

## Honey Bun (1982) Limited

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### Executive Summary

Honey Bun (1982) Limited (HONBUN) is a limited liability company incorporated under the laws of Jamaica, and has its registered office at 26 Retirement Crescent, Kingston 5. The Company was established in 1982 by Herbert Chong and Michelle Chong and listed on the JSE's Junior Market on June 3, 2011. Its primary activities are the manufacture and distribution of baked products for local and export markets. HONBUN became Jamaica's first Internationally Food Safety Certified (Hazards Analysis Critical Control Point - HACCP) bakery in March 2016 and subsequently completed a 5 for 1 stock split on June 1, 2016.

HONBUN has increased revenue at a CAGR of 8.9% between FY 2016 to FY 2020 (period under review) to \$1.7 billion. Meanwhile, profits have grown at a CAGR of 3.6% for the same period. The revenue and profit growth rate accelerated, for the 6 months ended March 31, 2021, up 12.9% and 20.7%, respectively.

Operating cash flow has increased at a CAGR of 5.4% for the period under review to a record of \$225.8 million. This trend has continued with operating cash flow increasing 81.4% in the 6M period ended March 2021 to \$168.2 million.

Meanwhile, debt-to-equity has been stable, averaging 0.04x for the period under review; its highest level was 0.07x at the end of FY 2017. As at March 31, 2021 HONBUN has debt of only \$19.7 million, resulting in a debt-to-equity ratio of 0.02x, indicating long-term liabilities can be readily met.

HONBUN's stock price has declined at a compounded annual rate of 4.7% for the period under review, marginally underperforming the Junior market's advance of 1.7% over the same period. HONBUN has been a reasonably liquid Junior Market stock over the last year, trading an average daily volume (ADV) of 56.5 thousand units, valued at approximately \$311 thousand.



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### Recent Developments

In Q2 ended March 2021, revenue increased 16.3% to a record \$527.4 million, aiding profit growth of 77.4% to \$76.8 million. The increase in revenue was assisted by introducing new products, including hot dog rolls and cinnamon loaf. Meanwhile, the improved profitability was aided by selling and distribution expense declining by 5.8% to \$59.2 million despite the higher revenue. Furthermore, the Company experienced lower finance expense and reduced loss on investments classified as FVPL.

However, for the 6M period, profits only increased by 20.7% due to a 29.3% decline in Q1 earnings to \$34.8 million. The decrease was primarily due to a 20.7% surge in administrative expense to \$107.3 million.

### Abridged Financials

	FY 2016	FY 2017	FY 2018	FY 2019	FY 2020	CAGR	6M 2020	6M 2021	Change(%)
Share Price	5.79	4.30	3.95	6.57	4.78	-4.70%	6.18	5.09	-17.64%
BVPS	1.00	1.16	1.31	1.57	1.85	16.55%	1.72	1.99	15.98%
EPS	0.31	0.20	0.18	0.33	0.35	3.61%	0.20	0.24	20.73%
Dividend Per Share	0.05	0.04	0.04	0.06	0.08	12.47%	0.05	0.09	79.99%
JSE Junior Market Index	2,390	2,907	3,395	3,533	2,556	1.69%	2,304	2,983	29.46%
<b>In Millions</b>									
Revenue	1,190.21	1,251.12	1,317.18	1,543.98	1,674.78	8.91%	875.98	988.72	12.87%
Gross Profit	531.12	544.20	601.29	744.81	799.27	10.76%	425.99	471.78	10.75%
Operating Profit	153.81	109.53	101.26	177.06	182.54	4.37%	118.46	131.10	10.68%
Pre-tax Profit	154.88	105.27	98.10	182.58	191.04	5.39%	107.56	127.76	18.78%
Profits	144.70	93.90	86.42	156.47	166.75	3.61%	92.42	111.58	20.73%
PP&E	343.92	386.95	491.54	510.60	553.45	12.63%	522.03	588.09	12.66%
Non-Current Assets	385.22	466.68	579.08	605.22	622.32	12.74%	591.68	659.15	11.40%
Current Assets	200.42	237.95	209.35	352.72	444.04	22.00%	473.54	506.12	6.88%
Total Assets	585.64	704.63	788.43	957.94	1,066.36	16.16%	1,065.23	1,165.27	9.39%
Non-Current Liabilities	31.94	52.38	49.84	49.35	48.84	11.21%	55.25	46.02	-16.70%
Current Liabilities	82.43	106.42	120.72	168.08	147.95	15.75%	200.60	180.52	-10.01%
Total Liabilities	114.36	158.80	170.56	217.43	196.80	14.53%	255.85	226.54	-11.46%
Debt	15.13	36.13	29.78	23.79	21.13	8.71%	29.70	19.74	-33.53%
Equity	471.27	545.83	617.87	740.51	869.56	16.55%	809.37	938.73	15.98%
Operating Cash Flow	183.22	152.27	174.10	209.22	225.75	5.36%	92.73	168.24	81.42%
Financing Cash Flow	66.15	(3.39)	25.19	35.78	44.60	-9.39%	18.31	45.63	149.25%
Investing Cash Flow	109.07	126.03	151.00	80.23	82.64	-6.70%	9.15	72.18	689.06%

