

Market Guide

THIS ISSUE

Assessing the Margins of the Junior Market
Manufacturing and Distribution Stocks

Foreign Exchange Market Summary

Money Market Update

Stock Recommendations

"In the long run, it's not just how much money you make that will determine your future prosperity. It's how much of that money you put to work by saving it and investing it." ~ Peter Lynch

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Assessing the Margins of the Junior Market Manufacturing and Distribution Stocks

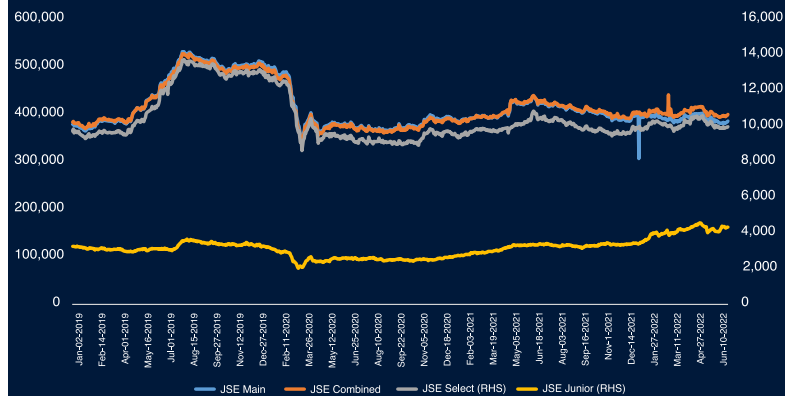
Global input prices, which increased as the world economy began to recover in 2021, have risen further since the start of the year due to the impact of geopolitical tensions on commodity prices, and the re-implementation of strict COVID-19 restrictions in China following a fresh outbreak. Notably, Bloomberg's commodity price index increased by 27.1% between December 2020 and December 2021. Shipping prices have also remained elevated with the Baltic Dry Index, which tracks shipping prices for raw materials, rising over 62.3% over the same period. Russia's invasion of Ukraine has added another headwind, which along with drought conditions in key commodity producers, has led to a historic rise in global commodity prices. Owing to these additional developments in 2022, based on Bloomberg's commodity price index, prices have risen by 18.2% from the start of the year to July 1, 2022. Though there has been a slight decline of 0.14% in the Baltic Dry Index in the year-to- July 1, 2022, which indicates a slight ease in shipping costs, these costs are still at elevated levels. These high and volatile commodity prices and shipping costs pose significant risks to the global and local economies and the financial markets. For local companies,

specifically those engaged in manufacturing and distribution, commodities are a key input into the production process, and shipping cost is an essential expense incurred to produce goods. Rising costs can compress margins and reduce their profitability, if they are unable to pass the higher costs on to consumers. Here we examine how these developments have affected the listed manufacturing and distribution firms on the Junior Market. By assessing profitability metrics such as the gross profit margin¹ and operating profit margin², it was found that most companies within the sector have witnessed an improvement in both their gross and operating profit margins since the beginning of the pandemic, fuelled by a mixture of revenue growth and cost management efforts. At the end of 2021, out of the 23 companies assessed, 18 had exceeded their pre-pandemic gross margin levels, while 15 had surpassed their 2019 operating margin levels. This was also reflected in the average operating profit margin which fell in 2020 due to a large fall in a few companies, and recovered in 2021 with the global and local economic rebound. Year-to-date, owing to higher inflation and other company

¹ The gross profit margin is a metric used to assess a firm's financial health and is equal to revenue less cost of goods sold as a percent of total revenue.

² The operating margin measures how much profit a company makes on a dollar of sales after paying for variable costs of production, such as wages and raw materials, but before paying interest or tax.

