

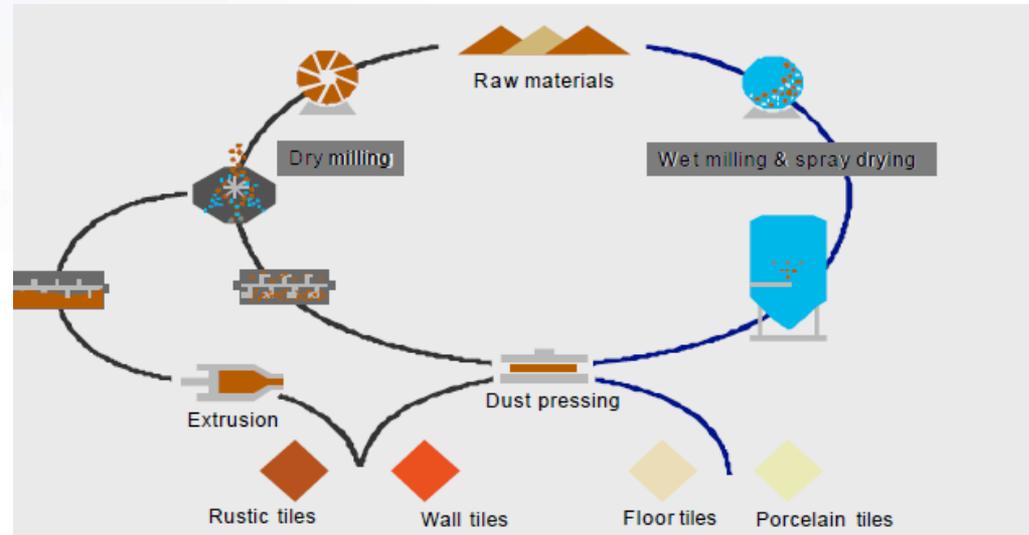
# TILE SECTOR UPDATE

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# ORIGIN OF THE CERAMIC TILE

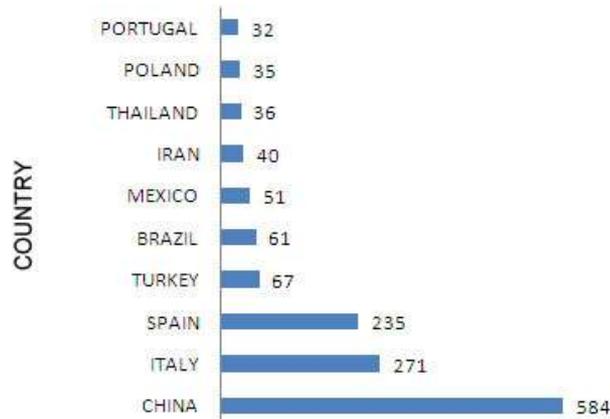
- Based on historical information, the usage of tiles can be traced back as far as the fourth millennium BC (4000 BC) to Egypt. In Egypt, tiles were used to decorate various houses when clay bricks were dried beneath the sun or baked, and the first glazes were blue in color and were made from copper.
- Today most of the ceramic tiles produced throughout the world is neither hand-made or hand-painted. Automated manufacturing techniques are used and the human hand does not enter into the picture until it is time to install the tile. They are used in an almost infinite number of ways.
- Ceramic tiles are preferred in the construction industry, as walls and floors must resist chemicals. Furthermore Space Shuttle never leaves Earth without its protective jacket of high-tech, heat resistant tiles.



# GLOBAL TILE INDUSTRY OVERVIEW

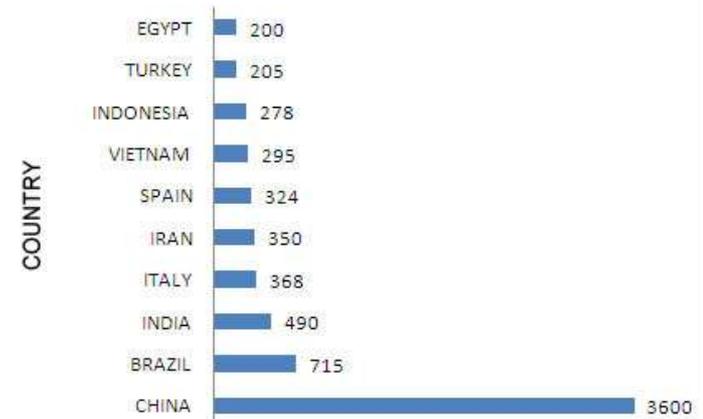


**TOP 10 EXPORTING COUNTRIES**

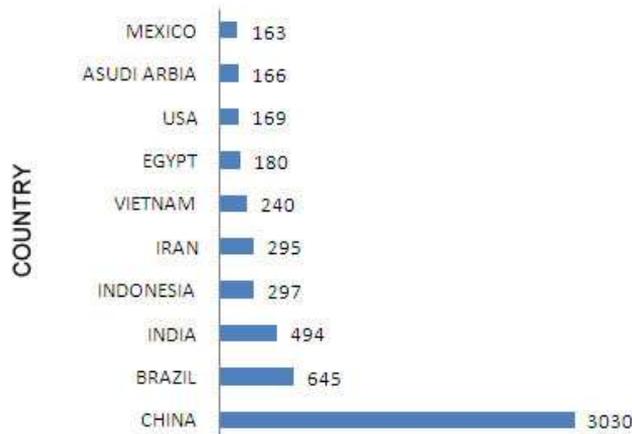


*Global Tile  
Statistics 2009*

**TOP 10 MANUFACTURING COUNTRIES**



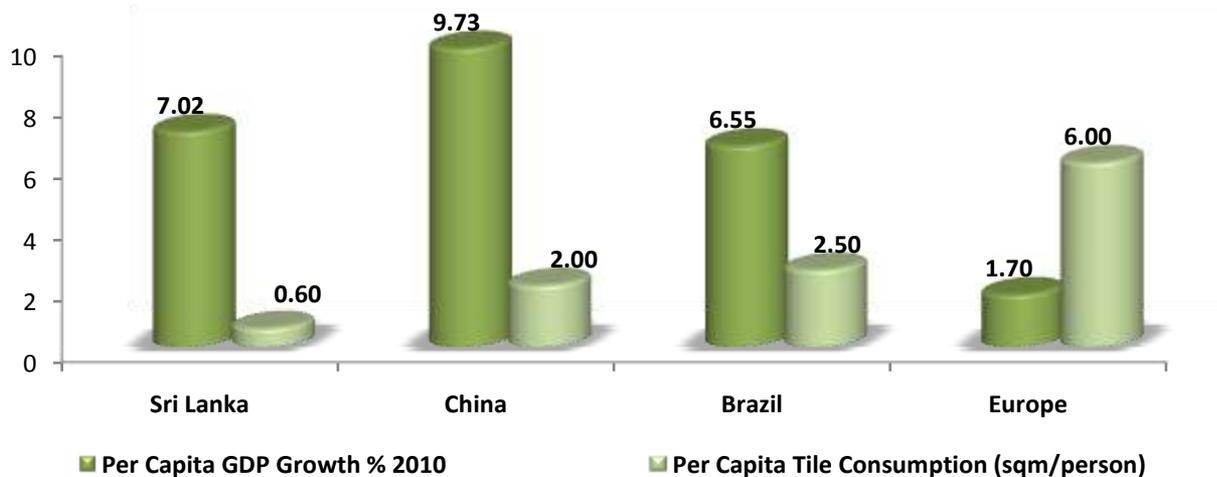
**TOP 10 CONSUMPTION COUNTRIES**



The statistics depicted in the charts highlight the dominant stance taken by global giant China, in terms of Manufacturing, Exporting and Consumption.

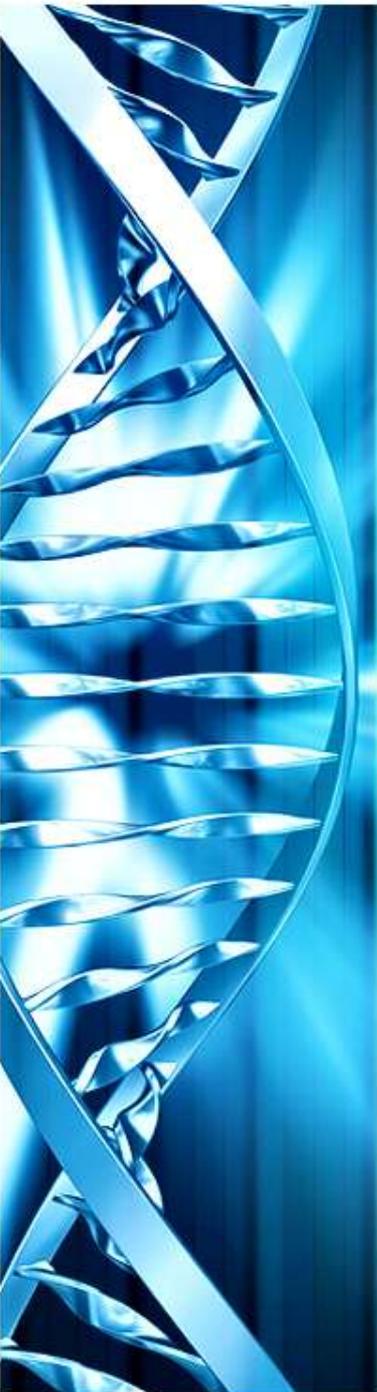
*(Source : CWR, Countries listed according to output in 2009)*

# IN COMPARISON WITH THE GLOBAL PEERS



*Source: Asia Wealth Management Research*

- When compared to certain countries, the Sri Lankan tile consumption is deeply low. This is due to the fact that tile is a luxury product and does not have a priority in a typical dwelling construction. Furthermore low per capita tile consumption compared to higher per capita GDP growth in Sri Lanka proves that there is ample room for the tile sector to grow.
- However we solemnly believe a commutation to take place as the per capita growth rate in Sri Lanka is at a sustainable level compared to other developed countries. It is emphasised in our report that tile consumption is highly correlated with the per capita income. Increase in income expects to lever the tile sector growth.



