Siena Market Line
2nd week of May 2016

Coffee Holding Co. Inc

JVA: NYSE

Analyst: Peter Ostrowski
Sector: Consumer Staples

Buy

Price Target: $6

Key Statistics as of 4/29/2016

Market Price:	$3.71
Industry:	Coffee
Market Cap:	$22.9M
52-Week Range:	$3-$5.50
Beta:	.83

Thesis Points:

- New member on board will increase free cash flow
- CEO has been personally buying shares over the past few months
- Negative net debt, $.28 net cash/share mitigate downside potential
- Analysts estimate coffee prices will rise

Company Description:

Coffee Holding Co is a family owned microcap coffee wholesaler and retailer that currently operates in the United States and Canada. They do this through their own brands such as Café Caribe and Fifth Avenue and also through their licensees. The three segments include whole green coffee, private label coffee and branded coffee. They make profit by purchasing coffee beans through futures and options, roasting, packaging and finally reselling them to businesses. Two of their main customers are Kuerig and DTS 8.

Thesis

Coffee Holding Co (JVA) is a buy. It is currently trading at 6X EBITDA with an upside potential of 60%.

JVA has a forty year legacy attached to it. The main issues associated with the company have been internal. They have had shrinking cash flows over the past few years due to decreasing turnovers. Luckily, there is a simple solution that JVA has just implemented that will effectively kill two birds with one stone. They have recently added a new board member, George Thomas who has experience with implementing electronic payment programs into companies. This will essentially help JVA collect on their receivables faster.

The price of coffee has been forecasted to increase over the next year which will help increase topline growth while others estimate it could increase bottom line growth as well. JVA purchases futures of coffee beans which will allow them to hedge against future price fluctuations. Because the price of coffee is projected to increase due to weather uncertainty, JVA will be able to increase the price of their coffee over the next few years while continuing to purchase coffee beans at a low price.

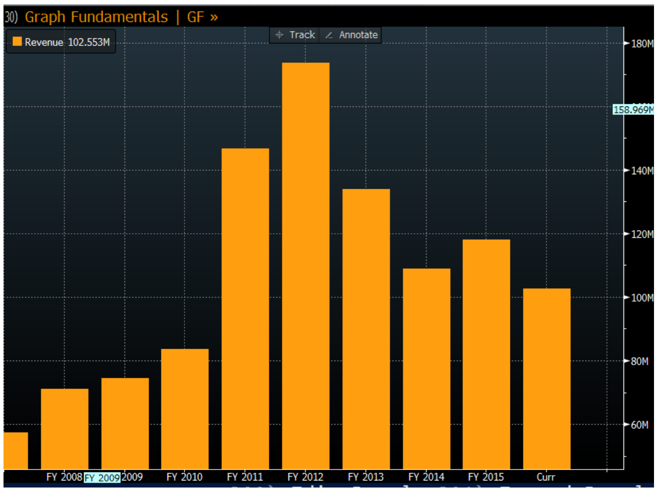
JVA is currently within their covenants and have recently increased their line of credit by $2M. This was stated in their 4th quarter report. The quiet period for share buybacks has also ended and management has already begun buying shares in the open market. This shows a significant undervaluation. Lastly, future positive earnings will most likely result in the implementation of a dividend.

Industry Outlook

The coffee business is cyclical. The price of coffee beans is currently at a low which is impacting JVA negatively. This macroeconomic effect has hurt JVA's sales and margins dramatically over the past two years.

Source: Trading Economics

This chart shows the price of coffee/pound over the past ten years. It seems likely that the price of coffee is currently at its trough. When the price of coffee is higher JVA has higher sales. 2011-2012 were the peaks in the price of coffee. As this next chart shows, 2011 and 2012 were JVA highest revenue years.



Source: Bloomberg

The reason why I mention this is because analysts estimate that the price of coffee will go up. This chart below is the average estimate of coffee prices over the next three years.

