

CHINA
DEVELOPMENT
FINANCIAL

JB Foods Limited

(JBF SP/JBFO.SI)

2019 is looking good; upcoming 1Q19 results may provide short-term catalyst

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- JBF reported a poor set of 4Q18 earnings on 26 February 2019, where net profit declined 30% YoY to US\$4.5mn.
- However, profits declined at a lower 15% YoY when excluding one-off items such as the US\$2.2mn in deferred tax and US\$0.8mn in forex gains from a depreciating GBP.
- We believe its current price offers an attractive opportunity to accumulate ahead of its 1Q19 results, which we expect to be announced on either 14 or 15 May.
- Valuations are attractive – JBF is only trading at 5.6x Trailing 12 months P/E, which is around 50-70% cheaper compared to international peers.

Financials & Key Operating Statistics					
YE Dec (US\$ m)	2014	2015	2016	2017	2018
Revenue	218.7	226.5	300.6	295.6	327.1
PATMI	-13.1	2.1	3.8	14.2	26.8
Net Margin (%)	(6.0%)	0.9%	1.3%	4.8%	8.2%
Net Gearing (%)	114%	117%	128%	75%	54%
Price P/B (x)	2.6	2.1	1.9	1.8	1.2
ROE (%)	(21.8%)	3.1%	5.2%	18.0%	21.9%

Source: Company data, KGI Research

Looking forward to 1Q19 earnings. We note from comments by JBF's closest listed peer Guan Chong (GUAN MK), that 2019 "is looking as good as last year" because of increased capacity and sustained margins. This is according to a Bloomberg article about Malaysia's cocoa processing industry posted on 22 April 2019. GUAN has been the best performer on the Bursa Malaysia Consumer Product Index in the past 1 year, with its shares surging 180% during this time. Meanwhile, JBF has only gained 22% over the last 1 year.

Improving profitability. JBF recorded losses in FY13 and FY14 due to high cocoa bean prices and oversupply in the cocoa processing industry. Management executed strategies during the downturn which began to bear fruit when it returned to profitability in FY15, and really began to accelerate from FY17 onwards. 2Q and 3Q FY18 are yet to be JBF's strongest quarters at around US\$9mn PATMI per quarter.

Figure 1: PATMI has accelerated from FY2017



Source: Company data, KGI Research

Not Rated

Price as of 2 May 19 (SGD)	0.68	Performance (Absolute)	
12M TP (\$)	na	1 Month (%)	4.7
Previous TP (\$)	na	3 Month (%)	3.1
Upside (%)	-	12 Month (%)	23.4
Trading data		Perf. vs STI Index (Red)	
Mkt Cap (\$mn)	205		
Issued Shares (mn)	303		
Vol - 3M Daily avg (mn)	0.2		
Val - 3M Daily avg (\$mn)	0.1		
Free Float (%)	17.7%		
Major Shareholders		Previous Recommendations	
JB Cocoa Group	45.5%		
Tee Yih Jia	23.9%		
Ecom Agroindustrial	8.2%		

4Q18 earnings impacted by one-offs. 4Q18 earnings included one-off items such as US\$2.2mn deferred tax expense. Furthermore, there were other seasonal expenses such as accruals for the performance bonus.

On the flipside, there was forex gains of US\$0.8mn due to the weakening of GBP against USD in 4Q18 arising from the group's GBP's borrowings. The group also recognised US\$0.4mn in fair value gains on derivative financial instruments. On a net basis when accounting for the one-off items, net profits would have declined by a smaller 15% YoY to US\$5.5mn.

Top line growth and positive long-term outlook. Demand from customers was particularly strong as revenues in 4Q18 increased by 23% YoY to US\$75mn, which was enough to offset the decline in average selling prices arising from lower cocoa bean prices. Management remains confident on the long-term growth potential on the back of strong cocoa consumption demand.

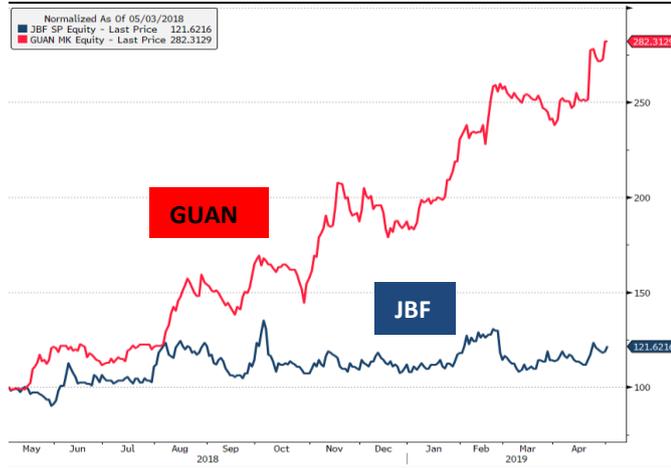
Valuation & Action: JBF is only trading at 5.6x T12M P/E, which we believe undervalues the company when compared to peers who are trading between 10-20x P/E. Demand growth from China and India is expected to provide a positive tailwind to JBF's business as it continues to expand.

1Q19 earnings. JBF is due to report its 1Q19 results on either 14 or 15 May. We think its current share price offers an attractive risk-reward trade over the next 6-12 months, which we expect to be driven mainly by revenue and earnings growth.

Risks: Key risk mainly from oversupply in the cocoa processing market, where it will have a negative impact on prices and margins of JBF.

