



Fisher Funds

Investor Education Centre

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F & P's profitability doesn't come out in the wash

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The Fisher & Paykel Appliances brand is iconic, well at least it's very well known in New Zealand. As an investment proposition, Fisher & Paykel has always had enormous potential. But it can be a hard road turning potential into profit.

F&P has built and maintained a large market share in New Zealand's appliance sector, and has been successful in building a market position in Australia, the US and more recently in Asia. The company has always prided itself on its R&D spend which has enabled it to develop new technologies to give it a competitive edge, at least until competitors caught up. With high quality products, a strong brand, and favourable market drivers - new home sales and renovations - the sky should be the limit for the company. But it has never quite lived up to expectations.

The company made after-tax profits of \$109 million back in 2006 and five years on, the company is making around a third of that - \$33 million in the year to March 2011. The F&P Appliances share price traded at over \$2.60 in 2006 compared to the current share price of around 64 cents. The company's earnings have been in steady decline for six years despite having a recapitalisation in 2009, employing a new CEO and Chairman, forming a partnership with Chinese appliance giant Haier, and working hard to compete against cheaper brands. It's obviously hard work.

We could forgive the company's underwhelming performance on the basis that the past five years have featured a GFC and the appliance market is extremely competitive. F&P wouldn't be alone in finding the last five years difficult.

Indeed a good comparison can be made with Nokia, a mobile telephone company based in Finland, a country with a population not too much bigger than New Zealand's. Nokia is similar to F&P Appliances in terms of its commitment to R&D, its technological edge, its strong brand and the fact that it operates in a constantly evolving, competitive sector.

Nokia has become the world's largest mobile phone maker however its profits have halved over the past five years and its share price has fared even worse. Nokia has been good at what it does - mobile telephone handsets - but it has been left behind as other more nimble competitors have stolen a march and stolen market share. The company's strong brand has not been enough to protect profitability.

The comparison of the two companies is not intended as a criticism of F&P Appliances or Nokia, but rather an illustration of the notion that strong brands don't necessarily guarantee strong profits or strong share prices. It also illustrates the importance of recognising the difference between a cyclical downturn and a business in terminal decline.

Over the past five years, analysts have been quick to recommend investors BUY F&P Appliances and Nokia on any share price decline, on the basis that things must eventually get better. But it is not always clear that things do get better.

In some cases the best way to support our preferred brands is to buy their products rather than their shares.

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