Apex Africa CAPITAL LTD
Part of AXYS Group

March 2018

KQ 9-Months to Dec 2017 Earnings Update
"A Welcome Surprise"

Bloomberg Ticker	KNAL KN
Reuters Ticker	KQNA.NR

Share Statistics

Price	11.35
Market Cap (KES B)	64.5
Market Cap (USD M)	382.0
Year end	31-Dec
Float (%)	36.7
Foreign Ownership (%)	8.7
3-Month D. Avg Trading Val (USD)	10,494

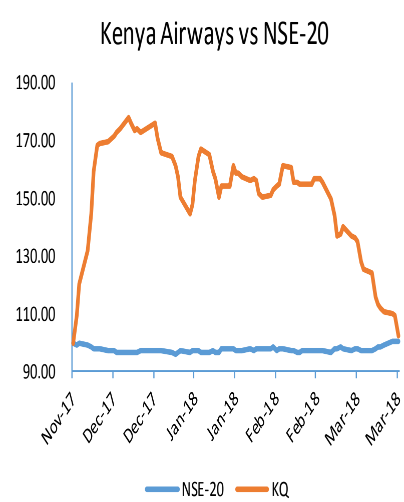
The airline's management decided to change the financial year-end from 31st March to 31st December which resulted in a surprise earnings release this morning. Given the numbers provided, we have apportioned the FY17 (to March 2017) figures to offer an appropriate basis for comparison. The airline posted an improved, though negative, bottom-line of a loss of KES 6.1B supported by galloping operating profit (+94.1% y/y).

Top-line continues to pick-up: Continuing from the previously observed trend, the top-line edged up 1.4% y/y to KES 80.8B attributed to improved cabin factor to 76.2% (from 72.3% in FY17) and a slight uptick in the number of passengers to 3.43M (from apportioned number of 3.35M). The improvement was however dented by the 6.5% decline in yield per passenger kilometer to 8.1 US cents driven by market capacity pressure and currency fluctuations. The prolonged electioneering period led to a 20% decline in domestic traffic during the period further curtailing the top-line growth

Cost management discipline pays-off: The airline industry is highly competitive with global and regional airlines fighting for market share across the skies. As a result, price competition is very stiff and airlines continually look for avenues to contain their costs. Despite the fuel costs rising during the period (+14.0% y/y to USD 62.0 per barrel) the airline registered a 77bps improvement in operating profit margin to 1.6%. Fleet costs (-9.3% y/y to KES 10.6B) and overheads (-15.4% y/y to KES 15.4B) closed lower; raising margins.

Capital optimization plan bearing fruit: During the period, the airline carried out an extensive capital restructuring exercise that saw the airline come from a negative equity position to a positive one (KES 0.5B). With some of the debt being converted into equity, the finance costs incurred fell (-5.3% y/y) leading to a 12.6% y/y decline in other costs to KES 7.3B. With the capital optimization being actualized towards the end of the period, the full effect on finance cost will be felt in FY19. The stability of the African currencies in the year saw the airline's forex losses plunge 72.6% y/y to KES 1.0B further lowering the other costs.

Price Trend



Source: (NSE)

Not yet out of the woods

The biggest hurdle for the airline in its recovery plan is growing its top-line in the midst of growing competition. To address this the airline plans to leverage on the direct flight to New York to be launched in 4Q18. Management estimates this to grow its top-line by 8.0% to 10.0% upon launch with the full effect to be realized from FY19 onwards. In addition, the airline plans to grow the use of partnerships and joint ventures with other airlines to target high traffic areas to grow its top-line. The airline plans to grow its fleet by calling back its leased dreamliners from Oman Air which will be largely used in the direct flight to New York and other new routes.

Among the biggest risks for its cost containment is rising fuel costs which amount to c.25.0% of the airline's bottom-line. The firm has announced plans to hedge its fuel costs which will keep these costs optimal. In addition, the airline intends to introduce Q400 aircrafts instead of jet engines in regional flights given that the former are more effective for shorter distances.

The excitement on the airline seems to have come to an end with the counter's share price

Senior Research Analyst

Harrison Gitau

hgitau@apexafrica.com

+254 (20) 760 2545

coming off drastically over the past few weeks. Adding insult to injury, the airline's performance, though good, was below the high expectations rallying the enthusiasm in the market. On a comparative basis, the airline ranks as among the most expensive publicly traded share with a P/B of 154.6X though it used to trade at negative equity position. The recovery story is still unfolding though at a slower rate than market expectation. In addition, the lenders who converted their debt into equity have been seen to be off-loading their stake in the market, raising supply while depressing prices. These two are likely to keep the share price depressed but the counter is anticipated to realize a support level at around KES 8.00.

