

**HEMAS HOLDINGS PLC [HHL.N0000]****UPGRADE TO BUY****“DEFENSIVE GIANT REPORTS EARNINGS IN LINE WITH OUR ESTIMATES”**

Fair Value: FY24E - LKR 85.0 [+21%] **Fair Value: FY25E - LKR 95.0 [+36%]**
Total Return with DPS: FY24E - 26% [AER 90%] **FY25E - 41% [AER 29%]**

HHL's earnings grew by 6.0%YoY to LKR 1.2Bn in 2QFY24, driven by a 10.0%YoY increase in revenue to LKR 29.8Bn. However, a marginal contraction in EBIT margin from 9.9% to 9.3% was witnessed in 2QFY24 amidst the steep rise in operating expenses. The topline growth was notably contributed by Consumer and Healthcare segments, while Mobility sector experienced negative growth amid challenging operating conditions. Despite a revenue surge, the profit margins of the Healthcare segment remained under pressure due to the MRP reduction of essential drugs and a spike in finance costs. However, it was offset by the growth in Consumer brands earnings which surged by 67.3%YoY in 2QFY24, accompanied by a 286bps expansion in profit margins. Looking ahead, the group is poised to benefit from an improving operating environment, driven by a declining trend in inflation. Meanwhile, the stable outlook on the currency is expected to further benefit the company, given its status as a net importer across the segment. As the reported earnings are in line with our forecast, we broadly maintain the earnings target for FY24E and FY25E at LKR 5.6Bn and LKR 6.7Bn, respectively. Hence, we maintain the FV at LKR 85.0 for FY24E and LKR 95.0 for FY25E. Since the previous report in Aug 2023, the stock price has significantly underperformed compared to the ASPI, declining from our FY24E FV of LKR 85.0 to the current market price. Hence, considering the outlook and potential return of the stock, we revised our recommendation.

UPGRADE TO BUY

LKR (Mn)	2QFY23	2QFY24	YoY	1HFY23	1HFY24	YoY
Earnings (LKR 'Mn)						
Revenue	27,119	29,829	+10%	51,960	58,951	+13%
Gross profit	7,593	8,655	+14%	13,932	16,510	+19%
EBIT	2,693	2,767	+3%	4,724	4,920	+4%
PBT	1,897	2,004	+6%	3,817	3,415	-11%
Net Profit-Equity holders	1,151	1,220	+6%	2,231	2,313	+4%
Balance Sheet (LKR 'Mn)						
Shareholders' Equity	38,894	35,138	-10%	38,894	35,138	-10%
Borrowings	22,187	20,230	-9%	22,187	20,230	-9%
NAVPS	65.2	58.9		65.2	58.9	

Consumer brands' profitability surges amidst margin expansions

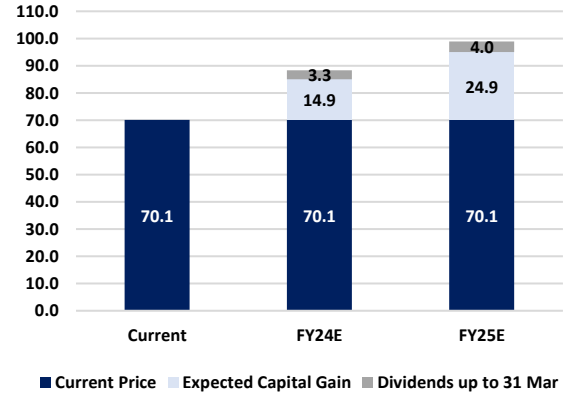
HHL's Consumer segment witnessed robust YoY earnings growth of 67.3% (12.2%QoQ) to LKR 1.0Bn, attributed to a 22.0%YoY growth in EBIT to LKR 1.5Bn (+28.8%QoQ). Amidst the decline in raw material prices (Palm oil: -8.7%YoY, Paper: -17.7%YoY) and currency appreciation (+10.6%YoY), EBIT margin further expanded by 85bps (+245bps on a QoQ basis) reaching 12.8%. Although revenue depicted a 13.9%YoY growth to LKR 11.5Bn, primarily due to a surge in average selling prices, overall volume experienced a slowdown as consumption remained stagnant on the back of increased tariffs on electricity and tax reforms which had a pronounced effect on consumer spending. On a positive note, the focus on new product launches in the beauty segment under the 'Prasara' and 'Vivya' brands resulted in robust volume growth. Despite a challenging environment in Bangladesh, 'Kumarika' and 'Eva' recorded double-digit volume growth, supported by the launch of value-for-money product ranges, and the new product range 'Kolombo' gained traction. Additionally, the learning segment, comprising Atlas and Innovate, displayed a 17.2%YoY growth, contributing over 20.0% to the Consumer brands' total revenue. However, challenges may arise for new entrants with the relaxation of the import ban. Looking ahead, HHL aims to concentrate on developing its international business, particularly in Asian, Gulf, and East African regions, while expanding the export portfolio within HPC and Learning segments.

