



## TEEJAY LANKA PLC [TJL.N0000]

## MAINTAIN BUY

## “THE COST-CONSCIOUS COMEBACK IGNITES MARGINS”

Fair Value: FY24E - LKR 40.0 [+16%]

Total Return with DPS: FY24E - 20% [AER 66%]

FY25E - LKR 50.0 [+45%]

FY25E - 50% [AER 35%]

TJL notched up a profit of LKR 943.0Mn, experiencing a modest 13.8%YoY decrease but a significant 210.5%QoQ surge in 2QFY24. This notable performance converted the previous quarter's loss of LKR 853.0Mn into an almost LKR 1.0Bn gain, surpassing expectations against a backdrop of stabilizing raw material costs and optimized inventory levels. The losses incurred in 1QFY24 were recouped during TJL's 1H, with revenue exceeding the Group's breakeven point. Furthermore, the top-line demonstrated a commendable 11.1%QoQ growth, marking a reversal from three consecutive quarters of top-line decline. TJL's 2QFY24 showcased a resurgence in the top-line, attributed to a multifaceted approach encompassing strategies to enhance the sales mix, optimize operational efficiencies, and expand into new markets. The company's forward-looking initiatives in synthetic capacities, digital brand segments, and market expansion aim to solidify its position amid market challenges, paving the way for sustained growth in the upcoming quarters. With the resurgence in consumer demand due to moderate inflation levels, we have upgraded the earnings outlook for FY24E to LKR 2.2Bn, while earnings for FY25E are estimated at LKR 2.4Bn. Hence, we maintain a FV of LKR 40.0 for FY24E and an FV of LKR 50.0 for FY25E. **MAINTAIN BUY**

LKR (Mn)	2QFY23	2QFY24	YoY	1HFY23	1HFY24	YoY
<b>Earnings (LKR 'Mn)</b>						
Revenue	24,753	15,550	-37%	48,611	29,547	-39%
Gross profit	2,160	1,891	-12%	4,281	2,174	-49%
EBIT	1,265	1,217	-4%	2,380	635	-73%
PBT	1,221	1,224	+0%	2,727	523	-81%
Net Profit	1,093	943	-14%	2,340	90	-96%
<b>Balance Sheet (LKR 'Mn)</b>						
Shareholders' Equity	36,497	31,606	-13%	36,497	31,606	-13%
Borrowings	30,534	26,867	-12%	30,534	26,867	-12%
NAVPS	50.9	44.1		50.9	44.1	

## 2QFY24 breaks three consecutive quarters of top-line decline

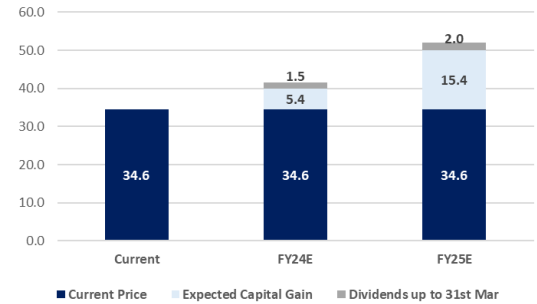
In 2QFY24, TJL observed a 11.1%QoQ increase in revenue, reaching LKR 15.5Bn, marking a reversal from three consecutive quarters of top-line decline. However, on a YoY basis, revenue experienced a substantial 37.2% decrease in LKR terms. This decline was primarily influenced by various factors including a reduction in volumes by 11.0% driven by current market conditions, a decrease in average selling prices (ASPs) by 7.0% (-40.0%YoY) predominantly due to falling yarn prices, 9.0% impact from LKR appreciation, and underutilization of capacity. TJL operated below capacity at 65.0% during 2QFY24 cf. 60.0% capacity in 1QFY24. Within this, TJL Lanka ran at over 80.0% capacity, whilst TJL India and Prince maintained levels between 50.0%-60.0%. Looking ahead to Q3 and Q4, TJL aims to enhance its capacity utilization rates which may expand its margins. Notably, the USD-denominated revenue also saw a sharp decline of 28.2%YoY, totaling USD 49.7Mn. The QoQ surge in top-line growth was largely attributed to increased sales, particularly driven by increased demand for high-end margin products, which were predominantly generated from gradually accumulating volumes throughout the quarter. During Q2, TJL also experienced an improved sales mix and enhanced margins owing to a gradual pickup across all its strategic brands, which helped to clear out a significant portion of its previously stagnant inventory. We anticipate that TJL's margins may improve in the forthcoming quarters with increased sales supported by the anticipated global decline in headline inflation from 8.7% in 2022 to 7.0% in 2023, attributed to lower commodity prices, as indicated by the IMF. Additionally, the upcoming holiday and winter season may contribute to an uptick in demand for apparel. Accordingly, we have estimated the topline for FY24E to be LKR 62.2Bn.

