Asia Credit Research

OCBC Bank

Fraser and Neave Ltd: New Credit Review

Monday, July 03, 2017

Recommendations Summary

Issuer Profile:	Bond Recommendation:	
Neutral	FNNSP 3.09 '22	Neutral
	FNNSP 3.8 '27	Neutral
Fundamental Analysis Considerations • Leading F&B player • Healthy balance sheet • Growth from Dairy and Vinamilk to offset slowdown from Beverages	Technical Analysis Considerations • Rare F&B issuer • HoldCo-OpCo subordination • Visible retail presence	

S&P: Not rated

Moody's: Not rated

Fitch: Not rated

Ticker: **FNNSP**

Treasury Advisory

Corporate FX & Structured Products

Tel: 6349-1888 / 1881

Interest Rate Derivatives

Tel: 6349-1899

Investments & Structured Products

Tel: 6349-1886

GT Institutional Sales

Tel: 6349-1810

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Key credit considerations

- **Diversified leading F&B player:** Fraser and Neave Ltd ("FNN") is a leading F&B player in Singapore, Malaysia and Thailand. FNN owns a portfolio of well-known beverages (e.g. 100Plus, F&N Seasons) and dairy products (e.g. F&N Magnolia, Farmhouse), and publishing and printing businesses through Marshall Cavendish and Times Publishing. FNN's dairies segment is the main contributor at 57% of the group's LTM revenue. PBIT for this segment has grown rapidly, from SGD57mn in FY14 to SGD132mn in LTM. This has offset the fall in Beverages PBIT (LTM: SGD7mn, FY14: SGD67mn) due to competition and cost increases. The publishing and printing segment is an insignificant contributor to PBIT.

- **Growing with Vinamilk:** Vietnam Dairy Products JSC ("Vinamilk") is Vietnam's largest dairy company. Vinamilk's contribution to FNN looks to increase as FNN has been increasing its stake (Current: 18.74%). Vinamilk has also grown rapidly between 2012-2016 with revenue CAGR of 14.7%, and targets to grow 2016's revenue of VND46,965bn (SGD2.9bn) by another 11.2% CAGR till 2021 to reach VND80,000bn (SGD4.9bn). Vinamilk will be a significant contributor to FNN, making up an estimated 56% of FNN's total assets. Vinamilk generates recurring FCF and consistently pays dividends. We estimate Vinamilk will contribute SGD55.6mn dividends and an additional SGD62.7mn PBIT to FNN in 2017.

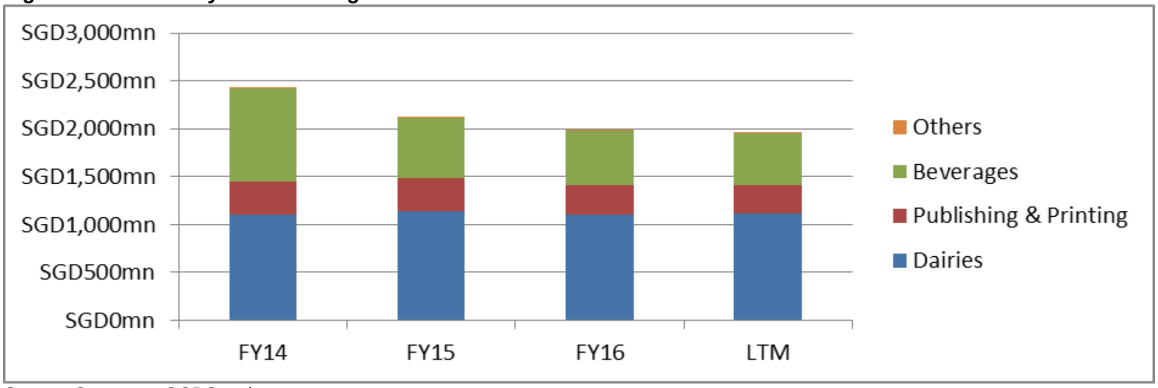
- **Healthy credit metrics:** Balance sheet looks healthy with net gearing of 3% while Net debt/EBITDA is only 0.6x as of 1HFY17. FNN can gear up further with a gearing policy of up to 80% with estimated debt headroom of SGD2.4bn, which FNN may utilise to continue acquiring more shares of Vinamilk and/or take a stake in other Vietnamese enterprises. There is room to accommodate more debt as we expect FNN to receive at least SGD91.6mn of annual dividends from both Vinamilk and its 55.5%-owned Fraser and Neave Holdings Bhd ("FNNB").

- **Structural factors:** After a hiatus from the bond market since 2013's consent solicitation to buy back its bonds, investor interest seemed strong with over SGD500mn orderbook for its SGD100mn bond printed in Apr 2017. However, HoldCo-OpCo risks remain as Vinamilk and FNNB (71% of FNN's revenue) are the main profit contributors to FNN. Risks though, are mitigated by upstreaming of dividends while subordination risks to FNNB are manageable given FNNB's low debt and FNN's controlling stake. We also see potential supply risk if FNN continues to acquire. Meanwhile, we recognise FNN as a rare F&B issuer with a high retail presence in the SGD space, offering a scarce supply of long-dated non-Temasek paper, which should appeal to investors looking for diversification.

I) Company Background

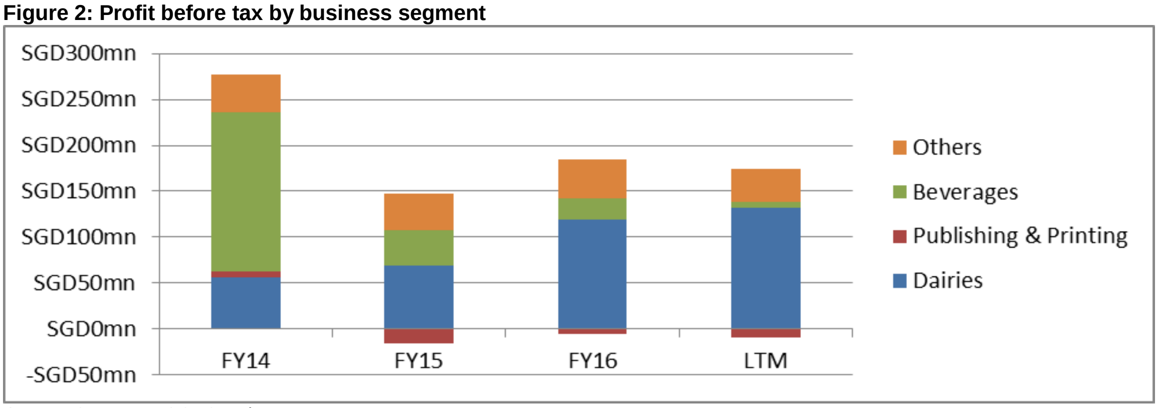
Fraser & Neave Ltd ("FNN") is a consumer group engaged in Food & Beverage ("F&B") and Publishing and Printing ("P&P") businesses with market leading positions in Southeast Asia. FNN owns well-known beverages and dairy brands including 100Plus, F&N Nutrisoy, F&N Seasons, F&N Magnolia and Farmhouse. FNN markets its P&P business through Marshall Cavendish and Times Publishing. FNN owns a 55.5% stake in Fraser & Neave Holdings Bhd ("FNNB"), which is a F&B company listed on the Bursa exchange with a market cap of MYR9.3bn (SGD3.0bn). FNN also owns 18.74% of Vietnam Dairy Products JSC ("Vinamilk"), which is a dairy company listed on the Ho Chi Minh exchange with a market cap of VND224.7tn (SGD13.6bn).

