



SAMPATH BANK PLC (SAMP.N0000)

DOWNGRADE TO HOLD

CSE: SAMP.N0000

Fair Value: LKR 340.0 [Pre XR], LKR 320.0 [Post XR]

Current Price: LKR 330.0

Bloomberg: SAMP SL

Buy Below LKR 316.0 [Pre XR], LKR 298.0 [Post XR]

Jan 2018

KEY DATA			
Share Price (LKR)	330.00		
52w High/Low (LKR)	350.0/255.0		
Average Daily Volume (Shares)	101,451		
Average Daily Turnover (LKR mn)	31.16		
Issued Share Capital (Shares mn)	186.2		
Market Capitalisation (LKR mn)	61,443		
Price Performance (%)	1 mth	3 mths	12mths
SAMP	-0.9%	0.6%	24.8%
ASPI	2.1%	-0.2%	5.9%
Major Shareholders as at 30th Sep 2017			
Vallibel One PLC	14.95%		
Mr Y S H I Silva	9.99%		
Employees' Provident Fund	9.97%		
Rosewood (Pvt) Limited - Account No.1	5.39%		
HSBC INTL NOM LTD-BBH-Matthews Intl Funds	4.58%		
Public Holdings	88.35%		

"Stability to augment Sustainability"

P/E 31 Dec	2015	2016	2017E	2018E	2019E
Net Interest Income (LKR Mn)	18,550	23,955	29,135	34,412	39,042
Net Profit (LKR Mn)	6,623	9,496	11,888	13,906	15,864
EPS (LKR) *	23.3	33.5	41.89	49.0	55.9
YoY % Growth	26%	43%	25%	17%	14%
Valuations					
PER (x)	14.1x	9.9x	7.9x	6.7x	5.9x
PBV (x)	2.3x	1.8x	1.3x	1.0x	0.9x
Dividend Yield (%)	4.1%	6.0%	5.9%	5.4%	6.0%
NAVPS *	137.8	175.3	239.6	322.3	370.4
DPS (LKR) *	13.0	18.8	18.6	17.2	18.9
Dividend Payout	56%	56%	44%	35%	34%

* Adjusted for the Rights issue announced in July 2017

SAMP, is the 3rd largest privately owned bank in the banking sector of Sri Lanka in terms of asset base with total assets of LKR 782Bn as at 30th September 2017. Earnings recorded a CAGR of 34% over a period from 2014-16 on the back of aggressive growth in lending and improved cost to income ratio which was registered at 48% in 2016. We expect SAMP earnings to reach c.LKR 13.9Bn in 2018E. SAMP at a fair value of LKR 340.0 for 2018E is expected to provide a total return of 9% at current price level of LKR 330.0 Downgrade to HOLD.

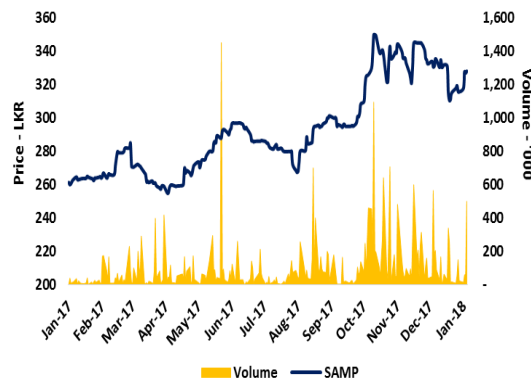
Margins and Spreads to stabilize amidst stable interest rate environment: We expect SAMP's interest spreads to stabilize around c.4.4% levels while Net Interest Margins to register at c.4.6% in 2018E resultant to the expected less volatile interest rates backed by the effects of prudent measures implemented by the government (e.g. Inflation Targeting Framework, Foreign Exchange Act, Liability Management Bill, etc...) improved revenue streams, increased foreign inflows into government securities market.

Aggressive lending to increase in Impairment provisioning: SAMP saw its loan book expanding aggressively at a CAGR of 24% over 2014-16 period while the NPL's hovered around 1.6% during the period. However, the increased loan disbursement is likely to result in increased impairment provisioning leading to an increased NPL of c.2% in 2018E.