Margin pressure and heightened finance costs dampen Healthcare segment's bottom line

Healthcare segment recorded a topline growth of 8.4% to LKR 17.9Bn in 2QFY24, contributing 60% to the group's revenue. However, this was not translated into the bottom line which reported a marginal growth of 6.0% to LKR 756.9Mn amidst the 18.4%YoY escalation in finance costs, coupled with the margin pressure. Profit margins remained under pressure during the quarter due to a 16% reduction in the MRP of 60 essential drugs mandated by the NMRA which aligned with the exchange rate of LKR 295.0 per dollar, with no subsequent adjustments made to account for adverse movements in exchange rates. However, imported medicines remain more expensive than locally manufactured drugs, presenting an opportunity to bolster local pharma manufacturing. Despite the prevailing challenges in the healthcare industry, there was a deceleration in the rate of contraction in volumes within the private market attributed to increased traction in essential categories. Meanwhile, the Pharmaceutical Manufacturing Arm of the Group continued to focus on the Morison branded portfolio which posted over 70.0% volume growth during 1HFY24. Notably, the Homagama factory surpassed the 50% capacity utilization mark and achieved breakeven driven by Morison brand's venture into third-party contract manufacturing, producing 'Sitagliptin' on behalf of a prominent global player. Moreover, Hospitals reported a growth in revenue, of 5.8%YoY to LKR 1.9Bn amidst the improved occupancy rates over 55% at both hospitals. As per the management, the group is poised to accelerate contract manufacturing, expand into export markets, and explore opportunities for expanding hospital operations. These initiatives are expected to foster growth and potentially enhance the performance of the healthcare segment.

FY24E fair value achieved, FY25E maintained at LKR 95.0 – UPGRADE TO BUY

Given the defensive nature of HHL's key segments, particularly in Healthcare and Consumer, and in anticipation of a recovery in economic activities from 2H2023, we maintain a positive outlook. As HHL's reported earnings align with our forecasts, the earnings targets for FY24E and FY25E are broadly maintained at LKR 5.6Bn and LKR 6.7Bn, respectively. Hence, we maintain the FV at LKR 85.0 for FY24E and LKR 95.0 for FY25E. At current market price of LKR 70.1, HHL provides an annualised return of 29% for FY25E. Considering the outlook and potential return of the stock, we revised our recommendation. **UPGRADE TO BUY**

**FIRST CAPITAL RESEARCH**

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Source: CSE

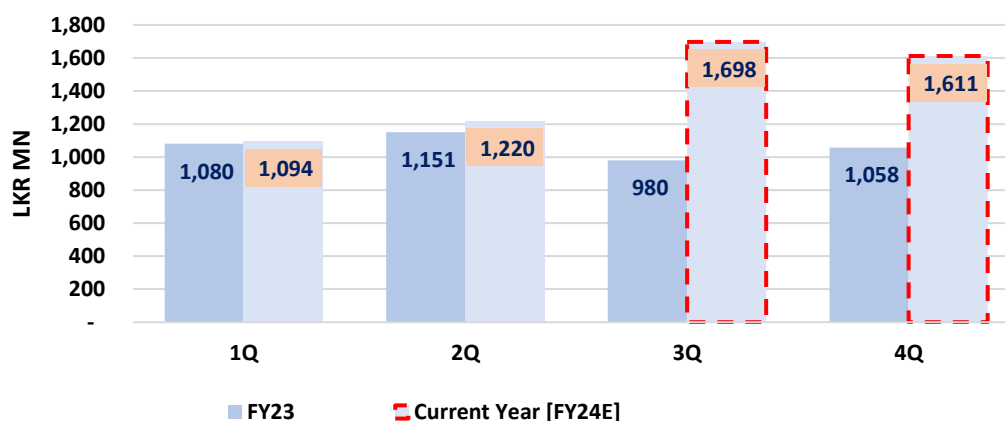
Minimum Return for BUY:

