

# Fraser and Neave

## Thirsty for acquisitions

### SINGAPORE | CONSUMER | RESULTS

- 1Q FY17 Revenue/EBIT met our 25%/26% of our FY17 full year forecasts
- Margin compression amid subdued consumer sentiment in core markets
- Dairies Thailand to continue bolstering earnings with stable contribution
- Higher market penetration in New Markets, but proceeds will be reinvested for continuous brand building efforts

#### Results at a glance

SGD mn	1Q17	1Q16	y-y (%)	Comments
Beverages	139	132	5.2%	Higher contributions from SG and New Markets; partially offset by weaker MYR; -1% overall volume growth
Dairies	279	277	0.5%	Weaker MYR, competitive pricing in MY; +1% overall volume growth
Printing & Publishing ("P&P")	77	84	-8.3%	Lower demand from both <i>Publishing and Printing and Retail and Distribution</i> divisions
<b>Revenue</b>	<b>495</b>	<b>494</b>	<b>0.2%</b>	Expanded vending network and growth in New Markets
Gross profit	182	176	3.4%	Lower milk-based commodity prices
EBITDA	64	69	-7.7%	Higher operating expenses (+7.9% yoy)
PBIT	46	54	-13.7%	Negative currency translation effects (weaker MYR)
<b>PATMI (continuing operations ex. exceptional items)</b>	<b>22</b>	<b>26</b>	<b>-12.1%</b>	

Source: Company, PSR

**Operating environment in core markets remain challenging; Subdued topline growth as expected.** Flattish year-on-year ("yoy") growth in terms of overall sales and volume reaffirmed our view that Fraser and Neave, Ltd. ("FNN") continues to face macro headwinds. We expect an unexciting topline growth of 1.5% for FY17 on the back of cautious consumer spending in its core markets (Singapore, Malaysia and Thailand), and in the absence of a new growth pillar.

**Dairies business remains a stable support to the bottom line**, driven by favourable milk-based commodity prices and improvement in operational efficiencies arising from the new UHT lines in its Sarawak plant and new evaporated milk processing as well as packaging line in Rojana factory. However, we expect Dairies Thailand to outperform Dairies Malaysia, as higher sugar prices would negatively affect Dairies Malaysia's earnings more (Malaysia's main sales driver is sweetened condensed milk).

**Strong top-line growth from its New Markets.** Beverages sales from *Other Markets* (includes Indonesia, Thailand, Myanmar and Vietnam) registered 240% yoy growth in 1Q FY2017. FNN shared that the strong growth was mainly driven by Myanmar and Vietnam, as a result of distribution expansion, marketing initiatives and promotions. We expect marketing costs to remain elevated as FNN continues to reinvest the proceeds into Vietnam and Myanmar for marketing activities.

**Expects margin to remain under pressure.** Higher operating expenses, intensified competition and increasing raw material costs (particularly sugar) will continue to weigh against EBIT margin. Possibility of a sugar "sin tax" implementation this year in Malaysia would further compress EBIT margin. The Health Ministry of Malaysia is considering imposing a "sin tax" on imported or locally processed sugar-sweetened beverages. Nonetheless, barring implementation of the policy, we do not expect FNN to increase soft drink prices to pass on the cost pressure to consumers amidst a backdrop of intensifying competition.

10 February 2017

#### Reduce (Maintain)

CLOSING PRICE	SGD 2.12
FORECAST DIV	SGD 0.05
TARGET PRICE	SGD 1.80
TOTAL RETURN	-13.1%

#### COMPANY DATA

O/S SHARES (MN) :	1447
MARKET CAP (USD mn / SGD mn) :	2167 / 3068
52 - WK HI/LO (SGD) :	2.23 / 1.9
3M Average Daily T/O (mn) :	0.05

