



ACL CABLES PLC

CSE: ACL.N0000

Bloomberg: ACL SL

STRONG BUY

Mar 2018

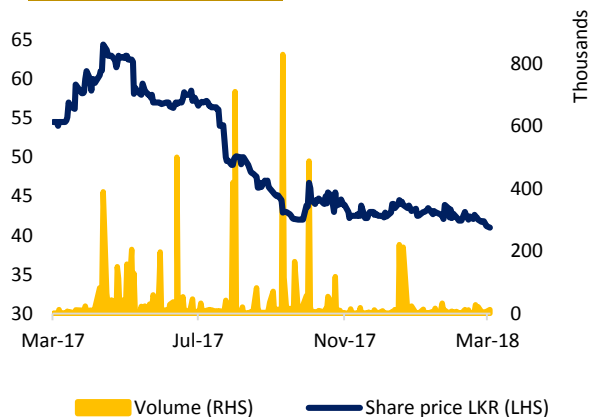
Current Price – LKR 43.0

Fair value [FY19E] – LKR 60.0

3QFY18 Earnings ↓ 10%YoY

KEY DATA			
Share Price (LKR)	41.0		
52w High/Low (LKR)	64.4/ 41		
Average Daily Volume (Shares)	33,091		
Average Daily Turnover (LKR)	1,697,201		
Issued Share Capital (Shares Mn)	120		
Market Capitalisation (LKR mn)	4,911		
Price Performance (%)	1 mth	3 mths	12mths
ACL	-3%	-4%	-25%
ASPI	-2%	2%	8%
Major Shareholders as at 31st Dec 2017			
U. G. Madanayake	38.15%		
Suren Madanayake	22.21%		
Employees Provident Fund	4.93%		
Employees Trust Fund Board	3.70%		
Deutsche Bank -National Equity Fund	1.89%		
Estimated Free Float	37.34%		

Price – Volume Chart



ANALYST CERTIFICATIONS AND REQUIRED DISCLOSURES BEGIN ON PAGE 6.

“Dip in copper prices and volume growth to favour earnings”

P/e 31 March	FY16	FY17	FY18E	FY19E	FY20E
Revenue (LKR Mn)	12,811	14,670	20,979	26,472	30,051
YoY % Growth	-11%	15%	43%	26%	14%
Net Profit (LKR Mn) ¹	1,094	1,118	759	1,301	1,498
EPS	9.13	9.33	6.34	10.86	12.51
YoY % Growth	27%	2%	-32%	71%	15%
Valuations					
PER (x)	4.6	4.5	6.7	3.9	3.4
PBV (x)	0.6	0.5	0.5	0.5	0.4
Dividend yield (%)	2.4%	3.6%	2.3%	3.9%	4.4%
NAVPS (adjusted)	70.5	77.9	83.3	92.5	103.2
DPS (adjusted)	1.0	1.5	1.0	1.6	1.9
Payout ratio	11%	16%	15%	15%	15%

1. Attributable to equityholders

LKR (Mn)	3QFY18	3QFY17	YoY	FY17	FY16	YoY
Revenue	3,602	3,711	↓ -3%	14,670	12,811	↑ 15%
Gross profit	820	837	↓ -2%	3,243	3,057	↑ 6%
Operating profit	482	526	↓ -8%	2,009	1,893	↑ 6%
PBT	382	439	↓ -13%	1,765	1,696	↑ 4%
Net profit	280	315	↓ -11%	1,255	1,269	↓ -1%
NP - equity	257	284	↓ -10%	1,118	1,094	↑ 2%

LKR (Mn)	4QFY17	1QFY18	2QFY18	3QFY18	QoQ
Revenue	3,002	3,403	4,664	3,602	↓ -23%
Gross profit	583	366	725	821	↑ 13%
Gross margin	19%	11%	16%	23%	↑ 7%
Operating profit	281	86	405	482	↑ 19%
Operating margin	9%	3%	9%	13%	↑ 5%
PBT	237	7	317	382	↑ 21%
Net profit	132	(5)	232	280	↑ 21%
Net margin	4%	0%	5%	8%	↑ 3%
NP - equity	116	(12)	212	257	↑ 21%

Disclosure on Shareholding:

First Capital Group and its affiliates does not hold shares of ACL and will not trade in this share for the three trading days following the issue of this document.

