Edison investment research

3 April 2012

Dolphin Capital Investors

Year End	Revenue (€m)	PBT* (€m)	EPS* (c)	DPS (c)	NAV/ share (p)	Disc. to NAV (%)
12/09	90.8	(93.0)	(13.2)	0.0	193	88
12/10	69.9	(53.5)	(7.6)	0.0	175	87
12/11	32.8	(36.1)	(3.9)	0.0	139	83

Note: *PBT and EPS are normalised, excluding non-cash adjustments to investment and trading properties, intangible amortisation and exceptional items.

Investment summary: Stabilising outlook

The case for investment at, effectively, an option valuation hinges upon views of the outlook for the group's key markets in FY12. Portfolio maturity and recent investment initiatives put self-sustaining finances within reach. Last year was affected by market turmoil, but the outlook is improved by the progress of advanced schemes and a simplified corporate structure; a reduced stake in its Aristo subsidiary reduces annual running costs, improves the portfolio's geographical balance and could ease the path to a more stable cost/income outlook. The latter assumes the return of buyers, JV partners and other investors. This may be a pivotal year.

First high-end resort, Amanzoe, to open this summer

Construction of DCI's first high-end resort, Amanzoe in Greece, progressed well in FY11 and is due to open this summer. This is an important catalyst for formal sales activity, both for the Aman and Seafront villas and the first phase of The Porto Heli Collection, the first villa-integrated Aman resort in Europe. Work at the Venus Rock and Pearl Island schemes are both also well ahead, while FY11 saw significant planning and development milestones achieved within the remaining portfolio.

FY11 results: A fourth tough year successfully negotiated

DCI successfully navigated another difficult year in FY11, for which management deserves some credit and we believe would, if required, be able to apply similar strategies until the market eases. A lack of visibility on project sales or operational income makes it difficult to provide useful forecasts at this stage, but that could certainly change this year as advanced schemes start to generate cash flows. By restructuring its holding in Aristo, DCI has cut group debt to assets from 27% to 13%, expenses by €4.2m pa and improved the portfolio's geographical balance.

Valuation: 83% NAV discount is an option on strategy

Significant sensitivities remain, but the outlook for sales of completed units should be supported by evidence of resilient demand and prices at the ultra high-end of luxury leisure and residential property. There is real optionality in the shares at the current price. Year-end NAV/share was 139p or 125p/share adjusted for deferred tax.

Price	23p
Market Cap	£101m*

Share price graph

Share details

Code	DCI
Listing	AIM
Sector	Real Estate
Shares in issue	438m*

** Adjusted for Aristo exchange.*

Price

52 week	High	Low
	40p	18p

Balance Sheet as at 31 March 2012

Debt/Equity (%)	13*
NAV per share (p)	125**
Borrowings (€m)	125

***Excluding deferred tax.*

Business

Dolphin Capital Investors (DCI) is a leading developer of high-end integrated leisure and residential property developments in the eastern Mediterranean and the Americas (Panama and the Dominican Republic). The group owns a 48.5% stake in Aristo developments, the largest developer of leisure property in Greece.

Valuation

	2009	2010	2011
P/E relative	N/A	N/A	N/A
P/CF	N/A	N/A	N/A
EV/Sales	N/A	N/A	N/A
ROE	N/A	N/A	N/A

Portfolio by geography (2011)

Europe	Americas
84%	16%

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Investment summary: FY11 results

To recap, DCI has a portfolio of 10 major leisure-integrated residential resort projects, which it plans to develop over the next 12 years, subject to market conditions. The value of these schemes should grow as they achieve planning consents, and progress through design and construction phases. DCI also expects to receive dividends from its 49.8% stake in Aristo Developers, the largest developer and private land owner in Cyprus.

FY11: Successful navigation of another tough year

FY11 was a fourth consecutive challenging year, but despite lower sales and asset valuations the four 'advanced projects' were steered towards a point where they could progressively attract the interest of luxury home buyers, joint-venture partners and other investors in residential assets.