SAMP to provide a 9% return over 12-months period: First Capital Research expect SAMP.N to achieve a fair value of LKR 340.0 providing a total return of 9% (Dividend yield 6%) over 12-month period. [based on average price of LKR 343.0 via PER based valuations, LKR 335.1 via Justified PBV based valuations and LKR 280.8 based on Residual income based valuation] at the current price level of LKR 330.0.

Risks associated: SAMP being a financial intermediary, company is exposed to credit, market and regulatory risks.

Figure 1: SAMP Price Volume Graph



Source: CSE

Disclosure on Shareholding:

First Capital Group and its affiliates do not hold shares in SAMP. Neither First Capital Group nor its affiliates have traded in the shares in the three trading days prior to this document, and will not trade in the shares for three trading days following the issue of this document.

ANALYST CERTIFICATIONS AND REQUIRED DISCLOSURES BEGIN ON PAGE 13

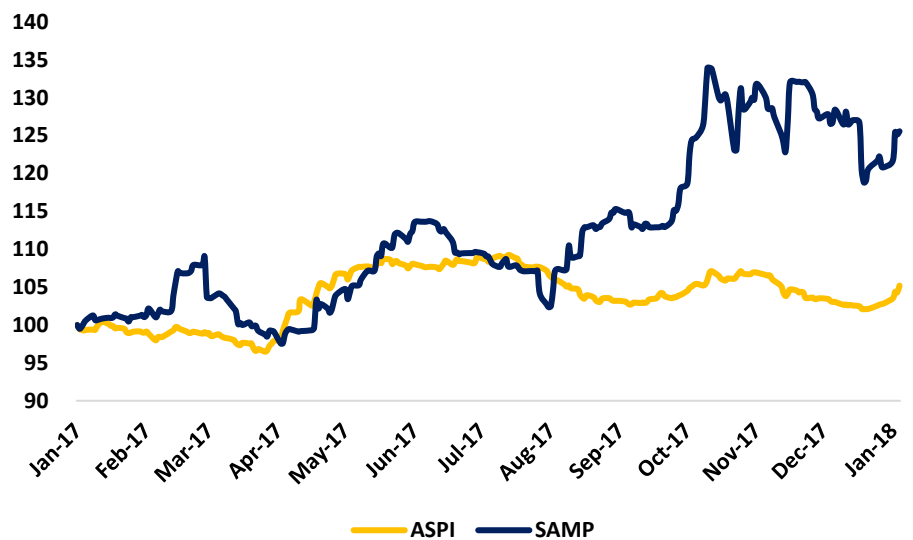
1.0 Introduction

1.1 “3rd largest player in the Banking Sector”: SAMP is the 03rd largest entity in the Banking sector in Sri Lanka with an asset base of LKR 782Bn by end September 2017. During 2014-16 period the total asset base of SAMP grew by a CAGR of an impressive 24%. SAMP’s lending portfolio accounts for 75% of the total asset base of the company leading to a Return on Assets of 1.6% as of 2016.

SAMP’s 3,966 workforce spread across 229 branches located island wide services the Company’s over three million loyal clientele, offering long tenure products ranging from lease, hire purchase, import/export loans personal/business/housing loans to short term financing through overdraft facility, credit cards and gold loans.

1.2 Share Price Performance: Over the past 12 months SAMP’s shares have outperformed the market where SAMP’s share price appreciated by 26%YoY while the ASPI inclined by a marginal 5% during the same period. SAMP.N has been trading between LKR 255.0 and all time high of LKR 350.0.

