

Company Analysis: Caribbean Producers Jamaica Ltd. (CPJ) 9M 2022/23

VMWM Research | June 15, 2023



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- Stock Recommendation: **OVERWEIGHT**
- Current Price: J\$9.72
- Price Target J\$12.30

- Shares Outstanding: 1,100,000,000 units
- Financial Year End: June 30

ABOUT THE COMPANY

Caribbean Producers (Jamaica) Limited (CPJ) is incorporated under the laws of and domiciled in Jamaica, with its registered office situated at Shop No. 14, Montego Freeport Shopping Centre, Montego Bay, Jamaica.

The company was founded by Mark Hart and Thomas Tyler in April 1994 and is a food service distributor that sells its consumable goods to the hospitality industry. These goods include both food and non-food brands along with wines and spirits that are well known internationally.

CPJ operates from the Montego Freeport St. James that consists of 120,000 sq. ft. of space that houses offices, manufacturing plants, refrigerated and dry warehousing. The wine brands carried by the firm are internationally known and include Bacardi, Grey Goose, Dewars, Louis Latour, Concha y Toro, Remy Cointreau and Taittinger.

FINANCIAL PERFORMANCE SUMMARY

US\$'000	FY 2020/21	FY 2021/22	9M 2021/22	9M 2022/23
Operating Revenue	58,178	119,960	86,440	107,037
Gross Profit	15,714	34,844	27,614	31,784
Operating Profit	(335)	12,411	10,208	7,525
Net Profit	(2,519)	7,722	7,018	3,822
Total Assets	66,330	88,455	78,571	86,166
Total Liabilities	51,081	62,415	56,303	56,304
Equity to Parent	15,642	26,039	22,268	29,862

Dividend Policy

The company does not have an approved dividend policy and has not paid any dividends over the last three financial years.

Outlook

CPJ aims to maintain high levels of service and quality products. The current environment, characterized by supply chain challenges and potential disruptions from the war in Europe, is expected to continue causing logistical difficulties. However, CPJ's management is focused on strengthening core business capabilities and forging strategic partnerships with key customers. The company is evaluating capital investment projects to enhance efficiency and considering expansions in manufacturing and operational areas to increase capacity and efficiency. CPJ is also investing in energy-saving projects and information technology systems to reduce costs and improve customer service. We expect continued growth in tourism to drive continued growth. The recent retirement of some debt obligations should also drive improved financial flexibility. We also expect the bottom line to improve going forward, given that the recent settlement of the TAJ audit was a one-off expense.

Projections and Valuation

The relative valuation approach was used to obtain a fair value of CPJ. We projected a 2024 EPS of US\$0.005795 and an estimated 2024 BVPS of US\$0.033203 based on the five-year historical performance and projected future growth. We established an average retail industry P/E and P/B of 12.0x and 2.70x, respectively, based on a review of its peers. Applying both multiples to our projections yielded an average target price of J\$12.30 when converted to JMD.

Risks to Price Target

Our price target may not be realized if the firm is unable to contain its operational expenditure, if the St. Lucian and Jamaican Tourism sectors experience exogenous shocks, if there are regulatory changes that adversely impact the company's bottom line or if the exchange rate fluctuates adversely impacting profits.

NINE MONTHS ENDED MARCH 31, 2023

CPJ Group's operating revenue for the nine (9) months ending March 31, 2023, was US\$107.04 million, representing a 23.8% increase compared to the previous year's revenues of US\$86.44 million. Revenue growth was driven largely by incremental growth in volumes, the introduction of new product lines and the development of online business. At the same time, Cost of operating revenue increased by 27.9% to US\$75.25 million from the US\$58.83 recorded for the same period in 2022. This resulted in Gross Profit margin of 29.6% for the period compared to a margin of 31.9% in the previous year, as the increase in costs outpaced revenue growth. Despite the significant growth in sales, CPJ is still managing fluctuations in commodity prices and higher-than-normal levels of inventory to maintain a consistent supply for its customers. The ongoing instability in the supply chain has reduced the year-over-year (YoY) margins attributable to the company.