Exhibit 1: Underlying revenues and profits

	FY10	FY11
Sale of trading and investment properties	59,180	28,486
Income from operation of golf courses	1,101	1,029
Income from construction contracts	5,919	172
Other profits	3,712	3,095
Cost of sales	(60,018)	(27,859)
Total	9,894	4,923

Source: DCI FY11 results

Underlying revenues and profits (ie excluding valuation movements and other impairments) is set out in the above exhibit and reflects a more difficult year affected by the economic backdrop. The portfolio has, however, progressed during the year and a number of schemes approach a point where they could provide useful confirmation of levels of demand in the key high-end market.

Three out of the four advanced projects are on track to complete the first phases of their development. The plans for these advanced projects comprise 12 luxury hotels, four 18-hole championship golf courses and one marina. The first phases include:

- The first Aman residential resort in Europe (Amanzoe), Aman golf-integrated resort worldwide (Playa Grande) and Nikki Beach resort in the eastern Mediterranean (The Nikki at Porto Heli), all in Greece.
- Two golf courses in Venus Rock Golf Resort (Cyprus) and one in Playa Grande Club & Reserve (Panama).
- A marina at Pearl Island (Dominican Republic), which will be expanded as the development progresses.

Scheme due May 2012 provides a template for DCI offer worldwide

The Amanzoe resort in Greece is due for completion in May and would provide an important step toward a more stable, self-sustaining financial performance. DCI expects Amanzoe – the commercial name for the Aman hotel at Porto Heli – to be operational this summer, together with the Aman Beach Club, a private club open only to members, hotel guests and villa owners. It has appointed the general manager, financial controller and HR manager of the hotel and is currently recruiting and training hotel personnel. The opening is expected to drive sales momentum for the

Aman and Seafront Villas, shifting focus to the entire Porto Heli area. The first two Aman Villas will be delivered this summer; construction of another four already sold is underway. DCI has so far:

- Drawn down €31.2m of a €33m construction loan, €5.4m of the €8m VAT bridge facility.
- Secured final approval (June 2011) for €7.8m of subsidies for hotel construction and the first 50%, ie €3.9m tranche in March 2012.
- Received €5.4m from the sale of shares in Amanzoe to Archimedia, which holds a 14.29% stake in the scheme and an option to exchange its project share participation for three Aman Villas.

A further €9.1m is receivable in line with construction milestones and DCI received deposits for two additional villas. This illustrates the growing momentum at this scheme. Elsewhere, The Nikki Beach Hotel, the next component of the Porto Heli collection, has received approval for €4.25m of subsidies. DCI signed a term sheet in May 2011 with a major European bank for a €10.5m long-term asset-backed construction facility. Construction will only begin with finance in place, additional equity funds or when a JV partner is on board and DCI is in advanced discussions.

Aristo Developers: Slower FY11, well placed for FY12

Aristo (a 100% subsidiary in FY11) had a slower year, with €27.4m of gross retail sales in FY11, 29% down on 2010 in a difficult market. That was 137 sales (homes and lots), 28% below 2010, but demand from Russian buyers grew relative to other nationalities. Total FY11 sales were €66.9m, including its 50% shareholding stake in the Kings Avenue Mall project in central Paphos at a €39.5m enterprise value, ie €15m in cash and the assumption of €24.5m of debt and other liabilities. The net consideration was a 13% premium to project NAV, 31% to the allocated investment cost.

Despite lower sales, Aristo restructured its key financial obligations in FY11 and launched new discount schemes to attract buyers for existing inventory. It only released a small number of projects in 2011, but expects to increase that number this year, including selective construction of show villas in key projects. It hired an experienced sales executive in November 2011 to revitalise sales and marketing in its two core foreign markets, the UK and Russia, and expand its reach into new markets such as China, northern Europe and the Middle East. During the year Aristo also strengthened its presence in Russia, increased the size of its local team and expanded its marketing efforts. In the UK, it participated in exhibitions and targeted events. It signed a series of mainly exclusive agreements with leading overseas agents and tour operators, and reports that early results have been encouraging.

Aristo share exchange: Lower expenses, better portfolio spread

At the end of March DCI announced that it had agreed a share exchange with Aristo Developers, which it believes will convey a number of benefits.