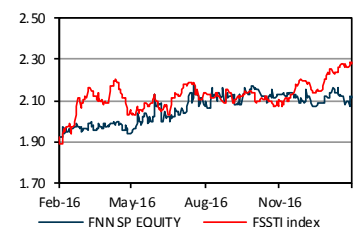
#### MAJOR SHAREHOLDERS (%)

TCC ASSETS LTD	59.35%
THAI BEVERAGE PCL	28.53%

#### PRICE PERFORMANCE (%)

	1M TH	3M TH	1Y R
COMPANY	10	0.5	8.9
STIRETURN	3.70	9.29	2157

#### PRICE VS. STI



Source: Bloomberg, PSR

#### KEY FINANCIALS

Y/E Sep	FY 15	FY 16	FY 17F	FY 18F
Revenue (SGD mn)	2,121	1,979	2,009	2,041
EBITDA (SGD mn)	209	190	174	141
NPAT, adj. (SGD mn)	115	109	106	100
EPS, adj. (Cents)	7.98	7.54	7.33	6.89
PER, adj. (x)	26.9	28.3	28.9	30.8
P/BV, (x)	1.4	1.1	1.1	1.0
DPS (Cents)	5.00	4.50	4.50	4.50
Div Yield (%)	2.3%	2.1%	2.1%	2.1%
ROE (%)	6.0%	4.3%	3.7%	3.4%

Source: Company Data, PSR est.

#### Valuation Method

EV/EBITDA Multiple (15x)

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### Bite-sized acquisition; still waiting for a game changing catalyst.

#### Proposed acquisition of Penguin Random House Pte. Ltd. And Penguin Books Malaysia Sdn. Bhd.

FNN has entered into a conditional agreement to acquire the sales and distribution offices of Penguin Random House Limited in Singapore and Malaysia with the intention to scale up the distribution business.

The deal hit a speed bump as the Competition Commission of Singapore (CCS) is conducting a public consultation on whether the deal would infringe the prohibition in the Competition Act against anti-competitive merger.

Printing & Publishing (P&P) segment contributed 15.5% of FY2016 Revenue and -2.9% of FY2016 EBIT. In view of a highly competitive market for book distribution, we do not expect a strong earnings turnaround for its P&P business in FY2017 should the deal went through.

#### Acquisition of additional shares of Vinamilk

FNN had increased its stake in Vinamilk from c.10.95% to c.16.35% through a competitive bid process on the Ho Chi Minh Stock Exchange ("HOSE") in 21 December 2016. It subsequently further acquired 1.1% shares in Vinamilk via open market purchases in January 2017, taking the Group's interest in Vinamilk to 17.5%.

We are generally upbeat on the increased stake in Vinamilk, as it will allow FNN to reap greater streams of dividend income and increase its foothold in Vietnam. The Group indicated interest in buying more shares in Vinamilk if opportunities arise.

### Maintain "Reduce" rating and with higher TP of S\$1.80 (previously S\$1.70)

We have adjusted upward our forecasted Beverages growth in FY2017 from 3% to 5%, on better than expected Beverages sales in New Markets and new agency brand, RIBENA. We have also updated our model to incorporate the acquisition of stakes in Vinamilk as well as a higher dividend income from Vinamilk.

We have also reviewed our FY17F EV/EBITDA multiple. In view that FNN's EBITDA and earnings will be highly dependent on its Dairy business, we think that FNN should trade closer to its ASEAN Dairy peers at 15x instead of its simple ASEAN peers' average at 11x.

We remain cognizant of:

(i) **Potential re-rating catalysts:** Acquisitions of stakes in Vinamilk and Saigon Alcohol Beer and Beverages Corporation ("SABECO").

We expect FNN to fund the acquisitions via borrowings and/or internally generated fund. As of 31 December 2016, the Company has a net cash position of S\$166.2 million. The Group has plenty of headroom before hitting its net gearing ratio ceiling of 80%.

(ii) **Adverse FX movements which could erode earnings:** Stronger USD against SGD; and weaker MYR and THB against SGD.