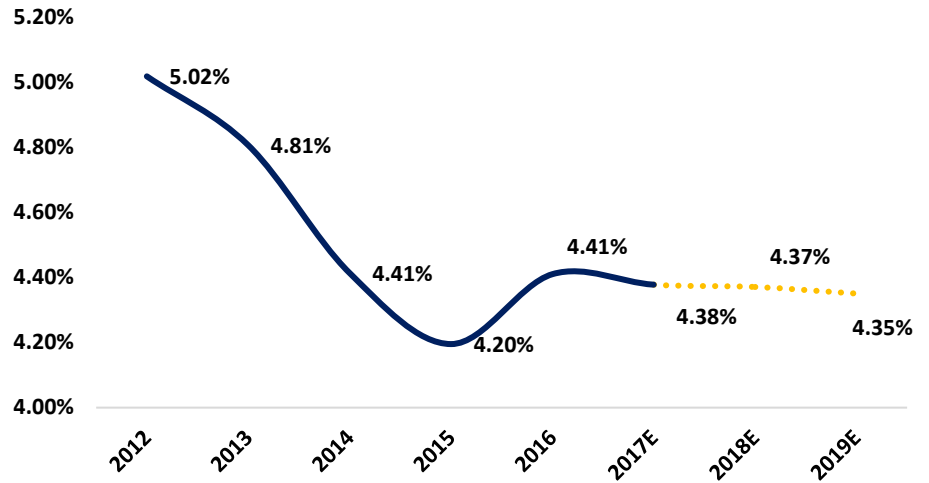
Figure 2: ASPI vs SAMP



Source: CSE

2.0 Interest Spreads to stabilize amidst less volatile interest rate environment

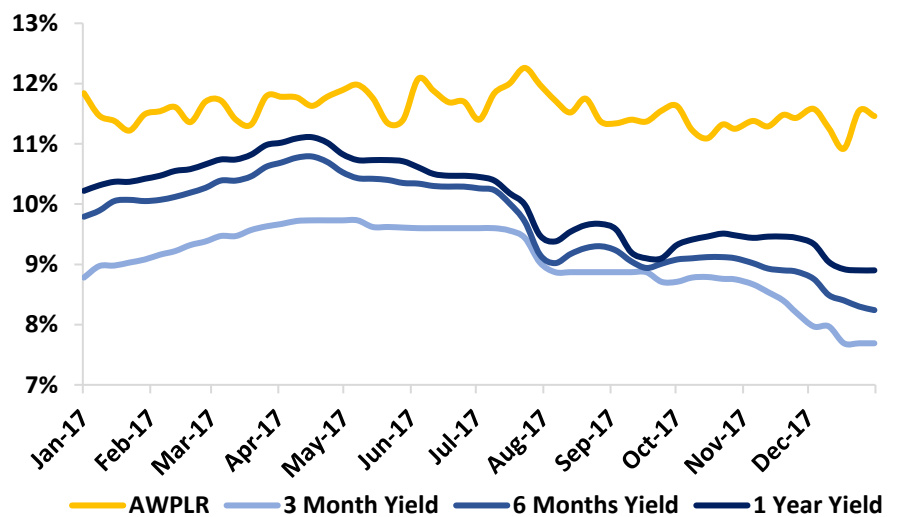
Figure 3: Net Interest Spread (2011 to 2019E)



Source: Company Annual Reports and First Capital Research Estimates

2.1 Interest Spreads to register at 4.4%: SAMP's net interest income is expected to reach c.LKR 34.4Bn by 2018E with a CAGR of 20% over 2016-2018E on the back of increased loan disbursements coupled with the higher interest rates prevailed during 2016-17 period. Term loans account for 43% of the total lending portfolio by end September 2017 in comparison to 41% in comparative period in 2016. Higher portion of term loans enables the company to manage overall average lending rates via revision of terms of the contracts to be in par with the market rates prevailing at the time thus reducing the volatility in the interest spreads. Net Interest Margins is expected to register at c.4.6% in 2018E as opposed to 4.4% registered in 2016.

