06/06/17

Chagala Group Ltd* (CGLO.L)

Corporate

FY16 Results

Forecasts revised following 2016 results

Chagala reported a 10% increase in adjusted profits before tax in 2016, despite a 14% fall in turnover and the ongoing effects of local currency devaluation in 2015. Although EBITDA was 4% lower, operating profit increased 17% on lower depreciation and admin costs. We have revised our forecasts slightly for this year to reflect top line assumptions, but lower operating and interest costs. No dividend has yet been proposed for 2016, and the ongoing shareholder dispute may influence when or if a dividend will be declared. However, we are assuming a minimum 50% payout, in line with the company's policy. The stock still trades on a significant discount to NAV, peers and our fair value.

- **Good results despite the impact of devaluation:** Room and rent revenue fell 11%, due to the ongoing effects of Tenge devaluation. However, lower costs, with salaries down 24% and admin costs 12% lower, meant that EBITDA fell just 4%. Reported profits were reduced by US$1.3m of litigation costs.
- **Outlook has improved:** Due to a more stable oil price and a gradual improvement in the local currency over the past year, the operating outlook has improved. Occupancy is still high and new sites were delivered last year at two locations.
- **Earnings forecasts revised lower:** We are expecting slightly lower revenues in FY17, with a 1% fall now pencilled in. We also forecast EBITDA to be unchanged. With lower debt costs, we expect adjusted PBT to more than double. We thus expect the NAV to start to recover this year on the improving profitability.
- **The valuation discount is unchanged:** NAVPS was flat last year, despite the weaker earnings, but we expect a recovery next year. The stock currently trades on a 64% discount to our 2017 NAV forecast and just 4.5x EBITDA. Recurring free cash flow is forecast to be c.US$4m a year (a yield of c.12.5%), which would easily support a potential dividend payout of up to c.US$1m.

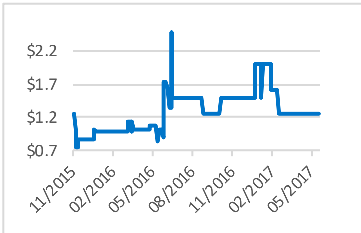
Dec Year End	FY14	FY15	FY16	FY17E	FY18E
Total revenues (US$m)	28.2	23.5	20.3	20.2	20.6
EBITDA (US$m)	9.2	8.0	7.7	7.7	7.8
PBT (US$m)	2.0	2.6	1.6	2.9	3.7
Reported EPS (USc)	6.8	8.8	3.0	9.6	12.4
Adj EPS (USc)	4.3	4.9	3.3	9.6	12.4
DPS (USc)	5.9	-	4.8	4.8	4.8
Free cash flow (US$m)	3.32	(1.54)	2.25	3.33	3.82
Net (debt)/cash (US$m)	(17.7)	(12.6)	(10.3)	(8.0)	(5.1)
Net LTV (%)	15%	15%	12%	10%	6%
NAVPS (US$)	4.78	3.56	3.57	3.52	3.63
EV/EBITDA (x)	4.8	4.9	5.7	4.5	4.0
P/NAV (x)	0.26	0.35	0.35	0.36	0.34
Dividend Yield (%)	4.7	-	3.8	3.8	3.8

Source: Company Data, Argento Capital

*Argento Capital Markets acts as financial adviser to the company and is an Appointed Representative of Citation Capital Management Ltd, which is authorised and regulated by Financial Conduct Authority.

Closing price	US$1.25
Shares in issue	21.25m
Market cap	£21m
Enterprise value	£25m
Share price as at	(close) (06/6/17)

Residential and commercial property provider to the oil & gas majors operating in Kazakhstan



Source: Capital IQ

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FY16 Results

Encouraging results despite currency devaluation

- Chagala reported a 10% increase in adjusted profits for 2016, despite a 14% fall in turnover and the devaluation of the local currency. Although the year-end rate was relatively unchanged, the average rate was 35% weaker than in 2015.
- Management commented that the results were in line with their projections and local market trends, despite the challenges of the local and wider economy. The generally difficult market included a reduction in oil and gas projects and staffing, which led Chagala to reduce the number of outlets.
- Room and rent revenue fell 11% due mainly to the effect of the weaker currency, which was a decent result. Food and beverage income was 25% lower, which was partly due to a slowdown in the development of projects like TCO, but was still ahead of the rate of devaluation. Other revenue was also 18% weaker.
- Continued cost control, with salaries down 24% and F&B costs 30% lower, plus the impact of the Tenge devaluation, meant that EBITDA only fell 4% to US$7.7m. As a result operating profit was actually up 17%.

