

29 August 2018

Consumer Cyclical | Restaurants

Japan Foods

Buy (Maintained)

Ground Checks: At Its Latest Ramen Restaurant

Target Price: SGD0.58
 Price: SGD0.49
 Market Cap: USD62.3m
 Bloomberg Ticker: JFOOD SP

Maintain BUY, TP of SGD0.58, 19% upside. The stock is trading at a discount relative to peers, which is unjustified, given its industry-leading yields, high gross profit margin and stable growth prospects from the launch of new franchise brands. We visited Japan Foods' new ramen franchise restaurant *Konjiki Hototogisu* and came back positive about the brand's potential for generating higher revenue per restaurant. We are also upbeat on the likelihood of it delivering net margins similar to other key brands. While this alleviates our concerns about its lower GPM, we do not expect the brand to make material revenue contributions amidst limitations on growth in the number of new restaurants.

Share Data

Avg Daily Turnover (SGD/USD) 0.008m/0.006m
 52-wk Price low/high (SGD) 0.53 - 0.4
 Free Float (%) 23.3
 Shares outstanding (m) 174
 Estimated Return 19%

Shareholders (%)

Kenichi Takahashi 66.0
 Wong Hin Sun 5.5
 Chan Chau Mui 4.7

Share Performance (%)

	YTD	1m	3m	6m	12m
Absolute	16.7	(4.9)	(3.9)	(2.0)	12.6
Relative	21.2	(2.5)	3.8	5.7	13.3

Source: Bloomberg

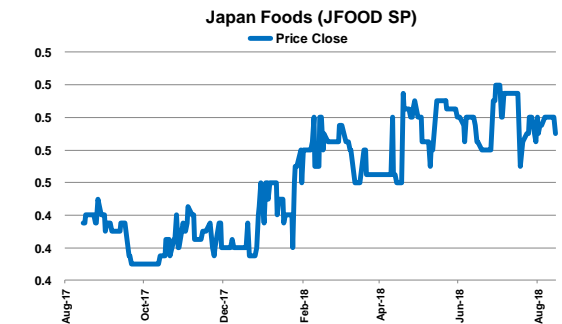
Konjiki Hototogisu operates in a small area, but in a unique location. Japan Foods usually looks for restaurant locations with an area of 2,000 sq ft or less. Average area of its *Ajisen Ramen* and *Menya Musashi* restaurants is between 1,000-1,800 sq ft. Its *Konjiki Hototogisu* restaurant is housed in a c.900 sq ft space. In contrast to other key brand restaurants, which are usually in key malls, *Konjiki Hototogisu* is located in CHIJMES, a historic complex with no direct access to a mall or MRT station. This implies higher foot traffic only for lunch/dinner during weekdays, and throughout the day on weekends.

Lower rental cost should compensate for higher material costs. The average monthly rental for Japan Foods' key restaurants is c.SGD25 psf. Given its unique location, the *Konjiki Hototogisu* restaurant should enjoy a lower rental rate of SGD18-22 psf (based on the Commercial Guru [website](#)). This translates into 10-30% lower rental cost, which, we believe, should compensate for higher material costs incurred by Japan Foods for premium ingredients used in making the Michelin Bib Gourmand ramen. While *Konjiki Hototogisu's* GPM may be lower than that of other brands, NPM should be similar.

Higher spend per person = higher revenue potential. Japan Foods indicated that the average spend per person for *Konjiki Hototogisu* is at SGD22-25. This is significantly higher than SGD15 for *Ajisen Ramen* and SGD17 for *Menya Musashi*. Although *Konjiki Hototogisu* seats only 35 people at any time – half of what other branded restaurants accommodate – the significantly higher spend per person implies that monthly revenue from *Konjiki Hototogisu* exceeds that of other brands. Assuming a seating capacity of 50 people, revenue from *Konjiki Hototogisu* could be 13-20% higher than other brands (Figure 2).

High revenue potential undermined by likely slow expansion. We believe the premium nature of the franchise brand, higher pricing and material costs along with need for suitable (low rental cost) locations imply the growth of the *Konjiki Hototogisu* restaurant network is limited. Unlike *Ajisen Ramen* and *Menya Musashi*, for which Japan Foods operates 18 and 10 restaurants, respectively, in Singapore, the group may only look at operating only 1-2 additional *Konjiki Hototogisu* outlets in the near term.

Key risks to our rating are rising labour costs and rental expenses, lower consumer spending and the non-renewal of franchise agreements.



