INVESTMENT AND SOVEREIGN RESEARCH June-21-2021

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Caribbean Cement Company Limited

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Executive Summary

Caribbean Cement Company (CCC) began operations in 1952 and is a member of the TCL Group, with CEMEX S.A.B de C.V being its ultimate parent. The main activities of CCC and its subsidiaries are the manufacture and sale of cement, clinker and the mining and sale of gypsum, shale and pozzolan. CCC is the sole manufacturer of Portland and blended cement in Jamaica, with its central plant located at Rockfort, Kingston.

Revenue surged by $1.4 billion or 31.2% to $6 billion for the 3-months ended March 30, 2021, while profits increased by $1 billion or 215.9% to $1.5 billion. The primary reason for the increase in profits was cement sales, which in March 2021 reached a record 100,000 metric tonnes. Furthermore, cash flow from operating activities surged by 103.3% to $2.3 billion.

Revenue for CCC has steadily increased from FY 2016 to FY 2020 (period under review) at a CAGR of 6.3%. Meanwhile, EBITDA has grown at a CAGR of 30.4% for the same period. As a result, EBITDA peaked in FY 2020 at $7.8 billion, increasing 32.4% or $1.9 billion versus the prior year. The growth rate in EBITDA was partially due to CCC completing a major PP&E acquisition in FY 2018.

CCC's stock has increased at a CAGR of 15.9% for the period under review underperforming the Main Market increase, which grew at a CAGR of 19.8% for the same period. However, YTD CCC is up 41.2% versus the Main Market's growth of 3.14%. Meanwhile, CCC's stock has modest liquidity, trading an average daily volume (ADV) of about 47.8 thousand each day over the last year.

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Recent Developments

CCC reported a $1.42 billion or 31.2% increase in revenue to $6 billion for the 1st quarter ended March 31, 2021. Meanwhile, net profit grew by 215.9% to $1.5 billion, partially due to the containment of operating costs. In addition, the surge in profitability aided the Company in producing Cash Flow from Operations of $2.3 billion, which helped the Company repay $1.9 billion of debt in the quarter.

CCC's revenue growth in Q1 was aided by a record of 100,000 metric tonnes of cement produced in March 2021.

Key Financial Data

	FY2016	FY2017	FY2018	FY2019	FY2020	CAGR	3M2020	3M2021	Change
BVPS	9.09	10.53	7.31	9.76	13.55	10.49%	10.32	15.35	48.78%
EPS	1.53	1.35	2.90	2.21	3.76	25.17%	0.57	1.79	215.92%
Share Price	34.80	32.46	42.40	83.41	62.81	15.91%	44.46	69.14	55.50%
Main Market (,000)	192.28	288.38	379.79	509.92	395.61	19.77%	379.24	394.66	4.07%
(In Billions)									
Revenue	15.78	16.51	17.57	17.76	20.11	6.25%	4.55	5.97	31.17%
EBITDA	2.70	3.03	5.32	5.91	7.82	30.43%	1.50	2.26	50.34%
Operating Profit	1.40	1.62	4.16	4.30	6.29	45.56%	1.14	2.26	98.29%
Pre-tax Profit	1.35	1.56	3.29	2.74	4.42	34.53%	0.70	1.89	172.02%
Profits	1.30	1.15	2.47	1.88	3.20	25.18%	0.48	1.53	215.92%
Non-Current Assets	6.71	8.29	23.78	23.63	22.98	36.03%	23.39	22.72	-2.85%
Current Assets	3.71	3.92	3.01	3.47	3.34	-2.59%	3.12	4.10	31.57%
Total Assets	10.42	12.21	26.79	27.10	26.32	26.07%	26.50	26.82	1.19%
Non-Current Liabilities	0.03	0.12	15.89	13.84	8.20	315.93%	12.85	6.46	-49.72%
Current Liabilities	2.65	3.13	4.48	4.95	6.59	25.54%	4.88	7.30	49.63%
Debt	0.10	0.55	12.16	9.16	4.44	155.63%	7.98	2.53	-68.33%
Equity (as reported)	7.74	8.96	6.22	8.31	11.53	10.49%	8.78	13.06	48.78%
Operating Cash Flow	1.72	3.20	4.37	4.81	7.00	41.98%	1.12	2.27	103.30%
Investing Cash Flow	1.70	2.23	16.66	1.33	0.78	-17.74%	0.12	0.08	-31.04%
Financing Cash Flow	(0.21)	(0.00)	11.05	(3.38)	(6.26)	134.89%	(1.18)	(1.94)	63.95%
Cement Sold (,000)	904.15	864.85	881.49	851.06	940.00	0.98%			
Ratios						Average			
EBITDA Margin	17.13%	18.33%	30.27%	33.26%	38.90%	27.58%	33.05%	37.88%	14.62%
Operating Margin	8.87%	9.82%	23.67%	24.23%	31.26%	19.57%	25.06%	37.88%	51.18%
Net Profit Margin	8.25%	6.95%	14.03%	10.60%	15.90%	11.15%	10.62%	25.59%	140.85%
Current Ratio	1.40	1.25	0.67	0.70	0.51	0.91	0.64	0.56	-12.07%
Debt-to Equity	0.01	0.06	1.96	1.10	0.39	0.70	0.91	0.19	-78.72%
ROE	18.36%	13.74%	32.50%	25.93%	32.22%	24.55%	15.19%	38.82%	155.60%
ROA	12.24%	10.14%	12.65%	6.99%	11.97%	10.80%	4.65%	15.90%	242.20%
P/E	22.75	24.04	14.63	37.69	16.72	23.17	30.54	13.88	-54.56%
P/B	3.83	3.08	5.80	6.34	8.61	5.53	4.31	4.50	4.52%
Stock % Change	82.87%	-6.72%	30.62%	96.72%	-24.70%	35.76%	36.98%	63.07%	70.54%
Main Market % Change	27.60%	49.98%	31.70%	34.26%	-22.42%	24.22%	-25.63%	-0.24%	-99.06%