STRONG BUY with earnings and fair value maintained: FC Research maintains the full year profit forecast at LKR 759Mn for FY18E and LKR 1,301 for FY19E. Copper prices fell 7%MoM to USD6,500/mt levels in Mar 2018 from its 3-year peak levels of USD7,000/mt in Feb 2018. Goldman Sachs has raised its 2018 Copper price forecast to USD 8,000/mt, however the average Copper prices from Apr 2016-Mar 2017 are in line with our forecast. As such we maintain our Copper price forecast at USD7,100 for FY19E without raising it further given the recent reversal in the price trend. We remain positive on the volume growth over the next 2 years at 13% and 15% as several large scale projects such as Sheraton, Colombo City Centre, AVIC Astoria are underway while the demand from Ceylon Electricity Board is seen growing due to replacement of bare conductor cables with PVC covered cables. Accordingly, the revenue growth is estimated to be at a CAGR of 27% between FY17-20E. FC Research estimates ACL’s fair value at LKR 60.0 for FY19E providing an annualized total return of 52%. It should be noted that ASPI has risen by 8% while ACL has fallen by 25% over the last 12 months. Thus we recommend a **STRONG BUY** on ACL.

Earnings performance: YoY profits dip 10% but QoQ profits up 21%

3QFY18 Reported Earnings down by 10% YoY: ACL recorded earnings attributable to equity holders of LKR 257Mn in 3QFY18, down 10% from LKR 284Mn in 3QFY17. The lower earnings is a result of the increased cost of material driven by continued increase in copper prices which were higher ~29%YoY from Dec 2016 levels. The increase in the selling prices has supported ACL to remain profitable. On a QoQ basis, profits increased 21%.



3QFY18 revenues dipped 3%YoY: ACL recorded a revenue dip of 3%YoY to LKR 3.6Bn compared to LKR 3.7Bn in 3QFY17. On a QoQ basis revenue dipped by 37% from LKR 3.4Bn in 1QFY18.

Gross margins improve as selling price adjusted upwards: ACL's gross margin improved to 23% in 3QFY18 from 18% in 3QFY17 and 16% in 2QFY18. The increased selling price to match the higher cost of sales helped the company improve the margins.

Net margins up despite higher finance costs: ACL's net margin improved to 7.8% in 3QFY18 from 6.8% in 3QFY17 and 5.0% in 2QFY18. This is despite the finance cost increasing 75% to LKR 121Mn in 3QFY18 from 69Mn in 3QFY17.

Investment case: volume growth to drive earnings in FY19E while falling copper price outlook to favour earnings

Revenue to grow at a CAGR of 27% between FY17-FY20E: ACL's revenue can further expected to grow, driven mainly from the institutional sales which comprises between 30%-40% of its revenues. AVIC Astoria has ~30% of the project to be completed by 2018. Colombo City Centre has ~15-20 more floors to be constructed by December 2018. For several more projects such as Altair, Sheraton and Shangri La phase 2 – all of which ACL has won the contracts – the cabling work is yet to be completed. The revenues from CEB which accounts for 25%-30% also is estimated to grow due to the expected distribution line upgrades. Overall, the total revenue is expected to grow at a CAGR of 27% between FY17-20E.

Short term copper price fall favours earnings: Goldman Sachs has increased the 12 month Copper price forecast to ~USD8,000/mt. FC Research has used an average Copper prices of ~USD 6,900/mt for FY18E and ~7,176/mt for FY19E. As the average Copper prices from Apr 2017 – Mar 2018 are ~ USD6,400/mt which is below our forecast, we maintain the Copper price forecast given the recent reversal in the price trend. We believe that ACL, being the market leader in cables with ~70% of market share, can pass on any increase in Copper prices to the consumer especially beyond FY18E for the new contracts being entered.

Recommendation

FC Research maintains ACL's fair value at LKR 60.0 for FY19E (DCF based LKR 55.0, PER based LKR 65.0 which provides a total return of 53% in FY19E (capital gain 46%, dividend yield 6%). The annualized total return for FY19E is 52%. Despite the increased risk profile due to the rising Copper prices in the short-term, considering drop in ACL's price by 25% (ASPI increased by 8%) over the last 12 months, FC Research recommends a **STRONG BUY** on ACL.

Investment risks

Volatility in Copper prices: ACL's margins are highly sensitive to the increase in Copper price increase and how much of the increase can be passed onto the customer by increasing its selling prices. The copper prices have seen volatility with some ups and downs in the last 12 months.

