

## COMPANY RESULTS

### Food Empire Holdings (FEH SP)

1Q20: Ahead Of Expectations; Near-term Challenges From Potentially Weaker 2Q

Food Empire's core earnings of US\$9.5m (+33.0% yoy) was slightly ahead of our expectations, forming 34% of our full-year estimate. Earnings growth was boosted by core net margin expansion of 2.5ppt in 1Q20 and stable revenue growth of 5.0% yoy. The outlook for 2Q20 appears challenging due to the lockdown measures in key markets and the depreciation of the ruble. We do however expect a recovery in 2H20, assuming lockdown measures ease and ASPs rise to mitigate the forex impact. Maintain BUY with a lower PE-based target price of S\$0.63.

#### 1Q20 RESULTS

Year to 31 Dec (US\$m)	1Q20	1Q19	yoy % chg
Revenue	74.2	70.7	5.0
Gross profit	30.0	28.4	5.5
Gross margin (%)	40.4	40.2	0.2ppt
Net profit	6.6	7.6	(13.3)
Net margin (%)	8.8	10.7	(1.9ppt)
Core net profit	9.5	7.2	33.0
Core net margin (%)	12.8	10.3	2.5ppt

Source: Food Empire, UOB Kay Hian

#### RESULTS

- Results above expectations.** Food Empire reported net profit of US\$6.6m for 1Q20. Core net profit (excluding FX loss) came in at US\$9.5m (+33.0% yoy), forming 34% of our full year estimate, slightly ahead of our expectation.
- Strong growth on better margins and steady increase in sales.** Group revenue rose 5.0% yoy in 1Q20 on the back of higher sales in Ukraine, Kazakhstan and other Commonwealth of Independent States (CIS) markets (+23.7% yoy). The strong revenue growth in these markets managed to offset the slightly weaker sales contribution from the Southeast Asia market (-1.7% yoy) due its exit from the Myanmar market which overshadowed the revenue growth from Vietnam. Sales revenue from Russia declined 2.0% yoy, attributed to lower translated revenue resulting from the depreciation of the ruble against the US dollar in Mar 20. Core earnings were further boosted by the increase in core net profit margin to 12.8% (1Q19: 10.5%) as operating expenses remained relatively flat despite the sales growth. Furthermore, gross margin rose slightly to 40.4% (1Q19: 40.2%).
- Near-term challenges from COVID-19.** The group is experiencing weaker offtake from stores in most of its markets due to lower customer footfall as various governments in key markets have implemented social distancing measures to contain the outbreak. Management remarked that key production, sales and distribution activities are still continuing, albeit with slight disruptions.

#### KEY FINANCIALS

Year to 31 Dec (US\$m)	2018	2019	2020F	2021F	2022F
Net turnover	284	289	257	288	312
EBITDA	27	39	32	40	44
Operating profit	22	30	23	31	34
Net profit (rep./act.)	18	26	19	26	28
Net profit (adj.)	22	26	19	26	28
EPS (US\$ cent)	4.1	4.8	3.6	4.8	5.2
PE (x)	8.5	7.2	9.7	7.2	6.6
P/B (x)	1.0	0.9	0.8	0.8	0.7
EV/EBITDA (x)	6.6	4.7	5.7	4.5	4.1
Dividend yield (%)	1.4	4.1	1.7	2.8	3.0
Net margin (%)	6.4	9.0	7.4	8.9	9.0
Net debt/(cash) to equity (%)	(4.9)	(2.3)	(1.4)	(1.5)	(8.4)
Interest cover (x)	34.7	27.4	31.3	44.3	54.3
ROE (%)	10.5	13.6	9.0	11.1	11.1
Consensus net profit	-	-	26	29	32
UOBKH/Consensus (x)	-	-	0.73	0.87	0.89

Source: Food Empire, Bloomberg, UOB Kay Hian

## BUY

(Maintained)

Share Price	S\$0.49
Target Price	S\$0.63
Upside	+28.6%
(Previous TP)	S\$0.92)

#### COMPANY DESCRIPTION

Food Empire Holdings manufactures and markets instant beverage products, frozen convenience food, confectioneries and snacks. The company exports its products to markets such as Russia, Eastern Europe, Central Asia, the Middle East and Indochina.

