INVESTMENT AND SOVEREIGN RESEARCH Thursday April-18-2019

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Jetcon Corporation Limited

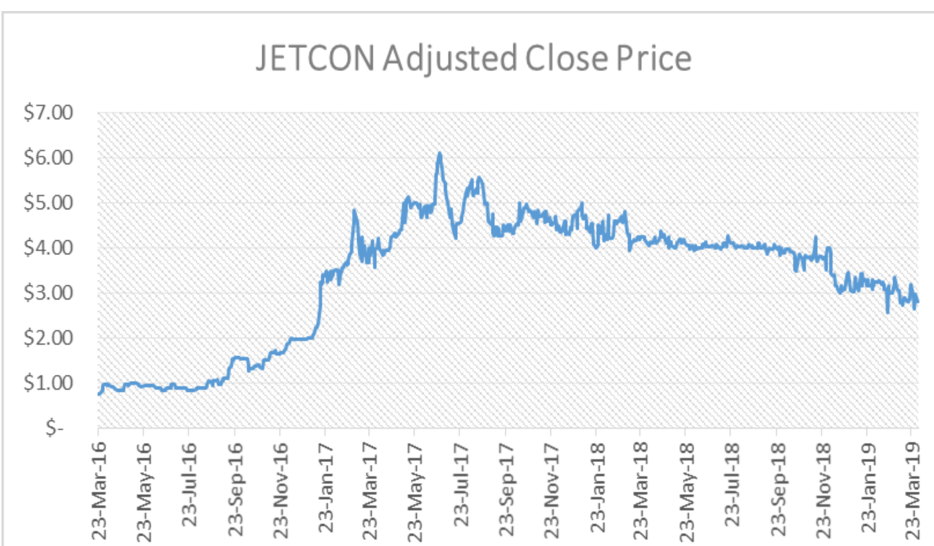
PLEASE SEE IMPORTANT DISCLOSURES & COPYRIGHT INFRINGEMENT IN THE APPENDIX

Executive Summary

Jetcon Corporation Limited (JETCON) is domiciled in Jamaica and has its registered offices at 2 Sandringham Avenue Kingston 10 Jamaica. Effective March 24, 2016 JETCON was listed on the Junior Market of the Jamaica Stock Exchange and on June 22, 2017 JETCON completed a 3 for 1 stock split. The main activities of JETCON is the importation and sale of motor vehicles, motor vehicle parts and the servicing of vehicles.

Profits have increased at a CAGR of 72.13% to $91.88 million for the period under review (FY 2014 to FY 2018), but in FY 2018 profits fell 40.25% or $61.91 million. The main reasons for the decline in profits are a deterioration in revenue and margins. Revenue decreased by 1.28% or $15.11 million in FY 2018 while gross profit margin fell to 13.97% significantly below its five year average of 16.54%. The weakness in earnings and revenue growth was prevalent in the second half of FY 2018, for that period revenue declined 10.83% or $67.52 million to $556.03 million, meanwhile for the same period profits fell 87.76% or by $64.79 million to $9.03 million.

JETCON's peak closing price was on June 26, 2018 at $6.10, soon after its stock split its closing price low was $0.75 on its first day of trading March 24 2016. JETCON now trades at trailing 12-month P/E and P/B of 17.77x and 3.24x respectively. All per share information and relevant calculations are done using the post-split shares outstanding. Therefore the 'actual' closing high of $16.97 is adjusted to allow for comparison.



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Recent Developments

For Q4 FY 2018 JETCON reported its weakest quarter for the period under review. Revenue fell $21.10 million or 7.27% to $269.23 million. Gross profit margin also slipped to its lowest level for the period under review to 5.10% significantly lower than its average Q4 gross margin for the period FY 2015 – FY 2018 of 13.39%. This resulted in a gross profit of $13.73 million and eventually a loss of $2.25 million in the quarter.

Key Financial Data

	2014	2015	2016	2017	2018	CAGR
BVPS	0.11	0.18	0.50	0.74	0.86	66.06%
EPS	0.018	0.069	0.170	0.264	0.158	72.13%
Dividend Per Share				0.023	0.035	
Dividend Payout Ratio				8.85%	22.21%	
Dividend Yield				0.49%	1.15%	
Income Statement Data ($)						
Revenue	349,040,626	523,245,799	857,044,456	1,176,584,124	1,161,472,587	35.06%
Gross Profit	53,226,363	87,597,870	153,188,388	221,696,959	162,299,575	32.14%
Operating Profit	23,422,503	55,309,963	105,074,702	156,113,615	94,717,741	41.81%
Net Profit	10,466,373	40,349,411	98,987,289	153,786,485	91,881,489	72.13%
Balance Sheet Data						
Cash and Equivalents	3,044,222	5,594,368	3,161,330	14,843,025	11,046,798	38.02%
Current Assets	91,140,472	113,237,240	297,263,645	469,015,868	480,854,449	51.56%
Inventory	71,664,852	84,479,822	250,826,759	393,821,450	434,648,425	56.93%
Non-Current Assets	31,520,901	30,864,271	35,837,768	68,769,767	82,008,362	27.00%
Total Assets	122,661,373	144,101,511	333,101,413	537,785,767	562,862,811	46.36%
Current Liabilities	45,580,581	33,490,023	39,086,940	92,285,768	58,310,973	6.35%
Non-Current Liabilities	10,726,322	3,907,751		12,465,743		
Total Liabilities						
Equity	66,354,470	106,703,737	294,014,473	433,034,256	504,551,838	66.06%
Ratios						
Inventory Turnover	4.02x	5.58x	4.20x	2.96x	2.41x	3.83x
Current Ratio	2.00x	3.38x	7.61x	5.08x	8.25x	5.26x
Cash Ratio	0.07x	0.17x	0.08x	0.16x	0.19x	0.13x
Debt to Equity	0.16x	0.04x		0.03x		0.05x