WEEKLY MOVEMENT IN INDICES



MOVEMENT IN INDICES

JSE Indices	Closing Levels	Weekly Change	YTD % change
Combined Index	400,219.74	+ 4,335.10	-0.2%
Main Market Index	386,327.32	+ 5,140.49	-2.5%
Select Index	9,974.89	+ 97.59	0.9%
Junior Market Index	4,337.03	- 52.44	26.5%

WINNERS & LOSERS (FOR THE WEEK ENDED JULY 4, 2022)

	\$ Change	% Change
ICREATE	+\$0.88	+26.75%
PULS	+\$0.78	+21.67%
CBNY	-\$0.94	-59.12%
MTL	-\$5.00	-23.26%

MARKET OVERVIEW

Last week, seven indices advanced while two declined. Across the indices 63 stocks appreciated in price, 47 declined and 9 traded firm. The Junior Market sustained the largest decline week-over-week, with the strongest performance delivered by the Main Market index. Barita Investments Ltd. and Wigton led the advancers and were two of the volume leaders in the overall market, behind Dolla Financial Services. Despite last week's gains, the Main Market has declined by 2.5% year to date as the more heavily weighted financial sector stocks have had a much slower recovery from their pandemic falloff. The sector's challenges is also being compounded by rising inflation which is weakening consumer disposable incomes and rising interest rates which are raising borrowing costs for consumers, which could reduce loan demand for banks and weigh on margins for securities dealers.

specific factors, we have seen a falloff in the gross margins of most companies (15 out of 23); however the industry average remains relatively stable. The same cannot be said for the operating margin of most companies which has largely continued to increase (15 out of 23 companies) with signs of weakening in a few companies. Overall, we do expect that margins for more companies will come under pressure in the coming quarters due to the high-cost environment and its impact on both consumer demand and direct and indirect costs.

Table 1 below shows the average gross and operating profit margin for the Junior Market Manufacturing and Distribution sector over the last three years, as well as year-to-date figures. Both margins dipped in 2020, due to the effects of the pandemic, but it should be noted that Junior Market Manufacturing and Distribution companies performed well during the pandemic despite the challenges, due to increased at-home consumption during periods of lockdowns, work-from-home, and at-home school sessions. Furthermore, in 2021 there was a recovery in both margins in line with the ongoing economic recovery from the pandemic. The average gross profit margin stood at 32.72%, slightly below its pre-pandemic level of 32.99%, while the average operating profit margin surpassed its pre-pandemic peak of 8.66% and stood at 10.03%. Though most companies fared well, a few companies continued to see margin declines. Jamaica Teas and Lasco Distributors have reported declines in their gross profit margins since 2019 attributed to a rise in cost of sales for both companies, while Mailpac Group's operating profit margin has decreased consistently since 2019. Overall, the average results for both margins are contrary to expectations of a deterioration of the average margins given the

mounting price pressures seen globally. However, year-to-date gross profit figures have indicated signs of higher input costs affecting profitability, with margins falling for 15 out of the 23 companies. Notably the magnitude of the decline for some companies has been small resulting in a relatively stable average gross profit margin YTD. On the other hand, operating margins have been performing contrary to our expectations increasing slightly relative to 2021 levels. However, more companies could see a material impact on their margins in line with the sustained costs seen globally in the coming quarters. Notably, companies like Honey Bun Limited and Blue Power Group have thus far seen a sharp decline in their margins in their year-over-year year-to-date performance. For the Blue Power Group, a combination of reduced exports and high raw material costs have impacted margins, while for Honey Bun, the company has seen a rise in raw material costs that adversely impacted its margins.

Overall, the company with the largest decline relative to its pre-pandemic levels is the Mailpac Group, which saw the most significant decline in both gross and operating profit margin in the Junior Market Manufacturing and Distribution sector in 2021. Though gross profit margin remained high at 49.0% in 2021, it was down 5.40 percentage points relative to its pre-pandemic level. Additionally, its operating profit margin stood at 24.70% in 2021 down 5.60 percentage points relative to its pre-pandemic level. Furthermore, year to date there has been a far sharper decline in margins. Its gross profit margin stands at 45.90% vs 47.90% in 2021 and its operating profit margin stands at 17.00% vs 24.84% in 2021. For 2021, its gross margin was adversely impacted by a significant rise in freight and brokerage fees, which is in line with the overall

Year-to-date, owing to higher inflation and other company specific factors, we have seen a falloff in the gross margins of most companies (15 out of 23); however the industry average remains relatively stable.