#### STOCK DATA

GICS sector	Consumer Staples
Bloomberg ticker:	FEH SP
Shares issued (m):	536.6
Market cap (S\$m):	262.9
Market cap (US\$m):	185.0
3-mth avg daily t'over (US\$m):	0.3

#### Price Performance (%)

52-week high/low S\$0.770/S\$0.425

1mth	3mth	6mth	1yr	YTD
(9.1)	(31.5)	(18.0)	(4.8)	(23.1)

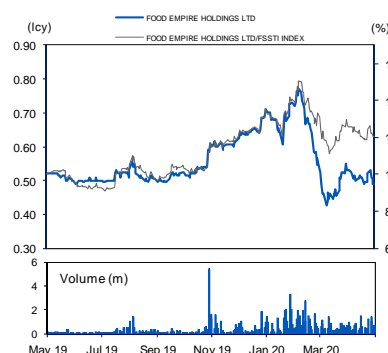
#### Major Shareholders

	%
Universal Integrated Corp	24.62
Tan Guek Ming	22.52
Sudeep Nair	11.44

FY20 NAV/Share (US\$) 0.41

FY20 Net Cash/Share (US\$) 0.01

#### PRICE CHART



Source: Bloomberg

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### STOCK IMPACT

- **Steep depreciation of the ruble partially offset by gradual ASP increase.** Mirroring the steep decline of oil prices, the ruble against the US dollar has experienced a sharp decline in Mar 20. The ruble averaged at 66.9 against the US dollar in 1Q20 and the rate is at 73.7 as of 12 May 20, compared to 61.9 as at 31 Dec 19. The currency depreciation would negatively impact Food Empire's core earnings due to lower translated revenue and could also lead to pressure on gross margins as some of its raw materials are denominated in US dollars. The impact of the currency depreciation would likely be more apparent in 2Q20 compared to 1Q20 as the depreciation of the ruble took place towards the second half of 1Q20/early-Mar 20. That said, we do highlight that the group has initiated a series of gradual price increases on its products from Apr 20 to mitigate the forex impact. It would take approximately 2-3 months for the higher prices (approx 10%) to be fully implemented; thus, we expect the impact of the price hike to materialise closer to 3Q20. Lower commodity prices could also help mitigate the forex impact on gross margins.
- **Weaker 2Q20 before potential recovery in 2H20 as lockdown measures ease.** Russia has been on a lockdown since late-March to stem the spread of the outbreak, with only essential industries allowed to continue operations. The government has announced a gradual easing of lockdown measures on 12 May 20. Moscow, its largest capital, is however expected to keep lockdown measures in place until May 31. Similarly, Kazakhstan has been in a state of emergency since end Mar 20 and is currently gradually reopening businesses as it eases lockdown measures from 11 May 20. This is also the case for Ukraine. Against this backdrop, we reckon sales volumes would be weaker for Apr-May 20, at least for its Russian, Ukraine, Kazakhstan and other CIS markets, thus adversely impacting earnings for 2Q20 on a yoy and qoq basis before recovering in 2H20, assuming lockdown measures are lifted/eased.

### EARNINGS REVISION/RISK

- We reduce our 2020-22 earnings forecasts by 13-32% as we lower our revenue forecasts by 9-16%. We now expect earnings for 2020-22 to come in at US\$19.1m (-32.4%), US\$25.6m (-16.1%) and US\$27.9m (-12.7%) respectively. Our forecasts incorporate a lower translated revenue and weaker sales volume due to the ruble depreciation, lockdown measures in 2Q20 and overall weaker economic sentiment. We also cautiously lower our gross profit margin forecast slightly. We expect a steeper revenue decline in 2Q20 before a partial recovery in 2H20 as lockdown measures ease and higher ASPs kick in. Our forecast revenue breakdown is as follows: approximately -22% yoy for 2Q20 and -13% yoy for 2H20.

### VALUATION/RECOMMENDATION

- **Maintain BUY with a lower PE-based target price of S\$0.63**, down from S\$0.92. This is based on 12.6x 2020F PE, in line with its long-term historical average (excluding outliers). Our target price also incorporates a slightly higher S\$/US\$ rate of 1.40 (S\$1.38 previously).
- At current prices, the stock trades at an attractive valuation at 9.7x 2020F PE, a significant discount to peer average of 24.3x for 2020F, suggesting that the ruble depreciation and potential weakness in sales volume have been priced in.

