



27th March 2020

Small Cap

Bubs Australia Limited: Leading Producer of Dairy Products

Reading Time: 5 Mins

By Team Ace Investors

Stock Code	ASX: BUB
Shares O/S	560.3 million
Closing Price	AUD 0.545
Market Cap	308.16 million
52 High/Low	0.400/1.615
One Year Stock Performance	
Avg volume (TTM)	5.16 million
EPS (TTM)	-0.023
P/E	-
Annual Dividend Yield	-
Franking	-
Last Dividend Ex-Date	-
Last Dividend Pay Date	-
DPS (AUD)	-
ROE %	-39.86%

COMPANY OVERVIEW

Bubs Australia Limited (**"Bubs" or the "Company"**) is the leading producer of goat dairy products in Australia with exclusive milk supply from the largest milking goat herds in the country. The Company's products are sold in major supermarkets and pharmacies throughout Australia, as well as exported to China, South East Asia and the Middle East.

Strong H1 FY 2020 Performance

The Company has delivered a strong set of results for the first half of the 2020 financial year driven by the strong performance of Bubs infant formula in all retail channels and regions. The Company reported revenue of \$28.8 million, up 37%. Infant formula gross revenue increased 77% and revenue from Baby Food increased 23%.

During H1 FY 2020, the Company's domestic revenue increased by 30% driven by strong penetration in Coles and Woolworths and the launch into Chemist Warehouse.

Following the successful \$35 million institutional capital raising and retail share placement in December 2019, Bubs Australia operates with robust balance sheet with \$39.1 million in cash reserves after recording operating cash outflows of \$12.5 million during the second quarter.

One Year Stock Price Performance



Source: ASX

KEY FINANCIAL FIGURES

	2015	2016	2017	2018	2019
Revenue (In AUD million)	0.11	0.02	3.95	16.91	43.91
Growth %	-	-78.83%	16979.22%	328.52%	159.75%
EBITDA (In AUD million)	-1.53	-0.51	-3.24	-16.61	-34.31
Margin (%)	-	-	-	-	-
PAT (In AUD million)	-1.53	-0.51	-5.06	-64.66	-35.51
PAT Margin (%)	-	-	-	-	-
EPS (In AUD)	-0.18	-0.04	-0.02	-0.20	-0.08
BALANCE SHEET FIGURES					
Shareholders Fund (In AUD million)	0.46	0.05	7.52	72.52	105.65
Debt (In AUD million)	0.00	0.00	0.00	2.00	2.00
Cash (In AUD million)	1.19	0.12	5.31	38.64	23.29
D/E Ratio	0.00	0.00	0.00	0.03	0.02

INVESTMENT RATIONALE/CONCERNS

- **Entered into New Deal with Woolworths** – On 18th Feb 2020, the Company announced that it has entered into a new supply agreement with Woolworths Group Ltd. Bubs first entered into a supply agreement with Woolworths in February 2018. This new updated agreement will allow Bubs to offer its entire range of eight infant formula products across a targeted selection of Woolworths' 700 national store network. We believe that this will have a significant uplift in its domestic volume and will materially add to its domestic revenues.
- **Update on the Impact of Coronavirus Outbreak** – The Company sources goat milk and packaging materials from Australia/New Zealand and thus its supply chain has not been impacted. On 18th March 2020, the management mentioned that the Company has increased its capacity and is continuously working to expand its inventory and meet the supply needs of its retail partners across both goat milk and organic grass-fed cow's milk-based formula. The Company has moved to two shifts per day and has the capacity to move to three shifts if required.
- **Domestic Sales accounted for about 74% of Bubs revenues.** Over the last few weeks, the Company is working with its retail partners including Coles, Woolworths, Big W and Chemist Warehouse to ensure distribution and continued supply of the newly introduced Bubs Organic 365 days Grass Fed Infant Formula range as well as its existing Bubs Australian Goat Milk infant formula range. With limited international exposure, we believe that the Company will be able to maintain its growth momentum.
- **Focus on High Margin Products** – The Company is deliberately reducing its fresh dairy lines of products due to poor profitability. The revenue contribution from dairy line has come down from 17% in H1 FY 2019 to 6% in H1 FY 2020. The Company aims to increased its focus on investing in growth of high margin products, primarily infant formula. This has been reflecting in the strengthening of gross margin to 24% from 19% in H1 FY 2019.
- **Significant increase in Expenses** – During H1 FY2020, the Company's expenses rose significantly. Employee costs grew 33% to \$2.85 million, distribution and selling cost increased 16% to \$0.79 million and marketing costs increased 269% to \$4.81 million to support a strong domestic presence and build brand awareness in China. The Company reported EBITDA loss of \$5.25 million as compared to the loss of \$8.52 million in H1 FY2019.

STOCK RECOMMENDATION

The Company holds a market leadership position and its brand holds a unique position of being the world's only producer of goat infant formula made from Australian goat milk. The Company continue to explore opportunities to develop its supply chain and improve manufacturing capabilities. For H2 FY2020, the Company expects stronger demand for infant formula across all channels. New markets and new products launches are expected to drive revenue streams. The Company is working to expand its product offerings with the launch of a new goat milk range aimed at adults.

*The Company's new Woolworths agreement will increase its product visibility for consumers across Australia. This also add credibility to the Company's product offering. The Company is working closely with retail partners such as Coles Group and Woolworths Group Ltd to meet the increasing demand for its product. We believe that the Company's effort to increase its presence in domestic market happened at the right time. By growing its sales at home in Australia, Bubs may be able to offset some of the revenue loss from China (~19% in H1 FY2020). At current levels, we would like to recommend **BUY** rating on the stock.*

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