Figure 1: Revenue by business segment



Source: Company, OCBC estimates

Figure 2: Profit before tax by business segment



Source: Company, OCBC estimates

Figure 3: LTM revenue by geography

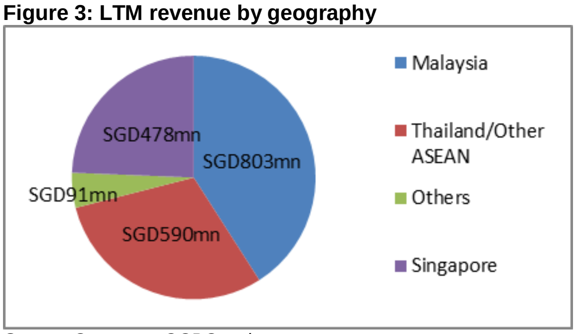
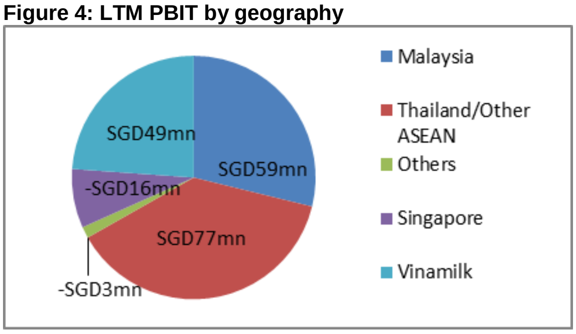


Figure 4: LTM PBIT by geography



Source: Company, OCBC estimates

Diary and Beverages segments make up 56.8% and 28.0% of LTM revenue respectively, while the P&P segment contributes the remaining 15.2%. Through FNNB, Malaysia (41%) and Thailand/Other ASEAN (30%) are the largest contributors to FNN's revenue by geography. By PBIT, Thailand/Other ASEAN (excl Vinamilk) and Malaysia are the largest contributors, followed by Vinamilk.

Recent corporate actions that led to the fall in revenue and profit after FY14

FNN used to be a larger and more diversified conglomerate. In Nov 2012, FNN completed the disposal of its 39.7% stake in Asia Pacific Breweries ("APB"), which holds the Tiger beer brand, to Heineken for SGD5.6bn. Subsequently in Jan 2014, FNN spun off its property arm, Frasers Centrepoint Ltd ("FCL"), via dividend in-specie distribution. In Aug 2015, FNN sold its 55% stake in Myanmar Breweries ("MBL") to Myanmar Economic Holdings Ltd for USD560mn.

II) Ownership & Management

Figure 5: Major shareholder as at 03/07/17

Investor	Shares	Stake
TCC Assets Ltd	858mn	59.30%
Thai Beverage PCL	412mn	28.50%

TCC Assets Ltd ("TCCA") is the largest shareholder with a 59.3% stake in FNN. TCCA is owned by Thai billionaire Charoen Sirivadhanabhakdi (50%) and his spouse (50%). TCCA acquired the FNN stake in 2013 when it offered SGD9.55 per share for FNN shares it did not already own, after Japanese beverage giant Kirin sold its 15% stake to TCCA. Together with the stakes held by Thai Beverage PCL ("ThaiBev"), Mr Charoen controls FNN with 87.8% effective stake. Mr Charoen's main holding company is the private Thailand-based TCC Group, which holds interests in F&B, property and financials.

ThaiBev is a beverage company listed on the SGX with a market cap of SGD21.8bn. Mr Charoen and his spouse hold a 51% stake in Siriwana Co Ltd, which in turns owns 45.27% of ThaiBev. While ThaiBev is in the same F&B industry as FNN, we understand from management that the relationship with ThaiBev is more about cooperation than competition. For example, FNN capitalises on ThaiBev's distribution network in Thailand for its dairy products but does not encroach into ThaiBev's soft drinks business in Thailand. Both companies also have the flexibility to cross-sell each other's products. For example, ThaiBev launched FNN's 100Plus in Thailand, while FNN have begun selling ThaiBev's Oishi Green Tea (instead of its FNN Seasons Green Tea) in Malaysia. Meanwhile, FNN is the vehicle for M&A outside Thailand – which may see FNN gearing up its balance sheet (e.g. acquisition of stakes in Vinamilk).

There has been market speculation that ThaiBev and TCC may enter into a stake swap, such that the TCC Group's stakes in FNN will be held under ThaiBev while FCL will be held under TCCA. However, we do not think this will result in a significant change in credit profile as both ThaiBev and TCCA are ultimately controlled by the TCC Group.

Mr Charoen and his spouse are the chairman and vice-chairman on the board of FNN. FNN does not have an overall CEO but has 4 appointed persons to head the various divisions.

Heading the Beverage Division (Non-Alcoholic) is Mr Lee Meng Tat, who has been with FNN for over 14 years. Mr Lee has participated in various parts of FNN's business. Prior to FNN, Mr Lee worked in the Singapore Tourism Board and Singapore Economic Development Board. Mr Lee finished his Advanced Management Program at Harvard and MBA at Imperial.

Mr Edmond Neo is the CEO of the Beverage Division (Beer), and has been with FNN for more than 24 years through various parts of FNN's business. Mr Edmond Neo graduated from National University of Singapore with a Bachelor of Accountancy.

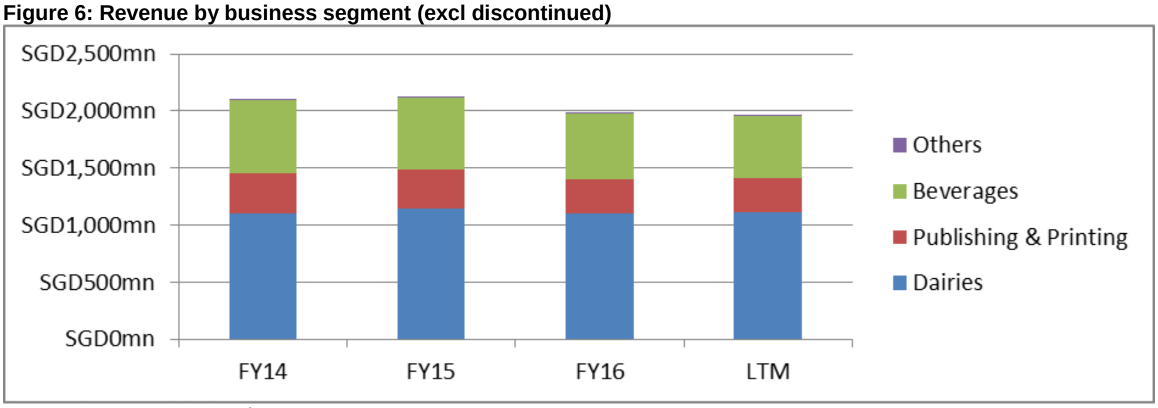
Mr Bennett Neo is the CEO of the Food Division, serving FNN for more than 9 years. Prior to FNN, Mr Bennett Neo was from ExxonMobil. Mr Bennett Neo graduated from Nanyang Technological University with a Bachelor of Engineering (Mechanical).

Mr Siew Peng Yim is the CEO of Times Publishing, and has been with FNN for nearly 5 years. Mr Siew graduated from National University of Singapore with a Bachelor of Accountancy and is a Chartered Accountant of Singapore.