### PROFIT & LOSS

Year to 31 Dec (US\$m)	2019	2020F	2021F	2022F
Net turnover	288.6	257.0	288.1	312.1
EBITDA	38.5	31.6	40.4	44.3
Deprec. & amort.	8.1	8.3	9.0	10.1
EBIT	30.4	23.3	31.4	34.2
Total other non-operating income	2.4	0.6	0.6	0.6
Associate contributions	0.2	0.4	0.3	0.3
Net interest income/(expense)	(1.4)	(1.0)	(0.9)	(0.8)
<b>Pre-tax profit</b>	<b>31.5</b>	<b>23.3</b>	<b>31.4</b>	<b>34.3</b>
Tax	(5.8)	(4.7)	(6.3)	(6.9)
Minorities	0.4	0.4	0.5	0.5
<b>Net profit</b>	<b>26.1</b>	<b>19.1</b>	<b>25.6</b>	<b>27.9</b>
Net profit (adj.)	25.5	19.1	25.6	27.9

### CASH FLOW

Year to 31 Dec (US\$m)	2019	2020F	2021F	2022F
<b>Operating</b>	<b>39.3</b>	<b>33.4</b>	<b>28.8</b>	<b>33.1</b>
Pre-tax profit	31.5	23.3	31.4	34.3
Tax	(5.8)	(4.7)	(6.3)	(6.9)
Deprec. & amort.	8.1	8.3	9.0	10.1
Associates	0.2	0.4	0.3	0.3
Working capital changes	2.2	6.1	(5.6)	(4.7)
Non-cash items	0.0	0.0	0.0	0.0
Other operating cashflows	3.1	0.0	0.0	(0.1)
<b>Investing</b>	<b>(37.0)</b>	<b>(26.4)</b>	<b>(24.4)</b>	<b>(9.4)</b>
Capex (growth)	(38.1)	(27.0)	(25.0)	(10.0)
Proceeds from sale of assets	0.2	0.0	0.0	0.0
Others	0.9	0.6	0.6	0.6
<b>Financing</b>	<b>9.9</b>	<b>(12.8)</b>	<b>(8.4)</b>	<b>(10.4)</b>
Dividend payments	(2.8)	(1.0)	(0.9)	(0.8)
Issue of shares	0.6	0.0	0.0	0.0
Proceeds from borrowings	70.7	0.0	0.0	0.0
Loan repayment	(54.2)	(4.1)	(4.4)	(4.4)
Others/interest paid	(4.4)	(7.6)	(3.1)	(5.1)
<b>Net cash inflow (outflow)</b>	<b>12.1</b>	<b>(5.7)</b>	<b>(4.0)</b>	<b>13.3</b>
<b>Beginning cash &amp; cash equivalent</b>	<b>42.2</b>	<b>54.7</b>	<b>49.0</b>	<b>45.0</b>
Changes due to forex impact	0.4	0.0	0.0	1.0
<b>Ending cash &amp; cash equivalent</b>	<b>54.7</b>	<b>49.0</b>	<b>45.0</b>	<b>59.3</b>

### BALANCE SHEET

Year to 31 Dec (US\$m)	2019	2020F	2021F	2022F
Fixed assets	99.3	118.1	134.1	134.0
Other LT assets	51.8	51.7	51.7	51.6
Cash/ST investment	54.7	49.0	45.0	59.3
Other current assets	101.8	92.3	101.4	108.8
<b>Total assets</b>	<b>307.6</b>	<b>311.1</b>	<b>332.2</b>	<b>353.8</b>
ST debt	14.7	15.0	15.0	15.0
Other current liabilities	45.5	42.2	45.6	48.3
LT debt	35.3	30.9	26.5	22.1
Other LT liabilities	6.4	6.4	6.4	6.4
Shareholders' equity	206.9	218.3	240.9	263.7
Minority interest	(1.2)	(1.6)	(2.1)	(2.6)
<b>Total liabilities &amp; equity</b>	<b>307.6</b>	<b>311.1</b>	<b>332.2</b>	<b>352.8</b>

### KEY METRICS

Year to 31 Dec (%)	2019	2020F	2021F	2022F
<b>Profitability</b>				
EBITDA margin	13.3	12.3	14.0	14.2
Pre-tax margin	10.9	9.1	10.9	11.0
Net margin	9.0	7.4	8.9	9.0
ROA	9.5	6.2	8.0	8.1
ROE	13.6	9.0	11.1	11.1
<b>Growth</b>				
Turnover	1.5	(10.9)	12.1	8.3
EBITDA	40.5	(17.9)	27.8	9.7
Pre-tax profit	58.5	(26.1)	34.5	9.4
Net profit	44.3	(27.0)	34.2	9.2
Net profit (adj.)	17.9	(25.2)	34.2	9.2
EPS	17.8	(25.2)	34.2	9.2
<b>Leverage</b>				
Debt to total capital	19.6	17.5	14.8	12.4
Debt to equity	24.2	21.0	17.2	14.1
Net debt/(cash) to equity	(2.3)	(1.4)	(1.5)	(8.4)
Interest cover (x)	27.4	31.3	44.3	54.3

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