



TOKYO CEMENT COMPANY (LANKA) PLC [TKYO.N0000]

DOWNGRADE TO HOLD

COSTS HEADWINDS DENT MARGINS!!!

Fair Value: FY22E - LKR 85.0 [+20%] **FY23E - LKR 80.0 [+13%]**
Total Return with DPS: FY22E - 23% [AER 31%] *FY23E - 21% [AER 11%]*

TKYO recorded earnings of LKR 1.3Bn (+92%YoY) in 4QFY21, slightly performing above our expectations. However, earnings growth was primarily driven by the income tax reversal of LKR 572.0Mn recorded for the quarter relative to income tax expense of LKR 22.4Mn in 4QFY20. Revenue growth of 47.4%YoY to LKR 12.4Bn was offset by the dip in GP margins by 629bps to 24.4% and unprecedented surge in distribution expenses by 95%YoY to LKR 1.9Bn. However, finance cost reduction by 65.7%YoY to LKR 170.6Mn favourably impacted the bottom-line. We believe that rise in production and other costs amidst the currency depreciation to remain an overhang and accordingly, we downgrade our earnings outlook to LKR 4.7Bn for FY22E and LKR 4.5Bn for FY23E from previous forecast of LKR 5.6n for FY22E and LKR 5.5Bn for FY23E. We also downgrade TKYO's fair value to LKR 85.0 for FY22E and to LKR 80.0 for FY23E while estimating to provide an annualized return of 31% and 11% respectively.

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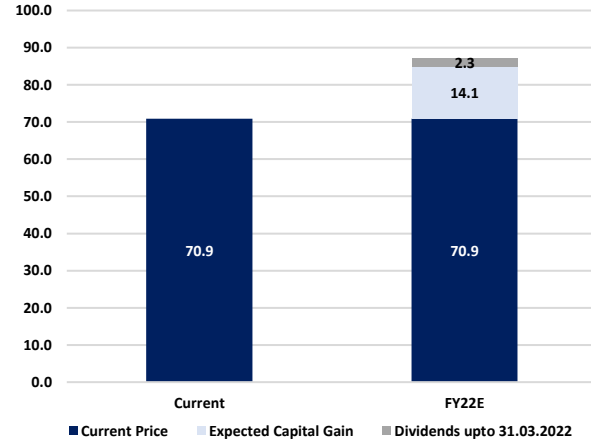
LKR (mn)	4QFY20	4QFY21	YoY	FY20	FY21	YoY
Earnings (LKR 'Mn)						
Revenue	8,385	12,356	+47%	35,768	42,946	+20%
Gross Profit	2,571	3,012	+17%	10,256	12,495	+22%
EBIT	1,203	904	-25%	4,494	6,301	+40%
PBT	729	747	+2%	2,629.5	5,221	+99%
Net Profit	685	1,316	+92%	2,297	5,425	+136%
Balance Sheet (LKR 'Mn)						
Shareholders' Equity	17,157	21,980	+28%	17,157	21,980	+28%
Borrowings	13,512	8,175	-39%	13,512	8,175	-39%
NAVPS	42.8	54.8		42.8	54.8	

Top line growth of 47%YoY for 4QFY21 amidst increase in local cement production

TKYO's revenue grew by 47%YoY as the company benefitted from a stronger rebound in housing and construction activities in the 4QFY21 which made the company to add more heft to its production. In the midst of low interest rate environment, local cement production continued to grow recording a growth of 29%YoY during 4QFY21 while imports continued to decline with a 22%YoY dip due to higher tax. We expect TKYO's market share to further improve with the grasp of volumes from importers as the new CESS tax for importers places local manufactures in an advantageous position in terms of the price. However, high competition among local manufacturers may prevent any major price change despite the impact from currency depreciation. With the demand for cement mainly arising from the residential sector amidst the low interest rate environment, and increasing market share of local cement manufacturers, we expect TKYO's revenue to grow by 20%YoY in FY22E and by 7% in FY23E respectively. We also believe that TKYO's new capacity addition of 1Mn MT from the new plant to be completed by 2HFY23 and to contribute to revenue from there onwards.

