A second instant coffee factory is also expected to be built in India, at a cost of c.US$50mln and US$4mln annual depreciation and operations to fully ramp up by FY21. Commencement of operations were supposed to begin in 2H20. However, management has recently guided in their 1Q20 business update that its construction will experience delays until international travel restrictions are lifted as they require OEM suppliers to test and commission the plant.

Lastly, following the success of FEH's fully utilized first Non-Dairy Creamer (NDC) plant, they have also decided to embark on their second NDC project in the same location in Malaysia with an estimated cost of c.US$25mln. The plant was initially expected to be completed within 2 years and commence commercial production starting FY2022. Upon completion, it will double their current NDC capacity and enable the Group to enlarge its B2B customer based by providing more customized and value-added products. However, in light of the current situation, we think that delays are to be expected for the construction both plants and automated machines.

Strong balance sheet and healthy cash flows. As FEH diligently managed operating costs while growing their profitable business segments, the company turned net cash as of FY17. This gives credence to the business' profit generating abilities. Recently, their net cash position fell slightly as a result of increased debt levels from US$33.5mln in FY18 to US$50mln in FY19, due to the drawdown of a loan for their subsidiary Indus Coffee. Moving forward, management does not expect any major CAPEX to occur over the next 2 to 3 years aside from those mentioned above. We anticipate that the prolonging of COVID-19 may require FEH to take up loans to bolster their working capital needs in the short term, but net gearing should continue falling once business returns to normalized levels.

Exhibit 12: Net Debt / EBITDA vs Net Gearing 2015 - 2019

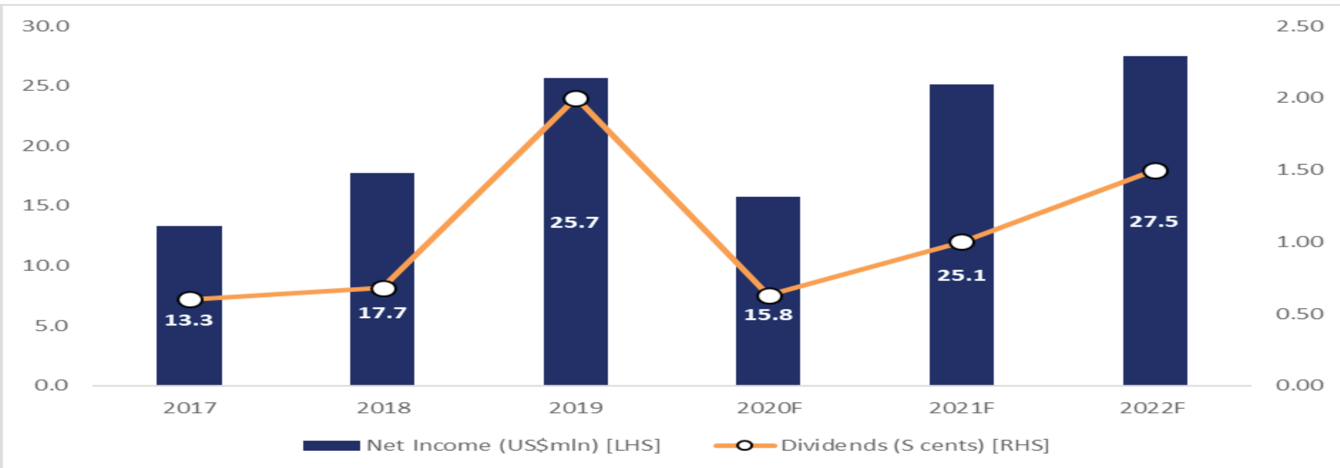


Source: Food Empire, LTS Research

Rewarding shareholders with dividends. As of FY19, FEH has no formal dividend policy. In early 2020, management had indicated that they intended to declare a dividend policy to reward shareholders. However, due to the impact of COVID-19, we understand that they have shifted their focus towards overcoming the current challenges this pandemic presents instead. We opine that once the situation abates and consumer demand returns, it is likely that management will possibly introduce a dividend policy then.

Previously, dividend payout ratios ranged between 10-20%. In contrast, before the COVID-19 outbreak, management had decided to reward shareholders with a dividend of 2 S cents per share for FY19, representing a dividend payout ratio of 28.6%. We believe that in good times, management will duly reward shareholders where possible. As such, we peg dividend payout ratios at a conservative 15% in the short term as a means of cash conservation for FEH, while remaining positive on the increment of dividend payouts upon the return of business confidence in the global economy.