### Financial Overview

Revenue has consistently increased at a CAGR of 8.9% for the period under review. Revenue grew at a similar pace of 8.5% in FY 2020 to a record \$1.7 billion, aided by a 41% increase in exports. Meanwhile, in the 6M period ended March 2021, revenue has increased 12.9% to \$988.7 million, a record for the period.

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Operating profit has increased at a CAGR of 4.4% to \$182.5 million for the period under review. However, the growth rate in operating profit margin trailed revenue growth due to expenses increasing at a CAGR of 12.9% for the same period. Meanwhile, in the 6M period ended March 2021, operating profit increased by 10.7% to \$131.1 million.

Meanwhile, profits for the 6M period surged 20.7% to \$111.6 million despite profits declining 29.3% to \$34.8 million in Q1 FY 2021. However, in Q2, profits surged 77.4% to \$76.8 million, aided by the introduction of new products.

Current assets increased 25.9% in FY 2020 to \$444 million, driven by cash and cash equivalents, which increased 54.1% in FY 2020 to \$297 million. The most significant contributor to cash and cash equivalents is short term deposits of \$197 million. In addition, the Company's cash resources continue to grow, reaching \$347.6 million at the end of Q2 March 2021. At the end of Q2 FY 2021, cash and equivalents represent 29.8% of total assets, while plant property and equipment constitute 50.5% of total assets.

Total liabilities for HONBUN declined by 9.5% to \$196.8 million in FY 2020, due to trade and payables falling 13.8% to \$129.9 million. However, trade and payables remain the most significant contributor of total liabilities accounting for 12.2% of FY 2020 total assets.

HONBUN generates strong operating cash flows reaching a record of \$225.8 million in FY 2020, the highest for the period under review. As a result, investors were rewarded with dividends of \$37.7 million in FY 2020, an improvement of 33.3% over the prior FY. The strength in operating cash flow continued in FY 2021, with HONBUN generating \$168.2 million in cash flow for the first half of the FY. In addition, the Company spent \$118.9 million on acquisitions to PP&E as the Company continues to make capital investments. Meanwhile, for the first half of FY 2021, HONBUN has paid \$42.4 million to shareholders, an 80% increase over the same period last year.

