June 2017

Centum FY17 Earnings Update

Centum Investment Company
"A bump in the road"

Centum Investment Company released their FY17 financials recording a **16.5% y/y** dip in **net earnings** to **KES 8.3B.** The overall group performance was commendable, notwithstanding the dip in performance. **Top-line** across the board soared **11.1% y/y** to **KES 20.8B** though the **80.9%** plunge in gains on disposals wrote-off the gains in the top-line. Cost control measures continue bearing fruit with the group's **total cost remaining fairly unchanged** despite the growth in the top-line.

Re-affirming confidence in the operations of the group, the board has recommended a K**ES 1.20 DPS (+20.0% y/y).**

Breakdown of the firm's financials

- Sales from the trading business (beverage, utilities and publishing businesses) leapt 15.5% y/y to KES 9.4B. This was attributed to the stellar performance of Almasi beverages following the successful investments of new RGB (returnable glass bottles) and PET (polyethylene terephthalate that's used in making plastic bottles) lines. First time full-year consolidation of Longhorn Publishers and Two Rivers Power and Sanitary companies (the two utilities that supply water and power at Two Rivers) buoyed up the top-line further.
  The RGB and PET lines saw the beverage business ease up on costs even as the top-line rose, resulting in a 37% growth in the beverage business. Overall improvement in efficiency in the trading business (440bps improvement in trading business profit margin to 12.7%) saw the segment record a 76.3% y/y surge in trading profit to KES 1.2B
- The financial services segment (Sidian Bank, Nabo Capital, GenAfrica Asset management and Zohari Leasing) was a bit gloomy with revenues remaining largely unchanged at KES 4.1B. This was further exacerbated by the 11.4% increase in funding and other costs to KES 3.9B resulting in a 67.4% slump in the segment's operating profit to KES 190.3M.
  The performance was attributed to the performance of Sidian Bank. The bank, was adversely affected by the rate capping that was effected late last year. In addition, the bank carried out a restructuring exercise, investment in technology and additional capacity to grow its corporate banking unit. These factors led to the bank recording a loss before tax of KES 168M in the year to March 2017.
- Centum group realised an 80.9% y/y plunge in gains on disposal to KES 1.0B. In FY16, the group partially disposed off its stake in Two Rivers Mall realising a gain of KES 3.2B. The group also disposed AON insurance brokers and a portfolio of listed securities, both resulting in a gain of KES 1.7B. In FY17, Centum completed an exit of its 26.43% stake in KWAL booking a KES 1.1B gain. The group also partially exited its stake in Platcorp Holdings Limited (8% stake) , realising a gain of KES 432M.
- Centum's investment and other income grew 12.4% y/y to KES 7.3B driven largely by revaluation of land at Vipingo Development. The group cemented its commitment to bring down operating costs realising a 21.8% y/y decline to KES 1.1B. Capitalization of some interest expenses saw finance costs decline 47.1% y/y to KES 1.0B. In light of the aforementioned, PBT fell 17.7% to KES 8.9B.

Bloomberg Ticker :	**CENTUM KN**
Reuters Ticker:	**ICDC.NR**

Share Statistics	
Current Price (KES)	39.50
Issued shares (M)	665.4
Market cap (USD M)	254.4
Year end	31 March
Free float (%)	44.7
Av daily trading vol (USD)	110,171

Price Trend

Source: Bloomberg

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Developments during the year

- The Company opened the Two Rivers Shopping Mall in mid-February. 70% of the Gross Lettable Area (GLA) has been let with some 16% of the GLA under negotiation. In the time the mall has been under operation, it has seen over 1.2M customers and is anticipated to further augment these numbers.
- Phase 1 infrastructure of Pearl Marina is complete; serving 41 acres. There are external and internal finishes ongoing on the other villas. Construction of access road from the Kampala - Entebbe Highway is set to commence later this year.
- Water and electricity provision at the Centum Vipingo industrial park is currently underway.
- Power projects (Amu and Akiira) progressing towards financial close. The two projects are also awaiting letters of support from the Government.
- The 120 acre farm in Ol Kalau (Agribusiness) continues to gain traction having exported high value herbs to the EU markets. It is anticipated to reach full utilisation of arable land by FY18.
- The company broke ground along Kiambu Road for the development of a school through a consortium of Centum, Investmentbridge Capital and Sabis International School.
- The Group has completed a feasibility assessment on healthcare provision and has identified an experienced operating partner.
- Deployed KES 1B in Almasi Beverage rights issue whose proceeds were used in the acquisition of new PET & RGB lines and the enhancement of its distribution network.