Source: Bloomberg

Forecasts and Valuations	Mar-17	Mar-18	Mar-19F	Mar-20F	Mar-21F
Total turnover (SGDm)	65.5	67.8	70.7	73.7	76.9
Reported net profit (SGDm)	4.7	5.8	6.1	6.5	6.8
Recurring net profit (SGDm)	4.7	5.8	6.1	6.5	6.8
Recurring net profit growth (%)	23.3	24.0	5.2	6.8	4.4
Recurring EPS (SGD)	0.03	0.03	0.04	0.04	0.04
DPS (SGD)	0.02	0.02	0.02	0.02	0.02
Recurring P/E (x)	24.5	23.3	22.8	22.3	21.8
P/B (x)	2.7	2.5	2.3	2.2	2.0
P/CF (x)	7.2	8.1	7.3	6.8	6.3
Dividend Yield (%)	4.1	4.3	4.4	4.5	4.6
EV/EBITDA (x)	6.4	5.8	5.5	4.8	4.3
Return on average equity (%)	14.9	17.6	17.2	17.1	16.6
Net debt to equity (%)	net cash	net cash	net cash	net cash	net cash
Our vs consensus EPS (adjusted) (%)					

Source: Company data, RHB

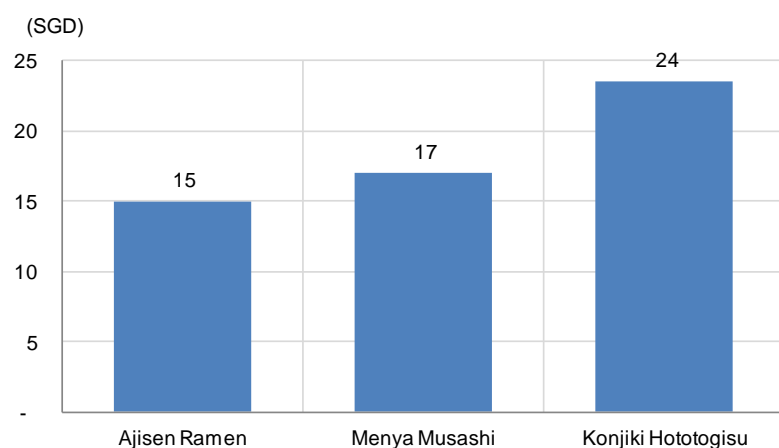
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Figure 1: Average spend per person across Japan Foods' key brands



Note: Konjiki Hototogisu data represents the average for the SGD22-25 range
Source: RHB, Company data

Figure 2: Konjiki Hototogisu offers high revenue potential

	Konjiki Hototogisu	Ajisen Ramen	Menya Musashi	Konjiki Hototogisu (potential)
Revenue per month (SGD)	120,000	124,074	131,667	148,500
Revenue per day (SGD)	4,000	4,136	4,389	4,950
Average seating per restaurant	35	65	65	50
Daily revenue per seat (SGD)	114	64	68	99
Avg. revenue per customer (SGD)	24	15	17	22
No. of seating per day	4.8	4.2	4.0	4.5

Source: RHB, Company data

Figure 3: Peer comparison

Company name	BBG ticker	Price (LCY)	M Cap (USD m)	Last year	P/E		EV/EBITDA		P/BV		D Yield 1FY	ROE 1FY
					Last	1FY	Last	1FY	Last	1FY		
BreadTalk	BREAD SP	1.01	418	Dec-17	26.0	33.7	7.6	8.2	3.21	3.61	2.0%	10.4%
Kimly Limited	KMLY SP	0.34	284	Sep-17	16.7	16.8	11.2	10.1	5.27	4.79	3.0%	28.6%
Jumbo	JUMBO SP	0.51	238	Sep-17	22.0	26.6	14.5	14.5	5.14	4.81	2.6%	18.3%
ABR Holdings	ABR SP	0.84	124	Dec-17	27.1	-	9.6	-	1.75	-	na	na
No Signboard	NSB SP	0.16	56	Sep-17	9.8	-	5.3	-	4.50	-	na	na
RE&S Holdings	RES SP	0.19	49	Jun-18	18.8	-	4.7	-	1.89	-	na	na
Tung Lok	TUNG SP	0.22	43	Mar-18	-	-	41.9	-	3.74	-	na	na
Katrina	KTG SP	0.20	33	Dec-17	45.6	-	10.5	-	3.20	-	na	na
Soup Restaurant	SOUP SP	0.16	34	Dec-17	23.4	-	10.2	-	4.58	-	na	na
Sakae Holdings	SAKAE SP	0.19	19	Dec-17	27.5	-	21.3	-	0.78	-	na	na
Average			1,299		22.7	26.8	11.1	10.4	3.90	4.27	1.8%	12.9%
Japan Foods	JFOOD SP	0.49	63	Mar-18	18.3	14.7	5.9	5.6	2.68	2.50	4.3%	17.6%

Note: Prices as at 28 Aug 2018
Source: RHB, Company data

Figure 4: The new restaurant is located at a small corner of CHIJMES building



Source: RHB

Figure 5: New Konjiki Hototogisu restaurant seats only 35



Source: RHB

Figure 6: The Tonkotsu Spicy Ramen, which does not contain MSG



Source: RHB

Figure 7: The signature Shoyu Hamaguri Soup Ramen includes triple soup made using Hamaguri clams, pork bone and Japanese broth



Source: RHB

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