Chagala FY16 Results (US$m)

	2015	**2016**	**Change**
Room and rent	17.53	15.62	-10.9%
Food & Beverage	3.46	2.61	-24.6%
Other revenue	2.54	2.08	-18.0%
Total Revenue	**23.53**	**20.31**	**-13.7%**
Utilities, cleaning & maintenance	(4.00)	(3.49)	-12.7%
F&B	(1.15)	(0.81)	-29.6%
Salaries & employee benefits	(7.15)	(5.44)	-23.9%
Gross profit	**11.23**	**10.57**	**-5.9%**
Administrative expenses	(3.28)	(2.87)	-12.4%
Other income and expenses	0.09	(1.25)	N/A
Operating profit	**3.74**	**4.36**	**16.6%**
Net result on disposal of investment properties	(0.06)	(0.07)	N/A
Impairment of work in progress/Recovery of PP&E	(0.31)	-	N/A
Revaluation of investment properties	3.07	(0.09)	N/A
Depreciation	(4.21)	(3.33)	-20.8%
Associates	(0.85)	0.02	N/A
Foreign exchange loss	(0.94)	0.16	N/A
EBIT	**5.68**	**2.98**	**-47.4%**
EBITDA	**8.04**	**7.71**	**-4.1%**
Interest income	0.05	0.01	-83.0%
Interest expenses	(2.18)	(1.54)	-29.3%
Profit before tax	**2.61**	**1.61**	**-38.4%**
Adjusted PBT	**1.46**	**1.61**	**10.4%**
Tax charge	(0.73)	(0.84)	15.0%
Profit after tax	**1.88**	**0.77**	**-59.1%**
Minority interest	0.07	0.14	101.4%
Attributable profit	**1.81**	**0.63**	**-65.3%**
Average number of shares outstanding (m)	20.70	20.81	0.5%
EPS (US$)	**0.088**	**0.030**	**-65.4%**
Adjusted EPS (US$)	**0.047**	**0.030**	**-36.2%**

Source: Company Data, Argento Capital

- Reported profits were hit by US$1.3m of litigation costs, relating to the ongoing shareholder dispute. However, in 2016 the income statement was largely unaffected by impairments or fair value gains.
- EPS, adjusted for one-offs and fair value impairments, fell 36% to US$0.03, due to a higher tax charge. Reported EPS fell 65% to US$0.03.
- This year the devaluation did not have a significant impact on the balance sheet, as the year-end rate was actually 2% stronger. PP&E was thus flat at US$79m, and total assets fell only slightly to US$92m.
- Net debt fell another 18% to US$10.3m, mainly as a result of debt repayment during the year, rather than the local currency weakness of 2015. As a result, the NAVPS was flat at US$3.57.

Earnings forecasts downgraded

- The recent relative strength and stability of both the oil price and the local currency has improved the operating outlook. We are still expecting slightly lower revenues than previously, with a fall of 2% YoY now pencilled in.
- We have revised down our EBITDA forecasts slightly to reflect a slower fall in administration costs, as the currency has stabilised. We still forecast EBITDA to be flat YoY, although that is 7% below our previous forecast.
- Nevertheless, we do still expect to see further margin improvements, as the largely local currency cost base continues to fall in dollar terms. Our EBITDA margin forecast is still 38%, unchanged from last year.
- We are not forecasting any revaluation gains in the income statement, but with lower interest expenses, following last year's debt repayment, especially the relatively more expensive bonds, we expect pre-tax profits to be up strongly, which is just 1% below our previous forecast.
- As a result, we are expecting a significant increase in both reported and adjusted EPS this year, although they are both 4% lower than the previous forecast, due to lower interest costs, following the lower debt at year end.
- In the current uncertain environment management has not yet proposed a dividend for 2016 and the ongoing shareholder dispute may influence when or if a dividend will be declared. However, we have forecast a total dividend payout of US$1m or US$0.048 per share in each year. We have also forecast an unchanged dividend for the next two years.

