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KBL-TSX

Rating:	Buy
Target:	\$42.00
Price:	\$38.75
Return:	15%
Valuation:	15x EPS, 10x AFFO, 10x EV/ EBITDA (F2022 est)

Market Data

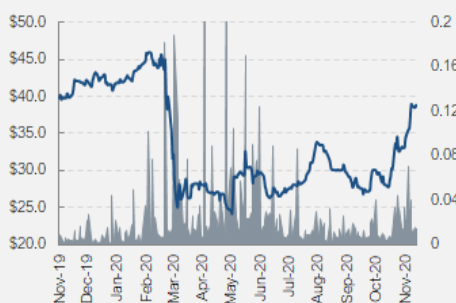
Basic Shares O/S (M)	10.5
Market Cap (\$M)	407.2
Enterprise Value (\$M)	465.5
Cash (\$M)	1.0
Debt (\$M)	59.3
52 Week Range	\$23.73-\$46.44
Avg. Weekly Volume	13,488
Dividend yield (%)	3.1%
Fiscal Year End	Dec-31

Financial Metrics

In C\$M	2019A	2020E	2021E
Total revenue	252.4	201.3	256.8
EBITDA	47.6	37.5	42.3
EBITDA growth (%)	61.1%	(21.1%)	12.7%
EBITDA margin (%)	18.8%	18.6%	16.5%
Net income, adjusted	10.9	5.4	15.6
EPS, adjusted	\$1.04	\$0.51	\$1.48
Op. Cash Flow	42.1	39.0	47.4
Cash flow per share	\$4.18	\$2.54	\$4.44
AFFO (FCF) per share	\$2.82	\$2.87	\$3.67
Payout ratio (%)	31.6%	48.5%	27.1%

Company Description

K-Bro Linen provides laundry and linen services for the healthcare and hospitality sectors in Canada & the UK



Source: Refinitiv, Leede Jones Gable

Initiating Coverage on Industry-Leading Healthcare-Hospitality Services Provider with a BUY Rating

We are initiating coverage on AB-based healthcare & hospitality-focused linen & laundry processing firm K-Bro Linen with a BUY rating and a one-year price target of \$42.00. The firm operates highly-automated laundry processing facilities in several Canadian provinces, mainly in Ontario, Alberta, and British Columbia, as well as in the northern UK through its acquisition in FQ417 of Fishers Topco, and though the firm has encountered pandemically-facilitated headwinds on revenue/EBITDA since FQ120, adjusted EBITDA margins have in fact been steadily climbing in recent quarters. Our valuation is based on the average of three distinct methodologies based on our F2022 financial forecasts for the firm (15x EPS, 9x AFFO, 10x EV/EBITDA), with our target corresponding to a one-year target return of 11.5%, and total return including 3.1% dividend yield, of 15.0%.

Firm remains undervalued to direct peer group; compelling valuation at current levels: At present, K-Bro remains relatively undervalued to its direct peer group. The firm presently trades at 13.7x FY1 EV/EBITDA and 12.7x FY2 EV/EBITDA, which is lower than its own peer group at 18.4x/16.7x respectively. Even at a conservative multiple of 10x 2022 EV/EBITDA, this implies a share price of \$43.68 or a +13% premium from current price levels. Loyal followers of our KBL research will recall that we were cautious on valuation during the early days of COVID-19 pandemic logistics, but FQ320 data and commentary as we describe below, gives us confidence in K-Bro's operational excellence and leadership in the niche healthcare/hospitality linen/laundry processing industry.

Still the safest dividend in our coverage universe: Despite topline impact from ongoing pandemic challenges, the firm's dividend payout ratio for FQ320 was 29%, which is the lowest in recent operating history. In contrast, debt on the firm's balance sheet remains low at \$59.3M, and with debt of that magnitude reflecting debt/EBITDA run-rate of 1.2x and EBITDA/interest of 11.1x. The firm has been a consistent dividend payer in the last ten years, and its last dividend raise was in 2014 (going from \$0.0958/shr to \$0.10/shr). On that note, we maintain our view that the firm's dividend is the among one of the most sustainable within our broader coverage universe.