Exhibit 13: Net Income vs Dividends 2017 – 2022F



Source: Food Empire, LTS Research

Insiders' goals are aligned with that of shareholders. Since 2016, Group CEO Sudeep Nair has been consistently repurchasing shares from the open market. From 2016 to 2019, he has purchased a total of c.20.5 million shares at an average of $0.54, bringing his total stake to c.11.20% as of FY19. While this keeps his interests aligned with that of the shareholders, it also shows his confidence in the growth of FEH. We note that other key personnel such as founder Tan Wang Cheow and his wife Tan Guek Ming also hold significant stakes in the company as major shareholders. In 2018, Non-Executive Director Tan Guek Ming purchased a total 827,200 shares at an average price of $0.65. Other directors such as Lew Syn Pau have also been increasing their stakes via exercising share options that they were previously granted.

In comparison to what the insiders have paid, we think that the current share price of $0.515 is relatively inexpensive along with the attractive valuations. Overall, we like that insiders have been increasing their stakes in FEH as this will ensure that they continuously drive FEH's growth for the benefit of all shareholders.

Exhibit 14: Insider Open Market Purchases Table (Estimated)

Summary of Insiders' Open Market Purchases [Estimated]				
Year	Name	Shares purchased	Value (S$)	Average price / share (S$)
2016	Sudeep Nair	1,558,400	548,713	0.35
2016	Sudeep Nair	1,350,000	544,185	0.40
2016	Sudeep Nair	2,500,000	1,042,250	0.42
2016	Sudeep Nair	2,500,000	1,080,000	0.43
2017	Sudeep Nair	824,200	465,591	0.56
2017	Sudeep Nair	3,175,800	1,847,680	0.58
2017	Sudeep Nair	2,800,000	1,830,920	0.65
2017	Sudeep Nair	813,800	535,155	0.66
2018	Sudeep Nair	511,500	351,861	0.69
2018	Sudeep Nair	963,400	658,031	0.68
2018	Sudeep Nair	598,200	413,356	0.69
2018	Sudeep Nair	1,394,700	972,803	0.70
2018	Tan Guek Ming	50,000	33,210	0.66
2018	Tan Guek Ming	50,000	32,990	0.66
2018	Tan Guek Ming	100,000	66,320	0.66
2018	Tan Guek Ming	195,100	130,288	0.67
2018	Tan Guek Ming	200,000	133,420	0.67
2018	Tan Guek Ming	200,000	131,140	0.66
2018	Tan Guek Ming	14,500	7,830	0.54
2018	Tan Guek Ming	17,600	9,504	0.54
2019	Sudeep Nair	1,340,700	750,658	0.56
2019	Sudeep Nair	230,800	138,226	0.60
Total		**21,338,700**	**11,702,631**	**0.59 (average)**

Source: Food Empire, SGX, LTS Research

Exhibit 15: Shareholders' Statistics

Substantial Shareholders as of 16 March 2020	Position	Direct Interest	%	Deemed Interest	%
Tan Wang Cheow	Executive Chairman & Founder	–	–	120,814,600	22.52
Tan Guek Ming	Non-Executive Director	37,547,400	7.00	83,267,200	15.52
Sudeep Nair	Group CEO and Excecutive Director	1,300,000	0.24	60,076,399	11.20
Anthoni Salim	–	–	–	132,079,200	24.62
FMR LLC & FIL LTD on behalf of their managed accounts of direct and indirect subsidaries	–	–	–	47,387,800	8.83

Source: Food Empire, LTS Research

Valuations

- **Highly undervalued due to lack of market visibility.** As FEH is a small-cap counter with a lack of coverage, we think that it is severely undervalued by the market compared to both local and global peers. FEH trades at the lowest of 7.4x P/E and 6.9x EV / EBITDA compared to the local peer average of 16.2x and 10.1x respectively. In terms of dividend yield, it is at the highest of 3.9%, compared to the peer average of 3.2%. Negative sentiments will likely continue to depress valuations for FEH and its peers, especially due to uncertainty revolving around the global economy. However, as aforementioned, we expect FEH to continue performing well upon the return of business confidence. We conservatively peg our TP to 9.0x P/E, representing a 44.4% discount to the local peer average P/E of 16.2x, and a potential upside of 22.3% from the current share price of S$0.515. Should FEH gain greater investor interest over time, increased coverage and greater geographical diversification, we believe that it this will warrant an upward re-rating of the counter by the market.

