

Blue Power Group Limited

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Executive Summary

Blue Power Group Limited (BPOW) is located at 4 Victoria Avenue, Kingston CSO. BPOW was listed on the Junior Market of the Jamaica Stock Exchange on April 22, 2010. BPOW's main pursuits are the production and sale of soap (laundry and beauty) and the sale of lumber, hardware supplies and related products. **The soap segment has been the most significant contributor to operating profit since FY 2014. In Q2 2019 \$14.21 million in operating profit was earned from the lumber division versus \$24.94 million from the soap division.**

BPOW has significant exposure to foreign currency moves, through its investment portfolio and cash holdings. In FY 2017 the company generated \$11.07 million in foreign exchange gain aided by 5% devaluation of the J\$ to the US\$ over the period. This inverted in FY 2018 when it lost \$10.25 million in FY 2018 due to foreign exchange loss when the J\$ strengthened 3.15% versus the US\$. Also of note BPOW in FY 2018 BPOW investment assets include a US\$1.20 million corporate bond of NCB 7% that matures in 2022.

BPOW has seen significant price appreciation over the FY 2014 to FY 2018 period. However, the earnings for the company has been relatively flat over the period. Therefore the rally in the stock price has been stoked by P/E multiple expansion. In calendar 2015 the stock market began to experience material multiple expansion which aided the majority of stocks to post material gains in 2015. At the end of FY 2014 and 2018 BPOW traded at a P/E ratio of 5.47x and 20.36x respectively

Despite lacklustre growth over the last 5-years, we see indications of improved growth ahead, already being reflected in the first half of FY 2019 primarily at the Soap Division. A key driver of growth going forward is the growth in the foreign exports. In the first half of FY 2019, 24% of Soap Division sale was to exports in the Caribbean, USA and UK.



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Company Summary

The company is located at 4 Victoria Avenue, Kingston CSO. The listing of BPOW on the Junior Market of the Jamaica Stock Exchange occurred on April 22, 2010. BPOW's principal activities are the manufacture and sale of soap (laundry and beauty) and lumber, hardware supplies and related products. The company completed a 10 for 1 stock split (all per share data has been adjusted to reflect this) in August 2018 increase its shares outstanding to 564.99 million.

Key Financial Data

	2014	2015	2016	2017	2018	CAGR
<i>BVPS</i>	0.76	0.87	0.99	1.19	1.35	15.41%
<i>EPS</i>	0.16	0.12	0.13	0.22	0.18	2.37%
<i>Dividend Per Share</i>	0.015	0.015	0.015	0.017	0.019	6.09%
<i>Payout Ratio</i>	9.10%	12.11%	11.14%	7.88%	10.50%	
<i>Revenue (\$B)</i>	1,046	1.06	1.22	1.40	1.51	9.57%
<i>Gross Profit</i>	218.30	221.27	253.11	327.28	323.13	10.30%
<i>Operating Profit</i>	85.54	66.74	74.91	118.59	115.86	7.88%
<i>Net Finance Income</i>	7.56	3.87	10.56	20.92	0.07	-69.41%
<i>Profit</i>	93.10	69.96	76.07	121.82	102.24	2.37%
<i>PP&E</i>	50.18	72.32	63.55	114.03	159.412	33.50%
<i>Investments</i>					148.50	
<i>Cash and Equivalents</i>	136.28	166.01	258.64	276.29	188.08	8.39%
<i>Assets</i>	500.48	565.64	641.23	757.00	904.36	15.94%
<i>Due to Related Party</i>	0.19	0.35	0.35	0.33	28.98	252.60%
<i>Long-Term Loan</i>		7.25	5.27			
<i>Equity</i>	81.85	88.39	103.12	115.99	130.04	12.27%
<i>Ratios</i>						
<i>Gross Margin</i>	20.87%	20.87%	20.82%	23.45%	21.43%	
<i>Operating Margin</i>	8.18%	6.29%	6.16%	8.50%	7.69%	
<i>Net Profit Margin</i>	8.90%	6.60%	6.26%	8.73%	6.78%	
<i>Current Ratio</i>	6.38	7.42	7.50	7.67	4.24	
<i>Acid-Test Ratio</i>	3.04	3.63	4.65	4.77	2.18	
<i>Debt-to-Equity</i>	0.000	0.015	0.010	0.000	0.038	
<i>ROE</i>	21.65%	15.19%	14.48%	19.80%	14.26%	
<i>ROA</i>	18.60%	13.12%	12.61%	17.42%	12.31%	
<i>P/E</i>	5.47	6.07	8.91	17.23	20.36	
<i>P/B</i>	1.18	0.86	1.21	3.13	2.73	

