

Lumber Depot Trading Company Limited (LUMBER)



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EXECUTIVE SUMMARY

Lumber Depot Company Limited (LUMBER), born out of the Blue Power Group (BPOW), was incorporated and domiciled in Jamaica on July 30, 2019. The company began trading on August 1, 2019 and listed on the Junior Market of the Jamaica Stock Exchange on December 16, 2019. The main activities of the company comprise of the sale of lumber, hardware supplies and other construction related products.

LUMBER's PRICE MOVEMENT



Over the 12-month period ended April 2023, LUMBER has grown revenues to \$1.52B, a 3.2% decrease over the 2022FY revenues of \$1.57B. LUMBER's profit also experienced a downturn by 21.1% to \$145.17M for the period under review, compared to profits of \$183.89M for the 2022FY. More recent, for the six-month period, LUMBER noticed an uptick in revenue by 0.7% to \$782.06M, as there has been a slow-down in the construction industry. LUMBER's net profits grew to \$86.73M for the period ended October 2023, compared to profits of \$78.20M for the corresponding six-month period in the 2022/23FY.

LUMBER's Statistics

Financial Year End	April
Stock Price (26/01/2024)	\$ 2.51
Trailing EPS	\$ 0.22
Book Value per share	\$ 0.78
Trailing P/E	11.00x
P/B	3.01x
Net Profit FY2023 (millions)	\$ 145
Price Target	\$ 2.60
Dividend Yield	2.18%

We attach an **UNDERWEIGHT** recommendation to LUMBER, as we anticipate a slowdown in growth, given the near to medium term challenges. The entity is susceptible to adverse economic conditions, this includes rising inflation and increased interest rates, which could have negative implications for the construction sector.

Company Overview

Lumber Depot Company Limited (LUMBER) is a full service hardware and building materials company. LUMBER was incorporated and domiciled in Jamaica on July 30, 2019 and commenced trading on August 1, 2019.

LUMBER entered into an Intragroup Reconstruction Agreement with the Blue Power Group Limited (BPOW), which saw them assuming the benefit and burden of the Hardware Business. On August 1, 2019, Blue Power Group Limited sold its' Lumber division to the company, and at that time certain assets and liabilities of BPOW's Lumber division were transferred at book value to the company. The assets of the Hardware Business were transferred to LUMBER and there was no change to the management team of the Hardware Business. The Hardware Business has been in operation since 1998. The Company conducts its principal trading operations at 17c Gordon Town Road in Papine, St. Andrew. Lumber also operates an off-site overflow storage facility at 4 Victoria Avenue, in Kingston.

LUMBER's main business includes the sale of lumber, hardware supplies and other construction related products. Approximately 70% of the company's sales consist of cement, steel, lumber and paints. The company's main clientele includes small contractors, home owners and a few owners of commercial buildings. Lumber sources most of its supplies locally, such as cement from Caribbean Cement Co., paint from Berger Paints Ltd and steel from Tankweld Metals. The company however imports its lumber from Brazil, China and the USA.

Financial Performance

Profitability



LUMBER reported revenue of \$1.52B, a 3.2% year over year decrease for the 2023 financial year, relative to \$1.57B in 2022. More recent, the company reported a decrease in revenue for the October 2023 quarter of \$364.61M, a 3.3% decrease over the \$376.87M achieved in Q2 2022/23. Moreover, for the six-month period, revenue was up marginally year over year, reported at \$782.06M from \$776.75M the

previous comparable period. Management highlighted that consumers reacted to uncertain

economic conditions, including high interest rates and a spike in commodity prices for certain key hardware items, which led to the tempering in sales for the period.

The company highlighted their efforts to contain the impact of fluctuations in global commodity prices and transport prices, by fostering relationships with key construction suppliers locally and overseas. Consequently, cost of sales for the period was relatively stable, amounting to \$1.23B. Nevertheless, there was an increase in the company's cost of sale margin from 78.4% (2022) to 80.9% for the 2023 year-end. Subsequently, for the six-months period, Lumber's cost of sales fell by 1.2% year over year, amounting to \$616.76M from \$624.53M the prior comparable period. This resulted in a decrease in the company's cost of sales margin to 78.9% from 80.4% in the 6M 2022/23 period.