Increasing competition and possibility of eroding market share: ACL cables is the market leader along with Kelani Cables. However, the company faces competition from imitated products which are produced at a cheaper cost and quality. While the company increase the prices to upkeep with the increasing Copper prices, they may face an erosion in the market share due to these imitated products, especially from the retail segment which is ~30% of the revenues. However, the imitated market size is not identified to be significant therefore we believe the impact would be minimal.



Valuation summary

Expected ACL price	FY19E
DCF based valuation	55
PER based target price	65
Average target price	60
Buy below price	53

Return	FY19E
Target price	60
Current price	41
Capital gain	19
Dividend	1.6
Capital gain %	46%
Dividend yield %	6%
Total return	53%
Annualised total return	52%

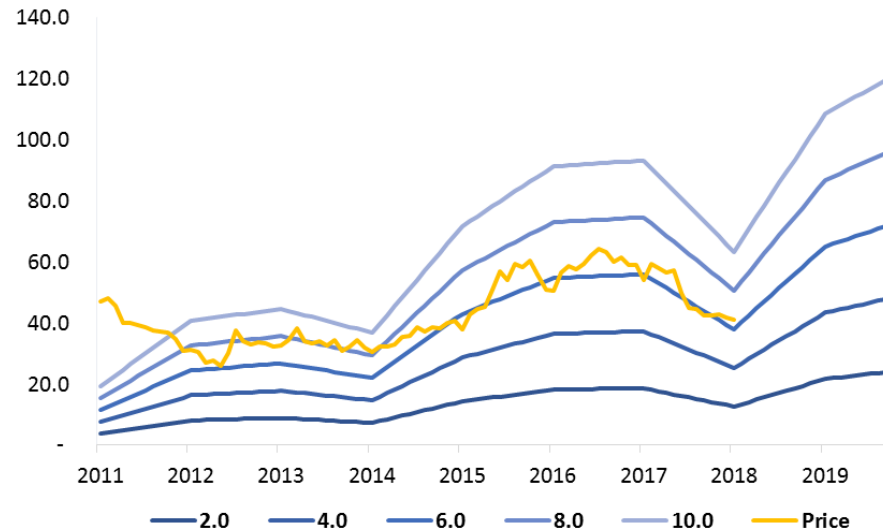
FY19E price annualised over 368

DCF valuation

Valuations	FY19E
NPV	7,780
Less: debt	3,299
Add: cash	2,080
Total value of Equity	6,561
No. of Shares	120
Value of Equity per share	55

COE		WACC	
R _f	9%	K _e	17%
R _m	18%	K _d	9%
R _m - R _f	9%	D/E	40/60
β	0.9	Terminal Growth rate (%)	3%
K_e = R_f + β (R_m - R_f)	17%	WACC	14%

ACL PE band



PER Valuation

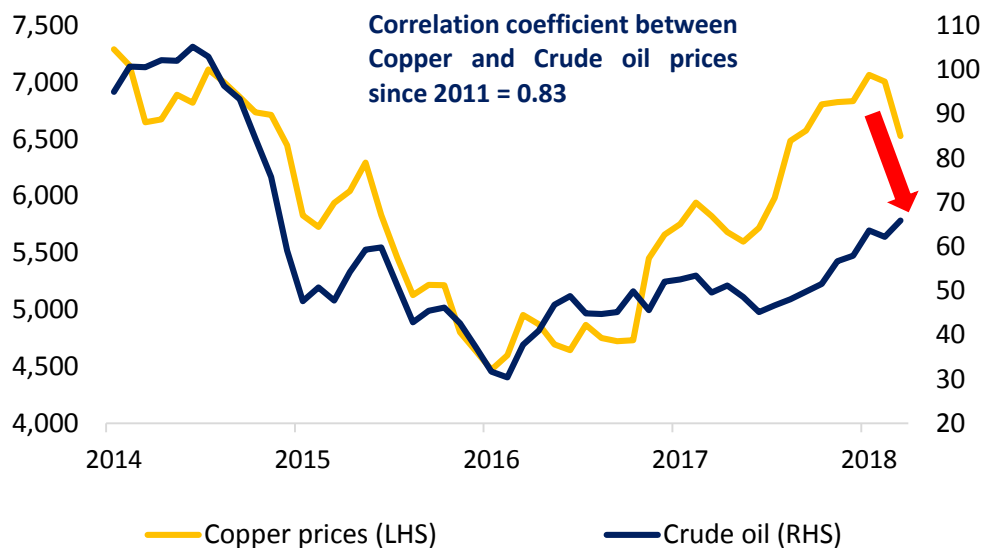
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Recommendation criteria

