



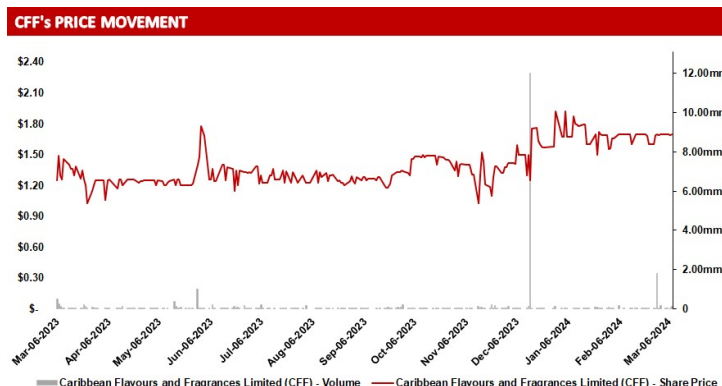
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EXECUTIVE SUMMARY

Caribbean Flavours and Fragrances Limited (CFF), was established in 2001 and its shares listed on the Junior Market of the Jamaica stock exchange in 2013. In 2017, CFF became a subsidiary of the Derrimon Trading Group, as they increased their holdings in the company from just over 45% to 75%. CFF's principal activities include the manufacture and distribution of flavours, mainly for the beverages, baking and confectionary industries. At the onset of the COVID-19 pandemic, the company began producing its own brand of hand sanitizer.

Over the period FY2020-FY2023, revenue improved at a compound average growth rate (CAGR) of 14.9%. CFF recorded revenues of \$900.8M in the 2023FY, as demand of CFF's products increased. CFF profits improved from \$61.7M to \$132.8M for the 2023FY.

We have placed a **MARKETPERFORM/HOLD** recommendation on the shares of CFF as we believe the stock is trading close to its fair value. We expect CFF's revenue growth rate to improve in the 2024FY, CFF's strategy to expand its footprint in the export market, providing new products to several partners, and the deepening of sales strategies in various markets. As the company continues to diversify its revenue streams and grow its regional customer base, CFF will be utilizing its parent company, Derrimon Trading Limited (DTL), presence in the diaspora through a specialty supermarket and food distributor. This synergy with CFF's parent company would allow the company to leverage Derrimon's distribution network to reach broader target markets.



CFF's Statistics

Financial Year End	December
Stock Price (8/3/2024)	\$ 1.70
EPS	\$ 0.15
Book Value per share	\$ 0.72
P/E	12.19x
P/B	2.48x
Net Profit FY2023 (millions)	\$ 132.8
Price Target	\$ 1.95
Dividend Yield	2.78%

Company Overview

Caribbean Flavours and Fragrances Limited (CFF) was incorporated on the 23rd of February 2001 and commenced operations later in October of 2001. CFF purchased its business and assets from prior owner Bush Boake Allen Jamaica Limited ("BBA") when that entity voluntarily wound up its Jamaican operations in 2000 after 40 years in business. CFF listed on the Junior Market of the Jamaica Stock Exchange on October 2, 2013. CFF's registered office is located at 226 Spanish Town Road, Kingston.

The company's principal activity involves the manufacturing and distribution of flavours, mainly for the beverages, baking and confectionary industries. CFF also manufactures and distributes fragrances for general and household cleaning products, as well as for sanitation purposes.

In January of 2017, Derrimon Trading Limited (DTL) made a tender to purchase all the stocks in CFF not already held by them. This offer was accepted by the 2nd and 3rd largest shareholders at the time¹, which increased DTL's stake from 49.02% to 75.02%, resulting in CFF becoming a subsidiary of the DTL group. As at December 2023, Derrimon's stake in CFF is 65.02%.

Notably, CFF's 10-year tax remission ended on October 2023 which means that the company will be taxed at the statutory 25% rate going forward.

Financial Overview

Profitability

Revenue has improved at a CAGR of 14.9% for the period FY2020 – FY2023. For the 2023FY ended December 31, CFF grew revenues by 16.6% from \$772.2M to \$900.8M. CFF highlighted that this growth in revenues for the period was driven by continuous refinement of sales approach strategy, providing new products to various partners and the deepening of sales strategies in various markets. Notably, increased orders in the flavours segment and expanded product range for bakeries also contributed to the growth in revenue.