## GP margin surges amid stable cotton prices and optimized inventories

In terms of GP margin, 2QFY24 witnessed a significant uptick of 1014bps QoQ, with the margin settling at 12.2%. This substantial QoQ growth was a result of TJL effectively utilizing a significant portion of previously idle inventories during the quarter. Furthermore, factors including stable cotton prices, reduced wastage, and other operational cost improvements also played a vital role in boosting the GP margin during this period. Currently, yarn prices remain stable, and with the release of the new Indian crop into the market in Q3, TJL expects a slight decline in prices in the upcoming quarters due to increased supply. With the decline in yarn prices and the concurrent reductions in furnace oil and energy prices, TJL anticipates achieving higher margins around 9.0%-10.0% in both Q3 and Q4. Additionally, once their plants are fully optimized, they expect margins to reach 11.0%-12.0%. However, TJL is expecting a positive trend in the upcoming quarters as there is an emergence of demand volatility, and we expect the GP margin to stabilize at 10.0% in FY24E. Looking ahead to FY25E, we envisage the GP margin to be stagnant, hovering around the same level. The company has also reduced borrowings by 12.0%YoY to LKR 26.9Bn, offsetting debt through reduced inventory and working capital.

## TJL's European surge and US woes

TJL experienced heightened sales in Q2, driven by robust growth in the European market, which constitutes half of its market presence. The EU market exhibited signs of recovery, with its annual inflation rate declining from 5.2% in Aug-23 to 4.3% in Sep-23. As a result, TJL expects an increase in orders from this region in Q3. However, the US, also holding a 50.0% share in TJL's market penetration, did not witness substantial progress due to market softness and a notable rise in the CPI to 3.7%YoY (+0.4%MoM) in Sep-23, signaling high inflation rates. Moreover, apparel prices in the US increased by 2.3%YoY in Sep-23. With a potential for further interest rate hikes in the US to curb inflation, TJL anticipates continued market softness in the US during the upcoming quarters. This expectation is driven by a slowdown in spending growth, with a notable shift towards purchasing services rather than apparel and other goods.

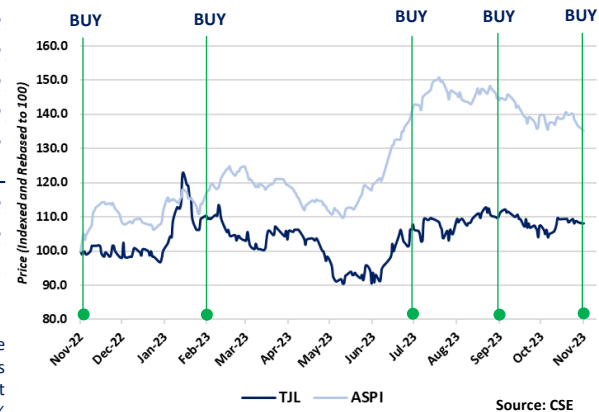


## FIRST CAPITAL RESEARCH

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



## Minimum Return for BUY:

Buy Below for FY25E [AER of 23.0% with DPS]: LKR 38.3  
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.

Source: CSE



**Bolstering synthetic capacity and capitalizing on growing global demand**

TJL is taking significant steps to enhance its synthetic capacity, aiming to increase its contribution to the topline from 12.0% to 25.0%. This move aligns with the company's expansion in the synthetic segment, marking a global growth of 7.0%YoY. In tandem with this, TJL foresees similar market trends throughout Q3, with further improvements expected in Q4. The company anticipates that the active wear fabric market's growth trajectory will persist and is actively seizing these opportunities by expanding its synthetic capacities across the Group. This expansion is set to enhance and diversify its product portfolio, catering to athleisure gym wear, sportswear, leisure, and yoga wear market segments. Notably, the prevailing shift towards remote work and the casualization of fashion trends further sustains the allure of sportswear and athleisure due to the ongoing preference among shoppers for comfortable clothing options. Notably, TJL is actively participating in the functional fabric fair in Portland, with an eye on securing partnerships with leading global functional brands such as Adidas and Under Armour.

