



TEEJAY LANKA PLC [TJL.N0000]

MAINTAIN BUY

"SAILING THE WAVES AMIDST SLUGGLISH DEMAND"

Fair Value: FY24E - LKR 40.0 [+18%]

Total Return with DPS: FY24E - 20% [AER 30%]

FY25E - LKR 50.0 [+47%]

FY25E - 50% [AER 27%]

TJL recorded a net profit of LKR 152.4Mn (-81.6%YoY) in 4QFY23, surpassing expectations despite a steep decline in volume as retail sales in key markets remained sluggish due to changing consumer buying patterns. Accordingly, the top-line reported a degrowth of 4.7%QoQ and improved on a YoY basis by 28.5% aided by LKR devaluation and a rise in average selling prices (ASP). However, increased domestic costs, deferred tax provisioning and higher taxes (14% to 30% w.e.f 1st Oct 2022), adversely affected the margins and profitability during the quarter. Despite a decline in overall volume, the synthetic fabric segment witnessed a notable growth during the quarter where revenue from the segment increased by 130.0%YoY largely supported by the capacity expansion in TJL India. We expect market softness to persist during the next few quarters and this trend might continue mainly in the US and UK markets for 6 to 9 months. However, market softness is expected to gradually improve from 2HFY24E as brands have cleared out inventories and consumer demand may start to pick up when market condition improves. However, considering the inflated cost pressure, subdued demand and higher tax impact, we have downgraded the earnings for FY24E to LKR 2.2Bn while earnings for FY25E is estimated at LKR 2.6Bn. Hence, in line with the revision of earnings, we have revised the FV to LKR 40.0 for FY24E (previous LKR 60.0) while FY25E fair value is estimated at LKR 50.0. **MAINTAIN BUY**

LKR (Mn)	4QFY22	4QFY23	YoY	FY22	FY23	YoY
Earnings (LKR 'Mn)						
Revenue	13,465	17,301	+28%	49,588	84,059	+70%
Gross profit	1,093	1,186	+8%	4,578	6,367	+39%
EBIT	716	773	+8%	2,573	3,276	+27%
PBT	892	409	-54%	2,864	3,111	+9%
Net Profit	826	152	-82%	2,531	2,127	-16%
Balance Sheet (LKR 'Mn)						
Shareholders' Equity	28,226	32,043	+14%	28,226	32,043	+14%
Borrowings	11,495	12,587	+9%	11,495	12,587	+9%
NAVPS	39.4	44.7		39.4	44.7	

QoQ top-line continues to decline whilst YoY records a 28.5% uptick

TJL's revenue declined by 4.7%QoQ to LKR 17.3Bn in 4QFY23, marking the second consecutive quarter of top-line decline. However, on a YoY basis, the revenue witnessed a growth of 28.5% in LKR terms, primarily due to currency depreciation (+58.0%YoY) and increased ASP (+29.0%YoY). Notably, the USD denominated top-line experienced a steep decline of 29.6% YoY to USD 47.8Mn. Degrowth in topline was mainly driven by a significant dip in volume by 30.0%YoY amidst high inventory levels held by TJL brands and the softening of orders in international markets primarily across the US and Europe which accounts for c.60.0% and 40.0% of TJL's topline, respectively. As a result, TJL's plants operated below capacity at 62.0% during the quarter cf. 55.0% capacity in 3QFY23. Due to consecutive declines in the order book and decelerating volumes, the TJL group faced a challenging environment. This was in line with decreased global consumer spending on fashion products, which was estimated to decrease by 41.0% during 1H2023, as indicated by the PwC Global Consumer Insights Pulse Survey. This decline was attributed to inflationary pressures and a cautious approach towards future spending, although there still exists some appetite for future expenditure. Accordingly, we have revised our topline forecast for FY24E to LKR 90.4Bn. TJL also capitalized on stabilized cotton prices during 4QFY23 to capture volume businesses and utilize open capacities for price-sensitive programs. This led to a significant increase in other operating income which was positively correlated to trade price hikes and higher prices of by-products. TJL currently expects price reductions driven by seasonal factors and permit reductions during the next few quarters which is expected to reduce its ASP and increase volumes in the forthcoming quarters.