Forecast changes

(US$m)	2017E Previous	2017E Current	Change
Total revenues	20.7	20.2	-2%
EBITDA	8.3	7.7	-7%
PBT	2.9	2.9	-1%
EPS (USc)	9.8	9.4	-4%
Adj EPS (USc)	9.8	9.4	-4%
NAVPS (US$)	3.86	3.52	-9%

Source: Company Data, Argento Capital

Financial summary

Dec Year End	FY14	FY15	FY16	FY17E	FY18E
P&L (US$m)					
Total revenues	28.2	23.5	20.3	20.2	20.6
Gross profit	13.2	11.2	10.6	10.5	10.6
EBITDA	**9.2**	**8.0**	**7.7**	**7.7**	**7.8**
Depreciation	(5.3)	(4.2)	(3.3)	(3.4)	(3.4)
Operating profit	**3.9**	**3.8**	**4.4**	**4.3**	**4.4**
Revaluations/Impairments	(0.9)	2.8	(0.1)	-	-
Associates/Disposals	1.5	(0.9)	(0.0)	-	-
Net financial expense	(2.4)	(2.1)	(1.5)	(0.9)	(0.7)
Other / Foreign exchange loss	(0.1)	(0.9)	0.2	(0.5)	-
PBT	**2.0**	**2.6**	**1.6**	**2.9**	**3.7**
Adjusted PBT	**1.2**	**1.5**	**1.6**	**3.4**	**3.7**
Average shares outstanding (m)	20.6	20.7	20.8	20.9	20.9
Reported EPS (USc)	**6.8**	**8.8**	**3.0**	**9.6**	**12.4**
Adj EPS (USc)	**4.3**	**4.9**	**3.3**	**9.6**	**12.4**
Balance sheet (US$m)					
PP&E/Investment property	106.3	77.1	78.9	75.4	74.7
Other LT assets	8.5	6.0	4.7	4.7	4.7
Current assets	10.8	9.7	8.5	7.8	7.8
Long term borrowings	16.1	6.1	10.0	7.5	5.0
Other long term liabilities	7.0	8.6	8.1	7.9	7.8
Short term borrowings	4.2	8.3	2.5	2.7	2.5
Other current liabilities	3.7	2.0	3.3	2.6	2.3
Net assets	**94.6**	**68.0**	**68.2**	**67.1**	**69.6**
Closing net debt	**17.7**	**12.6**	**10.3**	**8.0**	**5.1**
Cashflow (US$m)					
Operating cash flow	9.3	5.7	8.0	7.1	7.5
Interest & tax	(2.4)	(1.7)	(1.3)	(1.7)	(1.7)
Capex / Acquisitions	(3.6)	(5.5)	(4.5)	(2.0)	(2.0)
Dividends	(0.4)	(1.2)	-	(1.0)	(1.0)
Equity	-	0.1	0.0	-	-
Net proceeds from borrowings	(2.5)	2.2	(2.0)	(2.3)	(2.7)
Change in cash	**0.4**	**(0.5)**	**0.3**	**0.1**	**0.1**
Closing cash	**2.5**	**1.8**	**2.2**	**2.3**	**2.4**
Growth rates (%)					
Revenues	(16.1)	(16.5)	(13.7)	(0.5)	2.0
EBITDA	(13.2)	(14.3)	(23.9)	4.9	3.0
Adj EPS	35.2	12.7	(32.1)	189.2	29.1
NAVPS	(12.4)	(25.6)	0.3	(1.4)	3.3
Operating ratios					
Gross margin	47.0%	47.7%	52.0%	51.9%	51.4%
EBITDA margin	32.5%	34.2%	31.8%	38.1%	38.0%
OP margin	13.9%	16.3%	15.3%	21.2%	21.5%
Adj EPS/DPS	74%	N/A	69%	200%	258%
Leverage					
Net debt/equity	19%	19%	15%	12%	7%
Pre-revaluation interest cover (x)	1.6	1.8	2.0	4.7	6.2
Net LTV (%)	15%	15%	12%	10%	6%

Source: Company data, Argento Capital Markets

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HOLD	Share price appreciation or depreciation of less than 10% in absolute terms over 12 months
SELL	Share price depreciation of 15% or more in absolute terms over 12 months
SPEC BUY	Share price appreciation of 15% or more in absolute terms over 12 months, but with an unusual level of risk relative to return

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