**Expansion in Bangladesh and the digital brands segment**

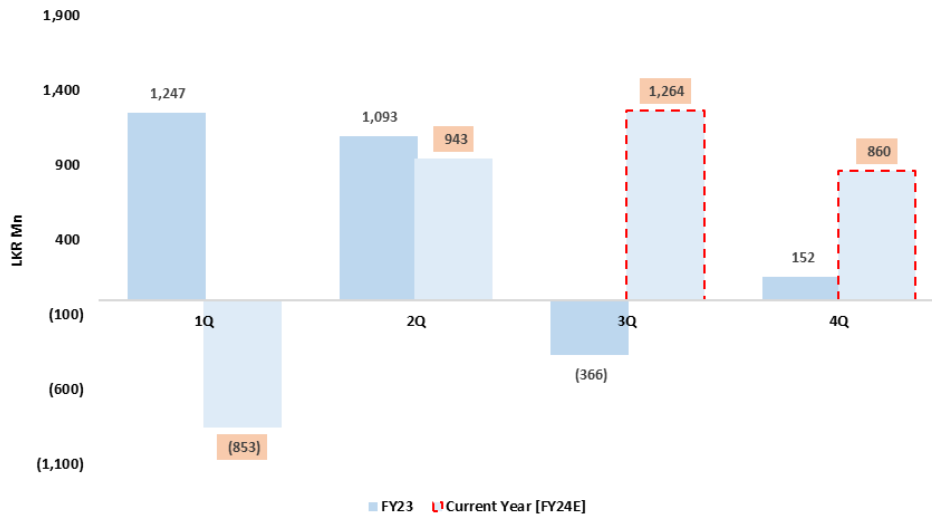
TJL has secured commercial orders in Bangladesh, focusing on expanding its presence within the synthetic space and leveraging increased capacities in India. Furthermore, TJL has outlined plans to enhance its marketing efforts to attract additional orders from this region. Presently, TJL ships products to Bangladesh from India and Sri Lanka, constituting approximately 5.0%-10.0% of their output. However, TJL is actively progressing towards establishing direct operations in Bangladesh, with expectations to generate tangible output from this initiative in Q3 and Q4. While domestic brands dominate the apparel segment in Bangladesh, the rising per capita income and consumer interest in international brands has created an opportunity for overseas retailers and brands to enter the market, contributing to the industry's maturation. Moreover, TJL garnered significant orders from the digital brand segment, which has positioned TJL as the local fabric partner for key vendor partners. Additionally, a dedicated cross-functional team has been established to facilitate this expansion and the company anticipates that the order volume in Q3 will mirror the levels seen in Q2. Amidst the ongoing "China Plus One" strategy, Sri Lanka is reaping benefits, witnessing an uptick in orders due to this approach. Additionally, some of TJL's clients are diversifying their sourcing destinations due to penetration challenges, where TJL's vertical integration within countries is proving advantageous.

**FV for FY25E maintained at LKR 50.0**

Looking ahead, TJL aims to introduce new strategic brands, extend its synthetic market footprint, and diversify across new customer bases, regions, and product segments in the near future. Furthermore, considering the resurgence in consumer demand, we have upgraded TJL's earnings forecast for FY24E to LKR 2.2Bn while earnings for FY25E is estimated at LKR 2.4Bn. Hence, on the back of higher than anticipated earnings growth, we are maintaining our FV at LKR 50.0 for FY25E providing an annualized return of 34.9% at the current price level of LKR 34.6. **MAINTAIN BUY**



