



# Japan Foods Holding Ltd

## (JFOOD SP/JPFD.SP)

### BUY - Maintain

Price as of 9 Feb 2018	0.470
12M target price (S\$)	0.540
Previous target price (S\$)	0.530
Upside (%)	14.9

### Trading data

Mkt Cap (S\$m) / (US\$m)	81 / 61
Issued Shares (m)	173
Ave Daily Traded (3-Month) Vol / Val	0.0m / \$0.0m
52 week lo / hi	\$0.40 / \$0.49
Free Float	23.0%

### Major Shareholders

Kenichi Takahashi	66.4%
Eugene Wong	5.5%
Chau Mui Chan	4.7%

### Previous Recommendations

Date	Rating	Share Price (S\$)	Target Price (S\$)
15-Nov-17	BUY	0.435	0.530
4-Aug-17	BUY	0.430	0.530
26-May-17	BUY	0.480	0.530
17-Apr-17	BUY	0.450	0.560

### JFOOD SP (1yr) VS STI



Source: Bloomberg

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See the last page for important disclosures.

## Stellar results; highest quarterly earnings since IPO

### Event

3Q18 net profit increased 73% YoY to S\$2.5m, driven mainly by two brands – “Menya Musashi” and “Shitamachi Tendon Akitmitsu”, which added S\$1.2m and S\$1.7m, respectively, to the quarter’s topline. Despite increasing cost pressures, Japan Foods managed to maintain gross profit margins at 85.0%-85.1% over the past 3 quarters by lowering raw material costs through bulk purchases.

### Impact

**Constantly reinventing.** As part of the group’s strategy to increase same-store sales at its most established brand, it launched a brand rejuvenation “Den By Ajisen Ramen” at four of its existing “Ajisen Ramen” restaurants. Financial impact has been positive, improving sales for this brand by 6% YoY for 9M18.

**Upcoming stars.** Japan Foods’ newest franchise brand, “Shitamachi Tendon Akimitsu”, is growing fast and may provide upside earnings surprise in FY18. It now has a total of 5 restaurants under this brand as of 7-Feb, an encouraging growth trend considering it opened its first restaurant just six months ago. The restaurant offers specialty tendon rice set that could complement menu offerings from other restaurant brands under Japan Foods.

**Overseas expansion above expectations.** Contribution from its existing China associates accounted for 14% of the quarter’s net profit growth. Japan Food currently has 8 restaurants in HK and 10 in China under its associates and JV. Discussions with a potential Indonesian JV may help it gain a foot in ASEAN’s largest economy, which we expect to drive further earnings growth momentum.

### Valuation & Action

We maintain our BUY recommendation with a fair value of S\$0.540 (DCF valuation). Japan Foods’ business model remains resilient and adaptable even in the face of higher costs. We see several upside catalysts in FY19 driven by organic growth amid an improving macro environment and through joint ventures with overseas partners. The group maintains a sizeable cash balance of S\$20.5m, supported by strong free cash flows averaging S\$1m/quarter.

### Risks

Rising labor costs and rental expenses, lower consumer spending amid slower wage growth; non-renewal of franchise agreements.

### Financials & Key Operating Statistics

YE Mar SGD mn	2016	2017	2018F	2019F	2020F
Revenue	62.8	65.5	68.1	71.5	75.5
Gross Profit	52.9	55.6	57.8	60.6	64.0
PATMI	3.8	4.7	4.5	5.0	5.4
Core PATMI	3.2	4.1	3.9	4.3	4.7
Core EPS (SG cents)	1.8	2.3	2.3	2.5	2.7
Core EPS grth (%)	-24.1	27.2	-2.7	9.9	8.8
Core P/E (x)	18.5	16.3	17.9	16.5	15.3
DPS (SG cents)	2.0	2.0	2.2	2.2	2.3
Div Yield (%)	5.0	4.6	4.7	4.7	4.9
Gross Margin (%)	84.2	84.9	84.8	84.8	84.8
Net Margin (%)	6.0	7.1	6.7	6.9	7.1
ROE (%)	12.3	14.9	14.1	14.7	15.2

Source: Company Data, KGI Research

## Results update – higher sales even with lower total restaurants

**Less is more.** 3Q18 topline grew 11% YoY to S\$18.7m despite having two restaurants less compared to the same period in the previous year. Japan Food had reduced its total number of restaurants to 49 as at end 3Q18 compared to 51 restaurants as at end 3Q17. It closed one restaurant under its “Osaka Musashi” brand, two under “Kazokutei” and one under “Fruit Paradise”. The closures were offset by the additions under “Menya Musashi” and “Shitamachi Tendon Akitmitsu”.

