



Derrimon Trading Company Limited (DTL)

PLEASE SEE IMPORTANT DISCLOSURES IN THE APPENDIX

Company Background

Derrimon Trading Company Limited (DTL) is a private company limited by shares, incorporated and domiciled in Jamaica. Its registered office is located at 233 and 235 Marcus Garvey Drive, Kingston 11. The principal activity of the DTCL is the distribution of bulk household food items inclusive of meat products. DTL also distributes branded products on behalf of a major global corporation.

In 2009, DTL purchased the assets of a wholesale distribution company and continued to operate from its original location at 233 Marcus Garvey Drive, Kingston 11. DTL maintained the entity's trading name, Sampars Cash & Carry. The Company also purchased Kerr's Enterprise Cold Storage Operations in 2011 at 8-10 Brome Close, Kingston 20 and rebranded same as Sampars Outlet- Washington Boulevard as the main hub for its cold storage distribution. During the year ended 31 December 2012, DTCL also acquired another distribution outlet in Downtown Kingston and branded it Sampars, West Street. In 2014, Derrimon Trading Company Limited acquired a 49% stake in Caribbean Flavours and Fragrances Limited (CFF). Also in 2014, the DTL acquired a Supermarket in Old Harbour and rebranded it as Sampars Old Harbour. In December 2016, DTL made an offer for another 26% per cent of the CFF.

SWOT Analysis:

Strengths: <ul style="list-style-type: none"> • Management has experience in the business area • Has well establish client base • Has shown a track record of profitability 	Weaknesses: <ul style="list-style-type: none"> • Lack of currency protection in earnings • High operating expenses • Liquidity constraints • Highly indebted
Opportunities: <ul style="list-style-type: none"> • Further expansion across the region • Increase automation through software • Further expansion in product offerings • 75% Acquisition of CFF opens the door for growth across the region 	Threats: <ul style="list-style-type: none"> • Slow economic growth could hinder sales revenue • FX movements could adversely affect costs of imported goods and net earnings

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Abridged Financials:

US\$ Million	Year Ended December								9 Months Ended September		
	2008	2009	2010	2011	2012	2013	2014	2015	2015	2016	Change %
Revenue	807.48	1,481.63	2,455.4	3,349.48	4,761.31	5,255.52	5,609.60	6,294.00	4,604.78	4,387.32	-4.7%
Cost of sales	754.85	1,392.11	2,295.9	3,100.61	4,349.31	4,694.56	4,983.19	5,460.67	4,032.21	3,807.93	-5.6%
Gross Profit	52.63	89.51	159.53	248.87	412.00	560.96	626.41	833.33	572.58	579.39	1.2%
Other Operating Income			46.52	55.84	35.86	39.37	48.32	8.22	9.619	11.13	15.7%
Total Operating Income	52.63	89.51	206.05	304.71	447.87	600.33	674.73	841.55	582.20	590.52	1.4%
Operating Expenses	41.91	78.45	177.30	259.52	403.02	499.52	585.58	702.29	477.56	479.13	0.3%
Administrative	37.41	67.02	142.43	186.73	303.92	384.09	471.83	538.26	386.12	376.09	-2.6%
Selling & Distribution	4.50	11.43	34.87	72.79	99.10	115.43	113.75	164.02	91.44	103.03	12.7%
Operating Profit	10.72	11.07	28.75	45.19	44.84	100.81	89.14	139.27	104.64	111.39	6.5%
Finance costs	2.33	2.89	11.26	9.27	19.52	29.32	45.60	87.08	66.45	62.50	-5.9%
Share of profit of associated comp.							8.12	35.95	30.49	27.10	-11.1%
Profit Before Taxation	8.39	8.18	17.49	35.92	25.32	71.49	51.67	88.13	68.69	75.99	10.6%
Profit for the year	8.39	4.66	11.66	23.94	15.79	49.93	51.61	51.61	68.69	75.99	10.6%
other comprehensive Income				25.543	17.58	14.38	(0.04)	0.65			
Total Comprehensive Income	8.39	4.66	11.66	49.49	33.38	64.30	51.57	52.26	68.69	75.99	10.6%
Total Assets	112.34	257.52	371.52	622.22	872.20	1,024.48	1,450.77	1,507.47	1,973.52	2,042.23	3.5%
Total Liabilities	111.24	247.88	344.32	551.44	768.04	716.47	1,091.19	1,058.56	1,545.26	1,517.88	-1.8%
Shareholder's Equity	1.09	9.64	27.20	70.78	104.16	308.01	359.57	448.91	428.26	524.35	22.4%
EPS (\$)	0.03	0.02	0.04	0.09	0.06	0.18	0.19	0.19	0.25	0.28	
Book Value per Share (\$)	0.00	0.04	0.10	0.26	0.38	1.13	1.32	1.64	1.57	1.92	
Key Ratios											
Net Margin	1.0%	0.3%	0.5%	0.7%	0.3%	0.9%	0.9%	0.8%	1.5%	1.7%	
Pre-tax Margin	1.0%	0.6%	0.7%	1.1%	0.5%	1.4%	0.9%	1.4%	1.5%	1.7%	
P/E Ratio	n/a	n/a	n/a	n/a	n/a	13.63	11.39	20.13	9.15	13.74	
Price / Book Value	n/a	n/a	n/a	n/a	n/a	2.21	1.63	2.31	1.47	1.99	
Return on Average Equity		87%	63%	49%	18%	24%	15%	13%	16.04%	14.49%	
Efficiency Ratio	80%	88%	86%	85%	90%	83%	87%	83%	82%	81%	