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	2014	2015	2016	2017	2018	Average
Ratios						
Gross Margin	15.25%	16.74%	17.87%	18.84%	13.97%	16.54%
Operating Margin	3.70%	9.67%	12.04%	13.08%	7.82%	9.28%
Net Profit Margin	3.00%	7.71%	11.55%	13.07%	7.91%	8.65%
ROE	17.12%	46.63%	49.40%	42.30%	19.60%	35.01%
ROA	8.17%	30.25%	41.49%	35.32%	16.70%	26.38%
P/E			11.79x	18.25x	19.29x	16.44x
P/B			3.97x	6.48x	3.52x	4.66x
Close Price	N/A	N/A	2.00	4.81	3.04	

Financial Overview

Revenue has increased at a CAGR of 35.06% for the period under review (FY 2014 – FY 2018). However, in FY 2018 JETCON's revenue experienced a decline of $15.11 million or 1.28% from FY 2017 levels. FY 2018 was the only year for the period under review that JETCON experienced decreasing revenue. The main reason for the deterioration in revenue is the weak performance in Q3 and Q4 FY 2018 of 13.93% and 7.27% respectively. Net Profit Margin has surged at a CAGR of 75.13% for the period under review. However, in FY 2018 earnings have tumbled 40.25% or $61.91 million to $91.88 million, due to poor performance in Q3 and Q4 FY 2018.

The primary contributor to inventory was motor vehicles. At the end of FY 2018, JETCON recorded inventory of $434.65 million of which more than $414 million (95%) was motor vehicles, goods-in-transit and parts. Inventory has been the most significant contributor to current assets (90.39% in FY 2018) and total assets (77.22% in FY 2018). The most significant contributor to current liabilities and total liabilities is payables. JETCON experienced its peak in long-term obligations in FY 2017 which was relatively insignificant at $12.47 million. This was a loan from NCB which was repaid in FY 2018 therefore at the end of FY 2018 JETCON was virtually debt free. Equity has increased at a CAGR of 66% for the period under review the main reason for this steady growth has been consistent earnings for the period under review. Additionally, in FY 2016 JETCON raised capital in its IPO increasing share capital to $88.82 million.

Inventory Turnover has trended lower since peaking in FY 2015 at 5.58x. The main reason for this is inventory growth outpaced revenue growth. The current ratio is relatively high peaking in FY 2018 at 8.25x. This is due to increased inventory and a decline in liabilities. Cash ratio has been relatively low, but given that JETCON has little to no debt the implication of a low cash ratio is unlikely to be meaningful. Debt-to-Equity has been relatively low for the period under review averaging 0.05x indicating that long-term liabilities can readily be met.

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JETCON grew margins for the period FY 2014 to FY 2017. However, in FY 2018 JETCON experienced a deterioration in gross, operating and net profit margins, which all fell below their 5-year average. The weakness in FY 2018 margins was primarily due to deteriorating margins faced in Q3 and Q4 FY 2018. Q4 FY 2018 was particularly bad, reporting Gross Margin of 5.10% the weakest quarter over the last four years. ROE and ROA have been relatively high for the periods F 2015 to FY 2017 however, both faced steep declines in FY 2018. JETCON effectively completed its 3 for 1 stock split on June 22, 2017, therefore, price per share calculations are done using the adjusted share count for consistency.

Forecast and Valuation

We used the relative value approach to arrive at our base case target of $2.08. Our base case assumes that investors' sentiment towards JETCON become more negative. We see this as likely for many reason chief among them is lower margins and declining earnings. As indicated previously margins have seen significant corrosion in the recent FY. Gross Profit Margin fell from 18.84% in FY 2017 to FY 13.97% in FY 2018. The decline in FY 2018 was largely due to margins in Q3 and Q4 FY 2018. Q4 FY 2018 was particularly troubling given that Gross margins were only 5.10%. This leads us to expect a material decline in earnings for FY 2019. The weakness in revenue growth specifically in the second half of FY 2018, revenue fell $67.52 million or 10.83% in the second half of FY 2018. JETCON's business operations are materially different from other listed entities and therefore finding a valid comparison is difficult.

Ticker	Market Cap(M)	P/E	P/B	Div Yield	ROA	ROE
JETCON	1,633	17.77	3.23	1.25%	16.70%	19.60%

Outlook

Our outlook on JETCON is negative given recent data and expectations for challenges in the used cars industry. The second half of FY 2018 was lacklustre with Q4 producing a loss of $2.25 million the only quarter of loss for the period of review. JETCON is in our view at an infection point. Therefore, we expect lower margins and marginal or no revenue growth in the near to medium-term. Additionally, interest rates on loans vehicles have trended lower for the period under review. Therefore the absence of revenue growth in FY 2018 is concerning given the macro-economic indications would indicate that revenue should continue to move higher.

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Key Risks to Our Price Target

The company is unable to meet our expectations for gross profit margins and revenue. While we maintained a conservative estimate for both the potential for underperformance if possible given reasons previously discussed.

Recommendation:

We recommend an **UNDERWIEGHT** rating on JETCON at this point given that the stock trades significantly above our base case scenario. In our projections we were conservative given recent performance indicating an infection point. However, we note that JETCON's fortunes could be materially worse than our current projections therefore this company is being closely monitored to assess if a downgrade would be warranted in the near future.

Source: http://www.Jamstockex.com, JMMB Investment & Research, Bloomberg, Various Company Financial Statements.

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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