**Four pillars of growth.** The group aims to have four main brands that will serve as key pillars of growth in the future. “Menya Musashi” is showing potential to be the group’s second pillar – 9M18 sales from this brand grew 18% YoY compared to the 6% YoY growth of its most established brand, “Ajisen Ramen”. Another rising star is “Osaka Ohsho”, which grew 9M18 sales by 3% YoY. “Shitamachi Tendon Akimitsu” is still in its early phase but we would be watching whether this could become Japan Foods’ fourth pillar in view of the positive reception since opening its first branch six months ago.

**Figure 1: Number of outlets in Japan Food's Singapore network**

<b>Number of restaurants</b>								
<b>Restaurants</b>		<b>1Q17</b>	<b>2Q17</b>	<b>3Q17</b>	<b>4Q17</b>	<b>1Q18</b>	<b>2Q18</b>	<b>3Q18</b>
Ajisen Ramen + Keika Ramer		18	19	19	19	19	19	18
Menya Musashi		8	8	8	7	8	9	10
Osaka Ohsho		6	6	6	7	6	6	5
Fruit Paradise		4	4	4	4	3	3	3
Kazokutei		3	3	3	2	1	1	1
Japanese Gourmet Town		1	1	1	1	1	1	1
Others		9	9	9	9	6	9	10
<b>Food court outlets</b>								
Ajisen Ramen*		1	1	1	1	1	1	1
<b>Total</b>		<b>50</b>	<b>51</b>	<b>51</b>	<b>50</b>	<b>45</b>	<b>49</b>	<b>49</b>

Source: Company data, KGI Research

## Newest self-developed brand – “Curry is Drink”

**Figure 2: New internally developed brand by Japan Foods**



Source: Company Presentation

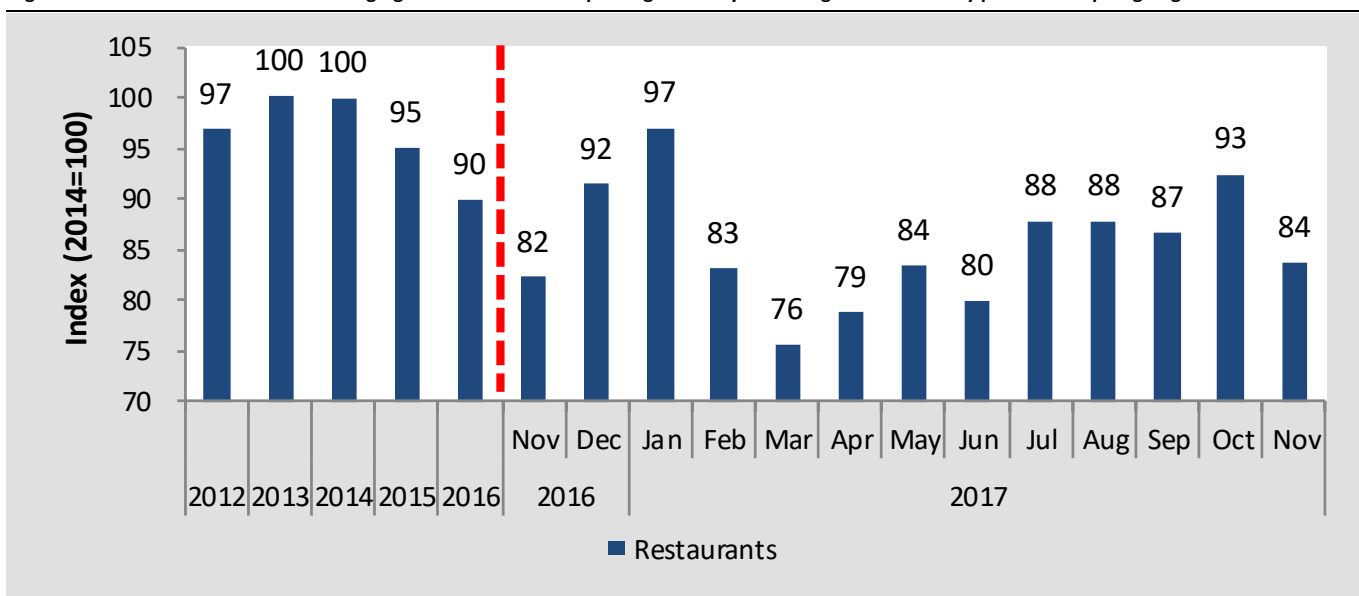
Japan Foods launched its newest self-developed brand “Curry is Drink” at Changi City Point in January 2018. Those who opt for the combo sets get their curries served in a cup – hence the name “Curry is Drink”. The main idea behind the new brand is to promote the idea of curry not only as a sauce. In some parts of Japan such as Hokkaido, curry is served as a soup.