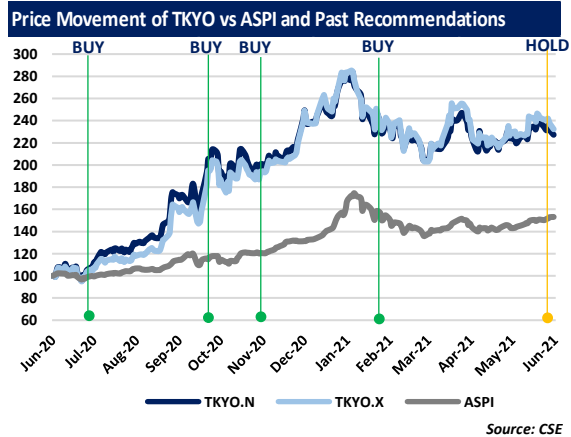
Bottom line compressed with increased COS and two-fold growth in distribution expenses

Despite the strong top line growth, the company's profits at operating level fell by 25% to LKR 904.0Mn due to the surge in cost of sales by 61%YoY and the distribution expenses which nearly doubled from the corresponding period last year. This resulted in GP margins declining by 629 bps to 24.4% and EBIT margins dipping by 703bps to 7.0% in 4QFY21. However, TKYO's finance cost reduction by 66%YoY within the low interest rate environment and settlement of sizeable portion of borrowings amounting to LKR 5.3Bn during the year aided in improving the bottom line. We estimate that expected currency depreciation (12% for 2021 and 6% for 2022) to increase the costs as TKYO is import dependant for clinker. However, focus on the BHC (Blended Hydraulic Cement) is expected to eliminate the exchange risk as it mainly uses fly ash as a key raw material which can be sourced locally. We expect bottom line to record LKR 4.7Bn (-13%YoY) in FY22E and LKR



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Minimum Return for BUY:

Buy Below for FY22E [AER of 10.1% with DPS]: LKR 81.0
 TKYO.N categorized as 'Grade A' counter

Disclosure on Shareholding:

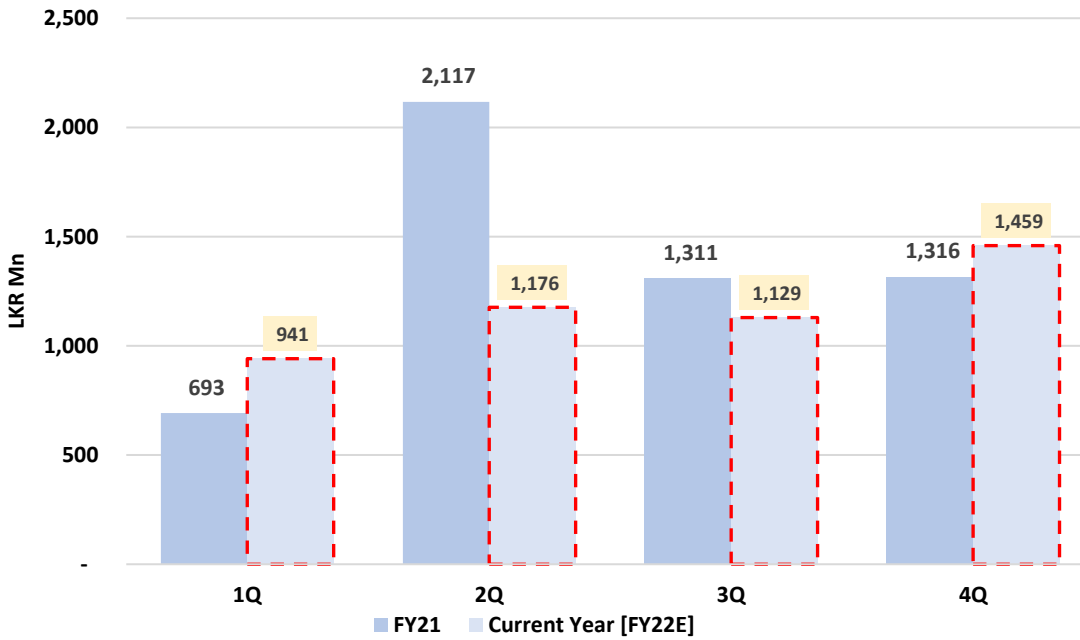
First Capital Group or the covering analyst did not hold 1% or more of the total outstanding share capital of TKYO.N and TKYO.X during the five trading days prior to the issuance of this document.

