Stock Analysis: Lasco Manufacturing Limited (LASM)

Moniker: LASM

Shares Outstanding: 4,087,130,170 units

Market Value of Shares Outstanding: $6,416,794,367

Financial Year End: March 31

Executive Summary

Lasco Manufacturing Limited (LASM) is a member of the Lasco Affiliated Group of Companies. The main activities of the company are to manufacture and export soy based products and to package milk based products. Throughout the past 5 years, the company has maintained a profitable position. In 2013, the company’s Revenue increased to $3,659M from $172M in 2010. For the period 2010 – 2012, the company’s Net Income grew by over 400%. With the construction of a new Manufacturing Plant, we expect production to be more efficient and the company’s product portfolio to expand resulting in an increase in revenue and decreases in expenses.

LASM’s stock is liquid and its price continues to increase over time. The stock is currently underpriced and we recommend a BUY as this stock could be a good investment in the long run.

Company Overview

Lasco Manufacturing Limited was incorporated in October 1994 and was listed on the Jamaica Stock Exchange’s Junior Market in October 2010. The company consists of two divisions; Manufacturing and Export. It packages milk based products and manufactures a variety of soy-based products. These products are distributed locally through its affiliated company, Lasco Distributors Limited and its soy based products are exported across the world.

Lasco products are exported to some 20 markets throughout the Caribbean, Central and South America, Canada, United Kingdom, Middle East and the United States of America.

As a part of its long-term strategic plan, Lasco Manufacturing Limited commenced construction of a new plant in January 2012 which is expected to be completed in September 2013. When completed, there is expected to be increased productivity and an expansion in its product portfolio.

The Managing Director of Lasco Manufacturing Limited is Dr. Eileen Chin. She has been working with the Lasco Affiliated Group of Companies since 1999 and specifically with Lasco Manufacturing Limited since 2007.

Company Outlook

The Outlook for LASM is positive. Once the Manufacturing Plant is available for use, we expect production to be more efficient and for the company’s product portfolio to increase. The company also has plans to increase its market reach and has embarked on a brand awareness campaign. Additionally, LASM is taking steps to improve accountability within the organization. With all these efforts, we expect the company to increase Revenues while decreasing Operating Expenses and improve its Profits.

Projections and Valuation

Using the Dividend Discount Model, LASM has a fundamental value of $4.16. Currently, the stock is undervalued.

---

1 As at July 29, 2013
2 As at July 29, 2013
3 Percentage Change

---
Stock Analysis: Lasco Manufacturing Limited (LASM)

Dividends – Payments and Policy

Ordinary Shares

Dividend Timetable | 2011 | 2012 |
--- | --- | --- |
Payment date | August 15 | September 28 |
Dividend Per Share (J$) | 0.15 | 0.14 |

The company’s Dividend Policy is to pay no less than 15% of Net Profit as annual dividends subject to the company’s need for reinvestment of some or all of its Profits in order to finance its growth and development. LASM has a dividend yield of 8.28%. In 2011, the company paid 15% of the 2011 Net Profit as dividends while in 2012, 10% of Net Profit was paid as dividends. The company is retaining its earning to help with the construction of its new facilities. If a dividend payment is made in 2013, it could also be lower than that paid 2012. However, as the plant becomes available for use, we expect dividends to increase.

Management and Corporate Governance

The Managing Director of Lasco Manufacturing Limited is Dr. Eileen Chin. Dr. Chin holds a post-graduate degree in Medicine and a MBA in Global Management. She has knowledge and skills in advanced negotiation and risk management. Assisting her is Financial Accountant, Paul Darby and Company Secretary, Vincent Chin.

The Board of Directors of Lasco Manufacturing Limited comprises of experienced professionals with knowledge from different professions. The experience and talent of these individuals should help to guide the company into successful endeavors. The Board consists of 5 Directors, 3 Executive and 2 Independent. This does not comply with the PSOJ Corporate Code of Conduct which states that at least two-thirds (66%) of the board should be independent. Currently, only 40% of the Directors are independent.

### Directors

<table>
<thead>
<tr>
<th>Directors</th>
<th>Experience</th>
</tr>
</thead>
<tbody>
<tr>
<td>Hon. Lascelles Chin O.J., C.D. (Executive Chairman)</td>
<td>Chairman and Founder – Lasco Affiliated Companies; Director – University of the West Indies School of Nursing Advisory Board, Kings House Foundation</td>
</tr>
<tr>
<td>Dr. Eileen Chin MBA. (Managing Director)</td>
<td>Board Member – Lasco Distributors Ltd. and Lasco Financial Services Limited</td>
</tr>
<tr>
<td>Professor Rosalea Hamilton Ph.D</td>
<td>Vice President of Development – University of Technology Jamaica</td>
</tr>
<tr>
<td>J.A. Lester Spaulding C.D., J.P.</td>
<td>Non-executive Director of the Board of Directors – RJR Communications Group</td>
</tr>
<tr>
<td>Vincent Anthony Chen</td>
<td>Appointed as director on June 20, 2013, Company Secretary(LASM)</td>
</tr>
</tbody>
</table>

