

Company Update: Stanley Motta Limited (SML) 9M 2023 Analysis

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- Stock Recommendation: **OVERWEIGHT**
- Price Target **\$7.95**
- Current Price: **\$6.10**

- Shares Outstanding: 757,828,490 units.
- Financial Year End: December 31

ABOUT THE COMPANY

Stanley Motta Limited (SML) is a Jamaican real estate company primarily engaged in property rentals. In November 2017, the company acquired Unity Capital, a wholly owned subsidiary.

SML is the owner of 58 HWT, a significant business process outsourcing and technology park in the English-speaking Caribbean. Positioned at the convergence of Half Way Tree and New Kingston, 58 HWT spans approximately six acres of prime land and features over 200,000 square feet of recently constructed commercial office space.

SML aims to finish the expansion of its 126,000 square feet structure, Unit 1 by April 2024, expecting a substantial boost in earnings. Meanwhile, firms like Alorica Jamaica, Symptai Consulting Limited, Eppley Limited, and General Accident Insurance Company Jamaica Limited (GENAC) are currently renting units 2 to 5. The majority of the rental space at 58 HWT is leased to tenants under triple-net leases, with transactions denominated in US dollars.

Although SML does not have any upcoming developments, the company is receptive to new deals despite the slowing influence of elevated interest rates.

FINANCIAL PERFORMANCE SUMMARY

JMD ('000) *	FY 2021	FY 2022	9M 2022	9M 2023
Revenue	492,620	499,370	373,423	387,013
Operating Profit	352,176	331,388	234,208	262,015
Net Profit	798,300	848,581	173,706	196,610
EPS	1.05	1.12	0.23	0.26
Total Assets	6,516,223	7,193,860	6,520,192	8,219,462
Total Liabilities	1,084,131	1,112,933	1,081,746	1,934,091
Total Equity	5,432,092	6,080,927	5,438,447	6,285,371
ROAE (%)	15.69%	14.74%	15.11%**	14.87%**

(*) Except Earnings per Share (EPS)

(**) Trailing Twelve Months Return on Average Equity (TTM ROAE)



Dividend Policy

Originally, the Board had anticipated distributing around 90% of its net profit to shareholders as cash dividends. Nevertheless, owing to changes in the Return on Average Equity (ROAE) and liquidity requirements, the company has, on average, issued a payout of 32.17% over the past four years.



Outlook

The projected slowdown the global and domestic real estate markets due to higher mortgage rates is not expected to drag SML's earning in the short to medium term, because to the nature of the company's operations. However, the inflationary impact on interest rates and consumption patterns may slow the company's expansion momentum and increase the likelihood of defaults from new and existing tenants.



Projections and Valuation

We used a Free Cash Flow to Firm model with a cost of equity of **15.56%** and a weighted average cost of capital (WACC) of **14.40%** to produce an intrinsic price of **\$11.16**. We also used a Market Comparable Approach using an implied P/E of 8.09x to arrive at a price of \$8.46 and an implied P/B of 0.79x to arrive at a price of \$7.34. The weighted average yielded a target price of **\$7.95** per share.



Risks to Price Target

Low trading volume stands as the main contributor to the target price. If volumes increase and macro-economic conditions improve, we may see an uptick in the price. However, if volumes remain muted, with limited influence of the external environment, the price is expected to remain within range.

NINE MONTHS ENDED SEPTEMBER 30, 2023

In Q3 2023, SML experienced a 3.64% growth in rental income, increasing from \$373.42 million to \$387.01 million. Other operating income also saw a significant rise, moving from \$10.38 million to \$21.84 million. Administrative expenses decreased slightly from \$149,591 to \$146,841. Despite increased security costs, the overall administrative expenses fell by 1.84%, attributed to efficient cost management. This is particularly evident in the reduced spending on repairs and maintenance, lower electricity costs, and diminished foreign exchange losses. The operating profit showed positive momentum, increasing by 11.87% or \$27.81 million to \$262,015.

In 2022, SML got a new loan facility from First Global Bank Limited to refinance a US Dollar denominated facility previously granted by the Development Bank of Jamaica Limited for the construction of Unit 4 at 58 Half Way Tree Road. Elevated interest rates resulted in a 6.80% uptick in the finance costs associated with the above mentioned, along with the existing mortgage from Jamaica National Building Society. The profit before tax displayed an upward trend, growing 13.50% from \$177,466 to \$201,416. The company was granted special economic zone status under the Special Economic Zone Act (SEZA) of Jamaica effective January 2021, resulting in income tax being charged on applicable profits at zero. Nonetheless, there was a 2.39% effective tax rate for the 9 months period, which was 27 basis points above the comparative period. Ultimately, the net profit for the period expanded by 13.19%, which contributed to the earnings per share (EPS) increasing from \$0.23 to \$0.26.

