# Del Monte Pacific

**P27.05 - BUY**


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**25 July 2013**

## Philippines
**Consumer**

| | |
|---|---|
| Reuters | DMPL.PS |
| Bloomberg | DMPL PM |

**Priced on 24 July 2013**
Phils Phisix @ 6,804.2

**12M hi/lo** /

| | |
|---|---|
| **12M price target** | P33.00 |
| **±% potential** | +22% |
| **Shares in issue** | 1.3m |
| **Free float (est.)** | 31.9% |
| **Market cap** | US$1m |

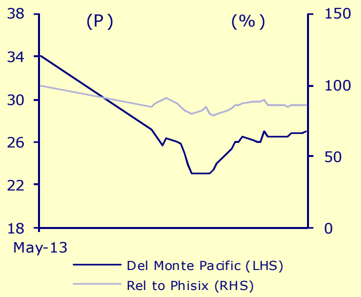
**3M average daily volume**
P30.1m (US$0.7m)

**Foreign s'holding** 87.6%

**Major shareholders**
NutriAsia Pacific Ltd. 67.1%

**Stock performance (%)**

| | 1M | 3M | 12M |
|---|---|---|---|
| Absolute | 17.6 | 0.0 | 0.0 |
| Relative | 3.2 | 0.0 | 0.0 |
| Abs (US$) | 19.4 | 0.0 | 0.0 |




Source: Bloomberg

www.clsa.com

# Sweet 15

Initiating coverage

**Del Monte Pacific Limited (DMPL) is one of the Philippines' leading processed food & beverage manufacturers, with a burgeoning global presence. Management is solidifying its position to maintain high profitability and deliver consistent growth. We expect operating and net income to manage 19% and 26% Cagrs over 2013-15, as long-term supply contracts from its non-branded business expire. We initiate on DMPL with a BUY, with target price of P33/sh implying a 23.8x 2014PE, and a 22% upside. ROEs to improve from 2012's 13% to 19% by 2015.**

### A household brand
DMPL is one of the leading processed food and beverages manufacturer in the Philippines. The company also holds the S&W brand globally (excluding Americas, Australia and New Zealand) and supplies the food-service and export markets. DMPL's goal is to establish itself as a global food marketer

### Digging a deep moat
The company is setting the stage, solidifying its competitive advantage to maintain high profitability and deliver consistent growth. The company has already established brand equity, owning trademarks to strong names. It operates one of the world's largest fully integrated pineapple operations. Its distribution network has also helped it tap the fragmented traditional trade

### Low hanging fruits
The company plans to leverage off its exposure to growth markets by using the Del Monte brand to introduce new products. The S&W brand will be used as a platform for regional exposure for its fresh and processed products. Further low-hanging fruit include the restructuring of its product mix into higher-margin businesses and the expiring of its long-term supply contracts. The turnaround of its joint venture in India and its waste-to-energy project are other imminent drivers

### Valuations
We expect Ebit to expand at a 19% three-year Cagr to US$84.8m in 2015, with margins at 13% as long-term supply contracts from its non-branded business expire. This is expected to add US$11-13m in operating profits from 2014-15, and 200bps to margins. We arrived at a DCF based fair valuation of P33/sh, crossed-checked with a PE and PE/G multiple. This implies a PE multiple of 23.8x on 2014 earnings.

### Financials

| Year to 31 December | 11A | 12A | 13CL | 14CL | 15CL |
|---|---|---|---|---|---|
| Revenue (US$m) | 425.2 | 459.7 | 504.7 | 560.8 | 632.6 |
| Net profit (US$m) | 25.7 | 31.2 | 34.6 | 41.5 | 60.0 |
| EPS (US$) | 0.02 | 0.02 | 0.03 | 0.03 | 0.05 |
| CL/consensus (0) (EPS%) | - | - | - | - | - |
| EPS growth (% YoY) | 76.8 | 21.1 | 10.9 | 20.0 | 44.8 |
| PE (x) | 31.5 | 26.7 | 23.1 | 19.3 | 13.3 |
| Dividend yield (%) | 3.3 | 3.8 | 4.3 | 4.9 | 3.9 |
| FCF yield (%) | 2.9 | 2.3 | 2.8 | 8.0 | 4.4 |
| PB (x) | 2.9 | 2.7 | 2.9 | 2.6 | 2.4 |
| ROE (%) | 11.4 | 12.8 | 12.9 | 14.2 | 18.8 |
| Net debt/equity (%) | 74.8 | 83.9 | 74.7 | 63.9 | 58.5 |

Source: CLSA

# A household brand

**A leading processed F&B manufacturer in the Philippines**

Del Monte Pacific Limited is one of the leading processed food and beverage manufacturers in the Philippines based on Euromonitor data, holding the trademark rights to the Del Monte brand for processed products in the Philippines, the Indian subcontinent and Myanmar. The company also holds the rights to distribute the S&W brand globally (except in the Americas, Australia and New Zealand) and has a 47% stake in FieldFresh from India, serving as a platform for its expansion globally. DMPL also has supply contracts and sells to private labels for supply of juices, processed fruits, concentrates and fresh pineapples for the export markets. Its single largest shareholder Nutriasia Pacific Limited is committed to building DMPL into a global food marketer.

**The Del Monte trademark is owned by different countries in respective regions**

Figure 1

**Del Monte trademarks globally**

| Company | Markets | Products |
|---|---|---|
| Del Monte Pacific Limited | Philippines, Indian sub-continent (India, Pakistan, Bangladesh, Sri Lanka, Myanmar, Bhutan, Nepal and the Maldives) | Processed food and beverage |
| Del Monte Asia Pte Ltd/ Kikkoman | Asia Pacific (excluding the Philippines, the Indian sub-continent and Myanmar) | Processed food and beverage |
| Del Monte Foods | USA ,South America | Processed food and beverage |
| Del Monte Canada Inc. | Canada | Processed food and beverage |
| Del Monte Fresh Produce | Worldwide (for fresh) Europe, Middle East, Africa (for processed F&B) | Fresh produce, processed food and beverage |
| Del Monte Pan-American | Central America, Caribbean | Processed food and beverage |

Source: CLSA Asia-Pacific Markets

**The group supplies fresh and processed fruits globally**

Figure 2

**DMPL's brand ownership**


Source: DMPL

**Del Monte's business is divided into the branded and non-branded segments, which account for 70% and 30% of revenue**

Del Monte's business is divided into the branded and non-branded segments, which accounted for 70% and 30% of 2012 revenue, respectively. The branded business sells processed and fresh products using the Del Monte and S&W brand name. The bulk (86%) of revenue comes from the Philippines, while the rest from Asia and the Middle East. The non-branded business composes of legacy supply contracts and sales to private labels for supply of juices, processed fruits, concentrates and fresh pineapples for the export markets. Some 56% of the non-branded business comes from non-supply contracts, with Europe and North America taking on two-thirds of total revenue.

