

# Company Analysis: TransJamaican Highway Company Limited (TJH)

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- Recommendation: **MARKETWEIGHT**
- Price Target: **J\$1.43/ US\$0.0098**
- Current Price: J\$1.29/USD \$0.0085
- Market Value of Shares: \$16.1 billion<sup>1</sup>
- Financial Year End: December 31

## ABOUT THE COMPANY

TransJamaican Highway Limited (TJH) oversees the development, operation and maintenance of the tolled roadway known as “Highway 2000” under a Concession Agreement with the National Road Operating & Construction Company (NROCC) made in November 2001. The concession is for 35 years (ends 2036). The company has contracted with Bouygues Travaux Publics to construct the highway and Jamaican Infrastructure Operator Limited (JIO) to maintain and operate the toll road.

TJH maintains the East-West Highways, including the Portmore Causeway, Spanish Town, the Vineyards and May Pen ramp.

## FINANCIAL PERFORMANCE

(USD '000)	2015	2016	2017	2018	2019
Revenue	38,229	40,342	46,125	52,430	21,412
Net Income	(6,457)	(4,121)	1,818	7,008	(1,084)
Total Assets	351,776	339,379	329,653	310,511	292,209
Total Liabilities	290,845	282,569	271,094	253,560	226,958

### Dividend Policy

NROCC anticipates that the company will pursue a dividend policy that will pay the maximum allowable amount under the Companies Act annually. The payout ratio is expected to increase from approximately 27% to a high of 85% by 2026.

### Outlook

We believe that the company’s performance will turn around within the next year as economic activity picks up. This will allow for a continued increase in revenue due to both increased traffic as well as toll rate increases. The company also anticipates benefitting from the renewal of the concession agreement as well as the right to develop, operate and maintain future highways along with other investment opportunities.

### Projections and Valuations

We used a Discounted Cash Flow model to establish a price target for TJH. Based on assessment of the expected future cash-flow and with a cost of equity of 13.2% we obtained a price target of **JMD1.43/USD 0.0098**.

### Risks to Price Target

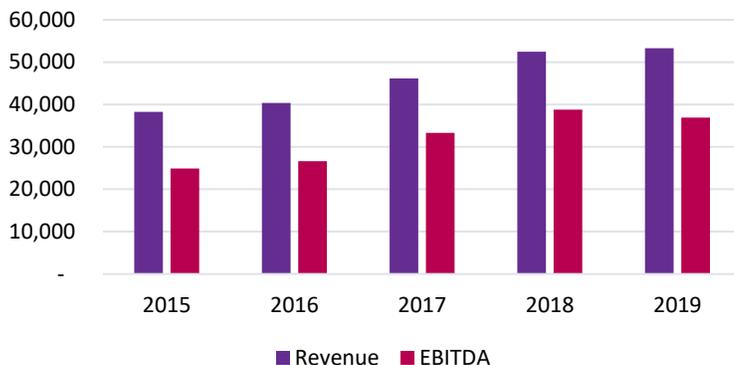
The persistence of the pandemic and possible behavioral changes among residents poses the largest risk to the company. If the pandemic continues to suppress daily traffic, the company will earn less Revenue and thus its financial performance will deteriorate faster than expected.

## FINANCIAL PERFORMANCE

(USD '000)	2015	2016	2017	2018	2019	2019 H1	2020 H1
Revenues	38,229	40,342	46,125	52,430	53,285	25,944	21,412
Net Income	(6,457)	(4,121)	1,749	6,350	8,300	1,511	-1,084
EBITDA Margin (%)	65.1	66.0	72.2	74.0	69.2	71.8	56.4
Net Profit Margin (%)	-16.9	-10.2	3.8	12.1	15.6	5.8	-5.1
Cash Flow Margin (%)	15.4	17.6	29.4	35.6	-11.8	28.5	33.1
Debt to Equity Ratio (x)	4.77	4.97	4.63	4.45	3.48	4.19	4.08