III) Business Overview & Analysis

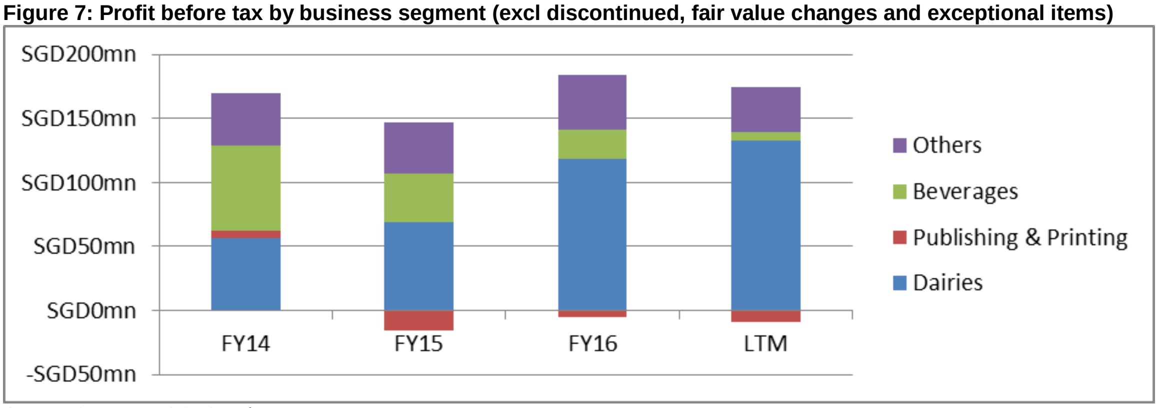
FNN has gone through significant changes to its business profile over FY12-14 due to the divestment and disposal of APB, FCL and MBL. As such, we will focus our analysis on FNN's financials without the effect of discontinuing business from FY2014 (complete information on the current continuing business segments prior to FY14 is not available). The main segment contributors are 1) Dairies, 2) Beverages and 3) Publishing & Printing.

Figure 6: Revenue by business segment (excl discontinued)



Source: Company, OCBC estimates

Figure 7: Profit before tax by business segment (excl discontinued, fair value changes and exceptional items)



Source: Company, OCBC estimates

Dairies have been the largest contributor to revenue, followed by Beverages, and Publishing & Printing. There is minimal revenue under 'Others' though its contribution to PBIT is substantial due to contributions from Vinamilk. Moving forward, Vinamilk will likely contribute more to earnings. Firstly, FNN has been increasing its stake in Vinamilk, from 10.95% in 2016 (prior to purchase of a further 5.4% stake on 12 Dec 2016) to 18.74% as of current. From the next results (3QFY17) onwards, FNN will equity account[1] its investment in Vinamilk as an "Investment in Associated Company", instead of recording only Vinamilk's dividends as earnings.

Dairies

Under the Dairies segment, the brands include F&N Magnolia, F&N Canned Milk, F&N Daisy, Farmhouse, F&N Fruit Tree Fresh, F&N Tea Pot, Gold Coin and Blue Cow. FNN also markets third-party brands such as Carnation and Sunkist.

Figure 8: Dairy brands

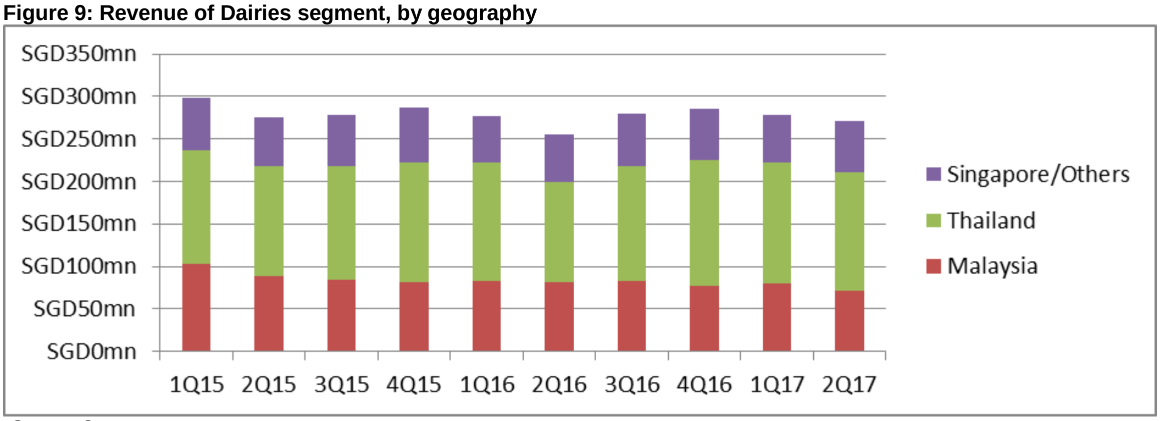
Source: Company

[1] FNN will record its share of profits from Vinamilk

Brand	Description
F&N Magnolia	Leading dairy brand in Singapore, offering pasteurised milk, UHT milk, sterilised milk, yoghurt, ice cream
F&N Canned Milk	Leading canned milk in Singapore, Malaysia, Thailand which includes brands such F&N, F&N Tea Pot, Gold Coin, Blue Cow
F&N Daisy	99% fat-free milk enriched with vitamins
Farmhouse	Australian milk products include fresh milk and UHT milk, offered in Malaysia and Singapore
F&N Fruit Tree Fresh	Juice brands with real fruit juices as ingredients
F&N Tea Pot	FNN markets creamers under the Teapot brand
Gold Coin	FNN also markets creamers under the Gold Coin brand
Blue Cow	Canned milk brand
Carnation	Carnation is a 3rd party creamer brand
Sunkist	Sunkist is an orange-based juice brand

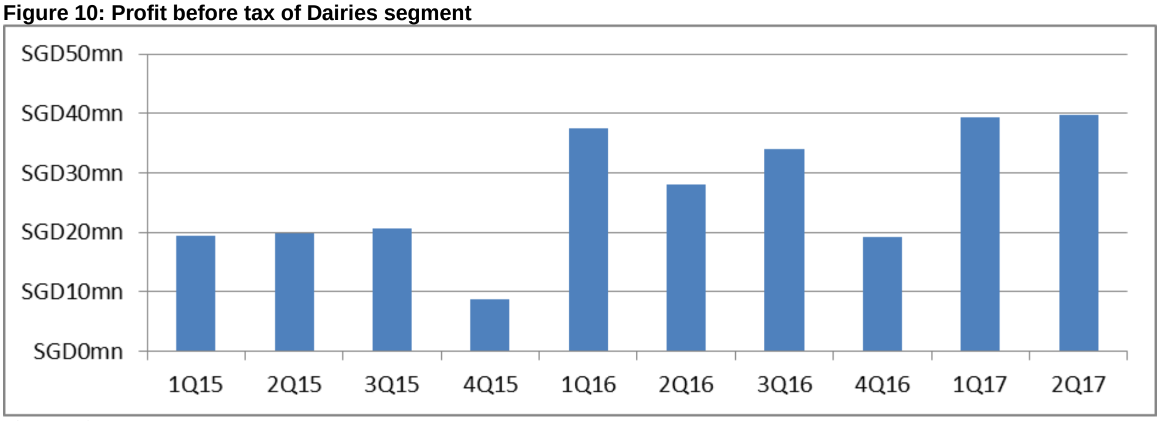
The Dairies segment is the largest contributor to FNN, at 57% of the revenue and 80% of the PBIT. Revenue in FY16 was lower 3.7% y/y due mainly to depreciation of MYR and THB. While FNN also lost sales from Bear & Milo UHT, the loss in revenue was mitigated by volume growth from new product launches in Thailand. Thus far in 1HFY17, Dairies Malaysia revenue (-8% y/y) has been impacted due to subdued consumer confidence and a competitive pricing environment, exacerbated by a weaker Ringgit. Nevertheless, 1HFY17 Dairies revenue remained relatively stable due to stronger performance from Dairies Thailand (+6% y/y) with a stronger Thai Baht while demand increased for its core brands with increased distribution coverage.

