

Supreme Ventures Limited (SVL)

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Executive Summary

Supreme Ventures is a leading lottery and gaming provider in the Caribbean, with a diverse portfolio of lottery products. The Company focuses on utilizing the technology of its platforms and extensive retailer network to provide non-lottery commercial services to the market. SVL's business segments include Lottery – which includes the Top Draw, Money Time, Pick 3, Cash Pot, Lotto and Super Lotto Games; Sports Betting – which includes the JustBet brand that offers wagers on international sporting events; Gaming and hospitality – which offers Video Lottery Terminal (VLT) games at gaming lounges and food and beverage operations; Pin Codes – which sells phone pin codes through the agent's network; Horseracing – which consists of the operations of Caymanas Track Limited; and Other – which covers all other income.

SVL reported revenues of \$41.24B for the period, a 24.8% or \$8.18B increase over revenues for the comparable period of 2016. This increase was driven by a \$3.88B increase in lottery revenues to \$29.75B and \$3.27B generated from the horseracing segment. Growth of \$1.12B to \$7.40B in pin code sales also contributed to the increase in the revenues. Gaming revenues rose 6.2% to \$281.04M while sports betting revenues were down 8.7% to \$516.37M.

Interest income rose 45% to \$71.43M while finance costs moved from \$354K to \$45.49M year-over-year. This increase was due to interest charges on a finance lease taken out to fund the acquisition and development of the Caymanas Park Operations. **Despite this increase, pre-tax profits rose 48.6% to \$1.77B. Taxation rose 29.7% to \$445.58M which resulted in net profits of \$1.33B, a 56.2% increase from the comparable period of 2016.** The effective tax rate fell from 28.8% to 25.1% year-over-year which contributed to the increase in net profit margin, which stood at 3.2%, up from 2.6%.

Applying the 1-year average P/E ratio of 15.1x to the forward EPS of \$0.67 yields a price of \$10.18 while the forward BVPS of \$1.57 and the 1-year average P/B ratio of 5.79x yields a price of \$9.07. The Gordon Growth Model produced a price of \$7.76, in which we assumed a 5% growth rate and a 9.84% cost of equity using the Capital Asset Pricing Model. As such, our estimation of the fair value range of SVL's shares is from \$7.76 to \$10.18. The latest price for SVL (as at Feb-20) is \$11.99 which is above our fair value estimated price range. Some of the movement in the share price has come due to market sentiments of increased dividend flows.

Recommendation

We recommend SVL as HOLD for investors with a medium risk appetite and a medium to long-term investment horizon. With the recent improvement in profitability and the addition of the Caymanas Track operation we are suggesting holding as the company works to improve the horseracing segment's performance. **Over the past five years, SVL has averaged a dividend pay-out ratio of 82% making it**

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a suitable stock for investors seeking income. As at the end of December-2017, SVL had paid out \$0.71 per share in dividends for a dividend yield of 13.5%.

Company Background

Supreme Ventures is a leading lottery and gaming provider in the Caribbean, with a diverse portfolio of lottery products. The Company focuses on utilizing the technology of its platforms and extensive retailer network to provide non-lottery commercial services to the market. SVL's business segments include Lottery – which includes the Top Draw, Money Time, Pick 3, Cash Pot, Lotto and Super Lotto Games; Sports Betting – which includes the JustBet brand that offers wagers on international sporting events; Gaming and hospitality – which offers Video Lottery Terminal (VLT) games at gaming lounges and food and beverage operations; Pin Codes – which sells phone pin codes through the agent's network; Horseracing – which consists of the operations of Caymanas Track Limited; and Other – which covers all other income.

Financial Performance – Nine Months ended September 2017

Profitability

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Direct expenses rose 24% or \$7.18B to \$37.07B for the period, however, gross profit rose 31.8% or \$1.0B to \$4.17B as the gross profit margin improved from 9.6% in the comparable period of 2016 to 10.1% in the nine months ended Sept. 2017. Operating expenses rose 19.3% to \$2.42B but operating profits grew by 54.1% to \$1.75B as the operating profit margin improved from 3.4% a year prior to 4.2%. The increase in expenses was mainly attributed to the Caymanas Track operations as excluding this segment operating expenses were down \$168.5M relative to 2016.