### Quarterly Earnings



### Estimate Revision

In LKR Mn	FY24E - O	FY24E - R	% Change	FY25E - O	FY25E - R	% Change
<b>Earnings Estimate</b>						
Revenue	70,225	62,202	-11%	76,272	67,480	-12%
Gross profit	3,511	6,220	+77%	6,102	6,748	+11%
EBIT	808	3,483	+331%	3,165	3,846	+22%
Profit before tax	1,069	3,280	+207%	3,323	3,578	+8%
Net Profit	748	2,214	+196%	2,326	2,415	+4%
EPS	1.0	3.1		3.2	3.4	
Growth YoY	-65%	4%				
<b>Balance Sheet Estimate</b>						
Shareholders' Equity	32,417	33,040	+2%	33,348	34,006	+2%
Borrowings	13,778	11,953	-13%	15,094	11,955	-21%
<b>NAVPS</b>	<b>45.2</b>	<b>46.1</b>		<b>46.5</b>	<b>47.4</b>	
<b>Ratio Estimate</b>						
<b>ROE (%)</b>	<b>2.3%</b>	<b>6.8%</b>		<b>7.1%</b>	<b>7.2%</b>	
<b>PER (x)</b>	<b>34.0</b>	<b>11.2</b>		<b>10.9</b>	<b>10.3</b>	
<b>PBV (x)</b>	<b>0.8</b>	<b>0.8</b>		<b>0.8</b>	<b>0.7</b>	

### Valuation Table

P/E 31 March	FY20	FY21	FY22	FY23	FY24E	FY25E	FY26E
<b>Estimates (LKR 'Mn)</b>							
Revenue	33,277	31,780	49,588	84,037	62,202	67,480	73,189
Gross profit	4,229	3,790	4,578	6,843	6,220	6,748	7,319
EBIT	2,728	2,441	2,573	3,295	3,483	3,846	4,172
<b>Net Profit</b>	<b>2,384</b>	<b>2,140</b>	<b>2,531</b>	<b>2,127</b>	<b>2,214</b>	<b>2,415</b>	<b>2,599</b>
Adjusted EPS (LKR)	3.3	3.0	3.5	3.0	3.1	3.4	3.6
YoY Growth (%)	28%	-10%	18%	-16%	4%	9%	8%
<b>Valuations</b>							
PER (x)	10.5x	11.7x	9.9x	11.8x	11.2x	10.3x	9.5x
PBV (x)	1.6x	1.4x	0.9x	0.8x	0.8x	0.7x	0.7x
DY (%)	6.9%	4.7%	5.7%	4.3%	4.4%	5.8%	6.2%
NAVPS	21.8	24.8	39.4	44.7	46.1	47.4	48.9
DPS (LKR)	2.4	1.7	2.0	1.5	1.5	2.0	2.2
Dividend Payout	72%	55%	57%	51%	50%	60%	60%



### Valuation Summary

Expected TJL price	FY24E	FY25E	Return	FY24E	FY25E
EV/EBITDA Valuation based target price	44.7	51.1	<b>Target Price</b>	<b>40.0</b>	<b>50.0</b>
PER based Valuation	40.2	47.2	<b>Current Price</b>	<b>34.6</b>	<b>34.6</b>
<b>Average Target Price</b>	<b>42.4</b>	<b>49.1</b>	<b>Capital Gain (LKR)</b>	<b>5.4</b>	<b>15.4</b>
<b>Target Price after Rounding off</b>	<b>40.0</b>	<b>50.0</b>	<b>Dividends up to 31st March</b>	<b>1.5</b>	<b>2.0</b>
			<b>Capital Gain %</b>	<b>16%</b>	<b>45%</b>
			<b>Dividend Yield %</b>	<b>4%</b>	<b>6%</b>
			<b>Total Return %</b>	<b>20%</b>	<b>50%</b>
			<b>Annualized Return %</b>	<b>66%</b>	<b>35%</b>

