



## JOHN KEELLS HOLDINGS PLC

CSE: JKH.N0000

Bloomberg: JKH SL

**STRONG BUY**

Feb 2018

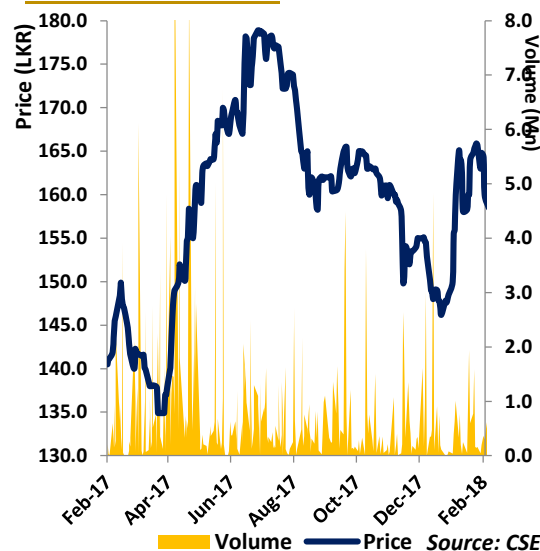
Current Price – LKR 158.5

Fair Value – LKR 210.0 [FY19E]

3QFY18 Earnings ↓ -13.0%YoY

KEY DATA			
Share Price (LKR)	158.50		
52w High/Low (LKR)	180.00 / 133.90		
Average Daily Volume (Shares)	831,639		
Average Daily Turnover (LKR)	133,818,048		
Issued Share Capital (Shares mn)	1,387.5		
Market Capitalisation (LKR mn)	219,919		
Price Performance (%)	1 mth	3 mths	12mths
JKH	7%	-1%	13%
ASPI	2%	-2%	6%
Major Shareholders as at 31st Dec 2017			
Broga Hill Investments Ltd	10.20%		
Mr S E Captain	10.10%		
Schroder International Selection Fund	6.20%		
Paints & General Industries Ltd	6.20%		
Melstacorp (Private) Ltd	3.50%		
Estimated Free Float	97.53%		

Price – Volume Chart



### “Tri-Zen uplift value of JKH on top of Cinnamon Life”

P/E 31 March	FY16	FY17	FY18E	FY19E	FY20E
Revenue (LKR mn)	93,709	106,273	122,913	139,675	179,087
EBIT	10,303	12,339	11,026	14,166	25,436
Net Profit (LKR mn)	14,070	16,275	15,421	18,182	26,691
Adjusted EPS (LKR)	10.2	11.8	11.2	13.2	19.4
YoY % Growth	-2%	16%	-5%	18%	47%
Valuations					
PER (x)	15.6	13.4	14.2	12.0	8.2
PBV (x)	1.4	1.2	1.2	1.1	1.0
Div Yield (%)	3.7%	3.3%	2.1%	2.5%	3.7%
NAVPS	112.8	130.0	137.8	147.1	160.7
Adjusted DPS (LKR)	5.8	5.3	3.4	4.0	5.8
Div Payout	57%	45%	30%	30%	30%

LKR (Mn)	3QFY18	3QFY17	YoY	9MFY18	9MFY17	YoY
Revenue	31,216	27,937	↑ 16.9%	60,127	49,798	↑ 14.7%
Gross profit	6,884	8,139	↓ -15.4%	20,716	22,690	↓ -8.7%
Operating profit	2,399	3,536	↓ -32.2%	7,258	9,632	↓ -24.6%
PBT	5,830	6,725	↓ -13.3%	14,867	15,479	↓ -4.0%
NP	4,492	5,149	↓ -12.8%	11,055	11,289	↓ -2.1%

LKR (Mn)	4QFY17	1QFY18	2QFY18	3QFY18	QoQ
Revenue	29,848	26,822	29,624	31,216	↑ 5.4%
Gross profit	8,425	6,706	7,126	6,884	↓ -3.4%
Operating profit	4,741	2,145	2,714	2,399	↓ -11.6%
PBT	7,408	4,088	4,950	5,830	↑ 17.8%
NP	4,986	2,833	3,730	4,492	↑ 20.4%

**Disclosure on Shareholding:**

First Capital Group and its affiliates does hold 225,000 shares of JKH and will not trade in this share for the three trading days following the issue of this document.