Under this deal it will exchange a 50.2% stake in this fully-owned DCI subsidiary for a 34.2% stake in DCI held by its largest shareholder, Theodore Aristodemou, Aristo's CEO. Mr Aristodemou will remain Aristo's CEO and will be further incentivised to deliver maximum value.

As the exchange will take place on an NAV for NAV basis before deferred tax (valued at €375.5m) DCI's NAV/share is unaffected. It will, however, have the following effects:

- DCI's shareholding in Aristo reduces to 49.8%; Mr Aristodemou's shareholding in DCI to 1.14% of its reduced share capital. Aristo will now be treated in DCI's accounts as an associate and the impact (see *pro forma* summary balance sheet below) is that DCI's consolidated debt falls from €453.5m to €124.4m and its debt to asset ratio from 27% to 13%. DCI will retain 100% of the small operations and asset portfolio of Aristo in Greece and Mr Aristodemou ownership of 256 residential plots within its Venus Rock project.

Exhibit 2: Pro forma group balance sheet - including Aristo exchange

	Before Aristo exchange		After Aristo exchange	
	€000	%	€000	%
Assets				
Real estate assets	1,604,110	94%	598,733	63%
Equity accounted investees	7,868	1%	306,750	33%
Other assets	82,755	5%	38,133	4%
Total assets	**1,694,733**	**100%**	**943,616**	**100%**
Equity				
NAV before DITL	1,100,030	65%	724,485	77%
Non-controlling interests	35,955	2%	35,955	4%
Total equity before DITL	**1,135,985**	**67%**	**760,440**	**81%**
Liabilities				
Loans and borrowings	453,515	27%	124,446	13%
Other liabilities	105,233	6%	58,730	6%
Total liabilities	558,748	33%	183,176	19%
Total equity and liabilities	**1,694,733**	**100%**	**943,616**	**100%**

Source: DCI FY11 results

- The exchange results in a €4.2m reduction in annual management fees, ie 2% on the €208m investment cost of the 50.25% shareholding transferred.
- Although it also triggers a performance fee of c €33.5m, the investment manager has agreed to waive this in return for a prorated reduction – equivalent to the net profit generated as a result of the share exchange – in the base cost of the remaining portfolio used for future performance fee calculations. It has also replaced the 8% soft hurdle with the average annual one-month Euribor rate.
- DCI's exposure to Cyprus is decreased and the portfolio balance improved across its six markets, Cyprus, Greece, Turkey, Croatia, Dominican Republic and Panama. It expects to increase focus on its core expertise, ie luxury residential resort development targeted at the highest end destination market, a segment in short supply relative to demand.

Exhibit 3: Current DCI investments – pro-forma including Aristo exchange

Project location	Net Investment Cost (€m)	Debt (€m)	Asset Value (€m)	Loan to Asset Value (%)
Greece	223	(46)	356	13%
Cyprus	197	(15)	344	4%
Croatia & Turkey	52	(16)	58	28%
Americas	51	(47)	147	32%
Total	**523**	**(124)**	**905**	**14%**

Source: DCI FY11 results

Financials: Potential for improved stability in FY12

There were no new investments in 2011, but over €85m of asset sales and divestments. Total group sales to date are €410m, above book value of assets sold.

The investment manager worked within the limits of group cash resources to progress advanced schemes in FY11. Cash resources were boosted by €8.5m raised in December 2011 via the issue of 26.2m shares at 27p (plus 5.055m warrants for additional shares at 35p/share). There was €31m of cash at the year end, €17.5m at 23 March 2012, but that does not reflect typical quarterly cash consumption. Indeed, management projection suggest that ongoing ‘cash burn’ this year will be significantly reduced post the Aristo share exchange, and income stronger as projects reach maturity. The latter already includes c €10m in the pipeline upon delivery of Aman villas sold to date, plus additional sales under negotiation and possible joint ventures, where discussions have picked up pace as the eurozone crisis has eased somewhat. Management also has the ability to delay construction commitments if necessary to match available cash resources.