Capacity underutilization weighs down on GP and OP margins

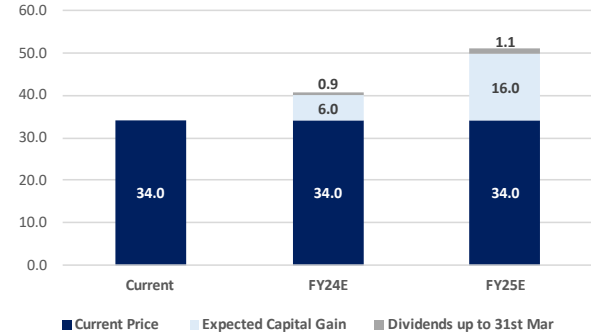
TJL's GP margin deteriorated by 120bps YoY and increased by 190bps QoQ to reach 6.9% in 4QFY23. This was influenced by the rise in depreciation and fixed costs due to capacity expansion in TJL India. Notably, the total capacity utilized was only 100 tonnes per day in India and Sri Lanka, while the actual capacity remained at 320 tonnes per day. Utilization rates are expected to be at similar levels for the forthcoming quarter, with improvements anticipated in 2QFY24E. Nevertheless, even with the anticipated recovery in consumer demand in 2HFY24E which could lead to an expansion in the order book, we project the GP margin to stabilize at 7.0% in FY24E. Looking ahead to FY25E, we expect a gradual recovery, with the GP margin forecasted to reach 7.5%. Although we expect a slowdown in 1HFY24E due to the negative impact on the order book, TJL has managed to onboard multiple bulk orders from top brands such as Lacoste and Walmart to expand its volume businesses, which might contribute to its topline in 1HFY24E. In 4QFY23, volume businesses accounted for 13% of TJL's total revenue.

Strengthening presence in Bangladesh mainly on synthetics space to increase margins

TJL anticipates a potential increase in revenue during FY24E, as it plans to expand its Fleece capacity and convert 30% of its total production capacity to synthetic (currently stands at 15%). TJL also aims to develop its synthetic business in Bangladesh, which is expected to increase the company's market share and topline in FY24E. TJL expects orders in Bangladesh to be placed in 1QFY24 and plans to enter the Indian domestic market once they obtain ETA approval. TJL also revealed future plans to convert some of its outsourced knitting and finishing facilities to TJL Lanka for fleece and polo ranges. In India, the company already possesses fleece capabilities and aims to implement similar operations in Lanka, potentially utilizing one of the existing outsourcing facilities. This is expected to increase economies of scale which will bring down its economic costs and increase margins.

FV for FY24E revised down to LKR 40.0 from LKR 60.0

Considering the tax impact and depressed consumer demand, we have downgraded TJL's earnings for FY24E to LKR 2.2Bn while earnings for FY25E is estimated at LKR 2.6Bn. Hence, on the back of slower than expected growth in earnings, we revise our FV to LKR 40.0 for FY24E providing an annualized return of 30.0% at the current price level of LKR 34.0. **MAINTAIN BUY**



FIRST CAPITAL RESEARCH

Vinodhini Rajapopathy +94 11 263 9866

vinodhini@firstcapital.lk

Price Movement of TJL vs ASPI (Indexed and rebased to 100)



Source: CSE

Minimum Return for BUY:

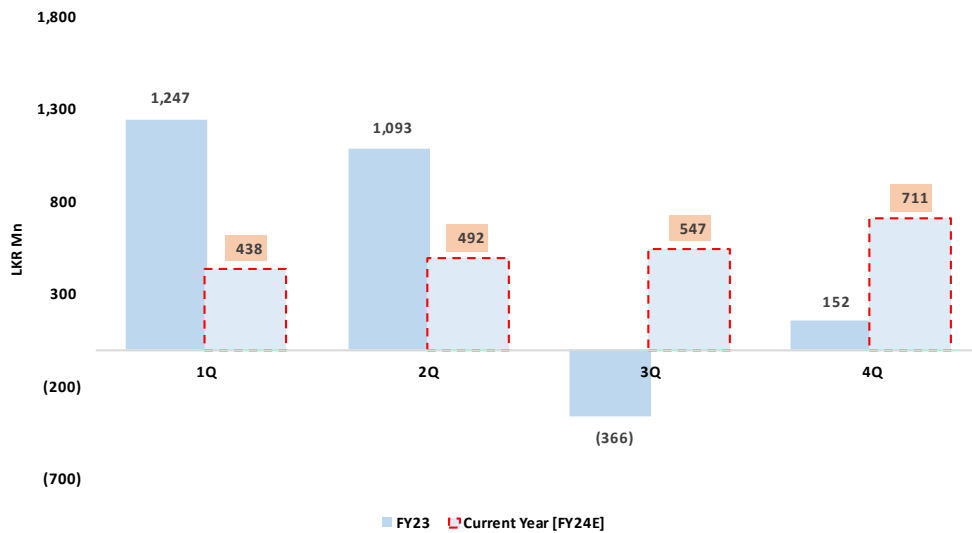
Buy Below for FY24E [AER of 23.0% with DPS]: LKR 34.4
TJL.N categorized as 'Grade B' counter