Figure 3

**Revenue breakdown**

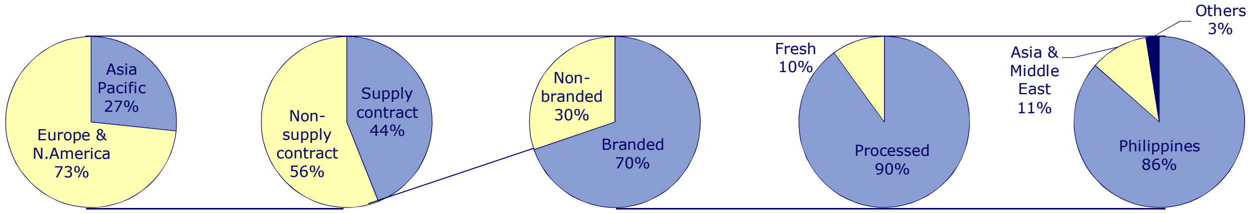
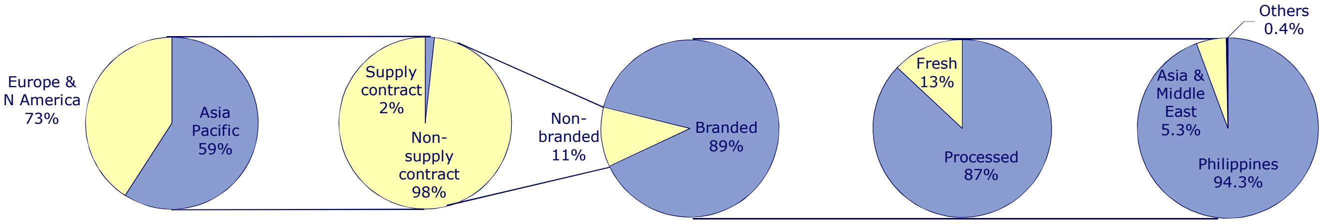



Figure 4

**Operating Ebit breakdown**




Source: CLSA Asia-Pacific Markets and Company data

Figure 5

**Countries and brands**

| Segment | Country | Brands/customers | Products |
|---|---|---|---|
| Branded | Philippines | Del Monte for processed | Culinary, beverage, processed fruits, fresh fruits |
| | Asia Pacific and Middle East | S&W for processed and fresh | Canned fruits, juices, beans, tomatoes, vegetables, fresh pineapples |
| | India | Del Monte for processed, FieldFresh for fresh | Canned fruits, juices, beans, tomatoes, vegetables, fresh pineapples |
| | Indian Subcontinent | Del Monte for processed | Beverage and processed fruits |
| Non-branded | North America | Del Monte Foods USA, Del Monte Canada | Processed fruits and concentrate |
| | Europe | Private labels | Processed fruits and concentrate |
| | Asia Pacific | Del Monte Asia/Kikkoman, private labels, Del Monte Fresh | Processed fruits, concentrate and fresh pineapples |

Source: CLSA Asia-Pacific Markets

Del Monte is setting the stage, solidifying its competitive advantage

# Digging a deep moat

Del Monte is setting the stage, solidifying its competitive advantage to maintain high profitability ratios and deliver consistent growth over time. The company has already established brand equity, built for the past eight decades. It has a solid market share in the Philippines, with plans to establish itself as one of the key brands in India and Myanmar. Likewise, S&W will be nurtured as DMPL's brand for processed and fresh products regionally. The company operates one of the world's largest fully integrated pineapple operations according to Department of Agriculture, and is the global low-cost producer of pineapples. DMPL operates an efficient supply chain, from production all the way to demand. Its extensive distribution network on the other hand allows easy scope for the fragmented traditional-trade market. Lastly, the key management team has immense experience in the FMCG industry with most of them having spent a number of years in internationally renowned companies.

The Del Monte brand has been in the market for the past eight decades

## Market share and brand equity

The Del Monte brand has been in the market for the past 12 decades, establishing itself as a well-known and trusted brand globally. The company boasts leading market shares in canned pineapple juice, mixed juice drinks, canned fruits, condiments and tomato and spaghetti sauces in the Philippines, according to Euromonitor, and plans to establish itself as one of the key brands in India and Myanmar. Likewise, S&W will be nurtured as DMPL's brand for fresh and processed fruit and vegetable products in Asia and the Middle East. The company continues to build its brand, with advertising and promotional expenses account for about 6% of sales in the Philippines in 2012. This fares higher than other consumer peers at only 2-3% of total sales in 2012. Del Monte's shelf space in the Philippines is also reflective of market share and expansion for key categories.

DMPL boasts leading market shares in certain categories in the Philippines,

Figure 6

**Market share and competitors in the Philippines**

| Category | Market share (%) | Competitors |
|---|---|---|
| Fruit and vegetable juices | 25 | Zest-O (Zest-O Corp) - 16%, Tropicana (Pepsi Co Inc) - 7%, Eight O'clock (Coca-Cola) - 4% |
| Canned Pineapple | 77 | Dole (Dole Food Co Inc) - 19% |
| Canned mixed fruits | 71 | Dole (Dole Food Co Inc) - 27% |
| RTD juice | 51 | Zest-O (Zest-O Corp) - 38%, Tropicana (Pepsi Co Inc) - 3%, Fun chum (8 o'clock) - 2%, Minute maid (Coca-Cola) - 2% |
| Tomato sauce | 77 | Hunt's (Hunt - URC) - 6%, RAM (Ram Foods products Inc) - 2% |
| Tomato Ketchup | 85 | Heinz (Heinz Co) - 3%, Hunt's (ConAgra Foods Inc) - 1%, Private Labels |
| Spaghetti sauce | 57 | White King Fiesta Spaghetti Sauce (RFM) - 9%, Royal Spaghetti Sauce (Unilever Foods Philippines) - 8%, Purefoods Spaghetti Sauce (San Miguel) - 4% |

Source: Euromonitor

**DMPL operates one of the world's largest fully integrated pineapple operations**

## Vertically integrated

DMPL operates one of the world's largest fully integrated pineapple operations and is the global low-cost producer of pineapples. The company operates an efficient supply chain, from production all the way to demand. DMPL operates 23,000 hectares of pineapple plantation in Southern Philippines, reaping 1.5 million pineapples a day on average. Its processing facility is only 30 minutes from the plantation, with a current annual capacity to process 700,000 tonnes of pineapples, representing about 20% of the world's processed pineapple production according to the Food and Agriculture Organization of the UN data. In the facility is an onsite can-making operation with a capacity of about 600,000 tonnes producing 150 million cans or six million cases per year, and a fresh pack house that yields 100,000 tonnes or 8.3m boxes of pineapples per year. Finally, its integrated seaport allows delivery of premium-quality products to world markets.

