



Premium Brands Holdings Corp.

- Integrity
- Independence
- Insight
- Individually-focused
- Investments

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5i Report Card

Metric	Value	Grade
Expected 1 year Revenue Growth	9.4%	B
5 Yr. Revenue Growth	21.8%	A
5 Yr. EPS Growth	-13.6%	B-
5 Yr. ROE	6.9%	B
Gross Margin	18.4%	B+
Net Margin	0.9%	B-
Current Ratio	1.94	B+
Debt/Equity	1.47	B-
Insider Ownership	3.31%	B-
Recessionary EPS (2008/2009)	1.22/1.07	B+
5 Yr Dividend Growth	3.25%	B+
Qualitative	Much needed stability in tough market, good valuation	A-
Rating -		B+

JANUARY 21, 2016

- Stability, growth, and FX hedge all in one?
- Sales visibility, clear management targets
- At worst, fair valuation relative to peers
- Good momentum in a bad market
- Initiating coverage at 'B+'

Traded as: PBH (TSX)

Price: C\$37.82

Dividend: 3.66%

Debt: Medium

Market Cap: \$1.03 Billion

Stability: High



Company Profile


Premium Brands Holdings Corp (PBH) acquires and builds food businesses consisting of specialty foods as well as differentiated food distribution. Specialty foods are foods where the purchasing decision is based on factors other than price. These are usually higher margin businesses that avoid large-scale competitors. An example of a specialty food would be pre-made sandwiches often seen at cafes, which is a business PBH has entered in a big way recently. Food distribution offers unique services as well as basic logistical services such as in-store merchandising and inventory management systems as well as equipment leasing solutions. PBH pays a healthy dividend that is growing and we believe restructuring over the last few years has set the company up for longer term, stable growth. PBH serves Quebec to BC and the US and considers itself a 'big fish in a small pond'.

Revenue Mix

PBH segments revenues into retail and foodservice with 65% of revenues from the retail segment and 35% from foodservice. Within retail, PBH further breaks down revenues into 'chains and large format stores' (33% of total sales) and 'independent/specialty retailers' (28.5% of total sales). Within foodservice, 18% of total sales are classified as 'Direct' and 6.6% as specialty/independent with the remainder coming from various other sources within foodservice. Digging deeper still into revenues, PBH is diversified across products, with Sandwiches making up 20%, Premium Processed Meats making 13.5%, Deli Products making up 16.6%, Seafood at 12.6%, Beef at 11.8%, and meat snacks, pork and poultry making up the remainder. Finally, roughly 28% of revenues come from the US, with the remainder generated in Canada. This US revenue exposure adds ~\$200K in unrealized gains for a one cent increase in the USD.

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Growth Plans

PBH targets an organic revenue growth rate of 6% - 8% and has so far been successful at achieving this with 27.2% revenue growth and 14.4% organic growth in retail in the last quarter and foodservice revenues up 7.6%. Total revenues were up 19.7% on the quarter. In addition to the 6% - 8% organic growth targets, PBH also targets an internal rate of return (IRR) for capital projects of 15% or more. A lot of near-term growth will be coming from margin improvements and ramping up of the recently launched sandwich production facility. Management estimates there is 4% to 6% volume growth here as well as cost savings as the kinks are worked out. With 13 lines at this plant, PBH is looking to still add two more lines. Looking out further, PBH has noted an interest in either building or acquiring a third sandwich facility while also expanding the foodservice business in Toronto by building a 50,000 square foot facility at a cost of \$13.3MM (largely to be incurred in 2016 and 2017). PBH also plans to expand a production facility of a recent acquisition, Expressco, for \$4.1MM. We like that while PBH is happy to make acquisitions, they do not just sit on it and let the purchases generate cash flows, the company continues to invest and grow the acquisitions organically. Looking at the dividend, the company targets a payout ratio of 50% of trailing twelve-month free cash flow. With the payout ratio currently at 44% and earnings growing, we think there is near term dividend growth potential at PBH as well. The last dividend increase was 2014 year-end.

