



# Japan Foods Holding Ltd

## (JFOOD SP/JPFD.SP)

### BUY - Maintain

Price as of 17 May 2018	0.485
12M target price (S\$)	0.640
Previous target price (S\$)	0.540
Upside (%)	32.0

### Trading data

Mkt Cap (S\$m) / (US\$m)	84 / 63
Issued Shares (m)	174
Ave Daily Traded (3-Month) Vol / Val	0.0m / \$0.0m
52 week lo / hi	\$0.40 / \$0.52
Free Float	23.3%

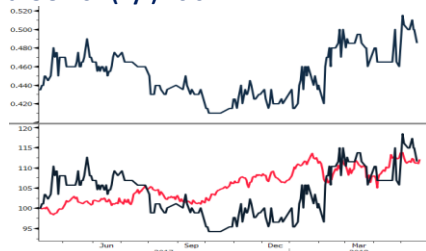
### Major Shareholders

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

### Previous Recommendations

Date	Rating	Share Price (S\$)	Target Price (S\$)
12-Feb-18	BUY	0.470	0.540
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.

## Scaling new heights; constantly reinventing its restaurants

### Event

**Full-year profits at four-year high.** 4Q18 net income increased 68% YoY to S\$0.9mn, driven mainly by its “Menya Musashi” brand. For the full-year 2018, earnings grew by 24% YoY to S\$5.8mn as it increased its total restaurant count by one, and as gross profit margins had a marginal 10 bps YoY improvement to 85.0%.

**Continuous improvement.** The improvement in gross margins is very impressive amid ever increasing costs in Singapore; management has been able to increase its gross margins from 77.5% in FY2011 to 80.1% in FY2013, then to 83.4% in FY2015 and finally to 85.0% in FY2018. We think that FY2018 may already represent peak margins and to be able to maintain it at 85% going forward would be commendable. Further earnings growth, in our view, may have to be driven mainly by overseas expansion.

**Highest dividend yield among peers.** Management has proposed a 1.30 S Cents final dividend to be paid on 17 Aug. Including the 0.80 S cents interim dividend would yield a full-year dividend yield of 4.1%, the highest among its peers in the F&B sector.

### Impact

**Overseas expansion as key driver.** JFOOD increased its overseas network to 21 in FY2018 - an increase from 18 in the prior year period – mainly from its overseas associates adding 4 new Menya Musashi restaurants in China and 1 in Hong Kong, offset by 2 store closures in Malaysia. 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\$0.640 (DCF valuation). Japan Foods’ business model remains resilient and adaptable even in the face of higher costs. We see several upside catalysts in FY2019, driven by organic growth amid an improving macro environment and through JVs with overseas partners. The group maintains a sizeable cash balance of S\$22mn (26% of market cap), 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	2017	2018	2019F	2020F	2021F
Revenue	62.8	67.8	69.6	71.6	74.4
Gross Profit	52.9	57.7	59.0	60.7	63.1
PATMI	3.8	5.8	5.9	6.3	6.7
Core PATMI	3.2	5.3	5.3	5.7	6.0
Core EPS (SG cents)	1.8	3.0	3.1	3.3	3.5
Core EPS grth (%)	-24.1	66.5	0.5	6.3	6.1
Core P/E (x)	18.5	13.1	14.2	13.4	12.7
DPS (SG cents)	2.0	2.1	2.2	2.2	2.3
Div Yield (%)	5.0	4.8	4.5	4.5	4.7
Gross Margin (%)	84.2	85.0	84.8	84.8	84.8
Net Margin (%)	6.0	8.5	8.5	8.8	8.9
ROE (%)	12.3	17.8	16.8	16.6	16.3

Source: Company Data, KGI Research

## Results update – Building brands

**Increasing same-store sales.** JFOODs revamped four “Ajisen Ramen” restaurants into “Den by Ajisen Ramen” in FY2018 at the following locations: (1) Tampines Mall, (2) Plaza Singapura, (3) Novena Square 2, and (4) Hougang Mall. As a result, FY2018 same-store sales at these four restaurants increased by 14% YoY. So even as its total Ajisen Ramen outlets decreased to 18 as at 31 March 2018 from 19 in the prior year period, total revenues from its flagship brand increased by 3.5% YoY to S\$26.8mn in FY2018.

**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 – FY2018 sales from this brand grew 20% YoY compared to the 4% YoY growth of its most established brand, “Ajisen Ramen”. Another rising star is “Osaka Ohsho” which had flat revenue growth as it closed 2 stores in FY2018 (1 in Eastpoint Mall), but which we think may be temporary as management decides on other more suitable locations.

“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. JFOODs now has six restaurants under this brand, contributing around S\$4mn to revenues in FY2018.