Figure 7

**DMPL operations**


Source: DMPL

**The company plans to increase its land utilisation by 5% per year on average**

The company plans to increase its land utilisation by at least another 20%, for its new sweeter variant of pineapple called MD-2 or the Sweet 16 brand which has already proven more popular than its Champaka variant which is used for processed products. The yield of a typical Champaka variant is at 175 MT per hectare (MTH), which is above global averages of 150 MTH.

**A third of DMPL's accounts are in the modern trade while the remaining 70% is catered to the traditional trade**

## An extensive distribution network

A third of DMPL's accounts are in the modern trade while the remaining two-thirds caters to the traditional trade. DMPL's products are distributed by its direct salesforce, regional distributors and independent business managers to supermarkets, grocery and sari-sari store outlets in the Philippines. Key accounts are handled by the salesforce directly while traditional trade is handled by 16 distributors, hitting 116,000 retail points (88,000 in beginning 2011). By end-2013, management is planning to increase by at least 10%. Distribution networks serve as the key foundation of DMPL's performance and will continue to do so in the years to come. As the retail market is such a fragmented industry, having the ability to distribute products to these retail outlets is critical.

Traditional trade is handled by 16 distributors, hitting 120,000 retail points

Figure 8

**Modern versus traditional**

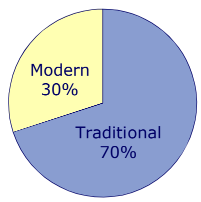
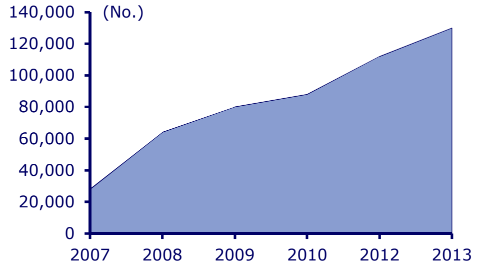



Figure 9

**Covered distribution points**




Source: CLSA Asia-Pacific Markets

## Experienced management team

The key management team has immense experience in the FMCG industry

The key management team has immense experience in the FMCG industry with most of them having spent a number of years in internationally renowned companies like Procter and Gamble, Kraft Foods, PepsiCo and Unilever at some point in their careers. We believe that the presence of different owners in the past has led to non-cohesive goals and strategies. Under the previous management teams, minimal efforts were placed in expanding the Philippines market. Few new products were launched with initiatives focused mainly on new packaging to expand its market presence. Since the entry of NutriAsia as the single largest shareholder, remarkable improvements in DMPL's operations have been quite evident. The revision of the long-term contracts with other Del Monte brand owners was one of the first developments that the new management brought to DMPL, which should bear fruit in 2015. Other important initiatives include improving its distribution network and expanding its business focus in the Philippines. Revenue has expanded at an 11% seven-year Cagr (2005 to 2012) and earnings at 8%.

NutriAsia group did not waste time in fixing immediate issues with DMPL

Figure 10

**DMPL management initiatives (since its entry in 2007)**

| Initiatives | Remarks |
|---|---|
| Supply contracts | Del Monte Foods (USA) - Amended Oct 2006 - clarified and enforced cost floor provision. Served notice of termination in Nov 2011, with three years notice, it will officially end Nov 2014. |
| | Fresh Del Monte Corp (EMEA) - terminated |
| | Fresh Del Monte Corp (Fresh) - Amended in Feb 2007 - Champanka prices will be replaced by higher priced MD-2 in three years. The most recent contract runs until 2017, which stipulates market prices for MD2 variety starting 2015. |
| | Del Monte Asia - New contract in Jan 2007 - Reduce prices in line with market and given direct access to private labels in Asia ex-Japan. |
| Distribution | Switched to 16 regional distributors from two nationwide distributors in the Philippines, effectively expanded to 116k distribution points, up from only 28k at end 2007. |
| Market expansion | S&W expands in Asia Pacific and Middle East for both processed and fresh pineapple. |
| Cost savings | Cost savings through increasing the number of tinplate suppliers to two. Other cost savings involving purchasing, logistics, rationalisation and cannery improvements. |
| Consolidation | Joint insurance procurement and advertising and promotion contracts with NutriAsia |
| Tax incentives | Tax incentives from the Philippines Economic Zone Authority (PEZA). Production from the cannery will be taxed at an amount equal to 5% of gross profit. |

Source: CLSA Asia Pacific Markets

# Low-hanging fruit and future prospects

**Management plans to leverage off its exposure to high-growth markets**

Management plans to leverage off its exposure to high growth markets by using the Del Monte brand to launch and introduce other packaged food products in the Philippines, India and Myanmar. S&W on the other hand, can be used as a platform for global exposure for its fresh products. Other low-hanging fruit includes the turnaround of its JV in India, a significant shift of product mix into higher-margin businesses for three key areas - the mix of branded versus non-branded, the mix of fresh versus processed and the mix of branded juice versus pineapple concentrate; the expiring of its long-term supply contracts; and cost savings from its waste-to-energy project.

## Access to high growth markets

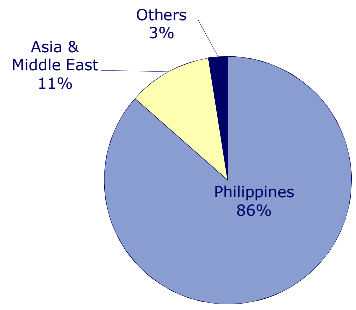
**Some 86% of Del Monte's branded business comes from the Philippines**

Some 86% of Del Monte's branded business comes from the Philippines, with 11% coming from Asia and the Middle East. Other revenue comes from the likes of Japan, Korea, Singapore and Hong Kong. Its geographic exposure includes markets with a young and affluent population that is climbing up the J-curve thanks to new job creation, low consumer gearing and rising disposable incomes. The rise in income will push large numbers of people past the level where discretionary spending takes off. As Figure 35 shows, US$3,000 per annum disposable income is the level of income where car ownership starts to take-off. We believe this is also the level of the inflection point where spending starts to take off. As can be seen, the majority of DMPL's revenue comes from markets that are expected to hit a consumption boom in the next decade.