Figure 9: Revenue of Dairies segment, by geography



Source: Company

Figure 10: Profit before tax of Dairies segment



Source: Company

Though revenue trended lower in FY16, PBIT surged due to lower milk-based commodity costs, favourable product portfolio mix, recovery of withholding tax royalties and greater operational and manufacturing efficiencies (from new UHT line in Kuching and new filling and packaging line in

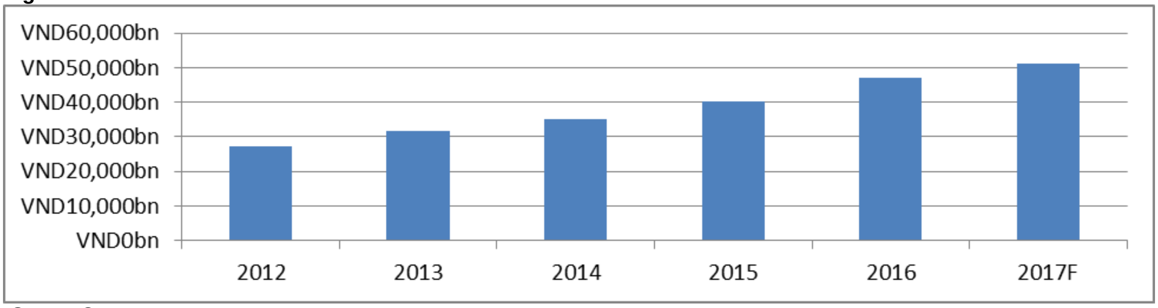
Rojana). The good performance has continued, with LTM Dairies PBIT trending up (+11.5% from FY16) due to favourable milk-based commodity cost.

Looking ahead, it may be unlikely for the Dairy segment to see further margin expansion due to the increase in milk powder prices. The economic sentiments in Malaysia are expected to remain soft, according to FNNB, as the rise in CPI has affected purchasing power. Nevertheless, we think that overall Dairies revenue may remain relatively stable as Dairies Thailand is still seeing strong demand for its core brands (Teapot and Carnation) while Dairies Singapore is also seeing increased domestic sales for chilled products and yoghurt lines.

Vinamilk

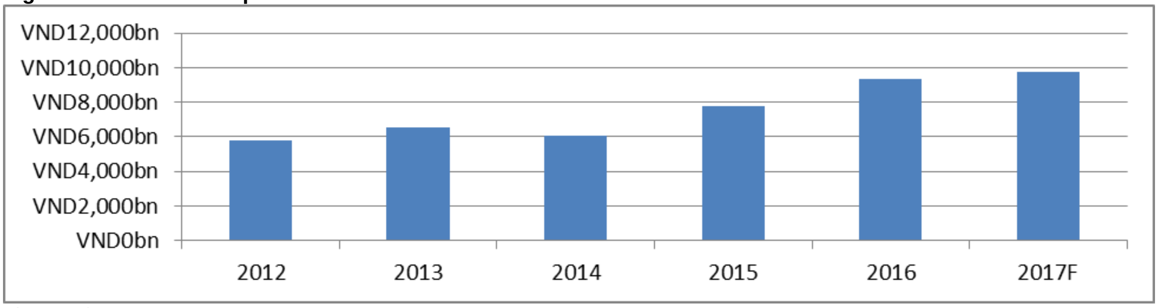
Vinamilk processes, produces and trades fresh milk, packed milk, powdered milk, other dairy products and raises cattle. FNN first acquired a 11.04% stake in Aug 2014. This was increased to 18.74% over Dec 2016 to June 2017, of which a 5.4% stake was acquired from the Vietnam government. FNN finds that Vinamilk holds a strong position in Dairy in Vietnam with 54.5%, 84.7% and 33.9% market share in liquid milk, eating yoghurt and drinking yoghurt respectively.

Figure 11: Vinamilk revenue



Source: Company

Figure 12: Vinamilk net profit



Source: Company

Vinamilk has been growing rapidly, with a revenue and net profit CAGR of 14.7% and 12.6% respectively between 2012 and 2016. Vinamilk plans to grow revenue and net profit by 8% and 4% in 2017 to VND51,000bn and VND9,735bn respectively. Growth rates are likely to be met given i) higher historical growth rates, ii) the planned growth is the minimum requirement set by Vinamilk and iii) 1Q2017 revenues and profits are already higher by 16% y/y and 36% y/y to VND12,074bn and VND2,935bn respectively, which forms 24% and 30% of the full year target. In the longer term, Vinamilk targets VND80,000bn revenue by 2021, with VND61,000bn from domestic sources (2016: VND38,099bn) and VND19,000bn (VND8,696bn) from outside Vietnam. In a move to meet its revenue target outside Vietnam, on 12 May 2017, Vinamilk signed a memorandum of cooperation to export dairy products to China.

Vinamilk will be a significant contributor to FNN's credit profile. 2017 dividends received by FNN from Vinamilk will likely exceed SGD55.6mn (2016: SGD48.6mn) given FNN's existing 18.74% stake in Vinamilk and Vinamilk's 2017 profit target with a dividend payout ratio of at least 50%. We estimate that FNN's stake in Vinamilk is worth SGD2.6bn, which would make up 56% of FNN's total assets. Vinamilk's 2017 profit target also implies that FNN's share of profits from

Vinamilk would increase to SGD111.3mn (2016: SGD48.6mn), which we estimate will form 49% of FNN's PBIT. 2016's profit contribution was lower as it was based on dividend income (and not share of profit) from Vinamilk while FNN used to own a smaller 10.95% stake in Vinamilk.

Going forward, FNN's stake in Vinamilk may grow further if the main shareholder, the State Capital Investment Corporation ("SCIC"), decides to dispose more shares. SCIC is state-owned by Vietnam and is disposing its stake in Vinamilk, together with 12 other companies, as part of Vietnam's economic strategy to contain the mounting public debt. Currently, the SCIC still holds 39.3% of Vinamilk.

Vietnam is open to foreigners taking a majority stake in Vinamilk. In July 2016, the 49% foreign holding cap in Vinamilk was removed by the Vietnam State Securities Commission. FNN is deemed to have significant influence over Vinamilk (after Vinamilk's AGM on 15 Apr 2017) as it nominated an additional member to the board of directors of Vinamilk, increasing FNN's representation on the board to 2 members.

Beyond Vinamilk, Mr Charoen has expressed interest in further M&A in Vietnam's Saigon Beer Alcohol Beverage Corp ("Sabeco"). As FNN is the vehicle for M&A outside Thailand, FNN may continue ramping up acquisitions. Sabeco is 89.6% owned by the Vietnam government, and the government is looking to sell its stake. Sabeco is currently listed on the Ho Chi Minh stock exchange with a market cap of VND132,617bn (SGD8.1bn). According to South China Morning Post, Sabeco has 40% market share of beer in Vietnam.

Beverages

Under the Beverages segment, the brands include 100Plus, F&N Nutrisoy, F&N Nutriwell, F&N Sparkling Drinks, F&N Ice Mountain, F&N Seasons, F&N Fruit Tree. FNN also markets OISHI, which is a tea brand under ThaiBev.