**ANALYST CERTIFICATIONS AND REQUIRED DISCLOSURES BEGIN ON PAGE 5.**

**“Transportation and Finance balance retail dip” – Earnings in-line to achieve FY18E forecast**

First Capital Research maintains Earnings Forecast with results falling in-line: As expected consumer goods sector, the previous front-runner of the group, continued to remain slow amidst the tight economic conditions and tax effects. However, Transportation and Finance sector performance helped to fill the vacuum created by the lower profitability in the leisure sector, consumer foods and retail segment. We maintain our FY18E and FY19E forecast on expectations of a slow rise in retail business boosting earnings in FY19E. It is also important to keep a close tab on the Group’s integrated resort project which begins to recognize revenue and boost earnings in FY20E and beyond. JKH’s property arm has also finalised the design for a new 800-apartment joint venture residential development project titled ‘Tri-Zen’ in Union Place, Colombo and the schematic designs are currently underway, which is not factored into the valuation. The progress of the project is the key catalyst to alleviate and re-rate JKH. First Capital Research maintains fair value for JKH for FY19E at LKR 210.0 while re-iterating a **STRONG BUY**

**3QFY18 earnings dipped by 13.0%YoY:** JKH recorded earning of LKR 4.5Bn in 3QFY18 dipped by 13.0%YoY, despite net earnings for 1HFY18 declined by c.2.1%YoY to LKR 11.0Bn which is broadly in-line with our forecast for FY18E. The quarterly earnings were largely backed by Transportation and Financial Services. JKH’s gross margins narrowed by c.707bps YoY to 22.1% for the quarter mainly due to c.23%YoY growth in cost of sales.



**JKH topline grew by c.12%YoY to LKR 31.2Bn:** Revenue growth was largely dominated by c.50%YoY growth in Transportation, c.30%YoY growth in financial services and c.13%YoY growth in Consumer & retail segments.

**Bare performance in city and resort hit Leisure:** Leisure EBIT for 3QFY18 dropped by 33.5%YoY to LKR 845.9Mn from LKR 1.27Bn due to decline in occupancies witnessed in City Hotel, primarily as a result of the increase in room inventory within Colombo. Furthermore, SriLankan resorts also underperformed due to the absence of revenue recognition from Bentota Beach Hotel (which was closed down on 1st July'17). Maldivian resorts segment recorded an improvement in Average room rates (ARRs), although profitability was impacted by lower occupancies and the partial closure of "Ellaidhoo Maldives by Cinnamon" for refurbishments in October 2017.

**Declined Volume and Sugar Tax impacted CF&R:** CF&R segment EBIT dipped by 27%YoY to LKR 896.5Mn from LKR 1.2Bn mainly on account of the decline in profitability on account of the consumer goods sector and to lesser extent the retail sector. The Beverage and Frozen Confectionery businesses recorded a decline in volumes as a result of continued tapering of demand arising from subdued consumer discretionary spending. The volume decline in the Beverage business was further exacerbated by the implementation of a sugar tax from November 2017, which resulted in substantial price increases across the industry. Hence manufacturing segment saw c.6.4%YoY decline in topline and c.46%YoY decline in EBIT in 3QFY18. EBIT margins also narrowed by c.833 bps to 11.26%. The retail business saw a topline growth of c.22%YoY to LKR 9.8Bn during the quarter despite segmental EBIT falling by c.8.8%YoY owing to higher OPEX incurred through the 3 new supermarkets opened during the period and the total outlets as of end 3QFY18 stood at 73.

**Moderate growth in volume maintained Transportation profitability:** The sector topline was up by 50%YoY to LKR 4.89Bn whilst bottom line was also up by 8.2%YoY to LKR 884.4Mn during the quarter under review due to better performance in bunkering business. South Asia Gateway Terminals (SAGT) saw c.8%YoY growth in TEU volumes to 479,535 in 3QFY18 which led to only c.7%YoY growth in associate income.

**Financial services segment recorded substantial growth:** Financial sector bottom-line for 3QFY18 increased by 45.5% to LKR 1.54Bn from LKR 1.14Bn in 3QFY17 mainly driven through increase in profitability of Union Assurance, where gross written premiums recorded strong growth whilst NTB recorded sound loan growth during the quarter under review.

### Investment case

**JKH to provide a return of c.30%:** First Capital Research estimates JKH's fair value at LKR 210.0 based on a sum-of-the-parts valuation for FY19E, providing a total return of 36% (capital gain 33%, dividend yield 3%). The annualized return is 30% in 2019E. **STRONG BUY.**

**Life to Cinnamon's Life beyond FY19:** First Capital Research expects Cinnamon Life's construction full completion by end FY20, compared to previous target of FY19. Pre-sales of both residential and commercial space continue to be encouraging. At the time of launch, pre-bookings for 'The Suites at Cinnamon Life' have exceeded 15%, whilst over 50% of the floor space of the first residential tower 'The Residence at Cinnamon Life' has already been sold. The growth in living standards and incomes, coupled with the anticipated influx of tourists in the future is expected to drive demand for real estate.