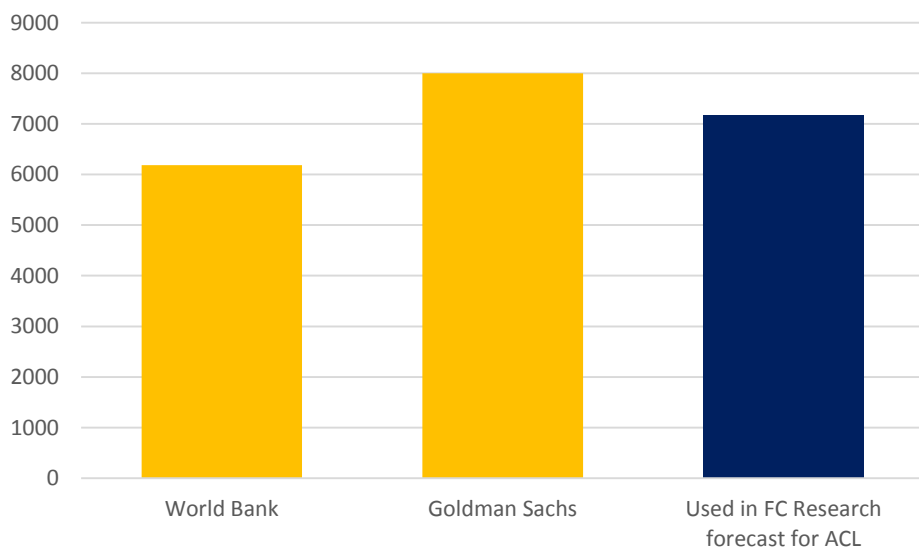
Categorization	Company Category	Strong Buy	Buy	Hold	Sell
Grade A	S&P SL20 Companies	T.Bill + 10% & Above	T.Bill + 5% & Above	T.Bill + 1% & Above	Below T.Bill + 1%
Grade B	Rest of the Companies	T.Bill + 13% & Above	T.Bill + 8% & Above	T.Bill + 3% & Above	Below T.Bill + 3%
Grade C	Companies less than LKR 1Bn Market Cap	T.Bill + 16% & Above	T.Bill + 11% & Above	T.Bill + 6% & Above	Below T.Bill + 6%



Annex I – Copper prices Vs Crude oil prices



Annex II – Forecast on Copper prices over the next 12-15 months



Annex III – Impact of changes in WACC and terminal growth on FY19E fair value

		WACC				
		10%	12%	14%	16%	18%
Terminal growth rate	1%	70	62	56	52	49
	2%	74	64	58	54	50
	3%	79	67	60	55	51
	4%	86	71	62	56	52
	5%	97	76	65	58	54

Base case

- Fair value for FY19E = LKR 60.0
- Buy below price for FY19E = LKR 53.0
- WACC for FY19E = 14%
- Terminal growth = 3%

Annex III – Impact of changes in Copper prices and volume growth on FY19E fair value

		Copper price FY19E USD/MT				
		6,458	6,817	7,176	7,535	7,894
Estimated volume growth FY19E	5%	140	97	54	11	-32
	10%	147	102	57	12	-33
	15%	154	107	60	13	-34
	20%	161	112	63	14	-36
	25%	168	117	66	14	-37

Base case

- Fair value for FY19E LKR 60.0
- Buy below price for FY19E = LKR 50
- Copper prices for FY19E = USD 7,176/mt
- Volume growth of 15%

Source: Company reports, Indexmundi, World Bank, CNBC, FC Research Estimates



Annex V – Income Statement

LKR (Mn)	FY16	FY17	FY18E	FY19E	FY20E
Revenue	12,811	14,670	20,979	26,472	30,051
Cost of sales	(9,754)	(11,427)	(17,687)	(21,928)	(24,775)
Gross profit	3,057	3,243	3,292	4,544	5,275
Other income	45	52	46	47	48
SG&A	(1,210)	(1,286)	(1,672)	(2,019)	(2,268)
Operating profit	1,893	2,009	1,666	2,572	3,056
Net finance cost	(252)	(219)	(475)	(526)	(698)
Profit before tax	1,696	1,765	1,199	2,055	2,366
Tax	(426)	(509)	(346)	(593)	(683)
Net profit	1,269	1,255	853	1,462	1,683
Non controlling	176	138	94	161	185
Equityholders	1,094	1,118	759	1,301	1,498
EPS (adjusted)	9.13	9.33	6.34	10.86	12.51
DPS (adjusted)	1.00	1.50	0.95	1.63	1.88