The Board of Directors is ultimately responsible for ensuring accountability and transparency within the company. The Board has established two sub-committees, the Audit & Compliance Committee and the Compensation Committee. The Audit and Compliance Committee, chaired by Mr. J.A. Lester Spaulding, ensures good fiscal discipline, open and accurate financial reporting and timely disclosures. The Compensation Committee, chaired by Prof. Rosalea Hamilton, evaluates the performance of the Executive Chairman and Managing Director. However, the company fails to comply with the PSOJ Corporate Governance Code, which states that, in addition to an Audit Committee and a Remuneration/Compensation committee, companies should have a Nomination Committee that is responsible for election and re-election of directors.

### Top 10 Shareholders

<table>
<thead>
<tr>
<th>Shareholder</th>
<th>Number of Units Held</th>
<th>Percentage Held (%)</th>
</tr>
</thead>
<tbody>
<tr>
<td>East West (St. Lucia) Limited</td>
<td>200,269,378</td>
<td>49.00</td>
</tr>
<tr>
<td>Lascelles Chin</td>
<td>124,442,847</td>
<td>30.45</td>
</tr>
<tr>
<td>Mayberry West Indies Limited</td>
<td>12,750,106</td>
<td>3.12</td>
</tr>
<tr>
<td>Mayberry Managed Clients Accounts</td>
<td>3,222,316</td>
<td>0.79</td>
</tr>
<tr>
<td>Joel Izquierdo Gonzalez</td>
<td>3,008,340</td>
<td>0.74</td>
</tr>
<tr>
<td>Catherine Adella Peart</td>
<td>2,500,000</td>
<td>0.61</td>
</tr>
<tr>
<td>Bamboo Group Holdings Limited</td>
<td>2,361,084</td>
<td>0.58</td>
</tr>
<tr>
<td>Liudmila Gonzalez Diaz</td>
<td>2,235,000</td>
<td>0.55</td>
</tr>
<tr>
<td>Huixiong Liao</td>
<td>2,213,383</td>
<td>0.54</td>
</tr>
<tr>
<td>Hilda Gonzalez Rosales</td>
<td>2,100,000</td>
<td>0.51</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td>355,102,454</td>
<td>86.89</td>
</tr>
</tbody>
</table>

---

4 As at June 30, 2013
Stock Analysis: Lasco Manufacturing Limited (LASM)

SWOT Analysis

**Strengths**
- Wide market reach and strong distribution network through affiliated company Lasco Distributors Limited.
- Customer base extends overseas.
- Company maintains a profitable position.
- Company is in the process of expansion with the construction of the new plant.

**Weaknesses**
- Exposed to adverse effects of fluctuations in the foreign exchange rate as the majority of its transactions are in foreign currency and could affect pricing.

**Opportunities**
- Building of new factory may increase efficiency and revenues.
- Plans to expand its market reach into new markets across the world.

**Threats**
- High competition from other companies such as GraceKennedy.
- Challenging local economic environment.

Financial Analysis

**Revenues:** In August 2010, Lasco Food (Successors) Limited acquired the business of Lasco Foods Limited. The name was then changed to Lasco Manufacturing Limited. Upon the merger, Revenues increased from $172M to $2,969M. Since then, it continued to increase by 11% p.a. on average. With the pending completion of the new manufacturing facility, and the company’s plans to expand its market reach, we expect revenues to continue to increase. During the April – June period, revenues increased by 0.88% in 2013 over the same period in the previous year.

Cost of Sales have also increased year on year by 13% p.a. on average. On the other hand, Other Operating Income has decreased year on year, due to consistent decreases in Interest Income and Management Fees. On average, Other Operating Income has decreased by 52% p.a.

**Expenses:** Once the businesses merged in 2010, it experienced a 604% increase in Operating Expenses, from $60.6M to $426.57M. In 2012, it decreased by 9% but began to increase again in 2013 due to the company spending time and money improving its Change Management Program to get employees comfortable with its new operations. During the first quarter of 2013/14, Operating Expenses increased by 17.3% compared to the first quarter of 2012/13.

