

**JOHN KEELLS HOLDINGS PLC [JKH.N0000]****DOWNGRADED TO HOLD****“COUNTING ON ECONOMIC RECOVERY”****Fair Value: FY24E - LKR 160.0 [-16%]**

Total Return with DPS: FY24E --15% [AER -44%]

**FY25E - LKR 220.0 [+16%]**

FY25E - +18% [AER +14%]

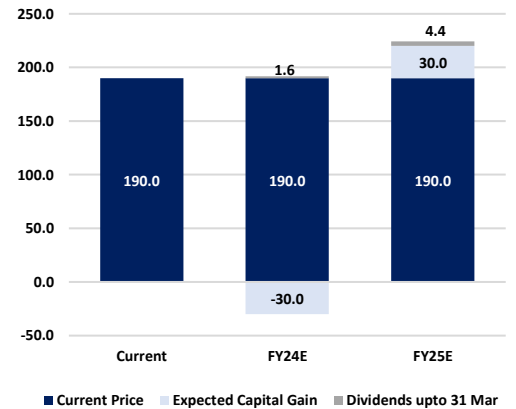
JKH reported a loss of LKR 574.1Mn in 2QFY24 cf. a net profit of LKR 1,605.0Mn in 2QFY23. The LKR 2.1Bn translation loss incurred from the change in reporting currency at the Waterfront Properties together with the abnormal profitability of the Transportation division during 2QFY23, contributed towards the steep dip in profitability during the period. Going forward, we expect a recovery in key sectors such as Transportation, Retail, Consumer Foods, and Financial Services, which is pegged to the recovery in the economy. Furthermore, FCR also expects JKH's Leisure sector to continue its turnaround performance, aided by the improvement in occupancies and ARR, as a result of the increased influx of tourists to the country. Furthermore, the scheduled commencement of the 800 keyed Cinnamon Life Hotel during Aug-24 is also expected to augur well for JKH in the coming years. However, given the recent underperformance of the profitability, we revised down our profit forecast of FY24E to LKR 7.6Bn and FY25E profit to LKR 15.4Bn. Considering the downward revision of earnings we are slightly downgrading our FY25E TP to LKR 220.0, offering a limited upside of 16.0% to the current share price. Given the limited upside on the share, we downgrade our recommendation from **BUY** to **HOLD**.

LKR (Mn)	2QFY23	2QFY24	YoY	1HFY23	1HFY24	YoY
<b>Earnings (LKR 'Mn)</b>						
Revenue	69,065	64,114	-7%	140,581	127,892	-9%
Gross Profit	10,616	11,509	+8%	24,423	22,593	-7%
Operating Profit	2,806	2,415	-14%	5,758	4,043	-30%
PBT	2,497	(154)	-106%	17,298	1,243	-93%
Net Profit	1,605	(574)	-136%	12,882	892	-93%
<b>Balance Sheet (LKR 'Mn)</b>						
Shareholder's Equity	363,549	337,900	-7%	363,549	337,900	-7%
Borrowings	210,733	181,962	-14%	210,733	181,962	-14%
NAVPS	263	244	-7%	263	244	-7%

JKH reports a loss of LKR 574.1Mn in 2QFY24. The loss incurred during the quarter was largely due to an one-off adjustment of LKR 2.1Bn made for the forex loss on Cinnamon Life loan translation whilst higher base of the transportation segment during 2QFY23 also added to the woes. However, excluding the translation loss together with the interest expense on HWIC Convertible Debentures of LKR 991.0Mn, recurrent profit of JKH declined marginally by 1.7%YoY to LKR 2,976.0Mn. On a quarterly basis, JKH's PBT demonstrated a strong recovery of 69.6%QoQ as all sectors (excluding Transportation and property) continued to improve whilst finance cost (excluding the translation loss of LKR 2.1Bn) continued to decline by 13.1%QoQ to LKR 4.7Bn aided from the declining interest rate environment (average weekly AWPLR was at 16.4% in 2QFY24 cf. 20.9% in 1QFY24 and 24.8% in 4QFY23).