Figure 1:

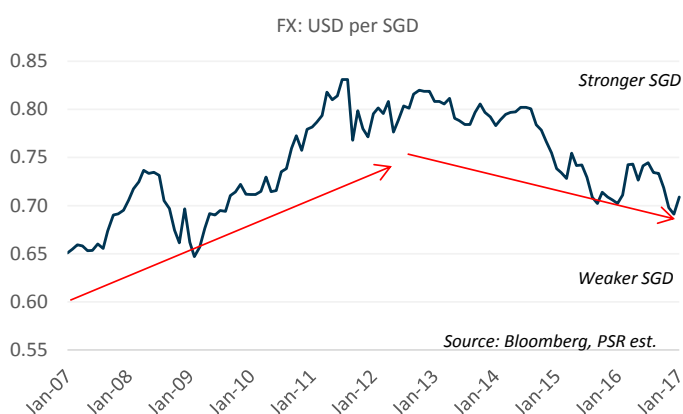


Figure 2:

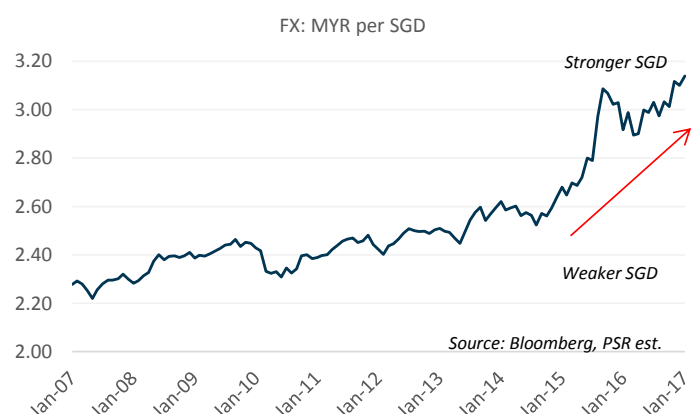
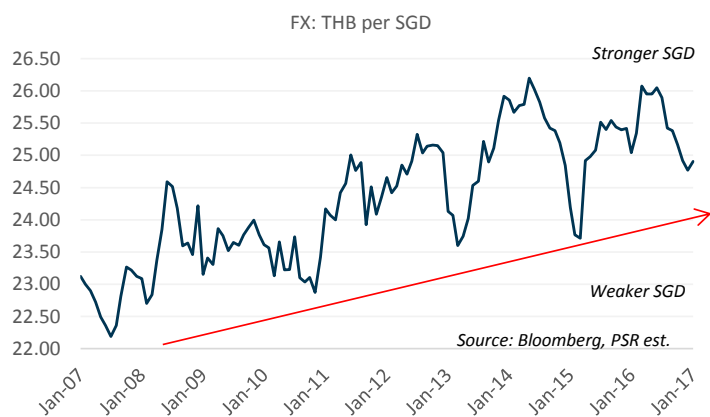


Figure 3:



## Valuation

### Peer Comparison

FNN currently trades at 28.6x FY17F PER, which is c.37% premium to its ASEAN Dairy peers' 20.9x. We think that the premium valuation is not justifiable given the lacklustre macro backdrop and lack of significant growth catalyst.

It also has lower return-on-equity (ROE), as compared to its ASEAN peers.

These support our thesis of 'Reduce' rating.