Buy Below for FY25E [AER of 19.0% with DPS]: LKR 78.13
HHL 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 HHL during the five trading days prior to the issuance of this document

Quarterly Earnings



Estimate Revision

In LKR Mn	FY24E-O	FY24E-R	% Change	FY25E-O	FY25E-R	% Change
Earnings Estimate						
Revenue	121,494	121,494	0%	131,723	131,723	0%
Gross Profit	34,140	34,140	0%	37,804	37,804	0%
EBIT	13,315	13,315	0%	15,050	15,050	0%
Profit before tax	9,830	9,830	0%	12,204	12,204	0%
Net Profit	5,623	5,623	0%	6,742	6,742	0%
Adjusted EPS	9.4	9.4	0%	11.3	11.3	0%
Growth YoY	32%	32%		20%	20%	
Balance Sheet Estimate						
Shareholders' Equity	42,058	42,058	0%	46,438	46,438	0%
Borrowings	21,268	21,268	0%	19,038	19,038	0%
Adjusted NAVPS	70.5	70.5		77.8	77.8	
Ratio Estimate						
ROE (%)	13%	13%		15%	15%	
PER (x)	7.4	7.4		6.2	6.2	
PBV (x)	1.0	1.0		0.9	0.9	

Valuation Table

P/E 31 March	FY20	FY21	FY22	FY23	FY24E	FY25E	FY26E
Estimates (LKR 'Mn)							
Revenue	60,043	64,501	78,831	113,940	121,494	131,723	143,295
Gross Profit	19,148	19,417	21,850	31,793	34,140	37,804	41,842
EBIT	3,532	6,061	6,783	10,963	13,315	15,050	16,012
Net Profit	1,236	3,253	4,249	4,269	5,623	6,742	7,450
Adjusted EPS (LKR)	2.1	5.5	7.1	7.2	9.4	11.3	12.5
YoY Growth (%)	-63%	163%	31%	0%	32%	20%	10%
Valuations							
PER (x)	33.8x	12.9x	9.8x	9.8x	7.4x	6.2x	5.6x
PBV (x)	1.5x	1.3x	1.2x	1.1x	1.0x	0.9x	0.8x
DY (%)	0.0%	2.6%	6.9%	3.4%	4.7%	5.6%	6.2%
NAVPS	46.8	53.5	59.7	64.4	70.5	77.8	86.0
DPS (LKR)	-	1.9	4.9	2.4	3.3	4.0	4.4
Dividend Payout	N/A	33.9%	68.1%	32.8%	35.0%	35.0%	35.0%

Valuation Summary

Return	FY24E	FY25E	Expected HHL Price	FY24E	FY25E
Target Price	85.0	95.0	PER Valuation based target price	84.8	101.7
Current Price	70.1	70.1	SOTP Valuation based target price	83.3	96.0
Capital Gain (LKR)	14.90	24.90	Average Target Price	84.1	98.8
Dividends upto 31 Mar (LKR)	3.30	3.96	Target Price after Rounding off	85.0	95.0
Capital Gain %	21%	36%			
Dividend Yield %	5%	6%			
Total Return %	26%	41%			
Annualized Return %	90%	29%			