# SRI LANKAN STORY

- Sri Lanka's ceramic industry boasts of a history that dates back several centuries. The country's historical ruins bear testimony to the rich diversity of ancient craftsmanship and the skills of the craftsmen themselves. The distinctive designs and exquisite elegance of the ceramic products manufactured by the Sri Lankan ceramic industry today vividly explains the influence of this rich heritage.
- Sri Lanka supplies quality ceramic products, mainly porcelain tableware, porcelain ornamental ware & glazed wall and floor tiles to discerning buyers in the world market. Among these buyers are USA, Australia, Italy, Germany, UK, France, Canada, Netherlands, Japan and Singapore.
- Sri Lanka is rich in minerals, such as kaolin, ball clay, feldspar, silica quartz and dolomite, which are used in the manufacture of ceramic products. The excellent quality and purity of these materials contribute to the high standard of the products, which are now of international repute. Pigments and other miscellaneous chemicals used in the preparation of glazes, decals, liquid gold and silver are obtained from reputed sources around the world.
- Sri Lanka has the availability of a highly skilled and literate workforce. An abundance of trained and gifted designers, chemists, technologists and engineers provide a highly productive workforce.

# DOMESTIC INDUSTRY & ECONOMIC OVERVIEW

- Sri Lanka's economy grew 8.3% in 2011 compared to a growth of 8.0% in 2010.
- The ceramic industry dipped 6.1% during the 2011 nevertheless there was a 25.9% growth in mining and quarrying and a 20.7% growth in the construction sector.
- The ceramic industry in Sri Lanka is gifted with a highly trainable workforce and provided direct livelihood to around 7,000 people while another 7,500 are indirectly employed.
- Currently the local tile cluster is on a low base with the per capita tile consumption only at 0.6m<sup>2</sup> compared to nations like Europe at 6m<sup>2</sup> per person, Brazil 2.5m<sup>2</sup> per person and global tile giant China at 2m<sup>2</sup> per person. Low per capita tile consumption compared to higher per capita GDP growth in Sri Lanka proves that there is ample room for the tile sector to grow.
- At present, floor tiles contribute 77% (with an estimated production of circa 8.9mn m<sup>2</sup> per annum) whilst wall tiles contribute 23% (i.e. 2.7mn m<sup>2</sup> per annum) to the local tile cluster.

## Ceramic Chain

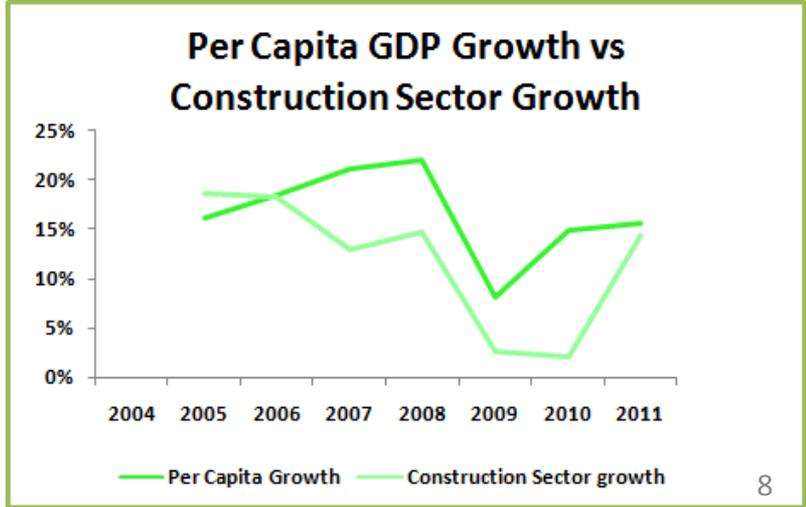
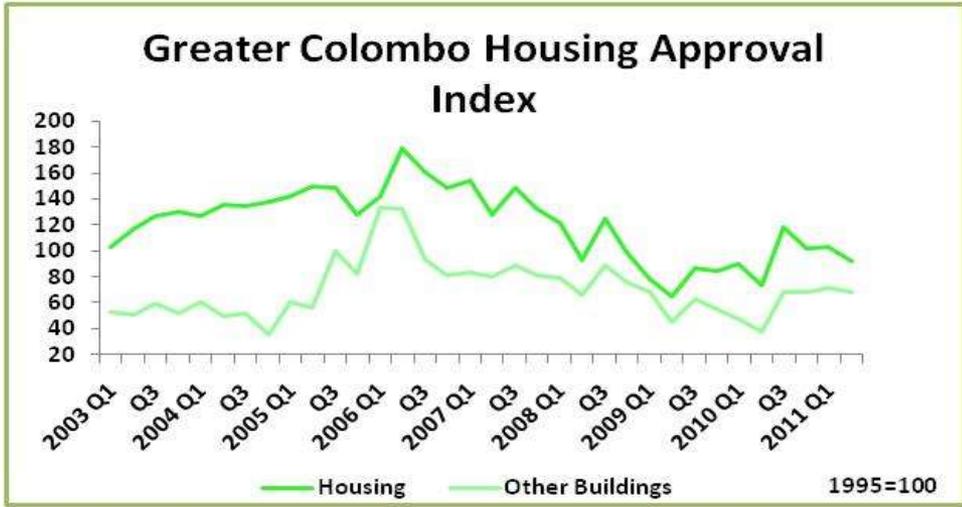
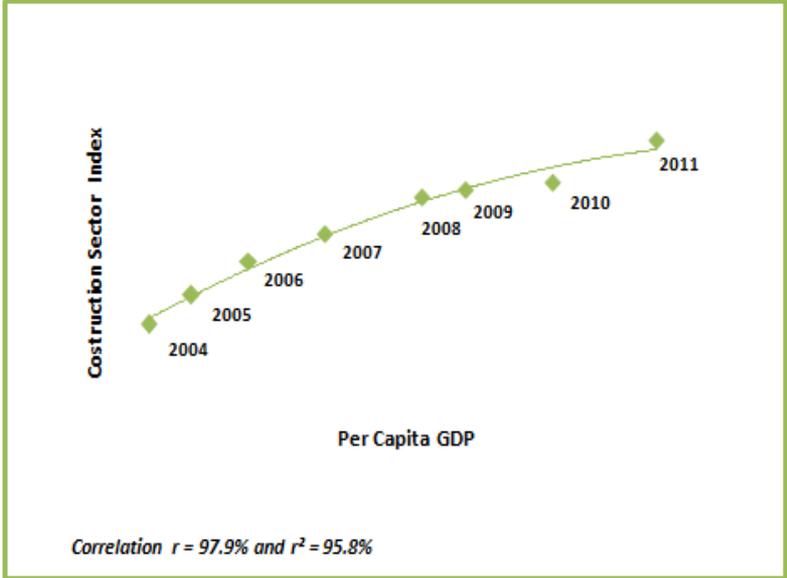


Share of Global market share	0.20%
Main Customers	US, UK, Germany, Australia, Spain
Main Competitors	China, Italy
Cluster	Sri Lanka Ceramic Council
Challenges	High Energy Prices and Rigid Labour Policies
Ministry	Ministry of Industrial Development
Est. Female employment	70%
Est. % of Rural Employment	85%
Key Geographich Areas	Central Province, North Central Province, North Western Province, Sabargamuwa Province, Western Province

Source: Asia Wealth Management Research

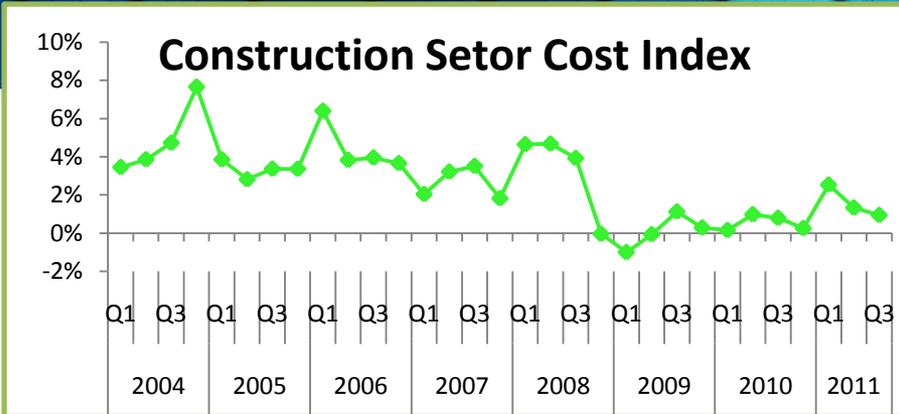
# DOMESTIC INDUSTRY & ECONOMIC OVERVIEW

- The graph proves the robust correlation (circa 97.9%) between Per Capita GDP and the Construction Sector Index. Hence the rise in real income had persuaded the middle income groups to consider construction of housing.
- We solemnly expect an upbeat momentum in future as the GDP forecast is positive and stable.
- Housing & construction is expected to grow moderately owing to increasing living standards. Growth in the sector is reflected by 25.3 percent YoY rise in the Greater Colombo Housing Approvals Index

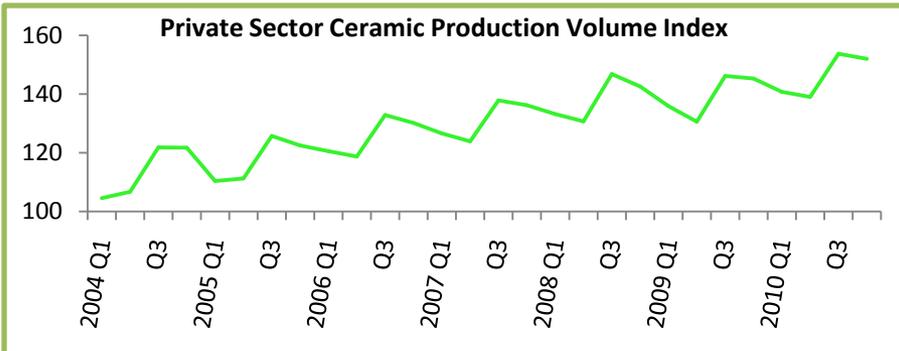


Source: CBSL Statistics and Asia Wealth Management Research

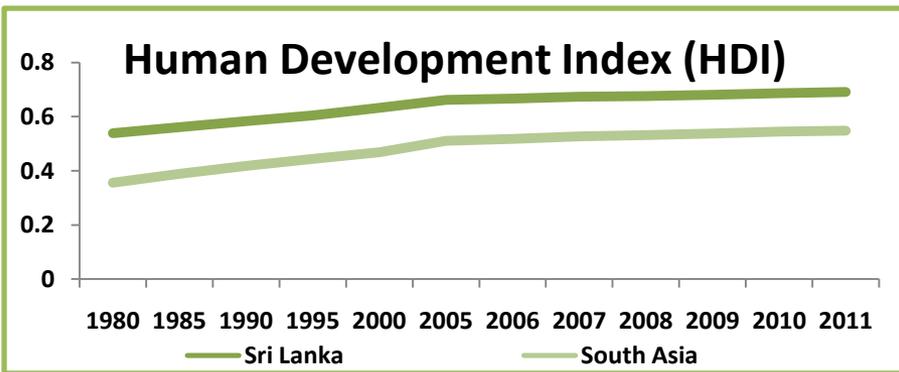
# DOMESTIC INDUSTRY & ECONOMIC OVERVIEW



Over the seven year period the construction sector cost index has been gradually declining due to the stringent government price controls on raw materials especially cement. Hence upcoming boom in the economy is levered by the lower construction cost which is anticipated to blossom new commercial and domestic construction projects thus positively backing the local tile cluster.



