

## Quarterly Equity Review

Rating

**SELL**



**Salada Foods Jamaica Limited**

Global

Sector: Manufacturing

Sub-Industry: Food Manufacturing

JSE

SALF

Bloomberg

SALF JA

### Q1 2023: Salada targeting export growth despite supply challenges.

Salada's exports grew by 72% between 2018 and 2022 but growth in FY 2022 was only 6.9%. Given that the US is the company's main export market, Salada acknowledges that a lot of work needs to be done to increase its presence in America. In its effort to broaden its market scope, the company considers e-commerce as important and so its products are now available on Amazon.

The company's ambition is also to push its products deeper into new export markets with product innovation a key component of this strategy. One such market that Salada has its sights on is CARICOM. Breaking into other Caribbean markets would prove to be a great boon for Salada's growth prospects and given the relative closeness (both geographically and culturally), the company could tap into a long-lasting customer base, if they are successful.

One of the main threats to Salada's business model is persistent supply chain issues, ranging from the cost of materials to inconsistency in the supply of raw materials (coffee), particularly from local farmers.<sup>1</sup> In recent times, Jamaican coffee farmers have been experiencing record production. lows As a result, it is increasingly difficult and costly for Salada to source local coffee beans to meet their annual demand, especially given the stipulation by regulators that all coffee blends contain at least 30 per cent Jamaican coffee.<sup>2</sup> Additionally, the cess on imported coffee beans continues to negatively impact Salada's operations.

To counter these threats, Salada continues to diversify into non-coffee offerings, collaborate with local lawmakers on policies affecting the coffee industry and work directly with coffee farmers to increase their yields. Recently, the company and the Jamaica Coffee Growers Association launched a coffee sustainability initiative. This initiative will see Salada's manufacturing by-products (grounds) turned into organic fertilizer, to cost-effectively improve the yields of local coffee farmers.

<sup>1</sup> <https://www.jamaicaobserver.com/news/coffee-problem-brewing/>

<sup>2</sup> <https://www.jparliament.gov.jm/attachments/article/530/The%20Jamaica%20Agricultural%20Commodities%20Regulatory%20Authority%20Regulations,%202018---h.pdf>

April 21, 2023

Closing price	3.66
Forecast Dividend	0.12
Target price	2.84
<b>TOTAL RETURN</b>	<b>-19.1%</b>

#### Company Data

Outstanding shares	1,038,832,900
Market Cap	3,802,128,414
52-Week (Lo/Hi)	3.50/6.70
1Yr Daily Average Volume	14,971
5Yr Daily Average Volume	83,937

#### Major Shareholders

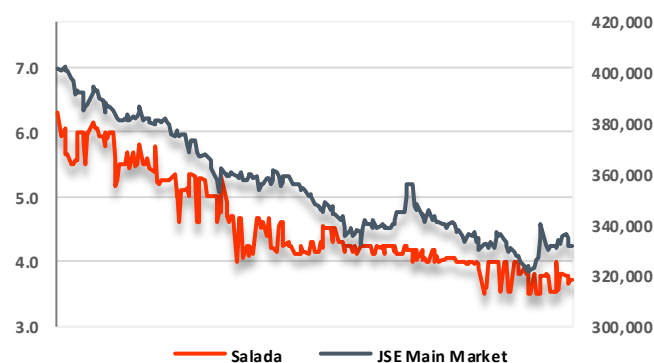
Resource In Motion Ltd.	65.07%
AIC (Jamaica) Limited	9.71%
Donwiz Limited	8.11%

#### Key Financials

J\$ Mn	FY21	FY22	FY23e	FY24e
Total Revenues	1,190	1,336	1,457	1,602
Operating Profit	182	224	259	300
Net Profit	157	175	203	238
Net Profit Change (%)	41.9%	11.9%	15.7%	15.7%
EPS	0.15	0.17	0.20	0.23
Dividend Yield	3.0%	2.0%	2.9%	3.4%

#### Price Performance

	1MTH	3MTH	1YR
Salada Foods	-2.6%	-7.7%	-42.2%
Main Index	3.1%	-2.4%	-16.3%



Source: Bloomberg; JN Fund Managers Limited

Return on Equity	Gross Margin	Net Profit Margin	Expense Ratio
2022: 17% (+6.2%)	2022: 30.8% (+1.5%)	2022: 13.1% (-0.4%)	2022: 14% (-6.7%)
2021: 16%	2021: 30.4%	2021: 13.2%	2021: 15%

## Financial Overview

### Revenue & Profitability

For the 12 months ending September 30, 2022, Salada reported revenues totalling \$1.34 billion, which was an increase of 12.3% over the previous year's out turn. Its's revenue growth locally, was attributable to improved distribution in trade channels as well as the successful introduction of their Flavoured Coffee line. Salada's export sales saw modest growth of 6.9% relative to the same period last year and was attributed, primarily, to the reopening of the Canadian market, as well as successful placement and positioning of the Ginger Turmeric instant teas in all main markets. The knock-on effect of the top line growth and reasonable expense management was a jump in Net Profits from \$156.8 million to \$175.42 million or by almost 12.0%.