We believe that the heightened cost environment will pose a significant challenge to local Manufacturing and Distribution stocks' margins in 2022. This is especially the case as the war in Ukraine has dealt a major shock to commodity markets in ways that will keep prices at historically high levels through the end of 2024, according to the World Bank's latest Commodity Markets Outlook report.

increase in shipping costs seen globally. Factors such as increased selling and distribution costs, and administrative and general expenses, including a rise in utility expenses, would have adversely impacted its operating profit.

Given the data, we have seen that most companies have seen an increase in their margins relative to their pre-pandemic levels while a few continue to lag. Additionally, year-to-date performance indicates a decline in gross margins and increase in operating margins for most companies. We believe that the heightened cost environment will pose a significant challenge to local Manufacturing and Distribution stocks' margins in 2022. This is especially the case as the war in Ukraine has dealt a major shock to commodity markets in ways that will keep prices at historically high levels through the end of 2024, according to the World Bank's latest Commodity Markets Outlook report. Consequently, in the near to medium term, we expect that companies' margins could face stronger pressures due to the higher cost of commodities that will affect both their direct and indirect costs. A saving grace for companies is that they could continue to increase prices and transfer costs to customers; however, this may result in an overall adverse effect as companies may see a reduction in demand. Therefore, to remain competitive and attractive, companies may have to absorb some of these costs which could ultimately weigh on their profitability.

Table 1: Junior Market Manufacturing and Distribution Average Margins

Junior Market Manufacturing and Distribution Margin Averages				
	2019	2020	2021	YTD
Average Gross Profit Margin	32.99%	31.50%	32.72%	32.22%
Average Operating Profit Margin	8.66%	7.73%	10.03%	10.47%

Sources: Bloomberg, S&P Capital IQ and Company financials

Foreign Exchange Market

The Jamaican dollar appreciated by 0.22% relative to the USD, week-over-week, with the USD selling rate moving from J\$151.89 on June 24th, 2022 to J\$151.56 on July 1, 2022. The appreciation of the Jamaican dollar continues to be fuelled by the presence of high USD liquidity in the market as players seek to liquidate USD portfolios to limit losses as the JMD appreciates. It was also driven by other BOJ actions such as the additional 50 basis points increase in the policy rate on June 30th, which continues to make JMD securities more attractive relative to USD securities.

Selling	Close: 24/06/22	Close: 01/07/22	Change
J\$/US\$1	\$151.89	\$151.56	-\$0.33
J\$/CDN\$1	\$118.40	\$121.24	+\$2.85
J\$/GBP£1	\$186.05	\$181.71	-\$4.35

Global Bond Prices

Economic data over the previous week showed the Fed's preferred measure of inflation, the Personal Consumption Expenditures (PCE) Price Index, rose 0.6% in May, a tenth of a percentage point less than expected, following a 0.2% increase the month prior. Year-over-year, PCE increased 6.3% for the second consecutive month, while core inflation increased 4.7%, down from the 4.9% annual increase last month. There were festering worries about economic growth, earnings growth, inflation, and Central Bank rate hikes. In response treasury yields declined last week as investors flocked to these safe haven assets and the prices rose, with the 10-year falling 25bps to 2.88%, the largest decline in seven weeks. Despite the general performance of global bonds, some corporates and sovereigns have been able to report strong credit metrics and relatively attractive yields and have therefore, presented buying opportunities.

Bonds	Current Rating	Indicative Price	Yield	Recommendation
ALSEA 2026 (7.75%)	BB-/ Stable	96.00	8.86%	BUY
PETRO-RIO 2026 (6.13%)	BB-/ Stable	94.5	7.78%	BUY
Sagicor Fin 2028 (5.30%)	BB-/ Stable	95.00	6.33%	BUY
DOM REP 2033 (6.00%)	BB-/ Stable	86.25	7.94%	BUY
GEOPAR 5.5%	B+/ Stable	87.00	9.07%	BUY
TPHLTT 9.00%	BB/ Negative	104.75	8.10%	BUY
MARFRIG 7.00% 2026	BB+/ Stable	103.5	5.97%	BUY

GOJ Globals

DomRep bond prices declined while the price of Jamaican bonds climbed further, more so on the longer end.

