

YOWIE GROUP LIMITED (YOW)

September Quarterly

Yowie Group Limited (YOW) has released its September Quarterly. During the period YOW delivered a material increase in sales revenue. This was largely driven by the national roll out of the Yowie confectionary to the Walmart store network. At the end of the quarter Yowie was being sold in approximately 3700 Walmart stores with a completed roll out to approximately 4700 stores expected by the end of October.

Overall retail sales of Yowie for the September quarter reached US\$4.8m, more than double the previous quarter. The largest driver of the improvement was the Walmart rollout (only begin in September) with Yowie also being sold in a further 44 active accounts.

Marketing activity continues to ramp up. YOW has engaged a US based creative agency and hope to have material ready by 2Q CY16. YOW management continue to drive the product through various social media channels – YouTube, Facebook, Instagram and Twitter.

Based on the current run rate, Yowie volumes will miss our FY16 estimate of 9m. We estimate that approximately 1.3m units were sold in the September quarter based on an average unit sales price of US\$1.40. We would expect volumes to grow significantly in the current quarter – closer to 2m units because the Walmart roll-out will be complete.

Cash at the end of the quarter was US\$8.3m or A\$11.36m. YOW has changed its reporting currency to US\$.

Beyond Wal-Mart

One of the key drivers of share price performance over the next 6 months will be YOW management delivering on new accounts. Beyond Walmart, Yowie is also being sold by 44 other retail chains with a total addressable store count of over 30,000. The Walmart rollout provides validation of the Yowie product. We believe this, together with the recent hire of additional sales people, greatly increases the likelihood that sales will increase from existing accounts and new accounts.

It is worth remembering that the Asia Pacific confectionary market is larger than the North American market. In April YOW announced that a small trial had been competed with a “Tier 1” supermarket chain in Dubai. The 12-store trial achieved benchmark targets across all stores at pricing similar to that of the US market.

Valuation

We have reduced our FY16 volume forecast to 8m (from 9.1m). We have not changed our FY17 US volume forecast of 26.1m. Based on these volume assumptions, we believe YOW will make an A\$1.8m EBIT loss in FY16, but generate A\$6.1m EBIT in FY17 from the US business. The global confectionary sector trades on an average FY17 PE multiple of 19x. Our base case valuation for the US business is A\$1.21 ps. We value the opportunity for YOW to expand into the rest of the world at \$50m or 28cps.

Share Price:	\$1.17
US Valuation:	\$1.21
12mth price target:	\$1.49

Brief Business Description:

Yowie Group (YOW) has global distribution rights to the Yowie confectionary brand

Hartleys Brief Investment Conclusion

Yowie Group (YOW) may be on the cusp of a successful launch of its Yowie confectionary brand into the US market. This would move YOW from what is essentially a concept to a genuine early stage growth story.

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Patricia Fields Executive Director

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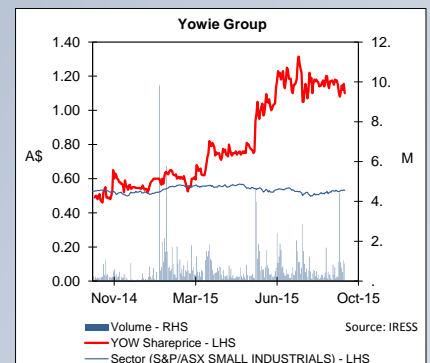
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Issued Capital:	148.5m
- fully diluted	181.0m
Market Cap:	\$173.0m
- fully diluted	\$210.9m
Net Debt (FY 15)	-\$11.1m

	FY15a	FY16e	FY17e
Op Cash Flw	-7.8	-2.7	2.1
Free Cash Flw	-8.2	-4.7	-0.9
NPAT* (A\$m)	-3.5	-1.8	6.1
EPS (\$, bas)	-2.7	-1.2	3.7
P/E (basic)	-42.9x	-98.6x	31.2x
P/E (diluted)	-31.9x	-118.7x	34.5x
EV / EBITDA	-25.3x	-69.7x	18.2x
DPS (cps)	-	-	-



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Hartleys has assisted in the completion of part of a capital raising in the past 12 months for Yowie Group Limited, for which it has earned fees.

Fig. 1: Quarterly Operating Performance

		FY15				FY	FY16
		1Q	2Q	3Q	4Q		1Q
USD/ AUD		0.80	0.80	0.78	0.75		0.73
Wholesale Price est.	US\$	1.40	1.40	1.40	1.40		1.40
Units Sold		18,857	126,286	402,814	720,536	1,268,493	1,293,571
Sales	% Chg.		570%	219%	79%		
	A\$ m	0.03	0.22	0.72	1.35	2.32	1.81
	% Chg.		570%	227%	86%		
Staff Costs		-0.07	-0.10	-0.12	-0.18	-0.47	-0.24
Ad & Marketing		-0.02	-0.02	-0.01	-0.17	-0.22	-0.10
R & D						0.00	0.00
Working Capital		-1.84	-3.28	-1.78	-2.76	-9.66	-2.22
Other		0.07	-5.61	-2.22	-0.72	-8.48	0.06
Operating Cash Flow		-1.83	-3.09	-1.14	-1.63	-7.69	-0.69
Investing Cash Flow		-0.17	-0.11	-0.05	-0.08	-0.41	-0.17
Share Issuance		0.02		10.25	0.88	11.14	1.20
Debt Issuance						0.00	
Other		0.00	0.00	-0.64	-0.04	-0.68	0.00
Financing Cash Flow		0.02	0.00	9.61	0.84	10.46	1.20
Cash Beginning		8.25	6.40	3.33	11.90		8.47
Net Cash Flow		-1.98	-3.20	8.42	-0.88		0.35
FX		0.13	0.13	0.15	0.04		-0.51
Cash End		6.397	3.327	11.896	11.058		8.82

