

CHINA
DEVELOPMENT
FINANCIAL

Japan Foods Holding Ltd

(JFOOD SP/JPFD.SP)

Holding steady despite challenging environment

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- FY2Q20 net profit was flat at S\$0.6mn despite the 8% YoY growth in its revenue. JFOOD now operates 58 restaurants in Singapore, an increase of 5 from the same period last year. However, this was offset by higher expenses related to the new store openings and losses from its overseas associated companies.
- We maintain our **NEUTRAL** recommendation as the outlook in FY20 is expected to remain challenging on the back of heightened competition and underperformance of its overseas associates.
- Given a longer investment horizon, JFOOD remains an attractive investment for its c.5% dividend yield and resilient business model. Its S\$23mn net cash position makes up 31% of its market capitalisation.

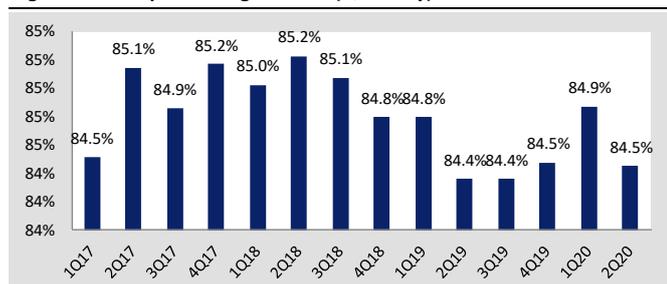
Financials & Key Operating Statistics					
YE Mar SGD mn	2018	2019	2020F	2021F	2022F
Revenue	67.8	68.1	71.8	74.3	76.2
Gross Profit	57.7	57.5	60.5	62.4	64.0
PATMI	5.8	3.3	3.5	4.0	4.1
Core PATMI	5.3	3.2	3.6	4.0	4.1
Core EPS (SG cents)	3.0	1.8	2.1	2.3	2.3
Core EPS grth (%)	175.6	-39.4	13.5	10.7	0.6
Core P/E (x)	12.1	22.6	21.2	18.6	18.4
DPS (SG cents)	2.1	1.9	2.0	2.2	2.3
Div Yield (%)	5.3	4.4	4.7	5.1	5.3
Gross Margin (%)	85.0	84.5	84.2	84.0	84.0
Net Margin (%)	8.5	4.9	4.9	5.4	5.3
ROE (%)	17.9	9.8	10.3	11.6	11.5

Source: Company Data, KGI Research

2Q19 performance. 2Q19 revenue rose 8.3% YoY to S\$18.0mn mainly due to higher contributions from new restaurants operated under "Fruit Paradise", "Afuri Ramen" and "Konjiki Hototogisu" brands. As at end Sep-19, JFOOD operated a total of 58 restaurants, an increase from 53 from end Sep-18. It continued to operate under 15 brands, of which, "Ajisen Ramen" (15 restaurants), "Menya Musashi" (11 restaurants) and "Shitamachi Tendon Akimitsu" (7 restaurants) made up the highest number of restaurants under its portfolio.

The group has proposed a higher interim dividend of 1.0 SG cents, an increase from 0.80 SG cents in 1H FY18. We estimate a 1.10 SG cents final dividend, which would bring full-year dividend to 2.10 SG cents, or an implied 4.7% dividend yield.

Figure 1: Gross profit margins trend (Quarterly)