Ticker	Maturity	Bid	Offer Yield*
JAMAN	2028	103.5	5.82%
	2039	107.50	7.07%
	2045	105.50	7.25%

*NB: The rates quoted above are opening indicative levels on the international market and are subject to change as market conditions vary throughout the trading session. Additionally, the prices quoted to clients of NCB Capital Market Limited (NCBCLM) are adjusted to reflect the costs associated with

completing the transaction on the respective client's behalf.

Local Corporate Bonds

Name	Maturity	Coupon	Price	Yield
GHL	2026	6.75%	105.00	6.47%
JBG	2028	6.75%	104.20	5.95%
Seprod	2024	7.25%	103.55	5.70%

Money Market

On June 29th, Bank of Jamaica (BOJ) announced its decision to further tighten monetary policy by increasing its policy interest rate by 50bps to 5.50%. This represents a cumulative increase in the policy rate of 500bps since October 2021. Although inflation at May 2022 of 10.9% was below the April 2022 outturn (11.8%), the Monetary Policy Committee (MPC) unanimously agreed to this increase since core inflation remains elevated and headline inflation is likely to continue to breach the Bank's target range of 4.0-6.0% over the next year. Owing to this action and sustained efforts to guide inflation back within the target range through GOJ's auctions and/or B-FXITT auctions tight liquidity conditions are expected to continue to prevail in the JMD money market.

Tight JMD liquidity continues to lead to strong competition for cash by market players, such as DTIs, to maintain liquid asset ratios and stay sufficiently liquid. Therefore, rates are anticipated to remain elevated. As of the 30th of June, a total of J\$29.2B is in the market, which was a 10.95% decrease in liquidity relative to the J\$32.79Bn that was recorded as of June 23rd. Market players were mainly square last week, with very limited lending during the week. The average yield from BOJ's competitive price auction remains elevated on its 30-day CD; however, it decline for the fourth consecutive week falling to 7.04% relative to 7.17% in the prior week. The highest bid rate for full allocation was 7.11%. The elevated BOJ CD rates

have caused demand for higher rates in the market.

The USD money market remains stable despite market activity changes, including the 75bps increase in interest rates by the Federal Reserve in June and the less optimistic outlook for 2022 economic growth. This adjustment brought the cumulative increase in the Fed's policy rate to 150bps since it began its tightening cycle in March 2022. The Fed also noted that a further increases totalling 175bps were possible for the remainder of 2022. Anticipated tourism inflows for the summer period will contribute to offsetting demand. Additionally, while BOJ remains committed to maintaining relative stability in the foreign exchange market, there were no B-FXITT auctions for the month of June. However, BOJ will likely continue to push USD liquidity to the market in an effort to bring inflation back in line. Broker market demand for USD remains at 30-days and longer-tenured funds, with some brokers offering rates as high as 5.25% to clients.

Stock Recommendations

Ticker	Closing Price (July 5)	P/E	Avg. Sector P/E	Current Recommendation
WISYNCO	\$19.98	19.6x	18.1x	BUY
JMMBGL	\$43.03	7.4x	12.0x	HOLD
MASSY	\$91.91	13.0x	12.3x	BUY
JAMT	\$2.89	16.1x	21.2x	BUY
PROVEN (JMD)	\$36.59	11.2x	12.0x	BUY
LAB	\$2.71	19.4x	21.0x	HOLD
SJ	\$55.00	11.7x	12.0x	HOLD
SEP	\$71.48	25.1x	18.1x	HOLD
QWI	\$0.86	3.9x	12.0x	HOLD
GK	\$102.24	12.2x	12.3x	BUY
CCC	\$64.13	12.8x	17.8x	BUY
PANJAM	\$64.88	9.5x	12.0x	BUY
KW	\$37.58	16.2x	17.8x	BUY
LUMBER	\$3.04	11.3x	25.0x	BUY
TROPICAL	\$2.92	27.0x	25.0x	HOLD
ELITE	\$3.48	30.3x	21.0x	BUY