The ceramic production volume is cyclical by nature, apart from tile most ornamental products are manufactured to cater during festive seasons. This nature is expected to persist in forthcoming periods.



The HDI represents a push for a broader definition of well-being and provides a composite measure of three basic dimensions of human development: health, education and income. Sri Lanka's HDI is 0.691 (2011), which gives the country a rank of 97 out of 187 countries with comparable data. The HDI of South Asia as a region increased from 0.356 in 1980 to 0.548 in 2011, placing Sri Lanka above the regional average. Thus improve HDI leads to improve standard of living, where by the construction industry benefits with better dwelling. This in turn levers the future tile requirements .

# MACRO ECONOMIC FACTORS AFFECTING TILE SECTOR

- **AWPLR & Exchange Rates**

AWPLR is expected to fluctuate within a range of 20 to 15 percent nevertheless the exchange rate would not remain stable as the central bank no longer intervenes due to the lack of dollar reserves. Hence there is a possibility for the sector to be adversely affected with increasing borrowing cost and high imported raw material prices.

- **Corporate Taxes And Import/Export Levies**

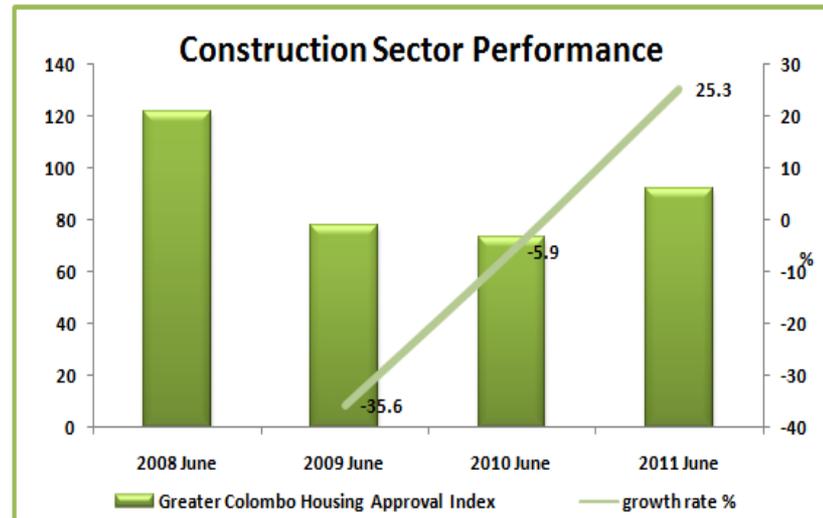
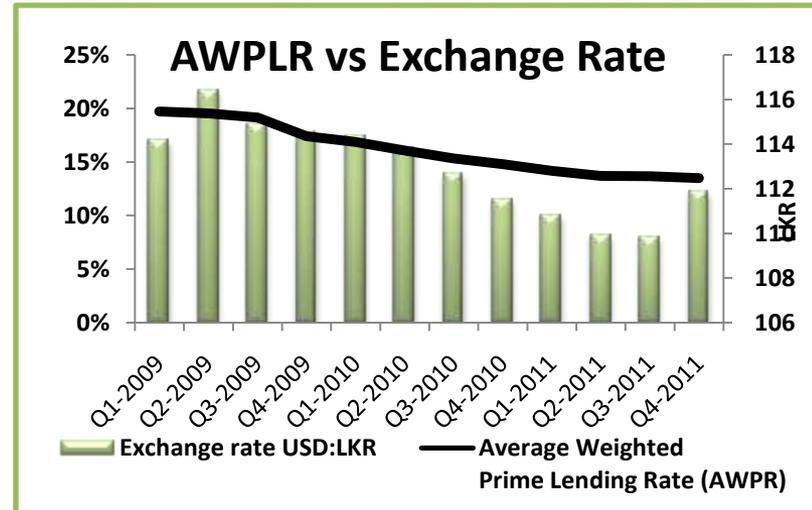
Reduction in corporate taxes from 35% to 28%, and the cess of 35% on imported tiles expect to positively contributed towards the tile sector making locally manufactured tiles competitive in the domestic arena.

- **Construction Sector Performance**

The 25% YoY growth as at June 2011 in the Greater Colombo Housing Approval Index expects to up heel the demand for tiles in the future.

- **Tourism Boom And Hotel Industry**

Heavy growth in the tourist arrivals has resulted in major refurbishments and expansions in the hotel industry. Thus this is a positive sign for the tile cluster as the demand for tiles is expected to increase at a rapid rate.



# PORTER'S FIVE FORCES MODEL



- ***Threat Of New Entrants***

The tile industry in Sri Lanka is on a growth stage which makes it an attractive investment. The demand for tiles is persistently increasing due to the booming construction sector. However the initial start up cost for a manufacturing plant is colossal especially on plant and machinery. The typical payback period of setting up a plant is circa 4 to 5 years. Hence this makes it unattractive for potential players to enter the industry. Nevertheless future alphas on incumbent firms can make the industry attractive to potential entrants.

- ***Bargaining Power of Suppliers***

Tile industry consumes large quantities of clay. Although there is an abundant supply of high quality ball and china clay in Sri Lanka, mining restrictions prevailing in the country act as a barrier in acquiring required quantities. Furthermore around 40% of the production costs accounts for energy such as electricity and LP Gas. Thus, due to the price in-elasticity of raw materials and energy, the suppliers possess a higher bargaining power. However, backward integration by tile manufacturers (Lanka Ceramic having its own ball clay mines) and hedging techniques may curb these adversities. Despite suppliers possess a heavy bargaining power.

- ***Bargaining Power of Customers***

There is heavy influx of cheaper tiles from China, India and Indonesia which is preferred by income elastic customers. Nevertheless despite of premium prices possessed by locally manufactured tiles, due to high quality and durability, the local demand still exists. Overall customers too possess a higher bargaining power due to the availability of cheap imports.

# PORTER'S FIVE FORCE MODEL



- ***Degree Of Rivalry***

Sri Lankan tile manufacturing industry is operating in an oligopolistic market. Both the wall tile and floor tile clusters are dominated by three large firms; viz RCL, LWL and TILE. Furthermore, there is a mutual agreement among these firms to evade price competition in order to prevent cheaper imported tiles capturing and dominating the market. In addition rapid economic growth has levered the construction sector thereby increasing the size of the market and allowing incumbent firms to increase their sales volume to produce a healthy bottom line.

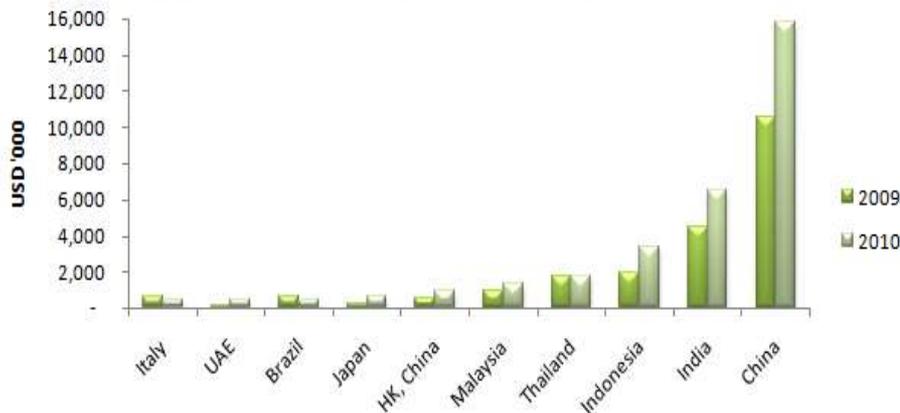
- ***Threat Of Substitutes***

The closest substitutes for tiles are marbles, wooden (parquet) flooring and grout & mortar. If the price of ceramic tiles may escalate due to heavy production cost (increasing energy and raw material prices). In addition there may be a shortage on imported tiles due to stringent protectionist policies enacted by the government. If the demand for ceramic tiles is price elastic, local consumers, especially domestic users may switch to the above mentioned economical substitutes. On the whole, despite of these drawbacks, households prefer to use ceramic tiles to get their desired fit and finish.

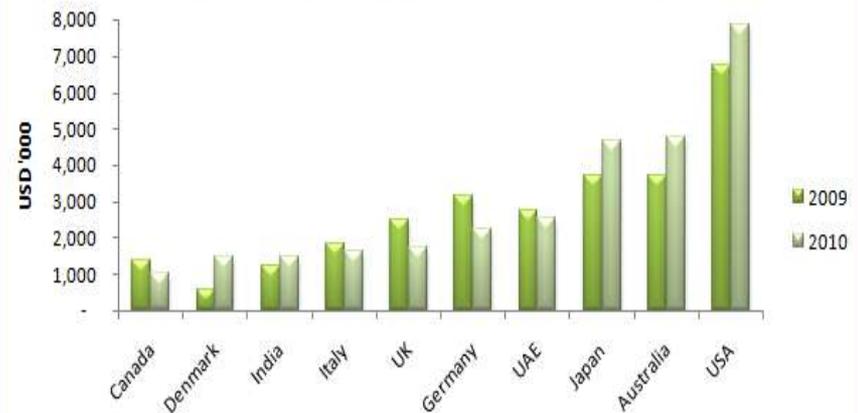
# EXPORTS VS. IMPORTS



### Main Ceramic Import Markets 2009-2010



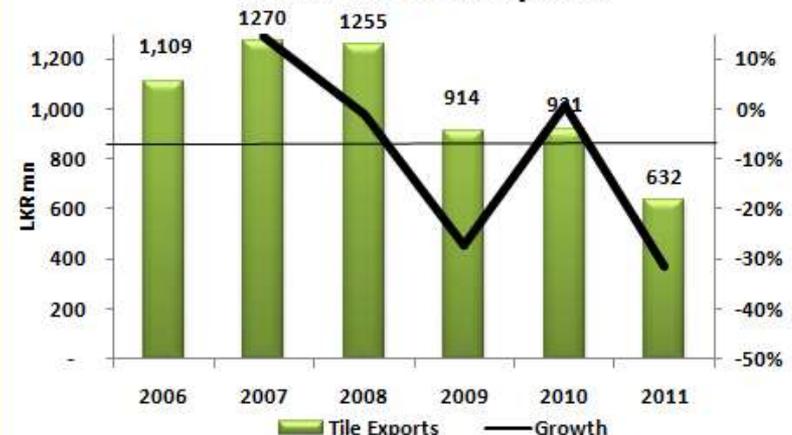
### Main Ceramic Export Markets 2009-2010



Over the recent two year period Sri Lanka has become a net importer of ceramic products. This mainly includes ceramic and porcelain tiles due to the booming demand in the local construction industry.