Ratios	FY 2016	FY 2017	FY 2018	FY 2019	FY 2020	Average	6M 2020	6M 2021	Change(%)
Gross Margin	44.62%	43.50%	45.65%	48.24%	47.72%	45.95%	48.63%	47.72%	-1.88%
Operating Margin	12.92%	8.75%	7.69%	11.47%	10.90%	10.35%	13.52%	13.26%	-1.94%
Net Profit Margin	12.16%	7.51%	6.56%	10.13%	9.96%	9.26%	10.55%	11.29%	6.96%
Current Ratio	2.43	2.24	1.73	2.10	3.00	2.30	2.36	2.80	18.77%
Quick Ratio	1.83	1.79	1.39	1.73	2.52	1.85	1.89	2.39	26.32%
Debt-to Equity	0.03	0.07	0.05	0.03	0.02	0.04	0.04	0.02	-42.69%
Debt Ratio	0.03	0.05	0.04	0.02	0.02	0.03	0.03	0.02	-39.24%
ROE	34.50%	18.46%	14.85%	23.04%	20.71%	22.31%	18.38%	21.27%	15.72%
ROA	26.97%	14.56%	11.58%	17.92%	16.47%	17.50%	14.44%	16.67%	15.41%
P/E	18.86	21.58	21.54	19.79	13.50	19.05	20.81	12.90	-37.99%
P/B	5.79	3.71	3.01	4.18	2.59	3.86	3.60	2.56	-28.94%
Dividend Payout Ratio	16.28%	20.07%	21.81%	18.07%	22.61%	19.77%	25.50%	38.01%	49.09%
Dividend Yield	1.53%	0.65%	0.88%	1.27%	1.32%	1.13%	0.73%	1.71%	134.57%
HONBUN Share Performance	576.40%	-25.73%	-8.14%	66.33%	-27.30%	116.31%	56.46%	-22.53%	-139.90%
Junior Market Index Performance	143.79%	21.63%	16.80%	4.07%	-27.67%	31.72%	-34.79%	16.72%	N/A

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HONBUN's current ratio has been relatively high for the period under review, averaging 2.3x and peaking in FY 2020 at 3x. Furthermore, its quick ratio averaged 1.9x and peaked in FY 2020 at 2.5x, indicating short-term liabilities can be easily met. Meanwhile, its debt-to-equity ratio has an average of 0.04x for the period and declined to 0.02x in FY 2020, indicating long-term liabilities can be readily met.

The Company's dividend payout ratio has been relatively stable, averaging 19.8% for the period under review. However, in FY 2021, the dividend payout ratio has increased materially to 38% resulting in a dividend yield of 1.71% for the first half of FY 2021.

### Forecast and Valuation

**We used our projection of HONBUN's FY 2022 EPS and BVPS and then applied the harmonic mean P/E and P/B multiple of peers (adjusted for historical differences) to arrive at our price target of \$7.47. Inherent in our price target is the assumption that investor sentiment towards HONBUN's peer group remains relatively stable. Below is a chart illustrating the relationship between HONBUN's P/B ratio and its peer group average over the last four years. We used the 75th and 25th percentile of P/B and the P/E valuation difference to derive the upper and lower price targets of \$8.45 and \$6.25, respectively.**

