

## Dolphin Cove Limited (DCOVE)

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INFRINGEMENT IN THE APPENDIX**

### Executive Summary

Incorporated and domiciled in Jamaica, Revenue from Dolphin Attractions is the primary revenue generating activity and involves the sale of dolphin, stingray and shark interaction programmes. The Group's sales also include revenue from "Ancillary Services" which includes the sale of souvenirs, photographs, food and beverages and the use of its beach cabanas and tours such as kayaks, boat, and the Yaa man park opened in 2017. The company continues to earn most of its income in United States dollars.

The company's shares were listed on the Junior Market of the Jamaica Stock Exchange on December 21, 2010. In 2015, World of Dolphins Inc. acquired 58.51% of its issued share capital, from a majority shareholder. Effective January 8, 2016, World of Dolphins Inc. holds 79.99% of shares issued by Dolphin Cove Limited.

- **Dolphin Discovery Group, the parent company of Dolphin Cove Limited, invested more than US\$2.0M on improvements to the Jamaican parks in 2017 and intends to spend an equivalent amount in 2018 on capital expenditure.** The investments in 2017 were partially used to relaunch Prospect Park as Yaaman, an adventure and cultural park in Ocho Rios. The company set aside US\$1.45M for its park in St. Lucia and had approved US\$3.5M for the total project cost. St. Lucia would be the third country in which Dolphin Cove operates and the fourth is underway as land has been acquired in the Turks & Caicos for a fourth location. Dolphin Cove Negril was rebranded as Dolphin Cove Montego Bay and offerings were expanded to kayaking and Segways.

The hotel sector is currently expanding its capacity which could be a boon for DCOVE if the hotels are able to translate this expansion into permanent improvements in visitor numbers. The company attributed its new online booking platform and websites for increasing individual and small group visits. DCOVE's visitors typically originate from cruise ships or hotels and the move was made to accommodate individuals who are increasingly planning their own activities while staying in hotels or in rooms rented via sites such as Airbnb.

The tourist sector continues to expand as stopover arrivals for the January – May 2017 period amounted to 972,634, a 3.4% increase year-over-year. Cruise passenger arrivals stood at 885,231 for the same period, up 5.4% from the comparable period of 2016. The number of cruise calls for the period was 301, up 7.9% from 2016. May 2017 saw cruise calls to the Falmouth Port falling 20% while the number of passengers were down 9.7%. This is cause for concern after Tourism Minister Edmund Bartlett announced in July 2017 that two cruise ships temporarily withdrew from the Port of Falmouth. This move was reported to have been driven by widespread tourist harrasment. The Minister anticipates that continued growth at the Montego Bay and Ocho Rios ports will offset these losses and result in continued

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growth in cruise arrival numbers. However, the issue of tourist harrasment is not limited to the Falmouth Port and if not tackled head on, could led to withdrawals at the other ports.

Based on these assumptions, we forecasted revenues of US\$15.82M for the year ended December 31, 2017 and net profits of US\$2.98M, up 3.6% and 4.1%, respectively. We anticipate high tax expenses in the current year as the company's tax holiday has come to an end. The projected net profit corresponds to an earnings per share (EPS) of US\$0.01 or J\$0.98<sup>1</sup>, which when applied to 1-year P/E ratio average of 15.78x yields a price of US\$0.12. DCOVE's shareholders' equity is expected to rise 4.4% to US\$26.6M which corresponds to a book value per share of US\$0.07. Applying the 1-year price-to-book ratio average of 2.25x yields a price of US\$0.15. Averaging these prices produces a fair price of US\$0.14 per share or J\$17.56.

- **We recommend Dolphin Cove as MARKETWEIGHT as the stock's last trade price on July 25, 2017 was \$17.50.** Dolphin Cove is suitable for medium to long-term investors who are seeking capital appreciation, dividend income—given the high pay-out ratio and exposure to the growing hospitality & tourism sector. Dolphin Cove paid a dividend of J\$0.60 per share in 2016, a yield of 3.9%. DCOVE enjoys healthy margins, strong capital reserves and solid liquidity and generates the majority of its income in U.S. dollars, shielding it from the impact of JMD depreciation.

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<sup>1</sup> assuming an average annual exchange rate of US\$1:J\$129.21 for 2017

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### Company Background

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### Financial Performance – Year ended December 31, 2016

#### *Profitability*

For the 2016 financial year, DCOVE reported total revenues of US\$15.26M, up 1.4% or US\$206.3K year-over-year. This increase was driven by a 26.4% or US\$1.35M increase in ancillary services revenues to US\$6.46M which offset an 11.5% or US\$1.14M decline in dolphin attraction revenues to US\$8.81M. The increase in ancillary revenue was attributed to the "introduction of new products as well as new sale strategies which served to boost sales".

Direct costs of dolphin attractions fell 32.9% to US\$416.58M while direct costs of ancillary services declined 4.1% to US\$717.09M. This resulted in a 3.2% increase in gross profits to US\$14.13M while the gross profit margin improved to 92.6% compared to 90.9% in 2015. Operating expenses rose 4.8% to US\$10.7M as selling expenses rose 3.4% to US\$4.41M while other operating expenses climbed 12.2% to US\$3.77M. Administrative expenses declined 2.3% to US\$2.53M. The operating profit margin was relatively unchanged at 22.5%.

