



Derrimon Trading Company Limited (DTL)

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Executive Summary

DTL was founded in 1998 as a distributor of bulk commodities in the Kingston area and in 2009 branched out into the retail space by acquiring Sampars Cash 'N' Carry, a large wholesale business in Kingston. The Company now operates seven retail stores under the Sampars Cash 'N' Carry brand and its flagship supermarket under the Select Brand via a joint venture agreement.

During the 2017 financial year, DTL purchased the former Empire Supermarket, at 1-3 Retirement Road, and finalized a Joint Venture Agreement to purchase the assets of Caribbean Home Entertainment Systems Limited, the former operators of Carihome Supermarket Limited, rebranding the operations under the Select Grocers brand. DTL's strategy of removing low margin products that do not meet a required threshold or provide a negative contribution, to focus on higher yield products has borne fruit and we expect such margin management to continue in the current year.

We recommend Derrimon Trading Company Limited as a BUY as we believe the stock is trading below its fair value. Our conservative estimate of the fair value ranges between \$16.07 and \$11.01 with an average of \$12.86.

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Company Background

DTL was founded in 1998 as a distributor of bulk commodities in the Kingston area. In 2002, DTL was appointed a regional co-distributor by Nestle Jamaica for the Kingston, St. Andrew, St. Catherine and St. Thomas areas. In 2009, the Company acquired Sampars Cash 'N' Carry, a large wholesale business in Kingston. The Company now operates seven retail stores under the Sampars Cash 'N' Carry brand and its flagship supermarket under the Select Brand via a joint venture agreement.

The Company listed its ordinary shares in December 2013 on the Junior Market of the Jamaica Stock Exchange. As a part of its growth strategy, DTL acquired a 49.02% stake in Caribbean Flavours and Fragrances Limited (CFF), another Junior Market-listed company. In 2017, DTL acquired a majority stake in CFF and now owns 65.02% of the company.

Financial Performance – Year ended December 31, 2017

Profitability

DTL reported revenues of \$6.72B for the year ended Dec. 31, 2017, an 8.9% or \$546.88M increase year-over-year. This increase follows the consolidation of Caribbean Flavours & Fragrances into the DTL group after DTL increased its stake to a majority holding in the first half of the year. The nine months results showed core revenues were also up, year-over-year, contributing to the growth in consolidated revenues. Gross profits climbed 42.9% to \$1.36B as cost of sales increased by just 2.8% from the previous year's amount to \$5.39B. The gross profit margin improved to 19.9% from 15.1% for the previous financial year. **DTL noted in its nine month results that the improvement in gross margin was driven by strategies employed to realign the product portfolio to focus more on higher yielding products.** Other income also moved from \$19.47M to \$257.13M as a gain on acquisition of subsidiary of \$206.35M was reported during the 2017FY.

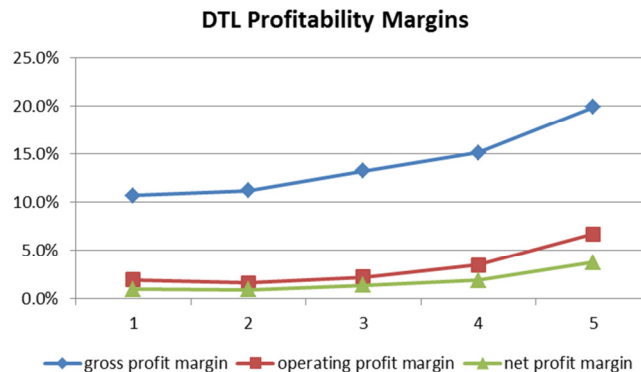
Operating expenses surged 54.3% to \$1.14B as administrative expenses jumped 79.1% to \$1.01B while selling and distribution costs declined by 23.8% to \$135.67M. DTL noted in the 2017 quarterly reports that the increase in operating costs was tied to expenses related to two new stores acquired during the year. Earnings before interest, taxation, depreciation & amortisation amounted to \$503.55M, more than double the \$238.28M reported for the previous year while the operating profit amounted to \$451.70M, also doubling the previous year's result. The EBITDA margin improved to 7.5% from 3.9% in the 2016FY while the operating profit margin moved from 3.5% in the 2016FY to 6.7% in the 2017FY.

Finance costs rose 24.4% to \$169.90M **but the strong improvement in operating performance strengthened the Company's ability to service its debt as the interest coverage ratio rose to 2.66x, from 1.57x in the previous year.** Profit before taxation amounted to \$281.80M, a 142.7% increase year-over-year. No taxes were recorded due to the 100% tax holiday afforded to Junior Market-listed stocks in their first five years of listing.

