

# **PROVEN**

Investments Limited

**Company Analysis**

**as at**

**December 31, 2012**

## Company Overview

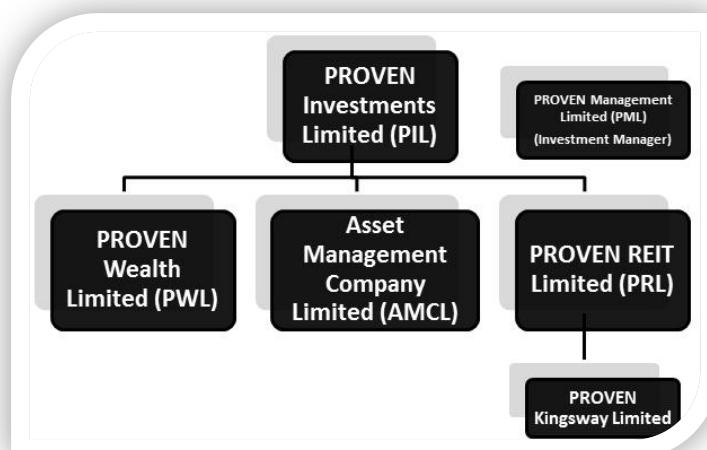
PROVEN Investments Limited<sup>1</sup> is a St. Lucian IBC<sup>2</sup>, incorporated on November 25, 2009 as a holding company. In February 2010, PIL successfully raised US\$20Mn through the private placement of 200Mn ordinary shares, and commenced operations in March 2010. In July 2010, PIL listed on the Jamaican Stock Exchange by way of introduction<sup>3</sup>. The Company subsequently expanded its capital base through a US\$9.6Mn rights issue in August of that year, followed by a J\$1Bn 5-year Preference Shares issue in December 2011.

VITAL STATISTICS AS AT DEC-12	
Stock	PROVEN
Recommendation	BUY
Industry	Finance
Current Stock Price	US\$0.10
Trailing EPS	US\$0.0132
Projected EPS (FY2014)	US\$0.0121
Trailing P/E	7.58X
Historical P/B	0.90X
Book Value	\$0.12
Target Price	\$0.11

## Company Structure

As an IBC, Proven is not regulated by the Financial Services Commission (FSC). PIL's business model was the first of its kind in Jamaica and is based primarily on holding tradable securities for investment purposes. PIL also actively seeks lucrative private equity investments which have led to the acquisition of a 100% stake in Guardian Asset Management Jamaica Limited

(later rebranded as PROVEN Wealth Limited (PWL)) and Asset Management Company Limited (AMCL). PWL, a securities dealer, is regulated by the FSC and engages in the management of client portfolios while AMCL, the owners of the 'Easy Own' brand, is a hire purchase financing company. PIL also has an 85% stake in Proven REIT Limited (PRL), a company established to facilitate real estate related investments. Proven Kingsway Limited is a wholly owned subsidiary of PRL, and is the vehicle through which the sole property owned by PIL was purchased in February 2012.



<sup>1</sup> Throughout this document, Proven Investments Limited will be referred to as Proven, PIL or the Company.

<sup>2</sup> IBC – International Business Company is “a corporation formed under the corporate legislation of a tax haven, which is not authorized to transact business in the country of incorporation but can have resident offices that manage global operations. IBCs enjoy benefits including low cost, little or no taxation, and minimal filing and reporting requirements.”

<sup>3</sup> Listing by way of Introduction allows a company to list its shares on the Jamaica Stock Exchange without issuing additional shares or raising additional funds.

## Investment Manager

PIL has no employees. Instead, Proven Management Limited (PML), a Jamaican incorporated company, is the investment manager for PIL which manages the Company's assets and businesses. PML holds the 10,000 units of Manager's

Preference Shares, collectively representing 50% of voting right in PIL. Management compensation is structured to incentivize strong performance for shareholders, with performance-based dividends only being paid if a predefined hurdle rate<sup>4</sup> is exceeded.

Investment Manager Compensation Structure		
<b>Management Fee</b>	2% per annum of PIL's average Net Asset Value	Paid Monthly
<b>Performance-based Dividends</b>	25% of Profits if, <i>ROE &gt; minimum (12 Month LIBOR plus 2%, 6%)</i>	Paid Quarterly

## Board of Directors

PIL has a five member Board, chaired by Mr. Hugh Hart. These professionals collectively bring expertise which spans a range of industries. This means the Board can provide strategic leadership over existing segments in which PIL operates and growth areas which it wishes to penetrate. PIL's objective of diversifying its operations outside of Jamaica is well supported by its Board composition, with directors bringing knowledge and experience from several Caribbean territories including Cayman, St. Lucia and Dominica. In adherence with good corporate governance principles, PIL has an independent Chairman, which should help to balance the interests of management and shareholders.

PIL's Board of Directors	Board Members				
	Hugh Hart	Yvor Nassief	Rhory McNamara	John A. Collins	Garfield Sinclair
Investment Banking		✓	✓		✓
Retail & Commerce		✓			
Real Estate		✓	✓		✓
Legal Services	✓		✓		
Trust Banking			✓	✓	
Tourism	✓				
Telecommunication					✓
Insurance		✓	✓		

Investment Manager - PML, has a four member Board chaired by Mr. Christopher Bicknell. Only one member holds dual roles as director of both PIL and PML which may help to minimize potential conflicts of interest. Led by Christopher Williams (CEO), one of PML's assets is its strong management team which has a wealth of experience in the financial sector.

