



Caribbean Producers Jamaica Ltd. (CPJ)

Company Overview:

Caribbean Producers Jamaica Limited (CPJ) was founded in April 1994 as an institutional food service distributor selling consumable products to the hospitality industry. The company was previously in the business of producing liquid pasteurized eggs with a partner, Caribbean Egg Processors Limited, however, the Company exited that business in September 2015. In addition to their distribution business, CPJ now manufactures its own line of beverages and meat products and has added a non-core business line which includes its CRU Bar and Kitchen and CPJ Market.



CPJ is recognized nationally as a leading food, non-food, wines & spirits distributor for major, international renowned brands



The Company mainly distributes to the hotel and other companies in the hospitality sector.

For the year ended June 2019, the Group posted record revenues of **US\$109.62M** but was hit with a compression of margins, rising non-budgeted variable costs along with the extraordinary write-off of IT asset, resulting in a loss of **US\$1.17M** for the group. While for the 6-Month period ending December 31, 2019 CPJ posted profits of **US\$0.52M**. However, with the current coronavirus outbreak which has dampened economic activity particularly in the hospitality sector, another poor year seems likely for the Company and this could likely extend into the next financial year if the economic activity is not returned to normalcy in the upcoming months.



Key Features:

Current Price	J\$2.87
One-Year Price Target	J\$1.99
Implied Downside	-30.68%
52 Week High	J\$5.30
52 Week Low	J\$2.00
YTD Gain/Loss	-44.73%
Current P/E (x)	47.83X
Market Capitalization (J\$B)	J\$3.16B

SELL

Target Price: J\$1.99

Potential Downside: -30.68%

Moderate to HIGH RISK

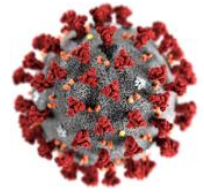


Analyst's Opinion

CPJ is a leading food service supplier to the hospitality sector in Jamaica, with over 25 years of experience. Over the years, the Company has focused on generating operational efficiencies in order to remain competitive in a fast-changing industry and where the cost structure of the business is such that its gross and net profit margins are extremely low. The knock-on effect of the low margins is that the Company does not have the flexibility to absorb cost shocks without generating losses. Over the years, CPJ has tried to diversify its business to serve clients in the wider hospitality and retail sectors, however, its revenues are still dominated by its transactions within the tourism industry. As a result, with the current virtual shuttering of hotels and the limits placed on areas in the hospitality sector, such as bars and restaurants, and supermarkets our projection is that over the short to medium term, CPJ's profitability is likely to decline significantly, which was the driving factor for our valuation estimate. CPJ's stock is currently trading at **J\$2.87** while our one year target price is **J\$1.99** which implies that the stock is trading at a premium of **~44%** and as a result we recommend that clients **SELL** the stock and assign a **MODERATE** to **High** risk rating to the security.

Impact of COVID-19 on CPJ

The unprecedented spread of COVID-19 has created a global health crisis. Each day presents new developments as countries around the world seek to “flatten the curve” by practicing social distancing measures which is significantly reducing economic activity around the world. According to data from the World Travel and Tourism Council, travel and tourism either directly or indirectly accounted for **31.10%** of Jamaica's 2019 gross domestic product (GDP), **32.80%** per cent of employment and almost **57.00%** of the country's total exports. The tourism and hospitality industry is one of the most directly impacted industries as a result of COVID-19's social distancing measures.



Most hotels across Jamaica are now closed and with the government ramping up its social distancing orders, restaurants and bars are fully closed or are open but with reduced operating hours. Some of the local hotels have initially indicated that their facilities will be closed for at least two months but it is likely that even if they reopen after two months they will not be back to full capacity as their guests may require a longer lead time to get comfortable with travelling and mingling in large groups. The lion's share of CPJ's revenues are generated from companies within the tourism and wider hospitality sector, while some is generated through retail channels like supermarkets, wholesales, restaurants, bars and variety stores.

Considering the outbreak of the coronavirus pandemic, we expect business and consumer confidence to be significantly lower in the first to the second quarters of 2020 and possibly beyond. The reduced confidence levels are already reflected in the Main and junior markets of the Jamaica Stock Exchange (JSE) that have fallen off by over **20.00%** year to date as investors increasingly sell down their positions to be in a liquid position to respond to the pandemic.

In response to the coronavirus outbreak, the Government of Jamaica announced a raft of measures to support the business and individuals likely to suffer from the fallout of the virus¹. Notwithstanding, with the current outbreak it is likely that Jamaica will realize negative growth in 2020. Consequently, given its direct exposure to the hospitality service, we expect CPJ’s revenues and profits to be significantly negatively impacted in 2020 and possibly 2021.