**Transportation business struggles as bunkering volumes continues to decline.** JKH's Transportation segment reported a decline in both topline (-57.0%YoY and 22.7%QoQ) and bottom-line (-44.0%YoY and -29.7%QoQ) as substantial performance during 2QFY23 was driven by high margins on account of the significant increase in global crude oil prices (WTI crude oil barrel averaged at USD 80.72 in 2QFY24 cf. USD 92.42 in 2QFY23). However, on the flip side, SAGT continued to witness improved volumes (+9.7%YoY and 8.1%QoQ to 482,255TEUs) outperforming Port of Colombo (+7.7%YoY and -1.6%QoQ) on Volumes. Going forward, we expect the Transportation segment to continue outperform Colombo port and grow at a 4Yr CAGR of 5.7% between FY23-FY27E period as both domestic and transshipment (WTO expects global merchandise trade volumes to grow by 3.3% for 2024) volumes improve. However, global Brent oil prices are expected to stay volatile and hover in the range of USD 78.0 – USD 83.0/barrel, with a slight increase towards 1H2024, amidst recently announced OPEC+ production cuts.

**Declining inflation boost Consumer foods business profitability.** JKH's consumer business continued to showcase resilient performance reporting a 1.5%QoQ growth in revenue to LKR 8.8Bn and 384.0%QoQ growth in net profit to LKR 528.3Mn. The recovery in business is largely attributable to the recovery in volumes across all three business units (Frozen confectionary degrowth slowed down to 2.0% in 2QFY24 cf. -10.0% in 1QFY24, Beverage's volumes increased by 5.0% in 2QFY24 cf. -3.0% in 1QFY24 and Convenience Foods reported a degrowth of 18.0% cf. -35.0% in 1QFY24). Meanwhile, reduction in key raw material input costs (Beverages business raw material and packaging costs declined to 67.0% in 2QFY24 cf. 68.0% in 1QFY24 whilst FC raw material and packaging costs declined steeply to 75.0% in 2QFY24 cf. 78.0% in 1QFY24) also contributed towards the improved EBITDA margins during the quarter (15.0% in 2QFY24 cf. 9.0% in 1QFY24). Going forward, we expect JKH consumer business to continue perform well and record a 4Yr FWD net profit CAGR of 24.5% backed by volume growth and margin expansion. However, impending VAT hike from 15% to 18% together with the recovery in global economies, which can push up raw material prices (skimmed milk prices has already picked up by 4.4% from Sep-23 end to date), also remains a concern for the future sector profitability.

**FIRST CAPITAL RESEARCH**

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[ranjan@firstcapital.lk](mailto:ranjan@firstcapital.lk)**Price movement of JKH vs ASPI (indexed and rebased to 100)****Minimum Return for BUY:****Buy Below FY25E - [AER of 16% with DPS]: LKR 185.0**

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.

**Retail sector shows promising recovery.** Group’s Retail business recorded a profit of LKR 346.4Mn in 2QFY24 cf. a profit of LKR 110.7Mn in 2QFY23 whilst segment EBITDA improved slightly by 1.0%YoY to LKR 2.0Bn. The revitalization of the Retail segment came in the wake of growth in same-store sales (+10.4%), which was predominantly driven by footfall growth (+10.6%) whilst average basket value declined for first time after 4Qs by 0.2% due to the on-going reduction in the consumption of non-essential items that led to a decline weight of purchase (WOP). Going forward, we expect JKH’s Retail segment to continue its exceptional performance, aided by easing inflation (CCPI inflation is expected to hover around 5% in the medium term) and increased footfall. However, the impending tax hike is expected to impact basket value, yet cost effective electricity tariff system together with increased new offerings (food etc.) and discounts offered by Keells (private label offering continue to increase offering attractive discounts) is expected to partly offset the tax hike impact. Meanwhile, Office Automation business is expected to witness steady improvement, as disposable incomes recover, and external operating conditions improve (lifting of import ban etc.).