Thus the local tile manufacturers have switched to local customers witnessing continuous dip in the value of tile exports over the four year period

### Sri Lanka Tile Exports



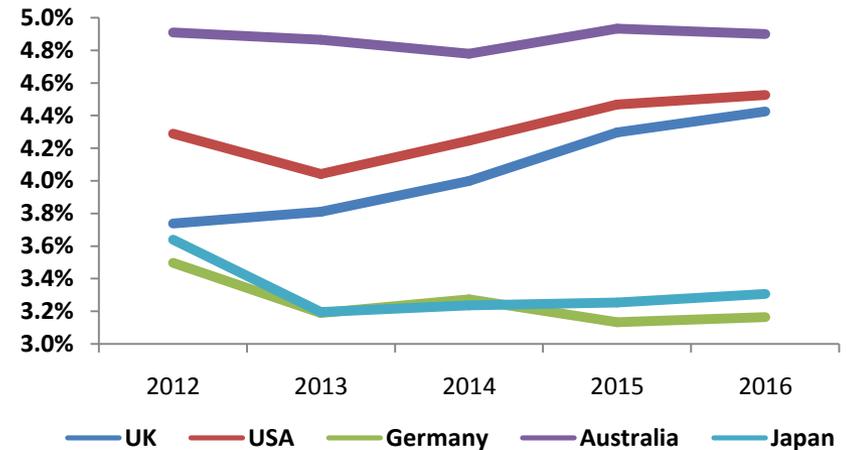
# INTERNATIONAL CUSTOMERS

- The following are the major international customers for Sri Lankan ceramic products,

- ✓ UK
  - ✓ USA
  - ✓ Germany
  - ✓ Australia
  - ✓ Japan
- } % share of exports

- With end of the global turmoil, a boom is highly anticipated in the local ceramic sector especially ceramic tiles thereby expecting hale and hearty growth in companies such Royal Ceramics, Lanka Walltile and Lanka Tiles in the local tile industry.
- Nevertheless, most local tile manufacturer emphasize on domestic clientele due to soaring demand from the construction sector.

### Forecasted GDP Growth Rates



Source: IMF

As depicted by the above chart, persistent growth in GDP of these countries expects to positively boost the export revenue of the domestic tile manufacturers in the island. Furthermore with the rupee depreciation, we can expect the industry to record higher export revenue from these countries in the future.

# TILE SECTOR COUNTERS



- *ROYAL CERAMICS LANKA PLC (RCL.N000)*

The prime activity of RCL Group continues to be manufacturing and selling of porcelain and ceramic tiles, along with the manufacturing and selling of sanitary ware. The group recently acquired a paint and allied product manufacturing company. Royal Ceramics Lanka (Rocell) manufacture vitreous floor tiles suitable for heavy duty traffic (R11) in 200x200mm, 300x300mm, 400x300mm, 400x400mm and 600x300mm in plain and mottle finishes. Stud and Rock face finishes are available for areas where slipping or traction is a problem, and they also manufacture step tread and 200x200mm cove tiles.

- *LANKA CERAMIC PLC (CERA.N000)*

The company is involved in the manufacture of Tableware, Sanitary ware, Hotel and Ornamental ware and low-tension insulators for export and local markets. Retail trading in Ceramic and allied products.

- *LANKA WALLTILE PLC (LWL.N000)*

The main activity of the LWL continues to be the manufacture of ceramic wall tiles for export and for sale in the local market.

Lanka Walltile is one of the few companies in the world still making the modest range of tiles suitable for renovations and period finishes. These include 152x75 mm and 152x152 mm in a wide range of colors plus biscuit tiles. Other sizes available are 108x108 mm, 200x200 mm and 400x300 mm together with capping, bead and cove tiles.

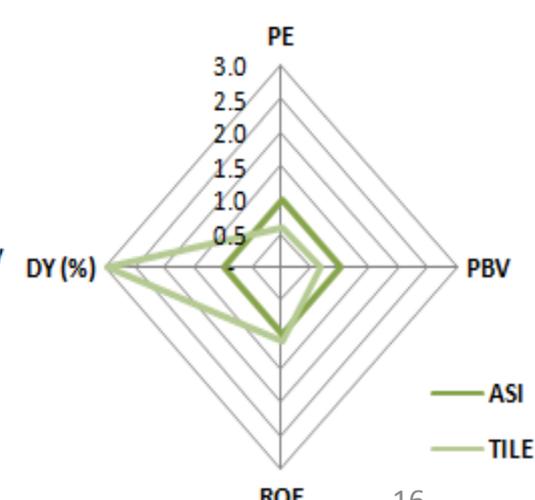
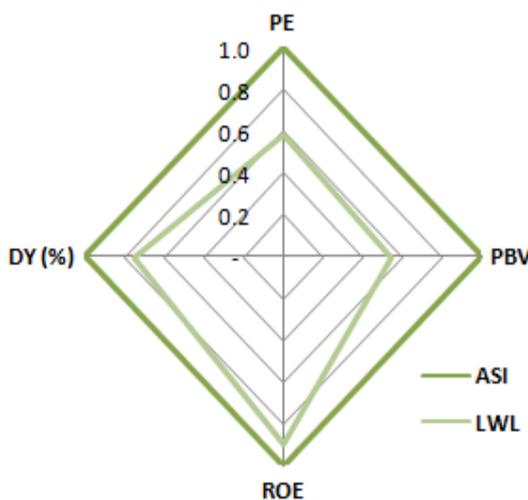
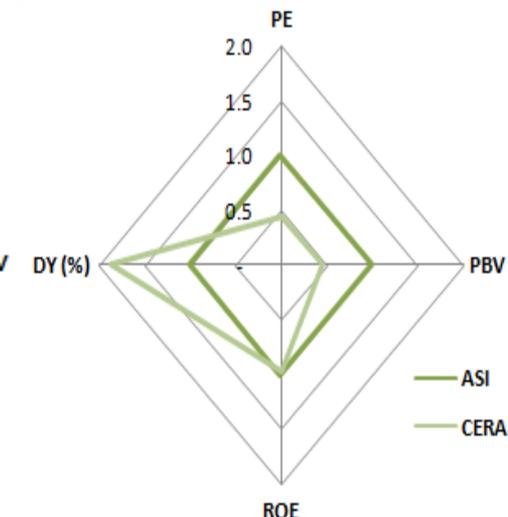
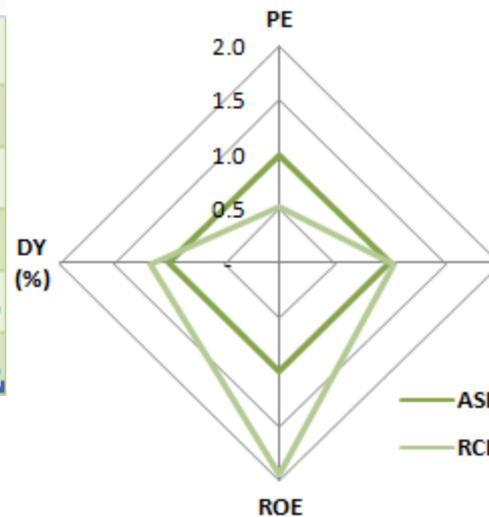
- *LANKA FLOORTILES PLC (TILE.N000)*

Lanka Floor Tiles is a leading manufacture of glazed ceramic floor tiles and its subsidiary company manufactures wood flooring, adhesives, and tile edging. Lanka Tiles have a large range of glazed floor tiles in 200x200, 300x300 and 400x400 mm.

# MARKET OVERVIEW



As at 17.04.2012	RCL	CERA	LWL	TILE
Market Capitalization (LKR mn)	13,028.8	2,100.0	4,089.5	3,262.6
PE	6.8	5.7	7.6	7.5
PBV	2.1	0.9	1.1	1.3
ROE	30.5%	15.1%	14.1%	17.3%
DY (%)	2.2%	3.6%	1.4%	5.7%



# MARKET SHARE

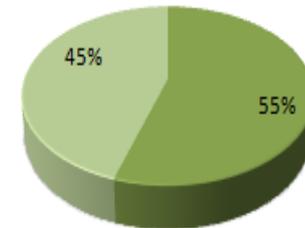


## A competitive oligopoly

- The tile sector in Sri Lanka which shows signs of an oligopolistic market is a highly competitive industry. The oligopoly consists of key listed manufacturers namely Royal Ceramics, Lanka Tiles and Lanka Walltile which contributes for a major portion of the tile market.
- Lanka Walltile dominates the local wall tile sector with a market share of 55% whilst imported tiles from the European and Asian market compete for the second place.
- In the floor tile sector Royal Ceramics dominates the local market with a circa 35% market share followed by Lanka Tile's with a 25% market share. The rest of the market's demand is mainly supplied through imported floor tiles from countries such as China, Italy and East Asia.

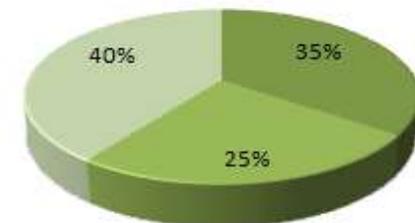
### Wall Tile Market

■ Lanka Walltile ■ Fragmented Importers



### Floor Tile Market

■ Royal Ceramics ■ Lanka Tiles ■ Fragmented Imports



# LOCAL PRODUCTION CAPACITY



- RCL's LKR3.0 bn investment to build its third tile factory in Kiriwaththuduwa to add another 12,000 m<sup>2</sup> per day to the ceramic tiles segment was post-poned by the senior management. The reason for this had been not stated but land preparation had been in progress.
- Lanka Walltile Meepe factory which had a current production capacity of circa 4,500 sqm per day was expanded by a further 3,000 sqm per day to facilitate production of 7,500 sqm. The commercial production commenced in June 2011. Conversely, Balangoda factory one of the oldest factories in the country, ceased operations at the end of April 2010. This will result in greater economies of scale and cost savings in future. Further, to promote the export business a "Trim Tile" line was added to the Meepe plant which commenced operation on 1QFY12. The factory has started producing larger tiles and has introduced a 30x60 inch tile in February 2011 which mainly targeted the local market.
- Lanka Tiles with an investment of LKR600mn expanded its capacity to 13,000 sqm per day. The commercial production commenced in Jan 2012.