Financial overview

Net earnings for the 9 months ended September 2016 rose 10.6% to \$75.99M from a year ago. Total revenue declined by 4.7% from \$4.6B to \$4.39B. This improvement came on the heels of a healthy performance in the retail business segment. Meanwhile, other operating income has moved to \$11.3M from \$9.62M. From this standpoint, Total operating income inched up 1.4% to \$590.52M for year ended September 2016. Operating expenses have moved from \$477.56M to \$479.13M during the year ended September 2016 against the background of an increase in selling and distribution expenses. Selling and distribution expenses moved from \$91.14M in September 2015 to \$103.03M in September 2016. Such a

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movement was influenced by the company's strategy to improve efficiencies. Meanwhile, net finance costs have declined by 5.9% for the period ended September 2016 to close at \$62.5M.

The asset base of the company has increased by 3.5% to \$2.04B, while total liabilities have moved from \$1.55B to \$1.52B representing a 1.8 % decline. The increase in asset base was related to the increases in fixed assets, receivables, inventories and cash balance. Meanwhile, liabilities were influenced by decreases in payables and shareholders' loan. With this said shareholders' equity improved by 22.4% to close at \$524.35M amidst an increase in retained earnings.

Ratio Analysis:

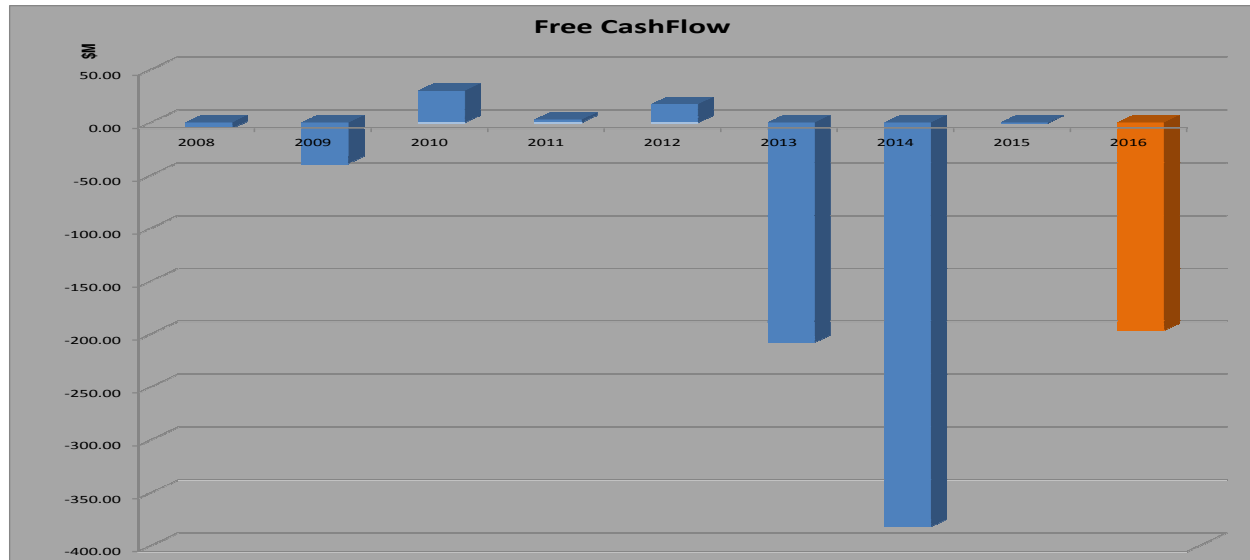
		Dec-09	Dec-10	Dec-11	Dec-12	Dec-13	Dec-14	Dec-15	Sep-16
Debt Ratios	Total Debt/EBIT	22.40	11.98	12.20	17.13	7.11	12.24	7.60	13.63
	Net Debt/EBIT	21.25	11.30	10.58	15.62	6.60	11.68	7.24	13.09
	Equity/Total Assets	3.7%	7.3%	11.4%	11.9%	30.1%	24.8%	29.8%	25.7%