4.5Bn (-5%YoY) in FY23E with the currency depreciation given that there will be no price hikes due to competition.

TKYO price is downgraded to LKR 85.0 for FY22E and LKR 80.0 for FY23E - DOWNGRADE TO HOLD

With downgraded earnings of LKR 4.7Bn for FY22E (-13%YoY) and LKR 4.5Bn (-5%YoY) in FY23E, we downgrade TP for FY22E to LKR 85.0 and to LKR 80.0 for FY23E. TKYO is expected to provide an annualised return of 31% for FY22E and 11% for FY23E at the current market

Quarterly Earnings Forecast for FY22E



Estimate Revision

In LKR Mn	FY22E - O	FY22E - R	% Change	FY23E - O	FY23E - R	% Change
Earnings Estimate						
Revenue	46,118	51,450	+12%	44,237	55,039	+24%
Gross Profit	14,557	13,871	-5%	13,933	14,050	+1%
EBIT	8,192	6,565	-20%	7,829	6,290	-20%
PBT	6,862	5,670	-17%	6,749	5,364	-21%
Net Profit	5,627	4,706	-16%	5,534	4,452	-20%
EPS	14.0	11.7	-16%	13.8	11.1	-20%
Growth YoY	13%	-13%		-2%	-5%	
Balance Sheet Estimate						
Borrowings	8,195	8,865	+8%	6,312	7,097	+12%
Shareholders' Equity	25,883	25,275	-2%	29,954	28,504	-5%
NAVPS	64.6	63.0		74.7	71.1	
Ratio Estimate						
ROE (%)	23.7%	19.9%		19.8%	16.6%	
PER (x)	5.27	6.0		5.40	6.4	
PBV (x)	1.15	1.1		1.00	1.0	

Valuation Table

P/E 31 March	FY18	FY19	FY20	FY21	FY22E	FY23E	FY24E
Estimates (LKR 'Mn)							
Revenue	35,633	38,496	35,768	42,946	51,450	55,039	59,323
Gross Profit	8,472	7,888	10,256	12,495	13,871	14,050	14,278
EBIT	3,481	1,807	4,494	6,301	6,565	6,290	6,032
Net Profit	2,343	(492)	2,318	5,425	4,706	4,452	4,270
EPS (LKR)	5.8	(1.2)	5.8	13.5	11.7	11.1	10.6
YoY Growth (%)	-31%	-121%	371%	134%	-13%	-5%	-4%
DPS	1.3	0.3	1.5	3.5	3.1	2.9	2.8
Valuations							
PER (x)	12.1x	-57.7x	12.3x	5.2x	6.0x	6.4x	6.7x
PBV (x)	1.8x	1.9x	1.7x	1.3x	1.1x	1.0x	0.9x
DY (%)	1.8%	0.4%	2.1%	5.0%	4.3%	4.1%	3.9%

Valuation Summary

Expected TKYO.N price	FY22E	FY23E	Return	FY22E	FY23E
DCF Valuation based target price	89.4	83.2	Target Price	85.0	80.0
PER Valuation based target price	82.2	77.7	Current Price	70.9	70.9
Average Target Price	85.8	80.5	Capital Gain (LKR)	14.1	9.1
Target Price after Rounding off	85.0	80.0	Dividends upto 31.03.2022 and 31.03.2023	2.3	5.3
			Capital Gain %	20%	13%
			Dividend Yield %	3%	8%
			Total Return %	23%	21%
			Annualized Return %	31%	11%
Expected TKYO.X price	FY22E	FY23E			
Target Price for TKYO.N	85.0	80.0			
Average 12 month discount	14%	14%			
Target Price for TKYO.X	72.9	68.6			
Target Price after Rounding off	73.0	69.0			