Gross margin for the 2023FY fell to 19.1% relative to 21.6% reported for the 2022 year-end. Consequently, gross profit for the period closed at \$290.81M, down 14.5% year over year from the \$340.31M reported in 2022 financial year. More recent, Lumber reported an 8.6% growth in gross profit for the 6M period to \$165.30M. As such, there was an improvement in gross margin to 21.1% from 19.6% for the 6M 2023/24 period.

In the year ended April 2023, there was a reversal of losses on trade receivables, totaling \$3.19M. Reversal of impairment losses occurs when there is a collection of outstanding credits, which factored into the calculation of loss allowances. The corresponding 2022 period, had a reversal of impairment loss on trade receivables, which amounted to \$2.59M. Additionally, the company reported administrative and other expenses of \$153.09M, down 7.4% from \$165.37M reported in the corresponding period.

LUMBER's net finance costs fell by 44.4% or \$3.22M, decreasing to \$4.04M from 2022FY's net finance cost of \$7.25M. Of this, finance income amounted to \$4.54M (2022: \$3.14M). Conversely, finance cost amounted to \$8.57M (2022: \$10.40M).

Net Income fell by 21.1% to \$145.17M, down from \$183.89M a year ago. This decrease in net income was mainly attributable to the slowdown in revenue and downturn in profitability margins. Moreover, net profit margin deteriorated to 9.5% from 11.7% a year ago. The return on average assets stood at 23.0%, compared to 33.1% a year prior, while the return on average equity stood at 27.2%, relative to 45.9% in 2022. Subsequently, net income improved to \$86.7M for the six-month period ending October 2023, up from \$78.20M for the corresponding six-month period in 2022. The trailing twelve month (TTM) EPS for Lumber stands at \$0.22.

Liquidity & Solvency

Total assets for LUMBER rose by 16.8%, from \$583.25M as at April 2022 to \$681.47M as at April 2023. Of this, there was an uptick in fixed assets to \$291.85M from \$290.97M, while there was a 33.3% increase in current assets, as it improved to \$389.62M from \$292.28M. The increase in current assets was mainly attributable to the rise in cash and cash equivalents, moving from \$82.81M to \$184.44M as at April 2023. Moreover, accounts receivables and prepayments rose by 9.9% to 43.75M, while inventories fell by 5.4% to \$158.87M.

Subsequently, total assets climbed to \$718.80M at the end of Q2 FY2024, a year over year increase of 11.6%. This was driven by a 64.8% surge in cash and cash equivalents, which grew to \$194.31M from \$117.90M the prior comparable period. Furthermore, inventories rose by 11.8% year over year, to \$177.31M.

For the 2023FY, total liabilities stood at \$94.28M, down 9.8% from \$104.51M a year ago. Current liabilities fell by 9.8%, driven by the decrease in accounts payables to \$94.28M from \$104.51M. As at April 2023, LUMBER has no long-term liabilities on their books. The company shareholders' equity amounted to \$587.19M, up 22.7% from the prior year, as retained earnings rose to \$417.13M from \$308.68M the prior year. This has resulted in a book value per share of \$0.83, which is \$0.15 greater than the \$0.68 book value per share as at April 2022.

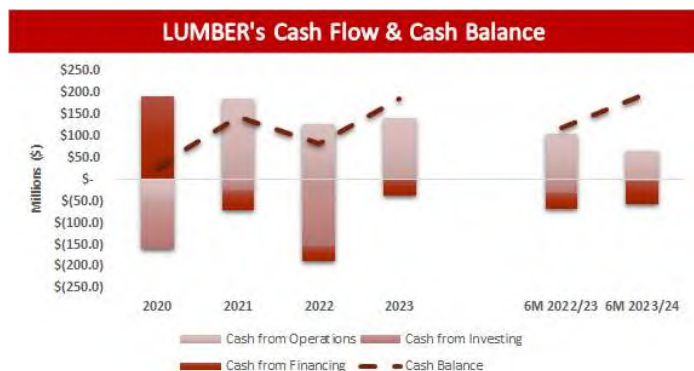


The company's current ratio for the period under review was 4.1x, an increase from a ratio of 2.8x in 2022. Lumber's quick ratio and cash ratio follow a similar trend, improving to 2.4x and 2.0x respectively. The average cash conversion cycle deteriorated, moving from 20 days to 29 days. This result was largely due to the decrease in average payable days outstanding from 35 days to 29 days. Moreover, average inventory days

outstanding increased from 46 days to 48 days, while average sale days outstanding remained constant year over year at 10 days.

