

**Berger Paints Limited (BRG)**



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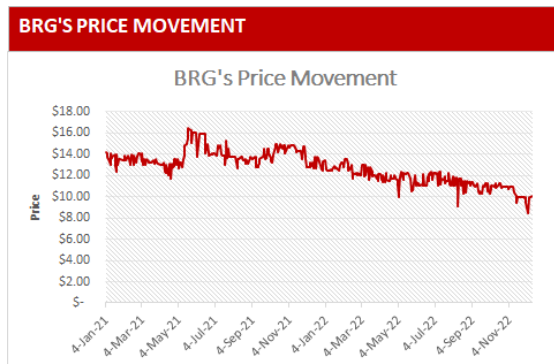
**EXECUTIVE SUMMARY**

**Berger Paints Limited (BRG)**, was incorporated in 1953 and its shares listed on the Jamaica Stock Exchange in 1992. In 2017, BRG became a subsidiary of the Ansa Mcal Group, as they purchased Lewis Berger Limited, which owned 51.1% of Berger Paints Jamaica Limited. This acquisition was done via a wholly owned subsidiary of the Ansa Macal group, called Ansa Mcal Coatings International. BRG’s principal activities include the manufacturing and distribution of industrial and decorative paints and paint related materials for the construction, automotive and other industries.

Over the period FY2018-FY2021, BRG grew revenues by a compound average growth rate (CAGR) of 4.61%. Since posting record revenue numbers of \$2.7B in FY2018, BRG has seen yearly declines in revenue. Since then, BRG has noticed recovery in revenue recorded for the FY2021, a 31% growth of \$2.37B the 2020FY year to \$3.11B. Subsequently, BRG reported revenue at \$2.18B for the nine-month period FY2022, an 11.4% year over year growth compared with the corresponding 2021 period.

BRG profits improved from \$11.6M to \$123.3M for the 2021FY. More recent, BRG reported a downturn in profits to \$20.8M for the nine-month period ended September 2022, compared to profits of \$37.6M for the corresponding nine-month period in 2021.

We have placed a **HOLD/MARKETPERFORM** recommendation on the shares of BRG, as we believe the stock is trading close to its fair value. We anticipate the company may continue to see some level of recovery in revenue in FY2022. Nevertheless, the entity is susceptible to adverse economic conditions, this includes rising inflation driven by fluctuations in raw material and freight costs, rising oil prices and a slowdown in the construction industry. BRG’s future earnings should improve, on the basis that strategies continue to be implement by management to contain cost and improve profitability margins.



<b>BRG's Statistics</b>	
Financial Year End	December
Stock Price (12/12/2022)	\$ 10.04
EPS	\$ 0.58
Book Value per share	\$ 6.15
P/E	23.23x
P/B	2.21x
Net Profit FY2021 (millions)	\$ 123
Price Target	\$ 11.20
Dividend Yield	0.0%

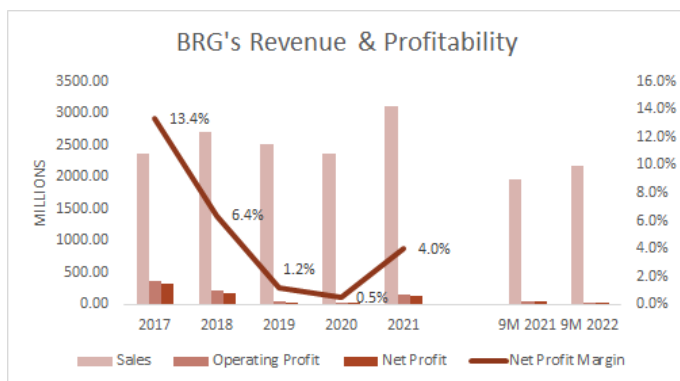
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## Company Overview

**Berger Paints Jamaica Limited (BRG)** was incorporated in Jamaica in 1953 and was listed on the Jamaica Stock Exchange (JSE) in 1992. BRG was originally owned by Lewis Berger Limited, a company domiciled in the United Kingdom and ultimately owned by Asian Paints of India. In June of 2017, Ansa Mcal Limited a Trinidad and Tobago based conglomerate, entered into an agreement to purchase Lewis Berger Limited which owned 51.1% of Berger Paints Limited Jamaica, making them BRG's new parent company. Lewis Berger Limited also owned 100% of Berger Paints Barbados and 70% of Berger Paints Limited. Ansa Mcal Limited acquired Lewis Berger Limited through its wholly owned subsidiary, Ansa Coatings International. Ansa Mcal launched a takeover bid for the remaining 48.9% of the share capital of BRG in September of 2017. They also stated that if they acquired 29% or more of the remaining shares in the offer, they would seek to have BRG's shares delisted from the JSE. They were however unsuccessful in their bid as they only received an additional 3% of the outstanding shares, bringing their total ownership to 54.12%. The company's principal activity involves the manufacturing and distribution of industrial and decorative paints and paint related materials. BRG's registered office is located at 256 Spanish Town Road, Kingston 11.

