

Date 20 January 2021

* Covid-19 has triggered a major downturn in global markets and shock impacts will still need to be assessed within the near future. It is too early to accurately forecast the full negative impact and all market participants are advised to exercise extreme caution.



RESULTS UPDATE

RFG had a decent 2020 financial year as they traded throughout the Covid-19 crisis and households stocked up on long life products, inflating sales by 22.2% in March. As we expected, dry foods and canned meat performed exceptionally while pie and fruit juice sales struggled under the hard lockdown regulations.

- Group revenue grew by 8.3% to R5.9bn off strong growth by the International segment which grew by 15.5% to R1.2bn, staging a pleasing recovery in H2 driven by currency depreciation and strong export volume growth from July 2020.
- Regional sales grew by 6.6% to R4.6bn with Fresh Foods and Long Life Foods increasing 1.7% and 9.6%, respectively.
- The operating profit margin dropped 40bps to 6.9% due to an adverse change in the sales mix and China products sold at far lower margins.
- Profit after tax and normalised HEPS were relatively flat at R216m and 82.7cps, respectively. Including the impairment and loss on disposal of PPE, HEPS grew 3.2% to 86.7cps. Dividend per share increased 3.2% to 28.8cps, an indication of a successful year for the food processing company despite Covid-19.

The International division reported an operating loss of R44.0m during the first half and recovered to post a profit of R36.6m for the year. While the depreciation of the Rand has positively impacted top-line sales and profitability, the benefit was negated by significantly lower sales in China and a foreign exchange loss of R54.6m as the Group uses forward exchange contracts (FECs) as a currency hedge on forward sales. The International division had an operating margin of 2.9% from 3.4%, mainly due to the loss in H1. Management advised shareholders that such a significant loss should not be experienced again as they expect profits from China to return. Management targets operating margins for the International division to stabilise at ~10%.

There is sustained demand for canned foods into FY21 and pie sales are showing a pleasing turnaround with restrictions now greatly eased while fruit juice sales are buoyant both locally and internationally. However, RFG is running below its 5-year CAGR in terms of revenue and we expect volumes to remain subdued over the next few months.

RFG is upgrading its bakery facility in Gauteng to accommodate the KZN consolidation and plan on installing a new fruit juice line in Wellington as well as upgrades at the baby food factory in Groot Drakenstein. Management previously held back on developments to preserve cash and now plans capex for FY21 of R250m compared to only R160m in FY20. They are also not against new acquisitions and will be looking to expand categories where they have very low market share. Capital developments will be funded with cash generated through the business which increased 21.6% in FY20.

Whilst management targets top line growth of 10%-15%, we think the Group can achieve growth in the range of ~9% given the lackluster consumer spending environment, high unemployment, and muted volumes through retail stores. When we strip out the effects of lockdown on juice and pie sales and include the uplift seen in canned meats (long life products), we do anticipate a recovery in operating margins from the current low of 6.9% but interim margins will continue to suffer due to the planned closing and restructuring of facilities in KZN. Second half margins should be stronger when costs normalise and sales rebound to former levels. We forecast operating margins for FY21 of 7.3%, increasing to 7.5% in FY22, owing to the stabilisation of the international business and recovery in Fresh Foods volumes.

We forecast ambitious growth in HEPS of 23.6% to 107cps in FY21 and HEPS of 123cps in FY22.

VALUATION

RFG retains a strong and well diversified range of products with good market share in their respective categories and is relatively better positioned than its competitors due to its focus on the mid to high LSM markets. This helps insulate the Group from a pressured lower-income consumer. The debt-to-equity is at a comfortable ratio of 43% from 47% and cash generated from operations is improving despite a low spending environment.

Our relative P/E valuation, comparing Rhodes to other food producers and applying a generous 20% premium to the peer average, yields an implied forward P/E of 13.8x which places the share at a price of only R13.42. Our DCF valuation indicates that the share is **undervalued**, with a price target of R14.80. The DCF price indicates a more longer-term value of the company as we have used moderate cash flow forecasts over the next 5 years, with a discount rate of 16.0% and a terminal growth rate of 6%.

RFG – Rhodes Food Group Holdings Limited FY20 Results Equity Update

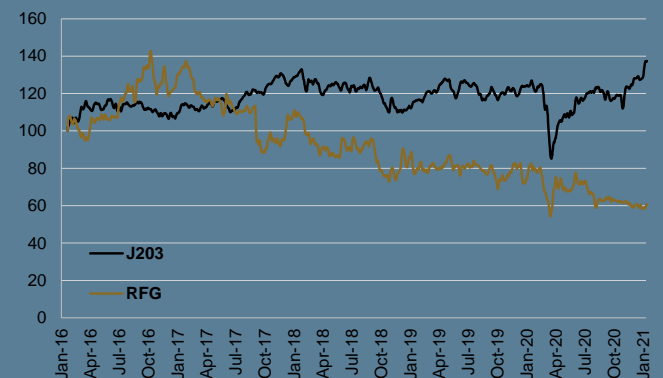
Valuation: **At Value**

RFG released results on 17 November 2020 for the period ended 27 September 2020

Price (R)	12.25
PE Fair Value (R)	13.42
DCF Value (R)	14.80
Upside(Downside) to DCF (%)	20.8%
DY %	2.4%

Price Performance	Absolute	Relative to JALSH
1 month	1.0%	-5.2%
3 month	-2.2%	-15.3%
YTD	1.4%	-6.3%
12 month	High	Low
(SA Rands)	17.50	6.06

No. of shares (m)	263	Price (R)	12.25
TNAV per share	9.90	Mkt cap (Rm)	3182
EV (Rm)	4351	Price/Book (x)	1.23



Growth rate	DCF Discount rate				
	12.0%	14.0%	16.0%	18.0%	20.0%
0%	23.86	17.85	14.25	11.85	10.13
2%	24.23	18.10	14.43	11.99	10.24
4%	24.59	18.35	14.62	12.13	10.35
6%	24.96	18.60	14.80	12.27	10.46
8%	25.32	18.85	14.98	12.41	10.57
10%	25.69	19.11	15.17	12.55	10.69
12%	26.05	19.36	15.35	12.69	10.80

Consumer Goods	Price	Mkt cap (m)	1 year fwd PE
Oceana*	67.59	8714	9.4
Tiger Brands*	212.65	39898	14.6
Astral*	125.80	5337	9.5
AVI	75.95	25262	14.3
Rhodes Foods	12.25	3182	12.6
Quantum Foods	6.01	1188	8.6
Average			11.5
*consensus forecasts used			10%
Rhodes Foods	12.25	3182	12.6
Premium (Discount) applied to average:			20.0%
Rhodes Foods: Implied current gain/(loss)	13.42	10%	13.8

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