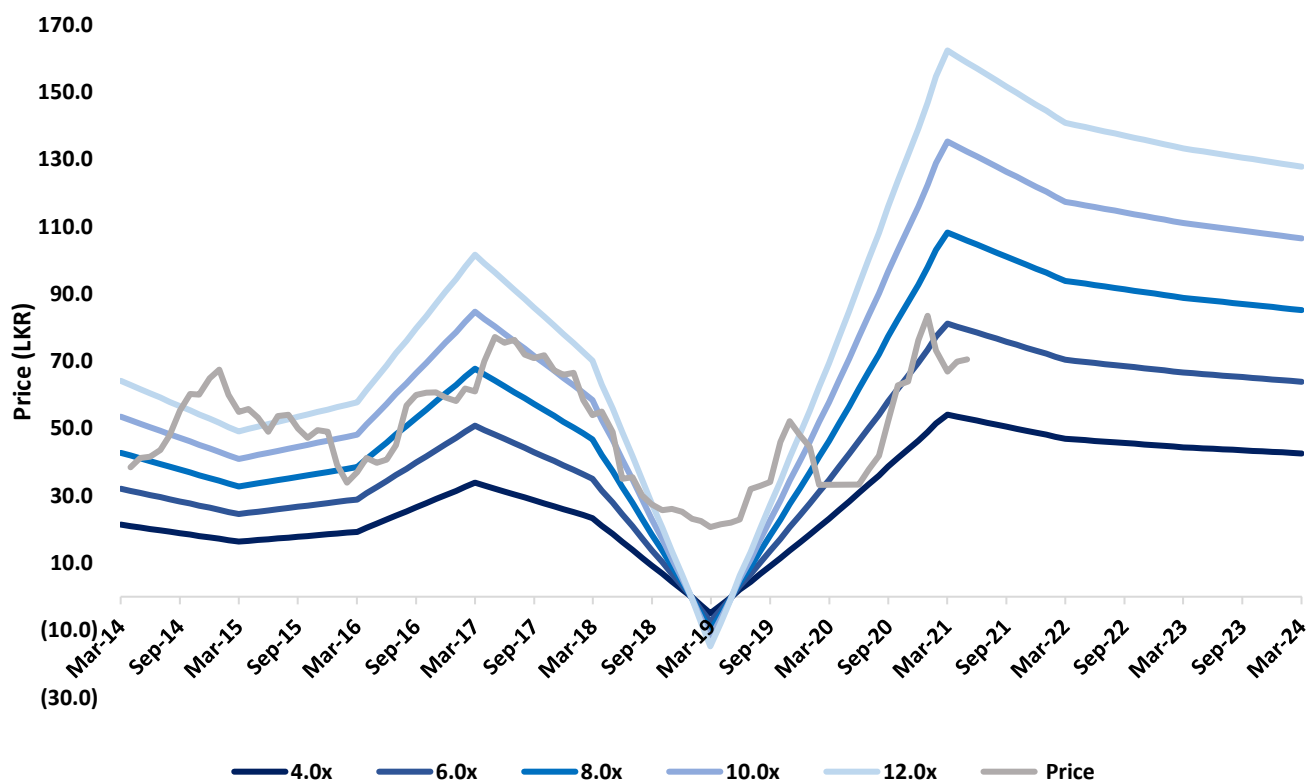
Discounted Cash flow Valuation

DCF based Valuation	FY22E	FY23E
Enterprise Value	43,052	38,509
Debt (-)	8,865	7,097
Cash (+)	1,644	1,962
Total Value of Equity	35,831	33,374
No. of Shares (Mn)	401	401
Target Price	89.4	83.2

WACC	FY22E	FY23E
Ke	20.6%	21.1%
Kd	10.0%	11.0%
D/E Assumption	40/60	40/60
Terminal Growth (%)	3.0%	3.0%
WACC	16.4%	17.1%

COE	FY22E	FY23E
Rf	7.0%	7.5%
Rm	15.0%	15.5%
Growth %	3.0%	3.0%
β	1.70	1.70
$Ke=Rf+\beta(Rm-Rf)$	20.6%	21.1%