	Long-Term Debt/Equity	106.8%	51.1%	38.4%	69.2%	15.8%	17.6%	109.6%	96.5%
	Long-Term debt/Total Assets	4.0%	3.7%	4.4%	8.3%	4.8%	4.4%	32.6%	24.8%
	Total Debt/Equity	25.7	12.7	7.8	7.4	2.3	3.0	2.4	2.9
	Total Debt/Total Assets	96.3%	92.7%	88.6%	88.1%	69.9%	75.2%	70.2%	74.3%
Liquidity	Net Debt/Equity	24.40	11.95	6.75	6.72	2.16	2.90	2.25	2.78
	Current Ratio	1.10	1.07	1.05	1.05	1.32	1.13	2.06	1.63
	CFO/Total Liabilities	-0.12	0.17	0.12	0.04	-0.23	-0.22	0.03	n/a
	CFO/CapEx	-3.91	2.06	1.04	2.49	-3.52	-1.60	0.99	n/a
	Acid test	0.91	0.61	0.62	0.61	0.68	0.54	1.03	0.99
	Net Operating Accruals/TA	0.14	-0.13	-0.06	-0.01	-0.11	-0.13	0.06	0.04
	Finance and Policy costs/ Free Cash Flow	-0.07	0.38	3.44	1.13	-0.14	-0.12	-186.88	-0.32
Profitability	Return on Equity	48.4%	42.9%	33.8%	15.2%	16.2%	14.4%	11.5%	14.5%
	Net Profit Margin	0.3%	0.5%	0.7%	0.3%	0.9%	0.9%	0.8%	1.7%
	Revenue/Total Assets	5.75	6.61	5.38	5.46	5.13	3.87	4.18	2.15
	Operating Margin	1%	1%	1%	1%	2%	2%	2%	3%
	Operating Efficiency Ratio	88%	86%	85%	90%	83%	87%	83%	81%
Working Capital	Inventory Outstanding	4.95	17.01	16.30	17.47	32.91	44.29	39.32	61.98
	Sales Outstanding	10.85	14.65	16.92	15.18	26.33	32.19	29.33	70.34
	Payable Outstanding	25.45	30.01	36.89	37.62	45.91	43.84	37.47	75.62
	Cash Cycle	-9.65	1.66	-3.67	-4.97	13.33	32.64	31.18	56.70

Source: www.jamstockex.com, Bloomberg and JMMBIR

The company seemed to have experienced some fluctuation in its debt levels over the review period. On the other hand, the liquidity level of the company has deteriorated during the review period through waning working capital levels. Profitability levels despite being stable have remained low as evidenced by its margins.

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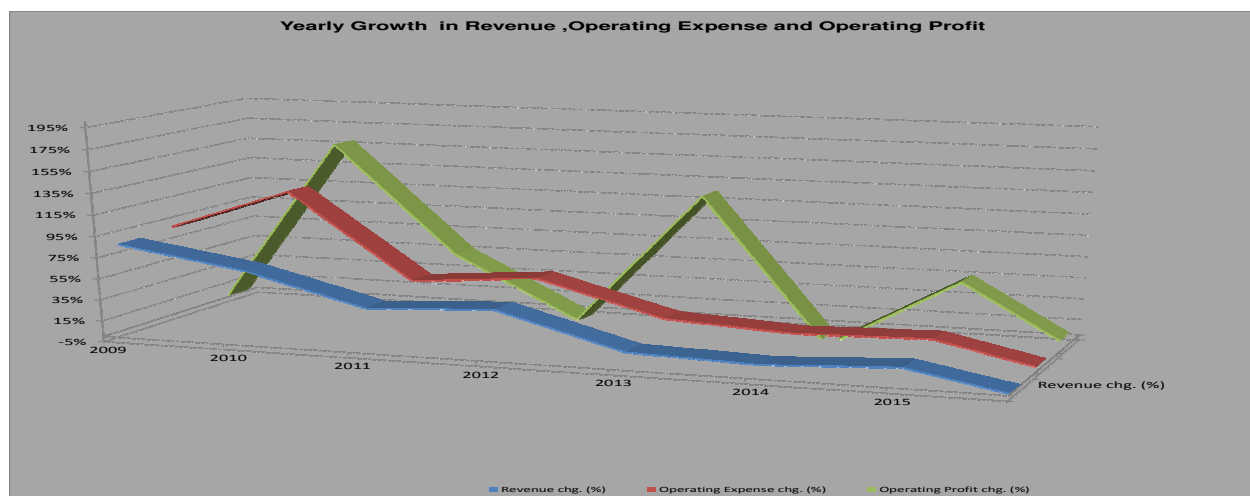
Graph 1: DTL's Free Cash Flow