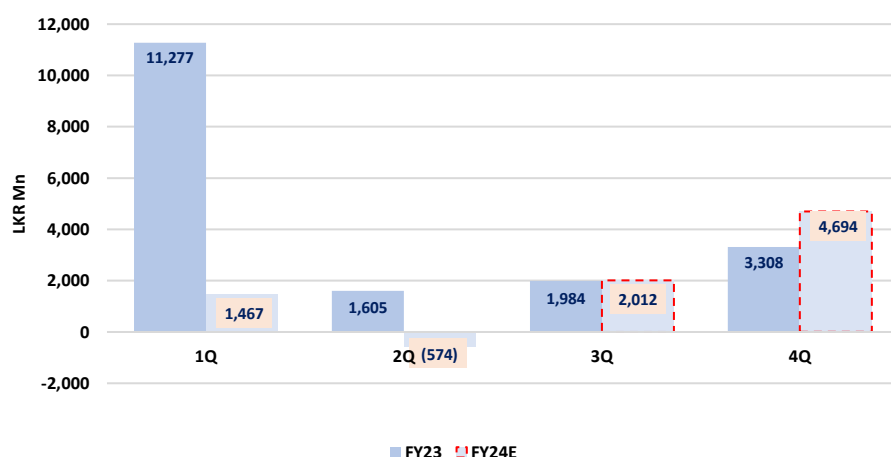
**Leisure sector EBITDA up 6.0%YoY whilst one-off charge drags down profitability.** Leisure sector EBITDA reported a 6.0%YoY (+275.0%QoQ) growth to LKR 1,065.0Mn during 2QFY24 driven by the excellent performance from the Sri Lankan leisure sector. Backed by the higher influx of tourists to Sri Lanka (arrivals +240.8%YoY and +35.3%QoQ to 391,382 arrivals during 2QFY24), both Colombo Hotels and Sri Lankan Resorts segment witnessed higher occupancies (67.0% and 71.0% in 2QFY24 cf. 29.0% and 31.0% in 2QFY23, respectively) whilst improvement in ARRs at both Colombo and Resorts segments (USD 69.0 and USD 62.0 in 2QFY24 cf. 62.0% and 57.0% in 2QFY23, respectively), also added a boost to the profitability (Colombo Hotels EBITDA margin improved by 1,700BpsYoY and 1,600BpsQoQ to 13.0% whilst Sri Lankan Resorts margins improved by 2,900BpsYoY and 2,200BpsQoQ to 4.0% during 2QFY24). Meanwhile, EBITDA margins at the Maldivian Hotels recorded a notable decline of 900BpsYoY and 600BpsQoQ to 17.0% due to the drop in occupancies which stood at 82.0% in 2QFY24 (-400BpsYoY and unchanged QoQ). The drop in occupancies in Maldivian Resorts was largely caused by the change in the mix of overall arrivals (arrivals from traditional European market declined by 6.7%YoY whilst the arrivals from Asia picked up significantly by 70.8%YoY during 2QFY24), rather than arrivals to the Maldives because number of arrivals continued to escalate during 2QFY24 (+14.3%YoY and +6.4%QoQ). Going forward, we expect Sri Lankan segment to continue its exceptional performance aided by higher arrivals and expansion in margins, despite the competitive challenges posed by the introduction of the minimum room rate on Colombo Hotels from 1<sup>st</sup> Oct 2023. Meanwhile, Cinnamon Life Hotel, which is scheduled for commencement in Aug-24, is also well on track (completed +650 rooms from available 800 rooms) and is also expected to augur well to the Sri Lankan sector profits in the coming years. Moreover, JKH is also in the process of signing the MoU with an international gaming operator and is expected to open within 2-3 months from hotel opening. Meanwhile, Maldivian Hotels segment is expected to face challenges in the short term largely arising from the poor occupancies, due to the delayed recovery in key markets such as Europe and China. However, the challenges are expected to ease off momentarily as global economy emerges from recession during the coming years.