Figure 13: Beverage brands

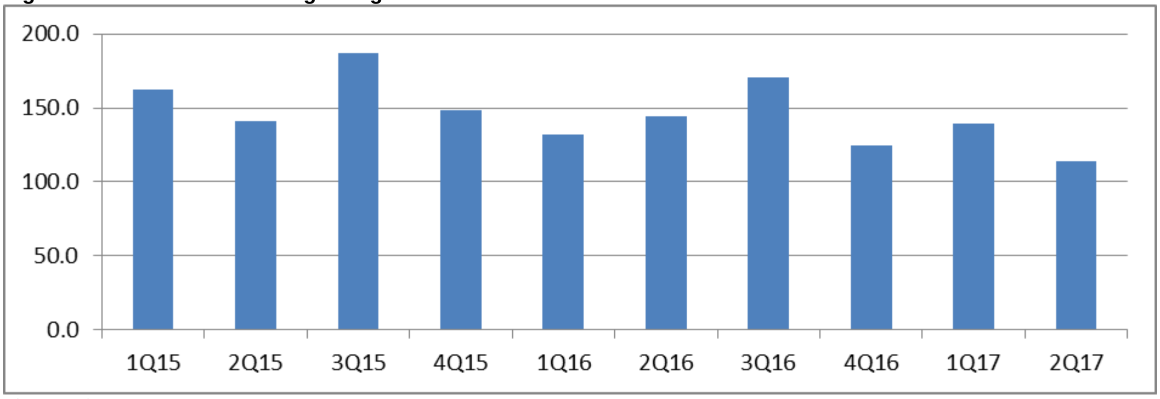
Source: Company

Brand	**Description**
100Plus	A leading isotonic beverage in Singapore, Malaysia and Myanmar with a rapidly growing presence in Thailand
F&N Nutrisoy	A leading soya brand in Malaysia and Singapore
F&N Nutriwell	Preservative-free pasteurised drink with reduced sugar
F&N Sparkling Drinks	Flavours include 'Sarsi', 'Cheeky Cheeryade', 'Ice Cream Soda', 'Zesty Zapple', ' Clearly Citrus'
F&N Ice Mountain	Mineral water
F&N Seasons	Tea brand which includes ice lemon tea, ice peach tea, ice apple tea
F&N Fruit Tree	Juice drinks (typically in cans) from real fruit juice

The Beverages segment contributed 28% of revenue but only 4% of PBIT in LTM. Despite the high contribution in the past in FY14 (Figure 7), PBIT has fallen quickly due to a decline in revenue and margins. In 2015, FNNB did not manage to renew its 5-year agreement to distribute and sell Red Bull in Malaysia, which used to contribute about MYR200mn revenue p.a. Numbers reported in SGD are also made worse as the MYR has weakened by 15% against the SGD since end 2014. PBIT fell more than revenue as margins have deteriorated due to intensified competition (e.g. Coke and Pepsi have been slashing prices in Malaysia, likely in an attempt to push volumes). In addition, raw material costs have increased due to an increase in sugar prices.

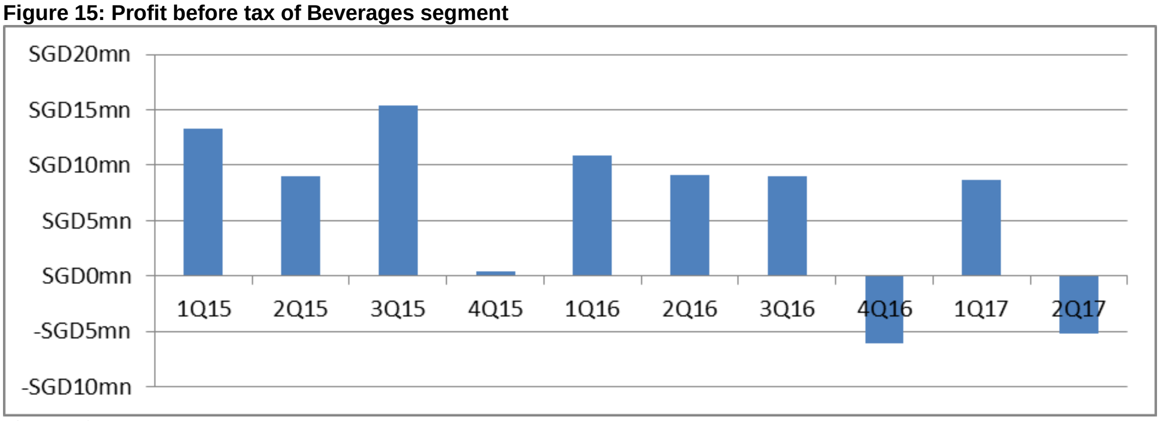
In the latest 2QFY17 results for the quarter ending 31 Mar, the Beverages segment has already swung into a net loss due to lower revenue and higher input costs. While it is difficult to assess the timing of a turnaround in the revenue (which is likely dependent on the pricing strategy of competitors), we think Beverages PBIT may not deteriorate further. After the non-renewal of the Red Bull contract, we are not worried about the continuity of the other significant partnerships, which include ThaiBev, Nestle and Sunkist. ThaiBev cooperates with FNN given the former's stakes in FNN, while FNN's license with Nestle runs till 31 Jan 2037. Sunkist does not form a significant part of FNN's revenue according to management. Sugar prices (which affect cost of goods sold) have since fallen by about 25% from its peak in Oct 2016. Seasonally, 4Q is traditionally the weakest quarter (with FNN posting a loss in 4QFY16) as market conditions in Malaysia are softer post Hari Raya. However, while competition remains intense in Malaysia, margins may remain compressed going forward.

Figure 14: Revenue of Beverages segment



Source: Company

Figure 15: Profit before tax of Beverages segment



Source: Company

Printing and Publishing

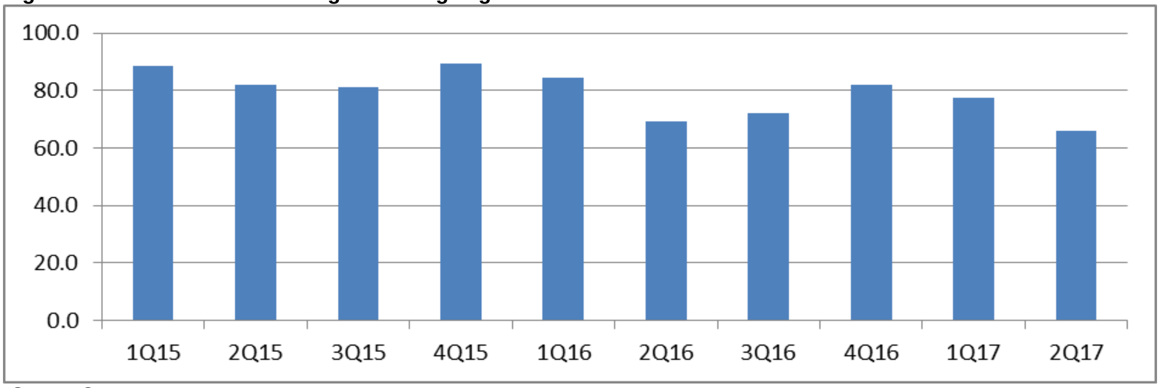
FNN's P&P segment include Marshall Cavendish[2] and Times Publishing Ltd. The major subsidiaries are Times Printers[3], Pansing Distribution[4], Times bookstores[5] and Times Travel[6].

The revenue of the P&P business has been on a decline and the segment remains unprofitable. For 1HFY17, revenues were impacted by lower print volumes from key magazine publishers. 2QFY17 is seasonally weaker due to lower retail orders and higher market returns post-Christmas. FY16's results (-10% y/y) were dragged down by the publishing segment which recorded lower revenue due to lower demand for textbooks at end-of-school adoption cycle. This was exacerbated by lower print volumes in Singapore and Malaysia and discontinuation of a print joint venture in China.