Valuation


Don't be fooled by the 56% one-year return or year-to-date performance of -1.21% vs. the TSX at -7.20%. PBH still does not look expensive with an organic growth rate target of 6% to 8% (which the company has been surpassing), a forward P/E of ~17.50 and EV/EBITDA of ~10.3. PBH is trading within historical valuations and in line, or at a discount to, peers. PBH also offers a superior dividend relative to peers with an opportunity for growth. While the forward price/cash flow metric looks high based on historic trading, we note it is trading in line with the closest peers in the industry (MFI and LAS.A). Given the organic growth targets along with the dividend, we think there is still short-term upside potential here and numerous projects/initiatives that should allow the growth targets to be met. Finally, we take the momentum and ability to hold up in a very difficult market as a strong sign and would view any weakness as an opportunity for an entry point.

No employees of 5i Research hold a position in companies mentioned and cannot initiate a position in individual Canadian stocks.

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Recent Financial Results

Retail revenues rose 27% in the recent quarter with foodservice up 7.6%. Growth was helped by price increases, acquisitions and the USD. PBH expects to continue to achieve organic growth targets in 2016 with the help of capacity expansions. Margins are also expected to rise as plant efficiencies improve, from gross margins in retail of ~22% and ~16% in foodservice (19.9% overall). Adjusted debt to EBITDA of 3.3 is below the target of 4 - 4.5, indicating a potential 'hunger' for more acquisitions. Adjusted EBITDA margins rose to 8.3% from 7.3% while Adj. EBITDA grew by 36%. PBH currently holds \$9.7MM in cash.

RECOMMENDATION:

Key Risks

If Chipotle Mexican is any lesson, food companies do assume regulatory and health risks, where bacteria outbreaks or simply practices that are not up to the highest standards can lead to very big problems.

As PBH expands in the US, there is increasing FX risks and while the level debt at PBH is manageable, the company holds floating rate debt. The typical risks with an acquisitive company exist but PBH is far from a roll-up based strategy. While PBH currently operates in a less competitive environment, there is also a chance that larger scale competitors begin to compete, driving down margins and stealing market share.

ST dividend growth potential

Revenue growth visibility (6% to 8%)

Should offer stability

"B+"

SUMMARY AND INVESTMENT RECOMMENDATION

Given the current sentiment in markets, we felt PBH was a timely report to initiate coverage on, not only for the way it has held up in the recent decline, but for the stability of the underlying business. Given that PBH concentrates on more niche foods, it should be less price sensitive in the case of an actual economic downturn occurring. Further, lower energy costs should benefit margins (they run plants to produce the food which require energy) and the growing US exposure offers a hedge to the falling Canadian dollar. On top of this, PBH is growing, has a good and stable dividend, some insider ownership and is approaching a \$1 billion market-cap, which potentially opens PBH up to a new set of investors. A weak market overall may weigh on performance in the short term, but we would view any weakness as an entry opportunity for longer-term investors. We are initiating coverage of PBH at 'B+'.

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PREMIUM BRANDS HOLDINGS

Relative Strength Index



Source: Thomson Reuters Datastream

Comparables Analysis

	Ticker	P/E	P/CF	P/B	EV/Sales	EV/EBITDA	Dividend Yield
Premium Brand Holdings	PBH	17.6	14.7	3.4	0.8	10.4	3.6%
MTY Food Group	MTY	18.1	1.3	2.7	4.4	11.6	1.4%
Colabor Group	GCL	10.3	1.7	-	-	-	-
High Liner Foods	HLF	10.6	-	0.5	0.9	10.4	3.1%
Maple Leaf Foods (Closest peer)	MFI	21.7	14.5	1.2	1.0	10.3	1.4%
Lassonde Industries (Closest peer)	LASa	20.7	14.4	-	0.6	5.5	1.0%

Peer Average	16.3	8.0	1.5	1.7	9.4	1.7%
Premium (Discount) to Peers	8.0%	83.8%	126.7%	-52.9%	10.6%	111.8%

*All metrics are based on forward consensus estimates. 5i Research cannot ensure the accuracy of these numbers at the time of reader consumption.

Historical Analysis

	Ticker	P/E	P/CF	P/B	EV/Sales	EV/EBITDA
Premium Brand Holdings	PBH	17.6	14.7	3.4	0.8	10.4
2 Year Median		16.8	9.8	2.6	0.7	10.0
Premium/Discount to Median		4.8%	50.0%	30.8%	14.3%	4.0%
5 Year Median		14.9	7.3	2.1	0.7	9.0
Premium/Discount to Median		18.1%	101.4%	61.9%	14.3%	15.6%

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