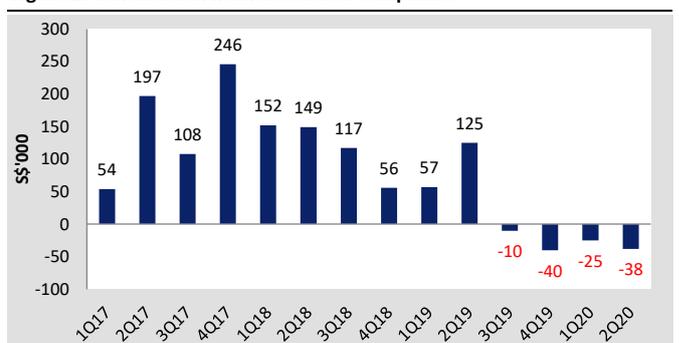
Source: Company data, KGI Research

NEUTRAL - Maintain

Price as of 8 Nov 19 (SGD)	0.43	Performance (Absolute)	
12M TP (\$)	0.46	1 Month (%)	-7.6
Previous TP (\$)	0.55	3 Month (%)	-5.6
Upside, inc div (%)	8.2	12 Month (%)	-
Trading data		Perf. vs STI Index (Red)	
Mkt Cap (\$mn)	74		
Issued Shares (mn)	174		
Vol - 3M Daily avg (mn)	0.0		
Val - 3M Daily avg (\$mn)	0.0		
Free Float (%)	23.9%		
Major Shareholders		Previous Recommendations	
Takahashi Kenichi	70.6%	22-May-19	N \$0.55
Eugene Wong	5.5%	1-Feb-19	N \$0.57
		12-Nov-18	N \$0.56

Overseas associates. JFOOD recognised its fourth consecutive quarter of losses from its associated companies in Hong Kong and China operating under the Menya Musashi brand as a result of intense competition and protests in Hong Kong. On a positive note, JFOOD's joint venture with Minor Food Group (Singapore) may open its first store in Japan in the next 12 months.

Figure 2: Contribution from associated companies



Source: Company data, KGI Research

Valuation & Action: We maintain our NEUTRAL recommendation on JFOOD due to a lack of near-term upside catalysts. Despite the challenging short-term outlook, JFOOD's business model remains resilient and adaptable in the face of higher costs. The group maintains a sizeable cash balance of S\$22mn (29% of its current market capitalisation), supported by strong free cash flows averaging S\$1m per quarter.

Risks: Rising labour costs and rental expenses, lower consumer spending amid slower wage growth.

This report is prepared by KGI Securities (Singapore) under the SGX StockFacts Research Programme. See the last page for important disclosures.

Figure 3: Number of outlets in Japan Food's Singapore network

Restaurants	1Q17	2Q17	3Q17	4Q17	1Q18	2Q18	3Q18	4Q18	1Q19	2Q19	3Q19	4Q19	1Q20	2Q20
Ajisen Ramen + Keika Ramer	18	19	19	19	19	19	18	18	18	17	17	18	16	16
Menya Musashi	8	8	8	7	8	9	10	10	10	11	11	11	11	11
Osaka Ohsho	6	6	6	7	6	6	5	5	5	5	5	5	5	5
Fruit Paradise	4	4	4	4	3	3	3	2	2	1	1	2	2	2
Kazokutei	3	3	3	2	1	1	1	1	1	1	1	1	1	1
Japanese Gourmet Town	1	1	1	1	1	1	1	1	1	1	1	1	1	1
Shitamachi Tendon Akimitsu					0	3	4	6	7	7	7	7	7	7
Others	9	9	9	9	6	6	6	6	7	10	11	10	14	15
Food court outlets														
Ajisen Ramen*	1	1	1	1	1	1	1	1	0	0	0	0	0	0
Total	50	51	51	50	45	49	49	50	51	53	54	55	57	58

Source: Company data, KGI Research

New brand. JFOOD opened its first “House Yamamoto” branded ramen restaurant in October at Raffles City Shopping Centre. This new concept was created by Michelin-starred Chef Atsushi Yamamoto, and specialises in check and seafood soup with black & white truffle and porcini mushrooms. JFOOD will be looking to switch out underperforming restaurants with either the “House Yamamoto” or “Konjiki Hototogisu”.

“Konjiki Hototogisu”, which is rated one-Michelin star, has continued to attract strong interest since opening its first restaurant in CHIJMES in July 2018. JFOOD has since opened another three outlets in Vivocity, Paragon and Changi Jewel.