Financials

Income Statement	FY17	FY17 Apportioned	9M to Dec 2017	p/p change	y/y change
	KES B	KES B	KES B	%	%
Total Income	**106.3**	**79.7**	**80.8**	**-24.0**	**1.4**
Total Operating Costs	(105.4)	(79.0)	(79.5)	-24.6	0.6
Operating Profit	**0.9**	**0.7**	**1.3**	**45.6**	**94.1**
Other Costs	(11.1)	(8.3)	(7.3)	-34.5	-12.6
Loss Before Income Tax	(10.2)	(7.7)	(6.0)	-41.5	-22.0
Income Tax (Expense)/Credit	0.2	0.2	(0.1)	-	-
Loss For The Period	**(10.0)**	**(7.5)**	**(6.1)**	**-38.9**	**-18.6**
Other Comprehensive Income					
Gain on Hedged Exchange Differences	0.7	0.5	1.3	76.6	135.4
Total Comprehensive Loss for the Period	(9.2)	(6.9)	(4.8)	-47.8	-30.3
Basic Loss Per Share (KES)	(26.61)	(20.0)	(1.04)	-96.1	-94.8
Diluted Loss Per Share (KES)	**(26.61)**	**(20.0)**	**(0.81)**	**-97.0**	**-95.9**

Statement of Cash Flows	FY17	FY17 Apportioned	9M to Dec 2017	p/p change	y/y change
Cash Generated From Operations	13.4	10.1	11.6	-13.7	15.0
Interest Received	0.06	0.0	0.03	-48.4	-31.2
Interest Paid	(7.4)	(5.5)	(4.9)	-33.4	-11.2
Income Tax Paid	(0.16)	(0.1)	(0.0)	-72.4	-63.2
Net Cash Generated From Operating Activities	**6.0**	**4.5**	**6.7**	**11.9**	**49.2**
Purchase of PPE	(0.8)	(0.6)	(0.7)	-15.3	12.9
Proceeds From Disposal of PPE	5.7	4.3	0.02	-99.7	-99.6
Commitment Fees and Aircraft Deposits	(3.0)	(2.3)	(0.8)	-73.5	-64.6
Aircraft Deposits Refund Received	0.1	0.1	-	-	-
Onerous Lease Payments	(1.5)	(1.1)	(0.8)	-48.4	-31.1
Net Cash (Used in)/ Generated From Investing Activities	**0.6**	**0.5**	**(2.2)**	**-**	**-**
Payment for Share Issue Costs	-	-	(2.5)	-	-
Borrowings Received	22.7	17.0	4.4	-80.8	-74.4
Repayment of Borrowings	(24.9)	(18.7)	(9.1)	-63.5	-51.3
Net Cash Used in Financing Activities	**(2.2)**	**(1.7)**	**(7.3)**	**230.0**	**340.1**
(Decrease)/Increase in Net Cash and Cash Equivalents	4.4	3.3	(2.8)	-	-
Cash and Cash Equivalents at the Beginning of the Period	4.8	4.8	9.2	90.3	90.3
Cash and Cash Equivalents at the End of the Period	**9.2**	**8.1**	**6.4**	**-30.8**	**-21.5**

Statement of Financial Position	FY17	9M to Dec 2017	p/p % change
Non-Current Assets	119.4	118.2	-1.0
Current Assets	26.8	21.9	-18.2
Total Assets	**146.2**	**140.1**	**-4.1**
Equity Attributable to Owners	(45.0)	0.4	0.0
Non-Controlling Interest	0.0	0.1	8.2
Total Equity	(44.9)	0.5	0.0
Non-Current Liabilities	119.8	87.6	-26.8
Current Liabilities	71.3	52.0	-27.1
Total Equity and Liabilities	**146.2**	**140.1**	**-4.1**

Source: Company Filings & ApexAfrica Research

Appendix

Investment ratings

- **Buy:** A total return is anticipated in excess of the market's long-term historic annual rate (approximately 10%). Total return expectations should be higher for stocks that possess greater risk.

- **Hold:** Hold the shares with neither a materially positive total return nor a materially negative total return anticipated.

- **Sell:** Stock should be sold as materially negative total return is anticipated.

Disclaimer

ApexAfrica Capital Ltd
A The Riverfront, 1st Floor, Prof. David Wasawo Drive, Off Riverside Drive | P.O. Box 43676-00100 | Nairobi | Kenya |
T: +254-20-2226440 | Fax: +254-20-2319092 | Cell: +254-723-420204|
W : www.apexafrica.com
Part of AXYS Group
W : www.axys-group.com