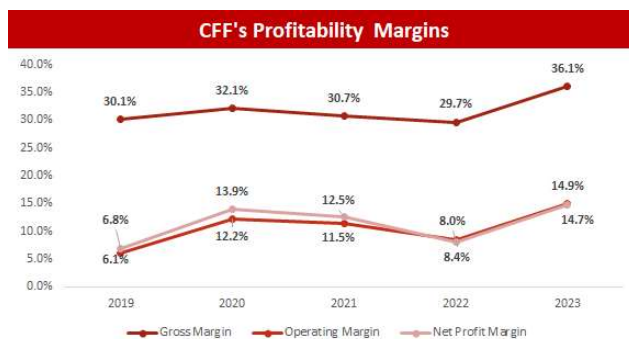


¹ The 2nd and 3rd largest shareholders were the principals of the company; Anand and Joan James.

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Cost of goods sold (COGS) increased to \$576M from \$543.2M, a 6.0% increase for the 2023FY. CFF's cost of sale margin improved year over year due to the stabilization of commodity prices along with efficiency strategies in place. Gross profits amounted to \$324.8M, up 41.8% year-over-year. As such, gross margin improved to 36.1% from 29.7% a year ago. Management highlighted the improvement in gross margin was driven by improved management of inventories, efficiencies gained from the manufacturing of processes and change of product mix.

Administrative expenses for the 2023FY totaled \$179.3M. This reflects a 16.7% increase when compared to 2022's administrative expenses of \$153.6M. In 2023FY, there were increases in staff related costs and directors' emoluments, increased legal and professional fees, insurance cost, bad debt and utilities. Notably, staff costs grew 20.5% from \$56.3M to \$67.9M as salaries and wages increased. CFF highlighted that the increase in expenses was mainly influenced by attracting new talent and other professional fees related to product development. Selling and promotional expenses increased by 19.1% from \$9.1M to \$10.9M for FY2023.



CFF reported an improvement in operating profit at \$134.6M for the 2023FY, from \$64.5M the previous year. As such, operating margin improved to 14.9% from 8.4% the previous year.

CFF's finance income surged to \$21.2M from \$6.2M a year ago. The main contributor to the increase in finance

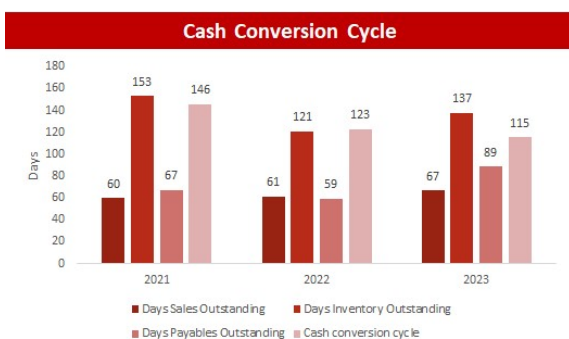
income, is the increase in interest income and foreign exchange gains to \$17.6M and \$12.2M respectively. For the 2023FY, profit before tax amounted to \$155.8M, up 120.3% year over year. Notably, the 10 years' preferential tax treatment that CFF received after listing on the Jamaica Stock Exchange's Junior Market ended on October 2023. Therefore, the company will now pay corporate income taxes at a rate of 25%. CFF's Net Income for the financial year ended December 31, 2023 amounted to \$132.8M. This represents a 115.3% surge in profit from \$61.7M recorded for the same period last year. Moreover, net profit margin improved from 8.0% a year ago to 14.7%. The average return on assets stood at 16.1%, compared to 8.3% a year prior, while the average return on equity stood at 21.9%, relative to 11.3% in 2022. Earnings per share (EPS) for the 2023FY came in at \$0.15, up from \$0.069 from the previous financial year.