Figure 4: Rate Movement – AWPR, 3M, 6M and 1Y T-Bill



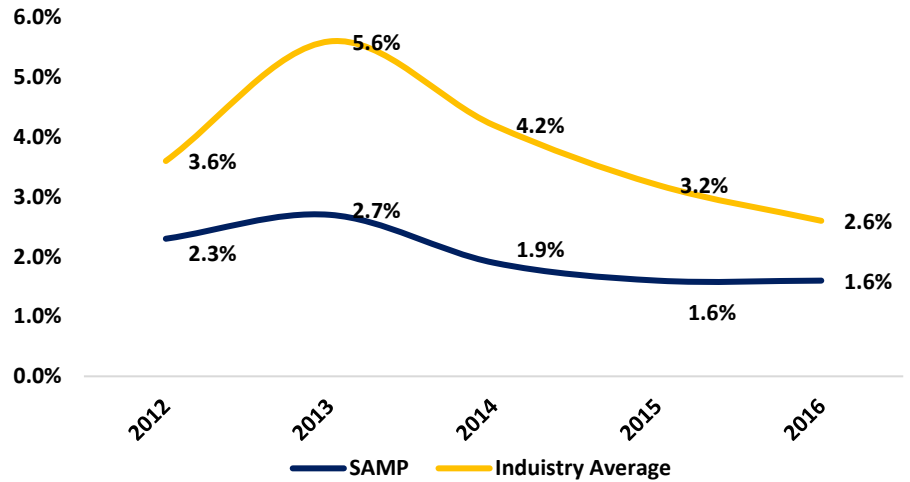
Source: CBSL

2.2 Macro environment factors favour the stabilization of interest rates and exchange rate: Sri Lanka’s rate of inflation is expected to stabilize in mid-single digits of 4%-6% resultant to the Inflation Targeting framework adopted by the CBSL supported by a more flexible exchange rate policy. Improved net foreign inflows into the government securities market, improved revenue collection stemming from the introduction of amended Inland Revenue Act, improvements to the auction system for government securities, etc... is expected to further stabilize interest rates and reduce volatility from 2018E and thereon.

With the proposed implementation of Liability Management Bill which permits the government to borrow funds in advance to meet the future liabilities, thus smoothening the cash flow management and thereby further supporting a more stable and less volatile interest rate regime. At present government’s liabilities are bunched up in specific periods where credit facilities are obtained as and when the payments fall due thus increasing the interest rate volatility.

3.0 Increased Impairment provisioning stemming from aggressive credit disbursements and adverse macro environment

Figure 5: NPA Ratio – SAMP vs Industry Average (2012-2016)



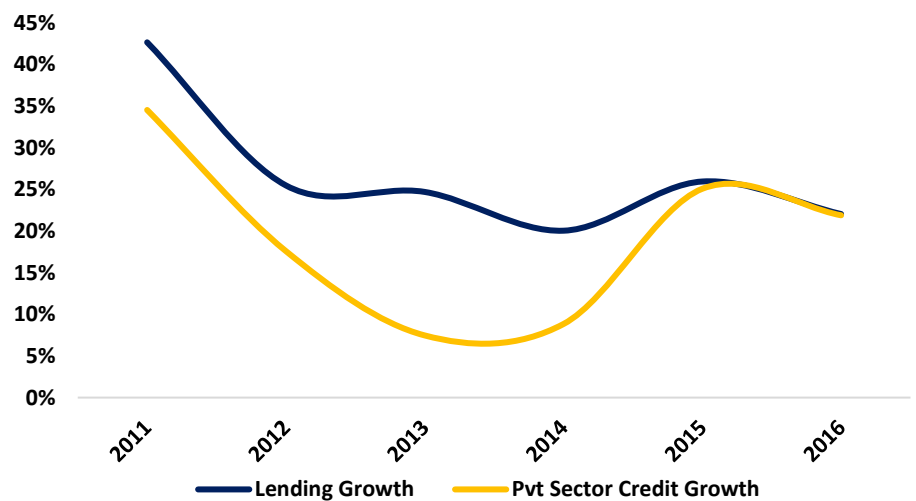
Source: CBSL and Company Annual Reports

SAMP’s NPAs to worsen leading to increased impairment provisioning

SAMP’s impairment provisioning is expected to register at c.2% in 2018E in comparison to 1.7% recorded in 2016. Adverse weather conditions prevailed in the country during the mid to latter part of 2017 coupled with bank’s aggressive growth witnessed in lending are expected to contribute to the jump in NPAs of SAMP.

3.1 Aggressive Credit disbursement to lead to increased NPAs in 2017 onwards:

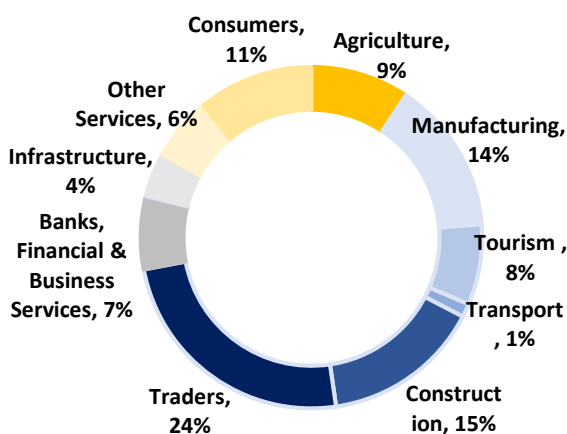
Figure 6: Private Sector Credit Growth vs SAMP’s Lending Growth (2011-16)