	Capacity	FY11	FY12	FY13E
<b>RCL</b>	Porcelain tiles (m <sup>2</sup> /day)	4,333	4,333	4,333
	Ceramic tiles (m <sup>2</sup> /day)	10,500	10,500	10,500
	Sanitaryware units per month	20,000	20,000	20,000
<b>LWL</b>	Wall tiles (m <sup>2</sup> /day)	4,500	7,500	7,500
<b>TILE</b>	Floor tiles (m <sup>2</sup> /day)	9,500	13,000	13,000

# COST BREAKDOWN



- **Rising energy costs**

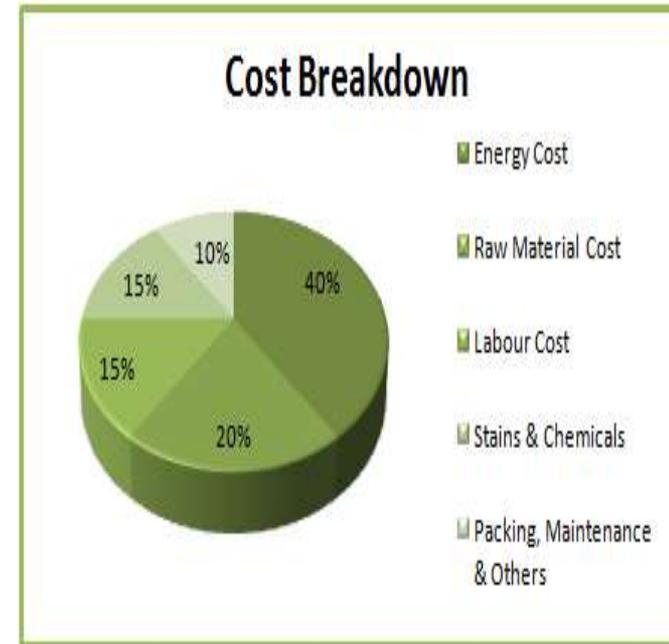
Currently 40% of the production cost is attributable towards the energy cost which acts as a critical factor for the industry whilst they consume around 1, 170 metric tons LPG per month.

The Ceramic Council of Sri Lanka (CCSL) together with the glass manufacturers has planned to lobby concerns against the sudden increase in levies and the long term impact to the sector.

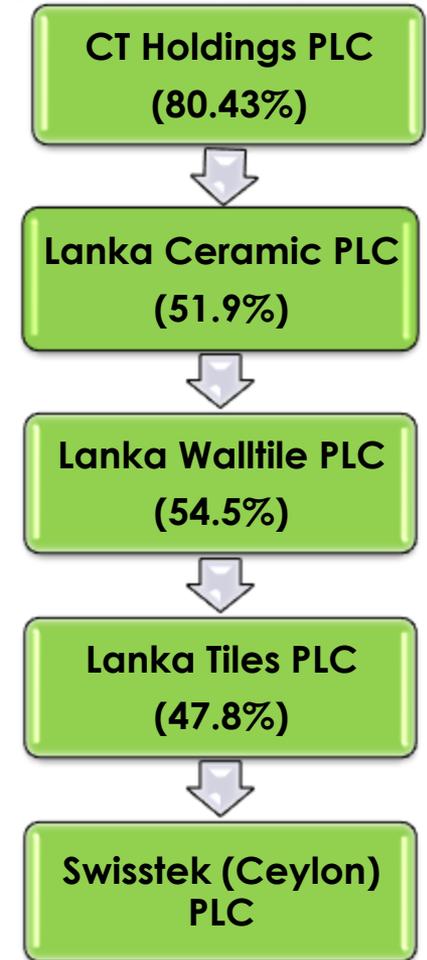
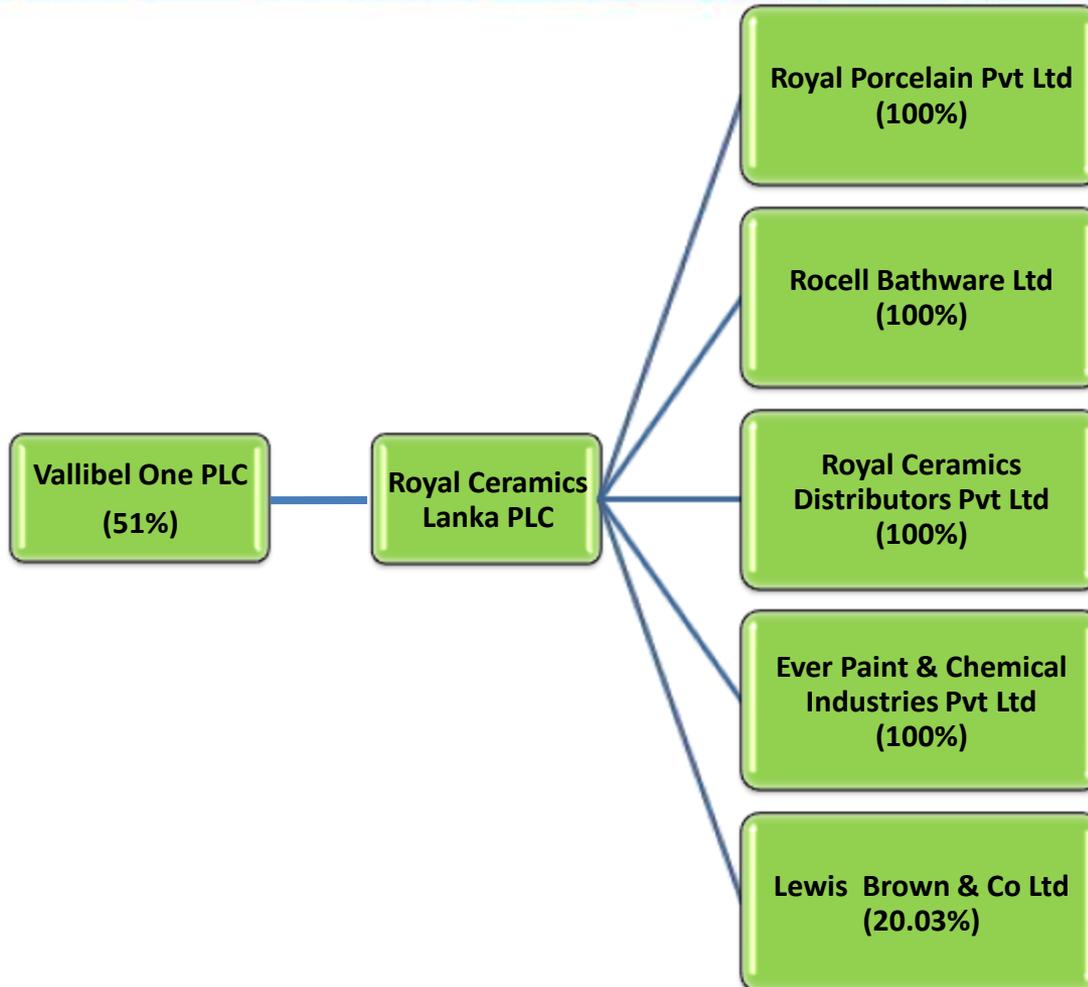
- **Escalating raw material cost**

Currently circa 20% of the production cost of ceramic tiles is accounted via raw material costs. Despite clay being easily available, the transportation cost and the escalation of fuel costs negatively impacts the industry at the point of extracting raw material. In the past Sri Lankan annual ceramic production included 10,000 metric tonnes of Kaolin, 25,000 tonnes of ball clay, 20,000 tonnes of feldspar and 5,000 tonnes of quartz which has doubled over the years up to now.

Lanka Ceramic, the parent company of LWL and TILE has the largest raw material reserves controlling the largest mining operations in the island. Furthermore, Royal Ceramics has also acquired land reserves to be utilized in the future whilst currently few regionally located independent miners also participate in supplying raw material.



# GROUP STRUCTURES

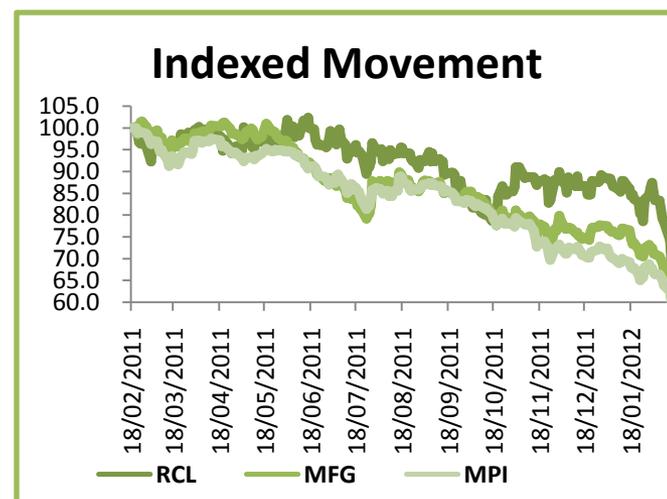


# RCL (LKR:113.00)



- RCL future performance would be strongly shouldered by the growth in the GDP of the country together with the staggering construction upbeat. With the local economy growing at circa 8.3% and industry growth rate of 9.4% RCL would easily be levered towards higher earnings in the future.
- The company's broad coverage with 41 showrooms and wider distribution network of 250 island wide dealers has strengthened the penetration ability of RCL. In addition RCL has expansion strategies down the pipeline, where it plans to have 10 additional showrooms during FY12 and 5 more in FY13. The management has expectations of increasing the dealer network at 10% YoY.
- The newly acquired paint company has a capacity of circa 65,000 gallons per month and is operating at full capacity catering to customer pre-manufacture orders. The group has a plan down its pipeline to expand the capacity to cater excess demand in the future.
- Moving forward, the tile and bathware segments expect to introduce new colours, designs and sizes to create vividness to the customer segment. This expectation may also be applied to the range of paint and allied products.
- Further, Royal Ceramics could be high turnover and robust earnings generating counter which has ample opportunity to further gain from the booming construction sector in the island. With the protectionist policies the government has placed on the local tile sector industries, RCL with its premium quality tiles and sanitary ware will have effortless penetration power in the local context. In addition this too will give RCL the momentum to shine in the global ceramic market.

