

**JOHN KEELLS HOLDINGS PLC [JKH.N0000]****MAINTAIN BUY****“EARNINGS FALTER YET OUTLOOK REMAINS INTACT”****Fair Value: FY23E - LKR 160.0 [+15%]**

Total Return with DPS: FY23E - +16% [AER +46%]

FY24E - LKR 180.0 [+29%]

FY24E - 31% [AER 21%]

JKH reported a decline in net earnings of 43.9%YoY (-85.8%QoQ) to LKR 1,605.0Mn owing to the poor performance of the property segment and significant rise in finance costs (+137.4%YoY and +17.8%QoQ) due to record high interest rates on working capital borrowings. Moreover, decline in profitability of JKH Retail segment, which was affected by poor performance of the office automation business and contraction in margins at the supermarket business, also contributed towards the decline in profitability. Meanwhile, Transportation business continued to thrive backed by increasing volumes at the SAGT terminal and higher margins from bunkering business whilst Consumer Foods segment shined as volumes of both beverages and frozen confectionary businesses grew, whereas price increases of products enabled JKH to keep margins intact amidst rising input costs. Leisure segment continued its recovery momentum with strong growth in occupancies and ARR at all key segments including Colombo Hotels, Sri Lankan Resorts and Maldivian Resorts. Given the subpar performance of the property segment and Retail segment, as disposable income weakens and apartment sales slows-down, we have cut the earnings forecast for FY23E by 14.4% to LKR 23,384.6Mn whilst reducing the TP to LKR 160.0 from LKR 162.2. However, we have increased our earnings forecast for FY24E by 10.6% to LKR 33,650.4Mn and TP to LKR 180.0 from LKR 169.0, taking in to consideration the revival of tourism, continued volume growth and relatively higher margins of transportation segment and return of disposable incomes owing to salary adjustments. Furthermore, Cinnamon Life 800 keyed hotel and office complex are also expected to boost leisure sector profitability during FY24E. Hence, given the strong upside and positive outlook of the company, we have maintained our recommendation at **BUY**.

LKR (Mn)	2QFY22	2QFY23	YoY	1HFY22	1HFY23	YoY
Earnings (LKR 'Mn)						
Revenue	49,269	69,065	+40%	88,068	140,581	+60%
Gross Profit	7,155	10,683	+49%	12,196	24,490	+101%
Operating Profit	2,685	2,873	+7%	2,961	5,825	+97%
PBT	2,833	2,564	-10%	4,143	17,365	+319%
Net Profit	2,861	1,605	-44%	4,395	12,882	+193%
Balance Sheet (LKR 'Mn)						
Shareholder's Equity	229,710	363,549	+58%	229,710	363,549	+58%
Borrowings	150,577	210,733	+40%	150,577	210,733	+40%

JKH net earnings down 43.9%YoY for 2QFY23

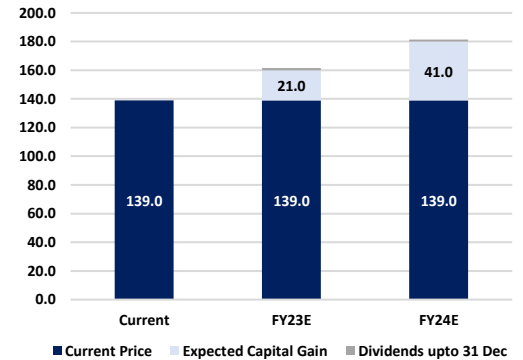
JKH net earnings reported a decline of 43.9%YoY (-85.8%QoQ) to LKR 1,605.0Mn owing to the poor performance of the property segment (posted a loss of LKR 405.2Mn cf. a profit of LKR 1,122.2Mn in 2QFY22), and increased finance expenses due to the significant rise in interest rates on working capital. The loss incurred at the property segment was largely attributable to the revenue and profit recognition from the sold apartments at Cinnamon Life during 2QFY22. Moreover, affected by the adverse operating environment, Retail sector profitability was dragged down by the office automation arm, which continued to witness reduction in sales volume due to restrictions on imports and notable growth in finance costs (+138.1%YoY). Meanwhile on a positive note, JKH transportation segment continued to thrive during 2QFY23 as volume handled at the SAGT terminal improved by 1.8%YoY whilst margins at LMS continued to strengthen benefitted by easing oil prices and translation impact due to Rupee depreciation. Despite the continued pressure from rising input costs (skimmed milk and sugar prices), Consumer Foods segment reported a profit growth of 52.1%YoY to LKR 478.1Mn driven by volumes in both beverages (+13%YoY) and frozen confectionary (+6%YoY) businesses. Furthermore, profit increase during 2QFY23 was also supported by the price increases and forward buying of raw materials. Meanwhile leisure segment continued its recovery momentum and marginally narrowed down the loss to LKR 1,163.7Mn in 2QFY23 cf. a loss of LKR 1,270.9Mn as both occupancies and ARRs improved in Colombo Hotels (occupancies improved to 29% from 20% whilst ARR improved to USD 62.0 from USD 54.0 in 2QFY22), Sri Lankan Resorts (occupancies up 31% from 18% and ARR up USD 57.0 from USD 38.0) and Maldivian resorts (occupancies up 86.0% from 76.0% whilst ARR up USD 316.0 from USD 262.0). However, rising finance costs due to higher interest rates of WC together with translation impact stemming from the amortization of leases across Maldivian resorts negatively affected towards the segmental bottom-line during the quarter. Meanwhile, Financial Services segment recorded a marginal 1.8%YoY growth in profitability to LKR 993.9Mn as both UAL and NTB posted marginal growth.

