

Equity Analysis: LASCO Manufacturing Limited (LASM) 9M 2023-24

VMWM Research | March 20, 2024



- Recommendation: **OVERWEIGHT**
- Price Target: **\$7.69**
- Close Price: **\$4.91**

- Shares Outstanding: 4,132,913,151 units
- Financial Year End: March 31

ABOUT THE COMPANY

LASCO Manufacturing Limited is a limited liability company that was incorporated in Jamaica in 1994 and is registered at 27 Red Hills Road, Kingston 10. It mainly operates out of its location in White Marl St. Catherine where it manufactures its products.

The entity was formed through the merger of LASCO Foods Limited and LASCO Foods (Successors) Limited that was complete with a name change in 2010 to its current name. It manufactures and sells soy-based products (often in powdered form), water, juice and milk-based products. It also provides canned products, condiments, seasoning, herbs and spices, soups, baby and personal care products to overseas markets, namely the Caribbean region, Canada, Central and South America, the United Kingdom and the United States of America.

FINANCIAL PERFORMANCE

J\$'000	FY 2022/23	FY 2023/24	9M 2022/23	9M 2023/24
Revenue	9,481,244	11,242,598	8,329,970	9,241,569
Operating Profit	2,223,058	2,689,200	1,973,279	2,412,136
Net Profit	1,707,485	2,081,897	1,464,031	1,695,997
Total Assets	12,067,412	13,740,763	12,993,551	15,245,181
Total Liabilities	2,719,145	2,642,969	2,594,545	2,935,866
Total Equity	9,348,267	11,097,794	10,399,004	12,309,314
ROE (%)	18.3	18.8	14.08	13.78
Inventory Turnover (x)	4.51	4.09	2.65	3.41

Dividend Payments

The Board of Directors of the Company, at its discretion, may declare an interim dividend to its shareholders. Declared dividend payments may be made from net profits, each year after taking into consideration regulatory requirements, if any. Over the last five years the company on average have a dividend payout ratio of 19%. For the current financial year, annual dividend amounted to \$0.12 per share which translates to a dividend yield of 2.44%.

Outlook

LASM product mix includes essential items such as food staples that tend to be resistant to inflationary pressures, within this context earnings projection is expected to steadily increase to meet demand. Mounting geopolitical tensions between Russia-Ukraine, Israel-Hamas, and uncertainty regarding the Red Sea and Panama Canal waterways, is expected to exacerbate and prolong supply chain challenges resulting in higher demurrage cost and delayed shipping which we anticipate could be partially passthrough to retailers to maintain sales margin.

Projections and Valuations

We used a combination of a Comparative and an Absolute approach to determine the value for the stock. For the Absolute approach, a cost of equity 11.20% was used to discount the expected future cash flows. For the comparative approach, a 2024 forward EPS of \$0.63 and an applied P/E of 10x were deemed appropriate and used to determine a relative value. By averaging both approaches, we obtained a consensus target price of **\$7.69** which represents a potential upside of 56.53% relative to current price levels.

Risks to Price Target

We anticipate that our target price may not be realized if the level of inflation persists, which may result in higher for longer interest rates aimed at cooling demand and compressing production. This may temper consumer sentiment and ultimately affect the sale of LAM's products. Additionally, supply chain challenges remain a concern which could hamper business operations.

NINE MONTHS ENDED DECEMBER 31, 2023:

For the nine (9) months period ended December 31, 2023, LASM reported higher revenue of \$9.24 billion or by 10.94% when compared to a corresponding period in the prior year underpinned by a mixture of elevated prices and increased volume. Similarly, Cost of Sales climbed to \$5.76 billion relative to \$5.28 billion resulting in an improvement in Gross Profit Margin to 37.6% from 36.6% for the prior period and above the five-year average of 36.7%, gross profit amounted to \$3.47 billion.

Operating Expenses grew to \$1.17 billion in tandem with a recharge in business operations, an equivalent \$81.48 million increase over the prior year's results. Additionally, the Company maintained its expense ratio of 13% over corresponding periods signaling improvements in efficiency levels. Resultingly, profit from operations pivoted to \$2.41 billion against \$1.97 billion reported in the previous year over a similar period. Profit before tax also advanced to \$2.39 billion, representing a 16.87% increase for the 9-month period. This cascaded into a net improvement in earnings of \$1.69 billion when compared to \$1.46 billion in the prior year indicating a 15.8% increase in profits available to shareholders (9M EPS: 41 cents).

