

17 January 2020

Consumer Non-cyclicals | Food & Beverage Products

Food Empire (FEH SP)

Buy (Maintained)

Sipping Vietnam's Coffee Culture; Still BUY

Target Price (Return) SGD0.83 (+18%)
 Price: SGD0.71
 Market Cap: USD281m
 Avg Daily Turnover (SGD/USD) 0.30m/0.22m

- **Maintain BUY and SGD0.83 TP**, 18% upside plus c.2% yield. Visiting Food Empire's second largest market, Vietnam, early this week, we witnessed the high visibility of its *Café Pho* products vis-à-vis its competitors in Ho Chi Minh City. With an extensive network of sales representatives and a strong marketing team, we believe *Café Pho* should be able to grow its market share, while revenue and margins could be further improved with the increased penetration of new products.

- **Success of the Vietnam market.** Vietnam is Food Empire's second-largest market, contributing c.20% to topline. While the group has been in Vietnam since 1993, the business only took off after it introduced *Café Pho*, a premium 3-in-1 ice coffee mix in 2013. The business turned profitable in 2015. Today, with one single product, Food Empire is among the Top 5 players in Vietnam's instant coffee mix industry based on volume share. It is also a Top 3 player based on value share.

- **Extensive network of sales representatives helps drive sales.** *Café Pho* is largely sold in sundry shops and markets, as general trade constitutes c.80% of the retail market in Vietnam. While the group uses third-party distributors to reach retailers, it employs 540 sales representatives across the country to bridge sales between distributors and retailers. These representatives visit the retailers on a weekly basis to ensure the retailers' timely restocking. They also help direct the retailers' shelf placements to ensure maximum visibility of *Café Pho* products.

- **High visibility of *Café Pho* increases its mind share.** During our visit, we noticed that *Café Pho* is widely available in the general trade. The product could be easily found in sundry shops or market stalls right next to each other (Figure 7). In addition, *Café Pho* is one of the few instant beverage products that focuses on selling in sachets aside from selling in bags and boxes (Figures 3-4). As *Café Pho* is a premium product with a higher price point, selling in sachets allows consumers with lower disposable income to buy at smaller quantity and lower cash outflows. Food Empire's sales representatives also encourage retailers to hang strings of *Café Pho* sachets from a rod across the shop's ceiling, which again raises the product's visibility (Figures 5-6).

- **Rolling out more products.** Following the success of *Café Pho*, the group has also launched a few new products and product variants – *Café Me* (hot coffee mix), *Café Ket* (mass market 3-in-1), *Café Pho Nha Lam* (even higher price point 3-in-1), and *Café Pho Den Da* (2-in-1) to increase sales. It is also venturing into the energy drink segment in 2020. While revenue contributions from these products are small, we believe they could capitalise on Food Empire's existing distribution and sales representatives network and help to improve operating leverage and margins.

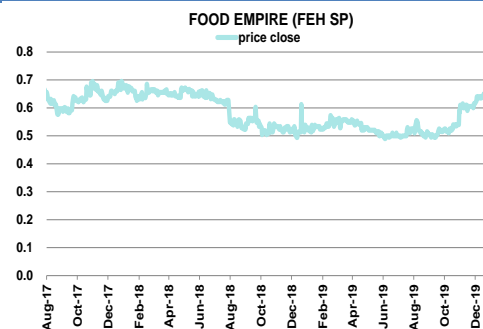
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Share Performance (%)

	YTD	1m	3m	6m	12m
Absolute	8.5	12.8	35.6	41.0	31.8
Relative	6.7	10.6	31.0	43.4	30.3
52-wk Price low/high (SGD)	0.49 – 0.71				



Source: Bloomberg

Forecasts and Valuation	Dec-17	Dec-18	Dec-19F	Dec-20F	Dec-21F
Total turnover (USDm)	269.5	284.3	283.1	305.2	333.7
Recurring net profit (USDm)	20.7	21.6	25.3	27.6	30.7
Recurring net profit growth (%)	98.7	4.5	16.9	9.0	11.4
Recurring P/E (x)	13.4	12.9	11.1	10.2	9.1
P/BV (x)	1.7	1.6	1.4	1.3	1.1
P/CF (x)	13.0	25.3	14.9	12.1	11.3
Dividend Yield (%)	0.9	1.0	1.2	1.5	1.6
EV/EBITDA (x)	7.8	9.8	7.8	6.3	5.6
ROE (%)	12.3	12.3	12.9	12.5	12.4
Net debt to equity (%)	net cash	net cash	1.9	net cash	net cash
Interest coverage (x)	32.3	27.3	26.2	35.9	40.0