<sup>4</sup> The hurdle rate specified in the management contract is set at the 12 Month LIBOR rate prevailing at the beginning of the year plus 2%, with a permanent ceiling of 6%

## Business Strategy

PIL's business model is similar to that of Berkshire Hathaway, a US holding company which manages a diverse number of businesses across the world. PIL targets viable high quality fixed income instruments and equity positions in companies which yields above average return on investments. The ability to provide attractive returns is supported by its tax efficient structure. Given the scope and risks associated with its investments, PIL targets the high net worth (HNW) market.

## Investment Strategy



Proven's investment strategy focuses primarily on three main revenue drivers: Carry-trade; Portfolio Positioning; and Private Equity Transactions.

### *Carry-trade*

A core strategy of Proven is the investment of funds raised through the issuance of short to medium term debt instruments in a diversified portfolio of securities. Its balance sheet is funded through issuance of secured structured notes and equity-linked notes, as well as margin arrangements with international brokers. This strategy, given the duration of liabilities, provides greater stability in PIL's fund raising relative to the repo-based model employed by most local securities dealers. Its portfolio of diversified, investment grade securities (approximately 60% of entire portfolio) stands as suitable collateral when sourcing funds from international lenders. The carry-trade strategy works well in the context of low borrowing costs and undervalued assets. The uncertainty in the market and decline in US interest rates has pushed the prices of investment grade bonds to at all-time highs<sup>5</sup>, thus limiting the profitability of this strategy. Subsidiary PWL also has local repurchase agreements, but has been actively reducing its exposure to this product.

---

<sup>5</sup> There is an inverse relationship between bond prices and yield.

### *Portfolio Positioning*

PIL currently generates most of its revenues from actively analyzing regional and global markets, in an attempt to identify attractive investment opportunities. This primarily includes fixed income securities as exposure to equities was reduced in light of the recent volatility in equity markets. Similar to the carry trade strategy, potential return from Portfolio Positioning may be affected by large exposure to investment grade bonds and the current low yields on these assets.



### *Private Equity*

PIL targets equity positions in companies which have strong business models with the potential for high levels of growth over the medium term. The success of this strategy will depend on the availability of market opportunities, management's ability to identify these opportunities and the availability of capital to execute as they arise.

## **Macroeconomic Overview**

### **Global Markets**

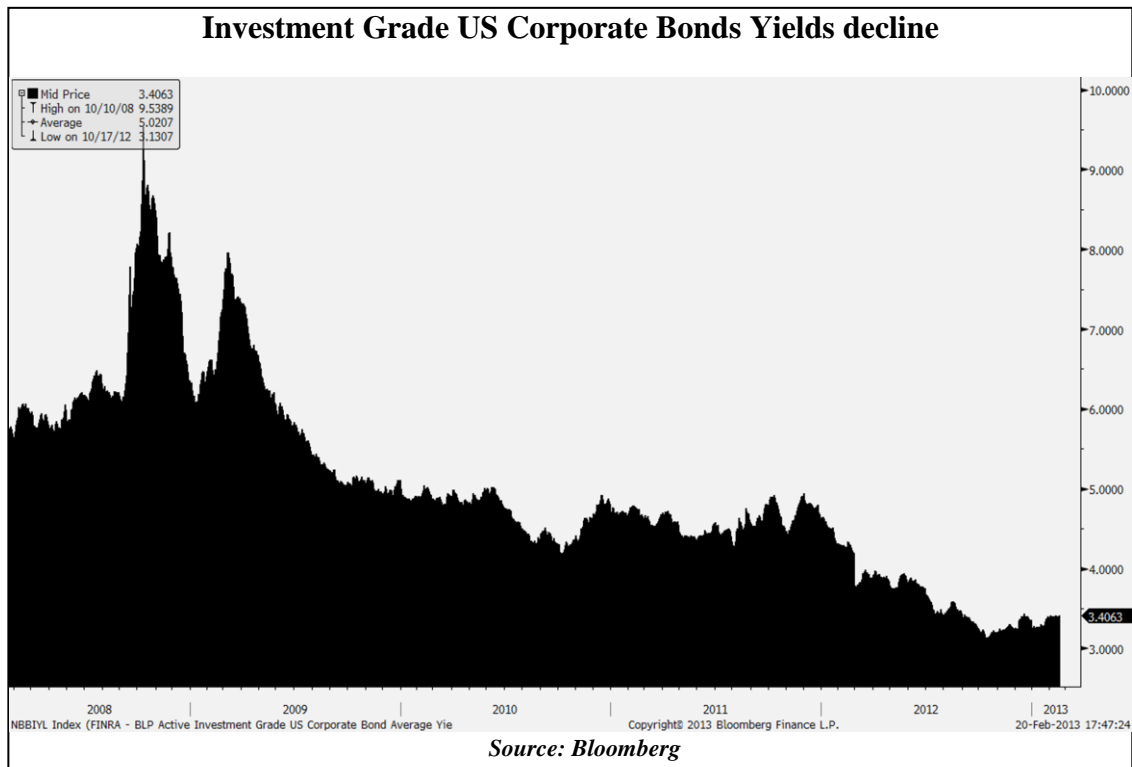
Proven's operations and its ability to increase returns to shareholders is being buffeted by current global and local economic conditions. This has been reflected in increased volatility in asset prices and restricted investment opportunities. In 2012, the global economy grew at a slower pace as risks faced by developed economies threatened the fragile recovery. The IMF estimated global economic growth at 3.2%, down from the 3.9% recorded in 2011. This reflected slower growth in advanced economies, particularly the euro area which is experiencing a recession.