[2] Marshall Cavendish is FNN's main brand for the publishing business, covering extensive contents in education, general interest, business information and home reference.
[3] Provides print solutions
[4] Distributor of books and magazine
[5] Book retailer
[6] Book retailer catered to the travel market

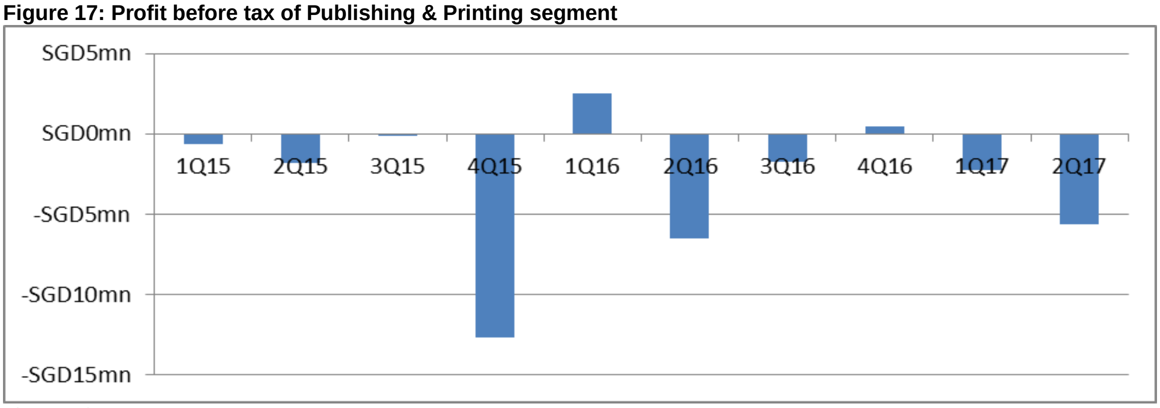
While the P&P segment remains unprofitable, FNN has contained the losses (2Q17 PBIT loss narrowed to SGD5.6mn from 2Q16's loss of SGD6.5mn) due to improved efficiencies and strict cost control. FY16's PBIT loss of SGD5.2mn is also lower than FY15's (loss of SGD15.3mn) which was due to a restructuring exercise to reduce the operating cost base. Going forward, management thinks that the P&P segment would likely remain challenging and further rightsizing may be necessary to turn the segment cashflow positive. Print capacity will likely be reduced to contain costs while investments will be made in the digital aspect of the publishing business. Management has no plan for the sale of the P&P segment. We note that FNN supports social causes including education – which the P&P segment caters to.

Figure 16: Revenue of Publishing & Printing segment



Source: Company

Figure 17: Profit before tax of Publishing & Printing segment



Source: Company

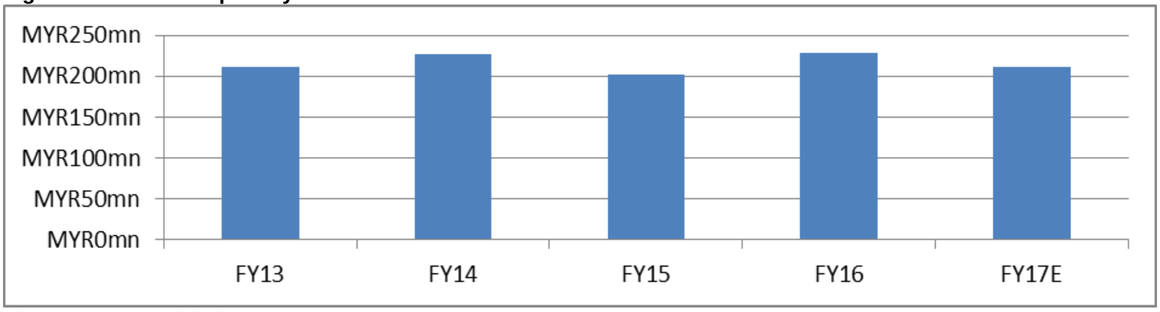
IV) Financial Analysis

- **Healthy credit metrics:** Despite expending another SGD947mn in 1HFY17 to acquire more shares of Vinamilk (est: 7% stake), FNN's balance sheet looks healthy still with a net gearing of 3%. Another SGD551mn of cash remains as of 2QFY17 with SGD117mn fixed deposits. However, the potential remains for FNN to gear up further with a gearing policy of up to 80%, which implies SGD2.4bn debt headroom. We think FNN may continue acquiring more shares of Vinamilk and/or take a stake in Sabeco. Cashflow metrics also look healthy, with positive free cash flows of SGD119.2mn in FY16 while Net debt/EBITDA is only 0.6x as of 1HFY17.

- **Managing earnings volatility, better outlook ahead:** We think the Beverages segment may take time to return to its more profitable days while it combats competition and manage the higher cost of sugar. However, overall PBIT (LTM: SGD166mn) has not changed much since FY14 (SGD170mn) as the Dairies segment PBIT has surged to SGD132mn in the LTM (FY14:SGD57mn), which largely replaced the decline in PBIT of the Beverages to SGD7mn in LTM (FY14: SGD67mn). However, going forward, we think that FNN will deliver stronger earnings (expected increase: SGD62.7mn) mainly due to a higher stake in Vinamilk.

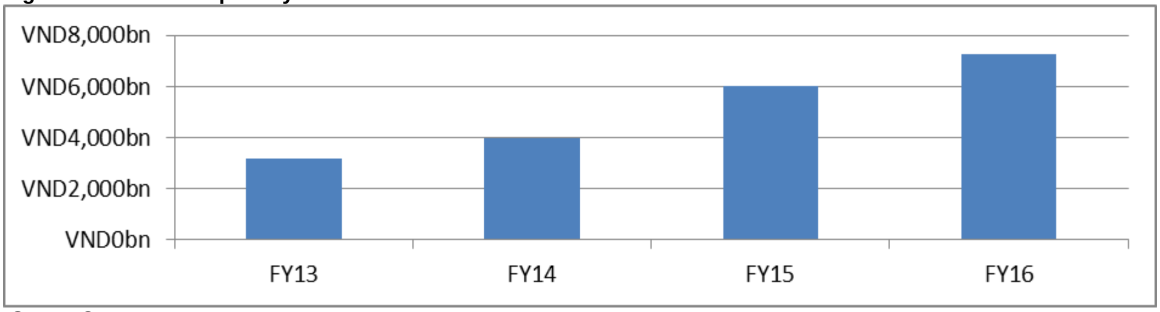
- **Credit profile supported key subsidiaries and associates:** We estimate that FNNB and Vinamilk contribute 71% of FNN's revenue and most of its PBIT. Thus far, FNNB has been paying relatively stable dividends of MYR200mn-MYR230mn p.a (SGD64mn-SGD74mn p.a.). FNN's 55.5% ownership of FNNB implies upstreaming of MYR110mn-MYR126mn p.a. (SGD36mn-SGD41mn p.a.) to FNN. For Vinamilk, it has been consistently paying dividends (FY16: VND7.2bn), and has maintained a dividend policy rate of at least 50% of profit after tax. We can expect further upsides to Vinamilk's dividends given its rapid growth rates with a target to grow revenue at a 11.2% CAGR to VND80,000bn in 2021. We expect FNN to receive more than SGD55.6mn dividends from Vinamilk in 2017. In total, we can expect at least SGD91.6mn of dividends from FNNB and Vinamilk, which supports net debt of SGD99.7mn. The subsidiaries and associates also provide FNN with some liquidity when needed as they are listed. FNN's stakes in FNNB and Vinamilk are worth SGD4.2bn.