  Super Group, a Singaporean firm that became a household brand for 3-in-1 coffee mixes, was successfully acquired by Jacobs Douwe Egberts (JDE) in 2017 at 30x P/E and 2.7x book value. The offer of $1.30 per share also represented a 62.5% premium to Super Group's share price of S$0.80 on October 4th 2016, before Super was queried by SGX over its trading activity. Similar to FEH, Super Group had a large portfolio of c.160 products, distributed in over 65 countries and 15 factories at the time of acquisition. This reinforces our belief that FEH is greatly undervalued by the market even when its business is successfully growing, with the company intending to further expand production output to meet demand needs.

Exhibit 16: Peer Comparison Table

Company	Market Cap (mln)	P/E (x)	Forward P/E (x)	P/B (x)	EV to TTM EBITDA (x)	Currency	Dividend Yield
Singapore Peers							
FOOD EMPIRE HOLDINGS LTD	276	7.4	12.3	0.9	6.9	SGD	3.9%
YEO HIAP SENG LTD	484	27.4	NA	0.8	7.8	SGD	2.4%
THAI BEVERAGE PCL	16,576	15.8	16.3	2.8	14.4	SGD	2.9%
FRASER AND NEAVE LTD	2,131	14.3	NA	0.7	11.4	SGD	3.7%
Average		**16.2**	**14.3**	**1.3**	**10.1**		**3.2%**
Global Peers							
NESTLE (MALAYSIA) BERHAD	10,594	52.2	50.1	38.0	31.9	MYR	2.0%
COCA-COLA AMATIL LTD	5,761	16.9	19.1	4.0	10.8	AUD	5.5%
FRASER & NEAVE HOLDINGS BHD	3,823	28.4	28.3	4.5	17.3	MYR	1.9%
COCA-COLA CONSOLIDATED INC	3,095	27.5	24.9	6.1	7.8	USD	0.4%
DYDO DRINCO	1,073	45.6	NA	0.9	4.5	JPY	NA
KEY COFFEE INC	690	68.2	NA	1.5	25.4	JPY	0.8%
HEY SONG CORP	605	16.2	NA	0.7	15.6	TWD	5.3%
POWER ROOT BHD	298	20.5	18.8	3.4	14.4	MYR	3.6%
UNICAFE INC	173	NA	NA	1.6	18.1	JPY	NA
TSIT WING INTERNATIONAL HOLD	129	8.2	NA	1.3	3.9	HKD	7.1%
TAC CONSUMER PCL	115	15.6	15.8	3.7	9.5	THB	3.3%
OLDTOWN BHD	NA	NA	NA	NA	14.5	MYR	NA
SUPERGROUP	NA	NA	NA	NA	9.8	EUR	NA
VINACAFE BIEN HOA JSC	340	8.2	NA	3.6	6.0	VND	11.4%
Average		**27.9**	**26.1**	**5.8**	**13.5**		**4.1%**

Source: Bloomberg, LTS Research

Risk Factors

- **FEH's reliance on natural hedging.** Traditionally, FEH has relied on natural hedging as a means of protecting themselves against foreign exchange volatility. However, as of FY19, FEH had a natural hedging ratio of 54.8% vs 66.4% in 2018. This means that only 54.8% of FEH's purchases and operating costs are denominated in the functional currencies of their operating units, which exposes them to the vagaries of the foreign exchange markets. In the most recent financial year, they've had the greatest exposure to the Malaysian Ringgit, Russian Ruble and Indian Rupee. Political risk arising from disputes such as the UK's departure from the EU or Russia's invasion of Ukraine could potentially have adverse effects of their currencies. On the same note, as this is the first global pandemic the world has faced since the Spanish Flu, this presents risk of currency destabilization should any country be severely affected. Management has guided that hedging costs in key markets such as Russia and Ukraine are high due to the hefty premiums charged by counterparties. As such, they have continued undertaking natural hedging as they have determined that the benefits of currency hedging do not outweigh the costs it presents. Although management has indicated that they will consider undertaking appropriate hedging measures if necessary, we advise investors to be cognizant of the forex risk present to FEH's bottom line especially in tumultuous times.