Macroeconomic Indicators for Selected Global Economies										
	Real GDP		Consumer Price Index		Unemployment (%)		Current Account Balance (% of GDP)		Fiscal Balance (% of GDP)	
	2011	2012	2011	2012	2011	2012	2011	2012	2011	2012
<b>Advanced Economies:</b>	<b>1.6</b>	<b>1.4</b>	<b>2.7</b>	<b>1.9</b>	<b>7.9</b>	<b>7.9</b>	<b>-0.2</b>	<b>-0.4</b>	<b>-6.5</b>	<b>-5.8</b>
United States	1.7	2.1	3.1	2.1	9.0	8.2	-3.1	-3.3	-9.5	-8.2
Japan	-0.7	2.0	-0.3	0.0	4.5	4.5	2.0	2.2	-10.1	-9.9
<b>Euro Zone:</b>	<b>1.4</b>	<b>-0.3</b>	<b>2.7</b>	<b>2.0</b>	<b>10.1</b>	<b>10.9</b>	<b>-0.3</b>	<b>0.7</b>	<b>-4.1</b>	<b>-3.2</b>
United Kingdom	0.7	0.8	4.5	2.4	8.0	8.3	-1.9	-1.7	-8.6	-8.1
Germany	3.1	0.6	2.5	1.9	6.0	5.6	5.7	5.2	-1.0	-0.7
Spain	0.7	-1.8	3.1	1.9	21.6	24.2	-3.7	-2.1	-8.9	-7.0
Greece	-6.9	-4.7	4.1	-0.5	17.3	19.4	-9.7	-7.4	-9.2	-7.0
Portugal	-1.5	-3.3	3.6	3.2	12.7	14.4	-6.4	-4.2	-4.2	-4.5
Ireland	0.7	0.5	1.1	1.7	14.4	14.5	0.1	1.0	-13.1	-8.3

*Source: Government of the Republic of Trinidad and Tobago Review of the Economy 2012*

The Eurozone continues to struggle with sovereign debt challenges and austerity measures are expected to restrict growth even further. Bouts of instability in the region have been a significant contributor to volatility in global asset prices. This triggered a rise in demand for safer assets and lower yields on investment grade securities as risks heighten.

Growth in the US has helped to mitigate headwinds coming out of Europe, but risks to the pace of US growth have risen given increased taxes and the implementation of spending cuts. Monetary policy has been largely accommodative in a bid to drive growth and reduce unemployment levels. Both the bond and equity markets rebounded significantly from the lows seen at the height of the crisis.



## Emerging Markets & The Caribbean

Macroeconomic Indicators for Selected CARICOM Economies										
	Real GDP		Consumer Price Index		Unemployment (%)		Current Account Balance (% of GDP)		Fiscal Balance (% of GDP)	
	2010	2011	2010	2011	2010	2011	2010	2011	2010	2011
Barbados	0.2	0.6	5.8	9.5	10.8	11.2	-6.1	-8.5	-9.1	-4.6
Guyana	4.4	5.4	3.7	5.7	n/a	n/a	-9.5	-13.7	-3.0	-3.1
Jamaica	-1.5	1.3	12.6	7.5	12.4	12.8	-8.1	-9.9	-6.9	-5.8
<b>ECCU (All Countries):</b>	-2.4	-0.2	3.2	4.1	n/a	n/a	-20.0	-19.9	n/a	n/a
Antigua and Barbuda	-8.9	-0.5	2.9	3.9	n/a	n/a	-12.9	-10.8	-0.4	-1.7
Dominica	0.3	0.5	1.4	4.0	n/a	n/a	-21.1	-23.9	-3.5	-2.2
Grenada	-1.3	1.1	4.2	3.5	n/a	n/a	-25.5	-22.9	-3.1	-4.6
St. Kitts and Nevis	-2.7	-2.0	5.0	1.2	n/a	n/a	-20.6	-14.0	-7.8	2.0
St. Lucia	3.4	0.2	4.2	4.8	n/a	n/a	-15.2	-17.1	-4.8	-7.5
St. Vincent and the Grenadines	-1.8	-0.4	0.9	4.7	n/a	n/a	-31.6	-28.8	-5.8	-3.9

*Source: Government of the Republic of Trinidad and Tobago Review of the Economy 2012*

In light of the challenges in growing returns from investment grade securities, Proven may need to seek opportunities present in Emerging Markets and the Caribbean. Led by the BRICs,<sup>6</sup> growth in Emerging markets is expected to region 5.5% in 2013<sup>7</sup>, increasing the attractiveness of these assets. Particularly in the Caribbean which is still experiencing sluggish growth, asset in specific industries may be attractively priced. However, investment of this nature will require Proven to take on additional risks and may require the company to strengthen its capital base.

### Jamaica

The Jamaican economy contracted during the last calendar year, and is expected to contract further. The preconditions to the Extended Fund Facility with the IMF have resulted in higher taxes and the second debt restructuring (National Debt Exchange) in three years. These austerity measures along with the weak state of the economy will have adverse impact on the income of both securities dealers and investors. However, PIL's limited exposure to GOJ assets puts it at a slight advantage relative to other securities dealers..

<sup>6</sup> Brazil, Russia, India, China

<sup>7</sup> IMF forecast

## Industry Analysis

Proven operates in a niche market, raising capital from local and international investors for investment in various asset classes. Through its subsidiary, PIL has extended its business lines outside the financial industry, already occupying space in

Subsidiaries	Country of Incorporation	Nature of Business
Proven Wealth Limited	Jamaica	Funds Management, investment advisory services, money market and equity trading
Proven Reit Limited and its wholly owned subsidiary	St. Lucia	Real estate investment
Proven Kingsway Limited	St. Lucia	Real estate investment
Asset Management Company Limited	Jamaica	Hire purchase financing

the real estate market with further plans to target healthcare, tourism and security industries. PIL's major competitors are Sterling Investments Limited (SIL) and BCW Capital Limited (BCWCL)<sup>8</sup>, both recently incorporated entities. Though Proven may have a larger share of the market given first-mover advantage, these entities have aggressively increased their market presence which will erode Proven's market share.