**Consumer demand drive:** The penetration of consumer food products continues to be comparatively low with per capita consumption of carbonated soft drinks and ice creams in Sri Lanka currently standing at 10 liters and 2 liters respectively, significantly below the regional average, highlighting the

potential for continued long term growth in these categories. In light of the opportunities that lie ahead, Ceylon Cold Stores CCS is committing to enhancing capacity with investments of LKR 3.8Bn in constructing a new ice cream factory and a further investment of LKR 2.5Bn in a new bottling facility for beverages. Jaykay Marketing services Pvt Ltd (JMSL) will continue to rapidly expand its outlet footprint, whilst constructing a new distribution centre, at an estimated investment of approximately LKR 3.2Bn.

**Bentota Beach by Cinnamon to 5-Star:** The Current bentota beach hotel a 4-star 133 property will become 5-star establishment with 151 rooms cost approximately LKR 4Bn, which expected to be commenced by FY20.

### Investment risks

**Headline risk:** Macro-economic and political environment policy uncertainty and the volatility of the economic environment - both locally and globally can affect the business segment of JKH.

**Exchange rate risk:** JKH exposed to exchange rate risk in relation to USD395mn syndicated loan facility, obtained by Waterfront Properties (Private) Limited for the development of "Cinnamon Life" project.

**Interest rate risk:** Movement in interest rates through CBSL monetary policy influences aggregate consumer demand which affect most of JKH's segments.

**Regulatory Risk:** A degree of uncertainty and volatility still prevails as a result of transitioning legal, regulatory and tax structures impact of the some JKH segments.



## Valuation Summary

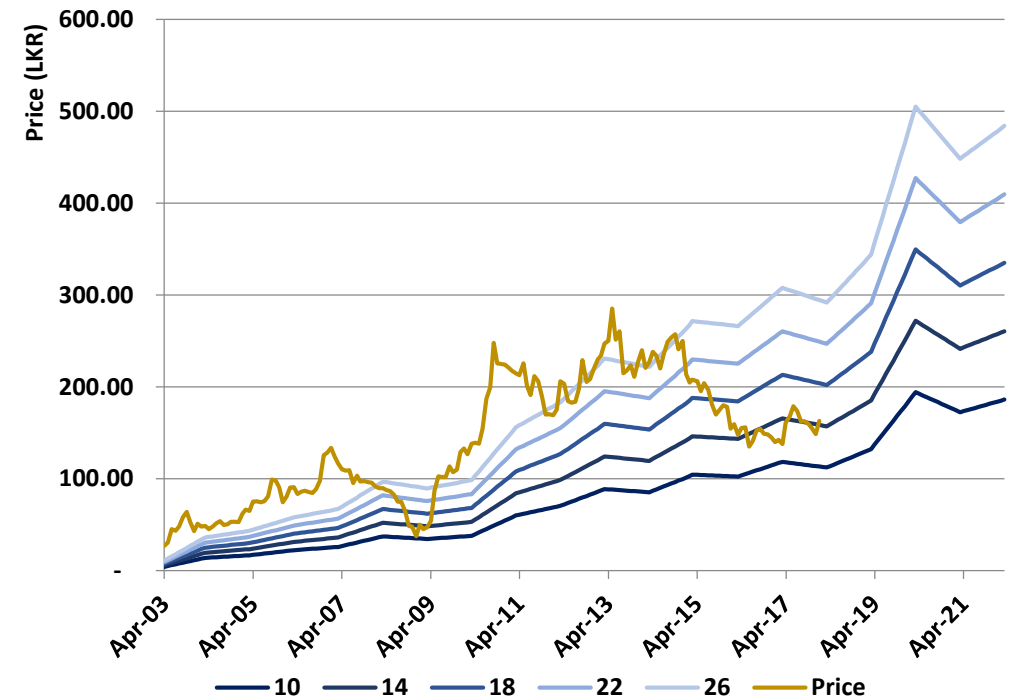
Segment	Valuation method	Valuation assumptions				Value in LKR Mn		Value per share	% of total
		D/E	CoE	WACC	Growth	Firm value	Equity		
Transportation	DCF	48/52	17%	14%	3%	14,064		10.1	7%
Leisure	DCF	40/60	17%	15%	3%	36,619		30.2	20%
Property	DCF	34/66	15%	13%	1%	41,808		30.2	20%
Consumer Foods & Retail	DCF	34/66	17%	14%	3%	100,797		72.7	48%
Financial Services	Justified PBV		16%		3%		10,336	7.5	5%
Information Technology	PBV						3,323	2.4	2%
Fair value before net debt								153.0	100%
Less: Debt								8.7	
Add: Cash								6.2	
Add: Short Term Investment								58.8	
<b>Fair value</b>								<b>209.4</b>	