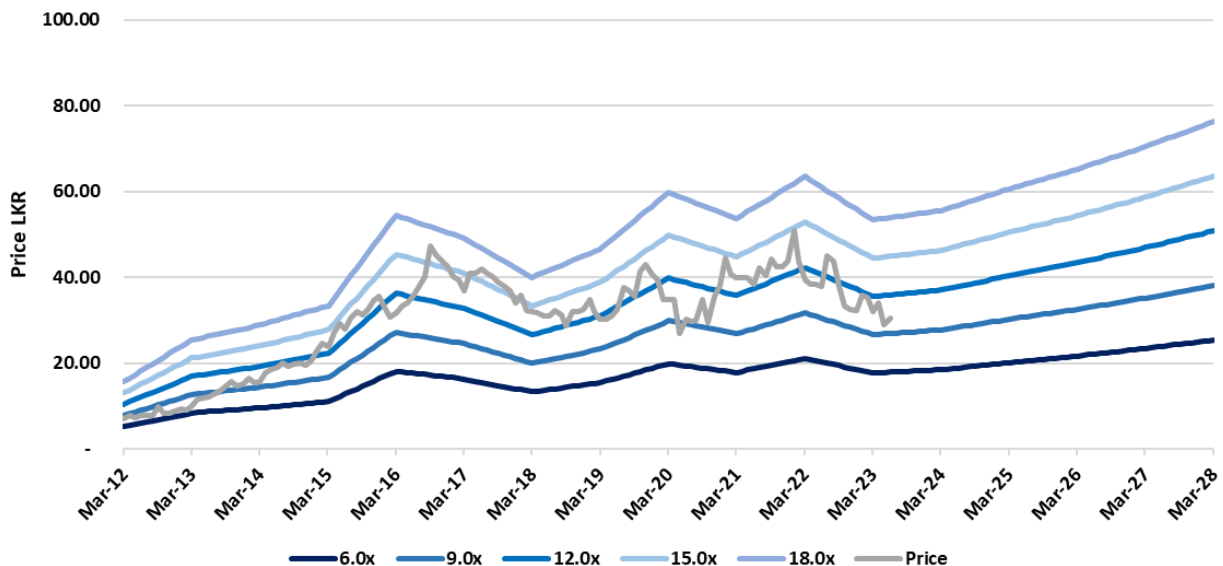
### PER based Valuation

PER based Valuation	FY24E	FY25E
Earnings (LKR 'Mn)	2,214	2,415
No. of Shares ('Mn)	717	717
<b>EPS</b>	<b>3.1</b>	<b>3.4</b>
<b>Expected PER</b>	<b>13.0x</b>	<b>14.0x</b>
<b>Target Price</b>	<b>40.2</b>	<b>47.2</b>

### EV/EBITDA Valuation

EV/EBITDA based Valuation	FY24E	FY25E
EBITDA (LKR 'Mn)	8,007	8,723
Avg. EV/EBITDA	4.0x	4.2x
No. of Shares ('Mn)	717	717
<b>Target Price</b>	<b>44.7</b>	<b>51.1</b>

### PER Chart





## Appendix I: Statement of Income and Expenses

Statement of Profit or Loss (LKR Mn)	FY19	FY20	FY21	FY22	FY23	FY24E	FY25E	FY26E
<b>As at 31st March</b>								
Revenue	31,747	33,277	31,780	49,588	84,037	62,202	67,480	73,189
Cost of sales	-28,061	-29,048	-27,990	-45,010	-77,194	-55,982	-60,732	-65,870
<b>Gross profit</b>	<b>3,686</b>	<b>4,229</b>	<b>3,790</b>	<b>4,578</b>	<b>6,843</b>	<b>6,220</b>	<b>6,748</b>	<b>7,319</b>
Other income	246	173	186	151	532	373	472	512
Selling, Distribution & Admin expenses	-1,587	-1,673	-1,534	-2,156	-4,079	-3,110	-3,374	-3,659
<b>Operating profit</b>	<b>2,345</b>	<b>2,728</b>	<b>2,441</b>	<b>2,573</b>	<b>3,295</b>	<b>3,483</b>	<b>3,846</b>	<b>4,172</b>
Finance Income	102	244	277	440	811	947	885	835
Less : Finance Cost	-189	-160	-119	-149	-990	-1,150	-1,153	-1,157
Net finance income	-88	84	158	291	-179	-203	-268	-321
<b>Profit before tax</b>	<b>2,257</b>	<b>2,812</b>	<b>2,599</b>	<b>2,864</b>	<b>3,116</b>	<b>3,280</b>	<b>3,578</b>	<b>3,850</b>
Income tax expense	-398	-428	-460	-332	-990	-1,066	-1,163	-1,251
<b>Profit for the Year</b>	<b>1,859</b>	<b>2,384</b>	<b>2,140</b>	<b>2,531</b>	<b>2,127</b>	<b>2,214</b>	<b>2,415</b>	<b>2,599</b>
EPS	2.6	3.3	3.0	3.5	3.0	3.1	3.4	3.6