## FOR THE LAST FIVE (5) YEARS:

### Revenue and EBITDA (USD '000)



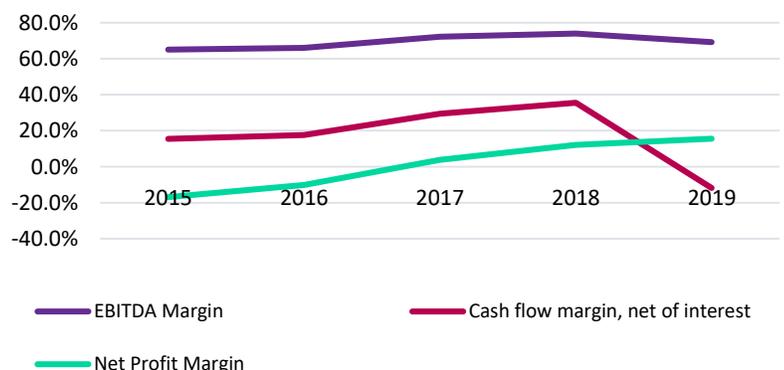
Between 2015 and 2019, Revenues increased by a Compound Annual Growth Rate (CAGR) of 8.7% due to a combination of toll price increases and increased traffic volume. Operating Expenses increased at a slower average rate of 6.0%, driven by the increase in Amortization Costs and Operator Fixed Fees from USD 13.8 million to USD 16.2 million and USD 9.2 million to USD 11.2 million respectively. Other than Operating Expenses, Finance Costs was the second highest expense incurred by the company. Between 2015 and 2018, TJH had several loans maturing in February 2029 that were actively being paid down, leading to a reduction in finance costs during that period. The reduction in finance cost along with the increase in Revenues allowed for greater profitability

during the period and after consecutive Net Losses, TJH became profitable in 2017. In 2019, however, Finance Costs more than doubled (USD 15.4 Million in 2018 vs USD 32.0 million in 2019), as a result of a high interest bridge loan facility undertaken towards the end of 2019 to repay other debts. TJH was able to maintain its profitability due to a tax credit of USD 21.4 million.

The Net Profit Margins associated with this investment are low, but not unlike other infrastructure investments. Infrastructure typically has high non-cash expenses, in the case of TJH, amortization, which leads to lower net profits. When observing the earnings before interest, amortization and depreciation (EBITDA) margins, these were comparable much higher increasing from 65.1% in 2015 to 69.2%, with a high of 74.0% in 2018. The Operating Cash Flow Margin was generally also much higher than the Net Profit Margin. It was negative in 2019 as a result of abnormally high Interest Expenses.

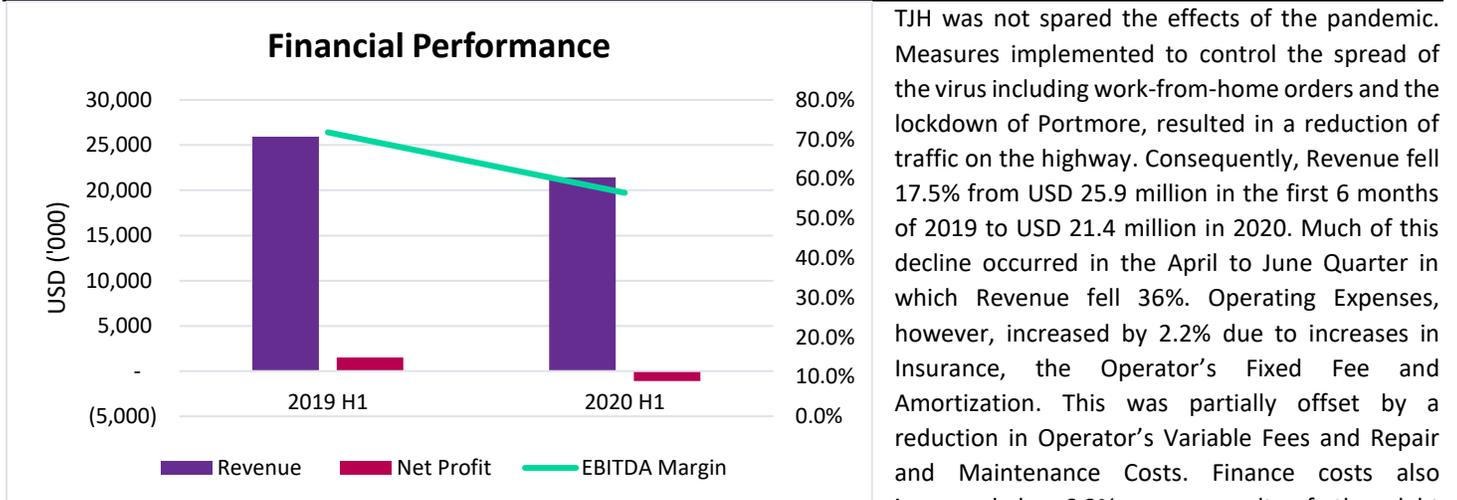
TJH's Total Assets have decreased from USD 351.8 million to USD 292.2 million (16.9%) mainly due to a 20.1% decrease in Intangible Assets along with a 69.2% decrease in Restricted Cash. This partially offset by an