## Annex I – Income Statement

Income Statement (LKR mn) Y/E 31st March	FY16	FY17	FY18E	FY19E	FY20E
<b>Revenue</b>	<b>93,709</b>	<b>106,273</b>	<b>122,913</b>	<b>139,675</b>	<b>179,087</b>
<b>EBIT by Sector</b>					
Transportation	560	2,652	776	853	924
Leisure	5,028	5,714	3,634	5,531	6,207
Property	1,620	541	300	330	9,273
Consumer Foods & Retail	4,322	5,147	5,645	6,532	7,796
Financial Services	717	935	1,066	1,243	1,449
Information Technology	-334	-572	428	471	519
Other	-1,681	-2,078	-822	-804	-731
<b>EBIT</b>	<b>10,303</b>	<b>12,339</b>	<b>11,026</b>	<b>14,156</b>	<b>25,436</b>
Finance Cost	-392	-419	-786	-550	-385
Finance Income	5,549	6,717	6,366	6,461	6,460
Change in fair value of inv. property	263	484	650	650	650
Share of profit of Associates	2,781	3,303	3,643	3,953	4,276
Adjustments	763	464	511	562	618
<b>PBT</b>	<b>19,198</b>	<b>22,888</b>	<b>21,409</b>	<b>25,232</b>	<b>37,055</b>
Taxation	-3,406	-4,771	-4,463	-5,260	-7,724
<b>Net profit for the period</b>	<b>15,792</b>	<b>18,117</b>	<b>16,946</b>	<b>19,972</b>	<b>29,331</b>
Minority Interest	-1,722	-1,842	-1,525	-1,798	-2,640
<b>Profit attributable to Equity Holders</b>	<b>14,070</b>	<b>16,275</b>	<b>15,421</b>	<b>18,175</b>	<b>26,691</b>
<b>Adjusted EPS</b>	<b>10.2</b>	<b>11.8</b>	<b>11.2</b>	<b>13.2</b>	<b>19.4</b>

Source: Company Annual Reports and First Capital Research Estimates

## PER Valuation



Source: First Capital Research Estimates

## 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%

Note: 1 year T-bill rate as of 30<sup>th</sup> Jan 2018: 8.90%



## Annex II – Balance Sheet

Balance Sheet (LKR mn)	FY16	FY17	FY18E	FY19E	FY20E
<b>As at 31st March</b>					
<b>Non current assets</b>					
Property plant and equipment	52,736	64,396	66,287	67,925	69,312
Investment Property	4,878	5,366	6,010	6,731	7,539
Intangible Assets	2,338	2,118	2,118	2,118	2,118
Other Investments	16,950	17,719	21,361	25,315	29,591
Other Non Current Financial Asse	22,635	27,667	29,050	29,340	31,394
Other Non Current Assets	46,575	55,042	56,694	58,394	58,978
	<b>146,113</b>	<b>172,309</b>	<b>181,520</b>	<b>189,825</b>	<b>198,933</b>
<b>Current Assets</b>					
Inventories	4,665	5,606	6,483	7,368	9,447
Trade and Other Receivables	9,999	11,687	13,517	15,361	19,695
Amounts due from related parties	133	112	112	112	112
Other Current Assets	2,303	3,265	3,265	3,265	3,265
Short Term Investments	72,635	79,174	79,966	81,565	79,934
Cash and cash equivalents	5,127	5,119	2,174	8,658	25,762
	<b>94,863</b>	<b>104,964</b>	<b>105,518</b>	<b>116,328</b>	<b>138,215</b>
<b>Total Assets</b>	<b>240,976</b>	<b>277,272</b>	<b>287,039</b>	<b>306,153</b>	<b>337,148</b>
<b>Equity and Liabilities</b>					
<b>Capital and reserves</b>					
Ordinary shares	58,702	62,790	62,790	62,790	62,790
Reserves	96,280	115,845	126,639	139,362	158,046
Shareholders Funds	154,982	178,635	189,430	202,152	220,836
Minority Interest	13,499	15,696	17,221	19,018	21,658
	<b>168,480</b>	<b>194,330</b>	<b>206,650</b>	<b>221,170</b>	<b>242,494</b>
<b>Non - current liabilities</b>					
Insurance contract Liabilities	27,205	31,700	36,455	41,924	48,212
Borrowings	13,707	14,203	9,942	6,959	4,872
Employee benefit liabilities	1,661	1,880	1,880	1,880	1,880
Other	5,986	7,109	7,820	8,602	9,462
	<b>48,559</b>	<b>54,892</b>	<b>56,097</b>	<b>59,365</b>	<b>64,426</b>
<b>Current liabilities</b>					
Trade and other payables	12,755	14,136	16,349	18,579	23,822
Amounts due to related parties	29	10	10	10	10
Current tax liabilities	1,873	2,395	2,395	2,395	2,395
Borrowings	3,813	4,299	3,009	2,107	1,475
Other	2,235	2,944	2,944	2,944	2,944
Bank overdraft	3,230	4,264	4,264	4,264	4,264
	<b>23,936</b>	<b>28,049</b>	<b>28,973</b>	<b>30,300</b>	<b>34,910</b>
<b>Total liabilities</b>	<b>72,495</b>	<b>82,941</b>	<b>85,070</b>	<b>89,665</b>	<b>99,336</b>
<b>Total equity &amp; liabilities</b>	<b>240,975</b>	<b>277,272</b>	<b>291,720</b>	<b>310,835</b>	<b>341,830</b>
<b>NAVPS</b>	<b>112.8</b>	<b>130.0</b>	<b>137.8</b>	<b>147.1</b>	<b>160.7</b>