Other revenues include the likes of **Japan, Korea, Singapore, Hong Kong, Myanmar and India**

Figure 11

**Revenue: Geographic breakdown**

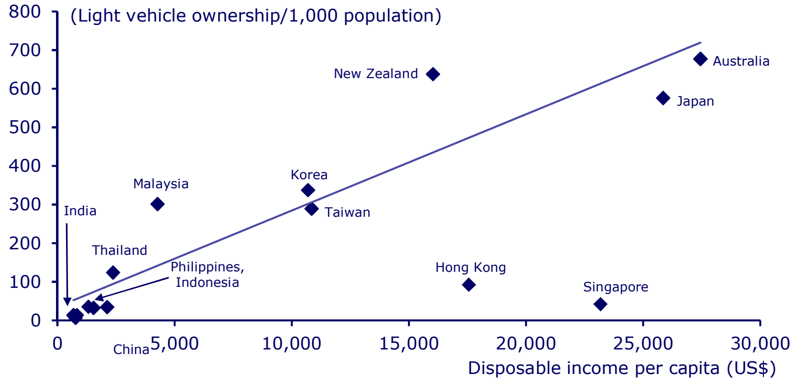



Source: CLSA Asia-Pacific Markets

US$3,000 per annum disposable income is the level of income where car ownership takes off

Figure 12

**Car ownership and disposable income**




Source: CLSA Asia-Pacific Markets

**Management plans to leverage off its presence in high growth markets**

Management plans to leverage off its presence in these high-growth markets by increasing it hectare utilisation by at least 20%, which will be supported by its recent expansion of an additional line for canned juices. Apart from DMPL's existing SKUs, the company can leverage off the Del Monte brand name to launch and introduce other packaged-food products in the Philippines, India and Myanmar. S&W on the other hand, can be used as a platform for global exposure. Since the acquisition of the S&W brand, DMPL has managed to grow sales by more than 10-fold to US$35m in 2012. Management has undertaken efforts to ride this momentum and penetrate new markets in the Asia Pacific region. We believe there exists significant growth opportunities for the S&W brand in Western Europe, Eastern Europe and Africa.

## Restructuring of product mix

**Management is aiming for a significant shift of product mix into higher margin businesses**

Management is aiming for a significant shift of product mix into higher-margin businesses for three key areas of the group - the mix of branded versus non-branded, the mix of fresh versus processed, and the mix of pineapple concentrate versus branded juice. The branded business now accounts for 70% of total revenue, versus only 50% in 2005. The branded business is significantly more profitable with gross profit margins at 30% versus DMPL's non-branded business which fetches a gross profit margin of only 11%. Management plans to increase the contribution of its branded business from 70% in 2012 to 80% by 2015. We expect that this will impact 2015 group-wide margins by at least at 50-100bps from current levels.

## Expiring of contracts

**The non-branded segment account for a big 30% of revenue**

The non-branded segment still account for 30% of revenue, down from 36% in 2011 due to weaker contribution from Europe and North America. In 2011 though, DMPL's European business turned around after the termination of an unprofitable supply contract. Selling prices and margins in Europe improved in 2011 as the group shifted out from its supply contract and sold directly to this market.

**The non-branded segment accounted for 36% of the business in 2011**

Figure 13

**OEM revenue and growth (US$)**

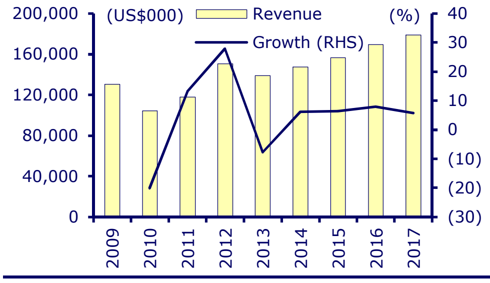
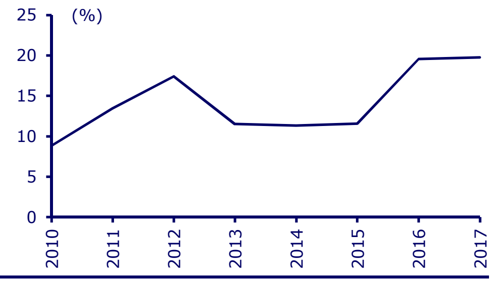



Figure 14

**OEM: Gross margin**




Source: CLSA Asia-Pacific Markets

**By November 2014, DMPL will be free from its Del Monte Foods (USA) long-term supply contract**

By November 2014, DMPL will be free from their Del Monte Foods (USA) long-term supply contract. DMPL supplies Del Monte Foods (USA) with processed pineapple. As of end-2012, DMPL sells more than US$45m under the supply contract generating low-single-digit margins. The upside is to be able to sell this under market rates of 15-20%. After November 2014, we expect to see an enhancement in DMPL's margin and profitability. Even if it were 15% versus breakeven, on US$40m that should be US$6m more profits for DMPL.

**The company also has a contract with Del Monte Fresh for fresh products until 2017**

Another similar case is a legacy contract that DMPL inherited. The company has a contract with Del Monte Fresh for fresh products until 2017. Del Monte Fresh is the global Del Monte Company that has the rights to all the fresh fruit and vegetables. DMPL supplies 1m boxes of fresh pineapple below cost

**Another contract that will expire in August next year (2014) is a toll packing agreement**

**The expiry of supply contracts will push up margins in 2015**

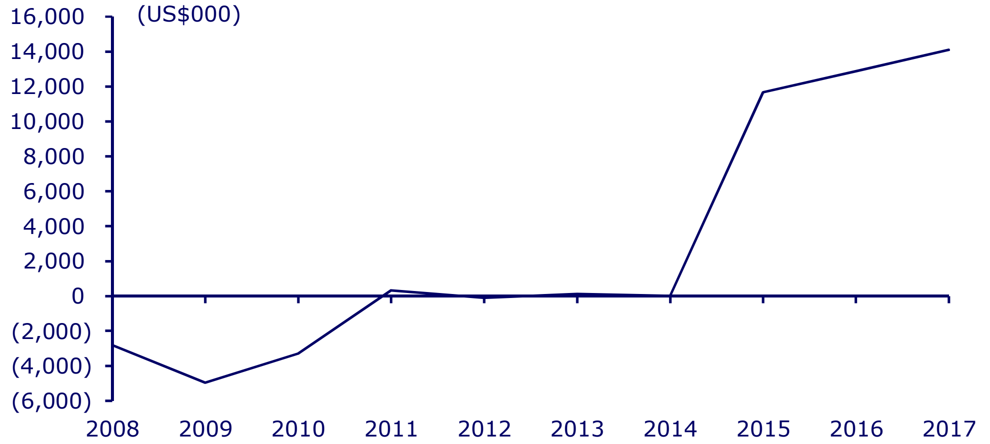
**DMPL is embarking on a waste-to-energy project**

(market price is at US$5.50-6 per box). From January 2015 onwards however, the contract will shift to market pricing until the end of the contract term in 2017.

