Company Analysis: Mailpac Group Limited (MAILPAC)

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- Recommendation: MARKETWEIGHT
- Price Target: $1.58
- Current Price: $1.64

- Shares Outstanding: 2,500,000,000 units
- Financial Year End: December 31

ABOUT THE COMPANY

Mailpac Group Limited (MailPac) which was incorporated on September 30, 2019, is the group that has acquired the assets, liabilities and debt of Mailpac Services Limited and Mailpac Local Limited. The purpose of the reorganization was to amalgamate both ecommerce platforms into one efficient operating business.

Consequently, Mailpac Group Limited became one of the leading providers of logistics services in the Caribbean with a wide range of services. The Company offers ecommerce fulfilment services from the United States to Jamaica (Mailpac Services), cross-border online shopping with local landed prices (Mailpac Marketplace), local online shopping and delivery from local retailers (Mailpac Local), online shopping financing (Mailpac Financial Services), sea freight shipping (Mailpac Ocean Freight) and brokerage services. The company is also in the process of launching a branded MasterCard.

FINANCIAL PERFORMANCE

(JMD '000)	2018	2019	2020 (P)	2021(P)
Revenue	969,240	1,213,163	1,152,505	1,267,755
Gross Profit	519,407	638,289	530,152	697,256
Net Income	213,145	289,421	196,980	335,947
Total Assets	204,336	444,844	511,571	639,463
Total Liabilities	116,014	91,203	100,324	108,349
Total Equity	88,322	353,640	411,247	531,114

Dividend Policy

The directors intend to pursue a dividend policy that projects an annual dividend of up to 75% of net profits available for distribution, subject to the need for reinvestment in the Company from time to time.

Outlook

The e-commerce industry, especially in emerging markets, has a lot of room in which it can develop, moving closer to levels more common in developed countries. However, the unprecedented impact of the COVID-19 pandemic continues to threaten supply chains and how businesses operate, all of which add to the COVID-19 impact on ecommerce. Across industries, storefronts have been shuttered and sales have declined. As the pandemic continues businesses should continue to weather the storm by pursuing models that could help them mitigate possible damages by the coronavirus pandemic.

Projections and Valuations

We used an average of the market P/E method and Discounted Cash Flow (DCF) model to establish a price target for MailPac. The DCF model assumed a medium-term growth rate of 10% for revenues and slight improvement in profitability margins. The discount rate used was 15.50% along with a long-term growth rate of 5%. A justified P/E of 13.25x was applied to our projected FY 2021 EPS of $0.13.

Risks to Price Target

If the Jamaican e-commerce industry does not increase its penetration levels, then the expected revenue growth for MailPac may not be realized, which will ultimately prompt a reassessment of our long-term expectations for profitability going forward. Also, if the current pandemic persists for more than a year then our projection may have to revisited.

FINANCIAL PERFORMANCE

(JMD '000)	2018	2019[1]	2020(P)	2021 (P)
Revenues	969,240	1,213,163	1,152,504	1,267,755
Cost of Sales	449,833	574,874	622,353	570,490
Gross Profit	519,407	638,289	530,152	697,265
Net Income	213,145	289,421	196,979	335,947
Total Assets	204,336	444,844	511,571	639,463
Earnings Per Share	$0.09	$0.12	$0.08	$0.13
Net Income Margin	21.99%	23.85%	17.09%	26.34%

For the financial year ended December 31st, 2019, company revenues which represents both local and international mail and courier services, grew by 25.2% to $1.21 billion compared to the $969.24 million reported a year prior. Cost of Sales for reporting period was J$574.8 million which up 125 million or 27.8% due to an increase in freight and brokerage cost. Gross Profit for the period totalled $638.30 million which represents a 22.9% increase on the comparable period prior. Administrative and General Expenses made up the lion's share (87.2%) of total expenses at $296.97 million which is $19.6 million more than the $277.41 million recorded on December 31st ,2018.

Total expenses for the financial year was $340.51 million which resulted in an operating income of $297.78 million. This resulted in an operating margin 24.5% which was 260 basis points more than last year (21.9%) which shows that company is improving its operational efficiency. Other Income ($18.34 million) and Finance Cost ($16.21 million) contributed to a Profit before Tax of J$316.12 million which is 47.8% more than what was recorded the entire FY 2018 (December 31, 2018: $213.94 million). Taxes of $10.49 million resulted in a NPAT of J$289.42 million (EPS: $0.09) which is 35.8% more than the 2018 net income of $213.94 million (EPS: $0.12).

Total Assets for the period ending December 31, 2019 more than doubled to $444.84 million (December 31st, 2018: $204.34 million). Of this Current Asset accounted for 35% ($155.62 million) and Non-Current Assets make up the remaining 65% ($289.22 million). Current Assets grew by 52.5% driven by a higher cash balances while Non-Current Assets increased by 183.0% driven by growth in Intangible Assets, which for the most part represents Goodwill generated from the acquisition of Mailpac Services Limited and Mailpac Local Limited.

Total Liabilities for the period was J$91.20 million which represents a 21.4% decline over the $116.04 million recorded last year. This decline was driven by reduction in a loan due to parent company which was paid with proceeds from the IPO during December 2019.