Liquidity & Solvency

For the 2023FY, assets grew to \$895.8M from \$757.4M. Non-current assets amounted to \$158.8M, slightly down by 1.2% year-over-year, while current assets amounted to \$737.0M, up 23.5% from the prior year's balance. There was an increase in property, plant and equipment (PPE) to \$45.3M from \$39.3M. However, right use of assets and deferred tax assets fell to \$68.1M and \$343K respectively. The increase in current assets was driven by a 334.8% surge in short term deposits to \$237.1M. Furthermore, inventories and receivables rose to \$217.0M and \$164.3M respectively. These increase was partially offset by a 50.8% decline in cash and bank balances to \$112.6M.

Total liabilities for the 2023FY, amounted to \$244.1M, a 26.1% or \$50.5M increase year-over-year. Non-current liabilities fell 9.1% to \$83.61M, while current liabilities grew by 58.0% to \$160.5M. The decrease in non-current liabilities was due to the downturn in lease liability booked at \$74.3M and a 30.4% fall in long term loans to \$9.3M. The increase in current liabilities was mainly driven by a 58.9% increase in payables to \$139.8M. The company's current ratio for the period under review was 4.6x, down from 5.9x the previous financial year. Moreover, the quick ratio and cash ratio followed a similar trend, deteriorating to 3.2x and 0.7x respectively.

Total debt amounted to \$13.5M for the 2023FY. CFF's leverage as measured by the debt-to-equity ratio stood at 0.02x, as the company has minimal interest bearing debt on its books. Shareholders' equity amounted to \$651.7M, up 15.6% year-over-year as retained earnings rose by 17.3% to \$595.5M. This has resulted in a book value per share of \$0.72, which is greater than the \$0.63 book value per share as at December 2022.

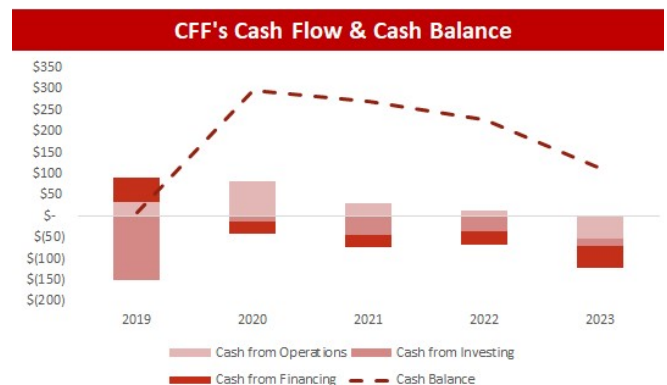


days a year ago.

Additionally, the company's cash conversion cycle has decreased to 115 days from 123 days. This indicates that the company is taking a relatively longer time to pay suppliers, as Days Payables Outstanding (DPO) increased to 89 days from 59 days in the 2022FY. Notably, Days Inventory Outstanding (DIO) increased from 121 days during the 2022FY to 137 days during the 2023FY, while Days Sales Outstanding (DSO) rose to 67 days from 61

Cash Flow Statement Overview

Cash from operating activities (CFO) represented outflows of \$52.0M for the twelve-month period, relative to inflows of \$14.5M in 2022. The deterioration in CFO was mainly driven by the increase in cash used for inventories and increase in due from related parties. Notably, the changes in working capital moved from an outflow of \$49.9M in FY2022 to an outflow of \$201.7M in FY2023, a main driver to the lower working capital is the increase in cash used for inventories from an inflow of \$6.1M to an outflow of \$37.6M and an increase in the movement of funds due to related parties amounting to \$181.9M. Cash from investing activities represented an outflow of \$16.5M for FY2023, relative to an outflow of \$35.4M in FY2022. Purchase of fixed assets was the primary outflow from investing activities. Cash from financing activities represented an outflow of \$53.8M for the period, relative to an outflow of \$31.3M in 2022. Notably, cash paid to long term loans amounted to \$4.1M. Moreover, the company made dividend payments, which amounted to \$45M, up from \$22.5M paid the prior period in the 2022FY. In FY2023, the company experienced a loss of \$122.4M to its cash balance (not accounting for currency translation gains).



Outlook & Valuation

The projected upward trends in various economic indicators, such as real GDP growth, suggest a promising outlook for the Jamaican economy. The World Bank estimates Jamaica's real GDP growth for 2024 and 2025 at 2.0% and 1.4%, respectively. Additionally, the domestic labor market is expected to remain solid over the next 12 to 18 months, contributing to buoyant income levels. This anticipated improvement is fueled by employment growth across diverse industries, including manufacturing, tourism, distribution, finance & insurance, and business process outsourcing (BPO), reflecting a normalization of economic activity.