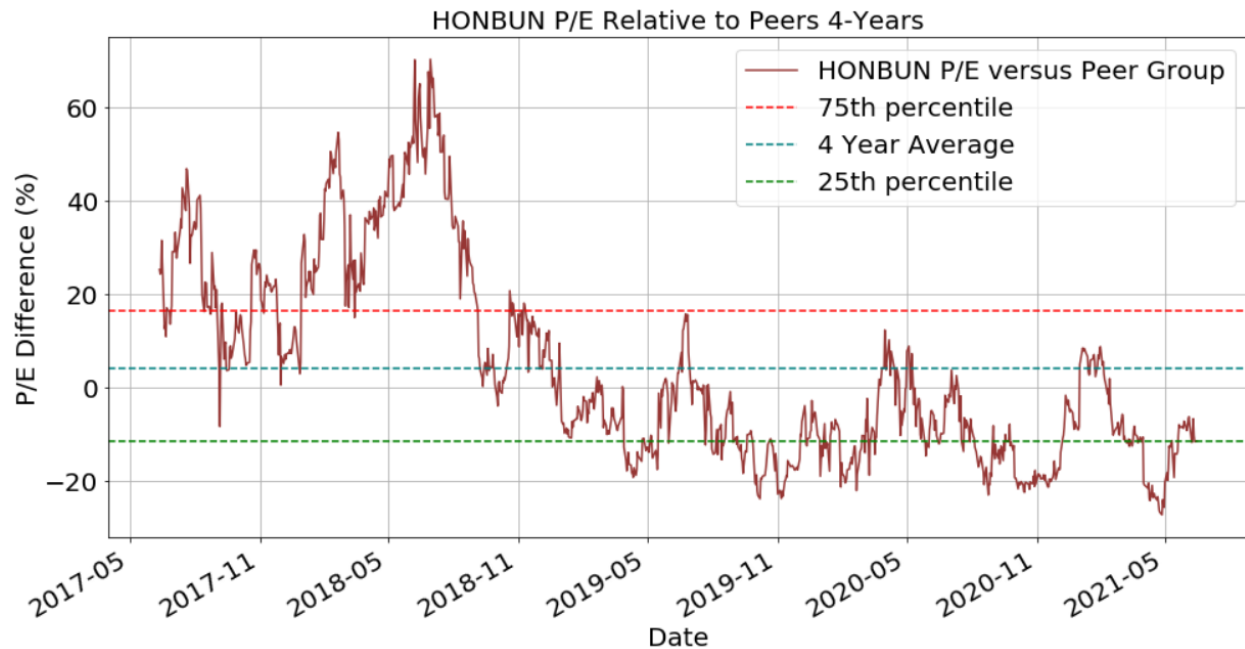
Chart 1 below indicates that HONBUN's P/E is trading close to the lower end of historical levels of an 11.7% discount compared to the peer group average. HONBUN's current P/E relative to peers indicate an opportunity given that over the last four years, HONBUN usually trades at a 4% premium to the peer group average. Additionally, HONBUN's current ROA and ROE are superior to peers, as seen in table 1, and are expected to remain; therefore, a premium to the peer group average on a P/E basis is justified.

Meanwhile, Chart 2 shows a similar pattern with HONBUN's P/B below its 4-year average of a premium of 115.8%. The premium HONBUN has relative to the peer group average is justified given its history of consistently strong performance and current ROA and ROE that exceeds the peer group average.

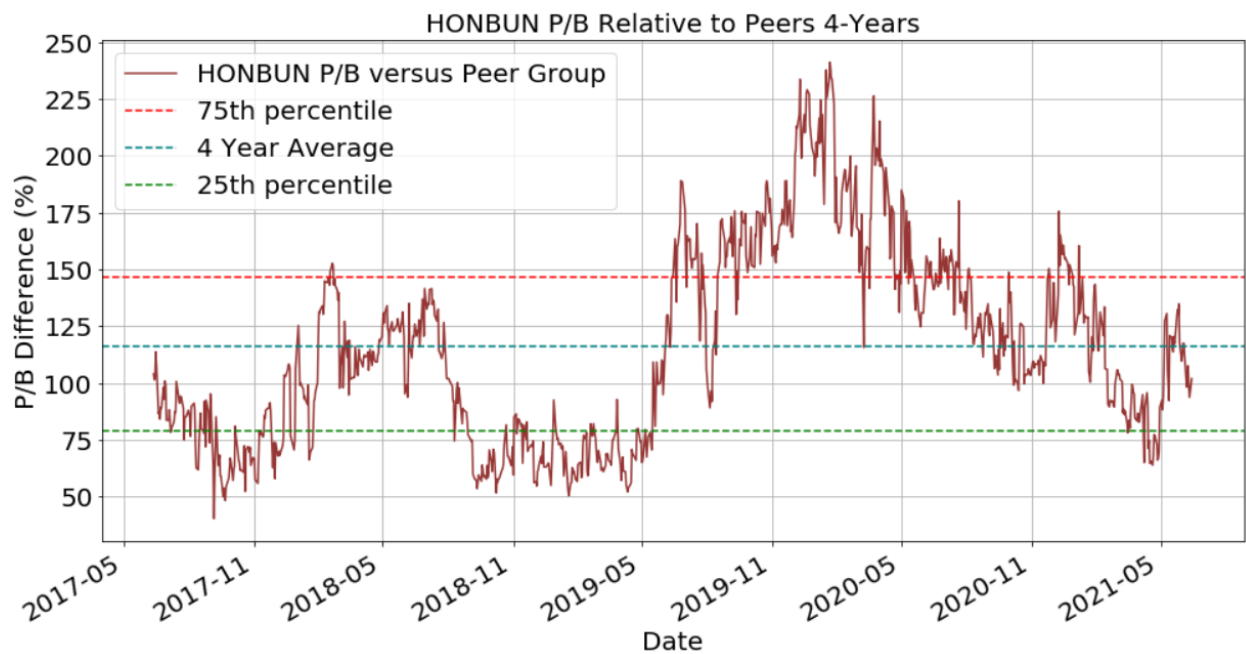
	Price Target	Implied Upside/(Downside)
Upper	8.45	28.48%
Base	7.47	13.45%
Lower	6.25	-4.94%