Although it is inevitably difficult to predict cash flows from early stage development projects, the statement was cautiously optimistic. The Amanzoe hotel is due for completion in May and when it opens this summer should become DCI’s first cash flow positive asset. It will moreover provide a showcase of its development capabilities and a template for the potential profitability of the remaining portfolio. Another possible catalyst for better appreciation of DCI’s appeal and indeed its equity rating is if the project provides evidence for resilient pricing of ultra-high-end homes. According to management, prices in some locations remain at historic highs levels and the group’s luxury offering is in a position to deliver a unique, prime product in scarce supply in its key markets.

Exhibit 4: Summary year balance sheet (before Aristo exchange)

31 December	2010	2011
Assets		
Property assets (investment & trading properties)	1,716,222	1,611,978
Other assets	43,653	51,687
Cash and equivalents	29,782	31,068
Total assets	1,789,657	1,694,733
Equity		
Equity attributable to Dolphin shareholders	1,143,524	995,695
Non-controlling interests	40,853	35,955
Total equity	1,184,377	1,031,650
Liabilities		
Loans and borrowings	396,704	462,612
Other liabilities	88,383	96,136
Deferred tax liabilities	120,193	104,335
Total liabilities	605,280	663,083
Total equity and liabilities	1,789,657	1,694,733
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Source: DCI FY11 results

Sensitivities: Buyer appetite, construction finance and equity

The key sensitivity is unchanged vs FY11, ie availability of construction finance, institutional investor appetite for residential resorts and development equity. A re-emergence of these would enable DCI to accelerate its development plans and realise significant returns from its portfolio. Although the Greek austerity budget dampened domestic demand, Greece remains an important international holiday and leisure destination. Group projects target the top-end international luxury market.

Valuation: Option on upside from future cash flows

Investors must take a view on (a) the investment manager's ability to continue to navigate difficult markets, (b) the timing of any recovery and (c) DCI's ability to reach this point without significant dilution or asset sales in a buyer's market. At the current price the shares are essentially an option on successful execution and delivery of a phased development programme.

We set out the IM's projections: total existing portfolio net cash potential of c €4.2bn, 808p/share over the next 12 years, updated for the reduced stake in Venus Rock. For the first phases of four advanced projects that is €560m (c 107p/share) over six years, ie sales of completed residential units and retail land plots, plus operational income from leisure components (hotels, golf courses, marinas). For all phases of the four advanced projects, c €1.5bn of net pre-tax cash (c 284p/share).

Exhibit 5: Investment manager's estimates of potential future net cash generation

	Residential Units		Land Plots	Leisure			
Advanced projects (€m)	Sales	Costs	Sales	Net Operating Income	Sales	Net Costs	Cash Returns
The Porto Heli Collection (100% DCI ownership)							
First phase	245	(93)	23	19	60	(13)	241
Other phases	548	(272)			134	(134)	276
	793	(365)	23	19	194	(147)	517
Venus Rock (49.8%)							
First phase	384	(182)		1	21	(18)	206
Other phases	211	(101)					110
	595	(283)		1	21	(18)	316
Playa Grande (99%)							
First phase	141	(96)		13	59	(30)	87
Other phases	379	(212)	140				307
	520	(308)	140	13	59	(30)	394
Pearl Island (60%)							
First phase	15	(10)	28	4	3	(13)	27
Other phases	424	(267)	82				239
	439	(277)	110	4	3	(13)	266
Total	2,347	(1,233)	273	37	277	(208)	1,493
Major Projects							
	2,545	(1,232)			311	(311)	1,313
Aristo Developers (49.8%)							
Dividends and Terminal Value							259
Residual Land Value							1,180
Grand Total	4,892	(2,465)	273		588	(519)	4,245

Source: DCI FY11 results

FY11 year-end NAV was €1.1bn, or €1bn less deferred tax. Those figures were respectively €103m (8.6%) and €90m (8.3%) below Q311. Equivalent sterling NAV/share was 139p and 125p, down 15.4% and 15% in the final quarter, post an average 5% decline in the value of DCI's Cyprus assets, 9% in Greece, NAV dilution post the issue of 26.2m shares at 27p in December and the impact of 3.7% GBP/EUR appreciation in the period.