Annex VI – Balance Sheet

LKR (Mn)	FY16	FY17	FY18E	FY19E	FY20E
Assets					
Non current assets					
PPE	3,466	3,348	3,263	3,182	3,104
Other non current assets	895	893	925	965	994
	4,362	4,240	4,188	4,147	4,098
Current Assets					
Inventories	3,987	4,363	6,251	7,793	8,954
Trade and other receivable	4,251	5,334	6,471	8,165	9,269
Other current assets	1,067	403	503	603	703
Cash and cash equivalents	1,707	2,225	2,137	1,477	1,898
	11,012	12,325	15,362	18,038	20,823
Total assets	15,374	16,565	19,550	22,185	24,920
Equity and liabilities					
Capital and reserves					
Stated capital	299	299	299	299	299
Retained Earnings	5,142	6,111	6,756	7,862	9,136
Other reserves	3,004	2,921	2,921	2,921	2,921
Total equity - equityholder	8,445	9,331	9,977	11,083	12,356
Non-controlling interest	1,026	1,135	1,229	1,390	1,575
	9,472	10,467	11,206	12,473	13,932
Non current Liabilities					
Borrowings	915	208	408	408	1,208
Other non current assets	463	510	510	510	510
	1,377	718	918	918	1,718
Current liabilities					
Trade and other payables	2,010	1,950	3,997	5,060	5,221
Other current liabilities	2,515	3,430	3,428	3,734	4,050
	4,525	5,381	7,425	8,794	9,270
Total equity and liabilities	15,374	16,565	19,550	22,185	24,920
NAVPS (adjusted)	70.50	77.90	83.29	92.52	103.15

Source: CSE, Company reports, FC Research Estimates

Research Disclosure

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First Capital

First Capital Holdings PLC

No. 02, Deal Place,
Colombo 03.

General: +94 11 2639 898
Fax: +94 11 5736 264

RESEARCH

Dimantha Mathew	+94 11 2639 853	Amanda Lokugamage	+94 11 2639 868
Atchuthan Srirangan	+94 11 2639 863	Nisansala Kuruppumudali	+94 11 2639 866
Hansinee Beddage	+94 11 2639 864		

GOVERNMENT SECURITIES SALES

Anjelo Simmons	+94 77 3031 636	Neminda Jayawardena	+94 76 6644 080
Anushka Dissanayake	+94 77 2220 021	Arun Kandasamy	+94 75 4861 506
Anushi Ranawaka	+94 77 3876 819		

CORPORATE DEBT SALES

Sewwandi Kathriarachchi	+94 77 3461 734	Naveen Samarasekera	+94 77 0073 684
Nethalie De Mel	+94 11 2639 854	Kemith De Zoysa	+94 77 2390 691

EQUITY SALES

CEO	Jaliya Wijeratne	+94 70 2910 042	Negombo	
			Priyanka Anuruddha	+94 70 2910 035
Colombo			Priyantha Wijesiri	+94 70 2910 036
Damian Le Grand		+94 70 2910 032		
Nishantha Mudalige		+94 70 2910 041		
Isuru Jayawardana		+94 70 2910 034		
Ifadh Marikar		+94 70 2910 033		
Thushara Pathiraja		+94 70 2910 037		
Anushka Buddhika		+94 70 2910 030		
Gamini Hettiarachchi		+94 70 2910 039		

UNIT TRUST SALES

Kosala Liyanagedara	+94 77 7230 788	Imali Abeygunawardena	+94 77 1764 799
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BRANCHES

Kandy	Kurunegala
2nd Floor, No.121 Kotugodella Veediya (E L Senanayake Veediya) Kandy	CSE - Kurunegala Branch, 1st Floor, Union Assurance Building, No 06, Rajapihilla Mawatha, Kurunegala 60000.

Manager:	Salinda Samarakoon	Manager:	Menaka Wavegedara
Tel:	+94 81 2236 010	Tel:	+94 37 2222 930

Matara	Negombo
2nd Floor, E.H. Cooray Building No: 24, 1/3, Anagarika Dharmapala Mawatha, Matara 81000.	No: 163B, Colombo Road, Negombo 11500 Negombo 11500.

Manager:	Rohana Jayakody	Manager:	Buddhika Edirisinghe
Tel:	+94 41 2222 988	Tel:	+94 31 4937 072

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