YE 31 Mar	FY10	FY11	FY12E	FY13E	FY14E
Net Profit (LKR 'mn)	964.3	1,441.2	1,814.9	2,144.5	2,257.7
+/- YoY	86.2%	49.4%	25.9%	18.2%	5.3%
EPS (LKR)	8.7	13.0	16.4	19.4	20.4
+/- YoY	86.2%	49.4%	25.9%	18.2%	5.3%
P/E	13.0	8.7	6.9	5.8	5.5
DPS	1.3	2.5	5.0	5.0	5.0
DY (%)	1.1%	2.2%	4.4%	4.4%	4.4%
BVPS (LKR.)	35.1	45.6	57.0	71.3	86.7
PBV (X)	3.2	2.5	2.0	1.6	1.3
Cash per share	0.5	0.6	0.5	0.8	1.5
ROE (%)	24.8%	28.5%	28.8%	27.1%	23.5%



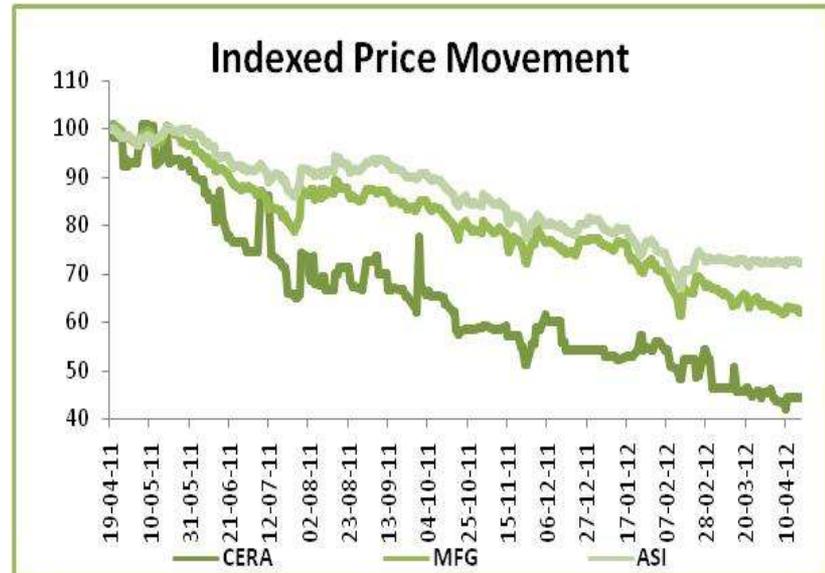
\*RCL forecast excludes the performance of newly acquired subsidiary of Asia Siyaka Commodities

# CERA (LKR:66.00)



- The Lanka Ceramics Ltd. group is the only company that has fully diversified operations in ceramics ranging from tiles to crockery to sanitary ware. It also controls about 80 percent of the supply of raw material. This supply is expected to last for at least 20 years.
- During FY10 the profits were boosted by capital gains of LKR160 mn on the sale of properties located at Boralesgamuwa. Hence excluding this the YoY growth in FY11 net profit compared to FY10 was 8.5%.
- The mining of ceramic minerals and retailing of ceramic and allied products, the two main operations of the Company, performed well during FY11 and the two divisions posted satisfactory growth in profitability.
- In December 2011 Lanka Ceramic Plc decided to close its retail division due to it being underperforming. Since the retail outlets division of the company was underperforming for a considerable period of time, it was resolved to gradually phase out and cease operations of this division.

YE 31 Mar	FY09	FY10	FY11
Net Profit (LKR 'mn)	133.3	392.8	255.0
+/- YoY		194.6%	-35.1%
EPS (LKR)	4.4	13.1	8.5
+/- YoY		194.6%	-35.1%
P/E	14.9	5.0	7.8
DPS	1.3	6.6	2.5
DY (%)	1.9%	10.0%	3.8%
BVPS (LKR.)	48.27	68.63	74.33
PBV (X)	1.4	1.0	0.9
Cash per share	1.6	6.4	9.3
ROE (%)	9.2%	19.1%	11.4%

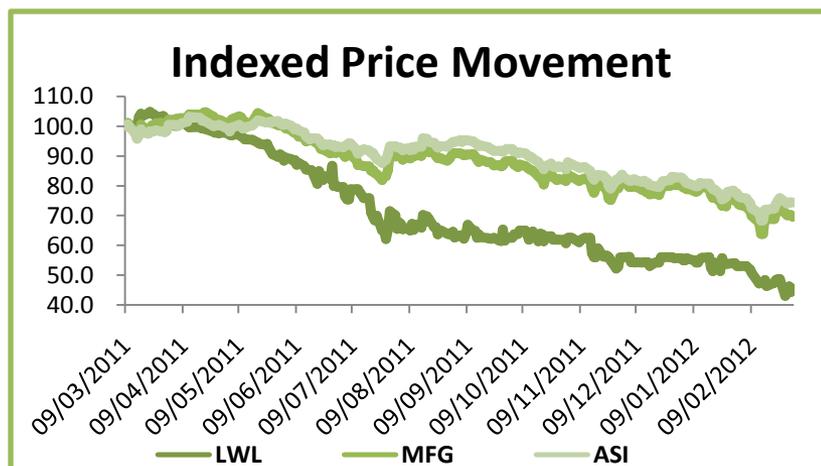


# LWL (LKR:72.00)



- Lanka Walltile is poised to grow in the current economic outlook backed by its presence in the construction sector. The hike in the per capita income backed by the credit growth in the island is going to strengthen the future earnings of the counter.
- The expected capacity expansion would shoulder the future revenue whilst the export oriented 'thin tiles' would gain additional income and add flavour to the international markets.
- The rebranding of the Lanka Walltile would uplift the image of the organization with a strong recognition among the local and international clients. Further, the growing franchise network would add presence to this newly developed brand across the island.
- Therefore, in the middle of rapid economic uptrend backed by the strong construction sector boom the company is poised to grow. The capacity increment together with the dismissal of the loss making counterpart (Balangoda Factory) would be reflected positively in the financials for Lanka Walltile. The Meepe factory with 7,500sqm as daily capacity expects to future sales volumes. With rigorous development in the construction sector, the counter is set to perform on an optimistic note in future.

YE 31 Mar	FY10	FY11	FY12E	FY13E	FY14E
Net Profit to equity holders (LKR mn)	477.9	484.5	490.1	528.1	568.0
+/- YoY	71.1%	1.4%	1.2%	7.7%	7.6%
EPS (LKR)	8.8	8.9	9.0	9.7	10.4
+/- YoY	71.1%	1.4%	1.2%	7.7%	7.6%
P/E	8.2	8.1	8.0	7.4	6.9
DPS	2.0	2.3	2.5	2.5	2.5
DY (%)	2.8%	3.2%	3.5%	3.5%	3.5%
BVPS (LKR.)	57.9	64.1	70.5	77.6	86.3
PBV (X)	1.2	1.1	1.0	0.9	0.8
Cash per share	3.4	5.1	1.8	2.7	1.7
ROE (%)	15.1%	13.8%	12.7%	12.5%	12.1%

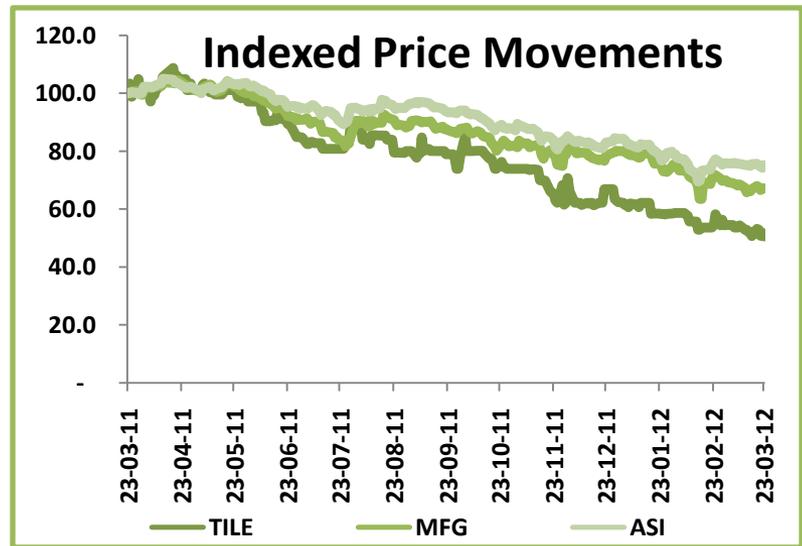


# TILE (LKR:61.50)



- Lanka Floortiles is planning to develop a broad five year strategy for which it increased the manufacturing volumes by 40% to circa 13,000 tiles per day in January 2012 at an estimated cost of LKR600 mn.
- An increase in manufacturing capacity will help to expand its market share and expand into the manufacture of glazed porcelain tiles in FY12.
- The strategy for FY12 hubs on amplifying the franchise operations further to perform direct sales, while maintaining a robust dealer and sub-dealer network.
- The distribution network will also be strengthened further and several harmonizing products (construction related items) will be added to product range to pick up the market share. Several direct marketing campaigns have been lined up in export markets such as Australia, New Zealand and Japan, while locally, is exploring options to capture and increased market share in less price sensitive segments.