Figure 18: Dividends paid by FNNB



Source: Company, OCBC

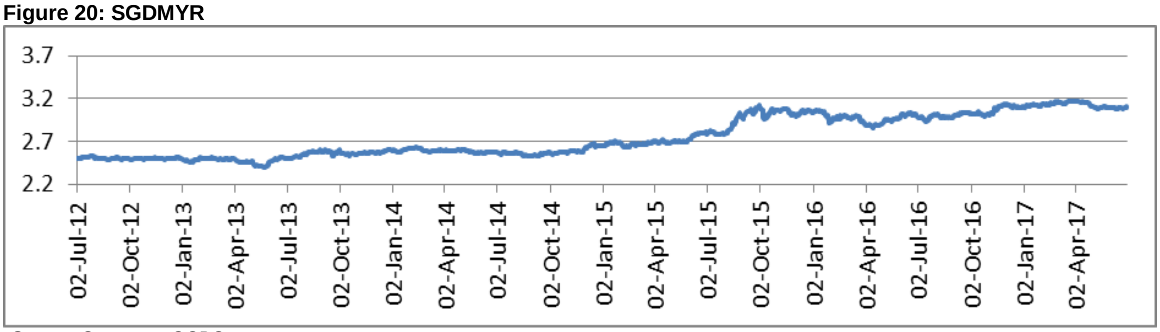
Figure 19: Dividends paid by Vinamilk



Source: Company

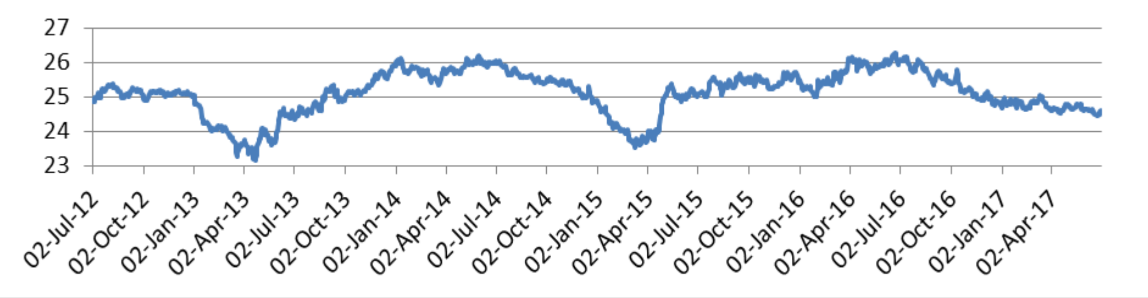
- **FX risks to be managed:** FNN is exposed to MYR and THB volatility with revenue from Malaysia (41%) and Thailand/Other ASEAN (30%). We think higher FX risks from VND have to be managed going forward as we expect Vinamilk will account for 56% of FNN's total assets and 49% of PBIT. FNN has a policy to cover 50%-90% of the FX exposure from transactions in foreign currencies using forwards with a maximum period of 12 months, though this may be ineffective to hedge FX exposure on the balance sheet over the longer term. Thus far, VND and THB appears to be relatively stable against the SGD. However, the MYR has depreciated over 20% since 2012.

Figure 20: SGDMYR



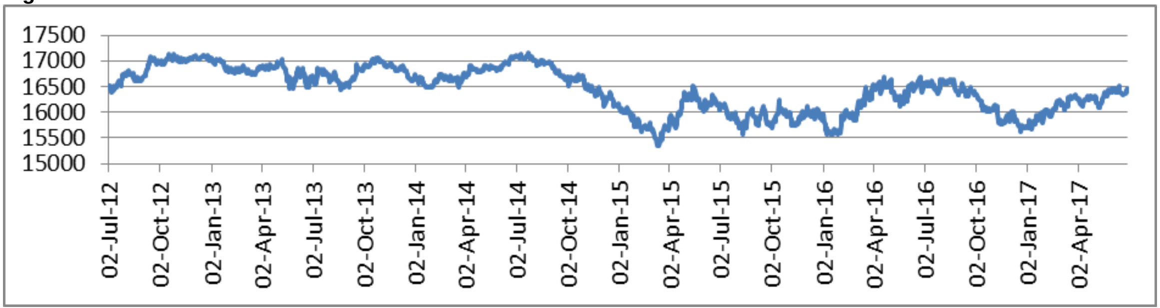
Source: Company, OCBC

Figure 21: SGDTHB



Source: Company, OCBC

Figure 22: SGDVND



Source: Company, OCBC

- **Access to capital markets suggests that goodwill has been rebuilt:** Thus far, FNN has issued SGD260mn in SGD bonds in Mar and Apr 2017. This follows a hiatus by FNN from the bond market after it threatened to default in 2013. Back then, FNN looked to spin out Frasers Centrepoint Ltd and launched a consent solicitation[7] with a buyback price that was deemed unfavourable to certain investors, who were holding FNN bonds that were previously trading as high as 107. If the consent was not obtained, an event of default would occur and the repayment of the bonds would be at par + accrued. This was eventually resolved when FNN revised its offer. Going forward, we think that goodwill appears to have been rebuilt as FNN received more than SGD500mn in orders for its SGD100mn bond printed in Apr 2017.

V) Technical Considerations

Positives

- Visible retail presence
- Diversification into a rare F&B issuer

Negatives

- HoldCo-OpCo subordination
- No credit rating
- Supply risk

Relative Value

Issue	Maturity	Ask YTW	Yield Spread	Bond Rating	Net Debt/ EBITDA	Net Gearing
FNNSP 3.09 '22	23/03/2022	2.93%	124bps	NR/NR/NR	0.6x	0.03x
FNNSP 3.8 '27	21/04/2027	3.71%	153bps	NR/NR/NR	0.6x	0.03x
FCLSP 3.95 '21	07/10/2021	2.98%	135bps	NR/NR/NR	9.4x	0.74x
FCLSP 4.15 '27	27/02/2027	3.96%	179bps	NR/NR/NR	9.4x	0.74x
FCT 3 '20	21/01/2020	2.39%	103bps	BBB+/NR/NR	6.8x	0.43x

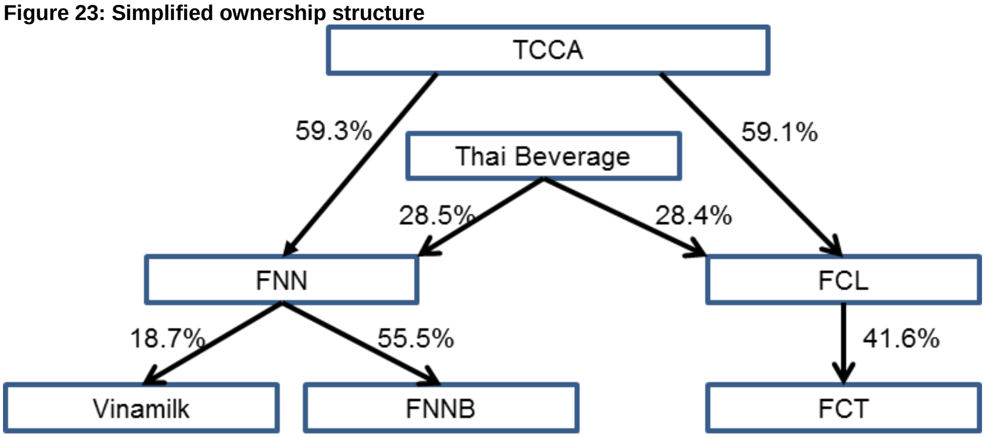
*Indicative spreads based on offer prices from Bloomberg on 28/06/17

[7] Includes buying back the bonds at par + accrued + half of the bond's coupon

FNN is a rare F&B issuer in the SGD space, and as such we do not find close comparables. Compared to Frasers Centrepoint Ltd ("FCL"), which is a property company that is similarly controlled by Mr Charoen and his wife, we think that FNNSP bonds look interesting trading only 10-20bps tighter in yield spread than FCLSP bonds given the far lower net gearing. However, we note FNN's potential to step up on the acquisition front.