Source: Bloomberg

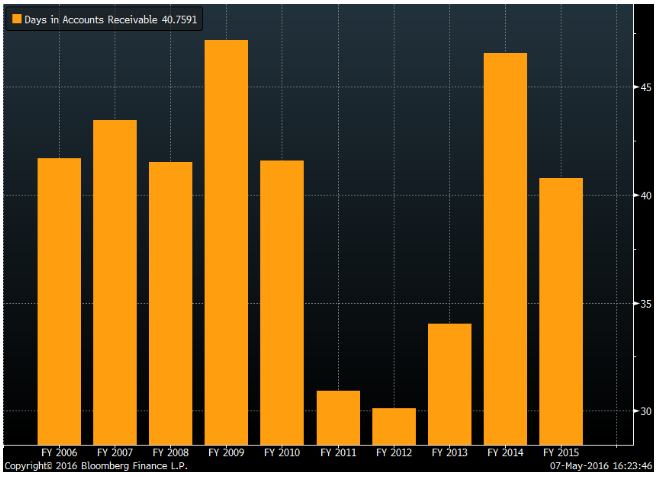
Increasing coffee prices will be very favorable for JVA as they have had to squeeze their margins over the past few years. The current position of JVA in the market makes them incredibly undervalued as their past performance will likely continue in the future as coffee prices rise. JVA has the opportunity to significantly increase performance when favorable market conditions come around.

The reason the price of coffee is currently trading so low is because there are currently no supply concerns. Brazil, the largest exporter of coffee, has seen consecutive increases in the exportation of coffee beans. This supply increase is not sustainable with current market conditions. The El Nino is currently causing very dry conditions in Brazil. This is causing mealybugs to infest coffee plants and could decrease the output of the Robusta coffee crop by 25%. The upcoming La Nina and the Brazilian winter could have a significant impact on the supply of coffee as well. As a result a decrease in supply will cause the price of coffee to rise. An increase in the price of coffee will largely benefit JVA. The current futures they have on coffee have a low of $1.20/pound with an average of $2.00/pound. Because the price of coffee could go well above $2.50 due to historical averages and the uncertainty associated with weather concerns, JVA could have a favorable next couple of years.

Recent Change in Management

It is highly important to note the level of expertise management has in this business. Nearly everyone has been on the board for at least 10 years. This is a second generation business that was founded in 1971 by Sterling Gordon. Since then his sons Andrew and David have taken over the business with a lifetime of experience in the coffee industry. They have both been in charge of the company since 1989 and took the company public in 2005. The average tenure on the board is about 15 years. Over the past few years JVA has had subpar performance and has suffered as a result. Margins have been squeezed due to volatility in the industry. In February, George F Thomas was appointed to the board. He has been in consulting for the past 35 years with a very interesting track record. He has served on the board of Egistics since 2007 and continued to after they were acquired by Top Image Systems LTD in 2014. This leads me to conclude that something must be brewing in the near future for JVA. The fact that JVA is putting a veteran in corporate finance onto the board after eleven years of no management changes, is a very compelling argument for changes in business structure. JVA has also had issues with collecting receivables and Mr. Thomas is an expert in electronic payments.

He has helped businesses incorporate his methods. He stresses the increases in business-to-business payment volume. JVA is increasing the time it takes to collect receivables. The chart below shows the a/r days since 2006:



Source: Bloomberg

JVA is not collecting on their receivables and this has been severely impacting their free cash flow. If Mr. Thomas is able to effectively implement his electronic payment system then the a/r days could dramatically decrease. This will increase free cash flow as a result.

Management has recently been purchasing more shares of JVA. Andrew Gordon, the current CEO of the company, has been purchasing shares on the open market recently. There was a quiet period restriction on management up until February. Between March 24 and March 29th Andrew Gordon purchased 3800 shares while the director Daniel Dwyer purchased 200 shares. Though these may only be modest purchases, management does not normally buy stock. They only account for about 10% of the ownership which leads me to conclude that they see the business as currently undervalued.

Acquisition target

There have been many hints over the past year that JVA may be acquired. Many of them are pure speculation but it is important to note other small coffee companies that have been acquired over the past few years.

Diedrich Coffee was acquired by GMCR in 2010 for $300M or 40X Ebitda. Diedrich Coffee is in the same business as JVA. They both source, roast and sell coffee to businesses. As JVA has done work with GMCR this may not be out of the question. GMCR also has $215M of cash on their balance sheet and typically makes an acquisition when they have more than $150M in cash.

DTS8 is a Chine coffee seller that has a licensing contract will JVA. DTS8 is one of JVA's biggest customers. They buy JVA's products and sell them in Shanghai. DTS8 recently acquired Comfort Foods, Inc. which was a small coffee manufacturer out of Massachusetts.

JVA is very cheap at $3.70/share. The current market cap is $24M. They were an $85M business a few years ago. This is very appealing to big companies as JVA's biggest issue is management which can quickly be changed.

Financials

JVA currently has $5.9M in cash and only $4.2M in debt as of last quarters report. This essentially means that this company is not going anywhere. With only 6M shares outstanding $.28 of the current price of $3.70 is backed in cash. This mitigates downside potential as the chance of default is greatly. Last quarter JVA was able to post positive free cash flow for the first time since 2011. And with the potential to collect on receivables faster with Mr. Thomas, free cash flow may continue to increase substantially over the next few quarters.

