

CHINA
DEVELOPMENT
FINANCIAL

Japan Foods Holding Ltd

(JFOOD SP/JPFD.SP)

Stable business under a challenging environment; interesting JV overseas

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- 3Q19 net profit declined 51% YoY to S\$1.2mn mainly due to lower revenues and losses from its associated companies.
- JFOOD has entered into an interesting JV with Minor Food Group Singapore (MFG). In the JV, JFOOD will bring and operate Thai brands in Japan while MFG will bring and operate JFOOD's brands in Thailand and China.
- We maintain our HOLD recommendation as outlook over the next 3-4 quarters is expected to remain challenging on the back of heightened competition and on slower-than-expected expansion of overseas associates.
- JFOOD's balance sheet remains strong and will be able to tide through the current market weakness. Its S\$22mn net cash position makes up 29% of its market cap, while offering a 4.4% dividend yield.

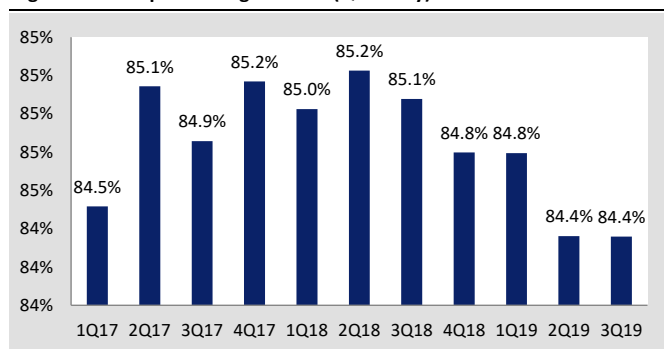
Financials & Key Operating Statistics

YE Mar SGD mn	2017	2018	2019F	2020F	2021F
Revenue	62.8	67.8	68.9	70.9	73.6
Gross Profit	52.9	57.7	58.0	59.6	61.8
PATMI	3.8	5.8	4.6	5.3	5.7
Core PATMI	3.2	5.3	4.0	4.7	5.0
Core EPS (SG cents)	1.8	3.0	2.3	2.7	2.9
Core EPS grth (%)	-24.1	66.5	-24.2	17.3	6.6
Core P/E (x)	18.5	13.1	18.8	16.3	15.3
DPS (SG cents)	2.0	2.1	2.2	2.2	2.3
Div Yield (%)	5.0	4.8	4.4	4.4	4.6
Gross Margin (%)	84.2	85.0	84.2	84.0	84.0
Net Margin (%)	6.0	8.5	6.7	7.5	7.7
ROE (%)	12.3	17.8	13.3	14.8	14.9

Source: Company Data, KGI Research

3Q19 performance weaker-than-expected. 3Q19 earnings declined 51% YoY to S\$1.2mn as revenues fell 6.3% YoY. The weaker performance was also due to losses from its overseas associates. 3Q19 gross margins declined 60bps YoY to 84.4%, contributing further to the weak quarter.

Figure 1: Gross profit margins trend (Quarterly)



Source: Company data, KGI Research

Singapore environment remains challenging. Based on our analysis of peers in Singapore (BreadTalk, ABR, Sakae, Soup Rest., Tung Lok, RE&S, Kimly), all face the same challenge of high rents and limited manpower. Thus, upside from its Singapore market is expected to be limited and we reiterate our view that growth will have to come from overseas expansion.

HOLD - Maintain

Price as of 31 Jan 19 (SGD)	0.44	Performance (Absolute)	
12M TP (\$)	0.57	1 Month (%)	1.1
Previous TP (\$)	0.56	3 Month (%)	-2.7
Upside, inc div (%)	29.5	12 Month (%)	4.3
Trading data		Perf. vs STI Index (Red)	
Mkt Cap (\$mn)	76		
Issued Shares (mn)	174		
Vol - 3M Daily avg (mn)	0.0		
Val - 3M Daily avg (\$mn)	0.0		
Free Float (%)	23.7%		
Major Shareholders		Previous Recommendations	
Takahashi Kenichi	70.6%	12-Nov-18	HOLD \$0.56
Eugene Wong	5.5%	16-Aug-18	BUY \$0.64
		21-May-18	BUY \$0.64

Interesting JV with Minor Food Group Singapore (MFG).

JFOOD has formed a 50-50 JV with MFG to expand overseas. MFG is the restaurant business of Minor International, which is listed on the Thailand Exchange and has an S\$8bn market capitalisation. The JV would allow the two food groups to leverage on each other's strengths – JFOOD would bring MFG's brands such as Thai Express and Xin Wang Hong Kong Cafe to Japan, while MFG will operate JFOOD's non-ramen brands in Thailand and China. The first restaurant is expected in around June/July 2019 but we do not expect any significant contribution in FY19/20. However, we do see this JV as necessary to offset the decline in JFOOD's current overseas associates. JFOOD's number of outlets overseas declined to 21 from 22 in the prior year period.