Selling and administrative expenses for the nine-month period were US\$19.62 million, a 33.6% increase compared to the previous year (2022: US\$14.68 million), mainly due to increased staffing levels as the company positions itself for further growth. Marketing and advertising expenses increased significantly compared to the previous year due to the return to normal activities compared to the pandemic conditions. Similarly, utility costs increased by 17% compared to the previous year, driven by additional distribution and manufacturing activities and overall increases in local utility charges. Additionally, there was an extraordinary expenditure of US\$1.45 million resulting from the settlement of the TAJ Audit for the years 2012-2015. The foregoing resulted in Operating Profit decreasing to US\$7.52 million from US\$10.20 million, or by 26.27%.

Total assets increased by US\$7.59 million compared to the same period last year (2022: US\$78.57 million), primarily due to an increase in inventory of US\$9.21 million and an increase in cash of US\$643 thousand. However, accounts receivables decreased by US\$1.25 million compared to the same period last year (2022: US\$19.29 million). CPJ recorded an increase in accounts payables of US\$3.06 million compared to the previous year (2022: US\$12.49 million). Additionally, CPJ redeemed a J\$500M Bond during the quarter. The company's current liabilities remained relatively unchanged, while total equity increased by US\$4.28 million, representing a 19.0% improvement over the prior year.

Despite the 25.7% increase in sales compared to the same period last year, accounts receivables decreased by 6.5% compared to the previous year. The accounts receivable days for the period ending March 31, 2023, were 45 days (2022: 61 days), indicating the company's continued strength in credit management policies. The Current Ratio of 2.45x also improved YoY by 16.0%.

OUTLOOK

Caribbean Producers (Jamaica) Limited (CPJ) focuses on local and overseas expansion project.

Caribbean Producers (Jamaica) Limited (CPJ) is planning a US \$7 million expansion in Jamaica and St. Lucia to accommodate the growing tourism sector and the influx of 6,000 additional hotel rooms. The company will invest in an 800kW solar project, a processing plant development, and normal capital expenditure. CPJ is experiencing increased sales due to the booming tourism industry and aims to capitalize on the growth by expanding its operations and product offerings. The expansion will be funded internally to avoid taking on more debt in the current high-interest rate environment. Despite a decrease in consolidated net profit, CPJ has shown improved cash flow from operations and recently retired a J\$500 million bond. The company plans to open new stores, especially on the eastern side of Jamaica, and targets the growing market of villas along the north coast. Additionally, CPJ aims to expand its presence in the Eastern Caribbean region through its St. Lucian subsidiary.

Based on the expansion plans and strategies outlined by Caribbean Producers (Jamaica) Limited (CPJ), the company appears to be well-positioned for future growth and profitability. The planned investments in solar energy, processing plant development, and capital expenditure indicate CPJ's commitment to enhancing its operations and meeting the demands of a growing tourism sector.

CPJ's focus on the local tourism market, particularly with the anticipated increase in hotel rooms and the influx of visitors, presents significant opportunities for the company to expand its sales and distribution channels. The partnerships with hotels and the distribution of the Sazerac brand in the spirits business are expected to contribute to future sales growth.

Furthermore, CPJ's plans to open new stores, explore potential locations on the eastern side of Jamaica, and tap into the market for villas along the north coast demonstrate a strategic approach to capturing emerging markets and diversifying its customer base. However, CPJ will need to navigate challenges such as high interest rates and market uncertainties. The decision to fund the expansion internally reflects a cautious approach to debt management and a desire to maintain financial stability. Overall, with a focus on organic growth, improved cash flow, and potential dividend resumption, CPJ appears to have a positive outlook for the future. The company's ability to successfully execute its expansion plans and effectively adapt to market dynamics will be key factors in determining its long-term success. While facing market uncertainties, CPJ remains focused on strategic growth and profitability. The company intends to strengthen its position in the market and is considering resuming dividend payments in the future.