Long track record of recurring revenue generation and financial prudence should help to weather the COVID-19 storm: Although K-Bro Linen's healthcare processing services were considered as an Essential Service in Canada, the firm has nonetheless endured instability on its healthcare revenue owing to the reduction in elective surgeries and decreased occupancy rates. Certain regions in Canada have re-entered into a second lockdown as a second wave of COVID-19 is anticipated (Toronto recently entered into a second lockdown), and this could further exacerbate processing volumes. On the hospitality front, global travel restrictions from COVID-19 has significantly impacted the tourism industry in Canada and the UK, with K-Bro's processing revenue from the hospitality division has also taken a significant hit.

Exhibit 1. Income Statement & Financial Forecast Summary – K-Bro Linen

<i>(C\$000, except EPS)</i>	2015A	2016A	2017A	2018A	2019A	2020E	2021E	2022E	2023E
Total revenue	\$182,001	\$175,324	\$170,559	\$239,534	\$252,410	\$201,323	\$256,790	\$278,054	\$286,133
Revenue growth (%)	17%	(4%)	(3%)	40%	5%	(20%)	28%	8%	3%
EBITDA	\$64,604	\$44,471	\$24,021	\$29,517	\$47,565	\$37,516	\$42,282	\$51,966	\$53,572
EBITDA growth (%)	41.9%	(31.2%)	(46.0%)	22.9%	61.1%	(21.1%)	12.7%	22.9%	3.1%
EBITDA margin (%)	35.5%	25.4%	14.1%	12.3%	18.8%	18.6%	16.5%	18.7%	18.7%
Net income, operations	\$45,149	\$30,264	\$5,718	\$6,169	\$10,906	-\$104	\$15,622	\$27,659	\$31,923
Net income, adjusted	\$45,149	\$30,264	\$5,754	\$6,105	\$10,898	\$5,407	\$15,622	\$27,659	\$31,923
EPS, operations	\$4.27	\$2.87	\$0.61	\$0.59	\$1.04	-\$0.01	\$1.48	\$2.62	\$3.02
EPS, adjusted	\$4.27	\$2.87	\$0.61	\$0.58	\$1.04	\$0.51	\$1.48	\$2.62	\$3.02
Distribution	\$3,169	\$3,169	\$11,310	\$12,610	\$12,612	\$12,668	\$12,675	\$12,675	\$12,675
Distribution per share	\$0.30	\$0.30	\$1.20	\$1.20	\$1.20	\$1.20	\$1.20	\$1.20	\$1.20
Distributable cash	\$49,419	\$22,405	\$17,633	\$15,202	\$39,974	\$26,122	\$46,792	\$53,498	\$52,267
Oper cash flow (ex W/C)	\$57,019	\$25,715	\$22,702	\$28,934	\$42,050	\$39,049	\$47,436	\$53,482	\$53,794
AFFO/free cash flow	\$54,436	\$22,081	\$20,047	\$24,765	\$29,607	\$30,252	\$0	\$0	\$0
Cash flow per share	\$4.80	\$2.32	\$1.99	\$1.67	\$4.18	\$2.54	\$4.44	\$5.08	\$4.96
AFFO (FCF) per share	\$5.15	\$2.09	\$2.13	\$2.36	\$2.82	\$2.87	\$3.67	\$4.24	\$4.27
Payout ratio (%)	6.4%	14.1%	64.1%	83.0%	31.6%	48.5%	27.1%	23.7%	24.3%
FCF yield (%)	13.3%	5.4%	5.5%	6.1%	7.3%	7.4%	9.5%	10.9%	11.0%
P/E	9.1x	13.5x	63.5x	66.7x	37.4x	75.7x	26.2x	14.8x	12.8x
EV/EBITDA	5.6x	8.2x	15.1x	12.3x	7.6x	9.7x	8.6x	7.0x	6.8x

Source: Company filings, Leede Jones Gable

Despite the significant impact to topline YTD, we remain confident in KBL's ability to weather the storm. To be clear, KBL's revenue tends to be generated by long-term contracts (5-10 years for healthcare, 2-5 years for hospitality), and tends to be recurring in nature. The caution on processing volumes is in our view, cushioned by the structure of these contracts, particularly on the healthcare front. This is evidenced by recent FQ320 data, with Canadian consolidated revenue in the quarter at \$43.0M, which reflects a reduction of -13% or \$49.4M on a y/y basis.