Cinnamon Life and West Container Terminal (WCT) on track for completion

As per the management, Cinnamon Life, which is a USD 1.0Bn investment is on track for completion during the 2HFY24. During August 2022, government gazetted the regulations under the Casino Business Act of 2010 to formalize the process of issuing of licenses and monitoring of operations for casinos in Sri Lanka. With this move, JKH strongly believes that group can finalize the process on a casino operator by 4QFY23 and launch the Cinnamon Life Hotel and office complex by 1HFY23. Meanwhile with regards to the West Container Terminal (WCT) project, construction work commenced on 9th November 2022 and the management have guided that the full completion of the project is scheduled for December 2025. With possible restructuring and privatization of state-owned enterprises on the cards, JKH management signaled that the group is actively interested in taking part of any on-going talks, in-order to consolidate market shares in already operational business segments.

JKH earnings and target prices revised

JKH performance during the 2QFY23 came 29% below our estimate of LKR 2,271.9Mn owing to the poor performance of the property segment and rising finance costs due to increased working capital financing. Given the subpar performance of the property segment and dampened operational climate amidst contraction in disposable incomes and increases in both direct and indirect taxes, we have cut our earnings for FY23E by 14.4% to LKR 23,384.6Mn whilst reducing the TP to LKR 160.0 from LKR 162.2. However, going forward in FY24 we expect Sri Lanka to witness near pre-pandemic arrivals boosting the leisure segment earnings whilst transportation segment is expected to enjoy relatively high margins amidst easing freight rates and easing oil prices. Moreover, disposable incomes are expected to improve as corporates increase salaries in lieu with record high inflation levels, which we believe would revive JKH retail segment as both basket value and footfall increases. Furthermore Consumer Foods segment is expected to witness volume growth whilst, near peaked global prices of key ingredients is expected to ease off resulting in margin expansion. Hence taking in to consideration the future outlook, we have revised up our earnings for FY24E by 10.6% to LKR 33,650.4Mn whilst raising the TP to LKR 180.0 from LKR 169.0. Given the strong upside to the share, we maintain our recommendation **BUY**.

**FIRST CAPITAL RESEARCH**

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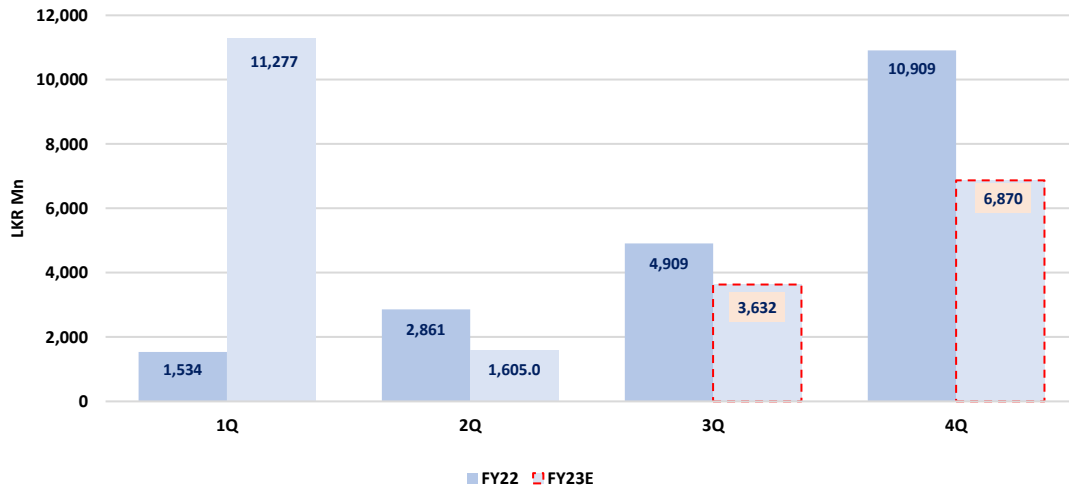
Buy Below FY23E - [AER of 20% with DPS]: LKR 149.6
JKH categorized as 'Grade A' counter