## Financial Overview

### Profitability



For the period FY2018 - FY2021, the compound average growth rate (CAGR) of Berger's revenues was 4.61%. Berger reported revenues of \$3.11B for the year ended December 31, 2021. This represents a 31% increase when compared to revenues of \$2.37B for the 2020 financial year. The company experienced growth in all their product lines, with decorative/

architectural products accounting for majority of BRG's revenue, which grew by 31.11%, industrial products (45.52%) and automotive products (4.84%). Subsequently, Q3 revenue increased by 13.5%, reported at \$789.3M from \$695.6M the corresponding quarter in 2021. BRG highlighted that this increase in revenue across all channels, is as a result of measures taken to counter the current macro-economic conditions and supply chain challenges. Notably, for the 9M

period, BRG reported revenue at \$2.18B, an 11.4% year over year growth with the corresponding 2021 period.

Raw materials and consumables used in production increased significantly by 72%, from \$1.09B to \$1.88B for the 2021FY. This increase is mainly attributable to the ongoing supply chain challenges and further devaluation of the Jamaican Dollar, as over 95% of BRG's raw materials are sourced internationally. Management highlighted that raw material prices incurred significant and frequent increases and the reliability of supply of these material continues to be under constant threat due to the ongoing supply chain and logistics issues.

Additionally, the increase in oil prices experienced in 2021 was a key contributory factor to the increase in the cost of raw materials used. Close to 50% of raw materials used in the manufacturing of paint are crude oil derivatives, and with crude oil prices rising in 2021, BRG's cost of raw materials would have increased. BRG further highlighted that with the unavoidable increased cost of inputs; a portion of the cost was absorb by the business and translated in the price adjustment of their products, which is absorb by consumers. For the quarter ended September 2022, costs associated with raw materials/consumables and changes in inventories increased from \$337.1M to \$463.9M, as the company experienced challenges with their production lines that resulted in less production when compared to Q3 2021.

Total operating expenditure has grown at a 3-year CAGR of 5%. For FY2021 total operating expenditure rose by 15.46%, as it grew from \$1.16B to \$1.34B. A major contributory factor to this increase was the rise in other operating expenses. Other operating expenses for the 2021 period amounted to \$659.50M, up 24.91% relative to the \$527.99M reported in FY2021. Notably, other operating expenses includes marketing, selling and distribution expenses, which has grown at a 3-year CAGR of 13.57%. Moreover, BRG highlighted that increases in operating expenses resulted mainly from the execution of planned investments in the BOLDLY BERGER campaign and focus on building a sustainable platform for continued growth. However, for the nine months ended September 2022, total operating expenses declined by 9.3% year over year down from \$1.05B to \$950.6M, of which the major contributor, other operating expenses fell by 18.3%.

BRG's operating profit peaked in FY2017 at \$365M, since then operating profit weakened for the 2018-2020 year. However, for the FY2021 operating profit recovered year over year, as it surged from \$11.79M to \$159.69M, a \$148M increase. As such, BRG's operating margin improved for the first time since FY2017, booked at 5.14% from 0.50% in 2020. In the 9M 2022 period, operating profit deteriorated year over year from \$46.9M to \$25.6M, mainly attributable to the rise in cost of goods sold.

Increases in the company's raw materials and consumables used, operating expenditures and a contraction in revenues since FY2017, has translated to diminishing net profits. Net profit has

fallen by a 3-year CAGR of 10.76%. However, despite the increase expenditures for the period under review, BRG has seen recovery in its bottom line as net income for the financial year ended December 31, 2021 surged to \$123.34M from \$11.65M in 2020. This represents a growth of \$111.70M over the \$11.65M recorded for the same period last year. Moreover, net margin improved from 0.49% a year ago to 3.97%, above the 4-year average margin of 3%, which is an indication of BRG's continued recovery. However, more recent net Income decreased to \$20.8M for the nine montha period ending September 2022, down from \$37.6M for the corresponding nine months period in 2021. This fall in net income was attributable to several factors, which includes supply chain challenges, fluctuations in raw material prices and weakened profitability margins.