Exhibit 2. Valuation summary for K-Bro Linen

Price-to-earnings multiple	9x	11x	13x	15x	17x	20x	25x
Implied unit price ^{1,2}	\$23.57	\$28.80	\$34.04	\$39.28	\$44.52	\$52.37	\$65.46
AFFO multiple	5x	7x	9x	10x	11x	13x	15x
Implied unit price ^{1,2}	\$21.21	\$29.69	\$38.17	\$42.42	\$46.66	\$55.14	\$63.62
EV/EBITDA multiple	5x	7x	9x	10x	11x	13x	15x
Implied share price (\$) ^{1,2}	\$19.08	\$28.92	\$38.76	\$43.68	\$48.60	\$58.43	\$68.27
One-year K-Bro Linen target price (C\$)	\$41.79						

¹ Based on F2022 forecasts (Adjusted EPS \$2.62, EBITDA \$52.0M, AFFO \$4.24/shr)² EV incorporates FQ320 cash of \$1.0M, total LT debt of \$59.3M, basic S/O of 10.6M

Source: Leede Jones Gable

Well-prepared to grow processing volumes in newly-constructed facilities in ON/BC, with growth capex already fully-deployed into those facilities: To supplement our revenue observations above, the firm's last major CAPEX projects were in 2017/2018 for the build out of two new facilities in Toronto and Vancouver. Across the board, the firm has 5 of 8 facilities that were built or acquired in 2011 to 2018. The relatively young age of these facilities implies high technology efficiencies and future cost savings from the use of new technologies at these facilities. Together with K-Bro's strong market share dominance in Canadian markets, its long operational history, financial prudence (more on that below), strong key customer retention, and tenured management, this gives us confidence that the firm will be able to sustain present shortfalls in revenue at least until the pandemic subsides.

Exhibit 3. Q320 Financial Summary & Comparative Performance For K-Bro Linen

Year-end December 31 (C\$'000)	Q319	Q220	Q320	% chg Q/Q	% chg Y/Y
Healthcare revenue	33,224	33,598	37,417	11.4%	12.6%
Hospitality revenue	16,267	1,755	5,628	220.7%	(65.4%)
Canadian Revenue	49,491	35,353	43,045	21.8%	(13.0%)
International Revenue: Fishers	18,351	2,167	8,394	287.4%	(54.3%)
Consolidated Revenue	67,842	37,520	51,439	37.1%	(24.2%)
<i>Operating expenses</i>					
Salaries & benefits	26,605	11,087	16,963	53.0%	(36.2%)
Linen	7,121	5,223	6,371	22.0%	(10.5%)
Utilities	4,105	2,109	2,849	35.1%	(30.6%)
Delivery	7,107	3,525	5,128	45.5%	(27.8%)
Occupancy costs	1,090	497	941	89.3%	(13.7%)
Materials and supplies	2,331	1,229	1,891	53.9%	(18.9%)
Repairs and maintenance	2,220	1,415	1,804	27.5%	(18.7%)
Corporate G&A costs	2,656	2,380	2,773	16.5%	4.4%
EBITDA	14,607	10,055	12,719	26.5%	(12.9%)
<i>EBITDA margin (%)</i>	21.5%	26.8%	24.7%	NA	NA
<i>Debt/EBITDA run-rate</i>	1.1x	1.4x	1.2x	NA	NA
<i>EBITDA/interest</i>	9.7x	12.7x	11.1x	NA	NA
Total expenses unrelated to operations	8,559	7,644	7,981	4.4%	(6.8%)
Earnings before taxes (EBT)	6,048	2,411	4,738	96.5%	(21.7%)
<i>EBT margin (%)</i>	8.9%	6.4%	9.2%	NA	NA
Tax expense (recovery)	1,379	798	1,296	NA	NA
<i>Tax rate (%)</i>	22.8%	33.1%	27.4%	NA	NA
Net income	4,669	1,613	3,442	113.4%	(26.3%)
Net income (adjusted)	4,659	1,613	3,442	NA	NA
<i>Net margin (%)</i>	6.9%	4.3%	6.7%	NA	NA
EPS (consolidated operations)	\$0.44	\$0.15	\$0.33	113.4%	(26.6%)
EPS (adjusted)	\$0.44	\$0.15	\$0.33	113.4%	(26.5%)
Shares (units) outstanding (basic, 000)	10,511	10,563	10,563	NA	NA
Shares (units) outstanding (fd, 000)	10,604	10,604	10,667	NA	NA
Distribution	3,181	3,196	3,203	NA	NA
Distribution per share	\$0.30	\$0.30	\$0.30	NA	NA
AFFO	8,768	7,259	11,050	52.2%	26.0%
AFFO per share	\$0.83	\$0.69	\$1.05	52.2%	25.4%
Payout ratio (%)	36.3%	44.0%	29.0%	(34.2%)	(20.1%)
Operating Cash (before WC)	12,353	9,215	13,220	43.5%	7.0%
Adjusted Operating Cash (with WC)	19,816	6,289	(504)	(108.0%)	(102.5%)
Cash flow per share	\$1.89	\$0.60	(\$0.05)	(108.0%)	(102.5%)