Interest income rose 45% to \$71.43M while finance costs moved from \$354K to \$45.49M year-over-year. This increase was due to interest charges on a finance lease taken out to fund the acquisition and development of the Caymanas Park Operations. **Despite this increase, pre-tax profits rose 48.6% to \$1.77B. Taxation rose 29.7% to \$445.58M which resulted in net profits of \$1.33B, a 56.2% increase from the comparable period of 2016.** The effective tax rate fell from 28.8% to 25.1% year-over-year which contributed to the increase in net profit margin, which stood at 3.2%, up from 2.6%.

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Solvency & Liquidity

Total assets for SVL amounted to \$7.01B, up 36.2% or \$1.87M from a year prior. This increase was driven by a 85.0% increase in cash and cash equivalents which amounted to \$2.43B and a 90.9% increase in property, plant and equipment to \$1.36B. The increase in assets was attributed to improved financial performance and the acquisition of the Caymanas Track assets. Trade and other receivables amounted to \$920.88M, a 12.7% increase from a year earlier while long-term receivables were down 7.9% to \$455.41M. Investment properties rose 8.2% to \$782.51M year-over-year.

Total liabilities rose 88.5% to \$2.92B as non-current liabilities amounted to \$613.84M, versus zero a year earlier, with the booking of \$273.62M in long-term liabilities and \$321.68M in finance lease payable. Current liabilities rose 48.8% to \$2.30B as trade and other payables rose 25.6% to \$1.66B while income tax payable moved from \$20.85M to \$249.13M. Loans payable of \$107.62M at the close of the period, versus a zero balance a year prior.

Despite the increase in liabilities, the cash ratio improved to 1.06x, from 0.85x due to the rise and cash & cash equivalents. The current ratio declined marginally to 1.54x, from 1.56x. The debt to equity ratio stood at 0.17x as total debt amounted to \$702.62M while shareholders' equity rose 13.8% to \$4.10B. SVL's ability to service this new debt is strong with an interest coverage ratio of 38.39x for the nine months period.

Outlook & Valuation

SVL's 2017 strategy involved: the continued enhancement of the portfolio of lottery games with introduction of attractive features and value-added promotions; sustained engagement of VLT gamers, exploiting new channels for delivery of value to Sports Betting customers; leveraging technology platforms to improve product offerings; and capitalizing on the expanded product range to create unique value propositions and improve business efficiencies.

The year-to-date results are a testament to the success of these strategies thus far. The \$1.3B in net profits reported for the first nine months of 2017 are SVL's best ever, despite taking on the loss making Caymanas Track operations, which would have negatively impacted the Group's bottom line. SVL noted that the horse racing segment booked \$508.6M in sales in August 2017, Caymanas' best monthly performance in its history, a positive indicator of the work being done to make the segment a viable operation.

Based on these factors, we have increased our estimate for the 2017 financial year from \$44.9B to \$56.15B, a 25.0% increase year-over-year. Net profits are seen improving 50.9% to \$1.78B (earnings per share: \$0.67), versus our initial estimate of \$1.19B. Shareholders' equity is forecasted to increase 8.8% year-over-year to \$4.13B which corresponds to a BVPS (book value per share) of \$1.57.