Another contract that will expire in August next year (2014) is a toll packing agreement that DMPL has with San Miguel Corporation (SMC). DMPL has a toll packing agreement with San Miguel producing juice drinks in PET bottles under the brand "Fit and Right". These contracts were entered into when the Fit'n Right brand was launched. Margins for this business today are low and the company projects better margins after the expiry of the contract by August 2014. Adding total impact of expiring contracts on the bottom line would give a figure of roughly US$13m on operating profits. This figure is already 26% of DMPL's operating profit.

Figure 15

**Supply contracts: Operating profit**




Source: CLSA Asia-Pacific Markets

## Cost savings

DMPL is embarking on a wastewater-to-energy project that will capture methane gas from its waste-water treatment facility and convert it to energy. This will supply 80% of its cannery's energy requirement which will reduce electricity payments by US$2-3m per year. Currently, the Philippines has among the highest electricity costs at US$0.23-0.25/kWh and should exhibit little changes given supply factors are not expected to propagate significantly. A waste-water-to-energy facility will require a capex of US$16m (53% of total capex) spread over three years (2013 = US$6m, 2014 = US$4m, 2015 = US$6m) and is expected to come onstream by 2015, reducing electricity costs for DMPL.

# Earnings forecast and valuation

**We expect revenues to increase by an 11% 3-year Cagr from 2013-15**

We expect revenue to increase at an 11% three-year Cagr over 2013-15 and operating income to expand faster at an 18% three-year Cagr. We arrived at a fair valuation of P33/sh, implying a 23.8x PE on 2014 earnings, a discount to consumer names in the Philippines which trade at a 29x. At this range, the PE/G is 1.2x, but this comes down to 1.0x using a three-year Cagr. DMPL offers a 13% 13CL ROE, after a 11% average over the past three years, and returns are set to improve to 18% as the company gets rid of its supply contracts in 2015.

## 1Q13 results recap

**1Q13 revenues were up 17% to US$87m driven by branded business**

1Q13 revenues were up 17% to US$87m driven by branded business which grew at a higher rate of 27%. This comprised of the Philippine market as well as the S&W brand, while the non-branded business only grew by .1%. During the first quarter, the branded business contribution to Group sales increased to 68%versus non-branded which contributed 32%.

Operating profit was down 7.3% due to the weak performance of its non-branded segment and higher A&P spending. Higher logistic costs (higher by US$2.2m) was warehousing driven, related to its export market business. A&P was higher by US$.2b, driven by the company's new marketing head who believes in front loading A&P spending early in the quarter.

**We expect revenues to increase by an 11% 3-year Cagr from 2013-15**

We expect revenue to increase at an 11% three-year Cagr over 2013-15, driven by strong domestic consumption, the 5% growth in pineapple production, doubling of canning capacity and higher contribution from the branded business. Operating income should expand faster by an 18% three-year Cagr as a result of expiring long-term contracts and the shift of product mix to higher-margin businesses. We expect DMPL to generate US$84.8m in operating income in 2015 and US$63.7m in 2014, with operating margin of 13% in 2015, a 200bps jump from expected 2014's 11%.

**Asia and the Middle East will grow the fastest at a 22%**

We expect Asia and the Middle East will grow the fastest at a 22% three-year Cagr, while the Philippines at 11%. For non-branded, we estimate 8% growth for supply contracts for 2013-15 and a 6% growth for no-supply contracts. Note that 2015 factors in the changes in the supply contract with Del Monte Fresh which provisions a shift to market pricing until the end of the contract term in 2017. Operating profits for the non-branded business should see huge spikes in 2015 as the expiry of locked in pricing contracts bring margins up to market levels.

## Valuation

**We arrived at fair valuation of US$906m-1.1bn for DMPL**

We arrived at a DCF based fair valuation of P33/sh, crossed-checked with a PE and PE/G multiple. At target price, the implied PE multiple would be at 23.8x on 2014 earnings, a discount to consumer names in the Philippines which trades at a 29x average 2014 PE multiple. The PE/G would be 1.2x, but this moderates to 1x when based on a three-year Cagr.

Figure 16

| Value calculation (in US$ thousands) | |
|---|---|
| Total PV of cashflows | 404,093.2 |
| PV of terminal value using growing perpetuity | 686,046.7 |
| Enterprise value | 1,090,140.0 |
| Cash and cash equivalents | 63,124.0 |
| Short term investments | 0 |
| Total debt | 155,148.4 |
| Minority interest | 465 |
| Equity value | 997,650.5 |
| Outstanding shares | 1,295,869 |
| Implied share price | 0.76987 |
| Exchange rate ($/P) | 43.0 |
| Target price (P) | 33.0 |

Source: CLSA

**We derive a WACC of 8.1%**

We derive a WACC of 8.1%. Our 9.5% cost of equity assumes a risk-free rate of 3.5%, an equity-risk premium of 6% and a beta of 1.0. We use an after-tax cost of debt of 4.7%. We assume a long-term debt-to-equity ratio of 30:70.

**We use a WACC of 8.1%**

Figure 17

| WACC computation | |
|---|---|
| WACC (%) | 8.1 |
| Ke (%) | 9.5 |
| Equity/(debt + equity) (%) | 70.4 |
| Kd (%) | 4.7 |
| Debt/(debt + equity) (%) | 29.6 |
| Cost of equity (%) | 9.5 |
| Risk-free rate (%) | 3.5 |
| Beta | 1.00 |
| Equity-risk premium (%) | 6.0 |
| Cost of debt (after-tax) (%) | 4.7 |
| Cost of debt (%) | 6.0 |
| Statutory tax rate (%) | 22.0 |

## Improving returns, dividend while you wait

**DMPL has a strong balance sheet**

DMPL has a strong balance sheet, with net gearing maintained below at the 50% level from 2008-12. Operating cashflow for 2012 was lower at US$19.5m compared to US$38.1m in the prior year as a result of changes in working capital. This is usually impacted by the levels of receivables and inventory. The company ended with a net debt position of US$116m as of 31 December 2012, translating to a gearing 46%. Moving forward, we expect gearing levels to improve, hitting 27% in 2015. With US$14-17m in annual operating cashflow, a balance sheet which we estimate can absorb a further US$15-20m in leverage, DMPL's financial stability is reassuring. Capex for 2013 is expected to hit a peak of US$30.3m. Maintenance capex should be US$16m-17m, while US$6m will be allocated to the waste-to-energy project. Additional funds will be allocated for cannery expansion for its beverages.