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Financial Overview

Revenue grew consistently at a CAGR of 6.3% to $20.11 billion for FY 2016 to FY 2020 (the period); growth was primarily due to solid domestic cement sales. For the period, cement sales increased at a CAGR of 1% to a record of 940 thousand tonnes in FY 2020. Strong sales continued in Q1 FY 2021, with the Company reporting revenue growth of 31.2% to $6 billion.

EBITDA has surged from $2.7 billion to $7.8 billion for the period, producing a CAGR of 30.4%. For the period, the primary reason for the EBITDA growth rate was the restructuring in Q2 FY 2018, which allowed the Company to have FY 2020 expenses in line with FY 2016 expenses. Meanwhile, EBITDA increased 50.3% in Q1 FY 2021 to $2.3 billion due to costs only rising 10% despite solid revenue growth.

For FY 2016 to FY 2020, non-current assets increased at a CAGR of 36% due to CCC acquiring Kiln 5 and Mill 5 in April 2018. As a result, debt surged to $12.2 billion at the end of FY 2018. Subsequently, the Company has aggressively paid down its debt to $4.44 billion at the end of FY 2020. Furthermore, debt levels declined further in Q1 FY 2021 to $2.5 billion. **Therefore, CCC will easily be debt-free at its current pace by the end of FY 2021, significantly decreasing CCC's exposure to JMD devaluation versus the USD and aid FY 2022 profitability**.

CCC's 'reported' equity value fell in FY 2018 due to preference shares being removed from equity. However, it has since steadily improved, reaching $11.5 billion at the end of FY 2020 and $13.1 billion by Q1 FY 2021.

Cash flow from operations (CFO) has surged at a CAGR of 42% to $7 billion at the end of the period. The increase in CFO has allowed the Company to make aggressive cash outflow for financing activities of $6.3 billion in FY 2020. The primary use of cash in financing activities for FY 2020 was repaying debt and preference shares of $4.7 billion and $1.5 billion, respectively.

EBITDA Margin has improved for the period under review peaking in FY 2020 at 38.9%. The increase in the reduction in operating lease due to the assets purchased in FY 2018 aided the EBITDA Margin increase. CCC's current ratio has been consistently below 1x since FY 2017, partially due to the Company not keeping a high cash reserve and instead opted to pay down debt rapidly. We do not see this as being severely risky at this point, given the Company's current debt load, which would allow it to raise debt to meet near-term obligations if required. Debt-to-equity also surged at the end of FY 2018 to 1.96x due to higher debt associated with the asset purchase. However, at the end of FY 2020, it declined to 0.39x as the Company paid down debt and continues to grow equity. Furthermore, at the end of Q1 FY 2021, debt-to-equity further fell to 0.19x.