Source: CBSL and Company Annual Reports

Loans and Advances grew at a CAGR of 24% over 2014-16 to reach of LKR 473Bn in 2016 while the same is expected to grow at a moderate pace with a CAGR of c.15% over 2016-18E to reach c.LKR 620Bn on the back of slowdown in private sector credit growth of the country in 2017. Sri Lanka’s private sector credit growth was registered at 21.9% in 2016 while it is likely to contract in 2017 amidst monetary tightening measures implemented by the CBSL. During 2016, impairment provision dipped to 1.7% in comparison to 1.9% the previous year.

Figure 7: Lending Portfolio Distribution - 2016



Source: CBSL, Company Annual Reports

3.2 Adverse weather conditions to further worsen the NPAs: SAMP’s lending portfolio is diversified amongst 11 main sectors where Construction, Manufacturing and Agriculture collectively contribute 39%. Construction, Manufacturing and Agriculture are three of the main segments of the economy that were severely affected by the adverse weather conditions prevailed during 2016 and 2017. This resulted in SAMP’s impairment provisioning increasing by a considerable 55%YoY to record at LKR 1.5Bn in 2016 in comparison to LKR 993Mn recorded in 2015. During the 9M2017, SAMP’s impairment provisioning was recorded at LKR 2.2Bn in comparison to LKR 958Mn the previous year.

3.3 Regulatory support to uphold the credit quality: Regulator, the Central Bank of Sri Lanka imposed restrictions on Loan to Value ratio which came into effect during the latter part of 2015 was further tightened in early 2017 resulting in LTV on commercial vehicles, Motor cars, SUVs and vans, Three wheelers and other vehicles restricting to 90%, 50%, 25% and 70%. This move resulted in avoiding less credit worthy customers from obtaining credit facilities and given the higher commitment required from the customer the probability of defaulting the payment is likely to reduce significantly thus reducing the irregular advances which in turn will reduce the non-performing loans and the impairment provisioning requirements.

4.0 SAMP to provide 9% return

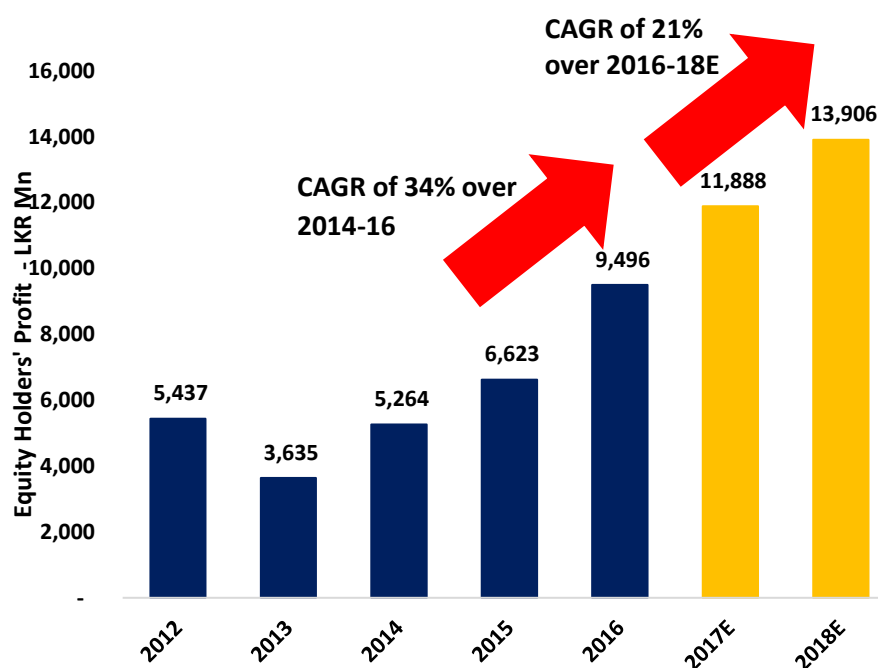
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YoY % Growth	26%	43%	25%	17%	14%
Valuations					
PER (x)	14.1x	9.9x	7.9x	6.7x	5.9x
PBV (x)	2.3x	1.8x	1.3x	1.0x	0.9x
Dividend Yield (%)	4.1%	6.0%	5.9%	5.4%	6.0%
NAVPS *	137.8	175.3	239.6	322.3	370.4
DPS (LKR) *	13.0	18.8	18.6	17.2	18.9
Dividend Payout	56%	56%	44%	35%	34%

* Adjusted for the Rights issue announced in July 2017

SAMP Earnings CAGR of 21% 2016-18E: For 2018E, First Capital Research expect a fair value of LKR 340.0 for SAMP.N providing a total return of 9% (capital gain 3% and dividend yield 6%) at current market price of LKR 330.0.