Figure 4:

Company	Mkt Cap (SGD mn)	EV (SGD mn)	EV/EBITDA TTM	EV/EBITDA FY1	P/E P/E	P/E FY1	Net D/E (%)	ROA (%)	ROE (%)	P/B
Fraser and Neave Ltd	3,068	3,221	17.8	15.5	29.2	28.6	Net Cash	3.0	4.0	1.1
<b>ASEAN</b>										
Fraser & Neave Hldgs Bhd	2,743	2,687	16.8	14.9	23.8	22.2	Net Cash	11.0	17.5	4.0
Alliance Global Group Inc	3,711	8,444	9.4	8.5	9.0	8.8	47.3	3.3	10.5	0.9
Pepsi-Cola Products Philippines Inc	337	447	4.3	4.2	14.1	12.9	-5.8	4.0	9.7	1.3
Ultrajaya Milk Ind & Trading	1,373	1,236	10.5	12.0	19.1	20.0	Net Cash	18.2	22.5	3.9
Vietnam Dairy Products JSC	12,168	11,583	14.8	14.2	23.0	20.5	Net Cash	32.9	39.3	8.8
Yeo Hiap Seng Ltd	820	722	15.8	N/A	24.9	N/A	Net Cash	4.8	5.6	1.4
<b>Simple Average (Excl. FNN)</b>			<b>11.9</b>	<b>10.8</b>	<b>19.0</b>	<b>16.9</b>	<b>20.8</b>	<b>12.4</b>	<b>17.5</b>	<b>3.4</b>

Source: Bloomberg

## Financials

### Income Statement

Y/E Sep, SGD mn	FY14	FY15	FY16	FY17F	FY18F
<b>Revenue</b>	<b>2,093</b>	<b>2,121</b>	<b>1,979</b>	<b>2,009</b>	<b>2,041</b>
Gross profit	659	696	728	743	745
<b>EBITDA</b>	<b>330</b>	<b>209</b>	<b>190</b>	<b>174</b>	<b>141</b>
Depreciation & Amortisation	(85)	(92)	(62)	(72)	(73)
<b>EBIT</b>	<b>170</b>	<b>132</b>	<b>179</b>	<b>181</b>	<b>181</b>
Net Finance Inc/(Exp)	9	0	10	9	(1)
Associates & JVs	2	3	3	3	3
Other items	(78)	12	48	75	110
<b>Profit Before Tax</b>	<b>178</b>	<b>132</b>	<b>189</b>	<b>189</b>	<b>181</b>
Taxation	(27)	(19)	(23)	(32)	(31)
<b>Profit After Tax (Con. Ops)</b>	<b>152</b>	<b>112</b>	<b>166</b>	<b>157</b>	<b>150</b>
<b>Profit After Tax (Discon. Ops)</b>	<b>205</b>	<b>637</b>	<b>0</b>	<b>0</b>	<b>0</b>
- Non-controlling interest	(109)	(87)	(58)	(51)	(50)
<b>Net profit, reported</b>	<b>147</b>	<b>633</b>	<b>108</b>	<b>106</b>	<b>100</b>
<b>Net profit, adj.</b>	<b>263</b>	<b>115</b>	<b>109</b>	<b>106</b>	<b>100</b>

### Per share data (SGD Cents)

Y/E Sep	FY14	FY15	FY16	FY17F	FY18F
EPS, reported	10.18	43.74	7.48	7.33	6.89
EPS, adj.	18.19	7.98	7.54	7.33	6.89
DPS	5.00	5.00	4.50	4.50	4.50
BVPS	111.07	156.82	196.65	201.03	205.13