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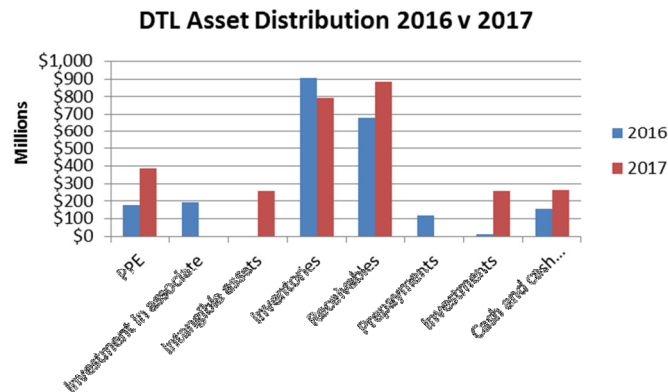
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Net profit attributable to shareholders amounted to \$252.37M, up 117.4% from the \$116.11M reported in the 2016FY. The net profit margin doubled to 3.8% on this performance. DTL's return on equity amounted to 35.3% while the return on assets stood at 9.8%, which compares to 22.9% and 6.1% in the prior year, respectively. DTL's margins have been on an upward trend, with a notable uptick in the last financial year, highlighting the success of the effort to focus on a higher-yield product mix.



Solvency & Liquidity

As at Dec. 31, 2017, DTL's assets amounted to \$2.89B, a 27.5% or \$623.21M increase year-over-year. Non-current assets rose by 75.3% to \$676.75M as property, plant & equipment more than doubled (up 119.7%) to \$387.01M. The company also reported intangible assets of \$256.52M, when none was reported at the start of the year. Current assets rose 17.7% to \$2.21B, driven by a 30.3% increase in receivables to \$887.21M and a \$244.8M increase in investments to \$256.98M. Cash & cash equivalents rose 68.1% to \$265.52M. Inventories amounted to \$795.55M, down 12.2% from the previous year while prepayments of \$120.62M were completely written off.



Current liabilities were up just 1.3% to \$1.1B as a \$227.87M increase in the current portion of borrowings to \$258.77M was partially offset by a \$194.30M decrease in short term loans to \$29.98M. Payables amounted to \$791.04M, up 2.5%. Non-current liabilities consisted of borrowings of \$754.32M, up 22.5%

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year-over-year. DTL's total debt amounted to \$1.06B as at Dec. 31, 2017, up 14.4% or \$133.50M a year prior. With shareholders' equity rising 53.1% to \$864.07M, DTL's leverage improved, falling from 1.64x as at Dec. 31, 2016 to 1.23x as at Dec. 31, 2017.

DTL's liquidity improved over the year as the cash ratio moved from 0.15x to 0.24x while the quick ratio moved from 0.78x to 1.28x. DTL's current ratio was also up to 2.01x, from 1.73x in the 2016FY. Net cash inflow from operating activities amounted to \$354.11M, which compares to a net cash outflow of \$288.28M in the previous year.

Outlook & Valuation

The last financial year was one of growth, both organic and inorganic. DTL purchased the assets of Chris Ryan Limited and rebranded the former Empire Supermarket, at 1-3 Retirement Road, to "Sampars Cross Roads Supermarket" in the first quarter of the year. DTL also finalized a Joint Venture Agreement and concluded the purchase of the assets of Caribbean Home Entertainment Systems Limited, the former operators of Carihome Supermarket Limited, rebranding the operations under the Select Grocers brand. The Company was also appointed as a distributor by Jamaica Cane Products for its Jamaica Gold packaged sugar.

DTL's strategy of removing low margin products that do not meet a required threshold or provide a negative contribution, to focus on higher yield products has borne fruit and we expect such margin management to continue in the current year. Operating expenses rose as the general cost of utilities, marketing expenses, scheduled repairs & maintenance of equipment, and staff increased with the addition of the two new stores. Whilst these moves may have increased the nominal amount of expenses, profitability margins were improved year-over-year.

As such, we are forecasting operating revenue of \$7.14B for the 2018 financial year, up 6.2% year-over-year while net profit attributable to shareholders is forecasted to decline marginally by 3.6% to \$270.3 million, which corresponds to a earning per share of \$0.89. Utilizing DTL's 1-year P/E average of 18.05x produces a price of \$16.07. Shareholders' equity is expected to close the year at \$1.06B, a 22.3% increase year-over-year, which corresponds to a book value per share of \$3.87. Utilizing the 1-year P/B average of 2.70 yields a price of \$10.45.

The peer group P/E ratio average is 15.64x which yields a price of \$13.93 while the peer group P/B ratio average is 2.85x which yields a price of \$11.01. These estimates produce an average of \$12.86, which is 43.0% higher than DTL's last traded price of \$9.00 on April 10, 2018.