Source: Company data, RHB

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Financial Exhibits

Asia	Financial summary	Dec-17	Dec-18	Dec-19F	Dec-20F	Dec-21F
Singapore	Recurring EPS (USD)	0.04	0.04	0.05	0.05	0.06
Food & Beverage Products	DPS (SGD)	0.00	0.00	0.01	0.01	0.01
Food Empire	BVPS (USD)	0.31	0.33	0.36	0.41	0.46
FEH SP	ROE (%)	12.33	12.27	12.88	12.51	12.43
	Valuation metrics	Dec-17	Dec-18	Dec-19F	Dec-20F	Dec-21F
	Recurring P/E (x)	13.4	12.9	11.1	10.2	9.1
	P/B (x)	1.7	1.6	1.4	1.3	1.1
	FCF Yield (%)	0.1	0.1	0.2	0.2	0.2
	Dividend yield (%)	0.9	1.0	1.2	1.5	1.6
	EV/EBITDA (x)	7.8	9.8	7.8	6.3	5.6
	EV/EBIT (x)	9.0	12.0	9.4	7.6	6.4
	Income statement (USDm)	Dec-17	Dec-18	Dec-19F	Dec-20F	Dec-21F
	Total turnover	269	284	283	305	334
	Gross profit	103	111	110	118	128
	EBITDA (adj.)	35	27	35	43	48
	Depreciation & amortisation	5	6	6	8	10
	Operating profit	29	22	29	34	38
	Net interest	-1	-1	-1	-1	-1
	Pre-tax profit	18	20	28	34	37
	Taxation	-5	-2	-6	-6	-7
	Net profit	13	18	22	27	30
	Recurring net profit	21	22	25	28	31
	Cash flow (USDm)	Dec-17	Dec-18	Dec-19F	Dec-20F	Dec-21F
	Change in working capital	-4	-12	-3	-4	-6
	Cash flow from operations	29	15	26	31	33
	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	-13	-4
	Cash at beginning of period	29	43	42	46	45
	Net change in cash	14	-1	4	-2	20
	Ending balance cash	43	42	46	45	65
	Balance sheet (USDm)	Dec-17	Dec-18	Dec-19F	Dec-20F	Dec-21F
	Total cash and equivalents	43	42	46	45	65
	Tangible fixed assets	65	69	93	105	106
	Total investments	13	11	11	11	11
	Total assets	247	245	286	304	335
	Short-term debt	20	20	10	0	0
	Total long-term debt	16	13	40	40	40
	Total liabilities	80	69	90	84	88
	Total equity	167	175	195	220	246
	Total liabilities & equity	247	245	286	304	335
	Key metrics	Dec-17	Dec-18	Dec-19F	Dec-20F	Dec-21F
	Revenue growth (%)	11.2	5.5	(0.4)	7.8	9.3
	Recurrent EPS growth (%)	98.5	4.5	15.9	9.0	11.4
	Gross margin (%)	38.3	39.0	38.9	38.8	38.5
	Operating EBITDA margin (%)	12.8	9.6	12.2	14.0	14.4
	Net profit margin (%)	7.7	7.6	8.9	9.0	9.2
	Capex/sales (%)	2.2	3.8	10.6	6.6	3.0
	Interest cover (x)	32.3	27.3	26.2	35.9	40.0

Source: Company data, RHB

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A look at Vietnam's 3-in-1 coffee mix market

Vietnam's 3-in-1 coffee market is traditionally dominated by Massan (*Vinacafe* and *Wake Up*), Trung Nguyen (*G7*), and Nescafe (*Nescafe 3-in-1*), with each sachet selling at c.VND2,000-2,500. Food Empire's *Café Pho* was introduced as a premium 3-in-1 ice coffee mix in 2013 and sells at c.VND3,500. The product quickly gained traction due to the taste similarity to ice coffee sold at coffee shops. It soon became the market leader in the 3-in-1 ice coffee sub-segment. Other players also began to introduce 3-in-1 ice coffee mix around 2016-2017, leading to a dip in Food Empire's Indochina revenue in 2017 before growth rebounded again in 2018 with its additional effort in advertising and promotions (A&P).

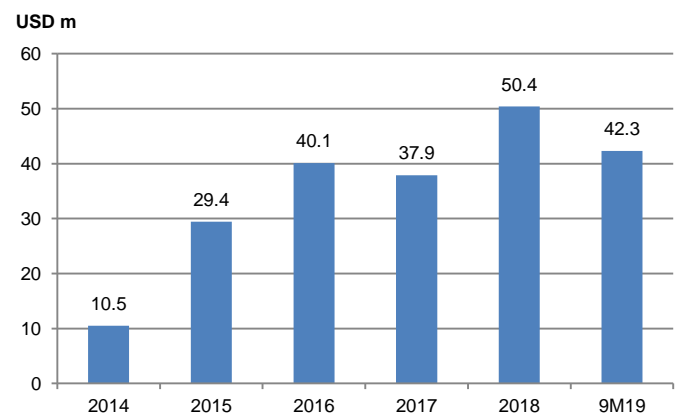
The group has launched *Café Me* and *Café Ket* at the lower price points (c.VND2,000-2,500) to compete in the mass market segment, and recently introduced *Café Pho Nha Lam*, a premium product with higher price point (c.VND4,000) than the original *Café Pho*.