YE 31 Mar	FY07	FY08	FY09	FY10	FY11
Net Profit (LKR 'mn)	273.0	313.0	282.3	379.1	511.9
+/- YoY		14.7%	-9.8%	34.3%	35.0%
EPS (LKR)	5.1	5.9	5.3	7.1	9.6
+/- YoY		14.7%	-9.8%	34.3%	35.0%
P/E	12.7	11.1	12.3	9.1	6.8
DPS	3.8	4.1	2.6	3.8	3.5
DY (%)	5.7%	6.3%	4.0%	5.7%	5.4%
BVPS (LKR.)	20.91	28.46	31.29	37.68	41.72
PBV (X)	3.1	2.3	2.1	1.7	1.6
Cash per share	4.7	6.6	4.1	13.4	14.3
ROE (%)	24.6%	20.7%	17.0%	19.0%	23.1%



\*TILE forecast has been incorporated to LWL

# FINANCIAL ANALYSIS



## RCL

Ratio Analysis	FY08	FY09	FY10	FY11	FY12E	FY13E	FY14E
<b><u>Profitability</u></b>							
Revenue Growth	33.9%	7.7%	19.0%	29.2%	21.2%	9.5%	5.0%
Gross Profit Margin	42.4%	43.9%	47.6%	46.2%	47.0%	47.5%	48.0%
Operating Profit Margin	28.6%	25.6%	31.0%	30.2%	31.0%	32.9%	32.9%
PBT Margin	18.5%	14.4%	22.5%	26.7%	27.4%	29.5%	29.6%
Net Profit Margin	17.6%	13.8%	21.7%	25.1%	26.0%	28.1%	28.2%
<b><u>Efficiency</u></b>							
Receivable Days	34.7	36.8	46.5	41.1	50.0	60.0	65.0
Inventory Days	194.0	260.5	237.2	162.7	120.0	115.0	120.0
Payable Days	56.0	65.9	69.6	86.1	75.0	50.0	45.0
Current Ratio	1.3	1.0	1.4	1.8	1.8	2.5	3.3
Acid Test Ratio	0.6	0.3	0.5	1.2	1.3	1.9	2.6
Interest Cover	2.8	2.3	3.6	8.5	8.5	9.7	9.9
Gearing(debt/equity)	96.7%	85.3%	47.1%	48.8%	42.4%	32.7%	26.3%
Gearing(debt/debt+equity)	49.2%	46.0%	32.0%	32.8%	29.8%	24.7%	20.8%
<b><u>Investor Ratios</u></b>							
ROE	23.0%	16.9%	24.8%	28.5%	28.8%	27.1%	23.5%
ROA	17.5%	15.5%	21.3%	20.5%	21.7%	22.3%	20.4%
Equity Multiplier	2.1	2.0	1.7	1.7	1.6	1.4	1.3
Asset Turnover	0.6	0.6	0.7	0.7	0.7	0.7	0.6

## LWL

Ratios	FY08	FY09	FY10	FY11	FY12E	FY13E	FY14E
<b><u>Profitability</u></b>							
Revenue Growth	18.2%	-0.3%	6.0%	16.9%	12.8%	13.8%	9.6%
Gross Profit Margins	23.3%	22.6%	24.6%	29.7%	24.0%	23.0%	23.0%
PBIT Margin	14.5%	13.5%	15.7%	20.0%	13.6%	12.8%	12.5%
PBT Margin	12.3%	9.8%	13.3%	14.9%	10.0%	9.5%	9.3%
PAT Margin	8.9%	6.4%	10.0%	11.7%	8.3%	7.9%	7.7%
Net Profit Margin	5.3%	4.1%	6.6%	5.7%	5.1%	4.9%	4.8%
<b><u>Efficiency</u></b>							
Inventory Days	92.8	126.3	113.9	112.6	120.0	130.0	132.0
Receivable Days	53.9	57.0	61.1	50.2	60.0	65.0	68.0
Payable Days	38.6	45.1	57.2	76.2	55.0	60.0	70.0
Current Ratio	2.0	1.6	1.9	1.6	1.8	1.9	1.8
Acid Test Ratio	0.9	0.6	0.9	0.8	0.7	0.8	0.7
Interest Cover	6.4	3.7	5.4	9.3	3.7	3.8	3.8
Gearing(debt/equity)	63.1%	81.1%	43.1%	52.9%	60.8%	57.5%	55.4%
Gearing(debt/debt+equity)	38.7%	44.8%	30.1%	34.6%	37.8%	36.5%	35.6%
<b><u>Investor Ratios</u></b>							
ROE	17.0%	11.9%	15.1%	13.8%	12.7%	12.5%	12.1%
ROA	15.9%	12.9%	14.0%	17.1%	12.5%	11.7%	11.7%
Equity Multiplier	2.9	3.0	2.6	2.8	2.7	2.8	2.7
Asset Turnover	1.1	1.0	0.9	0.9	0.9	0.9	0.9

\*RCL forecast excludes the performance of newly acquired subsidiary of Asia Siyaka Commodities

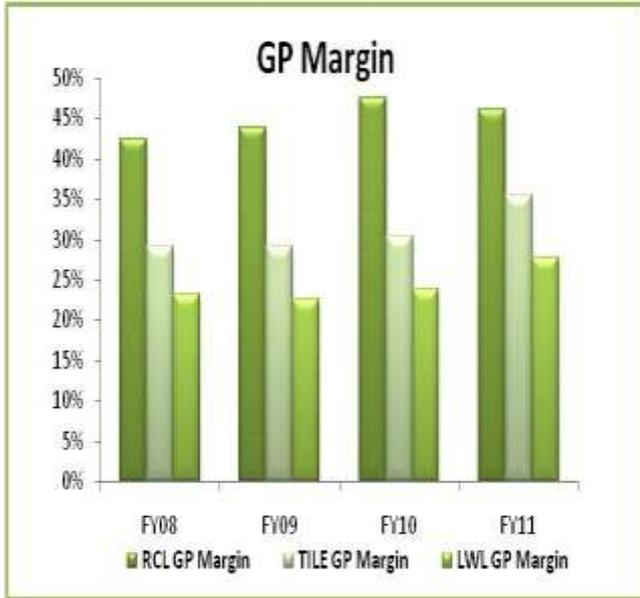
# REVENUE VS COST



During FY08 and FY09 in terms of total revenue, LWL was in a dominant position due to its robust export market. Nevertheless lost its dominance due to low volumes in the export market.

On the contrary, RCL's newly established bathware facility (August 2009) and high end domestic and corporate customer portfolio positively contributed to the revenue which surpassed the revenue of LWL in both FY10 and FY11.

# REVENUE VS COST



RCL's premium quality tiles and bathware fetched solid GP margins since FY08 when compared to both LWL and TILE.

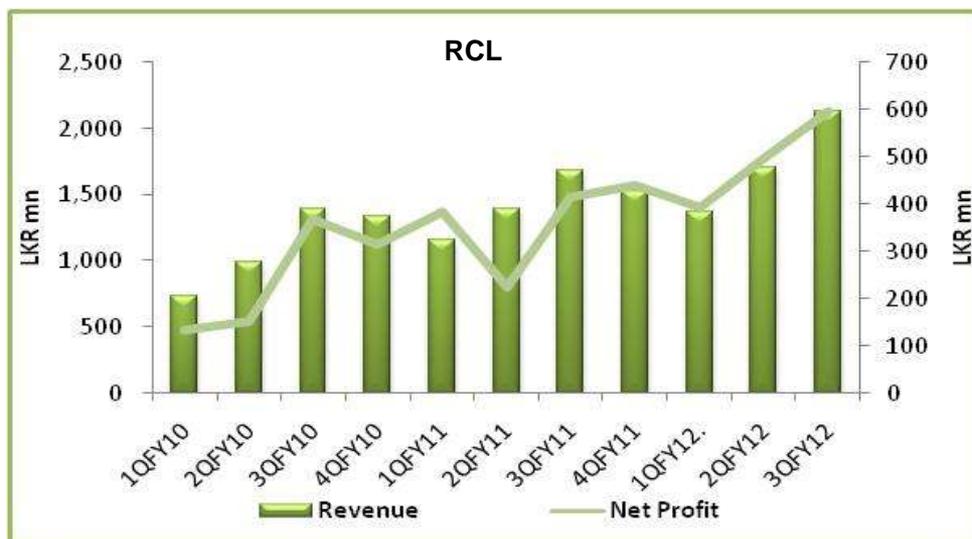
Both LWL and TILE possess lower NP margins compared to RCL. This is due to the fact that despite RCL having heavy operating expenses compared to LWL and TILE, the gross profits (backed by higher margins) of RCL are significant.

Moving forward, the labour force, branch and dealer network of RCL are superior to both LWL and TILE. Hence the expense margins of RCL are higher than LWL and TILE..

# QUATERLY ANALYSIS



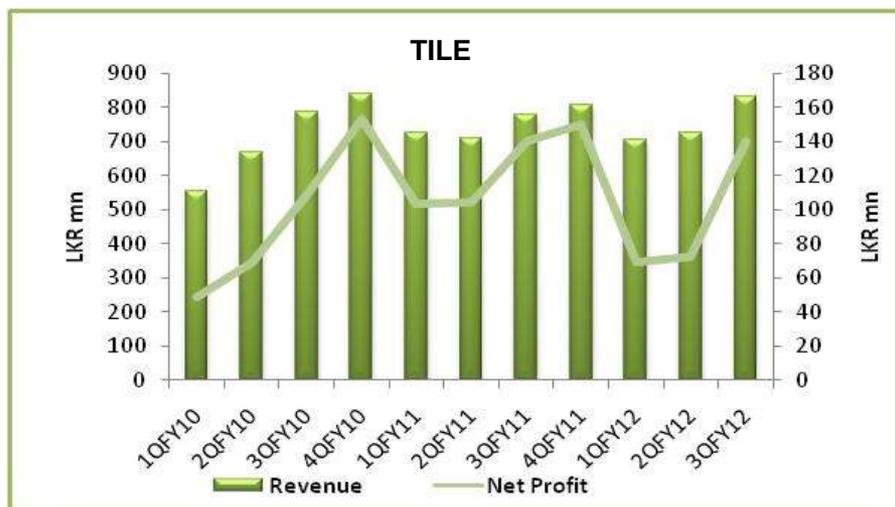
RCL	FY10				FY11				FY12		
(LKR mn)	1QFY10	2QFY10	3QFY10	4QFY10	1QFY11	2QFY11	3QFY11	4QFY11	1QFY12	2QFY12	3QFY12
Revenue	729.1	988.3	1,392.3	1,341.4	1,152.4	1,392.4	1,679.3	1,527.3	1,366.7	1,706.0	2,134.1
Cost of Sales	(387.1)	(532.4)	(717.7)	(695.2)	(636.2)	(751.9)	(893.0)	(813.7)	(774.7)	(868.6)	(1,105.0)
Gross Profit	<b>342.0</b>	<b>456.0</b>	<b>674.6</b>	<b>646.2</b>	<b>516.2</b>	<b>640.5</b>	<b>786.3</b>	<b>713.6</b>	<b>592.0</b>	<b>837.4</b>	<b>1,029.2</b>
Other Operating Income	108.7	10.3	22.2	15.5	182.9	24.1	(14.5)	21.8	122.3	42.2	(2.5)
Distributing Expenses	(130.3)	(134.9)	(131.6)	(141.4)	(178.7)	(269.3)	(166.7)	(90.7)	(176.3)	(217.2)	(224.0)
Administrative Expenses	(64.1)	(69.5)	(94.5)	(127.2)	(82.3)	(88.3)	(100.2)	(152.2)	(86.4)	(102.1)	(102.4)
Finance Expenses	(124.4)	(110.7)	(83.9)	(62.8)	(55.8)	(53.7)	(51.0)	(43.7)	(59.7)	(75.5)	(85.0)
Finance Income	0.6	0.3	0.3	0.3	0.2	0.2	0.2	0.1	0.1	0.1	0.2
Profit Before Tax	<b>132.4</b>	<b>151.6</b>	<b>387.1</b>	<b>330.6</b>	<b>382.5</b>	<b>253.4</b>	<b>454.1</b>	<b>448.9</b>	<b>392.1</b>	<b>484.8</b>	<b>615.5</b>
Associate Profit	-	-	-	-	-	-	-	-	-	17.0	(8.2)
Taxation	0.0	(0.2)	(20.8)	(16.3)	0.0	(29.3)	(41.2)	(9.2)	(0.7)	(5.9)	(11.6)
Net Profit	<b>132.4</b>	<b>151.4</b>	<b>366.3</b>	<b>314.2</b>	<b>382.5</b>	<b>224.0</b>	<b>412.9</b>	<b>439.7</b>	<b>391.5</b>	<b>495.9</b>	<b>595.7</b>