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**Chart 1.**



**Chart 2.**



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**Table 1.**

Junior Market Food Manufacturing Peers					
Ticker	Market Cap(\$M)	P/E	P/B	ROA	ROE
LASM	22,516.58	16.32	2.85	13.40%	18.82%
CFF	1,888.32	22.21	3.72	13.86%	17.87%
HONBUN	3,100.94	16.68	3.30	16.67%	21.27%
KREMI	2,346.81	23.31	2.81	7.85%	12.76%
PURITY	396.42	-28.55	0.56	-1.33%	-1.96%
Average	6,049.81	19.63	2.65	10.09%	13.75%

### Outlook

We have a positive long-term outlook on HONBUN given its potential to continue to generate growth via the introduction of new products and exports. Furthermore, the Company's substantial cash pile and operating cash flows will aid its ability to execute on opportunities to expand organically and inorganically.

However, our expectations for growth are tempered by rising commodity prices which may impact HONBUN's gross profit margins and may be difficult to transfer to customers. **Additionally, the Company will begin paying taxes at the full applicable rate at the end of June 2021**, which will constrain near-term profit growth.

### Key Risks to Our Price Target

The primary risk to our price target is HONBUN's inability to meet our growth expectations, translating to lower profits and cash flows than expected. In addition, a critical risk is HONBUN's ability to balance the need to raise prices to offset higher input costs against the backdrop of customer's disposable income being constrained by an economic recovery.

### Recommendation:

We recommend a **MARKETWEIGHT** rating on HONBUN at this point, given that the stock trades below our base price target and marginally above our lower price target. **Our rating considers several factors, including the quality of the Company's balance sheet, FCFE and stock liquidity.**