### *Liquidity & Solvency*

BRG's total assets grew to \$2.29B as at December 2021, which represents a 25.94% increase year over year. Of this, fixed assets grew from \$533.35M to \$618.49M, while current assets grew by 30.06%. The growth in current assets is mainly attributable to the increase in inventories and cash and bank balances which grew by 66.09% and 30.77% respectively. As at Q32022, total assets stood at \$2.3B. Of this, fixed assets rose year over year from \$507.1M to \$619.9M, while current assets fell by 26.8%. Berger faced challenges to increase inventories as at the September 2022 period, which amounted to \$961.3M, a 41.8% year over year downturn. Moreover, trade and other receivables amounted \$552.6M as at Q32022, a 13.9% year over year increase. Notably, cash and bank balances rose by 13.3%, totalled \$138.4M.

The company had an increase in total equity of 13% or \$148.66M for the 2021FY. Shareholders' equity totalled \$1.29B as at the end of the 2021FY, while it stood at \$1.15B at the end of the 2020FY. This increase in shareholders' equity is attributable to the increase in revenue reserved to \$1.11B from \$962.18M booked in FY2020. The return on equity for the company improved significantly to 9.50% from 1.01% in FY2020.

BRG's total liabilities for the 2021FY grew to \$1B from \$676M, an increase of 48% year over year. This is largely due to the increase in 'Due to fellow subsidiaries' which rose from \$102.32M to \$281.95M as at FY2021. Moreover, 'Due to immediate parent company' and 'trade and other payables' rose by 65% and 25% respectively. Notably, Berger has no interest bearing debt on their books. However, total liabilities for the quarter ended September 2022 fell by 39.5% year over year, totalling \$987.3M versus \$1.6B for the same period last year, driven by a 44.4% decline in current liabilities to \$801.3M.

The company's liquidity position deteriorated for the FY2021 due to the significant increase in current liabilities. The company's current ratio for the period under review was 2.07x, a

decrease from a ratio of 2.67x in 2020. Moreover, the quick ratio and cash ratio fell to 1.16x and 0.34x respectively.

### **Cash Flow Statement Overview**

Cash from operating activities (CFO) represented inflows of \$215.59M for the twelve-month period, relative to outflows of \$307.76M in 2020. The improvement in CFO was mainly driven by the increase in BRG's profit. Notably, the changes in working capital moved from an outflow of \$348.46M in FY2020 to an outflow of \$28.466M in FY2021, a main driver to the lower working capital is the increase in payables from an outflow of \$105.69M to an inflow of \$48.95M, indicating the company is taking longer to pay suppliers. Notably, the company's inventories increased from an inflow of \$192.98M for the 2020FY to an outflow of payments for increase in inventories to \$294.56M for the 2021FY, due to ongoing supply chain challenges.

Cash from investing activities represented an outflow of \$129.35M for FY2021, relative to an outflow of \$87.81M in FY2020. Acquisition of PPE was the primary outflow from investing activities.

Cash from financing activities represented an outflow of \$15.16M for the period, relative to an outflow of \$12.25M in 2020. This was driven by the increase in lease liability payments, which amounted to \$14.98M.

In FY2021, the company experienced an improvement of \$71.07M to its cash balance (not accounting for currency translation gains). To date, the working capital positioning of the Company has declined. Specifically, operating cash flow before working capital amounted to \$84.44M relative to \$88.83M in the prior year. Notably, the change in working capital for the nine-month period has amounted to an outflow of \$158.2M, relative to an outflow of \$140.6M the prior year. Consequently, net operating cash flow for the 2022 nine-month period has amounted to an outflow of \$98.8M relative to an outflow of \$59.2M the prior year.

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### **Outlook & Valuation**

The Jamaican economy continued its recovery in Q3 2022 (July-September) recording a year over year increase of 4.3%. The goods producing sector recorded a growth of 3.2%, while the service industry recorded a 4.7% increase. Notably, the construction sector recorded a 2.2% downturn for the third quarter, following a 5.4% decline (April-June 2022). This performance was primarily driven by a contraction in civil engineering works and building construction, in particular, residential construction. In addition, a contraction in construction tax revenue compared to a

REAL VALUE ADDED IN THE GOODS PRODUCING INDUSTRIES (%)					
	Jul-Sep 2021	Oct-Dec 2021	Jan-Mar 2022	Apr-Jun 2022	Jul-Sep 2022
Goods Producing	2.2	0.5	0.6	-2.0	3.2
Agriculture, Forestry & Fishing	7.3	13.8	8.4	6.3	15.4
Mining & Quarrying	-29.1	-60.5	-60.0	-62.5	-30.4
Manufacturing	3.7	-2.2	4.5	5.6	3.5
Construction	4.4	5.9	3.5	-5.2	-2.2

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year ago, particularly retail sale of hardware, construction material paint and glass, supports the assessed decline in the industry.