Share price laggard. JBF has only gained 22% over the past one year compared to GUAN’s 180% surge. Other than JBF’s weak 4Q18, we see no other reason for the significant discrepancy between their share price performances. JBF’s earnings has grown for the fourth consecutive year, and given the strong industry tailwinds based on comments from GUAN’s management, we expect JBF to have another YoY growth in FY2019.

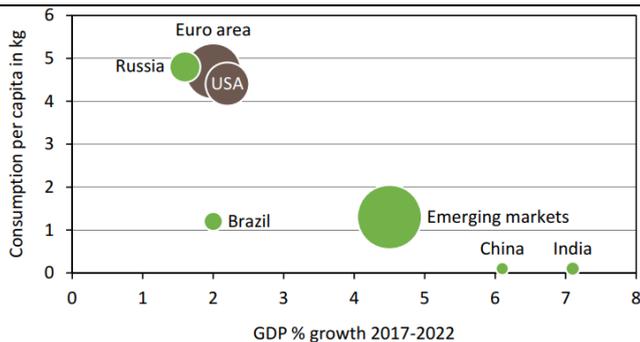
Figure 2: JBF and GUAN share price performances – 1 Year



Source: Bloomberg, KGI Research

Asia Pacific growth market. While growth of the confectionary market in North America and Western Europe has stagnated from 2013-2018, Asia Pacific volume growth has increased 3.2% p.a. on average during the same period. Asia Pacific represents a huge opportunity as it currently only accounts for 14% of the total market compared to 50% for North America and Western Europe.

Figure 3: China and India represent the two largest growth markets for the cocoa industry.

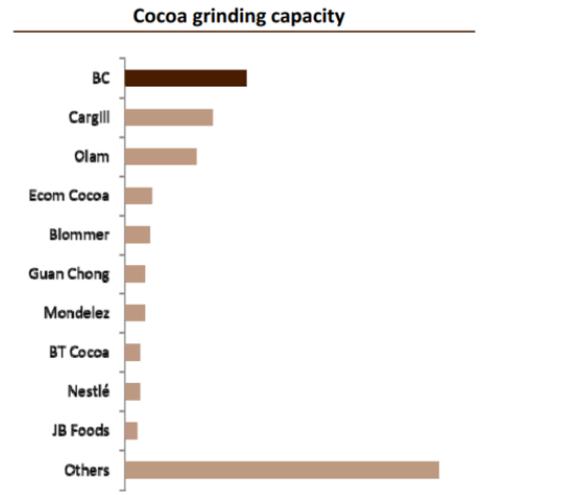


Source: Barry Callebaut

Established customer base. JPF supplies cocoa ingredients to among the most recognisable names in the industry, including Mars, Mondelez and Nestlé.

Competition. JBF’s closest peer is Bursa-listed Guan Chong (GUAN MK), which has the 6th largest cocoa grinding capacity globally. GUAN currently has a production capacity of 250,000mt per year in Johor, Malaysia and Batam, Indonesia. GUAN is currently trading at 10x T12M P/E.

Figure 4: JB Foods has the 10th largest cocoa grinding capacity in the world



Source: Barry Callebaut estimates

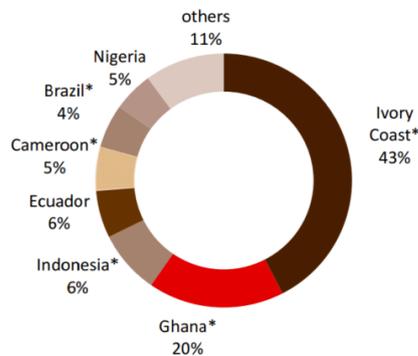
Industry consolidation a potential share price re-rating catalyst. There has been numerous M&A among local cocoa-related companies. Most notable among them was Barry Callebaut’s acquisition of Delfi Ltd’s (DELFI SP, not-rated, fka Petra Foods Limited) cocoa ingredients business for US\$860mn in 2013. Barry Callebaut was itself a result of the merger between Belgium’s Callebaut and France’s Cocoa Barry in 1996.

Key input – cocoa beans. West Africa supplies more than 70% of the world’s cocoa beans to companies like Barry Callebaut and JBF. As such, a key risk to cocoa processing companies is the sustainability of cocoa bean supply over the next few years. However, in the short-term, Bloomberg Intelligence reports that cocoa bean price inflation may accelerate in the later part of 2019 due to bad weather (e.g., El Nino), combined with reduced plantation acreage and decline in investment after 2017’s low prices. We saw a similar surge in cocoa prices in 2015-2016 due to El Nino impact brought dry weather to West Africa and Indonesia.

So, this is an important data point to track going into 2H19 as supply disruption of cocoa beans will impact JBF’s ability to fulfil clients’ requirements.

Figure 5: West Africa supplies 70% of cocoa beans globally

Total world harvest (16/17): 4,748 TMT



Source: Barry Callebaut

Company background. JBF was founded in the 1980s but started processing cocoa in its own facilities in 2003, when it completed its 30,000mt processing plant in Port of Tanjung Pelepas, Malaysia. It subsequently added more processing lines over the years and now produces 145,000mt of cocoa bean equivalent per year in a Malaysian and Indonesian facility. JBF mainly produces cocoa butter, cocoa powder, cocoa mass and cocoa cake. The group listed on SGX in 2012.

Figure 6: JPF’s key products



Source: Company data

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