The Bank of Jamaica's (BOJ) decision to maintain the policy rate at 7% despite concerns about inflation exceeding the target range of 4%-6%, has raised questions about potential rate hikes. However, it's likely that the BOJ will employ alternative measures to address inflation, including active participation in the foreign currency market. The inflation rate in Jamaica stood at 7.4% in

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January 2024, above the target range, primarily due to higher regulated prices and wage increases. The BOJ anticipates inflation to remain above the upper limit of its forecast band until March 2025, mainly driven by fare increases for public passenger vehicles. Although the government has reduced bus fares to mitigate inflation, risks to the forecast remain tilted towards the upside. Internal projections suggest that inflation may surpass the BOJ's target band by March 2024 and into 2025 due to international and domestic economic dynamics.

According to the Planning Institute of Jamaica (PIOJ), Jamaica's economy grew in Q3 2023, with a year-over-year increase of 1.9%. The manufacturing industry recorded a notable improvement, driven by higher output in food, beverages, and tobacco components. This growth bodes well for companies like CFF, which provides essential components for major manufacturing and service-based businesses. With increased demand expected in the manufacturing industry, CFF is poised to benefit.

Additionally, CFF's strategy to expand its footprint in the export market is gaining traction, with the company making its first export to a Spanish-speaking country since the start of the 2022 financial year. Also, supplying new products through Derrimon's retail outlets locally and in the diaspora further enhances its revenue potential. The increase in export sales is likely to mitigate the impact of fluctuating raw material costs, especially if the Jamaican dollar depreciates against the US dollar.

CFF's sound financial position, with comparatively low levels of indebtedness, positions it well to access debt at favorable rates for capital asset acquisition. Despite potential short-term challenges such as rising costs and higher tax rates, the company's robust growth in revenue and earnings in FY2023 underscores its long-term growth prospects. While a decrease in earnings is anticipated for FY2024, medium to long-term growth is expected as CFF expands its product range, export profile, and regional presence.

Despite navigating the pandemic successfully, CFF continues to capitalize on new opportunities, such as the production and sale of hand sanitizers. The sustained demand for these products, along with fragrances used in cleaning supplies, is expected to contribute favourably to CFF's revenue growth even as demand normalizes.

Overall, while short-term challenges exist, CFF's long-term outlook remains positive, driven by its strategic initiatives and growth potential in both domestic and international markets. Based on these assumptions, we are forecasting revenues of \$1.05B for the year ended December 2024. We expect the beverage sector in Jamaica to return to normalcy throughout the rest of the year,

leading to an increase in demand by beverage manufacturers. We have forecasted net income of \$97.5M.

We are forecasting a forward book value of \$710.1M as at December 31, 2024, which translates to a book value per share of \$0.79. We employed the price-multiples approach to determine the fair price for CFF. We utilized the average P/E of comparable listed companies to arrive at a market multiple of 22.4x, which when applied to the forward EPS of \$0.108 resulted in a target price of \$2.43, while the P/B for the peer group of 1.7x yields a price of \$1.33.

The 2-yr historical average for the P/B ratio is 2.55x, which when applied to the forward BVPS yields a price of \$2.01. The 2-year historical average for the P/E ratio is 18.58x, which when applied to the forward EPS yields a price of \$2.01. **The average of our price forecasts, \$1.95 is 14.6% higher than the closing price of \$1.70 on March 8, 2024.**

Company	Market Capitalization	Price to Earnings	Price to Book	Return on Equity	Return on Assets	Dividend Payout	Dividend Yield
AMG	1,489,612,369	16.7X	1.2X	7.0%	5.4%	0.0%	0.0%
BPOW	1,700,619,900	20.9X	1.1X	5.4%	5.1%	13.9%	0.7%
HONBUN	3,016,108,480	13.0X	2.3X	17.6%	13.4%	32.5%	2.5%
JAMT	5,195,232,905	27.9X	1.3X	4.6%	3.6%	0.0%	0.0%
KREMI	1,476,415,649	54.5X	1.8X	3.3%	1.3%	0.0%	0.0%
PTL	3,239,180,868	13.2X	2.9X	21.7%	11.1%	0.0%	0.0%
PURITY	449,872,525	35.0X	0.6X	1.8%	1.1%	0.0%	0.0%
Sector Average	4,405,976,267	22.4X	1.7X	10.0%	7.0%	23.2%	1.6%
CFF	1,709,989,485	11.5X	2.3X	20.4%	14.8%	36.4%	1.4%

