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Summary Analysis

TROPICAL BATTERY

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Tropical Battery Limited Summary Analysis

Analyst Insight

Currently, Tropical Battery's business is heavily driven by the sale of batteries, which represents 77% of total revenue. In recent quarters, the Company has made efforts to expand the reach of its business through its sales team which has resulted in the expansion of its customer base from 23,500 to over 25,000 in the past year, a significant increase, as suggested by the Company's revenue growth. Of the additional 1,500+ customers, 500 are Small and Medium-sized Enterprises (SMEs) that earn a significant share of their revenue by reselling Tropical Battery's products. The addition of these businesses supports the increased sale of inventory, solidifies the Company's market position, and broadens the reach of its products. To build on this, Tropical Battery is expanding its top-selling retail store. The Company has also employed more efficient inventory management systems that result in reduced lead time between warehouses, its retail stores, and resellers and decrease the likelihood of these outlets experiencing stockouts. This measure has driven increased operational efficiency.

The aforementioned highlights the first mode of driving growth and creating shareholder value, i.e., the expansion of the current business, as is, while managing efficiency. As a result of these initiatives, the Company reported growth of 46.78% in revenue, 151.13% in operating profit, and 197.55% in net profit. In the upcoming quarters, we believe these initiatives are likely to persist and should consequently, result in continued growth.

Looking beyond the near term, the Company has aligned itself with what we believe is an inevitable path as it relates to energy consumption, both locally and internationally, i.e., renewable energy and the use of electric vehicles. Specifically, Tropical Battery's current joint venture Company, ENRVATE, through its subsidiaries, seeks to be a player in the renewable energy industry. Granted, the industry remains in its infancy, but we believe this will change over time, and positioning early places Tropical Battery in a position to benefit.

A brief review of each subsidiary is presented below:

1. **Tropical Mobility** was created to serve the emerging electric vehicles market in Jamaica by selling electric vehicle batteries.
2. **Tropical Energy Limited** was created to provide renewable energy solutions for commercial customers. This would see Tropical Energy designing and implementing renewable energy solutions such as solar panels, wind turbines, etc. for these customers.
3. **Tropical Finance Limited** was created to finance the purchase of these renewable energy solutions and electric vehicles for users.

Certainly, these new ventures present clear risks, and we believe this, in particular, has been a driver for the structure of ENVRATE, i.e., ENRVATE's risk is spread between Tropical Battery and CAC 2000 since it is a joint venture. Outside of feasibility which we believe is a non-issue given the many tailwinds supporting renewable energy and electric vehicles in the long term, there is an obvious question of the margins that can be expected from these businesses since they are new. At present, the specific answer to this question is unknown. However, the important point here is how ENVRATE is accounted for on Tropical Battery's income statement. As a joint venture, Tropical Battery is represented under the equity method of accounting which means Tropical Battery benefits directly from ENRVATE generating profits, without adding the associated expenses to its income statement. We believe this places Tropical Battery in a very advantageous position and reduces risks to the Company's bottom line, profitability as measured by profit margins and the Company's return on equity.

Presently, the Company's initiatives to expand its sales reach have positively affected revenue and profit. We believe this is likely to continue throughout the year, solidifying our near-term positive expectations for the Company. Longer-term, the positioning of Tropical Battery into areas we believe have significant growth potential stand to benefit the company immensely. Given the aforementioned, we've issued an **OVERWEIGHT** recommendation on the Company's stock.

Income Statement

Revenue: For the quarter that ended December 2021, Tropical Battery has delivered robust growth relative to the same period for the prior year. For the quarter ended December 2021, the Company recorded revenues of $662.43 million which represents an increase of 46.78% or $210.95 million.

Profitability: For the quarter that ended December 2021, the company's operating profit margin was 12.37% compared to 7.23% for the same period in the prior year. This improved operational efficiency resulted in operating profit for the quarter amounting to $81.89 million which was an increase of $49.28 million or 151.13% YoY. Net Profit amounted to $56.65 million, which was an increase of 197.55% or $37.62 million YoY. The improved financial performance of Tropical Battery has been a derivative of increased revenues and improved operational efficiencies.

Valuation

Discounted Cash Flow and a **P/E valuation**. We firstly forecasted the company's income statement and arrived at a 1-year EPS of **$0.14.**

For our comparative analysis, we used companies that were listed on the junior market of the Jamaican Stock Exchange, whose businesses are centered primarily around distribution. Using these companies, we obtained an average P/E multiple of **22.21x.** This tracks very closely to the Company's trailing multiple of 21.99x. Using this multiple alongside the projected EPS of **$0.14** we obtained a fair value estimate of **$3.05.** We also note that even at a multiple of 18.00x, the Company would still trade at 18.31% above its present price and above our cost of equity as indicated below.

To complement the relative PE valuation, we then employed a Discount Cash Flow model of five years, the assumptions that guided this model included a cost of equity of 14% and a long-term growth rate of 6.46%. Using these assumptions, we arrived at a fair estimate value of **$2.95.**

Using a simple average of the two fair value estimates we arrived at a price target of **$3.00** which represents a potential upside of **40.85%.**

Given the Company's recent outsized growth, our positive outlook on its near-term and long-term potential, and the supporting valuation, we are recommending an **OVERWEIGHT** for Tropical Battery's stock.

Stock	TROPICAL
Close Price	J$2.13
Estimated Fair Value	J$3.00
Potential Upside	40.85%
Dividend Yield	0.78%
Total Return	41.63%
YTD Return	69.05%
Trailing P/E	21.99x
Forward P/E	15.53x
Recommendation	**Overweight**
March 16,2022	