Source: Yowie Group Ltd, Note – FY16 stated in US\$

VALUATION

We have raised our 12-month target price on YOW to \$1.49 ps, from \$1.20 ps. We value the US market opportunity at \$1.21 ps or close to 35x FY17 EPS. The fact that YOW has been able to secure a full national roll out with Wal-Mart should provide the market with further validation of the Yowie potential.

It is worth remembering that the Asia Pacific confectionary market is larger than the North American market. In addition, YOW has already completed a successful trial with a “Tier 1” grocery account in Dubai. We expect this to be a starting point for a wider launch of Yowie into the Middle East. A successful launch of YOW across Wal-Mart’s US store network may lead to a roll out across the global network. We think the opportunity for YOW beyond the US is significant enough for us to assign a value of A\$50m or 28cps.

Fig. 2: Valuation Base Case – US Business + RPW opportunity

US Base Case	FY17 Multiple	Target Multiple	Wgt.%	Tgt Price
EV/EBIT	18.8x	25x	20%	1.26
Earnings	34.3x	35x	20%	1.19
DCF			60%	1.21
ROW Opportunity			\$50m	0.28
12-month Target Price				\$1.49
Upside / downside from current share price				28%
P / E (6/17F) at price target				43.9x
P / E (6/18F) at price target				30.5x
EV / EBITDA (6/17F) at price target				28.4x
EV / EBIT (6/17F) at price target				29.5x
Dividend Yield (6/16F) at price target				0.0%

Source: Hartleys Research

RISKS

We highlight the following as the major risks to our investment thesis:

YOW's exclusive access to the Whetstone patent expires in 2018. Beyond this date other players may compete for access to the relevant patent. That said, having a first-mover advantage in the US market will make it difficult for competition trying to compete with YOW beyond the expire of the patent.

YOW does have exposure to commodity price increases. Rising chocolate, plastic and aluminium prices would have a negative impact, albeit minor, on EBIT margins.

Currently YOW has a relatively small management team. Whilst this is positive for the cost structure in the short term, it may impact the ability of YOW management to grow the company.

S.W.O.T ANALYSIS

Strengths	<p>A proven product in a developed confectionary market (Australia).</p> <p>Unique product offering within a US market context (ban on Kinder eggs).</p> <p>Exclusive use of patent that circumvents the issues that prevent Kinder eggs being sold in the US.</p>
Weakness	<p>Exclusive use of patent ends in 2018.</p> <p>Lack of proven distribution within the US market.</p>
Opportunities	<p>Opportunities to expand into other markets especially Asia and the Middle East.</p> <p>Re-introduction into the Australian market where Yowie had been previously successful.</p>
Threats	<p>The "Wal-Mart" effect – with Wal-Mart expected to become YOW's major customer during the early phase of the US market launch, YOW management will need to be focused on the requirements of a large, single customer with a history of pressuring margins of small suppliers.</p>