### Profitability and Cash Flow Margins



increase in Cash from \$1.9 million to USD 9.1 million. The Intangible Assets are related to the Kingston to Sandy Bay toll road concession and are amortized over the lifetime of the concession based on its projected usage during the period. The Net Profit earned between 2017 and 2019 positively impacted the Accumulated Profits resulting in a 7.1% increase in Total Equity. Liabilities, on the other hand, fell 22.0% as a result of the debt amortization between 2015 and 2018, and the restructuring undertaken in 2019. Originally the borrowings were related to loans obtained from the Inter-American Development Bank (IDB), International Finance Corporation (IFC) and Proparco to finance part of the construction, procurement and engineering costs for Phase 1A and Phase 1B. These loans were set to mature in February 2029, with quarterly interest payments tied to the LIBOR rate. However, in preparation for listing of the company on the Jamaica Stock Exchange, these loans were refinanced. Since the company had a simultaneous increase in Equity and decrease in Liabilities, TJH reduced its leverage as measured by the debt to equity ratio. This ratio fell from 4.77x in 2015 to 3.48x in 2019.

## FOR THE FIRST 6 MONTHS OF 2020:



TJH was not spared the effects of the pandemic. Measures implemented to control the spread of the virus including work-from-home orders and the lockdown of Portmore, resulted in a reduction of traffic on the highway. Consequently, Revenue fell 17.5% from USD 25.9 million in the first 6 months of 2019 to USD 21.4 million in 2020. Much of this decline occurred in the April to June Quarter in which Revenue fell 36%. Operating Expenses, however, increased by 2.2% due to increases in Insurance, the Operator's Fixed Fee and Amortization. This was partially offset by a reduction in Operator's Variable Fees and Repair and Maintenance Costs. Finance costs also increased by 6.2% as a result of the debt

restructuring which occurred earlier in the year. The previous bridge loan facility was replaced with Secured Notes in the first quarter of the year. The decrease in Revenue and increase in Expenses resulted in a deterioration of the company's profitability. During the six-month period, TJH recorded a Net Loss of USD 1.1 million versus a profit of USD 1.5 million last year.

Total Assets increased by 8.0% from USD 303.3 million to USD 327.5 million. The majority of this increase is accounted for by a USD 26.3 million Deferred Tax Asset and the increase in Restricted and Unrestricted Cash by USD 16.1 million. This was partially offset by a USD 17.2 million decrease in Intangible Assets. The increase in Assets were funded by the issuance of USD 250 million in Senior Secured Notes, some of which was used to repay the bridge loan facility and dividends. The Net Result of this transaction was a USD 18.2 million (7.4%) increase in Liabilities. Equity increased by 10.2%. Although Share Capital was halved, as the existing preference shares were replaced with the issuance of 2.7 billion 8% Cumulative Redeemable Preference Shares, Retained Earnings increased from USD 4.5 million to USD 37.4 million due to the write back of the NROCC Shareholder Grant. The Debt to Equity Ratio decreased from 4.19x to 4.08x.