In Q1 2023 (October to December 2022), the coffee maker struggled to grow its topline, with revenues for the period coming in at \$294.04 million, an increase of 1.62% over the similar period in FY2022, possibly indicating an end to the post-COVID-19 bounce. Additionally, despite maintaining its 32.0% gross margin, its Operating Profits came in much lower (at \$35.90 million vs \$43.16 million), as the manufacturer moved to re-engage its core consumers and pursued other marketing activities for the export markets. This resulted in a spike in sales and promotional expenses of around 24%. Further, an over 95% drop in finance income from almost \$13.0 million to less than \$1.0 million, ensured that Net Profit attributable to stockholders was 34.7% lower in the quarter at \$27.37 million, when compared to the corresponding period in FY 2022.

### Balance Sheet

At the end of FY2022 (September 30, 2022), total assets increased by 6.6% to \$1.35 billion. This was partly due to current assets increasing by \$107.0 million, propelled by investments, cash, and trade receivables. Investments grew by 53% on the back of increases in the company's investment portfolio, likely as the company moved to benefit from the increase in rates on money market instruments. Notably, inventories declined by \$53.80 million or 10% below the prior year. This decline was primarily driven by shortages of critical raw materials, namely Jamaican green coffee beans, which continues to hit record production lows year-on-year.

At the end of Q1 2023 (December 31, 2022), total assets declined by 13.7% to reach J\$1.17 billion from the end of FY 2022, as current assets suffered a 16.5% drop in value. Total liabilities at the end of FY 2022 was J\$302.6M, up 14.51% over the level it stood at the end of FY 2021. Following which, total liabilities declined by almost 50% to reach J\$152.3M at the end of Q1 2023, (December 2022).

## 3M Highlights

- **Marginal Revenue Growth** – Total revenues for Q1 2023 saw an increase of only 1.62% or J\$4.7 million compared to Q1 2022, possibly indicating an end to the post COVID-19 revenue surge.
- **Decline in Profits** – Operating Profit for Q1 2023 was J\$35.9 million, a 17% decline compared to the equivalent period in the prior year. Net profits declined by 35% to J\$27.4 million, when compared to Q1 of the prior year. The decline was primarily due to an increase in sales and promotional expenses as well as a reduction in Interest and FX gains.
- **Export Growth** – During Q1 2023, Salada pursued targeted digital marketing strategies designed to retain and grow consumers in main export markets. Salada is also seeking to expand its footprint in CARICOM markets and sent its first shipment to Antigua in March 2023.

## Risks to monitor

- **Local Supply of Coffee** – Salada's main risk currently appears to be the inconsistency in the supply of Jamaican coffee from local farmers. It is becoming increasingly difficult and costly for Salada to source enough local coffee beans to meet their annual demand, as coffee farmers are experiencing record lows in production. Adverse weather conditions may further impact the local supply.
- **Local Legislation** – Currently, local regulations stipulate that all coffee blends must have at least 30 per cent of Jamaican coffee, whether High Mountain or Blue Mountain. With the inconsistency in local coffee supply, coupled with this regulation, Salada's expansion ambitions are extremely challenging.
- **Raw Material Prices** – The volatility in global markets can have significant consequences for Salada's manufacturing businesses. Unexpected fluctuations in raw material costs and energy, for example, can destabilize markets and supply chains, making it difficult for the company to maintain/grow its margins.
- **Recessionary Fears** – With inflationary pressures remaining high, central banks continue to keep monetary policy tight, increasing the risk of a severe slowdown in economic activities for FY2023/24. A significant slowdown could potentially curtail Salada's revenue and profit growth in the future.

Earnings/Share	Cash Flow/Share	Dividend/Share	Dividend Yield
<b>2022: \$0.17</b> (+11.9%)	<b>2022: \$0.25</b> (+316.7%)	<b>2022: \$0.11</b> (+10%)	<b>2022: 3%</b> (+50%)
2021: \$0.15	2021: \$0.06	2021: \$0.10	2021: 2%

## Financial Overview

### Balance Sheet (Contd.)

Currently, Salada's liabilities include its accounts payables and tax payables only, as currently the manufacturer is debt free.

Driven by Salada's commendable profit outturn in FY 2022, total equity grew by 4.6% to close the year at \$1.05 billion. During the year its return on equity (ROE) was 16.7% compared to 15.6% in the prior year. At the end of Q1 FY 2023 its total equity was almost unchanged at J\$1.02 billion, after moving down by approximately J\$35.0M.

## Valuation Summary

### 1. Relative Valuation Method (Summary)

Industry Average P/E = 15.07x  
SALF's Forward Earning = J\$0.23  
P/E Valuation Est. = J\$3.45

### 2. Discounted Dividend Method (DDM) Method (Summary)

Required rate of return = 13.60%  
g = 5.87%,  
LT retention rate = 35%  
DDM Valuation Est. = J\$2.23

**SALF's Estimated Fair Price = \$2.84**

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