Subsidiary, PWL, actively competes with local securities dealers in the HNW space. The strategic move by PWL to divert from its repo-based business model is shared by many of its peers, given the regulatory thrust and the drive to move revenue generation off-balance sheet. The impact of the NDX has further reduced investors' confidence in GOJ and will see dealers diversifying their product offerings, ultimately threatening PIL's niche. These larger players, being more highly capitalized and having access to a wider branch network, are expected to make inroads into Proven's market.

PREIT has only one property in its portfolio. Locally, there has been improved demand for properties helped by falling interest rates which have made mortgages more affordable. Within the U.S., the properties market remains depressed, providing opportunities for Proven to acquire discounted properties outside the Caribbean region. Nonetheless, PREIT's ability to acquire properties and close private equity deals will be dependent on the liquidity in the capital markets.

AMCL has moderate market presence, with services being offered through 7 retailers (22 stores) including Bashco and MegaMart. Proven's CEO noted that hire purchase sales at participating retailers have been low, creating a need to expand product reach. Expansions in MegaMart network should allow for greater market presence. However, operating in a market already dominated by retail giants 'Singer' and 'COURTS', which have large consumer databases and a wider market presence (23 and 29 stores respectively), AMCL will face significant challenges growing market share.

<sup>8</sup> BCWCL and SIL are PIL's main competitors based solely on the company's business model.



## Porter's Five Forces Model

### Threat of New Entrants *High*

- There are no regulatory barriers to entry for companies that wish to employ a business model similar to that of Proven's. Further, the company's business model and products are fairly easily replicated, with the start-up cost and requirements for an IBC being minimal. Over the last few months, there has been two new entrants to this market, which will ultimately increase competition in this space. That said, the strong brand equity of PIL's principals puts it at an advantage relative to its competitors.

### Threat of Substitute Products *High*

- Despite having the advantage of accessibility, PIL generally targets HNW investors who also have access to similar and more diversified investment vehicles overseas. These investors also form part of the core clientele of traditional investment firms. HNW clients generally tend to spread their wealth among several financial institutions and post the NDX, the increase in aversion to GOJ assets may create an opportunity for PIL. That said, traditional securities dealers are seeking to diversify product offerings to reduce exposure to GOJ
- BCWCL and SIL, have also been aggressively targetting the HNW clientele which increases the availability of substitutes.

**Bargaining Power  
of Suppliers**

*Medium*

- This can be assessed by looking at the suppliers of assets and suppliers of capital. The weak state of global economies has decreased the bargaining power of certain asset owners, leading to some assets being sold at discounts to fair value.
- PIL's ability to fund private equity and other acquisitions is constrained by its ability to raise capital. Given the intense competition in the current space, suppliers of capital have a myriad of options which increases their bargaining power.

**Bargaining Power  
of Customers**

*High*

- Given that PIL appeals to HNW clients, quality service delivery is key to its ability to maintain and grow its client base. That said, the myriad of investment options available to these clients and low to no switching costs, increases the bargaining power of customers.

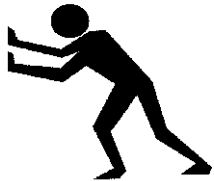
**Competitive  
Rivalry within  
Industry**

*Medium*

- PIL's has sought to differentiate from traditional securities dealers through its business model. However, given that the company operates in the HNW space, the pool of potential clients are limited given Jamaica's weak economy and contracting wealth. PIL will face competition from firms with larger capital bases and stronger brand equity.
- New players which have similar business model to Proven will also intensify the rivalry within the industry.

## SWOT Analysis

### S trengths



- ⇒ Cost and Tax efficient infrastructure: Through the establishment of a fixed management contract, PIL is able to better estimate and monitor cost. Also, PIL and its subsidiaries incorporated in St. Lucia pay corporate taxes of 1% in St. Lucia and none in Jamaica.
- ⇒ Unique Business Model: PIL primarily focuses on international, diversified investment opportunities and is first of three companies locally to employ such a business model. As such, PIL does not operate mainly in the space of larger securities dealers where competition is fairly intense. As first movers and given PIL's performance since inception, the company has garnered loyalty and trust from customers. This business model also allows for greater flexibility and allows the company to take advantage of global investment opportunities quicker than traditional securities dealers.
- ⇒ Strong Management Team: PML is led by a highly competent management team who share a wealth of experience from leading financial institutions in the industry.

⇒ With a fairly small capital base, PIL's ability to grow its business and take on additional risk is limited.

⇒ PIL is a fairly young company and as such, has a limited track record of performance and also weak brand equity both locally and internationally.



### W eaknesses

I  
n  
t  
e  
r  
n  
a  
l

# O

pportunities



- ⇒ The rebound in the economies of emerging markets may lead to continued increases in bond prices, providing an avenue through which PIL can boost revenues from its ‘portfolio positioning’ strategy.
- ⇒ Internationally, real estate markets are still depressed and as such, provide a great investment opportunity for PIL’s subsidiary PROVEN REIT.
- ⇒ With the recent NDX, investors have become less confident in the GOJ credit and as such, will embrace further diversification and new non-GOJ investment opportunities. PIL can leverage this to raise investment capital.
- ⇒ PIL’s private equity investments provides an avenue through which profitability can be improved through acquisitions.

- ⇒ The uncertainty brought on by the recession within the Eurozone could threaten the performance of emerging market debt and other risky asset classes, thereby adversely impacting revenues.
- ⇒ PIL reports profits in USD and as such, is exposed to the impact of adverse movements in exchange rates.
- ⇒ Weak global economies limit PIL’s ability to raise capital as investor’s wealth has been negatively impacted.
- ⇒ Potential changes in the political or regulatory environment in country of incorporation.
- ⇒ Investors’ demand for ‘safe’ investments has driven up the prices of investment grade securities and as such, threatens the returns on Proven’s future investments.