This increase in cash will give the company more flexibility for the future. JVA also has availibility of $2.3M on the credit facility until 2017 with an interest rate of 3.75%. This extra cash could be used to continue to purchase shares on the open market. With a float of only 5.5M, purchases of shares will increase the price substantially. With only around 10,000 shares traded each day, an increase in insider purchases will be noted by the street. Although insider purchases would not lead directly to volume increases, they could be the catalyst for a price increase when investors see the insider activity.

JVA has paid dividends in the past. This has generally depended on earnings. If JVA is able to generate positive earnings for the next few quarters; they will most likely announce a dividend for the future.

Conclusion

I recommend a buy on JVA. This is largely due to the industry outlook over the next few years. It is also important to note that JVA is positioning themselves for further growth. The recent appointment of Mr. Thomas to the board, could increase their ability to generate free cash flows. If JVA can collect on their receivables more efficiently cash from operations will increase; thus generating more free cash flow. There is also an opportunity for JVA to be acquired for a nice premium as they are only trading at 6X EBITDA. The general risks associated with this stock are higher as it is a microcap. I believe that high cash to debt and cash to share ratios mitigate these risks exponentially.

Coffee Holding Company, Inc. (jva)

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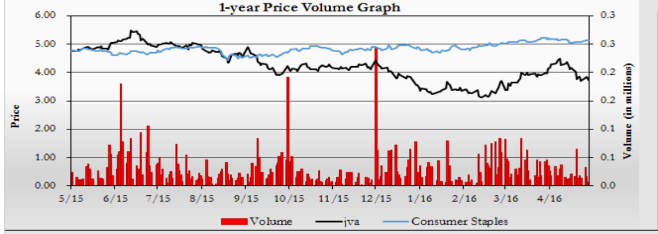
BULLISH

Analysis by Peter Ostrowski	Current Price:	$3.71	Intrinsic Value	$5.86	Target 1 year Return: 62.89%
5/7/2016	Divident Yield:	0.1%	Target Price	$6.04	Probability of Price Increase: 100%

1-year Price Volume Graph



Description

Coffee Holding Co., Inc. manufactures, roasts, packages, markets, and distributes roasted and blended coffees in the United States, Canada, Australia, England, and China.

General Information

Sector	Consumer Staples
Industry	Food Products
Last Guidance	November 3, 2015
Next earnings date	June 11, 2016
Estimated Country Risk Premium	6.00%
Effective Tax rate	40%
Effective Operating Tax rate	42%

Market Data

Market Capitalization	$22.86
Daily volume (mil)	0.01
Shares outstanding (mil)	6.16
Diluted shares outstanding (mil)	6.20
% shares held by institutions	78%
% shares held by investments Managers	10%
% shares held by hedge funds	2%
% shares held by insiders	10.86%
Short interest	0.39%
Days to cover short interest	0.79
52 week high	$5.50
52-week low	$3.00
Levered Beta	0.70
Volatility	68.17%

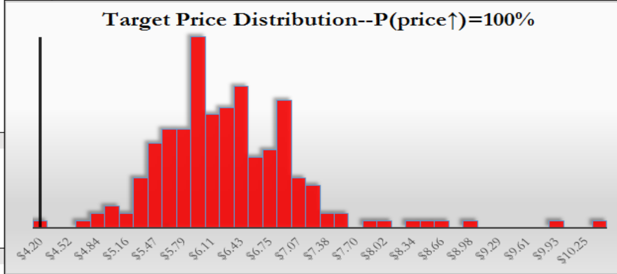
Past Earning Surprises

Quarter ending	Revenue	EBITDA
1/31/2015	N/A	N/A
4/30/2015	-51.39%	N/A
7/31/2015	-38.55%	N/A
10/31/2015	-54.13%	N/A
1/31/2016	-41.57%	N/A
Mean	-46.41%	#DIV/0!
Standard error	3.8%	#DIV/0!