We expect a post rights adjusted fair value of LKR 320.0 based on SAMP's earnings of c.LKR 13.9Bn in FY18E. At current market price of LKR 315.0 (adjusted for Rights issues announced in July and December 2017) SAMP is expected to provide a total return of 8% over a period of 1 year with a dividend yield of 6%.

Figure 8: Earnings to grow at a CAGR of 13% over FY16-FY18E



Source: Company Annual Reports and First Capital Research Estimates

Expected SAMP Price	2018E
PER based target price	343.0
Justified PBV based target price	335.1
Residual Income based target price	280.8
Average Target Price (Post Rights)	320.0
Average Target Price (Pre Rights)	340.0

4.1 SAMP to provide a Total Return of 9%

2018E (Pre Rights) Price: For 2018E, First Capital Research expect a fair value of LKR 340.0 for SAMP.N providing a total return of 9% (capital gain 3% and dividend yield 6%) at current market price of LKR 330.0.

2018E (Post Rights) Price: For 2018E, First Capital Research expect a fair value of LKR 320.0 for SAMP.N (based on average price of LKR 343.0 via PER based valuations, LKR 335.1 via Justified PBV based valuations and LKR 280.8 based on Residual income based valuation) providing a total return of 8% (capital gain 2% and dividend yield 6%) at current market price (adjusted for Rights issues announced in July and December 2017) LKR 315.0.

Return	Post RI	Pre RI
Target Price	320.0	340.0
Current Price	315.0	330.0
Capital Gain (LKR)	5.0	10.0
2017 Dividend (LKR) *	18.6	18.6
Capital Gain %	2%	3%
Dividend Yield %	6%	6%
Total Return %	8%	9%

* Only Dividend paid up to end March 2018 are being included in Dividend yield computation.

COE	
Rf	8.9%
Rm	16.9%
β	0.99
Growth %	3.0%
$Ke=Rf+\beta(Rm-Rf)$	16.9%

4.2 Justified PBV based Valuation

Justified PBV based Valuation	
ROAE	17.4%
Growth	3.0%
COE	16.9%
PBV	1.0
NAVPS	322.3
TARGET PRICE	335.1

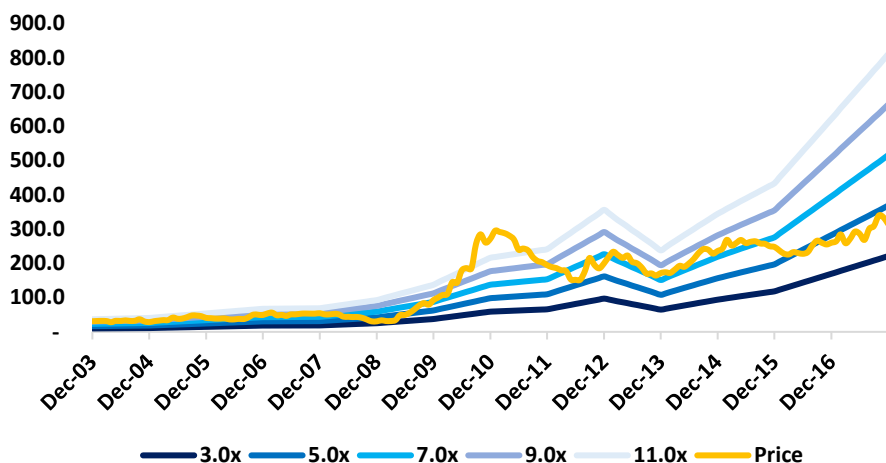
4.3 Residual Income based Valuation

Residual Income based Valuation	
PV of Residual Income (LKR Mn)	11,695
No of Shares (Mn)	284
RI per share	41.2
Opening book value per share	239.6
Value per Equity Share	280.8

