Company Analysis: Honey Bun (1982) Jamaica Ltd. (HONBUN) 6M 2024

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- Recommendation: **MARKETWEIGHT**
- Current Price: $7.77
- Price Target: **$8.43**

- Shares Outstanding: 471,266,950 units.
- Financial Year End: September 30

ABOUT THE COMPANY

Honey Bun was established in 1982 when Herbert and Michelle Chong acquired two small bakery outlets in Kingston. They have since become known for producing and distributing baked goods under their three distinctive brands: Honey Bun, Island Bites, and Buccaneer Jamaican Rum Cakes. In 2011, guided by the Chong's and their advisors, Honey Bun (1982) Limited (HONBUN) achieved a significant milestone by becoming the first wholesale bakery to be publicly listed on the Junior Market of the Jamaica Stock Exchange. Since that momentous occasion, the company has garnered numerous awards for its exemplary leadership, innovation, and best practices, solidifying its role as an industry trailblazer. Honey Bun operates six locations in Kingston and has expanded its presence with 6 additional branches in Ocho Rios, Spanish Town, Old Harbour, Santa Cruz, Morant Bay and Savanna-La Mar.

Its products are exported throughout the Caribbean region as well as to the UK, US, and Canada. The company is eyeing further expansion in 2024 with a $1 billion dollar investment earmarked for said goal.

FINANCIAL PERFORMANCE SUMMARY

J$ 000	FY 2022	FY 2023	6M 2024	6M 2023
Revenue	2,953,316	3,412,758	1,936,279	1,695,638
Operating Profit	246,799	276,919	220,789	171,323
Net Profit	203,486	232,091	167,742	131,058
Total Assets	1,527,015	1,738,278	1,944,019	1,658,226
Total Liabilities	367,702	422,276	521,540	424,409
Total Equity	1,159,312	1,316,001	1,422,479	1,233,817

Dividend Policy

HONBUN does not have a definitive dividend policy but has recently paid out interim dividends of $0.13 per share an approximate yield of 1.67%. HONBUN has also declared a dividend payment of $0.03 per share payable on June 12, 2024.

Outlook

We expect HONBUN to enhance its profitability further, driven by the growing demand for its new products and the $1 billion investment for expansion. Additionally, the local economy has been robust, and this should support revenue growth for HONBUN.

Projections and Valuation

We used a combination of a Comparative and a Discounted Cashflow Model to determine the value for the stock. For the DCF approach, a cost of equity of 15.70% was used to discount the future levered free cash flows. For the comparative approach, a 2024 forward BVPS and EPS of $2.04 and $0.72 respectively were used. An applied P/B and P/E of 1.91x and 13.00x were deemed appropriate and were used to determine a relative value. By averaging all three approaches, we obtained a consensus target price of **$8.43.**

Risks to Price Target

We believe that the company may experiences challenges to achieve our projected target price as the market is currently unstable and investor sentiment has not been strong despite the company being fundamentally sound. Additional risks to price include volatile commodity costs, which could be exacerbated by the persistent geopolitical tensions in the Middle East. However, the company's intent to respond to that potential threat by increasing inventory along with its expansion and projected revenue growth as a result, should see the price target being achieved.

Six (6) MONTHS ENDED March 31, 2024

HONBUN increased its revenue to $1.93 billion from $1.69 billion or by 16.96%. This was attributed to an increase in the demand for their products, satisfied by an improved efficiency in both production and distribution along with an expansion island wide with three additional distribution centers, such as the Savannah-La-Mar outlet in October 2023.

Cost of sales (COGS) grew by 7.16%, which was less than half the growth in revenue. This suggests commendable efficient management underscored by their investment in the production process with a focus on automation. This resulted in the COGS margin having a 3.03% reduction from the 56.30% ratio in the comparable period to 53.27% in the current period. Since sales revenue growth was higher than the increase in the COGS, Gross Profit improved to $904.63 million from $732.98 million when comparing the respective periods. Gross profit margins also increased from 43.20% to 46.70% in tandem with the decrease in COGS margin.

Operating Profit saw a 28.87% increase to $220.78 million from $171.32 million despite the uptick in Administrative Expenses and Selling & Distribution costs, which went up by 17.75% and 22.67% respectively. Net profit increased to $201.95 million or by 46.25% from $138.08 million in the corresponding period. The increase in demand for the company's products, which spilled over into their revenues, was the main factor for this.

As of March 31, 2024, Honey Bun's total assets amounted to $1.94 billion, reflecting a 17.23% rise compared to its asset position on March 31, 2023, when it stood at $1.65 billion. This growth can be primarily attributed to the expansion of its Inventories and cash and cash equivalents, which increased by 28.96% and 39.35% respectively. The considerable increase in inventory demonstrates the company's intent to navigate current and potentially future supply chain challenges. Furthermore, the substantial increase in Investments also played a significant role in boosting the total assets, surging from $97.75 million to $117.54 million.