**Property sector woes continues to 2QFY24.** JKH Property segment continued to remain impacted from the challenging economic conditions as reported EBITDA slid by 55.9%YoY to a loss of LKR 435.0Mn. Furthermore, increased finance expenses on account of temporarily higher working capital requirement at Tri-Zen (equity accounted investee share reported a loss of LKR 244.4Mn in 2QFY24) also added woes to the depressed EBITDA performance, and resulted in a net loss of LKR 391.2Mn during 2QFY24. However, on a bright note, several apartments were sold on both Cinnamon Life (12 units sold 6 each from Suites and residential apartments) and Tri-Zen (13 units sold and 221 units remains unsold) during 2QFY24 as economic woes eased and activity picked up in the economy (3Q2024 GDP reported a growth of 1.6%YoY). Going forward, we expect apartment sales to be further challenged as Sri Lanka introduces VAT rate of 18% on apartments from 1<sup>st</sup> January 2024. This is expected to hamper the recovery in disposable incomes and apartment sales, given that the JKH apartments are priced relatively higher to the market (Cinnamon Life apartments starts at USD 450,000 for 2Br unit with +1,200sq. ft whilst Tri-Zen prices starts from LKR 47.0Mn per 1Br unit with +407sq. ft).

**Financial Services segment remains resilient amidst declining rates.** Financial Services segment reported a marginal growth in EBITDA of 54.2%YoY and 0.5%QoQ to LKR 1.7Bn driven by both Union Assurance (UAL) and Nations Trust Bank performance. UAL net profit grew by 46.4%YoY to LKR 434.9Mn backed by double digit growth in gross written premiums (+15.4%YoY growth), driven by renewal premiums and higher yield on investments. Meanwhile, NTB continued to perform well during 3Q2023, recording a profit growth of 29.0%YoY, benefitted by the expansion of activity (loan growth +0.1%YoY) amidst a declining interest rate environment (NIMs declined to 6.7% in 2QFY24 cf. 7.6% in 1QFY24 and 8.1% in 4QFY23). Moreover, NTB continued to maintain the lowest stage 3 NPL in the banking sector, recording 3.3% in 3Q2023 cf. 3.4% in 2Q2023. Going forward, we expect NTB to continue to perform well aided by pick up in economic activity, thus the expansion of private sector credit growth and reduction in impairment charges as key sectors such as manufacturing, tourism and construction shows signs of recovery.,

**FY24E and FY25E earnings downgraded, and target price revised down to LKR 220.0.** Considering the 1HFY24 results reported by the company, which is down 93.1%YoY to LKR 892.4Mn, we downgraded our earnings for FY24E to LKR 7.6Bn whilst FY25E earnings is also downgraded to LKR 15.4Bn (growth of 102.2%YoY). The downward revision of earnings also caused a reduction in target price to LKR 220.0 for FY25E, from previous TP of LKR 240.0. Hence, considering the limited upside on the share, **we revise down our recommendation to HOLD from BUY.**

## Quarterly Earnings



## Estimate Revision

In LKR Mn	FY24E-O	FY24E-R	% Change	FY25E-O	FY25E-R	% Change
<b>Earnings Estimate</b>						
Revenue	284,501	280,879	-1%	331,024	364,676	+10%
Gross Profit	46,943	46,345	-1%	56,274	61,995	+10%
EBIT	21,032	13,391	-36%	27,666	22,947	-17%
Profit before Tax	25,645	9,618	-62%	34,843	22,454	-36%
Net Profit	19,113	7,598	-60%	25,694	15,366	-40%
Adjusted EPS	13.8	5.5		18.6	11.1	
Growth YoY	5%	-58%		34%	102%	
<b>Balance Sheet Estimate</b>						
Shareholders' Equity	356,313	346,341	-3%	376,868	355,561	-6%
Borrowings	167,464	168,311	+1%	174,219	174,219	-0%
Adjusted NAVPS	257.3	249.7		272.1	256.4	
<b>Ratio Estimate</b>						
ROE (%)	5%	2%		7%	4%	
PER (x)	13.8	34.7		10.2	17.1	
PBV (x)	0.7	0.8		0.7	0.7	