4.3 Average PER of 7.0x

PER based Valuation	
Earnings (LKR 'Mn)	13,906
No. of Shares ('Mn)	284
EPS	49.0
Sector Forward PER	7.0x
Price at 7.0x Earnings	343.0

Figure 9: PE Band Graph



Source : CSE and First Capital Research Estimates

SAMP price has been trading between 3.0x – 9.0x bands during the last 24 months. We expect SAMP to trade at a PER of 7.0x on 2018E earnings. By 2018E SAMP’s EPS is expected to reach c.LKR 49.0.

5.0 Investment Risks

Default risk dominates Credit risk: Given the nature of the business of being the financial intermediary, SAMP is exposed to credit risk which is the uncertainty that a borrower may not repay a loan and that the lender may lose the principal of the loan or the interest associated with it. Credit risk is inherent due to the nature of business thus can only be mitigated or transferred but not avoided.

Market risk primarily attributable to interest rate risk: SAMP is exposed to the market risk that is resultant to the uncertainty arising from the volatility in interest rates, exchange rate, equity price, commodity prices (e.g.: vehicle, gold, etc...). SAMP cannot eliminate Market risk but can be managed through hedging given it is considered a systematic risk.

Changes in regulations to impact the sectors’ performance: Banking sector of Sri Lanka is one of the most highly regulated segments in the economy, governed by the Central Bank of Sri Lanka acting as the Regulator. The uncertainty SAMP is exposed to as a result of adhering to laws, regulations and regulatory guidelines as well as internal controls and approved policies. SAMP is exposed to Regulatory risk which can only be managed through lobbying or compliance mechanisms.

Appendix 1 – Recommendation Criteria

Categorization	Company Category	Strong Buy	Buy	Hold	Sell
Grade A	S&P SL20 Companies	T.Bill + 10% & Above	T.Bill + 5% & Above	T.Bill + 1% & Above	Below T.Bill + 1%
Grade B	Rest of the Companies	T.Bill + 13% & Above	T.Bill + 8% & Above	T.Bill + 3% & Above	Below T.Bill + 3%
Grade C	Companies less than LKR 1Bn Market Cap	T.Bill + 16% & Above	T.Bill + 11% & Above	T.Bill + 6% & Above	Below T.Bill + 6%

*1 Year T Bill rate as of 03-01-2018 – 8.9%

Appendix 2 – Income Statement

Income Statement - (LKR Mn)	2015	2016	2017E	2018E	2019E
Income	49,443	70,211	89,679	100,747	109,074
Interest income	39,706	58,976	75,511	84,464	90,336
Less: Interest expenses	21,156	35,021	46,377	50,051	51,293
Net interest income	18,550	23,955	29,135	34,412	39,042
Fee and commission income	6,621	8,203	9,843	11,320	13,018
Less: Fee and commission expenses	1,204	1,467	1,969	2,264	2,604
Net fee and commission income	5,417	6,735	7,875	9,056	10,414
Net interest, fee and commission income	23,968	30,691	37,009	43,468	49,457
Net trading income	(341)	234	257	283	311
Other operating income	3,116	3,032	4,325	4,963	5,721
Total Operating income	26,742	33,957	41,591	48,715	55,489
Less: Impairment charge/(reversal) for loans and other losses	(993)	(1,535)	(1,747)	(2,752)	(3,425)
Net operating income	25,749	32,422	39,844	45,962	52,064
OPERATING EXPENSES					
Personnel expenses	6,524	7,835	8,893	10,264	11,737
Other operating expenses	7,438	8,431	9,391	10,502	11,580
	13,962	16,266	18,284	20,767	23,316
Operating profit before value added tax (VAT) and r	11,787	16,156	21,560	25,195	28,747
Less: VAT & NBT on financial services	1,998	2,943	4,568	5,319	6,073
Operating profit after value added tax (VAT)	9,790	13,214	16,992	19,876	22,675
PROFIT BEFORE INCOME TAX	9,790	13,214	16,992	19,876	22,675
Less: Income tax expense	3,161	3,712	5,098	5,963	6,802
PROFIT FOR THE YEAR	6,628	9,501	11,894	13,914	15,872
Profit attributable to Equity holders of the Bank	6,623	9,496	11,888	13,906	15,864
Profit attributable to Non-controlling interests	5	5	6	8	9
PROFIT FOR THE YEAR	6,628	9,501	11,894	13,914	15,872
EPS	38.44	52.30	53.25	49.01	53.94