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Financial Overview

Revenue has increased at a CAGR of 9.57% for the period FY 2014 to FY 2018 (period under review). The growth at BPOW's lumber division lead, improving at a CAGR of 10.03% versus the 8.50% experienced at the Soap Division. For FY 2018 \$1.07 billion or 70.79% of revenue was generated the lumber division. For the period under review, operating profit grew at a CAGR of 7.88%, again the drag on growth has been the soap division. Operating profit grew at a CAGR of 9.67% and 6.11% at the Lumber Division and Soap Division respectively. Finance income faced a steep decline in FY 2018 due to 3% strengthening of the J\$ versus the US\$ over the period. This resulted in the Soap Division facing a net financing cost of 3.84 million. While some of this was negated by a \$3.91 million net finance income from the lumber division. Profits for the period under review only increased by 2.37% with growth at the lumber division again the main contributor. However, more recent data for Q1 and Q2 FY 2019 reveal much-improved revenue and earnings growth at BPOW's soap division. BPOW's Soap division reported \$60.87 million in pre-tax profits outpacing all of FY 2018 pre-tax earnings. This growth was aided by 8% devaluation of the J\$ versus the US\$ for Q1 FY 2019, which resulted in net finance gain at the Soap Division of \$12.96 million.

As at the end of FY 2018 the most significant contributors to PP&E were land and building and plant and machinery which were \$63.65 million and \$59.94 million respectively. Cash and equivalents has steadily increased at a CAGR of 8.39% for the period under review. **In the last quarter of FY 2018 BPOW purchased US\$ 1.20 million of NCB 7% fixed rate corporate bond which matures in 2022 which is included in Investment Assets.** During the FY 2018 a subsidiary of BPOW, Cotrade Limited, agreed with Alacrity Limited, for the purchase of property at 4 and 6 Victoria Avenue, Kingston 2. The amount due to related parties, a balance of \$28.98 million represents the consideration due net of a cash payment and off-set of balances owed to the company by affiliated companies of Alacrity Limited. Of note, as at the end of Q2 for FY 2019 the amount due to related parties has been significantly reduced to 50 thousand. Shareholder equity has increased at a CAGR of 15.41% primarily due to BPOW's consistent profitability over the period under review.

Net profit has been consistently higher at the Soap Division, exceeding the Lumber division by as much as 11.31% in FY 2017. In FY 2018 the Soap Division reported a net profit margin of 12.24% versus 5.81% at the Lumber Division. BPOW has maintained relatively good liquidity and solvency ratios. Current and acid-test ratios were at a low of 4.24x and 2.18x respectively for the period under review. Meanwhile, debt-to-equity peaked at 0.04x, which occurred at the end of FY 2018. However, as at Q2 FY 2019, this ratio has decreased to virtually zero. Applying Dupont analysis, we see that the critical driver, the ROE, has been asset turnover which has averaged 1.98x over the period FY 2014 to FY 2018.

BPOW has experienced a material P/E multiple expansion moving from 2.99x to 20.36x for FY 2013 and FY 2018 respectively. The company's stock price has increased at a CAGR of 42.21% despite profits only producing CAGR of 2.37% over the same period.

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Forecast and Valuation

We used the relative value method applied to the 1-year mean P/E and P/B ratios to arrive at a price target of \$5.53 per share using FY 2020 forecasted EPS and BVPS. Innate in our base case assumption is that market sentiment remains at recent levels, leading to BPOW maintaining average P/E and P/B multiple ratios over the past year. Given the strength in earnings in the first half of FY 2019 aided by export sales growth primarily at the Soap Division, we view current sentiment maintaining or improving as highly probable. BPOW's peers P/E average is 22.20x, which is marginally above BPOW's current P/E. Also, while BPOW's dividend yield is immaterial, it exceeds the mean of peers while ROE and ROA surpass peers. **We also evaluated BPOW using the dividend discount model (DDM) which produced a price target of \$5.41 roughly in line with our base case assumption.**