**Net gearing maintained below at the 50% level from 2008-12**

Figure 18

**Debt vs gearing**

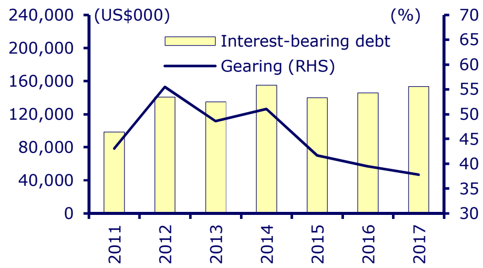
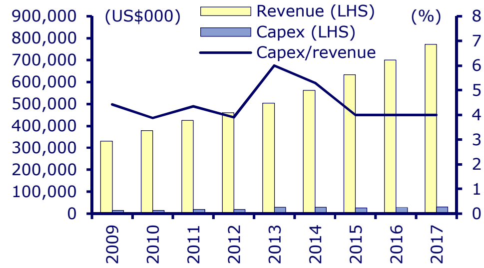



Figure 19

**Capex/revenue**




Source: CLSA Asia-Pacific Markets

**DMPL offers a 13% 13CL ROE**

DMPL offers a 13% 13CL ROE, averaging at 11% for the past three years, and returns are set to improve further as the company gets rid of its supply contracts in 2015. By then, ROEs should shoot up to 19% as a result of higher asset/equity ratio and huge margin expansion and higher asset turns. DMPL is a value creator with its 2012 13% ROE above its 9.3% cost of equity.

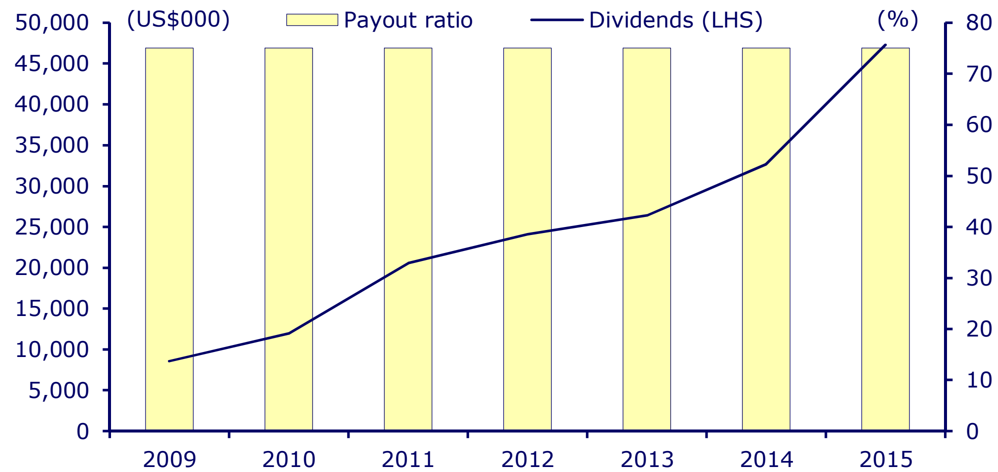
**DMPL has been paying out 75% of its profits for the past 8 years**

DMPL has a dividend policy of 33% of earnings but has been paying out 75% of its profits for the past eight years, and we are expecting the company to maintain this at 75% from 2013-15. This is above the average payout of other consumer names in the region, which we believe will supply shareholders with good returns while waiting for its operating margins to improve in 2015.

**DMPL has been consistently paying out 75%**

Figure 20

**Dividend payout**




Source: CLSA Asia-Pacific Markets

# Company outline

## The business

Del Monte Pacific Limited is one of the leading processed food and beverages manufacturer in the Philippines, owning the trademark rights to the Del Monte brand in the Philippines, India and Myanmar. The company also holds the rights to distribute the S&W brand globally (except in the Americas, Australia and New Zealand) and a 46% in Fieldfresh from India, serving as a platform for its expansion globally. DMPL also holds supply contracts and sells to private labels for supply of juices, process fruits, concentrates and fresh pineapples for the export markets. Its single largest shareholder Nutriasia Pacific Limited is committed to building DMPL into a global food marketer.

## Competition & market franchise

The Del Monte brand has been in the market for the past 8 decades, establishing itself as a well-known and trusted brand globally. The company boasts leading market shares in canned pineapple juice, mixed juice drinks, canned fruits and juices, condiments, and tomato and spaghetti sauces in the Philippines, and plans to establish itself as the leading brand in India and Myanmar. Likewise, S&W will be nurtured as DMPL's brand for fresh and processed fruit and vegetable products in Asia and the Middle East. The company continues to build its brand, with advertising and promotional expenses forming about 6% of sales in the Philippines in 2012. Del Monte's shelf space in the Philippines is also reflective of market share and expansion for key categories