Disclosure on Shareholding:

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



Quarterly Earnings



Estimate Revision

In LKR Mn	FY24E - O	FY24E - R	% Change	FY25E - O	FY25E - R	% Change
Earnings Estimate						
Revenue	98,476	90,417	-8%	112,364	93,682	-17%
Gross profit	7,681	6,329	-18%	10,337	7,026	-32%
EBIT	3,939	3,165	-20%	6,124	3,747	-39%
Profit before tax	3,811	3,201	-16%	5,992	3,743	-38%
Net Profit	2,668	2,188	-18%	4,195	2,559	-39%
EPS	3.7	3.1		5.9	3.6	
Growth YoY	46%	6%		57%		
Balance Sheet Estimate						
Shareholders' Equity	35,222	33,575	-5%	36,691	35,366	+4%
Borrowings	11,478	13,788	+20%	9,795	14,962	+53%
NAVPS	49.1	46.8		51.2	49.3	
Ratio Estimate						
ROE (%)	7.7%	6.7%		11.7%	7.4%	
PER (x)	5.0	11.1		6.1	9.5	
PBV (x)	0.7	0.7		0.7	0.7	

Valuation Table

P/E 31 March	FY19	FY20	FY21	FY22	FY23	FY24E	FY25E	FY26E
Estimates (LKR 'Mn)								
Revenue	31,747	33,277	31,780	49,588	84,059	90,417	93,682	97,047
Gross profit	3,686	4,229	3,790	4,578	6,367	6,329	7,026	7,764
EBIT	2,345	2,728	2,441	2,573	3,276	3,165	3,747	4,367
Net Profit	1,859	2,384	2,140	2,531	2,127	2,188	2,559	2,929
Adjusted EPS (LKR)	2.6	3.3	3.0	3.5	3.0	3.1	3.6	4.1
YoY Growth (%)	16%	28%	-10%	18%	-16%	3%	17%	14%
Valuations								
PER (x)	13.1x	10.2x	11.4x	9.6x	11.5x	11.1x	9.5x	8.3x
PBV (x)	1.7x	1.6x	1.4x	0.9x	0.8x	0.7x	0.7x	0.7x
DY (%)	5.7%	3.8%	8.2%	6.9%	2.2%	2.7%	3.1%	4.8%
NAVPS	19.4	21.8	24.8	39.4	44.7	46.8	49.3	51.8
DPS (LKR)	2.0	1.3	2.8	2.4	0.8	0.9	1.1	1.6
Dividend Payout	75%	39%	94%	67%	25%	30%	30%	40%



Valuation Summary

Expected TJL price	FY24E	FY25E
PER Valuation based target price	42.7	53.5
DCF Valuation based target price	38.6	47.1
Average Target Price	40.7	50.3
Target Price after Rounding off	40.0	50.0

Return	FY24E	FY25E
Target Price	40.0	50.0
Current Price	34.0	34.0
Capital Gain (LKR)	6.0	16.0
Dividends up to 31st March	0.9	1.1
Capital Gain %	18%	47%
Dividend Yield %	3%	3%
Total Return %	20%	50%
Annualized Return %	30%	27%

Discounted Cash flow Valuation

DCF based Valuation	FY24E	FY25E
Enterprise Value	31,639	39,075
(-) Debt	(13,788)	(14,962)
(+) Cash	9,828	9,660
Total Value of Equity	27,680	33,774
No. of Shares (Mn)	717	717
Target Price	38.6	47.1

