Fan Milk Plc 1Q2025 Results

Current rating: UNDER REVIEW

Current Price: GHS 3.80

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FML hits the ground running

Fan Milk Plc ("FML") released its unaudited 1Q2025 financial results on 02 May 2025, reporting an impressive profit outturn. The large ice cream producer churned out a net profit of GHS 24.1mn, representing a 65.9% y/y improvement. The profit outturn was mainly underpinned by a 56.7% y/y increase in revenue to GHS 242.2mn and an 80.4% y/y plunge in finance cost to GHS 1.3mn. The impressive topline growth in the current period suggests a potential recovery in export performance, indicating that prior challenges impacting export sales may have been effectively addressed, thereby supporting overall revenue expansion. However, we await topline performance in the quarters ahead for sustainability. Gross margin declined by 1.0pp to 37.5%. This suggest that cost pressures may have outweighed potential gains from material price negotiations, product mix optimization, and targeted sales promotions strategies which Fan Milk Limited has historically employed to mitigate cost volatility. Input costs surged by 59.2% y/y to GHS 151.5mn, while operating expenses rose by 30.2% y/y to GHS 60.3mn. We attribute the sharp increase in input costs to a 17.1% y/y depreciation of the Cedi against the US Dollar and a 9.3% y/y rise in the price of skimmed milk powder. Additionally, the uptick in operating expenses was largely driven by higher utility costs and increased spending on promotional and advertising activities. Overall, we are impressed by the significant surge in earnings, mainly supported by the focus on productivity initiatives and topline growth. With FML's 1Q2025 topline and earnings exceeding our estimates by 19.8% and 66.8% respectively, we believe this performance sets a solid foundation for a positive outturn in FY2025 as macroeconomic conditions improve

1Q2025 Performance: An increase in revenue and a plunge in finance cost propelled bottom-line growth

- FML reported an impressive 65.9% y/y surge in net profit to GHS 24.1mn in 1Q2025, mainly as a result of a 56.7% y/y increase in revenue to GHS 242.2mn and an 80.4% y/y plunge in finance cost to GHS 1.3mn.
- Input costs increased by 59.2% y/y to GHS 151.5mn, driven by a 9.3% y/y increase in the price of skimmed milk powder, FML"s key input material, coupled with a 17.1% y/y depreciation of the Cedi against the US Dollar.
- Meanwhile, we observed an 18.0% y/y decline in the price of cocoa futures, which, given cocoa powder's relevance in FML's product mix, could provide some relief to input cost pressures in the near term.
- Furthermore, OPEX elevated by 30.2% y/y to GHS 60.3mn, above 1Q2025 average inflation of 23.0% (vs 1Q2024 average inflation of 24.2%). Operating expense was mainly driven by a 47.8% y/y surge in administrative expense to GHS 20.1mn and a 27.3% y/y rise in sales and distribution expense to GHS 33.5mn. In our view, the rise in administrative expense was underpinned by higher utility cost and promotion & advertising.
- Other income declined by 40.8% to GHS 0.7mn
- Operating profit surged by 117.8% y/y to GHS 31.1mn
- As a result, FML's operating margin increased by 3.6pp to 12.8% in 1Q2025.
- Gross margin decreased by 1.0pp to 37.5%
- Finance cost impressively plunged by 80.4% y/y to GHS 1.3mn, while finance income plummeted by 72.1% y/y to GHS 3.4mn in 1Q2025.
- Resultantly, net profit margin inched up by 0.6pp to 10.0% in 1Q2025.

Outlook: We are optimistic about FY2025 top-line performance but cost containment is necessary for earnings sustainability

Cost Management and Margin Performance

- We expect management to maintain stringent cost control measures, as previously demonstrated, to support margin expansion and cushion potential bottom-line pressures in 2025. While input costs are likely to remain contained in the near term amid moderating inflation, the risk of rising skimmed milk powder and cocoa prices could exert upward pressure. In this context, we believe effective cost containment will be crucial in protecting margins and sustaining profitability amid ongoing market volatility.

Revenue Momentum and Export Recovery

- We anticipate that FML's revenue momentum will be sustained in FY2025, supported by the robust 1Q2025 topline growth of 56.7% y/y, which exceeded our estimates by 19.8%. The surge in revenue suggests a potential recovery in export sales. However, we await further clarity from management at the upcoming AGM on 16 May 2025. In the near term, we expect the company to leverage its enhanced distribution network and strategic promotional activities to drive topline expansion.

Strategic Initiatives and Operational Efficiency

- Fan Milk is advancing its vendor automation initiative to enhance sales visibility and strengthen its direct-to-market reach. The company's data automation strategy serves as a critical tool for enabling data-driven decision-making to drive growth. By piloting the vendor automation process, FML aims to gain deeper insights into vendor sales locations, optimizing its sell-out strategy. We expect this initiative to support the company in expanding its distribution network and deepening market penetration across key local markets.

Local Sourcing and FX Mitigation

- We anticipate that the company will intensify its local sourcing efforts to mitigate foreign exchange risk, a strategic move that could cushion margins against currency volatility and reduce dependency on imported raw materials. For the 2025 financial year however, the improved prospect of FX stability will ease the FX impact on input cost and support a recovery in gross margin

Energy Cost Management and Sustainability

- FML's strategic shift from diesel, gas, and electric boilers to biomass-powered systems continues to shield the company from energy cost volatility. By reducing reliance on electricity for electric boilers, FML mitigates exposure to rising electricity tariffs, while also dampening the impact of fluctuating fuel prices. While the Ghanaian authorities continue to implement quarterly utility tariff hikes with the recent hike in May 2025, we expect FML's energy cost management strategy to remain instrumental in containing production costs and supporting margin in the near to medium term.

Favorable Operating Environment

- As macroeconomic conditions gradually improve, we expect FML to benefit from a more favorable operating environment in the coming quarters. With 1Q2025 topline and earnings exceeding our expectations, we believe the company is well-positioned to capitalize on improving consumer spending and demand recovery, setting a positive tone for FY2025 performance.

Summary of Outlook

- Looking ahead, we maintain a positive outlook for FML's FY2025 performance, driven by strong revenue momentum. We expect management's emphasis on vendor automation and distribution network expansion to further bolster topline growth. While 1Q2025 revenue exceeded our expectations and indicates a potential recovery in export sales, we await further insights from management at the upcoming AGM for additional clarity.

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 TTM P/E of 5.6x and EV/SALES of 1.3x

Key risks to valuation

A slower-than-expected decline in inflation, FX volatility, elevated interest rates, utility tariff hikes, higher energy prices, spike in the price of skimmed powder, intense competition and proposed tax reforms by the new Ghanaian administration could impact FML's financial performance.

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