Source: Company filings, Leede Jones Gable

Summary and valuation: We are initiating on K-Bro Linen with a Buy rating and \$42.00 price target. Our PT valuation is the average of three methodologies, multiples of our F2022 EPS, AFFO and EBITDA respectively. In that year, we forecast EBITDA/EPS/AFFO of \$52.0M/\$2.62/\$4.24 respectively. Our EV incorporates FQ320 cash of \$1M and total LT debt of \$59.3M. The average of our three methodologies yields a PT of \$41.79, which we round to \$42.00. Our one-year PT along with the 3.1% dividend yield implies a total return of 15.0%.

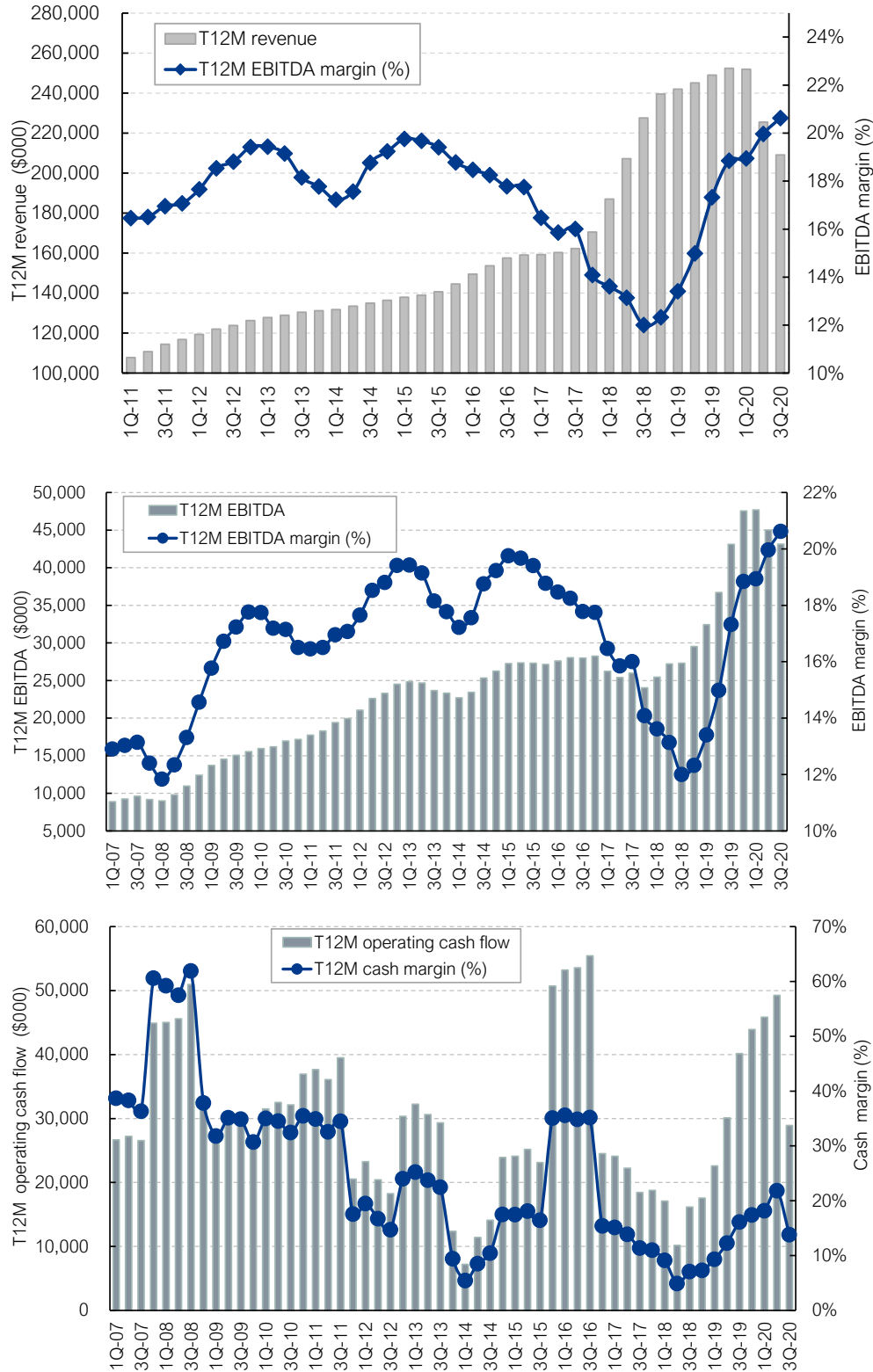
Exhibit 4. Comparable Companies for K-Bro Linen