CCC's stock has underperformed the Main Market Index for the period under review. However, year-to-date, CCC's stock has significantly outperformed the Main Market, surging 41.2% YTD versus the Main Market's advance of 3.1%.

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Forecast and Valuation

We arrived at our price target of $84.20 using the Free Cash Flow to Equity (FCFE) model. Meanwhile, using the FCFE under two additional scenarios produced our upper- and lower-case price targets of $116.96 and $61.09, respectively. The primary differences between the various scenarios are the expectation for revenue growth and operating margins in FY 2021 and FY 2022. The best-case scenario assumes the increase in revenue seen in Q1 FY 2021 continues for the remainder of FY 2021 before stabilizing in FY 2022. Meanwhile, under the worst-case scenario, we see revenue decline in the second half of FY 2021. Finally, under our base-case scenario, we see revenue growth and operating margins reverting to their long-run levels.

Outlook

Our long-term outlook on CCC is positive due to our expectation of continued growth in the construction industry and the Company's declining debt levels. Even under our worst-case scenario CCC is expected to reduce debt to negligible levels by the end of FY 2021. Therefore, we expect strong free cash flow to equity in FY 2022 and beyond as interest payments and repayment of debt principal is significantly reduced.

CCC recently started to produce elevated growth rates in Q3 FY 2020 when revenue grew 31.7% to $5.7 billion. **Therefore, CCC will have a high bar to clear starting in the second half of FY 2021 to reach our best-case price target.**

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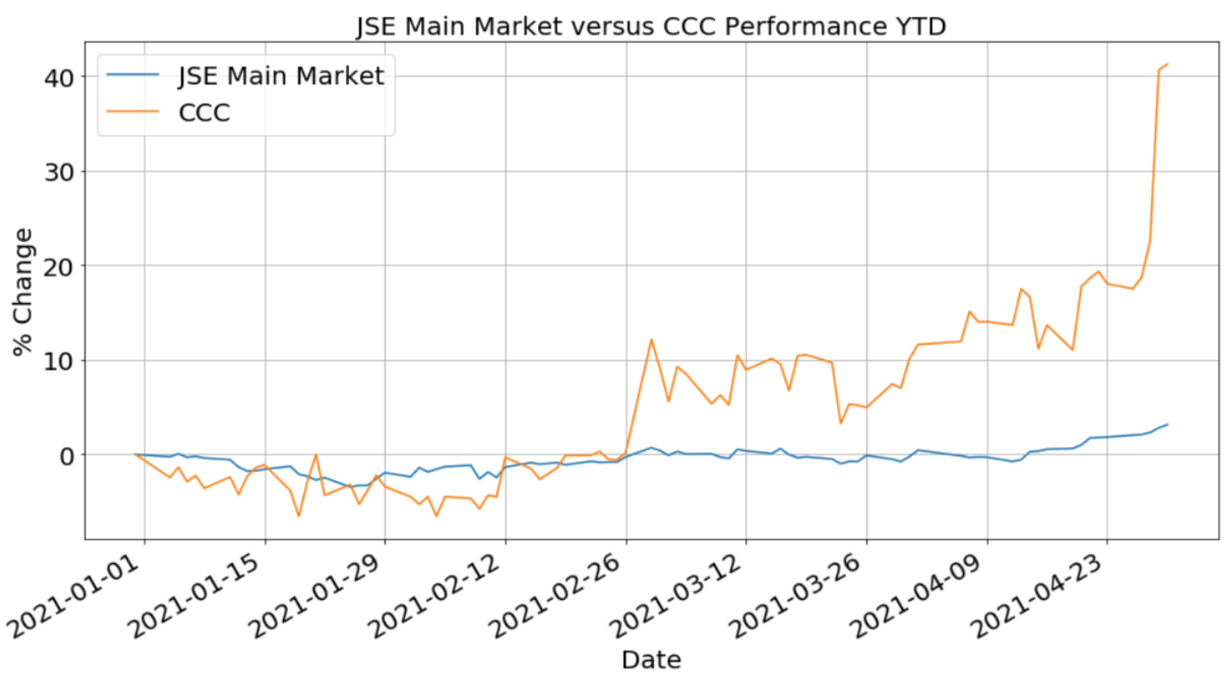
Recommendation:

We maintain a HOLD rating on CCC at this point, given that it trades marginally above our base-case price target and materially below our best-case price target. In addition, our recommendation considers the stability of CCC's earnings, operating cash flow, balance sheet strength and share liquidity.

We see several tailwinds ahead that could result in material upside from current levels. First, we view the aggressive debt repayment coupled with the Company's high operating cash flow generation as having a significant positive long-term effect. In addition, CCC could start returning cash to shareholders as dividends shortly, increasing sentiment toward the stock if the current trends hold.

At the end of Q1 FY 2021, CCC’s debt to equity was 0.19x, indicating long-term liabilities can be readily met. However, CCC's current ratio has remained depressed at 0.56x at the end of Q1 FY 2021, but we don't consider this an issue given that CCC is generating strong cash flow and is in a position to raise debt to meet short-term liabilities if required.



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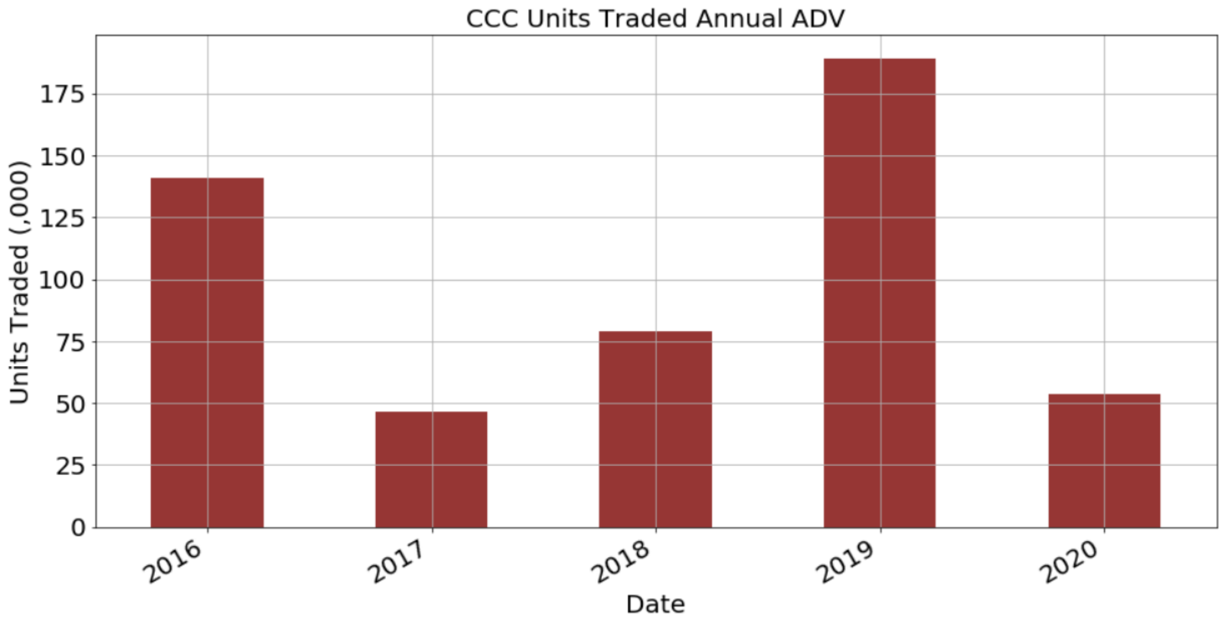

Source: http://www.Jamstockex.com, JMMB Investment & Research, Bloomberg, Various Company Financial Statements

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

UNDERPERFORM/UNDERWEIGHT— ADJUST EXPOSURE IN YOUR PORTFOLIO HELD AT JMMB TO BETWEEN 2.5% AND 4.9% FOR THIS PARTICULAR ASSET

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