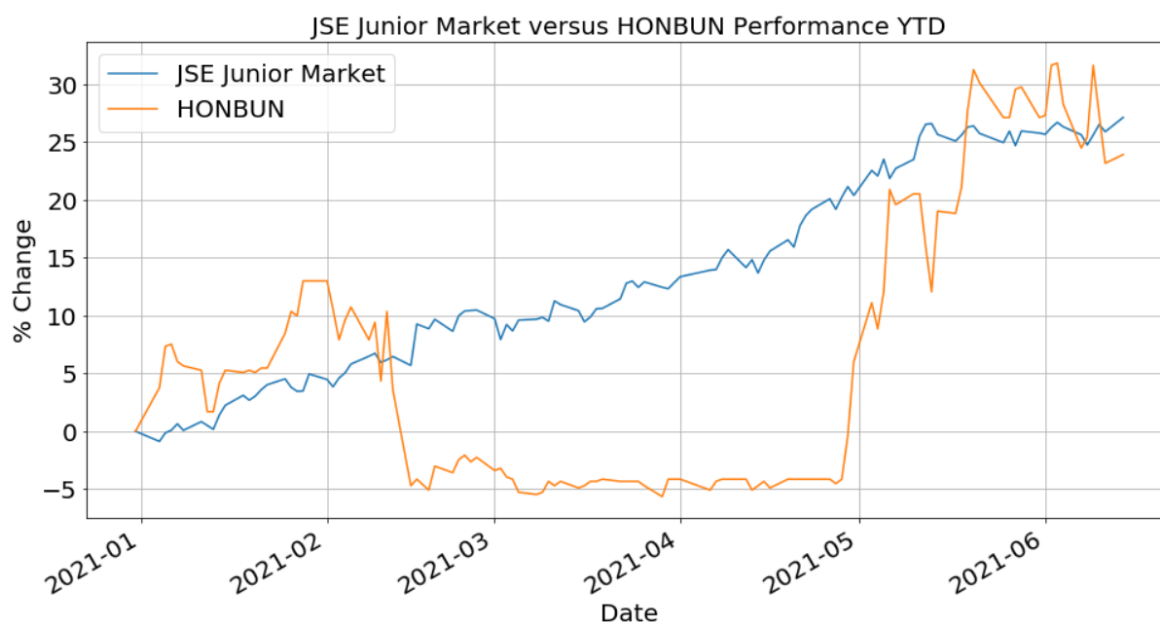
HONBUN has a liquid balance sheet with a current ratio averaging 2.3x for the period under review. In addition, the Company has maintained a debt-to-equity ratio averaging 0.04x for the same period. Furthermore, as of March 2021, it has \$347.6 million in cash & cash equivalents; therefore, we view HONBUN's balance sheet favourably. HONBUN has also produced strong operating cash flow for the period and continues to make PP&E investments to aid revenue expansion via new product offerings. Additionally, HONBUN's stock is a fairly liquid Junior Market listing, trading an average daily value of



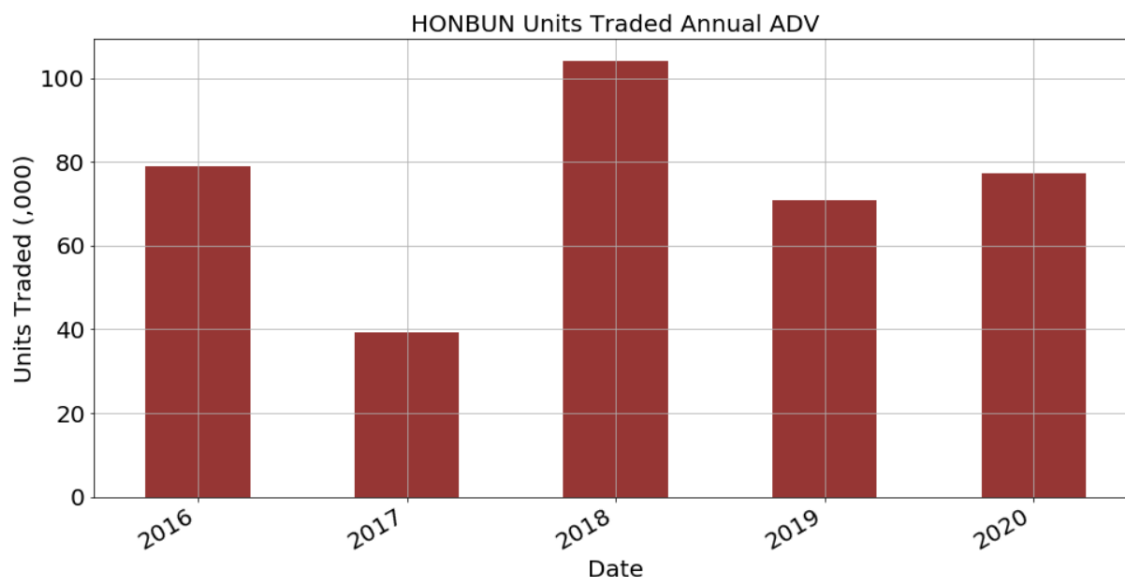
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about \$311 thousand over the last year. See charts 4 – 5 below for volume and value traded annually for the period under review.