Figure 21

## Peer comparison

| Company Name | Rec | Target | to target | Total stock return | EPS growth 2013 | EPS growth2014 | P/E 2013 | P/E 2014 | Dividend yield 2013 | Dividend Yield 2014 | ROE 2013 | ROE 2014 |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| ABS-CBN | BUY | 58.00 | 40.6 | 43.6 | 25.4 | (3.6) | 14.8 | 15.4 | 2.7 | 3.2 | 10.86 | 10.57 |
| Ace Hardware | OUTPERFORM | 1,000.00 | 38.9 | 39.4 | 6.2 | 24.0 | 26.6 | 21.4 | 0.4 | 0.6 | 25.78 | 25.56 |
| Astra Agro | UNDERPERFORM | 18,500.00 | 6.6 | 12.6 | 1.4 | 13.5 | 12.2 | 10.7 | 5.9 | 6.0 | 25.23 | 26.38 |
| Astra Intl | UNDERPERFORM | 6,500.00 | (3.0) | 0.6 | (1.9) | 21.6 | 14.2 | 11.7 | 3.2 | 3.8 | 24.92 | 26.31 |
| Astro | SELL | 2.75 | (8.9) | (5.6) | (33.6) | 11.5 | 37.9 | 34.0 | 1.3 | 3.0 | 84.06 | 91.62 |
| BAT Malaysia | SELL | 58.90 | (3.0) | 1.6 | 0.9 | 3.3 | 21.5 | 20.8 | 4.5 | 4.7 | 169.34 | 173.94 |
| BEC World | BUY | 75.00 | 11.5 | 16.4 | 24.9 | 16.5 | 22.5 | 19.4 | 4.4 | 5.2 | 68.75 | 71.18 |
| Big C Supercenter | SELL | 170.00 | (15.4) | (14.1) | 9.8 | 18.6 | 24.9 | 21.0 | 1.2 | 1.4 | 19.44 | 19.93 |
| Bloomberry | OUTPERFORM | 14.50 | 22.9 | 22.9 | nm | 103.2 | 29.1 | 14.3 | 0.0 | 0.0 | 23.01 | 34.66 |
| CP All | BUY | 50.00 | 30.7 | 35.5 | 32.7 | 26.5 | 23.5 | 18.6 | 4.0 | 5.4 | 49.00 | 52.47 |
| CP Foods | BUY | 40.00 | 39.1 | 43.7 | 0.5 | 13.2 | 11.8 | 10.4 | 4.2 | 4.8 | 17.20 | 17.67 |
| Dairy Farm | OUTPERFORM | 12.65 | 6.0 | 8.8 | 21.8 | 9.5 | 29.3 | 26.7 | 3.7 | 2.3 | 42.06 | 42.38 |
| Felda | SELL | 3.23 | (28.2) | (26.8) | (45.6) | 25.2 | 27.8 | 22.2 | 1.3 | 1.6 | 9.58 | 11.55 |
| First Resources | BUY | 2.38 | 38.8 | 41.6 | (8.5) | 14.2 | 9.6 | 8.4 | 2.6 | 3.0 | 18.86 | 18.62 |
| GMA | OUTPERFORM | 11.50 | 30.7 | 34.4 | 21.1 | 13.5 | 22.2 | 19.6 | 3.2 | 4.1 | 18.54 | 19.96 |
| Genting Bhd | UNDERPERFORM | 11.15 | 13.3 | 14.0 | (41.9) | 23.9 | 15.7 | 12.7 | 0.7 | 0.7 | 10.19 | 11.44 |
| Genting Malaysia | BUY | 4.85 | 22.8 | 24.6 | 22.1 | 6.4 | 13.1 | 12.3 | 1.8 | 1.9 | 12.40 | 12.01 |
| Genting Singapore | SELL | 1.54 | 12.3 | 13.0 | 26.2 | 27.8 | 26.3 | 20.6 | 0.6 | 0.7 | 9.17 | 10.69 |
| Golden Agri | BUY | 0.68 | 22.5 | 25.2 | 5.6 | 23.1 | 12.7 | 10.3 | 2.4 | 2.9 | 5.10 | 6.01 |
| Gudang Garam | UNDERPERFORM | 52,000.00 | 13.0 | 15.0 | 13.6 | 10.4 | 19.4 | 17.6 | 1.8 | 2.1 | 16.30 | 16.21 |
| Hero Supermarket | OUTPERFORM | 5,005.01 | 58.9 | 58.9 | 14.6 | 22.6 | 29.9 | 24.4 | 0.0 | 0.0 | 18.94 | 19.19 |
| HomePro | UNDERPERFORM | 12.30 | (1.6) | (1.2) | 18.7 | 21.4 | 32.3 | 26.6 | 0.3 | 0.4 | 26.71 | 24.55 |
| ICBP | OUTPERFORM | 12,500.00 | 9.6 | 11.5 | 18.6 | 10.6 | 25.7 | 23.2 | 1.6 | 1.9 | 21.25 | 20.88 |
| IOI | UNDERPERFORM | 5.60 | 2.8 | 5.3 | 4.0 | (12.1) | 18.8 | 21.4 | 2.5 | 2.6 | 14.22 | 11.75 |
| Indofood | OUTPERFORM | 7,500.00 | 5.6 | 8.3 | 1.3 | 12.3 | 18.9 | 16.8 | 2.6 | 2.6 | 14.98 | 15.52 |
| Jardine C&C | BUY | 51.00 | 21.9 | 26.1 | 6.7 | 14.4 | 11.2 | 9.8 | 3.9 | 4.5 | 21.33 | 21.64 |
| Jollibee | UNDERPERFORM | 143.00 | (5.7) | (4.7) | 10.6 | 10.4 | 37.7 | 34.1 | 0.9 | 1.0 | 20.61 | 23.30 |
| KL Kepong | SELL | 19.60 | (8.8) | (5.9) | (25.0) | 15.4 | 25.2 | 21.8 | 2.6 | 3.0 | 12.59 | 13.88 |
| Lonsum | UNDERPERFORM | 2,100.00 | 54.4 | 60.5 | 2.5 | 12.4 | 6.5 | 5.8 | 6.0 | 6.2 | 20.50 | 20.27 |
| MNC | OUTPERFORM | 3,620.00 | 13.1 | 15.5 | 16.0 | 23.1 | 21.7 | 17.7 | 2.1 | 2.5 | 26.75 | 28.29 |
| Major Cineplex | OUTPERFORM | 24.00 | 3.4 | 9.5 | 64.2 | (3.0) | 15.5 | 15.9 | 6.1 | 6.0 | 20.24 | 18.79 |
| Mayora Indah | OUTPERFORM | 32,000.00 | (4.5) | (3.8) | 21.8 | 11.5 | 28.9 | 25.9 | 0.6 | 0.7 | 26.42 | 23.92 |
| Megawide | UNDERPERFORM | 18.08 | 14.0 | 14.8 | 54.4 | 2.5 | 14.7 | 14.3 | 0.6 | 1.0 | 31.37 | 24.84 |
| Mitra Adiperkasa | OUTPERFORM | 9,500.00 | 37.7 | 38.3 | 16.7 | 23.7 | 22.7 | 18.3 | 0.6 | 0.7 | 20.89 | 21.23 |
| Olam | OUTPERFORM | 2.01 | 20.7 | 23.6 | 6.2 | 9.3 | 9.9 | 9.0 | 2.5 | 2.8 | 12.56 | 12.56 |
| Padini | OUTPERFORM | 2.10 | 14.8 | 19.8 | (10.4) | 21.9 | 14.2 | 11.6 | 4.4 | 4.9 | 24.07 | 26.82 |
| Parkson Retail Asia | BUY | 1.95 | 21.9 | 24.3 | 16.6 | 22.4 | 20.7 | 16.9 | 1.9 | 2.4 | 20.68 | 22.22 |
| Pepsi-Cola | BUY | 8.00 | 36.5 | 39.2 | 13.0 | 15.5 | 20.7 | 17.9 | 2.4 | 2.8 | 15.70 | 16.73 |
| Puregold | SELL | 34.00 | (14.9) | (14.9) | 21.3 | 21.1 | 28.9 | 23.9 | 0.0 | 0.0 | 13.01 | 13.77 |
| Robinson | BUY | 75.00 | 24.0 | 26.3 | 11.4 | 33.5 | 29.2 | 21.9 | 1.7 | 2.7 | 21.45 | 24.89 |
| SPH | SELL | 3.91 | (9.3) | (3.9) | (2.8) | (0.6) | 19.2 | 19.3 | 5.3 | 5.3 | 16.19 | 16.18 |
| Sampoerna Agro | SELL | 2,000.00 | 27.4 | 31.5 | 9.9 | 21.1 | 7.1 | 5.9 | 3.8 | 4.2 | 14.72 | 15.91 |
| Supra Boga Lestari | BUY | 1,300.00 | 52.9 | 53.9 | 40.1 | 33.6 | 26.0 | 19.5 | 0.8 | 1.0 | 13.46 | 15.99 |
| Surya Citra Media | OUTPERFORM | 2,800.00 | 0.0 | 4.7 | 33.7 | 29.3 | 22.3 | 17.2 | 4.0 | 5.2 | 54.48 | 66.30 |
| URC | OUTPERFORM | 135.00 | 7.9 | 9.4 | 4.9 | 15.6 | 33.1 | 28.6 | 1.4 | 1.5 | 19.29 | 21.19 |
| Unilever Indo | OUTPERFORM | 32,000.00 | (5.9) | (3.8) | 16.6 | 9.4 | 46.0 | 42.0 | 1.9 | 2.2 | 129.12 | 122.55 |
| Wilmar | UNDERPERFORM | 3.40 | 8.3 | 10.2 | (0.3) | 18.8 | 12.9 | 10.8 | 1.7 | 2.0 | 8.43 | 9.33 |