Compared to other companies in this industry, LASM does not spend a significant amount on promotions. Selling and Promotions Expenses decreased year on year, by 27% in 2012 and 0.5% in 2013. The company outsources its marketing services to Lasco Distributors Limited. However, this cost could increase in the near future as the company embarks on a brand awareness campaign.
Stock Analysis: Lasco Manufacturing Limited (LASM)

**Balance Sheet**: Some of the proceeds from the IPO in 2010 were used to pay off debts. Therefore, in 2011, Liabilities decreased by 41.78%. This figure declined even further in 2012 by 14%. However, to finance the construction of the manufacturing plant, a loan worth $1,005.855M was obtained from First Caribbean International Bank (Jamaica) Limited. This increased Total Liabilities by 197% and this loan is expected to be repaid over 5 years.

Total Assets have increased over the past few years. This was mainly due to additions in Property, Plant and Equipment. Between 2010 and 2011, there were additions of Land and Building from the merger, which caused a 35% increase in Property, Plant and Equipment and a 19% increase in Total Assets. Beginning in 2012, the Property, Plant and Equipment figure includes Assets under Construction which reflects costs incurred from the construction of the Manufacturing Plant. In 2012, Assets Under Construction amounted to $796M and $1,708M in 2013. Total Assets increased by 34% in 2012 and 80% in 2013. When compared to the first quarter of 2012, Total Assets increased by 44% in the first quarter of 2013. Estimated cost for the completion of the plant is $400M. Once the plant is completed and available for use, these costs will be depreciated.

Also contributing to the significant increase in 2013 was investments in short term US$ deposits which amounted to $68M and have a tenure of one year.

As the company pursues its expansion plans, Retained Earnings increased year on year, which increased the Shareholders Equity. In 2012, Retained Earnings increased by 101% over the previous year and increased further by 55% in 2013. During the April – June period in 2013, Retained Earnings increased by 55% when compared to the same period in 2012.

**Cash Flow**: Cash provided by Operating Activities has increased year on year with a significant increase in 2012. However, this was offset by increases in Investing Activities. Net cash used for investing activities has increased year on year for the past 4 years due to the company investing in the construction of its Manufacturing Plant. Between 2010 and 2012, cash used in Financing activities has increased steadily but the company received cash from its Financing Activities in 2013 from the procurement of a long term loan. LASM has also been making use of an overdraft facility provided by its banker which decreased its Cash balance even further.

All these activities have caused a decrease in Cash and Cash Equivalents over the past few years. From 2010, Cash and Cash Equivalents fell year on year until it reached a negative position in 2012 due to increased use of the bank overdraft facility. However, the company took steps to improve this and increased its Cash and Cash Equivalents balance in 2013. During the first quarter of 2013, Cash increased by 8%.

**Ratio Analysis**

**Financial Health**: The company’s debt to equity position (a measure of the degree of financial leverage) decreased in 2011 due to a decrease in debt. Long term debt was paid off with the proceeds from the IPO. The decrease in the ratio was also affected by an increase in Equity, due to an over 200% increase in Retained Earnings. The ratio fell in 2011 and further in 2012. However, the ratio increased in 2013 due to procurement of the loan from First Caribbean International Bank. This loan should be paid off over 5 years. During the first quarter of 2013/14, this ratio increased by 45% to 0.64x. We expect the debt/equity ratio to remain below 1x equity for the foreseeable future, indicating that the company is managing its debt well and its creditors have less money invested in the company than its shareholders.
Stock Analysis: Lasco Manufacturing Limited (LASM)

**Liquidity:** Over the past 4 years, the current ratio of the company has fluctuated, remaining between 1.5x and 2.8x. Hence, the company continues to be in a position to adequately cover its short term expenses with its current assets. In 2012, the ratio fell by 25% due to a significant decrease in Cash and Cash Equivalents. However, the company recovered in 2013. During the first quarter of 2013/14, the current ratio increased by 26% to 3.2x. We expect that as the new manufacturing plant is available for use, the company’s Receivables will increase, ergo, increasing the Current Ratio.

**Profitability:** The company has maintained a profitable position over the past four years. Operating Profit and Net Profit have increased year on year. However, both Operating Profit Margin (OPM) and Net Profit Margin (NPM) fell in 2011 due to a greater increase in Net Sales than in Operating and Net Profit. Net Sales increased by over 400% while Operating and Net Profit only increased by approx. 200% each. The company’s Operating Expenses increased significantly in 2011 and so did its Finance Costs. However, the company took steps to contain these costs subsequently, resulting in the OPM and NPM increasing in 2012 and 2013, remaining between 61% and 65%. With the construction of the Manufacturing Plant, we expect revenues to continue to increase while operating expenses remain steady, which should increase profit obtained from each dollar of sales.

Return on Equity (ROE) has decreased year on year. Shareholder’s Equity has increased more rapidly than Net Profit. On average, Net Profit increased by 28% p.a. while Equity increased by 76% p.a. This was due to significant increases in Retained Earnings over the past three years which can be used to facilitate the financing of the company’s expansion. However, as the company’s expansion is completed, we expect ROE to increase and, when compared to the other companies in the market, LASM’s ROE is high.