Fig. 3: Global Confectionery Sector Valuation

Bloomberg Consensus Estimates																
NAME	TICKER	Last Price	M. CAP (A\$m)	Net Debt	EV (A\$m)	"FY0" Year	EBIT / Sales FY2	NPAT growth			EV/EBITDA			EV/EBIT		
								FY0	FY1	FY2	FY0	FY1	FY2	FY0	FY1	FY2
Packaged Food and Confectionery																
US																
HERSHEY CO/THE	HSY US	95.93	21,205	1,489	22,694	12/2014	20.0%	1.1%	7.1%	5.0%	13.6	13.4	12.6	15.5	15.4	14.6
PEPSICO INC	PEP US	103.08	153,383	23,952	177,335	12/2014	16.2%	-5.7%	5.9%	6.2%	13.8	14.3	13.7	17.3	17.8	17.1
TYSON FOODS INC-CL A	TSN US	47.18	17,740	822	18,562	09/2014	6.1%	28.5%	8.4%	7.4%	8.4	6.2	5.8	11.2	8.1	7.5
MONDELEZ INTERNATIONAL INC-A	MDLZ US	46.94	78,091	14,970	93,061	12/2014	15.3%	-0.5%	11.3%	11.0%	16.8	18.7	17.1	21.1	23.0	21.0
GENERAL MILLS INC	GIS US	59.23	35,461	9,646	45,107	05/2015	16.8%	2.7%	4.9%	4.7%	13.3	13.1	12.7	16.4	16.1	15.6
KELLOGG CO	K US	72.01	25,636	7,030	32,666	12/2014	14.6%	-10.7%	5.9%	5.4%	12.1	13.3	12.8	15.1	16.8	16.1
DEAN FOODS CO	DF US	18.11	1,704	19	1,723	12/2014	2.6%	-1016.8%	0.0%	3.5%	8.5	4.5	4.5	40.2	7.7	8.0
median			25,636				15.3%	-0.5%	5.9%	5.4%	13.3	13.3	12.7	16.4	16.1	15.6
average			47,603				13.1%	-143.0%	6.2%	6.2%	12.4	11.9	11.3	19.6	15.0	14.3
GLOBAL																
NESTLE SA-REG	NESN VX	74.80	236,996		249,149	12/2014	16.0%	-2.4%	5.4%	6.1%	14.3	14.5	13.8	17.9	17.7	16.7
GRUPO BIMBO SAB- SERIES A	BIMBOA MM	47.55	223,637		279,349	12/2014	7.8%	12.3%	30.6%	13.0%	14.3	12.4	11.2	21.5	18.6	15.8
WOOLWORTHS LTD	WOW AU	27.48	34,807		38,424	06/2015	5.4%	-6.4%	-2.2%	0.9%	8.0	8.3	8.4	10.2	11.1	11.2
ORION CORP	001800 KS	994000.00	5,019,834		5,598,574	12/2014	14.1%	19.8%	17.3%	15.6%	13.5	12.1	11.2	20.0	17.5	15.3
LOTTE CONFECTIONERY CO LTD	004990 KS	2066000.00	2,907,688		3,114,243	12/2014	5.9%	12.6%	10.5%	8.2%	15.1	13.7	12.8	26.1	24.5	22.3
median			236,996				7.8%	12.3%	10.5%	8.2%	14.3	12.4	11.2	20.0	17.7	15.8
average			1684592.5				9.8%	7.2%	12.3%	8.8%	13.0	12.2	11.5	19.1	17.9	16.3

Bloomberg Consensus Estimates																
NAME	TICKER	P/E (dil. for new shs) (curr mkt cap / NPAT)														
		Dividend Yield			Dividend Yield			Dividend Yield			Dividend Yield			Dividend Yield		
		FY0	FY1	FY2	FY0	FY1	FY2	FY0	FY1	FY2	FY0	FY1	FY2	FY0	FY1	FY2
Packaged Food and Confectionery																
US																
HERSHEY CO/THE	HSY US				23.5	23.3	21.7	2.1%	2.3%	2.5%						
PEPSICO INC	PEP US				21.9	23.2	21.9	2.5%	2.7%	2.9%						
TYSON FOODS INC-CL A	TSN US				17.2	13.4	12.4	0.6%	0.8%	0.9%						
MONDELEZ INTERNATIONAL INC-A	MDLZ US				26.7	26.8	24.1	1.2%	1.3%	1.5%						
GENERAL MILLS INC	GIS US				20.3	19.8	18.9	2.8%	3.0%	3.3%						
KELLOGG CO	K US				18.5	20.7	19.5	2.6%	2.7%	2.8%						
DEAN FOODS CO	DF US					17.2	17.2	1.5%	1.7%	1.8%						
median					21.1	20.7	19.5	2.1%	2.3%	2.5%						
average					21.4	20.6	19.4	1.9%	2.1%	2.2%						
GLOBAL																
NESTLE SA-REG	NESN VX				22.2	22.7	21.6	3.0%	3.0%	3.1%						
GRUPO BIMBO SAB- SERIES A	BIMBOA MM				37.5	33.4	25.6	0.5%	0.3%	0.7%						
WOOLWORTHS LTD	WOW AU				14.2	15.2	15.6	5.0%	4.9%	4.9%						
ORION CORP	001800 KS				29.3	24.5	20.9	0.4%	0.6%	0.7%						
LOTTE CONFECTIONERY CO LTD	004990 KS				35.5	31.5	28.5	0.2%	0.2%	0.3%						
median					29.3	24.5	21.6	0.5%	0.6%	0.7%						
average					27.7	25.5	22.4	1.8%	1.8%	1.9%						

Source: Bloomberg

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Buy	Share price appreciation anticipated.
Accumulate	Share price appreciation anticipated but the risk/reward is not as attractive as a "Buy". Alternatively, for the share price to rise it may be contingent on the outcome of an uncertain or distant event. Analyst will often indicate a price level at which it may become a "Buy".
Neutral	Take no action. Upside & downside risk/reward is evenly balanced.
Reduce / Take profits	It is anticipated to be unlikely that there will be gains over the investment time horizon but there is a possibility of some price weakness over that period.
Sell	Significant price depreciation anticipated.
No Rating	No recommendation.
Speculative Buy	Share price could be volatile. While it is anticipated that, on a risk/reward basis, an investment is attractive, there is at least one identifiable risk that has a meaningful possibility of occurring, which, if it did occur, could lead to significant share price reduction. Consequently, the investment is considered high risk.

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