INVESTMENT POSITIVES

- **Strategic partnerships:** CPJ is focused on building strategic partnerships with key customers, which can enhance its market position and drive long-term growth.
- **Efficiency-enhancing investments:** The company is evaluating capital investment projects and selective expansions to improve efficiency. This can lead to cost savings and improved operational performance.
- **Online platforms:** CPJ is actively advancing its B2B and B2C online platforms, leveraging technology to reach a broader client base. This can increase sales and market penetration.
- **Growth in tourism:** CPJ expects continued growth in the tourism industry, which can positively impact its business. The anticipated expansion in the number of available hotel rooms presents opportunities for increased demand for CPJ's products and services.

Local and Overseas Expansion: The company aims to be strategic in how they expand their business in Caribbean with equity capital rather than debt which could help them capitalize on the recovering tourism sector.

INVESTMENT NEGATIVES

- **Supply chain challenges:** The current business environment is characterized by supply chain challenges, which can impact CPJ's ability to procure necessary inputs and fulfil customer orders on time. This may lead to operational disruptions and potential revenue loss.
- **Potential disruptions from the war in Europe:** CPJ acknowledges that the ongoing war in Europe can cause logistics challenges. Uncertainty and disruptions in international trade can adversely affect the company's supply chain and overall business operations.
- **Tax settlement impact:** CPJ faced an extraordinary tax settlement of US\$1.45 million, which had an impact on its financial results. Such unexpected tax liabilities can put a strain on the company's profitability and cash flow.
- **Concentration Risk:** Most of CPJ's operations are centralized in Jamaica.



CONCLUSION

The outlook for the tourism and hospitality sector has remained optimistic since the start of the financial year. CPJ continues to benefit from the recovery of the hospitality sector through its reporting of positive earnings throughout the year. Looking ahead to the final quarter of the year, CPJ aims to maintain high levels of service and quality products to ensure the success of customers and shareholders. The current environment, characterized by supply chain challenges and potential disruptions from the war in Europe, is expected to continue causing logistical difficulties. However, CPJ's management is focused on strengthening core business capabilities and forging strategic partnerships with key customers. The company is evaluating capital investment projects to enhance efficiency and considers expansions in manufacturing and operational areas to increase capacity and efficiency ahead of the influx of 6,000 additional hotel rooms to be built in next three (3) to five (5) years. CPJ is also investing in energy-saving projects and information technology systems to reduce costs and improve customer service. The company is advancing its online platforms to reach a broader client base through technology.

The improved performance of CPJ instills confidence in the management team and business model. Despite the impact of an extraordinary tax settlement of US\$1.45 million, Q3 unadjusted profit before tax reached US\$2.09 million, showing consistent growth compared to the previous year.

Based on our assessment of the health of the company and our expectation of what is likely achievable based on our analysis, we have established a price target of J\$12.30 which is above the current market price of J\$9.72 and is undervalued relative to current price levels at this time. Despite the rebound in tourism which bodes well for CPJ's operation, pivotal to their future success will be how debt is managed in the long-term with the expansion projects in mind. Also, CPJ will corporate tax due to the expiration of the corporate tax remission which could dampen earnings growth. All these factors taken into consideration; we recommend investors **OVERWEIGHT** the stock.

SOURCES

Caribbean Producers Jamaica Limited Annual Reports, Jamaica Stock Exchange (JSE), The Gleaner Company, Loop News Jamaica, The Jamaica Observer, and the Financial Services Commission (FSC)

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- **OVERWEIGHT** - Security is deemed to be undervalued and is expected to outperform compared to the average market return and/or return of comparable securities in the same sector or industry.
- **MARKETWEIGHT** – Security is expected to provide similar returns compared to the market in general or at the same pace as comparable companies; neither strongly positive nor negative.
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