Dates to watch this week

July 2022				
MON	TUE	WED	THUR	FRI
4	5	6	7	8
	CAR Dividend Payment (\$0.23)	MPCCEL Annual / Extra-Ordinary General Meeting	U.S. Trade Balance (May)	U.S. Unemployment Rate (Jun)
			CAN Trade Balance (May)	CAN Unemployment Rate (Jun)

Regional News

Regional Energy Strategy In The Making (Guyana Chronicles)

President Ali announced that several Caribbean Community (CARICOM) member states have come together to advance work on a regional energy strategy that will guide Caribbean nations in areas for investment. Discussions on the strategy have already begun with the President of Suriname, Chandrikapersad “Chan” Santokhi, and Prime Minister of Trinidad and Tobago, Dr. Keith Rowley and his Energy and Energy Industries Minister, Stuart Young. “We are proposing to move rapidly on a regional energy strategy to look at all the potential areas for investment, to bring investors together, bring the markets together, and see how quickly, and transparently as possible we can unlock opportunities,” Dr. Ali explained.

The strategy will also include Brazil, which is not a part of CARICOM, but, nonetheless, is currently in negotiations with Guyana and Suriname for the development of an energy corridor. The aim will be to find a solution that removed bureaucratic delays, advances dynamism, and unlocks its natural gas potential, which can contribute to rebalancing the supply side for the region.

Dominican Republic Travel Surge to Generate Seven Million 2022 Visitors (Travel Pulse)

The Dominican Republic is authoring a strong tourism rebound after hosting more than 2.2Mn visitors in the first four months of 2022. The DR closed the best month of April in the history of the country’s tourism with 736,000 visitors. The rebound comes following the government’s implementation of policies intended to attract visitors following the March 2020 pandemic’s outset such as implementing a state-funded visitor travel insurance. The Dominican Republic expects to host seven million land-based and cruise ship visitors in 2022 said government officials at the recent Dominican Annual Travel Exchange (DATE) conference.

Reaching the seven million visitor threshold will bring Dominican Republic travel within close proximity of its pre-pandemic high-water mark of 6.4Mn land-based travelers and 1.1Mn cruise ship visitors in 2019, according to Caribbean Tourism Organization data. In May, Expedia Group reported Dominican Republic summer bookings grew 40% year-over-year compared with 2021. International travelers drove this increase, led by the U.S., DomRep’s primary travel audience, representing 80% of visitors. The Dominican Republic has launched several projects, from infrastructure improvements in the historic capital city of Santo Domingo to new hotel developments and cruise port expansion in locations across the country. This will further attract and support the rebound and buoyancy

of the country's tourism sector.

International News

China's Economy Didn't Bounce Back In The Second Quarter, China Beige Book Survey Finds (CNBC)

Chinese businesses ranging from services to manufacturing reported a slowdown in the second quarter from the first, reflecting the impact of the recent lockdown in Shanghai. This statement was made by the U.S.-based China Beige Book, which claims to have conducted more than 4,300 interviews in China in late April and the month ended June 15. "While most high-profile lockdowns were relaxed in May, June data do not show the powerhouse bounce-back most expected," The analysis found few signs that government stimulus was having much of an effect yet.

Shanghai, China's largest city by gross domestic product, was locked down in April and May. Beijing and other parts of the country also imposed some level of COVID controls to contain mainland China's worst outbreak of the virus since the pandemic's initial shock in early 2020. Between the first and second quarters, hiring declined across all manufacturing sectors except for food and beverage processing, according to the China Beige Book report. The employment situation likely won't start to improve until China stimulates its economy more in the fall, China Beige Book Managing Director Shehzad H. Qazi said on June 29, 2022, on CNBC's "Squawk Box Asia."