Total Liabilities saw an uptick to $521.54 million from $419.82 million, marking a 24.23% increase. This increase was mainly driven by significant growth in payable, taxation payable, and current portion of lease liability, which expanded by 44.02%, 34.27%, and 10.30%, respectively.

Total Equity increased to $1.42 billion from $1.23 billion, representing a substantial growth of 15.29%, primarily driven by a 16.64% increase in retained earnings. This enhancement in both the company's earnings and its total equity resulted in an improved Return on Equity (ROE), which surged from 10.62% as at March 31, 2023, to 11.79% as at March 31, 2024.

The current Ratio fell to 2.47x from 2.51x or by 1.65%, mainly attributed to the increase in taxation payable. Notwithstanding, the current ratio for the period is above the benchmark 1.00x and indicates that the company remains in a strong liquidity position and will not likely face any challenges in meeting all its short-term obligations.

The increases in the DSO (Days Sales Outstanding) and DPO (Days Payables Outstanding) from 37.32 and 95.05 to 42.2 and 103.03 respectively, were mainly influenced by the 17.23% increase in accounts receivable and the 34.27% increase in accounts payable. This may indicate further initiatives are needed to improve the financial processes of the company, so as to improve overall efficiency.

OUTLOOK

$1 billion dollar expansion

HONBUN is set to invest $1 billion to establish a new production facility in Angels, St Catherine. This facility, spanning 160,000 square feet, will more than double the company's manufacturing capacity. The lease agreement for this four-and-a-half-acre property was signed recently, and the facility is expected to become operational between November this year to January 2025. The growing demand for HONBUN's products, as emphasized by the company, makes this expansion crucial to meeting this demand. The expansion is a key part of HONBUN's strategic growth plan and the new location, which is between two major highways, will provide access to a broader market across Jamaica. This expansion should be a positive adage to HONBUN's top line as the local economy remains robust and unemployment remains low, which should result in continuous strong demand for their products.

Positive local economic outlook

Jamaica's economy has remained robust throughout the high inflation and high interest rat environment. Unemployment hit an all-time low rate of 4.20% in October 2023, while tourism has been strong with total arrivals in the first two months of 2024 amounting to 1 billion. The low unemployment rate along with the income tax threshold increase give more disposable income in the hands of employed Jamaicans. This could see an increase in the demand for HONBUN's products as the year progresses and consumers start to spend more of that disposable income.

Potential for increase sales in the export market due to the robustness of the US and UK economies

HONBUN exports to the US and UK and is intending to increase its inroads into the overseas markets. The US labour market has withstood the pressures of the high interest rate environment, with unemployment still below 4.00%. The Federal Reserve is also looking to cut rates this year which could act as a stimulus to the economy. In the UK, inflation 12-month inflation has fallen to 2.30% just 30 basis points above the target. The possibilities of rate cuts are looking increasingly likely in the UK, who just came out of a technical recession in 2023. The positive outlook for both the US and UK economies could see an increase in demand for HONBUN's products which could be facilitated by the expansion project already in progress.

INVESTMENTS POSITIVES:

- Maintenance of costs to production in a difficult economic environment is proof of the company's dedication to efficient cost strategies.
- Improved profits and earnings are expected to continue as the company is still on its path of expansion of distribution centres.
- Positive outlook for the local and overseas economies could serve as an additional driving force behind sales

INVESTMENT NEGATIVES

- The increased operational costs that will accompany more manufacturing activity may strain profit margins and efficiency.
- The business is exposed to the volatility of the global commodity market which may result in increased raw material costs.
- Geopolitical tensions may result in supply chain issues which would still negatively impact the company despite their efforts to increase inventory.
- Government regulations could lean toward banning sugary snacks in school which would have significant implications for HONBUN's top line.

CONCLUSION

HONBUN is expected to continue to grow and improve its profit lines as the business is in a stage of organic growth which is concerned with expanding its distribution channels. The company's $1 billion dollar investment to establish a new production facility in St.Catherine should result in a greater platform for the increase in demand for their products to be met. This would likely be reflected in the company's top and bottom line and therefore its margins. Risks to the achievement of this strategy include the ability to continue to efficiently operate via cost effective inventory management and the possible impact of ongoing geopolitical tensions. However, the company's profit margin remains strong and their intent to continue to invest in cost management initiatives should bode well for the company.

Using an Intrinsic Approach with a cost of equity of 15.70%, we valued the company at $8.43 per share. Applying a P/E multiple of 13.00x and a P/B multiple of 1.91x, in line with the average of its peers on the Jamaica Stock Exchange, we arrived at a consensus target price of $8.43 which is a 6.89% upside from the current price of $7.77. Considering this, we have assigned an **MARKETWEIGHT** rating to the stock.

SOURCES

Honey Bun (1982) Jamaica Limited Annual Reports and Quarterly Financial Statements

DISCLAIMER

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.