Source: www.jamstockex.com, Bloomberg and JMMBIR

The free cash flow has been negative since 2013 and there seems to have been a deterioration of cash generated from operating activities (see Graph 1 above). On the flip side there have been increases in capital expenditure emanated from the expansion in capacity.

Graph 2: DTL's --Yearly Growth in Revenue Operating Expense and Operating Profit

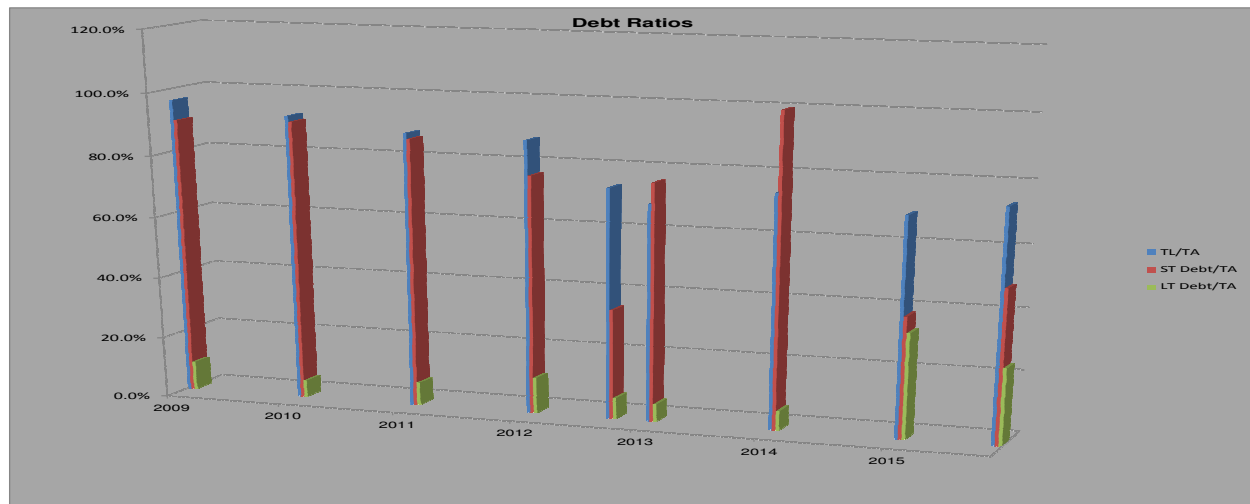


Source: www.jamstockex.com, Bloomberg and JMMBIR

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Graph 3: DTL's Debt Ratios



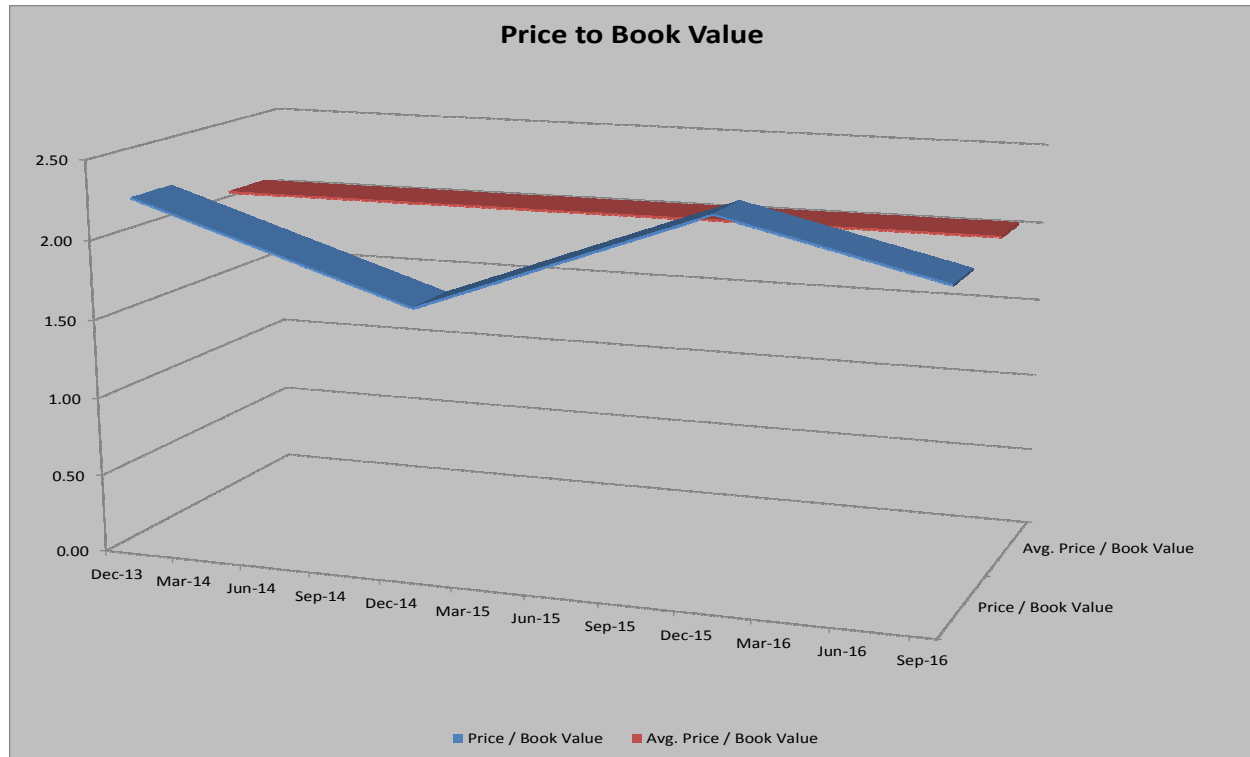
Source: www.jamstockex.com, Bloomberg and JMMBIR

Forecast and Valuation

The company has been experiencing low margins due to competition among other market players. From this standpoint, the company has actively reviewed its distribution division portfolio with a view to cut low margin items in a bid to enhance profitability and efficiency. Taking full control of CFF will allow DTL to chart the path of two companies and fully integrate these companies. This integration will allow DTL to benefit from the synergies. Net earnings are forecasted to reach \$129.29M or EPS of \$0.47 for 2017 financial year. Assuming a forward price-to-earnings (P/E) ratio of 14 times (3-year Average is 15.05 times, while trailing P/E is approx. 20 times), the targeted price of the stock at the end of the 2017 financial year is likely to reach \$6.62.

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Graph 4: Price to Book Value of DTL



