

Earnings Review: Fraser and Neave Ltd (“FNN”)

Recommendation

- FNN continues to run on a single engine, with Dairies contributing SGD51.6mn out of SGD36.3mn total reported EBIT (with other segments posting losses) in 2QFY2018. The growth in Dairies reported EBIT (+29.6% y/y) was largely due to Vinamilk’s contribution as share of associated companies’ profits. We estimate that Dairies reported EBIT would have declined ~10% y/y to ~SGD35mn without Vinamilk.
- Net gearing climbed q/q to 13.3% (1QFY2018: 8.1%) with additional investments in Vinamilk. Nevertheless, credit metrics remain intact, backed by cashflows generated from operations (1HFY2018: SGD45.1mn). As such, we continue to hold FNN at a Neutral (4) Issuer Profile.
- In our view, FNNSP 3.09% ‘22s and FNNSP 2.8% ‘22s look fully valued trading around 63-78bps spread. While there is no close comparable, for exposure to the F&B space, investors may consider BREAD 4% ‘23s. Although OUE Ltd has a higher net gearing, we find OUESP ‘22s more attractive than both FNNSP ‘22s with 75bps spread pickup.

Relative Value:

Bond	Maturity date	Net gearing	Ask Yield	Spread
FNNSP 3.09% ‘22s	23/03/2022	0.13x	2.95%	63bps
FNNSP 2.8% ‘22s	22/08/2022	0.13x	3.14%	78bps
BREAD 4% ‘23s	17/01/2023	0.24x	3.94%	155bps
OUESP 3.75% ‘22s	17/04/2022	0.57x	3.82%	153bps

*Indicative prices as at 10 May 2018 Source: Bloomberg, OCBC, Company
Net gearing based on latest available quarter*

Issuer Profile: Neutral (4)

Ticker: **FNNSP**

Background

Fraser & Neave Ltd (“FNN”) is a consumer group engaged in Food & Beverage (“F&B”) and Publishing and Printing (“P&P”) businesses. FNN is a F&B market leader in Southeast Asia, with brands including 100Plus, F&N Nutrisoy, F&N Seasons, F&N Magnolia and Farmhouse. FNN’s P&P business include Marshall Cavendish and Times Publishing. FNN owns 55.5% stake in Fraser & Neave Holdings Bhd (“FNNB”) and 19.06% stake in Vietnam Dairy Products (“Vinamilk”). FNN is owned by TCC Assets (59.3%) and Thai Beverage (28.5%), both linked to Charoen Sirivadhanabhakdi.

Key Considerations

- **Mixed results with Beverages still struggling:** FNN reported 2QFY2018 results. Revenue increased 4.8% y/y to SGD473.1mn, contributed by (1) Beverages segment (+10.6% y/y to SGD125.6mn) with successful execution of CNY festive promotions and (2) Dairies segment (+4.7% y/y to SGD284.4mn) which benefited from pricing promotions and growth in export sales. However, reported EBIT for Beverages remained lacklustre, posting a small loss of SGD0.8mn though this has improved y/y (2QFY2017 loss: SGD5.2mn) as a result of increased sales and lower sugar input cost. Dairies reported EBIT surged 29.6% y/y to SGD51.6mn though this is mainly due to the additional profit contribution by associate Vinamilk. Without Vinamilk, based on reported EBIT contribution by Vietnam (SGD15.6mn) we estimate reported EBIT would have declined ~10% y/y to ~SGD35mn, mainly due to lower contribution from Malaysia Dairies (affected by higher raw material prices). Overall, net profit rose 28.4% y/y to SGD301.mn due to contribution by Vinamilk, boosting share of associated companies profits to SGD17.1mn (2QFY2017: SGD1.5mn).
- **Credit metrics remain healthy, for now:** Net gearing climbed q/q to 13.3% (1QFY2018: 8.1%) due to investments in associated company (SGD125.8mn), which should be due to the purchase of additional stakes in Vinamilk. We think net gearing may continue to head higher as FNN may continue purchasing additional stakes in Vinamilk, with a gearing policy of up to 80%. FNN is also looking to invest in new markets. Meanwhile, we are comforted by its cashflow generative profile, with cashflows generated from operations (1HFY2018: SGD45.1mn) exceeding finance cost (1HFY2018: SGD15.2mn).
- **Losses at Printing & Publishing expected to narrow:** Reported EBIT losses deepened to SGD8.4mn for the printing & publishing segment (2QFY2017 reported EBIT loss: SGD5.6mn). This is due to timing differences which impacted sales and shift in product mix in Publishing. FNN expects the losses to narrow in FY2018.

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Explanation of Issuer Profile Rating / Issuer Profile Score

Positive (“Pos”) – The issuer’s credit profile is either strong on an absolute basis, or expected to improve to a strong position over the next six months.

Neutral (“N”) – The issuer’s credit profile is fair on an absolute basis, or expected to improve / deteriorate to a fair level over the next six months.

Negative (“Neg”) – The issuer’s credit profile is either weaker or highly geared on an absolute basis, or expected to deteriorate to a weak or highly geared position over the next six months.

To better differentiate relative credit quality of the issuers under our coverage, we have further sub-divided our Issuer Profile Ratings into a 7 point Issuer Profile Score scale.

IPR	Positive		Neutral			Negative	
IPS	1	2	3	4	5	6	7

Explanation of Bond Recommendation

Overweight (“OW”) – The performance of the issuer’s specific bond is expected to outperform the issuer’s other bonds, or the bonds of other issuers either operating in the same sector or in a different sector but with similar tenor over the next six months.

Neutral (“N”) – The performance of the issuer’s specific bond is expected to perform in line with the issuer’s other bonds, or the bonds of other issuers either operating in the same sector or in a different sector but with similar tenor over the next six months.

Underweight (“UW”) – The performance of the issuer’s specific bond is expected to underperform the issuer’s other bonds, or the bonds of other issuers either operating in the same sector or in a different sector but with similar tenor over the next six months.

Other

Suspension – We may suspend our issuer rating and bond level recommendation on specific issuers from time to time when OCBC is engaged in other business activities with the issuer. Examples of such activities include acting as a joint lead manager or book runner in a new issue or as an agent in a consent solicitation exercise. We will resume our coverage once these activities are completed.

Withdrawal (“WD”) – We may withdraw our issuer rating and bond level recommendation on specific issuers from time to time when corporate actions are announced but the outcome of these actions are highly uncertain. We will resume our coverage once there is sufficient clarity in our view on the impact of the proposed action.

Analyst Declaration

The analyst(s) who wrote this report and/or her or his respective connected persons did not hold securities in the above-mentioned issuer or company as at the time of the publication of this report.

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