Source: Company Annual Reports and First Capital Research Estimates

## Annex III – Cash Flow Statement

Cashflow Statement (LKR mn)	FY16	FY17	FY18E	FY19E	FY20E
<b>Y/E 31st March</b>					
<b>Profit before tax</b>	<b>19,198</b>	<b>22,888</b>	<b>21,409</b>	<b>25,232</b>	<b>37,055</b>
Adjustments	-4,621	-8,646	-6,112	-6,503	-6,737
Net Change in Working Capital	-27	-467	1,660	3,201	3,911
<b>Operating Activities</b>					
Interest Received	8,118	9,536	6,366	6,461	6,460
Inerest Paid	-956	-303	-786	-550	-385
Dividend Received	2,588	2,854	0	0	0
Tax Paid	-2,520	-4,631	-4,463	-5,260	-7,724
Gratuity Paid	-171	-219	0	0	0
<b>Cash from operations</b>	<b>20,513</b>	<b>21,013</b>	<b>18,073</b>	<b>22,582</b>	<b>32,579</b>
<b>Investing activities</b>					
Net PPE, Intangible Assets and Inv. Prop	-5,358	-7,107	-5,644	-5,721	-5,808
Acquisition and Increased stakes	-53	-44	0	0	0
Net other Non Current investments	-4,155	-10,519	0	0	0
<b>Cash from investments</b>	<b>-9,567</b>	<b>-17,670</b>	<b>-5,644</b>	<b>-5,721</b>	<b>-5,808</b>
<b>Financing Activities</b>					
Proceeds from New Share Issue	7,999	4,088	0	0	0
Net proceeds from loans & borrowings	-5,989	416	-5,551	-3,885	-2,720
Dividends	-8,038	-7,280	-4,626	-5,452	-8,007
Other	-1,690	-1,329	0	0	0
<b>Cash from financing</b>	<b>-7,717</b>	<b>-4,105</b>	<b>-10,177</b>	<b>-9,338</b>	<b>-10,727</b>
<b>Net cash during the year</b>	<b>3,229</b>	<b>-762</b>	<b>2,252</b>	<b>7,523</b>	<b>16,044</b>
Net cash at beginning	45,169	48,398	47,636	49,888	57,411
<b>Net cash at end</b>	<b>48,398</b>	<b>47,636</b>	<b>49,888</b>	<b>57,411</b>	<b>73,455</b>
Cash of Balance Sheet	5,127	5,119	2,174	8,658	25,762
Short Term Investments	47,213	51,463	51,978	53,018	51,957
Bank O/D	-3,230	-4,264	-4,264	-4,264	-4,264
<b>Net cash from Cashflow</b>	<b>48,398</b>	<b>47,636</b>	<b>49,888</b>	<b>57,411</b>	<b>73,455</b>

Source: Company Annual Reports and First Capital Research Estimates





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