PER Valuation



Source : CSE, Company Annual Reports and First Capital Research Estimates

PER based Valuation	FY22E	FY23E
Earnings (LKR 'Mn)	4,706	4,452
No. of Shares ('Mn)	401	401
EPS	11.74	11.10
Expected PER	7.0x	7.0x
Price at 7.0x Earnings	82.2	77.7

Appendix I: Statement of Income and Expenses

Statement of Financial Performance (LKR Mn) P/E 31st Mar	FY18	FY19	FY20	FY21	FY22E	FY23E	FY23E
Revenue	35,633	38,496	35,768	42,946	51,450	55,039	59,323
Cost of Sales	27,161	30,608	25,512	30,451	37,579	40,989	45,045
Gross Profit	8,472	7,888	10,256	12,495	13,871	14,050	14,278
Other Income	263	20	19	49	51	55	59
Total Operating Income	8,735	7,909	10,275	12,544	13,922	14,105	14,337
Distribution Cost	3,623	3,939	4,099	5,075	6,020	6,440	6,941
Administrative Expenses	1,631	1,782	1,682	1,168	1,338	1,376	1,364
Total Operating Expenses	5,254	6,102	5,781	6,243	7,357	7,816	8,305
Operating Profit	3,481	1,807	4,494	6,301	6,565	6,290	6,032
Finance Cost	967	1,819	1,888	1,115	896	926	888
Finance Income	58	11	23	36	0	0	0
Profit Before Taxation	2,572	(1)	2,629	5,221	5,670	5,364	5,145
Income Tax Expenses/(Income)	243	475	312	(187)	964	912	875
Profit for the Year	2,329	(476)	2,318	5,408	4,706	4,452	4,270
Minority Interest	(15)	16	0	-	-	-	-
Profit attributable to Equity Holders	2,343	(492)	2,318	5,408	4,706	4,452	4,270
EPS	5.8	-1.2	5.8	13.5	11.7	11.1	10.6

Appendix II: Statement of Financial Position

Statement of Financial Position (LKR Mn) as at 31st Mar	FY18	FY19	FY20	FY21	FY22E	FY23E	FY23E
Assets							
Property, Plant & Equipment	23,820	26,877	26,949	28,249	28,235	28,276	28,370
Capital Work-in-Progress	2,953	749	545	-	-	-	-
Inventories	2,530	3,636	3,493	3,236	3,993	4,355	4,786
Trade and other Receivables	4,177	5,993	4,985	4,613	4,939	5,917	6,329
Tax Receivable	310	310	298	-	-	-	-
Other Assets	59	123	102	84	84	84	84
Cash and Cash Equivalents	718	341	430	1,489	1,644	1,962	4,148
Total Assets	35,002	38,461	38,148	39,072	40,296	41,995	45,118
Liabilities							
Interest Bearing Borrowings	12,957	14,065	13,512	8,175	8,865	7,097	6,823
Current and Deferred Tax	2,544	2,726	2,859	2,273	2,273	2,273	2,273
Trade & Other Payables	2,639	4,813	2,507	5,391	2,631	2,869	3,153
Retirement Benefits Obligation	182	225	297	359	359	359	359
Bank Overdrafts	1,181	1,589	1,388	437	437	437	437
Other liabilities	7	27	336	393	393	393	393
Total Liabilities	19,511	23,445	20,899	17,028	14,957	13,427	13,438
Shareholders Funds							
Stated Capital	4,240	4,240	4,240	4,240	4,240	4,240	4,240
Retained Earnings	11,189	10,683	12,917	17,740	21,036	24,264	27,377
Equity Attributed to Equity Holders of the Comp	15,429	14,922	17,157	21,980	25,275	28,504	31,616
Non - controlling interest	62	94	93	64	64	64	64
Total Liabilities & Shareholders' Funds	35,002	38,461	38,148	39,072	40,296	41,995	45,118
NAVPS	38.5	37.2	42.8	54.8	63.0	71.1	78.9



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