Disclosure on Shareholding:

First Capital Group or the covering analyst did not hold 1% or more of the total outstanding share capital of JKH during the five trading days prior to the issuance of this document.



Quarterly Earnings



Estimate Revision

In LKR Mn	FY23E-O	FY23E-R	% Change	FY24E-O	FY24E-R	% Change
Earnings Estimate						
Revenue	251,015	282,641	+12.6%	295,237	329,342	+11.6%
Gross Profit	40,162	45,223	+12.6%	48,714	54,341	+11.6%
EBIT	13,101	15,093	+15.2%	18,054	22,536	+24.8%
Profit before Tax	34,249	30,221	-11.8%	37,878	43,545	+15.0%
Net Profit	27,326	23,385	-14.4%	30,428	33,650	+10.6%
Adjusted EPS	20.5	17.5		22.8	25.2	
Growth YoY	35%	16%		11%	44%	
Balance Sheet Estimate						
Shareholders' Equity	336,069	332,667	-1%	365,033	364,313	-0%
Borrowings	192,400	192,900	+0%	166,000	166,000	0%
Adjusted NAVPS	252.0	249.0		273.2	272.7	
Ratio Estimate						
ROE (%)	8%	7%		8%	9%	
PER (x)	6.8	7.9		6.1	5.5	
PBV (x)	0.6	0.6		0.5	0.5	

Valuation Table

YE Mar/LKR Mn	FY20	FY21	FY22	FY23E	FY24E	FY25E
Estimates (LKR 'Mn)						
Revenue	138,956	127,676	218,075	282,641	329,342	357,166
Gross profit	26,082	18,929	37,645	45,223	54,341	60,718
EBIT	6,789	2,552	7,308	15,093	22,536	25,581
Net Profit	9,414	4,772	20,213	23,385	33,650	34,906
Adjusted EPS (LKR)	7.0	3.6	15.1	17.5	25.2	26.1
YoY Growth (%)	38%	-49%	324%	16%	44%	4%
Valuations						
PER (x)	19.7x	38.9x	9.2x	7.9x	5.5x	5.3x
PBV (x)	0.9x	0.8x	0.6x	0.6x	0.5x	0.5x
NAVPS	162.3	169.3	233.0	249.0	272.7	297.3
DY (%)	2.5%	1.1%	1.1%	1.1%	1.1%	1.1%
DPS (LKR)	3.50	1.50	1.50	1.50	1.50	1.50
Dividend Payout (%)	49.7%	42.0%	9.9%	8.6%	6.0%	5.7%



SOTP

Segment	Valuation method	Valuation assumptions			Value in LKR Mn			Value per share FY23E	Value per share FY24E
		CoE	WACC	Growth	Firm value FY23E	Firm value FY24E	% of ownership		
Transportation	DCF	22.2%	13.9%	5.0%	126,053.6	124,726.2	80%	100,842.8	99,781.0
Consumer Foods	DCF	22.2%	13.9%	5.0%	46,771.7	47,370.2	85%	39,756.0	40,264.7
Retail	DCF	22.2%	13.9%	5.0%	43,855.1	39,434.3	85%	37,276.9	33,519.2
Leisure	DCF	23.0%	14.7%	5.0%	27,555.2	29,327.5	80%	22,044.2	23,462.0
Property	DCF	24.6%	17.0%	5.0%	18,141.0	28,245.2	95%	17,234.0	26,833.0
Financial Services	DCF	23.0%	16.0%	5.0%	12,135.6	12,934.0	60%	7,281.4	7,760.4
Other	DCF	23.0%	14.3%	5.0%	2,902.8	3,230.4	60%	1,741.7	1,938.2
Total per share								226,176.9	233,558.4
Number of shares								1,336.0	1,336.0
Value/share								169.29	174.82