Key Risk to Our Price Target

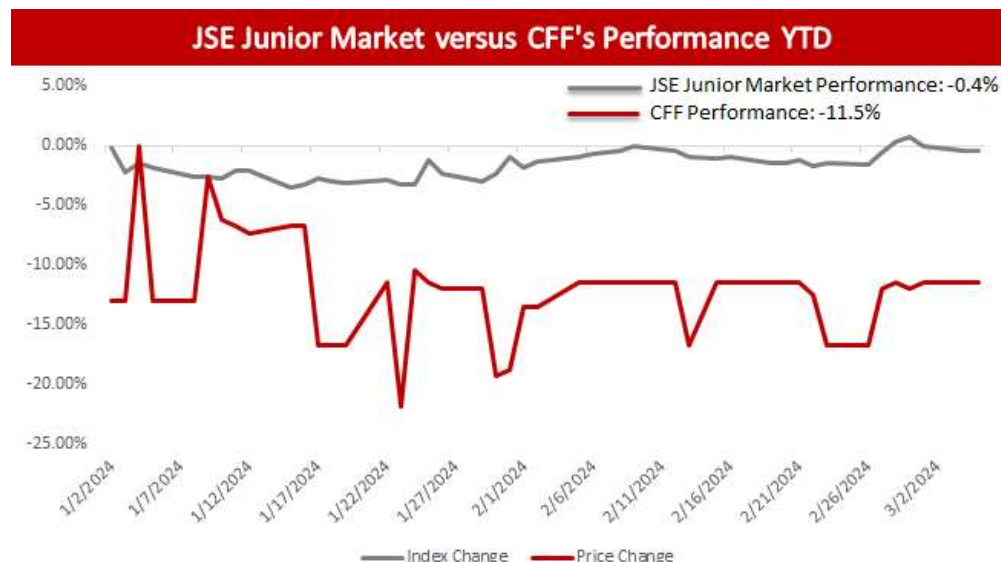
CFF's ability to contain costs is essential to the company's operating profits being in-line with our forecasts. The company continues to grapple with fluctuations in input cost and supply chain disruptions, which is likely to lower CFF's profitability margins. Management highlighted that there are disruptions in receiving key inputs, which is leading to shortages in various commodities. As such, the company increased inventory to mitigate against the delay in receiving raw materials from suppliers and meeting consumer demand. Additionally, as the price of raw material fluctuates, CFF makes moderate price increases. This increase in prices may reduce affordability by some consumer and as such lower demand. Furthermore, if CFF is unable to achieve the level of finance income forecasted due to exchange rate fluctuations, this would have an impact on net income. If there is a material impact on net income from the above mentioned factors, we are of the view that this may decrease the attractiveness of this stock to investors.

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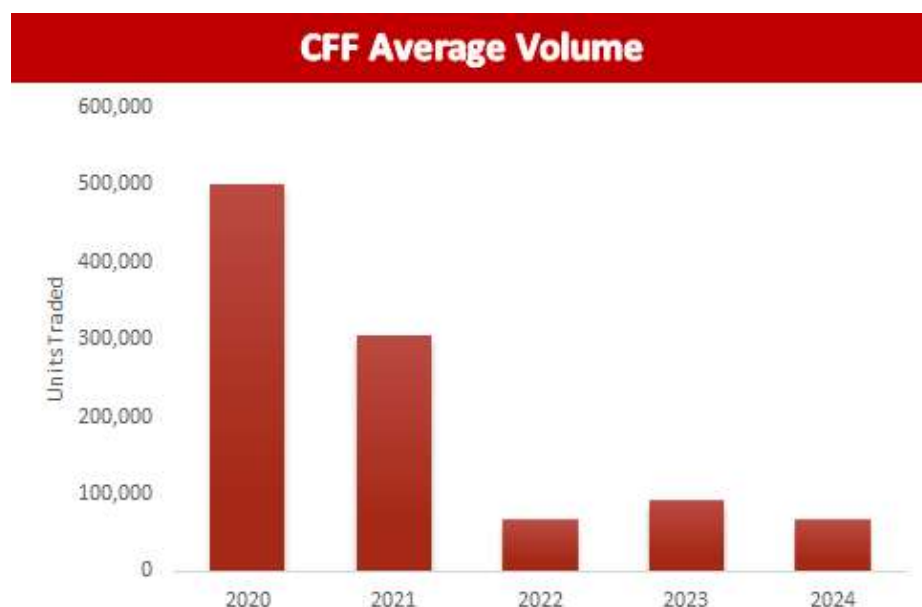
Recommendation