### Cash Flow

Y/E Sep, SGD mn	FY14	FY15	FY16	FY17F	FY18F
<b>CFO</b>					
<b>EBIT</b>	<b>170</b>	<b>132</b>	<b>179</b>	<b>181</b>	<b>181</b>
Depreciation & Amortisation	85	92	62	72	73
WC changes	(193)	(33)	18	(15)	(2)
Tax paid	(50)	(34)	(24)	(32)	(31)
Others	188	69	(50)	(78)	(113)
<b>Cashflow from ops</b>	<b>199</b>	<b>225</b>	<b>185</b>	<b>127</b>	<b>109</b>
<b>CFI</b>					
CAPEX, net	(1,039)	(68)	(76)	(60)	(61)
Others	(536)	600	36	64	99
<b>Cashflow from investments</b>	<b>(1,575)</b>	<b>532</b>	<b>(40)</b>	<b>4</b>	<b>38</b>
<b>CFF</b>					
Share issuance, net	7	3	1	-	-
Loans, net of repayments	648	(17)	33	(16)	(20)
Dividends	(257)	(102)	(99)	(94)	(91)
Others	(607)	(10)	(4)	(4)	(4)
<b>Cashflow from financing</b>	<b>(209)</b>	<b>(126)</b>	<b>(70)</b>	<b>(114)</b>	<b>(115)</b>
<b>Net change in cash</b>	<b>(1,585)</b>	<b>632</b>	<b>75</b>	<b>17</b>	<b>31</b>
Effects of exchange rates	(3)	(25)	2	-	-
Asset reclassification	-	(0)	-	-	-
<b>CCE, end</b>	<b>355</b>	<b>962</b>	<b>1,043</b>	<b>1,041</b>	<b>1,068</b>

Source: Company, Phillip Securities Research (Singapore) Estimates

\*Forward multiples & yields based on current market price; historical multiples & yields based on historical market price.

### Balance Sheet

Y/E Sep, SGD mn	FY14	FY15	FY16	FY17F	FY18F
<b>ASSETS</b>					
PPE	661	464	491	497	504
Intangibles	124	106	125	129	133
Investments in Assoc/JV	50	42	43	46	49
Others	845	965	1,488	2,137	2,236
<b>Total non-current assets</b>	<b>1,680</b>	<b>1,577</b>	<b>2,146</b>	<b>2,809</b>	<b>2,922</b>
Accounts receivables	360	332	321	330	336
Cash	355	962	1,043	517	496
Inventories	274	254	247	243	249
Others	6	17	16	16	16
<b>Total current assets</b>	<b>995</b>	<b>1,565</b>	<b>1,627</b>	<b>1,106</b>	<b>1,095</b>
<b>Total Assets</b>	<b>2,675</b>	<b>3,143</b>	<b>3,773</b>	<b>3,915</b>	<b>4,017</b>
<b>LIABILITIES</b>					
Accounts payables	394	392	381	391	397
Short term loans	23	3	12	62	62
Others	47	50	47	47	47
<b>Total current liabilities</b>	<b>494</b>	<b>446</b>	<b>451</b>	<b>491</b>	<b>500</b>
Long term loans	119	98	125	108	88
Others	61	42	44	48	52
<b>Total non-current liabilities</b>	<b>180</b>	<b>140</b>	<b>169</b>	<b>157</b>	<b>140</b>
<b>Total Liabilities</b>	<b>674</b>	<b>587</b>	<b>620</b>	<b>648</b>	<b>640</b>
<b>EQUITY</b>					
Non-controlling interests	396	288	309	361	411
<b>Shareholder Equity</b>	<b>1,605</b>	<b>2,268</b>	<b>2,843</b>	<b>2,906</b>	<b>2,966</b>

### Valuation Ratios

Y/E Sep	FY14	FY15	FY16	FY17F	FY18F
P/E (X), adj.	17.2	26.9	28.3	28.9	30.8
P/B (X)	2.8	1.4	1.1	1.1	1.0
EV/EBITDA (X), adj.	14.3	12.1	13.1	17.7	22.1
Dividend Yield (%)	1.6%	2.3%	2.1%	2.1%	2.1%