Brands by

MINOR
FOOD GROUP
SINGAPORE



Valuation & Action: While our DCF-backed fair value of S\$0.56 offers a 22% upside potential, we maintain our HOLD recommendation on JFOOD on the lack of near term upside catalysts and on a weak outlook over the next 3-4 quarters. Despite the challenging short-term outlook, JFOOD's business model remains resilient and adaptable even in the face of higher costs. The group maintains a sizeable cash balance of S\$22mn (29% of market cap), 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.

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Expanding its one-Michelin star brand. “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 store at Great World City in December 2018 and management plans to convert one of its restaurants in Paragon to the third “Konjiki Hototogisu”.

Figure 2: Konjiki Hototogisu-Award winning ramen restaurant at CHIJMES, famed for its chicken and pork broth



Source: Company data, KGI Research

Four pillars of growth. The group aims to have four main brands that will serve as key pillars of growth in the future. As of end-December 2018, the four brands that have 5 or more outlets include “Ajisen Ramen”, “Menya Musashi”, “Shitamachi Tendon Akimitsu” and “Osaka Ohsho”.

“Shitamachi Tendon Akimitsu” has continued to receive positive reception since opening its first branch nine months ago. JFOODs now has seven restaurants under this brand, contributing around S\$4mn to revenues in FY2018.

Overseas associates. As at end-December 2018, JFOOD’s associated companies operated a total of 21 overseas outlets: 7 in HK, 11 in China and 1 in Indonesia, all under the Menya Musashi brand. It has 2 outlets under the Ajisen Ramen in Malaysia and Vietnam.

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

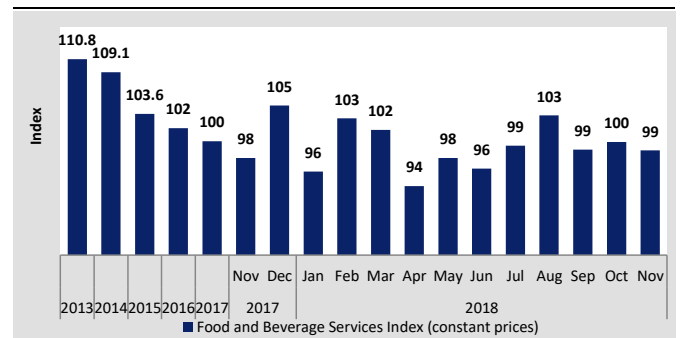
Number of restaurants	1Q17	2Q17	3Q17	4Q17	1Q18	2Q18	3Q18	4Q18	1Q19	2Q19	3Q19
Restaurants											
Ajisen Ramen + Keika Ramen	18	19	19	19	19	19	18	18	18	17	17
Menya Musashi	8	8	8	7	8	9	10	10	10	11	11
Osaka Ohsho	6	6	6	7	6	6	5	5	5	5	5
Fruit Paradise	4	4	4	4	3	3	3	2	2	1	1
Kazokutei	3	3	3	2	1	1	1	1	1	1	1
Japanese Gourmet Town	1	1	1	1	1	1	1	1	1	1	1
Others	9	9	9	9	6	9	10	12	14	17	18
Food court outlets											
Ajisen Ramen*	1	1	1	1	1	1	1	1	0	0	0
Total	50	51	51	50	45	49	49	50	51	53	54

Source: Company data, KGI Research

Industry analysis. A key trend among Singapore F&B companies is the cost pressure from rising rents and the tight labour market. The table below highlights the margins of SGX-listed F&B companies on a quarterly basis. On the consumer side, Singapore’s F&B service index (Figure 5) increased YoY in November but weakened MoM, which may indicate that weakness in the global economy is starting to filter to consumer spending in Singapore.

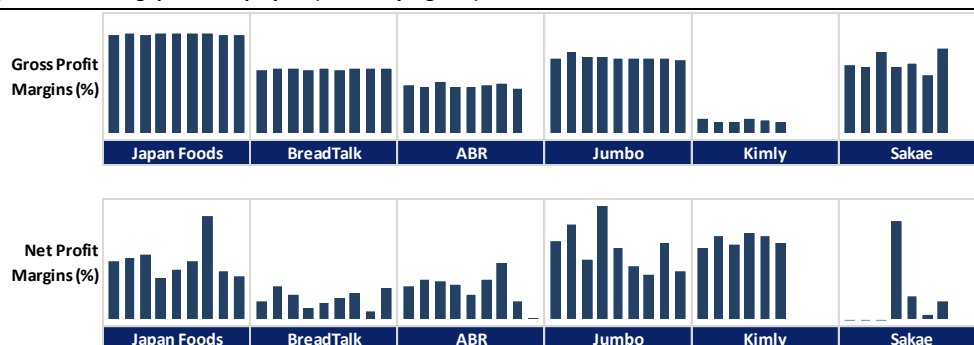
As a result, F&B players have been venturing overseas for growth e.g., BreadTalk in China and UK, Jumbo in China, and JFOOD in China and Indonesia, and now in Japan.

Figure 5: Singapore F&B Services Index (At Constant Prices)



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

Figure 4: Profit margin trends of Singapore F&B players (Quarterly Figures)



Source: Bloomberg, KGI Research

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

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