The combo sets cost around S\$13.90++ during lunch and S\$14.90++ for dinner, served with a side of shredded cabbage, crispy fried onions and variety of toppings including raisins. Mains are panko-Crusted deep-fried pork, chicken, prawn or fish. Diners will have a choice between two types of curry, either original Japanese curry or black curry, and from five levels of spiciness.

### F&B industry trends: Challenging 2015-2017 but outlook expected to improve on strong macro tailwinds

**Challenging environment but signs of turning around.** Singapore’s restaurants had a challenging environment from 2015 to 2017 amid lackluster global economic growth during this period. The cautiousness among consumers can be attributed to slowing wage growth and companies holding back on corporate meals at restaurants. On the flipside, there has been increasing sales at foodcourts, cafes and canteens.

Figure 3: Restaurant F&B Index - Challenging environment but improving economy and rising confidence may provide an uplift going forward



Source: Singapore Department of Statistics

**Improving consumer sentiments may increase restaurants revenues.** However, there has been a noticeable improvement in consumer confidence from 2017, which we think may lend support to improving restaurant revenues. According to MasterCard’s consumer confidence index, Singapore experienced a significant improvement in 1H17. Boosted by increasing expectations of economic performance, consumer confidence in Singapore moved from pessimistic into neutral territory, one of the highest improvements in Asia, just after South Korea.

Figure 4: Singapore's consumer confidence may be returning amid robust economic growth

	H1 2017 Current Status		Change from last half	
	Index	Status	Change	Assessment
Asia Pacific	66.9	Optimistic	4.2	Stable +
Korea	78.0	Very Optimistic	46.7	Extreme Improvement
<b>Singapore</b>	45.4	Neutral -	15.4	Significant Improvement
Malaysia	42.3	Neutral -	11.1	Significant Improvement
China	88.2	Very Optimistic	7.4	Some Improvement

Source: MasterCard Index<sup>1</sup>

<sup>1</sup> <https://www1.mastercard.com/content/intelligence/en/research/press-release/2017/bullish-outlook-on-stock-market.html>