**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>	<b>4Q18</b>
Ajisen Ramen + Keika Ramer	18	19	19	19	19	19	18	18
Menya Musashi	8	8	8	7	8	9	10	10
Osaka Ohsho	6	6	6	7	6	6	5	5
Fruit Paradise	4	4	4	4	3	3	3	2
Kazokutei	3	3	3	2	1	1	1	1
Japanese Gourmet Town	1	1	1	1	1	1	1	1
Others	9	9	9	9	6	9	10	12
<b>Food court outlets</b>								
Ajisen Ramen*	1	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>	<b>50</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

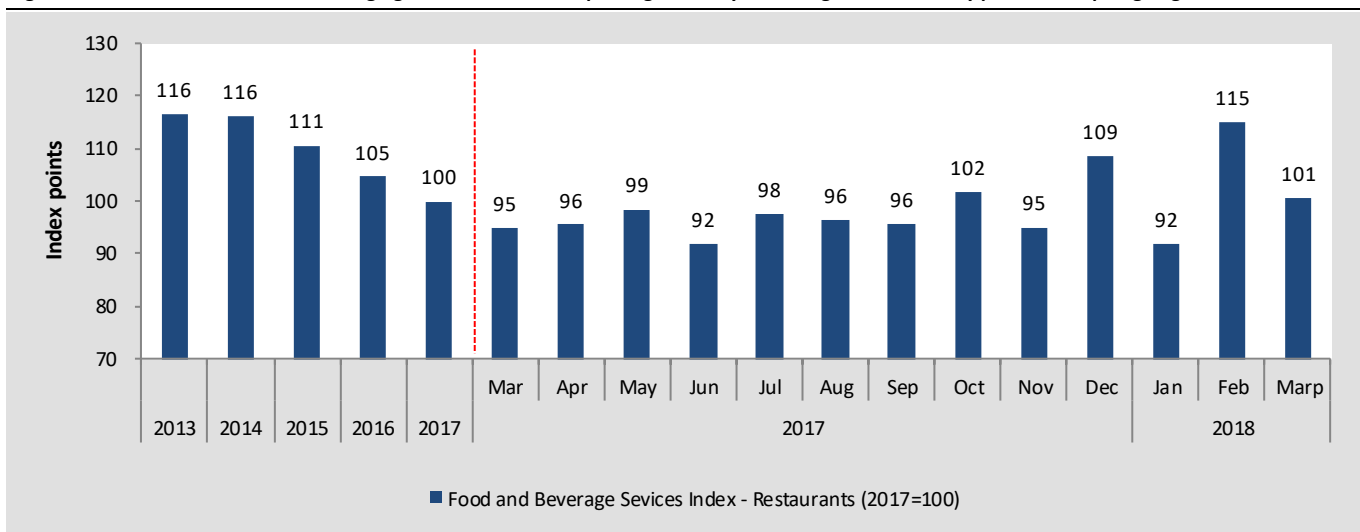
Japan Foods launched its newest self-developed brand “Curry is Drink” at Changi City Point in January 2018. Those who opt for the combo sets get their curries served in a cup – hence the name “Curry is Drink”. The main idea behind the new brand is to promote the idea of curry not only as a sauce. In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

**Industry turnaround.** 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. However, there has been a visible return of consumer sentiment based on the latest Food and Beverage Service Services Index for Restaurants, which after staying below 100 pts during 1H 2017, has improved to an average of 102 pts in 1Q 2018.

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, KGI Research

The Food & Beverage Service Index measures the short-term performance of the food & beverage (F&B) services industries based on the sales records of F&B services establishments.

