Fan Milk Plc 9M2023 Results

Current rating **UNDER REVIEW**

Ghana | 01 November 2023

Rolling with the punches

Fan Milk Plc ("FML") released its unaudited 9M2023 financial results yesterday, reporting impressive profit outturn. The large ice cream producer churned out a net profit of GHS 16.8mn, from a loss position of GHS 16.8mn in the prior comparable year. Our assessment of the 9M2023 financial results showed that a 1.8% y/y decline in input cost, together with strict containment of operating expenses and over 3-fold increase in finance income were major contributors to FML's profit outturn. Despite a sharp moderation in revenue growth to 7.8% y/y in 9M2023 (vs +14.0% y/y in 1H2023), management's explanation suggests a one-off challenge on a flagship product and eases our concerns about the outlook for top-line growth. Consequently, we anticipate a rebound to double digits revenue growth in 4Q2023 amidst ongoing OPEX control, although elevated inflation and re-emerging depreciation pressure caps our optimism on earnings outlook.

Performance: A decline in input cost amidst operational cost control sustains profit momentum

- FML reported a net profit of GHS 16.8mn in 9M2023, switching from a loss position of GHS 16.8mn in 9M2022
- Revenue increased by 7.8% y/y to GHS 412.1mn, mainly reflecting the upward price adjustments implemented in 9M2023 which was partly offset by challenges experienced on FANYOGO quality in 3Q2023 that adversely impacted sales on the product
- Input costs reduced by 1.8% y/y to GHS 274.3mn, driven by a fall in the price of FML's key input material such as skimmed milk powder (-38.9% y/y)
- However, we observed a 48.4% y/y rise in the price of cocoa futures, together with 22.9% and 22.3% YTD depreciation of the Cedi against the US Dollar and the Euro, respectively, in 9M2023. This dampened the benefit from the fall in price of input material such as skimmed milk powder
- Operationally, FML maintained a firm grip on OPEX, allowing a modest increase in operating expenses to GHS 122.9mn (+5.8% y/y)
- Although management contained the rise in sales and distribution cost at 3.0% y/y, administrative expenses witnessed a 24.2% y/y surge, on account of the prevailing high inflation which averaged 44.3% in 9M2023 (vs 25.9% in 9M2022)
- As a result of the controlled OPEX amidst the macroeconomic pressures, FML's operating margin improved by 7.1.pps, from -2.7% in 9M2022 to 4.3% in 9M2023
- Finance cost increased by 44.2% y/y to GHS 21.1mn in 9M2023
- However, finance income spiked over threefold (+211.0% y/y) to GHS 25.8mn, offsetting the higher interest paid on finance cost
- Resultantly, net profit margin improved from -4.4% in 9M2022 to +4.1% in 9M2023

Outlook: Poised to close FY2023 with first annual profit in three years

- In 4Q2023, we expect the upcoming festive season to drive demand across the FML brands and support the firm's focus on the four strategic pillars: expanding outdoor channels, accelerating the indoor channels, growing the ice cream brand, and promoting the export business. These outcomes should power a rebound in top-line growth to double digits in 4Q2023 and support a return to annual profit for the first time since FY2020.
- We take note of management's productivity enhancing initiatives, such as the use of biomass energy, which is positive and bodes well for the outlook on gross profit margin
- Despite intense competition, we anticipate that FML will keep expanding its agent base and footprint in the outdoor channel
- On the cost front, we are optimistic that FML will keep its grip on OPEX as inflationary pressures continue to moderate in the months ahead. We also expect input cost to remain under control in the short-term as price of skimmed milk powder stays depressed.

Valuation: Under Review

- We are in the process of re-initiating coverage on FML and have therefore placed our recommendation under review
- FML is trading at a PE of 21.5x and EV/SALES of 0.91x

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