We compare to Frasers Centrepoint Trust ("FCT"), even though it is a retail REIT, as it is linked to Charoen with 41.6% ownership by FCL and FCL as the REIT manager. For investors comfortable with an unrated bond, FNNSP '22 offers 21bps yield pickup over FCTSP '20s with a lower net gearing and net debt/EBITDA though FCT has a credit rating from Moody's (Baa1/Stable). However, we note that FNN is subject to HoldCo-OpCo risks as a substantial part of its revenue and PBIT are contributed by FNNB and Vinamilk, though we think that subordination risks from FNNB is manageable given its low debt while FNN holds a controlling stake.

Figure 23: Simplified ownership structure



Source: Company, OCBC

VI) Conclusion & Recommendation

Overall, FNN offers a good credit profile with its cashflow generative businesses and healthy balance sheet. We like FNN as it is a diversified F&B player, selling a variety of well-known beverages and dairy products. The diversity of the product-mix has helped FNN maintain its profitability despite pressure from higher sugar prices and competition in Malaysia's beverages segment. Meanwhile, earnings and cashflows are set to increase from an increase in its stake in Vinamilk. That said, we think that FNN may continue to step up on acquisitions, which may pressure its balance sheet. We initiate **FNN with a Neutral Issuer Profile**.

We think that FNN's current credit metrics look interesting relative to FCL and FCT with lower net gearing and net debt/EBITDA while FNNSP '22s and '27s offer a decent yield of 2.9% and 3.7% respectively. In addition, FNN is a rare issuer in the F&B space, which can offer investors some diversification in the SGD market. However, in view of the potential to further increase leverage and supply risk, we initiate **FNN's bonds with a Neutral recommendation**.

Frasers & Neave Ltd

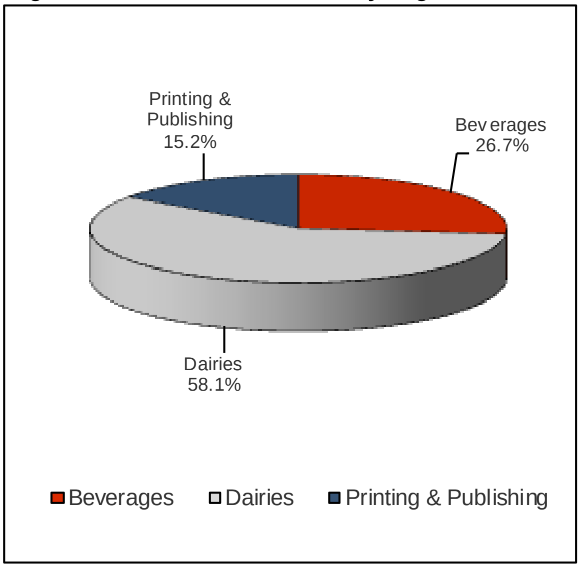
Table 1: Summary Financials

Year End 30th Sep	FY2015	FY2016	1H2017
Income Statement (SGD'mn)			
Revenue	2,121.1	1,978.6	946.3
EBITDA	141.7	161.8	90.1
EBIT	74.4	115.0	60.8
Gross interest expense	6.3	5.0	3.9
Profit Before Tax	101.7	188.2	72.2
Net profit	63.0	108.1	30.6
Balance Sheet (SGD'mn)			
Cash and bank deposits	961.7	1,042.6	667.3
Total assets	3,142.9	3,772.9	4,381.2
Gross debt	100.5	137.0	767.0
Net debt	-861.2	-905.6	99.7
Shareholders' equity	2,556.1	3,152.5	3,165.0
Total capitalization	2,656.6	3,289.6	3,931.9
Net capitalization	1,694.8	2,247.0	3,264.6
Cash Flow (SGD'mn)			
Funds from operations (FFO)	320.2	154.9	59.9
* CFO	224.8	184.7	50.9
Capex	56.1	65.5	29.6
Acquisitions	11.8	35.8	952.3
Disposals	559.5	0.4	0.4
Dividend	101.6	98.9	59.6
Free Cash Flow (FCF)	168.8	119.2	21.3
* FCF adjusted	614.9	-15.1	-990.2
Key Ratios			
EBITDA margin (%)	6.7	8.2	9.5
Net margin (%)	3.0	5.5	3.2
Gross debt to EBITDA (x)	0.7	0.8	4.3
Net debt to EBITDA (x)	-6.1	-5.6	0.6
Gross Debt to Equity (x)	0.04	0.04	0.24
Net Debt to Equity (x)	-0.34	-0.29	0.03
Gross debt/total capitalisation (%)	3.8	4.2	19.5
Net debt/net capitalisation (%)	-50.8	-40.3	3.1
Cash/current borrowings (x)	377.0	85.3	1.4
EBITDA/Total Interest (x)	22.5	32.6	23.3

Source: Company, OCBC estimates

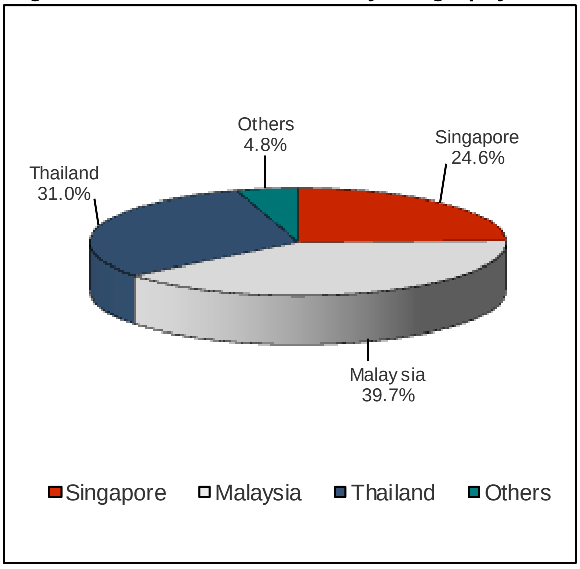
**FCF Adjusted = FCF - Acquisitions - Dividends + Disposals | *CFO after deducting interest expense*

Figure 1: Revenue breakdown by Segment - 1H2017



Source: Company

Figure 2: Revenue breakdown by Geography - 1H2017



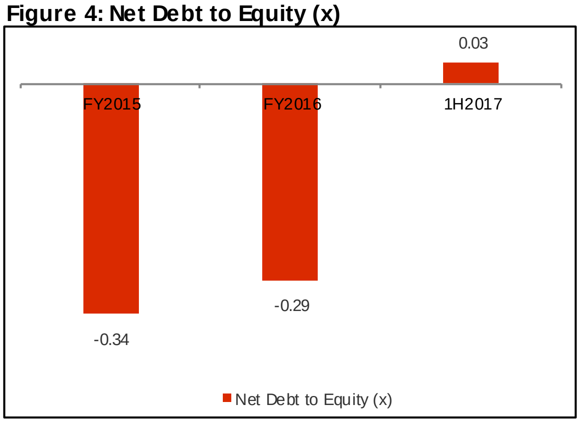
Source: Company

Figure 3: Debt Maturity Profile

Amounts in (SGD'mn)	As at 31/03/2017	% of debt
Amount repayable in one year or less, or on demand		
Secured	0.2	0.0%
Unsecured	491.7	64.1%
	491.9	**64.1%**
Amount repayable after a year		
Secured	0.0	0.0%
Unsecured	275.0	35.9%
	275.1	**35.9%**
Total	**767.0**	**100.0%**

Source: Company

Figure 4: Net Debt to Equity (x)



Source: Company, OCBC estimates