Finance income fell 22.5% to US\$172.39K while finance costs were down 1.2% to US\$307.94M leading to profits before taxation of US\$3.29M, unchanged from the previous year. Net profit for the year fell 13.8% or US\$456.89M to US\$2.86M as a taxation expense of US\$431.74M was recorded for the year, which compares to the taxation credit of US\$26.43K in 2015. This tax expense comes for the first time since listing on the stock exchange due to the end of the 100%, 5-year tax holiday the company was enjoying. DCOVE will now pay tax at 50% of the corporate tax rate for the next five years.

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### *Solvency & Liquidity*

Dolphin Cove's total assets amounted to US\$29.20M as at December 31, 2016, up 2.9% or US\$823.82K from the prior year. Driving this increase was the booking of US\$1.45M in amounts due from related parties, when no such entry was made as at December, 21, 2015. Also contributing to this increase was a 4.7% or US\$912.85K increase in property, plant & equipment to \$20.29M. Live assets amounted to US\$3.87M, up 2.6% from a year earlier. The company recorded no securities purchased under resale agreements as at December 31, 2016, compared to US\$1.36M as at December 31, 2015.

Cash & equivalents were down 20.4% to US\$1.22M while investments rose 11.4% to US\$300.04M. The cash ratio fell to 0.69x from 1.66x a year earlier while the current ratio stood at 1.62x, which compares to 2.66x as at December 31, 2015. Net cash flows from operations amounted to US\$3.89M, up slightly from US\$3.81M in 2011.

Total liabilities were down 4.8% or US\$189.78K to US\$3.76M, year-over-year. Driving this decline was a 42.9% or US\$455.68K decline in long-term liabilities, partially offset by a 24.3% increase in accounts payable to US\$1.34M. Total debt fell 22.8% to US\$1.46M as the decline in long-term debt more than offset the 186.6% increase in bank overdrafts, which closed the year with a balance of \$113.29K. Interest expense fell to US\$104.79K in 2016, resulting in an interest coverage ratio of 32.7x, which is an improvement on the 25.4x for 2015.

Shareholders' equity rose 4.1% to US\$25.44M as retained earnings rose US\$982.95K or 9.7% year-over-year. Retained earnings amounted to US\$11.13M while capital reserves were relatively unchanged at US\$10.66M.

### **Outlook and Valuation**

Dolphin Discovery Group, the parent company of Dolphin Cove Limited, invested more than US\$2.0M on improvements to the Jamaican parks in 2017 and intends to spend an equivalent amount in 2018 on capital expenditure. The investments in 2017 were partially used to relaunch Prospect Park as Yaaman, an adventure and cultural park in Ocho Rios. The company set aside US\$1.45M for its park in St. Lucia and had approved US\$3.5M for the total project cost. St. Lucia would be the third country in which Dolphin Cove operates and the fourth is underway as land has been acquired in the Turks & Caicos for a fourth location. Dolphin Cove Negril was rebranded as Dolphin Cove Montego Bay and offerings were expanded to kayaking and Segways.

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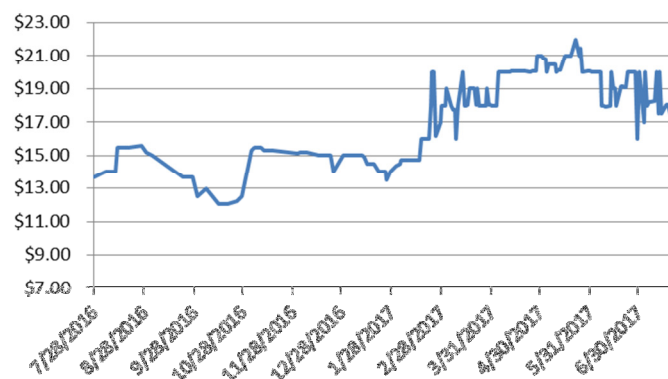
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**DCOVE 1-yr Stock Performance**



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### Recommendation

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### Abridged Financials

USD	Year Ended December 31				Change %
	2015	2016	3M16	3M17	
<b>Turnover</b>	<b>15,058,533</b>	<b>15,264,834</b>	<b>4,147,209</b>	<b>4,287,174</b>	<b>3.4%</b>
Operating Expenses	10,211,808	10,704,146	2,366,899	2,529,834	6.9%
<b>Operating Profit</b>	<b>3,379,986</b>	<b>3,427,456</b>	<b>1,570,448</b>	<b>1,535,501</b>	<b>-2.2%</b>
Profit Before Taxation	3,290,634	3,291,907	1,561,080	1,500,149	-3.9%
<b>Profit for the year</b>	<b>3,317,061</b>	<b>2,860,170</b>	<b>1,477,825</b>	<b>1,392,566</b>	<b>-5.8%</b>
<b>Total Assets</b>	<b>28,379,395</b>	<b>29,203,212</b>	<b>26,187,603</b>	<b>31,298,297</b>	<b>19.5%</b>
<b>Total Liabilities</b>	<b>3,951,662</b>	<b>3,761,883</b>	<b>3,354,187</b>	<b>4,464,403</b>	<b>33.1%</b>
<b>Shareholder's Equity</b>	<b>24,427,733</b>	<b>25,441,329</b>	<b>22,833,416</b>	<b>26,833,894</b>	<b>17.5%</b>
EPS (\$)	0.0085	0.0073	0.0038	0.0035	
Book Value per Share (\$)	0.0622	0.0648	0.0582	0.0684	
<b>Key Ratios</b>					
Gross profit margin	90.9%	92.6%	94.9%	94.8%	
Operating profit margin	22.4%	22.5%	37.9%	35.8%	
Net Margin	22.0%	18.7%	35.6%	32.5%	
Debt/Equity (x)	0.08	0.06	0.07	0.05	

**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**.

**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

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