# T

hreats

E  
x  
t  
e  
r  
n  
a  
l

## Financial Performance

### Historical Performance

#### Financial Health:

PIL has performed creditably over the last two years. In 2011, its first full year of operation, earnings totaled US\$6.6Mn (EPS: US\$0.02) and included a US\$5.0Mn gain from the purchase of GAM. ROE of 19.28% was on par with average of larger players.<sup>9</sup> Net profit however dipped 50.1% in 2012 to US\$3.3Mn.

Similar to local securities dealers, Net Interest Income (NII) accounts for a significant portion of PIL's net revenues. However, this is mainly from the investment of funds raised through private placements and a preference share offer<sup>10</sup> at a positive spread. Despite the notable difference in strategies, PIL's NII declined by 1.2% to US\$3.10Mn in 2012, consistent with the market. Consequently, Net Interest Margin (NIM) declined to 2.43% (FY2011: 2.68%). There's some concern for PIL in a declining interest rate environment as the duration of its existing liabilities cannot quickly adjust the cost of existing funds.<sup>11</sup> On a positive note though, PIL's has only 7% of its assets invested in GOJ securities and therefore will not be significantly impacted by the NDX. Further, the low interest rate environment may allow PIL to raise new capital at lower cost.

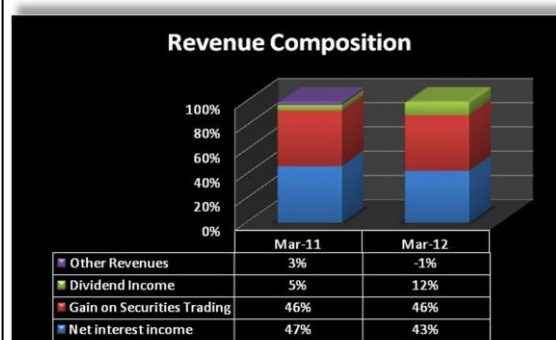
Trading gains increased 7.8% to US\$3.31Mn in 2012. Growth could be tepid in the coming year given that most of the portfolio is invested in

<sup>9</sup> Gains from GAM have been included as part of core earnings since Proven has identified private equity transactions as part of its core business strategy.

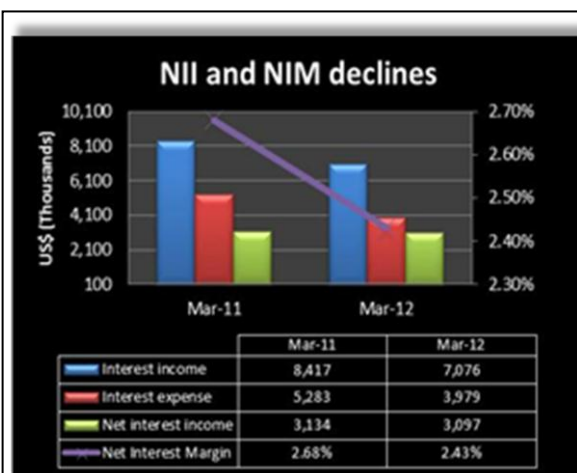
<sup>10</sup> This is unlike other securities dealers that raise funding primarily through repurchase agreements

<sup>11</sup> The duration on existing liabilities are medium to long term which limits speedy re-pricing

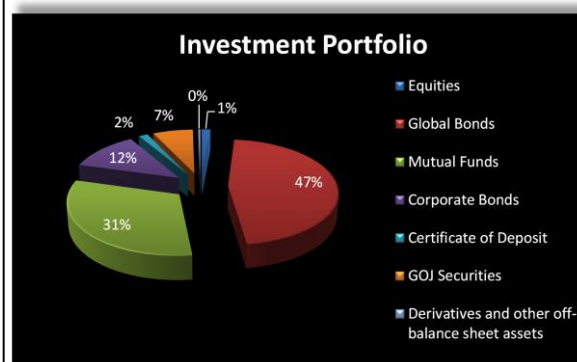
#### Net Interest Income (NII) and trading gains are the major revenue drivers



*Excludes gain/(loss) on property valuation and subsidiary purchase*



#### Only 7% of Investment Portfolio in GOJ Securities



investment grade credits which are currently priced at historic highs.

With a cost to income (CIR) ratio of 52%, PIL's cost structure is largely in-line with the 50% international benchmark. Operating expenses declined 18.3% to US\$18.3Mn given a decline in amounts paid in preference share dividend. Administrative Costs, which account for the majority of expenses, rose 8.8%, just above point-to-point inflation of 8.02%.

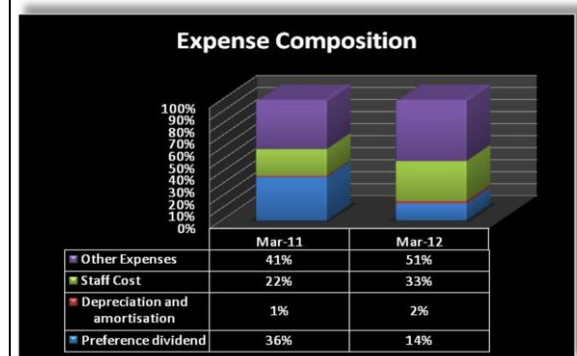
### Capitalisation:

PIL's capital base stood at US\$33.1Mn in 2012, down 3.3% relative to the prior year as a result of fair value losses on available-for-sale securities. Capital to assets ratio, however, held firm at 24%, suggesting an unchanged funding structure. Its asset base declined marginally reflecting reduced cash levels. Through its subsidiary, PWL, there has been a gradual reduction in repo liabilities.