# QUATERLY ANALYSIS



TILE (LKR mn)	FY10				FY11				FY12		
	1QFY10	2QFY10	3QFY10	4QFY10	1QFY11	2QFY11	3QFY11	4QFY11	1QFY12	2QFY12	3QFY12
Revenue	554.9	670.7	787.1	838.5	724.9	709.3	780.5	805.9	705.6	724.7	830.86
Cost of Sales	(392.3)	(477.6)	(530.3)	(585.0)	(485.0)	(462.6)	(488.5)	(502.6)	(501.3)	(521.9)	(538.92)
Gross Profit	<b>162.5</b>	<b>193.0</b>	<b>256.8</b>	<b>253.6</b>	<b>240.0</b>	<b>246.7</b>	<b>292.0</b>	<b>303.3</b>	<b>204.3</b>	<b>202.7</b>	<b>291.9</b>
Other Operating Income	7.0	10.9	10.8	(16.2)	6.9	6.9	9.3	3.0	5.1	4.5	11.56
Distributing Expenses	(30.2)	(38.0)	(35.6)	(34.3)	(39.3)	(40.1)	(38.5)	(43.5)	(47.1)	(53.4)	(48.98)
Administrative Expenses	(48.4)	(50.0)	(52.5)	(48.6)	(57.3)	(57.2)	(56.4)	(55.5)	(52.9)	(52.1)	(66.50)
Operating Profit	<b>90.9</b>	<b>115.9</b>	<b>179.6</b>	<b>154.5</b>	<b>150.2</b>	<b>156.2</b>	<b>206.4</b>	<b>207.4</b>	<b>109.3</b>	<b>101.7</b>	<b>188.0</b>
Finance Expenses	(20.9)	(17.2)	(24.6)	20.3	(9.5)	0.3	(11.1)	10.3	(3.2)	(4.9)	(8.86)
Share of Associate Results	(0.9)	(1.4)	(5.4)	(1.0)	0.6	(7.2)	-	2.7	(11.1)	(3.7)	1.26
Profit Before Tax	<b>69.1</b>	<b>97.3</b>	<b>149.6</b>	<b>173.9</b>	<b>141.4</b>	<b>149.3</b>	<b>195.2</b>	<b>220.4</b>	<b>95.0</b>	<b>93.1</b>	<b>180.4</b>
Taxation	(20.2)	(28.3)	(41.5)	(20.6)	(37.8)	(45.2)	(54.7)	(70.7)	(25.7)	(20.3)	(39.97)
Net Profit	<b>48.9</b>	<b>69.0</b>	<b>108.1</b>	<b>153.2</b>	<b>103.6</b>	<b>104.1</b>	<b>140.5</b>	<b>149.7</b>	<b>69.3</b>	<b>72.8</b>	<b>140.5</b>



# QUATERLY ANALYSIS



LWL (LKR mn)	FY10				FY11				FY12		
	1QFY10	2QFY10	3QFY10	4QFY10	1QFY11	2QFY11	3QFY11	4QFY11	1QFY12	2QFY12	3QFY12
Turnover	1,363.3	2,092.3	2,214.6	2,262.7	1,964.1	2,152.5	2,327.8	2,292.3	2,161.8	2,435.5	2,615.8
COS	(1,064.9)	(1,689.6)	(1,615.1)	(1,678.7)	(1,541.6)	(1,575.6)	(1,635.1)	(1,563.9)	(1,799.0)	(1,908.2)	(1,967.8)
<b>Gross Profit</b>	<b>298.4</b>	<b>402.7</b>	<b>599.5</b>	<b>584.0</b>	<b>422.5</b>	<b>576.9</b>	<b>692.7</b>	<b>728.4</b>	<b>362.9</b>	<b>527.2</b>	<b>648.0</b>
Other Income	20.1	28.1	22.6	(19.1)	31.2	42.1	50.2	36.9	47.4	54.0	57.7
Distribution Cost	(75.1)	(89.3)	(91.7)	(59.4)	(102.7)	(96.9)	(95.1)	(169.5)	(109.4)	(131.3)	(133.5)
Admin Expenses	(92.5)	(101.5)	(104.7)	(117.9)	(137.7)	(113.4)	(124.9)	(46.9)	(143.8)	(150.8)	(143.2)
<b>Profit From Operating Activities</b>	<b>151.0</b>	<b>240.0</b>	<b>425.6</b>	<b>387.6</b>	<b>213.4</b>	<b>408.7</b>	<b>522.9</b>	<b>548.9</b>	<b>157.1</b>	<b>299.1</b>	<b>429.0</b>
Finance Income	0.5	0.6	1.5	11.7	0.7	1.3	1.1	0.9	0.7	0.3	0.3
Finance Cost	(73.1)	(57.7)	(58.9)	(41.2)	(38.2)	(42.1)	(48.8)	(49.9)	(38.6)	(49.0)	(71.4)
Share of Associate Profit	(0.9)	(1.4)	(3.6)	0.6	-	-	-	-	(11.1)	-	-
Release of negative goodwill	-	-	-	25.8	-	-	31.5	10.6	-	-	-
Compensation Paid	-	-	-	-	(192.1)	(19.2)	(4.6)	-	-	-	-
Loss on Disposal	-	-	-	-	-	(16.3)	-	(61.4)	-	-	-
<b>PBT</b>	<b>77.4</b>	<b>181.5</b>	<b>364.6</b>	<b>384.5</b>	<b>(16.3)</b>	<b>332.3</b>	<b>502.1</b>	<b>449.1</b>	<b>108.1</b>	<b>250.4</b>	<b>357.9</b>
Income Tax	(28.5)	(74.4)	(85.4)	(54.0)	(65.7)	(95.4)	(91.8)	(105.2)	(39.8)	(70.3)	(76.4)
<b>PAT</b>	<b>48.9</b>	<b>107.1</b>	<b>279.2</b>	<b>330.5</b>	<b>(82.0)</b>	<b>236.9</b>	<b>410.3</b>	<b>343.9</b>	<b>68.3</b>	<b>180.0</b>	<b>281.5</b>
Minority	(18.6)	(21.8)	(121.8)	(125.8)	(48.6)	(86.3)	(183.5)	(182.8)	(14.3)	(41.8)	(99.5)
<b>Profit to Equity Holders</b>	<b>30.4</b>	<b>85.3</b>	<b>157.5</b>	<b>204.7</b>	<b>(130.6)</b>	<b>150.6</b>	<b>226.8</b>	<b>161.1</b>	<b>54.0</b>	<b>138.2</b>	<b>182.0</b>



# RISKS

- × Cess on importation of certain categories of worked monumental or building stones such as tiles, granite, marble etc. were reduced from 30 per cent to 20 per cent. This may directly affect local tiles manufactures as cheaper imports from China would dominate the market. Severe price competition may arise squeezing the margins of the local industry.
- × Tile industry consumes large quantities of clay. Although there is an abundant supply of high quality ball and china clay in Sri Lanka, mining restrictions prevailing in the country act as a barrier in acquiring required quantities. Illicit clay mining in the rural districts is also taking place which has a negative impact on larger producers. Currently 95% of the raw materials are supplied locally. Stringent regulations on ball clay mining may in turn escalate raw material prices to increase the production cost.
- × Currently 35%-40% of the production cost is attributable towards the energy cost which acts as a critical factor for the industry whilst they consume over 1,170 metric tons LPG per month. It is estimated that the increase in cess for LP Gas by Rs. 13.12 per kilo effective from 1 September 2010 would push costs by over Rs. 15m per month for a heavy corporate consumer and impose additional burdens for some of the seriously struggling companies.
- × The price of LPG remained volatile during most of the year, fluctuating between a low of LKR99.8/kg and a high of LKR134.32/kg. During the 1<sup>st</sup> quarter of 2011, the price of LPG rose to an all time high of LKR139.0. Future volatilities may adversely affect the cost structures of the industry.
- × Severe competition that is created by foreign tile suppliers may erode future margins of the company. This in turn may have an adverse impact on the overall bottom line of the local tile businesses
- × Due to stringent rules on local ball clay mining, local tile manufacturer's last resort may be to import from countries such as India and China. Nevertheless the quality of the material and adverse exchange rate fluctuations may escalate the future costs, thereby negatively impacting on potential earnings.

# CONCLUSION



- The growth in demand for housing is a key indicator on the future growth of the tile sector along with the rate of construction approval. Land and property sector is on a positive spin coupled with high demand for tile related products.
- Further with the influx of Foreign Direct Investments together with circa 8.1% GDP growth prevalent in the country, the spending on construction related activities has seen a hike over the past two years. We expect this upturn momentum to pursue in future.
- In addition with the Sri Lankan tile manufacturers working at full capacity and hovering for expansion the tile industry is sited to develop whilst distributing the generated high income among the participants.
- Also the contemporary protectionism acts carried out in the industry the local manufactures have a competitive advantage against the foreign competitors. We consider that construction industry collectively with the tile sector acts as a leading indicator of economic growth in the country.
- Heavy tourist arrivals have made leisure an attractive investment venture. Hence with the upcoming hotel construction and expansions may positively affect the local tile segment.

# CONTACT DETAILS



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