## Valuation Table

YE Mar/LKR Mn	FY21	FY22	FY23	FY24E	FY25E	FY26E
<b>Estimates (LKR 'Mn)</b>						
Revenue	127,676	218,075	276,640	280,879	364,676	382,019
Gross profit	18,929	37,645	49,450	46,345	61,995	68,763
EBIT	2,552	7,308	12,691	13,391	22,947	25,831
<b>Net Profit</b>	<b>4,772</b>	<b>20,213</b>	<b>18,174</b>	<b>7,598</b>	<b>15,366</b>	<b>17,032</b>
Adjusted EPS (LKR)	3.4	14.6	13.1	5.5	11.1	12.3
YoY Growth (%)	-49.3%	323.6%	-10.1%	-58.2%	102.2%	10.8%
<b>Valuations</b>						
PER (x)	55.2x	13.0x	14.5x	34.7x	17.1x	15.5x
PBV (x)	1.2x	0.8x	0.8x	0.8x	0.7x	0.7x
Dividend Yield (%)	0.8%	0.8%	1.1%	0.9%	2.3%	2.6%
NAVPS	163.1	224.5	245.9	249.7	256.4	263.7
DPS (LKR)	1.5	1.5	2.0	1.6	4.4	4.9
Dividend Payout	43.6%	10.3%	15.3%	20.0%	20.0%	20.0%

## SOTP

Segment	Valuation method	Valuation assumptions			Value in LKR Mn			Value per share FY24E	Value per share FY25E
		CoE	WACC	Growth	Firm value FY24E	Firm value FY25E	% of ownership		
Transportation	DCF	19.2%	12.4%	5.0%	19,805.4	20,400.5	80%	15,844.3	16,320.4
Consumer Foods	DCF	19.2%	12.4%	5.0%	42,694.6	53,494.3	85%	36,290.4	45,470.2
Retail	DCF	19.2%	12.4%	5.0%	111,684.6	128,978.2	85%	94,931.9	109,631.5
Leisure	DCF	20.0%	13.2%	5.0%	60,138.8	73,876.4	80%	48,111.0	59,101.1
Property	DCF	21.6%	15.2%	5.0%	36,744.8	42,854.0	95%	34,907.5	40,711.3
Financial Services	DCF	20.0%	14.2%	5.0%	23,795.2	24,343.1	60%	14,277.1	14,605.9
Other	DCF	20.0%	12.8%	5.0%	(4,280.7)	(4,467.9)	60%	(2,568.4)	(2,680.8)
Total per share								241,794.0	283,159.6
Number of shares								1,384.9	1,384.9
Value/share								174.6	204.5

## Valuation Summary

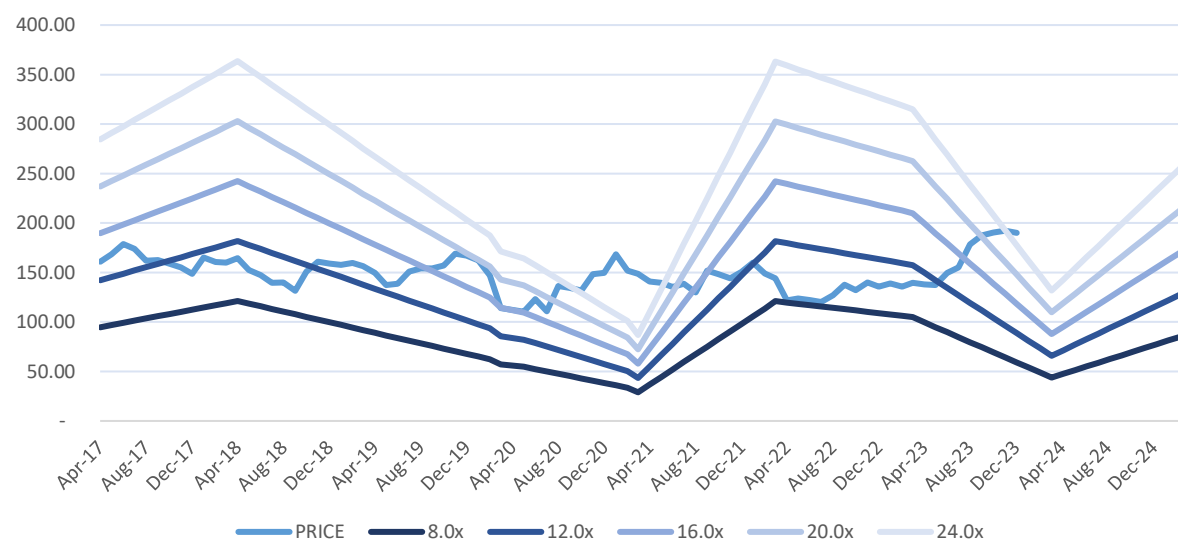
Expected JKH Price	FY24E	FY25E
PER Valuation based target price	153.4	221.6
SOTP Valuation based target price	174.6	204.5
Average Target Price	164.0	213.0
Target Price after Rounding off	160.0	220.0