Subsequently, the most recent 6M period saw the Company's total liabilities fell to \$95.72M (Q2FY2023: \$124.04M). As such, the company's liquidity position improved year over year, as current ratio stood at 4.4x, up from 2.6x and quick ratio improved to 2.5x from 1.3x. Moreover, cash ratio improved to 2.0x from 1.0x for the 6M period.

Cash Flow Statement Overview



LUMBER's cash from operating activities (CFO) represented inflows of \$139.33M for the twelve-month period, relative to inflows of \$127.95M in 2022. Notably, the changes in working capital moved from an outflow of \$61.12M in FY2022 to an outflow of \$5.54M in FY2023, a main driver to the improvement in working capital is the

cash used for inventories from an outflow of \$36.25M to an inflow of \$8.98M. Moreover, the company's accounts payable moved from an outflow of \$26.41M to an inflow of \$10.23M. For the six-month period October 2023, net operating cash flow amounted to an inflow of \$65.74M relative to an inflow of \$103.61M the prior year. Cash from investing activities represented an outflow of \$969.24K for FY2023, relative to an outflow of \$154.37M in FY2022. Notably, Lumber received interest in the amount of \$2.95M and utilized cash to purchase PPE, which amounted to \$3.92M. In the most recent six-month period, the Company's cash from investing activities represented an outflow \$5.02M relative to an outflow \$31.80M in FY2022/23. Cash from financing activities represented an outflow of \$36.72M for the period, relative to an outflow of \$33.43M in the 2022FY. This was driven by dividends paid amounting to \$36.72M. Subsequently, for the 6M period, the company's cash from financing activities experienced an outflow of \$50.85M, as the company paid dividends for the period. In FY2023, the company experienced a gain of \$101.63M to its cash balance.

Outlook & Valuation

The Jamaica economy is expected to expand based on the projected upward trends of various indicators such as, real GP growth. The World Bank estimated Jamaica's real GDP growth for 2024 and 2025 at 2.0% and 1.4% respectively. Furthermore, we expect income levels to remain buoyant as the domestic labour market is likely to remain solid over the next 12 to 18 months. The Jamaican market accounts for majority of LUMBER's revenues and as such, the company's prospects rely heavily on the performance of the local economy and its impact on employment and consumer disposable incomes. Moreover, with the continued recovery of the Jamaican

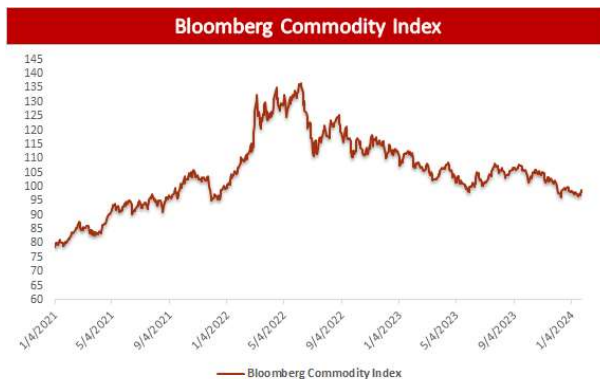
economy and the downward trajectory of the unemployment rate, declining to 4.5% as at July 2023, employment rates are expected to increase, which is likely to help to provide more disposable income to citizens and stimulate consumption, both of which augurs well for LUMBER's sales.

For the 2023FY, LUMBER highlighted challenges faced due to uncertain economic conditions, including high interest rates, challenges with the availability of certain key hardware items, which resulted in a slowdown of the Jamaican construction sector.