As such, we expect a slowdown in construction throughout the remainder of the financial year. This assumption was form due to a downturn in the construction sector, fewer housing starts and the likely negative impact rising interest rates would have on the industry. Therefore, a slowdown in the construction industry is likely to

impede the demand for BRG’s primary product, decorative paint. Additionally, the fluctuation in oil prices is likely to increase BRG’s cost of sales, which is expected to lower future earnings.

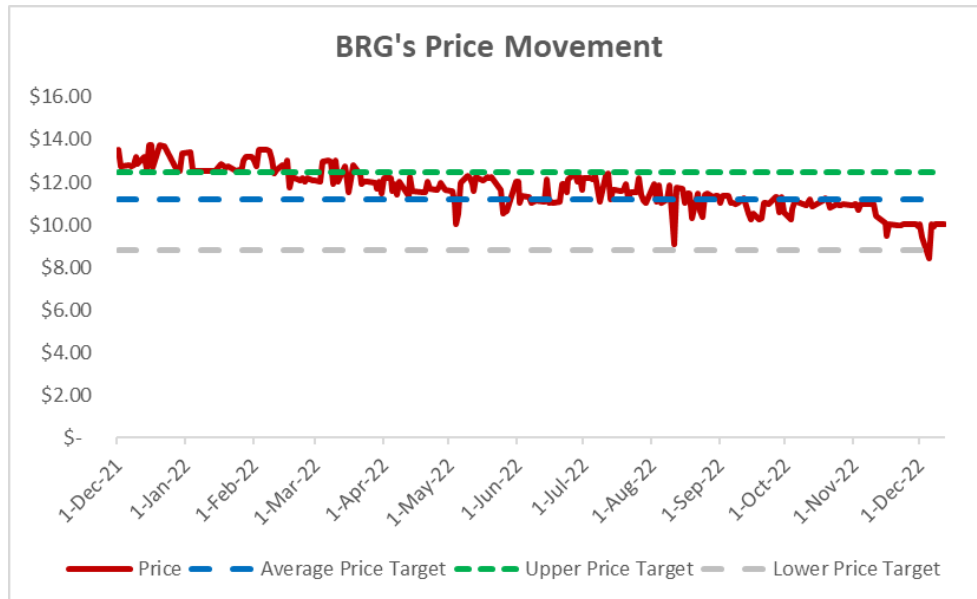
We expect a tightening of the monetary policy environment to contain inflation, and as such, this would translate to higher rates to finance housing developments and purchases, i.e. higher mortgage rates. This could possibly adversely affect BRG, which could see a reduction or slowing of the growth rate at which the entity’s products be demanded. Essentially, a possibly subdued construction industry for the projected period is likely to have a corresponding effect on BRG’s revenue generation.

We are forecasting revenues of \$3.41B for the year ended December 2022, a 9.61% increase year over year and net profits of \$112.3M, a 9% decrease from the prior year. This translates to earnings per share (EPS) of \$0.52. This represents a 5% increase over BRG’s trailing EPS of \$0.50.

Based on these assumptions, we arrived at our price target of \$11.20 using the Discounted Cash Flow (DCF) model. Meanwhile using the DCF under two additional scenarios produced our upper and lower case price targets of \$12.47 and \$8.78 respectively. The primary difference between the scenarios is the trajectory of interest rates, global commodity prices, oil prices and the impact it has on the construction industry. The best-case scenario assumes a reduction in interest rates, which would likely improve financing of housing developments, and a recovery in global commodity prices, lower oil prices and a booming construction industry. Meanwhile, we looked at a different scenario with a slowdown in revenue generation due to increased interest rates and global commodity prices, rising oil prices and a dampening in the construction industry.

	Price Target	Implied Upside/Downside
Upper	\$ 12.47	24%
Base	\$ 10.55	5%
Lower	\$ 8.78	-13%

Additionally, we employed the Price Multiples approach to determine a fair value for BRG. Applying the 1-year average P/E and P/B ratios to our forward estimates of EPS and BVPS of \$0.52 and \$6.68, yield prices of \$10.43 per share and \$12.63 per respectively. **The average of our price forecasts, \$11.20 is 11.6% higher than the closing price of \$10.04 recorded in mid-December 2022.**



### Key Risks to Our Price Target

The major risks to our price target include the ability of Berger to be able to generate forecasted revenues. An additional risk to our price target is the ability of BRG's management team to contain operational expenses as well as cost of materials used. Raw materials supply issues remained one of the most significant risks to the business. BRG highlighted that global supply chain challenges saw many international suppliers calling force majeure, as the shortage of key supplies drove unit prices up significantly. Furthermore, an increase in the price of crude oil, may potentially lead to an increase in cost of materials, given that half of the materials used in production, are crude oil derivatives. Additionally, volatility in the foreign exchange market versus its \$USD counterpart is likely to adversely impact BRG's cost of sales, as over 95% of BRG's raw materials is sourced internationally.