Shareholder's equity rose to $353.64 million (BVPS: $0.14) as at December 31, 2019 from $88.3 million (BVPS: $0.14) due to growth in share capital following the company's IPO.

[1] Calculated based on the performance of Mailpac Services Limited and Mailpac Local Limited up to September 2019 plus the performance of Mailpac Group limited for the December quarter.

The current and cash ratios both declined from 2.77x and 1.60x to 1.85x and 1.26x. Despite the decline, this still represents healthy levels and implies that short-term obligations can be covered from cash. The company used some of the proceeds of the sale of the IPO to liquidate its existing long-term debt obligations at the time, reducing overall leverage. It is importance to note that the company has no interesting bearing debt, with the remaining debt representing a loan from the parent company expected to mature on March 30, 2020 which will leave the company virtually debt free.

OUTLOOK

Mailpac exists in an increasingly competitive industry and therefore will need to offer unique products to suit their customer's needs and convenience. Their growth will be driven by ecommerce penetration in the country which is currently at about 4%-6%. By adding additional delivery points and a broader delivery network, MailPac expects to continue taking market share, which it has been doing for the past two years.

COVID-19 Impact on Ecommerce

Due to social distancing and stay home policies, the COVID-19 impact on ecommerce saw an initial spike in sales. With foot traffic significantly declining, sales spiked as consumers started going online to buy and have goods delivered to their homes. This prompted a new agreement between MailPac and PriceSmart, to stock their products on its website. This is familiar territory for MailPac, as the company built its customer base by delivering goods bought on its website from other local providers such as Hi-Lo and Stationary Centre. We expect that this will drive an uptick in growth in the Mailpac Local operation, but weaker performance in the Mailpac Services operation for an overall decline in revenue in 2020.

New Financing Options Will Appeal to an Untapped Portion of the Market

MailPac plans to offer new financing options for their customers. They will be providing captive financing through an exclusive online portal which will allow for the instant adjudication of loans. A beta for this service was launched in 2018 and has approve 43 loans thus far with no default. The service is expected to formally launch in 2020. In addition, Mailpac will be launching their own Mastercard. This Mastercard will be prepaid in nature allowing users to top up their card whenever they would like to make an online purchase. This will capture a significant amount of unbanked and underbanked customers who would like the opportunity to purchase products online but do not have the tools to do so.

Technological solutions will help to keep costs low

MailPac will continue to benefit from market-leading technological solutions and economies of scale provided through the company's partnership with Aeropost, the largest ecommerce logistics provider in the region. Cost of air freights have also decline which may see a shift of transportation services from sea to air which will drive costs down as well as allow for faster shipping services.

Growth in the E-commerce industry

We expect overall growth in E-commerce to be accelerated by the COVID-19 pandemic, as more persons become familiar with online transactions and shopping as social distancing restrictions create physical limitations. Additionally, as internet penetration continues to increase, there is likely to be an acceleration in the growth of the E-commerce market from 4-6% to potentially 10% percent over the next five years. This may create a feedback loop whereby the demand for E-commerce solutions accelerates as it becomes more available. However, this will be dependent on the pace of the economic recovery post-COVID-19.

MailPac will now be exposed to credit risks

With the launch of the new loans service, MailPac will now be open to these risks the main on being the risk of default. There will also be financial risks associated with launch of the Mailpac Mastercard.

INVESTMENT POSITIVES

- The diversity of the company's services will help to grow their existing customer base.
- The company has a large capacity to grow.
- The company is virtually debt free with no tax obligations which should increase company earnings in the to medium-term until the Junior market benefit expires.
- Mailpac has an experienced leadership team.
- The industry has many competitors with fragmented service offerings. Mailpac is well positioned to execute on acquisition opportunities that may arise.
- The business has fairly low capital expenditure needs to maintain its operation

INVESTMENT NEGATIVES

- Exists in a highly competitive industry with a low barrier to entry.
- Growth may be dampened by industry regulations or inadequate framework.
- The Mailpac Services Division is fairly exposed to economic downturns.

CONCLUSION

As the World has embraced social distancing to slow the spread of the pandemic, there has naturally been a decline in brick-and-mortar shopping. This should likely lead to an increase in in the prevalence of E-commerce as people purchase items online that they might have otherwise purchased in person.

Beyond the short-term effects of the COVID-19 pandemic we expect Mailpac to benefit from growth in both internet penetration and E-commerce utilization. Furthermore, the company maintains a sound liquidity position and is free of leverage. Additionally, the company has a comprehensive service offering relative to their competition. These factors position the company well to execute on any potential acquisition opportunities. Given the factors above and our assessment of the valuation of the company at $1.58 relative to the offer price of $1.65, we recommend MailPac as **MARKETWEIGHT.**

SOURCES

The Jamaica Observer, MailPac Group Limited Pospectus, MailPac Audited Financials, Jamaica Stock Exchange, Loop News

DISCLAIMER

DEFINITIONS

- **OVERWEIGHT** – More than 10% price appreciation anticipated (Higher weight in your portfolio relative to the market)
- **MARKET WEIGHT** – Price expected to fluctuate between 10% on the upside or downside (Similar weight in your portfolio relative to the market)
- **UNDER WEIGHT** – Price expected to decline by more than 10% (Lower weight in your portfolio relative to the market)
- **ZERO WEIGHT –** Do not hold this stock