According to the Planning Institute of Jamaica (PIOJ), the Jamaican economy continued its recovery in Q3 2023 (July-September) recording a year over year increase of 1.9%. The goods producing sector recorded a 2.3% increase, while the services sector recorded a 1.8% increase. Notably, the Construction industry remained flat for the Q3 2023 period. This was due to an estimated contraction in the Building Construction component, particularly housing starts, which was counter balanced by growth in the Other Construction component, specifically, increased capital expenditure

on civil engineering activities. There was a 3.1% contraction in the sales of construction related inputs which supported the building construction division. This performance was driven by 66% downturn in total housing starts by National Housing Trust (NHT), relative to the corresponding quarter of 2022. Furthermore, the volume of mortgages and value of mortgages disbursed by NHT declined by 12.6% and 45.4% respectively. Nevertheless, the construction industry is poised for a turnaround, with signs indicating that the decline has reached its lowest point. We anticipate incremental growth in the upcoming quarters, driven by civil construction and ongoing government projects. The focus will likely be on constructing hotels and affordable to moderately priced housing projects. However, activities in higher-priced projects may be constrained by high-interest rates.

REAL VALUE ADDED IN THE GOODS PRODUCING INDUSTRIES (%)					
	Jul-Sep 2022	Oct-Dec 2022	Jan-Mar 2023	Apr-Jun 2023	Jul-Sep 2023
Goods Producing	5.4	4.7	1.0	2.6	2.3
Agriculture, Forestry & Fishing	16.3	5.9	-7.1	-8.1	-9.0
Mining & Quarrying	-27.2	99.0	114.1	164.2	102.0
Manufacturing	9.4	5.4	3.8	3.1	3.2
Construction	-3.1	-4.8	-4.2	-0.7	0.0
November 24, 2023 Planning Institute of Jamaica					



The World Bank anticipates that supply chain pressures should ease and are returning to historical averages amid rising inventories and falling shipping costs, while supplier delivery times are increasing at a slower pace. The World Bank further highlighted that despite the recent conflict in the Middle East, most commodity prices declined in 2023 due to moderating demand, but they remain above pre-pandemic levels. The Bloomberg commodity index fell 12.6% for

2023 and is expected to remain subdued. The World Bank noted that a key driver of the continued weakness in commodity prices in 2024 is weak global growth amid tight financial conditions. Lower commodity prices bode well for LUMBER's profitability margins, as cost of sales is likely to subside.

The BOJ decided to maintain the policy interest rate at 7.0% and continue to maintain relative stability in the foreign exchange market. The Bank noted however, that while interest rates in the money and capital markets had generally increased in line with the policy rate, the response of deposit-taking institutions (DTIs) in the relation to the interest rates on their products had been slow. As such, tightening of the monetary policy environment to contain inflation, is likely to translate to higher rates to finance housing developments and purchases, i.e. higher mortgage rates. This could possibly adversely impact LUMBER, which could see a further reduction or slowing of the growth rate at which the entity's products will be demanded. Essentially, a possibly subdued construction industry for the projected period is likely to continue have a corresponding effect on Lumber's revenue generation.

LUMBER has positioned itself to increase assets and the development of an additional off-site warehouse facility to capitalize on larger volumes of a wide range of imported products to meet consumer demand. Also, Lumber is in a favorable position to raise debt capital if desirable, to sustain operations and/or to meet strategic objectives to grow the business.

We are forecasting revenues of \$1.60B for the year ended April 2025, and net profits of \$136.5M, which corresponds to earnings per share (EPS) of \$0.19. We are forecasting a forward book value of \$800B as at April 30, 2025, which translates to a book value per share of \$1.13. We employed the price-multiples approach to determine the fair price for LUMBER. We utilized our projections for the Company's book value per share and earnings per share for FY2025 and applied the

harmonic mean price-to-book (P/B) and price-to-earnings (P/E) multiples of comparable firms (adjusted to account for historical discrepancies). The harmonic mean of the P/E of comparable listed companies gives a market multiple of 17.3x, which when applied to the forward EPS resulted in a target price of \$3.34, while the P/B for the peer group of 1.5x yields a price of \$1.73.