**Improving consumer sentiments.** 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	Improvement
Asia Pacific	66.9	Optimistic	4.2	Stable +
Korea	78.0	Very Optimistic	46.7	Extreme Improvement
Singapore	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)	2017A	2018A	2019F	2020F	2021F
<b>Revenue</b>	<b>62.8</b>	<b>67.8</b>	<b>69.6</b>	<b>71.6</b>	<b>74.4</b>
Cost of Sales	(9.9)	(10.2)	(10.6)	(10.9)	(11.3)
<b>Gross Profit</b>	<b>52.9</b>	<b>57.7</b>	<b>59.0</b>	<b>60.7</b>	<b>63.1</b>
Operating Profit	4.1	6.5	6.4	6.8	7.2
Finance Income/(Expenses)	0.0	0.0	0.0	0.0	0.0
Share of JV/Associates' Results	0.6	0.5	0.6	0.6	0.6
<b>Profit Before Tax</b>	<b>4.7</b>	<b>7.0</b>	<b>7.0</b>	<b>7.4</b>	<b>7.9</b>
Income Tax Expenses	(0.9)	(1.2)	(1.1)	(1.2)	(1.2)
<b>PATMI</b>	<b>3.8</b>	<b>5.8</b>	<b>5.9</b>	<b>6.3</b>	<b>6.7</b>
Core PATMI	3.2	5.3	5.3	5.7	6.0
BALANCE SHEET (SGD mn)	2017A	2018A	2019F	2020F	2021F
Cash and Cash Equivalents	16.9	21.9	25.0	29.0	33.6
Trade and Other Receivables	0.9	1.0	0.8	0.8	0.8
Inventory	0.6	0.7	0.7	0.7	0.7
Other Current Assets	2.8	2.1	2.1	2.1	2.1
<b>Total Current Assets</b>	<b>21.2</b>	<b>25.6</b>	<b>28.5</b>	<b>32.5</b>	<b>37.2</b>
Property, Plant and Equipment	11.8	9.3	7.7	6.0	4.1
Other Non-Current Assets	5.9	8.4	8.9	9.5	10.1
<b>Total Non-Current Assets</b>	<b>17.7</b>	<b>17.6</b>	<b>16.6</b>	<b>15.5</b>	<b>14.2</b>
<b>Total Assets</b>	<b>38.9</b>	<b>43.3</b>	<b>45.1</b>	<b>48.0</b>	<b>51.3</b>
Borrowings (Current)	0.0	0.0	0.0	0.0	0.0
Trade and Other Payables	6.2	7.3	6.7	6.9	7.1
Other Current Liabilities	0.9	1.5	1.5	1.5	1.5
<b>Total Current Liabilities</b>	<b>7.1</b>	<b>8.8</b>	<b>8.2</b>	<b>8.4</b>	<b>8.7</b>
Borrowings (Non-current)	0.0	0.0	0.0	0.0	0.0
Other Non-Current Liabilities	0.9	0.4	0.4	0.4	0.4
<b>Total Non-Current Liabilities</b>	<b>0.9</b>	<b>0.4</b>	<b>0.4</b>	<b>0.4</b>	<b>0.4</b>
Shareholders' Equity	30.9	34.0	36.5	39.2	42.2
Total Equity	30.9	34.0	36.5	39.2	42.2
<b>Total Liabilities and Equity</b>	<b>38.9</b>	<b>43.3</b>	<b>45.1</b>	<b>48.0</b>	<b>51.3</b>
CASH FLOW STATEMENT (SGD mn)	2017A	2018A	2019F	2020F	2021F
Net Profit Before Tax	4.7	7.0	7.0	7.4	7.9
Depreciation	5.2	4.3	5.4	5.6	5.8
Other Non-Cash Adjustments	0.5	(0.2)	(0.3)	(0.4)	(0.4)
Changes in Working Capital	(0.5)	(0.7)	(0.4)	0.2	0.2
Taxes Paid	(0.3)	(1.4)	(1.1)	(1.2)	(1.2)
<b>Cash from Operations</b>	<b>9.6</b>	<b>9.0</b>	<b>10.6</b>	<b>11.6</b>	<b>12.3</b>
Capex	(4.8)	(3.9)	(3.9)	(3.9)	(3.9)
Other CFI	(0.2)	(0.1)	0.0	0.0	0.0
<b>Cash from Investing</b>	<b>(5.0)</b>	<b>(4.0)</b>	<b>(3.9)</b>	<b>(3.9)</b>	<b>(3.9)</b>
Dividends Paid	(3.5)	(3.6)	(3.6)	(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)	(0.1)	0.0	0.0	0.0
<b>Cash from Financing</b>	<b>(3.8)</b>	<b>(3.7)</b>	<b>(3.6)</b>	<b>(3.8)</b>	<b>(3.8)</b>
<b>Net Increase in Cash and Cash Equiv.</b>	<b>0.9</b>	<b>1.4</b>	<b>3.1</b>	<b>4.0</b>	<b>4.6</b>
Beginning Cash	14.2	18.4	19.8	22.9	26.9
<b>Ending Cash (ex pledged deposits)</b>	<b>15.1</b>	<b>19.8</b>	<b>22.9</b>	<b>26.9</b>	<b>31.5</b>
KEY RATIOS	2017A	2018A	2019F	2020F	2021F
Core EPS (SGD cents)	1.83	3.05	3.06	3.25	3.45
Core EPS Growth (%)	-24.1%	66.5%	0.5%	6.3%	6.1%
DPS (SGD Cents)	2.00	2.10	2.20	2.20	2.30
Dividend Yield (%)	5.0%	4.8%	4.5%	4.5%	4.7%
<b>Profitability (%)</b>					
Gross Margin	84.2%	85.0%	84.8%	84.8%	84.8%
EBITDA Margin	14.9%	16.0%	17.0%	17.4%	17.6%
Net Margin	6.0%	8.5%	8.5%	8.8%	8.9%
ROIC	25.3%	32.7%	32.7%	36.4%	40.7%
ROE	12.3%	17.8%	16.8%	16.6%	16.3%
ROA	9.8%	14.1%	13.4%	13.5%	13.4%
<b>Leverage (x)</b>					
Total Debt/Equity	0.0	0.0	0.0	0.0	0.0
Net Cash/Equity	0.5	0.6	0.7	0.7	0.8

Source: Bloomberg, KGI Research

**KGI's Ratings**

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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