### Liquidity and Financial Flexibility:

PIL has negative operating cash flow<sup>12</sup> which is typical for a company in the early stage of its life cycle. However, dividend obligations will increase cash requirements. A more prudent decision might have been to suspend dividend payments on ordinary shares until the company has adequately built up retained earnings and its cash reserves.

### Preference Share Dividends declines while other expenses rise

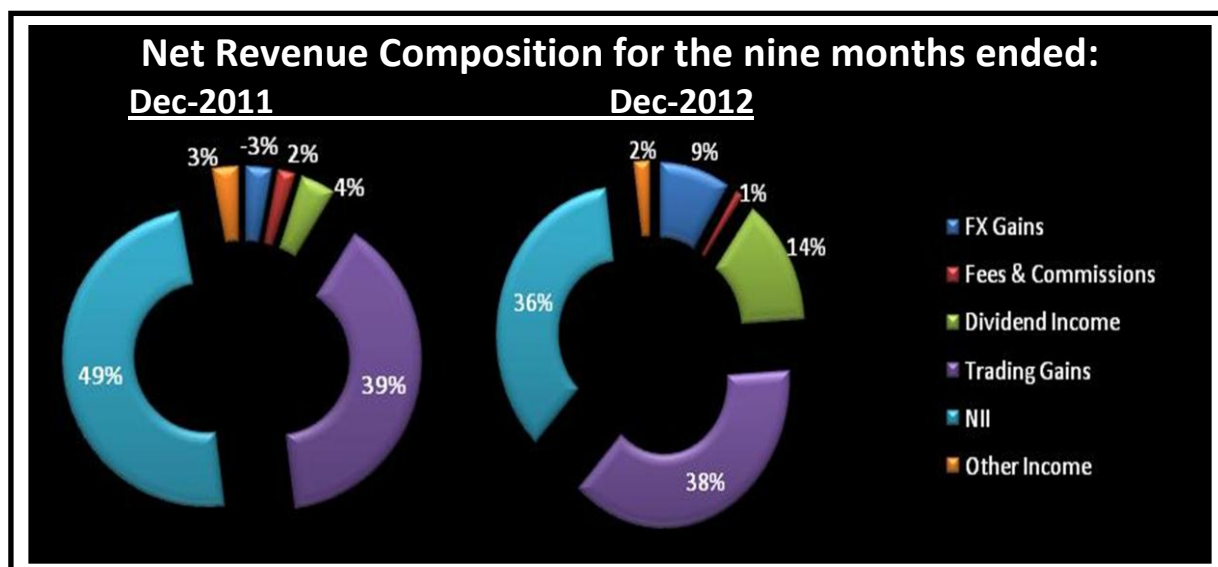


### Key Balance Sheet Movements

US\$'000	Mar-11	Mar-12
Resale Agreements	9,314	882
Margin Loans	-	13,792
<b>Total Assets</b>	<b>141,106</b>	<b>139,005</b>
Repurchase Agreements	66,454	35,344
Notes Payable	33,571	52,981
Preference Shares	1	11,240
<b>Total Liabilities</b>	<b>106,859</b>	<b>105,785</b>
<b>Total Shareholders' Equity</b>	<b>34,247</b>	<b>33,220</b>

<sup>12</sup> (-US\$25.9Mn in 2012)

## YTD 2012/13 Performance



For April to December 2012, PROVEN's earnings increased 23.7% to US\$3.13M, driven by growth in trading gains (+18.7%). Operating expenses grew by 24.7% due to higher preference share dividend. The inclusion of expenses related to AMCL also contributed to higher operating costs. However, CIR improved (moving from 50.7% to 49.9%).

*Carry Trade:* NII coupled with dividend income yielded a 12.6% year-over-year increase to US\$3.48M.

*Portfolio Positioning:* Trading gains rose 19% to US\$2.68M relative to the prior year.

*Private Equity:* All subsidiaries performed well for the nine month period, with PWL reporting earnings of US\$579K while AMCL and PROVEN REIT generated net revenues of US\$366K and US\$21.56K, respectively. AMCL grew its loan portfolio by 42% albeit from a small base. PROVEN REIT is also positioning to take advantage of new lucrative real estate opportunities.

YTD 2011/12 (US\$'000)	Dec-11	Dec-12	Change
Net interest income	2,835	2,535	↑
Gain on Securities Trading	2,257	2,678	↑
Dividend Income	253	941	↑
Foreign Exchange Gains/(Losses)	(157)	643	↑
Total Operating Expenses	2,785	3,473	↑
Net Profit for the Year	2,530	3,130	↑
Efficiency Ratio	50.71%	49.88%	↓
Net Profit Margin	46.07%	44.96%	↓

PIL's asset base grew 9% to US\$149.8M reflecting a 19.8% increase in available-for-sale assets, which was mainly funded through the issuance of Notes during the review period. Consequently, total liabilities grew 7.4% to US\$114.2M. The improvement in asset prices has led to an improvement in revaluation reserves, and ultimately, an increase in Shareholders' equity. Shareholder's Equity climbed 4.9% to US\$35.4M (BVPS: US\$0.12).

## Technical Analysis

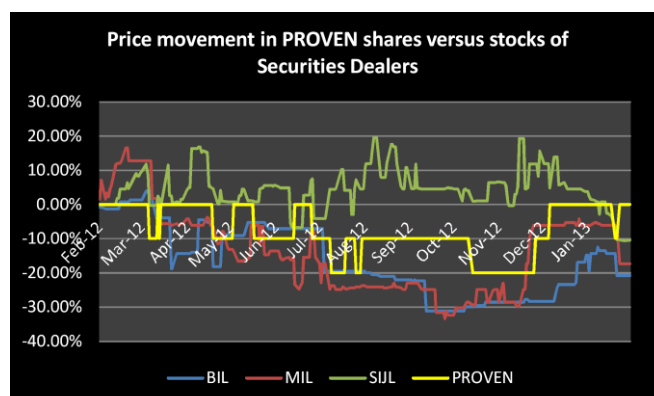
PROVEN is the only stock included on the JSE's USD index. The stock was listed at US\$0.112. Despite some volatility, PROVEN has shown a tendency to revert to its list price. Over the last year, the price has been flat but has outperformed the shares of most securities dealers which declined. The impact of the asset tax and other fiscal measures would have been far less on PIL's business relative to other dealers and this is likely reflected in its relative price performance.