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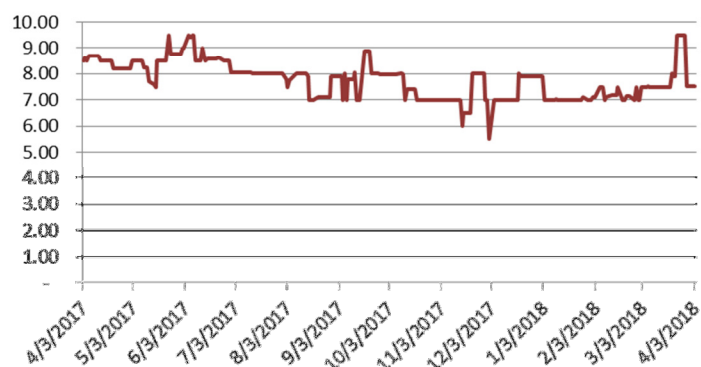
Peer Comparison – Junior Market Retail Sector

Company	Market Capitalization	Price to Earnings	Price to Book	Return on Equity	Return on Assets	Dividend Yield 2017
CAC	1,140,645,161	15.34x	2.71x	19.4%	7.7%	
CPJ	5,500,000,000	14.07x	1.92x	14.3%	4.6%	
FOSRICH	1,300,893,687	23.68x	2.14x	10.9%	4.5%	
JETCON	2,444,865,000	15.90x	5.63x	42.2%	35.3%	
LASD	13,704,250,469	18.84x	3.05x	17.5%	9.6%	
MDS	1,315,789,475	13.53x	2.10x	16.8%	7.6%	
Sector Average	3,922,742,522	15.64x	2.85x	22.3%	11.3%	
DTL	2,052,753,863	8.13x	2.38x	35.3%	9.8%	

Recommendation

We recommend Derrimon Trading Company Limited as BUY as we believe the stock is trading below its fair value. The shift to a higher yield product mix when combined with the earnings of Caribbean Flavours & Fragrances Limited has produced strong bottom line results for DTL. We assumed revenue growth which is consistent with its past performance and a maintenance of margins produced in the past year, which we believe is conservative as the trend is for upward growth of profitability margins. The stock last traded at \$9.00 which indicates the market is on to the turn in fortunes for the company. The Company is not historically a dividend payer, which is to be expected given its push into the retail/supermarket business and is suitable for investors with a medium-term horizon seeking capital appreciation.

DTL 1-Yr Trading History



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Abridged Financials

J\$000	Year Ended December 31					Change %
	2013	2014	2015	2016	2017	
Turnover	5,255,523	5,609,597	6,293,998	6,176,928	6,723,810	8.9%
Operating Expenses	499,520	585,644	702,286	739,412	1,141,231	54.3%
Operating Profit	100,812	89,086	139,265	214,540	451,697	110.5%
Profit Before Taxation	71,493	51,607	88,130	116,107	281,796	142.7%
Profit for the year	49,927	51,607	88,130	116,107	252,369	117.4%
Total Assets	1,024,480	1,450,767	1,526,660	2,264,007	2,887,219	27.5%
Total Liabilities	716,469	1,091,189	1,078,298	1,699,539	1,852,044	9.0%
Shareholder's Equity	308,011	359,578	448,362	564,468	864,068	53.1%
EPS (\$)	0.18	0.19	0.32	0.42	0.92	
Book Value per Share (\$)	1.13	1.32	1.64	2.07	3.16	
Key Ratios						
Operating profit margin	1.9%	1.6%	2.2%	3.5%	6.7%	
Net Margin	0.9%	0.9%	1.4%	1.9%	3.8%	
Return on Average Equity	24.2%	15.5%	21.8%	22.9%	35.3%	
Return on Average Assets	5.3%	4.2%	5.9%	6.1%	9.8%	
Quick Ratio (x)	0.67	0.54	1.00	0.78	1.28	
Current Ratio (x)	1.32	1.13	2.03	1.73	2.01	
Debt/Equity (x)	0.36	1.37	1.15	1.64	1.23	

Source: <http://www.Jamstockex.com>, **JMMB Investment & Research, Bloomberg, Company Financials**

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APPENDIX

IMPORTANT DISCLOSURES

ABSTRACT—As a part of our new Portfolio Strategy we are recommending strict adherence to the following Portfolio Allocation **DEFINITIONS/RECOMMENDATIONS**.

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UNDERWEIGHT—REDUCE EXPOSURE IN YOUR PORTFOLIO TO LESS THAN 5% FOR THIS PARTICULAR ASSET

SELL—REDUCE EXPOSURE IN YOUR PORTFOLIO TO ZERO.

HOLD/MARKETWEIGHT—EXPOSURE TO THE ASSET SHOULD BE EQUAL TO 5% OF YOUR TOTAL PORTFOLIO HELD AT JMMB.

OVERWEIGHT/BUY—EXPOSURE TO THIS ASSET SHOULD BE BETWEEN 5% AND 10% OF YOUR TOTAL PORTFOLIO HELD AT JMMB

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