Return on Assets (ROA) increased between 2011 and 2012 but decreased between 2012 and 2013. This was due to the significant increase in Total Assets, the addition of costs incurred from the construction of the Manufacturing Plant. Average Total Assets increased greatly by 61% in 2013 compared to the 27% increase in 2012. Again, as the new plant is available for use, we expect Total Assets and Profit to increase even further.
Stock Analysis: Lasco Manufacturing Limited (LASM)

Price Movement

Upon listing on the Junior Market in October 2010, the shares were listed at an IPO price of $2.50. Since then, the share price has escalated, trading as low as $2.50 and as high as $16.30. With the escalated price, the company declared a 10:1 stock split in July 2013 to make the stock more affordable for smaller investors. The stock then traded at $1.63 and has since traded as high as $1.77. Also, with the stock split, the number of share outstanding increased from 408.713 million to 4,087.130 million.

Since the company listed on the Junior Market, the stock has been fairly liquid. Volumes are high when compared to other companies in the market and, year to date, the stock price has increased by 55%. However, upon the publishing of the company’s first quarter results, the stock price fell by 7%, likely due to a fall in Net Profit. Nevertheless, the company is still in the process of expansion and investors may regain confidence in the stock as the manufacturing plant is completed.

Projections and Valuation

Lasco Manufacturing Limited is a growing company which pays dividends annually. Therefore, we believe that the Dividend Discount Model is appropriate for valuing LASM. The Cost of Equity of 11.67% was calculated using the Capital Asset Pricing Model and includes a Country Risk Premium and Equity Risk Premium. We assumed that dividends would decrease by 3% in 2013/14 but increase by 10% thereafter. Using these assumptions, the stock has a target value of $4.16.

Currently, the stock is undervalued. Although the P/E of 10.76x and P/BV of 3.56x is high when compared to the market, the price is justified by the company’s expansion plans and future prospects.

<table>
<thead>
<tr>
<th>Beta</th>
<th>Expected Market Return</th>
<th>Equity Risk Premium</th>
<th>Country Risk Premium</th>
<th>Risk Free Rate</th>
</tr>
</thead>
<tbody>
<tr>
<td>0.111</td>
<td>10.013</td>
<td>0.828</td>
<td>7.445</td>
<td>2.568</td>
</tr>
</tbody>
</table>
Stock Analysis: Lasco Manufacturing Limited (LASM)

Company Outlook

The company is currently completing the construction of a new manufacturing plant. The plant is expected to be completed by the end of September 2013 and, once available for use, we expect that efficiency in the production process will improve. This should decrease Operating Expenses while increasing Revenue as production is increased. This new plant can also facilitate the expansion of the company’s product portfolio. This includes the addition of a bottling operation to facilitate the production of Lasco beverages as well as other products. The company plans on introducing three new products upon the completion of its plant expansion. This will expand the company’s product portfolio and could expand its market reach. This plant is expected to provide 250 new jobs and could ultimately improve the profitability of the company.

LASM also has plans to enter new markets. The company plans on partnering with experienced distributors across the world which could help in market penetration and distributing the Lasco brand even further. These efforts could increase Revenue.

Lasco Manufacturing is currently embarking on a brand awareness campaign which began earlier this year with the “Lasco Food Drink Mega-Million Funanza” where loyal customers were rewarded. The company is planning to continue this campaign in an effort to increase brand visibility and increase profits.

The company has been undergoing a Change Management process. This is being done in an effort to increase accountability and efficiency within the organization. Management hopes that through this process, risks associated with the operation of the company will be properly managed ensuring the continuity and profitability of the company.

The state of the local and global economy has made operating difficult for companies such as LASM. The Jamaican economy may continue to experience low growth. Hence, the company is taking steps to improve its risk management and to strengthen its export division. This is in an effort to mitigate risks associated with the challenging local economy and improve profits.

Recommendation

BUY: LASM continues to maintain a profitable position. Revenue increases paired with decreases in Operating Expenses are expected as the company completes the construction of a new manufacturing plant. The stock is currently underpriced and is increasing. We expect the company to do well once the Plant is complete and available for use. Hence, we recommend a BUY at this time as this may be a good investment in the long run.

Prepared by VMWM Research Department August 9, 2013

Disclaimer: This Research Paper is for information purposes only. The information stated herein may reflect the opinion and views of VM Wealth Management in relation to market conditions and does not constitute any representation or warranties in relation to investment returns and the credibility of the sources of information relied upon in the preparation of this report, without further research and verification. Before making any investment decision, please consult a VM Wealth Management Advisor.