Source: Company Annual Reports and First Capital Research Estimates

Appendix 3 – Statement of Financial Position

Statement of Financial Position - (LKR Mn)	2015	2016	2017E	2018E	2019E
ASSETS					
Cash and cash equivalents	13,713	17,222	14,972	21,263	30,317
Balances with Central Bank of Sri Lanka	21,342	33,725	34,912	36,786	38,371
Placements with Banks	5,193	8,750	9,800	11,172	12,847
Reverse repurchase agreements	-	34,629	38,084	44,703	41,467
Derivative financial instruments	319	110	541	620	715
Financial investments	55,801	70,582	75,340	80,219	81,677
Loans and receivables from banks	1,651	2,642	1,771	2,002	2,262
Loans and receivables from other customers	386,278	472,755	540,578	620,399	715,098
Other loans & receivables	33,368	38,708	48,712	53,377	60,316
Property plant and equipment	8,697	10,709	11,060	11,468	11,938
Intangible assets	368	356	350	370	354
Deferred tax asset	23	1	1	1	1
Other assets	4,575	7,047	7,646	8,295	9,042
Total assets	538,647	680,099	765,843	872,999	983,536
LIABILITIES					
Due to banks	3,418	6,071	5,904	6,672	6,032
Securities sold under re-purchase agreements	8,663	10,095	10,812	12,408	14,302
Derivative financial instruments	457	64	177	177	265
Due to other customers	407,164	513,434	590,449	667,207	753,944
Debt issued and other borrowed funds	65,171	84,179	70,854	73,393	79,164
Other liabilities	14,571	16,513	19,657	21,680	24,715
Total Liabilities	499,444	630,356	697,852	781,537	878,422
EQUITY					
Stated capital	5,381	6,471	16,987	32,682	36,014
Reserves	29,103	36,955	37,550	36,974	37,767
Total equity attributable to equity holders of the Ba	39,109	49,742	67,985	91,448	105,091
Non-controlling interests	95	-	6	14	23
Total Equity	39,203	49,742	67,991	91,462	105,113
Total Liabilities and Equity	538,647	680,099	765,843	872,999	983,536
NAVPS	227	274	305	322	370

Source: Company Annual Reports and First Capital Research Estimates

Appendix 4 – Ratio Analysis

	2015	2016	2017E	2018E	2019E
Tier 1 (5%)	7.90%	8.31%			
Tier 2 (10%)	12.26%	12.87%			
Return on Average Equity	17.99%	21.38%	20.20%	17.44%	16.14%
Return on Average Assets	1.35%	1.56%	1.64%	1.70%	1.71%
Net Interest Spread	4.20%	4.41%	4.38%	4.37%	4.35%
Net Interest Margin	4.20%	4.38%	4.46%	4.62%	4.63%
Cost / Income	52%	48%	44%	43%	42%
Cost / Average Assets	2.85%	2.67%	2.53%	2.53%	2.51%
Asset Growth	22%	26%	13%	14%	13%
Deposit Growth	20%	26%	15%	13%	13%
Borrowings Growth	49%	29%	-16%	4%	8%
Loan Growth	26%	22%	15%	14%	15%
Avg. yield on earning assets	8.99%	10.79%	11.56%	11.33%	10.71%
Avg. cost of funds	4.79%	6.38%	7.18%	6.96%	6.36%
Loan / Deposits	103%	100%	100%	101%	103%
Loan / Total Assets	78%	76%	77%	77%	79%
Deposit / Liabilities	82%	81%	85%	85%	86%
Equity / Assets	7%	7%	9%	10%	11%
CASA	47%	39%	40%	43%	42%
Cost / Branch (Rs.'Mn)	62.1	71.0	78.1	86.9	95.6
Rev. / Employee (Rs.'Mn)	6.0	7.8	9.3	10.7	11.9
Employees	3,993	3,960	3,978	4,063	4,148
Branches	225	229	234	239	244
New Branches during the Year	5	4	5	5	5

Source: Company Annual Reports and First Capital Research Estimates

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