## Appendix II: Statement of Financial Position

Statement of Financial Position (LKR Mn)	FY19	FY20	FY21	FY22	FY23	FY24E	FY25E	FY26E
<b>As at 31st March</b>								
<b>ASSETS</b>								
<b>Non-Current Assets</b>								
Property, plant and equipment	8,408	8,777	8,711	14,715	20,259	20,802	19,725	18,886
Capital work-in-progress	119	590	425	5,269	1,836	336	336	336
Intangible Assets	94	78	125	143	161	1,084	1,772	2,284
Deferred tax assets	111	256	273	432	1,856	1,856	1,856	1,856
Goodwill	58	62	66	96	106	116	128	141
Right-of-use assets	236	910	899	1,341	1,740	1,740	1,740	1,740
<b>Total Non-Current Assets</b>	<b>9,026</b>	<b>10,673</b>	<b>10,500</b>	<b>21,996</b>	<b>25,958</b>	<b>25,934</b>	<b>25,558</b>	<b>25,243</b>
<b>Current Assets</b>								
Inventories	4,494	5,904	7,281	16,356	13,383	8,521	9,244	10,026
Trade and other receivables	4,013	4,137	7,181	12,859	9,026	11,929	13,866	16,042
Current Tax Receivable	9	18	6	477	497	0	0	0
Cash and cash equivalents	4,290	5,263	4,452	6,383	7,914	15,378	17,028	17,882
Other Financial Assets	553	967	1,680	1,822	3,281	3,445	3,445	3,445
<b>Total Current Assets</b>	<b>13,359</b>	<b>16,289</b>	<b>20,600</b>	<b>37,897</b>	<b>34,100</b>	<b>39,273</b>	<b>43,583</b>	<b>47,395</b>
<b>Total Assets</b>	<b>22,386</b>	<b>26,962</b>	<b>31,099</b>	<b>59,894</b>	<b>60,058</b>	<b>65,207</b>	<b>69,140</b>	<b>72,638</b>
<b>EQUITY AND LIABILITIES</b>								
<b>Capital and Reserves</b>								
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	10,396	11,362	12,402
Share option scheme	97	97	153	153	153	153	153	153
<b>Total Equity</b>	<b>13,925</b>	<b>15,649</b>	<b>17,764</b>	<b>28,226</b>	<b>32,043</b>	<b>33,040</b>	<b>34,006</b>	<b>35,045</b>
<b>Non-Current Liabilities</b>								
Borrowings	801	412	198	5,581	6,239	5,927	5,808	5,692
Lease Liability	0	628	655	930	1,341	1,341	1,341	1,341
Deferred tax liabilities	538	648	627	919	2,364	2,364	2,364	2,364
Retirement benefit obligations	252	378	520	425	569	569	569	569
<b>Total Non-Current Liabilities</b>	<b>1,591</b>	<b>2,065</b>	<b>2,000</b>	<b>7,855</b>	<b>10,512</b>	<b>10,200</b>	<b>10,081</b>	<b>9,965</b>
<b>Current Liabilities</b>								
Trade and other payables	4,703	5,643	8,087	17,623	10,556	15,337	18,303	20,754
Borrowings	2,167	3,502	3,108	5,914	6,343	6,026	6,147	6,270
Current tax liability	0	92	126	233	490	490	490	490
Lease Liability	0	12	14	43	114	114	114	114
<b>Total Current Liabilities</b>	<b>6,869</b>	<b>9,248</b>	<b>11,335</b>	<b>23,813</b>	<b>17,503</b>	<b>21,967</b>	<b>25,053</b>	<b>27,627</b>
<b>Total Equity &amp; Liabilities</b>	<b>22,386</b>	<b>26,962</b>	<b>31,099</b>	<b>59,894</b>	<b>60,058</b>	<b>65,207</b>	<b>69,140</b>	<b>72,638</b>
Adjusted NAVPS	19.4	21.8	24.8	39.4	44.7	46.1	47.4	48.9



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