U.S. Labour Market Remains Tight; Business Activity Slowing (Reuters)

A Federal Reserve tracker of economic growth is pointing to an increased chance that the U.S. economy has entered a recession. Most Wall Street economists have been pointing to an increased chance of negative growth ahead, but figure it won't come until at least 2023. However, the Atlanta Fed's GDPNow measure, which tracks economic data in real time and adjusts continuously, sees second-quarter output contracting by 1%. Coupled with the first-quarter's decline of 1.6%, that would fit the technical definition of recession.

"GDPNow has a strong track record, and the closer we get to July 28th's release [of the initial Q2 GDP estimate] the more accurate it becomes," wrote Nicholas Colas, co-founder of DataTrek Research. The tracker took a fairly precipitous fall from its last estimate of 0.3% growth on June 27. Data this week showing further weakness in consumer spending and inflation-adjusted domestic investment prompted the cut that put the April-through-June period into negative territory.

One big change in the quarter has been rising interest rates. In an effort to curb surging inflation, the Fed has jacked up its benchmark borrowing rate by 1.5 percentage points

since March, with more increases likely to come through the remainder of the year and perhaps into 2023. Fed officials have expressed optimism that they'll be able to tame inflation without sending the economy into recession. However, Chair Jerome Powell at a panel discussion presented by the European Union earlier this week said getting inflation down is the paramount job now.

More Parts of China Battle Covid and Threats of Lockdown as Cases Spike Again (CNBC News)

Just days after China relaxed some Covid controls, virus cases in different parts of the country have put new regions on alert. The number of cities restricting local movement more than doubled in a week to 11 as of Monday, up from five a week earlier, according to Ting Lu, chief China economist at Nomura. The latest measures affect regions that account for about 14.9% of China's GDP, up from 10.1% a week earlier, Nomura said. Mainland China's daily Covid case count, including those without symptoms, has surged from a handful of cases to around 200 or 300 new cases in the last several days. Most are asymptomatic. Many of the new cases are in the region around Shanghai. The nearby city of Wuxi in Jiangsu province said late Saturday that bars and gyms would need to close temporarily, while restaurants could only offer takeaway. Last week, a far smaller region called Si county in the neighboring province of Anhui ordered residents to stay in their homes, and leave only at designated times for virus testing.

In June, Beijing and Shanghai tried to resume normal business activity after weeks of restrictions that had kept children out of schools and many restaurants essentially closed. The southeastern metropolis of Shanghai was by far hit the hardest and locked down for April and May. Last week, mainland China cut the quarantine period for international travelers and close contacts of Covid cases. The country also changed a nationwide travel system that would theoretically make it easier to move within the country. The daily Covid case count in Beijing and Shanghai has fallen to single digits or zero in the last several days. "Markets could become a bit too complacent if they ignore the rebound of covid cases and underestimate the costs of persistent covid containment measures," Nomura's Lu said in a report Monday.

In addition to new cases on the mainland in economic powerhouses like Jiangsu province, Lu noted the spread of Covid in nearby economies — evident in Hong Kong's climbing case count and Taiwan's daily average of more than 100 new deaths in the past week. "We have been in the upswing phase of China's 'Covid Business Cycle (CBC)' since late May, thanks to a decline in the number of Covid-19 cases, the lifting of lockdowns and other easing of zero-Covid strategy (ZCS) restrictions, and stimulus measures," he said. "However, another wave of Omicron could prompt a return to a downswing phase, even though the timing of such an occurrence is uncertain."

NCB Capital Markets Ltd (formerly Edward Gayle and Co.) established in 1968 is Jamaica's oldest stockbrokerage. The company became a part of the National Commercial Bank (NCB) Group in 1994 and a fully owned subsidiary in October 2002. In December 2002, the then Edward Gayle and Co. was merged with another NCB subsidiary, NCB Investments. The products distributed by this combined subsidiary cover the traditional money market product offerings (J\$ and US\$ Repos), primary dealer services, stock brokerage and investment advisory services. Edward Gayle was renamed NCB Capital Markets Ltd. in October 2003.

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