## OUTLOOK:

### The Impact of COVID-19 on Revenue and Cash Flow Generation and the Potential Recovery

The COVID-19 pandemic and measures used to control its spread brought the Jamaican economy to a virtual standstill. In particular, Portmore, where the company generates the majority of its Revenue, was under lockdown for two weeks due to a cluster of confirmed cases in the area. The other toll booths also saw a reduction in average daily traffic as many persons restricted their movement. As the pandemic persists, we expect that traffic will remain below pre-pandemic levels, resulting in a decrease in profitability as well as

cash flow, given that its largest expense items are fixed in nature. However, as the economy recovers within the next 2-3 years in line with base expectations, traffic is expected to return to pre-pandemic levels and increase beyond that. Traffic volume is also expected to increase as a result of housing projects in close proximity to the highway. Given that the urbanization of the Kingston Metropolitan Area and the subsequent housing pressures, the highway will connect newer housing developments outside of Kingston to the KMA. These housing developments would add to the pool of potential users of the highway thus increasing traffic volume. Nonetheless if consumption patterns change, that is, residents do not travel as much due to work from home situations among others, traffic may remain stifled.

### **Yearly Toll Price Increases Hedge Against JMD Devaluation**

Yearly, the company can request an increase in toll prices at or below a predetermined maximum/ "Capped Level". This "Capped Level" is calculated to hedge against the devaluation of the Jamaican Dollar. In the case that the request is not approved, TJH will be compensated as per the Concession Agreement. This allows for a fair degree of consistency and predictability of cash flows. Despite the pandemic and subsequent economic downturn, TJH increased its toll rates though later than normal in September.

### **Opportunities for Further Investment and Expansion**

The company has the opportunity to become involved in multiple future investments. Within the short to medium term, as per the concession agreement, the company has the first right of refusal to maintain, operate and/or own they May Pen to Williamsfield leg of Highway 2000. This represents an additional 28.0km that could be operated by TJH. The opportunity to be involved in the design, building, owning and operation of the Montego Bay bypass is also available to the company. In the medium, to long term, the most direct opportunity is the opportunity to renew the concession agreement at the end of 2036, for an additional 35 years. The company may also pursue opportunities to design, develop and manage key infrastructure projects such as drainage systems, extension of the current east-west corridor, bypass roads for major towns and cities locally and regionally.

## INVESTMENTS POSITIVES:

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- Generally steady cashflow from toll income
- High Operating Cash Flow Generation relative to Equity invested
- The highways provide road users with a faster and typically better maintained alternative for traditional routes that may plagued with potholes and other grievances for motorists
- Attractive Return on Investment
- Consistent revenue and expense profile
- Relatively low capital expenditure requirements year-over-year
- The Revenue is materially hedged against Jamaican Dollar devaluation
- Contractual Protections

## INVESTMENT NEGATIVES

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- Upward trend in the toll rates may be a deterrent from usage by motorists
- Natural Disaster may compromise the structural integrity of the highway
- High Degree of leverage in the early years
- Long time horizon for investment



## CONCLUSION

Although TJH's financial performance has dipped during the pandemic, we expect that the company's performance will return to pre-pandemic levels as the general economy recovers. Though there are downside risks, like residents reducing their travel due to work from home measures, these risks are small in comparison to the upside which includes further investments and a faster than anticipated recovery.

Based on our assessment of the company and our expectations of its performance we established a price target of **J\$1.43/US\$0.0098**. This implies a 10.1% upside from current levels. Considering the company's historical performance, along with its many opportunities for future growth, we expect that this investment should provide returns in line with the general market. As such, we recommend investors **MARKETWEIGHT** this stock.

## SOURCES

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TransJamaican Highway Limited Prospectus & Audited Financial Statements

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## DEFINITIONS

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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.