CPJ's Product Type/Revenue Stream	Main Customer Base	Impact
Beers and Spirits	Hospitality Sector and Retail Customers	Hotel closures and restrictions placed on bars, restaurants and retail outlets, such as supermarkets, likely to result in significant revenue reduction for CPJ.
Ready to Drink Beverages	Retail Customers	
Beverage Systems	Hospitality Sector and Retail Customers	
Chemicals	Hospitality Sector Customers	
CPJ Market	Retail Customers	
CRU Bar + Kitchen	Hospitality Sector Customers	
Food & Dry Goods	Hospitality Sectors	

Positive and Negative

Positives

- 1 Market Leader Position:** CPJ has an established distribution operation with over 25 years’ experience. Over the years the Company has established itself as the market leader providing food service to the tourism sector.
- 2 Diversified Distributor:** Although the lion’s share of the Company’s revenues come from the hospitality sector, over

the years CPJ has managed to achieve some diversification which now sees them serving other areas such as retail, supplying their products to large supermarket chains, superstores, independent wholesalers, supermarkets and small retail outlets.

Negatives and Risks

- 1 High Exposure to the Hospitality Sector:** CPJ is very dependent on the hospitality sector which is very seasonal. A downturn in the hospitality sector is likely to have a material negative impact on the Company’s income.
- 2 Buyer Power:** CPJ is largely a distribution company distributing predominantly to large hotel chains. As a result, CPJ’s clients have a high bargaining power which typically squeeze the Company’s margins. Consequently, the Company operates with little room to absorb cost shocks without incurring losses.

- 3 Highly Competitive Industry:** As a result of the low barriers to entry, new entrants may enter the market easily and impact the group’s profitability and new or existing competitors can easily attempt to take CPJ’s market share in the hospitality sector, by undercutting their prices.
- 4 Thin and declining Gross and Net Profit margins:** Over the six-year period from FY 2014 to FY 2019 CPJ’s gross profit and net profit margins have consistently declined year after year from 29% to 24 and 4.38% to -1.07%. The knock-on effect of the low margins is that the Company does not have the flexibility to absorb cost shocks without generating losses

¹ <https://mof.gov.jm/mof-media/media-centre/press/2633-fiscal-stimulus-response-to-the-covid-19.html>

Valuation Analysis

To value CPJ we used the Price to Earnings (P/E) and the Free Cash Flow to Equity methods. In using the P/E method we compared CPJ to two other food product distributors listed on the Junior Market of the Jamaica Stock Exchange in Derrimon Trading Co. Ltd. and Lasco Distributors Ltd. companies listed on JSE's Junior Market in similar business line. The industry's average price to earnings as at April 15, 2020 was **17.53X**. When the average P/E is applied to CPJ's 1-year forward earnings of **0.0702** US cents a fair value of **US\$0.0123** or **J\$1.71** is produced.

The second method used was the Free Cash Flow to Equity method. With a required return of **12.96%** and a perpetual growth rate of **5.00%**, it was determined that the Company's shares were valued at **J\$2.27**. To arrive at a final valuation, we averaged the results of the two-valuation methods and arrived at a final valuation of **J\$1.99**. At the current price of **J\$2.87** CPJ's shares are trading at a premium of **44.22%** to our one year price target.

Appendix

Financial Statements Extract

CPJ's Income statement (US\$)

	June 30, 2014	June 30, 2015	June 30, 2016	June 30, 2017	June 30, 2018	June 30, 2019	Dec 31, 2018	Dec 31, 2019
	FY2014	FY2015	FY2016	FY2017	FY2018	FY2019	FY2019 Q2	FY2020 Q2
Gross operating revenue	79,006,082	86,850,246	94,104,389	98,288,970	107,795,501	109,620,529	53,729,746	59,465,065
Cost of operating revenue	(56,075,293)	(62,125,820)	(68,998,334)	(71,155,666)	(79,367,737)	(83,397,830)	(40,264,551)	(44,197,808)
Gross profit	22,930,789	24,724,426	25,106,055	27,133,304	28,427,764	26,222,699	13,465,195	15,267,257
Gross Margin	0.2902	0.2847	0.2668	0.2761	0.2637	0.2392	0.2506	0.2567
Selling and administration expenses	(15,969,831)	(17,590,656)	(20,236,962)	(20,036,435)	(21,949,403)	(22,861,791)	(11,690,876)	(11,329,221)
Depreciation and amortisation	(1,759,632)	(2,164,373)	(2,448,629)	(2,641,917)	(2,460,328)	(2,466,027)	(1,209,687)	(2,134,763)
Expected credit losses						1,842	(98,724)	(36,000)
Write-off of intangible asset						(679,713)	(692,235)	
Other operating income, net	294,254	362,102	132,691	163,448	99,145	175,059		100,058
Operating profit	5,495,580	5,331,499	2,553,155	4,618,400	4,117,178	392,069	(226,327)	1,867,331
Finance income	679	3,609	12,557	953	191,791	569	278	592
Finance costs	(1,985,704)	(2,026,066)	(1,855,747)	(1,762,143)	(1,670,924)	(1,677,861)	(800,794)	(1,247,342)
Share of loss in joint venture	(58,797)	(37,652)	11,515					
(Loss)/profit before taxation	3,451,758	3,271,390	721,480	2,857,210	2,638,045	(1,285,223)	(1,026,843)	620,581
Taxation	7,055	163,142	329,505	(267,563)	(327,439)	117,354	(105,791)	(101,954)
(Loss)/profit for the year	3,458,813	3,434,532	1,050,985	2,589,647	2,310,606	(1,167,869)	(1,132,634)	518,627
Earnings Per Share (US Cents)	0.3144	0.3222	0.0953	0.2323	0.1908	(0.1063)	(0.1084)	0.0477