Peers

Primo Water Corporation
Crystal Rock Holdings, Inc.
Farmer Brothers Co.
National Beverage Corp.
The J. M. Smucker Company

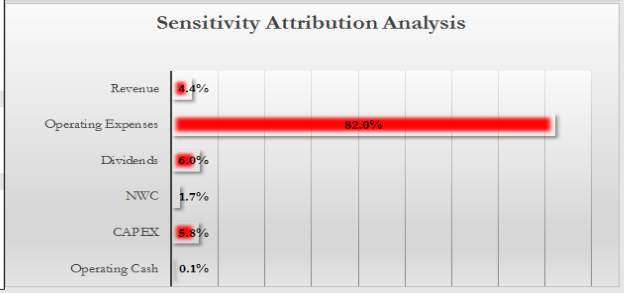
Target Price Distribution--P(price↑)=100%



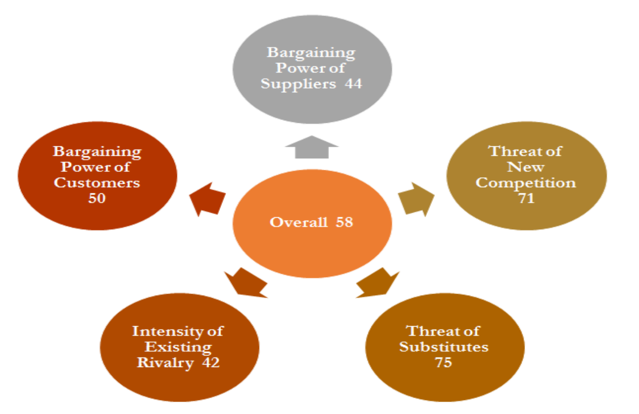
Management	Position	Total compensations growth	Total return to shareholders
Gordon, Andrew	Chief Executive Officer, Pre	-4.4% per annum over 5y	18.69% per annum over 5y
Gordon, David	Executive Vice President of	-1.33% per annum over 5y	18.69% per annum over 5y
	0 0	N/M	N/M
	0 0	N/M	N/M
	0 0	N/M	N/M
	0 0	N/M	N/M

Profitability	jva (LTM)	jva (5 years historical average)	Industry (LTM)
ROIC	-1.2%	7.93%	11.91%
NOPAT Margin	-1%	1.97%	9.0%
Revenue/Invested Capital	2.32	4.03	1.33
ROE	-2.2%	8.35%	13.99%
Adjusted net margin	-1%	1.88%	7.7%
Revenue/Adjusted Book Value	3.35	4.46	1.81
Invested Funds	**jva (LTM)**	**jva (5 years historical average)**	**Industry (LTM)**
Total Cash/Total Capital	13.8%	12.3%	10%
Estimated Operating Cash/Total Capital	8.2%	10.3%	N/A
Non-cash working Capital/Total Capital	47.6%	46.6%	6%
Invested Capital/Total Capital	95.4%	98.0%	87%
Capital Structure	**jva (LTM)**	**jva (5 years historical average)**	**Industry (LTM)**
Total Debt/Common Equity (LTM)	0.30	0.15	0.22
Cost of Existing Debt	3.70%	4.33%	4.16%
Estimated Cost of new Borrowing	2.85%	1.93%	4.16%
CGFS Risk Rating	A	AA	B
Unlevered Beta (LTM)	0.60	0.98	0.50
WACC	6.96%	10.94%	6.66%

Sensitivity Attribution Analysis



Porter's 5 forces (scores are out of 100)



Valuation

Period	Revenue growth	NOPAT margin	ROIC/WACC
Base Year	-14.5%	-0.5%	-0.17
1/31/2017	-13.0%	4.5%	1.33
1/31/2018	-11.5%	4.2%	1.15
1/31/2019	-10.0%	4.3%	1.13
1/31/2020	-8.4%	4.5%	1.10
1/31/2021	-6.9%	4.6%	1.08
1/31/2022	-5.4%	4.7%	1.05
1/31/2023	-3.9%	4.8%	1.02
1/31/2024	-2.4%	5.0%	0.99
1/31/2025	-0.9%	5.1%	0.96
1/31/2026	0.6%	5.2%	0.92
Continuing Period	2.1%	5.2%	0.90

Period	Invested Capital	Net Claims	Price per share
Base Year	$33.76	$4.85	$5.96
1/31/2017	$34.94	-$1.99	$6.21
1/31/2018	$37.54	-$5.36	$6.04
1/31/2019	$42.95	-$6.26	$5.61
1/31/2020	$44.19	-$4.94	$4.96
1/31/2021	$40.99	-$1.58	$4.08
1/31/2022	$36.67	$3.40	$3.02
1/31/2023	$32.70	$9.80	$1.80
1/31/2024	$29.55	$17.46	$0.45
1/31/2025	$27.16	$26.24	-$1.02
1/31/2026	$25.39	$36.13	-$2.59
Continuing Period			