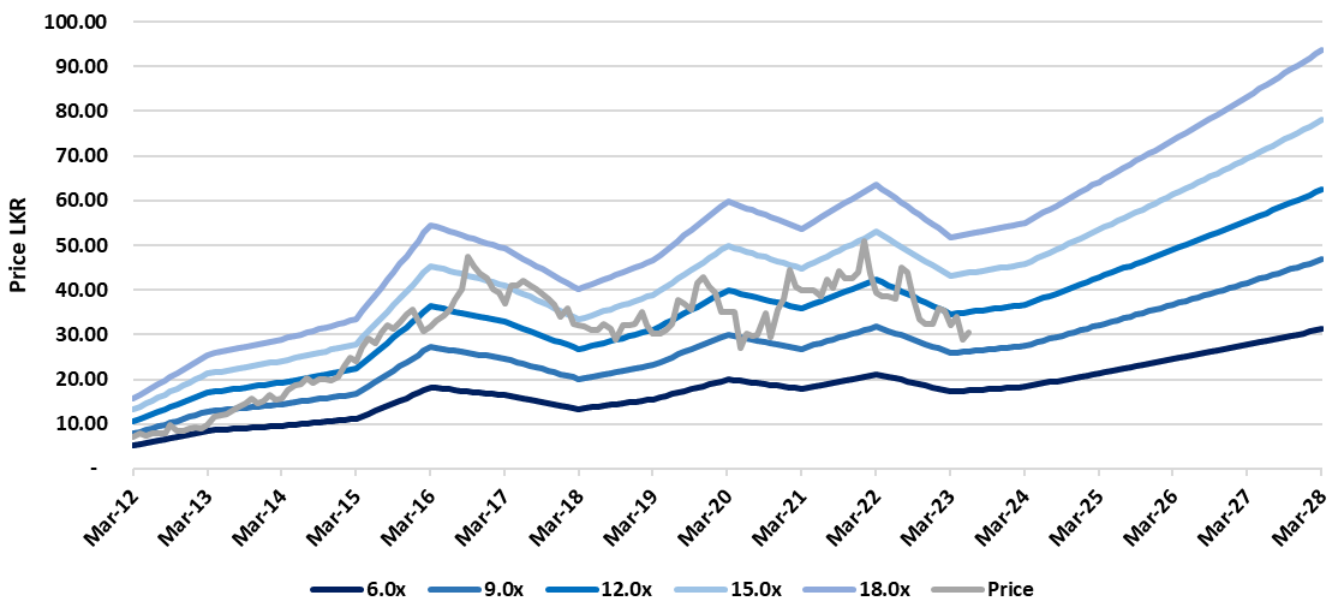
COE	FY24E	FY25E
Rf	15.0%	12.0%
Rm	23.0%	20.0%
Growth %	3.0%	3.0%
β	0.80	0.80
$Ke = Rf + \beta(Rm - Rf)$	21.4%	18.4%

PER Valuation

PER based Valuation	FY24E	FY25E
Earnings (LKR 'Mn)	2,188	2,559
No. of Shares ('Mn)	717	717
EPS	3.1	3.6
Expected PER	14.0x	15.0x
Target Price	42.7	53.5

WACC	FY24E	FY25E
Ke	21.4%	18.4%
Kd	17.0%	15.0%
D/E Assumption	40/60	40/60
Terminal Growth (%)	3.0%	3.0%
WACC	17.6%	15.2%

PER Chart





Appendix I: Statement of Income and Expenses

Statement of Profit or Loss (LKR Mn)	FY19	FY20	FY21	FY22	FY23	FY24E	FY25E	FY26E
As at 31st March								
Revenue	31,747	33,277	31,780	49,588	84,059	90,417	93,682	97,047
Cost of sales	-28,061	-29,048	-27,990	-45,010	-77,692	-84,088	-86,656	-89,283
Gross profit	3,686	4,229	3,790	4,578	6,367	6,329	7,026	7,764
Other income	246	173	186	151	532	723	749	776
Selling, Distribution & Admin expenses	-1,587	-1,673	-1,534	-2,156	-3,623	-3,888	-4,028	-4,173
Operating profit	2,345	2,728	2,441	2,573	3,276	3,165	3,747	4,367
Finance Income	102	244	277	440	811	800	695	604
Less : Finance Cost	-189	-160	-119	-149	-976	-764	-700	-687
Net finance income	-88	84	158	291	-164	36	-4	-82
Profit before tax	2,257	2,812	2,599	2,864	3,111	3,201	3,743	4,285
Income tax expense	-398	-428	-460	-332	-984	-1,013	-1,184	-1,356
Profit for the Year	1,859	2,384	2,140	2,531	2,127	2,188	2,559	2,929
EPS	2.6	3.3	3.0	3.5	2.9	3.1	3.6	4.1