Company	Curr.	Sym	Shares (M)	Share Price 13-Dec	Mkt Cap (C\$M)	Ent. Value (C\$M)	EV/EBITDA			Price/Earnings			Description
							(T12)	(FY1)	(FY2)	(T12)	(FY1)	(FY2)	
Linen/laundry services peers													
Cintas	USD	CTAS	104.6	\$349.11	\$46,530	\$49,357	NA	NA	NA	39.6x	39.0x	36.6x	Cincinnati-based uniform supply company provides healthcare uniform rental services
Aramark	USD	ARMK	253.1	\$37.60	\$12,633	\$20,815	20.4x	NA	13.8x	NA	NA	21.2x	PA-based services firm, with healthcare division focused on food services, facility management, uniform services
Eco Lab	USD	ECL	285.4	\$221.25	\$47,505	\$88,216	NA	NA	NA	NA	NA	NA	Diversified services, with hospitality and healthcare laundry operations internationally, including Canada
Sodexo	EUR	SW	147.5	€ 72.18	€ 16,458	€ 23,159	19.8x	19.9x	15.0x	NA	27.7x	16.8x	French service-solutions company with laundry management operations in Cda
Average							20.1x	19.9x	14.4x	NA	33.4x	24.9x	
Profitable Canadian healthcare firms													
Akumin	CAD	AKU	70.2	\$3.91	\$274	\$692	8.3x	10.1x	8.5x	NA	NA	18.2x	US-based medical imaging clinic consolidator, mainly in Florida
Bausch Health	CAD	BHC	355.2	\$26.22	\$9,312	\$30,725	9.8x	9.5x	8.9x	NA	7.1x	5.8x	QC-based specialty pharma firm, formerly Valeant/Biovail
CareRx	CAD	CRRX	52.4	\$3.60	\$189	\$256	NA	19.5x	12.0x	NA	NA	NA	Long-term care Rx services provider
CeaPro	CAD	CZO	77.6	\$0.70	\$54	\$51	10.8x	NA	NA	21.2x	15.9x	30.4x	AB-based biopolymer extraction & manufacturing firm (beta-glucan, avenanthramides), partnered with Symrise
Chartwell REIT	CAD	CSH.UN	215.6	\$11.57	\$2,494	\$4,981	18.5x	19.2x	17.6x	NA	NA	NA	ON-based nursing home and retirement residence operator
Cipher Pharmaceuticals	CAD	CPH	27.0	\$0.83	\$22	\$16	NA	1.3x	2.4x	3.1x	3.4x	6.6x	ON-based specialty pharmaceutical company; lead drug is isotretinoin formulation Absorica
CRH Medical ¹	CAD	CRH	71.4	\$3.63	\$203	\$326	10.9x	12.5x	8.6x	NA	NA	NA	BC-based but US-focused GI anesthesiology services firm
Extencare REIT	CAD	EXE	89.5	\$6.75	\$604	\$1,006	8.7x	8.2x	10.8x	19.0x	NA	30.7x	ON-based nursing home, homecare, and rehab therapy provider
Hamilton Thorne	CAD	HTL	138.5	\$1.29	\$179	\$132	NA	22.8x	14.2x	NA	NA	NA	US-based distributor of reproductive technologies, mostly optical lenses for microscopic analysis
HLS Therapeutics	CAD	HLS	31.7	\$16.78	\$533	\$506	24.7x	22.5x	13.2x	NA	NA	NA	ON-based specialty pharmaceutical firm, flagship products are Absorica & Vascepa
Knight Therapeutics	CAD	GUD	130.0	\$5.22	\$679	\$324	18.4x	NA	14.4x	24.9x	22.2x	NA	QC-based specialty pharmaceutical firm
Medexus Pharmaceuticals	CAD	MDP	14.5	\$6.60	\$95	\$143	13.2x	9.4x	6.5x	NA	NA	NA	QC-based specialty pharmaceutical firm, flagship products are factor IX analog Ixinity & injectible methotrexate Rasuvo
Medical Facilities ¹	CAD	DR	31.1	\$7.35	\$179	\$365	4.5x	3.9x	4.4x	3.4x	17.9x	21.3x	US-based operator of physician-owned surgical centers, ambulatory surgical ctrs
Northwest Healthcare Properties	CAD	NWH.UN	175.7	\$12.46	\$2,190	\$5,740	NA	20.7x	18.8x	14.1x	14.3x	19.5x	ON-based owner/operator of healthcare properties, major tenants include CML Healthcare/LifeLabs
Protech Home Medical	CAD	PTQ	112.4	\$1.45	\$163	\$149	NA	7.3x	5.4x	NA	NA	23.5x	US-based home respiratory care
Sienna Senior Living	CAD	SIA	67.0	\$13.63	\$914	\$1,895	18.4x	18.8x	16.0x	NA	NA	NA	Canada-based nursing care provider
Viemed Healthcare	CAD	VMD	38.9	\$11.29	\$439	\$325	10.9x	8.7x	11.2x	15.5x	17.7x	31.6x	US-based home respiratory care
Average					\$1,090		13.1x	13.0x	10.8x	14.5x	14.1x	20.8x	
K-Bro Linen	CAD	KBL	10.7	\$37.56	\$401.02	\$549.94	16.8x	13.7x	12.7x	NA	NA	38.6x	Laundry and linen processing services for healthcare & hospitality industries