Source: www.jamstockex.com, Bloomberg and JMMBIR

From a price-to-book value standpoint, the current price-to-book value ratio of 20.61 times is above its 3-year average of 15 times. Assuming the stock trades close to its historic average at 14 times and a projected book value per share of \$2.26, the likely target price for the 2017 financial year end is \$4.53.

Recommendation:

Based on the valuations above, Derrimon Trading Company Limited (DTL) is likely to trade within the range \$4.81 to \$6.62. The company will continue benefit from the tax break associated with listing on the Junior Stock Exchange. The company has embarked on its plans to improve capacity which has helped to put a strain on cash resources. From this perspective, the company is likely to be challenged to make dividend payments in the near term. Notwithstanding, the increase ownership in CFF and the strategic initiatives to improve efficiency could enhance the financial health of the company in the medium term. This stock is recommended as **MARKETWEIGHT** at this time.

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

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IMPORTANT DISCLOSURES

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

PLEASE NOTE THAT NO INDIVIDUAL ASSET IN YOUR PORTFOLIO SHOULD HAVE A WEIGHTING GREATER THAN 5% UNLESS OTHERWISE RECOMMENDED BY YOUR PORTFOLIO MANAGER OR A SPECIFIC JMMB RESEARCH REPORT. CONSEQUENTLY THE FOLLOWING **DEFINITIONS** ARE PROVIDED FOR CLARITY.

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