Record profits as Farsons celebrates its 90th anniversary

Simonds Farsons Cisk plc published its January 2018 annual financial statements on 16 May and last Friday 1 June, it published its 2018 Annual Report ahead of the company's Annual General Meeting on 21 June.

Farsons organizes an annual meeting for financial analysts on the day of the publication of their Annual Report when detailed presentations are given on the financial performance as well as market trends and developments across the group's various areas of operation within the food and beverage sector.

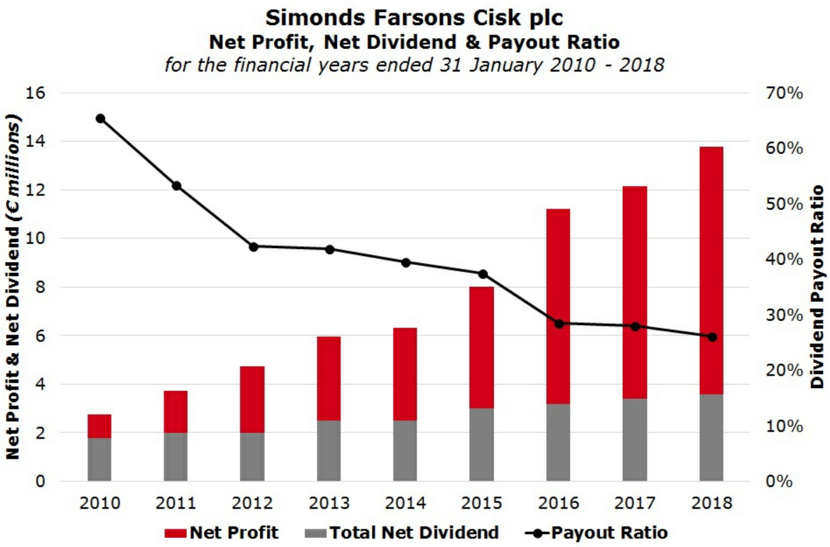
During the financial year to 31 January 2018, the Farsons Group registered a 7.8% increase in turnover to a record of just under €95 million. Chairman Mr Louis Farrugia started off the meeting by expressing his satisfaction on the excellent financial performance. Mr Farrugia commented that all of the group's business segments experienced growth during the period under review reflecting the continued positive performance of the local economy, the sustained growth of the tourism industry, the increase in the number of expatriates living in Malta, the favourable weather conditions experienced during most of 2017, as well as the various crowd events hosted during the year.

On his part, CEO Mr Norman Aquilina highlighted that over 50% of overall turnover is generated from the core business of the group which is the brewing and bottling of beers and beverages. In fact, the segmental analysis in the notes to the financial statements reveal that the core business generated €50.5 million in revenue. Mr Aquilina once again indicated that CISK remains a major contributor to both revenue and profitability since it maintains a very high market share despite the very stiff competition in the beer market. Meanwhile, Kinnie also remains an important brand for Farsons notwithstanding the increased awareness among consumers on the link between obesity and soft drink consumption. In fact, Farsons pledged to reduce added sugar content in its soft drinks portfolio by 10% by 2020.

The main subsidiaries involved in the importation of food and beverages (Quintano Foods Ltd and Farsons Beverage Imports Co Ltd) as well as the operation of franchised food retailing through Food Chain Ltd, generated total revenue of €44.5 million.

The segmental analysis in the annual report also provides the contribution to operating profit. The core business (the brewing and bottling of beers and beverages) generated an operating profit of €10.3 million, accounting for 70% of overall group operating profit of €14.7 million. Meanwhile, the remaining 30% of operating profit comes from the group's subsidiaries. It is also interesting to analyse the operating profit margin with the 'brewing and bottling of beers and beverages' generating a margin of 20.4% (unchanged over last year), the 'importation of food and beverages' generating a margin of 9.3% and 'the operation of franchised food retailing' giving an operating profit margin of 10.8%. As indicated by both the Chairman and the CEO in their presentation last week and also in the Annual Report, all business segments generated improved revenue and profitability. Mr Aquilina also commented last week that he believes that the subsidiaries have lots of room for further growth via an increased market share and additional brand representation. The CEO also referred to the recent openings of Food Chain Ltd, namely at PAVI in Qormi and PAMA in Mosta. These restaurants all performed strongly and rank as the better performers across the restaurant portfolio.

As a result of the bond issue in July 2017, last year was the first time that Farsons issued financial projections and it is important to compare the actual results achieved with the projections although there was no mention of this in last week's presentation. Shareholders should be pleased to note that total group revenue is 4% higher than expected and more importantly, profit after tax is 38.4% higher than previously anticipated. When questioned on the reasons for this superior performance compared to expectations, Mr Aquilina explained that while the philosophy of Farsons was to be prudent in their financial projections, it is also evident that the group's bottom line is improving at a faster pace compared to the growth in revenue and additionally there were certain events that were not anticipated at the time of the preparation of the financial projections at the start of the 2017/18 financial year. In fact, in the Annual Report, the CEO made reference to mass public events related to the General Election which "boosted beverage consumption, particularly beers, to above average levels".



In last week's presentation as well as in his detailed review in the Annual Report, the CEO also makes reference to the 5-year trend in turnover, earnings before, interest, tax, depreciation and amortization (EBITDA) as well as profitability. The growth achieved in the last few years is somewhat extraordinary. Over the last five years, Farsons' group turnover increased by 21% (from €78.3 million in 2014 to €95 million in 2018), EBITDA climbed by 56% to €22 million and profits after tax more than doubled from €6.3 million in 2014 to €13.8 million in 2018.

Mr Aquilina claimed that this strong track record is a clear indication of the benefits derived from the significant investment programme over recent years which translated into improved profitability levels. The investments by Farsons of over €100 million during the last 10 years is driving higher productivity and cost efficiencies.

The CEO explained that the heavy investment programme was required for the group to aspire to achieve additional growth also in future years. Mr Aquilina highlighted that exports and innovation remain two key strategic pillars for the future. Although it is very positive to note the increased success in exports with the CEO claiming in a recent interview in the media that the group exported to 20 countries during the last financial year, the revenue contribution remains low. At last week's presentation, Mr Aquilina noted that although revenue from exports amounted to under €5 million, the potential for growth can be significant if market depth is achieved in certain countries or regions. The CEO announced that Farsons is aiming to double export volumes over the next few years.

Although Mr Aquilina also noted the need to continue investing to maintain sustainable profitable growth, there was no indication on the size of the investments being envisaged. Meanwhile, Chairman Mr Farrugia noted in the Annual Report that one expects "a reduction in the very high levels of capital expenditure experienced in recent years". Given the expectation of a reduction in investments compared to recent years and the low level of group borrowings, shareholders ought to expect a higher dividend payout ratio.

In fact, **although the 2017/18 cash dividend increased by 5.9% to €3.6 million, the dividend payout ratio of 26% is the lowest level in the past 5 years**.

Meanwhile, as explained in one of my recent articles, shareholders should also be pleased that for the second successive year, Farsons generated a return on equity in excess of 10%. The ROE increased to 12.5% from 10.4% in the previous financial year. In the next few weeks, Farsons will be publishing its updated Financial Analysis Summary showing the financial projections for the current financial year to 31 January 2019. Shareholders should look out for some of the key figures within this detailed report in the context of the continued strong economic performance and the expectation of another record year for tourism which should translate into another very strong financial performance for the Farsons group.