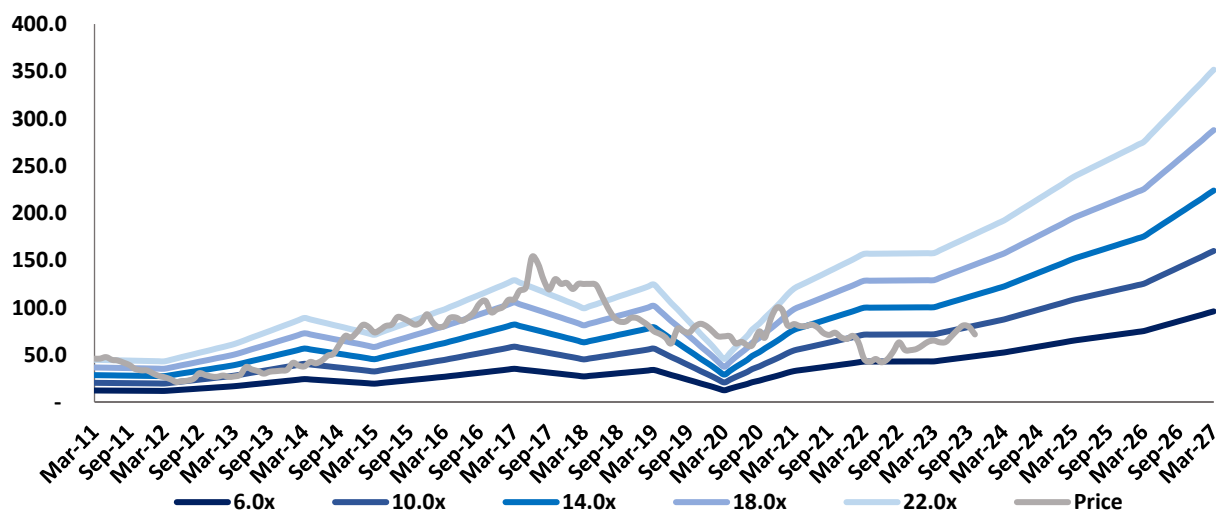
PER Valuation

PER based Valuation	FY24E	FY25E
Earnings (LKR 'Mn)	5,623	6,742
No. of Shares ('Mn)	597	597
EPS	9.4	11.3
Expected Average PER	9.0x	9.0x
Price at 9x Earnings	84.8	101.7

SOTP Valuation

Segment	Valuation Method	Valuation Assumptions			Value in LKR Mn	
		CoE	WACC	Growth	Firm Value FY24E	Firm Value FY25E
Consumer	DCF	22.4%	22.3%	3%	28,663.1	30,632.2
Healthcare	DCF	24.0%	20.9%	3%	26,985.5	31,645.3
Logistics and maritime	DCF	24.0%	22.5%	3%	1,803.2	1,520.9
Other	DCF	18.0%	25.7%	3%	-2,907.0	-3,076.2
Fair Value before Net Debt					54,544.8	60,722.2
Less: Debt					-19,560.2	-17,416.0
Add: Cash					14,727.8	13,960.9
Fair Value					49,712.3	57,267.1
No. of shares					596.6	596.6
Fair Value per share					83.3	96.0

PER Chart



Appendix I: Statement of Income and Expenses

Statement of Financial Performance (LKR Mn)	FY19	FY20	FY21	FY22	FY23E	FY24E	FY25E	FY26E
P/E 31st Mar								
Revenue	64,082	60,043	64,501	78,831	113,940	121,494	131,723	143,295
Cost of sales	-42,605	-40,896	-45,084	-56,981	-82,147	-87,354	-93,918	-101,453
Gross Profit	21,478	19,148	19,417	21,850	31,793	34,140	37,804	41,842
Other Income	794	623	681	1,099	720	607	659	573
Selling, Distribution & Admin expenses	-16,517	-16,119	-13,704	-15,641	-21,150	-20,881	-22,724	-25,507
Share of results of JV	-58	-120	-333	-525	-400	-551	-689	-896
Share of results of associate	-35	-	-	-	-	-	-	-
Operating Profit	5,661	3,532	6,061	6,783	10,963	13,315	15,050	16,012
Finance Income	478	269	249	352	911	981	295	280
Less : Finance Cost	-1,046	-960	-639	-486	-4,110	-4,466	-3,141	-2,807
Profit Before Tax	5,093	2,841	5,670	6,648	7,765	9,830	12,204	13,485
Income Tax Expense	-1,414	-1,357	-1,523	-1,814	-2,696	-3,440	-4,271	-4,720
Profit for the Year (continuing)	3,679	1,484	4,147	4,834	5,069	6,389	7,932	8,765
Profit/(loss) from discontinued operations	-	-121	-805	-	-	-	-	-
Profit for the year	3,679	1,363	3,342	4,834	5,069	6,389	7,932	8,765
Minority Interest	310	127	89	586	800	767	1,190	1,315
Profit attributable to Equity Holders	3,369	1,236	3,253	4,249	4,269	5,623	6,742	7,450
EPS	5.7	2.1	5.5	7.1	7.2	9.4	11.3	12.5