The top 20 shareholders own just 27% of the total shares outstanding, suggesting there is no concentrated ownership and a large free float. Despite this, trading volumes are fairly low, averaging 46K daily during the last year. The stock has traded on 85 out of a possible 251 days which further indicates low liquidity.

Higher dividend taxes<sup>13</sup> however augur well for increased interest in the stock given that PROVEN is incorporated in a tax-free jurisdiction. As such, the relative attractiveness of the stock should increase as returns from dividends are tax free.

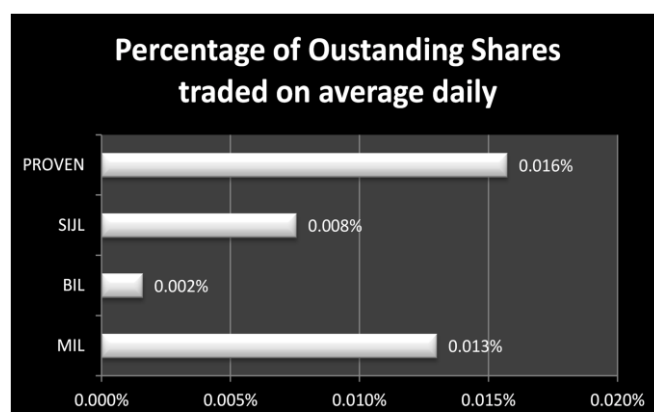
### Recent Statistics as at February 21, 2013

Stock Code	PROVEN
Shares Outstanding	294,951,884
Last Traded Price	\$0.1000
Market Capitalisation	\$29,495,188.40
Financial Year End	31-Mar
DPS 2012/13	\$0.0089
52-Week High/Low	\$0.10/\$0.80
52-Week Volume Range	0 units to 3,700,000 units
Closing Bid/Ask	\$0.09/\$0.10
Year-to-date % change	0.00%
% change over last 12 months	0.00%



Source: Jamaica Stock Exchange

**PROVEN outperforms most securities dealers' stocks**



Source: Jamaica Stock Exchange

**Moderate Liquidity relative to peers**

<sup>13</sup> The Government of Jamaica has proposed an increase in dividend taxes from 5% to 15% which takes effect on April 1, 2013.



## Earnings Projections

- ⌘ Interest income is expected to grow at a slower pace to US\$7.63M in FY2012/13. Continued reduction in the interest expense of PWL should help in growing NII to US\$3.16M. FY2013/14 performance is expected to be relative flat as the company is faced with greater pressures from lower asset yields and challenges in the target economies.
- ⌘ Using year-to-date performance as a gauge, inflows from other revenue sources are expected to grow a further 28.8%, driven by FX gains and dividend income. The outlook for these revenue sources during the FY2013/14 is less optimistic with trading gains and FX gains anticipated to fall.
- ⌘ Despite an increase in marketing related expense related to current and future private equity deals, operating expenses are expected to fall marginally in FY2013/14 as lower performance bonuses are paid to the management team.
- ⌘ The aggregate impact of these factors should result in net profit increasing to US\$3.8M by the end of FY 2012/13 (EPS: US\$1.29), but is expected to decline to US\$3.6M (EPS: US\$ 1.21) in FY 2013/2014.

## Valuation Methods

### Income Approach

PIL has an aggressive dividend policy through which a minimum of 50% of profits will be paid out annually. Using the Dividend Discount Model, dividends were discounted at 15% required return<sup>14</sup>. This yielded an intrinsic value of US\$0.11.

Year	1	2	3	4	5	TV
EPS (US\$)	0.0121	0.0134	0.0148	0.0162	0.0177	
Dividends	0.0061	0.0067	0.0074	0.0081	0.0088	0.0018
Discounted Cashflows	0.0053	0.0051	0.0049	0.0046	0.0044	0.0879
Value per Share (US\$)	<b>0.11</b>					
Premium to current price	<b>10%</b>					

### Book Value Approach

PIL, similar to other local securities dealers, trades at a discount to its book value due to a low ROE relative to its cost of equity. Over the last 6 quarters, PIL has reported an average P/B of 0.90X. Applying this multiple to its projected book value per share of \$0.127 gives an estimated forward price of \$0.11.

<sup>14</sup> Derived using the Capital Asset Pricing Model (CAPM) with risk free rate of 6%, beta of 1% and market risk premium of 9% (See appendix for details)

## Recommendation

At its current market price of US\$0.10, the stock is slightly undervalued as both models yield an estimated fair value of US\$0.11, representing a 10% premium to the current price. The stock provides an attractive dividend yield which is estimated at 5.50% in the next year. Using the 5 year average historical depreciation as a guide, foreign exchange gains could be close to 6%. With a projected total return of 21.50% which far exceeds the required return of 15%, a BUY recommendation is being placed on PROVEN. The table below shows the profile of investors for which this stock is best suited:

	Conservative	Moderate	Aggressive	Rationale
Risk Profile		✓	✓	Given the business model employed which assumes relatively greater risks to capital than traditional investment firms, Proven is not recommended for conservative investors
	Short	Medium	Long	Rationale
Investment Horizon		✓	✓	The company is in its growth stage and needs time to build out its investment strategy. As such, full benefits from successful execution may not be realised in the short term
	Low	Medium	High	Rationale
Reliance on Frequent Income Stream			✓	Proven has a very attractive dividend policy with a projected yield of 5.50%. Dividends are paid tax free which is appealing given the proposed increase in dividend tax. Dividends are paid in US\$ and investors could benefit from potential foreign exchange gains.