Source: CLSA

evalu@tor The Global Equities Database

# Summary financials

| Year to 31 December | 2011A | 2012A | 2013CL | 2014CL | 2015CL |
|---|---|---|---|---|---|
| **Summary P&L forecast (US$ '000)** | | | | | |
| **Revenue** | **425,235** | **459,711** | **504,735** | **560,802** | **632,616** |
| Op Ebitda | 57,242 | 64,410 | 72,728 | 84,700 | 107,783 |
| Op Ebit | 44,285 | 49,862 | 54,750 | 63,726 | 84,824 |
| Interest income | 1,460 | 824 | 304 | 324 | 782 |
| Interest expense | (3,057) | (3,883) | (3,730) | (4,288) | (3,862) |
| Other items | (10,589) | (6,090) | (6,234) | (5,786) | (3,852) |
| **Profit before tax** | **32,099** | **40,713** | **45,090** | **53,976** | **77,893** |
| Taxation | (5,508) | (9,088) | (10,065) | (12,049) | (17,387) |
| Minorities/Pref divs | (850) | (465) | (465) | (465) | (465) |
| **Net profit** | **25,741** | **31,160** | **34,560** | **41,462** | **60,040** |
| **Summary cashflow forecast (US$ '000)** | | | | | |
| **Operating profit** | **44,285** | **49,862** | **54,750** | **63,726** | **84,824** |
| Operating adjustments | (2,294) | 14,649 | 14,649 | 14,649 | 14,649 |
| Depreciation/amortisation | 12,957 | 14,548 | 17,978 | 20,974 | 22,958 |
| Working capital changes | 4,832 | (23,806) | (15,387) | 15,799 | (37,364) |
| Net interest/taxes/other | (17,694) | (18,237) | (19,725) | (21,799) | (24,319) |
| **Net operating cashflow** | **42,086** | **37,016** | **52,265** | **93,350** | **60,749** |
| Capital expenditure | (18,478) | (17,900) | (30,284) | (29,722) | (25,305) |
| **Free cashflow** | **23,608** | **19,116** | **21,981** | **63,627** | **35,444** |
| Acq/inv/disposals | 12,396 | (1,117) | 666 | 2,147 | (124) |
| Int, invt & associate div | - | - | - | - | - |
| **Net investing cashflow** | **(6,083)** | **(19,017)** | **(29,618)** | **(27,576)** | **(25,429)** |
| Increase in loans | (12,100) | 9,763 | 5,194 | 2,668 | (2,070) |
| Dividends | (20,533) | (24,084) | (26,269) | (31,446) | (45,379) |
| Net equity raised/other | 0 | 0 | - | - | - |
| **Net financing cashflow** | **(32,633)** | **(14,321)** | **(21,075)** | **(28,777)** | **(47,449)** |
| **Incr/(decr) in net cash** | **3,371** | **3,678** | **1,572** | **36,997** | **(12,130)** |
| Exch rate movements | - | - | - | - | - |
| **Opening cash** | **17,506** | **20,877** | **24,555** | **26,127** | **63,124** |
| **Closing cash** | **20,877** | **24,555** | **26,127** | **63,124** | **50,994** |
| **Summary balance sheet forecast (US$ '000)** | | | | | |
| Cash & equivalents | 20,877 | 24,555 | 26,127 | 63,124 | 50,994 |
| Debtors | 82,926 | 102,388 | 100,947 | 85,987 | 94,761 |
| Inventories | 89,381 | 113,458 | 111,215 | 122,717 | 134,200 |
| Other current assets | 91,791 | 109,665 | 117,968 | 126,271 | 134,574 |
| Fixed assets | 85,412 | 93,350 | 101,070 | 109,818 | 112,164 |
| Intangible assets | 16,004 | 15,433 | 16,004 | 15,814 | 15,750 |
| Other term assets | 37,500 | 36,671 | 40,020 | 38,064 | 38,252 |
| **Total assets** | **423,891** | **495,520** | **513,351** | **561,794** | **580,695** |
| Short-term debt | 186,338 | 221,366 | 212,037 | 232,581 | 223,364 |
| Creditors | - | - | - | - | - |
| Other current liabs | 2,595 | 5,174 | 3,735 | 3,835 | 4,248 |
| Long-term debt/CBs | 5,916 | 15,679 | 20,873 | 23,541 | 21,471 |
| Provisions/other LT liabs | 0 | 0 | - | - | - |
| Minorities/other equity | (1,474) | (1,939) | (1,939) | (1,939) | (1,939) |
| Shareholder funds | 230,516 | 255,240 | 278,645 | 303,776 | 333,551 |
| **Total liabs & equity** | **423,891** | **495,520** | **513,351** | **561,794** | **580,695** |
| **Ratio analysis** | | | | | |
| Revenue growth (% YoY) | 12.3 | 8.1 | 9.8 | 11.1 | 12.8 |
| Ebitda growth (% YoY) | 88.0 | 12.5 | 12.9 | 16.5 | 27.3 |
| Ebitda margin (%) | 13.5 | 14.0 | 14.4 | 15.1 | 17.0 |
| Net profit margin (%) | 6.1 | 6.8 | 6.8 | 7.4 | 9.5 |
| Dividend payout (%) | 1.0 | 0.9 | 0.8 | 0.8 | 0.8 |
| Effective tax rate (%) | 17.2 | 22.3 | 22.3 | 22.3 | 22.3 |
| Ebitda/net int exp (x) | 35.8 | 21.1 | 21.2 | 21.4 | 35.0 |
| Net debt/equity (%) | 74.8 | 83.9 | 74.7 | 63.9 | 58.5 |
| ROE (%) | 11.4 | 12.8 | 12.9 | 14.2 | 18.8 |
| ROIC (%) | 10.2 | 9.4 | 9.4 | 10.7 | 13.6 |
| EVA®/IC (%) | 2.2 | 1.6 | 1.5 | 2.8 | 5.7 |

Source: CLSA

## Companies mentioned

Del Monte Pacific (DMPL PM - P27.05 - BUY)

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