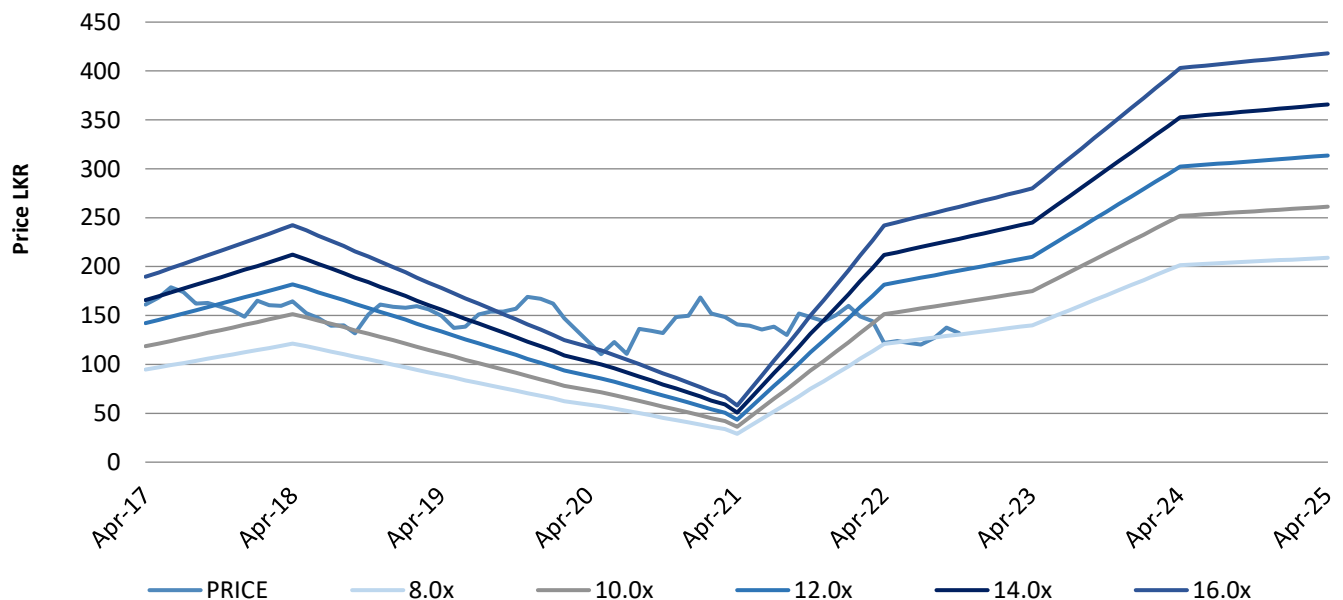
Valuation Summary

Expected JKH Price	FY23E	FY24E	Return	FY23E	FY24E
PER Valuation based target price	148.6	188.9	Target Price	160.0	180.0
SOTP Valuation based target price	169.3	174.8	Current Price	139.0	139.0
Average Target Price	158.9	181.9	Capital Gain (LKR)	21.0	41.0
Target Price after Rounding off	160.0	180.0	Dividends upto 31 Mar (LKR)	1.5	1.5
			Capital Gain %	15%	29%
			Dividend Yield %	1%	1%
			Total Return %	16%	31%
			Annualized Return %	50%	21%

PER valuation

PER based Valuation	FY23E	FY24E
Earnings (LKR 'Mn)	23,385	33,650
No. of Shares ('Mn)	1,336	1,336
EPS	17.5	25.2
Expected PER	8x	8x
Price at 8x Earnings	148.6	188.9

PER Chart



Appendix I: Statement of Income and Expenses

Income Statement	FY20	FY21	FY22	FY23E	FY24E	FY25E
Year ended 31st March (LKR 'Mn)						
Total revenue	138,956	127,676	218,075	282,641	329,342	357,166
Cost of sales	(112,874)	(108,747)	(180,430)	(237,418)	(275,001)	(296,448)
Gross profit	26,082	18,929	37,645	45,223	54,341	60,718
Selling and distribution expenses	(5,519)	(4,761)	(5,733)	(7,430)	(8,658)	(9,389)
Administrative expenses	(13,143)	(12,928)	(14,763)	(22,611)	(29,641)	(35,717)
Other operating expenses	(2,873)	(1,314)	(12,456)	(8,479)	(9,880)	(10,715)
Results from operating activities	6,789	2,552	7,308	15,093	22,536	25,581
Finance cost	(3,166)	(4,669)	(7,035)	(10,463)	(6,556)	(4,884)
Finance income	9,357	10,689	30,806	17,292	19,512	15,187
Change in insurance contract liabilities	(5,617)	(7,032)	(6,416)	(8,479)	(9,880)	(10,715)
Share of results of equity accounted investees (net of tax)	4,466	4,159	6,746	8,009	7,763	8,651
Profit before tax	12,403	5,445	27,324	30,221	43,545	44,826
Tax expense	(2,662)	(1,494)	(6,882)	(6,570)	(9,512)	(9,523)
Profit for the year	9,741	3,951	20,443	23,651	34,033	35,303
Attributable to:						
Equity holders of the parent	9,414	4,772	20,213	23,385	33,650	34,906
Non-controlling interests	327	(821)	230	266	383	397
	9,741	3,951	20,443	23,651	34,033	35,303
EPS	7.14	3.62	15.13	17.50	25.19	26.13