Return	FY24E	FY25E
Target Price	160.0	220.0
Current Price	190.0	190.0
Capital Gain (LKR)	-30.0	30.0
Dividends upto 31 Mar (LKR)	1.6	4.4
Capital Gain %	-16%	16%
Dividend Yield %	1%	2%
Total Return %	-15%	18%
Annualized Return %	-44%	14%

## PER valuation

PER based Valuation	FY24E	FY25E
Earnings (LKR 'Mn)	7,598	15,366
No. of Shares ('Mn)	1,387	1,387
EPS	5.5	11.1
Expected PER	28x	20x
Target Price	153.4	221.6

## PER Chart



## Appendix I: Statement of Income and Expenses

Income Statement	FY21	FY22	FY23	FY24E	FY25E	FY26E
<b>Year ended 31st March (LKR 'Mn)</b>						
Total revenue	127,676	218,075	276,640	280,879	364,676	382,019
Cost of sales	(108,747)	(180,430)	(227,190)	(234,534)	(302,681)	(313,256)
Gross profit	18,929	37,645	49,450	46,345	61,995	68,763
Selling and distribution expenses	(4,761)	(5,733)	(8,266)	(8,393)	(10,897)	(11,415)
Administrative expenses	(12,928)	(14,763)	(21,928)	(25,279)	(36,468)	(38,202)
Other operating expenses	(1,314)	(12,456)	(9,826)	(8,426)	(10,940)	(11,461)
<b>Results from operating activities</b>	<b>2,552</b>	<b>7,308</b>	<b>12,691</b>	<b>13,391</b>	<b>22,947</b>	<b>25,831</b>
Finance cost	(4,669)	(7,035)	(17,803)	(19,597)	(8,638)	(8,069)
Finance income	10,689	30,806	26,900	19,727	6,894	5,372
Change in insurance contract liabilities	(7,032)	(6,416)	(7,650)	(14,044)	(10,940)	(11,461)
Share of results of equity accounted investees (net of tax)	4,159	6,746	7,574	10,141	12,191	12,999
<b>Profit before tax</b>	<b>5,445</b>	<b>27,324</b>	<b>22,589</b>	<b>9,618</b>	<b>22,454</b>	<b>24,673</b>
Tax expense	(1,494)	(6,882)	(3,693)	(1,933)	(6,913)	(7,447)
Profit for the year	3,951	20,443	18,896	7,685	15,541	17,225
Attributable to:						
Equity holders of the parent	4,772	20,213	18,174	7,598	15,366	17,032
Non-controlling interests	(821)	230	722	86	175	194
	3,951	20,443	18,896	7,685	15,541	17,225
EPS	3.62	15.13	13.12	5.49	11.10	12.30