## **Outlook**

Proven has created a niche in a relatively untapped segment of the financial sector and is likely to benefit from first mover advantage even as other firms adopt a similar business model. One of its major strength is the management team which brings a wide array of knowledge and experience. That said, the company will need to intensify its marketing efforts in order to remain in the forefront of investor's minds. This will be critical in executing its strategy as strong brand image is important and more so in times of uncertainty.

The current environment should provide an opportunity for the company to build out its private equity strategy as the weak economic environment is likely to present more opportunities for undervalued assets. However, gains from this strategy are not always immediate and depend on management's ability to successfully identify attractive deals.

There are some concerns relating to the execution of its carry trade and portfolio positioning strategies in light of heavy exposure of investment grade securities. Given that these assets are at all-time highs, the yields are low and as such income from these strategies should remain subdued. Consequently, there may be greater focus on private equity strategy to boost growth. Diversification will become more crucial as the company should seek to make acquisitions across various industries, geographic locations and asset classes. Assets such as equities and real estate also provide lucrative investment opportunities given current market trends.

## References

- Bloomberg Finance L.P. (2013). NBBIYL Index (FINRA - BLP Active Investment Grade US Corporate Bond Average Yie.
- Damodaran, A. (2013, January). *Country Default Spreads and Risk Premiums*. Retrieved from [http://pages.stern.nyu.edu/~adamodar/New\\_Home\\_Page/datafile/ctryprem.htm](http://pages.stern.nyu.edu/~adamodar/New_Home_Page/datafile/ctryprem.htm)
- Government of the Republic of Trinidad & Tobago. (2012). *Review of the economy 2012: Stimulating growth, Generating Prosperity*. Retrieved 03 Saturday, 2013, from <http://www.finance.gov.tt/content/Review-of-the-Economy-2012.pdf>
- International Monetary Fund. (2013). *Gradual Upturn in Global Growth During 2013*. Retrieved 03 2013, from <http://www.imf.org/external/pubs/ft/weo/2013/update/01/pdf/0113.pdf>
- PROVEN Investments Limited. (2012). *Annual Report 2012*.
- PROVEN Investments Limited. (2011-2012). *Quarterly Report September 2011- December 2012*.
- Services, F. C. (2012). First Citizens Research & Analytics. *Caribbean Investment iQ*, First Citizens Investment Services Limited.
- Thorpe,C. (2012). *Provens US\$1M shopping spree*. Retrieved 03 2013, from [http://m.jamaicaobserver.com/mobile/business/Proven-s-US-1m-shopping-sprees\\_11621342](http://m.jamaicaobserver.com/mobile/business/Proven-s-US-1m-shopping-sprees_11621342)

## Appendix

<i>Proven Investments Limited</i>	<b>Actual</b>		<b>Projected</b>	
<b><i>Income Statement (US'000)</i></b>	<b>2011</b>	<b>2012</b>	<b>2013</b>	<b>2014</b>
Interest Income	8,417	7,076	7,630	7,265
Interest Expense	5,283	3,979	4,467	4,108
<b>Net interest income</b>	<b>3,134</b>	<b>3,097</b>	<b>3,163</b>	<b>3,157</b>
<b>Other operating revenue</b>				
Dividends	308	899	1,254	1,443
Fees and commissions	173	140	72	88
Gain on Securities Trading	3,070	3,310	3,328	3,079
Net foreign exchange gains	11	-417	943	179
Other income	213	-2	105	121
Gain/(Loss) on Property Valuation	0	179	0	0
Gain/(Loss) on purchase of subsidiary	5,009	0	0	350
	<b>8,784</b>	<b>4,109</b>	<b>5,703</b>	<b>5,259</b>
<b>Net interest income and other operating revenue</b>	<b>11,918</b>	<b>7,206</b>	<b>8,866</b>	<b>8,416</b>
<b>Expenses</b>				
Administrative and General Expenses	2,908	3,165	3,588	3,822
Depreciation and amortisation	47	76	92	101
Preference share dividend	1,668	538	950	628
	<b>4,623</b>	<b>3,779</b>	<b>4,630</b>	<b>4,551</b>
Profit before taxation	7,295	3,427	4,235	3,865
Taxation	693	133	436	293
<b>Net Profit after tax</b>	<b>6,602</b>	<b>3,294</b>	<b>3,800</b>	<b>3,572</b>
<b>EPS (US\$)</b>	<b>0.022</b>	<b>0.011</b>	<b>0.013</b>	<b>0.012</b>
<b>Ratios</b>				
NPM	55.40%	45.71%	42.86%	42.45%
Efficiency Ratio	38.79%	52.44%	52.23%	54.08%
Growth in Revenues	N/A	-39.54%	23.03%	-5.07%
Growth in Profits	N/A	-50.11%	15.35%	-5.98%

### Required Return Calculation

<b>Required Return Calculation</b>	
<b>Variable</b>	<b>Rate</b>
<i>Risk-free rate (Local)</i>	9%
<i>Risk-free rate (International)</i>	3%
<b>Average Risk-free rate</b>	<b>6%</b>
<i>Market Risk Premium (Local)</i>	14%
<i>Market Risk Premium (International)</i>	4%
<b>Average Market Risk Premium</b>	<b>9%</b>
<b>Beta</b>	<b>1%</b>
<b>Required Return</b>	<b>15%</b>