Appendix II: Statement of Financial Position

Balance Sheet	FY20	FY21	FY22	FY23E	FY24E	FY25E
Year ended 31st March (LKR 'Mn)						
ASSETS						
Non-current assets						
Property, plant and equipment	111,534	113,077	124,348	131,834	141,163	149,996
Right-of-use assets	37,170	40,617	53,482	52,930	52,850	53,036
Investment property	15,008	14,868	30,608	30,808	31,008	31,208
Intangible assets	3,289	4,853	5,399	6,320	7,388	8,474
Investments in equity accounted investees	28,329	28,630	33,866	33,866	33,866	33,866
Non-current financial assets	40,078	62,590	48,690	48,690	48,690	48,690
Deferred tax assets	902	1,089	1,554	1,554	1,554	1,554
Other non-current assets	79,583	104,580	180,920	180,920	180,920	180,920
	315,894	370,303	478,867	486,921	497,439	507,744
Current assets						
Inventories	50,169	54,296	36,225	47,666	55,212	59,518
Trade and other receivables	12,186	17,457	27,495	35,636	41,524	45,032
Amounts due from related parties	390	124	196	196	196	196
Other current assets	6,513	5,919	11,914	15,442	17,994	19,514
Short term investments	38,458	69,263	110,722	131,861	123,650	116,067
Cash in hand and at bank	13,334	19,433	52,377	15,627	15,195	33,354
	121,050	166,491	238,929	246,428	253,770	273,681
Total assets	436,944	536,794	717,796	733,349	751,210	781,426
EQUITY AND LIABILITIES						
Equity attributable to equity holders of the parent						
Stated capital	62,881	63,102	73,188	73,188	73,188	73,188
Revenue reserves	87,885	90,652	109,087	130,468	162,114	195,016
Other components of equity	66,085	72,403	129,011	129,011	129,011	129,011
	216,852	226,157	311,286	332,667	364,313	397,215
Non-controlling interest	26,872	16,830	18,805	19,071	19,454	19,851
Total equity	243,724	242,987	330,091	351,738	383,767	417,066
Non-current liabilities						
Insurance contract liabilities	38,186	45,161	51,349	51,349	51,349	51,349
Interest-bearing loans and borrowings	50,925	118,966	158,922	151,100	131,507	126,109
Lease liabilities	19,910	24,235	30,067	31,974	34,472	37,199
Deferred tax liabilities	8,295	7,720	12,016	12,016	12,016	12,016
Employee benefit liabilities	2,344	2,814	3,107	3,107	3,107	3,107
Non-current financial liabilities	3,620	3,661	2,414	2,414	2,414	2,414
Other non-current liabilities	12,614	19,546	220	220	220	220
	135,894	222,102	258,095	252,181	235,085	232,415
Current liabilities						
Trade and other payables	23,881	35,288	43,469	57,199	66,253	71,421
Amounts due to related parties	2	1	2	2	2	2
Income tax liabilities	1,748	1,988	2,619	2,619	2,619	2,619
Short term borrowings	5,804	6,904	14,833	14,000	11,500	11,000
Interest-bearing loans and borrowings	5,206	9,507	40,624	27,800	22,993	17,091
Lease liabilities	1,383	1,472	3,459	3,679	3,966	4,280
Other current liabilities	1,623	1,733	4,280	5,632	6,524	7,033
Bank overdrafts	17,679	11,820	20,322	18,500	18,500	18,500
	57,326	71,705	129,609	129,431	132,357	131,945
Total equity and liabilities	436,944	536,794	717,796	733,349	751,210	781,426
Net Asset Value	162.31	169.28	232.99	249.00	272.68	297.31



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