Investor sentiment around the shares of Berger Paints has decreased significantly since: 1) the takeover of the majority shares by Ansa Mcal, 2) the unsuccessful takeover bid of the remainder of the shares and 3) a string of subpar financial performances.



## Recommendation

We assign a **HOLD/MARKETPERFORM** recommendation to BRG at this time, as the stock is currently trading close to our estimated fair price estimate of \$11.20. The company may face negative headwinds in the near term. The ongoing supply chain challenges, rising crude oil prices, anticipated slowdown in the construction industry could possibly put a strain on BRG's revenue generation and ability to contain expenses.

Nevertheless, after three years of downward trajectory in BRG's revenue, the company was able to improve revenue for the 2021FY and their most recent quarter. This is an indication that despite the ongoing challenges to improve revenue and contain cost, some level of recovery is on the horizon for BRG.

## Abridged Financials

Abridged Financials \$'000	YEAR END						21-Sep	22-Sep	Change
	YE2017	YE2018	YE2019	YE2020	YE2021	Change			
<b>Sales</b>	2,363,088	2,714,994	2,525,347	2,371,281	3,108,089	31.07%	1,958,827	2,181,350	11.36%
Raw materials and consumables used	(1,080,705)	(1,384,371)	(1,366,689)	(1,091,421)	(1,878,366)	72.10%	(1,206,989)	(1,241,271)	2.84%
<b>Gross profit</b>	1,282,383	1,330,623	1,158,658	1,279,860	1,229,723	-3.92%	751,838	940,079	25.04%
Profit before Tax	365,668	212,160	41,397	11,793	159,693	1254.13%	46,900	25,607	-45.40%
<b>Profit for the year</b>	315,535	173,550	29,302	11,645	123,340	959.17%	37,617	20,805	-44.69%
<b>Total Assets</b>	1,488,973	1,928,006	2,321,224	1,825,801	2,299,453	25.94%	2,811,529	2,306,420	-17.97%
<b>Total liabilities</b>	512,050	787,623	1,212,395	676,081	1,001,074	48.07%	1,631,137	987,313	-39.47%
<b>Total Shareholder's Equity</b>	976,923	1,140,383	1,108,829	1,149,720	1,298,379	12.93%	1,180,391	1,319,108	11.75%
<b>EPS (\$)</b>	1.47	0.81	0.14	0.05	0.58		0.18	0.10	
Book Value per share (\$)	4.56	5.32	5.17	5.36	6.06		5.51	6.15	
<b>Key Ratios</b>									
Gross Profit margin	54.3%	49.0%	45.9%	54.0%	39.6%		38.4%	43.1%	
Pre-Tax Margin	15.5%	7.8%	1.6%	0.5%	5.1%		2.4%	1.2%	
Net Profit margin	13.4%	6.4%	1.2%	0.5%	4.0%		1.9%	1.0%	
Return on Assets	21.2%	9.0%	1.3%	0.6%	5.4%		1.3%	0.9%	
Return on Equity	32.3%	15.2%	2.6%	1.0%	9.5%		3.2%	1.6%	
Current ratio (x)	2.99	2.36	1.80	2.67	2.07		1.60	2.10	
Quick ratio (x)	2.09	1.64	1.19	1.75	1.16		0.45	0.90	
Cash ratio (x)	1.02	0.54	0.56	0.44	0.34		0.08	0.17	

**Source:** [www.jamstockex.com](http://www.jamstockex.com), [boj.org.jm](http://boj.org.jm), [pioj.gov.jm](http://pioj.gov.jm), [Bloomberg](#), [Company Financials](#), [Company Prospectus](#), [JMMB Investment Research](#).

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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.

**STRONGLY UNDERPERFORM**—REDUCE EXPOSURE IN YOUR PORTFOLIO TO LESS THAN 2.5% FOR THIS PARTICULAR ASSET

**UNDERPERFORM**—REDUCE EXPOSURE IN YOUR PORTFOLIO TO 2.5% - 4.9% FOR THIS PARTICULAR ASSET

**SELL**—REDUCE EXPOSURE IN YOUR PORTFOLIO TO ZERO.

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

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

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