Going forward

- The group has KES 7B worth of bonds maturing this year which would bring down its gearing currently at 27% to desired levels of 25%. Management, however remains confident of the group's ability to internally generate funds to meet the debt obligation. Going forward, the group expects to take up more debt on corporate level financing which would further raise the gearing, but not beyond the desired level.
- Upon the opening of Two Rivers Mall, the mall is anticipated to earn rental income going forward. Since the mall is being accounted on equity basis (being a joint venture of Two Rivers Development Limited and Old Mutual), we expect to see a bulge in Centum's bottom-line (and not revenue).
- We expect Almasi beverages to leverage on the enhancement of their distribution network which may lead to the firm expanding its market share. This would lead to an improvement in the firm's top-line.
  The new RGB and PET lines are anticipated to further the group's cost saving measures which would enhance the bottom-line going forward.
- Aiming to further grow its Agribusiness, the group acquired 14,000+ acres of land in Masindi Uganda. It intends to use the land for the farming of grains and establish a vertically integrated value addition operation. The firm plans to start the farming by the end of the year.
- Management remains cognisant of the effects of the rate cap and expect interest margins to remain constrained. To address this, the bank plans to amend its business model, shifting towards non-funded income and corporate banking. Technology advancements made by the bank are anticipated to aid in cost cutting as well as enhancing customer experience. Despite all this, we expect the banking industry to remain fiercely competitive and in favour of the larger banks due to their ability to attract cheap deposits. As such, we do not expect rosy numbers from the bank in the medium-term.
- At Vipingo Development, the group plans to kick off with the Centum Industrial Park which is estimated to occupy 150 acres. In addition, the park is to be fitted with a solar power firm and a desalination plant that will see the whole park occupy 200 acres.
- The group is venturing into uncharted territory in education and health care targeting the middle income earners. The Sabis International School is anticipated to open in September 2018. Centum also expects to break ground on the initial medical facility in FY18. These are anticipated to further diversify the group's business as well as add on its revenue.

Given the pipeline of projects lined up by the group, we anticipate that, in the long-run, they will realise handsome returns. With the current depressed price of KES 39.50, we feel the company is materially undervalued trading at a P/B of 0.6x and a P/E of 3.6x. The counter is alluring for risk neutral investors given the complexity of the company structure and planned financing for the projects.

FY17 Financials

Income statement KES M	FY16	FY17	y/y (%)
Trading Business			
Sales	8,141	9,402	15.5
Operating costs	(7,462)	(8,205)	10.0
Trading Profit	679	1,197	76.3
Financial services			
Income from financial services	4,072	4,075	0.1
Funding and other costs	(3,488)	(3,885)	11.4
Operating profit from financial services	584	190	(67.4)
Investment operations			
Investment and other income	6,533	7,346	12.4
Realised gains on disposal of investments	5,419	1,033	(80.9)
Operating and administrative costs	(1,435)	(1,122)	(21.8)
Finance costs	(1,982)	(1,048)	(47.1)
Share of associate profits	1,074	1,347	25.4
PBT	10,873	8,943	(17.7)
PAT	9,948	8,310	(16.5)
EPS	11.75	10.93	(7.0)
DPS	1.00	1.20	20.0

Statement of financial position	FY16	FY17	y/y (%)
Portfolio investments	57,021	65,464	14.8
Cash and cash equivalents	10,197	5,639	(44.7)
Other assets	10,836	17,282	59.5
Total Assets	78,054	88,385	13.2
Customer deposits	12,040	9,799	(18.6)
Borrowings	16,356	20,986	28.3
Other liabilities	6,400	8,127	27.0
Total liabilities	34,796	38,912	11.8
Total equity	43,258	49,473	14.4

Statement of cash flows	FY16	FY17	y/y (%)
Net cash from operations	2,863	1,219	(57.4)
Net cash from investing activities	(10,384)	(4,076)	(60.7)
Net cash from financing activities	9,528	(1,701)	-
Cash derecognised on disposal of subsidiary	(816)	-	(100.0)
Net changes in cash and cash equivalents	1,191	(4,558)	-
Opening cash and cash equivalents	9,006	10,197	13.2
Closing cash and cash equivalents	10,197	5,639	(44.7)

Ratios and margins	FY16	FY17	y/y (%)
Trading business profit margin (%)	8.3	12.7	4.4
Financial services profit margin (%)	14.4	4.7	(9.7)
Group net profit margin (%)	41.2	38.0	(3.1)
Dividend pay-out ratio (%)	8.5	11.0	2.5
ROaE (%)	27.3	17.9	(9.4)
Total debt to equity (%)	37.8	35.2	(2.6)
NAV per share (KES)	59.08	67.34	14.0
P/B (x)		0.6	
P/E (x)		3.6	
Dividend yield (%)		3.0	

Source: Centum, ApexAfrica Estimates

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