### Growth & Margins (%)

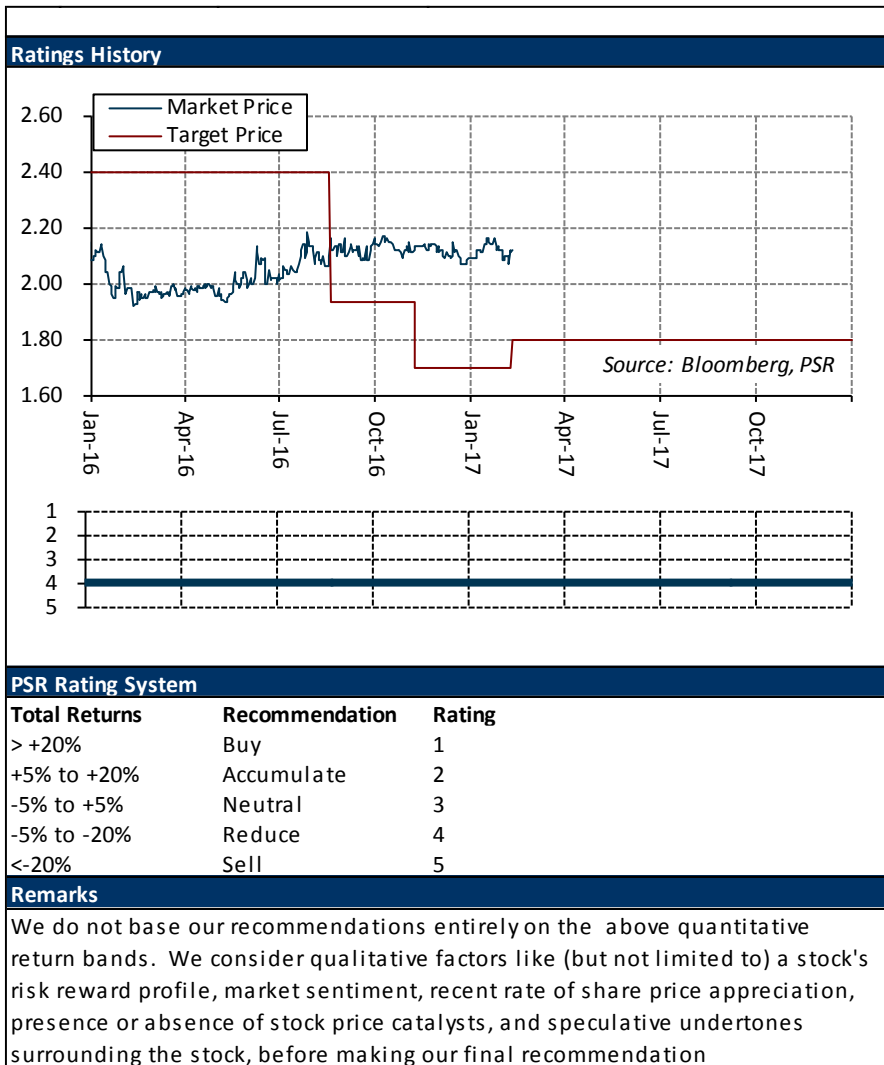
	FY14	FY15	FY16	FY17F	FY18F
<b>Growth</b>					
Revenue	-8.8%	1.3%	-6.7%	1.5%	1.6%
EBITDA	-28.0%	-36.6%	-8.9%	-8.5%	-18.9%
EBIT	-20.7%	-22.4%	36.2%	0.8%	0.5%
Net profit, adj.	-51.7%	-56.1%	-5.6%	-2.7%	-6.1%

### Margins

	FY14	FY15	FY16	FY17F	FY18F
Gross margin	31.5%	32.8%	36.8%	37.0%	36.5%
EBITDA margin	15.7%	9.9%	9.6%	8.7%	6.9%
EBIT margin	8.1%	6.2%	9.1%	9.0%	8.9%
Net profit margin	12.6%	5.4%	5.5%	5.3%	4.9%

### Key Ratios

	FY14	FY15	FY16	FY17F	FY18F
ROE (%)	5.2%	6.0%	4.3%	3.7%	3.4%
ROA (%)	3.1%	4.0%	3.2%	2.8%	2.5%
Net Debt/(Cash)	(213)	(861)	(906)	(347)	(346)
Net Gearing (X)	Net Cash	Net Cash	Net Cash	Net Cash	Net Cash



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