## Appendix II: Statement of Financial Position

Balance Sheet	FY21	FY22	FY23	FY24E	FY25E	FY26E
<b>Year ended 31st March (LKR 'Mn)</b>						
<b>ASSETS</b>						
<b>Non-current assets</b>						
Property, plant and equipment	113,077	124,348	362,097	367,036	375,279	383,433
Right-of-use assets	40,617	53,482	54,185	53,574	53,788	54,151
Investment property	14,868	30,608	33,029	33,229	33,429	33,629
Intangible assets	4,853	5,399	5,793	6,368	7,216	8,020
Investments in equity accounted investees	28,630	33,866	38,486	38,486	38,486	38,486
Non-current financial assets	62,590	48,690	63,957	63,957	63,957	63,957
Deferred tax assets	1,089	1,554	2,582	2,582	2,582	2,582
Other non-current assets	104,580	180,920	1,571	1,571	1,571	1,571
	370,303	478,867	561,701	566,805	576,309	585,831
<b>Current assets</b>						
Inventories	54,296	36,225	39,095	47,087	60,769	62,892
Trade and other receivables	17,457	27,495	21,508	35,414	45,979	48,166
Amounts due from related parties	124	196	318	318	318	318
Other current assets	5,919	11,914	14,570	15,346	19,924	20,872
Short term investments	69,263	110,722	82,222	86,276	79,649	74,948
Cash in hand and at bank	19,433	52,377	25,093	3,143	8,144	15,157
	166,491	238,929	182,806	187,584	214,784	222,353
<b>Total assets</b>	<b>536,794</b>	<b>717,796</b>	<b>744,506</b>	<b>754,389</b>	<b>791,092</b>	<b>808,184</b>
<b>EQUITY AND LIABILITIES</b>						
<b>Equity attributable to equity holders of the parent</b>						
Stated capital	63,102	73,188	73,188	73,188	73,188	73,188
Revenue reserves	90,652	109,087	121,743	127,062	136,282	146,501
Other components of equity	72,403	129,011	146,091	146,091	146,091	146,091
	226,157	311,286	341,022	346,341	355,561	365,780
Non-controlling interest	16,830	18,805	19,396	19,483	19,657	19,851
Total equity	242,987	330,091	360,418	365,824	375,218	385,631
<b>Non-current liabilities</b>						
Insurance contract liabilities	45,161	51,349	58,907	58,907	58,907	58,907
Interest-bearing loans and borrowings	118,966	158,922	159,779	143,530	147,616	147,616
Lease liabilities	24,235	30,067	32,052	33,943	37,089	40,246
Deferred tax liabilities	7,720	12,016	19,688	19,688	19,688	19,688
Employee benefit liabilities	2,814	3,107	2,560	2,560	2,560	2,560
Non-current financial liabilities	3,661	2,414	20,107	20,107	20,107	20,107
Other non-current liabilities	19,546	220	286	286	286	286
	222,102	258,095	293,379	279,021	286,252	289,409
<b>Current liabilities</b>						
Trade and other payables	35,288	43,469	29,866	56,504	72,922	75,470
Amounts due to related parties	1	2	4	4	4	4
Income tax liabilities	1,988	2,619	1,799	1,799	1,799	1,799
Short term borrowings	6,904	14,833	8,702	12,003	12,334	12,334
Interest-bearing loans and borrowings	9,507	40,624	12,839	12,778	14,269	14,769
Lease liabilities	1,472	3,459	2,259	2,392	2,614	2,836
Other current liabilities	1,733	4,280	5,192	5,564	7,181	7,431
Bank overdrafts	11,820	20,322	30,049	18,500	18,500	18,501
	71,705	129,609	90,709	109,544	129,622	133,144
<b>Total equity and liabilities</b>	<b>536,794</b>	<b>717,796</b>	<b>744,506</b>	<b>754,389</b>	<b>791,092</b>	<b>808,184</b>
<b>Net Asset Value</b>	<b>163.30</b>	<b>224.77</b>	<b>246.24</b>	<b>250.08</b>	<b>256.74</b>	<b>264.12</b>



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Thushara Pathiraja	+94 70 2910 037			
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