CPJ's Statement of Financial Position (US\$)

	June 30, 2014	June 30, 2015	June 30, 2016	June 30, 2017	June 30, 2018	June 30, 2019	Dec 31, 2018	Dec 31, 2019
	FY2014	FY2015	FY2016	FY2017	FY2018	FY2019	FY2019 Q2	FY2020 Q2
CURRENT ASSETS								
Cash and cash equivalents	2,995,323	3,049,479	4,004,917	2,763,268	3,756,720	4,212,776	3,173,068	2,920,917
Accounts receivable	13,576,049	12,121,195	13,159,888	13,908,764	15,214,933	15,889,156	20,221,590	22,560,430
Inventories	18,597,746	23,899,084	24,266,446	24,625,347	25,906,462	31,865,641	27,327,638	27,550,189
	35,169,118	39,069,758	41,431,251	41,297,379	44,878,115	51,967,573	50,722,296	53,031,536
CURRENT LIABILITIES								
Bank overdrafts	-	188,047	-	243,222	776,993	1,067,854	1,162,155	836,801
Short-term loans	6,325,000	4,925,000	5,100,000	2,500,000	1,700,000	5,150,000	6,150,000	6,356,712
Accounts payable	4,836,873	6,558,319	7,984,932	7,237,075	10,134,927	15,520,287	14,525,351	12,353,714
Short-term promissory notes	4,317,794	4,317,794	4,968,885	4,317,794	4,317,794	4,317,794	4,317,794	4,317,794
Current portion of long-term borrowing	365,695	523,444	464,469	475,310	615,127	1,070,490	633,072	652,290
Current portion of lease-liability	-	-	-	-	-	-	-	1,017,268
Taxation payable	177,180	175,753	175,376	578,804	450,413	70,648	480,192	446,174
	16,022,542	16,688,357	18,693,662	15,352,205	17,995,254	27,197,073	27,268,564	25,980,753
NET CURRENT ASSETS	19,146,576	22,381,401	22,737,589	25,945,174	26,882,861	24,770,500	23,453,732	27,050,783
NON-CURRENT ASSETS								
Investments	42,620	71,584	71,581	71,581	71,581	71,581	71,581	71,581
Interest in subsidiary	-	-	-	-	-	-	-	-
Interest in joint venture	219,786	159,186	-	-	-	-	-	-
Deferred tax asset	95,508	258,650	588,155	797,291	955,302	1,096,001	953,848	1,089,120
Property, plant and equipment	11,651,896	13,252,428	13,665,547	12,249,662	11,776,693	14,303,532	13,499,354	13,449,829
Intangible asset	-	19,070	91,494	158,550	707,091	32,585	71,805	75,467
Right of use asset	-	-	-	-	-	-	-	7,598,341
	12,009,810	13,760,918	14,416,777	13,277,084	13,510,667	15,503,699	14,596,588	22,284,338
<i>Net Current assets plus Non-Current Assets</i>	31,156,386	36,142,319	37,154,366	39,222,258	40,393,528	40,274,199	38,050,320	49,335,121
Total Assets	47,178,928	52,830,676	55,848,028	54,574,463	58,388,782	67,471,272	65,318,884	75,315,874
EQUITY								
Share capital	4,898,430	4,898,430	4,898,430	4,898,430	4,898,430	4,898,430	4,898,430	4,898,430
Accumulated surplus	11,289,402	13,969,969	14,475,108	17,030,012	18,606,749	17,074,870	17,414,381	17,599,041
Equity attributable to shareholders	16,187,832	18,868,399	19,373,538	21,928,442	23,505,179	21,973,300	22,312,811	22,497,471
Non-controlling interest	-	(109,215)	(106,579)	(71,836)	140,294	141,254	200,028	135,710
	16,187,832	18,759,184	19,266,959	21,856,606	23,645,473	22,114,554	22,512,839	22,633,181
NON-CURRENT LIABILITIES								
Long-term promissory notes	9,439,537	9,324,012	9,314,587	9,267,668	8,269,110	7,270,669	7,269,865	9,271,496
Long-term Borrowings	4,810,093	5,671,741	5,832,056	5,353,980	5,742,742	7,832,373	2,738,904	3,044,939
Due to related company	718,924	2,387,382	2,740,764	2,744,004	2,736,203	3,056,603	5,528,712	7,615,687
Lease liability	-	-	-	-	-	-	-	6,769,818
	14,968,554	17,383,135	17,887,407	17,365,652	16,748,055	18,159,645	15,537,481	26,701,940
	31,156,386	36,142,319	37,154,366	39,222,258	40,393,528	40,274,199	38,050,320	49,335,121

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