We recommend Caribbean Flavours and Fragrances Limited (CFF) as MARKETPERFORM/HOLD as our estimate of the fair value is line with the current market value. This asset is most suitable for equity investors with a medium to high risk tolerance. The strategic initiative to diversify income streams through regional expansion, should enhance the financial performance of the company. Conversely, cost containment should be managed within the context of achieving optimal operation efficiency. CFF has invested in its products and staff to be able to capitalize on opportunities presented by the pandemic as well as changes awaiting in the beverage sector.

CFF's stock performance year to date (YTD), depreciated by 11.5%, which is below the YTD performance of the Jamaica Stock Exchange (JSE) Junior Market. Moreover, CFF's liquidity has improved year over for the 2023YE, the average daily volume stood at 90.7K units traded in comparison to 65.5K units traded the 2022YE.



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Abridged Financials \$'000									
	2016	2017	2018	2019	2020	2021	2022	2023	Change
Revenue	362,500	410,636	674,298	462,462	593,753	637,714	772,229	900,805	16.6%
Cost of Sales	(227,805)	(242,694)	(432,190)	(323,302)	(403,172)	(441,813)	(543,217)	(576,017)	6.0%
Gross profit	134,695	167,942	242,108	139,160	190,581	195,901	229,012	324,788	41.8%
Operating Profit	62,499	72,930	93,856	28,100	72,307	73,149	64,545	134,620	108.6%
Net Profit	74,070	82,877	115,881	31,500	82,299	79,595	61,698	132,819	115.3%
Total Assets	296,092	376,108	474,469	563,221	635,016	725,308	757,449	895,819	18.3%
Total Liabilities	19,741	45,538	50,499	133,043	145,019	200,676	193,599	244,110	26.1%
Total Shareholder's Equity	276,351	330,570	423,970	430,178	489,997	524,632	563,850	651,709	15.6%
EPS (\$)	0.08	0.09	0.13	0.04	0.09	0.09	0.07	0.15	
Book Value per share (\$)	0.31	0.37	0.47	0.48	0.54	0.58	0.63	0.72	
Key Ratios									
Gross Profit margin	37.2%	40.9%	35.9%	30.1%	32.1%	30.7%	29.7%	36.1%	
Operating Profit Margin	17.2%	17.8%	13.9%	6.1%	12.2%	11.5%	8.4%	14.9%	
Net Profit margin	20.4%	20.2%	17.2%	6.8%	13.9%	12.5%	8.0%	14.7%	
Return on Average Assets	25.0%	24.7%	27.2%	6.1%	13.7%	11.7%	8.3%	16.1%	
Return on Average Equity	26.8%	27.3%	30.7%	7.4%	17.9%	15.7%	11.3%	21.9%	
Current ratio (x)	14.85	9.79	9.94	9.11	9.13	5.89	5.88	4.59	
Quick ratio (x)	11.21	7.15	7.07	5.83	6.53	4.02	4.11	3.24	
Cash ratio (x)	6.31	1.84	1.44	0.23	5.10	2.73	2.26	0.70	
Debt/Equity (x)	-	0.03	0.02	0.01	0.00	0.04	0.03	0.02	

Source: *www.jamstockex.com, boj.org.jm, pioj.gov.jm, www.worldbank.org, 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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