The 1-yr historical harmonic mean for the P/B ratio is 2.82x, which when applied to the forward BVPS yields a price of \$3.19. The 1-year historical harmonic mean for the P/E ratio is 11.0x, which when applied to the forward EPS yields a price of \$2.13. **The average of our price forecasts, \$2.60 is 3.4% above the closing price of \$2.51 on February 21, 2024.**

Company	Market Capitalization	Price to Earnings	Price to Book	Return on Equity	Return on Assets	Dividend Payout	Dividend Yield
CAC	581,935,484	28.5x	1.3x	4.6%	1.6%	22.1%	0.8%
DTL	8,704,052,486	14.1x	1.4x	9.7%	4.0%	0.0%	0.0%
EFRESH	1,170,000,000	24.3x	3.2x	13.3%	3.8%	0.0%	0.0%
FOSRICH	11,274,237,137	34.7x	6.3x	18.2%	6.4%	18.6%	0.5%
FTNA	13,280,854,390	20.3x	5.4x	26.8%	12.8%	19.1%	0.9%
INDIES	3,637,825,052	17.3x	3.0x	17.3%	9.5%	71.8%	4.2%
JETCON	484,305,000	31.4x	0.9x	2.8%	2.1%	0.0%	0.0%
LASD	14,393,881,078	10.6x	1.7x	16.1%	10.1%	23.3%	2.2%
MDS	713,157,895	8.9x	0.6x	6.7%	2.6%	29.5%	3.3%
Sector Average	6,026,694,280	17.3x	1.5x	12.8%	5.9%	27.0%	1.9%
LUMBER	1,765,593,750	12.2x	3.0x	45.9%	33.1%	34.4%	2.2%

Key Risks

The key risks to our earnings target are Lumber's ability to contain its cost of goods sold, and administrative expenses. Cost of goods sold can be impacted due to increasing cost of global commodities, as a result of demand outpacing supply, ongoing global supply chain issues and increasing transport cost. Lumber pays administrative expenses to BPOW based on the terms of a Corporate Service Agreement. The company pays for management, administrative, accounting and financial services. The Corporate Services Agreement was renewed effective May 1, 2021 and has a term of three years.

Recommendation

We are revising our recommendation on LUMBER to **UNDERWEIGHT**, given the near to medium term challenges. In addition, our recommendation considers the stability of LUMBER's earnings, operating cash flow and balance sheet strength. The company is positioned for growth, as there is currently little to no debt on its balance sheet. Nevertheless, the company is susceptible to economic conditions, such as the tightening of monetary policy conditions, which is likely to have an adverse effect on the construction industry from which majority of its revenue is generated.

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This stock is most suitable for investors with a medium to high risk appetite who are seeking capital appreciation. Given our outlook, the risk to our price target is the company releasing results which are below our expectations, which would lead to a decrease in investor demand for this stock.

Abridged Financials \$'000					SIX MONTHS		
	2021	2022	2023	Change	Oct-22	Oct-23	Change
Revenue	1,429,310	1,573,826	1,522,933	-3.2%	776,748	782,061	0.68%
Cost of Sales	(1,135,861)	(1,233,511)	(1,232,117)	-0.1%	(624,531)	(616,762)	-1.2%
Gross profit	293,449,587	340,314,266	290,815,534	-14.5%	152,217	165,299	8.6%
Profit before net finance costs and taxation	147,585	191,143	149,211	-21.9%	79,190	82,953	4.8%
Net Profit	144,990	183,889	145,174	-21.1%	78,201	86,732	10.9%
Total Assets	526,625	583,254	681,473	16.8%	644,264	718,802	11.6%
Total Liabilities	203,520	104,509	94,278	-9.8%	124,042	95,724	-22.8%
Total Shareholder's Equity	323,105	478,745	587,195	22.7%	520,221	623,078	19.8%
EPS (\$)	0.21	0.26	0.21		0.11	0.12	
Book Value per share (\$)	0.46	0.68	0.83		0.74	0.88	
Key Ratios							
Gross Profit margin	20.5%	21.6%	19.1%		19.6%	21.1%	
Operating Profit Margin	10.3%	12.1%	9.8%		10.2%	10.6%	
Net Profit margin	10.1%	11.7%	9.5%		10.1%	11.1%	
Return on Average Assets	32.2%	33.1%	23.0%		12.1%	12.1%	
Return on Average Equity	56.3%	45.9%	27.2%		15.0%	13.9%	
Current ratio (x)	2.29	2.80	4.13		2.62	4.39	
Quick ratio (x)	1.34	1.19	2.45		1.34	2.54	
Cash ratio (x)	1.03	0.79	1.96		0.95	2.03	
Debt/Equity (x)	-	-	-		-	-	

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

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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SELL—REDUCE EXPOSURE IN YOUR PORTFOLIO TO ZERO.

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