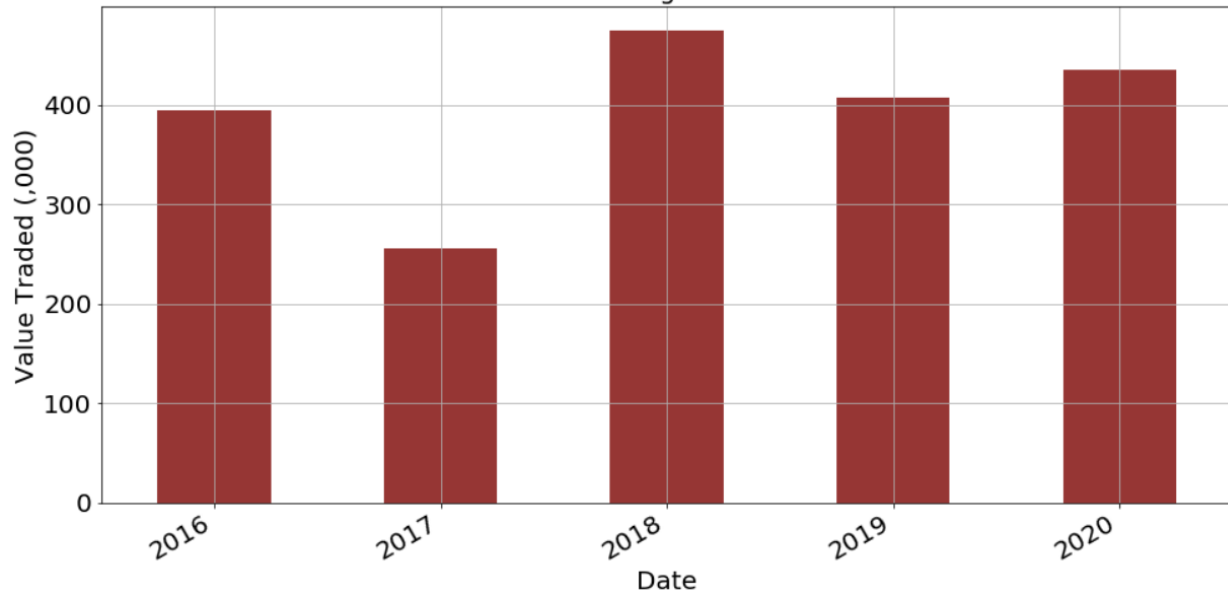
**Chart 3.**



**Chart 4.**



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**Honey Bun (1982) Limited****Chart 5.****HONBUN Average Value Traded**

**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**.

**PLEASE NOTE** THAT NO INDIVIDUAL ASSET IN YOUR PORTFOLIO SHOULD HAVE A WEIGHTING GREATER THAN 5% UNLESS OTHERWISE RECOMMENDED BY YOUR PORTFOLIO MANAGER OR A SPECIFIC JMMB RESEARCH REPORT. CONSEQUENTLY THE FOLLOWING DEFINITIONS ARE PROVIDED FOR CLARITY.

**OUTPERFORM/OVERWEIGHT/BUY**—EXPOSURE TO THIS ASSET SHOULD BE UP TO 10% OF YOUR TOTAL PORTFOLIO HELD AT JMMB

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

**UNDERPERFORM/UNDERWEIGHT**— ADJUST EXPOSURE IN YOUR PORTFOLIO HELD AT JMMB TO BETWEEN 2.5% AND 4.9% FOR THIS PARTICULAR ASSET

**STRONGLY UNDERPERFORM/UNDERWEIGHT**—REDUCE EXPOSURE TO THIS ASSET TO BELOW 2.5% OF YOUR TOTAL PORTFOLIO HELD AT JMMB

**SELL**—REDUCE EXPOSURE IN YOUR PORTFOLIO TO ZERO (0%).

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