Figure 4: New brand - 麵 (Men) House Yamamoto



Source: Company data, KGI Research

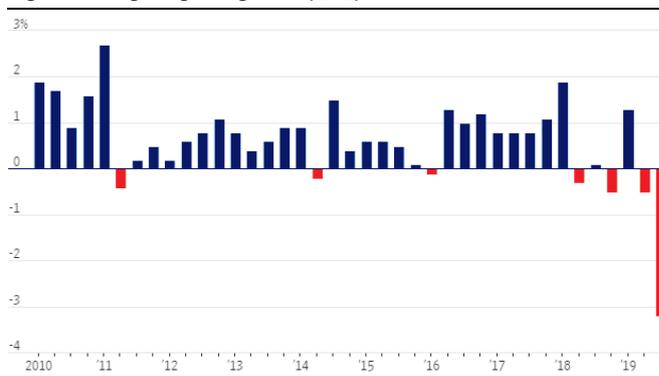
Overseas associates. As at end-Sep 2019, JFOOD’s associated companies operated a total of 18 overseas outlets operated under the “Menya Musashi” brand, and one “Ajisen Ramen” restaurant in Malaysia. JFOOD’s associated companies reported a loss of S\$29,000 in 2Q19, compared to profits of S\$125,000 in the prior year period, due to weak performance of its restaurants in Hong Kong. JFOOD would have reported a 12% YoY growth in operating profits if it were to exclude the losses from its associated companies.

Expansion plans still on track in Japan while Hong Kong still subject to ongoing developments. JFOOD updated that its joint venture with Minor Group (Singapore) has identified a few locations for its first restaurant in Japan within the next 12 months. As a recap, JFOOD will oversee, develop and manage the joint venture’s Thai cuisine restaurants in Japan, and is part of the group’s long-time vision to have a presence in the country.

Meanwhile, JFOOD’s 30-70 joint venture with Ajisen (China) Holdings Limited to open its first “Konjiki Hototogisu”

branded restaurant in Hong Kong will be subject to the ongoing developments which has caused the city’s economy to decline by 3.2% QoQ and 2.9% YoY in 3Q19. The 3Q19 GDP figures were the worst QoQ drop since 2009, as retail sales (measured by value) dropped by 23% YoY and tourist arrivals fell almost 40% YoY in August 2019. As a recap, JFOOD’s associated companies operated six “Menya Musashi” brand restaurants in Hong Kong as at end Sep-19.

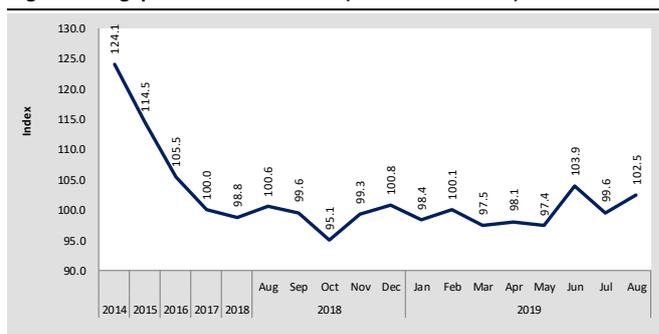
Figure 5: Hong Kong GDP growth (QoQ)



Source: Refinitiv, KGI Research

Industry analysis. Following a weak start to 2019, Singapore’s Restaurants Services index (Figure 6) improved 2.9% YoY (at constant prices) in August 2019, trailing behind the 8.0% YoY improvement of the Fast Food Outlets sector. The reversal in the weakness points to an improved environment for restaurant chains like JFOODS who have been challenged by rising rents and labour costs over the past few years. From our conversation with management, cost pressure from rising rents and labour costs has to some extent eased given the slowing economy.

Figure 6: Singapore Restaurant Index (At Constant Prices)



Source: Department of Statistics, Ministry of Trade & Industry, KGI Research

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