Figure 1: Vietnam's 3-in-1 instant coffee mix segmentation by price (VND)



Source: Company, Nielsen

Figure 2: Food Empire's Indochina's revenue

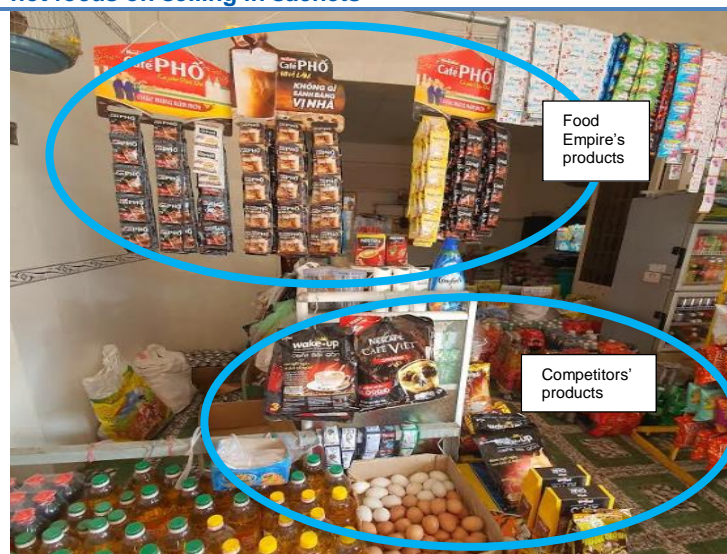


Source: Company data

High visibility drive continuous sales growth

Café Pho is one of the few instant beverage products that is sold in sachets. While 70% of the sales are made through bags and boxes, Food Empire continues to sell to its distributors and retailers in strings of sachets. The sales representatives carry the hangers as they conduct their visits to help retailers with the product's display. This helps to increase the visibility of *Café Pho* as most bags and boxes of 3-in-1 coffee products are kept at the back of the shops or hidden at some corner due to space constraints in most of these provision stores.

Figure 3: Most competitors only sell in bags or boxes and do not focus on selling in sachets



Source: RHB

Figure 4: Coffee bags are often placed at a corner of hidden behind the store due to space constraints



Source: RHB

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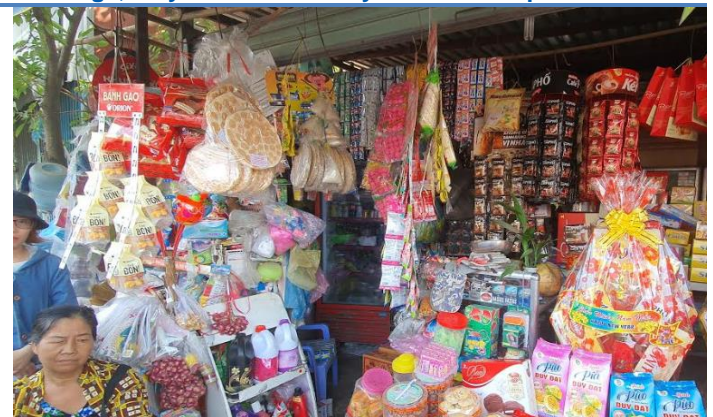
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Figure 5: Ability to hang strings of sachets from the top of the shop allows walk-in customers see the *Café Pho* from afar



Source: RHB

Figure 6: While the shop also sells the 3-in-1 coffee in boxes and bags, they are hidden away from the shop front



Source: RHB

Café Pho is widely available in the general trade. Often, we see the same *Café Pho* products being sold in stores right next to each other. Prices can vary slightly – depending on the relationship of the sundry shopkeeper and his/her individual customers.

Figure 7: *Café Pho* in two shops next to each other



Source: RHB

On the other hand, we note that *Café Pho*'s visibility is not as prominent in the supermarkets and convenience stores at the moment due to the lower penetration of modern trade (20% of retail) as well as high listing fees. However, management cited that it would still continue to work on its modern trade distribution in 2020. We believe this will ensure that the group has the tenacity to switch sales to modern trade when Vietnam's retail landscape modernises.

Figure 8: *Café Pho* and *Café Me* placed on the top shelf in a supermarket



Source: RHB

Figure 9: Competitors products are placed at eye level in a supermarket



Source: RHB

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