¹ Shares trade on TSX in C\$, market capitalization & EV converted to US\$ using current US\$:C\$ exchange rate of 1.31x

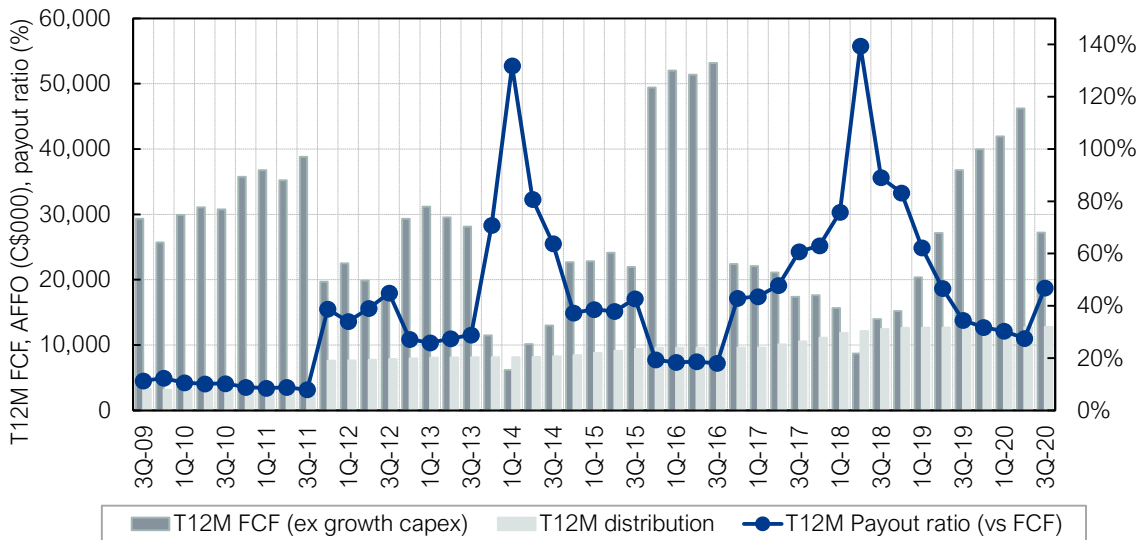
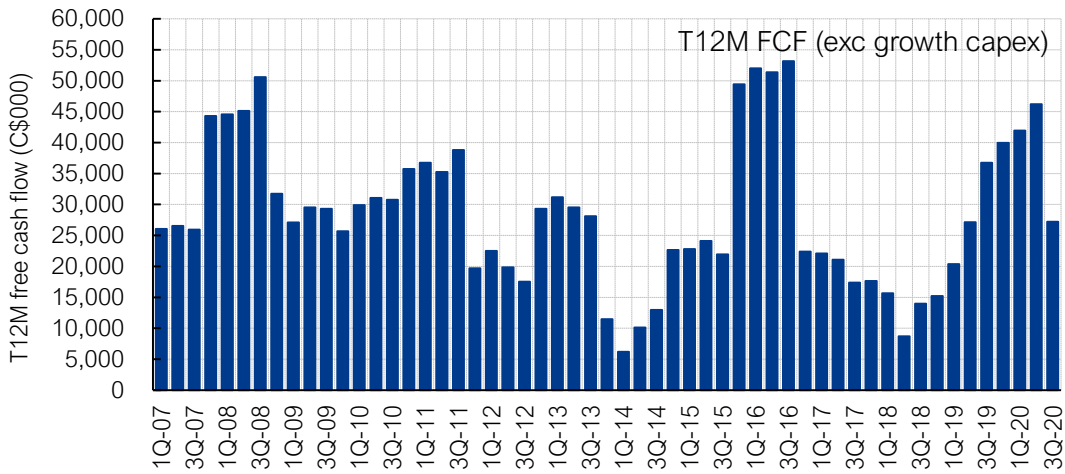
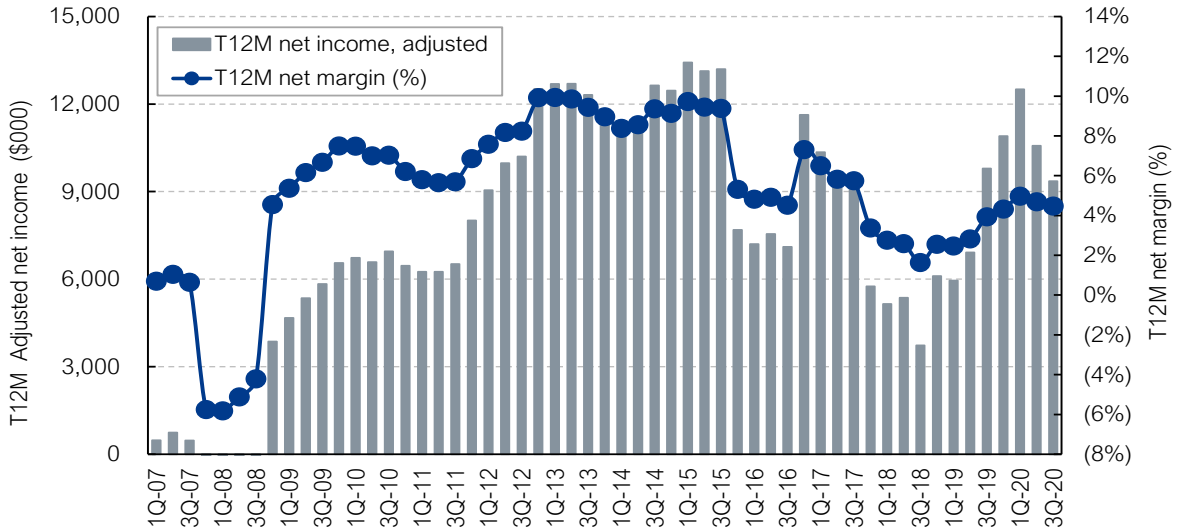
Source: Refinitiv, Leede Jones Gable, Company Filings

Exhibit 5. Historic T12M Revenue, EBITDA Margin, AFFO & Pay-Out Ratio Trends For K-Bro Linen



Source: Historical data – K-Bro Linen, modified for presentation by Leede Jones Gable

Exhibit 6. Historic T12M Net Income & Free Cash Flow Trends For K-Bro Linen



Source: Historical data – K-Bro Linen, modified for presentation by Leede Jones Gable

Disclosures none

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