As of September 30, 2023, total assets reached \$8.22 billion, marking a 26.06% increase over the previous period. While Property, Plant and Equipment was almost halved, Investment Properties increased by 25.86% as expansion continues, Receivables jumped 51.35% and Cash and Cash Equivalents almost tripled. However, the trailing twelve months (TTM) return on average assets (ROAA) decreased by 77 basis points, due to assets growing faster than the TTM net profit. Total liabilities rose by 78.79% to \$1.93 billion during the 9-month period, primarily driven by the growth in payables and both short and long-term borrowings. SML's liquidity position weakened with the current ratio falling from 1.09x to 0.85x, indicating the company's ability to meet short-term payments. The 33.06% rise in Retained Earnings coupled with the 18.99% increase in Cumulative Translation Reserve resulted in Shareholders' equity growing 15.57% to \$6.29 billion. Following this spike, the book value per share (BVPS) increased from \$7.18 to \$8.29, while the TTM return on average equity (ROAE) shed 25 basis points to land at 14.87%. The significant climb in total liabilities saw the company's solvency improving, with the debt-to-equity ratio increasing from 0.15x to 0.24x and the debt-to-capital ratio increasing from 0.13x to 0.19x.

OUTLOOK

The Completion of Unit 1

The ongoing construction of Unit 1 at 58 HWT Road will introduce an extra 84,000 square feet of leasable space. Only Productive Business Solutions Limited (PBS) has expressed interest in occupying the seventh and eighth floors thus far. However, SML has revealed that, as a precautionary risk management measure, the company intends to secure tenants for the building before the construction is done. This new commercial space is expected to increase the company's list of tenants and significantly increase rental revenue, despite rising administrative costs.

INVESTMENT POSITIVES

- With the USD weighing heavier than the JMD, SML enjoys the benefits of earning its rental income in USD and reporting its financial performance in JMD. This may also attract international tenants who prefer paying in the US currency.
- Units 2 to 5 are currently fully rented to stable and growing businesses, which lowers rental defaults and provides steady revenue to the company.
- SML has constantly paid dividends to its shareholders, which provides additional capital irrespective of the stock's price movement.
- Zero income tax charge granted by SEZA is expected to have a positive impact on the company's net profit and net profit margin, which should see EPS growing and more funds available for reinvestment.
- The company maintains a negative cash conversion cycle, indicating adequate working capital efficiency, which can improve liquidity and the overall financial performance of the company.
- The stock has relatively low trading volume, which reduces price volatility and stands as a consistent stock for long-term investors.

INVESTMENT NEGATIVES

- The impacts of high interest rates have not considerably impacted expansion plans, but it may slow short-term plans and pull the company's bottom line due to higher finance costs.
- Despite the growth in assets, the ROAA has been steadily declining, which may suggest inefficient asset allocation that can stymie the company's growth.
- The high interest rate environment can increase interest expenses for future debt raises, which will negatively impact the company's bottom line.
- Structural issues or upgrades may pull on the company's liquidity, if they use available the cashflow and debt to finance.
- The shipping attacks at the Red Sea could resurge supply backlogs, which could delay the completion of projects and slow revenue growth.
- The stock has relatively low trading volume, which reduces liquidity for investors who want to buy and sell the stock.



CONCLUSION

SML owns 58 HWT, a prominent business park, and specializes in property rentals. SML is completing the expansion of Unit 1 by April 2024, anticipating increased earnings. Notably, tenants like Alorica Jamaica, Symptai Consulting Limited, Eppley Limited, and General Accident Insurance Company Jamaica Limited currently occupy units 2 to 5 under triple-net leases, denominated in US dollars. While SML has no imminent developments, it remains open to new deals despite the impact of elevated interest rates. Q3 2023 indicated positive financial performance and growth for the company compared to the same quarter in the 2022.

We used a Free Cash Flow to Firm model with a cost of equity of 15.56% and a weighted average cost of capital (WACC) of 14.40% to produce an intrinsic price of \$11.16. We also used a Market Comparable Approach using an implied P/E of 8.09x to arrive at a price of \$8.46 and an implied P/B of 0.79x to arrive at a price of \$7.34. The weighted average yielded a target price of \$7.95 per share, which is 30.32% above to the current trading price.

As such, we recommend that investors **OVERWEIGHT** the shares in their portfolio.

SOURCES

Bloomberg, SML's Website (<https://stanleymottalimited.com/>), IMF, SML's Financial Statements, JSE, Jamaica Gleaner, Jamaica Observer, PSQJ, Damodaran Website

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- **OVERWEIGHT** - Security is deemed to be undervalued and is expected to outperform compared to the average market return and/or return of comparable securities in the same sector or industry.
- **MARKETWEIGHT** – Security is expected to provide similar returns compared to the market in general or at the same pace as comparable companies; neither strongly positive nor negative.
- **UNDERWEIGHT** – Security is deemed to be overvalued and is expected to underperform compared to the average market return and/or return of comparable securities in the same sector or industry.
- **ZEROWEIGHT** – This security is substantially distressed or at risk of a shock which may significantly impair its value.