For the 9-month period total assets climbed to \$15.25 billion on the back of a significant jump in short-term investments and cash balances of 61.64% (\$2.61 billion) and 67.26% (\$2.84 billion) respectively. Receivables were also higher by 17.02% to \$2.82 billion while inventory contracted to \$1.69 billion, 15.29% below the prior figure due to inflationary pressures. LASM continues to grapple with high demurrage costs and delayed shipment underscored by prolonged geopolitical conflict and more recent disruption at the Red Sea supported by inventory turnover ratio of 3.41 times which may indicate insufficient stocking.

Total Liabilities exceeded the previous period by 19.6% totaling \$2.01 billion dominated by a 55.01% increase in payables to \$1.28 billion. It is noteworthy that the company has no long-term loans and maintains the trend of reducing the current portion of long-term debt by 66.9%, closing the period at \$66.12 million. This translated into overall improvements in liquidity underscored by higher current and quick ratios of 5.0x and 4.1x respectively.

Total Equity ballooned to \$12.31 billion from \$10.40 billion or by 18.37%, which was largely attributable to notable higher retained earnings of 21.7% to \$11.75 billion, however this was tempered by significantly lower reserves which translated to a return on equity of 13.8% for the period. Share capital amounted to \$563.17 million, which have since March 2020 exceeded the 500 million limit set by the Jamaica Stock Exchange for junior stock market companies. As a result, LASM will migrate to the JSE main market effective March 27, 2024.

OUTLOOK

LASCO Manufacturing Limited continues to be plagued by the headwinds of inflationary pressures, mounted with geopolitical tensions between Russia-Ukraine, Israel-Hamas, and logistical disruption at one of the most heavily traveled waterways in the world, the Red Sea. This along with severe climate conditions negatively impacting the Panama Canal is expected to exacerbate and prolong supply chain challenges resulting in higher demurrage cost and delayed shipping. Nonetheless, the Company is poised to take mitigatory action to minimize and contain disruptions in business operations. Despite the improved consumer sentiment which grew to 174.7 points in the fourth quarter of 2023, annual inflation grew 7.4% year to date, the highest since February 2023. This further emphasizes that inflation may persist and compress the Company's margins marked by elevated raw material costs. It is noteworthy that LASM has reduced its debt significantly, currently the Company has no long-term debt on its books and has been steadily decreasing the current portion of its debt. This places LASM in an opportunistic position as it plans to seek acquisitions that conform to its business matrix.

INVESTMENTS POSITIVES

- The company has maintained a 5-year trend of profitability, which depicts resilience and supportive measures.
- Reduction of debt load, LASM currently has no long-term debt on its books making it attractive to take on investment opportunities as they arise.
- Competitive since the LASCO brand is a household name and carries a wide customer base.
- The company will migrate to the main market on the Jamaica Stock Exchange increasing its access to capital.

INVESTMENTS NEGATIVES

- Inflationary pressures compress margins owing to elevated input materials.
- Geopolitical conflicts exacerbate and prolong supply chain challenges.
- Lack of diversification since the Company predominately operates locally.



CONCLUSION

LASM product mix includes essential items such as food staples that tend to be resistant to inflationary pressures, within this context earnings projection is expected to steadily increase to meet demand. Mounting geopolitical tensions between Russia-Ukraine, Israel-Hamas, and uncertainty regarding the Red Sea and Panama Canal waterways, is expected to exacerbate and prolong supply chain challenges resulting in higher demurrage cost and delayed shipping which we anticipate could be partially passthrough to retailers to maintain sales margin.

Based on our assessment of LASCO Manufacturing Limited, using a discounted cash flow model and the comparative based approach we have established a price target of \$7.69. When compared to the current price of \$4.91 and including the annual dividend yield of 2.44%, translates to an upside potential of 58.97%. Therefore, we recommend that investors **OVERWEIGHT** the shares in their portfolio.

SOURCES

LASM Annual & Quarterly Reports, Jamaica Stock Exchange (JSE), The Gleaner Company, Loop News Jamaica, The Jamaica Observer, and the Financial Services Commission (FSC).

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DEFINITIONS

- **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.
- **UNDERWEIGHT** – Security is deemed to be overvalued and is expected to underperform compared to the average market return and/or return of comparable securities in the same sector or industry.
- **ZEROWEIGHT** – This security is substantially distressed or at risk of a shock which may significantly impair its value.