Exhibit 6: NAV performance

			Variation since			
			31 December 2010		30 June 2011	
	€	£	€	£	€	£
Total NAV before deferred income tax liabilities (m)	1,100	922	(13.0%)	(14.9%)	(8.8%)	(14.9%)
Total NAV before after income tax liabilities (m)	996	834	(12.9%)	(14.8%)	(8.6%)	(14.8%)
NAV per share before DITL	1.65	1.39	(17.9%)	(19.7%)	(12.4%)	(18.3%)
NAV per share after DITL	1.50	1.25	(17.9%)	(19.7%)	(12.2%)	(18.1%)

Source: DCI FY11 results

Exhibit 7: Financials

€'000s	2009	2010	2011
Year end 31 December	IFRS	IFRS	IFRS
PROFIT & LOSS			
Revenue	90,843	69,912	32,782
Cost of Sales	(94,276)	(60,018)	(27,859)
Gross Profit	(3,433)	9,894	4,923
EBITDA	(71,318)	(37,108)	(6,143)
Operating Profit (before amort. and except.)	(72,884)	(39,052)	(7,984)
Goodwill & intangible Amortisation	(628)	0	0
Other income	38,056	181	0
Gain/(loss) on portfolio revaluation/other impairment	(131,153)	(24,918)	(106,197)
Operating Profit	(166,609)	(63,789)	(114,181)
Net Interest	(20,111)	(14,418)	(28,151)
Profit Before Tax (norm)	(92,995)	(53,470)	(36,135)
Profit Before Tax (FRS 3)	(186,720)	(78,207)	(142,332)
Tax	19,518	5,940	16,238
Profit After Tax (norm)	(73,477)	(47,530)	(19,897)
Profit After Tax (FRS 3)	(167,202)	(72,267)	(126,094)
Average Number of Shares Outstanding (m)	583.2	627.4	636.1
EPS - normalised (p)	(13.2)	(7.6)	(3.9)
EPS - normalised and fully diluted (c)	(13.2)	(7.6)	(3.9)
EPS - (IFRS) (c)	(29.3)	(11.6)	(20.6)
Dividend per share (p)	0.0	0.0	0.0
Gross Margin (%)	-3.8	14.2	15.0
EBITDA Margin (%)	-78.5	-53.1	-18.7
Operating Margin (before GW and except.) (%)	-80.2	-55.9	-24.4
BALANCE SHEET			
Fixed Assets	1,469,749	1,387,002	1,321,390
Intangible Assets	0	0	0
Tangible Assets	1,380,457	1,275,974	1,201,933
Investments	89,292	111,028	119,457
Current Assets	395,884	402,655	373,343
Stocks	284,107	339,461	298,964
Debtors	48,860	33,412	43,311
Cash	62,917	29,782	31,068
Other	0	0	0
Current Liabilities	(164,233)	(157,413)	(237,903)
Creditors	(83,188)	(63,478)	(58,936)
Short term borrowings	(81,045)	(93,935)	(178,967)
Long Term Liabilities	(447,936)	(447,867)	(425,180)
Long term borrowings	(289,423)	(293,444)	(274,548)
Other long term liabilities	(158,513)	(154,423)	(150,632)
Net Assets	1,253,464	1,184,377	1,031,650
CASH FLOW			
Operating Cash Flow	(120,239)	(49,997)	(44,676)
Net Interest	(18,523)	(18,396)	(25,048)
Tax	(1,147)	(2,558)	(1,130)
Capex	0	0	0
Acquisitions/disposals	81,410	20,562	(17,988)
Financing	850	2,172	10,152
Dividends	(1,305)	0	0
Net Cash Flow	(58,954)	(48,217)	(78,690)
Opening net debt/(cash)	248,597	307,551	357,597
HP finance leases initiated	0	0	0
Other	0	(1,829)	13,840
Closing net debt/(cash)	307,551	357,597	422,447

Source: Company accounts/Edison Investment Research