YE 31 March

INCOME STATEMENT (SGD mn)	2016A	2017A	2018F	2019F	2020F
<b>Revenue</b>	<b>62.8</b>	<b>65.5</b>	<b>68.1</b>	<b>71.5</b>	<b>75.5</b>
Cost of Sales	(9.9)	(9.9)	(10.4)	(10.9)	(11.5)
<b>Gross Profit</b>	<b>52.9</b>	<b>55.6</b>	<b>57.8</b>	<b>60.6</b>	<b>64.0</b>
Operating Profit	4.1	5.1	4.7	5.2	5.7
Finance Income/(Expenses)	0.0	0.0	0.0	0.0	0.0
Share of JV/Associates' Results	0.6	0.6	0.6	0.6	0.6
<b>Profit Before Tax</b>	<b>4.7</b>	<b>5.7</b>	<b>5.3</b>	<b>5.8</b>	<b>6.3</b>
Income Tax Expenses	(0.9)	(1.0)	(0.8)	(0.9)	(1.0)
<b>PATMI</b>	<b>3.8</b>	<b>4.7</b>	<b>4.5</b>	<b>5.0</b>	<b>5.4</b>
Core PATMI	3.2	4.1	3.9	4.3	4.7
BALANCE SHEET (SGD mn)	2016A	2017A	2018F	2019F	2020F
Cash and Cash Equivalents	16.9	20.2	21.4	23.8	26.9
Trade and Other Receivables	0.9	0.7	0.7	0.8	0.8
Inventory	0.6	0.6	0.7	0.7	0.7
Other Current Assets	2.8	2.3	2.3	2.3	2.3
<b>Total Current Assets</b>	<b>21.2</b>	<b>23.8</b>	<b>25.1</b>	<b>27.5</b>	<b>30.7</b>
Property, Plant and Equipment	11.8	9.9	8.8	7.5	5.8
Other Non-Current Assets	5.9	7.1	7.7	8.3	8.9
<b>Total Non-Current Assets</b>	<b>17.7</b>	<b>17.0</b>	<b>16.5</b>	<b>15.7</b>	<b>14.7</b>
<b>Total Assets</b>	<b>38.9</b>	<b>40.8</b>	<b>41.6</b>	<b>43.2</b>	<b>45.4</b>
Borrowings (Current)	0.0	0.0	0.0	0.0	0.0
Trade and Other Payables	6.2	7.0	6.5	6.8	7.2
Other Current Liabilities	0.9	1.2	1.2	1.2	1.2
<b>Total Current Liabilities</b>	<b>7.1</b>	<b>8.3</b>	<b>7.8</b>	<b>8.1</b>	<b>8.5</b>
Borrowings (Non-current)	0.0	0.0	0.0	0.0	0.0
Other Non-Current Liabilities	0.9	0.9	0.9	0.9	0.9
<b>Total Non-Current Liabilities</b>	<b>0.9</b>	<b>0.9</b>	<b>0.9</b>	<b>0.9</b>	<b>0.9</b>
Shareholders' Equity	30.9	31.6	32.9	34.3	36.0
Total Equity	30.9	31.6	32.9	34.3	36.0
<b>Total Liabilities and Equity</b>	<b>38.9</b>	<b>40.8</b>	<b>41.6</b>	<b>43.2</b>	<b>45.4</b>
CASH FLOW STATEMENT (SGD mn)	2016A	2017A	2018F	2019F	2020F
Net Profit Before Tax	4.7	5.7	5.3	5.8	6.3
Depreciation	5.2	5.1	5.5	5.7	6.0
Other Non-Cash Adjustments	0.5	(0.1)	(0.3)	(0.4)	(0.4)
Changes in Working Capital	(0.5)	1.4	(0.6)	0.3	0.3
Taxes Paid	(0.3)	(0.7)	(0.8)	(0.9)	(1.0)
<b>Cash from Operations</b>	<b>9.6</b>	<b>11.4</b>	<b>9.0</b>	<b>10.6</b>	<b>11.3</b>
Capex	(4.8)	(3.5)	(4.4)	(4.4)	(4.4)
Other CFI	(0.2)	(0.5)	0.0	0.0	0.0
<b>Cash from Investing</b>	<b>(5.0)</b>	<b>(4.0)</b>	<b>(4.4)</b>	<b>(4.4)</b>	<b>(4.4)</b>
Dividends Paid	(3.5)	(3.5)	(3.5)	(3.8)	(3.8)
Borrowings Raised / (Repaid)	0.0	0.0	0.0	0.0	0.0
Equity Raised / (Bought Back)	0.0	0.0	0.0	0.0	0.0
Other CFF	(0.3)	(0.9)	0.0	0.0	0.0
<b>Cash from Financing</b>	<b>(3.8)</b>	<b>(4.3)</b>	<b>(3.5)</b>	<b>(3.8)</b>	<b>(3.8)</b>
<b>Net Increase in Cash and Cash Equiv.</b>	<b>0.9</b>	<b>3.1</b>	<b>1.2</b>	<b>2.4</b>	<b>3.1</b>
Beginning Cash	14.2	15.1	18.1	19.3	21.7
<b>Ending Cash (ex pledged deposits)</b>	<b>15.1</b>	<b>18.1</b>	<b>19.3</b>	<b>21.7</b>	<b>24.8</b>
KEY RATIOS	2016A	2017A	2018F	2019F	2020F
Core EPS (SGD cents)	1.83	2.33	2.26	2.49	2.71
Core EPS Growth (%)	-24.1%	27.2%	-2.7%	9.9%	8.8%
DPS (SGD Cents)	2.00	2.00	2.20	2.20	2.30
Dividend Yield (%)	5.0%	4.6%	4.7%	4.7%	4.9%
<b>Profitability (%)</b>					
Gross Margin	84.2%	84.9%	84.8%	84.8%	84.8%
EBITDA Margin	14.9%	15.7%	15.0%	15.4%	15.6%
Net Margin	6.0%	7.1%	6.7%	6.9%	7.1%
ROIC	25.3%	29.4%	25.0%	29.2%	34.1%
ROE	12.3%	14.9%	14.1%	14.7%	15.2%
ROA	9.8%	11.7%	11.0%	11.7%	12.1%
<b>Leverage (x)</b>					
Total Debt/Equity	0.0	0.0	0.0	0.0	0.0
Net Cash/Equity	0.5	0.6	0.6	0.7	0.7

Source: Bloomberg, KGI Research

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Rating	Definition
	KGI Securities Research's recommendations are based on an Absolute Return rating system.
<b>BUY</b>	>10% total return over the next 12 months
<b>HOLD</b>	-10% to +10% total return over the next 12 months
<b>SELL</b>	<-10% total return over the next 12 months

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