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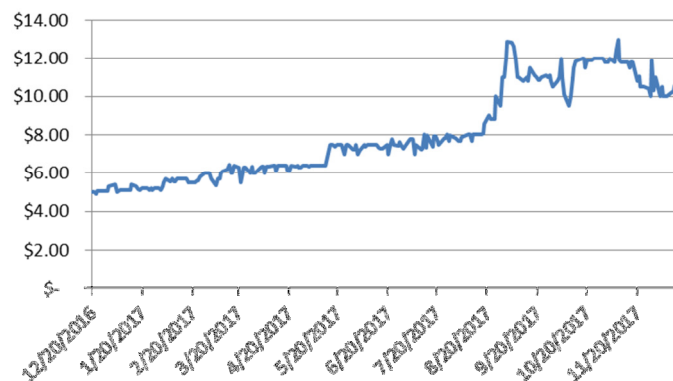
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Trade Performance

SVL closed trading on December 19, 2017 with a price of \$10.70, a 101.9% appreciation since the start of the year, and a 114.0% appreciation from a year ago. This performance compares with a 44.51% growth year-to-date in the JSE Main Market Index, and a 49.38% year-over-year growth.

SVL 1-year Trading Performance



Leadership Changes

In October, 2017, SVL saw a shakeup in its Board composition as Messrs. Nikolaos Nikolakopoulos, Georgios Sampson and James Morrison resigned as Directors of the company which led to the appointment of Messrs. Ansel Howell, Christopher Berry and Gary Peart. An extraordinary general meeting was requisitioned by Mayberry West Indies Limited and two other related parties shortly after.

Paul Hoo stepped down as SVL Chairman in November 2017 and the requisition for the EGM was withdrawn. After a meeting on November 7, 2017, Mr. Peter Chin resigned as a Director and Messrs. Peter & W. David McConnell were appointed to the board.

Recommendation

We recommend SVL as HOLD for investors with a medium risk appetite and a medium to long-term investment horizon. With the recent improvement in profitability and the addition of the Caymanas Track operation we are suggesting holding as the company works to improve the horseracing segment's

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Abridged Financials

J\$000	Year Ended December 31					Nine months ended Sept. 30		Change %
	2012	2013	2014	2015	2016	2016	2017	
Revenues	29,726,146	34,140,265	41,309,545	43,847,020	44,921,339	33,055,306	41,237,861	24.8%
Direct Costs	25,710,180	30,808,867	37,586,698	39,429,684	40,812,837	29,894,140	37,072,539	24.0%
Gross Profit	4,015,966	3,331,398	3,722,847	4,417,336	4,108,502	3,161,166	4,165,322	31.8%
Operating Expenses	2,657,317	2,768,146	2,648,936	2,982,306	2,709,768	2,028,393	2,419,202	19.3%
Operating Profit	1,358,649	563,252	1,073,911	1,435,030	1,398,734	1,132,773	1,746,120	54.1%
Profit Before Taxation	1,449,901	711,092	1,215,741	1,614,830	1,661,892	1,193,137	1,772,623	48.6%
Profit for the year	1,069,224	482,569	929,917	1,183,750	1,178,468	849,704	1,327,046	56.2%
Total Assets	5,656,846	5,323,844	5,900,514	5,398,913	5,433,350	5,147,757	7,012,949	36.2%
Total Liabilities	1,863,554	1,680,925	1,855,129	1,804,876	1,633,149	1,547,938	2,917,712	88.5%
Shareholder's Equity	3,793,292	3,642,919	4,045,385	3,594,037	3,800,201	3,599,819	4,095,237	13.8%
EPS (\$)	0.41	0.18	0.35	0.45	0.45	0.32	0.50	
Book Value per Share (\$)	1.44	1.38	1.53	1.36	1.44	1.36	1.55	
Key Ratios								
Gross profit margin	13.5%	9.8%	9.0%	10.1%	9.1%	9.6%	10.1%	
Operating profit margin	4.6%	1.6%	2.6%	3.3%	3.1%	3.4%	4.2%	
Net Margin	3.6%	1.4%	2.3%	2.7%	2.6%	2.6%	3.2%	
Return on Average Equity	30.0%	13.0%	24.2%	31.0%	31.9%			
Return on Average Assets	20.1%	8.8%	16.6%	21.0%	21.8%			
Debt/Equity (x)	0.09	0.06	0.02	-	-	-	0.17	

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

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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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