Exhibit 17: Sensitivity Analysis For Foreign Currency Risk On Profit Before Tax

		2018 US$'000	2019 US$'000
EURO/USD	strengthened 5% (2018: 5%)	471	53
	weakened 5% (2018: 5%)	-471	-53
RM/USD	strengthened 5% (2018: 5%)	54	265
	weakened 5% (2018: 5%)	-54	-265
UAH/USD	strengthened 5% (2018: 5%)	225	52
	weakened 5% (2018: 5%)	-225	-52
RUR/USD	strengthened 5% (2018: 5%)	348	198
	weakened 5% (2018: 5%)	-348	-198
INR/USD	strengthened 5% (2018: 5%)	291	234
	weakened 5% (2018: 5%)	-291	-234

Source: Food Empire, LTS Research

COVID-19's continued destruction on the global economy. As COVID-19 ravages through the global economy, its effects have yet to be quantified by any measure. Demand for discretionary items have fallen drastically while supply chains have been disrupted due to lockdown measures, affecting both consumers and businesses. As businesses have either started filing for bankruptcy or cut costs via retrenchments, general consumer purchases will most likely tighten, and consumers will begin flocking towards non-discretionary items in a bid to save money in times of uncertainty. Unfortunately, as aforementioned, FEH's factories have also been affected by their respective countries' lockdown measures which gave way to supply chain constraints. Management has acknowledged that both their top and bottom lines will be affected in the short run. Their first instant coffee plant in India is facing production and logistical challenges as the plant is located in a designated COVID-19 red zone.

Vaccines generally require 1.5 to 2 years to be released as they require extensive trials to ensure that mutations of the underlying virus do not occur. As such, we do not expect the situation to abate so soon. The global economy is expected to continue facing headwinds unless either a vaccine has been produced, or if the majority of the world has achieved herd immunity.

However, we hold the view that the demand for instant coffee should remain resilient compared to that of the broader market, given that it is easily accessible via both large and small retailers and can be stored at home for long periods of time. They are also much easier and inexpensive to make compared to having to brew coffee using coffee grounds. Similarly, coffee has become embedded in our daily lives such that it has become a habitual drink, with demand being relatively sticky. Upon the ease of the lockdown measures, we expect the retail industry to be one of the first to benefit via pent-up demand.

RESEARCH DISCLAIMER

This report is intended for clients of Lim & Tan Securities Pte Ltd [herein after termed as LTS] only and no part of this document may be –

i. Copied, photocopied, duplicated, stored or reproduced in any form by any means or

ii. Re-distributed or disseminated, directly or indirectly, to any other person in whole or in part, for any purpose without the prior consent of LTS.

This research report is prepared for general circulation. It does not have regard to the specific investment objectives, financial situation and particular needs of any specific recipient of this research report. You should independently evaluate particular investments and consult your independent financial adviser before making any investments or entering into any transaction in relation to any securities or investment instruments mentioned in this report.

The information, tools and material presented herein this report are not directed at, or intended for distribution to or use by, any person or entity who is a citizen or resident of or located in any jurisdiction where such distribution, publication, availability or use would be contrary to applicable law or regulation or which would subject LTS to any registration or licensing requirement within such jurisdiction.

The information and opinions presented in this research report have been obtained or derived from sources believed by LTS to be reliable. Their accuracy, completeness or correctness is, however, not guaranteed. Opinions and views expressed in this report are subject to change without notice, and no part of this publication is to be construed as an offer, or solicitation of an offer to buy or sell securities, futures, options or other financial instruments or to provide investment advice or services. Therefore, LTS accepts no liability for loss arising from the use of the material presented in this report where permitted by law and/or regulation. LTS may have issued other reports that are inconsistent with the assumptions, views and analytical methods of the analysts who prepared them.

LTS, its directors, its connected persons and employees may, from time to time, own or have positions in any of the securities mentioned or referred to in this report or any securities related thereto and may from time to time add to or dispose of or may be materially interested in any such securities. LTS's research analysts are primarily responsible for the content of this report, in part or in whole, and certifies that the views about the companies expressed in this report accurately reflect his personal views. LTS prohibits the research analysts who prepares this report from receiving any compensation (excluding salary and bonuses) or other incentives and benefits receivable in respect of this report or for providing specific recommendation for, or in view of a particular company or companies mentioned in this report.

LTS-SPECIFIC / REGULATORY DISCLOSURE

1. LTS does not have a proprietary position in the company / companies as recommended in this report as at the close of 26/05/2020.

2. The research analysts do not hold *interests in the company / companies as recommended in this report as at the close of 26/05/2020.

* *Includes direct or indirect ownership of securities or Futures Contracts (excluding the amount of securities or Futures Contracts owned), directorships or trustee positions.*