Appendix II: Statement of Financial Position

Statement of Financial Position (LKR Mn)	FY19	FY20	FY21	FY22	FY23E	FY24E	FY25E	FY26E
as at 31st Mar								
Non-Current Assets								
Property, plant and equipment	18,685	20,033	17,540	18,007	19,913	19,820	19,905	20,163
Investment properties	1,648	1,648	1,942	2,100	2,310	2,310	2,310	2,310
Right of use of assets	-	2,028	1,879	1,178	995	995	995	995
Intangible assets	3,469	3,439	3,290	3,295	3,311	3,311	3,311	3,311
Lease Receivable	-	172	140	125	122	120	117	115
Investments in JVs	884	701	557	85	702	702	702	702
Other non-current financial assets	1,448	541	209	210	182	182	182	182
Deferred tax assets	108	164	144	86	87	87	87	87
	26,242	28,727	25,700	25,086	27,623	27,527	27,610	27,866
Current Assets								
Inventories	11,201	13,560	15,451	16,807	28,602	30,329	32,451	35,231
Trade and other Receivables	18,434	16,094	13,655	19,772	25,456	29,554	33,675	37,496
Tax receivables	299	241	157	329	324	324	324	324
Lease Receivable	-	58	65	60	139	139	139	139
Other current financial assets	100	84	110	359	23	23	23	23
Cash and cash equivalents	6,474	5,617	8,458	13,895	16,331	14,728	13,961	15,482
	36,507	35,654	37,895	51,221	70,875	75,096	80,573	88,694
Total Assets	62,749	64,380	63,594	76,308	98,498	102,623	108,183	116,560
Equity and Liabilities								
Stated Capital	7,734	7,734	7,776	7,776	7,776	7,776	7,776	7,776
Other Reserves	185	217	181	160	119	119	119	119
Other components of equity	1,682	1,389	2,161	4,446	6,542	6,542	6,542	6,542
Retained Earnings	18,497	18,574	21,778	23,206	23,968	27,621	32,001	36,842
Equity attributable to equity holders of parent	28,099	27,914	31,895	35,588	38,405	42,058	46,438	51,279
Non-controlling interests	3,771	3,560	1,543	920	716	1,483	2,672	3,987
Total Equity	31,870	31,474	33,438	36,507	39,120	43,540	49,111	55,266
Non-current Liabilities								
Interest-bearing loans and borrowings	1,369	4,738	3,196	3,093	5,449	11,736	10,450	10,313
Other non current financial liabilities	1,956	2,207	278	277	276	276	276	276
Deferred tax liabilities	1,812	1,733	1,363	1,724	2,901	2,901	2,901	2,901
Employee benefit liabilities	969	1,019	1,033	992	1,199	1,199	1,199	1,199
	6,106	9,697	5,869	6,085	9,825	16,112	14,825	14,689
Current Liabilities								
Trade and other payables	18,599	17,937	17,947	27,165	29,626	29,521	31,740	34,286
Income tax payable	439	513	603	804	969	969	969	969
Other financial liabilities	-	-	1,973	2,272	2,949	2,949	2,949	2,949
Interest bearing borrowings	3,553	3,363	3,260	2,678	11,739	7,824	6,966	6,875
Bank overdraft	2,182	1,396	504	796	4,269	1,707	1,622	1,525
	24,774	23,209	24,287	33,716	49,552	42,972	44,247	46,605
Total Liabilities & Shareholders' Funds	62,749	64,380	63,594	76,308	98,498	102,623	108,183	116,560
NAVPS	47.1	46.8	53.5	59.7	64.4	70.5	77.8	86.0



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