Appendix II: Statement of Financial Position

Statement of Financial Position (LKR Mn)	FY19	FY20	FY21	FY22	FY23	FY24E	FY25E	FY26E
As at 31st March								
ASSETS								
Non-Current Assets								
Property, plant and equipment	8,408	8,777	8,711	14,715	20,259	19,017	17,974	17,099
Capital work-in-progress	119	590	425	5,269	1,734	2,734	3,734	4,734
Intangible Assets	94	78	125	143	161	107	68	39
Deferred tax assets	111	256	273	432	1,816	1,816	1,816	1,816
Goodwill	58	62	66	96	106	95	86	77
Right-of-use assets	236	910	899	1,341	1,740	1,740	1,740	1,740
Total Non-Current Assets	9,026	10,673	10,500	21,996	25,816	25,510	25,419	25,506
Current Assets								
Inventories	4,494	5,904	7,281	16,356	13,368	16,102	19,250	19,941
Trade and other receivables	4,013	4,137	7,181	13,336	8,499	11,147	12,833	13,294
Current Tax Receivable	9	18	6	0	0	0	0	0
Cash and cash equivalents	4,290	5,263	4,452	6,383	7,907	9,828	9,660	12,763
Other Financial Assets	553	967	1,680	1,822	3,281	3,445	3,445	3,445
Total Current Assets	13,359	16,289	20,600	37,897	33,055	40,523	45,189	49,444
Total Assets	22,386	26,962	31,099	59,894	58,871	66,033	70,607	74,950
EQUITY AND LIABILITIES								
Capital and Reserves								
Stated capital	4,057	4,057	4,249	4,442	4,442	4,442	4,442	4,442
Exchange equalisation reserve	4,172	5,263	6,225	15,220	18,048	18,048	18,048	18,048
Retained earnings	5,600	6,232	7,137	8,410	9,400	10,932	12,723	14,480
Share option scheme	97	97	153	153	153	153	153	153
Total Equity	13,925	15,649	17,764	28,226	32,043	33,575	35,366	37,123
Non-Current Liabilities								
Borrowings	801	412	198	5,581	6,239	6,974	7,671	8,055
Lease Liability	0	628	655	930	1,330	1,330	1,330	1,330
Deferred tax liabilities	538	648	627	919	2,324	2,324	2,324	2,324
Retirement benefit obligations	252	378	520	425	569	569	569	569
Total Non-Current Liabilities	1,591	2,065	2,000	7,855	10,461	11,196	11,894	12,277
Current Liabilities								
Trade and other payables	4,703	5,643	8,087	17,623	9,393	13,823	15,432	17,123
Borrowings	2,167	3,502	3,108	5,914	6,348	6,814	7,291	7,802
Current tax liability	0	92	126	233	500	500	500	500
Lease Liability	0	12	14	43	125	125	125	125
Total Current Liabilities	6,869	9,248	11,335	23,813	16,366	21,262	23,348	25,549
Total Equity & Liabilities	22,386	26,962	31,099	59,894	58,871	66,033	70,607	74,950
Adjusted NAVPS	19.4	21.8	24.8	39.4	44.7	46.8	49.3	51.8



First Capital

First Capital Holdings PLC

No.2, Deal Place,
Colombo 3

Tel: +94 11 2145 000
Fax: +94 11 2145 050

RESEARCH

Dimantha Mathew	+94 11 2639 853	Tharusha Ashokgar	+94 11 2639 866
Ranjan Ranatunga	+94 11 2639 863	Zaeema Jihan	+94 11 2639 863
Vinodhini Rajapoopathy	+94 11 2639 866	Nethmi Fernando	+94 11 2639 863

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

Tharusha Ekanayake	+ 94 77 7 809 154
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EQUITY SALES

CEO	Jaliya Wijeratne	+94 70 2910 042
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Colombo

Rasika Indra Kumara	+94 77 7072 698	Anjelo LaBrooy	+94 77 7546 645
Isuru Jayawardena	+94 76 7084 953	Dillon Lowe	+94 76 616 0647
Nishantha Mudalige	+94 70 2910 041	Evelyn John	+94 77 779 2452
Anushka Buddhika	+94 71 4310 600	Yudheshan Kannadasan	+94 77 415 5809
Thushara Pathiraja	+94 70 2910 037		

Negombo

Priyanka Anuruddha	+94 70 2910 035	Priyantha Wijesiri	+94 70 2910 036
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UNIT TRUST SALES

Kavin Karunamoorthy	+94 77 0328 060	Imali Abeygunawardena	+94 77 1764 799
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BRANCHES

Kandy	Kurunegala	Matara	Negombo
CSE Branch Office, No. 88, Dalada Veediya, Kandy 20000.	No.174/B2, Negombo Road, Kurunegala. Kurunegala 60000.	CSE Branch Office, 1st Floor, E.H.Cooray Tower, No.24, Anagarika Dharmapala Mawatha, Matara 81000.	Colombo Stock Exchange Negombo Branch Office, No. 72 A, 2/1, Old Chilaw Road, Negombo 11500.
Manager: Salinda Samarakoon	Manager:	Manager: Rohana Jayakody	Manager:
Tel: +94 81 2236 010	Tel: +94 37 2222 930	Tel: +94 41 2222 988	Tel: +94 31 4937 072

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