<u>Ticker</u>	<u>Market Cap (\$M)</u>	<u>P/E</u>	<u>P/B</u>	<u>Div Yield</u>	<u>ROA</u>	<u>ROE</u>
AMG	998.19	27.86	2.19	0.00%	-3.25%	-4.97%
BPOW	2,819.30	21.14	3.47	0.34%	14.97%	17.11%
CFF	1,708.48	19.59	4.09	0.00%	21.06%	23.31%
HONBUN	1,790.81	21.04	2.90	1.05%	11.58%	14.85%
JAMT	3,088.05	16.00	2.47	0.00%	11.37%	16.17%
KREMI	2,214.62	19.72	3.16	1.04%	12.61%	16.99%
LASM	15,750.98	28.08	3.20	0.00%	7.58%	11.97%
PTL	4,010.41	68.42	5.42	0.00%	5.21%	8.25%
PURITY	389.74		0.54	0.00%	-4.85%	-6.35%
Average ¹		22.20	3.13	0.27%	12.05%	15.52%

Recent Developments

BPOW has executed a 10 for 1 stock split which took effect August 28, 2018. The stock has since posted a marginal gain of 6.17% to close at \$4.99². BPOW reported improved profits for its 2nd quarter ended October 31, 2018. For the period revenue increased by \$45.21 million or 11.88% to \$425.86 million while profits rose \$9.06 million or 51.66% to \$26.58 million. For the quarter, profits at the lumber division fell 13.81% to \$7.99 million while profits at the soap division surged 125.09% to \$18.60 million.

¹ P/E average excludes PTL due to it being excessively high, ROE and ROA calculations exclude negative figures

² As at January 8, 2018

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Outlook

We maintain a positive outlook on BPOW at current levels given improving export sales. Also, given BPOW's non-existent debt and high cash and investment holdings it could easily improve dividend payout ratio or expand via acquisitions. While the exposure to US\$ provided a hindrance in FY 2018, we don't see that as the norm, and therefore net finance income is likely to move higher medium to long-term. However, the markets in which BPOW operates do not have high barriers to entry and are already highly competitive, and therefore the rate of growth of profits could be curtailed in the medium to long-term from current levels.

Key Risks to Our Price Target

The movement of the J\$ versus the US\$ has a material impact on BPOW's earnings in any given year. Therefore an unfavourable material change could impact our projections. Additionally, our earnings forecast expect the improved trends experienced in particular at the Soap Division to continue. Therefore if, weakness in key export markets such as Guyana and Barbados materialise this could also impact our projections.

Recommendation:

We recommend a **MARKETWEIGHT** on BPOW at this point given that the stock currently trades at \$4.99 a 10.87% discount to our **base case price target of \$5.53**. **Our best case scenario for the price target which uses an average of P/E and P/B multiple of 2 standard deviations above the last 1- year average applied to FY 2020 EPS and BVPS produces a price target of \$7.71**. Therefore the stock does have 54.42% upside to the top end of our forecast. **However, due to the relatively illiquid nature of BPOW's stock with the average daily volume over the past year being 7,101 units we recommend purchasing any significant amount of this stock at \$4.45 an equal weighting of our bear case and base price target of \$3.36 and \$5.53 respectively.**

Source: <http://www.Jamstockex.com>, JMMB Investment & Research, Bloomberg, Various Company Financial Statements.

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APPENDIX

IMPORTANT DISCLOSURES

ABSTRACT—As a part of our new Portfolio Strategy we are recommending strict adherence to the following Portfolio Allocation **DEFINITIONS/RECOMMENDATIONS**.

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UNDERWEIGHT—REDUCE EXPOSURE IN YOUR PORTFOLIO TO LESS THAN 5% FOR THIS PARTICULAR ASSET

SELL—REDUCE EXPOSURE IN YOUR PORTFOLIO TO ZERO.

HOLD/MARKETWEIGHT—EXPOSURE TO THE ASSET SHOULD BE EQUAL TO 5% OF YOUR TOTAL PORTFOLIO HELD AT JMMB.

OVERWEIGHT/BUY—EXPOSURE TO THIS ASSET SHOULD BE BETWEEN 5% AND 10% OF YOUR TOTAL PORTFOLIO HELD AT JMMB

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